RBC Global Asset Management


# 3 ways a Trump election could impact emerging markets

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"The winning party could present major changes to tariffs, trade relations and public diplomacy, disrupting investment decisions in emerging markets."

**U.S. election years typically cause volatility in the marketplace, but the U.S. stock market tends to perform well regardless of whether a Republican or Democrat takes office.**

Since 1950, US S&P stocks have averaged returns of 8.1% in election years, according to Bloomberg data. The same cannot be said for emerging markets. The winning party could present major changes to tariffs, trade relations and public diplomacy, disrupting investment decisions in emerging markets. We don't know the outcome of this year's election, but if there is a "red wave" of elections results and Republicans take control of the White House, Senate and House of Representatives, there could be major policy impacts. Here's a look at how a Donald Trump victory may impact emerging markets.

## 1. Trade and Foreign Relations

No matter who wins the U.S Presidential Election, it is highly likely that the aggressive trade policy against China will likely continue and have negative impacts across Asia. Whether it's a Democrat or Republican in office, we expect harsh trade tariffs on China. This stance against China is expected to impact the Foreign Exchange channel in Asia, in particular, given the open nature of most of those economies.

But if Donald Trump wins in November, stricter regulations and tariffs primarily aimed at China would likely result in a strong USD, negatively impacting the Chinese currency, but also likely the currencies of Korea, Taiwan and Vietnam.

Harsher tariffs on China could positively impact U.S. manufacturing but will raise the cost of goods sold domestically. In turn, China may be faced with a glut of goods that will then be dumped on other economies without the same level of tariffs as the US, reinforcing the disinflationary trend in many other economies including those of the emerging markets. Asian credits could benefit from a shift in manufacturing and investment focus. Countries such as Vietnam and India are already seeing the impact of this, and we have seen an uptick of Chinese companies investing in production in other EM countries.

Outside of Asia, Mexico, an emerging economy, may have the most to gain from harsher tariffs on China. Expect the U.S. to trade more closely with Mexico in place of China, particularly given the existence of the North America Free Trade Agreement (NAFTA), which is aimed at fostering trade relations between Mexico, U.S. and Canada. This will bring an increase to Mexican production and positively impact Mexican industry.

### 2. Fiscal Policy

No matter which political party takes the White House, we expect ongoing fiscal largesse. But if Trump wins, and the Republicans also control Congress, we expect him to cut taxes without offsetting cuts to spending. The American economy could grow more rapidly, inflation could pick up again and the Fed may need to move back to a more hawkish stance which could, in turn, could promote dollar strength.

When the US dollar strengthens, often it is at the expense of emerging market currencies and, if the move is prolonged or outsized, it increases pressure on EM central banks to stabilize their currencies which often means interest rate hikes (or at least less cuts).

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We expect Trump to also crack down on immigration which could lead to more job vacancies in America and increase the cost of labor, further challenging the disinflation narrative.

### 3. Security Measures

A Republican victory may also mean that America is expected to spend less on other countries and ramp up threats around possibly cutting ties with the North Atlantic Treaty Organization, NATO. This will result in more European countries spending more on security and defense and will lead to greater fiscal spending in Central and Eastern Europe.

If Trump does win, we expect him to push for a peace deal between Ukraine and Russia with the goal of ending the current conflict and the associated ongoing spending. If this does in fact happen, it will likely aid the disinflation narrative because of expectations that more commodities like oils and metals and agricultural goods like wheat from Russia and Ukraine will be available to boost global supplies, without a commensurate increase in demand. Some countries that traditionally benefit lower oil prices include Turkey as an importer, along with many of the Asian countries which are also traditionally importers.

We also expect the Republicans to adopt a harsher stance towards Iran. This would actually take more oil production off the market and add a marginal constraint to the supply of oil and act as a price support.

The consequences of policy shifts in the event of a Trump victory are a key concern for global investors. The potential further tightening of trade policy, loosening of fiscal policy and adjustments of security policy could have contradictory implications and markets will be looking to disentangle the implications for impact on asset prices and prospects for individual countries across emerging markets.

Author

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Anthony Kettle is Senior Portfolio Manager within the BlueBay Emerging Markets Team at RBC Global Asset Management. Anthony joined BlueBay in March 2006 and his primary portfolio management responsibilities include the EM long-short credit strategy, the EM Unconstrained Bond Fund and the suite of EM Corporate long only funds. Prior to joining BlueBay, he held a management position at National Australia Bank. Anthony holds a Bachelor of Commerce degree from the University of Melbourne, a Graduate Diploma in Applied Finance and Investment from the Australian Securities and Investments Commission, and is a CFA charterholder.

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