SkyView Investment Advisors:

Trump, Fiscal Policy, And the Yield Curve

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Trump Fiscal Policy

President Trump, working with a Republican House and Senate, should see fairly rapid progress for two major areas of his platform—tax reform and infrastructure spending. Tax reform will likely show a more immediate stimulus to the economy while the economic boost from infrastructure spending would not likely show up for some time.

Tax Reform – Timely Economic Boost

Trump's tax proposals would reduce the current seven tax brackets into three and lower the highest tax rate on individuals from 39.6% to 33%. Important for investors, his proposal would lower the tax rate on dividends and capital gains to 20%.

For corporations, the tax rate would come down from 35% to 15%. In return, most tax breaks for businesses would be eliminated. The Trump tax proposals would also introduce a one-time transaction tax of up to 10% on unrepatriated international income of U.S. companies, payable over 10 years.

While, in our opinion, it seems unlikely that final rates would decline fully to these levels, the chance for tax reform legislation seems very high. If made permanent, tax reform will likely provide a timely boost to consumer and corporate spending.

Infrastructure Spending – Lagging Economic Boost

Trump proposes to invest $1 trillion in infrastructure spending over a ten-year period. His proposal, in part, would look to leverage private investment. To do so, he would offer tax inducements and revenue sources such as tolls to private investors. Besides such projects, the new Trump administration will likely speed up approval of pipeline and energy export terminal construction to the benefit of the economy.

The proposed infrastructure spending, if passed by Congress will likely show its first economic impact in 2018. As important, a speedier regulatory process will create even further, positive economic impact.

What Do Both Programs Mean for Investors?

In our opinion, the risk to GDP growth rate forecasts will prove to be to the upside…to reflect the possibly of rate increases, investor should consider floating rate funds as one option.

Even before both tax reform and new infrastructure spending becomes enacted by Congress, financial markets began discounting their impact. For long-term credits-- notes and bonds-- interest rates increased and will likely continue that trend. Overall this means a more positive, upward sloping yield curve. The degree of that slope will, in part, depend on the rate and frequency the Federal Open Market Committee increases the Fed Funds rate.

Trump's fiscal spending plans may finally bring to reality increasing long rates. If so, the normalization of interest rates may finally begin. Our caution remains, however, since many economic observers mistakenly called for such an increase many times in the past. Therefore, the question remains whether this will prove to be another false call.

If interest rates continue to rise from their historic lows, we would still remain optimistic about continued economic growth. Surprisingly, in our opinion, the risk to GDP growth rate forecasts will prove to be to the upside despite the initial interest rate increases.
To reflect the possibility of rate increases, investors should consider floating rate funds that invest in bank loans as one option. For more information, please contact First Capital Advisory.