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What Trump Means for Bonds - Infrastructure

This report is one in a series examining the potential implications of a Trump administration on bond markets. Through the presidential campaign and since the election, President-elect Trump has highlighted policy areas on which his administration will focus. In this series, Ascent will focus on some of the proposed or discussed policies and examine their potential impacts on taxable and tax-exempt bond markets.

Policy:

President-elect Trump has pledged to make infrastructure investment one of the main policy focuses of his presidency. His most recent proposal would drive $1 trillion of infrastructure project investment.

Implications:

The ultimate impacts of any new infrastructure investment program will depend largely on what form the program takes. It appears most likely at this point that the administration will seek to boost infrastructure investment through the use of more indirect methods like tax credits or other corporate investment incentives. Other approaches that have been discussed range from a federal infrastructure bank to direct federal spending for project construction. If a plan is ultimately enacted, the final form could incorporate a wide variety of tools, including: direct federal spending, federal loan guarantees, matching funds for public or private investments, tax credits, or other structures. Ultimately, we expect the infrastructure investment concept to evolve over the coming months and we believe the costs on the federal level will ultimately be much smaller than the $1 trillion currently being discussed.

Impacts on Bonds:

- Since the election, bond markets have reacted strongly to the idea that there would be $500 billion to $1 trillion of new federal spending on infrastructure during a Trump presidency, which would significantly increase federal borrowing and could stoke inflationary pressures. Markets have been reacting to the assumption that Trump's plan would take a "direct investment" approach. Going forward, market reactions will likely be shaped by evolving shape of the plan's details.

- Tax law driven plans like tax credits will most directly benefit corporations in sectors related to construction and transportation, or to those industries targeted for investment. The size of such a plan and the projected impacts on federal tax revenues will help determine the negative effects on the federal budget, federal borrowing and negative impacts on bond market yields.
- Indirect plans, such as infrastructure banks, matching funds, or loan guarantees, could have a wide variety of impacts, depending on exactly how projects are selected on through what mechanisms they are executed. Construction and transportation sector companies again stand to benefit directly from increased business. State and local governments could also benefit to the extent that are able to participate.
- Direct federal spending would have the quickest and most direct impacts on employment, federal spending and the deficit. To the extent the incoming administration backs away from this approach, we could see bond markets react favorably to revised expectations of less direct borrowing, lower deficits and less potential inflationary pressure.

Ascent's Approach:

We do not believe that investors should change their long-term strategy based on political proposals. Only if a substantial increase in infrastructure investment become policy can investors then evaluate the risks and opportunities under the specific new programs. If increased federal spending drives yields higher, long-term buy-and-hold investors will benefit from rolling interest payments and maturing bond proceeds into new positions at higher yields. At the same time, more policy certainty will allow better informed fundamental analysis of the specific investment opportunities, rather than guessing on winners and losers based on this week's media chatter.

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