Reshuffling the Deck: Industry Impacts of a Trump White House

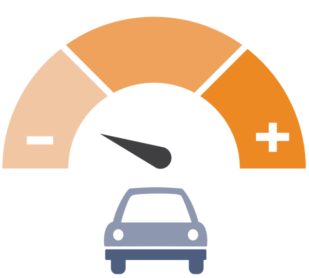
By Loomis Sayles Credit Research

How will President-elect Donald Trump's campaign rhetoric translate into policy once he's in office? It's too soon to know for certain, but markets are betting that a Trump White House will reshuffle the economic deck, making new winners and losers. Here, our credit research analysts offer their early take on how key sectors and industries might fare.

Healthcare & Hospitals

With Republicans controlling the White House and Congress, the Affordable Care Act (ACA) is a target and healthcare names face significant uncertainty. Hospitals could be at risk if insurance coverage is rolled back dramatically. On the flip side, managed care providers, medical device companies and other healthcare services would feel a more muted impact if the ACA were repealed.

We need greater clarity on proposals to repeal or replace the ACA, but we assume portions of the healthcare law will remain intact in the near to medium term. While future Medicaid expansion now appears to be off the table, benefits that have already been extended should remain in place. Though hospitals look vulnerable, we believe they will continue to display better metrics compared to pre-ACA levels.



Autos

Overall, risks surrounding future trade policies, especially as they relate to vehicles and parts sourced from Mexico and, to a lesser extent, China, are slightly negative for autos. The auto industry has been growing in Mexico since NAFTA was signed. On the positive side, if market conditions and consumer confidence remain favorable, any government-led economic stimulus may help sustain the currently high level of US light vehicle sales. Potential regulatory relief, particularly on fuel economy standards, could ease spending aimed at improving fuel economy and vehicle standards; however, severe investment cuts are unlikely since vehicle manufacturers and suppliers serve global markets.

Technology

Trump's preliminary positions on a one-time tax holiday for offshore cash, corporate tax reform and trade could be big for some companies in the tech sector. If there were a one-time repatriation holiday, companies with significant offshore cash would likely bring a portion back to the US to fund share buybacks, mergers and acquisitions, and potentially special dividends. Companies could slow new debt issuance at least temporarily, but leverage would increase on a net basis. Credit rating downgrades wouldn't necessarily follow, but agencies would likely re-evaluate their outlooks. With no concrete details available at this point, we'd view such a scenario as neutral to slightly negative for bond investors. More lasting corporate tax reform would likely have a similar effect, bringing a larger wave of cash back to the US to fund share buybacks. This could stem the recent trend of debt issuance to fund shareholder returns.

As for trade, a tariff on Chinese goods would lead to higher prices and lower margins for US tech firms since China touches so many component parts for tech manufacturing.

Retail

Consumer confidence has rebounded since the bitter election. Retail could conceivably benefit from lower healthcare costs, lower taxes and increases in disposable income at some point down the road.

On the downside, tighter immigration policies could put a damper on hiring and increase labor costs. And if trade relations with low-cost emerging market countries devolve, apparel and other product sourcing would be a pain point. Bringing apparel manufacturing back to the US would be a lengthy and extremely costly process. The strength of the dollar and consumer confidence will be critical variables to monitor.

Pharma

Trump has previously expressed his belief in universal healthcare, railed against drug pricing pressures and mentioned re-importation of drugs, but what actions he might take and the impact on pharmaceuticals remains to be seen. The fate of the ACA is unclear: lower coverage would be a headwind for pharma, but doing away with cost-cutting mechanisms like the Independent Payment Advisory Board would be welcome.

Corporate tax reform and earnings repatriation could be a positive for US pharma companies with significant offshore cash. As is expected in other industries, repatriated cash could be used in place of debt to fund shareholder-friendly actions and mergers and acquisitions, or it could be used to pay down some debt, although we do not expect any company to dramatically change its capital structure.

A shake-up at the Food and Drug Administration might remove logjams and lead to faster approvals. Generic drugs in particular stand to benefit because Congress wants to foster competition. Companies developing biosimilar products would also cheer faster approvals; however, this could hurt the biotech space.

US Banks

While there are many unknowns, a healthier macroeconomic environment and infrastructure initiatives should give way to rising interest rates, stronger commercial and industrial loan growth rates and, ultimately, higher net interest income.

Regulatory relief is widely expected but, perhaps counterintuitively, it could have a mixed credit impact. Reducing the power of the Consumer Financial Protection Bureau (CFPB) would lessen restrictions on many retail financial products and required reporting, which should boost revenues and lower expenses. While complete repeal of the Dodd-Frank Act seems unlikely, softer trading and investment restrictions could also feed revenues and reduce expenses. However, if the capital ratios and liquidity measures are cut significantly, or if the risk on bank balance sheets is allowed to increase, the results could be credit negative depending on how individual banks respond to the relaxed regulations.

Non-Bank Finance Companies

From a compliance and cost perspective, most lenders should benefit from a rollback of CFPB scrutiny. Student lenders, which have faced headwinds from CFPB scrutiny and the elimination of the Federal Family Education Loan Program (FFELP), may be one of the biggest winners. Trump has alluded to a greater role for private lenders and banks—or at least downsizing the Federal Direct lending programs—but costs associated with bringing back a program like FFELP mean change could be complicated. If private capital assumed a larger role in housing finance, it would be positive for mortgage insurers and possibly non-bank mortgage originators.

Cable, Telecommunications & Media

Republican impact on the Federal Communications Commission (FCC) could mean a net neutrality principle with far less teeth. In theory, this is good for the entire pay-TV ecosystem—cable especially, since the recent regulatory environment has heavily favored digital technology challengers over network operators on issues like shared network access, set-top box technology, fees and customer privacy rules. But any policy initiative that prolongs the status quo can be good for media too. One of the biggest fears—broadband rate regulation—has pretty much been put to rest, and infrastructure spending would likely boost demand for broadband and fiber networks.

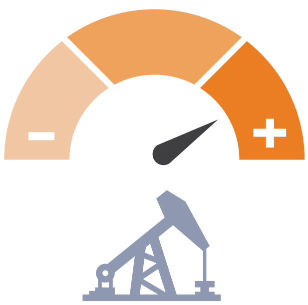
Broadly, a Republican-led Department of Justice and FCC should lower hurdles for mergers and acquisitions in the industry. This is positive for the industry overall, though the implications for individual companies and credits will be deal specific.

Defense

Republicans have wanted to increase defense spending above sequester levels for some time. Trump should be agreeable; he has discussed initiatives that could tack on an estimated $90 billion to the defense budget, including adding 90,000 troops to the Army and building 75 new ships. That said, increased defense spending typically takes a long time to show up in corporate earnings and estimates.

On the other hand, defense names could face risks if Trump decides to shake things up in Washington and change current contracting procedures. Another question is whether Trump's presidency will make America's allies spend more on defense, which could open up new opportunities for US and European companies.

Energy



A Trump White House and Republican legislature are generally assets to the energy sector at large, but pipeline operators and master limited partnerships (MLPs) could be the biggest winners. Stalled pipeline projects—including the controversial Keystone XL and Dakota Access pipelines—will likely gain approval with Trump in office. And Trump, like Obama, will likely leave fracking regulation to the states, and the potential for federal regulation looks very low. Refiners that do not have extensive retail operations also stand to benefit as the Environmental Protection Agency looks to alter the requirements and costs associated with its Renewable Fuel Standards mandate.

The outlook for taxes and regulation is also favorable. Under Trump, we don't foresee any movement on carbon taxation, a plus for refiners and other producers. Corporate tax reform is widely anticipated, but we doubt the legislation will threaten favored tax status for MLPs or the intangible drilling cost writeoffs that allow producers to defer taxes. The potentially lower corporate tax rate would help the refiners and integrated names the most given their high effective tax rate, while exploration and production companies typically do not pay taxes.

Sharply higher interest rates would pose a risk, particularly for MLPs, which rely heavily on access to capital markets at attractive rates to fund growth projects. Materially higher capital costs would reduce the number of profitable projects and darken the earnings outlook, likely depressing equity valuations in the near term. However, longer term, MLP management teams have a strong backlog of projects to draw on and a focus on improving their balance sheets, which we believe should support credit metrics.

Metals & Mining

Trump's proposal for increased infrastructure spending looks favorable for steel, copper and aluminum, but China will likely still drive the medium-term outlook for metals and mining.

Domestic steel producers with close ties to non-residential construction spending, including mini-mills and steel fabricators and manufacturers, should be well positioned to benefit from any infrastructure boom. Trump is also likely to advance comprehensive trade reform and support existing efforts to stop China from circumventing tariffs.

For the coal industry, it remains to be seen whether Trump can translate lofty promises into reality. Timing and how utilities change their investment plans will be key, but some damage may have already been done in this space. Persistently low natural gas prices have made coal plants uneconomical, so absent a significant rally in gas prices, we would not anticipate a substantial increase in coal demand. Also, state-specific clean energy standards have propelled a move away from coal that is unlikely to change under a new administration.

Capital Goods, Heavy Trucks & Transportation

Though equity markets rewarded capital goods names, particularly construction-related companies, following the election, there is speculation as to how Trump's proposed infrastructure plan will play out. Tax credits to private enterprises (as opposed to direct federal government spending) seem likely. Taxes from repatriated cash could also be used to fund significant infrastructure projects, which should provide a tailwind for revenues in the capital goods space; however, we are unlikely to see material revenue benefits until mid-2018 at the earliest.

At a more macro level, if Trump's plans bolster inflation and growth rates without triggering a sharp rise in interest rates, it would generally be a positive for the capital goods, trucking and transportation sectors.

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