Research Brief

Hancock Agricultural Investment Group®
A Manulife Asset Management Company

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Donald Trump's Election and Its Impact on the Global Agricultural Markets

Donald Trump was elected president and the Republican Party took control of both the Senate and the House of Representatives on November 8, 2016. The election results feel very similar to Brexit in terms of polls underestimating how far voters were willing to go to express their frustration and anger. With a full sweep, Trump may face fewer obstacles in pushing through his agenda. As with any candidate, it is difficult to parse out what a candidate says they will do versus what they will try to implement. This election is no different, but nevertheless, a high degree of policy uncertainty exists. The markets do not like uncertainty- as we saw in the initial Asian and European market responses to Trump's victory.

Trump's election is creating uncertainty in the agricultural market too, both domestically and internationally. Assuming Trump follows through on his campaign rhetoric, five major issues would cause the agricultural market particular concern, including:

- Trade policy
- Immigration policy
- Fed reaction to Trump's election
- Infrastructure policy
- Biofuels policy

Trade Policy

During the campaign, Trump consistently stated that the NAFTA deal was detrimental to the US and that he would attempt to renegotiate it. He also said that we were at a disadvantage on trade with China and Mexico and that he would consider imposing tariffs on goods imported from these countries. He also said that he opposes the Trans-Pacific Partnership agreement.

If these positions become policy, we anticipate a negative impact on the US agricultural markets across the board. Exports are a very large portion of US agricultural demand; in some commodities, exports account for more than 50% of total demand. Any policy that restricts US agricultural exports is likely to have a negative impact on total demand for US agriculture and push commodity prices lower. That the new administration views China and Mexico as the main culprits in regards to trade could be even more damaging. They are the largest and 3rd largest markets for US exports and account for approximately 30% of US agricultural trade demand.

A repeal or renegotiation of NAFTA and get tough approach on trade with China and Mexico (i.e. impose tariffs) would reduce US competitiveness in these markets, potentially lead to trade wars, reduce total demand for US commodities and lead to lower prices as stocks-to-use ratios would increase.

Immigration Policy

Trump said he wants to curb legal and illegal immigration, especially from Mexico, to create more job opportunities for US citizens. Historically, many of the typically lower paying jobs filled by immigrants from Mexico have been passed over by US citizens.

A stricter immigration policy is unlikely to have a significant impact on labor costs for farming industries which are more mechanized, such as row crops and tree nuts. On the other hand, for more intensive labor crops such as apples and wine grapes, a decrease in immigrants could reduce the size of the labor pool, increase competition for farm labor, and boost costs.

Fed Reaction to Trump's Election

We expect that the Fed will continue to be cautious on interest rate decisions going forward. On the one hand, Trump's economic policies are likely to be inflationary and could lead the Fed to hike interest rates throughout 2017. In this case, the likely result of a Fed rate hike will be that the US currency will appreciate against the currencies of competitive agricultural markets in the near and medium term. On the other hand, there is some concern that Trump's economic policies could potentially lead to another recession and the Fed will have to choose whether to curb inflation or promote economic growth with its monetary policy.

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The net result of an appreciating USD is likely to cause US exports of agricultural commodities to become more expensive and less competitive in the international markets. This lack of competitiveness in international markets, combined with the potential ramifications of variations in trade policy, will likely dampen the potential for US agricultural commodity prices and lead to higher stocks and lower prices going forward.

Infrastructure Policy

Trump also has proposed a massive investment in U.S. infrastructure, which he argues will lead to domestic job creation and improve, among other things, businesses ability to get goods to market more efficiently. We agree that infrastructure improvements are needed and would provide a strong boost to the agricultural industry. However, as currently structured and with proposed cuts to corporate and personal income taxes, infrastructure improvements will substantially increase the national debt, perhaps to unsustainable levels.

Biofuels Policy

One of the main drivers behind the agricultural commodity and land price boom of 2006-13 was the growth of the ethanol and biodiesel industries. Corn ethanol started to ramp up production in 2006 and by 2010, ethanol accounted for around 33% of domestic corn demand (today it is almost 40%). The farm community fears that Trump's dismissal of climate change might lead to a repeal of the ethanol subsidy/mandate provided by the RFS-2. If this happened, it would eliminate a major portion of corn demand and substantially reduce corn prices. Factor in potential trade policy changes and an appreciating USD and this could be catastrophic to the corn industry.

We think that political reality will temper any policy changes. Ohio, Indiana, Michigan, Wisconsin and Iowa helped push Trump over the line. All voted for Obama in 2012 and also have strong farm lobbies that will fight changes and likely hold back future support if Trump attempts to repeal RFS-2.

Conclusion

Overall, the lack of clarity around a Trump administration's policies and priorities means that uncertainty is the reality in the agricultural markets for the foreseeable future. Trump's trade policy and inflationary economic policy initiatives, if they occur, would have the most negative impacts on the agricultural markets. Aside from the manual-labor intensive sectors of the agricultural economy, the ongoing transition to a more mechanized and technology-driven production model means Trump's possible immigration policies are unlikely to have a huge impact. Infrastructure improvements would provide a boost to US agricultural markets and the economy overall, but the bill must be paid. Rhetoric aside, we expect biofuels policy to remain unchanged. We expect the net impact to be lower exports overall leading to higher stocks and lower prices in the short term, assuming trade policy initiatives are enacted. All in all, at this point, this is all conjecture until the fog clears and we can actually see what is on the ground.

Policies Impacting Ag	Net Result	Industries Most Impacted
Trade	Reduces Trade as trade relations with Mexico and China deteriorate; net positive for markets outside US	All industries
Immigration	No change for mechanized industries; industries requiring intensive labor experience intense competition and higher wages	Fruits in particular
Inflationary Economic Policy/ FED Reaction	Fed raises interest rates decreasing US competitiveness in international trade; net positive for markets outside US	All industries, but especially row crops where more international competition
Infrastructure	Positive as efficiency of moving goods to domestic and international markets improves; question is how do we pay for it	All industries
Biofuels	No Change	Row crops, particularly corn and soybeans

Source: HAIG Research