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DON'T COUNT ON IT

With rebuilding from recent hurricanes, is Trump's infrastructure boom now in play?

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ASK TYLER

Some investors may believe that natural disasters lead to increased economic growth. In the short run, this may appear to be the case. For example, American manufacturing expanded last month at the fastest pace in 13 years, in part due to the effects of Hurricane Harvey and Irma.

But fortunately we have the late French economist, Frédéric Bastiat, to set enquiring minds straight: destruction does not benefit the economy. In his "parable of the broken window", a man's careless son breaks a window pane. A crowd gathers and begins to contemplate the damage. They optimistically conclude that the boy has actually performed a community service.

Their logic? His father will have to pay someone to replace the window. That individual will spend the income on something else, multiply to another and so on. Voilà! The local economy is stimulated.

Bastiat, however, gently nudges us to consider "that which is seen and that which is not seen." What is less evident is that the father's income is reduced and used to fund a maintenance cost (simply replacing something that has already been purchased). What's more, the father could have spent the money on other goods or services. Ultimately the crowd was wrong — overall economic growth has actually been reduced.

Looking at the wider infrastructure thrust from the Trump administration, the fog is still thick. But some of it is lifting.

It is now clear that there will be significantly less than the $1 trillion of new investment promised by the Trump campaign. Elaine Chow, Trump's Transport Secretary, has repeated several times that the federal government accounts for only 16% of US infrastructure spending — that means less than US$200bn of federal money.

The rest is up to state governments. Where they will raise the money seems not to have been a consideration, except floating the idea of more public-private partnerships. In any case, there is no urgency to any of this. Even if the $1 trillion infrastructure promise could be financed, it was meant to be spread over ten years.

INVESTMENT IMPLICATIONS

Overall, Trump's infrastructure spending will have far less impact on the economy than originally envisioned by markets. The most encouraging development is the prospect for reduced regulation. Treasury Secretary, Steve Mnuchin, and Commerce Secretary, Wilbur Ross, are clearly determined to deregulate wherever they can. Even if the Congressional Democrats block specific changes (like Dodd-Frank), the administration has room to weaken regulations simply by re-interpreting existing laws. As such, Trump's sectoral impact will be substantial. From that perspective, US policy should support financials and be negative for infrastructure companies and energy (as prices should stay soft while supply continues to ratchet up).