Will Trump's Years Be Good for Gold?

Martin Hutchinson

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The price of gold shot up on Election Night, as it became clear that Donald Trump would be the next President of the United States. It has since sunk by more than $100 per ounce.

Two sides of the same coin man

Part of the reasoning for the decline is that President Trump may raise interest rates, cause a global depression through tariffs or govern as a Reaganite, boosting the stock market – all bad for gold.

Conversely, the reasoning for gold bulls is that Trump may blow out the U.S. federal budget, print money to fund it, thereby causing inflation or cause a massive market crash that destroys confidence – all good for gold. So, which tendency will win?

Views from The Donald

Trump himself has at different points in the campaign made promises that point both ways. For the Trump-is-a-second-Reagan theory, there is his promise to scrap much of the environmental and other regulations.

On monetary policy itself, Trump has suggested that the zero-rates policy pursued since 2008 has been very bad for U.S. growth and for savers. He has even expressed some guarded enthusiasm for the return of a Gold Standard.

However, it is highly unlikely that a Trump administration will go back to the Gold Standard. More likely, it will pay lip service to a Gold Standard and, through Fed appointments pursue a monetary policy that mimics a Gold Standard without actually adopting one – Paul Volcker 2.0, as it were.

In that case, there would be no special market demand for gold, because it would not be used in the world's currencies.

Instead, with money tight, inflation quiescent and productivity in the real economy soaring, gold would follow the trajectory it took in Reagan's 1980s — from a peak of $850 per ounce in January 1980 to around $410 at the end of 1988.

In today's world, that might see the gold price end President Trump's tenure at around $700 per ounce.

Tariff wars and gold

One other possibility to develop during Trump's Presidency that might also be bearish for gold is a tariff war.

At least in principle, if Trump adopted an aggressive tariff policy that decimated world trade and output, that should be bearish for gold.

Nevertheless, the history is a little unclear here. The Smoot-Hawley Tariff of 1930 was certainly bad for world trade, the volume of which declined by 65% from its 1929 level.

However, it was not all that bad for gold. The gold price rose from $20.71 to $35 per ounce between 1929 and 1934, as country after country went off the Gold Standard to try and boost their exports and President Roosevelt manipulated the gold market in his pajamas.

Thus, if a world trade depression causes governments to pursue aggressively expansionary monetary policies, even if the United States under a Trump administration does not follow suit, the price of gold may strengthen rather than weaken.

Infrastructure spending boosts gold

There are several Trump policy positions that, while bad for the U.S. economy, would be very good for gold. For a start, he wants to spend $1 trillion on infrastructure, cut taxes especially for corporations, and rebuild military spending.

Since the U.S. budget is already in deficit to the tune of over $500 billion per annum, this will make the deficit worse, even if Trump's policies produce higher growth, probably putting it above $1 trillion even in a period of relatively full employment.

Needless to say, any kind of recession, more than likely because of the monetary excesses of the last eight years, would rapidly push the U.S. budget deficit above $2 trillion, more than 10% of GDP.

Stock market crash and gold

A second possibility that might boost gold would be a massive market crash that destroyed confidence in the U.S. economic system. That would cause a “flight to safety” that would increase demand for gold from among the world’s investors.

Such a market crash would very possibly not be Trump’s fault. A major downturn is likely because of all the market distortions of the past eight years of funny money. It would however be worsened if Trump turned to true protectionism.

The Fed reading Trump’s lips

The effect of such policies on the gold price depends on how the Fed treats the budget deficit that would result from either Trump’s spending or a recession.

If Trump really means what he says about tighter money, and is prepared to accept a recession and much higher interest rates, the Fed will avoid monetizing the debt. In that case, the gold price would decline.

It is much more likely, however, that Trump’s commitment to higher rates is only skin-deep and would not survive real economic pain.

In that case, the Fed will monetize the deficits and we will set out on a path to hyperinflation. Needless to say, that would be a huge boost for gold, certainly in money terms and probably even in real inflation-adjusted terms.

Which path is chosen, and hence the future for gold, depends on which of Trump’s beliefs is stronger: the expansionary big-spending one or the sound-money one.

If Trump were to follow orthodox Republican policies, he ought to favor tighter money. If Trump follows his own history as a real estate entrepreneur, he might favor looser money.

The Goldman man at Treasury and the gold price

Until this week, this question was impossible to answer, and hence the likely path of gold prices could not be determined.

However, the President-elect has now chosen a Treasury Secretary, and all has become clear. He had the choice of two very capable hard-money, fiscal-restraint candidates, both of whom appear to have been considered: John B. Allison IV, the former CEO of BB&T Bank and President of the Cato Institute and Jeb Hensarling, the Chairman of the House Financial Services Committee.

Both men, from their published views and track record, would have been admirable proponents of sound money, much higher interest rates and fiscal rectitude, possibly even considering a Gold Standard.

Both men would have adorned the office of Treasury Secretary. Under either man, the prospects for the gold price would have been poor and my mining shares would have been rubbish.

However, Trump has not chosen either man. Instead, he has selected his campaign finance chairman Steven Mnuchin.

Hillary’s man?

Mnuchin has the — unfortunately not quite unique — distinction of having been connected with both Goldman Sachs and Soros Fund Management.

Mnuchin, in other words, is precisely the type of Treasury Secretary we might have expected from Hillary Clinton. In that regard, the entire two-year effort of the 2016 election campaign has been futile.

With Mnuchin as Treasury Secretary, expect the following:

1. The rich will be allowed to keep their grossly unfair and corrupt charitable tax deduction.
2. Corporations are going to gain even more tax loopholes.
3. Meanwhile, a fig-leaf of fiscal responsibility will be imposed at the expense of the middle class’s home mortgage tax deduction.

However, there is one benefit: The prospects for the gold price with Mnuchin as Treasury secretary are exceptionally bright.