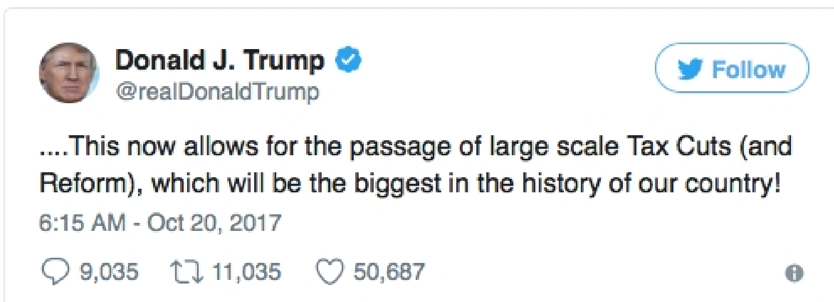
Trump Trade: How to Trade a Potential Tax Cut

Big things are just beginning to happen in the nation's capitol.

We've already talked a lot about how to trade defense spending bills, infrastructure, and even how to trade the gun stocks. Now, though, we have an opportunity to trade potential tax cuts.



According to the White House:

> *"This resolution creates a pathway to unleash the potential of the American economy through tax reform and tax cuts, simplifying the overcomplicated tax code, providing financial relief for families across the country, and making American businesses globally competitive."*

Just the other day, the Senate passed a $4 trillion budget that now lays the groundwork for promised tax legislation. That new plan provides for $1.5 trillion over the next decade in debt-financed tax cuts. And Republicans believe they can push it through by year-end.

In fact, according to PBS:

> *"The budget plan passed on a near party-line vote late Thursday includes rules that will allow Republicans to pass tax legislation through the Senate without Democratic votes and without fear of a Democratic filibuster."*

There's now hope the corporate tax rate could be cut from 36% to 20%, reduce taxes for most individuals, and repeal the inheritance tax on multi-million dollar estates.

Better yet, the standard deduction would be doubled to $12,000 for individuals and $24,000 for families. The number of tax brackets could also fall from seven to three. And the child tax credit would be increased. The Administration hopes this will be a big boost to the middle class, and spark economic growth and jobs.

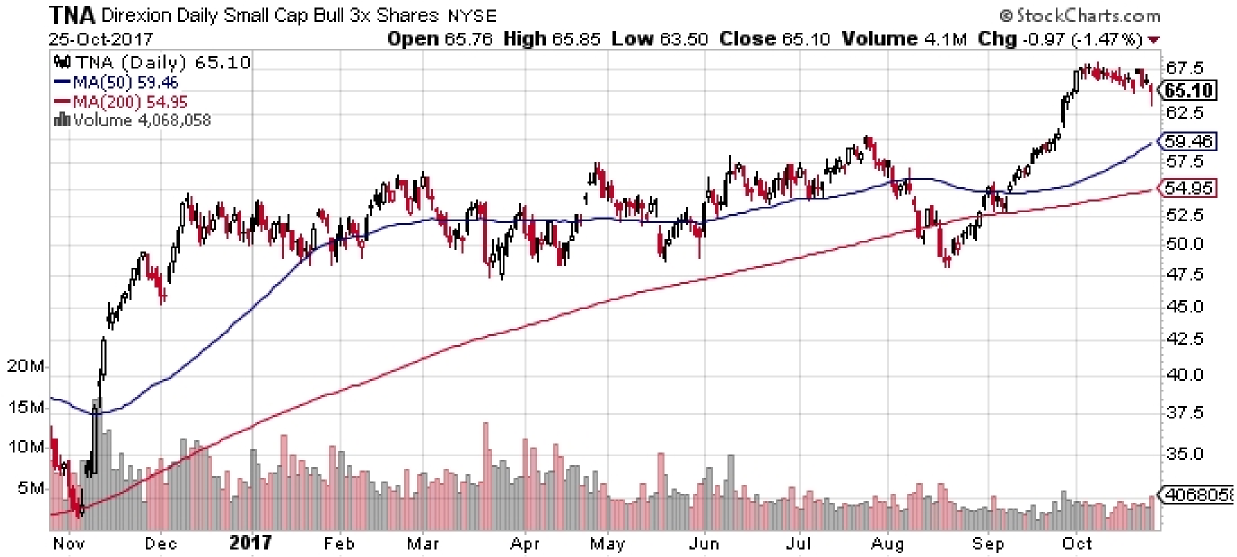
We could also see a one-time repatriation tax on untaxed overseas profits.

In other words, assets that are currently held overseas will be taxed as if that money was brought home. While a tax rate hasn't been announced, it's rumored to be 10%. Right now, some of the biggest companies in the world – Apple, Microsoft, Alphabet, Cisco and Oracle hold 88% of their money overseas. Other companies like Merck, Pfizer, Johnson & Johnson, Gilead, and Ford sit on about $25 billion.

Such news is why the Dow Jones Industrials is now hitting an all-time high of 23,329, a number that may just surpass 25,000 in weeks.

One of the biggest beneficiaries would be the Russell 2000 and small-cap stocks, especially with the possibility of a corporate tax reduction to 20%. At the moment, small cap companies see a tax rate of 32%, as compared to 26% for S&P 500 companies because they have less exposure to international tax havens. However, should Congress be successful in reducing the corporate tax rate to 20%, small cap stocks could move higher.

One way to trade small caps with an ETF is with the Direxion Daily Small Cap Bull 3x (TNA).



Or, look to buy some of the higher taxed companies.

About 99% of Southwest Airlines (LUV) flights are domestic. It also sees a monster tax rate of 38% at the moment. Depending on the outcome of the latest tax plan, reform could add millions of dollars to the company's bottom line every year. Plus, a boost to the middle class could mean a boost to travel plans and higher revenue to the airline, as well.

Traders are also picking up the LUV December 15, 2017 57.50 calls.

Home Depot (HD) could be a big beneficiary as well.

Right now, 87% of its stores are in the United States, paying a tax rate of 36.3%. In short, it gets hosed on taxes. But if the rate were to be dropped to 20% let's say, shares of the home improvement retailer could see millions added to its bottom line.

Traders have been buying the HD December 15, 2017 170 calls.

High tax paying sectors could also see upside.

Last year, some of the highest taxpayers were telecom (33.4%). AT&T (T), Verizon (VZ) and the iShares U.S. Telecom ETF (IYZ) could rise with a tax cut.

Now, all we can do is wait.

But smart investors may want to think about buying the above-mentioned stocks and sectors.