U.S. Elections: Recalculating

November 9, 2016

"*It's the economy, stupid*" – Bill Clinton in his 1992 presidential campaign

WHAT JUST HAPPENED?

"It's the economy, stupid" was a phrase coined by strategist James Carville for Bill Clinton's 1992 presidential campaign that became a de facto slogan for Clinton.

Fast forward a few years and apparently Hillary Clinton didn't get the memo.

Donald Trump did get it and he appealed to many Americans that see the U.S. economic growth as anemic and Mr. Trump as a strong proponent of change. Potential policies include spending aimed to stimulate the economy, reduced taxes particularly for families that make less than USD $50,000 a year, reduced corporate taxes, and a promise to protect American jobs as a priority (even if he needs to renegotiate NAFTA – which we sense will be a more arduous job than what Mr. Trump suggested in the campaign). Many Americans clearly view these issues as important.

We at QAM are not political analysts or sociologists. More expert opinions are going to analyze in detail how this event will shape up the political landscape of the United States and the world.

Independently of political and social views, QAM's mandate as portfolio manager and advisor is to make sense of topics we believe affect markets and to help clients position portfolios accordingly and achieve their long-term financial objectives.

Initially, when there is a surprise that catches investors off-guard, market momentum is negative. Emotions play out - as is to be expected. The Trump victory was unexpected by many because the polls were wrong - this outcome was not broadly anticipated. Futures markets initially pointed to a 5% fall in U.S. equities and ten-year U.S. Treasury yields fell from 1.90% to 1.72%.

After this initial reaction, global financial markets shook off their early worries about a Donald Trump presidency and fully reversed this move by early Wednesday.

WHAT HAPPENS NEXT?

Of the thousands of comments and tweets and opinions this morning from around the world about the outcome of the American election, one commentary that sticks out is that Trump's victory speech was better and more gracious than expected. Maybe in the end he is already a politician (mind you without any public service experience) and plays with the political game after all.

As the saying goes: “it’s one thing to be the drunk at the bar, a completely different story is to be the owner”.

Markets don’t like uncertainty and Trump provides uncertainty. Particularly on the risk for the rest of the world in terms of a move towards more protectionism and the fact that he has proven to be sort of a loose cannon in terms of foreign policy. But on the other hand it may turn out to be that this businessman will be more market friendly than not.

In our August/September 2016 QAM Perspectives we said that studies show that the stock market gains have been higher on average during years in which a Republican candidate wins the election and relatively healthy when the White House and Congress is controlled by the same party. The fact that Mr. Trump will be able to be Mr. Nice Guy because he has a majority in the House and Senate reduces uncertainty particularly after years of political gridlock in Washington.

Investors simply do not know what president-elect Trump will do once he takes office and what implications his victory has for global trade and global economies. We, at QAM, can’t claim to be any different and in no way can get to all the relevant information regarding the election fallout.

What Mr. Trump is going to do regarding NAFTA is of particular concern for Canadians. He was consistently pro-tariff and anti-trade as a candidate but was never clear on the specifics.

In our August/September 2016 QAM Perspectives we said that the election rigmarole was almost over and portfolios should remain depoliticized and focused on their long-term objectives. Now that the new president-elect is known, one uncertainty is removed but many still remain.

In the near term, policy uncertainty will impact risk assets, including U.S. equities, high-yield corporate bonds, and even investment-grade corporate bonds. Perhaps most intensely impacted will be emerging market assets.

This political outcome emphasizes the need for careful asset class and stock selection. Successful Managers, like the ones QAM selects, will be the greatest beneficiaries.

Berkshire Hathaway’s Charlie Munger advised: “It’s waiting that helps you as an investor, and a lot of people just can’t stand to wait.”

The QAM team will closely monitor political and economic developments over the coming weeks and months. Portfolios should remain depoliticized and focused on their long-term objectives.