

Perennial Perspective

“The minor fall and the major lift”?

Brian Thomas

I thought it was appropriate to use part of a famous lyric from Leonard Cohen (who sadly passed away earlier this month) to title this article. And indeed share markets did have a minor fall on the US election result based on increased risk followed by a major lift the very next day as investors realised that the massive spending program and tax cuts proposed by President elect Trump could be positive for share markets.

Let's cut to the chase – it is estimated by Goldman Sachs that the proposed spending will increase US Government debt by an astronomical 25% of Gross Domestic Product (GDP) if Trump proceeds with his “positions”(this is how he describes his sometimes vague policies). For this to work in the longer term he needs growth to pick up dramatically to help manage the future debt burden. Having said this, timing is everything and there is a positive view that the US economy needs some Government spending (the world has relied on central banks to do all the heavy lifting) and a “sensible” Trump outcome could be very good for the US and the World. On the subject of trade hopefully Trump's words/proposed policies were more about saying anything to get elected rather than turning the US away from the World.

To my mind the words “watch this space” have never been more important.

If there is one thing that we learnt from Brexit, it's that you should separate the **socio-political** issues from the **market** issues. In regards to Brexit, for instance it's remarkable that, despite the negative implications, UK Stocks (the FTSE100) have this year (in local currency at least) outperformed both the ASX300 and S&P500 price indices, mainly due to Gold companies and the exporters benefitting from a collapsed sterling. And even the UK economy is doing much better than expected. Part of the reason is that the actual EU exit will play out over a longer timeframe and the final results are still unclear.

Trump's proposed policies

Potentially Pro-growth policies:

- **Tax cuts** - cutting corporate rate from 35% to 17%
- good for business investment, employment and consumption
- **Fiscal stimulus** - US\$1 trillion spend over 5 years
- focus on infrastructure, transportation, water, electricity and telecommunications

Policies could be enacted given Republican control of both the House and Senate.

Potentially negative policies:

- **Trade restrictions** - import tariffs, Mexican wall, immigration controls

Combined with an already strengthening economy this could lead to inflationary pressures, rising bond yields and the strengthening of the US Dollar.

This will could possible mean the end of yield trade, positive for "Value" managers.

For investors the initial outcomes are as follows and assumes Trump can get things moving although I will stress my *"watch this space"* comment as there will be incredible volatility as the World watches Trump's every move.

Potential Outcome	Investment Issue	Australian Stock Examples
Inflationary - Interest rate rise	Typically bad for long duration bonds although market has moved quickly to price this in. Good for banks and insurance companies	QBE, Banks
Infrastructure spend	Can boost economy as well as builders and commodities etc.	Macquarie (infrastructure financing), Lend Lease
Less investment bank regulation (Dodd-Frank repeal)	Good for Banks	Macquarie etc.
More buoyant consumer	The US consumer drives their economy	Newscorp, Aristocrat
Commodity prices continue to rise	Good for producers	BHP, Rio
Trump fails and starts a tariff war for example	All bets are off!	Bonds, Protected strategies

Trump week was interesting



Source: IRESS, Perennial Value

Post Trump - Inflation is the new black

Deflation Winners	Inflation Winners
Monetarism	Keynesianism
Globalization	Protectionism
Surpluses	Deficits
Wall Street	Main Street
1%	99%
Bonds	Commodities
Growth	Value
US	Japan
Consumer	Banks
Technology	Materials
High Yield	Cash
Passive	Active
Financial Assets	Real Assets
Large-cap	Small-cap

Source: Perennial Value, Bof A ML

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