

TRUMP'S IMPACT ON NZ EQUITIES, BONDS

Just like the UK voting to leave the European Union, the US has voted against the establishment by electing Donald Trump to the White House.

The BBC ran an article entitled "World media shock and dismay at Trump win", and included a summary of headlines including:

The New York Times says Mr Trump "is the most unprepared president-elect in modern history" and "has shown himself to be temperamentally unfit to lead a diverse nation of 320 million people".

The Washington Post sees little cause for optimism about the vote, recalling that Trump "has promised to deport millions, rip up trade agreements and international efforts to fight climate change, each of which would hurt many people".

The Los Angeles Times asks in its editorial "How did that happen?" The paper says "the campaign, and the candidate, played to the worst in America, and it has left the electorate scarred".

What these headlines and comments fail to realise is that neither Brexit nor Trump's win was an accident – 'the people', in particular the working and middle classes, are purposefully and deliberately giving the political elites a thump on the nose.

Trump isn't necessarily special, but his timing is.

The progressive liberal policies that have been pushed harder and deeper over the past few years have finally awoken an electorate that's saying "enough".

In the same way that 'ever closer union' in Europe was seen as eroding national sovereignty and "helping them not us", so too the winners in recent US history have been the political and economic elites.

The country has been moving in just the direction that the bureaucrats desire, and with academic and media institutions cheering them on, such liberal progressive politics have been championed by nearly all the sources of power, particularly mainstream media.

But for many people, this political and social direction does not seem to have enhanced their lives at all – rather they feel to be paying for others to succeed and, at the same time, being derided for not feeling happy about that.

It is therefore no surprise that, just as London voted to remain in the EU, the East and West coasts of the US preferred what Clinton offered.

What did surprise the institutions was that outside their own world, there was a groundswell of discontent against their urban liberal values.

A couple of observations

1. When you live and breathe a particular environment, it's hard to fully appreciate a different perspective. Therefore, the media and political elites struggled to gauge the mood outside their world.
2. Such was the elite's desire for the existing policies, power and direction to continue as it had been doing, there was a concerted effort to denigrate, sneer and patronise anyone holding an alternate view. There was a sense that these elites were saying "freedom of speech is paramount – just don't disagree with me".

It is the second dynamic that was particularly powerful.

Firstly, it re-enforced the view that the elites are snobbish, out of touch and arrogant – and so the more they shouted, the stronger the resistance came back.

But secondly, it became a situation where the 'middle voter' felt somewhat unable to publicly admit support for the anti-establishment view – a worrying trend for the supposed leaders of the democratic world.

Such a voter wanted to give the establishment a poke in the eye, wanted to see an end to the ever increasing push towards the policies and practices that seemed to contribute to many of the problems observed and felt (rightly or wrongly), but couldn't admit to it for fear of reprisal and stigma.

And now we have that same arrogance from those same establishments against the democratic outcome, albeit that Clinton was marginally ahead on the popular vote 47.7% to 47.5%.

The headlines the papers choose to run, the rhetoric of 'shock, turmoil, uncertainty...', a questioning of whether the electorate knew what they were doing with questions like "Does America really want this?", and even phrases such as "for better or worse, Trump will be the 45th president", indicate some denigration of the actual outcome.

Even the protests, violence and chants of “not my president” suggest that a number of people don't like democracy when the majority disagree with them.

What the media, academics and political elites need to realise, and realise quickly, is that these results are not a mistake, not an accident, but a revolt by the people against the establishments that seem to have failed them.

Telling the people they're wrong, stupid or ignorant is not going to restore the confidence such institutions once enjoyed.

So what about the markets, world trade, foreign policy – are these things in tatters?

The answer seems to be a resounding 'no'.

There is the inevitable volatility in markets following an event that wasn't 'priced in', but overall we don't observe movements that are any cause for particular alarm or panic.

Trump may well replace Yellen after her term finishes in early 2018, and new Fed appointments are likely to be more hawkish.

This means both monetary and fiscal policies are likely to lead to higher inflation, and higher yields at both the short and long ends of the curve – but this is a long way from concluding we're about to witness a bond market crash.

For equities, if anything, US businesses should see a slight boost to the extent that Trump desires to ease regulatory and tax burdens. There may even be some consumption increases if the fiscal spending and tax cuts find their way into the hands of the working family.

Trump is not against trade, but he has said he wants trade to be on different terms; so the TPP is either shelved, or at the very least back on the drawing board, and even NAFTA may be up for re-negotiation.

We should probably expect some trade spats as the rules change on people, and possibly some tit-for-tat protectionist measures that do little to help anyone.

However, as the world's largest and most diverse economy, the US is best-positioned to be its own island of growth and prosperity.

Self-sufficiency in oil is one of the final pieces that would enable the US to weather a less globalised world more comfortably.

It's the same with foreign policy

Trump is not against NATO, but he is frustrated that the US continues to pay huge sums for defence, while other countries cut spending in the knowledge that the US is there to protect them.

The US relations with Russia have not been so bad for many, many years, but now we have two leaders stating a desire to work together to set a course for an improvement – if they manage that, then it's a good move in global politics.

But Trump is a political newbie, and so we should expect some mistakes and clangers.

However, the extent to which there will be damage will be determined somewhat by the strength of the team he puts around him, and the degree to which he will allow himself to listen to their advice.

These things aren't yet known.

And it's important to note that there are many Republicans who are part of the disliked establishment, and there is little love lost between them and Trump too.

So even with control in the Senate, Trump is not going to have things all his own way.

What does the future hold?

A key risk that remains following the US election is across the Atlantic in Europe. The risk is that the political and establishment elite don't listen to the lessons of Brexit and Trump.

We have the Italian referendum in early December and French elections in May 2017. Doubling down on the resistance to the anti-establishment sentiment may well be the undoing of Europe.

There is still an opportunity for the officials and bureaucrats to heed the lessons and address the concerns of the voting public – but will they do that, or will we see more of these types of election results?

So in the meantime, expect to see some volatility in markets, expect to see some changes in approach to a number of areas of domestic and international policy.

And expect to see a president say things and act in a way that differs from the polished politic-speak to which we've become accustomed.

But other than that, it's business as usual.

Considerations specifically in relation to NZ

Equities

It's extremely difficult to assess any particular macroeconomic theme that will impact NZ equities as a result of the US election.

We note that New Zealand as an economy remains attractive, and NZ assets are desirable on a global stage – and we don't expect this dynamic to change in the foreseeable future.

One aspect to keep an eye on is whether equities that have benefitted from the yield trade will underperform if bond yields do indeed head higher under a Trump presidency.

Having said that, our portfolios are modestly positioned on the defensive side, and active management should be well-placed to take advantage of any stress or market dislocations that may arise. This is helped by having strong connections within our global network of investment professionals.

Interest rates/Bonds

It is interesting to note that, as the world realised that a Trump victory was likely, bond markets rallied – a typical 'risk averse' response.

However, once the US market opened, there was a sharp sell-off on US treasuries, as investors knew that Trump's policies are likely to be inflationary, with hawkish monetary positioning and strong fiscal stimulus through stated infrastructure spending.

The RBNZ indicates that there is unlikely to be any change in monetary policy for an extended period, possibly into 2019, with modest further easing if conditions deteriorate.

But with the economy performing well and housing moderating, further monetary easing is unlikely.

A slight bias to shorter duration bonds and remaining in high quality assets is our approach to managing fixed income assets in the current environment.

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