Tilney Bestinvest

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Economic Insight

US Presidential Elections

Anti-establishment politics continues to be a global theme with the prediction-defying election of Donald Trump as the next President of the USA. After the initial shock reaction from the markets, there is likely to be a period of volatility as markets digest the news. As usual, we advocate clients not to get caught up in any panicked moves, and instead focus on the fundamentals, which are little changed. Our portfolios remain cautiously positioned, to mitigate downside risk whilst still participating in upward market moves.

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Pollster forecasts, much like Central bank policies, appear to have lost essentially all credibility, as the US electorate has defied predictions and elected Donald Trump as the next President of the United States. In this article, we'll discuss the impacts as we see them as well as putting this event into the wider context that is the politics of the disenfranchised. Before delving further though, it is worth saying upfront that our guidance, as usual, is not to panic, to resist the urge to start making aggressive changes to your portfolio, and instead to reflect on any changes to the fundamental economic and market landscape. As with the EU referendum earlier in the year, this outcome was always a possibility, and is something we have both considered as part of our investment strategy and continue to monitor closely.

Initial Market Reaction

Markets initially reacted as expected to this shock – equity markets and the US Dollar sold off whilst perceived 'safe havens' including gold and US government bonds rallied. However, a couple of hours after the initial result, most markets had pared back these losses as instinctive reactions from traders gave way to more considered views from the wider investment community. Volatility is likely to persist as markets digest what has happened, but there is rarely much benefit in investors trying to trade during such volatile periods.

Who Actually Holds Power?

Of more relevance to us is the fundamental impact on the investment outlook- which for the immediate future seems little changed. President-Elect Trump made a lot of fairly alarmist noises on the campaign trail, but how much of that is bluster and how much is substance remains to be seen. Already he has started making more conciliatory statements, recognising the especially divisive nature of this election. It is also worth bearing in mind the checks and balances that are baked in to the US political system, where the President's powers are heavily constrained by the will of Congress. These Congressional elections have garnered less attention than the Presidential election, but they are also an important part of the equation, with the Republicans managing to retain control of both houses of Congress (though only narrowly in the Senate). Usually this would be a strong boost to a Republican President, but the last couple of months have been particularly fractious between the party and its presidential nominee, meaning there are many bridges that need rebuilding if Mr Trump is to get anything meaningful done.

Policy Impact

It is difficult to know what Mr Trump's policies will actually be, but from what we do know, he is likely to take aim at global free trade deals (not great for an already-challenged global economy, particularly emerging economies) and immigration (with its impact on the US labour market). At the same time, Mr Trump, with the support of the Republicans, is likely to bring forward fiscal stimulus measures in the form of additional government spending and tax cuts. Such fiscal measures could provide a boost to the US economy, though the long-term sustainability is still very much in question.

However, the benefit to asset prices could well be offset as support from monetary stimulus provided by the Federal Reserve loses efficacy. We remain wary of US equities, and will consider taking profits on US Treasuries, which have benefited in the immediate aftermath of the election, but which we expect to come under pressure as the government increases fiscal stimulus which as well as being inherently unsupportive for government bonds could also drive inflation expectations higher. In the medium term we expect US Treasury yields to increase from here (that is, prices to decrease) and the yield curve to steepen, though the exact timing is almost impossible to know.

Politics of the disenfranchised

We see this latest political shock as part of a growing theme that we've talked and written about before in terms of the politics of the disenfranchised. There is a growing sense that in the post global financial crisis (GFC) period we have had an economic recovery that doesn't feel like a recovery to your average member of the electorate. Policies such as Quantitative Easing have boosted asset prices and helped those with financial capital, but haven't helped those relying on their human capital: real wages (wages after inflation) have consistently fallen in the UK since the GFC. This has driven wealth and social inequality, and the perception that it is simply a case of "the rich getting richer", which has caused people to reject the status quo and driven a shift towards anti-establishment politics. This has manifested in the UK as the EU Referendum and the rise of Jeremy Corbyn (who, regardless of your views, I think even he would agree is an anti-establishment figure), across Europe with the rise of the likes of Syriza, a far left party, and Golden Dawn, a far right party, in Greece and in the US with the rise of Donald Trump. This global theme is likely to continue, and could mark a further shift away from Central bank-led monetary policy and towards government-led fiscal stimulus.

Conclusion

The election of Donald Trump as the next US President has been a shock to markets, but comes amid a rising tide of anti-establishment politics. Rather than knee-jerk reactions, we take this opportunity to re-assess our fundamental outlook, and find that relatively little has changed. We are cautiously positioned in our portfolios given the challenges we see to the global economy.

Over the last twelve months we have reduced exposure to equities and bonds which have benefited the most from monetary policy stimulus, measures which are now losing efficacy. We have instead increased exposure to alternative asset classes such as gold and absolute return vehicles which we see as providing diversification benefits and further return opportunities against a difficult economic backdrop. Whilst our portfolios are positioned to participate to some degree in further broad market gains, our defensive stance also aims to mitigate some of the downside risk in equity and bond markets. We will continue to monitor markets and economic indicators closely, updating our core investment strategy appropriately.

Disclaimer

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