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Dear Valued Clients and Consultants

ANOTHER SHOCK POLITICAL EVENT AS TRUMP SWEEPS US ELECTION

2016 has turned out to be the year when politics shook markets, both domestically and globally. In many ways, Donald Trump's victory in the US presidential election is a repeat of the 'Brexit' shock, when the UK voted in a June referendum to leave the European Union.

As with Brexit, markets were volatile in the weeks leading up to the vote, but surged prior to voting day as the final opinion polls indicated that Hillary Clinton would win. Despite a decades-old tradition of fairly accurate polling in the US, the polls were wrong, and markets sold off -

- The Mexican peso was hardest hit, falling to a record low against the US dollar.
- Asian equity markets closed sharply lower, with the Japanese market worst hit.
- The US dollar weakened against other developed market currencies.
- The rand was very strong leading up to the vote. It immediately lost ground against the US dollar (and more against the pound and euro), but is still stronger than a month ago.
- The JSE All Share index opened lower.
- The gold price jumped above US $1300.

Why do the markets fear a Trump presidency? The main issue is that his presidency presents an unknown, while a Clinton win would have represented continuity. More specifically, Trump's campaign rested on an anti-globalisation and anti-immigration platform, with promises to shake up the establishment. It is clear that these ideas are now firmly entrenched in the developed world, as real incomes of the middle classes have stagnated. Looming elections in Europe could also have unexpected outcomes.

Trump vs. Brexit

Given the similarities with the Brexit vote, it might also be useful to look at the differences. As much as Trump is the anti-establishment candidate, this does not represent a fundamental disruption of any existing political or economic relationships. Brexit implied Britain cutting some ties with its largest trading partner, Europe. However, there is still massive uncertainty over how and when this will happen. It could take years and cause massive disruptions (it might also not). A US presidency in contrast is a fixed four-year term and exists within a 224-year old constitutional framework, a framework that was specifically designed to limit the power of any one political actor.

Several JSE-listed companies have substantial UK exposure and therefore the Brexit vote had a direct impact on our market. With the Trump win, our markets are impacted as part of a broader emerging market sell-off.

Despite being a shock, the Brexit vote had little lasting impact on markets (apart from the pound, which remains weak). This cautions against a knee-jerk reaction.

The US is of course a much bigger economy than the UK, and what happens there truly has global implications. It is too soon to tell what a Trump presidency means for the US and global economy. Many of his more extreme promises (like building a wall on the Mexican border) are unlikely to come to pass. A silver lining might be that with Republican control of the White House and Congress, there is a chance that infrastructure investment and other growth enhancing initiatives (like tax cuts) might actually take place. But the long-term implications of a Trump presidency are simply an unknown at this stage, and markets hate uncertainty.

Nonetheless, as far as the global economy and markets are concerned, the most important building in Washington, D.C. is not the White House, but the Eccles building where the Federal Reserve holds its monetary policy meeting. Aggressive interest rate hikes are much more likely to cause a US recession than policy changes from Trump. The likelihood of a rate hike in December has fallen from about 80% to 50% according to the futures markets, while the longer term outlook still suggests that a rate increase will be gradual. Janet Yellen will stay on as Chair until 2018.

Investment Implications

Markets typically overreact to such events and are likely to be volatile while the outcome and its implications are digested. At Old Mutual Multi-Managers, we follow a longer-term valuation-based investment philosophy. We don't react emotionally to market surprises, but when the market overreacts, it creates opportunities for us to add value through tactical asset allocation. Our underlying managers share this longer-term valuation focus, and the sell-off similarly provides opportunities for them based on also being valuation-focused. Our funds are appropriately diversified, and this remains the best way to manage the inherent uncertainty in investing. We urge our clients to similarly stick to their financial plans and not make knee-jerk changes to their portfolios.

Should you have any questions relating to this note, please do not hesitate to call us on 021 524 4430.

Kind Regards

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