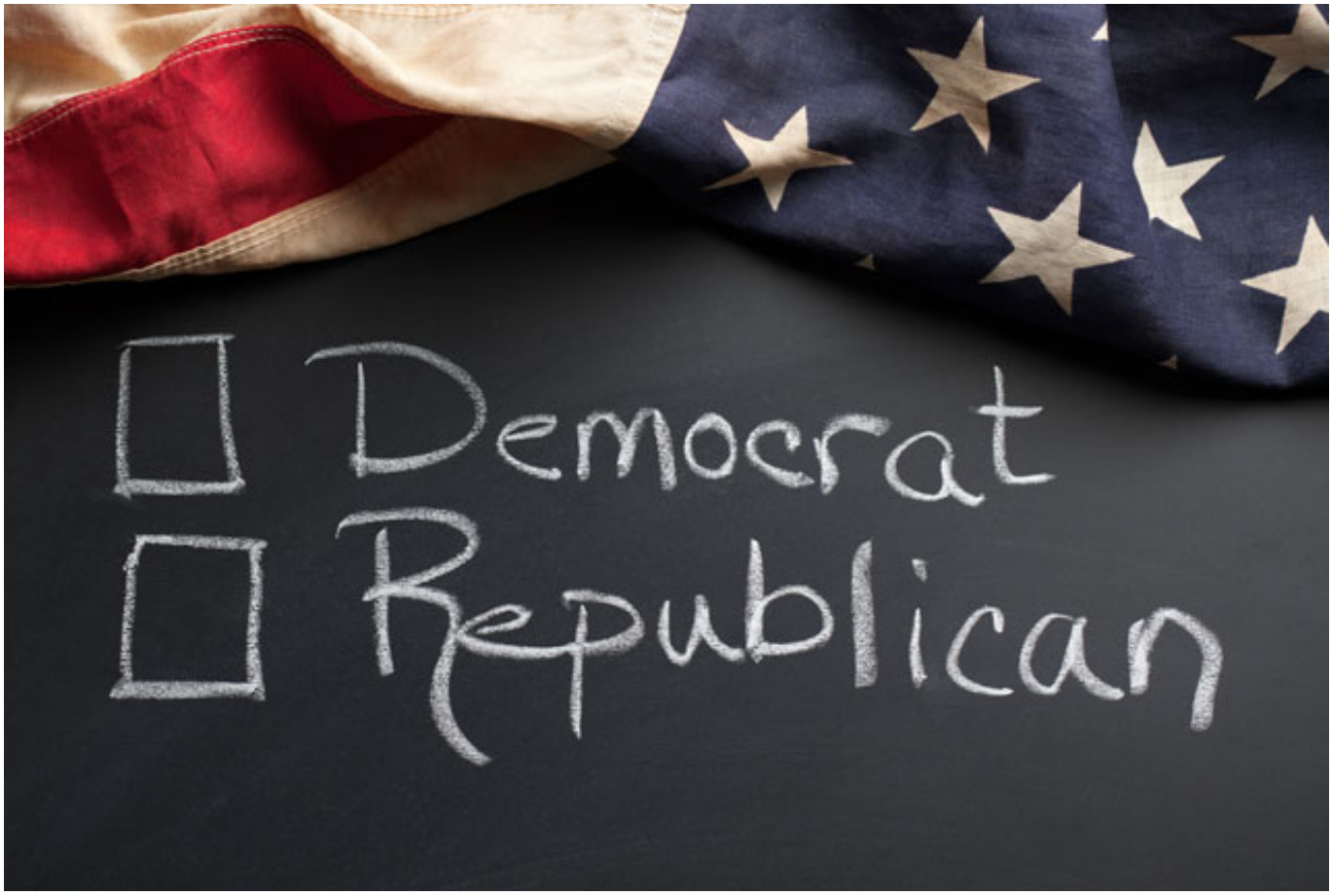


Is it crunch time for Trump?

After the volatility we saw in October investors would be forgiven for thinking markets were long overdue a respite from the assault of disruptive headlines. Indeed, Trump seemed to give us just that when he announced a new desire to strike a trade deal with China last week.

Before we can digest the potential of this we have to address the elephant in the room which is tomorrow's very partisan US mid-term elections which have the potential to upset the already volatile applecart of global markets.

First off, what are the US mid-term elections? Well, in laymen's terms, they are elections in the middle of a US presidential term in office. The difference here is the office of the president is not up for election, this time it's the House and the Senate which are up for election.

The "House" means the House of Representatives which consists of 435 representatives from every state in the US. Simply put, the more people living in a state, the more representatives that state has in the House. Tomorrow, all 435 seats in the House are up for re-election and should more than half of the

elected representatives be either Republican or Democrat, then that political party will control the House.

The same goes for the Senate which consists of 100 senators with no more than two senators from any one state. For a political party to control the Senate they simply need 51 out of the 100 seats.

The key point to keep in mind tomorrow is that, out of the 100 Senate seats, there are only 35 seats up for reelection not the full 100. Of these 35 seats up for grabs, 26 seats are currently being held by Democrats meaning the Democrats will need to hold onto these 26 seats and gain another 2 to take the majority. This is quite a tall order for any political party. Early polls forecast that the Republicans will win the Senate because almost all their seats coming up for re-election tomorrow are safe.

So, the early polling says it's the 435 seats in the House of Representatives we need to watch. 218 seats is the magic majority number and as it stands the Democratic party need to gain another 25 seats to hit 218. Again, polling indicates the Democratic party has 185 "safe" seats and the Republicans have only 140 safe seats. This leaves 110 seats which could go either way of which the Democrats only need 33 to take the majority in the house of representatives.

Why does this matter to the president? The situation is problematic for the president because, the current House and the Senate both have Republican majorities, meaning that passing policy reform through republican controlled houses should be relatively straight forward compared to passing new policy through a house controlled by the opposition.

In short, if the Republican party lose control of either of these houses, then the president loses control of his ability to implement policy change, which potentially leaves the president rudderless in terms of delivering the bumper reform package he was elected into office on. No surprise then that President Trump's mid-term election campaign efforts have surpassed that of any US president in history. To pour petrol on the fire, some political commentators are touting the possibility of a presidential impeachment if the Democrats take the house. A small chance of this happening, but it is on the table.

What can we expect from tomorrow's elections? Stock markets are pricing in the Republicans retaining control of the Senate and the Democrats taking control of the House of Representatives. This outcome will likely leave US markets flat to slightly negative but essentially it won't rock the boat because it's what the market has already priced in and it will mean the remainder of Trumps term in office will lack any real firebrand policy shifts as Democrats will simply vote it down.

Devil's advocate? Markets have consistently failed to correctly price in election and referendum polls, so perhaps we should be ready for a result that isn't quite as benign as the market hopes.

If the Republicans retain control of both the Senate and the House of Representatives, this will be seen as a 'risk on' scenario and markets should rally on the assumption that Trump will continue with his reform agenda which will likely ensure that the spending taps are kept on and thus kick the recession can down the road into 2020 or further. Markets also believe, in this scenario, that with control of both Houses, Trump will likely be more disposed to strike a trade deal with China which has been the main source of

negativity in 2019 and as such could go some way to correcting this.

On the flip side, if the Democrats win both houses then markets are likely to take this as a bearish event on the assumption that the Democrats will go after Trump's policies and political appointments and potentially will dismantle his stimulus plans which could bring the chance of a recession forward and thus re-ignite the volatility we saw in October. With Trump losing control of domestic policy implementation, he could also turn to the only avenue of presidential influence which doesn't require congressional approval, foreign policy. This could mean even harsher trade sanctions on China as Trump cannot so easily implement his domestic agenda. Whichever outcome arises tomorrow, this mid-term election has been marked as one of the most debated in US history with voter turnout set to reach record levels as the whole of the US comes out to have their say in what is being widely publicised as a referendum on President Trump.

TAM has factored the binary nature of these mid-terms into its stride and taken healthy profits for its clients by reducing its exposure to the US market. Even if markets get the 'risk on' scenario of a Republican clean sweep tomorrow, one thing remains clear, as we move into 2019 markets and investors will have to get used to the persistence of global volatility and as such TAM will continue to build defensive moats around our clients' investment strategies to prepare them for this new trading environment.

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