

The markets aren't having it

Capital is a coward. At the first sign of trouble (everyone calls it "uncertainty" these days) it bolts for the door. It's what the majority of the media and politicians warned us would happen if Trump won. It sounded plausible and all appeared to be going to their script in the small hours of last Wednesday morning when it became apparent that Trump's victory was nailed on. But the markets weren't having it.

Asian stock markets were the first to open. Entering stage left, Japan stepped forward to fulfil its familiar role as the nervous stock market prepared to sell at any price and shares closed down 5.3% in Tokyo. All other Asian markets fell. The futures markets for shares in London and New York were just as bad, and bonds everywhere rose sharply as they sucked in money desperately seeking a safe haven. Similarly, gold countered the fall in shares with a rise of 5%, helped on a little by a 1.5% fall in the US dollar. On any other day this would've been impressive but was even more so on a day where the dollar might've been expected to act as a safe haven.

Tokyo stock market: Nikkei 225. Source: Reuters, Nov 12th 2016

However, newspaper columnists barely had time to gleefully write their obituaries for global stock markets before European stock markets bounced. Even before New York had opened, the FTSE 100 was actually in positive territory, confounding bears and pundits alike. Bonds started to unwind again and even the Mexican Peso clawed back some of its initial loss of 11.6%. Trump's conciliatory and reassuring speech probably helped but clearly something else was going on.

It's fair to say that markets generally got caught facing the wrong way. Indeed, bookmakers Paddy Power revealed that a £5 treble bet on the unlikely trio of Leicester to win the Premier League, the UK to leave the EU and Donald Trump to become President would have won £15million.

Looking at various stock, bond and currency indicators that tracked the polls, they were all tilted towards a Clinton victory immediately prior to the election. Like the Brexit result, some degree of volatility was to be expected as investors shifted their short term bets to reflect a new reality even without having much idea of what it looked like.

It's not hard to imagine that buyers weren't exactly queueing up in the middle of it all or that there was some degree of forced selling driving prices down. However, we do know that there was a lot more cash on the sidelines. This wasn't surprising because, like Brexit, the election was a specific date and, knowing it was a binary event, everyone had plenty of time to prepare; whether to protect their portfolios or hoping to profit from some bargain hunting.

There has also been a reaction in investment themes related to Trump's policies which he appears determined to implement. The big one is infrastructure spending. This story could run because, unlike Japan, which undertook large infrastructure building projects of roads to nowhere and unnecessary bridges, it's been well known for years that swathes of the USA have suffered from underspending on roads, rail, schools and hospitals. The details are sketchy but stocks have reacted quickly. Shares in US construction machinery manufacturer Caterpillar, for example, rose 15% following the Trump win, as did Japanese plant maker Komatsu. The ramifications of a successful implementation are big and they are global.

But these are speculative moves. Trump's win has got global markets thinking about fiscal deficits, tax cuts and inflation. But, in this regard, Trump is unusual for a Republican insofar as he is a fiscal dove but a hawk on free trade agreements which he would like to tear up. But his Republican congress, with Paul Ryan at the helm, is almost the exact opposite with a more typically conservative view to curbing spending and favouring free and open trade agreements.

We will have to wait and see what actually gets delivered but, for now, the markets are pricing for a pickup in the economy driven by tax breaks, more jobs and a bit of inflation. We may find an increasing number of parallels with the Reagan years and the economic boom associated with Reaganomics. It's a nice idea and undoubtedly good news for the UK if it comes to pass but there's a long way to go yet.

For now, we are close to benchmark weight in an international mix of high quality stocks in developed

markets with a small exposure to emerging markets for higher risk mandates. An underweight position in international bonds continues to benefit from a bond market sell off in reaction to the prospect of higher inflation in the US spilling over into the other parts of the world. We are watching bond markets closely to see if an opportunity to start buying presents itself.

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