Australian Market Summary (Issue 425) – 11 November 2016

Australian Market Summary (Issue 425) – 11 November 2016

Wow.

So here we are.

Since Wednesday I've been trying to make head and tail of the implications for markets of a Trump Presidency, and in truth I'm still not sure my views are fully-formed.

The difficulty with this election outcome, and I say this entirely bereft of political bias, is that on paper at least it turns over so much of what has been investment market status quo for at least the last decade, if not more.

We know the vote is anti-establishment and anti-globalization to boot, that's a given.

But Trump's policies imply the need for a change, some of it good, in investment thinking.

Trump is seen as being fiscally expansionary and de-regulatory. He plans to spend aggressively on domestic US infrastructure and to cut corporate tax rates to promote business expenditure.

The market has seen these policies as reflationary and at least in this short period post the election result, has aggressively voted with its feet in support of those investments most likely to benefit from short-term stimulus.

> ***The Trump economic plan in an investment market sense can be encapsulated simply by several catch-all's:***

- Nationalism vs globalization
- Old economy vs new economy
- Fiscal stimulus vs monetary stimulus
- Labor vs capital
- The 'adorables' vs the 'deplorables'

Let me try and explain this all for a minute, and then after that I will try and put into context what this means for your investment portfolios going forward.

In seeking to grow jobs and the domestic economy, Trump policies will expand US government debt materially.

Many industries and companies that will benefit from the policies will be those that have lost out to international competition in recent decades, or in the case of domestic infrastructure spend, failed to receive much government support.

To this end, the policies are seen to be supportive of domestic employment and domestic US business demand, and furthermore very 'bricks and mortar' centric given the focus on infrastructure.

By expanding government debt and contributing to growth, bond-markets have sold off aggressively such that US 10-year bond yields have risen to 2.15% from under 1.40% as recently as July – they were 1.82% at the start of the week.

After a prolonged period of low bond yields and tepid economic growth, there seems to be a willingness to believe that by way of fiscal expansionism under a Trump presidency, the US economy might finally see some additional improvement.

Furthermore, that that improvement will be most significantly felt by the lower and middle classes by way of jobs and wage growth.

Reflecting these views, in the last 2 days of trading post the election we have seen an enormous change in investor behavior.

For example –

- Bond yields and bond proxy shares have seen heavy selling. Utility, real-estate and infrastructure stocks have been punished.
- Similarly, technology shares have been smashed on the basis that these shares trade on very high valuations that are highly sensitive to rising interest rates. The tech-heavy NASDAQ index has underperformed the financial and industrial-heavy indices such as the S&P500 and the Dow industrial.
- Commodity stocks have risen dramatically

Once again, these moves fly in the face of the consistent and prevailing investment trends we have seen in recent years.

So the next question then becomes – are these moves sustainable? Have we in fact had a basis change in bond yields and growth, and if so, what do we then do?

Is Trump really the economic savior that markets this week imply and that very few investment market professionals (me included) foresaw?

On the latter, I must share some skepticism, but on the former I think it is entirely appropriate to think that bond yields have now indeed bottomed out since Trump's plan to raise government debt and increase tariffs is bond market negative.

From an Australian stand-point I will make the following remarks:

- The prospect of a weaker Australian Dollar now seems very real given the expected US economic stimulus, and this is a good thing for the medium term
- Higher global bond yields (1) will drag higher bank funding costs, so I genuinely would expect bank mortgage rates to rise in the coming month. Australia is a nation with elevated household debt, so this factor will likely prove a continued negative for consumption trends going into 2017
- Higher global bond yields (2) now seems set to stay, which means that the

relative value of Australian property, infrastructure and utility assets will likely continue to see negative reappraisal. That said, the de-rating of companies like Telstra (TLS) and our recent BUY recommendation on Transurban (TCL) has made these stocks outright CHEAP here.

Guys in simple terms Australia is far more levered to China nowadays than it is to the US, and China on the whole will be negatively impacted by Trump's protectionist plans.

The rise in bond yields is another negative factor for Australian shares since so much of the market are seen to be defensive and income oriented, so the rise in Australian bond yields to 2.60% this week will prove a negative for valuations.

Property and infrastructure and utilities have been belted to the extent that I think they now look good value, whereas the exuberance around commodity shares in particular looks borderline evangelical – though again on this last point, I have been wrong here for the last few months.

There will be trades that emanate out of the Trump victory and we will be sure to be in touch, but for now many of the moves look particularly extreme and grounded in a surety that all of the Trump's policies will be enacted in a clear and concise manner.

One thing we have learned through the campaign however is of Trump's unpredictability, so please forgive me that right now I don't feel like I have all the answers, and that means I am reluctant to make too many changes until such a time as I feel confident in the ground beneath my feet.

I have many more comments I wish to make on the subject, so please don't consider this the start and end of the conversation.

Have a great weekend.

	Index	**Change**	**%**
All Ordinaries	5267	-94	**-1.8%**
S&P / ASX 200	5185	-90	**-1.7%**
Property Trust Index	1311	+13	**+1.0%**

Utilities Index	7083	+84	**+1.2%**
Financials Index	5754	-179	**-3.0%**
Materials Index	9069	+11	**+0.1%**
Energy Index	7961	-218	**-2.7%**

	Index	**Change**	**%**
U.S. S&P 500	2167	+78	**+3.7%**
London's FTSE	6828	+37	**+0.5%**
Japan's Nikkei	17344	+209	**+1.2%**
Hang Seng	22839	+155	**+0.7%**
China's Shanghai	3171	+42	**+1.3%**

Key Dates: Australian Companies

Mon 14th November **Div-Ex Date:** ANZ (ANZ), Westpac (WBC), SVWPA

Tue 15th November **Div Ex-Date**: WOWHC

Wed 16th November **AGM:** NAVITAS (NVT) **Div Ex-Date:** Dulux (DLX)

Thu 17th November **AGM:** Mantra (MTR), Sonic Healthcare (SHL)

Fri 18th November **N/A**

Disclaimer:

any financial investment decision. Prime is bound by the Australian Privacy Principles for the handling of personal information.