Innova Market Insights

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Issue #45 – "What Now?"

Interesting Links from Around the Web

Election : What Happened to the Firewall? : DailyMail
Markets : TSX, Dow Rally – Trump Election : GlobeInvestor
Video : Michael Moore Predicted it! : (Offensive Language)

'Predicting Rain Doesn't Count. Building Arks Does'
-Warren Buffett

Like many of you, I stayed up last night to watch what can be described as a slow-motion train wreck. When the dust settled, "the Donald" had secured enough votes to be named the next President of the United States of America. That said, let's examine how this might impact you over the next four years.

What does this mean for the economy?

At this time very little is known regarding Trump's economic policy as, remarkably, this was not a frequent talking point. Of the few policy related campaign promises, here are a few of the important ones:

On Taxation & Economic Stimulus

- Lower Business Tax Rates from 35% to 15%
- Introduce a 10% tax on repatriation of assets (companies bringing foreign dollars back to the US)

Lowering business tax rates is typical 'trickle down economics' which no longer have many supporters in the world of economics. This is particularly true given the huge debt burden currently faced by the US. Nonetheless, it will prove beneficial for investors who will see an increase in available cash in corporations. Hopefully it will be put to good use through reinvestment, or dividends to shareholders.

The second measure aims to tackle the over $2.5 trillion US dollars held by multinationals in offshore accounts. The hope is that this change in taxation will create an opportunity for US firms to bring their dollars back to the US and invest them into the economy, thus stimulating growth. Although the idea is sound in principle, it was attempted by Bush in 2004 with limited success. According to the National Bureau of Economic research, for every $100 brought back into the country, only $1 was invested back into the economy. Conversely, an estimated $94 of those dollars found their way back into the pockets of investors by means of share buy-backs or dividends.

In either case, the repatriation of this much money would lead to a considerable strengthening of the US dollar vs all other currencies. Tax-favoured strongholds in particular, like Ireland and Holland, both Euro denominated markets, will be especially impacted. The strengthening of the US dollar would be beneficial to investors already holding US stock and would help the Canadian export sectors. Sadly, the latter may get battered by the rest of Mr. Trump's proposed policies.

On Trade

Of greatest concern, Trump has voiced the desire to 'renegotiate' pre-existing trade agreements like NAFTA. He favours protectionist policies over free movement of capital and goods across the borders. Such policies could lead to a substantial cut in cross-border production lines and trade between Canada, the US, and Mexico. Given that the Canadian economy is heavily dependent on trade with its southern neighbour, this does not bode well for companies who were just starting to build momentum on the heels of a weakened loonie.

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On Energy

Trump is a big supporter of fracking and has stated his goal of being "totally independent of any need to import energy from the OPEC cartel or any nations hostile to our interests". Oil prices may falter as production increases with no offsetting increases in demand.

What does this mean for your investments?

As of midday, the US markets are proving considerably more resilient than expected, opening up a few points and managing to stay in the green. The Canadian dollar is down 1% so far on concerns over trade and oil prices. As one of the first markets to open, the Japanese Nikkei took a beating and lost 5.4% of its value today, while the Eurozone helped settle markets before the North American open.

Ultimately, investors are being reassured by the fact that the other executive branches of the government will stand in the way of Trump blowing up the country and all pre-existing trade deals. The split congress will continue to provide gridlock, for better or for worse, and so the economy and the markets will continue to march on.

This experience serves as a good reminder that betting on political issues is a fool's errand. As long-term investors, we try to find quality companies that can grow their companies and share those profits with us. We do not believe that President Trump or Clinton could have stood in the way of that happening. With this in mind, we remain cautious and look for down markets in which to buy up value positions should they materialize.

At the time of this writing, markets continue to trade at a premium, not at discount. The Dow Jones is hovering a few points below its record highs while the TSX is trading near its multiples peak at 15 times earnings.

Further, any drops in the Canadian dollar will offset our ability to 'bargain buy' in the United States. As such, a drop in the S&P500 and Dow Jones are not the only factors that will influence the timing of any market moves. As always, we will keep you posted!

Sources:
Manulife Investments "Investment Note" Nov 9th 2016.
National Bureau of Economic Research.
Twitter (RealDonaldTrump).
Globe & Mail (Market Data).