A Trump win – So this is what living through historical moments feels like!

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Like the post Brexit reaction the markets (ex Japan) have been remarkably mature about dealing with what was a massive surprise. Forgetting your political sensibilities, it is important to consider that the American people have voted against the logjam that dogged the Obama presidency over the last four years. This has also been a vote against the unconventional monetary policy which has ruled the roost in developed markets over the last five years.

The point is that I think you need to consider the market framework is changing. We can no longer expect the narrative of 'lower forever' bond yields which has underpinned every investment decision to continue. This will have an impact across asset classes and the reverberations will be felt depending on how decisive the policies out of Washington become.

So what does one do? I used the VUCA world analogy in my recent presentations in Australia. The American military coined the term VUCA (Volatile, Uncertain, Complex & Ambiguous) world to describe the conditions in Afghanistan and Iraq. Their considered advice was captured beautifully in this quote – "we are moving from a world of problems, which demand speed, analysis and elimination of uncertainty to a world of dilemmas which demand patience, sense making and engagement with uncertainty."

So engaging with uncertainty, I would suggest the following food for thought:

a. The biggest impact of the Trump presidency will be felt in the bond market - bond markets have a lot to think about in this new reality. Have we seen the bottom of negative interest rates? Will fiscal policies which the central banks are pushing be as 'bond market friendly' as the negative interest rate policies have been? Are reflationary policies likely to yield higher long term rates and a steeping yield curve. Is the bond market prepared for higher inflation?

b. If the answer to any of the above questions is a 'yes' then what has worked since 2010 in the equity markets (quality at any price and low volatility stocks) may not work as a cohort in the future. Stock picking and active management of your portfolio is likely to become even more important. If you're searching for value, sectors like financials, energy and materials must be appearing on your radar screens.

c. Beyond that, there is limited value to be had from second guessing what Trump might do based on his Twitter feed. The US political system has a number of checks and balances and it is not without reason that a politician's promise carries little weight!

d. However precisely because of this from a developed market perspective, US equity markets which have been amongst the strongest performers over the last few years, become less interesting in a global RELATIVE context. Europe and especially the UK which has obviously seen quite a sell-off in US dollar terms are likely to be areas where investors would like to re-engage. For Europe a lot depends on how the Italian referendum goes but the markets seem to be pricing in a worst case scenario which at least from a probability perspective bodes well. There is no all clear here but there are probably more unknown unknowns in the US now then there is in Europe where we have an idea of most of the bad scenarios.

e. Emerging markets continue to be interesting – though dependent on the path that the dollar takes. However it would probably be markets like Russia, Brazil which investors have hitherto shunned. I also continue to believe there is a high degree of complacency around China currently which we should be mindful of. The debt intensity of the economy continues to rise and it is taking more and more of credit to drive an incremental RMB of GDP growth – this has no good ending!

f. On the rate rise scenario, Trump has been pretty clear that he will look for a change in the Federal Reserve Governor. Given the reflationary policy framework, we expect the Federal Reserve to move rates in December as the markets currently anticipate. The only fly in the ointment would be if the markets sell off between now and December. The Federal Reserve has historically been a prisoner of equity markets and I would not hold my breath for it to be different this time.

g. Irrespective of the election battles, populism has clearly won the war this year. Populism is likely to be inflationary and in a world driven by protectionism is likely to be stagflationary (stagnation + inflation = the worst of all worlds). This combination will hurt the valuation multiples before it hurts the market's earnings.

The silver lining and introspections

I believe that with a focus on capital protection, while current market valuations may make driving strong absolute returns difficult, there is a significant opportunity to drive better outcomes for clients relative to their other investment avenues. In fact from an active manager's perspective (bond or equity) a sideways valuation driven market creates more opportunities than then one which we have been in for the last five years. We are ready for battle - 'bring it on'!

Lastly, in relation to both Brexit and the US elections, there has been introspection for me. While picking stocks, I always look for non-confirmatory evidence – so if I am buying a stock, I always like to the talk with the analyst on the street who has a sell rating on the stock to understand and appreciate his thesis.

It has struck me that with the advent of Facebook, Whatsapp and all these ways to remain connected, that I am not following this approach in my personal life. Looking at my Facebook/Twitter feed and my Whatsapp messages since the results, it seems we are all creating our own personal echo chambers populated by friends/colleagues who generally only confirm our beliefs – one of the unfortunate unintended consequences of a platform which only shows you it thinks you might like!

For me (and if you are like me, then you) it is now even more important to try and engage outside our comfort zone. It is only then we will make a positive step towards bipartisanship and appreciating the views of others – something both the economic as well as the political world sorely needs right now!