FINANCIAL PARTNERS

Weekly Digest

Week ending **13 November 2016**

Pollsters fail to sniff out silent Trumpers

Despite all the polls and indications to the contrary last week, a political outsider, Donald Trump, spectacularly beat Hillary Clinton to become President-elect of the United States. By all perceived wisdom Mrs Clinton should have walked the contest: she is a high profile career politician; she outspent Mr Trump significantly on the campaign trail; she had scores of celebrities lining up to endorse her Democratic candidacy; and Mr Trump's litany of embarrassments and gaffes would usually have derailed a candidate's progress. And yet, he won.

The day before the vote, some polls gave Hillary Clinton an 80% chance of winning. Clearly this was wide of the mark. Indeed, given this and the ineffectual polling in the run-up to the Brexit vote, it is difficult to know who has had a worse year – pollsters in 2016 or credit ratings agencies in 2008. There are some parallels that can be drawn from these two failures. The first is that neither pollsters nor raters can truly be considered as 'outsiders' to the system that they are judging. They are ultimately creatures of the environment that they are trying to assess and as a result, however sophisticated their analysis (or not), the analysts will be subject to a number of deep seated beliefs that are hard to recognise before the fact, let alone shake off. In 2008 Collateralised Debt Obligations (CDOs) were adjudged to be safe because the assessors were financially literate and this led them to take a number of assumptions at face value that may puzzle an outsider. Likewise pollsters in the US and the UK, as people who have lived and breathed politics for years, would deep down believe that the 'rational choice' of a Bremain vote or a Clinton presidency would happen. Conversely, Lehman Brothers was probably 'too big to fail', but collapsed anyway, despite that outcome being inconceivable to almost everybody in the system.

So, why did the polls miss the support for Trump? Perhaps the Democrats miss-stepped by casting Trump supporters as a "basket of deplorables". Had this not been the case, then perhaps a prospective Republican voter would have been more candid with pollsters and the result would have been a better understanding of the enormity of the challenge faced by Clinton and her team. The same can be said of the pro- and anti-Brexit campaigns. The group that were against Brexit were so successful in painting their opposition as parochial little Englanders that many of those voters that intended to vote to leave kept the fact hidden from pollsters. It is surprising, in this era of social media, endemic 'oversharing' and big data that it is not simpler to call an election. But perhaps social media turns political discourse into a righteous shouting match between factions. Members of either side have a 'network' that is self-selected and therefore creates an echo chamber of views which feed off themselves within this unchallenging environment. Whereas political discourse is it at its best when it is open and inherently challenging to all involved rather than simply perpetuating the views of groups in isolation.

What can investors learn from this? Firstly, and most obviously, politics is extremely unpredictable. As a result, an investment strategy that relies on predicting outcomes such as these to make money requires extremely good foresight. Our porfolio managers prefer to use a long term valuation based asset allocation framework because they believe that gives them a much greater chance of identifying solid long term investment opportunities. The managers do bear in mind risks such as these recent elections as a potential source of volatility, and so they will consider adjusting their risk exposure to better protect investors from these sorts of shocks, where appropriate. The other key takeaway is to remember that they are also part of a system, and that they must, from time to time, look at it as an outsider. It is this fresh perspective that can help to identify oddities and habits that have little fundamental justification. They must avoid being taken along with intellectual currents and be alert to identify occasions where the perceived wisdom is wrong.

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The **Marketplace**

- Donald Trump wins US election to become 45th US President
- Property mogul's victory sparks bond sell-off
- Emerging market currencies suffer
- Investors focus on sectors that will benefit from Trump's policies
- Commodity falls lead by oil and gold

Market **Focus**

US

- In a shock result, Republican candidate Donald Trump beat Democrat Hillary Clinton by 290 electoral votes to 228 to become the President-elect. Clinton won the popular vote by 60.98 million votes to Trump's 60.35 million, but Trump won key swing states such as Pennsylvania, Ohio and Florida to ensure his overall victory in the deciding college vote.
- The Republican Party also retained control of the Senate and House of Representatives, with 51 out of 100 seats held in the former, and 239 out of 435 seats held in the latter.
- Despite an initial fall, and contrary to the crash many had predicted, developed equity markets surged, with global equities rising 2.3% last week, whilst US equities rose by 3.9%.
- Prospects of higher government spending on infrastructure, lower tax rates, looser financial regulation and a potential repeal of the so-called Obamacare has benefitted US banks, healthcare firms, and industrials. Last week saw 11.3%, 5.8% and 8.0% rises for US finance, healthcare and industrial equities, respectively.
- Conversely, the prospect of higher spending leading to rising inflation resulted in a global bond sell-off, with global government bonds down 3.0% last week, whilst US 10-year Treasury yields rose by 37.4 basis points to 2.15%. Equity sectors dubbed as 'bond-proxies' such as utilities and real estate suffered similar sell-offs: 4.1% and 1.4%, respectively.

Emerging Markets

- EM equities and currencies took a hit as investors worried about the extent to which Trump might enforce protectionist policies. These prospective policies may potentially erode trade income from the US, something upon which many emerging economies are dependent for growth.
- Global EM equities fell 3.5% over the week, led by losses from emerging Latin America (-10.4%) and BRIC countries (-3.1%).
- In terms of currencies, the JP Morgan index of emerging market currencies fell by 4.2% against the US dollar from Wednesday. The Mexican peso was hit worst, falling by 11.2% against the US dollar.
- Global emerging market bonds suffered a similar fate, falling by 2.4% over the week.

Commodities

- Gold experienced its worst week since June 2013, falling 5.9% to USD 1,227.64 per ounce. The precious metal initially rose by 4.8% as investors flocked to safe-haven assets late on Tuesday, but then tumbled as sentiment turned after Trump's reassuring acceptance speech.
- Brent crude oil prices fell by 1.8% to USD 44.75 after OPEC's new 'World Oil Outlook' predicted that crude prices will not top USD 60 per barrel until after 2020. A separate report by the International Energy Agency increased its oil production estimate from non-OPEC producers to nearly 500,000 barrels a day, stating that "2017 could be another year of relentless global supply growth".

James Klempster (CFA) & Oliver Bickley

Source: Bloomberg. Returns in US dollars unless otherwise stated.

Asset Class/Region	Currency	Currency returns			
		Week ending 11 November 2016	Month to date	YTD 2016	12 months
Developed Market Equities					
United States	USD	3.9%	1.9%	7.3%	5.9%
United Kingdom	GBP	0.8%	-3.0%	12.0%	11.3%
Continental Europe	EUR	2.3%	-0.9%	-4.6%	-7.4%
Japan	JPY	2.3%	-1.1%	-9.1%	-11.7%
Asia Pacific (ex Japan)	USD	-1.2%	-2.9%	7.2%	7.1%
Australia	AUD	3.7%	1.3%	5.3%	9.2%
Global	USD	2.3%	0.4%	4.0%	2.4%
Emerging Market Equities					
Emerging Europe	USD	0.1%	-3.8%	11.8%	0.7%
Emerging Asia	USD	-2.3%	-4.1%	6.8%	4.5%
Emerging Latin America	USD	-10.4%	-15.4%	22.9%	11.4%
BRICs	USD	-3.1%	-6.1%	10.6%	5.9%
MENA countries	USD	4.1%	1.9%	1.0%	-1.7%
South Africa	USD	-6.5%	-10.3%	9.1%	-5.0%
India	USD	-2.9%	-5.0%	3.6%	5.7%
Global emerging markets	USD	-3.5%	-6.2%	9.1%	4.3%
Bonds					
US Treasuries	USD	-1.9%	-1.6%	2.4%	2.8%
US Treasuries (inflation protected)	USD	-1.0%	-1.0%	6.1%	6.2%
US Corporate (investment grade)	USD	-1.6%	-1.6%	6.6%	6.4%
US High Yield	USD	-0.1%	-0.9%	14.5%	10.2%
UK Gilts	GBP	-2.3%	-1.3%	8.6%	9.6%
UK Corporate (investment grade)	GBP	-1.7%	-1.0%	8.7%	9.9%
Euro Government Bonds	EUR	-1.7%	-1.7%	2.3%	2.5%
Euro Corporate (investment grade)	EUR	-0.8%	-0.8%	4.4%	4.2%
Euro High Yield	EUR	-0.3%	-0.7%	7.3%	5.3%
Japanese Government	JPY	-0.4%	-0.2%	4.9%	5.8%
Australian Government	AUD	-1.4%	-1.2%	3.6%	4.2%
Global Government Bonds	USD	-3.0%	-1.7%	5.1%	6.2%
Global Bonds	USD	-2.5%	-1.6%	4.6%	5.3%
Global Convertible Bonds	USD	-0.6%	-0.9%	0.5%	-0.7%
Emerging Market Bonds	USD	-2.4%	-2.8%	10.2%	9.3%

Source: Bloomberg

Asset Class/Region	Currency	Currency returns			
		Week ending 11November 2016	Month to date	YTD 2016	12 months
Property					
US Property Securities	USD	-0.4%	-4.0%	0.2%	3.7%
Australian Property Securities	AUD	-3.8%	-4.3%	-2.5%	0.8%
Asia Property Securities	USD	-2.2%	-2.6%	5.5%	6.2%
Global Property Securities	USD	-2.0%	-3.9%	1.3%	3.5%
Currencies					
Euro	USD	-2.6%	-1.1%	0.0%	1.1%
UK Pound Sterling	USD	0.6%	2.9%	-14.5%	-17.2%
Japanese Yen	USD	-3.3%	-1.7%	12.8%	15.2%
Australian Dollar	USD	-1.7%	-0.8%	3.6%	6.9%
South African Rand	USD	-5.7%	-6.5%	7.4%	-1.8%
Swiss Franc	USD	-2.0%	0.1%	1.5%	1.7%
Chinese Yuan	USD	-0.7%	-0.6%	-4.6%	-6.5%
Commodities & Alternatives					
Commodities	USD	-1.1%	-3.1%	5.0%	-3.1%
Agricultural Commodities	USD	-0.9%	-1.7%	1.2%	0.3%
Oil	USD	-1.8%	-7.3%	20.0%	-2.3%
Gold	USD	-5.9%	-3.9%	15.7%	13.0%
Hedge funds	USD	1.1%	0.2%	0.8%	-0.8%

Source: Bloomberg

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