Kenanga Investors

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Commentary on Post-US Presidential Election

Market Review

On Tuesday 8th November 2016, Donald Trump staged a surprise victory over Hillary in the now concluded U.S Presidential Elections. The initial market reaction was a sharp knee-jerk risk aversion as investors grappled with the uncertain policy outlook in US as Trump was widely perceived as a wildcard candidate. Asian markets plunged sharply while S&P 500 futures fell as much as 5% in intra-day trading. Price reaction moderated thereafter and US market staged a strong rebound to post record highs as investors interpreted Trump's pledges of fiscal stimulus and trade protectionism as highly inflationary and positive for dollar and equities. Emerging markets however continued to be negatively impacted mostly led by large declines in currencies. In the bond markets, the surprise election result has caused heavy selling of US Treasuries. US Treasury 10 year yield has since jumped to 2.15% as of 10 November closing from 1.85% on 8 November, the day before the presidential election. In tandem with yield increases across global bond markets, Malaysian government securities (MGS) also saw yields going higher, albeit in a more moderate amount. The 3 year, 5 year and 10 year MGS yields advanced to 3.24%, 3.45% and 3.78% separately on 10 November closing, compared to 3.08%, 3.32% and 3.66% respectively in the closing of 8 November.

Market Outlook

Key issue going forward lies mainly with the direction and stance of US policies in areas like immigration, trade and foreign relations in view of Trump's anti-immigration, anti-free trade and anti-globalisation rhetoric. This may lead to higher inflation in US as protectionist policies impact the supply chain and cause cost-push price reaction, whilst putting pressure on EM currencies on trade volume disruptions. On the other hand, Trump plans for broad-based tax cuts, increased infrastructure and military spending will lead to stronger US growth and hence lending further support to USD. This may potentially cause further divergence in global monetary policy as US tightens while other regions ease to support their economies. Foreign capital flows into EM could reverse as carry trades unwind as they are deemed unattractive given the rising yields in US, causing EM equities to underperform.

In the near-term, uncertainty has emerged on the Fed's monetary policy direction with the probability of a rate hike in December somewhat reduced marginally. However, in the longer-run, the Fed funds rate may normalise sooner than expected as inflation is driven up by fiscal expansion and infrastructure investment.

Strategy

Against these backdrops, we expect global financial markets to remain highly volatile in the shorter term. Importantly, we will need to have more clarity on Trump's policies to give a better assessment. Only time will tell whether Trump's controversial pledges are carried through after he takes office. Therefore, we advocate a defensive portfolio strategy amidst what remains a trading market in the short term, buying on weakness into names driven by domestic demand and resilient earnings (e.g. domestic consumption and infrastructure plays). We are also inclined to add positions into MYR plays (e.g. exporters) to hedge against the dollar strength.

In terms of bonds, further selling pressure on MGS is possible as MYR is expected to remain weak. However, Malaysian bonds still offer attractive yields compared to developed markets.We expect foreign buying to resume when things are more settled. In conclusion, due to the array of uncertainties, we shall adopt a neutral duration for now.