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WEEKLY INVESTOR RESEARCH

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# The coming Trump Pitch

By Jan Dehn

Brazil's institutions continue to deliver an orderly transition of power as Henrique Meirelles anchors acting President Michel Temer's new economic team. China's loans data is lumpy and the decline in loans largely balances out the sharp rise in the previous month. Philippines President-elect Duterte makes soothing sounds about economic policy. India's Senate prepares to discuss the Insolvency and Bankruptcy bill. In the US, Trump's voting intentions catch up with those of Hillary Clinton. The market has absolutely not priced a possible Trump victory – it is time to give it some thought.

| Emerging Markets | Next year forward PE/Yield | Spread over UST | P&L (5 business days) |
|---|---|---|---|
| MSCI EM | 10.3 | – | -1.12% |
| MSCI EM Small Cap | 11.0 | – | -1.13% |
| MSCI Frontier | 9.0 | – | 0.48% |
| MSCI Asia | 10.7 | – | -1.46% |
| Shanghai Composite | 11.4 | – | -2.95% |
| Hong Kong Hang Seng | 6.3 | – | -2.01% |
| MSCI EMEA | 9.1 | – | -0.69% |
| MSCI Latam | 12.5 | – | 0.07% |
| GBI-EM-GD | 6.46% | – | -0.59% |
| ELMI+ | 4.36% | – | -0.55% |
| EM FX spot | – | – | -0.76% |
| EMBI GD | 5.70% | 397 bps | 0.73% |
| EMBI GD IG | 4.29% | 248 bps | 0.48% |
| EMBI GD HY | 7.67% | 605 bps | 1.03% |
| CEMBI BD | 5.53% | 397 bps | 0.35% |
| CEMBI BD IG | 4.24% | 269 bps | 0.27% |
| CEMBI BD Non-IG | 7.74% | 617 bps | 0.50% |

| Global Backdrop | Next year forward PE/Yield/Price | Spread over UST | P&L (5 business days) |
|---|---|---|---|
| S&P 500 | 15.3 | – | -0.44% |
| 1-3yr UST | 0.77% | – | -0.01% |
| 3-5yr UST | 1.23% | – | 0.09% |
| 7-10yr UST | 1.72% | – | 0.53% |
| 10yr+ UST | 2.56% | – | 1.26% |
| 10yr+ Germany | 0.14% | – | 0.24% |
| 10yr+ Japan | -0.10% | – | -0.93% |
| US HY | 8.07% | 690 bps | 0.48% |
| European HY | 5.01% | 531 bps | -0.28% |
| Barclays Ag | – | 236 bps | 0.21% |
| VIX Index* | 15.84 | – | 1.27% |
| DXY Index* | 94.54 | – | 0.41% |
| EURUSD | 1.1318 | – | -0.57% |
| USDJPY | 108.93 | – | 0.56% |
| CRY Index* | 182.55 | – | 2.64% |
| Brent | 48.9 | – | 11.96% |
| Gold spot | 1282 | – | 1.39% |

Note: Additional benchmark performance data is provided at the end of this document. *See last page for index definitions.

## Emerging Markets

- **Brazil:** Brazil's institutions are performing exactly as they should. In a truly remarkable development, these institutions last week saw Brazil's publicly elected president suspended from office when the Senate voted to commence a formal impeachment trial against Dilma Rousseff. More than two thirds of senators voted in favour of impeachment. The size of the vote matters – in fact only a simple majority had been necessary to commence impeachment hearings, but a two-thirds majority is needed to finally approve impeachment. This vote has to happen within 180 days unless Dilma Rousseff steps down voluntarily. A voluntary resignation could make sense – it would spare the country much grief and might present an opportunity for Dilma to strike a deal to enable her to have a peaceful retirement. Vice-president Michel Temer has now taken over as acting president and Henrique Meirelles, formerly central bank governor, has been appointed as finance minister. This bodes well for economic policy in Brazil going forward. It is also positive that José Serra of the PSDB party has been appointed as foreign affairs minister.

- **China:** Last week's data releases are consistent with a gradual slowdown of the Chinese economy. Monetary data for April was largely in line with expectations, while credit data, notably new loans, slowed significantly. However, the slowdown in loans in April followed months with an extra-ordinarily high issuance of loans in March, so too much should not be read into the month to month volatility. Retail sales, industrial production and fixed asset investment also slowed, partly as a result of the introduction of emission-reducing technology for cars. China has not changed macroeconomic policy – fiscal policy supports the economy as reforms continue to be implemented. CPI inflation was stable in April at 2.3% yoy.

- **Venezuela:** In Venezuela, President Nicolas Maduro declared a 60 day extension to the economic state of emergency that was originally set to expire (and gave Maduro powers to guarantee the functioning of the economy). Bond prices were unaffected and, in fact, were boosted by comments made over the weekend by Vice President of the Economy Miguel Pérez Abad who re-affirmed Venezuela's willingness to pay and

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**Emerging Markets**

suggested a bondholder-friendly re-profiling is still under discussion. Furthermore, China is amenable to renewing its USD 5bn loan and the country is still working to improve the new FX mechanism which would allow for less distortions for the economy. Last but not least, oil prices continue to rise which is supportive for the bonds.

- Philippines: President-elect Rodrigo Duterte has made soothing sounds about economic policy since his recent election victory. Above all, he promised continuity of the macroeconomic policies that have stood Philippines in such good stead for many years. He emphasised tax collection reform and infrastructure spending in a bid to achieve 5% of GDP infrastructure spend. He will also continue to follow policies that encourage foreign direct investment. Government efficiency will be a priority with a focus on addressing bottlenecks, including education. Finally, Duterte said he would aggressively fight corruption. In unrelated news, the central bank adopted a more efficient monetary policy framework with the overnight borrowing rate as the main benchmark interest rate, replacing the repo rate.

- India: The Lower House approved the Insolvency and Bankruptcy Law after recent committee stage approval. The Senate is due to start discussing the bill this week. The bill significantly increases the efficiency of the insolvency framework. April inflation was higher than expected due to surprises in food inflation, while IP slowed in March following a strong print in the previous month. The trade deficit narrowed to USD 5bn in April (seasonally adjusted) from USD 6.9bn in March. In Q4 2012, the trade deficit was a massive USD 17.6bn.

Snippets:

- Argentina: Core inflation in Buenos Aires is beginning to respond to better monetary policies. Core inflation decelerated to 2.8% mom in April from 3.5% mom in March. It will take some time for Argentina to be weaned off Helicopter Money, so inflation will only come down gradually.
- Egypt: S&P changed its outlook for Egyptian foreign currency denominated debt to negative from stable. The rating was left unchanged at B-.
- Chile: The trade surplus declined to 1.1% of GDP in the first four month of 2016 compared to 1.3% of GDP in the same period of 2015.
- Hungary: Growth 0.9% yoy in Q1, much lower than 2.4% yoy expected.
- Malaysia: GDP expanded at a faster than expected pace in Q1 2016. The real economy grew at a 4.2% yoy pace compared to an expectation of 4.0% yoy growth.
- Mexico: IP declined in March by 0.2% mom. The consensus expectation was for a rise of 0.1% mom.
- Peru: The central bank left rates unchanged at 4.25%. The trade deficit narrowed to just 0.4% of GDP in Q1 2016 from 0.6% of GDP in Q1 2015.
- Poland: Poland's growth rate disappointed in Q1. The economy expanded only at a rate of 3.0% yoy. The market has expected 3.5% yoy.
- Romania: April inflation slowed more than expected. The yoy rate of inflation was -3.3% in April versus -2.9% yoy expected.
- Russia: Russia's monthly trade balance increased to USD 7.7bn in March from USD 7.4bn in March and FX reserves increased to USD 392bn from USD 387bn.
- Saudi Arabia: Moody's downgraded the sovereign from Aa3 to A1, which is still comfortably within investment grade territory.
- South Korea: Bank of Korea left rates unchanged at 1.5%. Unemployment declined to 3.7% in April from 3.8% in March.
- Thailand: Bank of Thailand left rates unchanged at 1.5%. Growth accelerated sharply from 2.8% yoy in Q 2015 to 3.2% yoy in Q1 2016.
- Turkey: The current account deficit was narrower than expected (USD 3.68bn vs USD 3.85bn expected).

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## Global backdrop

Broad trends in politics can often be predicted with a reasonable degree of confidence. For example, politics often turns more populistic and nationalistic following major economic crises. Establishment politicians lose courage, initiative and credibility. This happened following the Great Depression and it is happening again now in the developed economies that experienced the crisis of 2008/2009. Having failed to deal with the underlying problems of debt, declining productivity and rising inequality, voters are seeking answers from new politicians.

In the United States, Donald Trump is speaking to a majority increasingly desperate for change, while Hillary Clinton personifies an obsolete and increasingly despised status quo. Riding the rising tide of often ill-defined but nevertheless heartfelt discontent, Donald Trump appears to have the winning pitch and now looks very likely to become America's next president. This is not a prediction, but clearly it is a very possible scenario. Trumps nationwide poll-ratings have nearly caught up with those of Hillary's and Trump has wasted no time in reaching out to House Speaker Paul Ryan, increasing the odds that he can pass laws if he takes the presidency in early November.

Much uncertainty still surrounds Trump. While markets have so far reacted cautiously to his rising political star this is likely to change soon enough. Political analysts, much more so than markets, understand that uncertainty – at least in politics – is a good thing. They look at America and see a country hungry for change, hungry for hope, hungry for winners. And they think Trump can be sold as the embodiment of all three. In other words, the uncertainty that currently surrounds his eligibility to be president is nothing other than a giant gap that can be filled, using careful marketing, to tell a story, to create a myth, to build a business man into a president and to win a nation!

The 'Trump Pitch', the transformation of an eccentric political maverick into presidential material, is just about to hit you. It will be loud enough to reverberate in the markets and it will bring with it lots of trading. Investment banks and the financial media will therefore jump on the bandwagon until the Trump Pitch has a life all of its own. And have no doubt – the pitch will be a bullish one!

Institutional investors should therefore pay attention. Barring some very damaging revelations torpedoing Trump's bid between now and then – and those revelations would have to be very damaging indeed – the Trump Pitch may well be the biggest story in the world by the time of the Republican Convention in July, reaching fever pitch by 8 November 2016 when America goes to the polls.

We have no idea how the transformation of Trump will play out. The future has a habit of hiding itself right up until the last minute. But if we had to paint a picture of the coming Trump Pitch it would evoke Roosevelt's New Deal, designed to speak to all those who dream of a great new American Era.

The Trump Pitch will, of course, feature Trump himself at its very centre, but there will also be substance. We image a vision of six key messages orbiting around Trump's crown, like twinkling stars in the sky:

- The Trump Tone – Reassuring messages from Trump supporters that, as soon as the election is out of the way, their leader's colourful election rhetoric will be scaled right back and dismissed as just that, rhetoric. The new tone, we will be told, will be presidential, dignified, inclusive and sober.
- Trump for Growth – The one big economic idea out there screaming to be usurped is a giant nationwide infrastructure programme to push America back to winning ways. Expect Trump to latch on to it with big fiscal stimulus, promises of amazing productivity gains and lots and lots of new jobs. And stocks, we will be told, will love it.
- Trump the Financier – Trump will surely play the financial 'doh' card to great acclaim, even from the 'Krugmanites' of this world. Low US treasury yields are there to be used! Trump will place trillions in infrastructure bonds with US pension funds and the Fed, aided when needed by Helicopter Money.
- The Trump & Ryan Show – Trump will of course win over Republican hearts. It will soon be clear that Trump and Ryan both agree on the need to massively downsize the government bureaucracy in Washington (while creating new jobs for the laid-off in Trump's infrastructure programs).
- Trump for America – Trump will tell you that international trade deals never won anyone a vote in America. But vilifying foreigners sure does. Trump's America is a country that turns its attention on itself, but in so doing also fights less. Unless events absolutely demand American retribution there are likely to be fewer wars under Trump. And, footnote, Mexicans are welcome after all.
- Trump's Dollar Dump – An early Dollar rally on hopes for a bright new future under Trump quickly comes to grief when confronted with realities of yet more debt and Helicopter Money – but to everyone's surprise the weaker Dollar (and higher inflation) turn out to be great for US and global growth.

QE has been mistaken for recovery in developed economies for more than half a decade. The truth is that markets love a good story. Fiction, good narratives, fairy tales, they all move markets. The Trump Pitch could do the same, even if it is, for now, merely fiction on our part. If indeed the Trump Pitch does become reality, the biggest challenge investors will face will not be to jump on the associated bandwagon, but rather, it will be to decide what kind of reality will play out once the most controversial presidential candidate in recent times takes the oath of office. It is entirely up to you decide that for yourself.

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## Benchmark performance

| Emerging Markets | Month to date | Year to date | 1 year | 3 years | 5 years |
|---|---|---|---|---|---|
| MSCI EM | -5.17% | 0.79% | -20.83% | -6.04% | -4.39% |
| MSCI EM Small Cap | -4.01% | -1.62% | -17.76% | -4.25% | -3.10% |
| MSCI Frontier | 1.16% | 3.19% | -10.79% | 1.03% | 1.43% |
| MSCI Asia | -4.56% | -3.77% | -20.39% | -2.27% | -1.15% |
| Shanghai Composite | -3.75% | -20.07% | -34.36% | 10.91% | 2.17% |
| Hong Kong Hang Seng | -7.14% | -14.05% | -38.24% | -5.75% | -5.21% |
| MSCI EMEA | -7.66% | 8.32% | -21.80% | -9.71% | -7.05% |
| MSCI Latam | -5.66% | 19.20% | -18.02% | -14.05% | -10.15% |
| GBI EM GD | -3.46% | 9.93% | -5.25% | -7.97% | -2.58% |
| ELMI+ | -2.06% | 4.20% | -4.71% | -4.57% | -2.99% |
| EM FX Spot | -3.32% | 3.42% | -11.73% | -11.97% | -9.31% |
| EMBI GD | 0.36% | 7.29% | 5.31% | 3.29% | 6.14% |
| EMBI GD IG | 0.21% | 7.24% | 4.06% | 2.55% | 5.32% |
| EMBI GD HY | 0.54% | 7.18% | 6.86% | 4.22% | 7.34% |
| CEMBI BD | 0.30% | 6.00% | 2.97% | 3.11% | 4.99% |
| CEMBI BD IG | 0.43% | 4.80% | 3.25% | 3.38% | 5.35% |
| CEMBI BD Non-IG | 0.09% | 8.08% | 2.20% | 2.36% | 4.33% |

| Global Backdrop | Month to date | Year to date | 1 year | 3 years | 5 years |
|---|---|---|---|---|---|
| S&P 500 | -0.77% | 0.96% | -0.32% | 10.08% | 11.22% |
| 1-3yr UST | 0.12% | 1.18% | 1.11% | 0.67% | 0.70% |
| 3-5yr UST | 0.39% | 2.71% | 3.19% | 1.96% | 2.09% |
| 7-10yr UST | 1.02% | 5.49% | 7.18% | 3.30% | 5.43% |
| 10yr+ UST | 2.42% | 9.96% | 14.32% | 6.87% | 10.05% |
| 10yr+ Germany | 2.76% | 10.59% | 11.11% | 9.79% | 11.45% |
| 10yr+ Japan | 0.21% | 12.78% | 18.43% | 8.95% | 7.46% |
| US HY | -0.27% | 6.90% | -2.17% | 2.07% | 5.47% |
| European HY | -0.60% | 3.35% | 1.03% | 5.71% | 8.80% |
| Barclays Ag | 0.39% | 4.85% | 4.35% | 3.53% | 4.99% |
| VIX Index* | 0.89% | -13.01% | 27.95% | 21.19% | -13.16% |
| DXY Index* | 1.56% | -4.15% | 1.51% | 13.10% | 25.27% |
| CRY Index* | -1.12% | 3.64% | -21.13% | -36.23% | -45.80% |
| EURUSD | -1.12% | 4.26% | 0.03% | -12.14% | -20.05% |
| USDJPY | 2.35% | -9.27% | -9.21% | 6.53% | 34.83% |
| Brent | 1.50% | 31.04% | -26.88% | -52.94% | -56.67% |
| Gold spot | -0.89% | 20.74% | 4.57% | -7.54% | -13.95% |

*VIX Index = Chicago Board Options Exchange SPX Volatility Index. *DXY Index = The Dollar Index. *CRY Index = Thomson Reuters / CoreCommodity CRM Commodity Index.
Source: Bloomberg, JP Morgan, Barclays, Merrill Lynch, Chicago Board Options Exchange, Thomson Reuters, MSCI, total returns.
Figures for more than one year are annualised other than in the case of currencies, commodities and the VIX, DXY and CRY which are shown as percentage change.

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