

INVESTMENT NOTE

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TRUMPONOMICS 2.0



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The eyes of the world were glued on the United States last week, and for once, the Federal Reserve's policy meeting was completely overshadowed by other events. In a conclusive victory, Donald Trump and the Republicans now have a mandate to implement their agenda over the next four years. Even so, slightly less than half the country will be very unhappy with the outcome. If the Democrats had squeezed out a win, the other half would be distraught. The deep political and social divisions are not getting any better, which is worrying since the US remains the world's largest economy and most important military power.

For now, however, let's focus on the investment implications. The initial market response was for the dollar to rally, US bonds to sell off (sending yields higher) and for equities to jump. Unlike in 2016, this election outcome did not come as a complete surprise and markets were broadly positioned for a Republican win. The speed with which the results were finalised was also positive. Markets hate uncertainty, and a drawn-out or contested result would have weighed on sentiment. In other words, while there were some notable market moves, all in all the past week does not stand out as being unusually volatile.

TARIFFS, TAXES AND MIGRANTS

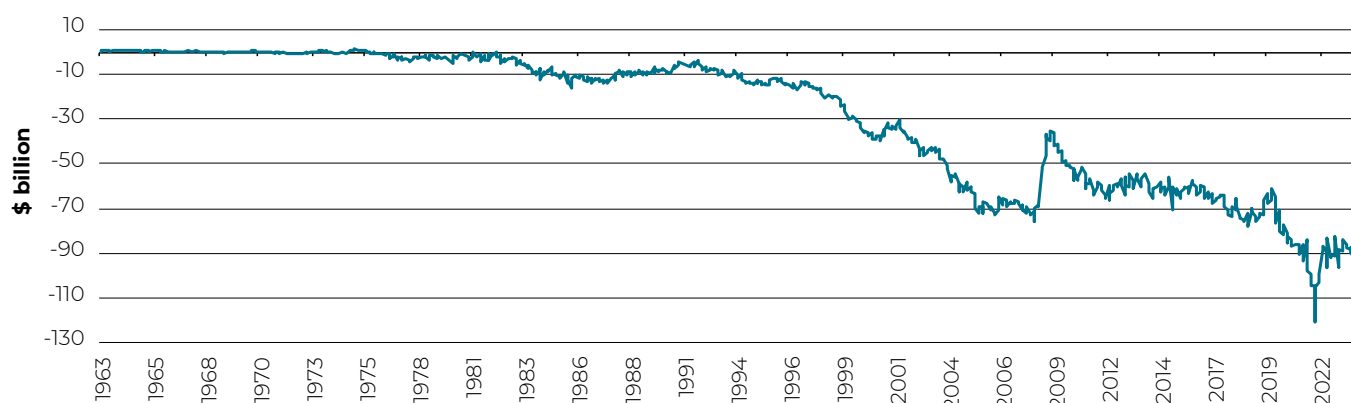
Looking ahead, Trumponomics has three broad policy elements. Firstly, he has promised tariffs on imports coming into the US, especially from China. Trump views importing from other countries as "losing", in contrast to the orthodox economic view that trade benefits both parties. Moreover, high levels of US imports are not a sign of economic weakness any more than China's export performance is an unambiguous sign of strength. China runs massive trade surpluses partly because domestic

demand is suppressed, while the US trade deficit partly reflects strong domestic demand. The US consumer is still on a roll. And while the US imports goods from abroad, it sells financial assets to foreigners, running a capital account surplus. To oversimplify, the US imports Apple phones and Nike shoes, but sells Apple and Nike shares to the rest of the world. It is no surprise then that the trade deficit did not narrow during Trump's first term, nor that it is hovering near record levels today.



WEALTH

CHART 1: US GOODS TRADE BALANCE



Source: LSEG Datastream

The threat of big tariff hikes is likely partly a negotiation tactic to get concessions from trading partners, but some tariff increases are coming. The only question is who gets hit and by how much. China will likely be the main target, but Trump has spoken of across-the-board import tariffs, hitting friend and foe alike. The intention behind the tariffs will be to discourage imports and allow US manufacturers to compete, and also to avoid Chinese trade being re-routed through friendly countries such as Mexico and Vietnam. It should be noted that the tariffs Trump imposed on China in his first term were largely kept in place by Joe Biden, his successor, a rare bipartisan policy consensus.

Exchange rates are likely to adjust to partly offset the impact of new tariffs. So, for instance, if a 10% tariff is placed on Brazilian imports, we could expect the Brazilian real to weaken and the dollar to strengthen. However, it is hard to see China allowing its currency to weaken by 60%, the tariff rate Trump proposed. Therefore, the impact must be absorbed by producers in China in the form of price cuts, or by importers like Walmart or Target in the form of reduced margins. Otherwise, the end customer will be paying more at the till.

Where it gets interesting is that Trump also wants a weaker dollar to support American exports. The dollar is of course already strong. But he cannot have both. Widely implemented tariffs will probably push the dollar higher, unless some large-scale offsetting action is taken.

Secondly, he is anti-immigration. Immigration is a political hot potato the world over, including in South Africa. Practically speaking, it is going to be difficult to deport millions of undocumented immigrants as promised, but we should expect immigration rates to decline. The problem is that the US economy needs migrant workers, as the native-born labour force is not growing anymore. We could therefore see firms running out of workers in the years ahead, which can put upward pressure on wages and possibly inflation.

Ironically, it might also give fresh impetus to shifting production to other countries where labour remains abundant and cheap, the exact opposite of what he wants. Similarly, some of Trump's other proposed policies could also end up at cross purposes with one another, which means we need to be sceptical of people who claim to know exactly what will play out over the next four years.

Finally, he favours lower taxes and deregulation. His 2017 tax cuts were due to expire in 2025 and are now likely to be extended, while corporate tax rates might be lowered even further. Lower tax rates and deregulation are positive for company profitability, at least in the short run, and is therefore good for the stock market. Bank shares, in particular, surged last week on anticipation that onerous capital requirements will be eased, and more mergers and acquisitions will be approved.

Any additional tax cuts will have to be funded by additional borrowing, unless there are spending cuts, which seem unlikely. The federal government's debt will therefore continue to rise, possibly by several trillion more on top of pre-Trump estimated trajectory. No surprise then that we've seen upward pressure on US bond yields.

The US economy is already growing faster than estimates of its long-term potential growth rate of around 2% and does not need additional fiscal stimulus today. However, since new tax cuts are only likely to arrive in 2026, much will depend on the state of the economy then. It might add some welcome oomph to an already cooling economy, or it could be the fuel that causes it to overheat. We'll only know when we get there.

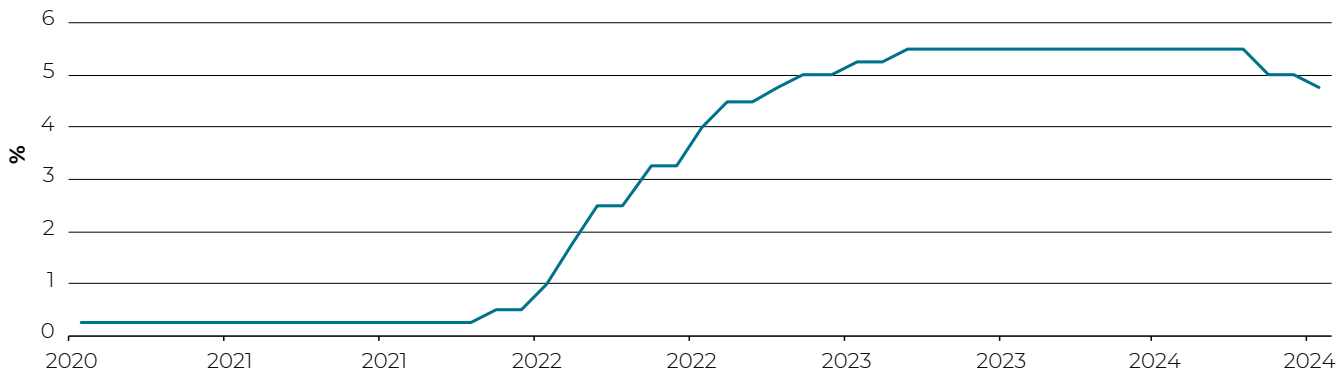
Then again, we should also remember that markets have a way of disciplining wayward politicians and moves in bond yields and/or the dollar could rein in Republican ambitions somewhat. Nothing is cast in stone today, and the old political saying of "campaign in poetry, govern in prose" could still apply.

FED DOWN, FED UP?

How does this impact monetary policy? Simply put, if the Fed fears that the inflation outlook will deteriorate due to tariffs pushing up prices or immigration restrictions lifting wages, it could be more circumspect in cutting interest rates. As with the tax cuts, the economic impact could take some time to materialise. For now, therefore, the Fed is still on a path to reducing rates. Market expectations for future

rate cuts have been scaled back considerably, however. Following last week's 25 basis point interest rate reduction, money markets are only pricing in slightly more than 100 basis points in additional cuts. This is almost 100 basis points less than was expected in late September, with the market now pricing in a Fed policy rate of 3.6% at the end of 2026.

CHART 2: US FEDERAL RESERVE POLICY INTEREST RATE, %

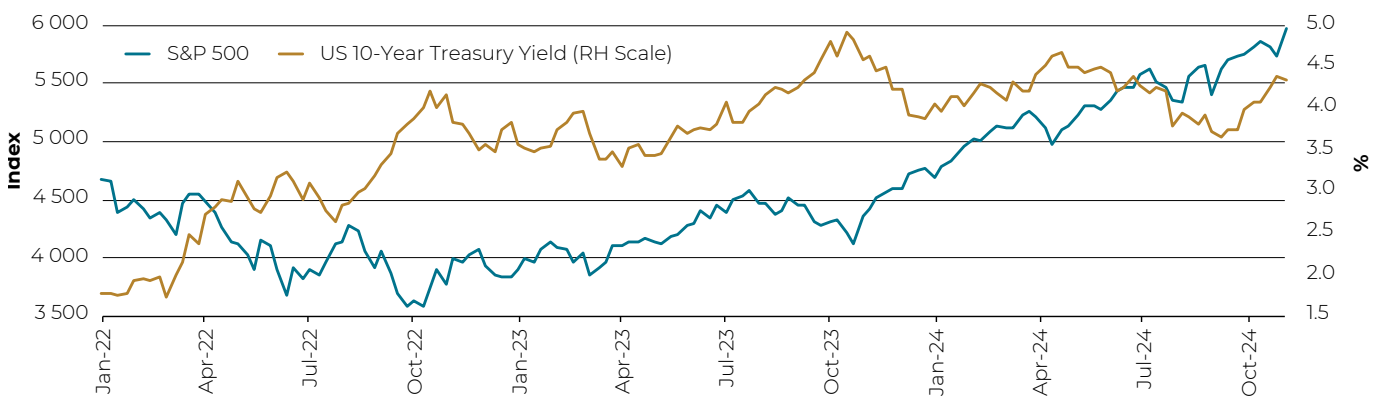


Source: LSEG Datastream

This could still change, of course, but for now the main point is that short-term rates are still declining in the US and most other major economies (the Bank of England and the Swedish Riksbank also cut rates last week).

If bonds yields keep rising, however, it will offset some of the impact of Fed cuts. After all, mortgage rates are linked to long bond yields, as are many types of loans to corporates. To use the finance jargon, financial conditions could tighten, instead of loosening as intended.

CHART 3: US BONDS AND EQUITIES



Source: LSEG Datastream

In an extreme scenario, the Fed could start hiking again if it sees signs of rising inflation and economic overheating. This is unlikely, but not impossible. Another complicating factor is that Jerome Powell's term in office as Fed chair expires in May 2026. Trump could very well try to replace him with someone who is more pliant. This would hurt the Fed's independence, but not completely undermine it since other top officials' terms expire much later, while the regional Federal Reserve bank chiefs are not appointed by the president. Nonetheless, it would mean that the US loses

monetary policy credibility at the same time as its fiscal credibility has already deteriorated. This could start shaking the foundations of global finance.

Meanwhile, the challenge for Powell and his colleagues is that they can only make decisions based on the current inflation and employment outlook and cannot pre-empt a Trump presidency's policies until they are implemented. "We don't guess, we don't speculate, and we don't assume," is how Powell described the approach.

GEOPOLITICAL UNCERTAINTY

In terms of geopolitics, it will very much be “America First”. We can expect Trump to put pressure on Ukraine to start negotiations with Russia, while ramping up support for Israel in its war with Hamas, Hezbollah and Iran. While he is hawkish on China, he is less likely to stand up for Taiwan. In other words, while his supporters tout his toughness on a global stage, he could end up emboldening the US’s big strategic rivals, Russia and China, rather than reining them in, especially if he undermines the traditional alliances the US has with Europe, Japan and others.

At the same time, the leaders of China and Russia probably also see him as someone they can do a deal with. This could ironically make the world safer, but only in the shorter term. One thing is certain: it creates a challenging foreign policy environment for countries caught in the middle, like South Africa. Navigating these turbulent waters will require great diplomatic skill on our part.

SOUTH AFRICA

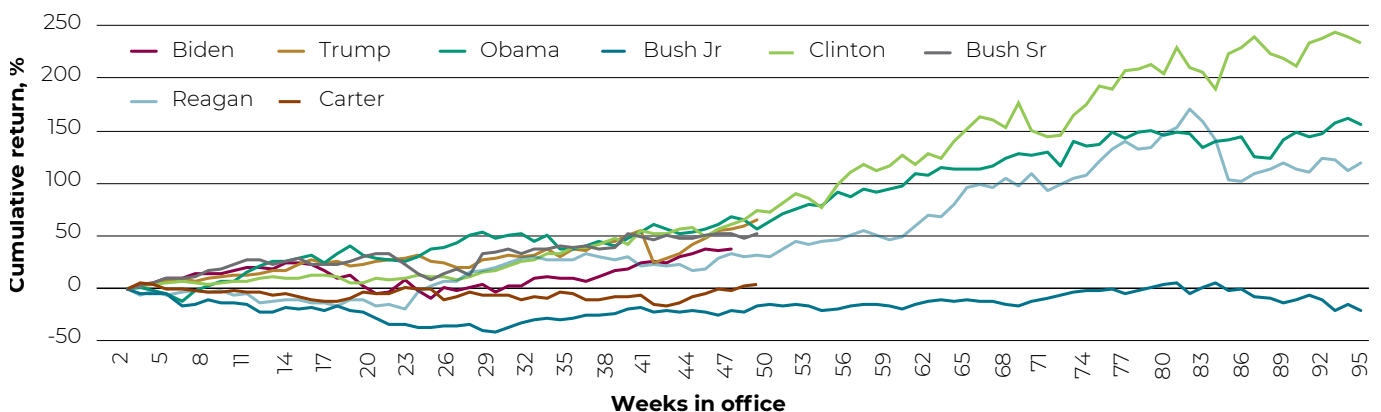
Which brings us back home. We don’t know yet if the incoming Trump administration will impose tariffs on imports from South Africa too. Attempts to retain duty-free access under the African Growth and Opportunity Act (AGOA) will almost certainly be complicated.

The outlook for SA Reserve Bank interest rate cuts has not changed, though it will proceed with caution given the greater uncertainty about the path of US monetary policy. It helps that the rand has been remarkably resilient, only experiencing a brief wobble on the day the election results were released. South Africa should remain on the road of

economic reform so that we can become more reliant on internal growth drivers in an uncertain global environment.

For instance, if there is to be further upward pressure on global bond yields, we should expect spillover to domestic markets, i.e. higher local bond yields. This makes it important to continue fiscal consolidation efforts and improve our relative standing in the eyes of investors. Securing credit ratings upgrades could help, as well as getting off the Financial Action Task Force’s grey list. Doing so is fully in our own hands, not in Trump’s.

CHART 4: US S&P 500 REAL TOTAL RETURNS PER PRESIDENTIAL TERM



Source: LSEG Datastream

In conclusion, a Trump presidency is therefore not entirely good or bad for investment portfolios. There will be winners and losers across different sectors of the global economy and across different asset classes. It is easy to overstate the impact where we stand today. Historically, for instance, the US stock market has performed well irrespective of which party controlled the White House, as chart 4 shows. The two terms of George W. Bush were an exception, given that they coincided with the dotcom crash at the start and the financial crisis at the end.

Nonetheless, the experience of Trump’s first term suggests things could be more volatile with policies changing at short notice. This will require more patience on the part of investors. The focus should not be on trying to second guess everything Trump says or does, but rather on appropriate portfolio diversification and sticking to the investment plan for what will undoubtedly be four eventful years.

EQUITIES - GLOBAL

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
Global	MSCI World	US\$	3 791.0	3.58%	3.95%	19.63%	31.27%
United States	S&P 500	US\$	5 996.0	4.66%	5.10%	25.70%	36.80%
Europe	MSCI Europe	US\$	2 075.0	-1.84%	-0.86%	2.72%	14.01%
Britain	FTSE 100	US\$	10 428.0	-1.30%	-0.31%	5.91%	14.68%
Germany	DAX	US\$	1 773.0	-1.28%	-0.89%	11.35%	23.99%
Japan	Nikkei 225	US\$	258.8	4.02%	0.67%	9.05%	21.45%
Emerging Markets	MSCI Emerging Markets	US\$	1 136.0	1.25%	1.43%	10.94%	18.58%
Brazil	MSCI Brazil	US\$	1 396.0	1.53%	-0.71%	-22.44%	-13.77%
China	MSCI China	US\$	67.7	1.84%	2.90%	22.03%	18.09%
India	MSCI India	US\$	1 054.4	-1.04%	-0.53%	14.36%	28.90%
South Africa	MSCI South Africa	US\$	479.0	-1.24%	0.42%	15.42%	24.42%

EQUITIES - SOUTH AFRICA (TOTAL RETURN UNLESS INDICATED OTHERWISE)

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
All Share (Capital Only)	All Share (Capital Index)	Rand	85 125.0	-1.25%	-0.30%	10.71%	17.47%
All Share	All Share (Total Return)	Rand	15 517.0	-1.24%	-0.30%	14.50%	21.82%
JSE Capped SWIX	Capped SWIX (Total Return)	Rand	37 993.7	-1.22%	-0.29%	14.50%	22.58%
TOP 40/Large Caps	Top 40	Rand	13 880.0	-1.43%	-0.46%	12.75%	19.67%
Mid Caps	Mid Cap	Rand	25 636.0	-0.99%	-0.08%	17.67%	29.52%
Small Companies	Small Cap	Rand	41 365.0	-0.40%	-0.05%	26.65%	36.27%
Resources	Resource 20	Rand	5 023.1	-3.22%	-2.31%	3.32%	7.05%
Industrials	Industrial 25	Rand	25 210.0	-1.72%	-0.70%	13.54%	19.05%
Financials	Financial 15	Rand	16 061.0	0.26%	1.15%	24.40%	35.95%
Listed Property	SA Listed Property	Rand	2 340.9	-0.99%	-0.60%	25.58%	44.95%

FIXED INTEREST - GLOBAL

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
IBOXX Global Government S&P Overall (USD Unhedged)		US\$	75.6	0.01%	-0.28%	-3.62%	2.74%

FIXED INTEREST - SOUTH AFRICA

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
All Bond	BESA ALBI	Rand	1 084.4	1.25%	1.00%	15.31%	19.59%
Government Bonds	BESA GOVI	Rand	1 067.6	1.23%	0.99%	15.17%	19.48%
Inflation Linked Bonds	BESA CILI	Rand	366.8	-0.59%	-0.77%	5.04%	8.56%
Cash	STEFI Composite	Rand	588.0	0.15%	0.17%	7.28%	8.52%

COMMODITIES

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
Brent Crude Oil	Brent Crude ICE	US\$	73.9	1.05%	1.19%	-4.06%	-7.66%
Gold	Gold Spot	US\$	2 685.0	-1.86%	-3.52%	30.15%	36.43%
Platinum	Platinum Spot	US\$	968.0	-2.52%	-4.06%	-1.93%	11.65%

CURRENCIES

DESCRIPTION	INDEX	CURRENCY	INDEX VALUE	WEEK	MONTH-TO-DATE	YEAR-TO-DATE	1 YEAR
ZAR/Dollar	ZAR/USD	Rand	17.58	0.54%	0.17%	4.12%	5.09%
ZAR/Pound	ZAR/GBP	Rand	22.71	0.48%	-0.04%	2.60%	-0.09%
ZAR/Euro	ZAR/EUR	Rand	18.84	1.57%	1.62%	7.19%	4.96%
Dollar/Euro	USD/EUR	US\$	1.07	0.93%	1.68%	3.18%	0.00%
Dollar/Pound	USD/GBP	US\$	1.29	0.02%	-0.14%	-1.69%	-4.78%
Dollar/Yen	USD/JPY	US\$	0.01	-0.21%	0.40%	8.24%	1.11%

Source: I-Net, figures as at 8 November 2024

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WEALTH

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