Trump Victory Brings Outsider to White House; Expect Volatility, But U.S. Economy in Good Shape

The election of Donald Trump to become the 45th President of the United States is historic in that it will bring a political outsider to the White House, which is expected to bring heightened uncertainty to the governing process. Despite polls that had tightened in recent weeks, Mr. Trump's victory must be considered a stunning upset as most major polls and odds makers were predicting a win by Hillary Clinton. As of this writing, Secretary Clinton could still win the popular vote but Mr. Trump has secured the necessary 270 Electoral College votes necessary to win the nomination. In addition the Republicans have retained control of both the Senate and House of Representatives. While a Trump Presidency brings elevated uncertainty to the markets, particularly with respect to international trade and immigration, he is considered a pro-business candidate who supports lower taxes, reduced regulation, and energy independence. **Historically, the U.S. economy has proven to be very resilient throughout election cycles and Presidential transitions and we believe that the economy is well positioned to sustain ongoing GDP growth, driven by job creation, solid consumer spending and business investment. In addition third quarter earnings have trended above expectations, giving us more confidence about sustained earnings growth in the fourth quarter of 2016 and in to 2017. While we expect market volatility as Mr. Trump communicates his political and economic strategies to begin his Presidency, we would use market weakness to add to positions in quality companies trading at discounted valuations. We urge investors to remain diversified and stay true to long term investment objectives.**

Equity market reaction this morning has been surprisingly mild, given an extreme decline in the overnight futures markets. However, as we begin the day, the U.S. economy is underpinned by solid fundamentals, which have not changed overnight. Market leadership today has come from Health Care, Financials, and Industrials, while Utilities, Consumer Discretionary, Consumer Staples, and Technology are weaker. Health care has rallied has investors anticipate more support for the group if President Trump scales back the threat of increased regulation and drug price controls. Financials are higher as interest rates have spiked higher with the U.S. 10-year treasury yield at 1.97%, up from 1.85% on Tuesday. Industrials have rallied, we believe, due to Mr. Trump's commitment to support massive infrastructure in the U.S., and on a surge in defense stocks. We attribute weakness in Utilities to concern about support for alternative energy as many utilities have invested in non-fossil fuel solutions. Consumer Discretionary weakness appears to be some trader caution regarding consumer confidence, which will play out over the next several weeks as Mr. Trump communicates plans to unite the country. Consumer Staples stocks tend to be significant exporters and would be vulnerable to international trade wars, which are perhaps the biggest uncertainty for the markets under a Trump Presidency, in our view. Finally, we attribute Technology weakness to trade uncertainty as well as many of the U.S. tech leaders generate substantial sales and have manufacturing relationships outside the U.S.

We continue to view the U.S. economy positively. Third quarter advanced GDP was recently reported at +2.9%, well above Q2 +1.4% and Q1 +0.8%. Growth was driven by consumer spending, business investment, exports, and government spending. In addition, the latest update from the Atlanta FED's GDPNow Forecast estimates 4Q16 growth of 3.1%, from early Q4 data that has already been reported. Consumer spending, as measured by year/year PCE has increased at least 3.5% each month since March 2016, Average hourly earnings increased 2.8% in October, the highest monthly year/year increase since 2009.

In our view, President Trump can instill increased investor confidence by communicating his lower taxes, reduced regulation, rebuild infrastructure message and toning down the rhetoric about protectionist trade policies, which remain a risk to the market in our view. We look for continued growth in U.S. GDP and corporate earnings and believe that equities can trade higher from current levels.

James D. Ragan, CFA
Director of IIG Research
(206) 389-8000
www.davidsoncompanies.com/indv