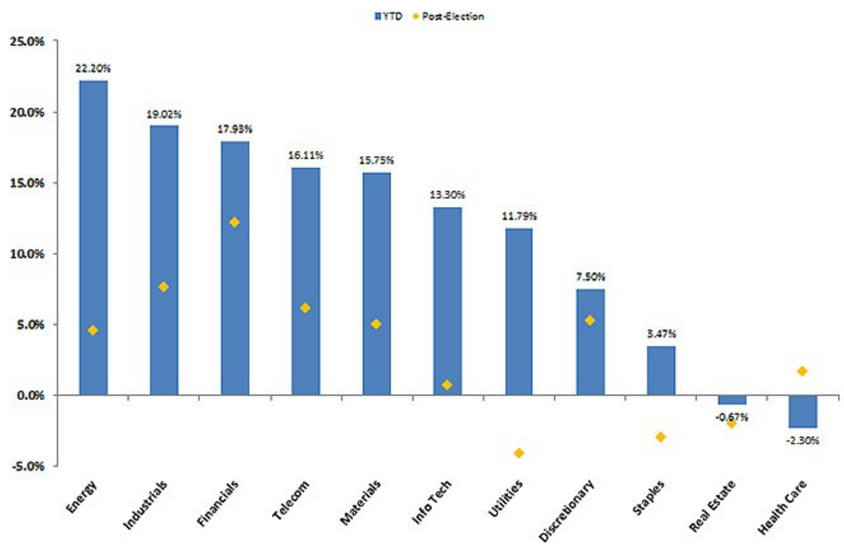
TRUMP CARD

19/12/2016

What an eventful quarter we've seen in equity markets. Donald Trump's election has brought unloved stocks back into favour, given the likelihood of tax cuts, infrastructure spending and a period of rising interest rates.

The turnaround has been most pronounced for the financials sector, up 11% and the strongest post-election performer in the US. By contrast, sectors like utilities and consumer staples have weakened, down 6% and 4.5% respectively.*

US Equity Market Sector Performance, as of November 25, 2016



Source: Factset sourcing the S&P 500 Index.

TRUMP CARDS TAKE PATIENCE

As value investors, we take positions in undervalued stocks and sectors around the world, waiting patiently for normalisation to occur. The US financials sector is just one example – we've held Wells Fargo since the inception of Perpetual's Global Share Fund six years ago. A little over a year ago, we bought back into Bank of America.

I didn't expect President-elect Trump to be the catalyst that would re-rate Bank of America to a more fair valuation, but that's what happened and the stock has rallied from $16 to $20 in the past month, along with other US financials.

No-one has a crystal ball to predict how the political results and world events of the future will affect share prices. We can't predict the future, but as value investors we can take advantage of the present by identifying and investing in companies that are undervalued.

We have taken the opportunity to trim our positions in Bank of America and Wells Fargo post the rally, but we still believe they are wonderfully positioned banks in a potential period of rising interest rates and fiscal stimulus.

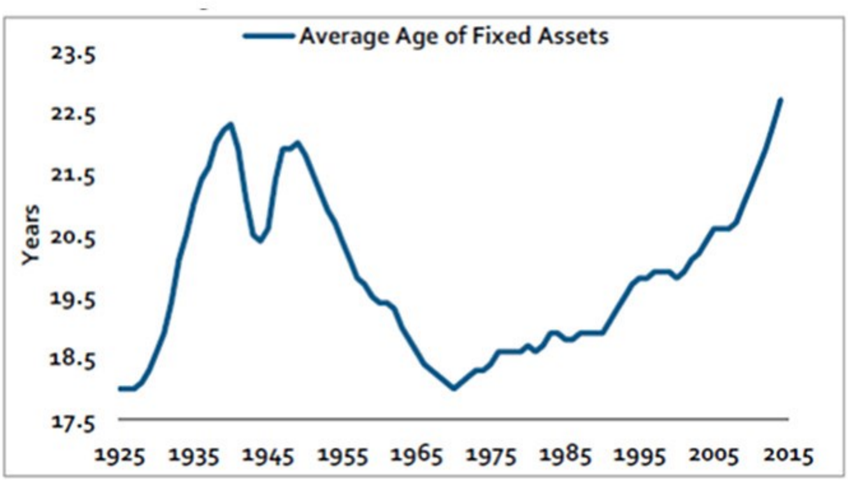
AN EYE ON INFRASTRUCTURE

There are no guarantees as to what US policy changes President Trump will be able to make as they still need to be approved by Congress. Having said that, I think there is a general acceptance that monetary policy has been ineffective at stimulating economic growth and the focus will now turn to expansionary fiscal policy in the form of tax cuts and infrastructure spending.

It will be interesting to see whether other global economies shift their policies to this approach. Australia is in much need of infrastructure investment as the population grows and I'm sure many other countries are as well.

In the US, the average age of fixed assets recently peaked at 22.5 years, compared to 18.5 years 30 years ago. This highlights how the US has underinvested in their infrastructure.

Age of Fixed Assets, as of year-end 2015



Source: Haver Analytics, Bureau of Economic Analysis (BEA), Morgan Stanley Wealth Management GIC

CORPORATE TAX CUTS WILL BENEFIT MULTINATIONALS

Mr Trump wants to cut the corporate tax rate to 15% in the US and allow corporates to bring back cash held offshore without having to pay a large amount of tax. This will be a boon for US corporates.

If it happens I think it will lead to an increase in mergers and acquisitions in the US, which will be a great benefit for multinationals with large cash balances offshore. We own a number of companies that will benefit from this policy including Alphabet, IBM, Oracle and Apple.

THREATS TO STIMULUS

I will be keeping a keen eye on the extent of the new President's protectionist policies, which could threaten economic stimulus in 2017. The key area of concern is his policy on global trade and whether he will place tariffs on imports from certain countries.

I don't think he will want to hurt the free trade of goods in and out of the US. While he has been vocal about his concerns regarding China devaluing their currency, I don't think this will affect the success of companies in the Asian region and we are still comfortable with our positions in Asia.

**Source: Bloomberg and Factset*