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## *The Intelligent Investor—November 2016*

### **Quick Thoughts:**

As I tucked my daughter in on election night, I thought about the various outcomes for the elections for both the President and Congress. While I won't bore you with my personal political commentary, I will tell you that the thought of the first woman president being elected right after my daughter's first birthday seemed special. When I tucked her in, it seemed a foregone conclusion.

Let's just say it was a long morning for anyone in finance, and for me particularly! I watched President Elect Trump's speech, grabbed a couple hours of shut eye and was up early reviewing market commentaries, strategist notes, and portfolio positioning. The futures market, which I assume most of you don't follow, reacted violently with the DOW falling over 900 points due to Trump's victory. For those of you that are curious, the futures market is the trading that goes on aftermarket hours and indicates how the market will open. All of that being said, as I currently stare at the television in my office I am happily looking at green arrows for US markets.

**Table 1: Key Index Returns**

	MTD %	YTD %	3-year* %
<b>Dow Jones Industrial Average</b>	-0.9	+4.1	+5.3
<b>NASDAQ Composite</b>	-2.3	+3.6	+9.8
<b>S&amp;P 500 Index</b>	-1.9	+4.0	+6.6
<b>Russell 2000 Index</b>	-4.8	+3.7	+2.4
<b>MSCI World ex-USA**</b>	-2.0	-1.5	-4.0
<b>MSCI Emerging Markets**</b>	+0.2	+14.0	-4.4

Source: Wall Street Journal, MSCI.com

MTD returns: Sep 30, 2016—Oct 31, 2016

YTD returns: Dec 31, 2015—Oct 31, 2016

\*Annualized

\*\*in US dollars

## **Trump Opportunity**

### *Infrastructure*

The president-elect has talked about an infrastructure plan of what could be at least \$500 billion, based on his informal pledge to roughly “double” what his opponent campaigned on. While many in the nation’s capital are skeptical, this effort may well include some version of a border wall intended to staunch the flow of immigrants across the southern border of the U.S., a centerpiece of his campaign. In theory, the U.S. could even give Mexico loan guarantees to borrow at very low interest rates to assist in its construction, thus making good on Trump’s promise to have Mexico “pay” for the wall. Such a huge project might come to be seen as a Keynesian-style jobs program on both sides of the border. Meanwhile, the same drive that led Trump to put his name on skylines in New York and elsewhere seems likely to inspire the new president to embrace an infrastructure agenda that would leave his legacy imprinted on any number of new or repaired roads, bridges, tunnels, seaports, airports, sewer systems, electric grids and more. If a stimulus of the size he’s discussed were to be dispersed over a five-year time frame, it could add up to half a percentage point to gross domestic product annually over the period.

### *Taxes: Lower rates for Corporations and Workers*

Those infrastructure projects could be partially paid for through a corporate tax overhaul. Any such deal would likely include a provision to repatriate the estimated \$2 trillion of U.S. corporate earnings trapped overseas by taxing it on a one-time basis at a roughly 10% rate. This could entice companies to bring the cash back to the U.S.

Most Republicans and Democrats agree that the U.S. corporate tax code needs reform. That makes it a prime candidate for bipartisan agreement and a potent early chance for Trump to showcase his negotiating skills. During his campaign, he pledged to cut the top marginal corporate tax rate to 15% from 35%, which should have the desirable side effect of curbing inversions — transactions that allow a U.S. company to merge with an overseas firm and pay a lower tax rate in the latter’s country. This practice has become popular over the past several years, much to the dismay of policymakers.

Trump has also pledged to dramatically lower personal income tax rates. If Trump has his way in the reconciliation process, the resulting blueprint — which would also include substantial defense increases — would spell higher budget deficits in the near-term.

More traditional Republican entitlement reformers, like Paul Ryan, will likely seek assurances from Trump that he’ll return to these long-term concerns within a few years.

### *Trade: Considerable Changes could be Coming*

A president has more unilateral power to make changes to current trade arrangements than is commonly understood. That means President-elect Trump could rewrite deals to be tougher on trade partners — or use the threat of U.S. withdrawal from existing deals

as a negotiating ploy to force changes in areas he deems important. While the Washington establishment fears Trump will lead us into a destructive and recession-inducing trade war, that's hardly guaranteed. It seems more likely that Trump would see his and the country's interests better served by a posture that flexed some unused trade muscles to arrive at better terms at the margins. In particular, Trump has pledged to revise the North American Free Trade Agreement, which was signed by his opponent's husband, President Bill Clinton, in 1993. He would also kill the Trans-Pacific Partnership, a result that would hurt America's prestige in the region. Finally, Trump has called for tougher rules on trade with China, who he says has taken advantage of U.S. trade negotiators for years. He could also attempt in various ways to crack down on U.S. firms that move jobs, plants or operations overseas.

### *Health Care: Repeal of Obama Care?*

Although Trump has been vague about his precise plans for health care, he has campaigned on repealing the Affordable Care Act (ACA). Most observers believe, however, that it would be politically disastrous to simply cancel coverage for the 20 million Americans who've gotten health coverage under the ACA. So, it's likely that the GOP plan to "repeal and replace" the law will ultimately be implemented as a kind of "repeal and rebrand" — i.e., some scaling back of subsidies and regulations Republicans find excessive while nonetheless holding the vast majority of current ACA beneficiaries harmless. During the transition, there may be market jitters for hospital and health plans that depend on the ACA's subsidies and related supports. In the end, however, they should be able to flourish even after a GOP revamp. During his campaign, Trump also criticized high drug prices, saying the government needs to be a stronger negotiator with pharmaceutical firms. If he follows through, that could mean a push for the government to exert its pricing power through Medicare, Medicaid and its other programs. However, the GOP more broadly is not aligned with Trump on the idea of direct price negotiations, so the outcome for now remains unclear.

### *Looser Fiscal Policy: Defense Spending Increases*

Trump has called for major defense spending increases, which would probably include beefing up defensive homeland security as well as offensive capabilities. That could signal something of a reversal from the Obama administration, which allowed defense spending to decline. Of course, if growth for such expenditures picks back up, it would be welcome news to big defense contractors in industries like aerospace.

### *Long Term View*

Over the long run, the U.S. economy is likely to remain one of the strongest globally no matter who resides in the White House. Nevertheless, the president has the power to execute policy changes that can move markets. While these five areas are some of the most significant in which the president-elect hopes to make changes, he and the new

Congress can affect the economy in other ways as well. For example, Trump has said he'll roll back 2010's Dodd-Frank financial regulation law. Trump has also said that he would pull out of the Paris climate deal and undo environmental regulations to promote fracking and the coal mining industry. That could have a negative impact on renewable energy companies and a positive one on fossil fuel firms. These steps would also be highly controversial. In the end, a Trump administration means a significant shift in Washington policy for at least the next four years. That could worry markets initially as they wait to see how a Trump presidency actually takes shape.

## Epilogue

I know that for some of you, this year's election has been particularly difficult. You are concerned about the direction of the nation, and you fear the leadership that will take the helm next year won't be in the country's best interest.

I won't comment on the many pressing issues of the day politically, but I will leave you with a quote I often refer to from Warren Buffett, "For 240 years it's been a terrible mistake to bet against America, and now is no time to start. America's golden goose of commerce and innovation will continue to lay more and larger eggs (Bloomberg – Warren Buffett's 2015 Shareholder letter, Annotated)."

A growing economy fueled by innovation and entrepreneurship has been the biggest driver of stocks over many decades. As Buffett emphasized, betting against America isn't a winning hand (and he didn't qualify his remarks based on the outcome of any election).

As I always emphasize, I take my stewardship role very seriously and I've been entrusted with tremendous responsibility to navigate these challenging times for you. If you have any questions or would like to discuss any matters, please feel free to give me or any of my team members a call.

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