Philequity Corner (June 10, 2019)
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Will Trump Murder the 10-year Bull Market?

Since Trump's May 5 tweet, markets were buffeted by sharp downturns and spikes in volatility. Hope turned to despair as negotiations with China broke down, prompting Trump to implement sweeping tariffs. Many feared that Trump's latest actions may put the bull market's longevity to the test. Unfortunately, it turned out that Trump was just getting started.

"TARIFF is a beautiful word indeed" - Trump

To justify his penchant for using tariffs as his primary tool to deter bad behavior of other countries, Trump tweeted the following on June 1, 2019:

"When you are the "Piggy Bank" Nation that foreign countries have been robbing and deceiving for years, the word TARIFF is a beautiful word indeed! Others must treat the United States fairly and with respect - We are no longer the "fools" of the past!"

Trump imposes tariffs on Mexico over illegal immigration

In a surprise tweet on May 30, Trump suddenly announced that he will be imposing 5% tariffs on Mexico with a 5% increase every month until it hits 25%. He added these tariffs will be kept "until such time as illegal migrants coming through Mexico, and into our Country, STOP." Fortunately for both sides, a deal was reached Friday night and the tariffs were scrapped. In a tweet, Trump said that "the USA has reached an agreement with Mexico. The tariffs… are hereby indefinitely suspended." This lifted the spirits of investors who were unnerved by more tariff threats from Trump.

China launches retaliatory measures

Meanwhile, China was not going to take Trump's tariffs sitting down. In addition to their own set of tariffs, various retaliatory measures were also launched. First, China threatened to cut rare earth exports to the US – a critical raw material for many high-tech products. Second, China issued a travel advisory warning to its citizens about potential harassment when they go to the US. Third, China is drafting an unreliable foreign entities list as a counter to the US' entity list which included Huawei. Saying that this will not focus on any one industry, China has already started its crackdown by investigating Fedex.

Trump against the world

In addition to China, a large portion of the global economy has been on the receiving end of Trump's tariffs. Canada, India and the European Union have all been threatened with increased tariffs on a wide range of products, such as steel, lumber, cars, appliances and some consumer goods. With Trump alienating even historical allies, it is no surprise the common adversaries of the

US have banded together. Just last week, President Xi Jinping embarked on a three-day state visit to Russia. President Vladimir Putin emphasized their closeness, calling President Xi his “best friend” and that their position on “key world problems are close.” In an apparent dig at Trump’s slogan, China state-run news agency Xinhua released a commentary titled “Forcing America First on others will lead to America Alone.”

Can the trade war cause a recession and kill the 10-year bull market?

Last week, Trump repeated his threat of imposing tariffs on the rest of China’s exports to the US worth $300 billion. With potentially more tariffs against China, it shows that Trump is willing to escalate trade tensions. This has led some investment firms to issue warnings. In a report, Morgan Stanley said that if the US were to push through with 25% tariffs on the rest of China’s exports and China retaliates, we could end up in a recession within the next 3 quarters. Goldman Sachs revised up its expectations of an escalation of the US trade war and, consequently, lowered its economic growth forecasts. For its part, the IMF estimates that as much as $450 billion in global economic output could evaporate by 2020 if the trade war continues to escalate.

Fed to the rescue

With growth concerns now taking centerstage because of the trade war and the stock market dropping for a month, markets got a breather from its plunge which started on May 5. The Fed delivered good news through a speech by Fed Chairman Jerome Powell last Tuesday. Powell said that he will address “recent developments involving trade negotiations.” Referring to the trade war, he said that “we do not know how or when these issues will be resolved.” Powell added that “we are closely monitoring the implications of these developments for the U.S. economic outlook and, as always, **we will act as appropriate to sustain the expansion**.” That last phrase was construed by investors to mean that a rate cut is coming. After Powell’s remarks, US markets rebounded more than 2% for their 2nd best day for 2019. With nonfarm payrolls coming in below forecast last Friday, markets priced in 2 rate cuts by end-2019, with the first coming as soon as July.

Philippine stock market outperforms

Fortunately for us, the Philippine stock market is outperforming its Asian peers recently. With the BSP taking a dovish slant as BSP Governor Benjamin Diokno promised more rate cuts in the future, the PSEi rose sharply. Combined with the S&P credit rating upgrade, this caused the PSEi to rise as much as 8.9% from the low.

Bull markets don’t die of old age, they get murdered

In a previous article, we said that economic expansions and bull markets don’t die of old age, they get murdered instead. While US economic growth in the past quarter continues to be strong, the trade war has the potential to cause a recession. We have seen the profound impact trade war concerns can have on the stock market. Fortunately, the Fed was able to stave off a more brutal stock market rout with its timely pronouncements. However, an investor still has to be vigilant as Trump may continue to make whimsical decisions. Will the Fed be able to save the market from the deteriorating sentiment because of the trade war? Or will Trump unwittingly murder this 10-year old bull market?

Philequity Management is the fund manager of the leading mutual funds in the Philippines. Visit www.philequity.net to learn more about Philequity's managed funds or to view previous articles. For inquiries or to send feedback, please call (02) 689-8080 or email ask@philequity.net.