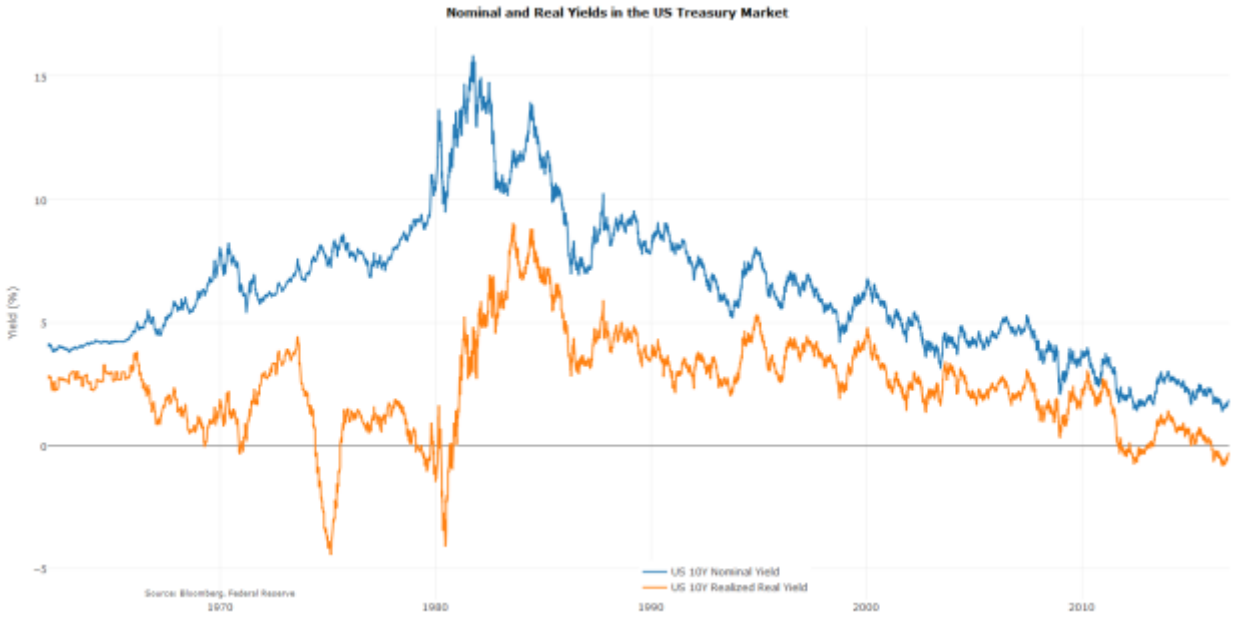
The Fed and the Economy – What's Next?

Posted on December 13, 2016 by Deepika Sharma

Navigating the low-return environment has been one of the top concerns for fixed income investors throughout 2016. Consider the fact that 35% of the global treasury market (as of this writing) is trading at negative nominal yields, which begs the question: Why are interest rates so low?

Read below to find out why or watch our explanation on YouTube (https://youtu.be/xyy0hQXByKc)

The common assumption is that the Federal Reserve and other central banks are keeping rates low, or that the cause is the 2008 financial crisis. In our view, however, this thinking is not entirely accurate. In fact, low interest rates are not a recent phenomenon. Real 10-year yields in the U.S. have been declining since the 1980s. Nominal 10-year yields were low in the 1960s, peaked at 15% in 1981, and have been falling ever since.



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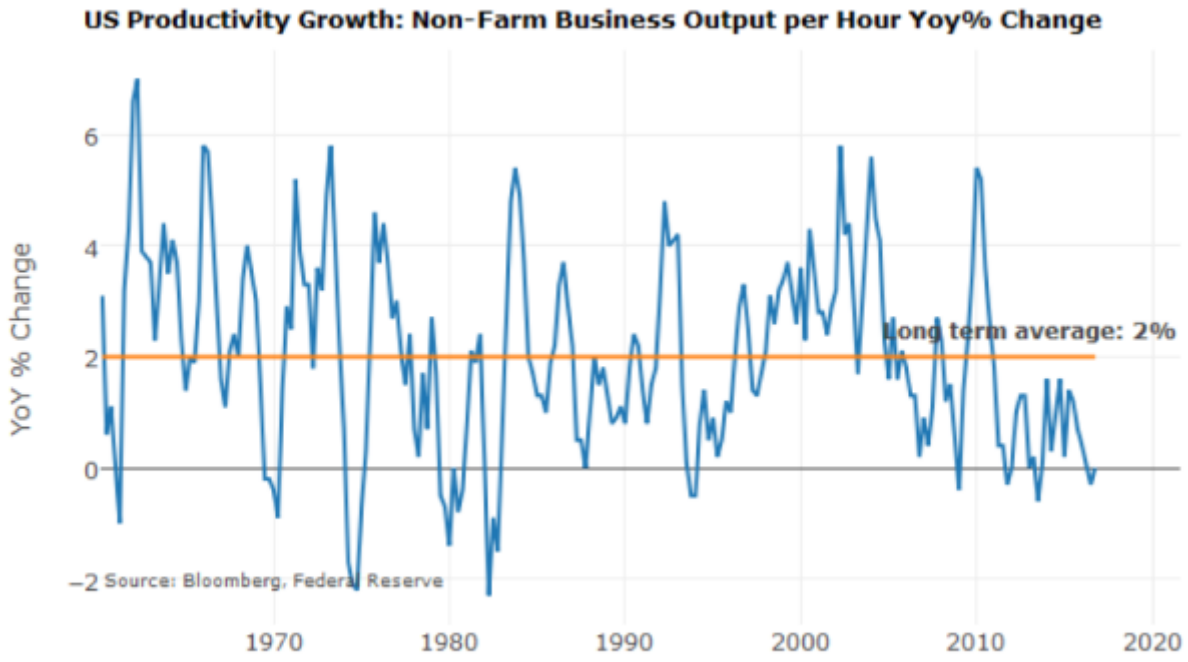
With an interest rate hike at the December 13-14 FOMC meeting seen as a foregone conclusion (http://www.cmegroup.com/trading/interest-rates/countdown-to-fomc.html), we have to ask: What is the upper limit of the Fed's potential to raise rates, given the long-term trend? How effective is Fed policy likely to be in the future? These are important questions because low long-term rates could very well mean that equities and other "risky" assets will remain overvalued, while fixed income investors struggle to meet target returns.

To address our Fed questions, we start with the understanding that the Fed cannot create growth; it can only affect money supply and nominal rates. The Fed is unable to solve economic changes or even influence real rates. Therefore, tracking the state of the economy is what ultimately determines long-term real returns. At Astor, we track economic trends using our proprietary Astor Economic Index®, and incorporate economic data into our portfolio allocation decisions.

Second, the long-term trend in real rates has rendered Fed policy tools such as the “Taylor Rule” ineffective. (Named for Stanford University economist John Taylor, the Taylor Rule was used previously to predict interest rates based on inflation, GDP, or other economic factors.) The Taylor Rule assumes a constant neutral or equilibrium Fed Funds rate, whereas both the FOMC and the markets agree that the neutral rate is much lower. In March 2015, Fed Chair Janet Yellen admitted to a non-constant neutral rate policy, and others including Fed Vice Chairman Stanley Fischer (https://www.federalreserve.gov/newsevents/speech/fischer20161121a.htm) and former Fed Chair Ben Bernanke also have spoken at length about it.

Third, we also have seen FOMC participants consistently shift down their long-term economic projections. The reasons for these diminished views are the same reasons why interest rates are low; hence these are the variables that we at Astor are watching closely:

Productivity – Growth in productivity has been disappointing, averaging only 0.5% (http://fortune.com/2016/03/25/labor-productivity-slump/) in the last seven years, compared to economists’ forecasts of more than 2%.



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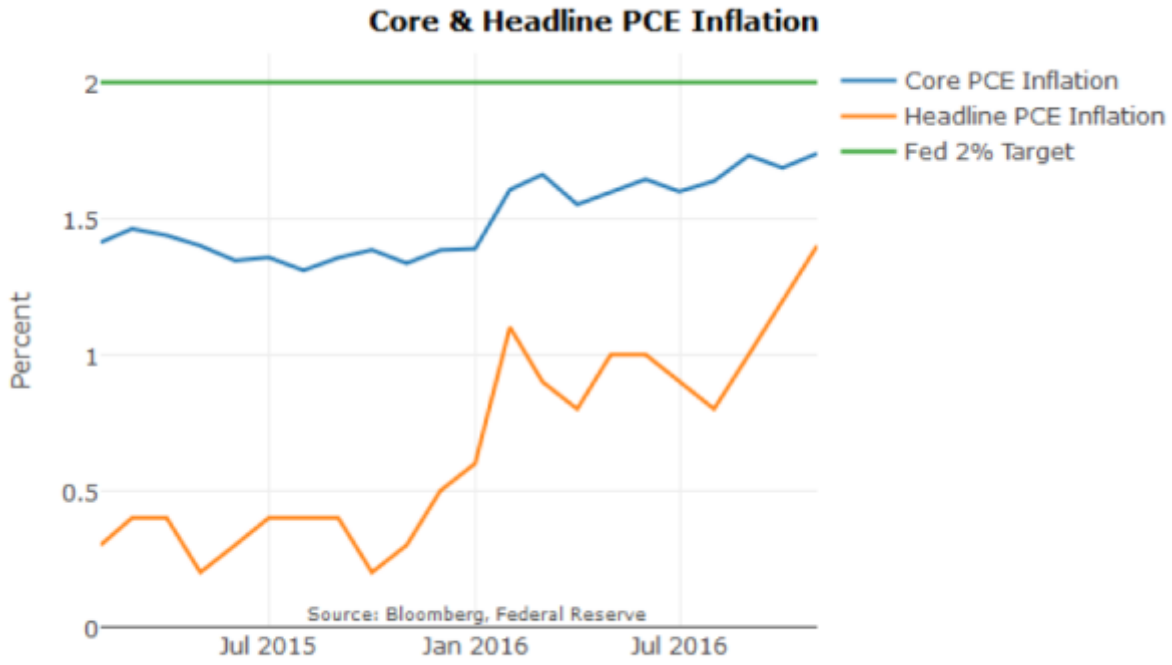
Payrolls and Growth — Even though payrolls have showed a lot of improvement (http://data.bls.gov/timeseries/CES0000000001?output_view=net_1mth)—this has not translated into faster economic growth, which, in our view, can only mean that the U.S. growth potential has been lowered as well.

Inflation — Wages have remained stagnant, and inflation hasn’t gone up, despite the growth in payrolls. The only likely explanation, as we see it, is that the relationship between wage and payroll growth has changed because inflation expectations are much lower.



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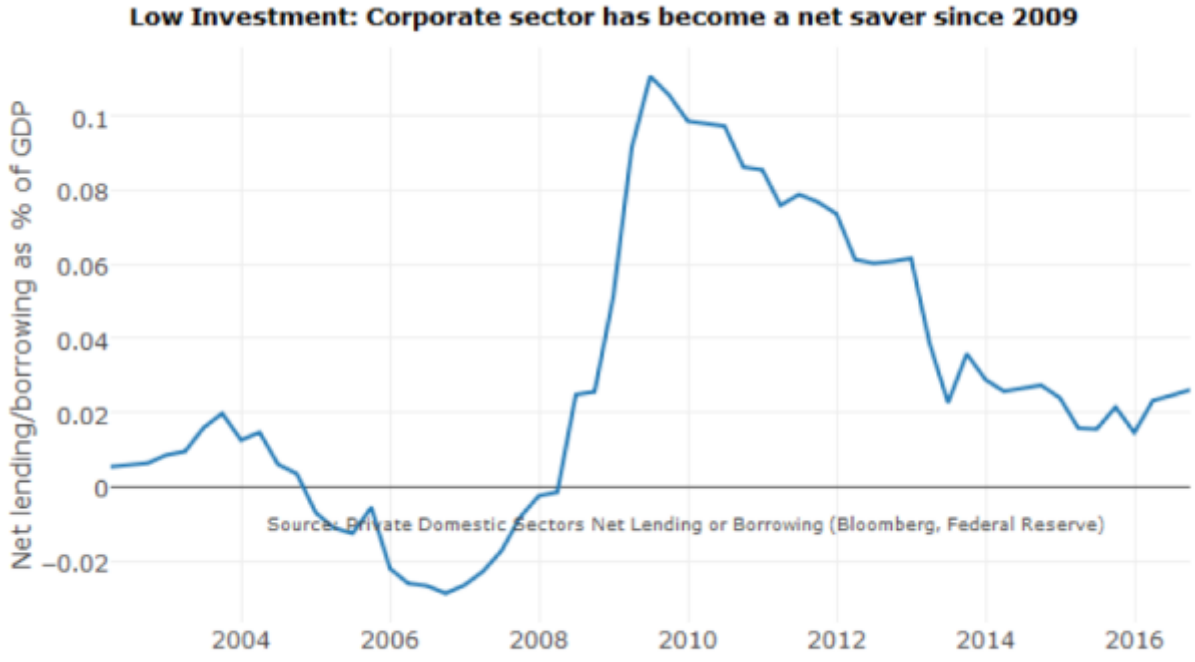
Structural factors – Factors such as a high savings rates, shifting demographics, and low capital spending and investment also have lowered the real interest rate.



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Taking all these factors into consideration, our conclusion is that, without improvement, it's questionable how effective Fed policy can be in the future—and possibly during the next recession, whenever that occurs—because the Fed cannot change the real economy. In addition, after its quantitative easing (QE), the Fed holds more than

$4.2 trillion in assets, mainly Treasury bonds and mortgage securities. This raises another question—will the Fed become an active seller moving forward, and how will that further impact fixed income securities?

As we consider what the Fed will do moving forward, these questions will remain on our radar.

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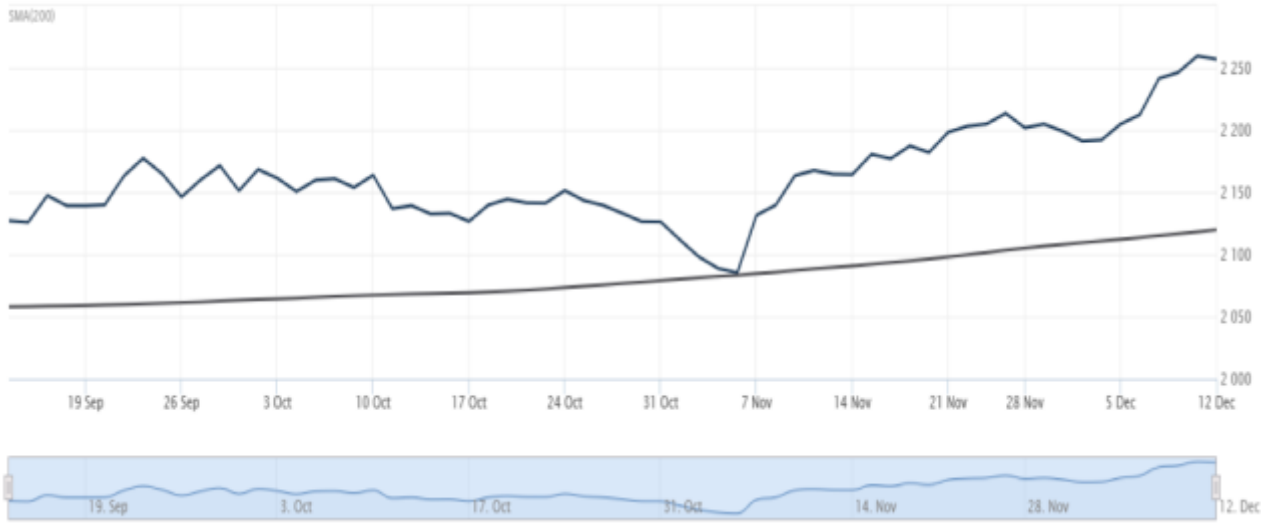
Is This Really a “Trump” Rally?

Posted on December 13, 2016 by Rob Stein

The latest market surge, as the Dow powers toward 20,000, is being called the “Trump stock market rally.” But as an economist and a realist, I have to question whether stocks would rally this much just on hope and expectations for a new administration, without the help of some other catalyst.

Granted, since the election, moves in the stock market have been significant: the Russell 2000 index (https://finance.yahoo.com/quote/%5ERUT/?p=^RUT) of small-cap stocks has gained about 20% and the S&P 500 (https://finance.yahoo.com/quote/%5EGSPC?p=^GSPC) about 8%. Conversely, bond prices have taken a beating, although no one is calling that the “Trump Bond Dump.”

S&P (SPX) 3-Month Chart with 200-day simple moving average (Source: Wall Street Journal)



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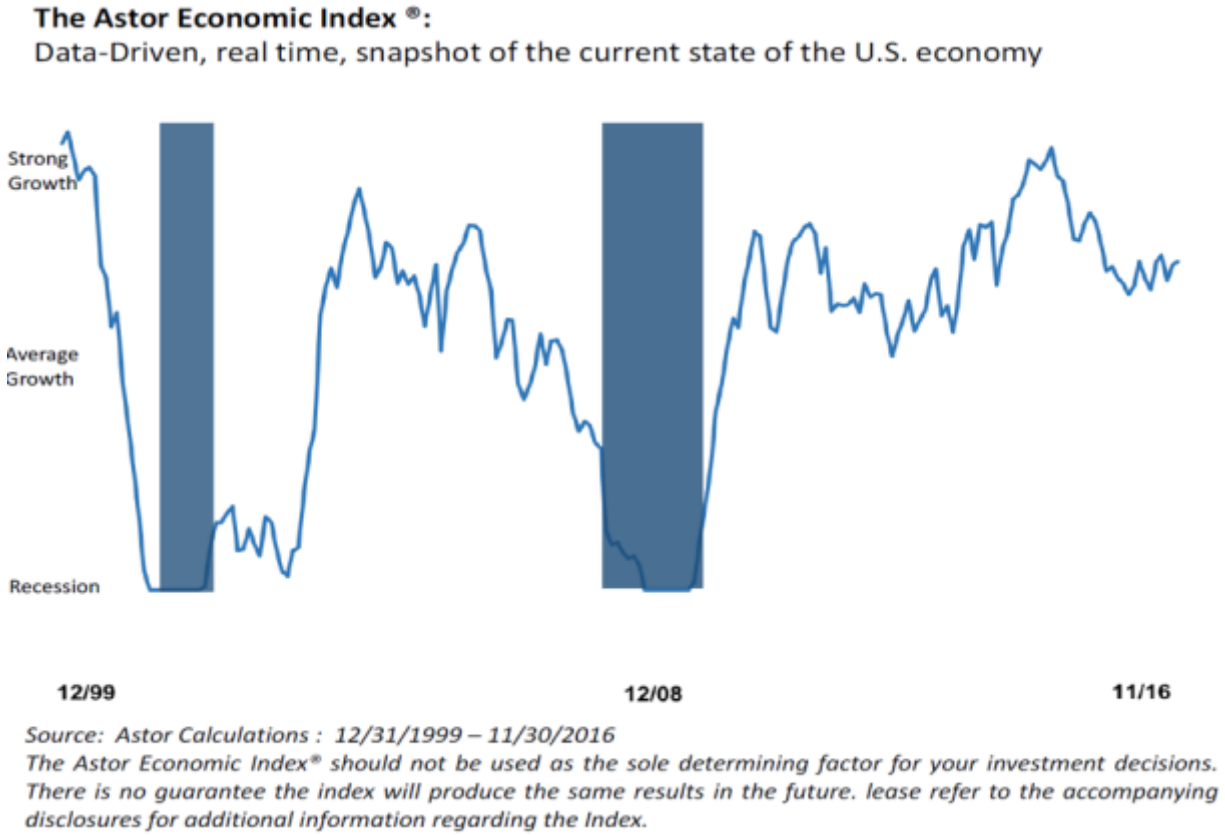
As I dig deeper into the stock market rally, I believe there is another explanation for the most recent strong upward move in equities. For one thing, we are no longer barraged by the election drama. Uncertainty is gone; we know who won. Minus uncertainty, the market can shake off fear and resume its trend that, prior to the election, had been upward. (Recall that we were at previous all-time highs in the S&P this past summer (http://www.cnbc.com/2016/08/05/us-markets.html), propelled higher by an improving employment picture.)

My point here is not to be political. Politics and economics are two very different animals who have to play nice in the jungle. But I do believe that this rally would have occurred no matter who won the election, based on the strength of the current economic fundamentals.

This is not meant to take anything away from President-elect Trump's plans. Some investors are interpreting the Trump agenda as being supportive of the economy (http://www.nytimes.com/2016/12/09/your-money/how-to-play-the-trump-stock-market-rally.html?_r=0). There are some proposals, however, that could hurt stocks, such as limitations on international trade. In addition, increased spending and lower tax revenue could lead to a larger deficit, while policies that could lead to accelerated interest rate hikes would make it harder for corporations to float debt. And for all his ideas that could stimulate growth (e.g. infrastructure investments) at least in the short run, keep in mind that it takes a lot for anyone to execute a plan into action.

As an aside, it's interesting to note how names get associated with certain things to describe or define them in some way. Think Watergate of the Nixon era; now any conspiracy or controversy is the next "Something-Gate"—immediately conveying a meaning, and a negative one at that. Health care reform—officially known as the Patient Protection and Affordable Care Act—is nicknamed Obamacare for the president who made it a policy hallmark. Ronald Reagan's economic policies were dubbed Reaganomics. And the list goes on. Now, as we head to Inauguration Day in January, Trump appears to have his first label whether he deserves full credit for it or not: the Trump stock market rally.

But let's be clear: This rally, as I see it, is not just built on hopes for what *might* happen with the new administration. Rather, it reflects what is already happening, namely improvements in economic fundamentals. The Astor Economic Index (http://astorim.com/astor-philosophy/)® (AEI) is showing the economy growing at an above-average rate.



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Unemployment continues to drop, with a current rate of 4.6% (http://data.bls.gov/timeseries/LNS14000000), the lowest level since mid-2007, while wage growth has also been rising steadily. GDP has improved (http://bea.gov/newsreleases/national/GDP/GDPnewsrelease.htm), particularly in the second half of the year. Inflation, which has been negligible, is moving toward the Federal Reserve's 2% target. And, the Federal Reserve appears to be giving a vote of confidence to the economy with a widely expected short-term rate hike (http://www.wsj.com/articles/global-economy-week-ahead-federal-reserve-meeting-china-data-1481486461). Globally, the economic picture appears to be bottoming out after a prolonged period of malaise, and growth is starting to tick up.

No matter what the stock market rally is called or who gets credit for it, I believe it's important to view it in the context of fundamental realities: U.S. economic growth is accelerating, an environment that we, at Astor, believe to be supportive of buying stocks and other risk assets.

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The Astor Economic Index® is a proprietary index created by Astor Investment Management LLC. It represents an aggregation of various economic data points: including output and employment indicators. The Astor Economic Index® is designed to track the varying levels of growth within the U.S. economy by analyzing current trends against historical data. The Astor Economic Index® is not an investable product. When investing, there are multiple factors to consider. The Astor Economic Index® should not be used as the sole determining factor for your

investment decisions. The Index is based on retroactive data points and may be subject to hindsight bias. There is no guarantee the Index will produce the same results in the future. The Astor Economic Index® is a tool created and used by Astor. All conclusions are those of Astor and are subject to change.

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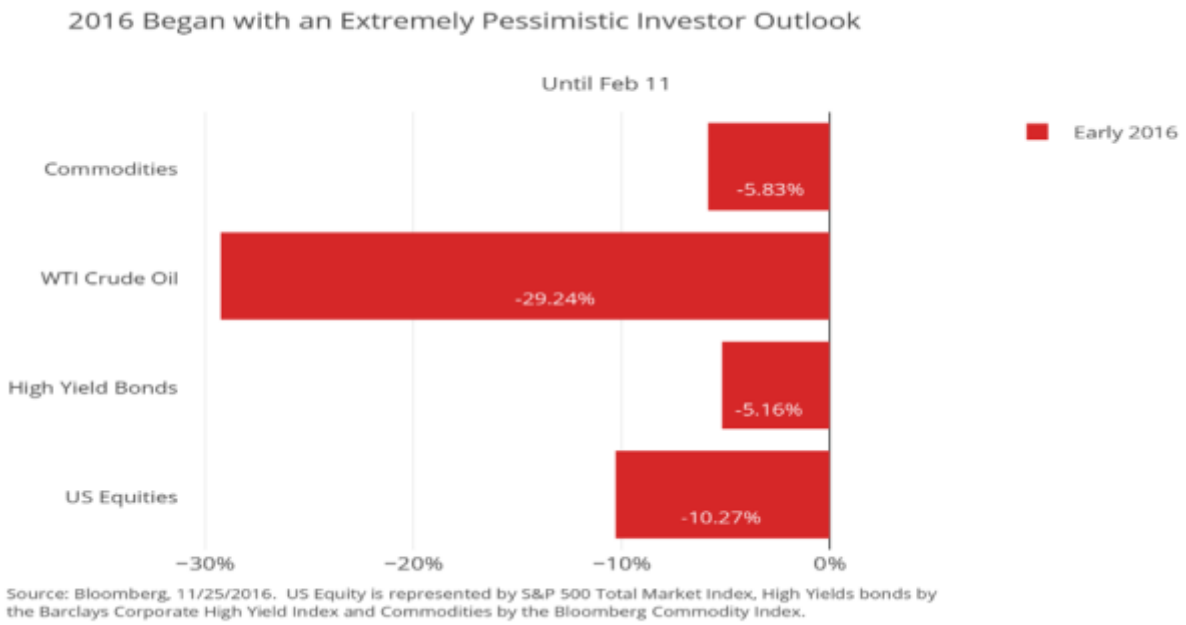
What Investors Got Wrong in 2016

Posted on December 6, 2016 by Deepika Sharma
As we look back on 2016, a notable theme is just how wrong the markets were when it came to predicting events and risk drivers.

The year began on a pessimistic note. By the February 11 low (http://money.cnn.com/2016/02/11/investing/dow-jones-oil-stocks-nasdaq/), the S&P 500 had lost more than 10%, and high-yield bonds were down more than 5%. A major culprit was sharply declining oil prices; WTI crude was down nearly 30%, which drove down commodities as a whole.

Market jitters were also caused by expectations that China's growth rate was going to fall short, which further compounded concerns about global growth in general.



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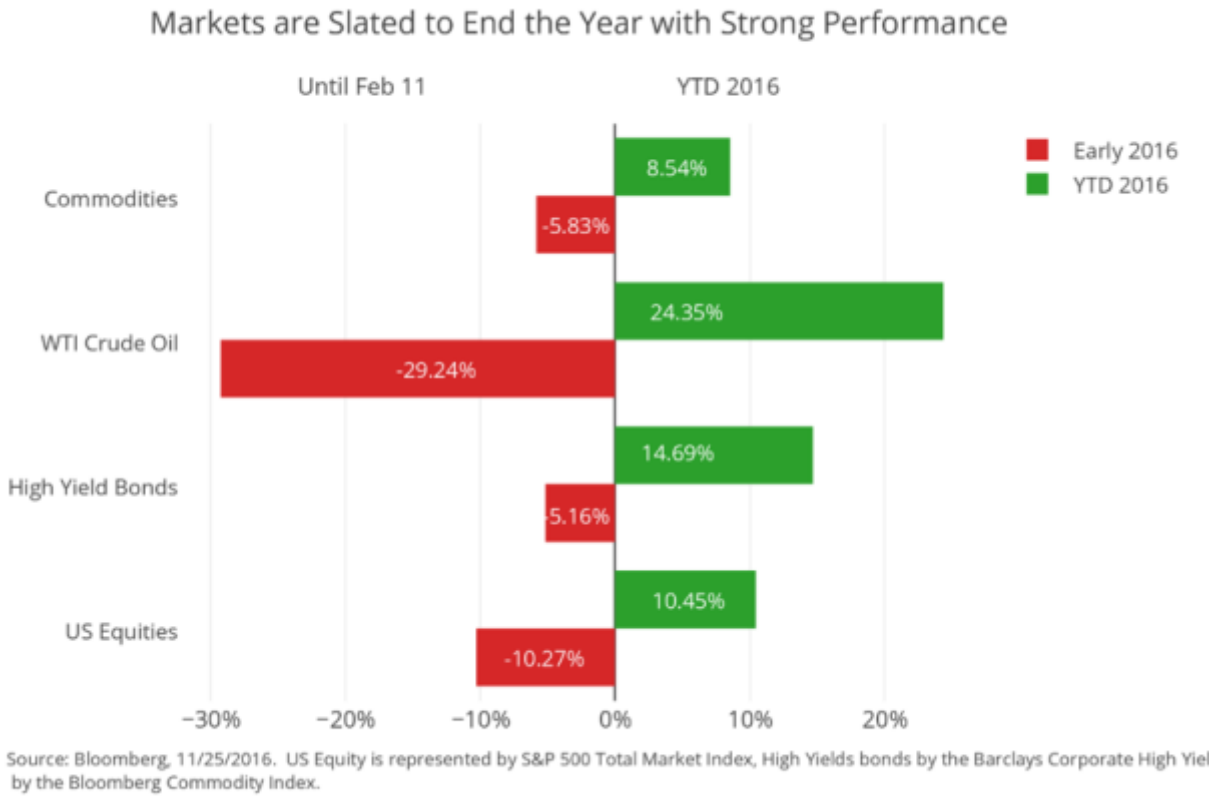
Now, at year end, the picture looks much different. Global growth in 2016 couldn't have been better. In the U.S., a third quarter GDP reading of 3.2% (https://www.bea.gov/newsreleases/national/gdp/gdpnewsrelease.htm) exceeded expectations.

Meanwhile, China (https://www.ft.com/content/faa4576c-0203-11e6-9cc4-27926f2b110c) grew steadily in 2016 at a rate of about 6.7%. As a result, over the first 10 months of 2016, investors have poured more than $50 billion into emerging market (https://www.bloomberg.com/news/articles/2016-09-30/stock-pickers-left-out-as-50-billion-rushes-to-emerging-markets) stock and bond funds.

As for market performance, year-end is nearly a mirror opposite of what occurred at the start of the year. From January through end-November, the S&P 500 is up about 10%. High-yield bonds are up more than 15% year-to-date, and oil has gained almost 25%.



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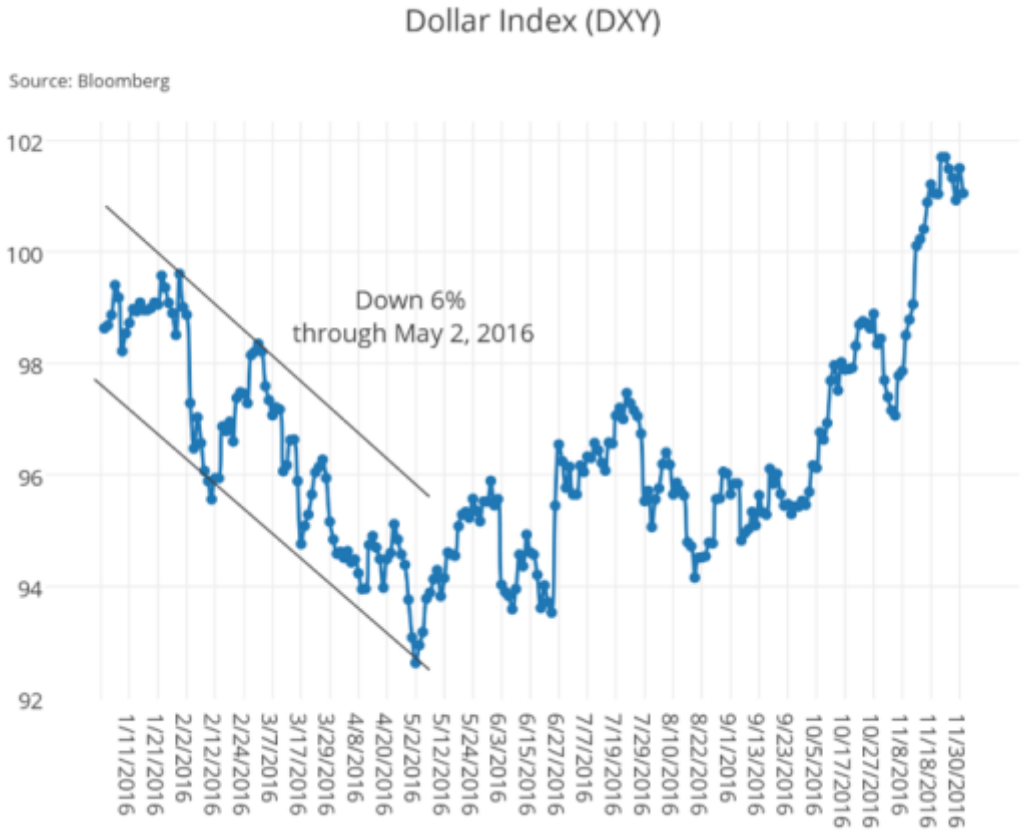
The second major thing that the markets got wrong was the expectation for rate hikes by the Federal Reserve. When 2016 began, the expectation was that four rate hikes were likely. In January, Fed Vice Chairman Stanley Fischer said that four rate hikes (https://www.bloomberg.com/news/articles/2016-01-06/fed-s-fischer-says-four-rate-hikes-in-2016-in-the-ballpark-) for the year were “in the ballpark,” although China’s slower economy and other uncertainties made it impossible to predict what would happen to interest rates.

The concern in early 2016 was that if the Fed pursued the expected course, the U.S. would go in one direction with interest rates, while the rest of the world was headed lower; in some countries more negative rates were possible.

As we now know, the Fed took a more guarded stance in 2016, following its December 2015 move, which was the first rate hike in almost a decade. This change in expectations affected currencies most of all. The U.S. dollar was expected to rally, but fell 6% in the first half of the year. In contrast, the Japanese yen appreciated through August due to safe haven trades.



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Now that we are at the end of the year, we can see how the markets did adjust to changing realities. In fact, both the Fed and the market appear to be aligned. The widespread expectation (http://www.cmegroup.com/trading/interest-rates/countdown-to-fomc.html), already priced into the market, is that the Fed will raise rates at its mid-December FOMC meeting.

The year, though, is not over yet. No matter how clear things may appear, we still think predicting policy events, central bank actions, and the market's reactions will always be a challenge.

Please watch the video on What Investors Got Wrong in 2016 (https://youtu.be/LXc9XDQGQs4)

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Last Economic Update for 2016

Posted on December 6, 2016 by John Eckstein

For my last economic update of the year I will review where we are today and try to read the tea-leaves of the incoming Trump administration. The president elect is lucky in inheriting a solidly growing economy. His penchant for decisive action may run into procedural roadblocks in Washington which could significantly delay actions which require congressional approval. Overall I see few significant effects in the coming months.

Our latest reading for the Astor Economic Index® ("AEI") improved over the month and currently shows the US economy as growing somewhat above average. I also see modest improvement year over year. As this is the last update of 2016 I can say that I am pleased with the performance of our index as an economic gauge over the last 12 months. Memories may be dusty, but a year ago there was widespread concern about US economic weakness. The AEI was showing only minor declines at the time and, in fact, no extended decline in the boarder economy occurred. The AEI is a proprietary index that evaluates selected employment and output trends in an effort to gauge the current pace of US economic growth.

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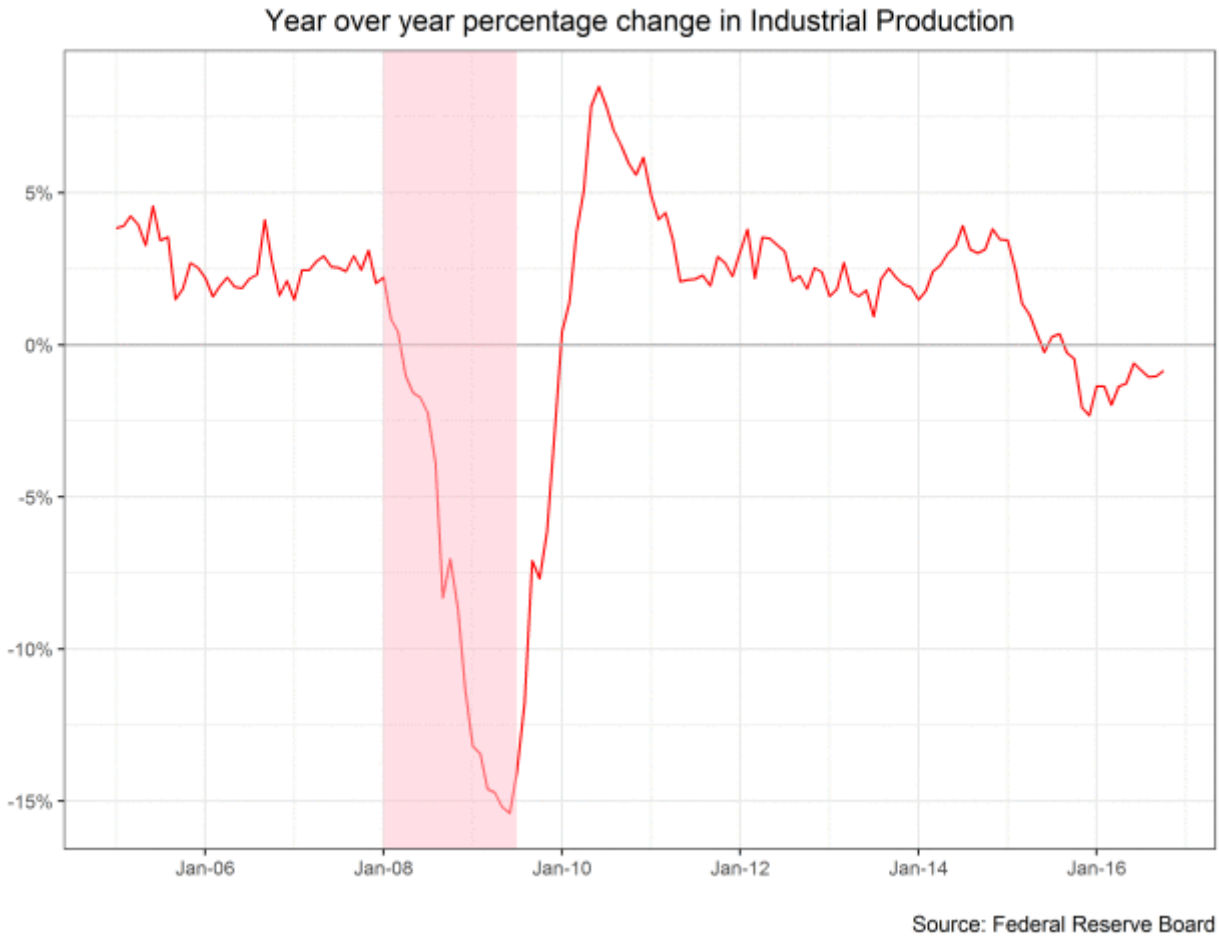
The new president's first element of luck is an economy running at full employment. Last Friday's employment report was fairly strong – showing the economy continues to add jobs faster than the number of new entrants to the work force. Levels of both unemployment and underemployment (ie, involuntary part time work) have both dropped significantly in recent months. Recently we have seen a trend of improving wages. That trend weakened slightly this month but the year on year improvement is still significant.

The nowcasts produced by the Federal Reserve banks of Atlanta and New York are both still showing strong growth in the fourth quarter. The Atlanta Fed (https://www.frbatlanta.org/cqer/research/gdpnow.aspx?panel=1) is currently estimating 2.6% SAAR and the New York Fed (https://www.newyorkfed.org/research/policy/nowcast) is currently forecasting 2.7%. Both somewhat above the average for the current expansion. Both estimates have been updated since the release of the employment number for November.

There is another element of luck in the external environment – what is going on with our trading partners around the world. I attribute the last few years tepid industrial production growth to weak external demand and the strength of the dollar.



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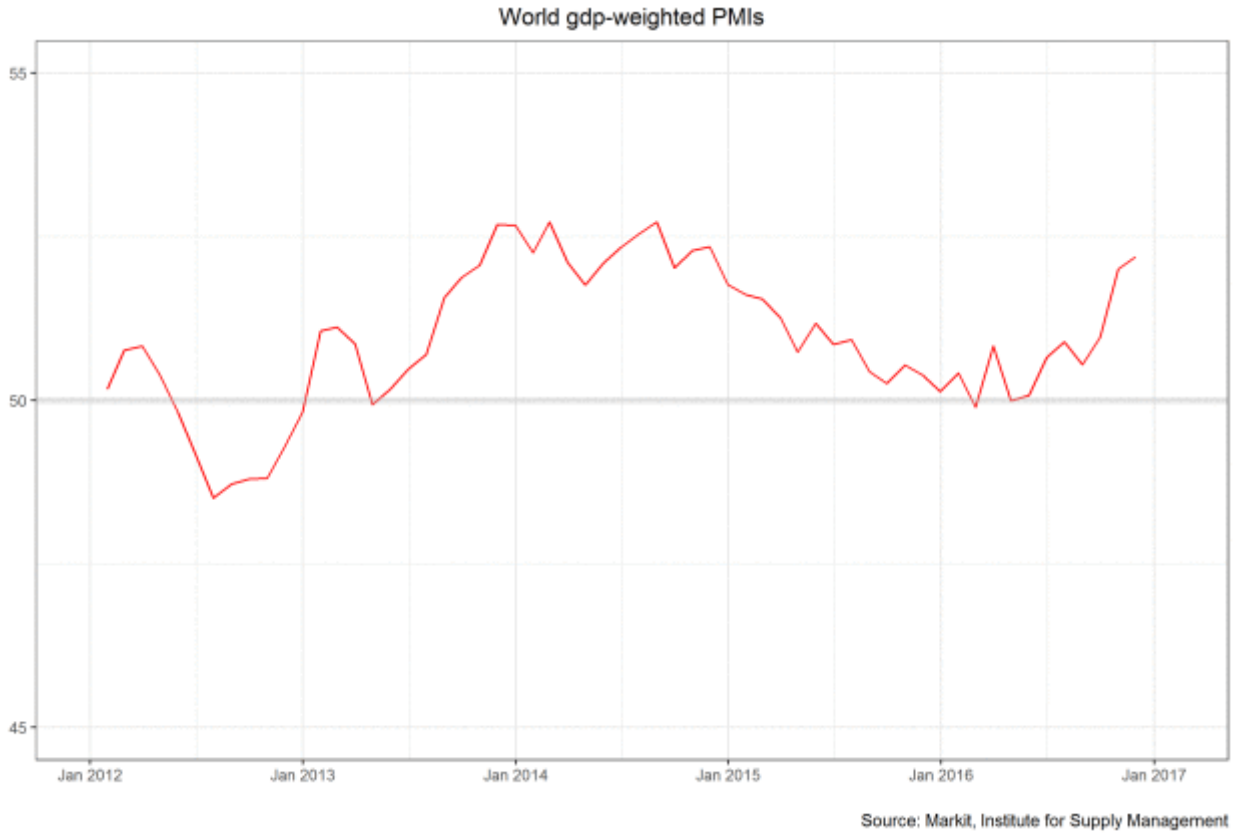
The chart below is the GDP weighted average of the individual purchasing managers indexes. I intend it to be proxy for the change in demand in the world manufacturing cycle.



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This reading is now approaching its highs from 2014 – suggesting that the weak global manufacturing environment may be improving. Mitigating this global good news somewhat is the performance of the dollar which has set new highs in trade weighted terms. This makes it harder for business to export, though dollar is not seeing the sharp rise it experienced in June 2014- December 2016 period.

The contours of economic policy under the Trump administration have yet to be fully fleshed out. One interpretation of the market action since the election is that there is a substantial likelihood of fiscal stimulus in the form of tax cuts and perhaps infrastructure spending. The President will need to negotiate with both the House and the Senate which have different priorities than does the President Elect. Additionally the GOP holds only slim majorities in both houses, increasing the chance for a small number of legislators to derail the process – at least temporally. If the normal timetable holds we will not see a budget from the new administration until February and House and Senate budgets until March. The negotiation process will then begin. This gives plenty of time for the markets to be disappointed by what may turn out to be an unusually public negotiating style.

The morning after the election I noted that the president has much more autonomy in trade policy. I feel that my comments are still germane: unlike in fiscal policy, the President is able take unilateral actions which may sound like the first shots in a trade war. Combine fiscal policy with trade policy and era of Government By Tweet may offer plenty of examples of what my bond trader father used to call Tape Bombs. These are shocks in the form of unexpected, inherently unpredictable pieces of news which the market reacts and over-reacts too. Recall the summer and fall of the debt ceiling to get a sense of what I mean.

At Astor we think that in times like these is even more important to approach the markets with a discipline which clarifies decision making by keeping the focus on facts not predictions. In our case we will continue to use the state of the of the business cycle as it unfolds as our key input in making investment decisions.

Closing with the fed, my judgement and that of the fed funds futures market (which has a conventional interpretation, see this CME page (http://www.cmegroup.com/trading/interest-rates/countdown-to-fomc.html) for example) is that the FOMC will raise rates at the next meeting. The using the same interpretation of the fed fund futures curve shows that the market expecting another hike or two by next year, though the market has been repeatedly disappointed in the last several years. Two things which could make the fed hike more quickly than the market expects would be a sustained rise in core inflation or the prospect of substantial fiscal stimulus. Keep on the lookout for comments by fed governors making the connection between the monetary and fiscal stances of the US.

Overall the economy continues its recent path of modest growth. With some headwinds dissipating we may be hope that next year will be on the upper end of the recent range of growth. As always we will continue to monitor the economy closely.

Posted in Home

Operations As a Vehicle for Business Success

Posted on November 28, 2016 by Astor Investment Management LLC
By Brian Durbin, Managing Director of Operations

All investment advisers have an asset target in mind. In order to reach that finish line, you need to have a solid vehicle. Having a qualified portfolio manager (i.e. the driver) is a large part of the race, but it is certainly harder to accomplish without efficient and effective systems and processes in place. A streamlined and prepared operations department will help take you the extra mile.

These days, there is no shortage of new regulation and technology to keep the operations departments of investment advisers on their toes. In order to fluidly maneuver through a changing landscape, it might be helpful to think of operations as a rally car. Here are five points to help visualize this reference.

Wear protective gear

Race car drivers know the importance of wearing helmets and harnesses to prevent injury in the event of a crash. The unexpected can happen. In investment operations, a technology glitch can create a trade error or an inattentive worker can input the wrong data. Risk controls and flags should be present in any adviser operations. Insurance products such as Errors & Omissions (E&O) can help provide financial protection.

Remove unnecessary weight

In order to maximize speed, race cars are stripped down to be as light as possible while maintaining safety and function. Operations departments should be lean as well. However, there is a fine line. Too light and you might tip over if you need to adjust quickly. You want to be nimble in case you need to build up. The key is designing systems and processes that are easily scalable so the addition or removal of an employee, group of accounts, etc. does not disrupt workflow.

Inspect and know your vehicle

Racers know their cars inside and out. Similarly, in investment operations a thorough review of systems and processes should be conducted at least annually. Dismantle each process and walk through it step-by-step to determine the weak points. If you do not have the headcount to complete this review, find a qualified consultant. Drivers may have to conduct small repairs or inspections themselves but a mechanic is often on hand as well. Similarly, third-parties provide additional value to the review of operations by removing bias and familiarity which can cause you to miss crucial gaps in processes. By knowing where risks lie and the capabilities of the systems, you will know what protective gear to use as mentioned above.

Use a co-driver

Rally car drivers often have a co-driver sitting in the passenger seat. The co-driver is part navigator, part handyman, and part safety (they counter-balance the weight distribution). For investment operations, compliance, legal, and portfolio management personnel should be integrated into operations to provide information on upcoming regulatory or industry changes that will impact operational processes. Given that the investment industry is ever-changing, being provided with information on the road ahead is valuable.

Prepare for the conditions

Heavy rain, mud, gravel, and other factors can determine the types of tires used during a race. Similarly, different market conditions and business channels can change how an investment adviser views operations. Using the proper systems for the current conditions is important, but preparing for upcoming changes is equally important. If a driver knows the first quarter of a race is in rain, but the rest will be dry, the decision may be to sacrifice better rain tires due to the limited amount of time they would be needed. Likewise, an investment adviser may forego the purchase of an order management system due to expected changes in account type (e.g. moving from discretionary management to model delivery).

Whether you compare operations to a rally car or construct it using another visualization, the key is to see the larger picture and shape processes according to the path your business is on.

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Revisiting Active Investing: Is the Trend in Passive Over?

Posted on November 21, 2016 by Rob Stein

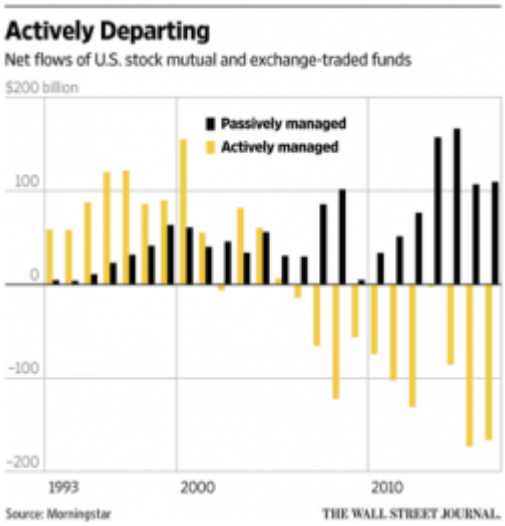
Over the past few years, financial advisors and their clients, in search of low-cost ways to capture market performance, have piled into passive investment strategies. As the *Wall Street Journal* reported recently, for the three years ended Aug. 31, 2016, nearly $1.3 trillion flowed into passive (http://www.wsj.com/articles/the-dying-business-of-picking-stocks-1476714749) mutual funds and ETFs. For investors, it seemed like a "no-brainer" move in a low-risk, low-volatility environment, with an upward trend for equities.

For years, I've been advising investors not to pay up for "beta"—that is, market exposure that is far easier and cheaper to capture with an ETF that seeks to replicate the S&P 500 or another index. But the rush to jump into passive and dump active may have thrown out the proverbial baby with the bathwater. There is growing evidence that active investing is coming back into favor. As *Barron's* reported, since July 1, 60% of actively managed funds (http://www.barrons.com/articles/active-stockpickers-are-outpacing-passive-funds-1478318812) are beating the S&P 500, the highest level in nearly two decades.

At Astor, we believe now may be the opportune time to revisit active strategies that might not be the lowest cost, but may be meaningful in helping investors achieve their portfolio goals. For example, the Astor Dynamic Asset Allocation Strategy (http://astorim.com/attachments/LSB_SMA.pdf) (formerly known as Long/Short Balanced) has outperformed the HFRI Total Macro Index for every year but one, and has posted a higher cumulative performance, such as for the past 3, 5 and 10 years (See Exhibit 4: Performance (http://astorim.com/attachments/LSB_SMA.pdf))

Not an 'Either-Or' Choice

To be clear, I'm not suggesting that passive's time has passed; however, it appears to be getting long in the tooth, with signs of becoming a "crowded trade," given the amount of money piling into passive funds, as the chart below indicates. (Source: *The Wall Street Journal* (http://www.wsj.com/articles/the-dying-business-of-picking-stocks-1476714749?mg=id-wsj))



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While investors may still benefit from having a portion of their portfolios dedicated to cheap beta, we believe active investing has a role to play in overall portfolio strategies. In fact, active investing, in our view, could very well be an answer to the essential question for investors (one that has become muted in the rush to passive investing): *What is my long-term portfolio objective?*

This question has become more relevant because, as we have observed, investors are taking on more risk with less professional input and guidance. In our view, this is reminiscent of the herd stampeding into tech stocks in the late 1990s, just before the 2001 recession—a time when a diversified portfolio of anything other than tech stocks would have weathered the storm.

To be clear, the current spotlight on active investing is not due to the surprising outcome of the U.S. presidential election and increased volatility of global equity markets (http://www.wsj.com/articles/traders-salivate-as-volatility-returns-1479160183). However, greater uncertainties and perceptions of increased political risk (http://astorim.com/wp-content/uploads/2016/11/Library-Doc-Template_Political-Risk.pdf) in the US and abroad are raising questions in investors' minds, especially about potential changes in economic and political policies (http://astorim.com/analysis-the-2016-presidential-election/). At Astor, we have heard from many investors who are asking such questions. As we've found, investors who had piled into low-volatility and passive strategies wanted guidance and interaction with professional managers. And robo-advisors with their static portfolios don't call you up to discuss long-term trends that may be impacted by a new president or changes in policies, interest rates, and so forth.

Our message to investors echoes our fundamentally-driven approach. At Astor, we use our proprietary Astor Economic Index (http://astorim.com/astor-philosophy/)® to identify the current economic trend and then make portfolio allocation decisions accordingly. We augment equity holdings with fixed income as we dial risk up and down. Furthermore, we allocate to additional non-equity assets that we believe will benefit from long-term market trends that are often hard to capitalize on with static or passive strategies.

Taking a dynamic approach allows investors to be more mindful of opportunities among asset classes or sectors. We do not advocate market timing, trying to pick tops and bottoms; however, we do believe that greater flexibility may be key to identifying those sectors that are more likely to perform favorably over the next several quarters or years. In fact, we believe there could be significant differences in performance from sector to sector.

Already we are seeing divergence in performance among styles and sectors. Small cap stocks are having a good run of late, while technology stocks are lagging. International markets are moving with in line with developed economies, while emerging economies are struggling. Risk premiums are changing around the world and among asset classes. Non-equity assets such as gold, currencies, and high-yield bonds are behaving in potentially diversifying and accretive ways. Investors holding fixed income investments should be mindful of rising interest rates, higher inflation, and yield curve fluctuations. Opportunities in metals, currencies, and international holdings should be considered for both diversification and the potential to generate a positive return through dynamic asset allocation.

While passive investing still has its place, in our view the time has come, once again, for taking a more dynamic approach to asset allocation as part of overall diversified portfolio solutions.

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Analysis: The 2016 Presidential Election

Posted on November 9, 2016 by John Eckstein

In light of Donald Trump's win and the GOP hold of all three branches of government, the question on most minds today is, what is the outlook for the US economy? My short answer is that it is too early to tell. At Astor, our philosophy is to be guided by actual economic data rather than forecasts. Nevertheless, it is important to think about possible implications for the U.S. economy.

The economy came into the election on an extremely stable path. Our Astor Economic Index®– a proprietary index that evaluates selected employment and output trends in an effort to gauge the current pace of US economic growth–has been steadily showing modest, but positive, growth all year. Indeed, it has been in an unusually narrow range recently suggesting to us that fundamental dynamics of the US economy are stable.

In the next days to weeks the heightened uncertainty caused by both the unexpected outcome and the unknown policies of a Trump presidency seem likely and the stock market tends to dislike uncertainty.

The nontraditional nature of Trump's campaign means that there are few coherent, detailed policy commitments to game out. Trump has held a variety of opinions on most matters and will have to work with Congress, which may feel emboldened by his political inexperience.

Discontent over the US trade position has been Trump's consistent theme. Much trade power has been focused in the executive branch, leaving the new President some leeway to act without Congress, subject to court review over an extended period of time. Given what Trump has said about his negotiating style, it would not be surprising to certainly see some eye-catching headlines about withdrawing from NAFTA. Trump has repeatedly called for a 35% tariff on Mexico and 45% on China, which he may be able to impose at least for a few years unilaterally. This will reduce trade broadly and disrupt international supply chains.

For more on Trump's views on trade see this article from the Peterson Institute (https://piie.com/system/files/documents/piieb16-6.pdf). The authors point out that using standard economic models, a full trade war (where the US raises tariffs on other countries that can then retaliate in kind) could on its own cause GDP growth to be as much as 2.9 percent lower per year for several years. his same paper estimates that an aborted trade war, which they operationalize by saying tariffs are imposed only for year before reverting to previous levels, could have a small stimulative effect on the economy. The future may be somewhere in between.

In my opinion, the reality of substantively reduced trade would likely also be a weaker dollar and higher inflation in the medium term in addition to lower GDP growth. It seems that the broader multilateral free trade deals such as the Trans Pacific Partnership will not be brought to Congress.

Early on it is possible that repudiation of as much of the Obama legacy as possible could be the GOP first order of business. As observers have noted, that may mean repealing Obamacare and reducing financial regulation such as Dodd-Frank and the Consumer Financial Protection bureau.

One thing all Republicans agree on is tax cuts—and that, in our view, could be the single most likely outcome. Both Trump's and speaker Ryan's plans skew cuts toward the wealthy. Trump agreed with his opponent that increased infrastructure spending is necessary, but that may prove harder to get through Congress. It is not clear if Congress will make substantive spending cuts to pay for the increased fiscal spending. This has the potential of being stimulating to the economy, but if unfunded could cause bond yields to move higher quickly.

Turning to the Fed, where is its promise to raise rates in December? Much will depend on the reaction of markets between now and the next FOMC meeting in a month. Should markets recover and treasury prices stabilize the Fed may still raise rates a quarter point in December. Should the new administration's plans crystalize to substantial fiscal spending the FOMC may see the need to raise rates preemptively.

Janet Yellen's term as Chair of the FOMC expires January 2018. Trump has both praised and condemned Yellen this year, but it seems likely in our view that he would prefer to install someone new as chair. In addition, there are currently two open seats on the board of governors giving the new administration a chance to move the Fed. My sense is that the rest of the GOP would prefer a more hawkish Fed and without a strong campaign promise to fulfill Trump may accede to their wishes.

Overall, I expect no large changes in unemployment or output over the next few months as a result of the election, but the increased uncertainty may lead to a challenging time for all assets until some clear signals emerge from the new administration. As always we will wait to see changes showing up in the economic numbers before adjusting client portfolios and will use our time-tested process to guide us whatever occurs.

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