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In the Trump era, stock portfolios need to be flexible

The main risks for share prices could come from the new president's protectionist policy

by Gaia Giorgio Fedi

Share portfolios are grappling with the Trumponomics effect. The experts are wondering what effects the new US president's protectionist policies will have on equity. "The initial reaction of the markets was optimistic in terms of positive expectations for infrastructure investments and tax cuts for business, but also for other reasons. Take the expected inflationary forces and higher rates, which are shifting attention to stocks, the rise in the oil price and Chinese growth, and the expectation of growing returns on shares", comments Gabriella Berglund, head of global stock picking for the Italian market at Comgest. Now, however, Berglund feels that other factors need to be assessed, because "the market has underestimated the geopolitical effects, as well as some potentially negative factors such as the combination of strong dollar, rising American pay levels and rising inflation".

Some experts fear Trumponomics. Angelo Meda, head of equities at Banor SIM, feels that the implementation of a fully-fledged US protectionist policy is "one of the main risks we see facing the world economy in the medium term". In the last century, globalisation "added at least one percentage point annually to global GDP growth. If we were to imagine a partial reversal of this effect, the impact for the world's economy, and consequently its stock markets, would be significant", adds Meda. For Marco Fiorentini, head of Investment Consulting at Credit Suisse, "with a protectionist policy - if that's what happens - the impacts could be positive for some geographical regions, for others less so". Certain emerging markets, especially exporting economies, could feel the effects, while "there could at the same time be a positive impact on the American indices". But there's another factor to keep under control: "the possible increase in US/China geopolitical tensions. You could say that the 'Pax Americana', which ensured stability and trading freedom for Asia after the Second World War, has run its course", adds Fiorentini.

Luca Tobagi CFA, investment strategist at Invesco, points out that protectionism can take different forms. "One is to apply duty on imports of goods and services from abroad", he explains. Another, more complex, form that is currently at an advanced stage of study is to apply differentiated tax levels to profits generated by exports by US companies, which would not in fact be taxed, and costs relating to the goods and services imported by them, which would no longer be deductible from income. To estimate the overall impact of these manoeuvres, we need to understand the potential net effect of these protectionist measures, and of the probable responses by other countries, on the growth of the global economy. This would presumably be negative and, like the differentiated taxation scheme, would impact the companies making up the indices both in the USA and abroad". In a scenario of this nature, making predictions is a complex exercise, "and the markets don't usually like complexity", adds Tobagi. However, the investment strategist feels that the macroeconomic situation of growth and inflation is moderate, but positive, and "would tend to favour stocks as an asset class". He notes that in recent years even some of the most traumatic political events "didn't have a negative impact on the stock markets".

According to the experts, the Trump presidency could introduce a further element of volatility. Fiorentini (Credit Suisse) is convinced that to build up a portfolio, investors should pay particular attention to diversification. It is important to concentrate on "carefully considered investment areas, maybe with an impact in the longer term and a strong focus on correlations, which might increase. So in portfolios we prefer to see instruments that have few correlations in the traditional markets, such as thematic funds (infrastructure, water, robotics, cybersecurity) and alternative instruments", adds Fiorentini. Meda, from Banor, recommends "a prudent approach with under-weighting on the main indices. Investors should select sound stocks and those with prospects for improvement. For example stocks linked to the domestic economy in Europe, financial stocks in the US and, in general, stocks benefiting from the increased expenditure by the middle classes in the emerging markets, China first and foremost". Comgest's Berglund also views stock picking as vital, and advises investors to invest in market-leading companies with low debt levels.

Historical events that have had an impact on the S&P 500 index