UOB Investment Insights

Monthly Market Views

October 2019

Trump impeachment inquiry: what it means for investors

Key takeaways

- The formal impeachment inquiry into US President Donald Trump initiated by House Speaker Nancy Pelosi marks the return of impeachment risk after the Trump-Russia collusion investigation.
- While the odds for Trump's removal from office remain low, political risk could add to global uncertainty.
- Against a backdrop of heightened political and economic uncertainty, investors should review their portfolio and reduce any excessive risk.

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Risk of impeachment

Impeachment fever returns

On 24 September 2019, US House Speaker Nancy Pelosi launched a formal impeachment inquiry into US President Donald Trump for enlisting Ukraine's help for his own political gain. The key thrust of the Democrat-led investigation rests on revelations from a leaked July phone transcript that Trump had pressured Ukrainian President Volodymyr Zelensky to investigate former Vice President Joe Biden, a potential 2020 presidential challenger, as well as his son Hunter, for alleged corruption.

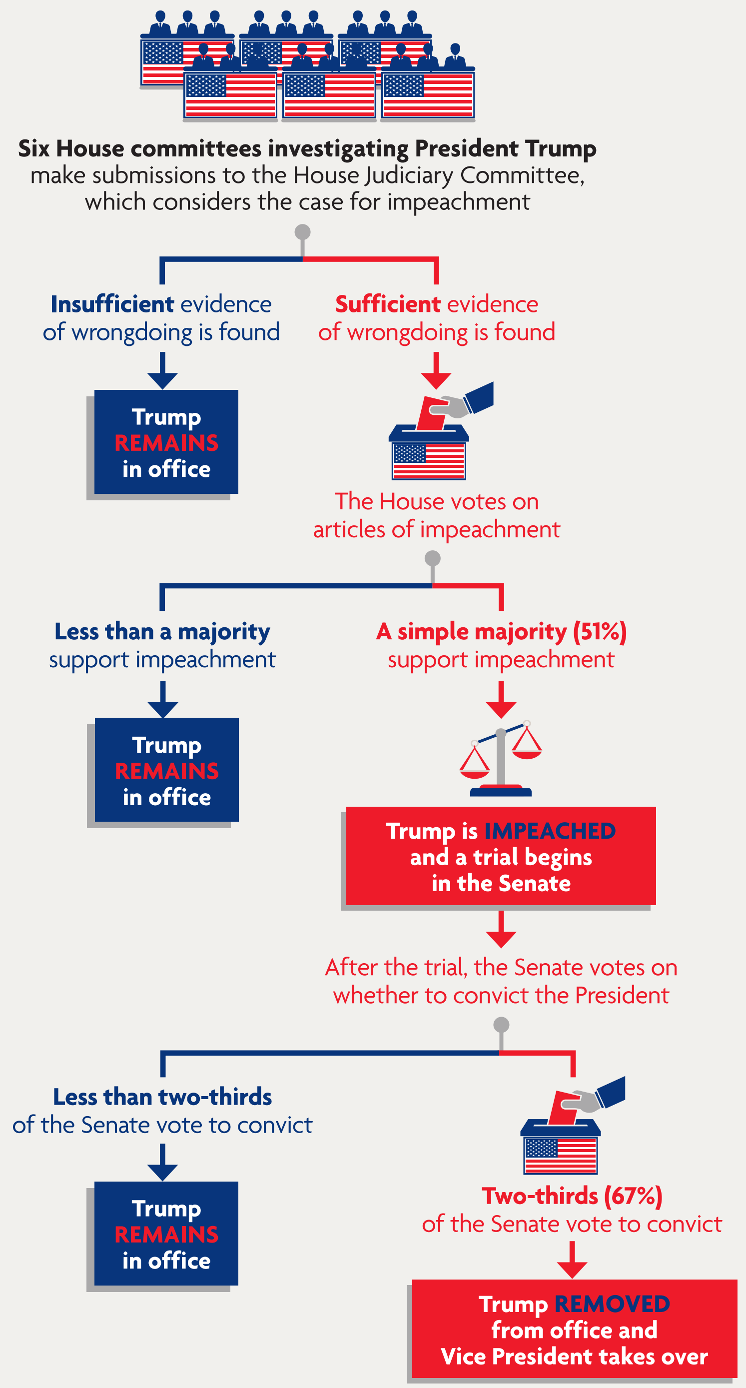
The previously moderate Pelosi had, up until recently, resisted calls for an impeachment without enough facts and bi-partisan support. Her turnaround suggests that the political tide has shifted.

... But the odds for Trump's removal remain low

Impeachment is a multi-step process

The path towards impeachment consists of multiple steps. Once the process is kick-started by the impeachment inquiry, the House committees will launch investigations on the president. If sufficient evidence of wrongdoing is found, the House needs a simple majority (more than 50%) to pass the articles of impeachment. Thereafter, an impeachment trial will be held before the Senate vote, where a two-thirds majority is required to remove a sitting president. Pelosi's activation of the impeachment inquiry into Trump marks the start of the impeachment process.

What happens next in impeachment process?



Source: Donald Trump: How could he be impeached, BBC News, 24 September 2019

Republicans still control the Senate

The Democrats' control over the House's various committees has enabled them to launch probes into Trump's administration. However, they would still need enough crossover votes from conservative Republican senators to remove Trump from office. It is unlikely that the Democrats would be able to secure the two-thirds majority vote as Trump continues to retain strong support among his base in the Republican-dominated Senate.

No US president has ever been successfully impeached

Throughout US history, no US president has been successfully removed from office by impeachment. While Andrew Johnson and Bill Clinton were actually impeached, both were acquitted by the Senate and managed to hold on to office. The impeachment process against Richard Nixon was cut short when he resigned.

Therefore, based on historical precedent, the odds for Trump's removal from office by impeachment remain low.

Investment implications of a Trump impeachment

As the calls for Trump's impeachment intensify, what is the impact on markets?

Political events tend to be short-term noises

If history is any indication, impeachment attempts are mere blips on the investment radar. During Bill Clinton's political scandal, the S&P500 rose 30% between January 1998 and February 1999, fuelled by a thirst for internet stocks. In the 1970s, Richard Nixon's Watergate affair led to calls for his impeachment and this culminated in his resignation. Though financial markets fell during this period, it was largely due to the oil crisis that tipped the US into recession.

... However, impeachment proceedings could weigh on Trump's flagship policies

The rising political heat in Washington can have spill-over effects on Trump's key trade policies - the trade tariffs on China and the US-Mexico-Canada Agreement (USMCA).

US-China trade war

Impeachment proceedings could alter the dynamics of the ongoing trade spat with China and complicate negotiations – should the Trump administration continue to take a hard stance or opt to make concessions and cut a deal? The deepening rift between Trump and the Democrats could lead to a complicated political calculus for his administration. This adds another layer of complexity and unpredictability to the outcome of negotiations with China.

USMCA

The impeachment process could also leave the fate of the USMCA hanging in balance. One of Trump's 2016 election promises, the USMCA needs the support from the House Democrats. The investigation into Trump is likely to delay the passage of the USMCA until after the 2020 presidential elections.

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Reduce excessive risk to weather the uncertain economic climate

In the face of slowing global economic growth and political uncertainty in Washington, investors should review their portfolio and ensure the investment strategy is still relevant to current market environment. Such approach will allow investors to better navigate volatility while capturing selected opportunities in the market.

In current environment, **bonds** are likely to hold up well as central banks are likely to remain dovish. We prefer exposure to **short-to-medium duration**, rather than long-duration bonds. At the current price level, the long-end rates may have reflected overly bearish economic outlook and too much optimism about US Federal Reserve (Fed)'s future rate cuts. Positioning in short-to-medium duration bonds will hedge against the possibility that the Fed could disappoint the market if it holds back on more aggressive rate cuts.

Within the equities space, we prefer investing in ideas with longer-term growth drivers such as **global healthcare**, **artificial intelligence and innovation**, **as well as China**. We also prefer equities with a defensive tilt or lower drawdown characteristics, such as **US consumer staples**.

To benefit from the looser monetary policy environment which supports both fixed income and equity prices, consider the **UOB Risk First bento** solutions as well as a multi-asset income strategy. The diversification approach offered by these strategies will provide better downside protection and capturing opportunities without undertaking excessive risk.

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Economic Drivers and Risks

Economic drivers

Global growth

The IMF downgraded its forecast of global GDP growth to **3.0% in 2019[1] from its earlier 3.2% forecast**, citing ongoing trade tensions as an overhang. However, a recession is still not expected in 2019.

Inflation and Central Banks

Central banks have adopted a **dovish tone**. The Fed did another **25bps "insurance cut"** last month. The ECB announced a perpetual EUR 20billion/month bond buying programme in September, while the BoJ is likely to announce more stimulus measures this month.

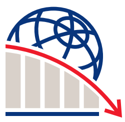
Corporate earnings

In 2019, strong personal consumption supported by a healthy jobs market should continue to drive the **positive trend** in corporate profits. Global earnings growth is expected to rise around **8% in both 2019 and 2020**.

Risks

US Policy Uncertainties

The US continues to engage many countries in **trade disputes**, such as China, Japan and the European Union, thus creating a drag on global growth. At the same time , it remains actively **entangled in geopolitical tensions** with North Korea and the Middle East. The upcoming **2020 Presidential and Congressional elections** further add to the uncertainty as political parties continue to vie for power.



Global Growth Slowdown

After 10 years of economic expansion, the global economy is entering a **late-stage expansion cycle**. Despite "insurance cuts" from the Fed and the ECB, global economic growth will remain positive but likely face a further slowdown.

China Policy Missteps

Markets are expecting China to stimulate its economy through **(i) currency controls, (ii) monetary stimulus and (iii) fiscal stimulus**. China is one of the few major economies that still has the ability to conduct fiscal stimulus, which the broader Asian region is relying upon. If China enacts the wrong policies, it could have a profound negative impact on Asia as a whole.

[1] World Economic Outlook, IMF, October 2019

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Asset Class Views

Asset Class	Subclass	View	VTAR framework	Rationales/Drivers
Equities	US	N	V T A R	Valuations are expensive, prolonged trade negotiations could hurt consumer and business sentiments due to the ongoing uncertainties.
	Europe	–	V T A R	Valuations and trends are attractive relative to the US. However, growth is slowing and volatility is expected to remain high due to political uncertainties.
	Japan	N	V T A R	Attractively valued, although global trade tensions are weighing on business sentiment. The consumption tax hike scheduled for Oct'19 remains a risk.
	Asia (ex-Japan)	+	V T A R	The downward earnings trend has stabilised and P/E is relatively cheaper than DM. Chinese stimulus expected to provide relief to US-China trade tensions.
	EM (ex-Asia)	+	V T A R	Valuations are attractive relative to DM peers. Expectations of Fed rate cuts and rangebound oil prices will sustain equity returns in 2019.
Fixed Income	DM Sovereigns	+	V T A R	Fed, ECB and BoJ are all expected to remain dovish with further monetary easing in H2 2019. US Treasuries offer better value than other DM government bonds.
	DM IG	N	V T A R	IG yield spreads have narrowed year-to-date as investors preferred quality assets to ride through equity market volatility.
	HY	–	V T A R	HY offers a relatively better yield pick-up but market volatility is likely to remain high, which will likely result in a high risk-low reward trade-off.
	EMD USD	N	V T A R	Spreads have narrowed after this year's rally. Easing in global central banks provides support to EMD USD. Prefer Asian investment-grade bonds.
	EMD LCY	N	V T A R	EM sentiment is likely to improve if the Fed remains supportive of economic growth. However, EM currencies, led by CNY, could weaken against the USD.
Commodities	Gold	+		The Fed's potential rate cuts are positive for Gold. China's reallocation of reserves into Gold will provide a support level. Target USD 1,650/oz by Q2 2020.
	Oil	N		Tensions in the Middle East could support oil prices in the short term. However, the upside is capped by concerns over slower global growth.
Currencies	USD	N		The USD is expected to hold up in the near term, but could face headwinds if the Fed continues cutting rates. The SGD is expected to depreciate against USD.

– – Negative   – Slightly Negative   N Neutral   + Slightly Positive   + + Positive

V=Value   **T**=Trends   **A** =Activity   **R**=Risk

● Positive   ● Neutral   ● Negative

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High-conviction strategies

Conviction	VTAR framework	Proposition	Risk
Global Quality Equities		Global quality equities tend to outperform broad equity markets over longer investment cycles.	Relatively expensive valuations could increase the probability of short-term corrections. However, the quality companies tend to better weather the economic slowdown, limiting the likelihood of large corrections in quality stocks.
US Consumer Staples		US Consumer Staples is a sector that offers a more defensive positioning than many other US equity sectors, and thus is less likely to experience the same level of drawdowns in a risk-off scenario.	Certain sectors, such as Beverages and Tobacco, could face regulatory risk to reflect the change in social norms and acceptable practices. Technological disruption could cause companies that fail to keep up to fall behind the competition.
EM Equities		Broad EM equities are supported by stronger fundamentals and attractive valuations.	An unexpected surge in USD strength could cause a retreat from EM equities, as seen in the Turkey situation last year. A worsening of US-China trade tensions could also lead to higher market volatility. Another escalation, such as the recent increase in tariffs by both sides, can cause near-term pullbacks.
Unconstrained Bond Strategy		A dovish stance from major central banks will keep key global interest rates low. An unconstrained bond strategy tends to enhance the return over the broad fixed income market.	An inflation overshoot will send bond yields higher, which will be the major risk to fixed income in general. However, inflation-linked securities such as TIPS will be less affected in such an event.

V=Value **T**=Trends **A** =Activity **R**=Risk
● Positive ● Neutral ● Negative ● NIL

Megatrends

Conviction	VTAR framework	Proposition	Risk
Global Healthcare		Healthcare is a structural growth story driven by long-term growth in an aging global population. In the medium-term, we expect drug approvals and an increase in M&A activity to be catalysts for a sector re-rating.	Policy uncertainty could weigh on sentiment for the sector. The Medicare-for-all proposed by Democrat Presidential candidate Bernie Sanders could lead to volatility, but the probability for the programme to pass is low at the present time. This risk will likely be mitigated in the long-term as a growing silver segment should contribute to stronger increase in demand.
Chinese Equities		Chinese equities are underowned by global investors, and provide a good risk-reward and diversification benefits.	A US-China trade war remains a key risk in the near term and is likely to negatively impact China's economic growth. Financial deleveraging could continue to put pressure on growth and lead to higher risks of policy missteps.
AI & Innovation		Artificial Intelligence (AI) has the ability to drive multi-fold increases in productivity by utilising big data and powerful computing hardware to accurately and reliably solve real-world problems with little human input.	Policy and regulatory uncertainty is a key risk to watch for. As AI permeates more and more into people's daily lives, questions about safeguarding individual privacy and appropriate use of such tools will surface. Regulators may step up efforts to curb the uses and applications, while differing standards from various countries can create barriers to universal adoption.

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Rates and FX Forecasts

Key Currencies					Key Rates (%)				
	4Q19F	1Q20F	2Q20F	3Q20F		4Q19F	1Q20F	2Q20F	3Q20F
USD/SGD	1.40	1.41	1.42	1.42	**USD**	1.50	1.50	1.50	1.50
EUR/SGD	1.54	1.55	1.59	1.62	**EUR**	0.00	0.00	0.00	0.00
GBP/SGD	1.68	1.69	1.72	1.73	**GBP**	0.75	0.75	0.75	0.75
AUD/SGD	0.97	0.97	0.99	1.01	**AUD***	0.75	0.75	0.75	0.75
JPY/SGD x 100	1.32	1.34	1.38	1.38	**JPY**	-0.10	-0.10	-0.10	-0.10
NZD/SGD	0.90	0.90	0.92	0.94	**NZD**	1.00	1.00	1.00	1.00
SGD/CNY	5.14	5.14	5.14	5.14	**CNY**	3.90	3.65	3.65	3.65
					SGD	1.45	1.45	1.35	1.35

* Last updated on 01 October 2019
Source: UOB Global Economics & Markets Research, 13 September 2019

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