Partner Talk®

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President Trump and the Futility of Predictions

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In the months leading up to the 2016 presidential election, we heard from many of our clients who were concerned about the possible impact of a Trump victory on the economy and the markets. They wanted to know if there were steps that PMA would take in advance as a hedge against a Trump win or actions we might anticipate after the fact as markets reacted.

Consistent with our 35 year record and investment philosophy, we responded that we did not have the capability to forecast either the outcome of this election or the market's reaction to it. While we believe that it is appropriate to reevaluate portfolio allocations and risk appetite in reaction to changes in one's own circumstances, we do not believe that it is ever wise or effective to speculate on anticipated short-term market reactions to unpredictable events. For these reasons, we advised clients to sit tight.

And, famously, it turns out that the experts who did make predictions were wildly incorrect.

Consider that in the days leading up to November 8th, we were told that Donald Trump would lose convincingly; that his terribleness as a candidate would deliver substantial defeats to vulnerable Republicans in the House and Senate; that this historic rout would splinter the Republican party into at least two factions and set it back for generations; that the financial markets were, if not enthusiastic about Hillary Clinton, at least not scared of her; and that a Donald Trump victory would cause the markets to tailspin.

There were no experts of whom we are aware who predicted that Donald Trump would win the Republican nomination and the presidency; that the Republicans would retain a majority in the House and Senate; and that the Democrats would wake up Wednesday in shock and despair. In fact, even the futures market got it wrong, predicting Election Day evening that the Dow Jones Industrial Average would plummet 700 points, when in fact it ended the week 700 points up.

If there is a silver lining to what was widely regarded as one of the least uplifting elections in history, which made the Bush-Kerry election of 2004 look like an English tea party, perhaps it will be the sharp drop in esteem in which the public holds the profession of prediction experts. Popular authors are now advocating skepticism to the public; for example, Michael Lewis, author of *Moneyball* and the recent *The Undoing Project,* writes that the certainty exuded by consultants at McKinsey & Co. when they make forecasts about the future price of oil, is in fact "a sign of fraudulence."

Accordingly, we offer the following as observations only and certainly not as predictions:

One, there are basic economic contradictions at the core of many Trump's economic policies that will need to be resolved. During a speech in 2014, Stephen Bannon, Trump's chief strategist, said that he was a hyper-capitalist who wanted to bring capitalism to the inner cities and end the practice of protecting large corporations when they get into trouble. At the same time, he is a fervent "anti-globalist", committed to protecting American corporations from allegedly unfair trade practices or, as we just saw, strong-arming companies like Carrier to stay in the United States. Cutting corporate tax rates and easing regulatory burdens while threatening CEOs and interfering in their capital and labor decisions is like putting air in your tires while locking the steering wheel.

Two, the markets will not ignore unsustainable budget deficits forever. Cutting taxes while increasing spending on infrastructure projects, in the face of already enormous fiscal strains, will spook both the equity and bond markets. The spending will have to be done wisely and efficiently and on the right projects and there will have to be some off-setting revenue, either now or in the future.

Three, the long predicted rise in interest rates may finally be here. But to say that interest rates will rise says nothing about when precisely they will rise, how sharply they will rise, and which interest rates will rise, let alone the relationship between rate changes and potential increases in inflation.

Four, no one yet understands the full details of Trump's plans regarding immigration, trade agreements, international defense arrangements or strategic alliances, let alone their potential ramifications for the economy or the markets.

Making campaign promises is easy; governing responsibly is hard. We do not know how President Trump ultimately will govern, or how the markets will react to his policies, but, as President Obama said during his initial meeting with Trump after the election, we hope he is successful because "if you succeed, the country succeeds."