OUR THOUGHTS ON ALLOCATING FOR A PRESIDENT TRUMP WORLD

Wisdomtree EU
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In a nutshell, we believe a Trump victory – especially coupled with a Republican Congress – is very good for US mid cap, US small cap and overseas markets, such as Japan, that are sensitive to a strong USD/weak domestic currency. Shortly after the US Election results, the market began to immediately discount expected policy changes next year that will likely lead to a pro-growth economic agenda. That agenda includes cuts in individual and corporate tax rates, increased spending on defence and infrastructure, and a rollback on energy (good for energy stocks and industrials), and regulations including Dodd-Frank (good for financials) and the Affordable Care Act (good for small businesses).

This is raising expectations for faster GDP and private sector job growth, higher inflation, higher interest rates, and, in the immediate future, a stronger Dollar.

How can investors take advantage of this bullish environment?

The focus is on US equity funds and Japanese hedged equity funds. We outline below some of the key sectors and strategies which can be interesting to investors.

Focus on Core Dividend Growth (DGRW)

As rates have declined in the first half of the year, we’ve seen success with our core dividend strategies. However, as the macro environment changes it is important to focus on the rising rate environment and investors may look at funds like the WisdomTree US Quality Dividend Growth UCITS ETF (DGRW).

We believe that DGRW is one of the best placed large cap US equity strategies in the post election environment. In the first eight trading days we saw the US market rotate away from Utilities, Real Estate, Consumer Staples and Telecom, and towards Financials, Industrials and Consumer Discretionary. DGRW is overweight by 18% Industrials and Consumer Discretionary relative to the market, underweight Financials by roughly 10%, and underweight Utilities, Real Estate and Telecom by roughly eight percentage points – it has virtually 0% exposure to those three sectors.

Given that rising interest rates should create a headwind for the higher yielding, more defensive parts of the market, we think investors should tilt towards “quality” in their US large cap exposure, towards companies that in aggregate have less leverage than the market as a whole. DGRW gets that exposure to total shareholder yield that’s higher than the market, and we feel that it is well positioned for this stage of the cycle.

Trump’s Pro-Growth Agenda Will Likely Benefit US Mid and Small Cap Stocks

If Trump’s plan to cut tax and regulation passes the Republican Congress, it will likely result in greater economic activity, industrial production, investment and consumption in the US. This will benefit mid and small cap companies that derive most of their sales and profits in the US, and who are less impacted by a rising Dollar overseas.

In our view mid and small caps is the place to be, and we believe that the WisdomTree US SmallCap Dividend UCITS ETF (DESE) is well positioned. In the US mid cap and small cap areas there are interesting macro themes to consider. In particular, the market has already priced in the discount of pro-growth policies in the US (tax cut and regulatory reform) to pass in to 2017, and that this will benefit small and mid cap companies.

+ Faster GDP growth, job growth, and wage gains may well translate into faster revenue and earnings growth for US companies with more exposure to the US consumer and the US economy

+ If corporate taxes are reduced, mid and small companies which benefit the most will be those that receive the lion's share of the profits inside the US

+ Small and mid companies are less impacted by the headwind of a rising Dollar

Japan

One international equity market that has rallied since the election as its currency has weakened, has been Japan. Our WisdomTree Japan Equity UCITS ETF USD Hedged (DXJ) was up about 6.5% since the election[1], and is separating from both other international developed and emerging markets. This happened during a period when the Yen declined about 5.5% versus the Dollar.

We expect Japan will be a continued focus in terms of international equity markets for 2017, reflecting our view that interest rates and the US Dollar is headed higher from current levels, and that, with the BOJ holding the line on the 10-year yield in Japan, that the Yen still has room to weaken from here.

At a macro level, since rates bottomed in the US on 8 July, DXJ has been more sensitive to the back-up in the 10-Year US Treasury Yield than any of the sectors of the S&P 500. DXJ is up 30% since then[2] – and is down just 2.9%[3] for the year. If the US 10-year yield goes to 3.0%, the Yen may well test the 125 range. With such large scale macro shifts Japan may be one of the best performing major equity markets for 2017.

In Summary

We believe the best performer in 2017 will be US equities. Specifically, we think small caps and mid caps have a lot to gain from some of Trump's legislation likely to be imposed (and revoked). However, if looking at US large cap, the focus should be on quality dividend strategies.

In other parts of the world, we think Japan is a bright spot especially looking at the recent depreciating Yen. To get 'pure' exposure to Japan equities without the USD/JPY currency fluctuation, we believe our range of currency hedged Japan ETFs could suit this market environment.

Source

[1] WisdomTree, as of 28/11/2016

[2] WisdomTree, as of 28/11/2016

[3] WisdomTree, as of 28/11/2016

View the online version of this article here.

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