MORNING BRIEFING
January 24, 2017

The First 100 Hours

See the collection of the individual charts linked below.

(1) Andrew Jackson's song. (2) Power to the forgotten people. (3) Trump is channeling Jackson, FDR, JFK, and Perot. (4) Jury still out on extent of Trump's protectionism. (5) DJT is no JFK on world stage. (6) Isolationism vs interventionism. (7) Foxconn pays the entry price. (8) Merkel seeks compromises with Trump. (9) China's sore point. (10) Mexico getting stomped by 800lb gorilla north of the border. (11) NAFTA will be renegotiated one way or another.

Trump World: Hail to the Chiefs. "Hail to the Chief" is the official Presidential Anthem of the United States. The song is played when POTUS appears at public events. Andrew Jackson was the first living President to have the song used to honor his position in 1829. Many commentators have observed similarities between Jackson and our new President Donald Trump. Like Jackson, Trump is opposed to the status quo and is intent on stirring things up. Like Jackson, Trump is a populist who believes that the government should use its powers to do more for ordinary people than for the ruling class.

As Trump said in his Inaugural Address on Friday, "What truly matters is not which party controls our government but whether our government is controlled by the people. January 20th 2017 will be remembered as the day the people became the rulers of this nation again. The forgotten men and women of our country will be forgotten no longer." He added, "From this moment on, it's going to be America First. Every decision on trade, on taxes, on immigration, on foreign affairs, will be made to benefit American workers and American families."

The focus on "forgotten" Americans is reminiscent of FDR, who claimed that his New Deal was aimed at helping the "forgotten man." FDR first said so in a 1932 radio address: "These unhappy times call for the building of plans that rest upon the forgotten, the unorganized but the indispensable units of economic power, for plans like those of 1917 that build from the bottom up and not from the top down, that put their faith once more in the forgotten man at the bottom of the economic pyramid."

The word "protect" appeared seven times in Trump's speech on Friday. It certainly wasn't a speech for conservatives, who would have liked to hear the new President champion smaller government with fewer powers, though he previously has pledged to reduce government regulations. In other words, Trump is out of step with the traditional Republican values of limited government, economic freedom, and free trade. He intends to use the power of the government and his bully pulpit to achieve his populist agenda. He has already bullied a few major corporations to invest more in the US.

The jury is still out on the extent of his trade protectionism. My hunch is that he will push for fairer trade deals without crossing the line into outright protectionism. My hunch is that any large corporation that agrees to invest at least $1 billion in the US and create at least 1,000 jobs for Americans will be removed from Trump's tweet hit list.

Trump's speech also was reminiscent of JFK's Inaugural Address, though in a mirror-image fashion. JFK announced that the US would be very active on the international stage:

“Let every nation know, whether it wishes us well or ill, that we shall pay any price, bear any burden, meet any hardship, support any friend, oppose any foe to assure the survival and the success of liberty. This much we pledge--and more. To those old allies whose cultural and spiritual origins we share, we pledge the loyalty of faithful friends. United there is little we cannot do in a host of cooperative ventures. Divided there is little we can do--for we dare not meet a powerful challenge at odds and split asunder. To those new states whom we welcome to the ranks of the free, we pledge our word that one form of colonial control shall not have passed away merely to be replaced by a far more iron tyranny. We shall not always expect to find them supporting our view. But we shall always hope to find them strongly supporting their own freedom--and to remember that, in the past, those who foolishly sought power by riding the back of the tiger ended up inside. To those people in the huts and villages of half the globe struggling to break the bonds of mass misery, we pledge our best efforts to help them help themselves, for whatever period is required--not because the communists may be doing it, not because we seek their votes, but because it is right. If a free society cannot help the many who are poor, it cannot save the few who are rich.

“To our sister republics south of our border, we offer a special pledge--to convert our good words into good deeds--in a new alliance for progress--to assist free men and free governments in casting off the chains of poverty. But this peaceful revolution of hope cannot become the prey of hostile powers. Let all our neighbors know that we shall join with them to oppose aggression or subversion anywhere in the Americas. And let every other power know that this Hemisphere intends to remain the master of its own house.

“To that world assembly of sovereign states, the United Nations, our last best hope in an age where the instruments of war have far outpaced the instruments of peace, we renew our pledge of support--to prevent it from becoming merely a forum for invective--to strengthen its shield of the new and the weak--and to enlarge the area in which its writ may run. Finally, to those nations who would make themselves our adversary, we offer not a pledge but a request: that both sides begin anew the quest for peace, before the dark powers of destruction unleashed by science engulf all humanity in planned or accidental self-destruction.”

Trump’s spin on the geopolitical role of the US is pithier and downright isolationist:

“We’ve made other countries rich while the wealth, strength and confidence of our country [have] dissipated over the horizon. One by one, the factories shuttered and left our shores with not even a thought about the millions and millions of American workers that were left behind. The wealth of our middle class has been ripped from their homes and then redistributed all across the world. But that is the past, and now we are looking only to the future. We assembled here today are issuing a new decree to be heard in every city, in every foreign capital and in every hall of power. From this day forward, a new vision will govern our land. From this day forward, it’s going to be only America first.”

Needless to say, there was no mention of any alliance for progress with our neighbors south of the border.

Yet love him or hate him, Trump’s in-your-face wheeler-dealer style continues to pay off. Consider the latest developments:

(1) *Foxconn.* Reuters reported on Sunday that Foxconn, the world’s largest contract electronics maker, is considering setting up a display-making plant in the US. The investment would exceed $7 billion and might create 30,000-50,000 jobs. Foxconn business partner Masayoshi Son, head of Japan’s SoftBank Group, talked to Foxconn’s Chairman and Chief Executive Terry Gou before a December meeting Son had with Trump. As a result of the meeting, Son pledged a $50 billion of investment in the US.

(2) *Germany.* Reuters reported on Saturday that Germany's Chancellor Angela Merkel "vowed on Saturday to seek compromises on issues like trade and military spending with U.S. President Donald Trump, adding she would work on preserving the important relationship between Europe and the United States. 'He made his convictions clear in his inauguration speech,' Merkel said in remarks broadcast live, a day after Trump vowed to put 'America first.'"

That's awfully gracious of the Chancellor after Trump's scathing attack on January 15, in which he said that the European Union is a "vehicle for Germany" and ranked the German Chancellor alongside Vladimir Putin as potentially troublesome. He said that while he had great respect for Merkel, his trust for her "may not last long at all." He said Germany's dominance of the EU showed why the UK was "so smart" to get out. "I think she made one very catastrophic mistake and that was taking all of these illegals, you know all the people from wherever they come from," he said. "And nobody even knows where they come from. So I think she made a catastrophic mistake, very bad mistake."

Trump also raised fresh fears for the future of NATO by saying that while it is "very important to me" the alliance is "obsolete." He said: "Only five countries … are paying what they're supposed to."

(3) *China.* Trump clearly has found the right button to push to get the Chinese leaders' attention on both trade and geopolitical issues that he wants to negotiate with them. Challenging their "One China" policy is certainly agitating them. According to Beijing, Taiwan and Mainland China are inalienable parts of a single China. Taiwan is viewed as a wayward province, to be brought under its control by force eventually, if necessary.

On Saturday, Chinese foreign ministry spokeswoman Hua Chunying told a regular briefing in Beijing, "We urge the new administration to fully understand the high sensitivity of the Taiwan issue and to continue pursuing the one China policy," Reuters reported. Hua called the policy the "political foundation" of future relations between the United States and China. She also reiterated China's position on the South China Sea, saying the United States should not meddle in issues of China's sovereign territory.

(4) *Mexico.* Despite all the abuse that Trump has heaped on Mexico, the country's President Enrique Peña Nieto said on Friday that he wanted to strengthen relations with Trump, whose attacks against the country raised fears of a major economic crisis and battered its currency. Trump said on Sunday that he will begin renegotiating the North American Free Trade Agreement (NAFTA) during scheduled meetings with Peña Nieto (on January 31) and with Canadian Prime Minister Justin Trudeau.

(5) *Japan.* The new Trump administration said on Friday that its trade strategy to protect American jobs would start with withdrawal from the 12-nation Trans-Pacific Partnership (TPP) trade pact. Japanese Prime Minister Shinzo Abe said on Monday that he believes Trump understands the value of free trade, but that he will pursue deepening the President's understanding of the TPP pact's strategic and economic importance.

Mexico: North of the Border. Investors will be listening for a "giant sucking sound" in the coming months. Candidate Ross Perot asserted during the 1992 presidential campaign that trade liberalization would cause other countries to suck up US jobs. Under President Trump, the sucking sound will most likely happen not in the US but abroad, particularly south of the border.

Before Trump burst onto the political scene, Mexico didn't get much attention in the US. During his campaign, Trump launched numerous attacks on Mexico over jobs, immigration, and trade. Since Election Day, Trump has mostly focused on stopping US companies from sending jobs to Mexico. Next, he aims to renegotiate NAFTA with both Mexico and Canada, as noted above. Meanwhile, as a result of his unremitting attacks, the Mexican peso has plunged. That could backfire if the weaker peso translates into a more competitive export market for Mexico and a more leftist government.

Since Election Day on November 8, the peso has fallen by 15% (*Fig. 1*). Mexico's non-oil exports, in pesos, are up 27% y/y through November (*Fig. 2*).

Mexico's MSCI stock price index (in pesos), remains on an uptrend, rising 11.9% y/y, but is down 5.0% y/y in dollar terms (*Fig. 3*). Some international investors see an opportunity. In November, Templeton's Mark Mobius argued that Mexican stocks were a bargain thanks to the cheap peso. However, he also expected that Trump's positions on Mexico would soften, which has not been the case so far.

Mexico has enjoyed relatively steady growth in the last couple of years, but the country is now facing challenges from north of the border (*Fig. 4* and *Fig. 5*). Ford pulled the plug on its $1.6 billion investment in Mexico and instead will expand its capacity in the US. The weaker peso is driving up consumer prices (*Fig. 6*). Mexicans took to the streets when the government announced that the price of gas would rise as much as 20% on New Year's Day as a part of the government's plan to end oil subsidies in March. Demonstrations and lootings turned deadly, with stores ransacked and 700 people arrested. Prices of basic necessities including food are expected to surge too. If tortilla prices soar, social unrest could worsen significantly.

A 1/18 poll showed that the approval rating for Mexican President Enrique Peña Nieto fell to 12%, down from 24% in December. The poll showed an approval rating for leftist Andrés Manuel López Obrador's National Regeneration Movement (Morena) of 27%, while only 17% preferred the ruling Institutional Revolutionary Party (in Spanish, "*Partido Revolucionario Institucional,"* or "PRI") party. PRI won five states, while the opposition party won seven states, in the June 2016 regional election. PRI losses included Veracruz, the state with the largest population and fiscal spending, which had always been in PRI control until June's election.

Mexico is likely to retaliate if a border tax is imposed by Trump, though that might not happen if NAFTA is successfully renegotiated. In 2009, Mexico slapped taxes of up to 25% on more than 90 different US farm goods because the US lawmakers delayed the process of allowing Mexican truckers on the US roads, as specified under NAFTA. US growers lost an estimated $70 million revenues in 31 months.

We expect that NAFTA will be renegotiated successfully. Both the US and Mexico have too much at stake to engage in a trade war.

CALENDARS

US. Tues: M-PMI Flash Estimate, Richmond Fed Manufacturing Index, Existing Home Sales 5.538mu. **Wed:** MBA Mortgage Applications, FHFA House Price Index, EIA Petroleum Status Report. (Bloomberg estimates)

Global. Tues: Eurozone, Germany, and France Composite PMI Flash Estimates 54.5/55.4/53.2, Eurozone, Germany, and France M-PMI Flash Estimates 54.8/55.4/53.4, Eurozone, Germany, and France NM-PMI Flash Estimates 53.9/54.5/53.1, Japan Merchandise Trade Balance (yen) 280b, Australia CPI 1.6% y/y. **Wed:** Germany Ifo Business Climate, Current Assessment, and Expectations Indexes 111.3/116.9/105.8. (DailyFX estimates)

STRATEGY INDICATORS

S&P 500/400/600 Forward Earnings (*link*): Forward earnings rose for all three indexes last week and were at record highs for LargeCap and MidCap. SmallCap remains just 0.1% below its record high three weeks ago. The yearly change in forward earnings for all three indexes has been edging higher from six-year lows in early 2016 as y/y comparisons have eased. In the latest week, LargeCap's forward earnings improved to a 25-month high of 6.4% y/y from 5.6%, which compares to a six-year low of -1.8% in October 2015; MidCap's dropped to 6.2% from a 23-month high of 6.3%, which compares to a six-year low of -1.3% in December 2015; and SmallCap's improved to a 27-month high of 10.1% from 9.4%, which compares to a six-year low of 0.3% in December 2015. Growth rates now expected for 2016 and 2017: LargeCap 0.7% and 12.3%, MidCap 1.8% and 12.7%, and SmallCap 6.2% and 15.5%.

S&P 500/400/600 Forward Valuation (*link*): Valuations for these three indexes fell last week, and remain slightly below recent multi-year highs. LargeCap's forward P/E dropped to 17.0 from 17.1, which had matched its 22-month high of 17.1 in early December. That's up from a 15-month low of 14.9 in mid-January, but remains slightly below the 11-year high P/E of 17.2 in February 2015 (when Energy sector earnings were depressed), and well below the record high of 25.7 in July 1999. MidCap's forward P/E slipped to 18.6 from 18.8; that's below early December's 15-year high of 19.2 and compares to a three-year low of 15.0 in January 2016 and a record high of 20.6 in January 2002. SmallCap's fell to 19.5 from 19.9; that's up from a three-year low of 15.5 last February, and compares to a 15-year high of 20.5 in early December and record high of 20.9 in April 2002.

S&P 500 Sectors Quarterly Earnings Outlook (*link*): Q4 earnings estimate revision activity picked up last week for the S&P 500 sectors as companies began reporting earnings. The Q4 consensus rose w/w for three of the 11 S&P 500 sectors, fell for four, and was steady for four. Financials rose 4.4% for the week, followed by gains for Industrials (0.4%) and Consumer Discretionary (0.1). Sectors with w/w declines in their Q4 forecasts: Energy (-3.8), Materials (-0.3), Health Care (-0.2), and Tech (-0.2). The S&P 500's Q4-2016 EPS forecast rose 14 cents w/w to $30.90, but is down 2.0% from $31.53 at the end of Q3. That represents a forecasted pro forma earnings gain of 6.3% y/y, up from 6.2% a week earlier and down from 8.3% at the end of Q3. Since the end of Q3, Q4 estimates are higher for 2/11 sectors and lower for 9/11. Financials' Q4 forecast has risen 4.9%, while Tech's has gained 0.8%. Materials is down the most (-13.2), followed by Real Estate (-8.7), Utilities (-7.0), Industrials (-5.3), and Consumer Discretionary (-4.2). The S&P 500's Q4-2016 forecasted earnings gain of 6.3% y/y would be its second straight gain after four declines and compares to Q3-2016's blended 4.3%, Q2-2016's -2.1%, Q1-2016's -5.0%, Q4-2015's -2.9%, Q3-2015's -0.8%, Q2-2015's 1.3%, and Q1-2015's 2.2%. Three of the 11 sectors are expected to beat or match the S&P 500's y/y earnings gain of 6.3% in Q4-2016, but analysts expect a y/y earnings gain in Q4-2016 for 7/11 sectors. That forecast is below the 9/11 sectors rising in Q3-2016, which was the best since Q1-2015 and compares to 6/10 rising during the quarters from Q4-2015 to Q2-2016. In early January, Energy had been expected to turn in positive y/y growth in Q4-2016 for the first time since Q3-2014, but it's slightly negative now. The latest forecasted Q4-2016 earnings growth rates vs. their blended Q3-2016 growth rates: Financials (17.2% vs. 8.5%), Utilities (10.9, 10.9), Tech (7.9, 11.5), S&P 500 (6.3, 4.3), Consumer Staples (6.2, 7.0), Health Care (5.7, 7.6), Materials (5.6, 10.9), Consumer Discretionary (1.1, 8.6), Telecom (-0.8, -1.8), Real Estate (-0.9, 2.4), Industrials (-2.4, 4.0), and Energy (-3.0, -67.5).

S&P 500 Earnings Season Monitor (*link*): With 13% of S&P 500 companies finished reporting Q4-2016 results, their revenue and earnings surprise metrics are weaker than at the comparable point of the Q3 season. On a mixed note, their y/y earnings growth comparisons are stronger, but y/y revenue growth has slowed. Of the 63 companies in the S&P 500 that have reported, 64% exceeded industry analysts' earnings estimates by an average of 3.8%; they have averaged a y/y earnings gain of 10.7%. At the same point in Q3-2016, a higher percentage of companies (83%) in the S&P 500 had beaten consensus earnings estimates by a larger 7.9% and earnings were up a smaller 4.9% y/y. On the revenue side, 44% beat sales estimates so far, coming in 0.2% below forecast and 2.7% higher than a year earlier. During Q3, a higher 70% were above forecast, which exceeded estimates by 1.2% and rose 4.4% y/y. Q4 earnings results are higher for 81% of companies versus 72% at the same point in Q3, and revenues are higher for 73% versus 72%. These figures will change markedly as more companies report Q4 results, but early data suggest Q2 was indeed the bottom for y/y earnings growth.

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