

August 2017

# Great American Eclipse

On 21 August 2017, a total solar eclipse was visible from within a narrow 113km wide corridor that traversed the US. The path of the Moon's full umbral shadow began in the north Pacific and crossed the US from west to east through 14 states – Iowa just squeezing a 2km<sup>2</sup> corner in – blocking all direct sunlight, turning day into darkness for a little more than two minutes in each place. The Moon's penumbral shadow produced a partial eclipse visible across a much larger area covering most of North America. The previous time a total solar eclipse was visible across the entire US was 1918, and not since 1979 has a total eclipse been visible from anywhere in mainland US. It's also the first eclipse since 1776 whose path fell only in the US. For the impatient, it will not be such a wait for the next, forecast for April 2024, just seven years away.

For those of a prophetic disposition, this recent eclipse belongs to what scientists refer to as the Saros series, which has included eclipses in 1999, 1981, 1963, 1945, 1927, and 1909. Renowned US astrologer Marjorie Orr noted major political events occurring in those years: the impeachment of Clinton, the attempted assassination of Reagan, the assassination of JFK, the atomic bombing of Hiroshima and Nagasaki, the death of Franklin D. Roosevelt, and a period of civil unrest in Chicago that included an attempted assassination of President William Taft. There has been much written of parallels between this recent eclipse and the shenanigans in the White House since Trump's inauguration. Astrologers point out that President Trump was born during a lunar eclipse, which they argue makes him more susceptible to their power. If it is to be believed that eclipses are monumental celestial events with real-world consequences, then the occurrence of the recent total solar eclipse could have major implications, especially given the rollercoaster ride of his early administration.

One doesn't have to believe in the interconnectivity between astrology and real-world events to acknowledge the recent overshadowing of underlying economic data by political headlines. It seems that markets have adapted to sitting perpetually in the umbra or at least penumbra of political headline eclipse. But to what extent do the ongoing political firestorms – occurring with what feels like increasing regularity – have a true impact or lasting effect on underlying economic progress? Which is the main event and which is the side show?

The political impact on markets is complex and rarely easy to measure. Even with politically stable economies, policy change and/or implementation can swing between having a direct or indirect market impact, and range from being short term and temporary to secular. A further variable comes from the transition of political control experienced in much of the developed world, with the US (under Trump administration) a leading example.

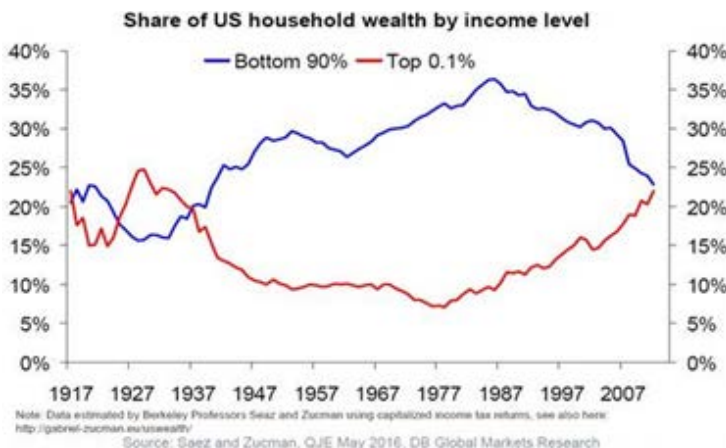
Despite initial expectations that a pro-growth and pro-inflation manifesto would provide strong tailwinds for markets, the inability to 'walk the talk' is arguably seeing markets shrug off what has become a largely stagnant policy implementation program and, albeit with a degree of melancholy, just 'shuffle along' at best. Worse, little policy progress and possibility that some US policies, particularly increasing trade barriers and removal of existing trade treaties, may actually undermine US economic growth, make the controversy surrounding the healthcare/immigration/tax reform debate and the latest addition/purge in the revolving show circus that has become the White House inner-circle, the smaller of our political concerns. Meanwhile our biggest politico-economic concern continues to be the growing potential for US Congress to fail to raise the US debt ceiling, creating a government shutdown and prospects for US Treasury default.

Two of the three branches of government are currently broken. The Republican-led Congress currently views the debt ceiling as a secondary issue and declined to extend their current session to deal with it (having another 1½ month vacation was deemed a higher priority than the welfare of the country). Rather, they are messaging their continuing focus on a healthcare overhaul bill, expanding upon the vast progress they've made over the past seven years. A Republican House minority stated they would force a Treasury default and government shutdown unless their demands that Obamacare was repealed and funding for building the wall across the Mexican border were met. Looking back, we've seen this faction shut down the government for 16 days in 2013 over a similar set of hostage demands, all of which failed. We have little confidence in Treasury secretary Mnuchin's stature and ability to push Congress into raising the debt ceiling. And with a career epitomized by defaulting on investors, it's hard for us to foresee President Trump having anything to

add to the situation other than finding a way to blame Hillary Clinton and Obama for the ensuing chaos.

While markets were positive about Trump's policies at first, now they are increasingly sceptical. It is hard to say whether current moves are simply an inertia – 'stopping an oil tanker' analogy pertinent – or self-driven. The transition from what has been a more active interventionist experience post GFC to a more classical 'laissez faire' instance of market dynamics is not an overnight one.

Ray Dalio of Bridgewater recently commented that "politics will probably play a greater role in affecting markets than we have experienced any time before in our lifetimes but in a manner that is broadly similar to 1937." By 1937 the Federal Reserve (Fed) had reduced interest rates to zero following the Great Depression and the US economy saw vast increases in money supply, high debt levels and a stock market rally. Populism had increased as wealth gaps remained high. Like today, the top 0.1% of households still held more wealth than the bottom 90%. This period saw few high paying jobs and many low paying jobs, resulting in fine looking averages but class divisions high, stirring populist uprisings.



Besides the obvious, other parallels exist: the Moscow Trials opened as 17 Communists were accused of trying to take control of the government; the first solar eclipse to exceed seven minutes in over 800 years was visible in the Southern hemisphere; the Ku Klux Klan appeared to gain

sympathy within the US government as Supreme Court Justice Hugo Black was forced to refute claims he was a member; General Motors finally recognized the United Auto Workers Union; and geo-political risks such as the first Japanese Kamikaze arriving in Croydon airport in the UK while the Nazi Luftwaffe bombed Spain in the Spanish Civil War. For each of these 'inputs' modern day examples are easily and tragically interchangeable (Charlottesville, ISIS, intervention in Syria, etc., etc.).

Then, like now, the Federal Reserve began hiking interest rates, knowing it to be important to create a more sustainable environment for growth and economic progress. Today, however, the environment has been one arguably less conducive to a swift succession of hikes lest the fragility of economic recovery be tested too far... as such the Fed (and RBA) left rates unchanged at recent meetings. For some time we have held the view that rate hikes would be slower to come than markets anticipated. That view has become a more widespread expectation today, considering US political disorder and a succession of soft Consumer Price Index prints. More recent payroll gains corroborate the last 7+ years of stable and steady jobs growth, although this story remains non-inflationary. Wage pressures will eventually become a concern; not least of all as average hourly earnings grow at 2.5% and the ratio of job seekers to number of available jobs moves from 9:1 toward 1:1. Just not this year, and maybe not 2018 either. We believe core inflation will remain contained until wage gains move beyond 3%, a level not seen for eight years.

Now drawing Noah-like parallels, some more extreme observants remain steadfast in their view that the eclipse was an unheeded warning for repentance (wrongly interpreted by the masses as an invitation to party). Those with anti-Trump political leanings further extend this to a message that the White House circus cannot continue. To boot, the ferocious Hurricane Harvey, uncanny in its timing in coming out of nowhere so soon after the eclipse, fuelled those same god-fearing disciples to wag 'told you so' fingers at the 'punishment' now being unleashed on America. Connection, conspiracy, or coincidence...?

Unless otherwise specified, any information contained in this publication is current as at the date of this report and is provided by Fidante Partners Limited (ABN 94 002 835 592, AFSL 234668) the issuer of the Kapstream Wholesale Absolute Return Income Fund (ARSN 124 152 790) (Fund). Kapstream Capital Pty Limited (ABN 19 122 076 117, AFSL 308870) is the investment manager of the Fund. It should be regarded as general information only rather than advice. It has been prepared without taking account of any person's objectives, financial situation or needs. Because of that, each person should, before acting on any such information, consider its appropriateness, having regard to their objectives, financial situation and needs. Each person should obtain the relevant Product Disclosure Statement (PDS) relating to the Fund and consider that PDS before making any decision about the Fund. A copy of the PDS can be obtained from your financial adviser, our Investor Services team on 13 51 53, or on our website [www.fidante.com.au](http://www.fidante.com.au). If you acquire or hold the product, we and/or a Fidante Partners related company will receive fees and other benefits which are generally disclosed in the PDS or other disclosure document for the product. Neither Fidante Partners nor a Fidante Partners related company and our respective employees receive any specific remuneration for any advice provided to you. However, financial advisers (including some Fidante Partners related companies) may receive fees or commissions if they provide advice to you or arrange for you to invest in the Fund. Kapstream Capital, some or all Fidante Partners related companies and directors of those companies may benefit from fees, commissions and other benefits received by another group company.