



The Day After

JOHN MAULDIN | November 9, 2016

We had a very late night in the Mauldin household, as I'm sure many of you did. I truly was unsure what to expect from this election, and I was as surprised as anyone when the Trump victory started taking shape. At our election party there were many of my neighbors who were ardent Hillary supporters, and they were shocked, as was much of the national media.

The real losers? Polling companies and those who create models built around them. It turns out that when you really need a poll to work, the model breaks down. Not unlike the models built by the Federal Reserve and many financial planners. Blame natural complexity, for starters.

I keep telling people that past performance is not indicative of future results, and yet even I am surprised (I ruefully admit) at the woeful inadequacy of the predictions of political polls this time around. Brexit? The US? Bring on Italy and France.

Today I have two short, thoughtful post-election articles for you from Gavekal co-founders Louis Gave and Charles Gave. (Charles lives in France, and Louis moves between Hong Kong and Vancouver.) They are among the most "global" people I know, but you will see that they view this election outcome quite differently from the stereotypical globalists. They see the elitist world created by what Charles calls "Davos man" cracking up all over the place as pushback intensifies from the unprotected classes – those left out of the party of globalism and world growth that has developed over the last 30 or so years.

Globalism may be a painful process, but it is ultimately what the world needs. The more thoughtful of world leaders will begin to figure out that we need to learn how to expand the party invitation list. Those who don't figure it out will find that their leadership stripped from them and handed to someone who will at least try.

I don't want to say too much about my own post-election views until I have a chance to think some more and talk to my sources. At my election party, there was an old friend and highly educated gentleman who is, by almost any definition, an "elite" in our society. He's a successful businessman and politician with real connectivity. Yet he doesn't consider himself elite at all. He showed up late, as he had been to three other election parties where he felt he had to make appearances. So we stood watching the TV, talking about old times, and telling people it was way too early, at 10:30, to make a call on the presidential race, because we knew how last-minute precinct counts can change things.

And then they called Wisconsin. Bluntly, we and everyone else in the room were shocked. The whole nation was shocked, for better or worse.

The attendees at our party were a wide variety of people from all walks of life and income levels. I realized that something I want to think about more is that the class divide everyone talks about isn't so much economic as intellectual. It is more than just the Protected versus the Unprotected. I am clearly in the protected class, but I don't think of myself as being part of the establishment. Neither do many of my friends, although many might characterize us that way. Yes, education and wealth are part of it, but not necessarily the main part. The movement that Trump discerned and rode to the White House on has more to do with the way we think about the world around us than it has to do with income level.

Someone sent me a piece from *Foreign Affairs* magazine that was basically an elitist cry, rife with angst, about the "populist nationalist" Trump election, basically dismissing what is clearly a movement by calling it populist and calling the people composing it uneducated and driven by unthinking emotion.

And that is the problem. When you can classify a significant movement as unworthy of your consideration due to your intellectual or political station, it is hard to then sit down and work out solutions to shared problems.

Is Trump himself one of the elite? Hardly, though he sure looks that way. He went to expensive private schools, inherited wealth, and enjoys the finer things in life. But the true "elites" hate him. Maybe that's why they underestimated him. The reality, I said to my friend (who is about as wired into the Republican establishment as you can get, except that he's been trying continually for 40 years to overthrow it) is that you and I are considered to be the elitists by many in our own movement.

Let me offer you two additional links with thoughts on the election. The 1st is from my friend [George Friedman](#), and it really made me nod my head and think. The 2nd is from my friend (and fellow investment junkie) David Bahnsen, a conservative Republican but not a Trump supporter, who offers a different sort of analysis of the election. (Warning: If you are a Hillary supporter you probably don't want to read this. I really offer it for my Republican friends who think the next four years are going to be easy. They are not.) David points out that Republican candidates down-ballot consistently outpolled Trump in terms of total vote. There is going to be a lot of soul-searching and debating among both parties in the wake of this election.

With that, I leave you to read these very interesting articles. I'll have more for you in *Thoughts from the Frontline* this weekend.

Your having a light bulb moment analyst,



John Mauldin, Editor
Outside the Box

President Trump and the Fall of Davos Man

By Charles Gave

Nov. 9, 2016

For decades, all around the world but especially in Europe, the notion of the sovereign nation has been under fierce attack. Leading the assault have been the international bureaucrats and a clique of economists in league with those I have dubbed the men of Davos, all of them resolute proponents of crony capitalism.

Until this year, the offensive worked for them like a dream. Unsurprisingly, it did not work so well for the mass of ordinary people, the poor “*idiotes*.” The problem, as Pope John Paul II pointed out nearly 40 years ago, is that “individual freedom” can be exercised only in a democracy operating in a sovereign state. And as a Pole, he certainly knew what he was talking about.

Over the last few years, I have observed with mounting alarm how the exponents of this new international order were not only trying to destroy that “willingness to live together” which as Ernest Renan argued constitutes the essence of a nation, but that they were also tampering with interest rates, exchange rates and international trade – the very cogs which allow capitalism to work.

So these men of Davos were not only intent on destroying our nations, they were also destroying our standard of living. Presumably this was because their attempts to destroy local sovereignty were not succeeding in creating faster growth. Apparently they reasoned that if destroying sovereignty does not work, then destroying the financial expression of that sovereignty – national currencies – would have more success. Inevitably under such stewardship, the world economy has gone from bad to worse.

The consequence is the “surprising” – at least to the men of Davos – election of Donald Trump as president of the United States, a result which has momentous implications not just for the US, but for the grand projects pursued by Davos man everywhere around the world.

“We the people” are in the process of taking back their sovereignties, and are serving notice to the technocrats that they are fired. First Brexit, now Trump, next Italy, probably to be followed in due course by the Netherlands and France.

The problem is that the recovery of these sovereignties will necessarily lead to the destruction of the false sovereign structures, let’s call them the usurper sovereignties, put in place by the Davos men in their attempts to create a new world order.

Nowhere has this usurpation gone further than in euro-land. So, when an old and proud European nation such as Italy, France, the Netherlands or Germany decides to recover its sovereignty in order to manage its future democratically once again, it will inevitably mean the destruction of that financial Frankenstein’s monster, the euro.

Trump’s election victory is a clear indication that the majority of people are not interested in a world government, but want to return to a classical, local democracy. Strange as it may seem to the Davos men, most people tend to love their “*patria*”, the land of their fathers.

In financial terms, this means that any currency which is not backed by a nation is a technocratic fiction, and has no value. In turn this implies that the historical price volatility of assets denominated in such a currency conveys no information about the risks run by the holders of debt in that currency.

The time has come to realize that in Europe owning a volatile portfolio of high quality shares which have nothing to do with the local governments is going to be far less risky than owning a diversified low volatility portfolio of euro-denominated sovereign bonds.

This applies even to Germany, because Germany holds close to €1trn in assets issued by countries that can repay at most just 50% of their debt. Germany has been engaging in a very unhealthy form of vendor financing, exchanging cars and machine tools for paper, and the bill is about to get torn up.

So if I were still a portfolio manager, and if I had to manage a Europe-only portfolio, I would hold a lot of cash, mostly in British pounds and the rest in Swedish krona, no euro-area bonds at all, and all my equity positions I would keep in the shares of companies operating in what I have previously called “the non-communist sectors” of the economy. By this I mean the free market sectors, rather than those heavily interwoven with government, because needless to say, the biggest value traps are going to be in the shares of companies in the communist sectors.

To me personally, the news is getting better and better as the men of Davos suffer setback after setback. Already, the second Berlin wall, hastily raised by those who never accepted the logical conclusions of the fall of the first – including that technocracy does not work – is crumbling. With one more effort, we will be back in a world with market-determined prices. And then we will enjoy the bull market of a lifetime. I have never felt so optimistic.

When Elites Fail

By Louis Gave

Nov. 9, 2016

The most timeless analysis of American political culture was provided by Alexis de Tocqueville, who wrote the following of American democracy:

“The election becomes the greatest and, as it were, the only matter which occupies people’s minds. Then political factions redouble their enthusiasm; every possible phony passion that the imagination can conceive in a contented and peaceful country comes out into the light of day... As the election draws near, intrigues multiply and turmoil spreads. Citizens divide up between several camps each of which adopts the name of its candidate. The whole nation descends into a feverish state; the election becomes the daily theme of newspapers, the subject of private conversations, the object of every maneuver and every thought, the only concern of the present moment. It is true that as soon as the result has been announced, this passion is dispelled, all returns to calm, and the river which momentarily overflowed its banks returns peacefully to its bed.”

Now the Burkean conservative in me wants to agree with de Tocqueville: the passions unleashed by this election will hopefully once again, go back into their box for the next three and half years, only to be stirred up again the next time the electoral cycle comes around. Still, there are two elements of this week's vote that do raise discomfort.

1) Back in 2004, John Kerry had made the theme of his campaign the problem with the “Two Americas”. And of course, back then Kerry referred to the rich and the poor. But this vote illustrates that the US really is dividing into two countries as the gulf in voting patterns widens along income, education, gender, class, and urban/rural divides. Increasingly, Americans seem to live in self-reinforcing echo-chambers where they solely interact with people who hold the same beliefs and values. Combine this new reality with the news filtering capacity provided by social media algorithms and it is clear that growing parts of the country will never have to confront uncomfortable facts, or opinions. Illustrating this is the fact that, while a generation ago, the median US congressman was elected by a margin of less than five percentage points, once again in this election the median US congressman will be elected by a sizeable double digit margin. This cannot be a healthy development.

2) However one cuts it, the unique feature of the 2016 election has been the rise of the populist vote; Bernie Sanders' insurgency was by far the best a red-blooded Socialist candidate has done in any big western democracy in recent years. Donald Trump's solutions to the challenges confronting our societies are broadly in line with those offered by France's National Front. Although, not even Marine Le Pen would dare propose a ban on Muslims entering France! Clearly, we have entered a new era where domestic discontent, not just in the US but across the Western World, is sky high. And behind this discontent sit factors such as technological disruption (see our 2012 book *Too Different For Comfort*), dislocations caused by the ascent of emerging economies as industrial powers (see our 2005 book, *Our Brave New World*), the ageing of Western societies and the shift that immigration has caused to the cultural make-up in these countries. And this brings us to the timeless observation by Arnold Toynbee who, in *A Study of History* argued that the role of an “elite” in any society is to handle challenges that allow the group to survive and so move on to the next phase of their shared journey. If bad solutions are offered up then problems intensify and rising pressures eventually trigger a change in the elite. This can happen in various ways. Needless to say, elections are by far the best case scenario (no bloodshed or destruction of property). But if elections do not trigger the required changes (e.g. France during the Fourth Republic and the challenge of decolonization), then this can engender a change of regime (a distinct possibility across euro-land?), or even revolutions. Judging by Donald Trump's likely win in the US presidential race, it would seem that the US for its part does not believe that political dynasties should be left to solve the country's problems. Looking forward, the hope must be that the new president will rise to the huge challenges facing the US and the wider world with genuine solutions to real problems.

But I am doubtful, which is why we prefer countries and markets that have the advantage of small scale as entrenched interests tend to run less deep and finding common ground for the “shared journey” is politically easier. It is also why we prefer overweighting countries with the Queen's head on the bank note (and as a Frenchman, it really hurts to say this!).

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