



Philequity Corner (October 9, 2017)
By Wilson Sy

Tax reform lifts US and PH stocks to record highs

US stocks continued to make new highs last week, buoyed by hopes for the eventual passage of the Trump administration's tax reform program. Following the lead of strong global markets and helped by optimism regarding the passage of our own tax reform program, the PSEi staged a decisive breakout above 8,000 and likewise recorded a new all-time high.

Milestone after milestone

The Dow, S&P 500 and Nasdaq are all trading at historic highs and are up by 15.2%, 13.9% and 22.4% year-to-date. Even the Russell 2000, a benchmark index for small-cap US stocks, is also trading at an all-time high. Last week, the S&P set a record for the longest streak of all-time high closes in 20 years by closing at all-time highs for six consecutive days. Not to be left behind, the PSEi also notched another milestone. Last Friday, it touched an all-time intraday high of 8,406. With last week's close of 8,311, the PSEi is up 21.5% year-to-date.

US and Philippines tread parallel paths

US and Philippine stocks treaded very similar paths on their way to new all-time highs. US and Philippine investors had to deal with political noise, negative news headlines, geopolitical risks and natural disasters. Incidentally, both countries experienced lone wolf attacks on casino hotels which unfortunately led to many casualties.

Trump and Duterte – birds of the same feather

Both the US and the Philippines are led by unconventional presidents with colorful personalities. Even before their ascent to the presidency, we pointed the many similarities between Trump and Duterte (*Year of the Underdogs*, November 14, 2016). Both started as underdogs before benefiting from a meteoric rise during their campaigns. Both were political outsiders who pulled-off upsets against experienced politicians. Now, as presidents, we see even more resemblance in their personality traits and temperament. Both have fiery and combative personalities. They are bold and decisive and are quick to act. They both talk incessantly are not afraid to speak their mind. Trump tweets on a daily basis while Duterte frequently gives long and passionate speeches. They seem to get along well and relate to each other. In fact, Trump will visit the Philippines next month.

A common agenda for Trump and Duterte

Apart from having similar personalities, we discussed that the Trump and Duterte governments also have a similar economic agenda centered on tax reform and a planned push in infrastructure spending. So far, their economic agendas have been well-received by the business and investment community. Because of optimism regarding tax reform, our stock market has sustained its upward momentum despite the Marawi rebellion, a weakening peso and recent political drama.

Balancing the tax reform package

The quick passage of the tax bill in the Senate may allow the government to pass it into law much sooner. However, we note that the Senate's current version will generate less than P60b in additional revenues for the government. This may become a disappointment for economists and a major downside

risk to investors who expect that the tax reform package will generate more than P100b in additional revenues. Hopefully, the Senate will come up with a final version that will minimize dilution from the DoF's original proposal. Reaching the target revenue threshold will be critical in supporting the government's massive infrastructure program while also maintaining fiscal responsibility.

Tax reform and global bull run trump the ghost month

In Chapter 10 of our book Opportunity of a Lifetime, we discussed that stocks tend to be weak during the lunar ghost month and in the calendar months of August and September. However, due to a global bull run and hopes regarding the passage of tax reform, the PSEi performed relatively well during the ghost month. The PSEi's return of +1.8% for this year's ghost month compares favorably vs. the -2.1% average historical loss for ghost months. Likewise, the index delivered a return of -0.7%/+2.7% in August/September 2017 compared to average historical losses of -3.7%/-1.3%. In the table below, we show the average returns of the PSEi for each month of the year.

PSEi's historical average monthly returns

Month	Batting Rate	Return
January	65%	3.25%
February	45%	1.17%
March	58%	0.83%
April	65%	1.86%
May	58%	2.11%
June	58%	1.61%
July	65%	2.04%
August	29%	-3.73%
September	52%	-1.33%
October	63%	2.23%
November	50%	-0.03%
December	70%	3.82%

From 1987 to 2017

Sources: Bloomberg, Wealth Research

Halloween to Valentine's – a seasonally strong period for stocks

As seen in the table above, the PSEi has the highest batting rates and average returns for the months of December and January. It is therefore important to note that we are about to enter a seasonally strong period for stocks. As we discussed in our book Opportunity of a Lifetime and in a previous article (*Halloween to Valentine's*, October 27, 2014), the PSEi generally performs well during the period starting from Halloween up to Valentine's day (October 31 up to February 14). Historical statistics show that Halloween to Valentine's has a 76% chance of delivering a positive return and an average return of 9.8%. This period may provide a good buying opportunity for people who want to start investing or for those who want to add to their equity positions.

Monitor the risks

Despite the record highs reached by US and Philippine indices and the strong performance of stocks during Halloween to Valentine's, investors should remain mindful of risks that may affect the stock market. Political noise is getting louder while geopolitical tensions remain high. In this light, one should be cognizant and mindful of political developments. Recent events in the US and the Philippines, such as

bickering among politicians, may dampen investor sentiment. Moreover, the threat of various impeachment complaints may distract Congress from its legislative agenda and from implementing important programs such as tax reform. Considering the recent steep run-up in stocks, political noise may give pause to some investors and cause the stock market to correct.

Mind the risks, but focus on fundamentals

Though recent events make it harder to ignore politics, investors should not get distracted by political noise. It is important not to let political noise alter or reverse our investment thesis even as we monitor the various risks and headwinds that may cause the market to correct. Instead, investors should maintain their focus on fundamentals and watch how the following factors and catalysts evolve: 1) the resurgent global economic growth; 2) the improving outlook for corporates on the back of the reflation trade; 3) the ongoing global bull market in stocks; 4) our country's robust economic performance; 5) the final outcome of the tax reform package; and 6) the roll-out of the government's massive infrastructure program. These factors will ultimately drive where our stock market will go.

Farewell, Uncle Wash

Mr. Washington Sycip, founder of the famed accounting firm Sycip Gorres Velayo & Co. (SGV), passed away last night on his way to New York City. He was 95 years old. Aside from putting-up SGV, Uncle Wash is widely known as an esteemed management guru and has served as director and board member for many reputable companies. We would like to take this opportunity to express our utmost gratitude to Uncle Wash for sharing with us his long-term vision and imparting to us his wisdom in the many years that he has been with us in the Philequity board as a director, mentor and friend.

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