



Bradley, Foster & Sargent, Inc.

Quarterly Market Commentary

July 2018

Donald Trump: The Art of the Deal

I don't do it for the money. I've got enough, much more than I'll ever need. I do it to do it. Deals are my art form. Other people paint beautifully on canvas or write wonderful poetry. I like making deals, preferably big deals. That's how I get my kicks.

The Art of the Deal,
Donald Trump with Tony Schwartz, 1987

Trump is not being reasonable. But, then, man does not live by reason alone, fortunately. Trump, who believes that excess can be a virtue, is as American as Manhattan's skyline, which expresses the Republic's erupting energies... He believes architectural exuberance is good for us, and he may have a point. Brashness, zest, and élan are part of this country's character.

George Will column, 1987

In our quarterly letter to our clients in October, 2016 we predicted that the U.S. stock market would likely experience a significant correction if Donald Trump were elected president of the United States. Our predictions were primarily based on Trump's campaign rhetoric on trade and the large potential tariffs that he might slap on Chinese and Mexican imports, inciting a trade war. We were wrong, and we were not alone. The great preponderance of investment advisors and analysts were in the same camp, predicting an upward trajectory in the market if Hillary Clinton were elected and a drop if Donald Trump were elected. Since the close of business on November 7, 2016, the day before the presidential election, the U.S. stock market has soared: the total return of the S&P 500 Index is up 35.6%; the Dow Jones Industrial Index up 42.2%; and the NASDAQ Composite up an amazing 53.1%. What did we get wrong about Donald Trump? And what happens from here?

President Trump is unlike any previous president. He is *sui generis* – one of a kind. In the past, America has chosen presidents who were American generals and heroes like George Washington, Ulysses Grant, and Dwight Eisenhower; lawyers like John Adams and Abraham Lincoln; governors like Theodore Roosevelt and his cousin Franklin Roosevelt. But never before has a candidate who was a businessman, a showman, and a celebrity been elected president. Ronald Reagan was an actor, but before becoming president, he was governor of California for eight years and thus had real political experience before entering the White House.

In all probability, Donald Trump will be our president for another 2½ years, as efforts to remove him from office appear increasingly unlikely. So it is important, we believe, for investors to learn about President Trump, his background, and how he operates in order to understand why the stock market has defied the predictions of most pundits, and may continue to do so for some time. If so many are put off and even repelled by his character and his behavior, why is the stock market performing so well?

Trump is seen by his many critics and by many in the electorate as a narcissist; a shameless, ostentatious boor; a bombastic showman; and a crass and gaudy nouveau riche. He makes claims that cannot be substantiated and seems unable to speak without exaggeration. One critic, Mark Singer, writing for the *New Yorker*, called him a “hyperbole-addict.” But he is also a visionary real estate developer and businessman, a consummate showman, a TV actor and star, a billionaire, and a politician who put his finger on a certain malaise in the America body politic and translated this instinct and intuition into a ticket to the White House.

So this commentary is an effort to understand how President Trump operates and recount the remarkable story of how this grandson of a German immigrant became president, and by doing so, help investors judge how Trump’s words and actions will affect the stock market going forward. In this analysis we depend primarily on two books. The first is *The Art of the Deal*, written by Donald Trump himself with the assistance of Tony Schwartz. This book gives chapter and verse about Trump’s modus operandi, and although written 30 years ago, it still serves as a valuable template in understanding Trump’s approach to achieving his goals. Published in January, 2017, *Trump Revealed* is a biography of Trump coauthored by Michael Kranish and Marc Fisher who assembled a team of *Washington Post* reporters and researchers to investigate every aspect of Trump’s life. There are hundreds of books about Trump and endless photos and videos of “the Donald,” as he relentlessly sought to build his own Trump brand over the past forty years. In seeking to understand the man, the problem is to condense the enormous amount of material which is available to come to a useful conclusion about his character, his values, and the direction in which he wants to lead America.

Family Background and Youth (1946-1968)

Donald John Trump, the son of Fred and Mary Trump, is the fourth of their five children. Fred was twelve when his father, Friedrich Trump, an immigrant from Germany who had prospered, died in New York as a victim of the worldwide influenza epidemic. Fred’s mother, Elizabeth, made herself head of the family real estate business called E. Trump & Son. Fred graduated from high school in Queens in New York City in 1922 and went to work as a carpenter’s helper. A year later, he had built his first house in Queens for \$5,000 and sold it for \$7,500. An extremely hard worker and even tougher taskmaster, Fred Trump built larger and larger houses in Queens and Brooklyn over the next several decades. He married Mary MacLeod, an immigrant from Scotland, in 1936. By the time Donald was born in 1946, Fred Trump was a major real estate developer in New York City, constructing and owning thousands of apartments for working- and middle-class families. When Donald was one, the family moved into a 23-room manse in Queens. From Donald’s earliest days as a real estate developer, his father served as the financial backstop for his son. Whenever Trump was in financial distress or one of his projects needed a guarantor, his father was there to bail him out. Trump’s financial success would have been impossible without his father’s full support and financial backing.

In his book, *The Art of the Deal*, Trump writes that he was “a very assertive, aggressive kid.” He claims to have given his music teacher a black eye, punching him because he didn’t think he knew anything about music. Whether the story is apocryphal or not, his father sent him to New York Military Academy in upstate New York to inculcate some discipline and self-control in his life. Trump did well there in his studies, as well as in athletics and leadership, graduating in 1964 and enrolling in Fordham University. After two years, he transferred to the Wharton School at the University of Pennsylvania as an undergraduate, graduating in 1968 with a B.S. in economics.

Key Events in the Life of Donald Trump

1946	Donald John Trump was born the fourth of five children to Fred and Mary Trump in Queens, NYC
1959	Sent to New York Military Academy to acquire focus and discipline; graduated in 1964 and enrolled in Fordham University
1966	Transferred as an undergraduate to the Wharton School at the University of Pennsylvania, graduating with a B.S. in 1968
1968	Joined his father's firm, becoming president of Trump Management in 1971 at the age of 25, overseeing the ownership of 14,000 apartments
1974	Won the right to buy the Commodore Hotel from Penn Railroad bankruptcy judge and put together a deal to transform it into the Grand Hyatt Hotel
1978	Began assembling the land and air rights for the construction of the iconic Trump Tower on Fifth Avenue in New York City, resulting in the highly successful sale of condo units in 1982, assuring Trump's reputation as a visionary entrepreneur
1981-1989	Developed and purchased three hotel casinos in Atlantic City by borrowing large amounts of money
1983-1985	Purchased the New Jersey Generals in the U.S. Football League; sued the NFL as a monopoly and won but damages were set at \$1; USFL folded
1985	Purchased Mar-a-Lago in Palm Beach and turned it into a Resort Hotel and Club
1986	Took over the rebuilding of the Wohlman Ice Rink in New York City, completing the task in six months after the city could not complete the project in six years
1989-1992	Bought Eastern Airlines, renaming it the Trump Shuttle; venture failed
1990-2004	Atlantic City Hotels and Casinos went through Chapter 11 bankruptcies, negatively impacting both his finances and his reputation
2004-2015	Hosted the reality TV show, <i>The Apprentice</i> , with 20 million viewers tuning into the first show, giving Trump a national platform
2012	In an early Republican survey, had second best name recognition behind Romney
2012	Filed a trademark of "Make America Great Again" with the U.S. Patent Office
2015-2016	Campaigned for president, first winning the Republican nomination against 16 competitors; then defeating Hillary Clinton with 304 electoral votes to 227

Trump Sets His Sights on Manhattan (1968-1973)

Upon graduation from Wharton, Trump joined his father's firm. Three years later Trump became president of Trump Management, with his father retaining the role of chairman. But Trump had his eyes on Manhattan, finding the ownership and management of thousands of apartments in Queens and Brooklyn not to his liking. The work was tedious and sometimes even dangerous when trying to collect delinquent rents or evicting tenants. In *The Art of the Deal*, Trump writes that one of his first principles is to "aim high and think big." So Trump rented a small flat in Manhattan and found a way, after many attempts, to get into Le Club – an exclusive gathering spot for New York movers and shakers. It was there that he met Roy Cohn, the tough and notorious lawyer who in his career had worked as counsel for clients as wide-ranging as Joe McCarthy's Permanent Subcommittee on Investigations in the Senate, the Catholic archdiocese in New York City, disco owners, and mobsters. Cohn became something of a mentor to Trump, and Trump's modus operandi reflected Cohn's influence. Cohn counseled that when one is attacked, the proper response is to counterattack with overwhelming force. Trump writes in *The Art of the Deal*, "Sometimes the only choice is confrontation. When people treat me badly or unfairly or try to take advantage of me, my general attitude, all my life, has been to fight back hard." When Trump's father's firm was sued by the U.S. Government for racial discrimination under the Fair Housing Act, Cohn's answer was not to settle, as counseled by several white-shoe New York lawyers, but to countersue the U.S. Justice Department (ultimately the lawsuit was settled with only modest financial cost to the Trump organization). By 1973, Trump was ready to seek his fortune as a Manhattan real estate developer.

Trump's Role in the Transformation of New York City (1974-1982)

In the fall of 1975, New York City was a mess and came perilously close to declaring bankruptcy, as \$453 million in bonds were coming due with only \$34 million on hand. The headline in the *New York Daily News* at that time was: "[President] Ford to City: Drop Dead." It was also a dangerous place to live. In some years in the 1970s, there were more than 3,000 homicides in the city. But where there is crisis, there is also opportunity. Donald Trump saw opportunity in the assets of the bankrupt Penn Central. In 1974, he bid for several New York City assets including the failing and decrepit Commodore Hotel on 42nd Street near Grand Central Station. With modest capital but huge ambition and the backing of his father's assets, he put together a deal with Hyatt's cofounder Jay Pritzker and persuaded the city to grant a 40-year moratorium on NYC property taxes. The result was the Grand Hyatt which did a great deal to rejuvenate the Grand Central Station section of New York. Once the Grand Hyatt deal was put together, Trump turned his attention in 1978 to a real estate parcel on Fifth Avenue and 52nd/53rd Street owned by Bonwit Teller. Trump decided that this would be the spot for his signature project – the Trump Tower. Trump negotiated an option on the Bonwit Teller lease, but to put the deal together, he needed two other pieces – the land below owned by Equitable Insurance and the air rights controlled by Tiffany & Co. He negotiated and secured the ownership of the land and air rights, and then to make the deal come to fruition, he needed to secure the construction financing and rezone the property which required working with and getting the approval from a dozen city and state agencies. He made it all come together, and in 1982, when Trump was only 36 years old, the Trump Tower commenced selling condos in the 58-story building for a minimum of \$500,000. Ultimately, the condo sales brought in \$277 million – enough to pay off the debt on the entire building before the first tenant moved in. Trump writes in *The Art of the Deal*: "More than anything else, I think deal-making is an ability you're born with. It's in the genes... It's not about being brilliant. It does take a certain intelligence, but mostly it's about instincts." In both the Commodore Hotel/Grand Hyatt and Trump Tower projects, Trump learned a great deal about public

relations and how to get the word out. As recounted in *The Art of the Deal*, “One thing that I’ve learned about the press is that they’re always hungry for a good story, and the more sensational the better... The point is that if you are a little different, or a little outrageous, or if you do things that are bold or controversial, the press is going to write about you... The final key to the way I promote is bravado... That’s why a little hyperbole never hurts. People want to believe that something is the biggest and the greatest and the most spectacular.”

Trump Diversifies and Goes Through a Time of Troubles (1983-2004)

By the time the Trump Tower was completed, Donald and Ivana Trump were arguably the most well-known celebrities in New York City. He had wed the glamorous Ivana in 1977. They were married by Norman Vincent Peale of *The Power of Positive Thinking* fame. (Trump later asserted that Peale had more influence on him than anyone beside his father.) But over the next several decades, Trump’s supreme self-confidence and ambition resulted in many deals that tarnished his reputation, leading to Chapter 11 bankruptcies or outright failures. Although he pulled off a public relations coup by renovating the Wohlman Skating Rink in six months (a project that the city was unable to accomplish in six years) and successfully created the Mar-a-Lago Club in Palm Beach, his lengthy foray into hotel/casinos in Atlantic City was a disaster. His involvement in the development and ownership of three hotel/casinos in Atlantic City lasted for twenty or more years and brought only heartache and financial losses. His purchase of the New Jersey Generals in the U.S. Football League was a costly mistake, as was his purchase of Eastern Airlines, which he renamed the Trump Shuttle. The airline failed in less than three years. Nevertheless, Trump believed that the Trump brand was so strong that if he merely lent his name to a business idea or start-up, it would succeed. Thus, innumerable companies with his name have failed over the years including Trump Vodka, Trump Mortgage, Trump University, Trump Magazine, Trump Steaks and even Trump: The Game. Despite these failures, Trump always persevered. He never gave up, always putting a positive spin on even the most dismal failure. In *The Art of the Deal*, he writes, “Sheer persistence is the difference between success and failure.”

Trump: The Apprentice (2004-2016)

The Trump brand was badly tarnished when he was rescued in 2004 by a reality TV show called *The Apprentice*, created by Mark Burnett and picked up by NBC with Trump as the host. Trump seemed born for the role. He came across as supremely competent and confident. His image as a highly successful businessman was restored. He refused to study his lines and usually improvised. The show’s catchphrase, “You’re fired,” was never scripted. By the end of the first season, 27 million people were watching *The Apprentice*. It turned out that Trump, like many politicians, is a natural actor. And *The Apprentice* turned out to be the bridge to the 2016 presidential campaign. Before *The Apprentice*, Trump was a celebrity primarily in New York City. Now Trump was known nationally.

Trump in Politics (1987-2012)

As a businessman in New York City, Trump donated to the campaigns of politicians of all different stripes. It didn’t matter whether they were Republicans or Democrats or members of the Reform Party – as long as he had access to and influence with the political players whom he needed in order to do business. It was the old pay-to-play, and it is the way that many in business throughout the country behave. So an analysis of to whom he gave money is not helpful in understanding Trump’s politics.

What is important to know is that Trump has had his eye on the presidency for a long time. In 1987, a Republican activist in New Hampshire sent out mailers encouraging Republicans to “draft” Trump. Trump appeared to be interested in this idea but only briefly, for shortly after taking out full-page ads in the *New York Times* and other East Coast papers, he flew to New Hampshire only to announce that he was not interested in running for president.

In October, 1999, Trump announced on *Larry King Live* that he was leaving the Republican Party to join the Reform Party and that he was forming an exploratory committee to run for president. Despite joining the Reform Party, he said that his role model was Ronald Reagan. For a vice presidential running mate, he said he might pick Oprah Winfrey. Five months later, Trump withdrew from the race, as he was not sure that a third-party candidate would be able to win.

In 2000, when Hillary Clinton ran for the Senate in New York, Trump donated to her campaign and hosted an event at the Trump Tower for her. Between 2002 and 2009, he donated repeatedly to Clinton campaigns and invited the Clintons to his wedding to Melania in 2005. In 2001, Trump joined the Democratic Party. As elucidated in *Trump Revealed*, it was the second of his seven party switches between 1999 and 2012. Many critics take this as a sign that Trump has no core values. However, to Trump, political donations and party affiliation were a cost of doing business. His practice of politics is transactional – the way to get things done – not ideological. He is quoted as saying, “I give to everybody. When they call, I give. And you know what? When I need something from them... I call them. They are there for me.”

Trump’s celebrity status put him among the 2012 Republican front-runners. An NBC News/Wall Street Journal Survey in April 2011 showed him tied for second place behind front-runner Mitt Romney. Among Tea Party supporters, he led the field. In February, 2012, he endorsed Romney and even flew to Boston on Election Day to attend what was supposed to be a Romney victory party. He was furious when Romney lost, tweeting: “This election is a total sham and travesty.”

Twelve days after the 2012 election, Trump filed an application with the U.S. Patent and Trademark Office for a phrase he wanted to be his own: “Make America Great Again.”

The 2016 Campaign for President

Already numerous books have been written about this election – perhaps unique in American history. There is neither time nor space to recapitulate the details of the election, but some comments are useful in pointing out how and why Trump was able to defeat a field of 16 other Republican contenders as well as a seasoned Democratic opponent. He possessed remarkably accurate instincts about what was distressing so many Americans. He was not analytical; he was intuitive and instinctive, which is the way that he has always operated. His PR and communication skills were ideally suited to the Twitter and social media world. Like Ronald Reagan, his strategy was to communicate directly to the electorate rather than going through the media which he distrusted, as does a large segment of the American people. He was able, as a celebrity, to make exaggerated and often inaccurate statements yet not be held accountable. He was deliberately politically incorrect, insulting entire groups of people as well as individuals like John McCain, whom he called a “loser.” At the same time, he was a celebrity, drawing enormous crowds. One day in New Hampshire, when Jeb Bush was still in the race, Trump drew more than 3,000 to his rally, while Bush was talking to fewer than 150 people. Trump also had a remarkable ability to brand his opponents with a one-line zinger that people remembered: Jeb Bush was “low energy,” Marco Rubio was

“little Marco,” and Ted Cruz was “lying Ted.” Later in the general election, Hillary was “crooked Hillary,” referring to her private email server.

Donald Trump won the presidential campaign because he positioned himself as a visionary businessman who got things done when no one else could. He won by being a tough pragmatist fueled by a large, flamboyant ego. He won because he appealed to Americans who also wanted to Make America Great Again. The people had seen the elites – the Washington establishment, the news media, Hollywood, academia and professionals – prosper, while they were left behind. Trump ran against the elites and won. He won because half of America believed in the slogan, “drain the swamp.” He won because he was a fighter, and whenever he was savaged by members of the chattering class, he fought back and gave as good as he got.

He also won because the turnout for Hillary Clinton was so low. Trump actually received one million fewer votes than Romney did in 2012. But Clinton received six million fewer votes than Obama received in 2012. Trump also won key states where working-class Democrats voted for him rather than for Hillary Clinton. A flip of only 107,000 votes in Michigan, Wisconsin and Pennsylvania would have given the election to Clinton.

President Trump

Following his 2016 presidential victory, President Trump said that his exaggerated rhetoric was just part of the political game. He said that “sometimes you need a certain rhetoric to get people motivated.” He seemed to believe that this statement was justification for his more egregious hyperbole as well as his attacks on individuals and ethnic groups. He also stated that much of what he said on the campaign trail was just “opening positions for negotiations.” This may be true, but much of America is deeply troubled by Trump’s character. The best American presidents have appeared confident but shown humility, whether real or feigned. They have come across as strong but willing to compromise. They have appeared “presidential” – measured, thoughtful and careful in their public statements. Our presidents have had unusually strong egos but taken pains not to appear narcissistic. In short, character has counted. Now America has a president whose character does not conform to what we consider to be presidential. Trump is aggressive, impulsive, and instinctive rather than thoughtful. He sees life as a zero-sum game; he is transactional rather than ideological; and he is quick to take offense and lash out with his hot temper. He rarely presents himself as “presidential.” But 50% of Americans seem willing to give him a pass on his character traits if he accomplishes his main goal, which they believe in, of restoring American greatness. They seem prepared to divorce character from results, which has rarely happened in American history. They appear willing to support a celebrity businessman and reality TV star if he gets the job done.

Why is the Stock Market Up So Much Since Trump was Elected?

The market is up primarily because investors like what President Trump has done to promote business in America. President Obama was widely perceived as being anti-business, and his administration presided over the weakest economic recovery since the Great Depression. President Trump is seen as pro-business. He is clearly in favor of the deregulation of many industries and has decreed that for every new regulation, two must be voided. He passed a tax reform bill which cut taxes on corporations, which was desperately needed, as corporate tax rates in the U.S. were the highest in the developed world. Tax reform will result in the repatriation to the U.S. of approximately two trillion dollars on the balance sheets of foreign subsidiaries of U.S. corporations. 85% of American households will get a tax break as well. Unemployment

is near an all-time low, and unemployment for African-Americans and Latinos is at the lowest rate on record going back to 1972. Economic activity has accelerated since Trump's election, and many expect real GDP in 2018 to grow by 3% or more – the first time in a decade. In short, the “animal spirits” of spontaneous optimism about which John Maynard Keynes wrote have been unleashed, and both consumers and business leaders are showing signs of optimism about the economy. Finally, *U.S. corporate earnings are up significantly this year, and with tame inflation and interest rates still at attractive levels, stock prices follow earnings.* These are the key reasons for the market's sharp increase over the past 18 months.

On the other hand, there is the possibility of trade wars with our NAFTA partners, our European allies, and China. Investors generally believe that the enormous increase of free trade since the General Agreement on Tariffs and Trade (GATT) was formed in 1948, and the World Trade Organization which replaced GATT in 1995, has been very good for the global economy. Investors are thus skittish about President Trump's threats to raise tariffs. It was his campaign rhetoric on tariffs which caused us to predict a market decline in October, 2016 if he were to be elected. However, investors are increasingly coming to recognize that the terms of trade with China need to be renegotiated. One example is China's requirement that Chinese subsidiaries of U.S. and European companies set up joint ventures with Chinese companies so that valuable technology can be transferred to China. China has established a program called “Made in China 2025,” whose goal is for China to gain economic and strategic ascendancy over America and Europe, and Trump's tactics may be the only way for America to counter this challenge from China.

Although investors are skittish about a possible trade war, they have come to realize that what is important about President Trump is not his boorish behavior or what he says or tweets, but what he does. President Trump sees everything as part of a deal, and thus investors should not confuse his negotiating tactics with what actually ends up happening – the end result of the deal.

Bradley, Foster & Sargent, Inc. *Investment Management*

Principals & Portfolio Managers: Robert H. Bradley • Cameron H. Burns • Nancy W. Donadio • Timothy H. Foster
John R. Gilbert • Charles J. Herbert • David P. Korzendorfer • Keith G. LaRose • Felicia M. Lazor • Roger H. Manternach
Jeffrey G. Marsted • Gregory M. Miller • William R. Peelle, Jr. • Robert A. Penney • Joshua O. Peteet • Thomas D. Sargent • Stephen L. Willcox

CityPlace II • 185 Asylum Street • Hartford, CT 06103 • 860-527-8050 • www.bfsinvest.com