

# Mitch on the Markets

## Why Political Gridlock is Good for Stocks



By Mitch Zacks  
Portfolio Manager

If watching the presidential debates and thinking about the outcome of the presidential election makes you cringe a little, we have two things to tell you: 1) You are not alone; and, 2) You probably don't have much to worry about when it comes to stock market investing.

We'll explain below why we think point #2 applies in this cycle. But before we do, it is important to remind readers that Zacks Investment Management is politically agnostic. While we all hold our own personal political views, we do not let them enter into the investment process whatsoever. If we allowed political bias to influence our investment decision-making process, it would mean straying from the quantitative and qualitative processes that have delivered us success over the years. It's simply not an option.

What we do watch and evaluate closely, however, is how likely the winning candidate is able to implement dramatic policy shifts. At the end of the day, in our view and from our experience, the market is more concerned about the new

president's *ability to legislate* versus who is actually doing the legislating. To understand that risk, an investor has to examine Senate and House races just as critically as the presidential one.

### **The Classic Political Outcome: Overpromise, Under-deliver**

What the market is ultimately hoping for is low legislative risk, which means a "divided" government. The least friendly outcome for stocks is if the president-elect ends up with a super-majority in Congress, which means legislative risk is high. The controlling party can use a legislative tool known as "budget reconciliation," which allows for expedited legislation to change laws impacting property rights, tax codes, and/or government spending policies. If this is the outcome of this election, then it would be important to evaluate each policy change and weight its impact on corporate profits and the economic outlook. Stocks could respond in any number of ways.

The other, more frequent outcome is a "divided" government, where the president is affiliated with one party and Congress is either split or controlled by

the other. In these outcomes, it is difficult for the new president to make good on promises made on the campaign trail, and the risk of dramatic legislation fades. The president almost always has to move to the center to get new laws passed, meaning a substantially watered down version of what was promised. Markets can generally handle an outcome that is better than expected.

In the current scenario, Republicans control both chambers of Congress, but seats are up for grabs in both chambers that could change that status. Odds-makers in the market appear to favor a GOP controlled House, with a toss-up for the Senate (even though Republicans currently control it 54 to 46). There is still too much time between now and the general election to opine on the presidency.

### **Bottom Line for Investors**

The long and the short for investors right now is to 'wait-and-see.' We would caution against making investment decisions ahead of the outcome of the election because of a political preference or influence, and if the outcome of the election is a divided government in any form, it probably means the political agenda promised during the election cycle won't be what was expected when it

comes to actual policy-making. If there is one vote investors should cast, it's a vote for gridlock.

### **-Mitch**

#### **About Mitch Zacks**

Mitch is a Portfolio Manager at Zacks Investment Management. Mitch has been featured in various business media including the Chicago Tribune and CNBC. He wrote a weekly column for the Chicago Sun-Times and has published two books on quantitative investment strategies. He has a B.A. in Economics from Yale University and an M.B.A in Analytic Finance from the University of Chicago.



*Past performance is no guarantee of future results. Inherent in any investment is the potential for loss.*

*Zacks Investment Management, Inc. is a wholly-owned subsidiary of Zacks Investment Research. Zacks Investment Management is an independent Registered Investment Advisory firm and acts as an investment manager for individuals and institutions. Zacks Investment Research is a provider of earnings data and other financial data to institutions and to individuals.*

*This communication is for informational purposes only and nothing herein should be construed as a solicitation, recommendation or an offer to buy or sell any securities or product, and does not constitute legal or tax advice. The information contained herein has been obtained from sources believed to be reliable but we do not guarantee accuracy or completeness. Zacks Investment Management, Inc. is not engaged in rendering legal, tax, accounting or other professional services. Publication and distribution of this article is not intended to create, and the information contained herein does not constitute, an attorney-client relationship. Do not act or rely upon the information and advice given in this publication without seeking the services of competent and professional legal, tax, or accounting counsel.*