

Observations

May 17, 2017

History and Resilience

With the political pot boiling hot and calls for impeachment in the air, we thought some investment perspective would be helpful.

According to the research firm Bespoke, the S&P 500 fell nearly 50% between the week prior to the sentencing of the first five Watergate burglars in January 1973 and the month after the resignation of President Nixon.

Yet when the President Clinton Monica Lewinsky situation erupted in the late 1990's and impeachment proceedings developed, the stock market became volatile but little lasting market impact occurred from Washington events.

What explains the significantly different reactions from investors to these two events?

Some might conclude that investors respond depending upon whether a president steps down or survives an impeachment process.

While that may indeed be part of the explanation, we believe economic context is needed to fully explain things.

A key difference in these two situations was the state of the underlying economic fundamentals. In 1973 the U.S. economy entered one of the most severe recessions since the Great Depression. Inflation and the unemployment rate approached or exceeded 10%.

As Fredrick Hayek--the co-recipient of the first Nobel Memorial Prize in economics--commented during his 1974 acceptance speech about this period: "we indeed have made a mess of things".

In 1998-99 as the Clinton/Lewinsky impeachment proceedings ran hot, the economy remained in expansion mode and corporate earnings overall continued to rise. This support from the underlying fundamentals enabled the stock market to weather the Washington D.C. turmoil.

No one can know at this point the outcome of the current political storm. However, the economic expansion—although slow in pace—remains on solid ground. Meanwhile our ear-to-the-ground investment process continues to hear the sounds of better things--in the form of productivity growth—on the horizon.

As D.C. events play on, the markets may indeed become more volatile. But the current economic expansion and uptrend in corporate earnings should provide stock market resilience.