News or Noise: Lessons from the Government Shutdown

By David Fisher, Chief Investment Officer

As expected, Congress came to a last-minute resolution last week before the U.S. slipped over the debt ceiling cliff. The deal appears to be a temporary respite, however, and not a long-term solution. A USA Today headline last Thursday exclaimed, “It’s over: Shutdown ends, debt limit rises.” The only problem is that it is not over. In fact, this may be more like the brief interlude between rounds in a boxing match. Both sides are exhausted and need to catch their breath before coming back for a continuation in a few months. But we did finally hear the truth from some members of Congress last week: Opinions on what the future of the country should look like are deeply divided.

A Divided America

We often hear people say that the founding fathers would “roll over in their graves” if they saw today’s battles in Congress. We strongly disagree; this is the system they set up and we speculate that they would be pleased that it is still operating. They never promised compromise would be easy or that the will of the majority would prevail without a fight. In fact, Benjamin Franklin once said, “Democracy is two wolves and a lamb voting on what to have for lunch. Liberty is a well-armed lamb contesting the vote.”

This week, dozens of surveys showed disappointment in Congress. A Rasmussen poll found that 78% would vote to get rid of the entire Congress and start over. A Gallup poll found that by an almost two-to-one margin Americans believe that politicians are a bigger problem for the country than the economy and unemployment. Finally, a Pew Research Center survey shows that only 19% of Americans have faith that the federal government will do the right thing. But are these feelings warranted? We would suggest that elected
officials are just a reflection of a deep division within our country. Members of Congress are merely representing the will of their constituents. The truth is, Americans have significant and fundamental disagreements on the role and scope of government. The Great Recession was a catalyst for this debate about the role of government in the U.S., and it will likely take a few more election cycles to be settled.

What Happens Next

There are different opinions about what happens next. Many project that the fight that began in the summer of 2011 (and which has gone through several rounds since) is going to get more nasty and vitriolic before things get back to normal. The Tea Party wing of the Republican Party is fighting an ideological battle and they believe they are winning. They are not going to back down now. In fact, the coming budget and debt battles will just be the warm-up for the Congressional elections next fall.

Senator Ted Cruz (R-Texas) went home this weekend to roaring applause. He is gaining significant power within the conservative wing of the Republican Party. Jim DeMint, former Republican Senator from South Carolina and current President of the Heritage Foundation, said of the Tea Party battle this week, “[The reason we] chose this moment to fight—and why we will continue to fight … is simple: to protect the American people from the harmful effects of this law”(i.e., Obamacare).1 In many ways, the battle is for the heart of the Republican Party. The national election in 2016 is an eternity away right now and even with many polls showing that voters are disappointed in the way Republicans handled the debt ceiling fight, the reality is that almost every House seat is safe for 2014.

Others believe that President Obama and Democrats scored a big victory this past week. They think Republicans are not likely to put up the same fight in the future as they did last week, especially just a few months before the 2014 midterm elections. The proponents of this view point to the new budget committee framework as creating the potential for a bipartisan solution that could lead to positive results for the economy via reduced sequestration cuts. The sanguine view also takes to heart the statements by Mitch McConnell and others that Republicans won’t use the debt ceiling again as a threat. Finally, some point to the pivot toward the center by Paul Ryan, a long-time budget hawk, as an important development. With Ted Cruz, Rand Paul and Marco Rubio staking out the conservative wing, Ryan and New Jersey Governor Chris Christie will have to battle for the centrist portion of the party. The pressure is on Ryan to deliver an effective and orderly budget deal that moderate Republicans can support.

Where Will the Fight End?

It is hard to know where this fight will lead over the next few months and years. However, the market seems to be looking past it. With minor exceptions, the bond and equity markets were relatively calm over the last few weeks. In some ways the market sees the fight as a positive to the extent it keeps Federal Reserve tapering on hold.
Whatever your personal political opinions, we would encourage you to continue studying the issues, express your opinions and vote. Remember that our country is not founded on a principal of majority rule via simple democracy; rather, we have a republic that allows for the voices of an effusive minority to be heard. Though the timeframe can be unpredictable, this system has always allowed for the best possible outcome. We have no doubt it will again.

Sources


What Is News or Noise?

Like most of you, we are inundated with information on our phones, in our email inboxes and on the Internet. Clearly, the world doesn’t need another investing blog to re-process stale information or reformat the day’s useless headlines. Thus, in our investment blog, “News or Noise,” we’ve taken up the challenge of sorting through the infinite bits of background noise and seeking the few truly newsworthy nuggets of information, so that we can focus on the stories today that are likely to be meaningful for investors in the future.

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