Don’t Let Your Politics Shoot You in the Financial Foot

By Russell Wild *Wed, Nov 10, 2010*

If you intend to be rational about investing, separate politics from portfolio, writes fee-only advisor and author (and political news junkie) Russell Wild.

Joan, a friend of mine, called me on the phone and told me that, thanks to the government and its “inane economic policies,” the dollar was due to get walloped. She asked me how to invest in foreign currencies. I cautioned against it, explaining that financial markets are unpredictable, but she insisted. The dollar rose, and her “investment” (I’d call it a gamble) tanked.

Ken, another friend, certain that Washington’s policies were driving this country to ruin, had kept his money in a savings account for six years. What started off as $70,000, thanks to six years of low-but-steady inflation and taxes on his interest, was now worth something less. That same $70,000, invested in a well-diversified, modestly aggressive portfolio, rebalanced yearly, would have been worth $100,000 or more.

These experiences taught me that politics and investing shouldn’t mix. Whether you are liberal or conservative, please don’t let your politics or your clients’ politics shoot anyone in the investment foot.

In our hyper-intense political environment, I’ve seen more and more of this knee-jerk reaction in which people want to move their investments to reflect their political leanings. The ease of transfer of assets has exacerbated this tendency, too, as I’ve noted in my book, *Exchange-Traded Funds for Dummies*. ETFs are in many ways the perfect vehicle for these politico-investors. Hate what’s happening in Washington? Invest your money in South Africa, Malaysia, or South Korea. Hate the oil industry? You can plunk your money in an alternative-energy ETF. It’s easy now to target specific market sectors for your political support or opposition.

Ken (the same guy mentioned above), for example, is certain that the exportation of jobs and the resulting squeeze on wages will slaughter the Middle Class. No one will be left to frequent the malls. Stores will be boarded up. The stock market will collapse. He is shocked that it hasn’t happened yet. “How can Wall Street be so blind?!” he asks me. Ken can easily short the market with the ProShares Short S&P 500 ETF. But I wouldn’t advise him to do so.

Wall Street, where many smart and educated people hang out, is not so blind, Ken. They know that even if you are right, even if history proves the administration to be as terrible as you think it is, even if polarized politics is driving this country down, it doesn’t necessarily mean that stocks will suffer.

Experienced financial advisors know that market movements in the short term, and possibly well beyond, are largely random. You’ve read the studies that show the huge disconnect between market returns and practically anything and else going on in the economy. But how do you convey this to clients?

I suggest that in addition to appeals to data or economic theory, you share with your clients anecdotes that will stick in their minds. Consider these tidbits:

- Researchers at the London School of Business found that a comparison of stock market returns around the world shows a generally *inverse* relationship between total market returns and a nation’s economic growth rate.
- And speaking of the British: England started off the past century as the undisputed #1 World Power. It ended the century with a lost empire, sky-high unemployment, and crumbling inner cities. During that time, of course, the United States came to dominate the known universe. The return of British large stocks over past 50 years? 11.0%. The return of U.S. large stocks over the past 50 years: 9.1%. Looking to small stocks, the Brits beat us by a mile.
- Consider the history of disaster. (Always fun to do!) 1918, the year of the flu pandemic, the worst disease outbreak in modern world history, was a good year for stocks. In 1942 Japan attacked Pearl Harbor and Hitler marched across Europe, but it too was a great year for stocks. The year of the Cuban Missile Crisis—and the near destruction of the entire world—wasn’t so bad for stocks. In contrast, in 1929, when the market began its Mother of all Nosedives, nothing terrible was going on. Ditto for April 2000, the start of the three-year bear market that shredded so many Americans’ 401(k)s.
- Compare China to India. China’s growth in gross domestic product has been blowing the doors off India’s, and most other nations’ GDP for the past several years. Headlines of China’s domination of the world economy fill the media.Year-to-date return of The China Fund: 18.53%. Year-to-date return of The India Fund: 24.71%.

I can’t explain all of these apparent contradictions. No one can, really. They are what they are. Stock market returns in the United States have averaged about 10% a year over the past 75 years. That’s way higher than just about any other investment. Will it continue? I don’t know.

But the stock market has been pretty darn resilient so far.

If you intend to be rational about investing, separate politics from portfolio. I hope that each one of you voted your conscience on Nov. 2. But I also hope that each of you—and your clients—invest without your political biases coming into play.

Russell Wild is a fee-only advisor in Allentown, Pa. He has written numerous investment and business publications, including **Exchange-Traded Funds for Dummies**.