

POLITICAL PULSE

## Don't Get Swept Away by the Sweep

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Donald Luskin

**GOP congressional control lessens the odds of two years of worsening policy stagnation. But it's not exactly a third term for Ronald Reagan.**

**Republican** control of the **Congress** is a positive and a surprise. But it is probably more of a surprise than it is a positive.

Markets have surely fully discounted GOP continued control of the **House**. But **Senate** control was probably discounted at a probability of no more than 25%. The politicians are probably surprised, too. And all the more so because this outcome is so utterly at variance with historical experience -- the party in power just never does this well, especially considering that a disproportionate number of Republican Senate seats were up for grabs this year. So it will take both parties some time to reassess the preferences of the electorate, and to discover their optimal strategies.

Let's not be naïve and imagine that this narrow GOP control will usher in a bold new era of pro-growth economic policy. Senate control is very narrow -- filibusters can still block anything the **Democrats** want to block.

But what's more important, today's GOP is not exactly a fire-breathing army of **Reaganauts** bent on liberating the American economy. Memories of the economic initiatives that got done early in the **Bush administration**, when the GOP also narrowly controlled Congress, hardly stir the soul. But the alternative would have been worse -- and it's good news that we've avoided that. An economy in a spasm of risk aversion now has one less worst case to worry about.

The split congressional control that markets were expecting was certain to produce economic policy stagnation, or worse. With Bush's monopoly on the war issue, Senate Democrats would have had no choice over the next two years but to block any pro-growth policy initiatives, hoping to set up a replay of the "it's the economy, stupid" campaign that unseated Bush's father in 1992. And Bush probably would have done little to prevent it. Over the last year he has shown a consistent preference to avoid the risk of controversial domestic economic issues, instead standing pat with his high approval ratings based on the war on terrorism. Whether or not Bush were re-elected isn't the issue -- the point is that, either way, the economy would suffer for two years.

The bad news is that the GOP sweep probably gives the Democrats even more reason to try to block economic recovery -- desperate people do desperate things. But they now have less power to do so than they did 24 hours ago. And while today's GOP may not be the brightest pro-growth bulbs, surely something at least somewhat good will happen. It is, at least at the margin, a positive surprise.

But as investors, we must not get carried away by wishful thinking. There is every possibility that the GOP will interpret its sweep as the electorate's statement of satisfaction or indifference with

the economic status quo, and an endorsement of winding up the B-52s and building Lake Baghdad. After all, the sweep took place amidst a worsening economy and ever more loudly beating drums of war.

We will see signs soon enough of the extent to which the GOP intends to use congressional control to try to implement a pro-growth agenda, and we'll be ready to translate those signs into investment forecasts. But remember, this is the Republican party that proudly put its name on the **Sarbanes Oxley Act**. This is the Republican president who proudly signed it, who derailed two decades of progress in global trade by slapping on steel tariffs, and who selected, from the entire adult population, **Larry Lindsey, Paul O'Neill** and **Harvey Pitt**. In another surprise last night, Pitt began what may turn out to be a purge of the Bush economic team, starting with himself. But that's only good news if he's *not* replaced with **Rudolph Giuliani**. And that still leaves Lindsey and O'Neill. And, truth be told (dare we say it...) **Greenspan**. When it comes to selecting economic policy talent, the old saying may be true: "A" players pick "A" players, and "B" players pick "C" players.

So it's good news. At least a little. But we'll have to wait and see how good. Right at this moment the GOP is like the dog who chased the bus -- and is surprised to have actually caught it. The really good news is that the other dog didn't catch it. But -- what now? What do either of these dogs know how to do with a bus, anyway? **IM**