

Stock Market Perspective: Iowa Political Markets

The interesting times curse certainly applies to this year's election. The apparent nominees for president of each of the major parties are each unprecedented in terms of background or gender. Moreover, each has important negatives and much higher disapproval ratings than is typical for presidential candidates. In addition, Trump's candidacy has created an unusual amount of uncertainty about political makeup of the next Congress.

Unless the Senate does an about face, the next president will have an immediate Supreme Court vacancy to fill, and given the ages of some of the justices, quite likely more during his or her term.

There are several polls that come out weekly or more often that claim to measure the electorate's current sentiment. Often they are inconsistent with each other and change quite a bit over time. Since financial markets are supposedly "efficient" and reflect the combined knowledge of their participants, perhaps they can provide a better assessment or have a less cloudy crystal ball.

The oldest of these has a track record that is as good as or better than most of the pollsters. It is the Iowa Electronic Markets (<http://tippie.uiowa.edu/iem/>) run by the business school of the University of Iowa as a research project. Anyone can participate, but the maximum amount that can be "invested" is \$500, which prevents trying to buy the outcome.

There are markets for both parties' nominees, the composition of the next Congress, and the presidential election's percentage vote and winner. These markets work like futures markets with each contract having a current bid and ask price. The terminal value of each is either \$1.00 if it comes to pass or \$0.00 if it does not. So a current price of 0.60 indicates the market "thinks" there is a 60% chance the

corresponding event will happen. I will express the prices as percentages since that is the way we think about opinion polls.

The nomination markets opened in January. On the Democratic side, Clinton had been well over 80% from the start. There are a couple of things interesting about the recent prices. One is that she is currently at 95% even though she has

supposedly "locked up" the nomination.

The other is the change from the July 2 to July 5 midnight prices. (I am writing this on July

7). On July 2 the price was 87% perhaps indicating that some thought the FBI report, which was expected soon, might indicate she should be indicted. On July 5, the day of the report that said she did bad things, but not so bad as to be criminal, the price jumped to 95%, which is as high as it has been.

Not surprisingly, the Republican nomination has been a lot more variable. When the market opened in late January, Trump had the highest price as about 40%. The outcomes of the primaries resulted in a lot of volatility. In February, Rubio rose briefly to 60% while Trump fell to 20%. By the end of that month, Trump's price became the highest and has remained there. In early April, his price fell to 40% while Cruz and rest-of-the-field (not Carson, Cruz, Rubio, or Trump) each rose to about 25%. Trump has been around 90% since the end of April indicating that some are willing to bet with 9 to 1 odds that the upcoming Republican convention will find a way to deny him the nomination.

The presidential election markets have been open longer, but until the likely nominees became clear, they did not fluctuate much. Clinton has had a higher price than Trump (although technically it is Democrat vs. Republican with no third party price at this

If you have a strong opinion about the upcoming election, the Iowa markets let you put your money where your mouth is.

point) since January being about 60/40 until a recent contraction to about 54/46. The “winner-take-all” market, which is a bet on which party will get the most votes¹ is currently about 75/25 in favor of Clinton and has widened a bit since the FBI report.

The congressional control market has five contracts, the four ways the two houses can be under the control of a party plus the possibility one or both of the houses does not have a party with a majority of the votes. Currently, the highest price is on a Republican House and Democratic Senate at 44%. Next at 27% is Republicans controlling both houses, followed

¹ The market is for popular, not electoral votes. It correctly predicted that Gore would win in 2000.

by Democrats controlling both at 20%. At least one house being without a majority party is at 8%, and a Democratic House and Republican Senate is considered virtually impossible with a price of under 1%. The trends in the past two months have indicated improving prospects for the Democrats.

I have never participated in the Iowa markets and have no plans to do so this year even with a maximum loss of \$500. It might be tempting to bet on the outcome one does not want as compensation for having to endure four years of agony or start funding emigration. I think you will enjoy following these markets whether or not you participate in them.