



# The Economy on Election Day: 3 Scenarios

By Rick Newman

January 3, 2012

The Republican primary elections are providing a forum for the candidates to riff on everything they feel is wrong with America, from abortion to immigration to the size of government. But little of that will matter come November, since one issue seems likely to trump all others in the presidential race: the state of the economy.

If a big bloc of voters begins to feel the economic gloom is lifting and some form of prosperity is returning, it would be an obvious boost for President Obama's re-election quest. But that would probably require a shift in expectations by many Americans, since the unemployment rate will most likely be above 8 percent on Election Day, the housing market will still be broken, and incomes will probably still be stagnant. So how will the economy look when voters hit the polls in November? And how will that determine who wins? Here are three plausible scenarios:

**More of the same.** Many economists believe the economy is in a slow healing process, with several more years until the housing market fully recovers, unemployment returns to historical norms, and the majority of the middle class feels financially secure once again. Although 2011 ended with a surprising burst of consumer spending, for instance, forecasting firm IHS Global Insights expects a consumer pullback in 2012, with the economy growing just 2 percent. That would be barely enough to dent unemployment or make much of a difference in overall living standards.

If that's what happens, Obama will be able to make a few modest claims on the eve of the elections. He'll be able to say, for instance, that the economy has added more than 3 million jobs since 2010. He'll also be able to say the recession ended under his watch, which would be technically true. By November, he may even be able to scrounge some data showing that home prices have bottomed out and begun an upturn.

But the status quo will still feel punishing to millions of Americans. Even if the economy continues to add about 100,000 new jobs each month in 2012, total employment will still be 4 million or 5 million jobs less than the peak levels of early 2008. Stagnant incomes mean it will still feel like a recession to many, even those with jobs. And the GOP nominee will probably frequently remind voters that under Obama, the U.S. credit rating was downgraded for the first time ever.

*Advantage: It's a tossup.* Obama would be on weak ground if the economy on Election Day looks much as it does today. But his GOP opponent would still have to convince voters that changing course would do more to boost the economy than the slow healing process that's already underway. The Republican nominee will also have to make Republican control of government--which is possible if the GOP holds the House and takes the Senate--seem like something that's good for the economy. That may be a tough sell, given that Congress's approval rating fell to all-time lows following the GOP surge in 2010.

**Crisis fatigue.** There's a lot that could go wrong over the next year or two. The European debt problem is becoming more acute, despite endless pronouncements from leaders there who still think a few reassuring words will calm markets. For a variety of reasons, 2012 could be the year the euro zone fractures and a full financial crisis erupts on the continent. At a minimum, most economists expect Europe to spend most of 2012 in another recession, which won't torpedo the U.S. economy but won't lift it either. Iran is another red flag on the world map. A showdown over Iran's determination to obtain nuclear weapons seems to be looming, with the West preparing further sanctions and Iran threatening to close the Persian Gulf to oil shipments and take other incendiary

steps. It may never happen, but fear alone may already have driven [oil prices](#) up by \$10 or \$20 per barrel, and any rise in oil prices takes money straight out of consumers' pockets. **Economist Bernard Baumohl of the Economic Outlook Group** predicts that oil prices, which have been around \$100 per barrel lately, could go as high as \$135 in 2012, with U.S. gas prices hitting \$5 per gallon. Others are more sanguine, yet it's not clear how the dilemma over Iranian nukes will be peaceably resolved.

If you're a worrywart, other entries on your crisis planner might include a sharp slowdown in China and an Egypt-style revolt in Saudi Arabia. There will always be a crisis somewhere, of course, but the weak U.S. economy is more vulnerable to problems elsewhere than in normal times.

*Advantage: the GOP nominee.* If problems in Europe or the Middle East were to depress the financial markets long enough, it would spread the kind of gloom that can often become self-actualizing and trigger a "confidence recession." And \$5 gas, or even \$4 gas, would probably be the kiss of death for Obama, since gas prices have an outsized effect on consumer psyches. Any oil shock at all could end Obama's presidency after one term, even if he did nothing to cause it.

**A relief rally.** The odds of a crisis in 2012 are uncomfortably high--but what if it's a short-lived one that ends decisively?

It could happen. In Europe, some analysts think a near catastrophe is the very thing that will get politicians and central bankers to take the extraordinary measures necessary to deal effectively with excessive levels of debt. Some investors, in fact, anticipate a "TARP moment," similar to what happened in the United States in September of 2008, in which a Greek default, say, or a failed Italian debt auction, generates a financial run that sends markets all around the world plunging. But such a severe reaction would also intensify the pressure on policymakers to do something drastic to intervene, which they probably would.

If Iran were to

make good on its threats and blockade Persian Gulf oil or attack western interests, it

would surely cause a panicky spike in oil prices. But the U.S. military would then intervene, probably accomplishing whatever it felt necessary to thwart Iran's nuclear ambitions. Obama, as U.S. commander-in-chief, would certainly have a strong incentive to solve that sort of problem in a hurry.

If leaders in Europe, the United States or elsewhere are able to strike a major risk from the economic equation in 2012, investors everywhere would rejoice. Dick Green of Briefing.com points out that corporate fundamentals remain very strong, with stock values likely depressed by media hype over what could go wrong. If those fears don't materialize, he argues, the stock market could enjoy double-digit gains in 2012. "The flat stock market in 2011," he writes, "has left the market coiled to spring sharply higher in 2012."

*Advantage: Obama.* A soaring stock market wouldn't directly help working-class voters with limited investments, but it would lift the overall economy as businesses began to hire more and wealthier consumers spent more freely. In this economy, any cause for optimism might feel like a victory.