



November 2018

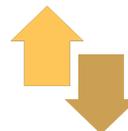
Gridlock has been good for stock returns

Voters sent a split Congress to Washington, D.C., earlier this month, which likely means gridlock will define the next two years of the Trump presidency.

With gridlock helping to temper legislative overreach, stocks are in a good position as we enter a traditionally strong period for equity returns.



Election uncertainty contributed to October's volatility.



Stocks have historically done well after midterm elections.



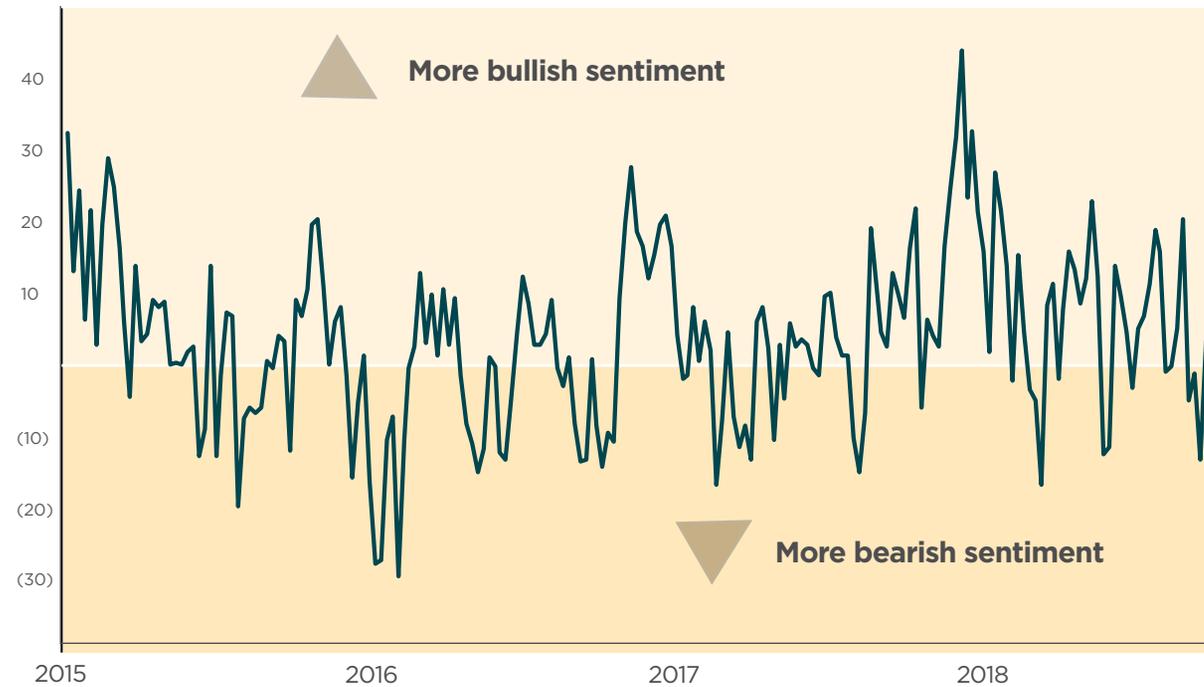
Strong fundamentals should likely support the market into 2019.



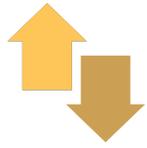
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- October was the worst month for stocks in several years, with the benchmark S&P 500® Index dropping over 7% and the Nasdaq Composite Index falling over 9% (its worst monthly performance since 2008).
- Investor sentiment fell to extreme lows during the month while volatility spiked, primarily driven by uncertainty over the outcome of the November 6 midterm elections. (See chart below.)
- The conclusion of the midterm election cycle removes uncertainty from the market, while the change in control of the U.S. House to Democrats sets up a gridlock scenario that has historically been good for the equity market.
 - As if signaling its vote of approval, the S&P 500 jumped over 2% on the first trading day after the midterm elections.

Chart 1: AAI investor sentiment index, 4-week average, 2015 to October 2018



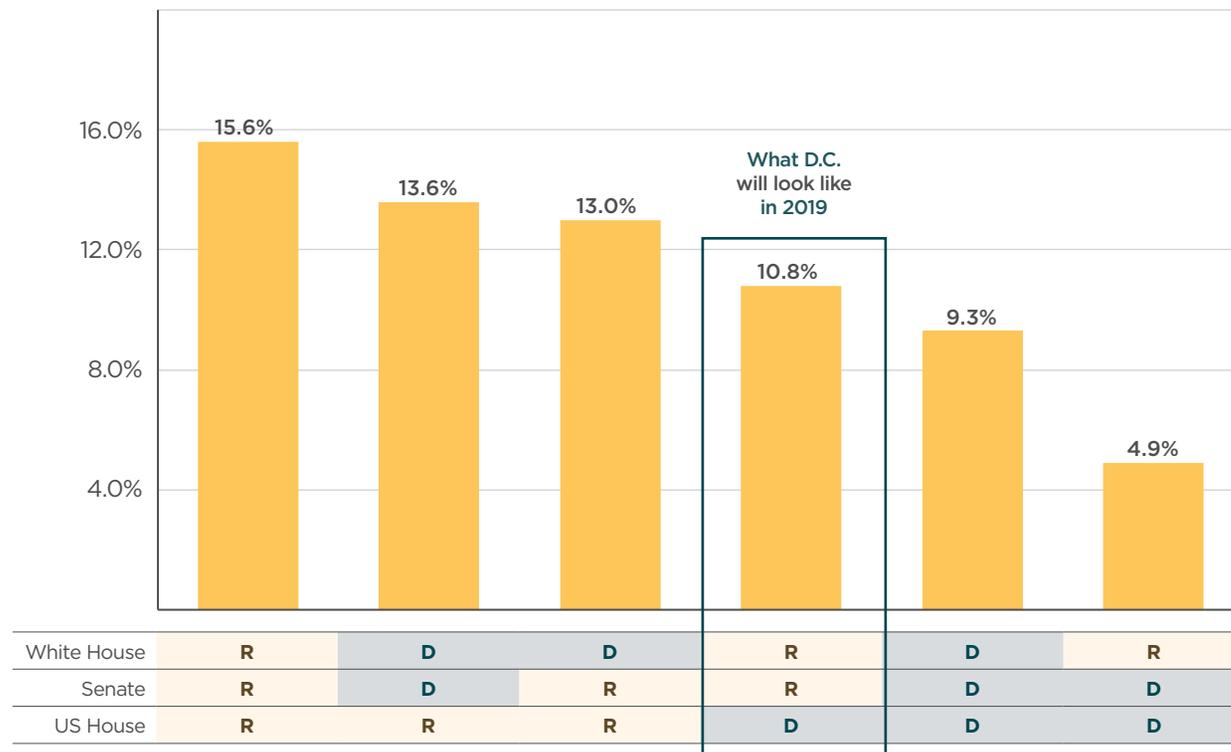
Source for chart data: American Association of Individual Investors (AAII)



Stocks have historically done well after midterm elections.

- The midterm elections are usually the inflection point for stocks in the presidential term cycle.
 - Historically, Q4 of the second year of a presidential term (after the midterm elections) has been the strongest quarter for stocks going back to 1950.
 - The S&P 500® Index has been positive in the 12 months following past midterm elections going back to 1946.
- Stocks have done well when Congress is gridlocked; the S&P 500 has returned just over 10% on an average annual basis when Congress is split during Republican presidential terms. (See chart below.)

Chart 2: S&P 500 average annual return by party control
1933 - 2016 (excluding 2001-02)



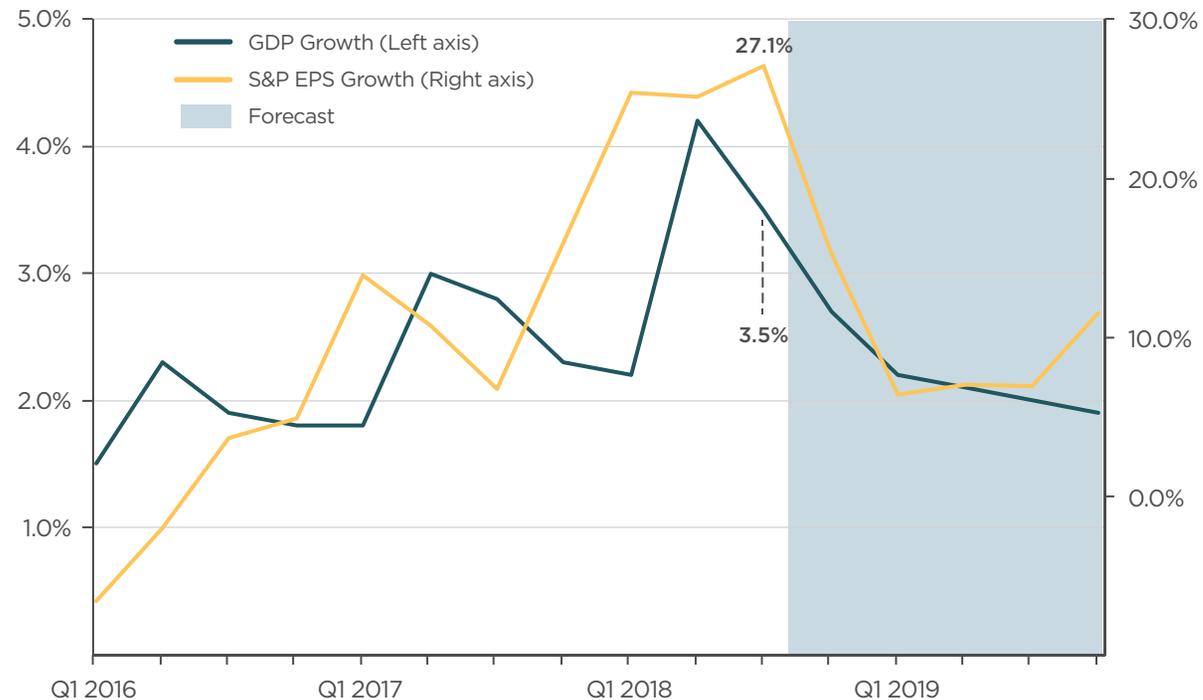
Source for chart data: Strategas Research Partners



Strong fundamentals should likely support the market into 2019.

- The U.S. economy remains on a roll, with the first estimate of Q3 gross domestic product (GDP) growth coming in at an annualized rate of 3.5%.
 - The year-over-year trend rate for real GDP growth (adjusted for inflation) has been accelerating since 2016.
- Q3 corporate earnings for S&P 500 firms were encouraging, hitting a growth rate of 27% for the third consecutive quarter on sales growth of more than 9%. (See chart below.)
- Stock investors may worry about future Federal Reserve rate hikes and what higher interest rates may mean for equity returns, but the Fed does not expect to end its tightening cycle until at least 2020, signaling positive fundamentals for market growth for the time being.

Chart 3: Gross domestic product (GDP) and earnings per share (EPS) growth rate
Q1 2016 to Q4 2019 (estimated from Q4 2018 to Q4 2019)



Source for chart data: FactSet

Key takeaways

The poor performance of stocks in October reminded investors about the market's potential for volatility, but the uncertainty over November's midterm elections had weighed heavily on their minds. Now that the election has been resolved with mixed party control of Congress, stocks are poised to roll through what has historically been one of the strongest periods for returns. The continuing strength of the U.S. economy and performance of U.S. corporations should likely support the current uptrend for stocks into next year.

- Maintain a long-term focus on stock market opportunities in a manner that aligns with your goals and risk tolerance.
- Keep political news in perspective and avoid the temptation to make investment decisions based on uncertain outcomes in Washington.
- Stay diversified to manage market risk as we continue through the late stage of the current economic cycle.



For more help or information, contact your financial advisor.



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