Two stories about stock prices are in the news this week, one about the role of lawyers, and one about that other lawyer known as POTUS. But before we dive in, let's go over a concept anyone discussing the stock market needs to be familiar with: Efficient Market Theory.

This theory states that professional brokers are way more knowledgeable than you, so shut up. Okay, maybe not that exactly. The idea is that stock prices reflect all the known information out there. For example, let's say an electronics company called Peach routinely produces blockbuster phones, tablets, and other devices. Your buddy Joe says "Dude, you gotta buy Peach stock, they keep making great stuff, their stock is going to just go through the roof!" Joe is wrong. All the brokers on Wall Street know that the next Peach product is going to be a hit, and so they're already buying stock with that in mind. The stock price has already gone up to reflect what people are predicting about Peach's future performance.

It's basically like a spread in Football. Alabama is predicted to beat Texas A&M. Does that mean you should buy stock and expect it to go up after this weekend? A win for Alabama won't necessarily make the stock price go up because brokers are already trading with the expectation of a win. Bama has to beat the spread (13.5 points). If Bama wins by 21, prices will go up. If they win by 7, prices will drop. Bama winning by 13.5 is the information the market is trading on, and only new information will change that.

Likewise, Peach's next product being a hit will not necessarily move prices up. The market is already trading on the 'knowledge' that it will be a hit. For prices to go up, it needs to be a larger hit than anticipated.

Now let's move on to the story coming at us from the [ABA Journal: Deal lawyers are not adding value to mergers]. The study comes from two law professors, Jeffery Manns (GW) and Robert Anderson (Pepperdine). They studied nearly 500 mergers between 2002 and 2011 and found that when the basic terms of the deal (mostly the price) are announced, stocks respond. That's what we'd expect. New information comes out and the market reacts. If the price were exactly what analysts were predicting, it'd stay the same, because it'd actually be trading at that price already.

So what happens later when the deal lawyers hammer out all the other legal terms and those are announced? Nothing. Stock price stays put. Manns and Anderson read this as meaning the market doesn't really care what the lawyers are doing, and thus the lawyers are not an added value.

But taking Efficient Market Theory into account, we can understand this lack of change differently. If the price stays the same, the lawyers have done what brokers predicted. If brokers already factored in the value added by having good counsel hammer out the terms then we shouldn't expect a change in price. The lack of change doesn't mean no value added, it just means that the lawyers are performing pretty much how the market expects.

And now on to the other story. On Wednesday, after Barack Obama won the election, the Dow dropped by about 2%. Immediately Romney supporters started harping on this as proof that the business world thinks Obama will hurt the economy. But going with Efficient Market Theory, what does the change tell us? That the market simply was wrong in predicting how the election would go.

But the direction it moves matters!

Okay, yes. A drop would mean that it was not only wrong, but that the outcome was worse than predicted. If the market was predicting a Romney win, then a downward move would indicate the market thinks an Obama victory is worse than Romney. But what if the market was predicting something else? Maybe it predicted Democrats picking up more seats in Congress than it did, and than poor performance caused the market to go down, then we'd read the market as saying it supports Democrats.

Or it could have been predicting lower turn out on election day and shorter waits due to many people engaging in early voting. If turn outs are high and people are spending a long time waiting in line then there are more lost wages and lost productivity in the economy on Tuesday. That would also cause a drop in stock prices.

And of course, a million other things were going on in the world at the same time as the election, such as bad economic reports coming out from Germany. It's impossible to disaggregate the impact of different events.

Finally, the market just moves. Every day, and a 2% swing over one day isn't really a big deal, so odds are the market isn't saying anything about Obama. The market has dipped below its current level 8 times since February, and spent a month below that level in May and early June.