

## It's A Natural Disaster, Not A Black Swan

At times of natural disaster and personal tragedy, it can be difficult to focus on economics. The devastation in Japan is beyond what the “dismal science” is designed to comprehend. However, there is an economic component to the Japanese earthquake as there is with any disaster.

In Haiti, for example, decades of awful leadership have created deep-seated poverty and corruption, which amplified the size and scope of its recent earthquake. In Kobe (1995), Chile (2010), San Francisco (1989), Katrina (2005), mostly free markets, accumulated wealth and a disdain for corruption helped overcome those disasters relatively quickly. In Japan today, the same will be true.

None of this means that these large scale disasters won't happen and that lives and property won't be lost. There is no place on earth that is safe from natural disasters. They are inevitable, they are not Black Swans. We know they will happen and we know that planning and accumulated knowledge help minimize the totality of damage. Japan and the world will overcome and recover. They always do.

To that end, what we know is that hardest hit areas in Japan represent a very small portion of the Japanese economic output. Early estimates put the cost at around \$100 billion. However, electricity output has been dramatically affected which is forcing closures of plants that were not directly impacted by the quake or tsunami.

A debate is underway about how this will impact the economy going forward. Hurricane Katrina (which totaled \$81 billion in property losses) is a relatively good example. While many predicted a bad US recession, caused by the hurricane,

the economy continued to grow in its aftermath and after digging into the data it's hard to see anything but a very minor and temporary impact on the economy at all. GDP growth accelerated in the following year. Nothing remotely close to a recession occurred.

Some could attribute that to rebuilding and clean-up. But don't think that this is all good news. It would be what Henry Hazlitt called the “fallacy of the broken window.” Hazlitt told a story about a vandal who broke a shopkeeper's window, which caused a glassmaker to get an additional order. But the shopkeeper was planning on using that same money to buy a new suit, so the tailor lost an order. In other words, even though rebuilding appears to create new economic activity, fixing things that have been destroyed actually robs an economy over time of the benefits of growth. Repairing does not generate new wealth, it only replaces old wealth.

Even if real GDP growth in Japan were to accelerate, the people of Japan would not be better off in a strictly material sense. Nonetheless, the Japanese economy (outside of the areas affected directly) will continue to grow. In the end, there is a cost to these disasters, but it is absorbed by growth and is hard to actually see from 30,000 feet.

There will be many ups and downs in the days ahead, and economic analysis at a time like this may seem crude...almost rude. Some will allow this event to scare them away from taking risk, but the real risk is assuming that the world is out of control and Black Swans are proliferating. These fears will make markets cheap for those who can keep things in perspective. Buy the dips. Japan and the world will overcome.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
3-15 / 7:30 am	Empire State Mfg Index - Mar	16.4	<b>20.0</b>		15.4
7:30 am	Import Prices - Feb	+0.9%	<b>+0.5%</b>		+1.2%
7:30 am	Export Prices - Feb	+1.0%	<b>+0.5%</b>		+1.5%
3-16 / 7:30 am	PPI - Feb	+0.7%	<b>+0.7%</b>		+0.8%
7:30 am	"Core" PPI - Feb	+0.2%	<b>+0.1%</b>		+0.5%
7:30 am	Housing Starts - Feb	0.570 Mil	<b>0.600 Mil</b>		0.596 Mil
3-17 / 7:30 am	CPI - Feb	+0.4%	<b>+0.4%</b>		+0.4%
7:30 am	"Core" CPI - Feb	+0.1%	<b>+0.1%</b>		+0.2%
7:30 am	Initial Claims - Mar 12	387K	<b>391K</b>		397K
8:15 am	Industrial Production - Feb	+0.6%	<b>+1.0%</b>		-0.1%
8:15 am	Capacity Utilization - Feb	76.5%	<b>76.8%</b>		76.1%
9:00 am	Philly Fed Survey - Mar	30.0	<b>32.4</b>		35.9
9:00 am	Leading Indicators - Feb	+1.0%	<b>+1.2%</b>		+0.1%