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Beware of Popular Narratives

Narratives matter. They affect political outcomes and influence investment decisions. Narratives serve a purpose, but in serving that purpose they are often highly misleading, especially when they are invented to cover up a mistake, or to convince people to vote a certain way. These days, there are three main narratives impacting investors.

Narrative #1 says that Wall Street caused the Great Recession of 2008/09 and that government saved the economy, and recoveries are always slow after financial crises.

Narrative #2 argues that the US is not really in recovery. Anything good happening out there, a rising stock market or falling unemployment rate, is either a bubble or a lie.

Narrative #3 says that the US government did not allow all the excesses of the 2008 crisis to be completely wrung out of the system. Using Quantitative Easing, TARP and government stimulus to boost economic activity has created a bubble on top of a bubble. The next crash will be even bigger.

We don't believe in any of these narratives. We believe that government (Fannie Mae, Freddie Mac, 1% interest rates, the Community Reinvestment Act, and Mark-to-Market Accounting) caused the crisis. The Troubled Asset Relief Program (TARP) and QE did not fix it, either. The S&P 500 fell 40% in the five months after TARP was passed and QE was invented. What turned things around was finally getting rid of the nonsensical mark-to-market accounting rule in March 2009. Only then did the stock market and economy turn around. This is a real, innovation-driven recovery.

Those who believe that the unemployment rate is a lie are ignoring the fact that jobs have climbed for 70 consecutive months and initial claims have been below 300,000 for almost 1 ½ years. These same analysts say the US stock market is one big bubble, inflated by global central banks. Yes, they say, the Fed "tapered" and stopped QE, then raised interest rates, but now foreign central banks have taken up where the Fed left off.

What they can't explain is why it didn't work the other way. Why have European and Japanese stocks fallen so far behind US stocks in the past 7 years? If foreign QE lifts US stocks, why doesn't US QE lift foreign stocks? No major European or Asian stock market is at record highs like the US.

All the bubble talk is either cover for a blown forecast, or an excuse to explain something good by someone who has said that nothing good can happen with a Democrat in the White House. Those who spin this narrative have argued for the past seven years that the US stock market or economy would collapse. But since the opposite has happened, these pundits have fallen back to the defensive position that everything is a bubble.

Slow growth isn't a surprise to us. We have called it a Plow Horse economy for a long time. But that is because government spending, taxation and regulation hurt economic growth, not because of financial problems. Continental Europe has an even bigger government burden and we call Italy, France, Spain, Greece, et al., a "Plow Horse with Shin Splints."

What we find interesting about all these narratives is that they are all so government-centric. All of them seem to ignore the role of Entrepreneurship. In the past seven years, fracking has made the US the most productive energy producer in the world. The cloud, smartphone, tablets, apps, 3-D printing, genetic mapping and testing, vertical farming, and Big Data are all boosting productivity and profits at company after company.

For the record, Ben Bernanke and Janet Yellen have never fracked a well or pulled an all-nighter writing an app, and those who call the stock market a bubble are actually slapping entrepreneurs and innovators in the face. QE did not create the cloud or Big Data. Entrepreneurs did! The stock market, jobs, incomes and profits are all up because of these new technologies.

The narratives the conventional wisdom has chosen to use to describe the economy are woefully inadequate and misleading. They should come with Surgeon General warning labels.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
8-15 / 7:30 am	Empire State Mfg Survey – Aug	2.0	2.5	-4.2	0.6
8-16 / 7:30 am	Housing Starts – Jul	1.180 Mil	1.190 Mil		1.189 Mil
7:30 am	CPI – Jul	0.0%	0.0%		+0.2%
7:30 am	“Core” CPI – Jul	+0.2%	+0.2%		+0.2%
8:15 am	Industrial Production – Jul	+0.3%	+0.4%		+0.6%
8:15 am	Capacity Utilization – Jul	75.6%	75.6%		75.4%
8-18 / 7:30 am	Initial Claims Aug 15	268K	265K		266K
7:30 am	Philly Fed Survey – Aug	2.0	-0.7		-2.9