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First Trust

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Monday Morning Outlook

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Who Gets Credit For the Recovery?

What's the opposite of a double dip? Whatever it is, that's where we are. Remember commercial real estate, re-setting ARMs, foreclosures, muni-bond defaults, Greece, Ireland, Egypt, Tunisia, Libya, high unemployment, more savings, or just plain old government debt? At least one of these, or maybe all of them, was going to make recovery impossible, or end any recovery prematurely. But none of it happened. The double dip turned out to be a figment.

Real GDP has expanded for six consecutive quarters, seven if housing is excluded. Retail sales are up 7.8% in the past year and 10.6% at an annual rate in the past six months. The ISM manufacturing index is now at its highest level since 1983. Initial claims fell to 368,000 and private sector jobs have expanded for twelve consecutive months, racking up a total gain of 1.5 million. The data can't be ignored and the battle to take credit for the recovery is underway.

Democrats say stimulus caused the recovery and cutting back will end it. Paul Krugman (New York Times' columnist) wants a great deal more spending, Mark Zandi (Moody's Analytics) says Republican plans to cut $60 billion in spending will cost 700,000 jobs. To some, just the thought of cutting spending is enough to threaten the economy.

Republicans are still stuck in dreary-land for the most part, but some are getting more optimistic on the economy and are starting to announce that the November election caused business to become more optimistic and "certain." This, they say, has caused job creation to accelerate. Just the thought of Republicans in power is helping the economy.

Ben Bernanke is even in on the game. He won't say the economy is strong, but he is trying to take credit for the stock market. Bernanke told Congress last week that the "first round" of Quantitative Easing (QE) was "almost the same day as the trough of the stock market." It's doubled since then and the economy turned up, too.

All of this is so blatantly political that it takes our breath away. With all due respect to Ben Bernanke, QE1 started in September 2008. The Fed's balance sheet tripled between then and March 2009, but the stock market got crushed anyway. When mark-to-market accounting was changed to allow cash flow, instead of illiquid market prices to be used to value assets, the equity market bottomed.

Once the accounting rule was "fixed," any risk of a Depression vanished and the economy started to recover. Private investment into banks resumed and corporate profits surged. Credit spreads collapsed and stock prices increased. But, corporate profits have increased faster than stock prices, which is why price-earnings ratios have fallen.

If it really was QE that lifted stock prices, then P-E ratios would have increased, not decreased. In other words, easy money would have puffed up stock prices, just like easy money puffed up housing prices. Never before in history has a Fed Chairman tried to say that easy money lifted stocks for two years, but that the economy is still so weak that it needs more easy money. Economically speaking, this isn't even shaky ground, it is non-existent ground. There is no economic theory that justifies Bernanke's thought process.

What's terrible is that all of this political spinning is confusing the average American about what drives economic activity. It's not the Fed or the government, it's the private sector. It's entrepreneurs that drive wealth creation.

And no matter how many times people try to say that free markets fail and government must "help us" when they do, it doesn't make it true. Free markets don't fail, governments fail. The US never would have had over-investment in housing if the Fed had not lowered interest rates to 1% back in 2004. And the over-investment in housing never would have created a financial crisis if mark-to-market accounting had not been instituted in November 2007. Who gets the blame and who gets the credit is the biggest economic battle of our times. Politicians, of course, all want the credit and they are not shy about asking for it. The American Entrepreneur is too busy to ask. But, it's the entrepreneur that deserves the credit, nonetheless.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
3-7 / 2:00 pm	Consumer Credit - Jan	+$3.5 Bil	**+$0.9 Bil**		+$6.1 Bil
3-10 / 7:30 am	Int'l Trade Balance - Jan	-$41.5 Bil	**-$42.2 Bil**		-$40.6 Bil
7:30 am	Initial Claims - Mar 5	375K	**372K**		368K
3-11 / 7:30 am	Retail Sales - Feb	+1.0%	**+1.2%**		+0.3%
7:30 am	Retail Sales Ex-Autos - Feb	+0.7%	**+0.9%**		+0.3%
7:30 am	Business Inventories - Jan	+0.8%	**+0.7%**		+0.8%
8:55 am	U. Mich. Consumer Sentiment	76.5	**77.5**		77.5