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Monday Morning Outlook

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Unnecessary and Artificial Stimulus

Let's hear it for irony. In almost simultaneous events last week Congress attacked baseball players for taking performance-enhancing drugs while at the same time supporting artificial and temporary stimulus for the US economy no matter what the long-term costs.

Forget the interesting question of why Congress thinks it has the time to waste investigating major league baseball in the first place; focus instead on the similarities between baseball players (or athletes in general) and the economy (or wealth creation).

Successful athletes train smart, work hard, eat well, sleep deeply, and practice, practice, practice. Some athletes have more talent or luck than others, while some are more disciplined, or just more tenacious. But, in general, those who work hard and smart have more success.

Successful economies are built on innovation, creativity and technological ingenuity. The better a country is at creating a positive environment, where this human ingenuity has a chance to bloom, the stronger its underlying growth, the more wealth is produced and the higher the standard of living climbs.

None of this means things are simple. Gifted athletes, enticed by big money or the thrill of victory, use artificial stimulus to enhance performance, or help in injury recovery. Politicians, enticed by the potential to gather more votes, use temporary economic stimulus for short-term gain.

Accelerating recovery from an injury is a positive use for these drugs. In fact, many doctors prescribe them to non-athletes for just this short-term benefit. Unfortunately, using these drugs persistently to enhance performance can have harmful side effects and produce long-term damage.

The same is true for economic stimulus, like Federal Reserve interest rate cuts. Sometimes, interest rate cuts are just what the doctor ordered. But this is only true when they were too high in the first place. Using easy money to alleviate pain that was not caused by hard money is dangerous. It may boost economic growth in the short-term, but this comes with harmful side-effects like inflation, a weak dollar, and eventually much higher interest rates.

The other kind of stimulus favored by Washington DC leans heavily on rebates – money – that politicians get from one group to give to another. But paying rebates, when a budget deficit exists, means that someone, at some point down the road, will be forced to pay it back. Moreover, because the money to fund rebate checks must be borrowed, it crowds out domestic private investment that might have been used to shore up losses at financial institutions.

Many people don't like professional baseball players using steroids because they mask the underlying ability of the player. They taint the results.

But so does artificial economic stimulus. Monetary policy accommodation can help people feel wealthier for awhile, but it cannot create wealth. Printing money does not make anyone wealthier. If it did, then counterfeiting should be made legal and everyone in the world would then be wealthy. The same is true for tax rebates. If they really could increase wealth, then why not make them much larger and much more frequent?

In the end, trying to increase spending without increasing the country's productive capacity is a fool's errand. Boosting demand without boosting supply causes a misallocation of resources. Like with steroids any boost is temporary and risks longer-term economic problems.

Both interest rate cuts and rebate checks will boost economic numbers as spring turns to summer, but our models show that the economy never needed any stimulus in the first place. Remember, after growing at only a 0.6% annual rate in the first quarter of 2007, the economy grew at nearly a 4.5% rate in Q2/Q3 of last year, without a boost from tax rebate checks or Fed rate cuts. The same thing is likely to happen again this year, but with an extra "pop" from the unnecessary and artificial stimulus.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
2-20 / 7:30 am	CPI – Jan	+0.3%	**+0.3%**		+0.3%
7:30 am	"Core" CPI - Jan	+0.2%	**+0.2%**		+0.2%
7:30 am	Housing Starts - Jan	1.009 Mil	**1.000 Mil**		1.006 Mil
2-21 / 7:30 am	Initial Claims - Feb 16	348K	**344K**		348K
9:00 am	Philly Fed Survey - Feb	-12.0	**-12.6**		-20.9
9:00 am	Leading Indicators - Jan	-0.1%	**-0.1%**		-0.2%