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INSIGHTS

RHYMING RECOVERIES

Mark Twain famously said, 'History doesn't repeat itself, but it often rhymes.'

Economists continue to draw comparisons between this post-COVID recovery and economic recoveries of the past, in an effort to make the case that government spending creates economic growth. However, there is no precedent for the government's actions undertaken over the past 15 months - making historical comparisons redundant.

Normal economic downturns are called "recessions." Growth phases are called "recoveries." The combination of these ups and downs makes up a "business cycle."

The catch – this has not been a normal business cycle. The contraction in the economy last year was not a normal recession – the government interrupted the normal business cycle by shutting down businesses. Similarly, the government doling out 'stimulus' money to support the economy cannot be framed as a normal recovery.

It is true that when government borrows money from the Federal Reserve, or borrows money from future taxpayers, and gives that money directly to people, spending goes up. But that is not a real (or sustainable) recovery. To use the Federal Reserve's favorite term, it is transitory.

Countries around the globe shut down major parts of their economies and kept people from working. This caused major economic disruptions within supply chains, put businesses and services that were not labeled "essential" under undue stress, and displaced millions of workers.

Henry Ford

In 1914, Henry Ford decided to pay his workers $5 a day to prevent turnover, but also so his employees could afford to buy the cars they were making. In contrast, in 2021 the government is paying people not to work, so they can buy things they did not produce. It is no wonder there are shortages.

Governments attempting to address the self-inflicted pain of shutdowns by borrowing money to stimulate the economy is akin to giving morphine to someone injured in a car accident – it masks the pain, but it does not heal the injuries.

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This masking effect shows up in the economic data. The US is still 7.6 million jobs short of where it was in February 2020. Yet, retail sales, which fell 20% during the year-ended April 2020, rose 51.2% since then - more than fully recovering! In the past 24 months, total retail sales are up 10% per year, on average, versus a 3.6% growth rate from 2014-2019. The only way a situation can arise where fewer people are working but spending is increasing is by having the government borrow, print, and distribute money for people to spend today. A boost in spending is a short-term shot in the arm for the economy, but its effects are short-lived and, as opposed to investing, spending does not create lasting wealth.

It's true that the economy is expanding. Part of this is because the economy is opening up, but part of it is because the government is borrowing money from future production to spend today.

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