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President Trump Surfs A Prosperity Wave That Could Grow Larger

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During Christmas, President Trump, according to Reuters.com, observed:

"We've got prosperity - now we want peace," Trump told a child named Ryan, who called the North American Aerospace Defense Command (NORAD) to check on Santa's progress.

Whether or not In Trump You Trust, peace and prosperity are his signature themes. "We've got prosperity" is a big claim.

Yet, so far, it's pretty well grounded. The Bureau of Economic Analysis reports real GDP growth rate of over 3% for both the second and third quarters of 2017, substantially greater than the rate of the two previous years. If it keeps up it represents a significant breakthrough.

That's a breakthrough that plenty of naysayers claimed impossible. It is one that some "until the last dog dies" Dems still deny.

Does President Trump deserve the credit for this wave of handsome growth?

Skill? Luck?

Politically, doesn't matter. Voters just want results.

Accordingly to *Washington Post* economic columnist Robert Samuelson, Fed Chair Janet Yellen deserves the lion's share of the credit:

One of Washington's permanent parlor games is how much credit or blame a president deserves for the state of the economy. Inevitably, then, the question being asked now is whether Donald Trump or Barack Obama created today's strong economy. The correct answer: neither. To the extent that personal responsibility can be assigned, the worthy recipient is Janet Yellen.

In practice, presidents' influence over the economy is limited. If it were otherwise, we'd live in an economic paradise. Unemployment would always be low, wages would always rise, and recessions would never occur. No one has that kind of power. Presidents and their agencies can't govern the business cycle.

…

Under Yellen, the economy has made huge progress. Here's the record since she became Fed head in February 2014: Payroll employment has expanded by nearly 10 million jobs; the unemployment rate has dropped from 6.7 percent to 4.1 percent; average hourly earnings, uncorrected for inflation, rose from $24.32 to $26.55. (Corrected for inflation, the wage gain is about 4 percent — not great but not stagnation either. The pace, if maintained, would be roughly 10 percent over a decade.)

Notwithstanding Fed skeptics like *Forbes.com*'s own John Tamny, Samuelson makes a reasonably persuasive case.

Also giving the Yellen Fed high marks is one of the most highly esteemed monetary economists working today, Scott Sumner. For the benefit of those (unlike me) who were not born and bred in the monetary policy briar patch Sumner was called by The *Atlantic Monthly: "The Blogger Who Saved The Economy*."

Have you heard of Scott Sumner? Unless you're an economist, an economic blogger, or a student at Bentley University, where Sumner is a professor, you probably haven't. And that's a shame. Because there's an outside chance that he just saved the economy.

Sumner is the author of The Money Illusion, an excellent blog that has relentlessly made the case since 2009 for an eccentric policy called "NGDP targeting." This is a complicated sounding plan with a simple idea at its heart. If the equation that solves the economic crisis is "GDP growth + inflation = 5%" then the solution to low GDP growth is inflation that brings us up to 5%. Therefore, the Federal Reserve should announce that it will do everything in its power to raise inflation expectations until we're back to where we want to be.

Three years ago, this idea didn't have a stable home outside the wilderness of The Money Illusion. But it slowly gained credence among bloggers, economists, and finally, the Federal Reserve itself.

So, what's next for the political economy and your portfolio?

Sumner, now at Mercatus Center, wrote earlier this year at *The Money Illusion*, *An even greater moderation?*

I am going to go out on a limb and predict that we are now entering a new Great Moderation, even more stable than the 1985-2007 period. … So why do I think we are entering an even greater moderation? Seven reasons, none of which I expect people will find all that persuasive…

Which Sumner then enumerates. And which I find pretty persuasive. Sumner, along with David Beckworth, also at Mercatus, are two of the leading proponents of something called "market monetarism" or NGDP targeting.

Per Wikipedia:

Market monetarism is a school of macroeconomic thought that advocates that central banks target the level of nominal income instead of inflation, unemployment, or other measures of economic activity, including in times of shocks such as the bursting of the real estate bubble in 2006, and in the financial crisis that followed.[1] In contrast to traditional monetarists, market monetarists do not believe monetary aggregates or commodity prices such as gold are the optimal guide to intervention. Market monetarists also reject the New Keynesian focus on interest rates as the primary instrument of monetary policy. Market monetarists prefer a nominal income target due to their twin beliefs that rational expectations are crucial to policy, and that markets react instantly to changes in their expectations about future policy, without the "long and variable lags" postulated by Milton Friedman.

As an aside, Memo to Drs. Sumner and Beckworth. According to Braithwaite Communications, per Nobel Prize in Economics winner Daniel Kahneman:

“No one ever made a decision because of a number,” Kahneman said afterward. “They need a story.”

He went on to demonstrate this phenomenon in multiple experiments. In case after case, he showed that people disregard even obvious facts and figures in favor of more vivid descriptions.

In essence, the easier people can picture something in their heads, the more they believe it. “The confidence that individuals have in their beliefs depends mostly on the quality of the story they can tell about what they see, even if they see little,” Kahneman later wrote in his best-selling book, “Thinking, Fast and Slow.”

Long story short: stories drive decisions. Data is difficult to decipher when it’s isolated, but it becomes meaningful if packaged with familiar or evocative concepts.

Anyone that ignores this reality is fighting against human nature. That’s a war you can’t win.

Where does President Trump, a master of “evocative concepts,” come in?

President Trump, uncharacteristically without much fanfare or drama, recently made and announced what is and will probably be the most important action respecting economic policy of his entire first term. Trump nominated Fed Governor Jerome Powell to succeed Chair Yellen at the Fed.

Powell has been described as a Yellen-like “cautious dove.” "Cautious hawk" might be more apt, yet all to the good.

Also, Memo to Fed Chair-designate Powell. Benn Steil and Benjamin Della Rocca, writing recently at the *Council on Foreign Relations*, warn Powell of the danger of becoming an Accidental Hawk:

Fed Chair nominee Jerome (Jay) Powell was a logical choice for Fed chair. A business-friendly Republican, he is likely to push forward President Trump’s deregulation agenda in the financial sector while continuing the Yellen Fed’s softly-softly approach to monetary tightening—an approach that has kept markets unusually calm and cheerful. Yet the course on which he’s heading looks more hawkish than he intends.

So, nothing taken for granted here. Yet there are grounds for optimism.

Trump’s appointment of Powell may have secured the sustainability of “the greater moderation,” permitting economic expansion to continue -- and grow. This may be far more significant than the recent high-profile tax cut passed in the Congress and signed into law with great fanfare by President Trump on December 22, who declared:

And all of this — everything in here — is really tremendous things for businesses, for people, for the middle class, for workers. And I consider this very much a bill for the middle class and a bill for jobs. And jobs are produced through companies and corporations, and you see that happening. Corporations are literally going wild over this, I think even beyond my expectations, so far beyond my expectations.

One hopes that these claims are not mere hyperbole. Sumner, like me, concludes, "Will the tax cut boost growth? I am enough of a supply-sider to think the answer is "yes", and enough of a realist to think the growth effects will be quite modest, maybe a couple of tenths of percent per year over the next decade (mostly front-loaded)."

The classic Mundell/Laffer/Kemp/Reagan supply-side policy mix weighted the restoration of good monetary policy at least as heavily as, perhaps more than, tax rate reductions. The vanquishing of inflation by Chairman Paul Volcker certainly was as important in unleashing the tsunami of economic growth as were the tax rate reductions.

Volcker's successor, Fed Chairman Alan Greenspan, eventually disclosed his own Secret Sauce behind the Great Moderation and its attendant sizzling growth. Greenspan, earlier this year, revealed that during the period of the Great Moderation he was carefully emulating the operation of the gold standard. As I wrote here:

Former Fed Chairman Alan Greenspan just provided a barely noticed Big Reveal. In an interview with the World Gold Council's *Gold Investor* Chairman Greenspan, stating "I view gold as the primary global currency," went on to explicitly reveal, for the first time to my knowledge, that "When I was Chair of the Federal Reserve I used to testify before US Congressman Ron Paul, who was a very strong advocate of gold. We had some interesting discussions. *I told him that US monetary policy tried to follow signals that a gold standard would have created.* [Emphasis supplied.]

The period of "following signals that a gold standard would have created," called the Great Moderation under President Clinton, was one of the most equitably prosperous in modern American history. That era saw the creation of over 20 million jobs. Robust growth converted the federal deficit into a surplus. It was, if only virtually rather than institutionally, a golden age.

The full interview at *Gold Investor* is well worth reading. It emphasizes the significance which Greenspan, during this period, attached to the dollar price of gold.

To loop back to Chair Yellen for a moment. The Fed appears to have stabilized the dollar-denominated price of gold between $1100/oz and $1400/oz -- primarily between $1200 to $1300 -- since January 2014. This would appear consistent with the range maintained by Chairman Greenspan during the Great Moderation.

Brava, Chair Yellen! Will Chair Powell follow her example?

Let's hope so.

Greenspan's secret monetary compass was inferred in 1995 by monetary economists William Lastrapes and George Selgin (now at Cato Institute), from the University of Georgia, in *Gold Price Targeting By The Fed*. Excellent deduction, Holmes! Greenspan, in the tradition of opacity deemed seemly by all central bankers, did not confirm this until over 20 years later. Yet there it is.

My favorite monetary economist considers NGDP targeting a (far) second-best option, after the classical gold standard. That said, for now, let us Gold Standard vs. Market Monetarist Bugs set aside our squabbles and cautiously toast the nomination of Jerome Powell and wish him great success.

Let this brief truce be undertaken in the spirit of humility, a quality for which I, neither an economist nor a PhD, am far more entitled than are Drs. Sumner and Beckworth. After all, as the Bank of England's flamboyant governor Montagu Norman once said to a new staff economist, "We have appointed you as our economics adviser. Let me tell you that you are not here to tell us what to do, but to explain to us why we have done it."

Thus, let us now praise President Trump for his appointment of Jerome "Cautious Hawk" Powell to the chairmanship of the Fed. And let us hope that the President's astute appointment will lead to a continued, even heightened, organic economic expansion through 2018 and beyond.