

Harvey & The Broken Window Fallacy

Weekend Reading

As the waters recede from "Hurricane Harvey," the rebuilding efforts begin. It will take quite some time before Houston fully recovers from the tragedy, but recover we will. Hopefully, lessons were learned by a city government that has avoided dealing with the drainage and flooding problems for far too long. **Despite hundreds of millions of dollars extracted from the citizenry of Houston via a "rain tax," the money was absorbed by the profligate spending of repeated feckless Mayors who chose to spend on "bike trails," "green energy," and other liberal agendas rather than resolving a critical issue that has plagued Houston for years.** We'll see. But I won't hold my breath as Houston continues to follow the shining examples of other fiscally responsible governments like Chicago, Detroit, and others. *[sarcasm alert]* But that is a story for another day. Currently, the mainstream story is the "economic boost" which will come from the recovery process. This is the essence of the ["Broken Window Fallacy."](#)

*"A window is destroyed, therefore the window has to be replaced which leads to economic activity throughout the economy. However, the fallacy of the 'broken window' narrative is that **economic activity is only changed** and not increased. **The dollars used to pay for the window can no longer be used for their original***

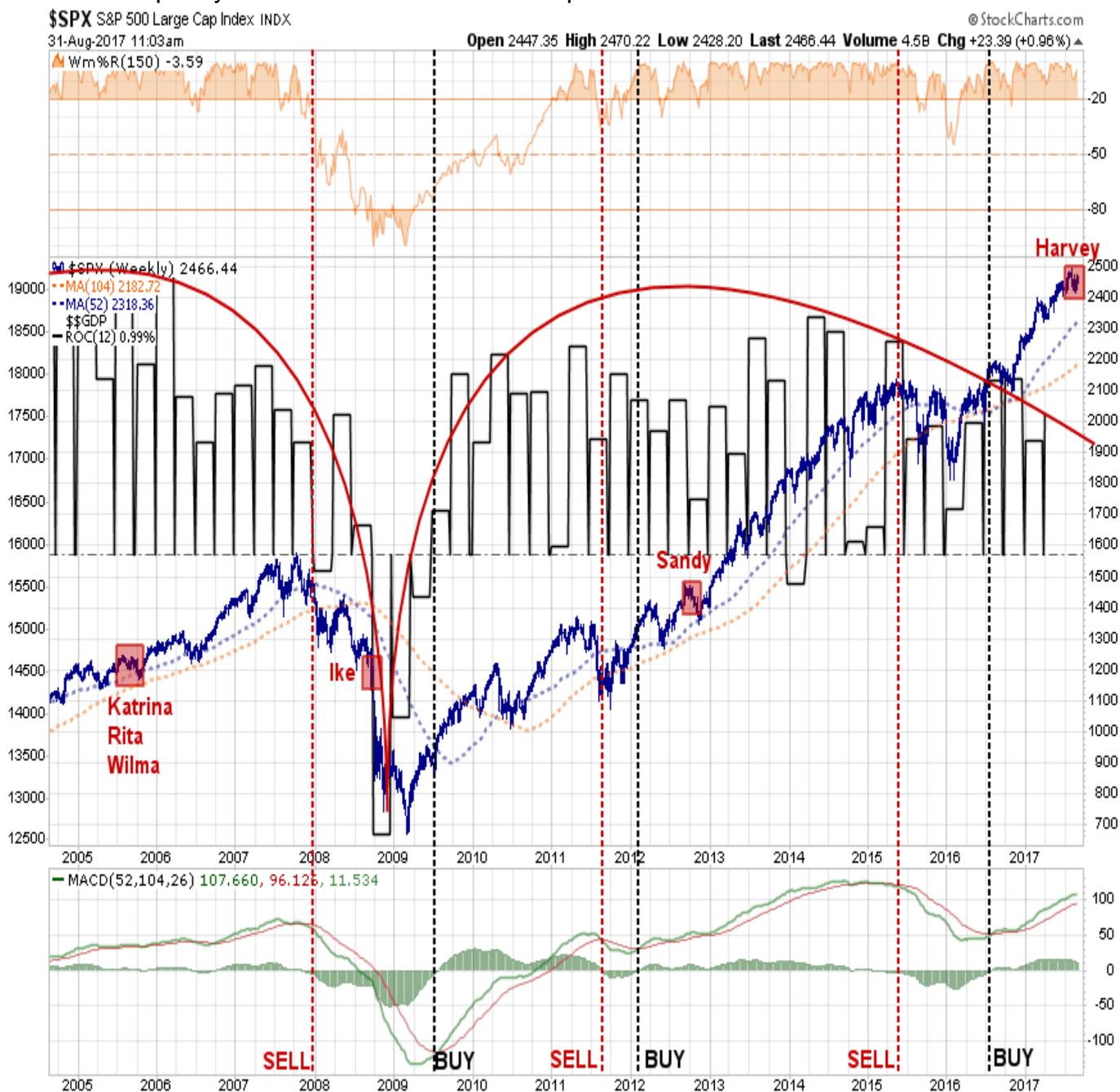
intended purpose. There is no free lunch."

To put a finer point on it:

"If natural disasters are such a good deal for the economy, why wait for Acts of God to come along? Why not nuke? <https://t.co/nc5WBUVzKW>

? Real Investment News (@RINonAir) [August 29, 2017](#)

She is right. Obviously, nuking cities to create economic growth is just plain silly. However, in the short-term, there will be thousands of temporary jobs created, supplies used, services needed and wages paid which will provide a **temporary** economic boost. **Unfortunately, what is not being accounted for is the offsetting of lost wages, business incomes, and other costs for the individuals and businesses that have been devastated and displaced by this tragedy.** From a market perspective, hurricanes have little impact in reality. **In 2005, the U.S. was rocked by three hurricanes over a three month period.** The market dipped but recovered shortly thereafter as the event was quickly absorbed by market participants. There was also a quick spat of economic growth which quickly faded over the next several quarters.



In 2008, "Hurricane Ike" made landfall at the same moment that Lehman was forced into

bankruptcy. However, what was not known by market participants at that time, because the NBER had not declared it, was **the U.S. was already in a deep recession.** It only got worse following the event. "*Hurricane Sandy*", much like "*Katrina*," "*Wilma*," and "*Ike*," **also provided a 2-quarter boost to economic output which quickly faded as the temporary inputs came to an end.** The market blinked, but then continued its advance. The difference between the outcomes of "*Ike*" and the other storms was really dependent on the overall cycle of the market. "*Ike*" occurred with market and economic sentiment already turning negative. That is not the case with "*Hurricane Harvey*" as overall market and economic sentiment remains very robust, even exuberant. Over the next couple of quarters, market participants will have their attitudes bolstered by better than expected economic numbers. Such will also give President Trump some cover despite the lack of legislative agenda moving forward. **However, it is the trend of the economic growth rates that must be paid attention to.** Despite hopes of a never ending "*bull market*" supported by ongoing "*emergency measures*" from Central Banks globally, **the reality is we are very late in the current economic cycle.** Just like in 2008, it was well after the fact, when the economic data was negatively revised, the recession became clearly evident. Given the deterioration in credit, the rise in delinquencies and plunge in savings rates, the economic backdrop is likely far weaker than headlines currently suggest. While Harvey may extend the current cycle for a little while longer, I would not get overly complacent with highly aggressive allocation models. **Like I said, there is no free lunch.** Here is what I am reading this weekend.

Politics/Fed/Economy

- **Keep It Simple Tax Strategy** by [Stephen Moore via Washington Times](#)
 - **No, Hurricanes Are NOT Good For The Economy** by [Caroline Baum via MarketWatch](#)
 - **Trump Pitches Massive Tax Plan** by [Bob Bryan via BI](#)
 - **Markets Are Worried About The Debt Ceiling** by [Akin Oyedele via BI](#)
 - **Tax Reform Should Not Add To The Debt** by [Committee For A Responsible Budget](#)
 - **Is GOP Tax Bill Focused On The Future Or Past** by [Neil Irwin via NYT](#)
 - **Trump Could Trigger A Shutdown** by [Stan Collender via Forbes](#)
 - **Can Trump Turn His Presidency Around** by [Michael Boskin via Project Syndicate](#)
 - **Dollar Struggles Are Reflection Of Trump Agenda** by [Pedro Da Costa via BI](#)
 - **The "Free" Economy Comes At A Cost** by [The Economist](#)
 - **15-Events That Could Trigger Next Recession** by [John Mauldin via Forbes](#)
 - **Thoughts On Failure Of Unemployment** by [Edward Harrison via Credit Writedowns](#)
 - **Get Ready For Deluge Of Tax Cut Lies From The Left** by [IBD](#)
 - **U.S. Doesn't Deserve A "AAA" Rating** by [Marc Joffe via Fiscal Times](#)
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Markets

- **A Decade Of Central Bank Collusion** by [Nomi Prins via NomiPrins.com](#)
- **October 12th, The Day Of The Equity Crash** by [Bill Blain via Zero Hedge](#)
- **Earnings Not Impressing Traders** by [Joe Ciolli via BI](#)
- **Real Estate Investors, Meet Your New Masters** by [John Coumarianos via MarketWatch](#)
- **Put These Charts On Your Wall** by [Charlie Biello via Pension Partners](#)
- **Money Moving Fast Into EM Stocks** by [Michael Kahn via Barron's](#)
- **Why You Should Consider Fortier Markets** by [Simon Constable via US News](#)
- **What Wall Street's Most Bullish Strategist Is Saying** by [Myles Udland via Yahoo Finance](#)
- **Stocks Are Fundamentally Sound** by [Ed Yardeni via Yardeni Research](#)

- **Last Time Americans Were This Fearless, Stocks Crashed** [by Tyler Durden via Zero Hedge](#)
 - **AMZN's Bull Market Could End** [by Doug Kass via Real Clear Markets](#)
 - **Gas Prices Spike As Refineries Shut Down** [by Mark DeCambre via MarketWatch](#)
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Research•/ Interesting•Reads

- **Fed Study Confirms Phillips Curve Is Useless** [by Mike Shedlock via MishTalk](#)
 - **Crowded Trades & The Next Quant Meltdown** [by Michelle Celarier via Institutional Investor](#)
 - **Worst Case Scenario For Passive Investing (Pt 1)** [by Stephen Gandel via BloombergGadfly](#)
 - **Worst Case Scenario For Passive Investing (Pt 2)** [by Stephen Gandel via BloombergGadfly](#)
 - **Sex Lives Collide When Millennials Move Back Home** [by Desiree Cooper via MarketWatch](#)
 - **World's 10-Most Valuable Sports Franchises** [by Steven Kurz via MarketWatch](#)
 - **A Dozen Attributes Of A Scalable Business** [by 25iq](#)
 - **"Game of Thrones" - A Story Of A Debt Crisis** [by Adam Epstein via Quartz](#)
 - **Electric Vehicle Goals Ignore Scientific Facts** [by Steve Pociask via Forbes](#)
 - **Investing Is A Fascinating Business** [by Morgan Housel via Motley Fool](#)
 - **Facebook Faces A Demographic Time Bomb** [by Tyler Durden via ZeroHedge](#)
 - **The Conceit Of Central Bankers** [by John Hussman via Hussman Funds](#)
 - **The ABCs Of Trendlines...** [by Dana Lyons via Tumblr](#)
 - **The Great Equity-For-Debt Swap** [by Jesse Felder via The Felder Report](#)
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?Never forget, things change.? - Lowell Miller

Questions, comments, suggestions ? please [email me](#).