

Animal Spirits and the Economic Outlook

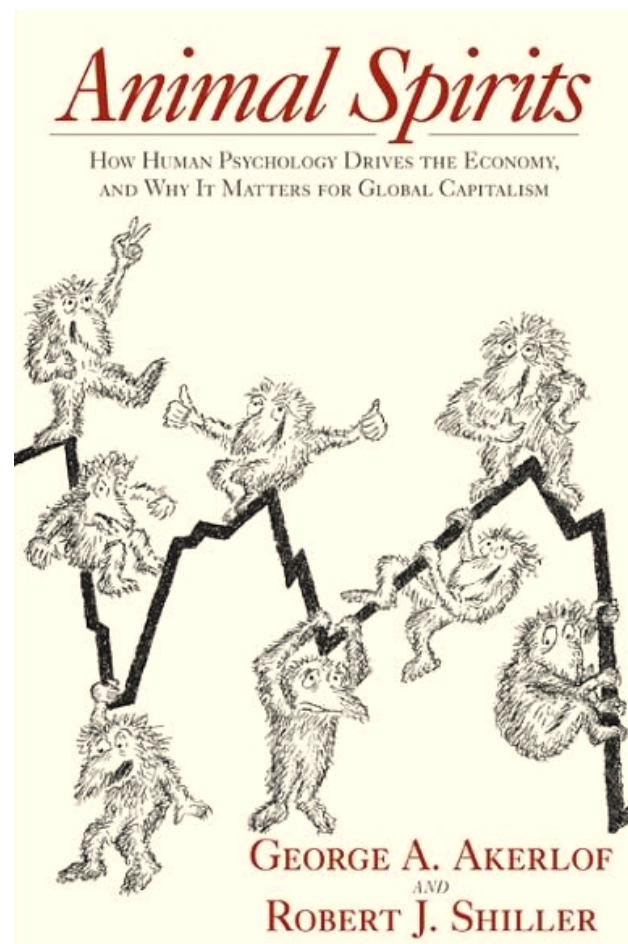
Prof. Robert Shiller, Yale University

National Economists Club

Washington DC, May 6, 2010

Animal Spirits after a Bubble

- Keynes' concept of animal spirits as a driving force for an economy
- Post bubble economy may involve too many uncertainties for animal spirits to reassert themselves

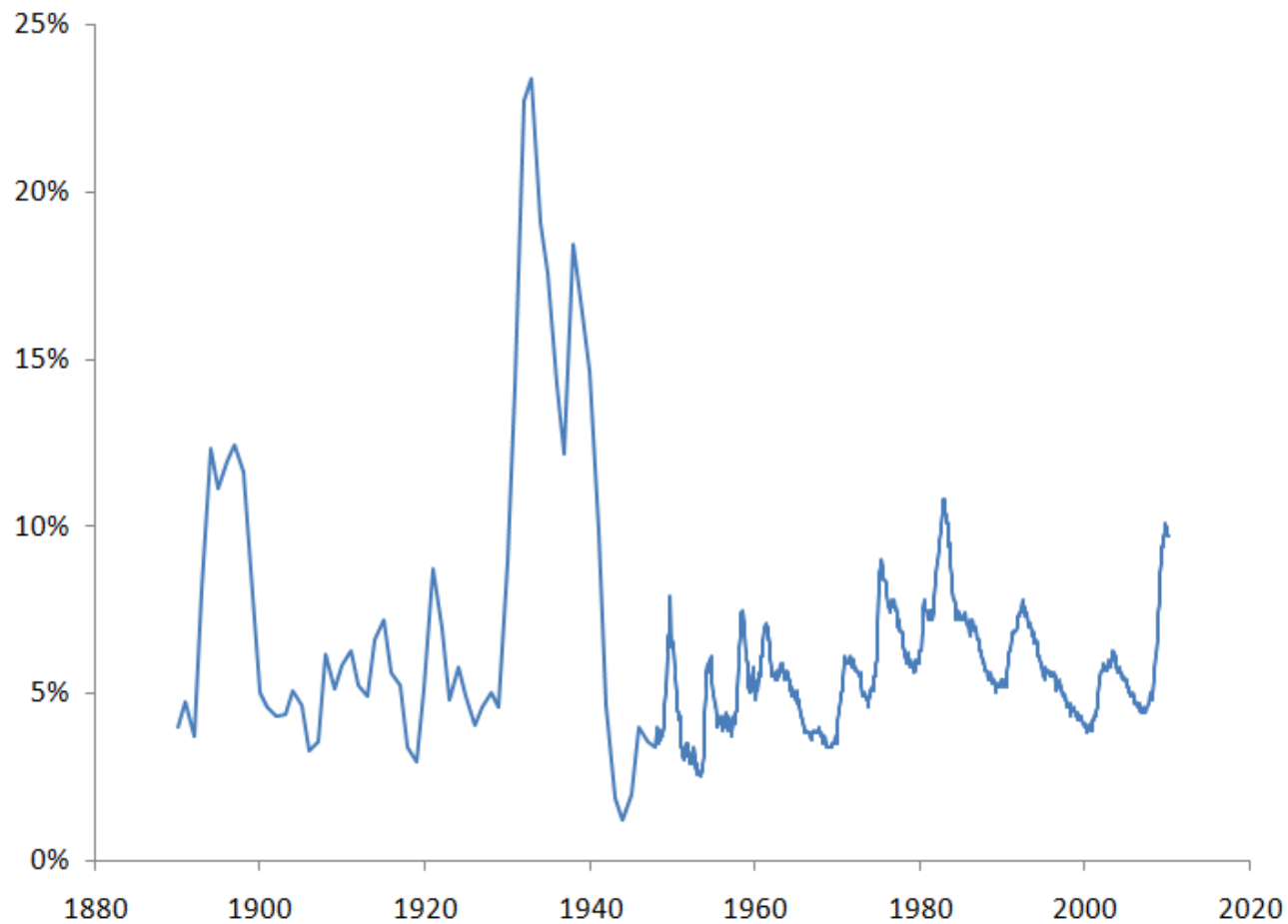


From John Maynard Keynes
*General Theory of Employment
Interest and Money, 1936*

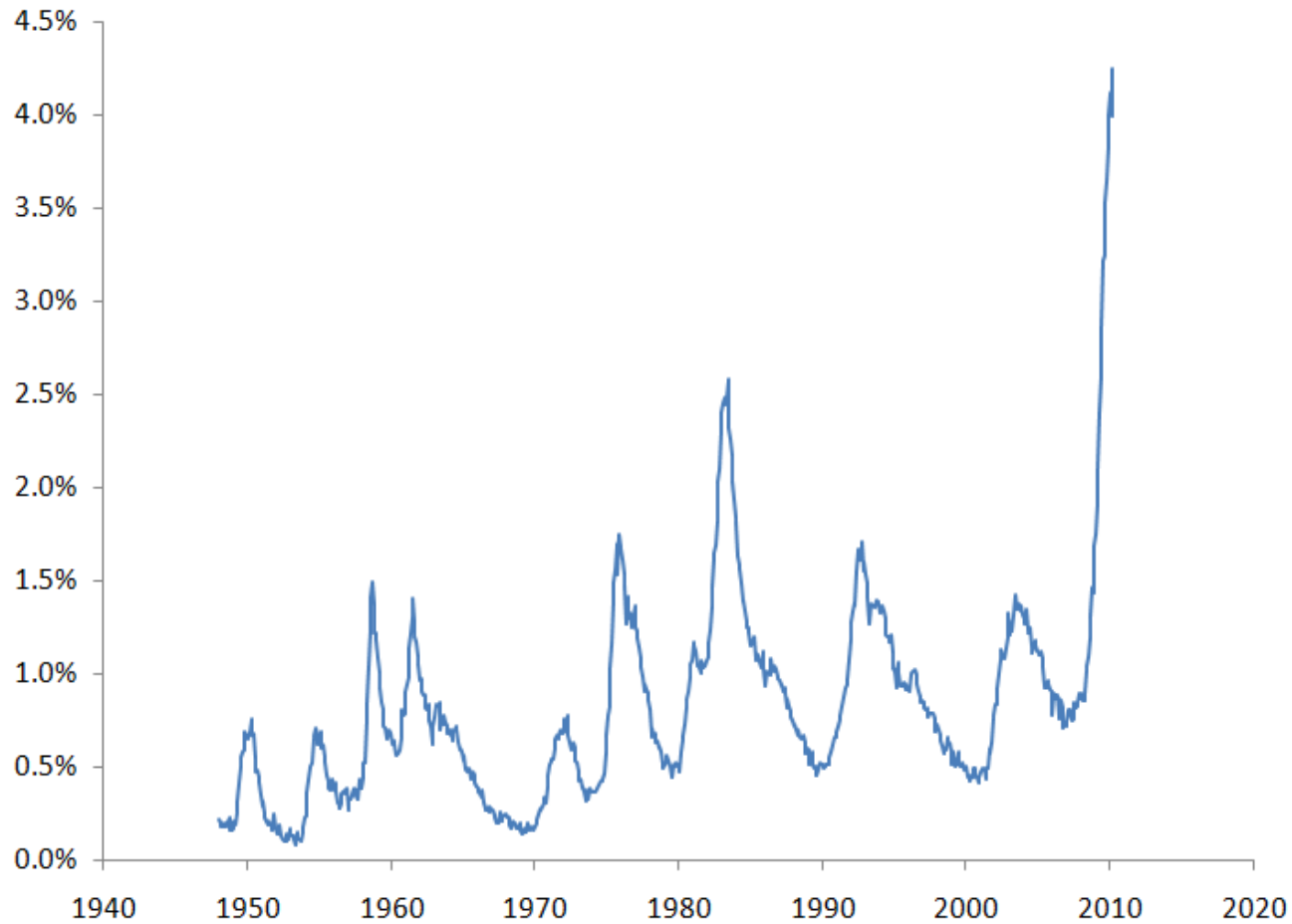
“The outstanding fact is the extreme precariousness of the basis of knowledge on which our estimates of prospective yield have to be made. . . . Most probably, of our decisions to do something positive, the full consequences of which will be drawn out over many days to come, can only be taken as a result of animal spirits—of a spontaneous urge to action rather than inaction . . .”

U.S. Unemployment Rate

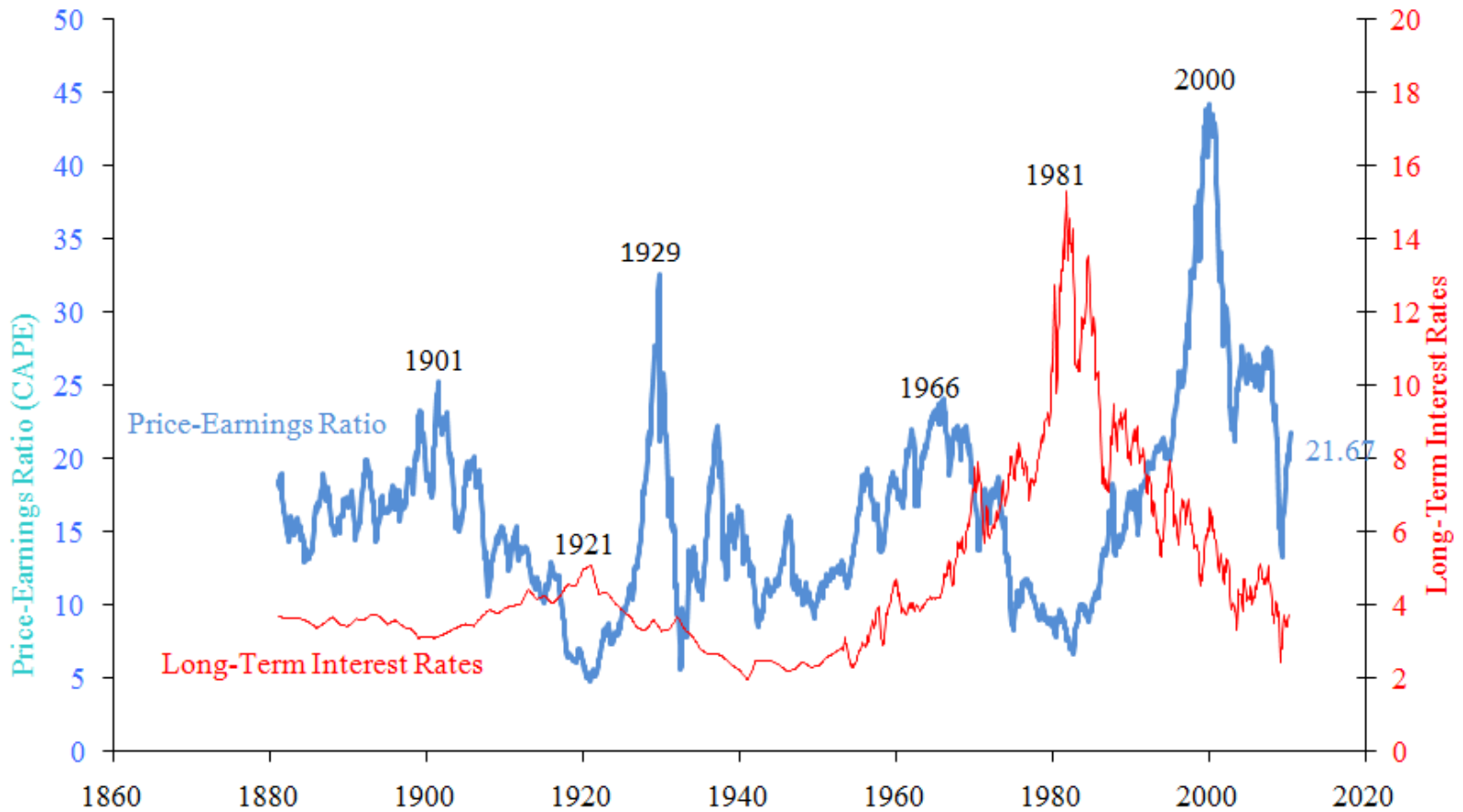
Annual 1890-1947 (Romer, BLS)
Monthly Jan 1948-March 2010



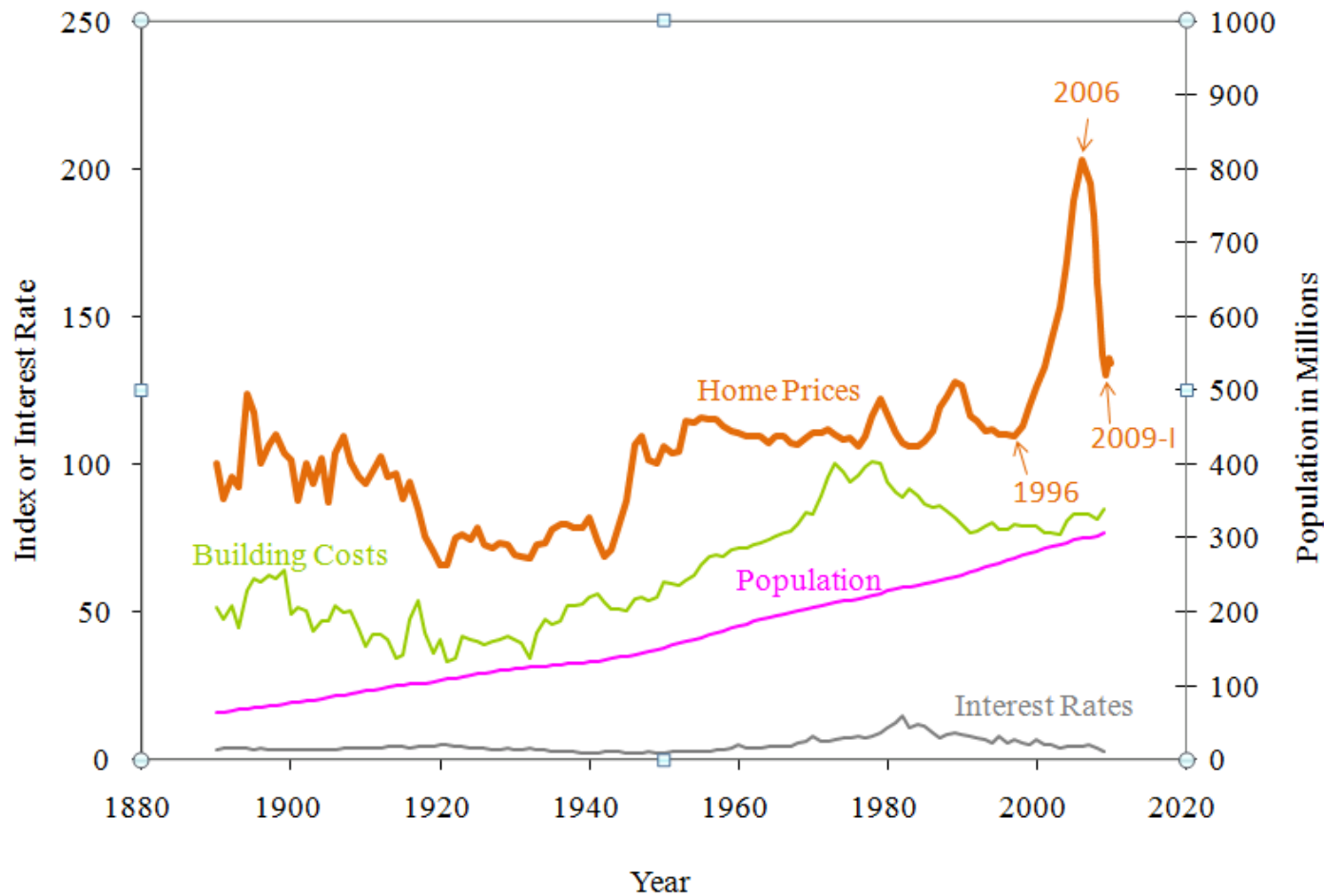
U.S. Unemployment Rate 27 Weeks and Over, Monthly Jan 1948 March 2010



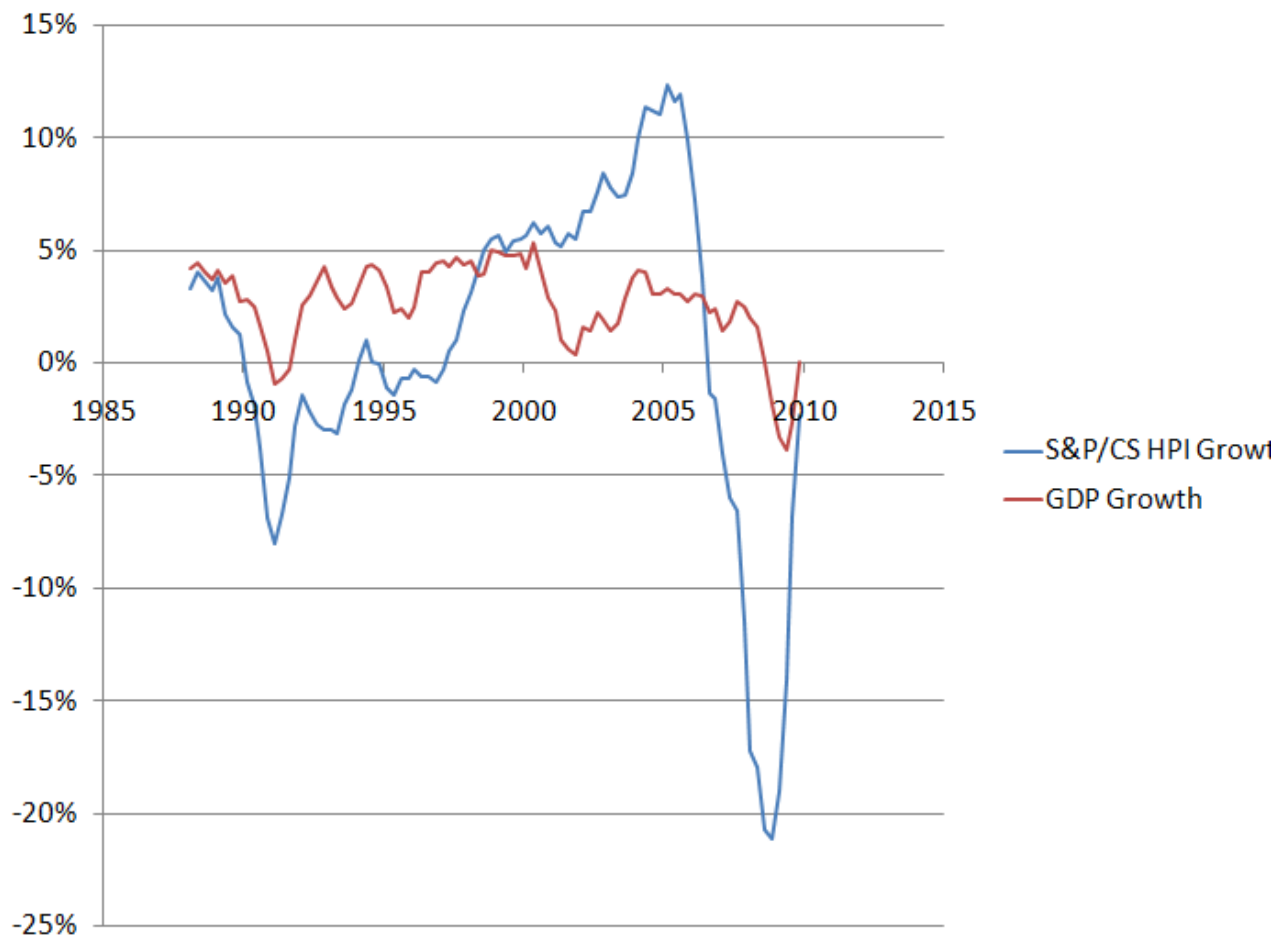
Cyclically Adjusted Price Earnings Ratio (P/E10) Monthly Jan 1881-May 2010 (Robertshiller.com)



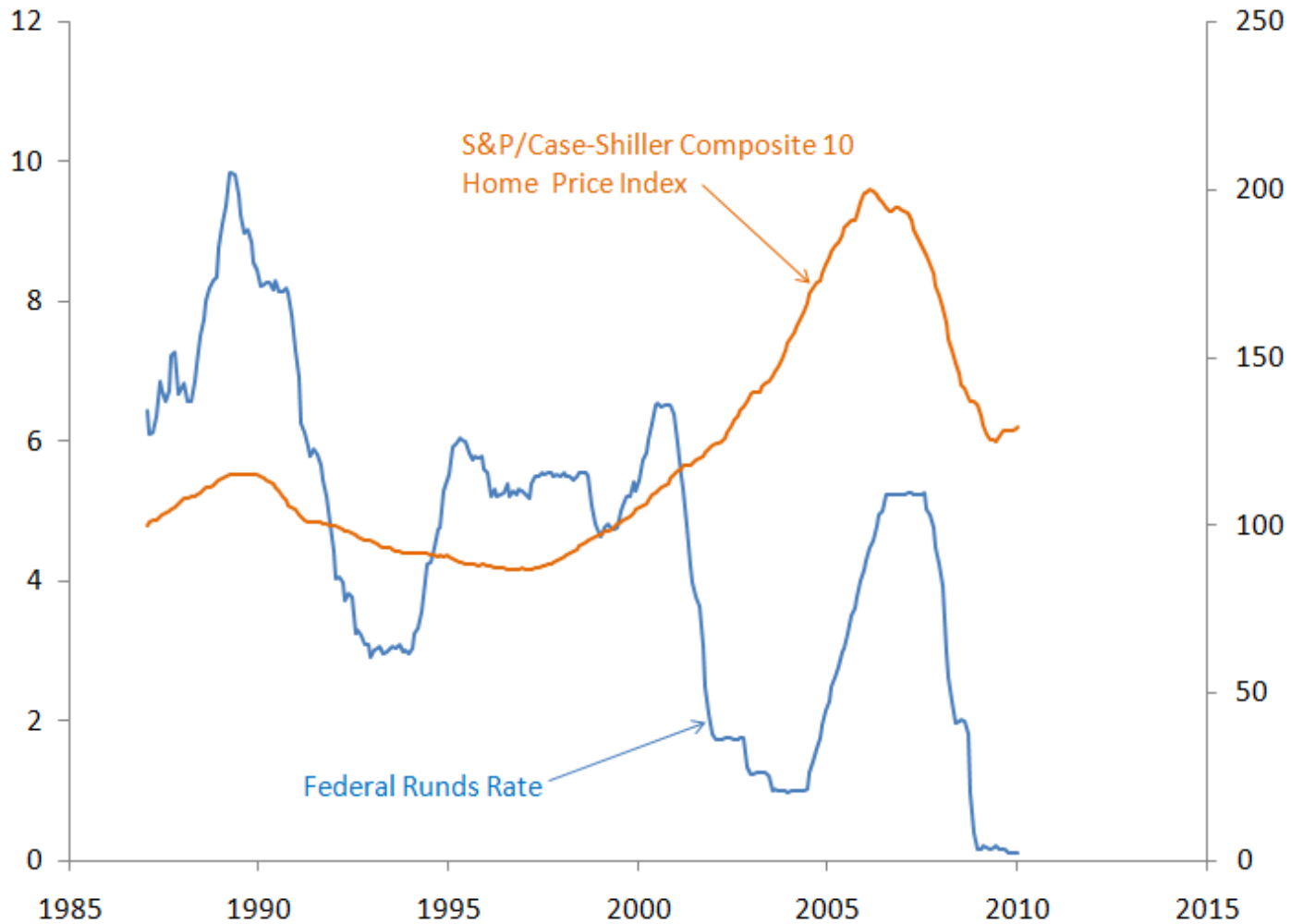
Real Home Prices, Building Costs, Population, Interest Rates 1890-2009-IV



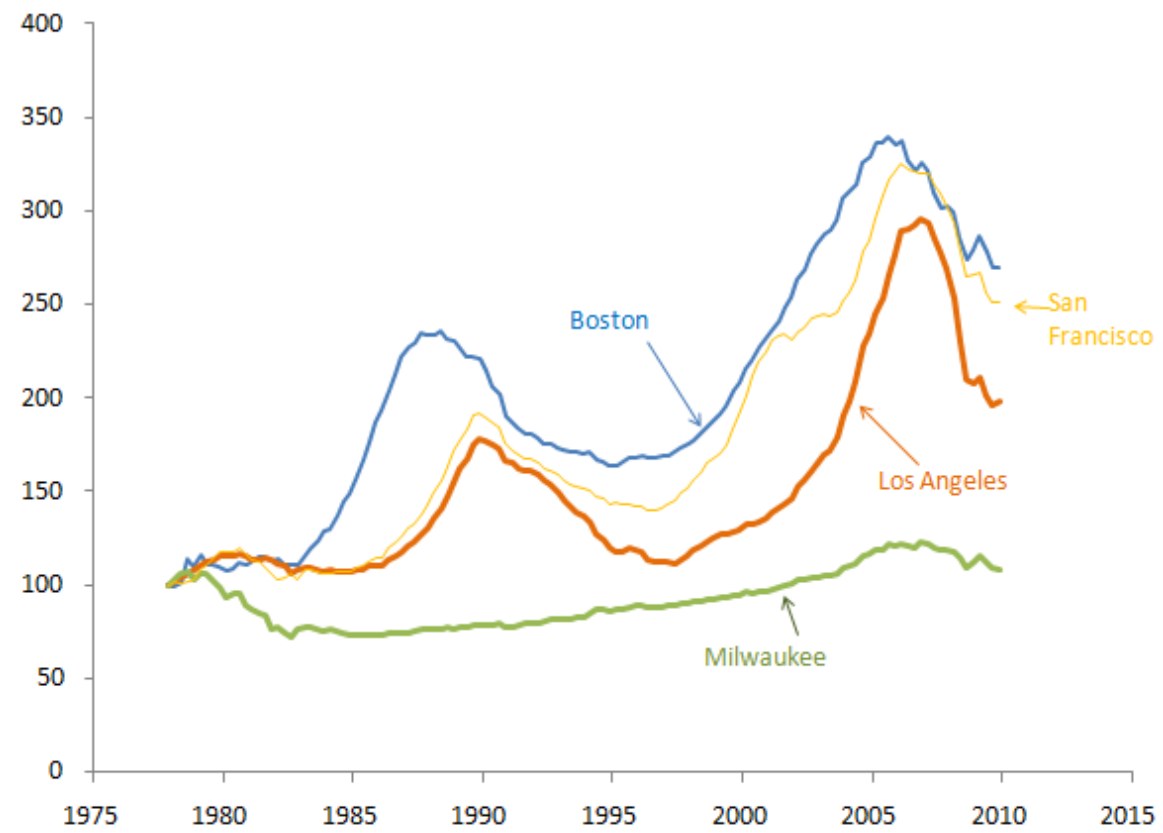
Home Prices and GDP 12-Month Growth Rates 1988-2009



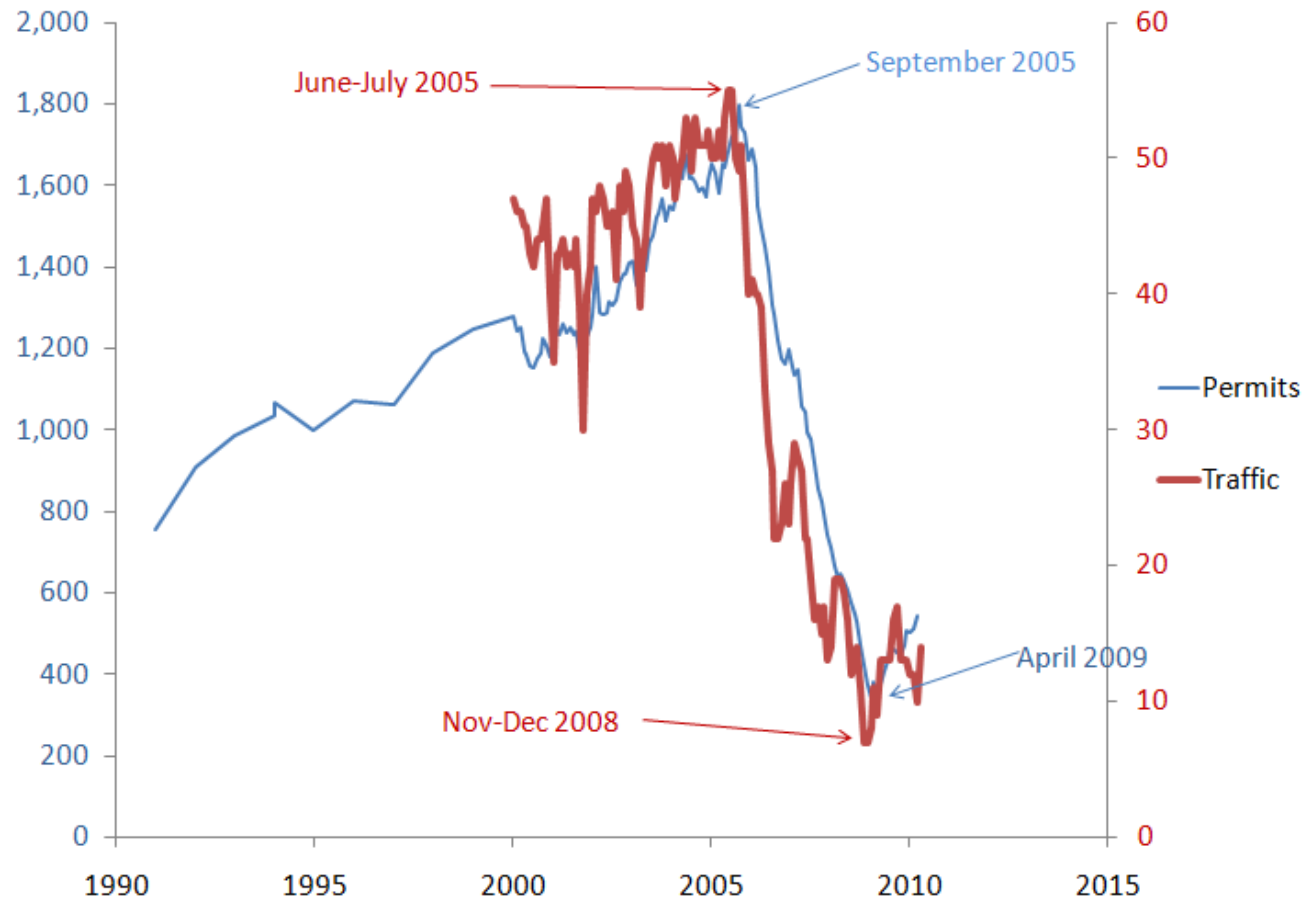
Real Home Prices and Federal Reserve Policy Rate Monthly Jan 1987-Jan2010



Real Home Prices in Boom Cities (Boston, Los Angeles, San Francisco) and Non-Boom City Milwaukee FHFA NSA 1977 IV – 2009 IV 1977=100

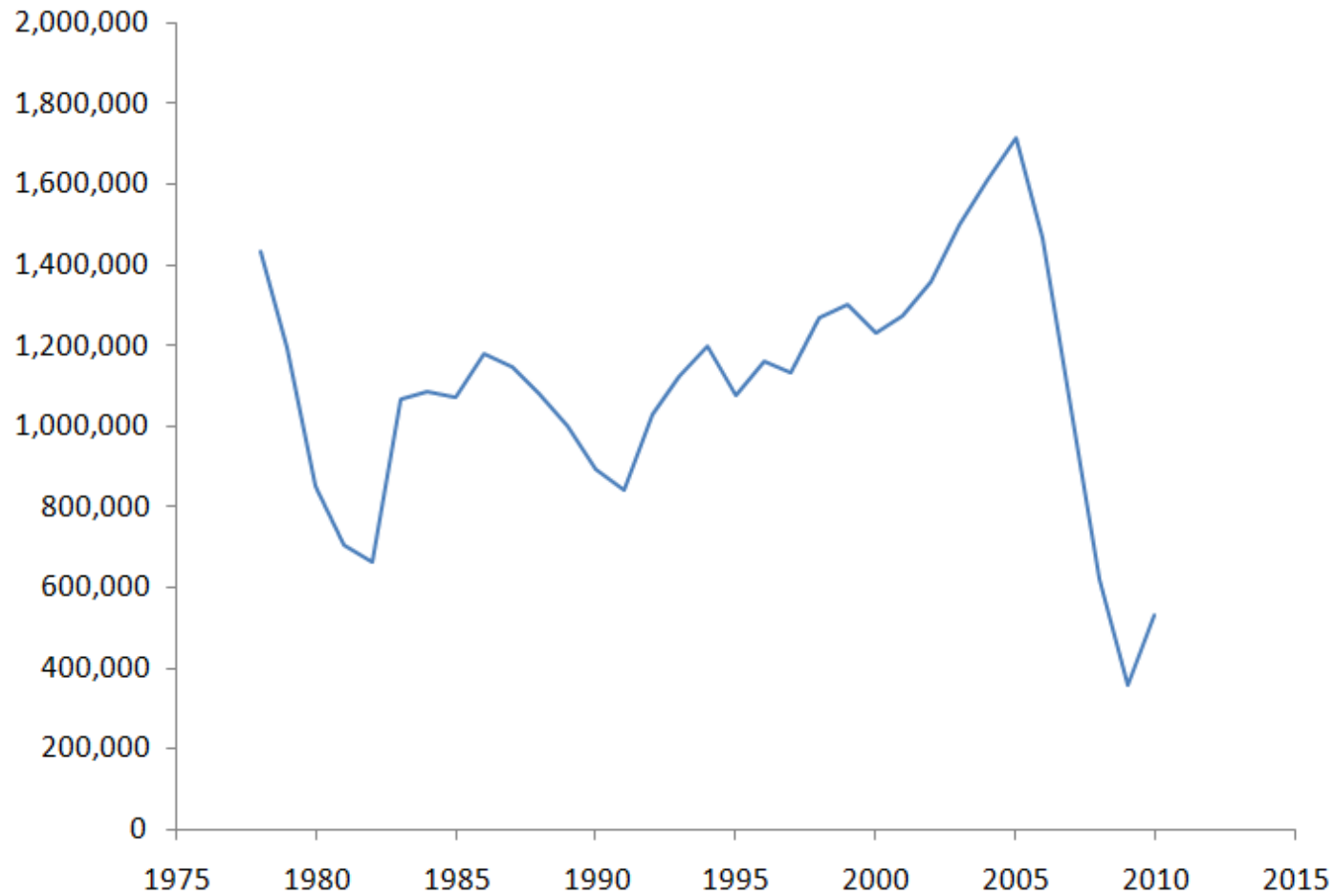


Permits (1-Unit) and NAHB Traffic of Prospective Home Buyers

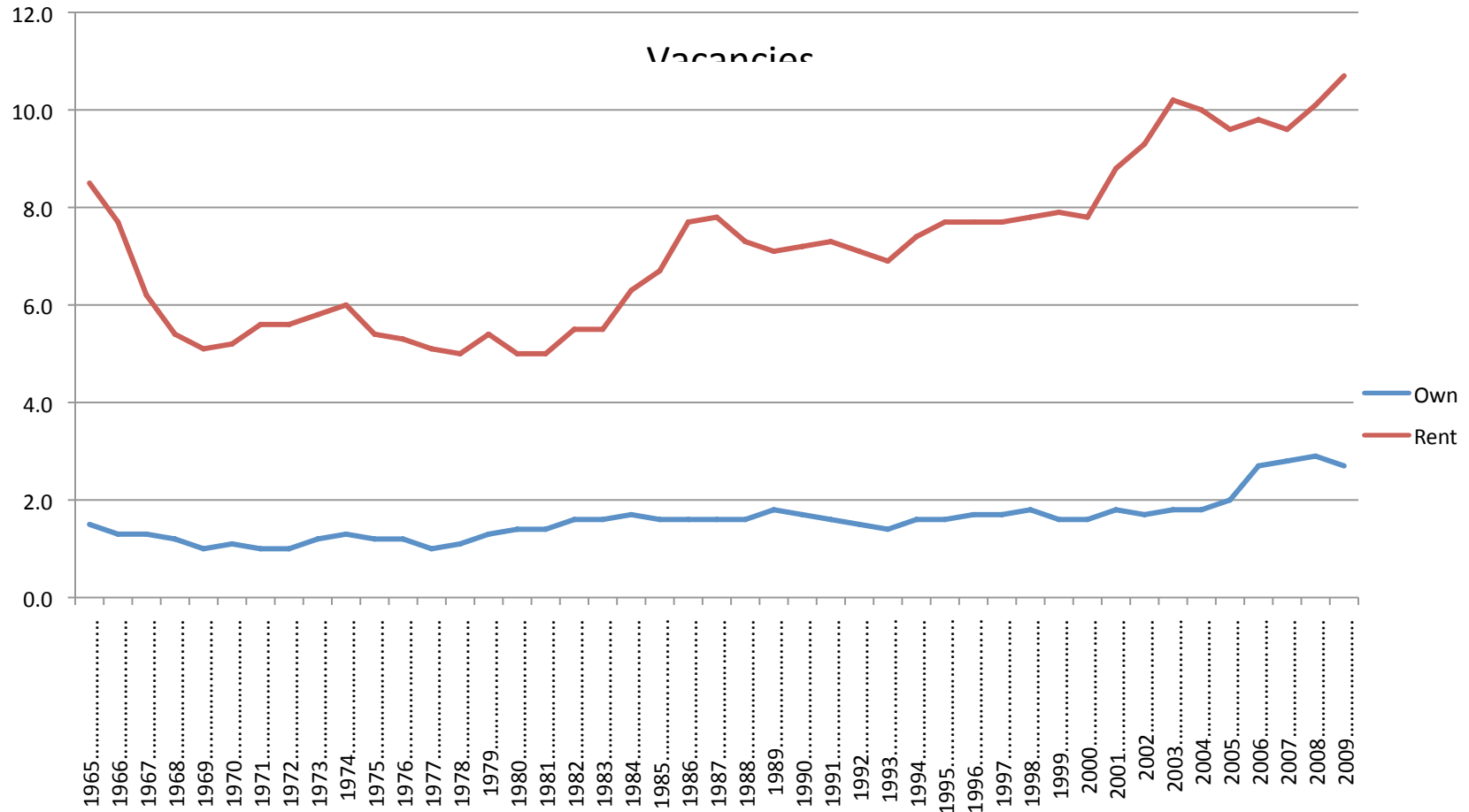


Housing Starts 1978-2010

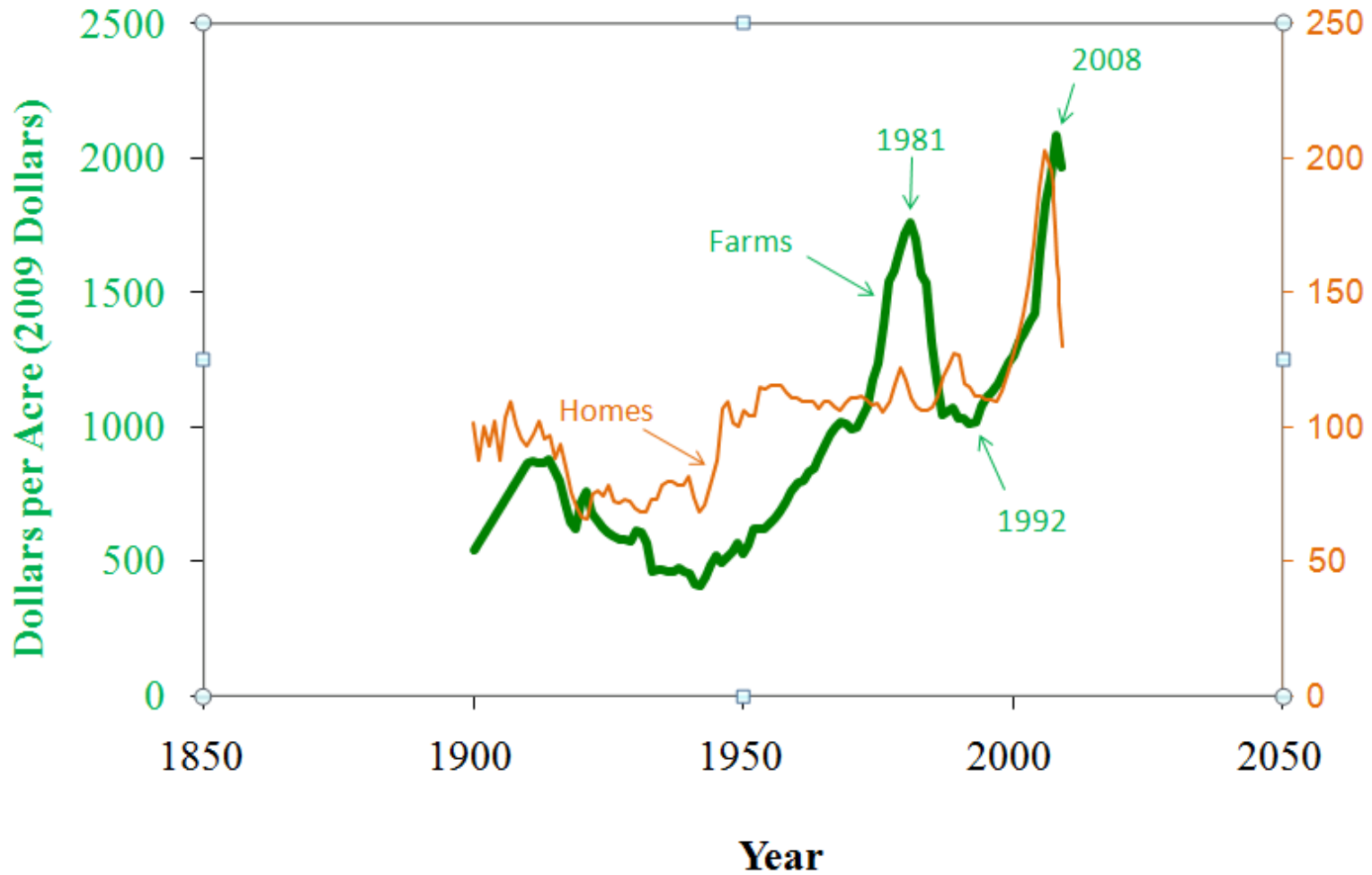
Single Family Housing Starts 1978-2010



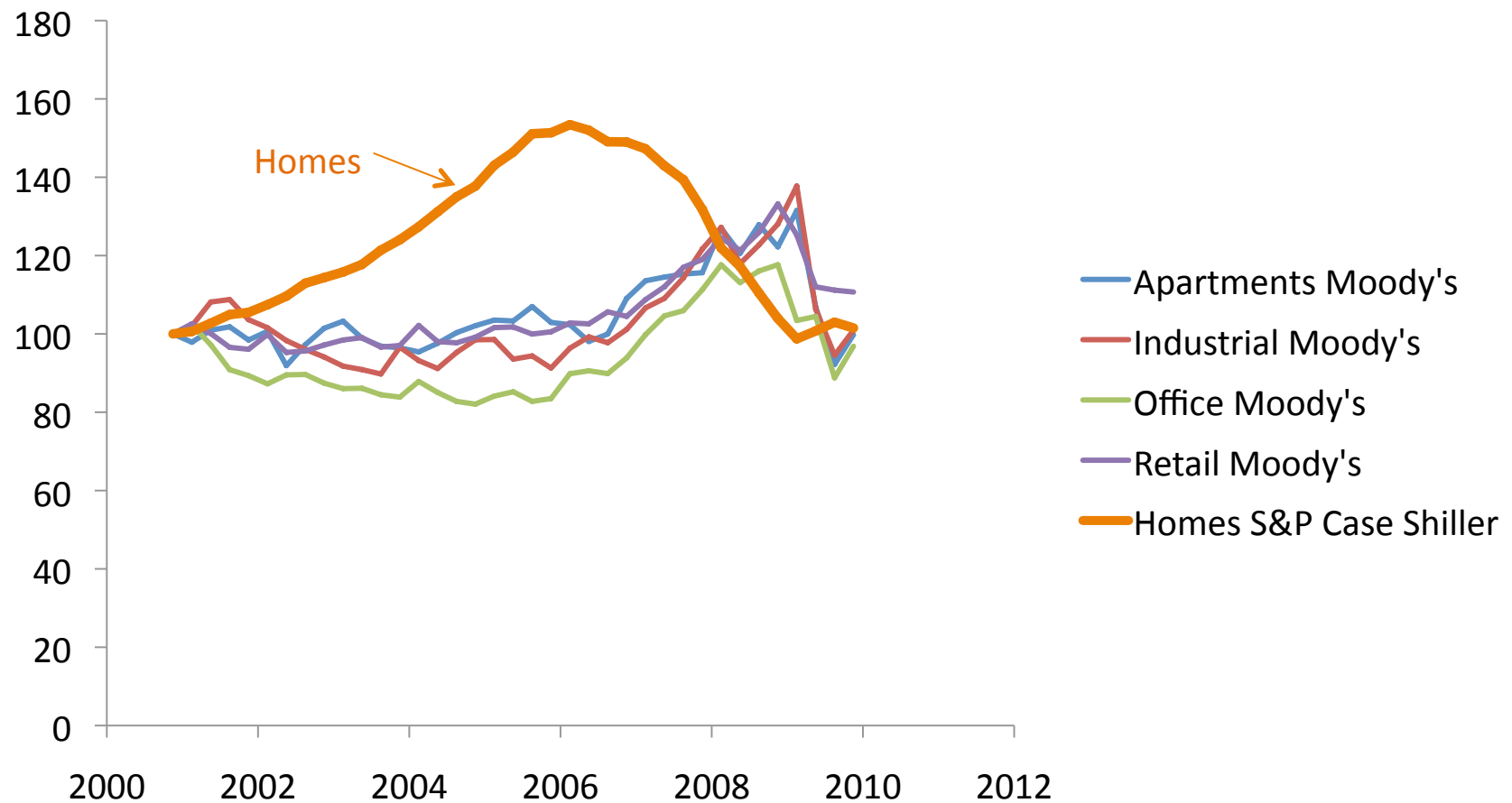
Vacancies 1965-2009



Homes (S&P/Case Shiller) and Farms (USDA) Real Prices 1900-2009



Real Commercial Real Estate Prices (Moody's CRE) and Real Home Prices (S&P/C-S) 2000-IV-2009-IV

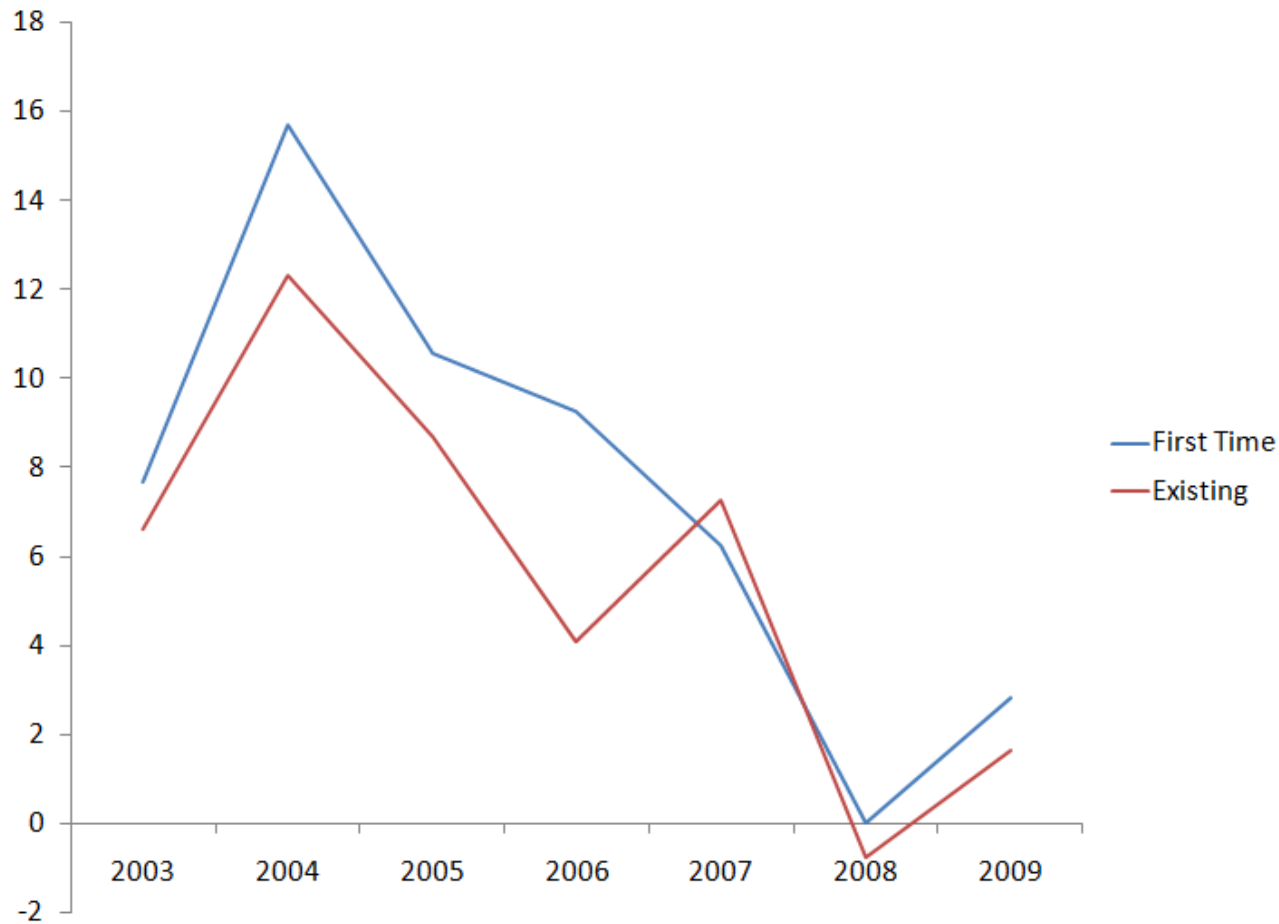


Case & Shiller Home Buyers Surveys

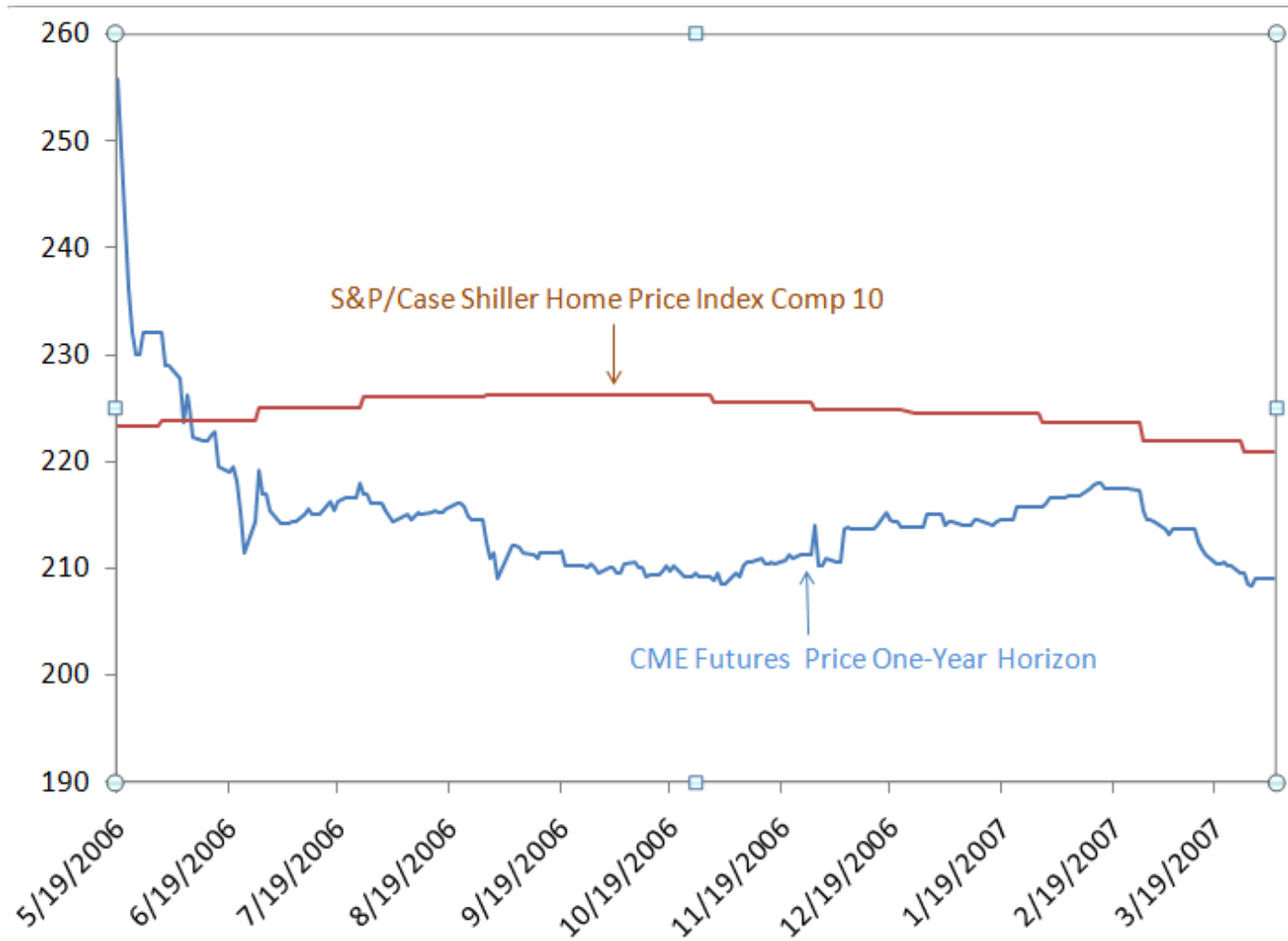
- 500 Identical questionnaires sent each spring to home buyers that year each of four cities (2000 total)
- Boston, Los Angeles (Orange County), Milwaukee, San Francisco (Anaheim County)
- Annually, 1988, 2003-2010
- In-depth questioning about purchase and sales (for those who also sold a home) decision

6. How much of a change do you expect there to be in the value of your home over the next 12 months?

_____ % (Percent Change) 1. INCREASE 2. DECREASE

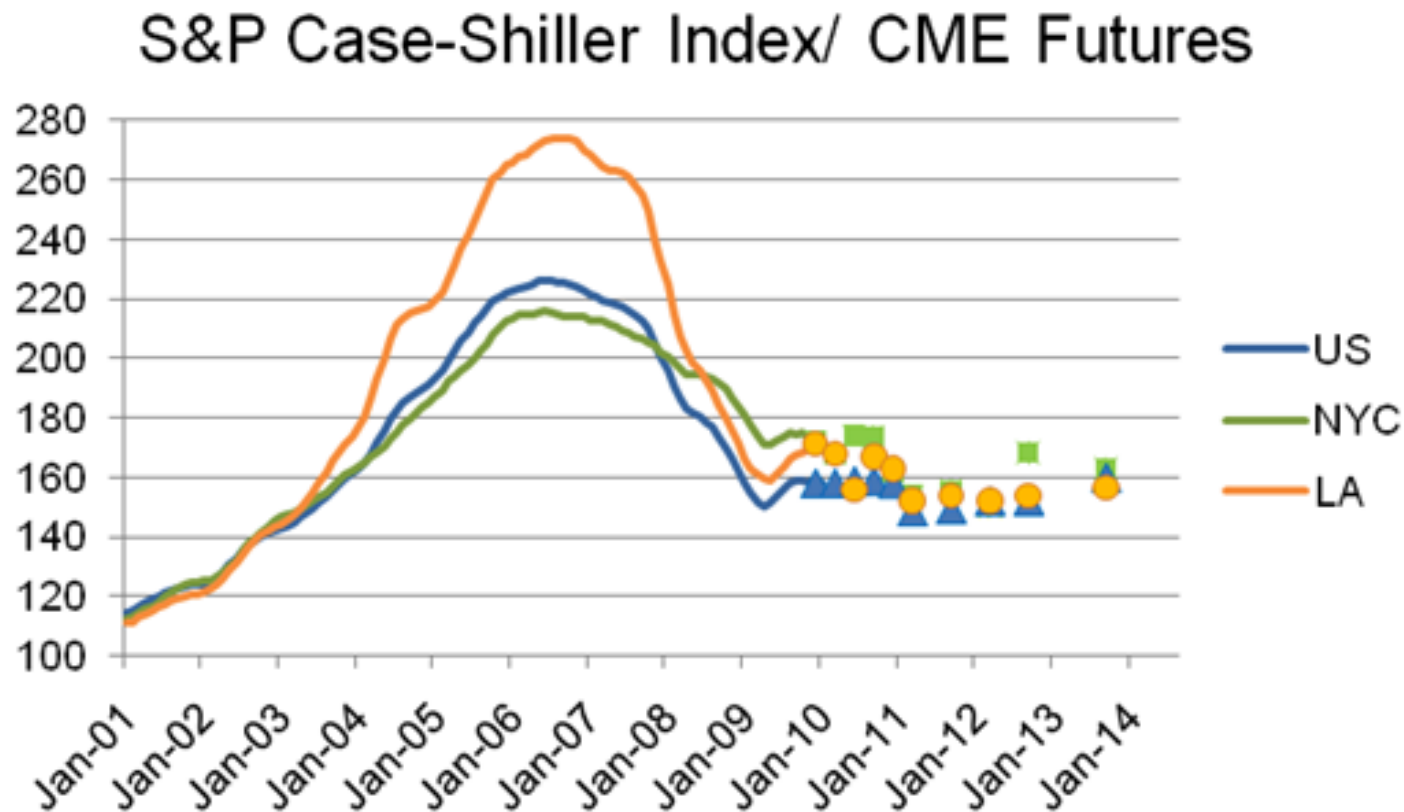


One-Year Futures Prices with Spot Prices, CME 2006-7



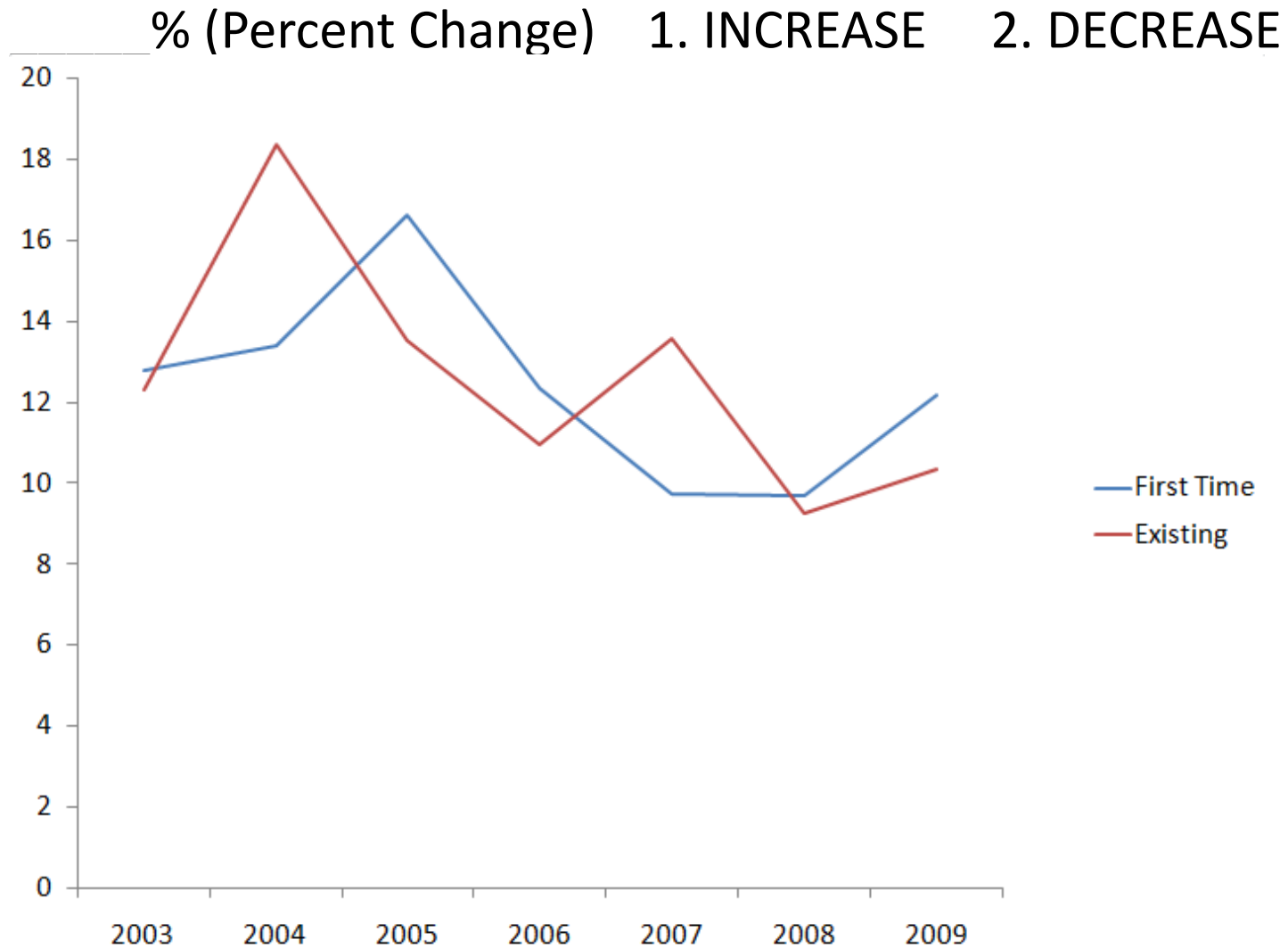
From www.homepricefutures.com

April, 2010

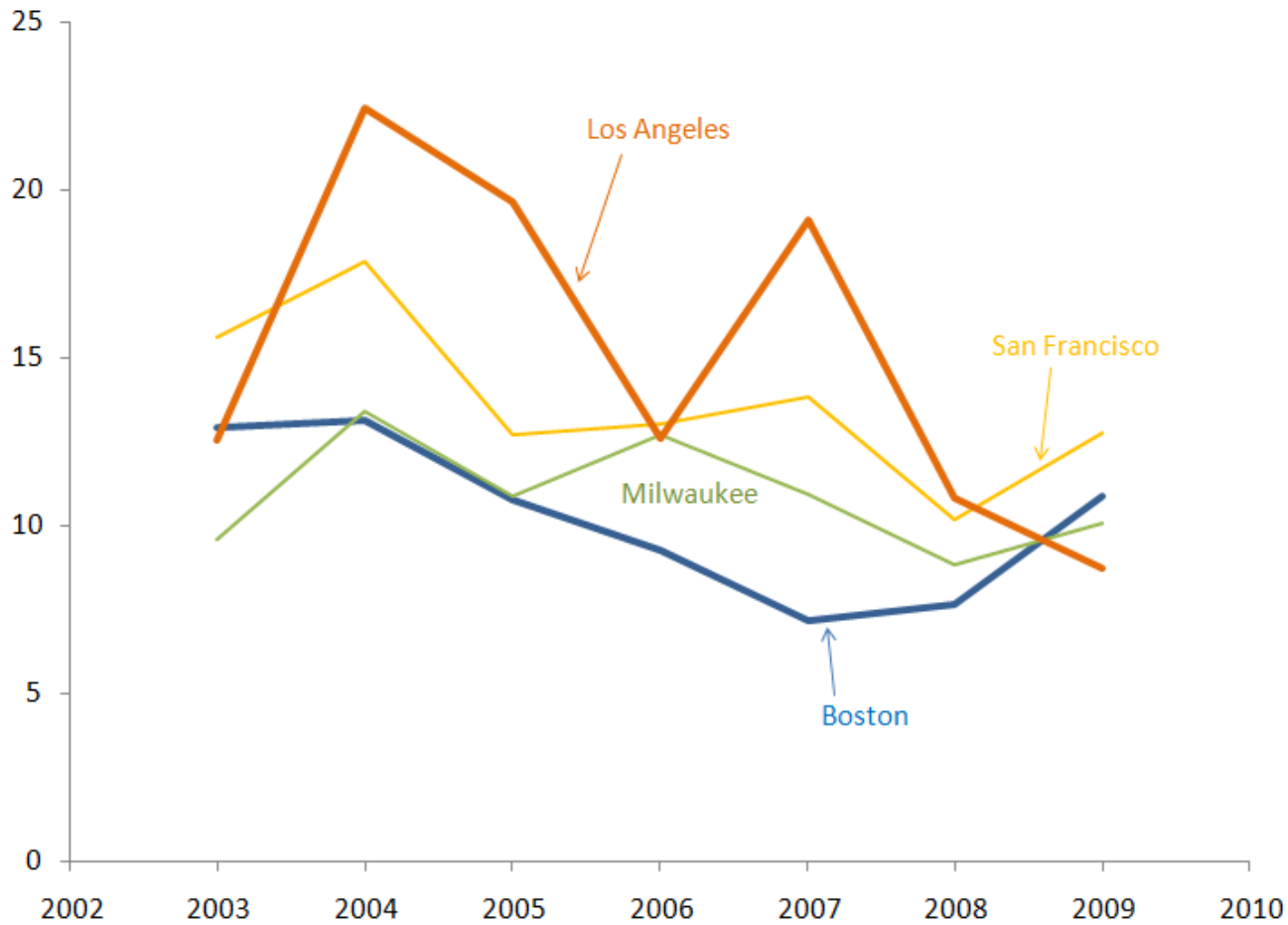


a/o 4/1/10

7. On average over the next ten years how much do you expect the value of your property to change each year?



Comparison across Cities of Average 10-Year Expected Appreciation

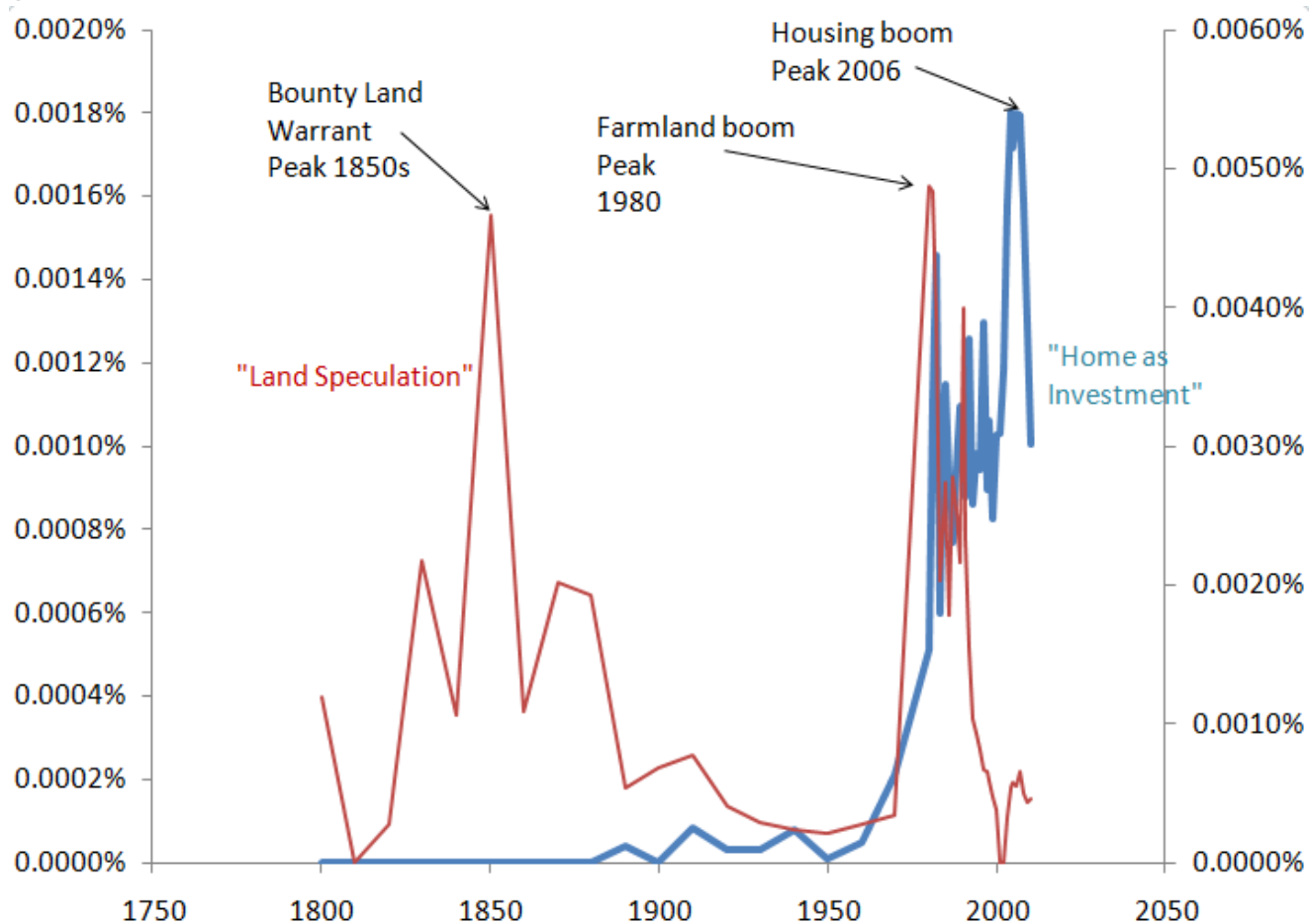


13. In deciding to buy your property, did you think of the purchase as an investment:

1. Not at all 2. In part 3. It was a major consideration



Estimated Percent of News Articles with Words “Home as Investment” and “Land Speculation” By Decade 1800-1970, Annual 1980-2010



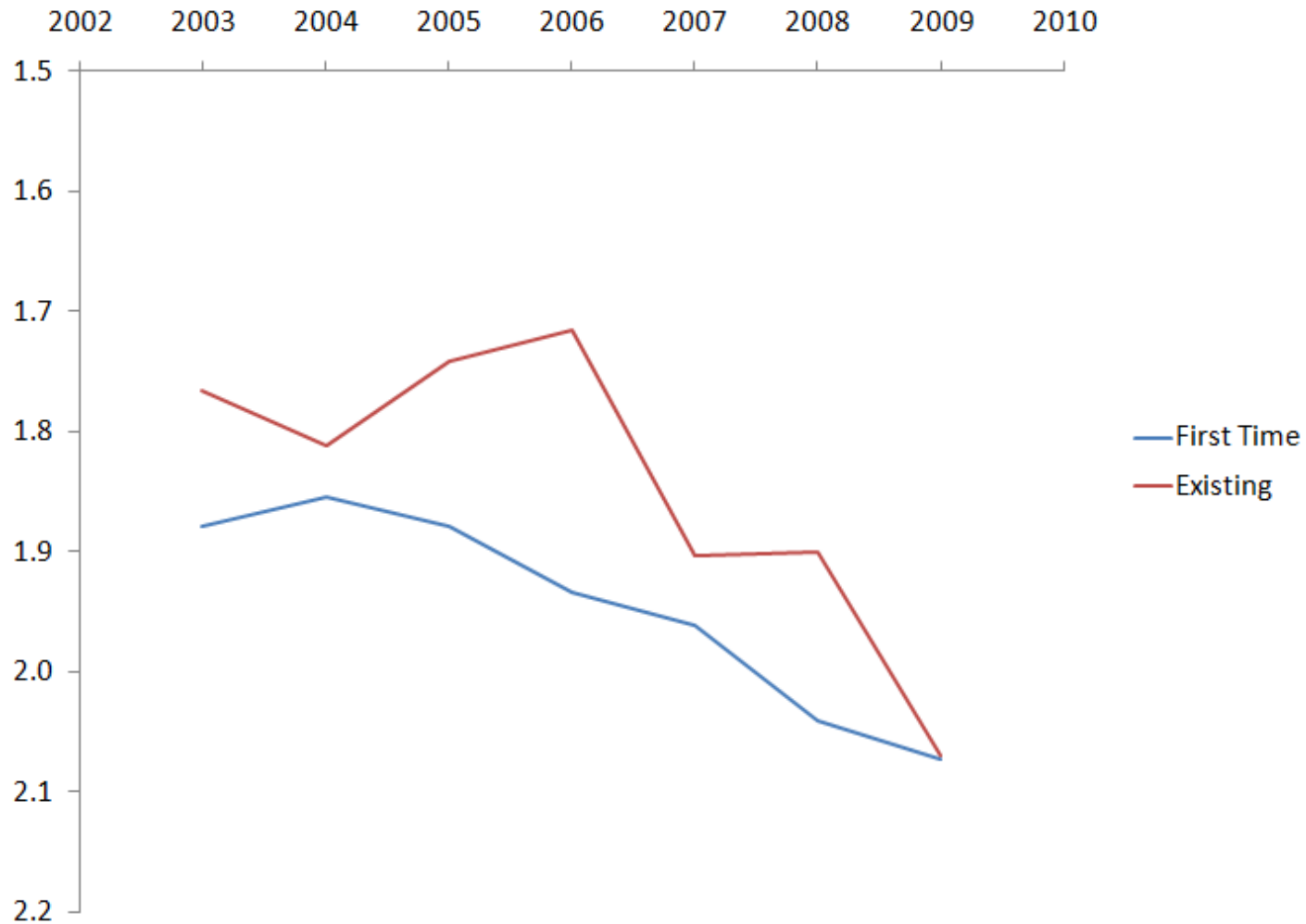
Real Estate as Best Investment

28. Do you agree with the following statement: "Real estate is the best investment for long-term holders, who can just buy and hold through the ups and downs of the market."

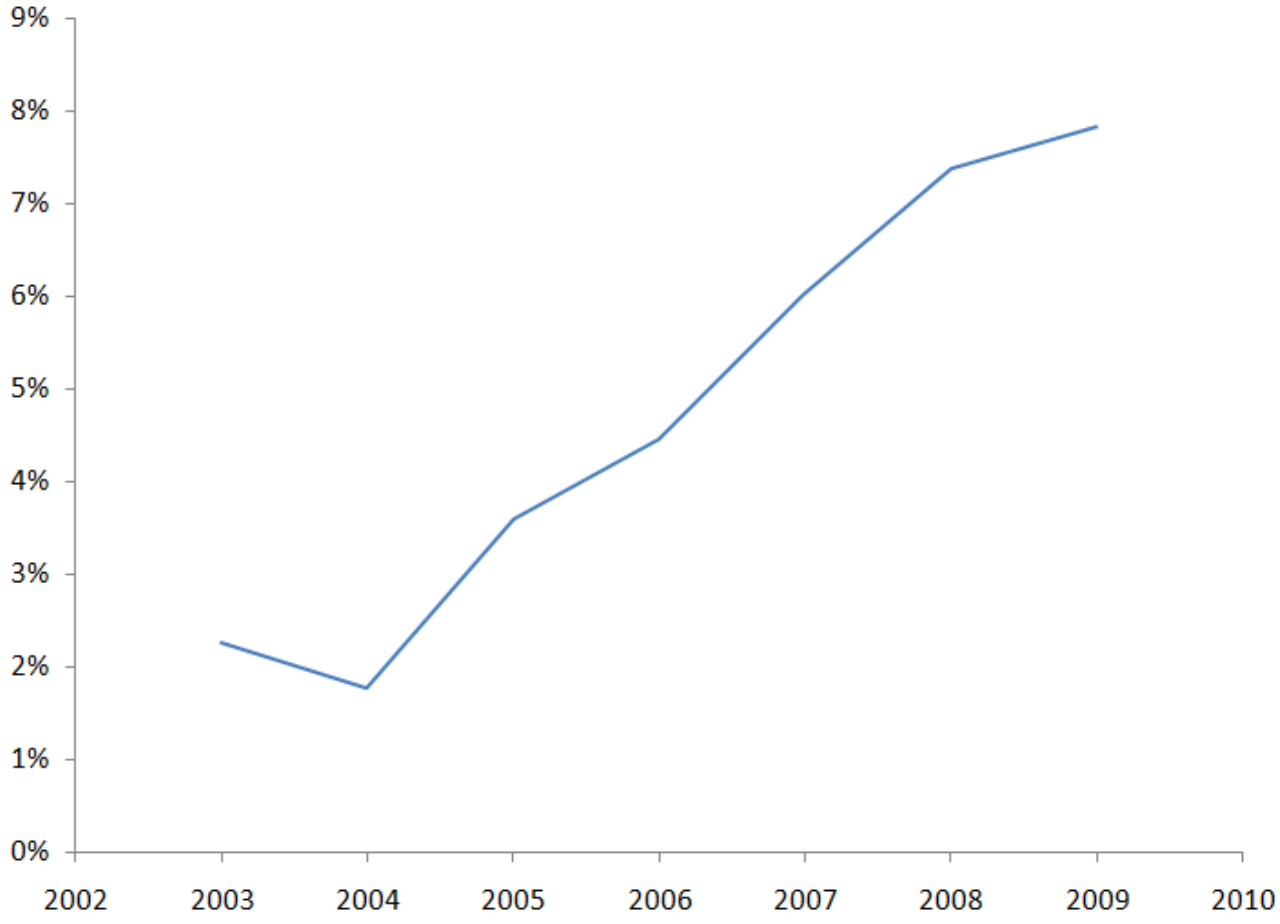
[Please circle one number on scale from 1 to 5]

Strongly Agree Agree Somewhat Neutral Disagree Somewhat Strongly Disagree

1

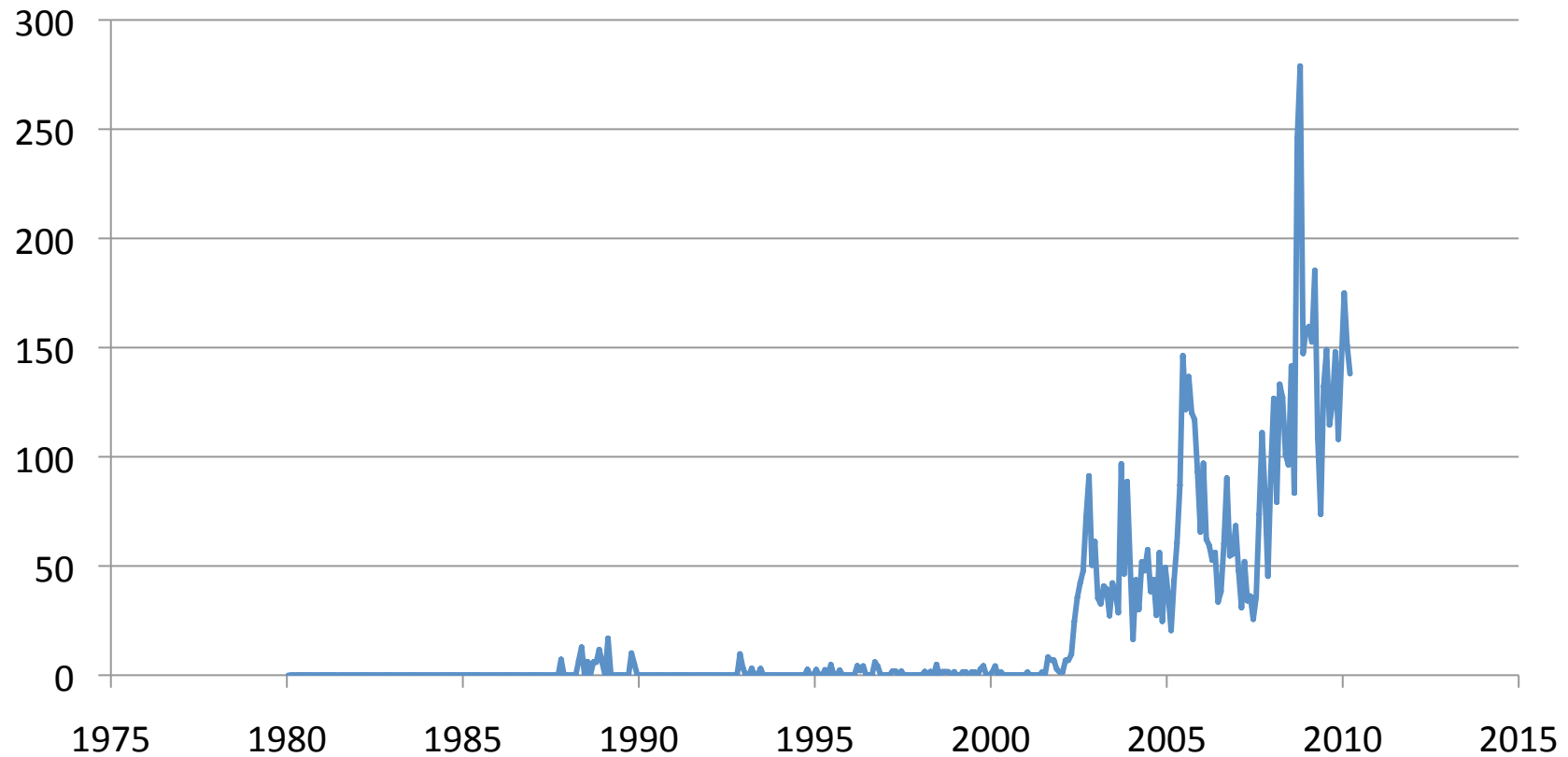


Count of Instances Respondent Volunteered Word “bubble” as % of Total Questionnaires Returned



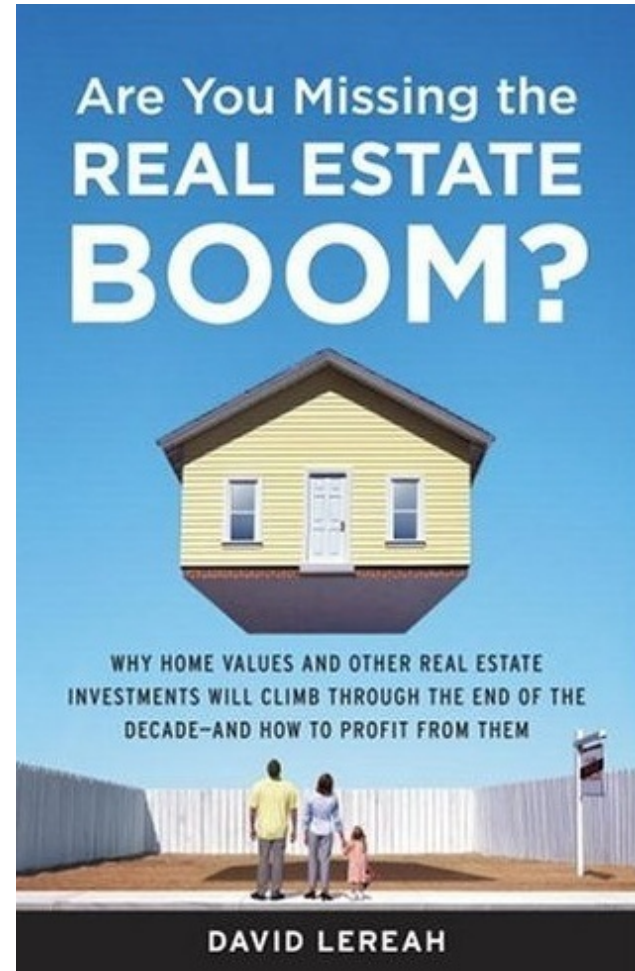
Scaled Lexis Nexis News Word Count for “Housing Bubble” Monthly Jan 1980-Mar 2010

Housing Bubble



David Lereah, March 2005

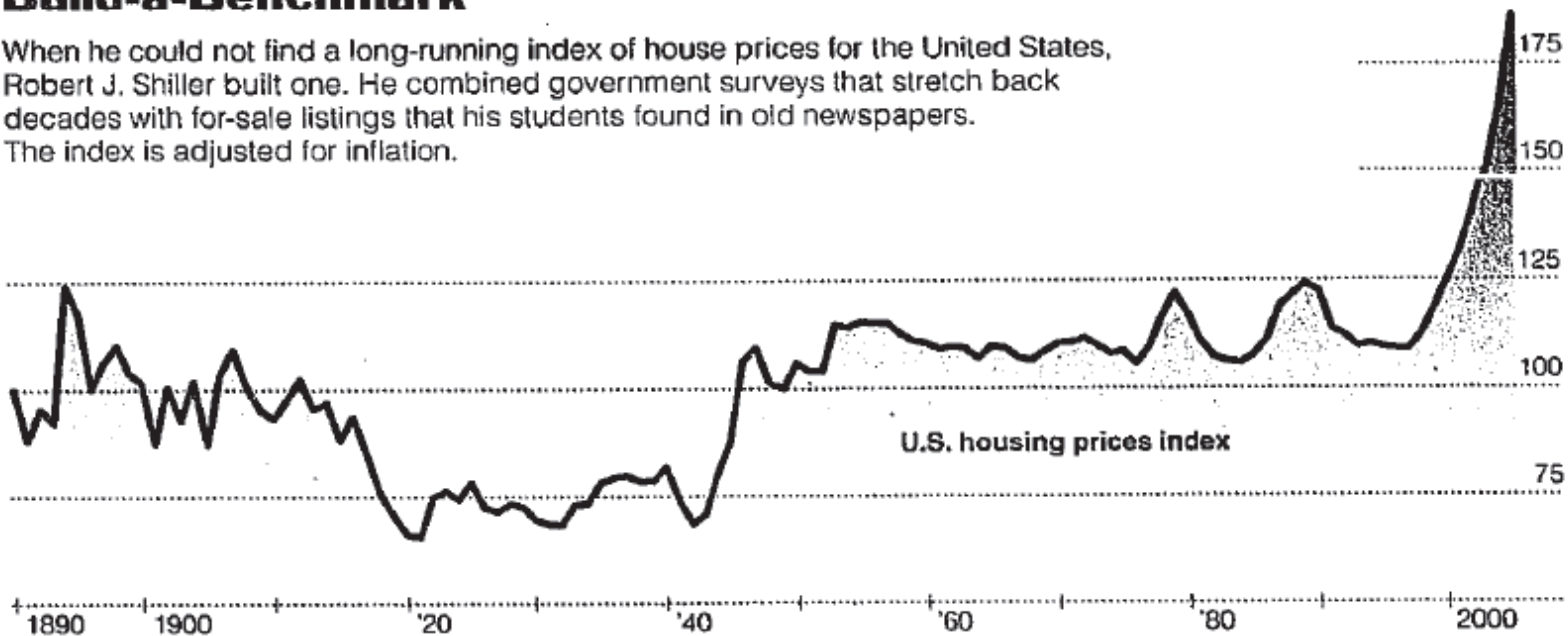
- Hostile reviews:
- **Better title - "Join the Greater Fools of America Club"**, April 19, 2005
- “Can the author do time?”
- “Has this guy changed his name yet?”



NYTimes David Leonhardt, August 21, 2005, P. B1

Build-a-Benchmark

When he could not find a long-running index of house prices for the United States, Robert J. Shiller built one. He combined government surveys that stretch back decades with for-sale listings that his students found in old newspapers. The index is adjusted for inflation.



Source: "Irrational Exuberance," Robert J. Shiller

The New York Times

Post Bubble Psychology and Economic Weakness

- Lamont Dupont, 1938: “there is uncertainty about the future burden of taxation, the cost of labor, the spending policies of the Government, the legal restrictions applicable to industry—all matters affecting computations of profit and loss. It is this uncertainty rather than any deep-seated antagonism to governmental policies that explains the momentary paralysis of industry. It is that which causes some people to question whether the recuperative powers of industry will work as effectively to bring recovery from the current depression as they have heretofore.”

Conclusions

Changes in animal spirits driven by social and media events that create new world view, new vocabulary, symbols

2006 peak in home prices occurred when diffusion of “bubble” idea had proceeded far enough (and with supply response coming online and Fed concern about bubbles causing a tightening)

Double dips are rare by historical standards but the bubble aftermath suggests possible weakness ahead