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Big Picture Charts

***e*Research Corporation** is pleased to provide an article by Scott Grannis for his Blog, "Calafia Beach Pundit".

In this article, Mr. Grannis provides some comforting charts about the U.S. economy, the stock market, and wealth.

The article is reproduced below, beginning on the next page, or you can go to this specific Blog at the following link: **Big Picture Charts**

You can also visit Scott Grannis' Home Page for his Blog at the link below:
http://scottgrannis.blogspot.ca/

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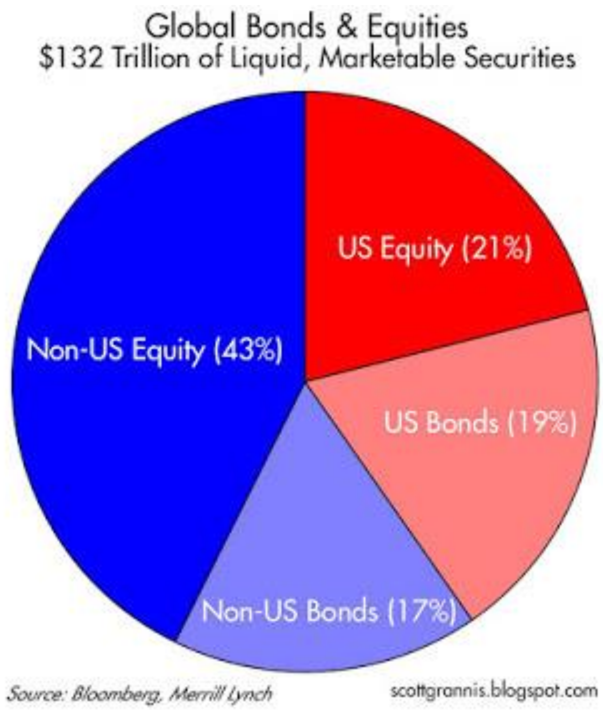
Big Picture Charts

The global economy and global financial markets are huge, but just how huge? Answer: a lot bigger than most people realize.

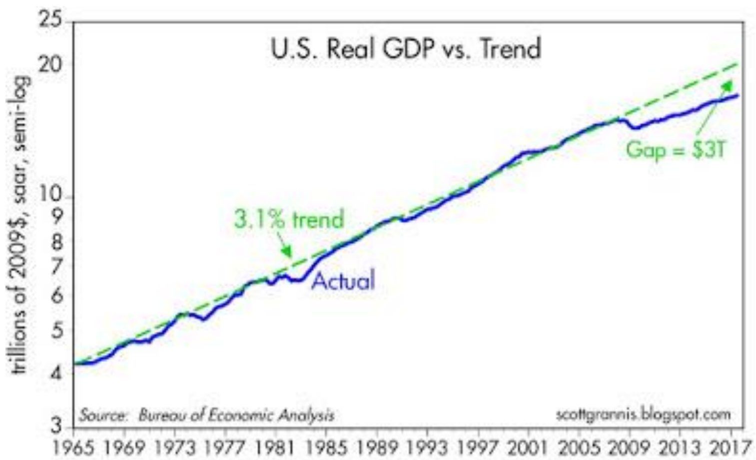
Here are some charts which help put things in perspective. They also show that what is going on today is not unprecedented nor extraordinary. As always, all the charts contain the most recent data available at the time of this post.



Global GDP is roughly $80 trillion, about four times the size of the U.S. economy. As the chart above shows, the global economy supports actively-traded bonds and stocks worth $132 trillion, of which about 40% are U.S.-based. There is nothing unusual about any of this, considering that a typical U.S. household has a net worth (stocks, bonds, savings accounts and real estate) equal to about three times its annual income.

As the charts below show, the market cap of non-U.S. equities has grown at a much faster rate than U.S. equities since 2004 (U.S. equities have grown at a 5.4% annualized rate, non-U.S. equities at a 8.9% annualized rate). U.S. equities are now worth about 50% of the value of non-U.S. equities, down from more than 80%. Non-U.S. equities have suffered somewhat, however, due to the dollar's 5% rise (on a trade-weighted basis) over the period of these charts, but that is relatively insignificant in the great scheme of things.

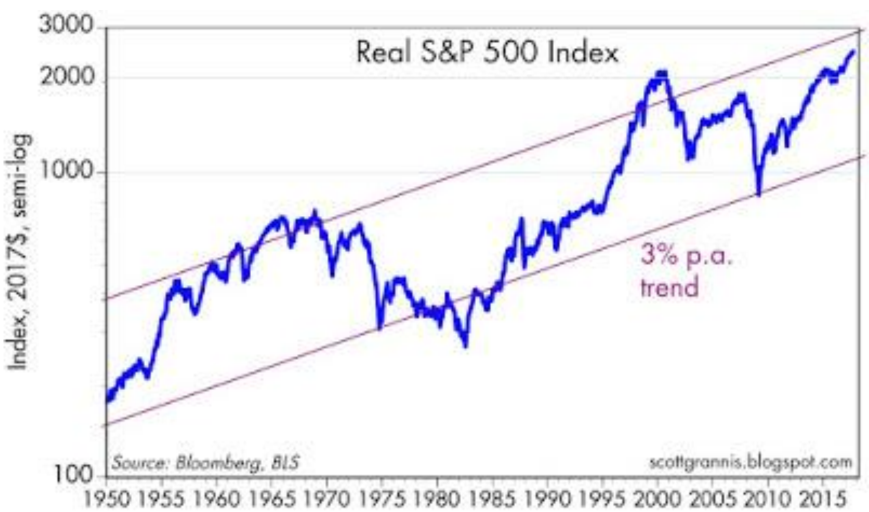
The defining characteristic of the current U.S. economic expansion is its meager 2.1% annualized rate of growth, which stands in sharp contrast, as the chart below shows, to its 3.1% annualized rate of growth trend from 1965 through 2007. If this shortfall in growth is due, as I have argued over the years, to misguided fiscal and monetary policies, then the U.S. economy has significant untapped growth potential and could possibly be $3 trillion larger today if policies were to become more growth-friendly.



As the next chart shows, the value of U.S. equities relative to GDP tends to fluctuate inversely to the level of interest rates. This is not surprising, since the market cap of a stock is theoretically equal to the discounted present value of its future earnings. Thus, higher interest rates should normally result in a reduced market cap relative to GDP, and vice versa. Since 10-yr Treasury yields—a widely respected benchmark for discounting future earnings streams—are currently at near-record lows, it is not surprising that stocks are near record highs relative to GDP. If the economy were $3 trillion larger, however, stocks at today's prices would be in the same range, relative to GDP, as they were in the late 1950s-1960s. Valuations are relatively high, to be sure, but not off the charts nor wildly unrealistic.

As the following chart suggests, over long periods the value of U.S. stocks tends to rise by about 6.5% per year (the long-term total return on stocks is a bit more due to annual dividends of 1-2%). The chart also suggests that the current level of stock prices is generally in line with historical trends.

Adjusting for inflation, we see that stock prices tend to rise about 3% a year, and the current level is not unreasonably high, as it was in the late 1990s.



U.S. equities have significantly outpaced Eurozone equities over the past nine years. That has a lot to do with the fact that the U.S. economy has grown faster as well.

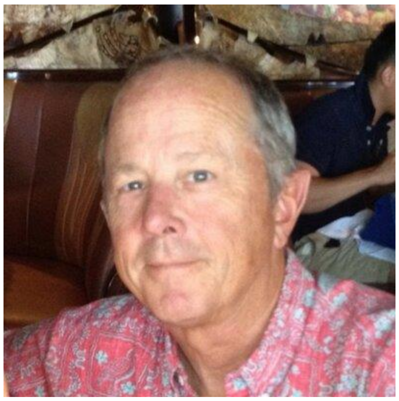
U.S. households (i.e., the private sector) have a net worth that is approaching $100 trillion. That figure has been growing at about a 3.5% annualized rate for a very long time. The current level of wealth is very much in line with historical experience.

Adjusting for inflation and population growth, the average person in the US is worth almost $300,000. That is, there are assets in the US economy which support our jobs and living standards (e.g., real estate, equipment, savings accounts, equities, bonds) worth about $300,000 per person.

We are richer than ever before, but the gains are very much in line with historical experience. (Note: the last two charts are based on Q1/17 data from the Federal Reserve. Data for Q2/17 will be released Sept. 21st, at which time I will be able to update these charts.)

BW: See ABOUT THE AUTHOR on the following page.

ABOUT THE AUTHOR



Scott Grannis was Chief Economist from 1979-2007 at Western Asset Management, a Pasadena-based, global manager of fixed-income portfolios for institutional clients.

He now enjoys keeping up on economics, markets, and politics from his condo overlooking Calafia Beach on the southern California coast, where he likes to think that he is immune to Wall Street group-think.

Married for 45 years to his Argentine wife, Norma, he has four children and five grandchildren (four boys and one girl).

He is a believer in supply-side economic theory, as practiced by his mentors, the late Jude Wanniski, Art Laffer, and Larry Kudlow. John Rutledge is another of his mentors, from the days that they worked together at Claremont Economics Institute.

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