Narrative Economics Summary

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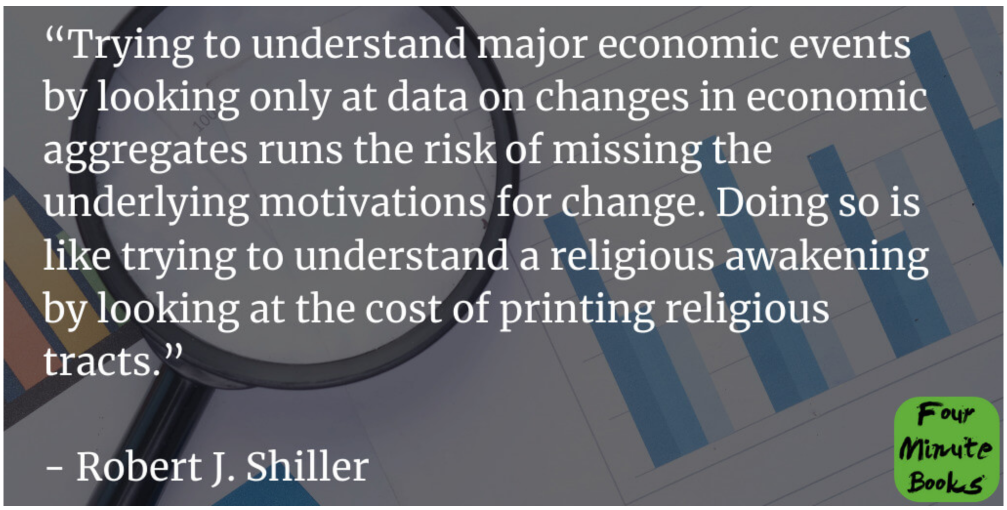
1-Sentence-Summary: *Narrative Economics explains the influence that popular stories have on the way economies operate, including the rise of Bitcoin, stock market booms and crashes, the nature of epidemics, and more.*

Read in: 4 minutes

Favorite quote from the author:



If you ask most economists about what makes a financial market fluctuate, they'll probably tell you it's all just statistics. To them, the economy is on its own numerical plane, separate from the rest of the world.

But here's the thing— the economy is driven by humans. Consumers, politicians, and business people all have a hand in affecting the way the market goes. And they are more than just a set of statistics. They have their own beliefs, biases, and passions. They are influenced by stories all around them.

The popular stories at the time can change economic outcomes, leading to everything from a craze of novice investors getting into Bitcoin to a spread of panic during a stock-market crash. So to get a full picture of what drives financial markets, one must also look at the surrounding narratives.

In *Narrative Economics: How Stories Go Viral and Drive Major Economic Events* by Robert Shiller, we explore how popular stories affect our economy. Shiller offers an entirely new way to look at economic change with plenty of historical evidence to back it up. By looking at financial markets this way, we can not only better understand the economy but also be prepared for what the future might throw at us.

These are the 3 most interesting lessons I got out of this book:

1. Bitcoin is the perfect example of how stories affect economics.
2. Epidemics and economic narratives have a lot in common.
3. If we want to be ready for the future, we need to understand the narratives of the past.

Let's jump right into these lessons and see what we can learn!

Lesson 1: To understand how stories affect economics, look no further than the example of Bitcoin.

When the idea of Bitcoin was first introduced online in 2008 by a mysterious person under the name Satoshi Nakamoto, hype quickly grew around it. It was an entirely new system of money that had the ability to change everything we know about currency. From there, it became a global phenomenon, though partly not for the reason you'd think.

Sure, its innovation and complex mathematical theory is impressive, but what excited most people about it seemed to be the hype and mystery surrounding it. If you ask most Bitcoin investors about the actual theory that runs Bitcoin, they probably could only give you the very basics.

But ask them about what excites them about it and they'll probably say it's the idea of a new, revolutionary way of using currency. The way of the future. **They feel that by investing in Bitcoin, they have a stake in the future, proving they are among the forward-thinkers of today.**

Another narrative attached to Bitcoin is that it's free of the control of governments and banks. This idea attracts those investors with an anarchic streak who view many modern institutions as corrupt. Because it isn't attached to any one country, investors feel they are promoting internationalism.

In short, it is these futuristic narratives along with the mysterious founding of Bitcoin that have made it so attractive to investors, not the complex math behind it. Without the exciting story, it probably wouldn't have succeeded as quickly as it has.

Lesson 2: There is a lot in common with epidemics and economic narratives.

Two subjects people don't usually compare are epidemiology, or the study of epidemics, and economics. This is a shame, because epidemiology and economics could learn a lot from each other. Epidemiologists study how diseases spread, and many of the patterns they see are similar to what economists observe.

For example, they study a disease like Ebola. They keep track of things like the rate of contagion and well as recovery and death rates. When an epidemic is quickly spreading, the contagion rate is much higher than death and recovery rates. When the epidemic starts to decline, the contagion rate falls while the recovery and death rate outnumbers new cases.

This idea can be applied to economic narratives that are contagious. The contagion of a narrative rapidly rises as people talk about it, whether through conversation in person or online. It also spreads through the news and other media. But just like an epidemic, eventually, the story slows down. People start to forget or they just lose interest and the story dies off.

We can see this parallel when we look at the Bitcoin craze again. If you search how often news stories over the last decade said the word "Bitcoin" you can see this pattern. There was a sharp increase in 2014, and then there was another peak in 2018 before it fell again.

While this isn't the end of the story for Bitcoin, we can see that the rapid increase and decline with secondary waves is strikingly similar to the shape of a graph of the contagion rate during an epidemic. So studying disease curves can give us a good idea of what a popular narrative might do to the market.

Lesson 3: We must understand the narratives of the past if we want to be ready for our economic future.

Clearly, narratives are important when we're looking at the economy. This is why it's essential that economists take these stories seriously, rather than just looking at the math, so they can more accurately predict what's coming next.

Luckily for economists, now more than ever we are able to access data about these narratives. We can learn through market research, looking at social media, and gathering information about internet searches.

Technology can help economists to find patterns in the data. They can then use this information to predict what the prominent narratives will be and how they might affect the economy. Shiller makes a point to say it has to be done carefully and accurately if you are studying the effects of narratives on economic events.

What good does this information do? **By having a good understanding of narratives, policy-makers can help shape people's behavior when there are times of stress.**

An example of this is during the Great Depression, when President Roosevelt addressed the nation with "fireside chats." He understood the people's lack of confidence was part of what was keeping the economy down. In these chats, he asked people to set aside their fears and spend money. It seemed to work, too. Following each address, the markets stabilized.

If people in charge of making policy understand the narratives and take control of them, they can be active participants in what's going on rather than just bystanders who have no control of the situation.

Narrative Economics Review

Narrative Economics is a super enlightening book. I'm not an economist, but I feel like this totally changes the way people will look at economics in the future! I think this is a really important conversation for us to be having in this day and age.

Who would I recommend the Narrative Economics summary to?

The 41-year-old financial analyst who wants to be ready for the future, the 63-year-old who doesn't understand money trends, and anyone who wants to be more informed about the past, present, and future of economics.