

Macro Roundup Article

Headline: [Long Term Expectations and Aggregate Fluctuations](#)

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Summary: The present value of short and long term expected earnings for S&P 500 firms, computed using a constant required return, fully explains observed stock market fluctuations btw 1980-2022. When long term earning growth (LTG) is high relative to historical standards, analyst forecasts of short and long term profits are systematically disappointed in the future, inconsistent with rationality. High LTG also correlates with higher survey expectations of stock returns, in contrast with standard theories, in which investors expect low returns in good times. High LTG thus proxies for excess optimism: it points to investors being too bullish about future profits and stock return. This evidence offers additional support to the hypothesis that boom-bust dynamics in non-rational expectations about the long-term act as an important driver of the volatility of key asset prices. A one standard deviation increase in LTG fuels an investment boom. Crucially, the investment boom sharply reverts 2 years later, and that reversal is fully explained by the predictable disappointment of the initially high LTG.

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Primary Topic: Business Cycle

Topics: Academic paper, Business Cycle, Financial Markets, GDP, Weekly

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