# Contents

(List of Figures) vii  
(Preface to the 2020 Paperback Edition) ix  
(Preface: What Is Narrative Economics?) xv  
(Acknowledgments) xxvii

## Part I  The Beginnings of Narrative Economics

1. The Bitcoin Narratives 3  
2. An Adventure in Consilience 12  
3. Contagion, Constellations, and Confluence 18  
4. Why Do Some Narratives Go Viral? 31  
5. The Laffer Curve and Rubik’s Cube Go Viral 41  
6. Diverse Evidence on the Virality of Economic Narratives 53

## Part II  The Foundations of Narrative Economics

7. Causality and Constellations 71  
8. Seven Propositions of Narrative Economics 87

## Part III  Perennial Economic Narratives

9. Recurrence and Mutation 107  
10. Panic versus Confidence 114  
11. Frugality versus Conspicuous Consumption 136  
12. The Gold Standard versus Bimetallism 156  
13. Labor-Saving Machines Replace Many Jobs 174

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### Contents

14  Automation and Artificial Intelligence Replace Almost All Jobs  
15  Real Estate Booms and Busts  
16  Stock Market Bubbles  
17  Boycotts, Profiteers, and Evil Business  
18  The Wage-Price Spiral and Evil Labor Unions  

**Part IV  Advancing Narrative Economics**  
19  Future Narratives, Future Research  

*Appendix: Applying Epidemic Models to Economic Narratives*  

<table>
<thead>
<tr>
<th>Notes</th>
<th>References</th>
<th>Index</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td>301</td>
<td>325</td>
</tr>
<tr>
<td></td>
<td>351</td>
<td></td>
</tr>
</tbody>
</table>
Chapter 1

The Bitcoin Narratives

This book offers the beginnings of a new theory of economic change that introduces an important new element to the usual list of economic factors driving the economy: contagious popular stories that spread through word of mouth, the news media, and social media. Popular thinking often drives decisions that ultimately affect decisions, such as how and where to invest, how much to spend or save, and whether to go to college or take a certain job. *Narrative economics*, the study of the viral spread of popular narratives that affect economic behavior, can improve our ability to anticipate and prepare for economic events. It can also help us structure economic institutions and policy.

To get a feel for where we are going, let’s begin by considering one such popular narrative, recently in full swing. Bitcoin, the first of thousands of privately issued cryptocurrencies—including Litecoin, Ripple, Ethereum, and Libra—has generated enormous levels of talk, enthusiasm, and entrepreneurial activity. These narratives surrounding Bitcoin, the most remarkable cryptocurrency in history as judged by the speculative enthusiasm for it and its market price rather than its actual use in commerce, provide an intuitive basis for discussing the basic epidemiology of narrative economics (which we explore in detail in chapter 3).

An *economic narrative* is a contagious story that has the potential to change how people make economic decisions, such as the decision to hire a worker or to wait for better times, to stick one’s neck out or to be cautious in business, to launch a business venture, or to invest in a volatile speculative asset. Economic narratives are usually not the most prominent narratives circulating, and to identify them we have to look at their potential to change economic behavior. The Bitcoin story is an example...
of a successful economic narrative because it has been highly contagious and has resulted in substantial economic changes over much of the world. Not only has it brought forth real entrepreneurial zeal; it also stimulated business confidence, at least for a time.

**Of Bitcoin and Bubbles**

The Bitcoin narrative involves stories about inspired cosmopolitan young people, contrasting with uninspired bureaucrats; a story of riches, inequality, advanced information technology, and involving mysterious impenetrable jargon. The Bitcoin epidemic has progressed as a cascading sequence of surprises for most people. Bitcoin surprised when it was first announced, and then it surprised again and again as the world’s attention continued to grow by leaps and bounds. At one point, the total value of Bitcoin exceeded US $300 billion. But Bitcoin has no value unless people think it has value, as its proponents readily admit. How did Bitcoin’s value go from $0 to $300 billion in just a few years?

The beginnings of Bitcoin date to 2008, when a paper titled “Bitcoin: A Peer-to-Peer Electronic Cash System,” signed by Satoshi Nakamoto, was distributed to a mailing list. In 2009, the first cryptocurrency, called Bitcoin, was launched based on ideas in that paper. Cryptocurrencies are computer-managed public ledger entries that can function as money, so long as people value these entries as money and use them for purchases and sales. There is an impressive mathematical theory underlying cryptocurrencies, but the theory does not identify what might cause people to value them or to believe that other people will also think they have value.

Often, detractors describe the valuation of Bitcoin as nothing more than a speculative bubble. Legendary investor Warren Buffett said, “It’s a gambling device.” Critics find its story similar to the famous tulip mania narrative in the Netherlands in the 1630s, when speculators drove up the price of tulip bulbs to such heights that one bulb was worth about as much as a house. That is, Bitcoins have value today because of public excitement. For Bitcoin to achieve its spectacular success, people had to
become excited enough by the Bitcoin phenomenon to take action to seek out unusual exchanges to buy them.

For Bitcoin’s advocates, labeling Bitcoin as a speculative bubble is the ultimate insult. Bitcoin’s supporters often point out that public support for Bitcoin is not fundamentally different from public support for many other things. For example, gold has held tremendous value in the public mind for thousands of years, but the public could just as well have accorded it little value if people had started using something else for money. People value gold primarily because they perceive that other people value gold. In addition, Peter Garber, in his book *Famous First Bubbles* (2000), points out that bubbles can last a long time. Long after the seventeenth-century tulip mania, rare and beautiful tulips continued to be highly valued, though not to such extremes. To some extent, tulip mania continues even today, in a diminished form. The same might happen to Bitcoin.

 Nonetheless, the value of Bitcoin is very unstable. At one point, according to a headline in the *Wall Street Journal*, the US dollar price of Bitcoin rose 40% in forty hours on no clear news. Such volatility is evidence of the epidemic quality of economic narratives that may lead to an erratic jostling of prices.

 I will make no attempt here to explain the technology of Bitcoin, except to note that it is the result of decades of research. Few people who trade Bitcoins understand this technology. When I encounter Bitcoin enthusiasts, I often ask them to explain some of its underlying concepts and theories, such as the Merkle tree or the Elliptic Curve Digital Signature Algorithm, or to describe Bitcoin as an equilibrium of a congestion-queueing game with limited throughput. Typically the response is a blank stare. So, at the very least, the theory is not central to the narrative, except for the basic understanding that some very smart mathematicians or computer scientists came up with the idea.

 Narrative economics often reveals surprising associations. Reaching back into history, we see the beginnings of the emotions behind the Bitcoin epidemic in the origins of the growth of anarchism in the nineteenth century.
Beginnings of Narrative Economics

Bitcoin and Anarchism

The anarchist movement, which opposes any government at all, began around 1880 and followed a slow growth path, according to a search for anarchist or anarchism on Google Ngrams. But the term itself dates back decades earlier, to the work of philosopher Pierre-Joseph Proudhon and others. Proudhon described anarchism in 1840 as follows:

To be governed is to be watched, inspected, spied upon, directed, law-driven, numbered, regulated, enrolled, indoctrinated, preached at, controlled, checked, estimated, valued, censured, commanded, by creatures who have neither the right nor the wisdom nor the virtue to do so.⁴

Proudhon’s words clearly appeal to people who feel frustrated by authority or blame authority for their lack of personal fulfillment. It took about forty years for anarchism to reach epidemic proportions, but it has shown immense staying power, even to this day. Indeed, the Bitcoin.org website carries a passage by anarchist Sterlin Lujan, dated 2016:

Bitcoin is the catalyst for peaceful anarchy and freedom. It was built as a reaction against corrupt governments and financial institutions. It was not solely created for the sake of improving financial technology. But some people adulterate this truth. In reality, Bitcoin was meant to function as a monetary weapon, as a cryptocurrency poised to undermine authority.⁵

Most Bitcoin enthusiasts might not describe their enthusiasm in such extreme terms, but this passage seems to capture a central element of their narrative. Both cryptocurrencies and blockchains (the accounting systems for the cryptocurrencies, which are by design maintained democratically and anonymously by large numbers of individuals and supposedly beyond the regulation of any government) seem to have great emotional appeal for some people, kindling deep feelings about their position and role in society. The Bitcoin story is especially resonant because it provides a counternarrative to the older antianarchist narratives depicting anarchists as bomb-throwing lunatics whose vision for society can lead only
to chaos and violence. Bitcoin is a contagious counternarrative because it exemplifies the impressive inventions that a free, anarchist society would eventually develop.

The term *hacker ethic* is another modern embodiment of such anarchism. Before the widespread availability of the World Wide Web, sociologist Andrew Ross wrote, in 1991,

> The hacker ethic, first articulated in the 1950s among the famous MIT students who developed multiple-access user systems, is libertarian and crypto-anarchist in its right-to-know principles and its advocacy of decentralized technology.6

In his 2001 book *The Hacker Ethic and the Spirit of the Information Age*, Pekka Himanen wrote about the ethic of the “passionate programmers.”7

In the Internet age, people’s willingness and ability to work together with new technology—in new frameworks that do not rely on government, on conventional profit, or on lawyers—have surprised many of us. For example, wikis, notably Wikipedia, encourage cooperation among large numbers of anonymous people to produce amazing information repositories. Another success story is the Linux operating system, which is open-source and distributed for free.

But among the many examples of viral economic narratives, Bitcoin stands supreme. It is a narrative that is well crafted for contagion, effectively capturing the anarchist spirit; and, of course, that is why most of us have heard of it. It is part bubble story, part mystery story. It allows nonexperts and everyday people to participate in the narrative, allowing them to feel involved with and even build their identity around Bitcoin. Equally appealing, the narrative generates stories of untold riches.

### Bitcoin as a Human-Interest Narrative

The Bitcoin narrative is a motivating narrative for the cosmopolitan class around the world, for people who aspire to join that class, and for those who identify with advanced technology. And like many economic narratives, Bitcoin has its celebrity hero, Satoshi Nakamoto, who is a central human-interest story for Bitcoin. Adding to the romance of the Bitcoin
narrative is a mystery story, for Satoshi Nakamoto has never been seen by anyone who will testify to having seen him. One early Bitcoin code-developer said that Satoshi communicated only by email and that the two had never met in person. On its website, Bitcoin.org says only, “Satoshi left the project in late 2010 without revealing much about himself.”

People love mystery stories and love to unravel the mystery, so much so that there is a rich genre of mystery literature. Bitcoin’s mystery story has been repeated many times, especially when intrepid detectives have identified a person who may be Nakamoto. The repeated publicity for an intriguing mystery made the contagion rate of the Bitcoin narrative higher than it would have been otherwise.

**Bitcoin and the Fear of Inequality**

In addition to tapping into anarchist sentiment and the mystery of Satoshi Nakamoto, the Bitcoin story is a story of the desire for economic empowerment. During the twenty-first century, as economic inequality in advanced countries has increased rapidly, many people feel helpless, and they desire greater control over their economic lives. Bitcoin prices first took off around the time of the 2011 Occupy Wall Street / “We are the 99%” protests. Adbusters, a social activist organization that wanted its message to go viral, launched these protests in the United States, and Occupy protests occurred in many other countries too. It is no coincidence that the Bitcoin narrative is one of individual empowerment, because, according to the narrative, the coins are anonymous and free of government control, management, and reach.

Another part of the underlying narrative that has spurred Bitcoin’s and other cryptocurrencies’ high contagion rate is the story of computers taking greater and greater control of people’s lives. In the twenty-first century, people have access to automated assistants, such as Amazon’s Alexa, Apple’s Siri, and Alibaba’s Tmall Genie, that understand human speech and respond knowledgeably and intelligently to questions with a simulated human voice. In addition, driverless cars, trucks, trains, and ships seem likely in the near future, raising the specter of mass unemployment among truck drivers and other people who drive or navigate for a
living. The “technology is taking over our lives” narrative is the most recent incarnation of a labor-saving-machinery narrative that has scared people since the Industrial Revolution.

The insistent fear in this Luddite narrative (to which we will return in chapter 13) is that machines will replace jobs. The fear is not that you will show up for work one day and be told that the company is purchasing a new computer that will do your job. Rather, the changes are more gradual, inevitable, and cosmic. More likely, as computers automate more tasks, you may find that your employer seems increasingly indifferent to your presence, fails to offer pay raises, does not encourage you to stay with the company, and doesn’t hire others like you, and eventually no longer even remembers you. Fear about your future is more an existential fear about not being needed.

In such an environment, options are eliminated. Computers can be educated to perform new tasks many orders of magnitude faster than human beings can. Calls for government expenditures on education of people to offset the job loss created by computers seem justified, but it is hard to imagine that people can win in the long run. Millions of students around the world question whether their education is preparing them for success, creating an anxiety that indirectly feeds the contagion of technologically driven cryptocurrencies such as Bitcoin, which seem at least superficially to offer some imaginable hope of mastering the computers.

### Bitcoin and the Future

The digital signature algorithm that underlies Bitcoin, that defines a Bitcoin’s individual owner, and that makes it prohibitively difficult for thieves to steal Bitcoin has received some attention since the early 1990s, but coverage of that narrative epidemic cannot compare with coverage of Bitcoin itself. ProQuest News & Newspapers finds only one article with the words *elliptic curve digital signature algorithm* in its entire database. It finds only five articles that use the phrase *digital signature algorithm*. The RSA algorithm, the original cryptography algorithm that may have started the Bitcoin revolution, dates back to 1977. ProQuest lists
twenty-six articles that mention the RSA algorithm. But that number doesn’t begin to compare with the fifteen thousand–plus articles that mention the word Bitcoin.

The difference must result from the contagiousness of the larger Bitcoin narrative. The phrase *digital signature algorithm* sounds like something a student would be trying to memorize for an exam: technical, painful, boring. There is so much more to the Bitcoin story. Notably, it is a story about how Bitcoin investors have become rich simply by being aware of new things on the cutting edge. Bitcoin is about the “future.” That sound bite is easily remembered, a topic to bring up with enthusiasm in conversation at a social gathering. In short, Bitcoin is a gem of a story.

People often buy Bitcoin because they want to be part of something exciting and new, and they want to learn from the experience. This motivation is particularly strong because of the underlying story, the narrative that computers are poised to replace many of our jobs. But computers can’t replace all of our jobs. Somebody has to control those computers, and there is a narrative today that the people in charge of the new technology will be the winners. Very few people feel secure that they will be on the winning end of this curve. Even taking a degree in computer science doesn’t seem to be a sure path to success today, because it may lead to a humdrum job as a low-level programmer, or even to no job at all. A desire to be on the finance side of the tech business, where Bitcoin sits, is popular because there are so many stories illustrating that financiers take control of things. Bitcoin enthusiasts may think that experimenting with Bitcoin will put them in touch with the people who are going to be winners in the new world, will give them insight about how to stay in (or gain) control. It is easy to jump-start one’s connection to this new reality by buying some Bitcoin. Best of all, one doesn’t have to understand Bitcoin to buy it. Vending machines at convenience stores now sell Bitcoins and other cryptocurrencies. This “Be a part of the future” narrative, enhanced by regular news of exciting fluctuations in the price of Bitcoins, gives them value. It generates fluctuations in Bitcoin prices in terms of national currencies, and these fluctuations thrive on and produce contagious narratives.
Bitcoin as a Membership Token in the World Economy

We are living in a peculiar transition period in human history, in which many of the world’s most successful people see themselves as part of a broader cosmopolitan culture. Our nation-states sometimes seem increasingly irrelevant to our ambitions. Bitcoin has no nationality, giving it a democratic and international appeal. Inherent in its pan-national narrative is the idea that no government can control it or stop it. In contrast, old-fashioned paper money, typically with historical engravings of famous men in a country’s history, suggests an obsolete nationalism, something for losers. Paper currency resembles little national flags in a way; it is a symbol of one’s nationality. Having a Bitcoin wallet makes the owner a citizen of the world and in some sense psychologically independent of traditional affiliations.

How, then, do we summarize the popularity of Bitcoin? In the end, people are interested in Bitcoin precisely because so many other people are interested in it. They are interested in new stories about Bitcoin because they believe that other people will be interested in them too.

The surprising success of Bitcoin is not really so surprising when we consider the basic principles of narratives discovered by intellectuals who have thought about the human mind, about history, and about mathematical models of feedback. We discuss these great thinkers and their contributions in the next chapter. Most of these thinkers were not economists by training or profession.
Index

A page number followed by f refers to a figure or its caption.

*The A B C of Technocracy* (Arkwright), 193
Abelson, Robert P., 37
Adams, James Truslow, 151, 153–54
Adbusters, 8
Addams, Jane, xvii
Advanced Micro Devices, Inc., 20
advertisements: for homeownership, 219–20; online searching of, x; phrase
*American Dream* in, 154
affect heuristic, 67, 233
Aiden, Erez, 24
AIDS (acquired immune deficiency syndrome), 24
Akerlof, George, xviii, 61, 64, 67, 250, 300, 301n13
Aldrich-Vreeland Act, 117
Alexa, of Amazon Echo, 8, 207
Alibaba’s Tmall Genie, 207
Alice, Yandex, 207
*Alice’s Adventures in Wonderland* (Carroll), 189
Allen, Frederick Lewis, ix–xi, 139
Allen, Lily, 92
AlphaZero chess computer program, 208, 316n22
Amazon’s Echo, 207
*American Dream* (O’Neil), 153
*The American Dream* (Albee), 153
American Dream Downpayment Assistance Act, 154
American Dream narrative, 151–55, 152f; stock market crash of 1929 and, 231
American Federation of Labor, 241
*The American Plutocracy* (Howard), 166
analogies, brain response to, 17
anarchism: Bitcoin narrative and, 5–7; history of, 6
Angell, Norman, 95
anger about inflation, 239, 263–64, 265–66; during wars, 265; after World War I, 245, 247
anger at businesspeople: boycott narrative and, 240; cuts in wages and, 239; depressions of 1920–21 and 1930s and, 243; inflation and, 239, 245, 247, 263–64, 265; profiteer narrative and, 241–43, 245, 247, 248–49, 250. See also boycott narrative
anger at oil crisis of 1970s, 256
animal spirits: business confidence and, xvi; Keynes’s idea of, 138
*Animal Spirits* (Akerlof and Shiller), 64
Anthropology: creation myths in, 15; economists learning from, 78
Apple Computer: Siri and, 8, 206–7, 287; Steve Jobs and, 208–9
Arab oil embargo of 1973, 256
archetypes, Jungian, 15
ARIMA (autoregressive integrated moving average) models, 295, 322n9
Aristotle, 174–75
Arkwright, Frank, 193
Arkwright, Richard, 193
artificial intelligence, in narrative economics research, 276, 287
artificial intelligence narrative, 196, 197f, 199, 211. See also robots
Atari, 203
*Atlas Shrugged* (Rand), 50

For general queries, contact webmaster@press.princeton.edu
autism spectrum disorder, narrative disruption in, 66
Automata (Hero of Alexandria), 175
automated assistants, 8. See also Siri (Apple)
automation narrative: difference from labor-saving machinery narrative, 199; as epidemic around 1955–66, 199–202; mutated in recessions of early 1980s, 204; with new catchphrases in 2000s, 205; offices and, 204; percentage of articles containing automation, 197f; post–World War II, 196; robots and, 191; second scare during 1980s, 202–4; surge in fears beginning around 2016, 206–8; third spike in concern around 1995, 204–5; unemployment and, 199–200, 204. See also robots
“automation recession” of 1957–58, 201, 264
autosuggestion narrative, 119, 120f, 121–23
baby boom, optimism associated with, 198
baby boomers retiring, elevated stock market and, 29
Baker, Charles Whiting, 210
bank failures: Great Recession of 2007–9 and, 132; loss of confidence during Great Depression and, 132
Bank of Canada, 156\bank runs: during 1857 financial panic, 115; in 1873, during depression, 176; in 1893, 164–65; in 2007 and 2008, 119, 134–35; as crisis of confidence, 114; Great Depression and, 133, 134–35; Roosevelt’s “fireside chat” during, 129, 278
banks taking risk, ten years after 2007–9 financial crisis, 55–56
Barthes, Roland, 85
Bartholomew, D. J., 296
Baruch, Bernard, 236, 237
Basic Income Earth Network, 210
basic story structures, 15–16
Bauckhage, Christian, 297–98
Baum, L. Frank, 171, 313n29
“beauty contest” metaphor, 63–64
behavioral economics, 277–78. See also economic behavior affected by narratives beliefs of public, and major economic events, xv
Bell, Brad E., 78
Bergman, Ingmar, 49
Bernanke, Ben, 156–57
best seller lists, 88
Bewley, Truman, 147, 281
bicycle craze in the Depression, 143, 149
Big Brothers movement, 274
bimetallism: appearance in news articles by year, 22, 22f; arguments in opposition to, 169; Bitcoin and, 108, 161–62, 171; epidemic theory applied to, 22–23; geographic and social-class dimensions of, 160, 161, 162–63; international contagion of, 160–61; popular in late nineteenth century, 158, 159–61; prior to being ended in 1873, 157; reasons for popular narratives about, 170–71; secondary epidemic in 1930s, 23. See also gold standard
Bitcoin narrative, xviii, 3–11; anarchism and, 5–7; bimetallism and, 108, 161–62, 171; cause of increased value and, 72; contagion of, 21–23; cosmopolitan culture and, 4, 11, 87; cryptocurrencies competing with, 92; epidemic theory applied to, 21–23; fading by 2013, 76; fascination with narratives about money and, 173; fear of inequality and, 8–9; the future and, 9–10, 87; geographic pattern of spread, 299; history of, 4; as human-interest story, 7–8; key features of, 87; mathematical concepts underlying, 5, 302n3; membership in world economy and, 11; as mystery story, 7, 8, 162; in news articles by year, 22, 22f; in news articles compared to relevant algorithms, 9–10; sale of Bitcoin in convenience stores and, 10; similarity to gold standard and bimetallism narratives, 108–9; as

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successful economic narrative, 3–4; technocracy movement and, 193; uncertain truth of, 96; volatility of value in, 5, 10. See also Nakamoto, Satoshi

Bix, Amy Sue, 186–87

Blade Runner (film), 203

Blanc, Louis, 102

Blinder, Alan, 281

blockchains, 6

blue jeans, 147–48, 149

blue sky laws, 220, 221

Booker, Christopher, 16

book jackets, 60–61

Boulding, Kenneth E., xv–xvi

Box, George E. P., 295

Boycott, Charles C., 239–40

The Boycott in American Trade Unions (Wolman), 241

boycott narrative, 239–43; in 1973–75 recession, 256–57; contributing to 1920–21 depression, 249; going viral, 241; during Great Depression, 254; origins of, 239–40; profiteer stories in World War I and, 241–42, 246; recurring periodically, 241; during world financial crisis of 2007–9, 257; after World War II, 255. See also anger at businesspeople

brain: activated by analogy and metaphor, 17; basic story structures and, 15–16; being replaced by artificial intelligence, 199, 211; in dreaming, 32; fear-related structures in, 56–58; flashbulb memory and, 80–81; long-term memory formation and, 47; narrative processing disrupted by injury to, 65–66; narrative tendency in music and, 35; neurolinguistics of narrative and, 16–17; risk assessment by, 67; sharing content in form of stories and, 54; source monitoring by, 84, 307n21. See also neurolinguistics and narrative

breadline, 134

Brooks, Peter, 16

Brown, Donald E., 33

Brown, Roger, 307n13

Bruner, Jerome, 65


Buffett, Warren, 4

Burns, Arthur F., 125, 309n10

Bush, George W., 83, 154–55

business confidence narrative, 114–15, 116f, 118–19; conventional economists’ view and, xvi–xvii; gold standard and, 167, 168–69; stimulated by Bitcoin narrative, 4

business cycle, 124–25, 271. See also economic fluctuations

butterfly effect, 299–300

buy-and-hold strategy, xiii

“Buy Now Campaign” during Great Depression, 255

Callahan, Charlene, 281

Canada, National Dream, 151; Bank of Canada, 156

Čapek, Karel, 181–82, 203

Capital in the Twenty-First Century (Piketty), 150, 210–11

capitalism: Bitcoin narrative and, 87; triumphant narrative of, 29

Capper, Arthur, 249

The Captive Mind (Milosz), 57

Carroll, Lewis, 188

Case, Karl, 216, 226, 285

Case-Shiller home price index, 216, 222

Cass, David, 74

Cassel, Gustav, 188

causality between narratives and events, 71–74; controlled experiments and, 72–73, 77–79; vs. correlation, 286; direction of, 71, 72–74; economists’ presumption about, 73, 76–77; flashbulb memory and, 80; for recessions and depressions in US, 112. See also self-fulfilling prophecies in economics
Cawelti, John G., 16
celebrities: adding human interest to narratives, xii, 100–102, 153; Alan Greenspan as, 227; American Dream narrative and, 153; in Bitcoin-related stories, 7–8, 92; of Bloomsbury group, 26; changed in mutated narrative, 108–9; economic events affected by colorful phrases of, 75–76; forgotten or discredited, 110; Franklin Roosevelt as, 128; J. P. Morgan as, 115, 117–18; Keynes as, 25–26; not usually the inventors of narratives, 72; Oliver Wendell Holmes, Jr., as, 127; preference for one's country or ethnic group, 102; quotes associated with, 102; Reagan's free-market revolution and, xii; Reagan's supply-side rhetoric and, 51; shoeshine boy narrative and, 236–37; substituted as originator of a quote, 102; substituted for different target audience, 101; substituted to increase contagion, xii; Trump as, xii; Virginia Woolf as, 26; William Jennings Bryan as, 168
Civil War, US: anger at those profiting during, 265–66; depression prior to, 111; emotional power of narratives and, 14; narrative describing first shots of, 81; panic of 1857 in run-up to, 115; Uncle Tom narrative and, 33
Cobden, Richard, 110
coop-epidemics: of diseases, 294–95; of diseases with narratives, 23; of narratives, 28, 110, 225, 322n9 (see also constellations of narratives)
Coinage Act of 1834, 157
Coinage Act of 1873, 157, 165
Coin's Financial School (Harvey), 161, 162
Cole, Harold L., 132
collective consciousness, 60
collective memory, 60
communications technology. See information technology
compartmental models of epidemics, 23, 289–93, 291f; applications that don’t fit such models well by, 295–96; ARIMA models and, 295; changed for social epidemics and epidemics of ideas, 296, 297; geographic, 296, 299; network models, 296. See also Kermack-McKendrick SIR model
compassion narrative, 137, 140, 141–42; decline in, 150, 272; in Japanese “lost decades,” 150
complacency, before financial crisis, 55–56
computer networks, singularity associated with, 204–5
computers: automation narrative mutated by, 204–5; “electronic brain” narrative and, 195; fear that jobs will be replaced by, 9, 10, 201; inequality in access to, 211; replacing human thinking, 199; successful in the home beginning in 1980s, 203; taking control of people's lives, 8–9, 87
condominium conversion boom, 223–24
confabulation, 32, 66, 96
confidence indexes, 79, 119, 129, 266–67
confidence narratives: of 1930s still affecting public confidence, 129, 252; business cycle and, 124–25; causes of Great Depression and, 130, 132; classes of, 114–15, 116f; Hitler’s appeal and, 122; labor-saving machinery narrative and, 174; opinion leaders’ optimistic assurances and, 125–26, 127–28; other people’s confidence and, 114, 272; rapid changes in, 272; real estate and, 212; seemingly irrelevant events affecting, 67; stock market crash narrative and, 238; stock prices and, 228; weather forecasting and, 123. See also business confidence narrative; consumer confidence narrative; financial panic narrative
confluence of narratives, 29–30
Conley, John M., 15
consilience, 12–17
conspicuous consumption narratives, 136; American Dream narrative and, 154, 155; delaying car purchase during Depression and, 144; depression prolonged by avoidance of, 139, 142, 144–46; housing boom narrative and, 225; Veblen and, 154, 310n1
conspiracy theories in narrative, 35–36
constellations of narratives, 28–30; built around celebrities, 101–2; class struggle over gold standard and, 166–67; co-epidemic models applied to, 295; economic decision-making and, 91; of financial panic narratives, 115, 118f; Great Depression and, 129, 131, 135, 144; about Halley’s comet, 124; “Happy Birthday to You” and, 100; about housing market, 227; impact of, 29, 92–93; Laffer curve in, 47–48; names attached to, 94–95; as new context for old narratives, 271; not obvious from archival data, 86; opposing pairs of, 113; overview of, 28–30; on people paying more than 100% in taxes, 49; random events feeding into, 40, 99–100; recovery rates and, 89; after September 2001 terrorist attacks, 83, 307n20; about stock market bubbles, 228; suggestibility and, 119; supply-side economics as, 47–48; on tax cutting and smaller government, 52; on Wizard of Oz, 172
Consumer Confidence Index, 119, 266–67
consumer confidence narrative, 115, 116f, 118–19; nineteenth-century worldviews and, 116–17
Consumer Expenditure Survey of Federal Reserve, 282
Consumer Financial Protection Bureau, and interstate land sales, 317n15
consumerism, Albee’s criticism of, 153
Consumer Price Index (CPI), 245
customers, theories based on motives and habits of, xv
clearance: depression prolonged by avoidance of, 139, 142, 144–46, 149; excesses of 1920s, 139; feedback loop between job loss and, 144–45; frugality narratives in Great Depression and, 136–37; labor-saving machinery narrative and, 209; underconsumption theory and, 187–92; visibility index of categories of, 144. See also conspicuous consumption narratives; spending
contagion of economic models, 24–28
contagion of economic narratives: affecting economic activity, 77; attached to celebrities, xii, 51; based on citations, 321n22; bimetallism and, 171; Bitcoin and, 21–23; consumer behavior and, 254; enhanced by memories, 252; focus group research and, 283; Frederick Lewis Allen and, x, xi; as heart of narrative economics, x; home prices and, 215, 226, 227; marketing-driven, 60–63, 297; medical model of epidemics and, 21, 23; by modern media, 297; mutation of
contagion of economic narratives (continued)
narrative and, 109; new theory of economic change based on, 3; opportunities for repetition and, 97; perceptions of other people’s reactions and, 64; profiteer narrative and, 241–42; stock market crash of 1987 and, 233; wage-price spiral narrative and, 260
contagion of ideas or social epidemics, 296, 297
contagion of narratives: caused by unknown processes, 41; celebrity as source of, 102; functioning as metaphors, 17; historical recognition of, 58–60; by modern media, 297; often resulting from arbitrary details, 62–63; opportunities for repetition and, 97–100; theory of mind and, 63. See also contagion of economic narratives
contagion rates: book jackets and, 60–61; credibility of narrative and, 28–29; cultural factors affecting, 274; declining with time, 296; difficulty of predicting, 41; in disease epidemics, 18–21, 289, 290; effect of slight changes in, 40; engineered by marketers, 60; great variability of, 88–89; increased by new context, 271; increased by social media, 297; models from epidemiology and, 23–24, 295, 296; new technology leading to changes in, 273–75; novel ideas and concepts affecting, 97; raised by small detail, 45; of true vs. false stories, 96–97; varying through time, 295
controlled experiments on causality, 72–73; from outside economics, 77–79
Coolidge, Calvin, 44, 125
Coolidge-Mellon bull tips, 125–26
corporate profits: taxes on, 45, 48; viral narratives associated with, 47–48
corporate raiders, as viral term in 1980s, 47–48
cortisol, 54–55
cosmopolitan culture, and Bitcoin, 4, 11, 87
cost-push inflation, 258–59, 259f, 260
Coué, Émile, 121
CPI (Consumer Price Index), 245
crash narrative, 228, 229–33. See also stock market crash narrative
creative people: of news media, 75; recurrent narratives due to, 109–10; viral narratives due to, 60
credibility of narratives in a constellation, 28–29
Crimean War, effect of weather forecasting on, 123
Crime of 1873, 157–58, 171
criminology, narrative, 15
crocodile logo, 62
Cronon, William, 79
“Cross of Gold” speech, 167–68
cryptocurrencies: concept of, 3, 4; constellation of related narratives about, 92; gold standard and, 157; initial coin offerings (ICOs) and, 76; lack of definite knowledge about, 96; sold by vending machines, 10. See also Bitcoin narrative
“Cult of the Offensive,” 95
cultural change: constellations of narratives behind, 86; narratives as vectors of, xiii; two-step flow hypothesis of, 297
cultural entrepreneur, 71–72
cultural factors affecting contagion rates, 274
Curley, James, 128
cybernation, 202
Daley, Daryl J., 296
databases for studying narratives, 279, 281–82, 284–85. See also search engines; searching digitized data; textual analysis
Davis, Chester C., 190
Davis, Henry L., 167
Davis, Morris A., 214
Dean, James, 148
debt, and promotion of homeownership, 219
INDEX 357

decision-making: automated by technology, 275; changed by economic narratives, 3; constellations of narratives in determination of, 91; fear-related brain circuitry and, 57–58; focused interviews for research on, 281; framing and, 66; of investors in stock market, 298–99; leading indicators approach and, 125; by mass of people not well-informed, 86
deficit spending: of Hoover administration, 188; Laffer curve and, 42
deflation: in depression of 1920–21, 111, 243–45, 246, 251, 253; gold standard and, 157, 161; in Great Depression, 253; wage cuts necessitated by, 188, 251
demand, depending on changes in narratives, 149–50
demand-pull inflation, 258
De Oratore (Cicero), 34
department store movement, 180
depression of 1873–79, 174, 176–79, 183, 188, 209
depression of 1893–99, 158, 159, 161, 163–65, 174, 179–81, 239, 241
depression of 1920–21, 111, 242–43; angry narratives in, 239, 241, 242; boycotts during, 254; deflation in, 111, 243–45, 246, 251, 253; excess profits tax contributing to, 249; fair wage narrative in, 250; family morale in, 138; fear of ostentation in, 144; Great Depression of 1930s and, 243, 251–53; labor-saving machine narrative and, 181–82; narratives causing abrupt end of, 250–51; postponement of purchases contributing to, 245, 246, 249; technocracy and, 193
depression of 1930s. See Great Depression of 1930s
depressions: in American colonies following French and Indian War, 58–59; biggest in US since 1854, 111–12; causes listed by economic historians, 112; crowd psychology and suggestibility in understanding of, 120; expected after World War II, 196–97, 199; gold standard narrative during, 158–59; information cascades and, 300; as narratives in themselves, 112; nineteenth-century worldviews and, 116–17; psychologically based economic narrative of, 118; technological unemployment narrative during, 176
The Desk Set (film), 201
devaluation: entering English language in 1914, 159; as positive terminology, 172–73; of US dollar in 1933, 172
dial telephone, and unemployment, 187, 190–91
digital divide, 211
digital signature algorithm, 5, 9–10
The Disposable American (Uchitelle), 150
donkeys for important ideas, 26, 303n11
dot-com boom, 109, 205, 206
dreaming: narrative form of, 32; suggestibility and, 120, 121
driverless vehicles, 8–9, 174–75, 207, 314n1 Dust Bowl, 130–31
dysnarrativia, 65–66
Ebola epidemics, 18–19, 19f, 21, 23–24; co-epidemics with narratives, 23; SEIHFR model of, 294
Eckstein, Otto, 112
eclipse of the sun in 2017, 61–62
economic behavior affected by narratives, xi, xii, xviii, 3; brief exposure to narrative and, 80; difficulty in establishing connection, 93, 286; false narratives and, 97; forgetting and, x; with impact changing through time, 93–95, 283–84; scripts involved in, 74; in small fraction of population, 29; uncertain knowledge and, 96; years after the relevant narrative, 109. See also consumption; economic events affected by narratives; investment; saving; spending
Economic Consequences of the Peace
(Keynes), xvii, 26

economic events affected by narratives, xii;
biggest such events in US since 1854, 111–12; celebrities’ phrases with impact on, 75–76; difficulty of predicting, 58; economists’ presumption about economic forces and, 76–77; by fake narratives, 85; by false narratives, 95; by frugality vs. conspicuous consumption narratives, 136; by latent narratives of earlier years, 109; limited value of quantitative indexes and, 74–75; seemingly irrelevant factors and, 67.

See also causality between narratives and events; depressions; economic behavior affected by narratives; recessions.
economic fluctuations: driven by attention-getting narratives, 86; leading indicators approach to, 125; seen as repetitive and forecastable, 124–25; self-fulfilling prophecies and, 73–74
economic forecasting: analogy to weather forecasting, 123–25; ARIMA models in, 295; business cycle and, 124–25; causes of events and, 71; economists’ poor record of, xiii–xv, 301n5–6; epidemic models and, xi, 295; leading indicators approach to, 125, 309n10; many different narratives required for, 267; moral imperative of, xv–xvii; promise of narrative economics for, xi, xiv–xv, 13, 277; self-fulfilling prophecy in, 123–24, 198
economic growth: inflation and, 319n10; supply-side economics and, 48. See also GDP growth in US
economic institutions, importance of narratives and, 3, 14
economic man, as rational optimizer, 120
economic models, contagion of, 24–28, 27f
economic narratives: analytical value of looking at, 238; anniversaries of past events and, 76; confluence of, 29–30; creative and innovative, 75; defined, 3; distorting professional narratives, xiii; geographic pattern of spread, 296, 299; history of, going back to ancient Rome, 58–60; human significance of stories and, 79–80; immense complexity of landscape of, 266–67; international, 110; judging which are important, 89–91; key features of, 87; medical model of epidemics and, 21–23; names attached to, 94–95; narratives that become economic, 74; originating with one or a few people, 71–72; oversimplified variants of, 26; predictable workings of, 77; recurrence of, 107–8, 109–10, 238; self-censorship of, encouraging panic, 115; seven key propositions with respect to, 103. See also constellations of narratives; contagion of economic narratives; moral dimensions of economic narratives; mutation of economic narratives; narrative economics; narratives; viral narratives
economic policy. See policy
economics profession: behind other disciplines in attention to narratives, 12–13, 13f; events as natural experiments in, 72–73; potential of collaborative research for, 17, 302n1
economic stimulus: Keynes and Samuelson on effects of, 27–28; in Republican policy of 1920s, 189; stimulate the economy as phrase in late twentieth century, 50–51
economic strength, perception of, 272
education, narrative-centered learning in, 77–78
efficiency experts, 184
Eichengreen, Barry, 133, 172
Einstein, Albert, 192, 199
Eisenhower, Dwight, 261
electric dollars, 193
electronic brain, 195
Elliott, Catherine S., 281
elliptic curve digital signature algorithm, 5, 9
emotions: affect heuristic and, 67, 233; Bitcoin epidemic and, 5–6; in construction of narratives, 65; of financial panics, 115; flashbulb memory and, 80–81, 307n13; of gold standard debate, 160, 172; Harding’s references to normalcy and, 244; historians’ explanatory use of, 14; in housing boom of 1997–2006, 217; perceptions of people’s reactions to story and, 64; profiteer narratives and, 247, 249; in quantitative study of narratives, 287; in response to narratives, xi, 35, 54; revealed in stories, xi, 35, 54; risk assessment and, 67; studied in economics without being partisan, 279; underconsumption narrative during Depression and, 188. See also anger about inflation; anger at businesspeople; anger at oil crisis of 1970s; fear

The Engineers and the Price System (Veblen), 193
entrepreneurship: cryptocurrencies and, 4, 92; labor-saving machinery narrative and, 209; Reagan policies and, 52
The Epic of America (Adams), 151

epidemic curve, 18–24, 19f, 22f, 289–93, 291f
epidemics of diseases: AIDS, 24; co-epidemics with narratives, 23; recurrence and mutation of, 108; repeats of variants of, 271; size of, 292–93. See also Ebola epidemics; influenza; Kermack-McKendrick SIR model
epidemics of economic narratives: on automation, 199–200; on bimetallism, 22–23, 22f; on Bitcoin, 22–23, 22f; co-epidemics of diseases with narratives, 23; co-epidemics of narratives, 294–95, 322n19; on cost-push inflation, 258, 259f; on electronic brain, 195; forecasting and, xi, 295, 322n19; of “going viral” and “trending now,” x; on housing market, 227; on leading indicators, 125; medical model and, 21–23, 22f, 292; not heard by everyone in the population, 292; on profiteer, 241–42, 243f; random events affecting, 75; repeats of, with unpredictable timing, 271; self-fulfilling prophecies and, 74; sizes and time frames of, 88–89, 292–93; on technological unemployment, 183–85, 294, 295; with varying contagion rates and recovery rates, 295; volatility and, 5; on wage-price spiral, 258, 259f. See also compartmental models of epidemics; Kermack-McKendrick SIR model; viral narratives
epidemics of narratives: random events affecting, 40, 99–100; recognized since ancient times, 58–60. See also epidemics of economic narratives; viral narratives epidemiology, insights from, xviii, 14, 17, 23–24, 277, 289
Escalas, Jennifer Edson, 77
“Every day in every way I get better and better,” 121
The Evolution of Beauty (Prum), 65

excess profits, 242
excess profits tax, of US during World War I, 249, 265
exogenous shocks to economy, 73, 75–76

expectations, and representativeness heuristic, 66–67
extraordinary popular delusions, 59, 119

Facebook, meme quickly going viral on, 88
fact-checking websites, 85, 96

fair wage-effort hypothesis, 250
fair wage narratives, 249–50
fake news, 84–85, 273
fake wrestling matches, 84–85
Falk, Emily B., 54
false narratives, 95–97

family circle, literature read aloud in, 274
Famous First Bubbles (Garber), 5

famous people: patterns of mentions in books, 24. See also celebrities
Farmer, Roger E. A., 74
farmland: earlier real estate talk centered on, 212; as speculative investment, 213, 214
Farnam, Henry W., 72–73
fear: of automation, 196; brain structures involved in, 56–58; changing economic behavior years after relevant narrative, 109; extended to unrelated events, 67; false narratives and, 95; in financial crises, 55–58; during Great Depression, 109, 127–28, 141; of human irrelevance, 208; identified as cause of Great Depression, 132; of machines replacing jobs, 175; “of fear itself,” 128; Roosevelt’s exhortations about, 128, 129; suicides after crash of 1929 and, 233; technocracy movement leading to, 194. See also panic
Federal Reserve: cause of Great Depression and, 132–33; Consumer Expenditure Survey of, 282; control of inflation and, 262; creation of, 111, 117; J. P. Morgan and, 111, 117–18; warning about speculation in 1929, 126
Federal Reserve Act of 1913, 117
feedback loops: 1930s-style models of, 287; between postponing consumption and job loss, 144–45; of prices in speculative bubbles, 216–17
Feelings in History (MacMullen), 14
Ferguson, Hill, 219
Festinger, Leon, 218
fiat money, 156
fiction, xii, 16. See also novels
films: less luxurious during the Depression, 142; predicting the success of, 41–42
finance, lagging in attention to narratives, 13f
financial advisers, automated, 275
financial crises, 55–56, 86. See also bank runs; world financial crisis of 2007–9
financial panic narrative, 114, 115, 116f; crowd psychology and, 119–20, 120f; frequency of appearance of five major occurrences, 118f; J. P. Morgan and, 117–18; nineteenth-century worldviews and, 116–17; rekindled in 2007 in United Kingdom, 119. See also panic “fire in a crowded theater” narrative, 127, 129
fiscal policy, motivations of, 281
Fisher, Irving, 75–76, 128, 247, 266
Fisher, R. A., 65
Fisherian runaway, 65
flashbulb memory, 80–83, 307n13; of stock market crash of 1929, 233; of stock market crash of 1987, 233
flipping, 223–24
Florida land boom of 1920s, 214, 215, 220–21
flu epidemics. See influenza.fmRI (functional magnetic resonance imaging): of brain activation by analogy and metaphor, 17; of sharing content in form of stories, 54
focused interviews, as research tools, 281
focus groups, 282–84
folklore studies, 15, 16
forecasting. See economic forecasting
forgetting, in epidemic model, x, 25, 296. See also memory
forgetting rates: differences in, 89; effect of slight changes in, 40; lowered by identified personality, 100; lowered by symbols or rituals, 62; lowered by visual detail, 45, 46. See also recovery rates
The Forgotten Depression (Grant), 242, 251
formula stories, 16
Forster, E. M., 181
founding-father story, 15
The Fountainhead (Rand), 50
framing, 66
free markets: forgotten nineteenth-century advocate of, 110; George’s Progress and Poverty on, 111; inflation and, 263; twentieth-century narratives about, xii, 50–51
Free Men and Free Markets (Theobald), 210

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Free Silver movement. See Silverites
Friedman, Irving S., 262, 263
Friedman, Milton, 73, 132–33, 307n3
"From each according to his ability, to each according to his needs,” 102
frugality narratives: American Dream narrative in contradiction to, 155; in Great Depression, 136–37, 142–43, 252; in Japan after 1990, 150
Galbraith, John Kenneth, 233
Gallup, George, 118–19
Gallup Data Collection, 284
gambling culture, and booming stock market, 29
Garber, Peter, 5
Garrett, Geoffrey, 299
GDP data, limited value of, 74–75
GDP growth in US: not successfully forecast, xiv, 301n5. See also economic growth
The General Theory of Employment, Interest, and Money (Keynes), 27
geographic pattern of spread, of economic narratives, 296, 299
George, Henry, 111, 178–79, 188, 209, 310n1
Germany: hyperinflation after World War I, 247, 266; reparations from World War I and, xviii–xviii
Glass, Carter, 191
Gödel, Escher, Bach (Hofstadter), 47
Goetzmann, William, 67
“going viral”: appearing in newspapers around 2009, x; mathematical model of epidemic and, 293. See also viral narratives
gold: fears and rumors about, at start of World War I, 94; mystique about, 157; public perception of value in, 5; seen as safest investment, xii; spiritual significance of, 165; still held by central banks, 156–57
Gold bugs, 163–64
Goldman, William, 41
gold standard: adoption in US, 166; defined, 156; eighteenth-century origins of, 166; end of, 156, 172–73; impact on farmers, 157–58, 161, 163; length of Great Depression and, 132; meaning “the best,” 158. See also bimetallism
Gold Standard Act of 1900, 157, 312n10
gold standard narrative: morality and rectitude represented in, 172; somewhat active today, 156; symbolism in congressional debate and, 165–66; two separate epidemics of, 158–59, 159f, 166; Wizard of Oz and, 171–72, 313n29
Google Ngrams, x, xiii; imperfect for narrative research, 280–81
Google’s “OK Google,” 207
Grais, R. F., 294
grand narrative, 92
Grant, James, 242, 251
Grant, Ulysses S., 157
The Grapes of Wrath (Steinbeck), 131
The Great Crash, 1929 (Galbraith), 233
Great Depression of 1930s, 111–12; angry narratives in, 239; bimetallism epidemic during, 23; blamed on loss of confidence, 130; blamed on “reckless talk” by opinion leaders, 127; confidence narratives in, 114, 122; consumption demand reduced after, 307n3; crowd psychology and suggestibility in understanding of, 120; deportation of Mexican Americans during, 190; depression of 1920–21 and, 243, 251–53; difficulty of cutting wages during, 251–52; Dust Bowl and, 130–31; fair wage narrative during, 250; family morale during, 138–39; fear during, 109, 127–28, 141; flu epidemic of 1918 mirroring trajectory of, 108; frequency of appearance of the term, 133, 134f; frugality and compassion in, 135, 136–37, 140–43, 252; gold standard narrative during, 158–59; labor-saving machinery and, 174; lists of causes created at the time,
Great Depression of 1930s (continued) 129–30; modern theories about causes of, 132–33; modesty narrative during, 135, 136–37, 139, 142–45, 147–48, 150; narratives after 2007–9 crisis and, 95; narratives focused on scarcity during, 129; narratives illuminating causes of, ix–x; not called “Great Depression” at the time, 133–34; not forecast by economists, xiv; ordinary people’s talking about, 90–91; photos providing memory of, 131; prolonged by avoidance of consumption, 139, 142, 144–46; as record-holder of economic downturns, 112; revulsion against excesses of 1920s during, 235–36; robot tax discussed during, 209; seen as stampede or panic, 128; technocracy movement and, 193–94; technological unemployment narrative and, 183, 184; today’s downturns seen through narratives of, 134–35, 264; underconsumption narrative during, 188–90; women’s writing about concerns during, 137–40, 145–46

The Great Illusion (Angell), 95

Great Recession of 1973–75, 112

Great Recession of 1980–82, 112

Great Recession of 2007–9, 112; bank failures as key narratives in, 132; fear about intelligent machines and, 273; fueled by real estate narratives, 212; predicted by few economists, xiv; rapid drop in confidence during, 272

Great Society, 50

Greenspan, Alan, 227

Gresham’s Law, and bimetallism, 169, 313n27

hacker ethic, 7

The Hacker Ethic and the Spirit of the Information Age (Himanen), 7

Hackett, Catherine, 140, 253–54

Halley, Edmund, 124

“Happy Birthday to You” (song), 97–100

Harari, Yuval Noah, 208

Harding, Warren, 244–45

“hard times,” 134

Hard Times: An Oral History of the Great Depression (Terkel), 234

Harris, Sidney J., 263

Harvey, William Hope, 161, 162, 312n10

Hazlitt, Henry, 247

“Heads I win, tails you lose,” 110

health interventions, narrative presentation of, 78

Heathcote, Jonathan, 214

Heffetz, Ori, 144

Hepburn, Katharine, 201

Hero of Alexandria, 175

Hicks, John, 24, 26

Hill, Napoleon, 121–22

Himanen, Pekka, 7

historical databases, 279; of letters and diaries, 285

historical scholarship: compared with historical novel, 79; economics learning from, 78; use of narrative by, 14, 37

Hitler, Adolf, 122, 142, 195

HIV (human immune deficiency virus), 24; coinfective with tuberculosis, 294–95

Hoar, George Frisbie, 178

Hoffa, Jimmy, 260

Hofstadter, Douglas R., 47

Hofstadter, Richard, 36

Holland, François, 151

Holmes, Oliver Wendell, Jr., 127

Holtby, Winifred, 140

homeownership: advantages over renting, 223, 317n18; advertising promotions for, 219–20; American Dream narrative and, 154–55; condominium conversion boom and, 223–24; seen as investment by many buyers, 226–27

home price indexes, 97, 215–16, 222

home price narratives, 215–17; declining by 2012, 227; fueling a speculative boom, 217–18, 222, 223–24
impact on events and, 77; many dimensions of, 79–80
human interest of stories, 32
human tragedy narratives in Great Depression, 137, 141
Hume, David, 58, 71
hyperinflation in Germany after World War I, 247, 266
hypnosis narrative, 122

ICOs (initial coin offerings), 76
identity economics, xxi
“I Have a Dream” speech (King), 153–54
Iliad (Homer), 174, 314n1
immunity to disease, 20, 289
Index of Consumer Sentiment, 119
Industrial Revolution: labor-saving machinery narrative and, 9; narratives about confidence and, 114; real estate narratives and, 212; as term introduced in nineteenth century, 175
inequality: artificial intelligence narrative and, 273; Bitcoin and fear of, 8–9; burgeoning public attention to, 210–11; decline in modesty narrative and, 150; George’s Progress and Poverty on, 111, 178–79; labor-saving machinery and, 178–79, 180; opposition to gold standard and, 166; origins of the boycott and, 240
infectives in an epidemic, 23, 289; declining contagion rate and, 296
inflation: anger about, 239, 245, 247, 263–64, 265–66; central bank role in control of, 261, 262; cost-push inflation, 258–59, 259f, 260; demand-pull inflation, 258; economic growth and, 319n10; economists’ views of, in 1997 study, 263, 264; highest in US from 1973 to 1981, 262; hyperinflation in Germany after World War I, 247, 266; as negative terminology, 172–73; public views of, in 1997 study, 263–64; runaway US inflation of 1970s, 256; sources of evil blamed for, 263, 266;
inflation (continued)
stock market response to decline in, 29;
unusually tame now, 266; wage-price
spiral narrative and, 258–62; during wars,
265–66; after World War I, 243–49, 250;
after World War II, 255–56
Inflation: A World-Wide Disaster (Fried-
man), 262
inflation targeting, 261, 262
influencer marketing, 274–75
influenza: new forms and new epidemics of,
271; pandemic of 1918, 108, 198, 252; SEIR
model of epidemics of, 294
information cascades, 300
information technology: changing
contagion rates and recovery rates,
273–75; communication of stories
through, xviii; history of inventions in,
273; for research in narrative economics,
279. See also Internet; search engines
initial coin offerings (ICOs), 76
initial public offerings (IPOs), flipping of,
224
interest rates: central bank changes of, xvi;
expectations of future rates, 55–56; of
limited value in understanding economic
events, 74–75; no proven record of
forecasting of, 55; wage-price spiral
narrative and, 260
international economic narratives, 110
International Monetary Fund, xiv
International Social Survey Program, 282
Internet: changes in contagion caused
by, 273, 297; cooperation using new
technology and, 7; fear of automation at
beginning of, 205; home price narrative
and, 218; narrative of computer power
launched by, 206; phrase “going viral” in
relation to, x; SIRS model for memes on,
297–98; views or likes on, x. See also
dot-com boom; search engines; social
media
Internet trolls, 67
interviews as research tools, 281–82
inventions, obvious but not adopted,
38–39
investment: fear-related brain circuitry and,
57–58; Keynes on decisions involved in,
xvi, 63–64; labor-saving machinery
narrative and, 209; profitable for some
during World War I, 94. See also stock
market
investment managers, stories told
by, 15
irrational exuberance: exogenous effect on
economy, 76; Greenspan on 1996 stock
market and, 227
Irrational Exuberance (Shiller), 29
Isaacson, Walter, 208
IS-LM model, 24–26, 27f
Jackendoff, Ray, 35
James, William, 121
Japan: “lost decades” of 1990s and beyond,
95, 150
Jenkins, Gwilym, 295
Jevons, William Stanley, 73–74
jigsaw puzzle craze, 148–49
Jobs, Steve, 208–9
Johnson, Lyndon, 50, 202
Johnson, Mark, 17
Jones, John P., 165
Jung, Carl, 15
Kahneman, Daniel, 66
Kasparov, Garry, 36
Katona, George, 66, 119
Katz, Elihu, 297
kayfabe, 84
keep-up-with-the-Joneses narrative, 136
Kempton, Murray, 230–31
Kendall, David G., 296
Kendall, Patricia L., 281
Kennedy, John F., 236, 307n13
Kennedy, Joseph, 236–37
Kennedy, Robert F., 260
Kermack-McKendrick SIR model, 289–93, 291f; chaotic solutions of, 299–300; investment decisions and, 299; still workable for idea epidemics, 298; variations on, 293–98. See also compartmental models of epidemics

Keynes, John Maynard: animal spirits and, 138; “beauty contest” metaphor of, 63–64; business confidence and, xvi; consequences of Versailles treaty and, xvii–xviii, 26; current consumption and current income according to, 307n3; gold standard narrative and, 172, 173; IS–LM model and, 25–26; on stimulus leading to economic boom, 27–28

Kim, Dasol, 67
King, Coretta Scott, 153
King, Martin Luther, Jr., 153–54
Kingsley, Grace, 142
Kiplinger, Willard Monroe, 130, 132
Klages, Mary, 16
Klein, Melanie, 15
Koopmans, Tjalling, xv
Kranton, Rachel, xx
Kristol, Irving, xvi–xvii
Krock, Arthur, 90–91
Kulik, James, 307n13
Kydland, Finn E., 24

labor-saving machinery narrative, 174–76, 175f; counternarrative to, 178; depression of 1873–79 and, 174, 176–78; depression of 1893–97 and, 174, 179–81; early history of, 174–76; economic decisions affected by, 209; economic effects of narrative itself, 211; fear during Great Depression and, 109; increasingly vivid before 1930, 182–86; office workplace and, 186; opportunity during dot-com boom and, 109; robots and, 181–82; underconsumption or overproduction theory and, 187–89, 191–92; unemployment and, xiv, 9, 130, 177–81, 187–88, 191–92. See also technological unemployment narrative

labor unions: associated by public with organized crime, 260; automation and, 200, 202; boycotts used by, 241; trends in public support for, 258–59, 266, 320n2; wage cuts in depression of 1920–21 and, 249, 251; wage-price spiral and, 258–60, 261, 263, 264

Lacoste, Jean René, 62, 63
Laffer, Art, 42, 44–45
Laffler curve narrative, xviii, 24, 42–47, 48, 51, 52; exogenous effect on economy, 76; impact on output and prices, 48; in supply-side economics constellation, 47–48; two epidemics in appearance of, 42, 43f

laissez-faire narrative, in second half of twentieth century, 50

Lakoff, George, 17

land: federal regulation of interstate sales of, 317n15; home prices and, 215, 216; narrative about its scarcity and value, 212; not depreciating like the home, 215; as percentage of home's value, 214, 317n5; sold as investment in undeveloped property, 220–21

land bubbles, 213

land speculation, 213; Florida boom of 1920s, 214, 215, 220–21; marketing of undeveloped land before Great Depression and, 220

Lang, Fritz, 203
Lange, Dorothea, 131
Laughlin, J. Laurence, 312n10

The Law of Success in 16 Lessons (Hill), 121–22

Lazarsfeld, Paul F., 297

leading indicators: in economic forecasting, 125, 309n10; epidemic models instead of search for, 295; narratives causing changes in, 276; underlying human behavior and, xv
learning, narrative-centered, 77–78
Le Bon, Gustave, 59, 119
leveraged buyouts, 47
Levi Strauss Company, 148
libertarianism, and hacker ethic, 7
Liebhold, Peter, 44
Lincoln, Abraham, 101
Lindgren, Astrid, 49
Linglong’s Dingdong, 207
linguistics and narrative, 16–17, 94–95
Linux operating system, 7
listening as a research method, 281
literary studies and narrative, 15–16, 286
Livermore, Shaw, ix
Loftus, Elizabeth F., 78
logos on clothing and shoes, 62–63; on blue jeans, 148
Long, Elisa F., 295
Lopokova, Lydia, 26
Lorayne, Harry, 46–47
“lost decade” story, 95, 150
Love Is a Story (Sternberg), 79–80
Lovejoy, E. P., 14
Lubell, Samuel, 200
Lucas, George, 203
Luddite event in 1811, 174, 176
Luddite narrative, 9, 185; in 1930s, 186–87
Lujan, Sterlin, 6

Machill, Marcel, 77
machine learning, 207–8, 211
machines replacing jobs. See labor-saving machinery narrative
“The Machine Stops” (Forster), 181
Mackay, Charles, 59, 119
MacMullen, Ramsay, 14
Malabre, Alfred L., Jr., 202
Mallon, Mary, 20
Mann, Dorothea Lawrence, 60
Marden, Orison Swett, 122
marketers: contagion rate engineered by, 60; lowering the forgetting rate, 62;

profiting from narratives, xiii, 62;
recurrence of narratives due to, 109–10
marketing: with accelerated analytics, 20;
appeals to patriotism in, 155; background music and, 67; bizarre mental images in, 46; book jackets and, 60–61; contagion of economic narratives and, 60–63, 297; detested by many consumers, 62; focus group methods developed for, 283; logos and, 62–63, 148; self-referencing in, 77; social media used for, 274–75; of “the news,” 61–62
Marx, Groucho, 133
Marx, Karl, 102
master narrative, 92
master plots in fiction, 16
maximize shareholder value, 47–48
May, John Allan, 38
McCall, Samuel W., 168
McCormick, Anne O’Hare, 140, 143
McGinn, Daniel, 217–18
McKinley, William, 163, 164, 171, 313n29
McQuiggan, Scott W., 77–78
Meaney, George, 202
“Measurement without Theory” (Koopmans), xv
Meeker, Royal, 245
Mellon, Andrew, 44
Meloney, Marie, 220
memes, 60, 88
Memoirs of Extraordinary Popular Delusions (Mackay), 59, 119
memory: aided by rituals and symbols, 62; aided by visual stimuli, 45, 46–47; collective, 60; contagion of narratives and, 252; fear-related brain circuitry and, 57–58; flashbulb memory, 80–83, 233, 307n13; source monitoring in, 84, 307n21. See also forgetting, in epidemic model
Men and Machines (Chase), 185
mentors for young people, 274
Merrill, Charles, 167

For general queries, contact webmaster@press.princeton.edu
Merton, Robert K., 73, 198, 281
metanarrative, 92
metaphors, 16, 17; of economy as sick or healthy, 79
meteorology narratives, 123
Metropolis (film), 203
Mexican Americans, deported during Great Depression, 190
Michel, Jean-Baptiste, 24
Milosz, Czeslaw, 57
Mitchell, Wesley C., 125, 309n10
Mitterrand, Francois, 42
“modern monetary theory,” 42
Modern Times (film), 195
modesty narrative: absent from George and Veblen works, 310n1; in Japanese “lost decades,” 150; present decline in, 272
modesty narrative of Great Depression: bicycle craze and, 143; blue jeans and, 147–48; conspicuous consumption and, 135, 136–37, 139, 142–45; decline in, 150
Modigliani, Franco, 301n13
Mokyr, Joel, 71
Moley, Raymond, 114
Monetary History of the United States (Friedman and Schwartz), 73, 132–33
monetary policy: causal impact on aggregate economy, 73; studies of narratives to infer motivations of, 281; wage-price spiral narrative and, 261
monetary system: inflation and, 262; typical American’s confusion about, 170
monetary theory: invoked by bimetallism and Bitcoin, 22; “modern monetary theory” narrative, 42
money narratives, 173. See also Bitcoin narrative; gold standard narrative
money supply: gold discoveries of 1897 to 1914, 73; Great Depression and, 132–33
moral dimensions of economic narratives, 80; abstract economic forces and, xvii; American Dream narrative and, 155; anger at business and, 239; annoyance with boycotts and, 241; concerns about labor unions and, 258; databases of sermons relevant to, 284–85; frugality during Great Depression and, 143; opposing pairs of narrative constellations and, 113; Roosevelt’s Depression fireside chat and, 129, 278; about stock market crash of 1929, 235–36; wage-price spiral narrative and, 261–62, 266
morality in historical narrative, 37
Morgan, J. P., 111, 115, 117–18
Morson, Gary Saul, 16
Mullen, Thomas, 128
Muller, Jerry Z., 75, 306n5
multiplier-accelerator model, 24–25, 27–28, 27f, 303n7
music: brain structure and, 53, 54; narrative and, 35; songs that are one-hit wonders, 41–42
Music, Language and the Brain (Patel), 35
music market of sociology experiment, 39–40
mutation in evolutionary theory, 64
mutation of diseases, 108
mutation of economic narratives, 108–9; by attaching new celebrity, 102, 108–9; on cryptocurrencies, 76; to more contagious forms, 31, 40; within narrative constellations, 86, 107; randomness in, 31, 40; of recurrent narratives, 107, 109–10, 238; self-fulfilling prophecies derived from, 74; of technological unemployment narrative, 196, 199
mutation of narratives: “Happy Birthday to You” and, 98–99; from hypnosis to autosuggestion, 122
Nakamoto, Satoshi, 4, 7–8, 108–9, 162, 193, 302n3, 302n8
names attached to narratives, 94–95
narrative economics: concept of, xi, 3; consilience and, 12; earlier use of the phrase, xi. See also economic narratives
narrative economics research: artificial intelligence in, 276; databases to be used in, 279, 281–82, 284–85; data collection in, 276, 279–86; economic theory and, 277–79; exact methods with humanistic approach in, 271–72; future of, 275–77; quantitative methods in, 279; remaining nonpartisan in, 278–79; textual analysis in, 279, 287; tracking and quantifying narratives in, 286–87

narrative psychology, 15, 65–67, 78, 287

narratives: academic disciplines attending to, 12, 13f; becoming economic narratives, 74; central to thinking and motivation, 31–32; conspiracy theories in, 35–36; defined, xi; disrupted by brain injury, 65–66; distinguishing humans from animals, 34–35; effective wording and delivery of, 271; historical, 37; hormones of listener and, 54–55; as human constructs, 65; names attached to, 94–95; norms of politeness in transmission of, 35; originating with one or a few people, 71–72; as particular form of story, 36; as scripts or social norms, 37–38, 74, 77; social change and, 32–33; universality of, 33–35. See also constellations of narratives; contagion of narratives; economic narratives; mutation of narratives; stories; viral narratives

National Association of Realtors, 216, 219, 220

National Bureau of Economic Research (NBER): biggest economic events in US since 1854 defined by, 111–12; chronicle of business cycles, 110; working paper database, 279

National Industrial Recovery Act, 132, 189, 252

“near-rational,” 300

network models, 296

neurolinguistics and narrative, 16–17; synonyms and, 94–95

neuroscience and narrative: hormones involved in, 54–55; research methods and, 287. See also brain

Newcomb, Anthony, 35

“No Deal,” coined by Stuart Chase, 185

The New Financial Order (Shiller), 38

news media: creative during major stock market corrections, 75; economic narratives spread through, 3, 21; improving retention with narrative presentation, 77; international economic narratives and, 110; marketing-driven, 61–62; in modified SIR model, 297; reminding public on anniversaries of events, 76; searching for words and phrases in, x

Nixon, Richard, 173

normalcy, 244, 252

North, Douglass, 14

Northern Rock bank run in 2007, 119, 135

novels: classical symphony as, 35; understanding human experience and, 16. See also fiction

Noyes, Alexander Dana, 127, 164, 231

Nudge (Thaler and Sunstein), 278

nudge units, 277–78

NVIDIA Corporation, 20

O’Barr, William M., 15

Occupy Wall Street protest, 8, 225

office workplace: automation of, 204; labor-saving machinery narrative and, 186

Ohanian, Lee E., 132

oil embargo of 1973, 256

one-hit wonders, 41–42

Only Yesterday (Allen), ix–xi, 139

organ donation, narrative presentation of, 78

overlapping generations model, 24–25, 27f, 303n8

overproduction or underconsumption theory, 187–92
“Ownership Society” (Bush reelection slogan), 155
oxytocin, 54
Oz: The Great and Powerful (film), 172

Palme, Olof, 48–49
panic: at beginning of World War I, 93–94; creation of Federal Reserve and, 117; in financial crisis, 55–56, 86; following complacency, 55–56; Great Depression seen as, 128; inflation in 1970s and, 262; stock prices and, 228. See also bank runs; fear; financial panic narrative
Panic of 1907, 94, 111, 115, 117, 118f
Part of Our Time (Kempton), 230–31
Patel, Aniruddh, 35
Pathways Back to Prosperity (Baker), 210

Patriotic appeal of a narrative, 101, 102–3
Paul, Ron, 156
Pavlov, Ivan P., 56
Pearl Harbor attack, memories of hearing about, 81–82
Penfield, Wilder, 53–54
perennial narratives, 107–8; nine major examples of, 113, 266–67 (see also specific examples); as works in progress, 276
permanent-income hypothesis, 307n3
“permanently high plateau,” 75–76
phantasies of Melanie Klein, 15
The Philosophy of Honest Poverty, 150
phishing equilibrium, 61
phools, 61, 62
Piketty, Thomas, 150, 210–11
Piore, Michael, 281
Plath, Robert, 38, 39
Plato, 34

Policy: formulating with knowledge of narratives, 3, 287. See also monetary policy
policymakers: creating and disseminating counternarratives, 278; narrative studies to infer motivations of, 281, 321n14
poliomyelitis enterovirus epidemic, 295–96
Pollack, Andrew, 204
Polletta, Francesca, 32
Pomperipossa in the World of Money (Lindgren), 49
Ponzi, Charles, 220–21
Ponzi scheme, 220
populism: inflation after World War I and, 245; opposition to gold standard and, 166
portfolio insurance, 93
post-traumatic stress disorder (PTSD), 57
“postwar,” 242–43
Pound, John, 298
poverty: decreasing basic-needs charity in today’s US, 272; Depression-era attitudes toward, 143; Dust Bowl and, 131; nineteenth-century moral views of, 117; technological advances creating, 178
poverty-chic culture, 143, 148, 149
power age, 183
predicting economic events. See economic forecasting
Prescott, Edward C., 24
price controls, in US after World War II, 255
price per acre, references to, 214
price setting: interviews of executives about, 281. See also wage-price spiral narrative
prison inmates, telling stories, 15
professional narratives, xiii
profiteer narrative, 241–43, 243f, 246–49; abrupt end of 1920–21 depression and, 250–51; falling consumer prices and, 243–44; inflation after World War I and, 245, 265. See also excess profits
profits, corporate: taxes on, 45, 48; viral narratives associated with, 47–48
Progress and Poverty (George), 111, 178–79, 188, 209, 310n1
property taxes, taxpayer revolt focused on, 50
Proposition 13, 50
Propp, Vladimir, 16
ProQuest News & Newspapers, x
Proudhon, Pierre-Joseph, 6
prudent person rule, 37
Prum, Richard O., 65
psychoanalysis and narrative, 15, 16, 280
Psychological Economics (Katona), 66
psychological impact of opinion leaders, 127
Psychologie des foules (The Crowd) (Le Bon), 59, 119
psychology and narrative, 15, 65–67, 78, 287
The Psychology of Suggestion (Sidis), 121
PTSD (post-traumatic stress disorder), 57
Public Opinion Research Archive, 284
purchasing power theory of wages, 188
push a button, 179, 200
Putin, Vladimir, 103
qualitative research, 281
quarantines, 19–20
quasi-controlled experiments, 73
questionnaire surveys, 285–86
Rand, Ayn, 50
random events with major effects, 40, 75, 99–100
randomness of which narratives go viral, 31, 40, 64–65, 286
random walk theory of speculative prices, xiii
rational expectations models, 277, 295, 301n13
Reagan, Ronald, xii, 42, 51–52, 153
Reagan administration, tax cuts by, 48, 51
real business cycle model, 24–25, 27f
real estate boom in 2000s: automation narratives and, 205; Trump University and, 226. See also housing booms
real estate narratives, 212. See also home price narratives
real estate speculation: in second half of twentieth century, 213. See also home price narratives
Rebel Without a Cause (film), 148
recessions: in 1949, 256, 264; in 1950s and 1960s, 199, 200–201, 264; in 1957–58, 201, 264; in 1973–75, 239, 256–57; in 1980 and 1981–82, 204; in 2001, ended after terrorist attack, 82–83, 307n17; biggest in US since 1973, 112; causes listed by economic historians, 112; consumer confidence narrative and, 115; economists’ reluctance to mention narratives underlying, 276; narrative infecting fraction of population and, 29; as narratives in themselves, 112; not successfully forecast, xiv, 301n6; popular belief in periodic nature of, 124–25; popular stories affecting, xii; reasons for hesitating to spend during, 75; self-fulfilling prophecy in forecasts of, 123–24, 125
reciprocity, human patterns of, 36
recovery in medical model, 18, 20–21, 23, 289; economic analogy to, 21
recovery rates: differences in, 89; difficulty of predicting, 41; models from epidemiology and, 20, 21, 23–24, 290; new technology leading to changes in, 273, 275; varying through time, 295. See also forgetting rates
recurrence of narratives, 107–8, 109–10, 238
redistribution proposals, 209–10
regulation: supply-side economics and, 48; twentieth-century reaction against, xii, 48, 50, 51
religious studies, narrative approaches to, 15
repetition of economic fluctuations, 124–25
repetition of narratives: contagion and, 97–100; meteorology and, 123
representativeness heuristic, 66–67
Republic (Plato), 34
Reserve Prime Fund, 135
retirement: homeownership as saving for, 219; ordinary people in nineteenth century and, 116
Rhys-Williams, Juliet, 210

For general queries, contact webmaster@press.princeton.edu
Richards, George, 265–66
Riefenstahl, Leni, 122
risk assessment, by primitive brain system, 67
risk taking: entrepreneurial narratives and, 52; excessive complacency about, 55–56
Ritter, Jay, 224
rituals, reminding people of the narrative, 62, 303n9
Roaring Twenties, ix, 133, 135, 235
Robbins, Lionel, 111–12
Robey, Ralph, 125
robo-advisers, 275
robots: artificial intelligence and, 196; broad use of the term, 192; as cause of Great Depression, 191; in Chaplin's Modern Times, 195; coinage of the term, 181–82; enormous spike in mentions during early 1980s, 202–3; fear of, 186; Great Recession of 2007–9 and, 273; labor-saving machinery narrative and, 181–82; military uses planned for, 195; in movies, 203–4; product line failing in 1980s, 203; technological unemployment narrative and, 186. See also artificial intelligence narrative; automation narrative
robot tax, 209
Rockefeller, John D., 236
Rollaboard, 38, 39
Romer, Christina, 307n3
Roosevelt, Franklin: Buy Now Campaign of, 255; Depression fireside chat, 129, 278; "fear of fear itself" and, 128; National Industrial Recovery Act and, 189, 252; running against Hoover in 1932, 90, 91, 188–89
Roosevelt administration: codes of fair competition and, 132; confidence narratives and, 114
Roper, Elmo, 196–97
Ross, Andrew, 7
Roth, Benjamin, 141
RSA algorithm, 9–10
Rubik, Ernő, 47
Rubik's Cube, 47, 52
Rumsfeld, Donald, 44
R.U.R.: Rossum's Universal Robots (Čapek), 181–82, 196
Ryōkan, 150
Sadow, Bernard, 38
Saïz, Albert, 222
Salganik, Matthew J., 39, 300
salon, literature read aloud in, 274
Samuelson, Paul A., 24, 27–28, 303n8
Sandow, Eugen, 122
Sartre, Jean-Paul, 31
Saver, Jeffrey, 65–66
saving: in early twentieth century, 219; in eighteenth and nineteenth centuries, 116–17; homeownership and, 219–20
Schank, Roger C., 37
Schapiro, Morton, 16
schizophrenia, narrative in, 66
Schwartz, Anna J., 73, 132–33
Scott, Howard, 193, 194
scripts, 37–38; bank runs of 1893 and, 164–65; of Bush's narrative after terrorist attacks, 83; economic narratives involving, 74, 77
search engines, x; changes in contagion caused by, 273; improvements needed for narrative economics research, 280–81
searching digitized data: companies offering intelligent searches, 287; differing meanings of words and phrases in, 93; of public documents and the media, 287. See also databases for studying narratives; textual analysis
secular stagnation: fears of, after 2007–9 financial crisis, 95; narratives in thinking about, 71
SEIHFR model, 294
SEIR model, 294; chaotic variations of, 299, 323n21
self-censorship of narratives, 115
self-fulfilling prophecies in economics, 73–74, 123–24, 125; optimistic stories after 1948 and, 198; temporary hardships creating pessimism and, 209

self-made man narrative, xii

self-referencing in marketing, 77

semantic search, 287

September 11, 2001, terrorist attacks, 82–83, 284

sexual selection, 64–65

Sharpe, William, 275

Shell, Karl, 74

Shiller, Robert, xviii, 29, 38, 61, 64, 67, 216, 285, 298, 301n13

Sidis, Boris, 121

Silber, William, 94

Silverites, 158, 159, 160, 162–63, 164, 167; *Wizard of Oz* and, 171, 313n29

Simonides, 46

singularity, 199, 204–5, 207

Siri (Apple), 8, 206–7, 287

SIR model. See *Kermack-McKendrick SIR model*

SIRS model, 294, 322n4; for Internet memes, 297–98

sit-ins, 32–33

*Six Cylinder Love* (film), 144

size of an epidemic, 88–89, 292–93

slavery, and Civil War, 33

Slichter, Sumner H., 184–85

Sloss, Louis, 168–69

Smith, Adam, 44, 304n6

Smith, Al, 191

Snowden, Philip, 183–84

social change, and contagion of narratives, 32–33

social comparison: narratives about home prices and, 218, 220; narratives about stock market bubbles and, 228

social media: changes in contagion caused by, 273, 297; complicating geographic models of spread, 296; economic narratives spread through, xviii, 3, 21;

home price narrative and, 218;

reconstructing arc of narratives from, xiii; recurrent narratives and, 109–10;

research using data from, 287. See also Internet social media marketing, 274–75

social norms, 37. See also *scripts*

social sciences: controlled experiments in, 78; study of popular narratives in, 15

sociology: economics learning from, 78; narratives central to social change and, 32–33; storytelling and, 15

Socrates, 34

*Something to Look Forward To* (Rhys-Williams), 210

source monitoring, 84, 307n21

S&P/CoreLogic/Case-Shiller home price index, 216, 222

speculative bubbles: feedback loop of prices in, 216–17; information cascades and, 300; resembling sexual selection outcomes in animals, 65; valuation of Bitcoin seen as, 4, 5, 7

speculative investments: flipping and, 223–24; real estate as simplest of, 221; in undeveloped land, 220–21

speculative markets: before crash of 1929, ix, 125–26, 231; Keynes’s explanation of, 63–64

spending: boycott narrative and, 240, 254; hesitation during a recession, 75;

postponed after World War I, 245–46, 249;

postponed after World War II, 256;

postponed during 1957–58 recession, 264; postponed during Great Depression, 129, 253–55; postponed in response to rising prices, 239; reduced by fear of automation, 201; reduced in 1973–75 recession, 256–57; revived after depression of 1920–21, 251; Roosevelt’s Depression fireside chat and, 278; women making most decisions in 1920s and 1930s, 254. See also boycott narrative;
consumer confidence narrative; consumption
Sproul, Allan, 262
Star Wars trilogy (Lucas), 203
Steinbeck, John, 131
Sternberg, Robert, 79–80
Steve Jobs (Isaacson), 208
Stewart, William Morris, 166
stimulus. See economic stimulus
stock market: automated advisers for, 275; biggest expansion in US history, 1974–2000, 206; conversations and news media during corrections, 75; Keynes's “beauty contest” metaphor and, 63; prices as indicator of public confidence, 129, 228; questionnaire surveys of investors, 285; speculative bubbles in, 216–17; survey of investors’ decision-making, 298–99; World War I and, 93–94, 283; World War II and, 94, 283, 308n6
stock market boom in 1920s: baffling to economists, 230; crowd psychology and, 119; Groucho Marx’s take on, 133; ticker projector and, 228–29
stock market boom in 1990s, 109, 206
stock market bubbles, 228; popping in 2000, 29, 83
stock market crash narrative, 228–29, 232–33, 232f; exaggerated assessments of risk and, 67; in Great Depression, 252; in Great Recession of 2007–9, 272; idea of divine punishment and, 236; lingering today, 238
stock market crash of 1929: American Dream narrative and, 231; battle between Wall Street and the Fed prior to, 126; blamed on surplus of goods produced by technology, 186, 192; boom and crash going viral after, 229; consumption demand falling immediately after, 307n3; disillusionment with optimistic predictions and, 126–28; economists’ puzzlement over, 229–30; evidence of danger prior to, 231–32; Fisher’s “permanently high plateau” phrase and, 75–76; high price-earnings ratio prior to, 231–32; moral narratives about, 235–36; narrative of human folly associated with, 228; narratives in 1920s and, ix–x, 72; overproduction or underconsumption theory and, 188; references to 1920–21 depression during, 252–53; rising unemployment prior to, 185–86; shoeshine boy narrative and, 236–37; “stock market crash” reminding us of, 17; suicide narratives associated with, 233–35
stock market crash of 1987: discussion of portfolio insurance and, 93; learned about by word of mouth, 89; narrative compared to 1929, 235; narrative of, 232f, 233; news media reminding public about, 76
stock price indexes: declining from 1929 to 1932, 230; public attention to, beginning in 1920s and 1930s, 97; public fascination with, 229
stories: basic structures of, 15–16; brain structure and, 54; emotion revealed in, 79; narrative as particular form of, 36; preference to share information in form of, 54; revealing personal values, 15; spread if we think others will spread them further, 63, 64; thinking in analogies and, 17. See also narratives
Stowe, Harriet Beecher, 33
structuralist literary theory, 16
Success Fundamentals (Marden), 122
suggestibility, 119–22, 120f; of less consumption during the Depression, 142
suicides after crash of 1929, 233–35
suitcases with wheels, 38–39
Sullivan, Mark, 172
sumptuary laws, 136
sunspots, 73–74
Sunstein, Cass, 277–78
super-spreaders, 20, 294
supply-side economics narratives, 48–52
surplus of goods produced by technology, 186, 192, 210
survey research, 285–86
susceptibles in epidemic, 20, 23, 289–90, 291f, 292, 294
Swing Riots in 1830, 174, 176
symbols, reminding people of the narrative, 62
synonyms, different connotations of, 94–95
talk shows, economic narratives spread through, 21
Talleyrand, 172
tax cuts: Laffer curve and, 42, 48, 51; of Reagan administration, 48, 51; supply-side economics and, 48–52
taxes: on corporate profits, 45, 48; Henry George’s single tax on land, 209; narratives of people paying more than 100%, 49; Rand’s Atlas Shrugged and, 50; reducing incentive to earn and create jobs, 42, 44; on Social Security benefits combined with Medicare surtax, 305n20
taxpayer revolt around 1978, 50
tax rates, of limited value in understanding economic events, 74–75
Taylor, Zachary, 110
teach-in, 33
technocracy, 192–94
technological unemployment narrative, 174, 175f, 183–86; automation with broader scope than, 200; concentration of business and, 190; during depressions, 176; economic effects of narrative itself, 211; epidemic models for, 294, 295; in Great Depression, 252; mutating after World War II, 196, 199; not strong in 1920s, 186–87; in run-up to World War II, 194–95; saturating the population in 1930s, 194; underconsumption and, 189. See also automation narrative; labor-saving machinery narrative
“technology taking over our lives” narrative, 8–9
Temen, Peter, 133, 172
Terkel, Studs, 234
The Terminator (film), 203
textual analysis, 279, 287. See also databases for studying narratives; searching digitized data
Thaler, Richard, 277–78
Thatcher, Margaret, 42, 51
Theobald, Robert, 210
theory of mind, 63–64
The Theory of the Leisure Class (Veblen), 310n1
“They say that . . . ,” 92
Think and Grow Rich (Hill), 122
Think Big and Kick Ass in Business and Life (Trump with Zanker), 150
Thompson, Anne Kinsella, 226, 285
ticker projector, 228–29
time and motion studies, 184
Tmall Genie (Alibaba), 8, 207
Tobias, Ronald B., 16
Tracy, Spencer, 201
traffic light, replacing policemen, 182–83
Trans-Lux Movie Ticker, 228–29
“trending now,” 1
trickle-down economics, 44
Triumph of the Will (film), 122
Trohan, Walter, 51
Trulia, 218
Trump, Donald J.: bigly and yuge coined by, 244; downplaying modesty and compassion, 150; gold standard and, 156, 173; modeling ostentatious living, 272; narrative of, xii, 225–26
Trump administration, less generosity toward the poor during, 272
Trump supporters, resembling Silverites, 162–63
Trump University, 226
trust, in business dealings, 101
trusts, public anger about, 181
tulip mania in 1630s, 4, 5
Tversky, Amos, 66
Twain, Mark, 124
Twitter: meme quickly going viral on, 88; retweeting of mostly false stories on, 96–97
Typhoid Mary, 20
tyranny of metrics, 75, 306n5

Uchitelle, Louis, 150
Uncharted: Big Data as a Lens on Human Culture (Aiden and Michel), 24
Uncle Tom's Cabin (Stowe), 33
underconsumption theory, 187–92
Understanding the Process of Economic Change (North), 14
unemployment: artificial intelligence narrative and, 273; automation and, 199–200, 204; constant reminders of possibility of, 89; crime and, 141, 142; in depression during 1890s, 111; employee morale and, 147; gold standard and, 172; in Great Depression of 1930s, xiv, 111, 132, 141, 142, 143, 146–47, 172, 187, 189–91, 193; Kiplinger’s 1930 list of causes of, 130, 132; labor-saving machinery narrative and, xiv, 9, 130, 177–81, 187–88, 191–92; narratives focused on massive occurrence of, 129–31; Nazi Party’s rise in Germany and, 195; robotics and, 209; technology raising specter of, 8–9, 130; underconsumption theory and, 187–91. See also labor-saving machinery narrative; technological unemployment narrative
unemployment rate, first measurements by US government, 131, 184, 185
unfair behavior, human eagerness to punish, 36
universal basic income, 209–10
universals: anthropologists’ study of, 33–35; social comparison as, 218
Valenti, Jack, 41
Van Evera, Stephen, 95
Vartanian, Oshin, 17
Veblen, Thorstein, 154, 193, 310n1
Versailles treaty, Keynes on consequences of, xvii–xviii, 26
viral diseases. See Ebola epidemics; influenza; Kermack-McKendrick SIR model
viral narratives: affecting economic activities without regard to truth, 95–96; American Dream as, 151–54, 152f; appearance of term “going viral,” x; about bimetallism, 170, 172; about boycotts, 241; causal elements of, 72; choice of celebrities and, 100; confluence of, 29; creators of, 60; experimental evidence relevant to, 39–40; of “fire in a crowded theater,” 127; about gold standard, 168, 172; about hypnosis, 122; about labor-saving machines, 195; mathematical model of epidemic and, 293; needing personality and story, xii; news publishers’ financial success and, 61; about office automation, 204; randomness of which stories become, 31, 40, 64–65, 286; Roosevelt’s quote about fear, 128; sit-ins and, 32–33; about stock market boom and crash, 229; about technological unemployment, 185; about wage-price spiral, 259–60
visual images: changed in mutated narrative, 108; memory aided by, 45, 46–47; power of Laffer curve narrative and, 45, 48
vivid mental images, jury members’ response to, 78
volatility, and epidemic quality of economic narratives, 5
Vosoughi, Soroush, 96–97
wage cuts: anger at business over, 239; criticized during Great Depression, 251–52; National Industrial Recovery Act and, 252
wage lag hypothesis, 264
wage-price spiral narrative, 258–62, 259f, 263, 264, 266
wages: interviews of managers on decisions about, 281; of limited value in understanding economic events, 74–75; National Recovery Administration and, 189; purchasing power theory of, 188. See also labor unions
Wagner, Robert, 184
Walker, Edmond, 250
Wall Street Journal “Mansion” section, 224–25
Wanniski, Jude, 44–45
war metaphors, 17
Warner/Chappell Music, 98
wars: inflation during, 265–66. See also Civil War, US; World War I; World War II
war to end all wars, 242
Washington, George, 100–101, 102, 117, 177
Washington Mutual (WaMu) bank run, 135
Watson, IBM computer on Jeopardy, 207
The Way the World Works (Wanniski), 44 “We are the 99%” protests of 2011, 8, 225
weather forecasting, 123–25
Weems, Mason Locke, 100
Weiman, Rita, 139
Welch, Ivo, 300
welfare mother, narrative on, 49–50
When Washington Shut Down Wall Street (Silber), 94
Whewell, William, 12
White, Hayden, 37
Whitman, Walt, 165
Wicked (Broadway musical), 172
Wicked (Maguire), 172
Wikipedia, 7
Wikiquotes, 102
wikis, 7
Williams, James D., 147
Wilson, E. O., 12
Windmill, Alexander, 59
Wizard of Oz (film), 171–72
Wolman, Leo, 241
The Wonderful Wizard of Oz (Baum), 171–72, 313n29
Woolf, Virginia, 26
word of mouth: cultural change completed by, 297; cultural changes in use of, 274; investment decisions and, 298–99; in learning about stock market crash of 1987, 89; popular stories spread through, x, 3
word-of-mouth marketing, 15, 297
world financial crisis of 2007–9: advertisements for homeownership around time of, 220; automation narratives and, 205; housing bubble that collapsed during, 154, 155, 217, 222–23, 226, 227; interpreted as harbinger of “lost decade,” 95; predicted by few economists, xiv; risk taking by banks ten years later, 55–56; seen through Great Depression narrative, 134–35; stock market expansion following, 206; thousands of boycotts during, 257
World War I: “Cult of the Offensive” false narrative and, 95; depression following, 197; excess profits tax imposed by US during, 249, 265; Harding’s appeal for normalcy and, 244–45; Hitler’s appeal in aftermath of, 122; inflation during, 243–49; monetary policy and, 73; profiteer narrative and, 241–43; stock exchanges closed at beginning of, 93–94
World War II: Keynes on Versailles treaty and, xvii–xviii, 26; meaning of “postwar” and, 242; modesty narrative during, 137; monetary policy and, 73; optimistic narratives after, 198; Pearl Harbor attack
and, 81–82; positive market reaction to
beginning of, 94, 308n6; technological
unemployment narrative and, 194–95,
196; “victory vacations” shortly after,
198; worldwide depression preceding,
112
wrestling matches, fake, 84–85

Xi Jinping, 151

Yandex's Alice, 207
Yellen, Janet L., 250, 300
Young, Kay, 65–66
Young, Warren, 25
“Your World in 90 Seconds,” 103
Zak, Paul J., 54
Zhao, Laijun, 297
Zillow, 218