

# RESEARCH REPORTS

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## RESEARCH REPORTS

AIER publishes over 100 articles per month that are distributed in digital form. Research Reports contains Business Conditions Monthly plus 10 of the most representative, chosen here for popularity, variety, and relevance. These articles are often reprinted in venues around the web, including *Seeking Alpha*, *Intellectual Takeout*, *Mises Brasil*, and dozens of other outlets. To read all of them, go to

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Dear Supporters,

We are happy to introduce Peter C. Earle as the author and researcher for Business Conditions Monthly. Pete is an economist who joined AIER in 2018. Prior to that he spent over 20 years as a trader and analyst at a number of securities firms and hedge funds in the New York metropolitan area. We are excited to have him leading the research and analysis behind Business Conditions Monthly.

Going forward, Business Conditions Monthly will be utilizing our Bloomberg subscription to produce more insightful charts and analysis. In addition, we will be providing full-month data to give you a more comprehensive and up-to-date view of the latest economic trends and business conditions. As a result, Research Reports will be sent on a different schedule than previously, so you will notice it arrives in your mailbox a couple weeks later than previously.

Thank you for your continued support, and we look forward to bringing you Research Reports and Business Conditions Monthly in the coming months and years.

Sincerely,

**AIER**



# BUSINESS CONDITIONS MONTHLY

Peter C. Earle

RESEARCH FACULTY

**A** IER Leading Indicators rose to 58 in January 2023 from 21 in December 2022, an increase to just over the neutral level of 50. This breaks a seven month trend below the neutral threshold. While numerically this signals business expansion, the internals of the twelve economic indicators were dominated by insubstantial month-to-month changes. Three economic indicators registered significant positive moves over December: initial jobless claims, debit balances in margin accounts, and the 10-year to 1-year US Treasury spread. Heavy truck unit sales fell substantially. With three components of the Leading Indicator index rising significantly, one falling significantly, and the remaining eight with small, insignificant changes over the previous month, the bias remains largely neutral.

Our Roughly Coincident Indicators fell to 50 from 83 in January 2023, with all six component indices in neutral trends over their December readings. Nonfarm payrolls, industrial production, personal income (less transfer payments), the labor participation rate, consumer confidence, and manufacturing and trade sales changed negligibly over the December 2022 levels, falling to the neutral threshold. This is the first time the Roughly Coincident Indicator has been neutral since October 2020, twenty-seven months ago.

The Lagging Indicators also fell from 83 in December 2022 to 50 in January 2023. As was the case with the Roughly Coincident Indicators between December and January, small but quantitatively insignificant changes in the constituents—CPI (core, year-over-year), short-term interest rates, outstanding commercial and industrial loans, manufacturing and trade inventories, private nonresidential construction, and average duration of unemployment—shifted the bias of lagging indicators to neutral levels.

The pervasively neutral bias among all three categories and subcategories of the Business Conditions Monthly diffusion indices is likely not consistent with randomness. The most likely explanation is that the rebound from the brief 2022 recession is slowing under the lagged effects of a historically rapid contractionary monetary regime settling in.

## **Leading Indicators**

January 2023 nonfarm payroll employment rose by 517,000, with most gains in hospitality, leisure, healthcare, professional and business services. The unemployed rate stands at 3.4 percent, having not changed substantially since early 2022. Both the employment-population ratio (60.2 percent) and the labor force participation rate (62.4 percent) have remained stable throughout 2022 and remain substantially below their February 2020 levels of 61.1 percent and 63.3 percent, suggesting persistent long-term structural changes to US labor markets in the wake of pandemic mitigation policies.

Debits in brokerage margin accounts increased in January 2023. This often suggests optimism (or bullish financial market outlooks), but the present levels are much lower than their early 2022 levels. The 1 year-10 year US Treasury spread narrowed by roughly eight basis points, a small but positive relaxation of one specific inversion of the US Treasury yield curve. The remainder of the indicators notched small but inconsequential gains or losses month-over-month.

## **Coincident & Lagging Indicators**

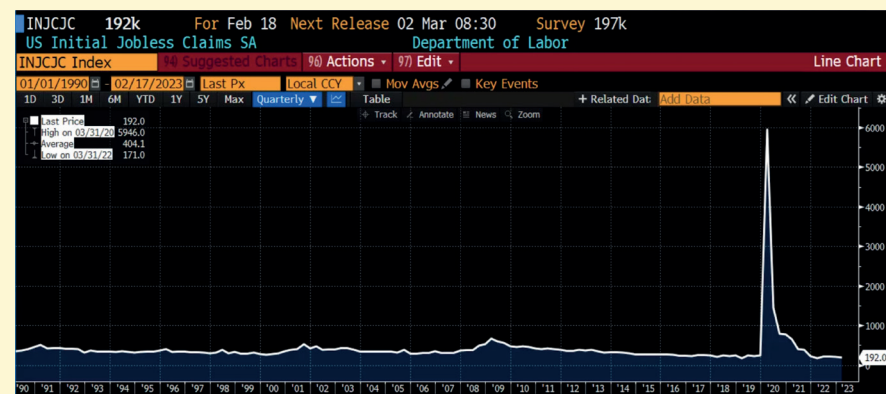
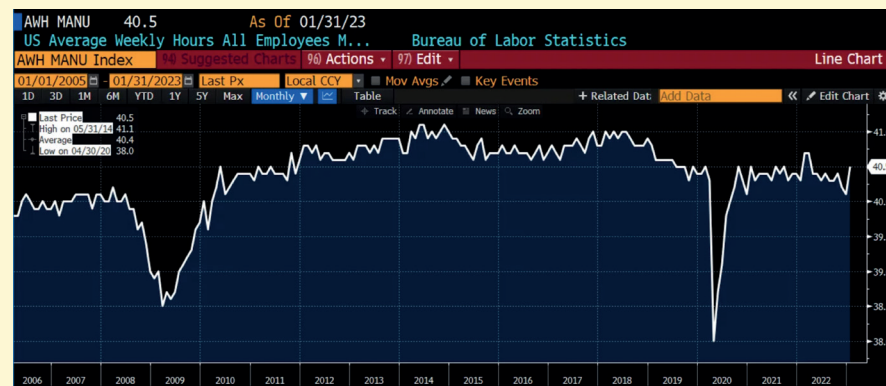
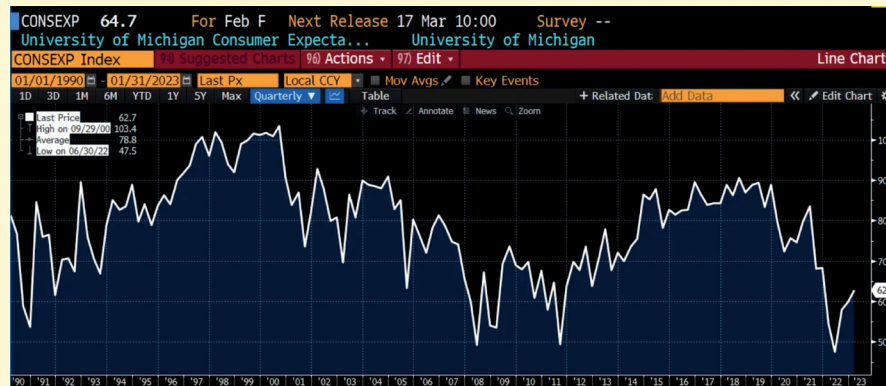
Like most of the leading indicators, all six coincident and lagging indicators were essentially neutral in January 2023.

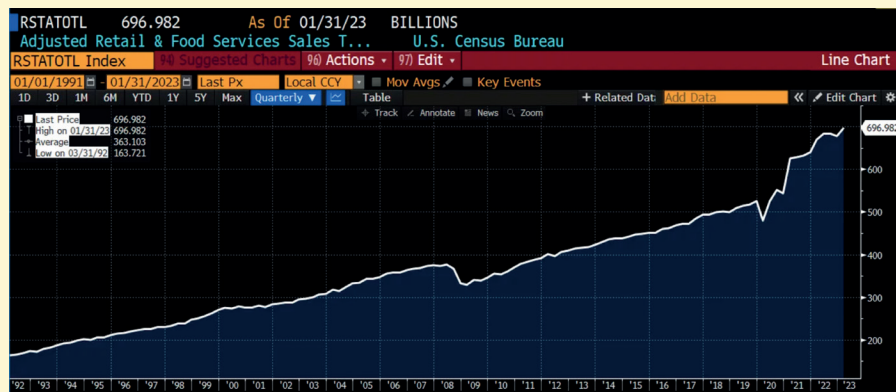
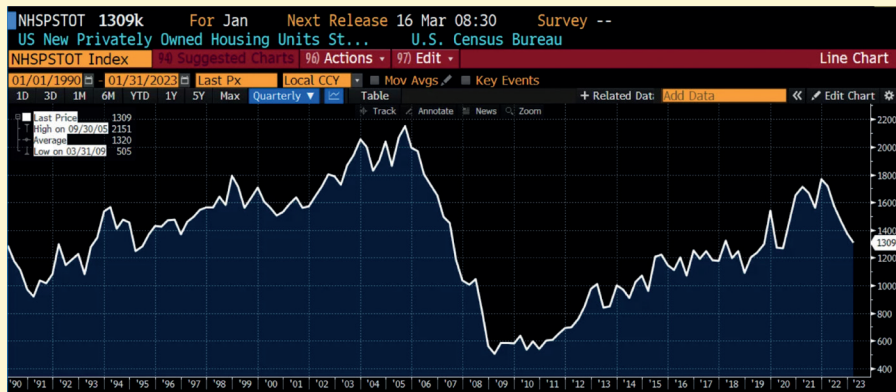
The last time that the Leading (58), Roughly Coincident (50), and Lagging Indicators (50) simultaneously indicated neutral biases occurred in March 2020, with respective readings of 54, 58, and 50. At that time,

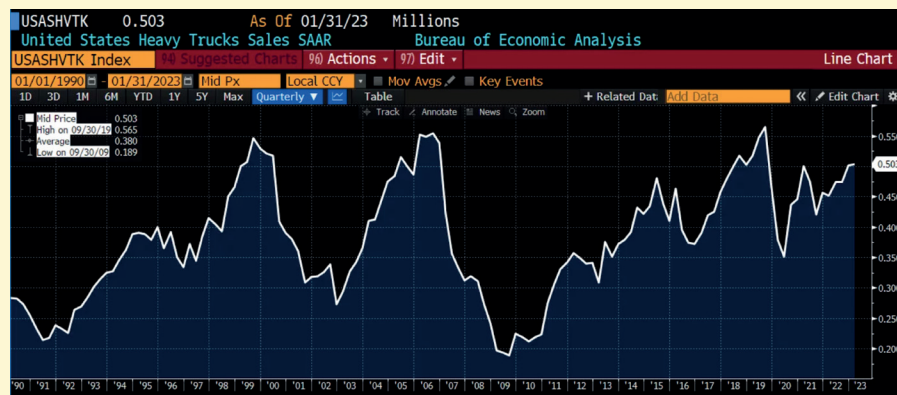
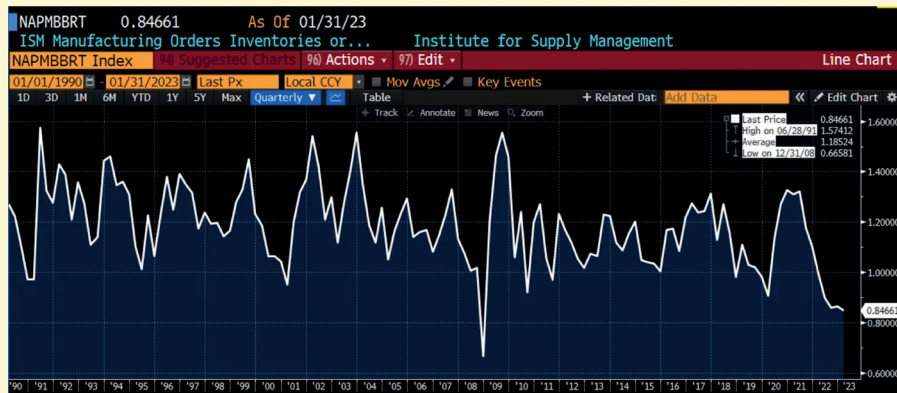
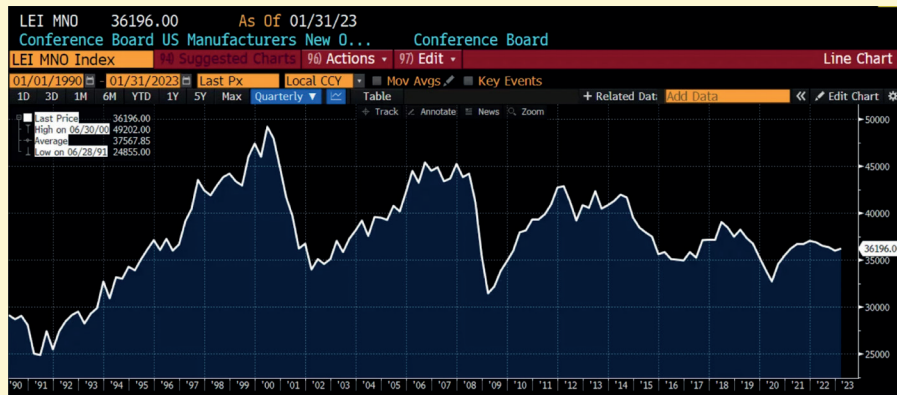
an already slowing US economy was blindsided by both Covid fears and the first wave of Covid policy measures, leading to generational and, in some cases, historical levels of uncertainty and fear.

It is likely that the neutral indications currently dominating the three Business Conditions Monthly indices are tied to a weak recovery from the brief 2022 recession, rising interest rates amid an increasingly unclear path for both inflation and monetary policy, the ongoing debt ceiling stalemate, and mounting geopolitical tensions between the US, Russia, and China. Risks, already elevated, are mounting.

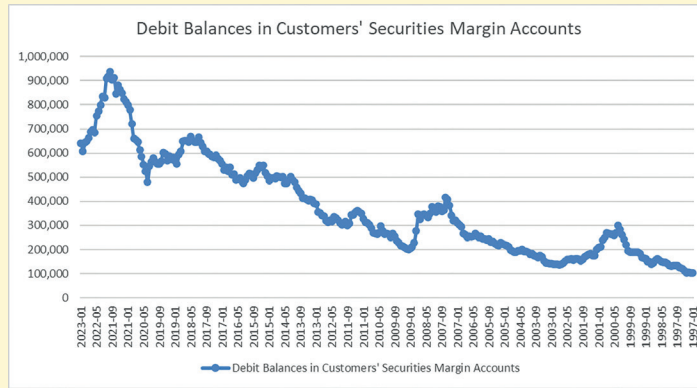
#### LEADING INDICATORS (1990 – present where possible)



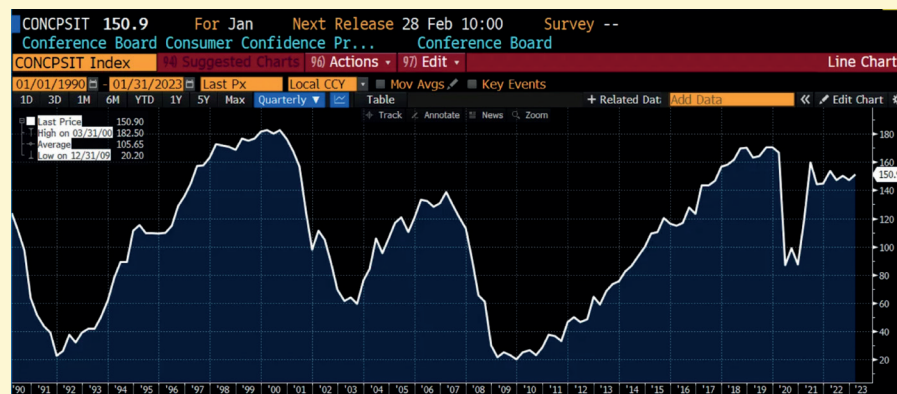
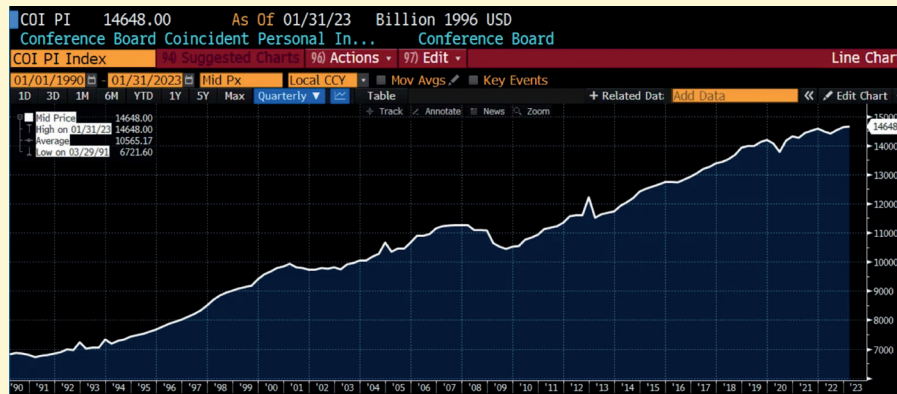
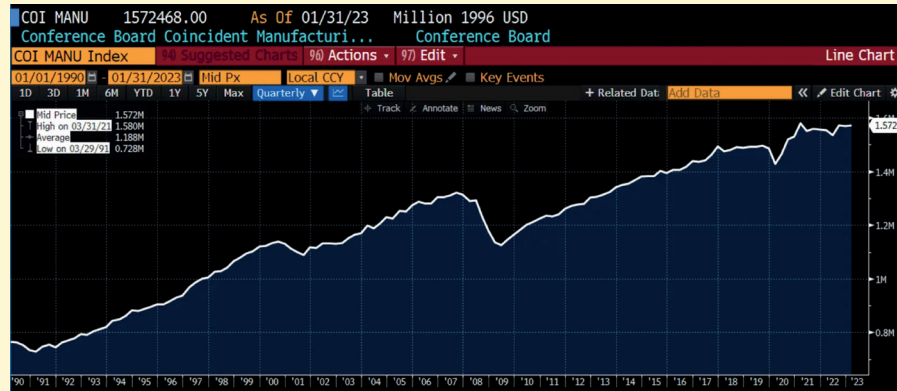


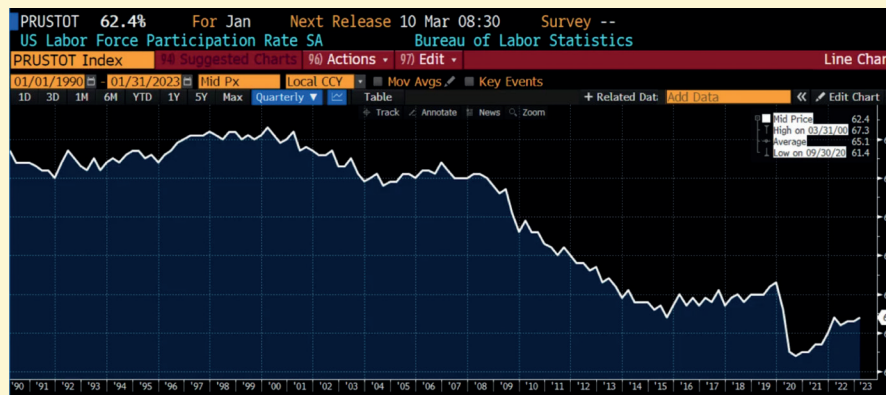
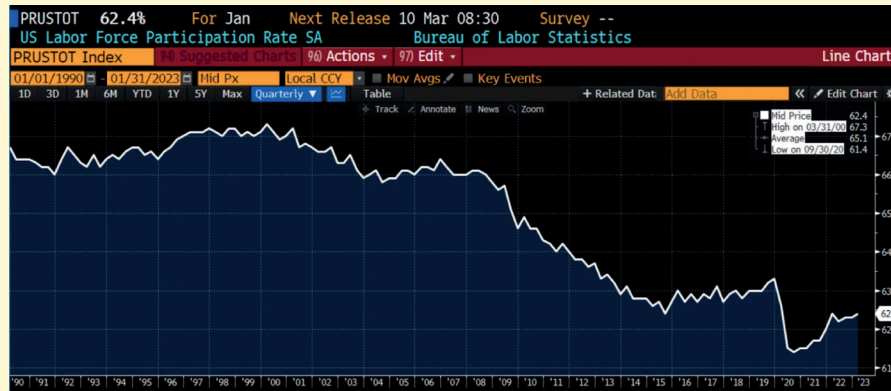
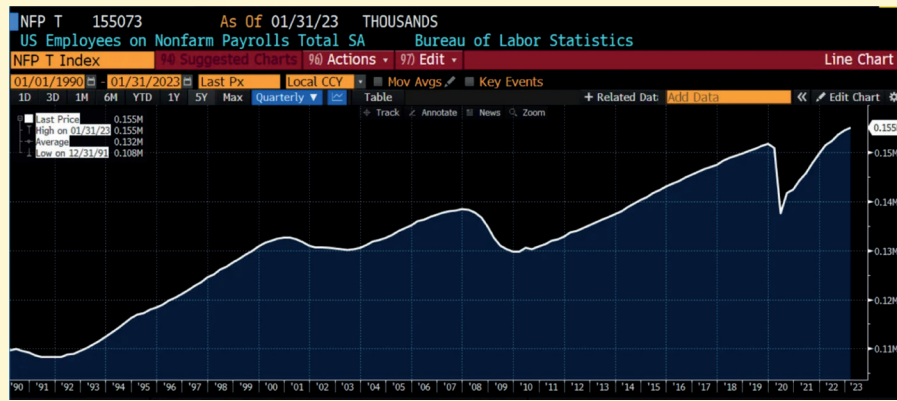




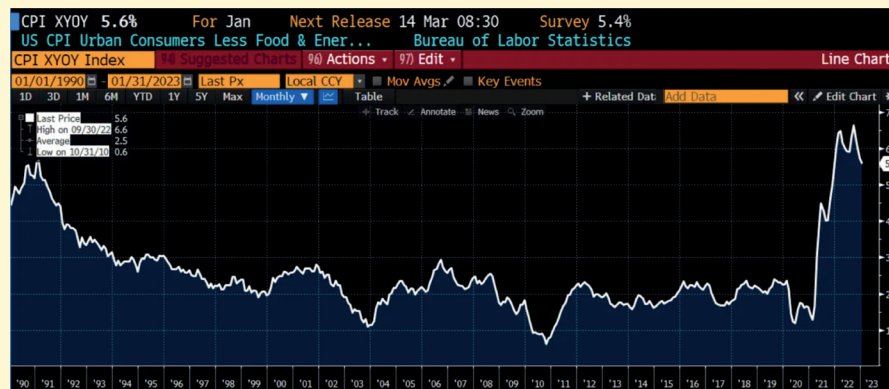


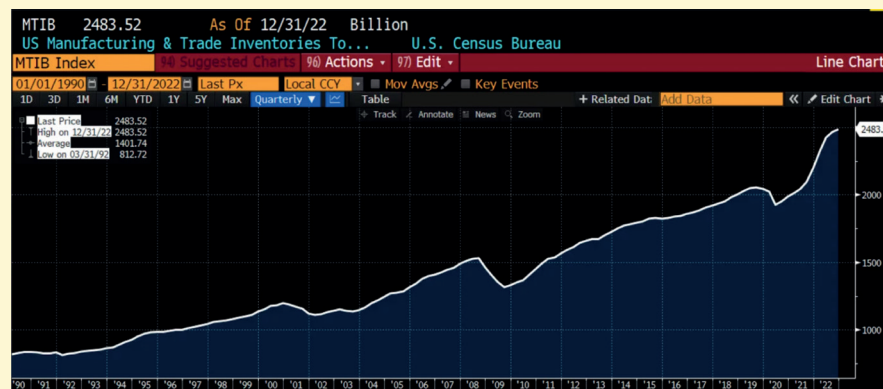
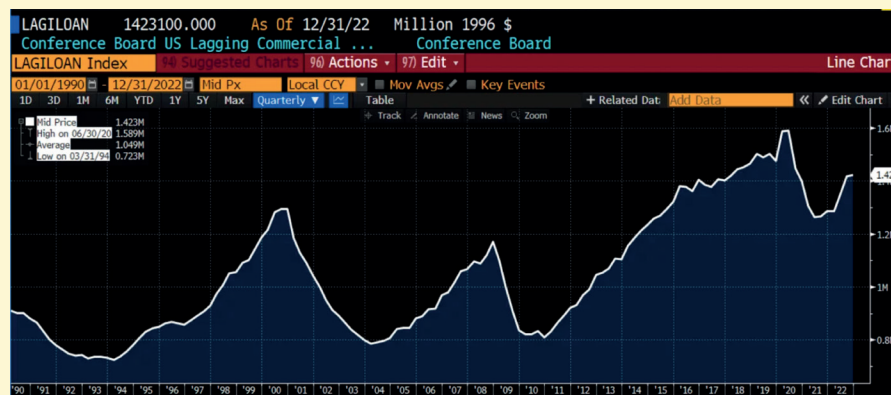
### ROUGHLY COINCIDENT INDICATORS (1990 – present where possible)



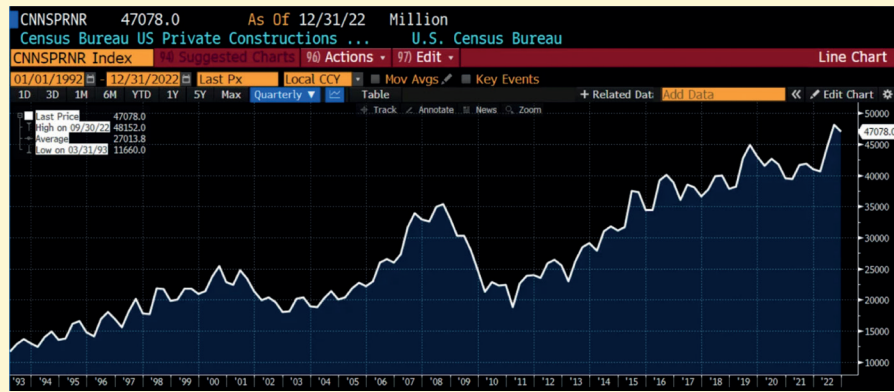


### LAGGING INDICATORS (1990 – present where possible)









## CAPITAL MARKET PERFORMANCE

Ticker	Short Name	%1M	%3M	%1YR	3 Year Annualize	5 Year Annualize	10 Year Annualiz
SPR	S&P 1500 Composite Index	-1.97%	-.81%	-8.63%	8.9996	9.3705	12.4993
SPXT	S&P 500 Total Return	-2.31%	-.96%	-7.93%	8.9049	9.5448	12.6727
SPX	S&P 500 INDEX	-2.17%	-1.09%	-9.18%	8.8848	9.5277	12.6580
MID	S&P 400 MIDCAP INDEX	-.55%	+1.78%	-2.12%	10.3571	8.0866	10.9552
RTY	RUSSELL 2000 INDEX	-.79%	+1.45%	-7.09%	6.3964	5.3934	9.3391
SXXP	STXE 600 (EUR) Pr	+1.63%	+4.96%	+2.00%	6.7286	7.1498	8.2804
TLT US	ISHARES 20+ YEAR	-5.12%	-1.60%	-26.02%	-10.8083	-1.0583	1.4732
QLTA US	ISHARES AAA - A	-3.25%	-1.09%	-11.96%	-3.9172	.6558	1.9089
CRY	TR/CC CRB ER Index	-3.26%	-1.70%	+1.57%	16.1168	6.3832	-.8859
XAU	Gold Spot \$/Oz	-5.74%	+4.36%	-4.80%			
XAG	Silver Spot \$/Oz	-12.61%	-1.47%	-15.63%			
ILM3NAVG	Bankrate 30Y Mortgage Rates	+9.18%	+3.69%	+65.18%			
ILM1NAVG	Bankrate 15Y Mortgage Rates	+11.31%	+2.27%	+81.56%			
MB301ARM	5 Year ARM	+6.59%	-1.22%	+73.62%			
ILA3NAVG	Bankrate 30Y Fixe Mtg Refis	+1.83%	--	+88.45%			

# NatCons, the American System, and the Founders

PHILLIP W. MAGNESS

Research and Education Director

Did America's Founding Fathers really embrace a nationalist economic program of tariffs and industrial subsidies? According to the "National Conservative" movement, such Founding Era luminaries as Thomas Jefferson and James Madison eventually abandoned their free-trade instincts and embraced a program of economic policies not unlike the NatCon agenda today. The American Compass website celebrates "Thomas Jefferson's conversion to Hamiltonian supporter of domestic industry," echoing Patrick Buchanan's 2018 claim that "Tariffs Made America Great." Most arguments in this genre point to Jefferson's qualified commentaries on the Tariff of 1816 as evidence of this claim, while also noting the law was signed by James Madison, his distinguished successor as president. These actions, the NatCons insist, demonstrate that the Founding generation converted to the interventionist economic program of the American System, first outlined by Sen. Henry Clay in a famous speech in 1824.

The NatCon's historical narrative seeks to wrap their own present-day, pro-tariff arguments in the imprimatur of the American Founding. If protectionism worked for Hamilton, Jefferson, and Madison, then it will also work for us today, they claim. While Hamilton, who died in a duel in 1804, did indulge protectionist arguments during his stint as Secretary of the Treasury, the rebranding of Jefferson and Madison as American System enthusiasts runs directly contrary to historical evidence.

Madison and Jefferson were both still alive when Henry Clay outlined his American System platform in 1824. Contrary to the NatCon claims, neither founding father approved of Clay's proposals. In

fact, both condemned it as a constitutional overreach by the federal government.

James Madison reviewed a transcript of Clay's speech a few weeks after its delivery in the Senate chamber. On April 24, 1824 the primary architect of the Constitution wrote the Kentucky Senator a lengthy letter. After crediting Clay for his eloquence, the former president proceeded to lodge his concerns: "candor obliges me to add that I can not concur in the extent to which the pending Bill carries the tariff, nor in some of the reasoning by which it is advocated." Madison then presented Clay with a lesson in basic free-market economics:

The Bill, I think, loses sight too much of the general principle which leaves to the judgment of individuals the choice of profitable employments for their labor and capital: And the arguments in favor of it drawn from the aptitudes of our situation for manufacturing Establishments, tend to show that these would take place without a Legislative interference. The law would not say to the Cotton planter, you overstock the market, and ought to plant Tobacco: nor to the planter of Tobacco, you would do better by substituting Wheat. It presumes that profit, being the object of each, as the profit of each is the wealth of the whole, each will make whatever change the state of markets and prices may require. We see, in fact, changes of this sort frequently produced in agricultural pursuits by individual sagacity watching over individual interest. And why not trust to the same guidance in favor of manufacturing industry, whenever it promises more

profit than any of the Agricultural Branches; or more than mercantile pursuits from which we see capital readily transferred to manufacturing Establishments likely to yield a greater income.

Madison did hedge his commitment to a modest degree, deviating from a pure laissez-faire stance on economic matters. He declared himself “a friend to the general principle of ‘free industry’ as the basis of a sound System of political Economy,” but recognized certain “particular reasons for exceptions to the General Rule, not derogating from its generality.” He was therefore willing to entertain a “a moderate tariff that would at once answer the purpose of revenue, and foster domestic manufactures,” perhaps not unlike the bill he approved during his own presidency.

Historical context is important in interpreting this passage though, as it is not an endorsement of the full-fledged protectionist program sought by Clay. In the early 19th century, tariffs provided the single largest source of revenue for the federal government. This circumstance gave rise to the doctrine of the Revenue Tariff with “incidental protection” insofar as the tax measure could be designed to offer moderate encouragement to domestic industries as a secondary effect of filling the treasury. This was not Clay’s objective though; the Kentuckian sought significantly higher tariff rates to provide explicit protection to industry, even at the price of losing tax revenue.

Madison clearly understood as much, warning Clay that his proposed “increase of duty on articles which will be but partially manufactured at home, with the annual increment of consumers, will balance at least the loss to the Treasury from the diminution of the tariffed imports.” At the same time, he claimed benefits to protected industries would be “frustrated by the increase of smuggling” and other forms of tax

evasion. In the end, he predicted that Clay’s measure would fail in its objective of fostering an industrial base in the young nation. The “Tariff, I apprehend will disappoint also those who expect it to put an end to unfavorable balances of trade,” he continued, as Americans were “accustomed to buy not only as much as we can pay for but as much more as can be obtained on credit.” Although Madison did not fully grasp the fallacious economic reasoning behind the drive to obtain a positive balance of trade, he did not fret at the United States’ failure to do so. “As long as our exports consist chiefly of food and raw materials, we shall have the advantage, in a contest of privations, over a nation supplying us with superfluities.”

Whereas Madison framed his opposition to the American System as constructive criticism to Clay, Thomas Jefferson responded by directly mobilizing his political contacts to defeat the tariff and subsidies program. Clay’s package contained a large “internal improvements” scheme, designed to assist politically connected industries with infrastructure spending and similar federal handouts. These measures illustrated the worst aspects of pork-barrel politicking, which is precisely why they were able to attract special interest support in Congress.

By late 1825, Jefferson considered the situation desperate. In a letter to Madison, he denounced Clay’s American system in no uncertain terms. Not only did the “internal improvements” scheme reach beyond the enumerated powers of the federal government, it imperiled the entire constitutional order of the United States.

To this end, Jefferson personally drafted a “Declaration and Protest of the Commonwealth of Virginia” to denounce Clay’s scheme as a direct violation of the United States Constitution. The document directly hearkened back to a strategy Jefferson and Madison pursued in 1798 with the Virginia and Kentucky Resolutions, a pair of measures adopted

at the state level to oppose the Alien and Sedition Acts as unconstitutional violations of the First Amendment.

In his new document, the author of the Declaration of Independence set his sights directly on the federal government's recent expansions into areas of economic policy that were not granted by the US Constitution. As the resolution opens, "the federal branch has, assumed in some cases and claimed in others, a right of enlarging it's (sic) own powers by constructions, inferences, and indefinite deductions, from those directly given, which this assembly does declare to be usurpations of the powers retained to the independent (sic) branches, mere interpolations into the compact, and direct infractions of it."

As examples, Jefferson targeted Clay's program for asserting a federal "right to construct roads, open canals, and effect other internal improvements." He turned his fiery pen to tariffs next, lambasting Congress for interpreting the Constitution's taxation clause as "a power to do whatever they may think, or pretend, would promote the general welfare" of the United States. Such an interpretation, Jefferson warned, would turn the federal government into "a complete government, without limitation of powers." Such measures, he concluded, undermined the spirit and letter of the Constitution itself.

Jefferson's protest was not a nullifier's document in any sense. Indeed, it affirmed Virginia's commitment to "the blessings of their union" with the other states and warned that a "rupture" of the federal bond would constitute "among the greatest calamities which could befall them." It adopted a pragmatic stance of abiding by this objectionable legislation, should it pass or grow in fervor, "to preserve the peace" of the country, while simultaneously denouncing it as unconstitutional in the strongest terms.

At the same time, Jefferson alerted his allies in the Virginia General Assembly to prepare to make

a stance against the American System measures. In a January 1826 letter to assembly member William Gordon, Jefferson warned in the strongest possible terms against the course Clay and his followers had charted for the country:

"It is but too evident that the branches of our foreign department of gov[ern]m[en]t, Ex[ecuti]ve, judiciary and legislative are in combination to usurp the powers of the domestic branch also, reserved to the states and to consolidate themselves into a single gov[ern]m[en]t without limit[atio]n of powers. I will not trouble you with details of the instances which are thread bare and unheeded. The only question is what is to be done? Shall we give up the ship? No, by heavens! While a hand remains able to keep the deck."

Jefferson noted the peril of the American System came from its propensity to attract votes through political payoffs and handouts. "The Western states have especially been bribed by local consid[eratio]ns to abandon their ancient brethren and enlist under banners alien to them in principles and interest," illustrating why it was difficult to defeat such measures through legislation. For the moment, he knew that his allies lacked the votes to stop the tariff and internal improvement measures.

At best, Jefferson hoped that they could delay them through compromise measures that weakened the bills and slowed the federal government's encroachment. As he closed his letter "I pray that what I have now hazarded to you as a friend may be sacredly locked up in your own breast." At 83 years, 61 of them in public life, his energies were exhausted. It was time for the new generation to stand against the growth of government power, and the aged Virginia statesman could only hope that others would reinvigorate constitutional constraints

against this latest turn of events. In this word of counsel, Jefferson made his last major foray into governance, dying on July 4th of the same year. It should be remembered that his final political actions stood firmly against Henry Clay's program of economic interventions.

Today's NatCons would do well to heed his counsel before repeating the same mistakes that broke the Constitution's original constraints on federal power, and opened the door to almost two centuries of legislative, executive, and regulatory intrusions into every aspect of American economic life.

– February 22, 2023



# Inflation Surges in January

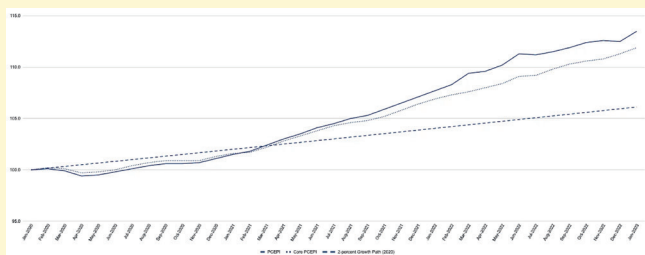
WILLIAM J. LUTHER

Director, Sound Money Project

After eight rate hikes from the Federal Reserve in the last year and declining inflation during the back half of 2022, many had hoped the worst of the price increases were behind us. Today's release from the Bureau of Economic Analysis suggests that might not be the case. The personal consumption expenditures price index (PCEPI), which is the Fed's preferred measure of inflation, grew at an annualized rate of 7.4 percent in January 2023 — the highest one-month posting since June 2022.

The PCEPI has grown at a continuously compounding annual rate of 4.2 percent since January 2020, just prior to the pandemic. As a consequence, prices are 7.4 percentage points higher today than they would have been had the Fed hit its 2-percent target over the period.

Core PCEPI inflation, which excludes volatile food and energy prices and is widely thought to be a better predictor of future inflation, also climbed over the last few months. In November 2022, core PCEPI grew at an annualized rate of just 2.6 percent. It ticked up to 4.5 percent in December 2022, followed by an incredibly steamy 6.8 percent in January 2023.



The recent surge in inflation means monetary policy has not been as restrictive as Fed officials had intended. The Federal Open Market Committee (FOMC) raised its (nominal) federal funds rate

target range to 4.5 to 4.75 on February 1. If inflation expectations were equal to the previous month's core PCEPI inflation rate, the current nominal target range would imply a real (inflation-adjusted) federal funds rate range of -2.0 to -1.75 percent — well below 0.25 percent, which many economists cite as an estimate of the neutral rate.

Had Fed officials known inflation was surging in January, they may have opted for a larger rate hike at their last meeting. Indeed, the FOMC meeting minutes — released on Wednesday — indicate that a few participants “favored raising the target range for the federal funds rate 50 basis points” at the previous meeting or “could have supported raising the target by that amount.” Cleveland Fed president Lorretta Mester and St. Louis Fed president James Bullard were among those pushing for higher rates. Neither Mester nor Bullard currently vote on the FOMC, but they do participate in the policy discussion.

Whether the FOMC will continue to raise rates in 25-basis-point increments or opt for a bigger hike in March remains to be seen. Most FOMC members have said they prefer making smaller moves at this point. But they did not expect such a large inflation reading. And they surprised markets last June by opting for a 75-basis-point hike, after Chair Jerome Powell had said rate hikes in excess of 50 basis points were off the table at the post-meeting press conference in May.

While the size of the coming rate hikes is uncertain, there is somewhat more certainty about where rates are ultimately going: higher.

In December, the Federal Open Market Committee projected just three 25-basis-point rate hikes in 2023. That would have taken the federal funds rate target

range to 5.0 to 5.25 percent. Now, the CME Group reports a 55.4 percent chance that the federal funds rate target range will be 5.25 to 5.5 percent, following the June 2023 meeting, and a 31.3 percent chance the range will be 25 basis points higher than that in July. The FOMC will revise its projections in March.

How high rates will ultimately go depends on how inflation evolves over the next few months — and how quickly the Fed reacts to restore confidence in its longer term-inflation projections. The January PCEPI release marked a step in the wrong direction.

– February 27, 2023

# Will Federal Spending Be Brought Under Control?

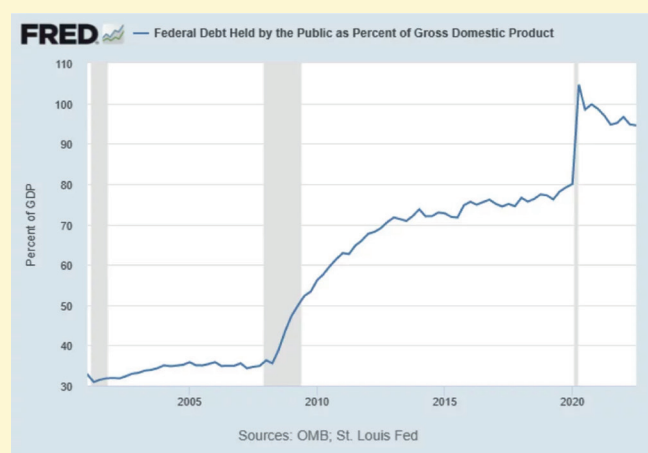
JASON SORENS

Senior Research Faculty

With the federal debt ceiling fight looming in Congress, now is a good time to look again at how much the federal government owes, and whether the new Republican House majority will be able to keep spending under control.

Figure 1 shows how federal debt held by the public as a percentage of the economy has changed between first quarter 2001 and second quarter 2022. Over the last 21 years, federal debt has tripled as a share of the economy. Now, these figures include debt held by the Federal Reserve System; in recent years, excluding that debt would reduce these figures by about 15 percentage points of GDP. But if we want to compare the US to other countries, we would need to include state and local debt, which USgov-spending.com “guesstimates” (actual local debt data releases lag by a couple of years) were about \$3.5 trillion by mid-2022, or 14 percent of GDP. Thus, general government debt held by private investors in the US almost certainly tops 90 percent of GDP today, which is right around the level in the United Kingdom, above Germany and below Canada and Spain.

Figure 1: Federal Debt Held by the Public, % of GDP, United States



The US is, therefore, probably nearing the limit of what investors would be willing to tolerate. Debt-burdened countries like Spain and Italy owe about 120 percent of GDP. Another spending spree like those of 2009 or 2020 could take this country right to that ceiling. Cutting federal spending is an absolute necessity if we are to avoid significant tax increases in the future.

Will Congress actually cut spending? History suggests not. Economic historian Robert Higgs invented the term “ratchet effect” to describe the way that government growth after a crisis tends to be locked in: the size of government never retreats to what it was before the crisis.

To answer this question more definitively, I revisit here some research I did in December 2016 and see if my conclusions have held good for the past few years. If so, we can have more confidence that there is a causal relationship between divided government and spending restraint. This is what econometricians call “out-of-sample prediction.”

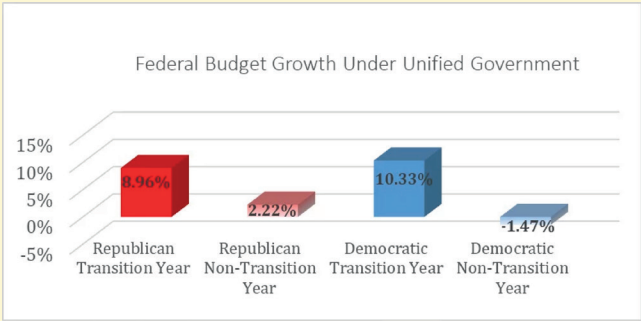
At the end of 2016, Republicans were about to take full control of the federal government. I hypothesized that in the first year of unified partisan control, Congress would increase spending on the priorities of the party in power, but I did not expect that they would continue to increase spending at an unusually fast rate in subsequent years. In other words, every time there was a *transition* to unified party control of the federal government, spending would rise rapidly, but in other years, there would be no difference in spending growth between divided government and unified government. I used inflation-adjusted data on federal budgeted and actual spending



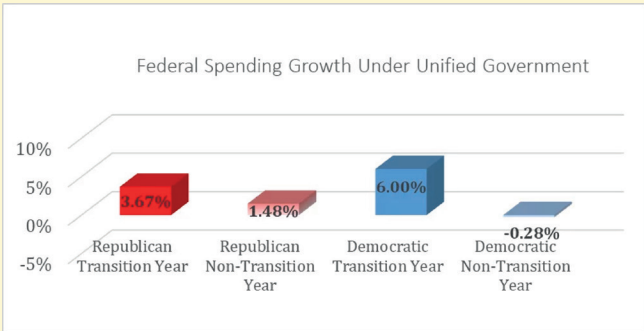
growth rates from fiscal year 1977 to 2016 to test my hypothesis, and the data supported it.

Figures 2 and 3 show the estimated statistical effect of a unified federal government in its first and subsequent years on budgeted and actual spending, respectively.

**Figure 2: Predicted Budget Growth Rates Under Unified Democratic and Republican Control, Relative to Divided Government**



**Figure 3: Predicted Spending Growth Rates Under Unified Democratic and Republican Control, Relative to Divided Government**



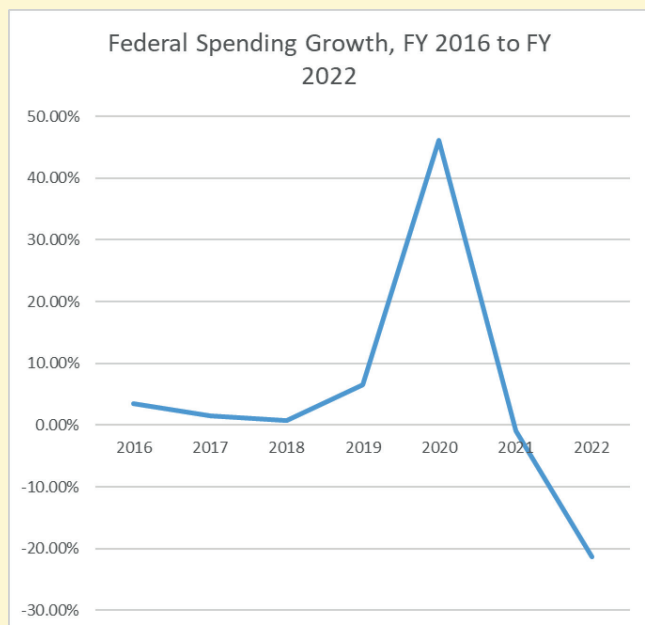
The data revealed that under the first year of unified Republican control, Congress had budgeted nine percentage points more spending compared to a divided government year. In subsequent years, Congress had budgeted only two percentage points more spending compared to a divided government year. Democrats budgeted over 10 percentage points more spending in their first year of control, but actually might have spent a little less in subsequent years than under divided government. The figures were more moderate for actual compared to budgeted spending.

Did my prediction hold good for transitions to unified Republican control in 2017 and unified Democratic control in 2021?

Only in part. Figure 4 shows the annual, inflation-adjusted percentage change in federal spending from fiscal year 2015 to fiscal year 2022, according to U.S. budget documents. Republicans increased federal spending less under unified control in fiscal year 2017 than the divided government had in fiscal year 2016, but they increased it even less in their second year of control. Then federal spending grew faster under divided government during and after the 2018 midterm election season and exploded in 2020 because of COVID-19. This evidence certainly does not suggest that divided government restrains spending, but it does imply that unified government increases it more rapidly in their first year of control.

Finally, under unified Democratic control federal spending was steady in FY 2021, and then declined rapidly in FY 2022 as the COVID-19 stimulus subsided. The decline in federal spending in FY 2022, however, was not nearly enough to make up for the explosion in FY 2020, and the fact that federal spending got locked in at an apparently permanently much-higher level is, itself, a sort of evidence for the unified-government-transition hypothesis.

**Figure 4: Annual Rate of Growth in Federal Spending, FY 2015 to 2022**



To sum up, we shouldn't expect a transition from unified Democratic control to divided government to reduce the rate of growth in federal spending. The evidence from before 2016 suggests that divided government restrained spending only compared to years in which there was a transition to unified government. The evidence since 2016 is even less positive about divided government, because divided government increased spending abnormally rapidly in 2015 and 2016 and then again in 2019 and 2020.

The Republican House will probably shift spending somewhat from Democratic to Republican priorities, but if Democrats or Republicans take full control of DC after the 2024 election, they will, more likely than not, increase spending on their priorities without cutting what's already been "baked in" to the federal budget. The ratchet effect lives on, and divided government can only delay growth in government, not reverse it.

– February 10, 2023

# The Age of Decline

ANTONY DAVIES

Contributor

Transitions between eras are only sometimes easily identified. Historians didn't identify the coming of the Industrial Revolution until decades after it began. By contrast, the start of the Atomic Age can be dated to the second that the first atom bomb exploded over Hiroshima, and it took only hours for the world to know that humanity had entered a new era.

Much of the developed world has recently moved into a new era that historians likely won't name, and the general public won't notice for a decade or so: the Age of Decline. Japan, Greece, Italy, Portugal, Russia, Germany, Spain, South Korea, and China, along with thirty other developed countries, are projected to see their populations decline in 2023. Hong Kong, Finland, Taiwan, France, Austria, Belgium, Netherlands, United Kingdom, Denmark, and the United States, among another thirty-three countries, will see their populations grow by less than one-half of one-percent. For most of the developed world and the major population centers, population growth has largely stopped.

While this may come as good news to those who fear overpopulation, theory and evidence indicate that we have far more to fear from declining populations. As the economist Julian Simon pointed out four decades ago, humans are the ultimate resource, because they create resources where none existed before. All of the resources that make our modern, comfortable lives possible, from energy to transportation to communication to refrigeration to climate control to pharmaceuticals, are the results of human ingenuity. It's no wonder that as the world population exploded, so too did our resources.

The Age of Decline will pose a particularly difficult problem for countries like the United States

that rely on younger workers to support retirees. The latest Census figures project that within the next seven years, net migration into the United States will exceed the country's natural population growth, making us, for the first time in almost 150 years, dependent on immigration for our population growth. Even then, the Census projects that the US population growth rate will fall (permanently) below one-half of one-percent within the decade.

For decades we've known the implications for Social Security. In 1960, there were more than five workers paying into the system for each Social Security recipient drawing out. Today, it's fewer than three. And that number is expected to fall to two within ten years. In short, we need today's average worker to contribute to Social Security two and a half times what the average worker of three generations ago contributed.

Changing demographics are not only placing a greater burden on workers, but also making it less and less possible to institute needed changes. As the ratio of workers to retirees declines, so too does the voting power of those workers. People aged 53 and older are either receiving Social Security, and so not interested in reforms that involve cutting benefits, or are close enough to receiving Social Security to be less interested in reforming the system to their own future detriment. To further stack the deck against them, younger workers are less likely to vote than are the elderly. In the extreme, if all likely voters aged 52 years old and younger supported cutting Social Security benefits and all likely voters aged 53 and older opposed cutting benefits, then in a vote held today, a "cut benefits" proposal would win by a scant 51 to 49 percent. In another seven

years, it would be a dead heat. From 2030 forward, the demographic shift toward the elderly makes it impossible for the “cut benefits” option to win. And that assumes that voters aged 52 and younger would be unanimously in favor of cutting Social Security benefits. In fact, almost 80 percent of working age Americans say Social Security benefits should be preserved, even if it means raising payroll taxes.

Unfortunately, the laws of arithmetic trump both political rhetoric and wishful thinking. The Social Security Board of Trustees estimates that with no changes, Social Security will run a \$2.5 trillion deficit over the course of the next decade. To eliminate that deficit would require either cutting Social Security benefits by around 25 percent or raising payroll tax revenues by around 25 percent, or some combination of the two. Of course, the federal government could always borrow to fund the Social Security deficit, but that doesn’t eliminate the deficit so much as move it from one set of government ledgers to another. No matter what we choose to do, taxpayers are going to pay the price. The question that remains is *which* taxpayers. Given the polling data and the shifting demographics, the answer appears to be the working taxpayers.

An oft-repeated possible solution is to remove the cap on payroll taxes. The danger there lies in imposing a significant cost on budding entrepreneurs. Households with at least one income, and a side business that has grown enough to provide significant income but not enough to be a full-fledged business, are more likely to be earning (or anticipate soon to be earning) near the Social Security payroll tax cap (currently \$160,000). As business owners must pay both halves of payroll taxes (employer and employee), removing the payroll tax cap imposes an additional 12.4 percent tax on business owners’ earnings beyond \$160,000. This will create a disincentive for entrepreneurs to grow their side businesses enough to support employees. A

more entrepreneur-friendly change of keeping the \$160,000 cap, but then removing it for earnings above \$250,000, would raise less than half of what’s needed to close the Social Security deficit.

Both the economics and the demographics lean toward placing the growing Social Security burden on the backs of workers. A stagnating population will make that burden both more financially onerous to bear and more politically difficult to alleviate. Meanwhile, slowing population growth ultimately means slower economic growth. In short, the problem only gets worse as time goes on.

It’s no coincidence that the United States grew from a small agrarian nation to an economic superpower over the same century and a half that its population grew thirty-fold. But that era has ended. The United States, and much of the rest of the developed world, has entered the Age of Decline. As population growth in developed countries slows, economic innovation and growth will slow also. This will place greater burdens on already-burdened retirement programs. The shift from a younger population to an older population will ensure that the bulk of that burden falls on the young, ultimately making it more expensive for them to raise children of their own, thereby further exacerbating the shift.

Having survived the Atomic Age without blowing ourselves to bits, and having generated wealth beyond imagining throughout the Information Age, we enter the Age of Decline and find ourselves victims of our own success. History tells us that impoverished societies die by war and famine. Now we are learning that prosperous societies die by attrition.

– February 6, 2023

# Government Siphon Targets Corporate Stock Buybacks

PETER C. EARLE

Research Faculty

During last night's *State of the Union*, President Joe Biden announced a quadrupling of the corporate buyback tax, which was introduced in the 2022 Inflation Reduction Act. The tax will be applied to stock purchases made by domestic public companies.

For reasons that are clear, the political left has long looked askance at stock buybacks. It has much to do with the transactions involving colossal amounts of money undertaken by massive business enterprises. The former is undoubtedly tempting as a target for official pilfering, whereas the latter are reliably despised by policymakers. It's surprising, really, that a measure to chasten the latter by seizing a portion of the former, especially when spun as some form of "justice" or restitution, has taken so long.

The tales are familiar. Corporate stock buybacks are driven by "greed," of course, and allegedly fuel "wealth inequality." Instead of repurchasing shares in the market, say activists and politicians (virtually none of whom have ever owned a business, let alone managed a massive one), employees should be given pay increases. Or new innovation should be explored.

Congresspeople and regulators are the last people who should be telling entrepreneurs and corporate executives that they should be on the lookout for new innovation. That's already in their DNA as creators, and it bears mentioning that, at times, there are no applicable innovations in or coming to the market. As for awarding pay raises, why would any firm paying what the market will bear – even more importantly, what their business segment and the unique labor market in their locality bears – increase compensation across the board?

So yes, a new tax is born. This one will do what all taxes do, to some extent or another: curtail the newly targeted activity while creating an incentive to explore imaginative workarounds.

But on the other hand, the billions or tens of billions of dollars raised will go to a fund that directly addresses the numerous groups severely injured by stock buybacks. Teachers, firefighters, union workers, and other groups — hard working Americans, all — will receive US government checks cut from the buyback tax fund to remedy the gross inequalities rooted in the heinous act of firms buying their own stock in the market.

No, of course they won't. All funds raised by taxing buybacks, which have purportedly served as an economic war machine in the service of plutocrats, will go directly into the US government's coffers — some of which will go toward providing actual war machines for Ukraine. The rest will be used for purposes ranging from wrestling with the mounting debt service on over \$31 trillion of government debt to creating woke indoctrination programs for the US armed forces and other federal agencies.

When corporate executives decide to direct funds into share repurchases, they are conceding that there are no clearly profitable projects, worthwhile product lines, or synergistic acquisitions worth spending on at the moment. Older, larger firms — sometimes called "cash cows" — frequently find themselves in this position. They may choose between doing nothing with their unused cash (which is a disservice to shareholders and employees), paying a dividend (which rewards certain shareholders but also brings inflexibility and tax consequences), or they may buy their own stock in the market. (Unlike the world



inhabited by the vampires of the Beltway, in the productive world commercial opportunities come and go unpredictably. And there are consequences for engaging in unprofitable ventures in the real world, unlike in DC.)

There is a view that stock buybacks are a tacitly manipulative exercise, undertaken simply out of “greed” to raise stock prices. It simply isn’t the case. While with each buyback a (somewhat) smaller number of remaining shareholders will share in the benefits of a larger share of future earnings, the company’s value is decreased by the total shares purchased. Below is a chart of the five year return on the S&P 500 index as compared to four indices and financial products that track the performance of stocks undertaking large buybacks. All underperformed the S&P 500, clearly demonstrating that large scale corporate share repurchases do not drive up stock prices.

**S&P 500 Index returns vs. S&P 500 Buyback index, Solactive US Buyback Index, Invesco Buyback Achievers ETF, and NASDAQ Buyback AchvTR (2018 – present)**



(Source: Bloomberg Finance, LP)

Buybacks aren’t undertaken with the sort of sloppy momentum buying seen in meme stock trading campaigns. Most are undertaken as block purchases from asset managers. In the event buybacks were to drive stock values into egregiously overvalued territory, two things would occur: first, short sellers would sniff out the excess profit opportunities in

no time at all. And second, the firm purchasing its own stock would have accumulated a position in overvalued stock.

Indeed, buybacks often increase when the broad stock market is down. In March 2020, the US stock markets crashed for the first time in 33 years, and over the next two quarters, stock buybacks surged. But it bears mentioning that corporate decision makers are fully cognizant of the effect that expansionary monetary policy has on financial assets, so it’s hardly surprising that they would continue buying throughout 2021. It would be a disservice to shareholders, approaching depraved fiduciary indifference, to know of the likely economic effects of central banks flooding the world with money but not act upon it.

Questions remain: how are the stock purchases associated with the issuance of convertible bonds to be treated? What of share repurchases undertaken as part of anti-dilutive measures to balance shares associated with 401Ks or Employee Stock Options Plans (ESOPs)? Will Special Purpose Acquisition Companies (SPACs) or corporate actions like mergers and acquisitions trigger the tax? The answers to these questions will potentially impact hundreds of millions of investors to the tune of tens or hundreds of billions of dollars. And they will all need to be answered.

Given the current political makeup of Congress, this particular increase in the corporate repurchase excise tax seems unlikely to pass, but some form of it probably will in the future. When it does, another market function will have fallen prey to the unslakable thirst of the insatiable American state.

– February 8, 2023

# Lust for Power is More Dangerous Than Climate Claims

DAVID WAUGH

Managing Editor

Government bureaucrats and international agencies point to impending “doomsday” events, often due to climate change. Recent headlines demonstrate an alarming number of apocalyptic forecasts by intellectuals and government officials.

Two weeks ago, pundits seized on *The Bulletin of the Atomic Scientists*’ updating its “Doomsday Clock,” a metaphor for how long we have until armageddon. The group responsible for the clock includes public policy professors, United Nations employees, and a staff writer for the *New Yorker*. This year, these experts moved the clock to its closest-ever to doomsday, citing the increased risk from climate change and war.

Earlier this year, Stanford scientist Paul Ehrlich claimed, “humanity is very busily sitting on a limb that we’re sawing off,” in a highly publicized 60 Minutes interview.

Like Ehrlich, President Biden, using language from a UN report, deemed climate change risk a “code red for humanity” in a speech on proposed energy regulations.

Curiously, the coming doom in these narratives is usually humanity’s fault, and the preferred solution is always more government. Global leaders implore us to accept more regulations and reduce meat-eating, travel, and energy consumption. If not, the day’s crisis will worsen.

There is a reason such threats are hard to ignore. Our biological programming primes us to look for things that might harm us.

In the face of growing regulatory risks to our preferred ways of life, the least we can do is see the perpetual crisis narratives for what they are: a tool to legitimize dangerous increases in the size and

scope of government.

By enabling politicians to expand the role of government recklessly, we risk working against what Americans want: a healthy economy. Recent polling data show Americans worry most about the rising prices of daily goods.

In last month’s Gallup poll titled “What do you think is the most important problem facing the country today?” 40 percent of Americans cited economic problems, while 15 percent pointed to “The government/Poor leadership.”

Where was climate change? Near the bottom. In contrast to mainstream media narratives, only 3 percent of Americans think climate change is our most important problem.

Still, governments worldwide use climate change to justify plans like the “Inflation Reduction Act” (IRA) and similar legislation containing billions in energy and climate subsidies. Researchers at the Heritage Foundation estimate the IRA will impose tax hikes of more than \$2,400 on the average middle-income family.

The COVID-19 pandemic is another recent example of headline-grabbing catastrophic predictions serving as a pretext for governments to expand their power dramatically. The resulting lockdowns inflicted enormous social and economic costs worldwide.

Americans care about economic issues, not empty threats. Further, unlike what some politicians might claim, the path to prosperity is simple: get the government out of the way.

Data from the Fraser Institute confirm the relationship between economic freedom and increasing prosperity. Researchers find positive associations

between economic freedom and income, economic growth, and entrepreneurial activity.

Almost 70 years ago, H.L. Mencken stated, “The urge to save humanity is almost always only a false-face for the urge to rule it. Power is what all messiahs really seek: not the chance to serve.”

Today, doomsday narratives enable government officials to “save” us from catastrophe by growing their ability to control our lives.

Whether a “Doomsday Clock” or another frightening metaphor, politicians and intellectuals claiming the end times are near often manifest as nothing more than cover for harmful government interventions into the economy.

– February 9, 2023



# Joblessness and the Fed

ALEXANDER WILLIAM SALTER

Senior Fellow, Sound Money Project

The US economy added more than half a million jobs in January, significantly exceeding forecasters' expectations. A robust labor market complicates the narrative of an impending recession. But some commentators worry it might force the Fed into even-more-contractionary policy. Does the recent strong jobs report spell trouble for the Federal Reserve?

The prevailing wisdom among economic and financial journalists is that tight labor markets drive up inflation. They claim that the Fed can ease pricing pressures by raising its interest rate target or shrinking its balance sheet, but only at the cost of worse employment conditions. This view is sometimes expressed with reference to the Phillips curve, which old-school Keynesians took to mean there was an exploitable tradeoff between unemployment and inflation.

Thankfully, we don't need to worry about the Phillips curve. The unemployment-inflation tradeoff doesn't exist. Phillips curve reasoning — that big swings in aggregate demand can push joblessness up and inflation down — only makes sense as part of a macroeconomic paradigm that invalidates simplistic thinking about the so-called “menu of policy options.”

Fundamental economic performance, including output and employment, is determined on the supply side. Living standards depend on labor, capital, technology, and institutions. They do not depend on green pieces of paper or bank reserves. Monetary policy can determine the dollar's purchasing power (or inflation, its rate of change), but it cannot make us richer or poorer in the long run.

Things are a little messier in the short run, where an unexpected change in monetary policy can affect

incomes and jobs. But the way to think about this is as a deviation from a (supply side) trend. There is no need to fashion an entirely new (demand side) economic reality to account for nominal disturbances.

The key word is “unexpected.” If households and businesses make their employment and production decisions based on a 2 percent long-run inflation rate, creating new money fast enough to result in 3 percent inflation may fool them into working and making more for a while. But once markets get wise to the game, the goods-and-services bonanza ends. The only permanent impact is an even-more-depreciated dollar.

Policymakers can't choose inflation-unemployment combinations like they're picking off a menu. The real (non-inflationary effects) of monetary policy are an artifact of policy unpredictability. In fact, if policy were credible, there would be almost no real effects of monetary policy! (“Almost” because even perfectly predicted inflation could induce investment and portfolio choices, such as economizing on cash and other non-interest-bearing dollar-denominated assets, that affect the allocation of resources.)

The best thing the Fed can do to fight inflation is rigorously commit itself to price stability. It should ditch its “average” inflation target, which it adopted in August 2020. Targeting 2 percent inflation on average only works if the Fed has the credibility to follow periods of overshooting with undershooting. It doesn't. Chairman Powell and the FOMC have no intention of delivering less-than-2-percent inflation to offset nearly two years of higher-than-2-percent inflation. Instead, they will allow the price level to remain permanently elevated. Without a symmetric

response to deviations from the target, the Fed's so-called average inflation target will not produce 2 percent inflation on average. Instead, it will tend to produce inflation that exceeds 2 percent. That's a far cry from price stability.

– February 15, 2023

# What's Up (and Down) With the Economy?

ROBERT E. WRIGHT

Senior Research Faculty

Will the economy grow or shrink in 2023? That is the trillion-dollar question. Some say shrink, some say grow, but maybe the smartest of all say “I dunno.”

Soon after the Global Financial Crisis of 2008-9, then *Wall Street Journal* reporter Simon Constable and I teamed up to write a book for investors about the 50 most important economic indicators. Some readers complained that 50 indicators were too many to track, but others responded to our view that any modern economy, especially that of the United States, is too complex to understand by looking at just a few indicators, especially when major structural shifts are underway.

Our notion was that investors can “beat the market” by not getting beat by it. In other words, above-average risk-adjusted returns can be yours if you simply ride the high tide with everyone else, but jump ship into safer asset classes when you see the tide turning before others do. That means, though, that investors have to pay close attention to all of the sundry warning signals that an economy in trouble cannot help but emit, though it does not always do so clearly or unequivocally.

Fast or mechanical rules may deceive, because every variable must be understood in context. For a long time, for example, burlap orders were key because furniture manufacturers shipped their wares, which as consumer durables were highly correlated to the business cycle, covered in burlap. As burlap lost favor with shippers, though, the economic predictive power of burlap orders waned. More recently, corrugated cardboard orders serve a similar role, but you would have missed the recession of 2020 if you thought the economy was booming because Amazon et al ordered a bunch of cardboard

shipping boxes as lockdowns spread across the country and globe.

AIER's Pete Earle recently gave us an excellent example of the importance of understanding the numbers behind the numbers. Although real GDP rose 2.9 percent in the fourth quarter of 2022, beating consensus expectations of 2.6-2.7 percent, most of the gain came from reduced imports, not higher exports, and increased inventories, which could just as easily indicate unsold goods piling up as it could mean businesses stocking up in anticipation of banner sales in 2023.

Various organizations, including AIER, try to simplify economic forecasting by publishing or selling their own indices. The Conference Board, for example, revised its Leading Economic Index (LEI) on 1 February. A composite of 10 leading indicators, the LEI is down 3.8 percent since June 2022 and over 6 percent over the last year, clearly flashing “recession.” If you dig deeper into the numbers, though, as Earle did with GDP, perhaps the LEI should be giving even stronger indications of recession.

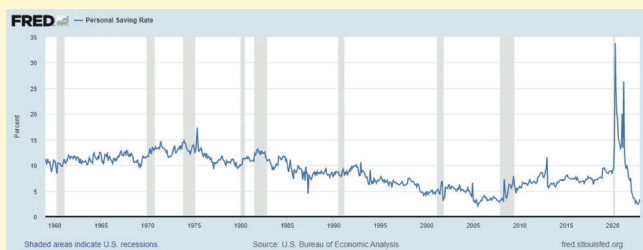
Consider, for example, average weekly initial claims for unemployment insurance, which is down slightly (and hence signaling a positive for the economy). The issue here is that the labor market has been behaving in an unusual fashion since the start of the pandemic: quiet quitting/resenteeism, record numbers of unfilled jobs, quiet hiring, a labor force participation rate that is improving but still below its pre-pandemic level, disability up at about 33 million, and so forth. The most palpable aspect of the current labor force situation, though, is that wages have not kept up with inflation, which is to

say, in the parlance of economists, that real wages are down quite a bit:

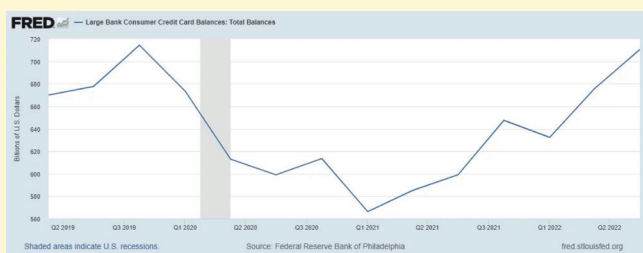


Only a few people are losing their jobs, hence the unfilled jobs stats, but many workers are merely “filling positions” instead of “creating value” and, on average, they are taking home less purchasing power. Which is worse for the economy: joblessness, or workers pretending to work for pretend pay?

I don’t know, but I do know that the personal savings rate is at a 60-year low and credit card debt is through the roof.



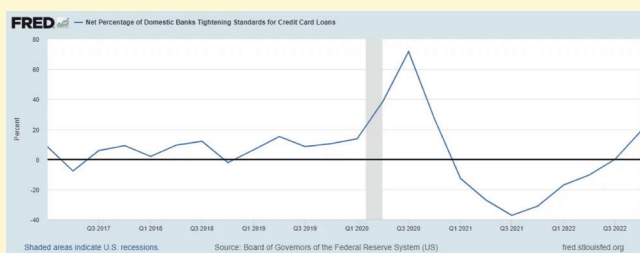
Apparently, I am not the only one who burned through his liquid savings, stopped paying into his 401K, and ran up card balances in 2022.



Credit card default rates are below their pre-pandemic level, but trending strongly upward.



Card issuers are already tightening standards.



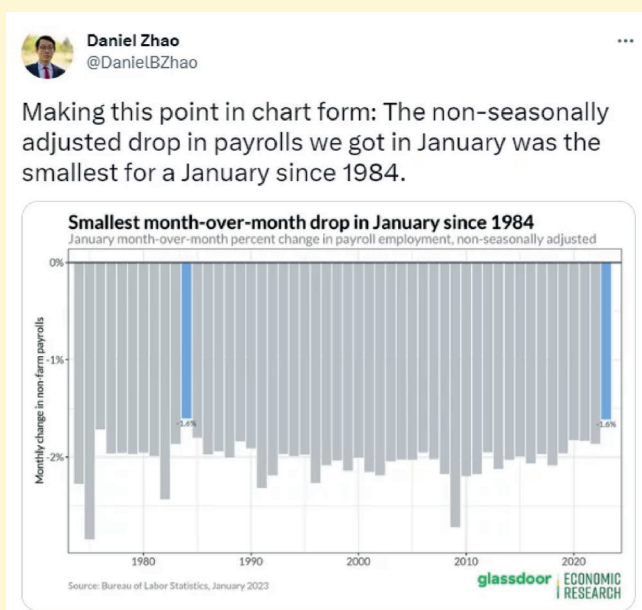
Automobile loan defaults are up too, especially among the youngest borrowers.

This all suggests that although consumers expect much worse business conditions in the near future, as the LEI shows, they still might be too optimistic. Surveys are notoriously bad because respondents have no skin in the game and hence may answer based on what they think the pollster wants to hear. Although this is a long-standing issue, it may have gotten worse over the last few years as partisanship has gripped the nation’s political discourse and people rightfully fear social or economic retribution for sharing disfavored views. Even if they respond truthfully, people’s views might be skewed more than in the past due to the rampant dissemination of economic disinformation on traditional and social media. (See the debate over the definition of recession in the summer of 2022 for some insights into the extent of this emerging problem.)

Case in point: Many Americans may actually believe that the US economy added jobs in January 2023 because of the Department of Labor posting dismisinfoganda like this on its website:



In fact, the reported numbers are seasonally adjusted. What actually happened is that the economy shed fewer jobs than in a typical January.



Journalists and social media bulls (or dollar bears) who want the Fed to stop increasing interest rates don't add that crucial context, though, inducing people to think everything is just dandy.

The S&P Index is another component of the LEI. The stock market is a great leading indicator, as stock prices are theoretically just the discounted present value of expected future earnings. It is up ever so slightly but in real terms it, like wages, is actually down considerably since its December 2021 high.

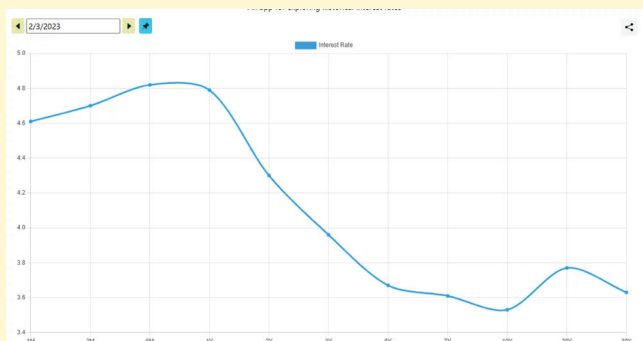
Moreover, the S&P trends upwards over long periods, which is why investment advisors suggest

buying stocks, especially when investors are young. But part of the reason that it trends upward is because most Americans have few other choices when it comes to their retirement savings. Sure, there are bonds and REITS and such but every week, week after week, the bulk goes into the same 500 "stonks." In short, the stock market doesn't just reflect expected future earnings, it also reflects expectations about future stock prices going up, simply because there aren't many viable alternatives.

The expectation of future stock prices independent of earnings increased recently with the passage of Secure 2.0 as part of the 2022 Omnibus monstrosity. That part of the bill mandates that employers automatically enroll workers in 401Ks starting in 2025. Moreover, contributions must increase one percent annually until they reach at least 10 percent. Workers can opt out, so this is, for now, a nudge policy rather than forced savings, but it's well understood that most workers will not, in fact, bother to unenroll, at least at first.

The LEI contains two other financial indicators, something called the Leading Credit Index, and a rough measure of the yield curve (10-year Treasury yields minus the federal funds rate). Inversion of the yield curve (short term yields > long term yields on bonds of comparable default and liquidity risk) has long been a tried and true recession indicator. The Treasury yield curve has been inverted for some time but in a unusually kinked fashion that the LEI's simple measure does not capture:

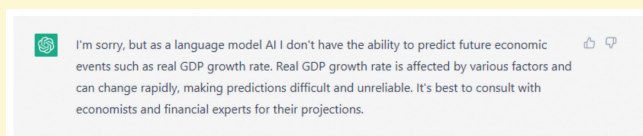




Source: <https://www.ustreasuryyieldcurve.com/>

The shape of the curve would traditionally have been taken to mean that bond-buyers think the economy is going to be flat in 2023 before heading downward in 2024. Maybe, though, the government is manipulating the curve (deliberately or not), or maybe bond buyers are also having a difficult time figuring out the US economy's future direction. It is almost as if they are waiting to see if some big event, perhaps a war or AI boom, will occur.

Composed of six indicators, including some interest rate spreads and some surveys of bank loan officers and investors, the Leading Credit Index is slightly negative. The tricky thing is weighting the six indicators properly, given rapidly changing structural conditions like the increased use of AI in lending and investment decisions. AI, or ChatGPT anyway, is of no use divining what the right weights should be. When I queried what America's real GDP growth rate would be this year, it responded:



Private Housing Building Permits, another component of the LEI, are also down. Perhaps it is also a bit too optimistic when viewed in context. New housing starts were down even more than permits in 2022, suggesting that the permit drop lag rate (permits

pulled but unused for longer than usual) has increased, likely due to recession fears and higher interest rates.

The remaining four components of the LEI – the ISM New Order Index, average weekly hours of manufacturing workers, non-defense, non-aircraft capital goods orders, and consumer goods orders – all relate to the manufacturing sector. They are all down or flat, indicating that the next quarter cannot be good. New orders can turn quickly, but why should they, given that the US economy remains trapped between the Scylla of higher interest rates and the Charbydis of higher inflation?

In short, I would keep my eye on the LEI (and AIER's equivalent) but pay special attention (overweight) to the manufacturing variables. Outside of the LEI, I would also carefully watch real wage trends and its downstream knockoffs (credit card and other debt and defaults, and the personal savings rate). Uncommon times call for uncommon measures.

– February 15, 2023

# The Childishness of Wokeism

DONALD J. BOUDREAUX

Senior Fellow

Wokeness features too many flaws even to list – never mind to discourse upon – in an essay of reasonable length. But one among these many flaws stands out for me as being the most irritating: incessant childishness.

I still recall from my days in Catholic elementary school the many times that one classmate would publicly accuse another of using a naughty word. Such accusations were always announced triumphantly, revealing the accuser's sense of heroically serving the public good by exposing a menace in our midst. Sometimes the allegation was rooted in pure ignorance of language, as when one of my fellow fourth graders used the word "asinine" and was immediately tattled on to our teacher, Sister Agnelia, as having cursed.

I don't recall whether "asinine" was used correctly, but thankfully Sister Agnelia knew that, either way, it's not a curse word. She declared the accused innocent of any wrongdoing.

Of course, genuinely verboten words such as "hell" or "damn" were sometimes uttered. Yet even as a child I always sympathized with the malefactor whenever his offense was publicly decried by another classmate, whom I invariably viewed as having committed an offense much more serious than using potty language.

Ever-vigilant against the use of naughty words, the woke are just as immature as were my prissy grade-school classmates. And the woke are also just as ignorant of the meaning of words – as was revealed several years ago when an aide to then-DC-Mayor Anthony Williams was forced to resign after being accused of uttering a racial smear when he used the word "niggardly" in a conversation about funding.

Actually, the woke are worse than even my most hyper-sensitive schoolmates. Unlike my schoolmates, who I don't recall ever consciously *manufacturing* pretenses to be offended by language, the woke are master craftsmen – sorry, master craftspeople – of such pretenses. For evidence look no further than the recent tweet from the AP's Stylebook that "We recommend avoiding general and often dehumanizing 'the' labels such as the poor, the mentally ill, the French, the disabled, the college-educated."

To be clear, because I recognize the enormous power of language, I applaud language becoming more inclusive, less racist, and less sexist. But language is organic. Its vocabulary and grammar are not conscious human constructs that can be changed at will or overnight. To take offense, for example, at the casual use of the term "craftsman" to describe a woman who earns her living as a carpenter or as a plumber is to take offense at an innocent habit of speech. It is to manufacture a justification to display one's allegedly superior sensibilities. And only immature people behave in such an obnoxious fashion.

But to take offense at the use of the article "the" requires an altogether higher degree of noxious immaturity. Immaturity of this sort is the immaturity of the playground bully who is as self-obsessed as he is destructive.

The woke are childish also in seeing the world only in black and white. Being woke to today's injustices apparently entails ignoring reality's complexities and uncertainties. It also seems to entail disregarding the fact that much that appears evil or undesirable is the result, not of bad or benighted actors, but instead of people making difficult and

unavoidable tradeoffs.

Nuance, apparently, is a mirage seen only by the selfish, while humility is a trait possessed only by the benighted.

Consider the example of trans rights for minor children. As reported by *Washington Post* columnist Megan McArdle, many among the woke want to dilute the say of parents in their children's decisions to transition from one gender to another. Yet regardless of your stance on the larger issue of trans rights, parental responsibility and parents' love for their children remain very real considerations. McArdle correctly suggests that to label as "transphobic" someone who merely argues that the state should not override parents' say in the medical treatments received by their minor children – especially when the exercise of that say doesn't put children's lives in jeopardy – is to childishly ignore the danger of stripping parents of this vital responsibility.

Whatever good might be imagined as coming from stripping away parental responsibility in this particular case is a 'good' purchased at the price of diluting the ability of those persons who love and who know their children the most – parents – from raising their children as they judge best. Only an immature mind would assert that this price is unquestionably one worth paying. Surely someone who resists diluting parental responsibility in such instances is not a knuckle-dragging ignoramus or an evil religious fanatic but, instead, someone who understands the reality of parental love and the value – both to children and to society – of parental responsibilities exercised because of that love.

Yet another manifestation of the woke's childishness is their interpretation of everything through the lens of imagined intentions. Is the average pay of women lower than that of men? Yes. *The reason must be that society is engineered by men to 'privilege' men at the expense of women!* Is the

number of Blacks enrolled in high-school honors courses disproportionately small? Yes. *The reason must be that school curricula and testing methods are designed to 'privilege' whites and Asians at the expense of Blacks!*

Sometimes, of course, bad intentions are at work. But for many of the social and economic issues that dominate public-policy discussions, differences in the 'outcomes' of different groups are the results, not of intention or design, but of innumerable decisions each made by individuals who strive to strike in the best way they can the inescapable trade-offs they confront. The woman who chooses to temporarily leave the workforce in order to be a full-time mom often thereby loses some workplace skills, and upon returning to the workplace is paid less than she would have been paid had she never had kids. Women's average pay, in turn, is pulled down relative to men's average pay. But in operation here is no pernicious design. Yet the childish mind, unable to appreciate the reality of unintended consequences and the inescapability of trade-offs, jumps to the conclusion that women's lower average pay is the result of male chauvinism and discrimination.

One final childish trait of the woke is worth mentioning – namely, their infantile inability, or refusal, to put matters into proper perspective. It's undeniably true that some individuals are racist while others are xenophobic, that some men are sexist, and that some people are homophobic. Such will always be the case, sadly so. But there's no question that racism, xenophobia, sexism, and homophobia are far less commonplace in America today than they were even just a few decades ago. Yet the woke seize upon every reported instance of such intolerance – reports which themselves are amplified by social media – as evidence that American society is suffused with incurable racism, xenophobia, sexism, and homophobia. Because the woke are far more interested in displaying their own imaginary moral



superiority than they are in understanding reality, they refuse to recognize the overwhelming civility and tolerance of modern American society. Like children, the woke's understanding of the society they inhabit is defective. Unfortunately, unlike children, they occupy prominent places in the media, in the academy, and in officialdom.

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# Reimagining Fusionism

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Amidst the on-going differences that presently divide the American right, about matters ranging from economic policy to the proper understanding of the US Constitution, one word has been cited with considerable frequency, usually in tones of praise or disdain. That word is “fusionism.”

For many national conservatives, the fusionist project, associated with names like William F. Buckley and Frank Meyer that sought to integrate the “classical liberal” emphasis on freedom with the “conservative” focus on virtue and tradition, is finished. In practice, they claim, it emphasized the liberty half of the fusionist equation (especially in the economic realm) but downplayed or even ignored the virtue and tradition half. That, they argue, contributed to the reticence of some on the right to acknowledge—let alone work to roll back—the genuine rot in American culture epitomized by the woke phenomenon that calls, they believe, for more pro-active responses, including from the state.

Many classical liberals dispute this analysis. Does the federal government’s unending growth since FDR, including during Republican administrations, really suggest that wild-eyed libertarians have been running the right’s economic policies for the past 90 years? They also argue that some conservatives’ desire to deploy state power to try and revive a culture of virtue risks further opening the door to an ever-expanding role for government—one that won’t always be directed by conservatives, and which the left will use to realize various nefarious ends whenever and wherever they hold power.

There is, however, something dissatisfying about the contours of contemporary commentary on fusionism. Its history is often presented primarily in

terms of strategy and tactics: i.e., getting American classical liberals, traditionalists, and free market economists on the same political page over and against the postwar progressive left and, more widely, the menace of the Soviet Union.

In this telling, thinkers like Meyer are presented as providing intellectual window-dressing to a pragmatic exercise in coalition-building. Communism’s collapse in Eastern Europe and the U.S.S.R.’s dissolution, it is held, removed a common enemy which was the essential glue that held the fusionist coalition together. Suddenly, the argument goes, many long-suppressed debates on Planet Fusionism, where a live-and-let-live status quo had hitherto prevailed, were up for grabs.

There’s some truth to that story. Meyer was as much an activist as a thinker, and coalition building is the lifeblood of successful political activism. The very nature of political coalitions is that you have to be willing to give up, say, 20 percent of what you want in order to realize 80 percent of your agenda.

Yet this account of fusionism is also an inadequate one. For one thing, fusionism never resulted in the marginalization of strong disagreements across the American center-right spectrum.

Consider, for instance, the disagreements between the classical liberal F.A. Hayek and the conservative Russell Kirk in the 1960s about the respective meanings of liberalism and conservatism. You can also go back and read some of the debates that occurred at venues like the Philadelphia Society. No one appears to have had much hesitation about engaging in vigorous disagreement about many issues in those circles where fusionism was regarded as a powerful influence.

Some of that disagreement also concerned Meyer's writings. They attracted significant criticism from some libertarians as well as particular traditionalists. Some held that Meyer's effort at fusion didn't integrate enough of their priorities and concerns. Others argued that the differences were simply too great.

Nor is it clear that fusionism was as driven by pragmatic political imperatives as is often supposed. To understand this, we need only look at Meyer's writings on the topic.

To be sure, Meyer's work was not the type of exercise in detailed political and economic analysis as, say, Hayek's *The Constitution of Liberty* or Wilhelm Röpke's *A Humane Economy*—let alone something on the scale of Adam Smith's *Wealth of Nations*. Texts like Meyer's *In Defense of Freedom* do have an air of incompleteness about them.

That said, the intellectual strength of Meyer's endeavor lay in his effort to trace the respective roots of the liberty and tradition camps back to particular streams of thought in the tradition of Western civilization. Meyer wanted to illustrate how these emphases had manifested themselves and, in many instances complemented each other, in the works of perennial classical and modern thinkers that people on the “non-left” recognized as among their intellectual forebears.

After all, questions surrounding the relationship between freedom, virtue, and tradition were hardly a phenomenon unique to the mid-twentieth century. Figures as varied as Thomas Aquinas, John Locke, Adam Smith, Edmund Burke, Thomas Jefferson, Thomas Paine, John Adams, Alexis de Tocqueville, and Lord Acton, as well as individuals like Hayek, Kirk, Buckley, and Röpke after World War II, wrestled with these matters and the associated tensions at length.

That's not to say that these thinkers arrived at the same conclusions about the precise relationship

between freedom and virtue (let alone a consensus on policy matters). They didn't. But one can find broad agreement in the writings of most of these individuals upon a number of axioms. These might be summarized along the following lines:

- Humans alone are capable of freedom. The social, economic, and political order should reflect that truth.
- Virtue is indispensable for a free society, not least because in the absence of a culture in which virtuous behavior prevails, liberty becomes difficult to sustain and hard to distinguish from libertinism.
- Pursuing the life of virtue requires a significant degree of liberty, to pursue knowledge of truth and to make choices between those habits which reflect consistent embrace of things like prudence, temperance, justice, and courage, versus the vices that represent their opposite (recklessness, hedonism, injustice, and cowardice).
- There are principled limits on what the state can do in terms of encouraging virtue and discouraging vice. Certainly, there is no such thing as morally neutral law. Nonetheless, law must allow significant, even wide space for people to make free choices, including choices that are not objectively good for people to make. It is only through free choice that people become moral or otherwise.
- Free markets, constitutionalism, rule of law, and the mediating institutions that we call civil society, which limit state power, depend on the existence of particular habits and attitudes that are objectively good in moral terms.
- Particular traditions embody and convey information that we may not fully understand, but nonetheless help societies to remain free and make it easier for us to pursue virtue and reject vice. Tradition can also help to promote virtue

and discourage vice through supporting the authority of non-state institutions to which people voluntarily adhere.

This is not an exhaustive list. But taken together, these axioms combine a number of “classical liberal” and “conservative” emphases that, it turns out, tend to support each other. They do provide a framework, even a common ground that, at a minimum, reflects a concern that liberty does not degenerate into libertinism, and that respect for tradition and recognition of virtue’s importance doesn’t become a rationalization for the destruction of freedom.

Certainly, that framework doesn’t definitively settle the stances of classical liberals and conservatives towards any number of questions, let alone generate uniform economic and social policies. But it does provide a number of principled starting points for classical liberals and conservatives to develop commonly grounded responses to particular challenges facing the United States.

One such challenge concerns how to address the serious policy and institutional wreckage that litters America’s social, economic, and legal landscape and which is a legacy of the progressive movement. Another is how to respond to the contemporary left’s desire to reduce freedom to self-expression and collapse the tradition of the West, especially its American manifestations, into one long story of oppression.

As conservatives and classical liberals tackle these issues, fusionist emphases would go some way to remind them that, however they do so, the simultaneous preservation and promotion of liberty and virtue is the point of the exercise. It also provides principled, rather than simply pragmatic, foundations upon which they can propose alternative institutional arrangements and policies to those favored by progressives.

Fusionism in this scenario is less about creating a permanent philosophical synthesis of classical

liberalism and conservatism than it is concerned with identifying principled points of reference that conservatives and classical liberals agree are crucial if liberty and virtue are to buttress each other. At the same time, fusionism in this sense separates such individuals from those conservatives who don’t regard liberty as especially important, as well as those classical liberals who view concern for virtue and respect for tradition as likely obstructions to the exercise of freedom.

This may add up to a somewhat different fusionism to that developed by Meyer. But a great deal has changed in America since he and others worked on these questions. It could even be argued that the word “fusionism” may have had its day. We’re not living in the 1970s or 1980s anymore, and few remain of the generation who were invested in the term.

But the expression itself is less important than the fact that the precise mixture of principles, ideals, and institutions identified by fusionist thinkers as important happens to express key principles of the American Founding, whose leading thinkers regarded liberty and virtue as mutually reinforcing. Such principles and ideals are also what the contemporary left is so intent on dismantling these days.

For the contemporary left, liberty has little to do with virtue in any classical sense of the word. Liberty, in their view, is ultimately about self-expression. As for virtue, the very idea has been reduced to signaling to everyone else that you are a good person “by virtue” of associating yourself with progressive causes. Similarly, tradition is increasingly viewed by the left through the lens of cultural Marxism, which sees oppression everywhere.

In such times, the primary significance for any revitalization of fusionism in our time may well be that of reminding classical liberals and conservatives what is at stake by pointing to principles that many in both camps consider to be important *à* that

matter if America's experiment in ordered liberty is to endure. Such a project is much more than an exercise in political pragmatism. It's also about underscoring what is needed for any society if it wants to remain free and civilized.

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