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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 8 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

www.aier.org

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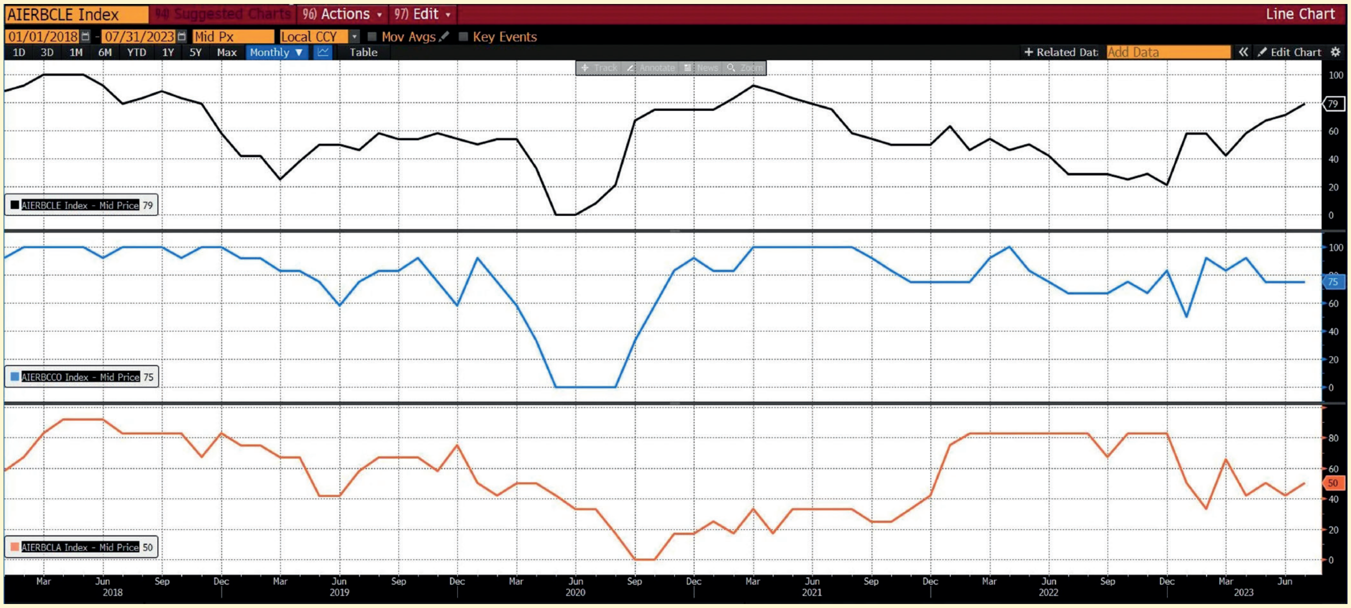
BUSINESS CONDITIONS MONTHLY

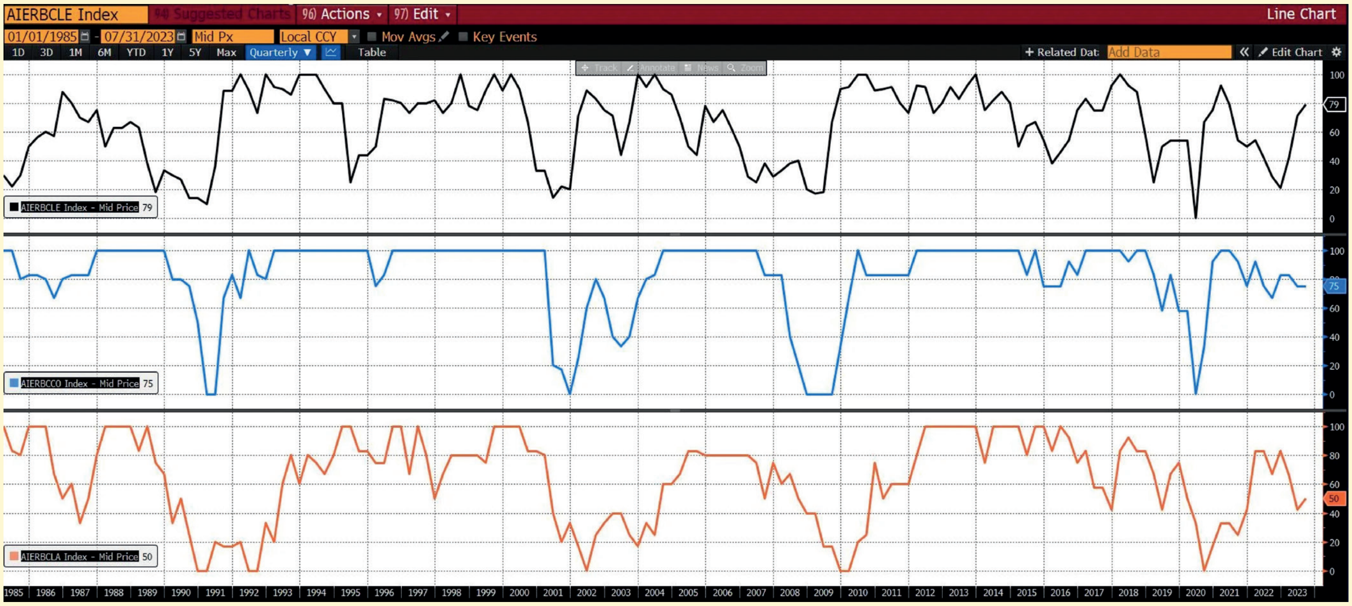
Peter C. Earle
RESEARCH FACULTY

n July 2023, AIER's Business Conditions Monthly took varied turns. While the Leading Indicator edged up from 71 to 79, the Roughly Coincident Indicator remained at its June 2023 level of 75. The Lagging Indicator turned from slightly contracting to neutral, rising from 42 to 50.

AIER Business Conditions Monthly (5 years)



AIER Business Conditions Monthly (1985 – present)



Leading Indicators (79)

With the rise from 71 in June 2023 to 79 in July, the Leading Indicator Is at its highest level since June of 2021 (79). Eight of the twelve leading indicators rose, three met the criteria of unchanged or neutral, and one declined in July 2023. Rising were the University of Michigan Consumer Expectation Index (11.1 percent), United States Heavy Truck Sales (8.2 percent), Debit Balances in Customers' Securities Margin Accounts (4.2 percent), US Initial Jobless Claims (2.4 percent), the Conference Board US Leading Index of Manufacturers New Orders, Consumer Goods, and Materials and Leading Index of 500 Stock Prices (1.3 percent and 3.7 percent, respectively), US New Privately Owned Housing Unit Starts (1.3 percent), and Adjusted Retail and Food Service Sales (1 percent). US Average Weekly Hours (All Employees, Manufacturing), the Conference Board US Manufacturers New Orders of Capital Goods Excluding Aircraft, and the US Census Bureau's Inventory to Sales Ratio (Total Business) were neutral/unchanged. The 1-to-10 year US Treasury spread narrowed by 10.2 percent.

Roughly Coincident (75) and Lagging Indicators (50)

The Roughly Coincident Indicator retained its reading of 75 from the previous month. With the exception of a sudden dip to 50 in January 2023, for the nearly three years since October 2020, the Roughly Coincident Indicator has shown various degrees of expansion with an average reading of 83.

Among the six constituents of the Roughly Coincident Index, four saw expansion, one was neutral, and one declined. US Industrial Production rose by 0.6 percent while US Employees on Nonfarm Payrolls grew 0.9 percent from June to July. The Conference Board's Coincident Manufacturing and Trade Sales and Personal Income Less Transfer Payments measures increased (0.8 percent and 0.4 percent, respectively) while the Consumer Confidence Present Situation declined 1.5 percent. The US Labor Force Participation Rate was unchanged.

Other than a reading of 66 in March 2023, since January the Lagging Indicators have been in neutral to slightly contracting territory ranging from 33 to 50.

The six components of the Lagging Indicator were evenly split among rising and falling releases. Average 30-day yields rose by 4.3 percent, the Conference Board US Lagging Average Duration of Unemployment increased by 0.5 percent, and the Census Bureau's US Private Construction Spending (Nonresidential) was up 0.5 percent in July. Declining were Core CPI (2.1 percent), US Manufacturing and Trade Inventories (0.2 percent), and Conference Board US Lagging Commercial and Industrial Loans (0.5 percent).

Discussion

AIER's Business Conditions Monthly indicators have, since the start of the year, told three different stories. One of growing strength, as the Leading Indicator has trended up from 21 in December 2022 to 79 in July 2023. Another is of slowing expansion, as seen in the Roughly Coincident Indicator's slide from 92 in February to 75 for the last three months (May, June, and now July 2023). And over that same time period the Lagging Indicator has oscillated between a February low of 33 to a March high of 66 indicating overall neutrality in its components. While the degree of correlation between the three would likely trend in roughly lagged parallel, the starkly conflicting readings bear evidence of the continuing disorientation of economic trends: not only from unprecedented pandemic policy measures, but the intervention-laden recovery period that followed.

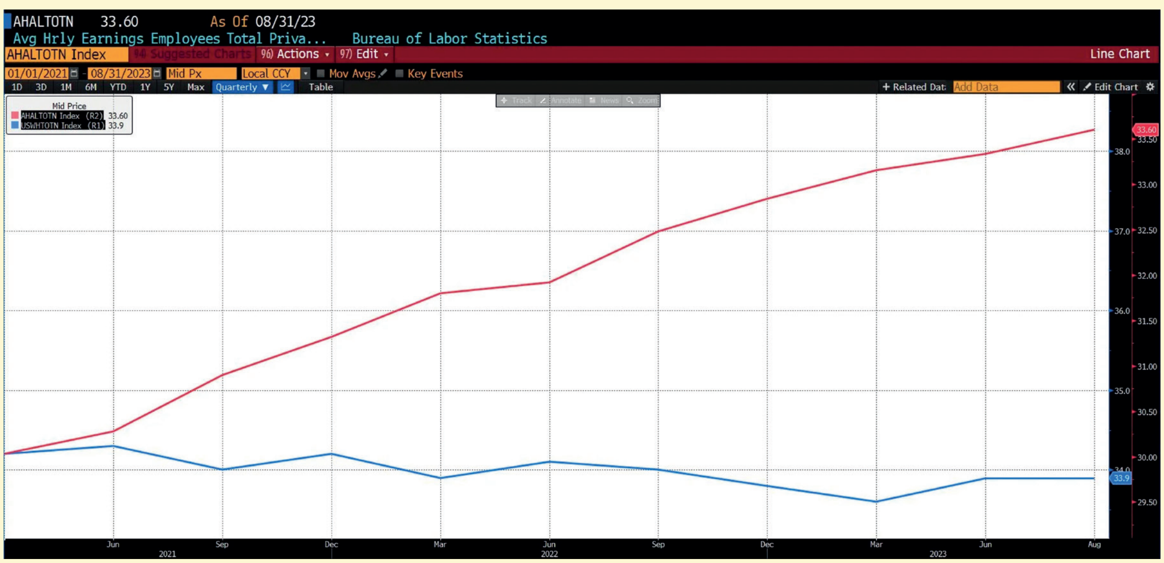
In June and July 2023, based on an unanticipatedly strong 2nd quarter US GDP number as well as positive data on US employment, consumer activity, growth in nonresidential fixed investment, and continuing disinflationary progress, soft landing predictions gathered purchase. Recent data, however, hints at those prognoses being premature at best. Labor markets are rapidly cooling, and there is growing evidence that headline payroll numbers have overstated the strength of the US job market. Monthly payroll estimates have also been subject to persistent downward revisions as hiring activity has declined.

(Although after the time period that this report contemplates, we know now that the U-3 US Unemployment Rate rose from 3.5 percent to 3.8 percent between July and August 2023.)

Furthermore, in late August the US Bureau of Labor Statistics (BLS) announced the completion of its preliminary re-benchmarking of the national Current Employment Statistics. The initial result of that revision indicates that as of March 2023 US nonfarm payrolls were overestimated by approximately 306,000 jobs (0.2 percent). This is roughly twice the historical average of other such revisions and the fourth largest on record. (Details on the process and consequent revisions are shown on aier.org.) Not only does this mean that job numbers have been overstated, but upward revisions in such sectors as government jobs, utilities, and construction (the latter driven in part by government spending on infrastructure and subsidies for nonresidential fixed investment) reveal the source of certain pockets of growth in the US economy. (A discussion of the breakdown of 2nd quarter US GDP, in particular the disproportionate contribution of nonresidential fixed investment, can be revisited on aier.org.)

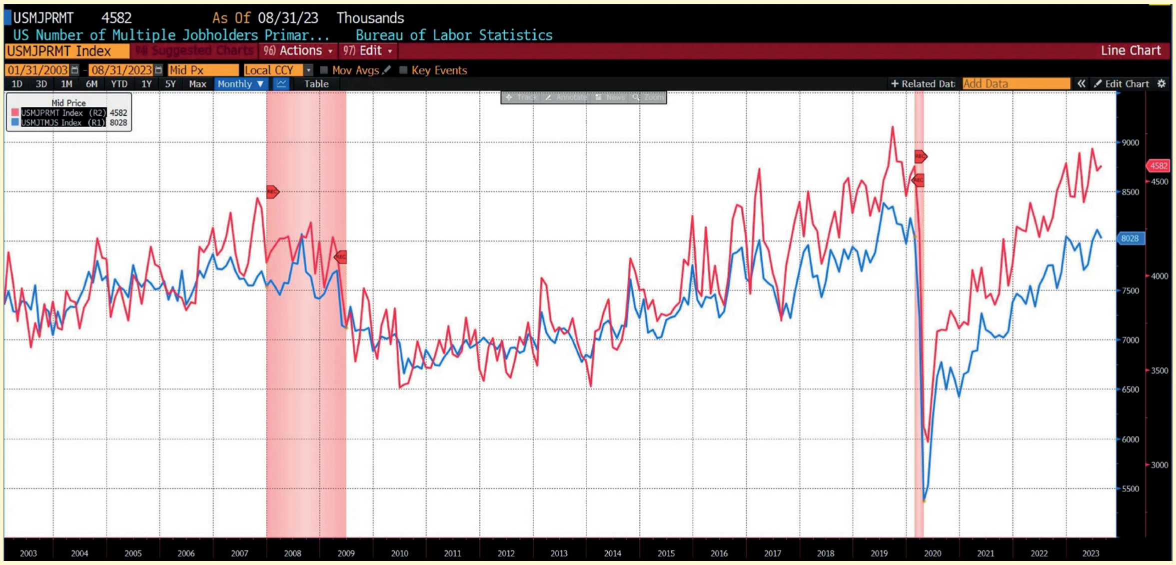
While hourly wages have grown over the past few years since the pandemic ended, both inflation and a trend of gradually declining average weekly hours worked has mitigated much of the benefit of that uptrend.

Average US Hourly Earnings Total Private Employees & Average Weekly US Hours Private Nonfarm Payrolls (both NSA), 2021 – present



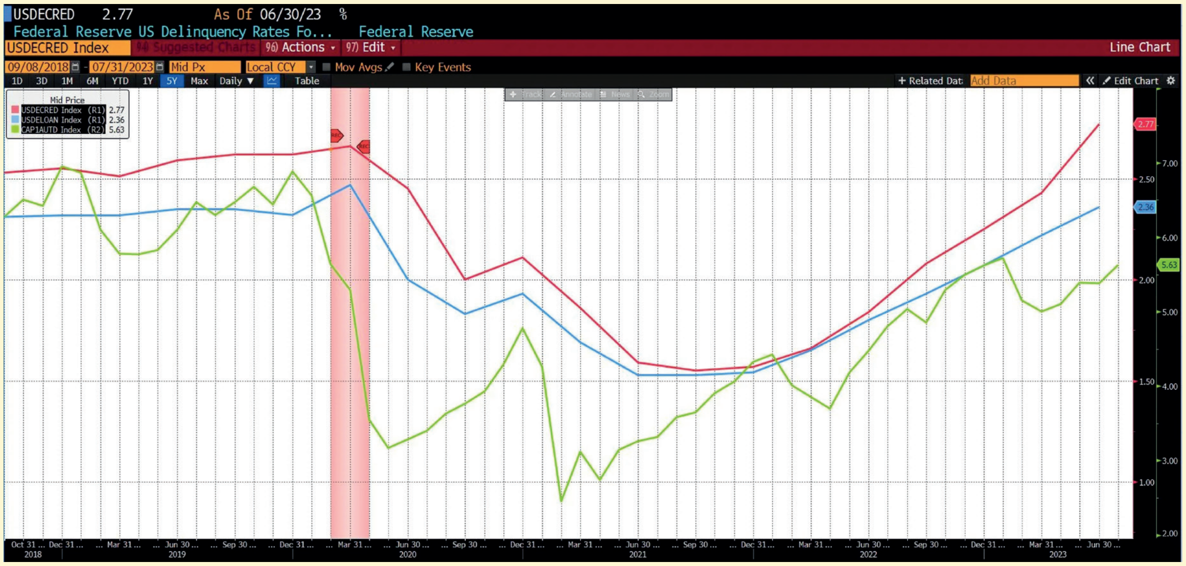
Additionally implying pressure on consumers, since the end of the pandemic workers reporting both a full- and part-time job and two full-time jobs have surged. These statistics, moreover, are likely underestimated as many secondary jobs are undertaken informally on an unreported income basis.

US Number of Multiple Jobholders, Total & US Number of Multiple Jobholders, Primary FT/Secondary FT (both SA), 2003 – present



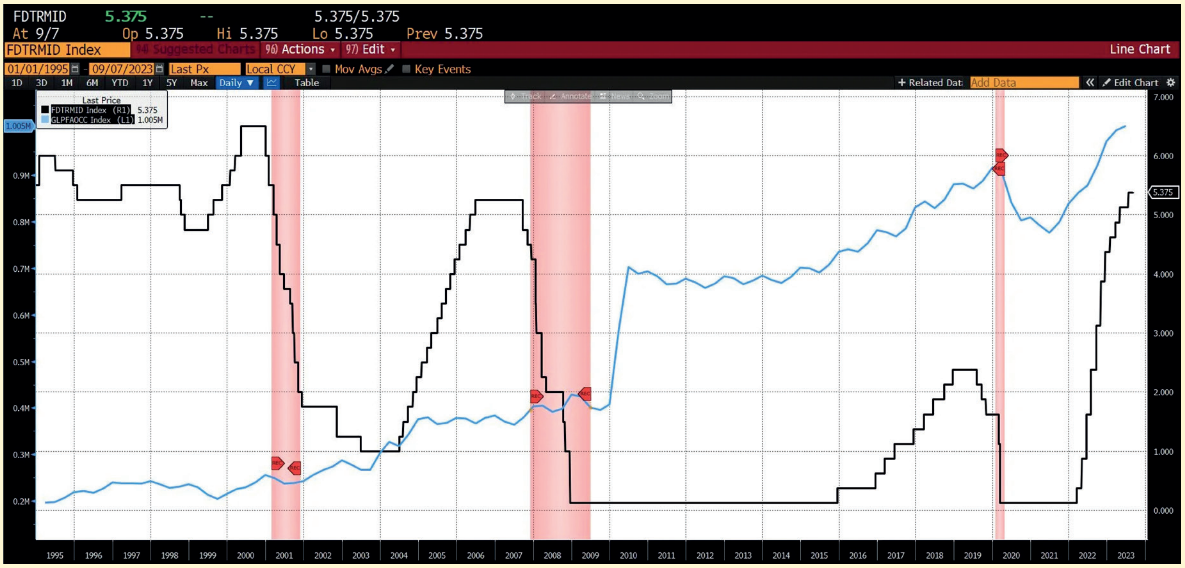
While increasing slack in US labor markets and effectively declining wages are aiding the deflationary trend, the outlook for ongoing consumer strength (which accounted for nearly half of the second quarter US GDP result) is consequently poor. Pandemic savings are nearly exhausted, and 30-day default rates on car loans and general consumer loans are approaching pre-pandemic highs. Credit card debt default rates now exceed pre-COVID levels.

Federal Reserve US Delinquency Rates for All Banks Credit Cards, Federal Reserve US Delinquencies for All Consumer Loans, and Capital One 30-day Delinquencies Auto Finance, 2018 – present



The average rate of interest on credit card balances is now at an all-time high of 20.63 percent, up from 16.34 percent in March 2022 when the Federal Reserve began its contractionary policy campaign. Over that period of time, outstanding credit card debt has risen from approximately $860 billion to over $1 trillion. Unlike previous cycles in which outstanding credit card debt has flattened or risen slightly when the Fed has raised rates more than one or two percent, total credit card debt has increased by 16.3 percent while Fed Fund rates have increased more than tenfold.

Fed Fund target (mid) & Federal Deposit Insurance Corporation Outstanding Credit Card Balance, 1995 – present



Mortgage rates (both 15-year and 30-year fixed) have more than doubled since the end of the pandemic.

Bankrate.com US Home Mortgage 15-year and 30-year Fixed Rate, 2021 – present

Many retailers, most notably deep discounters such as Dollar General, have been reporting headwinds to second quarter earnings. Several weeks ago, LendingClub Corporation released the 25th edition of its New Reality Check: Paycheck-to-Paycheck research, which "examines the impact of nonessential spending on consumers' ability to manage expenses and put aside savings." The findings (which can be reviewed in full on aier.org.) derive from July 2023 survey responses, and include the following estimates:

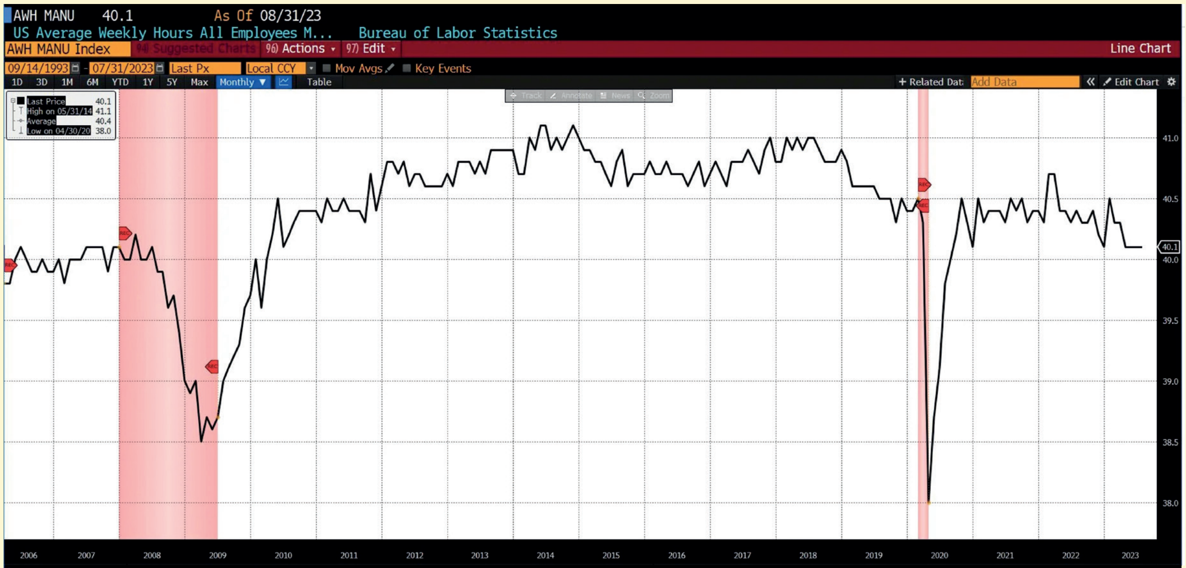
- Some 61 percent of US consumers live paycheck-to-paycheck
- Roughly one fifth of US consumers are struggling to make bill payments
- Sixteen million (10 percent of the paycheck-to-paycheck population) US consumers claim that frivolous spending is the primary reason for constrained personal finances

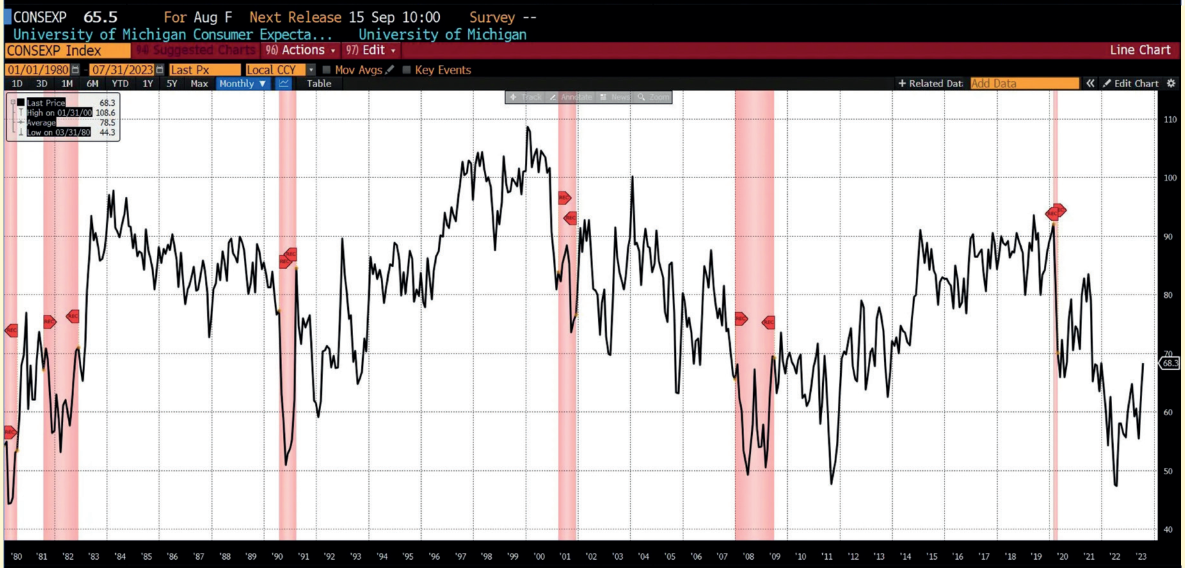
Elsewhere, a year-long survey of over 8,000 consumers reported that

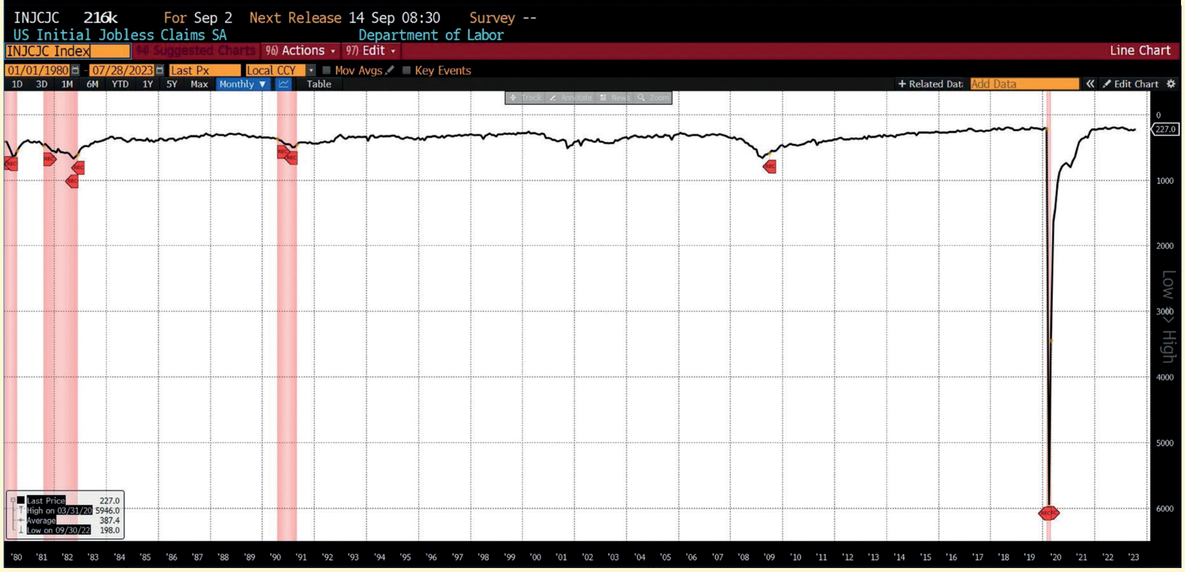
- Nearly one-third of Americans are skipping meals owing to financial concerns
- Americans believe that inflation in food-at-home items is over 22 percent year-over-year versus the 7.1 percent rate reported by BLS
- 62 percent of Americans, 72 percent of families, and 75 percent of US consumers between the ages of 18 and 44 would have trouble paying an unexpected $400 expense

In summary, and with the caution that should attend social science empirics: a weakening US job market on top of the increasingly encumbered financial circumstances of many US citizens renders the continuation of robust consumption doubtful. The impending resumption of student loan payments in October 2023 is likely to aggravate those trends, and if deleterious enough may prompt renewed attempts at political intervention.

It remains possible that the buoyancy provided by government spending via the Bipartisan Infrastructure Act, Inflation Reduction Act, and the CHIPS and Science Act may keep the US economy from entering a "statutory" recession. But strained consumers, contracting manufacturing, rising energy prices, the risk of over-tightening by the Fed, and other developing trends are apt to be less amenable to manipulation. The prediction that the United States will enter an economic recession on or before September 2024 stands.

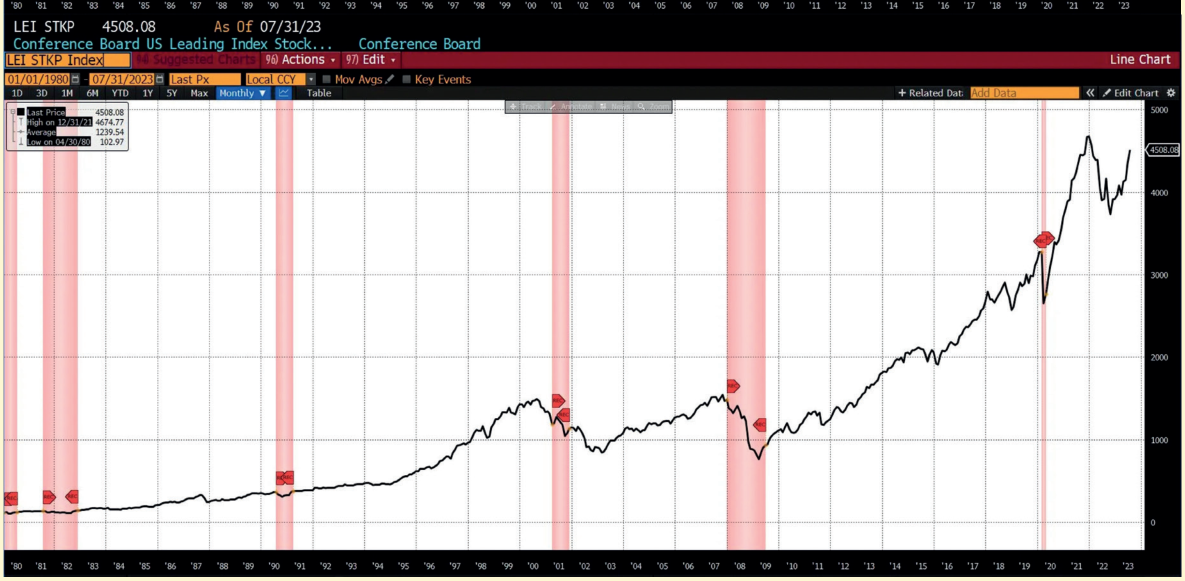

AWH MANU 40.1 As Of 08/31/23
US Average Weekly Hours All Employees M... Bureau of Labor Statistics
AWH MANU Index
Actions
Edit
Line Chart
09/14/1993 - 07/31/2023 Last Px Local CCY Mov Avgs Key Events
1D 3D 1M 6M YTD 1Y 5Y Max Monthly Table
Related Dat Add Data Edit Chart
Last Price 40.1
High on 05/31/14 41.1
Average 40.4
Low on 04/30/20 38.0
41.0
40.5
40.0
39.5
39.0
38.5
38.0
2006 2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017 2018 2019 2020 2021 2022 2023


CONSEXP 65.5 For Aug F Next Release 15 Sep 10:00 Survey --
University of Michigan Consumer Expecta... University of Michigan
CONSEXP Index
Actions
Edit
Line Chart
01/01/1980 - 07/31/2023 Last Px Local CCY Mov Avgs Key Events
1D 3D 1M 6M YTD 1Y 5Y Max Monthly Table
Related Dat Add Data Edit Chart
Last Price 68.3
High on 01/31/00 108.6
Average 78.5
Low on 03/31/80 44.3
110
100
90
80
70
60
50
40
'80 '81 '82 '83 '84 '85 '86 '87 '88 '89 '90 '91 '92 '93 '94 '95 '96 '97 '98 '99 '00 '01 '02 '03 '04 '05 '06 '07 '08 '09 '10 '11 '12 '13 '14 '15 '16 '17 '18 '19 '20 '21 '22 '23

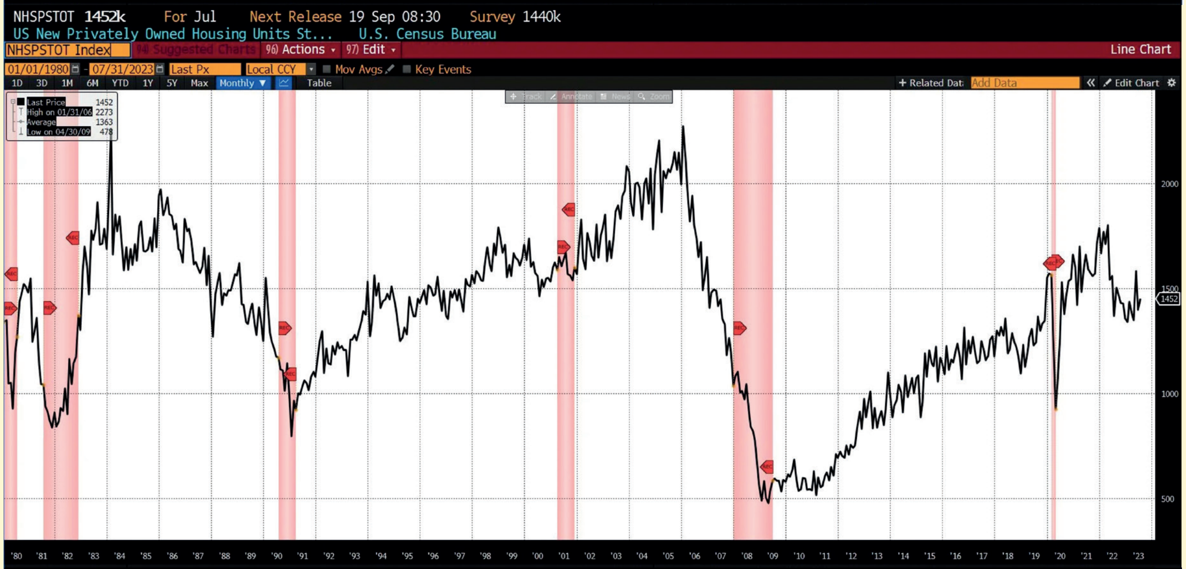

INJCJC 216k For Sep 2 Next Release 14 Sep 08:30 Survey --
US Initial Jobless Claims SA Department of Labor
INJCJC Index
Actions
Edit
Line Chart
01/01/1980 - 07/28/2023 Last Px Local CCY Mov Avgs Key Events
1D 3D 1M 6M YTD 1Y 5Y Max Monthly Table
Related Dat Add Data Edit Chart
Low > High
Last Price 227.0
High on 03/31/20 5946.0
Average 387.4
Low on 09/30/22 198.0
0
1000
2000
3000
4000
5000
6000
'80 '81 '82 '83 '84 '85 '86 '87 '88 '89 '90 '91 '92 '93 '94 '95 '96 '97 '98 '99 '00 '01 '02 '03 '04 '05 '06 '07 '08 '09 '10 '11 '12 '13 '14 '15 '16 '17 '18 '19 '20 '21 '22 '23

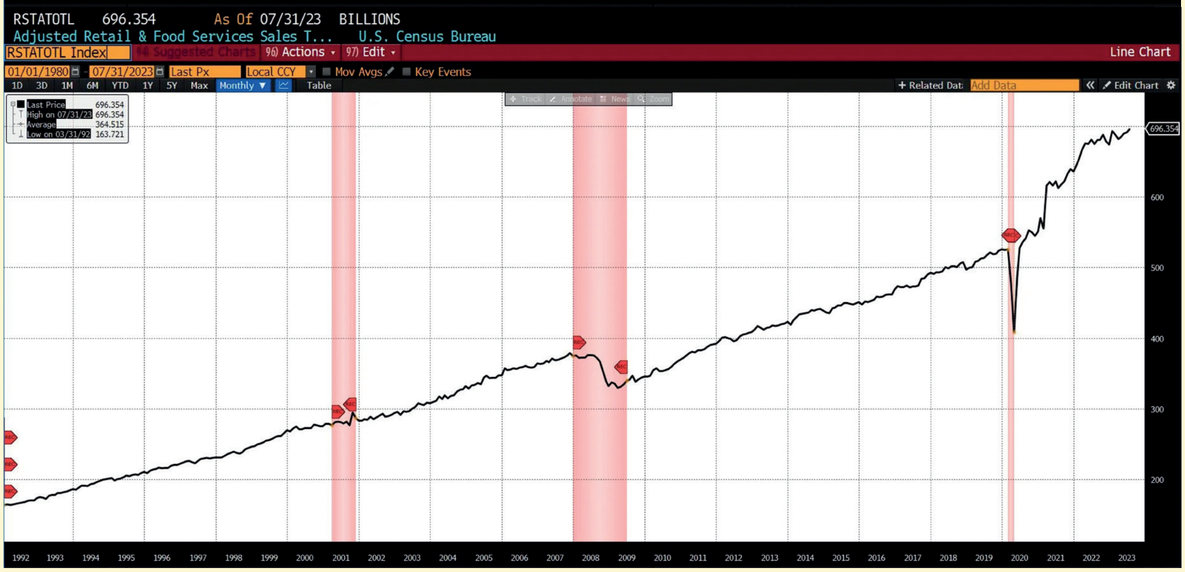

LEI NWCN 124758.00 As Of 07/31/23 MILLIONS
Conference Board US Leading Index Manuf... Conference Board
LEI NWCN Index
Line Chart
01/01/1980 - 07/31/2023 Last Px Local CCY Mov Avgs Key Events
Last Price 0.125M
High on 01/31/00 0.158M
Average 0.126M
Low on 10/31/82 82255.00


LEI MNO 34980.00 As Of 07/31/23
Conference Board US Manufacturers New O... Conference Board
LEI MNO Index
Line Chart
01/01/1980 - 07/31/2023 Last Px Local CCY Mov Avgs Key Events
Last Price 34980.00
High on 06/30/00 49202.00
Average 34998.72
Low on 12/31/82 20990.00


LEI STKP 4508.08 As Of 07/31/23
Conference Board US Leading Index Stock... Conference Board
LEI STKP Index
Line Chart
01/01/1980 - 07/31/2023 Last Px Local CCY Mov Avgs Key Events
Last Price 4508.08
High on 12/31/21 4674.77
Average 1239.54
Low on 04/30/80 102.97

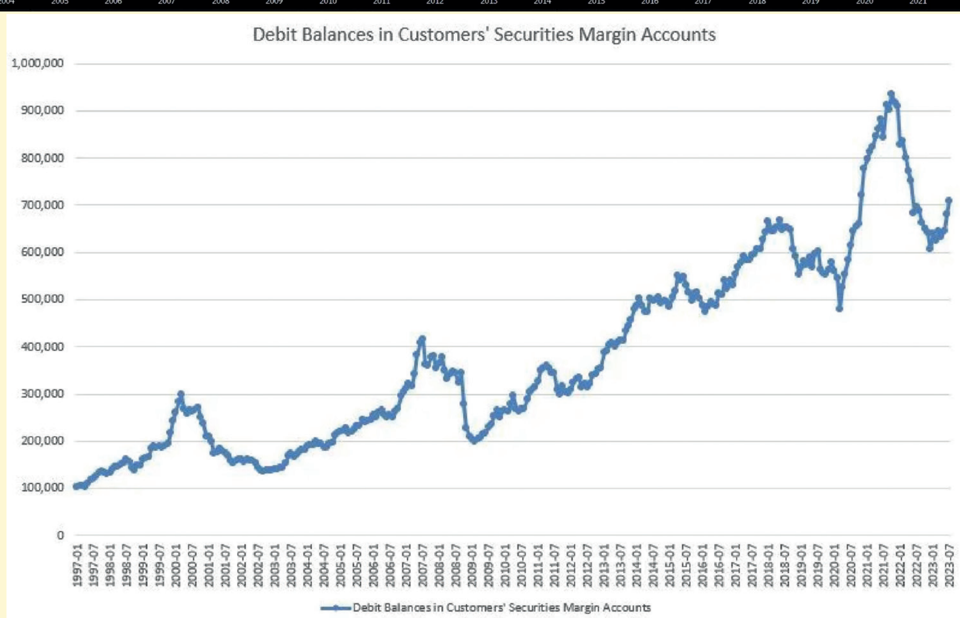

MGT2TB 1.40 As Of 06/30/23 SA
Inventory/Sales Ratio : Total Business U.S. Census Bureau
MGT2TB Index
Line Chart


NHSPSTOT 1452k For Jul Next Release 19 Sep 08:30 Survey 1440k
US New Privately Owned Housing Units St... U.S. Census Bureau
NHSPSTOT Index
Line Chart

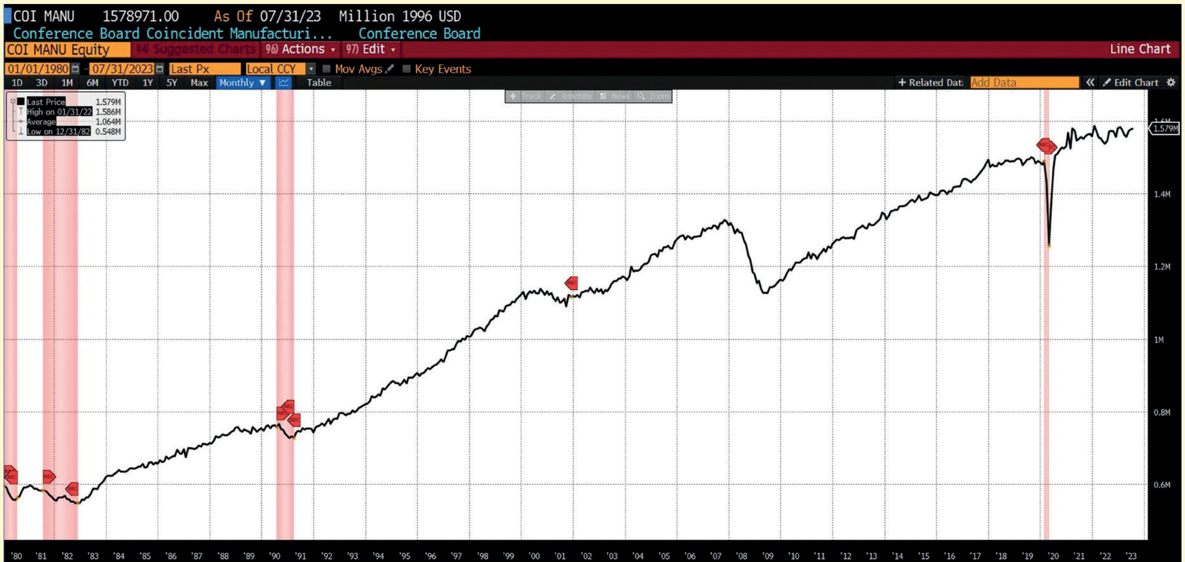

RSTATOTL 696.354 As Of 07/31/23 BILLIONS
Adjusted Retail & Food Services Sales T... U.S. Census Bureau
RSTATOTL Index
Line Chart

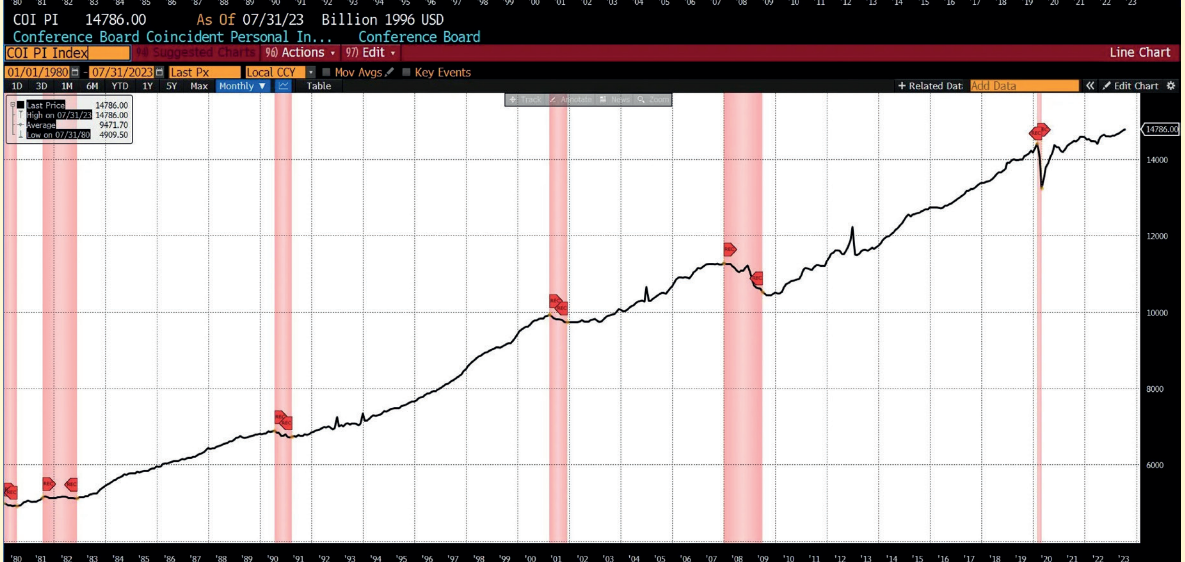

USASHVTK 0.512 As Of 08/31/23 Millions
United States Heavy Trucks Sales SAAR
Bureau of Economic Analysis
USASHVTK Index
Line Chart
Last Price 0.522
High on 04/30/19 0.571
Average 0.355
Low on 10/31/82 0.159

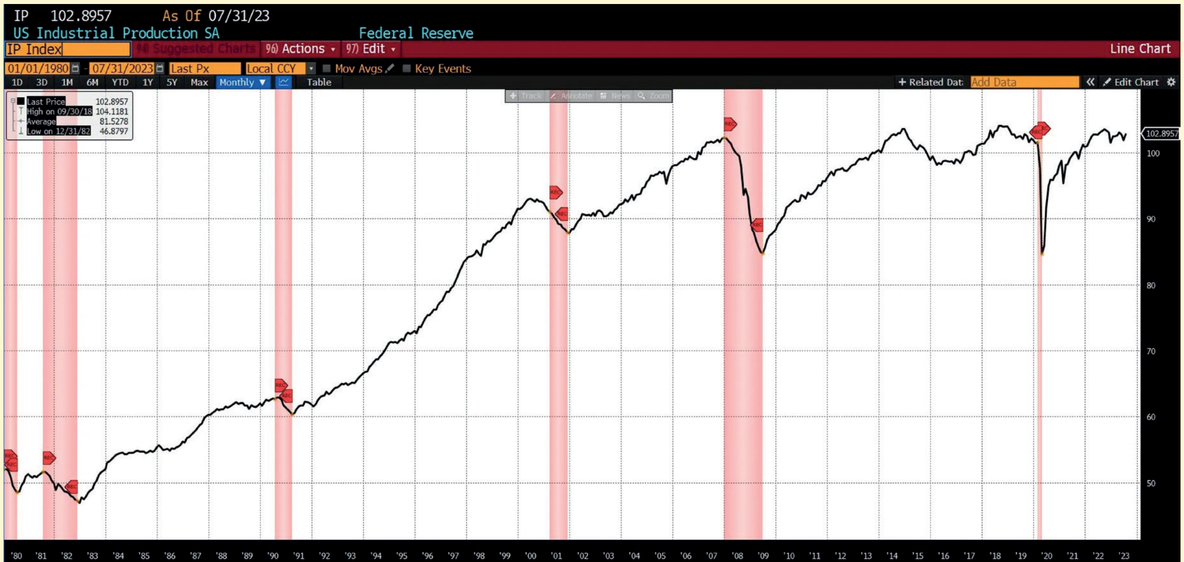

USYC1Y10 -119.443 -3.628 -119.443/-115.626
At 22:00 Op -117.345 Hi -117.345 Lo -121.966 Prev -115.815
USYC1Y10 Index
Line Chart
Last Price -143.833
High on 03/31/10 344.330
Average 136.841
Low on 06/30/23 -160.216
Low => High

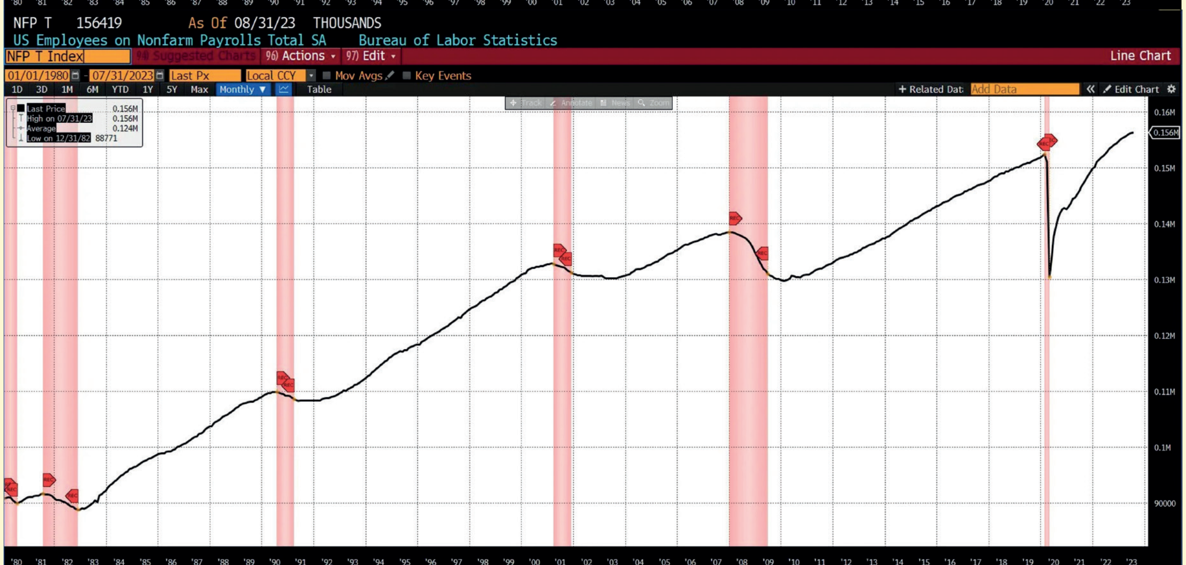

Debit Balances in Customers' Securities Margin Accounts
Debit Balances in Customers' Securities Margin Accounts

ROUGHLY COINCIDENT INDICATORS



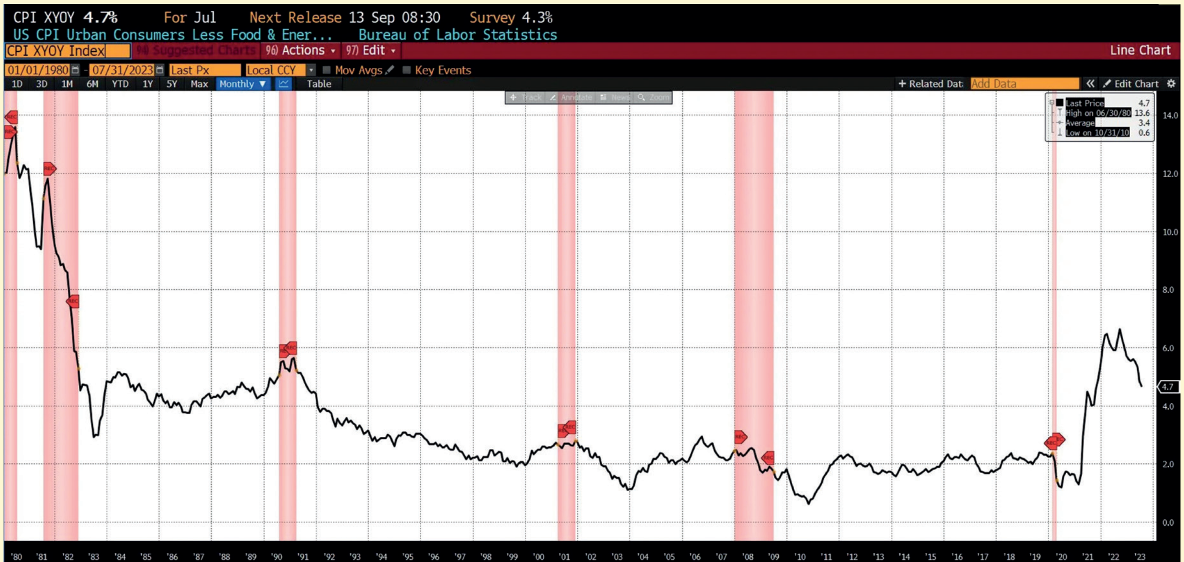


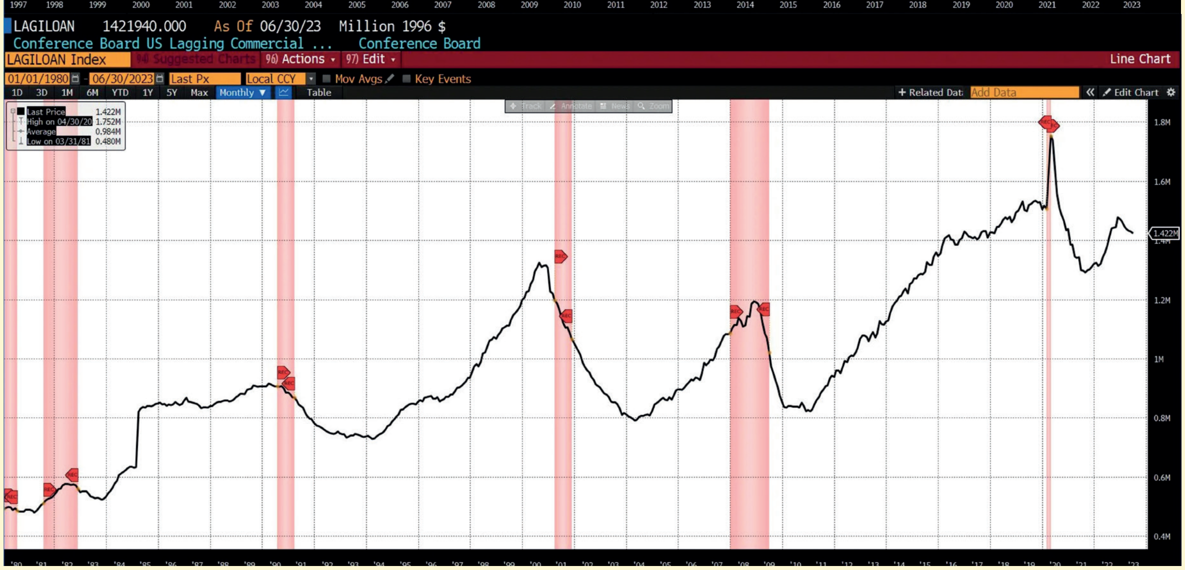

IP 102.8957 As Of 07/31/23
US Industrial Production SA Federal Reserve
IP Index
96) Actions
97) Edit
Line Chart
01/01/1980 - 07/31/2023 Last Px Local CCY Mov Avgs Key Events
1D 3D 1M 6M YTD 1Y 5Y Max Monthly Table
Related Dat Add Data Edit Chart
Last Price 102.8957
High on 09/30/18 104.1181
Average 81.5278
Low on 12/31/82 46.8797
'80 '81 '82 '83 '84 '85 '86 '87 '88 '89 '90 '91 '92 '93 '94 '95 '96 '97 '98 '99 '00 '01 '02 '03 '04 '05 '06 '07 '08 '09 '10 '11 '12 '13 '14 '15 '16 '17 '18 '19 '20 '21 '22 '23
100 90 80 70 60 50


NFP T 156419 As Of 08/31/23 THOUSANDS
US Employees on Nonfarm Payrolls Total SA Bureau of Labor Statistics
NFP T Index
96) Actions
97) Edit
Line Chart
01/01/1980 - 07/31/2023 Last Px Local CCY Mov Avgs Key Events
1D 3D 1M 6M YTD 1Y 5Y Max Monthly Table
Related Dat Add Data Edit Chart
Last Price 0.156M
High on 07/31/23 0.156M
Average 0.124M
Low on 12/31/82 88771
0.16M 0.15M 0.14M 0.13M 0.12M 0.11M 0.1M 90000
'80 '81 '82 '83 '84 '85 '86 '87 '88 '89 '90 '91 '92 '93 '94 '95 '96 '97 '98 '99 '00 '01 '02 '03 '04 '05 '06 '07 '08 '09 '10 '11 '12 '13 '14 '15 '16 '17 '18 '19 '20 '21 '22 '23

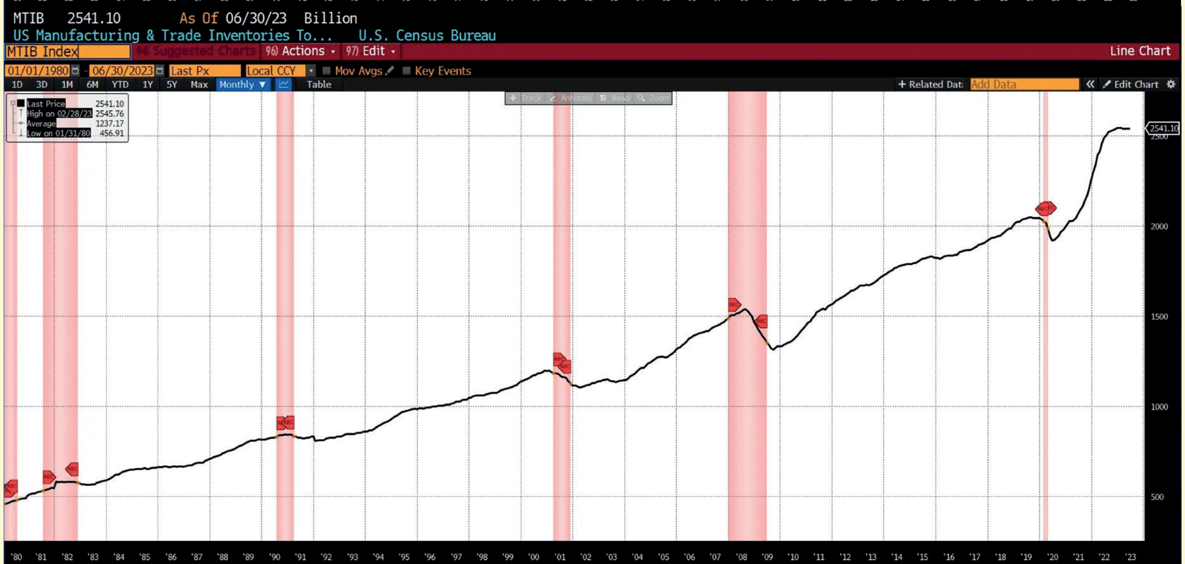

PRUSTOT 62.8% For Aug Next Release 06 Oct 08:30 Survey --
US Labor Force Participation Rate SA Bureau of Labor Statistics
PRUSTOT Index
96) Actions
97) Edit
Line Chart
01/01/1980 - 07/31/2023 Last Px Local CCY Mov Avgs Key Events
1D 3D 1M 6M YTD 1Y 5Y Max Monthly Table
Related Dat Add Data Edit Chart
Last Price 62.6
High on 01/31/00 67.3
Average 65.0
Low on 04/30/20 60.1
67.0 66.0 65.0 64.0 63.0 62.0 61.0 60.0
'80 '81 '82 '83 '84 '85 '86 '87 '88 '89 '90 '91 '92 '93 '94 '95 '96 '97 '98 '99 '00 '01 '02 '03 '04 '05 '06 '07 '08 '09 '10 '11 '12 '13 '14 '15 '16 '17 '18 '19 '20 '21 '22 '23

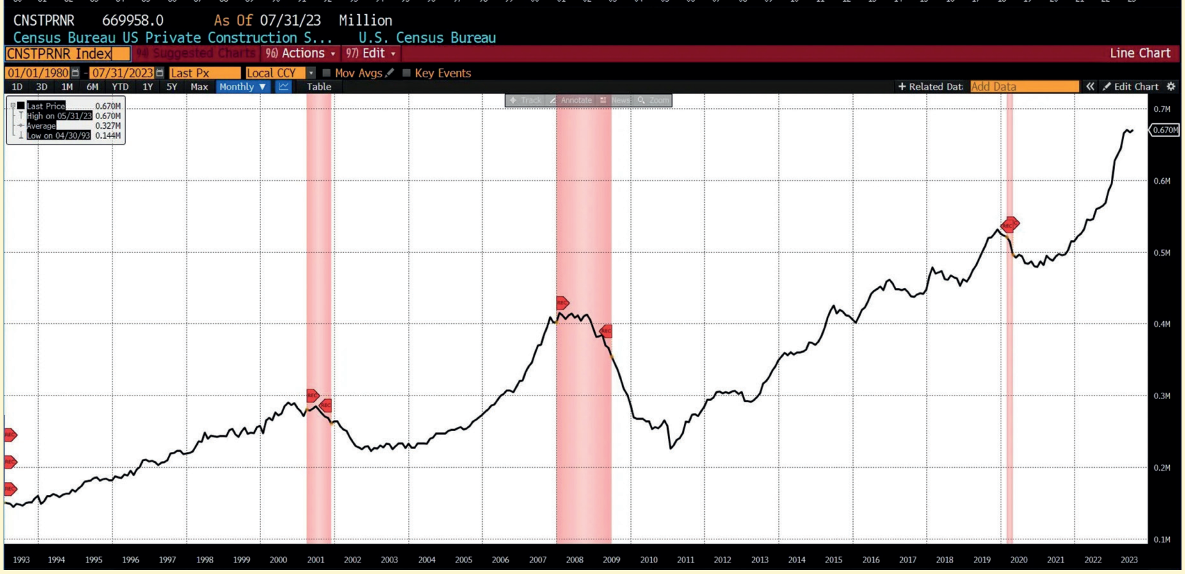
LAGGING INDICATORS






LAGIAVGU 20.600 As Of 07/31/23 Weeks
Conference Board US Lagging Avg Duratio... Conference Board
LAGIAVGU Index
Line Chart
Last Price 20.600
High on 07/31/11 40.700
Average 20.011
Low on 04/30/20 7.100


MTIB 2541.10 As Of 06/30/23 Billion
US Manufacturing & Trade Inventories To... U.S. Census Bureau
MTIB Index
Line Chart
Last Price 2541.10
High on 02/28/23 2545.76
Average 1237.17
Low on 01/31/80 456.91


CNSTPRNR 669958.0 As Of 07/31/23 Million
Census Bureau US Private Construction S... U.S. Census Bureau
CNSTPRNR Index
Line Chart
Last Price 0.670M
High on 05/31/23 0.670M
Average 0.327M
Low on 04/30/93 0.144M

CAPITAL MARKET PERFORMANCE

SPR		S&P 1500 Composite Index	-1.34%	+3.37%	+10.52%	11.0405	10.5865	12.5168
SPXT	d	S&P 500 Total Return	-.88%	+4.06%	+13.01%	10.9287	11.0805	12.7986
SPX	d	S&P 500 INDEX	-1.07%	+3.66%	+11.11%	10.9081	11.0633	12.7832
MID	d	S&P 400 MIDCAP INDEX	-3.82%	+.77%	+5.00%	12.6949	6.7170	10.0592
RTY	d	RUSSELL 2000 INDEX	-4.71%	-1.33%	+.48%	8.2013	3.1429	7.9328
SXXP	d	STXE 600 (EUR) Pr	-1.08%	-1.53%	+9.56%	11.3692	7.4219	8.0125
TLT US	d	ISHARES 20+ YEAR	-2.77%	-7.89%	-13.01%	-14.9762	-2.7802	1.4786
QLTA US	d	ISHARES AAA - A	-1.16%	-2.00%	-3.12%	-5.1423	.6928	2.0649
CRY	d	TR/CC CRB ER Index	+1.63%	+8.18%	+1.96%	23.8541	8.4470	-.3223
XAU		Gold Spot $/Oz	+.02%	-2.03%	+12.71%			
XAG		Silver Spot $/Oz	+1.37%	-4.72%	+24.59%			
ILM3NAVG		Bankrate 30Y Mortgage Rates Na	+1.75%	+6.94%	+24.18%			
ILM1NAVG		Bankrate 15Y Mortgage Rates Na	+2.71%	+6.41%	+27.77%			
MB301ARM		5 Year ARM	+2.43%	+17.44%	+31.60%			
ILA3NAVG		Bankrate 30Y Fixe Mtg Refis Na	+.68%	+.27%	+42.44%			

(All charts and data sourced via Bloomberg Finance, LP)

The Fed Hits 3,000 Percent Inflation

THOMAS L. HOGAN

Senior Research Faculty

The US economy was pushed to extremes during the pandemic recession and subsequent recovery. The unemployment rate peaked at 14.7 percent, the highest in the post-World War II period. Inflation reached its highest rate in 40 years, prompting the Fed to raise short-term interest rates to their highest levels since 2007.

As of June, the economy hit another dubious milestone: Inflation has now reached 3,000 percent under the Federal Reserve.

Inflation under the Fed

The Federal Reserve Act was passed by Congress in December of 1913, and the regional Federal Reserve banks opened for business in November of 1914. Comparing the price level at the end of 1914 to the level today tells us how much total price inflation the US economy has experienced under the Fed.

The consumer price index (CPI) is the most widely used and longest-running measure of the US price level, but there are disagreements about the accuracy of historical CPI. MeasuringWorth aggregates macroeconomic data such as interest rates, economic production, and the price-level from the most reliable historical sources.

Historical CPI data from MeasuringWorth show that the US price level rose by 2,920.2 percent from 1914 through 2022.

While the MeasuringWorth dataset provides only annual data, we can add monthly data for the current year from the official CPI data from the Bureau of Labor Statistics (BLS). According to BLS data, the CPI rose by 2.74 percent (not seasonally adjusted) in the first half of 2023.

That brings total inflation under the Fed to 3,000.2 percent.

Compared to what?

US inflation was not always as persistently high as it has been under the Fed. Before the Fed, the purchasing power of the dollar was determined by supply of and demand for gold. Consequently, the purchasing power of the dollar was relatively stable.

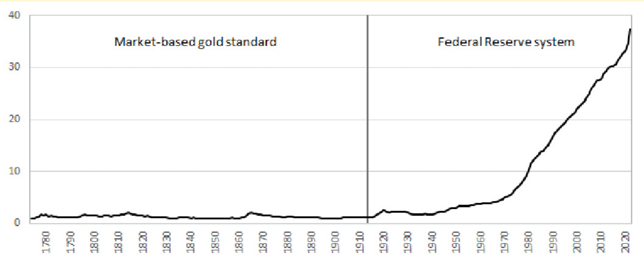


Figure 1. Index of the US price level, 1774-2022

Figure 1 shows the US price level back to 1774. After a brief turmoil during the American Revolutionary War, the price level was about the same in 1784 as it was in 1914.

That's approximately zero percent inflation over 130 years compared to 3,000 percent inflation in less than 110 years under the Fed.

Official statistics

The MeasuringWorth dataset combines data from the best historical research to correct for shortcomings in the official economic data.

One key difference from the BLS CPI is that, for the early years of the Fed, MeasuringWorth uses a study by Paul Douglas, which fills in a few months of data missing from the BLS and "computes the US index as a population-weighted average of the city indexes, whereas BLS uses an unweighted average."

How different are the MeasuringWorth data from the official BLS statistics? Using the official CPI data, inflation under the Fed has been *only* 2,952 percent since 1914. But don't worry: we'll hit 3,000 percent on the official measure soon enough.

– August 3, 2023

The Rise of BRICS-11

PETER C. EARLE
Research Faculty

The 15th BRICS Summit ended on August 24th, as expected, with new member states. The core members (Brazil, Russia, India, China, and South Africa) were joined by Saudi Arabia, United Arab Emirates, Iran, Egypt, Ethiopia, and Argentina. While there are many commonalities among the now 11-member BRICS bloc, two general observations can be made. First, that the economic center of gravity of the expanded group will be commodities: world energy markets, primarily. And, that the political backbone of BRICS is now primarily authoritarian.

Freedom House scores only three of the eleven (Argentina, Brazil, and South Africa) as "free" in its Global Freedom Score Index. The Heritage Foundation's 2023 Index of Economic Freedom rankings are more damnatory, with ten of the eleven countries ranked as "mostly unfree" or "repressive." United Arab Emirates is the sole exception, landing in the "mostly free" category at #24 in the world. (Bracketing it at #23 is Chile, and at #25, you guessed it: the United States of America.)

Some of the preexisting links between new and original BRICS members are obvious. Iran has developed close relationships with both China and Russia over the past decade or so. Ethiopia, despite a ruinous civil war, has increasingly been viewed as a nation of potentially strategic importance for several years. (Food aid to the nation was cut off several months ago following accusations that it was finding its way to military units as opposed to civilians.)

The official consecration of BRICS-11 will take place on 1 January 2024. Certain nations will likely capitalize on inter-bloc synergies and work together immediately, though it would be naive not to take note of some of the potential fault lines in the order. Saudi Arabia and Iran have been bitter rivals for decades, although in March of 2023 China brokered a peace deal between them. Similarly, Egypt and Ethiopia's tussling over access to the Nile River has put them at odds, but may be resolved by the end of 2023. (Egypt also, as a brand new member of BRICS, recently found itself on the receiving end (although distantly) of original BRICS member Russia's military activity on the Danube River.) And China's Xi and India's Modi agreed at the end of the summit to seek the expeditious resolution of border disputes which have intermittently resulted in combat since the Sino-Indian War in 1962.

The combined global GDP of the original five BRICS members accounted for approximately 42 percent of global GDP. With the new members, that number will rise to roughly 50 percent. (The G-7 nations, meanwhile, represent somewhere between 27 and 31 percent of global GDP.) But that statistic, like most economic statistics, is grossly misrepresentative without context. Argentina is currently in a hyperinflationary spiral, Ethiopia's debt is in desperate need of restructuring, the ruble is withering away to levels not seen since the initial invasion of Ukraine, and China's real estate sector is in freefall with several major firms facing Lehman-like collapses. Economic instability currently vexes about half of the BRICS-11 members, and for many has been more or less their default condition for decades. The explicit BRICS goals, which include expanding the reach of the New Development Bank (NDB), closer trade cooperation, and a dollar-alternative currency are undoubtedly viewed as a means to alleviate the perennial woes of economic mismanagement. And, of course, to slip Western spheres of influence.

About dedollarization, the most anticipated aspect of this year's summit, there were only conflicting messages and ultimately a deferment. Several days before the meeting began, announcements claimed that the NDB would make loans denominated in South African Rand and the Brazilian Real. Brazil's Lula de Silva's opening comments, in fact, included the staunch rhetorical "Who decided the dollar would be the [world's] currency?" Yet at the end of the summit South African Minister of Finance Enoch Godongwana commented that "[n]o one … tabled the issue of a BRICS currency, not even in informal meetings." He then added: "Setting up a common currency presupposes setting up a central bank, and that presupposes losing independence on monetary policy, and I don't think any country is ready for that." As commented previously, creating an accord of nations

> from different continents and cultures, with different histories and remarkably diverse resource endowments will be a heavy lift, organizationally speaking. Smaller members are likely to find their interests marginalized, with the resulting dynamic closer to what's seen in the United Nations than, say, OPEC. And few of the proposed members have confidence-inspiring track records where property rights are concerned.

Departing BRICS-11 finance ministers were tasked with reconvening at the 16th BRICS Summit in 2024, having by that time explored "issues of local currencies, payment instruments, and platforms." To some onlookers (and indeed, some participants) it was an undoubtedly anticlimactic end. Yet it clearly reflects both tensions arising of different levels of dollar dependence and the realization of the difficulty underscoring extricating the dollar from its global economic moorings. King Dollar is far from invulnerable, but the height of his throne is ritually underestimated.

– August 28, 2023

Only a Retail Gold Standard Could Dethrone the Dollar

ROBERT E. WRIGHT (Senior Research Faculty)

BYRON B. CARSON, III (Contributor)

The BRICS bloc is remaining coy about whether a global currency will be on the agenda of its 15th summit, which is set to take place August 22 to 24 in South Africa. Experts from Joseph W. Sullivan to Jim O'Neill to the Council on Foreign Relations warn that a BRICS currency would threaten American economic hegemony. Precedent suggests, however, that dethroning the US dollar with anything short of a full retail gold standard will be difficult.

As students of monetary history, we know that only one of the three major alternatives available to the BRICs bloc would likely last long enough to dent the dollar. That alternative, the retail gold standard, predates the fiat dollar by centuries, if not millennia.

If the BRICS bloc forms a supranational fiat currency like the euro, where demand today is generated by the expected demand for the currency tomorrow, it will surely soon be torn asunder, just as the euro almost was. Unlike the United States, BRICS countries are not a de facto common currency area. They are widely dispersed geographically and share no common fiscal apparatus. Their economies are very different and do not sync cyclically. So, BRICS countries may want to maintain monetary policy discretion, or in other words the ability to raise interest rates to cool inflation or lower them to stimulate growth.

But a supranational fiat currency could survive only if all BRICS national currencies are eliminated, lest one or more members become seigniorage-hungry "money pumps," as Rhode Island was in America's colonial period. That tiny colony caused a hyperinflation in New England but thankfully US policymakers learned from the experience and constitutionally banned states from issuing fiat money. That helps keep the US common currency area alive, as does the fact that America's fiscal and financial systems are unified, a big advantage in terms of macroeconomic stabilization that the BRICS currency, like the euro, would not enjoy.

To prevent interest rates from integrating and converging, as they do in countries that share a currency and allow the free flow of capital internationally, the BRICS countries could impose draconian capital controls. Such controls are costly to monitor, however, and defeat one of the main purposes of forming a common currency in the first place.

The question of control also looms large. Without strong institutional controls or a shared system of taxation, a sudden, massive depreciation of the new currency is possible if one or more of the larger BRICS partners decide to exit by issuing their own money again, perhaps to regain control of domestic interest rates.

Cognizant of those difficulties, the BRICS bloc might instead try to create a gold-exchange system like the free world did at Bretton Woods in 1944. In such a system, each nation would continue to issue its own currency and enjoy some domestic monetary policy discretion. But by pledging to redeem their fiat monies at their central banks for gold at a known, fixed rate, they constrain themselves from becoming a money pump. They must impose capital controls, though, lest they lose all their gold reserves if their interest rates fall too far below those of other countries in the system. Or, their monetary authorities must periodically devalue the domestic currency, which can get politically ugly. Sometimes, a dominant country must revalue its currency to keep the system in balance, but often it proves reluctant to do so for fear of hurting its export sector.

Moreover, countries can stop gold redemptions and leave the system whenever it is in their perceived best interest to do so, like when the United States left the Bretton Woods system in the early 1970s, less than 30 years after its formation. Another fixed exchange rate regime initiated in 1979, the European Monetary System, fell apart even more quickly, in 1992. The crisis made a billionaire out of George Soros but disrupted several major European economies.

Some say that fiat common currency areas like the euro and gold-exchange systems can work long term if only the details can be gotten right. Maybe, but many say the same thing about communism. We believe that only a retail gold standard could topple the dollar in the short term and survive indefinitely. In that system, which the United States and many other nations relied upon until the Great War (1914-1918), anyone can exchange central bank notes or commercial bank notes or deposits for gold on demand at a fixed, known rate in terms of the local unit of account (yuan, rand, reals, etc.). That fixes exchange rates between countries while the free international flow of gold and other capital ensures domestic price stability. The main cost, the loss of domestic monetary discretion, is really a benefit because it means that markets, not politicians, determine domestic interest rates.

The fiat dollar in place since 1973 achieved global dominance because it only had to compete against the fiat currencies of countries like Switzerland with better institutions but much smaller economies, or with the currency of a supersized economy with weaker institutions, the euro. If a large subset of countries, like the BRICS, adopted the retail gold standard, the United States and the European Union would have to join, or watch demand for their fiat currencies decline.

In short, America has little to fear from a BRICS common currency or even a gold exchange system. If the BRICS implements a retail gold standard, though, it will likely be forced to give up the fiat dollar for bricks, goldbricks that is.

The authors of this piece recently published
Explaining Money & Banking (Business Expert Press, 2023).

– August 12, 2023

AngerSong

JAMES R. HARRIGAN

Senior Editor

Oliver Anthony is the dog that caught the car. He has scored 31 million YouTube views (to date) on the first song he recorded with a professional microphone. In 13 days. God knows how many more streams he's had on Apple Music, Spotify, and all the other streaming services carrying "Rich Men North of Richmond." And God knows how many more he will have by the time this chapter in his life is said and done.

He is the first artist ever to make his debut on the Billboard Hot 100 at number one. That's right. His first song to be recorded with something other than a cell phone microphone is the number-one song in the United States.

And with all that unanticipated success, Anthony has yet to decide what to do. He has, it seems, decided what not to do, turning down some $8 million to continue living in his $750 camper.

But I'm not here to talk about Oliver Anthony. He's more than capable of doing that himself if he wants. I'm here to talk about the 31 million, and a good number of other people besides.

Anthony has clearly caught some kind of lightning in some kind of bottle. And just about everybody is angry, either with him or about him. That millions more people find and listen to the song every day is clear evidence that it resonates with them, and the song is pure anger.

He sings:

> It's a damn shame what the world's gotten to / For people like me and people like you / Wish I could just wake up and it not be true / But it is, oh, it is.

And we can argue about where the shame is. We can point out that people live a long time compared to their forebears, that they eat better and have more comforts than at any time in human history, that literacy rates are high, that children are not forced to work long hours in mines, factories, or on farms, that our houses are bigger, our cars are safer, our food is cheaper. We can point all of that out, but the simple fact of the matter is a sizable minority of our population isn't taking part in the spoils of modern life, and an even bigger subset, perhaps even a majority, are convinced they aren't either.

And they're getting angrier.

So when Oliver Anthony confirms one group's experiences, and the other group's biases, they all listen. With a vengeance.

But here's where the story gets interesting, because Anthony doesn't go for the usual villains. He doesn't point his accusing finger at the one-percent or evil corporations, he goes right for that 68-or-so square miles of land sandwiched between Virginia and Maryland and the sort of people who inevitably find their way there.

> These rich men north of Richmond / Lord knows they all just wanna have total control / Wanna know what you think, wanna know what you do / And they don't think you know, but I know that you do / 'Cause your dollar ain't shit and it's taxed to no end / 'Cause of rich men north of Richmond.

And when he went for the politicians, tribalism kicked in about as fast as the IV chord follows the I.

The left-leaning media (read: the media) pounced fast and hard.

New York's Intelligencer led with "Oliver Anthony and the Incoherence of Right-Wing Populism." *Variety* came up with "Oliver Anthony's 'Rich Men North of Richmond' Is an Instant Smash Among Conservatives, While Progressives Wonder if He's a 'Plant.'" Britain's *The Guardian*, still not understanding much about the former colonies, came up with "Rich Men North of Richmond punches down. No surprise the right wing loves it."

You would be forgiven for thinking this was some sort of new right-wing national anthem, given the breathless coverage.

But who wouldn't want you to think that? Oliver Anthony. He says he's been "middle of the road" most of his life, and he makes his political point of view pretty clear in another song, "Doggonit."

He sings:

> And Republicans and Democrats / Lord I swear they're all just full of crap / I ain't never seen a good city-slickin' bureaucrat

And that's the real appeal, and the danger moving forward. If the rich men north of Richmond don't find some way to rise above their self-serving antics, we can expect this anger to grow, and nothing good will come of it.

– August 22, 2023

Should We Abolish Zoning?

JASON SORENS

Senior Research Faculty

Most of America's land area is zoned, a government regulation that tells landowners what they're allowed to build in different places, and how much of it they can build. Some experts are now recommending getting rid of zoning entirely.

Are they right? I consider the proposal in a new paper. The case for abolishing zoning ends up a lot stronger than I expected.

Bernard Siegan's out-of-print study of Houston, the largest city without zoning, just came out in a new edition. The author of the afterword to this new edition, UCLA PhD student and urban planner Nolan Gray, has come out with his own book, *Arbitrary Lines: How Zoning Broke the American City and How to Fix It*. Together, they say the example of Houston proves our cities would be better off without zoning. Why?

Let's start with the litany of problems scholars have found with excessive zoning in the U.S. today. Stricter zoning has been linked to housing undersupply, housing unaffordability, homelessness, out-migration, slower economic growth, lower overall social welfare, socioeconomic segregation, racial segregation, higher property taxes, air and groundwater pollution, longer commute times, lower marriage and fertility rates, and bigger rich-poor test score gaps. With all these costs, reforming zoning looks urgent.

But why abolish it altogether? Don't we need zoning to prevent people from opening factories or sexually oriented businesses in residential neighborhoods?

Not at all, says Gray. First, market forces encourage industrial facilities to locate near transportation nodes, like ports and railroads. So these uses will cluster away from most people's homes, and that is just what we usually saw before zoning. Wanting to be a good neighbor also causes people to try to make their property uses and appearance amenable to their neighbors. To deal with the occasional exception, we could use private covenants, which restrict land use voluntarily and run with the land when it is sold or leased. If that's not enough, there's the common law of nuisance. If you cause air, water, light, or noise pollution that hurts your neighbors, they can sue you, which is a good deterrent to doing it in the first place.

Finally, if market forces, neighborliness, covenants, and nuisance law don't do the trick, local governments can pass ordinances limiting how closely certain uses can be located to other uses. You don't need to draw "arbitrary lines" around zoning districts and come up with lists of what's allowed in each district, says Gray. Just buffer incompatible uses!

That is what Houston has done, and it has allowed Houston to remain affordable while attracting thousands of new workers every year (Figure 1).

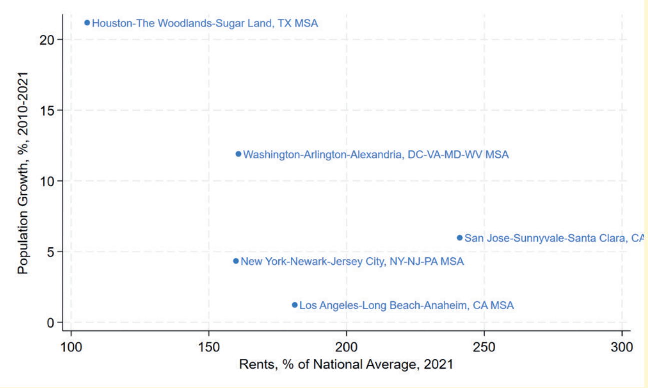


Figure 1. Rents and Population Growth in Selected Metropolitan Statistical Areas

Now, Houston is not a free-for-all. It requires a minimum number of parking spaces for different uses, which encourages sprawl. Its complex development code limits how many homes you may build on an acre. But it has no zoning, and its density restrictions are less severe than in almost any other large city.

Could the Houston model work everywhere else? Maybe. Central planning of land use is unthinkably complex. Siegan: "Questions of compatibility, economic feasibility, property values, existing uses, adjoining and nearby uses, traffic, topography, utilities, schools, future growth, conservation, and environment have to be considered for countless locations, covering hundreds of square miles." Zoning boundaries and regulations are based on little more than "guesswork."

The only problem is that zoning's popular. Many people consider zoning part of the "property right" they bought in their home. They really should set up covenants if they want that security, but the fact that zoning has been around so long has discouraged people from doing this.

Instead of abolishing zoning, we can promote private alternatives. Exempt private communities from zoning if they meet certain conditions. Let neighborhoods remove restrictions on their own. Require governments to compensate landowners if they add restrictions that reduce the value of a property. (For more details, see the paper.)

The surprisingly strong argument for abolishing zoning is the rare case of successfully moving the "Overton window." It should make all of us more sympathetic to fundamental reforms.

– August 25, 2023

Inflation is Back on Target

WILLIAM J. LUTHER

Director, Sound Money Project

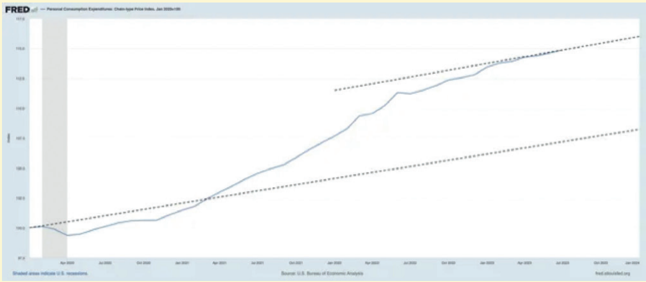
After more than two years of high inflation, the Federal Reserve finally has inflation back on target. The Personal Consumption Expenditures Price Index (PCEPI) has grown at a continuously compounding annual rate of 2.1 percent over the last three months, new data from the Bureau of Economic Analysis shows. Bond markets are pricing in roughly 2 percent PCEPI inflation per year over the next five years.

Some—including some Fed officials—are reluctant to accept the good news. And their reluctance is understandable. Annual inflation rates remain high. The PCEPI grew 3.2 percent over the last year. Core PCEPI, which excludes volatile food and energy prices, grew 4.2 percent. However, these high rates largely reflect price increases that occurred months ago. Those distant price increases should not be used to justify further rate hikes today.

An analogy serves to illustrate. Suppose you decelerate from 45 MPH to 20 MPH while approaching a school zone in your car. When you reach the school zone, you look down at your odometer and see that you are going 20 MPH. At that point, you do not stomp on the brake just because you have averaged 35 MPH over the last quarter mile. Of course your average over the last quarter mile is greater than your 20 MPH target: you were decelerating to hit that target. What matters now is not how fast you *were* going, but how fast you *are* going.

Likewise, the Fed is aiming for 2 percent inflation. Now, inflation is back around 2 percent. The Fed should not raise rates further just because inflation was higher months ago. What matters now is not how fast prices were rising, but how fast they are rising now.

Of course, the price level remains much higher than it would have been had the Fed hit its 2-percent target over the course of the pandemic. If inflation had averaged 2 percent, they would be 7.7 percentage points lower today. But that, too, is not a good reason for raising rates further.



Source: St. Louis Fed

In general, the Fed should set expectations and then deliver on those expectations. The first-best policy is clear: when a change in nominal spending pushes the price level above (below) the projected path, the Fed should promptly tighten (loosen) policy to bring those prices back in line with expectations. The Fed has not done this. But it does not follow that the Fed should do this now. Since the Fed did not act promptly, the first-best option is off the table. We can only hope for a second-best policy. We must seriously consider what the Fed should do when it hasn't done what it should have done.

Given that the Fed has made it clear—since at least December 2021—that it would gradually bring the rate of inflation back down to 2 percent but permit the price level to remain elevated, it would be a mistake to change course now and try to bring prices back down to where they would have been had it never erred in the first place.

People have adjusted their expectations. As shown below, the TIPS spread—adjusted for the difference between PCEPI inflation and Consumer Price Index Inflation—suggests market participants are pricing in 2.0 percent inflation over the five-year horizon and 2.1 percent inflation over the ten-year horizon.

Source: St. Louis Fed

More importantly, people have renegotiated their wages and purchase orders with those new expectations in mind. To course correct at this late stage would amount to a very painful contraction.

We've already borne the costs of an unexpected inflation. There's no good reason to tack on additional costs from an unexpected deflation.

– August 31, 2023

Against a 3 Percent Inflation Target

ALEXANDER WILLIAM SALTER

Director, Sound Money Project

The aimless drift of economic policy continues, as otherwise sensible economists push for the Federal Reserve to raise its inflation target to 3 percent. This will supposedly provide all the benefits of the Fed's current 2 percent target without incurring the costs (reduced growth, higher unemployment) of driving inflation down further. Even apart from the naive Keynesianism implied in this view, there are still several problems, any one of which sinks the argument for a higher target.

There are welfare costs to higher inflation. When the dollar depreciates faster, people try to reduce their cash holdings. But economizing on liquidity is itself costly. As Milton Friedman argued, it results in fewer transactions and, correspondingly, fewer gains from trade. The cost incurred by each of us is very small. Multiply it by 330 million, however, and it doesn't look so trivial.

The second cost, related to the first, stems from the redistributive nature of the policy change. Think about the millions of people with long-term debt contracts, such as banks and mortgage-holders. Raising the inflation target redistributes wealth from creditors to debtors. The longer the duration of the debt contract, the greater the transfer. By itself, a transfer of resources is neither a cost nor a benefit to society. The problem is all the resources people would use up to minimize the damage to their own net worths, as well as precautionary actions taken to avoid similar redistributions in the future. We already spend far too much time, money, and effort watching the Fed. Raising the inflation target would waste even more.

The third cost is significantly larger than the first two. Many tax rates are not indexed to inflation. Capital gains taxes, for example, are denominated in nominal dollars. Higher inflation means higher asset values, which will push owners of capital into higher tax brackets. Even if real asset values are decreasing, owners of capital will have to pay greater taxes on nominal price increases. This creates strong disincentives to invest, and hence create additional wealth. Furthermore, since it means Uncle Sam's share of the economic pie will increase in real (inflation-adjusted) terms, more wealth will be allocated to fundamentally unproductive uses. This is a needless drag on growth.

But the largest cost to a 3 percent inflation target is diminished Fed credibility. The central bank would essentially admit to markets that it is unwilling to do the hard work to return inflation to its previously adopted target. That would tarnish the Fed's reputation. If the central bank can't be trusted to hit a 2 percent target, why is a 3 percent target any more believable? After the next crisis—and given how bad the Fed is at its job, there will certainly be one—will the Fed acquiesce to a 3.5 percent or 4 percent target? What about the crisis after that? There's no end to this ratchet. The Fed's hard-won reputation as a guarantor of nominal stability would be lost, perhaps forever.

There is no good reason to accept a higher inflation target. All the arguments for it rely on dark-age macroeconomics, which should have stayed buried with the stagflation of the 1970's. If the Fed can really make such an elementary error and get away with it, a major prudential reason for keeping it around would no longer hold. A Fed that willingly accedes to the dollar-depreciation racket is too dangerous to keep around.

– September 1, 2023

US Credit Rating Downgraded, Again

PETER C. EARLE

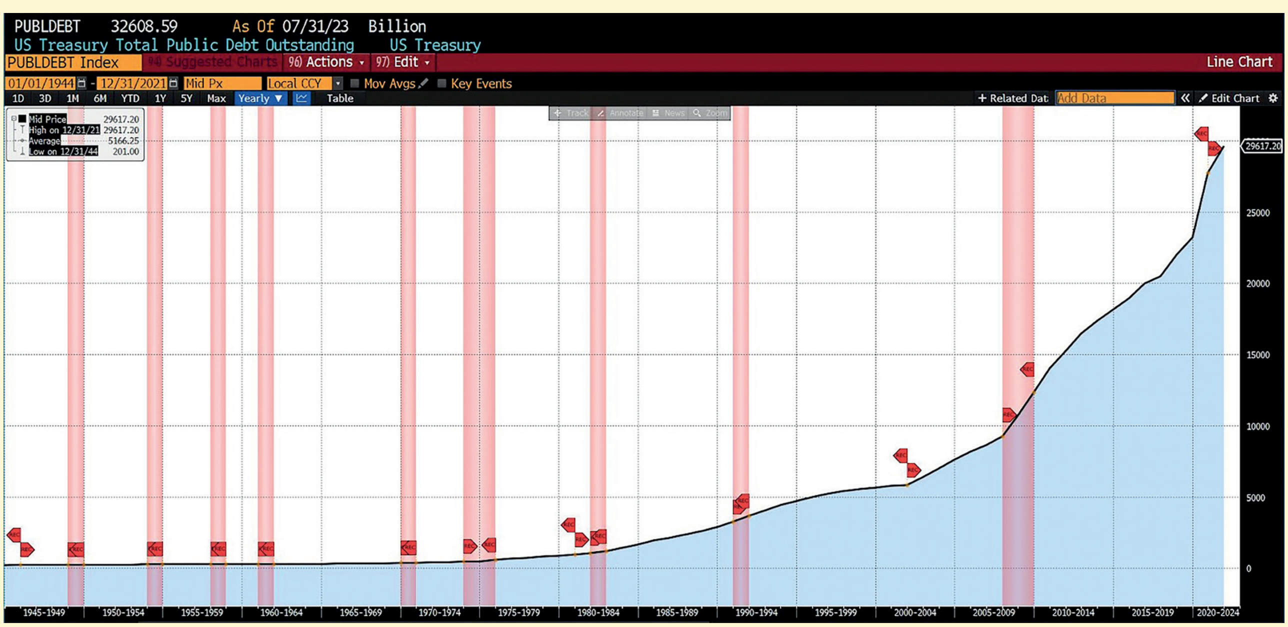
Research Faculty

US Treasury debt, the global benchmark for nominally “risk-free” securities, was downgraded for the second time in history late Tuesday. Fitch Ratings lowered the credit grade of US government bonds from AAA to AA+, citing a rapidly worsening fiscal outlook and an increasing vulnerability to economic shocks.

On August 5, 2011, S&P Global also downgraded the US sovereign debt rating from AAA to AA+. The downgrades indicate that doubt is growing regarding the US government’s capability to meet its financial obligations.

While the United States has been getting deeper in debt each year, the outlook for the nation’s fiscal health has been progressively deteriorating along a broader front. In particular, Fitch Ratings cited “repeated debt-limit political standoffs and last-minute resolutions [which] have eroded confidence in fiscal management,” referring to the increasing frequency of brinkmanship in budget and debt ceiling negotiations over the past decade or two. Further, the agency stated that “the [US] government lacks a medium-term fiscal framework, unlike most [or its] peers, and has a complex budgeting process.” A broad array of new government spending programs have been undertaken and added to, year after year, with little to no progress in arresting fiscal profligacy.

US Treasury Public Debt Outstanding (WWII – present)



(Source: Bloomberg Finance, LP)

Fitch expects the government deficit to nearly double from 3.7 percent in 2022 to 6.3 percent in 2023. The US Federal deficit reached $1.39 trillion for the first nine months of the current fiscal year, 170%

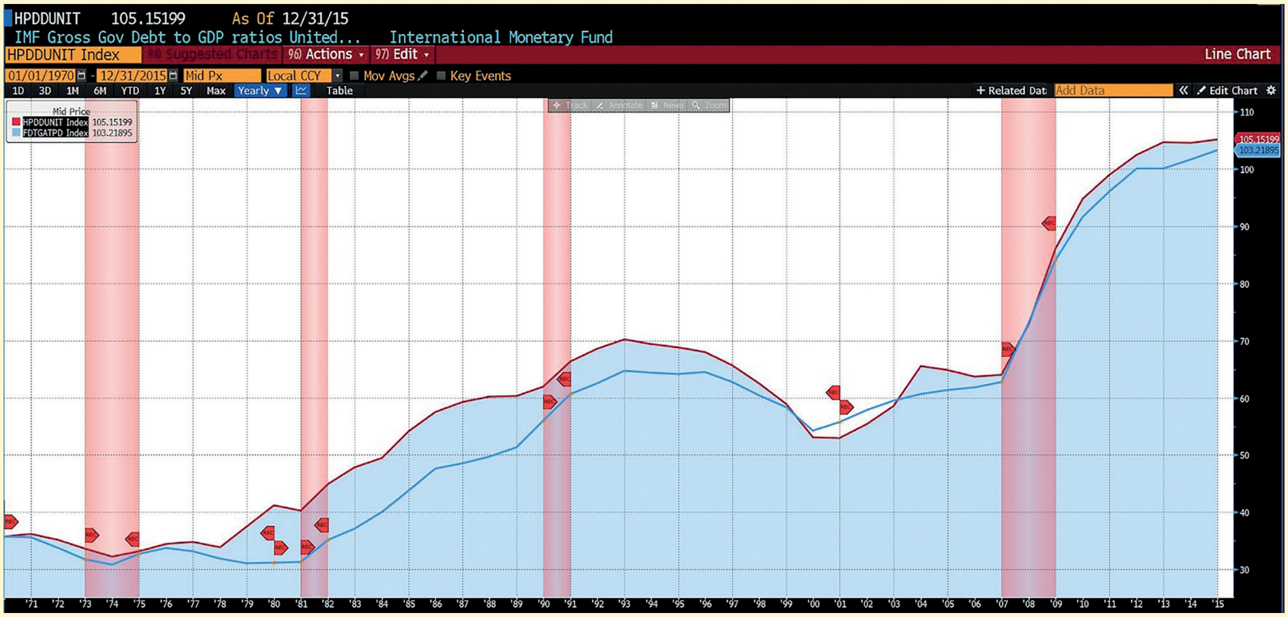
higher than this same point during the last fiscal year.

Additionally, the US Treasury boosted its borrowing projections for the current quarter from $733 billion to over $1 trillion. Despite that, US Treasury Secretary Janet Yellen responded shortly after the downgrade notice, calling the decision by Fitch "outdated."

Her characterization is categorically accurate: the median debt-to-GDP ratio of AAA rated sovereign debt issuers is currently 39.3 percent; for AA rated issuers, 44.7 percent. The current US debt-to-GDP ratio is 112.9 percent. Even before the COVID pandemic, in 2019 the ratio stood at 100.1 percent. The last time America's debt-to-GDP ratio was at the current AAA median level was between 1978 and 1979.

US debt-to-GDP ratio (1970 – present)

US Office of Management and Budget (blue), International Monetary Fund (red)



(Source: Bloomberg Finance, L P)

The initial reaction in US Treasury markets early Wednesday was a slight increase in yields for US government obligations with maturities of five years or longer. The US Dollar Index was essentially unchanged. Large financial asset managers will now face the dilemma of whether to move their US Treasury bond holdings into a category associated with marginally riskier securities, or to disregard the guidance of the rating agencies.

The reduction of the US credit rating is overdue in light of the long and enthusiastic abandonment of fiscal soundness in Washington DC, recently abetted by monetary policy authorities. A nation simultaneously so dependent upon outside financing while so eager to throw its weight around globally would be wise to, at the very least, keep its books somewhat orderly. US citizens would be well advised to consider both the recent bulking up of the Internal Revenue Service and rapid innovation of central bank digital currencies (CBDCs) in weighing the likelihood of sudden fiscal reform versus the exploration of new means of enhancing revenue.

– August 3, 2023

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