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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 9 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

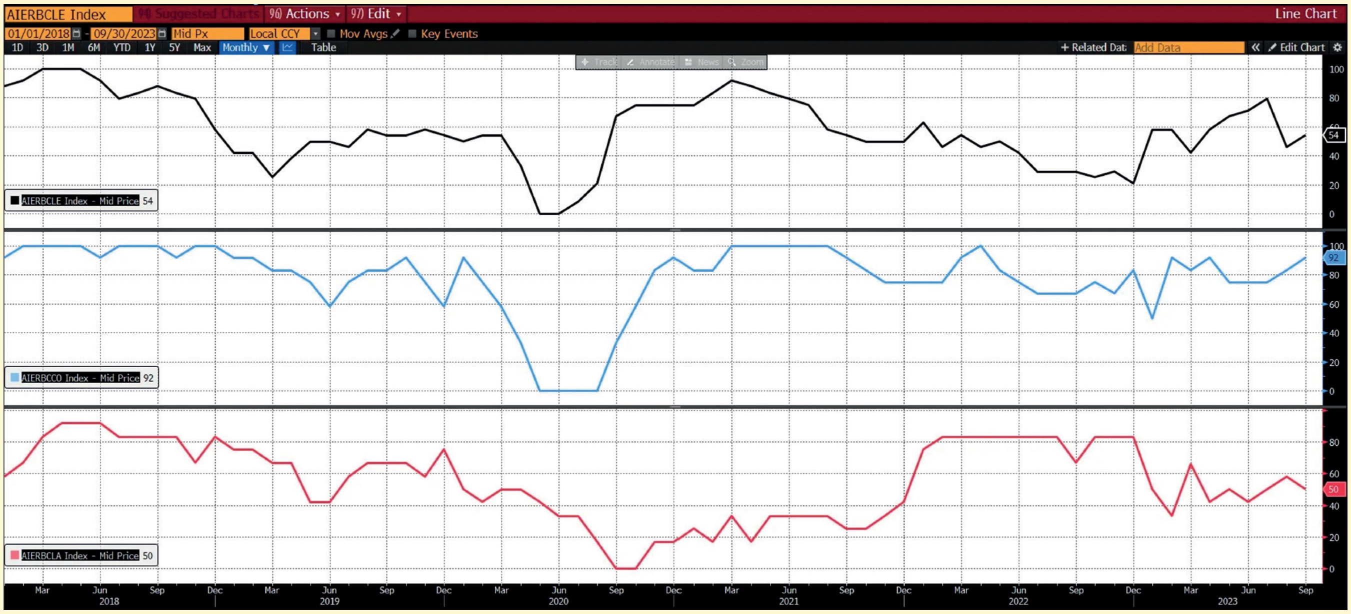
Contents

BUSINESS CONDITIONS MONTHLY

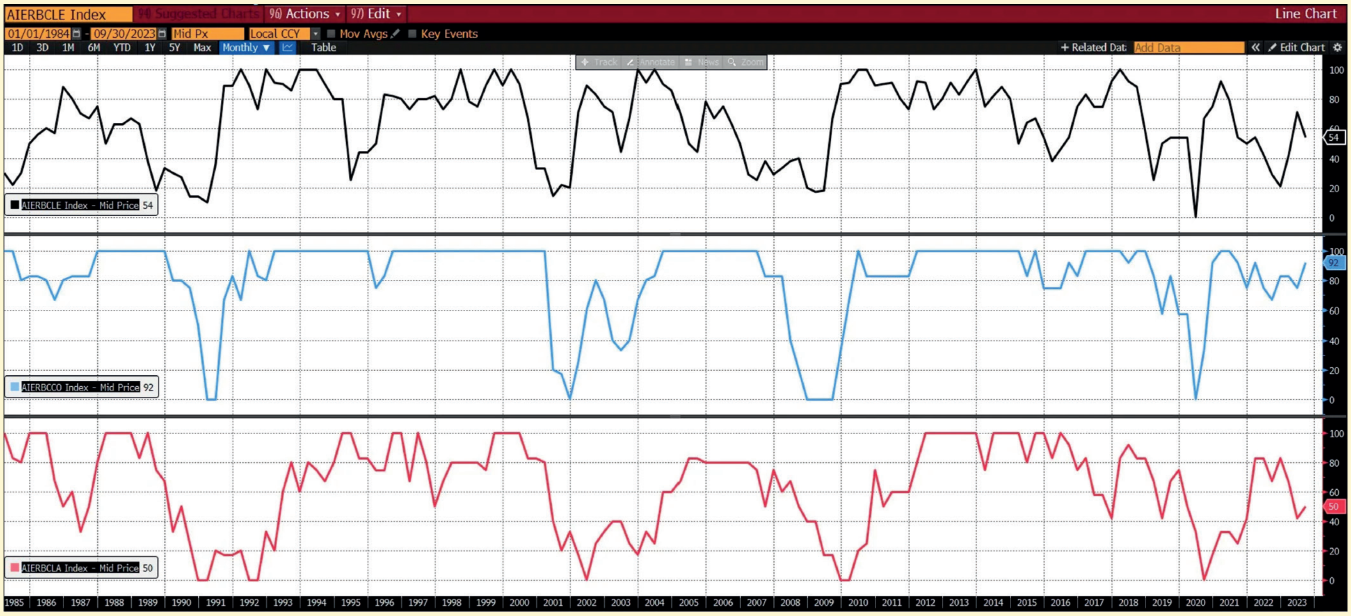
Peter C. Earle
RESEARCH FACULTY

In September 2023, AIER's Business Conditions Monthly indices continued on distinct trajectories. Our Leading Indicator rose from 46 to 54, remaining close to neutral, but with an expansion tilt. The Roughly Coincident Indicator continued its rise, reaching 92 after starting the year at 50. And our Lagging Indicator fell from a slightly expanding 58 in August to a neutral 50.

AIER Business Conditions Monthly (5 years)



AIER Business Conditions Monthly (1985 – present)



Leading Indicators (54)

Five of the twelve leading indicators declined, one was unchanged, and six rose. Among the decliners were the University of Michigan's Consumer Expectation Index (-8.0 percent), United States Heavy Truck Sales (-7.9 percent), the US Census Bureau's Inventory to Sales Ratio (-1.4 percent), FINRA's Debt Balances in Customers' Securities Margin Accounts (-1.2 percent), and the Conference Board US Leading Index of 500 Stock Prices (-1.1 percent). The Conference Board US Manufacturers' New Orders of Nondefense Capital Goods Excluding Aircraft was unchanged.

Rising were the 1-to-10 year US Treasury spread (30 percent), US New Privately Owned Housing Starts by Structure (5.8 percent), US Initial Jobless Claims (5 percent), Adjusted Retail and Food Service Sales (0.7 percent) US Average Weekly Hours All Employees, Manufacturing (0.25 percent), and the Conference Board US Leading Index of Manufacturer New Orders, Consumer Goods, and Materials (0.01 percent).

Roughly Coincident (92) and Lagging Indicators (50)

The Roughly Coincident Indicator rose to 92 in September from 83 in August, reclaiming a level it last reached in April of this year. After January 2023 (50), the indicator has been at a broadly expansive level of 75 and higher.

Five of its six constituents rose, with one unchanged. While the US Labor Force Participation Rate was unchanged, increases came in the Conference Board Coincident Manufacturing and Trade Sales (0.2 percent), US Employees on Nonfarm Payrolls (0.2 percent), Conference Board Coincident Personal Income Less Transfer Payments (0.2 percent), Conference Board Consumer Confidence Present Situation (0.3 percent), and and US Industrial Production (0.3 percent).

The six constituents of the Lagging Indicator were divided among three rising and three falling. The three decliners were the Conference Board US Lagging Average Duration of Unemployment (-5.4 percent), Core CPI year-over-year (-4.7 percent), and the Conference Board US Lagging Commercial and Industrial Loans (-0.4 percent). The Census Bureau US Private Construction Spending (Nonresidential) rose (0.3 percent), as did US Manufacturing and Trade Inventories (0.4 percent) and average 30-day yields (0.9 percent).

Discussion

The release of the first run of 3rd quarter GDP on October 26 provides a solid foundation for examining the current state of the US economy. The 4.9 percent annualized rate of expansion was the fastest in nearly two years, yet beneath the surface revealed an economy growing on the basis of disparate and unsustainable elements.

The three major contributors to the large 3rd quarter GDP print were consumption, private inventories, and government spending. Government spending contributed 0.8 percent to the 4.9 percent output, yet represents nonproductive redistribution generated by debt issuance, taxation, and/or monetary expansionism. Unsurprising in light of expanding US military aid commitments, 0.28 percent of the 0.8 percent of US government spending was national defense related.

The growth in private inventories, which added 1.3 percent of the 4.9 percent total, are likely to have been cautionary in nature. Two explanations have been suggested to account for the large accumulation of stocks in the third quarter. One is growing concern regarding the continuing consumption potential of American consumers. Businesses that rely on maintaining high service levels or fulfilling contractual obligations thus seeking to ensure that they can meet customer demands amid a continued slowdown. Additionally, the inventory build-up may be a substitute for declining capital spending plans, which have fallen to the lowest level since June 2020. A second explanation is that the success of the United Auto Workers strike against Ford, General Motors, and Stellantis has prompted companies with collective bargaining exposure to hedge against the possibility of disruption, whether from their own workforce or that of vertically/horizontally integrated firms. Keeping a larger than average number of intermediate or finished goods on hand safeguards against unexpected and possibly intransigent labor disputes.

Consumption accounted for 2.7 percent of the 4.9 percent 3rd quarter GDP number. For some months now, the deterioration of consumer activity has been anticipated, yet slower to materialize than expected. September represents the fourth straight month in which real spending has grown faster than real income. This suggests that a substantial amount of recent spending, which has been a major contributor to US output, has been funded mainly out of borrowing and savings. In terms of borrowing, the Federal Reserve's latest Senior Loan Officer Opinion Survey (SLOOS) indicates a continuing trend of tightening credit and higher credit standards. This comes atop declining demand for auto loans, consumer loans, and mortgage financing against a backdrop of rising interest rates. The prospects for ongoing borrowing are diminishing absent a reversal of the current monetary policy bias.

While wages and salaries rose by 0.4 percent in September 2023, disposable income fell for a third straight month, indicating that American consumers have been saving less to support future consumption. Personal spending growth is thus outstripping income gains. Also in September, the US saving rate fell to 3.4 percent, its lowest level since December 2022. These facts, on top of the resumption of student loan payments, stubborn inflation in certain goods and services, the ongoing contraction of credit, and higher interest rates, raise doubt as to the durability of robust spending.

Bolstering this interpretation, the University of Michigan's preliminary consumer sentiment readings for October suggested an abrupt reversal of personal financial assessments among survey participants. The Conference Board's consumer confidence index similarly declined from 104.3 in September to 102.6 in October. The slide in consumer confidence came on the basis of less optimistic views regarding current business conditions, a new post-pandemic low in job availability appraisals, and declining confidence regarding incomes over the next six months.

Recent employment data supports this conclusion. While September labor data was stronger than expected, October data showed job growth slowing by more than anticipated, with the U-3 unemployment rate rising to a nearly two year high of 3.9 percent. The increase from 3.8 to 3.9 percent derives from a decline in the labor force by 201,000 and a decline in the number of individuals employed by 348,000, and consequently a rise in the number of unemployed by 146,000 (versus 5,000 in the previous month).

Eight of the last nine monthly US Bureau of Labor Statistics reports in 2023 have been revised downwards in subsequent releases. The 150,000 nonfarm payroll number in October not only came in lower than the 180,000 expected, but 50 percent lower than the revised 297,000 jobs reported in the September release. The October nonfarm payroll number was the second lowest since June 2023 (105,000) going back to December 2020 (-115,000).

The composition of the October report was poor as well. Of the 150,000 jobs reported, slightly more than one third (51,000) were government jobs financed not out of productive commerce but fiscal redistribution. Of the other 99,000 jobs, some 89,000 were in education, social assistance, and health services: jobs with a high proximity to public expenditure. The remaining 10,000 came from financial services, information services, and transportation. Manufacturing saw a decline of 35,000 jobs.

The October employment report also revealed a record number of multiple jobholders in the US economy. A record 8.5 million individuals currently have two or more jobs, with just under 400,000 joining those ranks in the last month. (This is a somewhat obscure data series which AIER has been following since August 2022; please see "Making Sense of the Recession.") It is likely that the actual state of affairs with regard to multiple jobholders is vastly higher than even these numbers indicate, considering that many secondary or tertiary employment positions involve compensation outside of official payrolls.

Another statistic which has been reported previously is the increase in WARN Act (Worker Adjustment and Retraining Notification Act of 1988) filings. AIER first mentioned this in early May 2023 (see "The Path to Full Stagflation") as not only beginning a gradual ascent, but historically leading federal unemployment statistics. This seems to be the case.

The recent U-3 unemployment of 3.9 percent is close to triggering the so-called Sahm Rule. Named for former Federal Reserve economist Claudia Sahm, the rule stipulates that when the three-month average of the US unemployment rate rises by at least 0.50 percentage points above its lowest point from the previous 12 months, it indicates the start of an economic recession. With a low three-month moving average this year of approximately 3.4 percent, the October rate of 3.9 percent brings the increase to 0.43 percent. The rule has successfully identified all 11 US recessions since 1950, with a false positive rate of approximately 1 percent. A similar rule employs the U-1 unemployment rate (which focuses on individuals who have been unemployed for 15 weeks or more as a percentage of the total civilian labor force). Although the U-1 rate historically lags the U-3 rate, when it surpasses its 12 month low by greater than 0.2 percent it has identified recessions with a false positive rate of 0.6 percent, albeit with a five month delay. The current U-1 rate of 1.4 percent meets that criterion, 0.3 higher than the average rate of 1.1 percent in February, March, and April 2023.

A weakening labor market marked by consumers spending beyond their income capacities, with dwindling savings and increasingly diminishing borrowing options, is unlikely to sustain the rate of consumption which has dominated heretofore. And considering the prominent role which consumption has played in buoying economic data for some time, suggests an unfavorable trajectory for economic growth ahead.

With declining demand, firms are likely to struggle to pass along cost pressures, which in turn does not augur well for US production. The recent Institute of Supply Management (ISM) manufacturing gauge fell 2.3 points from September to October, landing at 46.7 (below 50 indicates contraction) in the largest decline in over one year. This indicator may, however, rebound in the wake of UAW strike resolutions. The ISM services indicator, meanwhile, fell from 53.6 in September to 51.8 in October, indicating ongoing expansion, albeit at a slowing pace.

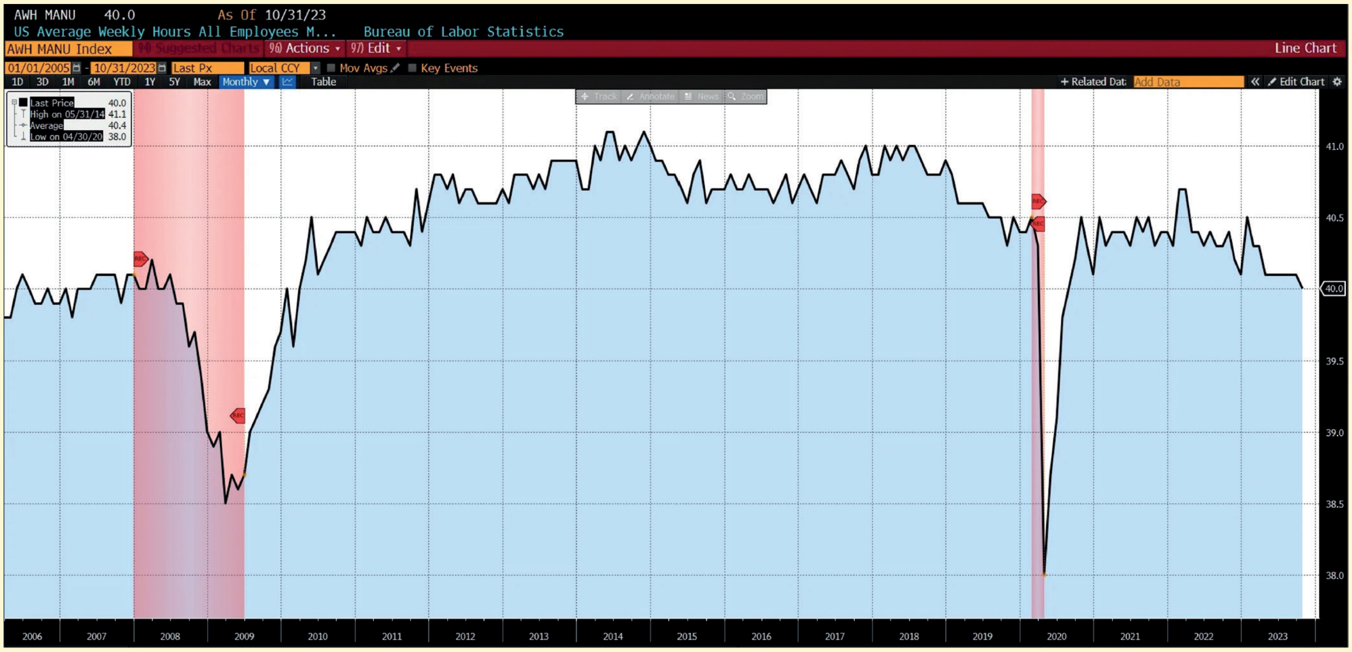
There are signs in equity markets of a broader slowdown as well. Berkshire Hathaway's cash position at the end of September 2023 reached a record $157.2 billion, of which some $97.3 billion was in cash and T-bills. A quarterly increase of 36 percent in cash and cash-equivalent instruments amid an increase of 3 percent in equity investments suggests a paucity of opportunities, at least in the context of higher yielding government securities. Since the reporting season began, S&P 500 4th quarter earnings per share estimates have declined by nearly half, from 7.6 to 4.6 percent. Bloomberg reports that 8 of eleven sectors have been subject to negative growth revisions.

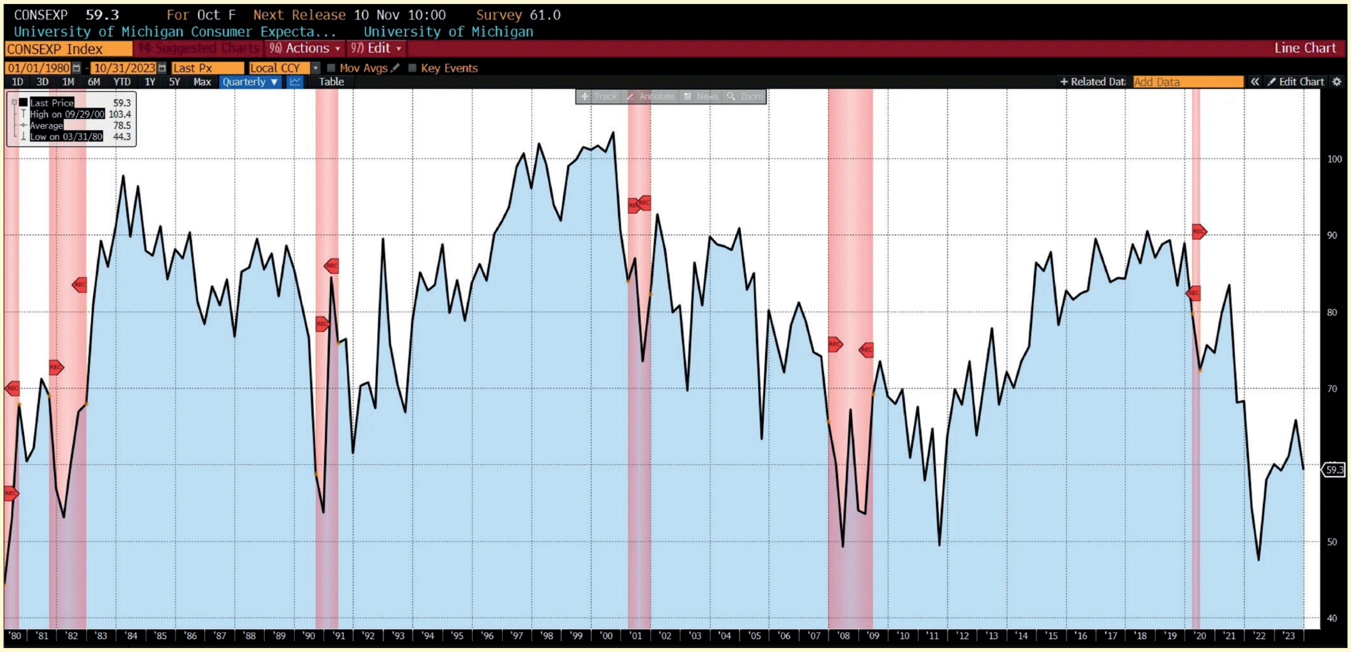
"Mega-bankruptcies," which describes filings by firms with greater than $1 billion in assets, reached 16 in the first half of 2023. From 2005 through 2022, that number averaged 11. Bankruptcies filed by both public and private companies holding assets exceeding $100 million rose in the first half of 2023, reaching a total of 72 filings, which has already exceeded the 53 bankruptcy filings recorded in 2022.

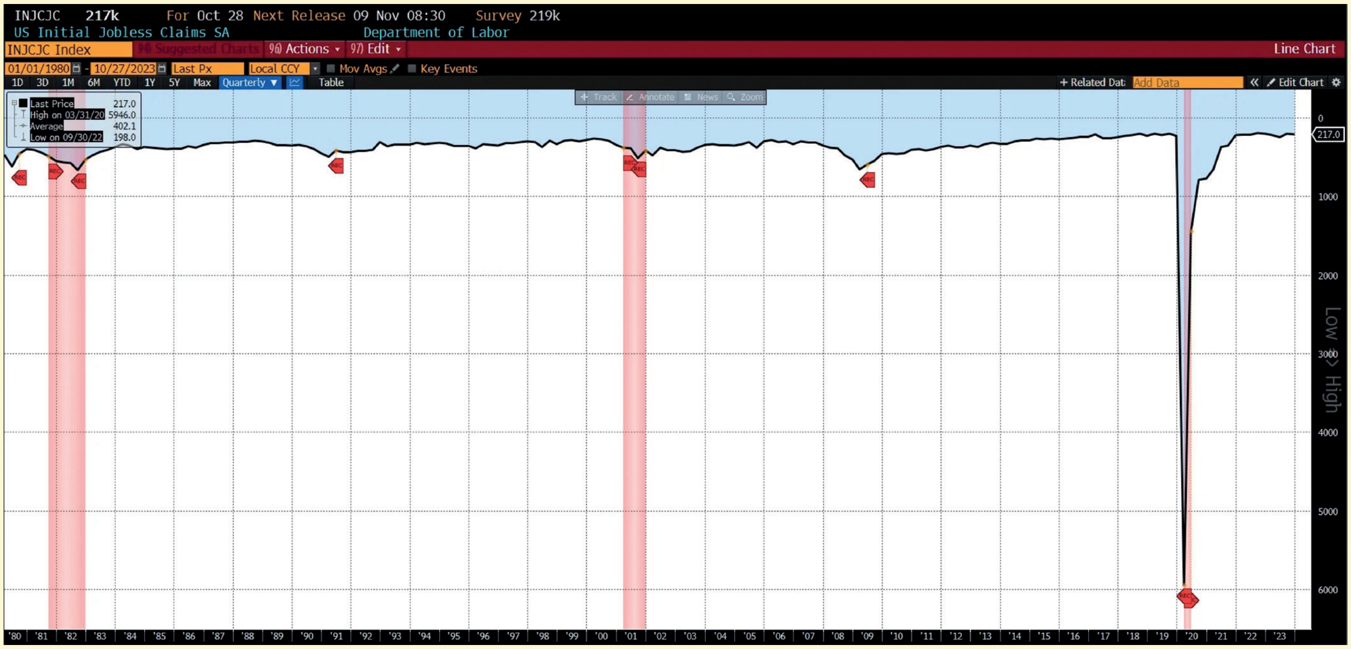
Among bellwethers, Caterpillar Inc.'s third quarter order backlog showed its first annual decline since mid-2020. Although the COVID pandemic skews results somewhat, of ten other instances in the past decade where Caterpillar has reported falling backlogs, seven saw GDP decline by roughly one percent in the following quarter. The global shipping firm Maersk has announced plans to reduce its global headcount by at least 10,000 employees percent amid a 92 percent drop in profits stemming from a decline in shipping rates. FreightWaves reports that some 35,000 trucking businesses (the majority of them owner-operated) have shuttered as of the end of September 2023 fiscal year.

In March 2023 we cited the "clear… deteriorat[ion]" of US economic fundamentals "with risks compounding to the downside." Our baseline estimate at that time was for an economic recession within the next twelve to eighteen months. Our choice to extend a substantially longer-term forecast for an economic downturn than most other economic analysts was anchored in historical data, empirical evidence, and professional experience. While we refrain from providing a specific magnitude for our recession forecast and acknowledge the possibility of inaccuracies or outright error, we maintain our contention that the US will enter an economic recession by September 2024.

LEADING INDICATORS






INJCJC 217k For Oct 28 Next Release 09 Nov 08:30 Survey 219k
US Initial Jobless Claims SA Department of Labor
INJCJC Index
Actions
Edit
Line Chart
01/01/1980 - 10/27/2023
Last Px
Local CCY
Mov Avgs
Key Events
1D 3D 1M 6M YTD 1Y 5Y Max Quarterly Table
Related Dat
Add Data
Edit Chart
Last Price 217.0
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Average 402.1
Low on 09/30/22 198.0
Low <> High
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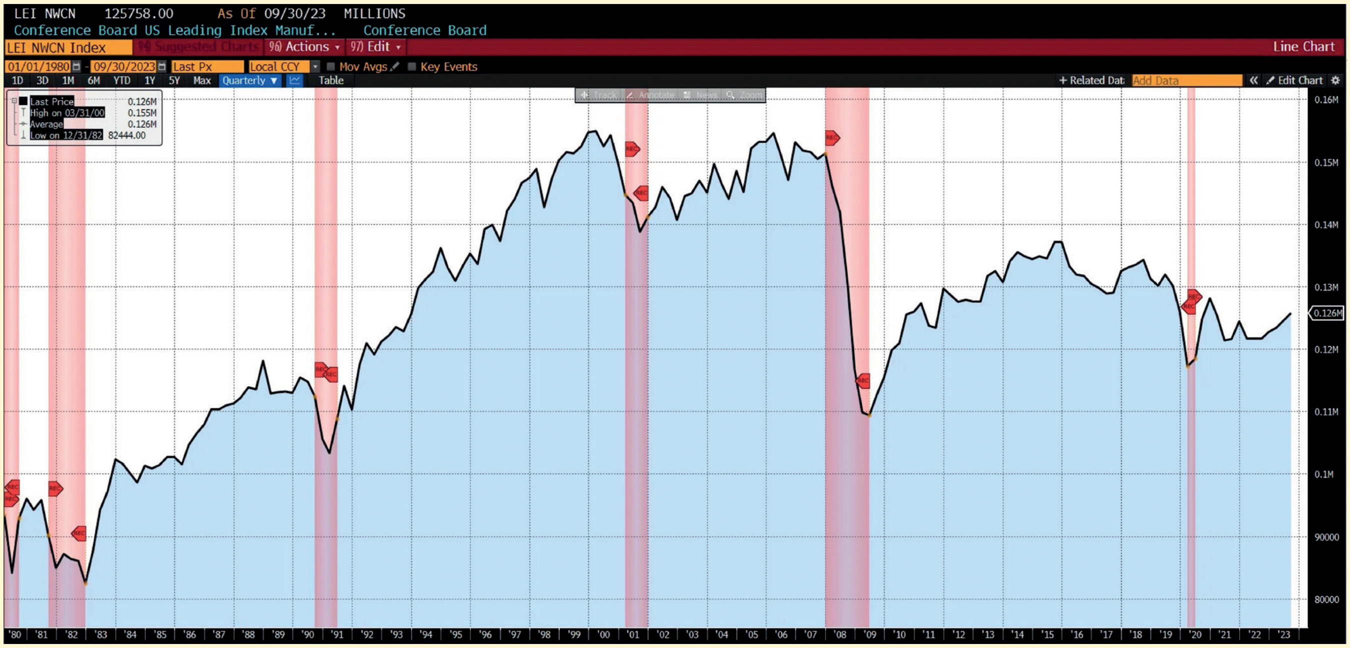
1000
2000
3000
4000
5000
6000
217.0


LEI NWCN 125758.00 As Of 09/30/23 MILLIONS
Conference Board US Leading Index Manuf... Conference Board
LEI NWCN Index
Actions
Edit
Line Chart
01/01/1980 - 09/30/2023
Last Px
Local CCY
Mov Avgs
Key Events
1D 3D 1M 6M YTD 1Y 5Y Max Quarterly Table
Related Dat
Add Data
Edit Chart
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High on 03/31/00 0.155M
Average 0.126M
Low on 12/31/82 82444.00
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0.15M
0.14M
0.13M
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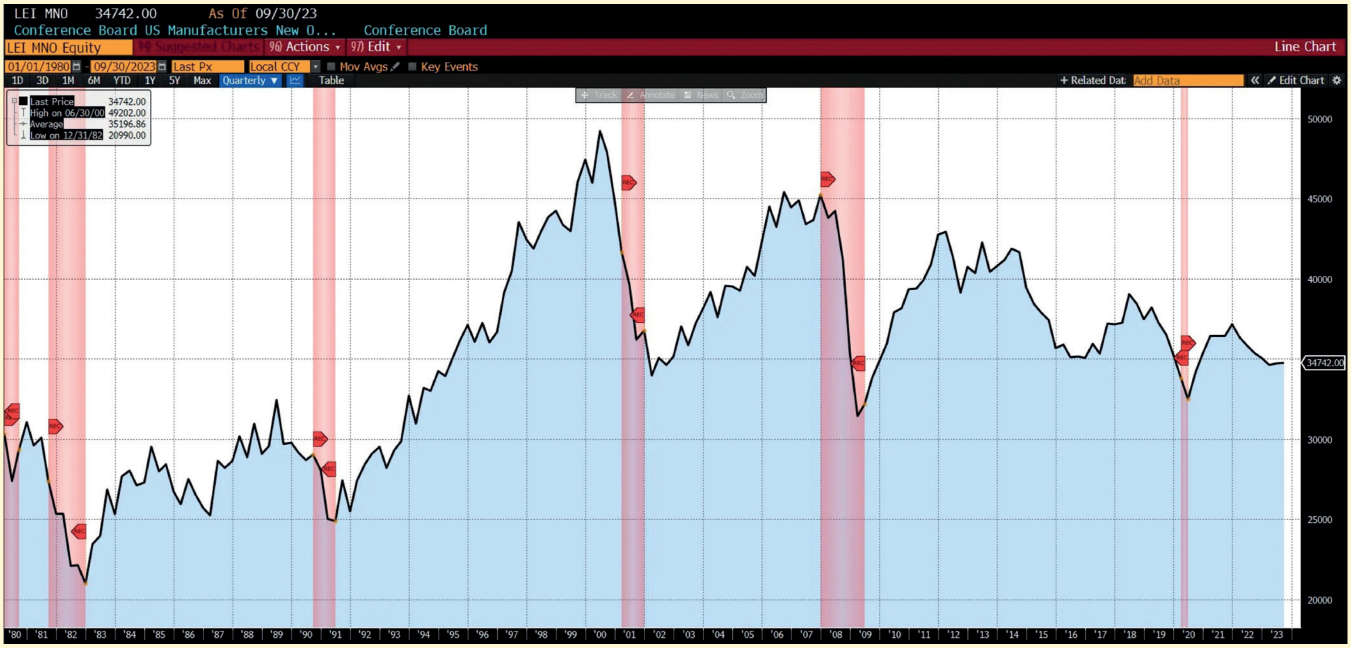
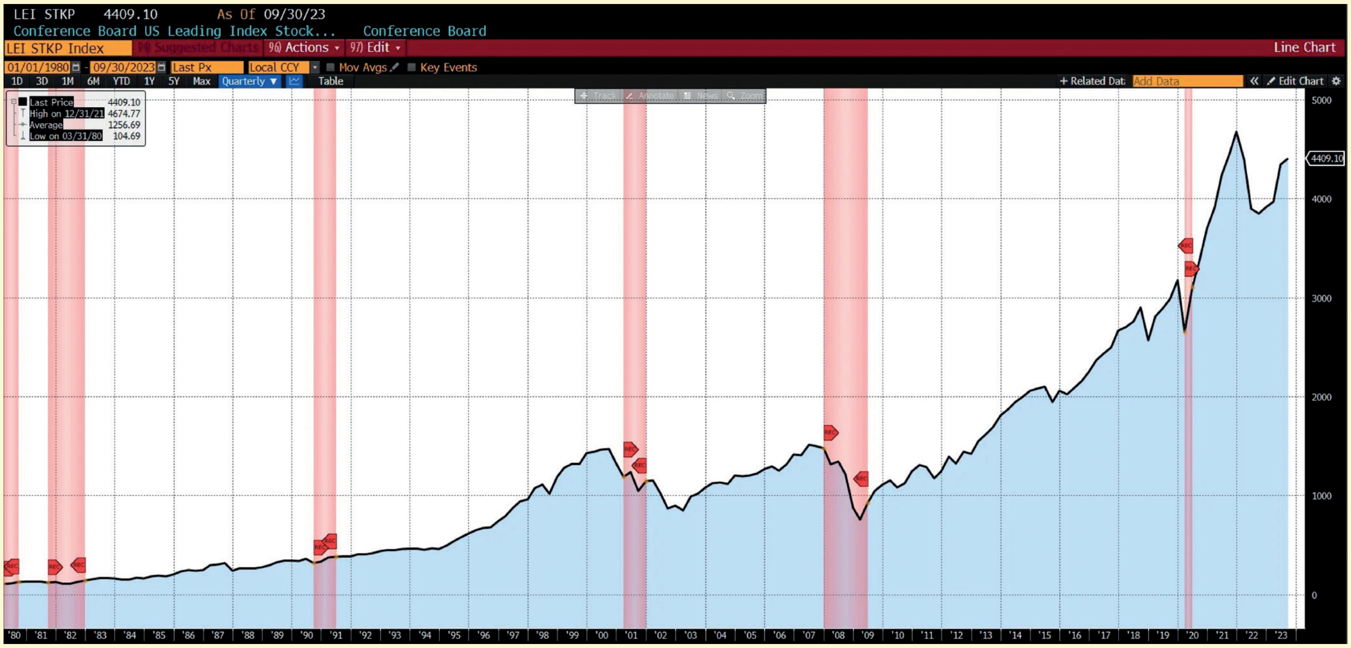
0.12M
0.11M
0.1M
90000
80000


LEI MNO 34742.00 As Of 09/30/23
Conference Board US Manufacturers New O... Conference Board
LEI MNO Equity
96) Actions
97) Edit
Line Chart
01/01/1980 - 09/30/2023
Last Px
Local CCY
Mov Avgs
Key Events
1D 3D 1M 6M YTD 1Y 5Y Max Quarterly
Table
Last Price 34742.00
High on 06/30/00 49202.00
Average 35196.86
Low on 12/31/82 20990.00
50000
45000
40000
34742.00
30000
25000
20000
'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 STKP 4409.10 As Of 09/30/23
Conference Board US Leading Index Stock... Conference Board
LEI STKP Index
96) Actions
97) Edit
Line Chart
01/01/1980 - 09/30/2023
Last Px
Local CCY
Mov Avgs
Key Events
1D 3D 1M 6M YTD 1Y 5Y Max Quarterly
Table
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High on 12/31/21 4674.77
Average 1256.69
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4409.10
4000
3000
2000
1000
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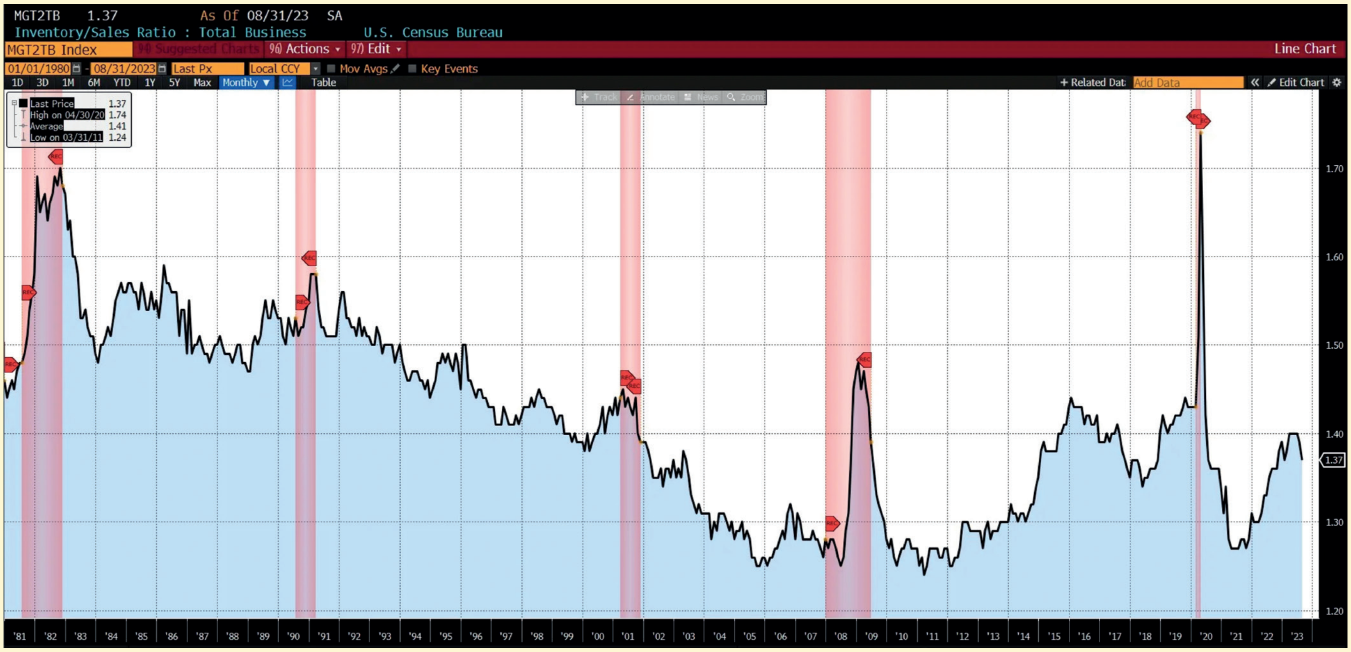
MGT2TB 1.37 As Of 08/31/23 SA
Inventory/Sales Ratio : Total Business U.S. Census Bureau
MGT2TB Index
Line Chart
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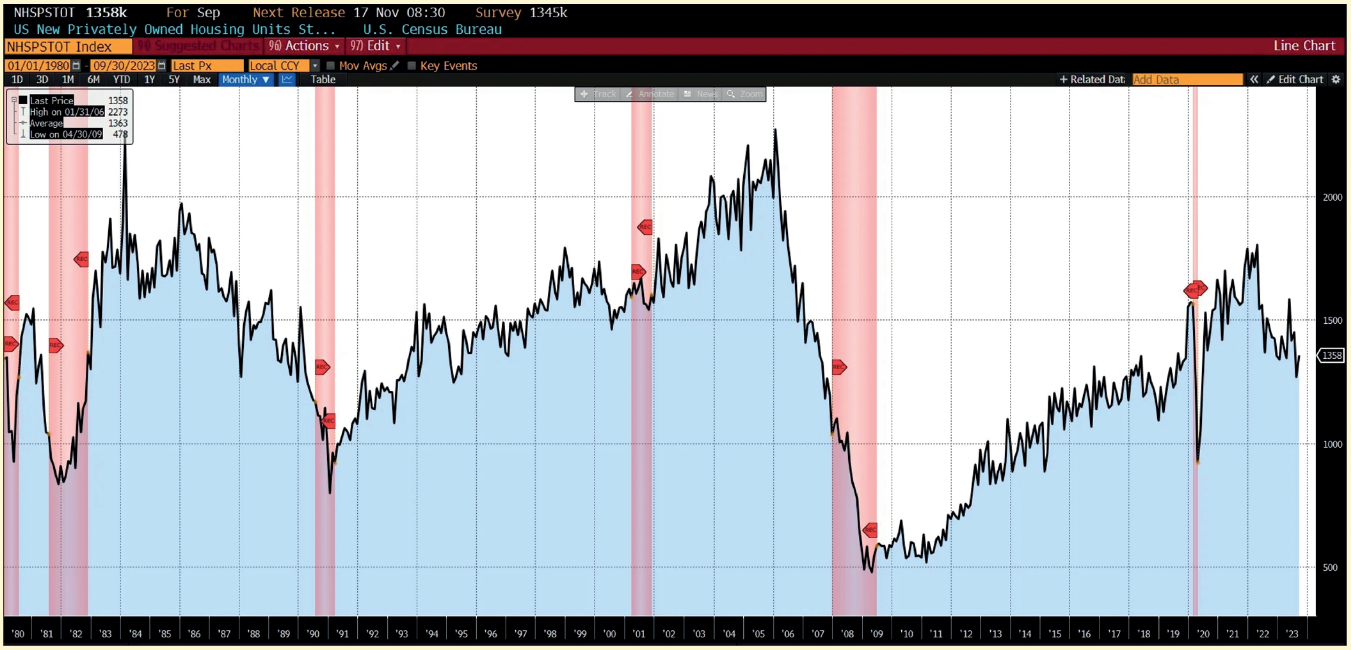
High on 04/30/20 1.74
Average 1.41
Low on 03/31/11 1.24


NHSPSTOT 1358k For Sep Next Release 17 Nov 08:30 Survey 1345k
US New Privately Owned Housing Units St... U.S. Census Bureau
NHSPSTOT Index
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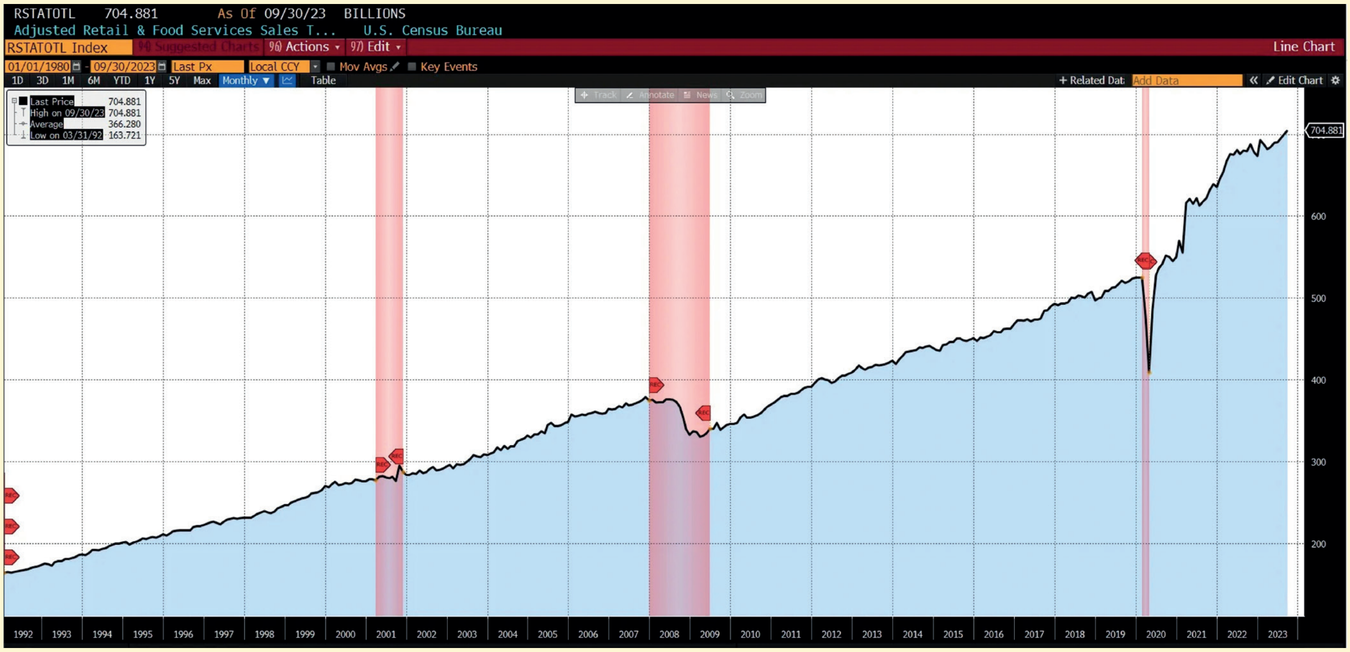
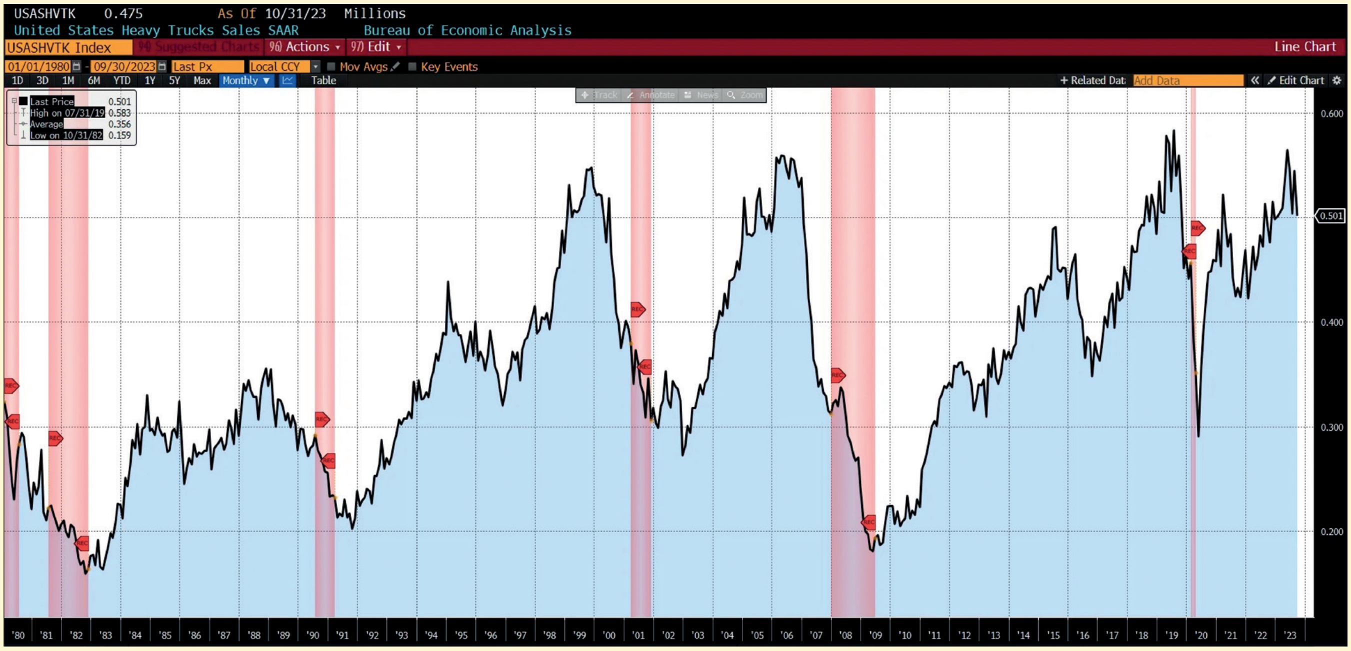
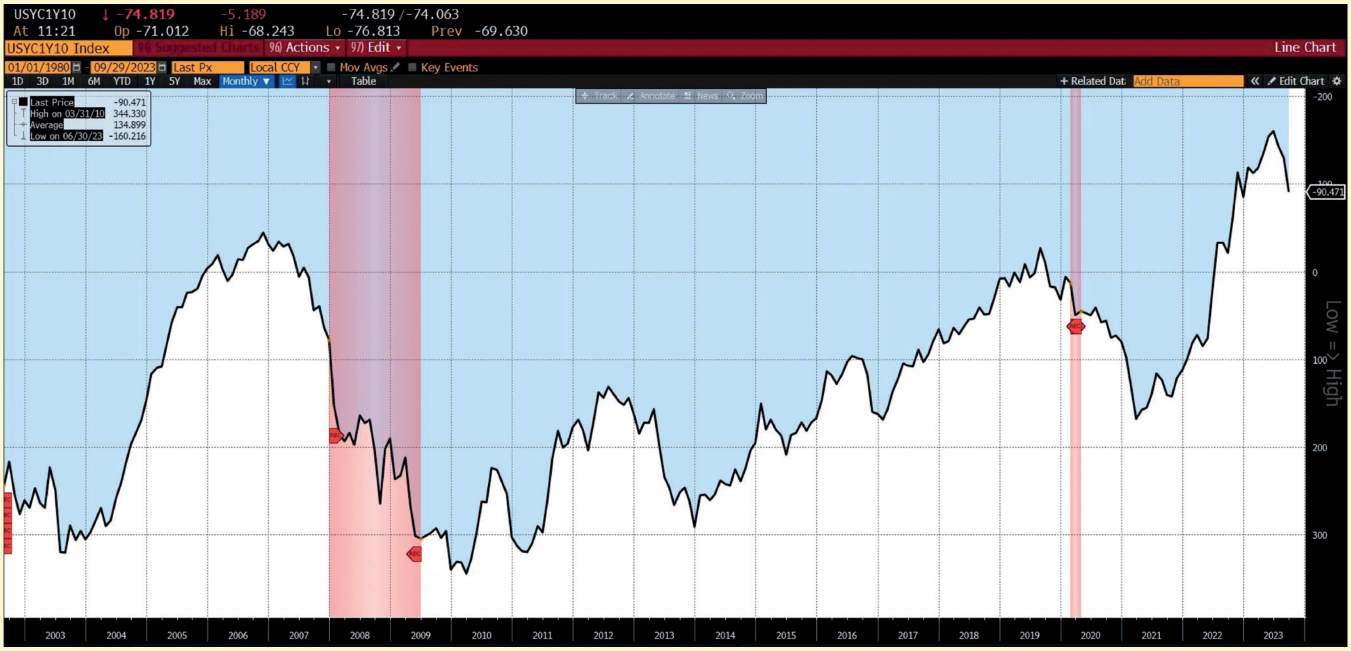
High on 01/31/06 2273
Average 1363
Low on 04/30/09 478


RSTATOTL 704.881 As Of 09/30/23 BILLIONS
Adjusted Retail & Food Services Sales T... U.S. Census Bureau
RSTATOTL Index
Line Chart
Last Price 704.881
High on 09/30/23 704.881
Average 366.280
Low on 03/31/92 163.721


USASHVTK 0.475 As Of 10/31/23 Millions
United States Heavy Trucks Sales SAAR Bureau of Economic Analysis
USASHVTK Index
Line Chart
Last Price 0.501
High on 07/31/19 0.583
Average 0.356
Low on 10/31/82 0.159


USYC1Y10
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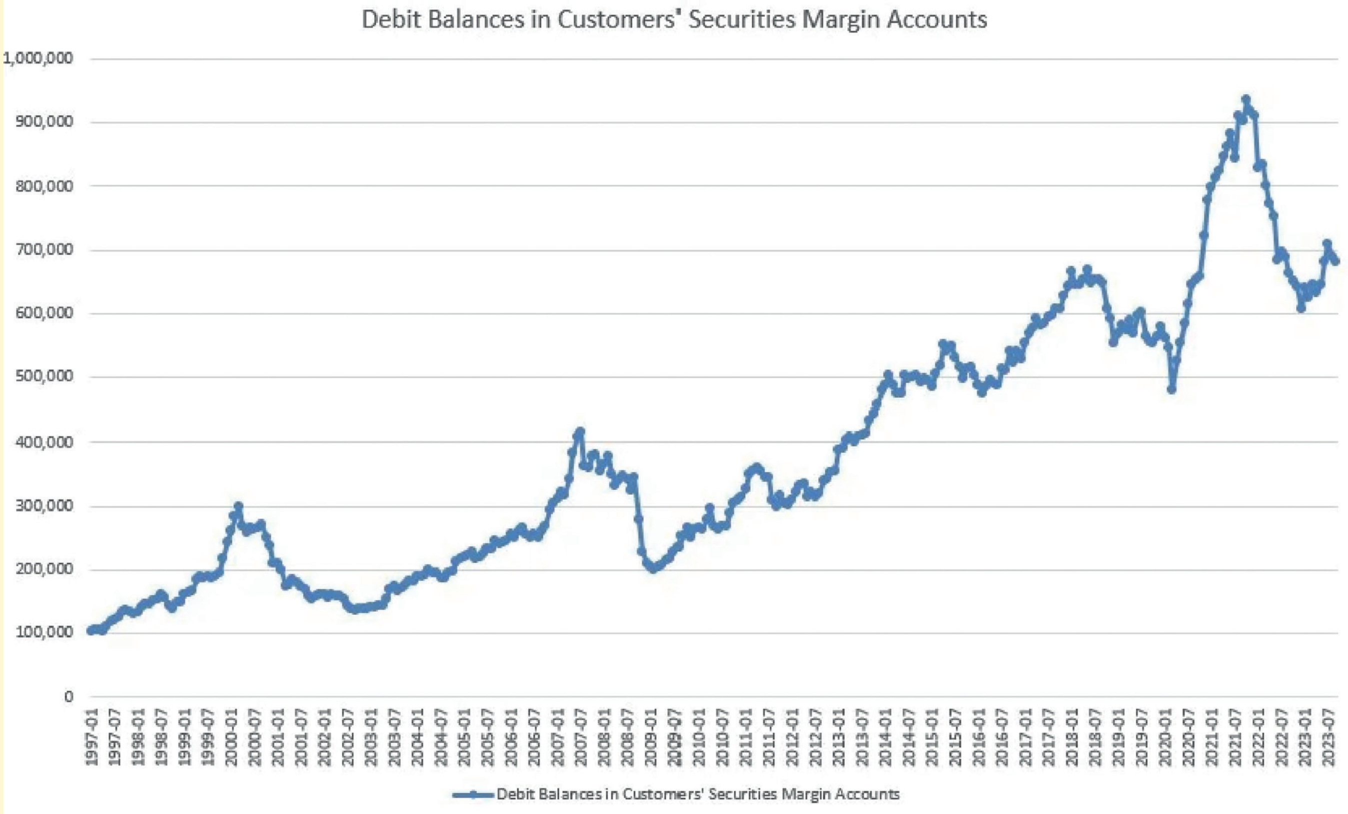
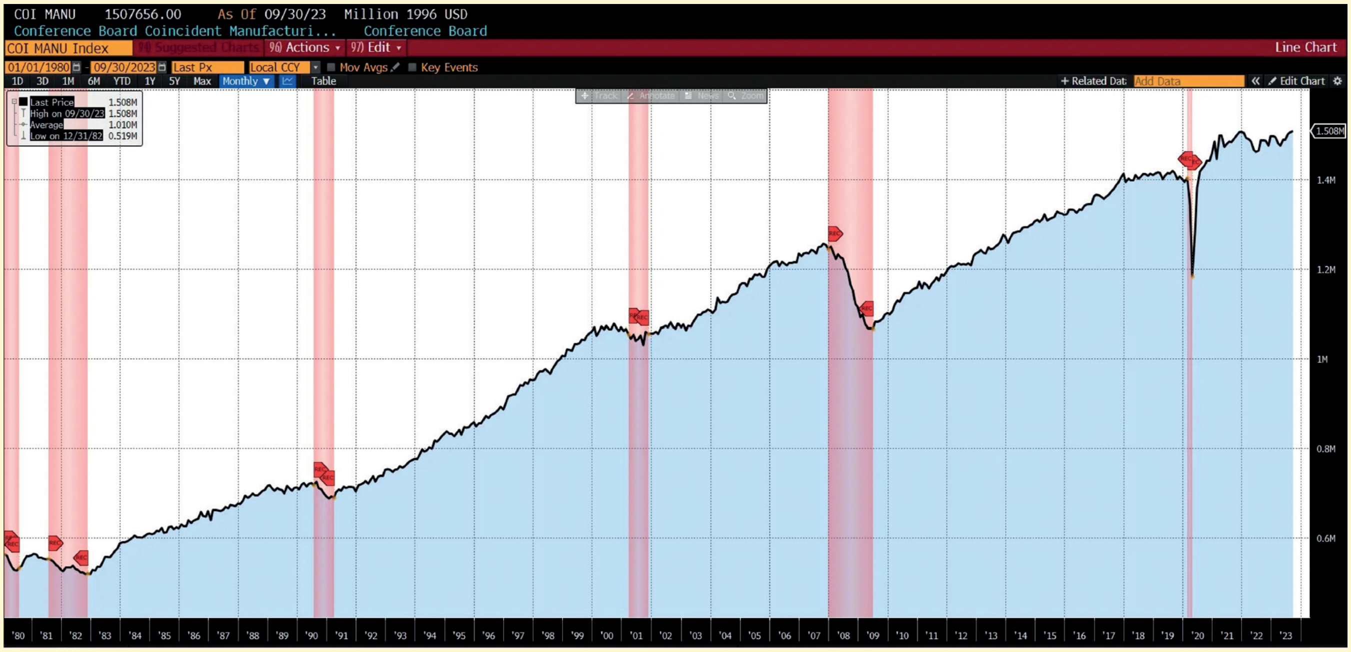
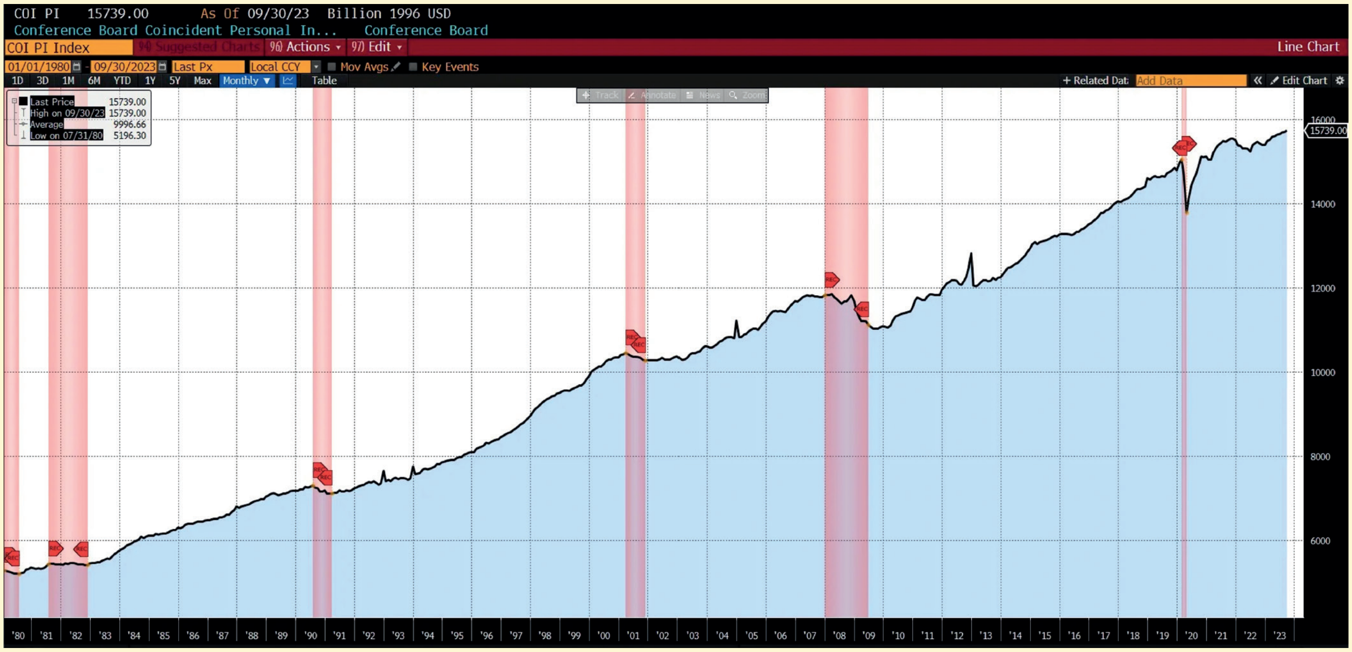
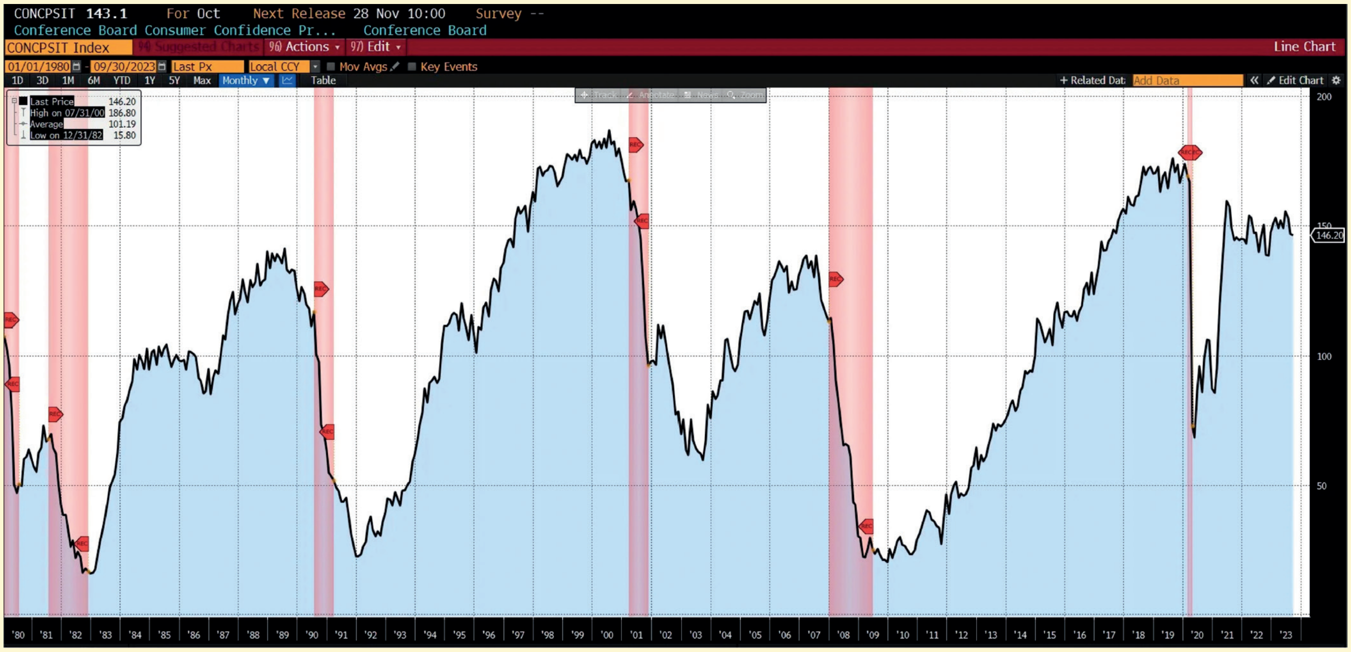
Low on 06/30/23 -160.216
Low => High

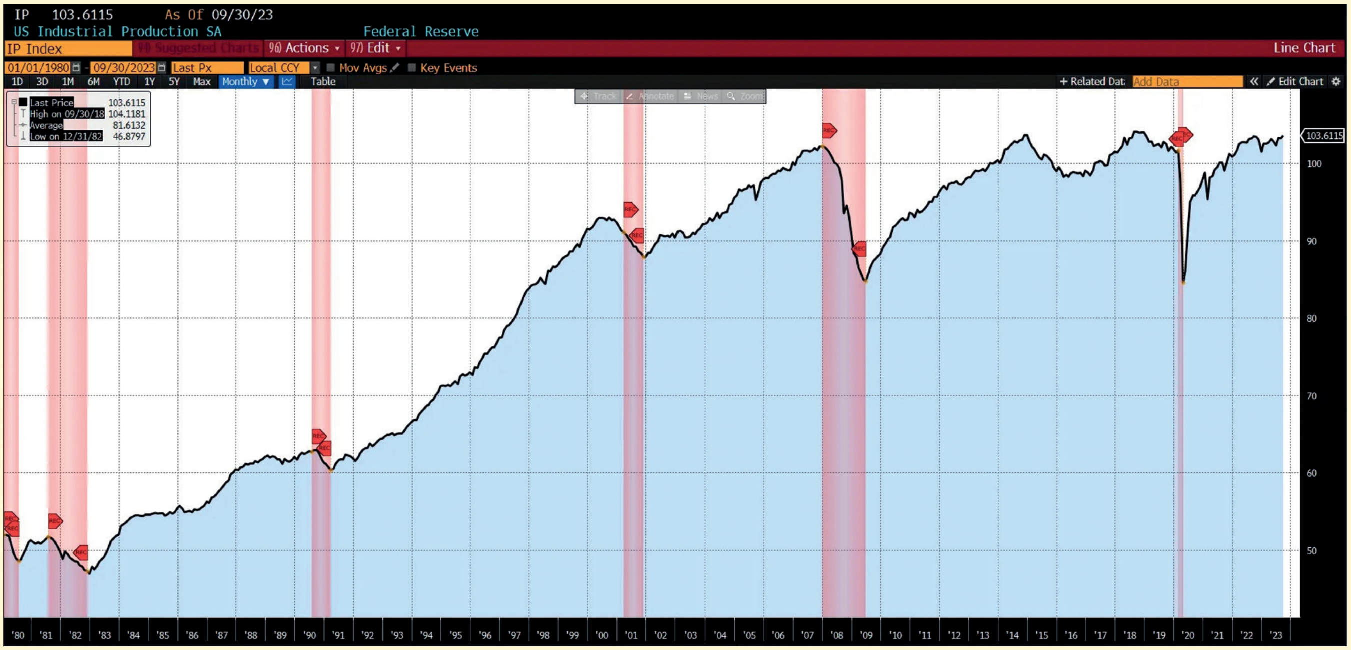

Debit Balances in Customers' Securities Margin Accounts

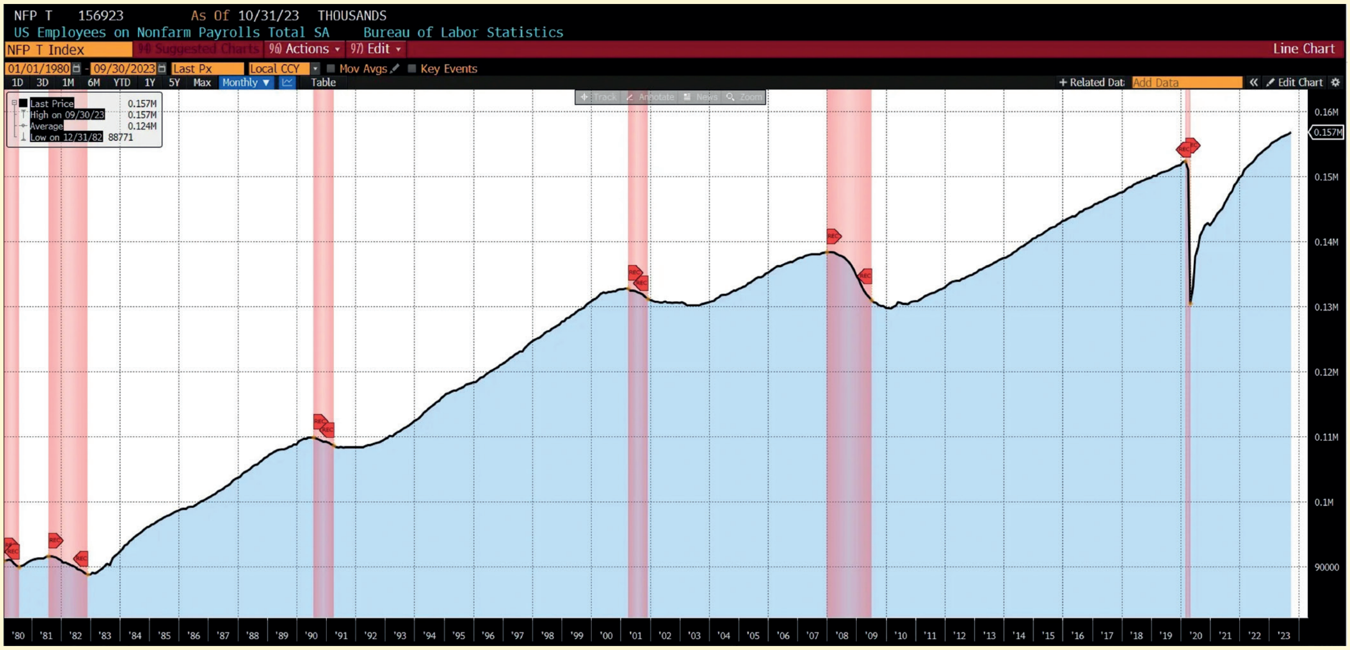
ROUGHLY COINCIDENT INDICATORS

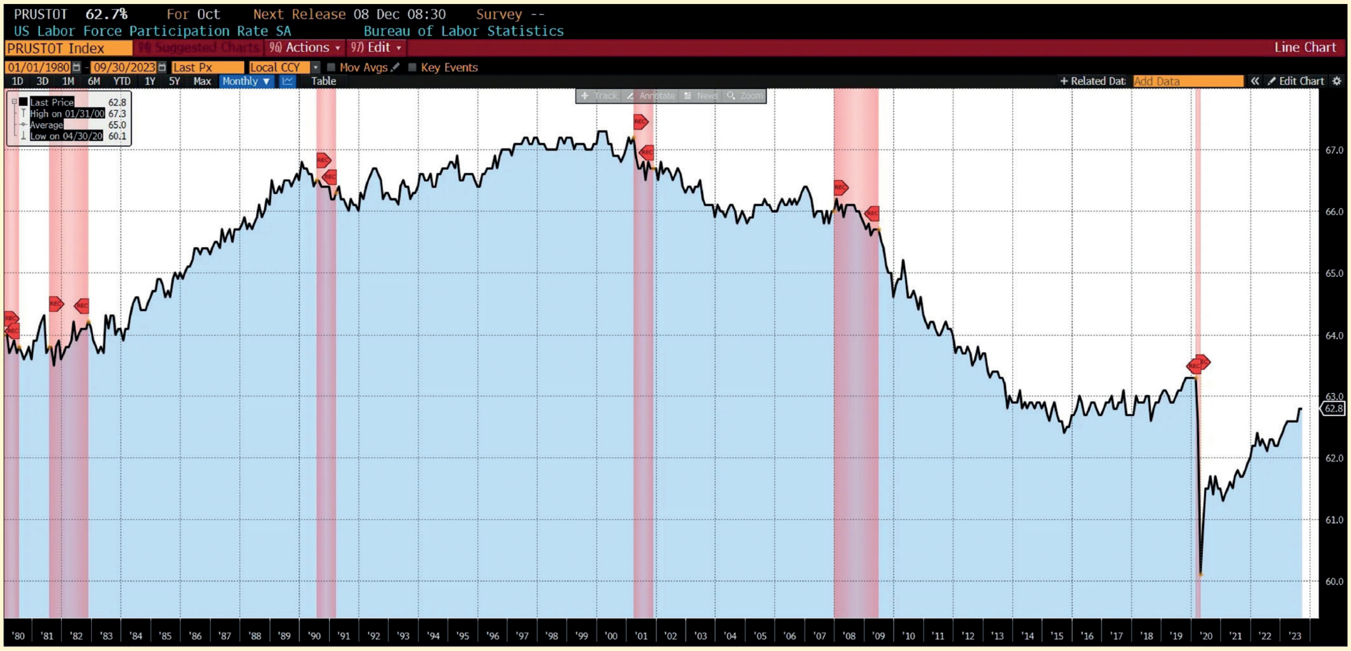




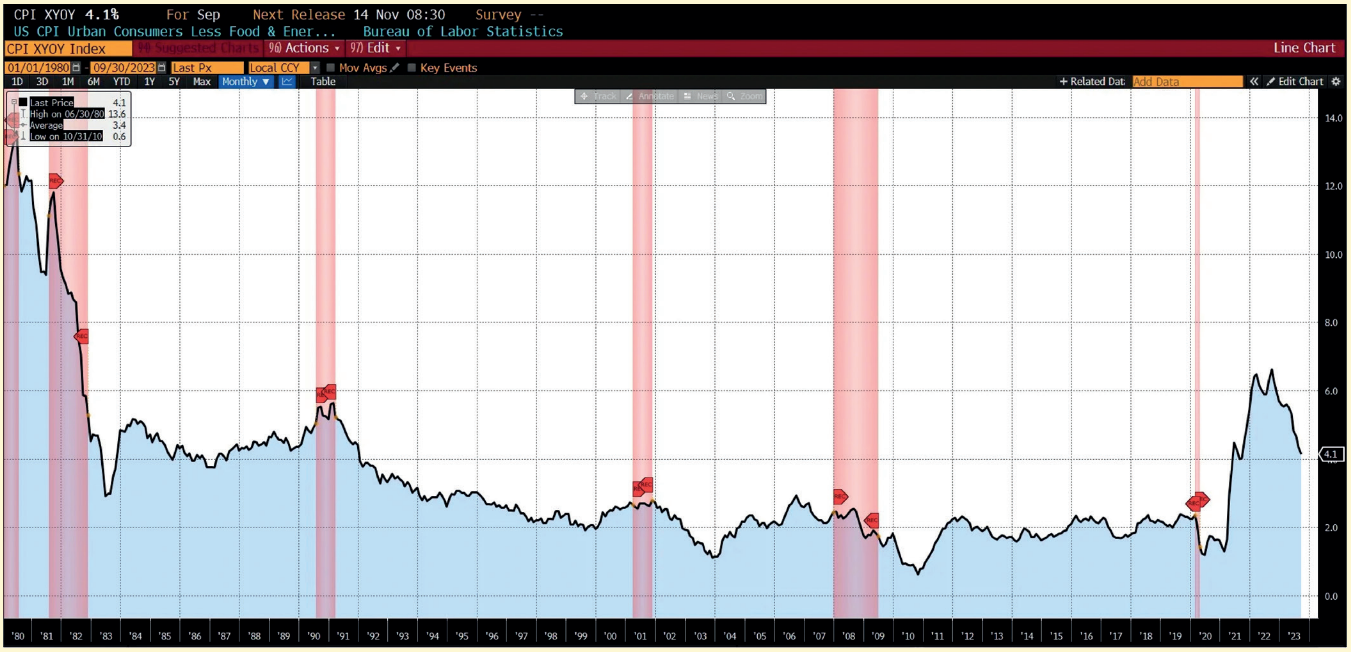

CONCPSIT 143.1 For Oct Next Release 28 Nov 10:00 Survey --
Conference Board Consumer Confidence Pr... Conference Board
CONCPSIT Index
Line Chart
01/01/1980 - 09/30/2023 Last Px Monthly
Last Price 146.20
High on 07/31/00 186.80
Average 101.19
Low on 12/31/82 15.80

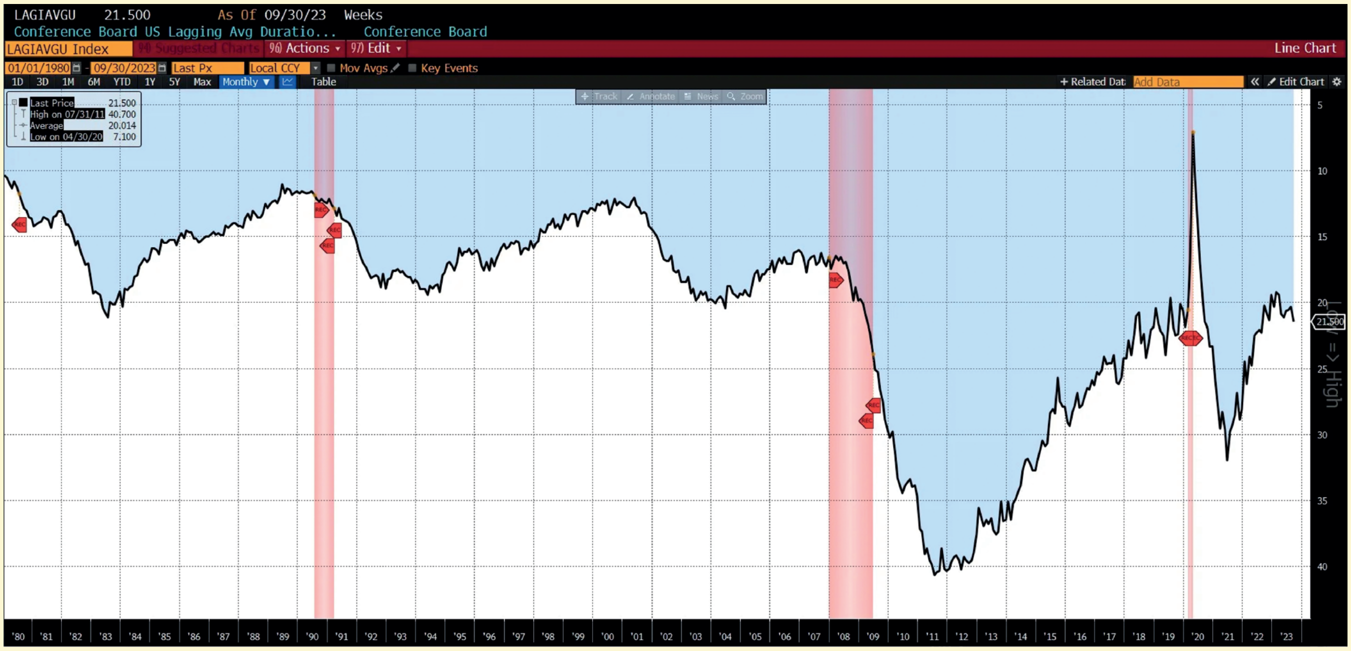

IP 103.6115 As Of 09/30/23
US Industrial Production SA Federal Reserve
IP Index
Line Chart
01/01/1980 - 09/30/2023 Last Px Monthly
Last Price 103.6115
High on 09/30/18 104.1181
Average 81.6132
Low on 12/31/82 46.8797

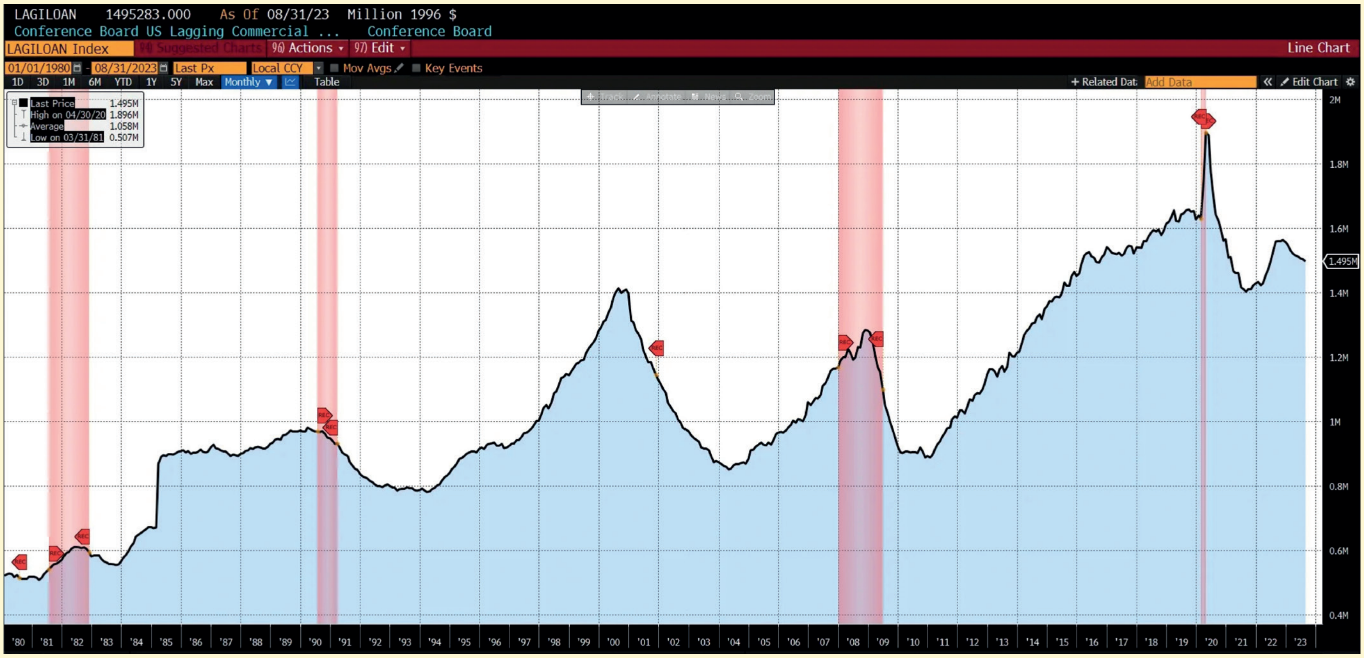

NFP T 156923 As Of 10/31/23 THOUSANDS
US Employees on Nonfarm Payrolls Total SA Bureau of Labor Statistics
NFP T Index
Line Chart

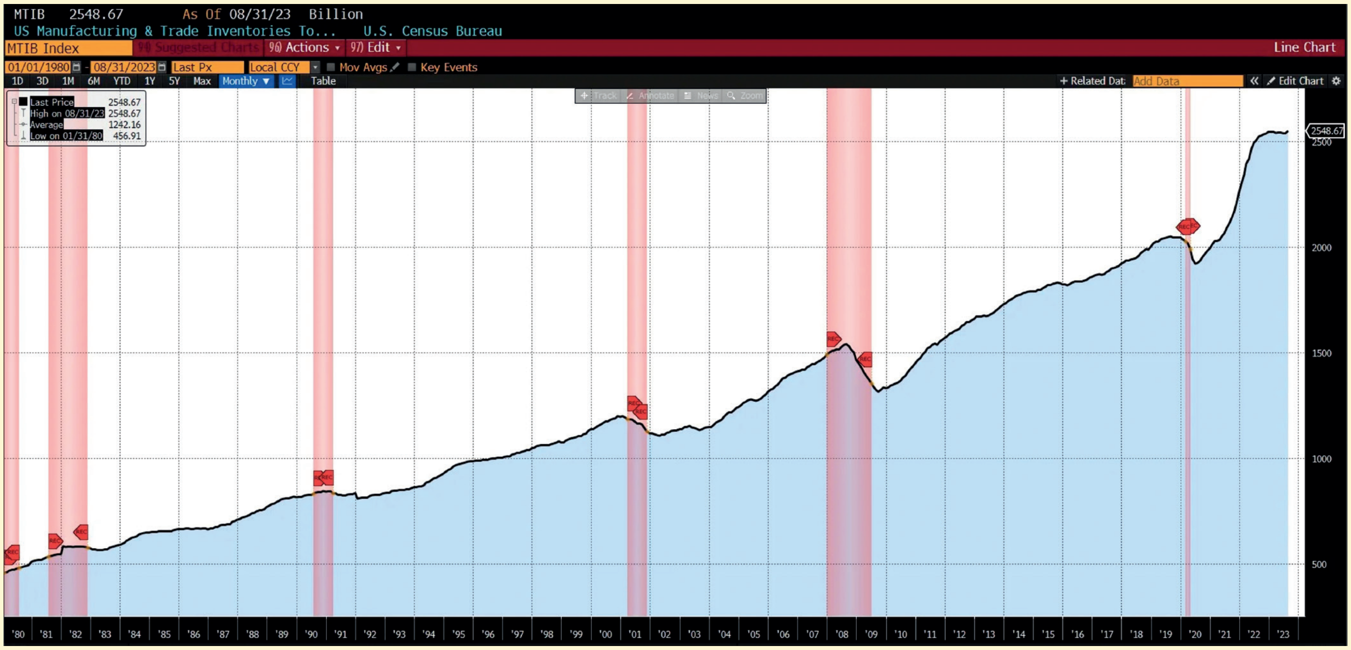

PRUSTOT 62.7% For Oct Next Release 08 Dec 08:30 Survey --
US Labor Force Participation Rate SA Bureau of Labor Statistics
PRUSTOT Index
Line Chart

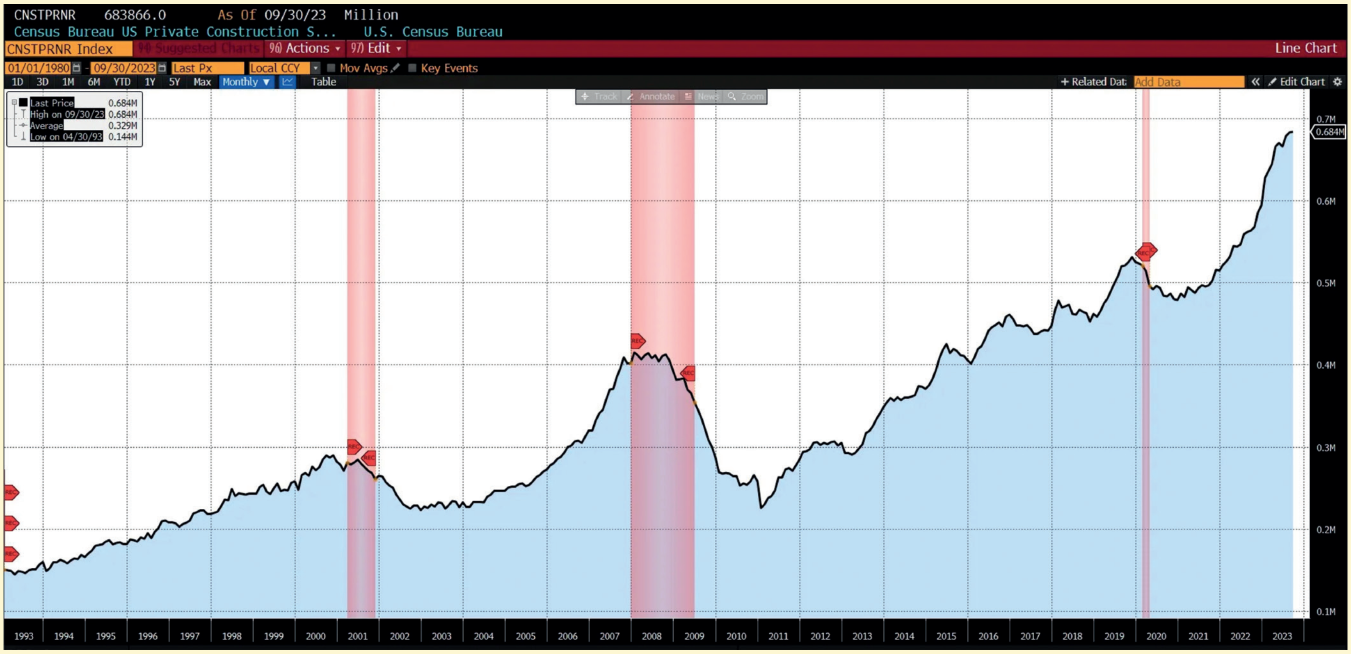
LAGGING INDICATORS




LAGIAVGU 21.500 As Of 09/30/23 Weeks
Conference Board US Lagging Avg Duratio... Conference Board
LAGIAVGU Index
Line Chart
Last Price 21.500
High on 07/31/11 40.700
Average 20.014
Low on 04/30/20 7.100
'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


LAGILOAN 1495283.000 As Of 08/31/23 Million 1996 $
Conference Board US Lagging Commercial ... Conference Board
LAGILOAN Index
Line Chart
Last Price 1.495M
High on 04/30/20 1.896M
Average 1.058M
Low on 03/31/81 0.507M
'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


MTIB 2548.67 As Of 08/31/23 Billion
US Manufacturing & Trade Inventories To...
U.S. Census Bureau
MTIB Index
Line Chart
Last Price 2548.67
High on 08/31/23 2548.67
Average 1242.16
Low on 01/31/80 456.91


CNSTPRNR 683866.0 As Of 09/30/23 Million
Census Bureau US Private Construction S...
U.S. Census Bureau
CNSTPRNR Index
Line Chart
Last Price 0.684M
High on 09/30/23 0.684M
Average 0.329M
Low on 04/30/93 0.144M

CAPITAL MARKET PERFORMANCE

Ticker		Short Name	%1M	%3M	%1YR	3 Year Annualized	5 Year Annualized	10 Year Annualized
SPR		S&P 1500 Composite Index	+1.53%	-3.63%	+13.70%	9.1546	11.0741	10.8346
SPXT	d	S&P 500 Total Return	+1.40%	-3.00%	+16.60%	9.2386	11.5421	11.1691
SPX	d	S&P 500 INDEX	+1.75%	-2.98%	+15.16%	9.2188	11.5252	11.1540
MID	d	S&P 400 MIDCAP INDEX	-.24%	-9.38%	+.95%	8.1830	7.1239	7.9257
RTY	d	RUSSELL 2000 INDEX	-.60%	-11.42%	-4.12%	3.1563	3.5907	5.6085
SXXP	d	STXE 600 (EUR) Pr	-.48%	-3.67%	+5.85%	10.0519	7.5351	6.5546
TLT US	d	ISHARES 20+ YEAR	+3.69%	-8.02%	-5.75%	-16.4650	-2.9433	-.1276
QLTA US	d	ISHARES AAA - A	+1.67%	-2.75%	+1.43%	-5.8179	.7491	1.3778
CRY	d	TR/CC CRB ER Index	+1.80%	+.97%	-1.75%	24.0408	8.0672	.1178
XAU		Gold Spot $/Oz	+5.53%	+1.43%	+17.23%			
XAG		Silver Spot $/Oz	+2.98%	-2.60%	+8.34%			
ILM3NAVG		Bankrate 30Y Mortgage Rates Na	-1.01%	+6.37%	+7.68%			
ILM1NAVG		Bankrate 15Y Mortgage Rates Na	+1.13%	+7.99%	+10.49%			
MB301ARM		5 Year ARM	+4.64%	+12.65%	+16.93%			
ILA3NAVG		Bankrate 30Y Fixe Mtg Refis Na	+2.81%	+5.92%	+25.65%			

Joe Biden, Shifty Economists, and the Big Lie

PHILLIP W. MAGNESS

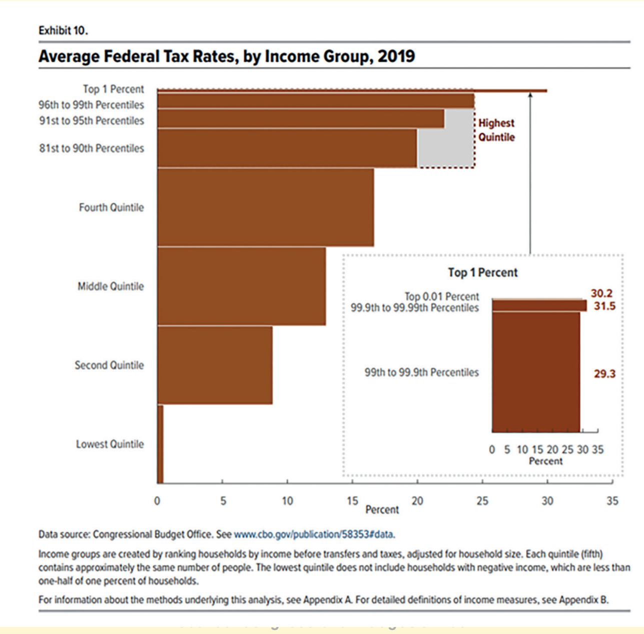
F.A. Hayek Chair in Economics and Economic History

Taking cues from his economic advisers, President Joe Biden has announced a proposed 25 percent minimum tax on the wealthy as a centerpiece of his "Bidenomics" plan. This "billionaire tax," which he outlined in a speech last month, is premised on the notion that the U.S. tax system provides too many breaks to the highest earners. As Biden claimed in his remarks, "billionaires pay an average of — guess what? — less than 8 percent in federal taxes — less than 8 percent on a yearly basis." To drive home the point, the President declared that this is a "lower federal tax rate than a firefighter, a teacher, a cop" pays.

Biden's contentions are meant to shock his listeners into believing that the federal tax system is steeply regressive, penalizing the working class at the behest of the rich. His statistics, however, are complete nonsense.

According to Congressional Budget Office statistics for 2019 (the most recent year with data), the heaviest tax burdens still fall squarely on the highest income earners. The Top 1 percent of filers pay an average federal tax rate of 30 percent. This number holds among the ultra-wealthy as well. If we restrict our subset to only the top 0.01 percent of earners, a category that generally applies to people with multi-million dollar annual salaries, the CBO estimates an average federal tax rate of 30.2 percent.

By contrast, the average tax rate on the lowest quintile of filers was just 0.5 percent in 2019 – a result of generous tax credits that are designed to relieve the poor of almost their entire federal tax burden. The second lowest quintile paid an average rate of just 8.9 percent in federal taxes.



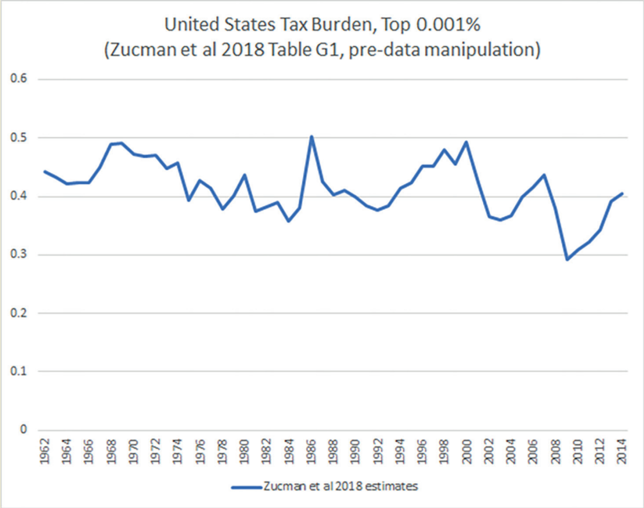
As we can see in the data, President Biden has his story exactly backwards. The average wealthy filer already pays well in excess of Biden's proposed 25 percent minimum tax, whereas the average working class filer pays only a little higher than the 8 percent rate that Biden falsely attributes to the ultra-wealthy.

Why, then, is the President so statistically confused?

The answer comes from his administration's continued reliance on manipulated tax stats by economists Gabriel Zucman and Emmanuel Saez. In 2019, the New York Times and Washington Post ran splashy headlines declaring that billionaires paid lower tax rates than average Americans, attributing this figure to a new book by Zucman and Saez. A sympathetic press heralded the Zucman-Saez numbers before they ever went through peer review because they appeared to confirm the progressive left's favored political narrative.

When I placed the Zucman-Saez stats under a microscope, several irregularities emerged. First, they intentionally excluded tax benefits for lower income filers such as the Earned Income Tax Credit, creating an illusion that the poor face a much higher tax rate than they actually do. Second, they manipulated their calculations for assigning corporate tax incidence among the rich, creating the illusion that billionaires only pay a little more than half of the actual rates. As part of the fallout from this discovery, Harvard University reportedly rescinded a job offer to Zucman because his "new" data could not be trusted.

There's another twist to the story, though. Before Zucman and Saez cultivated the patronage of the media and left-wing politicians, they released an earlier estimate of the total federal, state, and local tax burden of an even smaller slice of the ultra-wealthy. As of 2014, the most recent year of their data, the tax rate for this group stood at 40.6 percent.



Furthermore, as the chart above shows, the total tax burden on the ultra-wealthy has hovered just north or south of about 40 percent since the 1960s, subject to a few fluctuations tied to business cycle events and tax code overhauls.

So, no, Mr. President, the wealthiest filers are not paying a lower tax rate than the rest of us. IRS statistics show that America's federal tax system remains steeply progressive, and no politically motivated data manipulation will ever alter that fact.

– October 10, 2023

New Studies Show How Business Taxes Hurt Average Americans

JASON SORENS
Senior Research Faculty

Did you know that Congress and President Biden raised your taxes? The hike masquerades as a tax hike on business, but according to the latest research, it actually hits your paycheck.

State-of-the-art economic research overwhelmingly confirms that high business income taxes harm investment, research and development, worker productivity, wages, and growth, and three new studies explain just how.

Let's work through the basic economics. When a company pays higher taxes on its profits, it has less money left over to return to shareholders as dividends and to reinvest in the company. Those two effects have further bad consequences.

Falling dividends discourage people from saving and investing in companies. Rather than save and invest, they consume more. That means lower growth in the future.

Declining reinvestment hurts research and development and capital purchases. The new minimum tax on business income, part of the Inflation Reduction Act, makes this problem especially severe, because it punishes companies who would otherwise benefit from deductions for capital investment.

Evidence supports theory. The most recent, comprehensive review of published studies in the respected *Annual Review of Economics* reports decreases in wages resulting from a $1 increase in corporate income taxation ranging from 60 to 66 cents, with bigger effects for the less skilled, women, and young workers. About half of the decline in wages is passed on to landowners. They also find that when taxes increase the cost of capital by 1 percent, that reduces business investment by between 0.5 and 1 percent. Unpublished studies sometimes find no effect of corporate taxation on GDP growth, but many of these studies are of low quality, produced by activist organizations. The published literature consistently shows a negative effect of corporate taxation on growth.

The two newest studies are not covered in that literature review. Still awaiting peer review, they have been published by the prestigious National Bureau of Economic Research.

The first, by economists at the University of California–Davis, University of London, and London Business School, looks at the effects of politically driven corporate income tax cuts in the U.S. between 1950 and 2006. (They focus on politically driven cuts to improve causal identification.) They find that business tax cuts cause temporary growth in private research and development spending and permanent growth in productivity and GDP.

In the second new paper, an overlapping group of authors looks at who gains from corporate tax cuts. They find that goods producers raise capital expenditure and employment in response to a tax cut, while service sector companies increase dividends. So raising corporate income taxes cuts manufacturing investment and jobs.

State tax cuts may have even larger effects, because the investment they spur is not just new investment, but reallocation from other states, and because many states face balanced-budget requirements that should make any tax cuts that do occur more permanent. Recent research supports this hypothesis, with state tax cuts increasing both jobs and the number of establishments, in roughly equal amounts from new investment and from reallocation from other states.

New Hampshire's recent experience supports this finding. The Granite State has been cutting business profit and wage base taxes consistently since 2015. From 2015 to 2021 (the most recent year for which data are available), New Hampshire's real personal income grew by 24 percent, compared to 19 percent for its closely linked neighbor, Massachusetts. In the six years **before** the tax cuts, New Hampshire had underperformed Massachusetts in income growth, 14 percent to 18 percent. So New Hampshire's growth sped up and surpassed Massachusetts after business tax cuts began.

All this means that Congress's new tax increases on business couldn't come at a worse time: right when business is still recovering from the supply-chain shocks of the pandemic and wages fail to keep pace with inflation.

According to the Institute for Supply Management, new orders and jobs in manufacturing fell in August for the 10th straight month after a 28-month-long boom. Could the Biden tax hikes already be hitting the manufacturing sector?

Congress and state legislatures should start listening to economists, not special interests. Economists may disagree about many things, but on this point they speak with one voice: If you want to help workers, especially in manufacturing, cut taxes on their employers.

– October 7, 2023

Inflation Ticks Up Again. Keep an Eye on Oil

THOMAS L. HOGAN
Senior Research Faculty

The Consumer Price Index (CPI) increased for the third straight month, interrupting the downward trend seen over the previous year.

Recent inflation has been a heavy burden for most Americans. It has eroded the value of the U.S. dollar, reducing its purchasing power by more than 20 percent since the start of the pandemic recovery. After much delay, the Federal Reserve finally began raising interest rates in March 2022, causing inflation to fall from July 2022 through June 2023.

The past few months, however, have interrupted the downward trend. What has caused the recent uptick in inflation, and where might we expect it to go from here?

The Latest Numbers

The CPI for all items rose by 3.7 percent over the past 12 months, but the August and September increases were particularly high at annualized rates of 7.2 percent and 4.8 percent respectively. The main driver in those months was high oil prices, which pushed up the costs of gasoline and energy more broadly.

Core CPI (excluding food and energy) was higher than total CPI inflation over the past 12 months at 4.1 percent. Core CP ininflation, however, has not spiked as high as total CPI inflation in the past two months, coming in at annualized rates of 3.6 percent in each month.

The combination of high headline inflation and low core inflation is doubly bad for average Americans. The economy seems to be slowing, but they are still paying higher prices for gas, one of their most important purchases.

All About Oil

Interestingly, even core CPI appears to have been affected by the high price of oil. If we divide core CPI into goods and services, the average price of goods has seen zero net inflation over the past 12 months and has actually fallen in each of the past four months. Thus, all of the net price increases over the past year have come from services (not counting energy services).

If we look at the subcategories of services, there are two that stand out. The largest increase has come in Transportation Services, which has seen 9.1 percent inflation over the past year. This was partly due to higher used car prices in April and May, but the big increases in the past two months appear to be tied to higher gas prices.

The other major increase was in Shelter, which is the CPI category that captures the cost of housing. The average cost of shelter was up 7.2 percent over the past month.

What Comes Next?

A well-known problem with the CPI is that shelter is calculated in a way that lags changes in housing prices. Housing price indicators like the Case-Shiller index saw major increases during the pandemic recovery, but they are currently at about the same level as a year ago. Thus, we might expect the prices of shelter to see more moderate increases going forward.

The price of oil is less certain and is often affected by geopolitical factors. Renewed war in the Middle East, commodity trade agreements among the BRICs+ countries, and the US political response could all factor in. Major changes in oil prices seem likely to drive the near-term changes in CPI inflation, both headline inflation and possibly core as well.

Another big question is how the Fed will respond. With core inflation finally coming down, Fed officials may worry that a further uptick would lead to higher inflation expectations, which would make their job of bringing it down all the more difficult. If continued inflation leads to further interest rate hikes, the Fed runs the risk of over tightening monetary policy and potentially pushing the economy into recession.

What comes next depends a lot on global markets for crude oil. Sustained increases in oil prices could complicate the Fed's monetary policy decision, especially if they filter into core inflation, which Fed officials rely on in their monetary policy decisions.

– October 18, 2023

Argentina's Canary in the Coalmine

NIKOLAI G. WENZEL (Associate Research Faculty)
VALENTINA YAYI MORALES (Contributor)

A recent issue of *The Economist* contained a deep irony.

The newspaper's "Finance & Economics" section featured an article on the US economy. After expressing happy surprise that the US economy continues to grow despite headwinds, the article expressed two worries: first, that this growth would fuel further inflation (with no mention of the Fed's monetizing the full $4.2 trillion of bipartisan COVID deficit-spending spree, as *The Economist* continues to blame supply chains and pent-up demand), and second, that Treasury rates (now at a 16-year high) will place pressure on the economy.

On the very next page, the section turns to the latest Argentine crisis. Twenty years ago, Argentina had tackled the peso crisis of 2001, the hyperinflation of the late 1980s, and the frequent military coups that persisted into the early 1980s. One commentator glibly predicted in 2006 that the Argentine people would never again tolerate inflation above ten percent. That problem was solved for several years by federal interference in the Central Bank, and a delicious but inaccurate *asado* of fake statistics – to the point that *The Economist* simply stopped reporting unreliable numbers coming from Argentina's statistics office. Argentine inflation now stands at 138 percent (according to the latest official report). In a technicality that goes beyond the scope of this short piece, Argentina is now pushing the International Monetary Fund's lending model to a breaking point. After two decades of bailouts and borrowing, Argentina may yet again default.

Without irony, and without any indication of a parallel to the US situation, *The Economis*t reports that Argentina's "policymakers are torn between printing pesos to cover the government's bills and the need to avoid hyperinflation."

The difference is obviously one of degree, but certainly not of kind. Both the Argentine and the US economies are suffering the consequences of interventionism, as central bankers are placed in the simultaneously unenviable and coveted position of mopping up the mess from profligate politicians – even though they, themselves, clearly suffer from a Hayekian knowledge problem, and have contributed their fair share to the situation by printing money and causing boom and bust cycles in their attempts to "fix" the economy.

But wait… surely the US and Argentina cannot be compared! The US is the world's top economy. Despite the best efforts of politicians of both parties, the US manages to stay within the top 10 countries in the Economic Freedom of the World ranking. How can one compare the US to Argentina, which has suffered a century of political instability, and has been a darling of IMF case studies for the past 40 years?

Well, it wasn't always that way. In 1910, Argentina was among the top eight richest countries in the world. It had more miles of roads and railroads than most European countries. It had enjoyed 50 years of constitutional stability, after a rocky waltz of dictators and civil wars, from the country's independence in 1812 to unity under a classical liberal constitution in 1860. The Argentine constitution, mapped on the US Constitution, protected the rights of religion, free speech, commerce, and immigration, under a constitution of limited powers.

Alas, the constitution didn't stick. The US Constitution was drafted for a country with a deep tradition of rule of law, local governance, and a Lockean mindset. Rousseau was translated into Spanish before Locke, and his ideas arrived in Argentina first. The Argentine founders, for all their goodwill and vision, attempted to plant a translation of the US constitution into a soil that consisted of corruption, strong-man rule (caudillismo) and central planning, all atavisms of Spanish colonialism. For about 50 years, the constitution offered respite from the cycle of tyranny and instability; the country grew and economic freedom attracted immigrant labor. But by the second decade of the 20th century, Argentina was starting to turn. The military first ousted a civilian government in 1930; Argentina was to face five other military coups in the 20th century. Although the military putschists were traditionally anti-communist, Colonel Juan Domingo Perón established fascism in the Argentine style. That legacy remains today, not just with a political party that explicitly carries his mantle, but with widespread corporatism, dirigisme, and deficit-spending.

Argentina shows how a country can fall from splendor to misery in the span of two short decades. It is still recovering. Or will it ever recover?

Superficially, the problem is macroeconomic: Politicians spend money they don't have, and monetize the portions of the debt they can't borrow from the IMF. But, more deeply, the problem is institutional. Argentina lacks rule of law and constitutional constraints. The central bank (BCRA) lacks independence; only one president of the BCRA has served a full term without being removed by the executive (Ernesto Bosch, the first president of the BCRA, from 1935 to 1942. Ironically, his second term was cut short by none other than Juan Domingo Perón, who didn't have room in his agenda for an independent central bank).

Argentina is, once again, facing a crisis. In November, when its next payment is due, it might break the entire IMF system. Argentina's politicians are addicted to spending the money of taxpayers and foreign bondholders, while coddling favored groups. Alas, the IMF has acted as an enabler, as it continues to lend to a profligate and irresponsible Argentine political class.

The US may not be that far behind. Indeed, the US is barely recovering from inflation unseen in the past 50 years, an inflation that was created by the Federal Reserve monetization of COVID-era pork-barrel spending. US debt is at an all-time high of a 130 percent debt-to-GDP ratio. Regulations and job licensing are exploding, as is federal involvement in the economy. The US, with about half of the economy controlled, directly or indirectly, by governments at all levels, remains the world's cleanest dirty shirt. How long will that last?

Poor Argentina may well be the canary in the US coal mine, offering a textbook story of turning riches to rags through interventionist policies.

– October 28, 2023

Does a Blowout Third-Quarter GDP Number Vindicate Bidenomics?

PETER C. EARLE

Research Faculty

On October 26th, the first calculation of third-quarter US Gross Domestic Product will be released by the Bureau of Economic Analysis. The most recent Bloomberg forecasts show a substantial increase over the second quarter's 2.1 percent growth. The mean of current projections for tomorrow's third-quarter GDP release is 3.4 percent, with a median of 3.5 percent, drawn from 73 forecasts ranging from -0.03 percent to 5.4 percent. The Federal Reserve Bank of Atlanta's GDPNow estimate as of today is 5.4 percent. If realized, the Bloomberg mean estimate would represent a 62 percent jump over the second-quarter reading; the Atlanta Fed's number, a leap of 157 percent. If the third-quarter GDP number were to come in at 4.5 percent or higher, it would be the highest quarterly return since the late 2020 through 2021 recovery from pandemic policies. Barring that, a quarterly GDP result higher than 4 percent has not been seen since the third quarter of 2019.

More important than historical comparisons, though, would be answers to the following questions: Where in the components of GDP would such strength be coming from, especially considering that Fed rate hikes are beginning to exert a decelerating effect on the US economy? Is it a consequence of policy, or random economic interactions at the micro, meso, and macro levels? And does such a bounce in GDP portend a return to robust economic output, or a capricious, insignificant surge?

It is difficult to say in advance. But several factors behind the estimates for a strong third-quarter number are likely among the index's constituents. US consumers have continued to buoy the US economy, as evidenced by the strength of discretionary spending on the Barbie and Oppenheimer films, the Taylor Swift and Beyonce' tours, and vacations. Private inventories have also been rising as well, most recently owing to firms stocking up on supplies in anticipation of broadening labor unrest. The balance of US exports and imports will factor in, but other than a stronger dollar since July 2023 (which drags on US exports while increasing the marketability of imports), those numbers tend to be volatile from one quarter to the next and thus difficult to predict. And private nonresidential fixed investment (which alongside consumption was the other major contributor to the prior GDP release), is likely to play a significant role in tomorrow's number as taxpayer-provided subsidies from the Bipartisan Infrastructure Law, the Inflation Reduction Act, and the CHIPS and Science Act continue to flow.

If the bottom line third-quarter GDP number shakes out as the Fed's GDPNow and Bloomberg survey are hinting, and the elements listed above are the cause (consumption, private nonresidential fixed investment, private inventories, and perhaps some help from trade), it is probably not indicative of a renewal of strong economic growth. Other than the three federal spending laws (which are legislatively engineered to disburse government funds at regular intervals, providing an ongoing business spending boost to the US economy through the 2024 election cycle), the remainder of the factors are fickle. Consumers, still spending, have eaten through their pandemic savings, are borrowing at rates not seen in 40 years, and face both contracting credit and the return of student loan payments. The end of federal child care subsidies, and mortgage rates at quarter-century highs are adding to spending headwinds. American consumption has been impressive and somewhat mysterious of late, but cannot continue indefinitely. Accumulated private inventories will either be sold or drawn down once the latest wave of labor activism subsides. Government spending is likely nearly the same from the second to the third quarter and the impact of trade remains to be seen.

Behind all of these questions — if indeed a blowout third quarter US GDP number appears tomorrow morning — is a weightier issue: How will the Fed respond? A strong GDP number is likely to send Treasury bond yields up in anticipation of another rate hike, possibly dragging the 10-year note back above 5 percent. Whatever the specific sources within tomorrow's GDP, an overall increase by the estimated magnitude is likely to motivate the Fed to intensify its efforts, redoubling its contractionary policy bias.

US Treasury Yield Curve, 25 October 2023

[Source: Bloomberg Finance, LP]

Once more, it's important to note that this is an anticipatory scenario. But if the predicted increase in third-quarter GDP does materialize, and if it is on the order of 4 percent or more, anticipate a continuous promotion and celebration of the economic policies associated with the Biden administration. But aside from offering substantial taxpayer funding for unproven technologies and for ventures without market demand, fostering tensions nationwide between management and labor, raising regulations and taxes, and ramping up both US debt and deficits, the expected growth in GDP won't be attributable to the economic policies associated with the Biden administration.

One would do well to recall the heroically shameless efforts undertaken by the current administration to distance themselves from two quarters of contracting GDP in 2022. US citizens — consumers, savers, investors, and businesspeople — will, in the event of a strong GDP release on Thursday morning, benefit more from scrutinizing and taking note of any ensuing political self-aggrandizement than by absorbing or even ignoring it. Forthcoming GDP releases may require reminding administration officials of statements made tomorrow regarding the achievements, and prospects, of "Bidenomics."

– October 25, 2023

Curtailing Violence with Economic Freedom

ROBERT E. WRIGHT
Senior Research Faculty

Liberty lovers rightfully disdain violence, condoning it only when committed in self-defense, after violation of the non-aggression principle. The strategy finds empirical grounding in the success of employing tit-for-tat in a repeated game of Prisoners' Dilemma (you trade, I trade; you raid, I raid).

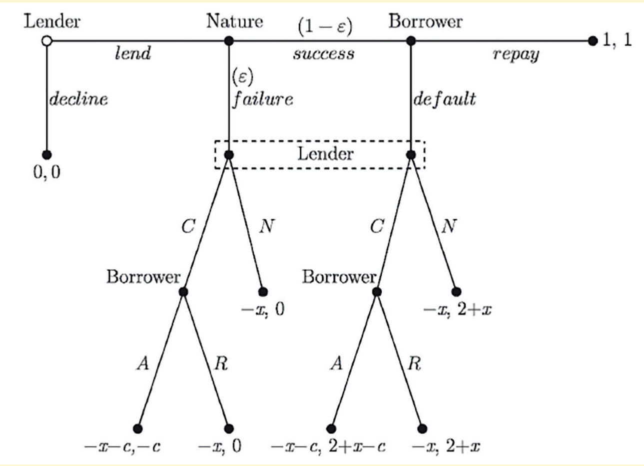
None of that, though, gets at why (too) many people engage in what appears to be senseless violence like mass shootings or terroristic attacks. It's a shame the matter cannot be investigated more fully empirically, because many of the most violent perpetrators die, and if they leave the world a manifesto, officials often censor it. Seemingly irrational behaviors, however, can be modeled well enough to produce insights for policymakers to ponder despite the dearth of empirical data. Models simplify complex phenomena to render their essence more understandable; Good models do not oversimplify.

In 2010, I teamed with Amherst College economist Christopher G. Kingston to publish a game theory model of dueling in the *Southern Economic Journal*. Although we developed the model with explicit reference to "pistols at ten paces" duels in antebellum America, it can be generalized to help people to think through the policies and conditions most likely to generate violence.

Most people intuit that violence becomes more likely when an individual or polity can plausibly calculate that the present value of the expected total benefits of violence exceeds the present value of the expected total costs of violence. People who have "nothing to live for," especially if they can be convinced that rewards await them in an afterlife, are more likely to turn to violent means than those who envision themselves sitting in hot tubs sipping on fine wine and gorging on surf and turf for the rest of their long lives.

So it is easy to imagine scenarios where somebody might voluntarily risk life and limb to protect hearth and home, or their livelihood. To the extent that their causes were documented, however, most antebellum American duels did not entail conflicts over tangible resources like land or the love of a woman. Many involved the intangible concept of creditworthiness, or "honor" as it was then often expressed.

Here is the extensive-form of our model:



The Credit Transaction with Potential for Dueling

In plain English, if the lender and borrower do not contract, there are no gains from trade (0, 0 payoff). If they do contract, the project succeeds, and the borrower is honorable/creditworthy, the loan is repaid and both parties benefit (1, 1). If the project fails or the borrower is dishonorable, then all heck breaks loose (all those variable payoffs, many negative or zero) because under certain conditions, like an underdeveloped credit market and unpredictable outcomes of the duel, it's rational to appear on the "field of honor" to re-establish creditworthiness, even at the risk of joining Alexander Hamilton and his son Philip in the list of those killed.

If we change Lender to leader (i.e., a government) and Borrower to individual (e.g., citizen or denizen), lend to lead (i.e., implement some set of policies), repay to pay (i.e., taxes, allegiance), the game would read in plain English: If the leader does not lead, the individual will not pay and the result is a failed state (0,0). If the leader leads, the policies interact with the real world (nature), where they may succeed or fail. If they succeed, and the individual is virtuous, both parties gain (1, 1). If the individual is not virtuous, though, he may not pay, potentially triggering a violent response on the part of the state.

If the policy fails its real-world test, violence may also erupt under certain conditions, like when the individual thinks the leader has deliberately failed her and that the leader can be defeated, killed, or replaced with sufficient probability at sufficiently low cost.

Ergo, any leader truly interested in minimizing violence, saving lives, and so forth, would only implement policies likely to succeed and likely to produce virtuous individuals. There is only one policy almost certain to succeed and to create virtuous individuals, or at least individuals who expect to be wealthy enough that they act virtuously because they do not wish to risk confrontation with the state. That policy, of course, is communism. Just kidding! It's the opposite of communism, something called economic freedom, or classical liberalism applied to policy matters. Note that the model also implies that leaders should assiduously avoid policies that create rents (unearned profits) because that creates non-virtuous individuals tempted to avoid taxes or service even at the risk of violece.

In short, allow individuals to build it and make clear that they cannot force others to build it for them, and they will build it. And, most likely, they will not want to blow it up.

– October 19, 2023

Abolish Parking Minimums. Yes, All of Them

JASON SORENS
Senior Research Faculty

It has been devilishly difficult to remove regulatory barriers to new housing, in spite of the growing support and activism of the Yes in My Back Yard (YIMBY) movement. Well-publicized bills in states like California often haven't done much. These bills haven't changed the major cost drivers for developers. As a result, California hasn't increased its rate of housing construction relative to the rest of the country even after starting to enact these laws, as law professor Chris Elmendorf pointed out recently on X.

What YIMBY needs is a good, clean win. Something that definitely reduces the cost of development without arousing large opposition or negative side-effects.

A good place to look is parking minimums. Parking minimums are one of the dumbest government regulations you've never heard of. State legislatures could easily abolish them all.

Parking minimums require landowners to include new, off-street parking spaces for anything they build. Apartments, retail shops, professional offices, industrial facilities – most towns' land-use regulations include detailed requirements about just how much new parking each type of development must include.

Why are parking minimums so stupid? To make the case for requiring parking, you'd need to show that parking has a positive externality: in other words, that the new parking provides significant net benefits to the community as a whole that the developer wouldn't otherwise consider.

But this is nonsense. A developer has every incentive to provide exactly the right amount of parking for the site's new use. If a developer doesn't provide enough parking for apartments, for example, then the development will have to charge lower rents. If a developer doesn't provide enough parking for a retail shop, it won't get enough customers and, once again, won't be able to pay the rent.

At best, therefore, parking minimums are irrelevant. They require parking spaces that a developer would build anyway. But in many cases, they require extra parking. Survey after survey shows that even peak usage of parking lots is well below capacity, often less than half of what the zoning code requires landowners to build.

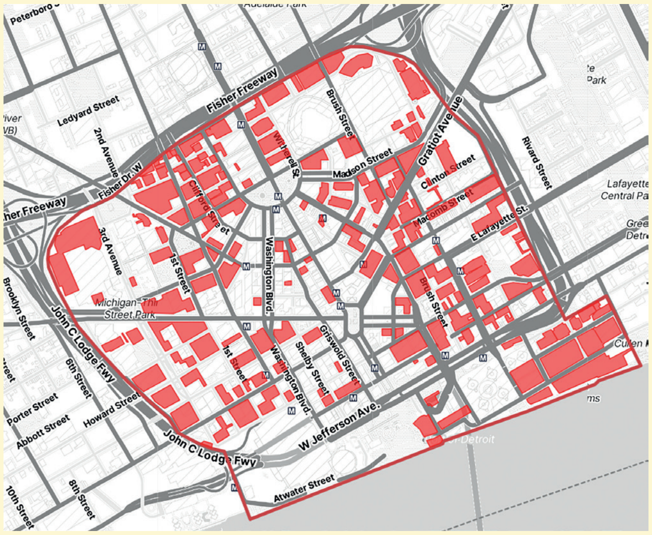
What are the costs of all that extra parking that the market doesn't want?

For starters, there are big environmental costs. Cutting down trees and paving over soil increases the risk of flash flooding in heavy rains. In northern climates, that extra pavement has to be plowed and salted in winter. Runoff from the pavement can seep into groundwater, contaminating wells. The extra disturbance from cutting into natural habitats and regrading soils helps invasive species colonize. Parking lots make driving more convenient and walking less convenient. Subsidizing the automobile leads to more air pollution.

Parking lots are ugly and unpleasant. They're baking hot in summer and windy in winter. They get in the way of attractive urban design that brings storefronts close to the street. And what happens if a business closes down? Large parking lots make redevelopment more costly and make a closed-down place seem even more blighted.

A Walmart parking lot in Amherst, NH

Parking lots don't pay a lot in property taxes. The land used for parking won't be assessed at a much higher rate than raw land, so developing a parking lot doesn't offset the property tax burden of other landowners in town nearly as much as developing buildings would. Certainly, a parking lot can add to the value of a nearby building, but then the landowner would want to build it anyway without any regulation. Reflecting on a study of the growth in parking at the expense of buildings and open space in Hartford, Connecticut, University of Connecticut professor Norman Garrick concluded, "The increase in parking was part of the collapse of the city."



30 percent of Detroit's central city is dedicated to parking, one of the highest percentages in the US. parkingreform.org.

Forcing landowners to build off-street parking reduces the potential revenue that towns could get from charging for on-street parking. On-street parking also makes streets slower and safer. Towns that rely on off-street parking are tempted to engineer their roads to highway standards, creating high-speed "stroads" that kill walkers and cyclists at high rates.

Parking lots can be costly. The cost of one parking space ranges from about $9,000 to about $80,000, depending on whether it's at ground level, above, or below. All those costs drive up rents for business and residential tenants.

Parking minimums are regressive, redistributing wealth away from the poor. After all, the poor are most likely to be willing to rent an apartment with only one parking space or none at all in exchange for lower rent. Forcing every apartment to have one, two, or even three spaces, as some towns do, drives up rents for everyone, but hurts the poor the most, because they spend a greater share of their income on housing than richer people do.

In his influential 2005 manifesto *The High Cost of Free Parking*, UCLA urban planning professor Donald Shoup pointed out that "planning for parking" in the absence of market prices is nothing more than a "pseudoscience." Zoning codes require parking based on rough estimates of demand for "free" parking at the time of development, ignoring how subsequent economic changes could affect demand and how demand for parking would change if users had to pay for the cost of providing the parking.

Professional planners have quickly caught on to the harm that parking minimums do, and several dozen towns and cities have abolished parking minimums completely in the last few years. And at the state level, Oregon now requires 61 cities to abolish parking minimums near high-frequency transit stops. A study of Seattle after its partial repeal of parking minimums showed that the move ended up saving over half a billion dollars in construction costs and 144 acres of land over five years.

There's no good argument for minimum parking requirements. States should simply amend the laws that allowed local zoning in the first place and specify that localities may not require parking. Abolishing all parking minimums might not solve the housing crisis on its own, but it's an easy and meaningful step in reversing a historic mistake.

– October 15, 2023

Critical Race Theory in Data: What the Statistics Show

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The concept of Critical Race Theory (CRT) has sparked heated debate in recent years, particularly after conservative activists singled out this school of thought as a hotbed of applied Marxism in both higher and K-12 education. The response from CRT's defenders has been peculiar, to put it mildly.

Just over a decade ago, leading CRT scholars Richard Delgado and Jean Stefancic boasted about how this school of thought had moved beyond its law school origins and "taken root in other academic disciplines, including sociology, social work, and education." According to Delgado, "We didn't set out to colonize, but found a natural affinity in education" schools and programs. "Seeing critical race theory take off in education has been a source of great satisfaction for the two of us," he continues, noting, "Critical race theory is in some ways livelier in education right now than it is in law..."

This celebratory account of CRT's growing influence contrasts sharply with the flurry of media depictions in recent years, almost all of which attribute a "moral panic" over CRT to a September 2020 episode of Tucker Carlson's program on Fox News. According to the New Yorker, conservatives "invented the conflict over Critical Race Theory." MSNBC host Joy Reid repeatedly claimed that CRT was just an obscure theory from advanced seminars in legal academia, insisting that the political right had "manufactured" a controversy by falsely claiming that its doctrines had migrated into the broader education system. NPR singled out the date of the Carlson broadcast and its guest Chris Rufo of the Manhattan Institute as the "origin" point of the CRT debate, as did *The Atlantic*, *Time Magazine*, and several other outlets. From mid-2021 to the present, the main defenders of CRT have advanced similar claims, suggesting it was just an obscure and largely innocuous academic theory until the political right made it into an issue by falsely alleging its expansion into teacher training in the very same education programs that Delgado and Stefancic bragged about.

The tension between these two competing claims is obvious. If CRT's academic presence was indeed growing rapidly in education programs over the last decade, then Carlson was responding – albeit bombastically – to a real and observable trend that predates September 2020. If, on the other hand, Reid and other media defenders of CRT are correct, then we should see little evidence of CRT's permeation beyond advanced law school seminars until the right made it into a "bogeyman" on the Fox News broadcast, to quote their characterization.

Understanding CRT

So what exactly is CRT? The concept itself is notoriously fluid, with even its proponents struggling to offer a coherent and simple definition. Briefly summarized, though, CRT is an applied extension of critical theory to race. This much is openly acknowledged by Kimberle W. Crenshaw, who first proposed the name CRT at an academic workshop in the 1980s. As Crenshaw recounts, "the organizers coined the term 'Critical Race Theory' to make it clear that our work locates itself in the intersection of critical theory and race, racism, and the law."

Critical theory, in turn, refers to a broader school of thought emerging from Marxist theorists Max Horkheimer, Herbert Marcuse, and Theodor Adorno in the 1920s and '30s. Positioning themselves as a breakaway branch of Marxist thought from its Leninist-Revolutionary doctrines in the Soviet Union, these early critical theorists styled themselves in opposition to what Horkheimer called "traditional theory" – i.e. that which purports to explain the world through conventional scientific and descriptive methods but which, in the eyes of critical theorists, really exists to reinforce the power relationships of a ruling class over the masses. The critical theorist, by implication, aims not to describe but to disrupt and overturn these alleged power disparities. The entire epistemic framework is accordingly a call to radical "activism" in the form of doing scholarship, pedagogy, and commentary about almost any aspect of society.

This basic framework, in turn, may be seen in the self-descriptions used by CRT practitioners, albeit with a specific focus on race. Delgado and Stefancic accordingly define the CRT movement as "a collection of activists and scholars engaged in studying and transforming the relationship among race, racism, and power." They situate CRT as having a shared interest with conventional civil rights issues surrounding race. The commonalities end there though. "Unlike traditional civil rights discourse," they continue "which stresses incrementalism and step-by-step progress, critical race theory questions the very foundations of the liberal order, including equality theory, legal reasoning, Enlightenment rationalism, and neutral principles of constitutional law."

Crenshaw describes the founders of CRT as a "collection of neo-Marxist intellectuals, former New Left activists, ex-counter-culturalists, and other varieties of oppositionists in law schools" who set out to disrupt the liberal legalist tradition of viewing law as a neutral arbiter of rules. Exemplifying the critical vs. traditional theory dichotomy, Crenshaw charges the traditional liberal-enlightenment view of law with having an "ambivalence toward race-consciousness," symptomized in its "continued investment in meritocratic ideology." While she views these issues as being most pronounced in areas of race, Crenshaw makes it absolutely clear that a radical economic program undergirds her position. She accordingly lists the "lukewarm liberal defense of the Great Society programs" and the failure to adopt radical economic redistribution as further failures of more traditional paradigms.

In her more recent work, Crenshaw has extended this critical theory attack to the entirety of conventional non-Marxian economics. She contends "the emergence of economics as a discipline from its previous locus inside moral philosophy suppressed the study of socially constructed institutions" and, citing discredited work by far-left academics like Nancy MacLean, asserts that "the core logic of an entire academic subfield," public choice, is "implicitly constituted around assumptions of white supremacy, even as it disavowed any racial intent and animus." Such stark language establishes not only the hostility of CRT to economics as a science. It shows that CRT, at its heart, is an anti-capitalist ideology.

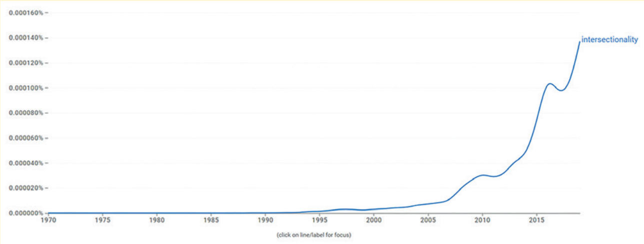
Measuring the Critical Theory Turn

The question of CRT's emergence as a point of contention in national debate could be reframed as a matter of whether the September 2020 coverage sparked the current controversy by pushing an obscure specialized theory into the limelight, as CRT's media defenders contend, or whether this show was simply responding to an already-emerging and rapidly expanding academic movement, as Delgado and Stefancic's earlier comments suggested.

Google's Ngram viewer helps to shed some light on this question, by tracking the use of CRT terminology over time. One of the central concepts of CRT is "intersectionality," a term first proposed by Crenshaw in 1989 and expanded upon in a

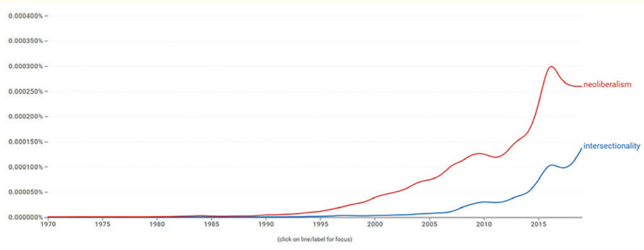
1991 article that is considered one of the defining works of the CRT genre. Intersectionality serves as a mental model for social interactions when a person is a member of multiple overlapping groups and identities (race, gender, ethnicity, religion, and the like), illustrating differences in experience compared to each characteristic in isolation (for a detailed discussion of intersectionality theory and the problems with it, see this article that I wrote in May 2020).

As both a proprietary term to have originated in the CRT movement, and one of its best-known concepts, the term "intersectionality" presents an almost ideal metric to track CRT's influence over time. We see the results in the figure below.

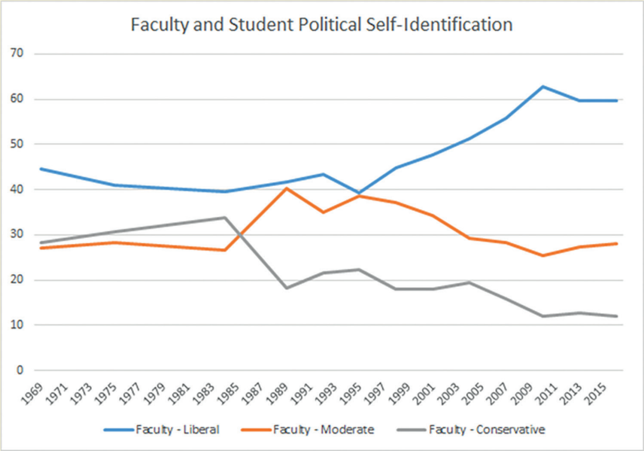


The term had only a small and limited adoption for the first decade and a half after its introduction by Crenshaw. Then, starting around 2006, it began to rapidly increase in use. The pattern accelerated further around 2013-2014, the period that even left-leaning commentators have dubbed the "Great Awokening" to signify an emerging radicalization in leftist viewpoints on campus. Intersectionality skyrocketed from 2014 to 2019, the most recent year in the Ngram database.

For perspective on the scale of this adoption, the chart below compares intersectionality with another proprietary academic term, the much-derided concept of "neoliberalism." The popularization of "neoliberalism" as a label predates Crenshaw's "intersectionality" by about a decade, with its modern discussion tracing to a series of lectures given by the French philosopher Michel Foucault in the late 1970s. It's therefore entirely expected that intersectionality, which wasn't coined until 1989, would lag behind neoliberalism. The trajectories of both are nonetheless revelatory. Between 2005 and 2019, "intersectionality" gained over half the ground between it and "neoliberalism," one of the trendiest academic buzzwords in existence.

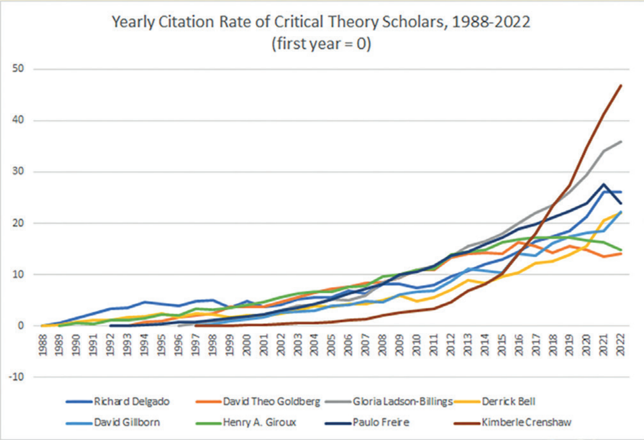


It is likely not coincidental that the "Great Awokening" and the popularization of intersectionality directly coincided with a historic leftward shift in university faculty affiliation. Survey data of US faculty political opinions have existed since the 1960s, having been originally collected by the Carnegie Commission on Higher Education, and later by the UCLA Higher Education Research Institute (1989-present). While left-leaning faculty were always a plurality on campus, their numbers rapidly increased between the early 2000s and the present. Currently, some 60 percent of faculty identify on the political left. In many humanities and social sciences, this number tops 80 percent.



Notably, these shifts in faculty politics have accompanied an increasing prioritization of political activism in the university system. In 2008, and again in 2016, the UCLA survey asked faculty participants if they believed it was their role to "encourage students to become agents of social change." In only 8 years, the percentage of respondents who said "yes" grew from 57.8 percent to 80.6 percent. While this indicator only captures a slice of classroom instruction, it is consistent with the expanding influence of critical theory, and particularly its "critical pedagogy" outgrowth, which strongly emphasizes using classroom instruction to cultivate political activists.

A third datapoint gives us a direct glimpse at how the CRT movement has rapidly expanded in its academic influence. While CRT may have been a niche subject as recently as the 1990s, academic journal citations of CRT scholars exploded around the time of the "Great Awokening," as well. The chart below shows the annual Google Scholar citation counts of several prominent CRT scholars (as well as critical pedagogy theorists Paulo Freire and Henry Giroux), indexed to a common starting point for scale. A marked upturn in citations begins in the late 2000s and accelerates in the mid 2010s. At present, Delgado regularly amasses over 3,000 citations per year. Fellow CRT scholar Derek Bell tops 6,000 citations per year. And Crenshaw leads the pack, with 16,000 citations, making her one of the most frequently referenced scholars today in the humanities and social sciences.



In each of these empirical indicators, the surge of academic interest in left-leaning politics generally, and CRT in particular, happened around the same time, starting in the mid-2000s and rapidly accelerating in the mid-2010s. All of these patterns were well underway before the September 2020 Fox News broadcast on CRT. That broadcast certainly drew attention to CRT and polemicized its coverage. But far from being an "obscure legal theory," CRT had already spread widely in academia going back a decade prior. It remains in a position of extremely high influence today, albeit with greater external scrutiny than it has ever faced. And that scrutiny has induced defensive revisions of its own academic history by CRT proponents.

– October 17, 2023

Inflation Remains High in September

WILLIAM J. LUTHER

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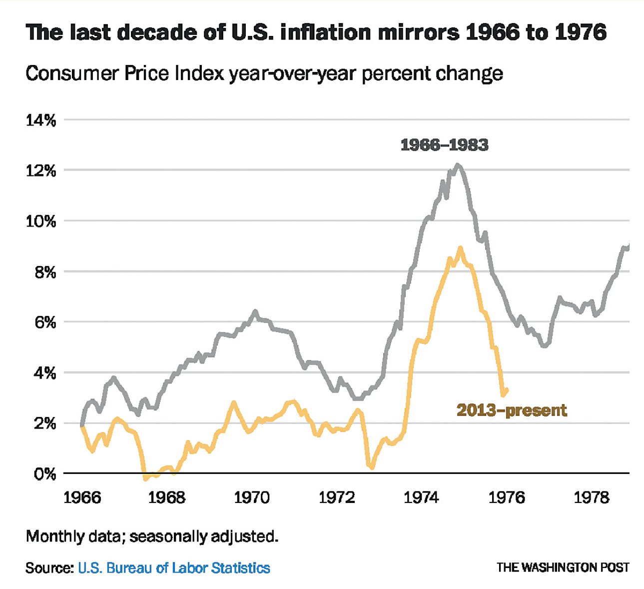
The disinflation process has not been as consistent as one may have hoped, new data from the Bureau of Economic Analysis show. The Personal Consumption Expenditures Price Index (PCEPI), which is the Federal Reserve's preferred measure of inflation, grew at a continuously compounding annual rate of 3.4 percent over the twelve-month period ending in September 2023—down from 6.4 percent over the twelve-month period ending in September 2022. That's the good news. But there's also bad news.

Although inflation has declined over the last year, it has rebounded in recent months. Over the three-month period ending September 2023, prices grew at an annualized rate of 3.7 percent, compared with 2.3 percent over the three-month period ending June 2023. The uptick is especially pronounced in the last two months. In August 2023, reduced energy supplies caused prices to grow at an annualized rate of 4.4 percent, up from 2.5 percent in the prior month. In September, prices grew at an annualized rate of 4.3 percent.

There are two distinct reasons to be concerned about the recent rise in inflation. First, one might worry about an inflation resurgence, with prices growing as fast as they did in late 2021 and 2022—or, at least faster than they were growing just a few months ago.

Some point to the two waves of inflation experienced in the 1970s. "It is sobering to recall," former Treasury Secretary Lawrence Summers wrote in August, "that the shape of the past decade's inflation curve almost perfectly shadows its path from 1966 to 1976 before it accelerated in the late 1970s."



One should be very skeptical when presented with a supposed pattern in macroeconomic data. There is no reason to think prices will inevitably evolve today as they did then. At most, the prior episode indicates that it *can* happen. If one believes that it *will* happen, one should identify the causal factors.

Perhaps the best argument that inflation will rise again relates to fiscal policy. Short-term interest rates are higher than they have been at any point in the last twenty years. Consequently, the federal government's interest expense has exploded. To deal with the additional expense, the government must (1) increase revenues, (2) reduce expenditures, or (3) issue more debt. There seems to be little appetite in DC for raising taxes or cutting spending. The most likely outcome is that the government will issue more debt.

Additional government borrowing would put upward pressure on the natural rate of interest. To prevent inflation, the Fed would need to offset the fiscal expansion by raising its interest rate target. Otherwise, the spread between the natural rate and the Fed's target will shrink, passively loosening monetary policy. Hence, inflation could rise again if the Fed fails to offset expansionary fiscal policy.

Another reason to be concerned about the recent rise in inflation is that it increases the odds that the Fed will overtighten.

The (nominal) federal funds rate target range is currently set at 5.25 to 5.5 percent. With core PCEPI inflation at 3.6 percent in September, the real federal funds rate target is probably somewhere between 1.65 and 1.9 percent. For comparison, the New York Fed currently estimates the natural rate of interest at 0.57 to 1.14 percent. Monetary policy appears to be sufficiently tight.

Nonetheless, at the September meeting of the Federal Open Market Committee, twelve members projected an additional rate hike in 2023. If anything, the inflation data released in September and October makes additional rate hikes *more* likely.

The Fed should keep monetary policy tight as inflation returns to its 2-percent target. But if it tightens too much, it will push the economy into an unnecessary and painful recession.

As I have written before, it is difficult to determine what the Fed should do when it hasn't done what it should have done. It would have been better had it avoided this situation altogether. Obviously, it is too late for that now. We are where we are. One can only hope that the Fed will navigate this narrow pass safely this time—and steer clear of such dangers in the future.

– November 3, 2023

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