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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

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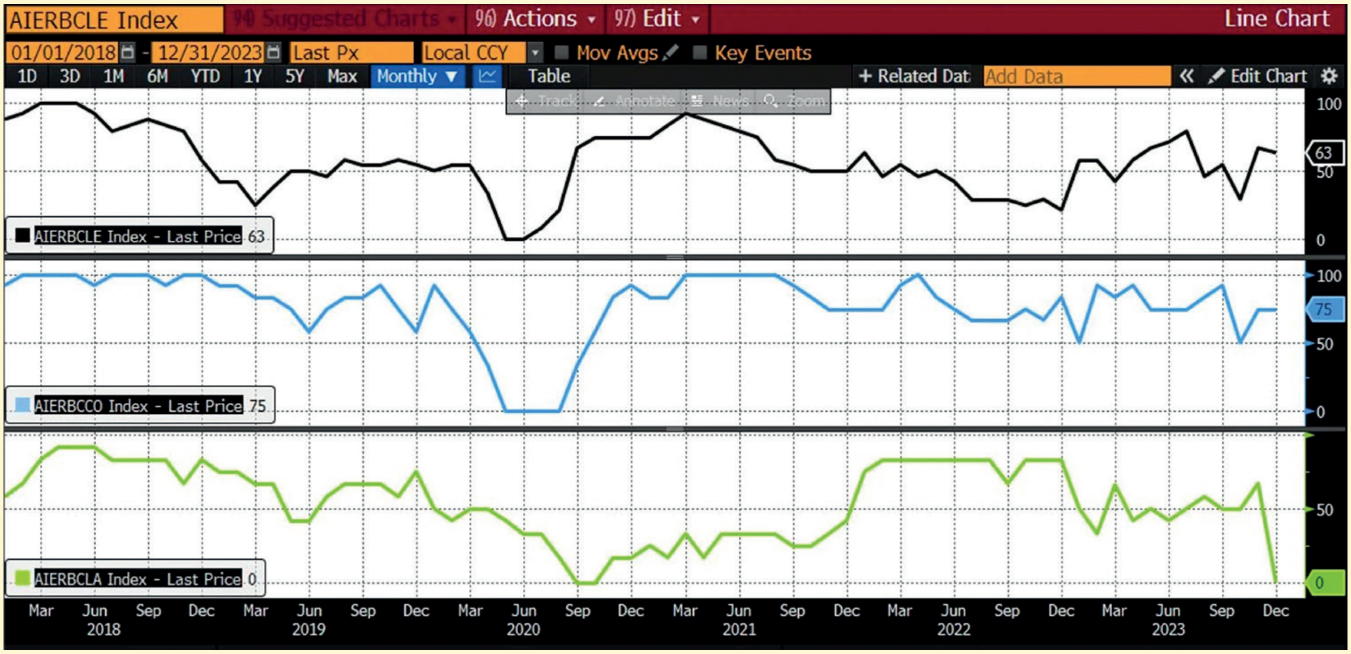
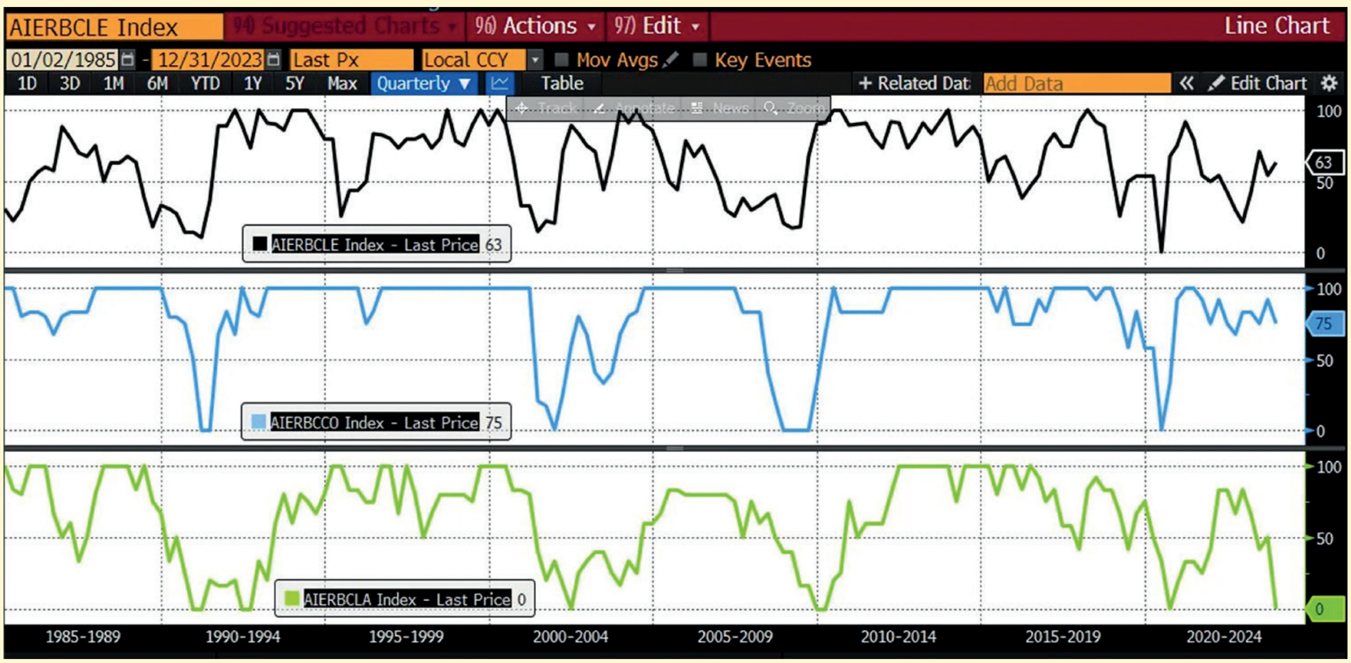
BUSINESS CONDITIONS MONTHLY

Peter C. Earle
SENIOR RESEARCH FELLOW

In December 2023, the AIER Business Conditions Monthly indices again emphasized the unpredictable nature of economic data in the post-COVID-19 period. The Leading Indicator fell slightly from November 2023's 67 to 63, while the Roughly Coincident Indicator remained at 75 from the previous month. The Lagging Indicator, however, plummeted to zero for the first time since late 2020.



(Source: Bloomberg Finance, LP)



(Source: Bloomberg Finance, LP)

Leading Indicators (63)

From November 2023 to December 2023, seven of the twelve leading indicators rose, four declined, and one was neutral.

Rising were University of Michigan Consumer Expectations Index (18.7 percent), FINRA's Debt Balances in Customers' Securities Margin Accounts (6.0 percent), US Initial Jobless Claims (5.6 percent), Conference Board US Leading Index Stock Prices 500 Common Stocks (5.0 percent), Adjusted Retail and Food Services Sales Total (0.6 percent), Conference Board US Leading Index Manufacturing New Orders Consumer Goods and Materials (0.1 percent), Conference Board US Manufacturers New Orders Nondefense Capital Good Ex Aircraft (0.1 percent). The Inventory/Sales Ratio: Total Business was unchanged from November to December. The US Average Weekly Hours All Employees Manufacturing (-0.3 percent), US New Privately Owned Housing Units Started by Structure Total (-4.3 percent), United States Heavy Trucks Sales (-4.6 percent), and 1-to-10 year US Treasury spread (-11.7 percent) declined.

Roughly Coincident (75) and Lagging Indicators (0)

Within the Roughly Coincident Indicator, four constituents rose, one declined, and one was neutral. From November to December the three Conference Board metrics, Consumer Confidence Present Situation (7.8 percent), Personal Income Less Transfer Payments (0.2 percent), and Coincident Manufacturing and Trade Sales (0.2 percent), as well as US Employees on Nonfarm Payrolls Total (0.2 percent), expanded. US Industrial Production was unchanged and the US Labor Force Participation Rate fell by 0.5 percent.

All six of the lagging indicators declined for the first time since November 2020 between November and December 2023. The ISM Manufacturing Report on Business Inventories (-0.1 percent), Census Bureau US Private Constructions Spending Nonresidential (-0.2 percent), US Commercial Paper Placed Top 30 Day Yield (-0.9 percent), Conference Board US Lagging Commercial and Industrial Loans (-0.9 percent), US CPI Urban Consumers Less Food and Energy Year over Year (-2.5 percent), and the Conference Board US Lagging Average Duration of Unemployment (-14.4 percent) contracted in the last month of the year.

The unprecedented volatility observed in the three Business Conditions Monthly indicators over recent months exemplifies the distortions prevalent in economic data broadly in the post-pandemic era. The sharp swings witnessed from one month to the next highlight the challenges in accurately capturing and assessing the underlying trends and dynamics of the current US economy. While such fluctuations raise reasonable concerns about the reliability of economic data, it is essential to recognize that they are occurring within a unique context shaped by policy responses to the pandemic and their subsequent effects upon consumer behavior, manufacturing, trade, business investment, and beyond.

The economic scenario depicted in the December 2024 Business Conditions Monthly is, once again, one of contradictory indications. A somewhat strong leading indicator suggests future economic growth, indicating potential improvement or expansion in the near future, driven by factors like rising consumption, consumer confidence, and manufacturing orders. The strong coincident indicator portrays current economic conditions as robust and stable, suggesting that, despite recent slowdowns in certain areas, the US economy is generally performing well. All of this is at odds with the plummeting lagging indicator, which suggests recent contraction owing to rising unemployment durations, falling inventories, declining private nonresidential construction, and other signs of weakness.

It may be premature to formally reevaluate the relationship within the Business Conditions Monthly indicators and macroeconomic aggregates. Over time, however, it may become necessary to reassess our analytical frameworks and methodologies in order to ensure the accuracy and relevance of the economic data used in capturing the progress of the US economy.

Discussion

Consumer spending, a stalwart contributor to economic expansion, exhibited a mixed trajectory in the fourth quarter, with growth in goods consumption moderating while spending on services accelerated. Mounting signs of labor-market softening, however, characterized by larger applicant pools and easing wage pressures, cast doubt on the sustainability of consumer spending trends. Business investment, particularly in equipment, remained lackluster, which suggests subdued corporate confidence in future growth prospects. The interplay of trade dynamics and inventory fluctuations add further complexity to the economic narrative, with the trajectory of trade services and the unpredictability of inventory adjustments posing additional forecasting challenges.

The economic landscape in early 2024 is similarly characterized by a mixture of positive and concerning indicators. On one hand, consumer confidence rose in January, reflecting optimism fueled by expectations for lower inflation and interest rate cuts. The Conference Board's consumer confidence index improved, driven by improving perspectives on current economic conditions and labor markets. There was, however, a notable drop in buying plans for homes, cars, and major appliances, indicating a hesitancy among consumers to spend following the holiday season. Additionally, recent hot inflation prints have tempered the improvement in sentiment, with rising inflation expectations potentially overshadowing positive economic news.

Retail sales in January experienced a larger-than-expected decline, signaling a pullback in consumer spending after a strong round of holiday shopping in December. While technical factors and adverse weather conditions may have contributed to the weakness, the overall trend suggests a less-vigorous start to the year for consumers. Despite this, strong fundamentals, such as the solid January jobs report, have provided some support to investor sentiment. But downward revisions to sales figures for December and November indicate that consumer spending might not have been as robust as previously reported, leading to a more cautious outlook for economic growth in the first quarter.

The January jobs report revealed surprisingly robust job gains, significantly lowering the likelihood of a Fed rate cut in March. Revised benchmark data showed that the labor market was weaker than previously thought from late 2022 through early 2023, but ran hotter than realized in the second half of 2023. Nonfarm payrolls increased by 353,000 in January, higher than expectations, with a net upward revision of 126,000 for December and January combined. While average hourly earnings increased and the U-3 unemployment rate held steady in the 3.7 percent range, average weekly hours worked declined, tempering the overall positive picture.

Favorable news on the job market continued in early February 2024, boosting consumer sentiment in turn and reflecting the positive impact of January's blockbuster payroll gains. Concerns about escalating inflation, however, particularly in light of recent price increases for gas and other goods, could dampen the improvement in sentiment. Inflation expectations have edged higher, raising concerns about the erosion of purchasing power and living standards. As inflation remains a key issue, particularly in the lead-up to the November presidential elections, policymakers and market participants will closely monitor future economic data releases to gauge the trajectory of inflation and its implications for the broader economy.

The labor market picture is cloudier than generally recognized at present. Three factors cast some doubt on the remarkably strong labor market data of late.

First, abnormally low survey response rates in 2023 and January 2024 raise questions about the reliability of the data. Second, there are reasons for questioning the accuracy of the birth-death model and the potential undercounting of business closures therein. Revisions to the Bureau of Labor Statistics' Business Birth-Death Model contributed significantly to non-seasonally adjusted payroll figures, with higher contributions from May to November. Updated population controls have additionally decreased the estimated size of the civilian noninstitutional population, affecting the reported labor force size. Third, the decline in average weekly hours worked, particularly in cyclical industries, offset higher wages. That leads to a constant level of weekly earnings from December to January, but adjusting for the decline in hours worked payrolls, would have declined by the equivalent of 485,000 full-time jobs in January 2024. So concerns about data reliability and potential economic implications remain, heightening uncertainty surrounding future Fed policy decisions.

Global economic headwinds, including the outbreak of recessions in the United Kingdom and Japan alongside notable economic slowdowns in both China and Germany, cast an additional shadow over the outlook. The predictive power of consumer sentiment has degraded over time, and rising inflation, credit card delinquencies, and a larger-than-expected drop in retail sales suggest underlying weaknesses.

In the aftermath of the first run of the fourth-quarter 2023 GDP report, which surpassed expectations, an air of cautious optimism has pervaded economic discourse in the media. Despite that outcome, concerns persist regarding potential downward revisions to GDP figures in light of tepid survey data, an aspect increasingly acknowledged by officials. The GDP growth of 3.3 percent for the fourth quarter, outperforming estimates and led primarily by robust consumer spending, underscores a semblance of resilience in the economy, albeit shadowed by apprehensions stemming from sluggish business investment and uncertain trade dynamics.

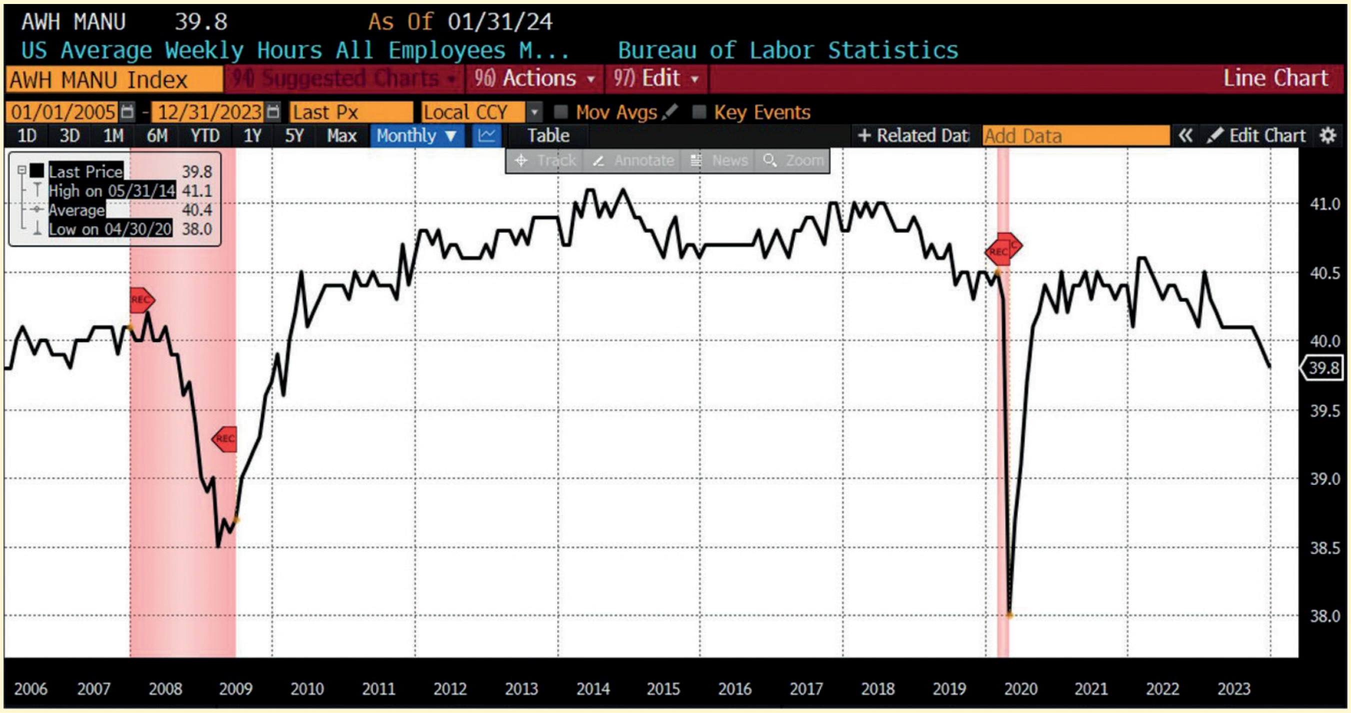
Readings from regional Fed surveys, meanwhile, suggest that GDP prints may eventually be revised downward. Despite the positive GDP figure, which is not heavily weighted by the Federal Reserve or the National Bureau of Economic Research, it remains possible that a recession is currently underway.

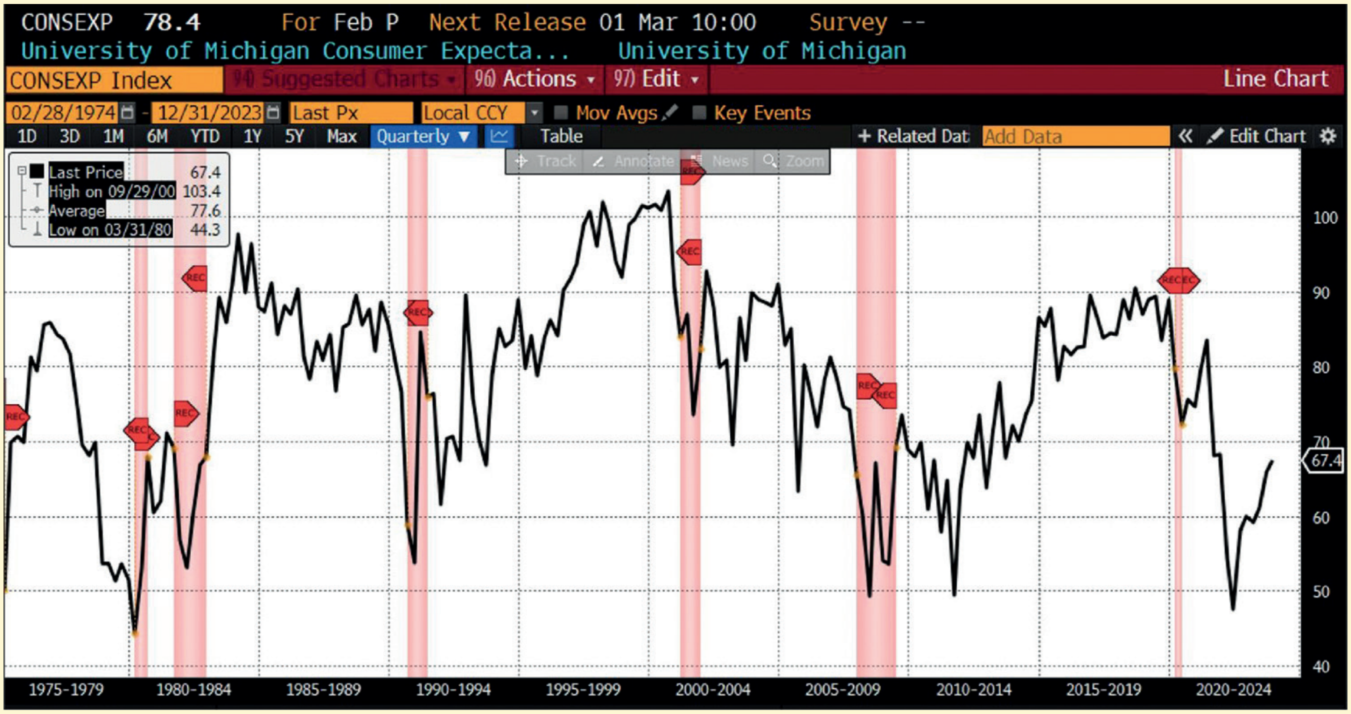
The NBER places relatively low weight on GDP in determining past business cycles, considering a range of indicators and focusing on monthly chronology. Contrary to popular belief, a recession doesn't necessarily require two consecutive quarters of GDP contraction, with equal weight placed on Gross Domestic Income (GDI), which contracted in the year through 3Q23. The NBER emphasizes economy-wide measures of economic activity, giving relatively little weight to real GDP due to its quarterly measurement and susceptibility to revisions. Each economic downturn is unique, with some marked by significant GDP contractions and others not, such as the mild recession in 2001.

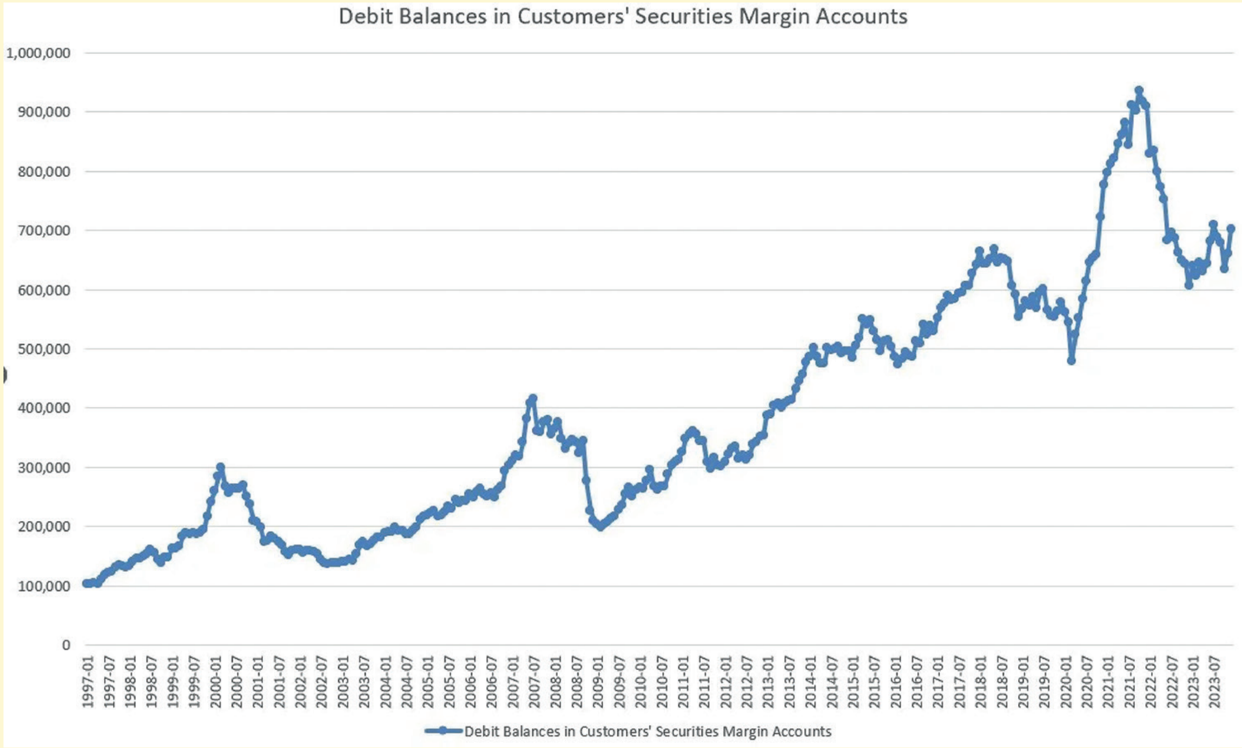
Historically, initial prints of real GDP were often revised down later, suggesting potential downward revisions to recent GDP prints, despite recent strength in hard data. Soft data indicate room for caution, emphasizing the need to consider both hard and soft data together. While GDP growth in 4Q suggests resilience, a holistic view suggests caution and the possibility of a mild recession similar to that seen in 2001.

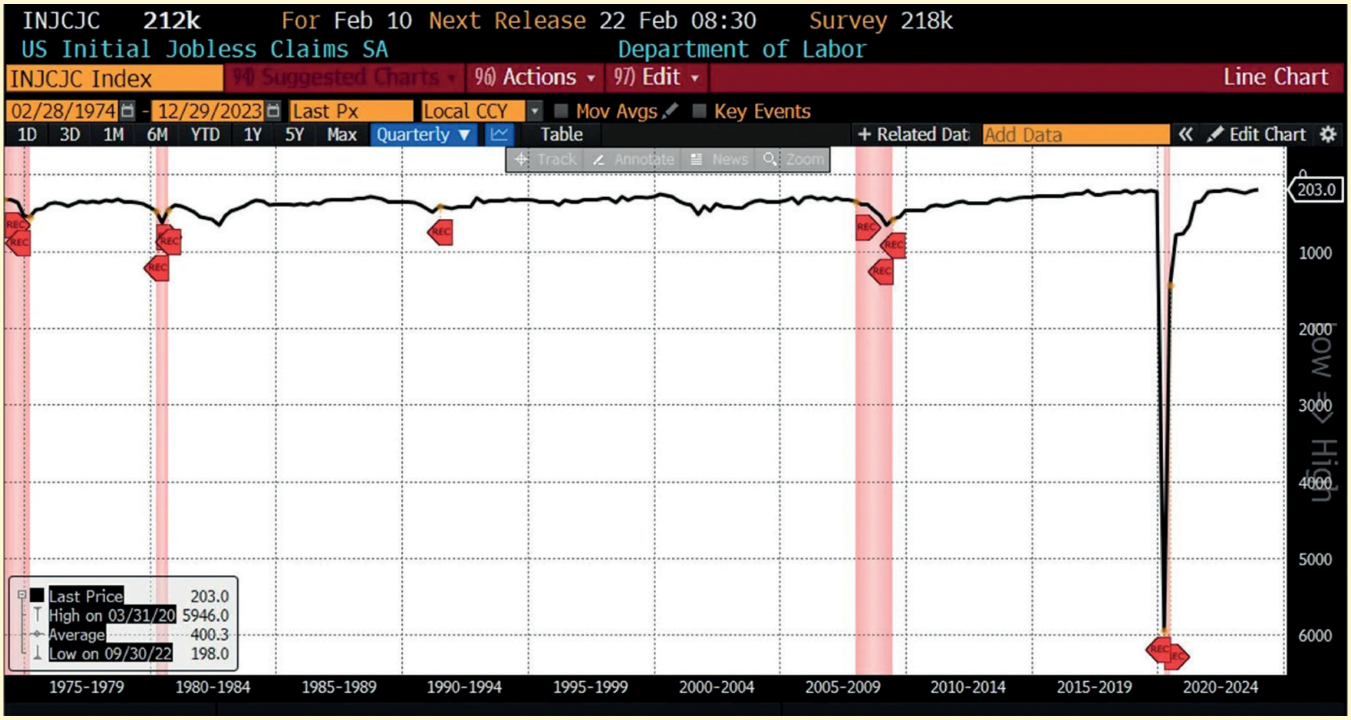
The anticipated Fed rate cuts, if realized, are likely to occur much later in the year due to nagging inflationary pressures and glimpses of economic resilience that the Federal Reserve cannot disregard. Amidst the prevailing economic landscape, characterized by a confluence of divergent signals across various indicators, prudence dictates our vigilant and objective monitoring of forthcoming policy deliberations and statistical releases. Given the intricacies inherent in recent (and perhaps distorted) assessments of the US labor market, consumer sentiment, and analogous datasets ostensibly portraying favorable contours, all of which juxtaposed against the contemporaneous downturns afflicting several major global economies, a forecast of economic contraction continues to pervade our outlook for 2024.

LEADING INDICATORS






Debit Balances in Customers' Securities Margin Accounts
1,000,000
900,000
800,000
700,000
600,000
500,000
400,000
300,000
200,000
100,000
0
Debit Balances in Customers' Securities Margin Accounts


INJCJC 212k For Feb 10 Next Release 22 Feb 08:30 Survey 218k
US Initial Jobless Claims SA Department of Labor
INJCJC Index
96) Actions
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Line Chart
02/28/1974 - 12/29/2023
Last Px
Local CCY
Mov Avgs
Key Events
1D 3D 1M 6M YTD 1Y 5Y Max Quarterly
Table
+ Related Dat
Add Data
Edit Chart
203.0
1000
2000
3000
4000
5000
6000
Last Price 203.0
High on 03/31/20 5946.0
Average 400.3
Low on 09/30/22 198.0
1975-1979
1980-1984
1985-1989
1990-1994
1995-1999
2000-2004
2005-2009
2010-2014
2015-2019
2020-2024


LEI MNO 34628.00 As Of 12/31/23
Conference Board US Manufacturers New O... Conference Board
LEI MNO Equity
96) Actions
97) Edit
Line Chart
02/28/1974 - 12/31/2023
Last Px
Local CCY
Mov Avgs
Key Events
1D 3D 1M 6M YTD 1Y 5Y Max Quarterly
Table
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High on 06/30/00 49202.00
Average 34176.89
Low on 12/31/75 20091.00
50000
45000
40000
34628.00
30000
25000
20000
1975-1979
1980-1984
1985-1989
1990-1994
1995-1999
2000-2004
2005-2009
2010-2014
2015-2019
2020-2024


LEI NWCN 124886.00 As Of 12/31/23 MILLIONS
Conference Board US Leading Index Manuf... Conference Board
LEI NWCN Index
96) Actions
97) Edit
Line Chart
02/28/1974 - 12/31/2023
Last Px
Local CCY
Mov Avgs
Key Events
1D 3D 1M 6M YTD 1Y 5Y Max Quarterly
Table
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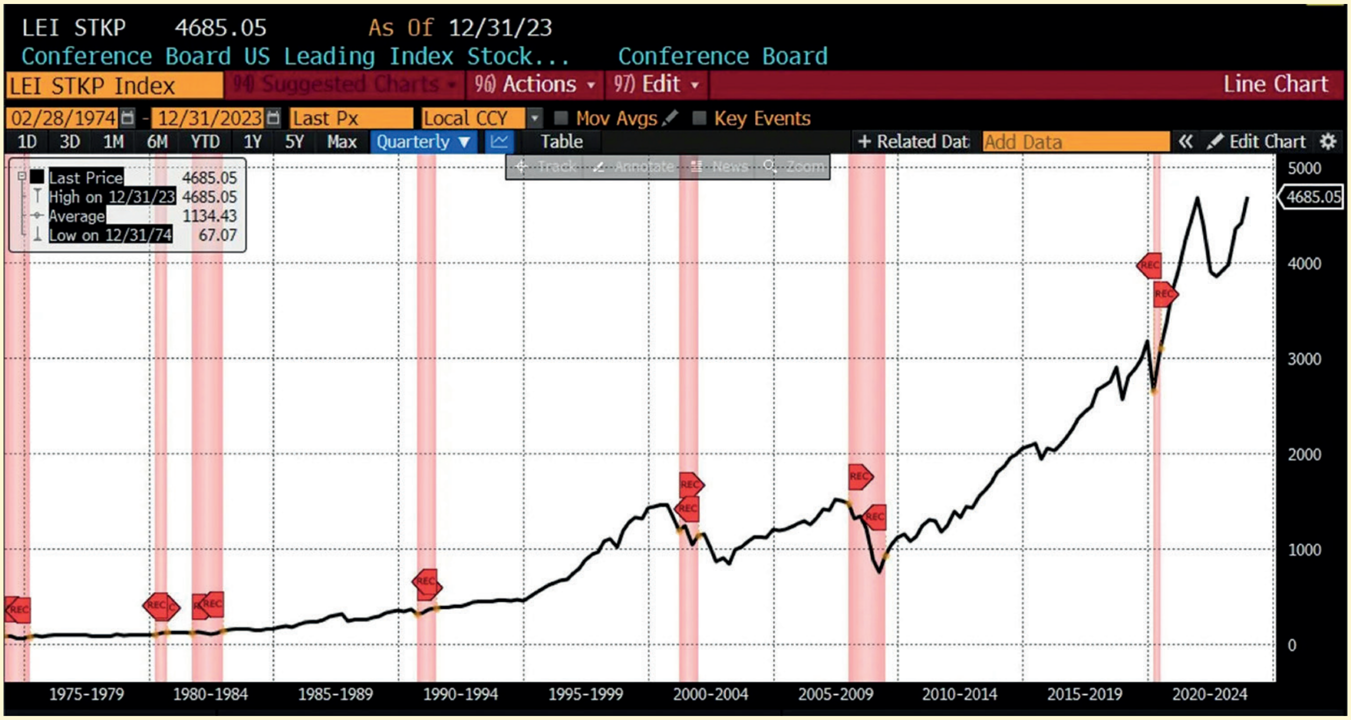
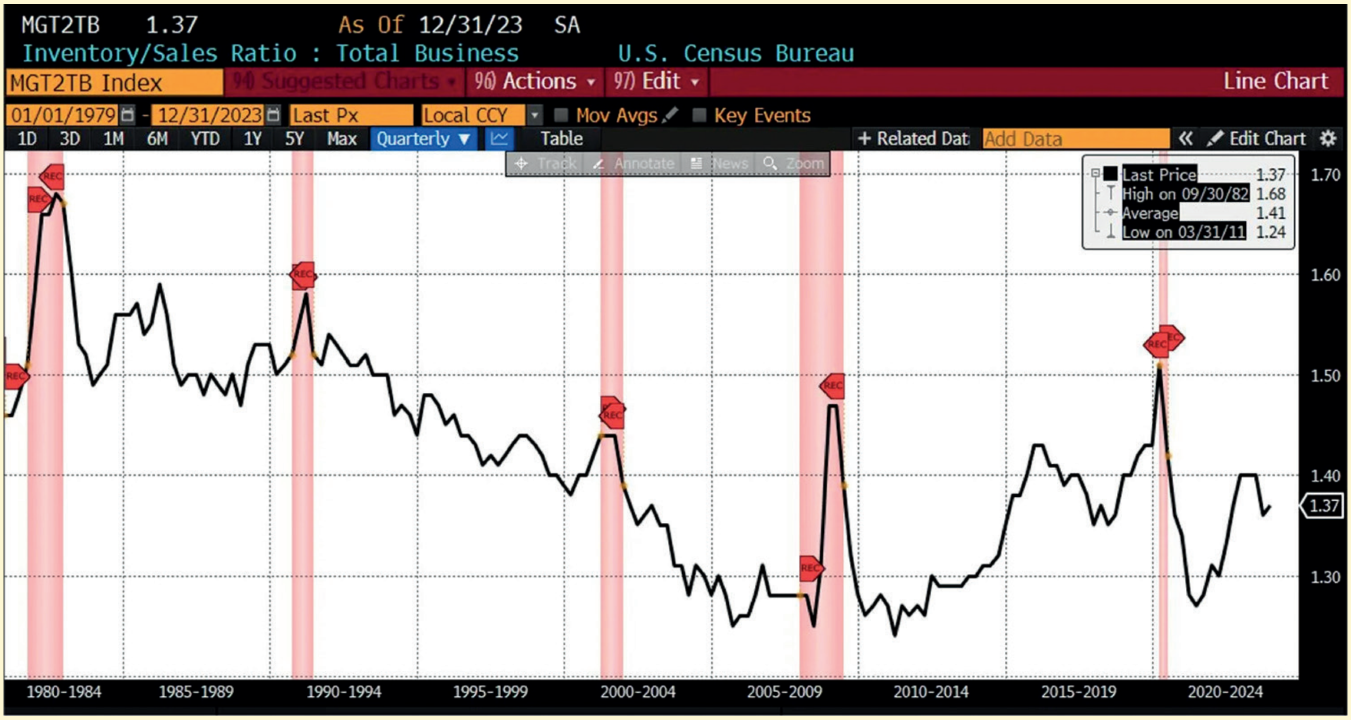
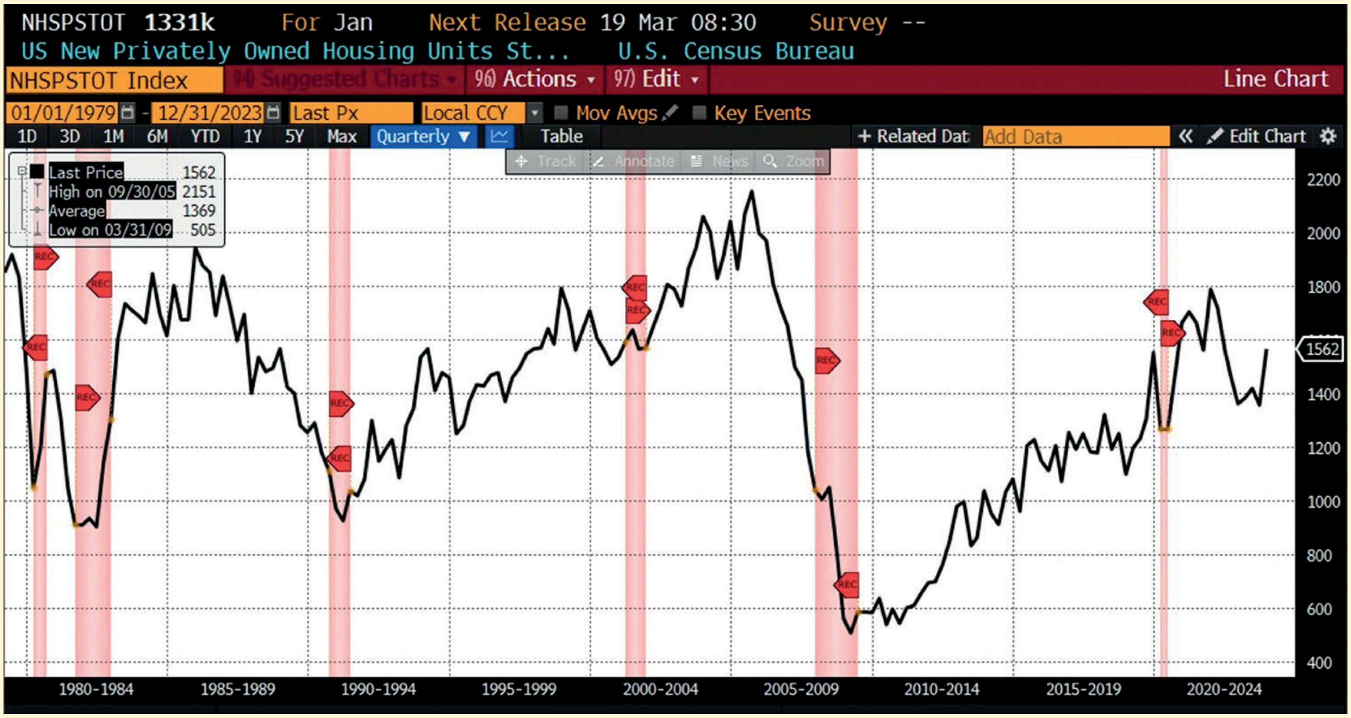
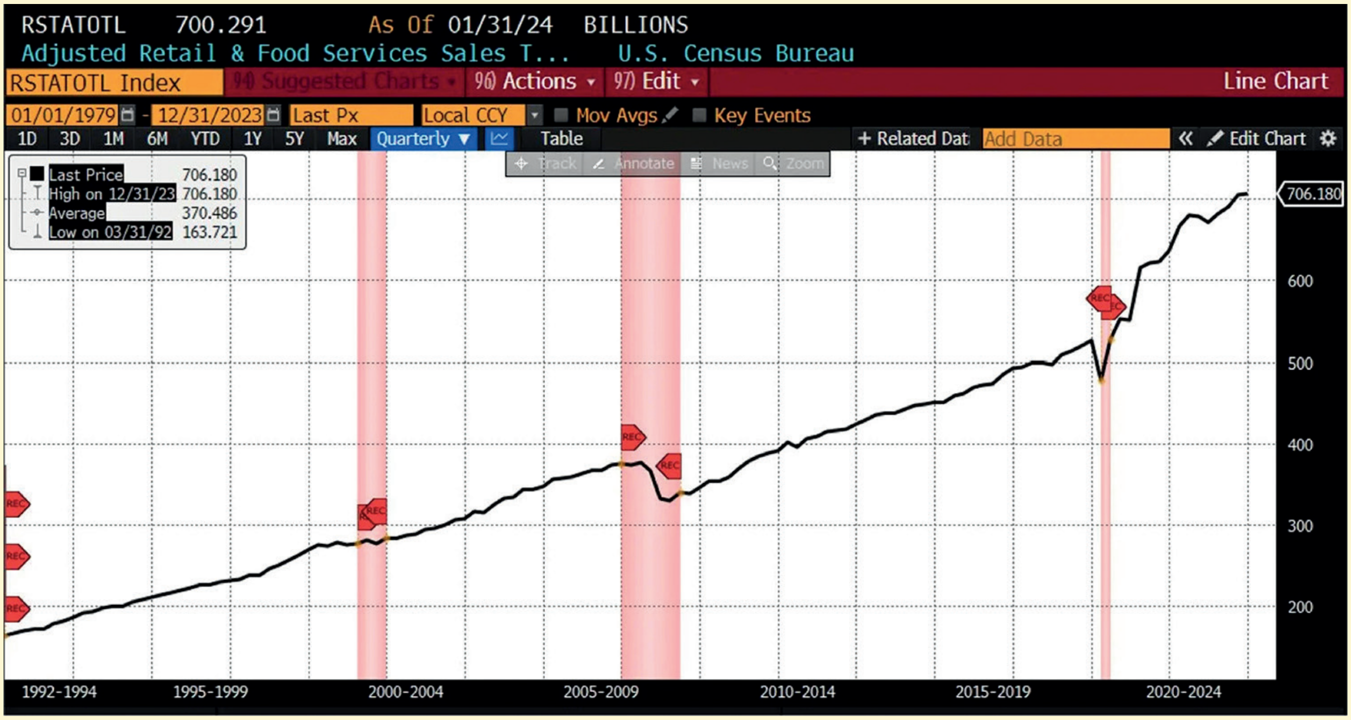
High on 03/31/00 0.155M
Average 0.122M
Low on 03/31/75 72104.00
0.16M
0.15M
0.14M
0.13M
0.125M
0.12M
0.11M
0.1M
90000
80000
70000
1975-1979
1980-1984
1985-1989
1990-1994
1995-1999
2000-2004
2005-2009
2010-2014
2015-2019
2020-2024


LEI STKP 4685.05 As Of 12/31/23
Conference Board US Leading Index Stock... Conference Board
LEI STKP Index
Line Chart
Last Price 4685.05
High on 12/31/23 4685.05
Average 1134.43
Low on 12/31/74 67.07
1975-1979
1980-1984
1985-1989
1990-1994
1995-1999
2000-2004
2005-2009
2010-2014
2015-2019
2020-2024


MGT2TB 1.37 As Of 12/31/23 SA
Inventory/Sales Ratio : Total Business U.S. Census Bureau
MGT2TB Index
Line Chart
Last Price 1.37
High on 09/30/82 1.68
Average 1.41
Low on 03/31/11 1.24
1980-1984
1985-1989
1990-1994
1995-1999
2000-2004
2005-2009
2010-2014
2015-2019
2020-2024


NHSPSTOT 1331k For Jan Next Release 19 Mar 08:30 Survey --
US New Privately Owned Housing Units St... U.S. Census Bureau
NHSPSTOT Index
96) Actions
97) Edit
Line Chart
01/01/1979 - 12/31/2023
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 1562
High on 09/30/05 2151
Average 1369
Low on 03/31/09 505
2200
2000
1800
1562
1400
1200
1000
800
600
400
1980-1984
1985-1989
1990-1994
1995-1999
2000-2004
2005-2009
2010-2014
2015-2019
2020-2024


RSTATOTL 700.291 As Of 01/31/24 BILLIONS
Adjusted Retail & Food Services Sales T... U.S. Census Bureau
RSTATOTL Index
96) Actions
97) Edit
Line Chart
01/01/1979 - 12/31/2023
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 706.180
High on 12/31/23 706.180
Average 370.486
Low on 03/31/92 163.721
706.180
600
500
400
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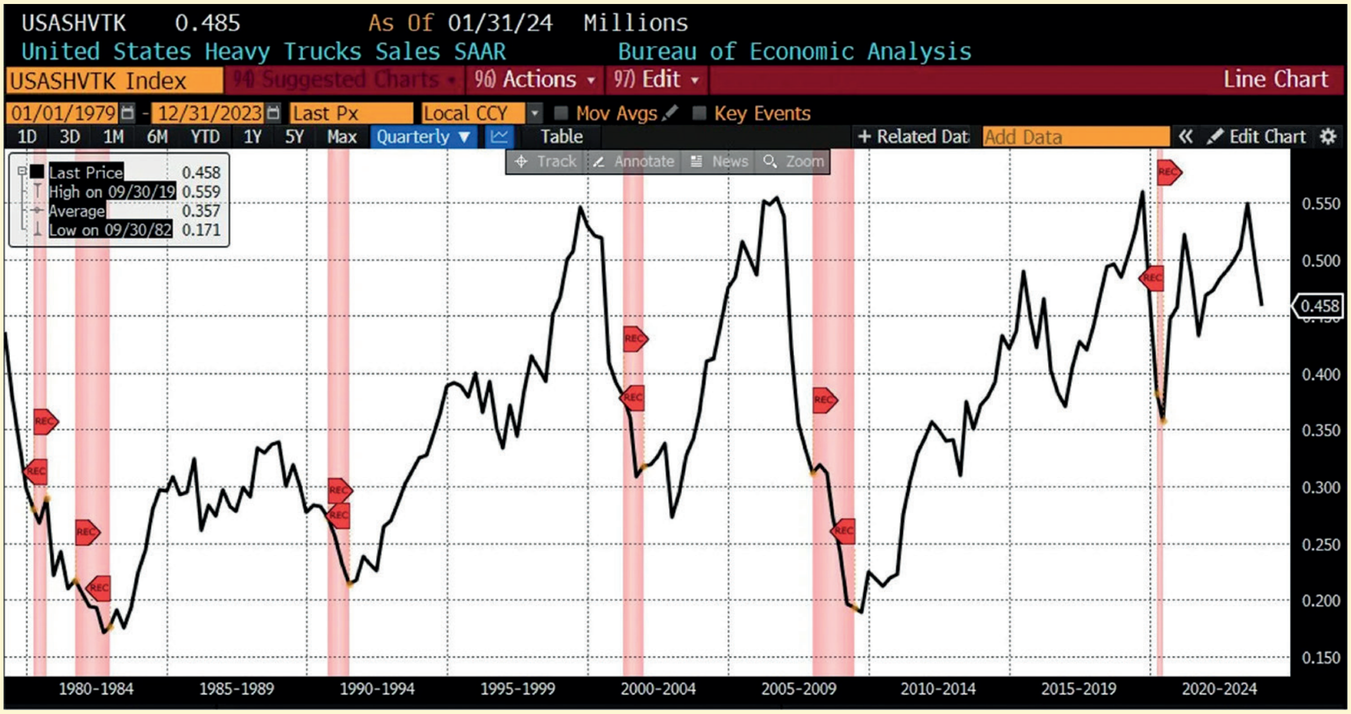
1992-1994
1995-1999
2000-2004
2005-2009
2010-2014
2015-2019
2020-2024


USASHVTK 0.485 As Of 01/31/24 Millions
United States Heavy Trucks Sales SAAR Bureau of Economic Analysis
USASHVTK Index
96) Actions
97) Edit
Line Chart
01/01/1979 - 12/31/2023 Last Px Local CCY Mov Avgs Key Events
1D 3D 1M 6M YTD 1Y 5Y Max Quarterly Table
+ Related Dat Add Data Edit Chart
Track Annotate News Zoom
Last Price 0.458
High on 09/30/19 0.559
Average 0.357
Low on 09/30/82 0.171
0.550
0.500
0.458
0.400
0.350
0.300
0.250
0.200
0.150
1980-1984
1985-1989
1990-1994
1995-1999
2000-2004
2005-2009
2010-2014
2015-2019
2020-2024


USYC1Y10 -71.816 +1.572 -71.816 / -66.797
At 2/16 Op -73.814 Hi -68.806 Lo -75.261 Prev -73.388 Vol 0
USYC1Y10 Index
96) Actions
97) Edit
Line Chart
01/01/1979 - 12/29/2023 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 -90.497
High on 03/31/10 344.330
Average 131.837
Low on 06/30/23 -160.216
-200
-90.497
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Low => High
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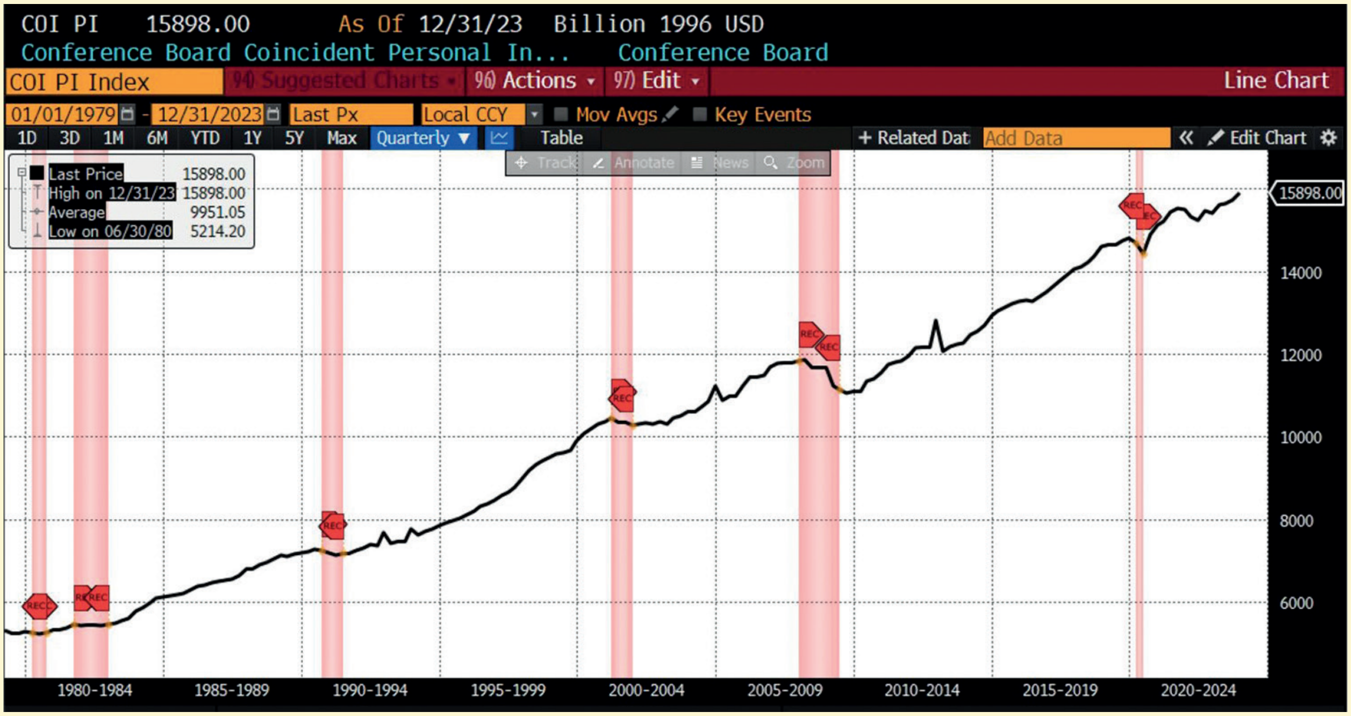
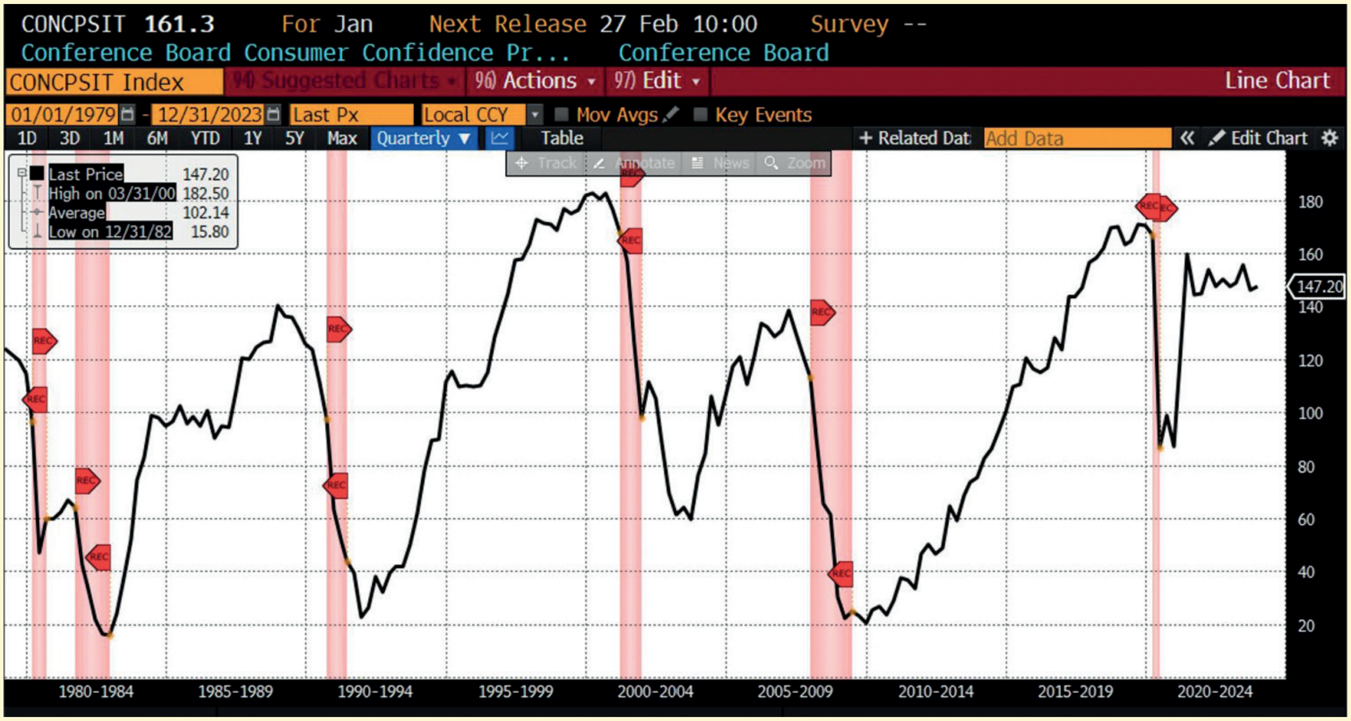
2023

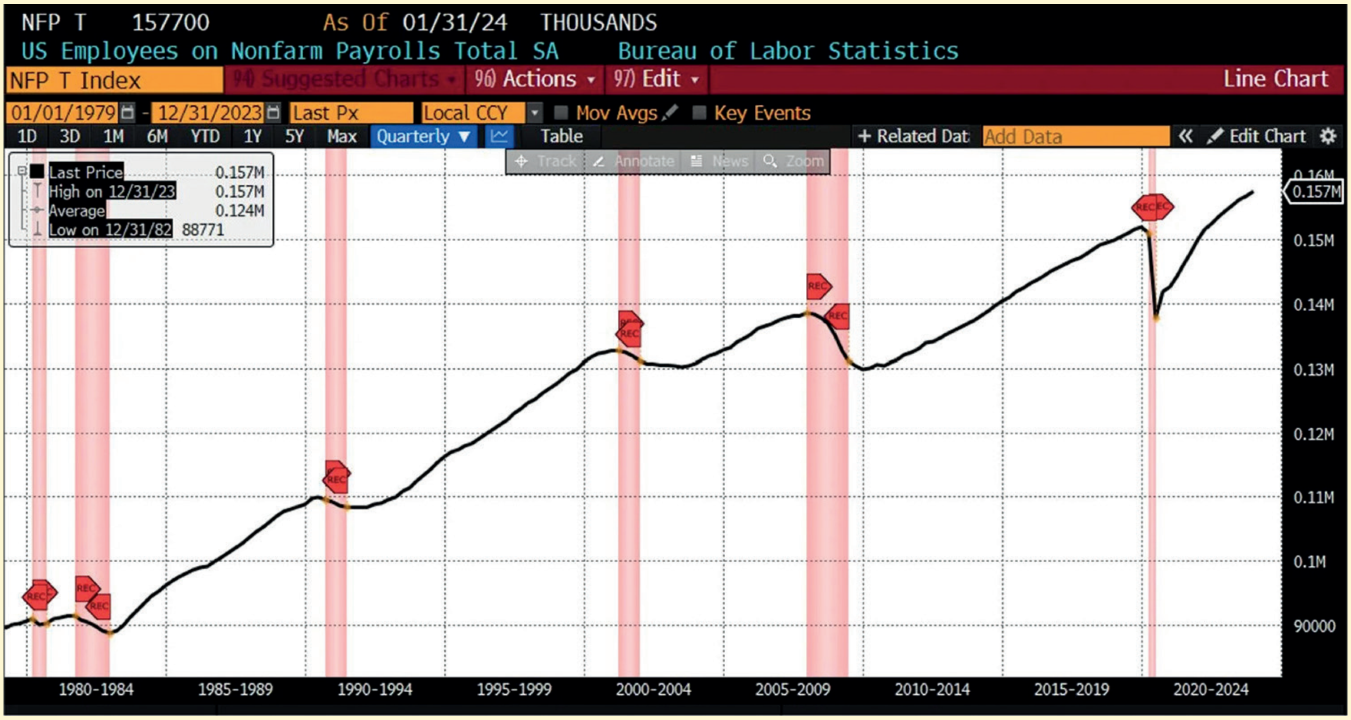
ROUGHLY COINCIDENT INDICATORS





CONCPSIT 161.3 For Jan Next Release 27 Feb 10:00 Survey --
Conference Board Consumer Confidence Pr... Conference Board
CONCPSIT Index
Line Chart
01/01/1979 - 12/31/2023 Last Px Local CCY Mov Avgs Key Events
Last Price 147.20
High on 03/31/00 182.50
Average 102.14
Low on 12/31/82 15.80
1980-1984
1985-1989
1990-1994
1995-1999
2000-2004
2005-2009
2010-2014
2015-2019
2020-2024

IP 102.5739 As Of 01/31/24
US Industrial Production SA Federal Reserve
IP Index
Line Chart
01/01/1979 - 12/31/2023 Last Px Local CCY Mov Avgs Key Events
Last Price 102.5715
High on 12/31/18 103.9784
Average 81.0624
Low on 12/31/82 47.1534
1980-1984
1985-1989
1990-1994
1995-1999
2000-2004
2005-2009
2010-2014
2015-2019
2020-2024


NFP T 157700 As Of 01/31/24 THOUSANDS
US Employees on Nonfarm Payrolls Total SA Bureau of Labor Statistics
NFP T Index
96) Actions
97) Edit
Line Chart
01/01/1979 - 12/31/2023 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 0.157M
High on 12/31/23 0.157M
Average 0.124M
Low on 12/31/82 88771
0.157M
0.15M
0.14M
0.13M
0.12M
0.11M
0.1M
90000
1980-1984
1985-1989
1990-1994
1995-1999
2000-2004
2005-2009
2010-2014
2015-2019
2020-2024


PRUSTOT 62.5% For Jan Next Release 08 Mar 08:30 Survey --
US Labor Force Participation Rate SA Bureau of Labor Statistics
PRUSTOT Index
96) Actions
97) Edit
Line Chart
01/01/1980 - 12/31/2023 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 62.5
High on 03/31/00 67.3
Average 65.0
Low on 06/30/20 61.5
67.0
66.0
65.0
64.0
63.0
62.5
62.0
61.0
1980-1984
1985-1989
1990-1994
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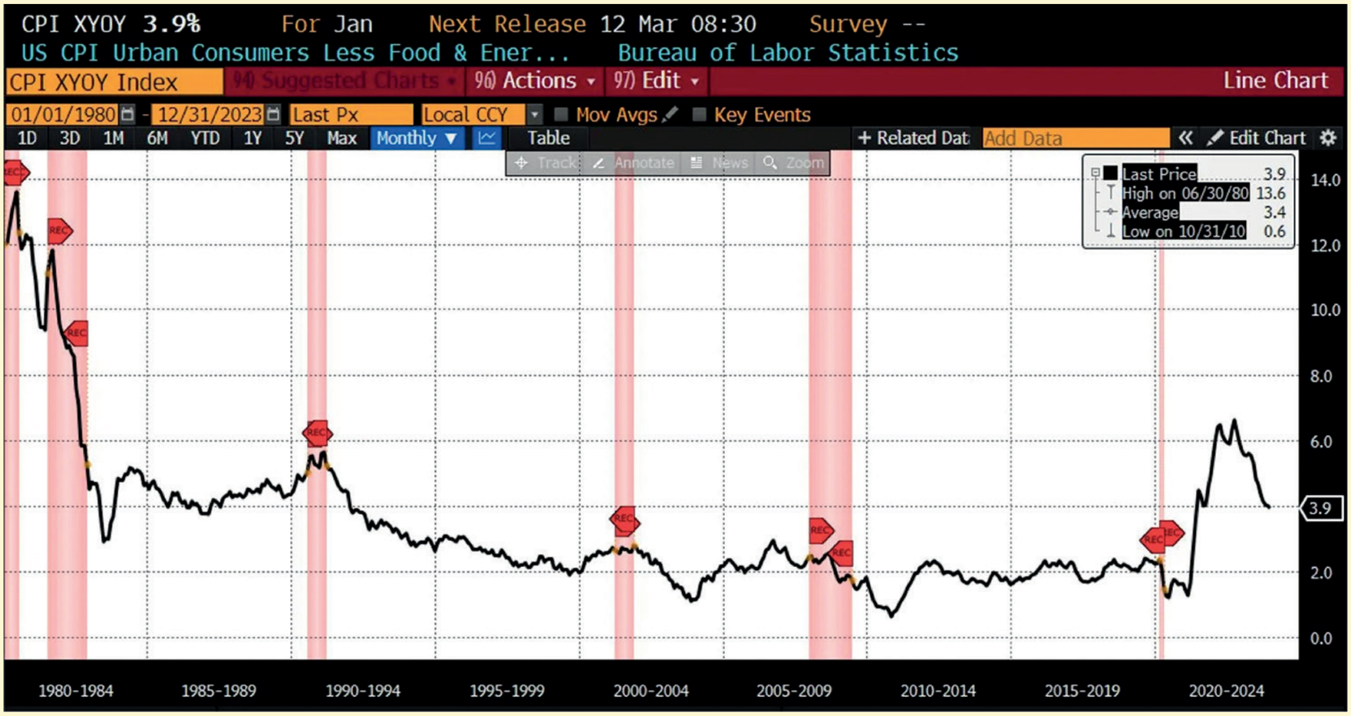
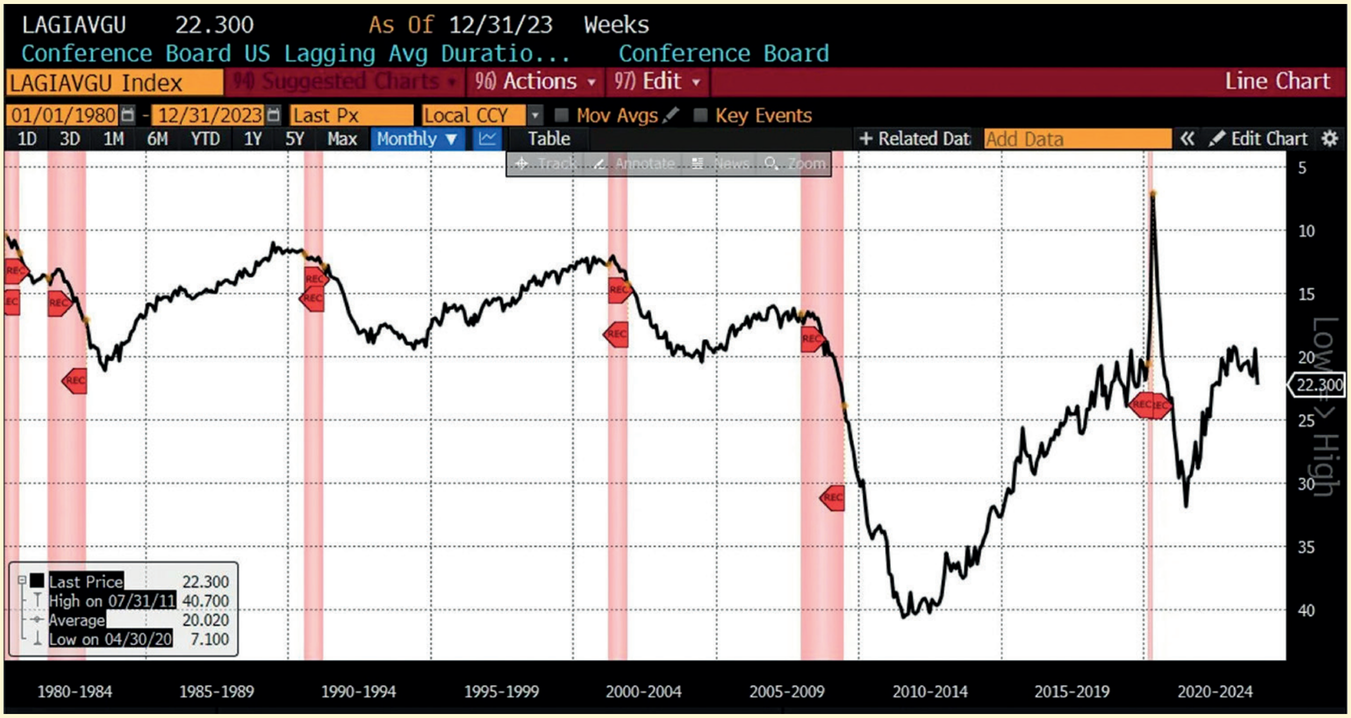
2000-2004
2005-2009
2010-2014
2015-2019
2020-2024

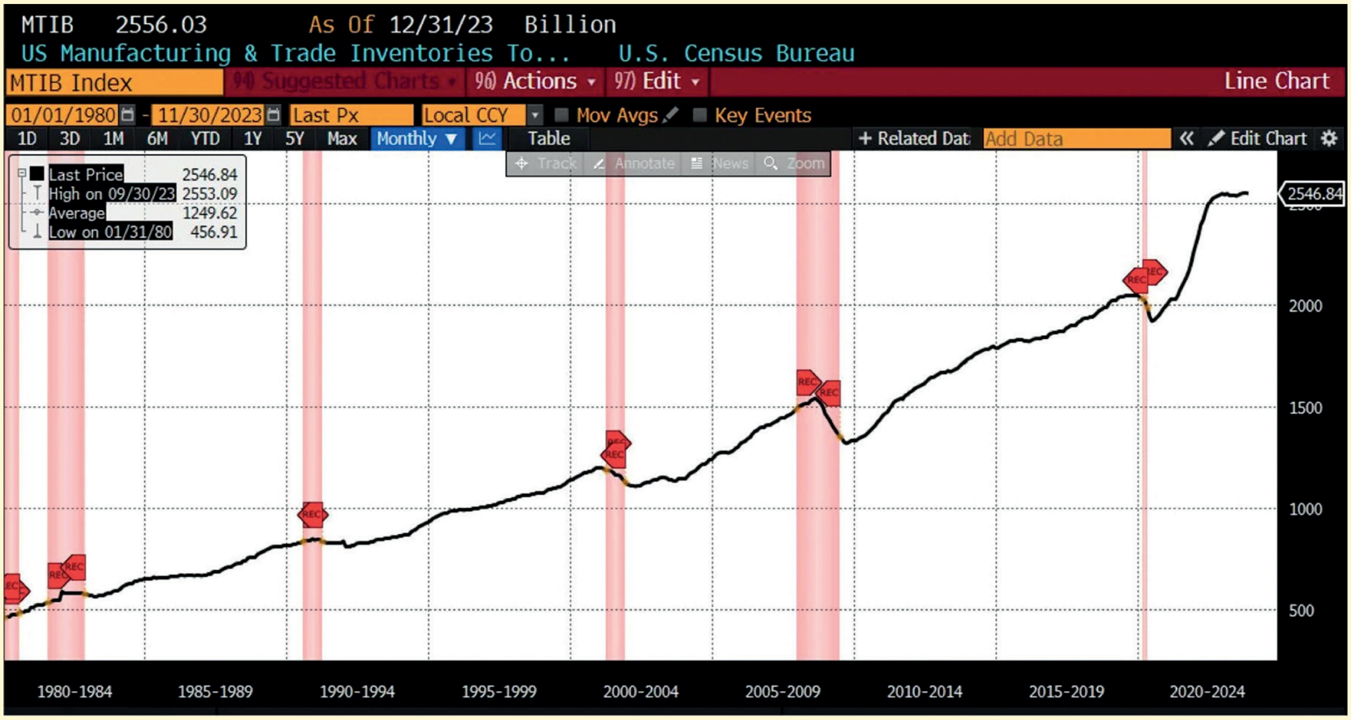
LAGGING INDICATORS




DCPB030Y 5.33 +.00 5.33 /5.33
At 2/16 Op 5.33 Hi 5.34 Lo 5.32 Prev 5.33 Vol 0
DCPB030Y Index
Line Chart
Last Price 5.33
High on 06/30/00 6.62
Average 2.25
Low on 05/31/21 0.04
'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


LAGIAVGU 22.300 As Of 12/31/23 Weeks
Conference Board US Lagging Avg Duratio... Conference Board
LAGIAVGU Index
Line Chart
Last Price 22.300
High on 07/31/11 40.700
Average 20.020
Low on 04/30/20 7.100
Low <-> High
1980-1984 1985-1989 1990-1994 1995-1999 2000-2004 2005-2009 2010-2014 2015-2019 2020-2024


LAGILOAN 1491610.000 As Of 11/30/23 Million 1996 $
Conference Board US Lagging Commercial ... Conference Board
LAGILOAN Index
96) Actions
97) Edit
Line Chart
01/01/1980 - 11/30/2023
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 1.492M
High on 04/30/20 1.896M
Average 1.061M
Low on 03/31/81 0.507M
2M
1.8M
1.6M
1.492M
1.4M
1.2M
1M
0.8M
0.6M
0.4M
1980-1984
1985-1989
1990-1994
1995-1999
2000-2004
2005-2009
2010-2014
2015-2019
2020-2024


MTIB 2556.03 As Of 12/31/23 Billion
US Manufacturing & Trade Inventories To... U.S. Census Bureau
MTIB Index
96) Actions
97) Edit
Line Chart
01/01/1980 - 11/30/2023
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 2546.84
High on 09/30/23 2553.09
Average 1249.62
Low on 01/31/80 456.91
2546.84
2000
1500
1000
500
1980-1984
1985-1989
1990-1994
1995-1999
2000-2004
2005-2009
2010-2014
2015-2019
2020-2024

CAPITAL MARKET PERFORMANCE

Ticker		Short Name	%1M	%3M	%1YR	3 Year Annualized	5 Year Annualized	10 Year Annualized
▸ SPR		S&P 1500 Composite Index	+3.39%	+10.94%	+21.14%	9.5716	13.9432	12.2692
▸ SPXT	d	S&P 500 Total Return	+3.56%	+11.31%	+24.69%	10.0893	14.4202	12.6078
▸ SPX	d	S&P 500 INDEX	+3.42%	+10.89%	+22.71%	10.0691	14.4013	12.5920
▸ MID	d	S&P 400 MIDCAP INDEX	+3.19%	+11.49%	+6.08%	5.2339	9.8119	9.2914
▸ RTY	d	RUSSELL 2000 INDEX	+4.54%	+13.07%	+4.44%	-2.3848	6.7074	7.0046
▸ SXXP	d	STXE 600 (EUR) Pr	+4.93%	+8.02%	+6.05%	8.9121	9.3663	7.7579
▸ TLT US	d	ISHARES 20+ YEAR	-1.41%	+3.02%	-9.40%	-11.6409	-3.1927	1.2805
▸ QLTA US	d	ISHARES AAA - A	-1.09%	+2.42%	+.17%	-3.5126	.9978	2.1957
▸ CRY	d	TR/CC CRB ER Index	+2.72%	-.38%	+1.88%	13.2506	8.4849	-.3915
XAU		Gold Spot $/Oz	-.58%	+2.00%	+9.57%			
XAG		Silver Spot $/Oz	+1.58%	-1.98%	+5.33%			
ILM3NAVG		Bankrate 30Y Mortgage Rates Na	+4.43%	-4.94%	+7.66%			
ILM1NAVG		Bankrate 15Y Mortgage Rates Na	+4.42%	-5.03%	+7.31%			
MB301ARM		5 Year ARM	+2.11%	-6.80%	+13.92%			
ILA3NAVG		Bankrate 30Y Fixe Mtg Refis Na	+2.21%	+2.21%	+17.66%			

(Source: Bloomberg Finance, LP)

– February 21, 2024

Inflation Hit Some States Harder

JASON SORENS
Senior Research Fellow

Last month, the Bureau of Economic Analysis released 2022 data on state and metro area inflation. These new numbers give us the opportunity to see where the inflationary cycle of 2021–2022 hit hardest. We can also adjust states' economic growth numbers for inflation to see where Americans are finding the most opportunity.

New England was hit especially hard by inflation in 2022. New Hampshire had the highest inflation in the country, 11.8 percent. Maine, Connecticut, Arizona, and Oregon were next. The state with the least inflation was Alaska, just 3.6 percent, followed by Arkansas, North Dakota, Nebraska, and South Dakota.

Inflation wiped out economic growth in most states last year. Adjusting for inflation, only five states had positive personal income growth last year: North Dakota, Delaware, South Dakota, Montana, and Alaska. Rhode Island, Oregon, DC, Mississippi, and New Hampshire all saw real personal incomes drop by more than eight percent.

State policy has a lot to do with why some states saw more inflation than others. Local land-use regulations that restrict home-building drive up the cost of housing, the largest part of the consumer price index. New Hampshire's eye-popping inflation rate was driven by housing costs, which also rose at the nation's fastest pace.

Some states have suffered in recent years because of shifts in the international market over which they had little control. In the 2010s, tech boomed, and commodity prices fell. The former trend helped places like San Jose, Austin, and Boise, while the latter trend hurt places like Kansas and Iowa.

Demographic trends also make a difference. The Northeast is growing slowly because people have been having fewer babies there for a long time. The historically high fertility rates in Utah and Idaho have helped make them the fastest-growing states for personal income since the Great Recession of 2008–2009. And Americans continue to move to warmer climates with natural beauty, so states without those features need to offer something else.

Beware of commentators who use per capita incomes to compare states. Per capita income is useful for comparing countries, not states, because Americans readily move across state lines for opportunities. A state can raise its per capita income by encouraging middle- and low-income households to move out. That's just what high-cost states like California, Connecticut, and New Jersey have done. Low-cost states like Arizona and Tennessee offer the best opportunity for families with modest incomes, which is why people move there in droves.

To figure out which states have the best policies for workers, we need to look at inflation-adjusted income growth over a long period, and we need to compare states within the same region that have similar climates and industries.

When we do that for the entire post-Great Recession period, some states stand out. In the West, Utah, Idaho, Colorado, Montana, Nevada, and Arizona have grown rapidly, while Alaska, Hawaii, Wyoming, and New Mexico have done the worst. In the Midwest, North and South Dakota and Indiana have all done well, while Illinois, Kansas, and Missouri have lagged. In the Northeast, all states have grown more slowly than the US as a whole, but Massachusetts and New Hampshire have done the best, while Connecticut is the worst (and the slowest-growing state in the U.S.). In the South, Florida, Texas, and Tennessee lead the pack, while Louisiana, West Virginia, and Mississippi have done badly.

What lessons can we derive from these patterns? First, states with better regulatory policies enjoy a lower cost of living and attract workers and investment. The most important regulatory policy is the freedom to build, that is, a lack of burdensome zoning regulations that make housing scarce and costly. But labor laws and licensing laws are also important, especially in manufacturing and health care.

Second, tax burdens and fiscal responsibility matter. South Dakota and Indiana have responsibly brought their tax burdens down and have out-competed Illinois and other nearby states that have not done so. In New England, New Hampshire and Massachusetts enjoy the lowest tax burdens. Florida, Texas, and Tennessee all lack state income taxes.

Workers don't like high taxes and will choose states with lower rates, all else equal. But taxes also feed into the costs of goods and services in the rest of the economy.

States can't control their climates or the vagaries of the international market. But they can control their tax burdens and regulatory policies. Smart policies can expand economic opportunity and shield residents from the inflation caused by Washington, DC.

– January 10, 2024

A Short Guide to ESG: Political Problems

PAUL MUELLER
Senior Research Fellow

Whether the political dimensions of ESG are features or bugs depends on your perspective. From the perspective of ordinary citizens, though, ESG is shot through with political problems in addition to its economic problems. Although the use of ESG affects ordinary people's lives in myriad ways, those impacted have little say in the project – even through their political representatives.

The elephant in the room is the special interest rent-seeking of ESG advocates. People are building careers consulting on "anti-racism" and "Diversity, Equity, and Inclusion" initiatives. Large financial firms charge up to 40 percent higher fees to clients investing in "Sustainability" funds. Entrepreneurs offer ESG data collection and reporting software, carbon offsets, and compliance consulting.

Hundreds of thousands of people work in ESG-related roles, which come with a pay premium. Corporate sustainability officers rely on in-house diversity officers who recruit consulting ESG impact researchers who appeal to climate advocacy organizations. Every major institution, from the World Bank to the United Nations to the World Economic Forum and the constellation of investment and advisory groups, has an ESG employee contingent.

ESG's Own Bootleggers and Baptists

Far be it from me to judge someone for wanting to earn a living. But we should consider whether those jobs represent *mutually beneficial exchange*. In a free market, jobs, products, and companies that serve no one disappear, but in highly regulated or artificial markets, the answer is much less clear. Do carbon offsets really create more value for people than they cost? Is extensive emissions reporting or DEI training making people's lives better?

We should note that ESG initiatives are not pushed by altruistic, disinterested, objective philosophers. They are backed by people whose livelihoods and careers are strongly tied to their success — and their expansion. How strongly these people believe in the philosophical merits of ESG is beside the point; ESG clearly is now a significant vested interest.

The question of motives, though, ties into an important theory of regulation: Bootleggers and Baptists. Regulations (prohibition of alcohol in this classic 1983 example) are often advanced by two different but aligned groups. Bootleggers (who don't want legal alcohol as competition) are driven primarily by their own material self-interests. Baptists (who would stamp out evil alcohol) are propelled by their convictions, a belief in the moral goodness of their cause.

Two important dynamics emerge here. First, (bootlegger) rent-seekers, greenwashers, and ESG salespeople use the moral justification of the (Baptist) environmentalists and equity advocates for their own gain. And second, it will be the Bootleggers who write the details of regulatory policy, because they care not about the moral wins, but the bottom line benefits. They will twist the terms and jargon until the best intentions serve only the vested interests. It happens every time.

Under the Baptists' altruistic moral language is the bootleggers' doling out of money and power. They invariably funnel benefits to themselves through favorable regulations, at the expense of everyone else.

When All You Have Is an ESG Sledgehammer

Implementing ESG politically presents a sledgehammer approach to an intricate web. Markets reward innovation, nimbleness, and nuance; Government policies must, by definition, be rigid and uniform. For administering justice and public order, the consistency of the law is admirable. But laws and regulations can't dictate something as dynamic as the most efficient solar cell, the appliances people use, the particular mitigation that will protect a village from flooding. Those solutions, as they emerge, are local, changing, and hard to anticipate. Government choosing between them only slows down the improvements.

Sweeping government rules about specific business practices create system risk as all players in the market are forced to engage in similar activities. No right to opt out means no innovation, market stagnation. When unintended consequences (inevitably) unfold, everyone in the market suffers together. This kind of systemic risk, created by and in response to extensive regulation, that resulted in the 2008 financial crisis.

Government laws codify a single, existing way of doing things. That makes laws a poor tool for experimentation, dissent, and innovation. Implementing ESG through political rulemaking creates a world with more corruption and widespread systemic risk.

ESG's Attack on Sovereignty

The political means required to implement a global ESG agenda are antithetical to national sovereignty, self-governance, and self-determination. Global organizations want to direct every country's policy in pursuit of global or universal goals. Officials at the UN, World Bank, WEF, European Union, and a host of other international organizations are not accountable to the citizens or voters of any country. Nor are they subject to the wishes of consumers and innovators, who might opt out in a marketplace. By what right do largely unelected global elite ESG advocates get to impose their priorities and values (to their own benefit) on everyone else in the world?

Despite the movement's superficial calls for transparency, ESG goals have primarily been advanced without the knowledge or consent of those they affect. Millions of people whose 401Ks are managed by Blackrock did not elect that their capital to be used to advance ESG initiatives. ESG advocates avoid market pushback that might be generated by unpopular taxes on gasoline or emissions. Instead, they engage in regulatory fiat and misdirection via massive subsidies to their preferred industries and companies.

The billions of dollars in subsidies to electric vehicle manufacturers, battery producers, and renewable energy companies were doled out by elected officials in the US, but the real costs are largely obscured. How much does a billion-dollar subsidy to an EV producer cost the ordinary taxpayer? And if we can't answer that question for hundreds of subsidies and handouts, how can citizens engage in robust and informed self-governance?

When Germany's high court ruled in 2023 that politicians couldn't simply shift funds allocated for COVID-19 into climate goals, the coalition government's will to spend collapsed almost immediately. Once accountable to their voters for allocating ESG spending in the general budget, politicians had to be much more honest about the costs of borrowing for net-zero and green energy projects.

Political Implementation Hikes Already High ESG Costs

Political problems surrounding ESG continue to proliferate. Large and growing vested interests can't evaluate "sustainability" fairly while cashing the paychecks ESG generates.

Those bootleggers inevitably hijack the earnest activists' high-minded ideals for personal gain, at the expense of everyone else and at the expense of the ideals themselves.

And finally, the regulatory and enforcement tools required to implement global ESG goals undermine national sovereignty and interfere with each nation's accountability to its citizens. The economic fallout from ESG implementation would be high, but the potential political damage could be even more costly.

– January 5, 2024

Immigration, Inflation, and Wages: Better Under Trump or Biden?

VANCE GINN

Associate Research Fellow

The Economist recently compared Joe Biden's and Donald Trump's economic records, concluding Biden wins so far. While the article raises valid points, it excludes key details that make the findings questionable.

Ten months from now, there's a high likelihood Biden and Trump could go head-to-head again for the presidency, especially after the results from the Iowa caucus. But voters should be informed about the effects of their policies on key issues like immigration, inflation, and wages.

Starting with a divisive bang, let's look at each leader's track record concerning immigration.

The Economist correctly noted that apprehensions along the southern border were much lower under Trump. They increased by the most in 12 years during the economic expansion of 2019, decreased early in the COVID-19 pandemic when people could be turned away for public health concerns, and rose again during the lockdowns.

While some may see apprehensions rising between Trump and Biden as a loss for Biden, I see it as a loss for both.

This metric is somewhat unreliable, given one person can be caught and counted multiple times, and those caught are a subset of total migrants. The truth is immigration is good for the economy, but government failures create unnecessarily complex barriers against legal immigration, contributing to the humanitarian crisis along the Mexico border today.

Neither President has pushed for what's needed (market-based immigration reforms) both lose.

Inflation is another hot topic, especially for Biden. *The Economist* hands the win to Trump, as inflation was far lower during his presidency. But can we give him the credit?

Remember, Trump pressured the Federal Reserve to reduce its interest rate target and expand its balance sheet, which was inflationary. His deficit spending skyrocketed during the lockdowns and was mostly monetized by the Federal Reserve, contributing to what was always going to be persistent inflation. Biden made this deficit spending and resulting inflation much worse.

Add in the Fed's many questionable decisions, such as doubling its assets, cutting and maintaining a zero interest rate target for too long, and focusing too much on woke nonsense, and we can see how this was always going to be persistent inflation.

But even the Fed's latest projections indicate it won't hit its average inflation target of two percent until at least 2026. Likely, it will cut the current federal funds rate target range of 5.25 percent to 5.5 percent three times this year, keep a bloated balance sheet to finance massive budget deficits, and run record losses. If so, this inflation projection is too rosy.

Some of Trump's policies helped stabilize prices, including his tax and regulation reductions. But he still allowed egregious spending. Biden has doubled down on red ink that has contributed to the recent 40-year-high inflation rate.

While inflation has been moderating recently under Biden, Trump gets the win. Of course, neither Presidents nor Congress control inflation, as that job is the Fed's, but its fiscal policies influence it.

When it comes to inflation-adjusted wages, *The Economist* grants a tie.

Let's consider real average weekly earnings that include hourly earnings and hours worked per week, adjusted for the chained consumer price index, which adjusts for the substitution bias and has been used for indexing federal tax brackets since the Tax Cuts and Jobs Act of 2017.

Trump's era witnessed a robust upward trajectory of real earnings, with considerable gains by lower-income earners, thereby reducing income inequality. We must acknowledge a real wage spike in 2020 during Trump's lockdowns, marked by the loss of 22 million jobs and various challenges. To maintain a fair analysis, I disregard this spike.

A year later, real wages demonstrated a decline under Biden. Extending the timeframe to two years later, real wages remain relatively flat to slightly increased.

To provide a contextual understanding, when we consider the trend under Trump, excluding the 2020 spike, real wages for all private workers or production and nonsupervisory workers fall below those observed during Biden. It's worth noting, however, that these wages have been higher since 2019, albeit nearly stagnant for all private workers.

Given real earnings, I agree with *The Economist* that Trump and Biden are tied.

While much more can be said for each President's policies, continuing to add context when making assessments is crucial.

I give Trump a nuanced "win" overall because his policies supported more flourishing during his first three years until the terrible mistake of the COVID lockdowns, with its huge, long-term costs. I should note that I made a strong case inside the White House for no shutdowns and less government spending but, alas, my efforts, and those by others, lost to Fauci, Birx, and Trump.

Given the improved purchasing power during his presidency, Trump receives better poll ratings than Biden after three years of their presidencies. But this win doesn't mean that Trump's record is best regarding these issues, protectionism, and more.

Let's hope free-market capitalism, the best path to let people prosper, is on display this November, no matter who is on the ballot.

– January 19, 2024

$34 Trillion and Climbing

PETER C. EARLE

Senior Research Fellow

Just before the start of 2024, the US Federal debt surpassed a new milestone: $34 trillion. In 2023 the US added $2.65 trillion in debt, the second largest annual increase in history after the 2020 increase of $4.5 trillion. Going back to 1995, Federal Debt has increased by just over $1 trillion per year, but since 2010 that number has jumped to $1.7 trillion annually.

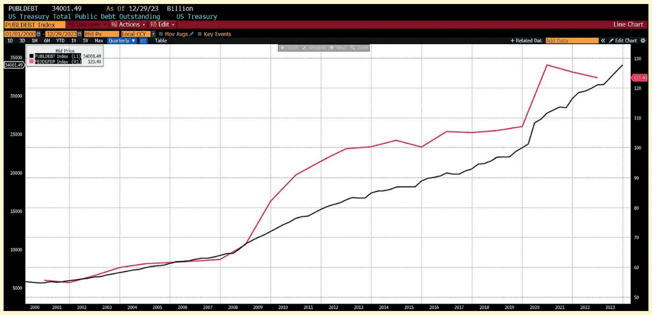
The surge comes amid mounting warnings from credit rating agencies and a "soft" repudiation of both the US dollar and US government-issued securities.

The time taken to surpass successive $10 trillion milestones has dropped. After crossing the $1 trillion dollar mark for the first time in 1981, the Federal debt didn't surpass $10 trillion until 2008, 27 years later. It only took nine years to surpass $20 trillion (2017), then a mere five years to eclipse $30 trillion (2022). Now, 22 months after that, the US is almost halfway to the $40 trillion point. (It's difficult to imagine that the US Federal debt was, well within many of our lifetimes, less than one-third the current market capitalization of Apple, Inc., but that is indeed the case.)

In a year where geopolitical hotspots are on the rise – Russia-Ukraine recently being joined by the Israel-Hamas war which is currently expanding across multiple fronts – of particular note is the ratio of the current US debt pile to annual economic output. At $34 trillion that ratio is 1.2, whereas the debt-to-GDP ratio at the end of World War II was 1.1 in an era of a managed gold standard with few international competitors. If a war footing were suddenly called for, only the colossal monetization of debt (if not the outright printing of money, and vastly higher taxes) would suffice.

The debt assumed over the last two years has additionally been incurred at much higher interest rates. The Fed began hiking rates on March 16, 2022, when the debt level had just surpassed $30 Trillion and the effective rate was 0.08 percent. The last $4 trillion of debt has been taken on at substantially higher rates, with the last $2.5 trillion sold at yields over 3 and 4 percent for 10-year maturities (Treasury bonds) and well over 5 percent at the short end (Treasury bills). The current debt service is in the neighborhood of $1 trillion per year annualized, double what it was less than two years ago and representing between 10 and 20 percent of the 2022 Federal budget.

US Treasury Total Public Debt Outstanding (black) vs. Gross US Federal Debt to GDP Ratio (red), 2000 – present



(Source: Bloomberg Finance, LP)

It is wholly understandable that repeated warnings about the increasing debt incurred by the US government would fall upon increasingly disinterested ears. Consider the following article from October 1981:

> The Treasury Department said a series of routine financial transactions during the day

> pushed the debt total beyond the symbolic trillion-dollar barrier. The debt figure had topped $999.3 billion last Friday, and then held steady for the next four business days as the Treasury's redemption of old securities nearly matched its issuance of new ones … The 13-digit debt is an inevitable result of tax and spending decisions made by Congress months or years ago. In the past few weeks, as the debt total approached the new benchmark, political figures from President Reagan on down have invoked the trillion-dollar liability as a symbol of government spending run amok. "One trillion dollars of debt," the president said in his televised address last month. "If we as a nation needed a warning, let that be it"…If the debt keeps increasing at the current rate, it will hit $2 trillion by the end of the 1980s.

In 1981, the debt service was an unthinkable $15 billion per year. In 2023, the average daily increase in the Federal debt was $10.7 billion and from June 2nd to June 5th last year the national debt increased by $358 billion, over 20 times the entire annual debt service in 1981. Of the 248 market days in 2023, the debt increased on 144 of them by an average of $24 billion. On the remaining 104 days, it fell by an average of $8 billion. Three steps forward, one step back.

Since the debt surpassed $1 trillion over 40 years ago, the claim has repeatedly been made that the end is near and that at some point in the near future the entire fiscal edifice would come crashing down spectacularly. But economists are legendarily bad at making predictions, and forecasting apocalypses is a particularly dodgy enterprise for our species. Personally, I am inclined to guess that whatever the end game of skyrocketing government debt is, the US is closer to it than to the beginning, but that too might be wrong. In October 1981 no one would've believed that 15-and-a-half thousand days and $33 trillion in debt later there would still be a market for US Treasury securities, or that the dollar would still be the global reserve currency (if increasingly under siege).

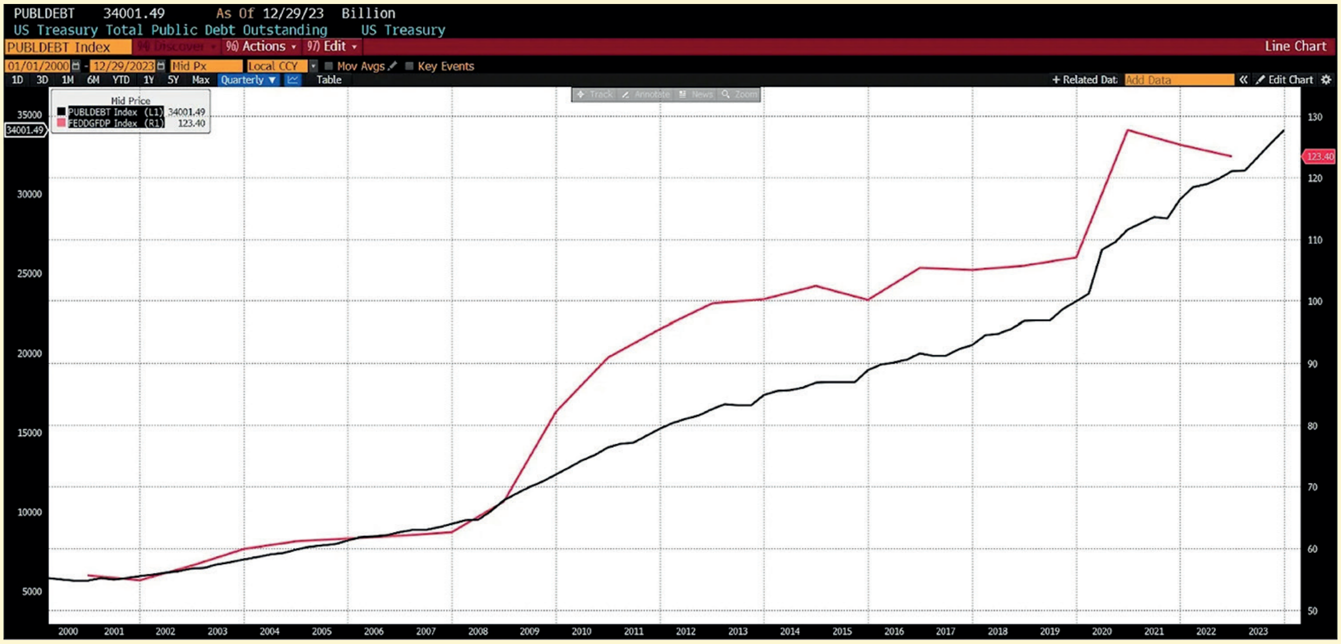
Perhaps a better tack to take regarding warnings about borrowing into oblivion is to ignore numerical benchmarks in lieu of expressing the following. First, the US government will never, ever, voluntarily cut spending. When at some point the issuance of Treasury bonds is no longer an option for some reason or another, some combination of the destruction of the dollar's value and increasingly confiscatory levels of taxation will follow. For our self-preservation, American citizens will need to find a means of arresting the Beltway's profligate instinct. Second, although only one-quarter of US government debt is currently owned by foreign creditors, the prospect of having our fates controlled by outside powers with interests that diverge vastly (and often in opposition) from ours should be menacing. At the very least, US citizens should consider what they are willing to live without or see others live without. Medicare? The US Coast Guard? Pension backstops? The Food and Drug Administration? Subsidies for just about everything?

At this point, $35 trillion in US debt is baked in. Forty trillion, too, may only be a handful of insincere political diatribes away.

Too much credibility has been squandered on the futile endeavor of predicting fiscal tipping points. Making the consequences of runaway debt clear – unprecedented levels of taxation, a browbeaten dollar, and unwelcome yet unavoidable foreign influence in domestic affairs – is likely a more effective, and more scientifically defensible, warning.

– January 6, 2024

US Treasury Total Public Debt Outstanding (black) vs Gross US Federal Debt to GDP Ratio (red), 2000 – present



(Source: Bloomberg Finance, LP)

ChatGPT is a Calculator; Deal with It

MICHAEL MUNGER
Visiting Senior Research Fellow

ChatGPT, the generative artificial intelligence processor found in a growing number of applications, uses "natural language processing" to estimate the sequence of words that users want next in phrases, sentences, and paragraphs. In other words, it's a calculator. Deal with it.

Cranks and crotchets in high dudgeon over calculators are nothing new. We made our kids learn long division, and their multiplication tables, because…. well, because we did. In 1990, Jerry Adler published an article in *Newsweek*, entitled "Creating Problems: It's time to minimize rote learning and concentrate on teaching children how to think." The article starts this way:

> Let us consider two machines, each capable of dividing 1,128 by 36. The first is a pocket calculator. You punch in the numbers, and in a tenth of a second or so, the answer appears in a digital display, with an accuracy of, for all ordinary purposes, 100 percent.
>
> The second is a seventh grader. You give him or her a pencil and a sheet of paper, write out the problem, and in 15 seconds, more or less, there is a somewhat-better-than-even chance of getting back the correct answer.
>
> As between them, the choice is obvious. The calculator wins hands down, leaving only the question of why the junior high schools of America are full of kids toiling over long division, an army of adolescents in an endless trudge, carrying digits from column to column.

Later in that article, Thomas Romberg, of the University of Wisconsin, Madison, is quoted: "There isn't anyone out there anymore who makes his living doing long division."

This argument was unpersuasive to many. Luddites argue that the point for educators was not to obtain the correct answer in the fastest and most reliable way. Rather, learning to do the long division problem "by hand" meant that the student actually understood the process of calculation, rather than simply producing an answer mysterio-mechanically. Still, a more persuasive argument, made by Professor Romberg, is that doing long division is archaic and inefficient, and you can't get paid for it because there is a better and faster way. At some point, we switch to using a calculator.

That wasn't always true, of course. The *original* calculators were just people, called "computers." They actually did "make their living doing long division," and computing square roots, and so on. Those people were put out of business by mechanical, and then electronic, calculators and computers of the sort we take for granted today. It was not easy to get a job as a computer, because you had to be smart and quick, and able to focus for long periods. A modern spreadsheet program, installed on an off-the-shelf $700 laptop, can do the work of 1,000 person-hours or more in a few seconds.

The advent of machine/electronic "computing" had two effects. First, it cost thousands of people their jobs. But second, because the cost of computing fell by more than 99.9 percent, there was a massive burgeoning of economic activity. Things became faster, cheaper, and more convenient on a scale that would have seemed like science fiction as recently as 1955.

Old Whines in New Bottleneckers

Note that there are three separate arguments:

1. People need to learn how to think, and understand deeply!
2. Protect the jobs! People have worked hard to do this!
3. New tech is disruptive, and the effects are hard to predict!

On a larger time scale, we have seen exactly the same argument play out over centuries in the case of many new technologies. It is hard to imagine how disruptive the introduction of the printing press was for society, but think about it: There were thousands of people who were highly accomplished scribes, and "illuminators." An illuminated text, done by artists who had practiced their craft for decades, was a work of art. The cost of such a book was the equivalent of decades of salary for the average worker, well beyond the ability of any but the richest elites to own. The printing press was capable of producing text, and illustrations, at a cost that was (comparatively) so low that skilled manuscript copiers became obsolete within less than a decade.

But, of course, the democratization of books, both because of the reduction in cost and the decision to print in the vernacular instead of only Latin, transformed the European world. As Andrew Pettigree has written in *Brand Luther*, the net effect was an enormous increase in the number of jobs in the printing industry, and upward trends in literacy, reading, and the ability to reach mass publics. One could argue that the effects, including the Reformation and shockingly violent wars that it provoked, were disruptive, and of course that's right. But very few of us, other than Patrick Deneen, want to go back.

More recently, but just as catastrophically for the "workers" involved, we saw the disruptive impact of universal access to GPS on phones using apps such as Waze. London's famous "black cabs" (originally short for "cabriolet") could only be operated by licensed drivers. And the most formidable part of the licensing process was simply called "The Knowledge." Established in 1865, this required that applicants acquire a mental map of all 25,000 streets, lanes, and alleys (London is a maze, not a grid). But ride-share companies, such as Uber, need not require the knowledge because they have "the app."

Which is better? In large measure — except for cost! the two are indistinguishable when operating properly. Waze has the advantage of real-time updates on congestion, accidents, and construction, of course. Human drivers who know the shortest route, but don't know there's an accident, are at a disadvantage. But all of us have had the experience of Waze, or Google or Apple Maps, telling us to turn into a building, or sending us on a bizarre route just because the AI is confused. Drivers who have paid the costs of acquiring "The Knowledge," just like book copyists before them, protest that the new technology should be banned.

But as Mellor and Carpenter argued in their book *Bottleneckers*, such movements are trying to count benefits as costs. It is good that people no longer have to waste years to acquire "The Knowledge," just as it is good that people can now spend their time on more productive activities rather than use pencil and paper to compute solutions to long division problems. It is difficult for those who currently find themselves displaced, but in just a few years the dramatic increase in productivity and decline in costs will dwarf those difficulties. These old whines in new bottlenecker form must not be acted on by policymakers.

ChatGPT

And so we come, finally, to ChatGPT. I'm assuming the reader is familiar with the technology, and I want to suggest that the analogy to the printing press, to calculators, and to GPS, is apt. In January

2023, I wrote a piece for Reason that I then considered satire. Now, I'm not so sure. There is nothing conceptually difficult about using natural language processing to create all possible word sequences, for documents ranging from haikus to enormous tomes. Of course, storing and indexing this trove would not be physically possible, but that limitation is at least in principle one that can be overcome. It would be Borges' "Library of Babel," only more comprehensive.

And then that is the end of that. There is no more writing to do, it's done. All we need is to find the right text from the universal library and use it. No writer's block, no staring at that mocking-blinking cursor, it's all there.

Of course, I can hear the traditionalists lining up for the old whines. Just like for the calculator: better to learn to think, no shortcuts, good for you to acquire the skill, just because you should, and so on. Further, people actually do "make a living" by writing. But then people made a living by spending years learning to be a human "computer" before calculators came along.

Look, folks. ChatGPT is happening. People are rapidly learning how to use it. For many routine tasks — and, honestly, most writing is routine, not creative — it is faster and actually better to have the AI create the text, at least for the first draft. Or to have the AI create 5 or more versions of a text so that you can pick one and then edit that.

Does this mean that we as a society will value writing less? Does it mean that the people — and I'd include myself, writing this right now! — who "make a living" writing are going to have to rethink our choices? Does it mean that 20 years from now we will look back, with 2020 hindsight, and say that the opposition to AI natural language applications was misplaced? I think the answer to all these questions may be "yes." Deal with it.

– January 1, 2024

Bidenomics and the Slippery Erosion of Economic Freedom

NIKOLAI G. WENZEL

Associate Research Fellow

Bidenomics is a moving target.

The sheer numbers are staggering, as the regulatory factory on the Potomac spews negative externalities, polluting the economy. 2023 closed with 90,402 pages of rules and regulations published in the Federal Register — you read that right… more than *ninety thousand pages* of rules. The Biden administration finished the year with the second-longest collection of all time. President Obama holds the record at 95,894, and President Biden just displaced President Trump's record of 86,356 pages in 2020. To achieve this feat, the Biden administration beat its own record of 79,856 pages in 2022.

But the numbers are not the only challenge. Indeed, regulatory watchers find themselves playing whack-a-mole with the *variety* of rules and regulatory agencies. It is now a sadly quaint notion that Congress, and only Congress, makes the laws. The language of the Constitution is unambiguous, and it's right there at the beginning, just after the Preamble, in Article 1, Section 1: "*All* legislative Powers herein granted shall be vested in a Congress of the United States" (emphasis added). Alas, this crystal-clear language, and the non-delegation doctrine which flows from it, are routinely ignored. Instead, we see an alphabet soup of rule-making agencies.

To be sure, Congress does occasionally break through the gridlock, and gives us some real doozies. In April 2021, following the example set by the Trump administration's 2020 CARES Act, the Biden administration pushed through a COVID-19 relief bill that had little to do with COVID relief, and much to do with seizing the commanding heights of the economy. The Infrastructure Investment and Jobs Act of November 2021 and the Inflation Reduction Act of August 2022 continued the profligacy and increased government control of the economy. The Chips and Science Act (also passed in August 2022) continued the protectionist trend towards national industrial policy.

Alas, legislation is just the tip of the iceberg.

In addition, of course, are executive orders, which are "directives written by the president to officials within the executive branch requiring them to take or stop some action related to policy or management. They are numbered, published in the Federal Register, and cite the authority by which the president is making the order." While they are formally an exercise for the executive to clarify its implementation of a law, in practice, executive orders permit the executive to make laws by decree, often by setting strategic priorities and enforcement targets for administrative agencies.

Then, the administration can issue Memoranda. Presidential memoranda "also include instructions directed at executive officials, but they are neither numbered nor have the same publication requirements. The Office of Management and Budget is also not required to issue a budgetary impact statement on the subject of the memoranda."

Finally, federal agencies issue rules, which are their interpretations of statutes passed by Congress. The 15 cabinet agencies, under the direct authority of the President, naturally reflect administration priorities. There is some debate about the actual independence of the 19 independent regulatory agencies, which are nominally independent from the executive, as well as (we can only say roughly) 400 executive agencies. But one thing is certain — they're all issuing preliminary and final rules, and contributing to the tidal wave of backdoor legislation and regulation.

To this, we could add policy statements and guidance documents, which are "agency statement[s] of general applicability and future effect, other than a regulatory action, that [set] forth a policy on a statutory, regulatory, or technical issue, or an interpretation of a statute or regulation."

Are you bewildered yet? Well, remember those 90,000+ pages of rules and proposed rules.

Over the holiday season, the Biden administration snuck in two particularly interesting rules.

On December 7, 2023, the National Institute of Standards and Technology (I bet you didn't see that one coming!) issued draft guidance regarding the federal government's exercise of "march-in" powers under the Bayh-Dole Act of 1980. The Act allows recipients of federal funding to retain patent rights on inventions developed with federal funding, and to commercialize them. The Act contains a clause granting the federal government "march-in" powers. In simple summary, this means that the federal government can force a business to commercialize a patent developed with federal funding, or impose certain conditions, if the relevant regulatory agency rules that the public interest is not being served. This can be broadly interpreted as prices that are "too high" or production that is "too low." To date, march-in powers have never been invoked by the federal government. In the past few years, activist groups and state attorneys general have petitioned the federal government to force drug manufacturers to lower their prices through the march-in mechanism. As this is a proposed rule, we don't yet know what will happen in the comment period. But the Biden administration is clearly signaling its intention to stick its regulatory nose into pharmaceutical markets, by attempting to invoke march-in powers for the first time in the 43 years of the Act's existence. Beyond the general move towards national industrial policy, the chilling effect on investment is obvious.

On January 10, 2024, the Labor Department issued a final rule on the classification of workers as employees versus independent contractors. The rule does not go as far as California's gig-worker law, which classified gig workers as employees, rather than contractors. But it does seek to reclassify some independent contractors as employees, by strengthening the "economically dependent" test, which posits: "the ultimate inquiry is whether, as a matter of economic reality, the worker is economically dependent on the employer for work (and is thus an employee) or is in business for themself (and is thus an independent contractor)." Because the rule seeks to strengthen the test, its results are still uncertain. A recent Mercatus Center working paper found that the California gig law reduced self-employment and overall employment. The Labor Department's rule is thus likely to have negative effects on employment, while stifling the dynamic and innovative gig and platform sectors of the economy.

These are but two recent examples. Bidenomics continues its Janus-like war on economic freedom. The Biden Administration claims to promote economic growth and increase competitiveness while choking the economy with rules and regulations.

There are many steps the US could take to clean up the economy and the government chokehold on entrepreneurial activity. A return to the Constitution would be a good place to start. This would mean, first, that the US federal government returns to its original purpose and scope of limited and enumerated powers. This would also mean curbing the federal government's extra-legislative regulatory activity. It's hard enough for entrepreneurs to keep up with congressional shenanigans without the executive branch throwing monkey wrenches into the gears of commerce, 90,000 pages at a time.

– January 25, 2024

Inflation On Target in December

WILLIAM J. LUTHER
Director, Sound Money Project

New data from the Bureau of Economic Analysis shows that inflation has slowed significantly over the last year. Prices are now growing at a rate consistent with the Federal Reserve's inflation target.

The Personal Consumption Expenditures Price Index, which is the Fed's preferred measure of inflation, grew at an annualized rate of 4.2 percent in Q1-2023. PCEPI inflation averaged 2.5 percent over Q2 and Q3. In Q4, it was just 1.7 percent.

Core inflation, which excludes volatile food and energy prices and is thought to be a better predictor of future inflation, has also declined. Core PCEPI grew at an annualized rate of 5.0 percent in Q1-2023 and 3.7 percent in Q2. It has grown 2.0 percent over the last two quarters.

Figure 1. Monthly Headline and Core Inflation, January 2021 – December 2023

The Fed was late to recognize rising inflation in 2021 and slow to begin tightening 2022. But it eventually tightened monetary policy—and tight monetary policy has helped bring inflation back down to the Fed's 2-percent target. If anything, the Fed is now ahead of schedule. In December, the median FOMC member projected PCEPI inflation would be 2.4 percent in 2024 and 2.1 percent in 2025. Given the most recent data, I expect inflation will be around 2 percent over the next year.

Has the Fed Really Done Enough?

I expect some will remain concerned about inflation and call for the Fed to do more to bring inflation down. They might point to *annual* rates, which still look high. The PCEPI grew 2.6 percent over the last twelve months. Core PCEPI grew 2.9 percent. Both are clearly above the Fed's 2-percent target. There's no denying that! But one must remember that these rates are annual rates. They show us how much prices have risen over the last 12 months. And much of the increase in prices observed over the last 12 months occurred more than nine months ago. Inflation has been much lower, on average, over the last nine months. Indeed, inflation is now in line with the Fed's 2-percent target.

Of course, one might accept that inflation is back down to 2-percent and nonetheless worry that it will resurge in 2024. That is, after all, what the median FOMC member has projected. But I think such concerns are unfounded. At present, there's no good reason to worry that inflation will pick back up.

What Caused the High Inflation?

To see why I am not worried that inflation will pick back up, consider the major sources of inflation since January 2020:

- Pandemic-related supply disturbances
- Russia's invasion of Ukraine
- Loose monetary policy

The first two sources of inflation are what economists refer to as real shocks. They reduce our ability to produce goods and services, pushing prices up. However, they are also both temporary shocks. As supply constraints associated with the pandemic and Russia's invasion of Ukraine ease, our ability to produce goods and services recover. That puts downward pressure on prices. In the absence of another disruptive wave of COVID responses or a ratcheting up of military activity in Eastern Europe, we should not expect these sources to result in future high inflation.

Of course, most of the inflation observed since January 2020 cannot be attributed to real shocks. This should be obvious to anyone who recognizes that supply constraints have eased and yet prices remain well above their pre-pandemic trend. As shown in Figure 1, prices were 8.2 percentage points higher in December 2023 than they would have been had inflation averaged 2 percent since January 2020.

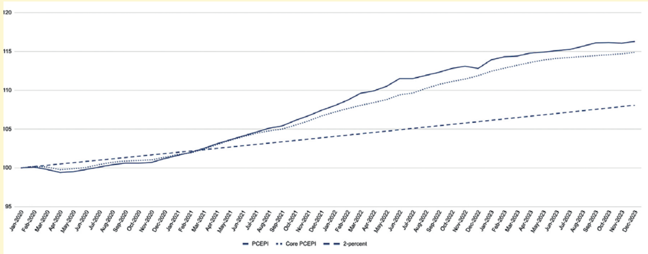


Figure 2. Price Level and 2-percent Growth Path, January 2020 – December 2023

Most of the inflation observed since January 2020 was due to loose monetary policy. The Fed accommodated large fiscal expenditures associated with the pandemic. Then, when nominal spending growth surged in the back half of 2021, it failed to tighten monetary policy promptly.

If monetary policy were loose today, one might reasonably worry that inflation will resurge in 2024. But it isn't. Monetary policy remains very tight. Interest rates are much higher than they were just prior to the pandemic. And the Fed is no longer accommodating expansionary fiscal policy. Indeed, its balance sheet has declined from $8.97 trillion in April 2022 to $7.67 trillion in January 2024.(That's still much bigger than it should be. But at least it is heading in the right direction.) So long as the Fed holds interest rates high and continues to shrink its balance sheet, inflation will fall.

Conclusion

There is a lot to lament about monetary policy over the last three years. The Fed should have recognized the surge in nominal spending growth in the Fall of 2021 and taken steps to offset it. Instead, it allowed prices to rise rapidly. More recently, however, it has kept monetary policy sufficiently restrictive to slow nominal spending growth, and bring inflation back down.

Is it possible that unforeseen shocks will push inflation back up? Sure. That's always a possibility. But the disinflationary trend is clear. And the forces that pushed inflation higher in 2021 and 2022 have since dissipated or reversed. Consequently, inflation is back on target.

– January 26, 2024

Milei Proves That Ideas Matter

G. PATRICK LYNCH
Contributor

Javier Milei arrived at the World Economic Forum last week and easily commanded the stage, rebuking Davos Man with wit and wisdom. While most of the attendees arrived in their private jets, Milei flew on a commercial flight sporting his signature sideburns and slightly mischievous smile. Along with his unique appearance another constant feature of Milei has been his dire warnings about the failures of collectivism. And frankly no other political leader at the event could say they know more about the dangers of collectivist political economies than the new Argentine leader.

If you've never watched one of Milei's speeches or television appearances, I strongly urge you to do so. The breadth of his knowledge about economic history and theory is remarkable and on evident display. You will be moved by the passion he brings to his discussions and presentations, and left wondering why other political leaders can't match his abilities and energy. Politicians aren't dumb, far from it, but their idealism tends to erode as they chase votes leaving their principles behind. Not Milei. He may not succeed in his mission to dismantle the sclerotic bureaucracy and dysfunctional central bank of Argentina, but he's been unwaveringly clear about what he believes and what he's trying to do. He's trying to save Argentina from almost a century of exploitative and destructive fiscal and monetary governance.

At Davos he began by presenting the case that Angus Deaton has made about the importance of market systems in promoting economic development since 1800. He also cited, by name, Israel Kirzner, and sounded almost like Ayn Rand when describing heroic entrepreneurs and parasitic state actors and bureaucrats. Milei rightly defended the importance of considering government failure and rejected neoclassical claims of pervasive market failures. It's almost as if the Mont Pelerin Society were his audience, not Davos.

The international media have tried to link Milei to Former President Donald Trump, right wing populism, and other anti-establishment politicians. There's little doubt Milei is taking on Argentina's elites, and Mr. Trump and his supporters are broadcasting a similar anti-elite message to anyone who will listen. It's also true that Trump and so many of his supporters (such as Heritage Foundation president Kevin Roberts, who also spoke at the World Economic Forum) have tried to embrace Milei with complimentary comments at Davos and on social media. Though the Trump camp might align themselves with Milei, the policy offerings from the economic nationalists bear little, if any, resemblance to the economic courage of the Argentine upstart. Rather than the thin gruel of economic grievance offered by American right-wing populists, Milei's policies are built on his vast knowledge of sound and successful, albeit politically unpopular, economic thinking.

Milei's ideas are a consistent set of interlocking principles based on an unqualified commitment to free markets in a classical liberal political economy. He, along with millions of Argentines, have experienced for years how significant government intervention severely damages an economy. After his victory on a platform of reversing that thievery and mismanagement, Milei must now confront the entrenched interests that have benefited from this vast web of crony capitalism. Milei will be lucky if he can simply stop the bleeding and redirect Argentina in a different direction.

Our GOP mouthpieces want to tell you that they are doing the same thing against the "deep state" who purportedly stole an election from President Trump in 2020 and are hurting Americans with elitist economic ideas about free trade and immigration. And America does face significant challenges, but the issues they cite are not the cause of our problems. The ideas of the economic nationalists in the US and elsewhere are hopelessly contradictory, politically expedient, short-term slogans to win an election and inflame passions. There is no underlying theory or consistent foundation to their hodgepodge of policies selected exclusively to please blue-collar voters in key electoral college states in 2024. If there is any underlying theory to these economic nationalist ideas it is collectivism, the exact danger that Milei himself identified in his speech.

Contrast Milei's intervention at Davos with Kevin Roberts, whose comments at the Davos summit constitute little more than a laundry list of issues that appear to have been bounced off of focus groups for key voters in swing states. At the top is immigration. Roberts said the next conservative president will "take on" elites on behalf of "the average American." He promises a Republican president would stand up to China, which he described as the "number one adversary to free people on planet Earth." Presumably more tariffs will dispatch the Chinese, similar to Trump's first term. It's interesting that while conservatives are no longer globalists on topics like Ukraine, they apparently are "planetary" in their concerns.

None of these issues are consistent with free markets and liberty oriented economic policies. Argentina has long had one of the most open immigration policies on the planet; it has struggled with free trade, which remains a key factor in producing growth, as much as some people wish to distort the facts about that.

Milei's popularity among young people throughout Latin America owes to the spark of hope he's provided to them in countries mired for years in the exact political interference that the economic nationalists wish to expand. Just because something polls well in Michigan and Ohio doesn't mean it's right, moral, or consistent with growth, freedom, and prosperity. Perhaps Milei's style and substance could rub off on Trump and the conservative populists. Instead of trying to claim him, they might endeavor to learn from him.

– January 31, 2024

Time for the Fed to Ease Up

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After a scare with January's Consumer Price Index (CPI) release, economists and market watchers are breathing a sigh of relief following the latest Personal Consumption Expenditures Price Index (PCEPI) data. Both headline and core inflation (excluding food and energy prices) inflation were 0.2 percent in December. Year-over-year, the figures were 2.6 percent and 2.9 percent, respectively. The overall impression is one of significant disinflationary trends.

These figures may even overstate the future inflation we can expect. For the past three months, headline inflation averaged 0.03 percent and core inflation averaged 0.13 percent. That's 0.36 percent and 1.56 percent annualized. Provided the recent data gives us a more accurate picture than single-month annualizations, we may start to undershoot the Fed's 2 percent inflation target before too long.

Real GDP growth is also improving, up to 3.11 percent year-over-year in Q42023 from 2.93 percent the previous quarter. The unemployment rate is holding steady at 3.7 percent. Fed tightening is bringing down inflation without causing major harms to income or jobs. It's too soon to celebrate a soft landing. Some economists anticipate a recession later this year. But, at least for now, the US economy looks strong.

Stronger growth and falling inflation should signal to the Fed it's time to consider easing monetary policy. The federal funds rate target range is currently 5.25 to 5.50 percent. Adjusting for inflation using the headline figures, we get a real rate of 2.65 to 2.9 percent. We must compare this to the natural rate of interest, which economists define as the short-term capital price consistent with maximum sustainable output and steady inflation. According to the New York Fed, the natural rate of interest is between 1.19 percent and 1.34 percent. This is a huge gap. Even if Fed economists have underestimated the natural rate of interest by half, monetary policy looks slightly tight. It looks very tight if the natural-rate figures are anywhere close to correct.

Monetary data also indicate Fed policy is restrictive. M2 was 2.31 percent lower in December 2023 than a year before. It's falling slower than previously, yet still, absolute declines in the money supply are very unusual.

Instead of simple-sum aggregates like M2, in which money supply components are weighted equally, we should also consider the Divisia aggregates, which weight components by liquidity. These are shrinking between 0.98 and 1.93 percent per year.

The Fed should strongly consider a rate cut at its next meeting. It's the Fed's job to use its policy instruments to manage aggregate demand. Nominal GDP, the cleanest measure of aggregate demand we have, is very close to its pre-pandemic growth path of 5 percent per year. Without monetary easing, it's possible the Fed will overcorrect its previous policy errors. This would cause the economy to dip below maximum sustainable output and employment. Nobody wants that, especially in an election year when partisan tensions are already high. Aggressive tightening was the right (albeit late) call for the past year. Now it's time for cautious easing.

– January 29, 2024

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