

AIER Research Reports

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Research Reports

AIER publishes over 100 articles per month that are distributed in digital form. Research Reports contains Business Conditions Monthly plus 8 of the most representative, chosen here for popularity, variety, and relevance. These articles are often reprinted in venues around the web, including Seeking Alpha, Intellectual Takeout, Mises Brasil, and dozens of other outlets. To read all of them, go to www.aier.org

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Contents

- 4 From the Senior Director of Research**
Peter C. Earle (Senior Director of Research)
- 6 Business Conditions Monthly July 2026**
Peter C. Earle (Senior Director of Research)
- 26 Mao’s ‘Great Leap’: Mass Starvation on *The Road to Serfdom***
Jeffery L. Degner (Research Fellow)
- 29 When Government Separates Choices from Consequences**
Donald J. Boudreaux (Associate Senior Research Fellow)
- 32 The Fed Finally Raised Rates, Now Comes the Hard Part**
Bryan P. Cutsinger (Fellow, Sound Money Project)
- 34 Debt Jubilees Only Change Who Pays**
Thomas Savidge (Research Fellow)
- 37 Made in (North) America: Canada Is Not Our Enemy**
David Hebert (Director of Economics and Economic Freedom)
- 40 Bond Markets are Losing Patience – And Putting Governments on Notice**
Peter C. Earle (Senior Director of Research)
- 43 The Great Repricing of the College Degree**
Joakim Book (Research Fellow)
- 46 Will Trump Accounts Make Every Kid a Millionaire?**
Paul Mueller (Director of Defending Freedom, Combatting Collectivism)

From the Senior Director of Research

Peter C. Earle
Senior Director of Research

The most consequential price in the US economy over the past 60 days or so is not that of oil, gold, compute tokens, nor the S&P 500. It's the price of time. And as elusive a concept as that is, there is a specific manifestation of it that periodically demands notice: the price of US Treasury bonds over time, collectively known as the yield curve.

After two decades in which policymakers and markets became accustomed to unusually cheap money, long-term US Treasury yields have returned to levels routinely encountered before the 2008 financial crisis. The 30-year bond recently crossed **5.6 percent**, its highest level since 2002. But more important than the absolute level is what has been happening all along the curve. Long rates have been rising even as investors have had to contemplate the future path of short-term rates. The Federal Reserve can exert considerable influence over the shortest portion of the yield curve (zero- to one-year instruments referred to as bills) but it does not, and cannot, simply dictate the yields on 10-, 20-, or 30-year instruments (notes and bonds). Longer-term bonds are delivering prices of their own, heedless of the Fed's machinations and the US Treasury Department's preferences.

Interest rates aren't merely numbers "set" by the Federal Reserve. Market rates coordinate the balance between consumption, savings, and investment; they also determine hurdle rates for investment, discount future cash flows. They convey information regarding inflation expectations, risk, scarcity, and competing claims on capital.

Those competing claims are becoming unusually large. The federal government must finance persistent deficits and refinance enormous quantities of maturing debt at the same time as private firms are undertaking capital expenditures on a scale rivaling the building of the railroads and the electrification of the nation. Treasury issuance, after all, does not occur in a vacuum: not just hyperscalers, but manufacturers, homebuyers, utilities, municipal and foreign governments, and every other type and stripe of borrower competes for capital. The yield required to induce a counterparty to supply it is the key mechanism by which the competition is resolved.

At precisely the moment that capital has become appreciably priced again, financial markets are contemplating one of the largest spending booms in history. To fund data centers, electrical transmission, semiconductor chips, cooling towers, networking systems, skilled labor, land, and more, enormous amounts of financing are being sought. An unintentional, near-perfect experiment in capital allocation is taking place: projects that appear attractive under near-zero rates may, and probably will, look very different when their opportunity cost is a Treasury security yielding over **5 percent**.

Indeed, it's likely that AI-related borrowing is one of several contributors to the upward pressure on yields.

A prospective investment does not simply have to promise a positive return; it must offer enough of a return above the risk-free alternative to compensate investors for uncertainty. In the early weeks of the COVID pandemic, the 10-year US Treasury note yield briefly fell to **0.318 percent**. The implications of so low a yield were nothing less than extraordinary: a security tying up capital for a decade was offering essentially no compensation for time, and likely a loss, after even marginal levels of inflation. At those rates, virtually any investment promising a positive, even distant, cash flow would look attractive. If the idea that virtually any business plan would look viable against such low rates is disconcerting, consider the flip side of that condition as well: investors seeking higher returns were pushed toward progressively riskier assets. The signal was not simply that capital was cheap; it was that, for any practical purpose, time itself had stopped carrying an economic price.

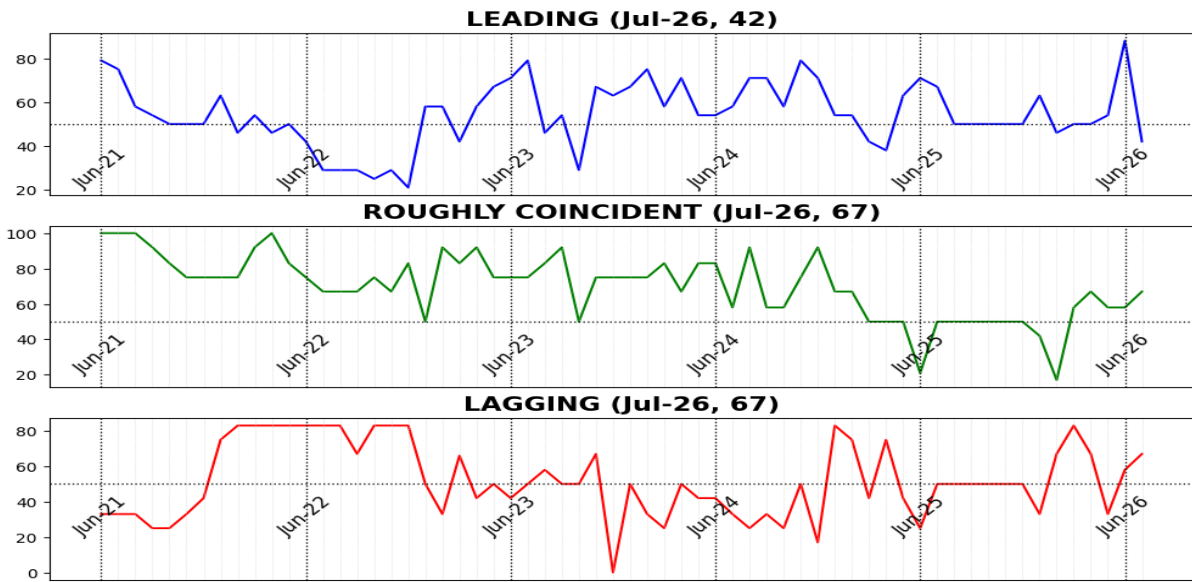
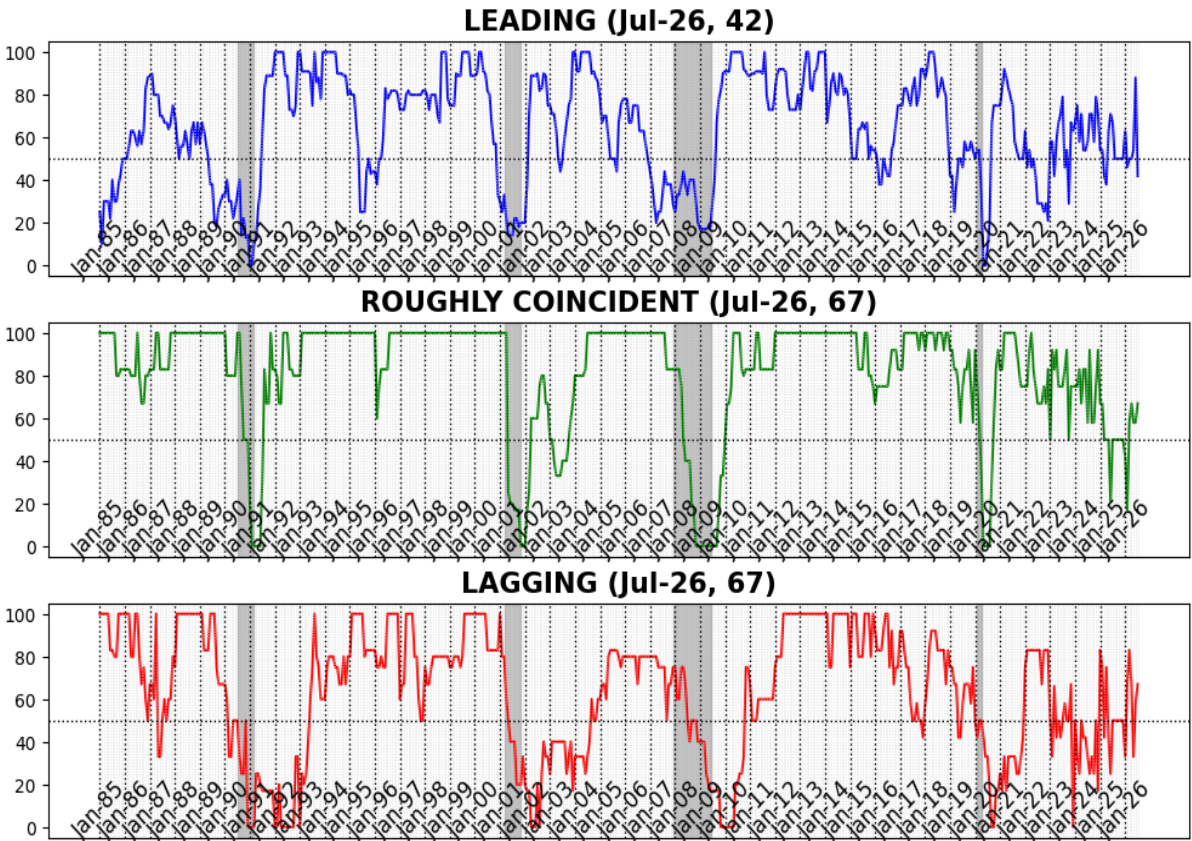
The current adjustment doesn't require an investment bust, but it will require discrimination. Some AI projects will comfortably clear the new, higher hurdle rates. Others will not. The same bifurcation will emerge in other areas: leveraged acquisitions, commercial real estate, speculative start-ups, new factories. Higher prices for capital influence not only how much investment takes place, but which investments are selected. "Financial tightening" may aptly be described as a more discerning price system.

Mortgage rates, home equity loans, auto financing, credit cards, and ultimately employment and wages all transmit the same signal. The price of capital is not an abstraction, and higher rates of interest are not an economic affliction requiring a cure. Attempts to suppress them without addressing the underlying conditions (including inflation, borrowing, fiscal imbalances, and scarcity) will only suppress the information those prices convey.

For decades, economic arguments proceeded as if capital were free, or almost free. That assumption is disappearing, but the ease with which it became an assumption is essentially proportional to the pain with which it will reassert. A meaningful price of capital will expose malinvestment. It will also constrain government spending, reward savers, make valuation models more relevant, and force choices that unjustifiably cheap money permitted us to postpone. Interest rates are not becoming, but are rather returning to, prices that economic engagement must take account of.

Peter C. Earle, Ph.D
Managing Editor, *AIER Research Reports*

Business Conditions Monthly July 2026



Peter C. Earle
Senior Director of Research

The July 2026 AIER Business Conditions Monthly (BCM) shows a sharp reversal in forward-looking conditions, even as measures of current and trailing activity improved. The Leading Indicator fell to **42** from **88** in June, with weakness concentrated in housing, retail activity, transportation, capital-goods orders, margin borrowing, and the yield-spread signal. The Roughly Coincident Indicator rose to **67** from **58**, suggesting that current economic activity broadened modestly across sales, income, production, and payroll employment. The Lagging Indicator also increased to **67** from **58** as unemployment duration, commercial and industrial lending, inventories, and nonresidential construction contributed positively.

LEADING INDICATOR (42)

The Leading Indicator dropped sharply to **42**, with four of twelve components improving, two unchanged unchanged, and six declining.

The positive components were concentrated in consumer expectations, initial claims, consumer-goods orders, and equity prices. The University of Michigan Consumer Expectations Index increased **9.3 percent**, rising from 50.7 to 55.4 and extending the improvement recorded in June. US Initial Jobless Claims SA declined **7.8 percent**, from 217,000 to 200,000, and contributed positively because lower claims indicate improving labor-market conditions. Conference Board US Leading Index Manufacturers’ New Orders Consumer Goods and Materials rose **0.5 percent**, while the Conference Board US Leading Index Stock Prices 500 Common Stocks increased **0.4 percent**.

Two measures were unchanged. US Average Weekly Hours All Employees Manufacturing SA remained at 40.4 hours, while the Inventory-to-Sales Ratio Total Business held at 1.3. Both therefore contributed neutrally to the July reading.

Weakness was considerably more widespread among the remaining components. Conference Board US Manufacturers New Orders Nondefense Capital Goods Ex Aircraft declined **0.4 percent**, indicating some softening in a key measure of prospective business investment. US New Privately Owned Housing Units Started by Structure Total SAAR fell **9.0 percent**, reversing part of June’s substantial increase. Adjusted Retail and Food Services Sales Total SA declined **0.5 percent**, while United States Heavy Trucks Sales SAAR dropped **9.5 percent**.

Financial measures outside equity prices were also unfavorable. Debit Balances in Customers’ Securities Margin Accounts declined **5.6 percent**. The 1-Year to 10-Year US Treasury Yield Spread increased **44.4 percent**; under the BCM’s inverted treatment of that measure, the increase was scored negatively.

July’s leading data represent a pronounced loss of forward-looking breadth. The decline from **88** to **42** reflects more than the normalization of June’s unusually strong reading: six components moved into the negative column, compared with only four that improved. Stronger consumer expectations, lower initial claims, firmer consumer-goods orders, and rising equity prices provided some support, but they were insufficient to offset deterioration in housing starts, retail sales, heavy truck sales, capital-goods orders, margin debt, and the yield-spread signal. One weak month does not establish a sustained downturn, but the July reading substantially tempers the optimism generated by June’s broad advance.

ROUGHLY COINCIDENT INDICATOR (67)

The Roughly Coincident Indicator rose to **67** from **58**, with four of six components improving and two declining.

Measures of sales, income, production, and employment advanced during the month. Conference Board Coincident Manufacturing and Trade Sales increased **0.2 percent**, extending June’s improvement. Conference Board Coincident Personal Income Less Transfer Payments also rose **0.2 percent**. US Industrial Production SA increased **0.2 percent**, while US Employees on Nonfarm Payrolls Total SA edged **0.01 percent** higher. Although the payroll increase was slight, it remained positive under the BCM scoring methodology.

The weaker components were consumer assessments of present conditions and labor-force participation. Conference Board Consumer Confidence Present Situation SA declined **3.5 percent**, falling from 118.5 to 114.4. The US Labor Force Participation Rate SA slipped from **61.5 percent** to **61.4 percent**, a decline of approximately **0.2 percent**.

Overall, the rise in the Roughly Coincident Indicator from **58** to **67** points to a modest broadening in current economic activity. Manufacturing and trade sales, income, industrial production, and payroll employment all moved higher, giving the coincident reading greater breadth than in June. At the same time, the decline in present-situation confidence was comparatively pronounced, and the further reduction in labor-force participation points to continuing limitations in the labor market. The current-conditions picture is therefore constructive but uneven: hard measures of activity improved, while household assessments and participation weakened.

LAGGING INDICATOR (67)

The Lagging Indicator rebounded to **67** from **58**, with four of six components improving and two declining.

Several credit, labor-market, inventory, and construction measures contributed positively. Conference Board US Lagging Average Duration of Unemployment declined **2.4 percent**, falling from 25.5 weeks to 24.9 weeks, and contributed positively because a shorter duration of unemployment represents an improvement. Conference Board US Lagging Commercial and Industrial Loans increased approximately **0.1 percent**, reversing the decline recorded in June.

US Manufacturing and Trade Inventories Total SA rose **0.8 percent**, while Census Bureau US Private Construction Spending Nonresidential SA increased **0.4 percent**. Together, those movements suggest continued expansion in inventories and nonresidential investment, although neither provides a timely indication of future momentum.

Two components restrained the index. US CPI Urban Consumers Less Food and Energy Year over Year NSA declined from **2.59 percent** to **2.48 percent**, a **4.2 percent** decrease under the BCM’s month-to-month scoring calculation. US Commercial Paper Placed Top 30 Day Yield fell **1.1 percent**, from **3.72 percent** to **3.68 percent**.

The increase in the Lagging Indicator from **58** to **67** indicates that trailing conditions became somewhat more broadly favorable in July. A decline in average unemployment duration, renewed growth in commercial and industrial lending, higher inventories, and stronger nonresidential construction spending outweighed the negative contributions from the core inflation measure and commercial paper yields. The result is a firmer lagging picture than in June, although the improvement reflects developments that characterize past or established activity rather than providing evidence of stronger growth ahead.

July’s BCM results therefore present a sharply divided configuration. Forward-looking conditions weakened considerably, with the Leading Indicator falling from **88** to **42** as housing, retail activity, transportation, business investment, margin borrowing, and the yield-spread signal deteriorated. Current conditions improved: the Roughly Coincident Indicator rose from **58** to **67** as gains in sales, income, production, and payroll employment outweighed weaker present-situation confidence and labor-force participation. Lagging conditions also strengthened, with the index increasing from **58** to **67**.

Taken together, the July readings describe an economy in which current and trailing activity remained relatively firm even as the forward-looking signal lost substantial momentum. That divergence warrants caution. The improvement in coincident and lagging measures suggests that the economy continued to expand during July, but the decline in the Leading Indicator raises questions about whether that strength will persist. Confirmation from subsequent months will be necessary to determine whether July’s leading weakness represents a temporary reversal following June’s unusually strong reading or the beginning of a more durable slowdown.

DISCUSSION, AUGUST— SEPTEMBER 2026

August 2026 inflation data were notably firmer than July’s, with renewed energy and commodity pressures appearing at both the consumer and producer levels. Headline CPI rose **0.40 percent**, up sharply from **0.07 percent** in July, as gasoline prices jumped **3.9 percent**, while core CPI accelerated to **0.29 percent** from **0.22 percent**. Despite the monthly pickup, year-over-year core inflation eased to **2.4 percent**, its lowest rate since March 2021, and inflation breadth improved modestly: an estimated **52 percent** of PCE components were rising faster than **3 percent** from a year earlier, down from **54 percent** in July. Goods inflation remained relatively contained, with core goods prices up just **0.1 percent** and declines in computer software, medical commodities, and vehicle insurance providing evidence of continuing disinflation, but services strengthened as lodging jumped **2.4 percent** and airfares rose **2.7 percent**. Producer prices reinforced the less benign near-term picture. Headline PPI increased **0.4 percent** and **5.4 percent** from a year earlier, while core PPI rose **0.2 percent** and **4.6 percent**, respectively, as higher oil and commodity prices pushed transportation and warehousing costs up **2.3 percent** and trucking costs **1.9 percent**. More importantly, several components feeding into the PCE deflator were unexpectedly strong, including hospital services and airfares, pointing to a firmer August core PCE reading even after methodological revisions that should reduce measured inflation somewhat. Taken together, the August data show that underlying disinflation has not disappeared, but the renewed pressure from energy, freight, goods inputs, and selected services suggests that the path back toward price stability remains uneven and increasingly exposed to commodity and supply-chain shocks.

Meanwhile, the US labor market is settling into an unusual equilibrium: companies are doing relatively

little firing, workers are increasingly reluctant to leave voluntarily, and hiring remains concentrated in a handful of industries. July job openings recovered only slightly to 7.27 million after June’s sharp decline, leaving 1.05 vacancies for every unemployed worker, while the quits rate slipped to **1.9 percent** and layoffs fell to **1.0 percent**. ADP’s August report told a similar story, with private employers adding only 38,000 jobs, the weakest increase since January. Pay growth was unchanged at **4.4 percent** for workers remaining in their jobs and slowed to **7.3 percent** for those switching employers, another indication that the wage premium associated with labor-market mobility is narrowing.

Against that subdued backdrop, the government’s August nonfarm payroll number was strikingly strong. Nonfarm employment increased 162,000 after a revised 21,000 gain in July, pushing the three-month average to 71,000, still only about half its spring pace. The headline strength also deserves qualification. Leisure and hospitality added 62,000 positions, including 59,000 at restaurants and bars, following unusually large World Cup-related employment swings earlier in the summer; an exceptionally mild August seasonal adjustment amplified the rebound. Construction added 22,000 jobs and manufacturing 16,000, consistent with strong defense and data-center investment, while information lost 23,000 positions and financial activities shed 11,000. The household survey recorded a 569,000 increase in employment, but roughly 350,000 came from workers aged 55 and older, while prime-age employment was essentially unchanged. A 683,000 expansion in the labor force raised participation to **61.6 percent** and kept unemployment at **4.1 percent**. The broader picture is therefore less a return to vigorous hiring than a stabilization after the early-summer deterioration: layoffs remain scarce and some capital-intensive sectors are competing for workers, but openings, quits, ADP payrolls, and the underlying pace of job creation all describe a labor market with substantially less churn and bargaining power than prevailed earlier in the expansion.

Factory output is holding up better than the demand indicators behind it, while service businesses are managing the opposite feat: stronger demand and activity with almost no corresponding appetite for additional workers. The manufacturing PMI slipped from 55.6 to 54.6 in August, its eighth straight month in expansion territory, but the internals were less encouraging. New orders fell three points to 53.7 and backlogs dropped to 51.8, while production gave back just 0.2 point of July’s 6.3-point jump. That gap cannot persist indefinitely. For now, customer inventories

remain lean enough to keep factories busy, although obtaining the inputs needed to do so is becoming more difficult. Supplier delivery times lengthened again, electronics and other components became scarcer, and prices paid held at 71.1 as higher petroleum, metals, and tariff-related costs worked their way through supply chains. Employment slipped to 51.2, and among the six largest manufacturing industries only transportation equipment reported an increase in hiring.

Services are telling a different, and perhaps more interesting, story. The PMI rose from 54.1 to 55.4, with business activity, new orders, and backlogs all strengthening. Employment barely budged, however, moving from 47.4 to 47.8 and remaining in contraction. Firms are finding ways to accommodate more business without adding many workers, and the details suggest AI investment is increasingly part of that process. GPUs joined the list of commodities in short supply, memory remained scarce and expensive, and respondents reported substantial investment in computing capacity, power generation, and transmission. None of that comes cheaply. Services prices paid climbed from 70.3 to 72.6, with 15 industries reporting higher costs and not one reporting a decline. The manufacturing pipeline is thinning while factories continue working through existing demand; services, meanwhile, are expanding with remarkably little hiring. What both have in common is increasingly expensive physical capacity, whether that means fuel, metals, electronics, computing hardware, or the electricity required to run it.

Rising prices are again showing up in measures of confidence although the underlying evidence on spending and employment is considerably less alarming. University of Michigan consumer sentiment fell from 51.7 to 47.8 in early September, more than **13 percent** below its year-earlier level, with expectations dropping particularly sharply to 45.8. The most obvious culprit is inflation. Year-ahead expectations jumped from 4.0 to **4.6 percent** as fuel prices rebounded, while longer-term expectations edged up to **3.4 percent**. Yet consumers became slightly less worried about losing their jobs, and real spending was still growing at better than two percent year over year in July. The familiar gap between what households say and what they do therefore remains unusually wide. Small businesses have a more tangible reason for becoming cautious. The NFIB optimism index fell 1.1 points to 98.7 in August as actual sales weakened, profit trends deteriorated, and expectations for business conditions declined. Hiring plans eased to a net **17 percent** of firms and planned capital spending slipped to **25 percent**, although both remain reasonably firm by recent standards. Inflation

also moved up the list of owners’ concerns, with higher metals, petroleum, and other input costs increasingly squeezing margins. There is little here to suggest that domestic demand has suddenly broken. What has changed is the environment surrounding it: households are again noticing higher prices, while businesses are confronting those same pressures from the other side of the transaction, through higher costs and weaker realized sales.

But having said that, whatever caution consumers are expressing in surveys has yet to reach the cash register. Retail sales rose **1.2 percent** in August after falling **0.5 percent** in July, with higher gasoline prices accounting for about a quarter-point of the increase and autos providing another modest boost. More tellingly, control-group sales, which strip out gasoline, autos, building materials, and restaurants, surged **1.4 percent** against expectations of only **0.5 percent**. Online spending rebounded **2.6 percent** as the distortions surrounding Amazon’s earlier-than-usual Prime Day faded, while back-to-school purchases helped lift electronics and sporting goods sales. Spending at restaurants and bars rose another **1.2 percent**. On present trends, real consumption appears capable of growing slightly above **3 percent** in the third quarter, not far below the second quarter’s **3.4 percent** pace. That is difficult to reconcile with survey measures suggesting a consumer in retreat.

The weakness is instead concentrated where financing costs matter most. Housing starts fell another **2.6 percent** in August to a 1.275 million annual rate following July’s 9-percent decline. Single-family starts bounced **7.6 percent**, but multifamily construction dropped nearly **22 percent**, and permits fell in both categories. The latter is more consequential for the months ahead: permits declined **1.8 percent** for single-family homes and **4.3 percent** for multifamily projects as mortgage rates, labor shortages, material costs, and poor affordability continued to weigh on builders. The consumption picture is thus stronger than the confidence data imply, but hardly uniform. Households remain willing to spend on goods, restaurants, and discretionary purchases while recoiling from the largest and most credit-dependent purchase most of them will ever make. Housing is increasingly where the effects of higher rates are visible, rather than in consumption generally.

Business investment is running well ahead of the factories that should, at least in principle, be registering some of it. Industrial production went nowhere in August, and the headline would have been negative without a **1.8 percent** increase in utilities

output as warmer weather lifted electricity demand. Manufacturing fell **0.3 percent**, its first decline this year, with durable-goods production down **0.5 percent** and capacity utilization slipping to **75.7 percent**. Construction supplies fell **0.7 percent**, while defense and space equipment declined **1.2 percent**. None of that sits especially comfortably beside the increasingly familiar account of AI, data centers, defense spending, and related capital investment driving US industrial activity.

But the investment data themselves remain difficult to argue with. Durable-goods orders were flat overall, yet core capital-goods orders, excluding defense and aircraft, jumped **1.6 percent** after July was revised substantially higher. Primary metals, machinery, and electrical equipment led the advance. Compared with a year ago, orders are up **20.1 percent** for primary metals, **16.5 percent** for computers and electronics, and **15.1 percent** for machinery. More important for current GDP, core capital-goods shipments rose **0.6 percent** and are running at a **14.1 percent** annualized pace so far in the third quarter. There is a genuine disconnect here, but not yet a contradiction. Companies are ordering and receiving equipment at rates consistent with a vigorous investment cycle even as domestic factory output stumbled in August. One month can be noise. If the divergence persists, though, it will become worth asking how much of the capital-spending boom is reaching US manufacturing, where it is showing up, and whether an investment cycle increasingly identified with AI is as broad as the aggregate numbers make it appear.

September’s 25-basis-point Fed funds hike did more than raise the target to 3.75 to **4.00 percent**. It revealed a Fed that has become considerably less tolerant of inflation remaining above **2 percent**. Sixteen FOMC participants now expect at least one more increase this year, four expect another 50 basis points, and the median path shows no reversal in 2027. That is a fairly aggressive policy path for projections that otherwise changed very little. Growth was nudged up to **2.3 percent** this year and **2.4 percent** next year, unemployment was marked down to **4.1 percent** through 2028, and the inflation forecasts moved only slightly higher, to **3.7 percent** for headline PCE and **3.4 percent** for core. Warsh described an economy operating near full employment, with insufficient progress on inflation and new geopolitical risks layered on top. The more important clue may be buried in the statement itself: policy is now intended to produce

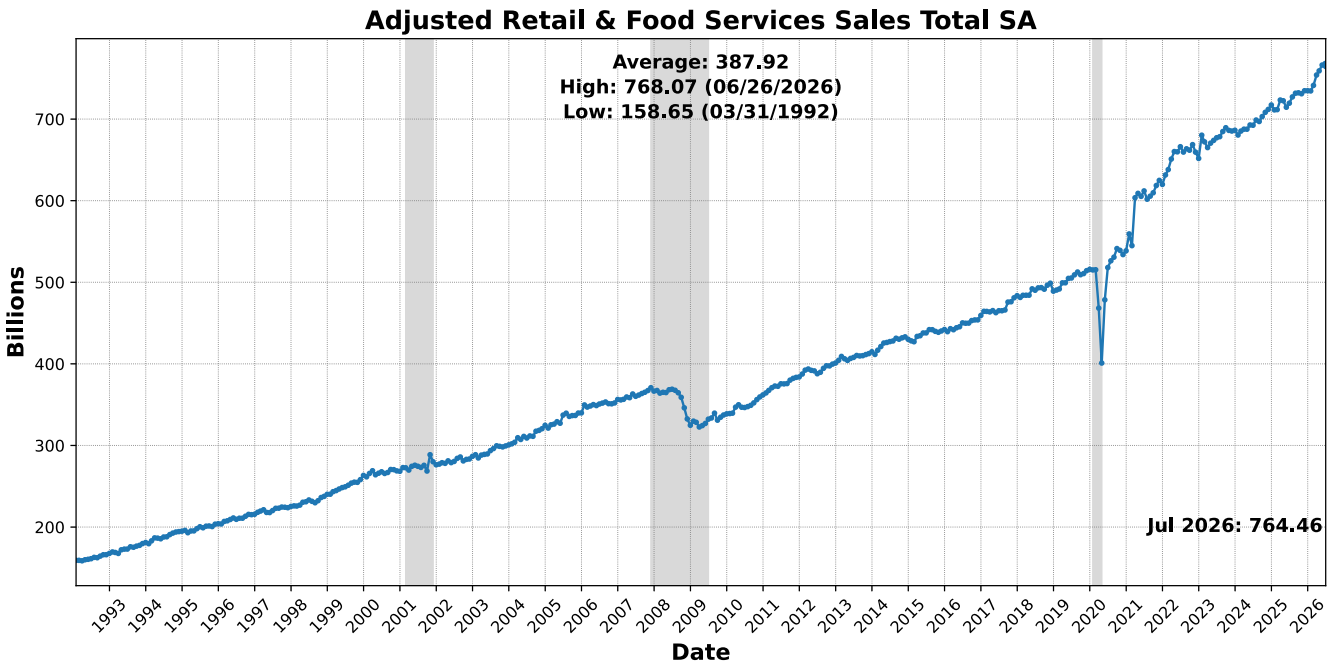
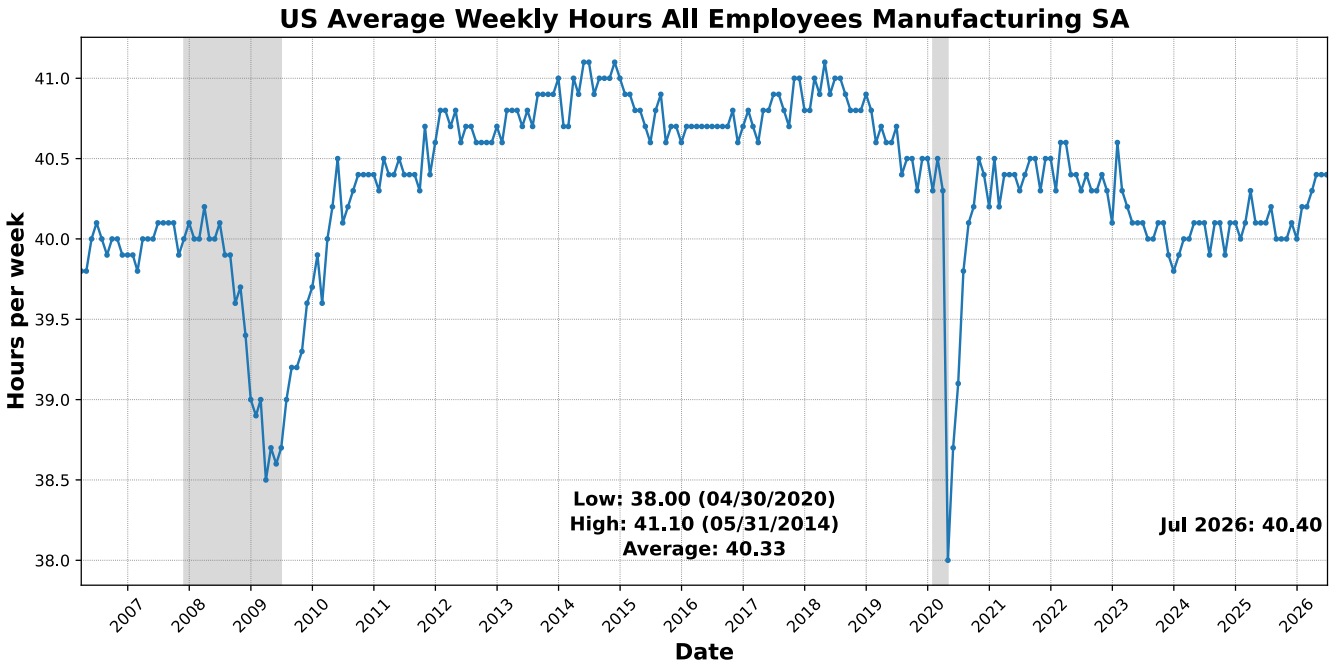
a “timelier return” to **2 percent**. That is a different standard from accepting a slow glide downward while protecting employment. And it comes at a peculiar moment, with long Treasury yields already doing some of the Fed’s work by raising borrowing costs well beyond the overnight market.

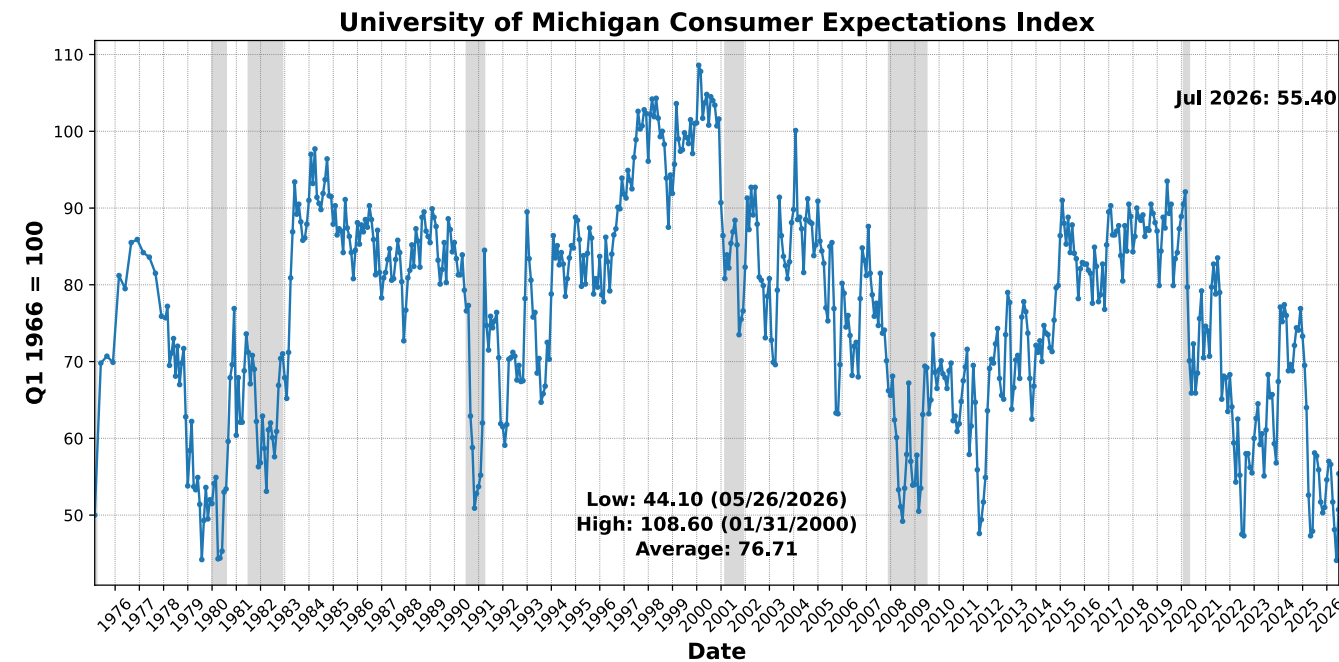
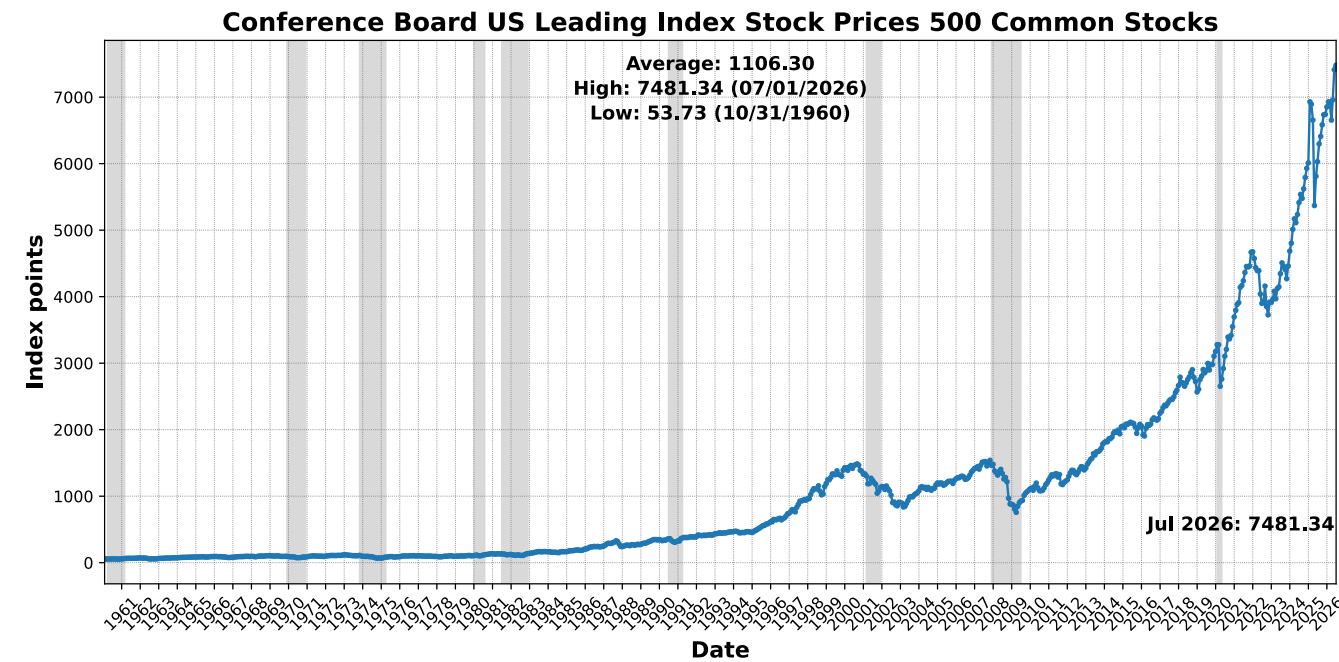
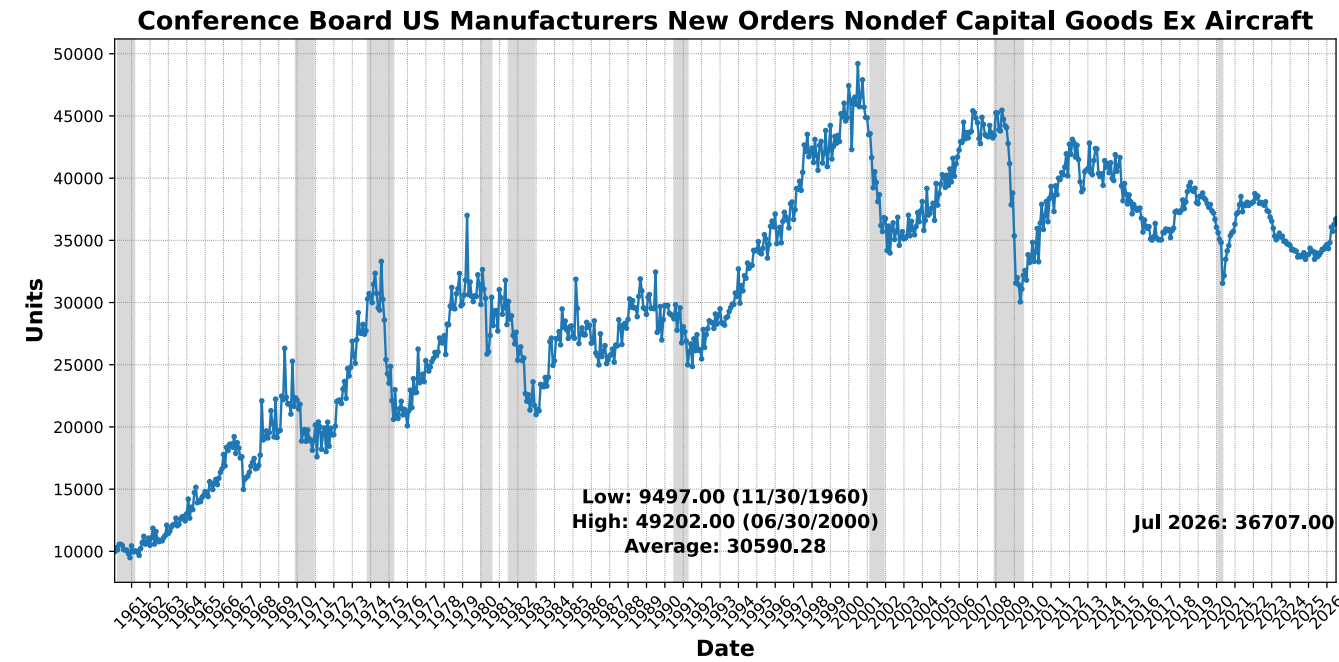
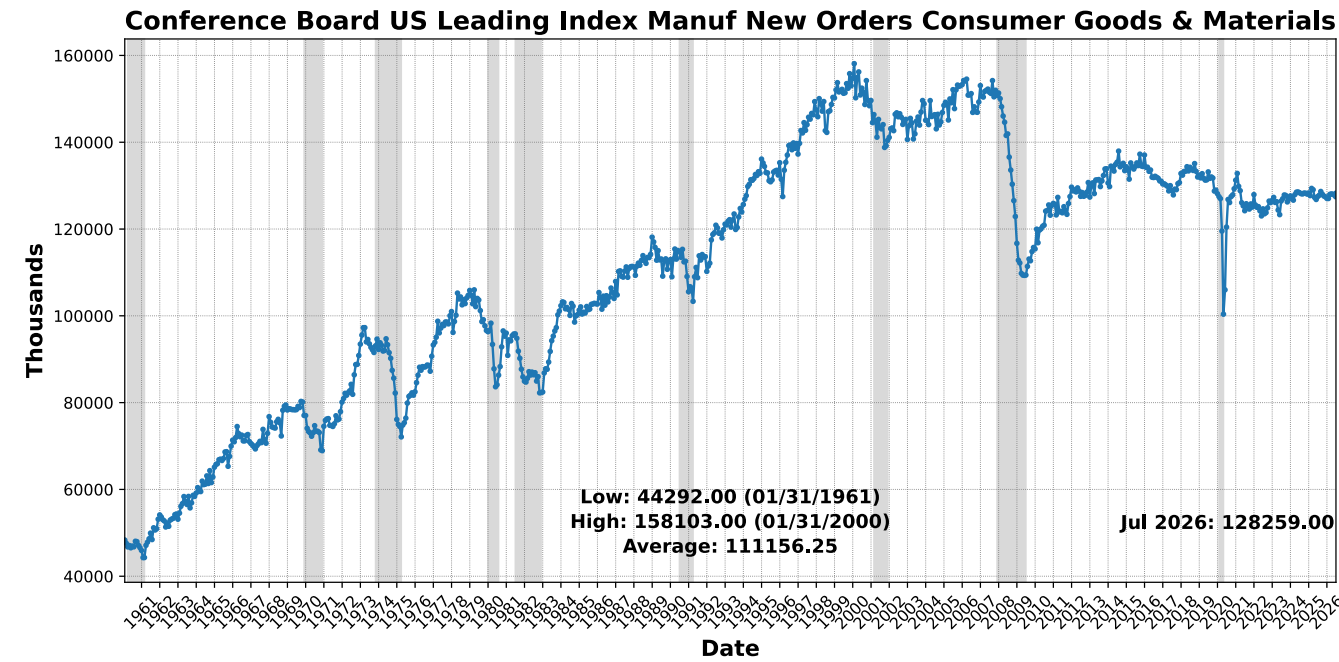
The Beige Book makes clear why that choice is not straightforward. There is plenty of strength in the economy, but it is concentrated in some unusual places. Manufacturing improved across most districts, defense activity is strong, data-center construction continues at a remarkable pace, and higher-income households are still spending freely, including on travel. Skilled labor in those areas remains scarce and expensive. Energy, freight, metals, petrochemicals, healthcare, and insurance costs are also moving higher. Move away from those sectors, though, and the picture changes. Retail and hospitality hiring is softer, automobile demand remains weak, and businesses selling directly to consumers are finding it harder to pass higher costs along. Margins get squeezed in the process. AI further muddies the labor picture because it is creating jobs and eliminating the need for them at the same time, depending on the firm and industry. Ten of the twelve Fed districts are still growing, so this is not an economy grinding to a halt. It is one in which the hottest areas increasingly revolve around capital spending, defense, technology infrastructure, and affluent consumers, while other businesses encounter customers who are becoming much more careful about price.

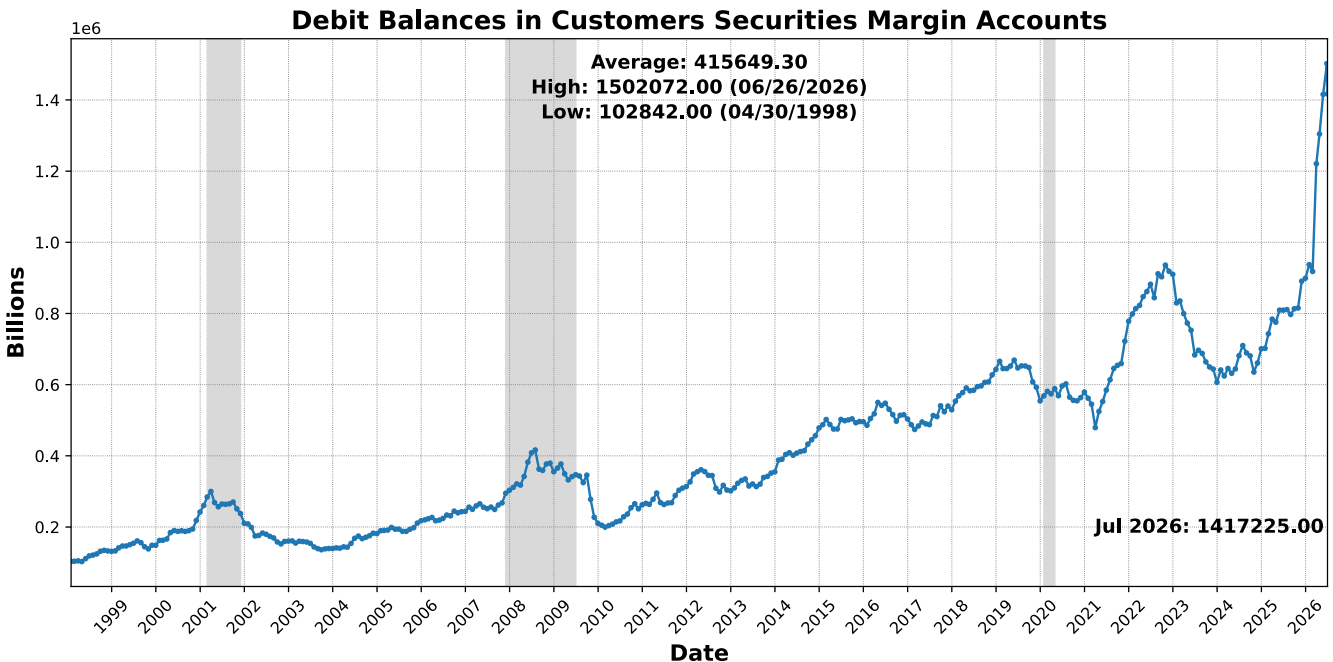
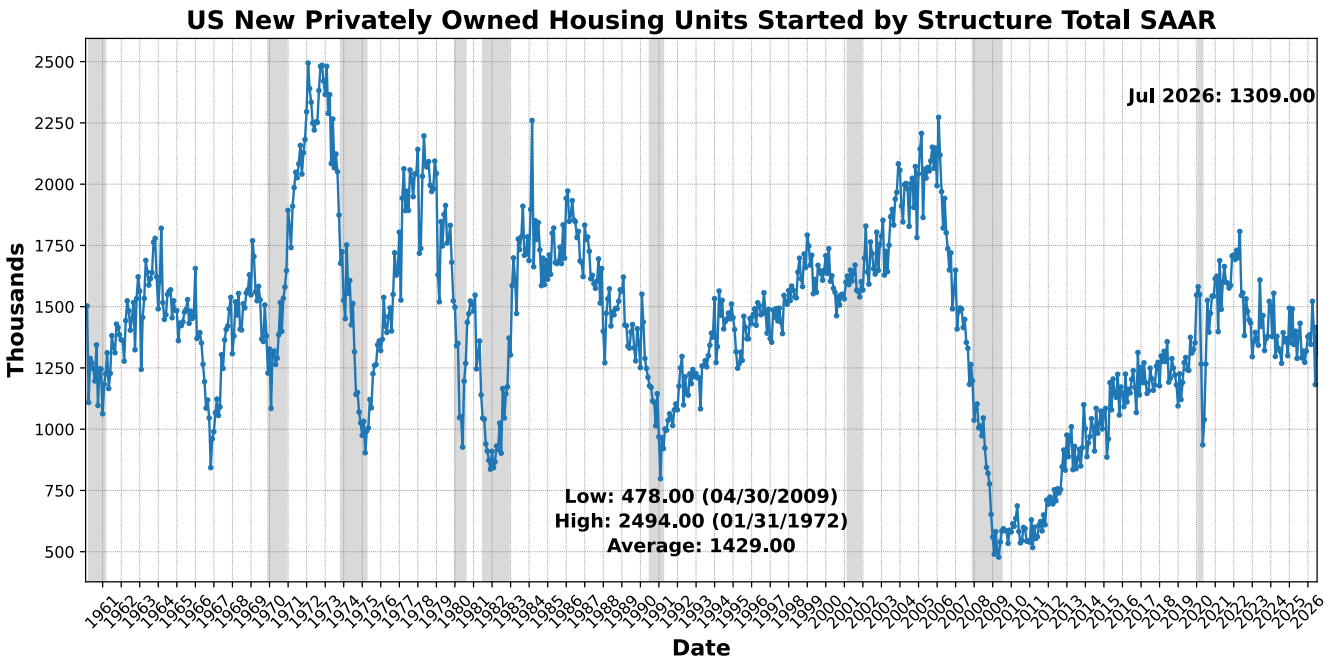
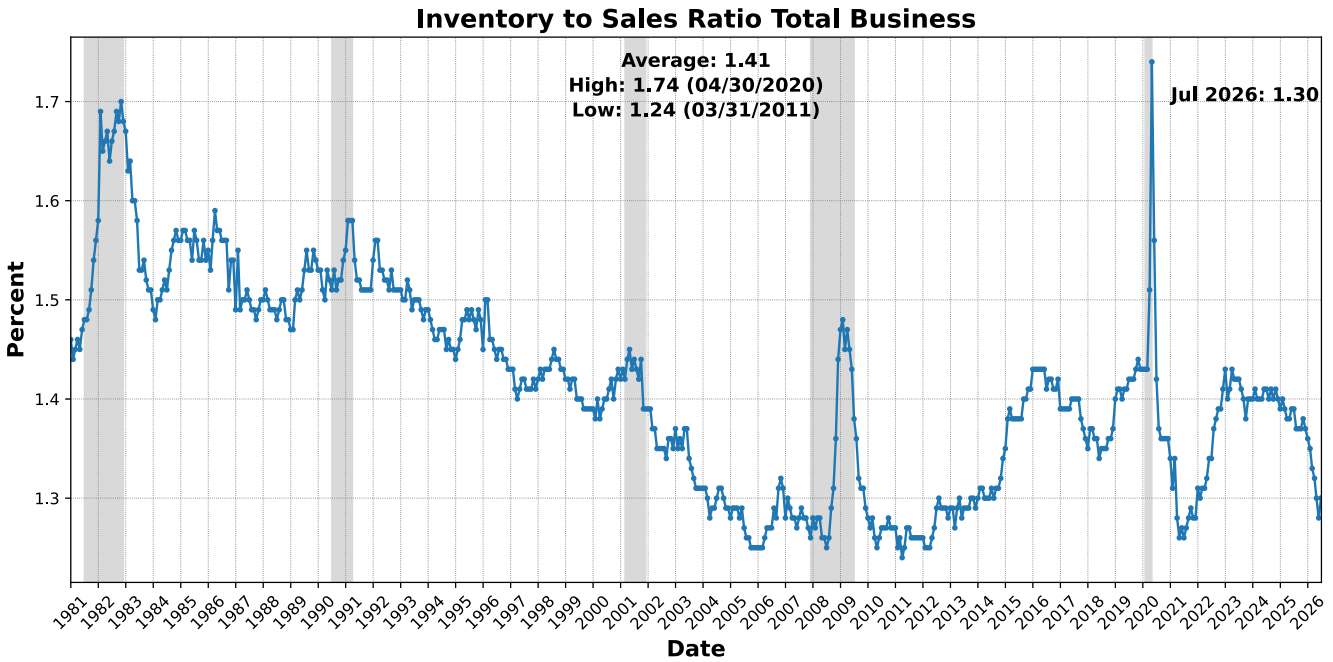
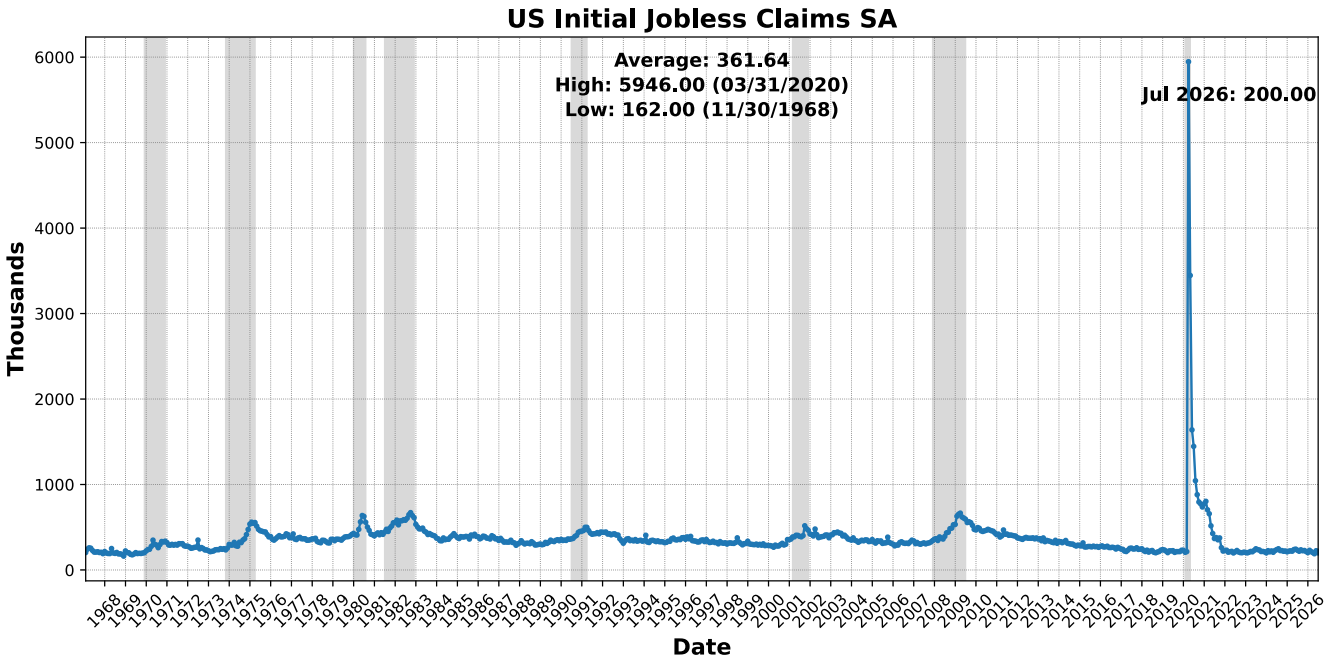
That same split runs through nearly every August indicator. Consumers spent heavily despite telling surveyors they felt miserable: control-group retail sales jumped **1.4 percent** and third-quarter consumption is tracking around **3 percent**, while housing continues to buckle under mortgage rates and poor affordability. The labor market produced a surprisingly large payroll gain and unemployment remained at **4.1 percent**, but workers are quitting less, openings remain subdued, ADP hiring is weak, and prime-age employment went essentially nowhere. Factories are still busy even as new orders and backlogs soften. Businesses, meanwhile, continue ordering and taking delivery of capital equipment at rates consistent with a substantial investment boom, although manufacturing output fell in August. Inflation has not so much returned as migrated. Some earlier pressures have faded while gasoline, transportation, metals, electricity, and selected services have taken their place.

The US economy is still expanding, and in several places expanding rapidly, but the sources of that growth are becoming narrower and more capital-intensive. That matters for economic policies broadly, but considerably more for monetary policy. Indeed: higher rates are a blunt instrument against an energy shock, a shortage of skilled tradesmen, and a rush to build data centers. They are considerably more effective against housing, credit-dependent businesses, and households that were already feeling the squeeze.

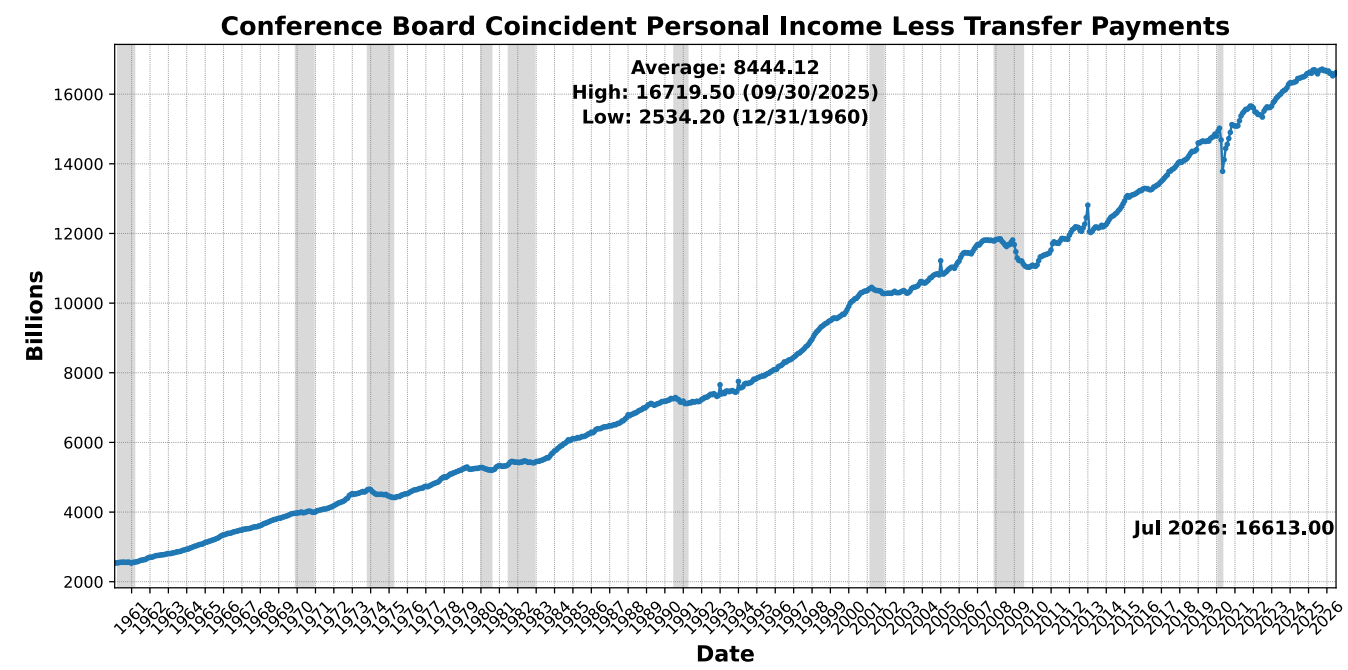
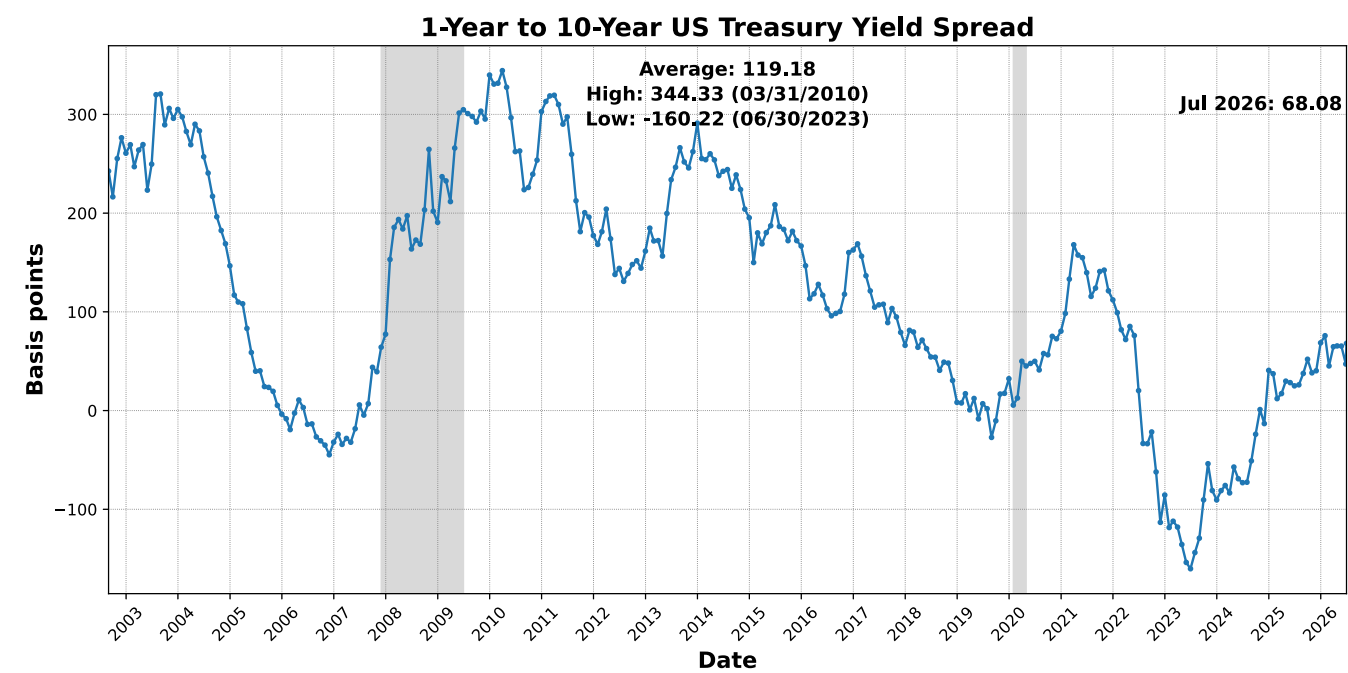
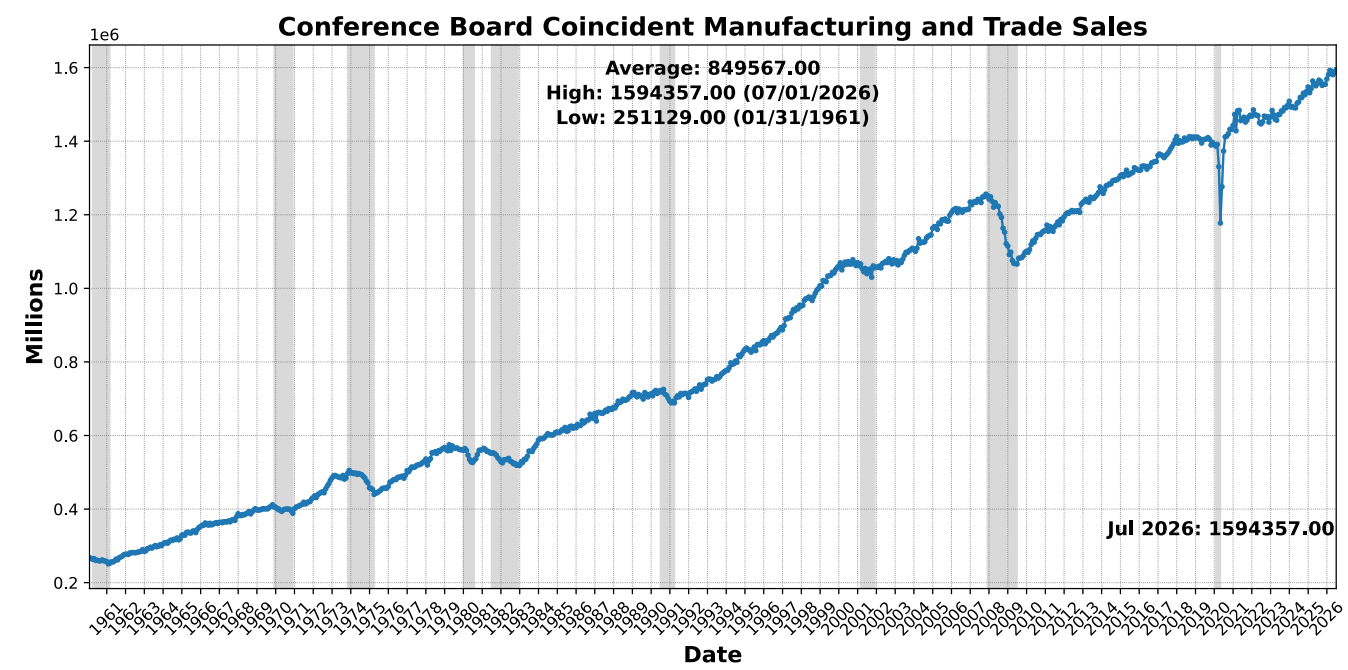
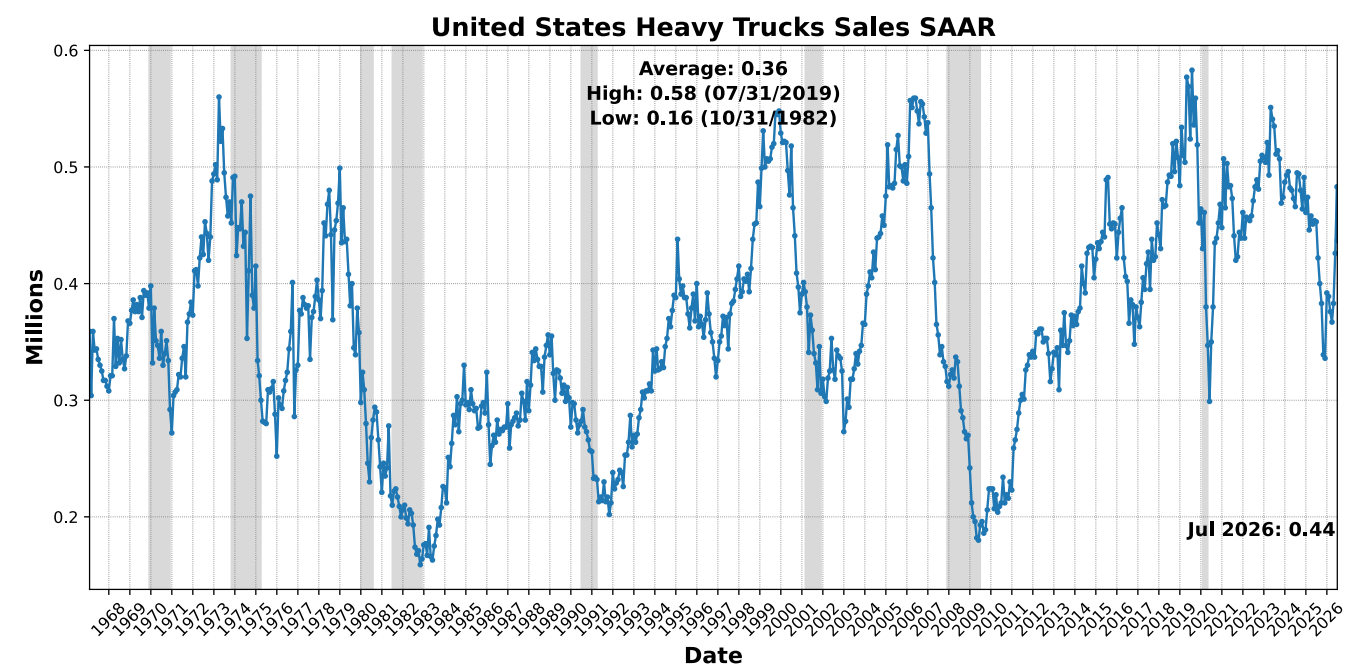
LEADING INDICATORS

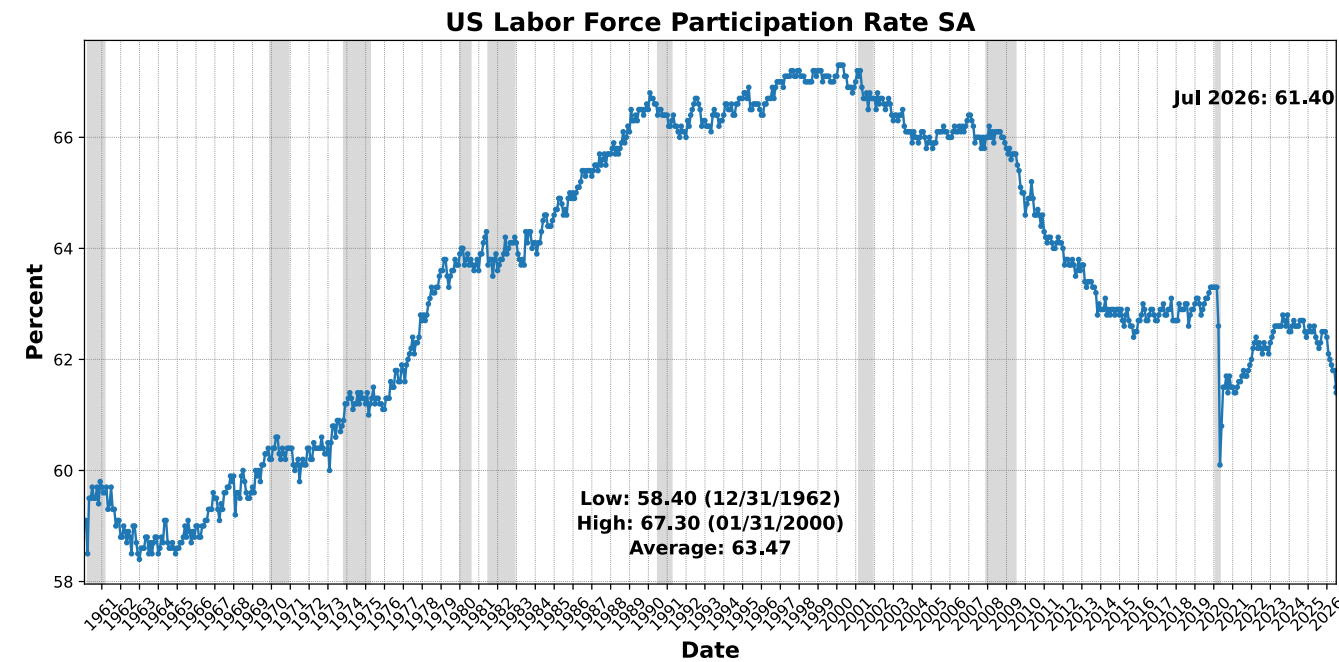
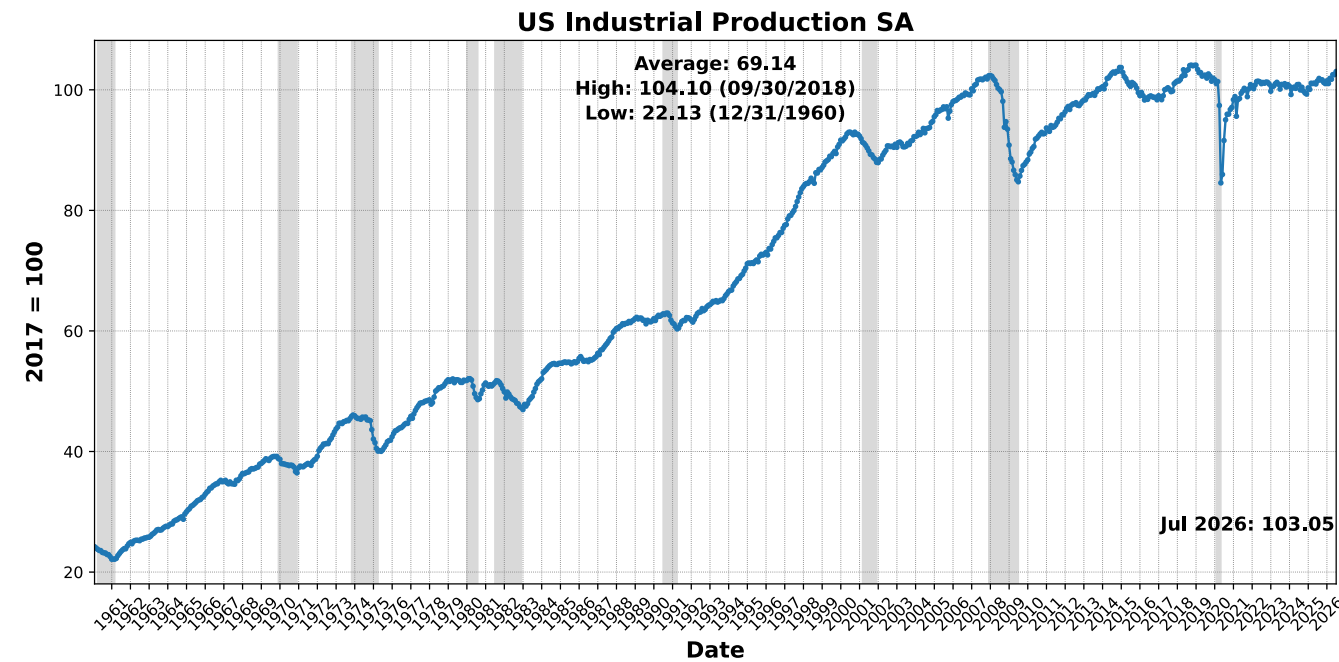
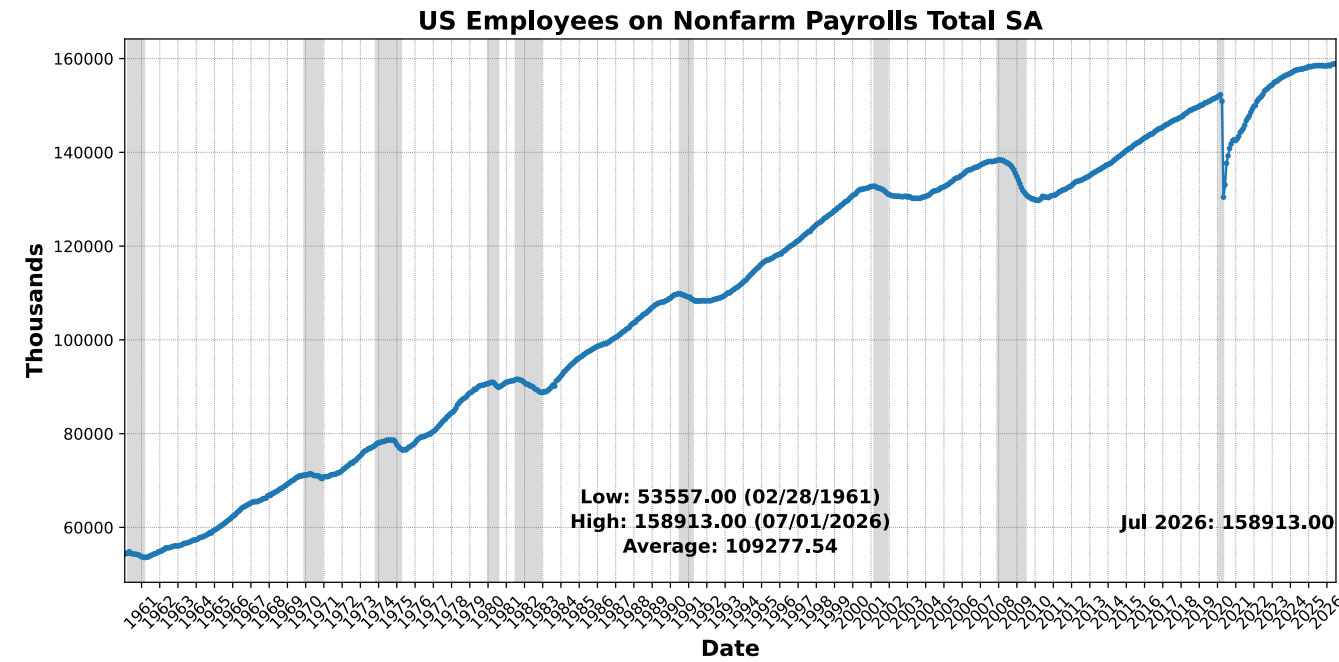
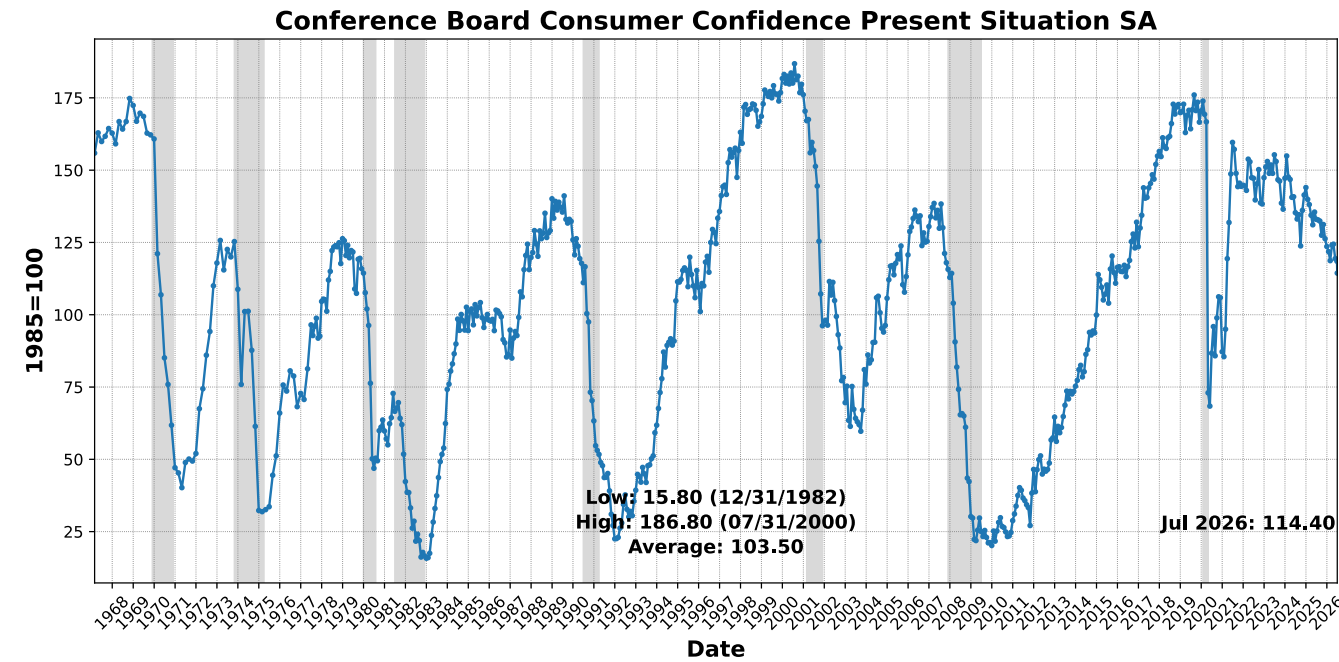




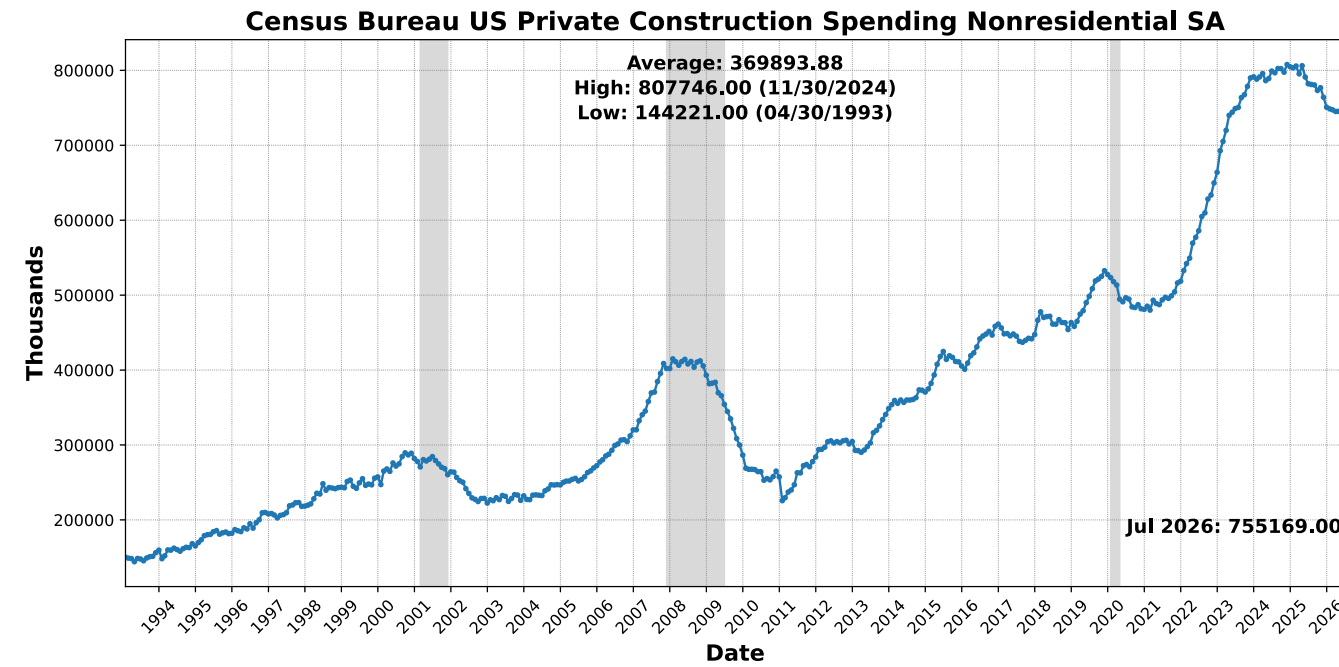
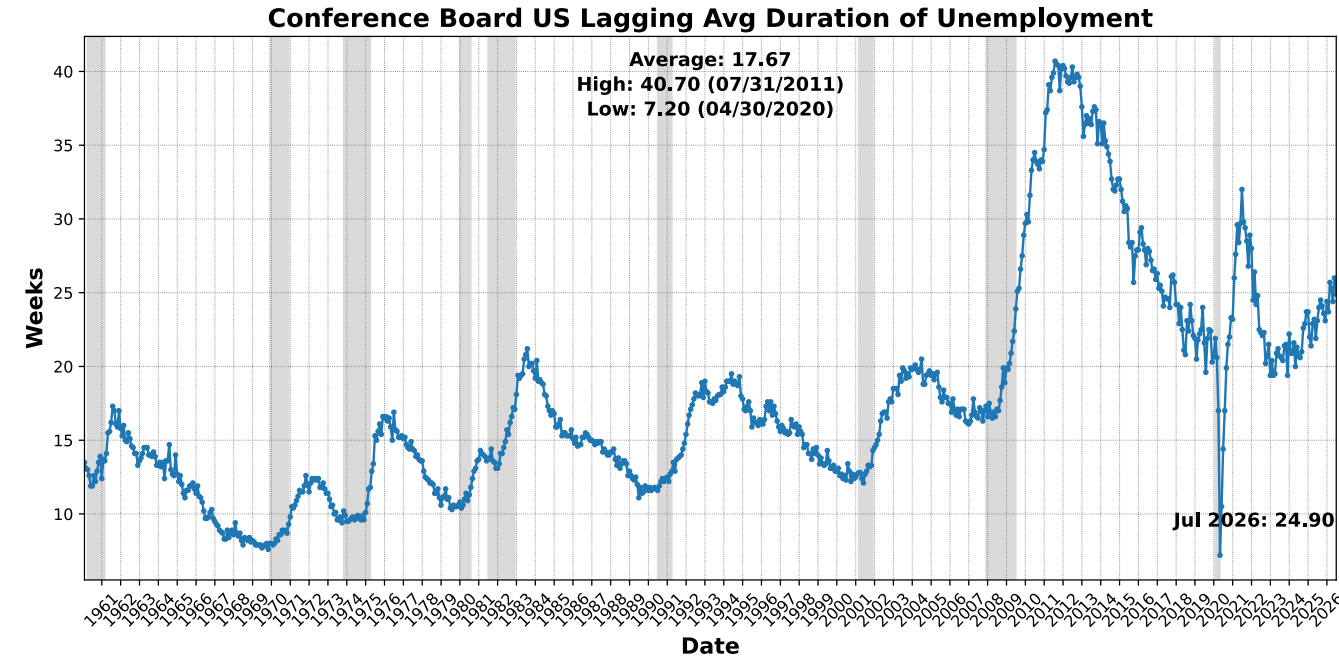
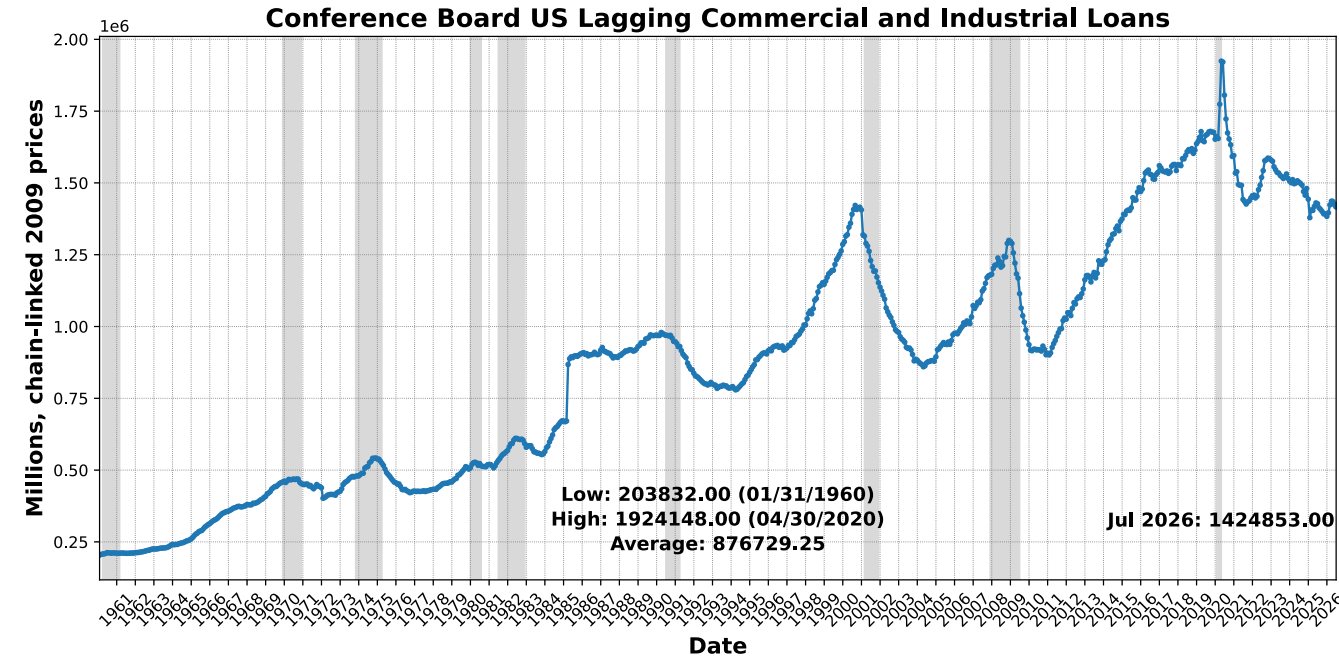
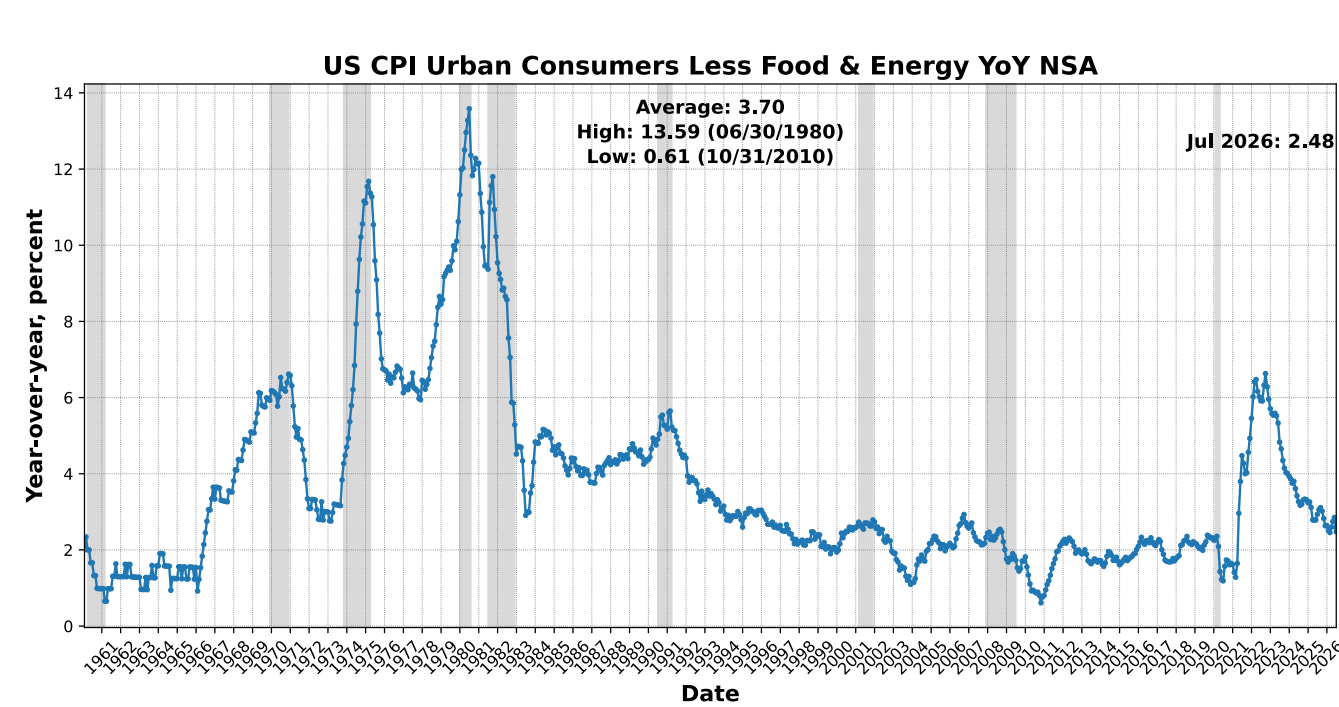


ROUGHLY COINCIDENT INDICATORS





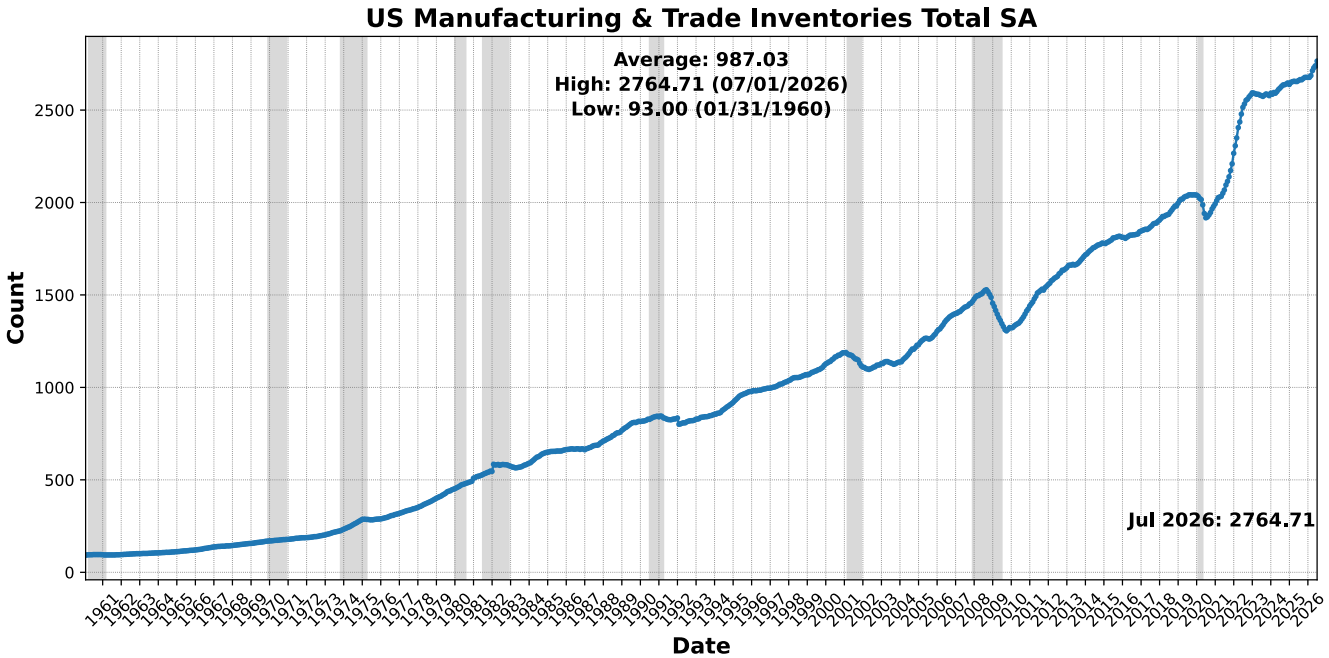
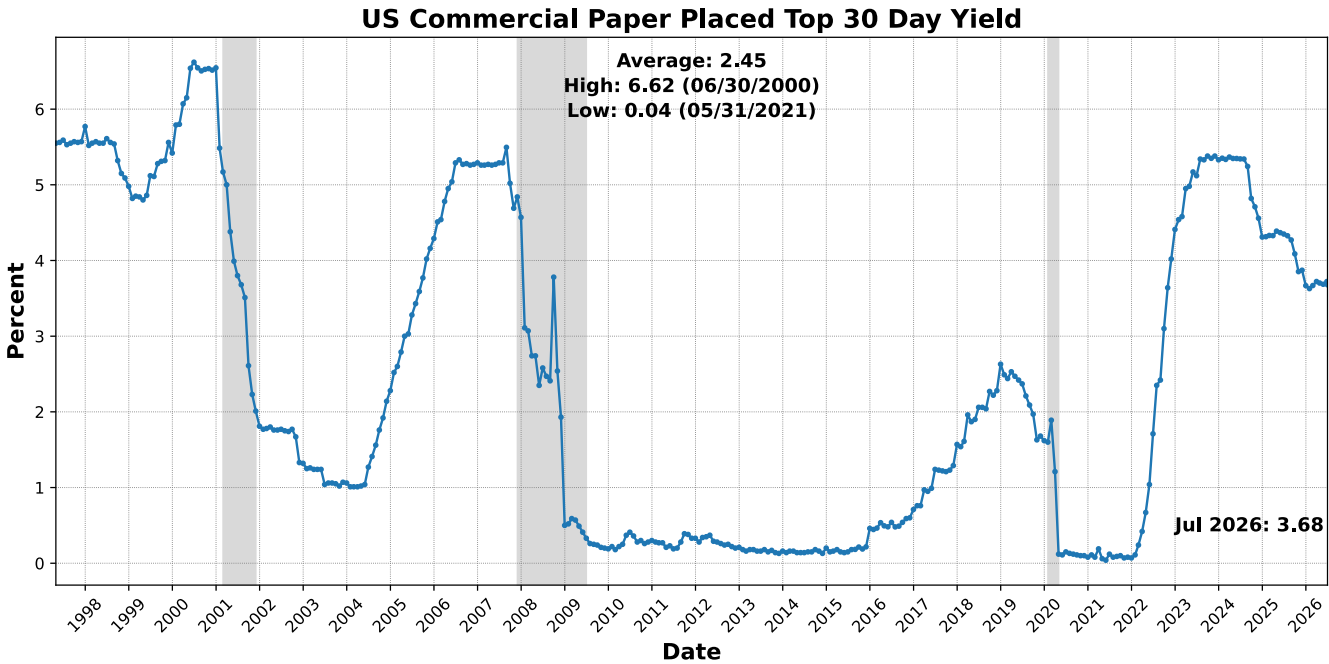
LAGGING INDICATORS



Capital Market Performance

Ticker		Short Name	%1M	%3M	%1YR	3 Year Annualized Total	5 Year Annualized Total	10 Year Annualized Total
▶ SPR	d	S&P 1500 Composite Index	+ .09%	+4.48%	+16.31%	22.2528	12.7928	14.9566
▶ SPXT	d	S&P 500 Total Return	+ .51%	+5.58%	+17.92%	22.8920	13.2828	15.3656
▶ SPX	d	S&P 500 INDEX	+ .41%	+5.29%	+16.55%	22.8660	13.2608	15.3488
▶ MID	d	S&P 400 MIDCAP INDEX	-3.46%	-4.40%	+11.65%	14.9372	7.8110	10.8411
▶ RTY	d	RUSSELL 2000 INDEX	-4.54%	-5.73%	+16.56%	18.3383	6.2206	10.5362
▶ SXXP	d	STXE 600 (EUR) Pr	-2.52%	+ .44%	+15.17%	16.0979	10.2462	10.1767
▶ TLT US	d	ISHARES 20+YR TR	-4.30%	-9.20%	-10.78%	.3237	-8.4173	-2.4176
▶ QLTA US	d	ISHARES AAA - A	-2.54%	-4.91%	-6.26%	4.3425	-.9096	1.6605
▶ CRY	d	TR/CC CRB ER Index	+3.00%	+18.83%	+37.21%	13.6605	13.1702	8.5781
XAU		Gold Spot \$/Oz	-5.35%	+5.00%	+10.00%			
XAG		Silver Spot \$/Oz	-5.81%	+7.32%	+33.22%			
ILM3NAVG		Bankrate 30Y Mortgage Rates Na	+7.00%	+9.28%	+13.25%			
ILM1NAVG		Bankrate 15Y Mortgage Rates Na	+7.86%	+10.57%	+16.64%			
MB301ARM		5 Year ARM	+2.69%	+4.10%	+10.31%			
ILA3NAVG		Bankrate 30Y Fixe Mtg Refis Na	-.14%	+ .43%	-2.92%			

(Source: Bloomberg Finance, LP. Data subject to shutdown limitations.)



Mao’s ‘Great Leap’: Mass Starvation on *The Road to Serfdom*

Jeffery L. Degner
Research Fellow

“A calamity ordained by Heaven may be escaped; A calamity ordained by oneself is inescapable.” So warns *Shujing*, the ancient Chinese *Book of Documents*. If only Mao Zedong had heeded this call to humility.

Despite a long history of civil strife, conflict brought by foreign powers, and countless natural disasters, the worst of China’s sufferings were self-inflicted wounds. Mao’s regime took power in October of 1949, and he unleashed too many horrors to capture in a brief essay. The policies of his poorly named Great Leap Forward led directly to the deaths of 36 million people. The long shadow of its horrors still haunts the Chinese economy and culture.

Five years prior to Mao’s assumption of national power, Austrian economist Friedrich von Hayek published *The Road to Serfdom*. In it, he observed, “Whoever has sole control of the means must also determine which ends are to be served...in short, what men should believe and strive for.” Once property is centrally controlled, that is, the goals of men are made subject to the goals of the owner. In the Chinese case, Mao’s goals were for steel and industrial production to exceed that of the West. At the outset of the Great Leap, he demanded “more, faster, better, cheaper” manufacturing.

What the Chinese people got instead was mass starvation and the worst famine in human history.

THE REHEARSAL

Eileen Chang witnessed firsthand the early stages of that campaign in the northern Jiangsu region. In her true-to-life novel *Naked Earth*, she depicts a moderately successful farmer, dragged in front of a jeering crowd with schoolchildren singing as he is harassed by members of the Farm Workers Association, the Women’s Association, and the Youth Vanguard Corps. He remains silent during his public shaming and beating. Eventually, he is crowned with a white paper cone-shaped cap emblazoned with the cue for his imprisonment: “Exterminate the Feudal Forces.”

The confiscation of land by the CCP and the negation of traditional land deeds were accompanied by the execution of potentially millions of landowners, seen as “class traitors” for earning more than their neighbors. Prior to their deaths, former property owners were publicly humiliated and beaten in shaming rituals known as “suku” or “Speaking Bitterness,” which served to “overturn” the social soil of rural life.

In June of 1950, Mao delivered a speech: “To Be a True Revolutionary.”

“War and agrarian reform are two tests everyone and every political party in China must go through in the historical period of New Democracy,” he thundered.

After the land seizures were complete, he proclaimed that every measure taken had produced a great victory for the revolution. Explaining his goals for this brutal “war,” he declared that the peasants who participated in the land seizures would “make the industrialization of the country possible.” What they truly made possible was their own demise.

THE GREAT LEAP FORWARD

Once land had been redistributed to the peasant class, what they thought belonged to them as “the people” was then claimed by the true owners: the centralized state. Initially, the rural poor received a Certificate of Land and House Ownership in 1952, which granted the legal right to farm, sell, transfer, and even bequeath it. The arrangement would be short-lived. Four years later, the People’s Congress promulgated the Model Regulations for Advanced Agricultural Producers’ Co-operatives on June 30, 1956. It forced all land rights to be yielded up to state-run collectives.

In early 1958, the Sixty Articles on Working Methods marked what could be considered the official declaration of the Great Leap Forward. The centralized planning was evident as the Sixty Articles called for party control of “a. targets of output; b. irrigation; c. fertilizers; d. soil; e. seeds; f. changes in the system of farming, such as enlarging the areas of a second crop” and even more.

At the center of this control was the fact that peasants no longer exercised decision-making: the farming communes were forcibly installed. What land the state had given, it would then take away. Secretly, some families hid their initial ownership certificates, perhaps in the hopes that they would one day be able to dispense with the property as they saw fit. That hope would be in vain. Instead, millions of them would starve to death.

The ultimate outcome of collectivized farming was a man-made famine. The mass starvation of 1959-1961 was triggered not by an act of Heaven, but rather as an inevitable consequence of the impossibility of rational planning under communist, centralized control. In a surprising contrast, the areas with the greatest productivity saw the highest rates of famine mortality. Production quotas were based on what regions had grown in the past, and when the harvest collapsed under low-productivity collectivism, the output quotas didn’t adjust the way a rational price system would.

When these minimums weren’t met, the Chinese central planners had two possible explanations. Either the plan was flawed, or peasants were hoarding the output. They incorrectly chose the latter. The only solution left to them was to forcibly search and seize what was on these farms and punish the offenders. The result was a catastrophic loss of life. Between terrifying violence and man-made starvation, scholars estimate between 16.5 and 45 million excess deaths.

While the famine’s death toll had begun to decline by 1962, its impact remained. The long-term health and economic outcomes were studied by Yuyu Chen and Li-An Zhou. They found that survivors born in 1959 were three centimeters shorter than they otherwise would have been, due to malnutrition. Yang Jisheng’s 2012 book, *Tombstone: The Great Chinese Famine, 1958-1962* estimated a birth deficit of approximately 40 million, further depleting the future workforce.

Is America in danger of these kinds of Maoist tragedies? If the surging popularity of socialism among the young and the praise of Mao by the likes of Hasan Piker are any indication, then answering “yes” is entirely reasonable. Continual erosion of property rights, hatred of landlords, and other interventionist policies slowly, perhaps unintentionally, lay the philosophical groundwork for these devastating outcomes.

While some may lean on American exceptionalism to preserve our freedoms, they do so at their own peril. Socialist ideas and their implementation have left a merciless, relentless path of destruction around the world. Indeed, there are no exceptions to that rule.

When Government Separates Choices from Consequences

Donald J. Boudreaux
Associate Senior Research Fellow

Economics textbooks often teach that a proper role of government is to intervene in markets to align incentives when the market fails. Markets work best when decision-makers bear the consequences of their choices. “Internalizing externalities” — say, making companies that discharge pollutants into a river pay to maintain it — is cited as a just cause for taxes, subsidies, and regulation. Most economists continue to teach, write, speak, and podcast as if this textbook prescription for government intervention is a reliable-enough description of reality.

But real-world government intervention routinely does the opposite. It takes costs and benefits that individuals would otherwise experience as consequences of their own choices and shifts them onto other people. In other words, the government regularly “externalizes internalities,” for which we pay the price.

INCOME REDISTRIBUTION AND WELFARE

The most obvious example is taxation for purposes of income redistribution. Whatever the merits or demerits of a policy of redistribution, the essence of any such policy is that some people (the net recipients of tax revenues) live partially at the expense of other people (the net payers of tax revenues). Consistent application of the economic logic that powers textbook explanations of externalities leads to the conclusion that government-engineered income redistribution causes too many people to seek such redistribution (chiefly, by exerting less effort than they otherwise would to increase their own earnings), while at the same time causing high-income earners to exert too little effort at earning taxable income.

Absent redistribution, each person would be paid as income an amount closer to the value of what he or she contributes to the market economy — meaning, the market causes each person to internalize the costs and benefits of whatever amount of effort they choose to devote to earning income. But redistribution obstructs this market result; it artificially dims both the personal penalty for not working and the personal reward for working.

TARIFFS AND TRADE WARS

Another example of the externalization of internalities is protectionism. Producers’ earnings in competitive markets reflect roughly the value of that product to consumers. When consumers spend their own incomes in whatever peaceful ways they choose, they personally pay the costs and reap the benefits of their choices. Producers that better please consumers are rewarded

with higher profits — higher profits voluntarily paid to them by consumers. Markets, in other words, internalize on producers the value of their efforts to please consumers.

Protectionist tariffs and non-tariff barriers, by contrast, externalize this internality. By shrinking consumers’ range of choices, protectionism artificially increases consumer demand for the outputs of protected producers. Protected producers thus earn higher profits without creating more value for consumers. A consequence that belonged inside the producer-consumer relationship has been transferred outside it.

Protected firms free-ride on a portion of their fellow citizens’ incomes — the funds these citizens would otherwise have spent on imports. As a result of protectionism, producers exert less effort than otherwise to please consumers. Far from correcting a market failure, protectionism distorts markets. Protectionism externalizes an internality.

OCCUPATIONAL LICENSING

A third example of a government policy that externalizes an internality is occupational licensing requirements.

Adults spending their own money for their own purposes have every incentive to assess the quality of different service providers’ offerings. Service providers who seem likely to supply unacceptably low quality don’t win new customers and fade from the market. Surviving suppliers will earn revenue based on how much consumers value the service. In a free market, each service provider — hairbraider, electrician, carpenter, florist, interior designer — has incentives to satisfy consumers to increase his own income.

In a competitive market, in other words, service providers gain or lose according to their own efforts, and no consumer is obliged to pay more than is necessary for that service. The consequences of service providers’ choices (even as they impact the consumer post-purchase) are internalized by the service providers.

Occupational-licensing regulations externalize this internality. Obstructing consumers’ ability to choose different service providers, and blocking new entries to the market, these regulations artificially increase the incomes of licensed suppliers, as all consumers are forced to pay more. Competition forces providers to bear the consequences of disappointing consumers; restrictive licensing weakens that discipline.

WHEN GOVERNMENT MAKES THINGS ‘FREE’

“Democratic Socialists” talk of providing for “free” the likes of tuition, bus rides, and childcare, along with subsidized groceries and other goodies. But obviously these goods and services do not become zero-cost simply by decree. What these socialists have in mind, instead, is to arrange for some people — bus riders relieved of ponying up fares — to free-ride on the productive efforts of other people (namely, net taxpayers). The more distant the rider is from the monetary cost of ridership, the more disordered are the choices and incentives.

The same incentives apply to subsidized college programs. When someone else pays, the cost of making a decision is far from the person making the choice.

It’s no exaggeration to describe the Democratic Socialists’ economic agenda as one that prevents individuals from experiencing the full benefits and costs of their personal choices — as one, in short, that externalizes internalities.

A clear-eyed survey of actual government policies reveals that the economics-textbook description of governments as internalizers of externalities is completely backwards.

The Fed Finally Raised Rates. Now Comes the Hard Part.

Bryan P. Cutsinger
Fellow, Sound Money Project

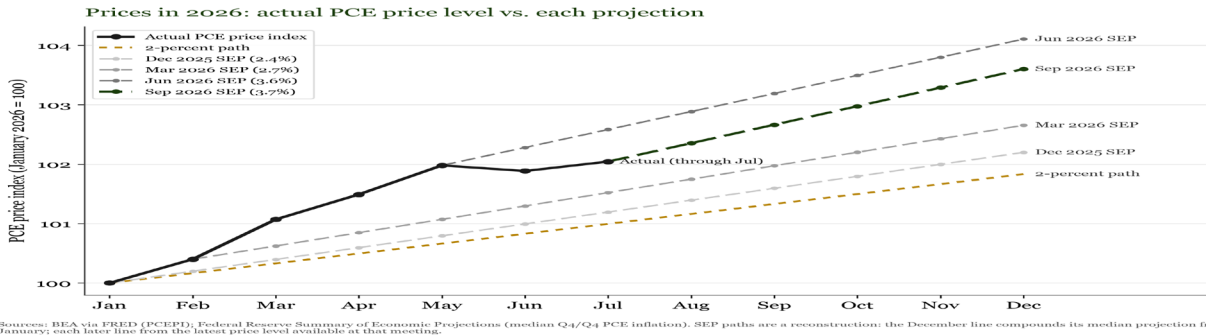
The Federal Open Market Committee (FOMC) voted unanimously to raise its target range for the federal funds rate by a quarter percentage point to **5.75–4 percent** on Wednesday, the first increase since July 2023. More importantly, the projections released with Wednesday’s decision suggest that more increases lie ahead. The decision came as little surprise to market participants: on the eve of the vote, futures markets put the odds of a quarter-point increase above **90 percent**.

In July, the FOMC noted that inflation was elevated “in part reflecting supply shocks that have driven price increases in certain sectors, including energy.” That language was nowhere to be found in Wednesday’s release. The statement made no reference to supply factors, saying only that “Inflation remains elevated,” and the rate increase “will support a timelier return to the Committee’s **2 percent** goal,” suggesting that the Fed now sees demand as the primary driver of inflation.

At the post-meeting press conference, Chairman Warsh defended the decision to raise rates on the grounds that the economy “appears to be strengthening,” and that he “would be hard-pressed to describe broad financial conditions as restrictive.” That view, Warsh noted, “was widely shared by the Committee. So we removed a dose of accommodation.”

At his Jackson Hole speech last month, Warsh committed himself to “a monetary policy discipline, not to a decision,” and set the standard he would use to evaluate whether policy is on the right track: “We must be confident that underlying inflation is moving to our objective, clearly and at sufficient speed.” According to Warsh, “the FOMC decided that this standard has not been satisfied,” which is why the Committee decided to raise rates.

The Summary of Economic Projections released with the decision aligns with the FOMC’s decision to remove the supply shock language from Wednesday’s statement. FOMC members now expect growth of **2.3 percent** this year, up from **2.2 percent** in June; unemployment of **4.1 percent**, down from **4.3 percent**; and inflation of **3.7 percent**, up from **3.6 percent**, with core inflation, which excludes food and energy, at **3.4 percent**, up from **3.3 percent**.



Sources: BEA via FRED (PCEPD), Federal Reserve Summary of Economic Projections (median Q4/Q4 PCE inflation). SEP paths are a reconstruction: the December line compounds its median projection from January; each later line from the latest price level available at that meeting.

The Fed Finally Raised Rates. Now Comes the Hard Part.

In short, they see faster growth, a tighter job market, and higher inflation: every revision in the projections points toward too much spending rather than too little supply. That should put policymakers on alert. Excess demand requires tighter monetary policy, not patience while supply recovers.

The FOMC’s inflation projection for 2026 has risen steadily over the past nine months, from **2.4 percent** in December to **2.7 percent** in March, **3.6 percent** in June, and **3.7 percent** on Wednesday. Inflation measures how quickly prices rise. The price level measures how high they are. The chart below shows what the Fed’s inflation revisions imply for the price level at year’s end. The decline in July’s PCE print puts the September projection path slightly below June’s, despite the Fed projecting higher inflation. Nonetheless, prices remain on track to finish the year a full percentage point above where policymakers expected last December.

Looking ahead, Fed officials project inflation falling to **2.3 percent** next year and not reaching two percent until 2029. Pressed on how a “timelier return” fits with the Fed not meeting its target until 2029, Warsh answered that the projections are his colleagues’, not his. That’s fine as far as it goes, but the Fed’s credibility depends on policymakers’ decisions and the results that follow. Projecting inflation to remain above target for another two years is difficult to square with Warsh’s promise of monetary discipline.

Most FOMC members expect to raise rates at least once more this year, while four expect two increases by the end of the year. The median projection puts the federal funds rate at **4.1 percent** at year’s end, up from **3.8 percent** in June, and keeps it there through 2027, compared with the previous projection of **3.6 percent**. In other words, Fed officials now anticipate both further tightening and a longer period of higher rates.

Wednesday’s increase was a promising start toward the monetary discipline Warsh has promised. But with nominal spending growing at an annualized rate of eight percent in the second quarter, Fed officials must recognize that restoring price stability will require further rate increases. The test is whether it tightens policy enough to bring inflation back to two percent “clearly and at sufficient speed.”

Debt Jubilees Only Change Who Pays

Thomas Savidge
Research Fellow

The United States has crossed a fiscal milestone that would have seemed unimaginable to earlier generations: \$40 trillion in gross federal debt.

One response is to look backward. In a recent guest essay in *The New York Times*, Paul Vigna invoked the Sumerian term amargi (also rendered amagi) and the associated practice of rulers canceling private debts. He urged America to consider the same remedy for its modern debt.

Amagi, however, is not a settled one-word synonym for “debt cancellation.” Its literal translation is “return to the mother.” It has been described as one of the earliest written expressions of liberty, but its precise meaning is unclear. Subsequent scholarship connected the term to freeing people held in compulsory service for tax debts, allowing them to return to their families. Larry Arnhart reads amagi broadly: release from debt servitude, lower taxes, restored property, fewer bureaucratic controls, and “freedom under the law.” These readings suggest that amagi concerned emancipation from personal subordination and official abuse, not the cancellation of sovereign securities.

The analogy breaks down at the outset. Mesopotamian clean-slate edicts typically remitted agrarian and personal debts, tax arrears, and obligations to palace or temple institutions. They did not cancel a sovereign’s bonds to investors in anything resembling today’s Treasury market. Wiping out federal securities would be a different policy aimed at a different kind of debt.

In a later LinkedIn post, Vigna acknowledged the central historical problem. “Sovereign debt didn’t exist then,” he argued. His proposal is instead “a really broad, multinational way to reset the entire debt clock.” Yet he insists that it must occur “not in a way that wipes out the creditors.” He calls a “controlled implosion” preferable to waiting for what he sees as an inevitable collapse because the debt will never be paid off.

That qualification contains the proposal’s central contradiction. A government cannot zero out a liability while leaving the corresponding asset intact. Making creditors whole would require governments to redeem their bonds through taxes or asset sales; replace bonds with another government obligation; or pay creditors with newly printed money. Those alternatives amount to repayment, relabeling, and monetization, respectively, not erasure.

Monetization does not solve the contradiction. The Federal Reserve creates most new money by purchasing

financial assets and crediting banks’ reserve accounts with new digital balances. A Treasury security becomes an asset on the Fed’s balance sheet, while the newly created reserves become its liability. Canceling the Treasury security would remove the Fed’s asset but leave the reserves it creates to purchase it outstanding. Nor does creating money create additional real resources. If the Fed creates more money than people want to hold, they spend the excess, bidding up prices and reducing the dollar’s purchasing power. Part of the obligation shifts to money holders, but it never disappears.

Making the plan multinational does not change the arithmetic. Governments could offset some debts they owe one another, but claims held by private investors and domestic public institutions would remain. A multinational agreement could not eliminate those securities without deciding who would absorb the losses or what equivalent assets would replace them. That allocation is the substance of the policy.

The claim that the debt will never be paid off also conflates the total stock of federal debt with the individual securities that compose it. Treasury securities mature and are redeemed continually, although the government often finances those payments by issuing new debt. Maintaining a debt stock is not the same as refusing to honor existing bonds. The problem is that persistent deficits cause debt and interest costs to outpace national income and federal revenues

Nor is the choice limited to a global jubilee or passive acceptance of an inevitable collapse. Congress can change the spending, tax, and borrowing rules that generate structural deficits. A “controlled implosion” without an explicit mechanism for allocating the losses would just be an implosion, whether it took the form of default, inflation, or a compulsory exchange of one government claim for another.

Even if Washington could declare all \$40 trillion canceled, Congress would still face the same incentives to promise more than it raises in revenue. Deficits would soon resume.

A debt jubilee would reset the clock without fixing it.

Nor would cancellation make the economic costs disappear. Treasury debt is a government liability and an asset held throughout the financial system. About \$32.3 trillion of that debt is held by the public. This includes households, financial institutions, foreign holders, state and local governments, and the Federal

Reserve. Another \$7.75 trillion is held within the federal government, including by Social Security and other trust funds.

Canceling the first category would impose losses on private and public holders. Canceling the second would erase trust fund assets without erasing the benefit promises associated with them. The liabilities would not disappear; they would just move.

A jubilee of federal debt would also raise serious constitutional questions. Section 4 of the Fourteenth Amendment states that the validity of public debt authorized by law “shall not be questioned.” In *Perry v. United States* (1935), the Supreme Court rejected the idea that Congress may borrow on the nation’s credit and later “alter or destroy” its commitments.

The fact that money and credit are “social constructions” does not make their consequences imaginary. Contracts, property rights, and yield curves are social constructs, too. Changing the rules governing them can redistribute wealth, but it cannot make the underlying costs disappear.

Why should creditors or holders of dollars bear the cost of Washington’s failure to reconcile its spending promises with the revenue it collects?

Treasury securities play a central role in modern finance. They serve as investments, collateral, and benchmarks for other financial assets.

Their usefulness rests on the government’s reliability. If investors came to view Treasury promises as politically contingent, they would demand a premium for that risk or reduce their willingness to lend.

None of this means Americans should accept our present \$40 trillion predicament. Instead, we must address the process that produced it.

The central problem is fiscal. Both parties face pressure to offer new spending without new taxes, and tax cuts without spending cuts. Borrowing postpones the tradeoff. Voters receive benefits now, and future taxpayers receive the bill.

America’s constitutional system recognizes that government power requires institutional constraints. Yet while the Constitution requires Congress to authorize taxes and spending, it places few effective limits on long-term debt accumulation. Congress can enact programs and tax cuts whose political benefits arrive immediately while their budgetary costs stretch across decades. The result is a system that makes borrowing easier than restraint.

The answer is a fiscal constitution that changes the incentives behind chronic borrowing through spending restraints and limits on government authority to prevent workarounds to budget rules. The details deserve debate. The principle is beyond dispute. Fiscal discipline cannot depend entirely on the self-restraint of politicians who benefit from deficit finance.

The harder question is whether America can establish institutions that prevent elected officials from repeatedly creating obligations without making the spending and revenue adjustments needed to honor them.

That is why the Sumerian example points toward a different lesson. Ancient rulers used debt cancellation to relieve political strain. Whatever its immediate benefits, a jubilee was an episodic remedy applied after obligations had become destabilizing, not an institutional rule preventing them from accumulating.

In addition, cumulative jubilees contributed to fiscal deterioration. A string of temporary exceptions, unfunded promises, or borrowed emergencies compounds strain over time. A civilizational collapse may appear sudden, but its causes accumulated over decades.

Recurring debt crises are evidence that the rules governing borrowing and repayment have failed. The durable solution is to make chronic deficit finance harder. America should learn from that warning without confusing that relief with wholesale repudiation of federal debt.

The United States needs a fiscal constitution, not fiscal amnesty.

Made in (North) America: Canada Is Not Our Enemy

David Hebert
Director of Economics and Economic Freedom

In the US, we have a tendency to stamp products as “American-made” and imagine that that product was entirely made within our borders. The truth is that we should be referring to almost everything that we build as “North American-made.” Cars, appliances, machine tools, tractors, toilet paper... the list goes on and on. If we trace their supply chains far enough, what we find is that they almost always run through Canada (and often, Mexico) before arriving at the US plant that gets to put its name on the box. That cross-border web is exactly what lets US manufacturing compete against the rest of the world.

Over the past few weeks, President Trump and other White House officials have looked at that arrangement and said, “we don’t need Canada, they need us.” President Trump called Canada “among the worst nations in the world to deal with” and said that it has been “ripping off the United States of America for years.” In response to these accusations, he threatened a **50 percent** tariff on Canadian cars, trucks, auto parts, and steel shipments starting in January.

But this would not be a tax on Canada. It would be a tax on the American assembly line that needs those parts to build cars, trucks, and machinery. When inputs are made more expensive, final goods become more expensive, too.

In September of 2025, Canada unilaterally dropped Consider how a car, for example, is built. Right now, a truck hauling a load of stamped metal from Ontario is heading toward a manufacturing plant in Michigan. Once delivered, it will be welded into a subassembly, trucked back across the river to have more work done, and returned to Michigan to be bolted into an “American-made” car. The same part can cross international borders six or more times before it finally becomes a finished Ford, Jeep, or Chevy. Detroit’s Big Three automakers did not look across the Ambassador Bridge to establish some of their operations there by mistake. They did so because it made them more productive and more competitive against the likes of Toyota, Hyundai, and BYD. But if we put a **50 percent** wall in the middle of that supply chain, the parts that US workers need to do their jobs suddenly become more expensive. The tax that was supposed to target Canada instead hits the very people it was supposed to help.

The most telling part of all of this comes from Shawn Fain, the president of the United Auto Workers. Mr. Fain is no free trader and has come out extraordinarily vocal in support of the president’s trade agenda, including tearing up the USMCA and rewriting it from the ground up. On August 25, just days after talks between the US

and Canada broke down, he released a statement reading, in part: “The UAW rejects any escalation on Canada, a country with strong unions and labor standards.”

To commemorate the one-hundredth day of his second term, President Trump held a rally in Michigan promising to bring jobs back to the automotive sector and Detroit “at levels you’ve never seen before.” When the leader of the union you claim to be helping comes out against your policy, odds are good that you’ve picked the wrong target.

Trade, in the president’s view, is described as if it were purely transactional and reducible to net flows of dollar figures. But trade is about so much more than that; it’s about trust and relationships built over decades. These relationships matter not just because Canada supplies us with steel, parts, lumber, energy, and other intermediate goods that US firms use every day, but because Canada has proven itself to be a friend and ally when friendship mattered most. This month marks a particularly important anniversary of exactly that.

On September 11, 2001, when the US shut its airspace in response to a terrorist attack on the World Trade Center, hundreds of planes full of Americans had few places to safely land. And on that day, Canada opened its doors without a moment’s pause. Gander International Airport in Newfoundland, Canada, remains the most famous example. Thirty-eight airplanes carrying a total of almost 7,000 passengers were redirected to an airport with two runways and 13 gates, almost doubling the local population of just over nine thousand people. An airport that usually sees four or five flights per day was suddenly asked to land thirty-eight planes in a span of about 90 minutes.

The town responded with hospitality. Gander had only about 500 hotel rooms, so residents opened their homes. They provided space, food, transportation, and comfort to thousands of complete strangers. Bus drivers in town, who happened to be on strike that day, dropped their picket signs and volunteered their time driving people for the next five days.

Across the rest of Canada, the story is the same. Tens of thousands of stranded travelers were housed and fed. Phone lines and cars were loaned; laundry was washed for days until American skies were deemed safe to reopen and flights could be rerouted.

That’s the country that President Trump has now called “nasty” and “among the worst nations in the world to deal with.” A nation that has been “ripping off” the US for decades isn’t one that will take in your people when their planes are grounded and borders are sealed off. The US-Canada border is the longest undefended border in the world and for a good reason. Canadians are not just our neighbors to the north. They’re our friends.

None of this means that Canada is purely innocent. Its dairy protections are real, softwood lumber has been a recurring problem for decades, and provincial restrictions on American alcohol genuinely burden brewers and distillers. Canada has certainly taxed its own citizens with tariffs against the US over the last several decades. But the solution to Canadian protectionism is more trade liberalization, not a 50-percent tax wall through the middle of North American production.

In a Fact Sheet released by the White House, President Trump points out that the US “economy is approximately 13 times larger than the Canadian economy” and is “home to over eight times as many people.” He thinks this gives us “clear leverage.” But leverage isn’t measured by how large your market is. Viewing trade as purely transactional misses the relational aspect, which matters significantly more.

The truth is that Canada does need the United States. But it’s also true that the United States needs Canada (and Mexico, too). We need the cross-border production networks that help American workers, including those in the US, compete. We need the trust that allows firms on both sides of the border to invest, specialize, cooperate, and build together.

If we want to continue seeing “American-Made” products on our shelves and in our driveways, we should be honest about what that label has always meant: North American-Made. The neighbor who supplies steel and manufacturing components is the same one that opened its doors to stranded Americans on the worst day we’ve seen in generations.

A trade relationship with an ally and friend like Canada is one worth preserving.

Bond Markets Are Losing Patience— And Putting Government on Notice

Peter C. Earle
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Something unusual is happening in global bond markets, and it is more consequential than the usual swings in yields. Government borrowing costs are rising across much of the developed world. The US 10-year Treasury is approaching **5 percent**, and the 30-year Treasury yield is at levels not seen since 2007. “Meltdown” is too dramatic a word, but the bond market is clearly sending a message. Bond prices fall when investors demand higher yields, and global investors clearly want to be paid more for lending money to governments carrying large debts, running persistent deficits, and still contending with above-target inflation.

Japan is perhaps the most striking case. Its 10-year government bond yield has moved through **3 percent** after spending most of a generation near zero, and its 30-year borrowing cost has risen above **4 percent** — a multi-decade high. Australia’s 10-year recently reached **5.16 percent**. Germany’s 10-year Bund has been trading around **3.3 percent**, with the 30-year above **3.8 percent**. Britain, France, and other developed economies are seeing versions of the same thing. The particulars differ from country to country, but the direction does not.

Global 10-Year Government Bond Yields

Current yields and changes in percentage points

COUNTRY	10-YEAR YIELD (%)	YTD CHANGE (PCT. POINTS)	YOY CHANGE (PCT. POINTS)
 United States	4.7850	+0.61%	+0.56%
 United Kingdom	5.2255	+0.75%	+0.48%
 Japan	3.0180	+0.94%	+1.38%
 Australia	5.2010	+0.44%	+0.77%
 Germany	3.3735	+0.51%	+0.63%
 Brazil	14.4800	+0.60%	+0.42%
 Russia	16.1100	+1.67%	+2.30%
 India	6.9780	+0.41%	+0.42%
 Canada	3.7980	+0.36%	+0.40%
 Italy	4.2219	+0.71%	+0.58%
 France	4.2530	+0.69%	+0.71%
 South Africa	8.8150	+0.61%	-0.83%
 China	1.6860	-0.18%	-0.09%



Source: Trading Economics
Data as of Sep 02, 2025 (17:15 ET for U.S.)

Oil prices and renewed inflation worries are part of the explanation, as is the growing possibility that central banks will have to keep monetary policy restrictive for longer than markets have expected. But these are proximate causes. The bigger story began several years ago. Governments entered the COVID period already heavily indebted, then responded to the pandemic with enormous fiscal programs supported by extraordinarily easy monetary policy. Central banks subsequently discovered that the resulting inflation was neither especially transitory nor easy to eradicate. Now, the consequently larger debts have to be financed and refinanced in markets where investors once again demand compensation for inflation, duration, and fiscal risk.

For the United States, the arithmetic becomes daunting fairly quickly. Gross federal debt recently passed \$40 trillion, with roughly \$32.3 trillion held by the public. The weighted-average maturity of marketable Treasury debt is about 71 months, although roughly one-third matures within the next year. So a 20-basis-point increase in the 10-year Treasury does not suddenly reprice \$32 trillion of debt. But the government does not get to ignore higher rates, either. Something on the order of \$10 trillion of marketable debt must roll over within a year. Meanwhile, Washington continues to borrow hundreds of billions more to finance new deficits.

A household analogy is useful here, with one qualification. Imagine an enormous mortgage that resets in pieces rather than all at once. A homeowner with a fixed-rate mortgage does not care very much if mortgage rates jump tomorrow: he cares about when he has to refinance. The US Treasury is constantly refinancing; some portion of the federal government’s enormous mortgage matures every day.

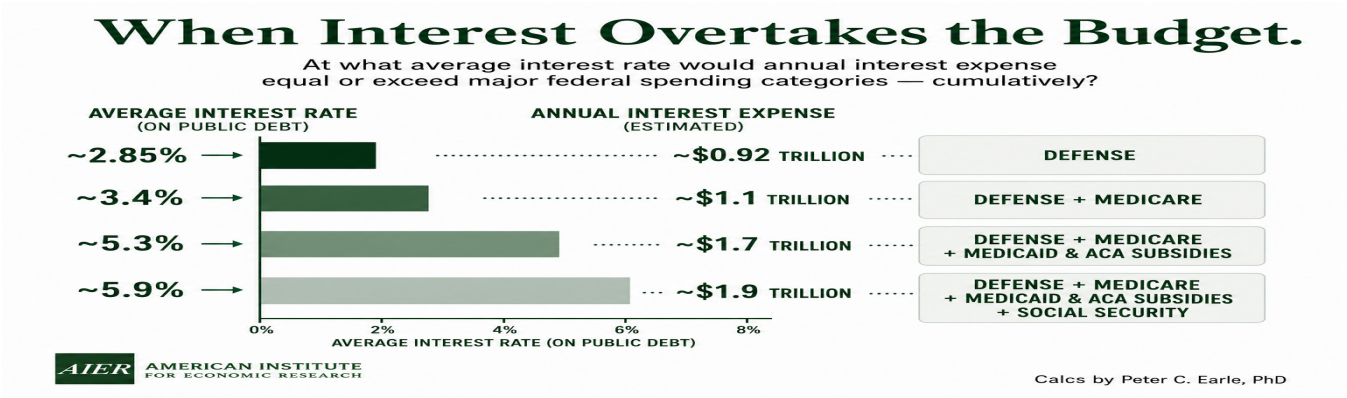
We can already see that process in the numbers. The average interest rate on interest-bearing Treasury debt was about **3.32 percent** in January. By July it was roughly **3.45 percent**. Thirteen basis points sounds like market noise, until the principal involved is measured in tens of trillions of dollars.

Using \$32.3 trillion of publicly held debt as a rough base, every sustained 5-basis-point increase in the government’s average financing cost eventually means about \$16 billion more in annual interest expense. Ten basis points means roughly \$32 billion; 25 basis points, \$81 billion; 50 basis points, \$161 billion. A full percentage point works out to approximately \$323 billion per year — about what the US spends on veterans’ support. Those are steady-state figures, not next-year budget estimates, because the existing debt has to reprice first. If roughly one-third of the debt rolls over within twelve months, a 10-basis-point increase would initially add something closer to \$10-11 billion to the annual cost of the existing debt, before considering new borrowing.



The change since January gives some idea of the scale involved. If the 13-basis-point increase in the US Treasury’s average interest rate were eventually reflected across today’s publicly held debt, the annualized increase would be around \$42 billion. But the interest rate is only half of the problem: publicly held US Treasury debt has itself grown by roughly \$2 trillion. Financing that additional principal at around **3.5 percent** adds another \$65-70 billion annually. Put the two together and the increase in the annualized interest burden is plausibly already in the neighborhood of \$100 billion. That is a run-rate calculation, not a claim about actual fiscal-year outlays, but it illustrates what happens when both the amount borrowed and the price of borrowing rise together.

The budget implications are no longer theoretical. The US Congressional Budget Office (CBO) projects net federal interest expense above \$1 trillion in fiscal 2026, against roughly \$898 billion of defense spending. In other words, interest has already become larger than the defense budget. Medicare is roughly \$1.1 trillion and Social Security around \$1.7 trillion, with Medicaid and ACA subsidies representing another substantial expenditure.



There is another way to visualize the problem. Using the same \$32.3 trillion debt base and deliberately simplified arithmetic, an average financing cost around **2.85 percent** produces an interest bill roughly comparable with defense spending. Raise the effective financing cost and the interest burden becomes comparable with progressively larger combinations of defense, Medicare, Medicaid, and ACA subsidies, and eventually Social Security. This is an illustration, not a forecast: Treasury debt matures at different times, inflation-linked securities complicate the calculation, the government receives some interest income, and the debt stock will not remain at \$32.3 trillion. But none of those qualifications changes the basic point: with this much debt outstanding, surprisingly small movements in average financing costs translate into very large amounts of money.

That is what makes the present bond selloff, and consequent rise in yields, significant. For years, developed-world governments operated as though enormous debt stocks and negligible financing costs could coexist more or less indefinitely. COVID pushed that experiment much further. And with the return of persistent inflation, the price of money changed.

Bond markets are now forcing governments to confront the change in circumstances. Yesterday’s deficit does not disappear when the fiscal year ends; it becomes part of the debt that has to be serviced tomorrow. Rising yields therefore work much like higher mortgage or credit card rates, except that governments are refinancing obligations measured in trillions. As more debt rolls over, the consequences migrate from trading screens into national budgets. Money spent servicing the debt is money that cannot be spent on defense, infrastructure, health care or Social Security without some combination of raising taxes, borrowing still more, or engaging in financial parlor tricks. At some point, the bond market stops offering commentary on fiscal policy choices and starts imposing limits. We appear to be approaching, if not at the early stages, of that phase.

The Great Repricing of The College Degree

Joakim Book
Research Fellow

For a few generations, heading off to college after high school became a rite of passage for many Americans. The academic landscape grew competitive, the names of the oldest and most illustrious universities entered common parlance, and the four-year degree was a ticket into a financially secure middle-class life.

For the longest time it was simply a matter of course that the bright, aspiring young ought to attend university; the fancier and more credentialed the institution, the better.

Even in the 2010s, it was rare for brilliant young people to opt *out* of the foreordained path that was college. Programs like Praxis — which matched young, entrepreneurial people with business through apprenticeships — offered an alternative, as did starting a business, learning a trade, or simply entering the workforce. But around American dinner tables, the question remained: “Where is your kid going to college?”

Not anymore.

Or, at least, not obviously.

Some survey results have hinted at this for a while, even though the financial logic behind the college boom has long been straightforward. Give up four years of wages, pay tuition and living expenses (perhaps borrow to do so), and receive a credential that lets you earn considerably more for the rest of your working life. The degree was an investment in human capital — the noncynical story goes — and depending on your chosen profession (and how lavishly you spent on those credentials, e.g., high living expenses versus working on the side and graduating early), you could reasonably expect to earn back what you lost fairly quickly.

As I described in a piece for *The Daily Economy* last year, the calculations were never quite that simple: The relevant comparison isn’t the lifetime earnings of graduates and non-graduates, but the incremental earnings attributable to the degree, net of tuition, financing, and four years of foregone income. Regardless of how much of higher education’s investment returns reflected raw ability and how much was a signal, the underlying wage premium was still a real, observed phenomenon. And for decades it was large enough to make the college bet look fairly safe.

A new pre-print by researchers from UPenn and the University of Navarra, titled “The College Wage Premium in the Generative AI Era,” has some bad news for the college-bound kids: the economic case for a degree has rarely looked this uncertain. The wage premium has declined precipitously in just a few years, bucking a long-term trend in the US. The authors, José Azar, Mireia Giné, and Javier Sanz-Espín, explain the significance:

The post-2022 contraction in the US college wage premium marks a structural shift in the returns to higher education. In long-run supply-and-demand accounting, 2022–2026 represents the first documented historical period characterized by a sustained, absolute decline in relative demand for college labor.

A four-year college degree was a scarce good whose value (the wage premium it attracted over what was otherwise available) rose as the economy demanded more professionalized, high-cognitive labor. For decades, the supply of that sort of worker exploded out of the universities. Now, many of the cognitive tasks their jobs require are becoming easier to automate or reproduce via the AI revolution. That’s contributing to the falling college wage premium. “Employers and officials have long argued that as the numbers attending university have ballooned, a degree has ceased to be a good proxy for job-relevant abilities outside of elite institutions and vocational subjects,” John Burn-Murdoch summarized for the *Financial Times*’ “Data Point” column.

The (unadjusted) wage premium peaked at about **80 percent** in 2001, after which it hovered around that level — until the post-pandemic work-from-home and AI revolution have recently reshuffled the playing field.

At some level none of this is unsurprising (markets *work!*): rising returns to education were contingent on a specific postwar, turn-of-the-century set of economic circumstances. Of course. The race between education and technology told us as much *decades* ago; Claudia Goldin and Lawrence Katz’s series of scholarly articles dates from the 1990s! The book that developed the framework, *The Race between Education and Technology*, came out in 2008.

Writes Burn-Murdoch again: “there is nothing inevitable about more education being met with more demand for those skills — it all depends on how the supply of particular skills interacts with the technological paradigm of the day.” The college premium wasn’t a fact of nature or an economic law, just the result of particular technological change fleetingly favoring one set of skills.

The workplace shift in previous centuries, from at-home artisans to intricate business environments and from manual labor to the service sector, created a premium for educated workers, and gave them good pay. The widespread schooling and high school education in the first half of the twentieth century eroded that. The information/digitalization era did something similar again, pushing technical competency way up the income ladder — with growing education efforts following. America did what rich

societies tend to do well: make more of the scarce, highly rewarded thing. The new tech complemented educated workers and enriched them.

In *that* informational revolution, the computer didn’t replace the college graduates but instead made them more productive. *Today’s* infinite-generation and agentic-AI revolution might turn the tables on that dynamic; technological change is not obliged to remain skill-biased in the same way forever. Importantly, the authors find a minority role for AI in causing the falling premium; they find that wage growth in *AI-exposed occupations* has been weaker than elsewhere. Some **70 percent** of the skill premium contraction, they write, remains unexplained: competing explanations involve labor market tightness in low-wage sectors, market power, firm sorting, or shifts in remote work flexibility.

It shouldn’t surprise us either that college enrollment is stagnating as the premium has weakened, even though intuitively slower growth of college-educated labor shouldn’t coexist with falling wage premium for that labor. The difference is that potential college attendees make a rough estimate of lifestyle and lifetime income with or without a degree. In a digital world of AI and many nontraditional opportunities, they observe that what pays is excellence and value, not credentials.

In a version of the same question that every AI commentator has brought up in recent years, Azar, Giné, and Sanz-Espín conclude their paper by wondering whether generative AI will replace “high-cognitive tasks” (and thereby permanently reduce the returns to schooling) or just temporarily displace workers, which then “ultimately yields skill-reallocation productivity gains” for everyone.

Parents of college-age kids learned the wrong lesson from what the world had shown them during their lives: *send the kids to college and they’ll earn higher wages — paying back even eye-popping loans won’t be a problem.* College was the way to gain an advantage in a competitive labor market.

Parents of college-age kids learned the wrong lesson from what the world had shown them during their lives: send the kids to college and they’ll earn higher wages — paying back even eye-popping loans won’t be a problem. College was the way to gain an advantage in a competitive labor market.

College may still pay: The wage premium remains large. For decades, a college degree was associated with a more and more valuable kind of skill for a technologically hungry labor market. Then America produced millions of people with those skills, and now

AI is making some of the cognitive output abundant, too.

The question for the next generation is *which kinds of education* will prove scarce enough to command a premium and generate a positive return on educational investments, all things considered.

The Great Repricing of The College Degree

Paul Mueller
*Director of Defending Freedom, Combatting
 Collectivism*

No — or at least, not by the time they finish high school.

Depending on how they're funded, a Trump Account could turn a child into a decamillionaire by retirement, or it might just be worth about \$4,300 on their eighteenth birthday. As with any account, three variables dictate the outcome: contributions, rate of return, and time.

What might Trump Accounts actually be worth for children born this year? A thousand dollars takes a very long time to become a million dollars. That initial thousand dollars for children born during this administration could grow to be \$4,342.45 (**8.5 percent** annual return), \$5,122.17 (**9.5 percent** annual return), or \$6,032.83 (**10.5 percent** annual return) by the time they turn 18. That's nice, but not life-changing.

Does this mean Trump Accounts won't materially benefit a lot of kids? No. The magic of the numbers really comes from the basic principles of compound interest over long periods of time, not anything special or magical about the Trump Accounts themselves.

Extending the time horizon to retirement, however, is a different story. These Trump Accounts could be worth a lot if funded aggressively and left to compound over a lifetime. By the time a child born today reaches retirement age in 2093, that \$1,000 seed money could be worth: \$236,478.93 (**8.5 percent** annual return), \$437,266.28 (**9.5 percent** annual return), or a whopping \$804,030.69 (**10.5 percent** annual return).

Currently, Trump Accounts are limited to \$5,000 annually of individual contributions, but qualified general contributions do not count toward this. So Michael Dell's \$6.25 billion gift of \$250 per child toward 25 million accounts will not count against the \$5,000 annual limit. The claim about Trump accounts creating millionaires only works if one assumes the money compounds at an above market rate until the kids retire at age 67, or that they receive thousands of dollars of contributions into their account while children.

Maxing out the annual contributions (\$5000/year, \$90,000 over 18 years), however, will deliver impressive results. By the time they turn 18, those children will have a substantial endowment of \$200,957 (**8.5 percent**), \$222,078 (**9.5 percent**), or \$245,691 (**10.5 percent**) depending on their rate of return. Extend that another 50 years or so to retirement and we are talking real money: ~\$11 million (**8.5 percent**), ~\$19 million (**9.5 percent**), or ~\$33 million (**10.5 percent**)*.

These calculations don't account for inflation. Prices may be three and a half (**2 percent** annual inflation) to seven times (**3 percent** annual inflation) higher in 67 years. So

that eye-popping number of \$33 million (which will not be a common outcome) may only be worth the equivalent of \$4 to \$10 million in today's dollars. While **10.5 percent** is the historical long-term average annual rate of return for the S&P 500, it can vary quite a bit year to year and even decade to decade. More importantly, most children will not see maxed-out annual contributions to their accounts every year.

Becoming a decamillionaire requires \$5,000 contributions per child annually for 18 years — no small feat for most people. One of the architects of Trump Accounts, Brad Gerstner, however, believes that hundreds of billions of philanthropic dollars will flow into these accounts every year. Plus, these accounts may serve as a focal point for family and friends who want to contribute to children's long-term prosperity — much as grandparents of an older generation would give long-term Treasury bonds to their grandkids.

But there were already tax vehicles to invest money for your own kids, like 529 education savings accounts. Trump accounts were created to facilitate broad-based direct-transfer philanthropy. Billionaires now have a mechanism for giving money directly to millions of people without government officials or NGOs taking a big cut. The distribution of the Dells' gift just hit children's accounts this week.

Will there be widespread adoption of Trump accounts, and will people contribute to them regularly? Less than a month after the rollout, Secretary Bessent said over seven million children were enrolled — a promising start. Will billionaires contribute significant amounts of their wealth to millions of kids through Trump accounts? Michael and Susan Dell's \$250 per child gift, matched by Gerstner in Indiana and Dalio in Connecticut, has become a reality. And will Trump accounts provide a viable alternative to currently unsustainable entitlement programs like Social Security? These are a few very important questions that will determine how much Trump accounts impact American society.

It's true that Trump accounts, should they be held until retirement, could be worth impressive amounts of money, especially if people contribute every year their child is a minor. But 2093 is a long way off. Saving and investing for the far future is great. Parents will still have to decide whether sacrificing thousands of dollars today is worth tens or even hundreds of thousands of dollars in future decades.

* The account projections do not incorporate the program's permitted fund fees, which may be as high as **0.10 percent** annually. Even a small fee matters over 67 years.



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