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Buried alive in 'Businessweek'

Things have come to such a sorry pass for the ancient scourge of paper money that *Bloomberg Businessweek* has written its obituary. Inflation is dead, declares the cover of the April 22 edition (Hank Blaustein renders the image below). "Dormant" is in fact the word, as we are about to demonstrate.

Businessweek isn't wrong to ask what happened to the consumer price index. Even the central bankers are feeling sorry for it, rooting it higher. They want it, or, technically, the core personal consumption expenditures index, to rise by 2% or more per annum. Pretending not to hear, the index drags its feet like a boy on his way to the dentist. In only two months in the past seven years has the core PCE hit the aspirational 2%.

Such a record used to define monetary-policy success. Now it's the mark of failure. "Lowflation," *Businessweek* argues, is a consequence of globalization, automation and de-unionization, to which might be added excessive debt and Bezos-ization.

The author of the story, Peter Coy, contends that a spot of inflation "greases the wheels of commerce." In this, he echoes the advocates of the "creeping" inflation in the 1950s. Then, too, he adds, "some inflation is also useful to central banks because it helps them fight recessions."

The central bankers' confidence on this score is apparently limitless. They do actually contend that they can generate "some" inflation, stopping just where they intend to stop. When asked at a press conference in March "what kinds of challenges" a subpar rate of debasement presents to the supposed guardians of the integrity of the currency, the Fed chair, Jay Powell, replied, "It's a major challenge. It's one of the major challenges of our time."

Expanding on his boss's remarks, Charles Evans, president of the Federal Reserve Bank of Chicago, last month advocated bumping up the inflation target by a few tenths of a percent. "Indeed," said Evans, "I would communicate comfort with core inflation rates of 2.5%, as long as there is no obvious upward momentum and the path back toward 2% can be well-managed."

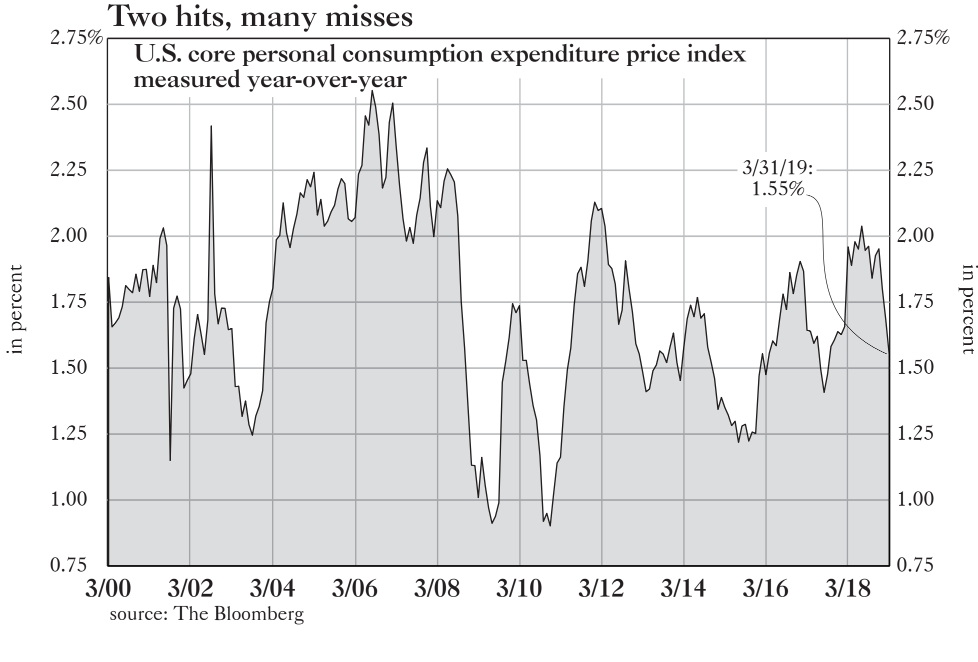
Few have paid a higher compliment to the technical prowess of the inflation ferrets at the Bureau of Labor Statistics than Evans does with that proposal to fine-tune the price target. Calculating price indices is rough and ready work. The price inspectors must avoid sampling error. They must not impute product-quality improvements where none exists. They must make allowances for cases in which today's 15 cookies cost what yesterday's 16 did (clever packaging obscures the shrinkflation).

Considering the margin for error—no less real for it being unacknowledged—you wonder if there's a meaningful difference between a 2.0% and 2.3% rate of inflation? Or even between 2.0% and 2.5%?

Evans implies that the Fed controls the rate. Another Chicagoan, Milton Friedman, positively asserted that it does. But hear Chair Powell in congressional testimony on Feb. 26: "In our thinking, inflation expectations are now the most important driver of actual inflation."

Inflation, then, has become a metaphysical phenomenon, not a monetary

Two hits, many misses



source: The Bloomberg

one. To generate more of it, the Fed must lower the people's confidence in the purchasing power of money.

It's a funny kind of ambition for a central bank—no stranger would be a pro-measles edict from the National Institutes of Health. Anyway, in the short run, is such precision feasible? Inflation expectations, observes James Bianco, founder and namesake of Bianco Research, LLC, besides being hard to measure, track not the things that the Fed controls but the squiggles in the crude-oil price chart. As much as the Federal Open Market Committee may wish to regulate the price of oil (see page 3) or meat (the latter now under a heavy inflationary threat from a pig virus in China), such exogenous events are customarily under the control of the Author of the Universe, not the economists.

In December 1965, Gardner Ackley, chairman of the Council of Economic Advisers under President Lyndon Johnson, gently reproved *The Wall Street Journal* for harping on news of rising prices. How slight were the rises! Since the bottom of the prior recession, in March 1961, Ackley pointed out, the CPI had increased by just 1.2% a year. Wholesale prices had scarcely budged. Indeed, the president's economist was able to observe, "In our whole history since the 1710s, there has been no similar period of wholesale price stability." He meant it as a good thing.

Then Ackley added the following words, anticipating the supply-side arguments of Stephen Moore, President Trump's nominee to the Federal Reserve Board:

> On many occasions in the past several years, we have been urged to buy insurance against inflation by slowing down the expansion of overall demand. Had we taken this advice we would have sacrificed the unprecedented gains in consumer living standards, the amazing expansion in jobs, the remarkable upsurge in profits and the fine productivity record which has brought such great rewards to the entire nation. Fiscal and monetary policy today must proceed with even more care than in the past. But we do not need to throw the economy into reverse.

Ackley's essay, which ran out under the headline, "Prospect of Avoiding Inflation Is Good," was dated Dec. 13, 1965. It bottom-ticked the rate of inflation for the next 33 years. Not until 1998 did the CPI record a yearly gain as low as the 1.6% registered in 1965. The prospect of "avoiding inflation" turned out to be very bad indeed.

One lesson to draw from these long-ago events is that low inflation does not necessarily presage even lower inflation. "It all depends," one could say, though on what it depends is clearest in retrospect. Looking back, there's no mistaking the building inflationary forces of the mid-1960s. The baby boomers were coming of age, the Vietnam War was hotting up, the dollar exchange rate (then fixed in terms of gold, an ounce costing you $35) was coming under well-deserved pressure, the Bretton Woods monetary system was on its last legs. Few connected the dots at the time.

And now? The best case for a new, unscripted inflation is how impossibly unlikely it appears, even in the context of today's cyclically incongruous budget deficits and a decade's worth of monetary improvisation. Still, analytical minds will want to know more. They will ask, What is the cause of inflation in 2019?

The eternal cause of inflation is the loss of confidence in money, the very thing the central bankers now say they want to bring about. The fundamental cause of that loss of faith is a persistent excess of aggregate demand over aggregate supply, with credit, not savings, financing the inflationary increment of spending. That condition, too, would seem to be in place, given the prospect of a $1 trillion federal deficit during a more-than-satisfactory business expansion.

If the measured rate of inflation continues to fall short of expectations, it wouldn't be the first time. "The deficits in the last three years, while believed to have spurred the economy, have clearly not been inflationary," *The New York Times* reported at the close of the 1964 fiscal year. "The wholesale price index is the same as it was six years ago." For the calendar year, the CPI would rise by just 1.3%. (We leave for another day a discussion of the differences in computing that index then and now.) In 1964, too, it seemed that inflation had gone to heaven.

The *Businessweek* argument for the death of inflation boils down to the contention that aggregate demand will never exceed aggregate supply by a margin sufficient to strain the limits of domestic production (and no unwanted surplus of dollars will again cause a material depreciation in the dollar exchange rate, therefore a material boost in the prices of imported goods). Yet a dozen Democratic presidential hopefuls, promising free college tuition, debt forgiveness, universal health care and more, might as well be running on a platform called "No limits."

In a 1957 essay entitled "Welfare, Freedom and Inflation," the German economist Wilhelm Röpke argued that inflation is an "illness of money" and that it "appears as a moral and a social disease."

In America, in 1957, the CPI flared to a 3.3% rate of rise, but consumer prices had climbed by 0.3% in 1954 and fallen by the same percent in 1955; they had increased by only 1.5% in 1956 and would ascend by 2.7% in 1958.

"Only" was not the word that Röpke used to characterize a sub-2% rate of inflation. He decried a "creeping, chronic condition of continually declining money values which becomes steadily more apparent; a 'cold inflation' which, without rising to fever pitch or showing other alarming symptoms, is for that very reason all the more dangerous. This problem is quite rightly beginning to overshadow all others."

Now Jay Powell calls the shortfall of inflation from the Fed's 2% goal "one of the major challenges of our time." Much has changed in monetary affairs in the past two generations. The repositioning of the central bankers as advocates of depreciating currencies is a change for the history books.

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