

# ***THE FOUR ADDICTIONS***



***The Challenge of Breaking Hard Habits in the 2020s***

# SUMMARY



## The Four Addictions



Over the first two decades of the 21<sup>st</sup> Century, the U.S. (and world) grew increasingly dependent on:

- **China** (for manufacturing, supply chains & deficit financing)
- **Digital** (as everything digitized, networked & automated)
- **Easy Money** (as low interest rates & QE persisted without serious inflation)
- **Debt** financing (as institutions spend more than they took in)

While each trend offered significant upsides, unaddressed downsides are increasingly problematic.

**These dependencies are becoming unsustainable**, but they're hard habits to break. Policies to address any one could worsen the other three.

**The central policy & political challenge of this decade is kicking these four addictions without crashing economies, stifling innovation or provoking wars.** Solutions exist, but they're not easy.

# THE FOUR ADDICTIONS

Addiction:



Upsides:

Disinflationary / new markets, faster growth

Faster innovation, productivity, efficiency

Depressions-avoided / asset values protected

Hard choices avoided, spend AND cut taxes

Downsides:

Dangerous dependencies

Ignored externalities

Excessive risks / asset bubbles

Mortgaging the future

Why Unsustainable:

U.S.-led world order in peril

Weapons of mass disruption ubiquitous

Inflation crushes growth & savings

High interest payments starve other spending

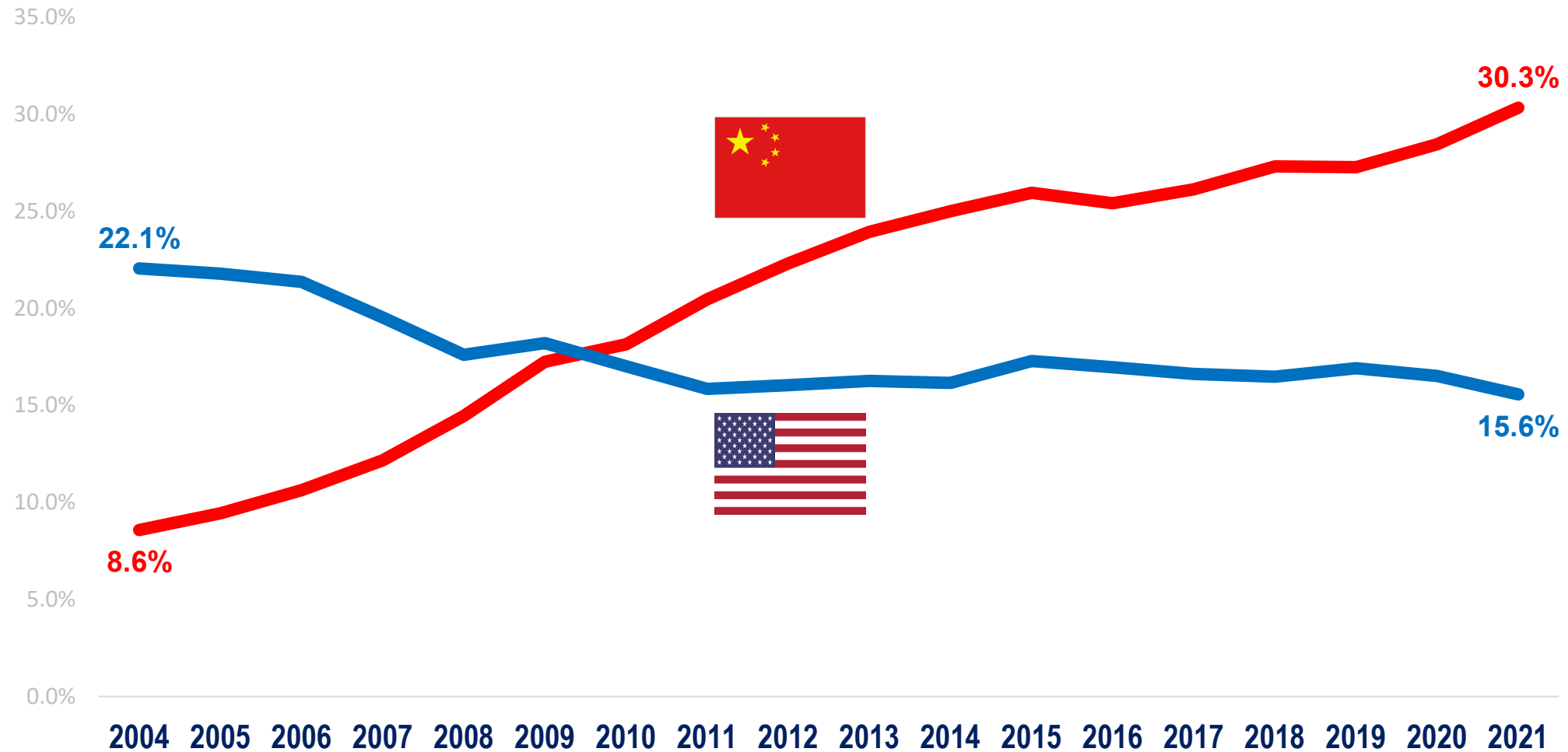


# CHINA

**Excessive Dependencies on an  
Increasingly Unreliable Competitor**

# THE TREND: CHINA BECAME THE WORLD'S FACTORY

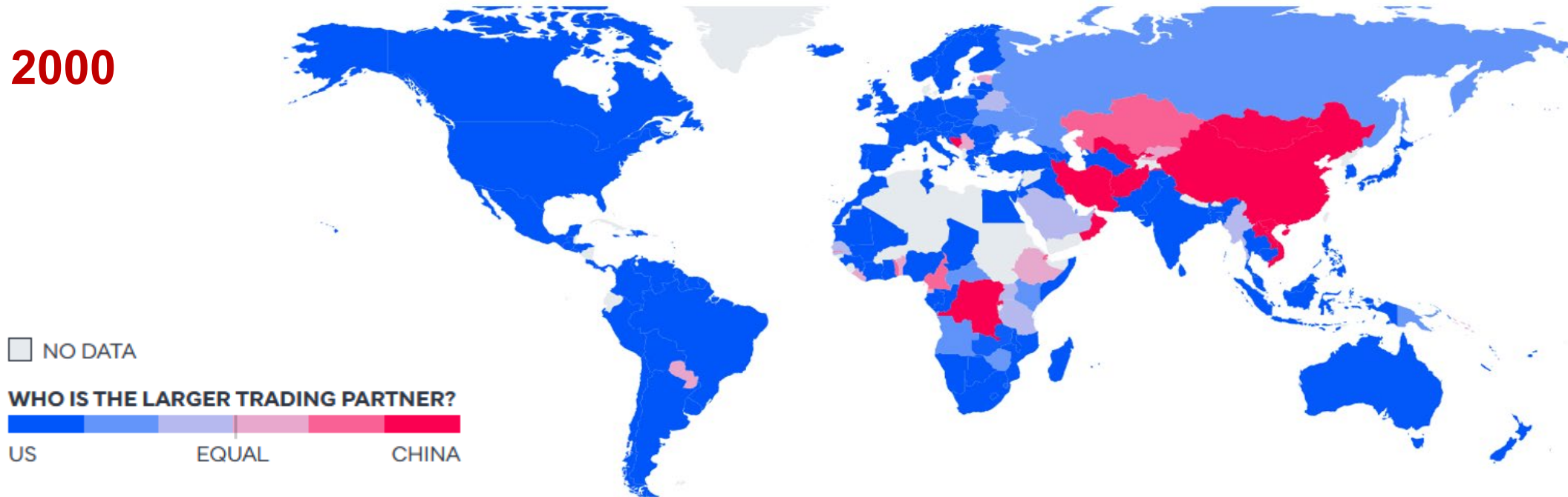
## Share of Global Manufacturing Value-Added





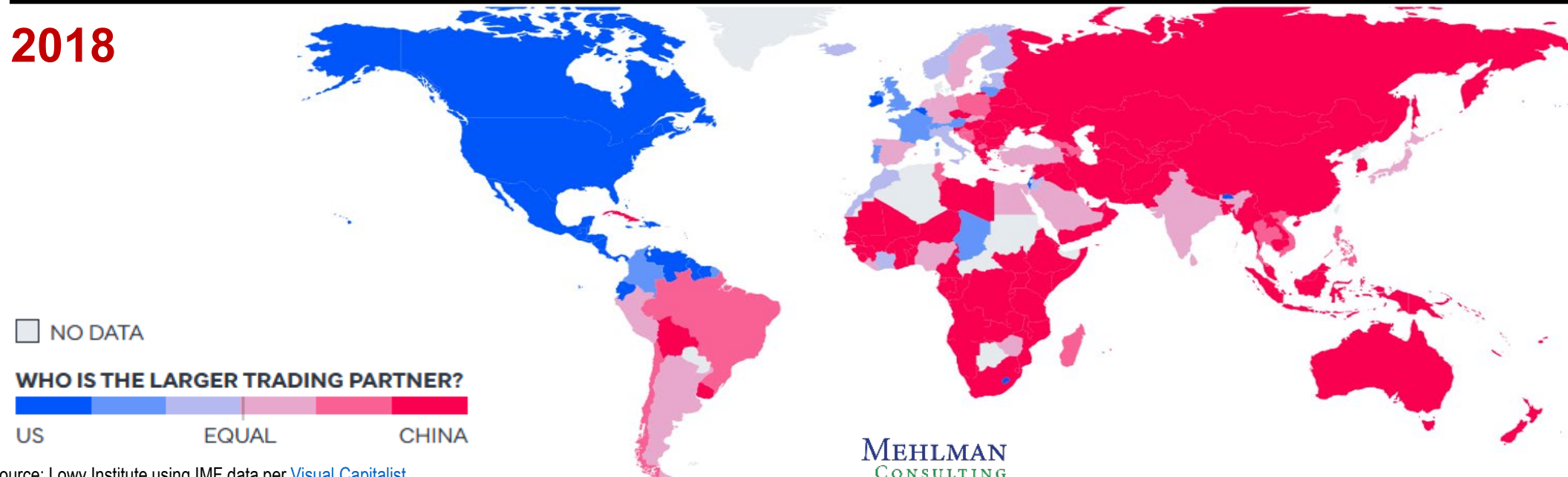
# THE TREND: CHINA BECAME WORLD'S TOP TRADING PARTNER

2000



U.S. was #1 trading partner to over 80% of nations

2018



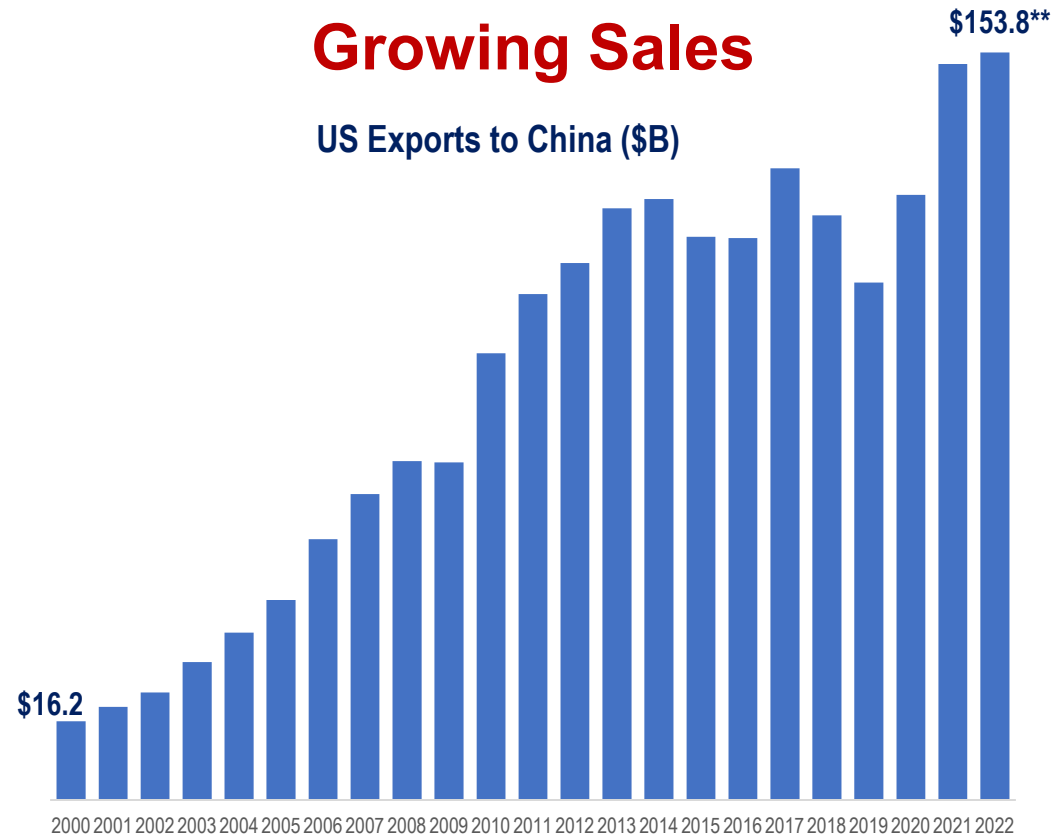
China was #1 trading partner to over 67% of nations (U.S. ~30%)

# UPSIDES OF ENGAGING WITH CHINA

## Cheaper Goods / Lower Inflation



## Market Access / Growing Sales



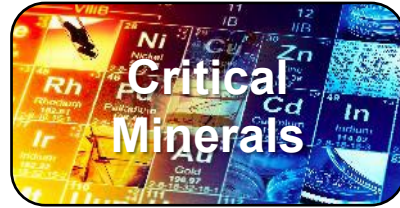
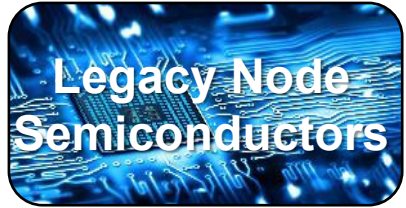
\*\* Only Canada & Mexico bought more from the U.S. in 2022

## Big Workforce / Efficient Production



# DOWNSIDERS: DEPENDENCIES, DEFICITS & DISREGARDED VALUES

## Dangerous Dependencies Grew



## Bilateral Trade Grew Extremely Unbalanced

2000 2001 2002 2003 2004 2005 2006 2007 2008 2009 2010 2011 2012 2013 2014 2015 2016 2017 2018 2019 2020 2021 2022

U.S. trade balance with China



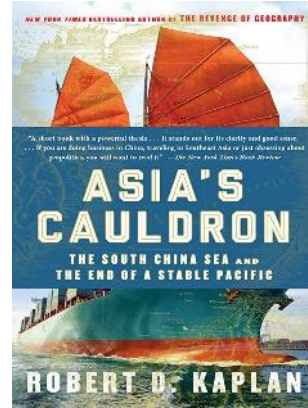
## Basic Values Disregarded





# WHAT CHANGED / WHY UNSUSTAINABLE

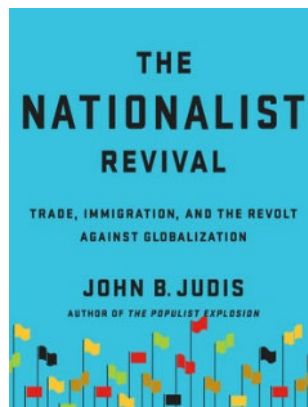
**China Became  
More Aggressive**



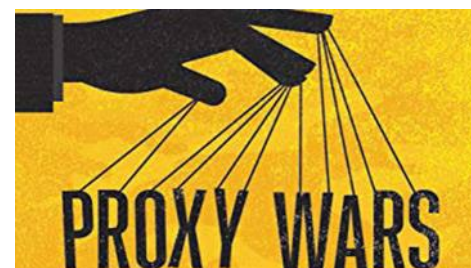
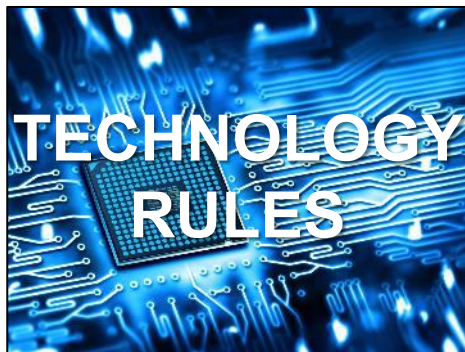
**China Became  
More Repressive**



**Frictions Rose Amid  
Global Events**



## Battlefields of the New Cold War





# THE POLICY: U.S. CHINA CRACKDOWN WILL DRIVE PAIN... AND OPPORTUNITY

## BUSINESS PAIN

- Tighter Tech Export Controls
- Outbound Investment Restrictions
  - Limits on Cross-Border Data
- Propaganda Transparency & Ban
  - Supply Chain Decoupling
  - Defense Deals & Strategy
  - Human Rights Liability
- Retaliation by China in China

## BUSINESS OPPORTUNITY

- Domestic Supports (eg CHIPS)
- On- / Near-Shoring Incentives
  - Help vs Unfair Competition
- New Regional Economic Alliances
- Military Buildup & Contracts
- Infrastructure Improvements
- Stronger IP Enforcement
- Return of Manufacturing Base

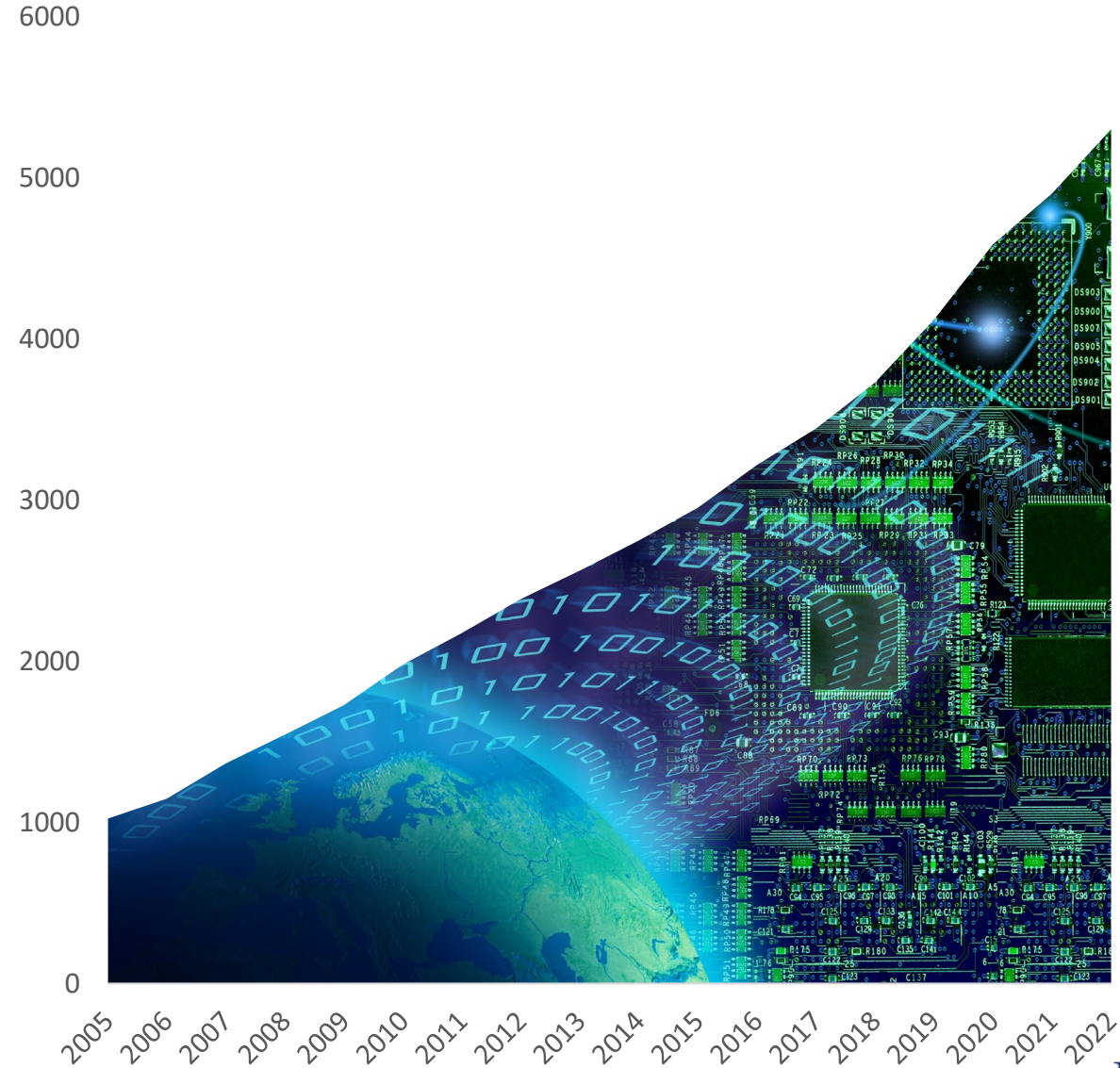
# DIGITAL

**Growing Power & Availability of Emerging  
Tech Make Risks Too Big to Ignore**

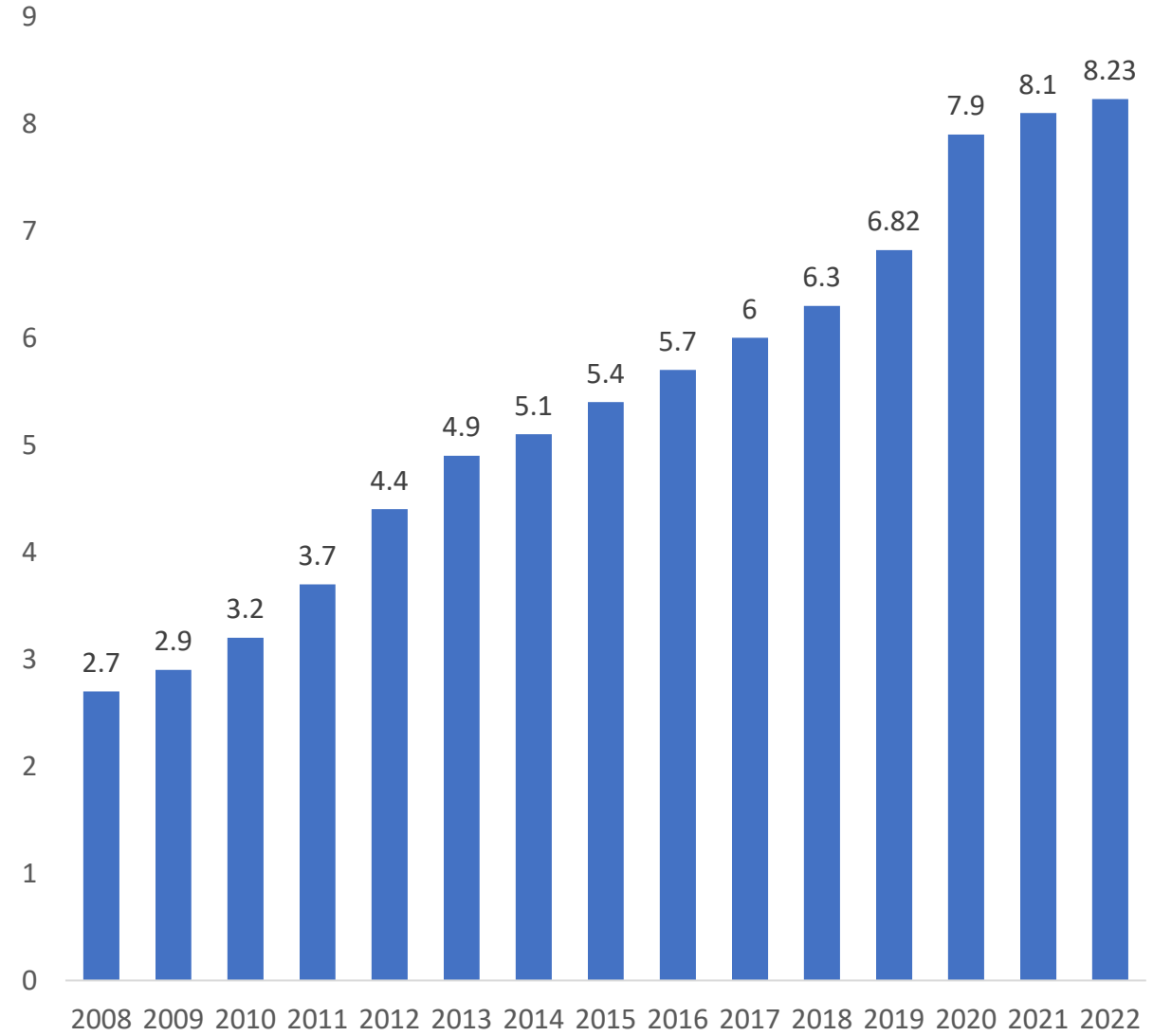


# THE TREND: EVERYONE, EVERYWHERE, ALL THE TIME

## Global Internet Users (M)



## Americans' Daily Hours Online



# UPSIDES: BETTER, SMARTER, FASTER

## The Digital Revolution Continues to Drive Immense Benefits

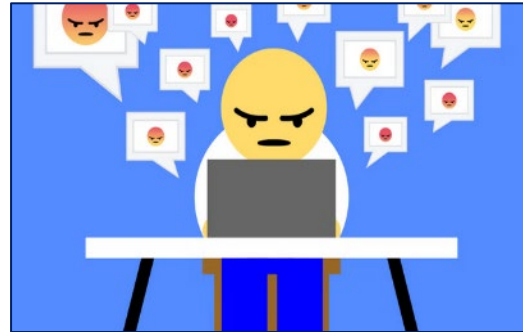


# DOWNSIDERS: GROWING NEGATIVE EXTERNALITIES

## Spreading Misinformation



## Monetizing Outrage



## Increasing Vulnerability



## Displacing Jobs



## Destabilizing Markets



## Invading Privacy



## Depressing / Addicting Kids

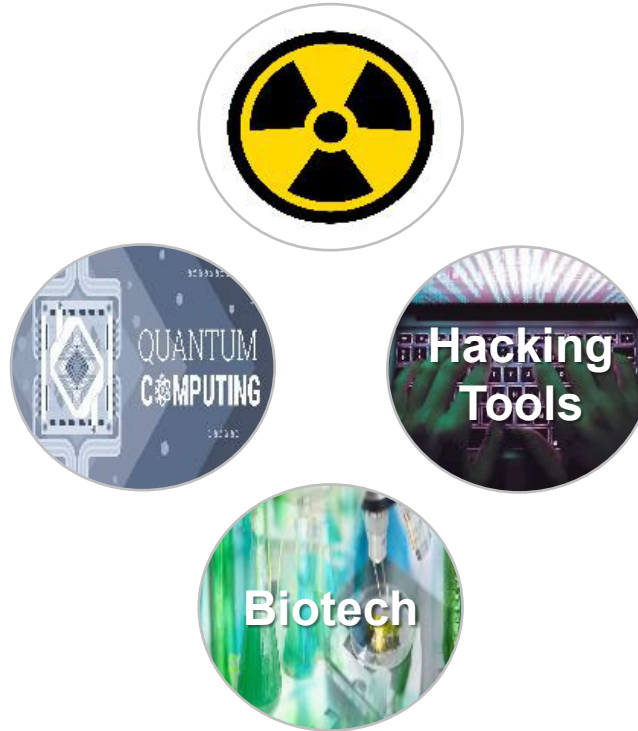


## Emerging Tech (esp. AI) Is Both Ubiquitous & Powerful

### UBIQUITOUS TECH (Power restricted)



### VERY POWERFUL TECH (Access restricted)






### POWERFUL & UBIQUITOUS (Minimal restrictions)



























# WHAT'S NEXT / POLICY: PUSH TO REGULATE... EVERYWHERE, ALL THE TIME

## Regulatory Posture

-  Aggressive
-  Moderate
-  Minimal

## Efforts to Regulate Tech by Government Expanding



ISSUES	EU	US Agencies	Blue States	Congress	Red States	China
<b>CONSUMER PROTECTION</b> <i>(Privacy; Kid safety; Content moderation/230; Crypto; Addiction)</i>						
<b>COMPETITION POLICY</b> <i>(Antitrust laws &amp; merger reviews; App stores; data porting)</i>						
<b>NATIONAL SECURITY</b> <i>(Export / import controls; Cyber; FDI limits; Supply chain)</i>			N/A		N/A	
<b>SOCIAL COMPACT</b> <i>(AI rules; Tax; Digital divide; Labor / Gig economy; Bias)</i>						

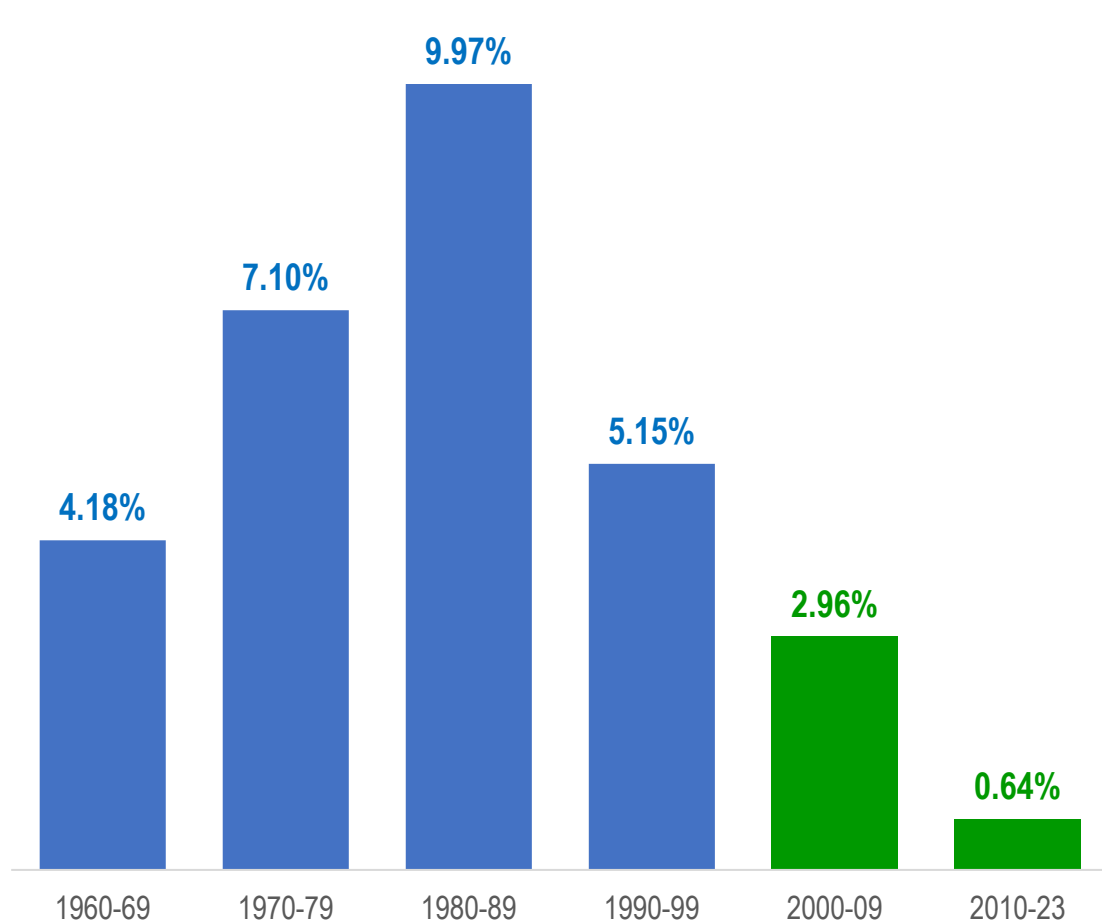
# EASY MONEY

**Return of Inflationary Forces  
Portends a Long Unwinding Road**

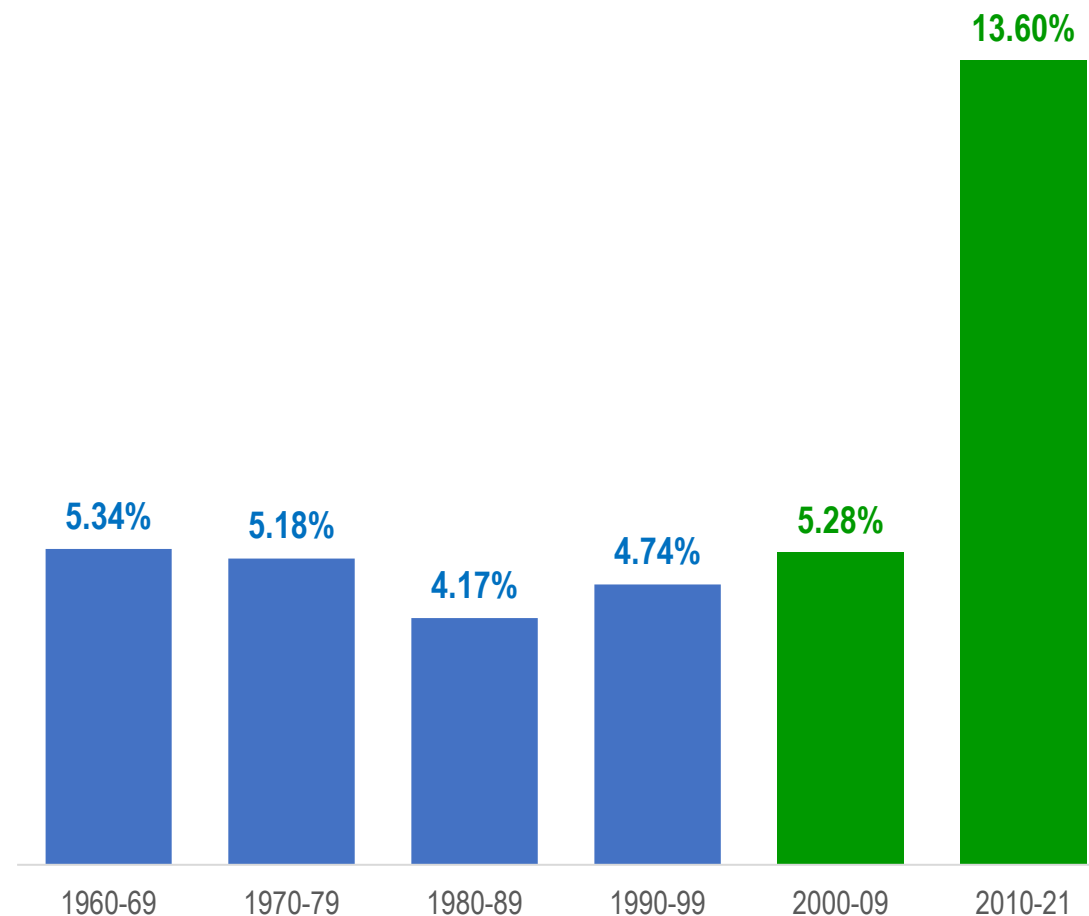
# THE TREND: HISTORICALLY-LOOSE MONETARY POLICY

**Low Rates + Quantitative Easing = Unprecedented Era of Easy Money**

## Federal Funds Rate

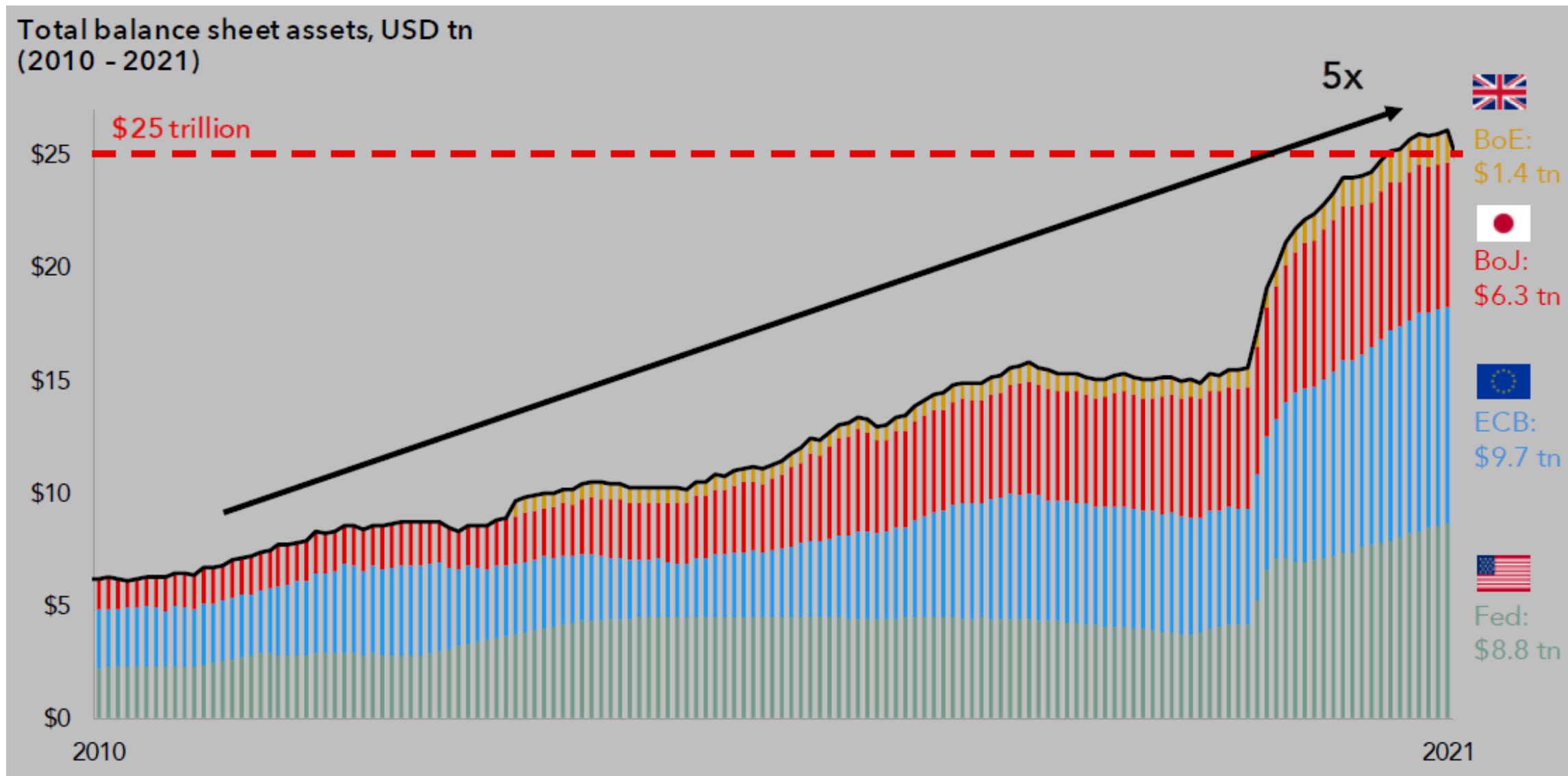


## Central Bank Balance Sheet (% GDP)



# THE TREND: NOT JUST THE UNITED STATES

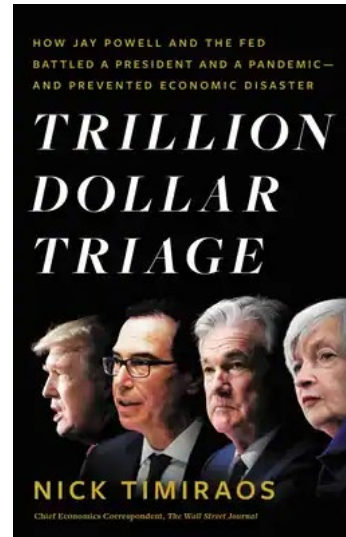
## Top Central Banks' Balance Sheets Up 500% Since 2010



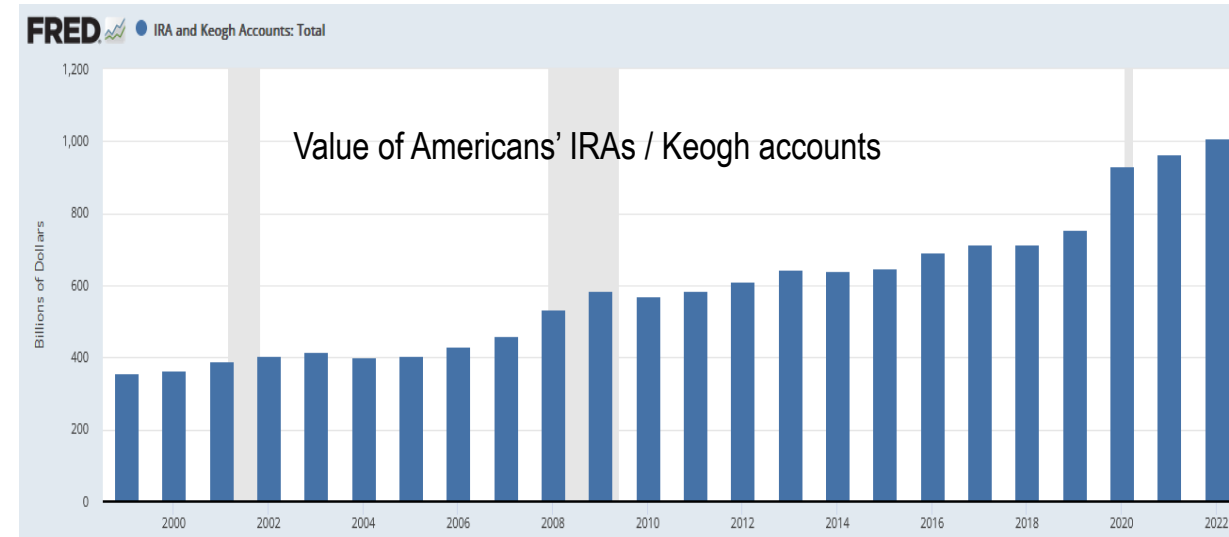


# UPSIDES: DISASTERS AVOIDED (OR JUST DEFERRED?)

## Prevent Depressions



## Protecting Investors

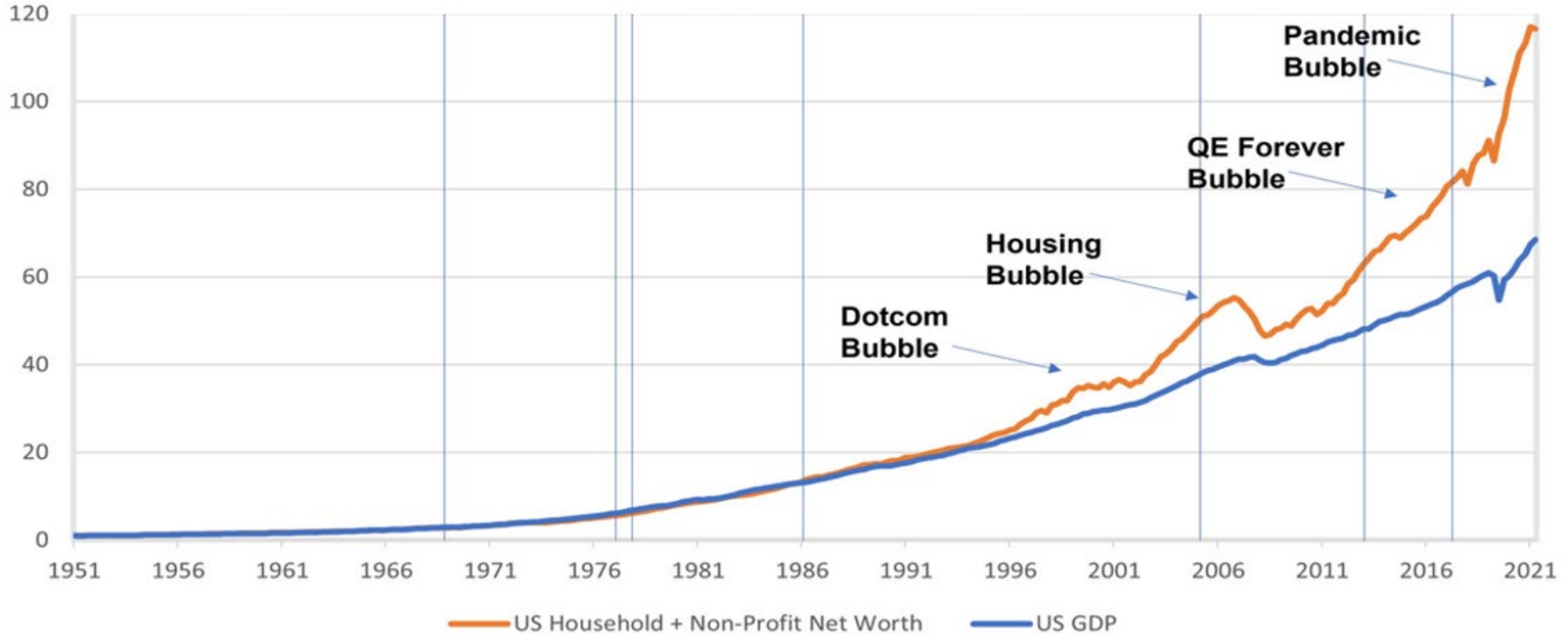


# Downsides: Asset Bubbles Grew As Investors Sought Yield

## U.S. Wealth Growth vs. U.S. GDP Growth

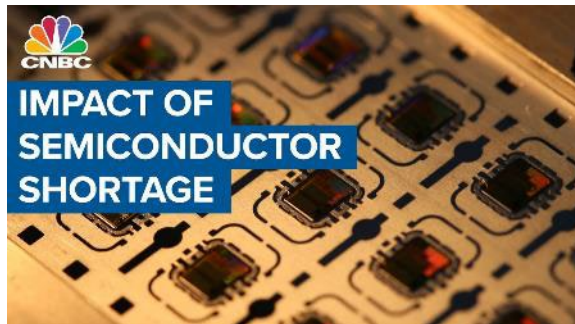
Oct. 1951-Jan. 2022

(Nominal USD, Oct. 1951 = 1)

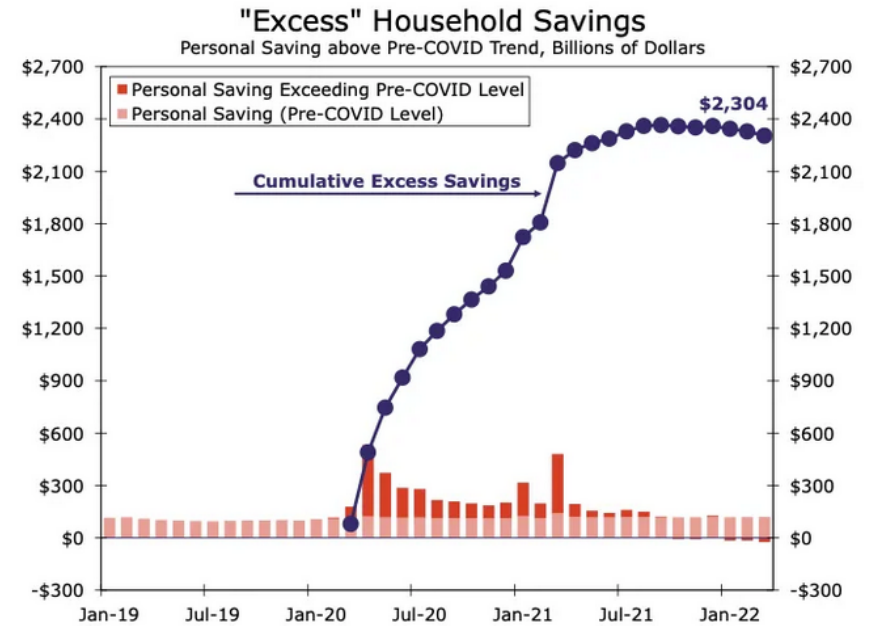


# WHAT CHANGED

## Supply Shocks



## Demand Shocks



Source: U.S. Department of Commerce and Wells Fargo Economics



# WHY UNSUSTAINABLE: BRAVE NEW INFLATIONARY WORLD

## Macro Trends Enabling Easy Money (2000-2020) Are Reversing (2020-2030)





## Two Decades of Easy Money Built a Fragile World



# THE POLICY: DEFINING THE NEW NORMAL (AND STICKING TO IT)

## Reducing Moral Hazard



## Reassessing Systemic Risk



## Managing Higher Rate Fallout

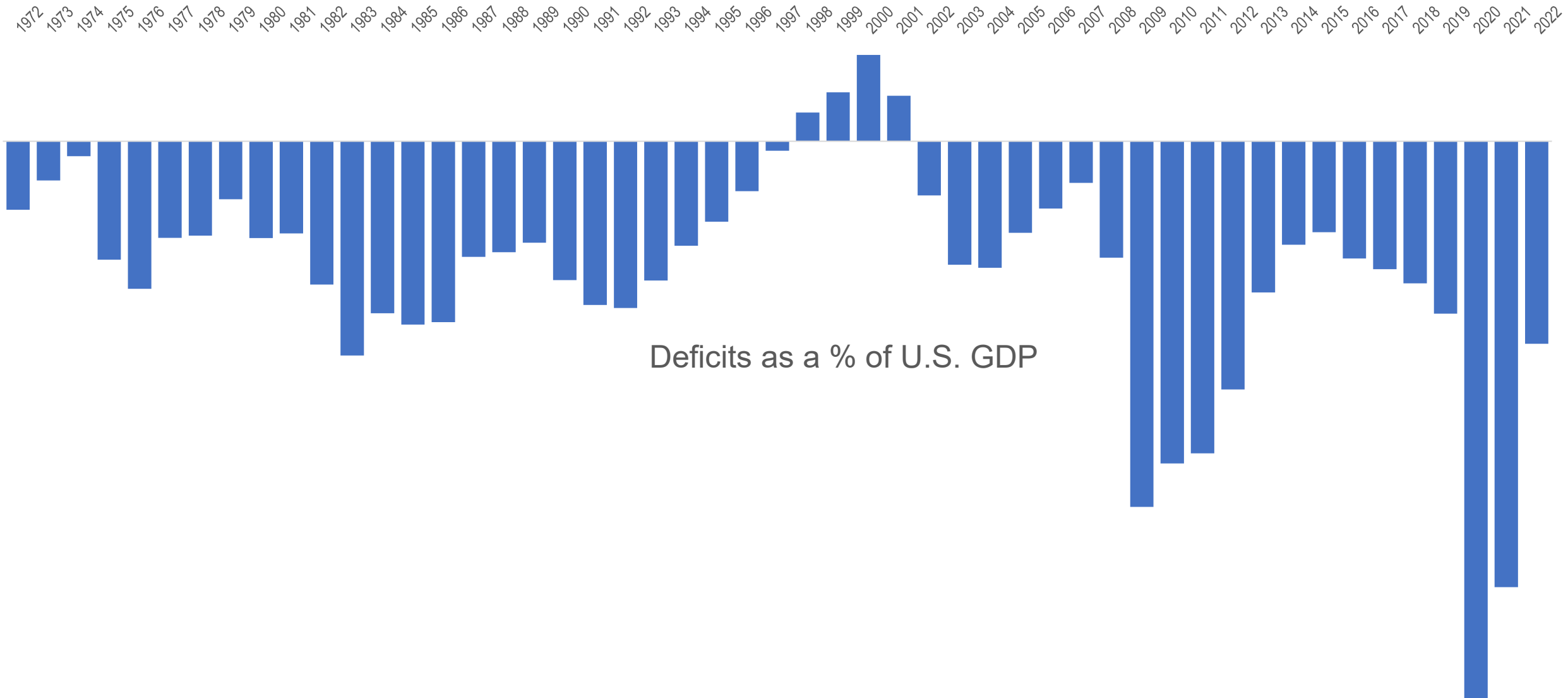


# DEBT

**Unsustainable Economics May Soon  
Force Hard Choices**

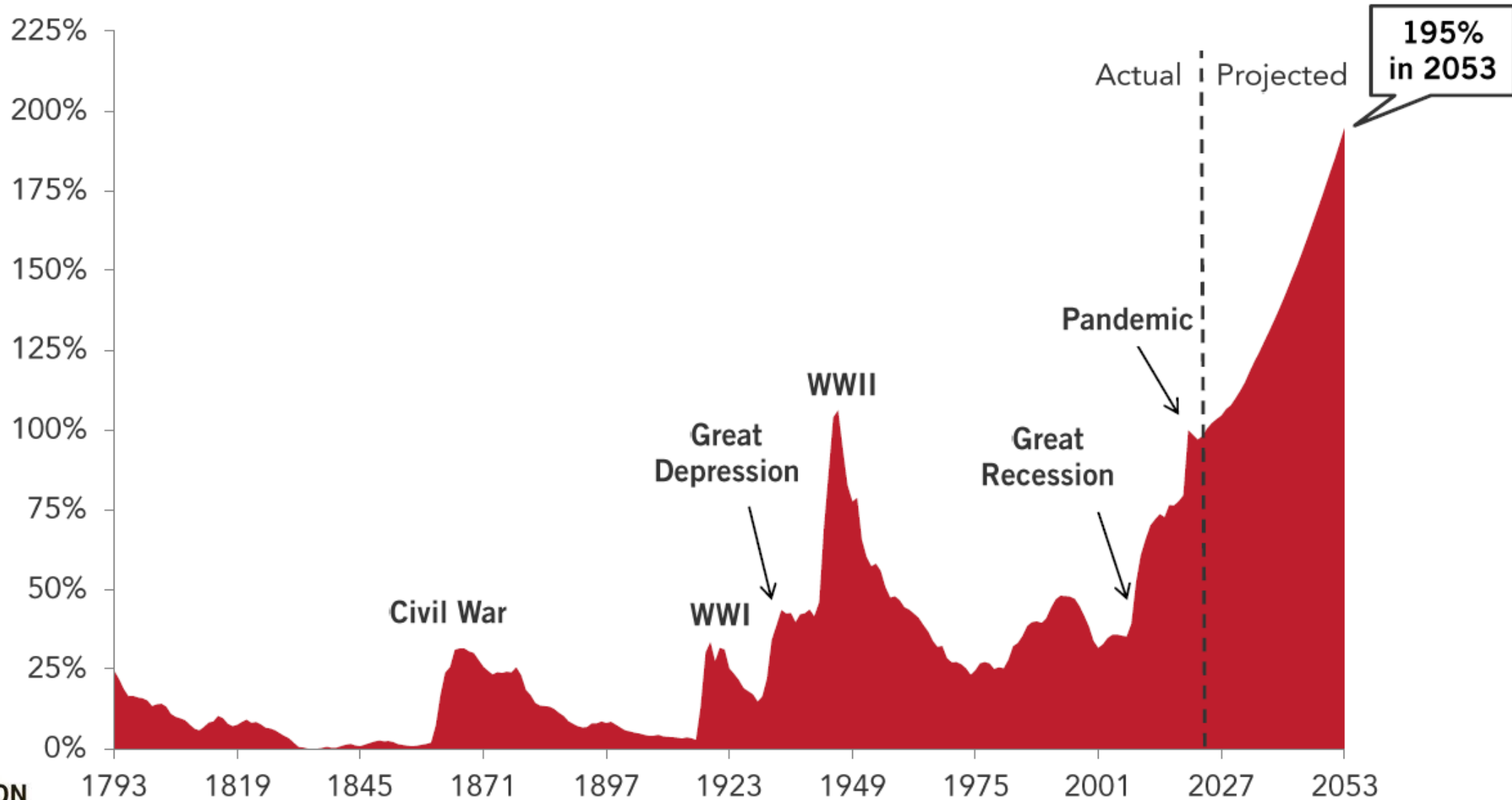
# THE TREND: U.S. HAS NOT LIVED WITHIN ITS MEANS

## 50 Years of Deficits Under Democrats & Republicans, in Peace & at War



# THE TREND: FEDERAL DEBT NOW EXCEEDS WARTIME LEVELS

## Debt Held by the Public (% GDP)





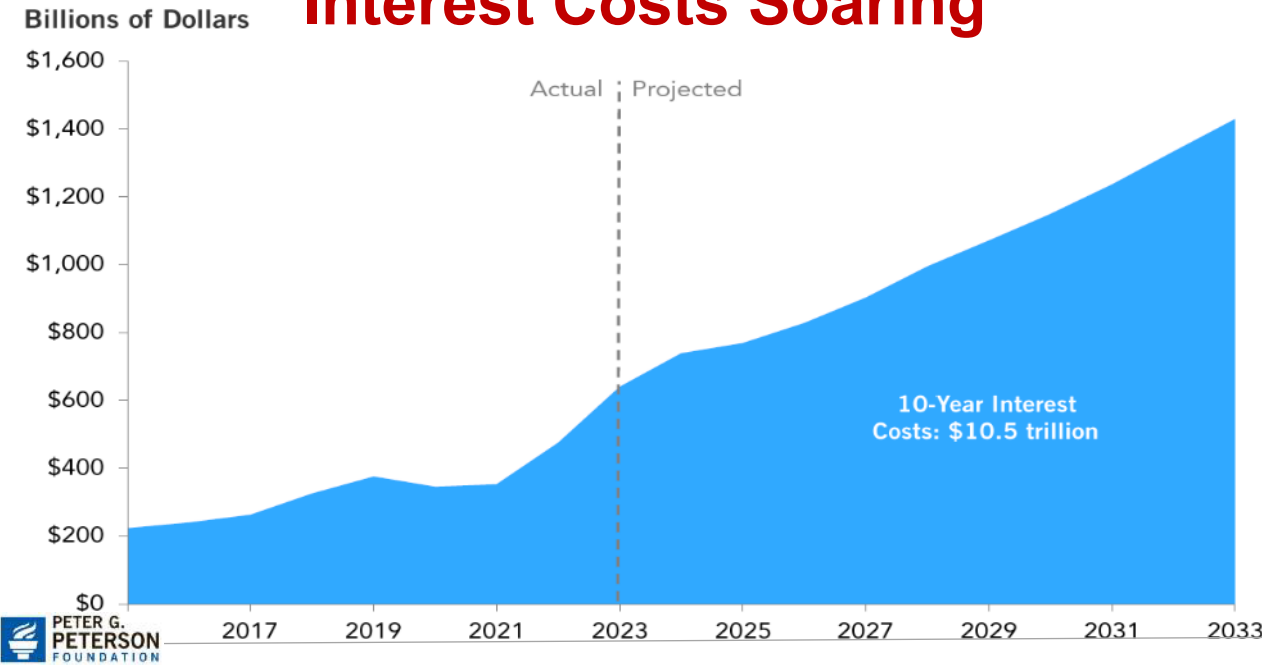
# UPSIDES: HARD CHOICES AVOIDED (DEFERRED)

## Two Decades of Funding Military, Expanding Entitlements, Rescues & Tax Cuts

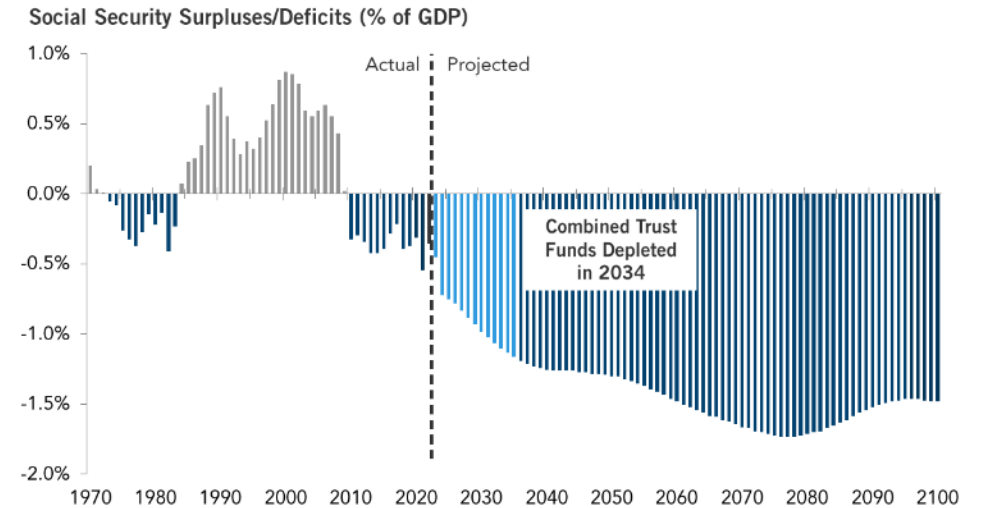


# DOWNSIDERS: BILLS ARE COMING DUE

## Interest Costs Soaring

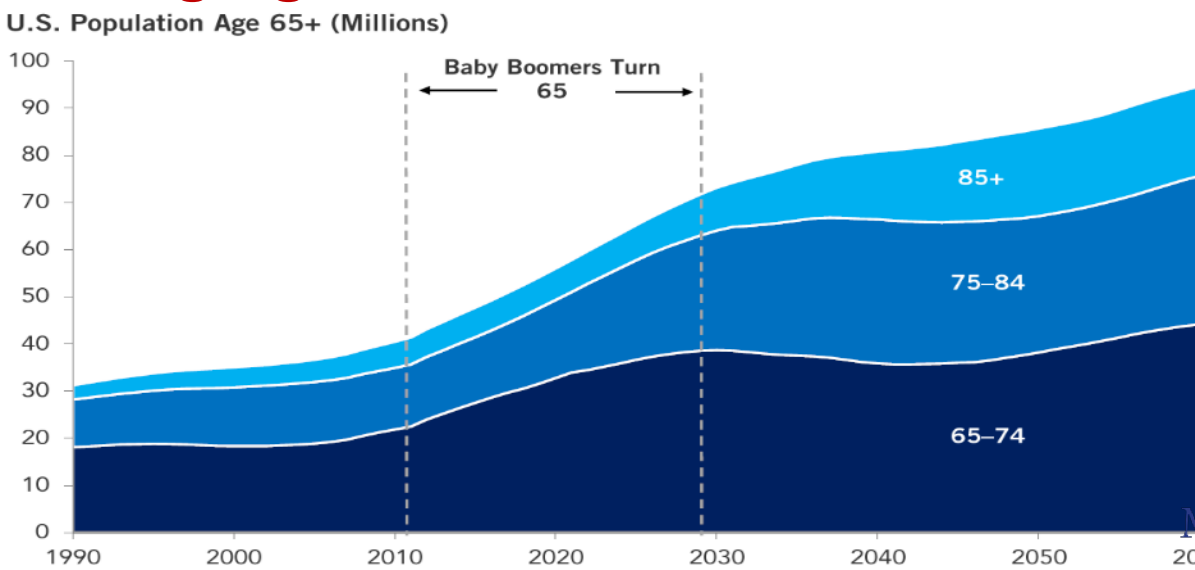


## Social Security Trust Fund Depleting

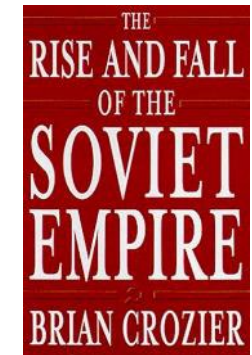
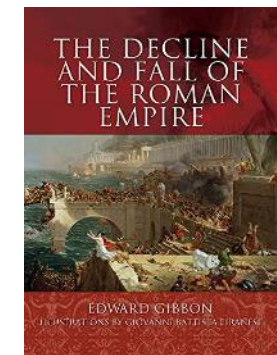
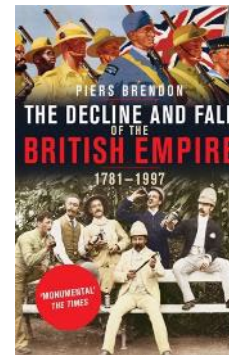


SOURCE: Social Security Administration, The 2023 Annual Report of the Board of Trustees of the Federal Old-Age and Survivors Insurance and Federal Disability Insurance Trust Funds, March 2023.

## Aging Boomers Will Tax Medicare

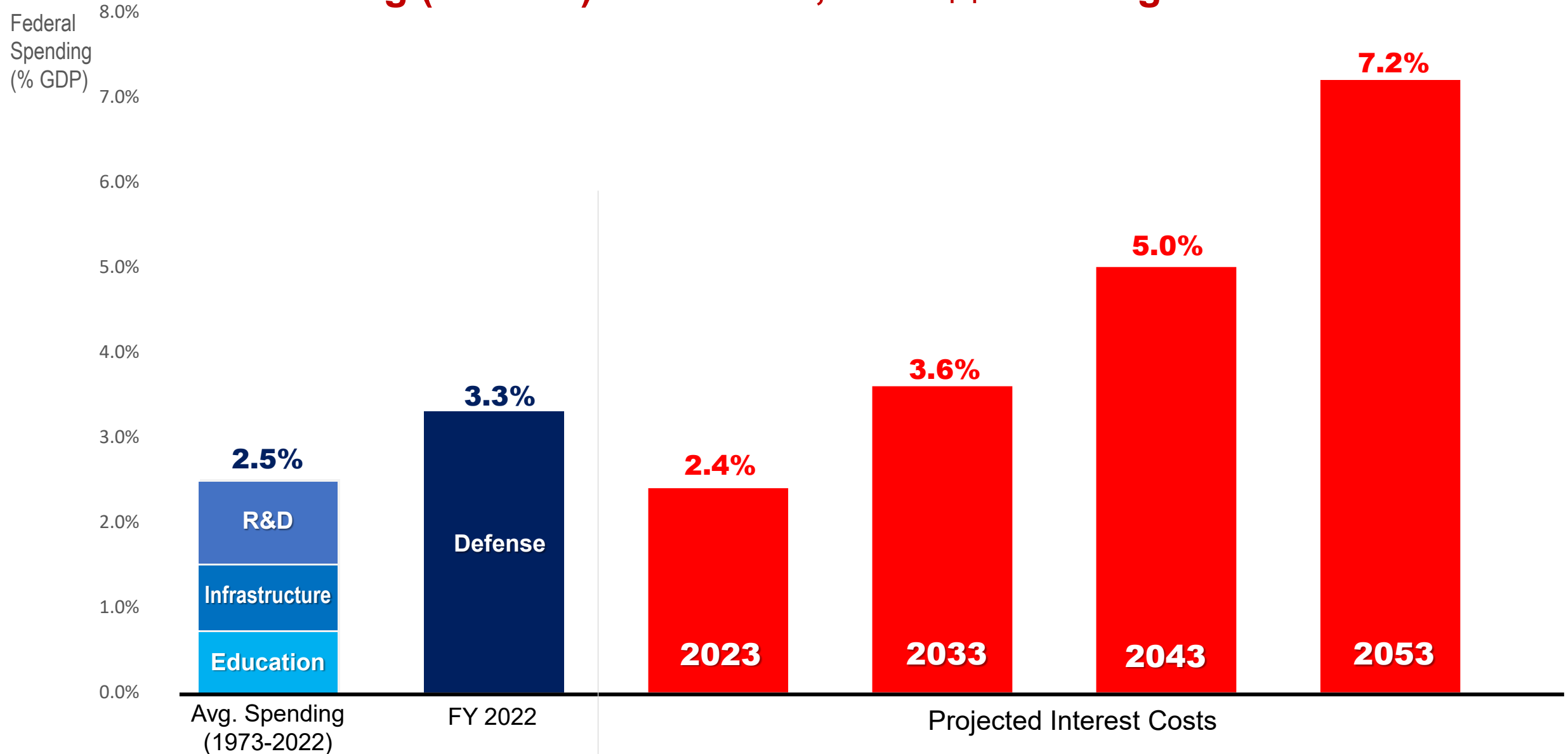


## Debt Drove Imperial Declines



# WHY UNSUSTAINABLE? INTEREST COSTS CROWD OUT OTHER PRIORITIES

## As Debt Servicing (Interest) Costs Rise, Less \$\$ for Long-Term Investments



## The 2023 Debt Ceiling Showdown



June 1

Both sides believe they're right.

Both sides believe they're winning.

Both sides believe the other will blink.

Both sides believe failure hurts the other worse.

There will be a deal, but...

...before the pain or after?



# THE POLICY: HARD CHOICES AHEAD

## Options to Reduce Federal Debt

### INCREASE REVENUE



Reduces growth,  
investment & innovation

### REDUCE SPENDING



Shrinks safety nets &  
investments in the future  
*(Defense, R&D, Education, Climate)*

### INFLATE CURRENCY



Crushes savers, reduces  
investment & increases  
interest costs on debt



# CONCLUSIONS

**Reasons for Despair,  
Reasons for Hope**

# NO WAY OUT?

## Solutions to Each Challenge Could Make Solving the Others Harder

FIX CHINA	FIX DIGITAL	FIX EASY MONEY	FIX DEBT
<ul style="list-style-type: none"> <li>Accelerate tech champions</li> <li>Restrict trade / decouple</li> <li>Invest more (DOD, R&amp;D)</li> </ul>	→ <b>Harder</b>		
		→ <b>Harder</b>	
			→ <b>Harder</b>
<b>Harder</b> ←	<ul style="list-style-type: none"> <li>Slow tech “champions”</li> <li>Accept lower efficiency</li> <li>Spend more on govt regs</li> </ul>	→ <b>Harder</b>	
			→ <b>Harder</b>
<b>Harder</b> ←		<ul style="list-style-type: none"> <li>Less decoupling / trade</li> <li>Maximize productivity</li> <li>Raise interest rates</li> </ul>	
	<b>Harder</b> ←		→ <b>Harder</b>
<b>Harder</b> ←			<ul style="list-style-type: none"> <li>Invest less (DOD, R&amp;D)</li> <li>Spend less on govt regs</li> <li>Slow interest rate hikes</li> </ul>
	<b>Harder</b> ←		
		<b>Harder</b> ←	

# REASONS FOR HOPE

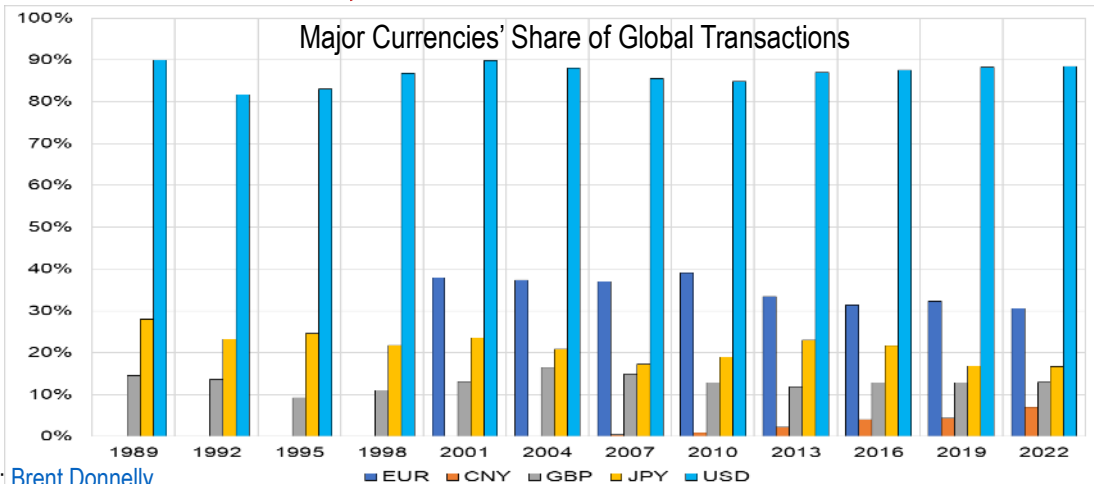
## CHINA: Neither Side Wants War, Both Have Lots to Lose



## DIGITAL: Productivity Gains Likelier than Robot Enslavement



## EASY MONEY: “Exorbitant Privilege” Persists, Dollar Still Dominates



## DEBT: Past 6 Presidents cut spending deals with hostile Congresses



## The Solutions Are Known... Just Hard to Implement



### CHINA → Constrain & Contain, But Don't Corner

- Limit trading that helps China's military or maintains dangerous dependencies
- Expand trading with allies & regional military coordination
- Maintain communications & economic engagement to make space for reform



### DIGITAL → Regulate, Don't Suffocate

- Seek greater transparency & awareness of emerging technologies' benefits & risks
- Push for greater accountability from tech creators & distributors
- Maximize national standards & global harmonization



### EASY MONEY → Reset Expectations, Don't Revert

- Reassess & specify what's too systemically-important to fail... add guardrails
- Privatize losses where privatized gains... allow failures



### DEBT → Reform Together, Don't Fall Apart

- Compromise to avoid default, economic / market meltdown
- Ensure entitlements are sustainable long-term
- Invest in U.S. workforce productivity



# DOOMSAYERS GONNA DOOMSAY

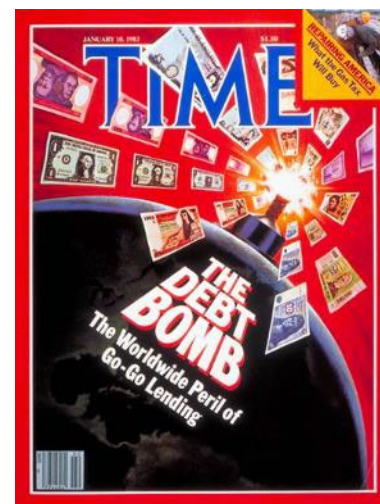
1973



1980



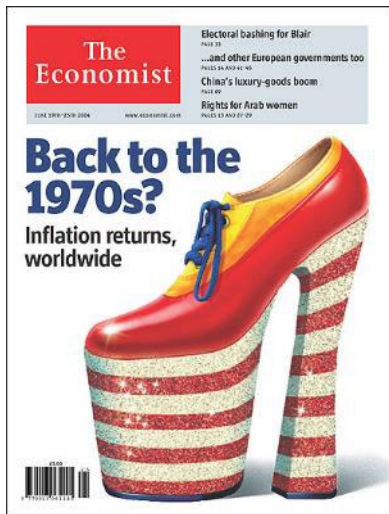
1983



1984



2004



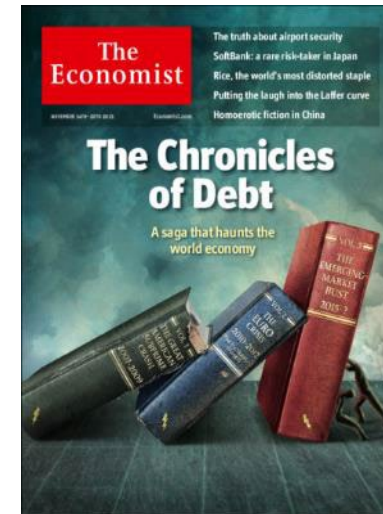
2008



2011



2015



2016





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