How Federal Policies are Accelerating Inflation

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Good afternoon, Chairwoman Warren, Ranking Member Kennedy, and Members of the Subcommittee. Thank you for inviting me to participate in today's hearing.

Inflation is currently creating significant economic pain for American families and businesses. With the inflation rate soaring to 8.5 percent – the highest rate in 41 years – real wages have fallen 2.7 percent. Moody's Analytics and Penn-Wharton estimate that inflation is costing the average household $300 per month. A Harris poll reveals that 84 percent of Americans are cutting back on key purchases. And the problem is deepening every month.

Inflation has been driven by numerous factors, but fiscal and monetary policy are the lead causes. Since the beginning of the pandemic, the Federal Reserve has pumped $4.8 trillion into the economy, more than doubling its balance sheet. Some of this was necessary to keep the economy afloat, but it was excessive, as the Fed was still buying mortgage-backed securities as recently as last month.

The Fed's actions have worked in tandem with overly aggressive fiscal policy providing more than $2 trillion in new benefits – an average of $16,000 per household. Again, a healthy portion of this spending was justified by the pandemic and the economy. But policies such as $11,400 in relief checks for a typical family of four, a child credit expansion as high as $1,600 per child, a $600 per week enhancement of unemployment benefits, and a continued student loan payment pause were often excessive and poorly targeted.

The Federal Reserve notes that consumer spending (annualized) has leaped by $2 trillion since the pandemic began and $1 trillion since last summer. No wonder supply chains are overwhelmed. Families also have $2.7 trillion in savings exceeding what would have been expected without the pandemic, yet the economy has not produced trillions more in goods and services for them to purchase. And as families spend those savings, consumer spending will surge even higher – and drive even more inflation.

A major culprit is last year's $1.9 trillion American Rescue Plan. At the time, the Congressional Budget Office estimated that the baseline economy would operate $420 billion below capacity in 2021, and then gradually close that output gap by 2025. While some stimulus was justified, lawmakers shot a $1.9 trillion bazooka at a $420 billion output gap. And this was just weeks after the December 2020 stimulus law poured in $900 billion. Economists on the left and right, such as Lawrence Summers, warned this excessive stimulus would bring inflation. They were right.

Yet other actions have also worsened inflation. The Biden Administration has hiked tariffs on Canadian lumber, and added tariffs on other building materials. It renewed President Trump's tariffs on solar panels, extended the tariffs on Chinese imports, and imposed tariff quotas on steel. It imposed Buy America provisions raising the cost of infrastructure, and is working to expand Davis-Bacon policies that raise the cost of government contracts. The White House is defending the Jones Act that raises shipping costs, and allowing a higher ethanol blend in gasoline that will raise food prices. It has also deferred student loan payments well past the point justified by the unemployment rate.

Many of these policies can be defended as achieving other important policy goals. But cumulatively, they significantly worsen an inflation problem that is already sinking under the weight of fiscal policy, monetary policy, supply chain disruptions, and the war in Ukraine. The Peterson Institute for International Economics calculates that even a 2-percentage point reduction in tariffs could lower inflation 1.3 percent and save $800 per household.

Current economic factors show that inflation will not likely recede by itself and may even accelerate in the near-term. There is no easy path to bringing down inflation, but the first rule should be to do no harm. That means resisting calls for more aggressive federal spending as well as ensuring that businesses can operate efficiently without expensive tariffs and over-regulation. Because if inflation persists and real wages continue to fall, it will soon cost jobs and create economic chaos that endanger all the good things you want government to do.

Thank you.