

Introduction

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Global tensions and domestic discontent are driving a new era of economic policymaking. Leaders in both parties are turning away from free-market principles and endorsing an increase in protectionist trade policies and more active government-directed industrial policy. Further, these disruptions come when the country's economic and political landscapes face systemic difficulties including limited state capacity and mounting federal debt. At the same time, rapid advances in generative AI have the potential to dramatically change the nature of work and the workforce as well as other fundamental aspects of society. This 2024 Aspen Economic Strategy Group (AESG) policy volume considers these topics and others, with a focus on strengthening America's economic dynamism.

With the uncertain outcome of the November 2024 US presidential election ahead of us, there are a lot of unknowns about the specifics of how US economic policymaking will unfold over the coming years. However, given recent trends and current rhetoric, one thing that seems likely is that, whichever candidate wins the US presidency, the US will continue moving toward protectionist and nationalist economic policies. This movement has the potential to hinder economic growth and dynamism if not pursued wisely and cautiously.

Economic liberalization over the past two decades drove rising standards of living in the US and lifted millions around the globe out of poverty. But this transition also brought pain to certain workers and communities, fueling a bipartisan reaction against this decades-long consensus. In a 2022 speech, President Trump's US Trade Representative Robert Lighthizer noted that in the years since trade liberalization in the 1990s, "we lost millions of good jobs and saw tens of thousands of factories close," driving "the stagnation of wages" and "economic division" across the country (Lighthizer 2022). President Biden's National Security Advisor Jake Sullivan painted a similar picture in 2023 remarks at the Brookings Institution, noting that a "shifting global economy left many working Americans and their communities behind" (Sullivan 2023).

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At the same time, national security concerns due to rising tensions with China have led to an increased focus on the need for US industrial and technical capacity. Disruptions to global supply chains during the COVID-19 pandemic have similarly thrust into light the perceived need for more domestic production. The convergence of economic and foreign policy concerns has fueled the view that we need a “new Washington consensus,” as Sullivan put it—or a “New American System,” in Lighthizer’s words. “This strategy will,” Sullivan says, “build a fairer, more durable global economic order.”

Manifestations of this new approach can be seen in policies enacted as China seeks to build a dominant role in sectors including clean energy and semiconductor manufacturing. The US has sought to restore its manufacturing capacity in these industries through high tariffs on Chinese electric vehicles, along with billions in semiconductor manufacturing incentives in the CHIPS and Science Act and electric-battery production subsidies in the Inflation Reduction Act.

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have generated decades of growth? More specifically, when is state-driven industrial policy likely to bolster innovation and improve economic outcomes, and when is it likely to hinder private-sector investment or be captured by political interests? When are national security concerns an appropriate justification for state-directed business activity and restricted trade? Are price-raising tariffs a reasonable response to trade-induced job loss, or can we commit to more effective ways of promoting widespread employment and higher wages? These and other related

questions need serious consideration as our nation aims to chart an economic policy path forward that advances economic growth and shared prosperity.

Another major challenge with US industrial-policy efforts is the practical fact that the public sector has limited capacity to achieve its goals, particularly when it comes to building the necessary transportation, manufacturing, and energy infrastructure. As Zach Liscow observes in a chapter of this volume, the average time to prepare an environmental impact statement, a necessary step to permit large projects such as new semiconductor facilities, has risen from an average of 3.4 years in the 1990s to 4.8 years recently.

Moreover, in contrast to historical projects like the construction of the interstate highways, little federal coordination or long-term planning exists across agencies or levels of governments—a need particularly glaring for renewable energy production, which requires long transmission lines that cross several states.

Furthermore, amid these historically large spending programs, the nation faces a skyrocketing federal debt. In 2024, the United States is set to run a deficit of 7 percent of GDP, the largest share it has ever known outside World War II, the global financial crisis, and the COVID-19 pandemic (CBO 2024).

This debt burden is already crowding out spending on important investments in future prosperity and safety: the federal government now spends similar sums on interest payments on the debt as it does on children, and by 2025 the federal government will spend more on interest payments than on national defense (CBO 2024; Kearney and Pardue 2023). Although it is hard to tell exactly when a debt crisis might unfold, the unsustainable path of the US debt represents a serious threat to our nation's economic security.

Of course, any consideration of US economic dynamism today must contend with the opportunities and challenges posed by new advances in artificial intelligence. AI yields the potential to fundamentally reshape the US economy, reducing employers' demand for certain skills and dramatically raising the need for others, across white- and blue-collar jobs alike. Experts have compared the scope of this impending change to that experienced after the introduction of electricity and the internal combustion engine (Brynjolfsson, Rock, and Syverson 2021).

Our country needs to make investments to be prepared for the transformations that are likely to occur. For instance, the demands for new energy sources are growing exponentially amid these accelerating AI developments (Sisson 2024). In addition, equipping a workforce with the skills to thrive amid the changing technological landscape will require educational investments from early childhood through adulthood.

Building a consensus around economic policy goals and approaches, improving government capacity, and preparing the workforce for transformational change are all made harder by the deterioration of the American public's trust in our nation's institutions, including the federal government, the media, universities, and the criminal justice system. Restoring this trust and engaging in bipartisan, evidence-based, forward-looking policymaking will be critical to the goal of strengthening US economic dynamism.

The six chapters in this book, organized into three sections, consider these and related issues.

1. Economic Nationalism in an Era of Globalization

The US Congress initiated major industrial policy efforts in 2022, with the passage of the CHIPS and Science Act and the Inflation Reduction Act (IRA), both of which include large-scale efforts to develop America's onshore production capacity in critical sectors.

The CHIPS and Science Act was spurred by pandemic-induced semiconductor shortages, along with rising geopolitical tensions between China and Taiwan, where most chips are produced, leading policymakers to invest billions in the domestic production of this critical technology. The 2022 CHIPS and Science Act included \$39 billion in grants and loans, along with \$25.4 billion in tax credits, to incentivize semiconductor manufacturers such as Samsung, TSMC, and Intel to locate production facilities in the US.

The IRA is aimed largely at catalyzing the clean-energy transition through consumer tax credits (on purchases such as electric vehicles) and incentives intended to develop US manufacturing capacity in critical green-energy sectors such as electric-battery production. Goldman Sachs (2023) estimates that the cost of the climate provisions in the IRA will reach \$1.2 trillion through 2031.

These industrial-policy efforts can be viewed as part of a deliberate move toward a more nationalist economic paradigm. US trade policy has very clearly moved in this direction in recent years. In January 2017, President Trump withdrew the US from the Trans-Pacific Partnership Agreement (TPP) and the following year initiated a series of escalating tariffs largely on goods imported from China, ending with 25 percent tariff rates on a broad set of Chinese imports by 2019 (Bown 2019). The Biden administration has not only kept those tariffs in place, it has also raised rates on Chinese electric-vehicle imports to 100 percent and boosted tariffs on Chinese steel, aluminum, semiconductor, and green-energy imports (Tankersley and Rappeport 2024).

These efforts raise fundamental questions of the proper role of policies that advance specific domestic industries within a market-based economy and the potential consequences of reduced international economic cooperation.¹ Proponents argue

1 The AESG has considered the topic of US international economic policy previously. Chad Bown (2021) evaluated several factors motivating changes in trade policy, including Chinese noncooperation, new green-energy goals, and concerns around displaced workers. In a 2023 paper written for the AESG, Mary Lovely also evaluated policy options to build resilience in key global supply chains through (a) "onshoring" capacity in a small number of critical industries, (b) building strong trade ties to allies via "friendshoring," and (c) "derisking" America's economic relationship with China.

that such steps are necessary to address concerns including national security and climate change and to boost the country's economic competitiveness. Skeptics contend that these efforts are often misguided and expensive and that they involve counterproductive provisions that result from the political process.

In chapter 1, “Protectionism Is Failing and Wrongheaded: An Evaluation of the Post-2017 Shift toward Trade Wars and Industrial Policy,” Michael Strain observes that recent trade measures aimed at promoting domestic manufacturing have been ineffective in achieving their stated aims, but he also questions the premise of such efforts to move economic activity onshore.

Strain considers the evidence on the employment effects of tariffs enacted under President Trump. (The more recent tariffs from the Biden administration are too recent to examine.) He notes that a growing body of rigorous research finds that the 2018–2019 tariffs enacted by President Trump either did not raise or slightly *reduced* US manufacturing employment. This effect comes as a result of retaliatory tariffs imposed by China on US produces and because US tariffs raised input costs for US producers, as many domestic manufacturers take imported goods as inputs to their own final products.

Moreover, Strain argues, the goals of reducing the trade deficit and boosting US manufacturing employment are themselves misguided. Free trade is not about the number of jobs—and indeed, in the aggregate, should not affect the total level of employment. It is instead about raising productivity, wages, and consumption by allowing any given country to focus on producing the goods and services where it has a comparative advantage—and then to benefit from the resulting gains from trade. Indeed, empirical evidence from the so-called China shock generated by China's ascension to the WTO in 2001 suggests that job losses in the US incurred in sectors affected by rising Chinese imports were more than offset by job gains due to rising US exports (Feenstra, Ma, and Xu 2019).

Strain acknowledges that other considerations can justify policies that seek to reduce America's dependence on China, notably concerns about national security in critical technology sectors. Such concerns, however, do not immediately justify expensive subsidies to promote domestic industries. Policymakers can build resilience in those sectors by building production networks across US allies.

Finally, Strain acknowledges first that, while trade does not affect the overall level of employment, it will advantage workers in certain sectors (where the US has a comparative advantage or in areas that are complements to imports) and disadvantage others (where US workers are close substitutes for foreign workers). But, in this way, trade acts like other dynamic forces in the economy, raising national income but changing the composition of jobs in the labor market.

Escalated tariffs and other protectionist measures are not the appropriate response to such developments, however. Instead, policymakers should look to support workers displaced by trade (and other labor market disruptions) by providing greater economic opportunities: investing in worker training programs, expanding policies such as reemployment bonuses that keep workers attached to the labor force, and reducing regulatory barriers to job transitions.

Chapter 2, “The Surprising Resilience of Globalization: An Examination of Claims of Economic Fragmentation,” is written by Brad Setser. He begins the chapter by noting that recent measures of globalization have not retreated—and China’s role in the global economy has in fact been accelerating. Current measures of global trade flows are at similar levels to those seen before the imposition of trade restrictions.

Furthermore, even as US-China bilateral trade has fallen, this drop largely comes a result of Chinese goods now flowing through third countries such as Vietnam before making their way to the US—making supply chains longer and less transparent rather than creating any material independence from Chinese goods.

Such dynamics serve as a warning, Setser writes, that higher levels of integration do not necessarily reflect desirable outcomes, such as the elimination of arbitrary trade barriers. Integration can come in the form of what he refers to as an “unhealthy” globalization—one that is a product of distorted incentives.

The large global financial flows that result from corporate tax avoidance are an important example of global integration that is unrelated to any economically meaningful efficiencies. Even following domestic and international tax reforms, many large corporations have strong incentives to shift profits to low-tax jurisdictions such as Ireland and Singapore. US pharmaceutical firms, for example, often license intellectual property developed domestically to offshore subsidiaries, where they then pay a lower tax rate on sales back to the US—and essentially zero US taxes. Similarly, Applied Materials, a strategically important American firm that builds machines needed to make semiconductors, has shifted its intellectual property and associated income to lightly taxed subsidiaries in Singapore.

As a second example of unhealthy globalization, Setser offers China’s current export-led growth model. As China’s domestic economy has weakened, leaders have turned to global trade to support its growth. Chinese companies that manufacture goods such as electric vehicles and semiconductors can rely on state support not only through formal subsidies but favorable debt and equity financing as well. China relies on exports because its households save too much. The imbalance between savings and consumption creates the need for export-based growth that drives global imbalances. For example, the savings glut of the first decade of the 2000s drove the accumulation of toxic assets, which in turn fueled the US housing bubble.

Setser offers several steps to maintain economic integration while fostering healthier forms of globalization. First, he proposes reforms to provisions of the US tax code that have encouraged US multinational firms to continue to move production of high-tech goods and profits abroad. Second, to counter China's large and potentially destabilizing state support of certain manufacturing sectors, Setser proposes stronger harmonization of trade policies among allies (for example, a subsidy sharing agreement between the US and European Union). Finally, he suggests that global leaders should pressure China to resolve internal economic imbalances. While he admits that policy options are limited here, he notes that leaders can make it clear that they will resist new forms of unbalanced integration.

2. State and Fiscal Capacity in the US

From a practical perspective, advancing America's industrial capacity requires a massive effort to build up transportation, energy, and manufacturing infrastructure. The US government's capacity to accomplish such tasks is not clear, as there are real limits to state capacity in the US, meaning the public sector's ability to execute government functions. These challenges are exacerbated and amplified by fiscal challenges resulting from the large and ballooning US deficit situation.

In Chapter 3, "State Capacity for Building Infrastructure," Zachary Liscow writes that America's low capacity to plan and construct infrastructure—a challenge highlighted by Glaeser and Poterba (2021)—is not inevitable. Rather, it is a result of policy choices that have reduced the size and quality of the government workforce, set up an onerous process that has made the process slow and highly litigious, and left those directing these efforts without long-term planning tools or efficient data systems.

Liscow identifies several key issues that hinder government capacity. First, he observes that neither the wages nor the employment of government workers has kept pace with the private sector. For instance, employment of civil engineers across federal, state, and local governments has remained stagnant since 1997, even as private-sector employment of such engineers has more than doubled in that time. Furthermore, looking at broader measures of pay across the public and private sectors, he finds that in the 1960s, there was virtually no difference between groups. By the mid-2010s, the public-private pay differential had risen to 35 percent, and it remains high at 24 percent as of 2022.

Second, he points out that the current set of procedures can result in a lengthy and litigious process simply to gain approval for new construction. The process of environmental review for large projects can now take over four years for approval, and substantially longer if litigation is involved. Third, officials involved in building

new infrastructure often lack access to clear data and long-term planning tools that would improve outcomes. Even simply comparing infrastructure costs across states is hampered by low availability and lack of consistency. Long-term planning across states, particularly for energy infrastructure, is also lacking.

Liscow recommends steps to improving each of these three aspects of state capacity: hiring more public employees with pay competitive with the private sector; streamlining the review process to gather public input, while making it harder for litigation to hold up projects; improving the consistency and transparency of infrastructure data systems; and increasing long-term planning, particularly for energy production and transmission.

Related to the topic of government capacity, Jason Furman takes up the topic of public debt in Chapter 4, “Eight Questions—and Some Answers—on the US Fiscal Situation.” He lays out the current fiscal landscape, with associated subjective levels of confidence in each aspect, and he presents a framework for building fiscal sustainability over the next decade.

The historic spending bills referenced above—including the CHIPS and Science Act and the IRA—come as the federal government faces a worsening fiscal outlook. In the years before the COVID-19 pandemic, low interest rates were widely considered to have made higher federal budget deficits more fiscally sustainable. However, as Bill Gale pointed out in his 2019 AESG paper, even during such a period, rising debt would eventually present a challenge to future economic growth and America’s global leadership. Since then, higher spending levels during and after the COVID-19 pandemic and rising interest rates have resulted in a materially worse US fiscal outlook. As Dynan (2023) lays out, currently, under even optimistic scenarios, the US debt will soon reach levels well above historical experience.

Furman begins his chapter by asserting with high confidence that the federal debt is on an unsustainable path. The CBO projects that the budget deficit will average 6 percent annually over the next decade, due to both a rising primary deficit (the deficit outside of interest payments on the debt) and rising interest payments (a result of higher current interest rates). With large deficits and high interest rates, the debt will continue to rise as a share of output under any plausible scenario. Indeed, Furman presents forecasts across a range of alternative scenarios. Even under the most favorable path, in which Congress does not extend the provisions from the 2017 Tax Cuts and Jobs Act (TCJA) and the US experiences substantially faster-than-expected productivity growth, the debt would grow steadily throughout the next decade, reaching 118 percent of GDP.

Although the federal debt must stabilize somewhere as a share of output—or else become impossible to roll over without explicit aid from the central bank—Furman is less confident about the level at which this stabilization needs to occur. Two lessons from recent experience have been instructive, however. First, he asserts that the US clearly has much more fiscal space than anticipated even 15 years ago, when certain experts were recommending that debt stabilize at 90 percent of GDP.

Second, debt dynamics have been dominated by large, discrete events like COVID-19 and the global financial crisis, which increased the debt-to-GDP ratio by a combined 55 percentage points. Given such dynamics, Furman recommends stabilizing the debt by setting it on a downward slope in “normal” times and allowing it to then ratchet back up during emergencies.

Furman points out that the known harms of failing to stabilize the debt are likely economically small. Higher government debt can result in higher interest rates and can crowd out private investment in productive activities, reducing growth. But he says that the long-term effects of these conventional channels are likely to be small: the CBO’s longer-term forecasts, which put debt at 166 percent of GDP in 2045, also have economic growth barely below the current pace of growth.

Furman cautions that it is the “unknown unknowns” of an ever-increasing federal debt that could be quite large. Most notably, America’s unsustainable current fiscal path carries the risk of a fiscal crisis in which investors lose faith in the country’s ability to repay its debt, along the lines of Canada’s fiscal crisis in 1994, which took a dramatic fiscal plan and two years to bring interest rates back down to prior levels. While forecasting such risks carries a high degree of uncertainty, the high costs associated with such an outcome is a strong reason, today, to take action that carries a relatively low cost.

Given these considerations, Furman offers a proposed framework for long-term fiscal sustainability. He recommends balancing the primary budget deficit by the end of the decade, which will see the debt reach 115 percent of GDP and set it on a slight downward path thereafter. Furman’s framework includes reverting back to pre-TCJA tax rates unless policymakers can agree on a revenue-raising package of extensions; a requirement that each dollar of new spending increases or tax cuts be fully offset and include an additional \$0.25 in deficit reduction (taking into account programs that are projected to pay for themselves, such as investments in children); restoring solvency to Social Security and Medicare through tax and benefit changes; and allowing limited exceptions for emergencies. Such a framework would set the US on a path toward much-needed fiscal responsibility while allowing for wise investments in sources of long-term growth.

3. Bolstering Workers, Firms, and Communities

American economic dynamism ultimately relies on the ingenuity and productivity of workers and firms.² In the years following the COVID pandemic, the US has experienced growth in labor productivity that has mirrored that of earlier decades—a trend that an AESG report by Luke Pardue (2024) connects to renewed business dynamism and new business formation. Additionally, rapid technological advances in areas such as artificial intelligence hold long-term potential to substantially boost productivity, raising the importance of efforts to support such innovations.

Chapter 5, “Technological Disruption in the US Labor Market,” written by David Deming, Christopher Ong, and Lawrence H. Summers, considers how these advancements will upend the labor market. The authors offer a perspective on the impact of innovations in artificial intelligence on the labor market first by taking a broad view of these changes back to the 1800s. They note that general-purpose technologies (GPTs) such as electricity and steam power had profound effects on the labor market, moving workers from the farm to the manufacturing floor and then to the office, but each advancement took decades to transform the labor market.

Artificial intelligence, Deming, Ong, and Summers argue, is likely to be a GPT, and they present several data points demonstrating the early signs of potentially transformative effects. They follow Autor et al. (2024) in delineating between the *augmentative* effects of such innovations, through which productivity gains expand the set of tasks workers do and thus generate employment gains in those occupations, and *automation* inventions, which cause employment declines.

An occupation highly exposed to the automative effects of AI is retail sales, where prediction technologies in e-commerce have been used to optimize business operations. Indeed, Deming, Ong, and Summers note that as such advances have been implemented over the past decade, employment in retail sales has declined by 25 percent. On the other hand, the share of employment in STEM jobs has increased by more than 50 percent since 2010, fueled by explosive growth in software and computer-related occupations, as demand for these skilled workers increases.

These trends characterize the broader “occupational upgrading” underway in the labor market today, whereby employment in both low- and middle-paid occupations is declining and employment in high-paid occupations is growing. This trend is

² In their 2023 AESG paper, Ufuk Akcigit and Sina Ates note that, since 1980, annual US productivity growth has been 60 percent lower than it was in the 1960s and 1970s, a drop they connect to declining business dynamism and reduced competition across the economy. In a 2019 AESG paper, Chad Syverson outlines a package of policy recommendations to raise productive market competition, and a 2019 AESG paper by John Van Reenen proposes a ten-year, \$1 trillion Grand Innovation Challenge to reinvigorate R&D investment and drive inclusive growth.

likely to play out even among professional and managerial workers: AI will likely commodify skills such as writing business plans and generating software code but will raise demands for skills such as cogent decision-making and analysis of complex counterfactual thought experiments. In this way, Deming, Ong, and Summers conclude, AI is more likely to ratchet up firms' expectations of knowledge workers than it is to replace those workers.

The final chapter in this policy volume takes up another issue of major importance to US individuals and communities: crime. In the immediate aftermath of the COVID-19 pandemic, there was a sharp increase in crimes, including homicides, shootings, and vehicle thefts. The issue of crime is one that presidential candidate Donald Trump raises often. In chapter 6, "Why Crime Matters, and What to Do about It," Jennifer Doleac lays out the recent trends in criminal activity using the best available data, and she evaluates evidence-based policies to reduce crime. She notes that, while crime did spike during the pandemic, it remained well below levels seen in the 1980s and 1990s, and most by most available measures it has continued to fall in recent months. Nevertheless, crime remains high in many urban areas and imposes large costs on communities. Combining the tangible costs of crime (such as medical expenses, lost earnings, and property damage) with intangible costs (such as pain and suffering), researchers estimate the cost of crime at \$4.7–\$5.8 trillion annually.

Doleac reviews three categories of evidence-based interventions to reduce crime: those aimed at preventing first interactions with criminal justice system, those aimed at deterring crime, and those aimed rehabilitating those who have been involved in the criminal justice system. Efforts focused on building economic opportunities for young people, particularly through investments in health and education, have strong evidence of success at preventing future criminal activity. Such interventions include teen job programs; investments in high-quality education programs; reduction of lead exposure among young children; and cognitive behavioral therapy programs, such as Chicago's Becoming a Man program, that push young adults to think more critically about the costs and benefits of their actions.

Second, Doleac notes that efforts to increase policing and efforts to detect perpetrators by using technological tools are both evidence-based crime reduction measures. A large body of research has found that hiring more police officers and increasing police presence has a large deterrent effect on crime. Given ongoing concerns about the unnecessary escalation of incidents involving police, policymakers should prioritize finding ways to reduce these social costs through improved training and management practices. Additionally, researchers have found that broadening the use of technological tools such as surveillance cameras provides a way to deter

crime through better detection of offenders at much lower cost than hiring more police officers.

To effectively rehabilitate criminal offenders, Doleac recommends the use of electronic monitoring instead of prison time—a means of keeping criminals out of the public (largely confined to their homes) while minimizing the negative effects of incarceration. Improving access to mental-health treatment is another means to rehabilitate offenders whose criminal activity is due to untreated mental illness.

Research has also found that repealing state bans on public benefits among persons with criminal records significantly reduces recidivism. In addition, erring more generally toward leniency in prosecuting first-time defendants, particularly among nonviolent misdemeanor offenders, reduces recidivism by offering offenders a second chance to avoid a criminal record and the associated costs that often lead them to return to crime, including difficulty finding a job and housing.

In sum, policymakers should focus on efforts to help prevent someone's first criminal record and on increasing the probability that perpetrators are caught, rather than on making the punishment longer or harsher. More fundamentally, policymakers should be open to new approaches to reducing crime but ensure they follow evidence on whether such efforts have been effective. To effectively reduce pain caused by crime and rebuild trust in the hardest-hit communities, we must invest in evidence-based solutions.

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