

EconoFact Chats: The Uneven Economy
Heather Long, Navy Federal Credit Union
Jon Hilsenrath, Serpa Pinto Advisory
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Michael Klein:

I'm Michael Klein, executive editor of EconoFact, a non-partisan web-based publication of The Fletcher School at Tufts University. At EconoFact, we bring key facts and incisive analysis to the national debate on economic and social policies, publishing work from leading economists across the country. You can learn more about us and see our work at www.econofact.org.

Michael Klein:

So, I'd like to welcome everybody to this EconoFact Chats Ask Me Anything webinar with Heather Long and Jon Hilsenrath. As I mentioned in the newsletters I've sent out, both Heather and John have had very impressive careers in journalism. Heather for, among other places, CNN, but especially the Washington Post, and John for the Wall Street Journal. What Heather and John have done in their professional lives is a lot of what we try to do at EconoFact – to take seemingly arcane but very important topics and make them accessible to people, and show them why these are important for their own lives.

Michael Klein:

I'd like to get right into it and start with a few questions for Heather and John. So Heather, I guess you were the one who identified the K-shaped recovery, a few years ago, and what that meant was that, some people were doing well, but other people were not. Can you very briefly describe what the K-shaped recovery was? And then, more recently, with very low rates of hiring, would you say that we should still be looking at the letter K, or maybe L, or I, or what letter would be best right now, if there is, in fact, one?

Heather Long:

I know, we need Sesame Street for economics, Michael, but hey, it's great to be here. So originally this K-shape economy concept came up in the summer of 2020, and that was obviously in the midst of the pandemic, and there was this real divergence between white-collar, generally wealthier workers who were able to work remotely and get back to work, and a lot of folks who were still struggling, who had lost their jobs at stores and lost their jobs at restaurants. And so that was that divergence, that literal K that was going on in the economy, where a lot of lower-wage workers were still out of luck. And so I wrote a piece last year, in summer of 2025, saying that the K-shape economy is returning, and what I meant by that is, while we still have pretty good employment numbers, pretty low unemployment rate, it wasn't so much a divergence in jobs, it was a divergence in spending, and how people were experiencing the consumer economy. We can see that in our Navy Federal Credit Union data. We have 15 million members, and how people are spending trends. You could also see it, a lot of people were referencing the Moody's...Mark Zandi over at Moody's, and some of the work that he had done, looking just in the past several years, and how the economy was reliant...more and more reliant on the top 10-20% of consumers. So, I keep saying the new dividing line in America is \$170,000 a year. People above that threshold still...Livin' La Vida Loca, still traveling, their consumption is growing, you know, 6-10% every month. They are throwing big weddings in Italy, and throwing big birthday parties for their kids. And then what

you see in the middle tier, maybe this is an E-shape economy for 2026, but in the middle tier, you see a lot of treading water, a lot of...they're still spending, but they're doing Costco. I called it a Costco Christmas. People are going to the warehouse stores, they're going to TJ Maxx, and they're really shifting to try to make every dollar go as far as they can, because they are feeling a little bit crunched. And then what's actually going on in the bottom, the bottom of the E, or the K, or whatever letter you want to choose, is people are actually pulling back on spending. They are spending less than they were a year ago. This is sort of the tier of \$65,000 and below, and in some cases, adjusted for inflation, they're spending less than they were in 2019, so it's this real kind of bifurcated, or even trifurcated, if you will, economy that's going on right now. And sometimes people say, well, wasn't it always like that in the United States? And the answer is no. I mean, certainly in the last several years, there was just a lot of 'revenge spending' across the income spectrum as those stimulus payments came in from the government, during the great, you know, resignation era, when people were trading up for better jobs, and a lot of lower-wage workers were getting strong pay boosts, there was just a lot of spending across the income spectrum, and now it just looks totally, totally different.

Jon Hilsenrath:

What I would say to amplify Heather's comments is that this is not just a feature of where we are in the business cycle, kind of post-COVID. It's not a feature of what America has always been, but it is a feature of the world that we've been in for almost a quarter century, and the forces behind it, in my view, are intensifying, which I think Heather has so well identified. To pull the lens way back, we're at least a quarter of a century into a transition from a manufacturing and kind of middle-income services-oriented economy, to a tech-driven, information-driven economy. Put another way, we are well into an era of exiting our place as an industrial economy. And we know a lot about what that looks like, and it's somewhat troubling. So, an industrial economy created a lot of middle-income work, because you needed people attached to all the machines – to produce the televisions and the phones and the refrigerators that we consumed. And you also needed people attached to those services, telephone operators. Well, in a high-tech, information-driven economy, you don't need as many people doing these kind of jobs that are kind of right in the middle, that are the core of the middle class. And what we've seen from decades of research is that technology, technological advancement, in the modern era has this effect of barbellizing income and wealth. So, driving people out of the middle class. And I think this is a profoundly important transition that transcends just, like, whether you shop at Costco or Walmart. It's driving our politics, right? Because what Donald Trump did, you know, a lot of Americans feel that they've been left out of this system by the elites, who are at the top of the K. And what Donald Trump did, in my mind, was pull off one of the greatest heists in American political history. He stole the working class from the Democrats. The question is whether he's going to be able to live up to the promises that he made to this kind of [inaudible] middle-income households. And we're starting to see in his own poll numbers, at least some people coming to a recognition that some of the ideas that he's put out there, say, tariffs we can talk about, you know, they might not be the panacea that he's promised them to be. But I think we're in the middle of a great transition from an industrial, middle-income services economy to a high-tech information economy, and it bifurcates wealth and income, and we're living through all the disruption of that.

Michael Klein:

Yeah, you know, one of the original researchers on this is David Autor at MIT, and we have a podcast and some memos from him. I would refer our participants today to those on our site at econofact.org, if they wanted to follow up with that. Both of you have alluded to, sort of issues of affordability and issues of tariffs. Let's start off with tariffs. One question is whether or not tariffs will lead to significant inflation. Another is that if companies stop paying the cost of tariffs and begin to pass those costs on to consumers, what impact would that have on the economy? And then somewhat related to that, about manufacturing employment, because manufacturing employment was supposed to benefit from the tariffs, but we've seen in the data that it's really fallen off this year. So, you know, there's recent research by Gita Gopinath and Brent Neiman about the pass-through of tariffs to prices, which they say is almost 100%. What are you seeing about the effects of tariffs, Heather and John? Heather, you want to start off?

Heather Long:

I'll start again. John's so good at adding and amplifying, so I'll take the baton first and let him do the brilliance later. Look, a couple of things. Tariffs, look, no doubt about it, it's been less of an impact than I think a lot of people were expecting in the spring. I think it's also important to add that, obviously, the effective tariff rate that we thought would happen on April 3rd has definitely come down a lot. And so, that's why a lot of these worst-case scenarios, whether on inflation or potential recessions, didn't happen. I think of when Torsten Slok from Apollo was out there at the end of April on TV saying there was an 80% chance of a recession, and now all of his notes are quite positive about what he thinks 2026 is going to be. Look, a couple of things. We have seen evidence of what you were mentioning, Michael, that Gita Gopinath and others have seen, of the pass-through of a lot of these tariff costs to consumers. And I can tell you in our Navy Federal Credit Union spending data, and really in the retail sales data that we've just gotten in the last couple of weeks, you can see that people are not spending as much on home improvement and furnishings, right? And so, sofa and electronics, and those are areas where it's been noticeable, even in the consumer price index data, the CPI data, that there has been some pretty big tariff impacts so far. And also, same thing in the car space. Obviously, it was a real shocker when the median and average price of a car, you know, got over \$50,000 in the fall of this year, and we could just see this massive shift of people moving into used cars who would have before preferred to maybe have a new car. So you can see consumers reacting, you can see companies passing along these impacts, but I think the number that I always keep in my head is at the end of the day, the import economy, you know, is impacting around 10-11% of the U.S. GDP. It's just such a small number overall, and the AI story has become so dominant that...not to say it didn't matter, but I think it mattered a lot less than many people, myself included, were thinking it would in April or May of 2025, when a lot of this was really coming down the pike. One word on manufacturing jobs, and that is, as the point that I've made, is there was virtually no job growth since April last year, and that's across almost every sector except healthcare, so there's certainly been an impact on the labor market. Companies have become, for a number of reasons, one of which is tariffs, a lot more hesitant to hire. I've called it a hiring recession or a jobless boom. It's important, though, with manufacturing, I see a lot of people mistake manufacturing for blue collar. Manufacturing jobs were already struggling even before April. What really changed since April is not only did manufacturing continue to struggle, as it had for the past year or so, we saw other blue-collar sectors also pull back on hiring – construction, transport and warehouse sector, and mining sector. And that's really unusual, to see the entire blue-collar workforce pull back so much on hiring. Alright, I'll pass it to John to do the better points.

Jon Hilsenrath:

So, I do have a few thoughts on this. So, I'm going to start with the Fed and the Fed's narrative about tariffs and their effect on inflation, which I think describes the view of a lot of people, right? So, their view is that tariffs are a one-time price level shock, so that what happens is tariffs come in, companies pass on the price, you know, the cost of that increased price of imported goods. Prices go up one time, but then they go back to rising at the rate at which they were rising in the past. And so, it's a one-time price level shock, and you can, as the Fed likes to say, look through it, and expect inflation to go back to, kind of, where it was in the past. I'll say two things. Well, I think that is completely upside down in describing what's actually happening, and what history suggests will happen. So in my view, again, to pull the lens way back, we were in a period from...actually before 1994, but intensifying from 1994 to 2016 of what I call trade opening. And it was marked by 3 big events – NAFTA in 1994, the creation of the World Trade Organization out of GATT in 1995, and then China's entrance into the WTO in 2001. These were 3 singular events, and out of those 3 singular events, we got 25 years of goods price deflation...consistent goods price deflation, as companies built out global supply chains, sourced low-cost labor, and we imported cheap goods, and that held down inflation over a 25-year period. Now, that changed with the election of Donald Trump in his first term...and the tariffs that we went through in 2017, 2018, now we're going through another round of it. And so, now we're in what I would call a period of trade closing. Which is contrary to the period of trade opening. And so my view is that this isn't a one-time price-level shock. It's a major adjustment to the world trading system. And it's gonna go for years. And companies are adapting and adjusting as they go. So what did they do in the first year of this latest trade closing round? They built up a lot of inventories on imported goods while they were still cheap. They started moving around their supply chains. They pass the increased costs kind of through the supply chain. There's all kinds of adaptation, which muted the initial rounds of these tariff increases, but in my mind, this is a long period of trade closing, and what it means to me is that this long period of downward pressure on goods prices is over, and that the deflation that Americans have experienced in Walmart and Costco is now over, and so this is a persistent upward pressure, in my mind, on inflation rates, and not on price levels. And so that's where I think we go. I think that it's harder for the Fed to achieve its 2% inflation target under these circumstances. We see that with the persistence of inflation, and in fact, I think the Fed is underestimating how persistent it's gonna be over the next couple years. On manufacturing, again, I think politicians have gotten this all wrong. You know, they kind of pretend that they've got solutions...and by the way, this isn't just Donald Trump and the Republican Party. Joe Biden made a lot of the same promises that we're gonna bring back manufacturing jobs to America. Well, if my view of the world is right, I said we're exiting a period of industrial-driven growth, and we're a quarter of a century into a period of tech and information-driven growth. We're not going to bring back industrial era jobs. It's not gonna happen. Either they're gonna stay overseas, or they're gonna be automated. But, it's naive to think we're going to rebuild the industrial economy of the 1950s. I think those periods are over, and if our politicians were being honest with people, and thoughtful about what's happening in the world, they would explain where we are, and what the possible solutions are a little bit more clearly. I think they have been, and I think that runs the risk of biting Donald Trump where he doesn't want it in the midterms.

Michael Klein:

One of our very first memos when we launched in 2017 was by David Deming at Harvard, and what he showed was value added in manufacturing had not declined at that time, but employment had. So that's to your point, John, that there's been this tremendous automation. You know, now the people who work in a

steel plant are either custodians or engineers, and, you know, everything has changed so much. John, I'd like to go to you first with the next question, because I know you've done a lot of work on the Fed, and we've had a few questions already about the Fed. One relates to the attacks on Fed independence, and what that might mean for a financial reckoning, along with the increase in private credit growth, the uptick in crypto, the high valuations in the stock market. Another is about, do you see the role of the Fed changing over the next 10 years? How do they adapt to the political and technological changes? And then about the selection of the next chair for the Fed.

Jon Hilsenrath:

So let me take two pieces of that. One is the kind of the Fed and its independence, it sounds like a few people are asking about that. And then the other is, like, all these alternative assets and what's going on there. I'll try to connect them. So, on the Fed and its independence, the worry is that the Fed's gonna risk losing its independence, it's gonna be either kind of bullied or ordered around by the President, and that's gonna lead to policy mistakes, and that's seen as a risk. I think it's already happening, right? That the Fed's independence has already been compromised, and we see it almost every week. The President tried to fire Lisa Cook last year, now they're threatening to prosecute Jay Powell. The Secretary of the Treasury has made some not-so-veiled critiques and attacks on the Fed's regional bank president. The President has said very clearly he wants a new chair who will listen to him and follow his advice, so to speak, on where interest rates should be. So, it's already happening, and what surprises me is how complacent the bond market seems to be about this. We talk about the yield curve steepening, so long-term interest rates have gone up a bit relative to short-term interest rates. But given all of the pressures that I'm talking about with this trade closing, and on the Fed's independence, I mean, it all seems like an inflation risk to me, which ought to add up to higher long-term interest rates. Which is why, by the way, I was talking to Heather Long earlier, I want to refinance a mortgage now while I can. So I think these attacks on the Fed's independence are very real, and they're going to intensify over the next year, and we can get deeper into that. I'm happy to get deeper into that, there's a lot of layers to that. But, suffice it to say that, the Fed's independence has already been compromised, and it runs the risk of...more so, there are constraints to how much the Fed can bend to this, which we can talk about, but I think it's already compromised. On the alternative assets, like crypto and private credit and such, I'll say two things. To me, it's in part a symptom of how extraordinarily easy financial conditions are right now. And this also lays waste to this idea at the Fed that its policy is slightly restrictive. The Fed has these models that say a neutral interest rate is...according to the models, around maybe 3 to 3.5%. And by a neutral interest rate, they mean that it's neither putting upward pressure nor downward pressure on inflation, and their inflation target is 2%. But when I look at the world, I say, alright, your inflation target is 2%, and inflation is closer to 3%, so financial conditions are easy. When I look at all of the money that's poured into private credit, and crypto, and all these alternative assets, when I look at what's going on in stock markets, financial conditions are exceptionally easy right now. And when you add on top of that fiscal policy, we've got budget deficits running close to 6% of GDP – the norm over the last century is closer to 2.5% of GDP at a time when we're not in recession and we don't have a mass war going on. We have exceptionally easy fiscal policy, so I think financial conditions are really easy, and the Fed is running the risk of making a mistake by continuing to cut interest rates.

Michael Klein:

Before I turn to you, Heather, I'll just mention that on Sunday, we're posting an EconoFact Chats podcast with Ken Kuttner of Williams College, who is not only a monetary policy expert, but worked as Assistant Vice President at the Federal Reserve Banks of New York and Chicago, and we had a really good discussion about a lot of the points that you're bringing up, John. So I'd encourage people to listen to that when it comes out on Sunday as well.

Jon Hilsenrath:

He's a very smart guy. I'm sure he was a source of Heather's, too, but I used to talk to him when I was covering the Fed.

Michael Klein:

Oh, he's great, and we had a really good discussion. Heather?

Heather Long:

Yeah, I think I'll just plus one to everything John said, and then the only other big picture idea I'll throw out, particularly around the rally that we've seen in gold, and to a certain extent in silver...you have to ask yourself as well, in addition to all these near-term questions about who the next Fed chair will be, and how much pressure will be on that person and the Fed overall, I think you also have to layer in the wider questions that John's been bringing up about the shift going on in the global economy and the U.S. economy, and the perceptions of the relative strength of the U.S. economy against the rest of the world. And what I'm trying to say is I do think we're in a period at the start of a regime change, you know, does it mean dollar dominance ends tomorrow? No. Does it mean, the Fed as the number one central bank in the world ends tomorrow? No. But, I started my career working at an investment firm in London in the early 2000s, and what people forget is emerging markets were the best performing asset class and the first until the great financial crisis. And we used to have to sit there in London and convince clients from Europe and Asia and North Africa to invest in the United States. They believed, even then, that the U.S. was on the decline. And then, the Great Financial Crisis happens, and the United States emerges, and the Fed emerges much stronger than most other parts of the world, so all these assets from around the world come back into the dollar. The Fed becomes the dominant player again. But I think people were ready. I don't think Americans fully understand how ready many other parts of the world have been, for a long time now, to begin to shift their assets other places. And it doesn't mean they're all going to take it away tomorrow, but they're getting back in this mentality of hedging a bit. I don't want everything in dollars. I don't want everything reliant on the United States anymore. And so I think that's why you're seeing gold surge and silver surge, and I think that's why, you know, there's a lot of rebalancing that's going on, and that's on the early edges of the potential end of dollar dominance.

Michael Klein:

I'd like to shift gears a little bit. There have been a number of questions about AI. Some people have asked is AI good or bad for the economy and for people? It's a very broad issue. But I was wondering if you just had a few thoughts about the economic impact of AI. John, you already mentioned that a little bit about, sort of those middle-tier jobs...the emptying out of the part of the barbell. Any other thoughts about what AI will do to people as workers and as consumers.

Jon Hilsenrath:

You know, Michael, you mentioned David Autor, and there's a really great debate that's been going on for a little while between David Autor, this MIT economist who identified the China shock, and is, like, really a brilliant labor economist, who I think ought to win a Nobel Prize someday, and Daron Acemoglu, who's at MIT, 3 or 4 doors down from Autor, and also, you know, treads a lot of the areas that Autor treads.

Michael Klein:

And won the Nobel Prize.

Jon Hilsenrath:

And he won a Nobel Prize. Yeah, and they have different views about AI. So Acemoglu's view is that all the things that I described about how technology is bifurcating income and wealth and thinning out middle-class work...Acemoglu's view has been that that's going to intensify and be amplified by AI. Autor's view is that AI has the potential to work through the economy in a different way than other periods of technology did, and that it actually could enhance the skill sets of middle-skill workers in ways that allow them to do better and work smarter. You know, his example is, let's say you're a physician's assistant. With AI, you're getting all kinds of knowledge at your hands that allow you, potentially, to do the kinds of things that only a medically trained expert doctor could do. So, like, these are two brilliant people who have different views about AI, and I'm not gonna come in and say that I know either more than Acemoglu or whatever, but I could tell you my gut is more in the Acemoglu camp. I think that the trends that we've been living through for the last 25, 30 years are...but my hunch is that they're going to intensify. I think it's the most important economic challenge of our times, and also perhaps the most important political and social challenge.

Heather Long:

That was great. I'll add two thoughts that may or may not be helpful, but yeah, the first one, I guess, that I see is I think I worry a lot about the AI economy doing more of the K-shape economy, in the sense of more of the rewards going to the capital owners, and, we're already struggling for people on Main Street, for middle-income Americans to really feel...they're looking at this stock market, great year in 2025, and sort of saying, why isn't that reflected for me? So I really wonder, what will it take to really be felt on Wall Street. We just saw data that we're at a record low of the amount of GDP that's going to labor versus capital in this country. So how much is going back into wages, which is still where most people are getting a lot of their bread and butter and their economic living from. So I worry a lot about that going forward, that we could see a great productivity boom, that we could see great GDP, but does it really filter through? One of the things that I keep an eye on, it's really hard to get forward-looking and real-time insights on a lot of this. There's been some great economic research of what we know so far, but I really pay a lot of attention to the Anthropic Economic Index. I think they've been very open and transparent, trying to put out a lot of granular data on how people are using their Claude LLM. They just put out one in the last few days, actually, here in January 2026, and it actually shocked me that the usage of Claude, and Claude is definitely seen as one of the better programming LLMs out there right now, so really being able to do more than just draft emails or, you know, redecorate your room. And they're finding that, more like what John was saying, that it actually is not coming for entry-level jobs. They're seeing more and more of the, kind of, middle-tier jobs that are being directly impacted. Now, this is early days, this is, you

know, use of Claude. You could have a million caveats here, the research is showing something very different. But I keep an eye on that Anthropic Index because I think those are the best leading indicators we have in some ways.

Michael Klein:

So, we only have a few minutes left. I'd like to shift gears yet again. And, both of you have worked, or are working as journalists. You still are, I know, to a certain extent. And I'd like to talk about the reporting of economics. First off, what economic and social policy topics do you think are underreported these days, and why do you think they're not getting the attention they might deserve? Heather, do you have any thoughts on that?

Heather Long:

Sure, I'll take a first stab. Look, it's really hard in newsrooms to get away from the big, shiny object. Reporters are a lot like toddlers, and they just chase whatever, the big noise or the big new present is, and in the world, President Trump is excellent at throwing and throwing and throwing big new noises and pops in the room, and it sort of forces/gravitates towards that 24-hour feeding the news cycle. I mean, just look at last weekend, like, you know, it was just mind-boggling, the amount of stuff that came out. You know, we haven't even touched on the potential 10% credit card cap idea. Obviously, Fed Independence, there was a jobs report, more action in Venezuela. I mean, it was just hard to even figure out what the lead story was on the top of the website. And so what I think's really missing, and we've kind of touched on it in this wonderful 45 minutes here, is I think care economy issues, sort of deeper structural issues in the United States around affordability of childcare, or the massive problems around elder care in the United States, let alone healthcare issues, they don't get as much coverage as they deserve. And then, I think a lot of the big structural shifts that John's done a great job of talking about, you know, where you step back and do the 30,000-foot look, a lot of people miss those in journalism because they are so worn out and exhausted from chasing particularly the Trump news cycle.

Michael Klein:

John?

Jon Hilsenrath:

I mean, I'll add to that, I think not only are these issues of bifurcation of wealth and income, part of it is that it doesn't get enough attention, but, like, my big problem is the kind of attention it gets. And I think people tend to fall into very conventional buckets, certainly in the political sphere. I would say in the public sphere, which is, you know, politics and media and all that. So, you know, on the left. You have these, kind of, like, same old talking points. The rich get richer, and a tax on billionaires, and tax the rich, and stuff like that, kind of traditional, conventional left of the political spectrum frameworks. And then on the right, and obviously, Trump is disrupting the way we think about all of this...they're attacking elites in academia, and in Washington, and attacking Democrats. And I think that everybody's missing the bigger picture in the process about how the world is changing outside of these political frameworks, and these old...I don't like the language we use in describing a lot of these issues. I had a rule in the newsroom that when we were writing about anything...I was an editor or a writer...I never wanted to use the language of the participants in the debate. I wanted to find a kind of neutral language that described what was going

on, and I think we could use more of that in these discussions about income and wealth inequality, because the lens is being distorted by the way we talk about things.

Heather Long:

On a positive note, I will say I think all of this is happening, on Substack has been great. A lot of people have been freed, or LinkedIn posts, I know John's done some great ones, and the podcasting world. Kudos to you, Michael Klein, for all you've built. But, I do think some of these discussions are happening, and that's why people are gravitating there, because they're finding something that they're not finding in the daily news coverage.

Michael Klein:

Well, I want to thank you both, Heather and John, very much for this really engaging conversation. We're going to distill this and have this as one of our EconoFact Chats in the next few weeks or a month or so. Also, I just mentioned we made this Ask Me Anything webinar available to everybody. Typically, they're only available to our Premium Subscribers. You can become a Premium Subscriber of EconoFact for only \$50 a year. And along with the Ask Me Anything webinars, we have a weekend reading, where we curate our stuff about timely topics. So, for example, the one that was sent today was about the independence of the Federal Reserve. More importantly, we at EconoFact depend on our ability to continue to do what we do on the generosity of individual donors and foundations, and if you think this is a valuable resource, we'd really appreciate your support. So, thank you for joining me today, John and Heather, and also everybody who tuned in to the webinar. There'll be an announcement about the next one, which will be in a month or so as well. So, thanks very much, everybody, and it was great to have you guys on today. Thanks very much.

Jon Hilsenrath:

Thank you.

Heather Long:

Thanks, Michael.

Michael Klein:

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