

EconoFact Chats: AI, Immigration, and Fed Independence – Understanding the Risks Facing the US Economy

Binyamin Appelbaum, New York Times

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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

Hi everyone, and welcome to this EconoFact Ask Me Anything webinar with Binyamin Applebaum. Binyamin is the lead writer for economics and business for the New York Times editorial board. He's also the author of the book 'The Economists' Hour'. I'm proud to say that he is a member of the Board of Advisors for EconoFact, and a regular participant in our quarterly journalists panel for EconoFact Chats. So Binyamin, thanks a lot for joining me today.

Binyamin Appelbaum

My pleasure.

Michael Klein

So let me start off with a question that was sent in before the webinar. One of the attendees who's on right now asked, what's the number one under-discussed aspect of the US economy that keeps you awake at night?

Binyamin Appelbaum

It's always a little hard to weight these things, right, like under-discussed. But I mean, some of the big ones, I guess, it's talked about all the time, but I still have this feeling that we're maybe not spending enough time thinking about AI. I think a lot of our economic problems are potentially compounded by AI. There is also opportunity there, and I think while everybody's sort of running around like headless chickens saying the word over and over again, I'm not sure we're having the type of substantive engagement on the issues there that we need. Certainly here in Washington, I worry a lot about that...that our policymakers aren't yet really dealing with this as a major economic issue. The debt is another one that lurks in the background that doesn't get talked enough about - the scale of the federal government's dependence on borrowing and the implications going forward – I'd put it high on that list as well.

Michael Klein

So with AI, there are two very different schools of thought about that. One group is saying this is going to displace lots of people from their jobs, and another group is saying it's going to enhance the productivity of perhaps even the very same people. And then another issue is that with any technology, there's going to be disruptions. So you can go back to the Luddites and the automatic weaving machines, and then you can think about sort of automation. And here it seems like the group that it's affecting are more kind of middle management, white collar workers. Which way do you come down on that, Binyamin? Is this going to be labor enhancing or labor replacing?

Binyamin Appelbaum

Well, I think it depends a little bit on how we move forward. I think it has the potential to be both, and probably will be both to some extent. But I think there's a role for policymakers to play in pushing AI to be labor enhancing in at least some contexts. There will undoubtedly be other contexts in which it is labor replacing. Self-driving taxis are a super obvious example that seems to be coming quickly. It's probably going to be both things. The thing that I'm most skeptical about is speed. I keep on hearing it's going to transform the world tomorrow, and just mechanically, it takes time for these things to unfold. And so I have been hearing all my life from the tech industry that each successive innovation is going to really, really change the world. This may be the one that has a larger impact than anything that's come before it, but I feel reasonably confident that it's not going to happen as quickly as everyone is saying, and we're already seeing...there's been some interesting reporting just in the last few weeks about the demands on the existing infrastructure and the inability of these AI providers to keep pace with all of the data requests. I think we'll pretty quickly start to see pricing that forces people to pay, and to pay a premium for access to this stuff. It's going to take a long time to build this out in the physical world. We have time to shape this. And from my perspective, the more we can make it labor enhancing rather than labor replacing, that to me is a direction public policy should be focused on.

Michael Klein

What would you see as a policy that would make it labor enhancing? When I was in Washington, people said "we should do this," and I said, "what's the lever you can pull?"

Binyamin Appelbaum

It's a really good question. I think there's a couple of categories of possibilities. One is that our tax system is heavily skewed toward taxing labor and advantaging capital. That's a lever you could pull on. You could reduce the incentives to replace labor with capital, and that would give employers, at least at the margins, an incentive to invest in labor and to maximize the output of their labor. Another possible policy lever, a more drastic one, is simply to set some things off limits. If you require a doctor to make the diagnosis, if you require a lawyer to sign the paperwork, you can in effect force companies to preserve some employment and to figure out

how to use those employees as efficiently as possible. That's a lever we've pulled to some extent during past technological revolutions, and it's one that's available to us again today. And then at the other end of the spectrum, the gentler end, you can encourage companies to train their employees to take advantage of AI with tax incentives, with labor regulations, by providing employees with stakes in their company so that they are able to negotiate in their own interest at the bargaining table. The Longshoremen's Union is a famous example of a union that was quite successful in managing the technological evolution of its sector, so that it realized some benefits alongside its employers. I don't think we're helpless to do this kind of thing. I don't exactly know what form these innovations...these interventions need to take, but there appear to be a couple of sort of big buttons that are available to push if we want to.

Michael Klein

In one of the interviews I did for EconoFact Chats, I was talking with Lant Pritchett, who's this very prominent development economist. Lant moved from Cambridge to Utah, and he's living in Utah now, and he tells the story of going into a supermarket, and over an automatic checkout machine, there's a sign saying we value our employees. And the irony is not lost that technology, not just AI, but lots of technologies have replaced people's work. But then, people find other kinds of things.

Binyamin Appelbaum

And I would just add to that like that sign may be more true than it was a decade ago, right? Like if what you're getting rid of are the employees with whom you have the most commoditized relationship and what you're preserving are the employees whose talents you actually need the most, you may in fact be a business that has fewer employees, and values each of the ones who remain more. That sort of has been the story of this evolution over time.

Michael Klein

Yeah, I guess the sign didn't say we value all our employees. Do you think AI is more likely to widen inequality, or could it help expand access to opportunity?

Binyamin Appelbaum

Again, I think it depends. I think the frame is a good one. We ought to be concerned about that and we ought to be thinking about how we ensure that AI broadens opportunities rather than exacerbating inequalities. It clearly has, in some ways, the potential to do that, to exacerbate inequality by concentrating the returns to capital, by depriving people of employment, by...if it turns out, which I think is very likely, that we quickly get into a world where access to AI at least in its most advanced forms is limited, and sort of pay to play – It's very easy to imagine some of these inequalities getting exacerbated pretty quickly. So thinking about how we preserve access to the technology, how we ensure that its gains are broadly distributed, I think these are really important public policy questions.

Michael Klein

You talked about some of the constraints on the expansion of AI. And one of those is the need for tremendous amounts of power. Some people have written about that being a binding constraint for AI, and maybe even more so now when we're having an energy crisis. To what extent do you see that as something that's going to hobble the expansion of AI?

Binyamin Appelbaum

I think it may slow the pace, but our capacity to generate energy is pretty significant. Like we have...given time, we have the ability to build new nuclear reactors. We have the ability to expand renewable energy sources massively. We have a lot of levers to pull, so I'm not sure why it would constrain it in the long term. I think it certainly is the kind of infrastructure that I'm thinking of when I say that I don't think this is going to roll out as quickly as some people seem to be predicting. But I don't see why that would be a binding constraint in the long term.

Michael Klein

And then talking about labor displacement, another source of possible labor displacement, or maybe not, is immigration. So you've written an article where you say that American jobs aren't really being threatened by immigration because there are different kinds of jobs that immigrants are taking. Then also some of the jobs of so-called high skilled immigrants, are complementary to the labor force, not substituting away from it. So what's your view on the ways in which immigration is affecting the labor markets in the United States?

Binyamin Appelbaum

Well, I think right now we're seeing that story run in reverse, right? We're seeing immigrants drain out of the country or be excluded from the labor force in various ways. And we're experiencing a labor crunch, and it's going to get worse. I've written as well that one thing we don't produce in this country, at least in the numbers we need, is babies. Even with AI looming on the horizon, the fact of the matter is that we have been dependent for some time now on immigrants to provide a significant portion of our labor needs. In their absence, we're gonna face a real crunch. So to me, the immigration debate is fascinating because the level of vitriol, of anger, of distaste for immigration, I'm not discounting it out of hand. I think people are entitled to their opinions and many of them are clearly uncomfortable living in a country with this level of immigration. I think my role as an economic journalist is to frame the consequences and to make sure people understand what immigrants have provided, are providing, and in their absence, what we won't be able to do. On those dimensions, it just seems very clear to me that without immigration, we're going to have a labor shortage.

Michael Klein

So this is a little bit outside the scope of economics, but you had what I thought was a really interesting article, which was about housing in New York City, but you visited the places where

your immigrant ancestors had lived. So you're third or fourth generation. I'm first generation. To what extent do you think the debate about immigration, and the effect of immigrants on the economy today is different than what it was in the past, or is it just sort of a new version of the same story?

Binyamin Appelbaum

So not to retell my whole family history, but my family, I'm basically descended from people who started immigrating to America in the 17th century and kept coming until the early 20th century. So for several hundred years, the experience of my family, of my ancestors was that they came from places, other places to America in pursuit of better lives. And it is undoubtedly the case that many of them experienced discrimination and reactions that are not altogether different from what immigrants experience today. So to some extent, the idea that there was a golden age in which America was totally open-armed about immigration is just, it's ahistorical. It's not the case. We have always struggled with the question of who should be an American, how quickly they were expected to assimilate, what assimilation even meant, whether it was even desirable. None of these are new issues per se. They're all things we've struggled with over time. So I think there are many parallels with the current situation and with past experience. And I take some comfort from that because the story in the past has always been that we have worked through these difficulties more or less successfully. I mean, third generation immigrant is just a term that doesn't mean anything in America, right? There are countries in which, if your family came from Algeria to France three generations ago, there's a very good chance that both you and your French neighbors still think of you as an Algerian immigrant. In the United States, if your family came here three generations ago, it's a trivia question about your origins. We have a long history of moving past that pretty quickly.

Michael Klein

Yeah, you can think about the signs, Irish need not apply, and they were demonized, and lots of other groups, of course, as well. So that is a hopeful view of it, and we all would like to see that emerge. I'm interested in your perspective on the price of oil. The world supply of oil seems to have been temporarily buffered by the number of loaded tankers on their way to refineries, but the situation in the Straits of Hormuz seems to be moving sideways at best. Why isn't the benchmark price of oil much higher? And we should say it's 40%, 30% or 40% higher than it was before February 28th. But why isn't it \$200 a barrel instead of \$100 or \$110?

Binyamin Appelbaum

This is a fascinating question. I'm not sufficiently a student of the oil markets to have my own view, but I do talk to smart people about it. And the consensus I hear is basically that the markets have not fully incorporated the realities that we're going to be confronting in the coming months—that for various reasons, some rational and some may be irrational, markets throughout this war have been rather slow to price what appear to be fairly inevitable shortages in our

collective future. Precisely because in the early months, we were able to live off the stuff that was already moving toward the places where it was needed. Even if the war ends today and magically the Straits of Hormuz were reopened completely, it will take a long time to restore production to pre-war levels. And as that works its way through the system, I think we are likely to see higher oil prices for some time. Now, so part of it, I think, is just that there's a pretty wide consensus among experts that markets are underpricing things right now, which is fascinating to think about in terms of theories of how markets work, and why experts are in a different place than investors and all of that. I do take seriously the countervailing possibility that investors are appreciating some things that experts are not. I don't see any reason to think that the experts are wrong about the supply of oil, but I think on demand dimensions, there may be more flexibility than some experts have appreciated...people substituting away from oil, limiting consumption, doing other things that to some extent limit the impact of all of this. But in general, not on the basis of my own expertise, but I'm struck by how consistently I hear this story that markets are wrong.

Michael Klein

So, at the risk of a market that nobody really understands that well, would you say the same thing about the stock market? It's sort of at very high levels now. And one would have thought that with all the uncertainty and disruptions in the world, the stock market would have tanked. In fact, I think Trump said something along the lines of, well, the stock market could fall by 20%, but that's one of the costs of war.

Binyamin Appelbaum

With oil, at least there's an active consumption fairly soon after the investment. There's a more direct connection between price and a real world experience. I would not even venture to give you a theory of the stock market.

Michael Klein

Okay, that's fair. I withdraw the question in that case. So when we're thinking about the economy, of course, a very big aspect of that is the Federal Reserve and its behavior. And you've written a few things about the Fed and most recently about the proposed next chair of the Fed, Kevin Warsh. What do you see as the challenges that he faces and the likelihood that he'll rise to meet these challenges? And what does this imply for the US economy, whether he meets the challenges or not?

Binyamin Appelbaum

Yeah, so by way of background, I spent the better part of a decade covering the Federal Reserve for the Times before joining the paper's editorial board. So this is a subject I've followed closely for a long time. And I covered Warsh the last time he was at the Fed as a governor during the financial crisis. I think it's kind of fascinating because this is a guy who simultaneously, I think,

is in some senses sort of a standard issue central banker, a guy who is worried about inflation and a bit of a technocrat, a bit of an egghead, and the sort of person who you wouldn't have any hesitations about appointing to the central bank under other circumstances. But in order to get the job, he has had to debase himself in front of the President. The President, at least, is under the impression that Warsh is the kind of guy who's going to lower interest rates for him. Warsh hasn't exactly disabused anybody of the impression that he had to kowtow to the President in order to get this job. And so I think he will enter the office with a shadow over his head. He will enter office needing to do something to restore his credibility as an independent central banker. And I think the only way he can do that in the long run is to make decisions that are in the public interest rather than the President's interest. And the most likely divergence is that Donald Trump is going to continue to press the Fed to lower interest rates, more or less irrespective of the short-term consequences for inflation. Warsh is likely to find himself in a fairly difficult position because there's very little reason, other than the President's wishes, to think that this is a good time to be lowering interest rates. So that's a difficult position. I think the best case scenario is that Kevin Warsh, once he has the job, recovers his integrity and decides to manage monetary policy in the way that more or less the current board is doing, which is gonna involve holding the line and trying to bring down inflation. That's the best case scenario. And he's going to be under a lot of pressure from some of the other members of the board to behave that way. If he tries to bring down interest rates, he'll have some support within the institution, but it's going to be a tough road for him to travel. And the hardest part may be explaining to the public credibly why he's inclined to do that. To sort of step back from all of those sort of political particulars, what's at stake here is not just the integrity of the Fed, but the health of the economy. We've had above target inflation for half a decade now. Nobody likes it at all, and the Fed has struggled to deal with it and needs to keep struggling to deal with it. To the extent that it fails to do that...oh, and by the way, the federal debt is going to increase the pressure on the Fed. It's going to make its life harder rather than easier, and to the extent that the Fed fails in that task, we're all going to suffer the consequences. So I think this is an extremely high stakes game that Kevin Warsh is playing. And I hope he knows what he's doing.

Michael Klein

Well, you know, there's a lot of betting on games these days. How would you bet that Warsh goes? Would he be more like David Souter, where he was...Souter was appointed to the Supreme Court by a Republican, but then came out with decisions that were perhaps not in line with the people who appointed him? Or do you think he'd be more along the lines of somebody who would continue to, as you put it, kowtow?

Binyamin Appelbaum

I guess I would just say this. We have seen what it looks like to stand up to the President. We have seen the current Fed chairman do that with a fair amount of courage and conviction. And

nothing that I've seen from Kevin Warsh to date suggests that he has comparable determination or integrity. So I worry a lot about where the Fed is headed.

Michael Klein

You have another piece in The Times where you say that the federal debt is going to tie the hands of the Fed. Could you explain why that would or could be the case, and what the implications of that are?

Binyamin Appelbaum

Yeah. So what we're worried about here is what's called fiscal dominance. And the basic idea is that a central bank can get into a position where the fiscal policymakers have borrowed so much money and need to keep borrowing so much money that they are pressing against the limits of their capacity. They need rates to stay low in order to be able to maintain that burden, and so they put pressure on the central bank to keep rates low for the purpose of facilitating government borrowing. We've already heard Donald Trump say out loud that this is one of the reasons that he wants the Fed to reduce interest rates is to reduce the burden of the federal debt. We're not yet at the point where it becomes impossible to avoid that. But in extreme cases, you can end up in a situation where a central bank is basically choosing between tolerating or even increasing inflation and the threat of a default on the federal debt. In situations well short of that absolute extreme case, you can be in situations in which there's just a lot of political pressure on the central bank to make life easier for the fiscal authorities. This has happened in a lot of other countries. It has also happened in the United States. In the period after World War II, this was the situation in this country. The Treasury essentially strong-armed the Fed to keep rates lower than they otherwise would have been for the purpose of essentially subsidizing federal borrowing. And the modern Fed era begins with an agreement in the early 1950s to allow the Fed to instead just focus on managing monetary policy to keep rates at the level that was appropriate for the health of the economy rather than health of the federal government's balance sheet. This year, we are likely to see a debt to GDP burden in excess of 100% for the first time since that post-World War II period – since 1946, actually. And so we are back in the situation where the federal government has historically put this kind of pressure on the Fed. I think the same rationale could produce a similar effort to pressure the Fed again. And it is another factor that is going to make life more difficult for the central bank going forward.

Michael Klein

In fact, there's been a lot of talk about the Treasury having more of a role in the Fed's decision making. So that's exactly the kind of thing that you're talking about.

Binyamin Appelbaum

Yeah, and it starts with little things, right? Kevin Warsh, one of the things he has said is that he doesn't think the Fed should hold mortgage-backed securities as part of its balance sheet, which

is not in and of itself a crazy position. People have different views on that issue. But he has said that it is tacitly a form of fiscal policy because it targets a particular sector of the economy and therefore the Treasury Department should have a role in determining what the Fed holds and how much it holds, and in unwinding this mortgage position. So on its face, it's a very modest form of intervention, but it cracks open a door to the Treasury's involvement in monetary policy that has been firmly closed for longer than either of us has been alive. And that, I think, creates a real risk that the door is opened wider. And I think people should be worried about it.

Michael Klein

So I want to thank you, Binyamin. This has been a really interesting hour, I really appreciate it. I hesitate to say this is the Economists' Hour, taking the title from your book, but it felt that way to me. And I very much appreciate you participating in this EconoFact Ask Me Anything webinar.

Binyamin Appelbaum

My pleasure.

Michael Klein

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