

Another Talk With Martin Wolf

Conversazione tra Paul Krugman e Martin Wolf

TRANSCRIPT

Wolf Well, Paul. Hello. How are you?

Krugman I'm good. How are you, Martin?

Wolf I'm feeling pretty good. Let's talk about where we are with our favourite villain, Donald Trump or President Trump, as he should be called. Now, we're getting towards the end of a year, and I get the impression from reading your Substack that you're feeling that things are going so badly, as it were. And the American people have really begun to notice this.

And maybe things aren't quite as grim. At least they're grim, but the grimness implies maybe things will get better in the not incredibly distant future. So overall, how are you feeling?

Krugman Well, I'm less terrified than I was. I mean, if you're... let's be serious here.

What is clearly the agenda? I mean, this is not a normal presidency. This is not normal politics in the United States. What we have is a group of would be authoritarians trying to speedrun a transition into one party, non-democratic rule. It's clear that the goal was to by - before anybody had a chance really to stand up to them to end US democracy more or less permanently. I mean, that's not hyperbole. That's just where we are. And the good news is, it does not seem to be going well, or at least it's not going according to schedule. People like Orban in Hungary or Putin in his early years had broad public support during their extended takeovers. Trump's support has cratered. If you had doubts about the polling, these elections in New Jersey and Virginia that we had early in November said, oh, no, the polling is right, if anything, it's understating how much the public now loathes Donald Trump. Now, that's not

necessarily enough. There are still a lot of craven politicians and craven institutions. At least the momentum has slowed. Now, whether we can actually turn this around, ask me in a couple of years.

Wolf The big point you make there is one I've been completely convinced of for a very long time. In fact, even in 2016, I think I've noted before that I fear that if he were allowed to, that was exactly where Donald Trump was going to try and take the US, and of course, with him, most of the hope for liberal democracy in the world. And so I've been also very, very anxious. And I've been surprised, actually, how many of my friends who are also very concerned about the issue have been really remarkably complacent about it all. But on this, you and I agree completely. Now, let's just step back and talk a little bit about what we're going to be trying to do. This is going to be the second series with you, the Wolf-Krugman Exchange, as we called it, on our Economics Show, and we're going to have four episodes running over the next four weeks. And we'll be talking about what's going on in the US, what's going on in the world, and where all this might lead us after having experienced this first year, which we just touched upon. And we also, of course, particularly be focusing on the US economy. We'll look at Maga Man. How much of the economics of male employment and male income driving support for Trump. And we'll discuss, I think, how other countries are reacting to the United States' rather unpredictable approach to economic policy and we might say foreign policy,

given the *démarche* that the US just gave to Ukraine on a deal which they seem to have negotiated entirely with Mr. Putin's people. It's a pretty weird story, even now, isn't it?

Krugman Oh, everything is weird. And we're in a situation where on diplomacy, we're actually getting conflicting stories from different members of the administration about what the policy is, who wrote it. The initial leaked peace plan showed clear signs of having been translated directly from the Russian. The syntax was basically not that of a native English speaker. While stuff, you think about policy in terms there's a process and who are the players and how does it work. But this appears to be no

process. And there's reason to believe that different actors, the vice-president, the Secretary of State,

are kind of independently trying to make foreign policy. And it's not at all clear that Trump has any idea what's going on. I mean, this is wild. World's greatest nation, and here we are. We're putting tinpot dictatorships to shame in terms of our disorganization.

Wolf I was just told by one of my colleagues, distinguished colleague, who was in America last week that every single Russian expert in the State Department has been sacked. So it's not surprising. I'm assuming that's correct. It's not surprising that they look completely clueless and they have to take the texts given to them by the Russians.

Krugman Yeah, we could go on about that. I mean, this is, of course, the diplomacy. But as far as we can make out, things like healthcare, basically large parts of the Centres for Disease Control, National Institutes of Health, they've laid off anybody who knew anything. And so we have critical policy being made by people who really haven't the faintest idea how any of this works. So I've been saying that we're kind of ruled by sinister incompetents right now, and quite something.

Wolf One sort of has this terrifying nightmare that they're actually going to start World War Three by accident.

Krugman Well, yeah. Pressing the wrong button. Well, there was this incident a while back where they accidentally laid off all the people who secure our nuclear weapons.

Wolf Yes, I remember that.

Krugman And then realised, oh, and then had a hard time getting them back because they had taken away their government emails.

Wolf Anyway, in our series we'll talk about China too, which beyond the US, the rest of the world, Europe and so forth. But let's kick off with something we often do on The Economics Show, where we put something on a scale from 1 to 10. So after a year of Trump, how healthy in one number scale 1 to 10, with one terrible and 10 everything is great, do you feel the US economy is now and perhaps also in comparison with where it was in January?

Krugman It's clearly in worse shape than it was in January. And maybe it's a five. Maybe, I mean, the normal indicators, unemployment rate, inflation rate are worse than they were in 2024. Unemployment is a few tenths of a percentage point higher. Inflation, which had been on a downward trajectory, is now up.

It's not catastrophe. We're not in a recession. But then there are weird shadows in the economy that make it, in some ways, considerably worse, probably in terms of how it's experienced than these conventional numbers would say. And also huge risks, because it's so much is being driven by highly speculative investments in AI.

Wolf When I thought about this question, I would have given them about a five too. So at a distance, I would agree. It isn't a catastrophe, but it's clearly of sliding down hill. And before we go on to that a little bit more, what would your number between 1 and 10

be for the state of American democracy at the moment?

Krugman Oh, I mean, we're below that. We're at a four or a three, but not a zero. I mean, and maybe be trending up. I mean, that's... there just has been a lot more pushback. I mean, we certainly... things are happening on a routine basis now that were completely unthinkable. I mean, if your worst fantasy, did you imagine that masked government agents would be kidnapping people off the street? And that's now a routine occurrence in our major cities. So, gosh, this is not a fully functioning democracy.

And we look enviously at places that know how to do democracy seriously, like Brazil, and pretty humiliating for an American. Public pushback, a lot of institutions just folded,

but the public has not. And so they I think they're not... I'm just vastly encouraged by the fact that we did have just gubernatorial elections, but they were blowouts for what is clearly a referendum on Trump, and if you look underneath it's in some ways even better. It really does look as if the idea that there was a MAGA coalition that was going to rule is not going to happen unless they basically use force and intimidation, which

is not out of the question.

Wolf I was just thinking about your comment about a country with a functioning democracy. I would also say a country with a functioning legal system, because they put Bolsonaro in prison. And the American president's reaction to that was to whack a 50v per cent tariff on them for the cheek of putting somebody who was trying to overthrow an election into prison, which is obviously from his point of view, a pretty horrible precedent. But it certainly gets the contrast. And it is, for somebody like me, always an Americanophile, absolutely horrifying.

Krugman Yeah, it's absolutely horrifying. But then if you like some of those tariffs, many of those tariffs on Brazil have just come off because American consumers are outraged about the price of coffee. And so that's in a way telling you, we would love to see that there was a mass public uprising against the threat to democracy. And we did have something like seven million people march against Trump not very long ago. But what really is killing the Trump, the Maga drive to take over America is the price of groceries. My view had been that what has happened has very dire long-term consequences, but I wasn't clear that there was going to be some crash, at least on the actions he's taken so far. So what's been happening to the economy hasn't really surprised me.

I see protection of this kind as more likely to have longer term, medium to long-term effects than short term effects.

Wolf Have you been surprised in any way by what you describe as the number five economies, or is that more or less what you would have guessed?

Krugman I think I'm pretty much on record as saying that this idea that protectionism causes a recession is not really right. It's not borne out by history. It's not borne out actually by basic economic models. Tariffs degrade long-run efficiency. They hurt long-run performance.

Now, what was special and is visible in some of the numbers is the uncertainty.

It's one thing if Trump had just sort of permanently imposed tariffs that were 1934 level,

I wouldn't have said that would be recessionary at all, be a terrible thing for the long run, but not recessionary. But it was the uncertainty, the constantly changing tariffs

that we seemed likely to have a chilling effect on business. How's a business going to invest when it has no idea what the trade regime will be next month? You can see it a little bit more subtly in some of the numbers. But at the same time, unfortunately, history

doesn't serve us controlled experiments where just one thing happens at a time. So we have simultaneously this radical break with 90 years of US trade policy, and at the same time, this vast boom in artificial intelligence.

And so most investment is kind of weak. Most businesses are not hiring. But on the other hand, they're spending enormous amounts of money on data centres. And that in some ways has masked whatever the effects of Trump's policies might be.

Wolf Now, you've written quite a bit recently, I think, about vibes. Is that to you a significant part of as why it's not doing as well as you would expect, that it's not something concrete is that despite this huge AI investment boom, but somehow the mood, if you look at confidence measures of various kinds, the Americans really do seem rather gloomy. Is that what you're talking about?

Krugman Yes. Now, it's not, by the way, we should say that consumer spending has not fallen as much, has not fallen a lot, despite the fact that people say that they're quite unhappy with the economy. So in some sense, this is - if we look at what people do rather than what they say - it's a little bit out of kilter.

But yeah, I mean, many people have made the analogy with the late '90s with, which was both the dotcoms, but even more important, the telecom investment boom, which ended in grief for a lot of companies. People were giddy. The ordinary person was feeling that they were part of this great adventure of prosperity. Now, it didn't last, but they... and there's been none of that now. There's nobody out there who is thinking,

well, Nvidia is doing well and that means that anybody can make it. That's not how it's playing now. Consumer sentiment is at its lowest point ever. It's lower than it was in the aftermath of the 2008 financial crisis. It's lower than it was in 1980 when we had 14 per cent inflation. People are really, really down on the economy.

And it's interesting because they've remained... I had thought that Trump might be getting better ratings on the economy than Biden did. But in fact, the vibecession has, if anything, intensified.

Wolf So why do you think that is? What's going on here? I was just thinking, as you were talking, that I recognise this contrast with the late '90s. Well, I think the overall economy

seemed to be doing better. Was part of it with the dotcom bubble, everybody felt they could get in on it. But here what we're seeing is booming expenditure by a really small number of gigantic companies, which is quite different from the players in that they

are real businesses. There's no doubt about that. But they looked like a bunch of incredibly powerful oligopolists. And that doesn't really excite ordinary Americans because it doesn't really have anything to do with them.

Krugman Yeah. I mean, the dotcom stuff was sometimes silly, often silly. And people even kind of recognised the silliness. But it was kind of nice, I mean, a feeling that there were opportunities. Everybody, I think everybody understood that some of these things were really not going to work.

And now, yeah, it's the same. I mean, having Google and Mark Zuckerberg leading the charge into the future does not give you a lot of confidence that the future is going to be very good for the common man.

Wolf I just wrote a column last week on Mark Zuckerberg's business, in which I pointed out that there's a recent very detailed and I think, well-researched report by Reuters, which indicates that about 10 per cent of their profits come from advertising for scams. Well, I think that's sort of filtering through to people, isn't it? I mean, this is a bit of a deviation, but isn't there some sort of awareness that some of these businesses aren't really quite the businesses we want to be so big and powerful. Is that actually - is that part of the vibe, before we go back to the economics?

Krugman Yes, I think it is. And I think people do have a sense, first of all, that these businesses are very heavily built on scams, on basically hacking your brain to indulging

and encouraging your worst instincts. Not a day goes by without some horror story about ChatGPT encouraging people to do something stupid or self-destructive. And if we have a government that clearly, basically is a government of by, and for predators, that's in ways that... including ways that I probably, we won't get into. And that does filter through. Everybody has a kind of sick feeling about where we are right now.

Wolf Do you think that one of the factors here, which you've written a lot about and it seems to me very important for the American, ordinary American sense of themselves, is that this government administration is so blatantly corrupt and so obviously in bed with a very small number of immensely wealthy plutocrats, and to a degree, which of course, this was the famous story, back in the beginning of the last century, the great Gilded Age period. But this seems in practise to be more egregious. Is this part of the vibe Americans are having? Is that part of what they're reacting against?

Krugman Well, it's very hard to pin that down. And I suspect that fewer people than you think are really aware of that. One of the things we've learned, and I'm following the political scientists and poll analysts and so on, is that it's very difficult for people like you and me who are immersed in this stuff, to appreciate how tangential much of the news is to ordinary people. And I'm not sure, even if you did a poll and you asked, are you aware of that Musk gets a lot, Elon Musk gets a lot of his money from government contracts. I would guess that many people are not. But I think there is a general sense that it's unfair.

Inequality doesn't actually have as much traction politically as you might expect, but unfairness does. And the sense of that we're in a regime of unfairness everywhere really does.

Wolf Now, we've been reading a lot over here about this affordability idea, and that is obviously what Mr Mamdani campaigned on in New York. And he only won a pretty spectacular victory and an encomium from Donald Trump, which I must say, must be one of the most surprising meetings I've ever seen in my fairly lengthy life. Is he onto something here that somehow this links, perhaps with their feeling about what happened with the inflation under Joe Biden, that there are really important things

that have become unaffordable for ordinary people. You've written about housing, rental rents and so forth. How live is that really is an issue? And do you think it will last?

Krugman We had a bout of inflation really from 2021 to 2023. It really was a one-time step jump in prices. People are upset about the jump in the level of prices, especially because we'd had three plus decades of very low inflation before it.

Wolf They expected 2 per cent a year, so 6 per cent over three years, and they got roughly 20. And that, sort of they say, we got cheated.

Krugman Yeah. Wages went up a lot and contrary to what many people believe, wages rose more towards the bottom of the wage distribution. So we actually had an equalisation. So ordinary struggling, struggling families on the whole were better off in terms of purchasing power. But it's a natural thing. You feel that you earned your wage increase and then it was snatched away by inflation. So that's a big part of it.

Also, the Consumer Price Index is honest. It's based on a lot of hard thinking about how to measure the cost of living. But it may be missing some things. It doesn't really take account of interest costs. It doesn't take account of, particularly the housing is one of those things where prices really have outpaced earnings. And so the sense that my father was able to buy a house and I can't, that is not wrong. Wages have risen more than grocery prices over the last five years or so, but wages have not risen more than housing prices.

And so there's some real affordability stuff.

Wolf But doesn't this imply that Mr Mamdani is not going to be able to do much about affordability, but then neither is Mr Trump given that the tariffs presumably the price effects of the tariffs, as I see it, are still coming through because a lot of the price effect was clearly absorbed by business. But it's not going to be absorbed forever, is it?

Krugman That's right. Although one quirk is that it's turned out that the effective tariffs are not as high as the posted tariffs. And part of the reason there is it's not really

we think a lot of illegal tariff evasion. But there were a lot of things that businesses

could do to avoid paying tariffs that weren't worth doing when we had 2 per cent tariffs and are worth doing when we have 17 per cent tariffs. But the pass through. Yeah we've probably seen something like half of the eventual price impact of tariffs on consumer prices. And the rest is working its way through the pipeline.

Part of the reason that the rage over affordability has persisted, I think that might have started to fade if we'd had some kind of continuity. Except Trump ran a campaign all about, I am going to bring prices down. I'm going to cut the price of energy in half. I'm going to make your groceries much cheaper, and then obviously hasn't delivered on that and hasn't even made an effort to deliver on that. And people feel betrayed, which is coming back to where we started. I'm glad that people feel betrayed. This is important.

Wolf Well, obviously, he works on the assumption that the promises I made have nothing to do with what happened six months later. People shouldn't hold me to account for something I said six months earlier. That's just unfair.

Krugman Yeah. I mean, this is Trump's whole modus operandi is that he - a promise from Trump is a suggestion at best. But that kind of works when you're dealing with, I don't know, university presidents. But it doesn't work when you're dealing with the American public.

Wolf Just one final thing on the tariffs. We've got this really rather important case in front of the Supreme Court on whether what he's done is legal. And my own reading of American trade law, and I know a few experts, is that it isn't. My confidence that the Supreme Court will decide that it's illegal isn't very great, given some of the other things they've decided. What do you think the Supreme Court's going to do?

Krugman My guess is that this may be a step too far, even for this Supreme Court.

The president can do some special things to deal with economic emergencies.

But when Trump imposes tariffs on Brazil because they have the temerity to try Bolsonaro, I don't think fits the definition of an economic emergency. And two lower courts have already ruled that the tariffs are, in fact, illegal.

The prediction markets say that there is only a 26 per cent chance, as of this morning,

that the court will uphold Trump's tariffs, which looks about right to me. And this is about 70 per cent of the tariffs would be voided.

Wolf Can he get around that? Can he ignore it?

Krugman Well, just blatantly ignoring it I think does become a problem. I mean, if this is an issue that applies much more to things like members of the military. But if you're a Customs and Border Patrol agent and you collect a tariff that the Supreme Court has ruled illegal, I think that you are personally liable. You have yourself broken the law.

Wolf He couldn't pretend that quote unquote, 'breaking the law is an official act,' which the Trump waged the Supreme Court, in an earlier judgement decided was actually completely kosher.

Krugman Yeah, well, there are other routes around. The president has a lot of leeway to impose tariffs to protect national security — Section 232. And Trump has been doing that quite a lot, so not all of it is under this Emergency Powers Act. But there too, I would imagine that the potential legal challenges are huge. I mean, he's imposed national security tariffs on bathroom vanities because God help us if we get into an international conflict and we depend on China for our bathroom vanities.

On any reasonable standard, almost everything he's done on trade is illegal. But we do not live in an age of reasonable standards.

So it could be possibly a very important judgement.

Wolf Yes, it could be. Because if they do come out against him, that's an important loss on what is after all, for him and for the world his signature policy.

Krugman Yeah. And it's humiliating if the court rules that his signature policy is illegal and I think we're less certain, but it does look hard to see how you can rule that the tariffs were illegal and avoid giving the money back.

Wolf So quite a scene. So let's talk about the labour market. Is what's going on there a significant factor for this vibe session, as it were, more than that, sort of anxiety about prospects for jobs?

Krugman We have not yet had mass layoffs. We've not yet seen large job losses.

But what we have seen... Not a lot of hiring. ..very low hiring. It's a frozen labour market, probably, at least in part because of tariffs and general uncertainty. But businesses are not hiring. They're not firing a lot either. If you're in your job, then you're reasonably secure.

But should you lose your job, or if you're a young person entering the market for the first time, it's actually very grim. Overall, unemployment isn't up very much, but long-term unemployment is because once you've lost a job, it's very hard to find another one. And this does reflect back even on people who have jobs.. It's frightening. If you lose a job, you've had it. And I better not get sassy with my boss because if I'm laid off, then I'm in big trouble. And so this does colour people's people's perceptions. Also, it's a tragedy. I mean, what happens if young people starting their careers enter into a weak labour market and have a hard time finding a job? How long does it take them to recover from that bad start? And the basic answer is forever. If the labour market is poor when you're starting out, you are put permanently down. You never get as far up the ladder as you would have otherwise. And so this is a big deal.

Wolf I think this actually is what we're seeing in Britain, have been seeing. We have had a really rather weak labour market in exactly this sense, even compared to our European peers. I'm not talking about America over the last... since the pandemic. And I think it's become a very deep source of anxiety for young people, percolates through to their parents because they're concerned about them, too. And I think it's a big source of worry. So I think, and I think it's considerably worse than in the US, from what little I know, so in this area. So I recognise this concern. But so what's causing it? It would suggest that the employers are being very cautious. They don't want to hire because they don't what's going to happen next. But it also would suggest that basically underlying demand is quite weak. And that seems to justify the Fed to cut rates.

And some people on the Fed are saying they should. At the same time, well, inflation is pretty damn sticky.

So how do you read that if you were sitting on the Fed board, what do you think they should be doing?

Krugman Glad I'm not sitting on the Fed board.

Wolf Yeah, I agree.

Krugman I actually know people who go around muttering dual mandate, dual mandate because it's really hard, because of the employment...

Wolf I know quite a few too. And I think it's a very tough job at the moment.

Krugman And by the way, if it's weak demand, you would expect more layoffs. It might be weak demand, but it might be also just this freezing effect of uncertainty and possibly, possibly AI. There's at least some straws in the wind that suggest that early business applications of AI are reducing hiring, or particularly of college graduates, or simply that companies are kind of waiting for AI. That if you're Amazon, you're hoping to replace a lot of your workers with robots a year or two down the pike. You might not want to hire a lot of people now. So, it's a little bit of a mystery. I've never seen anything like it. We normally have a pretty one-to-one relationship between the unemployment rate and hiring rates, and this situation of not especially high unemployment

but very weak hiring is really quite novel.

Wolf That could be, of course, as you say, the uncertainty. That could be tariff generated or tariff policy generated. And is the sticky inflation, despite what seems not a very strong economy, also related to that?

Krugman No, I mean, my guess, if anything, the inflation maybe actually you could say that the tariff uncertainty has limited, has slowed the pass through of tariffs into consumer prices. Raising prices does piss off your customers, to use the technical term. And if you think the tariffs might go away, I mean if you think that sometime in the next few weeks the Supreme Court might rule that all those tariffs that are making your products expensive may disappear in a puff of smoke, then you may choose to eat the tariffs until that's resolved. As I said, you're thinking about being a Fed - Federal Open Market Committee member and you say, so what is happening to the economy? And the answer is God knows. How do you make an interest rate call in that situation?

Wolf So let's look at the other area of really big uncertainty. You just mentioned AI's impact on the jobs market. I suppose that would suggest that productivity is improving. It might be... if that's... they're doing more with fewer workers. That might suggest inflation could fall, should be falling. Separate the two effects of the AI. Just say a little bit more about where you are now, we discussed it in the previous series, on this issue of is there going to be a jobageddon, as it were, as a result of AI. Are we going to suddenly start seeing really dramatic affects on the employment of relatively educated young workers, which I've always thought would be a nightmare politically for all our societies.

If you can't give these people good prospects, well, these are the people who start revolutions. They did that, young unemployed people who have got educated degrees and so forth, that's how all the 1848 revolutions started. So this is a big deal politically. Is this what we might be seeing?

Krugman It's possible. I mean, so far again, it's all pretty modest as far as we can tell. It is so difficult to interpret the various studies. Most businesses report that they have not actually succeeded in making productive use of AI, but some have. And then there's some... it's all over the place. And there's also this weird thing, which is that a number of businesses are telling their employees must use AI and when they can't actually figure out what good it does them. So we're in this kind of liminal space where it's all potential and hype. And maybe, I mean, what it can do is... it used to be that there were lots of things that were simple, common sense things that we just couldn't do, like recognise the same object seen from different angles. And all of a sudden, all of that is a solved problem. Translation by computer was a joke, and all of a sudden it becomes actually pretty damn good. So there's no question this is a powerful, productive technology, but we don't know yet. And then, of course, I guess there's a short run macroeconomic impact, which is that this is driving a lot of business investment and it's driving the stock market. And quite possible, as was the case in the late '90s, that you have a genuine, productive, important technology and everybody who invests heavily in it loses their shirt.

Wolf Let's come to that because that's the other aspect of it. So there are two aspects of this. One, the stock market is incredibly buoyant because of this or has been and maybe it's filtering over into some other speculative bubbles. I think you just wrote about Bitcoin. That may also be related to the deregulation going on, the encouragement of cryptocurrencies more broadly. And that may be really separate from AI, but it's noticeable.

So there must be a wealth effect, I mean, at least among relatively well-off people, because stocks of these major companies have gone through the moon. And second, associated with that, there's a huge investment boom, which this is funding.

The stock market must be funding to some degree. Now, if it turns out that the investment doesn't really get a decent return, which is perfectly plausible given that we don't see business models, then two things will happen. The stock prices will fall and the investment will fall, decline, weaken dramatically, and they will have all this stuff which will have been built, data centres and so forth, but it really will be very low return, though perhaps quite useful in some way. But this is bad for the future of the economy and the administration, with the budget and so forth, we've shot the macroeconomic bolts, except for the monetary policy ones.

And then there is a concern out there that actually they're beginning to borrow more. It's not all funded out of profits.

There are marginal companies borrowing a lot. There is a lot going on in private credit, which we don't really understand. And there are financial risks. So what's the downside here?

Krugman How bad could it get? I don't have any real reading on this, but there are these negative stories you can tell about where we are. Yeah, a lot of talk about the circular financing of the AI related companies are all kind of taking in each other's washing, making the bottom lines look artificially good. Well, they is a circularity. They are borrowing. A year ago, you can say, well, this AI boom is being financed out of retained earnings. And so yeah, Meta may lose a lot of money but who cares? But now there's a lot of borrowing. And markets are taking note. Oracle, credit default swaps, I feel young again. It's like going back to 2008.

But the credit default swaps on Oracle have just blown out, suggesting that people do think there's a significant risk that one of the big players here might end up defaulting on some of the debt that it's taken on. Financial stability is always a game of whack-a-mole. You're always trying to knock down financial risks. And you're often at risk of fighting the last war.

So we dealt with a lot of the old shadow banking stuff, but now we have private credit that creates a whole new set of risks that are at some level, at a metaphysical level, similar to the old shadow banking stuff.

I don't think we're at the edge of another financial crisis, but then to be honest, I didn't think that in 2007 either.

Wolf Well, I didn't then, but I was more worried than I am now, because I tend to think this is narrower, and I think it's not related to housing, which is a classic asset class to create problems. We saw that all over Europe, and the big companies involved in this are in cash flow and profit terms, basically about as solid as a company can possibly be. Microsoft, Google, Meta, these are pretty solid companies. So if you succeed in getting a colossal financial crisis out of this, I think that would be quite a major achievement.

Krugman The financial crisis is not high on my list of things to worry about. But then again, our track record, the IMF once did a systematic study of how successful economists are at predicting recessions. And the answer is a zero success rate.

So...

Wolf Well, that is slight. What does worry me is that when this happens, it could well be under another Fed chair. And that might not be a very sensible person. And I think on the whole, he made a few mistakes, Jay's been a pretty sensible person and by and large, actually over the last 20, 25, 30 years, you've had pretty sensible Fed chairs. And that might not be true a year from now. And that could make a big difference.

The Fed chair really matters if there's problems.

Krugman Yeah. Without getting into the individuals, but the people on the short list range from somewhat weak to absolutely horrifying.

Now, one saving grace to some extent is that the Fed chair is not a chief executive who

can just make the decisions on monetary policy. It's a committee. And the committee seems likely to remain sensible, at least for a couple of years.

So you're saying that these investments will leave us with useful stuff. That's one of the things that's unclear. When the '90s investments, you ended up with a lot of fibre optic cable in the ground that didn't get used right away but was eventually useful. But the data centres probably depreciate quite fast. And so in some ways, this is more like the companies that got over their skids on shale, which turned out... it's turned out that shale wells depreciate much faster than conventional oil and gas wells. And so we might have a bubble, a big waste of resources that is really lost. We may be just burning up real resources on stuff that won't get used, especially if they're kind of taking the wrong approach. One of the things that we're worrying about now is that the Chinese have been focusing on smaller models that are less comprehensive, that apparently can achieve about 90 per cent of the effectiveness of the big models at far lower cost. Aside from the inherent questions about AI, there's also the question of are we doing AI wrong? That is, I think, a really interesting possibility.

Wolf And that would certainly justify a pretty big collapse in stock prices and investment. I've just been to China, and they certainly do feel that they've got a more sensible approach. And when you look at the amounts being spent on these data centres and the dubious benefits in terms of improvements at the margin, you can ask that question. The Chinese have to make do, do more with less. And often in history, that's turned out to be a pretty good approach, hasn't it? Let's put this all together.

People aren't very happy about the economy. You've still got the Epstein files.

They certainly seem to be an amazingly hot topic. Trump's approval is remarkably low. So coming back to where we started, could we begin to feel that not only are we past peak Trump, but that we should really begin to feel that the American system will be able to get through this?

Krugman And I'm not sure. But what might be the case, it seems to me, that in order to maintain power, obviously they will be terrified of losing power, they're going to have to do some really egregious things, like putting the army or National Guard or both into places when important votes happen, like the midterms, in order to discourage people from voting. It would be so obvious that this is a coup attempt and they might not get away with it.

Wolf So I'm beginning to feel maybe this will work out. How optimistic are you of that?

I mean, I thought of it, it was 2 to 1 on at this stage about 10 months ago, eight months ago, that Trump would get away with it and he would create a dictatorship. But now, I'm beginning to think it's less than evens.

Krugman My view is that it's more likely than not that the autogolpe, the self-coup will fail, that Trump and company will not succeed in installing permanent autocratic rule in America. It tells you something about where we are that believing that they probably won't do that makes me optimistic. So no, it's still very scary, but it's really looking like they may not be able to pull this off. Now, that doesn't mean that we've gotten through it safely, even if we have, even if that's how it works out. For one thing, an enormous amount of damage has been done. Of course, to America and to the world. To us, to the world. I mean, the United States was the essential country and we are now completely unreliable. Nobody will trust America for decades, even if it ends. And then there's this longer term question.

Even if we get through, and we end up with a Democratic Congress next year, and then we end up with a Democratic president in 2028, winning every election is not a reliable strategy for safeguarding democracy. So the fact that just on the political side, if we don't end up not just holding back this bum's rush from Maga but if we don't end up having a truth and reconciliation commission of some kind, some accountability for all of this, then we're still in very, very bad shape.

Wolf The thing that particularly worries me, and I follow this very closely, and perhaps it's partly because of my family background, but - my history of my family is refugees from Hitler - there seems a remarkable amount, I mean, astounding amount of

genuine, clear fascism, even Nazism, circulating around on the extreme right. And even three or four years ago, I wasn't aware of that. And it's possible if the Republicans are in opposition, that's where they're going to go. These people only have to win once and you really have a problem.

Krugman It remains very, very scary, I think. But I certainly will feel better if the... it looks as though they haven't pulled this one off. Yeah. Put one foot in front of the other.

If we ask, what can we do to guarantee the survival of American democracy? The answer is no guarantees.

Wolf I'm writing a piece on that as a new chapter for my book, and it's a very, very good question. So in next week's episode, we're going to talk about the economics of Maga men. And it is Maga Man, to a significant extent, isn't it, and more generally, the manosphere or whatever you call it. On the other hand, well, what does the newly elected New York Mayor Zohran Mamdani tell us? What does that mean about the future of the Democrats?

And look at it from the economic point of view. And meanwhile, I think it's your turn to tell us about your cultural coda.

Krugman Actually, the one that captured my mood most correctly is some old Pink Floyd, The Great Gig In the Sky where the lyrics consist of nothing but an extended, wordless scream. That's kind of where I am in my view of the world right now.

Wolf So when I was asked to do this, I found it, I think, much more difficult than you do. But as I said before, I'm a sort of opera person. And I was thinking about the best things about tyranny, which has after all been the theme. Last time I think I had Fidelio from Beethoven. This one is even more direct. It's from Puccini's Tosca, which is about the evil ways of an Italian police boss who's really a gangster called Scarpia.

And the song is by Tosca, who's the heroine, whose lover has been tortured and she sings this absolutely magnificent song, Vissi d'Arte. I lived for art. I was a peaceful, loving, decent and honourable human being. Why, God, have you inflicted this upon me? Well, all I can say is our cultural references are not very much like what you

expect from a couple of economists, but here we are. Well, yeah, you have to remember,

even economists are human beings sometimes.

Krugman Some of us.

Wolf And that's it for the Wolf-Krugman Exchange on The Economic Show for this week, and we'll be back here at the same time next week.