

SICKENING AND CYCLICAL: COVID-19 AND ITS IMPACT ON THE CURRENT BUSINESS CYCLE

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ABSTRACT: As the COVID-19 pandemic progressed, there were significant government interventions in the market. This paper is concerned with the business cycle and the role of regime uncertainty on investment and will not be addressing the effects on economic growth that may be occurring. The government-mandated shutdown, paired with the CARES Act stimulus of the economy, created unique circumstances for the current business cycle. It affected the way traditional Austrian Business Cycle theory will manifest itself. The shutdown of the economy and severe monetary intervention during the COVID pandemic have not been seen in American history. As the pandemic has continued, unemployment has skyrocketed, and as has the welfare state in taking over the unemployed's support. Although inflation has had its typical effects in the short run during a boom, there is still an apparent manifestation of the business cycle. This business cycle is incredibly unique for this very reason.

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I. Introduction

The scale of government intervention in the economy has drastically increased following the COVID-19 pandemic. When COVID-19 began its spread, there was much uncertainty about how it could be stopped. Governors of certain states closed the economies in their states with the exclusion of business and industries deemed “essential.” During this time, there was economic turmoil and many shortages in those industries that were deemed essential. These industries were ones that the government believed to be vital to the survival of the nation. The shutdown of the economy resulted in significant unemployment, which led to a government increase in the welfare state. The federal government released the Coronavirus Aid Relief and Economic Security Act (CARES) stimulus package in March of 2020. As months went by, there seemed to be improvement in the economy based on what the economic indicators were saying, and towards June, it seemed like

recovery was imminent. However, as the later months of 2020 unfolded, a new wave of COVID cases prompted another intervention into the economy.

As many governors closed down their states’ economies in response to surges of new cases, the constitutionality of these actions has come into question. There are many courts that are ruling on these constitutional issues, which will have significant economic implications. When analyzing the effects of policy, the economist must set aside the ethical and constitutional validity of these government practices. This paper is concerned with the business cycle and the role of regime uncertainty on investment. It will not be addressing the effects on economic growth that may be occurring. The government-mandated shutdown paired with the CARES Act stimulus of the economy created unique circumstances for the current business cycle and affected the way traditional Austrian business cycle theory will manifest itself.

II. Reviewing the Literature

The first and most relevant literature to discuss is that literature on business cycle theory. After surveying this literature to establish our theoretical ground for economic analysis, this paper will overview the literature on regime uncertainty as elucidated by the economist Robert Higgs.

A. Austrian Business Cycle Theory

The CARES Act stimulus severely increased the money supply. The massive increase in the money supply will have major effects on consumption habits, interest rates, and many other aspects of the market. Business cycle theory is the field of study economists use to tease out the effects of changes in the money supply. It is one of the most debated aspects of economics due to the vast number of schools of thought. Though it is too daunting a task to address all these schools of thought in this paper, it is essential to establish what school of thought will be used in the present analysis, followed by some of the

literature that is being written by mainstream economists about economic shutdowns.

The Austrian understanding of the business cycle has been developed and furthered by some of the greatest economists, such as Mises, Hayek, Rothbard, Woods, Hazlitt, de Soto, and many others. The Austrian theory's understanding is based fundamentally on human action, which is the foundation on which the rest of the theory relies. Since humans apply means according to their preferences to achieve ends, certain economic laws have been discovered. The law of time preference is the foundation for understanding interest rates.¹ The law of marginal utility is the foundation for the understanding of inflation and its effects. In his book *Human Action*, Mises helps to frame all of this in the context of its intertemporal nature. All the previously listed authors and many others have made significant contributions to the Austrian theory

¹ LUDWIG VON MISES: HUMAN ACTION: A TREATISE ON ECONOMICS 4449 (MARTINO 2012) (1949).

of the business cycle. The Austrian theory couples the short and long term, which makes it more applicable and plausible to understand the real world. There are many critiques of the other mainstream schools worth researching, but these critiques will not be discussed outside of the context surrounding COVID-19.²

To support the claim that the economic shutdowns have impacted the business cycle, we must first understand the cycle theory this paper is utilizing. To establish an understanding of the business cycle, I will consult Woods, Hazlitt, Mises, Hayek, Rothbard, and de Soto. Tom Woods book *Meltdown* also helps to frame the most relevant parts from their arguments in the 2008 financial crisis context. During a boom, the government causes monetary inflation that will, in turn, lower interest rates and the purchasing power of money.³ It is important to remember that

² HENRY HAZLITT, FAILURE OF THE NEW ECONOMICS: AN ANALYSIS OF KEYNESIAN FALLACIES 98 (VAN NOSTRAND CO 2017) (1959).

³ *Id.* at 98.

interest rates are the price of loanable funds. This price is influenced by changes in demand and supply in the same way as all other commodity prices are. Therefore, there will be signals to the market that come from the lowering of the rate of interest.⁴ The government causes monetary inflation when assets are purchased from banks, allowing them to increase their reserves. These purchases allow banks to create the credit which has been generated from the intentional inflation. During credit expansion, lenders give funds to increasingly riskier ventures. The regular and most efficient market lines of production have already been undertaken, thus new market entrants must take less efficient production lines. This credit creation will have incentivized entrepreneurs to take out loans to expand their capital structures because the interest rate has signaled them to do so. The lower the interest rate, the less return individuals receive for their saving and investing.

⁴ *Id.* at 132.

The purchasing of more specific capital items creates asset price inflation and the lengthening of the production structure.⁵ The production structure is lengthened because the profits earned from inflation increase the demand for factors of production higher in the production structure. This brings about the Cantillon Effect, meaning that the first people to spend the new money have an advantage over the rest of the market because the purchasing power has yet to adjust. This means increased profits can be found where there were none before. Durable goods' production increases far past market demand, determined by people's time preferences, creating a cluster of malinvestment and errors.⁶ Loans that entrepreneurs have received will be put toward bidding for capital goods and will make false profits occur along the production structure. The inflation and credit expansion will have concentrated profits in

5 FRIEDRICH A. HAYEK, PROFITS, INTEREST, AND INVESTMENT 80-81 (AUGUSTUS M. KELLY 1969) (1939).

6 THOMAS E. WOODS, MELTDOWN: A FREE-MARKET LOOK AT WHY THE STOCK MARKET COLLAPSES, THE ECONOMY TANKED, AND GOVERNMENT BAILOUTS WILL MAKE THINGS WORSE (2009).

specific lines, creating what many refer to as a bubble.⁷

In the crisis phase, when the actual market demand is demonstrated by those who received lines of credit as profit, a crash will occur because these goods far exceeded the market demand. These lines of credit in production form bubbles. This will reduce the supply of credit from the amount generated during the boom. Interest rates will begin to rise according to time preferences. Many investors will start to pull out of their riskier projects when it becomes clear that time preferences are not satisfied. During this part of the crisis, there will be a financial panic. However, those entrepreneurs with superior foresight have already begun the liquidation of their assets in an attempt to not suffer as badly when the asset prices drop. Higher interest rates and lower demand for capital goods will cause the capital value to collapse. Lower capital value leads to losses for those engaged in the lengthening of the

7 JESUS HUERTA DE SOTO, MONEY, BANK CREDIT, AND ECONOMIC CYCLES 349 (MELINDA A. STROUP TRANS, LUDWIG VON MISES INST. 2006).

production structure while rewarding those who shortened it by either not borrowing during credit expansion or by liquidating before the crisis.⁸

The bust will occur when entrepreneurs who engaged in expansion without superior foresight begin their liquidation, which is known as the reallocation phase. They will sell their assets for significant losses to where the market can use them to satisfy consumer preferences better. The more specific to boom production the capital is, the less value it is going to have when it is reallocated. Banks will also fail during this time due to illiquidity and insolvency created during expansion.⁹ Credit will contract, and interest rates will decline because, even though the contraction of available credit increases interest rates, people after the crisis are already inclined to save enough that it makes the interest rate decrease. Purchasing power will rise during this time due to deflation, and this may

⁸ MISES, *supra* note 1, at 110.

⁹ DE SOTO, *supra* note 7, at 366.

lead the government to inflate. Still, the banks will keep the attempted reinflation as reserves after the suspicion due to concerns created by the panic they had just suffered.¹⁰

The recovery phase comes after reallocation is complete. It can be observed that there is no inflation or deflation, credit expansion or contraction, and that capital values normalize, prompting standard economic progress to resume. This is a simplified version of the Austrian perspective of the business cycle.

B. Regime Uncertainty

During the Great Depression, there was an evident drought of private investment shown by the drop of investment to GDP ratio from 1929 to 1932. In 1929 private investment made up 16% of GDP, and in 1932 it was down to 2% of GDP.¹¹ There was also a massive increase in government intervention in the economy.

¹⁰ *Id.* at 367.

¹¹ Robert Higgs, Regime Uncertainty: Why the Great Depression Lasted So Long and Why Prosperity Resumed after the War, 1 THE INDEPENDENT REV. 561, 565 (1997).

Higgs was not satisfied with the simple Keynesian explanation that the Animal Spirits were simply telling people not to invest. No one had yet put together that the lack of private investment not only exacerbated the Great Depression but also was a rational response to government interventions that business owners had. The significant threat of extreme taxes on income and the state's possible overtaking of production made owners very hesitant to reinvest in companies. Due to the uncertainty created by state intervention, the Great Depression was exacerbated. This theory of uncertainty is based on entrepreneurs' responses to the changing of present institutions.¹² These institutions are best thought of as "rules of the game." The entrepreneurs will adapt their strategy to operate most efficiently within the confines of these rules. However, when the rules change suddenly, so does the entire game. Before the intervention, the best way to "win the game"

¹² *Id.*

(achieve one's ends) would have been to provide a good or service more efficiently than a competitor in order to earn a profit. However, if the rules are changed so that the government can take one's profit through taxes, the game's objective has been changed. The ends and the means available to achieve these ends that the entrepreneurs seek are different from before. This may make activities such as lobbying and other seeking of special privilege more profitable. When governments change the institutional structure, it forces entrepreneurs to adapt and make changes.

C. Austrian's CARE(S)

In his writing for the Mises Wire, Douglas French shows that the CARES Act's stimulus is merely "kicking the can" further down the road. He shows that many banks are not receiving cash but are marking debts as being paid due to the intervention's nature. This raises the question: "How is this intervention affecting the business cycle?" French says that the crisis of the business cycle is

still coming but has just been delayed. The banks giving this treatment to their debt will have to recognize losses eventually.¹³ This would provide a causal implication that the business cycle will soon be coming into a crisis phase.

The International Journal of Banking recently published an article focused on the modeling of the CARES Act on the unemployment rate and consumption over the next few years. It makes the interesting claim that with or without the CARES stimulus, the economy would eventually end up at the same performance point on economic indicators according to their consumption and unemployment models. However, it seems that their primary contribution to the literature is that they would take standard unemployment models and consumption models but add special sections of data to account for the situation that COVID has provided. They added a “deeply

13 Douglas French, How the CARES Act Is Still Kicking the Can, MISES INSTITUTE (Aug. 20, 2020), <https://mises.org/wire/how-cares-act-still-kicking-can>.

unemployed” and a negative shock to the marginal propensity to consume to make the scenario more specific to COVID.¹⁴ Hazlitt’s critique of the “Marginal Propensity to Consume” makes it clear that there are significant issues with this concept that it should not be used for analysis.¹⁵ Although there is much to critique in this interpretation of data and the methodology, that is not our purpose. This work does not show any causality in the real-world changes that would affect human activity and has no root in microeconomics. For this reason, it seems that this interpretation is not very plausible.

III. Theory Applied to COVID-19

A. The Theoretical Economic Shutdown

To best understand the significant changes that occur to the business cycle when an economy is shut down, it helps to think of a hypothetical case where only one area

14 Christopher D. Carroll, Edmund Crawley, Jiri Slacalek, and Matthew N. White, Modeling the Consumption Response to the CARES Act, in FIN. AND ECON. DISCUSSION SERIES 2020-077. (Board of Governors of the Federal Reserve System, 2020), <https://doi.org/10.17016/feds.2020.077>.

15 HAZLITT, *supra* note 2, at 98-131.

of the market can be open. If a single sector of the market is open and a group of people is given a stimulus package that will be perceived as an increase in their real income, they will either spend the new income in the open market or save/invest their money. There is a difference in incentives for each option and a difference in the implications of these decisions. If the people choose to save, this means that they prefer to retain their money to deal with future uncertainty. If people spend their money in this sector because they perceive the stimulus as extra income, then the new money will affect the open market by increasing market prices. It is important to note that these two options are not mutually exclusive and could overlap, even within each person's decisions. The open market will see an increase in the demand for the open market's product due to the increased spending in their market. The incentive for this industry is to spend new profits on expanding their production process and capital goods. However, they will

not be able to do this since these capital-producing parts of the economy are shut down. The inability to exchange means that the price inflation will not affect the capital assets until the market production sectors open again. This means that price inflation will not create a bubble in these markets. However, there will be a change that occurs when the full market reopens. People will now have more options to spend their money. The producers that were able to operate and earn profits during the shutdown can finally buy assets. If this occurs, there will be asset price inflation.¹⁶ When people begin spending money in other places in the market, the open industries during the shutdown may also see a decrease in profits. In this case, the price inflation seen during the lockdown will likely return to average proportion with the rest of the price inflation throughout the economy. This inflation will be

16 MURRAY N. ROTHBARD, *MAN, ECONOMY, AND STATE: A TREATIST ON ECONOMIC PRINCIPLES WITH POWER AND MARKET: GOVERNMENT AND THE ECONOMY*, 869 (2ND ED. LUDWIG VON MISES INSTITUTE 2009).

distributed as it usually would be in the market and cause asset price inflation.

B. Business Cycle Specific to the Shutdown and CARES Act

The CARES Act authorized the spending of \$2.2 trillion on stimulus. The government gave part of this stimulus directly to households and individuals. Many different parts of this act allotted this money to the individual. Persons whose incomes were \$99,000 per year or less were given \$1,200. There were differences in the allocation of these grants based on dependents and household size. There were also significant increases in the government unemployment compensation for those who lost their job during the pandemic. The other part of this stimulus was given to businesses to aid them in paying off debts and rents. This act was a more substantially significant increase in spending than what has ever been seen before, even outdoing the stimulus of the “Great Recession” of

2009 that was only a mere \$831 billion (unadjusted to inflation). With such a substantial increase, the economist could have a small heart attack as they watch the monetary base increased by \$1.5 trillion over the course of a few months. It rose from around \$3.5 trillion to over \$5 trillion between January and March of 2020.¹⁷ Thus, the question now becomes: “Does the Austrian theory previously developed earlier in the paper hold to the real world?”

As one would guess, I believe the theory does hold. The first economic indicator worth considering is the prices for certain goods in industries that are deemed essential. The food industry was one of the parts of the market that remained open throughout the country, as it was deemed essential. After the stimulus was distributed, the Consumer Price Index jumped from 262 in March to 269 in June of 2020. This is significant inflation for a single industry to have in such a short time. It is almost half of

¹⁷ United States Money Supply M0 2019, TRADING ECONOMICS (May 11, 2019), <https://tradingeconomics.com/united-states/money-supply-m0>.

the price inflation seen in the entire year of 2008 when the last major stimulus bill was distributed, yet this was only a three-month period.¹⁸ However, when the market economy began to reopen in June in many conservative states, the CPI for the food industry stopped inflating, decreased slightly, and then held steady. This is consistent with the theory that when the market is allowed to reopen, people will no longer spend their stimulus in the same ways that they did before. It means that the open industries will not have the same demand that was being shown for their products as they did during the initial shutdown. Prices at this point should inflate throughout the market.

Another sector of the market that was significantly affected was industrial gas manufacturing. Although this industry itself was allowed to stay open, it nonetheless suffered from operating at a reduced capacity. However,

¹⁸ Consumer Price Index for All Urban Consumers: Food and Beverages in U.S. City Average, Fed. Res. Econ. Data, <https://fred.stlouisfed.org/series/CPIFABSL> (last visited Mar. 25, 2021).

many of the industries that use this gas saw a great reduction in their demand. Most likely this was due to the massive travel restrictions that were being enforced throughout the United States. The industrial gas manufacturing industry saw price deflation dropping nearly 17 points on the Consumer Price Index.¹⁹ The massive inflation could not circulate according to the demands of a normal open market and sectors of the economy that were shut down saw none of the profits from the stimulus.

Another industry that was hit particularly hard by government regulation and a subsequent drop in demand was the airline industry. This industry dropped on the CPI from 294.6 to 248.8. Early in the pandemic, almost all domestic flights were being canceled, and international travel was nearly impossible. Along with government intervention, there was also the perception that flying was not safe due to the pandemic's contagious nature.

¹⁹ *Id.*

Similar falls were seen in industries that produced apparel and other goods deemed non-essential.²⁰ Such relative deflations in the more COVID-19 regulated industries and inflations in the less COVID-19 regulated industries support the theory that inflation will manifest itself into the open sectors of the economy.

C. Show Me the Money

It is also important to acknowledge the other areas where the new money from the CARES Act was allocated. A significant amount of this money was used to relieve debt. Many businesses received loans and aid from the government. There were a significant number of businesses that used this aid to pay their rent. The companies that were not profitable and on the verge of closing down received bailouts from the government. The bank excess reserves represent an indicator of how companies operated during

²⁰ Table 7. Consumer Price Index for All Urban Consumers (CPI-U): U.S. City Average, by Expenditure Category, 12-Month Analysis Table, U.S. Bureau of Lab. Stat. (Mar. 10, 2021), <https://www.bls.gov/news.release/cpi.t07.htm#cipress7.f.4>.

this time. Such reserves saw increases of \$1.4 trillion. This indicates that banks received the subsidies and inflation during the crisis instead of the usual rent and interest owed by borrowers. This was a way in which the debt was being dealt with. This gives banks the option to lend more later on.

The S&P 500 took a significant drop at the beginning of the pandemic, losing approximately 1,000 points in March, dropping from around 3,000 points at the beginning of March. As the bailouts were given to companies, there was a significant increase in the stock market that trended upward until June. These bailouts mitigated investors' negative expectations and allowed for a temporary rise in stock prices despite companies' inability to produce.²¹ Bond prices saw a similar trend, dropping around 300 points in March, then rising through June.²² The mainstream

²¹ S&P 500, FED. RES. ECON. DATA (Apr. 20, 2020), <https://fred.stlouisfed.org/series/SP500>.

²² ICE BofA US High Yield Index Total Return Index Value, FED. RES. ECON. DATA (Nov. 26, 2020), <https://fred.stlouisfed.org/series/BAMLHYH0A0HYM-2TRIV>.

analysis of this data is that the faith in the government's ability to pay back bonds was restored quickly. These indicators also show that the government bailouts and subsidized rent payments allowed businesses to survive while not being productive. The short-term problem is in what inflation is doing to the rest of the economy and its resource allocation. However, the financial market seems to give a clear indication of the consumers' preferences. There were significant stock and bond price increases after the stimulus was distributed. This came from the understanding that individuals also have a propensity to save in the face of uncertainty. Rather than spending all their money in the open market, many chose to invest it or save it. This saving will be part of the increase in bank reserves by over a trillion dollars, as shown by the data from the St. Louis Fed in the discussion of debt payments.²³ These options can provide a better understanding of what

²³ Excess Reserves of Depository Institutions, FED. RES. ECON. DATA (Sep. 10, 2020), <https://fred.stlouisfed.org/series/EXCSRESNS>.

these preferences are.

Another factor influencing individual's decisions was the interest rates during March that were artificially pushed down to zero. The rates for stocks and bonds continued upward as the stimulus was distributed. The artificially lowered interest rate disincentivized saving. This is shown in the Austrian understanding of the business cycle when the Federal Reserve inflates again during the bust phase. If this inflation achieves its ends, it creates another boom.

Many banks were being helped through the bailouts given to businesses. These banks were able to simply mark that the debts that were owed to them were being paid. Banks also saw their reserves increase exponentially. According to the St. Louis Federal Reserve, the excess reserves of banks from February to April increased from \$1.5 trillion to \$2.9 trillion. This is significant because the bank's excess reserves will allow for greater ability to lend

later in the business cycle after the lockdowns have lifted enough for allocation to occur.²⁴ Robert Murphy also points out that the excess reserves also lend themselves to the possibility that these financial institutions will start buying treasury debt. This is concerning because it will also allow the money to be spent in the economy by the government. This spending will be in the hopes of stimulating the economy to an even greater extent than that of what was previously done.²⁵

IV. A Comparative Case

A. The United States versus Sweden

In studying comparisons that had to do with the COVID-19 pandemic and the effects of an economic shutdown, one country stood out as a good model for comparison with the United States. Sweden had a minimal amount of regulation that was implemented in their

²⁴ Excess Reserves of Depository Institutions, FED. RES. ECON. DATA (Sep. 10, 2020), <https://fred.stlouisfed.org/series/EXCSRESNS>.

²⁵ Robert P. Murphy, Are the Excess Reserves Finally Leaking Out?, MISES INSTITUTE (Apr. 22, 2010), <https://mises.org/wire/are-excess-reserves-finally-leaking-out>.

response to the pandemic. As could be predicted, many pro-interventionist sources have heavily criticized the Swedish government response. However, for this paper, it serves as a great benchmark.

The United States saw significant inflation in the prices of industries not locked down, as discussed earlier. Food prices in U.S. cities increased by 9 points on the CPI from March to June. Those industries that were closed or heavily affected by intervention saw deflation during these months.²⁶ As the theory would indicate, without the closing of the economy, there would not have been such massive price changes in these specific industries.

The Swedish food prices are an excellent example of the consumer preferences being manifested without government intervention limitations. Their price inflation in 2020 was not outside the usual amount from the previous years.²⁷ Actual food prices saw a decrease in comparison

²⁶ Consumer Price Index, *supra* note 18.

²⁷ Consumer Price Index (CPI). STATISTISKA CENTRALBYRÅN (2019),

to both 2019 and 2018. Another interesting point is that the prices of gasoline showed increases in comparison with other years. As stated previously, the United States saw the opposite effect with its price inflation.²⁸ Sweden also saw price inflation in its clothing prices. This was an area of the American economy that was heavily impacted by COVID preventative interventions. The American economy witnessed a drop in clothing prices by 3 points according to the CPI.²⁹ In contrast, the Swedish citizens saw their clothing prices rise around 7 points.³⁰ These are not perfect comparisons, but they show that prices will increase in the open or “essential” sectors of an economy.

A possible criticism might be that since Sweden did not inflate their currency in the way the United States did,

<https://www.scb.se/en/finding-statistics/statistics-by-subject-area/prices-and-consumption/consumer-price-index/consumer-price-index-cpi/>.

28 Inflation Rate Dropped to 0.3 Percent in September 2020, STATISTISKA CENTRALBYRÅN (October 13, 2020), <https://www.scb.se/en/finding-statistics/statistics-by-subject-area/prices-and-consumption/consumer-price-index/consumer-price-index-cpi/pong/statistical-news/consumer-price-index-cpi-september-2020/>.

29 Consumer Price Index, *supra* note 18.

30 Inflation Rate Dropped, *supra* note 28.

but this comparison is irrelevant because inflation impacts the way consumers act. Although this is true, the point of the comparison is to show that despite the inflationary monetary policy, when an economy is closed down, people’s ability to express their preferences is dulled. This comparison also helped further illustrate that there were lines of price inflation in those industries that could remain open during the mandatory shutdown in the United States. Those same industries in Sweden saw opposite results. The best critique of this comparison is that Swedish and American people’s preferences are too dissimilar for any comparison to be made. However, the food market could be an accurate measurement because all humans have a large preference for food and other life-sustaining commodities.

B. Florida versus New York

Within the United States, there were varying degrees of economic shutdowns. The state of Florida had almost no shutdowns, even during the pandemic’s peak. In contrast,

New York had significant shutdowns, and New York City itself was one of the most heavily intervened in areas in the country. Theory tells us that in states with significant lockdowns, the industries that remain open will see price inflation but no asset price inflation. This is due to the inability to purchase capital goods and services during this shutdown. Understanding the business cycle tells us that there will be significant asset price inflation if there is no shutdown, and the market is operating normally. Does the data of these two states support this?

To answer this question, the housing prices for the City of Tampa and New York City must be examined. Housing prices are useful for determining asset price inflation because they are immovable assets and land prices contribute to their value. Land is an original factor of production, and therefore its increase in value is indicative of what asset prices are. The increase in land prices gives light to the extent to which the new money is causing asset

price inflation. Housing prices for New York City saw almost no change during March, April, May, and June. They did not even vary a point on the CPI.³¹ However, after this, when the city began to reopen in June, there was a significant spike in these prices that has continued into October. From March until October the prices moved from 203 to 215 on their index value. The previous year only saw approximately a one-point increase.³² The City of Tampa saw a rise of 3 points during this time.³³ This is a significant difference in comparing these two cities, and the previous trends before any shutdowns were enforced. It confirms that the shutdown economies did not experience asset price inflation until they were reopened and allowed to continue with their business.

This means that after the closed industries are opened, there is bidding for production factors that will

31 Case Shiller Home Price Index 2020, STATISTA (November 5, 2020).

32 *Id.*

33 *Id.*

allow for inflation to spread throughout the production structure. This causes the asset price inflation that is theorized about by Austrian economists during the boom phase of the business cycle.

V. Regime Uncertainty

A. Application to COVID Interventions

It is no secret that government intervention exercised during this year has been completely unprecedented in this country's history. In a new and unique way, it has been called into question whether there is a constitutional right to work. Parties have taken to the courts to stop the forced closure of economic activity. There is no way to tell exactly what is going to happen in any of these court cases. Shutdowns of the economy changed many of the incentive structures businesses had. There are many cases of small businesses that were not able to sustain the closure and had to go out of business. On the other hand, many of the marginal firms that were on the brink of having

to close were able to receive financial support from the CARES Act and remain open. This again changed how the entrepreneur is incentivized.

As Higgs has shown earlier, when government intervenes in unprecedented ways, it creates much uncertainty for the entrepreneur. There is now the question of if and when this power will be used again. Entrepreneurs can have their entire business closed if the government deems it necessary. This makes reinvestment into their business significantly more costly than it was before. This means that they are much more likely to want to save their money. It could even result in a shift into industries that were deemed "essential" to minimize the cost of uncertainty. There are extreme similarities between the uncertainty of the Great Depression of the 1930s and the uncertainty faced now due to the massive government interference hindering many capitalists' ability to reap the profits from their business endeavors. The theory of

regime uncertainty indicates that entrepreneurs will not be investing back into their companies due to the heightened ambiguity surrounding the possible future returns.

B. Court Cases

After months of suffering from the results of a strict shutdown, the Michigan Supreme Court has ruled that their statewide lockdown was unconstitutional. During the time that preceded this ruling, there was extreme uncertainty about whether the government would allow many industries to reopen. This court decision should finally bring peace into the minds of the entrepreneur. However, the state's citizens once again run into the problem that the government has no restrictions to make it keep its word. The governor declared a brand-new set of restrictions only a month after this ruling that will again significantly affect businesses. The newest edict states that almost all businesses must function at 30% capacity. It also closed many indoor facilities that were not deemed

essential.

In the mind of the entrepreneur, this calls into question if the constitution is a reasonable restraint on the government. This raises uncertainty again for entrepreneurs. In many states, it seems that there is no safety from governmental intervention until this pandemic is over. Even after the pandemic is finished, the question will remain as to whether the government will use this power again for the next problem that it deems to be a crisis.

C. Great Depression, WWII, and the Pandemic

As Higgs writes on regime uncertainty, he illustrates that there are costs to the threat of imposition. Higgs claims that the lack of private investment was the cause of the length of the Great Depression. He also demonstrates that government imposition and spending cannot compensate for private investment. Standards of living are significantly lower when there is a significant

lack of private investment. And, as he points out, in World War II, even when the GDP increased, it did not reflect the standard of living or private investment. However, he is the first person to make the causal link that government intervention exacerbates the dearth of private investment. In the aftermath of the lockdowns, there will be severe uncertainty about government interventions and their use. As business cycle theory has told us, there will soon be a bust and reallocation since there have been massive amounts of inflation. However, if there is still such unprecedented uncertainty in entrepreneurs' minds, this may result in a situation where there is a long period in which there is little to no private investment.

D. Harm to Economic Calculation

To pair with the general uncertainty regarding intervention, there is also significant dilution of economic calculation. Industries that might earn profits during the shutdown will be unsure whether this is the actual

manifestation of preferences. Industries that suffered heavy losses will also be unsure what the actual demand for their product is. The firms that would have been profitable but were shut down are also at a disadvantage because they have less money to bid for scarce resources. The firms that remained open also had the advantage of the Cantillon Effect. Their money's purchasing power was significantly higher than those who receive the money last or not at all. There is also the concern that since the money supply was inflated it is now unclear how much people's savings are worth. The conclusion of all this will result in a dramatic increase in the uncertainty all people within society face.

E. The Tension

Many recognize that there seems to be a tension between applying the business cycle theory regarding asset price inflation advanced in this paper and the theory of regime uncertainty. Asset price inflation relies on the notion that entrepreneurs will reinvest in their businesses

with the new money created in inflation. However, both are merely examples of the incentives that entrepreneurs are currently facing. The fact that the inflation in consumer prices has not increased to the scale of the stimulus is a sign that there is heightened uncertainty in the mind of the entrepreneur. Even in areas where the state had minimal intervention, asset prices did not rise to scale with the stimulus, even though they did rise. The point of this is that there are two incentives to do different things with one's money. It is likely that some will choose to reinvest in their company with the inflationary money that they received as income, and those who are more cautious will not reinvest in their endeavors. Which incentive is stronger, however, depends on how one chooses to interpret the data.

VI. Conclusion

The shutdown of the economy and severe monetary intervention which occurred during the COVID pandemic has not been seen before in American history. As the

pandemic has continued, unemployment has skyrocketed and so has the welfare state in taking over the support of the unemployed. Although inflation has had its typical effects in the short run during a boom, there is still an apparent manifestation of the business cycle. This business cycle is incredibly unique for this very reason.

The Consumer Price Index tells us that some regions of the economy experienced inflation. Such inflation, however, was not to the scale of the stimulus. This is due to society's preference to save and the lack of possible exchange created by the shutdown. The lines of production that saw this inflation will have a reallocation that occurs during the reopening of closed sectors of the market, during which time consumer demands will be able to be better expressed. The resulting inflation of the CARES Act will then be able to fully circulate through the economy. Typical price inflation and the continuation of the boom phase of the business cycle will be seen until it

reaches its crisis. The uncertainty of institutional change will be expressed in the reinvestment by entrepreneurs into their endeavors. It is also currently being expressed by the increased savings that Americans are participating in to better adapt for future uncertainty.