

MANDATE FOR CHANGE



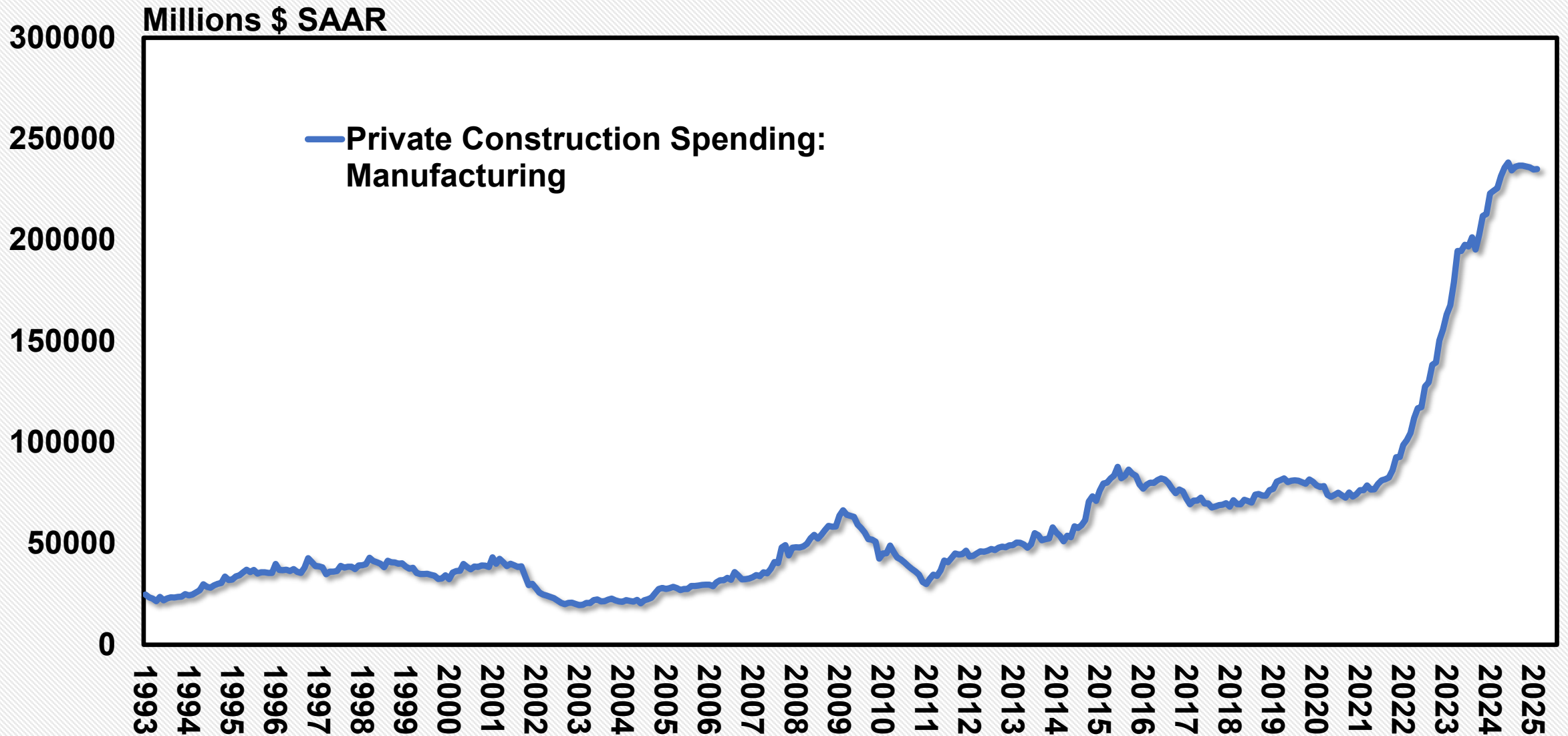
Bryce Gill
Economist
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 **First Trust**



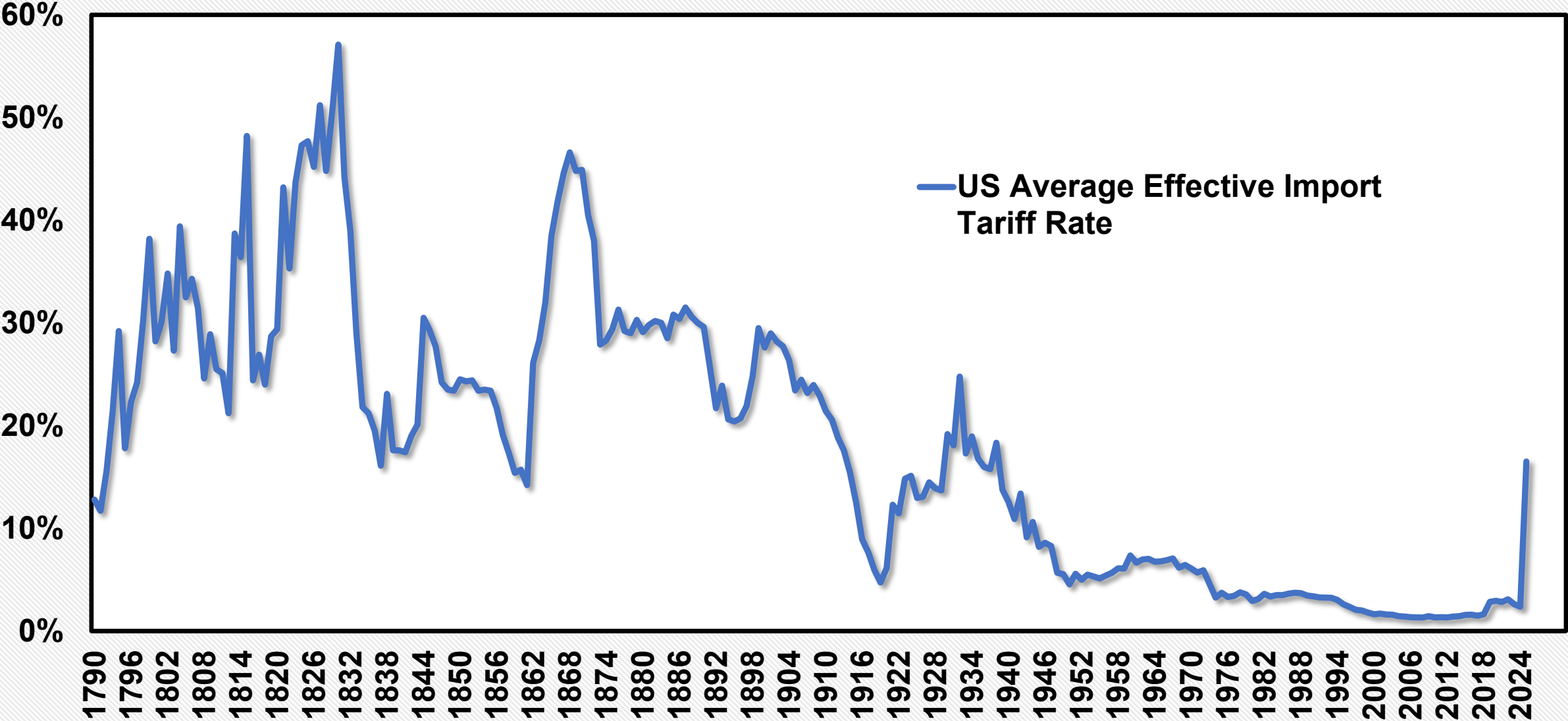
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The Reshoring Boom



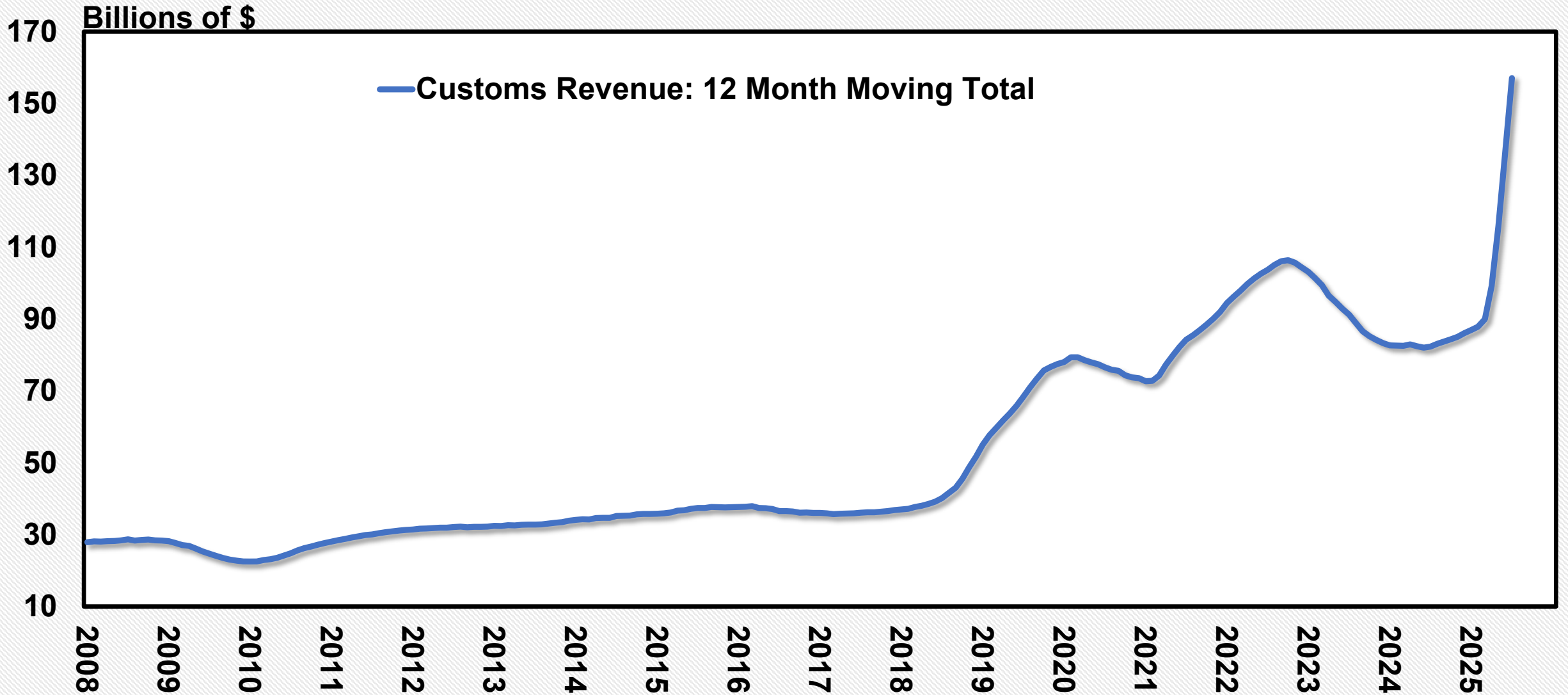
Source: US Census Bureau, Monthly Data Jan 1993 - Feb 2025

The History of Tariff Rates



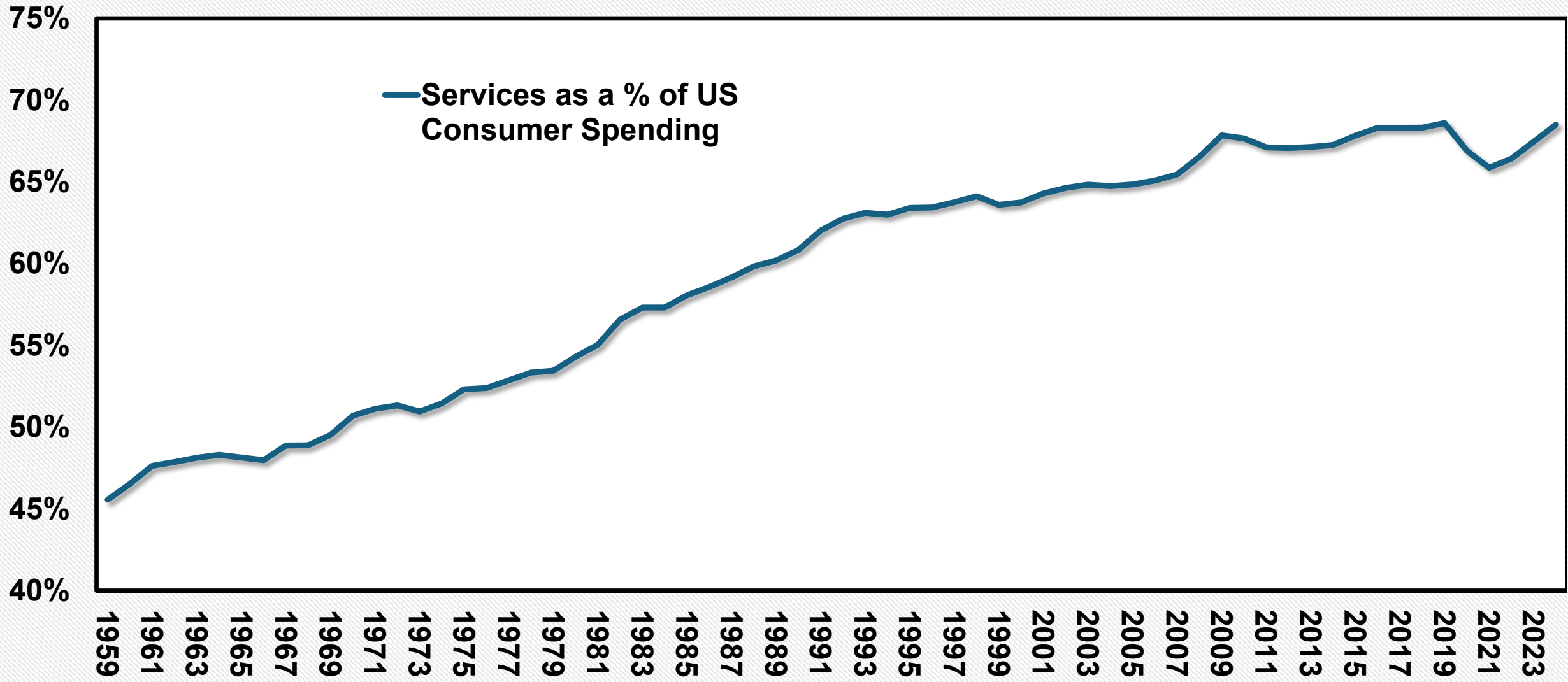
Source: Douglas Irwin/NBER: 1790-1837, Historical Statistics of the US: 1838-1900, US Treasury/US Customs: Data 1901-2022, Tax Foundation: 2025 Estimate

Tariff Revenue Surging



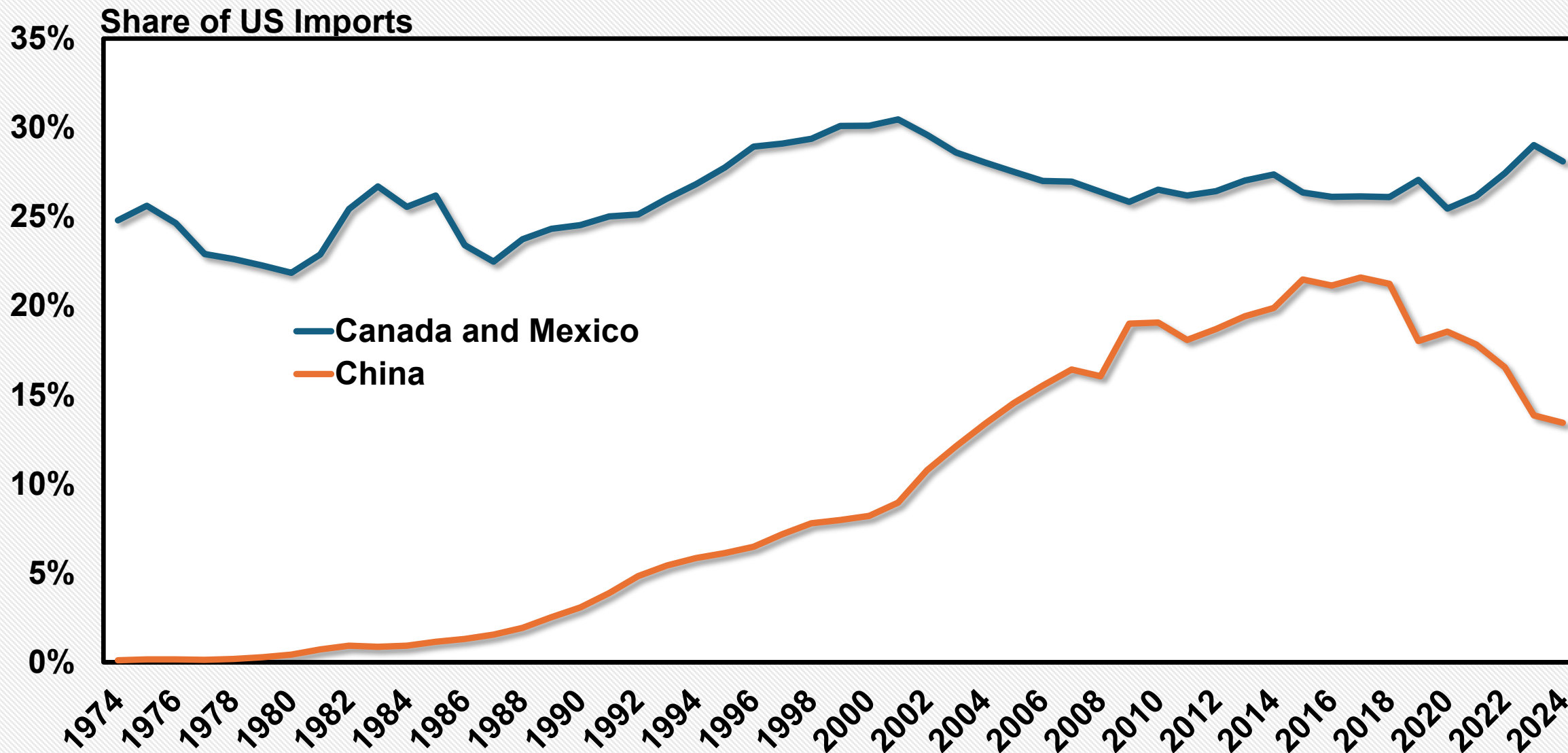
Source: US Treasury, Monthly Data Jan 2008-Jul 2025

US Economy is Mostly Domestic



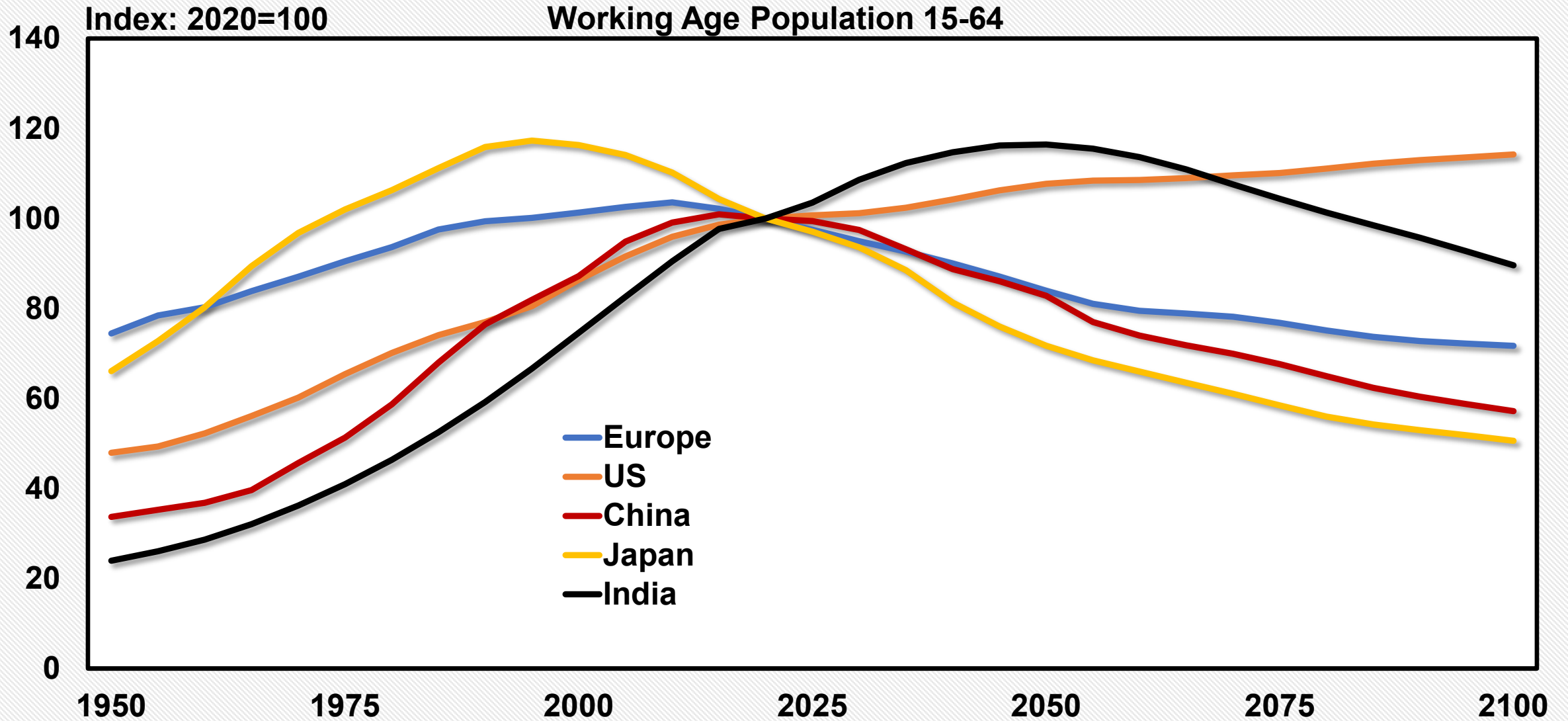
Source: Bureau of Economic Analysis, Annual Data 1959-2024

Large Amount of Trade Exempt from Tariffs



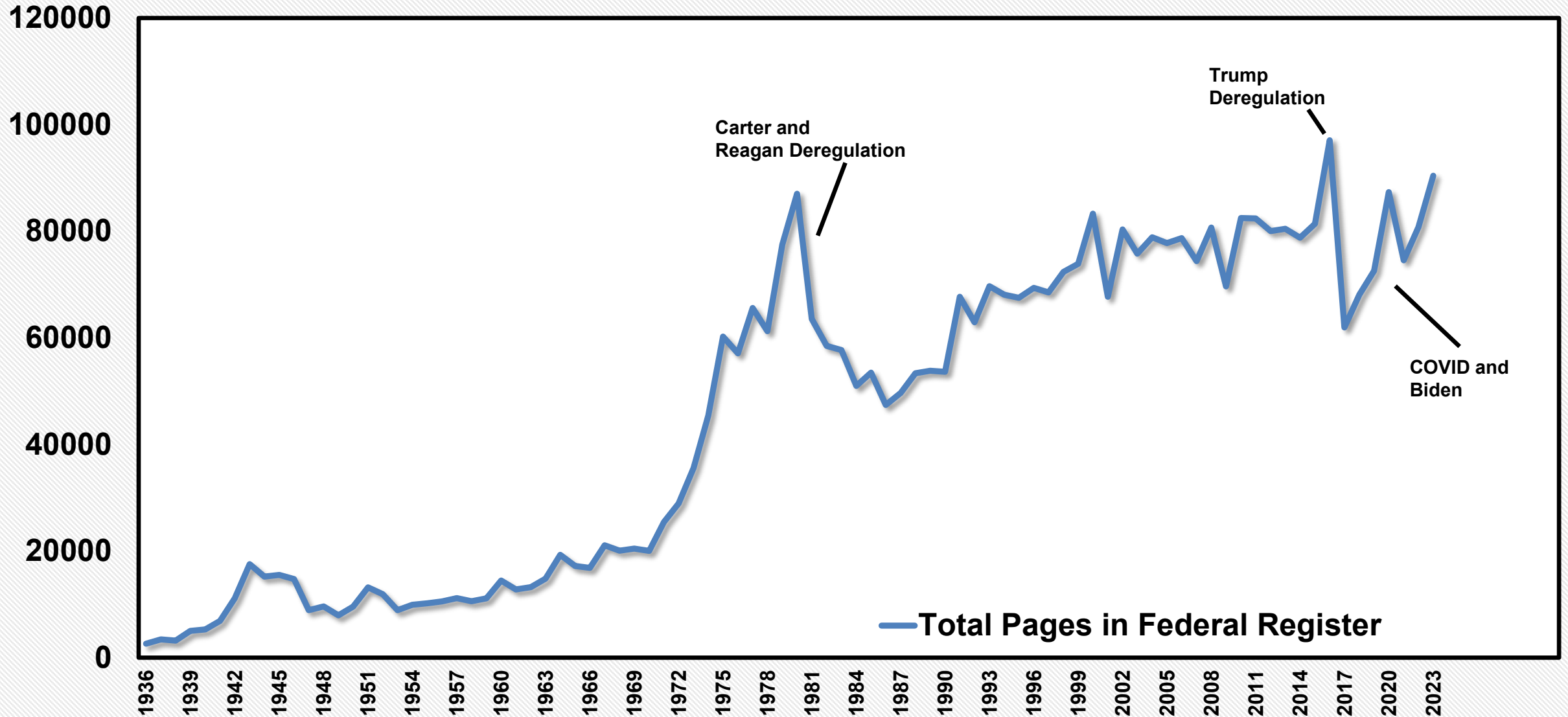
Source: US Census Bureau, Annual Data 1974-2024

The Big Picture



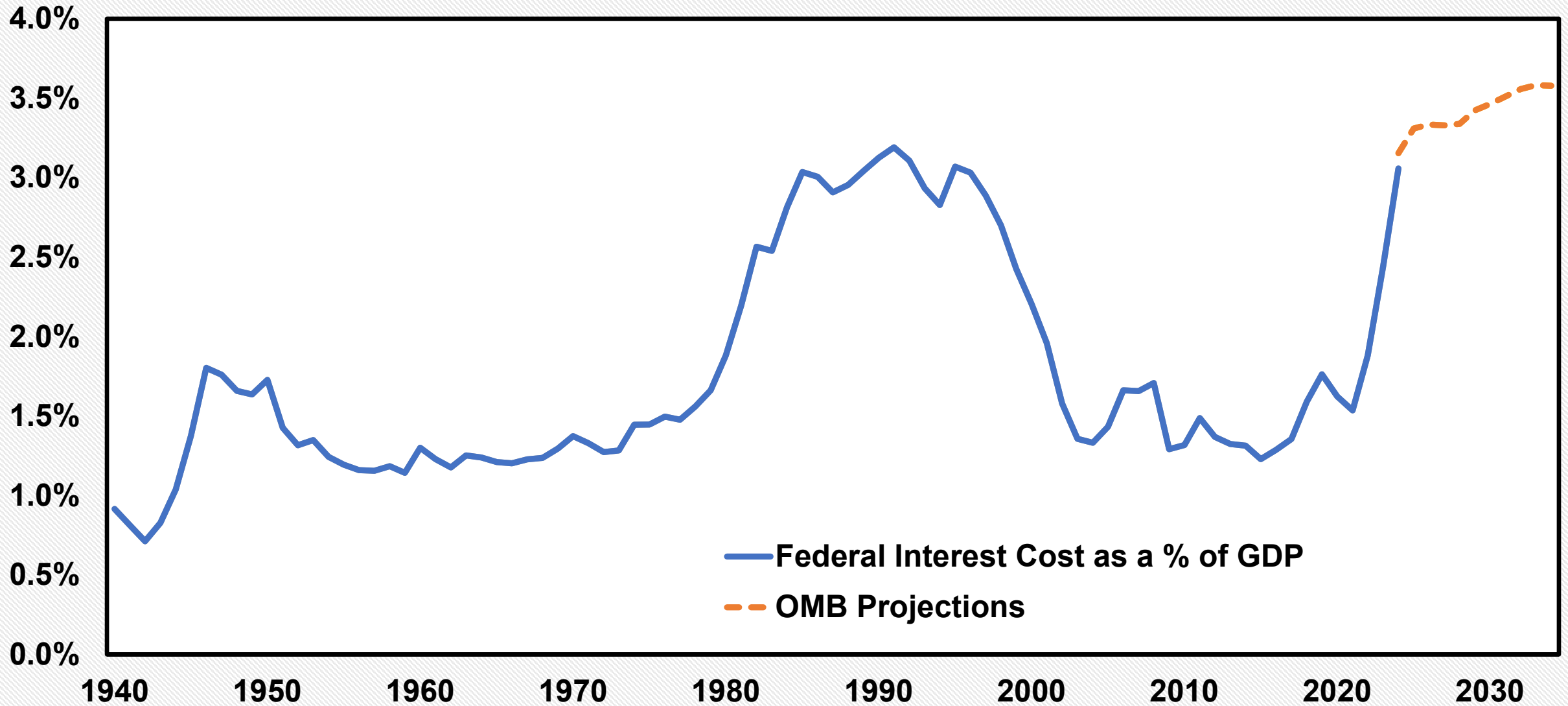
Source: United Nations, Annual Data 1950-2100

US Regulatory Burden



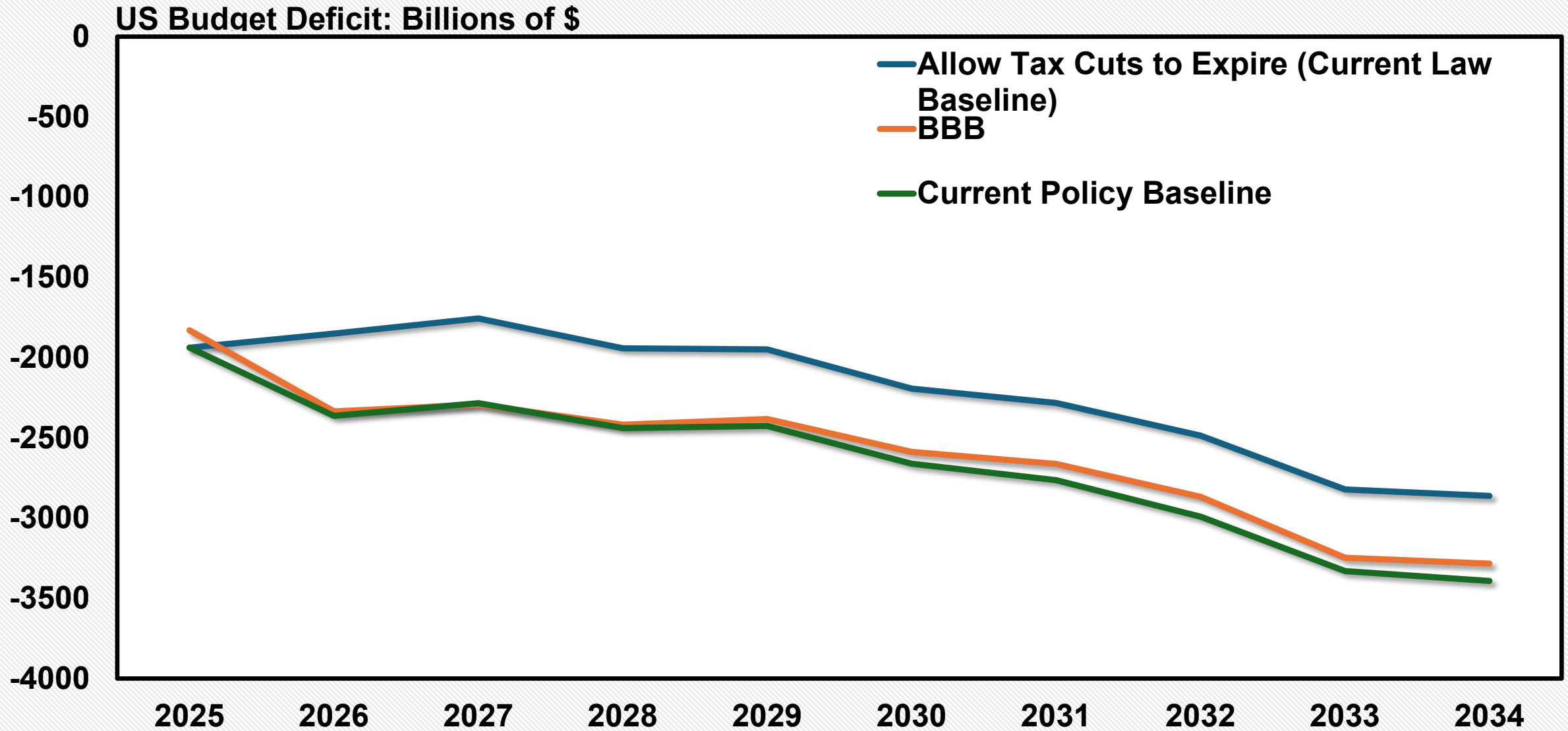
Source: Office of the Federal Register, First Trust Advisors, Annual Data 1936-2023

Interest Costs are the Highest in US History



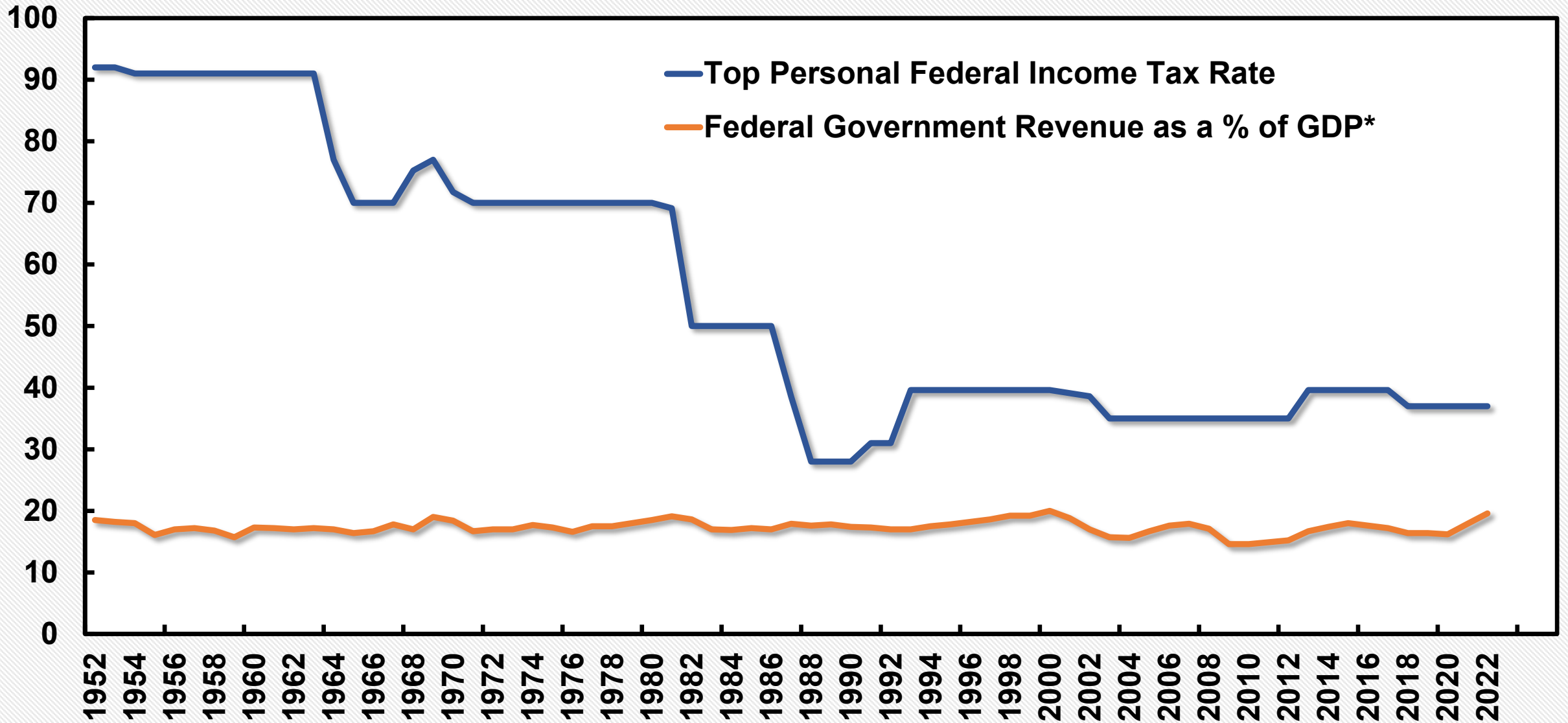
Source: Office of Management and Budget, Annual Data 1940-2024 (Projections 2025-2034)

Tale of Three Deficits



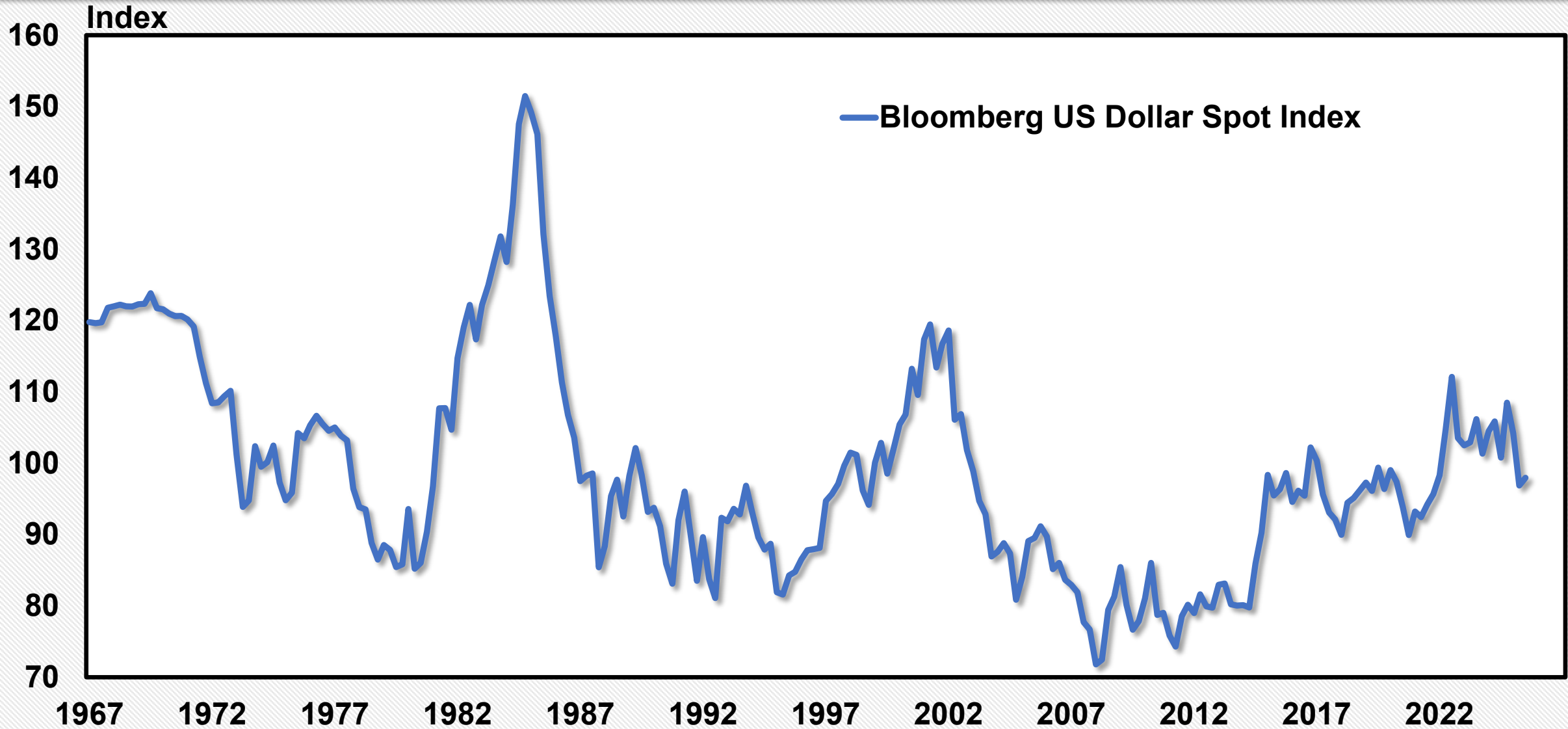
Source: Congressional Budget Office, TaxFoundation.org, Author's Calculations, All Conventional Scoring

Higher Taxes Won't Fix US Budget Problems



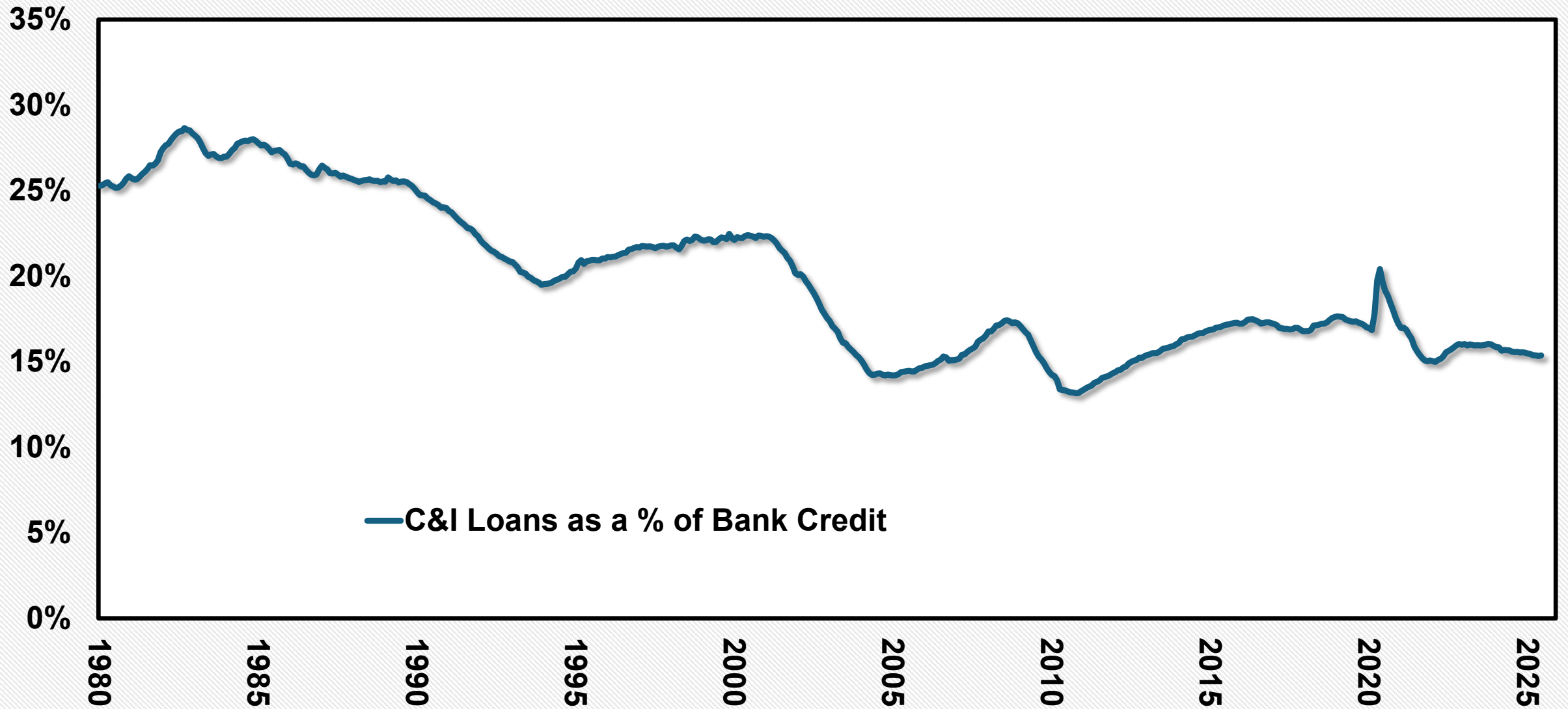
Source: Office of Management and Budget, Annual Data 1952-2022

US Dollar Isn't Dead



Source: Bloomberg, Quarterly Data: Q1 1967- Q3 2025

Industrial Investment Still Chronically Low



Source: Federal Reserve Board: Monthly data Jan 1980-Jun 2025

Inflation, Tariffs, and the Fed

The Federal Reserve made it clear on Wednesday that it's not about to cut short-term interest rates again anytime soon, which is good news if you'd like to see the Fed live up to its goal of bringing inflation down to 2.0%.

After all, progress toward that 2.0% goal has stalled. PCE prices, the Fed's favorite measure of inflation, increased 2.6% in 2024, barely better than the 2.7% climb in the twelve months ending December 2023. Core prices, which exclude food and energy, climbed 2.8% last year, slightly above overall inflation.

Meanwhile, SuperCore prices, which exclude food and energy, but also all other goods and housing rents, rose 3.5% in 2024 versus a 3.4% climb in the year ending in December 2023. That's right...SuperCore inflation was worse in 2024 than in 2023!

We like to pay attention to this measure not because we think it's a great inflation measure but because a few years ago *the Fed* was telling investors and the general public to watch it, but then mysteriously stopped talking about it when SuperCore stopped telling the story of rapid inflation reduction the Fed wanted to tell.

Now tariffs are coming, with the Trump Administration raising them on imports from Canada, Mexico, and China. Each of these countries is saying some retaliatory tariffs are likely on

the way, as well. How this will affect inflation, however, is often misunderstood.

Yes, tariffs will put upward pressure on prices for any items being tariffed. But ultimately inflation is a monetary phenomenon and as long as the new tariffs are not accompanied by a looser monetary policy – and it doesn't look like they will be – then higher prices for those products means consumers have less money to spend on other goods and services, putting offsetting downward pressure elsewhere.

In the meantime, expect the Fed to use the tariffs as a reason to hold the line on short-term interest rates. Especially with the press focusing on the prices that do go up because of those tariffs.

The Fed is probably happy that it has something else to blame for inflation and will be less reactive to incoming data than it normally is. Keep this in mind when you see the onslaught of economic reports over the next two weeks, including employment, retail sales, industrial production, and inflation.

If, as we expect, economic data begin to show signs of a slowdown, the Fed (and the market) will not immediately price in rate cuts. On the other hand, if the Fed does react to a slowdown in the economy and starts to increase the money supply too much, then stagflation becomes a problem. Either way, the equity market faces some serious headwinds. The era of easy everything is coming to an end.

Date/Time (CST)	U.S. Economic Data	Consensus	First Trust	Actual	Previous
2-3 / 9:00 am	ISM Index – Jan	50.0	49.7	50.9	49.2
9:00 am	Construction Spending – Dec	+0.2%	+0.5%	+0.5%	0.0%
afternoon	Total Car/Truck Sales – Jan	16.0 Mil	16.0 Mil		16.8 Mil
afternoon	Domestic Car/Truck Sales – Jan	12.2 Mil	12.3 Mil		12.9 Mil
2-4 / 9:00 am	Factory Order – Dec	-0.7%	-1.1%		-0.4%
2-5 / 7:30 am	Int'l Trade Balance – Dec	-\$96.8 Bil	-\$97.4		-\$78.2 Bil
9:00 am	ISM Non Mfg Index – Jan	54.1	54.4		54.0
2-6 / 7:30 am	Initial Claims – Feb 1	213K	210K		207K
7:30 am	Q4 Non-Farm Productivity	+1.4%	+1.8%		+2.2%
7:30 am	Q4 Unit Labor Costs	+3.4%	+3.6%		+0.8%
2-7 / 7:30 am	Non-Farm Payrolls - Jan	170K	165K		256K
7:30 am	Private Payrolls – Jan	141K	140K		223K
7:30 am	Manufacturing Payrolls – Jan	-2K	-10K		-13K
7:30 am	Unemployment Rate – Jan	4.1%	4.1%		4.1%
7:30 am	Average Hourly Earnings – Jan	+0.3%	+0.3%		+0.3%
7:30 am	Average Weekly Hours – Jan	34.3	34.3		34.3
2:00 pm	Consumer Credit – Dec	\$14.5 Bil	\$7.2 Bil		-\$7.5 Bil

Consensus forecasts come from Bloomberg. This report was prepared by First Trust Advisors L.P., and reflects the current opinion of the authors. It is based upon sources and data believed to be accurate and reliable. Opinions and forward-looking statements expressed are subject to change without notice. This information does not constitute a solicitation or an offer to buy or sell any security.

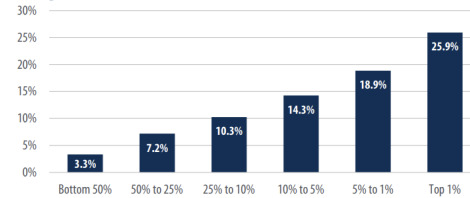
THREE ON THURSDAY

FIRST TRUST ECONOMICS

Are the Wealthy Paying their Fair Share?

With the Presidential Election fast approaching, conversations about the wealthy not paying their "fair share" of taxes have become more frequent. Figures like Warren Buffett are often cited, with examples showing he pays a lower tax rate than many of his office colleagues. For some, this serves as proof of a tax system that isn't progressive enough. But what do the actual data tell us? Are the wealthy really contributing less than their fair share, as some claim? And did the 2017 tax cuts only benefit the rich? In this week's edition of "Three on Thursday," we delve into the most recent IRS tax data from 2021 to provide a clearer picture of the federal income tax landscape. To offer further insight, we've included three detailed charts below.

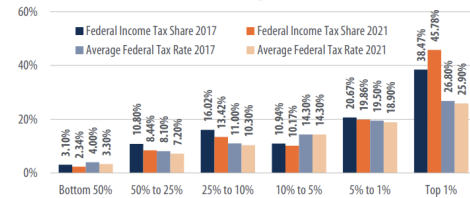
Average Federal Income Tax Rates



Source: IRS, First Trust Advisors. Data for 2021 (latest).

The latest IRS data from 2021 highlights the strongly progressive nature of the federal income tax system. Taxpayers in the top 1% (with an adjusted gross income of \$682,577 or more) paid an average tax rate of 25.9%. In contrast, those in the bottom 50% (earning \$46,637 or less) had an average tax rate of just 3.3%. This significant difference shows that the top 1% pay an average federal income tax rate that's over eight times higher than the bottom half of all taxpayers.

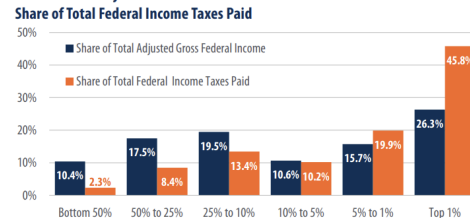
Total Federal Income Tax Share and Average Federal Tax Rates (2017 vs. 2021)



Source: IRS, First Trust Advisors. Data for 2017 and 2021.

The 2017 Tax Cuts and Jobs Act (TCJA), often called "the Trump tax cuts," reduced tax rates, widened tax brackets, increased the standard deduction, and expanded the child tax credit. But did these changes primarily benefit the wealthy? Not exactly. In fact, the TCJA lowered tax burdens on average across all income levels. By 2021, average federal tax rates were lower for every income group compared to 2017. However, the top 1% saw their share of total federal income taxes paid rise significantly, from 38.5% in 2017 to 45.8% in 2021. Conversely, the bottom 50% saw their share of federal income taxes fall, dropping from 3.1% in 2017 to 2.3% in 2021.

Share of Total Adjusted Gross Federal Income vs. Share of Total Federal Income Taxes Paid



Source: IRS, First Trust Advisors. Data for 2021 (latest).

The top 1%, representing 1.54 million federal income tax returns in 2021, earned 26.3% of total adjusted gross income but shouldered a striking 45.8% of the overall federal income tax burden. In contrast, the bottom 50%, with nearly 77 million tax returns, earned 10.4% of total adjusted gross income and carried only 2.3% of the federal tax burden. Remarkably, the bottom 98% of taxpayers—approximately 150.5 million returns—earned 68.1% of adjusted gross income in 2021 yet contributed just 46.2% of total federal income taxes, a share only slightly higher than that of the top 1%.

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