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THE RISE AND FALL OF FULL EMPLOYMENT

Part VI: Planning Against Mass Depression

by Bertram Gross

"What is it that converted capitalism from the cataclysmic failure which it appeared to be in the 1930s into the great engine of prosperity of the post-war Western world."

—Andrew Shonfield, *Modern Capitalism*

Since 1965, when Shonfield asked this question in his extremely influential book, "the great engine of prosperity" has never stopped running. Despite predictions of inevitable capitalist collapse, no nation of the Western World has been a "cataclysmic failure." A *New York Times* journalist was even obliged to invent the word "recession" to describe the moderate downturns of a tamed business cycle. And every recession has thus far been followed by an upturn. This record is as striking as the related fact that over 40 years have now passed without global warfare—whereas the second world war followed the first in only 21 years.

From War to War

Shonfield thought that the outstanding feature of the new success of capitalism in the post-war Western world was the vastly increased influence of the public authorities in the management of economic systems. France, Germany, Britain, Italy, and Holland succeeded in varying degrees to plan and promote innovation, trade expansion, higher real per capita income, a steady advance in social welfare programs, and greater intellectual coherence in business planning. But Shonfield neglected to emphasize the vital U.S. role in Europe's miraculous reconstruction.

The U.S. economy not only absorbed the millions of returning servicemen sooner than anyone expected, but also achieved Roosevelt's "fantastic" goal of 60 million civilian jobs by 1952, the last year of the Truman administration. It was this success that enabled the U.S. to provide both the aid and the trade on which European planners relied—in the Marshall plan and NATO, and in the availability of U.S. markets for rebuilt European industries.

Successful U.S. reconversion derived from much more than new planning approaches and the Employment Act of 1946. More immediate reasons included tax measures allowing corporations to pile up reconversion reserves, the contract settlement and surplus property acts, and the work of the Office of War Manpower and Reconversion. The huge backlog of consumer demand that had piled up during the war was a crucial factor, as was subsidized college education through the G.I. Bill of Rights. Then came low interest mortgages, particularly for veterans, and huge road and sewage and hospital construction programs that subsidized the enormous expansion of suburban areas. From the very beginning of the post-war era, American economic might and policy leadership played a leading role in shaping the monetary and trading systems of the free world.

American economic might, of course, was not independent from military might. The "military wherewithal" supplied by American cold war policies was decisive in repelling socialist and communist threats and building the multi-continental markets of the free world. With the Korean war, the huge expansion of U.S. military spending stimulated growth in Japan and in Europe and the U.S. as well. While this growth slowed somewhat during the Eisenhower years (1953-1960), it picked up under President Kennedy and zoomed higher with President Johnson's intervention in Vietnam.

During the Kennedy-Johnson period (1961-1968), both presidents resorted to deficit spending as an economic stimulus and also as a way of following the recent reconversion from war to peace with a partial conversion back to huge military spending. Kennedy did it through tax cuts. Johnson did it by using debt in-

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stead of taxes to finance the combination of military expansion and the welfare state programs of the "Great Society."

In the eight years of the Reagan Administration, the process of military expansion went still further, but not with old-fashioned forms of military power. The build-up of military forces was based instead on (1) enormous amounts of nuclear "overkill" and (2) more expensive, ultra-technical and unconventional "electronic battlefield" forces (sometimes mislabelled "conventional" forces) scattered all over the world. In part, this was done by cutbacks in so-called "social expenditures" and increases in consumer and business debt. In larger part, it was done through the "military Keynesianism" (now labelled "supply side economics") that provided war contractors with an abundant supply of profitable deals, and millions of people with jobs, and the nation with the greatest federal deficits in peacetime history.

The Discrete Wisdom of Advisers

From its inception, the Council of Economic Advisers (CEA) played an increasingly important role in all these developments. It had the advantage at the outset of a diverse membership, chosen by President Truman through a seven-month process of push-and-pull pressure and lobbying. The process resulted in the appointment of Edwin G. Nourse, a "conservative" economist from the Brookings Institute, as the CEA's first chairperson.

In 1933, Brookings had published two books by Nourse, with the main conclusion that in 1929, the peak of America's previous prosperity, industry was capable of producing 19% more, while 19% of the country's "labor supply" was unemployed. A basic reason, Nourse concluded, was the fact that wage-price-profit relationships undermined the purchasing power needed for a fuller use of capacity. After the Employment Act became law, I suggested Nourse's name to Senator James Murray, who then took a strong stand for him (and opposed the nomination of Winfield Riefler, who was then with the Federal Reserve Board).

The CEA's first Vice-Chair was Leon Keyserling, the very active government lawyer vigorously supported by Senator Robert Wagner (as well as Senator Murray) and by organized labor. Once Keyserling entered office, he and I worked closely together in recruiting an exceptionally able staff, mainly of economists with years of practical government experience. With the backing of the entire staff, Keyserling worked effectively with Clark Clifford, Truman's White House aide, to update the unfinished New Deal Agenda under the new label of Fair Deal.

The third member of the original CEA was John D. Clark, a business school dean who believed firmly in actions to control the concentration of economic power. His main supporter was Senator Jeremiah O'Mahoney, a middle of the road advocate of the original Full Employment Bill, and a strong advocate of protecting competitive private enterprise through vigorous enforcement of the anti-trust laws.

It was possible for anyone working at the original CEA to know the names of all the major economists in Washington, including those on Congressional committee staffs and in lobbyist organizations. (My secretary also had their phone numbers.) This was not, however, a consequence of the Council's prestige, which was low during its first years. Both Keyserling and Clark openly exhibited their value preferences, in full and clear support of President Truman's policies. They were therefore regarded more as "political operatives" than as truly professional economists. Nourse, in contrast, aimed to make the council a bulwark and a symbol of the presumed wisdom of professional economists. He therefore initiated the practice of bringing to the council a few people from university economics departments; later, more Council and staff members came from economics departments, and fewer came from government departments.

The fact that academics had less practical experience in government did not result in their being "above the fray." Both Council and staff members have invariably been supporters of the general policies of the Presidents they were called on to advise. This is in keeping, let me emphasize, with the basic political premises behind not only the Employment Act of 1946 but also the original Full Employment Bill of 1945.

Some Early Council "Traditions"

Lacking formal credentials as a professional economist, Keyserling reacted self-protectively by quickly abandoning any reference whatsoever to the framework of economic rights on which the Employment Act was originally based. On this subject he adopted the protective coloration of "objective economic analysis." A tradition was thus established that has consistently been followed by all subsequent Councils.

As Assistant to the original Chairman Nourse, and as Executive Secretary after his resignation, I worked closely with Keyserling to have the Council facilitate a vast expansion in economic statistics. On the basis of my earlier use of statistics to support the original Full Employment Bill, our staff developed the Statistical Appendices of the annual Economic Reports, and later the Council's monthly *Economic Indicators* (formalized by a Joint Resolution I worked out with a staff member of the Joint Economic Committee). Both of these soon became widely used and admired even by our critics.

At no time did we dare to enter the hornets' nest of procedures involved in estimating unemployment. In fact, we had a psychological investment in the existing official unemployment statistics, which became the basis for our estimates of the additional GNP that could be gained by putting the unemployed to work. Nourse himself quickly abandoned the concepts that led to his finding 19% joblessness back in 1929, and adjusted completely to the concept of full employment as a percentage of the "labor force." (I will discuss in more detail both the labor force concept and the unemployment estimates in the next article in this series.)

Also in our first year, the Council vigorously nudged the Commerce Department into adjusting estimates of GNP to correct for price changes (as well as presenting the estimates in current prices). This made it possible for us and others to set forth goals in constant dollars—especially the goal of the "needed level" of GNP. With this concept in hand, the Council popularized the so-called "full employment budget," and went on to articulate, under President Truman, the historic leap from stability to growth as a public policy goal.

The Growth Concept and the Military Establishment

Early in 1950 it became clear that growthmanship goals could be used to support major increases in military spending. I remember when the first draft of National Security Council Document 68 came across my desk, with an eloquent if not frenetic call for stronger military forces to counter Soviet threats. With many other conservatives of that day, Edwin Nourse had serious reservations. The one he expressed most openly was that a new arms race would bleed the U.S. economy.

Leon Keyserling argued that by reaching full employment goals, the U.S. would be rich enough to have "guns and butter" both. By the time North Korea invaded South Korea in June 1950, Keyserling had won the argument. Soon after, Nourse resigned and Keyserling became Acting Chairman. But it was only after many months of internal fighting that President Truman waved aside conservative opposition to Keyserling's liberal views and appointed him Chairman.

The Council's commitment to growthmanship then became much stronger. Conservative groups gradually came around to the idea of more military spending. But this did not protect the Council from growing opposition to Truman's Fair Deal proposals for moderate expansions in social programs, which Keyserling had helped to develop and the Council had justified. As Executive Secretary, I had to make the most strenuous efforts imaginable to win support for the Council's budget from the conservative majority on the House Appropriations Committee.

Even after the Truman administration ended and Keyserling was gone, the animosity toward him lingered on. The House Appropriations Committee came close to denying funds for the Council and casting it into the same limbo to which the National Resources Planning Board had been consigned 10 years earlier. Appropriations were assured only after President Eisenhower consigned the Council into "safe and sane" hands. As a result of this experience (as well as the personal convictions of most members), the CEA over the years has made a habit of "playing it safe" rather than attempting to "make waves" with new thinking.

In Eisenhower's second term, the Gaither Committee, a group of eminent Republicans, adopted growthmanship as the basis for arguing that the economy was big enough to afford a large increase in military spending (including a huge fallout shelter program). Eisenhower rejected the military spending proposals, and warned the country not to become "a garrison state." But the growthmanship concept survived, and became more legitimate at higher levels of the Establishment.

By the 1960s, growth (with stability) was "in." GNP goals became a staple in political discourse. The "full employment" budget entered the government's definitions of budgetary terms. But growthmanship was still attacked by conservatives, who thought it permitted too much presidential power in peacetime; it was also ignored by university economists, who had no part in its development. Eventually, university economists included these ideas in their college textbooks, but without recognition of the Council's role in their origin and development.

The Explosive 1960s—And Since

Growthmanship slowly spread in the 1960's decade to France and Britain, where counter-cyclical stabilization was ridiculed as "Le Stop Go" or "upsey-downsey." Targets for annual rates of GNP growth guided economic policy-making in most of this decade in Western Europe and Japan, helping capitalist regimes adjust to pressure from socialist and labor parties that continued their historic role of trying to reform capitalism. Growth targets also came to be used in development plans in so-called "developing nations." Around the world, economists were subtracting actual GNP from some full employment level of GNP—defined as the total number of people working at full employment times the average GNP per employee. They could thus show how many billions worth of goods and services were lost by slow growth, stagnation, or recession.

Since the 1960s, most U.S. Councils have helped to supplement military and welfare spending with new "incentives" for business—a euphemism for subsidies and tax give-aways benefiting the wealthiest people and corporations. In concert with the Federal Reserve System and the Treasury, the Councils have supported the bolstering of demand through huge increases in consumer and business debt.

As for federal debt, the U.S. Councils have obediently paid lip service to budget balancing, at least in the long run, while relying on federal deficits to counter recessions. But under Presidents Kennedy and Johnson, a major split developed on how to incur the deficits. A minority of liberals like John Kenneth Galbraith sought the stimulative deficit effect through more spending on neglected public amenities. The "realists" like Walter Heller (CEA chairperson) favored the older Republican principle, now enshrined in Keynesian terms, of cutting taxes.

As prices rose and inflation seemed to threaten, both liberals and conservatives deserted the compensatory idea of using a federal surplus as a counter-inflationary force. The Heller Council promptly abandoned the idea when economic expansion first suggested even the possibility of a surplus that might be used for debt reduction. On the well-reasoned ground that the "fiscal drag" of a surplus might trigger recession, the Council invented "revenue sharing" to distribute any impending surplus among the states without raising the specter of more federal programs.

As the Vietnam War escalated, the threat of a deflationary surplus subsided and the idea of revenue sharing was shelved. Inflation was to be stemmed not by a budget surplus but by exhortations, called "jawboning," or by "income policies" designed (with the help of the CEA) to get labor and business cooperation in moderating increases in wages and prices.

Like Truman, President Johnson revived New Deal domestic policies under a new label. Going even further than the Fair Deal, especially on civil rights, Johnson's "Great Society" program won him liberal support, while military expansion won him conservative support. Unlike Truman's Fair Deal, which was stopped in its tracks by conservative Congressional opposition, Johnson's "Great Society" made headway in Congress. But new legislation on medical care, education, housing, and general aid to urban areas cost money.

Federal deficits escalated as both military and civilian spending rose, and fears of inflation replaced fears of deflation. Against advice from the CEA, Johnson stubbornly refused to recommend higher taxes, preferring instead to cut back on domestic reform. By 1968, after huge casualties in Vietnam and devastating riots in Detroit, Newark, and even the nation's capital, the Great Society vision, as an energizing political force and a symbol of high aspiration, was dead. It was the last serious effort to revive and modernize the New Deal.

Nixon, Carter and Reagan Years

Under Nixon's detente with the Soviet Union, defense spending gradually declined, a process that continued during the first years of the Carter administration. As a stimulus to the economy, hopefully helpful at election time, Nixon picked up the old CEA idea of sharing federal revenues with the states—even though no deflationary surplus was in the offing. This was a way to increase federal spending without new federal programs, since the states had the freedom to use these federal funds, for any combination of more spending or less taxes.

After the invasion of Afghanistan and President Carter's break with detente, the Carter administration moved to increase military spending and slow down social programs. Later, President Reagan moved to extend the Carter policies much further. "Supply side" terminology at least temporarily united the Keynesians supporting tax cuts, the Keynesians advocating more federal spending, and the conservatives seeking less spending on social programs.

The Reagan administration's super-Keynesian expansion of federal borrowing and debt ended the deep 1981-1982 recession—but only after an enormous price was exacted in double-digit unemployment resulting from the Federal Reserve Board's high-interest rate monetary policies. With nothing but huge deficits now in the offing, revenue sharing was at first cut and in due course abolished. Social programs in the western European industrial democracies were also subject to new fiscal restraints in the 1980s. But they had previously developed more secure financing and higher overall benefit levels than the programs that were more severely cut in the U.S.

The Reagan deficits and debts and military spending restored slower but more acceptable growth rates, without the inflation that economists had heretofore predicted would come from even mild Keynesian deficits. The keys to this "success"—never previously envisioned either by liberal or conservative Keynesians—lay in (1) a widespread reduction of real wages and loss of workers' job and income security; (2) a huge in-flow of low-priced goods from abroad; and (3) an equally huge in-flow of foreign capital to help finance the enormous increases in federal debt.

The Central Planning Cluster

The Council of Economic Advisors has been effective in its brief, post-World War II history, only to the extent that it has not presumed to monopolize economic advice and guidance, but has functioned instead as one small entity within a much broader and constantly growing central planning cluster. To handle (and get) expanding responsibilities, Presidents have reached out for help from a vastly expanded Office of Management and Budget; a Central Intelligence Agency (to run the President's covert operations as well as collect intelligence); a National Security Council (to help the President coordinate military and foreign policies); a National Security Agency (to listen to the conversations and messages of other governments); and a host of special councils and counsellors in the White House or Executive Office.

From about 100 people under FDR, the institutionalized presidency grew to over 6,000 under Nixon, and still more under Ford, Carter and Reagan. This huge network, according to one observer, is "three times a strong as a marine battle group and not always as disciplined." In addition, every president has a "kitchen cabinet" and other informal links with people of influence, wealth and power. These linkages have made the chief executive network the linchpin of a remarkably resilient establishment that approaches some recent concepts of a corporate state.

With this kind of establishment support, our Presidents have been able to tame every general recession. In so doing, our national government has completed a full circle back to the deficit spending idea removed from the original full employment bill, and has developed super-Keynesian deficit spending policies in the process. But instead of providing an economic substitute for war contracts, which we sought to provide in the original full employment bill, this super-Keynesianism has become the agent for expanding war contracts and promoting the military image of a global superpower. Instead of providing the basis for full employment policies that would permit development of the "economic rights" which FDR sought, this super-Keynesianism has become a basis for planning *against* full employment—a subject for discussion in greater detail in the next article in this series.