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THE RISE AND FALL OF FULL EMPLOYMENT:

Part VII: Containing Full Employment with Conservative Theory

by Bertram Gross • //

Editor's Note: This is the seventh article in Professor Gross's series, which began with LCR 239 in July, 1988. The articles are condensed from the author's forthcoming book on the subject. Professor Gross welcomes comments, criticisms and suggestions from LCR readers, especially on the impact of our employment and unemployment policies on unions and their members.

The National Resources Planning Board's concept of full employment, set forth in 1943, was one of the greatest social inventions of the New Deal era — and also one of the shortest lived. Its chief virtues were its vision of "a Second Bill of Rights"; its inclusion of civil liberties and state and local planning; and its grounding in comprehensive federal policy-making in the context of "a jural world order outlawing imperialism, old or new fashioned." (See LCR 244, Sept. 1988.)

Debasing a Heritage

After the Board's demise, its vision of planning was gradually debased. Roosevelt himself started the process: Concentrating on "economic" rights and federal action, he dropped both civil liberties and state and local planning in announcing his "Second Bill of Rights" (January 1944). Following suit, the drafters, spon-

sors, and supporters of the original Full Employment Bill also focused only on the right to a job opportunity, and excluded explicit mention of other economic rights. They over-emphasized compensatory fiscal policy as the way to assure full employment, and came to exclude anti-trust action from full employment policy. By concentrating on economic advice and projections of foreseeable trends, the Council of Economic Advisers nurtured a growing obsession with numbers magic and technical approaches to problems that have always been moral and political also.

As the trumpet calls sounded for cold war mobilization against the insidious Moscow-Peking axis, the concept of economic planning to permit fulfillment of basic human rights gave way to the World War II mobilization concept of "full" or "maximum" use of national and personal resources and capacities. This concept negated the need for voluntary leisure or, in the words of the Planning Board's original bill of rights, "the right to rest, recreation and adventure; the opportunity to enjoy life and take part in an advancing civilization." The idea of full-time work became frozen in wage-hour legislation at 40 hours a week, beyond which overtime was to be paid. When people suggested staged reductions in officially measured full-time work, the answer was usual, "We need all the output we can get."

An unremitting glorification of rapid growth in GNP thus developed in the 1950s and 1960s. Goals expressed in GNP totals or average GNP per person concealed expanding gaps between the incomes, wealth, and power of the poor and the rich. President Lyndon Johnson responded to this situation by declaring a war on poverty, through which "the quality of the lives of our people" would be more important than the quantity of output. But the Great Society's anti-poverty programs were geared to a "poverty line" minimum of absolute deprivation, an approach which distracted attention from broader considerations of distribution and equity. And the Great Society's output included the expansion of U.S. intervention in Vietnam, with a quantity of deaths that made a mockery of "quality of living" rhetoric. By 1968, therefore, despite the vitality and promise of some continuing programs, the Great Society vision as an energizing force and symbol of high aspiration was dead.

Military Keynesianism

What survived was the political idea of using high and appealing rhetoric to justify total growth, which now lives on in conser-

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vative or military Keynesianism. The simile that “a rising tide raises all boats” — heard often during the Reagan Administration — suggests that rising output will by itself raise poor people from poverty or overcome institutionalized discrimination against women and minorities. Thus the original weakness of the emphasis on full use of resources has been used to justify the largest peace-time expansion in both military forces and federal deficits in our nation’s history.

In the forty year period since the late 1940s, rights to fair wages, social security, welfare, housing, health care, and increasing leisure — and the rights of labor, women, minorities, small business, family farmers, and the disabled — came to be pursued by separate groups, as single issues. Full employment planning and budgeting were gradually replaced by welfare payments that served to pacify the poor, by job training that did little to expand the supply of good jobs, and by job programs offering temporary, low-paid or dead-end jobs to a few people. Politicians and policymakers retreated from the broad full employment policies needed to justify and adequately finance these efforts. The high ground of moral vision was yielded to right-wing demagoguery used to extend the rights of the rich and powerful. As Roosevelt had warned, “rightist reaction” nourished tendencies marked by “the spirit of fascism” here at home.

Deflating or Inflating the Threat of Inflation

Keynesians have traditionally emphasized insufficient demand as the cause of unemployment, and excessive demand as the cause of inflation. At a time when people suffered from either depression or the fear of post-war depression, Keynesians impressed most economists with the importance of using government deficits to raise effective demand, but in the process opened themselves to the charge that they were “soft” on inflation. Their defense rested on the rather naive idea that when inflation loomed, a government surplus could then prevent or counteract it. Unfortunately, in such “surplus” situations the required anti-inflation contraction in government spending would quickly restore fear of large-scale unemployment.

In contrast, many neo-classical economists have gone to a greater extreme by wildly exaggerating the inflationary tendencies of high employment levels. In effect, the governments which have commonly followed their advice have come to regard high unemployment as their chief weapon for exorcising the inflation demon. In the process, they have developed a popular mythology to conjure up the demon.

The Myth that Wages Equal Prices

In 1958, A.W. Phillips, a London economist, developed historical data showing the tendency for wage rates to rise more rapidly when unemployment is low and to fall relatively more slowly when unemployment is high. His impressive statistical evidence supported the Marxian theory on the role of the “reserve army of the unemployed” in preventing wages from squeezing profits.

The Phillips data did not support the contention that higher levels of employment would lead to inflationary price increases. This interpretation came from leading U.S. economists, and it be-

came very popular. Year after year, U.S. students of economics have absorbed a revised “Phillips curve” — with statistical details omitted — making the case that a certain amount of unemployment is “natural” or “non-inflationary,” and must be preserved to combat inflation. The theory is that there must be a “trade-off,” i.e., a choice between (1) high employment with dangerous inflation, or (2) stable prices with unpleasant levels of unemployment.

As a result, the amount of official unemployment regarded as full employment has gradually been raised — from two to three percent of the labor force in the 1950s, to four percent in the early 1960s, to five percent in the 1970s, and to six or seven percent in the 1980s. The Council of Economic Advisers pontificated in 1983 that it would be “imprudent” to reduce the unemployment rate below its “inflation threshold” of six to seven percent. That level, many economists insisted, was the “natural” unemployment rate.

Higher national percentages of unemployment were then justified on the ground of the changing composition of the labor force. For white adult heads of households, unemployment usually remained close to the lower levels of earlier years. The difficulty was that more women, blacks, and young people were entering the labor force. In 1986, when the average rate of unemployment for all civilian workers was seven percent, the rate for all blacks was over 14 percent; for 16-19 year olds, over 18 percent; and for black teenagers, over 30 percent.

The teenagers, it was argued, did not really need the jobs. Blacks, it was alleged, preferred assistance handouts and did not really want jobs; in any case, many who may have been willing to work for a living were educationally unprepared for the many jobs that were presumably available. Women, on the other hand, were assumed to be supported primarily by a male “head of family,” or were interested in working only to “supplement” other family income. Thus the unemployed were drafted as freedom fighters despite themselves — to be pacified by some welfare handouts and a little job training.

Selecting Special Variables for Analysis

There is something to be said for the idea that inflation may result when employment is too high. With larger numbers of people on payrolls, effective demand may rise higher than the supply of goods and services available for purchase. But the supply itself will be reduced if labor productivity is lowered, if production costs are raised, and if military goods and services are a large part of the output and therefore not available to soak up consumer purchasing power.

There are other variables to be considered as well — particularly in any country with a high and growing capacity to produce. In a period of high unemployment, when an economic stimulus puts more people to work for pay, the increase in total output may hold prices down. But the same may happen when employment is high and there are raises in wages and benefits. In this situation, particularly in capital intensive sectors (where wages are a smaller part of total costs), labor costs should not rise proportionately, and may hold steady or even fall. Also in this situation, output may increase because workers do not need to

strike, or even to engage in slowdowns to keep from working themselves out of jobs. There is no good reason to assume that the incentives involved in higher income will increase the cooperation and productivity and efficiency of managers and administrators and professionals, but will not do the same for workers.

In addition, barring a shortage of some important component, higher output can reduce capital and overhead costs by spreading them over a larger volume of production. Finally, even if a shortage of materials or skills holds output down in particular industries at higher levels of employment and growth, this condition may coexist with an over-supply of certain goods, such as agricultural products, and of untrained or unwilling jobless in other industries. These are only a few of the situations in which increases in wage rates and prices do not necessarily go hand in hand.

Omitting Structural Variables

There are still more variables, structural in nature, in the relation between employment levels and prices. The role of government is fundamental in this regard. Government subsidies, tax incentives, anti-trust policies, and both regulation and deregulation policies continually affect the levels of both output and prices. Additional variables are the powerful influences of the many fiscal, monetary and exchange rate policies that affect both the structure and level of consumption, investment, imports and exports. Perhaps the most powerful of these influences is central bank manipulation of interest rates and money supply, carried out in the Federal Reserve System.

If some of these important variables are excluded from attention, economic analysis results in narrow theoretical formulations which fail to explain many events. Thus, as unemployment rose in the 1970s, so did prices. Traditional economists were baffled by this "stagflation" phenomenon, which did not fit any "trade-off" theory. In the early 1980s, when the expansionary tax cuts of the Reagan Administration threatened rapid inflation, restrictive monetary policies of the Federal Reserve Board precipitated the recession of 1981-82. The nation's fiscal and monetary policies were diametrically opposed at this point, and no one could predict the outcome. The result was that interest rates and unemployment rose sharply, farmers and home builders and many others were devastated, but prices stayed relatively high — particularly "big ticket" prices, for homes, autos, and health care, for example.

Since the 1981-82 recession, the Reagan Administration has accumulated unprecedented peace-time deficits, but lo and behold, price levels have remained relatively stable. Both the traditional trade-off theory, and the older idea that deficits are always inflationary, were confounded. There were many reasons for this confusion in the economic indicators. High on the list has been the increased power of transnational corporations to lower real

wage rates in the U.S. and to foster the import of more low-priced goods (sometimes from U.S. subsidiaries) from poor countries with abysmally low wage rates.

The Failure of Theory to Explain or Predict

Economic trade-off theories which ignore too many important variables also leave the interpretative field wide open to those who can easily take advantage of the perplexing realities of the real world. Conservatives can insist that price stability is more important than high employment. They usually limit their consideration of the economic variables to the power of labor unions (1) to keep wages from falling when the demand for labor falls; (2) to enlarge the gap between high-paid and low-paid labor; and (3) to contribute to inflation by wringing higher wages from corporations which will then raise consumer prices. Such limited analysis allows them to pursue many other special interests: protecting the value of bonds; raising profit margins by keeping wages down; redistributing money upward from lower to higher income groups; weakening organized labor; curbing welfare benefits; or reducing government regulation of business.

More progressive observers who are committed to full employment without inflation focus their consideration of the economic variables on the power of corporations and conglomerates (1) to use wage increases as an excuse to raise prices far more than any increased costs may require; (2) to fix minimum prices for their products; or (3) to manufacture shortages by agreements to reduce output and raise prices. In this process they also pursue other interests and goals: a revived labor movement; a healthy growth of essential social services; greater equality in economic opportunities; a reduction in wasteful or unneeded military spending; less concentration of private economic power; and a government which is strong enough to restrain corporate excesses, negotiate anti-inflationary income policies, and where necessary, impose direct or indirect controls over interest rates and prices.

Such conflicting adversarial approaches are shunted off to the political arena, without further illumination from present-day economic theories. The ambition of economists to approximate the formal elegance of natural scientists is one of the motives for excluding too many relevant variables. Unfortunately, the greater "elegance" of physics, which is usually regarded as the most advanced of all the sciences, is due primarily to the smaller number of variables which physicists juggle.

Another factor, perhaps more important, is psychological: the expectation that any serious effort to attain genuine full employment would be faced by enormous obstacles. Though rarely mentioned openly, this deeply felt presumption is probably just as strong as the expectation of future inflation, which is openly recognized by many economists as a factor in keeping interest rates high. Psychology contributes powerfully to the continued containment of full employment.

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