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13. The Role of Employment Policy

HYMAN P. MINSKY

INTRODUCTION

The war against poverty is a conservative rebuttal to an ancient challenge of the radicals, that capitalism necessarily generates "poverty in the midst of plenty." This war intends to eliminate poverty by changing people, rather than the economy. Thus the emphasis, even in the Job Corps, is upon training or indoctrination to work rather than on the job and the task to be performed. However, this approach, standing by itself, cannot end poverty. All it can do is give the present poor a better chance at the jobs that exist: it can spread poverty more fairly. A necessary ingredient of any war against poverty is a program of job creation; and it has never been shown that a thorough program of job creation, taking people as they are, will not, by itself, eliminate a large part of the poverty that exists.

The war against poverty cannot be taken seriously as long as the Administration and the Congress tolerate a five per cent unemployment rate and frame monetary and fiscal policy with a target of eventually achieving a four per cent unemployment rate. Only if there are more jobs than available workers over a broad spectrum of occupations and locations can we hope to make a dent on poverty by way of income from employment. To achieve and sustain tight labor markets in the United States requires bolder, more imaginative, and more consistent use of expansionary monetary and fiscal policy to create jobs than we have witnessed to date.

Incidentally, tight labor markets, by making all labor something of value will go far to building morale among our urban and rural poor. The community facilities program may be a poor substitute for tight labor markets, even for the social objectives it is trying to achieve.

The war against poverty must not depend solely, or even primarily, upon changing people, but it must be directed toward changing the system. However, the changes required are not those that the traditional radicals envisage. Rather they involve a commitment to the maintenance of tight full employment and the adjustment of institutions, so that the gains from full employment are not offset by undue inflation and the perpetuation of obsolete practices.

To anyone who has a deep commitment to a liberal pluralistic democracy, a policy of changing the system rather than changing people is most attractive.

Job creation in the context of the American economy means the sophisticated use of expansionary monetary and fiscal policies. Irrational prejudices, to which even the recent highly professional Councils of Economic Advisers have catered, exist against spending, deficits, and easy money. Ignoring these prejudices, are there any serious barriers against using expansionary aggregate-demand-generating policies to achieve tight full employment? In addition, if barriers do exist, can expansionary policies be designed which get around or over them? These are the problems upon which this paper will focus.

Other papers at this conference have considered the various definitions as well as the characteristics of poverty in America. We will just note that the Council of Economic Advisers estimated that in 1963 the heads of 30 per cent of the families living in poverty were employed all year and another 30 per cent were employed part of the year.[1] A program of ending poverty by generating tight full employment will mainly affect these families, as well as those which will have members drawn into the labor force as a result of jobs being available.

It is also estimated that the heads of some 40 per cent of the families living in poverty were not in the labor force during 1963. Obviously, expanded, improved, and modernized programs of transfer payments and income in kind for the aged, the infirm, the disabled, and needy children are necessary. As I see it, this has little to do with the war on poverty; it has mainly to do with our national conscience and affection for man. Simple decency calls for a system of transfer payments and income in kind for the case book citizens that lifts their lives well above any "poverty line."

[1] Council of Economic Advisers, *Economic Report of the President*, 1965, p. 166, Table 21.

This paper is almost exclusively concerned with the problem of generating enough job opportunities of the right kind, at the right place, and with sufficiently high incomes so that all who are willing and able to work can earn enough from jobs to maintain themselves and those for whom they are responsible at a level above some poverty line. Some adjustments and additions to our system of transfer payments may be required; in particular, family allowances may be in order. However, from the perspective of this paper, such changes are peripheral elements; the fundamental element in any war against poverty is jobs.

Of course, sane adults should be free to choose poverty, but no one should have poverty thrust upon him.

Tight Full Employment

The single most important step toward ending poverty in America would be the achieving and sustaining of tight full employment. Tight full employment exists when over a broad cross section of occupations, industries, and locations, employers, at going wages and salaries, would prefer to employ more workers than they in fact do. Tight full employment is vital for an antipoverty campaign. It not only will eliminate that poverty which is solely due to unemployment, but, by setting off market processes which tend to raise low wages faster than high wages, it will in time greatly diminish the poverty due to low incomes from jobs. In addition, by drawing additional workers into the labor force, tight full employment will increase the number of families with more than one worker. As a result, families now in or close to poverty will move well away from it. There may be a "critical minimum effort" that is needed to move families to a self-maintaining income growth situation, this effort bringing about a sharp move to a position well above poverty. Having multiple earners in a family is one way of achieving this.

That is, there is no better cure for poverty than family income, especially family income earned on a job.

There is a need for us to envisage what a tight full employment economy in the United States would look like. Many adjustments might be needed. For example, if we know that we can generate as many jobs as there are workers seeking work, then those programs, many of which are legacies of the Great Depression, designed to control the size of the labor force can be eliminated. In fact, the combination of a commitment to tight full employment and the view that income earned on a job is best indicates that programs to expand the labor force are in order.

Serious research on the attributes of tight full employment should be undertaken, not only because it is a weapon in the war on poverty, but also because it certainly is one of the attributes of any Great Society. In this section only three attributes of tight full employment will be taken up:

1. The size of tight full employment GNP in 1965
2. The effect of tight full employment on relative wages
3. The effect of the transition to tight full employment on the price level.

The "interim" employment goal set four long years ago by the Heller Council of Economic Advisers and reaffirmed by the Ackley Council this year is a four per cent unemployment rate. On the basis of Swedish and other European experience, this is a very slack employment goal. Even if we allow for considerably greater voluntary mobility and random industrial changes in the United States than prevail in Europe, the Swedish equivalent unemployment rate in the United States might be a measured 2.5 per cent unemployment rate (Table 1). As an interim definition of tight full employment, I shall use a 2.5 per cent unemployment rate. This is lower than the measured annual rate for any year since World War II.

The Council of Economic Advisers, which has been congratulating itself for the performance of the economy in 1964, admits that even with its slack four per cent definition of full

TABLE 1. UNEMPLOYMENT RATES, BY MONTHS, FOR SWEDEN, 1956–1963 (IN PER CENT)

Year	*Jan.*	*Feb.*	*Mar.*	*Apr.*	*May*	*June*	*July*	*Aug.*	*Sept.*	*Oct.*	*Nov.*	*Dec.*
1956	2.4	3.6	2.4	2.1	1.3	.7	.5	.7	.7	.9	1.3	1.9
1957	2.9	2.6	2.6	2.7	1.9	1.2	.8	.9	.9	1.2	1.7	2.7
1958	3.8	3.6	3.6	3.8	2.6	1.3	1.0	1.3	1.3	1.7	2.4	3.3
1959	4.3	3.4	2.6	2.7	1.9	1.2	1.0	1.2	1.2	1.3	1.6	1.8
1960	2.8	2.5	2.0	1.9	1.2	.8	.6	.8	.8	.8	1.1	1.4
1961	2.1	2.0	1.5	1.6	1.1	.7	.5	.7	.7	.9	1.2	1.4
1962	2.1	2.2	2.0	1.9	1.3	.8	.6	.8	.8	1.0	1.2	1.3
1963	3.6	2.5	1.9	1.8	1.1	.7	.6	.8	.9	—	—	—

Source: Sammanställning Arbetsmarknadstabeller, Kungl. Arbetsmarknadsstyrelsen, Stockholm, October, 1963.

The percentage unemployed is based on the number of registered unemployed within the unemployment insurance system. This number is considerably less than the total number of unemployed. Sample surveys of the labor force are also taken to gain more complete information about the number of the unemployed. The estimate of the total percentage of all unemployed as opposed to the actual percentage of insured registrants who are unemployed indicates a minor upward revision is necessary in the percentages in the table. For example, the estimated unemployment rate for all workers in November 1961 was 1.7 per cent compared to 1.2 per cent for workers covered by unemployment insurance. To adjust Swedish unemployment rates to American definitions, an upward adjustment of about 0.3 to 0.5 per cent is necessary.

Source: Joint Economic Committee, *Economic Policies and Practices, Paper No. 5, Unemployment Programs in Sweden*, Joint Economic Committee, 88th Congress, 2d Session, 1964, p. 16.

employment, the gap between the potential and actual gross national product was $27 billion in 1964.

What would GNP be in a tight full-employment United States in 1965? The forecast GNP is $660 billion, but the Council does not expect any reduction in the unemployment rate. Okun's rule of thumb is that for every one percentage point decline in the measured unemployment rate there is roughly a three per cent increase in measured GNP.[2] If we apply his rule to the difference between 5.2 per cent and 2.5 per cent unemployment rates, we get a gap of $53 billion. If we modify Okun's rule so that it holds only for unemployment rates down to four per cent, after which there is a one-one relation between percentage point declines in the unemployment rate and the percentage increase in GNP, we get a gap of $34 billion. No matter how it is estimated, the gap is much larger than the $11 to $12 billion which has been used as the amount it would take to raise the incomes of all those now living in poverty above the poverty line.

The pattern of relative wages in the United States reflects the past of the economy and present institutions as well as present labor market conditions. It is important to recall that relative wages are related to relative value productivities, and there is an interrelation between relative wages and relative prices.

The general rule seems to be that during periods of extreme labor market tightness wage differentials narrow, and that during periods of slack they increase.[3] The widening of the differential during a period of increasing slack in the labor market is illustrated by the relative gross average hourly earnings in the primary metal industry and in retail trade.

Since World War II, the ratio of primary metal to retail

[2] Arthur Okun, "Potential G.N.P.: Its Measurement and Significance," *1962 Proceedings of the Business and Economic Statistics Section,* American Statistical Association, pp. 98–104.

[3] A study which summarizes the evidence with regard to the effect of slack and tightness is Lloyd Ulman, "Labor Mobility and the Industrial Wage Structure in the Postwar United States," *Quarterly Journal of Economics,* LXXIX (February, 1965), pp. 73–97. The illustrative example used here is consistent with the results of Ulman's thorough analysis.

trade hourly earnings has risen from 1.54 to 1.70. In 1962, average hourly earnings in retail trade were $1.75, which is close to the $1.50 per hour that marks the poverty line. In 1947, wages in retail trade were two-thirds of those in the primary metal trade. If the same ratio ruled in 1962, given primary metal industry wages of almost $3.00 per hour, wages in retail trade would have been about $2.00 per hour. This is substantially farther above the poverty line than the $1.75 per hour that in fact prevailed. That is, if the 1947 wage ratio had been maintained, the contribution of retail trade employment to poverty would have been much smaller.

The cohesiveness of relative wages and the importance of key trade union contracts in setting a pattern for wage increases depend upon the over-all tightness in the labor market. In particular, wage gains in industries with weak trade unions—such as textiles—or with essentially no trade unions—such as retail trade—will keep up with or even improve on the bargains struck in highly organized industries such as steel and automobiles only if the labor market is tight.[4]

Between 1947 and 1962, employment in the primary metal industry fell by some 180 thousand, while employment in retail trade rose by more than 1,300 thousand. Over this period, as we have seen, the ratio of primary metal wages to retail trade wages rose from 1.54 to 1.70; that is, wages in primary metals rose relative to wages in retail trade, even though employment in primary metals was decreasing while employment in retail trade was increasing. This indicates that it was supply conditions rather than demand conditions that affected relative wages; for if it were demand conditions, the rising "demand" for labor in retail trade as compared with the primary metal industry would have led to retail wages increasing relative to primary metal industry.

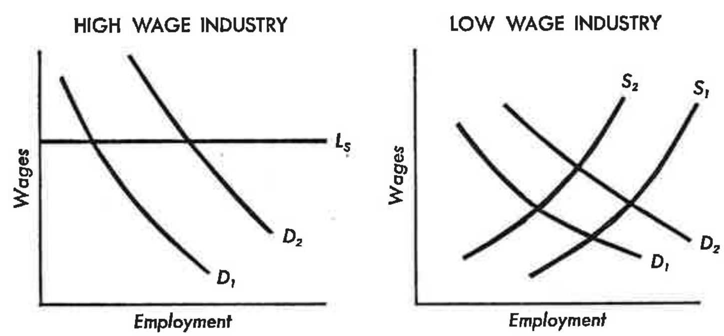
Conceptually, we can think of two sets of industries—high and low wage industries. High wage industries exist because the

[4] Harold M. Levinson, "Postwar Inflation," *Study Paper No. 21, January 1960, of "Study of Employment, Growth and Price Levels,"* Joint Economic Committee, U. S. Congress, 86th Congress, supported this view.

employers want to be able to "select" their workers. Perhaps they invest so much in training or are so vulnerable to worker dissatisfaction that they are willing to pay premium wages in order to be able to select their workers and keep them happy. Since they award a prize whenever they hire, these high wage industries have an infinitely elastic labor supply at their going wage (L_s in the diagram below).

A simple model which generates the observed type of relative wage behavior follows (Fig. 1):

FIGURE 1



The supply curve of labor to the low wage industries is upward sloping—but its position depends upon the number of workers employed by the high wage industries. Thus, if employment by the high wage industries increases, the supply curve of workers to the low wage industries shifts to the left; and if the high wage employment decreases, the low wage industry's labor supply curve shifts to the right. If the demand curve for high wage industry shifts to D_1 from D_2, the supply curve of labor to the low wage industry shifts from S_2 to S_1. As a result, wages fall and employment increases in the low wage industry.

If, on the other hand, aggregate demand is increased, so that the demand for labor in both the high and low wage industries rises from D_1 to D_2, then the supply curve in the low wage industry also shifts, this time to the left of S_2. Total employment in the low wage industry may rise or fall, depending upon the reaction of labor force participation rates to higher wages and improved job availability, but its wages will rise while wages in the high wage industry would remain constant.

This "model" of the labor market is static. It ignores the fact that in general real wages will rise over time. We can, as a first approximation, assume that in the high wage industry money wages will rise at the same rate as labor productivity. Thus, in a dynamic context, the fall in low wages, associated with labor market slack, and the rise in low wages, associated with labor market tightness, must be interpreted as a rise or fall relative to wages in the high wage industry.

One of the intermediate policy objectives of the anti-poverty campaign should be to facilitate the rise of wages in low wage industries while constraining the rise of wages in high wage industries. A problem that arises in implementing such an incomes policy is that it is also necessary to constrain the rate of increase of nonwage incomes. The proud boast of Gardner Ackley, Chairman of the Council of Economic Advisers, that corporate profits after taxes rose by 18 per cent in 1964 shows either that some policymakers are not serious about eliminating poverty, or a strange belief on their part that poverty has nothing to do with income distribution.

The anti-poverty campaign carries an implicit commitment to a rapid increase of those wages that are close to or below the poverty line. A more rapid increase in these wages than in the physical productivity of the workers implies a rise in the prices of the products or services that use these workers. For the measured price level to remain constant, offsetting decreases in some other prices—the prices for the products of high wage industries—would have to take place. That is, for price level stability, wages in high wage industries would have to rise by less than the increases in the productivity of their workers, and management in these often oligopolistic industries would have to pass this decline in unit costs on to their customers.

The existence of nonlabor costs and incomes makes the programming of declining prices when wages rise less than labor productivity difficult. Assume that the productivity of labor increases in our high wage industries, but wages are kept constant. Let us also assume that this is a truly disembodied increase in productivity: no increase in the capital stock or visible change in technique occurred. If prices per unit fell by the same percentage as did wages per unit, then gross profits per unit of output would also fall by the same ratio. However, the capital value of the firm and its ability to meet contractual financial commitments depends not upon the mark-up on wages, but rather on the flow of gross profits after taxes. Only if the elasticity of demand for the product is equal to or greater than one will such a fall in relative prices lead to a gross profit flow that is large enough to maintain capital values and meet financial commitments.

As firms tend to be risk averters, the usual assumption they will make is that the demand for their output is inelastic. They will attempt to cut price by a smaller percentage than the fall in their labor costs, thereby raising profit margins. Given the deviations from competitive conditions that exist in much of our economy, they will succeed in this effort. Thus, the distribution of income between profits and wages will shift to profits. This is not desirable both on policy and aggregate demand grounds, and given the generally strong position of trade unions in high wage industries, it is also not stable.

The outcome we can hope for with tight full employment and a commitment for low wages to rise more rapidly than high wages, is for high wages to follow some productivity guideline. As a result, prices of the products of the high wage industries will not fall, and prices of the products of the low wage industries will rise. The transfer of a larger proportion of the over-all productivity gains to the workers in the low wage industries will take place by way of rising relative prices for the output of the low wage industries.

We can look at the effect of relative wage changes in another way. The high wage workers, and other affluent citizens, have been subsidized, by way of low product prices, by the poor. If the poverty campaign results in tight full employment, it will lead to a cost push inflation; for the removal of the subsidy will lead to a rise in the measured price level.

This inflation is a phenomenon of the transition from a slack to a tight full employment economy. Once a tight full employment economy is generated and sustained, this source of inflationary pressure will cease. (Whether or not there is inflationary pressure in a sustained tight labor market will be discussed in the next section.) Given the highly emotional and thus irrational opposition to inflation that exists, those committed to the elimination of poverty in America will have to prepare to hold to their objectives while this transitional inflation occurs.

Incidentally, the position that the Administration (as well as many economists) has been taking—that the likelihood that inflation will occur increases as the unemployment rate gets to or below four per cent [5]—is in the nature of a self-fulfilling prophesy. By repeatedly stating this view, they are "brain washing" business and labor into believing that inflation is unavoidable at low unemployment rates. If business and labor begin to act as if inflation will take place once unemployment rates are down, then inflation will take place.

Part of the task of those committed to the success of the war on poverty is to enlighten all concerned that the rectification of relative wages—which is necessary for the success of the war—will be accompanied by a rise in the measured price level. This inflation is quite a different kettle of fish from an inflation which either maintains or perversely changes relative wages.

Our slogan must be: not all inflations are bad!

BARRIERS TO USING AGGREGATE DEMAND AS AN ANTI-POVERTY MEASURE

There is no doubt that the expected aggregate demand for 1965 is insufficient to generate tight full employment. A tight full employment GNP would be in the neighborhood of $700 billion. The Council of Economic Advisers forecast a GNP and thus an aggregate demand of $660 billion for 1965. They also predicted that no appreciable reduction in unemployment rates would be achieved. The estimated $660 billion GNP is below the slack employment definition of capacity the Council uses.

[5] Kermit Gordon, Director of the Bureau of the Budget, was cited by the *Wall Street Journal* of February 24, 1965, as holding this view.

A minimal aggregate demand policy for 1965 consistent with the objectives of the war against poverty is to use monetary and fiscal policy to raise demand to at least the four per cent unemployment capacity level, if not the tight full employment capacity level.

Three purported barriers to the effectiveness of measures to increase aggregate demand in the war on poverty will be discussed. One is that labor and product markets will operate so that an increase in aggregate demand will be dissipated in price increases. The second barrier is that urban white non-aged poor families are in the "tail" of the income distribution, so that an upward shift of median income will not appreciably reduce the proportion living in poverty. The third is that a rise in income, with or without an accompanying rise in prices, will quickly bring on a balance of payments crisis.

These three barriers are quite different. The first two are based upon technical characteristics of the economy; the third, the balance of payments barrier, is based upon legislated institutions and a policy objective. The dissipation via inflation argument depends upon assumptions as to the nature of labor demand and labor supply. The income distribution argument follows from an assumption that a move to tight full employment is equivalent to growth at full employment insofar as the distribution of income is concerned. These two arguments lead to the propositions that further increases in demand will merely result in inflation and in improving the lot of the already well-to-do.

As will be indicated below, it is not certain that these two barriers exist. Thus, they do not constitute a good reason for failing to take additional measures to increase aggregate demand, such as measures to ease the money market or an additional tax cut. Such programs should be adopted even though it can be shown that they would not be as effective in eliminating poverty as a correctly distributed increase in spending. However, they can be put into operation more quickly and thus should be used. If these technical barriers do exist, then the only cost of the experiment would be a once-and-for-all increase in the price level.

However, there is a real barrier to such an experiment with aggregate demand. It is the impact not only on our balance of payments, but also on our position as an international banker. Monetary ease as a means of expanding our economy is ruled out by the need to keep foreign (and domestic) short-term deposits in the United States. Since convertibility of European currencies has been achieved, the location of certain deposits is sensitive to covered interest rate differentials. Thus, the active use of monetary policy to expand demand is constrained by the banking aspect of our balance of payments problem. Under present arrangements, the monetary authorities must see to it that United States short-term interest rates are high enough to keep short-term balances—foreign as well as domestic—in the United States.

Thus the only really available devices for expanding aggregate demand are fiscal.

Underlying the Council of Economic Advisers' commitment to a four per cent "interim" unemployment goal is a belief that the "Phillips curve" for the United States is such that rapidly rising wages and prices occur whenever United States measured unemployment is below four per cent.[6] That demand increases are dissipated by price increases when unemployment is below four per cent is not a well substantiated argument. In the first place, the only type of tight labor market that has ever been observed in the United States is the transitional type. We move to tightness and back away. We have never observed the results of moving to a tight labor market and staying there. The evidence from World War II is not relevant; for unconstrained

[6] The "Phillips curve" is a relation between unemployment and wage or price increases. See A. W. Phillips, "The Relation Between Unemployment and the Rate of Change of Money Wage Rates in the United Kingdom, 1861–1957," *Economica,* XXV (November, 1958), pp. 283–299. See also, R. G. Lipsey, "The Relation Between Unemployment and the Rate of Change of Money Wage Rates in the United Kingdom, 1862–1957: A Further Analysis," *Economica,* XXVII (February, 1960), pp. 1–31; R. G. Lipsey, "Structural and Deficient-Demand Unemployment Reconsidered," in A. M. Ross (ed.), *Employment Policy and the Labor Market* (Berkeley and Los Angeles: U. C. Press, 1965), pp. 210–255; Paul Samuelson and Robert Solow, "Analytical Aspects of Anti-Inflation Policy," *American Economic Review,* L (May, 1960), pp. 177–194.

demand was far greater than potential supply, and of course great premiums were being paid to achieve desired labor mobility.

The evidence from Europe should be examined from the point of view of what labor market institutions would be needed in order to constrain inflationary pressures under conditions of tight full employment where the condition is expected to persist. It seems as if even in Sweden there still is a wage rate-unemployment relation similar to the Phillips curve, although, of course, the Swedish government does not use this type of inflation as an excuse for not maintaining tight labor markets.

The argument that tight full employment cannot be achieved by measures to increase demand is a structuralist argument. For the standard income determination models, it is assumed that labor is homogeneous and fluid. In such models, as long as there is any unemployment, the labor supply to any and all occupations is infinitely elastic at the same going wage rate. It does not matter how demand is increased: no matter where or what kind of initial impact occurs and no matter what the pattern of final output may be, the employment and wage effects are the same.

Obviously, labor is not homogeneous and fluid. The gestation period of a worker with particular skills in a particular place may be quite time consuming and the gestation process quite costly. At every date there is a need not only to generate the right kinds of labor, but also to make do with the available labor force. In theory, slight changes in relative supply prices of the various kinds, or qualities, of labor could lead to a considerable amount of substitution in production, that is, in making do. Such substitution in production would tend to narrow wage differentials. However, for many outputs the technical possibilities of substitution are limited.

Since labor is actually heterogeneous and viscous, the efficacy of different demand-generating instruments in raising employment depends upon where the initial change in final demand takes place, what the immediate derived demands are, and what is the ultimate change in final demand. In addition, it does not pay to train workers unless it is felt that the demand for a particular type of trained labor will be sustained. Thus, the expected length of time for which labor markets will be tight is a determinant of the extent to which labor will be trained to conform to the pattern of demand.

The standard theory of aggregate demand generation glosses over the differences in effect of the various demand-generating policy actions. Monetary ease, increased spending, and decreased taxes are perfect substitutes insofar as their effects upon GNP, employment, and prices are concerned. A conventional argument is that fiscal ease can be used to offset the effects of tight money; and seemingly, tax reductions are perfect substitutes for spending programs. But this, in fact, is not so.

All of the policy instruments have "what kind" as well as "how much" dimensions. Proper attention to the "what kind" is necessary in using monetary-fiscal measures, and the "what kind" should be determined in the light of the contribution it makes to the war against poverty.

As was mentioned earlier, the use of expansionary monetary policy is constrained by the international position of the dollar. Thus, we need not discuss it, except to note that the path from monetary ease to aggregate demand is not particularly favorable for the war on poverty.

The Administration emphasized tax reductions in its expansionary fiscal policy of 1964 and again in 1965. From the perspective of the war against poverty, this is a poor choice. The initial impact of tax reductions is through the increased spending power of those with incomes. The present poor are not direct beneficiaries; they benefit only to the extent that jobs are created, by way of the spending of the affluent, that they can get. Given the regional and ethnic concentration of poverty and income, the immediate demand for labor resulting from the spending by the beneficiaries of the tax cut will have only a small component of demand for the services of the present poor. From the point of view of the poverty campaign, it matters where the initial spending takes place. The "trickle down upon them" approach of tax cuts is not efficient; Harlem is not Scarsdale.

In order to use expansionary monetary and fiscal policy in an efficient program against poverty, it is necessary to recognize the heterogeneity and the viscosity of the labor force. This means that the emphasis should be upon the spending side of fiscal policy, and an object of the spending should be to have the largest primary and secondary impact upon the present poor. Thus, spending should be directed at the communities with low incomes, and the spending programs should directly employ the low-income worker.

If we look at the pattern of increases in government spending in the postwar period, it has been biased against the poor. The most rapidly growing sector of federal government spending has been upon research and development, which has been growing at the rate of 20 per cent per year. This has biased labor demand toward the highly educated and well trained. Another rapidly growing sector of final demand has been in education. The number of teachers increased by 48 per cent in the decade of the 1950's, while the labor force grew by 14 per cent. These policy-determined changes in the composition of final demand help to explain why the belief has grown that from now on job markets necessarily will be biased to the highly trained. A different emphasis in final government demand would have changed the trends in employment. After all, during the Great Depression the lament was, "I used to be on the daisy chain, but now I am a chain store daisy."

That is, there is nothing sacred about the pattern of demand for labor.

As a result of economic growth, the median family income of nonfarm white families whose head was aged less than 65 years had increased to $6,582 by 1960, and less than 10 per cent of this group had incomes in the poverty range. Even though the incidence of poverty in this class is small, it is a large group and contains some 30 per cent of all the poor. Locke Anderson advances the argument that for this large group of the poor, further increases in over-all income, resulting

[7] Locke Anderson, "Trickling Down: The Relationship between Economic Growth and the Extent of Poverty Among American Families," *Quarterly Journal of Economics,* LXXVIII (November, 1964), pp. 511–524.

from economic growth, will not appreciably decrease the incidence of poverty.[7] He based his argument on the fact that, in terms of the distribution of income, these present poor are in the long attenuated tail of the income distribution. An upward shift of the entire distribution will not draw a large number of these poor across the poverty line.

However, there is a difference between the growth of income that occurs in a persistently slack labor market, such as we have had in the recent past, and the shift from a slack to a tight full employment economy. There is no necessity for a tight full employment economy to grow any faster than a slack economy. The emphasis upon growth of the Heller era (which is persisting now that Gardner Ackley is Chairman of the Council of Economic Advisers) was a mistake. What needs to be emphasized is that the shift from a slack to a tight full employment economy would be accompanied by a once-and-for-all jump in GNP and a change in relative wages favoring the low wage industries. That is, the increase in average income which would occur during this period would be of such a nature as to reduce substantially the lower tail of the income distribution. Thus, the shift to tight full employment would lead to a marked reduction in poverty. This would be followed by a further slow decrease in poverty under conditions of continued growth with the new income distribution.

This can be illustrated by referring again to the argument about the relative wages of primary metal workers and retail trade workers. In 1962 the average hourly wage of primary metal workers was approximately $3.00, and retail trade workers averaged $1.75 per hour; that is, the median annual income was roughly $6,000 in primary metals, and approximately $3,500 in retail trade. Given this median income, a very small percentage of the primary metal industry workers would be likely to earn less than $3,000 per year, whereas a substantially greater percentage of the workers in retail trade would fall below the same poverty line. The change in relative wages which would occur in a tight labor market would increase the average annual income of retail trade workers relative to that of primary metal workers and markedly reduce the percentage of retail trade workers with incomes below the poverty line. On the other hand, an increase of, let us say, $500 in annual incomes of primary metal workers would not markedly change the number lying below the poverty line.

In addition, if the high aggregate demand resulted in shifting workers from low to high wage industries, then the incidence of poverty would be markedly reduced; i.e., the relative weights of the different occupations and industries in the determination of the over-all income distribution would change as tight full employment became the way of life.

Thus there is no real conflict between the proposition that tight full employment will lower poverty markedly and the proposition that further growth of capacity GNP will not quickly reduce poverty.

Fundamentally, tight full employment is inconsistent with the Administration's balance of payments objectives. An international monetary system with fixed exchange rates based upon the dollar is incompatible with tight full employment and the rapid elimination of poverty in the United States. If, for example, the marginal propensity to import equals the average propensity when imports are four per cent of GNP, then a GNP $50 billion larger than that achieved in 1964 would have resulted in additional imports of about $2 billion. Moreover, the move to tight labor markets would entail a rise in prices, which would further affect the balance of payments. A balance of payments deficit of $5 billion in any one year tends to generate a flight from the dollar; and a tight full employment economy would tend to create such a deficit.

To a considerable extent, ever since 1958 the needs of the dollar standard have acted as a constraint upon domestic income. We have not had tight labor markets because of the peculiar bind that the dollar is in internationally. It is apparently appropriate to allude to William Jennings Bryan by saying that, in part, the cross that the American poor bear is made of gold.

A Program Against Poverty

The reason we need to understand the barriers to pursuing a tight full employment policy is to enable us to design efficient

policy strategies to overcome these barriers—not to enable us to shrug our shoulders and prepare excuses for failure. In this section some suggestions will be made as to how the federal government's tax, spending, and monetary controls can be used to generate tight full employment, although, obviously, it will not be possible to include a complete catalogue of what should be considered.

The solution to the gold standard barrier is simple: get rid of the gold standard. If, for some subtle reasons understood only by bankers, the Department of State, and the Treasury, we cannot do this, then we can buy economic breathing room by raising the price of gold. An even better move would be to announce once-and-for-all that a "dollar is a dollar," that the U. S. Treasury will sell gold as long as it has any, but it will no longer buy gold. Within a very short time an international monetary system rooted firmly in the dollar's ability to command goods and services in the U. S. would arise—and we would be able to proceed to build the great society at home.

To the extent that we continue to try to live with the gold standard, expansionary monetary policy is not available as a weapon to achieve tight full employment. In fact, monetary constraint might have to be increased as income increases to compensate, as far as the balance of payments is concerned, for the greater volume of imports which accompanies the higher GNP.[8]

On the other hand, the argument that more rapid expansion will not improve the relative position of the poor is *not* a real barrier to more vigorous monetary and fiscal measures; it just asserts that it will not be effective. The answer to this objection is "let us try tight full employment and see what happens."

The function of intervention in a free enterprise economy is to make the economy behave so as to achieve the best of at-

[8] Obviously, all of the complexities of the international monetary problem cannot be considered in this paper, where it is but one of many issues. Many suggestions for modifying the present monetary system are being discussed, most of which are designed to bring greater flexibility into the world's monetary arrangements. It is important to note that we have brought "flexibility" into our international monetary arrangements by devices such as the interest rate equalization tax. The question is not one of fixity versus flexibility, rather it is "what type of flexibility."

tainable situations. "Best" often implies a choice, or at least a tradeoff, among objectives. The war against poverty as a "new" policy objective implies that the relative weights given to other policy objectives need to be reconsidered. In particular, the war against poverty requires both a definition of full employment as tight full employment and the inclusion of a relative wage or relative income policy objective in the set of policy goals.

Economic theory asserts that no appreciable inflation will occur until aggregate labor demand exceeds aggregate labor supply—the homogeneity and fluidity of labor will guarantee this result. However, labor is not homogeneous and fluid, and, in addition, effective production functions seem to be such that marked substitution among types of labor does not take place in response to small wage differentials. Thus, economic policy should devise interventions that make labor more homogeneous and that generate demand for the unemployed, relatively low wage workers.

The emphasis upon job training, labor relocation, and other similar programs is intended to make labor more homogeneous. However, there are limits to the capacity of such programs to transform particular types of labor which are in excess supply into the types that are in excess demand. Thus, as excess demand appears for particular classes of labor, further expansion of demand for labor should be concentrated on other types of labor. Once generalized excess supply of labor disappears, the choice between tax cuts and government spending as alternative fiscal stimuli becomes important. Whereas the ability to stimulate the demand for particular types of labor by way of generalized tax cuts is limited, the ability to tailor-make government spending to conform to the particular excess supplies is not limited. In other words, although tax cuts and spending are largely equivalent in stimulating recovery from a depression, they are not fully equivalent in generating full employment during a period when a substantial amount of unemployment is the result of structural changes.

Along with job training and labor relocation policies, programs to encourage the substitution of labor that is now in

excess supply for labor now in excess demand should also be undertaken. Aside from industry relocation, such programs might very well take the form of breaking complex jobs down into simpler jobs—for example, using park patrolmen as supplements to completely trained police. If we ever do get an urban extension service (comparable to the agricultural extension service) one of its tasks might be to look at an area's demand and supply of labor to determine how complex jobs might be divided into jobs within the grasp of the existing unemployed.

Dynamic economics is primarily concerned with differential reaction and gestation periods. We are learning that what happens to a child between the ages of three to five is of vital importance in determining the capabilities of the adult. Thus, preschool training is necessary to break the vicious circle of poverty. But if this view is true, then it takes 18 to 20 years to realize the benefits from such programs. Similarly, we cannot stimulate the demand for labor of a 20-year-old high school dropout by increasing appropriations for the National Institutes of Health, the Atomic Energy Commission, space programs, and the like. Programs must be designed which hold out a promise of a useful and productive life for our high school dropouts.

Spending programs aimed at directly employing those in the labor market who are poor, and opening up job opportunities for second earners in the families of the present poor, would have a strong impact upon poverty. Only in the second and subsequent rounds of spending following the original round will there be a demand for other kinds of labor, and, as indicated earlier, primary jobs for residents of Harlem will generate retail and service jobs in Harlem. The present poor are more likely to get such jobs than they are to get similar jobs in the suburbs.

The New Deal, with its WPA, NYA, and CCC, took workers as they were, and generated jobs for them. Sweden today generates public works jobs for the seasonally unemployed in its north country. We could easily do the same in areas such as Northern Wisconsin and Michigan, and for poor farm families throughout the country. The resurrection of WPA and allied projects should be a major weapon of the war on poverty.

Note that WPA was a labor intensive approach to unemployment, and it did tailor-make its projects to the capabilities of the available labor. There was another expansionary spending approach during the depression—PWA were its "initials" during at least part of its life—which went in for massive public works. Public works are favored by the trade union movement and by contractors as a solution to unemployment programs. In the context of the war against poverty, programs of expanding standard public works are inefficient; for they mean providing jobs for already affluent workers. "Public works" is not much better than a tax cut as an anti-poverty measure.

Work should be made available to all who want work at the national minimum wage. This would be a wage support law, analogous to the price supports for agricultural products. It would replace the minimum wage law; for, if work is available to all at the minimum wage, no labor will be available to private employers at a wage lower than this minimum. That is, the problem of coverage of occupations would disappear. To qualify for employment at these terms, all that would be necessary would be to register at the local public employment office.

Various national government agencies, as well as local and state government agencies, would be eligible to obtain this labor. They would bid for labor by submitting their projects, and a local "evaluation" board would determine priorities among projects. Because skilled, technical, and supervisory personnel are needed, the projects should be allowed to average something like $4,000 per worker. The federal government should put in some funds for materials, but the allocation for materials should be a fraction of the labor costs—let us say, 25 per cent.

Not so long ago, economists and other social scientists thought disarmament was a possibility. Daniel B. Suits used the Michigan model of the United States economy to estimate employment effects of various alternative programs. He found that if the government used $1 billion to employ some 260 thousand workers—i.e., a spending program concentrating on low income jobs—the result would be a rise of 322 thousand in employment (Table 2).

Let us assume that there are some two million more unemployed than there would be if we enjoyed tight full employment. As-

TABLE 2. MULTIPLIERS FOR SELECTED ACTIVITIES (BILLIONS OF DOLLARS)

	Government purchases	*Government employment*[a]	*Federal income tax level*	*Federal income tax yield*	*Social security transactions*	*Private investment in plant and equipment*
	+$1.0	+$1.0	+$1.0	+$1.0	+$1.0	+$1.0
Gross national product	1.304	1.903	−1.119	−1.798	0.825	1.690
Consumption expenditure	0.295	0.738	−0.915	−1.470	0.674	0.382
Unemployment insurance benefits	−0.160	−0.390	0.091	0.146	−0.069	−0.137
Tax recipts						
Federal	0.458	0.220	0.622	1.000	0.274	0.586
State and Local	0.030	0.034	−0.045	−0.072	0.033	0.058
Social Insurance	0.030	0.051	−0.024	−0.039	0.018	0.038
Employment (millions of persons)	0.089	0.322	−0.076	−0.122	0.056	0.115

[a] Additional government wage expenditure of $1.0 billion to hire 260,000 employees.

Source: Daniel B. Suits, "Econometric Analysis of Disarmament Impacts," in E. Benoit and K. Boulding (eds.), *Disarmament and the American Economy* (New York: Harper and Row, 1963), p. 104.

sume that the remaining "2.5 per cent" unemployed are short-term transitional unemployed who would not take advantage of such a program; standard unemployment insurance is sufficient protection for these unemployed. An expenditure of $7 billion per year, resulting in direct employment of 1,820,000, on the basis of Suits' estimates, would eliminate the excess unemployment. However, with a wage support law, workers making below the minimum wage—including many low-income farmers and people not now in the labor force—would join the program. Perhaps a $10 billion gross expenditure employing some 2,600,000 workers would be a more appropriate initial amount for the program.

Given that some 25 per cent of the labor cost would be available for material spending, the gross cost would be $12.5 billion per year. This would lead to a rise of $22.3 billion in GNP. Although it is a relatively unimportant consideration, federal tax receipts would rise by $3.3 billion; thus, the net cost of such a program would be some $9.2 billion per year.

This path to tight full employment generates a GNP that is smaller than the estimated tight full employment GNP used earlier. This is so because these workers are fed into the value of output at less than the median labor income.

Needed improvements of transfer and income in kind programs might cost an additional $5 billion per year. Thus, the total cost of a meaningful war against poverty might be $17.5 billion per year.

Incidentally, many of the proposed community development type projects might fit into the set of approved WPA type projects. Certainly a directive to the local evaluation body to weight such programs highly would be in order.

Once such an artifically created tight labor market existed, the pattern of excess demands for labor resulting from generalized measures to expand aggregate demand would indicate the job training and work relocations that should be undertaken. These training and relocation programs are really valuable within a context of tight labor markets. Lifelong learning for all is a necessary policy objective in our complex and ever-changing economy and society. Programs making this possible and ap-

pealing to all should be instituted. But this is not solely or even primarily a concern of the war against poverty.

In the process of achieving tight full employment, low wages in the private sector would be pushed up, hopefully, more quickly than high wages. (If this did not take place, tight full employment would have to be supplemented by an incomes policy.) Under these conditions, the national minimum wage could be raised. If, for example, $3.00 per hour is the median gross wage, the wage support level could be raised over time from its present level of 40 per cent of the median wage to 60 per cent. However, raising the minimum wage now is not particularly desirable; it is more important, first, to make the present minimum wage effective for all.

Many workers in both private and public employment are paid at or below the poverty line. Since an effective anti-poverty war would raise low wages relative to high wages, a question as to whether the rise in wages should be passed on to prices is in order.

For example, such workers as hospital attendants and orderlies require relatively little skill and can be trained easily. They also tend to receive incomes close to the poverty line. To raise their incomes and *not* raise the price of hospital care, the "public" nature of such employment should be recognized. It would strike a visitor from Mars as odd that in the United States the federal government can support the building and equipping of hospitals, but it cannot support the pay of the operating personnel. A scheme under which the federal government paid a percentage of the wages of workers in industries such as hospitals should be part of our permanent package of price- and income-determining measures.

Another aspect of the problem which I will just mention is that people can become impoverished, even though they are not poor. A skilled worker or an engineer, for example, may lose a job because of technical or program changes. If no fully equivalent job is available, this worker will suffer a capital loss—equivalent to the loss by fire of an uninsured house. Some integration of programs to cope with this dynamic and high level impoverishment into our unemployment compensation system seems to be in order. Perhaps the capital value of such contract revisions should be available as compensation to victims of technical change.

The line between what is private and what is public is narrow and arbitrary. Subsidized employment opportunities for the present poor and ill-trained are just as useful as subsidized employment opportunities for the people like us in conferences such as this, or in government supported research institutes. We are rich enough to afford boondoggles for the poor as well as the affluent, and I would expect the gains in welfare to be at least as great, per dollar of expenditure.

To conclude, the way to end the biggest chunk of poverty is to generate jobs at adequate incomes for the people in poverty. Some improvements in transfer payments, such as children's allowances and medical care for all without means tests, would help; but the basic approach must be to provide jobs for all who are willing and able to work—taking their abilities as they are.

Once tight full employment is achieved, the second step is to generate programs to upgrade workers. I am afraid that in the poverty campaign we have taken the second step without the first; and perhaps this is analogous to the great error-producing sin of infielders—throwing the ball before you have it.