

# Hyman Minsky and the War On Poverty

An Aggregate Demand Solution

# A Decade of Contributions

- (1965) “Poverty: The ‘Aggregate Demand’ Solution and other Non-Welfare Approaches,” Institute of Government and Public Affairs, UCLA
- (1965) “The Role of Employment Policy,” Reprinted from Poverty in America, Chandler Publishing Co
- (1968) “Effects of Shifts of Aggregate Demand upon Income Distribution,” American Journal of Agricultural Economics, Vol. 50, No. 2
- (19??) “Where Did the American Economy – and Economics – Go Wrong?” Draft Manuscript.
- (19??) “Policy and Poverty,” Draft manuscript
- (19??) “Minimum Wages”
- (1972) “Economic Issues in 1972: A Perspective,” Lecture given at Washington University, October 6, 1972. Draft.
- (1973) “The Strategy of Economic Policy and Income Distribution,” The Annals of the American Academy of Political and Social Science, Vol. 409
- (1975) “The Poverty of Economic Policy,” Draft Manuscript, Presented at the Graduate Institute of Cooperative Leadership

# The Age-Old Problem of Poverty

- Poverty was a **pressing** issue 200+ yrs ago
- Influenced by:
  - Enlightenment rationalism
  - Protestant evangelicalism
  - American self-confidence
- **Reformers** believed poverty could be “cured”
- Two main **causes** were considered:
  - Laziness or foolishness led to impoverishment
  - Political and economic structures failed to provide enough jobs and gave too much income to the rich

# Poverty in the Post-War Era

- **Little attention** to poverty throughout most of the 1950s
- Political discourse was preoccupied with **anticommunism** (McCarthy era)
- The **national debate** over poverty re-emerges in the late 1950s and intensifies in the 1960s
- Concern for the poor comes on the heels of **faltering economic growth** (1953-1958)
- In 1959, nearly 40 million Americans lived in poverty, despite unprecedented prosperity during the 1950s
- Discussion focuses on the **causes** of poverty and unemployment

# Paving the Way for LBJ

- Leftists and liberal scholars prepared the way for LBJ's War on Poverty
- Often **misleading** the public by focusing on the defective mentality of the poor
- JKG: *The Affluent Society* (1958)
- Michael Harrington: *The Other America* (1962)
- D.P. Moynihan's "culture of poverty" thesis
- Prepared the ground for a war on poverty that focused on people's defects



# John F. Kennedy

- In 1963, Michael Harrington's *The Other America* became the **first Penguin paperback** published in America
- Serious planning to combat poverty began the same year, following a dramatic **slowdown in exits from poverty** over 1956-1961
- Other events fueled anti-poverty agenda:
  - Civil rights leaders assailed Attorney General **Robert Kennedy** for the administration's poor record
  - **March on Washington** in Aug. '63 emphasized need for civil rights *and* jobs
- By November, President Kennedy had approved an **anti-poverty program**
- Days later, Kennedy was **assassinated**, and LBJ became the 36<sup>th</sup> President of the United States



# Who Was Lyndon B. Johnson?

- A great **admirer** of FDR
  - Directed the **NYA** in Texas
- Elected to **Congress** in 1937 and the **Senate** in 1948
- Democratic **Majority Leader (1955-1960)**
- Greatest American **liberal** president of the post-WWII era
  - Empire of laws and agencies called the **Great Society**
- First American president **thoroughly committed** to civil rights for African Americans



# Johnson's 3-Pronged Approach

- The day after Kennedy's assassination, President Johnson agreed to move "full speed ahead" with an anti-poverty agenda
- He declared an "unconditional war on poverty" in his first State of the Union address on January 8, 1964
- He signed the **Economic Opportunity Act** on August 20, 1964
- Johnson's approach relied on:
  - 1.) **Tax cuts** to spur economic growth
  - 2.) The **War on Poverty** to rehabilitate and train the poor for the jobs that 1.) would generate
  - 3.) New programs like **Medicare**, **Medicaid** and **Model Cities**, together with a beefing up of existing programs like **food stamps**, **welfare** and **Social Security**, were supposed to address any problems that 1.) and 2.) did not fix



# Richard Nixon

- **Eliminated** components of the War on Poverty
- But Nixon took **tentative** steps toward a new antipoverty policy in the early 1970s
- His plan for a **guaranteed income** failed in Congress
- But **Social Security** benefits were increased, Congress approved an Earned Income Tax Credit (**EITC**), and a limited program for **government jobs** for the poor and unemployed was introduced

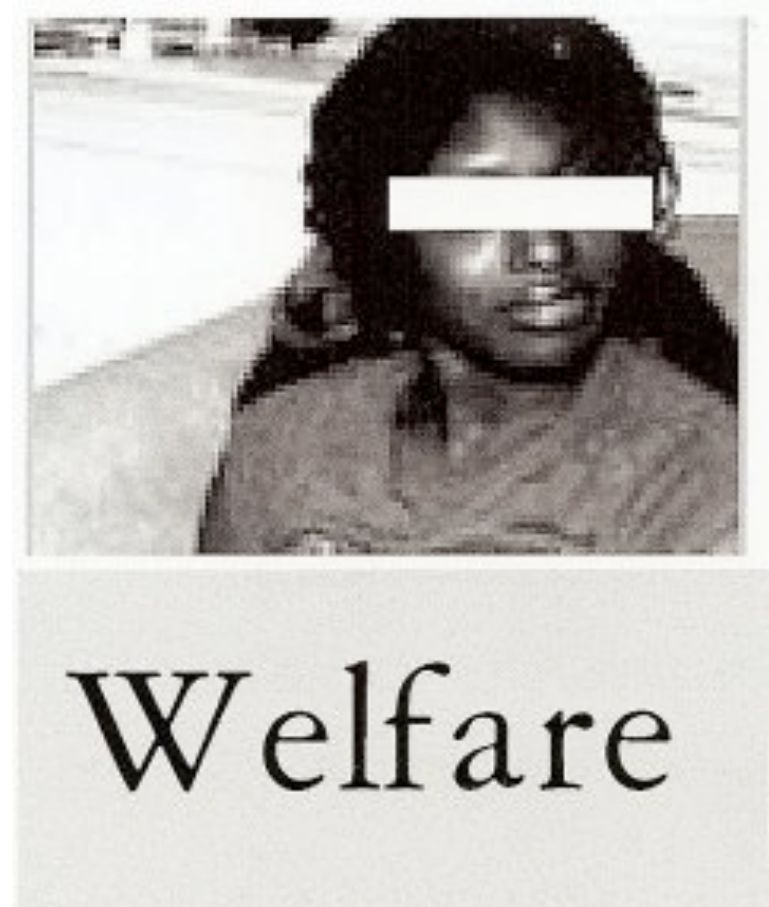
# The Demise of Liberalism

- By the late 1970s, the political **balance** had shifted against liberalism
- The **radical** movements of the 60s played a role in shifting public opinion
- But so did soaring **inflation** and rising **unemployment**
- Conservatives **blamed** social programs for discouraging hard work and entrepreneurship



# Ronald Reagan

- By the mid-1980s, conservatives began to shape **public debate** on poverty, welfare and unemployment
- Aggressive **campaign** to turn white workers against the average, poor person of color
- Led to **popular belief** that poor people were poor by choice



# Bill Clinton

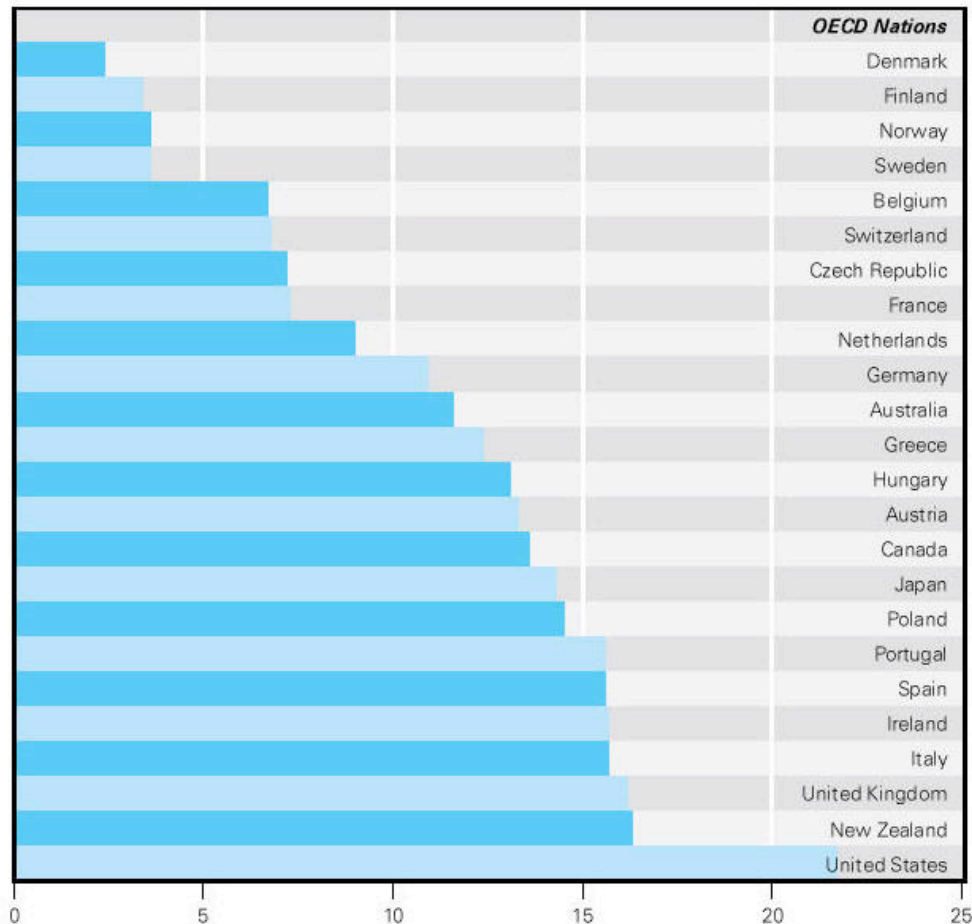
- During the so-called “Clinton boom,” the problem of unemployment **faded** from the radar
- Attention focused on the harmful effects of **welfare**
- A return to “**motivational rehabilitation**”
- Few **dared** to ask whether the positive reports on welfare reform, poverty and unemployment painted a realistic picture of what was happening



# George W. Bush

- By 2001, the 'Goldilocks' economy had **faltered**
- The US entered a **recession** in March 2001 and unemployment rose sharply
- The private sector showed almost **no net job growth** from March 2001-spring 2005
  - Only significant job growth was in the public sector
- By 2004, the US had the **highest poverty rate** of any rich democracy

**Figure 1.1** Relative income poverty: Percentage of children (0-17 years) in households with equivalent income less than 50% of the median.



Source: UNICEF, *Child Poverty in Perspective: An Overview of Child Well-Being in Rich Countries*, Innocent Report Card 7, 2007.

# Was the WoP Successful?

- In the **Long Term**....
- No
- Since the War on Poverty:
  - **Unemployment** rates have trended **upward**
  - **Long-term unemployment** has become increasingly **concentrated** among the labor force's most **disadvantaged**
  - **Poverty** rates have **stagnated**
  - **Real wages** for most workers have **declined**
  - The gap between the “**haves**” and the “**have-nots**” has widened
- In the **Short Term**, conditions improved
  - Poverty rates fell from 15% in 1965 to just under 12% before the start of the Nixon recession
  - Roughly 3% decline attributable to the WoP
- But the **improvements weren't evenly distributed**, and **most are no better off** today than they were before the War on Poverty was launched

# The Long Term Success of the WoP

## Percent of Males Aged 25-64 with Incomes Sufficient to Keep a Family of Four Out of Poverty

Year	White	Black
1940	40%	10%
1960*	75%	50%
1970	90%	70%
1990**	80%	60%

\* Fastest decrease occurred between 1940 and 1950

\*\* Similar to 1965, when the War on Poverty began

# Poverty Rates for Seniors

- Only the elderly have sustained their improvements over the long term
- Poverty rate for those 65+ was nearly 30% in 1966
- Fell to about 15% by 1974
- Then fell to around 10% by the end of the 1990s
- But was almost entirely due to expansions in Social Security -- had little to do with the WoP



# What the War on Poverty Did Not Include

- Although his Task Force pleaded with him to do so, Johnson **refused** to make **direct government job creation** part of the war against poverty
- Johnson was also **opposed** to **redistribution** and **avoided** terms like “**inequality**”
- And he rejected proposals to lift incomes through direct aid (e.g. grants), telling his assistant, **Bill Moyers**, “no doles”
- He even instructed **Lester Thurow** to remove all references to “cash handouts to the poor” from the *Economic Report of the President* in 1964 (anti-Buddhist!)

# Poverty Remains a Serious Problem

- In **each** of the last 50 years, at least 11% of the US population has been poor
- In 2004, a **family of 4** considered poor if household income was below \$19,157
- **37 million** poor under that definition
- Millions more in state of **near poverty** (not counted) with incomes that fail to provide for a decent standard of living

# What Follows

- We can accept that staying out of poverty *is* partly a matter of **individual effort**
- But it is also (and more so) about **institutions** and **structures** that allow individuals to succeed or fail in their aspirations
- The level of individual effort probably has **not changed** much since LBJ launched his War on Poverty
- But structures and institutions have, and these changes help us explain the **successes** and **failures** of Johnson's War on Poverty

# Eliminating the Welfare Structure

- Johnson's reforms relied on welfare and transfer payments rather than work and jobs
- Minsky said, "We live only as well as we produce"
- The explosion of transfer payments represents a perversion of Roosevelt's New Deal and Truman's Fair Deal
- Lot of the poor can only be improved by programs that put them to work

# The WoP According to Minsky

- Minsky believed that the war on poverty would fail unless AD was “**adequate**”
- He focused on:
  - The **size** of the necessary demand
  - The **barriers** to achieving it
  - The **efficiency** of the available weapons
  - The possible **side effects** that would accompany an “adequate” AD

# Minsky's “Non-Welfare Approach”

- He argued that **standard welfare economics** misinterpreted welfare because it ignored the importance of **uncertainty**
- Minsky **advocated** a policy approach that would **diminish** uncertainty for all (as opposed to adopting institutional arrangements that modify or diminish uncertainty for a particular sector)
- He **pointed out** that “in a world with uncertainty ... [a] scheme that limits the losses that are allowable may be a necessary first step ....”

# Money Income vs. Income In Kind

- Economists tend to prefer programs that distribute **money income** over those that provide **income in kind**
- **Efficiency vs. Safety**
- But **political** solutions tend to favor safety (education, Medicare, housing subsidies, etc.)
- Economists' efficiency-oriented policy prescriptions are based on world with **certainty**
- But the “**practical man's** preference [is] for programs that provide income in kind”

# A Higher Floor

- Minsky argued that the war on poverty, if successful, would **establish** “a floor to family real income that is substantially higher than the existing floor”
- But this goal had to **compete** with other, existing policy goals:
  1. Full employment
  2. Economic growth
  3. Domestic price stability
  4. International stability of the dollar
- The **weight** attached to each of these goals would indicate “how seriously the war on poverty is to be taken”



# #1 The Goal of Full Employment

- Minsky argued that the **weight** attached to this goal had to **increase** if the War on Poverty was to succeed
- He also believed that there were positive **externalities** associated with employment
- And he believed that it was “better to eliminate poverty by means of income from **jobs** than to eliminate poverty by transfer payments”

# Defining “Full Employment”

- Minsky **ridiculed** the Phillips curve approach, arguing that it “seems to beguile policy makers and analysts into cutting the employment goal to fit the price level cloth”
- He suggested some alternative ways to **define** full employment:
  - “When over a broad spectrum of occupations and a large proportion of the geographical regions more jobs are open at a going wage than the number of unemployed workers”
  - “Tight full employment”
    - A target unemployment rate that reflects European **postwar** experience and US **wartime** experience – about 2 ½ percent

# Benefits of “Tight Full Employment”

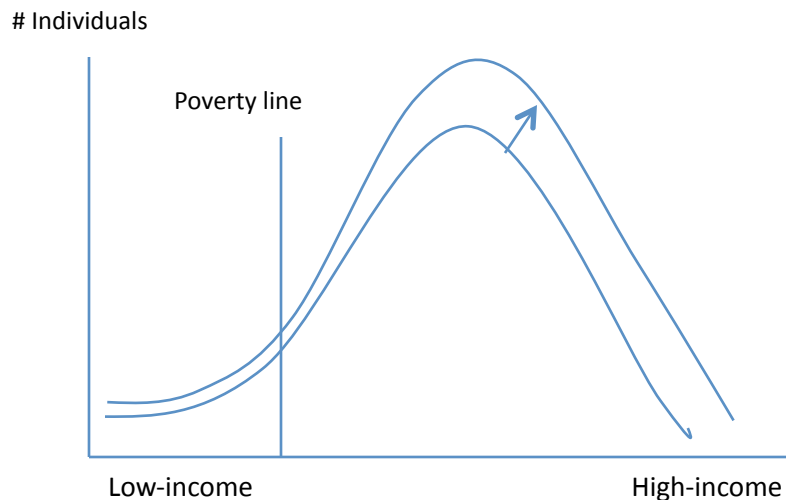
- Most obvious beneficiaries are those whose poverty is due to unemployment
- Benefits of Tight Full Employment policy include:
  - Some **heads of families** not currently in the labor force will be drawn into the labor market
  - Will increase **state and local** government **tax receipts** and alleviate strain on budgets to finance welfare services
  - Frees up financial and real **resources** to help the poor who really must depend upon public support (e.g. children, disabled, elderly)

## #2 The Goal of Economic Growth

- The **weight** attached to this goal should **decline** with the introduction of the elimination of poverty as a policy goal
- Policies aimed at increasing the rate of economic growth almost always affect **income distribution** perversely
  - Benefits flow to the well-to-do at the expense of low income families
- Does **not** imply a **no-growth** economy
- Growth may even be **higher** at tight full employment than with slack employment, even without growth-stimulating policy measures in place

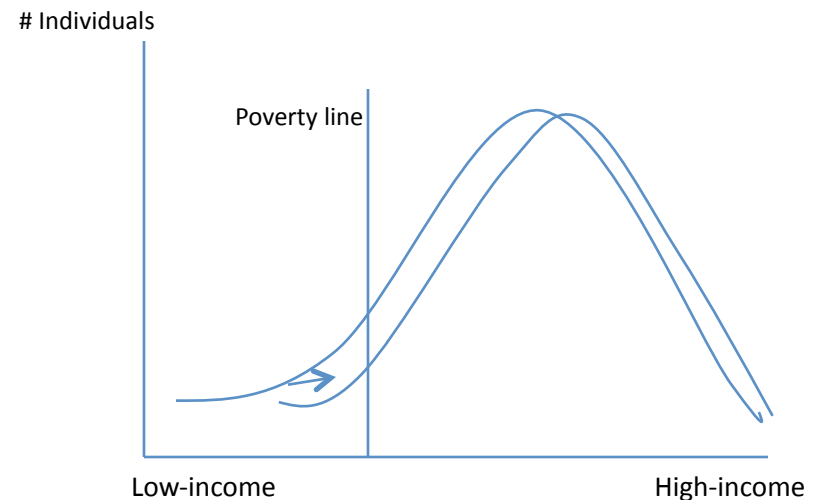
# Tight Labor Markets vs. Growth

Impact of Economic Growth with  
Unchanged Labor Market  
Conditions



**Accelerated Growth** shifts the entire distribution upward but **does little** to eliminate existing poverty

Impact on Distribution from a Move  
from Slack to Tight Labor Market



A **Tight Employment Policy** reduces poverty by truncating the lower end of the income distribution

# #3 The Goal of Price Stability

- Minsky referred to the goal of domestic price stability as “a most **peculiar** policy goal” that was “not consistent with tight full employment”
- By the mid-1960s, the **Phillips curve** was entrenched in mainstream thinking
- Policymakers were conditioned to the idea of a tradeoff and were willing to **sacrifice** employment in order to achieve price stability
- Minsky questioned the **existence and stability** of the Phillips curve and insisted that the **benefits** of price stability were **nebulous** while the costs of pursuing the goal could be quite high
- He believed **policymakers** had attached too great a weight to the goal of price stability

# Inflation as A Reasonable ‘Price’ to Pay

- Minsky argued that the transition from slack to tight labor markets would “**more than likely** be accompanied by some inflation”
- The wages of high-income workers would rise at least as fast as productivity, but the **incomes of low-wage workers** would rise even **faster**
- Costs of **G&S** produced by low-wage workers would rise relative to those produced by high-wage workers
- Minsky **acknowledged** that this would show up in the CPI
- But he believed that the costs imposed by a **modest** increase of inflation (estimated at 4 percent) would be outweighed by the gains from eliminating the output gap

# #4 The Goal of Exchange Rate Stability

- The US was on Bretton Woods
- Domestic policy had to ensure:
  - Holders of US dollars did not convert, *en masse*, to the reserve asset (gold)
    - Accomplished by keeping short-term interest rates high
  - The deficit on current account was constrained
    - Accomplished by keeping income low, relative to capacity and by restraining inflation through unemployment
- Moving to tight full employment would undermine these goals:
  - $\uparrow Y \rightarrow \uparrow M \rightarrow \downarrow CA$
  - $\uparrow P \rightarrow \downarrow X \rightarrow \downarrow CA$
- Minsky suggested that if the war on poverty was to be taken seriously, policymakers would have to abandon dollar stability as a policy goal



# Summary: A Reordering of Goals

A successful war on poverty would require:

- 1.) Tight Full Employment – **Elevated** as a policy goal
- 2.) Domestic Price Stability – **Downgraded** as an *economic* concern, but relevant as a *political* concern
  - Anti-poverty programs need to minimize the extent of inflation that accompanies tight full employment
- 3.) Economic Growth – **Downgraded** Somewhat
- 4.) Stability of the Dollar – **Downgraded** Substantially

# Minsky's Anti-Poverty Approach

- Minsky insisted that “tight full employment is **essential** for the rapid elimination of poverty”
- The policy problem is how to **achieve and sustain** TFE
- The **weapons** are monetary and fiscal policy
- Each has “**what kind**” and “**how much**” dimensions
- Minsky **assumed away** the major obstacle (Bretton Woods) and focused on the remaining barriers
- The most significant barrier stemmed from the **political** weight attached to domestic **price** stability

# Accepting Some Transitional Inflation

- Minsky cautioned that it would be necessary to “**ride out**” a transitional inflationary period in order to wage a successful war against poverty
- He focused on **two sources** of inflationary pressure that would accompany the transition to TFE:
  - The effect on the **ratio** of low to high wages
  - Trade union pressure for higher wages during TFE
- The first was considered **desirable consequence** in the war on poverty, the second could be dealt with through an **incomes policy**

# The Role of an Incomes Policy

- Minsky advocated **guidelines** for wage and non-wage incomes
- He recognized that it may be necessary to establish guidelines to limit the growth of **corporate income** (dividends and retained earnings) by using punitive tax policies to prevent these incomes from rising faster than some guidelines
- He wanted the guidelines **themselves** to be determined through a bargaining process

# What About the “Transitional” Inflation?

- Some wage-price pressure will occur due to **intrinsic heterogeneity** of labor demand and labor supply
- Not all workers are **fit** to **handle** all jobs
- Not all **mixes** of final demand generate the same mix of labor demands
- May have **excess supply** in some jobs and geographic locations and **excess demand** in others
- Wage (and cost) pressures arise as **local** labor markets pass to excess demand for particular type of labor
- When this becomes **generalized** (i.e. the aggregate unemployment rate falls), the weight of locally tight labor markets increase and costs pressures may arise

# A Final Word on Inflation

- Minsky argued that domestic price stability was “in practice not consistent with TFE”
- He also argued that “the economic costs of mild inflation are not imposing”
- But he recognized that inflation “remains a political hobgoblin,” so the anti-poverty program would have to be designed to minimize the inflation that would accompany TFE

# Was Minsky Right?

- Look at the experience during the “Clinton Boom”
- US experienced a recession in 1990-1991
- Leading Indicators suggested a strong recovery between 1992 and 1995
  - Investment rose at fastest pace since WWII
  - Productivity rose at twice the rate of the 70s and 80s
  - Inflation remained low
- The Clinton Administration saw rising productivity as “the primary source of income growth” and “the answer to stagnant real wages”

# But Living Standards Did not Improve

- According to the Census Bureau, median family income in 1994, adjusted for inflation, was \$38,782, one percent *below* its 1991 level
- And there was no significant increase in median family income in 1995
- Continues the downward trend that began in the early 1970s
- The average weekly earnings of 80% of working Americans **fell** by 18% between 1973 and 1995, from \$315/wk to \$258/wk
- NB: Total compensation (health and pension benefits plus wages) rose by roughly 2.7% during this period, but that was the lowest increase since the statistic was first compiled in 1981



# Growth Won't End Poverty

- It was the first time in postwar history that the real wages of most workers failed to increase **during a recovery**
- Reflected the fact that **compensation** had become increasingly tied to corporate share prices
- More and more, **rewards** from greater productivity went to shareholders, top managers and their employees

# Implications for Poverty

- Minsky argued that “the poverty program in its most fundamental sense is concerned about income distribution”
- He insisted that it mattered how the gains were distributed in a growing economy
- He said, “the world is better off if low incomes rise by say 5 percent while high incomes rise by say 2 ½ percent per year than if all incomes rise by 3 percent”
- And he added that “the world is worse off” if “the rich are getting richer and the poor are getting poorer”
- Even Greenspan warned in July 1995 that the growing inequality could become “a major threat to our society”

# Job-Related Poverty

- Normal for capitalist economies to operate with substantial unemployment
  - Early 50s and late 90s are exceptions
- In the absence of big wars, unemployment never stays low for very long
- Capitalists don't want depression-level unemployment
- But they don't want "tight full employment" either
- Want to be able to control workers and suppress wages

# Jobs, Not Transfer Payments



Problem with the WoP  
was its focus on welfare  
and transfer payments

Focus should have been  
on work and jobs

Working poor ended up  
worse off in many cases

# Too Much Income, Too Few Jobs

- Minsky insisted that “we **live** only as we **produce**”
- **Lamented** the growth of transfer payments for welfare, pensions and social security
- Provide in income without adding to production
- Transfer payments accounted for just **.1%** of GNP in 1929
- Called the trend a “perversion of Roosevelt’s New Deal and Truman’s Fair Deal”

**Historical Trends in Transfer Payments<sup>1</sup> and Grants in Aid**  
(Expressed in millions of dollars)

Year	Federal, State, and Local Transfer Payments	Grants-in-Aid	National Income	Total Transfer Payments and Grants	Total Transfer Payments and Grants as Percentage of National Income
1947	13.1	1.7	195	14.8	7.6%
1950	18.0	2.3	236	20.3	8.6
1955	18.3	3.1	328	21.4	6.5
1960	28.8	6.5	412	35.3	8.7
1965	39.8	11.1	566	50.9	9.0
1970	78.1	24.4	798	102.5	12.4
1971	92.4	29.0	858	121.4	14.2
1972	102.1	37.5	952	139.6	14.7
1973	116.1	40.6	1065	156.7	14.7
1974	138.1	43.9	1136	182.0	16.0
1975	173.6	54.6	1215	228.2	18.8
1976	189.1	61.1	1360	250.2	18.4
1977	202.9	67.5	1526	270.4	17.7
1978	218.7	77.3	1724	296.0	17.2
1979	246.0	80.4	1926	326.4	17.0

1. Transfer payments are defined as direct payments by government to individuals, e.g., social security, pensions, veteran disability, welfare, and tax rebates.

# Take People As They Are



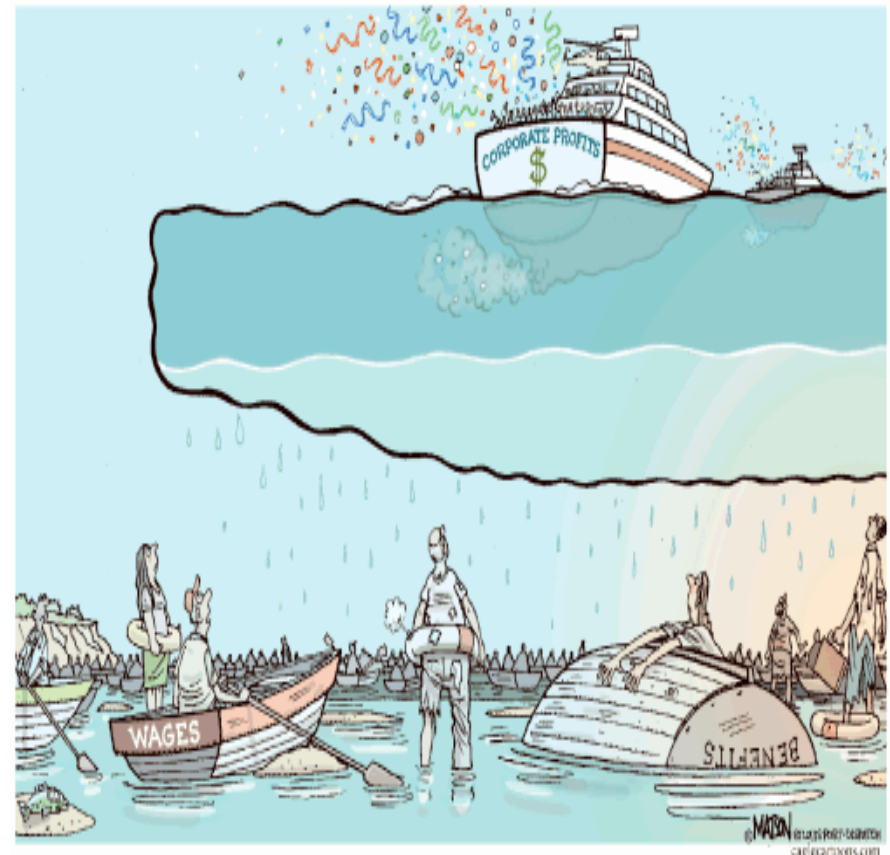


# Focus on Changing the System

- Job-related poverty cannot be solved as long as government is run for the capitalists (Stricker, 2007)
- Two choices:
  - Try to eliminate unemployment *indirectly*, by adopting policies to promote economic growth
  - Target employment *directly*, by creating jobs and raising wages
- Problem is to find jobs for all those who need and want to work

# What Remains of the War on Poverty?

- Economic **theories** upon which the WoP was based are **still dominant**
- **Problem** is with the **poor**
- Reliance on the rising tide of **private-sector-led growth** combined with some **supply side policies** to improve conditions for those at the bottom



"I'VE NEVER SEEN A TIDE RISE LIKE *THAT* BEFORE!"



# Need to Focus on Bones, Not Dogs



- **Supply-Side Explanation**

- Unemployment implies a problem in the labor market
- Something is wrong with the dogs (mismatch in skill set)
- Solution is better education and training of dogs

- **Demand-Side Explanation**

- Unemployment implies a problem with the level of aggregate demand
- Training and Education will not reduce unemployment – it will just *reallocate* existing jobs
- Solution is increased spending to make more “bones” (i.e. jobs) available

# Key Omissions in the WoP

- Lacked a massive job creation program
- Resulted from the CEA's belief that
  - Poverty is not inextricably linked to unemployment
  - Unemployment could be sufficiently reduced through AD policies (esp. JFK's tax cut of 1963)
  - A buffer stock of unemployed was necessary to keep inflation in check
- We must overcome these obstacles if we are to end poverty in America

# Ending Poverty: A Radical Approach

- Most of the early success at eliminating poverty had to do with creation of SocSec for the aged
- Little to do with more rapid growth of GDP or WoP programs themselves
- To mount a successful War Against Poverty, we Need:
  - To support redistribution of income away from the every rich toward the poor (Minsky, Keynes)
  - Direct job creation
  - Protection of unionization and requirements for higher pay
  - More training and better schools
  - Redesign social programs (provide income for those who cannot work)
  - National health care program