In: John Marangos and Nikolaos Karagiannis (eds.) *Toward a Good Society in the Twenty First Century: Principles and Policies*, New York: Palgrave

Friday, May 03, 2013
7:05 PM

Chapter 8

The Making of a Good Society: Lowe's Instrumental Method and the Pursuit of Full Employment

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Introduction: Economics and the Good Society

I have titled this chapter the "The Making of a Good Society." I have paraphrased it from Robert Heilbroner's now famous PhD dissertation; however the title suggests that a good society is something that is made. It is a process; in fact, it is a continual process—a process by which clearly defined (though modifiable) goals are forged and effort garnered toward their eventual achievement.

The policy goals for a good society should be toward enhancing society's general welfare. This presents economists and policymakers with three overarching concerns: (1) the problem of unemployment or the goal of full employment, (2) the problem of recessions or the goal of macroeconomic growth, and (3) the problem of inflation or the goal of price stability.

The objective of macroeconomics is toward the development of a theory that both aids in the analysis and provides solutions for policy makers toward the achievement and maintenance of the goals of a good society. There is little consensus among macroeconomists as to how to analyze such phenomena and as to what the viable solutions are. An ideological divide has been forged among economists. This divide has led to a methodological debate in both the analysis and the construction of viable solutions for macroeconomic problems.

The ideological debate to the present day centers on neoliberal policies backed up by the mainstream neoclassical economic approach versus active government involvement backed up by heterodox economic theory.[1] Neoliberalism is premised on the faulty assumption that the

promotion of individual freedom leads to the promotion of societal welfare. In other words, the neoliberal view assumes no misalignment between the microeconomic goals of self-interested individuals and the macroeconomic goals of society; promoting the former promotes the latter. This connection leads policy makers to advocate for the protection of individual property rights, the protection of institutions that provide for freely functioning markets, and the promotion of free trade (Harvey 2005, 64). The neoliberal agenda has become dominant in both the economic dialog and the American political strata.

> Common interests and values among the great powers are also the basis for promoting peace and security around the globe. . . . As we preserve the peace, America also has an opportunity to extend the benefits of freedom and progress to nations that lack them. We seek a just peace where repression, resentment and poverty are replaced with the hope of democracy, development, free markets and free trade. . . . Free trade and free markets have proved their ability to lift whole societies out of poverty—so the United States is working with the entire global trading community to build a world that trades in freedom and therefore grows in prosperity. (Bush 2002)

The quotation from the former president of the United States embodies the neoliberal tradition of free markets and free trade. The agenda can be reduced to the promotion of individual freedom.

The neoliberal agenda is not new; it has its roots in England with Friedrich Hayek and is further rooted in the United States with Milton Friedman and the Chicago School of Economics. Hayek's (and the Chicago School's) view of the individual is centered on the "knowledge problem."

The knowledge problem deals with coordination and action of economic actors. For Hayek, individuals lack all the information that is necessary to coordinate economic activities. Hayek's viewpoint is that individuals are filled with limited and mostly erroneous knowledge. Because of this it then becomes impossible for centrally planned economies to collect, much less filter, all the knowledge that is required for answering questions related to production and distribution. Thus, Hayek defends free market capitalism and suggests that the market, not the government, is clearly the most efficient device to coordinate economic activity.

For Hayek, free markets coordinate economic activity through the formation of spontaneous order. "The formation of spontaneous orders is the result of their elements following certain rules in their responses to their immediate environment" (Hayek 1973, 43). As such, it is the

result of "human action not of human design" (Forstater 2003, 189). In other words, macroeconomic order is assumed as the unintended consequence of individuals pursuing their own self-interest (Fehl 1994, 197). If such order is to be consistent with the goals of a good society, it must be shown that the promotion of individual freedom and free markets can always produce such macroeconomic results.

There are (at least) two problems to this conclusion for heterodox economists. The first problem can be immediately recognized from Hayek's definition of spontaneous order. According to Hayek, macroeconomic order is the unintended consequence of individualistic behavior *if and only if* "[the] elements follow certain rules in their responses to their immediate environment" (ibid., 43). The "rules" that must be followed are that businesses always engage in profit-maximizing behavior and consumers always pursue utility maximization. Profit and utility maximization guide economic behavior both in response from, and according to, the rules of supply and demand (Lowe 1987b, 143).[2]

Adolph Lowe (2003) suggests that "spontaneous order" (what Lowe terms "spontaneous conformity") presupposes a level of rational understanding of social processes. Lowe submits that such understanding of complex processes, such as industrial capitalism, exceeds the normal capacity of an individual (Lowe 1987a, 12). Henceforth, it is highly unlikely that the behavior of all individuals will conform to the strict rules of free market processes. Individual behavior can neither conform to the laws of supply and demand nor make rational, profit, and utility-maximizing decisions required for free market processes (Lee and Keen 2004, 188–192). The promotion of individual freedom cannot, at the same time, promote the larger goals of a good society. Lowe (1942, 1987b, 1951, 2003) was highly critical of such a deterministic relationship between supply and demand. Many contemporary heterodox theorists share Lowe's early objections.[3]

The neoliberal approach of the traditional economics confounds individualistic microeconomic goals with macroeconomic goals. Unlike the neoliberal approach, the methodological approach of Adolph Lowe (1965) termed the "instrumental method" requires the separation of microeconomic goals and macroeconomic goals of society.

By isolating the goal of full employment as our macroeconomic objective as a case study, here we address that the promotion of free markets in the United States over the past three decades has not achieved, and cannot achieve, this objective. Further, the "unintended consequences" of the promotion of free markets has not led

to advancing societal welfare in the United States. Rather, it has led to the deterioration of the working class, an increase in crime, and a deterioration of the psyche of those affected by unemployment. It is conveyed below that contrary to neoliberal thought, there must be a clear separation between the macroeconomic goal of full employment and the microeconomic goal of profit generation. The latter does not promote the former. Private sector businesses are guided by the profit motive and will always and everywhere not only fail to achieve a fully employed society but also, rather by promoting pecuniary self-interest, create a society where unemployment is the norm. If full employment is to be maintained, it must be an actively pursued policy by the federal government. These issues will be discussed below, and the chapter will end with a brief discussion of the current Employer of Last Resort (ELR) proposal, which advocates direct government involvement toward the goal of full employment at the same time maintaining the pecuniary interests of capitalists.

Traditional Methodology versus Lowe's "Instrumental Methodology"

Traditional neoclassical analysis is ill-equipped to provide any meaningful policies toward the goal of full employment. We can go into a variety of reasons why but this is a distraction. Therefore, we will abandon the traditional neoclassical method in favor of the heterodox approach of Adolph Lowe. For Lowe, the postulates of traditional economic analysis are neither suitable nor even capable of deriving confirmable predictions of economic activity (Lowe 2003, 1942, 1965. However, Lowe's instrumental method assumes that the "actual forces that rule economic movements and in particular bring about a change in their direction cannot be known a-priori, but themselves fall in a category of unknowns" (Lowe 1965, 15). The instrumental method inverts the technique of traditional economic theory and departs from neoclassical theory.[4]

The first point of departure is that the macroeconomic goals are an a priori judgment made by governing officials who represent the general interests of society. The second point of departure is that the instrumental method assumes that the initial state of the economy is directly observable and complex. The microeconomic elements that make up the macro-economy represent the data that need to be studied. Lowe asserts that behaviors of consumers and producers cannot be generalized as in neoclassical analysis. Economic analysis needs to be grounded in the "sociological raw material" (2003, 148) that

makes up everyday life that guide decision making regarding what to produce, how to produce, and how to distribute the output. The bulk of the work of the instrumental method is studying the sociological influences guiding production and distribution and gaining an understanding of its effect on the macro-economy. This framework is in stark contrast to neoclassical analysis that assumes a priori that consumption is based upon constrained optimization and producers maximize profits. For Lowe's instrumental method, consumer and producer behavior needs direct observation.

Following an investigation of the sociological and economic factors that guide production and distribution, the task of the instrumental method turns to discovering the conditions suitable, including necessary governmental regulations, for the attainment of the pre-declared macroeconomic goals. The instrumental method is a normative approach; it is "the logic of economic goal seeking" (ibid., 17).

To demonstrate Lowe's instrumental method, let us isolate and examine one macroeconomic goal of US policy makers, the goal of full employment as outlined in the Full Employment and Balanced Growth Act:

> An Act to translate into practical reality the right of all Americans who are able, willing, and seeking to work to full opportunity for useful paid employment at fair rates of compensation; to assert the responsibility of the Federal Government to use all practicable programs and policies to promote full employment, production, and real income, balanced growth, adequate productivity growth, proper attention to national priorities, and reasonable price stability.

The Full Employment and Balanced Growth Act was passed by the ninety-fifth US Congress as a macroeconomic goal irrespective of the current economic, political, or social makeup of the system. Given the lofty goal of full employment, the next challenge of the instrumental method becomes defining the current state of the U.S. economy, and studying both the economic and sociological impediments to maintaining our goal of full employment.

The Problem of Unemployment in Capitalist Economies

The Full Employment and Balanced Growth Act calls for "government to use all practicable programs and policies to promote full employment, production, and real income." Traditional Keynesian type of government intervention, such as priming-the-pump, has

been one popular approach to promote full employment, but it is limited in its effectiveness (Tcherneva 2008). This limitation is partly because pump-priming policies are designed to work countercyclically with only the attempt to pull economy out of a downturn but not to maintain full employment; thus no attempt is made to address the long-term social and economic consequences of unemployment (Wray and Forstater 2004. In reality, the unemployment problem is multifaceted; therefore it requires intervention in many areas.

True to Lowe's instrumental method, to understand how and where government should intervene requires an understanding of what the economic and sociological factors are that deter the unemployed from gaining and holding on to private sector employment. Further, what other social consequences are coupled with unemployment that may need to be contemporaneously addressed? These questions must first be investigated before devising policies for government intervention.

Sociological Affects and Consequences of Unemployment

Government legislation to promote full employment cannot be articulated without first analyzing the sociological factors or the "sociological raw material," (Lowe 2003, 148) which impedes workers' ability to regain private sector employment. Mark Granovetter (2005) proposes that the ability to attain (and maintain) employment will vary depending on the size and strength of a worker's social network. Social networks are the ties that individuals have with one another. There are strong ties and weak ties, strong ties being ties with family members and close friends. Similarly, weak ties are more impersonal, such as ties with acquaintances and colleagues. Weak ties further connect individuals who are more distant and are likely gained through employment. A weak social tie expands a worker's social network. The greater an individual's social network the greater an individual's prospects of maintaining employment throughout their lives. Likewise, Granovetter's (1983) analysis on "the strength of weak ties" argues that individuals with fewer "weak ties" are less likely to be exposed to employment opportunities than those with many. Frequent contact between network members is connected with the persistence of social relationships (Feld 1997). The persistence of relationships among the unemployed can diminish over time due to feelings of social isolation and depression.

The social and psychological effects of unemployment add a further barrier to regaining employment as evidenced from Browman,

Hamilton, and Hoffman's (2001) study of the unemployed in Michigan following the General Motors plant closings in the late 1980s. The study is important as it links social and personal effects, such as, increase in crime, increase in divorce rates, deterioration of mental and physical health, and so on, as all consequences of stress (Brenner 1973). Browman, Hamilton, and Hoffman find that high stress leads to social, physical, and psychological consequences. The initial response to unemployment becomes imperative to the overall level of stress that the unemployed are subjected to. It is not surprising that the response to unemployment is different for different individuals. One's support network at the time of unemployment plays an important role, as does the current financial situation and the original reason for unemployment. Browman, Hamilton, and Hoffman (2001) find evidence that unemployment due to mass layoffs (such as plant closings) is not an initial stressor in workers' lives. These groups of the unemployed tend not to fault themselves for circumstances that, in their minds, are beyond their control.

Nevertheless, stress and distress is of a circular, cumulative, and causative nature. Exposure to stress causes additional stressful situations, such as unemployment as an initial stressor that in turn causes financial hardship. Financial hardship in turn leads to anxiety, hostility, and depression. Anxiety, hostility, and depression will open the door for further exposure and vulnerability to additional stressors (Browman, Hamilton, and Hoffman 2001, 11). As the authors conclude:

> Simply put, to have become unemployed and hence distressed—depressed, anxious, whatever—is to less likely gain reemployment or more likely to lose a subsequent job. Unemployment deals a double whammy because its consequence, distress, has further consequences—reduced employability—which make it harder to get back to square [one], unemployment leads to family stress and disruption, this too can have consequences for future employment, if only because it feeds the spiral of distress. (10–12)

Even when the initial cause of unemployment is of no fault of the worker, as time passes, workers' inability to become reemployed becomes a major cause of stress in their own lives. Workers may now see themselves as being at fault for their inability to acquire employment, and stress mounts especially in the midst of continuing financial hardship. Stress then leads to lower self-worth, anxiety, depression, family disruption, increase in drinking and drug use to cope with the stress, poor physical health of the unemployed and their families,

and increased thoughts of suicide (Brenner 1973). Stressful situations simply do not pass; these are life-altering situations. The prolonging of unemployment further impedes the possibility of reemployment. Soon the unemployed could become unemployable.

Regular employment provides not only a basic income for individuals but also sets up a much needed social environment that is important and necessary for individuals. Losing one's regular job decreases their level of social activity that they were previously engaged in (Kelvin and Jarrett 1985). Workers become friends, and they engage in social activities inside and outside the workplace. Unemployment causes dependency issues within families. Inside and outside the family structure, the unemployed, especially the long-term unemployed, are seen as second-class citizens (Kelvin and Jarrett 1985, 6). The marginialization of the unemployed disrupt their day-to-day functioning within society and the normal functioning of the family. In these situations, both strong ties and weak ties dissipate further inhibiting the unemployed's possibility of regaining employment.

The relationship between unemployment, racial inequality, and crime could also be considered. As of the 2010 US census, 35 percent of Americans claim minority status. Of these Hispanics make up the largest share with 48.4 million Hispanics residents, accounting for over 15 percent of the US population, and African Americans comprising the second largest minority group with 37.7 million, accounting for over 13 percent of the US population. The distribution of unemployment in the United States is disproportionately skewed toward that of minorities. The two largest minority populations (Hispanics and African Americans) consistently have higher unemployment rates as compared to whites.

From 2000 to 2008 Hispanics narrowed the unemployment gap between themselves and whites to a difference of about 2.5 percent. Following the "Great Recession" of 2008–2009, this margin has increased to roughly 4 percent. The unemployment data for African Americans is not as promising. The unemployment rate for African Americans has consistently been about twice that of their white counterparts since 1980. During the Clinton expansion of the 1990s, the African American unemployment rate averaged just a little short of 8 percent. During this same period, the unemployment rate for white Americans was about 4.5 percent, 1 percentage point below the Federal Reserve Bank of Philadelphia's definition of "full employment."

One measure of economic inequality between minorities and whites can be illustrated by examining the black-white and Hispanic-white unemployment ratios. The ratio is calculated by dividing the minority

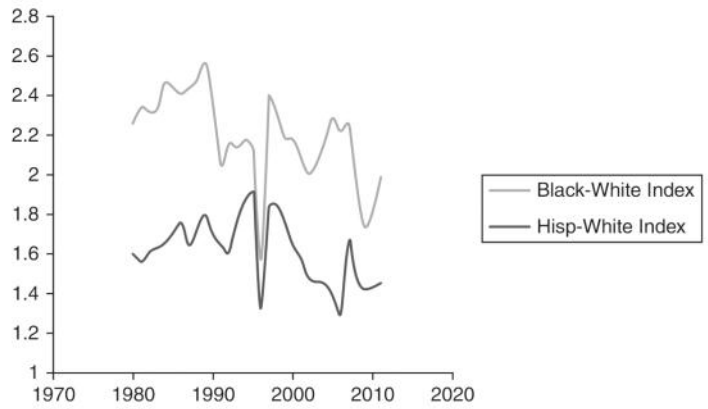

Figure 8.1 Black-white, Hispanic-white unemployment ratio.
Source: US Bureau of Labor Statistics and author's calculations.

unemployment rate by that of the white unemployment rate. A ratio of 1.00 is defined as economic equality between minorities and whites; the higher the ratio, the greater the degree of economic inequality. The unemployment ratios between these groups are graphed in Figure 8.1 for the period 1980–2011. It is seen from Figure 8.1 that African Americans are disproportionately affected by unemployment. With the exception of 1996, African American unemployment has continuously been 2.0–2.5 times that of whites for the past three decades.

Hispanics have fared better than African American. From 1999 to 2008, the economic outlook for Hispanics was improving as evidenced in Figure 8.1 by the steadily decreasing Hispanic-white unemployment ratio during this time. Since the Great Recession of 2008, any improvement in economic equality over the previous five years was lost; current economic policies have been unable to neither solve the problem of aggregate unemployment nor tackle the disproportional distribution of unemployment.

Addressing unemployment can also reduce criminal activity. Empirical studies illustrate a positive correlation between crime and unemployment (Raphael and Winter-Ebmer 2001). So government's active pursuit of the problem of unemployment also assists in the "war on crime" as evidenced by the 1990s, which witnessed a decade long expansion and a concurrent drop in overall crime (Wallman and Blumstein 2005, 319–348). During the Clinton expansion, the official unemployment rate fell to a 30-year low of 4.5 percent between

1992 and 1997, while the crime rate dropped 30 percent (Raphael and Winter-Ebmer 2001, 259).

Unemployment contributes to poverty, psychological and mental anguish, criminal activity, and racism. So public policy put toward alleviating unemployment is a large stepping stone to solving many other social problems.

The Macroeconomic Goal of Full Employment

A fully employed economy includes the whole of the labor force that is willing and able to work. It has become clear that current free market policies do not result in a good society (Murray 2010a). The neoliberal agenda of Hayek and the Chicago School, embedded in policy making of the United States, created a society where unemployment is persistent and is the norm rather than promoting full employment.

The promotion of free markets saw a brief period of high employment in the 1990s, but the Clinton free-market agenda also created a culture of private sector corruption and fraud that led to the collapse of giant companies such as Enron, WorldCom, and Tyco. High levels of output could not be maintained through the Bush presidency, and the Obama presidency has seen the highest official unemployment rates in decades; a corrupt corporate culture; the deterioration of the entire US financial system; and the rise of grassroots movements protesting the lack of job opportunities, corporate greed, and rising inequality. If the past two decades can serve as a yardstick, the macroeconomics outcomes of a laissez-faire policy are far from promoting public welfare as hypothesized by the neoliberal agenda of free markets.

The government must be an active player in the pursuit of full employment. The type of policies enacted by legislators must also be considerate of, and work with, interdependent firms operating in a capitalist society. One policy approach is for the creation of a direct-government-jobs program through an ELR program. The nature of the ELR program is to guarantee public employment for those who are willing to work, which is historically consistent with a number of legislative measures to remedy the problem of unemployment.

The federal government has historically subscribed (at least on paper) to actively pursue full employment as a policy agenda. Franklin D. Roosevelt proposed an "Economic Bill of Rights," which would have given Americans "[t]he right to a useful and remunerative job in the industries or shops or farms or mines of the nation"; however Roosevelt died in office before he could see the plan through.

Shortly after Roosevelt's death the Employment Act of 1946 was enacted, which called for the federal government to ensure "maximum employment." This legislation was followed in 1973 by the Comprehensive Employment and Training Act (CETA). Its purpose was to train workers and provide them temporary federal jobs. The Humphrey-Hawkins Full Employment Act of 1978 mandates that one of the four goals of the federal government is for full employment. The Humphrey-Hawkins Act replaced the earlier Employment Act of 1946 and has a more stringent goal of full employment rather than maximum employment.

Humphrey-Hawkins Act has been upheld, but the Reagan years saw the repeal of CETA, which was replaced by the Job Training Act of 1982, which provided job training for economically disadvantaged groups. The Job Training Act of 1982 was later repealed in 1998 under the Clinton administration and was not replaced with a federal jobs program. Rather it was replaced with watered down legislation that attempts to encourage private industries to assist in workforce and career development. The repeal of the Job Training Act and of similar legislation is despite the mandate under the Humphrey-Hawkins Act that one of the responsibilities of the federal government is to promote full employment.

The ELR approach is a solution to the full employment mandate required under Humphrey-Hawkins. Stemming from the earlier work of Hyman P. Minsky (1986), the government-job-guarantee approach to full employment is to hire off the bottom, hiring the workers who are unable to find private sector employment. As Minsky argued:

> The policy program is to develop a strategy for full employment that does not lead to instability, inflation, and unemployment. The main instrument of such a policy is *the creation of an infinitely elastic demand for labor* at a floor or minimum wage that does not depend upon long- and short run profit expectations of business. Since only government can divorce the offerings of employment from the profitability of hiring workers, in infinitely elastic demand for labor must be created by government. (1986, 307)

Much focus in discussions of the ELR approach involves affordability and feasibility. Concerning affordability, the main proponents of the ELR approach take a functional finance perspective, positing "that any nation that operates its own currency, and which adopts a floating exchange rate, can implement an ELR program, each nation might formulate the specifics of its program in accordance with its own political and economic situation" (Wray 2000, 1).

The functional finance approach to the ELR program is built upon Abba Lerner's (1943, 1947) approach to government debt and deficits. The first law of functional finance states that the main financial responsibility of the government is to control the issuance of currency to where the supply of money in the economy is just sufficient to buy the whole of the output, at the full employment level, at current prices. In other words, there is no financial constraint on a government that is the monopoly issuer of its own currency to provide for both full employment and price stability. The ELR approach to full employment is a direct means of the government to maintain full employment (and issuing currency to do so) rather than providing fiscal stimulus and waiting for the multiplier to go into effect so that the private sector can provide jobs.

The second law of functional finance states that the government should sell bonds when it is desirable to reduce the money supply in order to maintain positive interest rates. The government debt is not really a "debt" in the conventional term; rather it can be considered the interest rate maintenance account (Wray 1990).

When the ELR employs workers from "off the bottom," there are obvious stimulus effects. Employment provides income for individuals to spend in the private sector. Lower-income groups have higher marginal propensity to consume, which will provide the necessary initial boost in demand for employers in the private sector to increase investment, and thus output, to satisfy the additional demand. Increased production in the private sector will then cause an increase in labor demand. Workers will then move from ELR employment to private sector employment (Murray2010b, 2012; Fullwiler 2007; Forstater 2000; Tcherneva and Wray 2005; Carlson and Mitchell 2002). The ELR program will move countercyclically to the business cycle. Government spending on an ELR program will also be countercyclical.

An ELR program is an improvement upon unemployment insurance. Instead of the government paying unemployed individuals to not work, it is paying them to work. Keeping this group of workers employed maintains their skill levels and social networks; reduces the social costs of unemployment, including health consequences, psychological stresses, and crime; and targets the disproportionally affected minority group thereby promoting racial equality while simultaneously alleviating insufficient effective demand (Wray and Forstater 2004, Forstater 2004).

Keeping workers trained in skills, and educated in fields that are demanded by the private sector, can increase productivity thus

lowering costs to private sector production. It is a more comprehensive and direct-job-creation program. ELR also aligns with the American sense of democracy and social justice, because it encourages work rather than unemployment compensation, while still protecting the elders and the disabled.

Conclusion

The instrumental method requires Americans and our governing officials to decide which macroeconomic goals are worth pursuing. If the federal government is serious about the promotion of full employment, then a different methodology than what is offered by neoclassical economists is required. Policy makers should adopt an "instrumental methodology"; policy makers must articulate the policy goal first and then work with the private sector to achieve this goal. If deficiencies in pursuing full employment exist at the microeconomic level, then the federal government needs to step in and become involved in direct job creation. Government policy such as ELR is consistent with the existing US macroeconomic goals and contributes to the making of a good society.

Notes

1. It should be noted that New Keynesian sticky-wage and sticky-price models allow for the role of government intervention in the short run. New Keynesian theory is a branch of the neoclassical school and the methodological foundations are identical. There is nothing "new" or "Keynesian" with New Keynesian theory; it is merely a special case of neoclassical theory.
2. Heterodox economists would argue that economic decisions are rooted in, and guided by, their social and historical structure. Thus, none of production, distribution, or consumer behavior is isolated from their social environment. See J. H. Finch. "The Role of Grounded Theory in Developing Economic Theory," *Journal of Economic Methodology* 9, no. 2 (2002): 213–234.
3. On the other side of the methodological (and ideological) debate is heterodox economics. Heterodox economics diverges from the neoliberal tradition and is in stark opposition to contemporary neoliberal thought. Heterodox economic theory seems to hold steadfast to these principle tenets: (1) the economic system must be viewed as a non-ergodic historical process, (2) fundamental uncertainty is significant, (3) questions of production and distribution are important, (4) the workings of economic life do not take place in a vacuum, and (5) the economic process is a social process with social classes and

political institutions. Heterodox theory stems from a diverse collection of economists with differing and sometimes competing viewpoints; however, a survey of the heterodox literature seems to show that these five tenets remain fundamental. See for example see Holt 2007; Arestis 1996; Lawson 1994; and Hamouda and Harcourt 1990.

4. Traditional economic analysis is forward looking. Traditional economics forecasts a future state of the economic system from its initial state and from the postulated "laws of motion" of market-based economies.

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