Book Review: Full Employment Abandoned: Shifting Sands and Policy Failures by William Mitchell and Joan Muysken

Reviewed by Philip Lawn

Faculty of Social Sciences,
Flinders University,
Adelaide, Australia
E-mail: phil.lawn@flinders.edu.au

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This is one of the most important recent books on unemployment. In a nutshell, Mitchell and Muysken (M&M) convincingly demonstrate that unemployment is both morally indefensible and unnecessary. The book will, therefore, be of value to anyone interested in the unemployment debate; for anyone interested in the concept of social equity – since, as M&M explain, access to employment at a liveable wage is both a human right and the key to overturning the growing disparities between rich and poor; and for anyone whose understanding of macroeconomics and unemployment has been coloured by contemporary, mainstream, macroeconomic thought.

There are numerous illuminating aspects to this book. Three critical aspects stand out in my mind as lying at the heart of the misunderstanding on unemployment. The first is the widespread belief that central government deficits are inherently bad. Most people are of the belief that responsible economic management requires central governments to net save (i.e. generate budget surpluses) on the false premise that governments are as budget constrained as any individual citizen or private sector corporation. It is therefore argued that central government deficits reduce liquidity, drive up interest rates and lower private sector spending and investment. Hence, it is widely believed that central government deficits lead to a rise in unemployment.

M&M turn conventional macroeconomics on its head by demonstrating that central budget deficits exert downward pressure on interest rates. They show that the conventional wisdom regarding the interest rate impact of the government budget position reflects a gross misunderstanding of how the monetary system operates. In particular, they explain how economists and non-economists alike overlook the competition that occurs between the commercial banks as they attempt to rid themselves of excess reserves that, if the banks do nothing at the end of each trading day, earn a support rate less than the current market rate of interest. This competition between the banks exerts downward pressure on the short-term interest rate (overnight funds rate) that can drive the interbank rate below the operational target interest rate set by the central bank. In an effort to defend the desired target rate, the central bank must sell government securities to the commercial banks (i.e. drain excess liquidity by issuing government debt). The key point here is that a budget deficit increases the quantity of excess reserves, while a budget surplus reduces them. In so doing, a *budget deficit places downward pressure on the short-term interest rate* that must be matched by the issuance of government debt. So what appears as debt issuance to finance a budget deficit (the conventional budget constraint theory) is none other than an interest rate-defending response by the central bank.

The second critical aspect involves M&M's critique of the common argument that labour market clearances always lead to full employment – a key theoretical point underpinning mainstream views on unemployment. It is generally argued that unemployment exists either because (a) an institutional constraint prevents the real wage from falling to the market clearing rate, or (b) the gap between dole payments and market-clearing low wages is sufficiently small to provide low-wage workers with an incentive to withdraw their labour – that is, to voluntarily make themselves unemployed and claim unemployment benefits.

If unemployment is due to (b), it is argued that both the generosity of welfare payments should be reduced and the qualifying test for the receipt of unemployment benefits should be tightened. If unemployment is due to (a), the conventional solution is to deregulate labour markets to facilitate their smooth and rapid clearance. But as M&M explain, the proposed solutions to (a) and (b), which are key elements of what M&M refer to as the 'full employability' framework exemplified in the 1994 Organisation for Economic Cooperation and Development (OECD) *Jobs Study*, ignore the link between labour markets and product markets. It is merely assumed that employers are permanently willing and able to employ someone so long as the real wage is no greater than the marginal product of labour. But employ them to do what? Employing more labour is only profitable if the additional output generated can be sold in product markets.

Crucially, as M&M show, if a tax-paying private sector desires to net save, and the central government runs a budget surplus, then, by convention, effective aggregate demand will be insufficient to ensure that all output is sold in product markets. In these circumstances, the sale of all output will only occur if the central government engages in deficit spending. But just any budget deficit? That is, do M&M recommend traditional Keynesian pump-priming policies to eliminate unemployment? No, they do not. M&M propose the introduction of a Job Guarantee (JG) – a government offer of paid employment to anyone unable to find work – which not only ensures full employment but, if appropriately designed, can also overcome the concern that modern economists and policy-makers have with inflation and rising interest rates.

How would the JG prevent the emergence of inflation and rising interest rates? This brings me to the third critical aspect of M&M's book. It has already been highlighted that a central government budget deficit need not lead to rising interest rates. As for price inflation, M&M point out that the conventional approach involves demand-side manipulation of the economy to establish an inflation-stabilising ratio of unemployed labour to employed labour. The unemployment rate applicable to this ratio is referred to as the 'non-accelerating inflation rate of unemployment' or the NAIRU. The down side of a NAIRU policy is obvious – it implies the need for a sacrificial pool of unemployed labour to maintain price stability.

Ingeniously, M&M adopt the same NAIRU logic to explain how a JG can be instituted without causing an excessive rate of price inflation. M&M begin by pointing out that a central feature of the JG is the payment of a minimum liveable wage to JG workers. The payment of a minimum wage establishes a wage floor for the economy, thereby ensuring: (a) the government never competes with the private sector for labour; and (b) there is no distortion of the relative wage structure. Secondly, M&M ask the reader to imagine a NAIRU that typically involves a substantial unemployment rate (let's assume 6% of the labour force). The government then introduces the JG to remove all but frictional unemployment. Under the NAIRU scenario, the increase in aggregate demand caused by the boost in government spending leads to an accelerated rate of price inflation. To control this, the government deflates the economy via the use of fiscal or monetary policy measures. This, in turn, reduces the number of people employed in the private sector. People who lose their jobs in the private sector subsequently obtain paid work under the JG programme. This process is continued until an inflation-stabilising ratio of JG workers to conventional workers is reached. This ratio is referred to by M&M as the 'non-accelerating inflation buffer employment ratio' or the NAIBER. The difference between the NAIBER and NAIRU approaches is very clear – while the former achieves price stability in the presence of full employment, the latter does not. This constitutes a very powerful argument in favour of the NAIBER approach and undoubtedly forestalls any inflation-based argument that might otherwise be raised by NAIRU advocates against the JG.

M&M then proceed to explain why they believe the NAIBER would be lower than the NAIRU. This is a very important consideration given that a NAIBER above the NAIRU would entail some workers having to suffer a wage cut equal to the difference between their private sector wage and the minimum JG wage. I found the arguments put forward by M&M convincing, although I could not help but think they were more applicable to the medium-term and long-run and that a NAIBER above the NAIRU is almost inevitable in the short-run. Having said this, a JG ensures the immediate receipt of a liveable income for all previously unemployed citizens and, if the NAIBER is eventually lower than the NAIRU, more people ultimately on a higher private sector wage. This, to me, is an undeniably more equitable and desirable outcome than the NAIRU circumstance.

There are a number of other positive elements about the JG that M&M raise in their book and word limits preclude me from expanding on all of them. There are two benefits that are worth elucidating. The first is that the JG programme can be tailored to produce and deliver goods and services not currently generated by the private sector (i.e. those with public goods characteristics). Hence, as M&M stress, there would be few, if any, instances where JG activities would encroach on private sector activities. If anything, the JG would boost private sector activity by enhancing the stock of publicly provided infrastructure.

Secondly, the JG can allay all concerns about how large the government deficit needs to be to generate and maintain full employment. This is because the level of deficit spending is always just enough to eliminate unemployment – no more, no less. Indeed, because of the targeted nature of the JG, the size of the budget deficit required to achieve full employment is determined by the spending levels of the private sector, not by the central government. That is, if private sector spending is buoyant and conventional unemployment is low, the budget deficit is small. Conversely, when private sector spending falls during an economic downturn and conventional unemployment is much higher, the budget deficit is larger. Hence, the JG would act as an ideal countercyclical policy instrument to limit the magnitude of the boom-bust cycle.

There is, however, one concern that I have about the JG. It does not in any way devalue its potential role as a means of guaranteeing full employment, nor undermine the value of this book. The concern relates, in part, to the fact that I am an ecological economist, not a labour economist. Ecological economists believe there are severe ecological limits to the growth of real GDP which may have already been exceeded in many countries. Assuming that a nation is situated on an ecological precipice, it is possible that the introduction of a JG, which would initially increase real GDP, could tip a nation's economy into unsustainable territory. Because the JG can be implemented with public goods in mind, it is certainly possible to design JG activities in a way that generates positive environmental outcomes. But these, alone, are unlikely to guarantee ecological sustainability in the same way they can guarantee full employment. To simultaneously achieve full employment and ecological sustainability, the JG will need to be complemented by a range of sustainability policies.

But here, I think, is where the JG can play an even more valuable role than that envisaged by its architects. Should sustainability policies involve constraints on the rate of resource throughput to ensure it remains consistent with the regenerative and waste assimilative capacities of the ecosphere, and this subsequently limits the rise in real GDP (though not necessarily the rise in economic welfare), the JG could serve as a critical rationing device in an ecologically 'full' world. By this I mean that the JG could equitably ration paid work to the extent required to achieve and maintain full employment in circumstances where ecological limits render the stimulation of aggregate demand untenable.

Overall, there is little to fault this book. M&M have produced a well-written and eminently accessible piece of work replete with highly relevant empirical evidence and real-world examples. More than this, it is a book that will forever alter one's perceptions of macroeconomics, government deficits, fiscal and monetary policy, the causes of unemployment and what can be done by a currency-issuing central government to achieve and maintain full employment. For this reason, I believe it is compulsory reading for anyone concerned about unemployment, social equity and appropriate macroeconomic management.