The Unbalanced Economy: Business Domination as the Real Constraint on Egalitarian Policies

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Andrew Glyn concludes that "we should beware of blaming the narrow scope for egalitarian programs mainly, let alone exclusively, on internationalization." This is a conclusion that I agree with. However, at the same time, I am less than fully persuaded about the completeness of his argument, particularly as it applies to the U.S. economy. Glyn identifies five internal constraints on an egalitarian economic policy: (1) sluggish private capital accumulation, (2) conflicting claims, (3) government deficits, (4) financial markets, and (5) taxation and the costs of expansion. Each of these items sounds familiar. It is as if nothing fundamental regarding the economy's structure has changed since the early 1970s. In varying degrees, each of these constraints was present then, and the implication is that the only barrier against returning to the relatively more egalitarian economic outcomes of that period is changed political climate. This is a conclusion I would not feel comfortable with.

Though globalization is not the key factor, it has contributed something to the deterioration of economic equality. Moreover, the forces driving globalization are part and parcel of the forces that are the cause of increased inequality. For this reason, it is worth briefly examining the characteristics of globalization.

Globalization has created a "leaky" economic environment in which it is difficult to conduct effective economic policy. Three different types of leakiness can be identified:

(1) Macroeconomic leakiness. This type of leakiness has emerged because of increased international trade. In the U.S., between 1966 and 1995, exports and imports as a share of GDP increased from 7.4% to 18.7%; in the U.K., they increased from 29.0% to 45.9%; in Canada, they

increased from 33.6% to 63.7%; for the G-7, the country weighted share increased from 18.3% to 28.3%. If a country now expands its level of economic activity, consumer demand leaks out through imports potentially creating an unsustainable balance of payments deficit. This has afflicted almost all the industrialized countries except the U.S. The latter has been protected by the fact that the dollar is the international reserve currency, and by the fact that foreigners have wanted to build up their portfolio holdings of U.S. assets.

(2) Microeconomic leakiness. This type of leakiness is the result of the new conditions of production. Jobs leak overseas if labor market conditions aren't sufficiently flexible, or if relative profit tax rates aren't sufficiently favorable. This has created a climate in which business has been able to intimidate labor by threatening to move unless granted wage concessions. Business has also been able to intimidate government by demanding tax concessions, and the burden of taxation has therefore been increasingly shifted from corporations on to households.

(3) Financial leakiness. This is the result of increased integration of financial markets. Financial capital now flees those countries pursuing expansionary monetary policies which lower interest rates. This is because rates elsewhere become more attractive, and finacial capital is also resistant to any hint of inflation. As a result, financial capital can veto expansionary policy by threatening to "vote with its feet".

The increase in leakiness is the result of two forces. First, policy makers have systematically encouraged greater leakiness by liberalizing trade, encouraging export led growth, encouraging multi-national corporations, promoting foreign direct investment, and abolishing or suspending capital controls. Second, leakiness has increased owing to forces internal to the market. Thus, technological and organizational change have increased the mobility of both physical and financial capital. The multi-national corporate form is now common place, and a new corporate form predicated upon global sub-contracting is emerging. Meanwhile, national financial markets are more closely integrated owing to multinational banking firms, real time electronic communication and improved money transfer technology.

These developments are the natural outgrowth of market forces, and represent the systemic workings of a dynamic capitalist economy. Business seeks to maximize and grow profits, and it does this through innovation. This innovation takes two basic forms. Firms can seek to gain a competitive advantage over rival firms by capturing a greater share of the existing market or creating a new market that destroys the old. Alternatively, they can innovate in a way that redistributes income from labor to capital. In this latter case, rather than growing the pie, business redistributes the pie. Both forms of innovation involve organizational and technological innovation. They can also involve political innovation whereby corporations capture government policy and change existing laws and regulation so as to gain an advantage over competitors and over labor.

Organizational, technological and political innovation are clearly evident in the process of globalization. The political dimension is evident in the passage of NAFTA and the Uruguay round of the GATT, and it is evident in business advocacy of renewal of presidential "fast track" negotiating authority and passage of the Multilateral Agreement on Investment. However, these three types of innovation have also operated longer and more forcefully within the domestic economy.

Within the U.S. economy, the increased mobility of capital and the new organizational forms that facilitate globalization have long been evident in the competition between the "rust belt" and the "sun belt". Thus, firms have repeatedly either moved or threatened to move from the high wage unionized rust belt to the low wage ununionized sun belt in order to increase profits at the expense of wages and to bust unions. The same tactic of either moving or threatening to move has been used to win tax concessions from state governments.

With regard to political innovation, it is no accident that the real value of the minimum wage and the real value of welfare payments have been allowed to fall, since these measures contribute to establishing a "wage floor" that underpins market wages. It also explains why uninsurance benefit coverage rates have declined. The National Labor Relations Board has been increasingly understaffed, with dispute settlement times lengthening. Workers rights to organize have been de facto denied by laws that are inadequate to the task of protecting against corporate intimidation during unionization drives. Right-to-work legislation has also spread at the state level, thereby undermining the possibility for effective unions.

Globalization is being driven by the same forces that produced these domestic outcomes. One reason why it is important is because it aggravates these tendencies. More importantly, globalization is a harbinger of worse things to come if we don't fix the underlying problem of an unequal balance of power. It also threatens to engender institutional "lock-in" whereby fixing the problem will become increasingly difficult as new systems of production and patterns of trade become entrenched.

Unfortunately, Glyn's paper makes little mention of the microeconomic structural constraints on acheiving a more egalitarian economic outcome. These constraints are domestic in origin, and globalization is extending them to the international economy. It is in this sense that globalization is not the source of our difficulties, though it is important because it aggravates existing constraints by giving them an international dimension.

Andrew Glyn was an early critic of mainstream liberal Keynesian economics. Paradoxically, his own analysis could easily have been written by a liberal Keynesian. Liberal Keynesianism, which dominated in the twenty five years after World War II, believed it had solved capitalism's economic problems through the policy of demand management. Glyn's focus is on domestic constraints on aggregate demand, and how globalization may have aggravated them. His one structural concern is the possibility of competing claims inflation should we ever get to full employment.

I suggest that given the current imbalance of power between labor and capital, expanding aggregate demand and lowering unemployment will not solve economic inequality and nor will it produce conflicting claims inflation. Thus, the current U.S. economic expansion has seen the unemployment rate fall to a twenty three year low of 4.8% without a whisper of increased inflation. Indeed, inflation has actually been falling. Meanwhile, real hourly wages of production and non-supervisory workers (i.e the 80 percent of the workforce who are non-managerial) remain below the level of the last business cycle peak obtained in 1989.

There is no doubt that Keynesian demand management is a necessary part of the solution. However, it can only work effectively if the appropriate structure is in place. Keynesian demand management policy must therefore be supplemented by policies that get the structure right, and structure is the real constraint on a successful egalitarian economic program. Fixing this structure requires appropriate policies regulating business conduct, international money markets, and labor markets. These policies must preserve the incentive to enterprise, while preventing capital from adopting a "low road" strategy that generates inequality of income and economic insecurity for working families.

With regard to the U.S. economy, there is a need to design rules for international trade that prevent a race to the bottom; regulation that prevents tax competition between states and ultimately shifts the burden of taxes from corporations on to households; and appropriate labor market and welfare laws that deliver on workers' rights to organize, ensure that wages are not subject to dogeat-dog competition, and ensure effective counter-vailing power to that of business. In the realm of fiscal policy, taxation must be progressive and contain built-in stabilizers that help mitigate the swings of the business cycle, while government must invest in the nation through infrastructure and education spending. Lastly, monetary policy must be conditioned on the economic interests of working families rather than those of Wall Street, and this means breaking with the notion of a natural rate of unemployment and the policy goal of zero inflation. All of the above apply to some degree for Europe, but there is also the additional need to control financial capital vetoing economic policy by voting with its feet.

If we manage to implement the above policies, the problem of aggregate demand will automatically diminish of its own accord. Moreover, when a need for aggregate demand stimulus does emerge, the constraints on such a stimulus will also have largely disappeared. Lastly, aside from the period of the OPEC oil shocks, the U.S. economy has never really had conflicting claims inflation. In some European countries, there is more evidence of this phenomena. However, learning from the past, the modernization of the European trade union movement, and the denationalization of large chunks of industry with its accompanying removal of soft budget constraints for these industries have likely significantly reduced its extent.

Brief biography

Dr. Thomas I. Palley is Assistant Director of Public Policy (Economics) at the AFL-CIO in Washington D.C. He has a B.A. degree from Oxford University, and a M.A. degree in International Relations and a Ph.D. in Economics, both from Yale University. He has published extensively in numerous academic journals. Post Keynesian Economics; Debt, Distribution and the Macroeconomy was published in 1996 by St.Martin's Press. His forthcoming book title Plenty of Nothing: The Downsizing of the American Dream and the Case for Structural Keynesianism will be published by Princeton University Press in January 1998.

| .The thoughts expressed in this brief comment are fully explored in my book Plenty of Nothing: The Downsizing of the American Dream and the Case for Structural Keynesianism, Princeton University Press, 1998.