Mitchell’s Musings 7-7-14: All Incomes Are Not Created Equal

Daniel J.B. Mitchell

Our prior musing dealt with results from the California Field Poll on how folks felt about the general state of affairs in the U.S. As noted in that musing, polls are suspect when they get into detailed questions about specific public policies. Typically in those cases, pollsters have to explain the policy because most people don’t follow such matters in detail. The ways in which the explanations and questions are presented have a major impact on the responses. However, when the questions are general, attitudes are likely to be reasonably detected.

Table 1 on the final page of this musing shows the results concerning attitudes about income inequality among the California adult population.¹ A majority of adults are dissatisfied with income inequality. But beyond that simple observation, there are surprises. Immigrants, who are often at the lower end of the income distribution (especially Latinos), are less worried about income inequality than other adults. Presumably, the still-lower income level alternatives in their native countries influence the responses. Strongly conservative and strongly liberal respondents are more concerned about inequality than others so both (extreme) sides of the political spectrum are more concerned than centrists. Young people (age 18-29) are less worried about it – despite their well-publicized job problems, issues of college debt, etc. – than are other adults. Lower income respondents are less dissatisfied about inequality than others.

I came across this poll a few days ago. More recently, a reference appeared in the Huffington Post, ostensibly about what amounts to a push-poll aimed at showing that people generally (not just in California) are fed up with “government.”² Despite the pushiness of the poll, I have no doubt – based on the better poll discussed in our prior musing – that there is much concern about the overall state of affairs. The object of the poll discussed in the Huffington Post was to support a new political movement to be termed “We Need Smith,” a reference to the old (1939) Frank Capra Hollywood film “Mr. Smith Goes to Washington.” In that film an ordinary man is selected as a U.S. senator and confronts the political obstructions of the era.³ Although almost defeated by corruption, he is vindicated of false charges and his efforts in the Senate to push construction of a camp for boys advance.


²http://www.huffingtonpost.com/2014/07/03/we-need-smith_n_5554830.html. A link to the poll is in the article.

³Plot summary of “Smith” from imdb.com: The governor of an unnamed western state, Hubert “Happy” Hopper (Guy Kibbee), has to pick a replacement for recently deceased U.S. Senator Sam Foley. His corrupt political boss, Jim Taylor (Edward Arnold), pressures Hopper to choose his handpicked stooge, while popular committees want a reformer. The governor’s children want him to select Jefferson Smith (James Stewart), the head of the Boy Rangers. Unable to make up his mind between Taylor’s stooge and the reformer, Hopper decides to flip a coin. When it lands on edge and next to a newspaper story on one of Smith’s accomplishments he chooses Smith, calculating that his wholesome image will please the people while his naiveté will make him easy to manipulate. Smith is taken under the wing of the publicly esteemed, but secretly crooked, Senator Joseph Paine (Claude Rains), who was Smith’s late father’s oldest and best friend, and he develops an immediate attraction to the senator’s daughter, Susan (Astrid Allwyn). The unforgiving Washington press quickly labels Smith a bumpkin, with no business being a senator. Paine, to keep Smith busy, suggests he propose a bill. Smith comes up with legislation that would authorize a federal
Although “Mr. Smith” has a satisfying Hollywood ending, the notion that generalized dissatisfaction can be harnessed in some predictable way is an illusion. Hollywood produced another Frank Capra film – “Meet John Doe” (1941) – which may be more to the point.4 (Both “Smith” and “Doe” are available on YouTube in full and for free.) In the “Doe” case, an ordinary man runs for President, backed by a group that expects to control him. They see him as an appealing front man. But the scheme goes awry. The film has a more ambiguous ending than “Smith.”5 While the bad guys are ultimately unable to use the
government loan to buy some land in his home state for a national boys’ camp, to be paid back by youngsters across America. Donations pour in immediately. However, the proposed campsite is already part of a dam-building graft scheme included in a Public Works bill framed by the Taylor political machine and supported by Senator Paine. Unwilling to crucify the worshipful Smith so that their graft plan will go through, Paine tells Taylor he wants out, but Taylor reminds him that Paine is in power primarily through Taylor’s influence. Through Paine, the machine accuses Smith of trying to profit from his bill by producing fraudulent evidence that Smith owns the land in question. Smith is too shocked by Paine’s betrayal to defend himself and runs away. However, Smith’s chief of staff, Clarissa Saunders (Jean Arthur), has come to believe in him, and talks him into launching a filibuster to postpone the Works bill and prove his innocence on the Senate floor just before the vote to expel him. While Smith talks non-stop, his constituents try to rally around him, but the entrenched opposition is too powerful, and all attempts are crushed. Due to influence of the Taylor “machine”, on his orders, newspapers and radio stations in Smith’s home state refuse to report what Smith has to say and even twist the facts against the Senator. An effort by the Boy Rangers to spread the news results in vicious attacks on the children by Taylor’s minions. Although all hope seems lost, the senators begin to pay attention as Smith approaches utter exhaustion. Paine has one last card up his sleeve: he brings in bins of letters and telegrams from Smith’s home state from people demanding his expulsion. Nearly broken by the news, Smith finds a small ray of hope in a friendly smile from the President of the Senate (Harry Carey). Smith vows to press on until people believe him, but immediately collapses in a faint. Overcome with guilt, Paine leaves the Senate chamber and attempts to kill himself with a gun. When he is stopped, he bursts back into the Senate chamber, loudly confesses to the whole scheme, and affirms Smith’s innocence.

4 The “Doe” film – including a suicide element in the plot – appears to be inspired by California’s pensionite and other political movements of the 1930s.

5 Plot from imdb.com: When reporter ANN MITCHELL is laid off by managing editor HENRY CONNELL because of streamlining, she begs to stay on since she’s supporting her MOTHER and TWO SISTERS, but it’s no use. Angry, she gathers up her belongings but then, as a parting shot, types up a fake letter from “John Doe” stating that he’s so downtrodden by the unfairness of things that he intends jumping off the building on Christmas Eve. The paper prints the letter and it causes a sensation. Everyone relates to and wants to help John Doe. Connell, desperate to get hold of the original letter is shocked when Ann tells him there was no letter. Connell, angry, is ready to print a retraction but Ann suggests that they hire a “fake John Doe” to embody the pathos of the letter. She gets her job back along with a lucrative fee and contract. Several desperate MEN line up claiming to have written the letter, so Ann and Connell must now pick the one. When handsome JOHN WILLOUGHBY walks in, Ann’s clearly smitten. A likeable, quiet baseball player who’s fallen on bad times, John’s the one who will become “John Doe.” Although he seems too honest to lie, Ann believes he’s desperate enough. They create a fake letter; put him up at a fancy hotel with bodyguards, making him sign an agreement. Also in tow (much to Connell’s chagrin) is THE COLONEL, a confirmed vagabond, distrustful of society, who warns John that he’s falling into a trap of privilege. Next come publicity photos, which are directed by Ann to get the correct “angry protest” look. With headlines proclaiming his anger at the unfairness of the world, John becomes an increasing media sensation, courtesy of hyperbolic headlines concocted by Connell. Meanwhile, the GOVERNOR suspects John Doe is a myth but mistakenly feels it was concocted by publisher B. D. NORTON to discredit him. Ann convinces Norton to play it for what it’s worth. Norton offers her money to write radio speeches to sell Doe. He also wants her to work directly with him and not Connell. Ann goes to work, typing up a storm but nothing comes to mind. Ann’s Mother suggests that she write something upbeat and simple, using the values of Ann’s late father as an inspiration. By now, John has begun realizing that his baseball career might not get started again if the John Doe business is revealed as a phony. Nonetheless, John reads his first manufactured upbeat speech, written by Ann to a packed house. Ann coaches him to be sincere, suggesting that she’s fallen in love with John Doe. The speech, broadcast on the radio, stirs the people with its “love thy neighbor”-style message. CROWDS love him but John can’t get away fast enough. He and the Colonel resort to the boxcars and flee. B. D. Norton, thinking he was great, wants him located. When a DINER WAITER recognizes him, John’s hope for a return to normalcy is squelched by sudden CROWDS, eager to meet him. Ann and Norton locate him. John isn’t happy about it. When Norton offers him a lecture tour, he refuses it angrily. When the common PEOPLE who have a “John Doe” club talk to him, however, he softens when hearing how he’s touched them. Now, John’s torn. His itinerant pal, The Colonel, thinks he’s been “hooked” and, disgusted, walks out on him. Norton arranges the lecture tour. John speaks in state after state, addressing the many national clubs in his name. Connell tells Norton, however, that he’s curious why Norton is spending so much money on the tour. In the meantime, Ann, knowing that John now likes her, feels increasingly like the heel she feels she is. She feels even worse when John relates a tender dream that he had about her and talks to her about how he relates to the lonely, hungry people to whom he’s been speaking. Norton gives Ann a fur coat and a gift. He then tells her that he

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ordinary man for their nefarious purposes (the Hollywood code of that era prevails), the film ends with a vague promise that maybe someday things will be better.

So what lesson should we take away from the films? It isn't that good eventually triumphs over evil ("Smith") and the needs of the ordinary person will prevail. It is that mobilizing generalized discontent can indeed produce political consequences. But the notion that either groups on the left or the right can predictably use discontent and control it for their own agendas is an illusion. And the results you get may not be happy endings. Indeed, there may be no results at all ("Doe") or worse. If you want to be worried about growing inequality and generalized loosely-related anxiety about how “things” are going, that should be your concern. Ultimately, the political system may respond badly or not at all.
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Mitchell’s Musing 7-14-14: The California State Budget: Will a Rainy Day Fund Fix It?

Daniel J.B. Mitchell

The Great Recession caused fiscal distress to most state and local governments. Any time the economy turns down, tax revenue will also fall. If the downturn is large, the drop in revenue will also be large, although the magnitude of the drop will vary with the type of taxes on which the government in question depends.

California, as the largest state in the nation, received substantial national attention as it went through its most recent budget crisis. The state had a prior budget crisis in the early 2000s as a result of the downturn then and the bursting of the dot-com bubble. One consequence of that episode was the replacement of Governor Gray Davis in the early part of his second term by recall. Movie celebrity Arnold Schwarzenegger took his place, promising to fix what ailed Sacramento. Schwarzenegger, because of his movie star status, attracted even more attention to California’s fiscal woes than might otherwise have been the case.

In the end, however, Schwarzenegger’s two terms – which ended during the budget crisis that followed the Great Recession – left him equally unpopular as Davis was when he was recalled. Schwarzenegger was followed as governor by Jerry Brown in the general election of 2010; Brown had been governor for two terms during the 1970s and early 1980s. In his earlier iteration, Brown had been an eclectic, “new age” governor who saw himself as a fiscal conservative. His view in his earlier iteration (and in his second coming) focused on building up a healthy reserve in the state’s General Fund to cushion against future downturns.

Now a state or local government can save for a rainy day simply by spending less than it takes in. Such a policy will increase the General Fund reserve, a de facto rainy day fund. However, this time around, Brown wants voters in the upcoming general election to approve a formula-driven rainy day fund beyond the official reserve. One could argue that no such fund is needed since the dollars that would be accumulated could just as well accumulate with the conventional reserve. Moreover, the voters over the years have approved other formulas, notably Prop 98 in the late 1980s which drives K-14 spending. There is a case to be made that there are already more than enough formulas in California budgeting.

However, let’s put that argument aside and assume that a) Brown himself will be re-elected this fall and that b) his rainy day fund ballot proposition will be approved. Both outcomes seem very likely. The popularity of the governor is a function of a voter sense that things – primarily the budget - are being taken care of in Sacramento in an orderly process. Right now, despite various administrative issues for which Brown could be criticized, all seems well regarding the budget. Moreover, Republicans in the state have marginalized themselves to the point that whatever shortcomings there may be in Brown governance, their voice is not being heard except among party loyalists.

As for the rainy day fund proposition, since Brown is popular and Brown says he endorses the concept, voters will almost assuredly approve it despite concerns among policy wonks about too much formula-
driven budgeting. In any event, assuming Brown’s re-election and approval of his rainy day fund, is California out of the woods? The answer, unfortunately, is that it wouldn’t take much of a future downturn to upset the state budget. Thus, the economic pain of public sector layoffs and cuts to education, social programs, etc., could easily be revisited.

Let’s first look back at Brown’s first iteration as governor. As the figure below shows, under Brown the reserve in the General Fund back then built up to almost a third of the state budget. But then came the combination of Proposition 13 of 1978, which drastically cut and capped local property taxes, and a period of recession in the early 1980s. Due to Prop 13, the state had to bail out local governments, especially school districts. It initially could do so, thanks to Brown’s *de facto* rainy day fund. But then recession hit, further depleting the reserve.

![End-of-Year Reserve as Percent of Expenditures](image)

Even if we start with fiscal year 1979-80, when the reserve was about 15% of the budget, the reserve had disappeared into negative territory in a couple of years. In short, a rainy day fund can be depleted very fast and can only be a short-term cushion.

It’s unlikely that California will see a reserve of a third of the budget, or even 15%, any time soon. How much can be expected under the Brown plan. Official budget projections going out to 2017-18, *which assume no recession*, are shown on the figure on the next page. Historical precedent suggests that such continuous linear grown is unlikely (but not impossible). However, the figure shows that total reserves (regular reserve plus rainy day fund) under that scenario will rise to 5% of the budget. It wouldn’t take much of a setback to blow out 5%.
Note also that total reserves as a percent of the budget actually dip during the current fiscal year (2014-15). So although reserves remain positive, the official estimates have them dropping as a percent of the budget – and in absolute terms. That is, the projection for this year is that spending will exceed revenue. Only in subsequent years do total reserves begin to increase.

There is a caveat. Brown’s strategy with the legislature is to insist on conservative estimates of revenue during budget making to constrain spending. When the now-concluded 2013-14 budget was enacted, it assumed over $5 billion less in revenue than actually appeared. Possibly, there will be another positive revenue “surprise” during the current year. Even so, however, the projections above forecast a much more moderate level of reserves by 2017-18 than Brown had accumulated during his first iteration as governor. And we know how rapidly those funds disappeared.

The lesson is that, as a practical matter, rainy day funds of the magnitude currently being sought might buy a single year for an adjustment, assuming significant budget cuts were made during that year. If you are thinking of a rainy day fund as an umbrella over the budget, it is a leaky umbrella at best. The fact that the current fiscal year’s official figures forecast what in normal parlance would be called a deficit (income < outgo) is also not encouraging. As recalled Governor Davis can attest, a deficit at the peak is dangerous. Things can only get worse. Of course, no one knows for sure if 2014-15 will be a peak. But what if it is?

Hate to rain on your parade.
Mitchell’s Musings 7-21-14: Coordination Failure or Success?

Daniel J.B. Mitchell

Economists have long had the concept of a “coordination failure,” often applied in the context of negative externalities that could be avoided if only there was a coordinator. A classic example is overfishing. It is rational for each fishing boat to maximize its catch, even if the collective result is to deplete the stock of fish available in the future. However, all would be better off if there was a regulator that collectively restricted the amount of fishing allowed by each boat.

In the case above, the failure to coordinate produces a bad result. But there are forms of coordination that potentially produce bad results for society even if they produce good results for a subset of participants. For example, if competitive firms find a way to collude, e.g., a cartel of some type, the firms involved are likely to be better off. But consumers will be worse off and a suboptimal level of production will occur to keep the price high.

At the time of the 1992 Los Angeles Riots, it was argued that television acted as a coordinator for looting. Local TV showed that the police were not able to respond. Indeed, the greater the number of looters, the less the police are able to respond. So, at a point, the number of looters becomes self-encouraging. Coordination (by TV) produced a societal loss.

It is likely that phenomena that occur in waves have aspects of implicit coordination. Crime rates go up and down and the usual suspects of explanations such as demographics don’t explain the fluctuations, or don’t completely explain them. If there is more crime, the effectiveness of the police declines and the word gets out that the probability of getting caught has fallen – which makes committing a crime less risky. It is as if a coordinator had organized potential criminals to commit more crime simultaneously, again benefiting them but not society.

One suspects that the current influx of unaccompanied children as immigrants to the U.S. has elements of a de facto coordinator. The influx is attributed in the news media to rumors in Central America that the U.S. had softened its immigration policy. Regardless of the truth of that rumor – and there is some disagreement as to whether a policy change occurred – once lots of people begin coming, the immigration system becomes overwhelmed. It is as if a coordinator told potential immigrants to come en masse and at the same time. When the system becomes overwhelmed, word gets back that as a practical matter policy has softened and the process repeats.

Bubbles in financial markets have similar explanations. Prices will go up if demand for assets increases. Asset holders are better off if their assets gain in value but normally they can’t act collectively to bid up prices. However, if there is something that starts a rise in the market consensus price, the gain in asset value as the price goes up triggers momentum trading. The price begins going up because it is going up. The process becomes self reinforcing.
All of the examples above involve a kind of coordination without an explicit coordinator. No one is producing mandatory regulations affecting behavior. Unlike the fishing story, where an explicit legal regulator comes in and limits the catch to some mandatory quota, events and observations instead act as coordinators. An interesting question is whether there are counterparts to these tales in the labor market.

One of the puzzles of the early 21st century has been the drop in labor force participation and the employment-to-population ratio. Both are shown below as Figures 1 and 2. Both ratios have the same base, the civilian non-institutional population age 16 and over. But the participation rate includes both employed and unemployed persons in the numerator while the employment-to-population includes only the employed. The employment-to-population ratio is very sensitive to the business cycle and can be seen to be more erratic. Since the participation rate has the sum of employment (which falls in recession) and unemployment (which rises in recession), it is smoother and less affected by the business cycle.

Figure 1: Employment-to-Population Ratio (percent), Seasonally Adjusted

Figure 2: Labor Force Participation (percent), Seasonally Adjusted
Both indexes show a reversal in the early 2000s of the secular upward trend that began in the 1960s and is largely the result of more women coming into the workforce. There are many explanations that can be offered for that rise including the birth control pill and changing norms around the idea of women – particularly women with children – working outside the home. But the question is why did norms change? One possibility is that norms are based on what others are doing. So if more women are in the workforce, the norms shift to “society” expecting women to work.

If the rise in workforce activity had bubble-like elements – i.e., an implicit coordinator – then like other such phenomena at some point the bubble bursts. In this case, the reversal of the labor market bubble seemed to terminate with the end of the dot-com financial bubble. Jobs become less available and the word gets out. You begin to hear about “discouraged” workers, those folks who stop seeking work because they believe none is available. The bursting of the subsequent housing bubble added to downward trend shown on Figures 1 and 2.

In the period after the Great Recession, not only was there much talk about discouraged workers but also about a “New Normal” in which jobs allegedly would forever be harder to get because you needed new skills. On the demand side, employers were said to be cautious about hiring or some other story was offered about why employers should not be hiring. New Normal type stories can also be self-reinforcing. One thing we know employers do is to find out what other employers are doing. Benchmarking is the term of art for that tendency. If there is said to be a New Normal in which hiring should be more limited than in the past, then there will be such a New Normal.

It is interesting that the two drops in workforce activity rates occurred in conjunction with two financial bubbles: dot-com and housing/mortgage. Perhaps financial reversals are more dramatic that other types of economic downturns and command more attention. Suddenly, your wealth evaporates. Suddenly, you house is worth less than your mortgage.

In any event, if my interpretation is correct, i.e., that there is de facto coordination on both sides of the labor market which is currently impeding recovery, then you need an explicit coordinator to counteract it. In essence, that is what macroeconomics and macro policy is all about. It’s about trying to create conditions in which expectations about a New Normal of scarce jobs is replaced by a New-New Normal that, if anything, tilts toward labor shortage. Other than at the Federal Reserve, with its low interest rate policy, there hasn’t been much done of late to achieve a New-New Normal. Just as dramatic events created new pessimistic expectations, something dramatic is needed to create a reversal of expectations.

We learned from the Great Depression that hoopla is not enough to change pessimistic expectations. Back then there were parades, movies, and other efforts to reframe the situation. [https://www.youtube.com/watch?v=4jiUu8od_18] Those kinds of approaches don’t work. The one thing that is left is the fiscal approach, as John Maynard Keynes pointed out at the time.

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6 NRA in this video stands for National Recovery Act of 1933 (not National Rifle Association).
Mitchell’s Musings 7-28-14: Productive Impressions or Official Data?

Daniel J.B. Mitchell

In recent times, much has been said about technology being “disruptive” as if this was a new idea. Yet the modern era has been characterized by a stream of innovations that led to disruptions. Look at pictures from the 19th century of city streets and you will see horse-drawn vehicles. Then the automobile came along and the horses disappeared. One could go on and on: electricity, steam power, broadcasting, movies, airplanes, the telegraph, railroads, etc.

One explanation for the impression that we are living in a time of unprecedented technological disruption is that the particular disruption we are having involves information and, more specifically, publishing. Journalists write about their own predicament caused by the Internet. The myriad telephone operators who were displaced by dial phones didn’t have a platform on which to publicize their predicament.⁷

There are measures of productivity available. I’m not going to argue here that such measures are without flaws. In fact, if anything, what flaws there are probably tilt toward methodologies that exaggerate current productivity relative to the past. Government statisticians do not operate in isolation. If politicians and commentators just “know” that productivity is rising particularly fast nowadays – “Look at my cell phone!,” they might say – efforts are made to take account of the latest innovations.

As a practical matter, no one goes back to make sure that the historical productivity data properly accounted for, say, tubeless and then radial tires. But old timers like me can tell you that experiencing a tire blowout in a tube tire car was an experience not worth having. No one goes back and looks at whether the indexes properly accounted for FM, TV, color TV, long-playing records, or polio vaccine.

Anecdote: When I was about eleven years old, someone gave me a “portable” radio. Portable is in quotes because to use this vacuum tube/wooden cabinet radio with batteries required two large 45 volt batteries and two large 4.5 volt batteries. With the batteries in it, the radio was like a heavy suitcase in weight. In fact, the radio had a leather handle which broke under the strain. Moreover, the batteries were expensive and wore out quickly because vacuum tubes represented a significant drain. In those days, although car radios were common, parking your car and leaving the radio going would kill your car battery after a few hours. Then transistors

⁷ https://www.youtube.com/watch?v=ClDw75mUI6c. At the time, the displacement of telephone operators by dial services was seen as a sign of how disruptive technology could be.
came along and suddenly portable radios could fit in your pocket and were cheap to operate. Car radios no longer killed car batteries.

Even in old Hollywood movies from the 1930s, and certainly in modern films that take place back then, if someone turns on a radio, it comes right on. But vacuum tube radios did not come right on. Rather they would hum for awhile as the tubes heated up. Then the sound would fade in. Transistors changed all that so radios do turn on instantly. But in Hollywood films, no one wants to waste a minute or so waiting for radios to warm up, hence the fiction that they always could operate immediately.

I was reminded of all of this recently when someone sent me a YouTube link to the first Telstar satellite broadcast. Until the early 1960s, although voice could be sent across the ocean by phone cable or shortwave broadcast, moving pictures could not be transmitted. Telstar was a breakthrough that changed the situation.

Telstar was a satellite capable of receiving and forwarding TV signals. It was not geosynchronous and so as it orbited the Earth, there were only brief intervals during which a signal across the Atlantic was possible. When it was launched and readied in 1962, two demonstration broadcasts were arranged. One was a U.S. broadcast to Europe showing such scenes as the Statue of Liberty, Mount Rushmore, and the Golden Gate Bridge. You can see it at https://www.youtube.com/watch?v=0iX7vC4Ts_A. Then, after an interval allowing the satellite to come back into range, there was a Europe-to-U.S. broadcast. (Unfortunately, I couldn’t find that one on YouTube.)

The Telstar satellite was seen as so remarkable that a hit instrumental record entitled “Telstar” topped the charts with sound effects that were intended to sound like a rocket taking off: https://www.youtube.com/watch?v=Q5TB3kUdw-0. Decades later, Walter Cronkhite, one of the TV newscasters on the original Telstar broadcast, talked about the event on NPR:

8 The first ten or eleven minutes of the video consist of reminiscences by a technician from the North Dakota TV station that was responsible for the Mount Rushmore segment. You can skip ahead if that doesn’t interest you to the actual broadcast. All did not go entirely smoothly. There was supposed to be a side-by-side image of the Statue of Liberty and the Eiffel Tower but it didn’t work. In some spots, there were other technical difficulties, notably a tendency for the horizontal hold to break as the scene shifted from one location to another.

9 Later, lyrics were added and the record was released under the title of “Magic Star.” https://www.youtube.com/watch?v=xtubEdQUJZ0 I used to play the instrumental Telstar music at the beginning of my labor markets class while I set up the computer equipment. Students asked what the tune was and I said it would be revealed later in the class. When we got to the technology and productivity unit of the course and traced through the advances mentioning Telstar, I would note that a hit record was released related to the event which everyone in the class had heard and then play it. The secret was revealed.
By the end of the 1960s, the U.S. had succeeded in putting a man on the Moon. Those who are convinced that technical advance is very recent might ask themselves whether the U.S. today could put someone on the Moon without a great deal of re-learning.

We started out with a reference to official data on productivity. One commonly-used measure is the Bureau of Labor Statistics’ index of output-per-hour, where the “hour” refers to labor hours. When people talk about productivity, this is the standard index. Output-per-hour is erratic and highly sensitive to the business cycle. To smooth out the growth of the index, the chart below uses a five-year moving average although even that degree of smoothing doesn’t entirely eliminate the cyclical effects.

![Nonfarm Business Annual Change in Productivity: Five-Year Moving Average](https://www.youtube.com/watch?v=FgplIWibv4Q)

If you dismiss the most recent years in which productivity growth seems to lag as due to the Great Recession and its aftermath, there is indeed a productivity spike in the early 2000s. But it is comparable to an earlier spike in the 1960s, the Telstar era. The early 1950s seem to have productivity growing almost as fast. By this measure, anyway, we do not seem to be living in a time of unprecedented productivity growth. And – as noted earlier – if anything the official numbers tend to boost recent figures relative to the past.
It is often pointed out that productivity, when measured by output-per-hour omits the contribution of capital equipment. Technological advance should be what remains after you subtract out the gains in output that result from use of both labor and capital. The Bureau of Labor Statistics thus has a “multifactor” productivity index that takes account of the contribution of both factors of production. You can find a chart below using that index.

**Multifactor Private Business Annual Change in Productivity: Five-Year Moving Average**

Using the multifactor index in fact puts the Telstar era ahead of the early 2000s. So in fact the official data do not suggest that we are living in a period of technological disruption unlike any other. Unless you have better evidence that just pointing to your cell phone, that is the takeaway of this musing which, of course, was produced with technology that didn’t exist in the Telstar era, five decades ago. The point, however, is that Telstar was produced by technology that didn’t exist five decades before it was launched, too. Fifty years before Telstar, you couldn’t transmit voice by radio, let alone images. And so it goes.
Mitchell’s Musings 8-4-14: A Modest Proposal to Combat Income Inequality (in California)

Daniel J.B. Mitchell

California has long had a system of direct democracy – the initiative, referendum, and recall – going back to the early 20th century. The idea was that politicians – corrupted by special interest money – needed to be checked by the electorate. At the time, the villain de jour was the Southern Pacific Railroad, often depicted back in the day as an octopus strangling commerce and buying politicians. Reform was needed.

In particular, as part of the move to direct democracy, the initiative was developed to allow for enactment of direct legislation by voters. Essentially, if mom and pop, sitting around the kitchen table saw the need for a law that the corrupt legislature wouldn’t pass, they would gather their friends and neighbors and by petition put the proposed law on the ballot. But like many well-intentioned reforms, things did not work out quite as planned.

In smaller jurisdictions, the mom and pop model might work. Mom and pop might actually have enough friends and neighbors to mount a successful petition drive in a small or modest-sized city. But California is a large state, both in population and land area. To get enough valid signatures – in the vicinity of
800,000 – across the state, you have to hire a signature-gathering firm. And because some of the signatures will turn out to be invalid, you will probably need around a million signatures for which the firms will charge you at least $1 per signature and sometimes – if you are in a hurry - more. So you will need at least $1 million to get an initiative before the voters. Who has $1 million or more for this purpose? Typically, the answer is special interests – much like the Southern Pacific Railroad in its day – and, increasingly, very wealthy individuals with an agenda and more money than they know what to do with.

Signature-gathering firms hire folks to sit in front of supermarkets and similar locations and induce the requisite number of signatures from the passing crowds. The usual pitch is that even if you don’t favor the proposal, shouldn’t the people have a right to vote on it? In principle, there could be enough popular resistance to prevent enough signatures from being gathered in the allowable time frame. So our first question is whether hiring signature gatherers is a sure thing, regardless of what the proposed initiative says. If you have the money, can you get your proposal – whatever it may be - on the ballot? We are about to test that proposition (no pun intended, of course).

A little more background is in order. There are lightly-populated rural counties in northern California that feel estranged from the powers-that-be in the capital, Sacramento, and in the big urban centers. Back in the 1940s, there was a brief move for some counties to secede from California and form a new “State of Jefferson,” possibly taking some of southern Oregon with them. From time, the Jefferson fantasy floats up, as it did a year or so ago, complete with a flag for the new state that looks remarkably like the faux-Nazi emblem used by Charlie Chaplin in his film, “The Great Dictator.”
Anyway, to cut to the chase, there is a local California billionaire, Tim Draper, who apparently took the Jefferson idea and multiplied it by six.\textsuperscript{10} California would cease to exist and instead be divided into six new states. Then he filed an initiative and has submitted a little over one million signatures which are being reviewed at present by the California secretary of state, the official in charge of election matters.\textsuperscript{11} We won’t know for sure if Draper has enough valid signatures on his petition to get his proposition to divide California into six states on the ballot until September. But assuming enough signatures are valid, we would then have proof positive that you can get absolutely anything on the ballot – regardless of how wacky - providing you have enough money to pay for it. Then the question becomes, how can we better share the wealth that now goes to signature-gathering firms?

Let’s assume that secretary of state finds enough valid signatures on the Draper initiative, thus proving that anyone with $1 million can buy his or her proposition on to the ballot. If that is the case, why not cut-out-the middle man – the signature-gathering firms – and simply let ordinary voters get the $1 or more for their signatures? Such a system would be a transfer from billionaires and special interests to just-plain-folk like you and me and thus would be a blow against income inequality. Basically, the state could set up a website announcing initiatives proposed by anyone with $1 million. All you – as a registered voter - would have to do to get $1 is be among the first million voters to sign up on the website endorsing having the initiative on the ballot. (Remember: The endorsement is just to have the initiative on the ballot; it does not mean favoring the goal of the initiative.) Your $1 would then be transferred to your bank account electronically or perhaps to your credit or debit card account. And, of

\textsuperscript{10}\url{http://www.businessweek.com/articles/2014-07-31/six-californias-a-tim-draper-idea-just-as-madcap-as-the-others}

\textsuperscript{11} From the California secretary of state website comes the summary of the Draper initiative below:

\textit{Division of California into Six States. Initiative Statutory and Constitutional Amendment.}

\textit{Summary Date: 02/18/14 | Full Check Deadline: 09/12/14 | Signatures Required: 807,615}

\textit{Tim Draper (650) 233-9000}

Divides California into six states subject to approval by Congress. Assigns each county to a new state, unless county voters approve reassignment to different new state and second state approves. Establishes commission to settle California’s financial affairs after division; upon failure to resolve, each new state would retain assets within its boundaries and would receive proportionate distribution of California’s debts based on population. Authorizes counties to refuse to provide State-mandated programs and services absent sufficient State reimbursement. Empowers counties to make and enforce all laws governing local affairs. Summary of estimate by Legislative Analyst and Director of Finance of fiscal impact on state and local government: If the federal government approves the proposed creation of six new states, all tax collections and spending by the existing State of California would end, with its assets and liabilities divided among the new states. Decisions by appointed commissioners and elected leaders would determine how taxes, public spending, and other public policies would change for the new states and their local governments.
course, you could click on as many initiatives as you like. If there were ten initiatives available, you could get $10.

Now some would argue that a system of direct buying of signatures (as opposed to indirect through signature-gathering firms) is unfair to moms and pops who want to try to get signatures from their friends and neighbors (even though, as we noted, in practice they can’t). No problem! We just leave the current system in place as an alternative. Mom and pop could try and find a million friends and neighbors to sign a petition, just as they can now. Billionaires like Draper and other special interest groups could hire signature-gathering firms if for some reason they wanted to do so. But they would likely just do the easier thing and send the state a check for $1 million which would then be distributed through the official website to registered voters who offered to sell their endorsements.

If you like this idea to strike a modest blow against income inequality (or just think voters should be able to vote on it), all you need is a million signatures to get it on the ballot.
Mitchell’s Musings 8-11-14: What’s Cooking?

Daniel J.B. Mitchell

A few weeks ago, Los Angeles Times columnist Michael Hiltzik ran a piece entitled “A new right-wing claim: Obama must be lying about inflation!” which was about a new conspiracy theory concerning government price change data.12 The theme, as the headline suggests, is that some folks believe that the official inflation statistics are being kept too low, i.e., the books are being cooked. So let’s look at the data and see what the fuss is all about.

Below are June-to-June annual inflation rates (June is the latest month available at this writing) for the Consumer Price Index (CPI) for all urban workers (CPI-U). As can be seen from the table, since the Great Recession and its aftermath, inflation has been low by this measure. When you eliminate food and energy – the volatile sectors – from the index to get the so-called “core” inflation rate, the same picture overall results. Inflation is low by either measure.

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<tr>
<td><strong>CPI-U</strong></td>
<td>5.0</td>
<td>-1.4</td>
<td>1.1</td>
<td>3.6</td>
<td>1.7</td>
<td>1.8</td>
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<tr>
<td><strong>Core-CPI</strong></td>
<td>2.4</td>
<td>1.7</td>
<td>0.9</td>
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Now you might think low inflation is what might be expected when the economy is soft and, therefore, price raising is difficult. And you might think – based on the headline – that the notion that the price books are being cooked is just “politics” from folks who don’t like Obama. But the story is a bit more complicated.

Let’s start with the notion of an inflation-data conspiracy and what that might mean. One definition might be that someone nefariously is simply putting in false raw numbers out of which the overall CPI is made. That is, when the true data come in on the price of bananas, someone erases the true numbers and puts in figures calculated to lower the inflation rate, an outright fraud. Let’s just call it “fraud” for simplicity.

Another version of conspiracy involves methodology. The true raw numbers are kept, i.e., the actual price of bananas is entered, but the numbers are then combined and adjusted in ways which reduce the official inflation rate. So let’s call that version “methodology” for short. And

let’s also note that in any form of accounting, there are always choices, e.g., FIFO vs. LIFO, that can make the end results look different – but which have some analytic basis.

Let’s return now to the Hiltzik story. What is behind the belief that the books are being cooked, apart from the political element? The answer has to do with Federal Reserve policy starting with the Great Recession. Essentially, the Fed has followed an “easy” monetary policy, lowering short-term interests close to zero. It has done so by buying various financial assets. The goal was partly general stimulus to the economy from low interest rates but also to inject “liquidity” into the financial system and avoid disruptive bankruptcies of financial institutions. The Fed buys assets with money it creates which is technically a counteracting liability of the Fed that balances the assets. The chart below shows the large jump in liability of the Fed starting with the financial crisis of 2008.

It is this money-creating activity of the Fed that gives rise to the conspiracy charge. Versions of the quantity theory of money have been around for a very long time but the notion that money creation is inflationary – “too much money chasing too few goods” – is at the heart of all of them. So if the Fed has been creating money, there should be inflation. If the official figures don’t show that inflation, someone must be cooking the books.

The problem is that simple monetarism isn’t very helpful in a period of economic softness and changes in the financial system. In the most general sense, money creation is stimulatory. But exactly how stimulatory? Moreover, stimulation could mean enhancing the real level of
economic activity (employment, output) – relative to what it might otherwise be. Or it could be price increasing. While the “Keynesian” models of, say, the 1960s, posed an either/or answer (either real activity or inflation), the empirical evidence suggests you can get a mix of both responses. And, the degree to which you get one or the other responses in the mix seems to vary over time.

The simple fact is that the Fed doesn’t know exactly what the mix is. Therefore, it is proceeding pragmatically. If inflation were to arise, it would pull back. So far, the inflation that would warrant a pulling back hasn’t happened.\(^{13}\)

There is an irony in the belief that there must be a conspiracy hiding true inflation because theory suggests (to some) that Fed policy in recent times surely must be causing inflation. The believers don’t specify whether the conspiracy is of the fraud type or the methodology type. With outright fraud, of course, the fraudster gets to pick the results. But methodology manipulation is much more limited.

We have been diddling with CPI methodology, particularly in the 1990s after the Boskin Commission of that era said that the then-CPI was overstating the inflation rate by a bit over a percentage point.\(^{14}\) Generally, the motive for suddenly examining the CPI and diddling with it at that time came from the right side of the political spectrum. Various public benefits, notably Social Security, are indexed to the CPI. So, if you think those benefits are too generous, coming up with a bunch of methodological critiques and suggestions that have the effect of lowering the official inflation rate will cut those benefits.

But you can’t have it both ways. The official inflation rate cannot be too high for Social Security but too low given Fed policy. Moreover, the Boskin episode showed the limits of diddling with methodology as a way of cutting the official rate of inflation. Dropping it by 1 percentage point or so is the most they could do. If you are a puzzled monetarist today, adding a percent to the CPI inflation rate shown on the table of page 1 isn’t going to do much for you. Inflation should be raging. Saying it is really 3% per annum, not 2%, isn’t nearly enough.

Of course, you instead could say that the Great Inflation may not be present now, but it is surely coming. If that is your view, there is then no point in charging that the books are currently being cooked although I suppose you could charge that someone will cook them in


the future. The difficulty you will have with a certainty that a roaring inflation is coming is that financial markets don’t seem to believe it.

The charts on the next page show the yields on various Treasury securities ranging in maturity from five to thirty years. When yields on inflation-indexed Treasuries are compared with those of conventional Treasuries of the same duration (upper chart), you have a kind of market forecast of inflation. None of the yield spreads show an expectation of raging inflation. Admittedly, the spread is a forecast of the CPI inflation rate which is used in the indexing. So if you think the CPI is already corrupt, or will be corrupt, you might ignore that expectation.

However, you can’t ignore the raw yields – lower chart – which have no direct CPI connection. You probably believe that long-term nominal yields of the type the lower chart shows reflect both a real return to lenders and an allowance for inflation. Presumably, that allowance for inflation is the “true” inflation rate – whatever you think that is – and not necessarily CPI inflation. With 30-year Treasuries yielding around 3.3% per annum, there isn’t a whole lot of room for the “true” expected inflation rate to be very high, no matter how you interpret those yields. So here’s the question for inflation conspiracy believers. If inflation isn’t high now, and if financial markets don’t see it being high in the future, what do you know that no one else does?
Source: Federal Reserve Bank of St. Louis.
You could grow bananas at the North Pole. How? With enough subsidy for insulation, heating, solar lamps, etc., it would be possible. Since there would be a need to construct the facilities and then maintenance, there would be jobs created at the North Pole. But would such a project be worthwhile? Surely not. The North Pole is clearly not the best place for growing bananas.

It is also true in less extreme circumstances that you can artificially create jobs. Providing a subsidy can induce economic activity in the location offering the subsidy. But you can always ask whether it is worthwhile.

The question of “worthwhile-ness,” if there is such a word, can be explored further. Let’s assume that without a subsidy, a particular activity (with its jobs) would gravitate to a particular location. For example, steel mills might want to locate close to coal mines to reduce the transportation costs of coal. Nonetheless, if a locality far from coal mines offered to offset the transportation disadvantage with a sufficient subsidy, steel mills might relocate to the subsidized region, creating jobs there (at the expense of the region where steel might “naturally” be produced).

The original location, which had the natural advantage of coal, might – of course – offer a sufficient counteracting subsidy to offset the subsidy of the distant location (thus retaining jobs). Indeed, we can imagine both regions competing with each other to offer more and more subsidies, each with the argument that jobs are at stake. The ultimate beneficiary of such competition is the ownership of the steel industry. The losers are taxpayers who pay for the competing subsidies.

The flip side of subsidies is taxes. Suppose the location that was distant from coal imposed a tariff (a type of tax) on steel shipped from the area close to coal. With a high enough tariff, it could induce internal steel production to meet its domestic demand because the tariff would make steel imports uncompetitive. In response to the loss of steel demand (and related jobs) due to the tariff, however, the area with coal might impose a retaliatory tariff on some other product that would otherwise have gravitated to the far-from-coal region. In the end, the prices of the products on which tariffs were imposed would be increased, thus harming consumers.

Of course, there is more to this story than can be discussed here and some qualifications to it. Nonetheless, it is noteworthy that the U.S. constitution – which in part defines the relations of the states within the U.S. with each other as well as Congress’ authority over them – has provisions designed to limit artificial competition between the states or artificial advantages given to them:

In Article 1, Section 8, Congress is given the authority “to regulate Commerce with foreign Nations, and among the several States, and with the Indian Tribes.”

In Article I, Section 10, we find:
No State shall, without the Consent of the Congress, lay any Imposts or Duties on Imports or Exports, except what may be absolutely necessary for executing it’s inspection Laws: and the net Produce of all Duties and Imposts, laid by any State on Imports or Exports, shall be for the Use of the Treasury of the United States; and all such Laws shall be subject to the Revision and Control of the Congress.

To “create a more perfect union,” Congress is supposed to be the primary regulatory body when it comes to external commerce and commerce between the states. California, for example, cannot impose tariffs on goods coming from Nevada. The objective of the founding fathers was to create a federated system in which goods and people flowed freely within and whatever limits were placed on external commerce were to be centrally determined.

From an economic perspective, the U.S. can be seen as an early version of the E.U. Within the E.U. there are supposed to be no artificial barriers to trade among the various member nations. Germany cannot impose tariffs on French goods. Rules limit the ability of member states to subsidize their internal economic activities at the expense of one another.

These observations are a preamble to the observation that within the U.S., while we clearly don’t allow tariffs between the states, we do seem to allow all manner of subsidy. At this writing, in the California legislature, there is a bill pending to quadruple the tax credits for movie making within the state. The justification is that other states are giving bigger tax subsidies and California has to compete (for jobs) by spending (or forgoing revenue) at a higher level. Proponents can point to the fact that in the film “Battle: Los Angeles,” the LA that aliens from some other world actually invaded was Louisiana, due to that state’s tax credits for movie making.

Welcome to Louisiana
And it’s not just the film industry that is receiving taxpayer largess. California has been handing out tax credits to what remains of its old aerospace industry. Meanwhile, new industries in California – which have a certain cachet among state legislators – (Tesla is a recent example), have learned to play one state against the other. Isn’t it time for Congress to take seriously its authority over commerce among the states and legislate against state-provided corporate welfare?
Mitchell’s Musings 8-25-14: A Heritage of Snake Oil

Daniel J.B. Mitchell

It’s rare when you find an article in which you agree with the title but almost nothing else. However, I found one in an op ed entitled “Don’t believe that a sluggish economy must be the new normal” by Stephen Moore, president of the Heritage Foundation and available at http://www.losangelesregister.com/articles/economy-603678-growth-percent.html.

I have expressed the view in previous musings that the “new normal” thing is being way overdone. Whenever there is an adverse blow to the economy, it seems as if someone begins promoting the idea that what has happened was some kind of structural shift and things will be bad from now on. During the Great Depression, for example, when the cause was clearly a negative macro shock, there were voices saying that new technology meant that unemployment would be high forever. The idea persisted until the unemployment rate fell to record low levels during World War II.

During the sluggishness after the end of the Korean War, the “automation scare” developed. Again the idea was that unemployment was due to new technology – a structural shift - and therefore there was no sense in stimulating the economy. The result of such stimulus would only be inflation, not more jobs, according to this view. And, of course, now we hear similar prognostications. The new normalists tell us to forget that the unemployment rate was low before the financial crisis of 2007-2008. They say it’s still high now because of some kind of technological shift which amazingly took place just when the crisis hit. Want proof? Just look at all the fancy new cell phones!

Why are there always new normalists when adversity strikes? Some of them are pundits who want to be first to put forth a “new” concept. Being a pessimist who purports to see hidden, deep, underlying causes is easily confused with being wise. Other new normalists are the powers-that-be who would like to cast off blame for adverse current events by saying that those developments were inevitable, a force of nature, and beyond their control.

Anyway, that’s why I agree with the title of the op ed. The problem is the rest of the article. The op ed, after the provocative title, then focuses on the 1960s:

John F. Kennedy campaigned for president in 1960 by belittling the slow growth rate in the late 1950s of 2 percent to 3 percent and declaring, in his Massachusetts accent: “We can do bettah.” And he was right. In the 1960s, after the Kennedy tax cuts, prosperity returned, the economy grew by almost 4 percent annually, and unemployment sank to record lows.

So far, so good. But then:

... (T)he problems with the U.S. Economy aren’t structural, they are political. The current funk is the inevitable byproduct of a cascade of policy mistakes over the past seven years dating back to George W. Bush’s last years in office. It would be hard to conceive of a worse set of policy prescriptions than the ones Mr. Summers and others conjured up. We’ve had bailouts, stimulus plans, tax increases on “the rich,” Obamacare, hyperexpansive Federal Reserve monetary policy with near-zero interest rates, the Dodd-Frank bill, Obama’s anti-carbon policies, the vast expansion of the welfare state during the recession, and on and on. These have flatlined the economy.
It’s as simple as that. No there hasn’t been some external shock to the economy or some uncontrollable divine intervention with God ordaining: thou shalt only grow at 2 percent. It was the result of the White House and the Fed following a discredited Keyensian [sic] model that government spending, debt and cheap money are the way to restore growth. Ideas have consequences, and bad ideas have bad consequences...

If you know anything about U.S. economic history, you know that the Kennedy administration cut taxes entirely because of Keynesian ideas about how the economy ticked. If growth was sluggish, according to Keynesian views of the era (and now), stimulate through either more spending or tax cuts with their multiplier effects. You have only to look at the names of some of the members of the Kennedy-Johnson Council of Economic Advisors to get a sense of the degree to which Keynesian thinking and policy ruled:

Walter Heller, James Tobin, Kermit Gordon, Gardner Ackley, Otto Eckstein, Arthur Okun, etc.

Even apart from the formal White House advisors, there was a steady stream of outside experts brought into the Kennedy-Johnson White House for consultation. I was at MIT as a PhD student in economics during the 1960s and I can tell you that folks such as Paul Samuelson and Robert Solow – Keynesians! – were very much part of the policy conversation.

Now I suppose you could say – or maybe Moore would say - that while the Kennedy-Johnson economic advisors in the 1960s were Keynesians, they somehow inadvertently stumbled into laisser-faire/supply side policies. But that claim is hard to reconcile with such other policy initiatives as the wage-price guideposts program, i.e., direct intervention by the federal government into private wage and price setting. It’s hard to imagine anyone in the White House today even thinking of such a level of activism. There were also voluntary – and then mandatory – controls on international capital movements designed to defend the prevailing fixed exchange rate Bretton Woods system. (That system which they were defending, by the way, was designed in 1944 through negotiations between Harry Dexter White for the U.S. and – you guessed it! – John Maynard Keynes for Britain. It required continuous official intervention in private currency and gold markets.)

In the aftermath of the 2007-2009 Great Recession, one of the things the Federal Reserve attempted was to change the differential between short-term and long-term interest rates (lowering the latter). But if you go back to the 1960s, you will find “Operation Twist,” also an attempt to change that differential. If you don’t like monetary activism now, surely you can’t like it then. In short, the idea that the Kennedy-Johnson period was not Keynesian/activist at the macro level simply defies basic history.

What about social policy? According to the op ed:

We have paid people not to work, bailed out bad actors, disincentivized employers from hiring more workers, raised taxes on investment, passed new regulations to strangle our energy industry and refused to fix a corporate tax system that sends jobs abroad.

If those are the problems today, what does the author have to say about enactment of Medicare and Medicaid during the Johnson era? What about the various Great Society programs? What about the increases in the federal minimum wage in 1961, 1963, 1967, and 1968?
I suspect that although the op ed praises the real growth of the 1960s, the author would not praise the gradual build up of inflation during that decade, especially in the second half as the Vietnam War (and its spending) heated up. President Johnson was advised by his Keynesian economists that with the economy overheating, a tax increase would be in order, advice which he famously ignored for political reasons.

In short, if you like what happened in the 1960s in terms of real economic growth, you must also like Keynesian economics and government intervention – because that was what the 1960s were all about. If you like the real growth of the 1960s, but you don’t like the uptick in inflation during that period, you have to blame Johnson for not following the Keynesian advice of his Keynesian consultants.

The op ed closes with:

*Keynesianism should now be recognized as snake oil, and the challenge for Republicans is to convince the American people they have a plan that will “do bettah.”*

*There is indeed some snake oil on offer here, but it’s not being peddled by Keynes or his successors.*
Mitchell’s Musings 9-1-14: Remembrance of Things Past: A Party for the Boss

Daniel J.B. Mitchell

Sometimes, unusual things happen that seem unique to our time. Sometimes, however, the seemingly new developments may be echoes of events in the past. For this Labor Day musing, surely the unusual event de jour is the semi-strike and now settlement of a dispute at Market Basket, a family-owned supermarket chain in New England. There are a variety of unusual elements of the Market Basket story, not the least of which is that smaller regional supermarket chains are being swallowed up by national giants.

I won’t go into the details of the Market Basket case. Tom Kochan of MIT has been following the story he provides a description:

Imagine high-level executives, store managers, clerks, and warehouse workers standing outside their stores side by side for a month demanding their CEO be reinstated and the business model that made the company thrive be maintained. And imagine their customer base cheering them while they had to shop elsewhere at considerable inconvenience and expense. That is exactly what happened this summer at Market Basket, a highly successful New England family-owned grocery chain with 71 stores and 25,000 employees. On Wednesday night, Arthur T. Demoulas struck a triumphant deal to buy his warring cousins’ share of the family grocery empire, ending a six-week standoff between thousands of employees and management...

For years, Arthur T. had led Market Basket to high profits with a business model that provided consumers with low prices and good quality service by building a highly productive, well paid, and loyal workforce. But when (cousin) Arthur S. gained control in June, he fired Arthur T., replaced him with new co-CEOs of his choosing, and began pursuing options to increase the flow of cash to family owners. Employees demanded Arthur T. be reinstated and the business model they built together be restored. They organized rallies that attracted as many as 10,000 workers, customers, and community supporters. They used a “Save Market Basket” Facebook page to spread their message and maintain solidarity across the ranks. At one point 68 of the 71 store managers signed a statement saying they would not work for anyone but Arthur T. Customers offered countless testimonials to the low prices and good service they were missing and documented the increased costs they incurred in shopping elsewhere by pasting their sales receipts on the windows of their local stores...15

It is unusual for nonunion workers, as at Market Basket, to strike for obvious reasons. It is even
more unusual (unheard of?) for them to be joined by supervisors and managers. But it happened in this case.

Once we get away from the details, however, what seems most unusual is the degree of
empathy of the store workers for the top boss. It’s not that bosses can’t be liked or even be
popular among workers. But how many employees would sacrifice to keep the boss? For that
to happen, it likely requires both a popular boss and a sense that if he goes, jobs and conditions
will be in jeopardy.

Put in those terms, the Market Basket story reminded me of another story that my stepfather
once told me that took place in the late 1930s or early 1940s. As you are likely to know, those
years were a period of severe labor strife. My stepfather, William Mitchell, was an organizer
and official of the UE, the United Electrical Workers, one of the more radical CIO unions of that
era. The UE later was expelled from the CIO in the late 1940s for having communist leadership.
It still exists today, but is a shadow of what it once was.16 (It is symptomatic of the situation of
unions more generally nowadays that CIO currently means Chief Information Officer, but we
digress.)

In any event, the major employer that the UE had
organized was General Electric. But there were
various small employers that had been unionized by
the UE, typically in manufacturing. My stepfather was
stationed in New York City, but he was sent by the
union to visit and investigate a local in the Midwest
where, reportedly, something funny was going on.
When he got there, he talked to local officers and
union members and looked at the books. No
irregularities were to be found.

As he prepared to leave, one of the members asked him if he was coming to the party. What
party is that? The party for the boss! You’re having a party for the boss?

It turned out the boss/owner had signed a standard UE agreement, but found he could not
afford the contractual wage rates. So from time to time, the workers threw a party for the boss
and chipped in enough money to keep the firm going. As in the Market Basket case, the

16The union reportedly has about 37,000 members. It has a website: http://www.ueunion.org/
workers liked the boss and liked their jobs and realized that they need the former to keep the latter.

There may be no deeper lesson in this story. It’s just something that happened. Have a good Labor Day holiday.
Mitchell’s Musings 9-8-14: Wait a Minute; Wait a Minute

Daniel J.B. Mitchell

On September 5, the latest “Employment Situation” release for August became available from the U.S. Bureau of Labor Statistics (BLS). One of the closely watched numbers in that release is the latest month-to-month (July to August) change in nonfarm payroll employment. According to the release, the preliminary seasonally adjusted estimate is that there was a net increase of 142,000 jobs in August. Commentators immediately pronounced this number to be disappointing because it was lower than (someone) expected and lower than recent employment gains.

Some readers may recall the Al Jolson’s line from The Jazz Singer, “Wait a minute; wait a minute, you ain’t heard nothing yet.” (If not, go to https://www.youtube.com/watch?v=22NQuPrwbHA.) The problem with getting excited or disappointed as a result of the reported monthly change in employment is that the preliminary data, which already reflect the vagaries of seasonal adjustment, are subject to major revision. So we need to stand back and “wait a minute” before reading the monthly figures as guides to policy or to the general state of the economy. Maybe we haven’t heard “nothing” when we get the monthly number, but the “something” we have heard is pretty fuzzy.

The chart below shows the reported preliminary monthly changes for 2013 versus what now (as of September 2014) appears on the BLS website:
As it turned out for 2013, not only are the deviations of the preliminary figures relative to the current figures large, but they don’t even average out over that year. That is, except for July 2013, the preliminary numbers consistently understated what is now taken to be the true figure. Only in July 2013 was there an overestimate. Almost all of 2013, as seen initially, was disappointing relative to 2013 as seen today. The average error was a monthly understatement of about 30,000 jobs, i.e., something like 360,000 jobs over the year.

In past musings, I have made the heretical statement that maybe we don’t really need monthly releases and maybe, say, quarterly releases would be better. Of course, we will continue to do monthly releases because that’s how it has always been. Moreover, any change in frequency would become the subject of conspiracy theories about manipulated figures. But it would be nice if commentators just focused on changes over longer periods than just one month. Why not use August 2013 to August 2014 (a full year)? If you do it that way – and use just the numbers that are not seasonally adjusted since you are covering a full year – it turns out that we are creating net jobs per month at a rate of around 209,000. You can then decide whether that number is disappointing or not and what policy response, if any, should be taken. You may be right or wrong in your thinking but at least you won’t be basing it on statistical noise.
Mitchell’s Musings 9-15-14: Poles Apart

Daniel J.B. Mitchell

In past musings, we have commented on the uncertainty raised by opinion polls on important public issues. Complex issues that many people have never heard of or considered are presented by pollsters to respondents who provide “answers” that are highly dependent on the framing of the questions. Recent polls regarding two initiatives that are on the November 2014 California ballot illustrate this issue. If you doubted my point before, read on!

Proposition 45 would provide for rate regulation of health insurance by the state’s elected insurance commissioner, who currently can opine on such rates, but cannot cap them. Not surprisingly, the insurance commissioner supports Prop 45 since it expands his authority. The opposition comes from two sources. Again, not surprisingly, the insurance carriers in the state oppose the proposition. But also opposed are the operators of the state’s “Obamacare” health exchange. There seems to be a turf war going on between the health exchange administrators and the insurance commissioner that is behind the controversy.

Proposition 46 ostensibly is about drug testing of doctors (who wants a drugged out doctor?), but is actually an effort by trial lawyers to raise the state’s cap on malpractice awards. So, not surprisingly, doctors are opposed and lawyers are in favor. In both the cases of Prop 45 and 46, vast sums will be expended on TV, radio, and other advertising as Election Day approaches. And you can already assume that the sponsors of these propositions spent $1-$2 million just to hire commercial signature gatherers to put these initiatives on the ballot.

Naturally, there is much at stake for the proponents and opponents of these ballot propositions. And, of course, anything related to health care is topical these days because of the changes the health system is undergoing at the national level. Those in the policy wonk world and those representing the major interest groups involved are obviously aware of the initiatives and have been aware since the petitions to put them on the ballot began to circulate. But it is reasonable to assume that the general public had little knowledge of the propositions and are only now – as advertising has begun and news media articles are appearing – forming opinions.


18A sample radio ad that has begun to air is at https://www.youtube.com/watch?v=bWoVU_xhtOY.
One of the major sources of public opinion polling information in California is the Field Poll which for many years has been a source of political information on attitudes toward public issues. Like all pollsters, however, to be relevant and interesting, Field has to track opinions on what voters might be feeling about ballot issues and candidates. But that need poses a dilemma, since Field must produce opinions about issues on which many in the public simply don’t have formed opinions. So in one way or another, it must tell those being surveyed what the issues are all about. What it says is and how it says it is going to be important in determining the answers received.

| Trend of voter preferences on two statewide health-related ballot measures: Propositions 45 and 46 (among likely voters) |
|---|---|---|
| **Proposition 45** (Health Insurance Rate Changes) | Yes | No | Undecided |
| Late August/Early September | 41% | 26 | 33 |
| Late June/Early July | 69% | 16 | 15 |
| **Proposition 46** (Drug Testing of Doctors/ Medical Negligence Lawsuits) | | | |
| Late August/Early September | 34% | 37 | 29 |
| Late June/Early July | 58% | 30 | 12 |

Note: Late August/early September poll conducted using a summary of each proposition’s official ballot label. The official ballot label for these measures had not yet been released by the California Secretary of State at the time of the late June/early July survey.

As the table above from the Field poll shows, there was a dramatic swing in reported voter attitudes towards Prop 45 and 46 between late June/early July and late August/early September. In the earlier survey, the two were reported as favored by 69% and 58%, respectfully. A couple of months later, the percentages had dropped to 41% and 34%. Note that in the earlier survey, 15% and 12% said they were undecided. A couple months later, a lot of folks who were decided early on apparently changed their minds concerning what they were decided about. And the really heavy advertising regarding the two propositions had not begun in that interval.

Let’s put aside the merits and demerits of the two ballot propositions. It should be obvious that when dealing with issues in which there will be controversy as the election approaches, early polling is not very helpful as a forecast unless you can present the questions as voters will eventually hear them. QED

Let’s suppose that I am a journalist. I read somewhere that real wages have been stagnant and I want to illustrate this point in an article I am writing. I discover that the U.S. Bureau of Labor Statistics (BLS) on a monthly basis produces a series called “real average hourly earnings.” So I go to the BLS website to get some historical data on that series for my article. When I get there, I find:

I don’t immediately see a link for real average hourly earnings, but I do see a search option up in the right-hand corner. So I type in “real average hourly earnings” there and get:
As you can see on the screen shot on the previous page, a bunch of references pop up, mainly to BLS media releases that have only very limited recent data. I am looking for a longer time series, not just a few recent data points, for my article. So I go back to the starting page and click on “home.”

One of the options I then see there in a drop-down menu is called “pay and benefits.” That sounds right. Earnings are “pay,” after all. So I click there and get:
The result is a whole list of options as the screenshot on the prior page shows, but “real average hourly earnings” is not one of them. So I go back to the home page and try “data tools” since I am looking for a data series. Another drop-down menu appears:

One of the options there is “series report,” so I click on that one hoping that real average hourly earnings might be one of the series reported. The result is shown below:
Sadly, what I find is that if you want a particular data series such as the one I am searching, you have to know its ID number. But wait! There is another option to click on “series ID formats.” Maybe I will find a listing of the ID number for “real average hourly earnings” there. Another disappointment results. But I do find an option called “national employment, hours, and earnings.” That option at least has the words “hours” (which is close to “hourly”) and “earnings.” So I click there and get:

This time I get a lot of strange information about things like where a seasonal adjustment would be indicated in the ID number, if only I had the ID.

We could go on with this fruitless search but you surely get the point. The key issue here is that what should be a user-friendly public website just plain isn’t. Why - when I search for “real average hourly earnings” - don’t I immediately land on a webpage which gives the historical data for that series. Note that “real average hourly earnings” is not one of the more obscure data series produced by BLS. BLS in fact puts out a monthly release just for that series.

BLS has been in the data business for a long time. The agency’s history actually predates the creation of its parent, the U.S. Department of Labor, early in the 20th century. BLS got on the web when the web got going and there has been plenty of time since then to produce a website that simply lists every series and doesn’t require some arcane ID number. The website should be accessible to folks such as my hypothetical journalist, and not just to professional users of labor market data who have figured out the vagaries of the website. There are commercial data providers who make BLS data and data from other official government agencies available – generally for a cost - in just the simple way I have suggested. Other government websites are more user-friendly than BLS offers. Check out, for example,
the website of the U.S. Bureau of Economic Analysis, the agency that puts out the national income accounts.

Note that this musing is not dealing with the methodology behind particular data series. Maybe “real average hourly earnings” has drawbacks as a measurement. Maybe our hypothetical journalist would do better to use some other series. Those considerations are separate issues. The only point being made here is that if a data series is being made public, the figures should be easy to access.

It can be done.
Mitchell’s Musings 9-29-14: The Forgotten Unfunded Liability

Daniel J.B. Mitchell

In recent years, there has been much discussion of unfunded liability. Usually, the targets of this concern are pension and social insurance programs such as Social Security, Medicare, and various state and local public pension plans. The concern is that even if these plans have assets in them at the moment, the projections are that the eventual liabilities exceed those assets and coming generations, therefore, will have to come up with the money to cover obligations that represent labor services in the past.

From time to time, I have had fun calculating the unfunded liabilities of the Pentagon (we are committed to national defense “forever” but we don’t have assets on hand today to pay for that future commitment). I have even calculated the similar unfunded liability of my hometown Santa Monica’s police department. (As in the Pentagon case, the city is committed to provide police protection to all inhabitants “forever” but there are no assets set aside today to pay for that commitment.) Suffice it to say, you get very big numbers, numbers sufficient to scare your average congressional representative or Santa Monica city council member.

There is a difference, however, between pension unfunded liabilities and future service liabilities. In the former case, we seek to have assets accumulated in the past that pay for past service, even though the actual payments are received by employees at some point in the future. In the case of promised future services (Pentagon, Santa Monica police), future taxpayers will have to pay only for services which they will benefit from in the future. In the underfunded pension case, future taxpayers are paying for the services provided for, but not paid for, by past taxpayers.

In short, according to the idea of matching services and paying for services over time, it is a Bad Thing to have people in the future pay for the consumption of folks in the past. So let’s see if there is anywhere to be found an unfunded liability in which folks in the future must somehow pay for things in the past, apart from Social Security, Medicare, and public pensions.
As can be seen on the chart on the previous page, when you consider the US as a whole, you find that since 1980, we have tended to accumulate international assets (claims on the world) more slowly than we have accumulated liabilities. Whereas before the 1980s, our international liabilities generally grew more slowly than our international assets, afterwards, the reverse trend developed. Of course, there were periods of fluctuation in which the trend generalization did not hold, thanks to such things as movements in exchange rates. But the underlying trend is evident from the chart. In 1980, we had assets > liabilities of roughly 10% of GDP, we now have assets < liabilities of about one third of GDP. In the former period, we could in theory have “paid off” our gross international debt by selling assets and still had 10% of GDP in assets left over. Now, if we tried to “pay off” our gross liabilities, we would come up short after asset sales by about a third of GDP. That’s a lot.

Unless you think that we can go on increasing our net debt to the world forever (so there never will be a point where future folks will be paying for past consumption, you might be concerned by this forgotten unfunded liability now that you know. Of course, there is a comeback. Maybe our net borrowing has been directed toward accumulating capital assets which someday, somehow will produce the needed pay back. A visit to your local retail electronics store should disabuse you of the notion that the increase in debt is all going into capital goods. Flat screen TVs, iPhones, sure seem like consumption goods. Go to your local toy store and look at the country of origin of the products you find there. Sure seems like consumption goods there, too.
For that matter, go to your local Toyota, Kia, Volkswagen, Mercedes, or BMW dealer. We can argue over what exactly is a capital good. But your car, in the end, is more consumption than investment in the sense that it is unlikely to generate resources for the US to repay our net foreign debt.²⁰

When pensions are underfunded, their trustees often create a plan to achieve full funding over a period of time. Essentially, what is involved is first paying into the fund the “normal” cost of the plan (the amount that covers the incremental liability generated each year) and then setting up a schedule to amortize (pay off over time) the accumulated past unfunded liability. The analog to the normal cost in the case of net foreign debt is (roughly) the net export balance. If the US from now on kept its net export balance to zero, the unfunded liability would cease to increase since we would be paying for current consumption from the world (imports) with sales to the world (exports). But moving to a zero balance of net exports would not pay off the accumulated past debt. To do that, we would need to run a net export surplus. The bigger the surplus, the faster we would retire net debt.

Our net export balance seems to be around -$500 billion per annum. Our net debt is roughly 10 times that amount. (The figures vary from year to year.) So to pay off the net debt in ten years, we would have to run a net export surplus of around +$500 billion per annum. So the total “swing” from the current deficit situation to the 10-year payoff plan would be about a trillion dollars. In effect, the swing would be a stimulus of about 5-6% of GDP, with a fair amount coming from added manufacturing production.

There are ways to make it happen. All that is needed is for the folks who are so upset about the unfunded liability of programs such as Social Security to become equally concerned about the hidden unfunded liability embedded in international commerce.

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²⁰Yes, I know; in principle if I buy a Toyota instead of a Ford, you could say that I freed up US capacity to turn out that hypothetical capital good which will someday pay off that debt. There are a lot of formerly employed auto workers who might not have experienced it quite that way.