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Adequate Aggregate Demand and the Commitment to End Poverty

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Adequate Aggregate Demand and the Commitment to End Poverty

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Introduction

This paper has a number of aims. The major one is to examine the meaning of the phrase "an adequate aggregate demand" in the light of a commitment to end or drastically limit poverty in the near future, say by 1976. Thus the main concern is with the relation between aggregate demand (and its correlate, the level of unemployment) and progress in the War on Poverty. However, aggregate demand is also related to other measures of system performance, and the interrelations between full employment and other policy goals are explored.

The goal—end poverty in America—makes the size distribution of income an object of economic policy. Given that the world is so constructed that the various goals are not necessarily compatible, the trade offs among goals become relevant. There are two sources of trade offs. One source lies in the technical characteristics of the economy and the other in the nature of communal preferences.

Of particular interest, especially in light of the way in which the economy retreated from full employment during the late summer of 1966, is whether the American economy is flawed, and if so, how. A standard view is that prices rise at unacceptable rates whenever unemployment rates fall below some threshold. However, the low unemployment rates which lead to price increases are high unemployment rates from a viewpoint which emphasizes employment as the essential element in a War on Poverty. The standard position leads to the disheartening conclusion that the War on Poverty must be fought with overall unemployment rates of 4 percent or more unless, by the time-consuming and costly process of training and education, the structural characteristics of the economy can be changed.

An argument of this paper will be that the really serious flaw of American capitalism is not any such inverse relation between unemployment rates and price increases. Rather the meaningful flaw follows from the effect of successful operation of the system on the values of financial and real assets and through them on the willingness to invest. If a period of sustained tight full employment is necessary to achieve War on Poverty objectives, the same sustained tight full employment will breed a non-sustainable rate of increase of investment expenditures. Such growth of investment leads to financial market pressures on liquidity and ultimately to financial instability.

Aggregate demand will be adequate, from the perspective of the policy goal to eliminate poverty, only if it is sufficient to generate tight full employment. There are five ways in which labor market conditions may be related to the extent and trend of poverty. Most directly affected will be the extent of poverty due to unemployment and short time employment. In addition, if tight employment is sustained, the expectation is that wages will rise faster in the low wage industries than in the high wage industries. Labor market participation is sensitive to overall employment opportunities; thus multiple participation in one family, perhaps taking the form of drawing old and young into the labor market, will raise family income. The movement to tight full employment means a rapid increase in income which, in turn, means large tax receipts and smaller welfare expenditures by State and local governments. This easier fiscal position of "local" government can make a more adequate system of transfer payments possible. Finally, the overall growth rate of the economy may be sensitive to the extent to which current output is capacity output; thus tight full employment may mean a greater rate of growth of capacity income.

Poverty in an affluent economy is in large part a question of the size distribution of income and, in particular, income from work. Unfortunately, little of real substance is known about the mechanics by which relative wages, and thus relative incomes, are determined. Is the size distribution of income a result of the past employment history of the economy? That is, will tight labor market conditions for an extended period decrease the spread of wage rates, or weekly earnings, by industry?

It is worth noting that the low end of the size distribution of relative wages can change in two ways. The low end may be decreased by increasing low wages relative to high wages or by decreasing the proportion of employment in the low wage industries. The existence of a large rural population living in poverty may act as a reservoir that makes the elimination of urban poverty very difficult. That

is, the large number of rural poor serves to prevent both a rise in the low urban wages relative to other wages and a significant decrease in the proportion of the urban population in low wage industries. An economy in which such an infinitely elastic supply of low wage urban workers exists may be characterized as an enclave economy.

One caveat is necessary before we proceed. Among those living in poverty are many whom policy neither desires nor expects to be in the labor force. These include the aged, the infirm, the young, and the mothers of young. The standard of living of these poor can be raised by improving our system of transfer payments as well as by better job opportunities. This paper is not directly addressed to the proper design of a system of transfer payments although some thoughts on children's allowances, negative income taxes, and a proper social security system are offered.

From the perspective of this paper, rural poverty is a part of the general poverty problem in the United States. The special impact of rural poverty is that to date rural areas have been a source for a chronic migration to urban areas, and this flow is expected to continue. Thus policies to generate tight full employment, which will be the main proximate policy goal favored here, will have to be framed with a need for the urban labor markets to absorb a large and persistent flow from rural areas.

As the gross outmigration per year from rural America is very large compared to the net outflow per year, the potential rate of increase in the urban labor force due to internal migration is much greater than has been experienced. Thus the job generation and the level of aggregate demand needed to achieve any overall measured unemployment rate is greater than it would have been in the absence of such migration.

An Adequate Aggregate Demand

One of the phrases that constantly occurs in discussions of programs to end poverty is "an adequate aggregate demand." Usually, in context, "adequate aggregate" demand provides the framework within which some nonaggregative policy or program, that is, a policy or program designed to affect some structural attribute of the economy, is to take place. That is, aggregate demand is to provide the favorable environment within which some other policy or program is to function. Almost always, within such discussions, an adequate aggregate demand is taken to be a necessary but not a sufficient condition for the attainment of some antipoverty goal. In a number of previous pieces related to issues of poverty in America I have raised the question of whether achieving and sustaining a truly "adequate" aggregate demand would be a sufficient as well as a necessary condition for the elimination of a large portion of poverty (*5, 6*).[1]

[1] Italic numbers in parentheses indicate references listed at the end of this paper.

Whether or not aggregate demand is adequate can be determined only if the targets or goals set for the economy are stated and if some theory or model of the relationship between aggregate demand and these goals is accepted as valid. That is, aggregate demand is not a goal in itself. Full employment, economic growth, reasonable price stability, and the international stability of the dollar are the standard set of economic goals whose attainment has been related to the level of aggregate demand.

Within the model of the economy that is "accepted" by most working economists there are "trade offs" among these goals. These trade offs are due to the performance characteristics of the economy. As a result of these "technical" trade offs, a consistent social consensus which states the relative values of the various goals is needed if decision-making is to be rational and stable. Basically, in our democracy it is the Congress and the President who in the short run make the social choices. Unfortunately, on many occasions their decision-making is not based upon clear ideas as to what technical trade offs do exist in the economy.

Many who, because of the decisions they make, should know better have a "Pollyanna" view of the world: that all good or desired things are mutually compatible. Often decision-making seems to take place without regard for the possible existence of such incompatibilities and as a result considerable surprise occurs when unanticipated side effects to the pursuit of a particular goal take place.

For our purposes two things need to be done. The first is to make explicit the nature of the trade offs that exist in the world as it is among major policy objectives. The second is to inquire how the addition of another goal, the elimination of poverty, affects the weight attached to the various other objectives—i.e., makes them more or less important.

In what follows it is assumed that the size and rate of change of aggregate demand can be managed by monetary and fiscal policy. This assumption is being retained even though the events of 1966, especially during the second and third quarters, cast serious doubts on the efficiency, under all circumstances, of monetary and fiscal actions.[2] In addition, even if monetary and fiscal policies can manage aggregate demand, there are important effects from varying the mix of policies. We will tend to ignore these difficulties, especially as they have been very well documented.

In addition, it is necessary to emphasize that even the aggregate policy actions—monetary policy, gov-

[2] During the second and third quarters of 1966 the combination of rapidly increasing private investment demand, the increase in government expenditures brought about by the war in Vietnam, the passive fiscal policy, and the reliance upon monetary constraint led to a near financial crisis that has been labeled "the crunch." The crunch apparently cooled off the investment boom and was followed by a year of relative stagnation. The open question is whether the crunch was an accidental or an inherent characteristic of American capitalism.

ernment spending, and tax schedule adjustments—have a structure. A choice among techniques of managing aggregate demand needs to be made, and this choice will affect behavioral and distributive aspects of the economy. Thus the choice of instruments will also reflect the weights attached to different policy objectives.

Trade Offs Among Standard Goals

In the world *as it is*, a number of trade offs related to aggregate demand exist among the attributes of the economy. The dimensions of these trade offs depend upon the structural characteristics of the economy. For policy makers, these structural characteristics are real and effective constraints. This is so even though structural characteristics may also be subject to control by economic policy. Typically, changing a structural characteristic (such as the power and scope of trade unions, the character of agricultural policy, the organization of industry, the nature of the financial system, or the propensity to discriminate and segregate) is a much more serious and difficult policy step than changing tax and spending schedules or taking monetary policy actions. Thus, because structural characteristics are embodied in fiscal and monetary policy actions (investment tax credits and differential ceiling rates on various classes of deposits) and also because they occur as offsets to fiscal and monetary policy actions (the various constraints upon direct and financial investment abroad adopted during the past few years), structural characteristics cannot be ignored in making policy relative to aggregate demand. That is, for relevant policy discussions an economist cannot be cavalier and blithely, by waving his hand, abstract from the existing set of institutions and their behavior patterns.

An often-discussed trade off in performance among policy goals related to aggregate demand is between employment on the one hand and price stability on the other.

Within limits, employment is positively related to aggregate demand. The limit to this relation is given by full employment. As full employment is approached, increases in aggregate demand tend to raise prices. At full employment further increases in aggregate demand are absorbed entirely in price increases—at some level below the full employment level increases in aggregate demand result in a rise both in employment and in prices. The "Phillips curve" [3] analysis attempts to measure the relation between measured unemployment rates and the percentage increase in wage prices per period. The argument of the Phillips curve analysis is that beyond a certain point, decreases in unemployment will be associated with rising wages and prices and that the price, in terms of rising prices, of lowering the unemployment rate increases at an accelerating rate as the measured unemployment rate decreases.

Some warnings about Phillips curve reasoning are in order. First, the rise in prices—or wages—has been associated not only with the unemployment rate but also with the rate of change of the unemployment rate. The evidence as to the behavior of wages and prices in relation to the unemployment rate derived while unemployment rates were falling should not be used without further thought to forecast the behavior of wages and prices when unemployment rates are stabilized at some particular rate.

Secondly, as will be shown, there has been a marked change in the structure of earnings by industry since the end of World War II. The rate of increase of earnings that was obtained in some industries is sufficiently low so that if this rate were quite general, the pressures that tend to raise prices through wages would have been much smaller than actually took place.

In addition, structural characteristics of the economy—in particular those dealing with labor's geographical mobility and facilities for occupational training—will determine how easily job vacancies can be filled. Thus the scope of manpower-oriented nonaggregative policies is determined by their ability to position the Phillips curve so that a lower unemployment rate and a higher rate of decline of unemployment are associated with every rate of increase of prices.

We conclude that for any economy there is a relation that depends upon the structural characteristics of the economy and that states the cost in terms of the price increases of a given level of unemployment and a given rate of decrease of unemployment. During expansion, the level and rate of increase of aggregate demand generates a benefit (measured by the unemployment rate and the rate of decrease of unemployment) at a cost (measured by the rate of increase in prices). The question is whether the benefit is worth the cost.

One of the clearest relationships that exist in our economy is between aggregate demand and the import component of the balance of payments. As aggregate demand increases, in particular when a rapid run up of income that accompanies a rise in the ratio of employed to employable resources takes place, imports also rise. Thus there is a clear cost in terms of a tendency toward a deterioration in the balance of payments of increasing aggregate demand or increasing employment.

Even though the effect of current imports upon the balance of payments may be adversely affected by a decline in unemployment rates, the overall effect of rising aggregate demand upon the balance of payments depends upon capital movements as well as trade movements. The propensity of American business to invest abroad—particularly in the advanced countries of the world—may be sensitive to the level and growth of markets abroad relative to the level and growth of markets within the United

[3] The Phillips curve is a relation between unemployment and wage or price increases (*8*; see also *3*, *4*, *9*).

States. Thus, for the United States, during a period of chronic slack the deficit in the balance of payments may be heavily weighted by long term capital exports, whereas a period of rapid growth and high employment is associated with a decline in capital exports and a run up in the current imports component of the balance of payments.

In addition to the direct effect upon the balance of payments from rising aggregate demand, which operates by way of imports and capital movements, there is an indirect effect running by way of the price level changes to the balance of payments. That is, a rise in home prices relative to prices of trading partners and competitors in a foreign country will adversely affect the balance of trade. Thus, increasing aggregate demand to lower unemployment rates will adversely affect the balance of payments via two paths. It is clear that those who weight the balance of payments goal heavily will tend to define as adequate a lower level of aggregate demand than would those who did not consider balance of payments equilibrium as a leading objective.

The particular structural attributes of interest with respect to the balance of payments are tariff rates—including interest equalization equivalents—and various direct or administrative controls upon capital exports and commodity imports. Another structural attribute related to the balance of payments—one that will be considered when policy implications are discussed—is the international monetary system.

The fourth standard goal of aggregate policy is economic growth. In the policy discussion of growth and growth rates two things have been confused. These are the achieved rate of growth of actual income and the rate of growth of capacity, or full employment, income. When the economy moves from a period of considerable slack, as in 1960–61, towards a period in which capacity is more fully utilized, as in 1966, the achieved rate of growth of income exceeds the rate of growth of capacity. The policy goal of economic growth deals with the growth of capacity, not with the rates of growth achieved during a shift from a slack economy to an economy of relatively full employment. Nonsustainable rates of growth of income can be attained during a business cycle expansion as previously idle capacity is absorbed.

The relation beween aggregate demand and economic growth correctly defined is clear if large-scale excess capacity (unemployment) exists. Under these circumstances excess capacity acts as a damper on any scale increasing investment. In addition, the general low level of profits (especially as measured by net corporate cash flows) acts as a damper on the financing of innovations. Thus, large-scale unemployment or its equivalent, grossly inadequate aggregate demand, tends to decrease the rate of growth of capacity.

However, this does not mean that there is necessarily a marked difference in the rate of growth of capacity income during a period of "high level stagnation" such as 1953–60 and a period of a relatively full employment such as 1961–66. The evidence that higher capacity utilization is related to higher growth rates centers around the rate of growth of investment as compared to total income or consumption. If investment grows more rapidly, relative to income, during a period of high level employment than during a period of more unemployment, then there is some presumption that capacity is growing more rapidly.

In table 1 the take off of investment, starting in the first quarter of 1965 and continuing through the second quarter of 1966, is evident. Thus during a year and a half, while aggregate demand was increasing rapidly (note the increasing rate of increase of the gross national product (GNP) implicit price deflator), the ratio of investment to GNP was increasing. We can presume that the economic buoyancy reflected in the rate of growth of investment meant that technical progress was being "welcomed" by investors. All in all, the evidence of this expansion is that some investment impact can be expected from a sustained expansion, an impact that might lead to a rise in the rate of growth of capacity.

Table 1 incidentally also illustrates an instability in the pattern of growth of actual income over the 2 years 1964–66 that might "explain" part of the acceleration in the rate of increase of prices, as measured by the GNP deflator, over this period.

The expansion prior to the first quarter of 1965 exhibited fairly consistent rates of growth of capacity, consumption, and investment—with investment being a bit "jumpy." Through most of this period government expenditures lagged. Between the second quarter of 1963 and the second quarter of 1965 the rate of increase of government spending was much lower than the rate of increase of gross national product. The public sector was not a leading sector.

Beginning with the first quarter of 1965 and continuing for six quarters, the rate of increase of investment expenditures reached clearly unsustainable levels: Investment cannot long continue to grow at the rates shown in table 1 while aggregate capacity grows much more slowly. The rapid growth of investment activity meant that the incremental pattern of production and employment was dissimilar to the initial condition pattern.

Beginning in the fourth quarter of 1965 a rapid increase in government expenditure began. For the last two quarters (fourth of 1966 and first of 1967) the rate of growth of government expenditure has been more than twice as great as the high estimates of how fast the economy can grow.

Thus the observed growth of income since 1961 can be split into three parts: the first characterized by a rather balanced private sector with a lagging government, the second during which private investment became a leading sector growing at a nonsustainable rate, and a third during which private investment slackened precipitously and government

TABLE 1.—*Gross national product, components thereof and the gross national product deflator: annual rates of changes in year following initial quarter (1958 dollars)*

Initial-terminal quarter	GNP	Consumption	Investment	Government	GNP price deflator
02.61–02.62	7.1	4.7	16.5	8.3	1.4
03.61–03.62	6.4	5.0	13.2	5.7	1.2
04.61–04.62	5.2	4.6	8.0	5.4	1.1
01.62–01.63	4.1	4.6	1.9	4.5	1.1
02.62–02.63	3.5	4.5	2.0	.8	1.3
03.62–03.63	4.0	4.7	3.1	2.0	1.3
04.62–04.63	4.4	3.8	8.7	.9	1.4
01.63–01.64	5.3	4.9	7.5	.1	1.5
02.63–02.64	5.9	5.7	6.2	4.2	1.5
03.63–03.64	5.5	6.6	3.1	1.2	1.8
04.63–04.64	4.5	5.9	2.9	.6	1.8
01.64–01.65	5.4	5.9	13.4	1.1	1.7
02.64–02.65	5.1	5.7	11.3	−.1	1.9
03.64–03.65	5.7	5.1	14.2	3.3	1.7
04.64–04.65	7.5	7.3	13.3	5.9	1.7
01.65–01.66	6.7	6.6	7.9	6.1	2.3
02.65–02.66	5.9	5.1	11.5	6.4	2.8
03.65–03.66	5.1	4.9	4.7	8.6	3.3
04.65–04.66	4.1	3.0	4.1	10.0	3.5
01.66–01.67	2.6	2.2	−7.5	12.9	3.3

Source: Federal Reserve Bank of St. Louis.

became a leading sector growing at a nonsustainable rate. As the growth of actual income shifted from being balanced, to being led by investment, to being led by government spending, the rate of increase of prices accelerated.

Of course this acceleration in the rate of increase of prices was also associated with a decrease in the unemployment rate. The raw data seem to validate a Phillips curve type of relation—but the attainment of rate of increase of the GNP deflator in excess of 2 percent per year occurred only after these gross structural changes in the growth pattern took place. For policy considerations, where sharp shifts in the composition of output are not contemplated, the relevant question has to deal with the rate of increase of prices in a more stable and sustainable growth pattern.

The structural characteristics that affect the relation between aggregate demand and economic growth mainly operate through "tax" system characteristics. Most models of economic growth emphasize investment as the carrier of innovations as well as the vehicle for expanding productive capacity. Thus, shifting the composition of total demand by decreasing the consumption-income ratio and raising the investment-income ratio becomes a proximate policy objective. In part, the instruments to achieve this are rulings relating to depreciation allowances and items such as investment tax credits. The items introduced into the tax side of fiscal policy to expedite growth tend to be regressive changes in the progressiveness of the tax schedule.

On the spending side of fiscal policy, emphasis upon subsidizing research and education—both of which generate demand for skilled and already highly paid persons—has been a corollary to emphasizing growth as an objective. In many ways emphasis upon economic growth will tend to shape tax and spending policies in favor of the already affluent.

An emphasis upon economic growth tends to downgrade job-security-centered objectives of labor: the tendency is to substitute policy guaranteeing jobs in general for policy guaranteeing the particular job. However, "featherbedding" seems to be an issue in the United States only when unemployment rates are high. The U.S. labor force seems willing to accept changing techniques and seems to demand very little compensation for the loss of job security.

The Elimination of Poverty as a Policy Goal

To the standard policy goal of full employment, reasonable price stability, balance of payment equilibrium, and economic growth a new major policy goal has been added—end poverty in a reasonably short time. I will assume the above is true in spite of recent political setbacks to the program. How does the addition of this goal affect the "weight" to be attached to the other goals.

If increasing employment helps reduce poverty now, whereas economic growth is neutral toward reducing poverty now and will affect the proportion in poverty only in the long run, then the weight of employment relative to growth increases. Thus, the mix of policies will lean towards achieving more of those goals which help eliminate poverty and lean away from achieving those goals which either do nothing to alleviate poverty or worsen the poverty problem.

The dimensions of the poverty problem have been stated most often in terms of the number of households or persons whose income falls below some standard. Although this minimum income approach is a simple way of posing the problem, it does lead to quibbles as to the appropriate "poverty" line. In addition it has the grave fault that it opens the way to a fundamentally superficial solution to the serious problem: give the present poor enough "money" by way of transfer payments and services in kind to bring them up to the minimum standard of disposable income.

An alternative is to view poverty as a problem in the distribution of income. The scope of the poverty problem is broadened to include the determinants of the size distribution of income, and policy with respect to poverty becomes policy with respect to income distribution.

From the perspective of "poverty" income, distribution problems can be broken into two parts. The first part is the Ricardian "factoral" distribution of income between the classical trio: land, labor, and capital. The second part is the size distribution of earnings from labor. The problem thus becomes the determination of relative wages among different industries and occupations.

Adding the elimination of poverty to the policy objectives affects the significance of other policy goals in two ways. First, there is the direct relation between the goal and the extent of poverty. Second, there is the relation between the particular goal and income distribution—in particular the distribution of income from labor.

Tight Full Employment

Introduction

In the light of the campaign against poverty the importance of full employment as a policy goal increases. The American economy operated with considerable labor market slack—even accepting a very modest definition of employment goals—starting in 1954 and continuing through 1965. The income gap between potential and actual income was greater even in 1966 than would have been needed to move all those then living in poverty well above the "line" used to define poverty. That is, the lot of those living in poverty could have been substantially improved without requiring the lot of anyone else to deteriorate.

To the extent that the War on Poverty has social as well as economic targets, the importance of full employment as a policy objective is enhanced. The value to society of jobs for the chronically unemployed may be significantly greater than the value of output produced; employment has external social benefits. That is, it may be better to eliminate poverty by means of income from jobs than to eliminate poverty by transfer payments. The above proposition is taken as a postulate in what follows, as is the proposition that general and by right transfer payments are preferable to special and by discretion (case) transfer payments. The rationalization of these postulates lies in sociology and ethics.

In 1965 some 6.7 million families (11.5 million households) were "poor" by the standard definition. Of these poor families, some 4.8 million were headed by a male and some 1.9 million were headed by a female. Of the 4.8 million poor families headed by a male, some 2.7 million were poor in spite of the fact that their head worked at a full-time job during the year. About 1.7 million of these male heads of families were employed full time during the year.

Almost half of the families living in poverty in 1965 would certainly have benefited from better labor market conditions, and some 60 percent of these families would have benefited only if income from jobs were raised. The other 40 percent would have benefited directly from lower unemployment.

Between 1962 and 1965 the overall unemployment rate fell from 5.5 to 4.5 percent. In the January 1964 Report of the Council of Economic Advisors, some 9.3 million families were listed as living in poverty in 1962. The January 1967 Report lists some 6.7 million families living in poverty in 1965. The reduction of the aggregate unemployment rate and economic growth was associated with a reduction by some 28 percent of the number living in poverty over a 4-year period. In spite of the reduction in the number of families living in poverty, it remained true in 1965 that at least half of the families living in poverty do so either because of unemployment or because of low incomes from jobs.

Given that the poverty problem remains largely a question of job opportunities, the precise definition of the employment objective remains an open question. Definitions of full employment in terms of wage-price and unemployment relations are quite common. This aggregate Phillips curve approach has tended to generate definitions of full employment that lead to slack labor market conditions. From the perspective of the War on Poverty, a better definition of the full employment objective would be in terms of labor market conditions. Perhaps a useful definition would be that full employment exists whenever, over a broad spectrum of occupations and demographic attributes of the population as well as a large proportion of the geographical regions, more jobs are open at going wages than the number of unemployed workers. This definition of full employment is in terms of desired labor market conditions. It will be called tight full employment in what follows. It allows for inconsistency to exist between employment and price level goals, whereas defining target unemployment rates in terms of the Phillips curve does not. In addition, the Phillips curve approach seems to beguile policymakers and analysts into cutting the employment goal to fit the price level stability cloth.

For practical purposes it is more convenient to define full employment in terms of a target-

TABLE 2.—*The poor and their work experience, 1965* [1]

Work experience of head of household	Poor households (millions) [2]		Poor families			
			Number (millions)		Incidence of poverty (percent) [3]	
	Male head	Female head	Male head	Female head	Male head	Female head
Total	6.1	5.4	4.8	1.9	11	37
Aged (65 years and over)	1.8	2.4	1.2	.3	21	29
All others	4.3	3.0	3.6	1.5	10	40
Did not work in 1965	.7	1.5	.5	.8	38	66
Ill or disabled	.4	.2	.3	.1	42	(4)
Other reasons	.3	1.3	.2	.8	33	66
Worked at part-time jobs	.5	.5	.4	.2	34	44
Worked at full-time jobs	3.0	1.0	2.7	.5	8	23
Employed 39 weeks or less	.8	.4	.6	.2	23	49
Employed 40–49 weeks	.4	.1	.4	.1	13	24
Employed 50 weeks or more	1.8	.4	1.7	.2	6	15
0–3 children	1.0	.1	1.0	.1	4	11
4 or more children	.7	.1	.7	.1	17	65
South [5]	.9	.2	.9	.1	11	24
White [5]	.5	.1	.5	(6)	7	11
Nonwhite [5]	.4	.1	.4	.1	36	51
Rest of country [5]	.9	.3	.8	.1	4	10
White [5]	.8	.2	.7	.1	4	8
Nonwhite [5]	.1	.1	.1	(6)	10	22

Source: 1967 Economic Report of the President, p. 139.

[1] Numbers in this table are based on the Current Population Survey. An enlarged survey of the poor, now in progress, may show somewhat different results due to sampling error and the use of different interviewing techniques.

[2] Households are defined here as the total of families and unrelated individuals.

[3] Poor families as percent of the total number of families in the category.

[4] Percent not shown because of small number of families.

[5] Estimated by Department of Health, Education, and Welfare.

[6] Less than 50,000.

Note. Poverty is defined by the Social Security Administration poverty-income standard; it takes into account family size, composition, and place of residence.

Detail will not necessarily add to totals because of rounding.

measured unemployment rate, accepting a particular measurement technique as generating, if not a good count, at least a good index. The Council of Economic Advisors has taken as an "interim" goal a 4-percent measured unemployment rate. By their measurement technique the United States was at the interim full employment target in the fourth quarter of 1965 and remained at or below this target throughout 1966. In what follows it will be argued that a 2.5- to 3.0-percent measured unemployment rate is a better definition of full employment. By this definition even in 1966 there was a significant gap between potential and actual income.

The Measure of Tight Full Employment

There are as yet no generally available job vacancy data which can be used to estimate the positive or negative excess of vacancies over job openings by race, region, sex, and skill categories. Thus it is necessary to guess at the unemployment rates which should prevail in order to generate tight full employment.

One way to determine the limits to attainable unemployment rates is to examine the experience of other countries. Table 3 presents unemployment rates for 1960–62 for five European countries reestimated to conform to the U.S. definitions. Aside from Italy, all of these countries exhibited rates substantially lower than the U.S. interim target rates of 4 percent.

Gordon (2) summarized his findings on unemployment rate targets as follows:

> Today in Western Europe 2 per cent unemployment is the target most frequently mentioned. When translated into American definitions, this may mean an unemployment rate from something below 2 per cent to perhaps 3 per cent as a maximum. Virtually all countries are very loath to announce an official quantitative target. But various scraps of evidence permit one to infer the approximate goal in some of the leading European countries today, expressed in terms of American definitions, about as follows:
>
> | | Per Cent |
> |---|---|
> | France | 2.0–2.5 |
> | Germany | 1.5–2.0 |
> | Sweden | 1.2–1.5 |
> | United Kingdom | 1.8–2.7 |

The applicability of the European experience to the United States depends upon assuming that labor market operating conditions are similar. One argument that could be made centers around the heterogeneity of the United States labor force. Fortunately, data are available on the structure of unemployment rates by a variety of demographic and skill classes. By setting reasonable targets for such

TABLE 3.—*European unemployment rates re-estimated to conform to U. S. definitions, 1960–62*

Year	France	Germany	Italy	Sweden	United Kingdom
1960	1.9	1.0	4.3	1.6	2.4
1961	1.8	.5	3.7	1.5	2.2
1962	1.8	.4	3.2	1.5	2.8
Average	1.8	.6	3.7	1.5	2.5

Source: Adapted from Gordon (*2*).

demographic and skill classes and assuming that the structure of unemployment rates does not change radically, implications of the various targets for the overall rate can be drawn.

The structure of unemployment rates for each year is defined as the set of specific class rates divided by the overall rate for the year. The variation in the pattern of these rates over years indicates the stability of the structure. These specific class relative rates for various demographic and skill groupings for each year of the current expansion (1961 through 1966) are shown in tables 5, 6, and 7.

Over this period the overall unemployment rate was reduced from 6.7 percent in 1961 to 3.8 percent in 1966. Before examining the specific rates one warning might be in order. The war in Vietnam has led to an increase in the size of the armed services. As a result many of the most employable of the younger white and nonwhite males are not in the civilian labor force. In addition, the uncertainty because of the war raises the cost to the employer of hiring a draft-eligible male. Thus the pattern of unemployment rates for younger males may reflect special circumstances rather than general market behavior as overall unemployment rates are lowered.

Before continuing, it is worth noting that the reduction in the aggregate unemployment rates did not proceed smoothly over the period. The first year of the expansion witnessed a 1.2-percentage point decrease in the unemployment rate whereas in the second year an increase of .2 percentage point occurred. The 3 years following 1963 saw a succession of decreases in unemployment rates: a reduction of .5 percentage point in 1964 was followed by reduction of .7 percentage point in 1965 and again in 1966. This stop-go reduction of unemployment rates placed more pressure on prices in the economy than would have occurred if the decline had been steadier.

Table 5 gives relative unemployment rates for males and females by marital status. It is evident that some change in relative unemployment rates for this classification of the labor force did occur. Unemployment for married men with wife present was reduced from about .7 of the 6.7-percent rate of 1961 to .50 of the 1966 rate of 3.8 percent. Other relative unemployment rates did not change as markedly except for the rate for single females, which increased to 2.05 of the 1966 unemployment rate of 3.8 percent, from 1.30 of the higher 1961 unemployment rate of 6.7 percent. This change in ratio reflects the fact that while the overall rate was falling rapidly, the rates for single women fell by but .9-percentage point.

Married men with wife present are a stable, reliable core of the labor force. Our target for this subgroup should not be significantly lower than the best of the European experience. Thus a target rate for this group of about 1.2 to 1.5 percent—equivalent to the total Swedish target—seems reasonable. This would generate an overall target, using 1966 relative rate, of from 2.4 to 3 percent.

In table 6 the relative unemployment rate by sex and color are given. The expansion has seen some

TABLE 4.—*Unemployment rates and changes in the rate and rates of growth of gross national product, 1961–66*

Year	Aggregate unemployment rate	Change in the unemployment rate	Rate of growth of—GNP		GNP price deflator
			Current prices	1958 prices	
1961	6.7				
1962	5.5	−1.2	7.7	6.5	1.2
1963	5.7	+.2	5.4	4.0	1.3
1964	5.2	−.5	7.0	5.3	1.6
1965	4.5	−.7	7.8	5.9	1.8
1966	3.8	−.7	8.6	5.4	3.0

Source: Unemployment data: 1967 Economic Report of the President. Rate of growth data: Federal Reserve Bank of St. Louis, *Triangles of U.S. Economic Data*, Feb. 3, 1967.

TABLE 5.—*Unemployment rates relative to overall rate, by sex and marital status, 1961–66*

Sex and marital status	1961	1962	1963	1964	1965	1966
Male:						
Total	.970	.964	.930	.904	.889	.868
Single	1.955	2.036	2.175	2.212	2.244	2.263
Married, wife present	.687	.655	.597	.539	.533	.500
Widowed, divorced, separated	1.537	1.800	1.684	1.712	1.600	1.474
Female:						
Total	1.075	1.127	1.140	1.192	1.222	1.290
Single	1.299	1.436	1.561	1.673	1.822	2.053
Married, husband present	.955	.982	.947	.981	1.000	.974
Widowed, divorced, separated	1.105	1.164	1.175	1.231	1.200	1.237

significant changes in the structure of unemployment among these demographic classes. For each age group of white males between the 20–24 year group and the 55–65 year group there has been a sharp fall in the relative unemployment rate. Similar significant reductions in the relative unemployment rates for non-whites in the 25–34 through 55–64 year age groups occurred. Given that the relative rates for both white and nonwhite males declined, it follows by arithmetic that the relative rates for females rose.

Given the structure of relative rates, a reasonable target would be to achieve for white males between ages 25 and 54—the heart of the labor force—unemployment rates as good as the best European rates. If we take the German unemployment rate of 1960 as a target for white males 25 through 54, the overall unemployment rate, given 1966's relative rate, would be about 2 percent.

If a 4-percent unemployment rate is adopted as the target for nonwhite males aged 25 to 54, then the target overall rate would be about 3.4 percent.

Table 7 gives the relative unemployment rates by occupations of the experienced labor force. The expansion saw a decrease in the relative unemployment rates of craftsmen, foremen, and kindred workers; operative and kindred workers; and laborers, except farmworkers. The expansion seemingly reversed the trend toward higher blue collar unemployment rates. Whereas the unemployment rate of these blue collar classes decreased relative to the overall unemployment rate, the unemploy-

TABLE 6.—*Unemployment rates relative to overall rate, by sex and color, 1961–66*

Color, sex, and year	Total, 16 years and over	16 and 17 years	18 and 19 years	20–24 years	25–34 years	35–44 years	45–54 years	55–64 years	65 years and over
White male:									
1961	.851	2.463	2.254	1.493	.731	.597	.657	.791	.776
1962	.836	2.746	2.309	1.455	.691	.564	.636	.746	.746
1963	.825	3.123	2.491	1.368	.684	.509	.579	.702	.719
1964	.788	3.096	2.577	1.423	.577	.481	.558	.700	.692
1965	.800	3.267	2.533	1.311	.578	.511	.511	.689	.756
1966	.737	3.290	2.342	1.079	.553	.447	.447	.658	.790
White female:									
1961	.970	2.537	2.030	1.254	.985	.856	.716	.642	.552
1962	1.000	2.836	2.054	1.400	.982	.818	.673	.618	.727
1963	1.018	3.175	2.316	1.298	1.018	.807	.684	.614	.526
1964	1.058	3.288	2.538	1.365	1.000	.865	.692	.673	.654
1965	1.111	3.333	3.978	1.400	1.067	.911	.667	.600	.600
1966	1.132	3.816	2.816	1.395	.974	.868	.711	.579	.711
Nonwhite male:									
1961	1.910	4.627	3.567	2.782	1.925	1.597	1.522	1.567	1.403
1962	1.982	3.982	3.964	2.655	1.909	1.564	1.509	1.746	2.164
1963	1.842	4.737	4.807	2.719	1.667	1.404	1.246	1.298	1.772
1964	1.712	4.981	4.442	2.423	1.481	1.192	1.135	1.558	1.596
1965	1.644	6.022	4.489	2.067	1.378	1.133	1.133	1.200	1.156
1966	1.658	5.921	5.395	2.079	1.290	1.105	1.079	1.158	1.290
Nonwhite female:									
1961	1.761	4.642	4.209	2.911	1.657	1.597	1.105	.940	.970
1962	2.000	5.055	5.673	3.309	2.091	1.618	1.291	.655	.673
1963	1.965	7.035	5.597	3.281	2.053	1.439	1.070	.842	.632
1964	2.039	7.019	5.615	3.519	2.154	1.500	1.173	.731	.423
1965	2.044	8.400	6.178	3.044	1.867	1.689	.978	.867	.689
1966	2.263	9.158	7.684	3.316	2.132	1.111	1.111	.868	1.053

TABLE 7.—*Unemployment rates of experienced workers relative to overall rate, by major occupation groups, 1961–66*

Occupation group[1]	1961	1962	1963	1964	1965	1966
Professional, technical, and kindred workers	.299	.309	.316	.327	.333	.342
Farmers and farm managers	.060	.055	.088	.096	.089	.105
Managers, officials, and proprietors except farm	.269	.273	.263	.269	.244	.263
Clerical and kindred workers	.687	.709	.702	.712	.711	.737
Sales workers	.702	.746	.737	.654	.733	.711
Craftsmen, foremen, and kindred workers	.940	.927	.842	.808	.800	.737
Operatives and kindred workers	1.433	1.364	1.298	1.250	1.222	1.132
Private household workers	.881	.891	.912	.943	.933	.947
Service workers, except private household	1.105	1.164	1.088	1.173	1.222	1.263
Farm laborers and foremen	.851	.782	.965	1.115	1.067	1.079
Laborers, except farm and mine	2.164	2.255	2.123	2.039	2.100	1.921

[1] No rates were given for the group "Persons with no previous work experience."

ment rate among the white collar jobs—professional, technical, and kindred workers; clerical and kindred workers; and sales personnel—increased at least slightly. The argument that there are employment opportunities only for the educated was not borne out by experience in the expansion.

If the policy target is to reduce the unemployment rate of the highly trained and educated professional, technical, and kindred workers to the average unemployment rate in Germany in 1960–62, then the overall rate will be about 1.7 percent with 1966 relative rates. If the policy objective is to reduce the unemployment rate for laborers, except farm and mine, to 4 percent, then the overall unemployment rate would be about 2 percent.

That is, in terms of both the unemployment rates other advanced countries have achieved and the setting of attainable targets for unemployment rates in reasonably homogeneous subclasses of the labor force, an overall rate in the neighborhood of 2 to 3 percent does not seem like a heroic policy target. However, as will be pointed out, some structural changes may be required before this overall rate can be achieved.

Okun's Law

What I choose to call Okun's law (7) states that for each percentage point decrease in unemployment there will be approximately a 3-percent increase in GNP. The evidence from the expansion of 1961–66 is on the whole consistent with Okun's law, although it may indicate that a somewhat smaller increase in GNP per percentage point decrease in unemployment rates takes place.

Table 9 shows that if for each year we subtract twice the decrease in the unemployment rate from the rate of growth of actual real GNP, we obtain estimates of the growth of capacity GNP that clusters clearly around 4.3 percent. If we multiply the decrease in unemployment by 3 rather than 2, we get estimates of the growth of capacity GNP that average 3.7 percent, but the annual estimates have a much wider dispersion. The evidence seems to indicate that a 1-percent point reduction in the

TABLE 8.—*Reasonable target rates of unemployment*

Base class	Class target	Overall rate
	Percent	*Percent*
Married men, wife present	1.2 to 1.5	2.4 to 3.0
White males, age 25 to 54	1	2.0
Nonwhite males, age 25 to 54	4	3.4
Professional, technical and kindred workers	.6	1.7
Laborers, except farm and mine	4.0	2.0

TABLE 9.—*Relation between growth in actual gross national product and decrease in unemployment, 1962–66*

Terminal year	Rate of growth of actual GNP in 1958 dollars	Change in the unemployment rate	Rate of growth of capacity assuming GNP of—	
			3 percent per percentage point unemployment	2 percent per percentage point unemployment
			Percent	*Percent*
1962	6.5	—1.2	2.9	4.1
1963	4.0	+ .2	4.6	4.4
1964	5.3	— .5	3.8	4.3
1965	5.9	— .7	3.8	4.5
1966	5.4	— .7	3.3	4.0
Average			3.7	4.3

unemployment rate requires a real aggregate demand growth of some 2 or 3 percent more than the rate of growth of capacity. There is no indication in table 9 that carrying unemployment rates down to 3.8 percent saw any change in the general nature of the relation embodied in Okun's law.

Thus to continue to reduce unemployment rates at the rate of .5 to .7 percentage points per year would require a rate of growth of real aggregate demand averaging about 5.5 percent per year. Given the tendency for the GNP price deflator to rise, this may mean that a rise in aggregate demand at a rate of 8 percent per year for 2 years beyond 1966 is needed to bring unemployment rates down to or below a 3-percent overall rate.

If a 2.5-percent measured unemployment rate had ruled in 1966 rather than the observed 3.8 percent, then by Okun's law, as modified above, GNP would have been some 2.6 to 3.9 percent larger. GNP in 1966 was $740 billion. Even at the low unemployment rates of 1966, the cost in terms of GNP of the slack relative to tight full employment was in the neighborhood of $19 to $29 billion. This is much greater than the $11 billion that presumably it would take in transfer payments to lift all now living in poverty well above the poverty line.

It might be argued that the northern European countries were able to maintain such low unemployment rates because they operated with a large number of imported workers. First of all, there is nothing wrong with imported workers or bracero programs if they are carried out in the context of tight labor markets.

In addition, one very large element of flexibility is built into the American economy because of the chronic migration from the rural areas to the urban areas. The gross outflow per year is very large but the net outflow, because of returns to rural areas, is quite modest; therefore, a sizable increase in the rate of increase of the industrial labor force is possible if the urban retention rate rises. The level of urban retention rates seems closely related to urban job opportunities. A rise in aggregate demand that might, under other circumstances, lead to inflationary pressure would under these circumstances lead to faster absorption of formerly rural population into the urban society. Thus, a tighter urban labor market would go far to eliminate rural poverty.

Size Distribution of Earnings

The move from the current slack full employment to a tight full employment will directly benefit those who are in poverty because of unemployment or part-time work. It will not directly benefit those who are in poverty even though they worked full time at a job. For these poor, either a rise in their earnings from work or some scheme of wage supplements is necessary. The expectation is that some of the employed poor will benefit from tight full employment as they move into higher wage jobs. However, some of those who move from being unemployed to employed will move into jobs that yield poverty incomes.

Therefore, one facet of any serious concern about poverty is a concern about the size distribution of income. As long as a substantial portion of those living in poverty—or even close to poverty—do so in spite of working full time during the year, the root of this component of poverty lies in the existence of jobs that pay too little.

Various explanations of the differentials in wage earnings among industries and occupations have been proposed. The current or recent fashion is to explain differentials in earnings in terms of the differences in investment. These investments in humans could be on-the-job training, or craft training, or general education.

However, before we venture a conventional reply to the question of the determinants of relative earnings, it is perhaps best to look at some data. This is especially so because of the wide difference in the average weekly earnings of workers in different industries as well as the changes that occurred in relative earnings during the postwar period.

Our analysis of relative wages takes 1948 as its initial observation. The year 1948 is too close to the end of World War II, with its elaborate wage and price controls, to serve as a model for relative wages. However, 1948 was the terminal year for a protracted period of tight full employment. From 1948 through 1961 the trend was toward higher unemployment rates. The expansion of 1961–66 saw aggregate unemployment rates fall from 6.7 to 3.8 percent. The question is whether the slack affects relative earnings—and whether the gradual tightening over a 6-year period also affects relative earnings. Does chronic labor market slack widen the range of earnings among occupations, whereas a long period of labor market tightness narrows the spread?

The analysis examines relative earnings in the 21 two-digit manufacturing industries plus mining, contract construction, wholesale trade, and retail trade. For each year the wage in each of the 25 sectors is divided by average earnings in all manufacturing to get relative wages.

In 1948, weekly earnings in four industries (table 10) were in excess of 120 percent of the average earnings, and three industries exhibited earnings that were less than 80 percent of the base. In sharp contrast, in 1966 weekly earnings in six industries were in excess of 120 percent of all the manufacturing earnings and earnings in six industries were below 80 percent of the base. In other words, in 1948 of the 25 industries, 18 were in the range weekly earnings in all manufacturing ±20 percent; in 1966 only 13 were in this range. (If ± 10 percent of all the manufacturing earnings is used as the central group, in 1948, 12 of the 25 industries were in the range whereas in 1966 only 9 were.)

TABLE 10.—*Average weekly earnings as a ratio to average weekly earnings in manufacturing, 1948, 1953, and 1960–66*

Industry	1948	1953	1960	1961	1962	1963	1964	1965	1966
Mining	1.234	1.178	1.175	1.157	1.143	1.148	1.143	1.148	1.158
Contract construction	1.228	1.226	1.259	1.278	1.268	1.276	1.282	1.283	1.293
Manufacturing	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000	1.000
Durable Goods	1.060	1.087	1.086	1.086	1.268	1.089	1.089	1.092	1.084
Ordnance and accessories	1.078	1.108	1.208	1.224	1.207	1.208	1.187	1.218	1.209
Lumber and wood products	.896	.862	.821	.832	.820	.821	.827	.821	.825
Furniture and fixtures	.919	.893	.838	.827	.821	.821	.820	.816	.813
Stone, clay, and glass products	1.001	.995	1.031	1.031	1.020	1.026	1.024	1.023	1.018
Primary metal industries	1.151	1.198	1.221	1.243	1.240	1.251	1.262	1.248	1.230
Fabricated metal products	1.060	1.085	1.096	1.092	1.085	1.084	1.081	1.083	1.084
Machinery	1.136	1.173	1.165	1.163	1.170	1.166	1.181	1.185	1.202
Electrical equipment	1.026	1.000	1.011	1.023	1.009	.995	.987	.986	.969
Transportation equipment	1.162	1.210	1.242	1.228	1.265	1.271	1.263	1.283	1.267
Instruments and related products	.989	1.030	1.040	1.049	1.033	1.019	1.006	1.007	1.010
Miscellaneous manufactures	.904	.873	.827	.821	.814	.806	.799	.792	.791
Nondurable Goods	.931	.887	.895	.897	.889	.882	.882	.882	.877
Food and kindred products	.920	.901	.959	.961	.951	.946	.943	.931	.925
Tobacco manufactures	.689	.675	.723	.751	.739	.741	.738	.743	.758
Textile mill products	.822	.754	.708	.704	.706	.696	.712	.728	.731
Apparel and related products	.822	.691	.627	.628	.633	.626	.624	.620	.613
Paper and allied products	1.030	1.019	1.060	1.076	1.056	1.063	1.064	1.064	1.063
Printing and publishing	1.226	1.167	1.147	1.137	1.118	1.111	1.110	1.101	1.092
Chemicals and allied products	1.041	1.053	1.150	1.156	1.141	1.132	1.131	1.128	1.118
Petroleum and related products	1.304	1.282	1.322	1.346	1.314	1.322	1.298	1.290	1.288
Rubber and plastic products	1.004	1.031	1.031	1.041	1.036	1.011	1.018	1.021	.995
Leather and leather products	.773	.722	.674	.680	.669	.662	.669	.669	.667
Wholesale and retail trade	.827	.703	.788	.785	.777	.778	.721	.713	.704
Wholesale trade	1.009	.978	1.011	1.013	.996	.998	.996	.988	.990
Retail trade	.784	.705	.695	.693	.682	.682	.628	.620	.611

Not only has there been a marked thinning out of the middle of the range of weekly earnings by industry, but the minimum average weekly incomes as a ratio to the average has decreased. In 1948 only weekly earnings in Tobacco manufactures were below 70 percent of the average. In 1966 three industries exhibited weekly earnings lower than 70 percent of all manufacturing: these were Leather and leather goods, Apparel and related manufacturing, and Retail trade.

A surprising aspect of the developments in relative earnings over the post-World War II period deals with the change in relative earnings. Apparently the rich became richer and the poor poorer, over this period, at least among the industries examined. Of course, richer and poorer is in a relative sense.

Of the 10 industries with the highest relative earnings in 1948, 7 increased their relative earnings, 1 exhibited no serious change, and 2 (Mining and Printing and publishing) had substantial relative declines. In spite of their decline relative to all manufacturing during this period, earnings in Mining and Printing and publishing were 116 and 109 percent, respectively, of the average for all manufacturing in 1966.

Of the eight industries with the lowest relative wages in 1948, seven experienced a substantial decline in their relative wages by 1966. The exception (Tobacco) had the lowest average weekly earnings in 1948 (69 percent of all the manufacturing average earnings). By 1966 this ratio was 76 percent, and Tobacco manufactures were fifth from the bottom in weekly earnings.

Some of the declines in relative earnings were really substantial. Earnings in Apparel fell from 82 to 61 percent of the average for all manufacturing, Furniture from 92 to 81 percent, Leather from 79 to 67 percent, Textiles from 82 to 73 percent, and Lumber fell from 90 to 83 percent. In addition, Retail trade fell from 78 to 61 percent and Miscellaneous manufactures from 90 to 79 percent.

The seven industries that ranked from 11th (Paper and allied products, relative earnings 103 percent), to 17th (Food, relative earnings 92 percent) in 1948 tended to show but slight changes in their relative earnings in the period to 1966. The relative earnings of Electrical equipment dropped 6 percent; all the others remained approximately unchanged in relative earnings, that is the terminal relative earning was ±3 percent of the initial relative earnings.

Thus over the period 1948–66 the rich tended to get richer, the poor poorer and those in the middle tended to hold their own.

The increase in the spread of relative earnings in the United States since 1948 seems to be due mainly to the relative retardation in the increase in earnings in what were already low wage industries. The relative retardation of two high earning industries

in 1948 (Mining and Printing and publishing) are perhaps due mainly to technological changes, although the relative retardation of earnings in Mining is a part of today's rural poverty scene.

That Petroleum refining maintained its relative wages is also of minor interest. If we ignore Tobacco, Printing and publishing, Mining, and Petroleum, for the rest of the industries the change in the percentage points of relative earnings between 1948 and 1966 is highly correlated with relative earnings in 1948 (see table 11).

Many of the industries in which relative wages declined between 1948 and 1966 were sick industries for part or all of this period. In the case of the Textile, Apparel, Leather, and Furniture industries, one response to their difficulties was a rather large-scale migration of plants out of the major metropolitan centers and their historical areas toward small towns and the South.

A theorem seems to fall out of the experience of the postwar period. Marked declines in relative earnings in an industry will be accompanied by changes in the location of the plants in the industry.

If such migration in fact took place—and if it did go towards regions where large postwar outmigrations from agriculture were taking place—then three facets stand out:

(1) The cost of migration was less, being to a nearby industrial job rather than to a distant location. This lower cost tended to induce migration out of rural areas and to lower the retention rates of the urban centers.

(2) The probability that the migrant exchanges rural and agricultural poverty for industrial and urban poverty or near poverty was greater than if the same number of jobs had been created in these industries in their old sites.

(3) In the absence of migration, employment in these industries would have declined in relative size. If appropriate effects to sustain demand and employment had been undertaken, then job openings in high wage industries would have been greater than observed.

From table 12 it seems apparent that whereas most of the spreading of the range of relative earnings—the rich getting richer and the poor poorer—took place between 1948 and 1960, the relative improvement in labor market conditions between 1960 and 1966 did not reverse the trend. If the range of relative weekly earnings is too broad, from a social policy view, then it may not be sufficient to rely upon aggregate demand generating policies to reverse the trend. Of course, during the 1961–66 period only a very half-hearted attempt was made to achieve full employment and it may be that a sustained period of tight full employment is needed to achieve a desired narrowing in the range of relative earnings.

The maintenance of the wide range of relative earnings is evidence that the supply curves of labor to the low relative wage industries remain highly elastic as the overall unemployment rate is decreased. This may reflect their locational advantages: with the continuing migration out of rural areas, the advantageously located low wage industries may in fact be operating with a high reservoir of labor, responsive to job opportunities at unchanging relative wages.

An additional point is worth noting. The 1960–66 period was the era of wage-price guidelines which stated "acceptable" wage increases as a percentage change: this type of wage increases would tend to stabilize the relative earnings patterns.

To summarize: It appears as if the range of relative weekly earnings increased over the postwar period. This increase may have been a response to the rising slack in the labor market that dominated the scene through 1960. The modest tightening of the labor market since that date has not reversed the widening of the range of relative earnings. Thus if the concern about poverty can be translated into a concern about relative earnings it may be necessary to supplement aggregative economic policies with policies designed to narrow the range of earnings from jobs.

TABLE 11.—*Relative earnings (1948) and change in relative earnings (1948–66) by industries*

Industry	1948 relative earnings [1]	Change in relative earnings, from 1948 to 1966
Contract construction	1.228	+.065
Transportation equipment	1.162	+.105
Primary metal industries	1.151	+.079
Machinery	1.136	+.066
Ordnance and accessories	1.076	+.133
Fabricated metal products	1.060	+.024
Chemical and allied products	1.041	+.077
Paper and allied products	1.030	+.033
Electrical equipment	1.026	−.057
Wholesale trade	1.009	−.019
Rubber and plastic products	1.004	−.009
Stone and quarry	1.001	+.017
Instruments and related products	.989	+.021
Food and kindred products	.920	+.005
Furniture and fixtures	.919	−.106
Miscellaneous manufactures	.904	−.113
Lumber and wood products	.896	−.071
Textile mill products	.822	−.091
Apparel and related products	.822	−.209
Retail trade	.784	−.173
Leather and leather products	.773	−.099

[1] Earnings in relation to Manufacturing, as given in table 10.

Price Stability

In our discussion of price stability, we ignore the impact of rising prices upon the nonpoor. Price stability may affect the two classes of the poor—

TABLE 12.—*Relative earnings and ranking of relative earnings, 25 industries, 1948, 1960, and 1966*

Industry	Relative earnings			Rank of relative earnings		
	1948	1960	1966	1948	1960	1966
Petroleum and related products	1.304	1.322	1.288	1	1	2
Mining	1.234	1.175	1.158	2	6	7
Contract construction	1.228	1.259	1.293	3	2	1
Printing and publishing	1.266	1.147	1.092	4	9	9
Transportation equipment	1.162	1.242	1.267	5	3	3
Primary metal industries	1.151	1.222	1.230	6	4	4
Machinery	1.136	1.165	1.202	7	7	6
Ordnance and accessories	1.076	1.209	1.209	8	5	5
Fabricated metal products	1.060	1.096	1.084	9	10	10
Chemical and allied products	1.041	1.150	1.118	10	8	8
Paper and allied products	1.030	1.060	1.063	11	11	11
Electrical equipment	1.026	1.011	.969	12	15	16
Wholesale trade	1.009	1.011	.990	13	15	15
Rubber and plastic products	1.004	1.031	.995	14	13	14
Stone and quarry	1.001	1.031	1.018	15	13	12
Instruments and related products	.989	1.040	1.010	16	12	13
Food and kindred products	.920	.959	.925	17	17	17
Furniture and fixtures	.919	.838	.813	18	18	19
Miscellaneous manufactures	.904	.827	.791	19	19	20
Lumber and wood products	.896	.821	.825	20	20	18
Textile mill products	.822	.708	.731	21	22	22
Apparel and related products	.822	.627	.613	22	25	24
Retail trade	.784	.695	.611	23	23	25
Leather and leather products	.773	.674	.667	24	24	23
Tobacco manufactures	.689	.723	.758	25	21	21

those who actually or potentially receive income from jobs, and those who are mainly dependent on transfer payments—in quite different ways. To the extent that rising prices are a correlate of tighter labor market conditions, the improvement in job and income opportunities for the present unemployed and low wage employed is more than ample compensation to them for whatever hardships modestly rising prices bring. (Even the price rise of 1966 was modest by world standards.) For those who receive income by transfer payments, there is evidence that in the long run many of the transfer payments by right (social security, veterans pensions, etc.) keep up with price level increases. However, in the short run there is a lag which lowers the real income of these poor.

There is no evidence that the generosity of the public with respect to "case load" or discretionary transfer payments is such that a quick adjustment for price increases takes place. If such budgeted programs are not adjusted, once again some of the poorest are adversely affected by price level increases.

The casual or easy linking of price level increases to overall labor market tightening, however, is suspect. The price increase of 1966 was not a wage push inflation—in fact, for much of the labor force real wages went down—and it was not a delayed response to excessive wage increases earlier in the expansion. There was nothing in labor market conditions, as measured by overall unemployment rates, that made for a rapid run up in food prices during the year. Until the effects of special product and labor market circumstances are taken into account, too much weight should not be placed upon the price level increase of 1966 as an argument with respect to the relation between overall unemployment rates and prices.

From the perspective of the War on Poverty, some building of a consumers price level adjustment into social security and other payments (both by right and discretionary transfer) would be highly desirable. If this were done, then a portion of the adverse effect that modest inflationary pressures have upon the poor will be offset.

It is worth noting that the GNP price deflator has shown a tendency to rise from between 1.5 and 1.8 percent per year even with slack labor markets. At most the special rise in the deflator caused by the labor market tightening of 1966 was the difference between 3.3 percent and 1.5 or 1.8 percent. This is a modest price to pay for the reduction in the number of families living in poverty that has taken place in the expansion.

All in all, price stability is downgraded in importance from the perspective of a serious commitment to end poverty, especially if some price adjustments for transfer payment receivers can be regularized. However, to the extent that the War on Poverty is serious and the belief that income from jobs is preferable to a high level dole (even if it is called a negative income tax) then, if the relation between tight full employment and price level increases as stated in most empirical Phillips curves is valid, some serious experimentation with wage and price controls may be necessary.

Another aspect of the wage-price problem as related to the War on Poverty requires attention. Some inflationary pressure from wages on prices is good from the perspective of the War on Poverty. In the section on Size Distribution of Earnings it was pointed out that the range of relative earnings has widened since 1948 and that the expansion of 1961–66 has witnessed no perceptible reversal of the trend; if anything the trend has continued. Some pressure to push low wages up relative to high and average wages seems desirable. Such pressures could come from the market or, if necessary, from incomes policy. However, inasmuch as regular wage increases reflecting productivity increases are the now normal expectation for organized high wage workers, this required narrowing of the spread of relative wages can come about only if wages in the low wage industries increase faster than productivity. Thus the price of the product of low wage industries will need to rise, relative to other prices. Any price level increase because of this effect is an inherent part of any attempt to decrease poverty by way of employment.

As one of the low wage industries is retail trade, such a rise in prices may have a large impact on the consumers price index: the paths of consumer and wholesale prices will diverge. In addition, sectoral consumer price indices that are heavily weighted with low wage industries and occupations will rise relative to sectoral wholesale price indices where low wage industries are relatively important. Thus, for example, for the War on Poverty to be successful, automobile prices and wages should rise at a slower rate than textile and garment prices and wages.

Thus the addition of the War on Poverty to the set of policy goals downgrades the importance of price stability as a policy goal, especially if the rise in prices has a structure that reflects a "pushing up" of the present low wages.

Economic Growth

As Anderson has shown, economic growth by itself is not a very promising path for the quick reduction of poverty (*1*). To the extent that low wages and near poverty incomes depend upon the absorption of the rural poor into an urban poor, a great deal of growth in income can take place without reducing the population in poverty. This is true to the extent that the urban poor contribute more to measured GNP than do the rural poor. Because of the chronic surplus of labor from the rural sections, the United States in part may be an enclave economy, similar to many underdeveloped economies. In an enclave economy, as long as the reservoir of rural poor is full, a great deal of progress without any substantial improvement in the lot of the poor can take place.

That is, the supply curve of low wage labor in the urban sectors is infinitely elastic at some markup over the going earnings of the rural poor. As long as the reservoir of rural poor is not empty, economic growth will take the form of shifting workers from being rural poor to being urban poor.

If the supply price of labor in the urban sectors results in a poverty or near poverty standard of life, then even though there may be measurable and significant improvements in life standards, all that has happened is that urban poverty has been substituted for rural poverty.

Tax policies have a shape as well as a size. Fiscal measures can be used to affect income distribution. To the extent that increasing the rate of growth is a serious policy objective, the shape of the tax program is affected. Tax measures, such as the investment tax credit, rapid depreciation, and even personal income tax adjustments favoring high income earners, receive favorable consideration under the heading of improving growth prospects. From the perspective of the War on Poverty, increasing personal income tax exemptions, lowering consumption taxes, and increasing transfer payments are desirable. It may be true that not much can be done by way of Federal tax changes directly to improve the lot of the poor. But much can be done indirectly if Federal income tax revenues can be used to support government expenditures that tend to equalize real income by furnishing to all income in kind and to substitute Federal Government financing for regressive State taxes.

From the perspective of the War on Poverty, economic growth as a policy objective takes on many of the attributes of a pie-in-the-sky promise. Nothing directly done to support growth will yield quick benefits to the poor. For example, if education and research are promoted to accelerate growth, the immediate impact of a rise in such expenditures will be an increased demand for the labor of the already affluent. Economic growth as an instrument to fight poverty has little virtue—it really is a "trickle down upon them" view of how to fight poverty. Thus, from this perspective, economic growth as a policy objective is downgraded, because all of the growth-inducing measures that are usually suggested, aside from tight full employment, have a perverse effect upon the relative well-being of the present poor.

On the other hand, economic growth is an attribute of the highly innovative American economy when it functions normally—and full employment does seem to emphasize the innovative aspects of the American economy. Thus, nothing need be done to especially induce growth if the economy is functioning at full employment. As full employment is upgraded as a policy goal with the War on Poverty, a byproduct of the war may be a more rapid growth in capacity GNP than has been achieved, without any special growth-inducing incentives.

Balance of Payments

Within any set of tariffs and other direct constraints on making dollars available to foreigners,

the balance of payments acts as a constraint upon income. That is, within any structure affecting international trade and capital movements, there is a maximum level of income and rate of change of prices that is consistent with balance of payments equilibrium. If aggregate demand is too high for an extended period, a deficit will accumulate that will make it impossible for the United States to satisfy the commitment to pay gold.

From the perspective of the War on Poverty, the target aggregate demand needs to be high enough to generate and sustain a 3-percent unemployment rate. Such a rate initially may be accompanied by a somewhat more rapid increase in prices than we have averaged during 1964–65. These conditions, especially given the war in Vietnam, should lead to a larger deficit in the balance of payments than has been achieved in the past few years. Given the precarious gold position, even assuming the gold cover requirement is removed, such a movement toward tight full employment will cause difficulty in meeting the gold standard commitment.

Under these circumstances something will have to give way. The alternatives are: (1) to slacken on the aggregate demand target, (2) to change the structural elements which help determine imports and capital movements, and (3) to change the monetary rules. If the War on Poverty is serious, then alternative (1) is not available.

There really is little to choose between raising tariffs and tightening foreign capital movement constraints (withdrawing our troops from abroad is not taken as possible here) and changing the monetary rules. Whatever losses in efficiency that would result from constraining tariffs and capital movement regulations are not sufficient to compensate for the benefits of the higher GNP and the social benefits of tight full employment. Thus, a "liberal" presumption against interfering with free international trade becomes of secondary importance where the cost is a significantly lower aggregate demand. Certainly when it came to capital movements, "liberalism" was easily abandoned.

However, free international markets and aggregate demand unconstrained by balance of payments considerations are possible if the rules governing the international monetary system are changed. Basically this would mean abandoning the gold standard—which is a goal that has little domestic payoff.

From the perspective of the war on poverty, whether the abandonment of the gold standard takes the form of paper gold or freely fluctuating exchanges is not a matter of indifference. If the global amount of paper gold to be created is limited by some rule or determined by some central bank to central banks, there would still be some maximum aggregate demand consistent with the rules of the paper gold world. If this maximum is too low to achieve the target unemployment goals, then the price will be an abandonment of War on Poverty targets.

Freely fluctuating exchanges are consistent with the determination of aggregate demand by domestic employment needs. In order to make capital movements easier, and to promote the use of the dollar as an international currency, the Treasury for a fee should sell insurance compensating foreign owners of dollar balances for any increase of the GNP deflator by more than 1.5 percent per year.

That is, it seems, from the point of view of the War on Poverty, that the objective of balance of payments equilibrium is downgraded. A free product and capital market plus fluctuating exchanges seem marginally better than stricter import controls plus capital movement controls and fixed exchanges.

Summary on Policy Trade Offs

The effect of adding the elimination of poverty to the objectives of economic policy is to increase the weight attached to full employment as a goal. If, in the absence of the commitment to end poverty, a particular trade off existed now between full employment and some combination of price level increases and balance of payment position, with the addition of this new objective, tighter full employment at the expense of more rapid price level increases and a deteriorated balance of payments position is acceptable.

Aside from directly helping those in poverty who acquire jobs as a result of tighter full employment, tighter full employment aids in the War on Poverty by raising State and local tax revenues and decreasing welfare rolls. Both of the above will enable the relevant governments to either improve income in kind or raise welfare payments.

In addition, excess demand conditions over a broad spectrum of jobs will aid in upgrading workers. Workers presently in low-paying jobs can move up the occupational ladder. Fulsome job opportunities will help generate additional families with more than one income earner. This can lift families well above the minimum poverty line.

The existence of excess demand for workers in better paying jobs should, if no infinitely large reservoir of very low income people existed, raise wages and weekly earnings in the presently low-paying jobs faster than wages in general rise. However, as long as the huge reservoir of potential migrants from rural America is full, the upward wage pressure on the present low wage occupations may not take place. Thus there may be a need for special programs to affect relative wages.

In order to validate past decisions to invest and for technical progress not to force unacceptable losses upon the owners of inherited capital, which in a progressive society embody techniques that are no longer best usages, aggregate demand must grow. As long as aggregate demand grows, technical dynamism and large-scale gross investment, such as takes place at full employment, guarantee that productive capacity will grow. That is, adequate aggregate demand, defined as demand sufficient to gen-

erate tight full employment, is necessary both to validate past growth-generating behavior and to insure present behavior conducive to growth. Thus, economic growth is a byproduct of a full employment policy. In fact, the flaw in capitalism discussed in the next section centers around the runaway behavior of the propensity to invest if full employment is sustained over an extended period of time.

To the extent that corporate gross profits provide a large share of the financing for gross investment and that households which receive appreciable incomes from property tend to save a large portion of their income, a concern about increasing the growth rate indicates that moves to decrease the share of gross profits after taxes in gross national product are out of order. Thus, attaching significance to growth as a policy goal will not conflict with the War on Poverty as far as the size and rate of change of aggregate demand is concerned. It may conflict with the goal to eliminate poverty with respect to income distribution.

The income distribution goals of the War on Poverty center around three items: (1) raising low wages relative to high wages, (2) larger transfer payments to those not in or not expected to be in the labor force, and (3) elimination of taxes that fall most heavily on the poor.

The weight attached to growth as a policy objective will not necessarily affect the objective of raising low wages relative to high wages. The greater the weight attached to growth the greater the desire to ease taxes in general and profit taxation in particular. Thus there may be a conflict between goals relative to transfer payments and taxes.

That is, inducing growth may conflict with the War on Poverty in terms of the desired structure of the tax system.

The Flaw in American Capitalism

American capitalism is flawed. However, the major flaw may not be that encompassed by the Phillips curve analysis, which entertains the possibility that satisfactory unemployment levels are associated with unsatisfactory rates of increase of prices. Satisfactory, of course, means consistent with the achievement of specified social goals whether they be ethical or pragmatic. From the perspective of this paper, satisfactory means rapid progress toward the elimination of poverty. There is nothing in our experience through 1966 that proves that a balanced growth of aggregate demand relative to productive capacity when there is slack in the labor force, as measured by an excess of unemployment over tight full employment, will lead to rapid price increases. We have not had sufficient experience with the growth of aggregate demand at the same rate as capacity with tight or even slack full employment to venture a good guess as to how prices behave under those circumstances. What we have observed is that unbalanced growth of aggregate demand, which requires a shuffling of resources among sectors, combined with frequent changes in the way demand is unbalanced, which requires reshuffling of resources, leads to an increase in the rate of increase of prices.

To the extent that there is such a Phillips curve problem, even radical structural changes are consistent with the essential nature of American capitalism. Certainly the labor market policies adopted to date, which may or may not turn out to shift the Phillips curve in the appropriate direction, have not changed anything essential.

The flaw in American capitalism centers around the financial system, and the financial system is an essential attribute of the economy. American capitalism is an intensely financial system. The relative free entry into industry, the rapid changes in industrial structure, and the emphasis upon innovations are all in part due to, and are reflected in, the financial structure.

In a private financial system, the portfolios of households, business firms, and financial organizations all reflect speculations as to the future prospects for the economy. Some of the available menu of assets offer income in kind in the form of safety, other assets require the owners to take a full measure of the uncertainty that is inherent in the performance of a decentralized economy which historically has been subject to quite severe business cycles. When the prospects of the economy look very good, as they did, for example, at the end of the soaring year of 1965, all portfolio holders shift from preferring portfolio assets with "protective" features to portfolio assets that are expected to prosper from the now taken-for-granted prosperity.

For business firms—as well as for households (but this is not essential)—portfolio assets include real capital. In times of assured prosperity, portfolio preferences of business shift in such a way that large additions to their real capital stock is desired. Over 1964, 1965, and much of 1966 the American economy acted as if it were starved for capital. Investment in each of these years increased at a nonsustainable rate. An enterprise economy of this type might be characterized as "euphoric."

The essential flaw in American capitalism is this propensity for business investment to take off into a cumulative, nonsustainable explosion. The trigger to this explosion is a past of very good times which leads to a general reevaluation of business prospects.

The War on Poverty requires that tight full employment be achieved and sustained. But once it is certain that tight full employment will be sustained, then all enterprises would suddenly find they want much more capital than they have. Given the certainty of tight full employment, the gross profits of the firm are assured. Under these circumstances, managers will be very willing to finance the acquisition of new capital by emitting liabilities which, in a world where uncertainty loomed larger, they would never tolerate.

However, it is not only new investment that is affected by such emphasis. The investment decisions of the past leave a financial residue. These instruments carry yields that reflect the views about the relative riskiness of the different ventures and financial assets at the time they (the instruments) were emitted. These assets now have to be priced to reflect current views about expectations. The security that safe assets offered is now, in a world where uncertainty has been attenuated by the guarantee that prosperity will be sustained, of little value compared to the higher income offered by assets whose owners take their chances on the performance of the economy. The price of very safe assets falls; the price of risky assets rises.

The pressure on interest rates comes from two sources. One is the desire to invest larger and larger shares of total output. The second is the change in the desired asset structure by ultimates and intermediaries as a result of the new view about the future of the economy.

The end result of such an investment boom is a large-scale decrease in liquidity. Even in the absence of Federal Reserve constraint, but as long as the Federal Reserve does not turn into an engine of runaway inflation, the end result of the ever greater pinch in liquidity will be a financial tremor or crisis. The financial crisis forces a revaluation of desired assets and liabilities—including the desired stock of capital. The breaking of the investment boom can lead to a reciprocating set of feedbacks between income and financial sectors that ends in a deep depression, unless large-scale fiscal stimulants are undertaken.

Thus the sustained tight full employment that is required for the War on Poverty to succeed may be impossible to achieve with the financial system of American capitalism.

Notes on a Program Against Poverty

The conclusion of the preceding section is pretty dismal, fitting for an essay rooted in the dismal science. We are of necessity working with an economic system that is not perfect. We therefore should expect that any program aimed at some proximate policy goal, such as sustained tight full employment, will have side effects that adversely affect not only other dimensions of the system but also the ability to attain the proximate policy goal. Sustained tight full employment will set up a euphoric situation that may set in motion balance sheet adjustments that may tend to tear the very fabric of the financial system to shreds. If 1966 is evidence of anything, it is evidence that the economy has difficulty in assimilating a sustained expansion, let alone sustained full employment.

I will not venture into the morass of a program to reform the financial system so that it no longer is inconsistent with tight full employment. A planning constraint, such as investment licensing, and a constraint on using the financial market (capital issues licensing) might dampen the enthusiastic response. However, these direct controls on the runaway tendency to invest will fundamentally change the nature of the economy.

I also do not believe that the problem of 1966 was due to too much fiscal ease, so that monetary policy had to do too much of the job. This conventionally wise diagnosis of what happened in 1966 assumes that the sustained expansion of 1961–65 plus the guarantee by authorities that this progress could be sustained indefinitely had nothing to do with the pressure on financial markets.

The ingredients for a correct aggregate economic policy exist in the experience of the last three quarters (third and fourth quarters of 1966 and first quarter of 1967). A financial system tremor occurred which by itself would have resulted in a deep and fairly long depression in investment. The impact of the leveling off and decline in private investment was offset by a large increase in government spending. The net result has been stable unemployment levels and no decline in aggregate demand. True, the radical shift in the composition of demand has brought with it pressure on prices, but that is a small cost for the real output that was not lost.

What we need is a fiscal equivalent to an escalating war whenever runaway propensities to invest via financial repercussions lead to financial distress and instability. The financial difficulties are an essential part of the mechanism; the policy problem is to prevent the financial system problems from generating significant downward pressure on resource use.

If the government acts as a true employer of last resort, with reserve employment programs in being at all locations where unemployment can conceivably be a problem, then government expenditures will respond by increasing rapidly whenever unemployment becomes a reality. To date the automatic fiscal stabilizers act mainly on the tax receipts side; by employer-of-last-resort programs they will also act on the expenditure side.

It has been argued that the expansion to date (end of 1966) has not had the effect of rectifying the broadening of relative wages that has occurred since 1948 and that special measures may be needed. An obvious measure would be to gradually increase the ratio of the wage at which employer-of-last-resort jobs are available to the average wage—i.e., decrease the range between the statutory minimum and the average hourly wage, and guarantee jobs to all at the statutory minimum. It may be that policies which restrict wages above the average to a maximum increase of some 3 percent per year while the minimum wage rises by some 5 percent per year will be an important weapon in rectifying the wage structure. Continuing this program of differential rates of increase for a number of years will lead to a ratio of minimum to average of 80 percent rather than perpetuating the present more extended range.

If such pressure upon low wages results in unemployment in the private sector, the public employment sector needs to fill up the breach.

There are no shortages of useful and important jobs that such an employer of last resort can undertake; all that is needed to get a list of such jobs is to ask any mayor, or county supervisor, or school board head.

The employer of last resort should have a youth employment arm. By a combination of school years and vacation jobs, all youngsters in school 14 years old or over, male and female, should be guaranteed a minimum of $600 per year for 14-year-olds (rising to $900 per year for 18-year-olds). College student guaranteed employment should be geared to college room and board rates.

Under all circumstances youth income should be included as taxable income of the head of the household.

For youths who choose to drop out of formal schooling, the youth arm of the employer authority should provide both full-time employment and job training programs combined with part-time employment.

There are two aspects of the transfer payment programs that require marked revision. Many of the programs now in effect were introduced during the 1930's, a period of chronic mass unemployment. They were designed in good part to reduce the size of the labor force. There is nothing sacred about the existing retirement ages or the school-leaving ages. Of immediate issue is the adequacy of social security. Options should be available for a worker to delay retirement in exchange for larger benefits upon retirement. The ceilings on earnings while receiving full benefits should be revised to allow for regular part-time employment or seasonal full-time employment. Participation in the labor force of the healthy and alert aged should be at their option—aggregate demand policy should be relied upon to generate the requisite number of jobs.

Much is being said about a negative income tax as a means of supplementing the earned income of those who earn too little and as a substitute for welfare payments for those not in the labor market. If the negative income tax is really to aid those with low incomes, the marginal tax rates on income earners will of necessity be high. Thus it will have a large disincentive component.

A simple alternative to a negative income tax is a children's allowance. Recent computations indicate that many families are in poverty because of family size and the cost of maintaining their larger families. These computations indicate that the "cost" of an additional child is from $600 to $750 per year. A family allowance of $25 per month per child under 14 would cost about $16 billion per year gross. If the receipts from the family allowance are considered a part of taxable income, then the net cost would be somewhat lower—say $14 billion. Thus the cost of a family allowance would be some 2 years' fiscal drag at present income and tax rates.

The virtue of a family allowance is that the Federal checks will go to all—rich and poor, Negro and white, alike. There will not be any preponderance of receivers over payers for any particular social, ethnic, or other class. As it will be a part of the tax base, the subsidy to the poor will be greater than to the well to do.

The defect of the children's allowance is that it will still leave some room for "case work" welfare. However, by belonging to each child by right it also will not have any disincentive effects with regard to labor market participation by parents.

The ability to eliminate poverty depends not only upon the growth of potential GNP but also upon a higher ratio of actual to potential GNP than we have achieved to date. The maximization of aggregate demand, and thus of income from jobs, is the quickest way to constrain poverty.

The elimination of poverty is more than a minimum income goal. More deeply it is an attempt to foster the integration of the present poor and their descendants into society. This means that income from what is considered useful work is the main way to achieve the antipoverty goals. But this, in turn, requires that we invent new types of jobs—and it is the function of the employer of last resort to define new jobs which are available not only to the present poor who are now in the labor force but also to many of the present poor who, because of the peculiar nature of our income maintenance policies, are not now in the labor force.

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