MACROECONOMIC STABILITY AND ECONOMIC JUSTICE

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INTRODUCTION

This paper is motivated by the call to action in Economic Justice for All, Pastoral Letter on Catholic Social Teaching and the U.S. Economy, hereafter Pastoral Letter. This document charges lay men and women "through their competency and by their activity,...to bring the light of the Gospel to economic affairs" (p. 163). It enjoins "a communal task calling for dialogue, experimentation and imagination" (p. 63). Finally, it calls for compassion "especially for those whose vocation will call them to an active role in U.S. economic and political decision making" (p. 172).

Much of my research, teaching, and public service has been in the political economy of monetary and fiscal policy. Many economists in this area have become decidedly pessimistic regarding prospects for reducing macroeconomic instability. There is good reason for such resignation. As explained in part II, given the disincentives for change that are built into our political institutions, neither monetary reform, fiscal reform, nor new policy techniques have a realistic chance of sidetracking our economy from the inflation-unemployment roller coaster. It will be shown that in the final analysis macroeconomic instability is a product of politicized distributive conflict.

As realists, technicians, and positivists, most economists allow little room in their research and teaching for normative discussion of social values. The Pastoral Letter argues that they should. It suggests that economic problems (I will include macroeconomic instability in the list) can be reduced if teachers and researchers and their students stop hiding behind technique worship and the normative-vs.-positive-economics veil and begin to make political and social judgments that transcend the narrow efficiency criterion. Following the Pastoral Letter's lead this paper will go to the root of distributive conflict and make some suggestions to reduce it.

IS MACROECONOMIC INSTABILITY HERE TO STAY?

Political decisions have macroeconomic antecedents as well as macroeconomic consequences. Chronic government budget deficits and their monetization are politically motivated. Spending and tax reduction programs are intended to benefit politically important groups and sectors at the same time that financing these programs by raising other taxes or issuing interest-bearing debt would offend other politically
important groups. Thus, deficit monetization and the resulting inflation are symptomatic of the politician's retreat from distributive conflict. Inflation is simply the politician's way of buying time to avoid the wrath of groups and sectors who will ultimately bear the burden of tax increases or, for a debt-financed deficit, interest rate increases or exchange rate decreases.

It is, however, unfair to blame inflation on politicians. The monetization of budget deficits and inflation are simply the consequences of rational politician behavior. Politicians gain power simply by promising to deliver what their constituents desire. Politicians realize that they can most rapidly advance their ambitions by promising a larger share of the economic pie to key groups, for example those who have recently gained political power because of demographic or legislated changes in the distribution of voting rights. Unfortunately, a larger share for one group or sector means a smaller share for another. Politicians realize that their fortunes would suffer if they could and would pinpoint those groups and sectors which would ultimately receive a smaller slice of the economic pie because of resulting program cutbacks, tax increases or changes in interest rates or exchange rates. When specific groups finally feel these impacts, political leaders pressure the Federal Reserve to provide temporary relief in the form of more rapid growth in the nation's money supply, the ultimate effect of which is inflation. 2

Politicians regularly reject any fundamental reform of the present fiscal and monetary system that would remove spending, taxing and monetary policy weapons from their vote-getting arsenal. Fiscal reforms which would link new spending or tax cut programs to offsetting tax increases or program cutbacks are unpalatable to politicians because they would result in overt distributional conflict. Monetary reforms which would uncouple money supply growth from the size of the deficit, for example by returning to the gold standard or by depoliticizing monetary policy, are equally unacceptable because, by denying politicians the monetary camouflage, they, too, would bring distributional conflict out into the open. Open distributional confrontation in legislatures or in the streets would prove quite costly, especially to politicians. In short, inflation seems the most expedient way to mollify temporarily the parties to latent distributional dispute. In other words, given the inflationary alternative, there is an unacceptably high political cost of reforming our fiscal and monetary institutions. 3 In the absence of reform, macroeconomic instability promises will remain a persistent fact of economic life.

It can be further contended that distributional conflict and resulting macroeconomic instability is exacerbated to the extent that income expectations cannot be met. This could occur for two reasons. First, if the distribution of skills