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The New American Way: Work Harder for Less Pay

Federal Reserve Says Your Wages are Too High

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The Federal Reserve has declared that the reason for ongoing economic weakness is because wages have not fallen enough. Wages have been stagnant for four decades while productivity has soared, but nonetheless orthodox economists believe the collapse of 2008 has been a missed opportunity.

A paper prepared by two senior researchers with the San Francisco branch of the U.S. Federal Reserve Bank attempts to explain the lack of wage growth experienced as unemployment has fallen over the past couple of years this way:

"One explanation for this pattern is the hesitancy of employers to reduce wages and the reluctance of workers to accept wage cuts, even during recessions, a behavior known as downward nominal wage rigidity."

The two Federal Reserve researchers, Mary Daly and Bart Hobijn, based their argument on the standard ideology of orthodox economists, writing:

"Downward rigidities prevent businesses from reducing wages as much as they would like following a negative shock to the economy. This keeps wages from falling, but it also further reduces the demand for workers, contributing to the rise in unemployment. Accordingly, the higher wages come with more unemployment than would occur if wages were flexible and could be fully reduced."

The "problem" of wages stubbornly refusing to drop as much as corporate executives and financiers would like is referred to as the "sticky wages" problem in orthodox economics. Simply put, this "problem" is one that orthodox economists, themselves not necessarily subject to the market forces they wish to impose on others, have long struggled to "solve." You perhaps will not be surprised to hear that "government" is the problem. Consider this remarkable passage published on the web site of the Mises Institute, an advocate of the Austrian school of economics:

"Much of the alleged 'stickiness' of wages is due to government policies. … [T]he trouble stems from workers not being willing to take pay cuts. When the demand from employers drops, at the old wage rate there is now surplus labor — a.k.a. unemployment. Only when market wages drop to a lower level, so that demand once again matches supply, will equilibrium be restored in the labor market."

Collapsing wages in the Great Depression didn't help

According to this author, Robert P. Murphy, an "associated scholar" of the Mises Institute, failing to drive down wages is such a big mistake that it caused the Great Depression. He writes:

"After the 1929 crash, Herbert Hoover gathered the nation's leading businessmen for a conference in Washington and urged them to allow profits and dividends to take the hit, but to spare workers' paychecks. Rather than cut wages, businesses were supposed to implement spread-the-work schemes where workers would cut back their hours. The rationale for Hoover's high-wage policy was that the worker supposedly needed to be paid 'enough to buy back the product.' … The idea was that wage cuts would just cause workers to cut their spending, which would in turn lead to another round of wage cuts in a vicious downward spiral."

Herbert Hoover was not vicious enough! Although it was Hoover's Treasury secretary, Andrew Mellon, who advocated the government "liquidate labor, liquidate stocks, liquidate farmers, liquidate real estate" so as to "purge the rottenness out of the system," and not Hoover himself, the president did take hard-line right-wing positions. Michael Parenti, in discussing Hoover in his book *History as Mystery*, wrote:

"Like so many conservatives then and now, Hoover preached the virtues of self-reliance, opposed the taxation of overseas corporate earnings, sought to reduce income taxes for the highest brackets, and was against a veterans' bonus and aid to drought sufferers. He repeatedly warned that public assistance programs were the beginning of 'state socialism.' Toward business, however, he suffered from no such 'inflexibility' and could spend generously. He supported multimillion-dollar federal subsidies to shipping interests and agribusiness, and his

Reconstruction Finance Corporation doled out about $2 billion to banks and corporations." [page 261]

Hoover's concern for working people was demonstrated when his troops fired on veterans demanding payments owed to them and burned their camps. His laissez-faire policies led to manufacturing wages falling 34 percent and unemployment rising to about 25 percent by 1933. That collapse in wages did not bring better times; only the massive government spending to wage World War II put an end to the Depression. Such wage declines, in the real world, actually make the economy worse, argues Keynesian economist Paul Krugman:

"[Y]ou could argue that a sufficiently large fall in wages could restore full employment now — but it would have to be a very large wage decline, and the positive effects would kick in only after deflation had first driven just about every debtor in the economy into bankruptcy."

How many formulae can be written on the head of a pin?

Although orthodox economics is often nothing more than ideology in the service of capitalist elites, its practitioners like to believe themselves scientific because they base their theories on mathematical models. Unfortunately, these formulae are divorced from the real, physical world; the economy and the human behavior that animates it are not reducible to mathematics.

Robert Kuttner, a heterodox economist, explored these shortcomings in an article originally published in *Atlantic Monthly*. He wrote:

"The [prevailing] method of practicing economic science creates a professional ethic of studied myopia. Apprentice economists are relieved of the need to learn much about the complexities of human motivation, the messy universe of economic institutions, or the real dynamics of technological change. Those who have real empirical curiosity and insight about the workings of banks, corporations, production technologies, trade unions, economic history or individual behavior are dismissed as casual empiricists, literary historians or sociologists, and marginalized within the profession. In their place departments are graduating a generation of idiots savants, brilliant at esoteric mathematics yet innocent of actual economic life."

That was written in 1985; little if anything has changed since and arguably has gotten worse. Professor Kuttner points out that the very fact of persistent unemployment contradicts the basic theses of orthodox neoclassical economics. If the belief that markets automatically reach equilibrium were true, then wages would automatically fall until everybody had a job. Rather than acknowledge the real world, orthodox economists simply declare involuntary unemployment an "illusion," or claim "government interference" with the market is the culprit. "Business cycles were around long before trade unions or big-spending governments were," Professor Kuttner noted.

Wages are not as flexible as orthodox ideology suggests because within an enterprise preference is ordinarily given to existing workers to fill job openings, thereby buffering wages from external market forces, writes another heterodox economist, Herbert Gintis. In an essay originally appearing in *Review of Radical Political Economics*, he wrote:

"In particular, there is a tendency for the number of individuals qualified for a position to exceed the number of jobs available, in which case seniority and other administrative rules are used to determine promotion. Hardly do workers compete for the job by bidding down its wage."

In almost all cases, employees do not even know what wages their co-workers are earning. This top-down secrecy facilitates the disparity in wages, whereby, for example, women earn less than men. If everybody earned what they were worth, there would no such wage disparity. The very fact of disparities between the genders or among races and ethnicities demonstrates the ideological basis of orthodox economics, which assumes that employees who do the work of production are in their jobs due to personal choice and wages are based only on individual achievement independent of race, gender and other differences.

You produce more but don't earn more

Back in the real world, wages have significantly lagged productivity for four decades; thus, wages, examined against this benchmark, have significantly declined for those four decades. A study by the Economic Policy Institute, written by heterodox economist Elise Gould, reports:

"Between 1979 and 2013, productivity [in the U.S.] grew 64.9 percent, while hourly compensation of production and nonsupervisory workers, who comprise over 80 percent of the private-sector workforce, grew just 8.0 percent. Productivity thus grew eight times faster than typical worker compensation." [page 4]

Middle-class U.S. households earn $18,000 less than they would had wages kept pace with productivity, Dr. Gould calculates. Nor is that unique to the U.S.: Wages in Canada, Europe and Japan have also fallen well short of productivity gains. Canadian workers, for example, are paid at least $15,000 per year less than they would be had their wages kept pace.

To circle back to the San Francisco Federal Reserve paper that began this discussion, the authors claim that wage stagnation will persist until markets "return to normal." They assert:

"[T]he accumulated stockpile of pent-up wage cuts remains and must be worked off to put the labor market back in balance. In response, businesses hold back wage increases and wait for inflation and productivity growth to bring wages closer to their desired level."

But as we can plainly see, and as those of us living in the real world experience, wages cuts have been the norm for a long time. The caveat at the end of the paper that it does not necessarily reflect the views of the Fed board of governors should be noted, but the paper was issued as part of a regular series by the San Francisco Fed and the authors are senior members of it, so it is not likely to be at variance with opinions there. It certainly does reflect orthodox economic ideology. Similarly, the argument by the Austrian School's Mises Institute, stripped of its academic-sounding veneer, is a call to eliminate the minimum wage.

Stagnation, declining wages and the ability of capitalists to shift production around the globe in a search for the lowest wages and lowest safety standards — completely ignored in the orthodox hunt for economic scapegoats — *are* the norm. Our need to sell our labor, the resulting reduction

of human beings' labor power to a commodity, and the endless competitive pressures on capitalists to boost profits underlie the present economic difficulties.

Collective bargaining through unions and the needs of capitalists to retain their employees can be brakes against the race to the bottom — what the orthodox economists at the Fed and elsewhere are arguing is that these remaining brakes be removed and wages driven down to starvation levels. That is what global capitalism has to offer.