What is a Job Guarantee?

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Bill Mitchell, May 5, 2013

This is a background blog which will support the release of my Fantasy Budget 2013-14, which will be part of Crikey's Budget coverage leading up to the delivery of the Federal Budget on May 14, 2013. The topic of this blog is the concept of employment guarantees as the base-level public policy supporting a return to full employment in Australia. We introduce the specific proposal – the Job Guarantee. In the next background blog we will see how much the Australian government needs to invest to make this policy improvement possible.

The complete suite of Fantasy Budget blogs are as follows:

- The indecent inconsistency of the neo-liberals
- Australia output gap – not close to full capacity
- Daily macroeconomic income losses from unemployment
- The Australian labour market – 815 thousand jobs from full employment
- What is a Job Guarantee?
- Investing in a Job Guarantee – how much?
- MMT Budgetary Principles
- The Fantasy Budget 2013-14

Introduction

The recent background blogs (see links above), I provided some perspectives on how much capacity for **real** expansion currently exists in Australia. While these exercises involve considerable judgement, there is little doubt that there is significant idle capacity in the Australian economy.

The following (interrelated) conclusions emerged:

- Relative to the recent best unemployment rate period (February 2008) the Australian economy sacrifices $A77.4 million in lost national output and income every day as a result of the Government's failure to attack the unemployment problem.
- Relative to what would be a fairer representation of the true full employment unemployment rate (2 per cent) the Australian economy is foregoing $150.5 million in lost national output and income every day.
- Trend growth in Australia is between 3.1 per cent and 3.4 per cent. The annualised quarterly real GDP growth rate in Australia (from the December-quarter 2012) is 2.4 per cent and falling. The annual growth rate for 2013 will be below that given a further deterioration in the economy.
- Relative to trend growth, the incremental annual output gap (expressed as a percentage of trend real GDP) for 2012 was around 3.9 per cent or $A60 billion. The gap for the December-quarter had risen to 4.3 per cent reflecting the slowdown in the economy over 2012.
- The total estimated labour wastage in Australia – taking into account unemployment, hidden unemployment and underemployment – is currently at 13.9 per cent of the available labour force.
- To get back to where the economy was at the start of the crisis in February 2008 would require some 398 thousand jobs to be created. This would ensure the unemployment rate was 4 per cent, the underemployment rate 5.9 per cent and the participation rate at its February 2008 level.
- But at February 2008, the broad ABS labour underutilisation rate was close to 10 per cent, which means the economy wasn't at full employment then.
- If we define a reasonable full employment policy goal of 2 per cent unemployment, zero hidden

unemployment and zero underemployment, then the Australian labour market needs to create a further 815 odd thousand jobs.

The question that arises is this: Can we create enough jobs within the estimated output gap so as not to push nominal expansion beyond the real capacity of the economy to absorb it?

In advocating further fiscal stimulus, it would be useful to directly target job creation. There are three broad ways in which this could be done: (a) expand the career public service; (b) subsidise private employers; and (c) create a new public sector buffer employment capacity.

While options (a) and (b) have advantages and disadvantages, the first step in restoring full employment should be option (c).

As the **first** step to restoring full employment, the national government should introduce an open-ended public employment program – a **Job Guarantee** – that offers a job at a living (minimum) wage to anyone who wants to work but cannot find employment.

While introducing a public sector job creation capacity to the economy, the Job Guarantee is actually a macroeconomic policy framework designed to ensure full employment and price stability is maintained over the private sector business cycle.

The Job Guarantee jobs would 'hire off the bottom', in the sense that minimum wages are not in competition with the market-sector wage structure.

By not competing with the private market, the Job Guarantee would avoid the inflationary tendencies of old-fashioned Keynesianism, which attempted to maintain full capacity utilisation by 'hiring off the top' (i.e. making purchases at market prices and competing for resources with all other demand elements).

Job Guarantee workers would enjoy stable incomes, and their increased spending would boost confidence throughout the economy and underpin a private-spending recovery.

The Australian government could afford this program because it has has no financial constraint as the issuer of the currency.

The only question is whether there is enough real capacity in the economy (available resources and output space) for the extra government spending.

From our previous estimates of the output gap there would appear to be more than enough spare capacity in the economy to accommodate this policy shift.

The labour is available for work, and the government can easily supply the jobs. Few questions were asked when the government, in the early days of the crisis, instantly provided billions for the banks.

What is the Job Guarantee?

Between 1945 and the mid-1970s, western governments realised that, with deficit spending supplementing private demand, they could ensure that all workers who wanted to work could find jobs. Although private employment growth was relatively strong during this period, governments were important employers in their own right, and also maintained a buffer of jobs for the least skilled workers; for example, in the major utilities, the railways, local public services and major infrastructure functions of government. By absorbing workers who lost jobs when private investment declined, governments acted as an economic safety valve.

British economist Paul Ormerod (quote from the *Death of Economics*) noted that the economies that avoided high unemployment in the 1970s maintained a:

> *… sector of the economy which effectively functions as an employer of last resort, which absorbs*

> *the shocks which occur from time to time, and more generally makes employment available to the less skilled, the less qualified.*

He concluded that societies with a high degree of social cohesion (such as Austria, Japan and Norway) were willing to broaden their concept of costs and benefits of resource usage to ensure that everyone had access to paid employment opportunities.

It is in that context that the Job Guarantee (JG) can be understood. The program has the following summary features.

<u>Full Employment:</u>

The Government operates a buffer stock of jobs to absorb workers who are unable to find employment in the private sector. The pool expands (declines) when private sector activity declines (expands). The JG fulfills this absorption function to minimise the costs associated with the flux of the economy. So the government continuously absorbs into employment, workers displaced from the private sector.

The "buffer stock" employees would be paid the minimum wage, which defines a wage floor for the economy. Government employment and spending automatically increases (decreases) as jobs are lost (gained) in the private sector.

The JG works on the "buffer stock" principle. Recall the Wool Floor Price Scheme introduced by the Commonwealth Government of Australia in November 1970. The scheme was relatively simple and worked by the Government establishing a floor price for wool after hearing submissions from the Wool Council of Australia and the Australian Wool Corporation (AWC).

The Government then guaranteed that the price would not fall below that level by using the AWC to purchase stocks of wool in the auction markets if demand was low and selling it if demand was high. So by being prepared to hold "buffer wool stocks" in low demand and release it again in times of high demand the government was able to guarantee incomes for the farmers.

However, with some lateral thinking you can easily see that what the Wool Floor Price Scheme generated was "full employment" for wool! If the Government fixed the price that it was prepared to pay and then was willing to buy all the wool up to that price then you have an equivalent scheme.

This works just the same for labour resources – just unconditionally offer to buy all labour at a stated fixed wage and you create full employment. What should that wage be?

<u>JG Wage:</u>

To avoid disturbing private sector wage structure and to ensure the JG is consistent with stable inflation, the JG wage rate is best set at the minimum wage level. The JG wage may be set higher to facilitate an industry policy function.

The minimum wage should not be determined by the capacity to pay of the private sector. It should be an expression of the aspiration of the society of the lowest acceptable standard of living. Any private operators who cannot "afford" to pay the minimum should exit the economy.

Australia has a well-defined minimum wage setting structure.

<u>Social Wage:</u>

The Government would supplement the JG earnings with a wide range of social wage expenditures, including adequate levels of public education, health, child care, and access to legal aid. Further, the JG policy does not replace conventional use of fiscal policy to achieve social and economic outcomes.

In general, the JG would be accompanied by higher levels of public sector spending on public goods and infrastructure.

Note: that these supplements would be in addition to the scheme but not essential for the scheme to function effectively.

Family Income Supplements:

The JG is not based on family-units. Anyone above the legal working age is entitled to receive the benefits of the scheme. We would supplement the JG wage with benefits reflecting family structure. In contrast to workfare there will not be pressure applied to single parents to seek employment.

Again, note, that these supplements would be in addition to the scheme but not essential for the scheme to function effectively.

Funding:

The JG would be funded by the sovereign government which faces no financial constraints in its own currency. In the context of the current outlays that are being thrown around in national economies, the investment that would be required to introduce a full blown would be rather trivial.

I will provide detailed estimates of the required outlays in the next background blog.

Inflation control:

There is now an extensive literature within what is now known as the Modern Monetary Theory (MMT) tradition on how employment buffer stocks serve to control inflation while not sacrificing the full employment goal.

In brief, when the level of private sector activity is such that wage-price pressures forms as the precursor to an inflationary episode, the government manipulates fiscal and monetary policy settings (preferably fiscal policy) to reduce the level of private sector demand.

This would see labour being transferred from the inflating sector to the "fixed wage" sector and eventually this would resolve the inflation pressures. Clearly, when unemployment is high this situation will not arise.

But in general, there cannot be inflationary pressures arising from a policy that sees the Government offering a fixed wage to any labour that is unwanted by other employers. The JG involves the Government "buying labour off the bottom" rather than competing in the market for labour. By definition, the unemployed have no market price because there is no market demand for their services. So the JG just offers a wage to anyone who wants it.

NAIBER:

In contradistinction with the NAIRU approach to price control which uses unemployed buffer stocks to discipline wage demands by workers and hence maintain inflation stability, the JG approach uses the ratio of JG employment to total employment which is called the Buffer Employment Ratio (BER) to maintain price stability.

The ratio that results in stable inflation via the redistribution of workers from the inflating private sector to the fixed price JG sector is called the Non-Accelerating-Inflation-Buffer Employment Ratio (NAIBER). It is a full employment steady state JG level, which is dependent on a range of factors including the path of the economy. Its microeconomic foundations bear no resemblance to those underpinning the neoclassical NAIRU.

It also wouldn't be worth estimating or targetting. It would be whatever was required to fully employ labour and maintain price stability.

Workfare or Work-for-the-Dole:

Many people think that the JG is just Work-for-the-Dole in another guise. The JG is, categorically, not a more elaborate form of Workfare.

Workfare does not provide secure employment with conditions consistent with norms established in the community with respect to non-wage benefits and the like.

Workfare does not ensure stable living incomes are provided to the workers. Workfare is a program, where the State extracts a contribution from the unemployed for their welfare payments. The State, however, takes no responsibility for the failure of the economy to generate enough jobs.

In the JG, the state assumes this responsibility and pays workers award conditions for their work.

Under the JG workers could remain employed for as long as they wanted the work. There would be no compulsion on them to seek private work. They could also choose full-time hours or any fraction thereof.

Training

The JG would be integrated into a coherent training framework to allow workers (by their own volition) to choose a variety of training paths while still working in the JG.

However, if they chose not to undertake further training no pressure would be placed upon them.

Unemployment benefits:

The existing unemployment benefits scheme could be maintained alongside the JG program, depending on the government's preference and conception of mutual responsibility.

My personal preference is to abandon the unemployment benefits scheme and free the associated administrative infrastructure for JG operations.

The concept of mutual obligation from the workers' side would become straightforward because the receipt of income by the unemployed worker would be conditional on taking a JG job.

The JG wage could be paid to anyone who turned up at some designated Government JG office even if the office had not yet organised work for that person.

I would also allow a person a short-period – perhaps two weeks – in between losing their job and starting a JG job – to sort out their affairs. This period would be covered by full JG pay.

Administration:

For financial reasons explained below, the JG would be financed federally with the operational focus being local. Local Government would be an important administrative sphere for the actual operation of the scheme.

I would abandon the Jobs Services Australia Network and restore the Commonwealth Employment Service (CES), which would play and important role in coordinating the JG demand and supply with local level managers.

Local administration and coordination would ensure meaningful, value-adding work was a feature of the JG activities.

Type of Jobs:

Between 2005-2008, the Centre of Full Employment and Equity (known as CofFEE) – conducted a three-year study involving extensive interviews with Local Government engineers and managers in Australia.

Their final Report – Creating effective local labour markets: a new framework for regional employment policy – develops a new framework for the design of regional employment policy. It emphasises increased public sector infrastructure spending, the implementation of a National Skills Development framework and the introduction of a national Job Guarantee. The proposed new integrated policy framework would provide more effective ways to assist disadvantaged individuals into employment and advance sustainable solutions to persistent unemployment across regional Australia.

It also provides an exhaustive analysis of the community- and environmentally-based projects that could be completed at the regional level if Federal funds were forthcoming.

The JG workers would contribute in many socially useful activities including urban renewal projects and other environmental and construction schemes (reforestation, sand dune stabilisation, river valley erosion control, and the like), personal assistance to pensioners, and other community schemes. For example, creative artists could contribute to public education as peripatetic performers. The Report goes into much greater detail.

The buffer stock of labour would however be a fluctuating work force (as private sector activity ebbed and flowed). The design of the jobs and functions would have to reflect this. Projects or functions requiring critical mass might face difficulties as the private sector expanded, and it would not be sensible to use only JG employees in functions considered essential.

Thus in the creation of JG employment, it can be expected that the stock of standard public sector jobs, which is identified with conventional Keynesian fiscal policy, would expand, reflecting the political decision that these were essential activities.

Open Economy Impacts:

The JG requires a flexible exchange rate to be effective. A once-off increase in import spending is likely to occur as JG workers have higher disposable incomes. The impact would be modest. We would expect any modest depreciation in the exchange rate to improve the contribution of net exports to local employment, given estimates of import and export elasticities found in the literature.

Environmental benefits:

The JG proposal will assist in changing the composition of final output towards environmentally sustainable activities. These are unlikely to be produced by traditional private sector firms because they have heavy public good components. They are ideal targets for public sector initiative.

Future labour market policy must consider the environmental risk-factors associated with economic growth. Possible threshold effects and imprecise data covering the life-cycle characteristics of natural capital suggest a risk-averse attitude is wise.

Indiscriminate (Keynesian) expansion fails in this regard because it does not address the requirements for risk aversion. It is not increased demand *per se* that is necessary but increased demand in certain areas of activity.

The JG is **green**.

Conclusion

It is obvious that this summary will not answer all your questions. More reading is provided below.

When compared to a policy that maintains persistently high levels of unemployment, which incur millions of dollars in lost output and income per day, the JG has to be a better alternative.

The private sector has never employed all the available labour force.

It is the time the Government acknowledged that and stopped lying about the state of the labour market.

Further References

For detailed analysis and answers to all the questions you might have please consult the following work.

- Creating effective local labour markets: a new framework for regional employment policy – this report was the result of a three-year study and extensive interviews with Local Government engineers and managers.

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- Mitchell, W.F. (1998) ‘The Buffer Stock Employment Model and the NAIRU: The Path to Full Employment’, *Journal of Economic Issues*, 32(2), June, 1-9.
- Several blog articles available from this – Job Guarantee – archive