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Tami J. Friedman, John Miller, and
the *Dollars and Sense* Collective

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July/August 1999

THE GROWTH CONSENSUS UNRAVELS

BY JONATHAN ROWE

Economics has been called the dismal science, but beneath its gray exterior is a system of belief worthy of Pollyanna.

Yes, economists manage to see a dark cloud in every silver lining. Downturn follows uptick, and inflation rears its ugly head. But there's a story within that story — a gauzy romance, a lyric ode to Stuff. It's built into the language. A thing produced is called a "good," for example, no questions asked. The word is more than just a term of art. It suggests the automatic benediction which economics bestows upon commodities of any kind.

By the same token, an activity for sale is called a "service." In conventional economics there are no "dis-services," no actions that might be better left undone. The bank that gouges you with ATM fees, the lawyer who runs up the bill — such things are "services" so long as someone pays. If a friend or neighbor fixes your plumbing for free, it's not a "service" and so it doesn't count.

The sum total of these products and activities is called the Gross Domestic Product, or GDP. If the GDP is greater this year than last, then the result is called "growth." There is no bad GDP and no bad growth; economics does not even have a word for such a thing. It does have a word for less growth. In such a case, economists say growth is "sluggish" and the economy is in "recession." No matter what is growing — more payments to doctors because of worsening health, more toxic cleanup — so long as there is more of it, then the economic mind declares it good.

This purports to be "objective science." In reality it is a rhetorical construct with the value judgments built in, and this rhetoric has been the basis of economic debate in the United States for the last half century at least. True, people have disagreed over how best to promote a rising GDP. Liberals generally wanted to use government more, conservatives less. But regarding the beneficence of a rising GDP, there has been little debate at all.

If anything, the Left traditionally has believed in growth with even greater fervor than the Right. It was John Maynard Keynes, after all, who devised the growth-boosting mechanisms of macroeconomic policy to combat the Depression of the 1930s; it was Keynesians who embraced these strategies after the War and turned the GDP into a totem. There's no point in seeking a bigger pie to redistribute to the poor, if you don't believe the expanding pie is desirable in the first place.

Today, however, the growth consensus is starting to unravel across the political spectrum and in ways that are both obvious and subtle. The issue is no longer just the impact of growth upon the environment — the toxic impacts of industry and the like. It now goes deeper, to what growth actually consists of and what it means in people's lives. The things economists call "goods" and "services" increasingly don't strike people as such. There is a growing disconnect between the way people experience growth and the way the policy establishment talks about it, and this gap is becoming an unspoken subtext to much of American political life.

The group most commonly associated with an anti-growth stance is environmentalists, of course. To be sure, one faction, the environmental economists, is trying to put green new wine into the old bottles of economic thought. If we would just make people pay the "true" cost of, say, the gasoline they burn, through the tax system for example, then the market would do the rest. We'd have benign, less-polluting growth, they say, perhaps even more than now. But the core of the environmental movement remains deeply suspicious of the growth ethos, and probably would be even if the environmental impacts somehow could be lessened.

In the middle are suburbanites who applaud growth in the abstract, but oppose the particular manifestations they see around them — the traffic, sprawl, and crowded schools. On the Right, meanwhile, an anti-growth politics is arising practically unnoticed. When social conservatives denounce gambling, pornography, or sex and violence in the media, they are talking about specific instances of the growth that their political leaders rhapsodize about on other days.

THERE IS A GROWING DISCONNECT BETWEEN THE WAY PEOPLE EXPERIENCE GROWTH AND THE WAY THE POLICY ESTABLISHMENT TALKS ABOUT IT.

Environmentalists have been like social conservatives in one key respect. They have been moralistic regarding growth, often scolding people for enjoying themselves at the expense of future generations and the earth. Their concern is valid, up to a point — the consumer culture does promote the time horizon of a five-year-old. But politically it is not the most promising line of attack, and conceptually it concedes too much ground. To moralize about consumption as they do is to accept the conventional premise that it really is something chosen — an enjoyable form of self-indulgence that has unfortunate consequences for the earth.

That's "consumption" in the common parlance — the sport utility vehicle loading up at Wal-Mart, the stuff piling up in the basement and garage. But increasingly that's not what people actually experience, nor is it what the term really means. In economics, consumption means everything people spend money on, pleasurable or not. Wal-Mart is just one dimension of a much larger and increasingly unpleasant whole. The lawyers' fees for the house settlement or divorce; the repair work on the car after it was rear-ended; the cancer treatments for the uncle who was a three-pack-a-day smoker; the stress medications and weight loss regimens — all these and more are "consumption." They all go into the GDP.

Cancer treatments and lawyer's fees are not what come to mind when environmentalists lament the nation's excess consumption, or for that matter when economists applaud America's "consumers" for keeping the world economy afloat. Yet increasingly such things are what consumption actually consists of in the economy today. More and more, it consists not of pleasurable things that people choose, but rather of things that most people would gladly do without.

Much consumption today is addictive, for example. Millions of Americans are engaged in a grim daily struggle with themselves to do less of it. They want to eat less, drink less, smoke less, gamble less, talk less on the telephone — do less buying, period. Yet economic reasoning declares as growth and progress, that which people themselves regard as a tyrannical affliction.

Economists resist this reality of a divided self, because it would complicate their models beyond repair. They cling instead to an 18th-century model of human psychology — the "rational" and self-interested man — which assumes those complexities away. As David McClelland, the Harvard psychologist, once put it, economists "haven't even discovered Freud, let alone Abraham Maslow." (They also haven't discovered the Apostle Paul, who lamented that "the good that I would I do not, but the evil that I would not that I do.")

Then too there's the mounting expenditure that sellers foist upon people through machination and deceit. People don't choose to pay for the corrupt campaign finance system or for bloated executive pay packages. The cost of these is hidden in the prices that we pay at the store. As I write this, the *Washington Post* is reporting that Microsoft has hired Ralph Reed, former head of the Christian Coalition, and Grover Norquist, a right-wing polemicist, as lobbyists in Washington. When I bought this computer with Windows 95, Bill Gates never asked me whether I wanted to help support a bunch of Beltway operators like these.

This is compulsory consumption, not choice, and the economy is rife with it today. People don't choose to pay some $40 billion a year in telemarketing fraud. They don't choose to pay 32% more for prescription drugs than do people in Canada. ("Free trade" means that corporations are free to buy their labor and materials in other countries, but ordinary Americans aren't equally free to do their shopping there.) For that matter, people don't choose to spend $25 and up for inkjet printer cartridges. The manufacturers design the printers to make money on the cartridges because, as the *Wall Street Journal* put it, that's "where the big profit margins are."

Yet another category of consumption that most people would gladly do without arises from the need to deal with the offshoots and implications of growth. Bottled water has become a multibillion dollar business in the United States because people don't trust what comes from the tap. There's a growing market for sound insulation and double-pane windows because the economy produces so much noise. A wide array of physical and social stresses arise from the activities that get lumped into the euphemistic term "growth."

The economy in such cases doesn't solve problems so

MEASURING PROGRESS

Far from being a true measure of economic (and human) progress, the GDP thrives on bad news. The GDP soars when the government spends millions to clean up a toxic waste site or to treat those suffering from cancer who lived nearby. And the GDP can drop from some very good news. For instance, it is good news for a family if a parent can afford to cut back on work and devote more hours at home. But because she is working less, spending less money on day care, and earning less, the GDP measures it as a drop in economic activity.

In the mid-1990s, the San Francisco group Redefining Progress created an alternative GDP that measures the costs as well as the benefits of economic growth. The "Genuine Progress Indicator," or GPI, accounts for how production and consumption create social ills like inequality, and creates environmental problems that threaten future generations, such as global warming and the depletion of natural resources. It adjusts the GDP downward to account for each of these aspects of economic activity, along with underemployment and the loss of leisure time. It would adjust the GDP upward if there had been more leisure time and social progress.

The result: while the GPI rose somewhat between 1950 and the early 1970s, it has been falling ever since. By 1994 the GPI was 26% lower than in 1973. During the same period, the GDP was growing.

much as create new problems that require more expenditure to solve. Food is supposed to sustain people, for example. But today the dis-economies of eating sustain the GDP instead. The food industry spends some $21 billion a year on advertising to entice people to eat food they don't need. Not coincidentally, there's now a $32 billion diet and weight loss industry to help people take off the pounds that inevitably result. When that doesn't work, which is often, there is always the vacuum pump or knife. There were some 110,000 liposuctions in the United States last year; at five pounds each that's some 275 tons of flab up the tube.

It is a grueling cycle of indulgence and repentance, binge and purge. Yet each stage of this miserable experience, viewed through the pollyanic lens of economics, becomes growth and therefore good. The problem here goes far beyond the old critique of how the consumer culture cultivates feelings of inadequacy, lack, and need so people will buy and buy again. Now this culture actually makes life worse, in order to sell solutions that purport to make it better.

Traffic shows this syndrome in a finely developed form. First we build sprawling suburbs so people need a car to go almost anywhere. The resulting long commutes are daily torture but help build up the GDP. Americans spend some $5 billion a year in gasoline alone while they sit in traffic and go nowhere. As the price of gas increases, this growth sector will expand.

Commerce deplores a vacuum, and the exasperating hours in the car have spawned a booming subeconomy of relaxation tapes, cell phones, even special bibs. Billboards have 1-800 numbers so commuters can shop while they stew. Talk radio thrives on traffic-bound commuters, which accounts for some of the contentious, get-out-of-my-face tone. The traffic also helps sustain a $130 billion-a-year car wreck industry; and if Gates succeeds in getting computers into cars, that sector should get a major boost.

The health implications also are good for growth. Los Angeles, which has the worst traffic in the nation, also leads — if that's the word — in hospital admissions due to respiratory ailments. The resulting medical bills go into the GDP. And while Americans sit in traffic they aren't walking or getting exercise. More likely they are entertaining themselves orally with a glazed donut or a Big Mac, which helps explain why the portion of middle-aged Americans who are clinically obese has doubled since the 1960s.

C. Everett Koop, the former Surgeon General, estimates that some 70% of the nation's medical expenses are lifestyle-induced. Yet the same lifestyle that promotes disease also produces a rising GDP. (Keynes observed that traditional virtues like thrift are bad for growth; now it appears that health is bad for growth too.) We literally are growing ourselves sick, and this puts a grim new twist on the economic doctrine of "complementary goods," which describes the way new products tend to spawn a host of others. The automobile gave rise to car wash franchises, drive-in restaurants, fuzz busters, tire dumps, and so forth. Television produced an antenna industry, VCRs, soap magazines, ad infinitum. The texts present this phenomenon as the wondrous perpetual motion machine of the market — goods beget more goods. But now the machine is producing complementary ills and collateral damages instead.

Suggestive of this new dynamic is a pesticide plant in Richmond, California, which is owned by a transnational corporation that also makes the breast cancer drug tamoxifen. Many researchers believe that pesticides, and the toxins created in the production of them, play a role in breast cancer. "It's a pretty good deal," a local physician told the *East Bay Express*, a Bay Area weekly. "First you cause the cancer, then you profit from curing it." Both the alleged cause and cure make the GDP go up, and this syndrome has become a central dynamic of growth in the U.S. today.

Mainstream economists would argue that this is all beside the point. If people didn't have to spend money on such things as commuting or medical costs, they'd simply spend it on something else, they say. Growth would be the same or even greater, so the actual content of growth should be of little concern to those who promote it. That view holds sway in the nation's policy councils; as a result we try continually to grow our way out of problems, when increasingly we are growing our way in.

PEOPLE DON'T CHOOSE TO PAY SOME $40 BILLION A YEAR IN TELEMARKETING FRAUD. THEY DON'T CHOOSE TO PAY 32% MORE FOR PRESCRIPTION DRUGS THAN DO PEOPLE IN CANADA.

To the extent that conventional economics has raised an eyebrow at growth, it has done so mainly through the concept of "externalities." These are negative side effects suffered by those not party to a transaction between a buyer and a seller. Man buys car, car pollutes air, others suffer that "externality." As the language implies, anything outside the original transaction is deemed secondary, a subordinate reality, and therefore easily overlooked. More, the effects upon buyer and seller — the "internalities," one might say — are assumed to be good.

Today, however, that mental schema is collapsing. Externalities are starting to overwhelm internalities. A single jet ski can cause more misery for the people who reside by a lake, than it gives pleasure to the person riding it.

More importantly, and as just discussed, internalities themselves are coming into question, and with them the assumption of choice, which is the moral linchpin of market thought.

If people choose what they buy, as market theory posits, then — externalities aside — the sum total of all their buying must be the greatest good of all. That's the ideology behind the GDP. But if people don't always choose, then the model starts to fall apart, which is what is happening today. The practical implications are obvious. If growth consists increasingly of problems rather than solutions, then scolding people for consuming too much is barking up the wrong tree. It is possible to talk instead about ridding our lives of what we don't want as well as forsaking what we do want — or think we want.

Politically this is a more promising path. But to where? The economy may be turning into a kind of round robin of difficulty and affliction, but we are all tied to the game. The sickness industry employs a lot of people, as do ad agencies and trash haulers. The fastest-growing occupations in the country include debt collectors and prison guards. What would we do without our problems and dysfunctions?

The problem is especially acute for those at the bottom of the income scale who have not shared much in the apparent prosperity. For them, a bigger piece of a bad pie might be better than none.

This is the economic conundrum of our age. No one has more than pieces of an answer, but it helps to see that much growth today is really an optical illusion created by accounting tricks. The official tally ignores totally the cost side of the growth ledger — the toll of traffic upon our time and health, for example. In fact, it actually counts such costs as growth and gain. By the same token, the official tally ignores the economic contributions of the natural environment and the social structure; so that the more the economy destroys these, and puts commoditized substitutes in their places, the more the experts say the economy has "grown." Pollute the lakes and oceans so that people have to join private swim clubs and the economy grows. Erode the social infrastructure of community so people have to buy services from the market instead of getting help from their neighbors, and it grows some more. The real economy — the one that sustains us — has diminished. All that has grown is the need to buy commoditized substitutes for things we used to have for free.

So one might rephrase the question thus: how do we achieve real growth, as opposed to the statistical illusion that passes for growth today? Four decades ago, John Kenneth Galbraith argued in *The Affluent Society* that conventional economic reasoning is rapidly becoming obsolete. An economics based upon scarcity simply doesn't work in an economy of hyper-abundance, he said. If it takes a $200 billion (today) advertising industry to maintain what economists quaintly call "demand," then perhaps that demand isn't as urgent as conventional theory posits. Perhaps it's not even demand in any sane meaning of the word.

Galbraith argued that genuine economy called for shifting some resources from consumption that needs to be prodded, to needs which are indisputably great: schools, parks, older people, the inner cities and the like. For this he was skewered as a proto-socialist. Yet today the case is even stronger, as advertisers worm into virtually every waking moment in a desperate effort to keep the growth machine on track.

Galbraith was arguing for a larger public sector. But that brings dysfunctions of its own, such as bureaucracy; and it depends upon an enlarging private sector as a fiscal base to begin with. Today we need to go further, and establish new ground rules for the economy, so that it produces more genuine growth on its own. We also need to find ways to revive the nonmarket economy of informal community exchange, so that people do not need money to meet every single life need.

In the first category, environmental fiscal policy can help. While the corporate world has flogged workers to be more productive, resources such as petroleum have been in effect loafing on the job. If we used these more efficiently the result could be jobs and growth, even in conventional terms, with less environmental pollution. If we used land more efficiently — that is, reduced urban sprawl — the social and environmental gains would be great.

Another ground rule is the corporate charter laws. We need to restore these to their original purpose: to keep large business organizations within the compass of the common good. But such shifts can do only so much. More efficient cars might simply encourage more traffic, for example. Cheap renewable power for electronic devices could encourage more noise. In other words, the answer won't just be a more efficient version of what we do now. Sooner or later we'll need different ways of thinking about work and growth and how we allocate the means of life.

This is where the social economy comes in, the informal exchange between neighbors and friends. There are some promising trends. One is the return to the traditional village model in housing. Structure does affect content. When houses are close together, and people can walk to stores and work, it encourages the spontaneous social interaction that nurtures real community. New local currencies, such as Time Dollars, provide a kind of lattice work upon which informal nonmarket exchange can take root and grow.

Changes like these are off the grid of economics as conventionally defined. It took centuries for the market to emerge from the stagnation of feudalism. The next organizing principle, whatever it is, most likely will emerge slowly as well. This much we can say with certainty. As the market hurtles towards multiple implosions, social and environmental as well as financial, it is just possible that the economics profession is going to have to do what it constantly lectures the rest of us to do: adjust to new realities and show a willingness to change.

ARTICLE 2 *May 2001*

WHEN IS THE ECONOMY IN A RECESSION?

YOU'LL KNOW BEFORE THE ECONOMISTS DO

BY JOHN MILLER

Radical economists, according to an old joke, have successfully predicted ten of the last two recessions to hit the U.S. economy. But we're not the only ones predicting that the current economic expansion will end in recession before the end of the year. In March 2001, the prestigious Economic Cycle Research Institute concluded that a recession was "no longer avoidable." The last time the Institute made such a call was February 6, 1990 – just before the economy last plunged into recession.

The threat of recession is genuine. Slower economic growth abroad, higher oil prices, stagnating stock prices, and last year's jacked-up interest rates have already damped down U.S. economic growth. The real gross domestic product (GDP) grew at an annual rate of just 1% during the last three months of 2000 and a somewhat higher but still slow 2% during the first quarter of this year. While that sluggish growth has kept alive the current expansion, which began back in March 1991 and is already the longest in our economic history, the economy is hardly out of the woods. (See chart).

Some sectors of the U.S. economy are already suffering recession-like conditions. The manufacturing sector has endured its worst downturn since the last recession. Beginning in October 2000, manufacturing output declined for six months running, as rising energy costs, a strong dollar,

U.S. BUSINESS CYCLES, 1949-2001

Trough	*Peak*	*Trough*	*Expansion*	*Contraction*	*Full Cycle*
				Number of Months	
Oct 1949	July 1953	Aug 1954	45	13	58
Aug 1954	July 1957	Apr 1958	35	9	44
Apr 1958	May 1960	Feb 1961	25	9	34
Feb 1961	Nov 1969	Nov 1970	105	12	117
Nov 1970	Dec 1973	Mar 1975	37	16	53
Mar 1975	Jan 1980	July 1980	57	6	63
July 1980	July 1981	Nov 1982	12	16	28
Nov 1982	July 1990	Mar 1991	93	8	101
Mar 1991	???		121+		

and lower consumer spending cut into profits and sales. As manufacturing slumped, workers lost their jobs. The sector shed over 250,000 jobs from June 2000 through January 2001. Even top corporations such as General Electric and Daimler Chrysler announced large layoffs. Michigan's auto-dominated economy could shrink nearly 3% this year, David Littmann, chief economist of Detroit's Comerica bank, told the *Wall Street Journal.*

The high-tech "new economy" is hurting just as much as the smokestack industries. The NASDAQ, the supercharged high-tech stock index, has lost half its value over the last year. Production of computers, semiconductors, and communications equipment, after growing well over 30% in 2000, is now barely increasing. New orders for technical equipment are plunging into the negative range, the worst performance since the last recession. And with the NASDAQ meltdown, no new wave of venture capital is likely to rescue the high-tech sector anytime soon.

Worried that recession conditions will spread across the economy, leading to a collapse of consumer spending and investment, the Federal Reserve Board repeatedly cut interest rates during the first half of this year. So far, the rate cuts have helped forestall a recession. Lower interest rates have coaxed many homeowners to refinance their mortgages, partially offsetting the effect stock market losses are having on their spending. But maintaining consumer spending in the face of mounting layoffs, deteriorating consumer confidence, and rising consumer debt, already at higher levels than during the 1990-91 recession, will not be easy. If consumer spending collapses, a sharp downturn will quickly follow. The Fed then would be able to do little to forestall a recession as corporations, unable to sell their inventories and saddled with excess capacity, balk at making new investments.

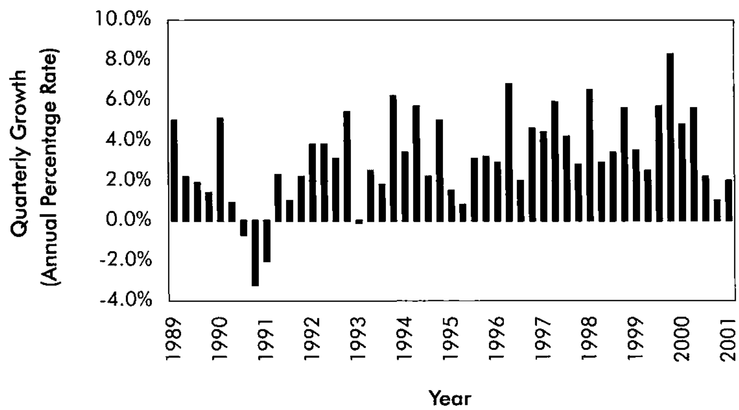
Despite all the signs of an economic downturn, the National Bureau of Economic Research (NBER), a private research organization designated by the Commerce Department as the nation's arbiter of the business cycle, has still not met to determine if the economy has fallen into recession. "Nothing in the data is yet anywhere close to the point that the [NBER] would investigate whether a peak occurred in late 2000," writes Stanford economist Robert Hall, chair of the NBER's business-cycle dating committee.

Still, the NBER's refusal to meet does not offer much comfort. The dating committee does not forecast recessions. It usually dates them after the dust settles. Should the current slowdown turn into a recession, we will have to live with its effects for a year or more before the NBER declares it "official."

A DATE WITH THE BUSINESS CYCLE

The NBER tracks the waves of the business cycle, from the trough of a recession to the peak of an expansion and back down into a trough. In the first phase of the cycle – the ex-

REAL GDP GROWTH



pansion – the economy grows as companies produce more goods and services and hire more workers. In the second phase, when the economy begins contracting, companies produce fewer goods and throw workers out of their jobs. The NBER has identified eight business cycles in the U.S. economy since World War II. (See table.) Its current task is to decide whether the expansion phase of the current business cycle, the ninth since World War II, has ended and the recession phase has begun.

The NBER's Dating Committee, currently a group of seven economists, admits that the dating process is "fuzzy." The committee has no rigid rules for determining the start or finish of a business cycle. The members rely on developing a consensus after studying a broad array of macroeconomic indicators. In short, they eyeball the data. The committee's founders worked with 46 indicators. Today the NBER's *Business Conditions Digest* lists around 1,000 measures. Members study the GDP, the index of industrial production, several interest rates, and personal income, among many other indicators. They also look at several composite indices, including the index of coincident indicators, which measures employment, income, output, and sales.

This last recession shows how hard it is to date business cycles. Economists define a recession as two consecutive quarters of negative real growth, or declining output, as measured by GDP. But applying this definition is not easy. It takes time for the federal government to publish official GDP figures. And the committee looks for several indicators to create a pattern before it feels comfortable declaring a recession. The NBER waited until spring 1991 before it declared that a recession had started the previous July. By then most economic indicators – including real growth rates for GDP – finally fit the definition.

If dating the onset of a recession is difficult, however, dating its end is even harder. Economists agree even less on how to determine when a recession finishes and an expansion begins. They generally divide an expansion, or a growing economy, into two phases. In its first phase, the economy recovers ground lost – in terms of jobs, output, and other measures – during the recession. When the economy expands beyond its pre-recession levels, it enters its second phase. Economists declare a recession over only when they know a recovery has reached this second phase. They then date the expansion at the point when the economy began recouping the lost output. Should the recovery falter and the economy start to contract again before the first phase finishes, economists will consider the recession uninterrupted.

With this last recession, the expansion began in March 1991. The economy grew sluggishly through the second half of 1991 and 1992. At that point, civilian employment, real personal income, and industrial output still had not reached their pre-recession peaks. The Dating Committee finally declared March 1991 the official end of the recession when, in the third quarter of 1992, more rapid growth finally pushed GDP beyond its pre-recession level.

RECESSION AND ECONOMIC HARDSHIP

With its expansion phase under way, faster growth followed – especially after 1995, when high-tech investment picked up. Those growth rates accelerated again after 1997, as consumption boomed and funds fleeing the East Asian economic crisis helped fuel a speculative boom in the U.S. stock market.

Consumption-fueled, stock market-juiced, and high-tech driven growth rates exceeded 4% in each of the last four years and reached 5% in 2000. The fall from these high growth rates, the most robust of the expansion, has already been painful. The stock market has turned sour, high-tech investment has halted, and consumer spending has begun to falter.

EVEN IF THE ECONOMY CONTINUES TO LIMP ALONG AT CURRENT SLOW GROWTH IN THE 1% TO 2% RANGE, THE RESULTS WILL HIT WORKERS AND FAMILIES HARD.

Even if the economy continues to limp along at current slow growth in the 1% to 2% range – what the Federal Reserve Board calls a "soft landing" – the results will hit workers and families hard. Only during the last few years, as labor markets have tightened, have most workers enjoyed rising wages. It took until 1998 for the "record" expansion to add back the purchasing power workers lost in the relatively mild recession of the early 1990s. Even still, real wages remained lower than they were some 30 years ago.

Before the NBER dating committee has even gotten around to meeting about the current downturn, real wages (especially in manufacturing) and employment opportunities have already stopped improving. It is time economic policy makers faced up to that, recession or no.

Resources: Robert E. Hall, "The NBER's Recession Dating Procedure in the Light of Current Developments," *National Bureau of Economic Research*, 18 April 2001; Economic Cycle Research Institute, *Newsletter*, March 2001; Michael J. Mandel et al., "Two More Years? The Tech Slump," *Business Week*, 30 April 2001; Rich Miller et al., "Downturn in Fast-Forward," *Business Week*, 19 February 2001.

January/February 2002

RECESSION FOR THE HOLIDAYS

BY JOHN MILLER

Talk about a lump of coal in your stocking. Late in November, just as the holiday season was taking hold, the National Bureau of Economic Research (NBER)—the nation's official arbiter of the business cycle—declared the economic slowdown that began in March 2001 to be a recession.

In some ways, the NBER declaration was hardly big news. Even before last March, many had already fallen on hard times. During the fall of 2000, economic growth—which had averaged a brisk 5% over the previous year—suddenly slowed to just over 1%. Manufacturing slumped, dot.coms shut their doors, and the stock-market boom fizzled.

In other ways, though, the announcement was surprising. By declaring that the recession began back in March, the NBER confirmed that the economy was well into a downturn before September 11. The economic fallout from the September 11 attacks did cause a faster and deeper drop-off in economic activity, and did help to convince the NBER that the downturn would neither reverse itself quickly nor be so mild as to not qualify as an actual recession. But now it's official: It didn't cause the recession.

In addition, by dating the onset of the recession back to March, the NBER ignored the economist's shorthand definition of a recession: two consecutive quarters of decline in Gross Domestic Product (the broadest single measure of economic output) adjusted for inflation, or real GDP. Real GDP fell in the third quarter of last year and undoubtedly contracted again in the last three months of 2001, but the NBER found a significant decline in economic activity well before then. Both industrial production and real (adjusted for inflation) sales in the manufacturing, wholesale, and retail sectors peaked early in the fall of 2000, and have fallen steadily since then. Once overall employment began to drop after March 2001, as job losses in manufacturing started to outweigh job gains in other sectors of the economy, the downturn was underway.

The official declaration also closed the book on the longest economic expansion in U.S. history, which began in March 1991 and lasted for 120 months. The much-heralded 1990s boom had inspired paeans to the "New Economy" and anointed Federal Reserve Chair Alan Greenspan as "Wizard Deluxe" of economic policy making. Nowadays, we don't hear much about either. The collapse of NASDAQ (the high-tech stock index) and the disappearance of gaggles of dot.com venture capitalists have raised doubts about whether the "New Economy" was authentic. Nor did the bursting of the stock market bubble do much for Greenspan's reputation. Greenspan did issue a 1997 warning about the market's "irrational exuberance." But in an act of colossal neglect, he took no direct action to deflate the bubble; for example, he could have raised the margin requirement (or down payment) for purchasing stock on credit. The current economic contraction, brought on in part by Greenspan's repeated interest rate hikes in the second half of 1999 and the first half of 2000—and so far immune to his now-furious cutting of interest rates—has further exposed the man behind the Fed's curtain.

How long will the recession last? That's hard to say. Since World War II, U.S. recessions have averaged 11 months. As you read this, the economy will already have logged about ten months of contraction. Most financial analysts believe recovery will begin in the first half of 2002. The November 2001 turnaround in the stock market made up the ground lost since September 11, and stronger-than-predicted consumer spending at the start of the holiday season gave cause for optimism too. In fact, a few economic forecasters are already yammering about a shallow recession, no worse than that of 1990-91, soon to be followed by the return of rapid economic growth.

But there are good reasons to believe that this downturn will be neither short nor shallow. Each positive piece of economic news last fall was matched by equally bad economic tidings. Consumer confidence plummeted to an eight-year low as job losses mounted; consumer debt exceeded the levels reached in 1990-91; stock market indicators remained below March 2001 levels; and stocks continued to be overvalued by historical standards, suggesting that a stock market rally is unlikely to be sustained.

There are other indications that this recession will be no better—and could be worse—than the usual postwar fare. First, for the first time since 1974, a recession in the United States has coincided with economic downturns in Europe, Japan, and much of the developing world. Simultaneous slowdowns across the globe will feed on each other, making for a prolonged downturn. For example, the worldwide 1974-75 recession dragged on in the United States for 16 months. Second, unlike every other postwar recession, the current downturn is business-led, not consumer-driven. The bursting of the stock-market bubble, the collapse of the dot.coms, and the decline of the manufacturing sector all contributed to the recession. By September 2000, industrial production had already fallen off by 6%, surpassing the average decline of 4.6% for earlier postwar recessions. The drop in consumer spending, made worse by September 11, came later.

Beyond that, the Fed will be hard put to counteract the downturn. With lingering excess productive capacity across the economy, devastated conditions in manufacturing, and a high-tech sector in disarray, businesses will be reluctant to make new investments even if the Fed cuts interest rates further. Lakshman Achuthan, managing director at the Economic Cycle Research Institute (the New York City-based group that, back in March, said a recession was "no longer avoidable"), points out that the last time business led the way downward was during the Great Depression.

This is not to suggest that a depression is in our immediate future. But, whether an official recovery comes early or later, the economy will continue to sputter. Even the business press is worried that the post-bubble economy will slip into a period of prolonged stagnation. In early November, one *Wall Street Journal* headline dared to ask, "Is the U.S. Economy At Risk of Emulating Japan's Long Swoon?"

Whether the economy expands or contracts, this much is clear: Working people will be tightening their economic belts for the foreseeable future. Workers did not begin to make significant gains during the 1990s boom until labor markets tightened—well into the second half of the expansion. And even when the current flagging economy begins to recover, unemployment rates will keep climbing—because employers will do little hiring until economic gains are solidified, and the hardest-hit sectors will continue to lay off workers. Should the economic stimulus package currently before Congress be passed into law, it will do more to relieve large corporations of their tax burden than to provide relief for those thrown out of work by the recession.

ARTICLE 4

February 2000

ECONOMY SETS RECORDS FOR LONGEVITY— AND INEQUALITY

BY JOHN MILLER

In the midst of the Great Depression, Random House published the first paperback, *Lost Horizon.* James Hilton's novel transported its readers from the economic hardships of 1933 to the valley of Shangri-La, a utopian community tucked away in the Himalayas, whose inhabitants lived in kindness and peace free from economic hardship and seemingly without aging.

The ideologues of today's new economy have gone one step further than the Depression-era paperback writer. They have brought Shangri-La to us. "These are the best of economic times by any measure," exults Marc Zandi, chief economist at the Dismal Scientist, an economic-consulting firm. "The economy is growing rapidly, inflation is nonexistent, unemployment is the lowest it ever has been and real median household income—probably the best measure of our standard of living—had never been higher."

In our new economy, "economic expansions don't die of old age," says Janet Yellen, former chair of President Clinton's Council of Economic Advisors.

But for many, today's buzz about the new economy is no more real than Hilton's story of Shangri-La. The new economy spreads its benefits widely but unevenly. Great gobs of wealth accumulate at the top, while only a thin layer of modest gains goes to most workers and still others miss out altogether, pushing economic inequality in the 1990s to a postwar high. Looking more closely, we will see that the new economy is far from Shangri-La.

A RECORD BREAKING EXPANSION?

Today's economy is no doubt the strongest in several decades. Nonetheless, the macroeconomic performance of the last decade fails on most counts to measure up to the standards set by the economic boom of 1961 to 1969, the strongest period of economic growth of the old economy. In addition, during the earlier boom, a labor movement far stronger than today's—and a federal government that led a war on poverty—made for more equitable economic growth.

If length is all that matters, the 1990s expansion is the winner. It is now the longest boom, this spring outdistancing the 1960s expansion, the previous record holder. Since March 1991, the end of the last recession, the U.S. economy has grown continuously for 110 months, more than twice the postwar average of 50 months, and it is still growing. "That's an impressive achievement. The equivalent of a human living to be 100," says Nicholas Perna, an economic analyst based in Ridgefield, Connecticut.

That long life has made a difference. After taking twice as long as most U.S. economic expansions to make up the ground the economy lost in the previous recession, the pace of economic growth picked up in the second half of the 1990s, lifting the average growth rate for the expansion to 3.3% (after correcting for inflation).

Still even that mark falls well short of a record. The postwar *average* real growth rate during economic expansions is considerably higher, and the 1960s boom maintained a 4.8% growth rate for nearly a decade.

It is a similar story on the jobs front. Shedding its earlier label as a jobless recovery, the 1990s expansion created more than the 2 million jobs a year promised by the Clinton Administration. But once again the 1960s boom did better, creating jobs more rapidly.

The 1990s job growth did push down unemployment rates to levels not seen since the 1960s boom. The unemployment rate fell to 4% at the beginning of this year, well below levels that many traditional economists called full employment at the beginning of the 1990s. But unemployment rates during the 1960s fell further and to lower levels, reaching a low of 3.5% in 1969. But when it comes to price stability, the 1990s economy beats the 1960s boom. As the 1960s economy heated up and spending on the Vietnam War escalated, inflation rates picked up, increasing more than fivefold from 1961 to 1969. In the 1990s, prices have remained stable as unemployment rates have dropped. Inflation rates today are no higher than those at the beginning of the expansion, some nine years ago. That is new.

The conventional wisdom about the new economy is that computer-driven productivity gains have made it possible to have both tight labor markets and price stability by reducing labor costs. But even with the boost of computer technology, productivity gains in the 1990s averaged just under 2% a year while the 1960s gains were closer to 3% each year. And despite all the hoopla about a new technological revolution, most traditional economists are not willing to say that the uptick in productivity gains will be sustained.

Trends other than computerization offer a more reliable explanation of this new-found price stability in the face of tightening labor markets: modest wage demands at home and misfortune abroad.

Corporate downsizing and layoffs from mergers have continued even as the economy has boomed, keeping workers anxious and their wage demands in check. While worker's real wages and purchasing power improved, after declining in the 1980s, wage gains during the 1990s were indeed modest, especially when compared to the 1960s. From 1991 to 1999, the real hourly wages of nonsupervisory workers rose just 5.6%. In the last few years wage gains have picked up and have been spread more broadly as labor markets have tightened and following a hike in the minimum wage. Still, it took until 1998 for the expansion to add back the purchasing power workers lost in the relatively mild recession at the beginning of the decade.

The 1960s expansion added nearly three times as much to workers' purchasing power. And by 1969, workers' real wages were higher than today, some 30 years later.

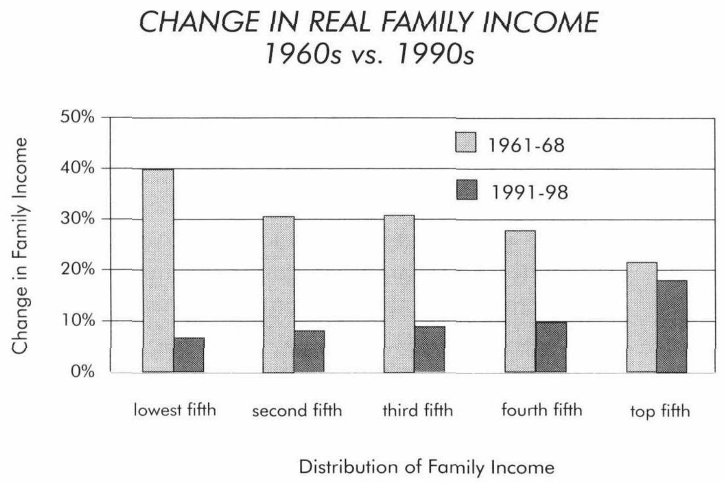
Just as wage levels exerted little upward pressure on prices, falling currency values in countries hard hit by the economic crisis in East Asia helped to keep prices down in the United States. At the same time, foreign investors fleeing financial instability elsewhere poured billions into the soaring U.S. stock market and government bonds, effectively lending money to the U.S. expansion. In pushing up the value of the dollar, they also reduced the cost of imported goods for U.S. consumers.

Beyond price stability, the hallmark of the current expansion surely has been its rip-roaring stock market. Far smaller stock market gains for investors in the 1960s had the virtue of not being so different from workers' wage gains. No such equality exists today. In the last decade, as Doug Henwood, publisher of the *Left Business Observer*, points out, stock market gains for investors were nearly 40 times the wage gains of workers. According to the editors of the *Wall Street Journal*, however, there is no need to worry. We live in the era of the "worker capitalist." More U.S. households than ever before own stock, and as a result, "the 1990s have benefited just about everyone."

True enough, according to the Federal Reserve Board's latest Survey of Consumer Finances, in 1998 48% of U.S. families, the highest number ever, owned stock directly or indirectly through mutual funds or 401(k) retirement plans. Still stock ownership remains highly concentrated. Fewer than one in 10 families with an income under $10,000 owned stock while nine of every ten families with incomes above $100,000 owned stock. As a result, the stock market boom has doled out its gains in a stunningly unequal fashion.

From 1989 to 1998 the net worth (total assets minus debt) of the median family increased about 20%, only about one-tenth of the added value in the stock market. The net worth of the median family most likely to have children at home—those headed by someone under 54—actually declined. So too did the net worth of the median family without a college degree. At the same time, the share of net worth of the richest fifth of families rose from 83.5% in 1989 to 84.5% in 1998, adding to economic inequality not reducing it.

All told, then, the new economy may have outlived the longest expansion of the old economy, the 1960s boom.



Source: Changes in family income in 1998 dollars for the upper limit of the lowest, second, third and fourth quintile, and the lower limit of the top 5% of families by income. Annual data from U.S. Census Bureau.

But on most counts its macroeconomic performance falls short—far short in some cases—of that of the older boom. The two exceptions are price stability, which is purchased in large part by suppressing workers' wages, and a booming stock market that continues to shower the great bulk of its gains on the well-to-do.

HOW MANY BOATS DID THE RISING TIDE LIFT?

Much like John F. Kennedy in the beginning of the 1960s, the new economy boosters also promise that the economic rising tide will lift all boats. Let's perform three experiments to test just how many boats the 1990s expansion lifted and how far and how evenly it lifted them when compared to the 1960s expansion.

Our first test looks at the real income of the median family. Corrected for inflation, the income of the family in the middle of the distribution of income is at an all-time high. By 1998, the real income or purchasing power of the median household had risen 8.7%, or roughly 1% a year, since the expansion began in 1991. But if you factor in the ground lost during the previous recession, 1998 real income was just 2.3% higher than in 1989, the peak of the previous business cycle.

That is a far cry from prosperity, especially when compared to the gains in real income for the median family during the 1960s expansion. Corrected for inflation, the income of the median family grew 29.8%, or nearly 4% each year, from 1961 to 1968 and even more, some 33.6%, from the peak of the previous business cycle in 1959.

A second experiment, looking at the effect of the 1990s boom on poverty rates, reveals once again that the new economy claims of widespread benefits are overblown. Measured poverty rates are down. In 1998, the poverty rate was 12.7%, the lowest rate in two decades.

That is something to celebrate, but not for very long. Poverty rates were lower throughout the 1970s. Compared to the 1993 high of 15.2%, the current rate seems to have made progress, but not when compared to the rate at the peak of the last expansion in 1989—12.8%. That was also the low achieved in the 1960s boom.

To take the true measure of how widely the new economy has spread its benefits, our third experiment examines how the real income of five families stationed at different points across the distribution of income changed during the 1990s expansion. If we look from the conservative's favorite starting point, 1991, the 1990s expansion lifted all five boats arrayed across the distribution of income from the 20th percentile to the 95th percentile. But considering that 1991 was the bottom of the recession, most boats really did not rise very far. Real income gains were hardly more than 1% a year for all but the richest family, and the poorest family got the smallest gains. (See chart.)

If we take one step back and measure improvement from 1989, we get a better sense of how little progress most families made during the 1990s. The real income of each of the five families increased, but those gains are miniscule in the middle and the bottom and sizable only for those at the top.

Take another step back to 1979, the year before conservative economic policies took hold, and the rising economic tide no longer lifts all boats, let alone brings prosperity to the majority of families. The poorest of our five families lost real income since then, and only the real income of families in the top 20% increased as much as 1% each year.

The old boom of the 1960s comes far closer to living up to the rhetoric of the new economy. From 1961 to 1968 the poorest of the five families saw the biggest gains, just about a 40% jump in real income. The richest of the five families saw the smallest relative gain. And the real income gains for all five representative families were greater in the 1960s than in the 1990s, and more than three times larger for all but the richest family.

In addition, some families missed out entirely during the 1990s boom. In New England, California, and New York, economies with large service sectors, households at the bottom lost ground as the well-to-do in their states made out during the 1990s. *Pulling Apart,* a recent joint report of the Center on Budget and Policy Priorities and the Economic Policy Institute, documents this worsening inequality. In 11 states, the incomes of families in the poorest fifth of the population dropped by more than 10% during the decade

By 1998 economic inequality in the United States was at its worst since the Great Depression. The richest fifth of households now receive nearly one-half of the nation's income. While economic inequalities in 1968 were pronounced, they were moderate by today's standards, and in that decade economic growth lessened economic inequality instead of adding to it.

CLINTON'S PACT WITH THE DEVIL

Economic growth is more inequitable today than in the 1960s also because corporations have captured not only the gains from economic growth but also the public policy agenda. During the 1960s boom, roughly one in four U.S workers were members of labor unions, about twice today's figure, and worker's bargaining power, while already on the decline, was much greater than today. And in that earlier period, stronger labor and social movements pushed the federal government to undertake programs that mitigated the worsening inequality that comes with rapid economic growth.

The expanding welfare state of the 1960s helped to lift dinghies along with the yachts. While no panacea, what that spending accomplished was Herculean by today's standards. In 1964 the Johnson Administration launched a "national war on poverty" that enacted Medicaid (medical care for the poor), Medicare (medical care for the elderly), and expanded Social Security coverage to most workers. It also put in place new programs targeted at particular needs: food stamps, aid to schools in deserted areas, and low-income housing subsidies, among others. All told, these programs, along with increased military outlays, pushed up federal spending from 18% of GDP to 21% of GDP.

You might have expected a similar effort from the Clinton Administration. After all, as a presidential candidate Bill Clinton promised to "Put People First" and just last year he selected FDR, the architect of the U.S. welfare state, as his man of the century. But New Democrat Clinton turned his back on the old agenda and instead instituted a program of budget austerity not so different from the one favored by his presidential rival Ross Perot.

Even conservatives noticed. "The good news of the Clinton presidency," says Stephen Moore of the Cato Institute, the think-tank championing free enterprise, is that "the federal government is getting smaller, at least relative to the size of the economy." This year, for the first time in more than 25 years, federal spending slipped below 20% of GDP. While post-Cold War defense cutbacks contributed to the trend, domestic spending is shrinking relative to private output. Federal government investment in physical capital, education and training, and research and development has already dropped from 2.6% to 1.6% of GDP in the past two decades.

Clinton now brags of having run the first back-to-back surpluses in 40 years, but those who would have benefited from the federal spending eliminated by his austerity budgets are paying the cost. In return for Clinton's fiscal discipline, Fed chief Alan Greenspan loosened his grip on the money supply and accepted lowered interest rates for a time.

Nor will Greenspan look the other way should tighter labor markets embolden workers "to start pounding the table for higher wages," as economist John R. Stanke, CEO of Chicago-based International Survey Research, fears they will this year. Rising wages and labor costs could eat into corporate profit margins or ignite a pickup in inflation that would erode the real returns on the financial markets of the well-to-do. In either event, the Fed is likely to sharply tighten the money supply in an attempt to keep labor costs in check, risking an end to the expansion.

MORE LIKE THE 1920S THAN THE 1960S

The new economy—driven forward by a galloping stock market, fast-paced technological change, reckless private borrowing, and gaping inequality—is more like the economy of the roaring 1920 than the 1960s boom.

The increased concentration of wealth in the hands of a few threatens the stability of the new economy much as it did in the 1920s. Those monies, along with a borrowing binge, have pushed stock and other asset prices to historically unprecedented levels compared to corporate profits and economic growth. The economy is also saddled with unsustainable levels of corporate, consumer, and foreign indebtedness as well as a worsening trade deficit. At some point these mounting problems will cut short the new economy's experiment with suspending the economic aging process.

Just when that will happen no one knows. But even Alan Greenspan is worried. Ever since his 1997 warning that an "irrational exuberance" was driving up stock prices, Greenspan has repeatedly tried to jawbone the stock market back to reality. He was hard at it again in January 2000, telling the Economic Club of New York that today's market could be another of history's "euphoric speculative bubbles."

Should that happen, we will be reading far fewer paeans to the new economy. Until then it is up to you to choose which utopian fantasy you prefer: We will grow old in a new economy that enriches us all. Or somewhere there is valley of prosperity with a social organization that would truly allow all its citizens to live in peace and free of want.