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New Public Policy Brief No. 95

SHAKY FOUNDATIONS: POLICY LESSONS FROM AMERICA'S HISTORIC HOUSING CRASH

PEDRO NICOLACI DA COSTA

There are signs that the Federal Reserve's (Fed) policies of large interest rate cuts and vast liquidity injections are fueling yet another asset price boom, this time in the commodity markets, with consequences more dire than the bursting of the real estate bubble. The reluctance of the Fed to use its regulatory authority to prevent a new bubble from forming is even more perplexing, given the magnitude of the current recession. This new Public Policy Brief by Pedro Nicolaci da Costa discusses the effects of the Fed's policies on commodity speculation, questions the reasons behind the agency's reluctance to apply interventionist policies, and argues the need for a change in attitude toward market regulation among policymakers.

The author points out that the Fed's actions on rates and liquidity have exacerbated the U.S. dollar's decline, and, in the process, have driven commodity prices to unprecedented heights. The rise in commodity prices has had a significant effect on the cost of nondiscretionary goods such as food and fuel, which make up the lion's share of the low-income consumer's budget; sharp food price increases have led to widespread shortages, and to food riots in some poor nations. Thus, the Fed's policies are helping to deprive some of the most vulnerable sectors of the global population of basic resources.

Since the Fed's regulatory powers are vast, the author asks why these powers have not been employed to dampen excessively risky speculative behavior. Da Costa examines the official view that asset bubbles are impossible to spot until it is too late, and that preemptive policies aimed at a particular sector in trouble, such as the stock market, also run the risk of derailing the broader (healthy) sectors of the economy. Therefore, the Fed believes that the control of speculative bubbles should remain outside its policy concerns. Da Costa disputes this reasoning. In the buildup to the housing crash, he says, there were plenty of warning signs: loan-to-value ratios were going through the roof, perceptions of risk (as evidenced by credit spreads) were at all-time lows, and in coastal

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The Levy Economics Institute of Bard College, founded in 1986, is a nonprofit, nonpartisan research organization devoted to public service. Through scholarship and economic research it generates viable, effective public policy responses to important economic problems that profoundly affect the quality of life in the United States and abroad.

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areas, home prices doubled, or even tripled, in a matter of a few years. Moreover, notes the author, the collapse of the overinflated housing market was widely predicted by a number of analysts, and asset bubbles in general have become increasingly obvious. (Former Fed Chairman Alan Greenspan himself spotted the stock market bubble well in advance of its peak in 2000.) If the Fed were to apply preemptive measures at early stages of a developing bubble, when its spillover effects are weak, it can also ensure that there are no adverse effects on the rest of the economy. The author therefore argues that asset prices must come under the central bank's purview in order to bring a degree of stability to the economy.

A major reason for the relative absence of regulatory measures is the prevailing tendency to associate regulation with inefficiency and a cumbersome bureaucracy. Da Costa argues that a change of attitude among regulators is even more important than shifts in policy; Fed officials must be convinced of the need for greater regulatory scrutiny. He notes that regulation simply provides a set of ground rules determined with broader social interests in mind, and that it often enhances, rather than erodes, business confidence; for example, companies on U.S. exchanges are viewed in a more positive light by prospective investors when tight regulatory and accounting standards are in place.

For the complete text, go to www.levy.org/pubs/ppb_95.pdf.

New Policy Note

What's a Central Bank to Do? Policy Response to the Current Crisis

L. RANDALL WRAY

Policy Note 2008/3

This new Policy Note by Senior Scholar L. Randall Wray assesses the adequacy of the Federal Reserve's (Fed) responses to the current U.S. recession, and examines more effective policy alternatives. Wray highlights the urgency of such a task by noting the deterioration in the economy's short- to medium-term prospects, as evidenced by the increasing number of foreclosures and the spread of financial losses far beyond the real estate sector. The current consensus on the need for central bank activism, in the form of changes in some "neutral " target interest rate in reaction to demand gaps, is hard to maintain, as the neutral rate can only be determined once it has been achieved. Moreover, the impact of rate changes is not so much on the cost of borrowing as on expectations; it is a signal to the market of the Fed's intention to contain inflationary expectations. However, as the current situation demonstrates, expectations management cannot prevent speculative bubbles, nor can it revive a weak economy in the aftermath of a bust. Indeed, lower interest rates on safe U.S. assets and the fear of an economic meltdown in the States sparked a movement away from the dollar. The effect of the latter on U.S. exports, Wray maintains, is limited by its inflationary impact, as domestic prices must rise to prevent U.S. residents from consuming goods destined for export. The falling dollar has encouraged the commodity price boom, reinforcing consumer price increases.

Wray considers alternative policy options and notes that the current fiscal stimulus package, based largely on tax rebates equal to 1 percent of GDP, did in fact stimulate the U.S. economy to a limited extent but has now run out of steam. Moreover, the combination of the dollar's fall and the rise in commodity prices has heightened inflationary pressures. The result has been "stagflation"; that is, rising prices combined with slow growth. The author considers the United States to be too rich and too large a country to rely solely on export-led growth to revive its economy, and argues for the suspension of a cheap dollar policy. His first recommendation is a fiscal stimulus based on the rebuilding and expansion of U.S. infrastructure—a particularly effective policy given the depressed state of the American construction industry. Furthermore, a substantial part of such an expansion should be directed toward expanding public transportation systems in order to conserve petroleum. His second policy recommendation is a plan for homeowner debt relief, combining debt write-downs, easier repayment terms, and the government's purchase and retention of troubled mortgages until the real estate sector recovers. Finally, he argues in favor of ending the "marked to market" valuation of bank assets. This practice generates exceedingly risky speculative behavior in a boom, as the market discounts default probabilities. In a bust, however, banks see asset prices fall, and are forced to accept "marked to market" losses or even to sell into a declining market, thus pushing prices down even further. Wray notes that the most important way banks fuel speculation is through off-balance-sheet operations that hide liabilities, and suggests that any institution involved in issuing home mortgages should be subject to leverage limits and the requirement that all its liabilities be shown on its balance sheet.

For the complete text, go to www.levy.org/pubs/pn_08_3.pdf

New Working Papers

Deficient Public Infrastructure and Private Costs: Evidence from a Time-use Survey for the Water Sector in India

LEKHA S. CHAKRABORTY

Working Paper No. 536

In this working paper, Lekha S. Chakraborty, National Institute of Public Finance and Policy, India, tests the hypothesis that improved access to public services redresses intrahousehold inequality by enhancing the time available to women for paid market work. Public investment policy can reduce the time women must allocate to unpaid work such as sanitation services and the collection of water and fuel. Evidence suggests that easy accessibility to drinking water facilities might lead to an increase in school enrollment for girls; in Madagascar, for instance, 83 percent of the girls who do not attend school spend their time collecting water.

Chakraborty notes certain deficiencies in the time-diary methodology common to most time-use surveys, in which respondents record how they spend each 24-hour period, and outlines the practical steps necessary to overcome them. For example, in recording time spent multitasking, the problem may be solved, she suggests, by respondents' separating the time-use data into primary and secondary activities. The author applies her model of time use to a 2000 survey conducted in six major Indian states by the government's Central Statistical Organization. She then sums up the available evidence on unpaid work and time use for India. The data indicate that women spent 50.5 percent of their time on unpaid work while men spent only 33 percent; the value of these unpaid activities could be as much as 38–41 percent of the State Domestic Product (using the individual state wage rate to value unpaid labor). The author points out that there are significant gender differentials in activities like fetching water and fuel, and in travel time, suggesting access to water infrastructure can release time locked up in nonmarket work for income-earning activities. She then sets up an econometric equation in which time available for market work is a function of public investment on water facilities across regions, time spent traveling, and the "opportunity cost of time"—the value of forgone earnings if the unpaid time were spent on market work, measured at the market wage rate. The estimated coefficients suggest that the relationship between infrastructure access and time allocated to market work is negative. The findings indicate that, the greater the time required to access basic services, the less time there is available for market-based work. This supports the hypothesis that better public water infrastructure may release women's time to more market-oriented work. The estimates also suggest that there can be a link between the deterioration of infrastructure and rural poverty in India, as the time spent bridging infrastructural gaps deprives the poor of available time for income-generating activity. Therefore, fiscal policies designed to redress income poverty are likely to be less effective if they do not take time poverty into account.

For the complete text, go to www.levy.org/pubs/wp_536.pdf.

The Keynesian Roots of Stock-flow Consistent Macroeconomic Models: Peering Over the Edge of the Short Period

ANTONIO CARLOS MACEDO E SILVA and
CLAUDIO H. DOS SANTOS

Working Paper No. 537

Post Keynesian economists have mostly been concerned with short-term macroeconomics in which supply and demand differ in some markets, while neoclassical models stress long-term equilibrium. In the latter, the functioning of market forces generates an "optimum" order in the long run. By contrast, Post Keynesian economists emphasize that, in the short run, there are suboptimum labor and credit markets, which persistently fail to equalize supply and demand. However, they have been unable to develop models of the consequences of market failures beyond the short term. In this working paper, Antonio Carlos Macedo e Silva, State University of Campinas, and Research Associate Claudio H. Dos Santos, Institute for Applied Economic Research, Brazil, argue that stock-flow consistent (SFC) macroeconomic models offer the basis for developing a much-needed medium-term Keynesian alternative that avoids the excessive emphasis on the short and long terms in current models.

The authors define SFC models as those in which various economic agents are identified with the main social categories/institutional sectors of the economy (e.g., household, government, and financial sectors). The relevant classification depends on the context. The stock market may be a critical agent for an advanced economy such as the United States, while state-owned industries may have a similar role in a developing economy. An SFC model then describes the short-term interactions of these agents and models their period-by-period balance-sheet dynamics. The authors start from the premise that Keynesian short-term equilibrium is determined by the portfolio decisions of wealth-owners. They also point out that Keynes himself divided the economy into three "classes"—investors, rentiers (owners of financial assets), and workers—in order to capture the influences of such decisions on the macro economy. The wealth-owning classes enjoy the privilege of changing the composition of their stocks of wealth through organized liquid markets, and by fund-raising through credit. The ways these agents interact when they decide to alter their portfolios lead to variations in the value of stocks that come from capital gains and losses, generating a new vector of asset prices different from the previous one and affecting future decisions—and thus altering the dynamics of the system. In this scheme, the decision to produce or employ is only a byproduct of the wider search by wealth-owners to increase their holdings. The core determinants of aggregate employment, according to this interpretation of Keynesian theory, are the portfolio decisions of wealth-owners. The causal macroeconomic chain starts from such decisions and ends with the multiplier effect, the ratio of the final change in income to an initial change in government expenditure. This interpretation is in the tradition of the financial Keynesianism of Americans James Tobin and Hyman P. Minsky, and differs from the "simplistic" dynamics of Michael Kalecki and Roy F. Harrod, in which effective demand is based on the interaction of the multiplier and the accelerator effects; that is, changes in investment determine a new capital output ratio, which in turn affects investment in the next period.

Macedo e Silva and Dos Santos stress the affinity between the Keynesian short-term equilibrium and the SFC models. The latter also start with the classification of relevant agents and all their assets and liabilities. This classification, of course, differs for different periods of an economy and across economies. The stock of wealth and the debt of agents generate financial flows between sectors, changing the balance sheets of the agents/sectors at the end of each short (accounting) period from what it was at the beginning. Since these changes will affect portfolio decisions in the subsequent period, linking short periods in order to construct longer-term models requires the clear mapping of the balance-sheet implications of each period. The authors believe that the SFC analysis makes clear whether the economic regime described is sustainable or unstable and identifies the conditions for equilibrium of steady-growth states, thus shedding light on the choice of economic policy proposals—features, they point out, that characterize the SFC macroeconomic model on which the Levy Institute's Strategic Analyses are based.

For the complete text, go to www.levy.org/pubs/wp_537.pdf.

The Buffett Plan for Reducing the Trade Deficit

DIMITRI B. PAPADIMITRIOU, GREG HANNSGEN, and GENNARO ZEZZA

Working Paper No. 538

The formulation of a sensible solution to the U.S. trade deficit is central to any plan for the revival of the American economy. In this working paper, President Dimitri B. Papadimitriou and Research Scholars Greg Hannsgen and Gennaro Zezza discuss a plan put forward by Warren Buffett and based on a government-issued "import certificate" scheme.

The authors present projections of the three macroeconomic balances (current account deficit, government deficit, and private sector balance) in three scenarios: a baseline, the original Buffett plan, and their modified version of the plan. Their baseline projection of the consequences of a continuation of existing policies is obtained from the Levy Institute macroeconomic model of the U.S. economy. The baseline assumes a "soft landing" scenario, meaning a gradual reduction in private sector borrowing achieved through slower growth of imports, generating a moderate slowdown in economic growth rather than a severe drop leading to a recession. Against this baseline, the authors first examine the original Buffett plan, whereby firms that exported $100 in goods would be entitled to a government–issued import certificate (IC) in the same amount. The certificate would entitle any firm in possession of it to import $100 worth of goods. The exporting firm itself could either import these goods or sell the certificates to other importers, in organized markets similar to those for carbon-emission credits in the European Union. Importers would then be required to submit the certificates back to the government.

ICs would encourage firms and consumers to buy fewer imported and more domestically produced goods; they would also encourage exporting firms to increase their output, raising employment in the export sector at the expense of more import-leaning sectors. A fall in the value of the dollar would provide an alternative by increasing the price of imports and reducing the price of exports. However, while the dollar has dropped by 22.3 percent since 2002, the devaluation has not been dramatic enough to have a significant impact on the current account deficit. In the authors' baseline model, the current account deficit gradually falls from 4.8 percent of GDP in the fourth quarter of 2007 to 4.3 percent in the following quarter. Under the Buffett plan, the current account deficit would have fallen to 1.3 percent over the same period. The authors estimate that the Buffett plan would initially raise the price of U.S. imports by about 9 percent and boost economic growth above what it would be under policies assumed in the "soft landing" scenario, and then below the path of the main sector balances over time.

The authors consider a number of drawbacks to the plan (e.g., retaliation by foreign trading partners) and formulate an alternate version to deal with the plan's effect on the distribution of income and wealth. They argue that import prices would most likely rise significantly under almost any plan to reduce the trade deficit, including Buffett's, but policymakers have the means at hand to make sure these costs are not passed on to those least able to bear them. This would suggest using the tax system to distribute some of the benefits of balancing the trade deficit to lower- and middle-income U.S. taxpayers—a key aspect of the authors' alternative plan. In this version, the certificates would be directly auctioned to importers rather than granted to exporters without charge, and the proceeds used to reduce payroll taxes, capturing revenues that would otherwise be put toward exporters' profits. Such a scheme would offset the effects of higher-priced imported goods on low-income earners, possibly reduce labor costs in the export industry, and should prevent fraud due to falsification of foreign "transactions." The authors' simulation of the revised plan shows that certificate-sale revenues would be sufficient to fund a payroll tax cut of approximately 2.4 percentage points each for employees and employers. Its economic growth effect would be about the same as in the original plan. The current account deficit figures for the revised plan are 4.9 percent of GDP for the last quarter of 2007, and 2.0 percent for the first quarter of 2008.

For the complete text, go to www.levy.org/pubs/wp_538.pdf.

The Return of Fiscal Policy: Can the New Developments in the New Economic Consensus Be Reconciled with the Post Keynesian View?

PAVLINA R. TCHERNEVA

Working Paper No. 539

Mainstream orthodox macroeconomics is evolving in a direction more open to the influences of some forms of fiscal policy as a means of stimulating the economy—a policy tool traditionally associated with Keynesian economics. Yet, important differences over the role of fiscal policies remain between this new mainstream macroeconomics, also known as the New Economic Consensus (NEC), and classical Keynesian economics. In this working paper, Research Associate Pavlina R. Tcherneva examines the chief features of the NEC and the limitations of its current thinking on fiscal policy, contrasting them with post-Keynesian policy prescriptions for economic revival.

One defining feature of the NEC concerns its rejection of the monetarist view that central banks can exogenously alter the stock of money. Instead, the NEC argues that the banks can only set the short-term interest rate to control inflation. Moreover, changes in interest rates affect investment through the cost of borrowing, giving monetary policy additional influence over output and therefore over aggregate demand management, should output deviate from its natural level achieved under fully flexible prices. However, the NEC acknowledges the policy ineffectiveness of changes in the short-term rate once it reaches zero, and the necessity of applying fiscal policy to stimulate the economy.

Another feature of the NEC is its rejection of "Ricardian equivalence," the notion that federal budget deficits are always exactly offset by future taxation, suggesting fiscal policy will have no effect on changing private agents' behavior since they are aware of the government's requirement to balance its budget. However, the government can clearly communicate to the public that, when it issues bonds to finance an increase in expenditure, there will be no future offsets to its current liabilities. For example, it can instruct the central bank to purchase the bonds if the public is initially reluctant to do so, thereby signaling that there will be no future tax increases since the debt due to the issued bonds is then cleared. The private holding of bonds thus results in greater expectation of lifetime consumption, creating a "wealth effect" and boosting household spending, rendering important fiscal aid to the economy. However, in the process, increased spending pushes prices up, eroding the value of government liabilities and thus restoring its budget constraint equilibrium.

Some of these results advocated by the NEC are very different from traditional mainstream macroeconomics; still, the author points out that important similarities remain between the two. One such similarity concerns the view that government should practice "sound finance," indicated by the current preference of the U.S. Federal Reserve for fiscal measures based on tax cuts rather than government spending to avoid increasing the government's debt. Another is the absence of any involuntary unemployment in their models—an approach at sharp odds with the Keynesian tradition.

The author also contrasts the NEC's fiscal thinking with two Post Keynesian approaches, both based on the notion that fiscal policies must be judged by their real effects on the economy and not their ex-post budgetary results, since sovereign currency governments differ from private economic agents in that they have the authority to *create* additional funds if required. The first approach advocates securing high levels of aggregate demand through increased investment when private demand is deficient, lowering unemployment until the economy runs into its inflation barrier (i.e., any further reduction in unemployment would increase aggregate demand to the point that prices would begin to rise). Additional policies are then required (e.g., fixing wages and prices) if the noninflationary employment level leaves large numbers of involuntary unemployed. The second approach is based on the guarantee of full employment for all those who are willing and able to work, regardless of its effect on raising aggregate demand. In this approach, increasing aggregate demand is not a necessary condition of full employment.

For the complete text, go to www.levy.org/pubs/wp_539.pdf.

The Effects of International Trade on Gender Inequality: Women Carpet Weavers of Iran

ZAHRA KARIMI

Working Paper No. 540

Globalization has its winners and losers, and often it is the winners who are the objects of analysis; losers have received far less attention. However, the entry into international trade of new producers with low labor costs has had devastating effects on the market share of some labor-intensive industries that typically provide employment for the poor, especially poor women. Iran's carpet industry provides a good illustration of the adverse effects of globalization. In this working paper, Zahra Karimi, University of Mazandaran, Iran, examines this adverse process using data from an informal survey of carpet weavers in and around the city of Kashan, a major center for Iran's handwoven carpet industry.

Within the last three decades, Iran's share of the international carpet trade has dropped from 60 percent to 30 percent. By 2005, China, India, Turkey, and Pakistan collectively held 60 percent of the international market. China, with its huge supply of low-cost labor, has a particularly sharp competitive edge; for example, in 2003, the highest monthly minimum wage for urban workers in China was $42, compared to $150 in Iran. Similarly, the average monthly wage of carpet weavers was $23 in India and $61 in Iran. The declining prices of Persian carpets have led to falling production and exports and to lower wages, changing the composition of the industry. Most middle-income weavers have left the industry, which currently employs the poorest families; in particular, immigrant Afghan women and children with no employment alternatives have increasingly turned to carpet weaving.

The study covers some 68 carpet-weaving households consisting of 80 women and 16 men from Kashan and five of its surrounding towns and villages, with Afghani immigrants constituting 40 percent of the households. The author finds a much younger average age for Afghan weavers compared to Iranian weavers, indicating an important role for child labor in this industry: among women weavers older than 30, 65 percent were Iranian and 25 percent Afghani; among girls younger than 16, 5 percent were Iranian and 40 percent Afghani. Illiteracy among Afghani women weavers was 50 percent, and among Iranian women, 20 percent—an outcome in part due to the limited access to educational possibilities for Afghani immigrants in Iran. In the sample, the average daily wage of a weaver, male or female, was $3; for a construction laborer, it was three times that amount. Nevertheless, the author notes, income from weaving constitutes an important addition to family income, especially if the household head is unemployed or absent.

Finally, Karimi draws attention to the compatibility of carpet weaving, which is carried out in the home, with child care and the performance of domestic tasks. She notes that this type of work results in stretching the length of women's working day. As carpet weaving is generally regarded as a hobby rather than a job, the contribution of women to household income remains invisible and unrecognized. This kind of employment, far from challenging the status quo, reinforces women's subordinate position in the household.

For the complete text, go to www.levy.org/pubs/wp_540.pdf.

The Unpaid Care Work–Paid Work Connection

RANIA ANTONOPOULOS

Working Paper No. 541

There are a large number of conceptual and empirical studies showing the importance of the intersections of paid and unpaid labor to an understanding of gender work differences. In this working paper, Research Scholar Rania Antonopoulos covers this vast ground, critically examines the key concepts, dissects the main issues, and reviews the empirical evidence showing the relevance, and the rich perspective paid/unpaid work interactions bring—not just to gender studies, but also to the economics of work and the measurement of macroeconomic variables. There is an attempt throughout to demonstrate that unpaid work constitutes an integral part of any functioning economy, and as such is linked to economic growth, government policy, worker migration, and many economic development issues.

The author argues that women's unpaid work constitutes a systematic transfer of hidden subsidies to the rest of the economy by imposing a time tax on women throughout their life cycle. This is evident even in the methodology of the U.N. National Account System (SNA), which disregards many, though not all, forms of unpaid work (e.g., washing, cooking, and home care) as "noneconomic." Equally important is unpaid work's impact on a household's ability to access water supplies and health services in order to fill in the gaps in the social and physical infrastructure. One consequence of the unrecognized contribution of unpaid work to the economy is the underestimation of GDP. Unpaid work lowers the overall cost of labor; it allows, at the macro level, for a smaller wage fund and thus a larger pool of profits, effectively transferring a "subsidy" to the business sector from one institution (the family) to another (the market). Moreover, such subsidies are also critical to the provisioning of goods and delivery of services that the public sector should be making available. Therefore, the author argues that the definition of GDP should be expanded to include the value of unpaid work, and "noneconomic" types of unpaid work (e.g., home care) should be included in the SNA accounting guidelines. Unpaid work, she points out, is also important to the understanding of a gender earnings gap. Since women spend much more time on unpaid work than men do, less time is available to them for paid work, despite greater total time spent working; hence, they have lower average earnings than men.

Antonopoulos also examines women's work with respect to globalization and poverty. An important change in the former context is the feminization of international migration through a substantial growth of domestic care labor to alleviate the crisis of in-home care, especially for the elderly, in the developed world. In-home care work has its own particularities; for instance, it is predicated on expectations of care workers being on call 24 hours a day and their children remaining behind in the home country, as domestic work conditions do not permit family members to accompany them. Nonetheless, the author notes that migration can offer women financial independence and decision-making power, as well as benefit their country of origin by contributing to its pool of foreign currency earnings (e.g., remittances provide Morocco with more foreign exchange than tourism, and Sri Lanka, more than tea production). Regarding poverty, the author discusses the notion of time-poverty based on the idea that the working poor must spend longer hours on paid work to secure a poverty-line income. One estimate for the United States gives the reduction in time available for sleeping, personal care, and so on as 26 hours per week. Moreover, estimates for poor urban households in Latin America suggest that poverty would be lowered by 8 percent if women were to receive wages for their unpaid work comparable to those earned by others in the same income group.

Most of the issues raised in this paper cannot be examined without time-use and unpaid-work data, and the author devotes a part of her discussion to methodologies on data collection. Questions discussed include whether to value unpaid work at an appropriate wage rate or by the output it produces, valued at a suitable output price, and the drawbacks of various data-collection methods. She concludes with a number of recommendations, such as employment guarantee policies to alleviate the unpaid work burden, and the provision of retirement benefits and social protection for informal care workers.

For the complete text, go to www.levy.org/pubs/wp_541.pdf.

Keynes's Approach to Full Employment: Aggregate or Targeted Demand?

PAVLINA R. TCHERNEVA

Working Paper No. 542

The current U.S. recession has given a new impetus to the application of fiscal measures to increase consumption expenditure, which is most commonly associated with Keynesian economics. However, there is disagreement among post-Keynesian economists as to the nature and purpose of such measures, with some advocating their application in order to manage aggregate output demand, and others, to maintain full employment. In this working paper, Research Associate Pavlina R. Tcherneva defends the latter interpretation through an examination of John Maynard Keynes's writings.

The author points out that, for Keynes, unemployment was the result of deficient effective demand (underconsumption) rather than deficient aggregate demand (consisting of various types of private and public outputs). During slumps, aggregate demand management policies are effective, but they will have different employment creation effects. For a quick reduction of unemployment in a recession, Keynes advocated large-scale public works expenditure. Tcherneva argues that, even in nonrecessionary conditions, Keynes preferred targeting unemployment directly. This is because he believed that boosting aggregate demand during economic expansions causes prices to rise before full employment is achieved, and that, near full employment, it creates a more unequal distribution of income between capital and labor. Boosting demand indiscriminately means that in sectors responding poorly to such a policy, most of the benefits of the increase accrue to capital rather than to wage earners. In an economy at or near full employment, an increase in aggregate demand brings inflationary pressures. Public works programs can circumvent these problems by targeting regional "distressed areas" and postponing new projects in other areas.

For Britain's full-employment war economy of the 1930s and 1940s, Keynes suggested another method of avoiding the inflationary gap without abandoning employment goals. He proposed taxing high incomes and depositing the amounts in saving accounts that would be made available to depositors for spending *after* the war. By contrast, the author notes that in the approach based on boosting aggregate demand, the goal is economic growth through investment stimulation, a policy that tends to produce inflationary forces, and hence brings on anti-inflationary measures that often prevent the achievement of full employment.

For the complete text, go to www.levy.org/pubs/wp_542.pdf.

Levy Institute News

New Research Scholar

SELCUK EREN has joined the Levy Institute as a research scholar in the Distribution of Income and Wealth program. Eren's fields of specialization are demographic economics and labor economics. His current research interests include the internal and international migration of labor, income and educational mobility in developing countries, and the measure of households' housing wealth, among other topics in applied microeconomics. Formerly a visiting assistant professor of economics at Hamilton College, Eren has taught courses on microeconomics, macroeconomics, health economics, and the economics of immigration. He is a member of the Econometric Society, the American Economic Association, the Society of Labor Economists, the Eastern Economic Association, and the Southern Economic Association. Eren received a B.A. in economics from Istanbul Bilgi University and an M.A. and a Ph.D. in economics from the State University of New York at Stony Brook.

New Research Grants

The Levy Institute has received an underwriting grant from the **Ford Foundation** in support of research to examine financial instability and reregulation in light of the current global financial crisis. The rapidity with which the crisis in the U.S. subprime mortgage market spread to financial markets in all the major financial centers, developed as well as emerging, was a clear representation of the fact that financial institutions are no longer limited to their home markets. This suggests a systemic fault in the current business model of these institutions, and in the regulation and supervision of domestic and global financial markets. The goals of the Institute's project are to determine the policies needed to bring about a rapid resolution of the crisis; to formulate proposals for the reform of mortgage finance and a new regulatory framework for the financial system as a whole; and to assess the implications of domestic reregulation on the global financial system. Another of the project's aims is the formation of a worldwide research network with the common objective of creating a global agenda for reform, leading to a cohesive program of reforms at both the national and the international level. Senior Scholar Jan Kregel, director of the Institute's Monetary Policy and Financial Structure program, will head the Levy research team.

The **Alfred P. Sloan Foundation** has awarded the Institute a generous grant in support of ongoing research within the Levy Institute Measure of Economic Well-Being (LIMEW) program. Standard measures of national income and product indicate that the United States is now ahead of most other Organisation for Economic Co-operation and Development (OECD) countries; however, it is not clear that it would maintain its lead in terms of a comprehensive measure of household income such as the LIMEW. The first stage of the project will be to develop comparable measures of economic well-being in four other OECD countries, all with widely varying political-economic systems: Canada, Germany, France, and the United Kingdom. Comparative analysis of the LIMEW measure among these countries will provide a much broader context for evaluating the United States' performance. The project will be co-directed by Senior Scholars Edward N. Wolff and Ajit Zacharias.

As a complement to its ongoing work on gender and poverty, the **World Bank** has awarded the Levy Institute a grant to study child-gender bias effects in household consumption patterns in Ethiopia. The study, which analyzes data contained in the national Household Income and Consumption Expenditure Survey, applies an innovative approach to the Rothbarth model of the intra-household distribution of income that considers both the influence of household type (nuclear/extended), and a selectivity mechanism of gender bias based on the number of children.

Publications and Presentations

Publications and Presentations by Levy Institute Scholars

FERIDOON KOOHI-KAMALI *Research Associate and Editor*

Presentation: "Child Gender Bias Effects in Ethiopian Consumption Patterns," presented as part of the World Bank's economic and sector work on gender inequalities in Ethiopia, Washington, D.C., June 12.

JAN KREGEL *Senior Scholar*

Publications: "Financial Liberalization and Domestic Policy Space: Theory and Practice with Reference to Latin America," in *Financial Liberalization and Economic Performance in Emerging Countries*, P. Arestis and L. Fernando de Paula, eds., Palgrave Macmillan, 2008; "Keynes, Globalização e Espaço de Política Nacional," in *Economia do Desenvolvimento: Teoria e Politicas Keynesianas*, C. Vidotto and J. Sicsú, eds., Elsevier Editora, 2008.

Presentations: "Policy Coherence in Trade and Finance as Major Systemic Issues," U.N. Regional Economic Commission for Latin America and the Caribbean (ECLAC), Regional Consultation Preparatory to the Follow-up International Conference on Financing for Development, Santo Domingo, Dominican Republic, June 9–13; "ELR as a Component of a National Development Strategy," Graduate Summer Workshop in Post Keynesian Economics, University of Missouri–Kansas City, June 25–28; "Predicting the U.S. Subprime Mortgage Market Crisis," 10th Post Keynesian Economics Conference, University of Missouri–Kansas City, June 30–31; "Reregulation of the US Financial System: Third Time a Charm? Or Strike Three?" Session on Regulatory Reforms—Fixing Last Year's Problems and Avoiding New Ones, Task Force on Financial Markets Regulation, Initiative for Policy Dialogue, Manchester, England, July 1–2; "The Impact of Changes in International Financial Flows on Trade and Production in Developing Countries," seminar on "The Productive and Dynamic Structure of Prices: Macro-micro Effects and Policy Responses," Summer School on Latin American Economies, ECLAC, Santiago, Chile, August 6–7; "Steps in the Development of Post Keynesian Economics," Graduate Lecture Series, Italian Association for the History of Political Economy (StorEP), Brixen (South Tyrol), Italy, August 23–28; "Inflation Targeting and Alternative Approaches to Monetary Policy," Central Bank of the Argentine Republic Money and Banking Seminar, "Financial Turmoil: Its Effects on Developed and Emerging Economies," Buenos Aires, Argentina, September 2; "Combining Full Employment with Inflation Control—Replacing Inflation Targeting," 10th Congress of Economists of Latin America and the Caribbean, Bogota, Colombia, September 4; "Inflation Targeting and Monetary Policy in Emerging Market Economies," National University of Colombia (UNC), Bogota, September 5.

THOMAS MASTERSON *Research Scholar*

Presentations: "Poverty and Unemployment in Recent U.S. History," The Union for Radical Political Economics Summer

Conference, Pine Plains, N.Y., August 15–18; "Long-Term Trends in the Levy Institute Measure of Economic Well-Being (LIMEW), United States, 1959–2000" (with E. Wolff and A. Zacharias), 30th General Conference, International Association for Research in Income and Wealth, Portoroz, Slovenia, August 25.

DIMITRI B. PAPADIMITRIOU *President*

Presentations: Interview regarding regulations limiting investments in banks with Ron Fink, *Financial Week*, June 27; interview regarding the economic programs of the presidential candidates with Bernice Yeung, *Glamour*, July 16; interview regarding the Buffett Plan to reduce the trade deficit with Peter Coy, *BusinessWeek*, July 29; interview regarding Norman Manea for a televised series on distinguished writers by Greek National Television, August 1; interview regarding the current state of economic well-being of the average American compared to the last U.S. recessionary period with Tammi Luhby, *CNNMoney.com*, August 14; interview regarding the Levy Institute Measure of Economic Well-Being (LIMEW) with Louis Uchitelle, *The New York Times*, August 18; "The U.S. Economy: The Road Ahead," Lifetime Learning Institute, Bard College, Annandale-on-Hudson, N.Y., September 9; "Contemporary Economic Issues," Center for Lifetime Studies, Marist College, Poughkeepsie, N.Y., October 7.

EDWARD N. WOLFF *Senior Scholar*

Publication: Review of *Unequal Chances: Family Background and Economic Success*, S. Bowles, H. Gintis, and M. Osborne Groves, eds., in *Journal of Socio-Economics*, Vol. 37, no. 3.

Presentations: "The Middle-Class Squeeze," conference on "The Americas Plural: Regional and Comparative Perspectives," Institute for the Study of the Americas, London, England, June 20; "Long-Term Trends in the Levy Institute Measure of Economic Well-Being (LIMEW), United States, 1959–2000" (with T. Masterson and A. Zacharias), 30th General Conference, International Association for Research in Income and Wealth, Portoroz, Slovenia, August 25.

AJIT ZACHARIAS *Senior Scholar*

Presentation: "Long-Term Trends in the Levy Institute Measure of Economic Well-Being (LIMEW), United States, 1959–2000" (with T. Masterson and E. Wolff), 30th General Conference, International Association for Research in Income and Wealth, Portoroz, Slovenia, August 25.

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WYNNE GODLEY, DIMITRI B. PAPADIMITRIOU, and GENNARO ZEZZA
April 2007

Can Global Imbalances Continue? Policies for the U.S. Economy
DIMITRI B. PAPADIMITRIOU, GENNARO ZEZZA, and GREG HANNSGEN
November 2006

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L. RANDALL WRAY
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Systemic Risk and the Crisis in the U.S. Subprime Mortgage Market
JAN KREGEL
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CHARLES J. WHALEN
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