

“Is the Economy Returning to That 70s Show?”

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Remember the 1970s economy? Gas prices on the rise, inflation, high unemployment, and a flat stock market. Recent economic news – rising unemployment, a struggling stock market, food and gas prices heading upward, housing and mortgage markets woes, and worries of inflation – make things sound much too close for comfort to the economic stagnation of much the 1970s. Fear not, however . . . at least not yet. Things aren't nearly as bad now as they were then. During the 70s, inflation averaged 7.1% per year. The unemployment rate averaged over 6%, with spells where it was over 7% and 8%. Our current 5.5% unemployment rate and 4.2% annual inflation rate don't look too bad by comparison. Still, things have been better and we don't want to return to those days. So it's sensible to ask why we have the present troubles? And what can be done about it?

My view is that much of the present economic slowdown is due to a great deal of uncertainty. There's a lot of out there these days . . . about how high gas and food prices will go, where housing prices will settle, and with credit markets. People don't like uncertainty and it makes them (and the firms and organizations they represent) hesitant to commit to long-term investments and long-term purchases like cars, homes, and other big ticket items. Collectively, this leads to a slowing economy.

To top it off, we have a Congress held in all-time low esteem. Handing such a Congress the above slate of economic problems does not buoy confidence about the future state of affairs, adding to the uncertainty and economic slowdown.

So while the above described scenario has, at least in part, led to the present troubles, what can be done about it? Before we go any further, note that I think that we're asking the wrong question. Perhaps “we” have done too much already and should be asking, “What shouldn't we do?” After all, some of the present problems are the result of government policies doing the wrong things. For example, U.S. government policy inducing more use of biofuels to combat CO₂ emissions has failed to reduce net carbon emissions, yet has led to higher food prices and plays a part in the higher gas prices. “Affordable housing” policies pushed by various government agencies has turned into the subprime mortgage mess, now conveniently relabeled as “predatory lending,” apparently to shift blame to the amorphous evil corporations. The increased liquidity and easy money provided by the Federal Reserve to patch up the credit market mess in the aftermath of the subprime crisis has fueled fears of inflation.

So it's clear that government micromanagement of our economy – with the ensuing patchwork repairs of policies gone awry and blame game – does not work. This shouldn't come as a surprise. The U.S. government is a very large, bureaucratic

organization with over 4 million employees and a budget of around \$3 trillion. It is attempting to influence the U.S. economy, with its 146 million workers that create about \$14 trillion of good and services. Nothing much happens very fast and as for fine details . . . forget about it! No matter how much management consultants want to think otherwise, elephants cannot dance.

Where does this leave us? With those old, standby admonitions about government macroeconomic policy. Don't try to micromanage. Focus on the big picture. Maintain a stable policy environment: sound money, low inflation, modest and sensible regulation, and low taxes to encourage and reward hard work and productivity. This surely will not eliminate all the uncertainty out there in the world . . . stuff happens beyond our control. But investors and consumers need reasonably reliable government policy to provide the critical element of stability in a world that often changes.

Seems like pretty boring stuff. Sadly, it doesn't seem to make for exciting stump speeches in this season of election year politics. It doesn't provide any quick fix, silver bullets, or scapegoats to pick on. But, given a little time . . . it works! I say that's what we hold out for.