BOOK REVIEWS

Out of Work: Unemployment and Government in Twentieth-Century America
Richard K. Vedder and Lowell E. Gallaway
Oakland, Calif.: The Independent Institute, 1993, 336 pp.

This is an impressive and ambitious work that debunks powerful myths about unemployment and calls into question conventional wisdom about how labor markets operate. In 15 chapters (plus a technical appendix and an extensive bibliography), the authors apply economic theory and empirical techniques to explain fluctuations in unemployment during the entire 20th century. They convincingly show that unemployment can be explained by movements in real wage rates after taking into account the quality and productivity of labor. Put simply, the laws of supply and demand remain valid for labor markets.

In the first three chapters, the authors develop and explain their model of unemployment, which is so disarmingly simple that its ability to predict the unemployment rate over even a short period of time would be suspect. Yet, amazingly, their model is incredibly accurate in predicting unemployment rates over the entire nine decades from 1900 to 1990 (see Figure 3.1, p. 31). During this protracted period, the labor market was buffeted by financial panics, two world wars, the Great Depression, and major technological, political, and social changes both at home and abroad.

Chapters 4 through 12 contain insightful and interesting discussions of these significant periods in U.S. economic history. Of note is how Vedder and Gallaway trace the formation of the conventional wisdom among economists and members of the business community in some of these major economic upheavals. The authors' examination of the intellectual history of state intervention reveals that economists are influenced by "group think" and self-interest.

Vedder and Gallaway are accomplished writers who transform material that could be esoteric and dull into fascinating reading, even for professional economists. Sadly, all too many recently trained economists have an appalling lack of historical perspective because their "education" has emphasized statistical and mathematical legerdemain rather than the lessons of history, which are often much more difficult to analyze and interpret. Learning from the past is decidedly out of fashion. Both professionals and interested laypersons will gain invaluable insights from *Out of Work*—a book that is urgently needed, long overdue, and cogently written.

Policymakers are well advised to take to heart the message Vedder and Gallaway convey in the last three—and most important—chapters, which investigate the effects of government involvement in labor markets. One sentence encapsulates their findings: "Government actions, as expressed in a wide range of public-policy actions, generally have contributed to the presence of higher levels of unemployment, rather than lower" (p. 264). Since the 1930s, virtually every aspect of the employer-employee relationship has been regulated by federal, state, and local government mandates. Minimum wages, mandated benefits, regulation of the work hours, unemployment compensation, and the promotion of collective bargaining are some of the myriad ways in which politicians have meddled in the labor market over the years.

Who bears most of the costs of this state intervention? In chapter 14, the authors persuasively argue that unemployment differentials have increased markedly during the last three decades for females, minorities, and teenagers—precisely the groups that public policy supposedly is designed to assist. The lesson is simple: Good intentions do not guarantee good public-policy outcomes. Markets respond in predictable ways to political meddling and, always and everywhere, those on the bottom of the economic ladder bear a disproportionate share of the burden.

For at least the last half-century, the oft-repeated mantra of politicians of every stripe in the United States and elsewhere in the world has been "Jobs!" The record high levels of unemployment during the Great Depression left serious, and as yet unhealed, scars on the psyche of Americans, and the Keynesian aftermath, which dictated that government "do" something to relieve unemployment and the associated dislocations, forever changed the economic landscape. Since the 1960s, the government constantly has been involved in the labor market, purportedly to create new jobs or to train potential employees so that their skills were better suited to existing employment opportunities. Over the decades, an alphabet soup of programs and agencies have spent hundreds of billions of taxpayers' dollars, most of which have been squandered on ill-fated and scandal-ridden schemes, such as CETA (Comprehensive Employment and Training Act).

On a common-sense level (and as indicated by the Vedder-Gallaway model), it is patently evident that government cannot possibly "create" jobs; if it could, unemployment and the often-associated ills of poverty would have disappeared long ago. When economic decisionmaking moves from markets to the political arena, political clout prevails—jobs are created for powerful union workers at the expense of other, less fortunate workers. Jobs created by government programs in one sector of the economy inevitably reduce employment opportunities elsewhere; employment is merely shifted around to favor certain groups. Politicians and voters who would never presume that the laws of physical nature could be repealed by legislative fiat are evidently too persuaded by self-interest—or in the case of voters, too gullible—when it comes to attempting to repeal the laws of economics in the labor markets.

Common sense, however, is no longer in vogue among either economists or (not surprisingly) politicians. Thus, this work performs the very significant function of showing both empirically and theoretically that the basic laws of supply and demand still operate in the labor markets, despite the efforts of politicians to repeal those laws.

Let us fervently hope that *Out of Work* is widely read and that its powerful message is heeded: Government has done far more harm than good by meddling in labor markets and has wasted untold taxpayers' money in the process.

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Federalism and Free Trade
Jean-Luc Migué
London: Institute of Economic Affairs, 1993, 77 pp.

When discussing politics and free trade, economists commonly argue that we must control the special-interest tendencies of government to fully secure the advantages of international trade. While recognizing the importance of this argument, Jean-Luc Migué persuasively points out that the opposite is also true: free trade is needed if we are to secure the advantages of controlling the special-interest tendencies of government. Migué's position is clearly stated in his introduction:

> Provided there is free inward and outward movement of factors and goods, a national government has little power to engage in redistributive policies. Stated conversely, it is the ability to restrict international movements of factors and goods which enables governments to engage in costly redistribution policies.

Migué's fundamental insight is a simple but powerful one: "free trade equals federalism." With free trade, governments are thrown into competition with one another for the patronage of consumers who can move their resources (tax bases) to those political jurisdictions that provide the best value for their tax dollars. The advantage that organized interests have over the general taxpaying public at communicating through the political process becomes less important as exit (as opposed to voice) options become more important.

Some have argued that attempts to restrict government power are likely to be futile at best and inefficient at worst. If, for example, a spending limit is imposed on government, it will employ some other means of controlling resources (e.g., regulation). And this alternative will probably be a less efficient way of directing resources than taxing and spending, with the result being worse than before. That argument is surely overstated for reasons Marilyn Flowers (1992) has put forth. But it is true that most attempts to control government with one policy initiative (e.g., spending limits) weaken the ability to control government