DEMAND-LED GROWTH UNDER POLITICAL CONSTRAINTS:
A LONG-RUN MODEL OF CONFLICT INFLATION

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Demand and Growth Regimes: Expanding the Debate

INTRODUCTION

- Income distribution is inherently conflictual
- The tension generated by this conflict influences the price dynamics, revealing the contentious nature of inflation
- The disciplinary role of unemployment has long been acknowledged in economic theory
- The distributive effect of unemployment at the heart of conflict inflation theories

low unemployment, leading to increases in nominal wages given prices, and increases in prices given nominal wages, and so on **Who is the author?**

- Development on previous work for inflation in open economy (Morlin, 2023).

SPOILER ALERT!

We find:

(a) an inverse relation between the unemployment rate and inflation, in line with the traditional, old-school (i.e., non-accelerationist) Phillips curve

(b) an inverse relation between the growth rate of autonomous demand and the unemployment rate; and, for this reason

(c) a direct relation between the growth rate of autonomous demand and the wage share

THE POLITICAL ECONOMY OF AUTONOMOUS DEMAND

Sraffian Supermultiplier: exogenous growth? (Blecker and Setterfield, 2019)

The ultimate causes of growth in the supermultiplier are not found in the intricacies of the economic modeling but in the political and social determinants of the autonomous demand components

Growth Theory and the Growth Model Perspective: Insights from the Supermultiplier (Morlin, Passos, and Pariboni, 2022)

- If the proximate causes of growth are to be found in the dynamics of autonomous demand, the ultimate causes can only be discovered by looking at the political and social determinants - and implications - of autonomous demand

GROWTH, DISTRIBUTION AND CONFLICT

- Sraffian and Neo-Kaleckian growth models: **exogenous distribution.**
- Distribution is shaped by conflict among social classes
- Unemployment affects workers' relative bargaining power
- Conflict inflation theory includes the unemployment rate as a determinant of workers bargaining power (Rowthorn, 1977)
- Assumption in line with the empirical regularity found in the original, old-school Phillips curve.

GROWTH, DISTRIBUTION AND CONFLICT (2)

- some issues emerge when moving to the long run…

if we were to suppose that the real-wage target of workers depends on the level of unemployment [. . .] complex interactions with limit cycles and the like would arise

the change in the rate of unemployment is roughly equal to the discrepancy between the natural rate of growth and the actual growth rate of output, so that the rate of unemployment keeps changing as long as these two rates are not equal to each other (Lavoie, 2022).

(Lavoie, 2022)

- **unemployment rate** only has a **temporary effect on distribution,** against the empirical evidence.
- What happens to the Phillips curve?
- Same issue in Nah and Lavoie (2019). But not in Serrano (2019).

ANALYTICAL SOLUTIONS

Autonomous demand-led growth.

Distribution has no persistent effect on the growth rate in the long run (Freitas and Serrano, 2015).

Stabilizing role of autonomous demand, when distribution is endogenous (Nah and Lavoie, 2019).

Endogenous adjustment in the labor market (Fazzari et al., 2020).

THE GROWTH PROCESS

Supermultiplier with endogenous distribution.

$$Y_t = \sigma_t Z_t \tag{1}$$

$$\sigma_t = \frac{1}{1 - c_t - h_t} \tag{2}$$

$$c_t = \phi \omega_t \tag{3}$$

$$\dot{h} = h_t \gamma (\mu_t - \mu_n) \tag{4}$$

In equilibrium

$$g^Y = g^Z$$

CONFLICT INFLATION AND ENDOGENOUS WORKERS' CLAIMS

- Nominal wages growth:

$$\widehat{w_t} = \alpha_1 \pi_t + \alpha_2(\omega_W - \omega_t) \quad (5)$$

- 'Price-setting' equation

$$\pi_t = \lambda_1 \widehat{w}_t + \lambda_2(\omega_t - \omega_K) \quad (6)$$

- Endogenous workers' claims

$$\omega_W = \theta_0 - \theta_1 u_t \quad (7)$$

- Labor supply growth

$$g^N = \beta_0 + \beta_1 u_t \quad (8)$$

(what about labor demand?)

THE MODEL

The dynamic system is constituted by four differential equations. The endogenous variables are:

- the propensity to invest
- capacity utilization
- the unemployment rate
- the wage share

The inflation rate is fully determined once we have found the equilibrium value for the other four variables

IN A NUTSHELL

Growth and distribution become interconnected processes linked through the unemployment rate.

The pace of growth influences the unemployment rate, which in turn affects distribution by weakening or enhancing workers' bargaining power.

THE EQUILIBRIUM

$$\upsilon^* = \frac{\beta_0 - \mathbf{g^Z}}{\beta_1} \qquad (9)$$

$$\omega^* = \frac{\alpha_2(1-\lambda_1)(\theta_0 - \theta_1 \mathbf{u^*}) + \lambda_2(1-\alpha_1)\omega_K}{(1-\alpha_1)\lambda_2 + (1-\lambda_1)\alpha_2} \qquad (10)$$

$$\pi^* = \frac{\alpha_2\lambda_2(\theta_0 - \theta_1 u^* - \mathbf{\omega_K})}{(1-\mathbf{\alpha_1})\lambda_2 + (1-\mathbf{\lambda_1})\alpha_2} \qquad (11)$$

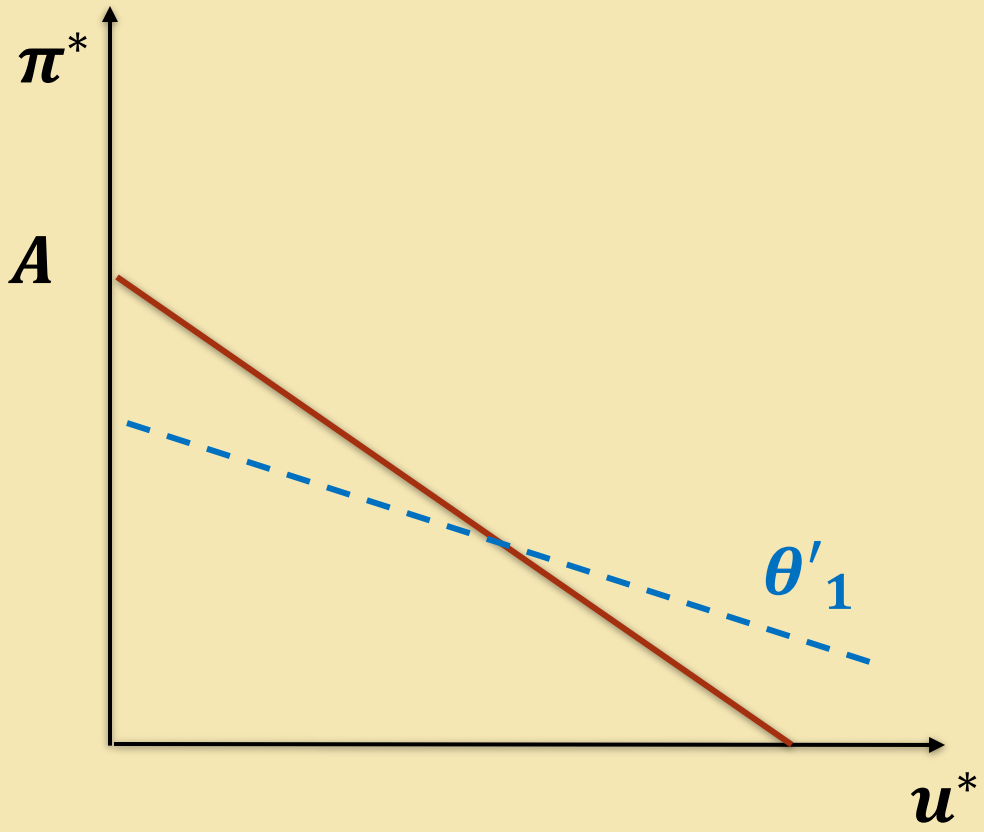
$$h* = v/\mu n\ (gZ + \delta)$$

THE PHILLIPS CURVE

$\pi^* = A - Bu^*$

$$A = \frac{\alpha_2\lambda_2(\theta_0 - \omega_K)}{(1-\alpha_1)\lambda_2 + (1-\lambda_1)\alpha_2}$$

$$B = \frac{\theta_1}{(1-\alpha_1)\lambda_2 + (1-\lambda_1)\alpha_2}$$



$A > 0$ whenever $\boldsymbol{\theta_0 - \omega_K > 0}$.

$\boldsymbol{\theta_0}$ corresponds to workers' target in the case of full employment ($u = 0$).

$\boldsymbol{\theta_1}$ determines the slope of the Phillips curve ($\theta_1 = 0$ means horizontal Ph. curve).

$\omega_W = \theta_0 - \boldsymbol{\theta_1} u_t$

GROWTH AND THE WAGE SHARE

$$\omega^* = \frac{\beta_1\phi_1 + \phi_2(g^z - \beta_0)}{\beta_1\phi_3} \qquad (12)$$

$\varphi_1 = \alpha_2(1 - \lambda_1)\theta_0 + \lambda_2(1 - \alpha_2)\omega_K$

$\varphi_2 = \alpha_2(1 - \lambda_1)\theta_1$

$\varphi_3 = (1 - \alpha_1)\lambda_2 + (1 - \lambda_1)\alpha_2$

$$\frac{d\omega*}{d\beta_0} < 0; \frac{d\omega*}{d\beta_1} < 0; \mathbf{\frac{d\omega*}{dg^z} > 0}$$

POLITICAL CONSTRAINTS TO GROWTH

- Unemployment sets a minimum growth trend for autonomous demand.
- Fazzari, Ferri, Greenberg, and Variato (2013): the growth of autonomous expenditures can provide a floor for unemployment rate.
- Distributive concerns and macro policy can set an upper constraint to growth.
- Serrano, Summa, and Freitas (2022): policy constraints coming from conflict inflation to dampen workers bargaining power even if there is no sign of a real scarcity.

POLITICAL CONSTRAINTS TO GROWTH (2)

- A higher rate of growth of the autonomous components of demand leads to a higher wage share
- Government and Central Banks have a powerful influence over the dynamics of autonomous demand growth, through fiscal and monetary policy
  - Kalecki: "the doctrine (or the myth) of sound finance"
- The business opposition to full employment policies can lead to a long-term "political trend" characterized by stagnation policies, with governments and central banks prioritizing "inflation and the public debt" over employment (Steindl, 1979).
- Weak labor relaxes this constraint.

TO SUM UP

- *The domain of macroeconomic policy is yet another dimension of the social conflict over the division of the social product between classes.*
- The investigation of the ultimate causes of growth does not belong exclusively to the sphere of economic modeling intricacies. Rather, they have to be explored by looking also at the political and social determinants, and implications, of growth.
- Resilience of austerity policies in spite of their (apparent) failure in delivering results (Blyth, 2013; Mattei, 2022).
- The more organized and combative the labor movement is, the more passionate the capitalists will be about tight monetary policy, fiscal discipline, and "sound finance"