

## DIRECT JOB CREATION: WHERE DO WE GO FROM HERE?

*There has been recent dramatic growth in federal programs that promote directly the creation of jobs, but this expansion has not consistently been accompanied by a clear understanding of a number of fundamental issues concerning their design and effects. To help fill this gap the Institute for Research on Poverty and the Brookings Institution jointly sponsored a conference on direct job creation in 1977 (see FOCUS 1, no. 3, Spring 1977). The following discussion of the policy issues at stake is taken from Irwin Garfinkel and John Palmer's overview chapter for a new book that emanates from that conference, Creating Jobs: Public Employment Programs and Wage Subsidies (copyright © 1978 by the Brookings Institution).<sup>2</sup>*

During the mid-1970s both unemployment and inflation in the United States set post-World War II record highs. Even after several years of vigorous recovery from the 1974-75 recession both are well in excess of comfortable rates. And many economists maintain that the persistence of high levels of structural unemployment may make it difficult to lower unemployment much below 6% through conventional macroeconomic policies without reaccelerating inflation. (Although unemployment rates are generally lower in Western Europe, a similar problem exists there.) For these reasons, selective federal policies to promote directly the creation of jobs are increasingly seen as desirable means of promoting two related objectives—reaching and sustaining low levels of unemployment without excessive inflationary pressure, and ensuring minimally adequate incomes for families with workers. These approaches have two distinctive characteristics: Federal funds are granted to public or private employers conditioned on their performance in providing employment; and restrictions are placed on eligibility and, possibly, other aspects of employment.

Such job creation programs can take many forms. Until recently they had been used intensively in the United States only during the Great Depression, but with the high unemployment rates of the 1970s, job creation programs once again are being used. The two predominant types are state and locally administered public service employment programs and employment tax credits for private employers.

Public service employment in the United States has evolved from very limited use in the late 1960s for particular groups of disadvantaged workers into several major programs with a mix of countercyclical and structural objectives. The federal budget for fiscal year 1979 provides 625,000 public service jobs for previously unemployed workers under Titles 2 and 6 of the Comprehensive Employment and Training Act (CETA) at a cost of about \$6 billion. The programs are administered by designated agents (local prime sponsors) of state and local governments. Almost \$1 billion more is being spent on public employment projects for unemployed youth, and smaller amounts on other special groups. Other large expenditures on public employment are being considered by Congress in conjunction with welfare reform.

Employment tax credits have only recently come into use in the United States. They are simply employer wage subsidies administered through the federal income tax system. The work incentive (WIN) tax credit, first passed in 1971 and then expanded in 1975, reimburses private employers for a flat percentage of the first year's wages they pay to any recipient of Aid to Families with Dependent Children (AFDC). It has operated only on a very small scale. A second, temporary measure—the New Jobs Tax Credit—was passed as part of the economic stimulus package in 1977. At a cost of over \$2 billion a year, it provided a tax credit to private employers for wages paid in excess of a base related to their prior year's wage bill. It was replaced in January 1979 by the Targeted Jobs Credit program, designed to increase hiring of certain categories of hard-to-employ workers.

What uses ought to be made of policies for creating jobs in the future and how should they be designed? Since value judgments often are crucial in determining the desirability of job creating relative to alternative policies, conclusions ought to be approached cautiously. Nevertheless, the already extensive use of public employment and wage subsidies, and the strong and immediate interest among policy-makers in improving and possibly expanding their use, make it imperative that these questions be addressed.

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John L. Palmer, Editor

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## Direct job creation

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No attempt was made at the conference to arrive at majority or consensus judgments; thus, while the policy conclusions set forth here are informed by the conference discussion and generally supported by the conference papers, they are the authors' and are not necessarily attributable to conference participants at large.

The primary use of jobs programs in the United States has been for countercyclical purposes during periods of recession. At such times they are competitors of other fiscal policy measures, such as general tax cuts and expenditure increases, and their consequences should therefore be assessed in comparison with these alternatives. The other principal use of jobs programs has been to reduce structural unemployment. This refers to policies aimed at (1) aiding particular groups of workers or potential workers who suffer from relatively high rates of unemployment and underemployment even during times of relatively full employment, or (2) reducing overall unemployment in a way that will have a smaller inflationary impact than will conventional macroeconomic policies.

## Countercyclical Policy

During periods of high unemployment, any expansionary fiscal policy is likely to yield strong economic benefits on balance. However, although they have some merits, the case for the use of public employment programs or wage subsidies for countercyclical purposes in preference to other macroeconomic policies is not strong.

The primary advantage of public employment programs is the potential for targeting the jobs directly created by the additional stimulus. This, in turn, could help disadvantaged workers or regions to participate more fully in the economic recovery and may exert less inflationary pressure than alternative fiscal stimuli of comparable magnitude. Public employment programs may also have a greater employment impact per temporary dollar increase in the federal deficit.

On the negative side, the timing and efficiency of public employment programs intended for countercyclical purposes appear to be less favorable than alternative fiscal stimuli that emphasize expansion of the private and regular public sectors. Rapid implementation is possible, but may come at some expense to targeting on the disadvantaged and avoiding fiscal substitution. (It is more difficult to design and implement special projects than to expand existing employment opportunities.) And the timely phasing down of countercyclical public employment programs is politically difficult. Similarly, such programs appear unlikely to provide additional output that would be valued as highly by society as the output that would result from an expansion of the regular public and private sectors of the economy, since the former is subjected to neither regular market nor political tests. And while in theory public employment might have a training effect that could raise the postprogram productivity of the working population beyond what an equivalent expansion of the regular sectors of the economy would, there is no evidence that this would happen—nor should it be expected of temporary

programs that must be rapidly implemented and subsequently phased out.

The evidence suggests that wage subsidies or tax credits could have as large an employment effect as public employment programs per dollar increase in the deficit. They also can be structured to favor low-skilled workers. They may be more economically efficient than public employment programs because the jobs directly created are in regular sectors of the economy, and the output therefore subject to conventional tests of consumer demand. And, since the jobs are regular ones, the problem of transition from specially created public jobs is avoided. Finally, general wage subsidies have the advantages of directly lowering labor costs to private employers (which should lead to lower product prices and lower inflation), of offering flexibility in the degree of the subsidy, and (perhaps) of being easier to phase out.

## Structural Policy

The usefulness of direct job creating policies for structural rather than countercyclical purposes appears more promising. However, limits in both the current state of knowledge and expertise regarding their use and their likely ultimate potential dictate that we proceed deliberately.

If certain conditions are met, direct job creating policies can permit continued expansion of employment at relatively full employment levels with less long-run inflationary pressure than conventional fiscal policies. Appropriate targeting is necessary but not sufficient. In addition, the disproportionately high unemployment rates among certain groups of workers must be due to particular kinds of rigidities in wage determination and wage adjustment processes. Since these are currently issues of considerable uncertainty and dispute, the extent to which the inflationary consequences of direct job creating policies are superior to those of other expansionary policies is a speculative matter. Clearly, the more they are restricted to workers with the poorest regular employment opportunities, and the lower the wage paid in public employment programs, the better their prospects for minimizing inflationary pressures. But even so, higher employment among workers in the target group may be partially at the expense of higher unemployment among other workers.

Public employment and employer subsidy programs also can help to ensure minimally adequate incomes to families with workers. The targeting requirements for this purpose are likely to overlap considerably with those for the objective of increasing employment with minimal inflationary pressure. When the primary objective is distributional, a jobs program that has the disadvantage of reducing gross national product over the long run may nevertheless be desirable, if its economic efficiency compares favorably with direct cash assistance programs or if a high premium is placed on providing assistance through jobs rather than cash. In fact, if taxpayers are willing to pay more to provide aid to those expected to work through subsidized jobs rather than direct cash assistance, and the former alternative is more costly, it is almost certain that some combination of cash and jobs is optimal.

Although structurally oriented job creating programs do not have to promote economic efficiency to be desirable, the degree to which they do should influence the extent of their use, and the maximization of their economic efficiency should be a principal policy objective. Little is known about the economic efficiency of narrowly targeted public employment and wage subsidy programs, largely because experience with them has been extremely limited and not subject to rigorous scrutiny. What is known suggests that they have potential, but that it is difficult to make them efficient.

In the case of wage subsidies, the main problem is to induce employers to hire and train workers with characteristics other than those of their usual employees. Once this is successfully accomplished, one can be reasonably hopeful about the outcome since the output will be meeting the market test and the workers will have learned a salable skill while in the regular labor market. In the case of public employment programs, it should be easier to provide jobs for the desired target groups. However, deciding what to produce and how to produce and market the output is difficult, as is helping workers make the transition to regular employment. Furthermore, the incentive structure faced by managers of public employment programs is unlikely to lead them to place much weight on achieving economic efficiency.

For these reasons, policymakers should proceed cautiously. The inherent limitations of job creating programs probably will preclude their ever becoming a panacea for structural unemployment, but they may be able to play a constructive role for particular groups of workers.

## Program Design

The design and operational requirements of countercyclically and structurally oriented job creating policies are quite different and, ideally, ought to be pursued through different program structures. Trying to accomplish the two types of objectives within a common framework will compromise both.

Table 1 lists the desirable design features of public employment programs. If such programs are going to be administered through state and local governments for countercyclical purposes, their eligibility criteria ought to be fairly broad, and state and local governments should not be restricted to special projects. Even though these conditions encourage fiscal substitution, they are important to rapid implementation and the provision of highly valued output. (Since the program is to be temporary, the degree of fiscal substitution will be limited.) The wage rate is not crucial from the point of view of displacing regular employment because of the assumed widespread cyclical unemployment.

In contrast, for structural programs, quite restrictive eligibility criteria are appropriate, as are low wage rates, in order to ensure participation of workers with lower opportunity costs. These also may be favored on distributional grounds, since they reserve the jobs for the most needy and, within a fixed appropriation level, reach the greatest number of workers. Emphasis on special projects will be

<i>Countercyclical criteria</i>	<i>Structural criteria</i>
Temporary funding with level varying inversely and rapidly with aggregate unemployment rate	Permanent funding
Funds allocated primarily to those local areas suffering from higher unemployment	Funds allocated to all local areas
Broad targeting on the unemployed	Narrow targeting on those with poor employment prospects even in a high employment economy
Emphasis on highly valued output	Emphasis on relevance of work experience to regular employment opportunities and transitional assistance
Employment of a type that can be promptly and effectively phased in and out	Employment in carefully designed, long-term projects
Wage rates that can be as high as prevailing rates	Wage rates close to minimum wage

**Source:** John L. Palmer (ed.), *Creating Jobs: Public Employment and Wage Subsidies* (Washington, D.C.: Brookings Institution, 1978).

necessary since the nature of the work generally will have to be tailored to meet the characteristics and needs of particular target groups and because the relatively permanent funding and assumed high employment rate make fiscal substitution and other forms of displacement more severe problems.

Although wages at or very near the minimum are desirable on some grounds in structural public employment programs, they can present difficulties. In many locales such wages are well below those of the lowest-paid jobs in the regular public sector. Consequently, the program jobs could either become dead ends with no relevance to regular employment or undermine standards in the public sector. In any event, the creation of a very large number of public employment jobs at a subsidized minimum wage raises the spectre of a stigmatized second class work force being permanently "warehoused" in the public sector.

Both public employment programs and wage subsidies have significant advantages and disadvantages for dealing with structural unemployment. Until more is learned about them, the scale on which they eventually might operate effectively is highly uncertain. There appears to be no general reason to greatly prefer one approach over the other (although one may have more potential effectiveness than the other for particular target groups). Current policies in the United States heavily favor public employment programs. A more balanced approach, with wage subsidies applicable to regular public as well as private employment, is likely to be more fruitful.

<sup>1</sup>Irwin Garfinkel is Director of the Institute for Research on Poverty and Professor of Social Work at the University of Wisconsin; John Palmer is a Senior Fellow in the Economic Studies Program, Brookings Institution.

<sup>2</sup>This is a shortened and edited version of that paper.