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PolicyPennings by Daryll E. Ray & Harwood D. Schaffer

Goldilocks role of federal economic policy

The nature of the agricultural policy that an individual or organization supports, to a large extent, depends upon the role one thinks the government ought to play in the economy, though when it comes to the cost of farm programs there is often an inverse relationship between the minimal role some want the government to play and the eventual cost of the programs they advocate. We will get to the reason for that in next week's column.

In this column, we want to pick up on our discussion of last week where we talked about the importance of the role governments have historically played in the implementation of agricultural policy. Today we are going to examine the various options for how extensively the government should be involved in economic policy and, by extension, much of agricultural policy.

For the major civilizations over the stretch of history, governments have had an overarching role in economic policy and a great deal of that policy involved agriculture in one form or another. Individual ownership of land was usually restricted to the government itself, a priestly class, or a few selected nobles, while the mass of humanity worked the land and had little control over their lives. In the twentieth century, communist governments, under the guise of a transitional period of the dictatorship of the proletariat, operated command and control economies with little economic freedom for individuals.

During the Enlightenment, in reaction to the power of royalty and the church, philosophers began to focus on the concept of individual liberty and limited government, turning the relationship between the government and the individual upside down. Instead of the individual living at the mercy of the government and the powerful, these philosophers argued that government derived its powers from the individuals. To secure this liberty from loss, they argued for a limited government.

Today we hear that philosophy in the calls for a small government that focuses on national defense, the protection of individual liberty, and the protection of property rights, positions that are advocated by libertarians and neo-liberal economists. These groups are skeptical of too large a role for the government in the economy and of governmental regulations, preferring the discipline of the marketplace to provide guidance for economic actors. We also see an extreme example of a minimal role for government in the failed states of the world where there is often no government at all, only competing fiefdoms and little economic activity at all.

In between, we have what might be called the Goldilocks role of government in economic policy: not too hot (a large role for government), and not too cold (a minimal role for government), but just right (for the circumstances). The level of government involvement in economic matters may differ over time for a given industry as well as from one industry to another. In each case, the appropriate role of government is dependent upon the economic characteristics of the economic sector and/or the stage of development of the sector.

One twentieth century advocate of this Goldilocks role for government in the economy was British economist John Maynard Keynes. In addition to a role in national defense, the protection of property, and public goods like air, water, infrastructure, and parks, he argued for a role for the government in the event of an economic collapse.

During the Great Depression as well as periodic recessions, consumer demand falls and the economy begins to contract. In those situations, Keynes argued that government has an obligation to provide demand to keep the economy from collapsing further so as to stimulate the economy into recovery. This idea provided the theoretical underpinnings of various policies of the US New Deal that put people back to work in infrastructure programs like the Civilian Conservation Corps as well as public support for agriculture.

Critics often argue against deficit government spending, even during an economic decline, using the example of a household where expenditures are limited by the income received by the family. In making this argument, they fail to distinguish between microeconomic theory; which describes the economic behavior of individuals, households, and business firms; and macroeconomic theory, which describes the behavior of economy-wide phenomena involving multiple economic firms, sectors, and governments.

It is true that if households regularly spend more than they earn they eventually fall into bankruptcy and default on their debts. Deficit spending by governments during an economic slowdown provides the demand that is no longer being provided by individuals. The deficit spending is particularly effective if it is used to invest in infrastructure—items that have a long-term benefit to the public like schools, transportation, and public items like public sewer and water systems. It is also important to provide support for families who are being hurt by the economic decline. To the extent that a significant level of infrastructure investment is put into place, the level of individual support needed is reduced.

The magic of macroeconomics is that the stimulus provided by deficit spending stimulates long-term growth, reducing government debt as a percent of Gross Domestic Product, even when the debt grows in absolute terms. Goldilocks policies also provide a backstop for families that fall below certain humanitarian norms, especially when it comes to food, water, health, and shelter.

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Our examination of economic and agricultural data and the behavior of the agricultural economy over our lifetimes suggests to us that the Goldilocks role is a compelling choice when considering the interventionist range of agricultural policies.

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