

**THE CLASS CONTENT OF PREFERENCES TOWARDS ANTI-INFLATION  
AND ANTI-UNEMPLOYMENT POLICIES**

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This paper assesses class based preferences towards anti-inflationary and anti-unemployment policy. Using a consistent cross-country social survey, I find that the working class broadly defined, and those with lower occupational skill and status are more likely to prioritize combating unemployment rather than inflation. The result is robust to the inclusion of several plausible controls. The idea that the working class is less 'relatively inflation averse' is consistent with earlier predictions coming from large body of political economy research in the 1970s. The finding that inflation and unemployment aversion have a distinct class character has implications for current debates on the implications of macroeconomic policies such as inflation targeting.

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## **Section (I): Introduction**

*From one important point of view, indeed, the avoidance of inflation and the maintenance of full employment can be most usefully regarded as conflicting class interests of the bourgeoisie and the proletariat respectively, the conflict being resolvable only by the test of relative political power in the society.*

Harry Johnson (Johnson, 1968, p 96)

Among the casualties of the advent of the rational expectations revolution in the 1970s was a rich vein of political economy which analyzed the macroeconomic dynamics of unemployment and inflation as deriving from distributive struggles between capitalists and workers (Boddy and Crotty 1975, Rosenberg and Weisskopf 1980, Rowthorn 1977, Bach and Stephenson 1974 Hibbs 1977). This approach often made explicit the class conflict innate in Keynesian accounts of the Phillips curve trade-off and in considerations of the natural rate of unemployment<sup>2</sup>. While the details of these studies varied, the argument, with slight modifications, remained the same: workers and capitalists had opposing and irreconcilable differences in the trade-off between inflation and unemployment. Such ‘conflict theories’ not only gave political explanations for the trajectory of inflation and unemployment, (most notably in the work of Hibbs 1977) but also thereby provided direct predictions for the preferences of individuals towards anti-unemployment and anti-inflation policies based on their position within the social stratification. Specifically, the working class, broadly classified, is more concerned about reducing unemployment than firm-owners. Unemployment reduces the lifetime income of workers directly and also exerts a downward pressure on wages by reducing the bargaining power of workers<sup>3</sup>. Inflation on the other hand worked to the advantage of those workers with low savings.

With the rise of new classical macroeconomics in the 1970s and its subsequent hegemony any trade-off between inflation and unemployment came to be seen as essentially short-term and certainly could not be utilized by policy makers to affect macroeconomic outcomes without incurring severe macroeconomic costs. As a consequence, much of the macroeconomic literature moved away from class-based, political economy models of inflation and unemployment towards what Iversen and Soskice 2006 elegantly call

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<sup>2</sup> Indeed, as Pollin, 1998, points out, class conflict is the implicit mechanism that drives the natural rate of unemployment even in orthodox neoclassical accounts. As he puts it—“Marx and Kalecki also share a common conclusion with natural rate proponents, in that they would all agree that positive unemployment rates are the outgrowth of class struggle over distribution of income and political power. [...] Of course, Friedman and the New Classical reach this conclusion via analytic and political perspectives that are diametrically opposite to those of Marx and Kalecki. To put it in a nutshell, mass unemployment results in the Friedmanite/New Classical view when workers demand more than they deserve, while for Marx and Kalecki, capitalists use the weapon of unemployment to prevent workers from getting their just due.” (Pollin 1998)

<sup>3</sup> The idea of unemployment as a labor disciplining device has, of course, a provenance from Marx. Marxist theories of the labor market maintain this as a key fact of the labor market (for example Bowles 1985)

macroeconomics which “[F]ocuses attention on what democratic governments can do wrong in the short term”. The prescription that followed was to replace government with independent central banks, and discretionary macroeconomic policy with rules based approaches such as inflation targeting (Barro & Gordon 1983, Cukierman 1992)

While Post-Keynesian and heterodox approaches never abandoned the idea of demand management, the advent of New Keynesian economics restored the space in mainstream economics for economic policy to have beneficial macroeconomic outcomes. As opposed to rational expectations, there is a role for demand management and other policies when imperfections arise due to wage and price rigidities whereby involuntary unemployment can be reduced. The now long literature on the NAIRU continues to suggest that combating inflation and unemployment involves two independent and potentially opposing targets<sup>4</sup>.

Given that there has been a restitution of space for macroeconomic policy, this paper seeks to make a contribution in reconstructing the political or class content of disinflationary and expansionary policy. Specifically, this paper seeks to provide some evidence based on individual level observations for the contention that those in contrary class positions respond very differently to policies engineered to combat inflation versus those that are designed to combat unemployment. Using a unique social survey data for 1996, I verify the fact that there are substantial class based differences in what may be termed ‘relative aversion’ to inflation and unemployment (a preference that policy is designed to keep inflation down rather than unemployment down). Capitalists and highly skilled workers are more likely to display relative inflation aversion than less skilled and unskilled workers. As such, the paper has implications for the debate on anti-inflationary policies and inflation targeting in particular as they apply to different countries.

In what follows, I very briefly summarize relevant research in the class impacts of inflation and unemployment and attitudes towards these problems in section (II). Section (III) describes the data that I use. Section (IV) presents the results of various logistic regressions. Section (V) summarizes and concludes.

## **Section (II): Class and attitudes towards inflation and unemployment**

The radical political economy approaches to macroeconomics saw unemployment as acting as 'a regulator of class conflict' (Rowthorn 1977). Unemployment was the central fulcrum of the labor-capital confrontation. Specifically, increases in unemployment maintained a downward pressure on wages while tight labor markets increased factor income going to labor by exerting upward pressure on wages (Boddy and Crotty 1975)<sup>5</sup>.

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<sup>4</sup> For a recent review see Ball and Mankiw, 2002

<sup>5</sup> Recent empirical studies, especially about the U.S experience of the nineties boom, support these ideas indirectly. Bernstein and Baker (2003) find that the low unemployment period in the American economy of the late 1990s aided in improving the welfare of workers according to several metrics. Real wages increased after a generation of decline, and the inflation adjusted income of low income families grew by twice the amount that they did in the eighties expansion ( when average unemployment was higher).

Conflict theories of inflation suggested that the rise in inflation was seen as the result of perpetual claims by workers for wage increases ahead of productivity . The detrimental impact of inflation was primarily on those who had nominally denominated assets whose value was eroded with increasing prices, although there were also pressures on firms which were unable to pass on higher wages as higher prices. To that extent the negative impact of inflation was more pronounced on the capitalist and rentier class. As a result these theories would predict pronounced differences in attitudes towards inflation and unemployment depending on the respondent's class position.

Drawing from this political economy research, empirical studies in the 1970s and 1980s had begun to establish the class character of individuals' preferences for inflation versus unemployment aversion. Given objective evidence that periods of relatively low unemployment and relatively high inflation coincided with an equalization of the personal distribution of income, a larger share of national income going to labor versus capital and a reduction in poverty as well as losses to those with savings in nominally denominated assets (typically the rich), attitudes towards inflation and unemployment had a class character. Hibbs 1977 summarizes the central findings from U.S and UK surveys:

*.. [P]opular concern about unemployment and inflation is class-related. Low and middle income and occupational status groups are more averse to unemployment than inflation, whereas, upper income and occupational status groups are more concerned about inflation than unemployment... it does appear that the subjective preferences of class or status groups are at least roughly in accordance with their objective economic interests...*

Hibbs (1977:1470)

Recent studies of attitudes towards inflation and unemployment have largely ignored class. While there is substantial empirical evidence from opinion research that both inflation and unemployment are seen by respondents as disutilities (see, among others, Di Tella *et al* 2001, Easterly and Fischer 2001 and Shiller 1997), there is less consensus on the relative importance that individuals in different classes place on reducing each of these. Part of the issue is simply that there have been few surveys done which explicitly ask the respondent to rate their aversion to inflation versus unemployment if these were alternative outcomes. As such, the data has limited researchers' agenda. Equally, there has been little interest in the characteristics of individuals who might support a policy designed to combat inflation versus one that tackled unemployment. To the extent that this has been undertaken, it has been to assess inflation aversion among the rich versus the poor (Jayadev 2006, Easterly and Fischer 2002)<sup>6</sup>. There has been little to no recent

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Abraham and Haltiwanger 1995 who review mainly US evidence suggest that real wages are more likely to be pro-cyclical than counter-cyclical.

<sup>6</sup> Scheve, 2003, 2004 remains an exception in providing more detailed evidence for the characteristics of individuals supporting each policy.

work which attempts to look at politics and in particular class politics in the determination of preferences towards anti-inflation and anti-unemployment policy. It is to this exercise that we now turn.

### **Section (III): Data**

#### *Measuring Inflation Aversion*

The International Social Survey Program (ISSP) conducted by the Inter-university Consortium for Political and Social Research in 1996 focuses on the preferences of more than 30,000 individuals in twenty-seven<sup>7</sup> different countries regarding the role of government in society. The countries included include OECD economies, former eastern bloc economies and unfortunately do not include any low income countries apart from China<sup>8</sup>. Among the questions asked in this survey is the following:

*If the government had to choose between keeping down inflation and keeping down unemployment to which do you think it should give highest priority?*

This is the key variable of analysis for the rest of the paper. I define a variable ‘relative inflation aversion’ as taking a value of one when the respondent prefers that the government prioritize reducing inflation rather than unemployment and zero when the opposite holds.

While this provides a direct measure of the weights placed in an individual welfare function on inflation as opposed to unemployment, it is not without some limitations. Ideally, such a question might ask how *much* inflation the individual might accept for reducing the level of unemployment and vice versa so as to have a more direct calibration of the marginal rate of substitution in the social and individual welfare function. However, the measure is certainly superior to questions which ask about inflation without reference to unemployment or any other macroeconomic policy objective, thereby providing no implicit budget constraint.

Figure 1 summarizes the average preference for keeping inflation rather than unemployment down by country.

Some interesting observations suggest themselves. Nearly 42 % of the overall sample report being relatively inflation averse. However, this masks large differences in the average relative inflation aversion between countries, from a low of less than 20% of respondents in France to a high of above 60% of respondents in the Czech Republic. In only five countries out of twenty is the percentage of relatively inflation averse

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<sup>7</sup> In the survey, respondents from Israel and Germany are divided in two separate categories each. The former is divided between Israeli Arabs and Israeli Jews and the latter is split between East and West Germans.

<sup>8</sup> The next round of this survey is to be conducted during 2006 and will include many more developing economies. The issue should certainly be revisited then.

respondents over half (and only in two countries-- West Germany and the Czech Republic-- is the percentage overwhelmingly above the midway mark).

### Measuring Class

Constructing readily comparable and objective measures of social class are fraught with difficulties (See Leiulfsrud et al 2005 and Wright 1997 for an exposition on some of these). Contemporary measures of class differ based on the elements that researchers consider important to their theoretical approach--for example along lines of ownership, management, career prospects, income, status, education or other such categories (Carchedi 1978, Wright 1985, Esping-Andersen 1993, Erikson and Goldthorpe, 1993). However, not all of these are likely to bear directly upon the question of relative inflation aversion. Class has relevance in as much as it reflects the labor market position of the respondent and therefore his preferences to policies which enhances his or her position. It is desirable therefore to utilize a definition which closely reflects the respondent's occupation and position as employer or worker.

In this paper, I utilize a few different measures of class. The ISSP dataset provides an occupational variable based on the ISCO 1988 classification which has previously been used by researchers to construct a wide array of measures of stratification. A first (crude) method is to utilize the traditional Marxist division between firm owner and employee. If the respondent is classified as self-employed with employees, he or she is classified as a firm owner, and an employee otherwise. I define a dummy variable called *firm owner* which takes the value of 1 if the respondent is self employed and has more than one employee, and 0 otherwise.

Sociologists have expended enormous effort in providing more useful and sophisticated categorizations of class. In order to perform a more satisfactory class analysis, I replicate Wright's (1985) scheme which divides the labor force into owners and wage laborers and wage laborers in turn into three categories- experts, skilled and low-skilled. Wright uses this to operationalize his idea of class locations and contradictions therein. Workers may be divided according to their relative privilege in the labor process. Based on a careful cataloging of occupations, Wright defines *experts* as those whose jobs require skills (and in particular accredited or credentialed skills) and who are in scarce supply relative to their demand by the market. *Semi-skilled* and *unskilled* class positions by contrast are held by those who have uncredentialed or no skills and who are thus in abundant supply. Using this approach has significant advantages. It makes theoretical sense for the question at hand to conceive of class measures which reflect the respondent's relationship to the labor market and therefore to his or her bargaining power and probability of continued employment. An expert for example, will typically enjoy a credential rent and be more likely to have both a higher level of bargaining power and a lower probability of being replaced than a low-skilled worker. He or she may therefore have opposing ideological and political interests based to other workers. At the same time both an

unskilled worker and a skilled worker are more concerned about unemployment than a capitalist<sup>9</sup>. Appendix 1 details the creation of the class variables.

.Figure 2 shows the average relative inflation aversion in each country for each grouping of wage laborers. As is evident, in most countries, ‘experts’ are more relatively inflation averse than semi-skilled and unskilled workers<sup>10</sup>, as might be expected given the logic that more highly skilled workers enjoy greater bargaining power and a lower probability of unemployment than lower skilled workers, but are equally likely to see their wages eroded by inflation.

Another approach is to look at subjective evaluations of class categories. The ISSP dataset asks respondents their own evaluation of their social class (the categories are lower middle class/ upper working class, middle class, upper middle class and upper class). Unlike more objective measures, subjective perceptions of class probably depend on an amalgam of factors such as the respondent’s education, status, income and gender as well as factors which are of direct relevance to the question of relative inflation aversion—the respondent’s position and prospects in the labor market and the asset market. Nevertheless, it is useful to look at this as a check on the robustness of the earlier measure of class. I define three subjective class categories—the variable *subjective lower class* takes a value of 1 when the respondent identifies as being in the lower class or in the working class and 0 otherwise. Another variable *subjective middle class* takes a value of 1 if the respondent is from the lower middle class or middle class and 0 otherwise. Finally, the value of the variable *subjective upper class* takes a value of 1 when the respondent is from the upper middle or upper class.

Table (I) provides summary statistics for all variables.

#### **Section (IV): Results**

In order to assess the class character of relative inflation aversion, I undertake a series of logistic regressions of relative inflation aversion on the respondent’s class position. Tables (II) and (III) provide the detailed results of these exercises

Columns (I)-(III) in table (I) are the results from performing the logistic regression on the three definitions of class without any controls. As is evident from column (I), firm owners are significantly more likely than workers to be relatively inflation averse (or less likely to be relatively unemployment averse). Column (II) uses the classification for wage laborers developed by Wright. The omitted dummy is expert workers and hence the results suggest that as compared to experts, both low-skilled and skilled workers display less relative inflation aversion suggests that in comparison with the omitted group. Similarly, in column (III) in comparison to those who consider themselves upper class, those who consider themselves middle and lower class are much less relatively inflation averse.

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<sup>9</sup> This is an example of what Wright terms a contradictory class location.

<sup>10</sup> The major exception is Israel- perhaps because of the impact that the period of hyperinflation in the 1970s had upon even skilled workers.

Columns (I)-(III) in table (II) shows that these results persist in the presence of a variety of plausible controls, including dummies for income, gender, age, employment status and union membership. Column (I) shows that a firm owner is about a fourth more likely to prefer anti-inflation to anti-unemployment policies as a worker. Column (II) shows that relative to 'experts', semi-skilled are about eight-tenths and unskilled workers are about nine-tenths as likely to report supporting anti-inflation to anti-unemployment policies. The results in column (III) show that as compared to the subjective upper class, subjective lower classes display significantly less inflation aversion. A respondent who considers himself or herself as being part of the lower or lower middle class is about three fourths as likely as someone who is in the upper class to prefer that the government keep inflation down. A respondent in the middle or upper middle class is about eight-tenths as likely as someone in the upper middle or upper class to prefer that inflation be kept down rather than unemployment.

The results on the control variables are interesting to note. Income is controlled for using dummies for income quintiles which take a value of 1 if the respondent is in that quintile or 0 otherwise. The odds ratio on the income quintile dummies reiterate the findings of Jayadev, 2006 - the poor are less relatively inflation averse than the rich, with each income quintile below the richest (the omitted quintile) displaying monotonically increasing inflation aversion, although in the second regression not all odds ratios are significant. Not surprisingly, the unemployed are less likely than those who have employment to prefer that the government pursue a policy of keeping inflation down rather than unemployment in all the models. Gender matters: women report being more relatively inflation averse than men. Trade-union members display statistically significantly less relative inflation aversion than non-union members, perhaps because union members can more easily bargain their wages upwards than non-union members in the face of rising prices. Somewhat surprisingly, age does not appear to have a statistically significant impact on an individual's relative inflation aversion either when expressed simply or as a categorical variable. These general results are quite robust to a host of other controls for individual characteristics, including household size, whether the respondent is based in an urban area or not, marital status, whether the respondent is employed in the public sector or the private sector and so on.

## **Section (V): Conclusion**

In the last three decades, the hopeful message of Keynesian demand management has fallen out of favor with policy makers; as more faith has been placed in market based solutions, in independent central banks and in microeconomic interventions to handle the problems of inflation and unemployment. The theoretical impetus for this shift was provided by the rational expectations revolution of the 1970s and subsequent new classical analyses of the state. These in turn argued that democratic governments were often bad for macroeconomic efficiency as they would tend to increase deficits and be unable to credibly tackle inflationary pressures. Worse still, any attempt to artificially reduce the unemployment rate would lead inevitably to higher inflation with no effect beyond the very short term on the unemployment rate. Thus, the standard prescription of



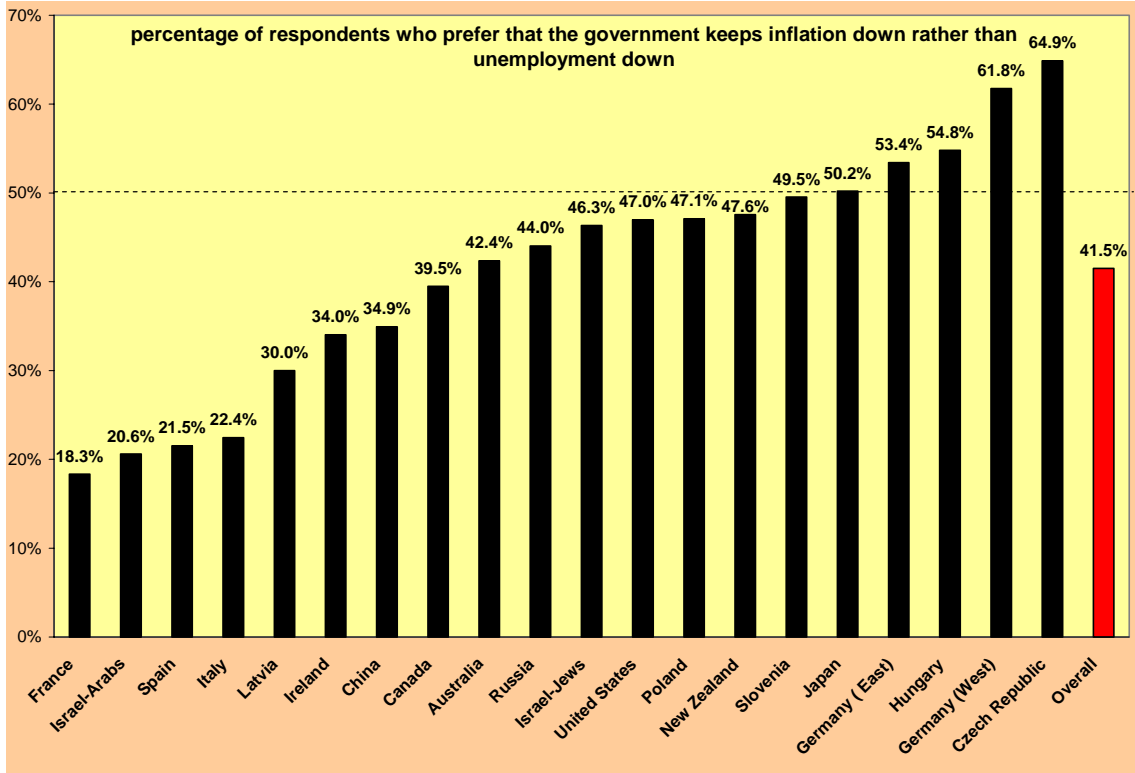
earlier times was replaced by the orthodoxy of central bank independence and, increasingly a narrow focus on inflation targeting (Bernanke *et al* 1999). For proponents of this view, delegating responsibility to an authority which can credibly commit to a single target is beneficial in increasing macroeconomic efficiency and protecting the public from a perhaps well meaning, but misguided government.

A movement away from commitment to full employment and towards low targeted inflation has potentially profound distributional consequences. Despite the claims made by some that anti-inflationary policy is, for example, pro poor<sup>11</sup>, it is an empirical question as to whether inflation or unemployment is seen as a bigger problem by different individuals. Recent research on inflation versus unemployment aversion (Jayadev 2006, Scheve 2004) found that the rich are more relatively inflation averse than the poor. The results presented in this paper further strengthen this idea by finding that relative inflation aversion is more pronounced among the privileged or elite broadly defined in class terms. Since class is a critical variable in determining an individual's labor market opportunities as well as the source and variability of his or her income, the results make sense. The findings are in concordance with conflict based models of unemployment and inflation which argue that macroeconomic policies may have systematically differential effects on the welfare of workers and owners (as well as on different segments of the working class) and that the preferences of individuals in separate class positions reflect these differences. These findings have important consequences for research on the implications of anti-inflation versus anti-unemployment policies in general and on the more current debate around inflation targeting in particular.

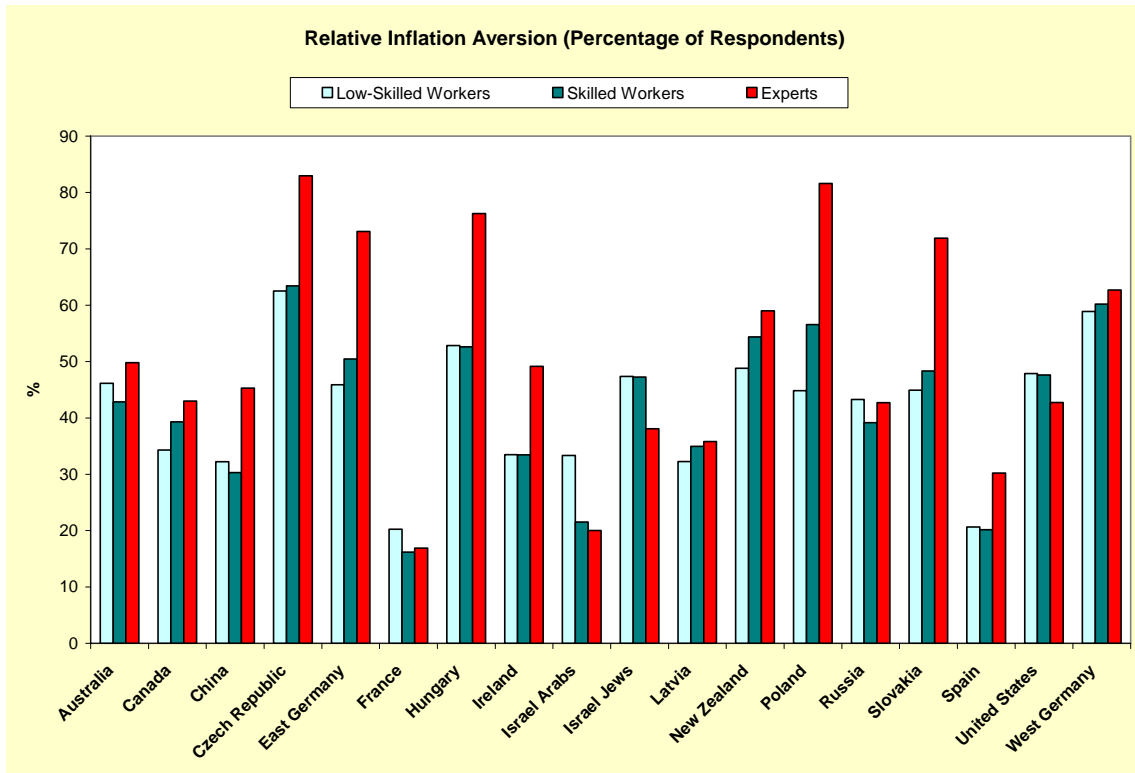
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<sup>11</sup> Dollar and Kraay (2002) for example argue that reducing inflation is “super pro poor”

**Figure 1**



**Figure 2**



**Table (I): Summary Statistics**

Variable	Source	Obs	Mean	Std. Dev.	Min	Max
Inflation Down	V 63: ISSP	23824	0.41	0.49	0	1
Expert	Constructed from V202: ISSP	35313	0.07	0.25	0	1
Semi-Skilled	Constructed from V202: ISSP	35313	0.23	0.42	0	1
Unskilled	Constructed from V202: ISSP	35313	0.24	0.43	0	1
Subjective Lower class	V221: ISSP	35313	0.31	0.46	0	1
Subjective Middle class	V221: ISSP	35313	0.49	0.50	0	1
Subjective Upper Class	V221: ISSP	35313	0.07	0.26	0	1
Firm Owner	Constructed from V213 and V214: ISSP dataset	35313	0.04	0.19	0	1
First Income Quintile	Constructed from V217: ISSP	35313	0.15	0.36	0	1
Second Income Quintile	Constructed from V217: ISSP	35313	0.11	0.31	0	1
Third Income Quintile	Constructed from V217: ISSP	35313	0.13	0.34	0	1
Fourth Income Quintile	Constructed from V217: ISSP	35313	0.11	0.31	0	1
Fifth Income Quintile	Constructed from V217: ISSP	35313	0.10	0.30	0	1
Union Member	V 222: ISSP	35313	0.18	0.38	0	1
Female	V 200: ISSP	35228	0.52	0.50	0	1
Unemployed	V 206: ISSP	35313	0.06	0.23	0	1
Age	V 201: ISSP	35109	44.82	16.65	15	97

**Table (II): Logistic Regression of Relative Inflation Aversion on Class Variables (without controls)**

Variable	(I)		(II)		(III)	
	Odds ratio	Z-statistic	Odds ratio	Z-statistic	Odds ratio	Z-statistic
Firm Owner	1.47***	(5.53)				
Unskilled			.69***	(-6.66)		
Semi-Skilled			.70***	(-6.44)		
Subjective Lower Class					.69***	(-6.37)
Subjective Middle Class					.84***	(-3.15)
N	23824		13955		20437	

Notes: \*\*\*= significant at the 1% level, \*\*= significant at the 5% level, \*= significant at the 10% level. Omitted variable is experts (high skilled) in column (II), and subjective upper class in column (III). Country average inflation dummies are included but not shown.

**Table (III): Logistic Regression of Relative Inflation Aversion on Class Variables (with controls)**

Variable	(I)		(II)		(III)	
	Odds ratio	Z-statistic	Odds ratio	Z-statistic	Odds ratio	Z-statistic
Firm Owner	1.20**	(2.11)				
Unskilled			0.87**	(-1.98)		
Semi-Skilled			0.82***	(-2.86)		
Subjective Lower Class					0.75***	(-3.72)
Subjective Middle Class					0.86**	(-2.08)
Lowest Income Quintile	0.63***	(-7.95)	0.66***	(-5.51)	0.68***	(-6.28)
Second Income Quintile	0.73***	(-5.17)	0.75***	(-3.65)	0.76***	(-4.24)
Third Income Quintile	0.80***	(-3.97)	0.81***	(-3.18)	0.85***	(-2.67)
Fourth Income Quintile	0.86**	(-2.50)	0.92	(-1.17)	0.89**	(-1.86)
Unemployed	0.70***	(-3.80)	0.74**	(-1.86)	0.71***	(-3.58)
Female	0.82***	(-5.43)	0.80***	(-4.75)	0.80***	(-5.76)
Union Member	0.79***	(-5.10)	0.81***	(-3.90)	0.80***	(-4.76)
Age	1.00	(0.97)	1.00	(0.53)	1.00	(1.24)
N	14245		9273		13469	

Notes: \*\*\*= significant at the 1% level, \*\*= significant at the 5% level, \*= significant at the 10% level. Omitted variable are experts (high skilled) and highest income quintile in column (II), and subjective upper class and highest income quintile in column (III). Country average inflation dummies are included but not shown.

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## Appendix 1: Class measures

The ISSP dataset provides ISCO-88 classifications for all but four of the countries. For each of these countries we have ISCO-68 classifications. Iversen and Soskice, 2001 provide a bridge between these coding mechanisms based on previous work by Ganzeblom. Using this code (available from Iversen's webpage at the Harvard School of Government), I recode all respondents as per ISCO-88 codes. I drop the 300 or so observations for which there is no bridge available.

Wright, 1997 provides a mechanism by which to classify ISCO-88 classifications into three skill categories, experts, skilled and low skilled workers. Using the codes provided by Leilsfrud et al (2005), I replicate these categorizations for the ISSP dataset.

The code is available upon request.