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MILTON FRIEDMAN AND THE NATURAL RATE OF UNEMPLOYMENT

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ABSTRACT

This guide focuses on Friedman's Nobel lecture and the importance of the term 'natural rate of unemployment' for economic policy and how an analysis of different translations of Friedman's contributions may shed light onto the different understanding of stabilization policy in European countries.

Milton Friedman probably shaped the development of economic thought since the 1960s like no other economist. This guide will show why Friedman's work is deemed to be so important and how Friedman's influence reached far beyond pure academic debates. Due to Friedman's enormous amount of publications and fields of research, this guide in no way claims to fully cover and honour Friedman's contributions to macroeconomics. Rather, it is aimed at providing a short but helpful insight and background information to Friedman's contribution to the Phillips curve discussion and its implications for economic policy.

1. MILTON FRIEDMAN'S LIFE

Milton Friedman – the Nobel Prize winner of 1976 – wrote an autobiographical note which can be freely accessed at the official [website of the Nobel Prize](#). In some way, Friedman realised the American dream. Born on 31 July 1912 in Brooklyn into a family originally from Austria-Hungary, Friedman at first faced no easy going life. The family often struggled financially and Friedman had to cope with the death of his father as he was only 15 years old. Hence, Friedman had to finance his education himself. Nonetheless, Friedman succeeded in graduating from Rutgers University in 1932 and was offered a tuition scholarship at the Chicago Economics Department where he earned a M.A. in 1933. From 1933 to 1934 he had a fellowship at Columbia University. In the year 1934 to 1935, Friedman returned to Chicago. He received his Ph.D. from Columbia University in 1945, after having also spent time at the National Resources Committee and at the National Bureau of Economic Research as well as at the U.S. Treasury Department. Friedman stayed at Chicago for the next 30 years since 'Chicago has been my intellectual home ever since' (Friedman 1976a). Friedman left Chicago in 1977 and was Senior Research Fellow at the Hoover Institution of Stanford University until his death on 16 November 2006. In 1976, Friedman was awarded the Nobel Prize in Economics "for his achievements in the fields of consumption analysis, monetary history and theory and for his demonstration of the complexity of stabilization policy". Hence, Friedman succeeded in attaining the highest academic honours while starting from a rather unfavourable position.

Friedman's contributions are without doubt outstanding and still influence economic theory and policy. [Lawrence H. Summers](#) hence remarked that '[if] John Maynard Keynes was the most influential economist of the first half of the 20th century, then Milton Friedman was the most influential economist of the second half.'

To get a grasp of Friedman's various contributions, the interested reader might want to have a look at the website of [IDEAS](#) which lists and makes accessible many, even though not all, of Friedman's contributions. At the time of writing this guide on Friedman, he was ranked among the top 5 per cent of all authors listed on IDEAS by 37 criteria! Many translations of Friedman's work are listed in the [worldcat database](#). Further bibliographic information can be found at the [library of the University of Chicago](#) and a short summary of his life and work is freely available at [Econlib](#). Another good source about Milton Friedman which also provides many Newsweek articles can be found at the website of the [Hoover Institution of Stanford University](#) which is dedicated to the life and work of Milton and his wife Rose Friedman. This website also provides further links to Friedman's television series 'Free to Choose' which is highly recommended as a starting point for analysing

Friedman's point of views. In particular, volume 9 '[How to Cure Inflation](#)' can be helpful in understanding the following discussion of Friedman's Nobel Prize lecture and its relation to the Phillips curve discussion. This volume also features a discussion with the President of the German Bundesbank from 1977 to 1979, Otmar Emminger. This is insofar important as the German Bundesbank was the first central bank to officially target a money growth rate (for the year 1975) and hence to follow Friedman's policy advice of a steady growth rate of the money supply (see on this [Spahn 2005](#)) which Friedman proposed as a superior policy than 'Keynesian' fine tuning (see [Friedman 1970](#)). Exactly this fine tuning by the means given by the Phillips curve is also criticised in his [Nobel lecture](#) (Friedman 1976b).

2. THE NOBEL PRIZE AND THE PHILLIPS CURVE

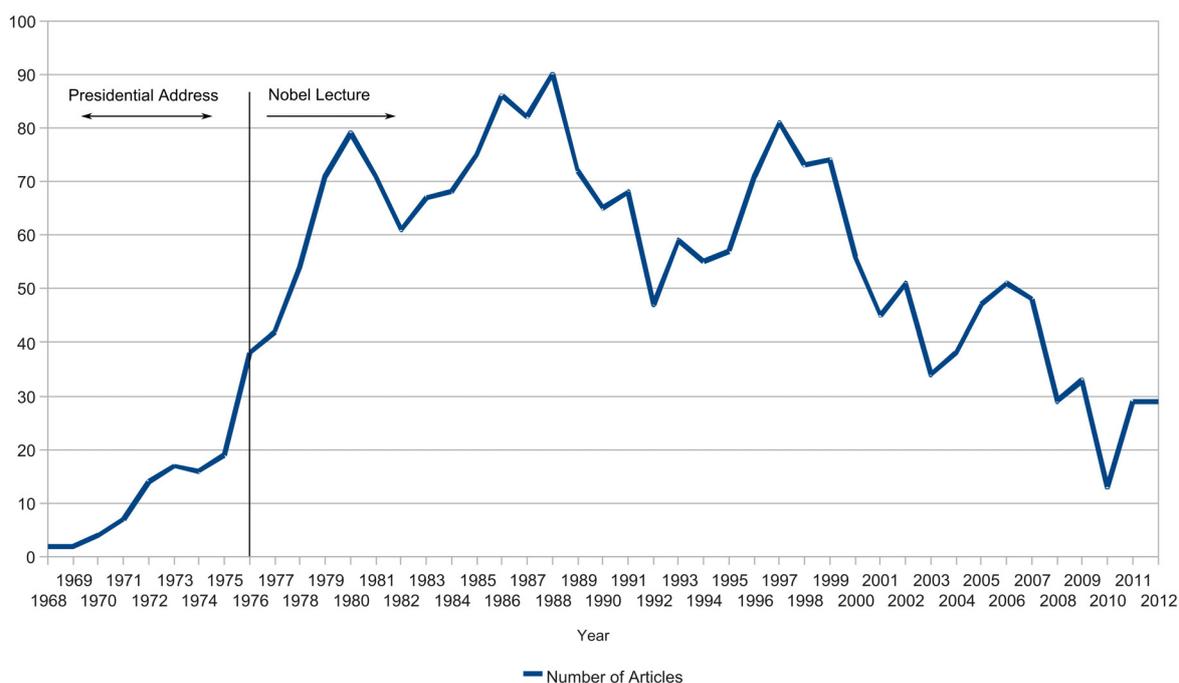
There are two outstanding contributions of Friedman to the Phillips curve debate: Friedman's 1967 presidential address to the American Economic Association (Friedman 1967) and Friedman's Nobel lecture in 1976 (Friedman 1976b). As there is already an [EE-T research paper](#) on the 1968 contribution, the reader might want to have a look at this article and at the [EE-T database](#) which includes references to two early German translations of his [presidential address](#) (Friedman 1968).

The Nobel lecture might be understood as bringing Friedman's concept of the 'natural rate of unemployment' to a broader audience, whereas the presidential address in 1967 was in particular given to a more narrow audience of economists. Furthermore, in 1976 – and contrary to 1967 – Friedman's expectation-augmented Phillips curve was not only appealing on theoretical grounds, but also empirically backed up by stagflation in the 1970s. Hence, Friedman's focus on the Phillips curve in his Nobel lecture might be also regarded as celebrating a victory over 'Keynesian' Phillips curve analysis.

Indeed, as can be seen from the diagram which shows the number of articles in JSTOR containing the term "natural rate of unemployment" anywhere in the document, there is a strong rise in the amount of articles after Friedman's Nobel lecture (see Figure 1). The amount of articles rose from around 20 in 1975 to nearly 80 articles each year at the end of the 1970s.

Figure 1: Article Count in JSTOR

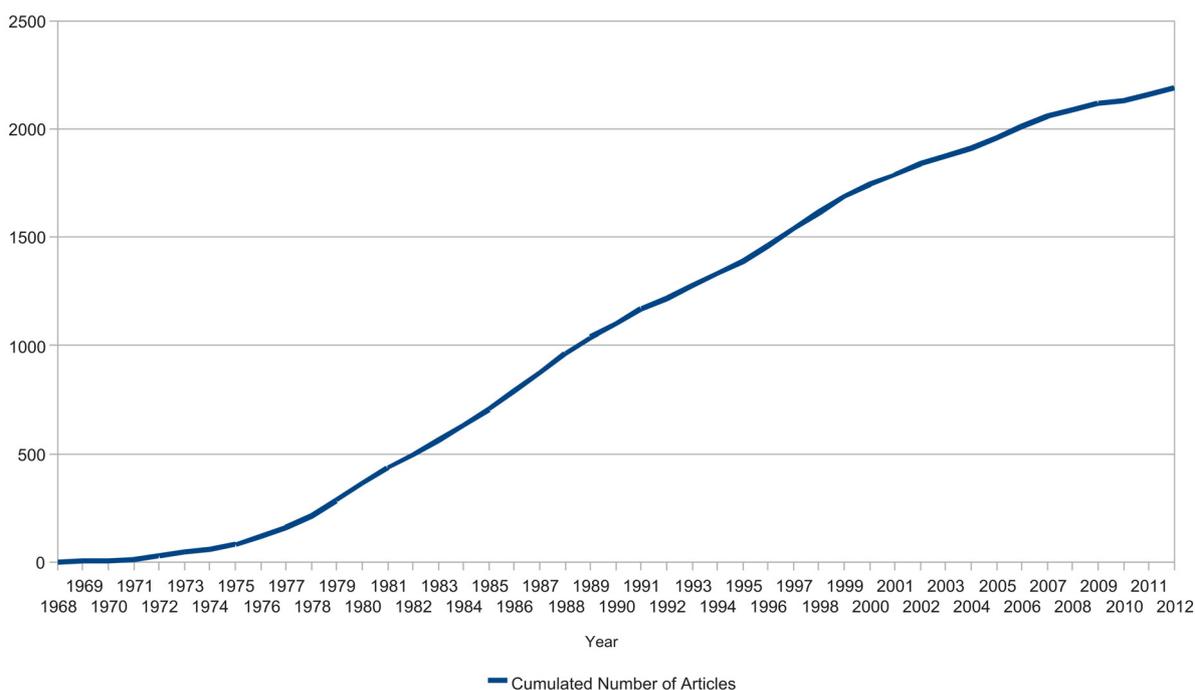
Data Source: <http://dfc.jstor.org>; Search Term "Natural Rate of Unemployment"; Search "anywhere in document"



By 2012, there are over 2000 articles referring to the concept of a 'natural rate of unemployment' (see Figure 2) – even though there is a secular decline in the amount of articles in each year since the peak in 1988.

Figure 2: Cumulated Article Count in JSTOR

Data Source: <http://dfc.jstor.org>; Search Term "Natural Rate of Unemployment"; Search "anywhere in document"



One of the most interesting questions with respect to the translation of economic texts is exactly the translation of the term 'natural rate of unemployment'. This is due to the fact that in particular the adjective 'natural' suggests at first sight that there is a certain unemployment rate which is somehow god-given. Quite to the contrary, Friedman (1968: 9) emphasised that the natural rate is not 'immutable and unchangeable'. Hence, an interesting research topic would be to track how the term 'natural rate of unemployment' and in particular the adjective 'natural' had been translated into other European languages and what implication or background might be inferred from a different translation than the word-to-word one. This is in particular important insofar as the concept of a 'natural rate of unemployment' has far-reaching consequences for economic policy as in this economic setup a long-run trade-off between inflation and unemployment is completely ruled out.

Furthermore, the existence of a 'natural rate of unemployment' renders any kind of stabilisation policy or fine-tuning unnecessary as this natural rate acts as a centre of gravity to which the economy will always return in the long run. Friedman hence not only changed the whole Phillips curve debate, but also made a clear statement against any activist stabilisation policy in general (see [Laidler 2012](#): 17f.). Thus, activist stabilisation policy is not only not necessary at all, but also very dangerous as it might rather be a source of instability than stability. Hence, the introduction of the concept of the 'natural rate of unemployment' into economic thought had far-reaching consequences for economic policy in general and activist monetary and fiscal policy in particular. An analysis of the different translations of the adjective 'natural' and of Friedman's contributions therefore might provide additional insights into the probably divergent understanding of the role of economic policy in the different European countries and hence might prove to be of importance regarding the current struggle of the Eurozone and the difference of opinions of political leaders on how to overcome the crises and recessions in its member states.



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