

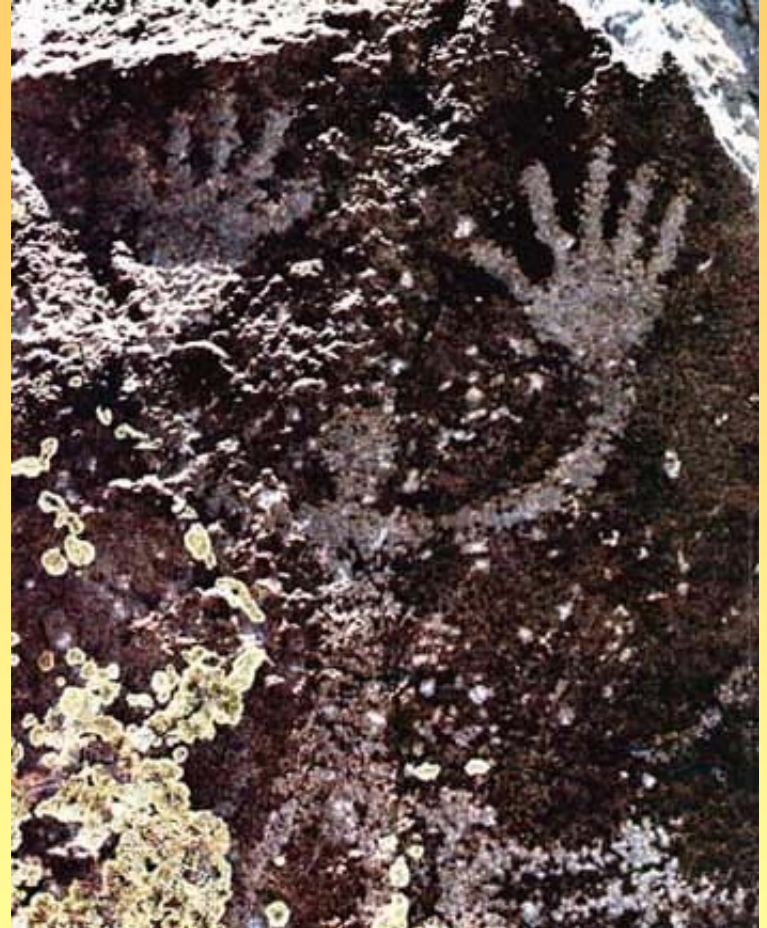
# America Works: critical thoughts on the Exceptional US Labor Market

Richard B. Freeman, Harvard, NBER  
Centre for Economic Performance, LSE



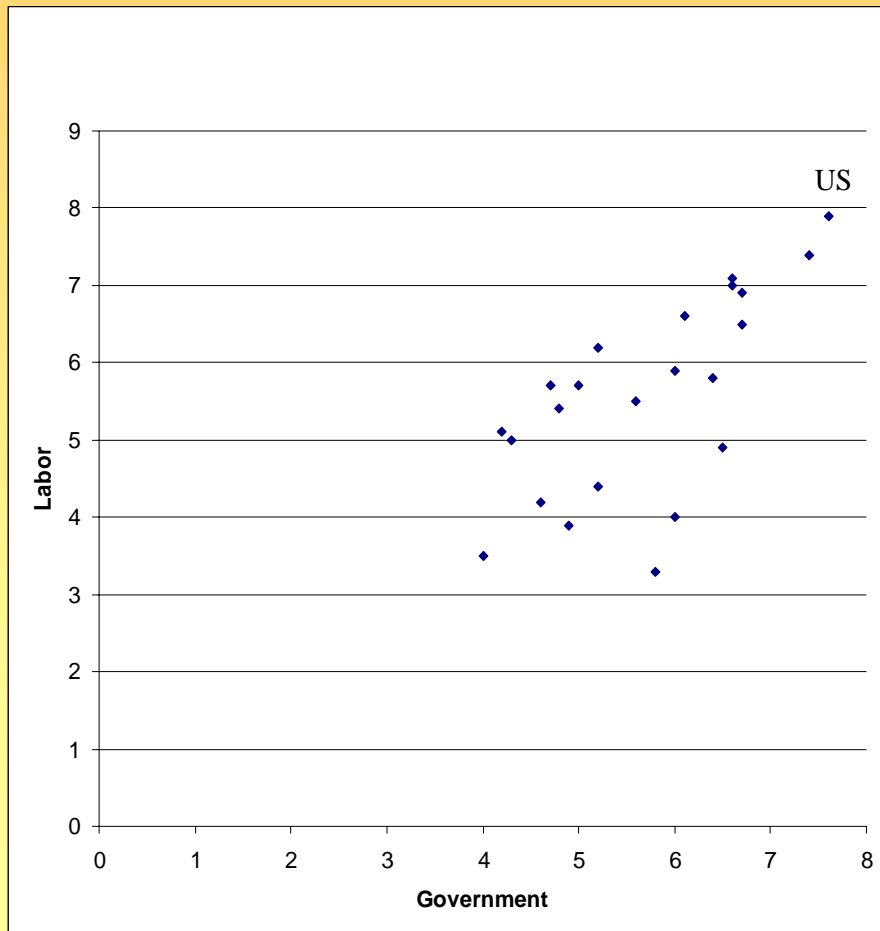
# What is exceptional?

Greater reliance on the Invisible Hand of market forces and less on labor institutions and government regulations than other advanced countries.

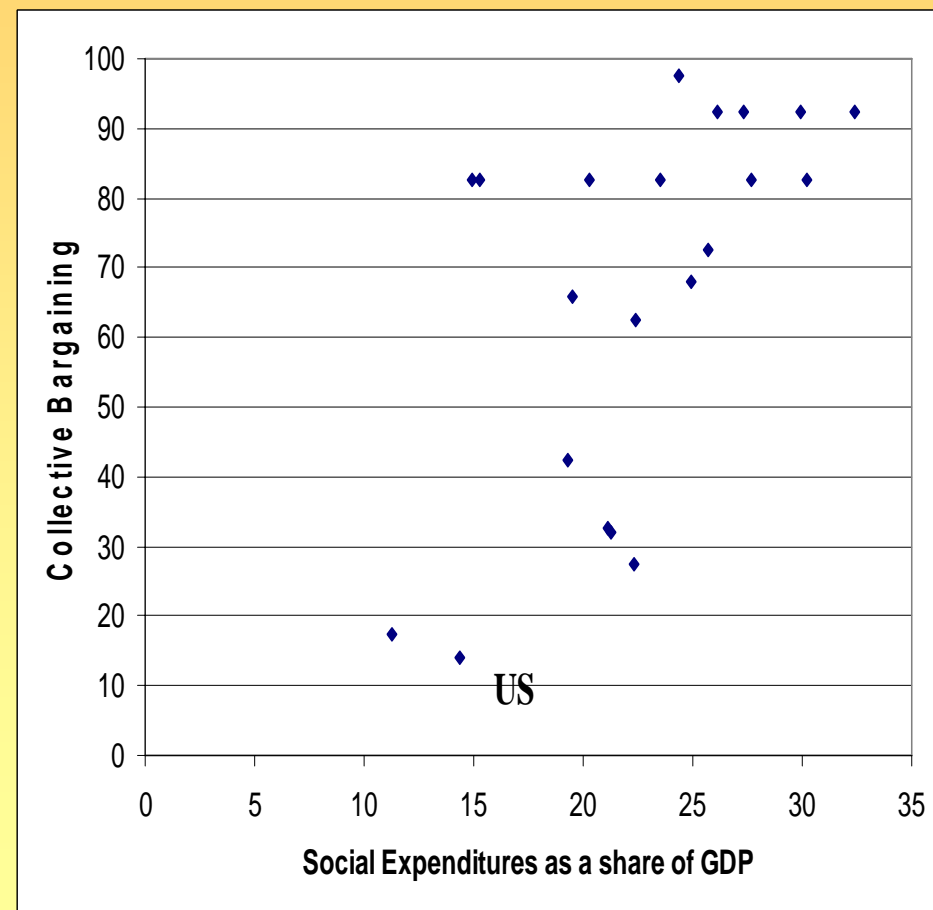


# Shows up in measures of market freedom/institutions

Fraser Institute Measures of Labor and Government: high is more market-oriented



% Collective Bargaining; Social X/GDP: low is more market-oriented





# Does it Work? The Ballyhoo



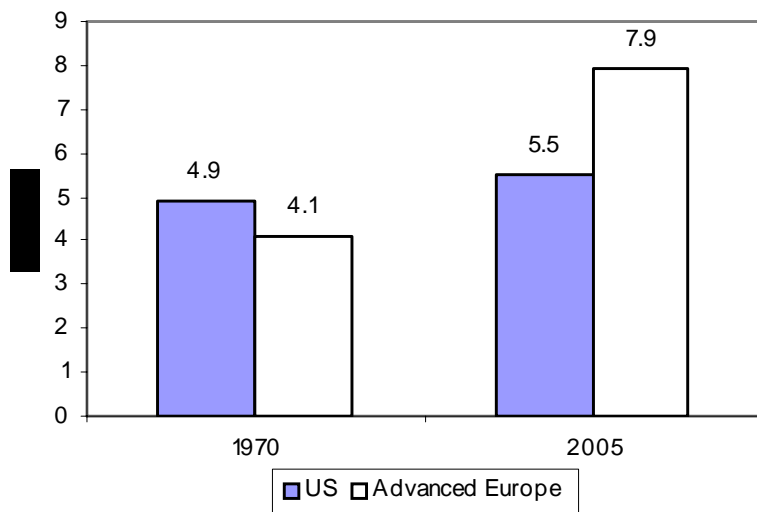
Considerable successes – high rates of employment and hours worked, rapid productivity growth, supply adjustments to economic change, successful absorption of large immigrant flows, opening of greater opportunities for women → good growth of GDP per capita, 1990-2006



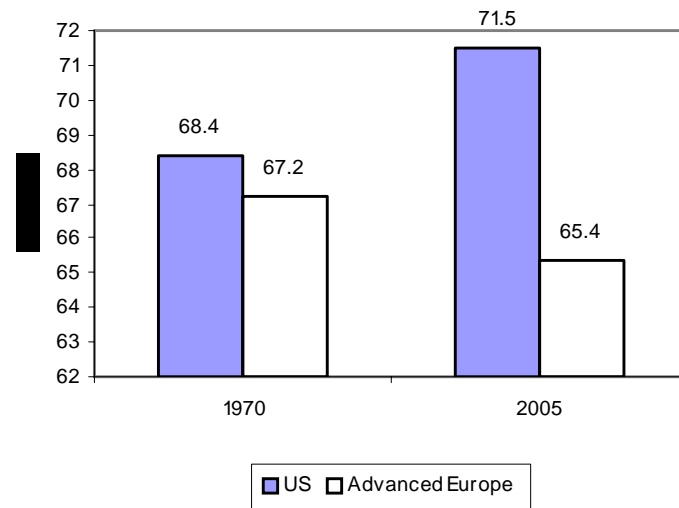
	Change	
	%	Absolute (ppp)
US growth	1.9	11,300
China growth	8.9	5,700

# SUCCESS IN ATTAINING HIGH EMPLOYMENT RATE

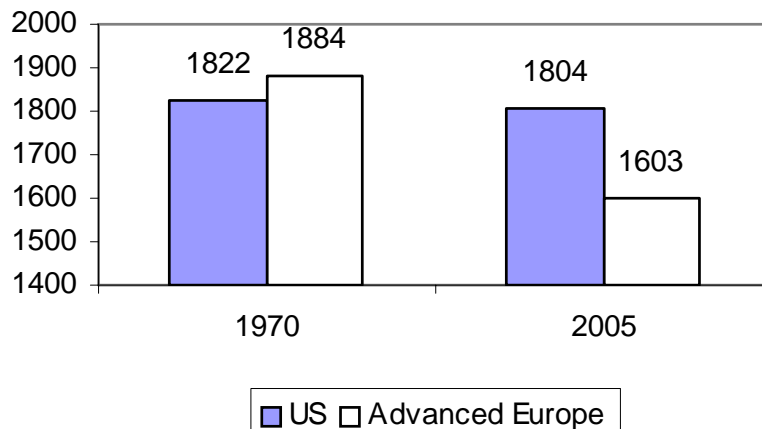
## Unemployment



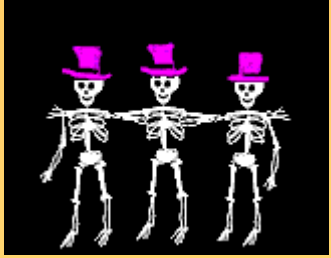
## Employment/Population



## Hours



# But ... skeletons in the Closet

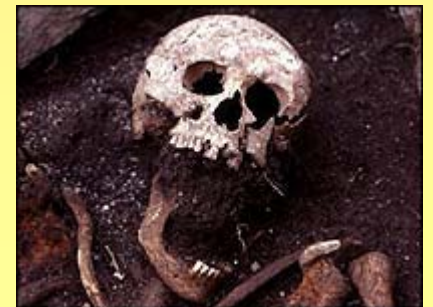


The failures –

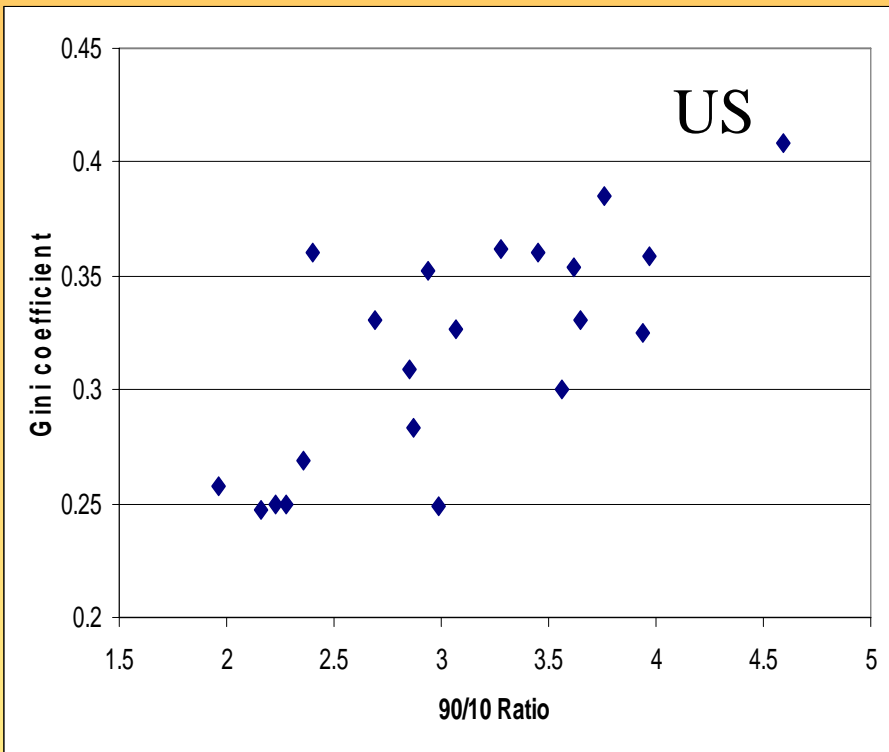
- the most unequal economy in the advanced world,

- productivity growth goes largely to the highest paid,

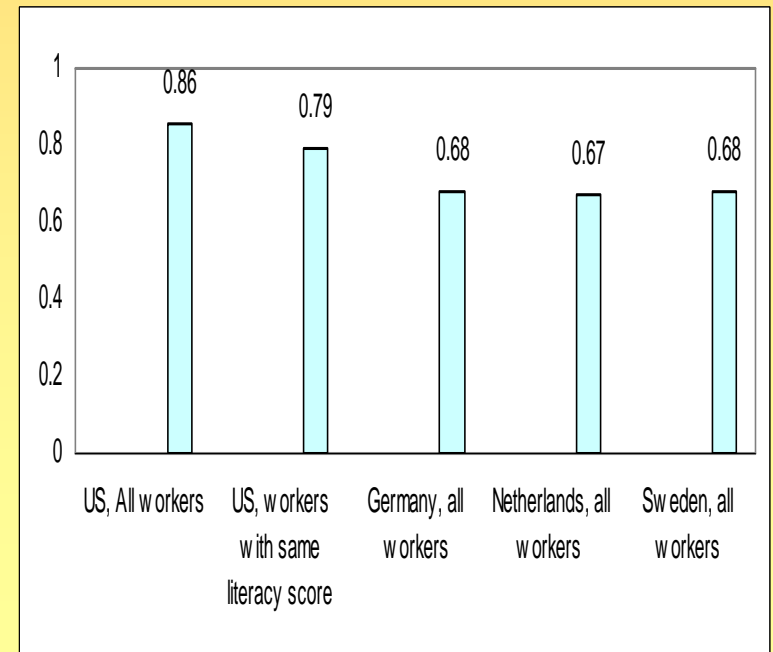
- workers unable to obtain the voice they want at their workplaces.



# INEQUALITY



## Standard deviation ln earnings



GINI (from CIA WORLD FACTBOOK)

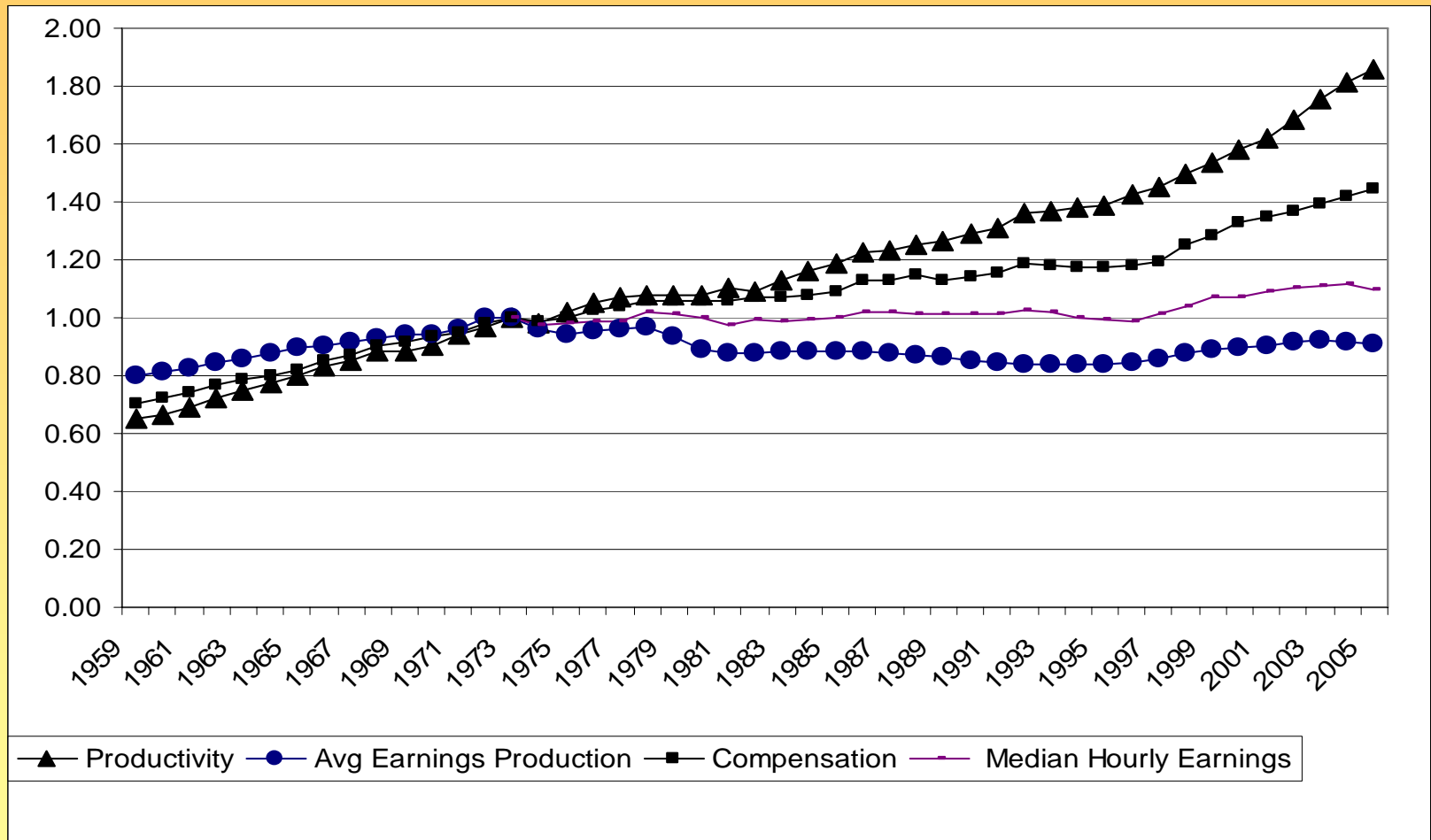
India 0.33

China 0.44

US 0.45 84<sup>th</sup> of 118 countries



# What good is productivity growth to workers?



Source:

Average hourly earnings, production and supervisory workers, from Economic Report of the President 2006 Table, B - 47

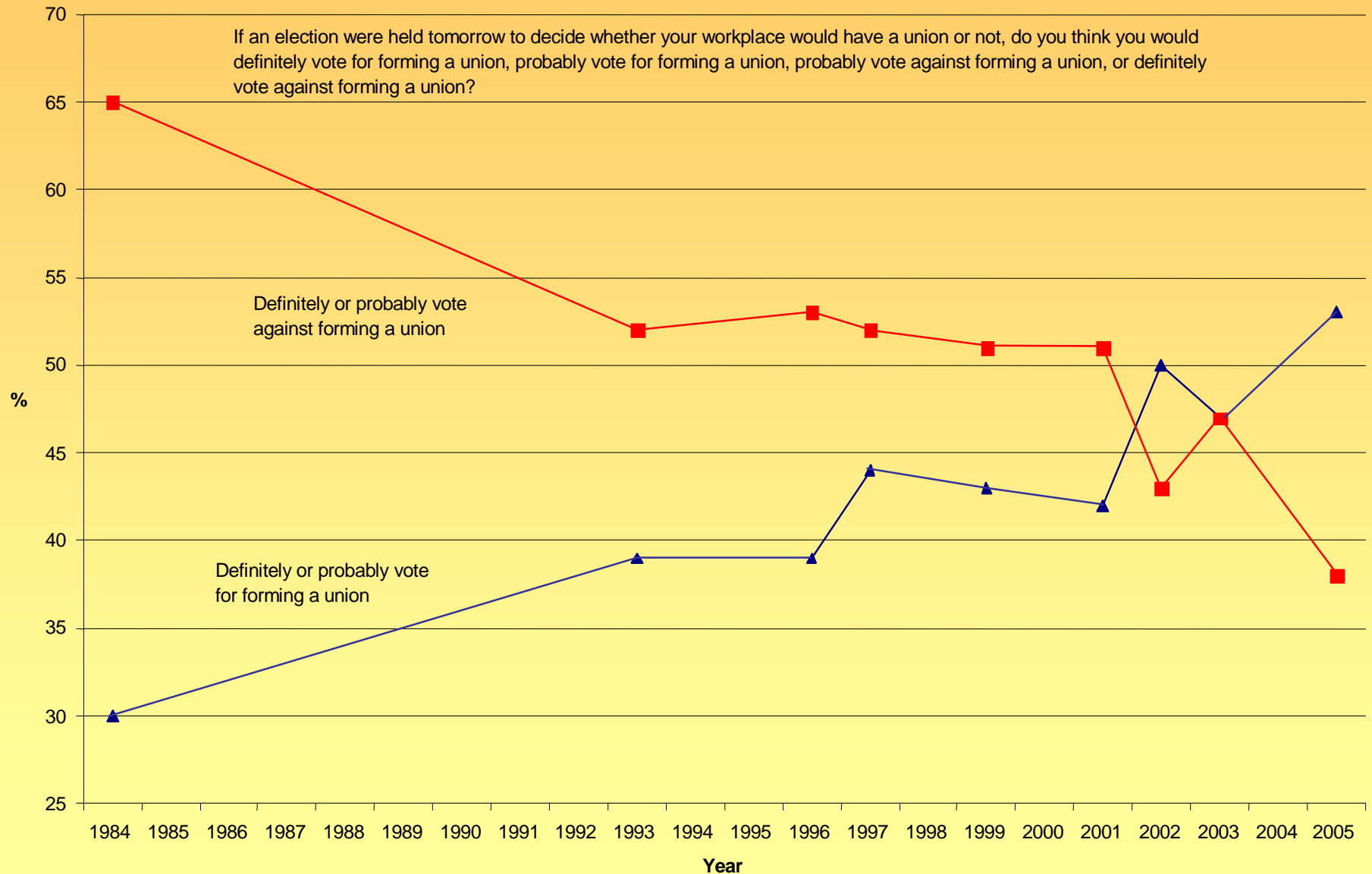
Productivity, Real hourly compensation from Economic Report of the President 2006 Table, B - 49 with 2005 updated from <http://frwebgate2.access.gpo.gov/cgi-bin/waisgate.cgi?WALISdocID=971353361824+9+0+0&WALISaction=retrieve>

Median hourly earnings, Economic Policy Institute

[http://www.epi.org/datazone/06/wagecuts\\_all.xls](http://www.epi.org/datazone/06/wagecuts_all.xls)



# MAYBE WE NEED ... A UNION





# We Don't!



The Perfect Payday Some CEOs reap millions by landing stock options when they are most valuable. Luck -- or something else? 1

The Great CEO Pay Heist Executive compensation has become highway robbery--we all know that. But how did it happen? And why can't we stop it? The answers lie in the perverse interaction of CEOs, boards, consultants, even the feds.2

In late September, 2001, while the world and the market reeled from the attacks on the World Trade Center and the Pentagon, scores of American companies ladled out options to hundreds of executives, options now worth millions of dollars. Sleaze balls and profiteering ghouls: is that what business is about? 3

There is a certain class of political dictator who realizes the situation in his country may be unfortunate ... But he justifies clinging to power by saying any possible successor would be worse. *Après moi, le déluge*, in the words of Louis XV. Some chief executives seem to be like that. They rule long after their best days are past, and collect huge sums while they're at it. 4

# Mother Jones? Dollars & Cents? The IWW? Lefty Loonies?



- 1 Wall Street Journal , March 18, 2006
- 2 Fortune 25, 2001
- 3 Editor, Harvard Business Review, PBS Aug 3, 2006
4. Forbes, April 25, 2002

# **New Global Economy**

**Doubling of global work force when China, India, x-Soviet join**

**Human resource leapfrogging: developing countries invest in university education; multinationals spread modern technology**

**→ trade, offshoring, immigration**

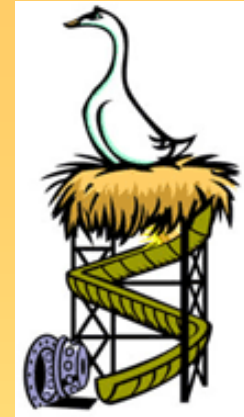
**Greater supply competition**

**Shift in balance toward capital**

**→ More difficult for market forces to help workers**

**Can we do better without ...**

**killing the golden goose? YES**



**throwing baby out with bathwater? YES**



**reducing income/growth of income  
of the super-rich? NO**



# Markets and Models

## Real markets are imperfect:

- huge dispersion of pay among observationally equivalent workers and firms
- employment and wage change among industries and firms inconsistent with market model
- seemingly excessive payoffs to executives – backdating options
- even stock market goes weird sometimes

## Models are imperfect:

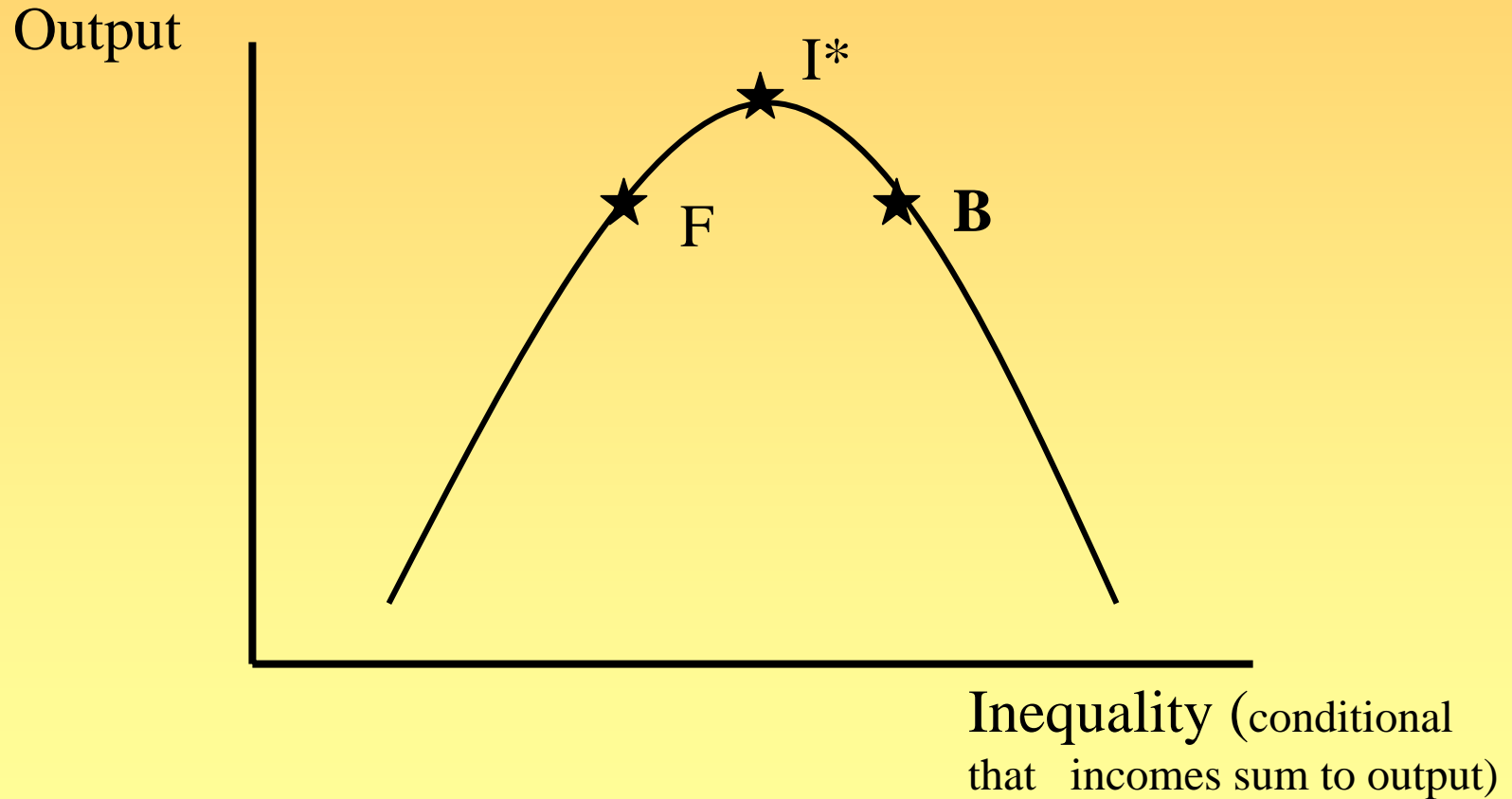
- “fairness” enters decision-making; imperfect information and responses to information;
- experiments show behavioral → more cooperative behavior

## Models and markets need rule of law:

- property rights to workers as well as capital; infrastructure
- growth and progress depends on knowledge – public good
- teamwork in production

# Inequality-Output Inverse U-Curve:

**Raise the curve is win-win; Lower inequality costs (raises) output if economy is to the right (left) of  $I^*$**





# The Road Forward

Economics cannot predict with certainty how policies will work out.

My presumption is that policies designed to help normal citizens are more likely to do that than policies designed to help the super-wealthy

But there can be unintended side effects. It depends on the specific policy and how it is implemented.

And some good/bad outcomes are related:

Inequality and hours worked, for instance.

# **Last Chapter Recommendations, with apologies to John Dunlop**



## **EVIDENCE BASED POLICY NEEDS**

**Simulations of economy with and  
without specified policy reform**

**Econometric evidence on size of  
parameters**

**Knowledge of implementation  
from discussion with decision-  
makers**

# Nine Ways to Help the Invisible Hand(s)



# Ways to help workers and firms operate more effectively

- 1) More R and D; fellowships for young; greater rights to younger researchers/workers\*
- 2) Supplement Wages to make work pay more – EITC, min wage
- 3) Wider basket of public goods- police protection, highways, public schools, parks. National health insurance that would take cost off the books of firms but require taxpayers to fund,

\* US could more than double NSF spending annual spending (~\$6B) with one month of Iraq War (~\$10B)!

4) Public investment in infrastructure -- mass transit; regulations for environmentally friendly production that will enhance the attractiveness of US cities to multinational firms and globally mobile workers. Again, these are market-enhancing investments.



5) Altogether Now, Sgt Pepper's Band "Yellow Submarine" Policies – more profit-sharing, employee ownership, all-employee options; Shared Capitalism Administration to gather information, publicize best practice, aid firms





# Four ways to improve property rights of workers

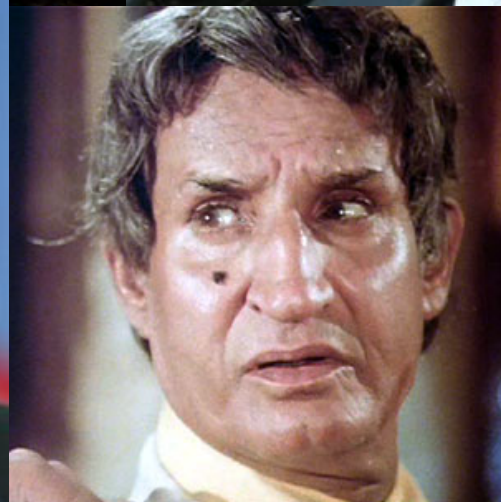
- 6) Expanded choice of modes of worker representation. Current US law produces long war to gain union representation/collective bargaining contract. It stifles other forms of workplace organization for fear that they will become company unions.

The free market solution to an imbalance between capital and labor is to enhance the ability of labor to take care of itself, as part owners of capital and as organized entity, union or nonunion, inside firms. Let the states experiment with new laws.

- 7) Greater worker control of worker assets.  
Activist pension funds have taken a lead in efforts to reform corporate governance, such policies are likely to benefit shareholders broadly; invest in metropolitan cores-where many workers with pension assets reside.
- 8) Tax breaks on options only if all workers given same treatment as management
- 9) Certification of persons on boards



**Some may get angry at  
these suggestions**



**But if you don't like these ideas,  
don't deny the problems ... give  
some other reforms**

What policy needs is open debate informed by evidence and disciplined by reason, but not cramped by political litmus tests or stringent feasibility assumptions. To paraphrase the great wandering mathematician Paul Erdos, our minds should be open – in this case not to new mathematical theorems or proofs, but to diverse plans to better the operation of the labor market and the well being of American workers .

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