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Mickey Kaus (left), contributing editor at The New Republic, and Resident Scholar Oren M. Levin-Waldman weigh the pros and cons of current welfare-to-work programs at the Levy Institute.

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- Work skills, not family ties, should be the criterion for admitting immigrants to the United States, argues Assistant Director Sanjay Mongia.
- Visiting Scholar David Alan Aschauer finds that investment in public infrastructure can yield long-term economic benefits, but some investments are more beneficial than others.
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The Jerome Levy Economics Institute of Bard College, founded in 1986, is a nonprofit, nonpartisan, independently funded research organization devoted to public service. Through scholarship and economic forecasting it generates viable, effective public policy responses to important economic problems that profoundly affect the quality of life in the United States and abroad.

S Jay Levy, Chairman
Dimitri B. Papadimitriou, Executive Director

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Annual Conference on Employment



(Left to right) Susan Dentzer, contributing editor at U.S. News & World Report; Lawrence Chimerine, managing director and chief economist at the Economic Strategy Institute; Maurice D. Hinchey, U.S. Representative; and Alan Reynolds, senior fellow and director of economic research at the Hudson Institute, at the conference session on employment and economic growth

Promoting Employment and Economic Growth

The United States's unemployment rate is falling, but many attending the Levy Institute's annual conference on employment said it has not fallen far enough. Whether or not there is a natural rate of unemployment and what that rate might be are topics of much debate among economists. Some economic models estimate the natural rate to be around 6 percent, but in opening remarks, Executive Director **Dimitri B. Papadimitriou** said the natural rate has been moving downward; it is now 5 percent and can be much lower. Not all conference participants agreed. But there was a general consensus that a goal of economic policy should be to reduce the unemployment rate further by expanding employment opportunities for all who want to work. How employment opportunities can be increased was the focus of this year's conference, which was held on May 1-2 at Blithewood. Featured speakers at the conference were Chairman **S Jay Levy** and **William E. Curry**, management fellow at Yale University and former counselor to President Clinton; there were five sessions. Summaries of the remarks by speakers and by session participants follow.

S Jay Levy

S Jay Levy discussed the absence of upward wage pressures even though the unemployment rate is declining. Inflation is about prices. The price of anything equals costs plus profits, and costs (aside from the cost of imports) are ultimately wages. Decreasing unemployment is leading to some upward pressure on wages, but it is likely that profit margins will narrow to maintain prices. No acceleration of inflation seems likely.

After a lengthy period of economic expansion workers are usually little concerned about job insecurity and are eager for higher pay. However today, after over six years of expansion, employees continue to be much more interested in job security than in wage hikes because of technological unemployment, foreign competition, relatively weak unions, and, of noteworthy importance, the absence of dismay at the checkout counter.

Technological changes are increasing job insecurity at an unprecedented pace. The latest devices replace white-collar as well as blue-collar workers. Moreover, advances in communications and transportation have enabled many businesses to take advantage of low wages in foreign countries. Management and workers both are aware that American firms must take advantage of low wages abroad because their foreign competitors are doing just that.

Increased productivity, especially in manufacturing, has led to smaller workforces and decreased union membership. The increasing numbers of workers who hold low-skill service jobs often see this work as temporary and are therefore less motivated to join unions than were assembly line workers in the past.

Dismay at the checkout counter, which often spurs employees to seek higher pay, is noticeably absent. If consumers did find that the cost of feeding their families was rising faster than their wages, militant demands for sizable raises would be widespread. But what shoppers find is relative stability of consumer commodity prices. Indeed, hourly wages have been rising somewhat faster than these prices.

Profit growth is likely to be inhibited by curtailed consumer use of credit, a growing balance of trade deficit, and Washington's efforts to reduce the federal deficit. The narrowing of profit margins and restraint in demands for pay raises will continue to maintain prices and contain inflation.

William E. Curry

As a state senator and state comptroller in Connecticut and as a counselor to President Clinton, Curry had the opportunity to view the political process from the inside and found it is not as organized as many believe. Policymakers tend to be reactive not proactive. Rather than creating an agenda and pushing it, they spend their time reacting to issues raised by the media and the public. Both Republicans and Democrats are struggling to reframe their view of the world and sell that view to the public. But as they seek to define their parties, the United States is in a period of uncertainty regarding which policies will work and which will not.

Despite this inability to create an agenda, Curry said, much has been achieved during the Clinton administration, especially in the area of social policy. Progress has been made in fighting crime, in welfare reform, and in the areas of affirmative action and school prayer. Some have argued that government has not gone far enough in addressing these social issues. But if so, it is not due to government's unwillingness to address these issues. "It's not that we don't have the courage of our convictions. We don't have the convictions yet to have the courage of," Curry said. Policymakers have probably achieved as much as possible with regard to social issues and should now turn their attention toward such issues as political and institutional reform.

Far too many politicians seem to believe that new problems caused by the technological and economic changes occurring in the United States today are beyond the scope of government. But they are not. Political decisions play an important role in economic growth. The nation faces big problems, but it does not necessarily need big government to solve them. What is needed is strong and effective government leadership.

Session I: An Overview of the Links among Education, Training, and Workforce Development Policies

The first conference session was moderated by **Fred R. Bleakley**, senior special writer for *The Wall Street Journal*. Participants were **Phyllis Eisen**, executive director at the Center for Workforce Success, National Association of Manufacturers; **Mary L. McCain**, vice president for policy and public affairs at the American Society for Training and Development; **Stephen Rose**, senior economist at the Educational Testing Service; and **William R. Steinhaus**, Dutchess County executive.

Eisen issued a wake-up call for those who have not yet realized that we are in a global economy. The reality is that if businesses are to survive, they must change. Some will make it, some will not. The challenge facing American policymakers and industry leaders is to develop the workforce training programs necessary to prepare workers for a diverse economy. Currently, the United States does not have such training programs in place and the educational system is failing to provide such training. Many businesses fill the gap through their own training programs, but when money is tight, training is one of the first things to go.

McCain echoed this concern about the quality of the American educational system. In a rapidly changing economy employers need workers who learn quickly and adapt to change. Workers with learning skills are more valuable than those with specific job skills. Unfortunately, the current educational system does not focus on learning skills. Businesses are willing to provide resources for workforce development, but they cannot train the workforce by themselves. The private and public sectors must work together to reform the educational system.

According to **Rose**, a larger percentage of Americans are going to college and earning bachelor's degrees than in decades past, and it is paying off in terms of income. Because more Americans are getting college degrees, one would expect that the incomes of such people would decrease due to an increased supply in the college-educated labor force. But this has not been the case. The reason is that education continues to be the ticket to high-paying professional and managerial jobs, and the number of such jobs has expanded to keep pace with the increasing number of college-educated workers. This indicates that the economy has undergone a structural change. Income gains are based not necessarily on skill, but on occupation, with those in the professional and managerial occupations gaining the most.

When IBM downsized its workforce in the early 1990s, many feared that Dutchess County's economy would never recover, said **Steinhaus**, but local regions can overcome such an economic blow if the private and public sectors pull together. Dutchess County has proved that. Rebuilding a regional economy requires that government act as the facilitator between private sector businesses and community groups. The most successful policy will be one that diversifies the economic base and builds on a region's human capital through workforce development programs.

Session II: The Virtues and Flaws of Implementing Welfare-to-Work

Judith Havemann, of *The Washington Post*, moderated this session. Participants were **John Howley**, director of public policy with the Service Employees International Union; **Mickey Kaus**, contributing editor at *The New Republic*; Levy Institute Resident Scholar **Oren M. Levin-Waldman**; **Richard McGahey**, economist at Neece, Cator, McGahey and Associates, Inc.; and **James D. Van Erden**, senior vice president in Workforce Development at the National Alliance of Business.

If low-wage workers are to survive, they will need the help of government and society, **Howley** said, and welfare policies are not the way to help these workers. Low-wage workers have little value in the open market and are in no position to push for higher wages because there are always others willing to take their jobs. By forcing welfare recipients into the labor market and subsidizing their employment, government weakens the position of low-wage workers. The influx of welfare recipients into the labor market will displace current low-wage workers, cause their wages to drop, or both. It would be better for low-wage workers if government worked to tighten the labor market and created public-sector jobs for welfare recipients.

Kaus believes there are some positive aspects of the new welfare law, but he said it also has the potential to create problems. On the positive side, decentralizing the system will make it easier for states to experiment with different programs and perhaps a number of successful models will be developed by the states. On the negative side, policies aimed at pushing welfare recipients into the private labor market are likely to displace other low-wage workers. These workers could be protected if public-sector jobs were created for welfare recipients. And if these jobs paid less, as they do in some states, welfare recipients would be encouraged to eventually move into the private market without the government's having to pay employer subsidies to get them there.

The new welfare system is a step in the right direction, but it does not go far enough toward moving welfare recipients into the workforce, **Levin-Waldman** argued. Employers are reluctant to hire them because of the stigma associated with being on welfare. Welfare-to-work programs should be merged with other unemployment assistance programs. If welfare recipients were treated the same as other unemployed, they would likely have an easier time finding employment.

A bright spot in the welfare-to-work debate is that it might cause policymakers to address the bigger problem of low-wage labor, **McGahey** said. Although the overall unemployment rate is low, it remains high among inner-city workers. And this is where many welfare recipients live. Moving welfare recipients into the workforce will require that policymakers address broader macroeconomic policies. What is needed are policies that promote economic growth and job expansion. In addition, policy should focus on creating intermediaries between the unemployed

and potential employers. Welfare recipients and other unemployed need help with such things as transportation, child care, work skills, and job matching.

Van Erden noted that lost in the discussion regarding welfare-to-work is the fact that many successful programs are already in place. A number of corporations already actively recruit welfare recipients and other unemployed, and many local governments have programs aimed at developing their local workforce and expanding employment opportunities. But if these, and new programs in the works, are to be successful, links must be developed between the business community and the governments operating work programs. The business community needs to be involved in the process and make its needs known, and policymakers need to better understand how business works. Welfare-to-work programs are most successful when the private and public sectors work together.

Session III: The Labor Market Effects of Institutional and Structural Change

Moderator for this session was **Michael Mandel**, *Business Week* economics editor. Participants were **Barry Bluestone**, Levy Institute research associate and **Frank L. Boyden** Professor of Political Economy at the University of Massachusetts Boston (a joint presentation with **Stephen Rose**, Educational Testing Service); **Anthony P. Carnevale**, vice president for public leadership at the Educational Testing Service; **Judith Fields**, Levy Institute research associate (reporting on a joint study with Research Associate **Edward N. Wolff**); and **Richard K. Vedder**, Distinguished Professor of Economics at Ohio State University.

According to economic theory, when the unemployment rate drops, the labor market tightens and this leads to wage pressure and inflation. But there does not appear to be any wage pressure in the United States even though the unemployment rate has dropped to 4.9 percent. **Bluestone** and **Rose's** explanation for this phenomenon is that Americans are working more hours than in the past. Because they know that no job is secure, American workers work extra hours when they can in order to maintain their lifestyle and save for periods of unemployment. This willingness of current employees to increase their work hours means the supply of available labor is greater than the unemployment rate indicates. If we are going to use labor supply as an indicator of wage pressure, we should measure hours worked rather than the number of people employed. Measuring hours worked also helps explain income disparities. Many people with high incomes have those incomes not because they are getting paid more per hour, but because they are working more hours.

Carnevale said that technological advances, globalization, and a shift from a manufacturing- to a services-based economy are transforming the American economy and leaving many workers behind. Surviving in such an economy requires that workers be able to adapt to rapid change and this requires that they be well educated. Education and training programs are not inexpensive, and neither the states nor the federal government appears willing to allocate more

funds in this era of budget cutting. But if education and training are left in the hands of individuals, we will continue the current trend where the children of middle and higher-income families receive better and more education than the children of lower-income families. The challenge for policymakers is to develop an educational system that provides equal opportunity for all.

In a joint study **Wolff** and **Fields** found that often it is not the education and skill of workers that determine wages, but the industry in which the workers are employed. Industries that are profitable or experiencing job growth tend to pay higher wages to both male and female employees than do stagnant, less profitable industries. However, even in these industries women tend to earn less than men, although the gender wage gap is less. Women fare best, in terms of wage equality, in those industries most likely to be targeted for affirmative action compliance reviews. Paying equitable wages to women benefits not only female employees but also business. Industries that pay women equitable wages experience less employee turnover and higher profits.

The American economy has experienced tremendous structural change in recent years, **Vedder** said. Union strength has decreased, corporations have downsized their workforces, the service sector has grown while manufacturing has decreased, and more Americans have moved into professional and technical career fields. In addition, increased immigration has led many to wonder if immigration policies should be based on immigrant skills rather than family ties. Many economists view these structural changes as damaging to workers, but the changes have also opened new opportunities for many American workers.

Session IV: Employment Policies for Urban America

Executive Director **Dimitri B. Papadimitriou** moderated this session. Participants were **Paul Davidson**, holder of the Holly Chair of Excellence in Political Economy at the University of Tennessee; **Randall W. Eberts**, executive director of the W. E. Upjohn Institute for Employment Research; and **Margaret C. Simms**, vice president for research at the Joint Center for Political and Economic Studies.

There are a number of reasons for unemployment and one is a shortage of jobs, **Davidson** said. Solving the unemployment problem will require policies aimed at increasing productivity in order to create more jobs. But many of the tools commonly used to increase productivity, such as reducing interest rates and increasing exports, create problems with trading partners. A better solution is to focus on the system of international capital flows. It might be better for many nations to move away from flexible exchange rates and return to fixed rates.

Inner-city residents face many barriers to employment, **Eberts** said. One is that while there may

be jobs in a metropolitan region, inner-city residents often lack the transportation to reach those jobs. Another problem is that inner-city residents, who are often African American, are socially isolated and thus lack the connections that will get them good jobs. One solution to the problem might be to encourage the growth of African American businesses in the inner city. While this would not entirely solve the unemployment problem, it would provide some jobs for inner-city residents. But perhaps more importantly, African American-owned businesses not only would provide their owners with economic self-sufficiency, but they would also serve as a stabilizing force in inner-city neighborhoods.

Simms presented findings of a study on minority-owned businesses that sought to learn if such firms grow in terms of revenue and number of employees and also whom they hire. The goal of the study was to learn what benefits could be obtained by encouraging the start-up and growth of minority-owned businesses. The results of the study indicate that minority-owned businesses not only are quite successful in terms of growth, but they also are important employers for minorities. Minority-owned firms are more likely to recruit workers from low-income neighborhoods than are nonminority-owned firms, regardless of whether the firms themselves are located in the inner or outer part of a city.

Session V: Perspectives on a Policy Agenda for Employment and Economic Growth

The moderator for this session was **Susan Dentzer**, contributing editor at *U.S. News & World Report*. Participants were **Lawrence Chimerine**, managing director and chief economist at the Economic Strategy Institute; **Alan Reynolds**, senior fellow and director of economic research at the Hudson Institute; **David A. Smith**, director of the Public Policy Department at the AFL-CIO; **Lonnie P. Taylor**, vice president for congressional affairs at the U.S. Chamber of Commerce; and Congressman **Maurice D. Hinchey** (D-New York).

Chimerine took issue with those who say major policy changes are needed to increase American economic productivity. With the exception of the post-World War II era, which is unique, there is nothing in America's economic past that should lead us to believe we can have annual economic growth of 5 percent or more. The current economic growth rate is not that bad. However, Chimerine admitted it could be slightly better. And the way to make it better is not by cutting taxes to stimulate investment. It is not more investment that is needed but better investment. Both public and private investments should focus on long-term job creation, not short-term payoffs for investors.

According to **Reynolds**, if in the next few decades the labor force in the United States grows more slowly than the economy, the country could face a serious labor shortage. To avoid this problem, more workers, especially women and older workers, must be enticed into the labor market. Many married women stay out of the labor market because their wages are taxed at their husband's higher tax rate. Older workers stay out of the labor market to avoid higher tax rates on

Social Security benefits. To keep women and older workers in the labor market, the tax system must be changed. Others could be lured into the labor market if wages were increased. Immigrants are another important source of labor. But if immigrants are to help solve the labor shortage problem, immigration policy must be based on skill not family ties.

The global economy is making life difficult for many American workers and the United States needs to address this issue, **Smith** said. There are a number of things policymakers can do to help American workers. First, the Federal Reserve should let the economy grow and the unemployment rate fall. Second, the United States needs to address the problem of job exports. Trade policies could be used to encourage other nations to raise the living standard of their workers. This would help American workers who now compete with low-wage workers in other nations. Third, on the home front, American policy should strengthen the bargaining position of American workers and increase investment in programs that promote economic growth.

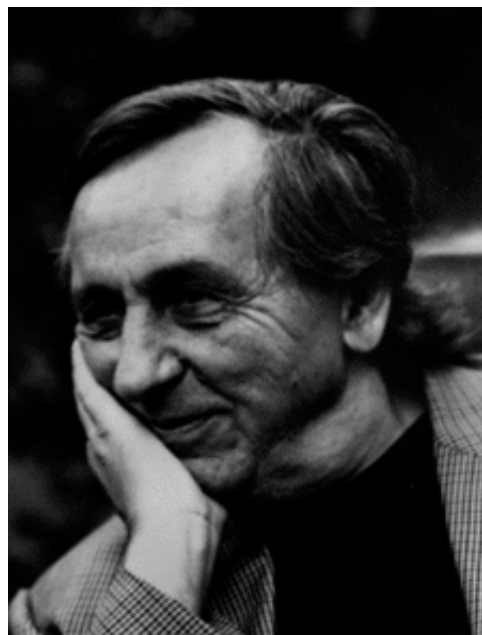
Taylor said the key to economic growth is increased productivity, and policies aimed at increasing productivity should focus on small businesses. Small businesses account for more than 54 percent of American jobs and over half of the gross domestic product. Among policies that would benefit small businesses are a reduction in the capital gains tax and reform of estate and gift taxes. In addition, if government reduced its spending, it could afford to reduce overall taxes, which would benefit businesses and increase productivity. Regulatory reform would also help businesses by reducing their compliance costs. Finally, export promotion policies would help businesses to expand and create more jobs.

The American economy is booming and the growth results from a reduction in the budget deficit, **Hinchey** said. The deficit, as a percent of gross domestic product, is now below 1 percent. Thus, it is no longer America's top economic problem. The problem is that the wealth created by this economic growth has not been evenly distributed. There is tremendous income inequality in America and policymakers are failing to address that issue. In order to help those at the lower end of the income ladder, the economy must continue to grow so that unemployment will drop. But a major obstacle to increasing the rate of economic growth is the Federal Reserve, which pursues policies aimed at slowing the economy to keep the unemployment rate from dropping further. Also a threat to increased economic growth is the failure of the United States to invest in the infrastructure, research, and educational programs needed to sustain the economy. American trade policy is also failing to promote growth because it allows trading partners to block American products from their domestic markets.

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The Levy Report Interview

William Greider Discusses Contradictions in the Global Economic System, Corporate Responsibility, and Progressive Policy



William Greider

William Greider, author and national editor of *Rolling Stone* magazine, has received both praise and criticism for his years of portraying looming economic crises for his readers. His most recent book, *One World, Ready or Not: The Manic Logic of Global Capitalism*, documents the unintended and often casually dismissed effects of the worldwide flow of capital. Greider warns that the rising influence of the business and financial communities has forced issues such as workers' rights and environmental standards to the background. Greider discussed themes from his new book and other topics with Assistant Director Sanjay Mongia on June 16, 1997. Excerpts of their conversation follow.

Mongia: You write in your new book that at the core of economic instability is global overcapacity in labor, production, and capital. How do you respond to critics who believe that these temporary imbalances of supply and demand are self-correcting and that market forces left to their own devices will adjust?

Greider: Classical economists always leave out the fun part of that "adjustment" in which millions of people lose their livelihood, countries lose chunks of their industrial base, and firms go belly up or are forced to merge with other firms. They use the word adjustment as a euphemism to brush that process aside, but most people, and most firms, regard that process as what matters most. If you look at a sector like automobiles, firms, especially American firms, have made those adjustments for the last 15 or 20 years--sometimes quite brilliantly--yet the gap between capacity and demand keeps getting wider and wider. And that happens not because the managers are stupid, but because the forces at work in globalization drive them and their competitors to keep building more factories, to keep modernizing production, etc., etc. Of all the arguments in my book, this is the one I am most confident people will see. About a month

ago *The Economist* ran a piece on this phenomenon and attributed it to the same forces. It didn't say this is the end of the world, and neither do I. But, unlike the average *Economist* piece, which says everything is going to be OK and all we need is more trade liberalization, it ended on a fairly dark note.

Mongia: But even those who concede that there is a human toll may have prescriptions different from yours. Free market advocates suggest that the proper role for policy is to facilitate transitions for workers and communities that are affected by market forces in a global economy. What's wrong with limiting government to serving as a buffer against the effects of market forces?

Greider: Is that what the Japanese government does? Or the Chinese government? Or the Indonesian or Indian or Brazilian? The trouble with the Milton Friedman view of reality is that it's absolutely blind to reality. So what we have is a process in which the United States, out of its supposed economic principles, argues for trade liberalization and anything that will stimulate export growth, while other nations (not all but many of them) are targeting shares of the global industrial base. I don't criticize those governments for doing that; they understand the game better than we do. The real question is, Does it matter if the United States loses major manufacturing sectors like autos, aircraft, semiconductors, telecommunications equipment? The classical economists say it doesn't matter, and I say that's crazy. Of course it matters.

Mongia: The American business community is betting on rising prosperity, increasing purchasing power, and rising demand in developing countries, such as China and India. Won't such conditions absorb the excess global capacity that you cite, and won't trade barriers and protectionist policies against these countries exacerbate global overcapacity by impeding their progress?

Greider: I'm not arguing for protectionist policies against the poor countries or even for simple tariffs to protect domestic industries. That's a retrograde approach. What I am arguing for is that rich and poor recognize their common interest in supporting demand and in doing so with growth policies, pulling up the bottom in wages, tax policies, and lots of other measures. If they don't attend to that, they're all going to go down together. That's not a nationalistic, protectionist perspective. Quite the contrary. I'm trying to describe a positive and progressive global perspective to save the whole system from its own contradictions. Where we are now is that most learned commentators, very much as in 1920, deny the existence of those contradictions. I think it's dangerous to just let things play out according to the present dynamics.

Mongia: You propose global standards for labor rights, environmental principles, and tax policies. Is it possible to adopt and implement global standards given sharp differences in business practices, cultural norms, and economic conditions?

Greider: That's the orthodox explanation of why we should be passing. I turn it around and ask if that's the case, why are you using all of your political muscle to insist upon "a rule of law" in

countries like China, Indonesia, and Malaysia. The rule of law that the multinational companies are insisting upon affects rights. Why isn't that as intrusive as insisting on labor laws? And, of course, it will be extremely difficult to get a consensus, but the fact that it's difficult doesn't make it wrong.

Mongia: You have said that the rich countries' belief that they are the only players that count is "an arrogant assumption." Is it not equally arrogant to insist that poor countries adhere to western or American cultural standards pertaining to workers and the environment?

Greider: Those who argue that we shouldn't impose western standards are being hypocritical in that they don't condemn western demands in areas such as intellectual property rights. Labor rights are fundamentally a contract right and in law not different from the right of any business contract. You're selling something and I'm buying something and we've got a contractual agreement on the terms of that transaction. Do workers have the right to enter into such a contract or don't they?

Mongia: There are critics who suggest that your prescriptions might contribute to a recurrence of 1929. How do you reassure those who fear that trade restrictions or punitive measures are a precursor to another round of Smoot-Hawley legislation and the massive global contraction of economic activity that led to the Great Depression?

Greider: We already have a risk of isolationism and protectionism, and it's being expressed in the political backlash against globalization. I'm arguing that if you want to avoid that outcome, you need to respond not just to the losers in the system, who are multiplying on both ends, but to the economic imbalances. If I'm correct that we're flirting with deflation and we do get a general deflationary pattern, you're damn right that countries are going to go protectionist, probably including this one. History tells us that's the way these things are dealt with in crisis. I'm arguing that we can avoid that cliff if we respond to these imbalances now. The only thing I propose that one could reasonably say is protectionist is the suggestion that we may need temporary emergency tariffs (which incidently are not prohibited by GATT) to correct the financial imbalances in the United States. Such measures are nonselective.

You have to conform to the rules as they exist; you have to declare we're in a financial imbalance here, we need to correct our trade deficits, and we're going to do that over maybe three to five years by imposing a general emergency tariff. I would go further and say you could even rebate the money to the developing countries. It's not about the money; it's about telling the rest of the trading system we can't go on like this or sooner or later the United States is going to tap out. Now, most orthodox opinion doesn't take that danger seriously. I suggest the economists and the American business community go read the history of Great Britain and see where that story ended. But even so, I do believe that if the United States, as the leader of the system, honestly put this question on the table and announced it was prepared to act, you wouldn't have to put those tariffs in place because every important trading partner, including Japan, would be at the table rather swiftly saying let's work this out.

Now, you have to make the threat credible. I think people got confused in the rhetoric of trade liberalization about where the leverage is. The leverage is in the market demand and this continues to be the biggest, most buoyant market in the world for selling stuff. That's a fact that gets overlooked. I'm not interested in provoking a crisis with China or even picking on China singularly, but it's a mistake to think that China has all the leverage. We could collapse the Chinese economy tomorrow if we wanted to. And the Chinese and everybody else need to understand that.

Mongia: You've said that we pay too much attention to China. Nevertheless, what conditions would you impose on China for extension of most favored nation trading status and membership in the World Trade Organization?

Greider: I think the MFN is such a nonmeaningful conditionality that I refuse to take it seriously. I think it is a mistake to demonize a country and then pick a fight with that country. I've believed that for years about Japan, and I believe it now about China. The ideal starting point is to articulate a set of problems that are perceived to be real and then propose solutions. If you look at what China is doing now--setting aside its peculiar Marxist-Leninist regime, history of repression, and other qualities I don't care for--it is doing what the global system permits a developing country to do. It is targeting certain industrial sectors; it is using its market leverage to gain shares of the industrial base of the United States, Germany, Japan, and other nations; it is controlling capital inflows; and so on. I think it's a hard case to make that Japan or China is uniquely malicious in the way it's doing these things. That's why I keep returning to a global system perspective. Can the system absorb a China, an India, a Brazil? If China were to disappear tomorrow, the scale of the problem would change, but the problem would not.

Mongia: "Corporate responsibility" entered the vernacular last year. How do you define corporate responsibility? Is it appropriate and possible to impose citizenship responsibilities on firms in a market economy?

Greider: Firms respond to market dynamics. I'm not painting them as evil greed heads. I'm just saying that as long as governments don't raise any objections or put any impediments in that path, firms will make those moves. I think I have more sympathy for the dilemmas confronting multinational corporations than a lot of the critics who say we need corporate responsibility. I don't think, for the most part, these companies act this way because their executives are immoral or indifferent to human suffering. The executives see as their first task to keep their company in the chase, and I think they believe they are creating a new and better world in the long run.

The issue is no longer about being a good American or German or Japanese company. The issue is that firms' collective behavior is leading to some sort of economic crisis. That ought to be the entry to discussing responsibility. But here's another point. I have seen companies doing lots of things that would offend their ideology, would certainly offend the ideology of free trade. Corporate managers on the whole are much more pragmatic than ideological. They do what the system tells them they can do and stop doing what the system won't allow them to do. So I'm

talking about building a new set of terms of trade that will point in the direction of important goals, such as equity and wages and faster growth.

Yes, the companies will oppose those terms because they see them as infringing on their freedom. But I think if you can get the politics in place to convince governments that this is necessary to do, the companies will do fine under the new rules. I'm not trying to put them out of business or even to stop globalization. We've had a warning signal from the voters of France and other countries; the people are choking on this process. Now you can attend to these warning signals or blow your way past them. I don't know which Europe is going to do, but I think in the U.S. the longer you ignore the real consequences, the more you're feeding reactionary protectionist politics. I think that's unnecessary. I know my critics don't believe this, but I really am making an argument to save the system from its own contradictions.

Mongia: A recent article labeled you the "Upton Sinclair of our times," a modern-day muckraker "with the vision and courage to take on powerful issues and even more powerful interests." What in the current political and economic framework makes you optimistic that we will witness the types of global social reform that you endorse?

Greider: My optimism is tempered by a pretty clear grasp of political reality. I guess I have a residual faith in the capacity of people to confront their reality and deal with it, which doesn't mean there won't be a lot of confusion and hard knocks, but as I read history this is what always happens. Commerce and finance quite creatively (and I mean that sincerely) leap ahead of social consciousness, political consciousness, and they invent a new world with new possibilities. They do not deal with the instabilities that their new world creates for societies, with unemployment or a loss of industrial base or social dislocations. And so it falls to the rest of us to catch up--to begin to think clearly and to demand political action. If you listen to the market reformers, they're saying trust the marketplace; it will work all of these things out. But I think history makes it clear that's wrong. Markets cannot replace societies. We should have learned that from the 1920s and 1930s. In a situation of contradictions, people may opt for crazy solutions--not just protectionism, but a kind of fascism. That's what opened the way for the rise of Hitler; he was going to resolve all of this instability and all of these contradictions. I'm not predicting another Hitler; I'm just saying we're flirting with similar consequences.

Mongia: Another reason for tempered optimism may be the public disenchantment with the political process. Americans have never had blind faith in government, but there now seems to be a heightened hostility. Is this increasing disconnection irreversible? Is there anything society can do to make government more responsive?

Greider: I've made a series of assertions about the political condition in this country and the economics surrounding it. If any of them are right (and feedback I get from ordinary people seems to confirm them), why doesn't anybody in politics ever say these things? I want to be fair to politicians; some do, of course. But you can go into almost any region of the country and hear the people saying that government officials hate to tell the truth about things--about the economy,

the corruption of Washington, the disregard the governing elites have for the people, and I happen to agree with them. The hostility will be reversed when those who have governing authority begin telling the truth about these things. That's the risk of leadership. There's nothing new in that. The alternative is to go on the way we've been going. I'll give you an example. At a dinner last week a ranking official at the Commerce Department in inter-national trade said, "Of course trade liberalization depresses wages in this country." I said, "Wait a minute. That's not what you've fed to the people. You've denied that." He shrugged and said, "Well, I can't say that in public, but we all know it's true."

We now have a weakened and unstable national political leadership. Both parties are in disrepute, this president is weak, the president before him was weak, and you get eccentric challengers like Ross Perot, Steve Forbes, and Pat Buchanan. That's going to continue until one or both major parties begin speaking more directly to the reality that people experience. And until that happens, confidence is going to be at a low ebb.

I'm on the side of whoever is trying one way or another to educate people and help them think clearly about these things and agitate. I'm not partisan. I can imagine a Republican or a Democrat or a third party standing up to do this. In the history of America it has often fallen to a third party to articulate a new reality and to do it so forcefully that one of the major parties has to say, hey, we'd better get on board. That's where the people are now. I can't tell you how this is going to happen, but it's going to be a big fight, and I'm on the side of those who are challenging the orthodox. The orthodox view is not only unfair to people but mistaken for the country.

Mongia: What are the prospects for a progressive renaissance, and what can progressives do to restore credibility to their ideas?

Greider: Who are the progressives? Are they the people who used to call themselves liberals? There are different strands. The populists of the 1890s and the progressives of the early 1900s brought about some worthy reforms, but they basically believed that well-intentioned managers can work things out and make everything run better for the society. I'm of another school, one that believes that there is a much deeper conflict and, of course, it's about class and it's about income.

One of the things that changed in America in the early twentieth century was that after 20 or 30 years the great waves of immigrants became competent enough to assert themselves intellectually and politically. They started in the election of 1928 and prevailed in the election of 1932, that is, their guy got elected. Now, I don't want to see the ruination of economic dislocation, to wait for a depression to stimulate that kind of political change, but I believe (and this is going to sound romantic to your readers) that America will get back to what it can be when the working class gets its act together. I mean across racial lines, across religious lines. I'm talking about Mexicans and Puerto Ricans and blacks and lots of poor whites. We have a great divide within the working class itself, which is tough to bridge but not impossible. If you can get these people to see politics as a place where they can be effective, they can change the country.

Most of your readers may think that there isn't a working class anymore or that it doesn't count. Surprise! The working class is still there and it's as large as it ever was. It's just been banished by the rhetoric of our politics.

I've been telling politicians for some years to start talking about the working class again and see what kind of response they get. Most of them say, "I can't do that. I'll sound like a lefty." But I tell them they won't; 45 percent of the population identify themselves as working class, which is about the same number who identify themselves as middle class.

Mongia: Has the working class been marginalized or did it voluntarily disengage because it had lost faith in the system?

Greider: Both. A lot of working class people who live in the suburbs now may or may not vote Republican, but they feel that they don't need the Democratic Party anymore and that the Democratic Party has somehow turned away from them. I think this is particularly true of working class people, but it's true of others as well. When you're feeling a lot of pressure, it's a natural human response to try to take care of your own--your family, your community, your hearth and home. I'm trying to coax people out of that response and convince them that it is insufficient to the situation. They've got to reengage in a larger politics.

Many people feel that if you just reform campaign finance or a few other things, the system is going to be whole again. I don't believe that. I think it's going to be much tougher. It's going to be a struggle, and I'm not Pollyannish about it. I'm not the only person saying this. There are lots of people around the country trying to recreate the social base for a progressive policy.

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Editorial

Mend It, Don't End It: A Case for a Skill-Based Immigration Policy

by Sanjay Mongia

Assistant Director, The Jerome Levy Economics Institute



Congress remains entangled in a myopic debate over welfare eligibility for legal immigrants. This debate amounts to a political red herring and avoids tackling the more pressing issue--the need to reform the United States's legal immigration policy. If lawmakers



Sanjay Mongia

are concerned about immigrants' becoming a public charge, they should forsake scapegoating legal immigrants through a thinly veiled and ill-conceived effort to reduce welfare spending. Rather, it would be far more responsible for public officials to rethink the number of immigrants our country can absorb and the criteria for the selection of prospective immigrants. Sound policy could balance America's humanitarian commitment to immigration with our national interest in promoting economic competitiveness and protecting the indigenous population. Such a policy would require greater emphasis on skill and education criteria and a modest reduction in the overall number of immigrants through a limited reform of the family reunification policy.

This is not to say that immigration has not yielded benefits for our country. Indeed, immigrants have given us a richer, more diverse culture and have made significant contributions to our science and engineering talent pool. A recent report by the National Academy of Sciences claims that immigration may offer modest benefits for the national economy. But a careful reading of the report would lead one to interpret its findings as both a testament to the value of immigration and a blueprint for legal immigration policy reform. The truth of the matter is that economists have struggled with the notion of marginal cost, which may better explain the fiscal impact of immigration. After all, if we take the finding of the report to its logical conclusion, we would expect that increasing the number of legal immigrants 10-fold (to 8 million) would yield 10 times the current net economic gain of immigration. That is an obvious fallacy--no one is endorsing an open border policy, which reflects healthy skepticism about the ability to gauge aggregate costs and benefits associated with immigration. Granted, the evidence on total public costs is inconclusive, but there is general agreement that the geographical concentration of immigrants implies that an uneven share of the revenues generated by immigration flows to Washington, while a large fiscal burden falls on select states.

The report concedes that states with high immigration populations bear a fiscal burden due to immigration. Our country annually admits about 800,000 legal immigrants, with 80 percent of the admissions determined by family reunification preferences. An estimated 75 percent of legal immigrants are concentrated in just six states. The report also confirms that low-skill and less-educated American workers suffer adverse employment and wage effects, particularly in labor markets with high concentrations of immigrants. Immigration may not have precipitated the declining prospects for these workers, but it certainly has accelerated their downward spiral.

Although 23 percent of immigrants who came to the United States during the 1990s have college degrees, more than 41 percent are high school dropouts. Immigration accounts for about 40 percent of labor force growth. Economists generally agree that an increase in immigration of 10 percent reduces American wages by about 1 percent and that immigrants have a disproportionate impact on the low-skill end of the labor market. Between 1980 and 1988 immigrants increased the number of high school dropouts in the workforce by roughly 25

percent. Not coincidentally, the wages of high school dropouts declined by 9.5 percent during this period, and research by George Borjas of Harvard University indicates that immigration may be responsible for approximately one-third of the wage drop. Immigration is contributing to the deteriorating condition of America's poor and unskilled.

The poor and most unskilled members of the indigenous population (representing minorities disproportionately) already find it difficult to obtain employment, and this condition is aggravated by an immigration policy that permits entry based not on skill levels or labor market needs but on family reunification. The result is predictable--a displacement of job seekers who are predominantly inner-city African Americans, who are mired in double-digit unemployment and typically do not have access to a network of family sponsors and employers in the low-end labor market.

Lacking the will and wisdom to make legal immigration policy more consistent with labor market needs, Congress crafted and the president signed a "welfare reform" bill that punishes legal immigrants. Architects of the new welfare law's punitive measures against legal immigrants contend that family sponsors, not taxpayers, should be the first line of assistance for new immigrants. At the same time, supporters of the current immigration policy--which allows an unmitigated flow of less-educated and low-skilled immigrants (who typically come from poorer families and have dim prospects for immediate self-reliance)--invite harsh attacks against the very immigrants they welcome to our country.

If one believes that immigrants are a public charge and that sponsors should bear more responsibility for family members admitted to the United States, then a rational policy to curb public expenditures would involve curtailing immigration levels by modifying the family reunification system and placing greater emphasis on skills criteria in the selection process. Such a policy would also offer modest protection to the indigenous at-risk population by slowing the growth of the low-end labor force--which will be augmented by the transition of several hundred thousand less-skilled women from welfare to work. A public policy that fails to amend legal immigration policy and denies legal immigrants access to public assistance is not sound. It neither reduces the import of unskilled workers nor promotes fairness in our immigration policy.

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New Working Papers

Do States Optimize? Public Capital and Economic Growth

Working Paper No. 189

Output and Employment Effects of Public Capital

Working Paper No. 190

Dynamic Output and Employment Effects of Public Capital

Working Paper No. 191

In a series of three working papers Visiting Scholar **David Alan Aschauer** presents findings that indicate investments in public infrastructure can yield long-term economic benefits. These findings, however, do not imply that any investment in public infrastructure will increase economic growth. Aschauer finds not only that some investments are more beneficial than others, but also that too much investment in public infrastructure can actually decrease economic growth. These findings resulted from an analysis of data from the 48 contiguous states from 1970 to 1990.

In **Working Paper No. 189**, Aschauer combines the data with a model of an economy with productive public capital. The data and model are used to investigate the relationship between public capital, productivity, and economic growth in an endogenous growth setting. Economic growth is measured by the growth in output per worker. Aschauer finds that an increase in public capital investment results in an increase in economic growth and suggests that an insufficient investment in public capital may be the reason why some states have experienced slow economic growth in recent decades. States might also be spending too much or spending inefficiently. When states spend beyond a certain level, economic growth decreases. Investments in core public capital--streets and highways, water and sewer systems--provide the greatest returns in economic growth.

In **Working Paper No. 190**, Aschauer returns to the link between state spending and economic growth and finds that a reduction in spending by all states in the study would increase economic growth. Most states underinvest in public capital, but overspend in other ways. When states increase their debt or increase revenue by raising taxes, economic growth decreases. This does not mean, however, that states should avoid taking on debt to finance public infrastructure. The economic benefits of an increased investment in capital, especially core infrastructure, can help offset the negative effects of taking on more debt. There is, however, a level at which investment in public capital can be counterproductive. Aschauer finds that the public capital stock is most beneficial when it is between 50 and 70 percent of the private capital stock. Anything higher tends to cause a decrease in economic growth.

In **Working Paper No. 191**, Aschauer expands his research to consider the long-term effects of public capital investment on the economy. He begins by developing a dynamic model that relates output and employment growth to public capital, initial output, and initial employment. The model focuses on the relationship between output and employment as the economy changes over time. Data from the two previous working papers are used with the model. The results indicate that investments in public capital lead to long-term benefits in economic growth.

However, the benefits vary depending on whether the labor force used with the model is endogenous or exogenous. Since the migration of labor changes the results from the model, Aschauer suggests that further research into the benefits of public capital should consider the effects of labor migration. In addition, he suggests that more attention should be paid to the methods by which public infrastructure is financed. His research indicates that public capital financed by federal grants leads to significant increases in output at the state level.

Social Security: The Challenge of Financing the Baby Boom's Retirement

Walter M. Cadette
Working Paper No. 192

In a recently released report, members of the Advisory Council on Social Security offered essentially two alternative approaches for ensuring the financial future of the Social Security system. One would keep the system much as it is, with relatively small adjustments in benefit and taxation levels. The other would privatize it, requiring individuals to invest a portion of their payroll taxes in individual accounts. In an examination of these proposals Senior Fellow Walter M. Cadette provides the background information needed to understand the arguments made by supporters of each option. He concludes that the better approach would be to alter the current system rather than abandon it for a privatized system.

Those who support maintaining the current system have proposed that benefits be reduced and taxes on benefits increased. They also propose that policymakers consider the investment of up to 40 percent of Social Security reserves in the stock market in the belief the market will provide higher returns than the special-issue Treasuries in which Social Security funds are currently invested. The privatization alternative would require that workers dedicate five percentage points of the current 12.4 percent Social Security payroll tax rate on covered earnings (this year, a maximum of \$65,400) to individually managed personal security accounts. Although such investment would operate under government strictures (regulating, for example, withdrawal of funds before retirement age), the privatized assets would be owned by the individual and could therefore be passed on to heirs.

Cadette concludes that the Social Security system can be put on sound financial footing for decades to come with relatively minor changes in tax rates or benefits formulas. Radical revamping of Social Security is not needed to right the system's long-term financial problems. Privatization is a poor substitute for the benefit Social Security has offered the nation since the 1930s: a guaranteed base level of income support for virtually all retiring workers, 50 percent of whom have no "private" pension. By tying retirement benefits to a worker's own investments,

privatization would circumscribe the capacity of the system to provide benefits to low-income retirees.

If the decision is to keep Social Security much as it is today, additional tax incentives to promote saving are in order. They would make for faster growth of the capital stock and productivity and thus ease the transfer of income from a relatively small to a relatively large generation. There are, after all, ways to raise national saving other than through the added taxation that privatization would require. From the narrow perspective of Social Security itself, saving incentives would help to soften the inevitably unpopular measures that will be needed to correct its long-term financial imbalance.

And unpopular these measures are likely to be. A reduction in benefits or increase in taxes, even if just over 2 percent of taxable payroll, will require difficult and explicit trade-offs. And hard decisions will also have to be made if policymakers attempt to improve the equity and efficiency of the system, which also are in need of repair.

The challenge for the government is to achieve financial security for the system while maintaining its popularity and meeting other obligations. Support of the elderly and near-elderly under Social Security and public health care programs already requires a tax rate approaching 10 percent of gross domestic product. Any increase in that percentage will make it more difficult for the government to finance its other obligations.

The Impact of Declining Union Membership on Voter Participation among Democrats

Oren M. Levin-Waldman
Working Paper No. 193

In 1994 the Republicans gained control of the House of Representatives for the first time in 40 years. This victory led a number of political observers to conclude that American voters were abandoning the Democratic Party in favor of the Republican--a phenomenon often referred to as party realignment. Resident Scholar Oren M. Levin-Waldman challenges this conclusion. Using data from the National Election Studies for the years 1952 to 1992, he finds that while voters have left the Democratic Party, not all are going to the Republican Party. Some have become independents, while others have simply stopped voting. Levin-Waldman argues that the Republicans' 1994 victory was not due to the changing of parties by Democrats, but rather to declining union membership that has weakened the Democratic Party.

Union members are more likely to vote than non-union workers, and they are more likely to be Democrats than Republicans. With the decline of unions, the Democratic Party has lost a large block of voters. And the Democrats cannot count on the support of the growing number of independent voters. Based on the research, Levin-Waldman concludes that independents are less likely to vote than either Republicans or Democrats. Americans are not shifting to the Republican Party in large numbers, as realignment theory suggests. Rather, Americans are dropping out of the political process.

Levin-Waldman sees a danger in this situation. As union membership and political participation on the part of union members declines, big business and other powerful economic interests gain more influence over public policy. This allows them to use public policy to benefit themselves at the expense of workers. This control that wealthier economic interests have over policy might also be a reason for the increased income inequality in the United States. It might be necessary for government to protect the position of workers and strengthen unions if we hope to solve the growing problem of income inequality in America.

The Working Poor: Lousy Jobs or Lazy Workers?

Marlene Kim
Working Paper No. 194

Most Americans believe that if one works hard, one should not be poor. But in this study of the working poor, Visiting Scholar Marlene Kim finds that this is not always true. She used data from the 1994 March *Current Population Survey* to determine if working more hours would lift the working poor out of poverty. Based on that research, Kim concludes that while some of the working poor could get out of poverty by working more hours, the majority would still be in poverty even if they worked 40 hours a week every week of the year. Moreover, many working poor cannot work full-time.

Researchers of poverty have long disagreed on why people are poor. One side in the debate argues people are poor because they do not work enough. The other side argues people are poor because they cannot find jobs or the jobs they do find do not pay enough to lift them out of poverty. Kim's finding has important policy implications. If it is true that full-time work will not lift the working poor out of poverty, then policies that force the poor to work will not solve the problem of poverty. Some of the working poor could earn enough to rise above poverty if they worked full-time year-round, and perhaps these individuals should be encouraged to work more. But many working poor are not able to work full-time because they are either disabled or unable to find full employment, and many of these workers would not rise above the poverty line even if they could find full employment because the wages they earn are too low.

Because of the difficulty many people face in working their way out of poverty, government policies aimed at supporting the working poor are still needed. These workers need government assistance during periods of unemployment, and they need education and training programs to help them find better-paying, full-time jobs. Also helpful to the working poor are policies that increase employment opportunities for low-skill workers; tax policies, such as the earned income tax credit, that raise their income level; and wage policies, such as the minimum wage, that increase their earnings. Upcoming Symposium on Immigration.

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