INDUSTRIAL STRUCTURE AND EMPLOYMENT: SOME PROBLEMS AND POLICY OPTIONS

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If aggregate monetary/fiscal policy is inadequate to deal with unemployment, unutilized plant and equipment, low productivity growth, stagflation, and related problems, what policy options and approaches should be considered? Do we need reindustrialization or an industrial restructuring program?

INDUSTRIAL STRUCTURE AND EMPLOYMENT POLICY

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National industrial policy is likely to be a "hot" topic in the 1984 election. The interest in industrial policy arises from a dissatisfaction with the performance of the U.S. economy and realization that we are losing out in worldwide industrial competition. The increasing exposure of a large part of our industry to international competition and the internationalization of the monetary system creates an impression and reality of vulnerability. Some see industrial policy as the means to get back on top and to better control our economic destiny.

Fundamentally the debate over industrial policy is not new. It centers on the proper role of the government in the management of the economy. Those who favor a new industrial policy generally believe government should become more involved — although the degree and nature of proposed involvement varies. The extremes range from proposals for active intervention and participation in economic planning and decision making, with emphasis on investment and protection of jobs, to tax policies to stimulate research and exports.

Opponents to the notion of an industrial policy see it as central planning and the substitution of bureaucratic decision making and control for the freedom of the market. Their argument is that we now

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have too much government involvement and that economic performance would improve with less regulation and taxes.

The U.S. economy is in transition, but that is not a new phenomenon. A dynamic economy always has adjustment problems, including technological displacement. Part of the recent problem may be that we have had technological displacement without increased output, partly due to international competition and a prolonged recession.

If we can step back from the ideological argument and look pragmatically at generally accepted economic objectives, at our current status in respect to these objectives, and at some specific policies intended to promote the achievement of the objectives, perhaps a bit of light can be generated. That at least is the intention of this brief paper. While there are clearly many objectives of economic policy, I focus on full employment and productivity with justice.

An effective industrial policy must deal with employment, productivity, and justice. Full employment promotes productivity. Adoption of new technology creates the potential for improved levels of living but also creates losers. Potential losers will naturally protect their interests. An equitable distribution of the benefits will facilitate productivity as well as contribute to our national goal of justice.

Another section deals with equity issues when it considers policies in regard to human services, thus I will focus on productivity and employment, leaving equity for the other discussions except where it is directly related to employment policy. However, I cannot refrain from commenting that the latest information has 15 percent of the population living below the poverty level. A large part of our output is the product of an inherited technology and the way we share this inheritance is a major policy issue.

The goal of monetary stability might also be included, for inflation has been and will continue to be a major economic problem. I prefer to consider it as an important instrumental goal because it affects productivity, employment, and justice.

I will briefly remind you of how the U.S. economy is doing in respect to employment and productivity growth and then offer a few ideas about possible components of an industrial and employment policy.

EMPLOYMENT

More than 11 million (10 percent) American workers were officially unemployed in May of 1983; nearly two million more are believed to have become discouraged and dropped out of the job search, and 5.6 million involuntarily worked less than full time. In 1982 more than 26 million people were officially unemployed at least part of the year. Less than half the unemployed received unemployment compensation. Based on demographic data we can expect about 1.5 million additional people to enter the job market each year for the next five years. Current unemployment and the generation of new jobs in the next five years is clearly a major problem.

Disparity in employment opportunities is illustrated by different unemployment rates among groups and in wage differentials. In May of 1983 unemployment rates were 9.6 percent for adult men, 8.5 percent adult women, 23 percent teenagers, 47 percent black teenagers, 20.6 percent black workers, and 8.9 percent white workers. Unemployment in Detroit was above 17 percent. Unemployment among black youth in Detroit is reported as above 60 percent. There are many people now in their late 20s who are still seeking their first legitimate job.

Average hourly wages for a few industries illustrate the disparity in wages: malt beverages $13.82; soft drinks $7.64; steel $12.76; motor vehicles $11.98; all manufacturing $8.77; textile mills $6.14; and retail trade $5.69 (13, p.4). In addition, according to Thurow (12), it is not uncommon for the wage of the highest paid people in a skill category to receive four times the wage of the lowest paid in the same category. Such differentials persist over long periods.

While unemployment has been at a post WWII high, total employment is only 1.9 million below the all-time high and the employment rate (percent of population over 16 years old who are employed) is about equal to the average for the post WWII period. In 1982 the civilian labor force participation was about 64 percent compared to 58.3 percent in 1947.

The male participation rate was 76.6 percent in 1982 compared to 86.4 percent in 1947, while participation by women increased from 31.8 percent in 1947 to 52.6 percent in 1982 (6). We seem to be in the process of a major shift in the composition of employment opportunities which have very unequal impacts. The increased labor force participation has greatly increased the need for creation of new jobs.

While manufacturing has remained about the same percentage of the GNP since 1950 (about 24 percent) the percentage of employment in manufacturing has declined from about 34 percent to about 20 percent (6). There has been a radical shift of employment from goods production to services. The need for physical labor in manufacturing has decreased. The trend continues. For example, in the spring of 1983 more than 200,000 workers were on indefinite layoff from the auto industry alone. Executives expect employment in the auto industry to decline even with substantial increases in production. The industry reports plans to revitalize (i.e., increase productivity) with multi-billion dollar investments the next five years. Robots can do many jobs better and cheaper than traditional workers.

Not only have people been underutilized, but so have plant and equipment. While the data on percent of capacity at which an industry operates are difficult to interpret they clearly indicate underutilization. Capacity rates for 1982 and early 1983 ran less than 70 percent for all industry, 40 percent for steel and 50 percent for autos and aircraft.

Productivity

Productivity is difficult to measure and indexes can be misleading. Nonetheless productivity indexes do give a general picture of an important measure of economic performance.

Except for a spurt in the productivity indexes in the past quarter, the indexes show recent poor performance. From 1945 to 1965 U.S. productivity growth was at an annual rate of about 3.2 percent. However, the U.S. had practically no productivity growth 1977-1982 and the index of industrial production in 1982 was below that of 1978. From 1960 to 1981 the rate of manufacturing productivity growth was more than twice as high in West Germany and France and more than five times as great in Japan as in the U.S. Many countries have developed modern manufacturing capacity and become competitive with the U.S. in areas we once dominated.

Policies To Promote Employment and Productivity

In this brief paper only a few of the many possible actions which might be taken can be discussed. Consider the following proposals.

1. Promoting Improved Management and Labor Practices

The presitigious Committee for Economic Development identifies a number of private actions by management and labor to promote productivity (3). These include raising productivity to a central goal of business; encouraging entrepreneurship, risk taking and constructive criticism by management; providing all employees with real financial and nonfinancial incentives to improve productivity; and closely monitor productivity performance of own firms and competitors to obtain information useful in managing to improve performance. In addition the committee suggested consideration of productivity gain sharing with workers, quality-circle programs, labor-management participation teams, improved employment-security programs and revised long-term management compensation plans.

Public policy can influence these management-labor practices through publicity, commissions, support of business education reform, tax code reforms, etc. But most importantly, industrial and labor leaders can do much in their mutual interests to improve productivity of U.S. industry by their private and public actions without big government programs.

2. Guaranteed Employment Via Wage Supplement

Start with a commitment to full employment. Many policies obviously influence the level of employment. However, if due to the structure of industry and labor markets, the lack of effective demand, high interest rates or whatever else, people who are willing and able to work are unable to find employment, it should be public policy to assure an opportunity for employment. What do the principle of equal opportunity and justice mean if the opportunity for employment is denied?

The right to employment is more than a right to income. Employment in our society brings status, a sense of self-worth, legitimate access to compensation, and a potential for personal development and progress.

Consider a direct solution of guaranteed employment through a wage supplement. Any certified employer would receive funding for 50 percent of the wage of any employee receiving less than a stipulated wage, say $7 per hour including benefits. Any citizen 18 or over or a high school graduate who is willing and able to work would be eligible to receive the supplement. This means that every person willing to and able to work would be guaranteed employment at no less than $3.50 an hour.

Many details of the program would have to be dealt with. Such as the most appropriate level of wage supplement; criteria for certification of employers; and employees use of the supplement for job training, technical training, or attending college. Special incentives could be created for state and local governments to employ workers to rebuild our infrastructure and provide other needed public services. This would be the safety net for the employable. Competition among employers would raise the wage above the minimum and would direct employment to the most useful purposes. The minimun wage, often cited as restricting employment of low skilled workers, would become obsolete.

While the problems of design, implementation and costs should not be minimized there are a number of advantages to a universal guaranteed employment wage supplement program. We have many unmet needs. The program would promote output rather than restrict it by paying people to work rather than to not work. It would make the U.S. more competitive in international markets. It is automatically countercyclical. It would dovetail with a number of other programs making them either more effective or less expensive. The wage supplement would likely be pro-competitive because it would be more likely to be used by small and new businesses than by large established ones.

There are many negative consequences of unemployment. For example, a study over a 16 year period by Brenner shows that associated with each 1 percent increase in joblessness there was a 4 percent rise in imprisonment, 5.7 percent in murders, 4.1 percent in suicides and 3.3 percent increase in mental hospital admissions (2, p.7).

3. Institute Indicative Planning

Consider instituting an indicative national economic planning board within the federal government but with representation from business and consumer interests. We have an aversion to economic planning based upon a warranted skepticism of government's ability to plan and a fear of inappropriate intervention in the economy. However, the government is already heavily involved. We have hundreds of tax incentives and disincentives, subsidies and transfer programs often working at cross purposes and all lacking coordination. We do not even coordinate monetary and fiscal policy.

A planning board should have the right and obligation to obtain and disseminate information to government agencies and businesses about the relevant structure and behavior of business and government including investment intentions, training, and impending technological adoptions. The board should give some guidance to investment in both plant and equipment and in training. The planning board would be advisory, that is planning would be indicative not imperative.

4. Pro-Competition Policies

Consider policies to promote competition in oligopolistic industries. One of the problems with some of the reindustrialization proposals is that they seem to be designed to protect firms from the discipline of competition. A good case can be made that the problems of the smokestack industries derive at least in part from the lack off effective competition over a long period of time, during which they failed to develop and adopt the most productive processes and also allowed labor costs to rise — making them high cost producers relative to foreign competition. Walter Adams (1, p.6), a specialist in the U.S. steel industry, refers to a mutual suicide pact between big labor and big business, validated by a permissive government dispensing selective bailouts and protections from international competition.

Vigorous antitrust enforcement and a requirement that any merger involving a large firm will be allowed only upon proof that it will contribute to competition are pro-competitive policies.

5. Price and Wage Regulation

A good case can be made that the structure of industrial and labor markets creates sticky wages and prices with an upward bias and that this results in stagflation. Given the structure of markets, monetary policy designed to curb inflation results in unemployment and slow growth. Okun (9) divides the economy into price auction markets which adjust readily and customer markets which do not. In customer markets — industrial goods and labor markets — adjustments take place in quantities produced rather than prices.

For example, last week U.S. steel manufacturers announced a 7 percent price increase for sheet and strip steel, even though plants were operating far below capacity. They simultaneously seek protection from imported steel. Also the communications workers settled a strike with a 16 percent wage increase over three years, even though a large number of the unemployed would be able and anxious to replace at least some of them at much lower wages. These markets do not behave like competitive markets. Since labor payments represent about 85 percent of the GNP, all theories and policies based upon the assumption that the competitive market describes the economy are seriously deficient.

Okun, among others, concludes that some kind of an incomes policy or price-wage regulation is necessary to avoid the very undesirable consequences of restrictive monetary policy needed to curb inflation.

In 1975 (11) at this conference I argued that the source of the stagflation problem was the structure of political and economic power and that more direct action by government than monetary and fiscal policy was required. Evidence since then reinforces that argument.

6. **Monetary-Fiscal Policy — Target Interest Rates and Increase Public Revenues** (5, pp. 66–78)

For a few years we believed that fine tuning the economy through aggregate monetary-fiscal actions would be all the industrial employment policy needed. That belief has been shattered. We do not understand the consequences of alternative policies. The structure of the economy limits the effectiveness of monetary policy. The world economy has changed. We cannot control the supply of money partly because of the huge quantity of Euro dollars beyond the control of the Federal Reserve. There are at least four competing macro theories (Keynesian, monetarist, rational expectations, neoKeynesian and perhaps supply side) with different prescriptions.

Thurow argues that all the macro theories assume the existence of competitive markets, which is counter factual, and that we have to go back to the drawing board and first develop a micro economic theory consistent with the way the economy works, especially in respect to industrial and labor markets and then develop a realistic macro theory. He further argues that following the prescriptions of existing macro theory is dangerous business (12).

Nonetheless monetary-fiscal policy is critical in achieving the employment-productivity goals and policy decisions must be made. It seems most reasonable for the Federal Reserve to target interest rates rather than the supply of money.

Reasonable and predictable interest rates would stimulate longer run investment and purchases of housing and durables. Also of critical importance, it would reduce the attraction of the U.S. money markets to foreign investors, resulting in reductions in the value of the over-valued dollar, thus making U.S. goods more competitive in world markets. Having a guaranteed employment program would reduce the pressure to have an expansive monetary policy to promote employment, making it easier to deal with inflationary pressures.

The issue of taxes and government spending is very difficult. Maintaining effective demand is important to employment and productivity. Large deficits probably increase inflationary expectations and interest rates, reducing needed long run investments and planning horizons. There is substantial need for revenues to pay for programs to meet commitments for justice and public investments important to future productivity and competitive capacity.

On balance a case can be made for increased public revenues. The type of taxes and their uses are of course of critical importance. A national value added tax to generate additional revenue deserves consideration. The use of value added taxes which are not applied to exports by some of our competitors probably give them an advantage in trade. In any case coordination of monetary and fiscal policies is needed and this is one of the objectives of establishing a national planning board.

7. Import Protection — Selective Tariffs and Subsidies

Does it make economic sense to close plants and accept unemployment because of an over-valued dollar? Paul McCracken writes that "Distortions responding to exchange rates dominated by financial flows may have already sounded the death knell of a liberal, open international trading system." (8, p.10).

Foreign competition may be the major source of competition needed to spur productivity in some U.S. industries. But there are good reasons to avoid the demise of basic industries such as steel and motor vehicles. Thus very selective protective measures or, more desirable, subsidies designed to directly contribute to productivity increasing investment seem reasonably consistent with our objectives. The problem is to use these measures without their being manipulated by interest groups and becoming a general practice of protection from competition.

8. Rebuild the American Infrastructure

Roads and bridges are crumbling. Sewers and water lines are leaking. The basic U.S. infrastructure, built at a time when real incomes were much lower than they are now, is seriously deteriorating. Productivity in the long run depends upon reliable transportation, water, and sanitation. The capacity to do the rebuilding is sitting idle. A long-range program designed to be countercyclical is suggested. Perhaps a national infrastructure development bank would be appropriate to facilitate long term credit to states and local governments.

9. Increased Public Investments in Research, Education, and Training

An advanced technological economy requires a large investment in education and research to keep the system moving and safe for the participants. Education is especially important for future productivity. Reform in both educational practice and in financing of education is an important productivity issue. At the same time employment and productivity objectives would be served by a major program to promote training for entry jobs and in retraining for existing and anticipated jobs.

It is wasteful and frustrating to train for non-existing jobs. Both West Germany and Japan do much better at this than the U.S. On-the-job training with commitment to future employment is effective. This could be combined with a wage subsidy program.

10. A Special Reindustrialization Credit System

The centerpiece of industrial policy for many advocates is a government sponsored credit institution designed to promote the most desirable industrial development. At least five bills in Congress seek reincarnation of something like the Reconstruction Finance Corporation (4, p.8E).

Representative Lundine, who has introduced one of these bills, and Murray Weidenbaum take opposite positions on this issue. Lundine argues that we need a development bank to generate the kind of "patient capital" required to foster innovative, new, and emerging enterprises and the huge reinvestments required to restore basic industry as world class competitors (7, pp. 16–21).

Weidenbaum (14, pp. 22–25) argues that the Reconstruction Finance Corporation was subject to favoritism, corruption, and waste and such a scheme would not increase total savings or investment. He argues that regulatory and tax reform, not government credit, is what is needed. A variation of the development bank are proposals to direct pension funds — a large part of our savings — to investments which would promote industrial development and employment in the U.S. The need for improved investment banking seems clear. The means for instituting it is not clear.

11. Regulate Uneconomic Competition Among States and Local Governments

A very uneconomic competition among states and local governments for plant locations has developed. Firms are given a variety of tax breaks, interest advantages, and other subsidies to locate in specific places. This does not increase total investment or economic activity. It does subsidize movement of location and creates more dislocation problems and equally important it creates unfair competition and may cause competitive firms to fail. Consider eliminating the use of any federal funds for this purpose and promotion of an agreement on reasonable guidelines for interstate and intercommunity competition for business locations. Industrial policy at the state level is frequently viewed as a program to subsidize location of industry in the state.

12. Many Other Policies Are Important

A great many additional specific policies, regulations, programs, taxes, subsidies, etc. influence productivity and employment. For example:

a. A rule that all union wage contracts expire on the same date would reduce the ratcheting effect of sequential bargaining which contributes to wage push inflation and disparity in wage rates.

b. Experience based unemployment compensation insurance discourages layoffs but also discourages hiring and increases costs to cyclical industries such as automobile manufacturing as they attempt to recover.

c. The tax code probably contributes to the emphasis of management and investors in manipulating ownership and financial arrangements at the expense of investments in improved productive capacity.

Interest Group Politics and Policy Education

Olson (10) argues that as a political economy matures special interest coalitions gain increasing political and economic power and use this power in such a way that it strangles economic productivity. He uses this analysis to explain the relatively high rates of growth of Japan and West Germany and decline in England and the U.S. If Olson is correct then interest group politics becomes a critical industrial policy issue. How can necessary reforms be made, given the power of the interest groups?

Somehow a broad based coalition of voters interested in national development and a just society would need to be fostered. The political parties could play this role. They would have to be greatly strengthened. Election practices, including especially financing and use of TV, need to be reformed to strengthen the parties.

There is no substitute for an informed electorate in dealing with these complex political economic problems. It may be that public policy education is the most critical input of all to achieving a productive and just society.

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