BROOKINGS

Op-Ed

Capitalism is failing. People want a job with a decent wage – why is that so hard?

Richard V. Reeves Monday, April 29, 2019

Editor's Note:

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Before capitalism, there was work. Before markets, before even money, there was work. Our remotest ancestors, hunting and gathering, almost certainly did not see work as a separate, compartmentalized part of life in the way we do today. But we have always had to work to live. Even in the 21st century, we strive through work for the means to live, hence the campaign for a "living wage".

As a species, we like to define ourselves through our thoughts and wisdom, as Homo sapiens. But we could as easily do so through the way we consciously apply effort towards certain goals, by our work – as Homo laborans. It nonetheless took two revolutions, one agricultural, one industrial, to turn "work" into its own category.

Industrial capitalism sliced and diced human time into clearly demarcated chunks, of "work" and "leisure". Work was then bundled and packaged into one of the most important inventions of the modern era: a job. From this point on, the workers' fight was for a job that delivered maximum benefits, especially in terms of wages, in return for minimum costs imposed on the worker, especially in terms of time.

For Karl Marx, the whole capitalist system was ineluctably rigged against workers. Whatever the short-run victories of the trade unions, the capitalist retained the power; the ultimate control, over workers' time. And the worker would remain forever alienated from their work. The goal was to assert sovereignty over our own time, free of the temporal control of the capitalist, able "to hunt in the morning, fish in the afternoon, rear cattle in the evening, criticise after dinner".

The problem of alienation is far from solved. Only one in three American workers say they feel "engaged" with their work. But in terms of material conditions of life, across the broad sweep of economic history, capitalism has delivered pretty well for most workers. Wages rose, hours fell, life (mostly) got better. Global poverty halved. As an economic system, socialism fell from grace, and, by and large, and in spite of recent rhetoric on the American political left, continues to fall.

There are many variants of capitalism, of course, from welfarist Scandinavia through Anglo-Saxon laissez-faire to Chinese market statism. But the trend seemed pretty clear. Capitalism works. And it works, most importantly, for workers.

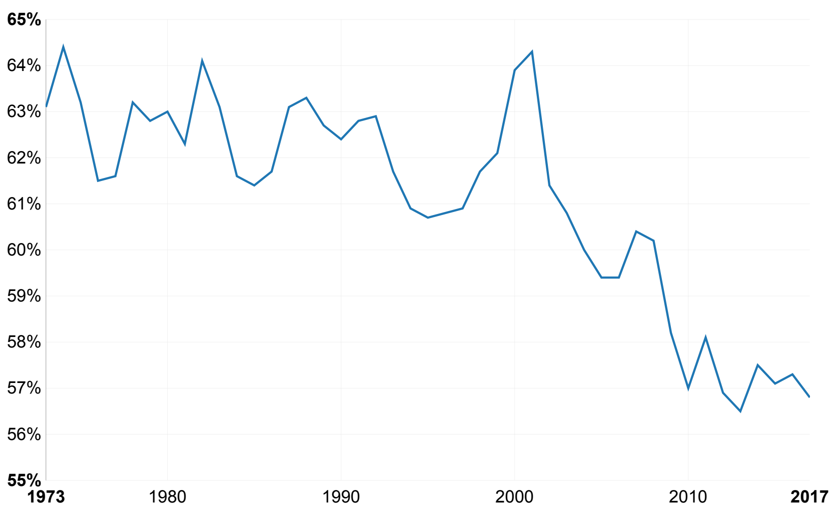
But now? Over the last decade, the logic of markets and the workings of capitalism have been intensely questioned and challenged, both from the populist right and the socialist left. Young Americans and supporters of the Democratic party are now more enthusiastic about socialism than capitalism (by 6% and 10% margins, respectively). Leading candidates now proudly describe themselves as socialists – unthinkable just a few years ago. (Whether they are in fact socialists by any sensible definition of the term is of course another matter.)

Future history books may begin the chapter on the current era with the events of 15 September 2008, when Lehman Brothers filed for the biggest bankruptcy in history, with $639bn in assets and $619bn in debt. Or perhaps the starting date will be three years later, when on 17 September 2011, two years after the official end of the recession, hundreds of protesters gathered in Manhattan's Zuccoti Park to "Occupy Wall Street". Or 8 November 2016, when Donald Trump ascended to the highest office in the land. It all depends whether, in hindsight, our crisis comes to be seen as economic or political in nature.

Certainly, the Great Recession was a massive economic shock. Nine million jobs were lost and 4m homes foreclosed on. Average household income dropped by 7%. Black families saw their already limited wealth stock cut almost in half. And the recovery has been painfully slow, in what some economists have labeled a “zombie economy”.

But the Great Recession also shone a light on trends long predating the downturn, not least in terms of stagnant wage growth for so many workers. By comparison with the postwar years, economic growth has been slow for the last few decades. At the same time, the transmission mechanism linking economic growth to the wages of workers appears to have broken. The share of income going to workers has dropped sharply, from 64% in 1974 to 57% in 2017.

Labor Share of Income

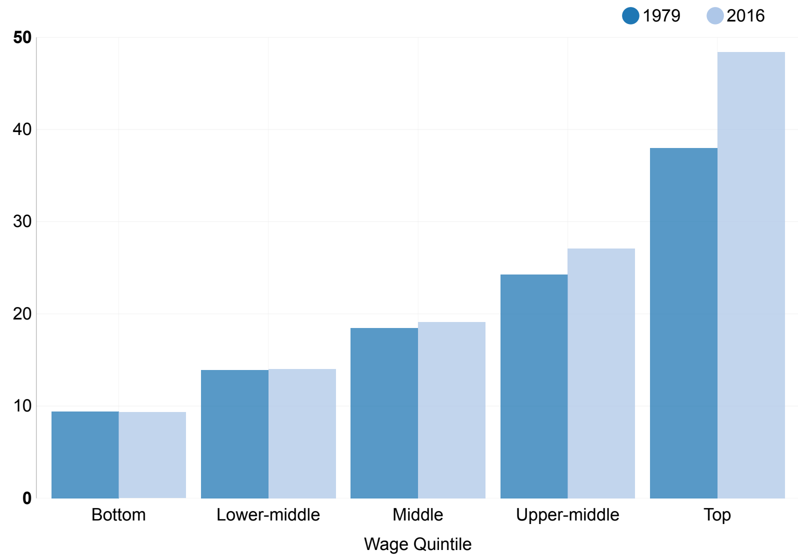


Note: Productivity and Costs, BLS (1973-2017). Labor share is defined as the sum of employee and proprietor labor compensation, divided by gross value-added output.

Source: Shambaugh, Nunn, Liu, and Nantz, 2017. The Hamilton Project

In the last few years, as the zombie gradually wakes up, household incomes and wages have begun to nudge upwards – but families are still having to work more hours to get the income they need. Women are working more, and earning more (though the pay gap remains). But as men work less, and earn less, many families are simply standing still in economic terms. Since 1979, the median male wage in the US has dropped by 1.4% for whites– and by 9% and 8% for black and Hispanic men, respectively. Workers at the top of the earnings and education distribution have seen their paychecks continue to fatten: not so on the middle and bottom rungs of the labor market. Wage growth remains torpid in the middle of the distribution.

Real Wages by Wage Quintile



Note: Current Population Survey, BLS (1979-2016). Wages are expressed in 2016 dollars, deflated using the CPI-U-RS. Sample restricted to workers ages 25-54. Growth rates are cumulative.

Source: Shambaugh, Nunn, Liu, and Nantz, 2017. The Hamilton Project

At the same time, the volatility of incomes at the bottom of the distribution has grown, in part because of shifts towards the so-called "gig economy", intrinsically episodic, and in part because of the rise of unpredictable schedules. Most American workers are still paid by the hour, and half of them have no formal control over their schedules. Two in five hourly-paid workers aged between 26 and 32 know their schedules less than a week in advance. Hard to arrange childcare on that notice. Many American workers are fighting, like the trade unions of old, on two fronts: for money, and for time.

Why? Why, for so many for middle-class and working-class Americans has "economic growth become a spectator sport", as the liberal economist Jared Bernstein memorably put it.

There are two competing explanations for what happened to tear the connective tissue between growth and wages: the Productivity Story and the Power Story. The productivity story goes as follows: wages reflect the productivity of the worker; the modern economy rewards skills more than in the past; and lots of people have not upskilled quickly enough. Under the wonky label "skills-biased technological change", this view prevailed across most of the political spectrum well into this century. Free markets could deliver fair-enough outcomes, so long as everyone got the education and training they needed. "Lifelong learning" became the mantra of all, and the cliched answer from politicians and scholars to the deepening problem of inequality.

There are two problems with this story. First, the necessary investments in education and training were never actually made. Community colleges, the most common post-secondary destination for students from families in the bottom 80% of the income distribution, are underfunded, overstretched and largely ignored by the policy elite. Lifelong learning never made it from the thinktank policy briefs and Davos panels to the real lives of real people.

The second problem is that productivity turns out to be only part of the story – and perhaps not even the most important part. It is certainly wrong to claim that there is no relationship at all between productivity growth and wage growth. But the connection has certainly become less clear over time, and harder to square with the trends in wage inequality.

Even the strongest and most thoughtful proponents of the Productivity Story, such as Michael Strain, director of economic policy studies at the American Enterprise Institute, concede that it is but one element. As Strain writes, "it is most useful to think of wages as being determined by a combination of competitive market forces, bargaining power, and institutions".

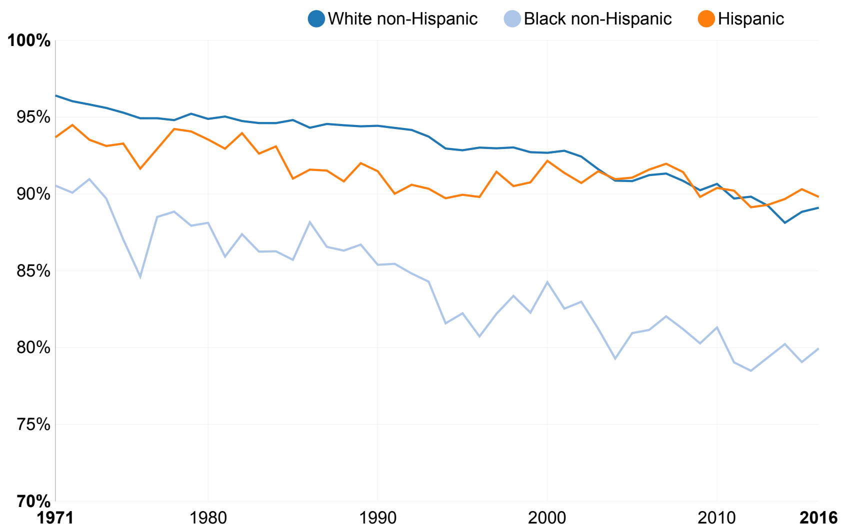
The Power Story is that wages do not reflect the productivity of the worker, but their power. Lower wages are a reflection of growing powerlessness, the result of four intersecting trends. First, unions have become almost mythical creatures, unicorns of the labor market. Just one in 20 workers in the US private sector are members of a trade union, down from more than one in four in the 1950s. Sometime around 1980, US businesses declared war on unions, and won.

Second, the wage gap between similarly qualified workers in different companies has widened. One widely cited study finds that one-third of the increase in the earnings gap from 1978 to 2013 occurred within firms, while two-thirds of the rise occurred *between* firms. It is the market power of one firm versus another that determines wages, rather than the power of a particular employer versus its workers. Even if workers can get organized, they cannot force a completely different employer to share more of their surplus with them. (Now that *would* be socialism.)

Third, market power has become increasingly concentrated into fewer, larger companies, especially in terms of power in the labor market. The dangers of monopoly power in market economies are well known, and the push for strong anti-trust laws has historically united the pro-market right and the progressive left. In recent years the threat of monopsony power (ie a dominant single buyer), not least in employment, has risen. Amazon is the poster child of monopsony power. But in many towns, a single hospital might be the biggest employer, and the sole employer of nurses, for example. Hard in these circumstances for workers to negotiate better pay and conditions

Fourth, the labor market is not as tight as it looks. There is a still a large "reserve army" of workers, serving to hold wages down. This may not be what the headline unemployment rate – now down to 4% – is telling us. But the headline rate tells us less than in the past, because millions of workers have dropped out altogether, and so are not counted in the unemployment statistics. The chances of a "prime age" man being in paid work has dropped by eight percentage points in the postwar decades. For most of this period, women's employment rates were increasing – but, in the US at least, that rise stopped abruptly around the turn of the century, and has actually edged down slightly. Black, Hispanic and less-educated adults have all seen the sharpest drops in participation.

Prime-Age Male Labor Force Participation by Race and Ethnicity



Note: BLS Current Population Survey. 1971 is the first CPS ASEC year with race/ethnicity categories comparable over time.

Source: Krause and Sawhill, 2017. The Brookings Institution

This powerlessness of workers in specific companies has fueled calls for higher minimum wages. At a federal level, the value of the wage floor has dropped by 46% since 1968. Seminal scholarship from David Card and the late, great, Alan Krueger helped to allay fears about negative economic consequences of a higher minimum wage. But a big challenge here is that the gap between richer and poorer places has also grown. A $15 minimum wage may make perfect sense in Boston (median wage = $24.16 an hour). But perhaps not in Brownsville, Texas (median wage = $11.59). Half of US workers earn less than $18.58 per hour.

A worker without power is one with a lighter paycheck. They may also suffer greater indignities or disrespect in the course of daily working life. James Bloodworth's Hired: Six Months Undercover in Low-Wage Britain describes the loss of dignity faced by Amazon warehouse employees and Uber drivers. Horror stories abound of workers under constant surveillance, unable to take bathroom breaks and so resorting to adult diapers, or bullied or harassed by bosses or other workers. In 2011, the Morning Call of Allentown, Pennsylvania, reported that managers at the local Amazon warehouse refused to open the doors for ventilation despite soaring temperatures. They put ambulances outside instead, for the workers who collapsed.

Vivid stuff, and no doubt true in the particular. But it is important to note that it is not the general experience of most workers. The proportion of Americans reporting that they were "treated with respect at work" has held steady at around 92% since 2002, according to the General Social Survey.

For some critics of capitalism, workers lost the power struggle right at the outset. As Marx (Groucho, this time, not Karl) once put it, "What makes wage slaves? Wages!"

Whatever material gains workers managed to achieve came at the price of a profound loss of sovereignty. In her book Private Government: How Employers Rule Our Lives (and Why We Don't Talk about It), philosopher Elizabeth Anderson argues that CEOs are the new totalitarians, who "think of themselves as libertarian individualists", while acting in practice as "dictators of little communist governments". We imagine ourselves free but effectively barter our freedom away in exchange for pay, effectively handing over our passports as we punch in.

What most people want is a job that pays a decent wage and offers both some satisfaction and security. The harsher critics of the system, like Anderson, believe that these goals are incompatible at a deep level with capitalist dynamics. But at least for some, especially for white men, market capitalism delivered pretty well for at least a generation. This is why it was so important to fight to crowbar the doors open for women and people of color. The progressive goal was not to curtail the market, but to open it.

In very recent historical time, the general direction of history seemed to be towards capitalism of one kind or another. In the sliver of time between the fall of the Berlin Wall and the fall of Lehman Brothers, it seemed like markets embedded in liberal democracies were the preordained future. Fukuyama declared the End of History.

Scholars adopted the term "late capitalism" to describe the trends towards service-led economies and increasingly flexible working arrangements (flexible, that is, for the employer). But with the dislocation, insecurity and inequality witnessed over the last decade, it is hard to disagree with the narrator of Adam Thirlwell's novel Lurid and Cute, who exclaims of capitalism: "'Late? It had only just got started!"