"Summary of article by David M. Gordon: Skills Mismatch or Globalization?" in Frontier Issues in Economic Thought, Volume 4: The Changing Nature of Work. Island Press: Washington DC, 1998. pp. 80-84

Social Science Library: Frontier Thinking in Sustainable Development and Human Well-being

"Summary of article by David M. Gordon: Skills Mismatch or Globalization?"

Most economists have emphasized one of two standard explanations of falling real wages and rising inequality -- the "wage squeeze" -- among U.S. workers today. Some attribute the problems to the changing skill requirements of the economy, creating a "skills mismatch" between labor supply and demand. Others see globalization as the cause of the problem, including both the growing competition from industry in low-wage developing countries, and immigration of relatively low-skilled workers from the same regions. This chapter argues that neither of these views comes close to a complete or adequate explanation of the wage squeeze. Other chapters of the book present the author's alternative explanation, in which "fat and mean" corporate management strategies are the principal cause of the problem.

THE SKILLS MISMATCH

In the most popular explanation of the wage squeeze, it is argued that low-skilled workers have suffered most acutely because they are out of step with the rising, technologically driven demand for high-skilled labor. The facts seem to support this view: since the early 1980s, real earnings of those with the most education have increased, while real earnings of nearly everyone else have declined.

However, these figures only show that better educated workers fared better, not that a skills mismatch was responsible for the differential outcomes. The educational differential cannot be attributed to labor supply shifts, since the supply of highly educated workers is rising faster than the supply of those with less education. Changes in labor demand must therefore be responsible; yet identifying the demand-side effect has proved difficult. There have been important interindustry shifts in labor demand, but researchers have found that these are not responsible for increasing wage inequality. The changes in average wages have occurred within industries, not as a result of movement of labor from one industry to another.

At this point, many economists simply assume that technological change is the only plausible explanation for changes in earnings. Technology is often treated as a residual, accounting for everything about wages and productivity that cannot be explained more directly by other factors. In a study of the rise in earnings inequality, two economists said, referring to possible explanations of the problem, "The term 'technological change' comes to mind, but it only underscores our ignorance."[1] The claim that the unexplained residual represents the effects of technology is at best based on circumstantial evidence, at worst a tautological explanation.

There are at least four substantive problems with the skills mismatch argument. First is the problem of timing. Much of the collapse in low-skilled workers' earnings and employment had occurred by 1984, well before the widespread computerization of the workplace. "Were businesses so shrewd and prescient that they *anticipated* the coming trends in computerization and began dumping their lower-skilled workers, as it were, before the deluge?" (182-183) Wages for male college graduates, on the other hand, fared worse after the mid-1980s than before. Thus the timing makes it difficult to attribute the relative gains of the best-educated workers over the last few decades to a rise in computer use.

A second problem lies in the assumption that rising educational levels imply rising skill requirements on the job. More detailed examination of skill requirements suggests that they have grown steadily over the past thirty years or more, with no particular acceleration in recent years. Computerization in manufacturing appears to have had little effect on actual job requirements; computerization in offices raises the skill levels needed for some jobs but lowers the skills needed for others.

A third problem is the absence of productivity gains in many sectors. Rapid technological change and an increase in the demand for skilled labor should result in rising productivity. Yet during the 1980s and early 1990s there was little productivity growth in non-manufacturing sectors, despite the increasing educational level of the workforce.

Finally, the skills mismatch argument assumes that earnings are directly related to skills and educational levels. This has proved problematical both in general and in specific terms. In general, empirical studies find little or no correlation between skills and earnings for non-supervisory, non-professional workers. More specifically, highly skilled occupations involved in the use of new technologies, such as computer operators and engineering technicians, have had only slow increases, or even decreases, in real earnings; meanwhile, non-technological professions such as lawyers have had rapid earnings gains.

GLOBALIZATION

If technology didn't do it, perhaps globalization is the culprit. Imports have risen rapidly, while manufacturing employment has fallen, making the trade-and-wages argument seem plausible. Specific industries and communities have certainly suffered from trade competition. But as with the skills mismatch argument, the evidence here turns out to be largely circumstantial.

One concern is that trade largely affects manufacturing and other industries, such as mining, that produce tradeable goods. If import competition were the primary explanation of the wage squeeze, the problem should be more severe in manufacturing and mining than in other, nontradeable sectors. This is not the case. Between 1979 and 1994, real wages fell faster in construction, transportation and public utilities, and retail trade than in either manufacturing or mining.

Even in manufacturing it is important to distinguish between import competition caused by low foreign wages and other causes. In the early 1980s, a critical period of job losses and real wage declines, the value of the dollar was unusually (and unsustainably) high relative to other

currencies. This made it unusually cheap for Americans to buy foreign goods, even those produced with labor paid as well as in the U.S.

In fact, most manufactured imports do come from countries where labor is paid well. A majority of the U.S. trade deficit in manufactured goods is with Japan and Western Europe, where labor costs are slightly higher than in America, rather than with low-wage developing countries. "[I]f we want to understand the trade advantages that many other advanced countries have enjoyed, we should pay more attention to the sluggish pace of our productivity growth than to the levels of our workers' wages." (193)

Economists studying the effects of trade have estimated that between 1978 and 1990 the U.S. lost almost a million production worker jobs in manufacturing due to trade with developing countries. While this is a large absolute number, it is less than one percent of private nonfarm employment in 1990, and thus cannot account for much of the overall decline in real wages.

Other evidence of the importance of trade also appears problematical on closer inspection. Widely quoted estimates that trade accounts for 10 to 15 percent of the increased inequality of wages in the 1980s are based on a study that did not consider other possible explanations, such as the decline in unionization.

The much-discussed idea that transnational corporations are transferring their production facilities to low-wage countries has some local or anecdotal validity, but it is not a growing trend. During the 1980s, the amount of U.S. trade controlled by transnational corporations actually dropped, and their manufacturing employment in the U.S. and in foreign affiliates declined at the same rate. Moreover, most of their majority-owned affiliates are in developed, not developing, countries.

A final argument about globalization is that immigration of low-skilled foreign workers is driving down U.S. wages. The most influential study of the subject finds virtually no effect of immigration on the relative wages of college graduates vs. high school graduates, but a sizeable effect on the wages of high school dropouts. Yet as in several of the other studies discussed here, this analysis assumes that there are direct links between education, skills, and earnings, and ignores other possible explanations such as the decline in union strength. Other discussion of the effects of immigration points out that immigrant-owned businesses and the additional purchasing power of immigrant households create about as many jobs as are taken by immigrant workers.

VEIL THE CORPORATIONS, BLAME THE VICTIMS

Strong skepticism about both the skills mismatch and the globalization explanations could seem like nihilism. In explaining the wage squeeze, what else is there?

Both the skills mismatch and the globalization arguments rely on the assumption that markets work in a way that closely resembles the competitive models of traditional economic theory. Employers simply reflect and respond to market forces that compel, for example, payment of growing skill differentials or movement of production to low-wage countries. In this theory, corporate power is invisible, indeed even impossible to imagine. The problems of the market

can then be blamed on individuals, who failed to become sufficiently educated and skilled, or refused to compete hard enough to win the battle against foreign producers.

However, the world does not behave according to the competitive model. Our economy cannot be explained without reference to the exercise of corporate power. An older generation of institutionalist economists recognized this fact; fortunately, the awareness of institutional factors is gradually reappearing within the mainstream of labor economics. A better explanation of the wage squeeze (the subject of the next chapter of the book) places the spotlight directly on corporate power, rather than on the individuals who are its victims.

Notes

1. Kevin Murphy and Finis Welch [[check Gordon's footnotes for citation]], quoted in Gordon, 182.