Testimony of Oren M. Cass
Senior Fellow, Manhattan Institute for Policy Research
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Good afternoon Chairman Rubio, Ranking Member Cardin, and Members of the Committee. Thank you for inviting me to participate in today's hearing.

My name is Oren Cass. I am a senior fellow at the Manhattan Institute for Policy Research where my work on strengthening the labor market addresses issues ranging from the social safety net and environmental regulation to trade and immigration to education and organized labor.[1]

<u>My primary message to the committee is this: A labor market in which workers can support strong families and communities is the central determinant of long-term prosperity and should be the central focus of public policy.</u> Alongside stable political institutions that protect basic freedoms, family and community provide the social structures necessary to a thriving society and a growing economy. Those institutions in turn rely on a foundation of productive work through which people find purpose and satisfaction in providing for themselves and helping others. The durable growth that produces long-term prosperity is the emergent property of a virtuous cycle in which people who are able to support their families and communities improve their own productivity and raise a subsequent generation able to accomplish even more. Conversely, without access to work that can support them, families struggle to remain intact or to form in the first place, and communities cannot help but dissolve; without stable families and communities, economic opportunity vanishes.

American policymakers have erred in their single-minded focus on maximizing consumer welfare, which they pursue by growing and redistributing the so-called "economic pie." Economic growth and rising material living standards are laudable goals, but they by no means guarantee the health of a labor market that will meet society's long-term needs. If we pursue growth in ways that erode the labor market's health, and then redistribute income from the winners to the losers, we can produce impressive-looking economic statistics—for a while. But we will not generate the genuine and sustainable prosperity that we want. Growth that consumes its own prerequisites leads inevitably to stagnation.

My testimony proceeds in three parts: First, I explain the limitations of consumer welfare as the organizing principle for our economic policy and the reasons why an emphasis on work—that is, people's role as productive contributors to society—offers a better formula for long-term prosperity. Second, I describe the goal of "productive pluralism," rather than economic growth for its own sake, as the appropriate target for policymakers and emphasize the importance of small business and entrepreneurship in pursuing this goal. Third, I highlight the central role that labor markets play in *productive pluralism* and suggest opportunities for policy reforms to strengthen those markets.

A recurrent theme will be the need to acknowledge trade-offs. Much pessimism about the future of work for the typical American begins from the assumption that we cannot possibly make concessions on any of our other priorities. And yes, if the preferences of the typical urban professional are always the most valid and important, if the maximization of economic efficiency and material consumption is inviolable, if businesses retain the incentive to find the cheapest possible workers anywhere in the world, then the future of the American labor market indeed looks grim. But all this merely begs the question, what should our priorities be? In the past, our society was much less affluent, and yet the typical worker could support a family. How could it be that, as we have grown wealthier as a society, we have lost the ability to make that kind of arrangement work? Or do we just not want to?

1. Production vs. Consumption

That GDP offers a reliable proxy for prosperity and that each individual's satisfaction depends on the share of GDP she can consume are the key components in the concept of the *economic pie*. When serving a pie, each portion's size depends on both the size of the dish and the share allocated to each slice. Likewise, the thinking goes, each person's consumption depends on the size of the overall economy and the share he receives. Fighting over shares is a zero-sum game, but if we concentrate on baking an ever-larger pie, then everyone's slice can grow. And who doesn't like pie?

Enthusiasm for the tenets of this "economic piety" is near universal. The phrase *economic pie* first appeared in the presidential lexicon in 1952, when Harry Truman quoted from a *Business Week* article that used the term. John F. Kennedy used it when addressing the U.S. Chamber of Commerce. Presidents Lyndon Johnson, Gerald Ford, Ronald Reagan, George H. W. Bush, Bill Clinton, and Barack Obama used it too.[2] The media and think tanks across the political spectrum bandy it about with ease. Republicans tend to promote free markets that will grow the pie rapidly, while grudgingly accepting a role for government in apportionment. Democrats focus more on the role of government in guaranteeing big enough portions for all but generally recognize that more growth will mean more to go around.

On its own terms, this approach has delivered. The overall economy has grown enormously: from 1975 to 2015, the nation's GDP increased threefold.[3] Redistribution has widened the smaller slices: during the same period, spending on programs targeting lower-income households increased fourfold.[4] Federal regulators' budgets expanded faster still,[5] yet the American economy remained the dynamic and innovative envy of the world. For Americans of all socioeconomic strata, material living standards, access to technology, and consumer variety all marched steadily higher.

The problem is not so much that public policy has failed as that it has succeeded at the wrong things. America is like the classic romantic-comedy heroine who, as the trailer intones, "had it all, or so she thought." She has the prestigious job and the elegant apartment, yet she is not happy. She has pursued the wrong goals, she discovers, and to reach them, she sacrificed the things that mattered most. We got exactly what we thought we wanted: strong overall economic growth and a large GDP, rising material living standards, a generous safety net, rapid improvements in environmental quality, extraordinarily affordable flat-screen televisions and landscaping services. Yet we gave up something we took for granted: a labor market in which the nation's diverse array of families and communities could support themselves.

In making GDP growth and rising consumption the central objectives of public policy, *economic piety* represents a truncated and ultimately self-undermining concept of prosperity. Workers have no standing, in this view of the economy; neither do their families or communities. Households that see their economic prospects plummet or their livelihoods vanish should ask for a government check and be placated when they get one. Towns that can no longer sustain themselves become places that people should just leave. Politicians will pay lip service to the importance of education and retraining, but they will not hold themselves accountable for such programs actually working. The *economic pie*'s expansion, regardless of what or who gets left behind, is the goal; maintaining a healthy, inclusive society is a hoped-for by-product, not an end in itself.

This isn't to say that economic growth isn't important; of course it is. Growth is a prerequisite to improved living standards, which we should want to achieve. But while growth is necessary to a prosperous society, it is not sufficient. Not all growth is equally beneficial, and the policy choices that yield the most immediate short-term growth don't necessarily prepare the ground for sustained economic and social progress. To the contrary, policies that target growth without concern for the economy's longer-term trajectory, or for the well-being of the society within which that economy operates, will tend to erode the capacity for growth. Politicians who equate GDP growth and rising consumption with prosperity pursue agendas that often bear little resemblance to what their constituents want or need.

Superficially, consumption seems a sensible focus. In popular culture, consumption is an obvious good. The toil of production, by contrast, is only a necessary means to that end—and if one manages to consume more while producing less, all the better. "The interest of the producer ought to be attended to, only so far as it may be necessary for promoting that of the consumer," as Adam Smith put it.[6] But allowing the consumption tail to wag the production dog distorts our understanding of prosperity. Only through production does the ability to consume exist. Production without consumption creates options; consumption without production creates dependence and debt. As Senator Sasse has written: "There is almost nothing more important we can do for our young than convince them that production is more satisfying than consumption."[7]

Most of the activities and achievements that give life purpose and meaning are, whether in the economic sphere or not, fundamentally acts of production. Yes, material living standards contribute to prosperity, but accomplishments like fulfilling traditional obligations, building strong personal relationships, succeeding at work, supporting a family, and raising children capable of doing all these things themselves are far more important to life satisfaction. What these things have in common is their productive nature not as boosts to GDP but as ways that people invest effort on behalf of others. Our social norms recognize productive activities as essential to a functioning and prosperous society, and so we award respect, dignity, and gratitude to those who perform them.

The Importance of Work for the Individual

For the individual, work imposes structure on each day and on life in general. It offers the mundane but essential disciplines of timeliness and reliability and hygiene as well as the more complex socialization of collaboration and paying attention to others. It requires people to interact and forges shared experiences and bonds. It promotes goal setting and long-term planning. True, other pursuits can provide these kinds of benefits—for example, raising children, keeping a home, or volunteering in the community. But sleeping, couch surfing, or playing video games does not. And for out-of-work men in particular, such idle activities tend to fill up their time.[8]

Without work—the quintessential productive activity—self-esteem declines and a sense of helplessness increases.[9] People become depressed—unemployed Americans are twice as likely as full-time workers to receive treatment for depression; the long-term unemployed are three times as likely.[10] In empirical "happiness" studies, life satisfaction drops ten times more from unemployment than from a substantial loss of income.[11] And while people return to their previously self-reported levels of happiness several years after marrying, divorcing, becoming widowed, or welcoming a first child into the world, they never get used to joblessness.[12]

The Importance of Work for Families

Work (especially for men) helps establish and preserve families. Where fewer men work, fewer marriages form.[13] Unemployment doubles the risk of divorce, and male joblessness appears the primary culprit.[14] These outcomes likely result from the damage to both economic prospects and individual well-being associated with being out of work, which strain existing marriages and make men less attractive as marriage partners. The so-called marriageable-men hypothesis associated with sociologist William Julius Wilson, which suggests that a lack of job opportunities contributed to the collapse of two-parent families in the African American community, remains controversial.[15] But that debate is largely about whether lack of economic opportunity was the underlying cause of male idleness. Few would question that such idleness would tend to reduce the likelihood and the stability of marriage.

Current economic conditions do appear to play a role in harming marriage formation. MIT professor David Autor and his colleagues found that U.S. regions facing greater competition from China experience lower rates of marriage and higher shares of children born to single mothers and that this effect appeared only when the economic disruption affected male employment.[16] Johns Hopkins professor Andrew Cherlin and his colleagues sought to study the "relationship between economic inequality and sociodemographic outcomes such as family formation," for which they noted a lack of "satisfactory evidence on the mechanisms by which inequality may have an effect."[17] When they accounted for a region's availability of "middle-skilled jobs," accessible to high school graduates and paying above-poverty wages, they found that the labor market, not the inequality, was influencing family formation. The issue was less who earns how much more than whom and more who has a chance to earn a living at all.

The Importance of Work for Communities

Work is both a nexus of community and a prerequisite for it. Work relationships represent a crucial source of social capital, establishing a base from which people can engage in the broader community—whether it's playing on a softball team, organizing a fund-raising drive, or hosting a field trip for the local preschool. This dimension of employment is especially relevant outside of urban centers; in such settings, the workplace can become a central meeting point. Community, in turn, provides the social foundation on which the economy is built. Measures of social trust, for instance, are highly correlated with GDP across countries and entrepreneurship across individuals.[18] Communities that lack work, meanwhile, suffer maladies that degrade social capital and lead to persistent poverty. Crime and addiction increase, their participants in turn becoming ever less employable;[19] investments in housing and communal assets decline; a downward spiral is set in motion.

The role of family and community in transmitting opportunity to the next generation also depends on work. When parents lose their jobs, their children tend to do worse in school, graduate at lower rates, and have less success as adults.[20] While productive activity provides direct benefits to workers, its worth also derives from the dignity and respect that society confers on self-reliance and productive contributions. In a community where dependency is widespread, illegality a viable career path, and idleness an acceptable lifestyle, the full-time worker begins to look less admirable—and more like a chump.

This is consistent with what our intuitions tell us. Former Senator John Edwards, in his famous "Two Americas" speech at the 2004 Democratic National Convention, described the "dignity and honor in a hard day's work" as among the most important values instilled by his parents.[21] "I still remember vividly the men and women who worked in that mill with [my father]," Edwards observed. "I can see them. Some of them had lint in their hair; some of them had grease on their faces. They worked hard, and they tried to put a little money away so that their kids and their grand-kids could have a better life." No one should be surprised if children raised in households and communities that lack the dignity and honor of work show less inclination or ability to climb onto the economic ladder themselves.

The Importance of Work for the Economy

Economic piety trusts GDP growth to produce widely shared prosperity and the thriving society that is our ultimate objective. But this places the cart in front of the horse. It is the healthy society that produces the requisite human and social capital from which true economic prosperity emerges—and toward which policy should orient itself. Conversely, when opportunity declines, a downward spiral is set in motion, in which the next generation, beginning from a worse point, can likely offer even less to the one that follows. When ways of life vanish or towns crumble or industries flee overseas, they are not easily replaced. When self-sufficiency gives way to dependence, cultural norms shatter. Families that fail to form leave both adults and children adrift. It should not be shocking if, under these conditions, growth stalls.

At the national level, whereas traditional economic theory suggests that specialization is key to prosperity, MIT professor César Hidalgo and Harvard professor Ricardo Hausmann have shown the opposite to be true. The more diverse is the array of knowledge and capabilities within an economy, the stronger is its long-term health.[22] This would suggest that when economic growth undermines pluralism, it may eventually undermine itself as well. Emphasizing consumption allows productive capacity to atrophy, but that capacity is not something that we can scale down and back up at will. Experience must accumulate; supply chains must develop; productivity must grow percentage point by percentage point, year by year. Where capacity and know-how are lost or not built, it becomes necessary to start over from behind those who moved more steadily forward. Where poor investments—or no investments—are made at one point, negative effects ripple outward for years.

The Failure of Economic Piety

The data that describe the worsening condition of American workers and their families are by now well known: decades of wage stagnation;[23] shrinking shares of prime-age males working full-time,[24] of households with even one full-time worker,[25] and of children raised in stable, two-parent families;[26] skyrocketing rates of substance abuse[27] and suicide,[28] culminating in a stunning three straight years of declining life expectancy—which last occurred a century ago in the face of a global pandemic and a world war.[29]

It bears mentioning, too, that our pursuit of growth is now failing even on its own terms. Without the stable foundation of a labor market that allowed for self-sufficiency, social structures buckled, social capital drained away, and the national economy struggled. Broken families and collapsing communities are not, it turns out, effective incubators of a productive workforce. Economic growth during 2000–2016 averaged 1.8 percent, half the rate recorded during 1950–2000. The best growth rate of the past decade, 2.9 percent in 2015, fell below two-thirds of the years in the prior century's second half.[30]

Underlying this trend is a collapse in the genuine economic dynamism that produces prosperity. Productivity growth turned in a seventh straight year below 1.5 percent in 2017 (since 1948, the nation had never experienced more than a three-year run so anemic).[31] As the Economic Innovation Group has shown, both the rate of new firm formation and the share of employment in new firms has been declining for decades and has become concentrated in an ever narrower geography. Just five metro areas accounted for half the net increase in businesses during recovery from the Great Recession; two-thirds of metros saw a net decline.[32]

Having forsaken the healthy society that makes economic growth possible, Americans now find that they have neither.

2. Productive Pluralism

As an alternative to *economic piety* and its GDP-based definition of prosperity, I suggest what I call *productive pluralism*: the economic and social conditions in which people of diverse abilities, priorities, and geographies, pursuing varied life paths, can form self-sufficient families and become contributors to their communities. This definition begins from the insight that productive pursuits—whether in the market, the community, or the family—give people purpose, enable meaningful and fulfilling lives, and provide the basis for the strong families and communities that foster economic success too.

As the term *productive pluralism* suggests, a critical corollary of a focus on production is a recognition that different people will build productive lives in different ways, so for this prosperity to be inclusive, it will also need to accommodate numerous pathways, even at the expense of some efficiency. Measures like GDP create the convenient illusion of a homogenous population benefiting (or suffering) in lockstep. Money being fungible, everyone is presumed to have access to whatever she might choose to buy. Production is not so simple.

People have different priorities, excel in different ways, and find meaning in different places, so a production-oriented prosperity that extends across society must offer numerous paths to its achievement. Cities may be more economically productive, for example, but not everyone wants to live in a city. A traditional college degree may correlate with higher earnings, but most people will not attain one. Having two parents work while the children attend daycare may be more efficient, understood in a narrowly economic sense, but a community consisting entirely of such households is one that many families would rather not live in. Growth may be fastest if we channel everyone to wherever his economic output is greatest, but pluralism will improve real prosperity if the options it leaves available more closely match people's abilities and the range of life choices they wish to make.

A goal of *productive pluralism* demands that policymakers move beyond the standard policy prescriptions of redistribution, retraining, and relocation. It rejects monetary redistribution as a solution. An emphasis on consumption offers what looks like a get-out-of-jail-free card: government spending. Connecting people to productive activity is a complex challenge that requires a healthy civil society and labor market. Public policies can support or hinder that process in myriad ways, but if preserving it is a priority, then sacrifices will inevitably be required elsewhere. When the goal is consumption, conversely, those challenges and trade-offs vanish. Like a medieval indulgence, a promise of redistribution cures all. And if replacing lost income with a government benefit solves little or makes a bad problem worse, this merely drives the indulgence's price higher next time around. Emphasizing consumption leads policymakers to ignore the actual experience of society's struggling segments and point to statistics that depict an alternate reality.

Productive pluralism also rejects the possibility of waiting for rescue to arrive from an education system or training program that can transform those left behind into those getting ahead. If this were readily available, it would indeed help ease the growing crisis—and, for that matter, solve any number of society's problems—but no such miracle appears imminent. Despite the nation doubling per-pupil spending and attempting countless education reforms,[33] test scores look no better than they did forty years ago.[34] Most young Americans still do not achieve even a community college degree.[35] Participants in training programs often achieve worse results than those in control groups left to their own devices.[36] We should of course continue to strive for better outcomes, but we can no longer pretend that reshaping people to fit our economy offers a plausible substitute for ensuring that our economy's shape fits our people.

Of particular importance to this Committee, *productive pluralism* demands that we meet people where they are not only conceptually, but also literally—in the communities where they live.

Residential mobility is the issue that best captures policymakers' misunderstanding of prosperity, the social endowments that foster it, and thus what should be their own objectives. The willingness to pack up and move in pursuit of opportunity is part and parcel of the American Dream and a key element of the nation's economic vitality. Yet, as hardship has increased in recent decades, the share of the population that relocates has declined.[37] If things are so terrible, some economists grumble, why won't anyone move? They have built elaborate models to show how much higher GDP would be if only people lived where their productivity would be highest.[38]

This gets things backward. Strong families and communities launch people into the world to seek their fortune. Relocation requires deep stores of social capital. Without the skills and habits to access opportunity, failure is likely. Lacking a strong support base, it can be hard to get started. If someone is already dependent on government benefits and a move places those benefits at risk, staying put can seem the better bet. Geographic mobility can't rescue America from the consequences of its socially unsustainable growth—because lower geographic mobility is one of those consequences.

Certainly genuine pluralism requires the opportunity to relocate. But in most circumstances, it should also include the opportunity to stay, a choice that has always been and remains the norm—and one we should applaud, not lament. The median American adult lives only 18 miles from his mother and 37 percent of Americans have never left their hometown.[39] Even when mobility was much higher, it rarely amounted to the abandonment of existing communities. The migration of "Okies" from the "Dust Bowl" of the 1930s may be the iconic American image of relocation in search of opportunity, but Oklahoma's population declined only 2 percent during that decade. In Kansas and Nebraska, the declines were less than 5 percent. As technology obliterated agricultural employment, the population of Iowa held steady or increased in every decade from 1880 to 1980.[40]

Relocation tears people away from their communities. If a critical mass relocates, it can decimate the community left behind. The idea that struggling communities should disband themselves is not a return to "how things used to be"; it is an admission of catastrophic failure and a prescription for further disaster. To be sure, the track record is not good for "place-based policies" seeking to revitalize particular industries in particular cities. But a commitment to returning restoring broad-based prosperity that reaches across the nation must be the non-negotiable starting point for debates about economic reform.

Small business and entrepreneurship will be central to meaningful progress. *Economic piety* has led economists to celebrate the idea of large multinational corporations centering their "knowledge" operations in coastal American cities while offshoring their "lower value-add" operations, including manufacturing. This model may generate economic growth and yield cheap consumer goods, but it is not a sustainable one. Every local market must have the opportunity to engage meaningfully in the broader national economy; this will require much higher levels of firm formation and a business environmental in which small- and medium-sized businesses can thrive.

Manufacturing ecosystems are of particular importance, for two reasons. First, manufacturing remains among the most productive economic activities for less-skilled workers. As a share of overall employment, manufacturing has fallen below 10 percent, but in 2016, the industry still accounted for more than 20 percent of private-sector jobs in traditionally blue-collar occupations with a median wage of more than $15 per hour. The manufacturing, construction, and resourceextraction industries combined to provide almost 40 percent of such well-paying, blue-collar jobs.[41] For men, that share is far higher.

Take Pittsburgh, sometimes cited as a poster child for postindustrial transformation from heavy industry to health care. From 1990 to 2016, the Pittsburgh area lost forty-six thousand manufacturing jobs while gaining sixty-seven thousand health care and social assistance jobs. But while "production" jobs in the area paid a median hourly wage of $18 in 2016, in line with the area's median for all occupations, "health care support workers" earn $14 and "personal care and service workers" earn $11.[42] Over the period, the area's median household income rose at an annual rate of only 0.3 percent.[43]

Second, "tradeables"—goods and services that can be consumed far from where they're produced—are the keystones of local economies. Americans take for granted that they can buy what products they want from around the world. But how can someone whose work consists entirely of serving others in his community expect a firm halfway around the world to make something for him?

Consider the local physician who provides care only to those in his town. He may be well compensated, but he can't sell his work to the makers of cars or phones halfway around the world or even to the medical equipment supplier in the next state. He must trust instead that some of his patients produce goods or services that can be sent to those places and, in purchasing his medical services, give him the resources to acquire the goods that he needs. Or consider the plight of a local economy as a whole. It wishes to receive from elsewhere almost all of its food, medicine, vehicles, electronics, energy, and more. It must send tradeables of equal value. Not every individual must do so; most may work in the local services economy—but they cannot all cut one another's hair.

Tradeables can take many forms. Wall Street provides its financial services around the country and the world, Hollywood exports its movies, and Orlando sells the Disney World experience to tourists. Call-center workers are exporters too. But manufactured products represent by far the largest category of tradeables and are, along with agriculture and natural resources, the ones in which less-skilled workers and less urban locations are best suited to excel. The strength of the industrial economy dictates the fortunes of workers with a comparative advantage in physical activity and regions with a comparative advantage in open spaces and raw materials.

The importance of tradeables to a local community also helps to illuminate the vast difference between the often-equated phenomena of automation and globalization. For the worker dislocated by trade, the facility in which he once worked is likely gone, and the production now occurs somewhere else. But for the worker laid off or never hired because of automation, the facility is still operating in town, likely producing more output than before. Total demand for labor from the firm and its surrounding ecosystem is likely larger, and if capital has replaced labor, the remaining workers are likely earning more—and some other highly paid professionals may be arriving in the area with new demand for services of their own. Furthermore, while productivity gains occur bit by bit, year by year, a plant that shuts down and moves overseas is here today and gone tomorrow. In which situation might it be easier to find a new, well-paying job?

A reporter telling the story of automation speaks to a laid-off worker at a lunch counter; one telling the story of trade reports from the empty parking lot of an abandoned building. There is no one left to talk to.

What happens to a community whose economy does not produce anything that the world wants? It has one export that it can always fall back on: need. Every resident enrolled in a program of government benefits entitles the community to more goods and services from the outside world. For instance, a prominent criticism of recent proposals to cut food stamp benefits has been that it would harm not just the individual recipients but also the local economies reliant on the outside income. The U.S. Department of Agriculture promotes food stamp enrollment as a "win-win for local retailers and communities. Each $5 in new SNAP benefits generates almost twice that amount in economic activity for the community."[44] Food stamp recipients, in effect, are the community's "exporters."

Some speak of local health care systems as bright spots in depressed regions, but these industries usually indicate the government's commitment to health care as the surest way to generate hard currency for these economies. When the retiree on the front porch laments to a reporter, "When I was young we had dances at the community centers. Now they have nothing. No work around here unless you are a nurse, or a doctor, or lawyer,"[45] the list is not of especially productive professions, just those for which some government will pay. A common sight in the most dilapidated town is a sparkling occupational therapy office. The people working there are selling to the nation's taxpayers their care of the local residents on disability.

3. The Labor Market

How do we ensure that our economy creates jobs throughout the country and for people of all aptitudes? In an agrarian economy, most people worked on the land, producing directly the things their families needed. Capitalism has the labor market, which can seem like an abstraction, disconnected from everyday life. In the stock market, people bid on shares, their fluctuating prices scrolling across the electronic ticker. The supermarket overflows with produce bins and cereal boxes, each displaying a price that the potential buyer can take or leave. But finding a job or showing up for work seems different, somehow. After all, what is being bought and sold—a person, or his time, or some set of services? And who is doing the buying and the selling? We speak colloquially of workers needing jobs and of employers providing them, but workers are really the labor market's producers and the employers its customers.

In fact, like any market, the labor market is a tool for connecting people who wish to exchange one thing for another. A "job" is the relationship formed by someone who can perform work and someone who wants that work performed. The labor market's conditions—who can perform what kind of work and who needs what kind of work performed, what wages will be offered and accepted, and which rules govern work relationships—determine how many jobs exist, of what types, located where, and at what pay scale. The result aligns buyers and sellers engaged in mutually beneficial transactions.

It’s tempting to conclude, then, that the labor market largely should be left alone to do its thing. Let it find equilibrium, just like other markets, and the result will be an efficient allocation of resources that maximizes the economy’s output. If we’re unhappy with the distribution of benefits captured by the labor market’s winners and losers, then we can equip people to do better next time, or we can redistribute after the fact.

The problem with this conclusion is that, in one critical respect, the labor market is not like other markets: people are not products. This is obviously true with respect to the intrinsic worth of human beings. But the observation also has two concrete economic implications.

First, people are not created for the purpose of selling their labor, so the potential supply of prospective workers does not always respond to market signals. Perhaps under conditions of subsistence agriculture, when resources governed population growth, the available supply of labor was directly a function of the work to be done. But one triumph of modern civilization is that this relationship no longer holds. The decision to have children depends little on their economic value, for instance, and the survival of those children throughout their lives depends little on their own productive capacity.

Not only the quantities of available workers but also the characteristics of workers are determined to some degree independent of market demand. This is entirely the case with respect to natural endowments, and it is often true with respect to the familial and social environments in which children grow up. Among those showing a particular set of physical and mental skills, yes, we may have some success in tailoring training—encouraging more computer programmers and fewer accountants among analytically inclined college graduates, say, or more plumbers and fewer carpenters among tradesmen—but as the market’s persistent wage differentials make clear, even screamingly loud signals don’t automatically induce families to switch their “production lines” from cashiers to chemists. When the labor supply does adjust, it does so gradually—typically over the course of a generation. Job switching is common, but career switching, especially as people get older, is much harder. Retraining has met with limited success. In sum, the nation’s population is generally less flexible than the market would optimally desire.

This becomes a problem when it collides with the second economic implication of people not being products: society can’t be indifferent to where the price and quantity of work settle. Among a typical market’s core functions is to discover the price that brings supply and demand into alignment and to send that information to other potential buyers and sellers. Whether oil costs $50 or $100 per barrel, whether a new car costs $10,000 or $20,000, society wants to know. People may drive more or less and companies invest more or less in searching for new oil fields; consumers may upgrade to the latest model sooner or later and firms expand or contract assembly lines. In each situation, the market translates external conditions and individuals’ preferences into an efficient result.

Typical markets can cope with oversupply—but the solutions they reach aren’t of the kind that we can tolerate if applied to society’s members. When a business finds it has overproduced, it takes a loss. When economy-wide demand for oil declines, producers provide less. A widget will gladly sit on the clearance shelf until it is sold. That’s not how people work. An insolvent family can’t be acquired and restructured; an oversupply of workers can’t be written off like obsolete inventory.

That is what our current policy framework too often does: it writes people off. Labor becomes one economic input among many. If capitalists have the ability and the incentive to make the most productive use of all the resources available to them, in whatever combinations they see fit, they will create the greatest amount of output for consumption. And that output can then be shared (redistributed), even among those who did not participate. If the economically efficient solution is one that sidelines a sizable segment of the population, so be it.

This dynamic—society needing the labor market to absorb the available supply of workers at a sufficiently high wage, even though that supply remains imperfectly responsive to market signals—is at the heart of America’s economic challenges. *Productive pluralism* is not satisfied with an efficient labor-market outcome per se. It requires a particular outcome: the provision of sufficient meaningful work to sustain families and communities. If the labor market settles on an efficient outcome in which large segments of the population lack meaningful work, our response can’t be to say “thanks, understood” and then to wait for those displaced people suddenly to transform themselves into something else, or simply to give them government aid. Our response must be “that needs to change.”

The path to strengthening the labor market can start with the observation of Harvard professor Edward Glaeser: “Every underemployed American represents a failure of entrepreneurial imagination. . . . Joblessness is not foreordained, because entrepreneurs can always dream up new ways of making labor productive.”[46] Yet saying that entrepreneurs can always dream up new ways of making labor productive does not mean that they will. Only so many entrepreneurs put their time—and investors their capital—into so many businesses each year. If their most attractive opportunities involve the deployment of American workers, they will pursue that course. If investing in continual improvement of each American worker’s productivity is critical to their success, they will do that too. But if other workers are more profitable to employ than Americans are, or if business models that rely less on labor present them with lower risks and higher rewards, then those entrepreneurs—and the economy—will respond accordingly.

The answer is not to blame the labor market for acting like a market. Again, a market is a tool that translates underlying conditions into the most efficient outcome. Even when conditions bring a bad outcome, the market mechanism itself remains hugely valuable. It preserves liberty and fosters choice for individuals, creates incentives via competition for innovation and investment, and helps resources flow toward the most productive uses. To observe an inadequate result at the macro level, that is, is not to imply that we know the correct result at the micro level. *Productive pluralism* says nothing about who should work for whom or at what wage, and trying to outperform a free market in answering such questions would be foolhardy. Instead, public policy should focus on those underlying conditions: why is the market settling where it does, and under what circumstances would it settle somewhere better?

The labor market’s conditions dictate its behavior along five dimensions—and it can be improved along all five, depending on the trade-offs that society chooses to make:

Demand

What work does the economy need done? Consumer preferences and industry economics dictate much of the answer, but, at the margin, the rules that government puts in place can alter the balance. For instance, heavily regulating industrial activity and imposing stringent environmental regulation on physical infrastructure, while leaving the digital economy mostly free from regulation, will tend to constrict the demand for manufacturing workers, while expanding it for software engineers. Targeting taxes at energy-intensive activities, while aggressively subsidizing health care and higher education, will have profound effects on which industries stall and which thrive.

Over time, these kinds of choices can begin to affect consumer preferences and industry economics. Innovation will start to shift to those areas where entrepreneurs anticipate building the most successful businesses—whether that's in manufactured goods or high-end services, housing renovations or artistic performances. And where greater investment accumulates, the efficiencies of scale and expertise and supply chains develop too. A country consistently seen as the second-best location for a new factory watches as factories get built in other places, and the researchers and suppliers and distributors follow—and soon it isn't even the fifth best location.

Supply

What work are people prepared to do? The employer bears significant responsibility for training workers to meet its needs and improving their productivity over time. But for this investment to make sense, the worker must demonstrate basic capabilities at the outset. The better prepared the prospective workforce, the faster an employer can bring workers on board and the higher their wages will be.

The students to whom the education system tailors its efforts will experience the greatest boost in their work prospects. This emphasis will also influence demand, as entrepreneurs build businesses where they expect to find well-prepared workers. If public schools offer a wide range of programs and lavish attention on those connected to the weakest segments of the labor market, they can push outcomes in a positive direction. If they adopt an attitude of "college or bust," we shouldn't be surprised to find a workforce consisting primarily of college graduates and busts.

Boundaries

Who gets to perform work and who gets to purchase it? When trade and immigration policies expand the pool of employers and consumers demanding various types of work, the workers able to provide it will likely see more opportunities—and higher wages. But when policies dramatically expand the supply of workers able to meet existing demand, domestic workers will suffer. In establishing a labor market's boundaries, balance is therefore crucial.

Unfortunately, in a wealthy country like the United States, balance will rarely be achieved for less-skilled workers if residents of poorer countries can participate without limit in the same labor market. Entrepreneurs gain access to a vastly larger and cheaper supply of labor, while imperatives vanish to build businesses that use the existing domestic labor supply or make investments in improving domestic workers' capabilities. This effect swamps the smaller uptick in demand for less-skilled American labor that those workers might see from poorer countries.

Transactions

How do workers and employers establish and manage their relationships? The set of negotiable terms and conditions and the rules of negotiation have a significant influence on the nature of transactions in any market. This is triply true in the labor market, where overlapping regimes of contract law, employment law, and labor law govern the efforts of workers and employers to reach mutually beneficial agreements. Any contract they wish to sign must grapple with the myriad rules that government imposes about hours, wages, conditions, benefits, and much more. On top of those rules, the presence of a union may introduce an additional layer of collective bargaining, itself controlled by government rules.

In principle, allowing workers to bargain collectively should give them an opportunity to secure better terms than they might each achieve individually. Furthermore, by placing workers and employers on equal footing, concerns of unequal power and unfair agreements fall by the wayside, reducing the need for government dictates. Why does the Department of Labor need to set the standard for overtime pay when the parties can be reasonably expected to work out this issue for themselves? But done poorly, a system of organized labor can have the opposite effect, creating industry-wide cartels that negotiate agreements in the long-term interest of no one.

Taxes

How do the employer's total cost and the worker's take-home pay differ from the agreed-upon wage? The term tax is meant here in the broadest sense. Obviously, the direct taxes imposed on both employers and workers represent a large wedge inserted between the bargain that the parties might like to strike and the costs and benefits that they ultimately experience. But many other factors play a similar role, adding to the cost of becoming a worker or hiring one.

Conversely, government can offer subsidies that offset tax burdens or even raise the transaction's value to one or both parties beyond what the market offers. If society wants more from the labor market, it must consider paying for it. This can take forms ranging from tax credits for the employer or worker to direct subsidies that boost wages to better infrastructure that lowers transportation costs. Such policies are more expensive than other reforms, though.

Conclusion

In each of these areas, America's choices have been misguided. We overtax and underinvest in less-skilled workers, make them costly and risky to employers, and discourage investment in the industries where they could work most productively. At the same time, we free employers from the constraints of using the existing domestic workforce, offering them instead an option of using much cheaper foreign workers overseas or bringing the cheaper workers here. The immediate effects of these policy choices have often appeared beneficial, even to the workers who now find themselves disadvantaged. But those policies have, over time, reshaped the economy's contours in ways that have left too many people out.

Endnotes

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