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HOW TO STOKE THE MIDDLE-CLASS COMEBACK

By William A. Galston
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Although there may be some argument about which is which, the lion and the lamb are lying down together: President Obama and the editorial board of The Wall Street Journal now agree on the major problem vexing our economy. As Mr. Obama put it in a speech last week at Northwestern University, “Even when you’re working your tail off, it’s harder than it should be to get ahead. . . . [O]ur economy won’t be truly healthy until we reverse the much longer and profound erosion of middle-class income and jobs.” For its part, the Journal’s editorial page placed a chart with real median-income statistics since the late 1990s at the center of a recent lead editorial, making the point — familiar to readers of this column—that median incomes have declined, not only since the beginning of the Great Recession, but even since its official end in June 2009.

With the exception of the holders of capital, who have done very well in the past five years, almost no one likes what’s happening. The question is what to do about it. To answer that question, we need more clarity about the causes of middle-class decline than our political system has produced so far.

Instead, we’ve had an unproductive stalemate. Many conservatives attribute falling median incomes to a witches’ brew of administration policies: the stimulus, huge budget deficits during the recession, the Affordable Care Act and the termination of the Bush tax cuts for upper-income filers. By contrast, many liberals point to the decades-long weakening of labor unions, the eroding value of the minimum wage, trade treaties that destroy middle-class jobs and an inadequate public-sector response to the biggest economic crisis since the 1930s.

Despite their manifest differences, these contending forces have something important in common. They both assume that what we need is a version of past policies: a revival of either Reagan-era policies or the New Deal. Although I’m more sympathetic to the liberal narrative, in the end I find it inadequate. Our current problems have novel roots and won’t yield to backward-looking programs. As Edward Luce of the Financial Times put it in the title of his recent book, it’s time to start thinking.

I claim no originality for my views, which reflect tectonic shifts in the global economy over the past seven decades. Briefly: After World War II, the United States’ was the last economy left standing, and we dominated the world for the next three decades. As Europe and Japan recovered, things began to change. By the early 1980s, the heart of our manufacturing sector — automobiles and steel — came under increasingly intense competitive pressure, to which complacent corporate leaders responded sluggishly at best. In the next two decades, the collapse of the Soviet Union, the end of the Cold War, and the entrance of China and other Asian nations into the global market economy brought more than a billion low-wage workers into direct competition with American workers.

As new markets expanded and the costs of transportation and information declined, it became increasingly attractive to locate production facilities in those markets rather than in the U.S. The rising technology sector exploited these trends to the hilt. Unlike the industrial era, when innovation led to mass production in America, firms such as Apple pioneered a new model: a limited number of research and managerial jobs in its U.S. headquarters, backed by many times more production workers in other countries. Although some foreign corporations — especially Japanese auto makers — based production facilities in the U.S., it wasn't nearly enough to counteract the outflow.

And then the coup de grace for American workers: rapid advances in computer technology made it possible to substitute capital for labor not only in mass production, but further up the skills ladder as well, hollowing out a steadily widening center of the labor market. The Great Recession accelerated the decline: The majority of the jobs that unemployed workers have found thus far pay significantly less than the ones they lost during the crash.

Government can mitigate these trends but cannot halt them. "The modest earnings of the generation that technology leaves behind will need to be topped up with tax credits or wage subsidies," the editors of the Economist argue in this week's issue. In the longer run, wealthy democracies will have to invest more in basic research that boosts innovation and education that raises skills while tearing down barriers to business formation and entrepreneurially minded immigrants.

But that is the work of a generation. We need a plan to get from here to there. The workers that technology is forcing down the income ladder must be enabled to sustain their families and offer opportunity for their children. Like it or not, this will be a core function of government in coming decades.