



# La Follette Policy Report

ROBERT M. LA FOLLETTE SCHOOL OF PUBLIC AFFAIRS

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## DIRECTOR'S PERSPECTIVE

Besides celebrating a new century and millennium, the La Follette Institute is changing its name: We are now the La Follette SCHOOL of Public Affairs.

Funding has also increased for our School, thanks to four new donors, and we have added a new degree program—the Master of International Public Affairs—as well as new faculty.

We have also updated our look—in at least a couple of ways. At our “house” atop the hill overlooking Lake Mendota, we have a bronze bust of Fighting Bob La Follette, donated by his heirs. Having resided at the State Historical Society of Wisconsin for many years, it now is in the hallway of the La Follette School. Another symbolic change is demonstrated by the new graphic style of this report. We hope you like it and that you'll enjoy reading this issue.

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## Living Wages and College Logo Apparel: Are the Two Compatible?

*University logo apparel made in sweatshops has prompted students, faculty, labor, and religious leaders around the country to work to end the practice. University of Wisconsin–Madison students meeting with Chancellor David Ward agreed in February 1999 to hold a symposium to cover issues relating to a living wage for workers in the international apparel industry. The three-day symposium held in November 1999 was funded by the University of Wisconsin–Madison and hosted by the La Follette School on the Madison campus. This article summarizes the symposium. A copy of the complete report is available at [http://www.lafollette.wisc.edu/livingwage/Final\\_Report/report.htm](http://www.lafollette.wisc.edu/livingwage/Final_Report/report.htm).*

Participants at the UW–Madison Living Wage symposium heard about perspectives on a living wage including the structure of the apparel industry and its religious underpinnings. They discussed how to define and measure a living wage as well as the economic effects and challenges to monitoring such a wage. The symposium ended with discussion about future research, pilot projects, and the creation of a multi-university consortium to address living wage and sweatshop issues.

### Perspectives on a Living Wage

The living wage movement is part of an earlier minimum wage movement in this country, according to University of Massachusetts-Amherst professor of economics Robert Pollin. Then, as now, the argument went, workers were entitled to earn enough to support their families, to maintain self-respect, and to have both the means and the leisure to participate in civic life. Medea Benjamin, of the human rights organization Global Exchange, compares a living wage to pornography: “It’s hard to define, but you know it when you see it.”

### Development of the Apparel Industry

The main story in the development of the clothing industry, according to Richard Appelbaum, an expert on the apparel industry at the University of California, Santa Barbara, is the enormous growth of imports in the last thirty years or so (see figure 1).

The United States now imports about \$50 billion worth of clothes each year, approximately two-thirds of all new clothing purchased in the United States. These are not imports in the traditional sense—products designed in other countries by manufacturers in those countries and then exported to the United States. Rather they are designed by U.S. businesses—retailers and manufacturers—and then fabricated by a global workforce and sent back to the United States as finished garments.

Appelbaum noted that although the primary factor that concerns many people involved in the current debate is wages, the wage portion of the cost of clothing is small—about 6 percent of the total cost of an item that is manufactured in the United States and considerably smaller for imports. Increasing the wage component by itself, he

argued, would not be likely to raise the cost of the clothing significantly. Wage pressure, he said, may not be the only factor driving companies south of the border.

### *Structure of the Industry*

The unique structure of the clothing industry relative to other types of manufacturing is the other important factor to consider when trying to understand apparel-making. Unlike U.S. companies that open an operation in another country (say, Goodyear with its own factory in Indonesia), the apparel industry has disparate layers and lines of accountability, lines both visible and invisible.

Appelbaum explained that following the consolidation of the clothing industry in the last decade, four large retailers now account for about two-thirds of all retail clothing sales in the United States. Wal-Mart is the largest with about \$138 billion in sales (in 1998), followed by K-Mart, Sears, and Dayton-Hudson. The retailers place orders with manufacturers who actually design the clothing and also eventually market finished garments to the retailers. Between designing and marketing, however, the manufacturers hire independent contractors—usually in other parts of the world—who in turn employ either another layer of contractors or the garment-makers themselves (see figure 2). The Gap, according to Appelbaum,

uses “approximately a thousand factories around the world.” The lines from retailers to manufacturers to contractors to subcontractors to sub-subcontractors are crosscutting. Each contractor has orders from numerous manufacturers and retailers. A tour through a garment factory in Los Angeles or in Asia or Mexico would reveal racks of clothes with many different labels, all side by side.

### *Religious Underpinnings*

About five years ago, religious workers at a Baltimore soup kitchen noted lengthening food lines, according to one symposium participant. The new people coming were not unemployed but their pay was too low to afford a reasonable diet.

Among other things, this story points to the fact that religious leaders are primary players in the living wage movement, that the religious perspective is an important one, and that it is articulated by practitioners of a number of faiths.

At the symposium, Todd Whitmore of the University of Notre Dame described Roman Catholic social teaching relating to the subject, and David Schilling explained the work of his ecumenical group, the Interfaith Center on Corporate Responsibility (ICCR).

According to Whitmore, a canon of texts—beginning with a doctrine expressed by Pope Leo XIII in 1891 and most recently expressed by John Paul II—articulates such values as “the common good,” “solidarity,” “participation,” and “option for the poor.” What underlies these values is the theological premise that all life is created by God, all created life is good, and since God created everything, everyone ought to be able to share it. According to Whitmore, Catholic theology holds that humans are social by nature and by design, that the family and communities they form are necessary for human fulfillment. This is a different approach than classical liberal thought that tends to honor solely the individual and self-interest.

David Schilling of the ICCR described the ecumenical movement against sweatshops and noted that religious leaders of all sorts—rabbis, popes, and various Protestant Christian leaders—have long considered a living wage to be an issue of human dignity and justice. The ICCR has 275 institutional members that have investments in many of the U.S.-based multinational corporations. As a shareholding organization, the ICCR has ongoing relationships with the companies, filing shareholders’ resolutions and meeting with top management on a wide range of issues, of which the living wage is but one. This group strongly urges attention to the already issued International Labor Organization (ILO) conventions, United Nations (UN) declarations, and human rights covenants.

## **Defining and Measuring a Living Wage**

Whether in industrial or developing countries, two basic approaches have been applied to income and living standard measures, and several basic methodological

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approaches have been developed for defining and measuring a living wage. The basic approaches have included minimum wage standards for regions, industries, or nations; and poverty lines or living wage standards.

### Minimum Wage

The minimum wage is a social and economic construct that has been around since the Great Depression in the United States. Robert Pollin, author of *The Living Wage: Building a Fair Economy*, argued at the symposium that commitment to social justice needs to be combined with economic analysis in order to consider what the benefits are of raising wages and whether it can be done without prices and unemployment rising.

Pollin showed that in the United States the minimum wage peaked in 1968 at \$7.49 per hour (in 1998 dollars) and has now fallen to about \$5.15 (see figure 3). It has fallen not just relative to the rest of the American economy, but in absolute terms. In 1968 the minimum wage for a family of three would put them 17 percent above the U.S. poverty line, but now they would be 20 percent below the line. Businesses frequently say they can't raise wages without productivity first rising. But productivity, according to Pollin's analysis, has gone up 50 percent since 1968 while the minimum wage, when accounting for inflation, has fallen by 30 percent.

Pollin's time-series graphs suggested that there is no statistical correlation between unemployment and the minimum wage and that a higher minimum wage thus will not cause higher unemployment, one of the "negative feedback loops" that mainstream economists fear.

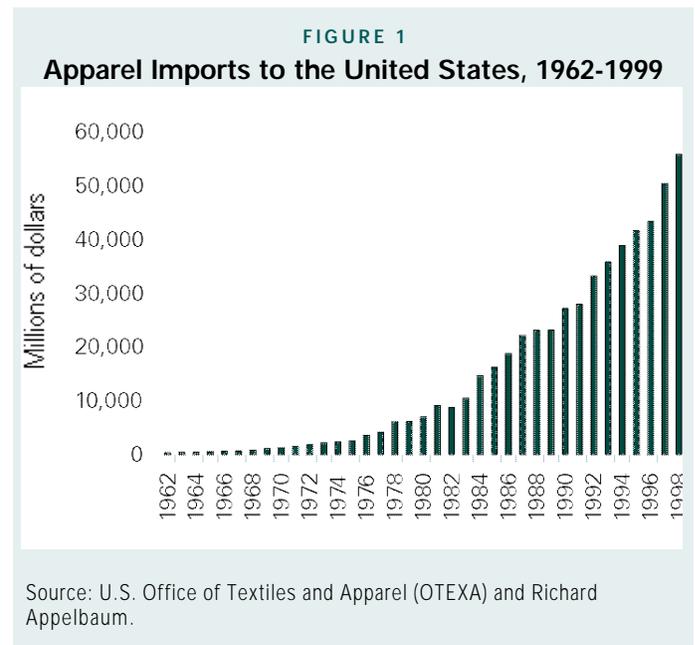
Although this analysis includes the entire workforce, when doing the same analysis with only the teenage labor market (in which a majority of those with jobs earn either the minimum wage or only slightly more than the minimum), Pollin had similar results. He found no statistical correlation between changes in the minimum wage and teenage unemployment.

A higher minimum wage would cause increased unemployment, he argued, if all else remains equal in the economy after wages are raised. The rise in unemployment then would follow from the law that when the price of something (low-wage labor) goes up, demand (to hire low-wage laborers) goes down. But the fact is, he says, that all else rarely remains equal when minimum wages go up.

The most important additional consideration, Pollin argued, is that if overall demand for goods and services in the economy is strong, businesses will still want to hire low-wage workers even after the minimum wage increases. In addition, when minimum wages are raised, this is likely to raise firms' productivity, because turnover and absenteeism would fall, which then also means that the costs of training and supervising workers would also fall.

### Cost of Living

Vietnam, one of the poorest countries in the world for which data are available, has been experiencing



economic growth since the late 1980s. At that time the state planning system ended, the country began a market economy, and foreign investment began—especially from Korea, Japan, and Taiwan.

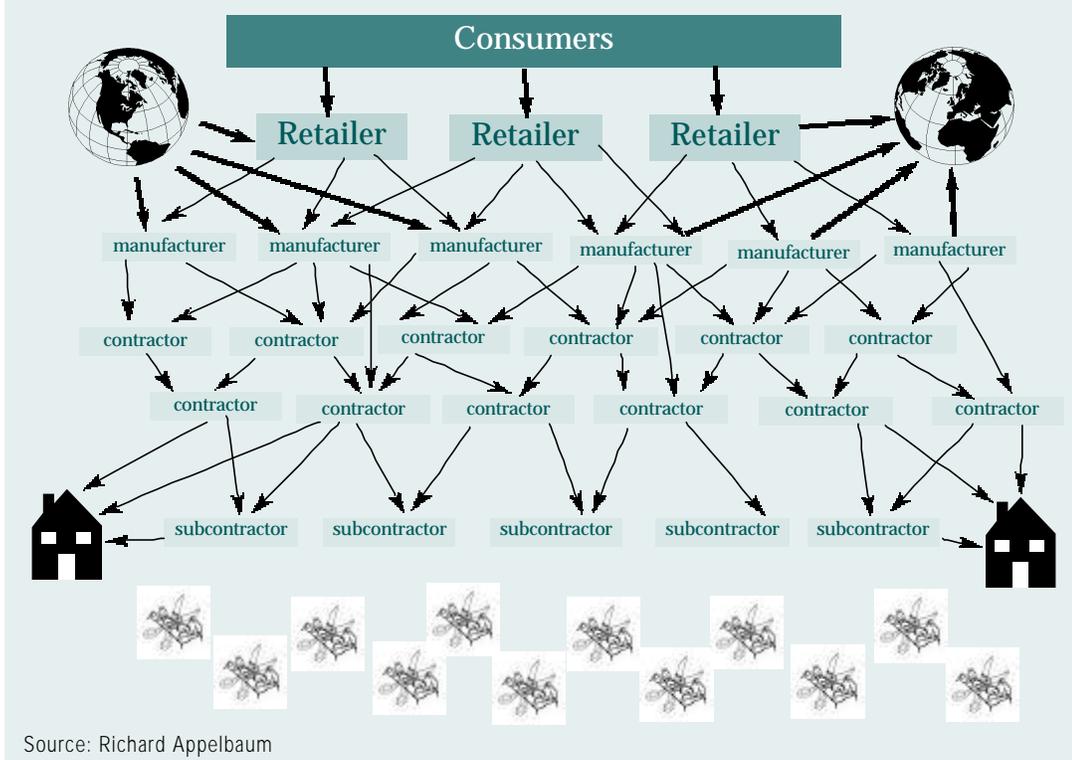
Paul Glewwe, a World Bank analyst on leave doing research at University of Minnesota, shared data on two wage and cost-of-living studies done in Vietnam—one in 1992-93 and one in 1997-98. The 1992 survey was of 4,800 households; the 1997-98 one was of about 5,000; 4,300 households were covered in both surveys. The surveys covered households in which someone in the home had worked in a paying job in the last seven days, and it covered income, expenditures, food consumption, health, savings, and prices, among other things.

While Vietnam is an exceedingly poor country, the two surveys showed that it is less poor than it once was and those working for foreign-owned enterprises (who were not in the 1992-93 survey) are better off than the general population. None are in the lowest 20 percent of the income distribution. That's still not saying much, according to Glewwe, but establishing a living wage that would be applied in foreign-owned enterprises would not help most of the Vietnamese people.

Ruth Rosenbaum, in her Connecticut organization, the Center for Reflection, Education, and Action Inc., has been collaborating with workers in Haiti, Indonesia, and Mexico to develop one method for determining a living wage based on cost of living. Her "purchasing power index" ascertains how many minutes a person must work at a certain wage in order to buy the items necessary for subsistence. For example, in Haiti in 1992, a person could buy a kilo of rice with 59 minutes of purchasing power (minPP). In 1996 the same worker needed 106 minPP for a kilo of rice. In Indonesia a worker needed 98 minPP and in Matamoros, Mexico, 35minPP.

To determine minutes of purchasing power, Rosenbaum and her staff, in cooperation with other

FIGURE 2  
Structure of the Apparel Industry



Source: Richard Appelbaum

nongovernmental organizations (NGOs), develop a pricing list specific to the country or region they are studying. To do this they include prices from actual shopping areas that workers patronize. Each price is then converted to the number of minutes of purchasing power required for the purchase.

Rosenbaum argued that combining the effects of wages, prices, and inflation into a single number allows assessment of the purchasing power of a worker after putting in an ordinary work week—in any currency, in any factory, in any region. It allows calculating the effects of overtime, bonuses, or benefits—in any country or region. Because the methodology allows a comparison of purchasing power from one region or country to another, it also allows study of the effect of a business moving from one region or country to another. It also allows analysts to see improvements or decline of wages or changes in inflation because it allows comparisons over time.

## Economic Effects

Two sets of issues are at play in trying to improve work and living conditions for workers engaged in producing college logo apparel. The first is whether and how to raise wages and create decent work environments. The second is how to get firms to operate transparently, which entails disclosing their activities, allowing monitoring, and allowing workers the right to organize collectively.

wages of more highly paid workers in the affected firms; or by the colleges and universities that earn fees through licensing their logos.

Nevertheless, as a fallback position, it is worth asking whether, if prices in consumer markets were to rise for college apparel, demand for the apparel would fall by a significant amount. If it did, that could bring cutbacks in the production of the apparel, and subsequent job losses for the workers producing these goods—precisely the type of unintended consequence (or “negative feedback loops”) that supporters of living wages need to commit themselves to avoiding, as much as possible.

Relatively small increases in college apparel prices on the order of 5 percent to 10 percent, in the judgment of some symposium participants, would not cause a decline in the demand for these products, especially if it were clear to consumers that the price mark-up was paying for higher wages and better living standards for the workers producing the apparel.

Universities earning licensing fees might also themselves absorb some of the cost increase, others suggested, at least in the initial phases of a living wage regime. This would mean that prices for these products could rise more slowly than otherwise.

### *Where to Set a Living Wage Standard?*

There are two basic standards through which one might establish what constitutes a “living wage” in any given setting. The first is a “consumption standard,” which establishes a living wage based on the costs of purchasing a basket of consumption goods that meets

### *Demand for College Apparel*

If wages rise and workplace conditions improve at the plants producing college logo apparel, economic theory dictates then that the costs of producing this apparel will rise. Those costs will have to be borne somewhere between the point of producing the apparel and its final sale. According to some symposium participants, it does not follow that these costs have to be borne by the final consumers of the apparel through price increases. The costs could also be absorbed by the profits of the companies marketing the apparel and its allied subcontracting firms; by the

the basic needs of a worker and his or her family. The second is a “local conditions” standard which, while recognizing the central importance of workers meeting their basic needs, also takes into account the status-quo wage standards in a given labor market.

From a social justice point of view, the consumption standard would seem to be the more appropriate measure, since it would ensure that the basic needs of workers are met. A consumption standard, however, could produce serious negative feedback loops, including the following:

- (1) Firms may concentrate their production of college apparel in high-wage countries, moving more of their other operations to the lower-wage economies. This would enable them to avoid facing significantly higher labor costs of college apparel production in the low-wage countries. Perhaps even more important, it would also allow them to avoid negative publicity.
- (2) Firms could maintain production in the low-wage economies but create small high-wage enclaves within them. This would certainly benefit those workers lucky enough to have jobs within the high-wage enclave. But because wages would be set at a level well beyond what the rest of the market will bear, the living-wage standard within the enclave would probably have little positive effect on the rest of the local labor market.

Setting the wage too high relative to local market conditions could create difficulties for monitoring, according to some participants. This, they said, is because a strong incentive would be created to circumvent the wage mandate. For example, workers could sell a share of their high-wage jobs under the table to their relatives or friends so that, in fact, multiple workers are employed at a single “living wage” job. Given these concerns, it might be necessary to combine a consideration of a consumption standard with a clear assessment of the local market conditions.

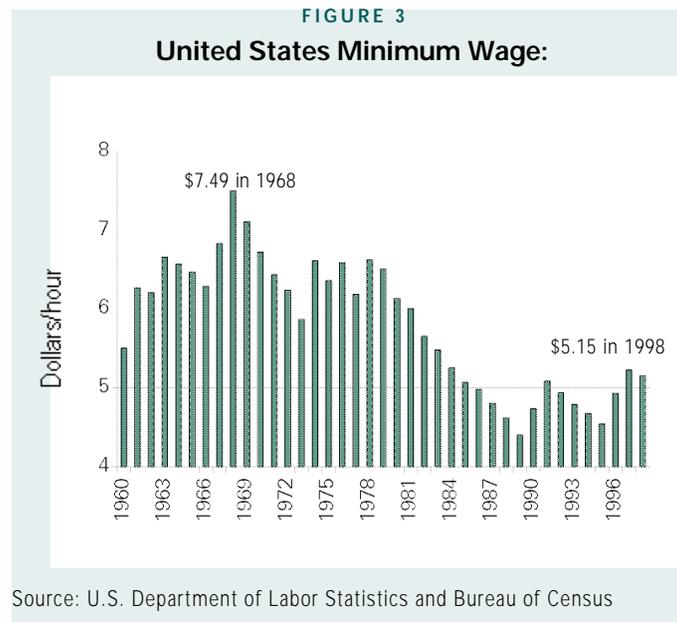
### Organizing Workers

What would be the wage bargained for by workers if they were allowed to organize and bargain collectively? There seem to be no clear-cut answers. For one thing, few countries, especially in developing economies, have strong labor histories with an established tradition of collective bargaining rights. In addition, even if free collective bargaining did prevail, the outcome of the bargaining

process would depend on local labor market and macro-economic conditions. For example, the wage bargain achieved by workers in a full-employment environment would be very different from one achieved when the unemployment rate is 25 percent of the workforce.

Nonetheless, if appropriately applied, this approach to gauging local market conditions may be one beginning point.

Positive collateral effects could also emerge from working with a standard of measuring local market conditions, which would be to strengthen demands for open bargaining and workers’ rights. Working from this principle for measuring a living wage would also reinforce an emphasis on openness and transparency among the firms producing college logo apparel.



### Broader Effects of Standards

Although a living wage standard applied only to workers producing college apparel might have minimal effects, it could also have “ripple effects”:

- (1) **Employment Effects.** The primary traditional argument against any minimum wage mandate is that low-wage workers will lose their jobs. Some participants, citing the work of economists David Card of the University of California–Berkeley and Alan Krueger of Princeton University, expect, however, that the demand for college logo apparel would not fall if the price of the apparel went up. Perhaps, then, there would be no incentive for firms to lay off workers, even if they are being paid a living wage.
- (2) **Productivity Effects.** Ideally, productivity would rise. “Soft productivity” gains might result from workers being in a cleaner, more open environment and getting paid more. This would reduce absenteeism and turnover, increase effort, and thereby also reduce supervisory costs. There might also be “hard productivity” gains when, faced with higher wage costs, firms substitute machines for people in their production processes. Both types of productivity gains could cause employment losses, or at least a reduction in the rate of job creation because increasing productivity means that fewer workers are needed to produce a given level of output.
- (3) **Redistribution Effects.** Redistribution might occur in two basic ways: from firm owners to the low-wage workers, or from higher-wage earners to low-wage earners. Social justice advocates support

downward redistribution—from firm owners to the low-wage workers—or some “wage compression” between low- and higher-wage workers.

## Monitoring a Living Wage

Jonathan Rosenblum, counsel to the International Labor Rights Fund in Washington, D.C., outlined the differences between industry, human rights, and university-based monitoring proposals and how they developed. The 1990s effort to control working conditions and wages in the fractured contracting system of multinational manufacturing has gone through several iterations. These include establishing individual company codes of conduct, followed by creation of the Fair Labor Association (FLA), an early university initiative by Collegiate Licensing Company-represented schools, and most recently the proposal for the Worker Rights Consortium (WRC).

### *Codes of Conduct*

For eight months—from August 1996 to April 1997—the FLA’s predecessor, the Apparel Industry Partnership (AIP), met to establish a code of conduct for humane labor conditions by apparel and footwear manufacturers. President Clinton created the task force to respond to problems in garment manufacturing plants in the United States and throughout the world. AIP included unions, companies, human rights groups, and, toward the end of its work, one university—Duke. Among other things, the code limited regular work hours to 48 hours per week, plus 12 hours of overtime per week; required one day off in every seven-day period; and required that no employees be younger than 14 or 15, depending on the country. Other provisions followed the basic framework of rights and standards established by the International Labor Organization.

Universities, on the whole, were not involved. Students were active, but not schools themselves (except Duke.) Students then began to focus on one segment of the manufacturing trade where they might hold sway: the estimated \$2.5 billion college merchandise industry that included baseball caps, mugs, banners, sport uniforms, jackets, and T-shirts. With major campus activities such as sit-ins and teach-ins, they persuaded their administrations to join in the discussion and implementation of the code. Many colleges adopted all or part of the AIP code.

### *Fair Labor Association*

The AIP code alone soon proved to be inadequate for many students, labor right activists, and nonprofit groups. They argued that universities were left out of the mix and that corporations had too much power in setting the code. The White House-sponsored coalition of corporations and human rights groups came up with the Fair Labor Association (FLA) as the next step in implementing protection for workers. Some colleges and

universities started working with the FLA as a way to reach higher standards. By June 1999, more than 100 campuses had affiliated themselves with the FLA.

The FLA code embodies nine elements, including child labor, forced labor, freedom of association, collective bargaining, and more—all part of the International Labor Organization standards.

Students have since argued that the FLA is controlled by corporations. The governing body of the FLA is composed of six corporate members, six NGO or human rights members, one university member, and one chairperson chosen by both sides (NGO and corporate) who is to be neutral. University representatives were provisionally selected co-chairs from Duke and Notre Dame who serve as board members of the university advisory council.

### *Worker Rights Consortium*

One of the main principles of the fledgling Worker Rights Consortium (WRC) is to allow local NGOs access to factories in order to educate workers about codes and develop trusting relationships with the workers and the NGOs. Leadership wants to start pilot projects to begin testing educational strategies and a range of complaint mechanisms with workers in different countries. It would use local organizations to verify company-reported information with the workers. Where NGOs are not allowed, a more traditional form of monitoring could be used, such as sending in an auditor.

### *Monitoring Concerns*

Several problems occur that make monitoring difficult. One is the high degree of mobility among businesses—contractors move, go bankrupt, open under another name. One Department of Labor study showed 56 percent of factories in Los Angeles were in business less than two years.

Another problem is that companies can and do hide contractors because they are thus far not required to disclose the entire list of factories they use. They may monitor their good factories and use others for short runs or quick turnarounds.

Finally, one of the biggest problems, according to activists, is that workers are not involved in the monitoring process. Monitors hired by professional auditors question employees on site, do not promise confidentiality, and the employees are sometimes threatened or fired for speaking out against their employers or about the conditions under which they work.

## Conclusions

Participants in the Living Wage symposium seemed to agree on at least two things: First, exploitation of workers in the apparel industry does occur, and it should end. Second, records of businesses should be available so as to determine the costs of production and the wages and working conditions of workers.

Unresolved questions included the following:

- Should U.S. companies be involved in apparel manufacturing in countries where wages are substandard?
- Should the federal government attempt to draw up (or ratify) international agreements that would require improved wages and working conditions in the apparel industry?
- How could benchmarks be established for wage rates and working conditions that would be acceptable to businesses, to governments, and to workers?
- If agreement could be reached on benchmarks and an international accord attained, who would monitor the agreement? How? Who would pay?
- What steps can be taken to assure humane treatment of workers and end exploitation?
- How can American consumers bring pressure on businesses that contract or subcontract their work to developing countries?
- How can governments regulate businesses?
- How can American universities collaborate to bring pressure on businesses and/or consumers? Which organizations should they join and collaborate with?

Despite these remaining questions, three general conclusions emerged from the symposium.

(1) Multi-University Consortium. A consortium of universities should address living wage and sweatshop

- issues—to further understanding of consumption costs and wage levels in some logo apparel supplying factories and regions, to encourage research on the economic effects of raising wages, and to explore how to monitor supplier compliance with agreed-upon codes of conduct.
- (2) Pilot Projects. The consortium should sponsor pilot projects in several countries that make a considerable amount of logo apparel. Such pilots should include measuring consumption and wages in one or more regions, and assessing and testing various approaches to monitoring.
- (3) Future Research. The consortium should plan and sponsor further research on the economic effects of a living wage. Three types of issues and studies were envisioned:
- a study of the demand elasticity in the logo apparel industry;
  - a study of the cost structure of the industry, especially the labor costs that go into the products; and
  - research on the “ripple effects”—both positive and negative—of higher wage standards. Further research is clearly needed on industry relocation effects.■

## La Follette Programs To Benefit from New Donors

At the same time that La Follette is transforming itself from an “institute” to a “school,” its research and educational activities are receiving increasing attention. Four benefactors have recently provided generous funds for encouraging more of the research, educational, and outreach activities that define our school. The faculty, staff, and students at La Follette are grateful for the support of these generous donors as they help us meet our program goals. Many of these donors established funds with the hope of encouraging other alumni and friends to support the La Follette School. If you would like additional information on making a contribution to any of these funds or establishing one of your own, please contact Beth Wells at the UW Foundation at (608) 263-9337.

**Emanuel “Manny” Lerner** (B.A. 1932, M.A. 1933, Economics) established the John Gaus Public Service Fund in memory of the distinguished former member of the UW–Madison’s Political Science Department and devoted public servant. The fund provides support for students planning a career in public service, an ideal which John Gaus’s life exemplified. Gaus was one of the first political scientists to combine practice in government with teaching and research. His accolades and accomplishments, too numerous to mention, include multiple honorary degrees and an American Political Science Association award named in his honor. John Gaus loved UW–Madison, and we would like to think he would be most proud of this latest honor.

The **Daniel Louis and Genevieve Rustvold Goldy** Public Policy Fellowship Fund provides support for faculty members conducting interdisciplinary research on emerging policy issues. A protégé of Edwin Witte’s, Dan Goldy is a 1936 graduate in economics from the University of Wisconsin. He was a public servant in the Truman, Kennedy, and Johnson administrations and continues to have a strong interest in public service and the study of public policy. The Goldys visited La Follette recently on a stop between their home in Portland, Oregon, and Washington, D.C.

**Clara Penniman**, emeritus political science professor at the University of Wisconsin–Madison and one of the founders of the Center for the Study of Public Policy (precursor to the La Follette School of Public Affairs), has established a fund to provide fellowship support for students. Professor Penniman taught courses in budget and tax administration and has a large number of former students working at all levels of government. She also supports a prize, bestowed at La Follette’s graduation ceremonies each year, for the best student research paper.

The family of **Laurie Carlson** established the Carlson Memorial Fund in his honor to fund an annual lecture series featuring speakers in the Progressive tradition. Carlson was a lifelong supporter of the La Follettes, was a member of the original Progressive Party, and served admirably in the Wisconsin legislature. Devoted to the public service, Carlson inspired similar ideals in his children. The first Carlson lecture was given this spring by Carlson’s daughter and son-in-law, Maya Carlson and Tony Earls, co-principal investigators in an eight-year study of Chicago neighborhoods by the Harvard University School of Public Health.

# Reinventing Reinvention: Reforming the Federal Bureaucracy in the New Century

by Donald F. Kettl

*Donald Kettl is professor of political science and public affairs at the University of Wisconsin–Madison. He is currently chairman of Governor Tommy Thompson’s Blue Ribbon Commission for State-Local Partnerships for the Twenty-first Century. More information about the commission is available on the La Follette School website at <http://www.lafollette.wisc.edu>. This article is a shortened version of an article published in Government Executive magazine. © 2000 by National Journal Group, Inc., publisher of Government Executive. Reprinted with permission.*

The 2000 presidential election sharply focuses two separate questions on the Clinton administration’s reinventing government campaign. If Al Gore becomes president, what will the next phase of reinventing government look like? If Bush wins—what will become of reinventing government?

The answer to the second question is easier. If anyone other than Al Gore sits in the Oval Office in January 2001, one of the new president’s early acts will be to abolish the National Partnership for Reinventing Government. That, however, will have to lead to its re-creation (under a different name) soon thereafter. The pressures for reforming federal management won’t evaporate.

That takes us to the first question. If the federal management reform movement will continue in some form, what will that be? Can the bureaucratic culture really change? Or are we doomed endlessly to push the rock of reform up the hill of reality only to have it roll back and squash the efforts?

## Gore and Reinventing Government

Reinventing government had remarkable staying power during the Clinton administration. Gore devoted remarkable energy to the issue over a very long time. The fact that he stood by reinventing government despite many distractions—the impeachment crisis was just the biggest of them—says something fundamental about his commitment to the cause.

But things would surely be different in a Gore administration. Even though we call our president “chief executive,” he spends little time managing. No matter how much Gore might care about reinvention efforts, as president he would have to hand primary responsibility for reinvention over to someone else—or take the risky step of making management a centerpiece of his presidency.

The political capital to be gained by touting reinvention has also proven small. Despite seven years of effort, reinventing government has barely penetrated voters’ consciousness. Only a little more than half of those surveyed in a June 1998 Scripps Howard News Service poll had heard of the term “reinventing government.” Most respondents—61 percent—did not believe that government had become more efficient, and 59 percent did not believe that the Clinton administration had reduced the number of federal employees. Federal employment

shrank, in fact, by 351,000 positions—more than one of every seven workers.

Earlier phases of reinventing government had failed to hold off the Republican “Contract with America” siege. The much-touted notion that the federal bureaucracy was smaller than at any time since the Kennedy administration got little attention in the 1996 presidential election. Reinventing government has, at least so far, played only a tiny role in the 2000 campaign—limited mostly to journalists probing it for keys to Gore’s character.

## Reinventing Government after Gore

What if George W. Bush wins the election? No non-Gore presidency would publicly embrace the reinventing government campaign, so the National Performance Review and the parade of Gore’s “Hammer Awards” would surely end.

But that only sharpens the problem. Congress has passed the Government Performance and Results Act, which requires agencies to write strategic plans and measure results of their programs. The new administration will have to make sure that agencies do this correctly, if only to avoid sniping from Congress. That means, at a minimum, that the president will have to ensure that the Office of Management and Budget continues to invest in government performance.

Even more important is the predictable unpredictability of management fiascos. As reporters become more aggressive and television news magazines have more hours to fill, the hunt for government scandals continues to grow. “Waste-fraud-and-abuse” has become a single word in the media.

In an institution as complex as government, opportunities for scandals are ever present. Government, after all, gets only society’s hard problems—the ones the private sector doesn’t want to or can’t handle. It also gets the public’s impossible dream: an endless appetite for ambitious federal programs along with an endless demand for tax cuts.

Management scandals—such as slow responses to natural disasters, abuses by tax collectors, or the failure of a missile system—are the one predictable feature of the federal government. Add to that the real definition of waste, fraud, and abuse—a program that benefits someone else—and one thing is clear: Whether the new

president wants to “reinvent” government or not, the winner will sooner or later be faced with the political necessity of doing something to improve the way government works.

The nation’s economy adds a wild card to the deal. Through skill, cooperation with the Federal Reserve Board, and a fair measure of luck, the Clinton administration has enjoyed a long stream of economic success. But odds are increasing that the next administration will have to deal with sluggish growth, at least for a while. If that happens, the pressures for management reform, in order to squeeze more services from tax revenues, will grow.

Thus whoever succeeds Bill Clinton will sooner or later have to craft his own brand of reinventing government. That is the lesson from governments throughout the world, virtually all of which have launched major management reforms.

It also means that the new president will have to cope with the political dilemma of management reform. While reform has become unavoidable, there’s still little evidence that it provides great political reward. Thus the new president might find himself with few incentives for continuing the Gore effort, yet little alternative but to do so.

## Culture Blocks

It would be tempting to chalk up the inevitability of reform (and the predictability of its failure) to the entrenched bureaucratic culture. It isn’t difficult to convince cynical Americans that government bureaucrats are in business for themselves more than to do the people’s business.

Even in the heat of the Gore reinventing government campaign, some stories seemed to support the cynicism. In 1997, Republicans savaged the IRS—and the Clinton administration—for mistreating citizens. Congressional hearings spotlighted problems ranging from armed agents busting up businesses to citizens who couldn’t get straight answers to tax questions. The Republicans quickly forced the Clinton administration to accept a new quasi-private governance board to run the tax agency. In fact, they were so successful so quickly that the issue had nearly evaporated before the 1998 congressional elections.

The administration responded by bringing in a new commissioner, Charles Rossotti, and launching a major effort to become more customer-friendly. It created one of the government’s jazziest web sites, with lively graphics and quirky news stories. The IRS started providing tax regulations in plain English, set up “problem-solving days” to give taxpayers face-to-face relief, and greatly expanded its telephone hotline service.

In short, the IRS scrambled to meet the reinvention government mandate to become more customer-friendly.

The agency might not have avoided the crisis had it moved more aggressively much earlier, but it surely would have defused the conflict and robbed it of its political value. Instead, the IRS found itself a poster child for what happens to agencies who fail to take reform seriously.

Likewise, the Energy Department (DOE) has been rocked by charges that sloppy handling of nuclear secrets allowed the Chinese government access to some of the nation’s most sensitive technology. Congressional Republicans, led by Senator Pete Domenici, R-N.M., blamed the Clinton administration, though it wasn’t clear that the

Chinese had actually stolen secrets from the nation’s labs or if they had, when it had happened. What actually

happened didn’t really matter—the administration’s congressional critics became determined to reorganize DOE to prevent future security lapses.

In mid-1999, Congress created a new office to oversee DOE security. The plan was to separate the job of safeguarding nuclear materials and secrets from the job of manufacturing and maintaining weapons. Congress did not trust the people who managed the nuclear complex to protect its secrets. And some Republicans may have relished the chance to embarrass the Clinton administration. But Clinton outflanked them and appointed DOE Secretary Bill Richardson to head the new office, at least temporarily. The Republicans, predictably, were furious.

Beyond the partisan sparring, however, lay a tough question: Would the new office actually promote national security? The employee suspected of sloppily handling the secrets actually worked for the Los Alamos National Laboratory, a facility long operated by the University of California under contract to DOE. The department’s problems stemmed from a 50-year-old culture of relying on contractors to do its work. Scrambling the headquarter’s structure is likely to have little impact on the contractors and might actually distract top officials from leading the kind of culture change that the scandal shows is needed.

The IRS and DOE had similar problems: dysfunctional bureaucratic culture, slowness in launching reforms, a crisis that brought demands for revolutionary change, and the difficulty of catching up. The two agencies’ stories drive home two enduring truths about reinventing government. First, it has been a highly variable effort. Despite large (and often justified) claims of success in some agencies, others lay largely untouched. Some of the administration’s own appointees have been uninterested in following the reinventing government plan. Second, the biggest federal management problems during the Clinton years occurred in the agencies where Gore’s reinvention efforts penetrated the least. If reinvention failed to produce political gains for the Clinton administration, non-reinvention often provoked embarrassing crises.

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It’s about getting the right leaders into place in agencies throughout the government

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## Culture Changes

Reinventors elsewhere, however, proved far more successful in transforming their agencies. For example, James Lee Witt turned the famously troubled Federal Emergency Management Agency (FEMA) around. FEMA had long been a lightning rod for criticism. Every hurricane, earthquake, tornado, and flood, the joke went, brought two disasters: one when the event occurred, and the second when FEMA arrived. Hurricane Andrew, which devastated South Florida in 1992, was FEMA's Waterloo. Critics charged the agency with malfeasance in getting aid to victims, and President Bush found himself fighting off charges of mismanagement in the heat of the election campaign.

Witt quickly seized the reins. He stood in the agency's doorway one morning to greet employees and signal his commitment to changing the culture. He worked with his staff to improve FEMA's management systems. He built closer ties with state and local officials, as well as voluntary organizations, private companies, and other federal agencies. He rebuilt FEMA's operations from its customers' point of view.

FEMA's new strategic plan, in fact, points to a radical change: Instead of responding to disasters, FEMA now pledges to "proactively help communities and citizens avoid becoming disaster victims." Instead of delivering disaster assistance, FEMA focuses on coordinating a broad disaster relief strategy with responsibility shared by a large number of partners.

When tornadoes hit the Midwest, an earthquake rattled the Los Angeles area, and Hurricane Floyd clobbered North Carolina last summer, FEMA's partnership model got more relief to victims faster. News stories on agency mismanagement disappeared. FEMA's managers had transformed the agency's culture as a strategy for transforming its mission.

Likewise, David J. Barram, head of the General Services Administration (GSA), turned that agency on its head. GSA had a reputation as the federal government's stodgy landlord and supply warehouse. Labels like "bloated" and "red tape" accompanied most stories about its operations. But Barram, with nearly a quarter century of experience in Silicon Valley, brought a new style to his agency. He pledged not just to satisfy but to "thrill" GSA's customers in other agencies. With a

straight face, he said, "We want our customers to wake up each morning and think, 'Boy, am I glad that GSA exists!'" He launched "changemasters" to help administrators master new management approaches. Most of all, he committed GSA to a culture of service.

The campaign led to negotiations that brought a 68 percent discount on airline coach fares for federal travelers and long-distance telephone rates for federal offices of just 4 cents per minute—so cheap they're not even worth auditing, GSA officials claim. The agency's award-winning "GSA Advantage!" web site ([www.fss.gsa.gov/cgi-bin/advwel](http://www.fss.gsa.gov/cgi-bin/advwel)) offers federal employees easy online access to a million products. The quiet word in federal agencies is that this indeed is a new GSA.

## Making Change Stick

If DOE and the IRS show the painful costs of falling behind in the reinvention race, FEMA and GSA show that strong leaders can indeed change bureaucratic culture. The struggles in DOE and the IRS, moreover, underline why government reform has become inevitable. Holding onto the status quo encourages similar disasters. Coping with the rapidly changing social and political environment, on the other hand, requires aggressive leadership.

The real story of Gore's reinventing government, in fact, is not so much of reinventing the bureaucracy from the White House. Rather, it's about getting the right leaders into place in agencies throughout the government, focusing them on real reform, sweeping away at least some dysfunctional bureaucratic debris, and turning them loose on the front lines of reinvention. It rarely works completely, but it beats the alternatives.

That's why a continuation of reinventing government—in some form, perhaps under a new name—is inevitable no matter who voters elect president in the fall of 2000. Predicting its new form is tougher.

No matter what, government reform efforts won't go away. Scandals have a way of forcing the reform agenda, and the pressures for boosting government's productivity are inexorable. The lessons of the Clinton years show that success requires a careful mix of top-level champions and front-line leaders. But—and this is most reassuring of all—the lessons also show that government's bureaucratic culture can be changed. ■

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## Spring Policy Analysis Workshop Yields New Studies

This spring semester, graduate students conducted policy analyses requested by various state, city, county, and nonprofit agencies. The studies are on the La Follette web site, and paper copies are also available upon request from the Publications Office.

**Mobility in an Aging America.** A study of aging drivers, accident and fatality rates, and suggestions for potential policy changes to address changing demographics.

**Affordable Housing in Madison.** An assessment of

the extent and the location of housing available to the low-income population.

**Alcohol and Drug Abuse Treatment for Jail Inmates.** A consideration of how AODA treatments might reduce jail overcrowding.

**Wisconsin Shares.** A review of the state's child-care subsidy program for low-income families.

**Flex Parking at UW-Madison.** An assessment of the program and suggestions for improvement.

# Globalization and Environmental Protection: Can We Expect More or Less Regulation?

by **Graham Wilson**

*Graham Wilson is associate director of the La Follette School of Public Affairs and professor of political science at the University of Wisconsin–Madison. His article examines the effect of international markets on the regulation of the environment and consumers, and he suggests that the more adaptable and flexible a national government is in partnering with businesses in its own country, the more likely will international regulatory initiatives lead to a raising of standards rather than a lowering.*

A wide range of indicators firmly supports what we sense in our daily lives: The importance of international factors and influences on life in the United States has increased and is increasing. Movement of goods and money across the globe is at a level long thought unimaginable. Even nations such as the United States whose economies were only marginally dependent on world trade in the past have been drawn heavily into it.

Whereas trade as a percentage of the Gross National Product (GNP) of the United States was 6.5 percent in the 13-year period from 1946 to 1959, between 1980 and 1992 it was 15.3 percent. Thereafter U.S. trade dependence continued to increase, growing 44 percent between 1992 and 1996 so that by 1996 trade was equivalent to 25 percent of U.S. GNP. Cross-border investment stock (assets in the United States owned by foreigners plus assets owned by Americans overseas) grew from 15.45 percent of GNP in 1960 to 41 percent in 1992. Growth has continued since then at a faster rate than the growth in GNP overall. Though the United States remains less trade dependent than countries such as the United Kingdom, it is fully engaged in international markets.

We have known for some time now that this growth presents a number of potential problems for national regulatory agencies and their political masters. A full exploration of this topic would cover numerous types of regulation, but this article focuses on one type of social regulation—the protection of the environment and consumers—which has been at the heart of the debate about globalization. This is because it is the type of regulation that appears to set states against markets in pursuit of public policy goals.

## Regulation as a Problem

Several types of problems for regulators that stem from globalization and internationalization may be distinguished. First, regulators may be pushed into a “race to the bottom.” The almost total elimination of capital controls in the developed world and the drastic reduction of tariffs on manufactured goods have created fierce competition for investment between nations for investment, just as there is fierce demand between states within the United States. This competition is likely to be particularly intense within economic zones such as the European Union (EU) or because of NAFTA. Both entities have attempted to eliminate trade barriers.

One means by which nations can compete for investment is by lowering taxes; another is by reducing the impact of regulations on business. Nations may become involved, therefore, in a competition for investment based on reducing the vigor with which they protect consumers, workers, and the environment. We may categorize this competition as a problem stemming from globalization in that the consequences result from the workings of global economic forces, not current political decisions. While globalization itself results in part from the past decisions of governments, such as lifting capital controls and reducing tariffs, once those decisions are made, economic forces are unleashed that allegedly produce strong downward pressure of regulations.

Second, regulators increasingly encounter international organizations that impede their freedom to regulate. Some of these international organizations may themselves be regulatory bodies that preempt national regulatory authority, the regulatory agencies of the EU being perhaps the best example. A more difficult situation arises, however, when regulators find that their freedom to regulate is limited by the actions and policies of an international organization that has an entirely different policy focus.

The best known examples are of collisions between trade and environmental policy. In the final days of the General Agreement on Tariffs and Trade (GATT) before it was reorganized into the World Trade Organization (WTO), GATT panels ruled that the U.S. Marine Mammal Protection Act, which led to banning the import of tuna caught in ways that endangered dolphins, conflicted with GATT obligations. The United States, an eager campaigner for freer trade, was in an embarrassing situation, and it ultimately revised the law.

In a more recent case brought against the United States within the framework of the WTO, the United States was found to be in breach of international trade law by banning the import of shrimp caught by poor fishermen in less developed countries such as India, Bangladesh, and Malaysia in a manner that harmed sea turtles, an endangered species. The U.S. Congress and executive agencies have attempted to revise their laws and regulations to comply with WTO rulings, but have been blocked by domestic legal challenges from environmental groups.

A third problem for federal regulators is that they face considerable pressure from multinational corporations to harmonize regulations. Corporations

understandably wish to avoid the problems with being in compliance with a rule or procedure in one country only to be out of compliance in another. This is a familiar problem domestically for American corporations that wish to avoid situations in which regulations differ from one state to another, and for this reason American business leaders have generally opposed efforts to devolve more regulatory power from the federal to the state level. Such complications arise more frequently internationally as trade with other countries increases. European bans on genetically altered food, for example, are creating massive problems for U.S. shippers of grain who often mix grain from different farmers. As a result of this mixing, both conventional and genetically altered grain from the United States pours into European silos.

Differences in regulations from one nation to another have even greater potential to disrupt trade in services, such as insurance, where the very nature of the product being sold is defined by laws and regulations. Corporations, generally inclined in the modern era to favor freer trade, are also well aware of the potential for environmental or consumer regulations to be used as shields against foreign competition by domestic industries. Corporations favoring trade liberalization, therefore, have an interest in making sure that domestic regulators achieve harmony with their foreign counterparts.

## Regulation (or Self-regulation) as a Solution

In general, internationalization—the transfer of authority to an international organization—and globalization—the broader impact of economic and cultural forces from a globalized economy—have been seen as reducing the likelihood of effective regulation. There are, however, a number of ways in which internationalization may enhance the prospects for effective regulation. First, as David Vogel has argued in his book, *Trading Up: Consumer and Environmental Regulation in a Global Economy*, countries with stringent regulations that have a significant impact on their production costs have a major interest in using international organizations to raise costs in other countries, too. The United States and Germany, Vogel argued, forced by strong environmental movements in their own country to adopt stringent (and costly) environmental regulations, will push their competitors to adopt similarly costly measures.

The more integrated markets are and the stronger the related international organizations, the more likely it is that a leveling up rather than a leveling down of regulatory standards will occur. Vogel's argument is clearly dependent, however, on the strength of environmental groups, particularly in the United States. If these groups were weaker, the globalization of trade could be followed by measures to weaken high regulatory standards rather than to export them to competitor countries.

Here the dominance of the United States as a world hegemonic power comes into play. While the power of its leaders is indeed great internationally, so also is its vulnerability to domestic pressure. Environmental groups

may feel weak and underfinanced in comparison to business, but they clearly have the ability to exert leverage. If Clinton, or more probably his successor, is to regain “fast track” authority for negotiating further trade liberalization, the environmental groups will have to be won over. Currently, the environmental groups are a crucial component of a protectionist coalition of interest groups based on labor, a component that brings not only added lobbying power but intellectual and moral respectability. In this context, the name of the game in Washington is to emphasize the compatibility of environmentalism with trade, not the possibility of weakening environmental commitments to promote competitiveness.

On at least two of the occasions when the United States was required by international bodies to revise its environmental laws to comply with its trade policy commitments (tuna/dolphin under GATT and shrimp/turtle under WTO), a very substantial resistance developed by environmentalists. Indeed, the United States came into compliance with the GATT ruling on tuna only after the complaining countries had settled for a compromise which they negotiated with five U.S. domestic environmental groups.

The United States has yet to come into compliance with the WTO ruling on shrimp/turtle, but once again we can be confident that the outcome will not be significant defeat for environmental groups. As Vogel's argument requires, the environmental groups have sufficient power in the United States to make it more rational for U.S. policymakers to try to raise standards in other countries than to weaken their own.

American leaders, including President Clinton himself, have pressed for “greater transparency” in WTO decision making, meaning, among other things, greater openness to lobbying by groups such as environmentalists. In the period following the initial ruling against the United States on shrimp/turtle, U.S. agencies such as the Departments of Commerce, State, and the U.S. Trade Representative engaged in vigorous lobbying of the WTO that contributed to a final ruling by the appeals panel which contained significant procedural gains for environmentalists. Their right to submit briefs to WTO hearings on trade laws was accepted (previously many members of WTO had argued that only countries had this right), and the WTO leadership attempted to open a dialogue with the groups. According to a news article entitled “Embracing Greenery” in the *Economist*, the current head of the WTO, Mike Moore, “is reaching out to the most vocal of all the WTO's critics: environmentalists.”

A second aspect of internationalization that has enhanced the prospects for effective regulation has been the unexpected gains from globalization that public interest groups such as environmentalists have enjoyed. Environmentalists have been adept at using globalizing forces (cheap air travel, cheaper phone calls, and the Internet) to build international movements and coalitions.

One consequence of this internationalization of public interest groups has been that they have been able to

mount campaigns at the point of greatest corporate weakness. British political scientist Grant Jordan provides a telling example. Shell wished to dispose of a North Sea oil storage facility, the Brent Spar, by sinking it in deep waters in the Atlantic. Shell persuaded most scientists and the British government that this was the most environmentally friendly way to dispose of the storage facility. The plan was condemned by environmentalists in Britain and in other European countries, but the British government had been so convinced by Shell that it not only approved its plan but defended it vigorously within the EU against criticism from foreign leaders such as German Chancellor Kohl. John Major, the British prime minister, left his meeting with Kohl only to be informed that Shell itself had retreated and now intended to follow the more expensive option of dismantling, not sinking, the Brent Spar.

Why had Shell retreated? In brief, the explanation was that a campaign including boycotts of its gas stations in Germany and the Netherlands was hurting Shell too badly. Shell's character as a transnational corporation allowed environmentalists to pressure Shell wherever the environmentalists were strongest and Shell was weakest. Thus internationalization can undermine the capacity of corporations to resist environmentalist pressures.

Business generally remains eager, for understandable reasons, to avoid further extensions of traditional regulations. In order to fend off further "command and control" regulation or restrictions on trade adopted in the name of environmental protection, corporations have themselves become agents for spreading a certain type of regulation. This type of regulation, of course not legally binding and therefore not formally regulation, focuses on managerial procedures. Businesses are encouraged, or in a sense required, to adopt specified forms of self-regulation if they wish to remain contractors or suppliers of major corporations. Some of these requirements are issued in forms that seem more mandatory than voluntary, except in the sense that suppliers can choose to lose important business for not complying. Thus on September 15, 1999, the Ford Motor Company issued a notice to all suppliers to register a minimum of one facility to international standards by December 31, 2001, and all manufacturing sites by July 1, 2003. Ford offered its suppliers training in order to meet these requirements.

The two most important forms of corporate self-regulation in this area are ISO (International Standards Organization) 14000 (a series of standards beginning with numbers at 14000) and EMAS (Environmental Management and Auditing System). The two forms differ significantly in character. ISO 14000 is a voluntary system of

self-management whose main tenets are that companies adopt procedures for evaluating their current environmental record and adopt plans and procedures for improving, evaluating progress, and setting new goals. Firms that adopt such procedures receive a certificate. ISO 14000 does not mandate specific targets or levels of performance. Indeed, one U.S. firm holding an ISO 14000 certificate was judged by regulators to be in breach of existing environmental laws.

EMAS, in contrast, derives from an EU directive issued in 1996, and whereas ISO 14000 covers all types of organization, EMAS is focused on producing industries as opposed to industries such as banking or insurance. EMAS requires firms to comply with all existing laws but then to adopt plans for additional improvements. Firms are audited at least once within each three-year period by auditors from a panel approved by national governments. A list of firms in compliance is maintained by an industry organization such as a chamber of commerce.

EMAS is a more stringent procedure involving not just process but external evaluation of performance. Although government is more directly involved with EMAS in establishing the scheme and by approving and monitoring auditors, it is similar to ISO 14000 in resting on the idea of improving environmental performance

through non-governmental means: private sector auditors—not civil servants—carry out inspections and identify underperformance. It is perhaps predictable, therefore, that ISO 14000 has had more appeal than EMAS, even in Europe where EMAS is heavily concentrated in Germany (see table 1).

So far ISO 14000 has made only very limited progress in the United States, in spite of its voluntary nature. American business leaders have often claimed that they are willing to accept environmental goals, but they oppose inflexible government regulations.

Yet the take-up rate of ISO 14000 has been slow. In Europe, 5,800 ISO certificates have been issued, in Japan around 2,500, and in the whole of North America, around 500. But while there is no indigenous enthusiasm for ISO 14000 in the United States, it is now being spread by American transnational corporations such as Ford that are afraid, as one executive put it, that if they do nothing one day "the Europeans will slam the door" on them through environmental regulations that have trade consequences.

### Playing Several Games at Once

It is clearly inadequate to characterize the interaction of international forces and regulation in terms of a simple race to the bottom. How, though, might we summarize the interaction of international factors and regulation?

**TABLE 1**  
**EMAS Versus ISO 14000 in Europe:**  
**Number of Permits in 1999**

|                | EMAS  | ISO  |
|----------------|-------|------|
| Germany        | 2,238 | 1450 |
| Sweden         | 165   | 645  |
| United Kingdom | 71    | 1009 |
| France         | 34    | 365  |
| Netherlands    | 23    | 210  |
| Italy          | 13    | 166  |
| TOTAL          | 2544  | 3845 |

The most powerful analogy put forward to capture the interaction of international and domestic policy goals of opening foreign markets to U.S. industry is from Harvard University's Robert Putnam, who proposes a "two-level game" analogy. National leaders in the United States increasingly interact with leaders of other nations; they also think about how to deal with powerful domestic actors (interest groups, legislators, other politicians) on the same issues at home. Their skill lies in playing the game at both levels. The struggles between environmentalists seeking to protect dolphins and turtles on the one hand and the agency pushing an international policy of trade liberalization on the other (the U.S. Trade Representative) is a case in point. U.S. presidents and policy-makers have had to struggle to reconcile powerful domestic forces pushing for environmental goals around the world with attempts to open foreign markets for U.S. firms through liberalizing trade regulation.

Putnam's analogy does not fully capture the interaction of domestic and international factors in regulation, however. The two-level game analogy misses at least two important aspects of the relationship between international factors and regulation.

First, international and domestic levels are not nearly as separated as the two-level game analogy suggests. Domestic interests are active at the international level seeking to influence policymakers not only in bodies such as the EU (which daily takes on more of the character of a state than of an international organization) but in truly international organizations such as the WTO. Domestic interests have won the right to submit their arguments directly to WTO hearings without relying on national governments as intermediaries.

Social movements have also been adept at acting internationally. German Greens, for example, are currently pressuring a paper manufacturer in their country, Handel, to force its pulp suppliers in British Columbia to adopt sustainable forestry practices. Indigenous peoples from British Columbia have been flown to Germany to take part in protests aimed at Handel. Using e-mail, the Internet, air travel, and cheap international phone calls, domestic social movements have gone global with their concerns. The boundary between the domestic and the international has eroded.

The second reason that the two-level game analogy falls short is that it provides inadequately for the independent impact of international organizations. International organizations, like domestic institutions, not only have their own power structures but they also generally have a particularly strong sense of their primary mission. The commitments and values of those who work in the organization, even the language and concepts used in analyzing problems and situations, make some policy outcomes more likely, others less so.

The EU is not a neutral setting in choices between more and less integrative policy options, the WTO is not neutral vis à vis more or less trade liberalization, and international bodies charged with environmental protec-

tion are not neutral regarding proposals to protect the environment. International organizations are also surrounded by a penumbra—a policy network of generally sympathetic journalists, commentators, interest groups, and agencies of national and subnational governments with whom they have contacts, all of whom can generate domestic support for international regulations. In certain areas of environmental policy, these international networks may be united by common beliefs, assumptions, and concepts. They may have formed what Peter Haas of Amherst College has called "epistemic communities." Even while Margaret Thatcher inveighed against the growing power of Brussels, some EU directives (for example, on the cleanliness of bathing beaches) attracted great support in Britain.

The point is that the independent influence of international organizations and the policy networks of which they are part result in something that is not purely international. Policy advocates who have succeeded at the international level can—and do—reach into the politics and society of individual nations to build support. There is no simple separation of the international and domestic games. Rather, policy coalitions and networks increasingly cross borders and the domestic-international divide.

## Combining National and International Regulation

Nations differ in the degree to which they favor investing resources in policies such as environmental or consumer protection. The causes for this variation are hard to determine and are no doubt deeply rooted in history and political culture. We might assume that the nations most keen on environmental protection in general will be the keenest on international regulation; as Vogel argued, nations with high standards, and therefore high costs, have important economic incentives in persuading other countries to adopt similarly costly measures. There is also an interaction, however, between nations' preferences on environmental policy and their policy capacities. Countries with a tradition of lax enforcement of regulations, such as the Mediterranean members of the European Union, are often willing to vote for stringent regulations that they have no intention (or capability) of enforcing.

The standard assumption to date has been that the more liberal economies gain from globalization. As their own economies are less encumbered by restrictive regulations, they have the flexibility to attract capital and compete in export markets. It is less clear, however, that more liberal economies will benefit from the internationalization of regulation. Calls for stricter standards at the international level will generally be experienced by liberal states such as the United States as a call for more regulation in the command and control format. This is the only policy capacity that they have. Such liberal states are therefore particularly likely to be placed in the dilemma of choosing between the international opprobrium resulting

from blocking what are seen as essential measures and the costs of additional command and control regulation. This was, of course, an important factor in Thatcher's deepening antipathy to the EU. In her declaration of principle at Brugges, Thatcher pronounced that she had not rolled back the frontiers of the state domestically only to see them advance in Europe.

States that are more practitioners of "organized capitalism" than of more liberal markets have other policy options, however, because of the institutional capacity that they possess. Internationally agreed-upon goals can be pursued through flexible agreements with industries rather than through "command and control" regulations. The Netherlands, for example, has promised to attain Kyoto levels of reduction in greenhouse gases. It will do so not through inflexible regulations, however, but through agreements—or as they are known, "compacts"—with major industries. Industry promises to attain the best environmental standards in the world; government promises to leave them free to do so (except for providing tax allowances).

The growth of EMAS in Germany draws on that country's long tradition of industrial self-governance intended in part to avoid action by the state. Again, this provides a more flexible means for pursuing internationally agreed-upon goals than "command and control" regulation. A more organized political economy provides greater flexibility.

The danger for the United States, in contrast, is that our regulatory traditions are based on legalism, which usually creates inflexibility. Pietro Nivola of the Brookings Institution has pointed to the American style of regulation as an important source, therefore, of competitive disadvantage.

## Conclusion

It is almost a truism in the study of the impact of international forces on domestic political systems that not all countries react in the same way or are similarly influenced by a common international force. Perhaps the time has come to start to assess the different ways in which regulators in advanced democracies will be affected by the common international environment of globalization and internationalization.

Most discussion of internationalization and regulation has focused on the danger of a "race to the bottom" in standards. Though this is one possible scenario, the interaction between regulation and international factors is in reality much more complicated and unpredictable. Indeed, international influences can as readily raise as they can lower the prospects for regulation. The ability of the international environment to promote regulation will be welcome news to countries where environmental protection is a priority. However, attitudes toward the capacity of the international environment to promote increased regulation will depend also on the domestic capacity of countries to achieve policy goals. The Netherlands, for ex-

ample, with flexible and adaptable partnerships between business and government, may feel better able to embrace international initiatives than countries such as the United States, for whom accepting higher levels of protection may also mean accepting a new wave of costly and inflexible "command and control" regulation. ■

## DIRECTOR'S PERSPECTIVE

*continued from page 1*

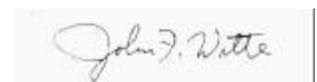
The La Follette School's new donors see great value in the programs that we are engaged in, and they all recognize the tripartite mission of our school—education, research, and outreach. Together, these funds, as well as those provided by earlier donors, support all of these goals. We are extremely grateful for the influx of these new funds and hope that they will attract yet others. Please see the brief article describing the funds and their donors on page 7.

Three faculty members are joining the La Follette team in the upcoming fall semester as our international program begins. David Weimer is a political scientist who writes, among other things, on property rights in the emerging post-Soviet and Central European states. Melanie Manion, also a political scientist, is an expert on China and is currently studying corruption in Hong Kong and China. Charles Engel is an economist who studies a range of trade and investment-related issues focusing primarily on Western Europe. Our next round of faculty hiring will target experts in international public management and administration.

A new program that is beginning with the MIPA degree is that of an accelerated master's degree for UW-Madison students who commit to the program while still an undergraduate. Taking a prescribed set of courses in public affairs as a senior in a B.A. or B.S. program, students will add two semesters of graduate work and receive a master of public affairs or international public affairs, thus completing their combined bachelor's and master's degrees in only five years.

The class of 2000, a group of fine students, is graduating from the Master of Public Affairs degree program as this issue of the Policy Report goes to press. In the past few years students have organized their own graduation ceremonies and held them in the state capitol to signify their commitment to public service. This year's ceremonies are to be held in the recently refurbished Senate chambers.

The list of programs and activities that the students, staff, and faculty at La Follette are engaged in goes on, but space permits the discussion of just these few. Please visit us and see the reason for my enthusiasm. Or visit us on the web at <http://www.lafollette.wisc.edu>.



# Education in the Twenty-first Century: Will It Look Like Education in the Twentieth?

by John F. Witte

John Witte is the director of the La Follette School of Public Affairs and professor of political science at the University of Wisconsin–Madison. This article reflects on the history of public education in the United States and the possible forms public education might take in the coming years. It is a shortened version of an article forthcoming from the *Stanford Law and Policy Review*. © 2000 by the Board of Trustees of the Leland Stanford Junior University.

Although the millennium provides us with an arbitrary but useful point for reflecting on the future, there is a temptation in “millennial thinking” to propose abrupt changes in institutions and social systems. Such is the case with the public education institution in the United States, which seems to be high on the agenda at all levels of government. In a rapidly changing environment predictions are difficult, and changes do not often occur predictably. My speculations, therefore, are based on past and recent trends, which by the beginning of the next century may be viewed as shortsighted.

## Past and Present

A great deal was accomplished in education in the nineteenth century. By 1900, our system of education had been transformed from an essentially private, almost completely elite system, into a system based on what had become known as the “common school.” That movement, which began in the mid-nineteenth century, emphasized professionalism, school organization (by age and grade), and a common curriculum built around national reading series and a Protestant Bible. As it rapidly expanded, a mostly Roman Catholic, private school system also emerged in response to the Protestant dominance of the public schools.

The system of common schools, however, was quite diverse in both size and structure. Systems ranged from large, urban ones to an enormous number of one-room schools in the predominantly rural areas. Waves of northern and southern European immigrants were filling the urban systems, while also having an impact on rural schools in states like Wisconsin.

Several trends dramatically transformed those systems in the twentieth century. Organizationally, although local control at the city or community level still persists to a much greater degree than in almost any other developed nation, consolidation of school districts reduced the number of districts from 127,531 in 1931 to 15,713 in 1987 (see table 1). Much of this reduction involved the

elimination of single-room schools that also comprised whole districts. The growth of cities, combined with a reluctance to break cities up into multiple districts, resulted in enormous school districts in New York, Chicago, Los Angeles, Miami, Detroit, and many other cities (see table 2). These school districts currently have budgets larger than many nations.

Due to northern migration of blacks, and the immigration of Hispanics and Asians, court-ordered integration, and the development and persistent growth of suburbs, those large districts and many smaller ones have become disproportionately non-white and poor. In contrast, the suburban districts, created by post-war migration from the cities, have become ever more affluent and remain predominantly white.

In the post-World War II period, education policy was dominated first by the effort to integrate schools following *Brown v. Topeka School Board*, then by efforts to cope with poor educational outcomes in inner cities. In the last two decades, debates about education shifted from racial diversity concerns to concerns about the general decline in educational outcomes and about various schemes to increase educational choices for families, including those desiring to attend private schools. The first of these trends was set off by the publication of *A Nation at Risk* in 1983. That study highlighted two concerns: a long-term decline in knowledge and skills, primarily evidenced by a drop in SAT scores; and

the belief that American students were going to be less able to meet future demands and less able to compete with better educated workers in other nations.

One reaction to these fears was a movement toward more state-centered and bureaucratic controls: more rigorous high school graduation requirements; state testing; increased requirements for teacher graduation and licensing; and more recently, moves toward state curriculum standards and testing for graduation and promotion.

Another reaction, which had other origins as well, was the movement advocating increased school choices for families. The movement actually began with magnet

TABLE 1

School District Consolidations

| Year | Number  |
|------|---------|
| 1931 | 127,531 |
| 1957 | 47,594  |
| 1967 | 22,010  |
| 1987 | 15,713  |

Source: U.S. Department of Education, *1998 Digest of Education Statistics*

TABLE 2  
SCHOOL DISTRICT SIZES AND BUDGETS

| District    | Student Population | Budget (\$ billions) |
|-------------|--------------------|----------------------|
| New York    | 943,969            | 5.45                 |
| Los Angeles | 625,086            | 3.13                 |
| Chicago     | 408,830            | 1.75                 |
| Miami       | 292,000            | 1.32                 |
| Detroit     | 168,956            | 0.79                 |

Source: U.S. Department of Education, 1998 *Digest of Education Statistics*

schools, which were created in the 1970s in response to the white flight that followed racial integration of schools. These specialty schools, which broke with the geographic assignment system (that with few exceptions had been rigidly enforced throughout the twentieth century) were created to achieve racial balance by drawing students of the appropriate race from throughout a district. The number of magnet schools increased dramatically in large-city districts in the 1980s and 1990s.

Subsequently, more extensive intra-district choice programs, such as controlled choice plans in Boston, extended assignment to large areas. At the same time, special programs to promote inter-district transfers (to enhance integration efforts) were established in many cities, including Milwaukee, St. Louis, and Kansas City. Finally, beginning with Minnesota in 1986, states began enacting open enrollment legislation, ostensibly allowing students to attend any district in the state. The most recent innovation is charter schools, usually chartered by school districts, but often having a great deal of independence from district controls.

Public subsidies of private schools were the final aspect of choice. As the century ended, these programs accounted for considerably less actual change, but much more political and legal controversy than public school choice. Unlike in other nations, where private schools receive direct state support, subsidies in the United States take the form of parental tuition support programs—either tax credits or vouchers. For the first time since before 1900, subsidies are also going to religious private schools in Milwaukee and Cleveland.

## Preservation and Continuity in the Current System

What are the foundations of the current education system? What should remain and be protected in the American education system?

### *Community-Based, Free, and Universal Education*

Free public education developed in the mid-nineteenth century has provided U.S. citizens opportunities to grow, develop, and prosper. That system of education

first contributed to rapid industrialization, loudly applauded at the turn of the twentieth century; and second, to the explosion in technological developments in many fields that is proving to be the hallmark of the turn of the twenty-first century.

The system was, and continues to be, based on a financing approach that amortizes the current costs of education over generations and across communities. Families without children contribute to the education of families with children, and those who no longer have children in the schools continue to pay for those who do. Without that system, families would likely invest less in their children's education. Also, the extent of one's education would become less dependent on talent, and more on economic resources. Thus the current system endorses two propositions: (1) an "over-investment" in education; and (2) equity of educational opportunity that expands the merit pool.

### *Over-investing in Education*

Why preserve a system that provides excess over what market efficiency might dictate? In practical terms, over-investment can push students to higher levels of education and re-education, whether or not there is an immediate payoff or use for the level of education obtained. Why should that be promoted?

The short-term answer depends on the assumption that as technology increases and becomes more complex, it is the long-term investment in human capital that will yield economic and political success, and further equality. For example, few would dispute that higher education in the United States, in almost any field, is at or near the top in the world. Although the payoff of that education may not be obvious in the short term, it remains the envy of most nations, nations that continue to try to enroll their students in our programs. At the other extreme, countries that restrict higher education to those with means, or deny it to certain subgroups of the population (such as women or certain social castes), will ultimately pay the price in a less effective workforce and a less capable citizenry.

### *The Continuing Push for Equity*

As we enter a new millennium, several issues of the last two decades remain hotly contested. These include a perceived general decline in American education, our status relative to other nations, and the comparative effectiveness of private and public schools. However, the inequities in educational outcomes from student to student, school to school, and district to district are not disputed. Additionally, we know where most poorly performing students are. They are increasingly concentrated in the same schools and districts, and those schools and districts are located in our large cities and poor rural communities.

Equal educational opportunity may be defined as the prospect of all children having the opportunity to receive an adequate and appropriate degree of education

commensurate with their ability, regardless of other social or economic conditions. This definition waffles on the notion of a minimal or “adequate” level of education, which is the implied normative assumption behind compulsory education laws and is the key issue in recent debates surrounding adequacy in funding. But it clearly specifies that extraneous factors such as class, race, gender, or luck should not bar students from having access to education commensurate with their abilities.

Why equal opportunity? Some arguments often reduce to ancient and fuzzy ideas about innate equality, or arguments that a democratic society, based on equality of citizenship, requires individuals to be treated equally in the public sphere. The former—that everyone is innately equal—by observation and every test we know, is patently false. People have differing abilities, intellectual and otherwise. The second is also hard to sustain unless one argues that our country is a failed democracy. Our inequalities are clear in terms of both opportunities and results, yet the demos seems to survive and persist.

A more compelling argument for equal opportunity may be based on economic efficiency. That argument rests on simple assumptions about innate abilities in a complex society. If we assume that abilities for learning and job requirements vary considerably, but the matches between those characteristics are not systematically related to external factors such as race, class, or gender, then arbitrarily excluding groups from equal job competition is very inefficient. If we then make the further assumption that preparation for the job market requires an often-unknown level and form of education, arbitrary exclusion from education effectively restricts the future job pool.

For example, when my mother graduated from the University of Wisconsin in 1940, 36 percent of the students were women. In the sixty intervening years, males dominated many jobs at which women could have been as or more effective—medicine, law, college teaching, and corporate management, to name a few. By effectively restricting women to certain roles, our society and/or economy lost considerable efficiency as less able men took jobs by virtue of their privileged place in the pool. And this inefficiency occurred whether the restrictions were based on true choices of women within families or on a male-dominated sexist conspiracy. Equality of opportunity need not depend on warm and fuzzy feelings about equality or dubious links to democracy, but rather on straightforward competitiveness in a global economy that will reward nations that maximize their pool of competence.

The access of women to education in America has become, or will very soon become, equal to that of men. The de facto prohibitions were lifted as a result of changes in belief, control of reproductive rights, and

family economic necessities. But the inequities based on class and race are much deeper and more intractable.

What then is to be done concerning race and class inequities in educational success and opportunity? First, we must resist ignoring the problem. The increasing distance between the haves and have-nots in American society makes it easier to overlook the problem. As many Americans live and work farther from the inner cities, the problems of these cities become less visible to them. In addition, increasing income disparities and movements to privatize services, including education, threaten the

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As globalization increases, the amount of relevant subject matter will skyrocket.

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education finance systems that remain considerably dependent on local financial support. And as political power at the state level follows suburban affluence, state aid to poor districts

is also threatened. Poor cities, if left on their own to educate those remaining in the public system, will obviously produce fewer resources for education—a fact already inherent in funding disparities within states. Thus it will take considerable political will to remain focused on the problem of equal educational opportunity.

But merely arguing that the issue of equity for poorly performing schools must remain high on the national agenda evades the question of what should be done. In the latter half of the twentieth century, dozens, if not hundreds, of proposals have been made addressing the problems of inner-city and, to a much lesser degree, poor rural schools. Many of these programs worked in parallel even though they may have been inconsistent in theory and practice. Indeed, reform proposals often occur so fast, tumbling out of schools of education and policy networks and directly into schools, that we end up with little if any systematic knowledge of their effects. This result may be inevitable given the depth of the problems and the intense political pressure on poorly performing school districts.

As incongruent as it may sound, the massive experimental approach recommended by John Dewey almost eighty-five years ago may be an appropriate strategy. The scattering of unconnected, uncoordinated trials may produce incremental improvements for some poor students in cases where the right mix of innovation and implementation takes root. The most effective of those reforms may then be replicated. And simply making the effort may motivate families to do their part in supporting their children’s education.

A simple conclusion may be that without attacking the underlying problems of poverty and racial differences, educational solutions may make very little headway. As education fails in poverty zones, those with means will move further away both physically and psychologically—and they will take their wealth and social attitudes with them.

## Alternatives for the Future

In relative terms, both over time and across nations, we are a privileged nation. Life expectancy is now 73.5 years for men and 80.4 for women, and even the poorest of our population live much better than the average of many nations. But our task is to improve existing conditions and respond to rapidly changing environments. And that requires new thinking and approaches to education.

### *The Uncommon School*

The argument that we must remain committed to a free and universal, community-based education explicitly avoided the additional term “common education.” The common school movement of the nineteenth century was linked to public support for education and compulsory education laws. It also proposed a common form of education, organization of schools, and credentials for teachers and administrators.

I propose retaining the universal, free, and community support of education, but jettisoning the rest. If we assume that societies will become more complex, that desirable skills will become more diverse, and that specialization will yield greater rewards, specification of any common form or content to curriculum seems ill-advised. Ten years ago, “web masters” would have conjured up confused and perhaps lurid images in almost all our minds. Recently I have posted advertisements for three such positions at my university, and it was tough to specify requisite academic credentials.

The movement toward the uncommon school is not futuristic. The magnet and charter school movements of the last twenty years provide the institutional vehicle for introducing the changes that will be important in the twenty-first century.

Those movements will take on new and varied forms as districts become ever less rigid in terms of the types of education they provide, where they provide it, and when. There is, for example, little reason to believe that most education in America will occur in common buildings occupied by groups of students and teachers at regular times. I am composing this essay, for example, at an airport in Montreal after having communicated electronically with my students, staff, and colleagues in Wisconsin. This is just the beginning.

### *Specialized Education*

Specialized forms and approaches to education were not uncommon in the twentieth century. Educators developed the idea of individually guided education that still prevails in some schools. Well prior to that, simple correspondence courses were available to students

wanting unique courses or courses not offered in their schools. The military perfected individually guided and paced instruction, first in paper form and then via computers. And special forms of education, such as intensive language training, Sylvan learning centers, and many others have become commonplace in our educational service systems.

What I am suggesting is that these forms of specialized education may become the standard, with graded movement of students working through a common curriculum at more or less the same pace as the exception. Learning from grade seven to twelve has been based on what college specialists would call a liberal arts model, but as the demands of—and for—technology increase,

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Although formal education has for the last 150 years been relegated primarily to teacher-led education, there is no reason to believe that will remain the primary mode of learning.

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specialization that now occurs in college will be pushed down to the secondary-school level or below.

Or an even more radical transformation might take place. Following a self-paced, technology-intensive, basic education in reading, science, and computational and mathematical techniques (largely carried out by computers or their successors), students might pursue literally hundreds of specialized paths. As globalization increases, the amount of relevant subject matter will skyrocket—and students will have increased access to information. As much as we may debate the reduced emphasis on American history, literature, or political science, we may be powerless to do anything about it. Perhaps we will be comforted by the knowledge that an aspiring student in Ghana is working on a paper on American educational reforms, accessing electronic journals as articles are posted.

### *Schools Without Walls, Without Teachers*

While part of me fears schools without teachers and students without peers, we cannot avoid the prospect of schools without walls. These schools could take many forms: distance learning; Internet education; and classrooms composed of interactive, two-way connections that form a “virtual classroom.” More education may occur in one’s home and/or one’s office.

With the trend toward distance learning comes numerous problems. As learning becomes more individualized and potentially isolated, however, questions of socialization will undoubtedly emerge. For example, early private prep schools in America and Europe were designed to create, socialize, and train future leaders of society. The fashioning of “gentlemen” was as important as, or more important than, education per se. Although current schools and colleges are hardly as extreme in their socialization regimes, they all serve to bring students together and into contact with adults outside their families. And that function may be lost as we access electronic classrooms continents away.

Early in our history advanced learning occurred essentially without teachers. Lincoln “read law”; and scholars during the colonial period read and worked on their own. Today, people do the same, learning from manuals, books, clubs, chat rooms, and the Internet. Although formal education has for the last 150 years been relegated primarily to teacher-led education, there is no reason to believe that will remain the primary mode of learning. Why should it? If the sources of knowledge become decentralized, and access is more or less universal, we may well revert to the earlier form of education. This time, however, it might be mass education conducted in specialized formats using modern technology and vast data and knowledge banks. Plato may still be there for Socrates, and Socrates for Aristotle, but they will be teaching millions and be connected directly to none.

### *Global Education*

American education is becoming increasingly international in perspective—from kindergarten on. Given the technological advances, one must begin to think about classrooms that may cross continents. This interaction already occurs in higher education in specialty fields. But it may also dramatically affect K-12 education as partner cities and schools merge classrooms and span political borders—facilitated by computer-generated instantaneous translation. Already the French distance learning network, Centre National d’Enseignement par Correspondance, has students enrolled from 170 countries. As Internet technologies spread and are integrated with television or its successor, classes of thousands or millions will be simultaneously translated electronically into hundreds of languages and dialects.

Thus, the challenges of isolation and individualism may be offset by participation in a true global community. Such participation may still lack the personal contact that is so much a part of our education systems today. But it may also allow learners to function in a new world that is unbounded by geography, politics, nationality, and language. One hopes that the world will also be less bound by class, color, or new status advantages that may emerge, possibly created by increasing educational access. Such conditions and boundaries are much harder to predict than the shrinking of the bounds of space, time, and language.

### **Reconciling the Future with the Past**

In one scenario, this new system will pose a significant challenge to aspects of the traditional learning system that I have argued need to be preserved. Universal, free education and, within bounds, equity of access and

results may in fact be best maintained through a centralized, hierarchical system run by states and local authorities in a largely monopolistic fashion. A traditional system could ensure sufficient and equitable funding across districts and schools. Common curricula, teacher training, and the organizational form of education would provide a degree of uniformity. Although inequality might continue because of differences in teacher quality or the

effects of widely varying family circumstances—primarily poverty—centralized state control would at least allow these issues to be addressed.

On the other hand, the new world of edu-

cation will be ripe with opportunities and alternatives. It is difficult to support continuation of current practices when one evaluates the differences in achievement and attainment by social class and race. It seems doubtful that the more diverse, decentralized, and specialized system I envision could make matters worse for those now failing. Those students who are failing using current, conventional approaches to education may fit considerably better into the array of learning modes that I foresee.

To reconcile the past with the future, several things are needed:

- Truly universal access to increasing choices and technologies;
- A more uniform funding system that facilitates not only the traditional school but also a diversity of approaches to education;
- A changed regulatory regime so that private schools are monitored more closely and public schools less;
- Attention to the need for socialization in an era of electronic instruction.

### *Learning for Its Own Sake*

Perhaps allaying fears about a future that may be increasingly isolated, individual, and technologically sterile, learning for its own sake may blossom as our society becomes universally better off—by requiring shorter working lives. Much of what has been described above has been learning that follows function, or the necessity of learning to conform to the needs of a working society. But we hope for more, for a broader vision of learning and education and their role in society.

As access to learning increases, however, to a degree we cannot now foresee, leisure time will grow as productivity reduces the time needed to procure adequate means of living comfortably. Those who aspire to become artists, philosophers, poets, webmasters, electronic cartoonists, or home designers of shuttle crafts will emerge. A further payoff for overinvestment in education may occur: utility may be gained from the pure pleasure of learning and acting on new and more accessible information.■

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There is little reason to believe that most education in America will occur in common buildings occupied by groups of students and teachers at regular times.

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# Late 2000 Economic Outlook: Watching Out for Inflation

by Donald A. Nichols

In this economic forecast for late 2000, economist Donald Nichols cautions that inflation should be the object of greatest scrutiny for the United States economy during the remainder of 2000. Professor Nichols is director of the La Follette School's Center on the Wisconsin Economy and professor of economics at UW-Madison. Previous outlooks are available on the La Follette School's web site at <http://www.lafollette.wisc.edu/out-reach/pubs>.

The economy entered 2000 with powerful forces propelling it. Household spending, particularly on housing and durables, remained strong, while business spending on equipment continued to grow rapidly. These forces are likely to continue to drive the economy throughout 2000 barring some large shock to the economic environment.

The big story in 2000 will be the battle between the economy's strong willingness to buy and its limited ability to produce. If spending outpaces production, we are likely to see inflation ticking upward. Or if the Federal Reserve just fears that inflation is about to start up, we will see higher interest rates. Figure 1 shows the past relationship between interest rates and inflation.

Higher interest rates would certainly change the environment for spending decisions. Higher oil prices or a decline in stock prices would also change that environment. Of these I view a continued increase in interest rates as the most likely barrier to unrestrained growth. Indeed, the big story over the next few months is likely to be a series of interest rate increases on the part of the Fed. Increases of three-fourths to a full percentage point are likely.

The Federal Reserve will try to slow the economy's growth without stopping it, which means they will try to bring about a "soft landing." It may be difficult to accomplish, but a soft landing is probably how the economy's performance will be characterized at the beginning of 2001.

For the year 2000, I expect growth at a rate of 3½ percent to 4 percent to continue. I expect growth to slow, somewhat to a rate closer to 3 percent or so in 2001. Even though we may see another year of growth well above 3 percent, the growth at recent levels cannot be sustained indefinitely. The question is when the economy will encounter the barriers to growth that will finally slow it down, and whether the slowdown can take place without troublesome side effects, such as a spurt of unacceptable inflation or a stock market crash, which could hinder the return to growth.

## The Trends of the Old Millennium Will Continue in 2000

Among the trends that were well established in 1999 and that will continue in the year 2000 are the following:

- Barring a collapse in the stock market, consumer spending is likely to remain robust.
- The growing demand for U.S. workers will continue in the year 2000. The question is whether enough new workers will appear to meet that demand or whether the demand will be dissipated in the form of higher wages or seep away into increased imports.
- Foreign economies turned around in 1999 and will grow strongly in 2000. The question is whether growth abroad will help the United States through its effect on our exports more than it will hurt us through its effect on raw materials prices.

■ The strength of consumer spending will continue to depend on the strength of the stock market in 2000, as it did in 1999. The question is

whether high stock prices can remain high enough to sustain consumer spending. (Editor's note: this article was written in early March 2000 before the stock market panic of mid-April 2000.)

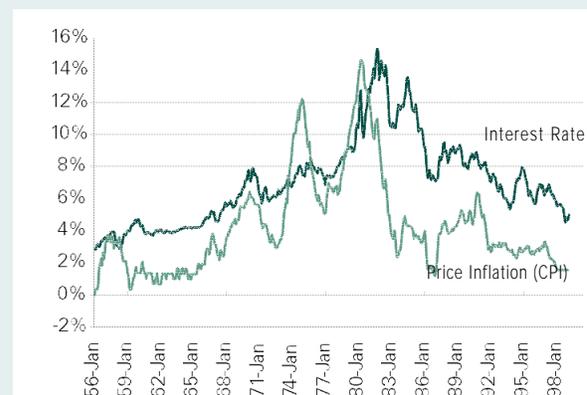
While these three trends and the likely increases in interest rates will dominate the nature of the expansion we will see in 2000, the overriding uncertainty is how long the economy can continue to grow faster than its capacity. The Federal Reserve has warned that a lack of balance between the growth in spending and the growth in the ability to produce cannot be sustained without increasing inflation. The Fed has warned that it will move to prevent inflation when it believes the threat has become too great.

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Despite the increased integration of the world's economies, distinct regional cycles remain.

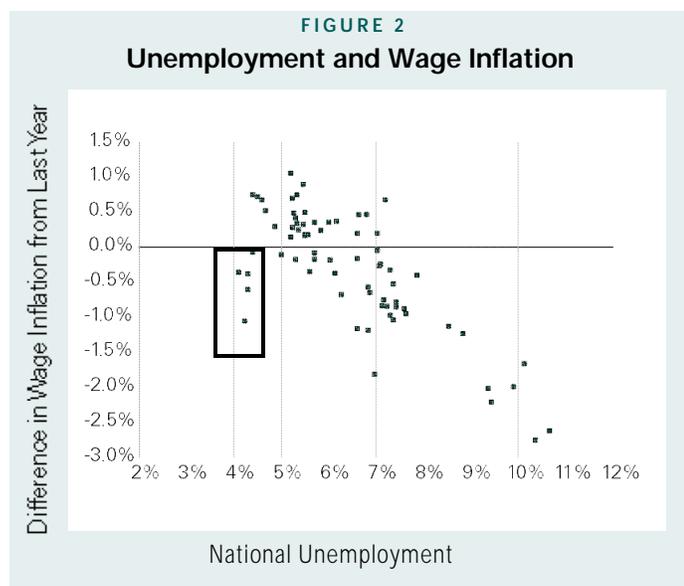
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FIGURE 1  
Interest Rates and Inflation



## Decline in Unemployment and Increase in Wages

The recent decline in unemployment has been welcome, but the question remains whether further declines are possible without an outbreak of wage inflation. I must confess that I am surprised that wage inflation has not already appeared. Figure 2 shows the relationship between wage inflation and unemployment in the 1980s and 1990s. The observations in the box show the record for the past five quarters. Clearly, the recent performance has shown much less inflation than would be expected based on the historical rela-



tionship. It is this benign performance of wage inflation that has permitted the economy to reach very low levels of unemployment in 1999. But regardless of the extent to which past relationships have changed, it remains the case that employment cannot grow more rapidly than the labor force indefinitely.

Wages can be measured in two ways. By one measure wage inflation has been benign in recent years, while by the other measure it has been explosive. One of the two major surveys of wages is a measure of wages paid by firms. The other survey measures wages received by workers. These two surveys have often yielded different results, for reasons that are related to the process of the typical business cycle, but the difference between the two rates of wage inflation is larger now than it has ever been. Wages paid by firms have not increased as much as would have been expected based on the past relationship between wages and unemployment. It is the inflation in wages paid by firms that is shown in figure 2. Wages received by households have soared. This difference has had wonderful implications for overall economic performance. Inflation has remained low because labor costs have been contained at the firm level, while labor income at the household level has grown rapidly and helped to support consumer spending.

How can wage increases at the firm level be lower than wage increases received at the household level? The answer is found in promotions and job reclassifications. A promotion leads to a wage increase for an individual worker. But a firm does not report wage increases for each worker, but rather reports wage increases for each job classification.

The metaphor of a job ladder helps to explain the difference. Think of a hierarchy of jobs that ranges from simple to difficult. The difficult jobs are on the top rungs of a ladder and the simple ones are on the bottom. Each job is filled by a worker, hence all employed workers are assumed to be standing on one of the rungs of the job ladder. As the economy expands, each rung of the ladder gets wider and new employees are needed to fill the new vacancies.

Many of the unemployed workers are not qualified to enter the work force at the top rungs, however. They typically enter employment at a lower rung. To fill the vacancies on the upper rungs, it is necessary to promote existing workers. In this way, a widening of each rung causes workers to climb the job ladder to more difficult and better paid positions, and hence to increase the number of vacancies on the bottom rungs for the unemployed to fill.

Workers receive pay increases from two sources in the job ladder metaphor. One increase comes from climbing the job ladder to better paying jobs on the upper rungs. The second source of pay increases for workers comes when firms raise their pay scales for the whole job ladder, which implies that they increase what is paid to workers on each rung of the ladder. On the surveys of wages at the firm level, firms report the amounts they pay at each rung of the ladder. In the household surveys, individuals report the wages they have received, which include increases from moving up the job ladder as well as increases they have received because the whole job ladder has received increases.

With widespread labor shortages, and with unemployment low and falling, the opportunities for workers to move up the job ladder in recent years have been unparalleled. The wage surveys show the largest divergence ever between the increased wages being earned by households and the increased wages being paid by firms. Since it is wages paid that is commonly thought to be inflationary, the recent expansion has had a surprisingly small increase in inflationary wage increases when judged by the large decline in unemployment we have experienced.

## Wages and Productivity

Official productivity statistics measure employment at the firm level. The hidden increase in wages that was noted in the preceding section can also be construed as an unmeasured increase in productivity.

The increase in pay from climbing the job ladder is a measure of the increase in the market value of the

worker's ability to produce. It is an increased payment for the particular configuration of skills that a worker possesses.

Macroeconomic measures of the growth in employment over the business cycle camouflage this possible increase in productivity. This increase arises because the average value of the skills of the unemployed are less than the average value of the skills of the employed. As the unemployment rate falls, we would expect to see a decline in actual worker productivity. If measured productivity does not fall, we could claim that the absence of a measured decline hides an increase in real productivity.

How does the current economic expansion affect productivity? From the perspective of the employer, the new people employed on each rung of the ladder after the expansion are slightly less qualified than the employees who were on the same rungs before the expansion. Worker qualifications have been downgraded. Productivity might be expected to fall. Hence the absence of a decline in productivity represents a hidden productivity increase.

Climbing up the job ladder is great from the perspective of the climbing workers, but it downgrades the average skill level at each rung of the ladder for the firm. There is no prior reason to expect that an expansion would lead to a reduction in the levels of skills expected of workers. Hence, there is a sense in which the increased pay of workers reflects the increased value of their old skills to the economy. It is a productivity increase in the sense of the increased value of the work performed by each worker.

## International Forces

Despite the increased integration of the world's economies, distinct regional cycles remain. At one extreme, the United States has just been through a wonderful decade, while at the other extreme, Japan has had a terrible one. Other economies have performed at levels between these two extremes, with Europe showing signs of life in 1999 that will continue into 2000.

The birth of the euro went smoothly in a technical sense, but its economic performance has been weak. This weakness has mistakenly been blamed on an apparent skepticism of investors for Europe's future economic performance. In my view, the euro's problem is a much simpler one related to the current supply and demand for euro-denominated assets. The euro bond market has exploded beyond anyone's anticipation. But the explosion is driven by an increased willingness on the part of large firms to float euro securities, not by an increased demand for those securities by institutional investors. The increased supply of euro securities is from companies with a large exposure to euro-denominated risks. It

should not be interpreted as a speculative position taken by these companies based on their political judgment about the long-term future of Europe.

Not surprisingly, the unexpectedly large issuance of these euro-denominated securities is having the same depressing effect on the value of the euro as would the sale of any euro-denominated asset. If companies continue to borrow in the euro market, the euro will remain weak. And the incentive to borrow in euros will remain strong as long as euro interest rates remain well below dollar interest rates.

Recovery is expected in 2000 not only in Europe but in the rest of the world as well. The one major exception is Japan, which is still digging out from the problems caused by its bubble of the late 1980s—declining real estate prices, bad loans, and excessive levels of capital investment. As recovery proceeds abroad (except in Japan), exports cannot be expected to

pick up to the levels they reached in 1987 before the Asian currency crises, because much of the rest of the world has devalued so strongly since then. So even if foreign economies recover, they will retain a cost advantage that will make it difficult for U.S. exporters to keep their market shares abroad. As a result, I expect only a modest improvement in our trade deficit in 2000 despite the emergence of strong growth abroad.

Strong growth abroad will hurt the U.S. economy by leading to increases in the prices of raw materials. These prices started to increase in 1999 and their further increase in 2000 could be a major inflationary force in the U.S. Oil prices in 2000 will depend not only on political forces, but also on the demand for oil, which should grow. Past OPEC price increases have been able to stick without cartel cheating only in 1973 and 1979, which were periods of strong economic performance with a growing demand for oil. A continued effort to substitute other energy sources for oil (similar to what occurred in response to past oil price increases), along with technological breakthroughs in the use of alternative sources of energy if oil prices remain high, would suggest that OPEC would not be wise to raise prices too much above current levels.

Every \$15 per barrel of oil represents 1 percent of GDP. Expenditures on oil are now 2 percent of the U.S. GDP, up from one percent before the recent price increase. On this basis further modest price increases are not likely to derail the current strong expansion. At this point, it would take increases in the price of oil to \$60 per barrel or more to disrupt the U.S. economy.

## Wisconsin

Labor shortage in Wisconsin continues and will dominate the outlook for Wisconsin this year and next (see

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The big story in 2000 will be the battle between the economy's strong willingness to buy and its limited ability to produce.

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caused by its bubble of the late 1980s—declining real estate prices, bad loans, and excessive levels of capital investment. As recovery proceeds abroad (except in Japan), exports cannot be expected to

FIGURE 3  
Unemployment Rates

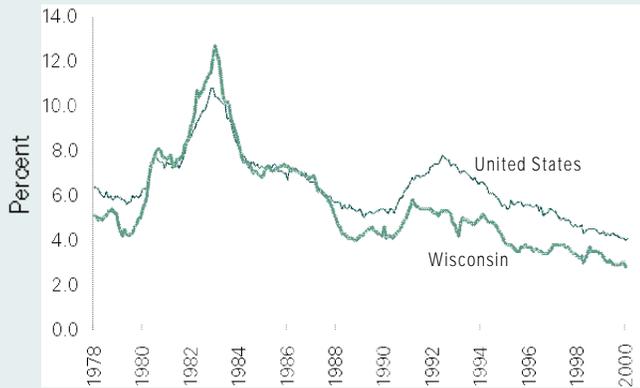


figure 3). Because times are now good in other states as well, there is little reason to expect an in-migration of workers from other states to alleviate Wisconsin's labor shortages. Furthermore, labor force participation is already so high it is hard to expect much further increase in employment from the existing population.

Employment in manufacturing may grow some as exports recover some strength. But exports are unlikely to return to previous levels because devaluations abroad have lowered costs. The dollar will have to fall—an unlikely event—if exporters are to regain their markets abroad.

Growth in manufacturing employment will come at the expense of the service sector as workers move to the higher paying jobs in manufacturing. Wage increases are likely to continue in Wisconsin especially at the lower end of the wage scale at least as the shortage of workers is likely to worsen. Employment growth in Wisconsin is likely to remain about a half percentage point below the national average because of the labor shortage. ■



## La Follette Policy Report

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