CHAPTER 5

Human Resources in the 1990s

THE SUSTAINED ECONOMIC EXPANSION of the 1980s has produced remarkable growth in employment and increased economic opportunity. As the Nation looks ahead to the 1990s, new challenges demand attention. Some have forecast that labor shortages—especially among skilled workers—will dominate the next decade and may limit the potential for economic growth. Based on the experience of past decades, however, the remarkably flexible U.S. labor market should—if left to itself—respond well to these new challenges. But continued growth will require increased labor mobility, reduced barriers to employment, and ongoing investment in the skills and knowledge of the work force.

The President has proposed a variety of new initiatives that will improve the productivity of American workers and the well-being of American families. The efforts of this Administration include new initiatives to raise the quality of the Nation's schools, changes in existing programs to ensure effective employment assistance to disadvantaged workers, implementation of a newly designed welfare system, innovative initiatives to improve housing opportunities for low-income families, and support for legislation that will decrease employment barriers for disabled workers. Coupled with sound macroeconomic policies, these initiatives will help ensure productive employment opportunities and economic security for American families.

ACHIEVEMENTS OF THE 1980s

Job opportunities for the U.S. population improved markedly in the 1980s. Since the beginning of the current expansion, the economy has created more than 20 million new jobs. The civilian unemployment rate has fallen from 9.7 percent in 1982 to 5.3 percent in 1989, its lowest level in 16 years. In 23 States, the unemployment rate in late 1989 was 4.5 percent or lower. And for almost every major demographic group, jobless rates in 1989 were at their lowest levels since the early 1970s. These gains stand in sharp contrast to the 1970s, when the rate of unemployment was successively higher at each business cycle peak.

U.S. employment growth has been especially strong in comparison with other developed nations. Major industrialized countries such as the United Kingdom, West Germany, France, and Japan have all experienced slower employment growth than the United States throughout the 1980s. Indeed, the total increase in employment in the United States since 1982 is greater than the increases in Western Europe, Canada, and Japan combined and is nearly as great as the entire work forces of Spain and Portugal combined.

Over the past three decades, the American people have clearly benefited from a remarkably flexible labor market that has successfully created jobs for its workers despite major demographic and industrial changes. This flexibility stems partly from an ongoing commitment to limit government interference that hinders economic adjustments. It also reflects the historic willingness and ability of the U.S. private sector—both workers and firms—to adapt to economic change.

For example, the baby-boom generation, born between 1946 and 1964, flooded the labor market in the late 1960s and 1970s. Yet, the economy successfully absorbed this group. Similarly, women's labor market participation has risen markedly over the past three decades. That increase in supply did not lead, as might have been expected, to lower wages and higher unemployment among women. Instead, women have enjoyed substantial economic gains. Female and male unemployment rates converged in the 1980s for the first time since World War II. And women's wages increased substantially relative to men's, closing almost a quarter of the gap in pay rates between the sexes.

In addition, the labor market has responded to major shifts over the past decade in labor demand across industries and occupations. International competition, technological change, and changing consumer demands have altered the nature and location of many U.S. jobs. Job mobility, migration, and skill retraining have all helped most workers to find new jobs in this rapidly changing labor market.

Labor markets do not adjust instantaneously. Rather, workers and employers respond over time to changes in supply and demand through the workings of the market. The growing economy in recent years has made it even easier for unemployed workers and new labor market entrants to find jobs and for working Americans to increase their living standards.

CHALLENGES OF THE 1990s

Perhaps shaped by experiences during the Great Depression in the 1930s, the debate on macroeconomic policy over the past five decades has been heavily influenced by fears that the U.S. economy could not produce enough jobs for its workers. Undoubtedly, occasional episodes of declining economic growth and rising unemployment will occur. But analysis of impending labor market developments in the 1990s suggests that other concerns will also demand attention. Many observers now worry about the availability of workers—especially skilled workers. Some have even argued that labor shortages will dominate the 1990s and may slow economic growth.

Indeed, changes in the labor force and the economy over the next decade will produce new challenges. The relatively small baby-bust generation is moving into its working years, reducing the share of new labor market entrants in the population. At the same time, the demand for skilled labor is likely to increase as the relative importance of the service sector grows.

As in earlier decades, the labor market should naturally adapt to these changes over time. Firms will shape compensation packages to attract and train the workers they need, and workers will respond to the higher wages that result from expanded skill demands by seeking additional training. Appropriate government policies can help quicken the pace of adjustment. To ensure an environment in which economic growth can be sustained over the next decade, private business must work together with all levels of government to provide Americans with the skills and the education necessary to function effectively as workers in a modern economy.

Chapter 4 of this *Report* discusses the need to increase investment in physical capital and in research and development. This chapter examines the concurrent need to increase the Nation's investment in human capital by expanding the skills and knowledge of the Nation's youth and strengthening job training for the existing work force. Reducing barriers to labor mobility and to the use of additional sources of labor—such as immigrants, the elderly, and the disabled—will also be necessary if employers and workers are to adapt quickly to labor market change.

The years ahead will provide a unique opportunity to integrate the poor and disadvantaged into the work force. A healthy and growing economy will provide additional opportunities for poor families to raise their living standards. Policies that increase employment and earnings of the poor can both reduce poverty and add to the Nation's productive resources.

Impending changes in the labor force pose real challenges for the 1990s. But those who argue that labor shortages will stall the economy in the next decade ignore the flexibility and adaptability of U.S. firms, workers, and governments.

THE CHANGING U.S. POPULATION

Several major demographic trends will influence the U.S. economy and its labor markets in the 1990s. The steady aging of the baby-boom generation will continue to increase the average age of the work force. As Chart 5–1 shows, the percentage of the population between ages 30 and 49 rose from 23 to 29 percent between 1970 and 1988, and is projected to rise to 31 percent by 2000. The percentage of the population age 65 and over will also continue to grow, while the percentage age 85 and over will grow even more rapidly. At the same time, the lower birth rates that followed the baby boom have resulted in a declining number of teenagers and young adults in the population.

Chart 5-1

AGE DISTRIBUTION OF THE U.S. POPULATION. The aging of the population means a more experienced work force, a declining share of teenagers, and an increasing share of elderly.

Source: Department of Commerce.

In addition, the share of the population composed of racial and ethnic minorities—particularly blacks, Hispanics, and Asians—continues to increase. Growth in the Hispanic community has been particularly rapid. Since 1980, as a result of higher birth and immigration rates, the Hispanic population has expanded at a rate five times as fast as the rest of the population. Inflation-adjusted weekly earnings among full-time minority workers have not risen since 1980. After several decades of steady growth, relative weekly earnings of black men have also remained flat throughout the 1980s, at about three-fourths of white men's weekly earnings. Employment has gone up among minority workers, however, increasing labor market income for this group as a whole.

This changing population mix has important implications for the U.S. labor market. The movement of the baby-boom generation into its thirties and forties means a work force that is, on average, older and therefore somewhat less flexible and mobile. The declining share of teenagers and young adults has meant labor shortages for those industries that traditionally hire young people for part-time jobs. At the same time, employment opportunities have increased for those older persons who seek employment.

The growing population of Hispanic and Asian workers, many of whom speak English as a second language, will need to adapt fully to the U.S. labor market. This population will also create new challenges for schools and employers to offer training and assistance to enable these workers to be fully integrated into the economy. Historically, this challenge is familiar to the U.S. economy; current immigration rates, while above those of recent decades, are well below those around the turn of the century. The labor market successfully absorbed these earlier immigrants, who worked hard for economic security in their adopted country. The growing share of racial and ethnic minorities in the work force also underscores the importance of ensuring equal economic opportunities for all workers.

Not only is the composition of the U.S. population changing, but so are the ways in which individuals form families and households. The proportion of individuals who do not live with any relative continues to increase, both because young adults spend more years living on their own and because the number of elderly single individuals has been rising. The share of female-headed households with children is also increasing, from 5 percent of all households in 1970 to 7 percent in 1988. Concurrently, the share of married-couple households has declined, from 71 percent of all households in 1970 to 57 percent by 1988. The nature of these married-couple households has also changed dramatically; in most of today's marriages, both husband and wife work. Even among married women with preschool children, 53 percent work at least part-time outside the home.

These trends underscore the increasing importance of women's earnings. More women are the sole earner in the household, either as single individuals or as single parents. Moreover, married couples are relying more heavily upon women's earnings. By 1985, women's earnings provided 28 percent of all income among white households and 46 percent of all income among black households. Women's wages have risen relative to men's over the past decade, and continued improvements in job opportunities and wages for women will help many low-income households improve their standard of living.

These demographic and household trends set the stage for some of the important labor market challenges of the 1990s:

- Adjusting to an aging labor force and a smaller number of new labor market entrants.
- Absorbing a larger share of workers from varying ethnic and racial backgrounds and ensuring economic opportunities for all workers.
- Continuing the expansion of women's labor market opportunities.

The Department of Labor estimates that more than two-thirds of all new labor market entrants between 1988 and 2000 will be Hispanic, Asian, black, or female. Strong economic growth depends on finding productive employment opportunities for these workers.

SKILLS AND EDUCATION: INVESTING IN HUMAN RESOURCES

A modern growing economy requires an educated and flexible labor force. The median years of schooling acquired by young adults (aged 25 to 29) rose steadily in this country to an historic high in 1976 of 12.9 years. But there has been no increase since then, while the need for a more highly skilled labor force continues to grow. Raising the quality of education in elementary and secondary schools is at least as important as increasing years of schooling. Higher achievement among students of every age will better prepare tomorrow's workers for productive employment. The Federal Government can play an important leadership role in stimulating improvement in the education and training of U.S. workers, but it is important to recognize that the primary responsibility for this task resides in State and local governments and in the private sector.

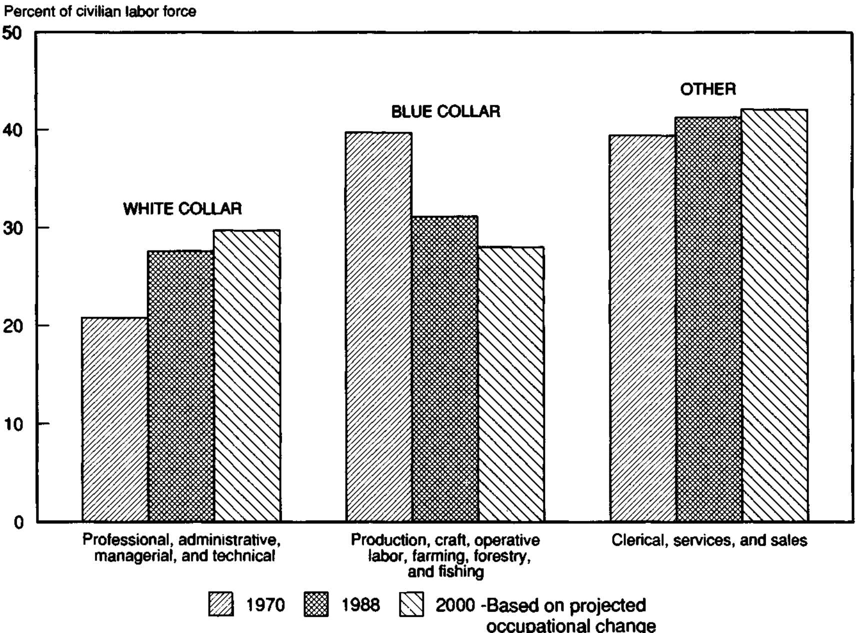
THE GROWING NEED FOR SKILLED LABOR

The demand for more highly educated labor has increased steadily for many decades in the United States. As Chart 5-2 indicates, the share of jobs in occupations requiring greater education has expanded. In 1970, 21 percent of the work force were in white-collar jobs (professional, administrative, managerial, and technical occupations). By 1988, 28 percent of workers held these jobs. Correspondingly, the share of blue-collar jobs (production, craft, operative, labor, and agricultural work) fell from 40 percent to 31 percent. The share of sales, clerical, and service jobs rose slightly, and there was a shift toward more skilled jobs within these categories.

These occupational changes have been closely related to the declining share of employment in traditional manufacturing industries and the rising share in service-producing industries. In con-

Chart 5-2

TRENDS IN OCCUPATIONS. Projected growth in white collar and service occupations will demand a more highly skilled labor force in the future.



Source: Department of Labor.

trast to the stereotype of service-sector jobs as low-skilled labor, the growing service sector in general contains a higher percentage of jobs requiring more education. Fully 24 percent of workers in the service-producing sectors of the economy held a college degree in 1980, while only 20 percent had no high school diploma. In contrast, only 11 percent of the workers in the goods-producing sectors held college degrees, while 30 percent had not completed high school.

As the economy continues to shift toward services, the need for skilled labor will continue to rise. The Bureau of Labor Statistics predicts that the fastest employment growth between now and the year 2000 will occur in white-collar occupations, where 57 percent of all workers are college graduates and 97 percent are high school graduates. Blue-collar occupations, where only 5 percent are college graduates and 71 percent are high school graduates, will continue to shrink.

EDUCATION AND PRODUCTIVITY

Just as a healthy economy requires investment in physical capital to maintain productivity growth, so it requires investment in human capital—in the education and training of workers. The skills and attitudes that young workers bring to the labor force are shaped by their families and by the public and private school systems of this country.

Education raises skill levels that increase job performance and productivity. Higher mathematics and verbal achievement scores are associated with higher labor productivity and wages. Years of school are related to increased future earnings and lower risk of unemployment. Moreover, studies show that workers who are better at understanding directions, asking questions, and solving problems are also more productive.

Increased education also provides greater job flexibility for workers in a changing economic environment. When production technologies change, better educated workers learn new procedures more easily. Moreover, when economic change leads to job loss, better educated workers find new jobs more readily.

Concern over declining school quality in the United States has led researchers to probe more deeply into the relationship between educational achievement and economic growth. Studies suggest that 10 to 15 percent of economic growth after 1945 was attributable to improvements in education. Thus, improving the quality of education may have lasting effects on the Nation's standard of living.

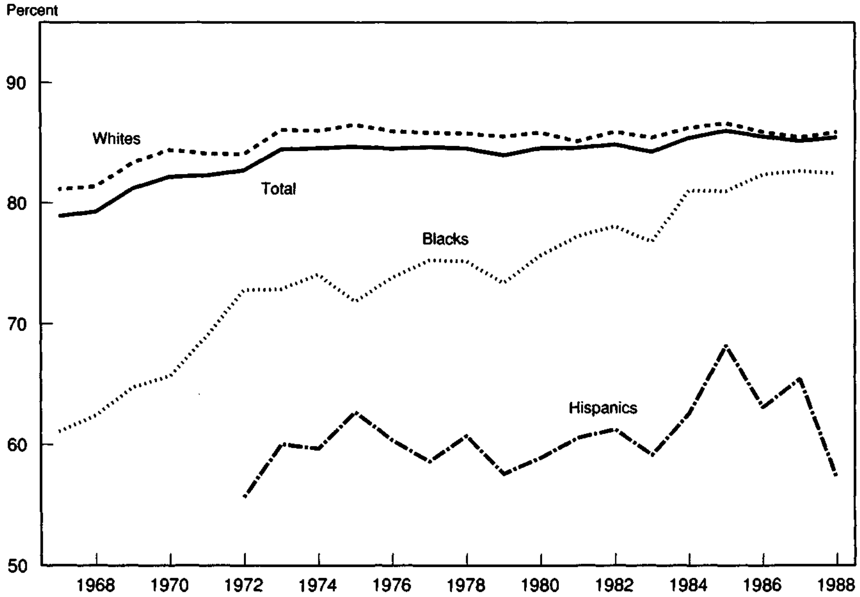
TRENDS IN BASIC SKILLS

A high school diploma is often considered the minimal requirement for a good job. Currently, 85 percent of the 20- to 24-year-old population has completed high school. High school graduation rates have been largely stagnant since the mid-1970s (Chart 5-3). The primary exception occurs among young blacks, whose dropout rates have fallen and whose high school completion rates have increased steadily to a current level of 82 percent. Among young Hispanics, however, high school completion rates remain at a very low 57 percent. The 15 percent of young adults who are high school dropouts face low earnings and high unemployment rates (Box 5-1). The lack of significant progress over the past decade in raising overall high school completion rates is a serious concern for an economy with a declining need for unskilled workers.

As important as whether a student has completed high school is the level of achievement a student attains in high school. The National Assessment of Educational Progress (NAEP) indicates that high school students' performance in basic subject areas either improved slightly or remained constant over the past two decades, although minority students showed marked improvements. Nonetheless, a significant number of high school students still lack adequate basic skills. The NAEP indicates that about 14 percent of 17-

Chart 5-3

HIGH SCHOOL COMPLETION RATES BY RACE. Total high school completion rates have been largely stagnant for the last decade, although completion rates of blacks have increased.



Note: Data are percent of 20 to 24 year olds with high school diplomas.
Source: Department of Commerce.

year-olds cannot read above the "intermediate" level, attained by nearly three-fifths of all 13-year-olds. Nearly 60 percent of all 17-year-olds cannot read well enough to "understand, summarize, and explain relatively complicated information," according to the NAEP. International comparisons of science and mathematical competency show U.S. students performing below students from such countries as Japan, South Korea, the United Kingdom, and Spain. Major improvements in the quality of U.S. schools are badly needed. Policies must be implemented that will reward excellence and increase the skills and achievement of U.S. students at all levels of ability.

TRENDS IN HIGHER EDUCATION

An increasing number of jobs in today's economy require college-level training. Moreover, maintaining competitiveness in technological development and innovation requires a pool of well-trained researchers with advanced university degrees.

Box 5-1.—Widening Earnings Differentials

Real median hourly earnings (earnings adjusted for inflation) have increased over the past decade, but since the mid-1970s the hourly earnings of young male high school graduates and dropouts have fallen dramatically relative to the earnings of more educated workers. More educated workers have seen substantial real earnings growth, implying that the economic rewards to education are rising. But real earnings among less educated workers have actually declined, even during the expansion of the 1980s. These changes have occurred across all age groups.

These shifts in relative earnings are still only partially understood, but they are clearly related to the increased competition in the world market for manufactured goods, which has led to a decline in high-wage, low-skilled jobs. The widening earnings differences are attributable to more than just sectoral shifts away from manufacturing, however, for they are also occurring within nonmanufacturing industries. If these changes persist, economic opportunities for low-skilled workers in the United States will be seriously limited. The rising rewards to education, however, will enhance the incentives for workers and students to invest in education and training.

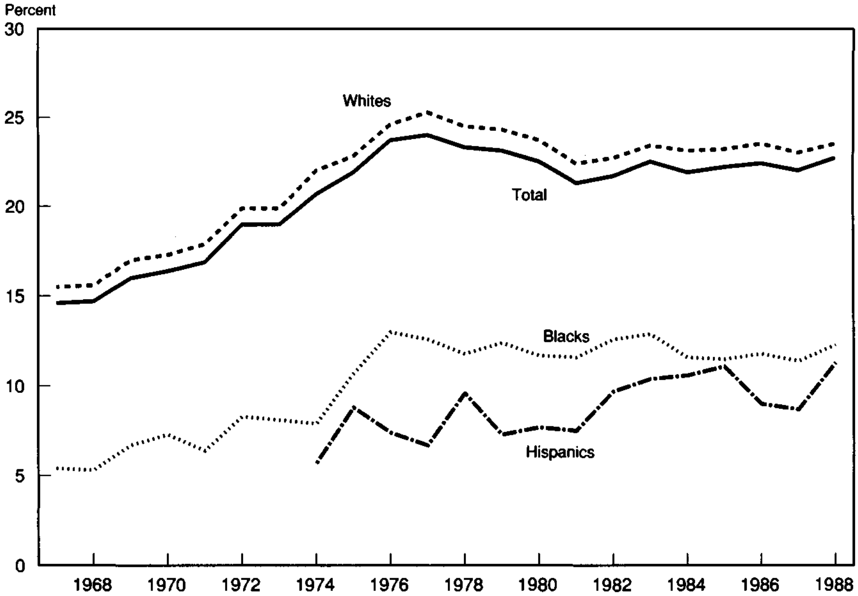
Undergraduate Degrees

The growing demand for skilled workers means a growing need for college graduates. However, the share of 25- to 29-year olds who have completed 4 or more years of college has been virtually unchanged at about 22 percent of the young adult population since the early 1980s (Chart 5-4). Some evidence indicates increasing college enrollment rates among recent high school graduates, but this increase has not yet fed through to college completion rates. Only 12 percent of young blacks and 11 percent of young Hispanics complete 4 or more years of college. Not shown in these data is a small increase in college completions among older students who return to school at a later age.

The rising cost of a college degree may be holding down college completion rates. Since 1980, the cost of a bachelor's degree at 4-year colleges and universities grew twice as fast as the consumer price index. The availability of financial aid (primarily student loans) has helped to offset these mounting costs, but the out-of-pocket expenses paid by students and their families has nonetheless risen.

Chart 5-4

COLLEGE COMPLETION RATES BY RACE. After rising through the mid-1970s, the percent of young adults completing four or more years of college fell in the late 1970s and leveled off in the 1980s.



Note: Data are percent of 25 to 29 year olds who have completed four or more years of college.
Source: Department of Commerce.

Rising relative wages for college-educated workers at least partially reflect a rising demand for their services. Over the long run, higher earnings of college graduates should induce a greater number of students to attend college, even in the face of rising college costs, although a lag may occur before high school students respond to this incentive.

Advanced Degrees

In an increasingly competitive international economy, the United States needs highly trained specialists and researchers; this requires a growing pool of workers with advanced university degrees. While information is available only on the total number of advanced degrees awarded, assuming that these degrees are given to 25- to 34-year-olds, then about 7 percent of young adults currently receive a master's degree in some field, while slightly fewer than 1 percent receive a Ph.D. These percentages have fallen slightly over the past decade, although large increases have occurred in the number of business and management masters' degrees awarded.

Recipients of advanced degrees are disproportionately white males. Although black and Hispanic students receive more than 8 percent of all bachelors' degrees awarded, they receive only 7 percent of all masters' degrees awarded and 5 percent of all Ph.D.s. In contrast, women receive approximately one-half of all masters' degrees. But women still receive a disproportionately small share of the doctoral degrees awarded, particularly in the natural and computer sciences and in engineering. Attracting a wider range of students into advanced study in all fields will expand the pool of future researchers and broaden the diversity of research perspectives, building the Nation's capacity for creative research and technological advance.

ON-THE-JOB TRAINING

Because many jobs require a significant amount of on-the-job training, workers do not stop learning when they leave school. Some of this training involves classroom participation or organized on-the-job teaching, but much of it involves informally learning procedures and responsibilities. Wages of workers who have received on-the-job training are between 10 and 30 percent higher than those of workers with similar characteristics who do not receive such training, a clear indication that on-the-job training results in productivity increases. On-the-job training also often encourages long-term job retention.

Approximately 5 to 12 percent of the work force claim to have participated in formal on-the-job training programs. (Estimates vary depending on how training is defined.) A higher percentage (around 15 percent) indicate that they have received informal on-the-job training with their current employer.

Theoretically, on-the-job training could reduce skill differentials that result from differences in formal education. The evidence indicates, however, that workers with more years of schooling are more likely to receive formal on-the-job training. Training is also more likely among white workers, more experienced workers, and full-time workers. Thus, there is little evidence that on-the-job training offsets other differentials; given the group of workers who receive it, it may well widen them. As skill demands rise, employers in the years ahead may have an incentive to provide on-the-job training to workers who have not traditionally received it.

IMPROVING THE EDUCATION AND SKILL LEVELS OF U.S. WORKERS

The Administration is strongly committed to improved education and training opportunities for all Americans. State and local governments have traditionally accepted primary fiscal responsibility for education, with the Federal Government providing small amounts of financial support—only 8.5 percent of the funds spent on education in 1986–87, for example. The Federal Government, however, still plays a vital role in shaping educational policy, as exemplified by last fall's Education Summit. For only the third time in history, a President called together the Nation's Governors and the Cabinet to discuss a vital national issue. As a result of this summit, the Administration is working with the Governors to define national performance goals for the educational system, to increase spending for preschool programs, to strengthen efforts at school reform, and to provide greater flexibility in Federal and State funding for local schools.

Improving Elementary and Secondary Schools

In terms of average per pupil expenditures, U.S. spending on elementary and secondary education is greater than that of most other industrialized nations; only Switzerland spends more resources per child. Despite these expenditures, elementary and secondary students do worse on educational proficiency exams than students from many other nations. Thus, the challenge is not to spend more, but to spend more effectively. Elementary and secondary education in this country must be dramatically improved. For instance, the President has challenged the Nation's schools to make U.S. students first in the world in mathematics and science skills by the year 2000. Improving the quality of education and training will require local school *flexibility* to meet the needs of students with diverse backgrounds, *choice* by students and their families to ensure high-quality schools, and *accountability* of educational institutions to achieving performance goals and standards.

The Administration's proposed Educational Excellence Act (Box 5–2) is designed primarily to provide leadership and support to State and local governments to improve the quality and effectiveness of America's schools and the achievement of America's students. Schools are the Nation's most prominent investment in its human resources; more than 4 percent of gross national product is spent on elementary and secondary schools alone. It has become clear over the past 20 years, however, that spending more money does little by itself to guarantee better schools. Once other aspects of the school environment are taken into account, differences in school expenditures have little relationship to educational achievement. Parental background and home environment are crucial determinants of achievement, but so are effective teaching and certain aspects of school organization, as the Educational Excellence Act recognizes.

Good education requires effective teachers. While teachers' real salaries are now at all-time highs and have been rising relative to those of other workers, many educators still express concern that teaching is not attracting the highest quality applicants. Particularly as a host of new career options have opened up for women, many of whom have traditionally trained as teachers, good female

Box 5-2.—The Proposed Educational Excellence Act

Because of its strong commitment to better schools, the Administration has proposed the Educational Excellence Act. This act will strengthen the quality of education in this country by providing:

- Presidential Merit Schools awards to schools making progress in raising educational achievement, creating a drug-free environment, and reducing dropout rates;
- Presidential Awards to excellent teachers;
- Short-term assistance to districts establishing magnet schools;
- Assistance to States developing alternative teacher certification programs;
- Emergency Grants to urban school districts with severe drug problems;
- A National Science Scholars' program to fund top high school students who undertake college work in the sciences, mathematics, or engineering; and
- Matching funds to support historically black college and university endowment fundraising.

college students have often been encouraged to enter other fields. Many States are working to improve teacher quality by attracting better students into teaching and through alternative certification and better preparation and training. Excellence in teaching can be rewarded through merit pay systems and greater public recognition of effective teaching.

Teachers need an effective school environment in order to do their jobs well. The President has spearheaded an effort, together with the Nation's Governors, to establish national educational performance goals, including a challenge to raise high school graduation rates to 90 percent and to make all schools drug free by the year 2000. A number of States have adopted statewide minimum competency tests to identify students and schools that require special attention and to ensure that schools provide students with an identified set of basic skills. In addition, many school districts are trying to involve private employers much more closely in the school system, both by encouraging employers to offer students valuable work experience, and by soliciting advice from employers on the skills needed by students. Some school districts are also exploring expanded school hours, a longer school year, and greater parental involvement in school decisions. The key is not only to allow schools flexibility to use the educational methods most effective for their students, but also to demand that schools be accountable for the resulting skill levels of their students.

The Administration particularly supports efforts to improve the quality of schools by offering students and their families a greater choice over which school they can attend, thus expanding competition among schools and increasing parental involvement in the education system. Allowing extensive parental choice among schools is a new idea, and from this and related reforms are emerging models of how school districts can implement choice most effectively.

Increasing Participation in Higher Education

The U.S. system of higher education—vocational programs, colleges, and universities—has long been among the best in the world. It is important to maintain the quality of this vital national resource and, given the increasing demand for skilled workers, to encourage even more students to use it. Improving the Nation's elementary and secondary schools will increase the number of students who are prepared for higher education. But other changes may be desirable as well, including those proposed in the Educational Excellence Act.

Counseling high school students about the possibilities and advantages of further education, and encouraging them to continue their studies, could increase college and vocational school enrollments. Greater involvement of private business in schools may also help, if students learn about the advantages of college or vocational education through internships or contact with older workers. Extremely low rates of college and university attendance among minority students are a particular public concern, especially because these students represent an increasing share of new work force entrants. High schools serving these students should prepare and encourage them to continue their education.

Higher education costs money. Because a student cannot use as collateral the career enhancement that higher education is designed to provide, government has come to provide loan assistance as well as grants and fellowships to low-income students who need this help. The Federal Government provides directly or subsidizes a substantial portion of all financial assistance—loans and grants—received by college students. Continuing support for these college aid programs is important, with continuing attention to their ongoing effectiveness and targeting.

Increased access to graduate degree programs is important to maintain a first-rank group of university-level researchers and teachers. The Federal Government has long encouraged advanced study and research. For instance, the National Science Foundation (NSF) finances fellowships to students pursuing advanced degrees in particular scientific fields. The NSF also underwrites fellowships that promote advanced research and study by minorities and women in the sciences. Given current concerns about potential shortages of personnel in technical and scientific areas, continued Federal funding of these and similar programs should help encourage a diverse group of students to pursue advanced study.

Adult Literacy

Led by the First Lady's work on behalf of adult literacy, this Administration has raised the level of public concern about the 20 million adult Americans who are functionally illiterate. These adults have difficulty performing simple tasks such as filling out a job application or reading a child's report card. Workers who lack basic skills are less productive on the job and experience higher unemployment. Furthermore, adult functional illiteracy can make it harder to improve school achievement; children of parents with low educational skills are also more likely to do poorly in school and to drop out.

Improvements in the Nation's schools will come too late to help these adults. Adult literacy is the focus of a wide range of private sector programs and volunteer organizations. One study estimated that 36 percent of Fortune 500 companies provide remedial basic skills programs to their workers. An estimated 200,000 volunteers provide individual and small-group tutoring to other adults. A variety of Federal, State, and local agencies also support or provide adult literacy services.

This Administration is strongly committed to reducing adult functional illiteracy. By publicly recognizing volunteers and private organizations working in this area, the Administration has increased the visibility of these efforts. The Administration is also committed to better coordinating Federal adult literacy programs, increasing Federal funding for these programs, and expanding research on effective adult literacy teaching techniques.

Job Training

Although improvements in the public and private school system of this country are important, classroom schooling is not the only way to provide a quality work force. On-the-job training may be more appropriate. The primary responsibility for training rests with employers and workers. As new skills are needed, employers have incentives to provide appropriate training to their workers, and workers have incentives to seek such training.

The Federal Government has a history of limited involvement in job training, largely through programs aimed at low-skilled and unemployed workers. The leading public job training program today is the Job Training Partnership Act (JTPA), which works with the private sector to educate, train, and provide employment-related services to targeted groups of workers. JTPA finances programs for displaced workers, disadvantaged youth, migrant and seasonal workers, Native Americans, and veterans. The public-private partnership created by JTPA is important to its effectiveness. Additional skills are useful to individuals only if the workplace needs them.

The Administration has proposed amendments that improve the targeting and effectiveness of JTPA services for workers facing serious barriers to employment. These amendments include enhanced performance standards to increase accountability; better coordination of services and more attention to individual needs to improve program quality; and more intensive and comprehensive services for disadvantaged youth and adults to improve targeting. In addition, the Administration is implementing the Family Support Act of 1988 (discussed below), which requires all States to provide education, job training, and job placement programs for public assistance recipients.

THE CHALLENGE FOR THE 1990s

To ensure high economic growth in the future, all American workers must acquire effective skills and education. This effort will require building a three-way network consisting of the public schools and other government training programs, the private sector, and the households of workers, parents, and children who are part of both the school system and the work force.

LABOR SHORTAGES, WORKER MOBILITY, AND IMMIGRATION

As the U.S. economy enters the 1990s, concerns are growing about the effects of possible labor shortages on production and wages. Employers in some areas of the country report a shortfall of entry-level workers and are paying wages well above the minimum wage to attract new employees. Other firms report difficulties in hiring suitably trained employees for more skilled positions.

In many cases, limited supplies of workers with particular skills or in particular geographic areas have developed from changes in the labor force, forcing employers to intensify their efforts to attract new workers. In other cases, uneven patterns of economic growth and technological change have altered the skill requirements or location of jobs, resulting in labor shortages for employers in growing areas or industries and job losses among workers whose skills have become obsolete or who find themselves in areas with few job opportunities.

Most of the time the labor market has readily and naturally resolved such imbalances. Employers perceiving a labor shortage have often raised wages to attract workers, encouraging new entry or geographic mobility. Other firms have relocated to areas with a greater supply of available workers, coupled lower hiring standards with remedial and on-the-job training, or targeted nontraditional sources of labor such as older workers and the handicapped. Immigration has also been an important source of new workers in particular industries and occupations.

Labor markets typically do not experience long-run imbalances, but gradually adjust to changes in supply and demand. Governments can help the market to adjust more promptly and efficiently by avoiding or easing regulations that inhibit labor mobility and restrict the use of alternative sources of labor.

LABOR MOBILITY

In recent years, changes in the composition of output and in methods of production have shifted the demand for workers across industries, occupations, and geographic areas. As some jobs were eliminated, new jobs were created that required new skills and abilities. Because job elimination often occurred in geographic areas or in industries different from those of job creation, some workers were displaced from their jobs while others found new opportunities.

Overall, the evidence suggests that workers have adapted quickly to these structural changes. Researchers estimate that the gross flows of workers between employment and nonemployment vastly exceed the net changes in employment and unemployment reported in the official data. Even when the economy shows no net job creation, some estimates suggest that roughly 10 percent of all jobs each year are new, resulting from new business creation or the expansion of existing businesses. This job creation offsets the annual disappearance of about 10 percent of the jobs in the economy as firms close their doors or lay off workers. Compared with such rapid rates of job turnover, the annual net increase in jobs has been roughly 3 percent during the current economic expansion. *The ability of the United States to combine high job turnover with rapid employment growth and low unemployment reflects the flexibility of U.S. labor markets and the adaptability of the U.S. labor force.*

For some workers, of course, shifts in labor demand can create problems of adjustment, characterized by spells of unemployment or reductions in wages. These problems do not suggest that governments should prevent changes in the labor market. Rather, policies should be designed to ease the transitional disruptions associated with labor market change and to reduce barriers to mobility. The experience of workers who make successful job transitions indicates that encouraging geographic and skill mobility will promote more efficient labor market responses to economic change.

GEOGRAPHIC MOBILITY

All regions have shared in the current economic expansion, enjoying sizable employment gains and declining unemployment rates. But the pace of economic growth over the past decade has varied across regions. Many areas on the eastern and western seaboards and in the Southeast have experienced strong economic growth, aided by industrial diversification and a shift toward services since the mid-1970s. Growth in some areas of the Midwest has been slower, reflecting foreign competition in many heavy manufacturing industries and problems in agriculture. Many local economies in the Southwest still suffer the lingering effects of the decline in oil prices between 1981 and 1986.

National Migration

Free movement of workers within the United States offers a potential source of labor to employers in prosperous areas and potential opportunities for workers in depressed areas. For example, strong employment gains in both the South Atlantic and Pacific Coast regions have stimulated increased migration to those areas. In contrast, net outmigration has occurred from the Midwest and East South Central regions, where economic growth has been less robust.

Despite the widening regional differences in economic opportunities, overall migration rates did not increase in the 1980s. Between 1980 and 1987, about 6 percent of the population moved to a different county each year and about 3 percent moved to a different State, similar to mobility rates in the 1970s.

In part, workers may not have migrated more because in many areas higher living costs offset better labor market opportunities in the 1980s. Regional variation in housing prices widened considerably, as prices for both new and existing homes rose rapidly in various markets of the New England, mid-Atlantic, and Pacific States, but posted declines or only small increases in many parts of the South and Midwest. Because the largest increases in housing prices often occurred in areas with the greatest economic gains and employment opportunities, some workers who might otherwise have migrated to those areas were likely discouraged by high housing costs.

Other factors also influence migration. For example, differences in climate and local public services are an important consideration for many households and partly explain the steady migration from the snowbelt areas of the North to the sunbelt regions of the South and West over the past two decades. A more important factor in the 1980s, however, may have been the aging of the U.S. population. Possibly because of stronger family and social ties, established workers are less likely than younger workers to uproot their families and relocate to another part of the country. As a result, the aging of the baby-boom cohort may have reduced the geographic mobility of the population in the 1980s. While an older work force in the 1990s will continue to hold down geographic mobility, increases in the percentage of young, educated workers, who often participate in national rather than regional labor markets, could partially counteract this trend.

Firm Location

Firms also migrate, often relocating to labor markets with larger pools of potential employees. Moreover, new firms, which contribute significantly to economic growth and job creation, base their location decisions, in part, on wage costs and labor quality. In effect, the market often brings the jobs to the people.

In the 1970s, this type of mobility helped to reignite growth in once-depressed areas. As local economies in the industrialized Northeast deteriorated in the wake of the energy shocks of the 1970s, for example, new ventures in light manufacturing and services took advantage of the relatively experienced work forces remaining in those areas. Similarly, much of the improvement in the economies of the sunbelt regions resulted from decisions by employers to locate new plants where labor costs were traditionally low. And while employers in some areas located parts of their operations abroad, by outsourcing production to low-wage countries, some foreign producers set up plants in the United States.

More recently, changing patterns of regional growth have again reduced the regional dispersion in labor markets. Sluggish employment growth has led to an increase in unemployment rates over the past year from their very low levels in New England and in some mid-Atlantic States. At the same time, however, employment opportunities have improved markedly in many Southern States, reducing joblessness in areas experiencing relatively high rates of unemployment.

Recent advances in telecommunications and computers have enhanced a firm's ability to link dispersed locations—both office to office and home to office. As a result, the physical location of workers and jobs may become even less important, increasing the speed at which market forces balance geographic variation in economic growth.

OCCUPATIONAL MOBILITY

As might be expected, economic growth in the 1980s has also led to shifts in employment across occupations and industries. Productivity gains and international competition have eliminated many traditional blue-collar jobs, while the computer revolution and the expansion of the service economy have boosted the demand for technical and service-oriented skills. In response, workers have displayed a high degree of occupational mobility, either by switching occupations voluntarily as economic opportunities improved, or out of necessity, after losing a job.

Voluntary Job Changes

About 10 million workers, or 9 percent of employed workers, switched occupations in 1986, the latest year for which data are available. Nearly 90 percent of those workers who switched occupations did so voluntarily, following a career plan, or seeking better pay or working conditions. Such job changes enable workers to improve their economic status and, at the same time, allow the labor market to adjust to changing demand conditions.

The propensity to change occupations is highest for younger workers. Moreover, much of the labor market adjustment to changes in the composition of demand occurs through the initial choice of a career, usually by relatively young labor force entrants. This propensity is not surprising, given older workers' large accumulated investments in training and skill development. But it suggests that the aging of the baby-boom cohort could reduce the occupational mobility of the work force as a whole in the 1990s.

Education offers a possible solution to the demographic factors reducing occupational mobility. Because of the expanded opportunities available to them, more educated workers exhibit higher mobility rates than less educated workers. For tomorrow's work force, greater educational achievement can both broaden workers' initial career options and improve their potential for advancement.

Displaced Workers

Although most workers who changed occupations in 1986 did so voluntarily, 1.3 million persons switched occupations as a result of a job loss, typically reflecting a plant closing, production cutbacks, or elimination of a particular job. Such job displacements are an expected result of economic and technological gains that benefit the population as a whole, but can bring hardship to individual workers. Clearly, the ability of these displaced workers to transfer their skills to another job is important in maintaining the flexibility of the U.S. work force.

Many displaced workers find employment fairly soon after their job loss. More than 25 percent of displaced adult workers who switched occupations in 1986 found new jobs right away. More than 70 percent of workers displaced between 1983 and 1987 were employed in 1988; another 15 percent had retired or otherwise left the labor force.

Significant numbers of displaced workers were not successful in finding new jobs, however. The unemployment rate for displaced workers—14 percent in 1988—is well above the national unemployment rate. And more than one-quarter of those who did find new full-time positions experienced a drop in earnings of more than 20 percent.

In general, higher education levels and geographic mobility appear to lessen the costs of a job loss. Reemployment rates for displaced workers were significantly higher among more educated workers; higher levels of schooling substantially reduced both the time spent unemployed and wage losses. Workers who moved to another area after a job loss were also much more likely to find another job, with the percentage of displaced workers who moved typically averaging about 13 percent.

Retraining is another important component of strategies to increase work force flexibility, particularly for workers with low general skills. Title III of the Job Training Partnership Act authorizes funds for retraining displaced workers. This program is projected to serve about 260,000 workers during the 12-month period beginning July 1, 1989, with an average training period estimated at 26 weeks.

Finally, the private sector also plays an important role in assisting workers threatened with a job loss. Many employers attempt to reassign workers within the firm when jobs are eliminated by new technologies. In addition, several major union contracts now mandate retraining for workers displaced for this reason.

IMMIGRATION

When labor market mobility is insufficient to eliminate area- or industry-specific labor shortages, employers often turn to immigrants. Throughout U.S. history, economic growth and job opportunities have drawn millions of foreign-born persons to this country, both legally and illegally. Of course, factors influencing immigration include family ties and the freedoms offered by the United States. But whatever their motivation for coming to America, immigrants traditionally have adapted well to the U.S. labor market and have contributed significantly to long-run U.S. economic growth.

Between 1980 and 1988, legal immigration averaged 580,000 persons per year—about one-quarter of 1 percent of the U.S. population. This rate of immigration was above the pace of the 1970s, but well below the average immigration rate prior to 1921, when numerical restrictions on immigration were first introduced. Efforts to control illegal immigration, estimated by the U.S. Census Bureau to have added between 100,000 and 300,000 illegal aliens each year in the first half of the 1980s, led to the Immigration Reform and Control Act of 1986. This act restricted the employment opportunities of illegal aliens by imposing penalties on employers who hired them, but offered legal immigrant status to aliens who were in the United States before 1982.

Do immigrants take jobs that would otherwise go to U.S. workers and depress wages in particular areas and occupations? The many case studies of this question provide no conclusive answer, and disagreement over the existence and magnitude of any effects continues to be widespread. However, one recent study of 120 cities between 1970 and 1980 found that, on average, an increase in the number of immigrants equal to 1 percent of a city's population (more than four times the annual rate of immigration to the United States as a whole) had a negligible effect on the employment status of less-skilled native workers and reduced their wage rates only about 1 percent over that 10-year period.

Moreover, numerous studies suggest that the long-run benefits of immigration greatly exceed any short-run costs. The unskilled jobs taken by immigrants in years past have often complemented the skilled jobs typically filled by the native-born population, increasing employment and income for the population as a whole.

Currently, U.S. immigration policy is based primarily on the humanitarian principles of family reunification and refugee resettlement. Fewer than 10 percent of immigrants in recent years were admitted because of their skills. Less skilled immigrants will clearly continue to be a valuable resource for employers. Yet, with projections of a rising demand for skilled workers in coming years, the Nation can achieve even greater benefits from immigration by augmenting this traditional emphasis on family reunification with policies designed to increase the number of skilled immigrants. Immigrants with more education or training will likely make the greatest contributions to the U.S. economy, suggesting that basic skill levels could be one guide to admitting new immigrants under a skill-based criteria.

POLICIES TO ADDRESS SKILL SHORTAGES

Policies designed to increase the quality and extent of education among today's youth may be the most important investment society can make to promote greater labor market flexibility in the years ahead. Continuing efforts at all levels of government to remove barriers to geographic and occupational mobility also are warranted.

For many workers, the lack of affordable housing restricts mobility. Linking Federal housing subsidies to tenants and making the subsidy portable is one way to overcome housing affordability barriers to greater geographic mobility. Eliminating State and local laws—such as rent control and overly restrictive building codes and zoning regulations—that limit the availability of such units, and enactment of the Administration's proposal, Homeownership and Opportunity for People Everywhere (discussed below), could also increase labor flows to rapidly growing areas.

Similarly, efforts to revitalize economically depressed areas through removal of barriers to growth could transfer job opportunities to areas of high unemployment. The Administration's commitment to develop public/private partnerships through the creation of urban enterprise zones can encourage private investment and job creation in these areas.

Immigration policy can also contribute to the smooth operation of the U.S. labor market in the 1990s. While continuing the humanitarian principles that have shaped immigration policies in the past, the Federal Government can encourage the immigration of workers with skills important to the economy, both by increasing the number of visas for workers with a job in hand and by increasing quota levels for potential immigrants with higher levels of basic and specific skills. This approach will strengthen the prospects for successful assimilation of immigrants into U.S. society and increase the economic gains from immigration for the population as a whole.

Efforts to expand domestic sources of labor will also help prevent potential shortages. The increasing share of healthy active elderly persons in the population could be a particularly useful labor market resource. In the years ahead, it may be increasingly common for employers to provide incentives for older workers to postpone retirement, or to accept part-time work after retirement, giving firms continued access to the expertise of the Nation's most experienced workers.

IMPROVING THE OPPORTUNITIES OF LOW-INCOME HOUSEHOLDS

This Administration is committed to an antipoverty agenda calling on the Federal Government, in partnership with State and local governments, to:

- Maintain a strong economy to ensure economic opportunities for unemployed and underemployed Americans.
- Work with the private sector to provide the training, assistance, and incentives that will help those with the ability to support themselves to achieve independence and self-sufficiency.
- Supplement family resources when necessary to provide ongoing and adequate support for those in need and unable to work, particularly the elderly and severely disabled.

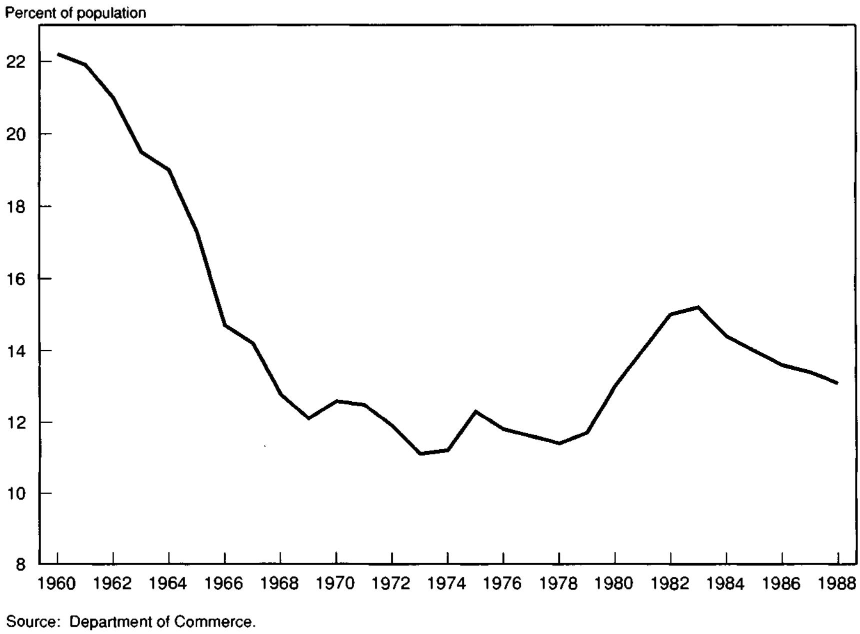
Integration of more low-income households into the economic mainstream will not only help these families gain economic independence, but will also increase the productive resources of the Nation and help maintain economic growth through the 1990s.

POVERTY IN THE UNITED STATES

The primary measure of economic need in the United States is the poverty rate, the percentage of individuals who live in families with income below the poverty line. (The poverty line, which varies with family size, is an approximate measure of the minimal amount of income necessary to purchase food, shelter, and other necessities.) As Chart 5–5 indicates, the poverty rate fell steadily through the 1960s, reaching a low of 11.1 percent in 1973, but rose again to a peak of 15.2 percent during the recession of the early 1980s. By 1988, the poverty rate was down to 13.1 percent, with 32 million individuals below the poverty line. While the poverty rate has fallen steadily for the past 5 years, too many families still confront daily problems of economic need.

Chart 5-5

POVERTY RATE. The poverty rate rose sharply in the early 1980s, but has since declined.



Source: Department of Commerce.

The aggregate poverty rate obscures significant differences among different types of households. The elderly have experienced the most dramatic decline in poverty rates; by 1988, the poverty rate among elderly persons was at an historic low of 12 percent. While poverty has fallen among the elderly, however, the poverty rate among children has risen, as Chart 5–6 shows. In 1988, one child in five lived in a family with income below the poverty line.

High poverty among children is closely related to the growth of female-headed households in the population, who have disproportionately high poverty rates. In 1988, more than one-half of all poor children lived in female-headed families. In addition, poverty rates are much higher among minorities than among whites, as Chart 5–7 indicates. While 10.1 percent of white individuals were poor in 1988, 31.6 percent of black individuals were poor, and 26.8 percent of Hispanic persons were poor. In female-headed black and Hispanic families with children, poverty rates approached 60 percent.

DISTINGUISHING AMONG THE POOR

Individuals who can work may lack training, available jobs, or access to adequate and affordable child care. In the long run, these individuals may be able to support their families, but need short-term assistance to reach self-sufficiency, such as temporary income support, child care, assistance in household management, job training, and assisted job search. Government programs to help these individuals must balance the need for adequate short-term assistance with the goal of long-term independence.

Not all poor people need this type of assistance. Some are temporarily poor, but have the resources to escape poverty quickly without any government assistance. The 6 percent of the poor who are full-time students are in this category. Other poor individuals cannot be expected to earn the income necessary for their support. This group includes both children and elderly persons, who together constitute almost one-half of the poor, and those with serious mental or physical disabilities. If these individuals do not have family support, society must provide the safety net of resources necessary for their support.

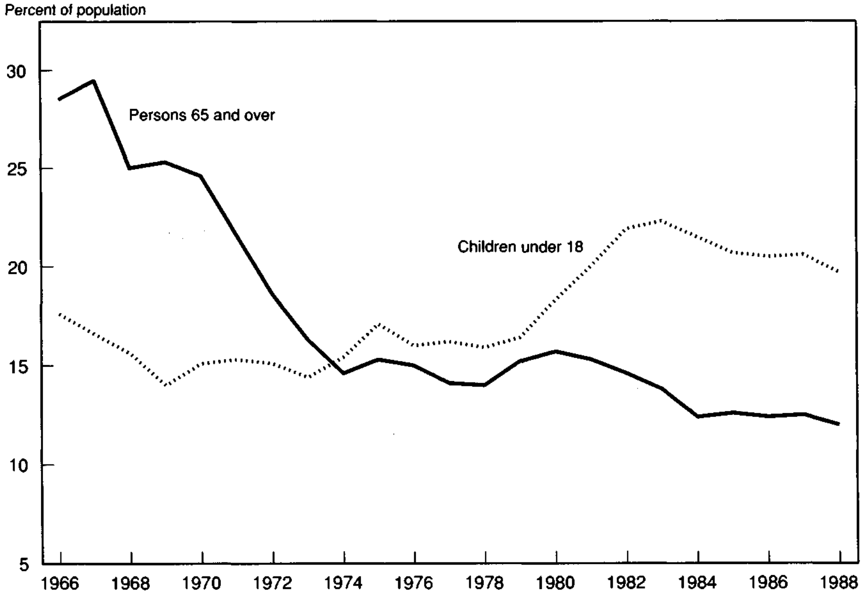
It is sometimes quite difficult to determine whether a particular individual can work. For instance, single mothers with very young children may be unable to work because of household demands rather than because of any inherent lack of earning ability. Arguments over the generosity and scope of public programs often revolve around these difficult judgments. The remainder of this section will focus on those low-income households who are generally considered able to benefit from employment-based strategies.

THE VALUE OF A HEALTHY ECONOMY

For the employable poor, the most important government responsibility is to maintain a stable and healthy economic environment that offers positive incentives and opportunities for all workers. The burden of unemployment is disproportionately borne by low-wage and less skilled workers. Indeed, the high poverty rates of the early 1980s reflected the high unemployment rates experienced at that time.

Chart 5-6

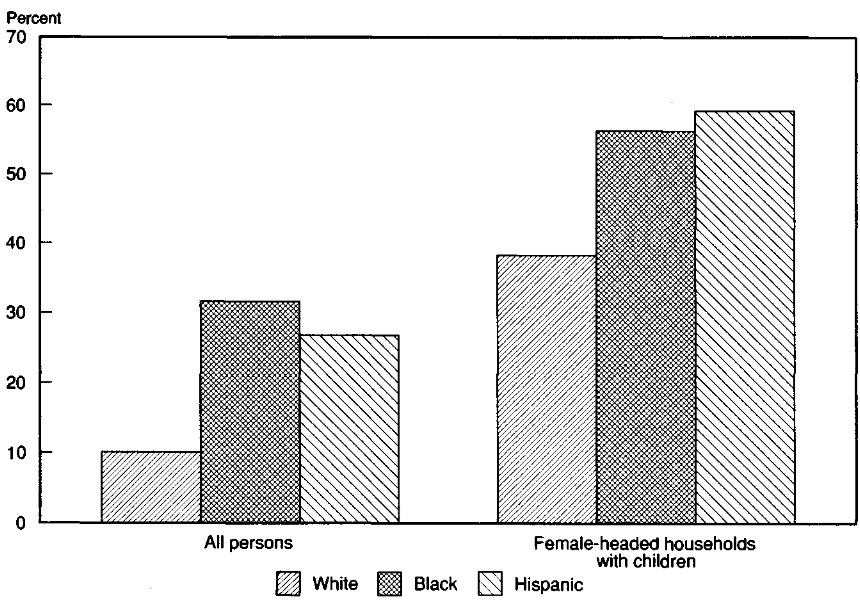
POVERTY RATES BY AGE. In the 1980s poverty rates of the elderly reached a record low, while children's rates remained high.



Source: Department of Commerce.

Chart 5-7

POVERTY RATES BY RACE, 1988. Poverty rates for blacks and Hispanics exceed those for whites, while rates for female-headed households are high regardless of race.



Source: Department of Commerce.

In contrast, when unemployment falls and the demand for workers increases, unemployed workers can find jobs and underemployed workers can increase work hours. Younger low-income households, particularly male-headed households, typically show strong income growth in an expanding economy, predominantly because of increased hours of work. The recent declines in poverty have occurred largely because of the sustained economic expansion.

TARGETED ANTIPOVERTY PROGRAMS

While a healthy economy is important in any government strategy to fight poverty, by itself it is not enough. Not all low-income households benefit from economic expansion. Elderly households, who are largely unable to expand their work hours, tend to show few gains. Female-headed households have not experienced substantial income gains during economic expansion. One reason why poverty rates have not fallen further during the economic expansion of the 1980s is the increase in female-headed families, whose incomes have been less responsive to economic growth. Thus, general policies that foster economic growth must be buttressed by strategies aimed at assisting particular groups.

Women and Children

Recent Federal initiatives, currently being implemented by this Administration, are designed primarily to provide new economic opportunities for poor women and their children. A disproportionately large share of poor families are headed by women—53 percent in 1988—and 90 percent of these families contain children under age 18. The steady increase in the share of poor families accounted for by female-headed families has been referred to as the feminization of poverty. Concern over this trend, coupled with concern over high children's poverty rates, has resulted in a new approach to assistance for this population.

The primary income assistance program designed to aid low-income single-parent families has long been aid to families with dependent children (AFDC), which provides income supplements to eligible low-income families with children. Responsibility for AFDC's funding and program structure is shared among the Federal and State governments. The median State in January 1989 paid AFDC benefits of $360 per month to a woman with two children (the average AFDC family) and no other income. When combined with food stamps worth $210 per month, this support provided the family with benefits equivalent to $570 per month, 73 percent of the 1988 poverty level. AFDC benefits are set by the States, however, so that a family receiving AFDC and food stamps will have benefits equivalent to less than 50 percent of the national poverty line in some States and close to 100 percent in others. Although income from AFDC plus food stamps is the base level of economic support available to a family, most poor families receive additional public assistance from other programs (such as fuel assistance) or they have other income sources, thereby raising their total resources relative to the poverty line. In addition, all AFDC recipients are eligible for health care assistance through medicaid.

AFDC was initiated in the 1930s to aid needy children without fathers. One of its primary purposes was to prevent widows from being forced into the labor market, allowing them to remain at home with their children. The changing nature of the program and the rising participation of women in the labor force, however, have resulted in significant recent changes in AFDC. Concern over long-term reliance on AFDC has led to an emerging consensus that AFDC participants need more than cash assistance; if they can work, they should also be expected to participate in education, training, and job placement programs to enable them to become economically self-sufficient. The "workfare" experiments run by a variety of States in the 1980s indicate that targeted work experience, job search, and job placement programs can be cost-effective techniques that assist AFDC recipients to work more and rely less on AFDC income. Furthermore, the individuals who benefit most from these programs are those women with little or no recent work history.

The success of these State experiments led to passage of the Family Support Act of 1988, which requires all States to establish a Job Opportunities and Basic Skills Training (JOBS) program for eligible AFDC recipients. The Administration is strongly committed to working with States to ensure that the JOBS program is effectively implemented to expand employment opportunities for poor women, as well as for the small number of two-parent families currently receiving AFDC. AFDC recipients who are able to work are expected to recognize their mutual obligation to their community: in exchange for AFDC support, they are required to participate in JOBS. States are given flexibility to design the education, job training, and employment programs most suitable for their population and economy. The JOBS programs must provide child care assistance as well as transitional child care assistance and medicaid coverage for up to 12 months after an individual leaves AFDC because of increased earnings.

The Administration is also committed to enforcing child support payments. Child support payments ensure that both parents share the economic burden of raising children. In 1987, only 44 percent of poor female-headed families with children had child support awards, and only 72 percent of these families (32 percent of all poor female-headed families) received child support payments, many of which were less than the award. In recent years, States and the Federal Government have sought to levy and enforce child support orders on absent fathers. The Family Support Act strengthened the ability of States to establish mandatory payment guidelines and to locate fathers and directly withhold their wages.

This policy alone will not have substantial effects on the poverty rate among women and children, both because absent fathers of many poor children are unemployed or employed at very low wages and because child support collected on behalf of AFDC families is primarily used to offset AFDC expenditures and thus does not produce much of an increase in overall family income. But, for women who increase their earnings and move off AFDC, child support payments can be an important additional source of income. Moreover, child support enforcement has the added social benefit of emphasizing that both parents have ongoing responsibility for their children.

The Working Poor

Providing incentives and opportunities for employment and better jobs among low-income families increases their economic independence, decreases government spending, and increases the productive work force of this country. About 48 percent of all poor families contain an employed worker, while 16 percent contain a full-time, year-round worker. Increased economic opportunities that allow these working poor families—especially those working full-time and year-round—to escape poverty will also provide incentives for other low-income persons to increase their employment.

For these reasons the Administration has proposed a new and refundable income tax credit, the child credit, for families with an employed parent and young children. This credit would increase income by lowering taxes among low-income families or by providing cash supplements to families with no tax liability. In addition, the Administration proposes making the existing dependent care tax credit refundable to increase its usefulness to poor families with child care expenses. This approach, rather than the alternative of subsidizing child care centers, allows families to choose the type of child care they need and involves less government regulation.

The Administration has also proposed a dramatic expansion in the Head Start program for preschoolers. This program significantly improves children's subsequent school performance and would also help low-income parents meet their child care needs. The 1991 budget requests a $500 million increase in budget authority for Head Start, a 36-percent increase over 1990 spending.

The President has signed an increase in the minimum wage to $4.25 per hour by 1991, and he sought and obtained a lower training wage for newly employed teenagers. This innovative provision will encourage employers to hire and train young workers and will offset the loss of employment opportunities that teenagers have historically experienced when the minimum wage is increased.

Providing incentives for labor market activity among low-income households is particularly important because it offers role models for children and teenagers in poor households. Teenagers and young adults in low-income families need to be convinced that those who play by the rules—finish high school, stay off drugs, do not get pregnant as a teenager, and find full-time work—can escape poverty and make a better life.

Lack of medical insurance can also cause problems for the working poor. Controlling for other differences, the uninsured are less healthy and receive less medical care than the insured; they also pay a higher share of medical expenses out-of-pocket. In 1987, 29 percent of all poor individuals were uninsured. In fact, the rate of uninsurance is higher among the working poor than among the nonworking poor because persons who receive AFDC (or supplemental security income, a program for poor elderly and disabled individuals) also have access to publicly provided insurance through medicaid. Many low-wage jobs, especially jobs in small businesses that cannot obtain low-cost group insurance coverage, do not offer health insurance.

Recent expansions in medicaid eligibility mandate that States must provide medicaid coverage to pregnant women and children under age 6 in families below 133 percent of the poverty line by April 1990. At their option, States may expand coverage to pregnant women and infants in families up to 185 percent of the poverty line. These medicaid expansions may be particularly useful in reducing infant mortality in low-income families.

Implementing the President's National Drug Control Strategy will help decrease the health problems experienced by drug abusers and their families. Medical care for women and children has become particularly costly in certain inner-city locations where cocaine addiction of mothers is linked to serious infant and maternal health problems. Although the number of poor mothers who are drug abusers is very small, the visibility and cost of the problems they create underscore the need to wage an effective war on drugs.

The Unemployed

The Administration's efforts to improve the quality of schools, its war on drugs, and its education and training programs for disadvantaged persons are all designed to bring more individuals into productive employment. After 7 years of economic growth, the share of the poor who are unemployed, or seeking more work than they can find, has fallen. But some individuals who may be able to work remain unemployed, often because they lack the necessary labor market experience, work skills, or training. This condition may be particularly costly to younger persons who have never held a steady job.

The Job Training and Partnership Act of 1982 established a structure of job training programs directed by private firms through local private industry councils. JTPA is projected to provide job training and placement services for 1.3 million economically disadvantaged individuals in the 12 months beginning July 1, 1989. Indeed, the expanded work programs for AFDC participants are expected to rely heavily upon local JTPA programs for job placement. The Administration's proposed amendments to JTPA (discussed above) include the creation of two special programs targeted on disadvantaged youth and adults. The Administration has also proposed a challenge grant program, Youth Opportunities Unlimited, for youth in high-poverty inner-city or rural areas.

The need to increase employment is particularly acute among minority populations in high-poverty urban areas, a group that is sometimes referred to as the underclass. Overall, unemployment rates among minority youth have fallen. In areas of concentrated poverty and deprivation, however, there is evidence of high rates of drug use, low educational achievement, high rates of teenage pregnancy, and alienation from legitimate employment.

No single policy can solve the multiple problems experienced by individuals in these areas; a multidimensional strategy is needed. Administration initiatives to improve inner-city public schools, combined with anti-drug efforts, job training, and job placement, should help some individuals. Targeted programs to geographically defined high-poverty areas, such as urban enterprise zones, may also help focus resources on concentrated poverty and its related effects on a community.

Several effective programs have brought young persons from highly disadvantaged backgrounds into the labor market. The Job Corps has 25 years of experience in providing such teenagers with education, job training, and placement. Research evaluations suggest that Job Corps participants are employed more, earn more, and are less likely to become involved in criminal activity than persons of similar background who were not in the Job Corps. Promising model programs include JOBSTART, which focuses on high school dropouts with low literacy skills, and STEP, which provides summer job training and educational services to teenagers.

Homelessness and Housing

This Administration has proposed expanded funding and new programs to address the problem of homelessness and housing affordability among low-income families. One of the more visible problems in urban areas in the 1980s has been homelessness. Not only is homelessness a social problem, but it is also a barrier to effective participation in the labor market. Reliable estimates of the homeless population are difficult to obtain, and few national estimates have been made. An extensive recent study estimated that 500,000 to 600,000 persons were homeless in the United States over a given week in 1987, while approximately double that number experienced homelessness at some point during that year. As the study acknowledges, however, no one knows exactly how many homeless people there are in the United States.

The homeless population is generally composed of at least three distinguishable groups. First, there are those who have a history of serious mental illness. Although estimates vary, most studies indicate that around one-third of the homeless population are mentally disabled. This group is often the most difficult to reach and the least likely to use temporary shelters and care facilities. Second, homeless families, primarily low-income women and children, constitute about one-quarter of the homeless, and tend to be actually on the streets for the shortest period of time before they enter the public assistance system. The remainder of the homeless are predominantly single men between the ages of 20 and 50. Many of these men work intermittently; some receive food stamps or small payments from State assistance programs; many have ongoing problems with alcohol or other drugs.

Changes in urban housing markets are often cited as an important cause of homelessness, along with the deinstitutionalization of the mentally disabled, drug abuse, spouse abuse, and other problems. Rising rents and land prices and the rejuvenation of downtown areas have displaced low-income populations. The availability of boarding houses and rooms for rent, typically used by poor single adults, has diminished in most cities. In some areas, rent control, restrictive building codes, and zoning regulations also may have decreased the stock of low-income housing.

The President has proposed programs that will provide housing assistance and supportive services to the most troubled homeless individuals as part of his HOPE initiative (discussed below). The Administration also supports full funding of the Stewart B. McKinney Homeless Assistance Act. Passed in 1987, the McKinney Act was the first legislation to authorize major direct Federal expenditures for emergency food, shelter, counseling, and other services for the homeless. For the past 3 fiscal years, the Congress has appropriated less money than it authorized, a situation the Administration seeks to rectify in its proposed 1991 budget.

Homelessness is a serious issue, but housing affordability is the dominant housing problem confronting most poor. It is estimated that more than 40 percent of the poor paid more than one-half of their income for housing in 1985. The Administration continues to emphasize housing vouchers or other tenant subsidies as the most efficient way to address low-income housing needs.

The Administration has also proposed a major new program, *Homeownership and Opportunity for People Everywhere* (HOPE) to expand housing opportunities for the poor. This proposed legislation includes tax incentives to encourage greater construction and rehabilitation of low-income housing and to encourage savings for downpayments; opportunities for residents of federally subsidized housing projects to have more voice over their housing, through tenant management and potential tenant-purchase plans; and 50 Housing Opportunity Zones that would establish Federal-local partnerships in metropolitan jurisdictions to remove barriers to affordable housing.

Disabled and Employable

The Administration supports a major new initiative to increase the economic opportunity for disabled persons. Surveys estimate that between 20 million and 50 million Americans are disabled. This large range reflects very different definitions of disability; while every study counts the 650,000 persons in wheelchairs, not all of them include the more than 24 million with hypertension. Of course, many disabled persons are fully employed, especially if a broad definition of disability is used. Many others are elderly, or do not seek employment. But because some disabilities limit the range of work options available and because some of the disabled have suffered discrimination in the workplace, disabled individuals suffer a disproportionate incidence of poverty. In 1988, 28 percent of poor household heads reported that they were not working because they were ill or disabled. Conversely, among those household heads who report that they do not work because they are ill or disabled, fully 42 percent are poor.

The primary program explicitly designed to assist disabled low-income households is supplemental security income, a Federal program available to individuals with low incomes who are certified as unable to work. In addition, those whose disability occurred on the job are typically able to receive workers' compensation, while those who have worked in the past are often eligible for social security disability payments. Several Federal programs also provide funds for work rehabilitation for the disabled.

The Administration supports the Americans with Disabilities Act (ADA), designed to lower barriers to employment, public services, and public facilities for the disabled population. Inaccessible workplaces and discrimination against disabled individuals have prevented many disabled persons who are able and willing to work from realizing their full economic potential. Major progress occurred with the passage of the Rehabilitation Act of 1973, which required institutions receiving Federal funding to make their facilities and services accessible to disabled individuals. Survey results still indicate that several million disabled individuals who want to work are unable to find employment, however, and the ADA is designed to open new employment opportunities for these persons.

FUTURE DIRECTIONS

Experience has shown that designing policies to alleviate poverty is a difficult task. Among the issues that will continue to be debated in the years ahead are the following:

How can low-income households be integrated into the economic mainstream? A delicate balance must be maintained between providing adequate short-term assistance and preventing long-term dependence. Government programs should move people toward employment and self-sufficiency. A growing job base and a healthy economy are crucial ingredients of this strategy.

How can social policy goals be balanced against budget realities? In a period of budget stringency, program expenditures must be effectively targeted to those who will benefit the most from them.

One of the major challenges of the 1990s will be to develop effective antipoverty programs that further reduce economic need in this country by increasing the opportunities for productive employment among those who are currently poor.

MAINTAINING LOW UNEMPLOYMENT AND LOW INFLATION

The civilian unemployment rate in 1989 averaged 5.3 percent, its lowest level since 1973. And the percentage of the civilian population employed reached 63.0 percent, its highest level ever. Recent concerns about labor shortages, however, have led some to ask whether further efforts to reduce unemployment might lead to a significant pickup in wage and price inflation. So far in the current expansion, inflation has remained relatively moderate. The GNP fixed-weight price index, the broadest economy-wide measure of inflation, rose 4.1 percent in 1989, well below its 9.8-percent rate in 1980 and down from 4.5 percent in 1988.

Underlying the concern that unemployment and inflation are linked is the widely accepted view that, when inflationary expectations are stable, the economy has a minimal rate of unemployment consistent with nonaccelerating inflation. The nonaccelerating inflation rate of unemployment, often referred to as the NAIRU or natural rate of unemployment, is an important guide for policymakers. It reflects unemployment associated with job changes (frictional unemployment) and with the mismatches between workers and jobs that occur in a changing economy (structural unemployment). Moreover, when the unemployment rate falls below the NAIRU, labor markets tighten, and employers face greater pressures to raise wages in order to maintain a qualified work force

(Box 5-3). Some have argued that at current levels of joblessness, further large increases in output could drive the unemployment rate below the NAIRU, thus triggering accelerating wage increases that, in turn, would threaten the progress in reducing price inflation made in the 1980s. Although some concern is justified, the evidence suggests that the United States can achieve sustained growth without accelerating inflation. The Administration projections in Chapter 2, for instance, show 3.0-percent average growth through 1995 and a modest decline in inflation.

THE SECULAR DECLINE IN UNEMPLOYMENT IN THE 1980s

Because alternative policies to reduce unemployment may have sharply different implications for the behavior of inflation, it is important to distinguish among the different causes of unemployment.

Demand-related, or cyclical, unemployment, by far the most visible cause of variation in joblessness, refers to unemployment that occurs when the overall demand for workers falls. The sharp increases in the unemployment rate that occur during recessions clearly represent cyclical unemployment. Much of the decline in joblessness in the 1980s reflected the strong recovery from the 1982 recession and the long expansion that followed.

Frictional unemployment refers to the transitional unemployment that occurs when workers enter the labor market or change jobs. Structural unemployment is joblessness associated with a general lack of skills or with labor market mismatches between workers and jobs. The decline in unemployment over the past decade also reflects a drop in frictional and structural unemployment, breaking an upward trend evident since 1969.

In particular, although unemployment rates were successively higher at each business cycle peak in 1973, 1979, and 1981, the unemployment rate in 1989 stood 2 percentage points *below* its 1981 level (Chart 5-8). Moreover, the decline in the unemployment rate in the current expansion has *not* led to a significant acceleration in wage inflation. These two facts together suggest that frictional and structural unemployment, and hence the unemployment rate consistent with stable inflation, fell during the 1980s.

THE EFFECTS OF DEMOGRAPHIC AND LABOR FORCE TRENDS

To a significant extent, the decline in the NAIRU in the 1980s reflected changes in the composition of the labor force, especially the aging of the baby-boom generation. As shown in Chart 5-9, unemployment rates are higher for young workers (aged 16 to 24) than for adults, reflecting both the relative inexperience of new

Box 5-3.—The Determinants of Nominal Wage Growth

Although the process of wage-setting is often quite complex, key determinants of nominal wage growth are current labor market conditions, past and projected rates of inflation, and labor productivity growth. Employer costs for fringe benefits are often influenced by events outside the labor market—such as the acceleration in health care inflation in the past few years. Because employers are ultimately concerned with total labor costs, however, the key determinants of wage growth also determine growth in total labor compensation beyond the short run.

The availability of labor influences both employers' willingness to pay higher wages and workers' efforts to seek larger pay increases. Relatively low unemployment rates increase upward pressure on wages as firms raise pay to attract new workers and retain their current employees. Similarly, high unemployment rates tend to hold down wage increases.

Recent rates of wage and price inflation and expectations about future inflation also affect wages. If wages are expected to be higher in other parts of the economy, because of recent wage increases at other firms or expectations of future wage increases, then workers and employers will probably settle on a higher wage. Past rates of price inflation may influence wages if workers and employers agree to "catch-up" adjustments to preserve real wage levels, while employees who expect high inflation will demand larger wage increases to maintain their future standards of living. Moreover, employers will be more willing to grant wage increases if they expect to be able to raise prices to offset their higher labor costs.

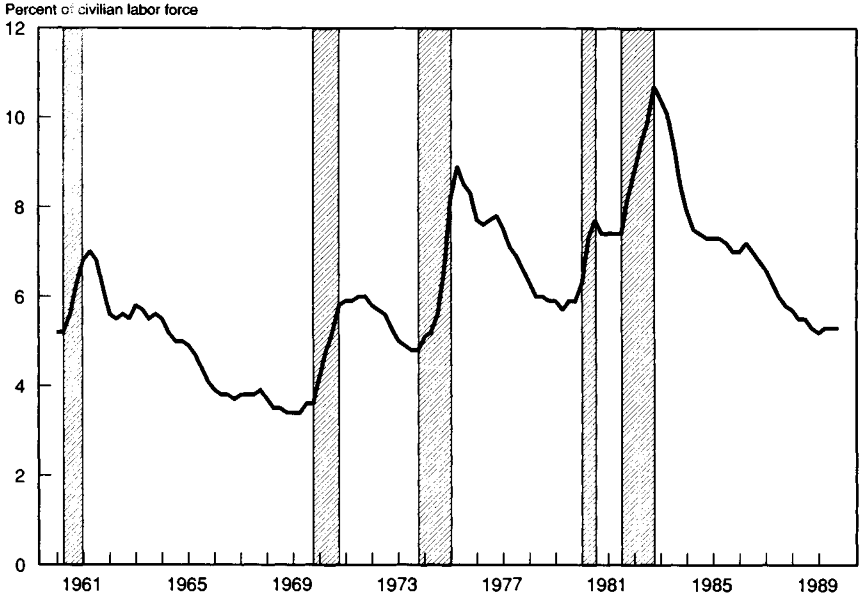
Over time, real wage increases have roughly matched the long-run rate of productivity growth in the economy. Pay hikes associated with productivity gains do not increase the relative cost of labor to an employer, and so do not contribute to an acceleration of price inflation. In this sense, productivity gains are important to workers; wage increases that are not matched by higher prices generate an improvement in living standards.

labor market entrants and higher rates of job turnover as young workers move in and out of various jobs during their search for a career.

The relative importance of young workers increased in the 1960s and 1970s, and this shift toward groups with relatively high rates of unemployment caused the overall unemployment rate to rise. In addition, overcrowding in lower skilled labor markets associated

Chart 5-8

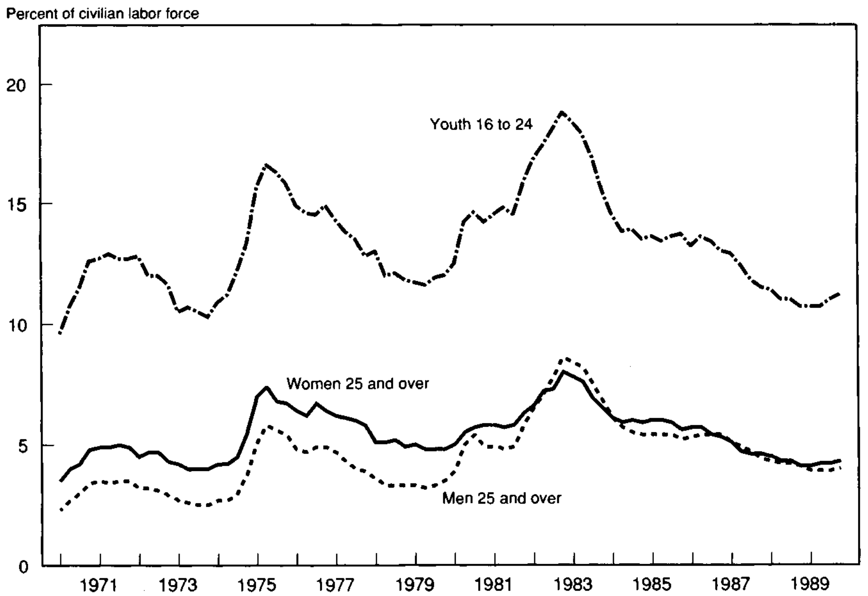
CIVILIAN UNEMPLOYMENT RATE. The unemployment rate has declined significantly during the current expansion.



Note: Shaded areas represent recessions; data are quarterly.
Source: Department of Labor.

Chart 5-9

UNEMPLOYMENT RATES BY AGE AND SEX. Youth unemployment rates are higher than rates for adults. Rates for adult men and women converged in the 1980s.



Note: Data are quarterly.
Source: Department of Labor.

with the baby-boom cohort exacerbated the unemployment problems for this group. The differential between youth and adult unemployment rates widened in the 1960s and 1970s. It is estimated that the higher percentage of young people in the labor force and their rising relative unemployment rates added close to 1.5 percentage points to the NAIRU between the 1950s and late 1970s.

As the baby boomers moved into age groups with lower average frictional and structural unemployment rates in the 1980s and were followed by the smaller baby-bust cohort, these trends reversed, contributing about 0.5 percentage point to the decline in the NAIRU in the 1980s. The unemployment rate for youth also fell as smaller cohorts led to decreased crowding in the youth labor market, probably reducing the NAIRU another 0.3 percentage point over the past decade. These favorable demographic trends should continue well into the 1990s.

Labor force participation among adult women rose steadily in the 1960s and 1970s, and higher unemployment rates for that group also boosted the aggregate unemployment rate over that period. Women's labor market participation continued to increase in the 1980s, but their unemployment rate fell to about the same rate as for adult men. This decline in joblessness among women, coupled with women's rising participation, has also contributed to the decline in the NAIRU in recent years.

LABOR MARKET MISMATCHES AND STRUCTURAL UNEMPLOYMENT

A reallocation of workers across sectors in response to changing supply and demand influences the amount of structural unemployment associated with mismatches between workers and jobs. Recent changes in structural unemployment can be seen across a variety of occupational, industry, or geographic markets. Some insight into these changes can be obtained by focusing on a key feature of the mismatch problem—the coexistence of job vacancies and unemployment.

For the most part, vacancies and unemployment move in opposite directions, with faster economic growth leading to falling unemployment and rising vacancies, while rising unemployment is associated with declining job vacancies. That pattern is consistent with the view that much of the unemployment variability in the United States over time represents changes in cyclical unemployment. Vacancies and unemployment sometimes move in the same direction, however, reflecting a change in structural unemployment arising from localized, industry-specific, or occupation-specific supply and demand mismatches.

The Conference Board's index of help-wanted advertising normalized by the level of payroll employment provides a very rough proxy for a job vacancy rate and illustrates the relationship between unemployment and job vacancies. Over shorter periods, comparisons show opposite movements in the unemployment and vacancy rates, reflecting the effects of economic recessions and expansions. A gradual upward trend in both the unemployment and the vacancy rate is evident throughout much of the postwar period, however, suggesting that structural imbalances in the labor market worsened through the 1970s. In 1989, the unemployment rate and the vacancy rate were both below their levels in 1979, indicating that these imbalances lessened in the 1980s. A continuation of this trend would reduce the unemployment rate consistent with stable inflation further in the 1990s.

Measures of the dispersion of unemployment across different labor markets can also be useful in assessing the efficiency of labor market adjustment. Uneven growth across markets will initially generate uneven patterns of unemployment and employment changes. Over time, however, efficient labor markets will tend to reduce those initial imbalances, as workers in labor surplus areas—geographic, industrial, or occupational—move to areas with better job prospects.

Across geographic markets, the evidence suggests that labor market imbalances worsened in the 1980s; after holding fairly steady during the 1970s, unemployment dispersion among States increased sharply through most of the 1980s. This rise in geographic dispersion reflected, at least in part, industry imbalances coupled with the industrial composition of particular regions. International competition and the decline in oil prices led to layoffs in the Midwest and Southwest, while strong growth in services and light manufacturing fueled employment gains in the coastal regions. It is difficult to judge whether the widening in unemployment dispersion represents unusually large sector-specific economic shocks or declining labor market mobility. As noted earlier, the geographic dispersion in jobless rates declined significantly over 1989 as the labor market began to adjust to those earlier shocks.

The existence of structural labor market imbalances clearly underscores the importance of labor mobility in reducing structural and frictional unemployment, and hence the unemployment rate consistent with stable inflation. Policies to improve the mobility of the work force and to improve the efficiency with which workers and employers find job matches could generate further declines in structural unemployment without building up inflationary pressures.

OTHER CHANGES IN LABOR MARKETS

Some researchers argue that significant changes in the U.S. economy also may have unexpectedly tempered wage inflation in the 1980s. Most prominently discussed is the increased exposure of U.S. producers to international competition. As the foreign exchange value of the dollar rose in the early 1980s, employment in a number of core manufacturing sectors suffered, resulting in unusually large layoffs that extended to workers with more seniority. This increased openness to international competition may have had an important impact on the perceived unemployment risks associated with aggressive wage demands, so that job security gained prominence over wage gains in the priorities of many workers, reducing the inflationary pressures associated with any given level of the unemployment rate. Some evidence suggests that such considerations were important in selected industries particularly vulnerable to foreign competition. Because these industries constitute a small part of the overall U.S. economy, however, international competition thus far appears to have had only a small effect on economy-wide wage behavior.

A second oft-cited, and related, argument is that the declining importance of organized labor in the U.S. work force reduced the contribution of noncompetitive union wage premiums to aggregate wage inflation in the 1980s. The proportion of the private work force that is unionized fell sharply in the 1980s, from more than 20 percent in 1979 to around 14 percent in 1988. Fewer workers receiving union wage premiums would reduce average wage growth, all else equal. In addition, proponents of this line of reasoning argue that the focus on job security in the 1980s was especially important in the union sector, where management became more aggressive in negotiating with workers in response to international and nonunion competition. Data from the employment cost index indicate that union wages have risen less rapidly than nonunion wages since 1983, after rising more rapidly throughout the late 1970s and early 1980s. But that shift may partly reflect the typical cyclical behavior of the union-nonunion wage differential. Moreover, several studies suggest that, although the declining strength of unions may have slowed wage inflation in the union sector, it has had only a small effect on aggregate wage inflation.

Finally, some analysts point to greater flexibility in both pay schedules and employer-employee relationships as evidence that wage determination in today's economy differs fundamentally from that in past years. Many union contracts now use lump-sum bonuses as a means of avoiding base wage increases during periods of uncertain demand. Moreover, profit-sharing and employee stock ownership plans have become more prevalent in recent years, tying workers' pay at some firms more explicitly to overall company performance. In addition, a greater use of part-time and temporary workers by firms has increased the ability to adjust employment levels promptly during periods of slack demand by lowering the costs typically associated with work force changes.

In general, it is difficult to assess the importance of any one of these factors in changing the fundamental nature of wage determination in the 1980s or to forecast whether such trends will continue. Taken together, the patterns over the past decade may have led to some small downward shift in wage inflation. It seems imprudent, however, to rely heavily on the continuation of these favorable factors in forming policies for the 1990s.

LOOKING AHEAD

The design of sound economic policies depends on the level of the NAIRU. That level provides a gauge of how far the actual unemployment rate can be expected to decline without a significant buildup of inflationary pressures, and thus represents one goal of an expansionary macroeconomic policy. Conversely, it is also an approximate measure of the extent of frictional and structural unemployment in the U.S. economy; reducing the unemployment rate consistent with stable inflation thus is an important goal of labor market policies.

Unfortunately, the NAIRU is not observable, and it is more difficult to estimate its level than its change. But a rough estimate of the current level can be inferred from recent trends in the unemployment rate and in wage inflation. Both wage inflation and unemployment have shown little movement over the past year. Moreover, the Michigan Surveys of Consumer Attitudes estimate that expectations of price inflation have stabilized at around 4.5 percent. These patterns are consistent with a pace of wage growth that roughly balances the demand for labor with the available supply, suggesting that the remaining unemployment is primarily frictional and structural in nature. *Thus, the average rate of unemployment in 1989—5.3 percent—may not be far above the nonaccelerating inflation rate of unemployment.*

In this setting, the most appropriate policy approach is to focus on reducing the NAIRU further in the years ahead. Maintaining steady economic growth and low unemployment is an important component of that policy, because additional job growth will create opportunities for many structurally unemployed and disadvantaged persons as employers lower expectations about qualifications and increase the intensity of training. Similarly, the decreasing number of new labor market entrants will give firms strong incentives to provide additional training for the existing work force and will reduce the number of labor market participants who experience frictional unemployment. Increasing workers' investments in education and training and reducing the barriers to labor mobility will also reduce the NAIRU. The prospects are good for maintaining low unemployment rates, on average, in the future. But, macroeconomic policies must be designed so that reductions in unemployment do not reignite rising inflation, which would increase the risk of a subsequent economic downturn.

SUMMARY

The U.S. labor market is remarkably efficient in adapting to economic change. Adjustments are not instantaneous, however, and public and private initiatives can help to speed the natural workings of the market. As the United States enters the 1990s, attention focuses on increasing the skills and flexibility of the work force to meet changing economic demands. The Administration is committed to achieving excellence in education at all levels. It is particularly important to improve dramatically the achievement of elementary and secondary students, which means improving the quality of the Nation's schooling system. Increasing the numbers of students receiving education beyond high school may also be important in meeting the job demands of the 1990s.

Within the existing work force, employers and workers must adapt quickly to changes in the supply of and demand for labor. For the most part, these adjustments are likely to occur automatically without government action. In some cases, however, strengthening training programs can facilitate the reemployment of workers whose skills have been rendered obsolete by economic change. In other cases, barriers to mobility can be reduced through policies that increase the affordability of housing or encourage the startup of business in economically depressed areas.

With population growth projected to slow over the next decade, additional sources of labor will be needed. Tapping these sources can be facilitated by immigration reform and by encouraging businesses to hire and train currently underutilized segments of the population such as the elderly, disabled, and the unemployed or underemployed poor.

Indeed, for the Nation to realize its full potential for economic growth in the years ahead, society must bring the poor and disadvantaged more fully into the mainstream of the economy. Policies that assist the poor will certainly be needed, but these policies must be linked with the goal of eventual self-sufficiency by ensuring education, training, and job opportunities for low-income households.

The challenges for the 1990s are large, but the current economic environment is favorable for achieving further progress toward these important goals. Unemployment is low and inflation remains in check. Economic opportunities are plentiful. If the Nation can more fully utilize its human resources in the decade ahead, the result will be rising productivity, stronger economic growth, increased opportunities, and rising living standards for Americans.