

Chicago Fed Letter

Work force issues

The application of labor in production continues to be the most fundamental relationship in every economy, including that of the Midwest. As part of its project to assess the Midwest's economic turnaround, the Federal Reserve Bank of Chicago recently conducted a symposium on regional work force developments and related policy issues. This *Chicago Fed Letter* presents the findings from that symposium and highlights several unresolved yet critical issues.¹

In the context of Midwest growth and development, public and private decisionmakers need to address three areas of the work force process that are now undergoing significant, perhaps profound, changes. In addition, recent changes in federal labor policy provide new opportunities for the states. The trend of transferring responsibility for labor and training programs to the states, coupled with the specific training needs associated with the new welfare reform measures, will increase the importance of state-level work force development.

Changing skill needs

First, the U.S. and Midwest economies are becoming increasingly centered on the flow of information and knowledge creation. Workers who are able to perform in this new environment are being rewarded in the marketplace, and a deficit or surplus of high-performing workers in the Midwest will determine the region's growth and welfare.

By historical standards, the portion of the work force having *low skills* has declined. Nonetheless, rising skill levels have been insufficient to keep up with the pace of rising skill demands. Surveys of new jobs being created by business suggest that new skill demands are higher than those of previous and existing jobs. An

extensive survey of firms located in four major metropolitan areas (Atlanta, Detroit, Los Angeles, and Boston) reported that skill needs for new jobs have risen, even in the relatively short time frame of the last five to ten years. Even in the blue-collar/service category, which is often perceived as requiring the fewest skills, 32% of surveyed firms indicated that skill needs had increased. Figure 1 illustrates the daily tasks and the credentials employers are demanding of new hires for various

not currently geared to meet the below-college skill needs of employers. For this reason, both public and private efforts are being initiated or stepped up. In the Midwest, Wisconsin and Illinois are embracing *school-to-work* programs, which attempt to keep up with changing business skill demands by directly linking school curricula with either business guidance or actual work-site learning. In Iowa, public vocational schools may provide a customized curriculum or training

1. Skills and credentials required for new jobs				
	All jobs	College required	No college required	
			White-collar	Blue-collar/service
-----fraction requiring task or credentials-----				
Daily task performance				
Customer contact	.73	.82	.82	.51
Reading or writing paragraphs	.68	.91	.67	.51
Arithmetic	.68	.77	.70	.56
Computer	.56	.74	.70	.20
Required credentials				
High school diploma	.78	1.00	.82	.54
GED accepted	--	--	.66	.44
GED not accepted	--	--	.16	.10
General work experience	.70	.75	.72	.62
Specific work experience	.64	.74	.64	.56
Previous training or certification	.43	.56	.39	.37
<small>Note: All results are sample weighted. A dash indicates information not available. Source: Harry Holzer, "Employer skill needs and hiring procedures," presentation prepared for the workshop "Work Force Developments: Issues for the Midwest Economy," held at the Federal Reserve Bank of Chicago, May 15, 1996.</small>				

job categories. The particular skills that relate to the new *knowledge worker* include both technical skills, related to computers and automated machinery, and interpersonal skills, such as the ability to communicate effectively and to work as part of a team.

New skill demands being made on the work force have resulted in several identifiable challenges. For the most part, the educational infrastructure is

program to meet the needs of a particular industry or large individual company.

The highly visible rise of in-house training programs and *corporate universities*, such as those of McDonald's and Motorola, further demonstrates the need for enhanced skills among the adult work force, as well as the efficacy of work-based or business-guided training and learning. In particular,

business training efforts that stress contextual learning, often incorporating training into the daily work life of employees, are highly effective. Nonetheless, because the economic returns to basic skills accrue to workers rather than to firms (or at least such returns are perceived to accrue to workers), there may be a lack of resolve among the private sector to shore up the basic skills gap of the adult work force.

Disadvantaged workers

A second work force issue relates to the persistent problem of bringing disadvantaged workers into the work force and the emerging problem of falling incomes for less-skilled members of the work force. Recently enacted federal welfare reform, which limits the time individuals can stay on welfare, makes it all the more important to develop strategies to bring the unemployed into the work force and keep them there. In 1995, unemployment among high school dropouts ran at 13%, while unemployment for college graduates was 2.6%. Midwestern and national values prescribe that greater work force participation among low-income and disadvantaged people can increase levels of economic well-being, improve self-esteem, and lessen social ills. With roughly two-thirds of all poor families having one or more members in the work force, work-oriented values do not appear to differ across social strata. A large part of the problem relates to the more rapid rise in the demand for those jobs requiring greater skills. Adults lacking labor force experience may not have and may not easily acquire the fundamental skills needed to find and keep a job when the opportunity arises. At the same time, motivation for training and education can become dampened and poverty-related social problems can arise which, in turn, become further obstacles to permanent labor force participation. Both newly fashioned government policies and innovative prototype work-force programs for the disadvantaged appear to be recognizing this vicious cycle of poverty and work force participation. In the past, the

most widely used program structure for bringing the disadvantaged into the work force emphasized a strong dose of training, followed by introduction of the client to a (permanent) job setting. In contrast, new and somewhat-more-successful programs try to move prospective workers quickly into job situations, with only basic coaching on interview and day-to-day job behaviors. However, once employed, the client may be offered a range of support services on an ongoing basis, for example, child care, family or substance abuse counseling, repeated job placement assistance, and more extensive training. More general public policies, such as Wisconsin's welfare-to-work initiatives, are now fashioning approaches which are similar in spirit and content. The twin tenets of such programs are that 1) a quick introduction to the work force for many disadvantaged people can help them gain elementary job skills and 2) supplemental family support services may be more helpful than formal and structured up-front training.

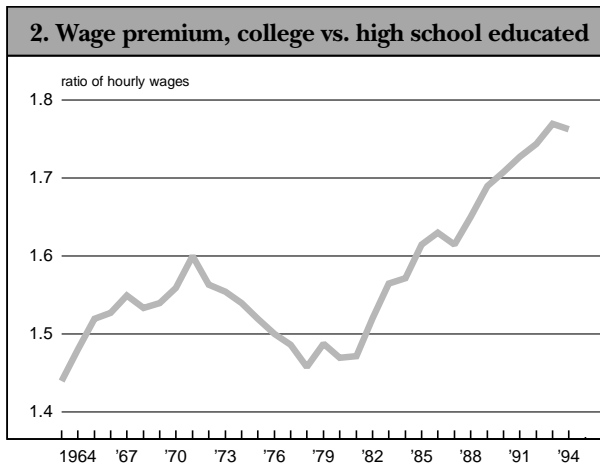
Pending legislation before the U.S. Congress proposes folding numerous federally assisted job training programs into block grants, whereby states would have greater freedom to match their ideas and needs with federal dollars. Philosophically and practically, this approach meshes with emerging state welfare-to-work initiatives that eschew up-front training in favor of immediate placement of workers and provision of support services. However, some observers question whether the new-found freedoms associated with pending federal and fledgling state initiatives will effectively serve the disadvantaged population. Concerns center on whether sufficient funding will be available to provide the follow-up training and other services that are needed to support initial labor market experience. There is also some concern as to whether, once freed from federal program restrictions, states might choose to steer monies away from disadvantaged sectors of the population. In recent years, wages have fallen among the less-skilled segments of the work force, while rising for those workers with better education and skills. Consequently, as figure 2 illustrates, the wage gap has widened between those with high-level educational credentials and those without such credentials. Whether this

wage gap is a problem or an opportunity remains open to debate. Some observers believe that, in addition to being an affront to notions of fairness, widening income disparities may adversely affect societal stability, to say nothing of the potential waste of human talent. At first blush, concentrating public training subsidies on those with low skills would seem to be the most efficacious means to close the gap between the haves and the have nots, especially since low-skilled individuals may face high barriers in financing their own education and training.

Some argue that, due to the increasing returns to skills, knowledge, and education, a widening income gap represents a broad societal opportunity that should be exploited in the most cost-effective manner. Individuals and society should take advantage of the higher returns to skills by investing more in education and training. Accordingly, this human capital investment need not necessarily focus on the less-skilled portion of the work force; it should be directed toward those segments yielding the greater returns—whether it be low-, medium-, or higher-skilled workers. Such policies may also be the most cost-effective way of narrowing the wage gap. Increasing the supply of highly skilled workers, while tightening the supply of less-skilled workers, will tend to allow market forces to push up wages from the bottom and pull down wages from the top. At the same time, policy interventions to remove barriers to education among the disadvantaged, such as school reform in the inner cities, should not be ignored.

A contingent work force

The third major change in today's work force is having a more pervasive impact on workers and firms, that is the increasingly transitory and fluid nature of the employer-employee relationship. In the U.S. and other industrialized nations, firms are increasingly acquiring their labor through contingent, contractual, or temporary arrangements rather than hiring permanent employees. The fastest growth has been in the business services sector, perhaps reflecting more outsourcing arrangements being made by such firms. In industries



Source: Kevin Murphy, "Wage and income disparity trends," presentation prepared for the workshop "Work Force Developments," Chicago, IL, May 15, 1996.

such as business services, the nature of the work itself has perhaps become more fluid, as have its skill requirements. Thus, firms may be motivated to acquire laborers with a varying range of skills, who can be switched from one area to another as the firm's needs change.

Alternatively, the trend toward contingent arrangements may be driven by firms' desire to gain better information about employees they will ultimately hire from the pool of contingent workers. Firms may also be motivated to use contingent workers in this way by more protective labor laws and regulations which can, in some cases, penalize firms for severing a regular employee in the event of substandard performance or a firm's changing labor needs.

From the employee's perspective, these changes have lessened expectations that a given job will remain available throughout much or all of one's working lifetime. Aside from any preference among employers for more contingent relationships, an increasingly competitive environment for many firms may make the loss of some permanent jobs inevitable.

The implications of the more transitory nature of work assignments are broad-based for both the public and private sectors. First, labor provisions and programs should adapt to the increased mobility that is being required of workers. Health care should be portable, so that workers are not discouraged from seeking

better opportunities out of concern that they will lose their health care coverage.² Similarly, pension contributions should be portable; the idea of offering generous pensions in return for longevity and loyalty has likely outlived its usefulness. Perhaps for this reason, private pension plans are shifting from defined benefits to defined contributions.

Changing work assignments also imply that employees will demand

that job offers are accompanied by opportunities to acquire salable skills. Presumably, firms that provide low-cost and salable training in conjunction with employment will be able to attract higher quality workers at lower cost. In order to be salable, these skills must be transparent, transferable, and certifiable to future employers. A prototype skills-and-credentials program is being developed by the Great Lakes Governors and the National Tooling and Machining Association for workers in the metalworking industry.

Finally, contingency and turnover in labor markets suggest that there are greater benefits to fashioning more efficient labor markets than ever before. Concurrent matching of employment opportunities with workers is being facilitated by advances in information technology and by innovative prototype programs such as *one-stop* centers, offering a broad range of employment and training assistance. Thirty-three states, including most midwestern states, have adopted one-stop facilities for employment services such as job postings and training opportunities. In the area of advanced technology, statewide programs include the America's Labor Market Information System talent bank project—a U.S. Department of Labor effort to make use of advances in computer-interactive technology to create a nationwide electronic resume system. Michigan and Missouri are joint leaders of a state consortium that is working to develop the system.

Conclusion

How well the Midwest has responded to these three broad work force changes and how well the region will adapt in the future cannot yet be determined. However, it is clear that the region's private and public sector work force policies are responding to the changing work force with great energy.

—Richard Mattoon
Senior economist
William A. Testa
Assistant vice president

¹For a complete summary of all the presentations at the symposium, see "Work Force Developments: Issues for the Midwest Economy," summary of the fourth Assessing the Midwest Economy workshop, Federal Reserve Bank of Chicago, May 15, 1996. (Copies are available from the Federal Reserve Bank of Chicago's Public Information Office.)

²The recently signed Health Insurance Portability and Accountability Act allows workers who change jobs to retain individual insurance coverage in their former employers' group medical plans. For more on this, see Stewart Ugelow's article in *The Wall Street Journal*, p. 1, August 22, 1996.

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Tracking Midwest manufacturing activity

Manufacturing output indexes (1987=100)

	Aug.	Month ago	Year ago
CFMMI	129.4	129.0	126.6
IP	129.1	128.8	124.2

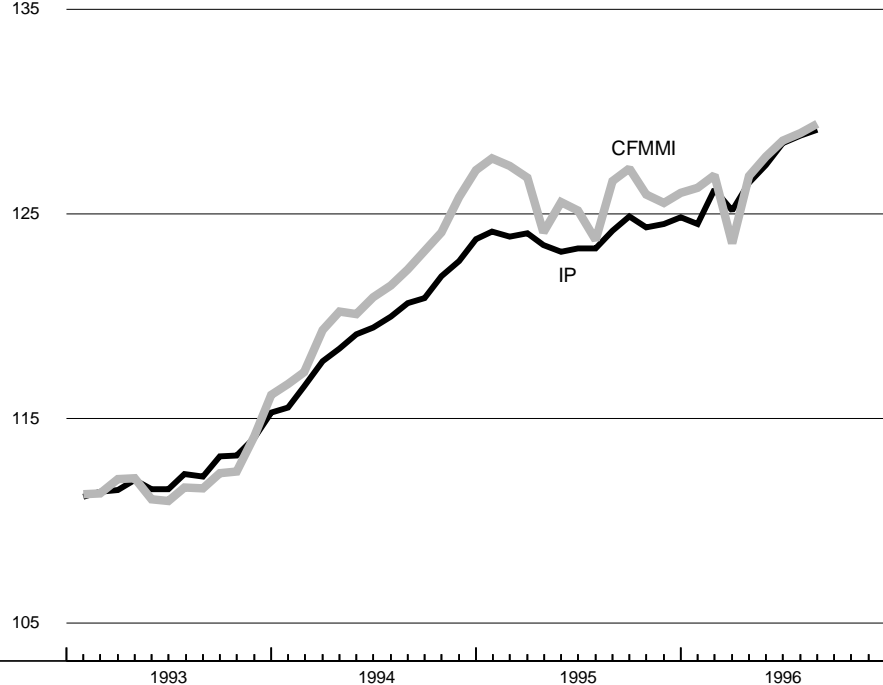
Motor vehicle production (millions, seasonally adj. annual rate)

	Sept.	Month ago	Year ago
Cars	6.5	6.7	6.3
Light trucks	5.4	5.6	5.2

Purchasing managers' surveys: net % reporting production growth

	Sept.	Month ago	Year ago
MW	62.5	63.6	53.2
U.S.	54.1	57.1	50.6

Manufacturing output indexes, 1987=100



Manufacturing activity in the Midwest, measured by the Chicago Fed MMI, rose 0.4% in August from the previous month, roughly in line with the nation. The steel and machinery sectors reversed July declines and the auto sector posted another solid gain. Despite an improvement, steel activity continued to be constrained by the disruptive effects of steel mill outages. The resource sector, primarily nondurable goods, declined in August, but has been relatively volatile for much of this year.

With the purchasing managers' surveys around the Midwest signaling continued expansion in September, prospects are favorable for continued gains in the CFMMI. However, light vehicle assemblies were down slightly in September from a month ago. Moreover, the Canadian Auto Workers' strike is expected to be a drag on regional production activity in the fourth quarter.

Sources: The Chicago Fed Midwest Manufacturing Index (CFMMI) is a composite index of 16 industries, based on monthly hours worked and kilowatt hours. IP represents the Federal Reserve Board's industrial production index for the U.S. manufacturing sector. Autos and light trucks are measured in annualized units, using seasonal adjustments developed by the Board. The purchasing managers' survey data for the Midwest are weighted averages of the seasonally adjusted production components from the Chicago, Detroit, and Milwaukee Purchasing Managers' Association surveys, with assistance from Bishop Associates, Comerica, and the University of Wisconsin-Milwaukee.

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Public Information Center
P.O. Box 834
Chicago, Illinois 60690-0834
(312) 322-5111

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