





CHAPTER 2

# Jobs and Wages

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## Jobs and Wages

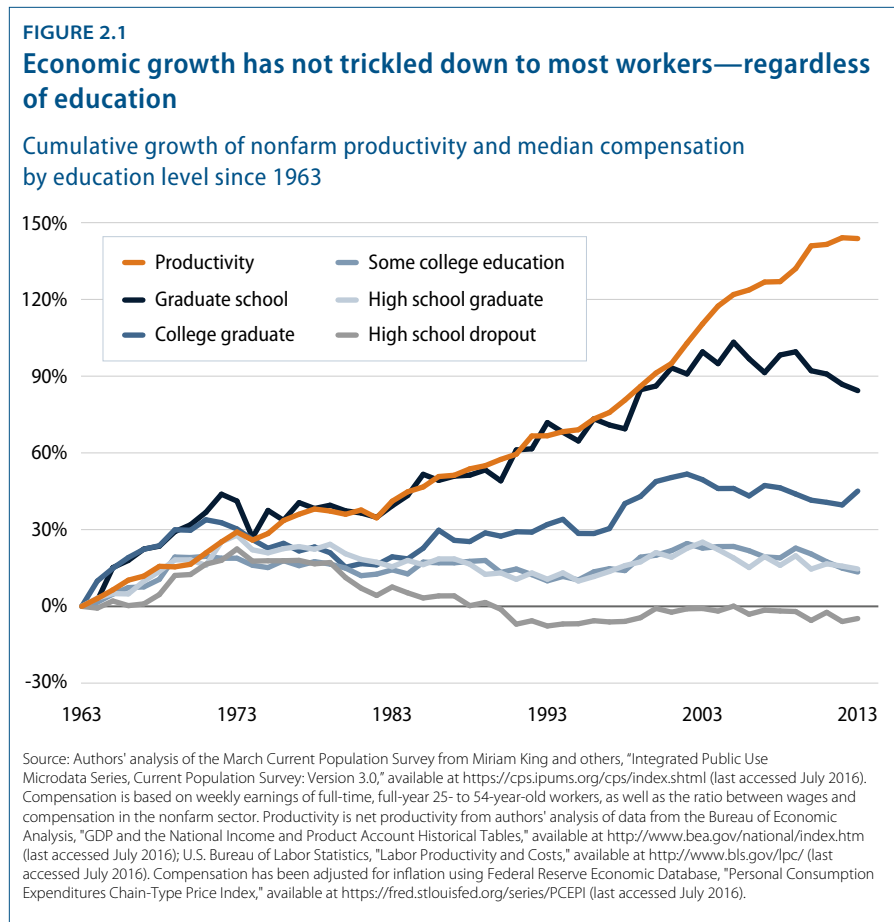
The most important step toward rebuilding middle-class economic security is raising middle-class incomes—and the vast majority of middle-class income comes from wages.<sup>1</sup> Therefore, raising wages and creating more good-paying jobs are both key to rebuilding middle-class incomes, wealth, and security.

The U.S. economy has made a great deal of progress on job creation since the end of the Great Recession. It is impossible to overstate how dire the economic and job situation was at the beginning of 2009, when the economy suffered a worse financial crisis than in 1929<sup>2</sup> and was losing 800,000 jobs per month.<sup>3</sup> It took extraordinary government efforts—including fiscal stimulus, industrial and financial system rescues, tax cuts, small-business support, and more—to prevent the economy from collapsing. The Federal Reserve’s actions and commitment to its full-employment mandate were also—and remain—critical to turning the economic ship around.

The economy has added about 15 million jobs since the labor market bottomed out in February 2010.<sup>4</sup> The unemployment rate in July 2016 was a low 4.9 percent, and broader measures of unemployment have almost returned to prerecession levels.<sup>5</sup> The economy’s progress toward recovery has been remarkable, yet there remains substantial room to create jobs.

Last year marked the first year of healthy real wage growth in the recovery as a result of stronger nominal wage growth and low inflation.<sup>6</sup> More troublingly, stagnant wages were a problem that long preceded the Great Recession. While real middle-class wages grew robustly in the 1960s and early 1970s—as they had since World War II—beginning in the mid-1970s, real wage growth stalled and, at certain points, disappeared. Strong, sustained real wage growth returned in the late 1990s but has been mostly absent since 2001.<sup>7</sup> Families originally coped with this wage stagnation by working more hours—primarily women joining the workforce—and later borrowing against their homes. Ultimately, rebuilding middle-class incomes and wealth will require a return to solid, broad-based wage growth.

One of the most striking aspects of wage stagnation before 2007 was that it occurred despite substantial output and productivity growth. Indeed, Figure 2.1 below demonstrates that even the earnings of full-time, college-educated workers grew at a slower rate than productivity. In other words, while the pie grew plenty fast until 2007, rising inequality had prevented middle-class workers from sharing in those productivity gains.



Broad-based wage growth has become even more difficult to achieve since the Great Recession as a result of weak demand and weak productivity growth. In this chapter, we analyze the forces restraining middle-class wage and job growth in the United States and propose a suite of policies to help boost them.

# The forces squeezing middle-class wages and the challenge to current policy

In January 2015, the Center for American Progress released the “Report of the Commission on Inclusive Prosperity”—the product of a multiyear collaboration between policymakers, academics, and thought leaders from across the developed world.<sup>8</sup> The commission concluded that economic growth was necessary for middle-class income growth but was insufficient without policies to ensure that growth was inclusive. Countries such as Australia and Sweden have demonstrated that the right set of policies can deliver robust middle-class market income growth, even amidst trends of automation and globalization, which are often blamed for the generation-long stagnation of wages in the United States.

Building on that report’s analysis, this chapter will briefly examine five trends that have played important roles in the stagnation of U.S. middle-class wages. They are:

- The undermining of worker power
- Global competition from low-wage labor
- The decline of labor standards and other regulatory protections
- The Great Recession and the incomplete labor market recovery
- Challenges tapping the full potential of people

The first three factors drove the uncoupling of economic growth and wage growth that preceded the Great Recession. The financial crisis, the Great Recession, and the slow return to full employment have made the challenge of wage growth more complicated. Wage growth is also complicated by continuing challenges in tapping Americans’ full potential, which has reduced productivity growth.

In sum, these five factors leave many Americans frustrated with the present and fearful about the future. We have made important advances on all of these fronts in recent years. However, much more needs to be done.

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## Undermining of worker power

Labor unions once guaranteed middle-class workers an equitable share of the pie. Unions helped build the robust post-war middle class, since they had the negotiating leverage to ensure that middle-class workers shared in the fruits of productivity gains. Middle-skilled workers in a union, for example, earn 20 percent more than similarly skilled nonunion workers.<sup>9</sup> Unions also deliver workers benefits such as paid leave and retirement.<sup>10</sup>

Today, however, unions have all but disappeared from the private sector: The share of private-sector workers in a union today is just one-third of what it was 40 years ago.<sup>11</sup> This collapse has directly contributed to the inequality that has robbed most workers of the benefits from productivity growth. One study by sociologists Bruce Western of Harvard and Jake Rosenfeld of Washington University in St. Louis estimates that about one-third of the rise of wage inequality is explained by the decline of labor unions.<sup>12</sup> Recent research by the Center for American Progress found that about half of the decline in the size of the middle class came from a weaker labor movement.<sup>13</sup>

One reason union membership has declined is a lack of enforcement of federal laws that protect the right of private-sector workers—regardless of their status as union members—to come together to discuss problems and push their employer for improvements. The penalties to businesses for violating workplace laws are often trivial or come too late to prevent the violation. And the fear of employer retribution and even firing has a chilling effect on workers seeking to exercise their collective rights and has helped drive the collapse of private-sector union density.<sup>14</sup>

Important progress has been made in recent years toward restoring worker power, even in the face of strong opposition. For example, President Barack Obama signed a number of executive orders to ensure that workers on federal contracts have a stronger voice on the job and are able to come together in unions. The orders require contractors and subcontractors for the federal government to inform their employees of their rights under federal labor laws; encour-

age federal agencies to consider labor agreements by project or consider prehire collective bargaining agreements on large scale construction projects; and require that workers on service contracts who would otherwise lose their jobs as a result of the completion of a contract be given the right of first refusal for employment with successor contractors.<sup>15</sup>

In addition, the president has consistently appointed pro-worker board members to the National Labor Relations Board, or NLRB, the independent federal agency charged with safeguarding workers' right to organize into unions. In October 2015, the Obama administration helped jumpstart a national dialogue about how to strengthen worker voice and power by convening a White House summit on the issue.<sup>16</sup>

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## Increased global competition

A second shift that has driven a wedge between economic growth and wages for many U.S. workers is increased competition from low-wage labor in other countries.

U.S. open-trade policies after World War II helped Europe, Japan, and other allies build or rebuild their middle classes. In the past 30 years, however, the United States has witnessed the opening of China, India, Eastern Europe, and other emerging economies around the world, absorbing new entrants to the global labor market with populations much larger than that of the United States, some of which also deploy aggressive export-led development strategies.<sup>17</sup>

At the same time, rapid changes in technology and financial market incentives have enabled and encouraged U.S.-based companies to coordinate production across national borders, putting domestic workers into direct competition with workers in other countries.<sup>18</sup> The parallel rise of the “knowledge economy”—the growing importance of intellectual property, or IP—has also shifted the relative strength of labor versus capital at a global level.<sup>19</sup>

In the past two decades, the ease of global transport and communication means that firms can shop around like never before for the lowest labor costs; weakest worker and environmental rights; minimal taxes; and highest subsidies. To obtain market access, companies also come under intense pressure from foreign govern-

ments to open production sites in local markets, as well as from competition from state-backed enterprises and industrial acquisition strategies. Together, we have witnessed a race to the bottom on a wide array of norms and standards.<sup>20</sup>

A growing body of research documents the effects of trade on U.S. workers' wages. MIT's David Autor and others have shown that the more a U.S. region was exposed to Chinese import competition between 1990 and 2007, the more it experienced declining wages, employment, and labor force participation.<sup>21</sup> Another study exploring the reasons for the declining share of income going to employees' wages, salaries, and benefits—which it calls the “payroll share”—found that globalization has been a key factor and that “increases in import exposure of U.S. businesses can explain about 3.3 percentage points of the 3.9 percentage point decline in the U.S. payroll share over the past quarter century.”<sup>22</sup>

Rising global trade competition, of course, has also benefitted the middle class through lower costs and greater variety of goods. Fred Bergsten of the Peterson Institute for International Economics estimates that benefits from increased trade translated into an additional \$9,000 in inflation-adjusted income between 1945 and 2003 for the average American household. And this is to say nothing of the millions of people in other countries able to join the middle class due to rising global trade.

Trade and foreign market access are also important for tapping new growth opportunities for U.S.-based parts of the value chain. They can further help build a middle class around the world that can be a source of demand for U.S. goods and services, as well as a driver of new democracies.<sup>23</sup> But those benefits can only accrue when trade meets certain basic norms and standards. For example, trade law has long recognized the importance of a level playing field in the form of prohibitions on unfair “dumping” products abroad below their domestic cost or of governments subsidizing products or services to boost market share.<sup>24</sup>

In recent years, progress has been made, for example, on better coordination of international tax transparency and by adding state-owned enterprise concerns into trade agreements. However, significant risks, practical details, and obstacles, such as insufficient enforcement, remain.

The challenge of growing global low-wage labor competition can also be met, in part, with a vigorous set of policies to better tap the full potential of people and better adjust to the new realities of an IP- and skills-driven economy.



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## Deteriorating labor standards and other regulatory protections

A third factor that has divorced middle-class wage growth from economic growth has been the deterioration of regulatory protections for the middle class.

The United States originally enacted a wide range of regulatory policies to rebalance the playing field between workers and powerful interests that had the ability and incentive to pay workers lower wages. And those regulatory policies have largely worked. Higher minimum wages, for example, reduce both poverty<sup>25</sup> and reliance on public safety net programs,<sup>26</sup> while also raising wages for workers making well above the minimum wage,<sup>27</sup> and increasing the economic security and stability of families.<sup>28</sup>

Many of those existing regulatory protections have not been sufficiently updated. Neither the federal minimum wage nor the overtime salary threshold have been automatically indexed to inflation or wage growth. Indeed, the \$7.25 federal minimum wage has not been raised for the past seven years, and it is currently below its real value in 1968 despite a doubling in output per hour.<sup>29</sup> And the overtime threshold—which once protected about two-thirds of full-time workers—only protects 8 percent today.<sup>30</sup> Fortunately, the Obama administration recently announced<sup>31</sup> that it will update the overtime threshold to ensure that middle-class workers are appropriately covered by the protections of overtime laws, as was intended by the original law.

Moreover, new challenges are also emerging. For example, the rise of volatile scheduling practices shift risk and responsibilities to working families without commensurate increases in pay. In 2011, 1 in 5 American workers—including more than one-fifth of parents with children under age 13—faced a nonstandard schedule.<sup>32</sup> Women, workers of color, and younger workers are particularly likely to face job schedule volatility.<sup>33</sup> Uncertain work also means uncertain pay, and these arrangements demand that workers budget, save, and plan more to get through the next week.<sup>34</sup>

Unfair scheduling practices make it nearly impossible for workers to balance work with caregiving responsibilities,<sup>35</sup> affecting not only parents but children as well. Research shows children's language development can be reduced if their parents work nonstandard schedules early in the child's life, and reduced academic performance in adolescence is associated with parents working nonstandard schedules for long periods.<sup>36</sup>

The deterioration of other regulatory protections has reduced middle-class economic security by reducing the buying and wealth-creation power of wages. For example, protections for employee retirement savings are critical to ensuring that workers' wages are efficiently transformed into retirement wealth and not siphoned off into unfair fees and financial traps. Consumer finance regulations perform the same role for financial services, such as a mortgage or a credit card, as does regulation for health insurance, student loans, or any number of other important middle-class consumer products.<sup>37</sup> And regulation can also have a broader effect on jobs and wages if a lax approach leads to a financial crisis,<sup>38</sup> if a corporate sector is focused on short-term profits at the cost of longer-term investments and sustainability,<sup>39</sup> or if industry concentrations raise costs, lower wages, or limit entrepreneurial opportunity.<sup>40</sup>

From the Affordable Care Act to the Dodd-Frank Wall Street Reform and Consumer Protection Act and beyond, the Obama administration has spent much of the past eight years updating these regulatory protections. Protecting the gains of recent years is critical—but more needs to be done.

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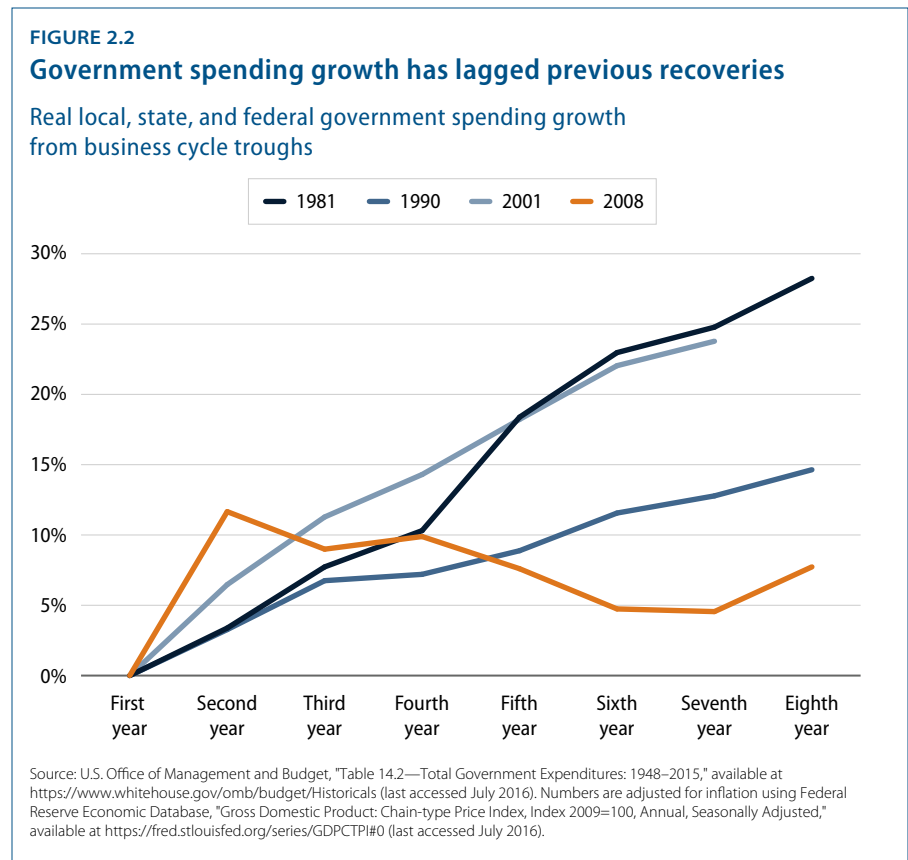
## The Great Recession and an incomplete labor market recovery

The three forces above—the undermining of worker power, increased global competition for low-wage labor, and deteriorating regulatory protections—drove a wedge between economic growth and middle-class wage growth between 1973 and 2007.

But wage stagnation became even more severe in the wake of the financial crisis and Great Recession, as well as the subsequent slow labor market recovery. Middle-class wage growth and full employment in the economy are inextricably linked. Employers do not raise wages out of charity—they raise them when workers have enough bargaining power to demand a raise or find a new job as a result of a tight labor market. When there are several out-of-work people willing to do the same job, wages will not rise.

It is difficult to overstate the economic effect on the middle class of the 2008 financial crisis and the subsequent Great Recession. To pick just a few data points: 20 percent of 16- to 24-year-olds were without a job in 2010; 2 million middle- and high-wage jobs were lost; 15 million families had their houses foreclosed on between 2007 and 2014; \$2.8 trillion in IRA and 401(k) wealth was destroyed; \$116 billion in small business lending evaporated between 2008 and 2011; and public confidence in the economy—and the American dream—was deeply damaged.<sup>41</sup>

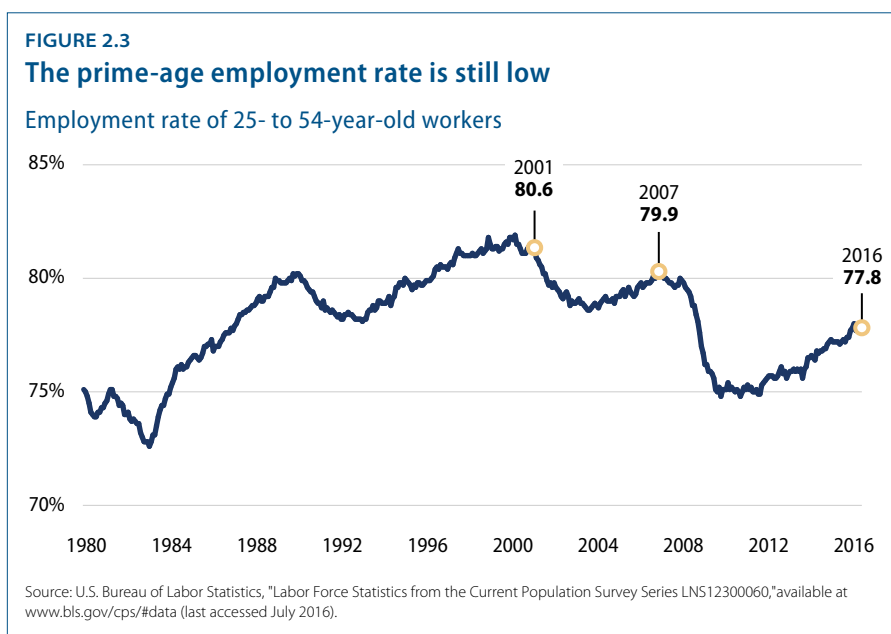
Upon taking office, the Obama administration correctly recognized the need for fiscal stimulus support and responded with a sizable stimulus program in 2009. Unfortunately, the Great Recession also produced severe budget crises among states and cities, causing them to cut spending, reduce hiring, and lay off workers. Rather than continuing to help state and local governments fill their budget hole, Congress itself cut spending beginning in 2011, culminating in the sequester cuts in 2013, which altogether cost 1.2 million jobs.<sup>42</sup> For several years thereafter, the Obama administration continued to fight for additional stimulus, but Congress continued to oppose it.



While the labor market has certainly improved over the past six years, it is far from clear that it has reached full employment, despite a low headline unemployment rate. The share of prime-age—25- to 54-year-old—workers with a job is still below its 2007 level and far below its 2001 level, as shown in Figure 2.3. There would be an additional 4.4 million employed workers today if the prime-age employment

rate returned to its 2001 level. The prime-age employment rate may in fact be a better indicator of labor market health today than the headline unemployment rate: While the relationship between the prime-age employment rate and wage growth has remained strong, the relationship between unemployment and wage growth has broken down.<sup>43</sup>

Perhaps the best evidence that the U.S. economy has not yet reached full employment is the fact that real wage growth—which only began to show signs of life in 2015—remains subdued. Subdued real wage growth and inflation this deep into the expansion suggests that employers still do not feel much pressure to raise wages, implying that a loose labor market is still putting downward pressure on wage growth.



## Challenges in tapping the full potential of people

A new concern about the U.S. economy is the recent slowdown of productivity growth—the long-run driver of rising living standards.

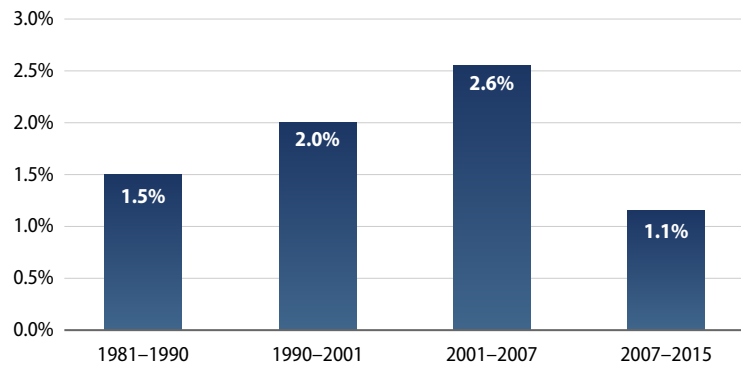
Slow wage growth may itself be a cause of slow productivity growth, as productivity and business investment are inextricably intertwined.<sup>44</sup> High wages give companies an incentive to invest in capital, such as machinery, and make their workers

more productive. But in a labor market marked by sluggish wage growth, firms can meet increased demand by hiring additional low-wage workers instead of investing in capital in order to make their employees more productive.

**FIGURE 2.4**

**Productivity growth has slowed sharply since the Great Recession**

Annualized real growth of net nonfarm output, per hour by business cycle



Source: Authors' analysis of data from the Bureau of Economic Analysis, "GDP and the National Income and Product Account Historical Tables," available at <http://www.bea.gov/national/index.htm> (last accessed July 2016); U.S. Bureau of Labor Statistics, "Labor Productivity and Costs," available at <http://www.bls.gov/lpc/> (last accessed July 2016).

The federal government, too, has not made enough productivity-enhancing public investments, such as in infrastructure, education, and scientific research. No number better summarizes this failure than the estimated \$3.6 trillion required to fix the United States' crumbling infrastructure by 2020.<sup>45</sup> While the Obama administration sought to rectify that with new investment proposals and attempts at budget deals, lawmakers' opposition to progress remained strong.<sup>46</sup>

Another reason productivity growth may have slowed is that long spells of unemployment can reduce workers' skills, as well as the quality of their matches with employers.<sup>47</sup> Workers who lose their jobs in recessions see their earnings fall even after they find a new job.<sup>48</sup> This earnings decline may reflect the loss of what economists call industry-specific or firm-specific human capital—skills and knowledge workers have that makes them more productive but could only be applied at their former industry or employer.<sup>49</sup> Millions of laid-off workers have returned to the labor force during the recovery, but they may not be as productive because they no longer have the on-the-job know-how they once did.



This speaks to a larger challenge the United States has had in maintaining its base of skills in an economy where workers move in and out of employment in order to take care of themselves and their families. For example, the United States is the only developed country that does not guarantee paid family leave when workers have a new child, and its investments in child care are inadequate. Whether a worker's extended separation from the workforce is the result of a struggling employer or a need to care for family, the result of this employment gap is a permanent reduction in their wages.

Addressing these challenges and restoring growth requires a policy agenda that fits the economy we have today. Fortunately, there are clear solutions to many of the problems we must address.

# Policy responses for reigniting growth, jobs, and wages

A policy agenda that seeks to raise middle-class wages must enable workers to share in the economy's gain, ensure a level playing field internationally, and restore the regulatory protections that prevent a race to the bottom at the expense of middle-class incomes and wealth. It must also ensure continued robust job creation, prevent financial crises, and raise productivity by tapping the full potential of the American people.

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## Maintain a high-pressure, full employment economy

In a vibrant, high-pressure economy, employment grows and employers compete for workers by offering raises. Establishing this kind of economic environment is a crucial starting point for raising wages and rebuilding middle-class wealth. The challenge of assuring that there is sufficient aggregate demand to run the economy at its full potential can be met by boosting public and private investment, ensuring resiliency in employment, executing a monetary policy that supports full employment, and effectively protecting against financial crises.

## Boost public investment

One of the smartest investments the government can make is in its infrastructure. Recent research by J. Bradford Delong and Lawrence H. Summers,<sup>50</sup> as well by the International Monetary Fund,<sup>51</sup> shows that infrastructure spending surpasses any reasonable cost-benefit analysis for two reasons. First, infrastructure expenditures have strong output and employment effects. When the economy is operating below potential, public spending increases total economic activity. This is also referred to as the multiplier effect, whereby one additional dollar of expenditure produces more than a dollar in total activity. Conservative estimates place the multiplier effect at approximately 40 percent, meaning for every dollar spent by the government, total economic output increase by a \$1.40.<sup>52</sup> Second, well-chosen infrastructure improvements raise overall productivity by providing effective support for economic activity.

Underinvestment produces chronic roadway congestion in metropolitan areas, service interruptions on public transit, and temporary closures of major facilities that add up to billions of dollars of lost productivity each year.<sup>53</sup> The time has come to move away from a reactive approach to infrastructure toward a growth-enhancing approach. To do so, the federal government must partner with state and local governments to provide robust and predictable fiscal support.

Recently, CAP released a comprehensive infrastructure report titled “An Infrastructure Plan for America: How Investing in Infrastructure Will Lay the Foundation for Prosperity, Advance Environmental Goals, and Rebuild the Middle Class.”<sup>54</sup> This plan calls for increasing total federal expenditures on infrastructure across sectors by \$500 billion over 10 years.

As part of this effort, Congress should establish a national infrastructure investment authority, or NIIA, to provide low-cost, flexible financing to projects of regional or national significance. Furthermore, the NIIA should have the discretion to provide zero or negative interest loans, as well as to offer truly subordinated debt. Finally, Congress should increase the share of federal funds that are distributed through competitive grant programs and expand performance management to provide greater transparency and accountability for how state and local recipients spend federal funds.

Taken together, increased expenditures and greater oversight will not only increase economic productivity but also ensure that funds flow to those projects that provide the greatest social, environmental, and economic return on investment.

### Boost business investment through long-termism

The private sector must also play a role in enhancing growth and raising wages. In particular, reducing the short-term focus of public markets may help remove corporate disincentives to invest.

Business investment began to fall off its pre-1990 trend in 2000.<sup>55</sup> Research by Bank of England Chief Economist Andy Haldane and others measured “impatience” across U.S. and U.K. industrial sectors, defined as how much markets excessively penalize a dollar of profit earned tomorrow relative to a dollar earned today.<sup>56</sup> They found no evidence of impatience between 1985 and 1994 but did find evidence between 1995 and 2004.

One of the most important policies that could promote long termism in the business community would be adjusting the tax provision that allows businesses to deduct executive compensation above \$1 million, if based on performance. This incentive should be restructured to encourage compensation that rewards long-term, rather than short-term, performance. The U.S. Securities and Exchange Commission, or SEC, should also increase transparency requirements for share buybacks in order to rein in insider manipulation and develop a better understanding of the link between buybacks and executive compensation. A sliding capital gains tax rate and greater proxy access both can reward long-term asset holding and better align the interests of executive decision-makers and long-term shareholders.

In addition, the SEC should enhance disclosure that would empower both investors and executives to focus on long-term results. For example—as proposed in a recent CAP report titled “Workers or Waste?”—enhancing disclosure of corporate investments in worker training could remove a disincentive to companies investing in their workforce while also better protecting investors who will want to reward productivity-enhancing workforce training.<sup>57</sup>

### Resilient employment solutions

Because the human and economic costs of recessions and slow growth are high, smart policy means preparing for recessions before they happen. Government should become a more active stabilizing force in the face of recessions by making it easier for workers to find jobs when the economy is weak. This will raise wages and curb employment loss in the short term by providing countercyclical stimulus, as well as raise wages in the long term by preventing spells of unemployment from permanently depressing workers’ earnings. And policy should also focus on helping workers who want to re-enter the workforce after leaving for non-economic reasons, such as raising a child or taking care of a parent.

We should enact a suite of policies that will raise wages by making employment more resilient, enabling workers who are laid off or who exit the labor force to find a job as quickly as possible. For example, the United States should deploy a new mechanism to automatically fund additional temporary national service positions during periods of high long-term unemployment, in addition to fully funding the 250,000 national service positions authorized by the Edward M. Kennedy Serve America Act of 2009.<sup>58</sup> The United States should also establish a national sub-

sidized jobs program that would help certain groups at the margins of the labor market—such as the long-term unemployed and persons with criminal records—find employment by providing incentives for local small businesses to invest in training employees whom they would not otherwise hire.

We should strengthen unemployment insurance, or UI, as a tool for fighting recessions and to help working families persevere through spells of unemployment. The Center for American Progress, the Georgetown Center on Poverty and Inequality, and the National Employment Law Project recently released a report, entitled “Strengthening Unemployment Protections in America,” that spells out ways to do just that.<sup>59</sup> The report suggests that UI must be better funded so that it can reach a greater share of the unemployed, including giving job seekers access to tools for successful re-employment and training. Eligibility criteria should be reformed to include part-time, lower-wage, and temporary workers. And UI must be made ready to respond to the next recession by modernizing its financing system and improving its solvency.

To support people who are searching for jobs but do not qualify for UI—such as recent graduates and individuals returning from unpaid caregiving—the United States should also create a Jobseeker’s Allowance that provides a modest, short-term weekly allowance, conditional on ongoing work search efforts.

### Execute monetary policy with the middle class in mind

The policy stance adopted by the Federal Reserve is key to allowing employment and wages to grow and the economy to reach its potential. Given the current economic environment of low inflation, very low long-term interest rates, and economic slack, monetary policy should resist calls to raise interest rates when circumstances do not require it. Premature rate increases could cut off economic recovery; with any challenge from inflation yet to materialize, this ought to be avoided. Instead, the Federal Reserve should focus on sustaining demand adequate to enable the economy to operate at full potential.



## Protect the economy and the middle class from financial crises

A healthy and effective financial system plays a central economic role in connecting those who want to save with those who want to borrow and grow. Yet, without strong and effective regulation, this system can break down—with devastating effects on jobs, wage growth, and middle-class wealth. Thus, a core element of maintaining full employment is preventing financial crises.

The Dodd-Frank Act and subsequent regulations under it made significant strides in addressing major fault lines in regulation. These improvements included requiring banks to have sufficient equity to absorb losses; to maintain enough liquidity to enable short-term resiliency; and to end proprietary trading and limit private fund investments to prevent swing-for-the-fences activities. The largest and most systematically important banks are also required to produce credible living wills that demonstrate how they can be wound down in an orderly fashion should they fail. The act also introduced measures to increase transparency and stability in derivatives markets to prevent unobserved daisy chains of risk. A robust Consumer Financial Protection Bureau, or CFPB, helps lay a solid foundation for financial stability as well.

More remains to be done. From the proper design of secondary mortgage markets to new and evolving markets engaged in credit extension—sometimes called shadow banking, or market-based finance—we will need appropriate regulatory guardrails and oversight. Ultimately, reform is also about restoring a sense of fairness and, therefore, trust.

Policymakers also cannot lose focus on making sure enough has been done, including capital, structural reform, and beyond. “Too big to fail” is not a challenge to be taken lightly. Failure to secure needed reform may not be broadly felt until it is too late, and the middle class again face the economic devastation wrought by a financial crisis and recession.

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## Empower workers to share in the economy's gains

A high-pressure economy with tight labor markets will help to raise wages, but more needs to be done to restore worker bargaining power. We need to firmly re-establish the link between wages and productivity that broke in the 1970s. Central to that is restoring and supplementing worker bargaining power. Here are several ways to do just that.

## Restore worker bargaining power

We should modernize our labor relations system—which has not been rethought since the 1930s—so that it can help workers and business thrive in the modern global economy. As described in CAP’s recent report “The Future of Worker Voice and Power,” there are four key elements to modernizing U.S. labor law: Replacing enterprise wage bargaining with multi-employer bargaining for an industry or region; expanding voice in the workplace to include organizations such as works councils; encouraging membership in worker organizations; and safeguarding basic rights for all workers. These proposals, taken together, will empower workers to negotiate for a larger share of the economic pie—even while supporting the productivity gains that will continue to see that pie grow.

Existing proposals such as the Workplace Action for a Growing Economy, or WAGE, Act are an important part of this modernization, but they should be understood of as part of a broader effort. Modernizing labor law will raise wages, ensure workers have a voice, boost productivity, and foster a collaborative relationship between workers and management.

## Deploy profit sharing

In addition to collective bargaining, profit-sharing mechanisms—such as broad-based stock options, worker cooperatives, and employee stock ownership plans—can also help raise wages and incomes. These programs are associated with higher pay, benefits, and long-term wealth accumulation for workers,<sup>60</sup> while businesses benefit from increased productivity, profitability, lower turnover, and a higher likelihood of long-term survival.<sup>61</sup>

Despite the benefits of these broad-based profit sharing programs, less than half of all American workers benefit from these programs today, and those that do only receive modest amounts of income from such programs.<sup>62</sup> As set forth in the CAP report “Capitalism for Everyone,” the federal government should adopt a range of policies to promote broad-base profit sharing.<sup>63</sup>

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## Address the labor market effects of globalization

Technology, transportation, and the end of the Cold War have inaugurated the arrival of a truly global labor market. The U.S. policy agenda must be clear-eyed about the effects on middle-class wages, incomes, and living standards wrought by globalization. This means developing trade policies that encourage open and vigorous trade—but on a level playing field for U.S. workers and businesses.

We must improve our understanding of how trade policy affects local economies, but we cannot close our doors. With the United States and its major trading partners needing to restore growth and increase productivity, trade will be an important tool for the developed world to access the fastest growing sources of demand around the world. Global demographics only underscore the importance of exports to future U.S. economic growth. When put on solid, well-regulated footing, trade can contribute to the prosperity and vibrancy of our global and domestic economies, lift people out of poverty around the world, and increase the United States' capacity to address global threats such as climate change and extremism.

As set out in the CAP report “Progressive Pro-Growth Principles for Trade and Competitiveness,” smartly structured trade relationships address challenges to fair competition—and with it, the effects on labor markets—posed by currency mispricing; state-owned and state-supported enterprises; unbalanced dispute settlement mechanisms; insufficient labor and environmental standards and enforcement; and rules of origin that undermine the supply chain benefits of trade deals for their participants.<sup>64</sup> Addressing subsidies that distort investment decisions is also critical.<sup>65</sup> Many of these arise from a lack of taxpayer accountability and uncompetitive, mercantilist practices.<sup>66</sup>

Trade should also move toward greater automaticity and become more like a regulatory relationship and less like a negotiated one.<sup>67</sup> As set out in the CAP report “300 Million Engines of Growth,” automaticity first and foremost focuses on making trade decisions more routine. Not only would this reduce the upfront costs of initiating trade actions but also reduces the chilling effects that threats of retaliation can have. Automaticity can also be deployed on a country-by-country level to reduce the potential negative political consequences of enforcing trade obligations.

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## Rebuild labor standards and the broader regulatory floor

From preventing the labor market from becoming a race to the bottom, to ensuring competition keeps prices in check, to protecting consumers from predatory financial practices, regulation plays an important role in protecting real wages. Much work has been done to rebuild the regulatory floor over the past eight years—but more needs to be done.

### Raise minimum wages

One of the most straightforward ways to raise incomes would be for Congress to raise the federal minimum wage to at least \$12 per hour by 2020 and index it to the median wage. In addition, Congress should eliminate the special \$2.13 subminimum wage paid to America's 4.3 million tipped workers, most of whom are women.<sup>68</sup>

There is growing momentum in states and cities to raise the minimum wage even higher than \$12—for example, California, New York, and Seattle have all put their minimum wages on track to reach \$15 in the coming years.<sup>69</sup> Cities and states should continue to raise their minimum wages above the inadequate federal minimum wage and consider raising it to \$15 per hour, especially in communities with a high cost of living.

### Reduce job schedule volatility

To help workers maintain a steady income, Congress should pass the Schedules that Work Act, which would require two weeks advance notice of worker schedules, allowing employees to plan around their work schedules and to request necessary schedule changes.<sup>70</sup> It would also protect workers from retaliation for making such requests and guarantee pay for shifts that were cancelled or shortened with little notice. State and federal policymakers should assess and learn from models of workplace policy reform enacted in municipalities around the country, such as in San Francisco, which recently became the first jurisdiction to pass a fair scheduling law.<sup>71</sup>

## Rebuild competition policy

Antitrust policy—and competition policy more broadly—remains a significantly underappreciated and underutilized regulatory tool. As a recent CAP report titled “Reviving Antitrust” shows, there is growing evidence that, across industries, increasing market power is having pernicious effects on our economy and politics.<sup>72</sup> These effects include higher prices and correspondingly lower wages; greater barriers to entry for new and expanding businesses; reduced product quality and innovation; as well as a corrosive influence on policymaking.

The report notes that there are a number of steps the United States can take to spur more vigorous competition. The past 30 years has been generally defined by remarkably permissive enforcement by the Federal Trade Commission and U.S. Department of Justice.<sup>73</sup> With new leaders and a reinvigorated approach, enforcement agencies can begin to administer presumptions against concentration and shift the burden of proof in favor of competition. In addition, executive branch agencies that presently lack clear competition mandates can be more actively engaged in order to provide oversight of concentrated sectors and assist with the sanctioning of anticompetitive behavior. Finally, antitrust enforcement needs greater transparency, which is achievable through more periodic disclosures of agency actions and industry competition data.

Whether it be ensuring that increasing market power does not result in higher prices for families, constrain wage growth for workers, or stymie small-businesses and entrepreneurs, revitalized antitrust policy has an important role to play in protecting middle-class economic security and opportunity.

## Empower vibrant pro-consumer regulatory approaches

By putting pro-consumer approaches at the forefront of their agenda, regulatory agencies can improve the economic position of middle-class households by reducing fraud, abuse, and unfair treatment, as well as by protecting against the devastation of a financial crisis. To take just one example, the Consumer Financial Protection Bureau, or CFPB, in its short history has provided more than \$11 billion in relief to 27 million wronged consumers and has processed nearly 1 million consumer complaints.<sup>74</sup> CFPB credit card regulations alone saved families \$16 billion in fees while also improving the reputation of the credit card industry and maintaining access to credit.<sup>75</sup> Protecting the CFPB from those who would strip it of its independence or effectiveness is critical.



Additional steps should also be taken to empower consumers of financial services and in other areas too. For example, once a year, consumers should be able to open an account at a different bank or credit union and have automatic deposits and withdrawals—such as paychecks and recurring bill payments—seamlessly carry over to the new account. This policy—which has existed in the United Kingdom for three years—would make it easier for families to switch financial institutions and would force banks and credit unions to truly compete for customers’ dollars and loyalty.<sup>76</sup>

Legal and regulatory approaches can also help rebuild wealth. Congress should make it easier to discharge student loans in bankruptcy for borrowers with poor-quality loan products or who attended programs with poor educational and career outcomes.<sup>77</sup> Similarly, while the courts currently permit modifications of mortgage loans on second homes and vacation homes, they do not permit modifications on primary residences.<sup>78</sup> During the foreclosure crisis, this restriction unnecessarily delayed the economic recovery of families and communities.<sup>79</sup>

Arbitration clauses that require individuals to waive their right to sue also create an uneven playing field for the middle class, eroding the ability of consumers to seek remedies in court when harmed by a product. Instead, any disputes go to arbitration—a process in which the company picks and pays for the ultimate decider in the case.<sup>80</sup> Despite their ostensible rationale, these provisions do not save consumers money: An analysis of credit card costs by the CFPB found that the difference in price based on the presence of arbitration clauses was not statistically significant.<sup>81</sup> Multiple agencies—including the CFPB, the U.S. Department of Education, and the U.S. Department of Labor—are seeking to limit the use of these clauses; Congress should stand with them.<sup>82</sup>

Overall, U.S. regulatory agencies need strong, independent leadership and funding to enable a vibrant, responsive regulatory approach working on behalf of both the middle class and the most vulnerable. Congress and the courts should not weigh agencies down with costly, burdensome red tape that only undermines their ability to execute the directives that Congress gave them in law.

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## Raise wages by tapping the productive potential of people

Productivity growth enables the long-run growth of living standards, and its recent slowdown should concern all Americans. Several of the policies found elsewhere in this report will boost productivity—just as full employment and higher

labor standards successfully raised productivity in the 1930s and World War II. But there are several additional policies that will raise wages through tapping the productivity enhancing potential of people, which can ensure growth is inclusive and a middle-class life is accessible for all.

### Enact family-friendly policies to conserve and increase human capital

In 2014, women who worked full time year-round earned 79 percent of what men who worked full time year-round earned.<sup>83</sup> Critically, the gap between the earnings of mothers and fathers is even wider. A recent analysis behind the factors driving this motherhood wage penalty found that about half is explained by the reductions in human capital and the types of jobs women take when they become mothers.<sup>84</sup>

The differences between men and women's work habits do not excuse the gender pay gap but rather spell out an agenda for closing it. Policies such as paid family and medical leave, paid sick days, and fair and predictable scheduling would all go a long way toward eliminating the differences between women and men's work histories and job placements. This is one of the most straightforward ways policy can raise incomes for families while growing our economy's long-run productivity.

### Invest in workforce training

A highly skilled workforce is essential to the ability of the American economy to respond to the global forces of change buttressing the middle class. Access to job training is crucial to developing those skills. An increasing number of middle-class jobs require postsecondary education or training beyond high school. Education or training can include two- and four-year degree programs; short-term certificate programs offered at a community or technical college; or job training programs offered by an employer or community-based or nonprofit organization. Such programs can offer a pathway to a stable profession with significant earnings potential.<sup>85</sup>

For example, apprenticeships are a job training model that is underutilized in the United States, yet has the potential to dramatically improve skill matching, job stability, and earnings for workers. A 2012 study concluded that those that complete an apprenticeship earn, on average, \$301,533 more in wages and benefits over their careers compared to peers who do not participate in apprenticeships.<sup>86</sup> Yet, less than half of 1 percent of workers in the U.S. labor force are enrolled in apprenticeship programs.<sup>87</sup>

Policymakers should work with stakeholders—including the business community—to expand apprenticeships among U.S. workers and increase the use of apprenticeship in nontraditional industries and occupations, as well as among nontraditional populations, including women and people of color. CAP set out a number of specific proposals to do so in the 2013 report “Training for Success.”<sup>88</sup>

Additionally, policymakers should take additional steps to incentivize and facilitate partnerships between education and training programs and the business community to ensure that worker training programs are preparing workers for jobs that are in demand and that local and regional employers have access to a pipeline of skilled workers. In particular, partnerships between community colleges and local business can help ensure that training is driven by real economic demand in the local community.

### Expand and diversify entrepreneurship

For many Americans, starting a business is not just a dream but also the path to reaching or staying in the middle class. Research by CAP has shown that entrepreneurship has declined from the 1990s to the 2000s.<sup>89</sup> Furthermore, the role of entrepreneurship in ensuring access to—and stability within—the middle class appears to be fading into the past, with more recent data suggesting that only those who already have access to capital and assets—typically wealthy, older, white Americans—are forming new businesses.<sup>90</sup>

To make entrepreneurship a vehicle for a middle-class lifestyle, access to stable, healthy capital and support for entrepreneurs must be expanded and targeted toward groups who are currently excluded from such opportunities. Policies that help strengthen the middle class will also provide the stability that entrepreneurs need to take risks, such as having access to housing equity; additional sources of income; education; and the training and skills necessary to start a business.<sup>91</sup>

### Eliminate unfair barriers to formal employment

Unfair barriers to formal employment encourage people to work in the less productive informal sector. Ending our ill-conceived immigration policies through comprehensive immigration reform would allow undocumented immigrants to find more productive employment and provide undocumented immigrants with

an incentive to invest in their human capital.<sup>92</sup> At the same time, eliminating these barriers will actually strengthen the effectiveness of protections such as the minimum wage and overtime for native-born workers, since undocumented workers will no longer fear speaking out when their employer breaks the law.<sup>93</sup>

The rising share of the population with a criminal record faces several barriers to finding a good job. Enabling individuals to earn a “clean slate” upon rehabilitation—through automatic sealing of minor offenses after he or she has remained crime-free for a set period of time—is a measure gaining bipartisan traction in states such as Pennsylvania and Michigan.<sup>94</sup>

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### Use tax policy to promote fairness

Tax policy is an important tool that can partially offset earnings lost due to a range of factors. While it is critical that the tax system raises sufficient government revenue to fund public needs—including everything from the defense budget to environmental protection—how we structure the tax system can make a significant difference for middle-class economic security.

Even though the tax code is progressive—and has grown more progressive under the Obama administration—it still retains various upside-down features that benefit the wealthy more than the middle class or those who aspire to enter the middle class. These include tax rates as low as 15 percent on income from financial industry partnerships,<sup>95</sup> a wide range of deductions that primarily benefit higher-income taxpayers,<sup>96</sup> and estate and capital gains tax rules that allow the wealthy to lower their tax rates or pass valuable assets to their heirs without paying the appropriate taxes.<sup>97</sup>

Eliminating these provisions to fund programs that boost the earnings of the middle class or those who aspire to enter the middle class makes a great deal of sense. For example, turning the mortgage interest deduction into a credit would provide the same benefit to all homeowners rather than a larger benefit to the wealthy.<sup>98</sup> There also exists bipartisan support for expanding the Earned Income Tax Credit, or EITC,<sup>99</sup> and CAP has proposed expanding the Child Tax Credit, or CTC, by eliminating its minimum earnings requirement, making it fully refundable, indexing the value of the credit to inflation, and introducing a Young Child Tax Credit in addition.<sup>100</sup>

At the same time, we can take action to simplify many of the existing tax benefits intended to make it easier for middle-class families to save for retirement and pay for their children's college education. Many of these programs are overly complex and may actually increase inequality since low-income individuals may not be able to afford the expertise to take full advantage of them. More can be done with tax policy, within limits, to increase economic security for the middle class, boost mobility for the aspiring middle class, and address the concentration of wealth and power at the top.

The recent trend for the wages and incomes of the U.S. middle class has been a challenging one. But the right set of policies, such as those outlined above, can help to rebuild them.

## Taxes, transfers, and the middle class

The analysis in this chapter and the introduction relies on income data from the U.S. Bureau of the Census and the Survey of Consumer Finances, which measure income before taxes and does not include the value of certain noncash transfers, such as Medicaid. Some datasets that include the effects of taxes and these noncash transfers show stronger middle-class income growth than described above. Yet, the value of these gains is overstated and has come almost entirely from tax cuts and transfers instead of the ability of families to get ahead through work.

Data from the Congressional Budget Office, for example, include the effects of taxes and noncash transfers and show an 11.2 percent increase in middle-class income between 2001 and 2013, which is substantially more than the negative income growth shown by the Census and Survey of Consumer Finances data over the same period.<sup>101</sup>

All datasets have their strengths and weaknesses, and the CBO data are no exception. While the information about the taxes and transfers received by families is invaluable, there are two important caveats to the relatively strong middle-class growth the CBO reports. First, almost half of that increase comes from increased employer and government spending on health insurance. The CBO adjusted these transfers for overall inflation, but health care prices grew more than 40 percent faster than overall inflation between 2001 and 2013.<sup>102</sup> Since Medicare, Medicaid, and employer-provided health insurance can only be used to purchase health care, the CBO overstates their rise in value since it does not adjust them for the rising real price of the only service they can purchase.

The other caveat is that almost two-thirds of the middle-class income growth reflects more government transfers—including health care—and lower taxes. The reliance of middle-class families on tax cuts and transfers from the federal government rather than rising market incomes is a new phenomenon: Between 1979 and 2001, 95 percent of income growth came from rising market incomes. It has only been since 2001 that middle-class income growth mostly relied on tax cuts and transfers.<sup>103</sup> While progressives certainly believe that progressive taxation and smart government transfers can help grow middle-class incomes, the tangible economic frustration that many middle-class Americans feel today demonstrates the importance of structuring the overall economy to facilitate inclusive prosperity.

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