How Economic Change Happens and Why We Resist It

Panel: How Change Happens and Why We Resist It . . . as if we could
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Andrew Reamer, Fellow
Metropolitan Policy Program, The Brookings Institution

I'm happy to be here and to play a role in celebrating the tenth anniversary of the founding of the Regional Institute. Congratulations to Kate Foster and her staff—may the Institute have many years of success ahead.

The title of this panel offers up two topics—how change happens and why we resist it. The short version of my talk is to offer, from an economic perspective, one word on each topic. Change happens because of innovation, and we resist it out of fear. The rest, as a sage once said, is commentary.

Economic change is endemic, actually it's integral, to modern democratic societies. The evidence of constant economic change is all around us. Let's explore the key dimensions of change for the nation and Buffalo, and tie these dynamics to the notion of innovation. To the extent that I can, I'll use 1960 as the base year, because as you know Buffalo was a very different place economically then than it is today.

By the most basic of measures, national economic growth has been phenomenal. Our national economy today is four and a half times bigger than it was in 1960, after adjusting for inflation. A fraction of that is due to a growth in population; the rest is because we are a much more productive society. Gross domestic product per person in 1960 was $13,800 (in 2000 dollars); in 2006, the figure was $37,800,

almost three times greater. Overall, this money allows us to have a lot more stuff—bigger houses, two houses, more cars, more gadgets, more leisure opportunities—and live longer lives.

Other good news is that the nation's poverty rate fell from 22 percent in 1960 to 12 and a half percent in 1970. The not so good news is that the poverty rate hasn't changed much since.

There's been another type of change in the nature of the nation's economic performance—regarding the distribution of benefits from economic growth. The share of nation income going to wages and salaries is now a little more than half the total, the lowest figure on record and well below the peak of 59 percent in 1970. In contrast, the share going to profits, 14 percent, is the highest on record. Looked at another way, between 2001 and 2006, 34 percent of the increase in national income went to workers, 46 percent went to profits, the first time profits have received a larger share of a recovery than wages.

OK, now let's look at the how, what, where, and who that underlie our remarkable growth in GDP per person. As implied by the above numbers, we've had a phenomenal growth in productivity, how much gets produced by each person. Between 1960 and 2006, productivity per worker hour climbed 161 percent. In 1960, the engine of our economy was manufacturing—in that sector, productivity exploded by 326 percent. In other words, what four and a quarter people in 1960 could produce in an hour, one person can today. How did this happen? Innovation, of course, in the technology of making things.

This explains in large part the remarkable decline in the presence of manufacturing in our economy. In 1960, U.S. manufacturing had 16.8 million workers, over 1 in 4 of the total. After peaking in 1979 at 21.2 million, the number has fallen to 14.2

million, less than 1 in 10. Yet these workers are producing 438 percent as much stuff as their counterparts did back when.

A lot more of which goes overseas than it used to, and, as we know, we have a lot more stuff coming off ships and planes here. The world has opened up, the U.S. is no longer an economic island. In 1960, our exports of goods equaled 5 percent of GDP; for imports, the figure was 4 percent. By 2006, the corresponding figures were, 8 percent for exports and 14 percent for imports.

Why has the world opened up? Innovations in communications, transportation, and information technology. The diffusion of knowledge is allowing other countries to do what we have done, communication networks are allowing people to transverse the globe without leaving home, innovations in shipping and air have allowed us to move massive amounts of goods, and IT has greatly expanded our power as individuals and as organizations to manipulate, acquire, and communicate massive amounts of information, instantaneously,

Historically, humans have worried about getting their immediate material needs met, once those are taken care of, we look for gravy. With the wealth given society by the enormous increase in goods manufacturing, service-producing sectors have exploded in size, services of all kinds—for instance, health care, professional and business services, transportation, leisure and tourism, and information services. As an example, in 1960, health services employed 1.6 million people, just 2.5 percent of the total—at one level, health care was a societal luxury, at another, there wasn't much 1960 medical care could do for many health problems. In 2006, the industry has 15.4 million workers, 11 percent of the total and more than manufacturing. Of course, the growth in health care was enabled not only by the wealth generated by improvements in goods productivity but by innovation in the

sector itself. We can take care of people in a way not possible ever before, and there are jobs to be had in providing those services.

All of which means that our occupational structure has dramatically changed. In 1960, nearly half the workforce could be considered blue collar—factory workers, construction workers, laborers; today the figure is about a fifth. Conversely, in 1960, a little over a fifth of workers were managers, professionals, and technical workers; today that figure is above 35 percent. One of my favorite statistics—it startles us to think this, but through the 1950s, the peak earning age of a man was about 38-39, after that his physical strength and his ability to grab hourly or piecework wages, went into decline. Now, of course, peak earning years come much later for most.

Because, essentially, the combination of technical productivity improvements and education have shifted the foundation of our economy from brawn to brains. In 1960, only 8 percent of adults had a college degree; today the figure is 28 percent. The shift was brawn to brains, enabled by innovation, has of course enabled women to participate in the workforce to a much greater degree than 50 years ago.

And innovation has facilitated an improvement in our national moral character in that economic opportunities for those who have other than white skin have improved substantially over 50 years ago.

There's another dimension of economic change to be mentioned, corporate dynamism and volatility. The innovations that allow movement of goods, services, information and people around the globe have led to far more intense competition—among firms, communities, and countries. Innovation has led to jumps in economic opportunity and risk for the entrepreneur--the rate of business formation and business deaths is about four times that of 50 years ago.

There's a magnitude of job flows that is difficult to see on the surface. Every three months, the net change in total U.S. jobs is a few hundred thousand, more or less. Now let's look at gross flows. Between October and December 2006, new and expanding firms added 7.7 million jobs, and closing and shrinking one cut 7.2 million, out of about 140 million jobs total. Change is happening all the time, even when we don't see it.

We also see the geographic disaggregation of economic activity. As we are reminded regularly, firms can slice and dice various operations across the country and overseas, out-sourcing at the drop of a hat. Our new ability to move massive amounts of money, and analyze opportunities for doing so, has led to a wave of mergers and acquisitions about ten times the number in 1960. Which has had, we all know, substantial impacts on many communities, which cannot pick up and go like corporations can.

Overall, the combination of capital mobility, heightened competition, and greater productivity has transformed our communities for better and not better.

Which brings us to Buffalo, radically transformed radically since the time when is economic engine was manufacturing. For all the reasons I've just outlined—huge jumps in manufacturing productivity, global competition, mergers and acquisitions—Buffalo's manufacturing employment is a third of what it once was. Which may mean that the area actually produces as much stuff as it once did, but now its economic engine has diversified into services, particularly financial, health, and education services.

OK, so Buffalo has moved from brawn to knowledge, fine, but. Buffalo's transformation has not been an easy one. Its population peaked in 1970 and keeps

hitting new lows, now down about 15 percent. The number of wage and salary jobs topped out in 2000. In the last seven years, Buffalo lost 22,000 manufacturing jobs, as many as it had lost in the previous 18. The loss of these jobs is telling, because manufacturing jobs tend to pay well. In 1969, the average Buffalo job paid 109 percent of the national average; in 2005, that figure was 88 percent.

Perhaps for this reason, recent job growth has been among the self-employed. Between 2000 and 2005, the Buffalo area lost 12,000 wage and salary jobs and gained 15,000 new sole proprietors, this after the number of self-employed was rock steady for over a decade. Which may suggest that this is likely an entrepreneurship of necessity as much if not more than entrepreneurship of opportunity.

The loss of good-paying jobs in turn is having an impact on population size and composition. Studies show that the rate of outmigration from upstate New York is not much different than that for other areas; the problem is that few people are moving in. Which gives Buffalo a relatively old population. It turns out that one engine of the Buffalo area is the Social Security checks and Medicare benefits its elderly receive.

These various trends might explain an unusual comparison with the U.S. with regard to poverty. Buffalo’s 2006 poverty rate among kids is far higher than is so for the nation, while its poverty rate for the elderly is much lower, perhaps a remaining benefit of the old manufacturing economy. But these differentials, the legacy of economic change, are not a positive sign.

And there is a glimmer of hope. 2007 looks like a turnaround year. Jobs are up for the first time in a while, entirely due to finance and insurance and business services.

What hath innovation wrought? The 20th century economist Josef Schumpeter said that capitalism was a form of creative destruction, and the experience of Buffalo in the last several decades certainly gives evidence of that dynamic. And a good reason to resist change.

And yet we can argue that, you know, Buffalo wasn't left out of the great economic benefits produced by this nation. Real per capita income didn't climb three times over like it did elsewhere, but it did climb a lot, and a lot of people are far better off in Buffalo now than they were in 1960. So absolute gain is real, but so has been the pain.

Which is why people resist economic change. We seek to avoid loss and fear of further loss, of three things. First is the loss of real, tangible economic benefits, money and what money will buy—a roof over our head, food on the table, clothes—the physical essentials of life.

Second is loss of experience, of coming to work in the morning and seeing familiar faces, of feeling the accomplishment of a task well done, of being part of a team, of setting a long-term goal and reaching it. It's the loss of the dopamine effect, of the opportunity to have the brain go "ah," we all know what that feels like and losing that is real.

Third, and here is the heart of the matter, is the loss of meaning and identity, of our "story" or narrative. For we all have a story about who we are and how we are doing, that we are living a life that has purpose, that we have worthy goals and we've done a good job reaching them. Economic change, particularly if you're on the front end of Schumpeter's creative destruction, can destroy the story you've

been living for years, for decades, and not give you a desirable, worthwhile alternative or show you how to find one.

You can lose the sense of adequacy, the sense of dignity, the sense of meaning that a job gave you. Moreover, you may be wrenched out of a world in which you knew, and liked, the values, the culture, the way people related and solved problems. Economic change may mean that you have to learn a whole new way of being, and you may not like that way of being or having to cope with adjusting to it. If the local industry is disappearing, you have to make a choice about who you want to be, which may involve a bewildering and unattractive set of options. And once you do make a choice about a different way of working, you may have difficulty adjusting to the change, perhaps in how much control you have over your work, of the kinds of choices you have or don't have to get the job done, of the kinds of relationships you have on the job. Economic change may mean that you have to be adaptable when you liked the way the world worked before, thank you very much.

The destructive end of economic change also wreaks havoc with the sense of the broader "us," of the group, our place in it, and how the group is doing. We all have groups we belong to and give us meaning. It may be the work team, the union, our neighborhood, the church, our town, our metro area. The Bills fans on Monday night screaming for that kid from Dallas to miss the field goal. Economic change can toss these groups, and the sense of self we get from belonging to them, up in the air and scatter them to four winds. Or can give us a sense that our group isn't a winner anymore—"hey, that's Buffalo," Jerry Sullivan of the Buffalo News said after Monday's game—and you all understood what he means. When a business closes, when industries disappear, we can lose not only a workplace but all sorts of groups beyond the building's gates.

We all live stories, a narrative. Our emotional experience in large part is a function of the size of the gap between who we think we are now and who we think we want or are supposed to be. When that gap is large, we have problems. And we have several choices—we can change our circumstances, we can change our judgment of them, we can change our goals, or our sense of what should be. It's natural then, to want to block economic change, and if it occurs, to look for ways to bring back the world we knew.

When the world has changed—when machines replace people, when borders open up, when Buffalo's economic advantages disappear—eventually resistance and denial disappear as well. Individuals and communities recognize they need to reinvent themselves. Which can be incredibly difficult, there's no perfect roadmap for doing that. Other people, other places have been successful, but we quickly discover that each circumstance has its own logic and ultimately we realize we are on our own. And we have to be wary of the opposite of resistance and denial—unrealistic or magical thinking that this new industry, or firm, or job—in biotech or IT, say—will make everything all right.

At one level, adjusting to regional economic change is a social and institutional phenomenon, and so the coming remarks are a segue into those of my co-panelists.

Fundamentally, positive adjustment to regional economic change is far more likely to take place with effective regional leadership, from the public and private sectors. One of the challenges for a region like Buffalo is overcoming the loss of community leadership from locally–owned businesses that were major employers, one of the consequences of economic change.

Be that as it may, regional reinvention quite often takes place because of civic entrepreneurs, people with vision to grasp the sense of the possible and the power

to communicate that vision, that new story, and move others to action. In the realm of the concrete, they are able to influence investment in the resources for change, investment in plant, in equipment, in workforce. Most important, though, is that they catalyze hope, they build consensus about reframing the regional story, about what's possible and how to work together to get there. And when reinvention is successful, the burden on economically displaced individuals becomes lighter. Not that it can erase all losses, because many individuals will have difficulty finding work that matches the skills and wages they had in their old jobs, but the possibilities for personal recovery increase.

In closing, economic change happens, always, because innovation is constant and the consequences are ongoing. Resistance to innovation is futile. The question is, individually and collectively, how to deal with these consequences.