The United States is about to experience economic upheaval on a scale unseen for generations. Will social harmony be a casualty?

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It has become conventional wisdom that class politics has no legs in the United States today—and for good reason. Regardless of actual circumstance, an overwhelming majority of Americans view themselves as middle-class. Very few have any bone to pick with the rich, perhaps because most believe they will become rich—or at least richer—someday. To be sure, the issues of jobs and wages inevitably make their way into our political campaigns—to a greater or lesser extent depending on where we are in the business cycle. But they seldom divide us as much as simply circle in and out of our political life. Lately anxiety about the economy has been palpable, but for the most part it has not evolved into anger or found specific scapegoats.

Economic insecurity could well divide us in the future, however. We are on the cusp of an economic era whose challenges will be unfamiliar to most Americans of working age. It is likely to erode the psychological pillars on which class unity has rested in this country: personal economic stability for the middle class, and the promise of at least some upward mobility for most Americans. The most likely division—besides that between the truly rich and the truly poor—will be between those in the middle class who are able (through agility or luck) to manage economic risk and those who find themselves helpless before the economic pressures of a new age.

Once upon a time, or so it is said, America was a place with lots of upward but little downward mobility. In the really old, pre—Civil War days you could start out splitting rails, head west, make a success of yourself on the frontier, and perhaps even wind up as president. In the relatively recent, post—World War II expansion you could do well by landing a blue-collar job in a unionized manufacturing industry or a white-collar job at a large, stable American corporation such as IBM, AT&T, or General Electric—which offered job security, high salaries, and long, steady career ladders.

There was always as much mythology as truth to this image of America. Lighting out for the West was expensive; covered wagons did not come cheap. More generally, although many terms could be used to describe economic life in the nineteenth and early twentieth centuries, "stable" and "secure" are not among them.

But there was considerable truth to the image as well, particularly after World War II. Regardless of education level or family background, many Americans who valued stability and security really did have the chance to grasp it; jobs with "a future"—that is, with steadily rising wages and solid retirement plans—were plentiful. And even for many of those who were fired, the economic risks were fairly low: the unemployment rate for married men during the 1960s averaged 2.7 percent, and finding a new job was a relatively simple matter. During the first decades following World War II, to the astonishment of interviewing sociologists, a majority of Americans began to define themselves as middle-class.

This post—World War II period stands as a reference point in our popular economic history—a gold standard for rapid growth and shared prosperity. It lingers in our national memory, and remains an important source of confidence in the unity of our culture and the awesome power of our economy. But although it engendered our current economic expectations, our sense of "the way things ought to be," in reality the postwar era was probably an aberration, a confluence of events never before seen in our history and unlikely to be seen again.

Most obviously, it was an era defined by the isolation of America's continental market from the devastation of World War II. In the early postwar decades foreign competition exerted virtually no pressure on our economy. (In 1965, for example, imports of automobiles and auto parts came to less than $1 billion—about a fortieth of what they are today, after adjusting for inflation.) At the same time, domestic manufacturers benefited from an enormous pent-up demand for mass-produced goods: cars, washing machines, commercial aircraft, refrigerators, lawn mowers, television sets, and so on. New highways gave rise to new suburbs, and to a resulting construction boom.

These economic conditions, along with successful federal efforts to maintain full employment through loose monetary policy, created an environment exceptionally friendly to workers. With little foreign competition on the one hand and a very tight labor market on the
other, American firms were willing and able to offer workers strong incentives—such as pensions and first-rate health insurance—in order to attract and retain them. (Generous tax breaks from the federal government encouraged the roll-out of these benefits.)

Meanwhile, the Great Depression had given rise to a system of government programs and policies that came into full force and maturity only after World War II—among them Social Security, unemployment insurance, welfare, and high marginal tax rates. The rise of communism abroad could only have strengthened commitment to workers' welfare, as a means of demonstrating that the American capitalist system offered a humane alternative.

Thus favorable macroeconomic circumstances, the absence of foreign competition, and a historically unique political dynamic all combined to allow postwar America many of the benefits of social democracy without the costs. The economy did not stagger under the weight of ample benefits and high taxes. Americans—at least white male Americans—did not have to worry about tradeoffs between security and opportunity, because the United States offered both. And it seemed that this was the natural order of things.

The threat of downward mobility first hit America in a big way in the 1980s, when the old-line, unionized midwestern manufacturing companies found themselves under enormous pressure from foreign competition, in particular from export-oriented Japanese companies such as Honda, Toyota, and Komatsu. The result was a hemorrhaging of unionized manufacturing jobs and the emergence of the Rust Belt.

In addition, new technologies and consumption patterns were shifting the U.S. economy's center of gravity from skilled, unionized, mass-production industry—which fashions products from expensive materials and capital-intensive machinery—to services and retailing, where barriers to the entry of competitors are lower, labor costs more significant, and competitive advantage more reliant on squeezing those labor costs. The nation's largest private-sector employer today, of course, is not General Motors or Ford but Wal-Mart. Wal-Mart is in many ways a fine company, but its strategic goals and constraints are quite different from those of the manufacturers of the 1960s. Between them the automakers and the UAW offered workers a fairly robust "social contract": pensions, good health care, high wages, long-term job security. Wal-Mart makes no such offer.

By the early 1990s the nature of unemployment had changed as well. As Erica Groshen and Simon Potter, of the New York Federal Reserve, point out, temporary layoffs have become less common. Instead companies under constant competitive pressure are more frequently making layoffs permanent—using advances in technology to eliminate some types of jobs altogether.

At the same time, the rising cost of health care and the falling rate of health insurance have left families much more economically vulnerable in the event of a serious accident or illness. Many Americans today are one lost job and one medical emergency away from bankruptcy.

We do not want to overstate how bad things are. Not even white males would be better off in the economy of the 1960s, when median real household incomes were only about two thirds of what they are today, and much of the medical care that we now fear we cannot afford was unavailable at any price. In a sense we've merely returned to a more natural economic state, in which jobs are not always secure and progress is not always assured. And we've done so while improving the opportunities and lifestyles available to most Americans. So far, in other words, we've adapted reasonably well to increased risk and reduced security. But we're not at the end of economic history—and the history that will be made in the coming decades is likely to be substantially more turbulent than what we've seen in recent years.

Although the impact of globalization on American jobs has been overhyped in the past, its impact in the future will be hard to exaggerate. Last spring saw a short political boomerlet of worry over the offshoring of white-collar jobs to India, China, and elsewhere. In the next few years these issues will be raised at the political level once again—and loudly.

The basic storyline is simple enough: what formerly could not be imported now can be. A compelling parallel can be drawn to the latter half of the nineteenth century, when the steel-hulled oceangoing steamship and the submarine telegraph cable revolutionized international trade. Companies could now use the telegraph to tell their agents in distant ports what goods to ship; moreover, powerful steamships made it practical to export not only precious goods (such as rare porcelains, spices, and tobacco) but also staple agricultural and manufactured products: grain, hides, meat, wool, furniture, and machines (which would eventually include motor vehicles, computers, and consumer electronics). First in a great rush, and then at a somewhat more measured pace, industrial and agricultural workers the world over began to lose their jobs to more-efficient foreign competitors. Illinois could grow wheat more cheaply than Prussia could grow rye. Malaysia could grow rubber more cheaply than Brazil. Of course, displaced workers could generally find new jobs, sometimes better ones. And consumers benefited greatly from lower prices. But that did little to dim the spectacle of immediate dislocation. The expansion of international trade ushered in a century-long storm—though many Americans (perhaps owing to the anomalous calm following World War II) seem to remember only the recent gusts that have buffeted our heavy industries.
The transformation taking place today will have just as great an effect on the world economy. The transoceanic fiber-optic cable, the communications satellite, and the Internet are making much white-collar service work as tradable as anything else. Broadband cables and satellites can connect India or China or Bulgaria to the United States instantly, seamlessly—and almost without cost. A huge new swath of American jobs is beginning to become vulnerable to foreign competition.

When the offshoring of services truly hits (and it will stretch out over several decades), it is likely to deliver a much greater shock to the U.S. economy than the offshoring of manufacturing did. There are several reasons for this. First, in the 1970s Americans' incomes exceeded those of the Japanese by a ratio of about two to one. The ratio of American to Indian incomes today is more than ten to one. Economists will point out that the gains from trade will thereby be that much greater for the U.S. economy as a whole—and they'll be right. Indeed, more and greater openness will expand opportunities and raise incomes for some Americans, producing many highly visible winners. At the same time, the potential pay cuts for workers who lose out in rich countries will also be that much greater.

Second, the coming global trade in services will potentially affect a much larger proportion of the U.S. labor force. Even at its height manufacturing constituted only 28 percent of all non-farm employment, and large sectors of manufacturing (food processing, for example) are closely tied to sources of supply and thus immovable. Service jobs constitute 83 percent of non-farm employment in the U.S. economy today, and every job that is (or could be) defined largely by the use of computers and telephones will be vulnerable.

Third, the impact of foreign competition will be borne much more directly by American workers than by their employers. In the 1970s and 1980s foreign imports threatened U.S. companies and workers equally. The CEOs at GM and Ford were on the same "side" as the men and women who worked on the factory floor. The coming wave of economic dislocation will look very different: it will be something that American CEOs do to their own workers.

Not that they'll necessarily have much choice; offshoring will in many cases be necessary if American businesses are to remain competitive. Remember H. Ross Perot's "giant sucking sound"? In the early 1990s no one spoke out more strongly against the prospect of job loss caused by foreign competition. Yet on February 7 of last year the Times of India reported that Perot Systems was going to double its employment in Asia from 3,500 to 7,000—nearly half its total worldwide employment. If the economic logic of foreign outsourcing is so overwhelming that Ross Perot can't resist it, what American CEO will be able to?

One of this is to say that we face a future of permanent widespread unemployment. It is a truth universally acknowledged (except in campaign seasons) that the rate of employment in the United States is set not by levels of imports and exports but, primarily, by whether the Federal Reserve's monetary policy manages to settle aggregate demand in that sweet spot where neither unemployment nor inflation is too high.

Moreover, during the course of any single year or business cycle the effects of globalization on the U.S. labor market are small. Forrester Research has estimated that by 2018 some 3.3 million jobs in business processes are likely to go offshore. That's a little more than 18,000 a month—not a huge number in an economy of 140 million jobs.

But—and this is a very big "but"—even though imports and offshoring do not determine the number of U.S. jobs over time, they do powerfully influence the long-run level and distribution of real wages. Eventually the offshoring of service jobs will exert a strong downward pressure on wages and benefits in jobs that stay onshore, just as the offshoring of manufacturing jobs did in the 1980s. Essentially, the pool of workers competing for many service jobs will be increased by, say, several million English-speaking college graduates in India, who will work for a tenth to a fifth of a typical American salary.

In many cases the jobs in question are held by Americans unaccustomed to layoffs or reduced incomes. Often they are high-paying white-collar jobs. The people who hold them may believe that they are on top because they deserve to be: they are smart and industrious; they worked hard in school while others screwed around; they have been diligent and successful in their careers. These people are likely to become very angry when unexpectedly threatened by substantial downward mobility.

How will the country respond when a broad new array of classes and professions are exposed to downward mobility—particularly as others benefit from new opportunities? Will existing class fissures be exacerbated? What new ones might be created?

Winners and losers are unlikely to sort cleanly. People of similar background and training may see their fortunes diverge greatly depending on subspecialty, or on the presence or absence of some idiosyncratic ability that is hard to replicate. But one can make a few predictions. First, the new environment is likely to pit those who are most flexible—most able to shift jobs or careers, most able to absorb unexpected blows, best positioned to benefit from unforeseen opportunities—against those who are less so. The contours of such a divide seem predictable: young versus old, generalist versus specialist, people with savings versus those who depend on their next paycheck.
A second (and overlapping) split might open between those who are highly educated and possess complex skills and those who are merely well educated and skilled. An MIT education may still be hard to imitate abroad. Can the same be said of a finance degree from a state college? Third, a divide may occur between those—whatever their education or income level—who by disposition can tolerate unexpected income swings across a lifetime and those who abhor uncertainty.

The last group is probably large. The dissatisfaction resulting from falling wages is usually greater than the satisfaction resulting from rising wages. People are not wrong to be risk-averse; for middle-class Americans, just as for portfolio managers, life consists largely of trying to manage risk. This, the Yale political scientist Jacob Hacker thinks, is the source of middle-class Americans' unease with the current state of the economy—perhaps the primordial form of a sharper discontent to come. "Voters say the economy isn't getting better because, as far as they're concerned, it's not," Hacker writes. "And perhaps the best explanation for this perception is that Americans are facing rising economic insecurity even as basic economic statistics improve." The median annual household income twenty years ago was about $38,000 in today's dollars. Today it is about $43,000—13 percent higher. Yet, at least in Hacker's analysis, Americans typically feel that increasing risk and rising inequality have hurt them at least as much as increasing income has helped. Yes, if they are middle-class, they have higher real incomes and living standards than their parents; but the incomes are known to be insecure, and the prosperity is felt to be fragile.

From one viewpoint, economic risk is the flip side of flexibility, entrepreneurship, and innovation—the very things America does best. In the 1980s, when Americans worried about whether the social organization in Japan's export-manufacturing sector (morning calisthenics, the company song, consensus, lifetime employment, and so on) might offer a better way of doing business, The Atlantic's national correspondent James Fallows answered with a resounding no. What Americans needed, he argued, was to become "more like us" (the title of his book on the subject), not more like them: America's competitive advantage was rooted in disorder, constant change, flexibility, mobility, and entrepreneurial zeal. In 1991 Robert Reich, about to become Bill Clinton's first secretary of labor, looked at the tremendous expansion of manufacturing and other export-related employment elsewhere in the world and came to a similar conclusion. How, he wondered in his book The Work of Nations, could Americans preserve and accelerate economic growth if the market position and efficiency advantages of America's largest firms came under threat? He, too, concluded that we needed to shift our focus away from old-style stable mass-production employment to high-knowledge, high-tech, high-entrepreneurship fields. Workers, he argued, should expect to go back to school to learn new skills for new industries.

But embracing change and uncertainty in this way does not come naturally, in the United States or anywhere else, and the pollsters and media-affairs people of the Clinton administration soon told Robert Reich to be quiet: people did not like to hear their government telling them that their jobs were going to vanish.

Economists rightly say that the rising wave of trade-driven service globalization will, like the last waves of trade-driven manufacturing globalization, benefit Americans and foreigners alike. At home more will be won than lost. Fears that expanding trade will destroy jobs and disrupt the economy also need to be counterbalanced by the knowledge that reducing trade—or even failing to expand it—would reduce national wealth potential, destroy future jobs, and ultimately disrupt the economy even more. The social problems of a stagnant economy are far greater than those of a dynamic one.

But economists too readily dismiss concerns about those who lose out, saying merely that they can be compensated. In practice they seldom are. The United States simply does not make the investments needed to turn economic change into a win-win process—investments in retraining and rebuilding that would transfer some of the gains from the winners to the losers (who've done nothing personally to merit their loss). In the late 1970s and the 1980s little money was spent on Flint and Detroit in particular, and Michigan in general, to cushion the economic impact as Toyotas and Hondas came to America's shores. Producers in Japan and car buyers in Boston and San Francisco pocketed the gains, while producers in the Midwest absorbed the losses. As the Princeton economist and New York Times columnist Paul Krugman puts it, free trade is a salable policy only if accompanied by a well-built social safety net and confidence in full employment. But our safety net is full of holes.

Some companies have traditionally provided many of our social services, particularly in the form of health insurance and retirement support. Those companies will not continue to sustain that burden in the future. At the same time, our limited system of government benefits will not be adequate to the changes that we'll face—leaving aside the possibility that it may be weakened or removed completely, as some politicians propose. That system was designed to protect the poor and the aged, and to tide the rest of us over in case of (temporary) job loss. What we need now is far more career-transition assistance for the middle class, and perhaps more government funding and (surely) portability for the benefits—notably health care—that the private sector increasingly fails to provide. America's economy will need flexibility in order to compete, but we can provide this protection without sacrificing our flexibility.

Because we are facing an economic transformation that will hit not over the course of a few years but over the course of the next generation, we have time to do what needs to be done. We will need all this time, because the approaching economic shock will be greater in magnitude than anything in recent historical memory.