Chapter 10
Reply: Premature Reports of Demise

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Are current employer practices qualitatively different from those of the recent past? This is the issue dividing Peter Cappelli and myself. Unlike Cappelli, I do not think that the institutions of the postwar U.S. labor market have undergone a structural transformation, certainly nothing so drastic as to warrant an obituary.

Social scientists regularly contest the nature of institutional change, as in recent debates over the nation state, Nordic corporatism, collective bargaining, and superpower hegemony. Typically the debaters divide into two camps. On one side are the saltationists: those who see institutional change representing a break or rupture with the past. Here there is fascination with punctuated equilibrium models and other metaphors of discontinuous change. On the other side are the gradualists: those who see change occurring adaptively and being accommodated by existing institutions.[1]

Each side in these debates has its virtues and vices. The gradualists are sensitive to structural continuity and to path dependence, although this breeds a conservatism that causes them to miss historical turning points. The great neoclassical economist, Alfred H. Marshall, was a gradualist whose marginalism caused him to declare "Natura non facit saltum" (nature makes no leaps). The problem is, sometimes it does. Saltationists are alert to these transitions and quick to see fresh patterns. They also, however, have a tendency to give recent events more weight than a long-term perspective would warrant. There lies the nub of my differences with Cappelli (this volume).

To understand my position, we need to go back to the late 1960s, when economists concerned with poverty developed a labor-market taxonomy known as the "dual labor market" model. In this model, the secondary sector was comprised of jobs that were easy to learn, paid relatively low wages, and offered few rewards to tenure. Some of these were full-time jobs; others were part-time or temporary positions. Secondary workers were disproportionately young, female, and nonwhite, with high turnover rates (Doeringer and Piore 1971; Edwards et al. 1975).

The primary sector was the *locus classicus* of the internal labor market, characterized by use of administrative principles to guide labor allocation and by strong attachments between employers and employees. These attachments caused the formation of firm-specific human capital. To retain and to motivate employees, companies offered wages and benefits that rose with seniority. Incumbents were favored over outsiders for vacancies. The employment relationship was maintained over time, although the strength of the tie varied by occupational tier.

The primary sector's upper tier was composed of salaried executive, managerial, and professional employees. Except in catastrophic situations like the Great Depression, these employees had Japanese-style lifetime jobs. The lower tier was filled with hourly blue-collar, clerical, and sales employees. Their jobs offered fewer rewards to tenure than the upper tier (as in the distinction between annual salaries and hourly wages), but they did provide a fair degree of stability. The big contrast in lower-tier jobs was between those in the union sector, where income security was emphasized, and those in the nonunion sector, where employment security was more prevalent.

During business downturns, the union sector utilized a layoff-rehire system tied to seniority and subsidized by unemployment insurance and private benefits. The nonunion sector was more likely to respond to downturns by cutting hours and compensation, or by transferring employees. Because of these differences, layoff rates in the 1960s were two to four times higher in the union sector, and unionized workers were about 50 percent more likely to experience temporary layoffs. Unionized workers also were more likely to experience layoffs than their counterparts in Europe or Japan (Jacoby 1997). While permanent mass layoffs were rare during the postwar boom, they did sometimes occur. Typically unions handled them through transfers of senior members, or, if this was not an option, through a severance pay plan. Like temporary layoffs, severance plans revealed labor's preference for income, rather than job, security. As observers noted in 1960, this preference demonstrated "a basic conservatism in the American labor movement" because it allowed unions to "avoid the necessity of bargaining over such essential management decisions as production schedules, capital improvement plans, and plant location (Slichter et al. 1960).

In short, the antediluvian world had a certain structure and logic. The least stable jobs were in the secondary labor market, where weak attachments resulted in low tenure and high turnover. In the primary sector, the most stable jobs were held by managers and executives; lower-tier primary workers enjoyed many upper-tier perquisites, albeit to a lesser degree (and, in the case of unionized workers, with a greater emphasis on income security). Pay and employment levels fluctuated less than market conditions; when employers made pay and allocative decisions, they gave heavy weight to organizational factors (like seniority, equity, and morale) and not only to market considerations. Risks that might otherwise be borne by employees were absorbed by the employer.

Of course, the fact that employers operated internal labor markets in this fashion had everything to do with self-interest and not benevolence, except to the extent benevolence constituted a form of enlightened self-interest. That employers chose to shoulder risk for employees was the result of an interplay between efficiency factors (recouping investments in employees and providing incentives for employee effort); the rise of modern management (including professional personnel managers and systematic attention to employee psychology); social norms; and various external forces (ranging from union pressure to law to tax incentives).[2]

So where do Cappelli and I disagree? We differ on four main issues: the persistence of the labor market's pre-1980 structure; the manner in which this structure has adapted to the post-1980 environment; the contrast between managers and other occupational groups; and the interpretation of data.

The Pre-1980 Model

The model sketched above remains a good first approximation to the contemporary labor market. Employers in the primary sector — the focus of my essay — still face a similar set of incentives and pressures, what I referred to in my essay as the "organizational realities of managing a workforce." True, some of the underpinnings to internal labor markets have grown weaker, notably labor unions. However, there also are new forces that are raising the return on employee retention. The economy increasingly is being driven by competition based on creativity, skill, and relationships. While some companies are content to cross-fertilize an industry through the turnover of skilled employees, as in parts of Silicon Valley, most employers prefer a proprietary approach. Hence they make strenuous efforts to manage and retain their intellectual capital (Pfeffer 1998; Stewart 1997).

To reduce the cost of these efforts in a riskier world, employers rely on a core-periphery model, in which secondary jobs — temporary, part time, and others — are used as a buffer to stabilize core jobs and as a screening device to select future core employees. Secondary workers are employed by outside contractors or by the primary employer (a distinction that has legal ramifications, as Microsoft recently discovered). These new forms of sectoral articulation are a change from the older version of autonomous dual markets. However, they are consistent with the preservation of career-type jobs.

How large and persistent has been the growth of secondary or nonstandard positions? Cappelli and I agree that nonstandard jobs have not been growing since the mid-1990s. Where we differ is in our assessment of their growth before then. Currently, of the roughly 30 percent of the employed who hold nonstandard jobs, over two-thirds are part-time workers, a group whose share of employment has not changed since the early 1970s. The remainder consists of workers in "alternative employment arrangements": independent contractors and consultants (6.7 percent); on-call workers (1.6 percent); temporary help workers (1 percent); and workers provided by contract firms (0.6 percent). This is a motley group. The independent contractors and consultants are relatively educated; one-third possess college degrees, a higher proportion than traditional workers. Only 4 percent consider their jobs likely to last for less than a year and 84 percent prefer their arrangement over a traditional job. Workers provided by contract firms resemble independent contractors; they tend to be educated and consider their jobs to be stable. On the other hand, temporary help workers and on-call workers are disproportionately young, female, and less educated. Most do not think their jobs will last and nearly 60 percent would prefer a traditional job. Thus an upper bound on the increase since the 1970s of nonstandard jobs that are undesired and unstable is less than three percent of employment, a change but not a sea change (USBLS 1997, 1998b).

Adaptation not Extinction

It is true that the economic environment is different now than in the 1970s, due to technological innovation and the intensification of domestic and global competition. However, the new environment has not led to the death of internal labor markets and long-term jobs, such as they were (and are). Rather — and this is the central point of my essay — internal labor markets have adapted to change by shifting risk and uncertainty from the firm to the employee. Employees today are bearing more risk — including the risk of job loss — but are doing so within structures that have remained stable over time. When we look at the kind of workers who held primary jobs in the past — adult high-school and college graduates — the proportion reporting more than ten years' tenure with the same employer was 42 percent in 1979 versus 37 percent in 1996. Despite job losses and restructuring since 1980, long-term attachments are only slightly less prevalent today (Farber 1997b).

Real wages have declined for some workers, especially the less educated. However, this in itself is not inconsistent with a world of long-term jobs and risk-sheltering by employers. In fact, to a degree the two phenomena are related: Some workers have traded (or been forced to trade) lower real wages for job security and the maintenance of benefits; other workers — particularly managers, a point I will return to — have enjoyed rising wages at the expense of job security and some job-related benefits. The real paradox of today's labor market is the coexistence of job loss and long-term employment, sometimes within the same organization. This causes job losses to have a ripple effect, making survivors work harder and worry more. However, the survivors, while bearing more risk, continue to hold long-term jobs whose pay and working conditions remain heavily influenced by organizational considerations.

Managers and Other Occupational Groups

Cappelli gives a lot of weight to the experiences of managerial and executive employees. In fact, his argument about the death of career jobs is really about the collapse of job security for managers, and his evidence of a shift from organizations to markets is weighted heavily to managerial phenomena, such as executive compensation and careers.

Without doubt, managerial work has changed drastically in many firms. Much of the decline in aggregate job stability in the 1980s and 1990s was concentrated among long-tenure males in managerial occupations. Prior to those years, managers were an extremely privileged group. In large companies, they had Japanese-style lifetime employment, generous perquisites, and insulation from market forces. As William H. Whyte observed in 1956, the Organization Man believed "his relationship with The Organization is to be for keeps" because if he was "loyal to the company . . . the company would be loyal" to him (Jacoby 1985: 279). It's not an accident that Whyte wrote his book in the 1950s. The multidivisional or M-form model took hold after World War II, bringing with it an enormous demand for middle managers to hold together increasingly complex and differentiated corporations. The 1950s also saw American companies become increasingly multinational, with a rising rate of foreign investment and consequent need for managerial expertise. At the same time, there was a scarcity of talent. MBA programs had not taken off yet, and the cohort born in the Depression (who were graduating from college in the 1950s) was relatively small. As sociologist Glen Elder has shown (1974), these children of the Depression were obsessed with security, and big American companies were happy to provide it. The result was a golden age for American managers. To some extent the party was paid for by shareholders, who had ceded power to managers. Writing in 1959, Adolph Berle called this "power without property" and dubbed it "a new development in American political economy" (1959).[3]

In the late 1980s, there was a sea change for managers. Managerial hierarchies were gutted as mergers, information technology, and corporate decentralization reduced the need for middle managers. Further down the hierarchy, self-managing teams took the place of first-line supervisors. Meanwhile, MBAs graduating in the 1980s were a different breed, too young to have been touched by the depression and different in other respects from their elders (Mills 1987; Osterman 1996). They were drawn to expanding sectors like Silicon Valley, Wall Street, and management consulting —

places where the upside pay potential was high but where careers were more market oriented than under the postwar model.

Nevertheless, recent evidence indicates that the corporate pendulum is starting to swing back to a concern with managerial retention and development. In most big companies, managerial downsizing is now a fait acccompli. That fact, coupled with tightening labor markets and shifting demographics, is causing a new shortage of managerial talent. "Brain Drain," the cover story of a recent issue of *Business Week* (1999), explains that with the leading edge of the baby boom generation nearing retirement, companies are "moving decisively to hang on to their most experienced workers," including executives over fifty, a group that "until recently was being rushed out the door."

What about nonmanagerial occupations? This is a huge and diverse group, including blue-collar jobs; service and sales positions; semiprofessionals like technicians, teachers, programmers, and nurses; and traditional professions such as law, engineering, and accounting. Most of these occupations remain situated in internal labor markets. While these jobs were never as stable as managerial positions, they were hardly a spot market. In 1979, before restructuring got under way, the proportion of blue-collar workers with tenure over ten years was precisely the same as it was for managers (46 percent); clerical employees were only slightly lower (39 percent; see Farber 1997b).

The big change for blue-collar jobs came in the early 1980s, when there was a wave of layoffs and plant closures that caused enormous pain in affected communities. However, the contraction of blue-collar jobs failed to receive the sort of publicity that occurred a decade later when managerial jobs were on the block. As I have written elsewhere, "only in the 1990s, when professionals and managers were the ones at risk, did the politically influential middle class begin to feel threatened and the media take notice." Another reason blue-collar layoffs did not attract more notice was their consistency with labor's earlier decision to favor income security over job security. As a former Steelworkers official admitted in the early 1980s, "We may have backed ourselves into a corner by settling for income security rather than dealing with the immense complexities of fashioning job security arrangements." (Jacoby 1997: 257, 261).

Since then, however, unions have painfully shifted their emphasis to job security, while U.S. manufacturers have made an equally painful transition to quality production. Now there is a new regard for high-performance work practices such as self-managed teams, job rotation, and problem-solving groups. The use of these practices increased rapidly in the 1980s and 1990s. Cappelli is skeptical that such practices are leading to greater training investments and that they require enhanced employment security. However, recent studies by Paul Osterman and others find training investments to be substantially higher in establishments utilizing high-performance practices.

Moreover, use of these practices is associated with having fewer contingent employees and less outsourcing. That is, high-performance practices solidify the jobs of core employees, sometimes at the expense of managerial positions. Companies adopting these practices have fewer managerial employees and their managerial ranks grew at a slower rate in the 1990s. This is one reason why, since the mid-1980s, blue-collar job displacement rates have steadily dropped while those for managers have steadily risen (although managerial rates remain at levels well below those of manual workers; Cole 1999; Osterman 1999; Erickson and Jacoby 1998; Kletzer 1998).[4]

In service and sales occupations, mobility patterns and job-security measures both show that internal labor markets are being preserved, even as pay becomes more differentiated by market segment. While such occupations continue to have lower tenure levels than managerial positions, they are relatively stable. The fraction of sales and service workers with tenure over ten years held steady between 1979 and 1996, unlike managerial tenure (Batt 1999; Frenkel et al. 1999: 105–6; Farber 1997b).[5]

As for the fast-growing semiprofessional and technical occupations, their skill and education levels are helping to drive the economy. Yet as sociologist Charles Heckscher (1988) points out, "they are semi in that their status is bound up with their place in a particular company, not with universal standards that go beyond the firm" (69). That is, their skills are partially firm-specific and this fact, combined with high demand for their skills, has kept their displacement rates since 1981 lower and less variable than for managerial employees (Kletzer 1998; Frenkel et al. 1999).[6]

Tenure Data

I agree with Cappelli's (this volume) assessment that the "findings of declines in tenure are modest." His caveat — that many of these studies are comparing tenure in the recessionary 1980s to tenure in the expansionist 1990s — does not apply to most of the studies we cite, which either use pre-1981 basepoints or adopt sampling and other controls for business-cycle effects. His second caveat is that rising tenure for women is not due to changes in employer policy but is a statistical artifact: the result of more women not quitting their jobs when they get married. However, the fact is that the rise in female tenure, although modest, is robust and persists even when demographic controls are applied to the tenure data. One of the major growth areas for corporate welfare activity in the 1990s has been "work and family" programs that attempt to accommodate women's career aspirations by making it easier for working women to be mothers. Employers have been spurred to do more in this area partly as a result of the 1993 Family and Medical Leave Act, although efforts started before then. The programs can be faulted for delivering less than they promise, but they are more than fluff. Hard dollars are being spent on flexible spending accounts that reimburse employees for childcare expenses, on greater amounts of paid time for personal and sick leave, and on direct childcare (although this is less prevalent than other programs). The evidence shows that these expenditures are affecting women's career decisions (Hofferth 1996).[7]

Job Attachment Data

True, tenure tells only part of the story and we need to look at other data from which we can infer job attachment. The problem is that these data are more ambiguous than the tenure data. Studies based on the CPS show stability of retention rates over the 1980s and early 1990s; those based on panel data are more diverse, with some showing a decline in retention rates and others no evidence of change. Another approach is to separately examine involuntary and voluntary (quits) mobility. One would expect a rising proportion of involuntary separations to make workers feel less secure, even if total separations have not changed. Here too, some studies find increases over time in the proportion of separations that are involuntary; others do not.[8] One could attribute the lack of consensus to the shortcomings of labor economics, or conclude, as I do, that the findings are ambiguous because changes in job attachment have been modest.

Other studies look at job loss rates using data from the Displaced Workers Survey. The DWS is problematic because there have been changes over time in question wording and survey design. In his analyses of the data through 1995, Farber (1997a, 1998) has made heroic efforts to control for these problems. Farber finds that, until the 1993–95 period, adjusted job loss rates had a strong cyclical pattern, rising during recessionary periods (1981–93, 1989–91) and falling during expansions. The only exception is 1993–95, when job loss rates failed to decline despite the beginnings of what has become a sustained expansion. If Cappelli is right, then the mid-1990s mark the start of an historic shift in job-loss patterns. However, it is also possible that the huge job losses of the mid-1990s were one-time events not likely to recur. The mid-1990s recovery was exceptionally feeble; unemployment barely fell and productivity was weak. Only after the mid-1990s did the expansion pick up steam. Indeed, the most recent DWS data show job displacement declining since the mid-1990s. While the number of displaced workers is not small — 3.6 million individuals from 1995 to 1997 — it is 15 percent lower than the number displaced in 1993–95. Also, reemployment is occurring more quickly than in the mid-1990s, as one would expect given the recent strength of the labor market.

We do need to supplement these aggregate data with analyses of particular firms, both those that are downsizing and those that are expanding. On the former, the Watson Wyatt data on large companies with shrinking employment finds no evidence that mid-career employees have been singled out in downsizing decisions. Consistent with the logic of internal labor markets, the impact of downsizing is still borne by junior workers, and there is no evidence that firms are substituting junior for mid-career employees. Moreover, these large but downsizing firms continue to have higher retention rates than the labor market average. "From a purely statistical standpoint, a worker in the early 1990s had higher odds of staying with [a shrinking firm in the Wyatt sample] than they would have had in any job picked at random." (Allen, Clark and Schieber 1999).

As for companies with job gains, the Wyatt data show that these firms had higher retention rates than those that were shrinking — not only for junior employees but also for those with substantial seniority (over twenty years) — a finding that suggests that internal labor markets are enduring. True, some of these companies are privately held, which gives them freedom to do things that other firms can not. However, ownership is not destiny. There are plenty of publicly held growth companies oriented to employee retention. Even in the high-technology sector, such firms — like upstart Inktomi and giant Microsoft — pride themselves on being "sticky" employers (at least of their core employees). Furthermore, publicly held companies sometimes offer more security and risk sheltering than do private companies. David I. Levine et al. (1999) point out that Wal-Mart's 910,000 employees are "buffered from the external market in ways similar to the traditional internal labor market, particularly as compared to the Mom & Pop stores they displaced."

Pay Data

Not only stable employment, but wages that rise with seniority are another characteristic feature of internal labor markets. The single most comprehensive study of returns to tenure finds that these returns not only have persisted over the period 1975–91, but have actually risen slightly. The picture for young workers is mixed: returns to tenure have fallen for those holding jobs less than eighteen months but have risen for those holding jobs for nineteen months or more (Altonji and Williams 1997; Bernhardt et al. 1998, Teulings and Hartog 1998).[9] Other types of market-sheltered wage practices also are not eroding. Employer wage premiums have remained stable in the 1980s and 1990s. Also, the compensation practices of large and small firms are at least as different in the 1990s as they were in the late 1970s. Big firms continue to pay more and their occupational wage structures have not converged with smaller firms. All of this suggests the continued existence of pay structures based on organizational considerations (Levine et al. 1999; Belman and Levine 2001).

It is true that there has been a movement in recent years toward basing pay more heavily on individual and organizational performance. However, the shift has been monetarily most important for managers. For nonmanagerial employees, performance-based pay, while more prevalent, still affects only a tiny fraction of total compensation. Conversely, job characteristics remain an important determinant of pay. Wage inequality among people with the same job title in the same organization changed very little in the 1980s and 1990s. Also, the use of formal job evaluation plans has increased over the last five years, further evidence that job characteristics still matter for pay setting (Levine et al. 1999).

Conclusion

Most adults continue to be employed in long-term jobs situated in internal labor markets, although they are more exposed to market forces than thirty years ago. Shifting risk to employees is a sign that internal labor markets are adapting to a more turbulent environment, not that they are dead. Managers and executives have experienced major changes in career patterns and pay practices, more so than other groups. To what extent those changes will endure in coming years is, however, an open question.

None of this is to deny that segments of the labor force are experiencing leaner and meaner arrangements. Risk-shifting may sound bland but it does mean more uncertainty and stress for affected employees. For now, the tight labor market has taken the edge off these changes. The general mood is optimistic, much as in the late 1920s, when overall prosperity was combined with sectoral dislocations and risk-shifting in response to market turbulence. Hopefully, history is merely rhyming and will not repeat itself.

Notes

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1. See, for example, Ohmae (1995) versus Wade (1996); Lange et al. (1995); Erickson and Kuruvilla (1998); Brilmayer (1994) versus Steel (1995).
2. On the rise of internal labor markets, see Jacoby (1985).
3. See Chandler, (1962); Tsurumi (1977).
4. One of Osterman's troubling findings is that use of high-performance practices in 1992 is positively associated with higher layoffs five years down the road, except in unionized establishments. Yet more research needs to be done on this important issue, because the model can't tell whether the layoffs are a result of productivity gains being appropriated by nonunion firms or of declining sales for those firms.
5. The picture for clerical jobs is decidedly mixed: job losses and insecurity for some; higher skill levels and new opportunities for others (Herzenberg et al. 1998).
6. One might argue that the relevant approach is not to look at occupations but at education levels. Yet long-term jobs (over twenty years) are as prevalent for those with twelve or fewer years of education as they are for those with baccalaureate and advanced degrees. Cutting the tenure data at 10+ rather than 20+ does show college graduates being more likely than the less educated to hold long-term jobs. However,

the same advantage existed twenty years ago, before the turmoil in the labor market. Similarly, four-year job retention rates fell in the 1980s for high-school dropouts and high-school graduates relative to college graduates, but ten-year retention rates for college graduates showed a slight decrease relative to the less educated (Farber 1997b; Diebold et al. 1997).

7. Earlier that year Motorola announced that it was opening onsite childcare centers at several of its semiconductor manufacturing plants (*Wall Street Journal*, 1999).

8. For a review of these studies, see Allen et al. (1999) and Bansak and Raphael (1998).

9. The Chauvin study cited by Cappelli is based on manufacturing managers during the period 1979–83, not the best sample for assessing aggregate or long-term trends.

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