

What Changed in the 1980s and Why

Quick Summary

The 1980s will be recorded by economic historians as the decade the postwar social contract broke down. A look back at Figure 1-2 shows this vividly. Wages have flat-lined since then. Nothing has yet replaced the broken social contract.

So let's look at what and why these changes happened in the 1980s, again with an eye toward what we might learn for shaping the future.

The place to start has to be with changes in the environment of firms and workers that were unfolding, whether or not they were recognized clearly by those shaping workplace practices at the time. Here's a list for starters. Each of the forces mentioned here continue to be with us today and have to figure into our own efforts to shape the future of work.

Globalization

The post war social contract thrived in an era when the American economy was growing steadily and U.S. firms were dominant competitors in most other countries around the world. This changed dramatically in the early 1980s and continues to be the case today. America went from having a consistent positive balance of trade (dollar value of exports exceeded the dollar value of imports) with other countries to experiencing a persistent trade deficit. Nowhere was this more apparent and impactful than in manufacturing, and particularly in key manufacturing industries such as autos and steel. In the early 1980s the value of the U.S. dollar rose dramatically relative to other currencies, and especially relative to the Japanese Yen. This corresponded with a rapid influx of Japanese autos, steel, electronics, and other goods into U.S. markets. Indeed Japan had improved the quality of its manufacturing products and the productivity of its manufacturing processes to the point where the "Japanese model" became the benchmark for manufacturing in the 1980s. While the Japanese economy faded (badly) in the 1990s, by that point other lower cost developing countries—Korea, Mexico, Indonesia, Malaysia, and then most importantly China took over as havens for outsourcing U.S. manufacturing.

The effect, in the 1980s and continuing to today, has been the loss of over half the nation's manufacturing jobs and equally importantly strong downward pressures on wages of any work that could potentially be outsourced to another country. The implication going forward as we think about the future of work is obvious: Today and in the future we must assume that much of economic activity is global, not just national, in scope.

Technology: “It’s People Who Give Wisdom to the Machines”

In the eighteenth century, it was the British Luddites who took clubs to the mechanical looms that were replacing them. In the 1960s, it was the fear that “automation” would produce massive permanent unemployment. In the 1980s, futurist Jeremy Rifkin predicted that technology would bring the “end to work.” We hear some similar warnings today as the digital economy advances. So while there is no shortage of warnings and predictions that the end of work is near (only to be consistently proven wrong), there is little doubt that advances in information technology and machine intelligence, perhaps along with advances in the life sciences, will profoundly change the demand for labor in the years ahead and will continue to lead to a decline in jobs for workers that machines can and will do.

But it is important to recognize that technology is a not a deterministic force. If used creatively it can be a complement (i.e., a force that supports) to work rather than a pure substitute for human labor. The best way to bring this lesson home is to look at the experience General Motors had in coping with automation in the 1980s. This lesson only cost them \$50 billion, in 1980s dollars no less! The story goes as follows.

In 1979, NBC ran a documentary called “If Japan Can Do It Why Can’t We?” Essentially the program reported on the Japanese success in building higher-quality automobiles with fewer work hours (higher productivity) than their American counterparts. GM decided it would step up to meet this challenge. Its solution: automate operations to get rid of costly UAW labor. It pursued this path with gusto in the 1980s, spending a reported \$50 billion to install robots and other forms of advanced automation in selective factories. I visited two of their most highly automated factories, one in Wilmington, Delaware, and one in Hamtramck, Michigan. In both plants one could see that the strategy was not working well. There were too many robots standing idle and too many vehicles in the repair bay at the end of the assembly process waiting for something to be fixed before they could be shipped. Two little vignettes pulled from my notes on those plant visits tell the story.

On a tour of the plant our guide points out with considerable pride a walled-off area he describes as the “\$5 million room.” Once inside the room we saw two work stations, each with a set of lasers beaming at door panels that had come in from external suppliers for inspection for “dimensionality”, i.e., to see if they fit within all specifications. Attached to each laser work station was a computer monitor and an operator. I asked the operator to describe what he was doing.

“See all the data on my screen. Those numbers tell me whether or not the doors we get from our supplier fit our specifications in all dimensions. This is great stuff. Before we had this technology I used to always get into fights with the guy I talked to at the supplier. I’d say a part wasn’t right. He’d say it was ok when it left their shop and off we’d go. Now we have the same numbers and equipment so there’s no debating.”

I asked: “If they have the same technology and can produce the numbers and check the quality, why do you need this technology here? Aren’t you duplicating what they are doing?”

His answer: “Yeah. But it’s simple: They lie!”

Then, as we moved on with our tour of the assembly line and watched how these high-tech-tested doors were fitted onto the cars, I noticed (and our tour guide was considerably embarrassed to see) that the workers had rubber mallets in their hands and were gently pounding the door frames into place. Apparently this traditional “technology” was still needed to fix imperfections in fit that remained despite the high-tech investments and checking!

A short time later, I toured a Japanese assembly plant located in the United States and asked our tour guide how they tested the same panels for proper dimensionality.

“We don’t do that. We assume the supplier got it right. That’s their responsibility. We worked with them at the start until we were confident in their ability.”

I asked: “You mean you don’t have a \$5 million room with lasers?”

His answer: “We’ll let our competitors have that technology.”

These two vignettes explain why, despite its \$50 billion investment in new technology, GM remained the high-cost auto manufacturer at the end of the 1980s. Careful studies by MIT students John Krafcik and John Paul MacDuffie have documented that the highest levels of productivity and quality in auto assembly plants worldwide were ones that carefully integrated work force training, employee involvement and teamwork, and flexible work systems with investments in new technologies. They embodied the Japanese phrase that it is “workers who give wisdom to the machines.”

This same finding has now been replicated with respect to investments in information technologies in service and manufacturing industries. Erik Brynjolfsson and colleagues studied the effects of investments in information technology across industries in the 1990s. Their results showed that the biggest returns to IT were realized in organizations that combined these investments with innovations in work processes that complement the new technology. Similarly, Adam Litwin found the same results in his study of how different clinics at Kaiser Permanente implemented and used electronic medical records technologies.

The Lesson: IT or other advanced technologies don’t stand alone or apart from the people who will use them. Involving the people who will ultimately use them in the design, deployment, and ongoing use of the technologies and adapting work practices in ways that complement these new systems makes the technologies pay off.

The Financialization of Corporations and its Effects

Private sector firms, by definition have always pursued the goal of profit maximization. But for many years during the heyday of the post war social contract this goal competed with other values and was tempered by the power of unions demanding a share of productivity and profit growth for the workforce. This changed dramatically in the 1980s and has not rebounded since then. We can best tell the story of how and why this changed by looking back on how the pressures on CEOs changed over the course of time from the 1960s to today. Indeed, we will start the story with the 1949 graduating class of the Harvard Business School.

The Harvard Business School class of 1949 has been acclaimed for producing an exceptionally large and impressive number of business leaders who dominated and shaped business norms over the next three decades. Many were first-generation college graduates, although the usual cadre of elite or legacy admits was present in the class as well. The combined experiences of growing up in the Great Depression and serving in World War II appeared to have had profound effects on this cohort of future business leaders. Their sense of community and responsibility, perhaps along with the balance of power that came from the strength of the labor movement, led them to see their responsibilities as CEOs as more than maximizing short-term earnings.

Peter McColough was the CEO of Xerox Corporation from 1968 to 1982. Perhaps as much as anyone, McColough exemplified the type of leadership that supported and reinforced the postwar social contract. He played an active leadership role in community affairs in Rochester, New York, where the company was headquartered, and in national political and government advisory roles; he built strong and positive relationships with the union that represented Xerox manufacturing workers; he led other companies in initiating total quality and employee involvement processes in partnership with the union in the early 1980s; and, perhaps most importantly, as early as 1968 he initiated an affirmative action program that made it possible for women and minorities to rise to a wide range of executive leadership positions at Xerox. It is no accident that in 2002, Ann Mulchay was named CEO of Xerox and that in 2009 she was succeeded by Ursula Burns, the first African American female CEO of a Fortune 500 firm.

The foreword to a book about this leadership cohort by the former editor of Forbes Magazine summarizes their views and offers a ringing indictment of the generation of CEOs that succeeded them in the 1980s and beyond.

As I write, it is midsummer 2002. The business and Wall Street people who are in the news today seem a sorry lot compared with most of the [class of 1949]. When I say “sorry lot,” I am not just talking about the Ken Lays, the Bernie Ebbers, the Jack Grubmans [CEOs who went to jail]. I also refer to the dozens of CEOs who destroyed corporate balance sheets during the 1990s and early 2000s. They did so by taking on short-term debt to pay for overpriced acquisitions. They went into debt to buy in their own shares at exalted prices. They showed an utter disregard for the probabilities by promising an endless string of 15 percent and more annual earnings gains. And when they couldn’t produce earnings, many of them claimed that earnings didn’t matter; only EBIDTA [earnings before interest, taxes, depreciation, and amortization] matters. Others made their stock options pay off by gutting their corporate payroll, literally making themselves rich off the misfortunes of their colleagues. All this in the name of “maximizing shareholder values.” . . .

I don’t know precisely when the term maximizing shareholder value came into common usage, but in a way I wish it never had. Too often it means using gimmicks to get your stock up. It is rarely taken to mean building a solid business that adds value for your customers and creates exciting careers for your employees.

Other CEOs coming out of this class echoed this critique of the later generation that followed them:

In the twilight of their lives, members of the class of 1949 were shocked and appalled by the corruption within the executive suites of corporate America—in companies like Enron, WorldCom, and Merrill Lynch. “There has been a diminution of values,” said Jim Burke [CEO of Johnson & Johnson]. “Greed is a very serious problem in American business.” At Johnson & Johnson Burke had been a leader in developing a strict ethical code to guide the company known as the Credo. “I saw that value system as an asset to the business, not as a constraint, but an asset.” Tom Murphy [CEO of ABC], easily one of the most respected businessmen of his generation, found the rapacious behavior rampant among CEOs hard to fathom. “It’s sad,” he said. “We were never guilty of what corporate America does today. We were oriented toward the stockholders. . . . They’ve got to put some of these white collar criminals into jail.” As many 49ers saw it, the bad behavior in corporate America was not just sad; it was also unnecessary. “Social responsibility—and expanding profitability—are not intrinsically at odds with one another,” Roger Sonnabend [CEO of Sonesta Hotels] believed. “Quite the contrary. They are two faces of the same coin.”

The managers of the post-war era were conditioned to be concerned about balancing the interests of multiple stakeholders—investors, employees, and communities. Consider the following policy statement from the Business Roundtable, a group comprised of 200 CEOs of leading U.S. companies, in 1990:

Corporations are chartered to serve both their shareholders and society as a whole. The interests of shareholders are primarily measured in terms of economic return over time. The interests of others in society (other stakeholders are defined by their relationship to the corporation.

The other stakeholders in the corporation are its employees, customers, suppliers, creditors, the communities where the corporation does business, and the society as a whole. The duties and responsibilities of the corporation to the stakeholder are expressed in various laws, regulations, contracts, and custom and practice. . . .

The central corporate governance point to be made about a corporation’s stakeholders beyond the shareholders is that they are vital to the long-term successful economic performance of the corporation. Some argue that only the interests of the shareholders should be considered by directors. The thrust of history and law strongly supports the broader view of the directors’ responsibility to the corporation or to the long-term interests of its shareholders.”

Compare the above Business Roundtable’s view with the statement the same group issued just seven years later:

In the Business Roundtable's view, the paramount duty of management and of boards of directors is to the corporation's stockholders; the interests of other stakeholders are relevant as a derivative of the duty to stockholders. The notion that the board must somehow balance the interest of the other stakeholders fundamentally misconstrues the role of the directors. It is, moreover, an unworkable notion because it would leave the board with no criterion for resolving conflicts between interests of stockholders and of other stakeholders or among different groups of stakeholders.

Like so many other institutional innovations, this one was also the product of a set of ideas. It started with a mathematical formula that was developed for pricing options by three finance professors, Fisher Black, and Robert Merton at MIT and Myron Scholes at the University of Chicago. The big effect of this invention (aside from garnering Scholes and Merton the Nobel Prize in Economics—Fisher Black died before the prize was awarded in 1997) was to make it easier for firms to develop stock options into a significant part of the compensation package for CEOs.

The power of this innovation was reinforced when other scholars, particularly Michael Jensen and William Meckling, began popularizing a "principal-agent" view of the firm and the responsibilities of the CEO. In brief, the argument was that managers had been allowed to develop their own ideas of what firms should do, apart from the interests of shareholders. Jensen and Meckling suggested that CEO compensation plans should give priority to including stock options or other means of more tightly aligning CEO incentives with shareholder interests. CEOs would then do whatever it took to boost stock prices. Since another rising theory in finance promoted by University of Chicago professor Eugene Fama (who also won the Nobel Prize for his work in 2013) argued that the price of a firm's stock was the best and most efficient indicator of the future value of the firm, financial analysts only needed to concentrate on likely movements in this indicator when advising clients about where to invest.

Along with these theories came new debt instruments—sometimes called junk bonds—that allowed firms to leverage a firm's assets and buy companies more easily, even in the face of managerial opposition. The era of hostile takeovers and equity buyouts of firms was thereby launched. Actor Michael Douglas memorialized this development with his famous "Greed Is Good" speech in his depiction of a Wall Street takeover artist in the movie *Wall Street*.

As generous and lucrative stock options were inserted into compensation packages of top-level executives, their interests shifted from promoting stable, growing firms to developing incentives to maximize short-term earnings and stock prices at any cost. Decisions to lay off employees shifted from painful, reluctant actions of last resort to proactive "restructurings" to strengthen current and or future earnings. The social norms regarding layoffs changed.

Consider the story of Stanley Tools, a venerable U.S. manufacturing company known for the high quality and durability of their products. New York Times columnist Louis Uchitelle documented how that company slowly abandoned its culture of doing everything possible to avoid laying off workers by using layoffs as a strategy of last resort during business downturns and changed to seeing layoffs as a more

proactive or preemptive move to restructure the company in pursuit of higher short-term profits. The title of his book tells the story in a nutshell: *The Disposable American*.

Changing Education Requirements

While there is no specific date that we can say serves as the birth of the “knowledge-based” economy we highlighted in our history of work video and lecture, clearly the signs were on the wall that education was becoming an even more important key to success in the job market than in earlier periods of time. In their book *The Race Between Education and Technology*¹ Harvard economists Claudia Goldin and Lawrence Katz show clearly that the income benefits to a college degree relative to a high school degree grew in the 1980s and continues to be substantial. Unfortunately, as the title of their book suggests, the growth in the number of Americans achieving a college degree slowed down since the 1980s compared to prior decades (indeed compared to most of the 20th century). This slowdown in growth of the supply of more highly educated workers combined with the increased demand for workers with high skills is part of the explanation for the stagnant wage profile and the increase in earnings inequality experienced from the 1980s to now.

So America needs to increase the opportunities for young people to get access to and to successfully complete degrees beyond high school. But more fundamental changes in our educational system are needed as well. Reforms are needed to provide life-long learning opportunities starting with access for all young children to pre-kindergarten educational programs and going through opportunities for workers to have access to educational and on-the-job training and retraining and continuing educational programs throughout their working careers. We will come back to this issue later in this course when we view a set of videos devoted to what the next generation needs to do to assure that education not only catches up with technological demands but perhaps gets one step ahead!

Triggering Events

All of these forces—global competition, advancing technologies, the shift to a financial-shareholder value view of the firm and the growing demand for highly educated/skilled workers were growing incrementally as the decade of the 1980s arrived. But it was the confluence of these pressures along with a dramatic change in the political environment that ushered in a fundamental change in U.S. employment relations.

Three events converged at the beginning of the 1980s that broke the inertia in labor-management relations of the 1970s.

1. The country replaced Democrat Jimmy Carter with Ronald Reagan, a strong-minded conservative Republican.

¹ Claudia Goldin and Lawrence Katz, *The Race Between Education and Technology*. Cambridge: Harvard University Press, 2010.

2. The economy fell into a deep recession in large part induced by Paul Volcker, a strong-minded chair of the Federal Reserve Bank who single-handedly took up the task of breaking the back of inflation, even if it meant breaking it on the backs of the American work force.

3. International competition mentioned above hit the auto, steel, and other manufacturing industries of the Rust Belt with a vengeance as the value of the dollar rose relative to the Japanese yen and the Japanese demonstrated that the goods they had to import were of high quality (and in some cases higher quality than their U.S. counterparts) and were produced at higher levels of productivity than could be achieved in the United States.

Together these three forces ushered in an era of managerial militancy in labor relations. President Reagan set the tone by firing air traffic controllers who engaged in an illegal strike in August 1981.² Private-sector employers took their cue from the president and became proactive in demanding wage concessions and implementing what came to be called “two-tier” wage agreements, i.e., setting a lower wage rate for new hires than for existing workers doing the same jobs. One estimate indicated that over 40 percent of collective bargaining agreements reached in the early 1980s involved some form of concession in wage settlements. Any relatively new hires in the auto industry today will be able to relate to this fate. They too are now working alongside their seniors, doing essentially the same work for about 30 percent less pay. History can repeat itself.

The era of pattern bargaining ended. So too did the value of the strike threat as a source of bargaining power for workers. Strikes at the Phelps Dodge copper mines, the Greyhound bus line, and the Hormel meatpacking company ended in deep wage cuts. A strike at Eastern Airlines even ended in liquidation of the company. Econometric evidence shows that overall during this period, the end result of strikes were negative and the positive effects of intra-industry pattern bargaining came to an end.

These developments created a great academic debate: Were these just temporary setbacks for labor reflecting the deep recession of the early 1980s? Would things return to normal once the economy recovered? Or was this a turning point that signaled the need for fundamental changes in labor-management relations?

History resolved this debate. There was no rebound in union bargaining power or labor-management relations when the economy recovered in the mid-1980s or when it entered a boom in the mid-1990s. The bargaining power that used to accompany the threat of a strike never returned. Yet no new sources of power came along to replace labor’s traditional weapon. The bottom line: unions and the workers they represented were on the defensive, a trend that continued long after the recession of the early 1980s ended.

The lesson: The bargaining power labor used to gain from threatening or actually withholding labor is gone, and some new sources of power are needed going forward. Simply rebuilding

² Joseph A. McCartin, *Collision Course* (New York: Oxford University Press, 2011).

unions as the mirror image of what they were in their twentieth-century glory years will not work.

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