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# The Roaring Nineties: Can Full Employment Be Sustained?

Alan B. Krueger

Robert Solow

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# BOOK REVIEWS

## Labor Economics

*The Roaring Nineties: Can Full Employment Be Sustained?* Edited by Alan B. Krueger and Robert Solow. New York: Russell Sage Foundation and Century Foundation, 2002. xlvi, 576 pp. ISBN 0-87154-817-8, $49.95.

The United States in the second half of the 1990s surprised economists by its rapidly falling unemployment rate at low and constant inflation. This book is the result of a project jointly sponsored by the Century Foundation and the Russell Sage Foundation, whose aim was to understand the reasons for this unexpected performance. The two editors chose the topics and authors and wrote a long and very useful introduction to the book, which reflects as much their own view as that of the contributors. The contributions are mostly long, leisurely articles with a wealth of data, econometric tests, and occasional speculation about the meaning of facts of the kind one mostly finds in publications such as Brookings Papers. The collection of 11 articles and a long introduction by 26 distinguished economists is an achievement, and this book is destined to become a standard reference for students of the 1990s. The writing is first-rate, and even when the reader disagrees, the book provokes thought that should lead to further research.

My one reservation about the book's organization is that finding things in it is not easy. The index is of no use, being rather carelessly prepared, the introduction gives a deep but not a quick guide to the book's contents, and the articles do not have abstracts. But taking the time to find out where each chapter's argument leads usually proves a worthwhile investment.

In the first part of the book, which discusses the time-series properties of unemployment, inflation, and productivity growth, the surprising conclusion is that the Phillips curve proved robust through the economic changes of the 1990s. One needs to correct for changes in the non-accelerating inflation rate of unemployment (NAIRU) and the rate of productivity growth, but this should come as no surprise. The key question the book addresses is this: why did the NAIRU fall, and is the new lower rate sustainable?

The first two chapters, respectively by Douglas Staiger, James Stock, and Mark Watson and by Laurence Ball and Robert Moffitt, focus on productivity growth as the reason for the fall in the NAIRU. Staiger et al. find the correlation in the data but offer no explanation for it. Ball and Moffitt suggest a long lag in the adjustment of worker aspirations to changes in the rate of growth of productivity. But if this is the explanation for the link between productivity growth and the NAIRU, one needs to explain why aspirations take so long (more than 20 years) to adjust to the rate of growth of productivity. This contrasts with the apparent consensus in the profession that adjustments of aspirations to changes in the *level* of productivity are quick. Alternative explanations based on the nature of technological progress and the behavior of relative market and non-market returns are ignored, both by these authors and by others in the volume. Thus, the evidence for the existence of a link between productivity growth and the NAIRU is a good deal more convincing than the explanations the authors offer for that link.

The "productivity miracle," starting in the mid-1990s, receives less attention in the book than the NAIRU, although I sense that as the research for this volume progressed, many of the authors probably came to the conclusion that explaining the causes and labor market consequences of the rise in productivity growth was at least as important as explaining the NAIRU. Several of the papers speculate about the reasons for the productivity growth.

A fascinating article on the role of policy by two of the most prominent economists in the thick of it, Alan Blinder and Janet Yellen, gives credit for the shift in the NAIRU and productivity growth to a combination of good fiscal and monetary policy (credible fiscal tightening and Fed "forbearance" in the face of falling unemployment) and industrial restructuring, which took place in the early 1990s. Policy also takes some of the credit for the industrial restructuring (loose regulation and dollar appreciation forcing inefficient plants to close down) and for

the fact that wage inflation did not take off when unemployment fell, although the fact that non-wage benefits (health insurance, for example) also fell contributed to falling labor costs. Both Blinder and Yellen and other authors (in particular, Stephen Nickell and Lisa Lynch) emphasize falling computer prices and fast productivity growth in the IT sector as contributors to productivity growth elsewhere.

Of course, the fact that these technologies were available to European countries, which did not mirror the experience of the United States, needs explanation. Giuseppe Bertola, Francine Blau, and Lawrence Kahn argue that although more strict European regulation may explain some of the difference, the much better U.S. performance in the late 1990s remains a puzzle. A possible reason is the change in work practices in the United States, emphasized by Jessica Cohen, William Dickens, and Adam Posen as a key reason for the fall in the U.S. NAIRU, which to my knowledge (though this is not discussed in the book) did not take place in Europe. Reforms in work practices increased flexibility within the corporation, increased product market competition, and dissipated the rents for high-wage jobs. Nickell and Lynch also emphasize this reason and, in addition, product market regulation. This contrasts with the emphasis on labor market regulation by most other contributors to this project.

Rebecca Blank and Matthew Shapiro show that the cyclical properties of the macroeconomic aggregates in the 1990s were similar to those of the 1960s and 1980s, with the interesting exception that in the 1960s labor earnings grew faster than real value added and capital, but in the 1990s they grew at the same rate. Despite this apparent sluggishness in earnings growth, James Hines, Hilary Hoynes, and Alan Krueger argue that the rising tide of the 1990s lifted all boats, in the form of more employment and more earnings at the lower end of the wage distribution.

Trade effects do not appear to attract much credit for the "fabulous decade," but George Johnson and Matthew Slaughter's chapter is a must-read for those needing an explanation of how to identify trade effects (looking at the size of trade flows is not enough). The interesting and perhaps surprising claim comes in the more speculative discussion, as an answer to the question of how open the U.S. economy is. Apparently it is 50-50 and rising in favor of openness because of trade, immigration, and foreign direct investment, a claim that may call for some re-writing of macro economics textbooks, which make the closed economy model their benchmark.

The question of immigration also arises in discussions of demographics, where the only worrying signs about the future appear to emerge. David Ellwood argues that more investment in education to improve skills or a carefully planned immigration policy may be the only ways to sustain growth, in view of the fact that increased domestic labor supply can come only from more entry of married women and older workers, who are not likely to be skilled. Katharine Abraham and Robert Shimer show that demographic changes, in particular the aging of the baby boom generation and the increased attachment of women to the labor force, may also be behind the lengthening of unemployment durations at given rates of unemployment, another change that may require rethinking of social policy on unemployment.

*Christopher Pissarides*
Professor of Economics
London School of Economics

*Reemployment Bonuses in the Unemployment Insurance System: Evidence from Three Field Experiments.* Edited by Philip K. Robins and Robert G. Spiegelman. Kalamazoo, Mich.: W.E. Upjohn Institute for Employment Research, 2001. 296 pp. ISBN 0-88099-226-3, $39.00 (cloth); 0-88099-225-5, $25.00 (paper).

Suppose you are a policy analyst and you conduct a controlled experiment testing some social program that generates benefits far in excess of its costs. What do you do next? You seek to conduct additional experiments to validate the initial findings. If those results are supportive, you may strongly advocate implementation of the program. But what happens if the subsequent experiments yield results indicating the program may be OK, but not the greatest thing since sliced bread? What do you do then? At that point, one would have to spend a great deal of effort reflecting about the experiments, their attributes, what caused the discrepancy in findings, and where to go from here.

This is precisely the situation in which the contributors of this book find themselves. The editors, Philip K. Robins and Robert G. Spiegelman, and the other contributors, Walter A. Corson, Carl Davidson, Paul T. Decker, Chris-