WORKFORCE
NARRATIVE PROJECT

Investing in Workforce Development: Defining the Business Interest

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I. Introduction

The national interest in workforce development clearly rests on the needs of different groups of workers in the labor force, and on the needs of the economy as a whole. Many workers, especially with high school or less education, have suffered stagnant earnings growth over the past three decades. The rising rate of *inequality* between skill groups in the labor market has drawn a great deal of attention recently, and workforce development is often viewed as part of the solution to this problem. But even more highly educated workers have enjoyed only modest income growth in recent years; and, in a world of more frequent layoffs and displacement in the job market at all skill levels, both more- and less-educated workers feel increasing *insecurity* as well.[1] The need for a high-quality workforce system that provides retraining opportunities even for more-educated workers is also recognized quite widely. Finally, concerns have grown not only about the well-being of individual workers and their families, but also about the *competitiveness* of our national economy, relative to newly emerging economic powers like China and India (e.g., Freeman, 2007). Generating a highly skilled workforce with sufficient scientific and math skills is viewed by many as essential for maintaining our nation's competitiveness vis-à-vis these other countries.

But what is the business community's own specific interest in workforce development? Do employers have major needs in this area that have not been met by the nation's workforce system? If so, how frequently is this true? And why has the business community not been more vocal about the need to improve the workforce system, and not invested more effort and political capital to improve it?

Below I consider the business community's interest in the quality of our workforce development system. I will argue that the employer community has a strong interest in its quality, but that for a variety of reasons they haven't made these interests a top political priority. I then consider how the business community's interests might be addressed more explicitly by workforce development advocates, and how employer involvement with the workforce system might become more active and effective.

II. The Interests of Business in the Workforce System

No matter what their size, location or sector of the economy, U.S. businesses must make an important set of decisions in the areas of employment and human resources. First, they must decide on the mix of employees that they want at different skill levels. They must also choose what wages to pay, how to fill vacant jobs with productive workers (through recruitment and screening), and whether/how much to invest in worker

[1] For evidence that, even among college graduates, income gains have been concentrated among the very top earners in recent years, see Piketty and Saez (2003). For evidence on the growing frequency of job displacements at all levels of education see Farber (2006). This viewpoint is also stressed in recent books by Louis Uchitelle (2006) and Jacob Hacker (2006).

productivity through on-the-job training, either through formal instruction or informal learning and work experience.[2]

Recent labor market developments create a new context in which these decisions are made. New technological advances have been "skill-biased," in the sense that they reduce employer demand for less-skilled workers and raise it for more-skilled workers. The growth of "globalization" and international trade have added to this development, and raised competitive pressures on all businesses to be more efficient - by employing workers who are either more productive or less costly (or both).[3]

Newer technologies and globalization might increase competitive pressures on companies to increase performance and/or reduce costs, but they also generate more options for employers on how to do so. Recent analyses suggest that, even within fairly narrow industry segments, firms have a fair amount of leeway in choosing *how* to be competitive – i.e., whether through low wage and benefits costs or through lower turnover, higher productivity and higher performance (sometimes referred to as the "low road" and "high road" of human resources policies respectively). Their choices in this regard may well reflect personal philosophies of owners and managers, institutional networks, availability of technical assistance, or the presence of collective bargaining at the firm. [4]

But why should the quality of the nation's *public* education and workforce development system affect employers' abilities to meet their *private* employment needs – especially if their skills needs are not minimal, or if they are choosing at least a somewhat "higher road" strategy?[5] For one thing, the ability of employers to find skilled workers and even invest in training depends on the supply of general skills that workers bring to firms, which in turn reflects the education and training system that produces these skills. If the educational "pipeline" and training system is weak, it will be harder for employers to find workers who either already meet their skill needs or are worthy of additional training investments. [6]

More generally, when the needed skills are in short supply, relative to the demand for them in the market, employers will have to pay higher wages and benefits to recruit and retain skilled workers, or to invest more of their own resources in training. The *private costs* to businesses of generating and retaining skilled employees thus rise when

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[2] Newer economic models that highlight personnel decisions of firms can be found in Lazear (1995). Economic evidence on recruitment and screening practices, and their impacts on firm outcomes, can be found in Bishop (1993) and Holzer (1996), among many other sources. Recent evidence on job training can be found in the papers published by Polachek (1999).

[3] Levy and Murnane (2005) emphasize the role of technological change in replacing less-skilled labor in the middle of the wage distribution. For the role of international forces on labor markets see Freeman (2007).

[4] See Appelbaum *et al*. (2003) or Andersson *et al*. (2005).

[5] While "high road" and "low road" might be useful summaries of different employer viewpoints on labor issues, the reality is more complex – with a continuum of possible employer responses along many dimensions of worker pay, promotion and protection issues.

[6] This implies that the general skills that workers bring to any given employer, and the more specific skills for which employers might train on the job, are "complements" rather than substitutes.

the *public* system of generating skills is weak. Alternatively, they may need to live with high turnover and/or poor worker performance if they do not pay these high wages. Absent a strong workforce system that generates a ready supply of skilled workers, these tradeoffs become particularly acute during periods of tight labor markets, as many employers discovered during the boom of the late 1990's (Holzer *et al*., 2006). And, during periods of time when imbalances (and therefore shortages) develop between employer demand in certain sectors or occupations (like nursing, machinists, skilled construction contractors, and the like) and their supply, the costs to employers of filling their slots will be even higher.[7]

Furthermore, a company's willingness to invest its own resources in training will depend importantly on the extent to which the skills it needs are "general" or "specific" to the firm. The more general are the skills, the more reluctant employers will be to pay for these investments in worker training (Becker, 1993). This is true because, with general skills training, the workers whom they train might then leave for other jobs, allowing other employers to draw the returns on their investments. In reality, the gap between general and specific skills might not really be so clear-cut, implying that the employer decision might be somewhat more ambiguous than the original theory suggested.[8] Nevertheless, employers may refuse to invest their private resources in fairly general employee skills on their own, which constitute a "public good" for other employers in their industries or local areas; and thus the need for public support of this training (or its direct public provision) rises.

A variety of other labor market "failures" also limit the ability of employers to make the appropriate (or "optimal") employment and training decisions on their own. For one thing, it is widely recognized that information among both employers and workers is limited. Informal networks play a huge role in how workers are "matched" to employers (Granovetter, 1974; Ioannides and Loury, 2004); if some quite highly-skilled or potentially productive employees lack access to these networks, employers may miss the ability to hire some potentially strong employees. Similarly, employers who lack information about worker quality or their previous training might either over- or underinvest in new training at the time of hiring (Acemoglu and Pischke, 1999). Workers and employers might also underinvest in training for general skills in other circumstances – e.g., if wages are "rigid" or firms are constrained in terms of liquidity.[9] In all of these instances, public support for employer workforce behaviors – through financial assistance, technical assistance, or direct provision of information and skills – might be needed to offset the market forces that tend to limit private employer activities.

In fact, all of these factors imply a strong need for a public workforce system that responds directly to employer skill needs, especially in local areas – by providing

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[7] Most economists view shortages in particular occupations as short-run phenomena, as long as wages are free to rise and attract new workers to these occupations. But, where education and training requirements for these jobs are not negligible, this "short run" can persist for some time.

[8] See, for instance, Barron *et al*. (1999) or Acemoglu and Pischke (1999).

[9] "Rigid" wages imply that employers cannot reduce worker wages to help finance their on-the-job training. "Liquidity constraints," especially for smaller employers, suggest that firms are resource-strapped in the present and cannot always borrow from their future profits to finance training today. See Lynch (1994).

information about available job candidates to employers (and vice versa), resources for training where the supply of skilled workers in specific occupations is short, direct links between employers and the educational system to make sure the training occurs, technical assistance for those employees who train on their own, etc.

Of course, the system generated by the Workforce Investment Act (WIA), with its heavy reliance on business-led local workforce boards for the distribution of training funds, was designed to meet exactly these needs. Whether is does so successfully might remain a topic of some debate, as we discuss below. And where the unmet hiring needs in particular sectors remain persistent, and the "mismatches" between vacant local jobs and available less-skilled workers remain too high, an additional set of approaches might be needed to help bridge the existing gaps between labor demand and supply. These mechanisms might include "sectoral" training initiatives and other efforts of local "intermediaries" to provide job placements, skills and other supports (transportation, child care, etc.) to workers, while assisting employers in the development of human resource policies that will help them attract and retain additional workers.

Also, the seriousness of employer skill needs and their difficulties meeting them privately will vary across industries, geographic areas and employers. For instance, the average training levels required of employees is much higher in some sectors (like construction) than in others (like retail trade and personal services), implying different burdens on employers in meeting skill needs. Smaller employers might especially lack the needed information and liquidity to provide appropriate training to their workers (as well as the visibility and resources needed to effectively recruit and screen); and those in smaller metropolitan or rural areas might also have greater difficulty having their needs met by the local supply of workers. In some sectors, unions may help provide apprenticeship programs and training, though they limit human resources practices and flexibility in other cases. Overall, the number of sectors and geographic regions in which employer skill needs will be both serious and difficult to meet is likely to be substantial.

Furthermore, some new economic developments over the next few decades will likely affect employer workforce needs and their choices, though in ways not yet clear. On the one hand, the retirement of "Baby Boomers," and their replacement with less-educated immigrants, will generate more job vacancies and unmet skill needs among employers (e.g., Damico and Judy, 1997; Aspen Institute, 2003). On the other hand, the growth of new technologies, immigration and especially foreign outsourcing will, all else equal, have the opposite effect: by making much less well-paid workers in China, India and elsewhere competitive with U.S. workers, employers will have a much easier time meeting their labor needs, and worker wages will suffer (Freeman, 2007).[10]

The above discussion suggests that the forces of globalization may help solve employer difficulties, and enable them to forego the costs and expenses of training their own workers. Of course, the magnitude of foreign outsourcing to date has been quite

[10] Note that, while new technologies generally are labor-saving, they tend to reduce labor demand in some occupations and raise it in others. On net, technological change tend to raise demands for skills, but the impacts across specific firms or industries vary quite a bit. See Levy and Murnane (2005).

limited (Schultze, 2004), suggesting these claims might be oversold. The parts of the workforce that are even potentially affected by outsourcing might constitute 10-15% of the total (Bardhan and Krol, 2003) – not a trivial amount by any means, though not a tidal wave either.

And, in sectors or areas where employers cannot outsource their work (and also cannot meet their hiring needs through technology or immigration), workforce needs will remain serious. The clearest cases of these unmet labor needs are in the health care and elder care sectors, where demand for workers will rise dramatically over time while employers are constrained (by third-party payers) in their abilities to raise pay and benefits in order to attract more workers (Stone and Weiner, 2001). In other industries with a strong "home bias" in production – such as construction, transportation, and a variety of services (Mann, 2006) – the retirements of Baby Boomers will also likely strain the abilities of employers to find skilled workers.[11] For these many employers, the business interest in workforce development will remain strong, despite the growing options provided by "globalization".

III. Why Doesn't the Business Community Fight Harder for Better Workforce Policies?

If at least part of the business community really has a strong interest in the quality of the workforce system, it is not always apparent from their activities in the public sphere. There are some clear exceptions to this generalization; for instance, the National Association of Manufacturers (NAM), the U.S. Chamber of Commerce, the Committee for Economic Development and the National Alliance of Business all pay significant attention to human resources issues.[12] But, when political fights erupt over the investment of resources in the public workforce system or in the development of particular approaches (like the School to Work Act of the 1990's), business political efforts on their behalf often seem limited – especially among corporate CEO's rather than their lower-level human resources staff.

Why doesn't the business community invest more political capital on behalf of the public workforce system? Perhaps the numbers of employers with unmet workforce needs are simply too small, relative to the total business community, to influence their actions. Alternatively, other forces might be working to limit this influence.

At least two sets of hypotheses immediately come to mind. First, many business owners and managers still seem to maintain a traditional viewpoint in which the distinction between "capital" and "labor" remains very sharp, and where the latter is strictly viewed as a nonpermanent factor of production of relatively uniform (and often

[11] A "home bias" implies that production of the goods and services must occur locally, as is clearly true for construction or transportation and also for many services (like health care) that require direct contact with customers.

[12] For instance, NAM's Manufacturing Institute has a Center for Workforce Success, and the Chamber operates an Institute for a Competitive Workforce. These groups tend to advocate for workforce development policies, though not always for large public expenditures in these areas.

low) quality; in this view, a company's primary goal (especially in the face of foreign competition) with respect to labor is simply to keep wage and benefit costs low. In this view, a firm "invests" relatively little in labor. To the extent that skills and "human capital" are clearly relevant for production purposes, it is the capital that workers bring with them from formal educational institutions and earlier work experience, rather than training on the current job.

Indeed, owners and managers with this point of view are much more likely to choose the "low road" in human resources performance. The recent business success of Wal-Mart, and its dramatic expansion across the U.S. in the past decade, suggests that this model might also be growing at the expense of the "higher-road" model, though the empirical evidence on that is not yet clear. The growing perception among employers that outsourcing might provide cheap sources of foreign labor to the service sector (and that immigration might provide them domestically) – even when quite highly-educated workers are needed - no doubt reinforces this point of view, at least in some sectors.

Second, even among employers who know they must provide training and develop the skills of their private workforces, many remain indifferent towards or averse to using the public workforce system. They merely seek to find job candidates with good general skills and job readiness, and then rely on themselves to train them in whatever specific occupational or sectoral skills are necessary. An old stereotype that workers who have been publicly referred (through the U.S. Employment Service) or trained must be poorly skilled by definition persists in some circles, or that any public system is not "employer-friendly." While WIA was designed to make the public system more responsive to business needs in a variety of ways, it is unclear that this has changed the broader perceptions of the workforce systems within the business community.[13]

Of course, if this skepticism is well-founded, the reluctance of the business community to advocate for workforce development becomes much more rational. The evaluation evidence overall suggests publicly-funded training impacts for adults that are generally positive, though sometimes quite small; and for youth they are even more mixed (Lalonde, 1995.)[14] And, for businesses that do not have serious problems recruiting or retaining skilled workers (or for whom the "low road" is demonstrably profitable), opposition (or at least indifference) towards higher public expenditures on workforce development is quite rational as well.

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[13] The responsiveness of the training system to employers was supposed to be enhanced in WIA because of the high representation of businesses on local workforce boards, through the efficiency of "One-Stop" shops, and through an emphasis on the provision of "core services" (like job search assistance) that might fight the traditional perception that the system caters to less-skilled employees. This perception has traditionally plagued and limited employer usage of the U.S. Employment Service (Eberts and Holzer, 2004).

[14] There have been no evaluations to date of WIA-funded training using random assignment techniques. The most recent such study of federally-funded programs was for the Job Training Partnership Act, and was published in 1994. A study of "human capital" strategies for welfare recipients conducted as part of the National Evaluation of Welfare-to-Work Strategies (NEWWS) also showed little positive impact, though the effects were quite positive at one site (Portland Oregon) and for some kinds of training. See Hamilton (2002) and Holzer and Martinson (2005).

Thus, convincing more of the business community that a "high road" is economically viable and consistent with being competitive, and changing the stereotypical view that public sector training is ineffective or only serves stigmatized workers, might have to be part of any major effort to "sell" greater investments in the public workforce system to the U.S. business community.

IV. Conclusion

The above discussion indicates that many, though certainly not all, American employers will continue to have a strong interest in the quality of the public workforce system. This interest will be most pronounced in sectors requiring fairly specific skills (that are generally not provided through the U.S. postsecondary educational system), and especially when labor markets are tight – either overall or in particular local areas and sectors.

In a nutshell, *a strong workforce development system serves the interests of employers because*:

- When highly skilled workers are not widely available in the workforce, employers find it more difficult and costly to recruit and retain these workers on their own;
- Companies will often not invest their own resources in training, even for skills they need, because these workers might then be bid away by local competitors;
- Lack of information and short-term financial constraints on companies also make it difficult for employers to hire the best available workers and invest adequately in such training on their own;
- "Baby boomer" retirements will put extra pressure on employers in many sectors, such as health care, construction, and the like;
- Globalization – in the form of foreign outsourcing of jobs and continued immigration at home – will not meet employer skill needs in many sectors (especially where there is a strong "home bias" to producing the goods and services and where customer contact and communication needs limit reliance on recent immigrants).

These factors imply the need for a public system that provides information to employers and workers, resources for training, institutional linkages between employers and training providers, and a variety of other supports and services – as the WIA system attempts to do and as various "sectoral" and intermediary-based approaches might do even more successfully.

Of course, many businesses can pursue their interests with or without these supports – especially through "low road," cost-minimizing strategies. But, wherever possible, it is in the country's interest to encourage businesses to pursue profits through a strategy based on higher skills, productivity and earnings rather than lower ones. In this way, the business interest and the national interest might be better brought into sync with one another.

Convincing employers that they have a strong stake in the public workforce system, and getting them to invest effort and political capital in improving that system, has always been a tough "sell" – and maybe has grown tougher in recent years as foreign outsourcing becomes a more viable option and as competitive pressures from Wal-Mart and other low-cost employers become more severe. Many employers prefer to either not use skilled labor at all (i.e., the "low road"), to hire workers who have already been fully educated and trained (either domestically or overseas), or to simply rely on themselves to train workers with good basic education and general skills without getting involved with the public workforce system. Long-held beliefs that any such public system will not be employer-friendly or not effectively provide skilled workers dissuades many employers from becoming actively engaged, and certainly dissuades their CEO's from

So how can the above case for a strong public workforce system be made more effectively to such a skeptical audience and in a less-than-supportive environment? For starters, identifying those sectors (and the employers within those sectors) who would be more amenable to these arguments might be a first step at engaging more of the business community in this process. For instance, among those businesses who know that they directly face a strong wave of "Baby Boomer" retirements among skilled workers over the next decade, and who cannot obviously turn to foreign outsourcing or immigration to deal with it, the sale might not be quite as difficult. And for those who remember their experiences of the late 1990's, when recruiting and retaining qualified workers was a major challenge for many businesses, the sale might be more promising as well.

Other efforts might pay off as well. For instance, the perception that the publicly supported workforce system is not "business-friendly" or is unresponsive to business needs can be challenged by highlighting the growing set of training models where businesses are active partners in the training process. "Sectoral" programs, apprenticeships, public funding for incumbent worker training, and the like all private rely heavily on *private* employer provision of training with significant assistance from public entities and public-supported third-party "intermediaries" – who widely view businesses as well as workers as their clients These efforts can counteract a stereotype in which anything public-provided is immediately suspect.

Finally, providing rigorous evidence of the cost-effectiveness would make all of these efforts even more convincing. Though such evidence on "sectoral" initiatives and other more recent efforts is not yet widely available, simply describing to employers the wide range of these efforts that have been launched in the previous decade, and how much they differ from more traditional public training, would be helpful. And having truly *rigorous* evidence (i.e., based either on random assignment or other careful statistical methodologies applied to very carefully matched treatment and control groups) more broadly of effective training programs financed by WIA or other public mechanisms might help to dispel the widespread impression among business managers that public workforce efforts are not terribly effective.

To be more successful, all of these efforts might try to rely more heavily on employer and industry associations. Especially in those industries where employers feel vulnerable to imminent Baby Boomer retirements, the associations might be active partners and provide the necessary infrastructure through which individual members can be educated about newer workforce approaches and convinced about their effectiveness. This infrastructure then can also be used to help deliver technical assistance and information about training approaches and opportunities.

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