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The Exceptional Economy

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When I was a young child, my father used to emphasize to me that, in America, we were all individuals and could do anything we desired. America was the land of opportunity. But while most coming-of-age Americans may have heard such sentiments from their own parents, the message is not universal. When I conveyed my father's words to a European colleague, she said, "Oh, really? We were told exactly the opposite. Our parents always told us, 'Don't think you're so special. You're one of a large group of people in society, but you're not so special.'"

In an economic sense, are we special—or rather, is America exceptional? Part of the answer is revealed in tracing the relative growth of our GDP compared to other countries over time, starting in the 1820s. Unsurprisingly, our political parents, the British, once led the world in terms of GDP per capita. That has changed over time. We gradually matched the United Kingdom, eventually and significantly surpassing them after World War II. By 2010, we were 28 percent richer than Britain, 22 percent richer than our Canadian counterparts, and 65 percent richer than Italy.

When assessing the American economy, economists and noneconomists alike care first about whether the economy offers the prospect of a good living or healthy wages. A related concern is a desire for job security. Does our labor market offer us freedom from the worry that our source of income is in jeopardy? And finally, the third factor addresses the long-term wish that our children be able to live better than we do. We want our economy to afford continual opportunity, and we want our children to be upwardly mobile.

The American economy has done quite well in terms of both income levels and growth. What about job security? The unemployment rate is one measure of job security. Over the last thirty years, the unemployment rates in the United States, on average, have been lower than just about every comparable country in the world. The one exception to this statement is Japan. Japan has exceedingly low unemployment rates, and it is entirely reasonable to ask why we are not surpassing them in this metric. One possibility is that Japan's unemployment rate is actually too low. Japan has a somewhat stagnant, impacted labor force that may have too little labor market churn. The United States has low unemployment rates but also has one of the most dynamic labor forces in the world.

Most American children actually do better than their parents despite the rhetoric and fears to the contrary. According to a dataset called the Panel Study of Income Dynamics, 84 percent of children are earning more than their parents in real buying-power terms, which corrects for inflation.[1]

Ninety-three percent of children in the lowest quintile—that is, the people whose parents were in the bottom 20 percent—do better than their parents. That is not so surprising. It is easier to rise to the top when starting from the bottom. But even among the top 20 percent, 70 percent of children do better than their parents.

In terms of mobility, is it possible for Americans to move up, or are we stuck where we were born? The answer is that we move up very successfully. Of the people who are currently in the top 20 percent of earners in the United States, 60 percent came from families that were in quintiles other than the top 20 percent. If it were purely random, 80 percent would come from the other quintiles because 80 percent by definition are in the other four quintiles.

To be fair, America has been criticized for some lack of mobility across generations, and this is particularly true within certain communities, especially among the poorest individuals in our society. There is some tendency to get locked in. But most of income is not explained by birth, and that is not a strictly American phenomenon. For example, in Canada, the leader in mobility, 95 percent of income is not determined by parental income. Factors other than parents' income account for 95 percent of variation in personal income in that country.

In the United States, that figure is lower, but it's still 78 percent: the bulk of where you end up in the economy is independent of where you were born in terms of your income or your status. Despite the fact that we're not doing quite as well as some other countries in this measure, we actually do very well in terms of mobility albeit less well than some other countries.

The best indicator of whether we are exceptional is the market test. Are people buying our products? Do people want to come here? There are four times as many people in the queue for a green card as are actually issued one in any given year.[2] We are the team everybody wants to play for.

A survey of Europeans asked in which country respondents would prefer to work.[3] The largest number chose the United States. We do not see Russia or China on that list. We remain the choice destination. People are putting their money where their mouths are, and this tells us that the United States is exceptional.

What are the ingredients that have made our economy so successful over time? There are a number of factors. There are four clear factors: we are industrious; we are a mobile society; we are welcoming; and, compared with others, we have light regulation and low taxes.

Tocqueville wrote, "The state of things is without parallel in the history of the world. In America, everyone finds facilities unknown elsewhere for making or increasing this fortune, the spirit of gain is always eager, swayed by no other impulse but the pursuit of wealth." Tocqueville admired Americans' pursuit of wealth, an attribute that some view negatively these days.

Tocqueville was really affirming a position that was articulated decades earlier, in 1776, by Adam Smith in *The Wealth of Nations,* where he argued that people acting in their own interest will, like an invisible hand, help the economy grow and move things forward. Tocqueville had never seen a country that had people working to move this invisible hand along as successfully as in the United States.

That remains true. We work harder than our counterparts. Figure 1 shows the average number of hours worked per person in the working-age population.[4] This is not merely the average number of hours worked among workers. It takes the total number of hours that people are working and divides that number by the population, so having a large percentage of our population employed is one reason why our average hours of work among those who can work is so high.

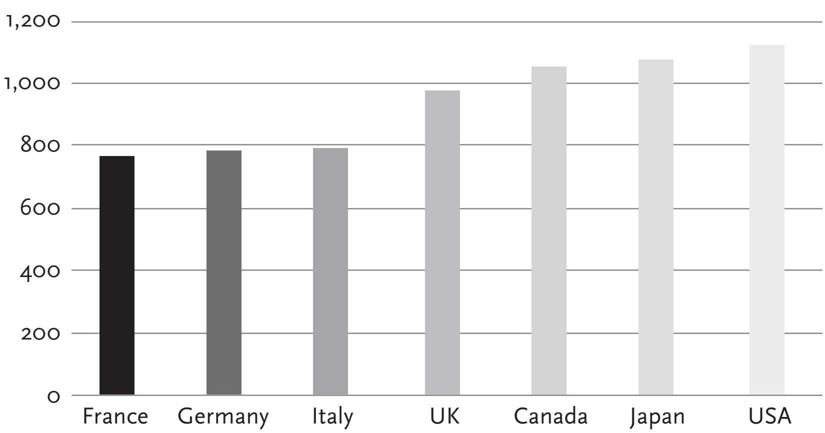

Figure 1. Average Hours Worked Annually per Person, 1991–2014

Japan used to lead in this regard for a significant period after World War II. But in the last couple of decades, the United States has passed Japan. We have both high labor force participation and hours of work. Some may believe we are working ourselves to death. But I view it positively. Wealth has not made us lazy. We still seem to have the drive that was required to make the economy and the country grow throughout our first two hundred years.

We also work hard in school. We invest very heavily in education and human capital. Not only is it true that we lead the big countries in terms of average levels of schooling right now, but we did so early on. We had compulsory schooling up to age sixteen before almost all the other countries in the world did. We recognize the value of education and of investing in human capital, and we were willing to put resources behind that view.

Education is an important driver of geographic mobility, and there our numbers are impressive. In any given year, 16 percent of the US population has moved, compared to 7 percent in the European Union.[5] If a good job comes up on the other side of the country, Americans are willing to take it. Europeans historically have been less likely to move. And geographic mobility is an important determinant of economic growth. When I was growing up here, California had 10 million people. It now has three and a half times that. It still has very rapid expansion, manifesting a mobility westward from the east. There were tremendous opportunities on the West Coast, and Americans moved to take advantage of them.

An example of another kind of mobility that was extremely important in the development of this country is the migration of African Americans from the rural South to the urban North, which took place starting in the late 1940s and continued throughout the 1980s and 1990s. Cities such as Detroit, which started out with very low African American populations, became very highly African American, in large part because of economic opportunities in manufacturing. More recently, we have seen the reverse: mobility back down to the urban South, adding to the growth of cities such as Dallas, Houston, Miami, and Atlanta. This is an exceptional American phenomenon.

In addition to geographic mobility, we enjoy job mobility. In any given year, about 60 million people are hired, which is two-fifths of the labor force. At the same time, 58 million are separated. Labor market churn helps move workers to their most productive use. We lead the world in this type of mobility. Ten years ago, a colleague and I did a book in which we looked at a dozen countries and compared this labor-force mobility. Some other countries also do fairly well in this respect. Denmark, surprisingly, is a very mobile and quite open labor market. We are the leaders.

America is exceptional in the opportunities it offers immigrants. Of all countries, including Canada, we are the only one where the unemployment rate among the foreign born is lower than that among the native born. Our immigrants actually do better in finding jobs than does the native-born population. We remain a welcoming nation.

This good news is related to our relatively light labor regulation. Employment at will essentially implies that the employer is free to decide whether or not you work for that firm. This is less true in Europe, where layoffs cannot happen without compensation. That seemingly just approach has consequences. In Spain, for instance, employers have to give a laid-off employee six months of pay if they are laid off after ten years of service. In Italy, it's about $2,000 for three years of service. As a reaction to that, firms in these countries have lowered their hiring rates dramatically. If a company fears that it cannot lay off a worker, it is less likely to hire in the first place.

As a result, European companies have moved toward temporary employment contracts. In France today, virtually everyone is hired into a temporary job. People who stay in the jobs for long enough become permanent, and this frequently results in inefficient termination. Just when the worker is getting good at the job, he is terminated so the employer does not have to make him a permanent employee.

America has also had historically light taxes. The ratio of combined state, local, and federal tax to GDP in the United States is 26 percent. In France, the figure is 45 percent.[6] By international standards, our taxes are still quite low.

There are also less quantitative elements that differentiate our economy from other economies in the world. We are much less tolerant of economic class welfare than most economies. We do not have labor parties in the United States. Socialism has never taken off here. Even the union movement in the United States is thought of as one of business unionism, as opposed to social or revolutionary unionism.

Sam Gompers, the founder of the American Federation of Labor, said he believed that management and workers could get together to reach beneficial understandings—to get the job done with a fair day's work for a fair day's pay. Other countries have revolutionary unionism, which is essentially the desire to displace, rather than work with, capitalists.

Finally, new money tends to dominate old money in this country. The Fortune 500 firms in 1955 did not include McDonald's, Walmart, Apple, CVS, Microsoft, Amazon, Home Depot, or United Health Group. All these firms are now among the top twenty firms in the country, with a number in the top ten. None of these firms existed in 1955.

The same is true of individual wealth. A hundred years ago, the group of richest families in the country consisted of well-known names such as Sloan, Carnegie, Ford, and Getty. Their descendants are probably still pretty wealthy, but the group of big names today is dominated by Buffett, Gates, Ellison, Bezos, Koch, Zuckerberg, Bloomberg, Walton, and Page—names that were unknown two or three decades ago.

Is this mobility a stable element of American economics, or has it changed over time? Consider President Obama's response to a question by Edward Luce of the *Financial Times* about whether America is exceptional. Obama said, "I believe in American exceptionalism just as I suspect the Brits believe in British exceptionalism and the Greeks believe in Greek exceptionalism." That was a very tactful answer, but this is probably not the topic on which we want our president to be humble. It is not such a bad thing for the president of the United States to believe that we are the greatest country in the world, especially given evidence that supports that view.

Indeed, there was some erosion under President Obama in those factors that make America exceptional. Obama did not subscribe to the view that light regulation is beneficial. Nor did he seem to believe that incentives matter very much, emphasizing redistribution over growth as the most important feature in an economy, labeling growing inequality and lack of upward mobility the defining challenges of our times. We have seen in recent years the erosion of employment at will, and we have seen rising marginal tax rates.

During the Obama administration we saw increased regulation—the Dodd-Frank Act, the Affordable Care Act, aggressive action by the Environmental Protection Agency, and the Department of the Interior's redefinition of navigable waters, among the most egregious. These moves may undermine the exceptionalism that has characterized the past two centuries.

Exceptionalism is not all about economics. While it is true that economic success affects our standard of living, it also affects our prominence in the world. Historically, the countries that have led the world politically tend to be the richest. It is expensive to have an army. It is expensive to have national defense. It is expensive to be a world leader. Consider ancient Rome, eighteenth-century Britain, and the United States in the twentieth century. All were at the time of prominence the richest economies in the world. The Soviet Union collapsed when it became impoverished and could no longer afford to support an enormous military. Russia's self-confidence and desire to affect its neighbors seem to vary with the price of oil, which is a significant source of government revenue. Similarly, China's recent aggressiveness in the South China Sea and elsewhere in the world matches its economic progress. Whether we want to be a world power is a separate matter. But having the ability to do so clearly depends on our exceptional economic position. If we lose it, we will be losing more than merely the right to claim that we are the land of opportunity.

Notes

1. Pew Charitable Trusts, *Pursuing the American Dream: Economic Mobility across Generations,* 2012, 4, http://pewtrusts.org/~/media/legacy/uploadedfiles/pcs_assets/2012/pursuingamericandreampdf.pdf (accessed June 8, 2017).

2. U.S. Department of State, Bureau of Consular Affairs, "Annual Immigrant Visa Waiting List Report as of November 1, 2015," 2015; and Department of Homeland Security, Office of Immigration Statistics, "Yearbook of Immigration Statistics 2014," 2016.

3. European Commission, "Geographical and Labour Market Mobility: Report," Special Eurobarometer 337, June 2010, 32, http://ec.europa.eu/public_opinion/archives/ebs/ebs_337_en.pdf (accessed June 8, 2017).

4. Organization for Economic Co-operation and Development, Statistical Data Base, 1991–2014, http://stats.oecd.org (accessed June 8, 2017).

5. Alexander Janiak and Etienne Wasmer, *Mobility in Europe—Why It Is Low, the Bottlenecks and the Policy Solutions,* European Commission, 2008, 22.

6. Organization for Economic Co-operation and Development, Centre for Tax Policy and Administration, https://oecd.org/ctp (accessed June 8, 2017).