Sustainable Prosperity in the New Economy?

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Preface

As I write this preface in March 2009, the United States is in the midst of the worst economic crisis since the Great Depression. The Obama administration has established a massive stimulus package to get the economy back on track. As I show in this book, however, there are fundamental problems with the U.S. economy that predate the current crisis. Even in recovery, the U.S. economy will not generate stable and equitable growth—or what I call “sustainable prosperity”—unless these problems are fixed.

For the past three decades the distribution of income in the United States has become more unequal, with a hugely, and some might say grotesquely, disproportionate share of total national income now going to the very richest households. Over the same period, the U.S. economy has experienced an inexorable disappearance of “middle-class” jobs—stable employment opportunities that provide a decent standard of living. A key finding of this book is that even when economic conditions are generally prosperous, economic insecurity afflicts well-educated and highly experienced members of the U.S. labor force. Yet these are the people who should be best positioned to make a good living.

In this book, I analyze the ways in which the “New Economy business model” in the information and communications technology (ICT) industries has contributed to this instability and inequity. In the last decade, U.S.-based ICT companies have been replacing well-educated and highly experienced U.S. workers with qualified labor in lower-wage nations such as China and India. The contribution to the growth of these developing economies represents progress. The problem is that rather than use the profits from globalization to sustain and upgrade the employment of U.S. workers, companies like Cisco Systems, Hewlett-Packard, IBM, Intel, and Microsoft have been using these profits to repurchase billions of dollars annually of their own outstanding shares in an effort to boost their stock prices.

Underlying this mode of corporate resource allocation is the corporate governance ideology that contends that to achieve superior economic performance companies should “maximize shareholder value.” In this book, I expose the fallacies of this argument, and I show how in practice shareholder-value ideology contributes to instability and inequity in the economy and tends to undermine the accumulation of innovative capability. This book provides an alternative perspective on how corporate resource allocation can contribute to the achievement of sustainable prosperity.

The research that underpins this book goes back some two decades, when I first started analyzing the financialization of the U.S. corporate economy and the consequent decline of what the eminent business historian Alfred Chan-
dler called “managerial capitalism,” or what I call the “Old Economy business model.” In the last half of the 1980s, when my principal academic appointment was in the economics department of Barnard College at Columbia University, my work benefited greatly from my involvement with Al Chandler and “the Business History Group” at Harvard Business School. One result was the publication of Business Organization and the Myth of the Market Economy (Cambridge University Press 1991), a critique of the notion that the neoclassical theory of the market economy can comprehend the actual allocation of resources in the U.S. economy. Another result, published in Industrial and Corporate Change in 1992, was “Controlling the Market for Corporate Control: The Historical Significance of Managerial Capitalism,” my first extended critique of agency theory and shareholder-value ideology.

Shortly thereafter, I met Mary O’Sullivan, a graduate of the Harvard Business School MBA program and a doctoral candidate in the Harvard Business Economics PhD program. Her insights into corporate finance, financial economics, and the evolution of the industrial corporation have contributed significantly to the analysis in this book. Our first major project, funded by the Jerome Levy Economics Institute, resulted in an edited volume, Corporate Governance and Sustainable Prosperity (Palgrave 2002), which focused on the disappearance of good jobs in the U.S. economy under a shareholder-value corporate governance regime. Among the contributors to this volume were Bob Forrant, Phil Moss, and Chris Tilly, my colleagues in the Department of Regional Economic and Social Development (RESD) at the University of Massachusetts, Lowell, with whom I have had ongoing discussions about employment and income distribution in the U.S. economy.

In 1993 I had been lured away from Columbia University to UMass Lowell by Chancellor William Hogan and Vice Chancellor for University Relations and Development Frederick Sperounis, both of whom were committed to a university-wide program of interdisciplinary research informed by an in-depth understanding of the realities of economic and social development. My RESD colleague John Wooding subsequently became provost in the Hogan administration. I would like to thank this trio for creating the intellectual environment and working conditions in which the type of research that is found in this book could be pursued.

Since the early 1990s I have sharpened my perspective on the distinctive evolution of U.S. capitalism through comparative research on corporate governance, innovation, and economic performance in Europe and Asia. An understanding of the European experience is important because of the persistence of distinctive corporate governance regimes across the European Union and the resistance of Europeans—to their ultimate benefit, I would argue—to the wholesale adoption of the U.S. shareholder-value model. An understanding
of the Asian experience is important because, starting with Japan in the 1950s, the world’s most dynamic developing economies have emerged in this region, with, as in the most recent cases of China and India, an increasingly heavy emphasis on the ICT industries as the engines of growth and the availability of highly capable labor forces to make that growth happen.

I am grateful to Keith Smith for introducing me, beginning in 1993, to the European collaborative research environment through my involvement in the Studies in Technology, Innovation, and Economic Policy Group in Oslo, Norway, when he was the director of that research institute. From 1996 to 2007 I carried out my research as a faculty member of INSEAD, the Institut Européen d’ Administration des Affaires, or European Institute of Business Administration, in Fontainebleau, France. While at INSEAD, I led a major European Commission project, Corporate Governance, Innovation, and Economic Performance (CGEP), and was a participant in a subsequent EC project, European Socio-Economic Models of a Knowledge-Based Society (ESEMK), led by Yannick Lung of Université Montesquieu-Bordeaux IV. Research carried out under these projects has contributed to this book, as has work done with Henrik Glimstedt of the Stockholm School of Economics and Ulrich Jürgens of Wissenschaftszentrum-Berlin.

My research on Asia began in the early 1990s with a project with Kazuo Wada of the University of Tokyo and Takeshi Abe of Osaka University on the dynamic interaction of organization and technology in Japanese economic development. I greatly deepened my understanding of Japanese development when I was a visiting professor in the faculty of economics at the University of Tokyo in 1996–1997, as well as through a subsequent project on the Japanese enterprise led by Akira Kudo of the University of Tokyo and Glenn Hook of the University of Sheffield. I also benefited immensely from numerous discussions about Japanese and comparative capitalism with Ronald Dore, a person of remarkable knowledge and insight.

From 1997 to 1999, I was joined at INSEAD by my Harvard sociology student Qiwen Lu, whose pioneering book, *China’s Leap into the Information Age* (Oxford University Press 2000), alerted me to the innovative capabilities being developed in China, a subject I address in Chapter 5 of this book. Sadly, Qiwen died just after his book manuscript was completed. Through Qiwen’s work, I got to know Dic Lo of the University of London’s School of Oriental and African Studies (SOAS) and Renmin University of China, who in 2006 hosted me on an illuminating trip to China. I have also learned much about China from my UMass Lowell graduate students, especially Hao Xie, Yue Zhang, and He Gao.

My firsthand insights into Indian development began in 1993 with a United Nations Development Programme project on the jute industry with my UMass...
Lowell colleagues Michael Best and the late Sukant Tripathy. At the time there were tens of millions of educated unemployed in India. The rapid growth of the Indian information technology (IT) services industry from the late 1990s changed all that. In 2007 I made two trips to Bangalore, the center of the Indian IT services industry, to observe the economic transformation that had taken place. I owe special thanks to Parteii Sawyan of Shillong, who, through her friend, Naina Kidwai, CEO of HSBC India, helped me gain access to executives at a number of Indian IT services companies, including Infosys, Mindtree, and Wipro. For sharing with me their knowledge of the Indian ICT industries, I am grateful to Arundhati Chakraborty, Amrita Dhindsa, and Sunil Swarup of HP India; Muthukrishnan Subramanian of IBM India; Somnath Baishya, Bikramjit Maitra, and Deependra Moitra of Infosys; Srinivasa Rajam of Ittiam; Puneet Jetli, Krishnakumar Natarajan, and R.K. Veeraraghavan of Mindtree; Mohan Kumar of Motorola India; Swati Bhatia and Marion Leslie of Reuters India; and Ranjan Acharya, Jatin Dalal, Vinod Harith, Ashok Herur, Divakaran Mangalath, Sudip Nandy, Veena Padmanabhan, Jessie Paul, and Swapna Pillai of Wipro.

In the United States, I received a grant in the late 1990s from the Russell Sage Foundation to study how, in the Internet boom, Lucent Technologies, a major high-tech employer in Massachusetts, was coping with shortages of skilled production workers at its Merrimack Valley Works, which had 5,600 employees. As I was doing this research, however, boom turned to bust, and the project ended up being about the demise of a major high-tech manufacturing plant and the subsequent employment transitions of its displaced workers. Through this project, I came to know Edward March, director of engineering at Merrimack Valley Works, who subsequently was for a number of years a highly valued colleague of mine at UMass Lowell and who continues to enlighten me about the processes of technological change.

This plant-level study fed into a substantial research effort, initially in collaboration with Marie Carpenter and Mary O’Sullivan at INSEAD as part of the CGEP project, to analyze the impact of the New Economy business model, as epitomized by Cisco Systems, on strategy, organization, and finance at Old Economy communications equipment companies such as Lucent, Nortel, and Alcatel. INSEAD provided us with excellent access to executives at Alcatel, headquartered in Paris. I am especially grateful to François Béhague, Jean-Luc Corniglion, and Elizabeth Eastland for the time that they spent with us explaining the changes in organization and technology that occurred at Alcatel during the Internet boom and bust. Subsequently, in 2003, I also began to do research with Henrik Glimstedt on Ericsson, the Swedish communications equipment giant. With the extraordinary cooperation of Marcus Sheard, the company’s
vice president of worldwide compensation and benefits, we analyzed how Ericsson adopted U.S.-style employee stock option plans and then transformed their use to fit with the much more egalitarian Swedish business model.

Building on our research on the communications equipment companies, in August 2007 Marie Carpenter, Henrik Glimstedt, Ed March, and I organized a conference at INSEAD on innovation and competition in the global communications technology industry that brought together practitioners and academics. Besides providing material for this book, the conference led to an ongoing collaborative study of the global communications technology industry with Petter Kilefors and Martyn Roetter of Arthur D. Little consultants.

While all of this work has fed into Sustainable Prosperity in the New Economy? it was a grant from the W.E. Upjohn Institute for Employment Research that transformed a wide-ranging research agenda into a focused book. The Upjohn Institute’s support for this project went far beyond funding. Susan Houseman encouraged me to apply for the grant and provided much-appreciated guidance and patience throughout the project. Two anonymous referees provided constructive comments on my original book proposal. Kevin Hollenbeck made excellent suggestions concerning the organization and editing of the book. Bob Wathen was a superb copy editor; he helped me to emphasize the bigger picture that I was painting while cleaning up my errant brushstrokes. The production of the book was then placed in Richard Wyrwa’s very capable hands and Benjamin Jones did a great job of proofreading the galleys.

Since 2005 the material in this book has been presented at invited lectures in various venues around the world. Previous versions of some of the chapters have been published in various journals and edited volumes, in most cases with considerably more empirical detail than has been included in this book. These publications include Internet and Digital Economics; The Future of Work in Massachusetts; Employee Pensions: Policies, Problems, and Possibilities; The Oxford Handbook of Information and Communication Technologies; Perspectives of Corporate Governance; Industrial and Corporate Change; Louvain Economic Review; and Capitalism and Society.

Besides those people whose intellectual contributions I have already mentioned, in writing this book I have benefited from discussions with and/or comments from Ron Adner, Sanjay Anandaram, Tosun Aricanli, Randy Barber, Ross Bassett, Christophe Belleval, Michael Best, Margaret Blair, Danny Breznitz, Eric Brousseau, Kristine Bruland, Bob Buchele, Leonardo Burlamaqui, Jose Cassiolato, Ha-Joon Chang, François Chesnais, Chris Clott, Andrea Colli, Tony Daley, Stephen Diamond, Yves Doz, Ciaran Driver, Steve Early, Jim Elliott, Dieter Ernst, Jan Fagerberg, Kaidong Feng, Tom Ferguson, Lou Ferleger, Patrick Fridenson, James Galbraith, Teresa Ghilarducci, Debbie Goldman, Margaret Graham, Leslie Hannah, Susan Helper, Ronil Hira, Ha
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My daughters, Ashley, Léah, and Casey, heard me say all too often that the book was almost done. Now that it actually is finished, I want them to know how much their interest in their dad’s work means to me. The person who heard me talk about this book-in-progress more than any other was Carol Oja, a brilliant musicologist and incredible human being, whose pertinent questions and insights helped me to clarify my arguments in my mind and on the written page. Finally, I would like to dedicate this book to the memory of my parents, Louis Lazonick (1914–1995) and Pearl Lazonick (1917–2005). Coming of age as they did in the Great Depression, they understood the importance of achieving stable and equitable economic growth.