Albert Rees and the "Chicago School of Economics"*

By

Orley Ashenfelter and John Pencavel**

Abstract: Though Albert Rees was certainly a member of the "Chicago School of Economics," his role was perhaps distinctive in that group. This essay explains that role.

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**Orley Ashenfelter is the Joseph Douglas Green 1895 Professor of Economics, Princeton University and John Pencavel is the Levin Professor of Economics, Stanford University.

Albert Rees (1921-1992)

Albert Rees was born in New York City and earned his undergraduate (BA) degree at Oberlin College in 1943. His MA degree at the University of Chicago was followed by his appointment as an Assistant Professor in the Economics Department at Chicago. His PhD was awarded at Chicago in 1950. He remained at Chicago until 1966 when he assumed a position as Professor of Economics at Princeton University. His Princeton appointment lasted until 1979 (having been Provost between 1975 and 1977). During his tenure at Princeton, he spent several years in Washington, D.C., involved in administrative efforts to restrain wage and price inflation. He served as President of the Alfred P. Sloan Foundation from 1979 to 1989.

Rees's scholarship centered on Labor Economics and his contributions ranged from theoretical modeling to resourceful empirical research to the careful construction of original data. The public policy ramifications of this work were never far from his research. He was a very conscientious and courteous adviser of many students. Teaching was important to him and, in the 1970s, he authored the major textbook at that time in Labor Economics (1973). His gracious manner made him a popular teacher and colleague. He served as editor of the Journal of Political Economy for a number of years.

A persistent social issue for Rees - as it was for many economists of his generation - concerned the effects and appropriate public policy role of labor unions. His years as an undergraduate and graduate student were a period when unionism in the United States expanded and became a major policy concern for the country. Unlike some economists, Rees was eager to apply the analytical tools of economics to the study of unionism. No doubt, this suited the climate of the Chicago Economics Department at the time. Perhaps the best example of his readiness to subject unionism to classical economic reasoning is Rees's (1963) well-known estimates of the resource misallocation costs of unionism. In this work, Rees applied to labor markets Arnold Harberger's methods of assessing the cost of product market monopolistic pricing. Ostensibly, the gap between the wages of workers in unionized and non-unionized markets is a source of resource misallocation because equally productive labor is being sold at different prices. Rees's calculations suggested that, in the United States in the late 1950's, the costs of this source of resource misallocation were approximately 0.14 percent of national output, an amount that did not seem to justify some of the alarmist views about labor union activities in the United States.

The study of unionism was Rees's lifelong interest and his fundamental views about American unionism appear to have changed little from his early scholastic days to his later years. He tended to regard the economic effects of unionism as largely undesirable. Thus, in the third edition of his text The Economics of Trade Unions (1989, p. 191), he wrote, "If the union is viewed solely in terms of its effect on the economy, it must in my opinion be considered an obstacle to the optimum performance of our economic system. It alters the wage structure in a way that impedes the growth of employment in sectors of the economy where productivity and income are naturally high and that leaves too much labor in low-income sectors of the economy."

Yet he immediately proceeds to describe this judgment as "narrow" if offered as a complete assessment of unionism. He wrote (1950, p. 257) in an early review of a wide-ranging denunciation of unions, "The least that can be said for unions is that their noneconomic activities are, by and large, highly beneficial. Through grievance procedure, seniority, and control of the speed and conditions of work, unions have given the industrial worker a new sense of dignity, individual worth, and participation in the process of production." Rees saw "a strong union movement [as] the best guaranty against movements which might lead workers to demand the exchange of our democratic freedoms for the 'security' of a police state" (1950, p.261-2). In appraising unionism, Rees was ready to accept the basic framework of economic reasoning, but also recognized that a full evaluation required a broader perspective.

Rees was conscious of the problem posed by the public policy goals of full employment and price stability in a context in which labor unions may be a strong force on wage-setting. He pursued this concern both at a micro-economic level by examining wage determination in a single industry, steel, (1951b), one of the subjects of his PhD thesis, and from a macro-economic perspective by asking "Do Unions Cause Inflation?" (1959). He demonstrated (1952) that one measure of union activity, the incidence of industrial strikes, increases as the economy approaches full employment with the peak in strikes slightly preceding the peak in business activity. The general positive covariation of strikes and the business cycle suggests that union activity was an integral part of a structural interpretation of the movement of wages and prices. In 1967, after reviewing efforts to estimate Phillips' Curve relationships for the United States, he urged the authors of Phillips' Curves to label them conspicuously as "Unstable. Apply with extreme care." Later (1970b) he identified what he saw as the policy issues presented by Phillips's Curve.

This deep scholastic interest in the junction of full employment, stable prices, and labor union activity ultimately led to Rees assuming administrative positions in government in the early 1970s as part of an attack on what seemed like a relentless tendency for inflation to accelerate. In 1971-73, Rees was a member of the Construction Industry Stabilization Committee whose work was addressed to bringing public pressure to bear on wage and price inflation in the construction industry and, in 1974-75, he was Director of the Council on Wage and Price Stability where the anti-inflationary mission was wider. Though he was acutely aware of the limits of incomes policies, he did feel that some public pressure on relieving the wage-price spiral would be worth while if this reduced the need for deflationary measures that would diminish employment. In incomes policy, his preference (1965) was for gentle public suasion over a set of explicit rules and penalties.

Rees's interest in the problems presented by full employment, price stability, and unionism reflected his deeper interest in how labor markets function whether in the absence or in the presence of unionism. He tended to believe that, in the absence of unions, the conventional neoclassical model served as a useful device and his original research (1966) into information networks in labor markets revealed his respect for market mechanisms. This work drew on his detailed study of Chicago labor markets, a major research project whose results were published in 1970 in an important monograph written jointly with George P. Shultz who had been Dean of the Graduate School of Business at Chicago. Rees's examination of the ways in which job seekers collect information about alternative jobs and how employers find workers emphasized the value of informal channels such as referrals from existing employees and other employers. The channels that economists often extolled - state employment services, employment agencies, newspaper advertisements, union hiring halls, and school placement bureaus - tended to be used less by market participants.

However, Rees found the standard market-clearing model manifestly unsatisfactory when applied to the experience of labor markets during the 1930s Depression. In one of his early papers (1951a), he conjectured that wage levels do not always clear labor markets and, in particular, wages may be at levels at which more people seek employment than firms choose to employ. This was most likely to occur when aggregate demand had fallen and when wages were slow to adjust to restore market clearing. He provided a number of reasons for the absence of market-clearing in such situations. The implied presence of involuntary unemployment in these situations made him very skeptical of research that presumed market-clearing throughout the 1930s and an exchange with Robert Lucas and Leonard Rapping in the early 1970s provides a clear and forceful statement of his beliefs. Lucas and Rapping (1969) proposed that unemployed workers may choose not to accept wage offers they consider temporarily low and, as a first approximation, movements in unemployment are to be understood as the consequence of misperceptions by the unemployed. But Rees asked, "How long does it take workers to revise their expectations of normal wages in light of the facts? Unemployment was never below 14 percent of the labor force between 1931 and 1939 and was still about 17 percent of the labor force in 1939, a decade after the depression began. It is hard to imagine the long-term unemployed holding out for jobs comparable with their old jobs, at their old real compensation, over periods of up to ten years" (1970a, p.308).

Finally, as a scholar, Rees was above all an empiricist. Even his papers that focused on theoretical models are infused with data. He constructed (1961a) the definitive series on real wages in manufacturing industry in the 25 years before the First World War and, in committee reports with others, he advised (1961b, 1962, 1979) on the government's methods of measuring prices, unemployment, and productivity. With George Schultz, he led (1970c) a major empirical project examining Chicago's labor markets which involved the collection of large bodies of data on wages, employment, and many other aspects of labor markets. Later (1974), he was a principal investigator in the New Jersey/Pennsylvania Income Maintenance Experiment whose purpose was to determine the response of low income people to different terms of welfare benefits. He collaborated (1991) on a survey and analysis on faculty retirement behavior designed to anticipate the effects of the ending of mandatory retirement in universities. This uninterrupted commitment to careful measurement informed by public policy issues and by the precepts of economic theory is the type of scholarship that has the hallmark of the best Labor Economics research which is why so many of today's researchers think of Rees as their intellectual paragon.

Orley Ashenfelter and John Pencavel

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