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College Degree Still Pays, but It's Leveling Off

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Ever so gradually, the big payoff in wages from a college education is losing its steam, which calls into question the emphasis that the White House, under both Bill Clinton and George W. Bush, has placed on a bachelor's degree as a sure-fire avenue to constantly rising incomes.

Men and women with four years of college earn nearly 45 percent more on average than those with only a high school diploma, according to the Bureau of Labor Statistics. The spread is as high as it has ever been, but it has been stuck in the 45 percent range since the late 1990's, and through the 1990's it rose much more slowly than in the 1980's.

Although the payoff from a college education is leveling off, income inequality continues to grow. That suggested to some economists at the annual meeting last weekend of the American Economic Association that employers are making wage decisions on criteria that have little to do with the supply of and demand for educated workers.

The leveling off of the wage premium for a four-year college degree has lasted long enough to suggest that it is not just a pause in an otherwise constantly rising payoff for those with bachelor's degrees, but another significant shift in labor market dynamics. The payoff for a college education fell in the 1970's only to reverse course, rising sharply in the 1980's and then leveling off in the 1990's, even showing signs of beginning to fall in the current decade.

"We always knew that the return in wages to a college education fluctuates, but we forgot," said Cecilia E. Rouse, a Princeton University labor economist, "and now we are being forced to remember."

The 1980's experience gave birth to the skills-mismatch thesis - the view that millions of workers lacked the college training required for the increasingly high-tech jobs that the new economy generated. Out of that thinking came stepped-up federal spending on college scholarships, tuition tax credits and the like. That put the burden on individuals to get the necessary education, with the government playing a supporting role as financier.

The portion of the population with bachelor's degrees today is about 30 percent, not much above where it was in the 1980's. That limited supply of baccalaureates would suggest strong demand for them and a continual increase in the spread between what college graduates earn and what the much more numerous high school graduates earn.

The dynamics, however, do not work that way. For one thing, the wage spread between high school and college graduates is determined by what happens to each side of the equation. During the 1980's,
high-school-educated blue-collar workers lost well-paying jobs by the hundreds of thousands as domestic manufacturers increasingly lost out to foreign competitors. As their incomes fell, the spread widened rapidly.

The wages of the high school educated did not begin to increase again until the late 1990's, when tight labor markets increased the demand for their services. Now, the incomes of the high school educated are rising almost as quickly as the incomes of the college educated, according to an analysis of wage data by the Economic Policy Institute. That brings into question how much value a college education adds.

"The obsession with education has become a mantra to avoid tough political choices," said Harley Shaiken, a labor economist at the University of California, Berkeley. While education is essential, Mr. Shaiken and other economists argue, it is not enough. They would put more of the burden on government to close the wage gap, through such additional steps as raising the minimum wage and strengthening the laws governing collective bargaining.

That argument may undervalue the advances that are being made in high school education, says Richard Murnane, a specialist in the economics of education at the Graduate School of Education at Harvard. He notes that many states now require high school seniors to pass "exit exams" to get their diplomas.

Because these exams require considerable proficiency in reading and mathematics, "employers are beginning to see that high school graduates have more skills than they used to have," Mr. Murnane said. If college graduates ask for too much money, he said, employers may hire these high school graduates instead.

Another dynamic also undermines the value of a college degree, says David H. Autor, an economist at the Massachusetts Institute of Technology. While the college premium appears to be leveling off, the spread between the incomes of the highest-earning Americans and those in the middle expanded almost as fast in the 1990's as it did in the 1980's.

"If I may speak somewhat loosely, there continues to be rising demand for people who have very strong cognitive, managerial and communications skills," Mr. Autor said. "The vast middle, whether they are college educated or not, are not in that upper category of cognitive elite. The elite is college educated, but not all the college educated are those people."

The leveling off of the college premium came up in various panel presentations at the American Economic Association meeting in Philadelphia and in interviews with economists. One panel explored what Richard B. Freeman, a Harvard labor economist, described as the seemingly inexhaustible supply of immigrants with advanced college degrees who hold or seek jobs in America, depressing the demand for and the wages of all well-educated job seekers, immigrants and native Americans alike.

Another study, presented by Robert G. Valletta, an economist at the Federal Reserve Bank of San Francisco, found that wage increases associated with computer use at work were "relatively constant across educational categories" from 1984 through 2003, favoring the college educated only from 1997 to 2001, the era of the dot-com boom. A third study, presented by Ms. Rouse and Lisa Barrow of the Federal Reserve Bank of Chicago, found that the payoff from schooling was roughly the same across ethnic and racial groups - rising in tandem in the 1980's and tending to level off in the 1990's.

Their study, they said, knocked down the view, held by some economists, that the return to education was higher "in individuals who come from more advantaged families." The study also added to the documentation
that the income return for schooling rose in the 1980's, adding roughly 10 percent to a worker's wage in 1990 for each year of education, up from 7 percent in 1980. Since 1990, however, the added value has remained at 10 percent.

That puts Mr. Freeman of Harvard on the spot. He first made his name as a labor economist with the publication in 1976 of a book entitled "The Overeducated American," which argued that the college wage premium, which was then falling, would continue to fall. His reasoning was that the demand for college-educated workers was being suppressed by the large number of educated baby boomers taking jobs, while the growth in exports was sustaining the demand for high-school-educated factory workers. All too soon, Mr. Freeman turned out to be dead wrong.

"The only reason the payoff for a college degree went up in the 1980's was that there was a wonderful relative shift in the demand for educated workers," he said. "But there is no rule of law that says demand for educated labor will always rise faster than the supply. It could go the other way."