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Brookings Briefing

FREE TRADE IN THE NEW GLOBAL ECONOMY:

A DISCUSSION ON THE STATE OF U.S. TRADE POLICY

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The Brookings Institution
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[TRANSCRIPT PREPARED FROM A TAPE RECORDING.]

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Panelists: LAEL BRAINARD

PAUL CRAIG ROBERTS

THOMAS J. DONOHUE

SEN. CHARLES E. SCHUMER

THIS IS AN UNCORRECTED TRANSCRIPT.

P R O C E E D I N G S

MR. NESSEN: Welcome to this afternoon's discussion of America's trade policies, particularly focused whether changes in the global economy may require changes in America's current free trade policies. I'm Ron Nessen, I'll be the moderator for this afternoon's forum. And I especially want to welcome those who are watching today's discussion on CSPAN.

Couple of housekeeping notes first: Biographies of our panelists and other background information is available outside at the registration desk, if you didn't pick it up when you came in.

A summary of today's forum will be on the Brookings Web site later this afternoon. That's at brookings.edu and a full transcript of this discussion will be on the Website in the morning. Also, a great deal of additional information on trade issues can be found on the Website at brookings.edu.

We're going to begin our forum this afternoon with brief statements from Democratic Senator Charles Schumer, the senior senator from New York. And Paul Craig Roberts, the senior research fellow at the Hoover Institution, who was assistant treasury secretary for economic policy in the Reagan Administration.

I know most of you probably saw their op-ed article in yesterday's New York Times, in which they called for a re-examination of America's trade policies in light of changes in the global economy. And, if necessary, revisions of those policies to reflect what they call the new realities. Today, they will elaborate on their thoughts in that op-ed piece.

Next, we'll hear from Thomas J. Donohue. He is the president of the U.S. Chamber of Commerce, an organization, obviously, representing business. He will briefly outline the Chamber's view on trade issues.

And then, Brookings trade expert, Lael Brainard, a senior fellow and holder of the New Century Chair here at Brookings, who was deputy assistant to President Clinton for international economics, will comment on what we've heard.

Then we'll have a lively discussion among ourselves and panelists. Finally, the panel will answer questions from you in the audience.

Those watching today's discussion on CSPAN, you can submit your questions by e-mail to questions@brookings.edu, if you have questions for the panel.

It should be an interesting and informative afternoon. So, let's begin with Senator Schumer and Mr. Roberts.

SENATOR SCHUMER: Well, thank you, Ron, and I want to thank Brookings for hosting this little gathering on short notice. And I want to thank my unlikely partner, Paul Craig Roberts. We really don't know each other very well, but when I started thinking about trade issues, I just called a whole variety of people. And I found his thoughts to be well, I guess, a more satisfying fit of the new facts than we're seeing than just about anybody else's. And so, we began talking and, hence, our unlikely collaboration.

And I want to also thank our fellow panelists, Tom Donohue, who represents the Chamber very well and Lael Brainard and Ron, you, as well.

Before I begin with the substance and I'll be kind of brief and let Paul Craig--I just learned this--that he likes to be called Craig, we don't know each other that well.

The one sort of admonition that I would offer is that there's a great temptation on this issue to say everything, are you for free trade or are you protectionist? And almost everybody, economists, writers, thinkers, sort of just like to classify people one or the other.

And what we're trying to do here is different than that. We think that the fundamental model for free trade has changed due to all the changes we have seen in the world economy. We don't know what should replace it. We are certainly not advocating old-time protectionist answers. But we do think that people do have to start thinking about this in a new and unconventional way. And I have found in the places where I've begun to discuss this issue that there's almost an overwhelming tie to say, well, that's free trade, that's protectionist and see things in that regard and that's not what we're trying to do.

Let me just walk you through what made me start thinking about this. My record in the past has been, I guess I would say mixed. I have generally supported free trade, but I have voted against a number of free-trade measures. I did lose at one point the AFL-CIO endorsement when I was in the House for preventing the override of Ronald Reagan's veto of a textile--there was a textile barrier that I thought was very, very regressive. And I was one of the--I rounded up five Democratic votes and the AFL-CIO was mad at me for five years.

But, I began looking at the new issues. And two--two or three things--two or three people commented to me as I began to ask them about this.

One was the head of a New York securities firm who said to me that they had 800 people doing high-level computer software programming, not mundane stuff, but the highest level stuff. These are the guys who put together the programs for the derivatives where billions of dollars are at risk. Their average salary was $150,000. And he said to me that within three years, all of those jobs will be in India where we can pay the average worker about a quarter of what we are paying here.

And then I met somebody who was active in the American Radiological Society who represents the radiologists. And he said to me, within five years the number of radiologists needed in America is going to greatly decline because when you need a typical type of x-ray--you break a leg or you need a chest x-ray--you will still go to a technician who will take the picture, but that picture will be beamed to India or China where a very capable radiologist will read it for a quarter of the cost.

Now, he said, mind you, at the high end, if it's a very difficult radiological reading, it probably won't be beamed. But for the vast majority of them, which are more standard, it will.

And I began thinking--because in those two situations, it's not the classic free-trade model which has sort of kept us going, which is, well, the high-value jobs--the ones that take a lot of education and creative thought and intellectual property, will stay here and it doesn't matter if the--in fact it's probably good in the classic Ricardo--I don't know what the adjective is--"Ricardoan", since that they, you know, that fits the free-trade model. But it doesn't fit the free-trade model when these very high-end jobs, migrate overseas.

And I began thinking about it and realized that there are three factors that are different today than they were even ten years ago and are different than at any time in the history of the modern free-enterprise-Adam Smith-world.

And the first is that capital can flow very freely between countries. Ten years ago, people would not have invested in India and China in significant amounts, because their political structures were regarded as too unstable.

That second, communications changes allow broadband, allowed communications to occur at such a more sophisticated level that things could be done anywhere.

But, third, and most important, that for the first time, we had two countries--and this is to their credit--China and India--which will turn out millions and millions of high-end, well-educated, college-educated people who are well motivated; who are highly educated, probably as well-educated as here; or almost as well, in most instances, who make about a quarter of the money, who make much lower salaries for doing those jobs.

And you put those three-and this is not a couple of million--this is probably 50 million new people entering the world's labor market in the next ten years. Now, admittedly, that's a small percentage of the Indian and Chinese populations and--but it's such a large number absolutely that this presents a new challenge to us that we never had before.

Mexico or Brazil did not present such a challenge because their educational systems weren't so large. Because their populations weren't so large and their educational systems weren't as sophisticated.

And you put those three things together and you think, something is different than classically. Because, if overseas can out compete us--and maybe they can and maybe they can't, but it's certainly a possibility--not only for the low-end, low-value-added jobs and middle-value-added jobs, but, also, for the high-value-added jobs, then maybe something is awry.

At least, maybe, we ought to re-examine our fundamental precepts that high-value-added jobs will always be created here. Now that may be. Again, what Craig and I are doing is not positing what the future is. Just saying that the past, the recent past has changed so quickly that we ought to re-examine our fundamental assumptions and see if they stay fit.

And what we have found is sort of an atavistic pulling back, no, we can't do that. In the beginning of our essay, I forget exactly the words, but, you know, Canes described free-trade to economists is close to religion. And you couldn't step on it.

So, I just have to--we'll talk about--I'll let Craig talk about the theoretical underpinnings and where some of Ricardo's assumptions, he's the developer of the free-trade theory, I remember reading him in Ec-1 in college. Although I know far less about him than many of you in the audience. But the bottom line, again, is we are not positing a solution. We are not saying just, you know, go back and build trade barriers. We are saying something different has changed than in the past, which has been a progression from agriculture to textiles to higher-end manufacturing. Something different is in the air now. And we ought to look at it and examine it. And now I'll turn it over to Craig, because I've been told just five minutes each, to go over the theoretical parts of this where Ricardo--the assumptions that Ricardo assumed in his own world may not be true in our 21st century world.

MR. ROBERTS: Yes, you see, Senator Schumer and I are not attacking the doctrine of free trade. We're not saying that it's a wrong doctrine or a bad one or that we shouldn't have it.

What we're asking is, whether the conditions specified in trade theory for free trade to be mutually beneficial to the trading partners, where those conditions hold, when factors of production are as mobile as traded goods. That's the question.

The case for free trade, since the time of Ricardo, rests on the principle of comparative advantage. And the principle of comparative advantage, in turn, rests on the immobility of factors of production. This is in all the textbooks, it's in the literature. I have a recent piece from a trade theorist, Roy Ruffin, it's basically addressing Ricardo's theory of comparative advantage and why he has the claim to it. And he says, the key assumption of trade theory is the inability of factors to move from a country where productivity is low to another where productivity is higher.

And he goes on to give Ricardo's example where he's talking about Portugal and England and wine and cloth and Portugal has the absolute advantage in the production of both commodities. And why should England be able to come out of this when it only has a relative advantage. And he explains the principle. And then he says, as well, that since Portugal has an absolute advantage in the production of both cloth and wine, it would undoubtedly be advantageous to the capitalists of England and to the consumers of both countries that under such circumstances, the wine and the cloth should both be made in Portugal and, therefore, that the capital and labor of England employed in making cloth should be removed to Portugal for that purpose.

So, in other words, if the factors of production can flow freely across international borders, they move to where the absolute advantage is greatest and there's no comparative advantage. And there are no shared benefits from trade. One country gets rich and one gets poor. As I understand it, this is still the basis for trade theory.

And this particular trade theorist asserts that is the case, this is what's in the textbooks. And, yet, it's changed out from under us. And economists, apparently, disagree with this interpretation of the basis of trade or they're not aware that it's changed out from under them.

When resources--when the factors of production can flow across borders--in fact, they can actually move quicker than goods because goods have to be shipped, capital and technology and ideas can move with the speed of light.

And I think that Senator Schumer is right in observing that things have changed. There's always been some mobility to capital. But it was mainly confined into the first world. It's the new political stability in India and China that lets it move beyond the first world.

Moreover, there's another difference: when the capital flows between Japan, the United States and Europe, were different than the kinds of capital flow now. You see, when the Japanese and the Germans come here and build a plant to produce cars, they don't do that in order to send them back to Japan and Germany. They do it to sell in this market. The way it's working today, firms close facilities here, remove them to China, produce there, and send the products back here. This is not covered in the "Ricardoan" case for free trade.

So these kinds of differences and, of course, the Internet, which lets tradable services be performed anywhere. People in India check into their offices in Los Angeles or Chicago or wherever. This has made labor mobile. Ricardo expresses the immobility of capital and labor. The Internet makes labor mobile and the mobility of capital and technology makes labor mobile. The Chinese labor doesn't need to come to the United States, if American capital and technology goes to China. That makes the Chinese labor mobile.

So you end up with the situation where labor that is not paid the value of its margin of product because of huge excess supplies of labor in those labor markets, China and India, for example, labor that's not paid the value of its margin of product is highly mobile. Whereas, U.S. labor, which tends to be paid the value of it's margin of product is high. And so you see a substitution of labor that is paid the value of its contribution, it's substituted out of production functions and its place is taken by labor that's paid less than the value of it's margin of product.

So the issue we're discussing here is really--is comparative advantage the basis for free trade? If not, what is? If comparative advantage is the basis of free trade, how can it exist when the factors of production are as mobile as goods, that is, where does the relative advantage lie when the factors of production can move to where their productivity is greatest? So, it's clear then in Ricardo's own words the model breaks down under the conditions that we currently see in the world.

And this is the issue that we're trying to raise. We don't have a solution. We don't know what--in fact, we may be wrong. We're perfectly willing to admit that we may be mistaken in the way we see this. But we have yet to have it explained to us why we are mistaken. Generally economists are in denial. They go into denial because they're very protective of free trade and they learned throughout decades, you know, that you defend it. And they learned that anybody that says anything about it is a protectionist and should be slammed down. And so, you can't get engaged with them. It's very difficult to get them engaged.

But I hope I made it clear what we're really asking. Again, do the conditions on which the theory of free trade rest--do they hold when factors of production are internationally mobile?

Now, of course, some factors can be mobile. That's all right. But the question is whether all of them are or so many of them are that the principle is eroded and there's no basis for relative advantage. There's no basis for each country to specialize in what it can do best and then trade.

In many of the things that we've noticed and discussed, it's hard to see what the trade is. It looks more like substitution of one form of labor paid the value of its margin of product, it's substituted out of production function and cheaper is substituted in.

Now, I don't know how economists can describe that as the workings of free trade, it's a confusion in my view that they may, between the free flow of goods and the free flow of factors of production. In trade theory, these things are different. If you look at Kindelberger's text, for example, he discusses these things quite separately. And the mobility of capital, necessary for comparative advantage, is mobility within a country, it has to be able to move within a country from where it hasn't a relative advantage to where it does, not out of the country.

So that is my summary of the economic aspect of what Senator Schumer has noticed and is experiencing.

MR. NESSEN: We'll come back and we'll talk a lot more about that, but I want to turn to Tom Donohue. Paul Craig Roberts says we don't have a solution. Do you have a solution?

MR. DONOHUE: I think we have a constantly moving problem: challenge and opportunity with which we have to deal. Now, of course, as somebody that--by the way, Happy New Year, I'm glad to be here. This is the second time today, I've been with a group of people talking about some of these issues. And I come very well equipped because I have a great staff and so I have all the right things to say and I'm going to ignore most of them.

I thought that the--first let me say that I'm very happy to do this. I think this is very much worthwhile and I would rather see this discussion take place in an inquisitive environment than on the campaign trail with a dozen people running for President of the United States with all their own views on trade. As I listen to a lot of that, I wish to scream out from time to time, if I accept your views, how would you do that? And that is immediately when things begin to move in different directions.

Now, let me see if I can tie two or three different things together. First of all the issue of comparative advantage is one that is fundamentally changed by the points the Senator made. Money, information, and people and ideas spin around this world at the speed of light. And people, at the speed, sometimes of sound. And this is an extraordinary--extraordinary circumstance.

I, by the way, serve on four public company boards, so I have some sense of the pressure that's on corporations. I'm on a telecommunications board and you put up on the wall the month's events and while you watch, before you finish the meeting it's all changed. People are looking at the telecommunications companies and saying what happened to all of their telephone lines? They're going away every day.

I finally took an older fellow on our board--and I'm old--so you can imagine how old he was--I took him over to the window and I said look down there on the street, it was lunchtime. I said, what do you see? What do you mean? I said, everybody's walking along like this and the ones that aren't are walking like this talking to themselves because they have a thing in their ear. Those people aren't going to have a home telephone. Young people say, why do we have a home telephone, we don't get the messages?

So, we're living in a radically changing environment in terms of the issues of the Senator raised.

Second, the demographics between the West, as we understand the Western world, and the demographics in the rest of the world are fundamentally different and challenging. We, by the way, in this country, we look at our demographics and we get very frightened because we say how are we going to be able to afford all these people that have now decided--you know, we had a covenant between the government and industry and everybody that was going to retire--we said, look, you work, you retire, you go on a cruise and you statistically die and in the meantime, we'll provide you with all of this coverage of healthcare and pensions and all that sort of thing.

Well, that was great until they decided not to statistically die. And at the same time, at the same time, the American business community broke their covenant because now, and I think the exact numbers, because they're sort of fun, I talked about them--25 years ago, it took General Motors 454,000 workers to turn out 5 million cars in a year. Today it takes 118,000 workers.

Now, this is creating a series of circumstances that require you to re-look at the whole fundamental issue of how does this process work? Now, first of all, in part, we're guilty of creating this thing. For 50 or 25 in a great sense and 50 in a lighter way, we've been saying to the rest of the world, listen, you guys gotta understand it, we have a great comparative advantage. We're smarter than everybody, and we have better education, and we have better technology, and you guys ought to get in the boat. Come on, let's go, we're all going to free trade, we're going to open up markets, we're going to try and find forms of government while, maybe not democratic or not intrusive on enterprise. We're going to encourage education. And they did it. How dare they do it? After we've been saying this for so long.

And then what happens, as the senator says, and as Craig says, then they go out and educate all these people. And they're smarter than can be and because they're not in as sophisticated, as matured, as advance society, they figure out that at $20,000 or $40,000 a year, they're gazillioniaires and they're talented. And now they're competing with us and how dare they do what we've been telling them for 50 years they ought to do. It's a fascinating experience.

Now, the demographics are going to continue to change. That's why I'm very pleased and surprised that the President, today, is coming out with a more aggressive posture on the question of how to deal with ten and half million, he says eight and a half million illegal workers in the United States?

If we send them home, we shut down the deal. Why is it? Demographics. It's the one sort of science or analytical process that doesn't lie. If you weren't born 21 years ago, then you're not here as a 21-year-old worker today, unless you're an immigrant.

Now, at the Chamber, we've got a fascinating set of circumstances going on. Our chairman this year is an American Indian, in part. Other than that, the rest of us are immigrants. And it's like moving to Potomac out here. Once you move in, you don't want anybody else to come. You know, it's too crowded here, don't-- So there's a great, there's a great reaction against immigration. I mean, why do you think Arnold got elected out in or overthrow and then got elected in California. It wasn't about all these ethereal issues. Part of it was driver's licenses for immigrants.

Now all this is part of trade, by the way. All this is a part of the fundamental issue of what's going to happen in Japan with a negative, move it, negative population growth and everybody's getting old and they're going to come here, Senator, and get all their money out of Wall Street and bring it home to support those people.

What's going to happen in Germany, in France or what's going to happen in Italy? As a matter of fact, I saw somebody the other day with a little equation at the rate the Italians are going, notwithstanding the Pope, there won't be any Italians in 50 years or something, you know. It's a fascinating-- So it is this demographic environment that in the Western world continues to shrink. Now what's happening--as the Senator and Craig indicated--what's happening in what we have known as the developing world?

They got all kinds of people. They're educating them. They all want to work. A lot of them want to come here. And the ones that can't come here want to connect with us.

Now, what's wrong with that philosophically, because we told them to do it? Now they're doing it. And they work like hell. They're very, very competitive and they have a demographic issue that's on the other side.

You take Mexico, by the way. You take, and as the Senator indicated, they, at present, don't have as high value and high education and stuff. But if you put those two populations together, you've got the perfect population. All their folks are under 25, all our guys are going to be over 55, makes a lot of sense.

Now, this is a fascinating time to look at the trade issue. Now, if I were out on the stump, I'm going to go out and tell you all the reasons that we have to do--we have to open markets. We have to--why do we want to deal with the Chinese? You can't figure that out? It's mathematics. They got a billion 3 people. You know, only four percent of the people that buy stuff life in the United States. So, we're hanging out in China, in India, and all those kind of places because we want to sell stuff to them. And we want to use their people to fill in for where we have a void.

One of the real issues on the high end people to perform the kinds of jobs the Senator's talking about, you know, that may be going to India, is, tell me. And I get around to the universities as the Senator does and Craig's at one. And I guess you're at Stanford, as well. You know, go, tell me who's in all the high-tech programs, there? Who's in chemistry? Who's in physics? Who's in computer technology? Who's in advanced mathematics? Who's--well, if we send all the immigrants home, that's nobody in there. So we have this whole circumstance of not-intended, you know, events because of what we do.

I'll give you just another little side deal because I want to show you something that's happened. Twelve years ago, we started a major effort in this country to get people to use natural gas because it's clean. If you use it in fixed source, to generate energy, you know, it cleans up the air, this is wonderful, we really want to do this. We're going to use it, even we're trying to use it in cars, we use it in homes and everything.

But then, the other side of our society said, but you can't get it here. You can't get it in the Rocky Mountains, you can't get it off the West Coast, you can't get it off Florida, you can't-- So, what happens, we get more people using it, we can't get enough of it. We can't build pipelines, the price goes up. Now, the natural thing to say is the price goes up, people go back to other sources or they buy it overseas. Not what happened.

Here's what happened. Here's a trade issue for you. The chemical industry. 12 years ago, was our biggest commodity export. We had all kinds of people in this country working in the chemical industry. When the price of natural gas tripled--and by the way they're competing with the chemical industry in Europe and Japan and other developing places around the world--what did they do? They moved to the source of the natural gas. Because remember we can't drill it, we can't pipe it, we can't get it. So, within two or three years, the largest commodity import in the United States is going to be chemicals.

So, I've sort of rambled about this, but I--and I'll give you my--I have to end with my minute on you know, goes with what I do. But I think the Senator's on a--and Craig are on a very interesting question. The deal's changing. We've got a demographic situation that is pushing us in directions of where are markets, where are skills, where are workers?

We have a whole series of things that we do in this country that drive us towards moving in that direction. Both on the positive sense to command markets and on the negative sense because if I stay here, I'm sued, as you've been helping us work on, Senator. I'm regulated to the tune of $200-- or $300 billion or trillion a year, depending on you take overregulation versus regular regulation. I've got a tax system that doesn't encourage me to operate around the world. And so I applaud the suggestion that these guys made. That we really need to go and look at what's going on and figure out how we position ourselves in the years ahead.

And I want you to--in fact, I'm even going to forget the commercial--I want you to think about three questions: First of all or three issues: Every day companies make decisions. Their boards, their management, their investors, their critics, the stock market, every day they make decisions. And what those decisions are driven by is the need to get raw materials, the need to get talent, the need to compete, the need to get in the markets, the need to keep your stock price up and keep your job.

Forget the ugly stuff that 15 or 20 out of the 17,000 public companies have done to embarrass the business community or lock those guys up. And there's a clear difference between crime and, you know, restating accounting issues after all the government restates their stuff every three months. So, you know, we've got those kinds of problems.

But if you look at what--every day companies make decisions. And they are forced into many decisions that put them into the world market to compete, because if they don't go there, somebody's taken all the business.

Now, here's the real interesting thing: Every day people make decisions. And I've got, you know, a wife, who's very bright and probably be closer to folks that would be very socially conscious than the business community might be, but she makes decisions every day. And they're absolutely in conflict. you know, she says, I think we ought to work hard to have American jobs here. That's right. And so, she buys a foreign car. Now it happened maybe to be made here, I'm not sure, I think it was made here. But why did she do that? Quite frankly, because she believes it's a better product for which she's going to get longer return and which is safer for her. Now that probably is less true today than it was 15 years ago. But she makes that decision.

I had some people over the holidays were going on and on and on about jobs going out of the United States, except they shop price. All the time, they want to go to Wal-Mart, they want to go to Legget's, they want to go to, you know, they want to get on the Internet and buy, they want to do all that sort of stuff. And I said to them, hey, what about what this is going to do to jobs. I was giving them a bad time, obviously, I'd had a few--and [laughter] -- well, you know, it's the holidays.

But people make decisions every day and their decisions are often in conflict with their values. Their values of clean air; their values of strong regulation; their values of limiting the movement of immigrants; their values of protecting American workers; and then they go out and behave in a way that is 180 degrees away from what they say their values are.

And the final question is the question? And these gentlemen raised it in the beginning. They said, we don't't' think this system is working as intended philosophically; intended practically; and we ought to think about it. And I absolutely agree with them.

And then I add the final question: What should we do? You see, it's great to say we ought not do this. It's really tough to say what we ought to substitute it for.

So, I would suggest, just to get the talking going well, I would suggest that the fundamental position of open markets, of competition around the world, fair competition, of seeing the value of trade in terms of creating rules-based systems around the world that rub themselves off in putting like the Chinese in a rules-based system and have them closer to the issues that we think are valuable--I'd rather stay here while we figure out what to do. And, by the way, I'm willing to associate myself with the figuring out, instead of reacting to the Pavlovian suggestions that we're getting in the political--you know, lock the door and don't let everybody in. Have you ever stopped to think we're losing direct foreign investment to others. The EU is a larger--and particularly with the additions will be a much larger economy than us. And if we get too independent and too insular a lot of people will ignore us.

So, let's take up the suggestion to find a better way to do these things. But let's do it from the strongest position we can hold while we get there and let's ignore folks that want to throw the baby out with the wash water giving us unintended circumstances and situations that none of us wish for.

MR. NESSEN: Thank you, Tom. I think we'll spend quite a bit of time today talking about what should we do?

We want to hear from Lael, but before that, I want to ask you one very quick follow-up question. I take it that you don't think that the campaign trail or the political arena, generally, is a place where this kind of serious conversation or approach to this issue is likely to take place?

MR. DONOHUE: First of all, please don't laugh, I'm not a politician. I've never run for office. We are engaged in the political process. I have never found serious, in-depth discussion in a campaign. What one does is do the necessary polls to see which words and which issues trigger the greatest amount of votes to achieve the most desirable end result. That is not generally a good place for a serious debate.

You know, some of the very best people in the political business will tell you you want to find out who's doing well in the debate, turn the sound off. Well, that's very true.

MR. NESSEN: Yeah.

MR. DONOHUE: I mean, you can see, immediately, the Senator, thought of three or four circumstances when I said that where people--well, look at George Bush I, you know, he was not comfortable, I mean, Clinton's one of the best speakers movers around you know up on the stage, just people looked at it. So I don't think that's the place to have--I think this is a good place to have a debate. I think the Chamber, when we're doing our foundation and our thinking thing is a good place to have a debate. When we're doing our. you know, when we're selling our stuff, that's not a good place to have a debate, we're trying to win.

MR. NESSEN: Lael, have you got any answers to Tom's question, what should we do?

MS. BRAINARD: I might. First let me just say, I think this is a great debate to kick off the year and I think we owe Senator Schumer and Craig Roberts a debt of gratitude for putting the subject on the table.

In my own view, services off-shoring is going to be the next big thing in the great American globalization debate.

And let me talk a little bit about whether, in fact, it is markedly different from what's gone before and then turn to this question about what should we do about it.

First, let's talk about the facts. The discussion's very short. We actually know very little about this phenomenon of companies outsourcing their services and their business processes offshore. The data simply isn't in yet. And, in some cases, the government doesn't even keep it. From what we know, so far, not a lot has happened. Goldman Sachs has an estimate that puts it at about half-a-million job losses over the last three years. That represents about 1/10 of one percent of GDP.

But if you look at the entire category of telemarketing and customer services, that's 2 and 1/2 to 3 million jobs, that entire job category could be put at risk. And any corporate executive you talk to, you know right away that this is just the tip of the iceberg. So, I would submit we are actually having this debate at the right time for a change. And the other trend that's absolutely clear is that this phenomenon is moving up the value chain at a very breathtaking pace.

Now is this services off-shoring, is this phenomenon really a challenge to everything we've learned about trade? In many ways, I would actually say, it's just a logical continuation of what we've seen in manufacturing. Prior to that in agriculture. There is a relentless pressure in a market economy to drive down costs; to take any part of your production process that you can de-link that is not absolutely central to your corporate core value and move it to the cheapest provider, the cheapest location. This is very old news in manufacturing.

We also have seen this process taking place, not just outside our borders, but don't forget what happened in manufacturing? Manufacturing moved first from the rust belt, hence the term rust belt, to the sun belt. And then it went overseas. And services, to a large degree has done the same thing.

What is really different, what feels different about this phenomenon is that services was, traditionally, the category of production that economists considered non-tradable. And why non-tradable? Mostly to do with how the activity took place. What's happening right now is not mostly the result of policies taken here in

Washington, it's mostly the result of a coincidence of forces. Digitization of information; the build up of high-speed data network; much improved band width in places like China, in India; and higher education in those countries, which is completely out of our control.

So, for the first time what we're seeing is white-collar jobs being subjected to foreign competition at a small fraction of the cost. Is this a matter of concern? You bet it is, especially, especially for those like myself who believe that a strong, rules-based international system of trade is absolutely vital to American economic dynamism. And to our foreign policy interests.

And I think that it would be great if, unlike the last several rounds of the trade debate, policy makers actually got out ahead on this issue, like Senator Schumer is doing with thoughtful proposals, rather than playing catch up once the policy options are very limited.

But there are two things I want to just say to put this into context. First of all, there is a tendency in this debate, not by any means the people on this podium, but in this debate to kind of all prey to the notion that somehow the loss of a white-collar professional job is more concerning than all those losses we've seen over the years in manufacturing.

Let's be clear, it's not any less scary or unfair to those individuals who suddenly find that all of their skills, all of their investments have dropped in value.

And the other think I think is important: Although it may be the first time we're seeing white-collar professional jobs really meeting up with competition from overseas, the insecurity in a lot of the professional categories is, by now, a wellestablished fact. Don't forget the waves of downsizing or reorganizing. Technology has already played an enormous role in changing those jobs.

Just think about financial services back offices. Before we had this debate, we had the debate about the moving to Hoboken out of New York and then, out of Hoboken, New Jersey, all over the United States. When was the last time you interacted with a human bank teller or a human switchboard operator?

And we all know that the Internet is making inroads into a whole host of occupations: travel agents, stockbrokers, mortgage brokers, accountants.

So, let's get quickly to this issue of what should we do? I don't think we know all the answers yet. Anyone who's trying to sell you a solution that we can somehow stop this phenomenon is absolutely misguided. But anyone who tells you to sort of, don't worry, be happy or we don't have any tools, I think is similarly misguided.

The first set of proposals, let me just put a bunch of things on the table then we can talk about them.

The first set of proposals, I think, have very much to do with the kinds of things Tom was talking about. Making America an absolutely premiere location for high-value activities, whether those be in manufacturing, in services, or agriculture. That means looking at tax incentives. It means looking at the sharing of health burdens. It means the whole regulatory environment.

Secondly, we do need to look at our trade agreements. We do need to make sure that they're balanced and fair. And we need to make sure they're enforced. Nobody in India, I don't think, is fooling themselves that they're going to continue to enjoy the kind of open access into our services markets if we don't get a more balanced set of services commitments on the part of India. Just to give you a, for example.

Third, now let me put some stuff on the table, that's a little bit more controversial. Manufactured goods all have country-of-origin labels on them. This gets back to this whole issue about consumers making choices based on their values. We've got to look at this issue in the services area. Should call center employees identify their location? We've got to look at that issue. And the same is going to be true of when your x-rays are analyzed overseas or your payroll information is processed, that's a right-to-know issue that we should be looking at.

Another issue, which I think is going to become increasingly important is the question about oversight of things like privacy, security, and consumer protections. When services are being produced in jurisdictions where professional credentials are different or where regulations are different. If radiologists in India increasingly are going to be analyzing our MRIs, at some point, it's inevitable that we're going to be needing to look at the credentials of radiologists in India and seeing whether they're comparable to the ones we have here.

Five, is the obvious one, does this mean, less emphasis on education, less emphasis on science and engineering? Absolutely not. In fact, the way India and China are getting into this game is by putting emphasis on skills, on science, engineering, and we don't do it comparably here. Every measure you look at, we don't do it comparably here.

Sixth is cushioning those who lose out. The one thing we also know from trade is that it is redistributive. People lose in trade and because our social safety nets here are so thin to begin with, the resistance here is greater than it is in some of the other industrial countries. There's a whole host of things that we need to do better and to make those things available for the first time: wage insurance; trade adjustment assistance to services workers.

And, finally, let me stop with the thing I started with. We actually need to get a better handle on just how big this phenomenon is. And that means quickly getting the government agencies that collect data to collect better data and more targeted data.

So, let me just sort of conclude with one thought, which I think gets back to the points that were made earlier. The really big, new news here is that we are facing the prospect of integrating two massive new labor forces into the international economy. And that is primarily based on policy decisions that are being made in those countries not here.

What we're discovering is that those adjustment pains and opportunities associated with that integration are going to reach into a far broader set of job categories than anybody ever anticipated.

MR. DONOHUE: Ron, can I just make one point, please--

MR. NESSEN: Of course.

MR. DONOHUE: --actually one and a half. I think it's good to look at the job loss. I think next to it we ought to look at the job gain. There have been a lot of job gains here because of things that are being done and services provided.

The second thing is, which I really think is very interesting, let's assume, just for a minute, we shut the door and we weren't dealing with these things around the world and we look at the manufacturing business in the United States. Manufacturing output's grown 40 percent in the last ten years. But it gets a little scary when you go into a factor that used to have 1,500 people in it and there are four guys running an Nintendo game and the whole factory is working, robotics, computerization, it really is--it really is quite something and you look at the restructure of the steel industry in this country. When they restructured it and put the money in it, they basically took a lot of the people out of it.

It's sort of what happened over on agriculture. And I think it's important to understand that we have gotten so much better at doing what we do. Forget China; forget India; forget everybody else. That we are doing things to be competitive here and around the world with far, far fewer people. There is a terrible problem that we don't' think about there. And that is that now that we have far fewer people, how are we going to support all those other people that used to work here. And then you can start talking about the trade stuff.

But a huge amount of loss of manufacturing jobs we did it, we did it ourselves because we were smart, we used technology, we used computerization, we did outsourcing in the United States, we did all this kind of stuff. And we look at it and we ain't got anybody to blame but ourselves.

MR. NESSEN: Well, I want to follow-up on a couple of Lael's specific suggestions. But let me throw out this general question first. Why does it seem that there's more concern, including your op-ed, which has obviously touched off a serious discussion. Why does there seem to be more concern about the loss of jobs by white-collar workers, back-office workers, radiologists, as you cite in your piece, software developers, as you cite in your piece? Much more concern in the beginning of a national debate that I don't think happened with the loss of factory jobs?

SENATOR SCHUMER: Well, first, I guess, I would disagree, I think it did happen with factory jobs. Certainly, in up-state New York where there were a lot of factory jobs. Maybe it wasn't heard as clearly in Washington.

But I think it sort of misstates and this is an important point and it relates to what Lael said, too. We are not saying, oh, this is white-collar jobs, that was blue-collar jobs, this is different. We are saying this is high-value-added jobs, which have traditionally stayed here. Whether it's the guy who works in the factory where it took four years of computer training to work 16 robots at once or it's the computer programmer. And that is the key point that's different here

It is very easy to say, oh, well, what happened in manufacturing will happen in white-collar. We are simply--what happened in white-collar, basically, was, they tended to be, the newer jobs tended to be higher-value-added jobs. When, because of communications, because capital can flow freely, instead of it taking 15 or 20 years for those jobs to be exported, the minute some genius on Wall Street or in California thinks this up, it's all done over there.

Now, that's one--and then it affects, you know, there are lots of jobs that won't leave, as we mentioned in our piece. Radiologists, may leave, figuratively speaking. Internists won't, because they have to look at you. You know, you can't--it's very hard now, maybe they'll figure out at some point some mechanical fingers and mechanical eyes to look at you that way, but at the moment that's even beyond what we can see.

And then there are a lot of white-collar jobs that have to stay here, you know, I mean, in New York City, one of the great ladders up for immigrants are jobs in restaurants. And who's eating in those restaurants? All the sort of Wall Street people and advertising people and lawyers who are making more money. But if those jobs go, the high-end jobs, so do the low-end jobs.

You know, and if Goldman-Sachs ends up just being the partners who want to live here, but everybody else, those 400 people stay in New York, but the other 10,500 are all overseas, whether they make $500,000 or $20,000, that's the change here.

So, again, the admonition is this is not just, oh, the natural progression. Agriculture to manufacturing, to white-collar jobs. This is, rather, the basic theory that we have posited, we have bet the ranch on here in the United States for a long time, which is, well, the highest-value-added jobs stay here. Because we're the best educated, we have the, you know, that system, but they go or they never even start here. That's the difference.

And, in fact, and Craig pointed this out to me. Two little points that I don't know if they matter or not, but just to think about. Just in the recent job growth that we've seen over the last three, four months--the overwhelming majority of those jobs were the more poorly paid jobs, not the higher-end jobs. Number 1, that's sort of different. And so, maybe the higher-end jobs are going more and that's a difference. Well, I'll leave it--there was another point that I wanted to make, but I don't want to monopolize here and I'll make it in another.

MR. NESSEN: Well, I want to follow-up on one thing you said about education, Lael, you listed that as among the things to think about. The response to the loss of manufacturing jobs used to be, well, the people who worked on the assembly line are going to have to go back to school, get more training, more education so they can do the higher-tech or higher-end jobs as you say of the future.

Now that the higher-end jobs of the future are also going overseas, what happened? Does the education equation still work?

MS. BRAINARD: Let me just say one thing about job categories, first of all. In terms of where have we been creating jobs recently, don't forget the technology boom-and-bust cycle. Don't forget the recession. So I think there's a lot of things going on in this economy that complicate what we can read.

But, as Cathy Mann at the Institute for International Economics has shown, if we look at recent numbers, end of 2003 numbers, compared with '99, so we're trying to kind of move outside of the business cycle, we actually saw, 9 percent increases in business and financial categories. We saw 6 percent increases in computer and mathematical. We've seen employment pretty stable in engineering. And where we've seen the tremendous losses are really in manufacturing and in management, interestingly.

In terms of this issue of education, the--what's happening, I think is an incredibly accelerated cycle, in terms of where is the highest-end innovation taking place? Where are there pockets of specialization that the U.S. is going to master. And so the notion that somehow there's a generic linear amount of education that, you know, the more education you get, you know, the more kinds of jobs you can do is wrong. We're simply going to have to keep moving the work force, whether it be adults who are going back for retraining or younger kids who are preparing before they enter the work force into areas that continue to be vital to the economy.

And they're going to change. It may be--it may have been IT yesterday, it may be biotechnology tomorrow. That requires a tremendous, tremendous continued investment in our nation's work force and we don't actually have a very good system for doing that right now.

MR. NESSEN: I think you were also agreeing that the loss of white-collar jobs is not as great as, perhaps--

SENATOR SCHUMER: Well, can I just--I know that that is true, not question. What we're saying is, what's causing 2 percent of radiologists to go overseas or 5 percent of high-end, high-value-added computer programmers to go overseas is not the peculiar nature of those two professions but, rather, the fundamental change in broadband with 50 million new educated, highly educated people being put into the labor market. Lael's exactly right, it's brand-new labor markets being thrown together.

And is this the tip of the iceberg? That's the question we're asking. And if it is the tip of the iceberg, we ought to be thinking about it and preparing about it to see what we should do. It would seem logical that it is, unfortunately, because the fundamental conditions that allowed the first few to happen, there's nothing to change the next whole bunch to do the same thing.

The head of a big insurance company told me that, except for the sales people, who are like the internists, that if he's doing his job in 10 years, 80 percent of the people who work here in American, the low-end, middle-end, and high-end should be overseas. Who's replacing them?

MR. DONOHUE: Just one sentence. One of the reasons CEOs are driven in that direction is that for the last ten years, you've not been able to get any price pressure at all. You can't put prices up on anything. The American people won't sit still for it, you see. So what do you do if you want to keep your stock up and keep your job, you look for ways to become more and more and more productive and part of that, a small part of that is to--

SENATOR SCHUMER: And I'd just make one other point, I know Craig is eager to say--one advantage of this, which ought to be talked about -- equation is goods are going to become cheaper. If you're only paying the radiologist $20,000 and you're only paying the computer programmer $25,000 and there continues to be cut-throat competition, which is what Adam Smith wanted, I mean, my problem with the free-market system is not its fundamentals, but when things get in the way and prevent that competition, we see a lot of that in the political realm right now. But once you have that competition, the price will come down. And maybe the scenario is, incomes go down and prices go down and standard of living stays just the same. I don't know, but that's a possible scenario.

MR. NESSEN: Paul will tell us--Craig will tell us.

MR. ROBERTS: Oh, you see, the dollar goes, too. And when the dollar goes, the prices will go up. I think that the real problem is different. You see, young people are far more aware of the problem. I'm talking about seniors in high school, freshmen in universities. When I talk to them, they know more about it than any of my economists friends, no matter how distinguished they are.

And the reason they know more about it is they spend a great deal of time searching for an occupation that can't be wiped out underneath them. And they are having great difficulty in finding one. And, last night, my son who's just home from the university, handed me the current issue of Popular Science, he was going to go off to be an engineer. And here in the current issue, the February issue of Popular Science, it says, nearly 750,000 high-paying jobs in high-tech industries have fled the United States in the past two years, says the American Electronics Association. Lost jobs, paid salaries averaging $66,300. Foreign workers receive far less. India leads in computer-related jobs. China has targeted electronics manufacturing and Russia has become the lowest-cost supplier of engineering services.

What they find is that there's no career in engineering, civil engineering, because it's hands-on and has to be here. Every other engineering can be done offshore.

They're finding the same thing with architecture. Wherever they look, people sit around and say, oh, education's the answer. Well one of the trustees of Georgia Tech told me recently that the president of Georgia Tech is convening a study to see if engineering schools in America have any future because the students don't see any reason to take engineering because they don't expect there to be any jobs.

The problem--to come back to what the problem is. The problem is very simple. Labor that is paid the value of it's margin of product, and that is, it's paid the value of it's contribution to output, cannot compete with equally competent labor that's not paid the value of it's margin of product. And that is the situation that we have now today interest he world. That is the situation, period. And it has come about because factors of production are as mobile as traded goods. And as Ricardo said, when that happens, there's no longer a basis for comparative advantage.

There is only absolute advantage. Where is the productivity of capital and technology highest? Where labor is cheapest. These are simple facts, they're in all the economics textbooks. Why won't economists acknowledge it?

See, we live in a delusion. We think everything that's happening is the workings of free trade. We all know free trade is good for us. We've all learned this. And we live in the delusion that what is going on is free trade. It is not free trade. It's factors flowing to where the absolute advantage is greatest. That is not free trade. That is not free trade. What is happening is free trade. We think it is. So we don't worry about it because we've all learned it's good for us. If you lose this industry, you get another one. That is not what's happening. Somebody has got to become aware of this.

You know, it can go--it's going very fast, it's very rapid. If high school seniors and college freshmen are aware of it and Nobel Laureates ought to be aware of it.

MR. NESSEN: We're going to take the audience questions. I want to ask one other very quick question before we do that. Just to follow-up on one of Lael's other ideas, get a very quick response from the panel to the idea of country-of-origin labels for services. Would you support something like that, Senator?

SENATOR SCHUMER: I mean, that's free market, people should have full knowledge. And if I want to make a decision to pay a little more to buy and American product, I should be able to do it. And there are advantages. I mean, we just had an example. Here's, this is classic. In--we passed, at the behest of the ranchers, a what's called COOL, country-of-origin-labeling for meat. It's technologically feasible, which it wasn't, I guess ;ten years ago. And it was supposed to take effect within the next few months. The meat industry opposed it and in the big Omnibus Bill, which the Omnibus Appropriations Bill, which the House passed and the Senate didn't, they delayed it. Now, that's free market. Country of origin labeling is free market. Everyone wants to make up his or her own mind and even by the free-market model, if I want to pay more for an American-made good because I'm patriotic, because it might be safer or for whatever reason, I should have that knowledge.

MR. ROBERTS: But this was for services, so if you--

SENATOR SCHUMER: Either one, anything.

MR. ROBERTS: --so if you call a customer service office, they have to be--

SENATOR SCHUMER: How is that not consonant with free market, perfect knowledge?

MR. ROBERTS: But it won't do any good, it's just, as we already know, things are driven by lowest costs. So none of these things do any good. The question goes back--

MR. NESSEN: You have Tom's wife who goes and buys the--

MR. ROBERTS: --to the same point. We think what's operating as free trade, it is not. There's no basis for comparative advantage when factors of production are as mobile as traded goods.

MR. NESSEN: Tom, do your members support country-of-origin labels on services?

MR. DONOHUE: Well, first of all, I want to stay on the question of [inaudible]

SENATOR SCHUMER: I didn't mean to get us--

MR. DONOHUE: No, no, no, I want to point out something very, very interesting. We are going to go from where we were a couple of months ago to country-of-origin on the cow, not on the end product, because we need to know now where that came from so that we can protect ourselves, you see. So, I think this goes back to what Craig and the senator were saying. Things are changing while we sit here and watch them. You know, the senator is concerned, rightfully, about what happened in New York City to jobs, but part of what drove jobs out of New York City is after 911, everybody sat down and said, we've got to split it into three point deal: what we keep in New York; what we send to Hoboken; or Buffalo; and what we're going to send to India. We have got to spread ourselves out to protect ourselves.

I think the country-of-origin stuff, there is some value in that. A lot of it, you know already, although you think you know. Because you say, well, I'm buying a Chevrolet. That must have been made in the United States. Yeah, maybe it was, the hood was put on, but the parts were made in Canada or Mexico. It's very hard to know where country-of-origin is in manufacturing because it's aggregated from all over the world.

Services, I don't duck things very often, let's keep talking.

MR. NESSEN: All right, we have, if you have questions raise your hand. Wait for the microphone to come to you and stand up and identify yourself. Bob, you want to go first?

MR. SOLOMON: Robert Solomon, Brookings. I wanted to address a question to Craig, if I may, first of all, I don't understand why you say this is not free trade. You may not like the effects of it, but I don't see what's unfree about it. My main point--my main question is the following? You've described a process that's very, really happening, and I think you've identified some real problems. But one thing you did not address is what are the dynamic effects? What's likely to happen in India and China as time goes on? Are wages and salaries likely to go up in those countries and will all this tend to change over time? I'd like to see some discussion of the dynamic effects.

MR. ROBERTS: Sure, Bob, I'll be glad to. First of all, I say it's not free trade because free trade is based in comparative advantage, that's the basis for free trade. I'm using the word as it's used in economics and free trade is based in comparative advantage. And comparative advantage requires that the factors of production are not as mobile as the traded goods. And that condition, I'm saying doesn't hold any longer and, therefore, it is not free trade. It is not what Ricardo defines as free trade, it's not what Kindelberger and the textbooks define.

Now to come to your question.

SENATOR SCHUMER: In other words, to put in a sentence whether you define it as free trade or not, the theory of comparative advantage depends pretty fundamentally on the immobility of the factors of production and the latter has changed, whatever you want to call it.

MR. ROBERTS: All right, thank you. That's right. Now, what are the changes and the future changes? See what really is happening, any time absolute advantage rules over, you know, in place of comparative advantage, you have an international redistribution of income and wealth. That's what Ricardo said would happen. The English labor and capital would move to Portugal and produce the wine and cloth there. So, England would become poor and Portugal would become rich. That's what's happening. The United States is undergoing a redistribution of incoming wealth to India and China.

And what will happen, they'll become richer, we'll become poorer, somewhere along the way, the dollar's going to help us become poorer because the good that we're importing are going to cost more when the dollar goes. And so it is a big adjustment. And not only that, but there's something really bad that's going to happen. The ladders of upward mobility of the United States are collapsing, while we're importing of millions of Third World immigrants, many of them poor and illiterate. The ladders of upward mobility collapse, when the high-value-added jobs leave.

Then you get real political instability because the guys running the big companies who, you know, you get a complete break between the stock market and the economy, because the United States economy becomes less and less of any meaning to multinational firms. Their profits are made with Indian and Chinese labor. So you get tremendous political instability in a country where the ladders of upward mobility diminish, while poor immigrants poor in; the value-added jobs are leaving. It's not a very pretty picture. It will be challenging even for senators like Schumer to do.

SENATOR SCHUMER: I just would make two other quick points in reference to what Mr. Solomon said and I have such respect for him. Number one is just backing up Craig as I understand it and I caveat as I haven't read it--I'm calling hundreds of people about this just to try to get ideas and stir the pot. And somebody told me that Canes in his latter days backed off the theory of free or thought free trade might not work or was becoming not working, I guess, is the way he put it.

Second, very specific question that he asked, Mr. Solomon asked, is exactly right. What is the educational system? How broad and wide open is it in China and India? Does it get bottlenecked soon? And, if it does, then the lower price of an Indian software program or a Chinese radiologist, quickly evaporates. But it seem logical in countries that are so large with rapidly growing educational systems and lots of people who are eager to take advantage of those systems and able to take advantage, that it will happen. But this may be 20, 30 years.

I talked to a leading businessman, one of the smartest men I know, who has a company that has jobs all over the place. And by the way, you can't blame the company, they're supposed to seek lowest cost by the capitalist model, so they're doing what they're supposed to do. This has really got to be a governmental and even a world discussion eventually. But he said, oh, yes, the only thing that will change this around is when American standards are lower and--living standards are lower and Chinese and Indian standards are higher, so the computer programmer in America only gets paid, you know, the guy who had $150,000 I mentioned, gets paid $80,000 and the guy in India or China gets paid $60,000 and it's close enough that it's not worth $20,000 to go relocate it elsewhere. He said, that'll take about 30 years.

Well, that's not a scenario that I, who represent 19 million people all of whom want jobs want to sit back and say--and so I'm filled with a little anxiety about this and I want to, at least stir the pot so we begin thinking of solutions and his frustration, which is so palpable is real. And justified. Because these are--no one, just speaking for myself, and I don't know half as much about economics as either as the two of you. No one has given me a good answer to all these questions that I've been asking, other than faith. Well, it's always worked out that way in the past and there'll be new high-end jobs that we can't even think of in the future.

Maybe that's right, but what if it's wrong.

MR. NESSEN: Other questions, right here.

MR. ROSNIG: Dave Rosnig [ph] Center for Economic and Policy Research. I want to address a couple things really quickly. I was going to bring up the subject of Canes, he was actually--he backed of off free trade for exactly the same reasons that we're talking about today. For the very reason, he was concerned that the assumptions of Ricardo simply just did not hold. And for that reason, I don't see this as a new crisis, this is something that has been going on for decades.

Apart from the factors of production, there's another assumption that's of great concern and I think it's something that we can handle. It's that trade--these trade theories also rest on full employment. So, maybe is it, I want to know what the panelists think--maybe is it time for us to scrap this narrow-based theory and move to full employment, is that something that can help our situation here?

MR. ROBERTS: Moving to full employment, I mean, you're going to be moving to gradual more unemployment under this arrangement. Now, I do think that whatever Canes was thinking, this is a new situation because it took the Internet and it took the mobility of capital and labor out of the First World to make labor mobile and it certainly wasn't the case in his day. You didn't have any willingness for capitalists to move their plant and equipment out of England or the United States to China and India. And you certainly didn't have any ability to hire engineers or scientists or whoever via the Internet from these countries.

So, Canes may have been perceptive in seeing that the basis for the "Ricardoan" theory was going to be eroded with the passage of time, but I don't think it happened in his lifetime. It's a new phenomenon and it's happened because of the reasons the Senator identified.

MR. NESSEN: Lael, you were nodding your head.

MS. BRAINARD: I guess what I'd like to say is I very much associate myself with the camp that sees this as the tip of an iceberg and an issue that's going to happen and for which we need to have policy solutions.

I am a card-carrying economist and very little of the discussion today bears any resemblance to what I used to do at MIT. The reality is economists have evolved a great deal in their thinking on trade. And there are enormous issues associated with redistribution with trade. And I think there is a very heightened sense of awareness of that within the profession. And those are the issues that we really should be focusing on.

In an economy, in a political system like the U.S., how you deal with some of those redistributive issues. And in this particular case that we're talking about where we do have this massive infusion into the world economy of essentially a labor supply that we didn't have access to before in a lot of ways. How do we cope with that. I think those are really big issues. I don't think that, you know, somehow the field of trade must fundamentally change to deal with those issues. I think we've dealt with a number of those issues before.

On the issue of labor and capital mobility, it's always worth keeping in mind that the world was actually as integrated from a capital point of view before World War I, as it became in the 1990s. We didn't, again, see the amount of capital integration that we saw in the pre-war period that we--until the 1990s. So that's I think, very worth keeping in mind.

And don't forget on the labor mobility front, it is true, now that Internet and band width means that we can take ideas here and match them with minds far from here. But don't forget those massive migrations of actual people from the Old World to the New. So we have seen phenomena that are comparable to this. And, all of that said, I think we are faced with a very, real policy conundrum.

MR. NESSEN: Right here.

MR. DALEY: Herman Daley [ph], University of Maryland. I'd just like to say that I think that our panelists have raised an extremely important issue and that we've had governments both Republican and Democratic which have pushed free trade and global economic integration as a number one priority for quite sometime. They have shown that the standard economic logic that underlies that policy is wanting, is shaky, there's no basis for it. With free mobility of capital and labor, the whole thing collapses.

Now, while economists stop and debate that, I wonder if, you know, the question what to do? Maybe the first thing we could do would be to stop pushing global integration and free trade through our government policies. Let's declare a little moratorium on that, perhaps, have economists think about this some more and see if there's any other basis on which this policy can be based beside the one of comparative advantage.

Since we're all quoting Canes, I'll conclude with one little quote from him, says, the influence of economists, whose common sense has been insufficient to check their faulty logic has been disastrous to the latest act. I think we're in the latest act right now. on trade theory and I really congratulate Schumer and Roberts for bringing this to our attention.

MR. DONOHUE: All of us on so many issues, whether it's healthcare, whether it's international disputes, whether it's trade, whether it's science, whether it's education, we would all like to stop for a minute and take a breath. Because the fundamental realities that we live in a world where what is really most effecting us is the acceleration of speed at which things happen.

You think about people that work in government with responsible positions that are asked to make extraordinary decisions in questions from the press about things that happened six minutes ago. And about which they've had little or no briefing or understanding or--we are all spending, you know, we're spinning through an acceleration of speed in everything we do.

Now we could stop, maybe, on the trade thing, but we'd have to look at the EU. The EU now has 36 free-trade agreements. And we have five, and two or three of those are for fun. They're not serious. I mean, Jordan's a great thing, and it sent a message, but we don't trade anything with them.

So it's, you know, it is an issue that while we're doing what we're doing, in many ways, if you listen to the Senator and you listen to Craig and you listen to the professor, we are frustrated with the speed. But most of all, we don't want to talk about this, we're frustrated because we used to be the top dogs and in some ways we're falling behind.

And Americans don't like that stuff. By the way, it is the sort of reason that I can get a little comfortable with where we are. Because the great innovation, the great job creation, the great spirit in this country is not in General Motors and Hewlett Packard, it's in 20 million small businesses all over this country that are going to survive and fail and start again and survive and fail, create the inventions, hire the people, and they're going to be here long after these other guys are doing their thing.

But I understand exactly what people are saying. My goodness, look what's happening to us. We used to be in charge and now other people are driving the ball game. And we are going to have to figure out ways to be more effective.

I want to say one thing about economists. By the way, we've got a great economist at the Chamber, he can explain things in English. I love it. But, one thing about economists is they spend a lot of time trying to find, very natural, a lot of time trying to find an explanation for things that have already happened and are on the way to happen again. And somehow, what Craig is saying, which I respect, is could we stop doing that and race quick, three weeks down, three months down, three years down the road and get ahead of this thing so we can give some advice so that economists will make a very constructive contribution to what we ought to do next, not to what we have just done.

MR. NESSEN: Yes.

MR. ROBERTS: I'd like to say one last thing. Your things have unintended consequences. And Karl Marx pointed out that one of the unintended consequences of the enclosures was to create a labor market to destroy the feudal system. It led to the rise of capitalism. And what we may actually be witnessing now, the rise, the global economy is way out front of nation states.

When you created a global economy and you still have nation states, there's no way to redress the income and wealth redistributions. You said, early in our history we had the migration of industry from the North to the South, but we all had a way to make this happen. But when it crosses national borders and the economy's global and sovereignties are national, you see economic development changing the political system. And you may simply be seeing something like Marx described, where no one thought the feudal system was going to be destroyed, but it was. And it may well be that global economies mean the end of national sovereignties. You have to have some kind of a world government system. Otherwise, you can't handle all the imbalances that come from these highly mobile factors of production.

So that may be what is going to happen. It'll be beyond anybody's ability to do anything about it, it'll happen and there'll be tremendous dislocations, just as there was in the transformation out of feudalism to capitalism. And that may be exactly what's going on and no one recognizes that.

MR. DONOHUE: You know, Craig, that's very interesting.

MR. NESSEN: Do you have a time frame on that.

MR. ROBERTS: I keep saying the United States will be a Third World Country in 20 years.

MR. DONOHUE: That's a long trip. Craig, I think the thing you just described is, we can see a fascinating example of it in our own country. Forget the borders. Look what's happened in the movement of industry and production from the North and the East to the South and the West. Look what's happened to the change in the political mix in our country as that has happened--

MR. ROBERTS: That's true, but it's--

MR. DONOHUE: --in the demographic mix.

MR. ROBERTS: --but it's still, the labor can follow. If you're an American engineer, try going to China and getting a job. Within a country, labor can move with the capital and it's still producing for the same markets. But if you have a plant in the U.S. and you're employing American workers and you close it and move the plant offshore and employ workers, but you still sell in this market, then you are simply substituting out labor pay the value of its marginal product and putting in its place exploited labor and the labor's exploited because of the huge excess supplies of labor in those countries.

And how long does it take, what is the overhang in the Chinese labor market. It must be several hundred million people, it's probably as large or larger than the population of the United States. So, how long does it take for that to be absorbed? It's not going to be any instantaneous adjustment that brings all the wages into equilibrium all over the world, it just can't happen.

MR. DONOHUE: By the way, Ron, you asked me about country of labeling and think about with states. If we get into it to a certain extent, then we're going to say, wait a minute, you know if all the people that are answering my telephone are not in my state, then I want them to tell me, because the Senator wants the jobs, it's just for fun, I mean, we're going to deal with labeling around the world in fascinating way. But I think Craig's raised a great discussion. I'm here to say that the Chamber's ready to participate in that discussion. My idea is to see how we get down the road ahead of it. But we better start running fast, because it's moving.

MR. NESSEN: Well, I think that's a good place to stop and a good point to make. I think Senator Schumer and Paul Craig Roberts have called attention to a big issue, a serious issue, a fast moving issue as you say. We don't know what the solution is today, but what we have agreed on, I think, is that it's a serious issue that requires a thoughtful discussions--more discussions here at Brookings in the future.

Thank you all for coming. And thank you for beginning to take part in this serious discussion.

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