Trade and the Future of American Workers

On October 7, the Cato Institute and The Economist *held a conference, "Trade and the Future of American Workers," in Cato's F. A. Hayek Auditorium. Speakers included Sen. Chuck Hagel (R-NE); Harris Miller of the Information Technology Association of America; Brink Lindsey, former director of Cato's Center for Trade Policy Studies and now vice president for research; and Roger W. Ferguson Jr., vice chairman of the Federal Reserve Board. Excerpts from their remarks follow.*

Chuck Hagel: One of the great successes of America since World War II has been our leaders' realization that we have common interests with the rest of the world. Hence, the development of coalitions of common interest: the General Agreement on Tariffs and Trade, which is now the World Trade Organization; NATO; the United Nations; the World Bank; the International Monetary Fund; and dozens of multilateral institutions.

Leadership in the global economy is absolutely critical for America's survival. America's economic security and prosperity cannot be separated from global economic leadership. Free trade promotes stability and democracy everywhere by encouraging business and investment practices that contribute to more open societies across the globe.

Countries that trade with each other usually don't send armies across each other's borders. America's leadership in free trade, our leadership in helping countries develop, reduces America's security commitments abroad. Very simply put, it means we have to put fewer military divisions in other nations and therefore less money in our security budget.

Why? Because it's a fostering of development; which brings security; which brings stability; which brings responsible, open, transparent governance. Which brings market economies.

Meeting the demands of a global economy requires maintaining America's leadership in free trade, expanding programs to retrain workers who lose their jobs, and educating the next generation of Americans about what it will take to compete in a more competitive global economy.

Let's talk about productivity. Long ago, somebody came up with a stone wheel. Now, that was a very stupid idea, because the wheel displaced workers. It took jobs away from people. It would probably end whatever civilization there was at that time.

Well, it didn't. And from that stone wheel things progressed and developed to where we are today. And what's the lesson here? The lesson is that, as you develop productivity in technology and new ideas, you enhance economies, you enhance job prospects, and you enhance the ability to create better jobs.

I see a very dangerous protectionist streak developing in the Congress, in both parties, in the country. You can't have it both ways. You can't espouse free, fair, open trade and then say, well, I'm not sure about my oranges, or my beef, or my sugar beets; that's different. You can't say, we want the Europeans' and the Asians, jobs here, we want Toyota and Honda and Airbus, but we don't want to outsource jobs to India.

Sen. Chuck Hagel: "This is not the time to retreat from our commitment to free trade and market economies. This is a time to engage."

Take any trade treaty—take all the trade treaties of the last 55 years: America has prospered more than any other nation in the world as a result of those trade regimes. Have there been problems? Of course. Trade is not a guarantee. Trade is an opportunity. But if we undo the trade regimes that we worked so hard to build over the last 55 years, that will make for a far more dangerous world than we have today.

The world now is presented with some pretty stark choices, far starker than I think most of our policymakers understand. Free trade, fair trade, does not guarantee peace or stability, but it is one of the few verifiable, accountable paths to stability and security.

This is not the time to retreat from our commitment to free trade and market economies. This is a time to engage more than we have ever engaged with the rest of the world.

Harris Miller: The Information Technology Association of America was very pleased to publish in 2004 a major study that we did in conjunction with an organization called Global Insight. Prof. Lawrence Klein, a Nobel Prize–winning macroeconomics professor, led the study, along with Nariman Behravesh, also a well-known global macroeconomics expert. We asked Global Insight to try to answer the questions: What is the impact of offshoring on U.S. jobs? Is it true that this is leading to a decline in the U.S. workforce?

In fact, what the study showed is that, in 2003, because of the global sourcing of IT work, approximately 90,000 more jobs were created in the United States, and the study projects that by 2008 more than 300,000 new jobs will be created in the United States because we are using a global sourcing model for IT.

With regard to the second issue, maybe more jobs are being created—but they are lower-paying jobs, right? That's what we keep hearing. Again, the study shows that that is a myth. Workers, real wages have actually increased as a result of the global sourcing model and will continue to do so. Real wages were .13 percent higher in 2003 and are expected to be .44 percent higher in 2008 than they would have been without outsourcing. Not a huge pay raise, but, nevertheless, it shows that the idea that somehow global competition has an overall deleterious effect on U.S. workers' wages is just flat-out wrong.

Brink Lindsey: I would like to make a few points to try to put the offshoring issue in the broader context of anxiety about job losses.

Number one, job churn is a fact of life in a dynamic market economy. Every time you hear Lou Dobbs say that company X has shut down a factory or has relocated a factory overseas or that it has moved some operations to India, that tells you nothing about

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the overall state of the U.S. economy. Those anecdotes don’t demonstrate any kind of problem with American economic health. They demonstrate business as usual in a constantly changing American economy.

Between 1993 and 2002, total U.S. employment went up by about 18 million jobs. During the same decade, we created 328 million jobs and eliminated 310 million. So during the boom time of the 1990s, roughly 30 million jobs a year were destroyed. About half of those were seasonal jobs that had actually been created that year. So when you’re looking at layoffs, it’s about 15 million layoffs a year, even in good times.

Where does outsourcing fit in that picture? Outsourcing is a red herring when you’re looking at major sources of job churn in the U.S. economy. The Bureau of Labor Statistics recently did a survey of mass layoffs and found that 2.5 percent or so were attributable to moving jobs overseas. So if you completely eliminate outsourcing, you’ve still left 97.5 percent of layoffs unaddressed.

Number two, we have a double standard when it comes to job losses. Consider a hypothetical company that is looking at ways to cut costs in some back office function, say managing payroll. It has two basic options. Option one is to ship the job off to India, to outsource it to some firm that manages payroll and transmits the data back electronically for 50 percent cost savings on net.

Option two is to computerize the job—bring in some new hardware and bring in a few computer technicians, at a net 50 percent cost savings. So if the company chooses option two and computerizes it, everybody says, Yay! That’s progress in action. The information revolution marches on. We’ve gotten leaner and meaner. We’re increasing productivity. That’s the basis for higher living standards in the long run. Yes, some people just lost their jobs, but that’s the price you have to pay. We all know that technological progress causes some jobs to become obsolete. But in the long run, technological progress produces more opportunities than it eliminates.

But if the company chose the first option—well, that company would end up on Lou Dobbs Tonight as a Benedict Arnold company that’s “exporting America.” And yet, in both cases the company would be doing precisely the same thing. It would be figuring out some way to do its business at a lower cost. In other words, to improve its productivity. And that would generate benefits that ripple throughout the economy. But at the same time some people would lose their jobs.

We need to confront the fact that automation and technological innovation generally dwarf outsourcing as a source of job churn. Go back as far as you want and you can see a seemingly endless stream of jobs eliminated by technological innovation: longshoremen put out of work by containerized shipping, telephone operators put out of work by computerized switching, factory workers put out of work by robots, bank tellers put out of work by automatic teller machines, receptionists put out of work by voicemail.

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Now, the Europeans don’t have this double standard. They understand that competition of any variety poses a threat to existing employment. And they have grasped that nettle and enacted a whole gamut of policies designed to make it very difficult to get rid of existing workers. So they put their money where their mouth is. And as a result, they have double-digit unemployment and virtually stagnant private-sector job creation.

Point number three, concerns about running out of jobs are nothing new. Every time we have a recession we have a temporary job shortage. There is a growing gap between the number of people who want jobs and the number of jobs available. And virtually every time we have a temporary job shortage, smart people concoct theories for why the temporary job shortage isn’t temporary: It’s actually the dawn of a grim new era of permanent job shortages.

In the 1930s, “secular stagnation.” In the 1960s, the automation crisis. Computers would do everything and we wouldn’t have anything to do. In 1981, de-industrialization, the hollowing out of the manufacturing sector, the decline of the middle class, the undermining of the American manufacturing base. In 1991, the giant sucking sound and the downsizing of America. These policy bubbles emerge, predictably, with each economic downturn, but they have a long lag time. It takes quite a while for the bubble to burst. You might not remember that the *New York Times* made a big splash with a seven-part series on the downsizing of America in 1996, right in the middle of the rollicking Clinton-era boom.

And once again, now, we’ve had an economic downturn and we are once again gnashing our teeth about the possibility that we have run out of good jobs in this country.

Notwithstanding my last point, things are different this time. History doesn’t repeat itself. To some extent, we are in unprecedented circumstances. We have deep-seated structural differences, so that the pace of job churn may be increasing. A political scientist at Yale, Jacob Hacker, has found a big increase in income volatility today compared with three decades ago. We certainly have ongoing structural change in the nature of what makes our economy go and the structure of the job market in this country.

Frank Levy of MIT has drawn a distinction between rules-based jobs and face-to-face jobs. Rules-based jobs are ones that can be reduced to a set of preestablished procedures; you can write down on paper what that job consists of. Face-to-face jobs are either ones that require a physical presence or are so complex that you can’t specify in advance exactly what the job entails.

All rules-based jobs have a bull’s eye on them these days in the American economy. If you can specify exactly what the job entails, then the odds are that, before too long, either you will be able to find an Indian or a Chinese to do it more cheaply or you’ll figure out a way to get computers to do it more cheaply. And so we are definitely shift-

Continued on page 10

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POLICY FORUM *Continued from page 9*

ing away from certain types of employment and toward new types of employment. And that entails all kinds of challenges for various aspects of economic and social policy.

These are serious issues, and they need serious attention and creative policy responses. But blaming everything on outsourcing and pretending that the churn and challenges of a dynamic and changing market economy would just go away if we went back to some mythical Fortress America are a distraction from the real challenges we face. And that really is the final burden of such demagoguery. Not only does demagoguery lead us and tempt us to do the wrong thing, but, maybe even worse, it takes our eye off the ball so that we aren’t paying attention to doing the right thing.

Roger Ferguson: As you know, finding overwhelming agreement among economists on issues is difficult, but free trade is an exception. So what accounts for the apparent deterioration in public support for free trade over the past five years? The widening of the U.S. trade deficit may have exacerbated concerns about the country’s international competitiveness. More important, some observers have blamed overseas competition for the job losses associated with the economic slowdown earlier in this decade.

Without solid public support for free trade, achieving continued progress in reducing protectionist barriers, both at home and abroad, may become more difficult.

The public likely has a reasonably good grasp of the benefits of free trade. It is the perceived drawbacks to international trade that probably account for the ambivalence indicated in opinion surveys. Some of those fears may be overstated—for example, the claim that imports lower aggregate employment. But other concerns cannot be dismissed out of hand—especially the claim that trade leads to disruptions for some workers. Balancing the pain for a few against the lasting gains for the economy as a whole, economists generally view the latter as outweighing the former, but it is admittedly difficult for many individuals in American society to share that assessment.

Rather than arguing the merits of international trade in the abstract, advocates of free trade might gain more traction by arguing against concrete examples of protectionism. Consider several related and highly egregious consequences of protectionist actions:

First, by raising the cost of goods that are inputs for other producers, import barriers may destroy more jobs in so-called downstream sectors than they save in protected sectors. According to one study, the 2002 steel safeguard program contributed to higher steel prices that eliminated about 200,000 jobs in steel-using industries, whereas only 187,500 workers were employed by U.S. steel producers in December 2002.

Second, trade protection may lead to very large payouts to a small number of producers and hence is often inequitable. Any time a product receives import protection, of course, a relatively small number of domestic producers receive benefits—through higher prices—at the cost of all domestic consumers. On top of that, a disproportionately small number of sectors, and often a disproportionately small number of firms within a sector, tend to enjoy the gains from protection. For example, more than one-half of the antidumping and countervailing duty orders in place as of August 2004 were on iron- and steel-related products alone; by contrast, iron and steel producers account for less than one-half of 1 percent of total private nonfarm employment. As another example, according to a 1993 General Accounting Office study, 42 percent of the benefits to growers from sugar protection went to just 1 percent of growers. Although Americans favor policies designed to help the small farmer, much larger enterprises are also benefiting from agricultural trade protection.

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The disturbingly inequitable distribution of the benefits of protectionism is exacerbated under current law by provisions allowing antidumping and countervailing duties to be disbursed to the companies that petitioned for the duties. Those provisions, which have been ruled illegal by the WTO, lead to protected producers being rewarded twice: once through the higher prices stemming from the trade protection and again through the disbursal of the higher duties paid by importers. The distribution of those payouts has been extremely skewed: In fiscal year 2003, a single firm received more than one-fourth of the $190 million in countervailing and antidumping duties that were distributed to U.S. firms.

Import quotas (as opposed to tariffs) raise a third concern about trade protection. By restricting the supply of certain types of imports into the United States, quotas may benefit those foreign producers who retain the right to sell to U.S. markets by raising the prices of their goods. For example, one study found that, of the $8.6 billion in net welfare costs induced by the Multi-Fiber Agreement, which restricts textile and apparel imports, about $6 billion accrued to those foreign producers who were allotted shares of the import quotas. Surely, many Americans would cease to support certain types of import protections if they knew that such actions were propping up the profits of foreign producers.

Finally, we must not forget that trade actions, while sometimes protecting some American workers in import-competing industries, often invite the threat of foreign retaliation that would hurt American workers in export industries. For example, after the imposition of steel safeguard duties in March 2002, eight of our trading partners initiated safeguard investigations of their own on steel imports. Given the importance of export markets to the most dynamic areas of U.S. manufacturing, we cannot afford to jeopardize them by inviting foreign barriers to our products.

In conclusion, I think it unlikely that we will see a marked global reversal of trade liberalization on the order of the restrictions enacted in the 1930s. Policymakers have generally learned the lessons of that destructive episode. Nevertheless, it is not inconceivable that progress in dismantling trade barriers could stall. Many of the easiest negotiations—such as those on lowering tariffs—have already taken place. More ambitious and intrusive trade liberalizations, which often involve dismantling barriers to internal competition or cherished systems of domestic subsidies, may not have the necessary public support. It is also possible that a multiplicity of narrow, targeted trade actions—such as antidumping or safeguard actions—could lead to a de facto rollback in the overall degree of free trade even without a concerted shift in national policies.

Thus, it is crucial to maintain public pressure for free trade. It is important to continue to educate the public and create a political environment supportive of free trade as well as to implement policies that foster stability and economic growth. ■