Blinder *Baloney*

Today's scare talk of jobs outsourcing is grossly exaggerated.

BY WILLIAM T. DICKENS AND STEPHEN J. ROSE

THE INTERNATIONAL ECONOMY

THE MAGAZINE OF INTERNATIONAL ECONOMIC POLICY

888 16th Street, N.W.
Suite 740
Washington, D.C. 20006
Phone: 202-861-0791
Fax: 202-861-0790
www.international-economy.com

The fear that expanding international trade will cause job and income loss in developed countries has been with us for decades. In the past, the large wage gaps between the first and third world led many to fear an exodus of good-paying blue collar manufacturing jobs. Recently, the rise of the Chinese and Indian economies coupled with the Internet has given rise to a new concern, that high-skilled professional and technical jobs will be at risk for offshoring.

Surprisingly, some of the most prominent voices raising concerns about the new trade in services have been economists long identified with the mainstream pro-trade orthodoxy. For example, Alan Blinder, formerly vice-chairman of the Federal Reserve Board and a member of President Clinton's Council of Economic Advisors, published an article in *Foreign Affairs* arguing that forty million U.S. jobs are at risk of being offshored in the next ten to twenty years (he has since followed that claim up with two more articles further developing his ideas and estimates). Blinder is emphatic that in the long run, U.S. residents will benefit from offshoring overall and remains unequivocal in his defense of international trade. Despite this, he argues that offshoring of service jobs will be a "big deal," increase unemployment, and may lower some worker's incomes.

Others go further in response to this fear. Many in Congress have argued for requiring such restrictive labor standards in future trade agreements that it would likely be difficult to negotiate such treaties with less-developed economies. The previous and current Congresses failed to extend

---

William T. Dickens is Schelling Visiting Professor at the University of Maryland School of Public Policy. Stephen J. Rose is the author of Social Stratification in the United States: The American Profile Poster.

the President's trade promotion authority for the near-dead Doha Round of trade talks and have not approved a new trade agreement since the Central American Free Trade Act (CAFTA) passed in 2005, despite the fact that bilateral agreements between the United States and Peru, South Korea, and Panama have been negotiated. Support for trade agreements has virtually evaporated inside the Democratic Party; the fifteen Democratic House members who voted for the 2005 deal are derisively called the "CAFTA 15." Beyond blocking new agreements, some in Congress would go further and insist on renegotiating past treaties, including the agreement underlying U.S. participation in the World Trade Organization. Senators Byron Dorgan (D-ND) and Sherrod Brown (D-OH) each have books cataloging the purported costs of free trade to American workers including lost jobs and lowered incomes.

Hyping the New Politics of Outsourcing

Alan Blinder [right], formerly vice-chairman of the Federal Reserve Board and a member of President Clinton's Council of Economic Advisors, published an article in *Foreign Affairs* arguing that forty million U.S. jobs are at risk of being offshored in the next ten to twenty years (he has since followed that claim up with two more articles further developing his ideas and estimates). Blinder is emphatic that in the long run, U.S. residents will benefit from offshoring overall and remains unequivocal in his defense of international trade. Despite this, he argues that offshoring of service jobs will be a "big deal," increase unemployment, and may lower some worker's incomes.

—W. Dickens and S. Rose

Should we in the United States be afraid of declining wages or rising unemployment in the coming decades? We do not think so. The wage differentials between the first and third worlds have existed for decades, and the development of technology and institutions facilitating trade have been reducing the cost of imports since the end of the Second World War. Despite nearly constant increases in the extent of trade over this entire period, there is little evidence of substantial negative impacts on American employment or wages. Modern market economies regularly destroy and create tens of millions of jobs just from their own internal dynamics. Trade plays a very small role in this job churning. Time and again, modern market economies have proved that they can produce good jobs for workers who need them. There is no reason to believe that this will not be the case in the future.

Modern market economies regularly destroy and create tens of millions of jobs just from their own internal dynamics. Trade plays a very small role in this job churning.

THE HISTORICAL RECORD

The public perception that more of what we consume is "foreign-made" is true. As Figure 1 shows, imports as a share of our economy grew slowly from 1946 through 1983 and then grew more quickly from 1983 to the present. From 1983 to 1994, exports also grew, leaving the excess of imports over exports at about 1 percent of GDP. However, from 1994 through 2005, the negative balance of imports over exports grew to 5.6 percent of GDP annually.

Figure 1 also shows that, as the relative importance of imports was growing, the unemployment rate was going down. In fact, the data over the last sixty years do not show any negative relationship between the level of trade (as measured by imports or by trade balance) and employment (as measured by share of adult population employed or by the unemployment rate). This result is unaltered if changes in trade/imports instead are correlated with employment outcomes. Whatever job dislocations have been caused by trade, they cannot be contributing very much to aggregate unemployment.

This should not come as a surprise because modern economies have proven to be very good at creating jobs for those who want to work. This does not always happen immediately—during recessions, millions of people who want work cannot find it. Even during good times, churning of sectors and businesses in the economy forces many workers to face short spells of unemployment and some people with difficult circumstances suffer long-term unemployment. Still, it is remarkable the degree to which employment levels in modern economies tend to rise with the supply of workers to provide jobs for almost all of those who want them. Over the last sixty years, the U.S. economy has weathered the return of veterans after World War II, the entry of the baby boomers into the labor force, substantial increases in the participation of women, and waves of immigration, that have all increased the size of the labor force without causing any permanent rise in average unemployment. Other countries have had similar experiences.

Figure 1 Growth in Imports Versus Yearly Unemployment Rate

In many ways, this is counterintuitive. It would seem that if we consume goods or services produced with foreign labor, that is a missed opportunity for domestic workers—at least if the imports are not offset by exports. But this view ignores the amazing ability of market economies to adapt to changing conditions. Consider the similar process that takes place when new technology makes it possible to produce more output with fewer workers. Today, we produce the same tonnage of steel as we did in 1965 with one-quarter of the number of workers. Once 80 percent of the U.S. labor force was involved in farming; that figure was 40 percent in 1900, while today it is about 2 percent. Since the beginning of the industrial revolution there have been repeated prophecies of doom—this or that technical change, this or that surge of cheap labor, or this or that trade agreement will create massive unemployment. It has not happened.

The changes brought about by trade in the past, and even those projected for the future, pale in comparison to the revolutionary changes in our economy brought about by technical progress.

The Luddites were wrong—machines make our economy richer and they do not cause permanent increases in unemployment. Sometimes old jobs are eliminated, but even when that happens, the lower prices allowed by the increased productivity increase people's buying power, or real incomes, allowing those people to afford more goods. This creates new jobs. The twentieth century saw the introduction of a slew of new products: automobiles, telephones, radios, televisions, airplanes, and all the new consumer electronics that we prize today. In the process many industries reduced employment or even disappeared. Sometimes towns or entire regions lost their main source of income, but there is no doubt that America is richer today as a result of these changes. The changes brought about by trade in the past, and even those projected for the future, pale in comparison to the revolutionary changes in our economy brought about by technical progress.

As with the introduction of new technologies, there have been repeated warnings that increasing foreign trade would create massive unemployment. Remember Ross Perot in the 1992 presidential debates and the "great sucking sound" that we were supposed to hear as NAFTA caused U.S. jobs to move to Mexico? Unemployment in the United States was lower for the first seven years after the passage of NAFTA than it had been for more than two decades before. Many jobs did "move" to Mexico, but more jobs were created for a net gain of more than two million jobs a year from 1993 through 1999. Counterintuitive as it may seem, unemployment tends to be lowest when trade is expanding most rapidly. The simple explanation for this is that trade tends to expand fastest when incomes grow during times of rapid job growth.

If trade is not causing high unemployment in the advanced economies like the United States, is it destroying good jobs and leaving only bad ones? Is trade responsible for an overall trend towards wage stagnation for many workers? In order to answer this claim, we will look at the change in the distribution of jobs in the United States by pay category from 1979 to 2005. We begin in 1979 because this was the last cycle peak year before the restructuring that began in the early 1980s and before the increase in the rate of import growth in the economy that took place in the 1980s. If the critics are right, then the change should be towards worse jobs than those that existed in 1979.

It is important to distinguish between two different arguments. On the one hand, manufacturing jobs pay higher than average. Since many of these workers are older and have specialized skills, if they lose their positions, a large share of them will not be reemployed at their former wage. Programs exist to help such workers weather the transition, but we would be quick to agree that the United States could do more. On the other hand, many people make the larger claim that trade leads to the decline in the number of good jobs throughout the entire economy. This argument neglects the growth in other sectors, and the data presented here focuses on the overall net changes in employment and earnings.

Although the technological change has been revolutionary in many ways, the ratio of imports to GDP in the United States is still less than 18 percent.

We examine the experience of men and women in the United States separately because their experiences are so different. As Figure 2 shows, employment opportunities for women are notably improved. It is striking that less than 1 percent of female workers in 1979 earned more than $75,000 in 2005 dollars (which would have been $30,000 in 1979 dollars); and only another 3 per-

Figure 2 Evolution of Female Jobs, 1979 to 2005

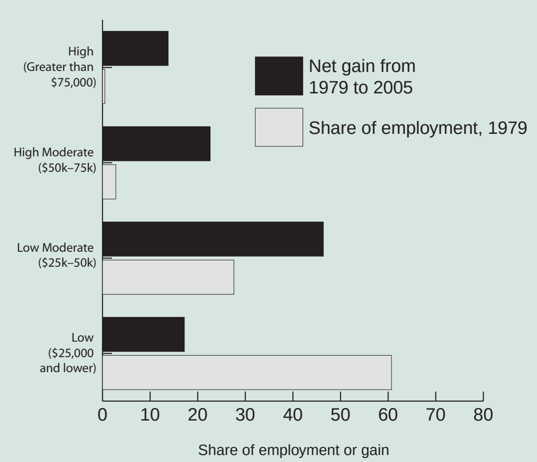
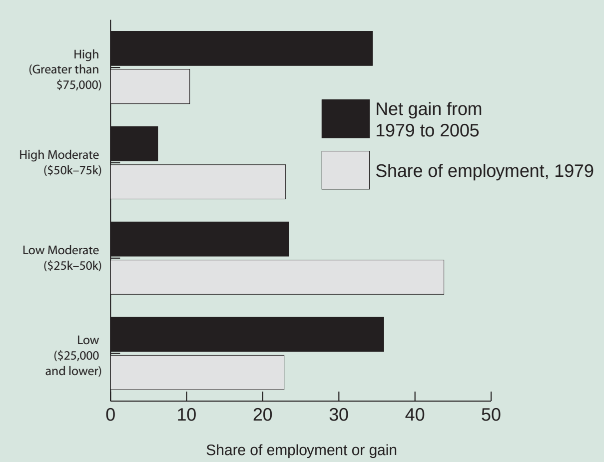


Figure 3 Evolution of Male Jobs, 1979 to 2005



At the end of World War II, the fraction of the workforce in manufacturing was roughly the same as the fraction of U.S. employment that Blinder believes is at risk of being offshored.

cent earned between $50,000 and $75,000. By contrast, among the net new female jobs created since 1979, over one-third (36 percent) were in the top two earnings categories. At the other end of the spectrum, fully 61 percent of prime-age women workers in 1979 earned less than $25,000 while only 17 percent of net job gains were in this range.

As Figure 3 shows, the distribution of men's jobs since 1979 has changed greatly, but very differently from the changes for women. The growth of the share of high-pay jobs is particularly large: only 10 percent of 1979 male workers earned more than $75,000, but 34 percent of net new jobs fall in that category. At the bottom end of the labor force, 23 percent of the jobs were in the lowest pay category versus 36 percent of the net new jobs created. By contrast, moderate-paying jobs (between $25,000 and $75,000) represented 67 percent of male employment in 1979 but only 30 percent of the new jobs created since 1979.

So during the period when trade was growing, there were two positive labor market shifts and one negative one. For women, the story is one of increasing pay for traditionally female-held jobs and an opening up of high-paying managerial and professional jobs that had previously been denied to them. College-educated men also benefited from the increasing pool of managerial and professional jobs, but for those with just a high school diploma or less, high-paying blue collar jobs dried up and they were forced into lower paying positions.

This is a mixed picture, but one that is more positive than negative. At a minimum, these numbers do not support the claim that trade led to a worsening of job prospects for most American workers. Whatever negative effects trade has had, they are more than outweighed by changes elsewhere in the economy. In fact, most economists who have tried to look at the causes of rising male income inequality have estimated that trade is only responsible for 10 percent to 20 percent of the change. While trade certainly played some role in the loss of good jobs for high school-educated men in the United States, the economy created a steady stream of new jobs, many of which were higher paying than the ones lost to trade.

WILL THE FUTURE BE DIFFERENT?

Many trade pessimists are concerned that the old rules no longer apply. It is argued that the rise of the Internet and other modern communication technologies have made the world a smaller place and put a growing portion of U.S. workers into competition with low-wage workers in less-developed countries. One also often hears that the sheer size of the low-wage labor forces in China, India, and other emerging markets now integrated with the global economy changes the rules of the game.

But the Internet is not something that happened overnight. For the last two centuries, technical change has continually lowered the cost of international and interregional trade and has been a major force causing its expansion. From locomotives, to steam ships, to the telephone, to jet airplanes, to container shipping, invention after invention has made it cheaper for us to buy from abroad and for foreigners to buy our goods. Although the technological change has been revolutionary in many ways, the ratio of imports to GDP in the United States is still less than 18 percent.

Like the technology supporting trade in general, improvements in communications technology have been going on for a long time. The telegraph was introduced in 1844 and the telephone in 1876. By 1897 Marconi had demonstrated the practicality of wireless telegraphy. The first inter-city fax transmission was accomplished in 1902. Binary coded data has been exchanged over phone lines for decades. The authors of this paper have been using email and exchanging data through the Internet (and its forerunner the Bitnet) for about twenty-five years, and the World Wide Web has been around for over fifteen years. Yet despite this, most estimates place the number of service jobs that have been offshored from the United States at less than one million, and the surge in U.S. imports has actually slowed as the Internet has become ubiquitous in the last seven years.

American manufacturing workers have earned much more than those in nearly every country in the world for the entire post-war period. At the end of World War II, the fraction of the workforce in manufacturing was roughly the same as the fraction of U.S. employment that Blinder believes is at risk of being offshored.

The share of the workforce employed in manufacturing has fallen considerably and the number of workers employed in manufacturing peaked in 1979, due to changes in both trade and technology. Yet the value of manufacturing output in the United States is over seven times as high today as it was at the beginning of 1947 and there are nearly as many workers employed in manufacturing now as then (14.3 million in January 1947 vs. 14.0 million today).

With wage gaps so large and transportation costs so low, why has U.S. manufacturing survived so well? First, being close to the markets served has many advantages in gauging demand and responding to changes in the market place. Second, it is easier to service products when production is located close to the market as inventories of parts can be lower. Third, and most of all, we have to export to generate foreign exchange to buy our imports. Even though the United States ran a large trade deficit in 2006, we still were responsible for 8.5 percent of world manufacturing exports.

Furthermore, there are many newly tradable services that the United States is likely to excel at and to export to a growing market rather than import. Over the last ten years, the United States has been the world's leader in exporting entertainment, financial and consulting services, education, research, and other high-end services. The world business language is English, our capital markets are huge and open, and the dollar is still the world's main currency. These advantages are probably not going away soon.

Several studies have attempted to estimate the number of jobs likely to be off-shored starting from the perspective that the United States must export if it wants to continue to import. Assuming that the pattern of comparative advantage in the production of services is likely to remain roughly the same, three such estimates all place the number of jobs that will ultimately be off-shored at between twelve and fourteen million. This figure is slightly less than the net number of jobs that have been displaced by the rise in imports since 1979. Since we have been able to keep employment high through the last twenty-eight years, we will probably be able to adjust to a change of this magnitude without much difficulty. Blinder argues that many more jobs may be vulnerable, but even he does not expect a gross loss of more than about twenty million jobs over the next twenty years.

Even if Blinder's worst case came true and we lost twenty million jobs over the next ten years, that would add less than 5 percent to normal weekly turnover.

This level of job loss is small relative to total changes, including those due to domestic factors, in a U.S. workforce of 140 million or more. Technological change will continue to reshuffle employment between firms and sectors, and the biggest source of job loss—and gain—will remain domestic competition. We know, for example, that even in relatively good times over 300,000 people claim unemployment insurance each week after being laid off—and many workers who are laid off do not qualify for benefits or apply for them. From other surveys, we know that more than three times that many workers leave their jobs each week (many by choice). Simultaneously, there are more than one million new hires every week! So, even if Blinder's worst case came true and we lost twenty million jobs over the next ten years, that would add less than 5 percent to normal weekly turnover (and this assumes that the twenty million is all in addition to the churning currently caused by trade).

Further, since the majority of Blinder's jobs at-risk are service jobs, the impact will be less than during adjustment to the manufacturing displacements of the past. First, offshoring in services does not tend to wipe out entire plants or industries. Rather, companies have off-shored particular parts of their operations while keeping most in the United States. Second, service employment tends to be less geographically concentrated than manufacturing and is most often located in large cities. One of the visible costs of trade adjustment over the last half-century has been the devastation of many towns and smaller cities when their leading company was driven out of business by foreign competition. By contrast, there are few "ghost" towns created when service jobs are lost.

Also, U.S. labor institutions have adapted to enable more flexible adjustment by workers than in the past. ERISA, the Employee Retirement Income Security Act, protects workers' pensions, and defined benefit pensions are being replaced by defined contribution plans which are more portable. COBRA allows workers to continue

Continued on page 83

Continued from page 23

their health insurance when they are laid off. The extended Earned Income Tax Credit and wage insurance for workers affected by trade provide some protection of workers' earnings that was not available in the past. And arguably workers' job prospects today are more dependent on their general and thus portable skills than on those specific to their current employment, so that they have less to lose when they are displaced.

We can and should do more for displaced workers. For one thing, retraining and income support programs now reserved for workers impacted by trade should be made available to all. There is no point in distinguishing between sources of involuntary job loss. Whether due to domestic or foreign competition, we benefit as a society from the "creative destruction" that enhances productivity, and should compensate the losers from that process. This could help with political fears and pressures about the effect of trade on jobs and wages as well. But responding to these adjustments and fears about trade at the local and individual level must not be based on misleading projections of national pain—if the future of American wages and jobs is different than the past, it is likely to be in the direction of less rather than more dislocation.

CONCLUSION

For decades, trade pessimists have predicted that the large wage gap between the United States and less-developed countries would cause U.S. jobs to flee overseas, driving up unemployment and driving down wages. For most of the postwar period, that fear has focused on loss of manufacturing jobs, but in recent years concern has spread to the loss of American service and high-wage jobs to outsourcing to China and elsewhere, abetted by the Internet.

These concerns have been vastly exaggerated. The U.S. economy creates tens of millions of jobs every year, replacing the tens of millions of jobs that are lost due to the forces of competition and technical change. Losses due to trade are only a small fraction of the total job churning, and ongoing increases in the amount of trade by the United States have never been associated with major changes in jobs or wages. Not surprisingly, therefore, it is not possible to detect any impact of trade on unemployment in aggregate data. Not only do we see no reason to believe that this pattern is likely to change in the future, there are good reasons to believe that labor adjustments caused by trade in the coming decades will have less of a negative impact because of the changing nature of off-shored jobs. ◆