Occasional Paper 45

10-1-1985

Imports and Unemployment: Dispelling the Myths

Murray L. Weidenbaum
Washington University in St Louis

NOT FOR RELEASE BEFORE
9:30 A.M. EDST
OCTOBER 22, 1985

IMPORTS AND UNEMPLOYMENT: DISPELLING THE MYTHS

by Murray L. Weidenbaum, Director
Center for the Study of American Business
Washington University in St. Louis

Testimony prepared for the Subcommittee on Employment
and Productivity of the
Senate Committee on Labor and Human Resources
Washington, D.C., October 22, 1985

OP45

NOT FOR RELEASE BEFORE
9:30 A.M. EDST
OCTOBER 22, 1985

IMPORTS AND UNEMPLOYMENT: DISPELLING THE MYTHS

by Murray L. Weidenbaum, Director
Center for the Study of American Business
Washington University in St. Louis

Testimony prepared for the Subcommittee on Employment
and Productivity of the
Senate Committee on Labor and Human Resources
Washington, D.C., October 22, 1985

We hear so much about the inroads that imports are making in the American economy and their tremendous effect on employment. What is the evidence? The truth is far less dramatic than the overblown charges. Let me cite four key examples:

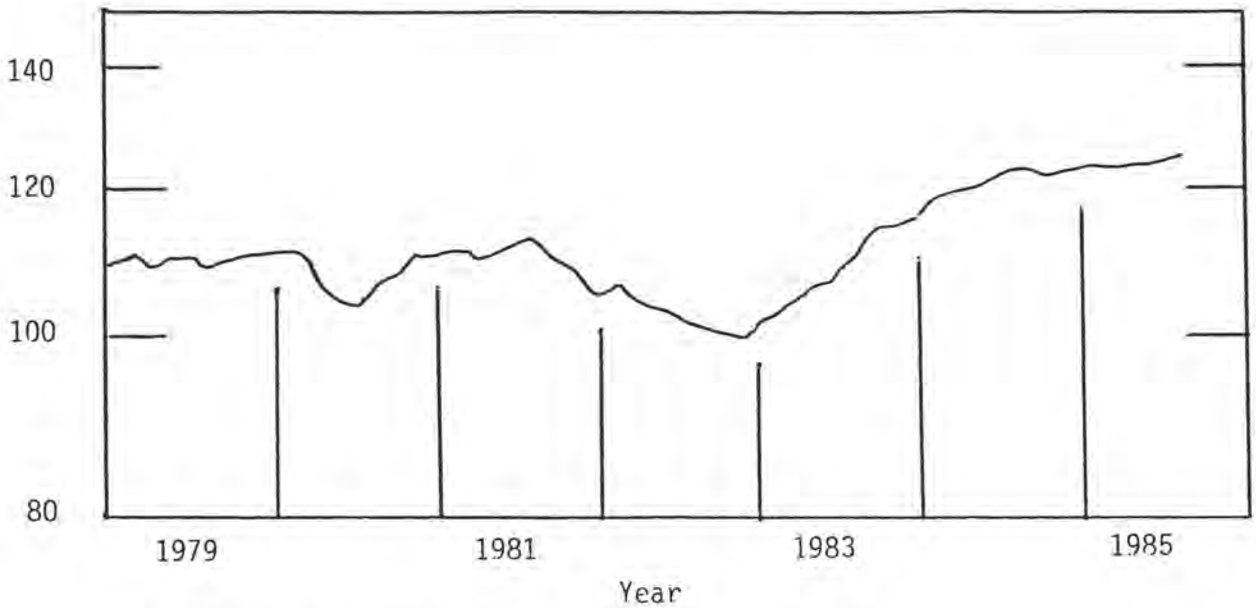
MYTH #1. **Imports are dragging down the American economy, depressing employment especially in manufacturing.** The truth of the matter is that the rapid rise in employment in the United States in recent years is the envy of the rest of the world. Total U.S. civilian employment has increased from 98.8 million in 1978 to 107.2 million today.

We hear so much about the decline in manufacturing. But industrial production in the United States reached an all-time peak in 1984 and has remained on a high plateau ever since. See Figure 1. Moreover, as shown in Figure 2, manufacturing's share of the real gross domestic product has held very steady for the last 30 years.

Note: The views expressed are entirely personal.

Figure 1

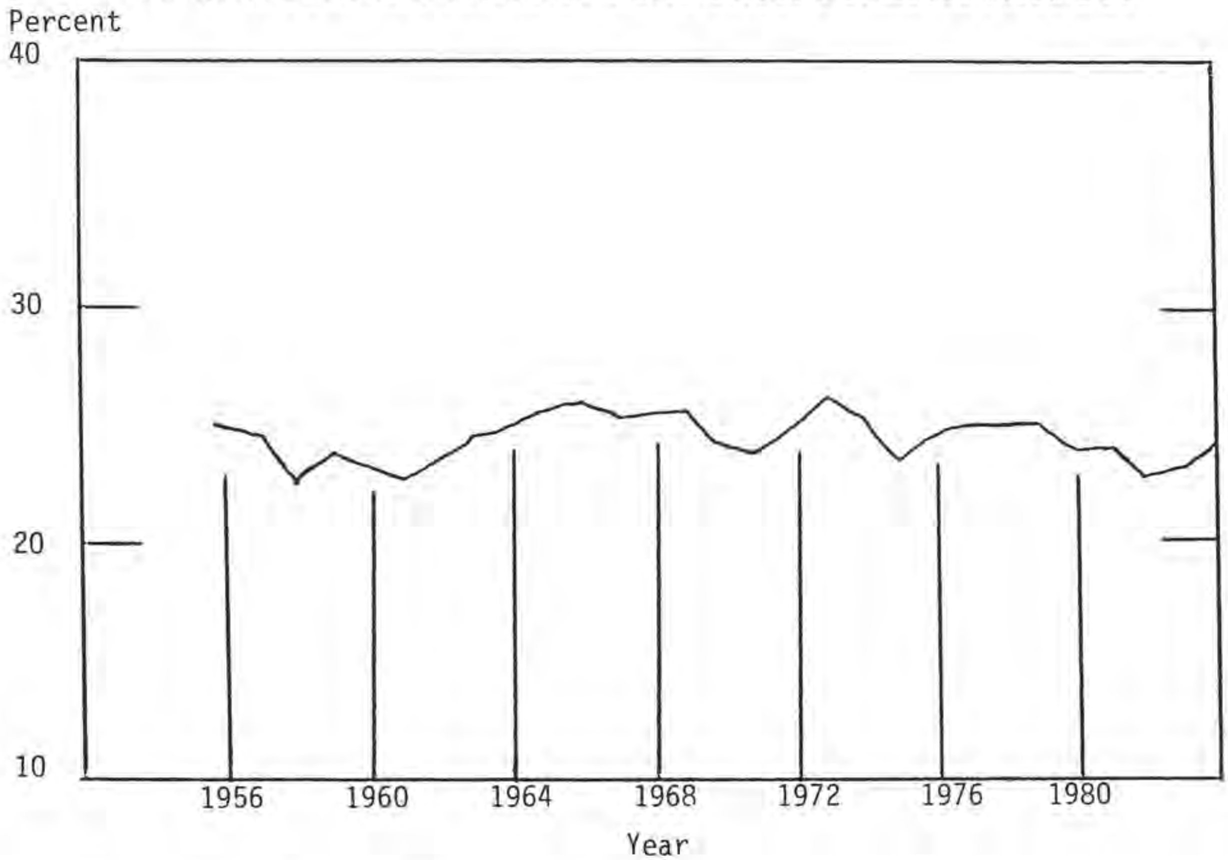
INDUSTRIAL PRODUCTION
Ratio Scale, 1977=100



Source: Federal Reserve System

Figure 2

MANUFACTURING'S SHARE OF REAL GROSS DOMESTIC PRODUCT



Source: Federal Reserve Bank of Cleveland

The trend in manufacturing employment, however, is not quite as sanguine. The total number of manufacturing jobs has fluctuated in the vicinity of 19 million since 1970. This is not exactly booming growth, but it is certainly a far cry from the alleged decline and fall of U.S. manufacturing that we hear so much about. In fact, my colleague at the Center for the Study of American Business, Professor Richard McKenzie, is doing research that shows that total employment of production workers in the U.S. is continuing to rise. The point overlooked by most analysts is that the fastest growing opportunities for production workers are occurring in the service industry. In large measure, this results from the trend toward less vertical integration among manufacturing firms. Manufacturers are performing a smaller range of activities in-house and contracting out other activities to subcontractors and suppliers, many of whom are classified as being in the service sector.

MYTH #2. **Imports are the main reason for unemployment in steel, textiles and other key industries.** The data do not support this contention. For example, a Federal Trade Commission study of the American steel industry shows that granting generous wage increases -- in excess of the average wage gains by other factory workers -- has been the largest single reason for the lack of competitiveness and, thus, declining employment in American steel companies. On-going research by Professor McKenzie indicates that rapidly improving productivity is the main reason for declining employment in the American textile industry. Unfortunately, it is very difficult to determine the extent to which the pace of automation has been accelerated by international competition in textiles.

MYTH #3. **Protection is the way to save jobs.** Protectionist actions increase the cost of producing goods and services in the United States, reducing the competitiveness of American products. A recent study by Professor Arthur Denzau at the Center for the Study of American Business shows that if the United States had imposed a 15 percent import quota on steel in 1984, as the steel industry sought, 26,000 steelworker jobs could have been saved -- but at the cost of 93,000 jobs in the steel-using industries. The higher prices for protected domestic steel make American automobile and durable goods producers less competitive at home and abroad. If the steel quota had been implemented, the American consumer would have been saddled with paying for a high-cost jobs program that would have resulted in a net loss of 67,000 jobs.

Moreover, protectionism turns out to be the most inefficient and regressive welfare program ever designed. If anyone were to identify a government program where the benefits delivered to the recipients amounted to only 50 or 60 percent of the costs, the public would criticize it as shamefully wasteful. But in the case of protectionism, the typical increase in prices to be paid by American consumers far exceeds the total wages of the jobs that are "saved." In the case of footwear quotas, the ratio of costs to benefits was 9 to 1; in the case of steel and autos, 4 to 1.

Protectionism, of course, may be a politician's delight because it delivers visible benefits to the protected parties while imposing the costs as a hidden tax on the public. But the higher prices that invariably result are paid by American consumers. In all too many cases, such as textiles and apparel, this burden hits most heavily on the poorest people in our country.

MYTH #4. **Workers in import-affected industries deserve to be treated more generously than other employees.** I know of no reason why workers in industries facing serious international competition should be viewed as more meritorious than, say, defense workers who lose their jobs when government contracts are completed or cancelled. After all, the line of causation from the government's budget deficits to the high-priced dollar to rising imports to reduced employment is far more indirect than the link between a government decision to close a military facility and the resultant economic hardship.

To be sure, programs intended to ease the burden on unemployed workers are a standard part of government activity in the United States, and these general purpose programs will continue to be relied on. But the most effective way of dealing with the rising tide of imports is not to try to dam up foreign trade. Nor is it to create trade adjustment programs that, in effect, become entitlements -- and that discriminate against other workers. It is to increase the competitiveness of American industry.

Recommendations

I would like to suggest five positive approaches to foreign trade policy that would help American business compete. These suggestions constitute "preventative medicine" for the ills of import-related unemployment.

1. Reduce the Budget Deficit

Although the linkages are complex and indirect, I believe that financing a string of $200 billion deficits has increased real interest rates substantially, and that, in turn, has attracted large amounts of foreign capital. That substantial inflow of foreign money has increased the demand for dollars and resulted in a major appreciation of the dollar. The high relative value of the dollar has unfortunately made it easier for foreign companies to compete against American companies, both in our home markets and overseas.

Moreover, reducing the budget deficit is inherently desirable for purely domestic reasons. The trend during the 1980s thus far has been for federal spending to be a rising share of GNP. That trend should be reversed.

2. Gear Tax Reform to Enhance Productivity and Competitiveness

It is sad to note that most tax reform proposals to date ignore the repercussions on international trade. Many of the industries hardest hit by imports are those whose tax burdens would rise the most under the modified flat tax proposals submitted both by members of Congress and the Administration.

This is simply not the time to elevate the development of an ideal tax system to the top of the roster of public issues. Rather, tax policy needs to continue emphasizing incentives for the items important to enhancing our international competitiveness -- saving, investment, and research and development.

3. Renew the Regulatory Reform Effort

The costs of producing goods and services in the United States can be decreased by launching another effort to reduce government regulation of business. The elimination of some economic rule-making has reduced the cost of transportation. This is not, however, a reason to dismantle social regulation. But closer attention to the tremendous costs imposed by EPA, OSHA and other regulatory agencies would help to restore industrial competitiveness.

4. Reduce U.S. Barriers to U.S. Exports

About one-half of our trade deficit with Japan could be eliminated if Congress rescinded the bans on the export of timber and oil. Also, restraints on the export of strategic goods should be administered with common sense. It does not contribute to national security to prevent American companies from selling items overseas that are readily available from foreign competitors.

5. American Business and Labor Must Face the Challenge of Increasing Their Productivity

We cannot blame our poor production practices on foreigners. The answer is not to prop up industries with import restrictions or government subsidies -- or to play King Canute and try to prevent businesses by law from closing or "running away." Rather, labor and management in each company need to face the challenge of enhancing their competitiveness.

Management must show the way. Cutting the proliferation of staff activities and layers of executives creates an operating environment in which labor is more likely to accept changes in needlessly costly factory work rules. Protectionism is counterproductive because it lessens the pressure on management and labor to make the painful but necessary changes that improve productivity. The painful fact is that foreign competition is the most effective spur to greater productivity.

Fundamentally, the future of American industry will not be settled by government directives from Tokyo or Washington -- but by decisions made in business offices and on production floors in Boston, Detroit, Chicago, Pittsburgh, Los Angeles, St. Louis and other major cities throughout the nation.

Sources

Arthur T. Denzau, *American Steel: Responding to Foreign Competition* (St. Louis: Washington University, Center for the Study of American Business, 1985).

Richard B. McKenzie and Stephen D. Smith, *The Loss of Textile and Apparel Jobs* (St. Louis: Washington University, Center for the Study of American Business, forthcoming).

Richard B. McKenzie and Stephen D. Smith, *The Rise of the Production Sector in the U.S. Economy* (St. Louis: Washington University, Center for the Study of American Business, forthcoming).

Michael C. Munger, *A Time-Series Investigation into Factors Influencing U.S. Auto Assembly Employment* (Washington, D.C.: Bureau of Economics, Federal Trade Commission, 1985).

Murray L. Weidenbaum and Michael J. Athey, *The Revival of the Rust Belt* (St. Louis: Washington University, Center for the Study of American Business, 1984).

Murray L. Weidenbaum and Michael C. Munger, "Protection at Any Price?" *Regulation*, July/August 1983.

Murray L. Weidenbaum with Michael C. Munger and Ronald J. Penoyer, *Toward a More Open Trade Policy* (St. Louis: Washington University, Center for the Study of American Business, 1983).