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AGENDA FOR SHARED PROSPERITY

GLOBALIZATION THAT WORKS FOR WORKING AMERICANS

BY JEFF FAUX

Competently managed, America's integration into the global economy can contribute to increasing living standards for workers in America and in the rest of the world. Unfortunately, the process is being tragically mismanaged, carried out not with a carefully considered plan but with a chaotic patchwork of international trade and investment agreements and policies increasingly unaccountable to any country's citizens.

In America, as elsewhere, the benefits of the current form of globalization have been concentrated among those at the top of the income and wealth ladder, while the costs have been paid by working families at the middle and the bottom. Real wages and benefits for the majority of workers are stagnant, jobs have been destroyed, and family and community life has been stressed and, at times, broken apart.

In the United States, the mismanaged policies of the last two decades have severely damaged the nation's competitiveness and plunged it into a spiral of trade deficits. To some extent the economic harm has been obscured by massive borrowing from the rest of the world, borrowing that is clearly unsustainable.

America urgently needs to reverse its course with a comprehensive strategy that matches the scope and depth of globalization's challenges.

Global integration, not just trade

America has always traded with other nations. From the end of the Civil War to the 1970s the international share of the U.S. economy was modest, and exports and imports were generally in balance or showed a small surplus. But in the last 25 years, foreign trade has risen 700%, more than doubling as a share of gross domestic product to 28%. In 2006, the excess of imports over exports will reach some $900 billion—7% of GDP (**Figure A**).

This dramatic shift reflects more than simply an increased movement of goods and services between the United States and other nations. It reflects an unprecedented economic integration with the rest of the world that is blurring the very definition of the "American" economy.

AGENDA FOR SHARED PROSPERITY

The Economic Policy Institute initiative for solutions that match the scale of the problems.

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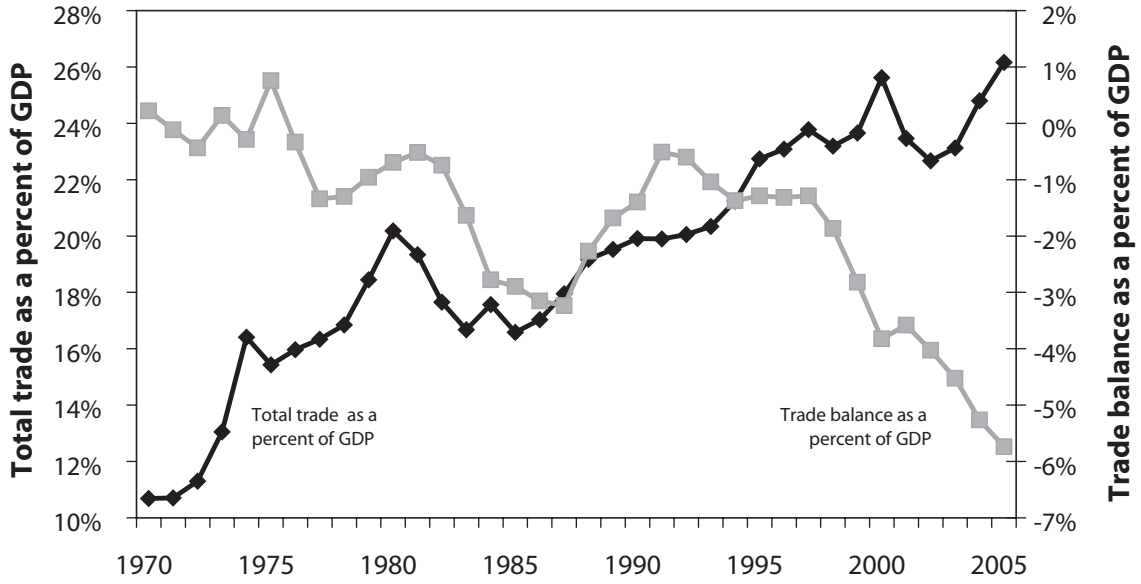
FIGURE A



SOURCE: U.S. Commerce Department.

American business is steadily moving finance, technology, production, and marketing beyond our borders. Some 50% of all U.S.-owned manufacturing production is now located in foreign countries, and 25% of the profits of U.S. multinational corporations are generated overseas—and the shares are rapidly growing.

To think of global integration as simply "more trade" is as much an error as it would have been to label the consolidation of the continental U.S. economy in the 19th century as simply more trade among the states. As Renato Ruggiero, the first director-general of the World Trade Organization (WTO), observed in 1995: "We are no longer writing the rules of interaction among separate national economies. We are writing the constitution of a single global economy."

This new "constitution" is evolving from the increasing number of multinational agreements such as the North American Free Trade Agreement (NAFTA) and the WTO, bilateral trade and investment deals, and the policies of institutions such as the International Monetary Fund (IMF) and the World Bank. The World Trade Organization, for example, enforces some 17 different agreements, only two of which directly concern trade. The others are primarily aimed at making domestic economic policies (e.g., financial regulation, privatization, product safety) conform to a single standard.

Unfortunately, this new global economic constitution primarily protects and promotes the interests of only one category of citizen—the global corporate investor. The rules of the global economy now give corporate property rights priority over human rights, undercutting the hard-won domestic social contract that has supported broadly shared prosperity in advanced societies and in some developing countries as well. The rules have encouraged and often imposed policies of privatization, deregulation, domestic austerity, and export-dependent growth on sovereign nations. They have denied governments the right to effectively regulate imported products produced by exploiting labor and the environment, while requiring governments to protect corporate patents and other intellectual property. And they give corporate investors extraordinary privileges to sue governments in secret tribunals.

The U.S. government is the leading advocate of the new rules, which have consistently traded away opportunities of Americans who produce goods and services in the United States in favor of access by multinational corporations to workers and financial markets in other countries.

The policies that make up the evolving "constitution of a single global economy" have not themselves created the global marketplace. Rather, the root causes are changes in transportation, information, and management technologies that, since the end of the Cold War, have doubled the available global labor force to three billion workers. Under any circumstances this process would have challenged American living standards and the survival of companies that produce here. But instead of managing the process carefully and controlling the opening of the U.S. economy in sync with strategies to maintain our competitiveness and protect real incomes, successive U.S. governments have plunged American employers and workers into a global market governed by rules reminiscent of late 19th century capitalism.

The emergence of these perverse policies is no accident. As "American" corporations can increasingly get their workers, financing, components, finished products, and customers in other countries, they are less dependent on the economic health of those who live and work in the United States.

As individuals, Americans who manage and own global enterprises may be as concerned about their nation's future as anyone else. But institutionally, they are paid to worry about their corporations, not their country. For decades, they have been making the point themselves, quite openly. In the 1980s the chief executive officer of Dow Chemical said he yearned to place his headquarters on an island "beholden to no nation or society." In 1995, the CEO of the Ford Motor Company said: "Ford isn't even an American company, strictly speaking. We're global. We're investing all over the world….Our managers are multinational. We teach them to think and act globally." In 2006, the CEO of Cisco Systems—poster company for the information economy—went a step further: "What we are trying to do is outline an entire strategy of becoming a Chinese company."

Ralph Gomory, former IBM executive and now president of the Alfred P. Sloan Foundation, notes that, "There is and can be fundamental conflict between the goals of the company and the goals of the country." Jeffrey Garten, a major architect of U.S. globalization policies and now dean of Yale Business School, observes that America "must adapt to the reality that U.S. multinationalists' goals may no longer dovetail with the national interest."

But policy making has not caught up with this changed reality. Lobbyists for global corporate investors have been the most powerful influence on the way Washington has managed America's integration into the global economy. As a result, the policies that have guided this integration have systematically favored the interests of global investors over those of the typical American worker.

The broken job ladder

Since 1979, as trade has expanded, imports have grown faster than exports, directly displacing some 7 million jobs in America.[1] The threat of jobs being shipped overseas has in turn translated into reduced wages and benefits and a general decline in the bargaining power of U.S. workers. A 2004 Gallup poll showed that 61% of Americans fear that they or someone close to them will lose a job because the employer is moving to another country. The threat to off-shore production, real or exaggerated, gives employers substantial leverage over their employees.

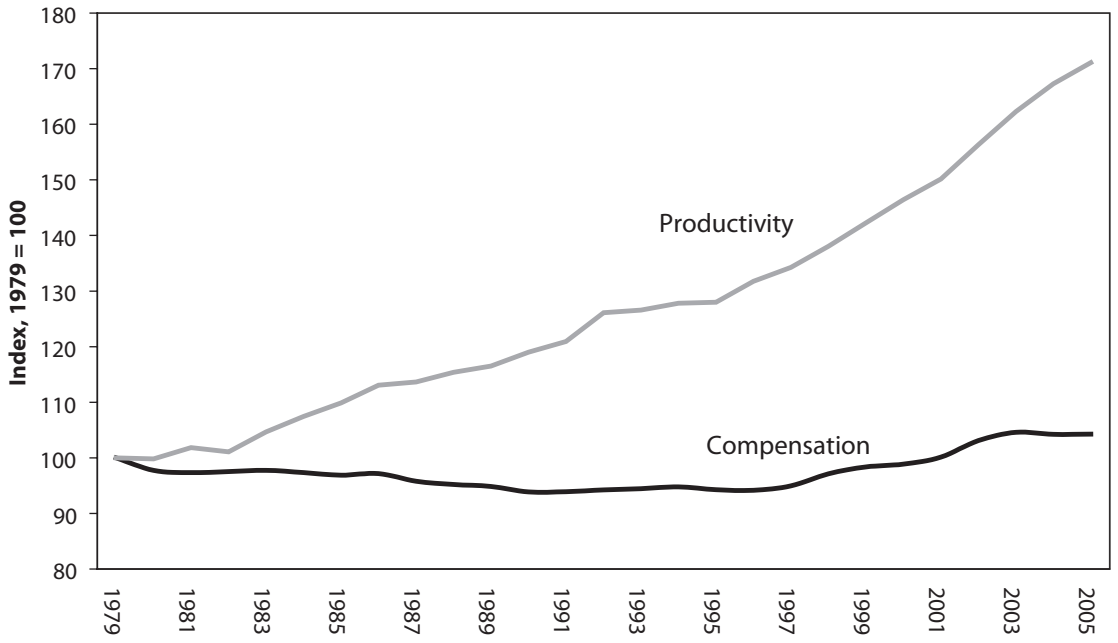
Not surprisingly, workers are receiving a shrinking share of the economic pie. The gap between what workers produce and what they receive has dramatically widened: between 1980 and 2005 productivity in the U.S. economy rose 71%, while the real compensation (including benefits) of nonsupervisory workers rose 4% (nonsupervisory employees make up about 80% of U.S. workers). In the tradable manufacturing sector, productivity rose 131% while compensation of nonsupervisors gained 7% (**Figures B-1** and **B-2**).

Since the end of the last recession in 2001, the purchasing power of the typical American worker's weekly paycheck has dropped 3%. Among working males, real hourly wages are now about where they were in 1973.

Economists differ in their estimates of precisely how much of the rise in wage stagnation and overall income in-

FIGURE B-1

Productivity growth and the compensation of production workers, 1979-2005



SOURCE: BLS.

equality is attributable to imbalanced trade, but there is little doubt that it has been substantial. Research on the 1980s and early 1990s shows that trade flows alone account for 10-30% of the growth in wage inequality, with some major studies suggesting ever greater contributions (see books by Adrian Wood (1994) or William Cline (1997) for estimates of roughly 40%). Such estimates are sufficiently high by themselves to warrant attention, but even these understate the case.[2] Moreover, they miss many of the ways that globalization influences other factors that are typically cited as contributing to wage inequality (e.g., de-unionization, the threats by employers to move jobs overseas, and the growing political influence of multinationals).

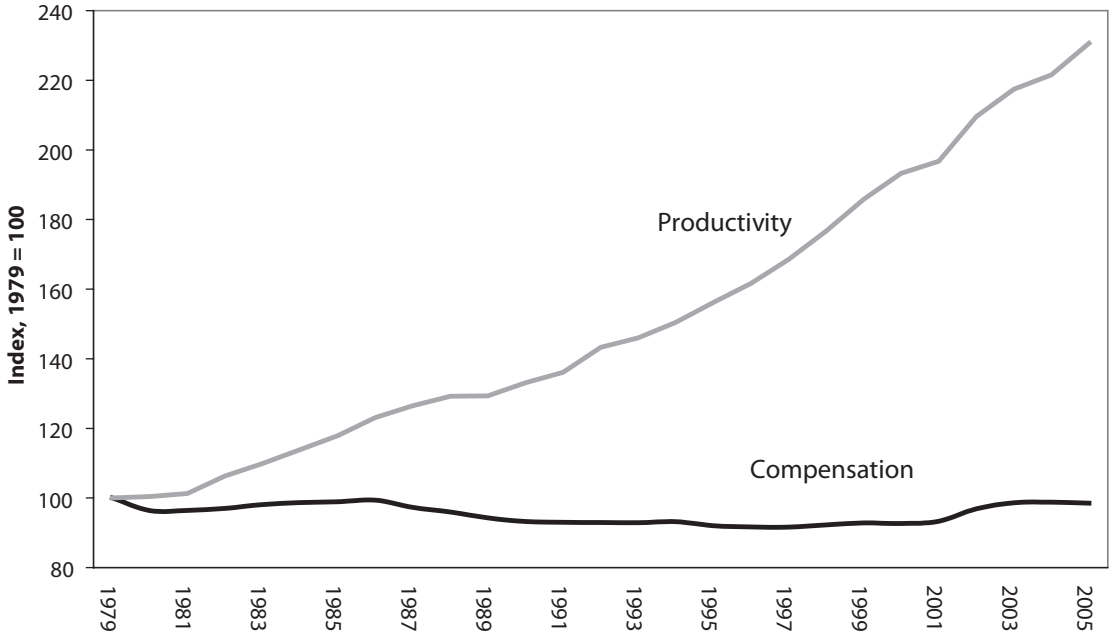
That trade will make the distribution of income worse is embedded in fundamental economic logic. When workers in a high-wage nation are thrown into competition with workers in less-developed countries, those at the bottom end of the wage ladder in the former will be relatively worse off and those at the top end better off.[3]

Defenders of the present mode of globalization tend to dismiss this as a problem for a small number of unskilled workers. But globalization's "losers" extend way beyond the uneducated—and their ranks are growing. Twenty-five years ago, American workers were assured by the promoters of "free-trade" agreements that their better education and access to superior U.S. technology would allow them to produce more high-value-added products. Americans would move up the global wage ladder, while workers from other countries would get the vacated lower-wage jobs at the bottom. But when skilled, high-paid jobs began to disappear, American workers were told that they were not skilled and educated *enough*. The problem, they are now informed , is not the ill-considered policies, the problem is them. So if they want to maintain their living standards they have to become much more educated and productive and to work harder and longer hours. And if they can't, perhaps their children can.

Yet Americans are working longer and are certainly more educated. The share of the workforce with college degrees doubled from 15% in 1973 to 30% over the last three decades, while the share of high school drop-outs fell from 29%

FIGURE B-2

Productivity growth in manufacturing and the compensation of nonsupervisory manufacturing workers, 1979-2005



SOURCE: BLS.

to 10%. Still, the American economy is not generating the promised good jobs. Projections by the Bureau of Labor Statistics conclude that by 2014 the number of occupations filled by people with college degrees will rise by merely one percentage point—from 28% to 29%. The share of jobs for which college-level education is actually required is projected to be just 21%.[4]

The evidence is overwhelming that what was once thought of as America's natural comparative advantage—skills, technology, and organization—can now be duplicated or even surpassed by other nations. Outsourcing off-shore has now ratcheted up to jobs in research and development that Americans had assumed would always be ours because of our advanced technology, prestigious universities, and Nobel-prize-winning scientists. "American" transnationals are locating R&D in India, Taiwan, and China, where the skills are high and come cheap. An analysis of 57 recent major research initiatives of the U.S. telecommunications industry showed that all but five were located outside the U.S. According to one estimate, 80% of engineering tasks in product development can be "easily outsourced." Another suggests that as many as 60 million U.S. workers are vulnerable to having their jobs shipped to another country.[5]

The notion that the U.S. economy can prosper by selling high-value services while the rest of the world sells us their goods is now clearly not credible. Manufacturing is our most important source of productivity and motivator of technological innovation. In fact, much of the jobs and wealth creation associated with the information economy are tied to the production of goods; success results from setting trained people to work on problems in the context of day-to-day production, whether autos or pharmaceuticals or Hollywood films. The more we off-shore production, the harder it is to compete in the world on the basis of higher productivity and creativity.[6]

Princeton economist Alan Blinder, former vice chairman of the Federal Reserve Board, recently warned that "tens of millions of additional workers will start to experience an element of job insecurity that has heretofore been reserved for manufacturing workers. It is predictable that they will not like it."

The growing disconnect between many large American employers and their employees is further shredding the sense of mutual dependence that lies at the heart of a productive workplace. Employers who are searching the globe for cheaper labor have less incentive to invest in the long-term development of their U.S. labor force. And workers who are constantly threatened by off-shoring have little reason to feel loyal to the firm. Again, these attitudes have spread beyond the sectors immediately impacted by trade and increasingly pervade the U.S. economy. As Thomas Kochan of MIT has observed, "employers have replaced the basic social contract at work—the norm that hard work, loyalty, and good performance will be rewarded with a good wage, dignity, and security—with a norm that gives primacy to cutting operating costs and obtaining the highest possible profit."[7]

Globalization's benefits—worth the cost?

Most Americans have rejected the radical claim that the elimination of worker, consumer, and environmental protections in the U.S. domestic economy would be justified by a promise that an increase in overall economic growth might result. Yet the argument for a global economy without a social contract is essentially just that.

Globalization does generate some economic benefits. But they have been routinely exaggerated in an effort to justify rising inequality, job loss, and other costs.

Thus, a recent report by the Hamilton Project at the Brookings Institution[8] begins by asserting that "the global system of open trade has brought substantial and widespread benefits to the U.S. economy." The authors acknowledge that there have been unexpected costs, but assert that these are small and affect only a small number of victims, who can be compensated through a few modest and inexpensive programs.

The Brookings paper claims that expanded trade provided gains of between $800 billion and $1.5 trillion to the U.S. economy in 2004—over 8% of that year's GDP. If so, it would have been a substantial contribution to the country's growth. But the evidence doesn't nearly support this claim.

Most of the assumed economic gains come in the form of lower prices. The principal source cited for the lower price benefit is the Bush Administration's 2006 *Economic Report of the President*, whose evidence is that import prices rose 9% between 1990 and 2004 while the prices of all goods and services rose 60%. But imports are concentrated in goods. Comparing the price change of domestic and imported goods under the same methodology yields a savings from imports to the average American of about $36 a year. A gain, but hardly "substantial" enough to justify any costs.

Moreover, as economist Josh Bivens has shown, the academic studies that the Hamilton Report uses to show vast benefits from greater variety and productivity gains are technically flawed, based on unrealistic assumptions, and often contradict each other. (See the box on global benefits.) An analysis more consistent with standard economic principles suggests a one-time 2004 gain from imports not of 8.0% of GDP, but of 0.7%.

A central problem with claims of huge gains from expanded trade is that they come not from actual experience but from simulations of what might happen under extremely unrealistic conditions. Among other things, they assume a state of permanent full employment. Thus, by definition, trade can never cost any workers their jobs. Moreover, these models simulate only trade, not globalization. They do not analyze the costs to America of investment flowing to other nations, the undercutting of bargaining power, nor the off-shoring of American technology.

A more sophisticated effort by the Carnegie Endowment for International Peace in 2006 came up with a benefit to the U.S. economy from the Doha Round of trade agreements of $4.6 billion—a gain of less than one half of one percent of U.S. GDP, or about $15 per person.[9] The U.S. International Trade Commission estimates the total costs to America of import constraints at roughly $14 billion, or $50 per person.[10]

While trade surely provides some benefits, it is not likely that the benefits received by the majority of working families outweighs the costs they suffer from the lower wages and benefits, job losses, insecurity, and other forms of fallout from globalization.

In a democracy, one of the most sensible ways to judge a trade policy is to compare the outcomes with the promises

AN EXAGGERATED CLAIM OF GLOBAL BENEFITS

The Hamilton Project's estimate of the benefits from globalization rests heavily on a paper written by Bradford et al.* Applying others' research and models and assuming tariff reductions of almost 40%, the paper argues that trade liberalization added $1 trillion to U.S. GDP by 2004 (about 8% of GDP in that year). This number is far outside the bounds of any estimate of gains that one would obtain using standard economic models (models of static comparative advantage provide the foundation of assertions on the inevitability of the gains from trade). Using these more standard models would show a gain of less than 1% to GDP.

The Bradford paper is a review article of several studies, not a single one of which argues for benefits to the United States of anything close to the range of the estimates claimed by the article. One of the studies specifically states that its conclusions cannot be taken as directly relevant to policy evaluation. Another shows zero benefits from trade liberalization over the past quarter century.

Some of the technical arguments in the Bradford et al. paper directly contradict each other. For example, to support their claims of large price benefits, they assume that imported goods are the same as domestic goods. Elsewhere, to bolster an argument that imports give consumers the benefit of variety, they assume that imports are different from domestic goods. In the real world at least, goods cannot simultaneously be the same and different.

—L. Josh Bivens

* The Bradford et al. and other studies are described in Scott Bradford, Paul L.E. Grieco, and Gary Clyde Hufbauer, "The Payoff to America From Global Integration," in C. Fred Bergsten and the Institute for Intenational Economics, ed., *The United States and the World Economy* (Washington D.C.: Institute for International Economics, 2005).

made to the electorate. Thus, promoters of the North American Free Trade Agreement assured members of Congress and the public that NAFTA would create a booming middle class Mexican market for American goods, expand the U.S. trade surplus, generate net new jobs, and substantially reduce illegal immigration. The fact that Mexico had higher tariffs than the U.S. was said to assure that the net benefits would accrue to the U.S. Instead:

- The trade surplus with Mexico turned into a trade deficit—displacing hundreds of thousands of American jobs by 2005.
- Mexico's growth since NAFTA has been far below what is needed to provide jobs for its growing labor force.
- Real wages and incomes for most Mexican workers have stagnated and actually declined in many regions.
- Mexico's agricultural sector was devastated by subsidized grain from the U.S. and Canada. Over a million farmers have been dislocated in the corn sector alone. The dislocation of impoverished rural people will turn into a flood in 2008, when NAFTA dictates that all trade barriers against U.S./Canadian agribusiness be removed.
- Illegal migration from Mexico (representing some 85% of the total of undocumented workers) has more than doubled since NAFTA took effect in 1994, as workers now desperate to find good jobs risk their lives to come across the border.

The major economic impact of NAFTA was to reinforce the undercutting of the social contract in all three signatory countries. As in the United States, worker productivity in Mexican and Canadian manufacturing rose while wages stagnated (**Figure C**).

Moreover, no statistical calculation or economic theory can provide a clear answer to the question, for example, of whether the benefits of cheaper sneakers and electronic toys are worth the cost of lost jobs, disrupted families, and

increased economic insecurity. These are essentially value judgments, which economic consideration can inform but not, in a democracy, decide. At this point it seems clear that the voters think their values are not being reflected in current trade policy. A June 2006 poll showed that large majorities of voters—self-identified liberals, moderates, and conservatives—prefer policies that give priority to better jobs over those that emphasize cheaper prices.[11] The November election seemed to reflect that view.[12]

Workers elsewhere

As finance, trade, and technology relentlessly connect labor markets across borders, the wages and benefits of American workers are increasingly linked to the wages and benefits of workers in other economies. Thus, when the international treaties and policies that make up the rules of globalization protect and promote the interests of employers over employees, workers in all countries will suffer.

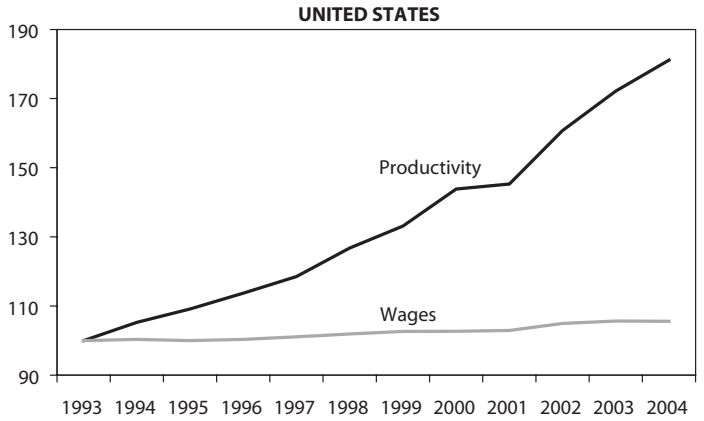
The present form of globalization has undoubtedly brought some benefits to some people in the world's developing economies. But again, the question is whether these benefits justify the costs, including the destruction of communities, the widening of economic inequality, the undermining of the social contract, and the crippling of the capacity of governments to pursue development strategies through regulation, procurement, and tax policy.

Great benefits are claimed, but the closer one looks, the more they

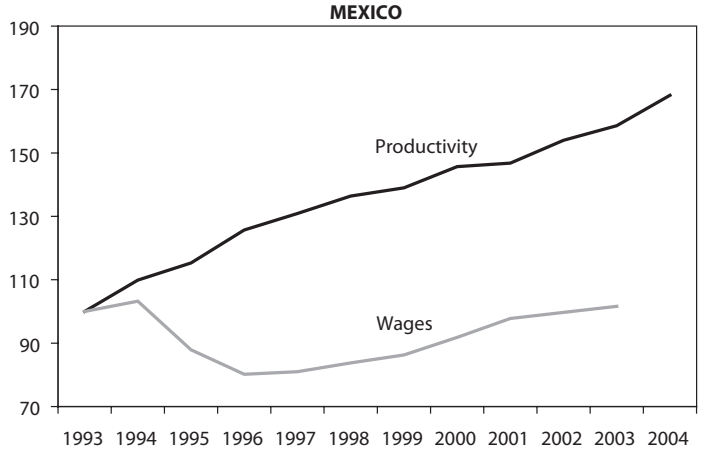
FIGURE C

Productivity and real wages in the manufacturing sector in the three NAFTA countries

SOURCE: IMF, ILO and EPI.



SOURCE: BLS and EPI.



SOURCE: INEGI, ILO and EPI.

shrink. In 2003, the World Bank estimated that a successful Doha Round of trade negotiations would generate $500 billion for Third World economies. After the report's methodology was criticized, the Bank lowered its estimate to $90 billion. Further adjustments by economists at Tufts University brought the estimate down to $39 billion, implying a benefit to those in the developing world of less than a penny a day.[13]

Indeed, the annual rate of per capita growth among developing nations, excluding China, in the era of global deregulation has actually declined, from 2.5% between 1960 and 1980 to 2.0% in the two decades that followed.[14] The reason for excluding China is that, rather than pursuing a "free trade and investment" agenda, it has managed its trade in a straightforward mercantilist policy of expanding exports and limiting imports. In contrast, most nations of Latin America have faithfully followed the free market fundamentalism often referred to as the "Washington Consensus." The results have been disastrous. From 1960 to 1980 real per capita income in Latin America rose 82%. Over the next 20 years it rose 9%. And between 2000 and 2005 it dropped to 4%.

The social and economic costs of the Washington Consensus' failure to generate either growth for the economies or prosperity for the workers of Latin America have been enormous. The costs include increased crime and violence, civil strife, the rise of the illegal drug industry, and outward migration of trained and ambitious workers. It is hardly a surprise that leaders have been elected in Brazil, Venezuela, Argentina, Chile, Bolivia, Ecuador, Uruguay, and Nicaragua who in various ways have all rejected the radical free market model so strenuously promoted by U.S. administrations in the past few decades.

Impact on immigration

The failure of globalization's promise to workers in poor countries is reflected in the rising waves of immigrants desperately seeking jobs and opportunities. In effect, elites in many poor nations are responding to the failure of neo-liberal policies by exporting their unemployment to the United States.

Economists may debate the exact impact of the accelerated number of immigrant workers on wage levels, but there is little doubt the result is a downward pressure.

The 12 million undocumented workers in the American labor force are particularly vulnerable to the power of employers and recruiters, who can threaten to hand them over to the authorities for deportation. In addition to low wages, these workers are often faced with brutal working conditions, cheated of their pay, and even physically abused. Exploitation of undocumented migrants primarily undercuts living standards at the bottom of the wage ladder.

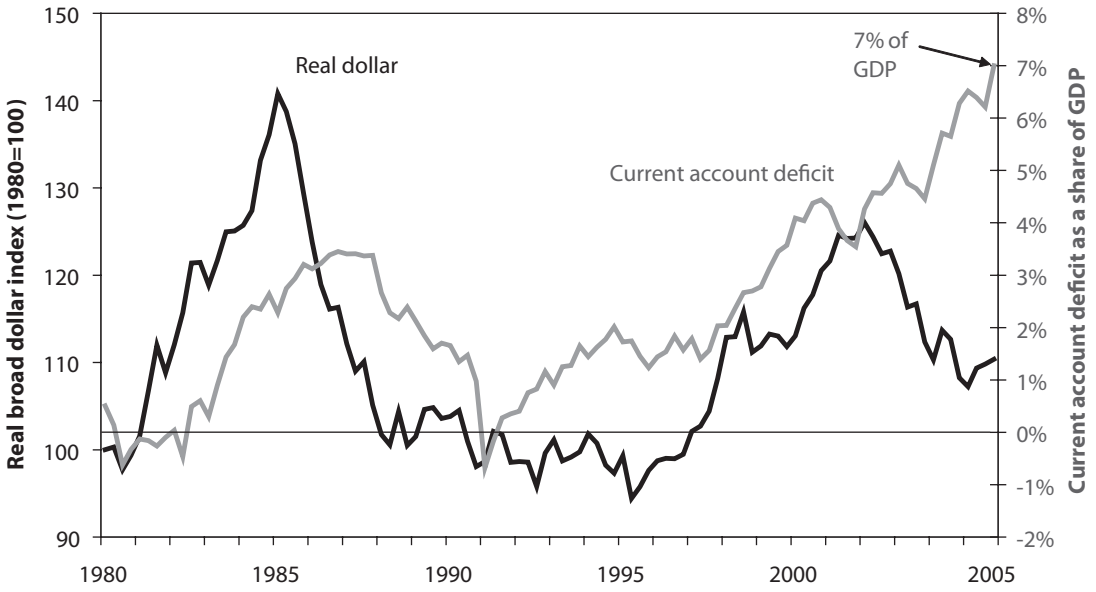
But U.S. government policies have also allowed employers to import immigrants legally, as an alternative to training and paying higher wages to Americans. Thus, the H-1B program permits employers to recruit and employ "temporary" professional workers on the grounds that firms face a "skill shortage." The program currently admits about 100,000 people a year. Salaries of H1-B workers are typically lower than the salaries of existing professional workers.

In some sense, many if not most employers always face a skill shortage in that they find it difficult to find *above-average* employees for the *average* wages that they are offering. The market answer is to raise wages. But if the U.S. government is willing to allow employers to bring in foreign workers who will work cheaper, the market incentive disappears. Moreover, although the program is supposed to be temporary, large numbers of people who come in under it stay in the U.S.—either legally or illegally—which is generally the case with temporary worker programs all over the world. As the late conservative economist Milton Friedman noted, the H-1B program is an unjustified subsidy to business.

Nursing has traditionally been an important avenue in America of upward mobility into the middle class, particularly for women. Yet, we continue to import thousands of nurses from other nations—many of them Third World countries desperately needing these skills at home—to fill a chronic domestic "shortage." In 2006, the U.S. Senate voted to increase substantially the number of foreign nurses allowed to come to the U.S. after the American Hospital Association claimed that there was a national shortfall of 118,000 nurses. Meanwhile, in 2005, U.S. nursing schools had to reject almost 150,000 qualified applicants for lack of space.

FIGURE D

The dollar and the current account deficit, 1980-2005



SOURCE: Federal Reserve Board of Governors, Bureau of Economic Analysis, and Economic Policy Institute.

The deficit/dollar debacle

For the past 25 years the U.S. has been buying more from the rest of the world than it is selling, and it has been borrowing and selling off assets to make up the difference.

The deficit in the overall U.S. current account, which represents the U.S. financial position in the global economy, will be close to $900 billion for 2006, about 7% of GDP. Until recently, the U.S. had a small surplus in the part of the current account that represents the difference between the earnings of Americans from foreign investments and foreigners' earnings on their investments here. Now, however, we are suffering losses in both our trading and financial markets.

The accumulated U.S. foreign debt at the end of 2006 will be somewhere between $2.5 and $3.0 trillion. This debt is made up of loans from abroad and foreign ownership of stocks and other productive American assets. Both represent present and future income that must be transferred from Americans to foreigners in the form of interest, dividends, and profits, and making good on these obligations will be a drag on future U.S. growth and incomes.

Textbook economics tells us that a sustained trade deficit should force the value of a nation's currency lower against other currencies, making imports more expensive and exports cheaper, until trade balance is achieved. But although the dollar has weakened somewhat in general (and a great deal against the euro in particular), it has not fallen nearly enough to bring down the trade deficit (**Figure D**).

The dollar has resisted market forces for several reasons. First is its importance as the world's premier reserve currency, used by most central banks to back up their money supply and to settle international contracts (e.g., for oil). Dollars are also in demand because the U.S. is seen as a safe haven for wealth from politically unstable societies. Thus, global demand for U.S. dollars has remained high even as demand for American goods weakens.

Secondly, many of our big trading partners, especially in Asia, keep their currency artificially low relative to the dollar (i.e., lower than justified by their trade surpluses with the U.S.) by accumulating dollars in reserve and intervening

in currency markets to maintain their currency's low value. China, for example, keeps its currency roughly pegged to the U.S. dollar. So when the dollar recently fell against the euro and the Canadian dollar, China, not the U.S., gained many export markets because the Chinese yuan also fell.

Thirdly, countries that run trade surpluses with the U.S. are re-lending the dollars they earn back to the U.S. in order to maintain the U.S. market for their exports. In effect, exporters to the U.S. are financing a U.S. consumption boom. Fueled by this foreign borrowing, U.S. consumption has grown faster than that of some of its developed country trading partners (e.g., Europe and Canada), with the result that our imports from them have risen faster than their imports from us.

The persistently overvalued dollar has undercut the competitiveness of American producers in both foreign and our own domestic markets, resulting in the shutting down of capacity, the discouragement of investment, and the abandonment of skilled workers, management talent, and shared knowledge and infrastructure that often took decades to create.

U.S. economic policies aggravated this threat to jobs and incomes through:

- implementing trade and investment agreements that leave foreign producers free to manipulate their exchange rates and undercut U.S. competitiveness;
- influencing the IMF, World Bank, and other international institutions to push developing nations to give priority to exports (rather than the development of internal markets); and
- publicly committing successive U.S. governments to maintaining an overvalued dollar.

Common sense and simple arithmetic suggest that the U.S. cannot go on spending more than it is earning forever. The trade deficit is now self-reinforcing: as income grows, spending on imports grows faster. This vicious spiral requires more foreign borrowing, making the burden of servicing the debt heavier. Given our propensity to import, the more we expand trade through trade agreements and other policies, the more debt we accumulate.[15]

It is often said that the root cause of the current account deficit is a weak U.S. savings rate—which can be solved principally through balancing the federal budget. It is theoretically true that, to the extent that we Americans saved more, we could pay for our imports with less foreign borrowing. But unless the core problem of eroding competitiveness is addressed, attempting to increase the savings rate implies that we reduce the deficit by lowering consumption (of both public and private goods and services) and therefore lower our incomes—so that we import less. Ironically, lowering our incomes will eventually mean less, not more, savings. It should also be remembered that during the latter part of the 1990s, when the fiscal deficit was reduced and finally balanced, the trade deficit continued to expand.

As the external debt grows, the numbers of exposed creditors will grow as well, with each becoming worried that others will start a run on the dollar, thus lowering the threshold at which some event (military, political, or economic) could start a panic. This year alone, the combination of the trade deficit and U.S. corporations buying up foreign assets will add roughly another $1.4 trillion to the huge supply of dollars sloshing around the world's financial channels. Until recently, it was not clear where investors fleeing the dollar would go. But euros now represent about 30% of hard currency reserves, and oil and other commodity contracts are increasingly being written in euros.

Without a change in policy, the market will sooner or later force the dollar down, rebalancing U.S. trade by cutting the price of what we sell and raising the price of what we buy, thereby lowering real incomes.

The central question is whether the landing will be "hard" or "soft." A hard landing would mean a sudden steep drop in the dollar, panicked financial markets, and spiking interest rates that could bankrupt over-indebted consumers, over-leveraged pension funds, and families with overpriced houses. Thanks to George W. Bush's tax cuts, the federal government will have limited ability to overcome an economic crisis by expanding its fiscal deficit, as it did in the last economic downturn.[16]

The more optimistic scenario is that the dollar will of its own accord fall gradually, allowing a readjustment without global trauma. But, left to the market alone, even if there is a soft landing, we are headed for further downward

pressure in American living standards. Sectors that have benefited from debt-fueled growth of the recent past—housing, retail trade—will shrink, either absolutely or relative to the rest of the economy; the cost of living will rise as imports become more expensive; Americans will be left to compete on the basis of lower wages; and it will take years before investors regain enough confidence in the U.S. to expand domestic production and build new industries for future domestic and foreign markets.

The macroeconomic problem of the trade deficit and the microeconomic problem of declining U.S. competitiveness in a global labor market reinforce each other, but they are hidden by the illusion of prosperity based on borrowing. Over time our eroding competitiveness requires a larger and larger compensating drop in the dollar in order to rebalance the trade and current account.

Turning this situation around will require a policy of expanding domestic production of tradable goods and services as we gradually lower the value of the dollar. Investors and workers need to have confidence that the U.S. government is committed to a future in which their investments in plant, technology, and skills will be justified in higher profits and better incomes.

It will not be easy, but the longer we wait the more painful the inevitable adjustment will be.

A new strategy

Current trade policies have already damaged the nation's competitiveness and financial solvency upon which future opportunities and living standards will depend. Reversing the present course demands a comprehensive strategy that rises to the level and urgency of the global challenge. It should address at least the following:

- Pursuing trade strategies that put American working people first.
- Increasing investment in people, infrastructure, and new technologies to enhance competitiveness.
- Restoring the lost bargaining position of workers.
- Reforming NAFTA.
- Building the foundation for a global social contract.
- Making government more effective.

The new strategy will require some economic restructuring to increase the share of productive investment and reduce the share of consumption in the economy. A reduction in consumption growth, with or without increased investment, is inevitable. But without a strategy, this restructuring, if left to the unregulated market and the irresponsible pursuit of current trade and tax policies, will cause more economic pain and inequality, risk financial instability, and threaten increased political polarization.

Responsible trade policies

A strategic pause

No matter what one thinks is the core problem of our exploding trade deficit (e.g., low savings, currency distortions, trade deals, skill deficiencies, the tax code) the reality of America's present condition is that the more trade expands, the larger the trade and current account deficits grow. Thus, the promiscuous promotion of more trade agreements before we are prepared for them simply makes our competitiveness problem worse and drives us further into debt.

The first step therefore is to do no further harm. Congress should immediately impose a strategic pause on all trade negotiations and postpone approval of agreements not yet signed until we have a credible program, agreed to by Congress and the president, (1) to reduce the current account deficit at least to the point at which it is not rising faster than our income—roughly about 2% of GDP; (2) to improve American competitiveness; and (3) to renew the social contract and safety net.

Replace fast track

The president's authority to put trade agreements to an up-or-down vote has essentially stripped Congress of any significant role in their negotiation. The result is trade deals that are written by influential multinational business interests—commonly the people that the trade negotiators have worked for or will work for when they leave government.

New rules for the trade agreement process should include required measurable objectives for U.S. negotiators, such as:

- labor rights and environmental standards having the same enforceable status as investor rights;
- no restrictions on U.S. or state governments from favoring domestic producers in economic development policies;
- no extraordinary investor privileges for the settlement of disputes;
- inclusion of protections against currency manipulation;
- reciprocity of open markets and enforcement provisions;
- assurance of basic levels of judicial independence and democratic norms in the negotiating partner.

Specific milestones should be included in negotiating instructions that provide Congress an opportunity to judge whether key objectives have been achieved. The president would, of course, continue to have the right to submit to Congress whatever agreement he or she wishes, but, if the objectives are not met, the agreement would not get fast track privileges.

A Plaza Accord II

In 1985, after the dollar had risen against other currencies, resulting in a rapid expansion in the U.S. trade deficit, Treasury Secretary James Baker reached an agreement with the financial ministers of the United States' major trading partners and creditors that successfully brought the dollar down through orchestrated intervention in the currency markets. Between early 1985 and late 1987 the dollar fell 26% against the currencies of U.S. trading partners, which helped reduce the trade deficit from 3% to 1% of GDP.

A similar effort is needed today, although it will be more difficult for a number of reasons. The trade deficit is much larger. The Cold War and thus military dependence on the United States is over. The Bush Administration has left the United States even less influential and credible with its trading partners. And the emergence of China as a new player and major creditor adds a large measure of uncertainty to any outcome. Economic circumstances have also changed. The amount of private capital moving through global markets and the number of private investors are substantially larger today, so the central banks may have less power to move the dollar downward.

The leaders of other major nations might see their common interest in helping the U.S. economy to a soft landing, but the politics are very complex. It will not be easy for the government officials of our major trading partners to agree voluntarily to shrink their surpluses with the U.S., much less to run a deficit without risking substantial political trouble at home.

So getting international cooperation for a managed adjustment to the dollar might well require economic brinkmanship, i.e., a threat to unilaterally protect the U.S. market against imports. In order for it to work, of course, the threat must be credible, and so the U.S. government should begin planning for unilateral temporary tariff increases to signal its firm intention. Among other things, it should point to Article 12 of the WTO rules, which permits temporary tariffs when a nation is facing a foreign exchange crisis. This argument might not stand up in a WTO court (it can be argued that the United States, whose floating dollar is used as a reserve currency, could not by definition have a foreign exchange crisis), but the current account deficit is at crisis levels whether it fits WTO definitions or not.

Economist Wynne Godley of the Levy Institute at Bard College has estimated the impact of an across-the-board tariff of 25% (oil excepted). He assumed that importers would pass on half of the increase and that foreign governments would retaliate with an average 10% surcharge on U.S. products. The result was about a 1.5 percentage-point improvement in the U.S. balance of payments.[17]

Others have proposed a somewhat different model. Financier Warren Buffet, for example, suggests that balance could be achieved by capping imports and auctioning off import licenses to foreign exporters.[18] Still others have proposed specific sanctions against China if it continues to resist revaluing its currency.[19] But given the mobility of capital to shift production to other low-wage countries, and the ability of foreign exporters to hide the real source of their product, a less discriminatory across-the-board solution may be superior and less politically dangerous than one aimed exclusively at China.

Review the H-1B and similar programs

Although there is justification for companies in special temporary situations to be allowed to import workers with critical skills and unique talents, there is no justification for a government policy that encourages importing skills instead of creating them at home. It is a mockery of the promises that have been to Americans that globalization would provide job ladders with upward mobility.

Moreover, the H1-B and similar programs have been abused. The definition of a labor shortage is vague and increasingly stretched to the point where the approval is hardly more than a routine rubber stamp. Among other abuses, employers have been found to request foreign workers for facilities in low-wage states with relatively small supplies of highly technical labor, only to employ them at low wages in higher-wage areas.

A thorough congressional review of these programs' purposes and an evaluation of their operation is needed. Existing contracts must be honored, but, with carefully defined exceptions, new applications should not be approved pending such a review.

Competitiveness policy

The above policies might stop the bleeding, but they do not add up to a cure. Without an improvement in the fundamental competitiveness of American-made products and services, the dollar will have to fall continuously until U.S. wages and other costs converge with those of our trading partners

By and large, the fate of American competitiveness will be determined by the activities of workers, managers, and investors in the private sector. But as the history of successful economic development has shown, competent government policies are essential.

A competitiveness agenda for the 21st century must make manufacturing a priority. Despite the conventional portrait of manufacturing as an obsolete economic sector, it must be a part of our future. We cannot earn our way back to trade balance (or anywhere near it) in a way that increases real incomes without exporting more than we import—and for the most part, goods, not services, are what we do and will trade.

Moreover, developing technological comparative advantages that can employ large numbers of people depends on the existence of manufacturing. There is much about the process of technological innovation that remains a mystery, but we do know that it involves trial-and-error and requires hands-on access to the production process.

A manufacturing base is also essential for national security. Today, components of systems that are essential to military security are outsourced and supply lines[20] are extended around the world. This structure not only makes U.S. national security vulnerable to disruption, it creates constant pressure for an expanded American military presence around the world to protect the outsourced supply lines.

The targeting of manufacturing is not an argument for preserving any single industry, particularly since many of the products we will make in the future will be different from the products we are making today. Rather, it is an argument for providing the necessary supports and incentives for a healthy foundation of skills, technology, infrastructure, and capital for goods production that can exploit the changing demand in the domestic and global marketplace in ways that support high wages.

A high-wage strategy will require a shift in the pattern of future growth toward an industrial base of perhaps 10 million more workers over the next decade. This is certainly not an impossible goal in a labor force that now numbers 150 million,

but it will require a dramatic change from policies that have discouraged long-term investment in manufacturing and have signaled to young people that they would be better off becoming international lawyers or financiers than engineers. Some of the specific ways to send the appropriate signal regarding competitiveness to the private sector include:

Eliminating perverse tax incentives

By law, corporations that invest in the United States pay taxes when they are earned. But corporations that invest overseas can delay the payment of taxes until they repatriate their profits—which can take a long time. In 2005, in order to get some short-term relief to the fiscal deficit, the Congress voted to offer corporations that brought their money back that year a 5.25% tax rate, a much lower rate than they would pay on profits made in the U.S.

This loophole might have been justified after World War II as a way of helping Europe and others get back on their feet. But it has long outlived its rationale and should be eliminated.

Indeed, U.S. integration into the global economy requires us to rethink our whole approach to taxation. Other nations, for example, use "border-adjustable" value-added taxes to favor exports over imports. A progressive VAT is something that ought to be considered as an instrument to level the playing field.

Supporting effective research and technology development

There is a virtual consensus among leaders of both political parties in support of increased federal funding for research and development. Its only constraints at present are budgetary—those imposed by the Iraq War and the Bush tax cuts. But in the integrating global economy, simply providing funds for companies, universities, and research centers for this work can easily be counterproductive, because the resulting products and processes are increasingly likely to be produced in other countries. Not only have American firms become global, but so have universities, with partnerships and subsidiaries around the world. Harvard, for example, now refers to itself as a "world university."

In the global economy ideas cannot be stopped at the border. By its very nature, research and innovation need to be free of bureaucratic constraints. We need government policies that increase the chances that research and development will be channeled to production in the United States. Precedents for guiding the location of end-use production already exist in the area of military-sensitive R&D.

Re-emphasizing industrial extension services

We do not have to invent a new program for aid to U.S. manufacturing. Over the past 20 years local and state-based efforts to provide technical, managerial, and financial assistance to small- and medium-sized firms producing in the U.S. have grown into a rich network of talented people. States and municipalities have developed an institutional infrastructure that connects businesses with technical and business schools. These efforts—with the great advantage of being locally based—should be enriched and expanded throughout the country.[21]

Launching a national energy development program

U.S. history is full of examples of successful government leadership in the creation of great industries that propelled U.S. growth and prosperity. The U.S. government financed the first assembly line; subsidized railroads, metal ships, and jet planes; organized the highways for the auto industry; and nurtured long distance communication, electric power, and computer technologies. It organized the technical assistance, marketing, and financing that made American agriculture the most profitable in the world.

Many of these great national enterprises were motivated by security concerns. Today the most pressing economic issue affecting our national security is our dangerous reliance on imported energy. Although this dependence is widely recognized by the public and policy makers, the policy debate is stalled. Ideological blinders have limited the discussion

to supply-side proposals to accelerate the draining of U.S. off-shore oil reserves and demand-side proposals for large increases in the price of energy that are fiercely resisted by a public that has come to rely on cheap energy.

But there is now a great opportunity to develop a series of 21st century industrial sectors devoted to the generation of alternative energy that can spur technological advances and at the same time generate high-wage jobs.

The federal government began such an effort during Jimmy Carter's presidency in the 1970s. But in the wake of the radical free market ideology that later dominated federal policy and the drop in oil prices in the 1980s, forward motion was abandoned. One result is that the European and Japanese governments nurtured their own alternative industries and overcame our lead in this area. Today, the Japanese have 50% of the global market for solar technology, and the Europeans serve 90% of the market for wind turbines.

The specific projects Carter began may or may not have succeeded. Innovation is a process of trial and error. But clearly had we pursued such a program over the last 25 years, we would be miles ahead of where we are now. The need is not to become completely self-sufficient in energy, but to reduce the level of dependency that makes us vulnerable to political and economic threats to our energy supply.

No single "silver bullet" program will do it. It is impossible to say exactly which combinations of alternative fuels—hydrogen, solar, bio-mass, wind, geo-thermal—will prove the most effective. But neither was it possible to know just what combination of technologies would get us to the moon when John F. Kennedy made that commitment in 1960. What is critical is the commitment that gives American workers and investors the confidence that time and money spent developing skills and businesses in the alternative energy sector can pay off.

The Apollo Alliance, a coalition of business, labor, and environmental organizations, has proposed a $300 billion effort over 10 years to kick-start and nurture a major effort.[22]

In a forthcoming paper for the Agenda for Shared Prosperity, economist George Sterzinger estimates the substantial job creation associated with increased energy production from several alternative technologies, as well as potential bottlenecks and development paths for bringing the production to market.

American policy makers have the skills, the resources, and the public support for such a program. All we need is the will.

Restoring the social contract

Training and education

As the economist Joseph Schumpeter reminded us, capitalism is a process of "creative destruction." That is, growth always produces job loss and product obsolescence. Integration into the global market has magnified and sped up this process, generating even greater insecurity and job volatility and undercutting the capacity of workers to join together to protect themselves.

It has long been recognized that a competently managed market economy will provide ways to make this inevitable shifting among occupations and industries efficient and humane. Unemployment compensation, public employment programs, job search assistance, and local economic development are among the recognized tools used. Moreover, given that public policy plays such an important role in determining who wins and who loses, it is generally recognized, although certainly not universally, that to some degree winners who get the benefits should provide some help to the losers.

The experience of the advanced nations that have been most successful in competing in the global economy while maintaining high incomes and financial security (e.g., Sweden, the Netherlands, Denmark) has demonstrated how social safety nets and partnerships with trade unions can enhance competitiveness by using the periods of unemployment that accompany economic growth and change to upgrade the skills and flexibility of workers while supporting their incomes.

Unfortunately the United States has lagged far behind the best practices in the world. In fact, the low levels of unemployment assistance tend to force the unemployed to quickly accept jobs that are lower paying and require fewer, not more,

skills. Therefore, we need a large and serious upgrading of our transition assistance in ways that support good jobs.

First, any such strategy must provide for much more generous assistance for the unemployed. The current levels of support (averaging roughly $260 a week for a maximum of six months) are obviously inadequate. Second, the system of education and job training needs to be completely revamped and upgraded to the levels of our more advanced competitors. The cost of a minimal system for adjustment is in the order of $75 billion per year. The Danes, whose economy competes in the world and who enjoy high and rising incomes, spend 4% of their GDP on such programs—the equivalent in the U.S. economy of about $500 billion.

The recent flurry of proposals to solve the adjustment problem with "wage insurance" does not meet the criteria for an efficient and humane program: the proposals on the table encourage a downgrading of skills and are financed by taxing workers and/or reducing unemployment compensation. Thus, they propose that the losers in the economic transition, not winners, support the other losers. (For more, see the accompanying box on wage insurance.)

Bargaining power

Trade unions have been critical in supporting the social contract for American workers, and not only union members: the have played a major role in setting wages and working conditions and advocating for laws that benefit non-union workers are well. The threat of unionization has been a major force in supporting higher wages and benefits in the non-

WAGE INSURANCE IS NOT THE ANSWER TO GLOBALIZATION

The typical wage insurance proposal offers job losers a payment of half the difference between the salary at their old job and a lower-paying new job, for up to two years. Thus, a textile worker who lost a job that paid $28,000 and accepted one at $18,000 would be paid $5,000 a year (half the $10,000 salary cut) for two years. The subsidy permits the employer to offer her less than he might have otherwise, because he knows that the subsidy will make the job substantially more attractive. Wage insurance can encourage downward mobility, particularly when the subsidy is available only if the job is taken within a limited time, in order to encourage "rapid reemployment." To the extent that it cuts short a worker's job search or turns a worker away from a training opportunity by making a low-paying job seem more attractive, it leads to the under-utilization of skills and lower productivity. After two years of wage insurance, instead of having made an investment in her skills, the worker is, perhaps, left with another wage loss and an $18,000 a year job.

By subsidizing low-wage jobs, wage insurance reduces upward wage pressure on employers. The employee earns $23,000 at a cost of only $18,000 to the employer; the $5,000 supplement makes the low-paying job acceptable to the employee.

Some advocates suggest paying for an expanded wage insurance program by repealing the unemployment insurance program and replacing it with voluntary, self-funded personal accounts. But any scheme that cuts the safety net for one group of job losers to repay the earnings losses of another group is no answer to economic insecurity.

Money spent on wage insurance is money that won't be spent on education or skills training. The federal government's support for job training and employment services for dislocated workers is half what it was in 1983, after adjustment for inflation, despite a 30% larger workforce. Wage insurance is a poor substitute for a significant commitment to provide skills upgrading and educational opportunities to dislocated workers (including sufficient income support to permit schooling).

—Ross Eisenbrey

union sector. By allowing employers to undercut trade unions through threats and intimidation, our globalization policies have given firms substantial additional bargaining leverage over their employees.

The current labor law is 70 years old and is no longer very useful for workers being thrust into a globalizing economy. Among other things, the tortured process of certifying a union as collective bargaining agent makes it all but impossible for workers to organize. Yet, while roughly 13% of American workers belong to a union, polls show that 50% would join if they had the opportunity.

In virtually every other advanced nation, a majority of workers can form a union by signing a card expressing their preference. Labor law reform that would permit this "card check" system is long overdue.

Changes in management tactics and government regulations have also exacerbated the growing imbalance in bargaining power. For example, the right to strike has been severely crippled because employers will permanently replace workers who join the picket line. Another is the National Labor Relations Board decision (the "Kentucky River" cases) that permit employers to arbitrarily and falsely classify jobs as "supervisory," thereby enabling employers to deny workers a variety of rights from overtime to union membership. Such efforts to further weaken the market power of workers should be reversed.

Lifting of the burden of benefits

For much of the American middle class, the social safety net has depended on a system of health care and pension benefits provided by employers. But globalization has put employers under great competitive pressures to cut costs. The pressure comes from both low-wage countries, where workers get few if any benefits at all, and more advanced nations, where government shoulders more of the health care and pension burden. Globalization also gives U.S. companies that can afford such benefits the opportunity to escape paying them. As a result, benefits are shrinking and jobs with benefits at all are becoming scarcer. For middle-aged and older workers, losing such a job can be a calamity.

The reality is that American workers can no longer rely on a voluntary employer-based social safety net, nor can American products be sufficiently competitive if employers have to compete with foreign firms that do not have that benefits burden. Successfully competing in the world market will demand greater government participation in health care and the provision of pensions.

In both areas, efficiency and mobility require universal access and public accountability. As papers for the Agenda for Shared Prosperity by Jacob Hacker and Teresa Ghilarducci will show, universal systems for health care and pensions can be built on existing successful programs like Medicare and Social Security.

Replacing NAFTA

NAFTA succeeded in integrating the three North American economies to the point of no return. Too many economic channels have been redirected north-south to reverse the course of economic integration. But it failed to deliver on its promises—including its promise to stem the tide of undocumented workers crossing the border in search of jobs that pay enough to support them. The immigration issue cannot be solved with walls or guest worker programs. It can only be solved with the creation of sustained and broadly shared growth in the places the vast majority of immigrants come from—primarily Mexico.

Since we cannot go back, we must go forward and replace NAFTA with a more comprehensive agreement. The first task is to establish a set of rules for the common market that recognizes the three NAFTA nations' joint economic future. The rules would include, at a minimum, a "bill of rights" for citizens of North America, enforceable in all three countries, that would reestablish rights for people at least as strong as the extraordinary protections NAFTA gives to corporate investors. These rights would include guarantees of freedom of association and collective bargaining across borders, as well as public transparency in government dealings with the private sector.

To support this revision, we also need a continental "grand bargain" in which Canada and the United States would commit substantial long-term aid to Mexico in order to nurture higher and sustainable economic growth, while Mexico

commits to policies (independent trade unions, adequate minimum wages, equitable taxes, assistance to its depressed farm sector) that assure wages in all three nations rise with their productivity.

Finally, we should begin discussions toward a North American customs union to manage foreign trade in the service of the needs of the people of all three countries and to develop a North American option in response to the growing regional economies in Europe and Asia.

New global rules

The current set of rules governing global economic relations—what Renato Ruggiero called the "constitution of a single global economy"—are inadequate, and should be revised, on at least three major fronts.

International labor rights

The absence of any social and human dimension to the regulation of the market would not be tolerated within the domestic economy of most developed nations nor in many less-developed nations. The institutions charged with managing the global economy—the WTO, the IMF, and the World Bank—not only reject responsibility for such a dimension, but by ideological culture and policy actively undermine social and human concerns in their operations. When challenged, the bureaucratic response is that labor rights are the responsibility of the International Labor Organization. This assertion is disingenuous. While the WTO has the power to protect investors through trade sanctions, and the IMF and the World Bank through their loans and grants, the ILO, a tripartite structure in which business, government, and labor representatives have equal voting rights, has neither the ability nor the authority to protect workers.

It is often charged that labor rights are a smoke screen for "protectionism" and that developing nations do not want their workers protected. Surveys show that most people in the world's nations think that labor rights and environmental standards should be a part of trade agreements. The resistance comes from elites in both rich and poor nations who have a common interest in weakening workers' bargaining power everywhere.

It is time for the United States government to stop dragging its feet on the issue of international labor rights. We should not be a party to any new WTO trade negotiating round that does not provide workers the equivalent protection that it gives investors. At a minimum this means making the core standards prescribed by the ILO, including the right to join a union and bargain collectively, enforceable with trade sanctions.

No one model

The World Bank, the IMF, and other international financial institutions have forced developing nations into following policies that suppress worker incomes and the growth of internal markets.

After a quarter century, the fixation on the export-led, one-size-fits-all package of development known as the Washington Consensus has clearly broken down. Fiscal austerity, privatization, and deregulation and the ripping up of social protections for workers have produced slower growth, a worsening distribution of income and wealth, and more political instability.

Yet, although the Washington Consensus has broken down, we cannot return to the previous model that combined centralized government power in alliance with elite oligarchs. The lesson is that there is no one model of economic development that fits all. Each developing nation has its own economic, political, and social environment, and successful development is most likely to be a product of experimental trial and error.

The United States government should therefore use its influence in the World Bank, IMF, and other international financial institutions to clear away the ideologically driven culture that has developed in those agencies and promote the design of new programs crafted to allow governments in poor countries to work through development paths that are more suited to their local conditions.

A competent global financial system

The crisis of 1997 brought the global economy to the brink of meltdown. It was averted by the rescue operations led by the U.S. Treasury—high-wire ad hoc policy acrobatics that depended on the talents and contact lists of a few people who were almost by accident in the right place at the right time. This is hardly a satisfactory way to manage the global economy.

Moreover, as the world's greatest debtor, the United States cannot continue to act as banker to the rest of the world, i.e., supplying liquidity through printing more dollars to pay for its imports. The expanding importance of the euro will gradually take some of the burden from the dollar, but relying on any one or two currencies to support the world's money supply will continue to lead to the distortions and imbalances reflected in the U.S. imbalance of payments, which has poor nations supplying capital for consumption in rich nations.

The world needs a new financial architecture that forces the ongoing adjustment of current account imbalances. Nations that run surpluses must be forced to revaluate, and those running deficits must devalue their currency in a routine way.

The world does not lack people who have been thinking about this issue;[23] it just lacks the will and attention of the leaders of the major nations. As still the most influential power in the world, the U.S. government should take the lead in establishing a high-level international planning group to start the process of building a more stable and equitable global financial system.

Organizing for better policy making

Trade should be an instrument for expanding American living standards and opportunities, not a goal in and of itself. But the way both the Congress and the executive branch are organized makes negotiating and approving trade deals the number-one priority and obscures the more fundamental questions of the U.S. role in the global economy—both to the public and to policy makers themselves. It also makes it even easier for special private interests to drive public decision making.

Refocusing globalization policy on economic policy, rather than deal making, would be enhanced with two shifts in government organization:

- Each branch of the Congress should establish a Select Committee on Globalization, to include members not only from the Ways and Means and Finance Committees (whose present jurisdiction over trade stems from the even narrower reason that changes in tariffs affect government revenue), but also from the committees dealing with education, labor law, transportation, telecommunications, foreign affairs, armed services, and other relevant areas. The purposes would be to connect the dots of economic integration among the various committees. Select committees would have the power to hold hearings, issue reports and recommend legislation.
- The Office of the U.S. Trade Representative should be relieved of its cabinet rank. The USTR serves neither a special administrative function (as does the Office of Management and Budget) nor a generally acknowledged national goal (e.g., environmental protection, drug control). Rather, it should be an instrument for negotiation of trade objectives set by policy makers with a responsibility for a vision larger than deal making. A new department of industry and trade should be formed out of the USTR and Commerce Department, and its mandate should define its mission as the support of job creation in the United States.

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The policy agenda described above clearly represents a major departure from the policies of the last 20 years. It is of course not likely to be enacted all at once, particularly under the present administration. But the Congress can begin the task now. It can implement a strategic pause, put conditions on fast track, revise R&D guidelines, support new energy

initiatives, and start putting the national social contract back together by allowing workers the freedom to join a union. And it can finally begin the national dialogue through hearings and debate that will help both citizens and leaders address the question of America's role in the new global economy. The answers to these questions will determine not only our economic future but the future of generations to come.

— Jeff Faux is a distinguished fellow at the Economic Policy Institute. His latest book is The Global Class War *(Wiley 2006).*

Endnotes

1. Lawrence Mishel et al., *The State of Working America 2006/7* (Cornell University Press 2007), Table 3-30.
2. Some have attempted to minimize the impact of globalization on inequality by claiming the culprit is "technological change," which increases the demand for skilled labor relative to unskilled. But the evidence for this is weak. Indeed, the economic models upon which this conclusion is based do not measure "technology" at all. Technology is simply a label put on the largest part of the causation of inequality that is in fact unexplained—as reflected in frequent references to the "mystery" of rising inequality. Evidence presented in Mishel et al. (2007) provides detailed reasons for skepticism about pinning too much of the blame for rising wage inequality on technology.
3. Wolfgang Stolper and Paul Samuelson, "Protection and Real Wages," *Review of Economic Studies*, Volume 9(1): 58-73 (1941). This article is a foundation of modern international trade theory.
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5. J. Bradford Jensen and Lori G. Kletzer, "Tradable Services: Understanding the Scope and Impact of Services Outsourcing," Peterson Institute, Washington, D.C., May 2006. http://www.iie.com/publications/papers/paper.cfm?ResearchID=638
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12. Public Citizen, "Nationwide Candidates Win by Fighting for New Trade Policies, Opposing NAFTA Model," http://www.citizen.org/hot_issues/issue.cfm?ID=1471
13. Timothy Wise and Kevin Gallagher, "Doha Round and Developing Countries," Policy Brief No. 22, Research and Information System for Developing Countries, April 2006; and Frank Ackerman, "The Shrinking Gains From Trade: A Critical Assessment of the Doha Round Projections," Global Development and Environment Institute, Tufts University, October 2005.
14. Alan Heston, Robert Summers, and Bettina Aten, Penn World Table Version 6.2, Center for International Comparisons of Production, Income, and Prices at the University of Pennsylvania, 2006.
15. For the most part, the recycling of dollars is *not* financing productive investment. In recent years foreign investment has been increasingly shifted to the purchase of U.S. government securities. Indeed, the willingness of foreigners to invest in dollar-denominated assets seems increasingly based on political, rather than economic, decisions. On the other hand, average returns to investments in the U.S. are actually now lower than returns from investments elsewhere in the world. To some degree, American investors are borrowing cheap money from the Chinese to reinvest for greater returns—in China. How long the Chinese will be willing to indulge U.S. consumers and give U.S. investors an advantage in this "arbitrage" is unknown, but it is not likely to last for a long time. As economist Joseph Stiglitz has pointed out, China has other options. "Rather than lending money to the United States to increase consumption by these people [i.e., America's rich], it could lend its money to its own people or it could finance investment in its own country."
16. Grim forecasts to this effect can be found in recent pages of the *Economist, Business Week*, and other business periodicals. Former Federal Reserve chairman Paul Volcker in 2004 said that there was a 75% chance of an economic crisis over the next five years, which "could be fueled by a decision by other nations to reduce their purchases of U.S. securities." Even N. Gregory Mankiw,

who as Bush's chief economist famously praised the off-shoring of American jobs, recently acknowledged that U.S. reliance on foreign savings to support its consumption means a "less prosperous future." Trends forecast by economists at the Levy Institute suggest a crisis by 2010. The International Monetary Fund, a reliable supporter of the economic policies of U.S. administrations, acknowledges in its 2006 *Global Financial Stability Report* that "a decline in the dollar could become disorderly." Note that the IMF believes that a dollar decline is inevitable.

17. Wynne Godley et al., "The United States and Her Creditors: Can the Symbiosis Last?" The Levy Institute of Bard College, September 2006.
18. Warren Buffett, "America's Growing Trade Deficit Is Selling the Nation Out From Under Us. Here's a Way to Fix the Problem—And We Need to Do It Now," *Fortune,*" October 26, 2003.
19. In 2005 U.S. Senators Charles Schumer and Lindsey Graham introduced legislation to this effect.
20. Barry C. Lynn, *End of the Line* (Doubleday 2005).
21. See Sue Helper's forthcoming paper for the Agenda for Shared Prosperity.
22. Apollo Alliance, http://apolloalliance.org/
23. See, for example, Joseph Stiglitz, *Making Globalization Work* (Norton 2006); John Eatwell and Lance Taylor, *Global Finance at Risk* (New Press 2000); and Robert Blecker, *Taming Global Finance* (Economic Policy Institute 1999).

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