In Whose Interest?
Inclusive Trade vs. Corporate Protectionism

By Harley Shaiken

The photo on the opening page of The New York Times business section in late September 2016 is striking. A woman in a bright-yellow t-shirt and blue pants stacks cans for a food bank at a local union hall with her back to the viewer. Emblazoned on her t-shirt is the slogan “Fair Trade Is Our Future.” The caption for the photo reads “Cathy Marsh, a former employee of the steel mill in Granite City, Ill., organized donated food for laid-off workers this month.” These laid-off workers include almost 900 of the 1,250 who used to work at the U.S. Steel plant in Granite City, and their prospects are bleak.

In the article following the photo, titled “More Wealth, More Jobs, but Not for Everyone: What Fuels the Backlash on Trade,” New York Times reporter Peter S. Goodman correctly points out that “economists failed to anticipate the accompanying joblessness and governments failed to help.” As he observes, “across much of the industrialized world, an outsized share of the winnings has been harvested by people with advanced degrees, stock options, and the need for accountants.”

Meanwhile, ordinary workers from Rotterdam to Granite City — where advanced degrees and stock options can be scarce — are feeling the pain and dislocation of lost jobs. In the United States, they fueled a sharp political backlash that resulted in the upset victory of Donald Trump as president in 2016. In emerging economies, workers from Ciudad Juárez to Hanoi may be finding new jobs — a welcome development — but wind up with few rights, low wages, and harsh conditions, in any case.

The Distorted Debate Over TPP

While proponents cast the debate over trade agreements as a titanic struggle between those embracing a global future and those seeking to retreat behind national borders, the reality of what’s going on is profoundly different. The fierce debate in the United States over the Trans-Pacific Partnership (TPP), a mega-deal between the U.S. and 11 other countries, including Canada, Mexico, and Japan, is a case in point. The agreement encompasses almost 40 percent of global GDP and about 25 percent of global trade. Equally important, the TPP was meant to set the standard for trade across the globe for decades to come.

While the TPP already appeared to be on life support after a bruising electoral campaign in which both major presidential candidates opposed it, Trump pulled the plug weeks after the election when he announced, “I am going to issue our notification of intent to withdraw from the Trans-Pacific Partnership, a potential disaster for our country.” That said, the U.S. Chamber of Commerce, an army of corporate lobbyists, most Republican members of Congress, and some Democrats would still like to see the TPP happen in one form or another. The Cato Institute’s Daniel Ikenson pleaded in Foreign Affairs “for Mr. Trump to put the TPP on the back burner and keep open the option to reconsider it in the future, when the deal’s geostrategic imperative becomes more apparent.” Whatever happens with this agreement, the issues in this debate are vital for defining the role of the U.S. in the global economy going forward.

Critics of the TPP fall into two camps, one nationalist and the other internationalist. In his campaign, Trump hammered bad trade deals as the problem undermining the U.S. economy and threatened high tariffs as a critical part of the solution, a perspective that clearly resonated. However, for many others, including political leaders, labor leaders, academics, and environmentalists, the issue isn’t “free trade” versus protectionism — a fascinating 19th-century debate to be sure — but rather who wins and who loses in a far more complex 21st-century global economy. These critics argue for rules of the game insuring that trade benefits workers, consumers, communities, and the environment.

Supporters of the TPP assume that “everyone wins” pretty much automatically — theoretically, production goes where it is most efficient, allowing goods to become cheaper and real incomes to rise. Yet real people with
regular jobs in Granite City or Milwaukee tend to be unconvinced by the “everyone wins” argument and rightly so. Popular thinking (and Donald Trump), however, assume winners and losers are defined primarily by national borders in a zero-sum game. In nationalist terms, “we” win because the United States negotiates well, or “we” lose because the United States negotiates badly. But the nationalist view is as far from the truth as a reflexive “everyone wins” globalist view. The division between winners and losers is within countries rather than between them. Under the structure of modern trade agreements, ordinary people in both poor and rich countries can lose, while the wealthy and the powerful win. Mexico didn’t win with Nafta, and the United States didn’t lose, as Donald Trump put it, but plenty of ordinary people in both countries missed the gains, and many were devastated, losing jobs, homes, college educations, and much more.

Despite these new global realities, “economists can be counted on to parrot the wonders of comparative advantage and free trade whenever trade agreements come up,” Harvard economist and trade advocate Dani Rodrik points out. Congressman Sander Levin, an influential member of the U.S. House Ways and Means Committee, concurs when he observes that “the 18th- and 19th-century notion of comparative advantage tells us almost nothing about modern trade agreements.” He asks, “What do David Ricardo and Adam Smith have to say about the inclusion of investor-state dispute settlement (ISDS) in our trade agreements? About biologics data exclusivity?”

Nonetheless, TPP proponents tend to launch into lectures on the abstract benefits of free trade. “Through the creation of economies of scale and the exploitation of comparative advantage, nations involved in trade become more efficient producers,” a Wilson Center study informs us. “We see these benefits play out clearly in U.S.–Mexico trade.” Such benefits, however, are not seen as clearly in the food bank lines in Granite City or among workers earning sharply depressed wages in Ciudad Juárez. “It’s off-point and insulting to offer an off-the-shelf lecture on how trade is good because of comparative advantage and protectionists are dumb,” Paul Krugman writes. He isn’t arguing against the potential benefits of expanded trade by any means, but rather against the simplistic notion that textbook theories translate seamlessly to broadly shared benefits on Main Street.

Free trade as a mantra has driven the TPP debate to a surprising degree. New York Times columnist Thomas Friedman reportedly admits in a television interview, “I wrote a column supporting Cafta (Central American Free Trade Agreement) … I didn’t even know what was in it. I just knew two words: free trade.” Typical of much media coverage, Washington Post columnist Robert J. Samuelson refers to all opposition to the TPP as “anti-trade sentiment” rather than sentiment against the skewed terms of this agreement. One can have an internationalist vision, embrace expanded trade, and oppose rules of the game that ravage working families and communities.

The reality is that all trade is highly managed today. MIT economist Simon Johnson, a former chief economist at the International Monetary Fund, cautions that “who gains and who loses is very much dependent on … the details of the agreement.” The TPP has a lot of details. 30 dense chapters and appendices are spread out over 6,000 pages. A classic free trade agreement could be laid out on a postcard: all parties agree to eliminate tariff and non-tariff barriers. What then comprises the remaining thousands of pages in the TPP? The agreement sets out enforceable rights and protections for corporations and investors — necessary in global trade to be sure — but crafted in an excessively narrow way to privilege corporate interests over those of consumers, workers, and the environment.

The outcome reflects the negotiating process. “With 500 official U.S. trade advisers representing corporate interests having been given special access to the policy process,” Jared Bernstein and Lori Wallach write, “it is not surprising that corporate interests have thoroughly captured the negotiating process…” The result? Provisions such as investor-state dispute settlement (ISDS) panels reflect the sharp corporate tilt.

“This is not a trade agreement,” Krugman points out. “It’s about intellectual property and dispute settlement; the big beneficiaries are likely to be pharma companies and firms that want to sue governments.” Proposed three-person panels — composed of corporate “experts” — allow international investors to sue in private arbitration. While the stated goal is fair treatment, Joseph Stiglitz suggests a darker purpose: “to make it harder to adopt new financial regulations, environmental laws, worker protections, and food and health safety standards.” Foreign firms would be able to sue the U.S. government in these tribunals as well, he points out. “Two arbitrators can, in effect, undermine decisions of Congress and the president.” The net result is corporate protection at the expense of democratic values and the well-being of ordinary people.
In Whose Interest?

In the 2016 U.S. presidential election, labor unions and the American voter were clearly on the mind of the then-presidential candidate Donald Trump. As he won the primary and general elections, labor conditions in Mexico became more like those in Honduras. Why? In terms of economic integration, the agreement created two very different North Americas as integration, the agreement created.

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What would happen if workers in Mexico had the right to form independent unions and bargain collectively in the export sector? The lives of Mexican workers would improve considerably and a more balanced trading relationship would result as Mexican workers purchase more from the U.S. and elsewhere. If the wage bill in the hypothetical plant above doubled in Mexico, the savings for the corporation would still be $240 million relative to the U.S. Moreover, significant additional corporate labor cost savings come from salaried and supplier workers nearby and throughout Mexico. Some costs — such as security or transportation — will be higher in Mexico, but the overall corporate gains remain high.

Isn’t linking high productivity to growing wages a bit utopian? It wasn’t for Henry Ford. In 1913, he combined the soaring productivity of the moving assembly line with the $5 day, double the prevailing wage at the time. Editorial writers, economists, and competitors warned this move was a dangerous scheme and said Ford would bankrupt the industry. Instead, profits rose and workers entered the middle class. In the aftermath of World War II, powerful industrial unions linked rising productivity to higher pay and benefits across the U.S., creating a vibrant economy. In fact, the most important model to roll off Detroit assembly lines or come out of Akron rubber plants or Pittsburgh steel mills was a rapidly expanding middle class.

Absent this wage/productivity link in Mexico, Nafta has reshaped the geography of the North American auto industry. In 2005, the U.S. produced 73 percent of all light vehicles in North America, Canada produced 16 percent, and Mexico 10 percent. Projections for 2021 indicate that while the overall volume of auto production will increase in North America, the U.S. share will fall to 64 percent, Canada will plummet to 10 percent, and Mexico will more than double to 26 percent.

North America Light Vehicle Production Share

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<th></th>
<th>2005</th>
<th>2020 (projected)</th>
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<tr>
<td>Canada</td>
<td>16.7%</td>
<td>9.9% (1.9 M)</td>
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<tr>
<td>Mexico</td>
<td>10.1%</td>
<td>26.4% (5.1 M)</td>
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<tr>
<td>U.S.</td>
<td>73.2%</td>
<td>63.7% (12.2 M)</td>
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It’s hardly a surprise that international automakers have chosen to site nine of the latest 11 major North American plants in Mexico. In 2005, the U.S. produced 73 percent of all light vehicles in North America, Canada produced 16 percent, and Mexico 10 percent. Projections for 2021 indicate that while the overall volume of auto production will increase in North America, the U.S. share will fall to 64 percent, Canada will plummet to 10 percent, and Mexico will more than double to 26 percent.

Steven Rattner seems to agree with the Nafta paradox: “The vast preponderance of American job losses has come simply because emerging-market countries have gotten much better at making stuff with workers earning far less.” The often-unasked question, however, is, why are “workers earning far less”? The implication is that low wages are a part of the natural habitat — they come with the territory — in the way that favorable land and climate might be good for coffee production. In fact, a lack of labor rights fractures the link between rising productivity and wages, which in turn becomes a magnet for investment. Lost in this calculation is not simply the damage to workers and communities, but the larger cost of this strategy: the flipside of low wages is anemic purchasing power, which slows economic growth. In contrast, firms can be highly competitive and, at times, more productive with higher wages — turnover is lower and morale is higher — and the economy benefits. Moreover, low wages in Mexico put a downward pressure on wages in the U.S. and Canada.

Some argue that wages are no longer important in advanced manufacturing. Consider, however, a $1.5 billion investment in highly automated auto factory, which still could employ about 3,000 hourly workers. At $56 compensation per hour — wages and benefits for senior workers in a United Auto Workers (UAW) plant — the annual labor cost would be $336 million dollars in the United States. At $8 compensation per hour in a Mexican plant, the annual labor cost would be just $48 million, and the annual labor-cost savings for the corporation would approach $300 million.

— and median hourly real compensation for workers fell 13 percent, widening a severe long-term gap.

The experience of the last two decades underscores two critical factors: first, a new auto plant in Mexico can achieve quality and productivity comparable to a plant in the U.S. or Canada; and second, wage costs will be low and stay low. In 2013, wages in a state-of-the-art auto assembly plant in Mexico were only 19 percent of U.S. levels, and wages in the parts sector in Mexico were 12 percent of U.S. levels.

### Mexico-U.S. Labor Costs

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Source: Center for Automotive Research; Bureau of Labor Standards.

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American auto plants in Mexico. The country has attracted more than $2.5 billion in new auto investment from 2010 through mid-2016. Eighty percent of the output of these plants — 2.6 million vehicles — was for export in 2014, 71 percent to the U.S. and 11 percent to Canada. Mexico became the world’s fourth largest light vehicle exporter, and General Motors projects that Mexico will become the second-largest global exporter (after Germany) by 2020.

Major automakers from throughout the world are siting new mega-plants in Mexico. They range from the Detroit Three — Ford, GM, and Fiat Chrysler — to luxury brands such as BMW and Mercedes. And it isn’t just subcompact vehicles. These plants already build highly profitable SUVs, such as BMW and Mercedes. And it isn’t just subcompact vehicles. These plants already build highly profitable SUVs, like the Chevy Suburban and the Audi Q5. GM expects to draw their supply base to Mexico.” That country is now the fifth largest auto parts producer in the world, exporting 70 percent of its production, with 90 percent of these exports going to the U.S.

The $2.40 hourly wage in the Mexican auto supplier sector combined with high productivity has resulted in $54 billion auto parts exports to the U.S. in 2015 and a $24 billion sector combined with high productivity has resulted in $54 billion auto parts exports to the U.S. in 2015. Had these jobs been located in the U.S., “another 162,000 jobs in downstream industries (e.g., retail, healthcare, education, real estate, construction) would have been created in the United States,” for a total of 213,000 jobs, according to CAR. If past trends continue, 80 percent of the output from these new plants will be exported, mostly to the U.S.

Rather than questioning the cost of these policies to workers on both sides of the border, some observers view them as the natural outcome of “comparative advantage.” By allowing manufacturers to spread their operations and link up their supplier networks throughout North America, trade facilitates the creation of a system that combines the comparative advantages of each nation, allowing each country to specialize in the aspects of production that it does best and make the overall production process more efficient,” the Wilson Center concludes. “The auto industry, which is probably the single most integrated regional industry, is a perfect example.”

This idealized description may have a Ricardian flavor, but it has little to do with what’s actually taking place. In an intensely competitive global market, the auto industry in both the U.S. and Mexico is highly productive. Should a lack of labor rights then be the basis of comparative advantage? While the increased profitability for firms next quarter or next year is real, is this situation in the long-term interest of most people and healthy economies on either side of the border? Not only will Mexican workers earn less — even far less — than their productivity makes possible but a strong downward pressure is exerted on U.S. wages. Proponents often interject that the consumer will
benefit from lower prices as a result of these arrangements. Not necessarily. The “savings” are more likely to go into increased corporate profits and stratospheric executive salaries; automakers hardly offer a North American “discount” on vehicles produced in Mexico.

Delphi Automotive, among the world’s largest auto suppliers, illustrates the consequences of this kind of comparative advantage. The company, once a wholly owned subsidiary of General Motors, employed about 32,000 unionized hourly workers in the U.S. in 2005. The corporation filed for Chapter 11 bankruptcy that year, ultimately eliminating virtually all its U.S. hourly jobs and threatening or eliminating pensions and health care for its workers. Business Week wrote the company “was careful to exclude Delphi’s 115,000-worker foreign factories, many of which operate in low-wage countries such as Mexico and China.” Today, Delphi is one of Mexico’s largest private employers with 54,000 workers largely producing for the U.S. market, while all UAW hourly jobs in the U.S. have been eliminated. Does it come as any great surprise that manufacturing workers in the U.S. are deeply concerned about trade issues? Again, Delphi gets higher profits, while workers in the U.S. lose, and Mexican workers wind up with a minor fraction of what Delphi gains.

Mexican production cast a shadow over the Detroit UAW auto talks in 2015. Moving “production to Mexico,” according to Bloomberg, “will help the automakers save cash, reduce total payrolls, and offset the union’s gains.” The pressures are even greater in the supplier part of the industry. You might be thinking, doesn’t manufacturing account for only 8–9 percent or so of U.S. employment in any case? The answer is yes, but manufacturing has a high multiplier effect particularly in the auto sector. Each auto job supports six or seven jobs throughout the economy. These job losses and wage pressures go well beyond autoworkers and their families, impacting entire communities, states, and regions. Teachers, nurses, sales clerks, and government workers all see their employment and wages impacted. When plants close, the finances of towns collapse and infrastructure implodes. In the wake of industrial collapse, Flint slid into bankruptcy. A subsequent series of disastrous decisions under a state-appointed emergency manager resulted in the drinking water becoming so contaminated that thousands of children were victims of lead poisoning.

Rules of Origin

Other proposed features of the TPP would have exacerbated job loss across North America. “Rules of origin” stand out. In highly managed trade agreements, these rules determine which products qualify for trade benefits among the trading partners. Defining and calculating these rules are a complex, at times convoluted, process. To qualify for Nafta tariff advantages, rules of origin mandate 62.5 percent of the vehicle be produced in one or more of the three Nafta countries. Rather than raising the rules of origin over the much broader sweep of the 12 TPP countries, the rules were loosened considerably so only 45 percent of vehicle content is necessary for the preferential treatment. These more relaxed rules accommodate the global supply chains of international producers that already source in low-wage countries, say Thailand or China.

 Ironically, 55 percent of a vehicle could be sourced from China without that country agreeing to any TPP provisions, displacing Mexican as well as U.S. and Canadian auto parts workers. Mexico has already seen a major surge of imports from China in a highly unbalanced trade relationship. Mexico’s imports from China have soared from $500 million dollars in 1994 to $70 billion in 2015, but its exports to China have remained anemic. Even under the Nafta “rules of origin,” a higher percentage of exported vehicles from Mexico could well be coming from China.
impressed. He told Congress admiringly in 1993, “Nafta is probably the most one-sided and unbalanced agreement that the United States has ever negotiated.” He then pointed out the agreement spells “out what Mexico must do to join the Canada–U.S. free trade club,” and of course, there were no requirements in relation to labor.

The problem isn’t a new investment in Mexico. Competition based on innovation, productivity, and quality can provide real benefits for workers and consumers, but competition based on low wages and a lack of worker rights is damaging to workers, communities, and consumers in all countries. Mexican workers who share in productivity gains enter the middle class and create the “high velocity purchasing power” capable of fueling a growing, more balanced trading relationship. U.S. workers are also able to share in the gains from competitive, prosperous companies.

Second, effective enforcement of core labor rights — the right to form a union, to bargain collectively, and to strike if necessary — are essential. Congress took important steps in this direction in 2007, which were written into the U.S.–Peru Free Trade Agreement (FTA). Without the preconditions of effective labor reform prior to signing, however, Peru has been able to avoid its commitments since the agreement became operational six years ago. After the Peruvian experience, the U.S. and Colombia agreed on a Labor Action Plan to meet core international labor rights. Colombia also has not met its commitments since this agreement came into effect four years ago. When workers in Peru, Colombia, or Mexico are denied their rights, workers and unions in the U.S. are undermined.

Finally, winners and losers will still exist in global trade, and a far better social safety net is essential. Given the intensity of the political earthquakes trade has triggered, many now agree something must be done. “There are going to be losers,” admits Chad P. Brown, a trade agreement proponent at the Peterson Institute for International Economics in Washington D.C., “and we need to have policies to address them.”

Christine Lagarde, managing director of the IMF, Jim Yong Kim, president of the World Bank Group, and Roberto Azevedo, director-general of the World Trade Organization, wrote in The Wall Street Journal, “Governments can step up investment in education, job training, temporary income support, job-search assistance, and targeted trade-adjustment assistance, using approaches crafted to best fit their national circumstances.” In fact, the U.S. spends less on retraining as a share of GDP than the 34 member countries of the OECD, with the exception of Chile and Mexico.