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Globalization: Threat or Opportunity for the U.S. Economy?

I. Good evening, and thank you for having me here tonight.

A. As a monetary policymaker, my main concern is the health of the U.S. economy.

1. Although the economy turned in a pretty sluggish performance for a long while after the 2001 recession,

a. it has shown some real strength over the last few quarters in terms of

(1) output growth
(2) and productivity.

B. But along the way, the jobs market performance has been surprisingly disappointing—at least, until the last few months.

1. This certainly has been a concern—not only for those who have been looking for work,

a. but also for us at the Fed

b. and for other policymakers around the country.

C. In the discussions about this so-called "jobless recovery," a lot of attention has focused on trade issues.

1. The terms you hear are "globalization," "outsourcing, "offshoring," and the like.

2. The concern, of course, is that a free-trade environment is

a. letting good jobs drain from the U.S. economy

b. and wind up in China, India, and other countries where workers command much lower salaries.

3. And, in the extreme, some would like to see restraints on trade to protect those jobs and halt the globalization trend.

D. Now, the question of whether globalization is a threat or an opportunity for the U.S. economy is a big one, with serious ramifications.

1. In my remarks tonight, I won't be able to cover *all* the issues.

a. But I would like to say a few words to add a little balance to the discussion.

2. Before I turn to that question, I'd like to address a few background questions.

a. First, why are most economists in favor of free trade?

b. Second, what exactly are "outsourcing" and "offshoring"?

3. Then I'll lay out some of the threats and opportunities I see for globalization's impact on the U.S. economy.

4. Finally, I'll say a few words about focusing policy on protecting people, not on protecting jobs.

II. So, why are most economists in favor of free trade?

A. Basically, the argument is that *everyone* benefits when countries specialize in the type of production at which they're relatively most efficient.

B. Let me illustrate with an analogy that's very close to home—the family.

1. No family tries to make everything that it eats, wears, and enjoys.

2. If it's cheaper to buy something or have someone else do something, that's what a family does.

3. That allows individual family members to concentrate on becoming good at their jobs in order to pay for what they buy.

C. A nation isn't any different.

1. If it costs less to make certain products abroad than it does in the U.S.,

    a. then it's difficult to argue that U.S. consumers and U.S. companies should pay more for those products from U.S. producers.

    b. Instead, it makes sense to purchase those products more cheaply from abroad,

        (1) whether they're hard goods, like VCRs,

        (2) or services, like call centers.

2. That lets us devote our resources to producing and exporting those goods where we have a relative advantage.

    a. The result is a twofold benefit—

        (1) —greater efficiency

        (2) —and lower costs for U.S. firms and consumers.

III. Now, what are "outsourcing" and "offshoring"?

A. In its broadest sense, outsourcing is simply contracting out functions that had been done in-house.

B. And outsourcing has been going on a long time in our economy.

1. When a car manufacturer in Michigan chooses to buy brake pads from an intermediate supplier in Ohio rather than produce them in-house, that's outsourcing.

2. When a company replaces its cleaning and cafeteria workers with an outside contractor who provides the same services more cheaply, that's outsourcing.

3. When a company contracts out its payroll, accounting, and software operations, *that's* outsourcing.

4. And outsourcing clearly can result in job losses if the outside supplier is more efficient and uses fewer workers.

C. Now, what about offshoring?

1. Offshoring has been referred to as the global cousin of outsourcing.

    a. Instead of turning to domestic providers, firms may decide to purchase a good or service from overseas providers.

    b. And the reason is the same—lower costs.

2. We've been familiar with the offshoring of a lot of manufacturing for many years.

    a. For example, firms in Mexico are important suppliers of seat covers and wiper blades for Detroit automakers.

3. What appears to be new about offshoring these days is that it's affecting workers in the service sector who never expected to see foreign competition for their jobs—

    a. —data managers, computer programmers, medical transcriptionists, and the like.

D. Now, it would be good to get a handle on just how much offshoring is going on.

1. But that's easier said than done.

    a. We don't have official statistics,

    b. and there are a lot of unsettled measurement issues.

2. But let me refer to a couple of estimates that have gotten some press recently and that seem to be pretty similar.

    a. One is from Goldman-Sachs, and the other is from Forrester Research, a consulting firm.

    b. These estimates indicate that the number of jobs lost to foreign workers between 2000 and 2003 was one hundred to one hundred and seventy thousand.

3. Those numbers sound high.

    a. But they don't sound high when you put them in the context of all the job turnover that occurs every year in the U.S.

(1) Each year, some fifteen million jobs are lost for all kinds of reasons— voluntary employment changes, layoffs, firings, and so on.

(2) And in a growing economy, every year even more jobs are created.

IV. Now let me turn to my main question: Is globalization a threat or an opportunity for the U.S. economy? To answer this, I want to focus on three important issues that I think are sometimes neglected in the discussion.

A. First, it's important to remember that globalization means that economic activity flows in *both* directions.

1. So, although we may lose jobs to foreign workers, we also may gain jobs and boost economic activity.

2. For example, the data suggest that, in terms of office work, the U.S. *insources* far more than it *outsources.*

a. That is, just as U.S. firms use the services of foreigners, foreign firms make even greater use of the services of U.S. residents.

(1) Here I'm referring specifically to the category of business, professional, and technical services.

(2) This includes computer programming, telecommunications, legal services, banking, engineering, management consulting, and other private services.

(3) It also encompasses U.S. outsourcing of call centers and data entry to developing nations, among other things.

b. In 2003, we bought about seventy-seven billion dollars' worth of those services from foreigners.

c. But the value of the services we *sold* to foreigners was far higher, over one hundred and thirty billion dollars.

3. Here's another set of interesting numbers.

a. Between 1991 and 2001, U.S.-based multinationals created close to three million jobs overseas.

b. But they also created five and a half million jobs inside the U.S. ─an increase of about thirty percent in payrolls.

c. That's a significantly faster rate of job growth than purely domestic companies generated.

d. So, this is an instance that shows you can't assume that a job created overseas necessarily means one isn't created here.

(1) For example, expanding an overseas network frequently means you have to hire more workers in the U.S., too─

(a) ─people in management, logistics, research and development, and international IT.

4. Here's a final set of numbers.

a. According to the Commerce Department, even as the U.S. "loses" jobs when our companies send operations offshore, we also "gain" jobs as foreign corporations invest here.

(1) Specifically, foreign firms employed almost six and a half million workers in the U.S. in 2001─up from about five million in 1991.

(a) These workers included highly paid Honda and Mercedes-Benz workers in the auto industry.

(b) And in 2006, Toyota is going to employ two thousand people building cars in San Antonio.

b. And there are plenty of similar examples.

(1) Samsung is investing $500 million to expand its semiconductor plant in Texas.

(2) And Novartis is moving its R&D operation from Switzerland to Massachusetts.

B. Another key point to recognize in the globalization debate is that open trade creates opportunities in the U.S by helping foreign economies become stronger.

1. As foreign incomes grow, the demand for U.S. exports expands as well.

2. And that provides even more opportunities for high-paying jobs in this country.

C. Finally, globalization can help increase productivity growth in the U.S..

1. Let me illustrate with a brief look at how offshoring has affected the spread of IT in the U.S. and, therefore, our economic growth.

a. According to Catherine Mann at the Institute for International Economics, globalized production of IT hardware—that is, the offshoring of computer-related manufacturing, such as Dell computer factories in China—reduced the prices of computer and telecommunications equipment by ten to thirty percent.

b. These price declines boosted the spread of IT throughout the U.S. economy and raised both productivity and growth.

2. Offshoring offers the potential to lower the prices of IT software and services prices as well.

a. This will promote the further spread of IT—and of new business processes that take advantage of cheap IT.

b. It also will create jobs for U.S. workers to design and implement IT packages for a range of industries and companies.

3. Although some jobs are at risk,

a. the same trends that make offshoring possible are creating new opportunities—and new jobs— throughout the U.S. economy.

b. For example, a McKinsey Global Institute study finds that

(1) for every dollar of activity outsourced to India,

(2) the U.S. receives between $1.12 and $1.14 in economic benefits.

V. Now, I've mentioned productivity several times so far, and I want to take a few minutes to focus on this subject, because I think it deserves to play a significant role in the discussion about the so-called jobless recovery.

A. Over the past two years, U.S. productivity in the nonfarm business sector has grown at a 4.8 percent annual rate.

1. In the short term, this increased productivity has let businesses satisfy the demand for their output without having to hire new workers on net.

2. So, it appears that this extraordinary surge of increased efficiency in our economy explains much more about the jobless recovery than offshoring, outsourcing, or globalization does.

B. Although, clearly, productivity creates pain for workers who are displaced, most economists agree that higher productivity is a good thing for the economy.

1. Why? Because, in the long run, higher productivity is the only way to create higher standards of living across the economy.

C. The ongoing ability of the American worker to produce more goods and services per hour has been the key to the U.S. economy's surprising success throughout its history.

1. Clearly, in the manufacturing and agricultural sectors, more output can now be produced with fewer workers.

2. The same trend has occurred in services.

a. The U.S. used to have lots of elevator operators, telephone operators, bank tellers, and gas station attendants.

b. But now technological advances have taken over many of these jobs.

c. Likewise, the Internet has taken over many routine tasks from travel agents, stock brokers, and accountants.

d. And, with high speed data links, a lot of office work can be done more cheaply abroad.

D. What happens to the displaced workers?

1. They move into other sectors of the economy, as new jobs emerge.

a. For example, by one estimate, about a quarter of today's labor force is in jobs that didn't even exist in 1967.

E. This emergence of new jobs and workers' ability to move into them are the hallmarks of a flexible economy—

1. that is, an economy in which labor and capital resources move freely among firms and industries.

2. And such flexibility is a significant strength of the U.S. economy.

    a. We operate in competitive markets,

    b. and competition, whether from domestic or foreign competitors, induces change.

3. To adapt to that change, and to ease the burden of adjusting to it, flexible labor and capital markets are critically important.

VI. Now let me wrap up with a few words on what policy can do to help U.S. workers.

A. In terms of the overall economy,

1. appropriate monetary and fiscal policies can ensure that aggregate demand

    a. keeps the economy on a sound footing

    b. which helps generate jobs to replace those that have been lost.

B. But words about aggregate demand can seem like cold comfort to the individual workers whose offices and plants are closing because their jobs are going overseas.

1. And concern for these workers, of course, is why there's interest in trying to restrict trade by imposing tariffs, quotas, or other barriers.

    a. Indeed, such measures may actually succeed in slowing job losses in affected industries temporarily.

C. But, as I hope I've illustrated, in the end, they impose significant costs on the rest of the economy—

1. —costs that are much higher than any benefits.

D. That's why, as I said at the outset, I think it's far more appropriate to have policies that focus on protecting the *people* at risk, not the jobs.

1. Such policies ought to aim to do two things during difficult transitions:

    a. help workers get through the hard times,

b. and help workers become more flexible so they can adapt when they do face these kinds of changes.

2. In fact, there already are policies like this in place—

a. unemployment insurance, for example.

3. And there are even policies specifically for manufacturing workers who have lost jobs to foreign competition.

a. These trade-adjustment assistance programs offer

(1) both financial support for a time

(2) and the opportunity for training, so that workers can retool their skills and find new jobs.

4. So, in order to help the *service* workers who have lost their jobs because of outsourcing, it might be appropriate to extend these programs to them.

5. Now, I know there's some debate about how effective the programs are,

a. but the concepts they're built on are, to my mind, right on target—

(1) providing a safety net for workers

(2) and providing them with the training and tools to qualify for the jobs being created in the U.S.

b. In fact, such programs could be appropriate

(1) not only for workers who have lost jobs to outsourcing,

(2) but also to workers who have lost jobs in the wake of the technology-driven productivity surge.

E. In the long-run, of course, the solution is simple to state, but difficult—and costly—to implement.

1. And that solution is improving the performance of the U.S. education system.

a. Education is the bedrock of our current edge in technology and productivity.

b. It's the key to producing workers with the flexibility to learn new skills as market conditions evolve.

c. And it's the hope and promise we must provide for future generations of Americans.

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