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► THE LIMITS OF GLOBALIZATION: UNDERSTANDING THE RISE OF DONALD TRUMP

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June 2016

The rise of Donald Trump to the top of the United States Republican Party is not as incredible as establishment pundits profess. In fact, he is the voice for an increasing number of Americans, who count themselves amongst the biggest losers of globalization and free trade. Each election, the gap widens between the winners and losers of globalization and free trade. And each election year, U.S. politicians express concern about their issues, then conveniently ignore them when they reach power and implement policies from the same Washington Consensus that has dominated the past 40 years. In Trump, the electorate has somebody playing a very different game, even if his policies lack the coherence and elegance so beloved in the world of economic policy seminars and think tanks.

In the post-Cold War era, the dominant force in the development of the world economy has been globalization. The single biggest factor was China's entry into the World Trade Organization. In the process, distance evaporated as a concept. Businesses moved to China, India, Latin America, and other emerging markets in search of cheaper places and means to produce goods and services for Western economies. As a result, several hundred million people in underdeveloped economies were lifted into urbanization from centuries of debilitating rural poverty.

But, globalization also created losers. Revolutionary technological

advances enabled an unprecedented outsourcing by American companies seeking to maximize profits by employment of low-cost foreign labor. The scale of the outsourcing was made possible because of advances in technology, global trade treaties and capital-account liberalization. For all of the vaunted gains in profitability, it is unclear that globalization has been the huge win-win, as its apologists argue. Internationally, the richest five percent of people receive one-third of total global income, as much as the poorest 80 percent.¹

In the U.S., workers have been replaced by low-cost foreign workers. As a result, for more than 25 years a huge number of Americans have experienced stagnant wages and incomes, with trade agreements exacerbating the problem.

Trump has taken this one stage further with his hardline stance on immigration. For all the media attention devoted to walls along the Mexican border, or an outright ban on Muslim immigration, there is method to Trump's madness which goes well beyond racism. By linking immigration and trade, however crudely, Trump has exposed the paradox and inherent contradictions which lurk between the two.

Historically, immigration law in the U.S. and Canada has concerned itself with many considerations, key being the displacement of domestic workers. By contrast, advocates of free trade ignore this

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consideration, or blithely suggest that the resultant unemployment in a displaced sector (e.g., the automobile industry), is a “negative externality”, offset by the resultant gains in competitive efficiency, and lower-cost goods. Cheap imports, then, outweigh the displacement of workers.

But we do not extend this logic to immigration, or we would move straight to a policy of open borders. The reason we do not have open borders is because it would substantially drive down the wages of American workers. Low costs for traded goods are okay; low-cost labour, not so good, at least that is implicit in the application of current immigration policy.

Businesses have sought to evade this inconvenient immigration restriction via offshoring manufacturing facilities, resulting in the displacement of workers by low-cost foreign labor. The economic impact subverts the policy goal behind American immigration policy. In many respects, it mirrors the impact of a hypothetical open-borders policy, in effect creating “synthetic immigration”, which reduces employment and lowers wages as investment is increasingly outsourced abroad.

Globalization advocates argue profits to U.S. corporations spur re-investment, which in turn creates employment. In reality, the profits do not go toward domestic re-investment (and, hence, more jobs), but to increasing investment abroad. That is, when they are not using corporate cash to buy back stock and inflate share prices and CEO executive compensation.

To offset the economic drag outsourcing and synthetic immigration impose, policy makers have been pursuing a program of Quantitative Easing (QE) in unprecedented amounts, both absolutely and relative to GDP. Designed to stimulate consumption and ultimately investment by pumping up housing and stock markets, it has resulted instead in a weak real economy, persistently high underemployment and non-existent wage growth.

In regards to free trade, tens of thousands of automobile workers in Michigan and Ontario are displaced because we attach primacy to buying the cheapest cars available. The theory is that the savings will generate sufficient demand elsewhere to offset the impact of displaced workers. The implicit policy assumption is that this “good” outweighs all other considerations, even though the relative consumption problem that occurs as one person buys the lower-cost good creates a consumption equivalent to Keynes’s “paradox of thrift” – insofar as consumers fail to realize that if they all do it, then many more of them ultimately end up unemployed or underemployed.”

Consider a thought experiment: imagine a country with one worker who is also the sole consumer. The worker would understand that by consuming foreign-made goods produced by the synthetic immigrant, he would soon have no income and, as a consequence, no consumption. In the real world, people want to maximize their welfare and do so by maximizing current consumption, which is said to be one of the benefits underlying free trade. Maximizing current consumption means purchasing the lowest-priced goods at any particular level of quality.

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This behaviour cascades as in the short-run the increased standard of living offered by low-cost goods swamps the longer-term effects of chronic job losses. The paradox of consumption is that a rational person in a one-person world would never behave in the same way as many rational utility-maximizing individuals behave.

Prior to the post-Cold War period of globalization, this was not a problem because displacement by immigrants generally began at the most menial level of the labour force, and policy changes adopted in the aftermath of each successive immigration wave (at least until 1965) generally prevented massive amounts of displacement and consequently stopped the migration of jobs at the menial labor level.

The ethics debate regarding immigration is similar to that regarding trade. Should policy be constructed with respect to domestic or global welfare? For the most part, it seems as if domestic concerns dominated immigration policy; whereas trade policy, haunted by misconceptions regarding the Smoot-Hawley Tariff of the 1930’s, is generally obsessed with global considerations. Today, false ideas about great prospects for exporting into the enormous Chinese market hinder national policy and enable employee displacement. Because of technological advances, today’s trade policies are effectively an immigration policy.

There are differences to be sure, but those differences work to the

detriment of American and Canadian workers. Typically low-cost labour attracted long-lived capital investment. Today, synthetic immigration via global outsourcing leads to capital investment in the immigrant's country (China) resulting in a greater capital stock there and increased competitiveness.

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It is, and always has been, the government's duty to provide for and protect its citizens. Protection of U.S. workers from synthetic immigrants is long overdue and the cost of government neglect is huge. Immigration policies differ everywhere and change as the government's responsibility to its citizens is enforced. And yet we never apply the same principles that underlie our immigration policy for trade. At least until now, where it has become a major feature of the Trump campaign. For Canada, with its economy so closely integrated with the U.S., the rise of similar populist sentiment is not unlikely.

So what is the right policy response? There has been a backlash against trade agreements, such as the recently signed Trans-Pacific Partnership. As Thomas Frank has recently noted:

Trade is an issue that polarizes Americans by socio-economic status. To the professional class, which encompasses the vast majority of our media figures, economists, Washington officials and Democratic powerbrokers, what they call "free trade" is something so obviously good and noble it doesn't require explanation or inquiry or even thought. Republican and Democratic leaders alike agree on this, and no amount of facts can move them from their Econ 101 dream.

To the remaining 80 or 90 per cent of America, trade means something very different. There's a video going around on the internet these days that shows a room full of workers at a Carrier air conditioning plant in Indiana being told by an officer of the company that the factory is being moved to Monterrey, Mexico, and that they're all going to lose their jobs.²

Trump uses this video in his campaign. As Frank notes, "Trump is making a point of assailing that Indiana air conditioning company from the video in his speeches. What this suggests is that he's telling a tale as much about economic outrage as it is tale of racism on the march." Granted, the reaction against immigrants may well appeal to racists, but it also overlaps with economic concerns of people displaced by decades of trade and immigration liberalization, both real and "synthetic".

As globalization has intensified, companies have increasingly competed with each other. Those with substantial low-cost advantages have generally prevailed, eliminating competitors which sought to preserve well-paying American jobs. Therein lays the paradox of outsourcing. It is the responsibility of government to construct

policies that stop, or least restrict, the cascading of outsourcing because of its adverse impact on employment and the negative incentives outsourcing imposes on domestic investment.

We have historically considered these factors in our immigration policy. Why is trade so sacrosanct? Trump is the candidate who has been most persistent, however crudely and coarsely, in asking these questions.

But are his policies the right ones?

Whether right or wrong, policy makers in the U.S. must address the problems Trump highlights. A new set of policies is required to create a greater growth dynamic for those left behind as globalization, trade and immigration have liberalized. The objective of these policies should be to improve the real economy, which will require an investment in new capital stock and human capital, not foster increased stock market speculation or resort to other forms of financial bubbles.

One possibility to address the unemployment/underemployment problem is a federally funded U.S. Job Guarantee (JG) program. The federal government would ensure a job offer to anyone ready and willing to work, at the established program compensation level, including wages and benefits package. To make matters simple, the program wage could be set at the minimum wage level, and then adjusted periodically as the minimum wage is raised.

Proponents of a universal job guarantee program operated by the federal government argue that no other means exists to ensure everyone who wants to work will be able to obtain a job. Benefits include poverty reduction, amelioration of many social ills associated with chronic unemployment (health problems, spousal abuse and family break-up, drug abuse, crime), and enhanced skills due to training on the job.

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We do not imagine that determining the level of compensation will be easy; however, a public debate that brings into the open matters concerning the minimum living standard the U.S. should provide to its workers is not only necessary, but healthy. And the question of the minimum wage has become a major topic of conversation amongst all of the remaining Presidential candidates, especially as immigration has acted as a wage depressant.

The federal government would not have to micromanage such a program. It would provide the funding for direct job creation, but most of the jobs could be created by state and local government and not-for-profit organizations. There are several reasons for this,

but the most important is that local communities have a better understanding of needs. The New Deal of the 1930s was more centralized, but many of the projects were designed to bring development to rural America: electrification, irrigation, and large construction projects. To be sure, we need infrastructure spending today, but much of that can be undertaken by state and local governments. This program would provide at least some of the labour for these projects, with wages and some materials costs paid by the federal government.

More importantly, today we face a severe shortage of public services that could be substantially relieved through employment. Examples include elder care and childcare, non-hazardous environmental clean-up, caring for public space, and low-tech improvement of energy efficiency of low-income residences. Decentralization promotes targeting of projects to meet community needs -- both in terms of the kinds of programs created but also in matching new jobs to the skills of unemployed people in those communities. Also, by creating millions of decentralized public service jobs, we avoid one of the major criticisms of the stimulus package: because there were not enough "on the shelf" infrastructure-type projects, it is taking a long time to create jobs. Instead, we should allow every community service organization to add paid jobs so that they can quickly expand current operations.

As the economy begins to recover, the private and public sectors will begin to hire again, drawing workers out of the program. That is a good thing; indeed, one of the major purposes of this program is to keep people working so that a pool of employable labor will be available when a downturn comes to an end. Further, the program should do what it can to upgrade the skills and training of participants, and it will provide a work history for each participant to use to obtain better and higher-paying work.

In regards to the areas of trade and immigration, Trump has raised the legitimate issue of corporate outsourcing, which produces creeping synthetic immigration and, in turn, domestic unemployment. Since unemployment is the source of the extended pay benefits provided by the government, the government should

permanently tax the source of the unemployment—U.S. corporations producing abroad. Doing so will help restore a permanent incentive to invest in plant and equipment in the U.S.

Furthermore, today's robust corporate profits are the result of expense reductions, most notably lower interest expense stemming from the Fed's massive asset purchases and FDIC guarantees of commercial bank borrowing. The argument for these subsidies is that corporations would reinvest the profits and hire more people, but this assumption has proven false. The government should therefore place an excess profits tax on all corporations that issued term debt subsequent to the initiation of FDIC guaranteed programs. By so doing, revenues can be re-directed toward employment-oriented policies, such as infrastructure improvements, as well as refunding the FDIC, where reserves were depleted in the aftermath of the 2008/09 financial crisis.

The lack of detail and policy coherence in the Trump campaign suggests that Trump does not have the answers to the current economic malaise. But he does understand that there must be change and it must be navigated to everyone's benefit, not just the elites who have profited from the globalized free trade environment that has created as many losers as winners, a fact most economists have steadfastly refused to acknowledge.

NOTES

1. According to research by Professor Branko Milanovic, a visiting presidential professor at CUNY's Graduate Center and a senior scholar at the Luxembourg Income Study Center
2. <http://www.theguardian.com/commentisfree/2016/mar/07/donald-trump-why-americans-support>



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ISSN 2369-0224 (Print)
ISSN 2369-0232 (Online)

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