THE NEW CENTER

Policy Paper

Think Centered

Making Trade Work for All

AN ECONOMIC AGENDA FOR THE 21ST CENTURY

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ABOUT THE NEW CENTER

American politics is broken, with the far left and far right making it increasingly impossible to govern. This will not change until a viable center emerges that can create an agenda that appeals to the vast majority of the American people. This is the mission of The New Center, which aims to establish the intellectual basis for a viable political center in today's America.

THE NEW CENTER

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Executive Summary

NEW CENTER SOLUTION:

Making Trade Work for All

Economists struggle to agree on much of anything, but one thing they all seem to agree on is the benefit of trade.

The expansion of free trade between 1950 and 2016 increased the size of the U.S. economy by $2.1 trillion, which is equivalent to an $18,000 increase in the income of every American household each year.[1]

Yet if you listen to President Donald Trump or leading Democratic presidential candidates Elizabeth Warren and Bernie Sanders, you might assume trade is a loser for America. In the leadup to the 2016 presidential election, Trump criticized supporters of free trade for having "aggressively pursued a policy of globalization, [which moved] our jobs, our wealth and our factories to Mexico and overseas."[2]

Similarly, Elizabeth Warren, in an October 2019 debate, argued that Ohio "had a lot of problems with losing jobs, but the principal reason has been bad trade policy," rather than disruption caused by automation.[3] While both politicians suggest using different tools—Trump likes tariffs and Warren wants more inclusive trade deals—the core proposition seems to be that trade makes America worse off.

This simply isn't true. Free trade's benefits far outweigh its costs. The challenge is to ensure its benefits are more evenly distributed.

Although you wouldn't know it from the campaign trail rhetoric, 64% of Americans support free trade.[4] But the benefits and downsides of trade are not shared equally, and many communities that have been harmed are in the industrial swing states likely to decide the outcome of the 2020 election.

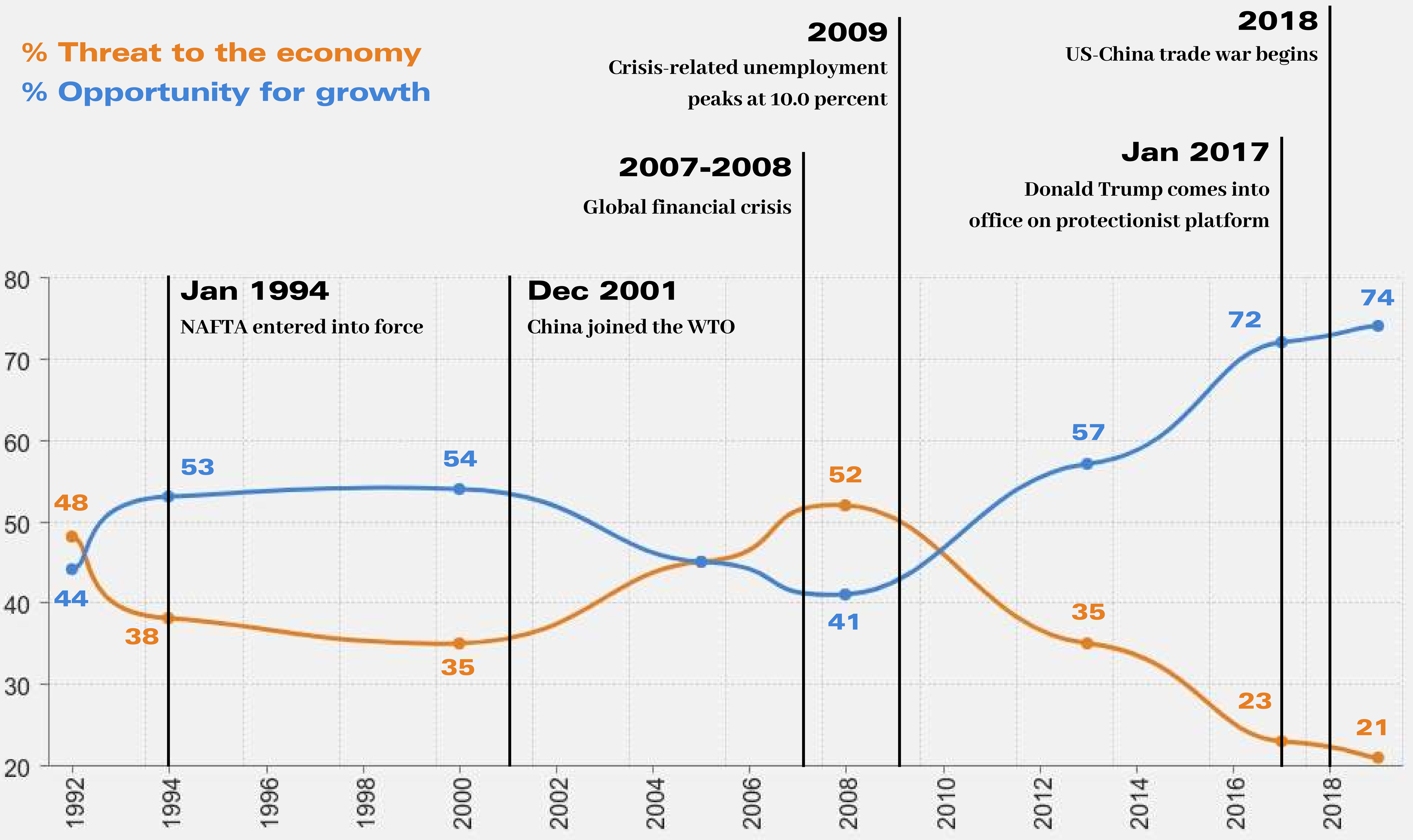
The next president needs to embrace trade, but with a more comprehensive plan that ensures the benefits are shared broadly and equitably across America. This policy paper will provide some ideas on how to get there.

Public Support for Free Trade

- Support for free trade in the U.S. hit an all-time high of 64% according to an August 2019 Wall Street Journal poll, a 7% increase since 2017.[5]
- A 2018 poll conducted by the Chicago Council on Global Affairs found that 67% of Americans believe trade is good for job creation.[6]
- A Gallup poll conducted in March 2019 found that 70% of Americans see foreign trade as an opportunity for economic growth, including 79% of Democrats and 70% of Republicans.[7]

WHAT DO AMERICANS THINK OF FOREIGN TRADE?

Percent of Americans who see foreign trade as a...



Source: Gallup, Bureau of Labor Statistics

The Problem

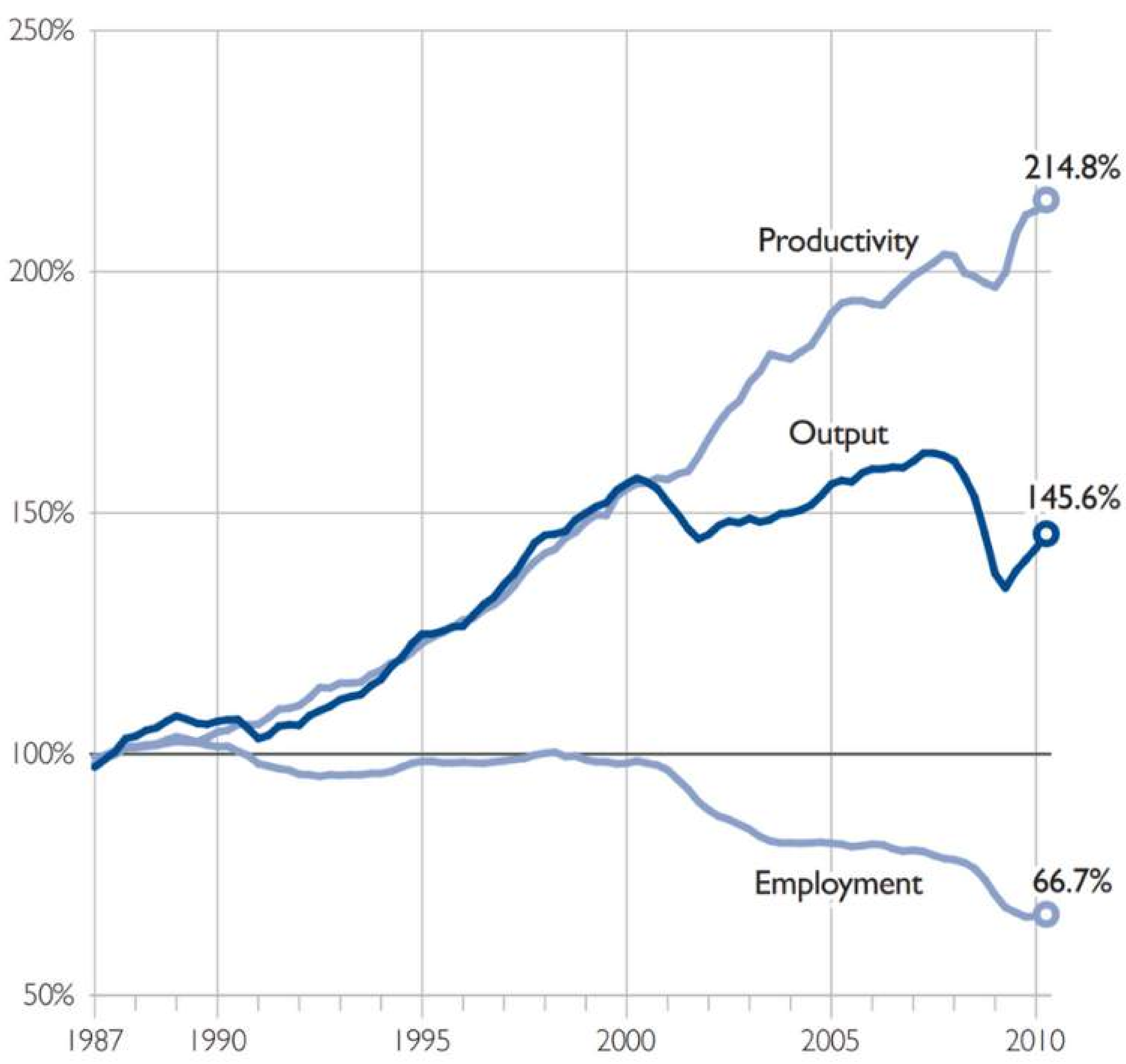
The Decline of Manufacturing Jobs

Manufacturing employment in the U.S. has declined by over 25% since 2000, and some Americans and political leaders hold trade responsible.[8] In reality, manufacturing output is increasing, and job losses in the manufacturing sector might be more attributable to new technology than they are to trade.

According to a study by the Center for Business and Economic Research at Ball State University, 85% of manufacturing jobs lost since 2000 are attributable to technological change like automation.[9]

U.S. Manufacturing Productivity and Output Have Risen While Employment Has Declined

1987=100%



Source: Heritage Foundation and U.S. Department of Labor, Bureau of Labor Statistics, "Productivity and Costs: Manufacturing Sector," 1987-2010, in Data Link Express, Haver Analytics.

U.S. manufacturing real output increased nearly fivefold from 1960 to 2015, even though the number of manufacturing workers in 2015 was nearly 3 million fewer than in 1960.

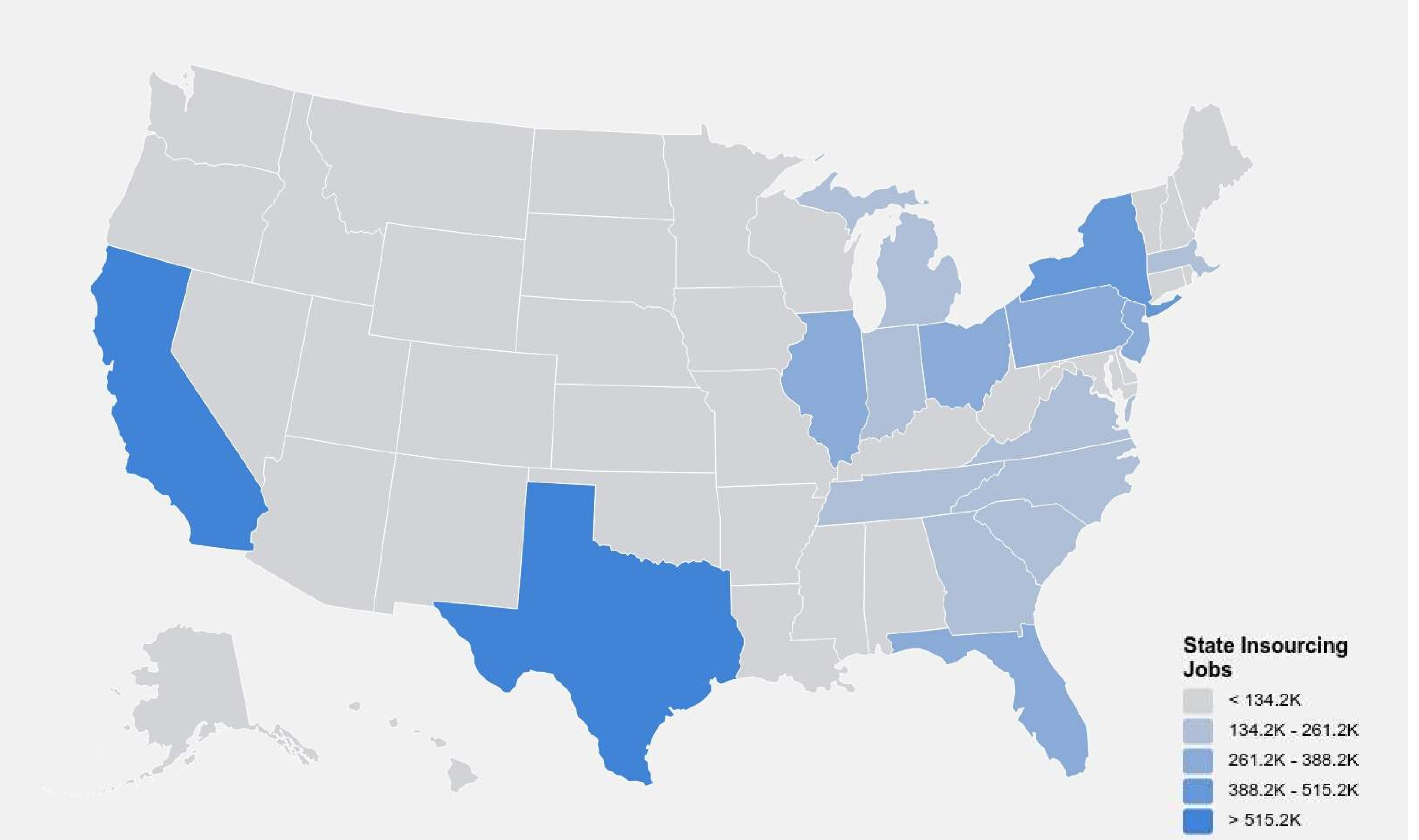
This increase in productivity is the main reason for the declining share of manufacturing employment.[10]

Outsourcing Jobs

A major source of outrage related to trade policy, and one of the most apparent consequences of free trade, is directed at the process of "outsourcing" jobs. As the economy opens itself up to international trade, countries that provide cheaper labor incentivize American companies to relocate businesses and jobs abroad in order to cut costs and increase profits. Ross Perot, an independent candidate in the 1992 presidential election, famously described that the passage of the North America Free Trade Agreement would result in the "giant sucking sound of jobs leaving the country." But jobs don't just go in one direction. While U.S. companies outsource jobs to access global markets and increase profits, foreign companies do the same in the U.S through a process of "insourcing" jobs.

According to data from the Bureau of Economic Analysis, foreign companies employed more than 7.1 million American workers in 2016.[11] That represented 5.6% of all U.S. private-sector employment that year, and contributed more than $910 billion to U.S. GDP.[12]

Americans Employed by Foreign Companies (2016)



Source: Bureau of Economic Analysis

The number of jobs created by foreign companies has been steadily growing since 2009, and they continue to make up a greater share of total private sector employment.[13] Additionally, these jobs provided an average annual compensation of $80,028, which was nearly double the average salary in the U.S. in 2016.[14]

Even though U.S. companies send jobs abroad, their increased competitiveness and profitability allows them to create new jobs in America. A study from the London School of Economics Center for Economic Performance found that the overall impact of offshoring on employment is neutral. Since offshoring tends to increase productivity and reduce costs, companies can expand domestic hiring enough to offset the jobs lost to workers overseas.[15]

Adjustment to Trade

Free trade advocates have long understood that there would be disruption. President John F. Kennedy, in introducing the Trade Expansion Act of 1962, said that "when consideration of national policy make it desirable to avoid higher tariffs, those injured by that competition should not be required to bear the full brunt of the impact." His 1962 legislation created a program of "trade adjustment assistance" (TAA), which provided tax breaks, technical assistance, loans, and new investment to industries and communities hurt by import competition while also providing income assistance and retraining for affected workers.

Kennedy described it as "a program to afford time for American initiative, American adaptability, and American resiliency to assert themselves" and "to strengthen the efficiency of our economy."

But TAA has never quite delivered as promised and, over its life, the TAA program has benefited fewer than one-tenth of the workers potentially eligible for the assistance.[16]

Fred Bergsten, former assistant for international economic affairs to Henry Kissinger, wrote in 1973 that the nation had only two choices in confronting the disruption caused by rising import competition:

"To limit the imports themselves, or to help the dislocated workers and firms adjust to the new competition." Unfortunately, the United States made a third choice: it remained open to imports and did little to aid those harmed by the new competition.

Instead of using government money to put people back to work through proper funding of the TAA, the federal government pays people to stay out of the workforce by focusing on unemployment benefits at a huge cost to the overall economy.[17] In 2018, the U.S. paid $27.5 billion in total unemployment benefits and $144 billion in Social Security Disability benefits, with at least some of this going to displaced workers who would likely be better served by more robust forms of trade assistance that let them regain a toehold in the workforce.[18]

Answers from Across the Aisle

ANSWERS FROM THE RIGHT

President Trump has advocated for an “America First” trade agenda with tariffs as his primary policy tool. Although Trump is responding to serious concerns that have been shared by previous presidents—ranging from theft of American intellectual property to countries unfairly subsidizing their state industries—the cost of tariffs on U.S. businesses and workers has been significant.

For example, Caterpillar, the world’s largest maker of construction and mining equipment, reported that its 2019 earnings outlook would need to be lowered “due to uncertainty in the global economy resulting from trade tensions.”[19] Similarly, American toy-maker Hasbro saw its stock plummet 17% in late October after the company announced reduced revenues due to “the threat and enactment of tariffs.”[20]

According to IMF research, the cumulative economic loss from the trade war could amount to $700 billion by 2020, or about 0.8% of global gross domestic product.[21]

In an analysis written for the National Bureau of Economic Research, economists found that the impact of the Trump administration’s use of tariffs in 2018 reduced the real income of American consumers by $1.4 billion per month, equivalent to a $424 cost every month per person in the United States.[22]

President Trump has in recent months struck important new trade deals with some of our biggest trade partners including the U.S.-Mexico-Canada-Agreement (USMCA) and the Phase One Trade Deal with China. While moving in the right direction, the Phase One Trade Deal still leaves in place tariffs on $370 billion worth of Chinese goods, and the only enforcement mechanism to ensure compliance with the deal is the implementation of more unilateral tariffs on China.[23] On the other hand, the USMCA is practically identical to the North America Free Trade Agreement (NAFTA), a trade deal that President Trump once called "the worst trade deal ever signed".[24] The Trump administration is still far away from a trade agenda that best supports the American economy.

ANSWERS FROM THE LEFT

Leading Democratic presidential contenders like Bernie Sanders and Elizabeth Warren say they will protect American jobs and businesses with better trade deals rather than tariffs. Elizabeth Warren’s trade policy proposal would require nine separate criteria to be met before a trade deal can be negotiated with the U.S., which include upholding certain labor rights, human rights, and undertaking efforts to end climate change.[25] These requirements would also apply to any existing trade deals, which Warren would renegotiate as president. However, the United States itself does not meet many of these criteria now, and neither do many of its largest trading partners.[26]

The upshot could be fewer trade deals, less trade, and ironically, less progress toward the goals Warren cares about as countries would be unfettered by fewer binding trade agreements.[27]

The Dangers of Trade Protectionism: A Case Study of the Smoot-Hawley Act

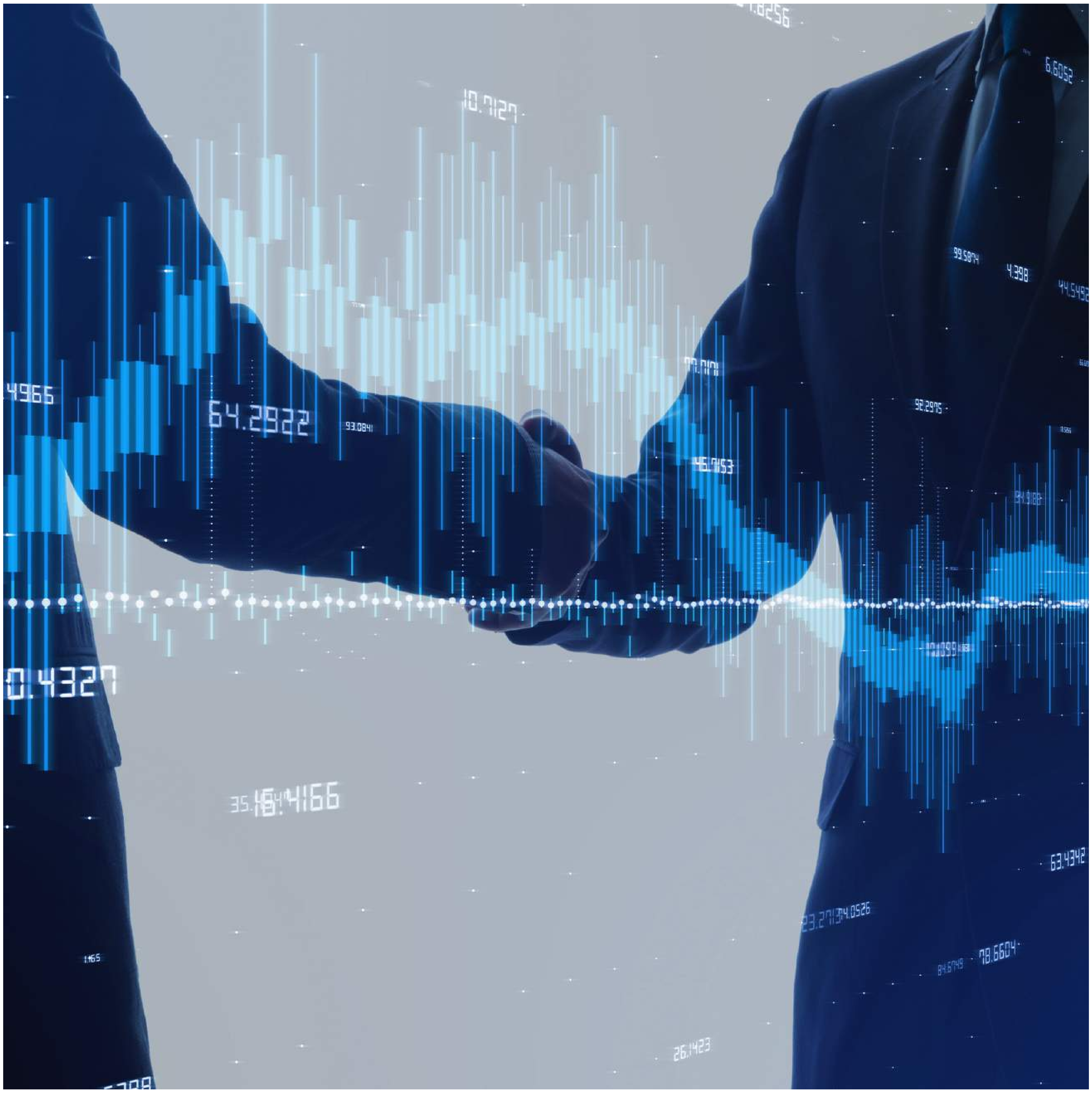
The Smoot-Hawley Act, or the Tariff Act of 1930, increased 900 import tariffs by an average of 40% to 48%. In June 1930, Smoot-Hawley raised U.S. tariffs on foreign agricultural imports to support U.S. farmers harmed by the Great Depression. This inadvertently increased food prices since the previously cheaper imported food was made more expensive as a result of the tariffs. It also compelled other countries to retaliate with their own tariffs. Canada, Europe, and other nations swiftly retaliated by raising tariffs on U.S. exports. As a result, exports fell from $7 billion in 1929 to $2.5 billion in 1932.

Farm exports fell to a third of their 1929 level by 1933. Global trade declined by 65% by 1933.[28]

Just as the stock market had begun to recover from the crash of 1929, the passage of the Smoot-Hawley Act led to even more financial turmoil. In the two weeks leading up to the bill being signed into law, the Dow Jones Industrial Average fell 23%.[29]

Because the tariffs were fixed, the dutiable percentage of products grew as their value collapsed. The less trade there was, the more difficult it became. Rather than the promised new era of prosperity, Smoot-Hawley helped bring about an era of misery.

Between 1929 and 1933, America's wealth nearly halved—while the unemployment rate more than tripled from 8% to 25%.[30]



The Solutions

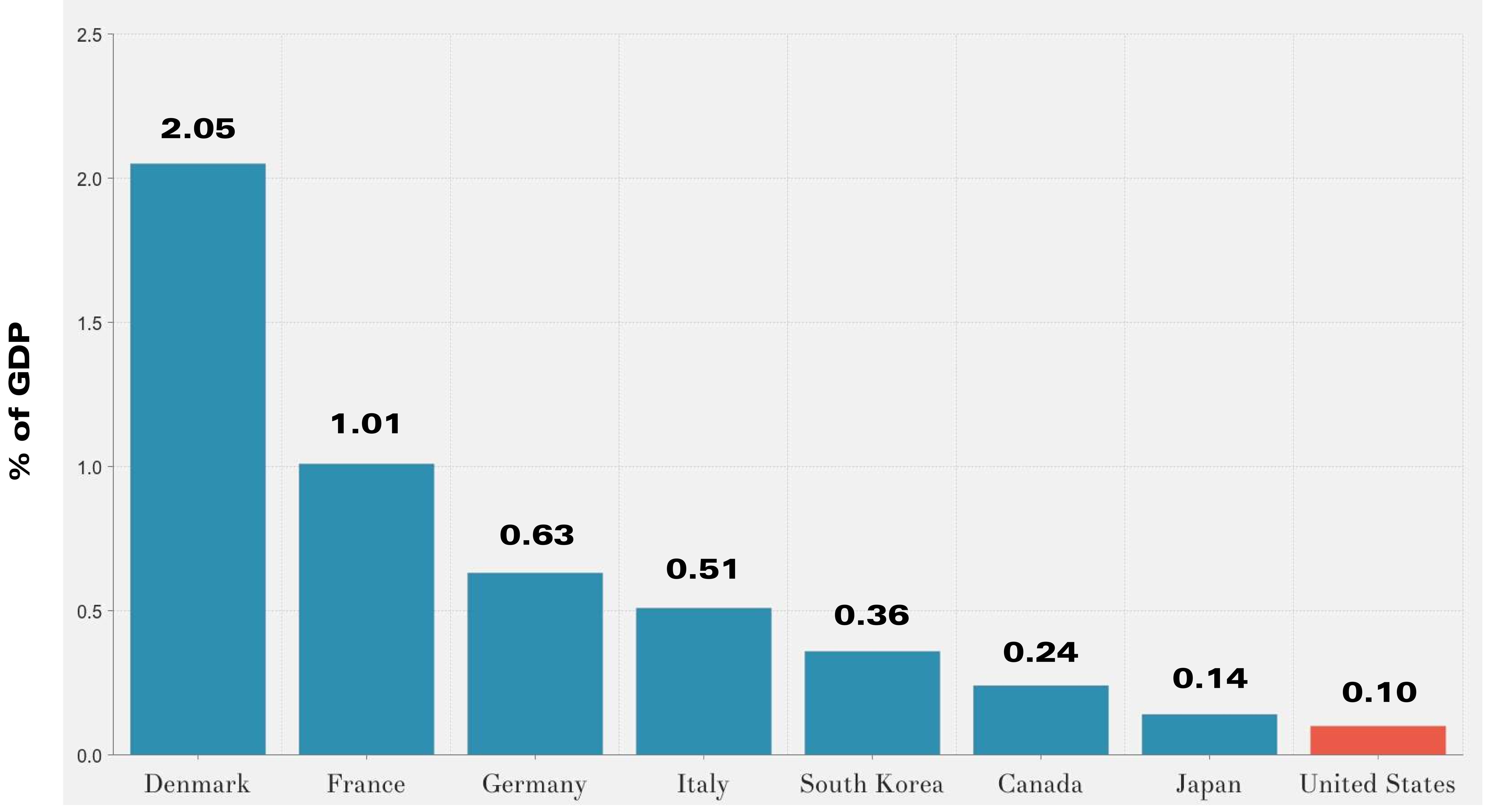
A New Trade Adjustment Assistance (TAA) Program

The current TAA program is underfunded, narrow in scope, poorly managed, and only reactive in helping American workers. We need a new Trade Adjustment Assistance Program that is more ambitious and truly makes trade work for all Americans. Here are some of the steps to create such a program.

1. INCREASE FUNDING

According to the OECD Employment Outlook 2016, the U.S. spends about 0.1% of GDP on programs that actively encourage labor force participation, the lowest of any OECD country besides Mexico and Chile.[31] With arguably the most volatile labor market in the OECD, the United States spends the least on programs supporting displaced workers. The federal government should expand the budget of TAA to help close this gap by spending at least 0.5% of GDP (the average of the OECD) on active labor market programs.[32]

Public Expenditure (% of GDP) on active labour-market programmes (2015)



Source: Organisation for Economic Cooperation and Development (2017).

2. WIDEN ELIGIBILITY FOR ASSISTANCE

TAA benefits have mostly been made available to workers who met a narrow interpretation of suffering a "serious injury" (generally meaning job loss caused by a rise in import competition), which is too narrow to adequately account for workers in need of assistance. Widening eligibility for TAA benefits could help provide more training and support to American workers who are transitioning to new jobs.[33]

3. PARTNER TAA WITH REGION-FOCUSED INITIATIVES AND GOVERNMENT PROGRAMS

Trade isn't the only issue responsible for disruption and job loss, but many shocks repeatedly affect the same region or area. By improving coordination with other government programs such as Job Corps and Temporary Assistance for Needy Families (TANF), a new TAA program could provide a more comprehensive solution to supporting areas like the Rust Belt that have already been impacted by trade or have faced other shocks like the adoption of new technology. Workers unaffected by trade can still lose out due to the rippling effects of a neighbor's job being outsourced. Therefore, local government needs to engage a broad range of stakeholders, service providers, and government programs to improve economic outcomes for regions most affected by disruption.

4. PROACTIVELY DEAL WITH WORKFORCE DISRUPTION

The current TAA program only provides help after a plant has been closed or workers have been laid off. Programs should be anticipatory and offer support when disruption is forecast but not yet hitting home. The federal government could use regional income inequality and regional economic diversification to measure the economic resilience (the ability to avoid, withstand, and recover from an economic shock) of a community and target support to those regions that are the least resilient.[34] Proactive efforts will maximize the opportunities for successful adjustment, whether by permitting worker retraining and job search prior to a crisis or by supporting companies in efforts to seek new customers or build new products.[35] A new TAA program could encourage proactive retraining by providing tax benefits to companies that make human capital investments as AT&T has done for its workforce.[36]

Expand the Earned Income Tax Credit

The Earned Income Tax Credit is a wage subsidy provided to low- and middle-income working families where workers receive a credit equal to a fixed percentage of their earnings.

The Center on Budget and Policy Priorities calculates that the EITC was responsible for lifting 8.9 million people out of poverty in 2017.[37]

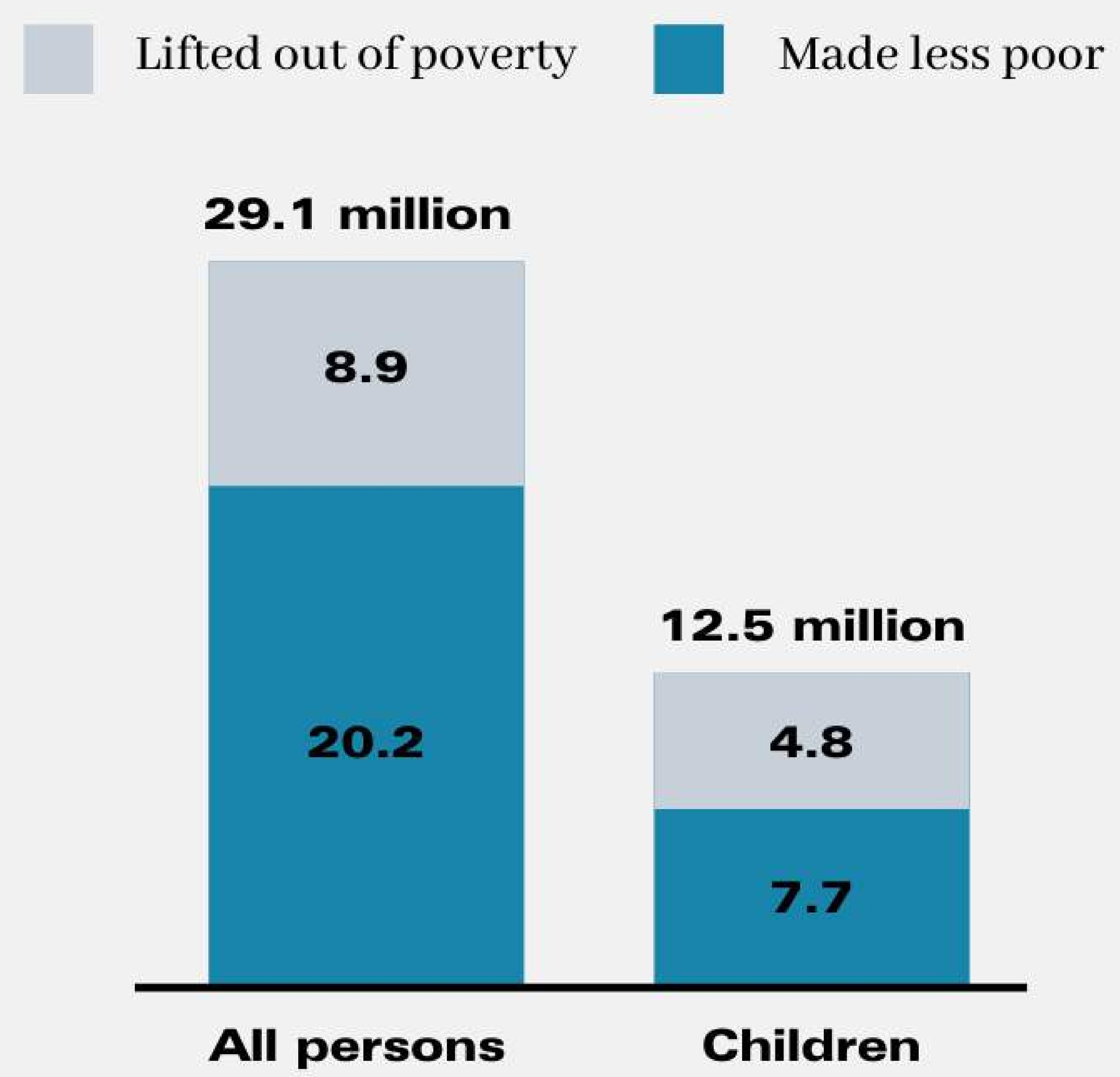
According to the Tax Policy Center, this makes the EITC the single most effective government program at bringing working-age households out of the poverty income level.[38] Lowering the age of eligibility from 25 to 21 and expanding the EITC, particularly for childless adults who qualify for much lower benefits, would incentivize individuals to join the workforce. The EITC encourages potential workers to seek out jobs so that they can earn credit upon finding employment.

Meanwhile, employers increase their search efforts to fill jobs because they get to capture part of the credit for themselves by paying lower wages. This drives firms and workers to aggressively seek each other out. An added benefit of expanding the EITC is that it can reduce reliance on unemployment insurance and other federal programs while getting people back to work.

An analysis by the Urban Institute suggests that the EITC likely reduces participation in the Food Stamp program, since EITC benefits reduce the need for other welfare.[39] In the case that disruption due to trade causes a worker to lose his or her job, an expanded EITC would help incentivize them and their future employer to seek each other out quicker.[40]

Earned Income Tax Credit and Child Tax Credit Have Powerful Anti-Poverty Impact

Millions of persons lifted out of poverty or made less poor (using Supplemental Poverty Measure) by EITC and CTC, 2017



Note: Unlike the Census Bureau's official poverty measure, the SPM counts the effect of government benefit programs and tax credits.

Source: CBPP analysis of Census Bureau March 2018 Current Population Survey and 2017 public use file.

Expand the Manufacturing Extension Partnership (MEP)

Manufacturing employed 8.5% of the total workforce and contributed almost 12% of all economic output in the U.S in 2018.[41] Since manufacturing is such an important industry to the U.S. economy and is so closely tied with trade, there should be a clear strategy to support American manufacturers in today's modern economy. One program doing that is the Manufacturing Extension Partnership (MEP), a highly effective agency housed within the U.S. Commerce Department that has satellite centers in every state.

The central mission of the MEP is to provide local manufacturers with business and technical guidance to tap into the global market. Rather than paying the high fees charged by large consulting companies, these local manufacturers pay for MEP services on a sliding scale.

Over 26,000 companies consulted with MEP in 2017, and they reported $12.6 billion in new and retained sales, $1.7 billion in cost savings, $3.5 billion in new investment, and over 100,000 new jobs.

Fifteen comparison-based group evaluations of the effectiveness of MEP found some positive and significant effects in firms served by the program relative to un-served firms after controlling for size, industry, and other factors. These effects included improvement in sales growth, productivity (value-added per employee) growth, job retention (and in one case, job growth), and technology and process improvement adoption.[42]

Recent MEP projects have helped small manufacturers implement the necessary technology to link up with digital supply chains, meet new food safety and cybersecurity demands, realize energy savings, and upskill their workforce.

The MEP's budget is only $140 million per year, but its economic benefits are nearly 14 times greater than its cost according to independent evaluations.[43]

With a benefit-cost ratio of that magnitude, expanding the MEP program could provide enormous benefits to American manufacturers.[44] Other OECD countries like Japan, Germany, and Canada spend much more on programs like the MEP to great effect. In a show of bipartisan consensus, U.S. Representatives Mike Kelly (R-PA) and Jim McGovern (D-MA) authored a letter to Congress in support of continued funding of the MEP program for FY2020.[45] Rather than eliminating the MEP program as President Trump has suggested in his previous budget proposals, Washington would be well served to increase its funding significantly.

THE IMPORTANCE OF DIGITAL TRADE

Already, around 12% of global goods trade is via international e-commerce. Businesses can use websites or other digital platforms to become global through online purchasing and offline delivery. E-commerce provides a potentially significant opportunity to increase small business participation in international trade. For instance, having a website gives small businesses an instant international presence without having to establish a physical presence overseas. In addition, the internet provides access to advertising and communication services, as well as information on foreign markets—all of which help small businesses participate in international trade.[46]

A HIGH RETURN ON INVESTMENT TO TAXPAYERS

For Every One Dollar of Federal Investment

$29.5
in New Sales Growth for Manufacturers

$31
in New Client Investment

This Translates Into

$3.8 Billion
in New Sales Annually

For Every

$1,065
of Federal Investment the Network Creates or Retains One Manufacturing Job

Establish Tax-Base Insurance in States and Cities

When the federal government suffers a temporary economic downturn, low wages and job losses often reduce collectible tax revenues. The federal government often has the option to take on more debt to maintain government services, but states—many of which have annual balanced budget requirements—are often forced to cut spending or raise taxes immediately—risking a vicious cycle that exacerbates a short-run slowdown.

Moreover, since states cannot cut many of their programs (like Medicaid) because of federal mandates, any spending reductions may fall disproportionately on a narrow pool of programs, many of which serve blue-collar workers and low-income households.

Akash Deep and Robert Lawrence, economists at the Harvard Kennedy School, have proposed using a federal tax-base insurance program to help states get through a sudden reduction in tax revenue.

Just as the federal government provides workers with unemployment insurance, it should provide counties, cities, and states with tax-base insurance, a self-financing program that could allow communities to pool the risks of negative shocks to their tax base. States and localities would pay a small premium for the insurance, which would only take effect when tax revenues dropped below a certain threshold.

Beyond that point, the federal insurance program would compensate a proportion of the lost tax revenues. The insurance would be based on changes in revenues that happen for economic reasons, factoring out any tax increases or tax cuts enacted by policymakers. Such a policy would allow states and localities to pool the risk of tax-base shocks and thus be able to respond to short-term crises in ways beyond cutting spending or raising taxes.[47]

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