Episode 480: Is Free Trade Helpful or Harmful for America?

Guest: Don Boudreaux

WOODS: This topic, I've gotten so many requests, you've got to talk about free trade, because so few people it seems are really mustering a very effective defense of free trade. It's like the anti-traders have just swept the boards. They're the ones who are getting the big crowds. We've got Donald Trump, we've got Bernie Sanders — they are the ones getting all the attention. And it seems like the establishment, which is supposed to be for free trade, at least some form of it, is not even trying to fight back.

So I want to know, on this — and the establishment has trade agreements with 20,000 pages in it. You and I would have one sentence for these agreements. What I want to know is, before we get into the classical arguments for free trade, what kind of response can we make when somebody says the following things, and right now I'm reading from Pat Buchanan's book, *Suicide of a Superpower*. I'm going to read you some facts and figures, and you tell me if there's anything wrong with these or if there's a different way we can think about them.

He says, "From December 2000 through December 2010, U.S. industrial production fell for the first time since the Depression, and America lost over 3 million private sector jobs, the worst record since 1928 to '38. In the same decade, 5 ½ million U.S. manufacturing jobs, one out of every three we had, disappeared. Manufacturing, 27% of the U.S. economy in 1950, is down to 11% and accounts for only 9% of the non-farm labor force."

And then he goes on and talks about trade deficits. He says, "The Bush II era was the first in U.S. history in which government began to employ more workers than manufacturing." And then he again cites more trade deficit figures. Then he says, "From December 2000 to December 2010, New York and Ohio lost 38% of their manufacturing jobs. Over the same period, New Jersey lost 39% and Michigan lost 40%." And he goes on to say that, "This goes to show" — forget about all your abstract theorizing in your economics departments — "these are the real consequences of free trade, which is why we need to go back to economic nationalism." What is wrongheaded about that?

BOUDREAUX: So much. Where to start? First of all, let's pause it at the beginning, that of course the period from 2001 to 2010 was no great laissez faire era. Government did grow too much. It is unfortunate that government employment grew. We all agree that that's a bad thing. But beyond that, there's not much of any merit in what Buchanan says. The time period he chose is very suspect, 2001 to 2010. 2010 was still in the midst of very high unemployment created by the Great Recession, so the data just on that basis alone are suspect. Of course you're going to have deficiencies in jobs in every sector, in most sectors because of the time period that he chose.

But more fundamentally, what he fails to ask is what's happened to living standards over the few decades. And the one thing that you mentioned that Buchanan raised is he goes back to the 1950s. Well, if you look at what's happened to American living standards, the living standards of the way ordinary people, ordinary families in America enjoy over these past 60 years, they have gone up unquestionably. We live today, ordinary Americans do, at a level of material prosperity that is off the charts much higher than it was in the 1950s, even than it was in the 1990s. So what matters ultimately is not what kind of jobs you have; what matters is how ordinary people are living.

Now, he focuses on manufacturing jobs. This is sort of a red herring. Yes, it's true, there has been a decline in manufacturing jobs. It is not controversial at all to point out that much of that decline — not all — much of that decline comes from automation, having nothing to do with international trade. Some of it has to do with international trade. Countries that have a large pool of very low-skilled workers who are willing to do rote assembly work at low wages, they will get some jobs that were once performed in higher wage countries, such as the United States, but that's a good thing for Americans; it's not a bad thing. We get more things at a lower cost than we otherwise got.

Buchanan, whose knowledge of economics is deeply suspect, fails to apply his alleged reasoning to a longer period of history. You could say the same things that Buchanan says today about manufacturing jobs, you could say the same things 100 years ago or 90 years ago about agricultural jobs. At one point in this country, agricultural jobs were about 80% of all jobs, and look, by gosh, they've largely gone away. Roughly 1 ½ out of 100 jobs today, as opposed to 80% of the jobs is in the agricultural sector. That doesn't mean Americans are somehow poorer; that means Americans are richer. We get food — and by the way, more food, much better food, a larger variety of food — at a lower cost today than we did at any time in the past, despite the fact that we have far fewer Americans actually working on farms than we did in the past.

The same thing is now happening with manufacturing, and largely for the same reason. While some of it is moving to countries that have a comparative advantage in manufacturing, much of the increase in manufacturing output is occurring because of automation. And so Buchanan picks and chooses, he throws out these statistics that seem on their face to the uncritical thinker to make a case against free trade; in fact, they make no such case at all, because the data are poorly chosen and the interpretation of the data are done without any economic understanding.

WOODS: A lot of people will say that what we've been seeing is a transition from manufacturing to a service-based economy, and they'll say that — well actually, frankly, I'm not really sure what their argument is, because it's very difficult to grasp. They seem to be suggesting that there's something inherently better about making physical stuff than there is about performing services for people.

BOUDREAUX: Yes, just as some people in the past argued that there was something physically better about working on a farm than working in manufacturing plants in cities. People do have a fondness for the past. Look, it is true, Tom. People do have this affection for manufacturing jobs, because, particularly for people in Pat Buchanan's generation, those were the stereotypical jobs where the working class, middle class worker without a college education spent his or her career and provided for his or her family.

But think about it. Even back then, no one, when you think about the kinds of jobs we want our children to grow up to perform, those jobs are all in the service sector. We want our children to become doctors and lawyers and architects. I've never heard anyone say, you know, son, I really want you to grow up to be a pipe fitter. That's what my dad did. My dad worked in the manufacturing sector. I'm a college professor. I have a much higher income, real income than he could ever dream of by working in the manufacturing sector.

So the manufacturing sector, just like the service sector, has a range of different jobs, some of which pay more than others. There are certainly some manufacturing jobs that still pay more than some service sector jobs, but many service sector — the service sector is not limited to what people like Pat Buchanan want us to think it's limited to. It's not limited to people working flipping burgers at McDonald's or cleaning rooms at Motel 6. Those are part of the service sector, but the service sector also includes neurologists; it includes college professors; it includes architects; it includes lawyers; it includes people doing medical research; it includes engineers. These are all people in the service sector, and it's that sector that's growing.

And one reason it's growing — this is a fact Pat Buchanan and people like Bernie Sanders and Donald Trump miss — one reason service sector jobs are growing and service sector output is growing is precisely because we can get manufacturing output now using much more automation than we could in the past. That releases workers; that releases resources to work in the service sector in those areas that are most responsible today for increasing our standards of living.

WOODS: What about the argument from anecdotal evidence that we hear, that there's a tremendous amount of insecurity that people feel in employment these days or we have a lot of people who are underemployed? And they will conclude from this that we had jobs before, then we got these trade agreements — now, bearing in mind that they are not factoring automation, but even if they did, they would probably be against automation, because it takes away their jobs. But they would say that before we had much more economic security, whereas now we can barely fit ourselves into the economy, that the professors are telling us that our labor has been released so that we can now do other things, but well, tell that to some guy who's been sitting there unemployed for a year. How do we respond to that kind of claim that we're hearing, that this is a unique sort of economy that we have now, where you don't have the kind of security you used to have?

BOUDREAUX: Yeah, see, I dispute the empirical claim. I mean, the 1950s were a unique time in the United States. The rest of the world was largely destroyed by war, and so the American economy then having largely been isolated from the effects of the war didn't have to worry about — there was no foreign competition. I think that was bad for America, not good for America. A secure job in itself is not what's desirable, but what's desirable is a high and rising standard of living. And our standard of living, as I said before, is high, and it does, despite all the government interventions, continue to rise.

I think the more general point to make — as opposed to disputing the empirical claim — the general point to make is that when people oppose free trade, what they're really opposing is economic change. What they're really opposing is competition. What they're really opposing is the freedom of consumers to spend their money, the money that they earn, as they wish, rather than as some political elites would prefer them to spend their money. Any kind of economic change — I don't care where it comes from: international, domestic — any kind of economic change puts some people out of work and creates jobs elsewhere.

An example I'm fond of using is the Salk-Sabin vaccine for polio. That was largely a domestic process. Salk and Sabin were doctors in the United States; they invented this polio vaccine, and my gosh, look what happened. It worked, and so all these people who played by the rules and were secure in their jobs making wheelchairs and crutches and iron lung machines and working in polio sanitariums, suddenly they find themselves out of jobs. Do we want to stop that? Should we lament that? Of course not. That's a good thing. This technology made people better off and therefore reduced the demand for people who otherwise had to make things like wheelchairs and crutches. And it's the same kind of thing for any economic change.

Another example I use is, you remember about 15 or so years ago, the Atkins diet was very popular. That was a domestic thing, so people chose to consume fewer carbohydrates and more meat, and so you had an increase in the demand for pork and beef and a decrease in demand for donuts and beer. Do we say, oh this is terrible; we shouldn't allow people to change their consumption patterns, because that causes economic insecurity? Obviously we don't do that.

And then I see nothing about commercial transactions that happen to cross political borders that's any different from commercial transactions or commercial changes that occur within political borders. It's all economic change. So if you say I want to protect existing workers' jobs, I want make existing workers more secure in their jobs by stopping international trade, I will say I'm willing to at least concede that your argument is consistent if you're also willing to say that part of your program is that you're going to prevent consumers from changing the way they spend their money even domestically. Because any kind of change in the way consumers spend their money causes some job insecurity.

So these people who argue against trade, they fail to — among many other errors — they fail to adequately identify just what it is they're opposed to. They think, unthinkingly, because some money happens to cross a geopolitical border, that that transaction is somehow unique or distinguishes it from transactions that take place domestically, and in fact, it does not.

WOODS: You said before that in Buchanan's day in the 1950s, it was very common for people to have a job in manufacturing because they could get that job, get reasonable wages, without even having to finish high school, and today we have different kinds of jobs. But the opponents of your position would say that we may have shed some of these lower skilled jobs and maybe we are getting higher paying jobs in replacing them, but the problem is these low-skilled people don't have the skills, so that the jobs they might have been able to get have either all been automated or exported, so there's no reason that we should say that a free market economy automatically makes everybody better. What if you're low-skilled? All your jobs have been exported or automated now.

BOUDREAUX: Well, I repeat what I just said a moment ago. For some people, this can be true. You can be 55 years old and you were specialized in doing a very certain kind of thing in the market, and suddenly the demand for your services has declined. But there's nothing unique about international trade that brings that about. Any kind of change, it can happen domestically —

WOODS: But I think there would be, and the thing they would say is that at least in the United States, I'm on a level playing field, because everybody — we have a standard of living and cost of living that is roughly equivalent across the U.S. with some variation, whereas in China, they can afford to work for $1 a day, and there's no way I can compete with that. That's why I'm losing my job.

BOUDREAUX: Two things I want to say: the first thing, I'm going to push back a little bit. If the problem is that someone who is a decent person, mid-50s, early 60s spent his or her life working in a particular job and suddenly finds that the demand for his or her services has declined, it makes no difference to that person why. It might be because the consumers are now buying what he or she produced from some lower wage Chinese people, or it might be because fellow Americans have decided they no longer like that product and they're buying something else maybe domestically. From their perspective, it's all the same.

And the more fundamental thing I want to say is part of the bargain that people make when they work in a market economy is part of playing by the rules. Playing by the rules includes the following: that you as a producer respond to consumer demands. The only reason people in our economy are as prosperous as they are is because they have an economy that's largely consumer-driven.

Consumer sovereignty is largely the rule, to the extent that consumer sovereignty is not the rule with poorer, to the extent that we're wealthy — and we're very wealthy — it's because consumer sovereignty is the rule that we play by. And no one should be entitled to say, oh look, I like consumer sovereignty, because it enables me to spend my money as I want, and when consumers were buying things from me for my producer side, it made me reasonably wealthy. I liked consumer sovereignty then. But when consumers change their mind for whatever reason, I want to be an exception to that rule. I want government to prevent consumers from shifting their expenditures away from what I produce and force people to spend their money on what I produce. I want to be an exception to that rule. No one gets to be an exception to that rule. If we made everyone an exception to that rule, then we would be a desperately poor country. All of us would be desperately poor.

Another way to look at it or another aspect of this is to recognize that, despite America's protectionist past, we've never been completely closed off. By 2015, I think it's almost impossible — maybe I need a few exceptions. It's almost impossible to identify any job that's not itself largely the creation of international trade. It's largely impossible to identify any job that exists today that wouldn't have existed today in its current form, had we not had open international trade. So I think a lot of — I understand that look, it's difficult to lose a job. Of course I understand that. But being flexible and being willing to play by the rules of consumer sovereignty is required to have the kind of prosperity that the people who are losing their jobs don't want to lose.

WOODS: All right, well what about the claim that, given that Americans earn pretty good wages compared to people in other countries — and there are reasons for the differential, but the differential exists — wouldn't the opening of international trade necessarily mean that there'd be a convergence of wage rates somewhere in the middle, so that the people on the lower rungs would see theirs go up, but Americans would see, in competition with these people, their wages go down? Is that true or is it not true, and if it is true, why would they want that?

BOUDREAUX: That's not true. The best way to begin to explain why that's not true is to ask the question, why are Americans' wages as high as they are. Americans' wages are not as high as they are because American workers are enjoying some unearned surplus by being protected from competition. American workers' wages are as high as they are, because Americans have a lot of capital to work with, which makes American workers highly productive. And by capital here, I don't mean just highly automated factories that they work in and the machines that they work with. That's part of it, but also, the great infrastructure we have. The network of roads that are safe and passable. Deep water harbors that allow people who produce to have their product shipped abroad safely. The system of the rule of law that we have. This infrastructure, broadly conceived, makes American workers highly productive. That's why Americans' wages are as high as they are.

And so when we have more open trade with people in lower wage countries, in many cases, the lower wages of foreign workers are not necessarily an advantage; they're just a reflection of the fact that those workers produce less per hour than do American workers. Now, the fear is of course that when trade is opened up, that capital will flow to these low-wage countries, because well, if you build a factory in Pakistan or if you build a factory in Mexico, the entrepreneurs who do that, they can gain access to low-wage workers, and these workers have these higher, more productive capital, so more production will take place in these foreign countries.

Some of that's true, but what people who tell that story typically miss is that the amount of capital in the world is not fixed. If it becomes more attractive to invest in Mexico or in Pakistan or in Bangladesh, that doesn't make it necessarily less attractive to keep investing in America. The patterns of investment may change. We know from the principle of comparative advantage that when trade opens up, it may be that Mexico has revealed they have a comparative advantage of producing, say, shoes. And so Americans who are currently working in shoe production, they will lose their jobs. But that means that Americans have a comparative advantage at producing other things.

You know, when Ross Perot — you and I remember this, Tom — when Ross Perot posed NAFTA — and I agree with you; a genuine free trade agreement is one sentence, not multi thousands of pages — but when Ross Perot opposed NAFTA, which did generally make trade freer between the United States and Mexico, he famously predicted the giant sucking sound. And of course the giant sucking sound is well, if you open up trade between high-wage America and low-wage Mexico, all the investments are going to take place in Mexico and none in the United States, because who would invest in high-wage America when they can invest in low-wage Mexico?

And lo and behold, guess what happens. In that time after NAFTA, America's trade deficit with Mexico rose. Now, what that means — it sounds bad, because people don't understand what trade deficit is — what that means is that there was a greater amount of investment by Mexicans in America than there was by Americans in Mexico. So what this reveals is that the factors that make Americans' wages higher — the rule of law, the relative attractiveness of investing in the United States as opposed to Mexico — dominated, for investors, the fact that the hourly wages earned by typical Mexican production workers were lower than were such wages in the United States. And so since NAFTA went into effect, both the United States — ordinary Americans — and ordinary Mexicans have grown wealthier. I think ordinary Americans have grown wealthier certainly in absolute terms, and I think even relatively so compared to Mexicans, because America compared to Mexico continues to be a more attractive place to invest, not because —

WOODS: But what about when we hear about wage stagnation in the U.S.? What has been the real trend in wages in the U.S. over the past 20 or so years?

BOUDREAUX: Yeah, this is a giant myth, and it's one that requires — we could do a whole show on this. I believe that this wage stagnation thing is a complete fallacy. There are official statistics that you can point to in support of that case, if you want to make that case. The Bureau of Labor Statistics gathers a statistic, I forget the exact name, like the Inflation-Adjusted Hourly Wage of a Non-Supervisory Production Line Worker — something like that. Basically an ordinary worker. And if you look at that wage adjusted for inflation using the consumer price index over the past 50 years, it hasn't changed. It has stayed pretty much the same, adjusted for inflation. So people point to that and say see, Americans' wages have stagnated.

Well, at least two things, although I said we could do a whole show on it: this is an average; it's not a wage that tracks individuals. As more and more people enter the workforce — so as we get more immigrants coming into the workforce, as women enter the workforce in larger numbers as they have over these past several decades — the lower wages that they earn tend to pull down the average, even if that has no effect on the actual wages that flesh and blood workers are earning.

More fundamentally, I think the wage measure is grotesquely inadequate. First of all, it does not include non-wage benefits. Non-wage benefits have almost doubled as a portion of the typical worker's pay package over the — I forget the exact date; I think since 1975. It's gone up from about 10% of the typical worker's pay package I believe in the year 1975 to today, 2013, to about 19% of that worker's pay package. So that is a part of pay that's not calculated.

But even more fundamentally, as the nature of the economy has changed, the kinds of things that ordinary people consume, that Americans consume, changes. Tools we use to measure economic activity were created back in the 1930s and '40s, national income accounting. These tools I believe are increasingly inadequate to account for the modern economy. So if you look at work hours, if you take a simple measure — not of taking nominal wages and adjusting them for changes in the price level in order to come up with real wages over time — but if you look at the number of hours the typical worker had to work to earn income to buy various goods and services in the past, and then look at the number of hours the typical today has to work in order to buy similar goods and services today, what you find in almost all circumstances is that the number of hours that the typical American has to work today to buy a coffee maker, to buy a kitchen range, to buy automobile tires, to buy contact lenses — the number of hours has fallen dramatically.

There are exceptions to the rule, but overall the number of hours a typical person has to work today to buy a standard bundle of commodities or household goods is dramatically lower today than it was in the 1970s. And this is not to mention the improvements in quality — you and I are talking now using a technology that wasn't available even to the richest American in 1975. And we're doing it free of charge.

WOODS: Yeah, exactly. I always wondered how, if at all, this could ever be factored into any official statistic.

BOUDREAUX: It's very, very difficult. This is part of the problem, precisely because — you and I are using Skype now — precisely because these official income and economic activity measurement tools were not designed to account for the kinds of economic activity that are so common today. We miss in these statistics a huge amount of the advances. We fail to quantify and measure a huge amount of the advances that ordinary Americans enjoy. And so I believe this wage stagnation story is a complete myth. This is something I've researched a fair amount, and the more I research it, the more I'm convinced it is just nonsense. It's an older book now, but Mike Cox started this line of research back in the 1990s. Mike's now an economist at SMU, he used to be the chief economist at the Dallas Fed —

WOODS: Oh, is this the book, *The Myths of Rich and Poor*, or something like that?

BOUDREAUX: Yeah, it came out in 1999 and it's a very data rich book, and so it's a little bit dated in its data, because it's already 16 years old, but I've basically tried to update a lot of what Mike and his co-author, Richard Alm, have done in that book. And the story not only continues, it gets stronger. Ordinary Americans are growing richer and richer by the year. There was a blip a few years ago because of the Great Recession, but even that, it didn't alter the trend very much.

WOODS: Is this work of yours, is this something you're doing on the side, is this something you've had published in anything we can read?

BOUDREAUX: Yeah, I have a lot of it on my blog, Tom. I would like to assemble it in one space. I'd be happy to send to you some links to things on my blog.

WOODS: Yeah, because I'll put links — today's show notes page will be TomWoods.com/480, and I definitely want to link to this, because this is really the meat of the whole question right here, is what is the trend in living standards.

BOUDREAUX: Yeah, and I have a stock speech that I give with a PowerPoint presentation, and I'll give this in pointing out that, look, Americans, the cost of living when measured in work time for ordinary Americans has fallen dramatically over the past 40 or 50 years. And then people who don't like it, they'll come to me and say, oh yeah, well, the reason that's true is because of free trade — as if that's a condemnation. Yes, part of the reason is that Americans are trading more freely, but this is the benefit of trade, that we get more and more goods and services, a wider variety of goods and services at lower and lower costs. That's precisely what free trade is supposed to do economically, and it's doing it. And it always amuses me that on the one hand I'll have people say that, well, because of free trade, ordinary Americans are not living any better today than they were in 1975. And then I'll do this presentation, and then the similar kinds of people will say, yes, that's true, but that's only because we've had free trade. It's weird.

WOODS: (laughing) Yeah. You know, I've sometimes thought, just do a thought experiment: do you really want to Buchanan back in the '70s listening to your 8-track tapes and your exploding Pinto without air conditioning? I mean, there are so many things that people today would find absolutely intolerable, they would be begging to get back into that time machine sitting here in 2015. Now of course, I will link to whatever you send me, but also in general, if people just want to follow what you're doing, where's the best place for them to do that?

BOUDREAUX: Oh by far, it's my blog that I do with Rush Roberts. It's Cafe Hayek, www.CafeHayek.com, and we put stuff up on it two or three times a day almost without fail. And if you go to Cafe Hayek, there's a drop-down list of categories on the left-hand side of the page, and on that drop-down list, one of the categories is Standard of Living, and a lot of my posts about the things that you and I just talked about are, if you click on "Standard of Living," it'll take you directly to those series of posts that deal most closely with questions about changes in the standard of living over the past several decades.

WOODS: Okay, so that's what people should do. I'll link to whatever you can send, and then we'll link to the blog in general, CafeHayek.com. You should check out the Standard of Living stuff, but just check it out. Any blog where you can reliably get two or three posts a day is pretty good in my book, because sometimes I'll go to some place and they're great, but then five days go by, I get no more content. So we'll definitely try and drive some traffic your way. Well, Don, thanks, I know we actually went a little longer than I promised we would —

BOUDREAUX: My pleasure.

WOODS: — but it was great material, and I know listeners are going to benefit from it. Thanks so much.

BOUDREAUX: Thank you, Tom.