

Free Trade That Makes Sense is Regional, Not Global

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GLOBAL FREE TRADE has become a sacred principle of modern economic theory, a sort of generally accepted moral dogma. The ultimate objective of global free trade - to create a worldwide market in products, services, capital and labor has an instrument to achieve this in GATT, the General Agreement on Tariffs and Trade.

GATT however, is flawed, as are the theories on which it is based. If it is implemented, it will impoverish and destabilize the industrialized world while at the same time cruelly ravaging the Third World.

During the past few years, 4 billion people have suddenly entered the world economy. They include the populations of China, India, Vietnam, Bangladesh and the countries that were part of the Soviet empire. The populations of these countries are growing fast; they are predicted to pass 6.5 billion within 35 years.

The nations where those 4 billion people live have very high levels of unemployment. And pay for those who have jobs is a tiny fraction of pay levels in the developed world. So new entrants into the world economy are in direct competition with the work forces of developed countries. They have become part of the same global labor market.

This will lead to a new type of competition. Take two enterprises, one in France and one in Vietnam, making an identical product for export to the same First World market. Both use the same technology and have access to the same pool of international capital. The difference is that the Vietnamese enterprise can employ 47 people for what it costs the French enterprise to employ one. It is not difficult to understand who the winner will be.

In most developed nations, an average manufacturing company pays its work force an amount equal to 25 to 30 per cent of sales. If such a company decides to maintain only its head office and sales force in its home country while transferring production to a low-cost area, it can save about 20 per cent of sales volume. Thus, a company with sales of \$500 million will increase its pretax profits by up to \$100 million a year.

If, on the other hand, it decides to maintain production at home, the enterprise will be unable to compete with low-cost imports, and will perish.

When an economic policy makes you rich if you eliminate your national work force and transfer production abroad, and bankrupts you when you employ your own people, then something is wrong.

High-tech industries can survive and prosper in these circumstances, of course, for they are highly automated and employ few people; labor is a minor item in the overall cost of the products they make. They obviously cannot compensate for the lost manufacturing jobs; the fact that they employ few people means that they are incapable of employing very many. As soon as they need a reasonable number, they will be forced to move offshore.

IBM, for example, is moving its disk-drive business from the United States and Western Europe to low labor-cost countries. It plans to operate as a joint venture with an undetermined Asian partner and use non-IBM employees so that it will be easier to move to an even lower-cost region when warranted.

IBM estimates that moving from higher-cost regions to Asia halves the cost of assembling a disk drive. Boeing has announced plans to transfer some production to China. Companies like Hewlett-Packard and Advanced Micro Devices, the sort that created Silicon Valley, are also shifting employment to low-wage countries.

Proponents of global free trade insist that exporting such high-tech products as airplanes, satellites and high-speed trains will create jobs on a large scale. Alas, this is not true. A recent \$2.1 billion contract selling high-speed French trains to South Korea has resulted in the maintenance, for four years, of only 800 jobs in France. Much of the work is carried out in Korea by Asian companies using Asian labor. After the transfer of technology to South Korea, in a few years Asians will be able to buy high-speed trains directly from South Korea and bypass France.

A big mistake in thinking about balanced trade is to consider it exclusively in monetary terms. If we export \$1 billion worth of goods and import products of the same value, we conclude that our overseas trade is in balance.

But the number of people employed annually to produce \$1 billion worth of high-tech products in the developed nations could easily be fewer than 1,000, while the number employed in low-cost areas to manufacture the goods that we in the developed world import would be in the tens of thousands, because these goods are produced with traditional levels of employment.

Balancing trade in this way can end up exporting jobs and importing unemployment.

The application of the GATT accord will have tragic results in the Third World. Modern economists believe that an efficient agricultural system is one that produces the maximum amount of food for the minimum cost, using the least number of people. That is bad economics.

When you intensify agricultural methods and substantially reduce the number of people employed on the land, those who are idled are forced into the cities, where they often end up in slums. Families are broken, the countryside is deserted, and social stability is destroyed. This is how the favelas came into existence in Brazil.

An estimated 3.1 billion people live from the land. If GATT manages to impose the sort of productivity achieved by the intensive agriculture of nations like Australia, some 2 billion of these people will lose their livelihood.

Some of these GATT refugees will move to urban slums, while many others will be forced into mass migration. As a result of Chinese market-oriented economic reforms, an estimated 100 million peasants are drifting around China seeking work.

Is it not possible to repeat the successes of countries like Taiwan, Hong Kong, South Korea? Well, the United States might be able to achieve a similar success with Mexico, and Western Europe could progressively accommodate Eastern Europe. But attempting to integrate 4 billion people at once into global markets is blind utopianism.

To avoid disaster, we must first reject the concept of global free trade and replace it with regional free trade. That does not mean closing off any region from trading with the rest of the world. It means that each region is free to decide whether or not to enter into bilateral agreements with other regions.

We must not simply open our markets to any and every product, regardless of whether it benefits our economy, destroys our jobs or destabilizes our society.

Those who wish to industrialize should form free trade areas, such as the trading regions currently being created in Latin America and Southeast Asia. These areas should consist of nations with economies that are reasonably similar in terms of development and wage structures. Trading regions would enter into mutually beneficial bilateral agreements with other regions in the world. Freedom to transfer technology and capital would be maintained.

Commercial organizations wishing to sell their products in any particular region would have to produce locally, importing capital and technology and creating local employment

and development. That is the way to create prosperity and stability in the developing world without harming developed nations.

GATT must be rejected. It is too profoundly flawed to be a stepping stone to a better system. The damage it will inflict on the communities of both the developed world and the Third World will be intolerable.