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"Trade in the Age of Anxiety"

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Good afternoon. It is a pleasure to be here today.

I would like to discuss some of the Administration's present efforts to open trade. But first, I want to address the broader context in which trade matters are considered in Washington these days – namely the broader context of globalization.

The title of my remarks is "Trade in the Age of Anxiety."

The theme of my remarks is best reflected in Yogi Berra's observation: "We are faced with insurmountable opportunities."

If you would indulge me for a moment, I would like to suggest that Berra's commentary on baseball also applies to globalization. In today's increasingly globalized world, we are, indeed, faced with insurmountable opportunities.

Yogi's line captures the paradox that, while the global economy has yielded unprecedented gains in standards of living in the United States and throughout the world, it is also a source of great anxiety for some. I know that many individuals, families, communities, even countries are not benefiting fully from the global economy. Yet, never in history have so many had so much.

There was a compelling chart in the "Financial Times" several months ago. It measured global Gross Domestic Product (GDP) per capita, over the past two-thousand years.

I cannot vouch for the methodology of assessing GDP a thousand or more years ago, but even at an intuitive level, the chart painted a powerful picture. It showed a fairly straight line of no meaningful economic growth for nearly two millennia. Then, beginning with the onset of the Industrial Revolution about two hundred years ago, it showed a very steep climb in per capita income growth. Undeniably, a major factor in this growth is increased productivity.

As a result of unprecedented gains in productivity in recent generations, millions of people today enjoy lives unrecognizable a century ago, in terms of the quality and quantity of food, health care, housing and other goods and services.

By today's standards, Thomas Hobbes' characterization of life as "nasty, brutish and short" seems overly cynical and unimaginative. But when he uttered those words in the seventeenth century, they reflected a world far different than the one most of us know today.

Ever-expanding technological know-how has unleashed a steady stream of tools, permitting us to become the most productive work force in history. As labor-saving technologies have been adopted, people have been freed up to pursue new kinds of work, and to enjoy more leisure.

At the beginning of the 20th century, approximately 40 percent of the American workforce was employed in agriculture. Today, only about two percent of our population farms on a full-time basis. Yet today's agricultural output dwarfs that of even a generation ago. Advances in technology, particularly after World War II, have led to tremendous growth in agricultural productivity.

A similar story can be told in manufacturing. Fewer Americans may work in manufacturing today, but we produce far more than ever. In fact, since 1994, manufacturing output in the U.S. has grown by 50 percent. Despite the rhetorical impression that we have lost our manufacturing prowess, the United States remains the world's largest manufacturer, accounting for a quarter of world production. Even in the auto sector, Americans produce one third more cars today than were produced in 1980. Technology has allowed a precipitous drop in the number of man-hours it takes to build a car, allowing fewer people to produce more cars.

Technology has also allowed significant reductions in the costs of moving goods around the world. The marginal cost of moving a product from Asia to the United States is a fraction of what it was a short period ago. Similarly, advances in communications technology are driving those costs close to zero at the margins.

Beyond technological advances that allow workers to be more productive, there are considerably more people in the global workforce today. According to the International Monetary Fund, the number of "globalized" workers has quadrupled since 1980, rising from 225 million in 1980 to 900 million in 2005.

More workers and more productive workers have allowed standards of living for those in developed countries to rise and millions in developing countries to escape poverty.

So, if globalization is so great, what accounts for the political backlash?

First, we must recognize that the backlash is real, and is often fueled by heartfelt anxiety about the global economy. Responsible voices must engage in this debate. It is dangerous to allow the public debate to be dominated by the extremes:

> Those whose zeal for open trade leads them to ignore the anxiety, and
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> Those whose disdain for open trade leads them to exploit the anxiety.

Responsible voices must engage because the legitimacy of the global trading system is at issue. The current backlash is not so severe that legitimacy is likely soon to be lost. But complacency in the face of the current concerns invites avoidable risk.

The backlash comes from two very different groups:

> Those who think there's been ***too much*** globalization in their lives; and
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> Those who think there's been ***too little*** globalization in their lives.

Both groups deserve careful attention and tailored responses.

Those in the first group tend to come from the developed countries. They view globalization as a destructive force and believe they were better off before it.

To be effective, we must address this group in two ways:

First, we must raise the level of understanding of how the global economy benefits us. If left to Lou Dobbs and other critics to paint the picture, political support for trade will surely continue to deteriorate. Supporters of open trade must speak out forcefully about its benefits.

As consumers, we benefit tremendously from access to a broader array of goods and services than a closed system would provide.

As producers, we benefit from access to broader markets. More and more U.S. jobs rely on exports. One in six manufacturing jobs, for example, is supported by exports. And U.S. jobs reliant on exports pay an estimated 13 to 18 percent more than the U.S. national average. Exports from the U.S. are currently growing at more than twice the rate of imports, highlighting the importance of exports in creating higher paying jobs.

As producers, of course, the benefits of market access abroad are balanced against the pressure of more competition at home. Unfortunately, these costs often fall disproportionately on a small number of workers and businesses. The politics of trade can be explained mostly by the asymmetry of the costs falling mostly on a vocal minority while the benefits are enjoyed by a silent majority.

The politics are exacerbated by the fact that – to hear the rhetoric -- *every* job loss in America is attributable to trade. In fact, trade accounts for a very small percentage of job losses. By some estimates, they account for less than three percent of long term job loss in any given year. Technological advances, domestic competition and changes in consumer preferences account for the lion's share of worker displacements.

We also must help people understand that trade is not a zero-sum game. Economic growth in Asia or Latin America does not come at America's expense. The United States is both the world's largest importer and its largest exporter. As other countries prosper, they become better markets for our exports, and offer a greater variety of goods and services for import. The economic pie is not fixed.

The second response to those who see globalization as a destructive force must be a policy response. Preaching the virtues of the free market will not be effective if unmatched with policies to help people take advantage of the global economy.

In broad terms, those policies fall into four categories: job creation; education; portability; and an effective public safety net.

<u>Job Creation</u>: Job creation is the best form of adjustment assistance. A system of regulation and taxation that encourages

job creation and entrepreneurialism is the best antidote to job losses. Government policies that seek to preserve job security by making it harder to displace workers will have the opposite result. Such policies discourage job creation and invite higher unemployment.

Education: In a dynamic economy, those able to adapt more easily and quickly to change will fare the best. Such adaptability by workers requires strong basic education, including high school and beyond. It also requires lifelong opportunities – in and out of the workplace -- to refine skills. Any country's fate today will be determined significantly by its investment and output in education.

Portability: Employment-related public policies must reflect the frequency with which workers today change jobs. Many tax and labor-related policies were established when workers were assumed to receive health-care and retirement benefits from the same employer for their effective working lives. Given the increasing frequency with which workers today change jobs, some of these policies are out-of-date. For instance, more can be done to enhance the availability and portability of healthcare and retirement benefits.

Social Safety Net: An effective public safety net is essential. People will be less anxious walking the high wire of a dynamic economy if there is a net below. The dynamic nature of today's economy is ***the*** key source of its productivity. But it is also a key source of the anxiety about the economy. Some of the gains attributable to the global economy must be used to assist those who are adversely and temporarily affected.

Risk-sharing measures are not and should not be limited to those adversely affected by trade since job losses are caused far more often by non-trade factors.

The most important tools in mitigating risk are policies that promote economic growth. It is through such policies that new jobs will be created to replace the old ones. A dynamic, job-creating economy will always provide a better safety net than any individual assistance program.

Let me now turn to the second group of critics of globalization who tend to be from developing countries. They view globalization as a constructive force but feel they are not sufficiently reaping its benefits.

Maintaining political support for the policies and institutions that support the global economy requires expanding the opportunity to plug into the global economy.

This goal is best served through three policies: openness; rule of law; and foreign assistance, including capacity building.

Openness: Policies of openness are progressive in that they benefit the poorest the most. A study published in the *Journal of Economic Literature* found that openness has the highest income-growth effect at the lower quintiles of society. This makes sense. In a closed economy, the elite do fine. By definition, they are on the inside of the economy and enjoy a preferred status. The more open and transparent a society is, the more opportunities available to non-elites in a society.

Rule of Law: Peruvian economist Hernando DeSoto has written extensively about the direct link between property rights and economic growth. Clear and enforceable property rights allow for what economists call "impersonal exchange."

To non-economists, "impersonal exchange" sounds like something to be avoided. However, as many of you in this audience know, "impersonal exchange" is a key to our modern economy. It is what allows us, for example, to finance our houses with money from perfect strangers.

Without clear and enforceable property rights, people with capital would lend only to those whom they know personally and trust to repay the debt. As a result, there would be a significant under-investment in housing and businesses, as DeSoto has described in developing countries.

Rule of law is directly linked to progressive, broad-based economic growth. Strong institutions are necessary to promote and enforce the law. Building these institutions is often difficult and expensive, which leads us to the third policy.

Foreign assistance/Capacity-building: Without a strong domestic commitment to strengthening rule of law, foreign assistance – including trade capacity building and efforts to help foster accountability and greater transparency – will meet with very little success. Even with such a commitment, achieving success can be difficult. Helping countries build institutions and adopt best practices to foster rule of law is critical. The United States and other developed countries must continue to help in this regard.

Helping countries promote open economic systems can also play an important role in promoting independent political institutions. The trends favoring rising economic freedom are often closely tied to trends favoring expanding political freedom. Over the past 50 years, as economic freedom has been embraced by more and more countries, we have seen the number of democracies more than quadruple.

Both groups critical of globalization – those who think there has been too much and those who think there has been too little – arrive at their positions differently, but they are united in challenging the legitimacy of global economic integration.

During the last century, the world saw the collapse of political support for open economies and open trade, as nations embraced protectionist measures. The result was a decline in world trade between 1929 and 1934 by two thirds. It took generations for the world to recover from these misguided policies. I do not think the current backlash against globalization foreshadows a collapse of political support for open trade. Nevertheless, we should be informed by history and recognize that complacency in the face of today's backlash is imprudent.

A passage in Jeffrey Frieden's recent book, Global Capitalism, sums it up well,

> The history of the modern economy illustrates two points. First, economies work best when they are open to the world. Second, open economies work best when their governments address the sources of dissatisfaction with global capitalism.

We must address this dissatisfaction.

Let me now climb down from the high altitude of globalization and talk specifically about the Administration's trade agenda before Congress. In the interest of time and given the current focus in Congress, I will limit my remarks to our trade agenda within Latin America. I am pleased, however, to take questions on other aspects of the trade agenda.

For reasons already discussed, it is a challenging political environment in which to move trade items through the Congress. In fact, as I reflect on how best to do this, I am reminded of the wag who, upon being asked for directions by a lost motorist, replied, "Well first, I wouldn't start from here."

The focus of our Latin America trade agenda is securing Congressional passage of separate trade agreements we have negotiated with Peru, Colombia and Panama. Coincidentally, formal Congressional action on the Peru agreement begins today in the Senate Finance Committee.

Once these agreements are in place, a free trade zone will extend from the northernmost points of Alaska and Canada to the southernmost point of Chile.

This will be an historic achievement, fulfilling in large part the goal of a free trade zone in the Americas set forth at the first Pan-America Conference held in 1889 in Washington.

Building upon our existing trade agreement with Canada and Mexico, this Administration has negotiated, and Congress has approved, trade agreements with Chile, Costa Rica, Dominican Republic, El Salvador, Guatemala, Honduras, and Nicaragua.

I am confident the three pending agreements with Peru, Colombia and Panama will pass this Congress, paving the way for further trade liberalization in the hemisphere.

The case for these agreements is compelling for economic and geo-political reasons. Together, Peru, Colombia and Panama represent a market of nearly sixty million consumers. Duty-free access to these markets is important to US exporters.

Producers in these countries already enjoy duty-free access to the United States through tariff preference programs enacted by Congress. The benefits of providing U.S. exporters reciprocal access to these countries would seem obvious.

The agreements will also help to “lock in” rule of law, transparency and economic openness – the very principles necessary to ensure broad-based economic growth, political stability and regional stability.

Many in Congress are properly concerned about the wages and working conditions of workers in these countries. The best way to help these workers is by providing better economic opportunities. As President Reagan and President Clinton agreed, “The best social program is a good job.”

Numerous studies have shown that, all other things being equal, jobs related to trade offer better pay and working conditions than those unrelated to trade. I recently had a chance to see this first-hand during a visit to Colombia this summer.

Finally, I do not believe Congress will want to bear responsibility for America turning its back on those Latin American countries that have stepped forward to ask for our assistance in promoting more openness and stronger rule of law. Rejecting any of these trade agreements would have long-term and far-reaching effects on America’s standing in the region that would not easily be overcome.

The pending trade agreements with Peru, Colombia and Panama are part of a longer sweep of history. It is a history of freedom and empowerment of the individual. Latin America has suffered from too much concentration of wealth and power. Peru’s, Colombia’s and Panama’s successes in expanding opportunities throughout society will be determined primarily by policies established within the borders. But policies at the border – policies of open trade and investment – can reinforce internal reforms to open the economy and strengthen rule of law.

Let me close by making an appeal to you as leaders in the business community.

Do not be complacent about the policies and institutions that underpin international trade. Globalization is a choice, not a fact.

Trade flows are greater this year than last year, and will be greater still next year and the year after that. In the face of these trends, it is tempting to dismiss any concerns of political risk to the global trading system. But assessing risk is always a function of measuring the probability of an outcome against the consequences of that outcome. While the probability of political support for globalization completely evaporating is low, the consequences would be enormous. As such, I urge you to not take political support for open trade policies here or abroad for granted.

I strongly believe that global economic integration is a constructive force that will continue to bring positive changes to the world. But, as the Chairman of the Federal Reserve Bank Ben Bernanke has said, it is critical that the benefits of global economic integration be “broadly shared.” For moral, economic and political reasons, I believe he is right.

Thank you.