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Distressed workers: What has globalization to do with it?

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1. Introduction

We have recently witnessed a flurry of comment, by prominent figures such as Ben Bernanke and Larry Summers who are strong proponents of Globalization, asking the question: how do we assist the unskilled workers whose wages have been stagnating for far too long? Several of them also believe that even the “middle class” is at risk.

Lou Dobbs of CNN, the labour groups’ think-tank Economic Policy Institute, and nearly all the Democrats newly elected to the Congress, believe that globalization has much to do with the economic distress of the working and the middle classes. Therefore they have coherence and plausibility on their side when they want to lean on the door, even to close it, on trade with poor countries and occasionally on unskilled immigration from them. But the proponents of globalization, when they typically skirt and hence accept this “distributional” critique of globalization and nonetheless propose that the adversely affected constituents accept globalization but allow themselves to cope with their affliction in other ways, find themselves in a politically implausible position. Indeed, if it pours, we do not have the means to turn the torrent into sunshine and must open an umbrella. But man allows globalization; and men can turn it off.

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2. Globalization and wages of US unskilled workers

As it happens, however, the proponents of globalization are on firmer ground. Examine the common arguments linking globalization to the distributional distress; and little survives.

First, nearly all empirical studies, including those done by some of today's top trade economists (such as Paul Krugman and Robert Feenstra, both students of mine from MIT in the 1970s), show that the adverse effect of trade on wages is not substantial. My own empirical investigation, reported in Chapter 10 of my 2004 book, *In Defense of Globalization*, in fact argues that the effect of trade with poor countries may even have been to moderate the downward pressure on wages that rapid unskilled-labour-saving technical change would have caused.

Second, the same goes for the econometric studies by the best labour economists today, regarding the effects of influx of unskilled illegal immigrants into the United States. The latest study by George Borjas (no friend of illegal immigrants) and Larry Katz, both of Harvard, once necessary adjustments are made, also shows a virtually negligible impact on US workers' wages.[2]

Can it be that globalization has significantly reduced the bargaining ability of workers and thus put a downward pressure on wages? I strongly doubt this. First, the argument is not relevant when employers and workers are in a competitive market and workers must be paid the going wage. As it happens, roughly around 10% of the workers in the private sector in the US are now unionized. Second, if it is claimed that acceleration in globalization has decimated unionization, that claim is dubious. The decline in unionization has been going on for longer than the last two decades of Globalization, shows no dramatic acceleration in the last two decades, and is to be attributed to the union-unfriendly provisions of the half-century-old Taft-Hartley provisions that crippled the ability to strike. Third, it seems plausible that unionization has also suffered because fewer workers now expect that unions can deliver higher wages. In the public sector, the wages are squeezed because of budget constraints: as the recent NY Transit strike showed, the public utilities are increasingly unable to raise the price of services or to get more subsidies to finance losses and therefore the ability of unions in such a situation to get more for their workers is crippled. Again, increasing numbers work at home, in no small measure due to technical change such as on-line transactions, that facilitates such decentralized work, in a return to the pre-factory-work era, and are therefore less amenable to unionization.

But then, has the outflow of Direct Foreign Investment caused a decline in the capital which works at home with unskilled labour and hence to a decline in wages? But, as I look at the data, the US has received more or less as much equity investment as it has lost over the last two decades. One cannot just look at one side of the ledger.

3. Unskilled-labor-saving technical change and the wages of the unskilled

So, in lieu of Globalization as the culprit, one has to fall back on the argument that substantial unskilled-labour-saving technical change is putting pressure on the wages of the unskilled. Technical change happens to be continually economizing on the use of unskilled labour. Much

[2] Their study was the subject of an excellent Economics Focus column in *The Economist* magazine some weeks ago. I should add, however, that, just as my own work suggests that the effect of trade with poor countries on wages in the rich countries may even have helped, rather than harmed, the workers in the rich countries, there is also the work on US immigration by Giovanni Peri of the University of California, Davis, which argues similarly that illegal immigration into the US has improved the wages of US workers, not just harmed them insignificantly. His two studies have been published by the Immigration Policy Center, a division of the American Immigrant Law Foundation in March and in October 2006.

empirical argumentation and evidence exists on this, coming from labour economists such as Alan Krueger.

But a telling example comes from Charlie Chaplin's famous film, Modern Times. Recall how he goes berserk on the assembly line, the mechanical motion of turning the spanner finally getting to him. Try to see such an assembly line today and the chances are you will not succeed. Yes, there are assembly lines today; but they are without workers; they are managed by computers in a glass cage above, with highly skilled engineers in charge. The disoriented Charlie Chaplins have increasingly disappeared, at least from the assembly lines.

The facts are that this is rapidly occurring in the United States, and in other rich countries, as technical change is quickly spreading through the system. This naturally creates, in the short-run, pressure on the jobs and wages of the workers being displaced. But we know from past experience with technical change that we usually get a J-curve where, as productivity increase takes hold, it will (except in cases where macroeconomic difficulties may occur and are not addressed by macroeconomic remedies) get to increase the wages: so that a Luddite response is hardly called for. So, why has there been no such effect, at least a significant effect, in the statistics on wages for almost two decades?

I suspect that the answer lies in the intensity of displacement of unskilled labour by IT-based technical change – its potency is dramatic, as is evident from the daily experience of nearly everyone – and in the fact that it is continuous now, unlike discrete changes like the invention of the steam engine. So, before the workers get on to the rising part of the J-curve, they run into yet more such technical change, so that the working class gets to go from one declining segment of the J-curve to another, to yet another. The pressure on wages gets to be relentless, lasting over longer periods than in earlier experience with unskilled-labour-saving technical change. But this technical change, which proceeds like a tsunami, has little to do with Globalization.