Development with and beyond the market: in search of economically rational alternatives to neo-liberalism

Michael Burgess
University of Wollongong


This paper is posted at Research Online.
NOTE

This online version of the thesis may have different page formatting and pagination from the paper copy held in the University of Wollongong Library.

UNIVERSITY OF WOLLONGONG

COPYRIGHT WARNING

You may print or download ONE copy of this document for the purpose of your own research or study. The University does not authorise you to copy, communicate or otherwise make available electronically to any other person any copyright material contained on this site. You are reminded of the following:

Copyright owners are entitled to take legal action against persons who infringe their copyright. A reproduction of material that is protected by copyright may be a copyright infringement. A court may impose penalties and award damages in relation to offences and infringements relating to copyright material. Higher penalties may apply, and higher damages may be awarded, for offences and infringements involving the conversion of material into digital or electronic form.
Chapter 5

International Trade and Globalisation

Introduction

Throughout the developing world factors such as increasing literacy and access to sources of mass communication (television, etc.), the end of the Cold War, and the move towards democracy have fuelled expectations about rises in living standards. In the attempt to satisfy the growing expectations of their populations, governments have increasingly sought to follow in the export-oriented footsteps of the NICs. The discussion in the previous two chapters suggests that this approach is to be encouraged. As long as they invest sufficient resources in developing the capabilities, infrastructure and institutional arrangements required to take advantage of technologies and expertise developed elsewhere, late industrialising economies can obtain significant benefits from trade.

The growing popularity of export-oriented, growth development strategies has ensured, however, that much greater competition currently exists for access to affluent markets than was the case when these countries, with their relatively small populations, started their development push. If other countries are to enjoy similar success, it is imperative that the world economy grows strongly and that further progress is made in lowering trade barriers in more affluent economies. Without this, not only will living standards rise more slowly than otherwise, but unmet expectations could generate significant social unrest.

According to the majority of economists, the good news for developing countries is that developed countries have a strong vested interest in continuing to lower any barriers they have in place against the goods and services of low-wage economies. They argue that trade liberalisation conveys benefits all round, as it allows individual countries to further specialise in those areas in which they have a comparative advantage and, as a consequence, also results in an acceleration in the rate of world economic growth.¹ The bad news for

these countries is that, despite some progress, many trade barriers remain and some new ones have been introduced. As the recent meeting of the World Trade Organisation in Seattle illustrated, further progress could also be hard to come by as many in the developed world simply do not believe the assurances of economists. For many, globalisation is a process dominated by large corporations, and is, among other things, undermining national sovereignty and resulting in increasing unemployment, inequality and environmental destruction.

Many workers in the developed world are especially concerned by the threat posed to their living standards and working conditions by increasing competition from workers in low-wage economies. In fact, such competition is already widely claimed to be a primary cause

---


2 For the views of some of those who led the protests against the WTO (World Trade Organisation) at the recent trade talks in Seattle see the following web sites: for the site of the local organisers of the protest see www.seattlewto.org; for the web site of a coalition of activists opposed to globalisation and the WTO see www.turnpoint.org. The latter, among other things, published a series of ads in the New York Times both prior to the WTO summit and subsequent to it critical of such factors as international trade, globalisation and the commercialisation and modernisation of agriculture.

of unemployment, de-industrialisation, slow wage growth and growing inequality. According to a major report on the future of trade unions by Australia's Evatt Foundation, highly visible examples of the threat posed by such trade can be found when advanced countries share a common border with less advanced ones, as in the case of the US and Mexico. It notes that the maquiladora regions of Mexico have grown from 65 manufacturing plants employing 22,000 workers in 1970 to 1700 plants employing 400-500,000 workers in 1991. In a similar vein, one-time independent U.S. presidential candidate, Ross Perot criticised the NAFTA trade agreement between the United States, Canada, and Mexico by referring to the 'giant sucking sound' that would be made as jobs moved southwards into Mexico.

Because the trade policies of developed countries have at least as much bearing on the growth prospects of developing countries as domestic factors, this chapter explores whether these concerns have any basis in reality. Also explored are some more general issues relating to globalisation. Contrary to the impression given by economists such as Paul Krugman and many financial commentators in the media, critics of neo-liberal economic policies are not the only ones promoting misconceptions about globalisation. Actors on all sides of the debate have increasing cited imperatives associated with globalisation as a


justification for the policies they support and, in the case of the business community, to gain concessions from governments. Many also exaggerate the extent to which the changes taking place in the world economy have undermined the ability of governments to control their own destinies. As shown, such perspectives not only encourage misguided policies, they also ensure that discussions on the options open to both developing and developed countries take place within an increasingly narrow frame of reference.

1. Globalisation in Perspective

1.1 The Neo-Liberal View of Globalisation

Supporters of neo-liberal economic policies often represent the globalisation debate as a conflict between 'progressive internationalism' and 'nostalgic economic nationalism'. That is, a conflict between those who are embracing the technological changes which are creating a globalised world economy, whether one is ready for it or not, and those who would seek to remain attached to an increasingly obsolescent nation state. Such representations are highly misleading. Rather than emphasise narrow nationalistic responses to the changes unfolding in the world economy, many critics of neo-liberal economic policies stress the importance of international initiatives such as a tax on international financial transactions to bring greater stability to the international economy.

Many critics of neo-liberal economic policies also stress the importance of incorporating basic labour rights clauses into international agreements such as the World Trade Organisation Charter. As the current Australian Labor Party's Shadow Minister for Finance, Lindsay Tanner argues, phenomena such as the torture and imprisonment of trade unionists and child labour should be seen for what they are - producer subsidies which have the same

7 For the views of someone who argues that the influence of governments is being undermined but who sees this as a good thing see Ohmae, K. 1995. The End of the Nation State. Harper Collins, London.


effect as tariffs and bounties. Consequently,

If developed nations are obliged to relinquish their protective mechanisms they are entitled to ask developing nations to do likewise, particularly those mechanisms which are morally repugnant. The argument that developing countries are going through the industrialisation process in the same way that western nations did and should therefore be permitted to commit similar outrages against human rights in the process is entirely specious. Developing nations are not industrialising with the spinning jenny and cotton gin. In most cases they have access to some form of late twentieth century technology. It is therefore only reasonable that they should be expected to conform to some basic late twentieth century values, such as abhorrence of slavery and torture. Even renowned advocates of free trade such as Jagdish Bhagwati support this approach.  

In John Quiggin’s opinion another reason why it is misleading to represent neo-liberal supporters of globalisation as ‘progressive internationalists’ and their opponents as ‘nostalgic economic nationalists’ is that the former’s views on international legalisation and the exercise of power by international institutions such as the United Nations are often similar to those of the more xenophobic sections of western societies:

Consider, for example, proposals to enhance the power of the United Nations by giving it some power to levy taxation on seabed mining or international financial transactions. It is hard to think of a more natural response to the supposed obsolescence of national boundaries. Yet any such proposal will see soi-disant supporters of globalisation joining Pauline Hanson and the black helicopter brigade in condemnation of ‘world government.’

Quiggin observes that the same pattern can be seen at work in the discussions on the European Union, albeit with more complications. The British union movement, which is often represented as being narrow-minded and parochial, has been strongly supportive of the European Union and (given the attitude of both the Blair government and the Conservative party) views the European Social Charter as its best option to protect workers’ rights. In contrast, in matters such as discussions on the European Monetary Union, strong advocates of economic reform and globalisation such as members of the British Conservative Party have ‘lined up with xenophobes such as the French National Front to defend national sovereignty.’

10 Tanner, op. cit., pp. 115-6.


12 Ibid.
As Quiggin argues, all this indicates that many supporters of free market reform do not so much as want 'one world, ready or not' but rather a global economic system in which capital is allowed to move freely around the world and governments and trade unions are confined within national boundaries. In this highly selective version of globalisation international co-operation is frowned upon 'except where it takes the form, as in GATT or the now aborted Multilateral Agreement on Investment, of governments agreeing not to do things.' As discussed in the previous chapter, such a one-sided approach to globalisation is already creating major problems for the world economy. So much so, in fact, that prominent economists such as Joseph Stiglitz (the current senior vice-president and chief economist of the World Bank) are now forcibly arguing the case for some form of collective action to be taken to bring greater stability to the international financial system.

1.2 The Not So Global Economy

In support of their view that factors such as technological change and economic liberalisation are rapidly transforming the world economy and greatly undermining the power of the nation state, many writers on globalisation cite, among other things, statistics which show that trade is now growing at a much faster rate than GDP. On the surface, the evidence is compelling. In fact, if conventional trade statistics are to believed (see table 5.1), the importance of trade tripled in Western Europe and almost tripled in the United States between 1950 and 1992.

13 Ibid.

Table 5.1: Merchandise Exports as a Percentage of GDP

<table>
<thead>
<tr>
<th>Year</th>
<th>Percentage of GDP</th>
</tr>
</thead>
<tbody>
<tr>
<td>1950</td>
<td>1.2%</td>
</tr>
<tr>
<td>1960</td>
<td>2.1%</td>
</tr>
<tr>
<td>1970</td>
<td>3.8%</td>
</tr>
<tr>
<td>1980</td>
<td>5.5%</td>
</tr>
<tr>
<td>1990</td>
<td>7.2%</td>
</tr>
</tbody>
</table>


One problem with the use of such statistics is that they are measured in constant prices and assume that the price of exports has risen at the same rate as the economy as a whole. That is, they simply compare the volume growth of trade relative to the volume growth of production overall and do no take into account differences in productivity and price growth between the export sector and the rest of the economy. To illustrate the limitations of this approach, Andrew Glyn refers to OECD statistics for the 15 countries of the European Union for the 1950-94 period. In this period, the volume of exports grew at 5.7 percent a year while GDP only grew at 3.2 percent a year. However, because labour productivity growth was significantly higher in the export sector than the economy as a whole, at least two thirds of this difference was offset by slower growth in the price of exports.

A more accurate measure of the export sector’s importance to an economy is its share of output at current prices. As table 5.2 illustrates, when this is done, a less dramatic picture emerges of the extent to which trade is causing economies to become more integrated. In fact, not only is the trend towards the export sector playing a more significant role in the economy less pronounced, it has also weakened significantly. This weakening is partly the result of cyclical factors, in particular the fact that in the early 1970s and 1980s OECD


16 Between 1960-94 the deflator for exports rose 4.3 percent a year while the GDP deflator rose 6.0 percent a year (Ibid.).
countries exported more to pay for the increased price of oil.\textsuperscript{17} It is also the result of the gradual shift that has occurred in the OECD countries away from manufacturing in favour of the less trade-intensive service sector.\textsuperscript{18}

Table 5.2: Exports as a Percentage of GDP, 1950-1994

\textit{Please see print copy for image}


Other factors that are ignored or played down in much of the literature on globalisation include the reality that 60 percent of OECD workers are employed in sectors which are almost completely insulated from foreign competition. These sectors are community, social and personal services, construction and utilities, and wholesale and retail trade.\textsuperscript{19} Trade, investment and financial flows also still remain very much concentrated in Europe, Japan and the United States. This triad collectively has the capacity to co-ordinate policy in such a way as to exert a good deal of influence over the way the world economy operates.\textsuperscript{20}

As regards multinational corporations, they are still generally far from being the transnational and footloose entities they are often made out to be. Some factors such as the

\textsuperscript{17} Ibid.

\textsuperscript{18} Ibid.

\textsuperscript{19} Ibid.

patterns of sales and production do, it is true, fit in with the transnational image often presented of multinational corporations. However, as Linda Weiss points out, when it comes to key criteria such as the share of assets, ownership, management, employment, and R and D, the findings of several studies clearly indicate that the home base still generally exerts by far the dominant influence:

Especially important is the finding that most firms concentrate their most important value-adding activities at home, thus ensuring a strong contribution to the nation’s standard of living. According to existing estimates, the extent of value-added being produced at home is in the range of 70-75 percent. Overall, the studies conclude that most MNCs are national firms which operate internationally while retaining home base.

While multinational corporations do undoubtedly exercise undue influence over economic policy, this often has far more to do with the policy failures of governments than it has with a structural shift in power away from the state in favour of big business. In June 1997, for example, the Prime Minister of Australia, John Howard backed down on his plan to cut car tariffs to five percent. This was in response to pressure from car multinationals which threatened to pull out their investments unless tariffs were frozen at 15 percent or they were provided with a $1.8 billion public subsidy.

The discussion in the previous two chapters suggests that carefully targeted state support for emerging industries that show promise and generate significant externalities is often warranted. Such support, though, should be based on a careful evaluation of the costs and benefits and not influenced by the argument that dynamics associated with globalisation make it imperative that governments increase their assistance to business. In the following section this argument is shown to have little theoretical and empirical basis. As far as established industries such as the car industry is concerned, the social and economic opportunity costs of business support in such areas arguably often well outweigh the benefits. In fact, the total value of subsidies provided in Australia between 1968 and 1992 to

---


22 Ibid., p. 185.

the car and clothing industries alone was approximately $150 billion.\textsuperscript{24} Currently the overall costs of business support from the various states, territories, and local governments are approximately 6 to 7 billion dollars a year.\textsuperscript{25} The Commonwealth also provides significant support to industry. In 1994-5 this support, which is mainly in the form of border and domestic market protection measures, was estimated to amount to $9.9 billion.\textsuperscript{26}

Much of the support that has been given to industry over the years has generally been in an ad hoc fashion, with little thought to the overall benefit of the national economy.\textsuperscript{27} A good deal of the assistance provided to industry by the various states and territories is simply the product of a destructive cycle of competitive bidding between these actors for investment that would take place anyway.\textsuperscript{28} Another fact which highlights the lack of thought generally given to industry assistance in Australia is that those sectors which have been provided with the highest level of protection and public subsidisation (e.g. the automobile and clothing industries) have also been those where employment has declined the most.\textsuperscript{29}

Given these realities, it seems reasonable to assume that a significant reallocation of resources away from business welfare in areas such as the car and textile industries to areas

\textsuperscript{24}Ibid., pp. 60-61.

\textsuperscript{25}The latest comprehensive survey of state assistance to industry is that by the Industry Commission. According to the Commission, spending by the states on various forms of assistance to industry was $2.5 billion in 1994-5. This figure, however, does not include payroll tax concessions which the commission estimated to be $3.2 billion in the 1994-5 period. On the basis of this report, and their examination of recent state budget papers, the authors of a series of special reports by the Sydney Morning Herald on business welfare have concluded that the total current state assistance to business is $6-7 billion a year. See Sydney Morning Herald, 6/12/99, pp. 1 & 4.; Sydney Morning Herald, 7/12/99, pp. 1 & 4. See also Industry Commission, 1996. State, Territory and Local Government Assistance to Industry. AGPS, Canberra, 29th October, p. xxvi.

\textsuperscript{26}Industry Commission, op. cit., p. xxvi.

\textsuperscript{27}Unlike the case of the social welfare sector where mutual obligation is increasingly stressed, few constraints are placed on business recipients of welfare. On this and other issues relating to the ad-hoc and generally unproductive nature of business welfare in Australia see Industry Commission, op. cit., pp. xxv-xxxvii; Sydney Morning Herald, 6/12/99, pp. 1 & 4.; Sydney Morning Herald, 7/12/99, pp. 1 & 4; Latham, op. cit., ch. 8.

\textsuperscript{28}On this see Industry Commission, op. cit., pp. xxvii-xxix.

\textsuperscript{29}Latham, op. cit., p. 60.
where current resource allocation is sub-optimal would (at least when combined with an increase in taxation\textsuperscript{30}) be both socially and economically beneficial. These areas arguably include education, research and development, labour market programmes,\textsuperscript{31} investment in public transport, roads and other infrastructure,\textsuperscript{32} migrant support\textsuperscript{33} and early intervention initiatives in the area of child education, child abuse and neglect, drug addiction and mental health. Apart from anything else, the neglect of such areas generates significant direct long-term economic costs (costs associated with crime, long-term state support for the mentally ill and victims of child abuse and neglect, etc.) which are likely to well outweigh any short-term savings.\textsuperscript{34}

\textsuperscript{30} Apart from generating the additional resources that are needed for spending on infrastructure and the community service sector, increased taxation results in a reduction in imports. As John Quiggin suggests, this has the same positive effect on the current account as a favourable shift in the terms of trade. In other words, this is both a more socially productive and economically efficient way of increasing, or maintaining, employment levels than tariffs or other mechanisms conventionally used such as reductions in payroll taxes and general wage subsidies. On this see Quiggin, J. 'The Real Economic Illiterates.' \textit{Australian Financial Review.} 18/9/97.

\textsuperscript{31} For a discussion on which type of labour market programs are the most effective see Martin, J. P. 1998. 'What Works Among Active Labour Market Policies: Evidence from OECD Countries' Experiences.' In Debelle, G. and Borland, J. (ed.). \textit{Unemployment and the Australian Labour Market - Proceedings of a Conference held at the H. C. Coombes Centre for Financial Studies, Kirribilli on 9-10 June 1998, AGPS, Canberra, pp. 276-302; Langmore and Quiggin, op. cit., ch. 10.

\textsuperscript{32} One study which highlights the importance of investing more resources in transport infrastructure is that by the Australian Road Research Board. This study found that traffic congestion delays are costing the nation about $5.5 billion a year. On this see Beale, B. 'We're Stuck in a $5.5bn Traffic Jam.' \textit{Sydney Morning Herald,} Monday, 29/1/96, p. 2. For a more extensive discussion on infrastructure see Dowrick, S. 1994. 'Impact of Investment on Growth: Externalities and Increasing Returns.' In EPAC, \textit{Investment for Growth - Background Paper No. 39: Papers presented at an Office of EPAC seminar held in Canberra on 23 November 1993, AGPS, Canberra, pp. 11-38; Battin, T. 1997. 'Employment Blues: What Can Be Done.' \textit{Current Affairs Bulletin} 74 (3): 4-11.

\textsuperscript{33} Since the election of the Liberal/National Party coalition government in 1993, support for migrants has been steadily reduced. This includes the introduction of lengthy waiting periods before migrants are eligible for social security and other benefits. This last policy is particularly ill-advised, given the initial difficulties even highly educated and skilled migrants experience in becoming established in a new country and gaining employment.

\textsuperscript{34} In the case of child abuse, one effective and cost-efficient initiative that could be taken to reduce this would be to increase the amount of resources currently available for marriage and human relationship education and conflict resolution. However, government spending in Australia in this area has been pathetically low. In 1993-4, for example, the Commonwealth only allocated just over $20 million to marriage counselling (Langmore and Quiggin, op. cit., pp. 129-31). Government support for initiatives in the areas of mental health and drug addiction is also very low. For a discussion on this and related issues see Langmore and Quiggin, op. cit., pp. 128-29; Burdekin, B. 1993. \textit{Report of the National Inquiry into the Human Rights of People
2. Ideologies of Globalisation

In addition to a basic failure to see through all the hype about globalisation, another reason why there is a lack of perspective in many actors' analysis of the implications of the changes taking place in the world economy is that they subscribe to some appealing but flawed notions about what governments need to do if nations are to benefit from these changes. The dangers of this are now explored.

2.1 The Notion of National Economic Competitiveness

According to many influential writers on globalisation such as Lester Thurow, the key to economic prosperity in the new global economy is national economic competitiveness. They argue that if nations are to benefit from globalisation rather than suffer from its more negative effects, governments will need to act strategically rather than simply let market forces dominate. While there are differences of opinion about the policies needed, most supporters of this perspective argue that governments in developed countries should give greater support to exporters of high-tech manufactured goods by, for example, providing them with tax breaks and subsidies and/or protection from foreign competition. Especially in the United States, the concept of managed trade has also received strong support. One outcome of this is the Clinton administration's threat to close off U.S. markets to Japanese imports if Japan does not import more from the U.S.35


Many analysts justify such views by arguing that the rapid development of East Asian economies such as Japan, South Korea, Singapore, and Taiwan is mainly the result of the willingness of their governments to ignore conventional wisdom and act strategically. As shown in the previous chapter, the success of these economies is, for a large part, the result of factors which are unique to late-industrialising societies. Consequently, their experience has little relevance to developed societies. As regards Japan, both its continuing economic problems and the continuing strength of the US economy also highlight the limitations of this line of argument.

Krugman believes that a more fundamental problem with the notion of national economic competitiveness is that no theoretical justification exists for treating the nation state as if it were a corporation competing (with or without a strategic plan) in the global marketplace. According to Krugman, the key to greater prosperity is to become more productive and not more competitive. Being especially productive in manufacturing industries has no particular value, as in developed countries such as the United States a large average productivity gain in this sector would not increase living standards as much as a smaller average productivity gain in the service sector. This is because the latter now accounts for a substantially higher proportion of employment.

From Krugman’s perspective, a country experiencing below average productivity growth should only be concerned because its living standards will not rise as fast as that of other

References:


37 Krugman, Peddling Prosperity, op. cit., p. 287.

38 Krugman, Competitiveness, op. cit. and Krugman, Peddling Prosperity, op. cit., ch. 10.
countries, and not because it will be less competitive than them. Krugman illustrates this point with examples showing how adjustments to the exchange rate and other changes compensate for changing relative productivity. For instance, if domestic wages (as measured in the domestic currency) continue to rise at a similar percentage rate to elsewhere, the domestic currency will need to be devalued to compensate for the below-average productivity performance. This does not result in an increase in the price of its imports, as the fact that other countries are more productive means that the price of the goods they produce has decreased relative to their income. Because the value of the currency in the low productive country has also declined, the price it pays will either stay the same or decrease. This country is still able to sell its goods on the international market, as the devaluation of its currency compensates for its poor productivity performance. 39

2.2 Krugman's Critique of Thurow

Krugman's line of reasoning can be questioned on the grounds that it is far too dependent on the conventional neoclassical view that all sectors of the economy should be treated equally. 40 However, Krugman backs up his theoretical arguments with trade and other statistics that strongly support his conclusions about the lack of perspective of some prominent supporters of the notion of national economic competitiveness. Indeed, with devastating effect he points out how many of the claims made by analysts such as Thurow are based on both a basic misreading of the economic data and some flawed mathematics. In one publication, for example, Thurow bases his arguments on some highly questionable statistics, including a trade deficit figure four times what it actually was. 41

Elsewhere, Thurow makes the assertion that trade has been responsible for a massive decline in middle-skill and middle-income employment in the US, and that it has also put downward pressure on the wages of middle-skill occupations:


40 As discussed in chapter 3, economists have generally ignored or dealt inadequately with, a range of factors such as knowledge spillovers which, if taken into account, could have caused them to reach significantly different conclusions on the overall consequences of state support for certain sectors of the economy.

41 Krugman, Proving My Point, op. cit.
The United States effectively enjoyed substantial economic rents in medium-skill industries that were not justified by their intrinsic skills or unique technologies. Having fully recovered from World War 2 by the early 1970s, competition with the rest of the industrial world simply eliminated the economic rents that the United States had been enjoying in the middle of its earnings distribution.\footnote{Thurow, The Future of Capitalism, \textit{op. cit.}, p. 175.}

Thurow maintains that real wages fell by six percent during the Reagan and Bush years, and in this period the United States' manufactured trade deficit was responsible for forcing a million workers out of manufacturing jobs into lower-paying service employment. He also claims that average wages in the manufacturing sector are 30 percent higher than those in the service sector.\footnote{Cited in Krugman, \textit{Competitiveness: A Dangerous Obsession, op. cit.}}

In response, Krugman argues that the one million job figure is too high, and that the difference in wage rates between the two sectors is primarily related to differences in hours worked. He also makes the point that even if these figures are taken at face value, a loss of one million jobs is still less than one percent of the total workforce. Consequently, this would reduce the average US wage rate by less than 1/100 of 30 percent (the supposed manufacturing wage premium) - that is, less than 0.3 percent, which is too small to explain the 6 percent real wage decline by a factor of 20. Or, to look at it another way, the annual wage loss from deficit-induced deindustrialisation, which Thurow clearly implies is at the heart of US economic difficulties, is, on the basis of his own numbers, roughly equal to what the US spends on health care every week.\footnote{Ibid.}

Terms of trade statistics cited by Krugman also suggest that Thurow and others have overstated the aggregate impact of trade. Between 1973 and 1991 the average annual price rise of the goods imported into the United States was 6 percent, while that of exports was 5.2 percent. Because exports accounted for an average of 10 percent of national income in this period, this 0.8 percent decline in the United States' terms of trade has been responsible, according to Krugman, for a drag in real income growth of less than 0.1 percent annually.\footnote{Krugman, \textit{Peddling Prosperity, op. cit.}, pp. 271-277}
These statistics are not adjusted to take into account hours worked. U.S. workers could have responded to a deteriorating relative position by increasing the hours they worked relative to workers in other countries. Government statistics suggest that this would appear to have been the case, but that it was not very significant given the small difference in the growth rates between command GDP per hour and real GDP. Between 1973 and 1990 command GDP per hour (the volume of goods and services the US economy can command per hour worked) only grew at an annual rate of 0.65 percent, as opposed to 1.87 percent in the 1959-73 period. Because real GDP grew at only 0.73 percent in the later period (compared to 1.85 percent in the earlier period), 91 percent of this slowdown must have been the result of domestic factors.  

2.3 Variations on a Theme

Like many economists, Krugman places too much emphasis on the role that an improved productivity performance plays in increasing living standards, at the expense of other factors. While, for example, an increase in the productivity of insurance companies or hospitals would reduce the cost of insurance or health care to consumers, far more significant gains would be obtained if the conditions that generated the need for such expenditure in the first place (social disadvantage, crime, poor driving, unhealthy diet and pollution, etc.) were improved. Despite this, his central point is essentially a valid one, which is that too much emphasis is often placed on the importance of being competitive at the expense of broader issues relating to the general health of the economy.

Contrary, however, to the impression given by Krugman, it is not only interventionists such as Thurow and Robert Reich, and politicians such as Bill Clinton, who are guilty of treating national economies as if they were corporations fighting to obtain greater market share. In Australia, at least, right-wing economists (such as Helen Hughes), sections of the bureaucracy, 47 right-wing media commentators (such as Alan Woods), conservative politicians, and members of the business community have justified a wide range of

46 Krugman, Competitiveness: A Dangerous Obsession, op. cit.

economic reforms (often citing in support some highly dubious statistics on comparative living standards\(^{48}\)) by arguing that they are necessary if we are to compete in the new global economy, or more specifically, if we are to be competitive in Asia.\(^{49}\) Some of these reforms might be more difficult to defend if the rhetoric used were merely consistent with mainstream economic theory; that is, more along the lines that if these reforms were introduced gross national income might grow slightly more rapidly than otherwise.

To illustrate how such rhetoric can limit debate on options open to societies, imagine what the response would be to a proposal by a government or the trade union movement to increase the average annual holiday period by a week or two, or to put in place an eight day fortnight of eight hour days. Such a proposal would inevitably be greeted with a barrage of criticism by almost all of the business community and by many other actors on the grounds

---

\(^{48}\) To gain support for their view, many advocates of economic reform have often greatly exaggerated the relative decline of living standards in Australia. A case in point is the Industry Commission's (IC) annual submission to the Treasurer in September 1991. In this submission, the IC argued that while Japan's US dollar per capita income was the same as Australia's in 1980 it was 66 percent higher by 1989. However, as Dowrick points out, such comparisons are often misleading as they are insensitive to movements in exchange rates. In this particular case, when income comparisons are made on the basis of purchasing power parities, the 1989 income gap between the two countries is approximately only a quarter of that suggested by the Industry Commission. In addition, the average working week in Japan was approximately one-third higher than Australia's (Dowrick, S. 1993. 'Australia's Long-Run Macroeconomic Performance.' In King and Lloyd, op. cit., pp. 236-257).


\(^{49}\) In fact, as Quiggin points out by the mid-1980s an alarmist tone had started to dominate discussions on economic reform, a common theme being that in its absence Australians were destined to become the 'Poor White Trash of Asia' (Quiggin, Great Expectations, op. cit, p. 14.). See, for example, Scutt, J. (ed.). 1985. Poor Nation of the Pacific: Australia's Future? Allen and Unwin, Sydney; Duncan, T and Fogarty, J. 1984. Australia and Argentina: On Parallel Paths. Melbourne University Press, Melbourne; Stone. J. '1929 and All That....' Australian Economic Review 3: 18-31; Hughes, H. 1985. 'Australia and the World Environment – The Dynamics of International Competition and Wealth Creation.' In Scutt, op. cit.

The pessimistic views of the Australian economy's prospects, if drastic changes were not introduced, were reinforced by critical comments made by some Asian leaders. Singapore's Lee Kuan Yew, for example, referred to Australia as a 'newly declining economy' (Reported on ABC news radio 2/3/96).
that the Australian economy would be less competitive than it already is. In reality, the only outcome of such initiatives would be a relatively small percentage drop in average income to reflect the relatively small percentage drop in average hours worked (plus any transaction and other costs and less any benefits obtained from a happier and less stressed workforce). If wages were not cut directly (or indirectly by lower pay rises in the future) to reflect this, the dollar would drop in value relative to other currencies, and the country’s exports would still be competitive. In other words, the only issue that the Australian people need consider is whether they value increased leisure and more time with family and friends sufficiently to accept slightly lower living standards.

In developing countries specifically, the implication of this line of analysis is that decisions such as whether it would be wise to allocate more resources towards meeting the basic needs of the population or to supporting exporters need to be based on a careful evaluation of the costs and benefits. They should not be influenced by the arguments that such policies should either be rejected (such as in the case of a proposed increase in basic needs spending) because they will make the nation less competitive or embraced (such as in the case of proposed additional support for exporters) because they will make the nation more competitive.

3. Trade with Low-Wage Economies

As noted, for many actors in developed countries, their greatest fears about globalisation are the potential consequences for their living standards and employment opportunities of increasing competition from workers in low-wage economies. At an aggregate level, the volume of goods and services exported by low-wage economies to high-wage ones is still far too small for it to have the type of impact many fear. In 1980, only 2.4 percent of the manufactured goods consumed in the European Community, United States, and Japan came from the developing world. By 1988 this had risen to just 3.1 percent.\(^{50}\) In the United States, imports from low-wage economies (defined as ones paying less than half the average U.S. wage rate) have hardly increased over time, rising from approximately 2 percent of

---

U.S. GDP in 1960 to approximately 2.7 percent in 1990.\textsuperscript{51}

Some critics of conventional wisdom concede that such statistics clearly indicate that trade with low-wage economies cannot be having too much of an impact on overall wage or employment growth. However, they also argue that conventional trade studies are based on an outdated view of comparative advantage and that this causes them to greatly underestimate the distributional consequences of such trade.\textsuperscript{52} To determine whether this perspective has any validity, the rest of this chapter examines the work of Adrian Wood, who is the author of the most systematic study on this issue.

3.1 Woods' Thesis

According to Wood, the traditional neoclassical economic view that developed countries should specialise in capital-intensive goods is flawed, largely because, as a result of the mobility of financial capital, interest rates and profits are essentially the same in developed economies as in developing ones. Because capital goods such as machinery can move relatively easily around the world, or in the case of buildings, be constructed anywhere within a year or two, this means that the main barrier to the development of capital-intensive industries in developing countries is their relative lack of skill. The second most important difference between developed and developing countries is the greater availability of infrastructural capital in the former.\textsuperscript{53} Both these variables have strong positive externalities associated with them. The greater density of skills that exists in developed countries generates positive learning externalities, the gains from which are reinforced by the greater availability of infrastructure. These factors ensure that skilled personnel can earn more in the developed world than in the developing world and (in addition to family and

\textsuperscript{51} Krugman, Peddling Prosperity, op. cit., pp. 146-148.


\textsuperscript{53} Wood, North-South Trade, op. cit., p. 5.
Wood argues that one reason why most studies have failed to recognise the importance of skill relative to capital is that many skill-intensive industries are also capital-intensive, while many industries requiring relatively low levels of skill also have relatively low capital requirements. He suggests too, that the conventional method of measuring capital intensity by determining the capital/labour ratio is flawed, and what should be measured is the capital/output ratio. Sectors with higher average wages tend to have higher capital/labour ratios, as they have fewer workers per unit value of output. Consequently, in a situation where the capital/labour ratio is comparatively high the capital/output ratio could still be comparatively low because of the high cost of skilled labour. This means that a rise in the real interest rate could lower rather than raise the relative price of the output of a sector with a higher capital to labour ratio. This would occur if the sector had a lower capital to output ratio because it was also much more skill-intensive.

3.2 Consequences for Unemployment and Inequality

Wood concludes that if comparative advantage is determined by the availability of skill rather than capital, an expansion of trade with developing countries is unlikely to drive down average real wages in the developed world or to raise the share of profits at the expense of labour. In fact, because trade allows countries to specialise in goods they have a comparative advantage in, average incomes are likely to significantly increase. The main concern is that the costs and benefits associated with any increase in trade are likely to be apportioned more unevenly. Increased competition from low-skilled economies will increase unemployment among basically skilled workers in developed economies and put a downward pressure on the wages of such workers still in employment. At the same time, an upward pressure is put on the wages of more highly skilled workers, whose bargaining position increases as a result of the extra employment opportunities created by trading with countries whose comparative advantage does not lie in the more highly skilled areas of

54 Ibid., p. 55.

55 Ibid., pp. 74-79.

56 Ibid., p. 5.
In support of his conclusions, Wood cites evidence of a trend for wage differentials between skill levels to widen during the 1980s, reversing the movement towards more equality. In contrast to the situation in the US, this trend has been resisted somewhat in Europe by the 'power and egalitarianism' of labour unions and by higher minimum wages and welfare payments which ensure that people are less willing to accept low-paid jobs. The downside of these policies for Europe (and Australia) are higher levels of unemployment among unskilled workers than in the US, and shortages of skilled labour. As for unemployment, Wood argues that conventional analysis has grossly underestimated the loss of basic-skilled jobs from high-wage economies to low-wage economies. Based on a mixture of calculation and guesswork, he estimates that between 1960 and 1990 trade with the South reduced the demand in the North for basically-skilled labour relative to skilled labour by around 20 percent, 70 percent of which occurred during the 1980s. This means that trade-related job losses in the basically-skilled group has been approximately 10 times greater than generally assumed.

Wood cites two main reasons why the impact of North/South trade has been underestimated to such an extent – the first of which is that conventional methods are based on the view that imports from the South of manufactured goods compete with identical goods made in the North. The assumption is that 'their labour content can be estimated from data on

---

57 Ibid., pp. 1-26.

58 Ibid., pp. 15-18.

59 For a discussion on how the actions of governments and unions in Australia have prevented the wages of low-income earners from falling further behind that of higher income earners see Gregory, R. G. and Woodbridge, G. L. 1993. 'Economic Rationalism and the Earnings Dispersion.' In King, S. and Lloyd, P. (eds.). Economic Rationalism: Dead End or Way Forward. Allen and Unwin, Sydney, pp. 220-231.


61 Which he acknowledges (ibid., p. 11) is subject to a wide range of error of approximately plus or minus 8 percentage points.

62 Ibid., pp. 10-11.
Northern industries that produce goods in the same statistical categories as the imports. In reality, firms in the North no longer manufacture many of the labour-intensive items imported from the South:

As a result, the usual method of calculation, using actual Northern input coefficients in industries now producing more skill-intensive items, gives much too low an estimate of the unskilled labour content of these imports. The extent to which trade with the South reduces the relative demand for unskilled labour is thus greatly underestimated.

Wood also argues that most analysts have failed to take into account the jobs that are lost when increased competition from low-wage economies induces labour-saving technical progress in many industries.

3.3 Alternative Explanations

Alternative reasons given for rising inequality and unemployment within developed countries include the impact of right-wing economic policies (such as tax cuts favouring high-income earners and cuts to welfare spending), technological change, and North-North trade. Wood cites evidence to suggest that, while right-wing economic policies did help widen skill differentials in wages in a number of countries (especially in the US), there must also have been more fundamental factors at work. Among other things, this is because 'skill differentials in unemployment and vacancy rates widened, even when wage differentials did not, indicating a more basic shift in the balance between relative demand and relative supply.'

Wood also notes that exports from developing countries accelerated in the 1980s, which is when the widening of skill differentials started to occur; that the magnitude of both sets of changes is similar; and that the position of unskilled workers apparently deteriorated the most in countries which import the largest amount of goods from developing countries.

---

63 Ibid., p. 9.
64 Ibid., p. 9.
65 Ibid., pp. 16-17.
66 Ibid., p. 16.
Wood considers that North/North trade is unlikely to have been a major contributor as 'the differences in the skill intensity of trade flows among developed countries are much smaller than those of North-South trade flows.' He also argues that trade arising from intra-North differences in skill intensity cannot explain why skill differentials in all developed economies moved in the same direction.

According to many analysts, technological change and not trade is the main reason why unemployment and inequality has risen in developed countries in recent decades. Among other things, it is argued that the relative income of those who are trained to use technology increases as technology becomes more sophisticated. Wood acknowledges that the evidence is not clear enough to discount the possibility that technological change might have been as important or more important than North-South trade. He suggests, however, that this is unlikely, given that new technologies also displace skilled workers, and that the underlying cause behind technological change might still be defensive expenditure in the face of threats from the South. He also argues that the 'new technology' explanation cannot easily be reconciled with the slowdown of productivity growth that has occurred in recent decades. His conclusion is that the evidence is 'consistent with the view that trade with the South had a larger role, but leaves open the possibility that new technology was important.'

---

^67 Ibid.

^68 Ibid. pp. 6 and 199-200.


^70 Wood, North-South Trade, op. cit., pp. 16-17.


^72 Wood, North-South Trade, op. cit., p. 17.
3.4 Evaluating Wood's Thesis

A potential problem with Wood's analysis is that, while in his model comparative advantage is increasingly determined by skill and not capital, the assumptions underpinning it are still essentially the same as those that support more conventional neoclassical trade models. He assumes, among other things, that increasing returns to scale do not exist, that technological change is independent of capital accumulation and that the information environment in which market agents operate is a rich one. These assumptions were shown in chapter 3 to be problematical.

In the present context, the mobility of capital is restricted by a number of factors. Many investors still have a home country bias and, with the exception of some countries such as Australia, domestic savings still largely finance domestic investment. Market imperfections in financial markets also ensure that price convergence is still far from complete in many areas; a case in point is the large interest rate differentials that can be found in domestic retail markets. Investors are also more able to obtain the information necessary to make an educated judgement about a firm's prospects (especially small and medium firms) if it is local. While some of the above factors might become less of an issue as individuals and institutions adapt to the global economy, other factors limit the mobility of capital. Natural resources such as natural gas or hydroelectricity are costly to trade, and have a strong locational pull for certain industries. Transport costs also mean that many intermediate goods are not readily tradable.

---


74 For example, interest rate differentials are still very large in retail markets. A major reason for this is the absence of foreign banks and institutions in domestic retail markets (see Ibid.). This is despite the removal in many countries of many of the constraints that existed on setting up bank branches.


Wood acknowledges that his skill-driven model of comparative advantage is also open to some of the same criticisms that have been made of more conventional trade models, and that these factors could have an important bearing on North/North trade. However, as he also points out, they are relatively insignificant when compared to the differences in factor proportions (capital, labour, skill) that drive trade between developed and developing countries.  

3.5 The Disappearing Middle

In Wood's model the trend is for the wage gaps between the various categories of skilled and basically skilled workers to gradually widen (that is, an 'expanding universe'-type wage dispersion). In contrast, other analysts argue that the main dynamic at work within labour markets in developed countries is a 'disappearing middle' phenomenon. They suggest that a large proportion of the jobs that have been lost in recent times have been middle-income ones, while most of the new jobs that have been generated have been either low paying or high paying ones. However, in Australia (as an EPAC study points out) the 'disappearing middle' effect is somewhat of a statistical creation. Most studies calculate wage distribution by reference to the median wage and fail to take into account the fact that it moves over time due to compositional changes in the workforce such as increases in part-time work and women in the workforce. As the study notes, an increase in the numbers of employees earning high incomes will make it appear as though the middle is disappearing out of the labour market.  

Another point to consider is that factors other than skill, such as strong labour unions, can earn workers middle income wages. This means that in economies undergoing economic liberalisation a decline in middle income jobs can occur without a decline in the supply of middle skill employment. This factor has been an important dynamic at work in the

---

77 Wood, North-South Trade, op. cit., p. 46.


80 For example, in the United States, unions in the manufacturing sector were able to obtain
United States where the 'disappearing middle' has received the most attention. In the post-war economic boom manufacturing unions were able to gain middle class wages for their employees. This was not the case in many areas of the service sector. Consequently, as manufacturing employment has shrunk as a percentage of total employment, so have middle income jobs - although, as discussed in section 2, this has not been to the extent to which Thurow claims. The employment situation has also improved significantly in recent years. A Department of Labour Study found that between 1993 and 1996, 8.5 million net new jobs had been created, most of which were full-time and in industry/occupation categories that were paying above-median wages.

3.6 Additional Problems with Wood's Model

A more serious problem with Wood's analysis is that the volume of manufactured goods exported from developing economies into developed ones simply does not seem to be large enough for it to have had as much of an impact as he suggests. The basic fact that only 20 to 30 percent of the workforce in western economies is employed in the traded goods sector also suggests that Wood's conclusions, which are based on a combination of empirical analysis and guesswork, are likely to be overestimates. Another difficulty with Wood's thesis is that the relative wages of the unskilled have also fallen in the non-traded sectors - of both developed as well as developing countries.

The most extensive research examining the impact of trade relative to technology and other factors has been undertaken in the United States. Most studies conclude that in the U.S., middle skilled wages for basically skilled workers. However, in other areas of the economy basically skilled jobs, such as those in service industries, were subject to low minimum wages. On this see Wood, North-South Trade, op. cit., p. 466.

81 Langmore and Quiggin, op. cit., p. 33.


171
trade has only been responsible for around 5 to 7 percent of the decline in manufacturing employment that has occurred in recent times. Given that manufacturing only employs around 17 percent of the workforce, this is too small a figure to have a major impact on wage differentials. As for the impact of trade on wage differentials, a study by labour economists G. Borjas, R. Freeman and L. F. Katz has found that a maximum of 15 percent of the growing wage gap between college and non-college graduates could be attributed to trade, while trade economists R. Z. Lawrence and M. J. Slaughter claim that, if anything, trade has had a positive effect on income distribution.

The relative unimportance of trade in income distribution is further illustrated by figure 5.1, which shows that the wages of the more poorly educated sections of the workforce have trended downwards against more educated workers in both the trade and non-trade sectors. Wood, it is true, argues that most studies have failed to take into account the jobs that are lost when increased competition from low-wage economies induces labour-saving technical progress in many industries in developed countries. However, for this to be significant, those industries in which developing countries have a growing share of the market should have experienced an unusually rapid increase in skill intensity as their more labour-intensive sections relocated offshore in search of lower wages. A study by Sachs and H. J. Shatz concludes that this has not occurred. More supportive of Wood's argument are several studies that found that the pace of technological change in developed countries has been particularly rapid in the production of labour-intensive products.

---


86 Lawrence, Trade, Multinationals and Labour, op. cit.


88 Sachs and Shatz, op. cit.

89 See Lawrence (Trade, Multinationals and Labour, op. cit.) for a review of this evidence.
In Australia, income differentials started to widen well before tariff cuts could be expected to have had much impact. A study by J. Fahrer and A. Pearse of Australian manufacturing employment and productivity trends also found little evidence, with the exception of the textile, clothing and footwear sector, of any correlation between trade and changes in the workforce. The highest number of job losses occurred in industries where competition from low-wage economies had been relatively minor, such as basic metal products, transport equipment and other machinery and equipment.

---

90 Gregory and Woodbridge, op. cit.

91 Fahrer, J and Pease, A. 1994. 'International Trade and the Australian Labour Market.' In Lowe and Dwyer, op. cit., pp. 177-224. While Quiggin argues that their methodology causes
The findings of studies analysing the impact of new trade arrangements such as the US-Canadian Trade Agreement and the (then) Common Market also suggest that Wood has overstated his case. The studies found that these agreements had only a minor impact compared to other factors.92 Where the Common Market is concerned, 80 percent of European executives replied in the negative when asked, in a 1993 questionnaire, whether the single market had brought noticeable benefits to their company.93 A variety of domestic and international factors were seen as being far more important. As Richard Freeman suggests, 'if changes in trade policy are not the driving force in the world economy, at least over the medium term, they are surely unlikely to be the driving force in changes in demand for less skilled labour over the same period.'94 One would also expect to find (given that migration and trade have much the same impact) that the wages of low-skilled natives would be less in places where migrants are concentrated than in other areas. A number of studies in the U.S. and elsewhere have found that this is not the case.95

3.7 The Continuing Relevance of Keynesian Economic Perspectives

For many economists and other commentators, technological change and not trade is the main cause of high unemployment (and underemployment) and the main reason why pressure has been mounting in recent decades for wage differentials to widen. In relation to income inequality, one problem with this explanation is that the income of technological professionals such as engineers and programmers has not grown as rapidly as that of corporate executives, lawyers and doctors.96 It is also difficult to see how technological change (or trade) could have caused the gap between groups of people with similar levels of

92 Freeman, Does Globalisation Threaten Low-Skilled Western Workers, op. cit.

93 Ibid.

94 Ibid.

95 For a review of this evidence see Ibid.

96 Krugman, Peddling Prosperity, op. cit., p. 149.
education such as teachers and the CEOs of large corporations to widen so markedly. In the
United States, for example, the average salary of the latter has risen from approximately 35
times that of the average manufacturing employee in 1970 to approximately 150 times as
much at the present time.97

The view that technological change is the primary cause of unemployment (and
underemployment) is also difficult to sustain. If this is the case, one would expect to find
evidence of a strong relationship between a country's level of mechanisation and
automation and its level of unemployment. Yet, as Tim Battin points out, countries which
have the highest levels of mechanisation and automation also often have some of the lowest
unemployment rates, and vice versa.98 Another reason identified by Battin for rejecting this
explanation is that rapid technological progress also occurred in the 1950s and 1960s, which
was a period of low unemployment. As Battin and other analysts such as John Langmore
and Quiggin argue all this suggests that the main cause of unemployment and a growing
inequality is not technological change or trade but rather the continuing neglect by
governments and policy elites of Keynesian economic perspectives on economic
management.99

Initially Keynesians argued that governments should intervene in their economies to
stimulate aggregate demand for all varieties of goods and services.100 Later variants of
Keynesianism stress the role of public-sector demand. With varying emphasis, governments
are urged to allocate more resources to public infrastructure development,101 including

97 Krugman, P. 1996. The Spiral of Inequality. Mother Jones, November/December,

98 Battin, op. cit.

Macmillan; Langmore and Quiggin, op. cit.


101 This conclusion is based, among other things, on the findings of a number of studies which
suggest that a strong link exists between productivity growth and government investment in
infrastructure. In the United States, for example, studies have found that publicly-owned stock
in core infrastructure areas of transport, communications and water services has had (apart
from its public benefits) important long-term spillover benefits on private sector productivity.
These studies also conclude that a decline in public investment has accounted for a significant
proportion of the decline in private sector productivity that has occurred since the early 1970s.
environmentally beneficial initiatives, and to take action to shift demand to more labour-intensive sectors of the economy. The most effective and socially beneficial option available to governments to achieve such a shift in demand is for them to significantly increase their spending in the community services sector.\textsuperscript{102} Because state spending on areas such as health and education is below that of most other developed countries, an increased allocation of resources to this sector is especially critical to Australia's future economic and social development. In addition to reducing unemployment and meeting other pressing social and environmental needs, a further advantage of this strategy is that it addresses the nation's chronic current account problems, as the increased taxation that is required to fund it would reduce the demand for imports.\textsuperscript{103}

Many commentators reject such an approach on the grounds that Keynesianism was discredited by the simultaneous occurrence of high levels of unemployment and inflation in the 1970s. As discussed in chapter 3, this view is based on a very narrow economistic interpretation of Keynesian economic thought which neglects the political and institutional dimensions of inflation and unemployment. In this world view, Keynesian economics becomes almost solely associated with 'Phillips Curve Keynesianism' and, more specifically, with the discredited assumption that stagflation was an impossibility. However, while 'Phillips Curve Keynesians' did undoubtedly lack an appropriate framework for dealing with inflation, this was not true of left-Keynesians and post-Keynesians. In fact, as long ago as the early to mid-1930s, Polish political economist Michael Kalecki and followers of Keynes such as British economist Joan Robinson warned that an economy moving towards low unemployment would experience strong inflationary pressures as a

result of the increased bargaining power of trade unions.104 Their solution to keeping inflation in check while maintaining low unemployment was to support an incomes policy, albeit one that allowed wages to rise beyond a level which was deemed to be acceptable by the business community and the majority of economists.105 To ensure a more equitable distribution of the benefits of economic growth and technological change and to provide workers with an incentive to accept lower wage rises, they also supported progressive tax reform and enhancements to the social wage.

Reducing Wages

An alternative approach to reducing unemployment favoured by supporters of free market reform is to drastically reduce real wages. In the Australian context, a 30 percent reduction in real wages is claimed to be required to reduce unemployment to a similar level to that of the United States.106 One obvious flaw with this argument is that it focuses on the cost of labour and plays down the fact that wage earners also consume. Demand for a particular commodity will generally increase when its price is reduced. However, the demand for labour is determined not simply by its price, but by the overall level of economic activity, which is strongly influenced by both the levels of employment and wages. Reducing real wages by anything approaching 30 percent would result in a large reduction in the consumption of goods and services, with serious consequences for employment.107

Even if this strategy does somehow succeed in significantly reducing unemployment, the overall consequences are still likely to be highly undesirable. In fact, as Langmore and Quiggin point out, even many of those who gain employment will experience a reduction in

104 Battin, Abandoning Keynes, op. cit., pp. 4 & 66-71.

105 As discussed below, post-Keynesians reject the simplistic neoclassical notion that high wages are the main cause of unemployment.

106 This conclusion is derived from the findings of a comparative study by Bob Gregory of real wage and employment growth in the United States and Australia. The findings of the study indicate that in the 1950s and 1960s employment and wage growth was similar in both Australia and the United States. However, in the following two decades real wages rose by about 30 percent in Australia relative to that in the United States. In this latter period, employment growth was stronger in United States (Langmore and Quiggin, op. cit., pp. 50-51).

107 Ibid., pp. 49-54.
Consider workers who experience spells of unemployment such that they are unemployed for 20 percent of their working lives, or around nine years in total. Employment growth of 10 percent might reduce unemployment by half, yielding, say, five years of extra employment, but this would be more than offset by low wages. Overall, lifetime earnings for these workers would fall by 20 percent. These losses could only be recouped by working longer hours, by taking a second job, or if other family members took paid employment.108

Advocates of a United States-style labour market approach also fail to take into account the fact that disguised unemployment is significantly higher in the U.S. than in other OECD countries because of more limited access to welfare benefits or employment insurance. In Australia, 82 percent of unemployed people obtain unemployment benefit. In the United States by contrast, only 34 percent of those recorded unemployed in labour force surveys are covered by employment insurance. A more accurate way of measuring the respective employment-generating performance of nations is to compare non-employment statistics. In 1992, the male non-employment rate in both the United States and Australia was 14 percent. This compares with 18 percent in Britain and 15 percent in EC Europe.109

Another reason why comparisons based on conventional unemployment statistics are misleading is that it would seem that the approach increasingly favoured by the United States to addressing the lack of demand for low-skilled labour has been to massively expand its prison population. In 1995, the prison population was already an incredible 1.6 million. This is double that of the previous decade, and an incarceration rate 5-10 times that of other Western developed countries.110 In the first year of this century, the figure has now gone beyond the 2 million mark. A frightening factor to consider is that over the next two decades increasing numbers of now hardened criminals will be released back into society. Another frightening factor to consider, before following any further in the footsteps of the United States, is that states such as California now spend more on prisons than they do on higher education. This is in addition to the massive social and economic costs incurred by

108 Ibid., p. 51.


110 Ibid.
society and by the victims and families of criminals as a result of this criminal justice system approach to reducing unemployment and addressing social disadvantage. 111

4. Conclusion

This chapter has highlighted several concerns with the way many actors approach the issue of globalisation. As shown, much of the literature on globalisation has exaggerated both the degree to which economies are becoming integrated as well as the extent to which the changes taking place are undermining the power of the nation state. Many supporters of economic reform have also misleadingly represented the globalisation debate as conflict between progressive internationalism and regressive economic nationalism. In reality, many (though, by no means all) critics of neo-liberal economic policies support trade liberalisation, but also emphasise the importance of complementary national and supranational initiatives such as controls of the movement of capital and basic environmental and human rights legislation. 112 In contrast, many supporters of free market reform subscribe to a far more narrow vision of globalisation in which capital is allowed to move freely around the world but governments and trade unions are confined within national boundaries. In this highly reductionistic model of globalisation, the only form of international co-operation generally favoured is that which encourages free trade.

A more specific problem identified with the approach taken to globalisation by supporters of free market reform (as well as by many of their critics) is the way certain imperatives supposedly associated with globalisation are used as an ideological tool to gain support for certain policy initiatives. As regards prominent supporters of interventionist policies such as Thurow and Reich, their conceptualisation of the nation state is essentially that of a corporation competing in the global market place. Initiatives favoured to make nations more competitive include increased state support for so-called strategic industries as well as for education and job retraining.

The strongest critic of the notion of national economic competitiveness has been Krugman, 111 Ibid.

112 See, for example, Langmore and Quiggin, op. cit., pp. 184-8; Tanner, op. cit., pp. 84-87.
who argues that it does not make any economic sense to view the nation state the same way as one would view a corporation. From his perspective, the key to greater economic prosperity is simply to become more productive. A country experiencing below average productivity growth should only be concerned because average incomes will rise more slowly than in other countries, and not because its exports will be less competitive. While all sectors of the economy are not necessarily as equal as Krugman’s model implies, his theoretical arguments are backed by trade and other statistics which, as shown, clearly demonstrate the lack of perspective of many writers on globalisation.

Apart from the danger of encouraging governments to engage in trade wars, the problem with viewing nations as if they were corporations competing with each other is that it encourages analysts to favour certain initiatives over others, without carefully examining the social and economic opportunity costs of the policies they favour. For example, one never hears arguments along the line that governments should increase their support for early intervention initiatives in the areas of child welfare, mental health and drug addition because it will result in their nations becoming more competitive. Yet, in addition to any direct benefits to the individuals involved, increased spending in these areas could well be more economically beneficial than additional resources allocated to the development of so-called strategic industries. This is because, over the medium to long term, cost savings and other gains arising from such factors as a reduction in the amount of resources societies allocate to long-term support, social workers, prisons and theft insurance are likely to significantly outweigh the initial costs involved. In Australia, such initiatives are undoubtedly likely to generate far more beneficial economic and social outcomes than the type of ad-hoc industry support introduced by various state and federal governments over the years.

Despite the impression given by Krugman, supporters of interventionist policies such as Thurow and Reich are not necessarily the ones most deserving of criticism for claiming that the policies they favour are essential if nations are to be successful in the global economy. Many economists, right-wing commentators, conservative politicians and members of the business community have justified a wide range of economic reforms on these grounds. These reforms include tax cuts for corporations and for the rich, the privatisation of public utilities, initiatives to weaken the power of unions, cuts to the public sector and social spending, and the abolition of penalty rates and even of some public holidays. Citing
globalisation as an imperative for change has often proved to be an effective strategy for these actors, as it surrounds proposed reforms with a sense of fear about what might occur if they are not introduced. However, as this chapter has shown, issues such as how long the working week should be, what rate of tax higher income earners and corporations should pay, and what proportion of national resources developing countries should allocate to meeting the basic needs of the population have relatively little to do with how globalised the world economy has become.

Trade and Low-wage Economies

For many in the developed world, their greatest fear about globalisation is the threat posed by growing competition from low-wage economies. This issue was addressed in some detail in the second half of this chapter. Because the volume of goods and services imported from these economies is still far too small for it to have much of an impact on overall wage and employment growth, the focus was on examining the merits of Wood’s claim that the main problem with conventional trade studies is that they greatly underestimate the distributional consequences of trade. In Wood’s model, it is the level of skill an economy possesses, and not the level of capital, which increasingly determines comparative advantage. Because trade allows countries to specialise in goods they have a comparative advantage in, any growth that takes place in trade between high-wage and low-wage economies increases average incomes in both sets of countries. However, because skill has grown in importance relative to capital as a determiner of comparative advantage, increasingly the costs and benefits of any growth in trade are shared out unevenly, with basically skilled workers being the losers and more highly skilled workers the winners.

In support of his arguments, Wood identified several reasons why conventional studies greatly underestimate the negative consequences of trade for basically skilled workers. While his analysis was found to be sufficiently convincing to indicate that the distributional consequences of trade are likely to be greater than conventionally assumed, several reasons were also identified why this is highly unlikely to be to the extent which he suggests. In fact, it was suggested that by far the main cause of growing inequality and high unemployment (and underemployment) has not been trade or technological change, but rather the failure of governments to adopt a more pragmatic and socially equitable approach to economic management. In particular, it has been their failure to both allocate sufficient
resources to infrastructure development and to take action to switch demand to more labour-intensive sectors of the economy, especially the community services sector.

If this analysis is correct, then, rather than generally railing against globalisation, actors concerned with issues such as inequality and unemployment need to concentrate their energies on pushing for initiatives that address the real causes of social injustice. These include progressive taxation reform, cuts to business welfare, and increased spending on infrastructure, education, health, social services and labour market programs. Because of its potential benefits to their own economies and also because of its critical importance to developing countries, they should also support further trade liberalisation, albeit trade liberalisation which takes place within a stronger framework of international rules and regulations governing such factors as child labour and the suppression of trade unions.