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WILL "LOCAL CONTENT" HELP LABOR?

=by Kent Osband=

"Local content" laws limit the amount of foreign-made goods permitted for sale within a country. Producers manufacturing more than a certain proportion of their goods abroad must either increase domestic production or reduce domestic sales. A number of countries already have local content laws; Congress is presently considering several versions of this legislation.

Local content legislation is finding enthusiastic support among some sectors of labor. This is not surprising, given the tremendous unemployment inthe U.S. and the inroads made by foreign producers in domestic markets. The UAW leadership, for example, is actively campaigning for local content restrictions on auto sales. Labor proponents claim local content laws will protect jobs, help "reindustrialize" America by encouraging foreign investment here, and strengthen organized labor by discouraging runaways and outsourcing.

Enticing it is. But can local content really help labor? There are reasons to think it cannot. Any short-term relief local content provides is likely to be minimal, while in the long-run it is likely to aggravate difficulties.

Local Content and Jobs. Curbs on foreign-built autos would undoubtedly increase U.S. auto employment in the short run. But at what cost? U.S. consumers would have to pay more for autos. Auto workers in other countries would be laid off. Their countries in turn might retaliate with new restrictions on U.S. goods. U.S. exports of food, farm machinery, aircraft, and many other products could fall. Those producers in turn could lay off more workers or hire fewer new ones, and reduce purchases of intermediate goods. The overall effect could be both higher prices and higher unemployment, in the U.S. and abroad.

The prospect of retaliation, always a danger when following protectionist policies, is magnified during economic crisis. In 1930, Congress passed the Smoot-Hawley Act, setting extremely high tariffs on imported goods. The aim, ostensibly, was to protect domestic jobs. As it turned out, other countries increased their trade barriers too, and the ensuing collapse of international trade made the depression worse. With the world economy today more interdependent than it was in 1930, a protectionist trade war would be more disastrous.

Today the world economy stands to lose even more from a protectionist trade war than it did in the 1930s. In 1980 the U.S. derived 12% of its national income from foreign trade, compared with 4% in 1930. Most countries depend on foreign trade even more. The multiplication of trade restrictions in recent years has already cost them and us deeply. Let U.S. labor press for trade negotiations to roll back restrictions, instead of advocating new ones. That way it can help itself and workers in other countries too.

Local Content and Industrial Development... Proponents of local content argue that its stimulus to industrial development will more than compensate for the loss of trade. They point to the success many other countries have had using local content laws to start new industries and get them to flourish.

However, the main U.S. industries local content advocates want to protect are **not** infant industries. Protection of the auto and steel industries, for example, would more likely retard innovation than speed it. (Besides, international experience suggests that even infant industries can develop faster and with less burden on workers' living standards through investment planning and direct subsidies than through protection.)

Take a look at steel. Formal or informal quotas on Japanese and European steel date from 1969. If we accepted local content arguments, we would expect to see more U.S. steelworkers employed, more European and Japanese firms establishing steel mills here (in order to circumvent quotas), and more innovation. Instead, steel employment is down, foreign investment is minimal, and technology on the whole is less up-to-date than it was. The extra income garnered by domestic steel producers has been invested largely in non-steel ventures. (Recall U.S. Steel's recent takeover of Marathon Oil.)

This is not to blame quotas for steel's decline. Stagnation in the rest of the economy, both at home and abroad, has cut demand for steel. An overvalued exchange rate has weakened U.S. goods vis-a-vis foreign ones. Conservative managers and shareholders have skimmed off short-term profits instead of investing. "Low-wage" foreign steel producers have undercut U.S. sellers. It is impossible to analyze all these phenomena here. Let us instead concentrate on the factor local content advocates emphasize: the competition of low-wage steel producers.

The crux of the problem is this: by world standards, U.S. wage rates in steel have come to be relatively high compared to productivity. This is true even though U.S. labor productivity in steel is among the highest in the world, and U.S. wages have risen more slowly than wages in many other countries. What has happened is that many newly-industrializing countries are catching up to developed countries' levels in steel technology faster than they are catching up in wages. The repressive, anti-labor nature of governments in many newly-industrializing countries serves to widen this gap (another reason for U.S. workers to oppose our government's support of such regimes). But to a great extent the gap is inevitable--the result of developing countries catching up in some fields faster than others.

Japan's experience illustrates both the promise and the perils of development. Twenty five years ago the combination of rapid adoption and improvement of Western technology and relatively low wages helped propel Japan into the front rank of world steel producers. Since that time Japanese wages have risen toward Western European and North American levels, and steel technology has passed on to poorer countries. Today Japanese steel producers find themselves threatened by South Korean competition, even in their home market.

According to the modern-day jingoists, the more developed countries ought to try to resist the shift at all costs. Restrict technology transfer; clamp down on trade; prop up ailing industries with tariffs and subsidies; continue to tie the prosperity of one group of countries to the restriction of others' development. But there is another way. Use trade to get cheap basic goods from other countries. Emphasize the development of high-technology industries; raise the skill levels of the workforce; improve work organization and product quality.

"Reindustrialization" doesn't require local content. What it does require is more public financing and national coordination of research and development, industrial investment, and manpower training and retraining. U.S. labor should, and has to, fight to direct research and development and industrial investments toward peaceful development instead of military build-up. It should, and has to, fight to reduce the burden of adjustment borne by workers. But it should not fight against adjustment itself.

Local Content and the Labor Movement. Whatever the "economic" merits of the case, some argue that organized labor would be slitting its own throat politically not to support local content. The basic industries that are threatened are the main strongholds of organized labor. If these industries go, organized labor goes with them.

The danger exists, to be sure. But the outcome need not be so bleak. Let us recall some U.S. labor history. In the 1920s, the C.I.O. movement brought about some needed reorientation from the A.F. of L.'s principle of craft organization. This strengthened the labor movement and enabled it to organize the growing basic industry workforce.

Today even a "basic industry" orientation is too narrow. Massive restructuring of the U.S. economy will indeed draw some resources from traditional union strongholds. But it also opens up new opportunities for organized labor to influence national and international development. It is up to labor to champion changes that benefit the masses of people. Let labor do this, and it can once again inspire and lead its own ranks, and millions of others--as it has done before. Local content is an ineffective response to U.S. labor's crisis and a retreat from its domestic and global responsibilities.

-- Kent Osband