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RE: Topic for discussion for Gereffi-Sturgeon globalization workshop.

The free-market argument favoring globalization is some variant of the following: The losers from globalization are usually believed to be developed country labor pools that are displaced by cheaper labor pools in the developing countries. But developed country company profits increase. The higher profits will be reinvested to generate new jobs.

This argument has the following theoretical flaws that need empirical analysis prior to substantiation:

(1) Higher corporate profits may not be reinvested to generate new jobs that will offer employment opportunities for those who have lost their jobs. This can happen either if the reinvestment instead creates new jobs in developing economies or if the jobs created in the developed country are not accessible by the displaced workers. For an example of the latter, if reinvestment creates jobs that require high technical skills not available with those who have lost jobs, then a “globalization-induced” divide is introduced: wage rates of uncompetitive workers in developed countries will converge towards wage rates in developing countries while wage rates of deployers of capital and owners of the relevant high skills will see their wages increase or at least remain protected. Overall, the haves will receive a greater share of the reward consisting of the transfer of the wage differential and associated second order benefits of reinvestment.

(2) The higher earnings in developing countries may mostly be spent on domestically produced goods and not on purchasing developed country goods, in which case it represents a net loss to the U.S. economy. For example, if a call center is shifted from the USA to India because of a wage differential of \$3/hr (say, \$8/hr in the USA and \$5/hr in India), and if the \$5/hr earned in India is mostly used to buy food produced domestically, there may be no gains for the US economy. Hence, the immediate net benefit to GDP for an hour of such work transferred is only \$3, which equals the corporate gain. Provided the displaced worker can generate income in an alternative job of at least \$5/hr, say, \$6/hr, there is a net gain to the economy of a larger amount, equal to \$9/hr. (this is the traditional “gains from trade” argument)

(3) Welfare transfer payments may distort incentives for reemployment, leading to a net economic loss. Suppose welfare is \$4/hr and suppose that the displaced worker chooses welfare. In that case, the private firm’s gains from trade equals \$3/hr but the economy’s gains from trade is -1 (because of the welfare payment of \$4/hr).