

Testimony on SB-04-170, Keep Jobs in Colorado (2/09/04)

Bob Powell, Ph.D., MBA
Continuous Improvement Associates

I'm a management consultant with a background of 20 or so years in the semiconductor industry in computer-aided design and product engineering. I've done studies of workforce dynamics for the EDC in Colorado Springs. Primarily, I now help organizations become more efficient and effective using a systems thinking approach. Also, I teach a class on "Systems Thinking and Problem Solving" at Colorado Technical University.

Systems thinking is seeking to understand system behavior by examining "the whole," instead of by analyzing the parts. As an example, think about the question, "Why does a bell ring?" The obvious answer is because someone strikes it. The systems thinking answer is, "A bell rings because it's designed to ring, not simply because it's struck." Most tables don't "ring like a bell" when we strike them; they go "thunk" because their structure isn't designed to ring.

For the last year I've been involved in the Greater Colorado Springs Economic Development Corporation's Manufacturing Base Restoration Initiative. I became interested in using a systems thinking perspective to understand why the U.S. is losing manufacturing and other jobs. I've come to see it as a very serious problem.

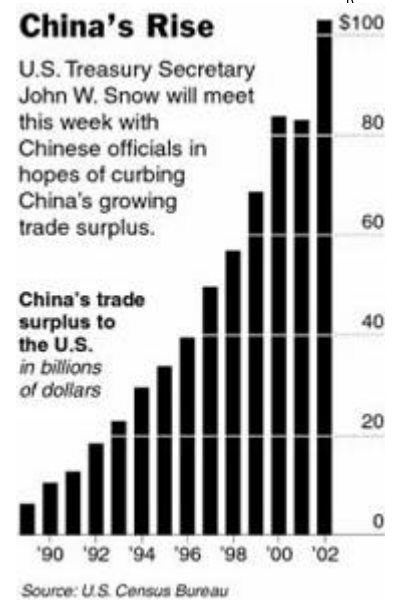
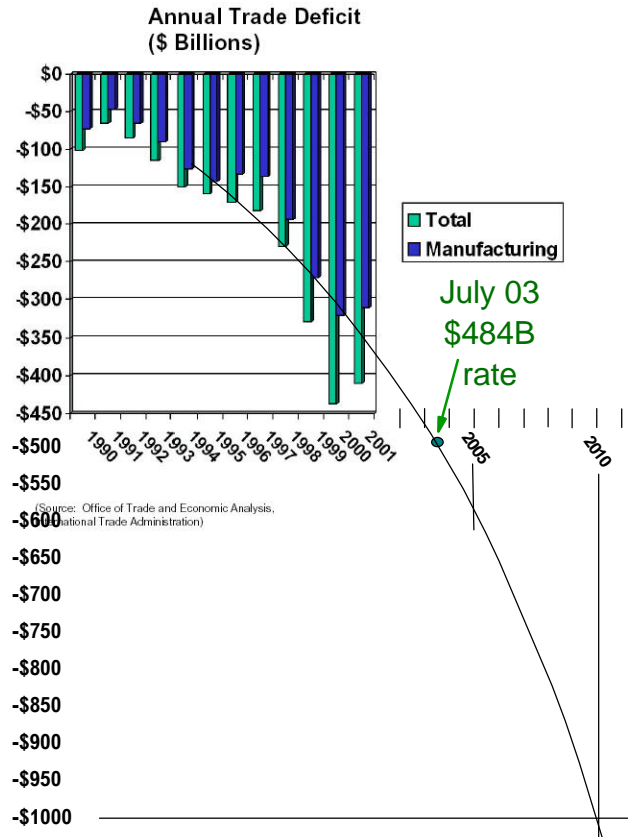
With that introduction, I heard about this bill from a story in the *Rocky Mountain News*, "Bills tie state contracts to keeping jobs in U.S." I read that Chuck Berry of CACI said that "Protectionist legislation won't keep jobs in Colorado."

But to the contrary, U.S. policy is the exact opposite of "protectionist." If it were "protectionist," we would not have exponentially increasing trade deficits with China and the world, approaching \$500 billion per year. (See charts.)

For a trade balance this negative, the opposite of "protectionism" must be the case. For it to be exponentially increasing, a reinforcing process must be driving it. U.S. policy is, in effect, "reverse protectionism" ... forcing industry and jobs out of the country. This is currently undermining U.S. economic and military security.

In fact, as I researched the issues and listed all the reasons the U.S. is losing jobs of all kinds, I found it frightening. I explain what I learned in my paper on "A Systems Thinking Perspective on Manufacturing & Trade Policy" that can be found at my web site. Last week, *IndustryWeek*, a national magazine on manufacturing, notified me they will post this paper on their site.¹

I realized that conclusions of "free trade" advocates based on the theory of "comparative advantage" are seriously flawed. That theory says, "You do what you do best and I'll do what I do best, and we'll trade products." But what's happening now is not simple "trade of products," but "transfer of the factors of production" that create the products. Not only are the requirements of the comparative advantage not met², given free migration



¹ <http://www.exponentialimprovement.com/cms/fostermfg.shtml> ; <http://www.industryweek.com/iwinprint/agenda>

² From Lester Thurow, *The Future of Capitalism* (1996, pp. 69, 70): **First**, full employment is assumed to exist. Free trade does not push anyone into unemployment. **Second**, transition costs are assumed to be zero. There is no region-, industry-, or firm-specific

of the factors of production (labor, capital, and land), they will move from the U.S. to other places, such as China, as long as they are places of greater composite attractiveness. Because world conditions do not meet the constraints of the underlying theory, this “economic migration” means that “absolute advantage” applies, not “comparative advantage.” Because China, India and other relatively undeveloped countries have a virtually inexhaustible supply of cheap labor, with many of them highly educated as well, if unchecked this “economic migration” of all kinds of will go on for decades, if not the next century.

But long before that, I believe the U.S. economy will collapse because the trade deficit, now at about 5% of GDP, will be closing on 10% of GDP in 5 or 6 years. Those now accepting the dollar in exchange for goods and services will no longer do so. Warren Buffett, also concerned with the long-term problems caused by international trade that’s “out of balance,” has proposed an Import Certificates mechanism to create balanced trade to deal with what he describes as “a shifting maze of punitive tariffs, export subsidies, quotas, dollar-locked currencies, and the like.”³ That would mean, not “free trade” or “fair trade,” but “even trade.”

Obviously companies want to move the factors of production to other countries to avoid taxes and worker protections to increase profits. But they still want to take advantage of all the U.S. government support and military that protects their property and capital and allows them to do business in this country. If companies want to move services offshore, then they should pay significantly higher taxes to pay for these protections and services. If they don’t, we’re essentially subsidizing them to outsource offshore.

Barring companies that outsource offshore from government contracts is a minimal step in stopping “reverse protectionism.” While individual company decisions may be logical, they produce behavior of the whole that is collectively insane. This should be discouraged by government, the only entity that can effectively represent the long-term interests of the country as a whole.

Therefore, I fully agree with the proposed bill and not using tax dollars to reward such behavior.

It’s not simply about “protectionism,” it’s about what we protect. “Free trade” advocates believe in protectionism for private capital and intellectual property, but unfortunately they don’t believe it’s legitimate to protect the social capital built up in the U.S. over hundreds of years. If government won’t take steps to protect it, who will?

Thank you for giving me this time to speak.

Bob Powell
2/09/04

Examples of “reverse protectionism”:

- Allowing other countries (e.g., China) to manipulate and undervalue their currencies to maintain trade advantages.
- Giving investment tax credits to companies that do not keep their complementary assets (e.g., manufacturing) in the U.S., because the nation subsidizes the innovation, but does not fully profit from the innovation.
- Not including labor⁴ and environmental⁵ standards in trade pacts creates a uneven playing field by allowing countries that do not respect labor standards burden their population and mortgage their long-term future for short-term gain.
- Trading with countries that lower taxes to the point that they mortgage their long-term future for short-term gain.
- Allowing corporations to engage in flawed transfer pricing schemes to avoid U.S. taxes.
- Allowing corporations to move headquarters out of the country to avoid U.S. taxes and yet still perform government contracts.

physical or human capital that is destroyed when workers are forced to shift between regions, industries, or firms. **Third**, returns are assumed to be everywhere equal. Each industry has the same rate of return on human or physical capital. Each firm and industry pays the same wage rate for a worker’s being willing to give up an hour of leisure. As a consequence, being forced to shift jobs doesn’t change wages very much, if at all.

³ Warren E. Buffett, “America’s Growing Trade Deficit Is Selling the Nation Out From Under Us. Here’s a Way to Fix the Problem — And We Need to Do It Now.” *FORTUNE*, 11/10/03. <http://www.fortune.com/fortune/investing/articles/0,15114,525644,00.html>.

⁴ Doing so allows countries to lower labor standards to shift the gains of trade to a relative few and shift the costs of trade (in negative impacts on health) to the many. Again, only democracies with the technical ability and financial resources can properly value and monitor public health.

⁵ The argument that countries should be free to value their own environment only holds if they are democracies with the technical ability and financial resources to properly value and monitor the environment. The environment is a public good (a commons) for which only governments can set the value, not individuals or “the market.”