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The Truth Comes Out About Offshoring

By [Paul Craig Roberts](#)

On January 6, 2004, Senator Charles Schumer (D, NY) and I scandalized the economics profession and Washington policymakers with our New York Times article, [Second Thoughts on Free Trade](#). We noted that the two conditions on which the case for free trade rests no longer exist in the present-day world and that there was no basis for the assumption that offshoring of US jobs was beneficial overall to Americans.

The Brookings Institution in Washington, D.C., organized a conference, televised by C-Span, to subject our argument to peer review, and we easily dominated the conference.

Business Week (March 22, 2004) was receptive to a column from me explaining the adverse effects of offshoring, and Tim Aepfel at the *Wall Street Journal* organized an [online debate](#) between myself and Columbia University trade theorist [Jagdish Bhagwati](#).

Aepfel hoped to test the validity of my points in the crucible of debate with a leading academic proponent of offshoring. However, Bhagwati evaded my argument and threatened to withdraw his participation if my reference to the latest work in trade theory by Ralph Gomory and William Baumol was included in the edited version of our debate in the *Wall Street Journal* (May 10, 2004). In [Global Trade and Conflicting National Interests](#) published in 2000 by the M.I.T. Press, Gomory and Baumol show that the case for free trade is a special case and had never [been one of general validity](#). Their criticism is more far-reaching than the one made by me and Senator Schumer.

Professor Bhagwati's skill in evading my argument told most people who read the edited version of our debate that he could not answer me. Obviously, all was not well with the establishment's contentment with offshoring and "globalism."

Paul Samuelson, in many respects the [dean of American economists](#), wrote an article supportive of Gomory and Baumol's work. [*Where Ricardo and Mill Rebut and Confirm Arguments of Mainstream Economists Supporting Globalization, Journal of Economic Perspectives*—Summer 2004 ([PDF](#))] But nothing happened. Economists simply closed ranks and ignored the points that I brought to their attention as well as the latest work in trade theory. Libertarian free trade ideologues got upset with me. Unable to deny that the case for free trade had lost its necessary foundations, libertarians reduced the issue to one of economic freedom and concluded that I was impure.

Since 2004 I have written a number of articles pointing out that offshoring is really labor arbitrage and that if offshoring had the mutual economic benefits associated with free trade, there would be US employment growth in export and import-competitive industries. Instead, employment in these industries has declined in the US but grown remarkably in Asia. In the 21st century the US economy has been able to create net new jobs *only* in [nontradable domestic services](#), such as waitresses and bartenders and health and social services. Moreover, the growth in productivity and GDP attributed to the US economy were inconsistent with the stagnant real incomes of Americans. Somehow productivity and GDP were growing strongly, but it wasn't showing up in the incomes of Americans.

Economists have found it difficult to think about the issues that I have raised. Economists are taught that free trade is a good thing and that anyone who disputes it is a [protectionist](#) in the pay of some industry scheming to raise prices that consumers have to pay. The notion that there could be any problem with free trade is beyond the imagination of most economists.

In addition to their unexamined commitment to free trade, economists disbelieved my analysis because they thought it was inconsistent with statistics indicating high US productivity and GDP growth. They thought GDP and productivity statistics trumped my use of job data.

All of this may be about to change. [Susan N. Houseman](#), a good but previously obscure economist with the Upjohn Institute, has discovered a problem in the statistical data that produces phantom US GDP. [Phantom GDP](#) results when cost reductions achieved by US firms shifting production offshore are miscounted as US GDP growth. Phantom productivity increases occur when gains from moving design, research and development offshore are counted as increases in US productivity. Obviously, production and productivity that take place abroad are not part of our domestic economy.

Business Week's June 18 cover story by Michael Mandel [[The Real Cost Of Offshoring](#)] explains the problem identified by Houseman. Economist Matthew J. Slaughter, a proponent of offshoring, says: **“There are potentially big implications. I worry about how pervasive this is.”** *Business Week* says the implications are big. The cover story estimates that 40% of the gain in US manufacturing output since 2003 is phantom GDP.

Most likely that estimate is low. Consider, for example, that furniture imports have doubled in the past few years (offshored production counts as imports) while US jobs in furniture manufacture have declined 21%. US statistics, however, show that US output and productivity rose even as US manufacturers closed their plants and no new investment went into the industry.

My hat is off to *Business Week*. It requires courage for a publication dependent on advertising from global corporations to tell the truth about offshoring.

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