



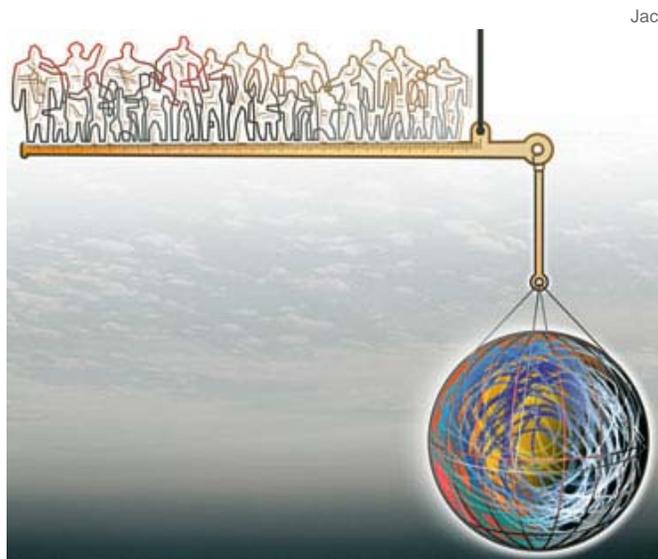
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**ECONOMICS FOCUS****Economics focus****Buying off the opposition**

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**New ideas to shore up support for open markets**[Get article background](#)

AFTER months of impasse, America's trade policy may be inching forward. As *The Economist* went to press, the Democrat-controlled Congress looked set to pass a free-trade deal with Peru. Though small beer economically, it is symbolically important. George Bush's administration hopes other bilateral deals will follow, as a new bipartisan consensus on trade develops.

Alas, that seems unlikely. Listen to the Democratic presidential candidates and it becomes clear that the Peru vote is likely to be an outlier rather than a harbinger: they all want to "revisit" existing trade deals and are against an agreement with South Korea, the biggest negotiated by the Bush team. Trade wonks reckon the Peru vote is a cynical ploy that will allow Congress to block other trade deals without being branded globophobes.

Polls suggest that voters are becoming more, not less, sceptical of trade. According to a new one by the Pew Research Centre, the share of Americans who believe that trade is good for their country has plunged from 78% in 2002 to 59%, the lowest proportion among the 47 countries included in the survey. Nor are the concerns confined to Democrats. A recent *Wall Street Journal* poll of Republicans suggested that trade sceptics outweighed trade supporters by almost two to one (59% versus 32%).

Alarmed by these trends, centrist thinkers from both parties are searching for new ways to convince Americans that turning inwards is a bad idea. The most ambitious proposals have been championed by Matthew Slaughter, a former member of Mr Bush's Council of Economic Advisers, and now a professor at Dartmouth

College. In an article earlier this year in *Foreign Affairs*, written with Kenneth Scheve of Yale University, Mr Slaughter called for a "New Deal" on globalisation.

Today's protectionist pressures, they claimed, stemmed from Americans' unhappiness over stagnant living standards. Globalisation may or may not be the cause of this stagnation, but people think it is. Thus the only way to keep trade barriers down is to boost ordinary people's incomes by cutting their taxes and raising levies on the rich. They target the payroll tax, a 15% levy on earnings up to \$97,500 which is mainly meant to fund public pensions. They want to scrap payroll taxes entirely for the poorest half of workers and lift them on richer workers. That would be a huge redistribution, worth some \$250 billion a year.

The logic of such a "New Deal" weakens on closer inspection. Economists, as Mr Slaughter admits, are unsure what role freer trade—rather than, say, technological innovation—has played in widening income inequality. And if the economic rationale is tenuous, so, too, is the political one. Even if some workers see a lower tax bill, what is to stop them still opposing freer trade?

## Help for the losers

More promising approaches concentrate on reducing the pain of economic dislocation. Making health insurance more portable is one route. Another is to overhaul the system of Trade Adjustment Assistance (TAA). Since 1962 America has offered extra unemployment benefits and training to manufacturing workers who lose their jobs because of foreign competition. The scheme is widely criticised. Its premise that involuntary job loss thanks to trade deserves more generous treatment than involuntary job loss thanks to, say, technical innovation is unfair. Its focus on extending unemployment insurance deters recipients from finding a new job. And, at less than \$1 billion a year, TAA is too small to make a political difference.

One idea is to eliminate the artificial link to trade so that all dislocated workers can benefit. Another is to refocus America's overall system of unemployment insurance away from assistance for temporary job loss and towards helping those who suffer long-term wage loss. Robert LaLonde of the University of Chicago points out that the biggest losers from structural change—whether because of trade or technology—are middle-aged workers who have had a long tenure with one employer. Workers who lose their jobs after 20 years with one firm see wage losses 30 percentage points bigger than those who have been with a firm less than a year.

Helping these workers ought to be a priority. One possibility is retraining. But Mr LaLonde points out that for many middle-aged workers even extensive investment in retraining is unlikely to yield returns that close the wage gap. Another approach is wage insurance, where the government tops up the earnings of a dislocated worker forced into a lower-paying job.

Wage insurance is not a new idea. Several economists have proposed plans that would top up half the difference between old and new wages for two years. Today's TAA includes a modest scheme for people over 50. But Mr LaLonde argues that wage insurance must last longer to be effective. Replacing half the difference in earnings for a person of 40 for two years, he points out, offsets only 5% of that worker's likely lifetime earnings loss. More generous wage insurance could be paid for by refocusing America's existing \$30 billion system of unemployment insurance. Jeffrey Kling at the Brookings Institution has proposed such a scheme (see [article](#)).

Are these ideas politically feasible? Not at the moment. The Bush team recently threatened to veto congressional Democrats' far more modest plans to expand TAA to service-sector workers whose jobs are outsourced. Under pressure from the unions, the Democrats, in turn, are loth to consider any restructuring of America's overall unemployment benefits. If America is to build a bipartisan consensus for open markets, politicians on both sides must do more to explain the benefits of a dynamic economy. They must also become less blinkered in dealing with the consequences of dislocation.

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## References

"[A New Deal for Globalisation](#)", by Kenneth Scheve and Matthew Slaughter. *Foreign Affairs*, July/August 2007

"[The Case for Wage Insurance](#)", by Robert LaLonde. Council on Foreign Relations, September 2007