

Blue-Collar Blues: Is Trade to Blame for Rising US Income Inequality?

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Over the past quarter century, output per worker in the US economy has increased significantly, yet the typical worker has seen only a modest increase in take-home pay while the richest Americans have done exceedingly well. Many link these developments to the expansion of US trade, particularly with developing countries such as India and China. Public opinion polls indicate that there is widespread anxiety about trade among American workers, and politicians are thus expressing increasing skepticism about globalization. But is trade really to blame? In this study, Lawrence explores the links between slow US real wage growth, increased earnings inequality, and trade and concludes that the latter has played only a minor role in growing income inequality and labor-market displacement in the United States.

He first deconstructs the reported gap between real blue-collar wages and labor productivity growth over the past quarter century and estimates how much of the gap is due to measurement issues and how much higher these wages might have been had the distribution of income been kept constant. He demonstrates that about 60 percent of that gap reflects measurement issues, in particular, the use of different price deflators for output and real wages and the omission of benefits in take-home pay. He also finds that an additional 10 percent can be ascribed to the relatively rapid acquisition of skills by white-collar workers.

However, he concludes that three types of increased inequality do account for about 30 percent of the gap: conventional wage inequality, which reflects an increase in the returns to skills; super rich inequality, which reflects the dramatic increase in wages of the richest Americans; and class inequality, which reflects the rising share of corporate profits in income. Lawrence considers what role trade is likely to have played for each type of inequality.

While increased trade with developing countries may have played some part in causing greater inequality in the 1980s, over the past decade the impact of such trade on inequality has been too small to show up in the wage data. To be sure, since 1990, powerful globalization forces have been operating that might have been expected to increase wage inequality. Not only have imports from developing countries increased dramatically but the relative prices of manufactured goods from these countries have declined steadily. Yet the big surprise is that wages of the least-skilled Americans—the lowest 10 percent—have kept pace with the median and, since 1999, while real wage growth in general has been sluggish, most US relative wage and compensation measures indicate little evidence of increased inequality. This is true whether workers are distinguished by skill, education, unionization, occupation, or major sectors.

Lawrence points out that some of the goods that the United States imports, even from developing countries, are quite sophisticated and produced in the United States through skill-intensive and automated methods. Though it may cause displacement and could put downward pressure on wages gener-

ally, this import competition does not increase wage inequality. A more benign view is that a significant amount of what America imports today is no longer produced domestically. Thus declining import prices simply yield consumer benefits but do not exert downward pressure on US wages nor cause dislocation of US workers.

The recent increase in US inequality, therefore, has little to do with global forces that might especially affect unskilled workers—namely, immigration and expanded trade with developing countries. Instead, the sources of increased inequality have been the increased share of profits in income, much of which could be cyclical, and the rising share of the super rich—a development in which trade is likely to have played only a small role.

Since 2000, labor's income share has fallen as wage increases have failed to match productivity growth almost across the entire spectrum of education levels. This decline could, in principle, be the result of increased trade pressures such as offshoring, which raises profits and reduces wages in part through affecting labor's bargaining power.

But there are reasons to be skeptical. First, the low labor income share in 2006 was actually similar to that in 1997, suggesting a strong cyclical component in recent performance. Second, while it is plausible that labor's bargaining power and labor rents could be reduced by the ability to offshore, there was no such decline in labor share over either the 1980s or 1990s. Third, if offshoring to developing countries were the major driver of labor's depressed share, the fall would be especially apparent in tradable goods, but recent profit growth has not been especially concentrated in manufacturing. Indeed, it has been concentrated in financial corporations. In fact, between 2000 and 2005, the share of compensation in manufacturing (or traded goods) did not decline more rapidly than in the rest of private industry, and manufacturing compensation has actually increased relatively more rapidly than compensation in general. Similarly, offshoring of services, for example, to India, has actually been much smaller than public headlines suggest and too small to account for the pervasive slow real wage growth since 2000.

Trade also does not appear to be a disproportionately important driver of the growing share of income earned by the super rich. To be sure, globalization has played some role in increasing the size of relevant markets and thus incomes of CEOs, sports stars, entertainers, and software producers. But remarkably, the share of total US profits earned abroad by US multinationals has remained fairly constant. Far more important sources of this inequality are technological changes, institutional developments such as financial deregulation, modifications in US corporate governance practices, and rising asset markets, most of which have domestic origins.

The study does not dispute the importance of growing US inequality and the need for policies to deal with it. But Lawrence provides compelling evidence that those seeking to give trade a prominent role in the explanation are looking in the wrong place. The minor role of trade suggests that any policy that focuses narrowly on trade to deal with wage inequality and job loss is likely to be ineffective. Instead, policymakers should (a) use the tax system to improve income distribution and (b) implement adjustment policies to deal more generally with worker and community dislocation.

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