Does Trade Hurt Workers?

"Are Your Wages Set in Beijing?" by Richard B. Freeman, "Income Inequality and Trade: How to Think, What to Conclude" by J. David Richardson, and "How Trade Hurt Unskilled Workers" by Adrian Wood, in *The Journal of Economic Perspectives* (Summer 1995), American Economic Assn., 2014 Broadway, Ste. 305, Nashville, Tenn. 37203-2418.

Is there a connection between the rising tide of cheap imports and the unhappy condition of less-skilled workers in the United States and Europe? American and European economists generally disagree—with each other.

In a survey of the debate, Harvard economist Freeman says that American economists—including Richardson, of Syracuse University—generally assign trade minimal blame, while European economists—such as Wood, of the University of Sussex—generally indict it.

About the plight of the less skilled, there is little debate: demand for their labor is falling. In the United States, the result has been stagnant or declining wages; in Europe, where wages are propped up by law and labor unions, the result has been rising unemployment.

Several recent studies, Freeman notes, have found that not "all that many" less-skilled American workers have lost manufacturing jobs as a result of increased trade. The reason is simple: only about 15 percent of such people are now employed in manufacturing. Most are in retail trade and services. They aren't competing with Indonesian garment workers and Chinese toy makers. Other factors—including technological change and the decline of unions—have been more important, he believes. Trade, by economists' most common method of calculation, accounts for only 10 to 20 percent of the overall fall in demand for unskilled labor.

Wood, however, maintains that this method understates trade's impact. It assumes that, say, low-tech toys imported from China displace high-tech U.S. toys. Since the high-tech toys require less labor to make, relatively few jobs are lost. But Wood argues that economists should base their job-loss estimates on the assumption that the labor-intensive low-tech toys would have been made in the United States.

Moreover, Wood says, developing countries are increasing exports of services in such "low-skill–intensive" areas as shipping, tourism, and computer keypunching. And growing trade stimulates technological progress throughout developed economies, encouraging all firms to reduce unskilled labor. In the developed countries, he believes, trade and trade-induced technological change account for about half of the decline in demand for unskilled labor.

Wood, like most economists, does not favor protectionist policies. Better, he writes, for government to help the unskilled obtain education and training. He also favors government subsidies of various sorts to ease the plight of unskilled workers on both sides of the Atlantic.

The Air Bag Peril

"Are Drivers of Air-Bag Equipped Cars More Aggressive? A Test of the Offsetting Behavior Hypothesis" by Steven Peterson, George Hoffer, and Edward Millner, in *The Journal of Law & Economics* (Oct. 1995), Univ. of Chicago Press, P.O. Box 37005, Chicago, Ill. 60637.

Anybody who doubts that people are strange ought to consider the research on car safety measures. There are conflicting findings, of course, but one line of research strongly suggests that people react to new safety devices, from seat belts to studded snow tires, by driving with greater abandon. In the curiously apt jargon of the economist, they are said to increase their "driving intensity." So much so, apparently, that they may totally negate the worth of the safety measure.

That is precisely what Peterson, Hoffer, and Millner, all of Virginia Commonwealth University, find in their study of the effects of air bags (which will be required for both front-seat occupants in 1998 autos). They made a list of the car models (excluding station wagons) to which air bags were added between 1989 and '93, then checked insurance industry records of personal injury claims. Sure enough, claims for the air bag models rose "significantly." (Interestingly, however, claims dropped for models that were "upsized.")

The authors then looked at data on the 207 fatal car crashes in Virginia during 1993 that involved late-model cars. "Of the 62 crashes involving cars equipped with air bags, 53 were . . . initiated by the driver of the air-bag equipped car." That's strong evidence, the authors say, that the reassuring presence of air bags promotes hot-dogging on the road.

It gets worse. There were 33 crashes in which the driver was the sole fatality, and 16 of these drivers were protected by an air bag. This is further evidence, the authors say, that protection offered by the air bags is offset by a new recklessness.

Even worse, drivers protected by air bags seem to be a danger to passengers. There were 13 single-car crashes in which a passenger was killed but the driver was not. In nine of these, the driver had an air bag.

The authors leave readers to draw their own conclusions. (It's important to note that traffic fatalities have been declining for decades.) One obvious possibility is that cars ought to be equipped with air bags for everybody but the driver.

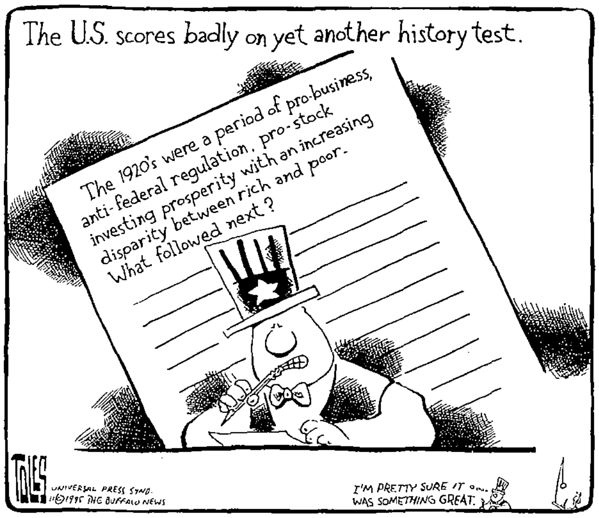
Supply-Side Stories

"Federal Personal Income Tax Policy in the 1920s" by Gene Smiley and Richard H. Keehn, in *The Journal of Economic History* (June 1995), 302 Thayer St., Box 1981, Brown Univ., Providence, R.I. 02912; "Tax Projections and the Budget: Lessons from the 1980s" by Alan J. Auerbach, "Behavioral Responses to Tax Rates: Evidence from the Tax Reform Act of 1986" by Martin Feldstein, and "Income Creation or Income Shifting? Behavioral Responses to the Tax Reform Act of 1986" by Joel Slemrod, in *American Economic Review* (May 1995), American Economic Assn., 2014 Broadway, Ste. 305, Nashville, Tenn. 37203.

In the recent history of the "dismal science," few theories have received a worse press than supply-side economics. Yet more than a decade after Ronald Reagan made it a household term, economists hotly debate the doctrine's validity. While the crude tax-cuts-pay-for-themselves version finds little support, there seems to be a growing sense that conventional economics has missed some important points about taxation.

A recent study of the federal tax cuts of the 1920s by economists Smiley, of Marquette University, and Keehn, of the University of Wisconsin, Parkside, is a case in point. With World War I over, there was broad agreement that federal income tax rates were too high. In the upper brackets, marginal tax rates (the amount taxed on each additional dollar of income) exceeded 70 percent, and tax avoidance, especially the purchase of tax-exempt government bonds, was common. In 1921, '24, and '26, Washington cut the marginal tax rates dramatically, especially for the rich.

Secretary of the Treasury Andrew Mellon, who served under Presidents Harding, Coolidge, and Hoover, argued that such cuts could keep tax receipts almost the same while shifting more of the overall tax burden to higher-income individuals. Smiley and Keehn say that is what happened. The decrease in tax avoidance, along with economic growth, led to a rise in tax receipts after 1923. The share of all federal income taxes paid by taxpayers with net incomes of $100,000 or more jumped from 35 percent in 1922 to 65 percent seven years later.



Supply-side economics even gets blamed for the Depression.