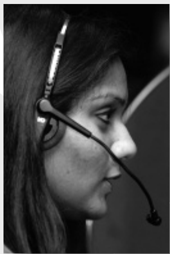


Why Sending Jobs to India is a Sign of Patriotism

By Stuart Anderson

"WHEN I AM PRESIDENT, and with your help, we're going to repeal every benefit, every loophole, every reward that entices any Benedict Arnold company or CEO to take the money and the jobs overseas and stick the American people with the bill." So declared John Kerry during last year's presidential campaign. As it turned out, American corporate executives did not like being compared to Benedict Arnold.

Dave Sikora, CEO of Pervasive Software, responded to Kerry with a very personal opinion piece in the *Wall Street Journal*. "And how is it that I am a

Indranil Mukherjee/Getty Images

Prakash Singh/Getty Images

traitor?" Sikora asked. "This is the country that I would die for, if asked. It's also the country that benefits from the economic production that occurred in my 22-year career in the information technology industry, where I have created hundreds of jobs and hundreds of millions of dollars in shareholder wealth." So why did Sikora's company start building software products in India? "The supply of talented computer software engineers created favorable economic conditions to build products at terrific prices, with the same reliability and high standards. These cost savings will mostly be redeployed into top-drawer American jobs – highly paid professional positions to handle the increased production capacity."

The Sikora-Kerry debate on offshore outsourcing is only the latest chapter in a centuries-long battle pitting the interests of this country against the principles of free trade. Throughout much of American history those who have favored protectionism have justified tariffs or blocking imports by waving the flag of patriotism and claiming their policy was in the national interest. But a closer look at this history shows that impugning the integrity of businesses that engage in free trade by calling them traitorous is a more recent phenomenon.

As with most stories that involve economics, it is useful to begin with Adam Smith. *The Wealth of Nations* was actually a response to the mercantilist interests that had been determining economic policy in Scotland for over two hundred years. They favored protecting domestic industry from foreign competition and tried to achieve a trade surplus in order to stock the national treasury. Smith explained that "consumption is the sole end and purpose of all production; and the interest of the producer ought to be attended to, only so far as it may be necessary for promoting that of the consumer …. The maxim is so perfectly self-evident, that it would be absurd to attempt to prove it. But in the mercantile system, the interest of the consumer is almost constantly sacrificed to that of the producer; and it seems to consider production, and not consumption, as the ultimate end and object of all industry and commerce." Put another way, we work so that we may consume goods or services that help us survive or give us pleasure, not simply for the sake of working. If you run a business (or work for one) it may be in your personal interest to use the government to block competition from imports but it is not in the interests of the other individuals in that society. Smith argued rightly, however, in saying that "if a foreign country can supply us with a commodity cheaper than we ourselves can make it, better buy it of them with some part of the produce of our own industry, employed in a way in which we have some advantage."

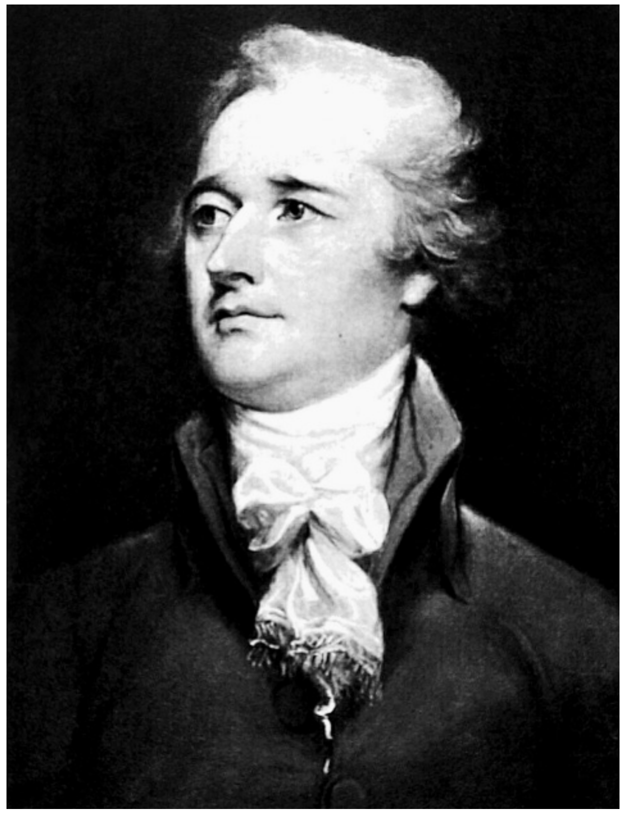
DURING GEORGE WASHINGTON'S FIRST TERM as president, trade and tariff issues were at the forefront of the debate over the future of the American economy. In the influential *Report on Manufactures*, published in December 1791, then treasury secretary Alexander Hamilton made the case for allowing manufacturing a key role in a young but modernizing American economy. Although only a small portion of Hamilton's report addressed trade protection, Pat Buchanan and other contemporary commentators have adopted Hamilton as the founder of American protectionism. "Hamilton laid the first layer of brick and mortar on America's tariff wall … Washington and Hamilton were America's first great economic nationalists. To them it was inseparable from patriotism," Buchanan writes in his 1998 book *The Great Betrayal*.

> ★ Alexander Hamilton *was skeptical of high protective tariffs because they sheltered inefficient and efficient producers alike, led to higher prices for consumers, and gave rise to* smuggling.

Hamilton himself, however, never tried to advocate his trade policies by calling on (or questioning) his readers' loyalty to the new America, let alone their distrust of foreigners. Modern protectionists express a fear of foreign capital, in clear contrast to Hamilton's view. As he wrote in the *Report on Manufactures*, "it is not impossible, that there may be persons disposed to look with a jealous eye on the introduction of foreign Capital, as if it were an instrument to deprive our own citizens of the profits of our own industry; But, perhaps, there never could be a more unreasonable jealousy. Instead of being viewed as a rival, it ought to be Considered as *a most valuable auxiliary, conducing to put in Motion* a greater Quantity of productive labour, and a greater portion of useful enterprise, than could exist without it [emphasis in original]." Dartmouth College economist Douglas Irwin writes that although Congress implemented certain tariff changes sought by Hamilton to provide temporary protection to manufacturers, "Hamilton was not as much of a protectionist as he is sometimes made out to be .... Hamilton was skeptical of high protective tariffs because they sheltered inefficient and efficient producers alike, led to higher prices for consumers, and gave rise to smuggling."

So where do today's protectionists find their intellectual ancestors? The debate over the McKinley Tariff Act of 1890 did not seem to involve one side questioning the other side's loyalty to country. However, this type of argument did creep into the debate before Herbert Hoover signed the Smoot-Hawley tariff into law in 1930. Smoot-Hawley, of course, represents a high-water mark of U.S. protectionist legislation. More than one thousand economists signed a letter to Hoover warning that the tariff would harm both the U.S. and world economy, but to no avail. The average (*ad valorem*) tariff rate, already at a high rate of 40.1 percent, rose to 47.1 percent under the bill. Many economists believe the tariff contributed significantly to the Great Depression.

While businesses that favored the tariff stood to gain a lot from decreased foreign competition, there is little evidence that those who lobbied for Smoot-Hawley accused their opponents of disloyalty to America. In fact, lobbying for the tariff proved to be a series of accommodations among special interest groups in favor of protectionism, as each made tactical moves designed to preserve its own piece of the pie. For example, to maintain high tariffs on imports of agricultural goods, the American Farm Bureau Federation did not oppose high tariffs on manufactured goods that raised the price of farm machinery for its members. The farm bureau calculated that its members were better off paying the elevated tariff on machinery rather than risk a liberalized trading regime or political compromise that would lower tariffs on competing agricultural imports. Opposition to the Smoot-Hawley tariff proved to be diffuse and ineffective. But for the first time in American history nationalism forcefully entered the policy discussion over trade.



©Topham/The Image Works

In his seminal work, *Politics, Pressures, and the Tariff*, Wesleyan University professor E.E. Schattschneider notes that manufacturers favoring the tariff claimed that they were serving the American

Mark Kauffman/Time Life Pictures/Getty Images

public, though in fact the businesses themselves stood to benefit most, and the public would pay the cost in the form of higher prices for goods. "The whole amalgam of emotional attitudes associated with nationalism has been appropriated as their own by the immediate beneficiaries of the system, for nationalism makes men willing to bear the burdens imposed by the tariff because it makes private interests seem public," writes Schattschneider. "It legitimizes and clothes with a semblance of public interest a host of impulses which could not otherwise gain approval, and the plausible arguments by which the recipients of favors undertake to persuade the public enable them likewise to rationalize their conduct to satisfy themselves."

Unlike today, when retail store chains and domestic corporate users of certain products are organized to lend a counterweight to those seeking trade protection for steel, textiles, and other imports, the years of debate over Smoot-Hawley saw "no significant concentration of forces able to reverse the policy and bring about a return to a system of low tariffs or free trade." Senators dismissed tariff opponents as a collection of "dealers, commission merchants, and jobbers." Moreover, Schattschneider explains, the language of nationalism worked against the importers: "In this organization of attitudes the importer is almost fatally handicapped. He is the agent of foreign interests that have no standing in court, and does business on sufferance, continuing only until challenged. His opposition is taken for granted, discounted in advance."

There was still no question, however, as to whether the importers were patriotic Americans. To the extent that loyalty arguments entered the public discourse during the first part of the twentieth century, they focused not on trade issues, but on national security and the rise of communism in the aftermath of the Bolshevik Revolution. Hollywood writers and actors had to take loyalty oaths during the McCarthy era, but no one asked corporate CEOs to do so.

A MAJOR SHIFT APPEARS TO HAVE TAKEN PLACE in the 1980s when Japanese companies emerged as the ubiquitous suppliers of American goods. Japan's success in selling automobiles to American consumers became the first flashpoint, prompting a number of (unsuccessful) bills requiring cars to be built primarily with U.S. parts, as well as a "voluntary" export restraint agreement foisted on Japan by the Reagan Administration. The restraint on auto exports allowed both U.S. and Japanese car companies to raise prices, costing American consumers an extra $5.8 billion in 1984, according to economists Gary Hufbauer, Diane Berliner, and Kimberly Elliot of the Institute for International Economics.

Hollywood **writers** and **actors** *had to take loyalty oaths during the McCarthy era, but no one asked* **corporate CEOs** *to do so.*

Japan's continued success in the U.S. consumer market – despite the restraints imposed by the agreement – and its purchases of U.S. landmarks like the Pebble Beach golf course and Rockefeller Center, led some commentators to declare Japanese companies America's enemies and those who helped them traitors. In his book, *Agents of Influence*, published in 1990, Pat Choate claimed that former U.S. government officials who worked as advisers or lobbyists for Japanese companies were selling out America's interests to the highest bidder. The book includes a list of more than two hundred former federal officials who represented Japanese or other foreign companies between 1980 and 1990. Choate charged that "the United States is not only selling corporate assets and real estate to foreign bidders; also for sale is American integrity and national honor." The larger subject of *Agents of Influence*, summarized on the book jacket, is

> the nature of Japan's unprecedented political power in this country – how Japan can, in effect, veto U.S. legislation inimical to its interests, politically overwhelm virtually any combination of American companies, unions, or other groups it opposes, shape those key U.S. trade and economic policies that decide which American industries will grow or decline, which American jobs will remain or disappear. He reveals how Japan can reach up to the American presidency itself or down to the grass-roots level across the nation and influence political decisions that allow Japan to advance its national interests and win market share in the United States for its target industries.

The book is even listed as recommended reading in Michael Crichton's 1992 novel *Rising Sun*. A central part of the novel deals with the shifting allegiances of a U.S. senator who goes from warning America about the dangers of Japan to supporting the sale of a computer firm to a Japanese buyer. The book is filled with speeches, cast as dialogue, railing against the alleged Japanese domination of all aspects of American life. "If the Japanese are willing to put up the money … then the Japanese will control American education," says one character while watching children play. A discussion of a murder caught on videotape allows another character to opine that "the Japanese are becoming much better in software. Soon they will surpass the Americans in that, as they already have in computers." The novel contains several references to Americans who are too afraid to do anything but go along with the nefarious business designs of Japan, regardless of the harm done to America.

If Michael Crichton had waited a few more years, he might have called his book *Setting Sun*, because the Japanese economy went into a nosedive in the early 1990s (from which it has yet to recover), taking with it important Japanese real estate investments in America. In a move of supreme irony, in view of earlier warnings about fellow travelers who work on behalf of Japan, Sony Corporation has just named an American, Howard Stringer, to run the company. "Cries that the Japanese were taking over America now appear quaint," said U.S. deputy treasury secretary Kenneth Dam in a 2002 speech.

Starting in the mid-1990s, following the passage of the North American Free Trade Agreement (NAFTA), opponents of trade shifted their sights from Japan (and Mexico) to China, and later to India. As Pat Buchanan argued in a 2003 article in

The American Conservative: "When U.S. companies go global, they shed their loyalty to America."

IN HIS BOOK, *THE WORLD IS FLAT* (2005), THOMAS Friedman describes how lower technology costs and an abundance of skilled and highly trainable citizens turned China and India into prime locations for manufacturing and service industries. Observers such as Craig J. Mundie, chief technology officer for Microsoft, point to the "diffusion" of personal computers, dial-up modems and global telephone networks as elements in creating the global information revolution in the 1990s. Friedman also argues that when China joinined the World Trade Organization in 2001, it gave a huge boost to offshore outsourcing, taking "Beijing and the world to a whole new level of offshoring – with more companies shifting production offshore and then integrating it into their global supply chains."

More than two centuries after *The Wealth of Nations*, the view that exports are good and imports are bad is still reflected in the thinking of many members of Congress, as well as populist commentators like CNN's Lou Dobbs. Since 2003, Dobbs has devoted a significant portion of his nightly program to reports, debate, and criticism of international trade. In 2004, he published a book called *Exporting America*, named for the regular segment on his show attacking outsourcing. As it is defined today, outsourcing describes almost any activity that involves importing goods or services that could have been produced in the United States.

"The power of big business over our national life has never been greater," writes Dobbs. "Never have there been fewer business leaders willing to commit to the national interest over selfish interests, to the good of the country over that of the companies they lead. And the indifference of

Stuart Briers

those business leaders to our long-term national welfare is nowhere more evident than in the exporting of American jobs to cheap overseas labor markets." Dobbs takes special aim at CEOs, who, he writes, "seem to think that their businesses are, first and foremost, international companies, not American. Otherwise they couldn't routinely ignore the needs of their employees and their communities and outsource their jobs to lower-paid workers in other countries."

Although easily the most prominent critic, Dobbs is hardly alone in suggesting that outsourcing is a form of disloyalty. More than eighty anti-outsourcing web sites have established themselves in recent years, most questioning the patriotism of companies and executives that hire employees or maintain facilities outside the United States. The Information Technology Professionals Association of America (ITPAA), started by Doug Kerwin, a technology consultant, displays an assortment of T-shirts and bumper stickers on its web site (www.itpaa.org): "Patriotism is Not a Crime but Outsourcing Should Be"; "Outsource a CEO"; "Lost Your Job to Free Trade & Offshoring Yet?"; "Stop Outsourcing Abroad: the Real American Express"; and finally, a T-shirt that says, "My Job Went to India and All I Got Was a Stupid Pink Slip."

"It's odd to push the loyalty argument at a time when the world is more interdependent than it's ever been," says Charles K. Rowley, professor of economics at George Mason University. Today, there are many sources for a particular product, so it's unlikely that any country could withhold resources successfully from U.S. buyers. Rowley questions the definition of loyalty used by critics of trade and outsourcing. "It's loyalty to a particular group. Is it loyalty to Americans? No, it can't be, because Americans gain. You and I gain whenever a cheap Toyota car comes over here and lowers the price of autos," he says. He believes the specter of disloyalty is being used by workers and executives in industries like steel and textiles as a way to justify support for less competition in their industries. "Is loyalty just another word for joblessness? If that's the case, then it's loyalty to a special interest, it's not loyalty to the nation. Because with comparative advantage you're better off as a country when people trade."

> ★ Politics and self-interest, *rather than concern about the welfare of individual Americans as consumers,* drives most efforts *to erect trade barriers.*

Nearly two hundred years after the law of comparative advantage was put forward by David Ricardo, the principle of the mutually beneficial impact of international trade remains central to economic thought. "Regrettably, few politicians then or now seem to understand the analysis. As a result, quotas, tariffs, and trade wars mar the world's economic history," according to economist Todd Buchholz, author of *New Ideas From Dead Economists*. As Buchholz writes, "Ricardo showed that people and countries should specialize in whatever leads them to give up the least.… The point of Ricardo's analysis: free trade makes it possible for households to consume more goods *regardless* of whether trading partners are more or less economically advanced."

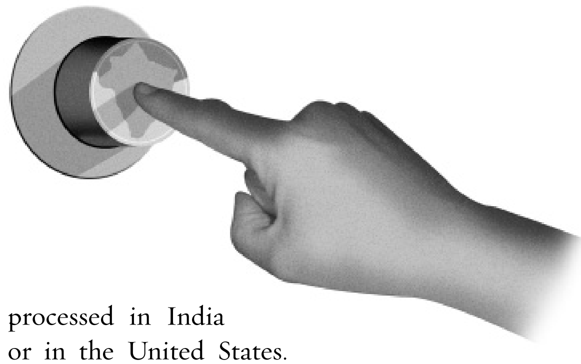
Buchholz explains that one should look at protectionist arguments on a micro-scale. Does it make sense for a rich man make his own shoes

> *The* crucial *thing to remember is that* individuals *trade,* not *nations.*

rather than buy them? "If not, why would the United States be hurt by someone buying shoes from Malaysia? Would the nation be richer if all people were self-sufficient? Should individual countries erect boundaries? . . . Why should a nation be enriched by turning away goods produced more cheaply abroad?"

Politics and self-interest, rather than concern about the welfare of individual Americans as consumers, drives most efforts to erect trade barriers. Imagine, for instance, a dying French billionaire who is grateful to America for liberating France during World War II. In a magnanimous gesture, he establishes a foundation that will send every American family a free automobile every two years for the next ten years. For individual Americans this would be wonderful, with each gaining approximately $100,000 worth of consumer goods without paying for them over the course of a decade. Yet there is no doubt this action would cost many jobs in the U.S. auto industry, as there would be relatively little need for Americans to buy cars domestically when their needs are being met for free. As a result, it is possible that U.S. car companies and the United Auto Workers Union would try to block the sending of free cars to American families. Should Americans be considered disloyal if they accept free (or buy inexpensive) automobiles?

It is instructive that critics choose to blame CEOs and others in business, not consumers, for purchasing goods or services produced overseas. This may be because to attack all U.S. consumers who purchase foreign-produced goods and services would be like a lawyer indicting the jury. Last year, California-based E-Loan began offering its customers a choice of having their loan paperwork



Stuart Briers

processed in India or in the United States. Customers were informed that if they press the "India" button, their loan will be processed in one day. However, if they chose to have the work done in the United States it would likely take two days or longer. The result? More than 80 percent of customers for home equity loans, according to the company, chose to have their work done in India. Sometimes the best way to evaluate an issue is to look at what people do with their own money.

"The crucial thing to remember is that individuals trade, not nations," Charles K. Rowley explains. Yet it is also true that the individuals who make up the population of a country gain from the efficiency and specialization brought about by international trade. This does not mean that every person will gain from every transaction. There are always transition costs for those most affected in competing industries. "But that's not America, that's a segment of the country, so to talk about being loyal means being loyal to that interest," concludes Rowley.

America benefits from individuals and companies purchasing goods and services at the best value, economists argue. In addition, the world as a whole gains from the free exchange that trade brings, allowing specialization, increased quality of consumer goods, and, ultimately, higher standards of living. Expanding free trade would lift more than 500 million people in the Third World out of poverty, according to the Center for Global

34-43ic4.indd 42 9/16/05 10:50:10 AM

Development, based in Washington, D.C. One executive told me that because of the close-knit family structure in India, the 4,000 workers employed there by his company provide financial support to over 50,000 people, making more of a direct difference in those lives than would an aid program.

While Americans are generally better off than Indians, the average American consumer sees real benefits from saving a few dollars here and there every day. When critics scoff at the savings obtained by consumers from international trade, it is useful to recall Adam Smith's rule of economics: The end of economic activity is consumption, not production. Offshore outsourcing "creates wealth for U.S. companies and consumers and therefore for the United States as a whole," concludes a 2003 report by the McKinsey Global Institute. Offshoring saves U.S. companies, on average, fifty-eight cents for every dollar spent overseas, thereby increasing productivity, profitability, and competitiveness. For every dollar spent offshoring, U.S. service providers purchase an additional five cents worth of U.S. goods and services, which creates U.S. jobs. Finally, global outsourcing frees up U.S. labor to engage in work the market determines is more efficiently performed in America. "Far from being bad for the United States, offshoring creates net additional value for the U.S. economy that did not exist before," according to the McKinsey Global Institute.

Today, the trade critics charge that U.S. manufacturing jobs have been "exported" to China. But China itself has lost 15 million manufacturing jobs between 1995 and 2002, according to the New York-based Conference Board. So where did the jobs go? "What's going on?" wonders President Clinton's labor secretary Robert Reich. He answers, "Two words: Higher productivity." In other words, getting more output from fewer workers is a global phenomenon, one that in the long run raises living standards.

Why do critics of free trade find it appropriate to portray CEO decision-making as motivated by greed and, by implication, disloyalty? The answer seems clear: the rhetorical effect of accusing corporate executives of bad intent gives the arguments against international trade much of their force. If the answer is not greed, then an executive is simply making choices that he or she believes are in the best interests of the company's customers and shareholders. Such decisions would also be in the interests of the firm's workforce, broadly understood, although not necessarily of every single worker in a company. Paradoxically, protecting jobs in one part of a company puts more jobs in jeopardy elsewhere in the corporation, since the firm will become less competitive. Even with the best intentions a company must remain profitable to stay in business, to grow, and to hire more people.

"To remain competitive, I must consider every opportunity to run my business as efficiently and effectively as possible. This is what I get paid to do," argues Dave Sikora. "If I miss the mark, my customers will leave me, my employees will have to find new jobs, and all of my stakeholders will lose." As Adam Smith wrote, "I have never known much good done by those who affected to trade for the public good."

CEOs and other business people are not disloyal to America for operating in India, China, or elsewhere. They are loyal to the people who hired them and to those who placed faith in them to enhance shareholder wealth, increase customer value, and ensure long-term business viability for employees. Critics say executives should "put America first," which implies that engaging in international trade would itself be a form of disloyalty. But as Charles K. Rowley puts it: "It doesn't mean you're loyal to the nation because you stop other Americans from buying freely." ♣

Stuart Anderson *is Executive Director of the National Foundation for American Policy, a public policy research organization based in Arlington, Virginia.*

Stuart Briers