YET MORE FALLACIES IN GLOBAPHOBIA

International free trade gives national governments complete freedom to fashion the kind of society they choose, but does require that they efficiently manage the policies they adopt.

by Jean-Jacques Rosa

Following last week's article, a number of readers have argued that the mergers and acquisitions resulting from international markets open to free circulation of goods and services as well as capital -- globalization, in other words -- result in job cuts, and worsen unemployment. Shareholders demand for increased profitability, combined with intensive competition from less developed countries, is seen as depriving many French companies of breathing space. Some feel that this trap must at all costs be avoided, since it would force us to give up our social policies and fall into line with the "lowest bidders" in social policy amongst our competitors. That low Asian salaries and child labor would endanger the viability of the systems of social protection in rich countries, while simultaneously eliminating jobs. Economic globalization would lead to depriving a nation of any political sovereignty. So, let us take a close look at each of these arguments.

Political unemployment

Firstly, it is important to remember that mergers generally involve same-nationality companies rather than companies from different countries. However, we can nevertheless admit that such mergers are often forced upon our companies by shareholders demands for profitability -- shareholders who are free to move and invest anywhere else in the world. It is also clear that this type of operation is a way for merging companies to reduce production costs, both by the sale of certain subsidiaries (considered less profitable by the new group), and by downsizing due to business downturns or elimination of redundant positions. The objective of reorganization is to reduce costs for merged companies while still maintaining turnover at its former level.

However, downsizing does not necessarily result in unemployment. In a growing economy, redundant workers often find new employment very quickly. Mergers and restructuring are quite common in the United States and Great Britain and far more widespread than in continental Europe. Yet the unemployment rate in these countries has continued to decrease at a spectacular rate over the last few years to reach its lowest level in half a century. And neither of these countries has implemented systematic protectionist policies to boost employment.

European and French unemployment is, first of all, a result of the poor macroeconomic policies -- monetary policy, exchange rate policy and fiscal management -- that have been followed over the last 15 years, rather than of company mergers or international free trade. The proof? Our economy was as open in 1995-96 as it is today, but this did not prevent unemployment from decreasing due to the policy of increasing public deficits at that time. In 1986-88, renewed growth also resulted in increased employment. A similar trend prevails today. In a nutshell, the Euro is falling with respect to the dollar, and this accounts for the improved French economy and the fall in unemployment rates, however irritating this may prove to those who believe that an expansive currency encourages growth and employment. Fortunately, thanks primarily to the rise of the dollar, the Euro has been revealed as a weak currency.

It is perhaps difficult to understand why exchange rates play such a decisive role, but actually the mechanism is quite simple. Imagine that Renault or Peugeot decide to lower the price of their vehicles by 10% over a period of a few weeks, while competitors' prices remain the same. The consequences on sales, and ultimately on production, will not take long to make themselves felt. Remember the effects of the "Balladurette" policy, implemented by Prime Minister Balladur, that involved artificial manipulation of prices, fortunately not widely applied and relatively short-lived. Consumers react to variations in prices, and variations in the exchange rate have an instantaneous effect on the price of all exports to international markets. With significant effects on an economy where over one third of total production is exported.

Company restructuring does not create durable unemployment in a strong growth economy. It is only harmful in an anemic, tightly controlled economy. Which implies that an independent government will always have considerable freedom in choosing macroeconomic policies to reduce unemployment while allowing companies to increase productivity and profitability.

Threatened by the poor

But what about social dumping? Do international trade and free capital movements force us to reduce salaries and social benefits to remain on an equal footing with the poorest countries, where work is remunerated at extremely low levels? Not at all. First of all, because although salaries are the result of comparisons and competition on an international level, this works in both directions. Asian countries such as Japan or Korea with a high level of exports have seen salary levels rise extremely fast to the level of salaries paid in European countries or in the United States for an equal qualification of labor. A fact that, curiously, has not been taken into account in arguments advanced by European protectionists.

And the threat to social benefits? Are the contributions that finance these benefits, that is, taxes on employment, an impossible burden for our companies as they strive to compete with companies who pay low salaries? This would only be the case if increases in contributions were passed on in the form of demands for salary increases. However, if wage earners believe that the social services they "purchase" with their contribution are sufficient to justify the cost, there will be no additional demands for increased salaries because their standard of living will have been improved by additional benefits.

Thus, we are faced with a choice between direct wages for private purchases, and indirect wages stemming from health benefits and increased security. If an increase in indirect wages compensates for a reduction in direct wages in the eyes of the wage earner, the total cost of labor will not increase in countries who choose to improve the level of social protection. Thus labor costs will not be superior in this respect to countries with more restricted social policies.

The problem, however, becomes real when the wage earner considers that the benefits received are not worth the price. This implies that the social security system is considered inefficient or that it does not correspond to an acceptable substitution between health and retirement benefits and a direct wage. The problem then lies in the efficiency of the social security system and the level of coverage demanded by wage earners, rather than being a question of international competition that would oblige us, against our will, to decrease the level of health care and retirement benefits.

There are many good reasons to believe that France's current social protection policies must be rethought, as they were designed over fifty years ago and no longer correspond to modern standards of efficiency nor to wage earners' expectations. But here reform must be driven by reasons internal to France as a nation, rather than the iron rod of that traditional scapegoat, international competition.

Public infrastructures and ecology

The same holds true for other areas of public policy. A national government can decide to implement a policy of infrastructure investment or the fight against pollution without necessarily compromising the country's economic future. France as a rubbish bin, where the environment is not protected, the country deserted and traditional activities totally abandoned, would certainly cease to attract tourists and thus lose an important source of revenue. It is also certain that high-polluting companies prefer to work in countries where pollution is not controlled or taxed. On the other hand, "clean" companies will appreciate a better-preserved environment. And many investors chose to locate their production activities in countries where taxes are high but top-quality infrastructures can be guaranteed. If this were not the case, all European companies would have already emigrated to Zaire, Thailand or Sri Lanka, and Paris would be an economic desert, massively relinquished for Luxembourg and Ireland.

Thus, the idea that all public policy choices result in increased taxes and costs that invariably compromise economic growth is fundamentally wrong. It is not true that international competition imposes a societal model where the government's role is reduced to a minimum, where social protection is non-existent, wages at an all-time low and the environment irrevocably damaged.

However, it is plain that national governments will henceforth compete with other countries and other governments. Public revenue may be used efficiently, but may also be frittered away. States, like companies, must manage their resources efficiently. This in no way implies a dearth of choice in terms of economic and social policies. No one would claim that a company has only one possible strategy available at a given point in time in a certain competitive situation. It is just as fallacious to maintain that only one public policy would be feasible in every country throughout the world. However, once the policies have been chosen, they must be managed in a rigorous and efficient way.

There is no such thing as the dictatorship of market forces and globalization. Governments must continue to do their job, that is, to propose public policies that satisfy the citizens who voted them into power. But it may be that yesterday's policies are no longer viable, simply because today's citizens and taxpayers have new, and different, expectations.

J.J.R.

Le Figaro, October 1st, 1999