

CAFTA: A TWO-WAY STREET TO JOB LOSS IN THE AMERICAS

In the fight to push through the Central America Free Trade Agreement (CAFTA), the Bush administration, some economists and corporate lobbyists have argued that the trade deal will create jobs both in the U.S. and the six other nations party to the agreement. The legacy of the North American Free Trade Agreement (NAFTA), which was also sold as a job-creating deal, casts significant doubt on these dubious claims.

Like NAFTA before it, CAFTA will do much more than just reduce barriers to the flow of goods and services – it will establish a new legal regime that increases safeguards for multinational investment and reduces protections for workers' rights, thus *creating a double incentive for American companies to ship jobs overseas* and produce abroad for export back into the U.S. market. Also like NAFTA, the accord could result in large displacements of subsistence farmers in Central America, creating masses of unemployed whose numbers may swamp the few jobs created in export-oriented manufacturing. Finally, like NAFTA, the Central America agreement would do little to jump-start a virtuous cycle of domestic demand growth in the region, leading to increased dependence on exports to the U.S. market and greater economic instability.

Unfortunately, *when it comes to the creation of good jobs at good wages, CAFTA could be a lose-lose for U.S. and Central American workers*, rather than the win-win promised by the Bush administration. CAFTA's likely impact on jobs in the U.S. and Central America is summarized below:

CAFTA Impacts in U.S.	CAFTA Impacts in Central America
Trade deficits rise and shifts in production overseas accelerate	Imports of staple crops and falling prices displace subsistence farmers
More U.S. jobs lost, particularly in manufacturing	New opportunities in export-oriented industries insufficient to absorb farmers and other workers displaced by imports
Downward pressure on wages intensifies and income inequality rises	Weakened rules on workers' rights prevent workers from organizing and pull down wages even in export sectors
Employers use threats to violate workers' right to organize unions, further eroding wages and working conditions	Deteriorating labor conditions force the region to compete with China on wages, not high standards and quality

The Facts About Trade and Job Loss

Free trade agreements like CAFTA can serve as a catalyst to eliminate American jobs in two ways: 1) weak protections for workers' rights and the environment combined with the removal of tariffs and quotas on imports lowers the price of production overseas, driving competing U.S. producers out of business and eliminating American jobs; and 2) new protections for foreign investment in other countries, combined with permanent, unconditional access to the U.S. market, reduce the risk of foreign investment, thereby encouraging U.S. companies to move jobs abroad.

The two processes reinforce and complement each other. Companies that can no longer afford to produce in the U.S. because of increased import competition may be more likely to move abroad. At the same time, companies that produce overseas can take advantage of lowered trade barriers, and are thus more likely to export their products back into the U.S. This further increases competitive pressures on those companies still left in the U.S.

The record of job loss under NAFTA illustrates this process.

- Under NAFTA, the U.S. trade deficit with Canada and Mexico exploded, despite predictions by NAFTA supporters that the deal would generate sizeable trade surpluses with Mexico for another fifteen years.¹ ***Our NAFTA trade deficit is now twelve times bigger than it was before NAFTA began.*** Our combined trade deficit with the NAFTA countries was \$9 billion in 1993; in 2004 it had jumped to \$111 billion.
- When NAFTA was being sold to the public, ***job creation predictions for the agreement were wildly inaccurate.*** These predictions were based on erroneous predictions of shifts in the trade balance that were off by more than \$50 billion annually. Gary Hufbauer and Jeff Schott, of the Institute for International Economics, predicted that by 2005, the U.S. trade surplus with Mexico would be between \$9 billion and \$12 billion annually. Instead, in 2004 the U.S. ran a trade deficit with Mexico of more than \$45 billion. These predictions relied too heavily on the assumption that reductions in tariff barriers would generate relatively faster growth in U.S. exports to Mexico, compared to imports. Similarly erroneous assumptions dominate the rosy trade and job projections with respect to CAFTA.
- When imports rise faster than exports, our trade deficit grows, and jobs and job opportunities in the U.S. are lost. The Economic Policy Institute estimates that ***nearly 900,000 net jobs were lost due to the growth in the NAFTA trade deficit through 2002***, and the deficit has only grown since then.
- ***The U.S. Department of Labor certified 525,094 workers for NAFTA trade adjustment assistance through 2002*** because their jobs were lost due to NAFTA imports or shifts in production to Canada or Mexico under NAFTA. This figure vastly undercounts the true scope of NAFTA-related job loss, since it only includes workers who knew about the trade adjustment assistance program, applied for benefits, and met the program's strict certification standards.

¹ Gary Clyde Hufbauer and Jeffrey J. Schott. *NAFTA: An Assessment*. Institute for International Economics, 1993, pp. 14-15.

Workers Who Don't Lose Jobs Also Suffer Under Free Trade Rules

Economic theory predicts increased trade will lower wages for lesser-skilled occupations in a country like the United States (that is relatively well-endowed with skilled labor and capital), thus increasing income inequality. ***Though economists' estimates vary, increased trade is likely responsible for about 20 percent of the recent increase in income inequality in the U.S.*** This translates into a decrease in real wages for the majority of American workers – roughly a 6 percent loss for the two-thirds of workers who lack a college degree, relative to what they would otherwise have earned.

Recent wage trends confirm what economic theory predicts. ***Real wages have stagnated since 1973, even though productivity has grown rapidly.*** Real hourly wages for a majority of male workers have actually fallen since 1973. For the typical male worker (that is, at the fiftieth percentile), for example, hourly wages fell from \$15.20 in 1973 to \$15.04 thirty years later (in constant 2003 dollars). While women workers have fared somewhat better, the overall gap between wage gains and productivity growth continues to grow. The Economic Policy Institute reports wages in the industries in which jobs are being created are, on average, 21 percent lower than wages in those industries in which jobs are disappearing. In addition, expanding industries are less likely to provide workers with health insurance than industries cutting jobs.

Increased employer mobility resulting from free trade deals like NAFTA and CAFTA also hurts workers by increasing the incidence of violations of workers' right to organize and decreasing their bargaining power. Even when employers do not actually shift production, their threats to do so can squelch union organizing drives and result in concessions at the bargaining table.

- A Cornell University survey showed the incidence of such threats increased after the passage of NAFTA. By the late 1990s, during 51 percent of union representation election campaigns, ***employers threatened that they would close or move the workplace if the workers voted to form a union***—up from the 29 percent of campaigns during which such threats were made in the mid-1980s. In organizing campaigns in mobile industries such as manufacturing, the “threat rate” reached 71 percent by the late 1990s.
- These ***threats are a very effective means of repressing workers' right to organize***: workers trying to organize unions won union elections 51 percent of the time in plants without threats, but only 24 percent of the time when employers did use such threats. Employer threats to close or move the workplace are an important reason why fewer than 100,000 workers per year succeed in forming unions through the NLRB representation election process, even though a February 2005 survey by Peter Hart revealed that 53 percent of non-union workers—some 57 million workers—want a union in their workplace.
- ***Such massive suppression of workers' freedom to form unions harms workers and the larger society.*** A partial list of these damaging consequences includes: suppression of wages for all workers, union and non-union alike; widening economic inequality; destruction of retirement income security (only 16 percent of non-union workers have defined benefit pensions, versus 70 percent of union workers); and further increases in the ranks of the uninsured (non-union workers are six times more likely than union members to lack health insurance coverage, according to a May 2005 report from the Employee Benefit Research Institute).

CAFTA Encourages Destruction of More High-Paying U.S. Jobs

CAFTA is likely to only exacerbate the loss of jobs and downgrading of working conditions that has resulted from free trade agreements such as NAFTA. *The U.S. International Trade Commission (ITC) predicts that CAFTA will increase the U.S. trade deficit with Central America.* In its economic impact assessment of the accord, the ITC predicts that CAFTA will increase U.S. imports from the region by \$2.8 billion and increase U.S. exports to the region by \$2.7 billion, for a net increase in our deficit of \$110 million. While this is a small increase relative to our current trade deficit with the region of \$2.7 billion, it is notable that even without explicitly taking into account the possibility of accelerated production shifts from the U.S. to Central America, the ITC estimates that our trade deficit with Central America will grow under CAFTA, not fall.

The ITC also predicts that the overall U.S. trade deficit will be slightly reduced under CAFTA, by \$756 million, because of Central America's displacement of U.S. imports from third countries. This prediction merits skepticism. None of the economic models reviewed by the ITC during the NAFTA debate were able to project the explosive growth in our aggregate trade deficit over the past eleven years, which ballooned by almost 900 percent. Even though many other factors clearly contributed to this rapid growth in the deficit, the ITC models appear to continue to exclude these crucial factors.

The Bush administration argues that CAFTA will actually improve our trade balance with Central America, since the vast majority of exports from Central America already enter the U.S. duty-free, while the U.S. faces somewhat higher tariffs selling in Central America. Thus, they argue, unlike under NAFTA, the additional market access CAFTA grants Central America is small, and will not appreciably increase the U.S. trade deficit or harm U.S. workers. But this argument ignores the history of NAFTA. Many U.S. imports from Mexico also entered duty-free before NAFTA went into effect, yet imports still boomed after NAFTA's implementation. In fact, *the average tariff rate on our imports from Mexico was less before NAFTA began than the average tariff rate is on Central American imports today.* Duties paid on U.S. imports from Mexico totaled only 2.07 percent of their value in 1993 – average duties on U.S. imports from Central America, by contrast, were 2.93 percent in 2004. The argument that our market was much more closed to Mexico before NAFTA than it is to Central America today is not supported by the facts.

But, ultimately, changes in tariff rates, rules of origin, and quota phase-outs explain only part of the job loss caused by trade agreements like NAFTA and CAFTA. In addition to eliminating trade barriers, these free trade agreements also *make foreign countries more attractive locations for offshore production.*

- The agreements' rules on investment, services, intellectual property, and government procurement combine to *provide more security and predictability for foreign investors*, by guaranteeing their right to invest, produce and profit abroad, by providing dispute resolution mechanisms to resolve potential conflicts, and by reducing the ability of host-country governments to regulate investors.

- In addition, the agreements' rules on labor and environment do very little to ensure that companies shipping production overseas meet basic international standards, ***reducing their accountability to the communities in which they produce.***
- In fact, ***CAFTA actually reduces protections for workers' rights that exist in current trade programs***, thus providing an additional incentive for companies to produce in Central America, where workers are easily barred from union organizing, collective bargaining can be avoided entirely, and strikes are routinely declared illegal.

CAFTA Would Also Harm Workers in Central America

For all of the harm CAFTA would cause U.S. workers, it is likely to have very few, if any, net benefits for workers in Central America. If Mexico's experience under NAFTA is any guide, CAFTA will harm large segments of the Central American workforce, particularly in rural areas, and this harm may far outweigh the few gains the accord confers on export sectors, thus creating ***a net loss for workers in Central America*** as well as workers in the U.S.

- In Mexico under NAFTA, growing imports of staple crops such as corn from the U.S. contributed to huge losses for small farmers and peasants. According to Oxfam America, nearly 1.7 million small farmers have lost their jobs, and another 15 million have seen their incomes fall significantly, since NAFTA went into effect. CAFTA also requires Central American countries to open their markets to staple crops, despite the lack of safety nets for farmers. The World Bank estimates that ***one in ten households in Nicaragua, and one in six in Guatemala, will end up being net losers from agricultural trade under CAFTA.***
- These losses could far outweigh any job gains in Central American export industries under CAFTA. In Mexico's export assembly plants, despite booming exports to the U.S., job growth under NAFTA peaked at only 800,000 in 2001 according to the Carnegie Endowment for International Peace. ***Manufacturing growth thus provided less than half of the jobs needed to make up for losses in the rural sector.*** And more than a quarter of these new maquiladora jobs were lost since the 2001 peak, many to competition with China. In addition, employment in non-maquiladora manufacturing actually fell in Mexico under NAFTA, as more inputs were sourced from abroad. CAFTA is likely to have the same results, producing short-term gains in export sectors that are insufficient to absorb displaced workers and rural populations and highly susceptible to fierce competition with China.
- ***NAFTA has not protected Mexico from competition with China, and CAFTA offers little hope that the Central American region will fare any better.*** Central America's inherent advantages over China, in terms of location and ties to the U.S., will not be altered by CAFTA's passage or failure. The marginal additional market access that CAFTA would provide for Central American goods over current trade preference programs for the region will be insufficient to overcome China's cost advantage in terms of wages, since workers in Central American countries earn two to ten times as much as their Chinese counterparts. Any attempt by Central American producers to compete with China on the basis of wages would only plunge workers in the region deeper into poverty and put domestic demand-led development farther out of reach.
- Moreover, Central America's greatest potential for establishing a lasting advantage over China – by developing the ability to guarantee workers' rights that meet the global sourcing

guidelines of major apparel brands – would actually be harder to achieve if CAFTA passes. ***The accord would reduce existing protections for workers' rights, robbing workers in the region of the leverage they need to secure advances in labor laws and practice.*** The U.S. government could do much more for the long-term health of the Central American apparel sector by imposing restrictions on import surges and unfair trade practices by China, thus opening up more space for Central American imports, and by helping the countries upgrade their labor standards through enforceable trade conditionalities.

Displacement of rural populations, disappointing job creation in manufacturing, unmitigated competition with China and the failure to protect fundamental workers' rights have all contributed to ***a decline in real wages and an increase in poverty in Mexico under NAFTA.*** Rather than learn from these failings by negotiating a new kind of trade agreement with Central America that would create good jobs, guarantee workers' rights, and help build the foundations for a thriving middle class in the region, the administration has duplicated NAFTA's flaws in CAFTA. Unfortunately, the results in Central America are all too likely to mirror Mexico's experience, and bring the region no closer to the sustained economic development and poverty reduction its workers and their families need.

Conclusion

The optimistic job creation predictions of CAFTA supporters echo those that were used to sell NAFTA. Instead of improving our trade balance, creating good jobs, and spurring development in Mexico as promised, NAFTA led to booming trade deficits, lost jobs and rampant union busting in the U.S., and falling wages and rising poverty in Mexico. ***CAFTA, which is built on exactly the same model as NAFTA, will cause the same harm to workers.*** Increased trade can support job creation and economic development, but it can only do so if the rules of trade are done right. To deliver on its promises, CAFTA must be renegotiated to protect workers' rights and support robust job creation at home and abroad.