# Unions, Protectionism, and U.S. Competitiveness

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In the past three decades, labor union leaders have emerged as among the chief critics of trade liberalization, while the economic evidence has grown that labor unions compromise the ability of American companies to compete in global markets.

Organized labor has been politically vocal in the United States ever since the movement emerged in the late 1800s. A striking development since the 1970s, however, is its hardening opposition to trade liberalization. Labor leaders have opposed virtually all legislative initiatives since the 1980s to reduce barriers to trade, including the North American Free Trade Agreement, China's entry into the World Trade Organization, presidential Trade Promotion Authority, the Central American Free Trade Agreement, and pending trade agreements with South Korea, Panama, and Colombia.

In the past 30 years, labor unions have pushed for higher trade barriers in the form of "domestic content" requirements for autos sold in the United States, import quotas for textiles and steel, and the Gephardt amendments of 1986–87 that would have imposed sanctions on imports from nations that ran large bilateral trade surpluses with the United States (Destler and Balint 1999: 19). More recently,

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unions have lobbied for higher tariffs, quotas, or outright bans on imported steel, tires made in China, and Mexican-driven trucks on U.S. highways. Labor leaders lobbied hard for the "Buy American" provisions in the $800 billion stimulus package that Congress approved and President Obama signed in early 2009.

Labor leaders such as Richard Trumka of the AFL-CIO and James Hoffa of the Teamsters union express the fears of many of their members that free trade and globalization have reduced the scope and power of organized labor in the United States. They see import competition and the ability of U.S. companies to locate production abroad as direct threats to the living standards and bargaining leverage of the union members they represent.

Organized labor was not always uniformly hostile to trade liberalization. In the 1930s, labor leaders supported the Reciprocal Trade Agreements Act that allowed the Roosevelt administration to negotiate bilateral agreements to roll back high tariffs that had been enacted by President Hoover and a Republican Congress.

In fact, labor unions in most industrial countries resisted the rising protectionism of the interwar years. Back then, labor leaders and the left-of-center parties they supported understood trade policy more as a means for delivering lower prices to workers rather than protected markets to producers. In her book *Who Adjusts?*, Simmons (1994: 197) noted:

> One of the prime effects of tariffs in the interwar years was that they improved the return to capital in import-competing industries while raising the price of imported consumer goods to the working classes. One left-wing party after another lowered tariffs when it came to power: the American Democrats reversed the high tariff policy of the Republicans after 1932, and the Front Populaire lowered tariffs in France in 1936. Even where they did not have the electoral power to block protection, parties of the Left were the voice of free trade. Hence, the British Labour party opposed the General Tariff of 1931; and Belgian Socialists inveighed against tariffs and quotas because of the effect these policies would have on the cost of living for workers.

U.S. labor unions continued their support for trade after the war, endorsing the Trade Expansion Act of 1962, which authorized negotiations that led to the ambitions Kennedy Round agreement with members of the General Agreement on Tariffs and Trade in 1967 (Destler and Balint 1999: 15). In the first decades after World War II, U.S. organized labor was, in the words of trade historian I. M. Destler (1998: 389), "a consistent and reliable member of the free-trade coalition that found a comfortable home in the Democratic Party."

Labor leaders began to express disenchantment with trade in the early 1970s as U.S. industry faced increased competition from a resurgent Western Europe and Japan. Machine tools, automobiles, and consumer electronics such as radios and TVs were industries where U.S. producers had dominated after World War II but where import penetration grew. In the face of competition, a growing number of industries and their unions began to seek import relief by the 1970s.

The United Auto Workers union was conspicuous during the decade for its continued support for an open automobile market, but then turned against free trade as imports of smaller, more fuel-efficient Japanese imports rose sharply along with oil prices and a steep industrial recession gripped the nation in 1981–82. Job losses were especially steep in more unionized sectors such as steel and other heavy industry, and in more unionized regions of the country such as the upper Midwest. As the 1980s unfolded, private-sector labor unions in the United States had become monolithically skeptical of trade liberalization.

## Trade Expands, Union Membership Contracts

Are union leaders and members justified in their opposition to trade liberalization? Has the recent growth of trade and globalization been detrimental to the labor movement? For a variety of reasons, the recent era of globalization has not been kind to the labor movement. In theory, increased competition in product markets can be expected to undermine the bargaining power of unions in labor markets. Circumstantial evidence would seem to reinforce the theory, although the story of unions and globalization has proven to be much more complicated.

Two broad trends are undeniable. In recent decades, the share of private-sector workers who belong to labor unions has been declining in most developed countries, while at the same time levels of trade, foreign investment, and other measures of globalization have been rising rapidly.

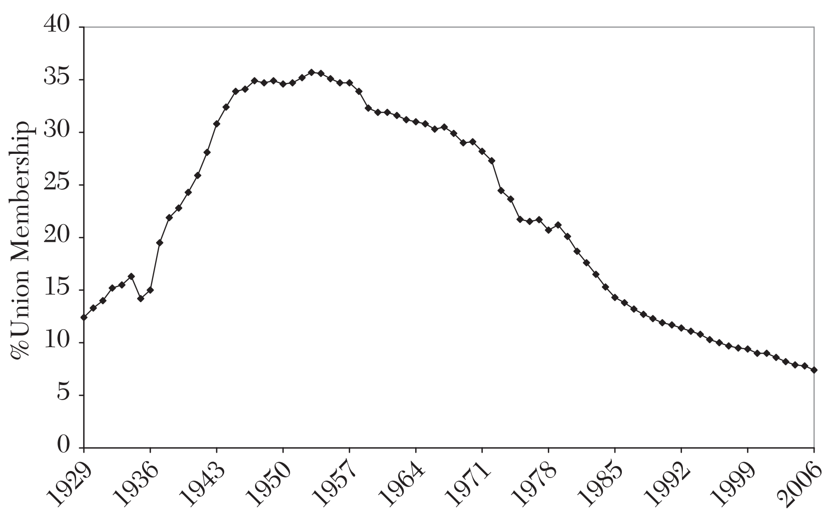
Union leaders who blame globalization for their declining membership and power can point to a lot of circumstantial evidence to support their fears. The share of private-sector American workers who belong to labor unions peaked at 36 percent in 1953-54, then declined slowly through the 1960s and more sharply beginning in the early 1970s. By 2006, private-sector union density had fallen below 8 percent (see Figure 1).

During that same time frame, cross-border trade in goods, services, and assets has expanded dramatically. The ratio of imports to gross domestic product (GDP) in the United States has nearly quadrupled in the past 40 years, from 6 to 23 percent; the ratio of exports to GDP has nearly tripled, from 6 to 17 percent. The ratio of foreign investment to GDP has grown even more rapidly. In 1976, the sum of U.S.-owned assets abroad and foreign-owned assets in the United States was equivalent to about 40 percent of our GDP; by the end of 2008, the sum total of cross-border assets was nearly three times our GDP (Griswold 2009: 4).

The phenomenon of declining union membership is not unique to the United States. Between 1990 and 2003, union densities declined in 21 of 24 industrialized nations surveyed by the U.S. Department

FIGURE 1

U.S. Private Sector Union Density, 1929–2006




Source: Hirsch (2008a: 156).

of Labor. The decline was especially sharp in the United Kingdom, Australia, and Japan (Visser 2006: 45).

Union membership has not only shrunk during the era of globalization but unions have become less militant. After peaking in the 1970s, the number of days lost to strikes plummeted into the 1990s. In a survey of 15 major industrialized countries, not including the United States, Piazza (2005: 290) calculates that the number of days per worker lost due to strikes was 1,641 in the 1960s, 2,586 in the 1970s, 1,632 in the 1980s, and a mere 658 in the 1990s.

## How Product Competition Undermines Labor Monopolies

Economic theory offers a number of reasons why growing international competition would be damaging to the interests of labor unions. More competition in product markets means greater elasticity of demand for labor—that is, global competition means that demand for labor is more sensitive to any change in wages. Employers competing in global markets cannot simply pass higher wage costs along to consumers in the form of higher prices because consumers themselves can choose to buy substitute products from lower-cost, often nonunionized producers.

Expanding capital mobility means that employers are more able to shift production to lower-wage countries if necessary. A more mobile company is better able to threaten or employ an "exit" option in response to union demands. In the face of product competition and capital mobility, union demands for higher wages can lead instead to fewer domestic union jobs, as has been the case in a number of firms and industries.

In contrast, in markets insulated from robust competition, unions can more readily demand a share of a company's or industry's profits without fear of compromising the survival or competitiveness of the employer. Insulated markets create rents in the form of above-market profits that unions can then bargain with management to divide between them at the expense of the consuming public.

As a result, union densities tend to be much higher in the public sector or in heavily regulated industries, where competition is much reduced or lacking entirely compared to the nonregulated private sector. According to the U.S. Current Population Survey (Hirsch and Macpherson 2009), the unionization rate in the public sector was

36.8 percent in 2008 compared to 7.6 percent in the private sector. Rates of unionization were above 50 percent for railroad conductors and locomotive engineers; parking enforcement workers; Postal Service mail carriers, sorters, and clerks; fire fighters; subway, streetcar, and rail transport workers; electrical power line installers and repairers; and secondary school teachers. All those occupations are concentrated in government or regulated sectors.

On the policy front, globalization may also encourage governments to adopt laws less friendly to unionization. Globalization can enhance the appeal of more pro-market ideas that favor greater competition in labor as well as product markets. It can also put pressure on governments to side more with management in the name of competitiveness in global markets. The result can be right-to-work laws, which allow individual workers more freedom to opt out of union contracts, and other laws that make workplace organization more difficult.

Technology has also worked to increase competition in product markets and therefore weaken the organizing and bargaining power of unions. The spread of computers and the Internet have opened more sectors to competition, reducing both barriers to entry and the advantages of scale and centralized production. This has allowed new firms to enter product markets and compete with more established producers, eroding industry profits and potential gains for union members through bargaining. As Pencavel (2008: 427) summarizes, "Essentially, in the last few decades, product markets in the developed world have become much more competitive and, therefore, less accommodating to the wage-making activities of labor unions."

Increased trade and globalization can in theory also work in favor of labor unions in a way that at least partially offsets the negative forces. Multinational companies more dependent on supply chains and "just-in-time" inventory management are potentially more vulnerable to strikes by their unions. A study of labor relations in Germany, for example, found that the competitive pressures of globalization actually enhanced the bargaining power of unions. Thelen and Wijnbergen (2003: 860) found that "employers are more dependent than ever on stable relations with labor at the plant level and more vulnerable to overt industrial strife."

A more internationalized economy can, depending on a country's stage of development, expand certain core areas of manufacturing with traditionally higher union density. Indirectly, if expanding trade contributes to a perception of rising worker insecurity about jobs and wages, it could spur more workers to be favorable toward unions as a way to bolster job security. And by increasing overall growth and productivity, globalization can raise the living standards of union members if not the scope and power of unions themselves.

A final mitigating factor is that, despite perceptions, the large majority of workers are simply not exposed to direct competition with foreign workers. Most workers are employed in service sectors that by their nature are not widely traded across international borders, including government-provided services. As Scruggs and Lange (2002: 151) conclude, the impact of globalization on unions tends to be exaggerated because "much of the economy, even in the private sector, is not directly affected by the capital mobility promoted by globalization; for instance, personal services, domestic transportation, and communication are more sheltered from international competition than export manufacturing or financial services."

## Nontrade Factors behind Declining Union Density

Labor leaders have focused most of their attention on the negative impact of import competition on their movement. The story they tell is straightforward: competition from lower-wage countries and producers has caused unionized U.S. industries to shrink, disproportionately affecting union members and contributing heavily to the decline in union density. The empirical evidence of the past few decades, however, offers little support for their story. Most recent research finds, despite the theoretical connections, that trade plays at most a small role in the decline of unionization.

The actual evidence on globalization and unions is mixed, and points in some unexpected directions. In a comprehensive study of the impact of trade on U.S. labor unions, Baldwin (2003) concluded that the decline in union density in the United States has not been driven by a shift of employment from unionized sectors to non-unionized sectors, but by a broad economy-wide decline of unionization across sectors and regions.

Examining shifts in unionization rates across two decades, Baldwin (2003: 4) found that only a small share of the decline could be attributed to between-industries shifts in national employment shares from more unionized to less unionized industries. From 1977 to 1987, only a quarter of the decline was caused by shifts between industries, and from 1987 to 1997, only 10 percent.

Most of the decline in unionization rates was because of declines within sectors.

In the 20-year period Baldwin (2003: 7) studied, unionization rates declined in 73 out of 74 manufacturing sectors and 46 out of 56 services sectors. Nor is the story one of production shifting from union-friendly states to "right-to-work" states. Baldwin also found that unionization rates fell across regions of the country.

Shifting employment to less unionized service sectors or less unionized Southern states, Baldwin (2003: 66, 68) concluded,

> play at best a modest role in explaining the decline in unionization rates. The decline is ubiquitous, in all sectors and regions, suggesting deep fundamental sources such as growing employer opposition, unfavorable legislative trends, and declining worker trust in union institutions. . . . The main finding from my regression analysis is that factors other than changes in trade account for most of the large decreases in the number of union relative to nonunion workers.

Other nontrade factors contributing to the decline of unionization include the more rapid growth of certain categories of workers, such as women, southerners, and white-collar workers, who are less favorable to unionization; the deregulation of transportation industries; declining efforts of unions to organize new members; government activity that substitutes for union services, such as unemployment insurance, industrial accident insurance, leave policies, and other workplace regulations; the decline in pro-union attitudes among workers; and increased resistance among employers.

## Inward Foreign Investment and Social Integration

Although the evidence is lacking to implicate globalization as a whole, two aspects of the trend have been found to have significant negative effects on labor unions: inward foreign direct investment (FDI), and "social integration" across borders.

In a 2007 study, "Globalization and Declining Unionization in the United States," Slaughter (2007: 342) found no robust correlation with union coverage and exports, imports, or net exports, but he did find a surprising correlation with direct investment in the United States. Greater FDI in a sector was strongly and significantly associated with a lower number of unionized workers.

This has not been a simple story of employment shifting from more unionized domestically owned companies to less unionized foreign-owned affiliates. According to Slaughter, union membership within domestically owned companies has fallen more rapidly than employment has grown at foreign affiliates. And U.S. affiliates of foreign-headquartered firms actually have higher average unionization rates than U.S.-based firms (Slaughter 2007: 342–43).

The principal impact of inward FDI on labor unions appears to be the "demonstration effect." According to Slaughter, the presence of foreign-owned affiliates in an industry sends the signal that capital is mobile. Firms that can enter a market across borders can also exit. Slaughter cites evidence that manufacturing affiliates in the United States and United Kingdom are more likely to shut down than domestically owned producers (Slaughter 2007: 334). The correlation of FDI and declining rates of union density suggests that "many workers feel greater insecurity from seeing capital mobility in their sectors, even if not in their own particular firms," Slaughter (2007: 344–45) concluded.

Another factor of globalization that works against unionization is the rising social contact that accompanies economic globalization. According Dresher and Gaston (2007: 174–75), "unionization significantly decreases with rising social globalization," which they define as "the spread of ideas, information, images and people." This aspect of globalization tends to undermine the status quo and promote acceptance of new concepts, policies, and institutions, which can work to weaken the power of unions to control markets and competition.

Social globalization reinforces what Dresher and Gaston (2007: 176) call a "growing normative orientation towards individuals rather than collectivism [which] makes collective organization more difficult." Adding to the trends are rising levels of immigration and perceptions of younger workers who view unions as old-fashioned and anachronistic institutions.

In their study, Dresher and Gaston analyzed unionization rates and various measures of globalization over time in 17 major, developed countries, including the United States. Under the heading of "social integration," they considered outgoing telephone traffic, remittances, international tourism, the costs of phone calls to the United States, foreign-born as a share of the population, telephone mainlines per 1,000 population, Internet hosts per capita, Internet users, cable TV penetration, daily newspapers, radios, and even the number of McDonalds restaurants. After analyzing those and a number of other globalization variables, Dresher and Gaston (2007: 180) "confirm that economic integration has *not* affected union membership. However, we found that social integration has been *very* important.… the social dimension of globalization has adversely affected union membership."

Globalization has indeed affected levels of unionization in the United States and other developed countries, but not in ways commonly believed. The evidence is lacking to blame imports from low-wage countries, or the decline of more unionized sectors in relation to those that are less unionized. The major driving forces behind the decline in union densities are primarily domestic and cut across regions and sectors. The effects of globalization on union membership are secondary and work through unexpected channels such as inward direct investment and a softer social globalization that has changed perceptions of labor unions.

## How Unions Affect the Competitiveness of U.S. Industry

While globalization has affected labor unions in surprising ways, unions have also had a measurable effect on the ability of firms to compete in the global economy. The 1984 publication of *What Do Unions Do?*, by Freeman and Medoff, launched a growing body of research into the effects of labor unions on the performance of unionized firms compared to nonunionized firms. The evidence indicates that unions and globalization are not a happy mix for companies with unionized workforces.

Freeman and Medoff noted in their landmark work that the impact of unions on the workplace reveals itself in two faces, a "monopoly face," which tends to reduce the efficiency of the affected firm, and the "collective voice/institutional response face," which can raise productivity by encouraging worker loyalty and reducing turnover.

The monopoly face of unions can be seen in their efforts to fix wages and benefits at levels above those of a competitive labor market. A labor union is, among other things, a cartel or monopoly that attempts to exert market power to extract a higher price for the labor it offers to a firm. Like monopolies in product markets, the result can be a misallocation of resources. Higher wages cut into firm profits, reducing investment and employment levels in the affected industry. Unions can also impose restrictive work rules and featherbedding that reduce productivity and stifle innovation. An emphasis on seniority over merit in pay and promotion can reduce the incentive for worker effort. One result can be the inability of management to respond in a timely way to changing market conditions, putting the firm at a competitive disadvantage. Strikes and other industrial action can damage a firm's ability to retain market share.

On the positive side, as summarized in Bennett and Kaufman (2008: 3), unions can reduce worker turnover and increase their sense of loyalty to the firm, thus reducing transaction costs to the firm for hiring and training. The effect is consistent with the efficient-wage theory, which argues that paying workers an above-market wage can yield benefits to the firm that more than offset higher payroll costs. The protection of a union can empower individual workers to suggest workplace improvements, exercising the option for "voice" rather than "exit." The organizing of a union can shock management into organizing production more efficiently to maintain competitiveness. Unions can enhance the representation of older, more experienced workers rather than allowing wages and benefits to be determined by more mobile, "marginal" workers who tend to be younger and single.

Freeman and Medoff came to the conclusion in their influential book that the voice/representational face of organized labor tends to predominate the monopoly face, with the result that unions on balance play a positive role in enhancing the output and competitiveness of unionized firms. Twenty-five years later, however, the evidence does not support their more optimistic view of the impact of organized labor on the competitiveness of U.S. companies in the global markets.

The weight of evidence indicates that, for most firms in most sectors, unionization leaves companies less able to compete successfully. The core problem is that unions cause compensation to rise faster than productivity, eroding profits while at the same time reducing the ability of firms to remain price competitive. The result over time is that unionized firms have tended to lose market share to nonunionized firms, in domestic as well as international markets.

After studying the effects of unions on firm performance, and surveying the literature, Hirsch (2008a: 154) concluded that unions will typically raise labor costs to a firm by 15 to 20 percent, while delivering a negligible increase in productivity. "Unions have, at most, small positive (but variable) effects on productivity insufficient to offset the substantial compensation gains, thus leading to lower profitability. Unionization is associated with lower investment in physical and intangible capital and slower growth," he wrote, concluding, "The combination of a union tax and sluggish governance is proving debilitating in economic environments that are highly competitive and dynamic."

The "union tax" has caused firms to underperform in a number of areas. Studies cited by Hirsch (2008b: 212) find that the profits of unionized firms are 10 to 20 percent lower than similar nonunion firms. The typical unionized firm has 6 percent lower capital investment than an equivalent nonunion firm, and a 15 percent lower share of spending on research and development. The change in a firm's capital investment in response to union certification is equivalent to a 30 percentage point increase in the corporate tax rate (Hirsch 2008b: 211).

Further evidence of the negative impact of unions on firms can be found in capital markets. Lee and Mas (2009: 5) found that the organization of a union did not have an immediate impact on the operating performance of the firm but was instead reflected in the longer-term market value of the affected business. They found that a successful election to unionize produced negative returns of 10 to 14 percent for about 15 months afterward. That translates into a decrease in the market value of the affected business by at least $40,000 per worker eligible to vote (in 1998 dollars). The authors describe the reduction in equity value as "a combination of transfer to workers as well as lost profit due to inefficiencies caused by the union."

## Unionized Firms Just Fade Away

In competitive product markets, the drag that unions impose on firm performance can be debilitating to the firm and its workers over time. As described above, firms facing vigorous competition are not able to pass along higher costs to consumers without risk of losing significant market share. Newly unionized firms in such markets face the cruel choice of passing along higher labor costs to consumers, thus losing market share to more cost-efficient competitors, or eating the higher costs in the form of lower profits and less reinvestment in physical and intellectual capital. Either choice will result over time in an erosion of the unionized firm's market share.

The negative impact of unionization can be blunted if product markets are less competitive, or if the rest the industry is unionized. As Hirsch (2008b: 199–200) explains:

> For a union firm in a reasonably competitive, largely nonunion industry, cost increases cannot be passed forward to consumers through higher prices. Thus, absent a productivity offset, unions should have little bargaining strength. Substantial union wage premiums in a competitive setting absent productivity improvements should lead establishments to contract over time. If a sizeable proportion of an industry is unionized, industry-wide wage increases absent productivity offsets increase costs throughout the industry, costs increases are passed through to consumers, and no individual firm is at a severe disadvantage. But such a situation is difficult to sustain in the long run, if entry/expansion of nonunion companies is possible or products are tradable on world markets.

The inescapable conclusion is that unionized companies in the United States have performed poorly relative to nonunion companies. To the extent that output and resources are mobile, poor union performance has led to a shift of production and employment away from unionized industries, firms, and plants and into the nonunion sector or to producers overseas.

Interestingly, the evidence does not show a higher failure rate among unionized firms. While more highly unionized industries are subject to more employment contractions, fewer expansions, and fewer plant "births" than nonunionized counterparts, there is no evidence of more frequent plant "deaths." As Hirsch (2008b: 218) concludes, "Rent seeking unions are willing to drive enterprises toward the cliff but not over it."

The overall trend of the American economy during the era of globalization has not been toward "deindustrialization" but "deunionization." Union density in the private sector has not been falling because of a major shift of employment from unionized manufacturing to nonunionized services. Instead, the real shift has been from unionized manufacturing to nonunionized manufacturing. According to Hirsch (2008a: 156–57), nonunion manufacturing employment held steady from 1973 to 2006, while total employment of unionized manufacturing workers fell sharply. Nowhere has this trend been more evident than in the automobile industry. While total auto manufacturing employment in the United States during that same period was remarkably steady, the share of unionized workers in the industry fell from 71 percent to 26 percent as production migrated to foreign-owned nonunion plants, mostly in Southern, "right-to-work" states (Hirsch 2008a: 170). Like other sectors, heavy unionization has not proven to be a successful production model in the competitive U.S. automobile industry.

## Bringing Labor Markets into the 21st Century

Private-sector unionization achieved its greatest success in the middle decades of the previous century, in an era when domestic and global product markets were much less open and competitive. U.S. producers faced less competition, allowing unions to extract higher wages from the rents their employers were able, in turn, to extract from a relatively captive consumer base.

Unions had originally been established in the late 19th century in part to offset and oppose the market power of protected capital, but by the 1930s unions had collaborated with the government and certain businesses to stifle competition. F. A. Hayek, in his classic 1944 book, *The Road to Serfdom,* noted the turn of organized labor against competitive markets. "The fatal turning point" occurred, writes Hayek (1944: 199), when the labor movement

> came under the influence of anti-competition doctrines and became itself entangled in the strife for privilege. The recent growth of monopoly is largely the result of a deliberate collaboration of organized capital and organized labor where the privileged groups of labor share in the monopoly profits at the expense of the community and particular at the expense of the poorest, those employed in the less-well-organized industries and the unemployed.

In the decades since Hayek wrote those words, barriers to international trade and investment have fallen, and domestic markets, including transportation, energy, and telecommunications, have been largely deregulated. Meanwhile, new technologies such as the Internet have helped to lower barriers to entry into existing markets.

The result has been a loss of market power for both "organized capital" and "organized labor."

U.S. industries, on the whole, have accepted and even embraced the more competitive environment. Sectors such as steel, textiles, and sugar continue to demand protection from foreign competitors, but they are now the exceptions and not the rule. But leaders of organized labor, on the whole, do not accept the new, more competitive environment. They routinely oppose any efforts to further liberalize trade and tend to favor efforts to raise barriers to imports and capital mobility.

A return to the era of more closed and regulated markets should be strongly resisted. Although labor leaders may have seen that period as a golden era, it extracted a heavy price on Americans in the form of lost consumer welfare, product innovation, and freedom. The preferable policy alternative is to allow competition to work in labor markets just as it has been allowed to work more fully in product markets.

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