

## CHICAGO COUNCIL ON URBAN AFFAIRS

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### **The City of Big Shoulders in a Shrinking Globe?**

I'm very happy to be here and welcome this opportunity to discuss a topic that's so important to the well being of our city and our region. I'd like to thank the Chicago Council on Urban Affairs for bringing together such an esteemed group of community leaders, with representatives from the Chicago Council on Foreign Relations, the Chicago Hong Kong Development Council, the Cosmopolitan Chamber of Commerce, the Latin American Chamber of Commerce, and the MEGA Center. It's a good sign to see so many diverse groups working together to benefit our city.

As indicated in the introduction, I have some experience and a deep personal interest in trade issues, an interest that continues with my current responsibilities at the Federal Reserve Bank. As the nation's money manager, the Federal Reserve is responsible for fostering a sound economy and a stable financial system. In today's environment, understanding global trade issues is, of course, an important part of the job.

My remarks this morning, however, do not focus on these national issues. Rather, I'm focusing on local concerns, specifically Chicago's involvement in the global economy. I'm an economist by training, a practitioner of the dismal science. As someone once said, an economist is someone who's too boring to be an accountant. I don't usually have a chance to discuss something that's been such a hot topic in the general press.

I'm heartened by the interest in international trade but disheartened by the fear and confusion surrounding the issue. Just a few days ago, for example, I came across a letter on the subject in a column by the Chicagoan Ann Landers. I thought this letter was interesting because it summed up a lot of the anger about global trade. Here's an abridged version:

“Dear Ann: Do you have room for one more letter about why young people are not getting jobs? I know why. Check the manufacturer's tag on the back of your blouse, dress, coat, or suit. Chances are

good that they were made in Sri Lanka, Bangladesh, Pakistan, Thailand, or Indonesia. Do us all a favor, Ann. Tell your readers to check the tags on their clothing and refuse to buy anything not made by our fellow citizens.”

The letter obviously comes from the heart. But today I'd like to make the case that this writer has it all wrong. In fact, the best way to ensure as many jobs as possible and the highest standard of living here at home is to keep our markets open. This has special implications for us here in Chicago. Simply put, the best way to create jobs here and invigorate the local economy is to plunge headfirst into the global economy.

### Fear About The Global Economy

Despite the controversy in the media, economists agree on the value of international trade. And economists aren't known for agreeing with each other. You've probably heard the joke that if you lay all the economists in the world end to end, they won't reach a conclusion. And the follow-up, that if you lay all the economists in the world end to end, it probably would be a good idea. However, while we economists may disagree about everything else, almost all of us agree that open markets and free trade benefit the economy.

So why is there so much apprehension about globalization? One of the reasons is that it all seems so new. Yet globalization has been with us a long time, just more so lately. Back in 1914, for example, John Maynard Keynes, while sipping tea in bed, used his telephone to make investments around the world. “The internationalization of economic life is nearly complete,” he asserted.

Many people are also concerned about the seeming instability of a global economy. Again, though, this is nothing new. During the 1840s, several states in the rapidly developing U.S. repudiated their debt to British lenders following a severe recession. British investors were outraged. Even Charles Dickens commented on the scandal. In *A Christmas Carol*, Scrooge's nightmares include having his solid British assets turn into a, quote, “mere United States security” unquote.

What are the positive effects of trade? There are many, but today I'd like to focus on the opportunities for U.S. and local businesses to increase exports. Since 1987 about one third of all U.S. economic growth has come from exports. This trade has real benefits for our economy. It's estimated that for every billion dollars in exports, there are about 16,000 new U.S. jobs created. And these export-related jobs are high-paying, with wages exceeding the U.S. average by 13 to 17 percent.

We usually hear a lot about the success or failure of large firms in the global marketplace, but small- and medium-sized businesses are responsible for much of the export market. In fact, the top fifty U.S. exporters account for only about one third of all U.S. exports. Illinois companies included here are giants like Deere, Abbott Labs, Motorola, and Caterpillar. This, of course, means that the other two thirds of U.S. exports come from smaller firms. Clearly, the export market provides tremendous potential for both large and small firms.

There is a message for Chicago here too — We can help create local jobs and strengthen the Chicago economy by getting involved in the global economy.

## Increased Importance of International Trade

Some may say we don't need international trade to help the Chicago economy. These critics say businesses can make it by concentrating on the domestic U.S. market alone. After all, it is the largest in the world.

It is true that the U.S. accounts for about 25 percent of the world's economic activity and roughly 50 percent of its financial wealth. In comparison, the U.S. economy accounted for about 35 percent of the world economy thirty years ago. We're not getting smaller – the rest of the world is catching up.

It's also true that most U.S. firms produce for our own domestic market. While the percent of exports is growing, it's still comparatively small.

The U.S. economy is so large that many U.S. firms have been able to stay domestic. However, we have many mature markets and the populations of developing countries are growing more rapidly, creating larger markets for U.S. exports. Some estimate that the world market will grow as much as 40 percent faster than the U.S. market through the year 2000. As large as the U.S. market is, the world market is four times larger. It makes sense to trade in the large, fast-growing global market. Trading only in the domestic market limits our potential.

It's not surprising that foreign trade has grown so rapidly. First, as I said, the population of the rest of the world is simply growing faster than it is here, creating larger markets. Second, we have recently seen a substantial reduction in trade barriers, notably the NAFTA and numerous GATT agreements, the most recent being the Uruguay Round. Third, improved and less expensive transportation and communication makes trade much easier. This means that a lower volume of sales is required to reach the "critical mass" for effective entry into world trade, which provides more opportunities for small businesses. A telephone or a FAX machine may be all that's needed. Today even small firms have the ability to buy and sell materials and components all over the world. In turn, this also allows them to reduce costs and make higher quality products.

Competing on a global basis enhances the competitiveness of U.S. firms. If you ignore the rest of the world, you simply limit your own potential. If you want to be the best, you must be able to succeed in the home market of your competitor. Otherwise, you're always on the defensive. You must go on the offensive. Entering competitors' home markets forces you to improve. I should also say that you must remain competitive in your home market, because you can be sure that foreign competitors are going to be active here.

There is more and more evidence that U.S. firms fare very well in this competitive environment. Recent studies by the Organization for Economic Cooperation and Development (OECD) indicate that the U.S. is one of the most competitive economies in the world. Measured by relative unit labor costs and relative export prices in manufacturing, U.S. competitiveness has improved more significantly than most of our major competitors, including Germany, France, England, and, yes, even Japan. The key reasons include the fact that the U.S. economy has been relatively open, and firms responded to global competition by becoming more productive. The competition can be tough. For many firms, becoming more competitive is a matter of survival.

I'm speaking of the whole U.S. economy now. While the economy as a whole can be better off, a local plant may close, putting hundreds or even thousands of people out of work. Deciding how to respond to this reality of the market place is an on-going issue of public debate. In my view, society has an obligation to assist those who have lost their jobs because of reduced tariffs that benefit the economy as a whole. In the long run, competition results in healthier, more efficient firms and a higher standard of living. We must do everything we can to encourage this competition while at the same time help those adversely affected.

I'm focusing on exports today, but it's worth saying that open markets also provide opportunities for imports and foreign direct investment. In 1994, imports accounted for about 28 percent of total goods consumed in the U.S. This 28 percent may seem like a high number, but keep in mind, I'm talking only about goods, not services. Few people question that imports provide benefits to consumers, such as a greater array of high quality goods at lower prices, resulting in a higher standard of living.

The same holds true for businesses. With access to less expensive intermediate goods, manufacturers can lower their costs of production and sell their products at very competitive prices.

U.S. consumers and workers also benefit from foreign direct investment. This investment results in a larger pool of funds, opportunities, and resources. There's a number of examples here in the Midwest, such as the Mitsubishi plant in Bloomington, Illinois, the Matsushita consumer electronics plant in Elgin, Illinois, and the French manufacturer, Thompson Electric, with a plant in Indianapolis, Indiana. All have created jobs, income, and production here.

### Midwest In Global Economy

The Midwest is already a successful, active competitor in the global economy. Canada is the region's largest trading partner, receiving almost half of the Midwest's manufacturing exports. The region also exports heavily to the advanced Asian economies, particularly Japan, and the western European economies, notably the United Kingdom and Germany. These four countries account for almost two thirds of Midwestern exports.

Here in Illinois, we're the sixth leading exporting state in the nation, up from eighth just two years ago. More than half a million Illinois jobs are supported by exports — about 1 in 8.

A bright spot offering tremendous opportunities for future Midwest and Illinois trade is the third world. Midwestern firms in general, and Illinois firms specifically, produce what the world's most rapidly growing economies need — industrial machinery, telecommunications equipment, electronics and electrical equipment, and financial services. In other words, the products and services needed to build a strong economy.

The U.S. Department of Commerce has identified ten so-called BEMs, or Big Emerging Markets, in Latin America, central and southeastern Europe, Africa, and the Pacific Rim. These BEM countries have large populations, are political leaders in their regions, and, most importantly, have economies that are growing twice as fast as the rest of the world's.

Illinois is already heavily involved in exporting to two of the BEMs — Mexico and China. Illinois exports to these two countries grew more rapidly than others between 1987 and 1994. While the actual amount of trade may not be large now, the potential, particularly the potential with China, is huge.

Regarding Mexico, almost all Illinois industries saw exports grow significantly during this period. However, the devaluation of the peso in late 1994 and Mexico's sharp economic downturn in 1995 have temporarily reversed this trend. As the Mexican economy improves, we can expect renewed gains in exports to this market.

So there is no confusion, let me clarify that the Mexican peso problem was an internal problem and was not caused by the NAFTA. In large part, the NAFTA extended and formalized an already dramatic opening of the Mexican economy during the previous five years. The lesson to be learned from the peso problem is that international business can be risky, and firms that want to take advantage of the significant rewards also must accept risk. That's what we mean by a free market system.

### Chicago in the Global Economy

I'd like to focus now on Chicago and discuss the city's participation in the global economy.

Chicago starts out with significant advantages. It is an international city. We have many different ethnic groups, and nearly 50 branches of foreign banks located in Chicago. Our commodity and futures exchanges are truly international operations with links to exchanges all over the world. O'Hare Field, the busiest airport in the world, is a significant international transportation facility. We have major universities of world class quality with heavy concentrations of foreign students.

To continue to build on these advantages and enhance trade, there are three requisites. First, you have to have strong competitive businesses here at home. Second, you have to provide these businesses some export assistance. Third, you have to have trade agreements that open markets. I've already indicated that we have the first requisite, competitive firms selling what the world needs.

Regarding the second requisite, export assistance, Chicagoans are working to put together a solid export infrastructure. There was a time when many different agencies were trying to offer export assistance, but no one knew what the others were doing. Now many of these groups are working together, as evidenced by this group here this morning.

On the federal level, we have here in Chicago a U.S. Export Assistance Center, which brings together representatives from the Department of Commerce, the Export-Import Bank, and the Small Business Administration. On the state level, we have the International Business Division of the Illinois Department of Commerce and Community Affairs. These organizations offer a variety of assistance programs for businesses and are good places to start if you're just beginning to export.

In addition, there are many private and not-for-profit organizations working to promote trade. A group that I was personally involved with prior to joining the Fed — the Illinois Coordinating Committee on Exports — was established by Governor Edgar to coordinate the efforts of all these groups, both govern-

ment and private. Now headed by Gary Edson, a friend and colleague from my trade representative days, the ICCE publishes a newsletter, directory of services for exporters, and a common calendar of events, as well as conducts research. This type of coordination and communication is important in expanding opportunities for Illinois trade.

The third requisite is trade laws that open markets. As I mentioned, we've made significant progress in this area with the NAFTA and GATT. These are good agreements because they lower trade barriers. On a local level, they certainly benefit the Midwest and provide a great opportunity for Illinois. To give you an example, in the agricultural sector, the agreements lower foreign barriers on corn, dairy products, pork, and poultry, and in the industrial sector, they eliminate tariffs on agricultural equipment and paper products. As I said, we're very competitive here in the U.S. and in the Midwest. We're tough to beat. Overall, it's to our advantage to lower these barriers.

## Conclusion

In conclusion, I'd like to emphasize the need to guard against protectionism. Rather than closing markets and reducing our opportunities, we should look to expand trade and open foreign markets through agreements like the NAFTA and GATT. While the current agreements are good beginnings, there's more to do, particularly in the areas of telecommunications, financial services, and intellectual property rights. Also we need to be careful that regional trade agreements don't encourage trade only within the designated region. The goal of the agreements is to open markets world wide.

It's not easy to compete in a global economy, but staying out is not a realistic option. It's where the growth markets are; it's where the opportunities for Chicago businesses are. Firms, small and large, increasingly understand the need to be aggressive global competitors. Local citizens and local governments are also taking significant steps to support exports.

The crucial point to remember is that competing in the global economy helps us here at home. We've seen that it is the way to create local jobs, stimulate the local economy, and enhance our local standard of living. In this case, the best defense is a good offense.

French explorer Robert de La Salle once wrote that Chicago was a place where settlers would have to be particularly enterprising. "Each day as he rises," de La Salle wrote, the typical Chicago citizen exclaims, "I act, I move, I push." When it comes to global trade, I encourage all of us to act; to move; to push.

Chicago is no longer the hog butcher of the world, but we still have big shoulders. We still make what the world wants, and we have sold and will continue to sell it to the world.

Thank you.