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Definition: Trade Sanction

-Refusal to trade with another country for political reasons, usually in an effort to influence behavior of that country. In an extreme form: an embargo.

More on Globalization: Trade explains part (approximately 30%) of the rising skill premium. The main cause, however, is considered to be technology, which has increased the return to skilled labor, "skill-biased technical change."

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Labor Standards and Trade

I. What Are They?

- Requirements for how to treat labor well rather than poorly.
- Formal list made by the ILO (purpose to improve treatment of labor worldwide). Members of the ILO include representatives from governments, business, and labor unions. The list features "conventions" or standards (more than 180 of them) and "recommendations." The conventions are like treaties, in that countries can choose to ratify them.
- See the handout on 8 Fundamental ILO Conventions.
- Note that even though ILO conventions are signed and ratified by some nations, it does not mean that they are not violated or that they are necessarily enforced within those nations.
- See handout Labor Standards Found in U.S. Trade Law
- GSP = Generalized System of Preferences: Have lower tariffs on developing country goods than the tariff levels on DC goods. Possible to remove the lower tariffs (for higher tariffs) if labor standards are not met.
- Often in agreements with other nations the U.S. will include labor standards. These standards include things not on the ILO list (e.g. minimum wage, hours of work, safety, health, and enforcement).
- See handout: Labor Standards in U.S. Trade Policies (no need to memorize).

ISSUES

II. Should Labor Standards Be Promoted?

- Of course, it would be better if labor were treated better. But is it a good idea to legislate these standards?
- Minimum wage example (see graph)
- If we impose a minimum wage, the results depend on where the wage is set. If the wage is set at the equilibrium level or below, it has no effect. If it is set above the equilibrium level (competitive equilibrium!) it will cause

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unemployment. This is illustrated in the graph: at W_{min}, the quantity of

labor demanded by firms is reduced and unemployment (supply minus demand) rises. A similar story can be told with labor standards (as in, they can often be interpreted as increasing in the wage or the cost of labor).

- The result for welfare illustrated on the graph is ambiguous. Some workers are made better off, because they have higher wages and some are made worse off by becoming unemployed. (Analysis similar to what we've used for tariffs and other markets consumer and producer surplus can be used to show that the net effect of the minimum wage is negative, but this is less important than the harm that it does to those who lose.)
- Major concern: Imposing higher labor standards in LDCs may create unemployment thus leaving more people with even less money.
- Example: Suppose we go into Indonesia and insist companies treat their
 workers better. Some companies may leave Indonesia in search of places
 with higher productivity (assuming workers in Indonesia were receiving
 lower wages because they were less productive). This will cause a very
 large increase in unemployment. So, it turns out that workers can be hurt
 by labor standards.
- Note that previous wage increases in DCs is not entirely due to increases in the minimum wage or labor standards.
- If employers have too much market power (thus making the labor market noncompetitive) it makes sense for workers to be allowed to organize and to form unions to counteract the firms' power.

III. Should Standards Be Linked to Trade?

- NO, say most economists (including most trade economists). Trade lawyers are a prominent "NO" group, as are many LDCs (even some LDC labor unions). LDCs often worry that trade sanctions will be used against them to make them pay higher wages, thus eroding their comparative advantage (abundant and relatively inexpensive labor). MNCs are also part of the "NO" group, even though they usually provide higher wages and better working conditions then many local companies.
- YES, says the Clinton Administration, most Democrats, most unions in DCs are routinely in favor of linkage, and many NGOs (Non-governmental Organizations).