

***By American***

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A 2004 *Frontline* program titled “Is Walmart Good for America?” (WGBH Educational Foundation) presented the view that Walmart, or the trend represented by Walmart, is leading to a decline in the U.S. standard of living. It was suggested that Walmart’s monopsonistic practices are driving its U.S. suppliers out of business and forcing those that remain, or wish to remain, to move their manufacturing operations abroad. In other words, in response to Walmart’s pressure on suppliers to reduce wholesale prices, many U.S. companies have chosen to move their manufacturing operations to low-wage countries, such as China. A consolidation trend in retailing—from smaller stores to larger mass retailers—means U.S. suppliers have fewer, but larger, customers, which in turn means U.S. manufacturing companies that produce consumer products are increasingly vulnerable to monopsonistic pricing practices. As U.S. manufacturing moves abroad, U.S. manufacturing jobs are lost at home and gained abroad. Associated with a loss of U.S. manufacturing jobs, manufacturing wages and income—income that would have been earned by U.S. citizens (and/or U.S. residents) in the U.S.—also are lost. The movement of U.S. manufacturing abroad produces a downward effect on U.S. per-capita income, all else equal, and thus a downward effect on the U.S. standard of living. On the other hand, some claim the lower prices that Walmart and other retailers like Walmart offer to U.S. citizens lead to an increase in the after-retail-purchases incomes of U.S. citizens, and thus raises the U.S. standard of living. U.S. citizens pay lower prices for necessities and consumer products, so more of their after-tax or disposable income is left over for other purchases or for saving.

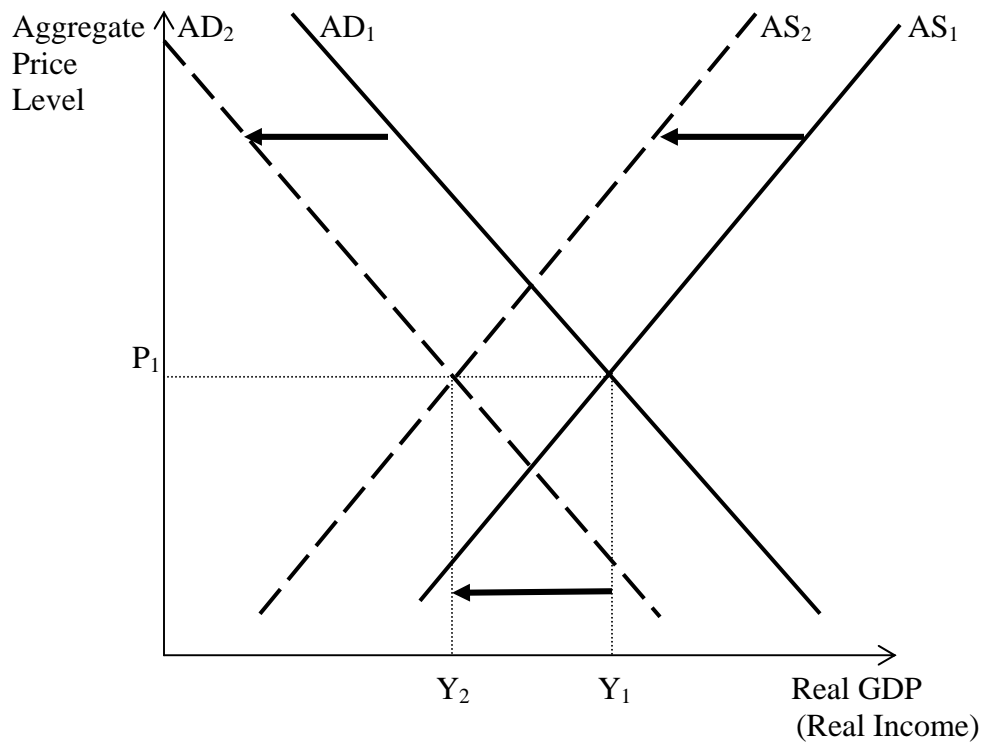
What is the net effect on the U.S. standard of living? Although there appears to be a defeatist view in the U.S., which is perhaps rooted in the belief that a decline in the domestic manufacturing sector is an inevitable and necessary consequence of an evolving domestic economy, this is not necessarily so and, in fact, a thriving domestic manufacturing sector is not inconsistent with the profitable strategy of foreign outsourcing of domestic manufacturing to relatively lower-wage economies. Yes, the domestic manufacturing sector should shrink as the domestic economy evolves (at least with respect to the once-domestically-produced goods that are now produced abroad), but that does not mean some of those same goods cannot still be produced profitably at home. Indeed, domestic consumer demand dictates that some of the same goods whose manufacture is now outsourced to lower-wage foreign companies should continue to be produced domestically. The net effect on domestic per-capita income, therefore, need not be so large if certain conditions are met (i.e., the implementation of a successful *By American Standard*, for example, or simply a non-policy-induced, spontaneous change in domestic manufacturer strategy toward filling existing domestic consumer demand for domestically-produced products). Furthermore, it may not necessarily be negative in the long-run if the continued domestic manufacturing promotes additional domestic manufacturing in the future (through positive learning curve effects, for example) and if domestic companies forge competitive advantages in the manufacturing of new and innovative goods.

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The short-term response to a relocation of U.S. manufacturing abroad is a decline in U.S. real income. The U.S. economy contracts due to (1) the exogenous or autonomous reduction in U.S. aggregate supply equal to the real value of the relocated production abroad and (2) the autonomous reduction in U.S. aggregate demand due to the substitution of imported products for the once-produced U.S. products. In the longer-term, a combination of U.S. price level and exchange rate adjustments might help eliminate the contractionary demand-side effect on U.S. real income. However, downward wage and price rigidity (which keeps the aggregate supply curve from becoming effectively vertical in the long-run) and the need to maintain a positive capital inflow from abroad to finance the trade deficit and U.S. budget deficit (which keeps the price of the U.S. Dollar from falling) both contribute to a persistence in the contractionary aggregate demand effect on the U.S. economy. An increase in U.S. investment spending at home might help alleviate the contraction in aggregate demand, but U.S. interest rates cannot fall enough to stimulate sufficient new U.S. domestic investment spending (since, to finance the trade deficit and U.S. budget deficit, U.S. financial investments must remain attractive to foreign lenders). Limited U.S. investment in the short-term also has a long-term supply-side impact. Without sufficient new investment to stimulate U.S. productive capacity, U.S. aggregate supply remains at its lower level into the longer-term. In sum, apart from national security concerns, the persistent contraction in aggregate demand and aggregate supply lead to a decline in long-term aggregate U.S. real income (and, without a decline in U.S. population, a decline in per-capita real income).

**Figure 1**



In the long-term, there is likely to be a fundamental shift in the U.S.'s relative competitiveness that would reinforce the reduction in U.S. real income, as it is difficult to regain

lost industries (and the know-how that underlay them) when one attempts to re-enter. As U.S. companies relocate their manufacturing operations abroad, foreign entrepreneurs and foreign joint venture companies gain valuable experience and knowledge that allows them to quickly move up the learning curve. In addition to the Chinese policy of requiring foreign companies to form a joint venture with Chinese companies, which has a primary benefit of ensuring foreign companies who set up shop in China will be in a position to transfer key know-how (and competitive strength) to Chinese companies, the relocation of U.S. manufacturing to low-wage countries reinforces the decline in the U.S.'s relative competitive position and standard of living. The *Frontline* program also presented the Rubbermaid example, where Rubbermaid, as a supplier of Walmart, failed to meet Walmart's low-price requirement (during a time when the plastics industry was facing rising raw material costs) and lost a large volume of business from Walmart. Given its dependence on business from large retailers, including Walmart, the lost business from Walmart led to the sale of Rubbermaid to a competitor company, Newell, and ultimately to its bankruptcy. In the Rubbermaid bankruptcy auction, Chinese entrepreneurs purchased a key machine used to make Rubbermaid products for \$850,000. The movement of key U.S. company operating assets to foreign companies, which have embedded in them substantial intangible value in the form of know-how that reverse-engineering can decipher, is a more tangible and direct way in which the relocation of U.S. manufacturing abroad causes a transfer of skills and knowledge to foreign companies and workers, and subsequently to decline in the U.S.'s relative competitive position in global markets. A saving grace might be technological progress that, over time, creates new products and new business opportunities for U.S. manufacturing companies to produce them. Nevertheless, will enough U.S. citizens have the manufacturing experience and critical know-how necessary to produce them later on, and further down the road what will happen to these new manufacturing jobs and incomes when these new industries evolve over time into more competitive industries? Will these once-new U.S. manufacturing jobs be exported abroad as well when competitive pressures increase?

Why not retain U.S.-owned, -located, -worked, and -sourced manufacturing companies—and the associated U.S. manufacturing incomes—in some (or many, or all) industries, old and new, even when competitive pressures develop as manufacturing industries evolve and mature? Perhaps there is a flawed U.S. business mindset that leads us to readily accept the loss of any or all manufacturing jobs as an inevitable consequence, or a necessary part, of economic progress of this country. More importantly, is the existence of Walmart and its standard of living-promoting attributes necessarily incompatible with a thriving U.S. manufacturing sector, a manufacturing sector that simultaneously produces many of the same products that Walmart and other mass retailers obtain from abroad? The answer is no. Consider two distinct groups of U.S. consumers. At a given price for a given high-quality product, (1) some people prefer to buy the product that is made by a U.S.-owned, -located, -worked, and -sourced company, while (2) others prefer to buy the product regardless of where or who produced it. Call these Type 1 and Type 2 consumers, respectively. There are two distinct types of Type-1 consumers: (1a) A portion of Type-1 consumers are willing to pay a reasonable price premium for the high-quality product when it is produced by a U.S.-owned, -located, -worked, and -sourced company, while (1b) the remainder of Type-1 consumers are not willing to pay a price premium, even if reasonable, for a high-quality product that is produced by a U.S.-owned, -located, -worked, and -sourced company. Even though the market for retail consumer products is quite competitive, there are U.S. consumers who separate themselves as being 1a-Type-1 consumers. These 1a-

Type-1 consumers represent a distinct subset of the market, which reflects a valuable market niche that could be filled by retailers that sell high-quality U.S. products that are produced by 100% U.S.-owned, -located, -worked, and -sourced companies, or “By American” companies. These U.S. manufacturing companies, and the retailers that ultimately sell their By American products, could use the “By American” badge as a distinct and valuable selling point to attract 1a-Type-1 U.S. consumers, which in turn would promote U.S. manufacturing of some of the same imported products sold at Walmart and other mass retailers (and perhaps other products as well). The word “By” is used instead of “Buy” to highlight an important shift in focus away from the demand-side to the supply-side. On the demand-side, it is difficult for consumers to know whether a U.S.-branded product really is a U.S. product in a true sense (i.e., is it produced by a U.S.-owned, -located, -worked, and -sourced company?). One should not place blame on U.S. consumers for not buying American products because there is, indeed, a subset of U.S. consumers that would purchase U.S. products, if only one could really know which products are U.S. products. The focus of the *By American Standard* proposed here is the supply-side. The *By American Standard* would provide accurate information to consumers about which products are truly U.S. made. To be a successful business strategy, U.S. consumers must know (not just perceive) a By American product is truly a U.S. product, or else the By American badge would be a hollow mark. The ownership of By American manufacturing companies must not be only in name, but in substance. To restrict indirect and less-visible ownership by foreign individuals, stockholders of By American suppliers should be verified to be legal U.S. citizens, and these citizens should be individuals (not companies or entities or asset portfolios, like pension funds, mutual funds, partnerships, etc.). Additionally, By American workers should be verified to be legal U.S. citizens, and By American companies should be verified as being located within U.S. borders.

A price premium for By American products would be required for By American manufacturers to survive because U.S. citizens are paid higher real wages than workers in lower-wage counties. However, since the retail consumer products industry is competitive, price gouging would not be viable business strategy—no 100%-markup-over-cost-pricing strategy would do here. As long as the price premium is reasonable, By American retailers could survive, and even thrive, along-side the Walmarts, because there is a distinct market niche of 1a-Type-1 U.S. consumers who feel that By American products provide greater intangible value to them than identical imported products. Supporting the self-earned incomes of your domestic neighbors is far more desirable and commendable than bailing them out after their jobs have been exported. The notion that both large and small retailers could sell By American products along side lower-priced foreign substitutes is a win-win opportunity for the U.S. because, not only would it promote U.S. manufacturing and incomes, lower-priced products from abroad would continue to be available for 1b-Type-1 and Type-2 consumers and the retailers that follow the Walmart business strategy would suffer little from competition from By American products. Indeed, they would also stock By American products on their shelves as well. To ensure that domestic manufacturers could remain profitable while simultaneously charging a *reasonable* price premium, only raw materials, strictly defined, might be an acceptable exception to the domestic source requirement, to the extent that certain, quality raw materials cannot be produced competitively in the U.S.

The proposal that only a 100% U.S.-owned, -located, -worked, and -sourced companies can be By American companies would be fair. As a voluntary standard, any company that wishes to be a By American company can choose to adhere to the *By American Standard's* requirements. The goal here is to promote U.S. citizens' standard of livings by increasing U.S. manufacturing and U.S. manufacturing incomes, which can be accomplished in a substantial way only by a strict requirement that all By American products be produced by 100% U.S.-owned, -located, -worked, and -sourced manufacturers. A *By American Standard* would not be a protectionist policy that violates the U.S.'s commitment to the World Trade Organization (WTO). It would not be a regulation imposed on companies, like an import tariff, but rather compliance with the *By American Standard* would be voluntary. It would involve nothing more than the U.S. government's (or an independent organization created by government, like the SEC or FASB) commitment to implementing and enforcing the *Standard*. The core task would be to gather information to verify that each By American manufacturer adheres to the requirements, and to provide information on compliance on a product-by-product basis to consumers (through a website, for example) so that 1a-Type-1 consumers may choose not to buy products fraudulently carrying the By American badge (which would ensure the survival of only true By American companies, thereby promoting U.S. manufacturing jobs). The beneficial impact of a *By American Standard* on U.S. manufacturing jobs and incomes would be the by-product of a sound business strategy on the part of companies choosing to meet its requirements that fills a valuable market niche in the U.S., not based on protectionism. It would be a consumer-driven improvement in U.S. manufacturing, since a viable and successful By American strategy on the part of retailers would depend upon not only the U.S. supplier response to produce high-quality products when demand calls for it, but most importantly it would depend on the U.S. consumers' demand for such U.S. products. A substantial group of U.S. consumers do separate themselves as being 1a-Type-1 consumers, and would readily purchase high-quality By American products when available, which means retailers can profitably offer By American products (even if at first on a limited basis). Over time, as U.S. demand dictates and as U.S. manufacturers respond, more By American products would become available, such that greater shelf space for By American products would become viable for retailers. The biggest hurdle to a successful *By American Standard* would be to insulate the implementation process from political forces that would water down or loophole the policy.