

Decoupled – US Corporations, Workers and the US Economy - What's Good for General Motors or Dell is No Longer Good for America – Ernest Nounou, May 23, 2004

The Problem

“What’s good for the country is good for General Motors and vice versa” is a famous 1952 remark by Charles E. Wilson, at his confirmation hearing before the Senate Armed Services Committee to become Secretary of Defense. That statement assumed an alignment of GM and other US companies’ interests with those of their workers and the US economy. While generally true for much of the period 1950 – 2000, this assumption is no longer true today.

Bastions of traditional values of loyalty, teamwork and lifetime employment, US companies were the primary source of entry-level jobs leading to higher paying work, including health, education and pension benefits. But as they expanded beyond domestic to foreign markets, corporate and country interests began to decouple. In his book “The Seven Sisters” on the multinational oil companies, Anthony Sampson could have been speaking about all multinationals in starkly describing their behavior during the 1973 oil embargo and Arab - Israel war:

“As soon as the embargo began, in October 1973, the seven sisters were compelled, at the risk of forfeiting their concessions, to be the instruments of the world-wide cutback in oil. And the American companies had to enforce an embargo of their own home country. The angry question came up ferociously: where are the oil companies' true loyalties?”

Sampson’s own response, as valid today as when he made it thirty years ago, was:

“...The sisters are basically committees of engineers and accountants preoccupied ... with profit margins, safeguarding investments, and avoiding taxation...to put it another way, it was an abrupt test of the companies' multi-nationality; could they, in this crisis, continue to be all things to all countries?”

As they established foreign subsidiaries to sell and provide services in foreign countries, US corporations gradually took advantage of the lower cost differentials those subsidiaries enjoyed, to service US markets. In so doing, foreign subsidiaries evolved into cheaper alternatives and competitors to their own domestic manufacturing and service bases. Whether underestimated or deliberately minimized by economists and the Administration in proclaiming it as limited to lower paying call centers, offshoring of US jobs has increased apace and includes lawyers, accountants, business and medical analysts.

Leading high tech and pharmaceutical firms have announced the establishment of research centers offshore, and financial institutions are hiring analysts by the hundreds in their offshore offices. This has led to the great outcry against the offshoring of American jobs, concerns regarding the inexorable movement of more, particularly higher value service sector jobs offshore, and cries for protection.

Even with GDP growing in excess of 4%, and two months of payroll gains in excess of 500,000 jobs, reversing the tepid economic growth and jobless recovery of past 30 months, surveys reveal American workers remain unusually anxious over their future prospects. Their responses indicate the recovery hasn’t reached them nor addressed their concerns. Rather, it further reflects and confirms the decoupling of interests of the three stakeholders.

Corporations

US corporations have responded to globalization, competition, and geopolitical challenges with a business model emphasizing information technology and other productivity enhancing investments, together with global sourcing of production. They have enjoyed great success in achieving record productivity and profits, making them spectacular wealth creation machines for their owners and shareholders. Simultaneously, their role as lifetime employers and primary source of entry-level work leading to higher paying jobs and benefits has greatly diminished.

A caveat: In stating and describing the decoupling of US corporations from the US economy and workers is not a judgments on their patriotism. Features of this decoupling include the following:

- As Warren Buffet has pointed out, despite record earnings US corporate tax share of total tax receipts in 2003 were at near record low level of 7.4% as compared to 32% in 1952, when Charles Wilson made his famous remark. The average effective tax rate of US corporations in 2003 was less than 10% according to the BLS.
- Global sourcing of components and services from offshore third parties and subsidiaries originally established to facilitate entry to foreign markets, competes with and is reducing domestic operations.
- Capital investments in production and information technology have enabled corporations to generate more sales and profits with fewer employees and more just-in-time temps receiving no benefits.
- Corporations such as GE and Dell employ more people offshore than in the US.
- Domestic sales of companies such as Dell contain little if any US components. Dell alone contributed an estimated \$17 billion to the US trade deficit in 2003. (See <http://www.thethinktank.biz/articles/dell.shtml>)
- Pension plans have shifted from defined benefit to defined contribution plans, often at the expense of older long-standing employees at companies such as IBM.
- Companies have shifted a greater share of rising healthcare costs to their employees and in a number of cases such as Weirton Steel have eliminated benefits earned by retirees.
- CEO and senior management teams are enjoying record compensation, even as employee compensation has stagnated during the past two decades, growing barely 1.5% after inflation.
- Defying periodic predictions of macroeconomic orthodoxy during the 2001 – 2003 Jobless Recovery - that high paying payroll jobs were imminently returning - corporations have generated record sales and profits in a growing economy, while continuing to lay off 2.9 million employees.

US Economy

Global sourcing of components, services and productivity increases have led to world class US corporations, many the leaders in their industries. On the flip side global sourcing has contributed to significant losses of higher paying domestic payroll jobs and purchasing power. Moreover imports by US corporations of products and services from their foreign subsidiaries represent a growing and significant structural component to the annual balance of trade deficit, now \$600 billion.

The classic cure for reducing trade deficits would be to devalue the dollar. But this will lead to perverse results for the US economy, given the absence of domestic alternatives that have been offshored. (See <http://www.thethinktank.biz/articles/dell.shtml>):

- Prices of imported components and hence the trade deficit will actually increase.

- Inflationary forces will be introduced into the economy, diminishing a principal value proposition for offshoring factories and jobs in the first place.
- Offshoring of production facilities and jobs are likely to speed up, as corporations seek to benefit from appreciating currency effects on foreign assets and earnings.

Further examples of decoupled fortunes in a 4% growth GDP economy, record corporate profits, stock market gains, and CEO compensation, are communities throughout the country left with closed factories, large segments of unemployed workers, with unclear prospects. Other phenomena include:

- Record bankruptcy filings by two-income earning middle-class families, when one loses his or her job.
- Replacement jobs taken are frequently lower paying temp jobs without benefits.
- 40 million working Americans do not have health insurance, relying on more expensive emergency room alternatives.
- Unemployment rate closer to 8% than the official 5.7%, when factoring in underemployed and temp workers seeking fulltime positions, and discouraged workers who have stopped actively seeking work.

Nor is it intuitive that the US economy can continue to offshore jobs and production facilities and still retain its pre-eminent leadership. National security will clearly be impacted as the economy develops greater reliance on offshore components and services, ironically even as the US tries to reduce its dependence on foreign energy sources.

US Workers

As third stakeholder in the decoupling process, US workers have borne the brunt of the downside, even as corporations and the US economy have enjoyed the productivity and profit increases. Those working at major corporations are exhibiting unusually high anxiety, even as their employers have enjoyed record profits and GDP growth in excess of 4%. This seeming paradox is wholly understandable. From the vantage of close proximity, corporate employees understand clearly the following:

- 70% of Americas' 130 million jobs are in the service sector, and few are immune to the twin forces of outsourcing and offshoring.
- Absent unlimited sales growth, corporations have maintained profit growth through a combination of rigorous cost control, productivity enhancing capital investments, and mergers. All have the net effect of reducing or eliminating jobs, as the 2.9 million jobs lost in the past 30 months attests.
- Few jobs are immune from reengineering, as the corporate model converts higher paying decision making jobs to lower cost data entry tasks. A classic example is the virtual elimination of bank lending officers with decision-making and lending approval authority. In their place are less costly and more junior customer facing personnel who facilitate customer form filling; which forms are computer "rated" and approved by formula.
- Business Process Outsourcing ("BPO"): Corporations are increasingly advised to outsource non-core business processes to third parties such as IBM, EDS, or to their own foreign subsidiaries. While the former outsourced employees may become employees of IBM or EDS, the strong likelihood is this is temporary, and their jobs are eliminated via staff reduction or offshoring to IBM and EDS subsidiaries offshore.
- Corporate workers bear an increased portion of healthcare and pension benefits costs, even as their wages have stagnated for two decades.

Many in the economic establishment refer to the "Payroll Survey" as the better gauge of job growth, as it measures self-employed and small business employees not picked up by the Department of Labor's Payroll Survey. As corporate layoffs continue and payroll jobs are shed,

more workers will continue to show up in the Household Survey. Their profiles offer a precarious picture:

- Workers are increasingly self-employed or working for small businesses as temps at lower wages and no benefits in a parallel service economy.
- They are responsible for their own medical insurance, assuming it is available and affordable.
- Despite officially low and cruelly irrelevant CPI statistics, these workers are exposed to rising costs of living (food, shelter, transportation, and education),
- And for good measure they have to constantly find new job opportunities.

US worker anxiety amid record profits and GDP growth is no mystery at all, and is the logical outcome of their decoupling with the corporate sector and US economy. Perception by workers that their plight is being minimized or not understood heightens their anxieties and concerns. This situation is untenable for sustaining a traditional middle-class America.

Solutions

In considering solutions, policy makers must recognize the decoupling of the previously aligned interests of corporations, workers, and the economy. While avoiding harm to corporate interests, solutions must focus efforts benefiting workers and the economy. For example, corporate tax cuts to stimulate domestic hiring will achieve minimal results. Specific solutions impacting the entire economy, especially those workers in the parallel non-corporate sector, include:

1. Universal Healthcare as infrastructure and good business, benefiting the economy and nation. There is no surer more cost-effective way to increase domestic job creation while reducing anxiety and pessimism regarding future prospects.
2. "Domestic Content" provisions, successful in the auto industry, requiring foreign as well as domestic corporations such as Dell to have minimum percentages of US components and services in products sold in the US.
3. Nation Building

Guiding Principals

- Do no harm - Avoid protectionism, as it will make matters worse
- Avoid spin
- Forget about just leveling the playing field! Let's make the infrastructure changes needed to ensure that America has the best damn playing field anywhere, thus enabling us to continue to have the best labor force, and to once again draw the outside world's best experts and companies to feel they have to come here.

Specific Solutions (Note this list will grow):

Leadership at all levels of government and private sector must convey by message and deed we're all in this together to prevail. Leadership must challenge the country to compete to win, and forthrightly lay out what it will take. It is again time to say, credibly, "ask not what your country can do for you, but you can do for your country." Calls for volunteerism and sacrifice, if credibly and forthrightly made, will rally and bring out the best in the nation.

Infrastructure, of all kinds must be provided to American workers, who are increasingly self-employed or in smaller service companies. If properly enabled, their talent and ingenuity will respond, compete, and prevail. It always has and will, if given the chance.

1. Universal healthcare as infrastructure, not as an entitlement

Polls indicate that the majority of current and retired American workers are anxious and insecure about losing their jobs and benefits, even as Chairman Greenspan has called for a reduction in Social Security benefits, while increasing the eligibility age. The biggest subset of this is the loss of health insurance. Already the most Balkanized health delivery system in the world, more patches and limited solutions are being proposed to address the continued loss of insurance by laid off workers.

We believe health care issues are the single biggest source of Americans' anxiety about their future. It is a major impediment to future job growth; and must be solved not with yet another six-month study, but implemented forthwith. As to affordability, studies by Ewe Reinhardt and others indicate the cost of Single Payer Universal Coverage is affordable. It would reduce administrative costs and spread the actuarial cost of healthcare over the entire population, as younger healthy workers are included.

Corporations and individuals would continue to pay through taxes the equivalent of what they pay now, but no one would be denied access, be tricked by vendors preying on the unsuspecting, or be denied critical medical care when needed. Providing this to American workers is simply good business, similar to providing the best physical infrastructure - roads, bridges, tunnels, or communications bandwidth. Given these, American workers will be freed to compete against others with confidence and advantage. Benefits include:

- a) Job Creation, as self-employed individuals and small business are encouraged to take risk.
- b) Mobility and Volunteerism as workers move to locations having job demand, and perform work they seek, rather than cling to current jobs to preserve health insurance coverage.
- c) Job openings would increase as workers pursue goals unrelated to their current work, be it entrepreneurial, lower paying but psychically satisfying, or simply volunteering in faith and community based endeavors.
- d) The overall economy would greatly reduce wasted energy and administrative costs of the present system.
- e) Other financial benefits of Universal Healthcare include:
 - 1) Broadening of the tax base, as more workers find work.
 - 2) Savings from forgoing additional outlays for job loss insurance and expanded unemployment benefits.

By taking healthcare off the table as an issue, we eliminate the greatest cause of anxiety accompanying job loss, sow seeds of optimism, and unleash the forces of creative energy and risk taking that are what the American economy is all about. This is as essential a priority for our future as the war on terrorism, and can't be discussed in dollars and cents alone. If put to a national referendum, we bet universal health coverage, in the form of a single payer, would win hands down.

2. Domestic Content

Arguably the US economy's leading comparative advantage is the size and scope of its domestic market. Access to this market is the goal of every major foreign company, and accordingly they and domestic companies must pay the appropriate price for this access. That price must be in sourcing US goods and services in their final products, thus rationally stimulating the creation of US based jobs. A version of the auto industry model is an effective place to start.

3. Physical and Electronic Infrastructure

We can afford no less than the very best Broadband, highways, bridges, tunnels and anti-terrorism measures. Expenditures would result in immediate job creation and increased

competitiveness for the American worker. Surveys show superior broadband at multiples of the speed offered and at a fraction of the US equivalent in Korea, Japan and other competing countries. American households must not remain comparatively disadvantaged in this critical area.

4. Nation Building

- a) Mandatory two years service of national service after high school would be required in either military or domestic programs, and with no deferments.
- b) Encourage and enable volunteerism by older generations. Those aged in their late 30s through 50s tend to be the most experienced and expensive workers, hence vulnerable to cost-cutting considerations. It makes good sense for the economy not to lose such experienced talent, encouraging and enabling it to continue to contribute to society and the economy.
- c) Compensation would be in several forms:
 - 1) Minimal in cash
 - 2) Training, whether in the military or domestic programs.
 - 3) Points or credits towards college tuition and retraining at all US colleges (private and public), and vocational schools without exception, further enabling life long retraining.

5. Tax code review

- a) Address extravagant or foolish laws that encourage offshoring and avoid repatriation of earnings.
- b) Avoid reducing US corporate competitiveness
- c) Tax simplification, including consideration of a Flat Tax approach having three rates, and limiting deductions to:
 - 1) Mortgage interest up to \$1 million
 - 2) State and local taxes
 - 3) Charitable contributions

6. Overhaul Bureau of Labor Statistics to require accurate data to facilitate sensible decision making

- a) Data on the number of jobs offshored are not currently compiled. The SEC should require public companies to disclose the geographic distribution of employees, their increased and decreased numbers by location.
- b) Nature and income of new jobs created, and level of benefits. The BLS should not rely on simple averages when weighted averages are more appropriate.
- c) Establish sensible data on inflation. To claim the economy has a core inflation rate of 1% is meaningless for an economy with exploding prices for healthcare, education, housing, food and fuel.

7. Police Borders

- a) Curb illegal immigration and border crossings, as to ignore the issue invites disrespect of the law.
- b) Anti-terrorism would be strengthened with more secure borders and ports of entry.

8. Lifelong Access to Training and Education

Payment for training could be supplemented through points earned from participation in nation building activities.

9. Enforce Trade Agreements to Open Markets for US Exports

10. Government Contract Bidding – US Job Considerations

Invite global bidders, weight should be given to where work will be performed and number of new jobs created.

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