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I Z A
World of Labor
Evidence-based policy making

International trade and economic insecurity

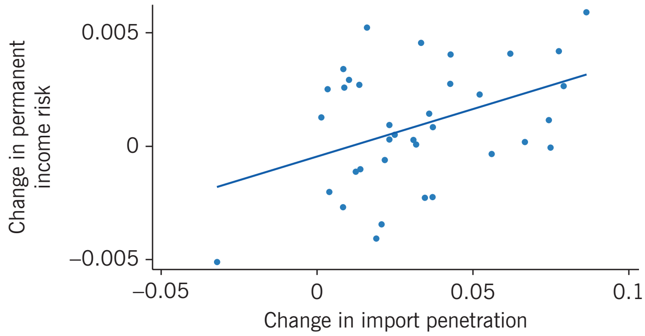
Trade can increase economic insecurity for some workers while increasing stability for others

Keywords: trade, volatility, income risk, displacement risk, firm survival, offshoring

ELEVATOR PITCH

Whether or not international trade exposes workers to economic insecurity depends on the nature of the trade exposure of the firm, or industry, in which the worker is employed. Import-competing industries experience higher levels of risk to workers' incomes and employment, while firms that import intermediate production stages ("offshoring") display bigger employment responses to small changes in workers' wages, and are more likely to shut down home factories. But offshoring also helps firms weather economic shocks. Offshoring firms are more likely to survive and provide greater employment stability to their workers.

Positive association between import penetration and permanent income risk in the US



Source: [1].

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KEY FINDINGS

Pros

- Employment is more stable in firms that export goods to other countries.
- Shifting some production from home factories to factories located in other countries (offshoring) may protect firms against temporary economic shocks and ensure greater employment stability for their workers.
- Firms that engage in international trade, either by importing or exporting, have a higher probability of long-term survival.

Cons

- Offshoring makes firms more responsive to changes in cross-country economic conditions, which could lead to larger swings in employment and wages at home.
- The higher the level of net imports at the sector level, the higher the rate of job turnover among workers in that sector.
- Offshoring intermediate production stages makes employment more responsive to wage changes and can lead to shutdowns of home factories.
- Income risk (measured as the variance of unpredictable changes in income) is higher for workers employed in import-competing sectors.

AUTHOR'S MAIN MESSAGE

Although free trade results in gains in aggregate (economy-wide) welfare, the process of job creation and job destruction that it involves is not orderly or costless. The distribution of these gains is uneven across segments of the population and associated with a high level of uncertainty. This can result in higher levels of economic insecurity, with even similar types of workers experiencing very different economic outcomes. Extending the size of the social safety net necessary to insure workers against this risk, and introducing policies that ease the adjustment costs, would help address this problem and mitigate the risk.

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