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Defining Away Economic Failure: "Offshoring Manufacturing" and the Decline of America's Industrial Base

Redefinition Is America's Most Powerful Factor of Production

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Theme: [Global Economy]

Last week's government guesstimate that second quarter 2014 real GDP growth will be 4% seems nonsensical on its face. There is no evidence of increases in real median family incomes or real consumer credit that would lift the economy from a first quarter decline to 4% growth in the second quarter.

Middle class store closings (Sears, Macy's, J.C. Penney) have spread into the Dollar stores used by those with lower incomes. Family Dollar, a chain in the process of closing hundreds of stores is being bought by Dollar Tree, the only one of the three Dollar store chains that is not in trouble. Wal-Mart's sales have declined for the past 5 quarters. Declining sales and retail store closings indicate shrinking consumer purchasing power. Retail facts do not support the claim of a 4% GDP growth rate for the second quarter, and they do not support last Friday's payroll job claim of 26,700 new retail jobs in July.

What about the housing market?

Don't the headlines accompanying last Friday's payroll jobs report, such as "Hiring Settles Into Steady Gains," mean more people working and a boost to the economy from a housing recovery? No. What the financial press did not report is that the US is in a structural jobs depression. In the 12-month period from July 2013 through July 2014, 2.3 million Americans of working age were added to the population. Of these 2.3 million only 330 thousand entered the labor force. My interpretation of this is that the job market is so poor that only 14% of the increase in the working age population entered the labor force.

The decline in the labor force participation rate is bad news for the housing market. The US labor force participation rate peaked at 67.3% in 2000 and has been in a sustained downturn ever since. The rate of decline increased in October 2008 with the bank bailout and Quantitative Easing. From October 2008 to the present, 13.2 million Americans were added to the working age population, but only 818 thousand, or 6%, entered the labor force. http://investmentresearchdynamics.com/americas-structural-job-depression-is-here-to-stay/ Despite government and financial press claims, the Federal Reserve's multi-year policy of printing money with which to purchase bonds did not restore the housing or job markets.

What about the stock market?

It has been down in recent days but is still high historically. Isn't the stock market evidence of a good economy? Not if stocks are up because corporations are buying back their own stock. Corporations are now the largest buyers of stocks. Recently we learned that from 2006 through 2013 corporations authorized $4.14 trillion in buybacks of their publicly traded stocks. Moreover, it appears that corporations have been borrowing the money from banks with which to buy back their stocks. Last year there were $754.8 billion in authorized stock buybacks and $782.5 billion in corporate borrowing. In the first three months of this year, companies purchased $160 billion of their own stocks. http://wallstreetonparade.com/2014/07/another-wall-street-inside-job-stock-buybacks-carried-out-in-dark-pools/

Borrowing to buyback stock leaves a company with debt but without new investment with which to produce revenues to service the debt. The massive stock buybacks demonstrate that American capitalism is now corrupt. In order to maximize personal short-term financial benefits flowing from bonuses, stock options, and capital gains, CEOs, boards of directors, and shareholders are decapitalizing public companies and loading them up with debt.

Well, isn't the economy being helped by the return of manufacturing to America? Apparently not. Data for 1999-2012 indicate that the offshoring of manufacturing increased by 9%.

One economist, Susan Hester, an economist for the Retail Industry Leaders Association, has decided to turn the loss of manufacturing jobs into a virtue. Her argument is that retail employment dwarfs manufacturing employment and that more American jobs can be created by selling more imports than by encouraging manufacturing in order to provide exports.

According to Ms. Hester's research, the US makes more money from the retail side than from the production side. She concludes that the value added to a product by offshore labor is a small percentage of the value added by "managing offshored production, handling Customs clearances, managing warehouses and distribution, marketing apparel products, and by millions of people in the retail sector stocking shelves and working cash registers."

In other words, the US manufacturing jobs moved offshore are just a throwaway. The money is made in selling the imports.

Ms. Hester neglects to recognize that when offshored production is brought to the US to be marketed, it comes in as imports and results in a larger US trade deficit.

Foreigners use dollars paid to them for the products that they make for US firms to purchase ownership of US bonds, stocks, and real assets such as land, buildings, and companies. Consequently, interest, profits, capital gains, and rents associated with the foreign purchases of US assets now flow to foreigners and not to Americans. The current account worsens.

It works like this: The excess of US imports over US exports leaves foreigners with claims on US income and wealth that are settled by foreign purchases of US assets. The income produced by these assets now flows abroad with the consequence that income earned by foreigners on their US investments exceeds the income earned by the US on its foreign investments.

According to Ms. Hester's reasoning, Americans would be better off it they produced nothing that they need and in place of manufacturing relied on the incomes of US fashion designers and pattern makers who specify the offshored production for US markets, on the compliance officers and freight agents, on production planning and expediting clerks, and on longshore workers and railroad employees who deliver the foreign-made goods to US consumer markets.

Ms. Hester believes that the value-added by offshored manufacturing is inconsequential. How then did China get rich from it, becoming the second largest economy and employing 100 million people in manufacturing (compared to America's 12 million), and acquire the largest foreign reserves of any country?

After Ms. Hester answers that question she can explain why US corporations go to the trouble to offshore their manufacturing if the contribution to value-added is so low? The value added is obviously substantial enough for the labor cost savings to pay for transportation costs to the US from Asia, for the cost of set-up and management of foreign based facilities, and for the cost of the adverse publicity from abandoning US communities for Asia and still leave value-added after all costs to enlarge profits and drive up stock prices and executive bonuses.

Ms. Hester fools herself. The low value that she calculates Chinese, Indian, or Vietnamese labor adds to the price of a shirt reflects the low foreign labor cost, not a low value of the shirt in US markets or a low value of an iPhone in European markets. Marketing, warehousing and distribution are done in the US by more highly paid people, and this is why it looks like the value added comes from sources other than manufacturing. Ms. Hester overlooks that the lower cost of foreign labor does not translate into a less valued product but into higher profits.

Economists assume that the labor cost savings are passed on to the consumers in lower prices, but I have not experienced declining prices of Nike and Merrell sports shoes, of sheets and towels, of Brooks Brothers and Ralph Lauren shirts, of Apple computers, or whatever as a result of moving US production offshore. The labor cost savings go into profits, managerial bonuses, and capital gains for shareholders and is one reason for the extraordinary increase in income and wealth inequality in the US.

Focused on short-term profit, manufacturers and retailers are destroying the US consumer market. The average annual salary of a US apparel manufacturing worker is

$35,000. The average salary of US retail employees is less than half of that amount and provides no discretionary income with which to boost consumer spending in retail stores.

The American corporate practice of offshoring manufacturing has made it impossible for the Obama regime to keep its promises of creating manufacturing jobs and exports. Unable to create real jobs and real exports, the US government has proposed to create virtual jobs and virtual exports made by "factoryless goods producers." In order to keep his promise of doubling the growth of US exports, the Obama regime wants to redefine foreign output as US output.

A "factoryless goods producer" is a newly invented statistical category. It is a company like Nike or Apple that outsources the production of its products to foreign companies. The Obama regime is proposing to redefine companies such as Apple that own a brand name or a product design as manufacturing companies even though the companies do not manufacture.

In other words, whether or not a US company is a manufacturer does not depend on its activity, but on its ownership of a brand name made for the company by a foreign manufacturer. For example, Apple iPhones made in China and sold in Europe would be reported as US exports of manufactured goods, and iPhones sold in the US would no longer be classified as imports but as US manufacturing output. Apple's non-manufacturing employees would be transformed into manufacturing employment.

Clearly, the purpose of this statistical deception is to inflate the number of US manufacturing jobs, US manufacturing output, and US exports and to convert imports into domestic production. It is a scheme that eliminates the large US trade deficit by redefinition.

The reclassification would leave the government's Office of Statistical Lies with the anomaly that products made in China, India, Indonesia or wherever become US GDP as long as the brand name is owned by a US corporation, but the payments to the Asian workers who produced the products remain as claims on US wealth and can be converted into ownership of US bonds, companies, and real estate.

For example, Chinese workers produced the Apple products, and China has the claims on US wealth to prove it. How are these claims accounted for statistically by the Obama regime's redefinition? The US can add China's production of the Apple products to US GDP, but how does the US deduct the Chinese-produced Apple products from China's GDP? And how does the Obama regime's redefinition get rid of the payments by Apple to the Chinese labor that produced the products? These payments comprise claims on US wealth.

In other words, the reclassification would double count the output of Apple's products. If every country does this, world GDP will rise statistically regardless of the fact that no more goods and services are produced. Perhaps this is the way to define away world poverty.

"Factoryless goods producers" was foreshadowed by Harvard professor Michael Porter's 2006 competitiveness report, a justification for jobs offshoring. Defending jobs offshoring, Porter downplayed the rise in the US trade deficit and decline in the US GDP growth rate caused by jobs offshoring. Porter argued, in effect, that ownership of the revenues and products, not the location in which the revenues and products are produced, should determine their classification. As I pointed out in my critique (see *The Failure of Laissez Faire Capitalism and Economic Dissolution of the West),* the result would be to raise US GDP by the amount of US production outsourced abroad and by the output of US overseas subsidiaries and to decrease the GDP of the countries in which the manufacturing actually takes place. Consistency would require that the German and Japanese autos, for example, that are produced in the US with US labor would become deductions from US GDP and be reported as German and Japanese GDP.

As I have emphasized for years, the West already lives in the dystopia forecast by George Orwell. Jobs are created by hypothetical add-ons to the reported payroll figures and by inappropriate use of seasonal adjustments. Inflation is erased by substituting lower priced items in the inflation index for those that rise in price and by redefining rising prices as quality improvements. Real GDP growth is magicked into existence by deflating nominal GDP with the understated measure of inflation. Now corporations without factories are going to produce US manufacturing output, US exports, and US manufacturing jobs!

Every sphere of Western existence is defined by propaganda. Consequently, we have reached a perfect state of nihilism. We can believe nothing that we are told by government, corporations, and the presstitute media.

We live in a lie, and the lie is ever expanding.

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