

Adjustment and Income Distribution in the Trans-Pacific Partnership

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March 28, 2016

Adjustment costs & Income inequality: Major concerns with TPP

- Jobs and income inequality are major concerns and the TPP will require shifting workers among US industries and it could also impact income distribution.
- The analysis of Petri and Plummer sheds light on what adjustments will occur and the long run impacts on wages and profits but does not directly provide estimates of the costs born by displaced workers or income distribution across households.
- We find, however that even under the most pessimistic assumptions, the benefits of TPP outweigh the costs during the adjustment period, and once adjustment is made the TPP provides growing annual benefits. In addition its impact on income distribution across households is very small and slightly progressive.

Three displacement scenarios

Based on Petri and Plummer we develop three scenarios to estimate displacement

- Scenario 1: If all TPP imports displaced all US workers directly and indirectly involved in production, displacement could amount to nearly 1.7 million workers, 170,00 per year over 10 year adjustment period.
- Scenario 2: Many industries are expected to grow substantially over the next decade, with or without TPP. In these industries, import competition should suppress growth, rather than displace workers. Roughly 280 thousand workers would be displaced under this assumption, 28,000 per year.
- Scenario 3: Going further, some adjustment could be accommodated by voluntary quits rather. Taking this into account, TPP might displace 240 thousand workers. (We use the share of voluntary quits in manufacturing), 24,000 per year.

Displacement is Costly For Workers.

- In January 2014, 61 percent of long term workers displaced in prior three years were re-employed – 48 percent at less than previous earnings. (Displaced Worker survey BLS 2014)
- “In present-value terms, men lose an average of 1.4 years of pre-displacement earnings if long-term male workers are displaced in mass-layoff events that occur when the national unemployment rate is below 6 percent” (Davis and Von Wachter, BPEA 2011) This takes account of costs of unemployment and of lower future earnings trajectories.
- We therefore use 1.4 times annual earnings as cost of each worker’s displacement
- Note: Displaced worker surveys indicate that most prime age workers remain in the labor force: After three years, just 11.6 percent of all long-term workers and 8.7 percent of men between 25 and 54 had left the labor force. For all displaced workers 15.7 percent out of labor force (9.0 percent of males between 25 and 54).

Under the most realistic assumptions, TPP’s benefits will outweigh its costs by over 17:1 during the period of adjustment. After the adjustment period, the benefit-cost ratio rises to over 356:1

Adjustment costs and benefits of the TPP

	2017	2021	2026	2030	Average		
					2017-2030	2017-2026	2027-2030
Annual benefits in terms of real income (US\$ billions)	8	42	122	131			
Benefit-cost ratio, scenario 1	0.7	3.0	3.6	37.4	12.3	2.9	36.0
Benefit-cost ratio, scenario 2	3.9	17.1	14.2	355.0	98.1	15.2	305.5
Benefit-cost ratio, scenario 3	4.6	19.9	16.6	414.3	114.5	17.7	356.5

Income Inequality?

- Higher returns to all factors of production but labor will enjoy % greater benefits than capital from TPP and given share in net factor income, almost three quarters of all benefits.
- Taking the additional step of attributing changes in labor and capital income into households incomes, TPP will have a (very) modest positive impact on the US distribution of income by quintiles.
- Moreover, poorer households will enjoy (slightly) greater benefits from the fall in import prices that will result from TPP than rich households.

Implications:

- Some American workers may lose but TPP's benefits far outweigh its costs for US workers and for Americans as a whole.
- The US should work to implement a wage loss insurance program to compensate workers that suffer earnings losses due to displacement.
- Going forward, this approach should be cover all displaced workers, not just those displaced by trade.