

Comment on *Trading Down: Unemployment, Inequality and Other Risks of the Trans-Pacific Partnership Agreement*

Tufts University

Capaldo, Izurieta and Sundaram

January 2016

- Capaldo, Izurieta and Sundaram, use the United Nations Global Policy Model (GPM) to estimate the impact of TPP. GPM was developed to consider the macroeconomic consequences of unexpected shocks such as the global financial crisis, and how such shocks spread between countries. The model doesn't capture exports, imports, foreign direct investment or shifts in industry structure. The model therefore ignores benefits of freer trade such as increased specialisation, greater consumer choice, or economies of scale. (UN agencies do not use this model when analysing changes in trade policy.)
- There are alternative economic models designed to assess trade. To assess the economic impact of a trade agreement like TPP, almost all of these trade models "shock" the model by changing trade barriers, and hence relative prices of imported and domestic goods, and then allowing the economy to adjust with movement of labour, land and capital.
- In order to model the effects of TPP, Capaldo et al instead shock their GPM model by introducing a change in exports (with the export values taken from Petri et al estimates of the TPP – modelling criticized by Capaldo et al). They assume that labour and capital does not respond to the change in exports. This has the result, for example, that if a sector declines in a country, people previously employed in that sector stay unemployed rather than taking employment in growing sectors. Similarly, a sector experiencing increase is unable to draw in new labour and capital, which limits the extent to which it can grow. Under the model, new competition from trade liberalisation is assumed to lower wages and cause unemployment.
- There is a considerable amount of empirical evidence showing the exact opposite. For example, in New Zealand as the wool sector declined people took new jobs producing dairy products, kiwifruit and wine. Generally exports tend to increase when barriers to trade are lowered, and evidence shows that wages are higher in export-intensive industries. It should also be noted that given New Zealand's already open economy, the effects of trade agreements in different sectors are often best viewed in relative terms. Faster growing sectors tend to attract more labour and capital over time, which can be accompanied by decline in some other sectors.
- Robert Lawrence from The Peterson Institute for International Economics compared Capaldo et al analysis of the TPP with Petri and Plummer analysis. He suggested considering each model's credibility by asking three questions:
 - Is the model appropriate for exploring trade policy.
 - Has the TPP been depicted in that model in a sensible way.

- Are the results of the model credible.
- As noted by Lawrence:

“[Capaldo modelling] predicts a decline in employment in every country in the TPP, which totals 770,000 [people]. The authors claim their model is “more realistic,” yet their model also predicts declines of 5.4 million jobs in the rest of the world! Indeed, GDP in non-TPP developing countries (i.e., China, India, Indonesia etc.) falls by 5.24 percent. It is not believable that a trade agreement of this magnitude could cause the rest of the world to plummet into recession. Whatever the merits of the model used by [Capaldo], it is simply not suited for credibly predicting the effects of the TPP.”
- In response to Lawrence, Capaldo has stated:

“in line with the limited scope and purpose of our paper, we do not claim to have provided reliable and definitive projections of the TPP’s likely effects”
- Capaldo used the same model and approach to estimate changes to GDP, employment and inequality from the Transatlantic Trade and Investment Partnership, with similar results. Economists from the European Center for International Political Economy (ECIPC) studied Capaldo’s methodology, the model used and data, and concluded that:

“The Capaldo study is associated with such serious flaws that its results should neither be regarded reliable nor realistic. It fundamentally contradicts all other existing studies of the effects of FTA’s and the reality of what liberalised trade actually brings about.”
- The ECIPC economists point out that:
 - The model is ill-suited to analysing trade reforms.
 - Model deficiencies are covered up with unrealistic assumptions.
 - Capaldo’s thesis is not supported by history.
 - Capaldo’s results conflict with the United Nations global rebalancing assessments based on the same model.

RELEASED UNDER THE OFFICIAL INFORMATION ACT

OUT OF SCOPE

OUT OF SCOPE

OUT OF SCOPE

OUT OF SCOPE

Effect of TPP on employment and income in New Zealand

Coates et al suggest TPP would reduce employment and increase income inequality in New Zealand.

- Coates et al are referring to the Capaldo modelling described above (estimates an employment decline of either 5,000 or 6,000 for New Zealand - 5,000 is reported in the text and 6,000 in a table).
- There are costs as people move between different types of employment, particularly if these changes occur in the short term. But it is not correct to suggest that transition between sectors does not occur, as Capaldo et al claim. For example, as demand for shearers in New Zealand has declined, employment opportunities have grown in dairy farming, wine cultivation, horticulture, tourism, education etc. It is also important to note that given New Zealand's already open economy, few sectors are expected to experience sudden decline. Rather, changes are much more likely to result from increased productivity in certain sectors compared to others.

¹ Published on 5 November 2015, see www.tpp.mfat.govt.nz.

- Capaldo et al report that employment in TPP and non-TPP countries would decline due to the Agreement. Alternatively, Petri and Plummer estimate that TPP will increase United States wages but is not projected to change United States employment levels; it will slightly increase "job churn" (movements of jobs between firms).

OUT OF SCOPE

OUT OF SCOPE

OUT OF SCOPE

OUT OF SCOPE

OUT OF SCOPE

OUT OF SCOPE

OUT OF SCOPE

OUT OF

SCOPE

OUT OF SCOPE

OUT OF SCOPE

RELEASED UNDER THE ACT
OFFICIAL INFORMATION ACT

Pages 5-10 - OUT OF SCOPE

RELEASED UNDER THE
OFFICIAL INFORMATION ACT