DR. BLUESTONE: My name is Barry Bluestone, and I am the Russell B. and Andrea B. Sterns Trustee Professor of Political Economy and Director of the Center for Urban and Regional Policy at Northeastern University in Boston, Massachusetts.

I appreciate the opportunity to testify before this distinguished Commission on the question of trade globalization and the trade deficit.

I have prepared formal remarks for you, and therefore, will just take a few moments to highlight some of the points included there.

As Chairman Volcker did this morning, I would like to place this issue of trade, service, E-commerce, and globalization in a broader context by addressing briefly two critical issues. The first is the effect of trade on wage and income inequality. The second is the role that trade and, more generally, fiscal policy and public investment -- particularly leading to the growth in information technologies -- have played in the current era of rapid economic growth.

In addressing these issues, I will try to make two points. One is that a combination of increasing globalization, expanded trade, and the ballooning trade deficit has been the major factor contributing to increased wage and income inequality in America. Whatever effect it may have on job growth or

a decline in the number of jobs, it is increasingly clear that it has had an impact on the distribution of income through earnings.

The second point is that despite the conventional wisdom, trade actually plays a relatively minor role in the dazzling economic growth we are now enjoying. Instead, public investment, public investment in basic research, education, and training and infrastructure has been responsible for the growth in E-commerce and the economic renaissance the U.S. has been enjoying. Instead, public investment in basic research, education, training, and infrastructure has been responsible for the growth in E-commerce and the economic renaissance the U.S. has been enjoying. I will try to clarify this rather startling and counter-intuitive point in the next few moments.

This leads me to the rather unconventional conclusion that while a completely laissez faire trade policy inevitably contributes to increased inequality, modestly regulating free trade through international labor rights and international labor and environmental standards, plus some regulation of international capital flows would not necessarily hamper economic growth, but it would improve the chances that growth will be shared more equitably.

Moreover, a renewed federal commitment to public investment in basic research, education and training, and infrastructure could contribute to reducing the trade deficit as the result of maintaining America's worldwide lead in information technology and E-commerce.

Permit me to address these issues in a little more detail. There's no doubt that the earnings and income distribution have become vastly more unequal in this country. Just yesterday I was in Berlin testifying before a commission not unlike this, and I had remarked to me the dramatic differences in the income gap in Europe versus the U.S.

We've seen a continued growth in income inequality since the early 1970s, and even in this period of rapid growth there has been very little reduction in inequality.

Why has this inequality grown? There are many theories. One is that it's due to technological change.

Another, de-industrialization.

A third, de-unionization.

Fourth, expanded global trade.

Fifth, acceleration in transnational capital mobility.

Sixth, increased migration, and

Seventh, and most important to this Commission, the chronic U.S. trade deficit.

Well, there's been a lot of research into this question of what contributes to inequality, and what we now know is that it is difficult to pin this on technological change itself or what economists call skill biased technological change.

For one, the greatest growth in earnings inequality has not come in science based professions and technical specialties, but in occupations that include medical doctors, lawyers, sales representatives, brokers, and business managers, not the kind of science-based or technology-based occupations you might think.

On this subject I note in my testimony Alan Greenspan is in agreement. He notes that there has been so much growth in inequality even within occupational groups that it is hard to consider skill-biased technological change as the most important factor.

In looking at the evidence, I come to the conclusion that de-industrialization, the decline in the union movement, and the movement from manufacturing to a service-based economy has led to a growth in inequality. For all kinds of reasons the manufacturing sector has historically been a sector in which earnings

are more equally distributed, while the service economy has been the sector where inequality is growing the quickest. Thus, as we've seen a decline in employment in manufacturing and most of the growth in employment in the service sector, this has naturally led by simple mathematics to growing inequality.

But to a great extent the decline in manufacturing employment and the decline in unionization are tied very closely to the growth in trade, to the trade deficit, to globalization of capital, and increased capital mobility. If you were to look at all of these factors together, I come to the conclusion that between three quarters and 93 percent of the growing gap between college and high school educated men is due to increased trade or its effect on the manufacturing sector and unions.

Let me turn quickly to my second issue, and that has to do with economic growth and free trade. The standard model, the conventional wisdom today, is that we're enjoying tremendous economic growth once again in America because we got our federal deficit under control, and equally important, we kept inflation under control.

We then credit increased trade not so much with increasing our export base, as with keeping intense downward pressure on prices leading to the

control of inflation. If this was the major reason why we're now growing more rapidly, one would have to argue that freeing up trade and continuing to free up trade without any restrictions in the market would be necessary to grow.

But, indeed, the evidence seems to show that what we're really benefiting from today is not so much trade per se, but the final delayed impact of improved productivity due to investments that we made beginning with the public sector in information technologies.

I was asked in Germany who I would give credit to for the great American economic recovery. Is it Bill Clinton because he reduced deficits? Is it Alan Greenspan because he's kept inflation under control, or is it Ronald Reagan because he reduced the size of government?

My answer was none of the above. The person who's probably most responsible for our growth today is Nikita Khrushchev! He forced us into a space race. He forced us into a missile race, and we spent billions upon billions of dollars on defense and on NASA, which ultimately gave us integrated circuits and the ARPANET, which became the Internet, which gave us E-commerce and the growth that came about because of that. Ironically, to some to some extent the reason

why the United States is doing better than Germany or Japan today is that they were prohibited from spending so much money on defense. My final is that if we had a better understanding of growth, we'd come to the conclusion that public investment has been critical both in terms of basic research as well as infrastructure, education, and training.

My great concern is that today we have a model which says that free trade and deficit reduction are the keys to future growth, and in accepting this, we are beginning to neglect the investments that we really do have to make in basic research, in infrastructure, in education and training, which will maintain our lead in E-commerce and information technologies leading to a future of lower trade deficits.

Thank you very much.

CHAIRMAN D'AMATO: Thank you, Dr. Bluestone.

Mr. Kohl.