



## Stop Protesting Sweatshops

Guest: Benjamin Powell

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***Benjamin Powell is a professor of economics at Texas Tech University, where he directs the Free Market Institute. He is the author of Out of Poverty: Sweatshops in the Global Economy.***

**WOODS:** Well, I was excited for you when I heard last time that you had this book coming out from Cambridge. This is incredible. Your friend Ed Stringham has a book coming out from Oxford. What's the world coming to? This is fantastic.

I want to go right to the question that I think most people have. These firms that set up shop in the Third World, and they have working conditions that of course, nobody in the Western world would want to live under and work under: these firms are all really wealthy and they're making big profits. What would it cost them to just pay these poor people a few extra dollars an hour?

**POWELL:** A lot of people make silly comparisons with these companies. They will say, you are buying a set of Nikes for \$120, and the labor only costs \$5 and the materials \$10, and they imply that Nike is making this huge profit on each shoe. And of course that's not the case, because they have all the rest of their supply-chain costs. For that matter, the reason that Nike creates subjective value in lots of people's minds is the brand image, and you know, everybody wants to be like Mike, right? So the idea that these companies are making huge profits is wrong, but secondly, it's not even the case that Nike or these multinational corporations that people tend to protest are usually the employers of the sweatshop workers. It's usually domestic firms in these poor countries that are subcontractors, and aren't making a fortune on this, that are the actual ones who supply it.

But the general point here is: even if they were making billions in profits off each of these, it doesn't suddenly turn them into charities when you say, you're going to have to pay more for your Third World labor. These firms are trying to maximize profit, and they will keep hiring Third World labor right up to the point that it's no longer profitable. If you do something that mandates them paying more to these workers, they are going to use fewer of these workers and substitute more First World unionized workers or capital for the workers. Some of these Third World workers will get higher wages, but some who used to work in factories will get unemployed or they will compete with the even poorer workers in the informal sectors of these economies and push down wages there.

**WOODS:** I want to read to you a passage from our friend Roderick, Long who takes a different view from you on this general subject. He does favor boycotts against sweatshops. Not to shut the sweatshop down. He realizes that that would be counterproductive. But he says that what the people protesting sweatshops are demanding is not that the employers fire all their employees and close down the shops. Rather, they are demanding higher wages and better conditions. If a company responds to a boycott, not by improving its sweatshops but by closing them, and the boycotters respond by ending the boycott, then the boycott is being done in a counterproductive way. But that's a reason for condemning stupid anti-sweatshop boycotts, not for condemning anti-sweatshop boycotts per se. But then he says, what if the company can't afford to offer higher wages and better conditions? Sometimes that's the case, but with most of these international corporations, there's a sizable gap between what the employers are offering now and what they can afford

to offer while still remaining profitable, and he's saying, look, there have been examples of strikes that have often, or at least in some cases, succeeded, and that proves there must have been some gap between what the firm could offer and what it had been offering. What do you say to that? Roderick describes himself as a left-libertarian, and this is not an uncommon perspective among them. How do you respond?

**POWELL:** Yeah, I think there's actually a lot of misconceptions among left-libertarians, particularly ones who don't understand price theory. Roderick I wouldn't throw into that camp. I think he's one of the better ones, and I consider him a friend. But the problem here is if there really is a demand for these products that could pay higher wages, companies have every incentive to discover this market niche, pay their workers more, and market their products accordingly to appeal to consumers. The fact that they are not—and I am a good Austrian here: I don't believe markets are always in equilibrium or perfect or anything. Markets are a discovery process. But these firms have an incentive to discover this. The fact that this remains a relatively niche market, and I should also say one that's wrought with fraud, where people pretend to be so-called ethically branding when it's really just a scheme to enrich unionized workers in the United States. There's one group—"Shop With a Conscience" guide that promises all of its products are made sweat-free with unionized labor with good wages and good working conditions, but when you look at a map of their factories, they are almost all in the United States and Canada. You're not helping poor workers of the world when you do that. So I think Roderick is wrong in thinking that boycotts are necessary if there is actually a market for higher-wage, better condition products by appealing to U.S. consumers. If there was there, firms have every incentive to discover it.

Now, the second part of this, talking about that they could actually pay more. I actually think this is true, right? So how wages are determined are two factors. One, a worker's productivity. That's the maximum that a firm is willing to pay them. If they can create two dollars a day in revenue, the firm is going to pay a maximum of two dollars a day. But they'd like to pay zero. What makes them not pay zero is whatever the workers' next-best alternative is. That's the lower amount. So actual wages fall somewhere between those two bounds. Now, that means that it could be near the lower bound, and there could be room for firms paying more to get up to that productivity level, the productivity top bound. But when we study wages across economies, about 85 percent of the variation in wages is explained by productivity differences. This means in talking about that wage gap, and this is the bargaining power part, at most 15 percent of the differences in wages across countries can be explained by that. And that includes our error term, so it's not just that 15 percent comes from bargaining. *At most* 15 percent can come from bargaining. So it's really a sideshow, what Roderick is referring to. The real game is increasing productivity in these countries to raise that upper bound and get compensation up.

**WOODS:** In giving this answer, you're inviting us, in part, to consider the alternatives that are available to these people. How does the sweatshop compare to alternatives. You have a chapter in your book on comparing sweatshop wages to the alternatives, to what's being paid by firms that are native to the country as opposed to these sweatshops that come in from international concerns. How do they compare? The chapter is called "Don't Cry for Me, Kathy Lee." She got in trouble because I guess she had invested in or was in some way responsible for some Third World firm that was paying sweatshop wages, and she professed to be outraged and appalled at this. You are suggesting maybe she shouldn't have been.

**POWELL:** That's right. She actually cried on TV with an encounter with a young girl, Wendy Diaz, a 15-year-old who was working in her Honduran sweatshop for I believe \$0.31 an hour and she cried, apologized and said that she would make amends. But everyone was comparing the \$0.31 an hour to what someone might earn in the United States. It's the wrong comparison. Significant chunks of the population of Honduras at that time, large chunks, were living on less than \$2 a day of earnings, less than \$1 a day of earnings, and this girl's income was actually higher than those big chunks of people that were stuck in poverty, and she was only 15. And in fact, actually if you annualize her earnings, she was earning more as a 15-year-old girl working in the sweatshop than the average Honduran earned at the time. Her job was not one of the bad ones in that country. Instead, the informal sector, the agricultural work, and this is the norm. So the point here is that when these cases—and the Kathy Lee case is not an anomaly. What we did is we studied sweatshops across a number of countries from 1995 to now. In fact, what we used was U.S. news sources to identify places that had been protested as harmful sweatshops, documented the wages there, and then

converted it into purchasing power parity, so we're trying to control for differences of cost of living across countries so that we can compare it with these poverty thresholds of \$1 and \$2 a day. What we found was the average protested sweatshop in every country, including Bangladesh—the poorest of the bunch—got their workers above the \$2 a day threshold while large chunks—in Bangladesh about 80 percent of the population lived on less than \$2 a day.

We also compared it to average incomes in these countries, and we found sweatshops, some of them paid two to three times the average annual income. Most of the average sweatshops in these countries paid somewhere around average income, and there were a few that were significantly lower. But interestingly, almost all of those involved cases of migration—you'd find the sweatshops in Brazil paying a smaller percentage of the average income in there, but you find, though, that it's illegal immigrants from Bolivia who are working in Brazil, and if you compared it to the Bolivian alternatives it's far above average. So the general thing is these sweatshops job seem bad by our standards in the U.S. Compared to anything that's realistically available to the workers in these countries, these sweatshops are by and large much better.

**WOODS:** Well, what would be the harm of just having governments in these countries pass more stringent health and safety and working conditions laws, right? If we could get some kind of modest improvement, it would be forced on everybody who's in the country. They would have to do it. It would be a very, very minor blip on their bottom line. So why not just do that? And maybe we could come up with a continent-wide policy. Let's say all throughout some portion of Asia. Just in theory, imagine we had some regional government and it could impose working conditions laws and safety laws throughout that whole region, wouldn't that make those people better off because then the workers would have to be offered these improved conditions? It would be against the law not to offer them.

**POWELL:** Sure! And in fact some countries do have such laws. It's just they largely go unenforced or ignored. But let's say you do it worldwide, through a trade agreement. You're still going to have a shift in labor: as you raise the cost of labor in these poorer countries, more of the jobs will go to wealthier First World countries that already have good conditions. But secondly, to the extent that it does actually improve conditions in these countries, it's going to be at the expense of the workers—and I know that sounds weird, Tom, maybe not to you or to your audience, but for most audiences it does. Employers are relatively indifferent between compensating workers in wages or in other forms of compensation, be it improved working conditions, vacation time, shorter hours, what have you.

For the employer, a cost is a cost is a cost. It comes off their bottom line. If they have to pay the worker \$1.50, what they care about is the total of the \$1.50. They couldn't care less whether it's \$1.50 in wages or whether it's \$1 in wages and \$0.50 in improved working conditions. Who does care are the workers. Workers care about their mix of compensation. These workers are desperately poor and trying to feed, clothe, and shelter their families. When you are in that situation, you want the vast majority of your compensation in wages. Over time, as productivity increases and you become more productive and wealthier, you demand more of your compensation in these other things. These are what economists call "normal goods." This is the process that happened in the United States and Great Britain. It didn't come about through labor laws.

In fact, this is a mistake that many people make. They see our labor laws, and they think it's because of these laws that we escaped the Gilded Age and the industrialists exploiting us. Hogwash! These laws came in after the fact, after competition that already improved health, safety, working conditions, child labor, etc.

**WOODS:** I had George Reisman on the program last year talking about whether robots are going to take all the jobs, and somehow we wound up segueing into the subject of working conditions. He just has this methodical, step-by-step, relentless, laser-beam presentation of exactly what you just said, and it runs so contrary to what people think that it's immensely frustrating sometimes to try to convey it. But once you see it, you see it.

And of course, you can think about your own situation today. If we just extrapolate and apply the same principle to the idea of maximum-hours legislation, we could all work 120 hours if we want. But eventually we got to a point where we're able to earn enough in 80 hours, or 60 hours, or 40 hours, that we prefer the

leisure time. And so to impose on us maximum-hours legislation before we were prepared to prefer that leisure time, that may seem like it's helping us, but of course it's just diminishing our options.

You have a chapter called "A History of Sweatshops, 1780-2010." I think when economists make the sorts of arguments that you make about sweatshops, what they are saying either explicitly or by implication is that the history of sweatshops is such that over time, sure, you start off with terrible conditions, you start off with sweatshops, but these countries gradually wind up with more prosperity, higher real wages, greater productivity, better working conditions. Is that what has happened, and what is the process? What is the process by which I go from earning a sweatshop sort of wage, and then 40 years later things have changed, and I am earning a much better wage? How does that happen?

**POWELL:** You and I both have experience with this, Tom. You are a North Shore Boston guy originally as well. So we grew up in the area where sweatshops were in the United States. I am from Haverhill, Massachusetts, that's known as the "shoe city" because it was the big shoe producer in the United States at the turn of the century. What we had there and in Lowell, and in other industrial cities at the time were what sweatshops are in Third World countries today. The proximate causes of economic development of higher standards of living are capital and technology. What do sweatshops bring with them? Capital and technology that start improving productivity. Where did the United States get ours? You are a historian. You know we stole the technology from Britain initially, and then a lot of capital and investment actually came from Britain throughout the century, and we accumulated our own. Our process and Great Britain's process of course, was a 100- to 150-year process if you want to date the start of the Industrial Revolution to something that looks like post-sweatshop working conditions, because all of the capital had to be created anew. All of the technology had to be discovered. Today that process can go much more quickly. If I said, "Tom, what's a sweatshop country?" and we were talking in 1960, it's going to be Hong Kong, Taiwan, Singapore, South Korea, even Japan a little bit maybe. These were the places that garment production shifted, post-World War II years too, and that— except for Japan—had pre-industrial standards of living, under \$3,000 per capita for the year.

These textile factories had these same poor working conditions that we had had in Britain and the U.S. and that exist in Bangladesh and India today, but in about a generation, a generation and a half, they went from pre-industrial, to post-sweatshop First World living standards to today, with some of their cases, like Hong Kong, being wealthier than the United States. It's because the world has so much more capital and technology now that when you get your institutions right, these things can flow in and drive the process of development much quicker. Some people mistakenly characterize this as a race to the bottom: that as soon as the country gets richer, those sweatshops leave and go find poor labor somewhere else. Well, yeah, but it's not like Hong Kong was left in shambles when the sweatshops left. The problem was labor got too productive in Hong Kong, so it was too valuable to use in making garments, and garment factories could not bid enough to get those workers there compared to the other industries they were competing with. So they left and went to another place. Sweatshops are the bottom or second-to-bottom rung on the ladder of economic development, and as they leave your country, it's a sign that you've graduated to a higher standard of living and someone else is about to get on that train.

**WOODS:** Ben, what about the issue of child labor? How does that come into your analysis?

**POWELL:** Sure, save the children. Listen, children don't work—and you know this—because their parents are mean. Children work because their families are desperately poor and need the income. Banning products made with child labor does not change that. Those families are still desperately poor and need the income. Most children don't work in manufacturing that exports products to us. Most children in countries where sweatshops are located work in agriculture or household services. In both of those sectors, the pay is lower than in manufacturing, and in the case of agriculture it's also more dangerous for the children than working in manufacturing. So when we ban products with child labor, it shifts them into these other, less productive industries where they are also going to build less human capital to have higher future earnings. In some cases it's disastrous. There's a famous case in the '90s when a congressman, Tom Harkin, opposed banning products from Bangladesh made with child labor, and in response Bangladeshi factories fired a bunch of children and Oxfam—no right-wing group here—went in and investigated and found that many of

them became child prostitutes or starved. So the same analysis that we apply to adults applies to children too. Child labor disappears as income goes up. If you get up to about \$11,000 per capita, child labor vanishes. Countries with \$11,000 per capita do not have child labor, and really, the only countries where child labor is prevalent is when you're down around \$3,000-\$4,000 per capita or less, you get about a third of children working.

As you escape poverty, children cease to work, and that's what happened here in the United States too. In fact, we didn't even have national child labor legislation until 1938. Adjusted to today's dollars, our income at the time was about \$10,500. So once the process of development had eradicated child labor, we passed a child labor law that said children couldn't work. Until then, we didn't have a prohibition at the national level. Some states did, but they were non-binding. My home state, Massachusetts, had the first child labor law I believe in the 1860s, and it said something on the order of: children under 12 are not allowed to work more than 10 hours per day in a factory. It simply wasn't a binding constraint. So these laws, just like health and safety ones, come in and codify it after the process of development has already happened.

**WOODS:** Ben, is there anything that activists, so-called, can do when faced with sweatshops and seeing that people are working in poor conditions? Is there anything they can do that isn't counterproductive?

**POWELL:** Yeah, I think there is. I think if they want to do activism, one thing that they could do is go around and actually monitor the people that are claiming to produce sweat-free products and expose frauds like this Shop with a Conscience Guide that are really ways to transfer wealth to unionized, First World workers. But if we're talking about things that will actually make a difference in the lives of people who work in sweatshops today, probably the number-one thing they could do is drop the cause of sweatshops and become advocates for more open borders. If you really want to improve the lives of someone who works in the Third World, allowing them to come to the United States will make their income jump by a factor much greater than anything you could hope to accomplish in their home country. The reason these people are poor, the proximate causes, are lacking capital and technology, but the underlying cause is that these countries have really bad governments that don't protect property rights, that don't give you a reasonable rule of law or economic freedom. I like to complain about our lack of freedom here in the United States but compared to where these countries are we have a much better and much freer environment here, and these people can flourish. If you move a Haitian from Haiti to the United States they become so much more productive than anything you could hope to accomplish in Haiti.