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Rethinking California's Policy Options in a Global Economy

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California has much to trumpet regarding its performance in the international economy. As the nation's leading exporting state, California saw its goods exports rise from $58.4 billion in 1990 to $129.7 billion in 2000, an increase of more than 120 percent, compared to 99 percent for the nation as a whole. As of 1998, the year with the latest available data, almost 603,000 Californians worked in foreign-owned firms – the highest level of any state in the nation – while the value of property, plant, and equipment these firms owned in California measured $104 billion – again the highest level.[1]

It is understandable that state policymakers want California to continue to capitalize on foreign trade and investment. In this context, I want to point to three issues not normally considered in planning California's engagement with the world economy.

<u>What do we export?</u>

There has been a tremendous focus on policy to increase exports by California firms, with the discussion centering on goods exports. World trade in services is growing, and the Uruguay Round Agreements of 1994 finally succeeded in formally bringing services trade under international discipline through the General Agreement on Trade in Services. In 2000, U.S. services exports accounted for almost 28 percent of total U.S. exports, goods and services combined. For every dollar's worth of goods exports, there was 38 cents worth of services exports. Can California ignore this?

Services trade for California means tourism, education, banking and finance, professional services, port services, airport activity, and other categories. Any future trade planning by the state should include serious thinking about how to expand trade in services, especially since California likely has a comparative advantage in services relative to the rest of the United States.

<u>What Other Policy Areas are Essential to Expanding Trade and Investment?</u>

Let me give you what I think is a stunning figure to consider. In the year 2000, almost 45 percent of America's imports of parts of electronic integrated circuits and microassemblies came by air through the Customs District of San Francisco, which, in the case of trade by air, mostly means San Francisco International Airport. In fact, California's ports and airports play a key role in a

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[1] After these comments were written, the 1999 data became available and give the same picture. Employment totaled almost 639,000, while gross property, plant, and equipment measured almost $116 billion. Both place California first among states.

large share of all U.S. trade. When the glamour of international deals passes, the detailed work of moving the product remains.

Trade infrastructure is an obvious means by which California can benefit from engagement with the international economy – the rest of the nation needs us. Yet is there any serious thinking at the state level about California's trade infrastructure? True, this can be a sticky issue politically because airports and ports are local entities. But because the state's – and even the nation's – economic well-being rests in part on the fitness of California's airports and seaports, state policymakers must participate. At a minimum, the state could consider trade infrastructure as a whole, forecast the growth of demands on it, and offer an analysis of statewide needs. These actions can focus attention and develop momentum for local authorities to address these needs, individually and cooperatively.

Are Exports and Inward Direct Investment Enough?

It should not be difficult to find a California firm that might otherwise have failed if it had not found a foreign supplier to make an essential input. Nor should it be difficult to find a firm that was able to expand its U.S. operations and create more jobs because it was able to invest overseas to better compete against foreign companies. Nor should it be difficult to find a California consumer made happier through the purchase of some product made in Japan, or France, or Chile, or Botswana. Yet the state focuses exclusively on exports and inward direct investment.

There are sound political reasons for doing this, yet the economic reasons became old with the publication of Adam Smith's *Wealth of Nations* in 1776. Whether we like it or not, imports and outward direct investment can be economically beneficial. In addition, all aspects of international economic exchange are tied together– outward direct investment creates export opportunities, while inward direct investment often leads to imports.

What does this mean for California? It means simply that the World Trade Commission should focus on how California can benefit from the global economy rather than how California can increase exports and inward direct investment. It should be within the purview of the Commission to recommend policies that will increase California's benefits from the global economy by any means. Because of the political realities, it may be that the state will need to support the beneficial aspects of globalization through cooperation with other trade entities, such as the World Trade Centers, rather than directly. The important point is that the state should not constrain its policy options as it considers the missions of the Technology, Trade and Commerce Agency and of the World Trade Commission.