The Economy in Perspective

Fabricating the truth…We hear and read so many opinions, from so many sources, that it is often difficult to tell fact from fiction. Some opinion makers seem to operate under the premise that there are no longer any facts—that everything today is just a matter of subjective interpretation. But most people want to believe that what they value is true, and there is a plethora of interest groups whose livelihood depends on spin, hype, and packaging.

Economists are trained to resist these foibles of human nature, but we are not perfectly immune to them. Diversity of opinion is not rare among our ranks, and we have even been known to overreach in debate. However, economists are also critical consumers of news stories, and there are days when so-called "economic reporting" drives us up the wall. Here are a few pet peeves, culled from numerous news accounts.

Small businesses create most of the jobs in the U.S. economy. It's easy to get a warm, fuzzy feeling about the role of small businesses. They're the stuff that the American dream is made of: the opportunity to begin a venture in your garage and end up a millionaire. But exactly what are small businesses, and how do they contribute to jobs? Although definitions vary for certain purposes, the U.S. Small Business Administration suggests that a small business is generally one that employs up to 500 people. Data on the distribution of firms by size indicate that roughly 99.5 percent of all businesses in the United States fit this definition. Moreover, although small businesses account for about three-fourths of the new jobs created, only half of all employment is located in small businesses. This means that the one-half of 1 percent of the firms that are not small businesses account for the other half of employment. These figures also show that although small businesses generate new jobs, they also contribute the overwhelming fraction of all jobs lost in the U.S. economy.

Business reporting may miss the mark in two respects. Some stories focus on small firms' importance in economic development, when large firms' expansion might be equally virtuous. Other stories focus on big companies' layoffs, not realizing that employment growth in small firms might offset corporate reorganizations. More informative reporting might result from paying less attention to a firm's size and more to industry dynamics and underlying economic issues.

Trade barriers protect jobs. In behavior that has been evident for millennia, every industry, organization, and occupation tries to protect itself from competition. When interest groups ask the government to shield them from domestic competition, watchdogs are usually quick to cry foul over proposed trade restraints. Yet foreign trade protection rarely elicits the same degree of public opposition. It seems more sensible to the public that a nation would impose tariffs or quotas against certain products made in other countries, in order to shelter domestic producers and their employees from competitors (usually branded cutthroats and dumpers). Although the situation of protected groups is generally improved, the nation that protects them is generally not better off as a whole. Why not? Domestic consumers usually pay more for the protected items after barriers are erected—they are transferring some of their wealth to the protected parties. In addition, protected industries have less incentive to improve quality or to innovate. Finally, restricted imports invariably mean reduced exports—and fewer jobs in export industries—because foreign residents are denied opportunities to earn dollars that will buy our goods.

Media accounts of trade protection often focus disproportionately on the protected industry's value to the national welfare but neglect the cost of restricting imports and losing export opportunities. In most instances, foreign trade barriers ought to inspire as much skepticism as domestic ones.

The U.S. should reduce the exchange value of the dollar. The exchange value of the dollar, much like that of any commodity, is determined by the preferences of buyers and sellers in a very competitive global market. Strong foreign demand for dollar assets probably drove the dollar's nominal exchange value higher during the last decade, benefiting those who borrowed U.S. dollars for capital investments or consumer and home loans. This is another example of some groups benefiting more than others from a strengthening dollar. The U.S. government could weaken the dollar by encouraging an inflationary monetary policy or by discouraging investment in U.S. firms, but such strategies would not help the public at large, even though certain industries might be better off. Once again, a story that asks who wins and who loses from public policies is likely to be more informative than a story that pays most of its attention to vested interests.