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NATIONAL INDUSTRIAL POLICY: AN OVERVIEW OF THE DEBATE

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INTRODUCTION

Through the passage of a wide range of government initiatives, grouped under the rubric of "national industrial policy," a growing coalition of American political, labor, and business leaders is seeking to realign in a fundamental way public and private decision making in the economy. The proponents' objectives are laudable: to renew economic prosperity and growth in national wealth and to enhance social justice. The attendant rhetoric, however, echoes appeals of bygone generations of social reformers intent upon spurring social improvement through greater government control of the economy. Senator Gary Hart (D-CO) has summarized a now familiar political theme within the movement: "Today, more than at any other time since the Depression, traditional policies are producing unintended consequences. They are increasingly irrelevant to the unique economic realities of this decade."[1]

What Hart and many other industrial policy champions argue is that a new holistic approach to public policy can be forged by "melding" the "Jeffersonian principle of free competitive economy"

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1 Gary Hart, "Restoring Economic Growth," a policy statement presented to the National Committee Strategy Council, February 6, 1982, p. 1. These views are recited by Robert Reich, Professor of Business Policy at the Kennedy School of Public Policy, Harvard University, in his new book The Next American Frontier (New York: Times Books, 1983).

with the "Rooseveltian principle that economic success cannot be divorced from social conscience."[2] Senator Ernest Hollings (D-SC), for instance, stresses that we need a "unity of purpose" to economic policy.[3] A founding father of industrial policy is Harvard University Professor Robert Reich. In The Next American Frontier, he contends that "in the emerging era of productivity, social justice is not incompatible with economic growth, but essential to it. A social organization premised on equity, security, and participation will generate greater productivity than one premised on greed and fear."[4] Mirroring Hart's vision of the industrial world (or, perhaps, having originally articulated that vision for Hart), Reich writes, "America has a choice: It can adapt itself to the new economic realities by altering its organization, or it can fail to adapt and thereby continue its present decline....But failure to adapt will rend the social fabric irreparably. Adaptation is America's challenge. It is America's next frontier."[5]

The trouble with this new talk about industrial policy is that it is not new. It is at least as old as the 18th century's mercantilism and as familiar as this century's disastrous experiments with central planning, the corporate state, and five-year plans. From what industrial policy proponents have been saying so far, there is no reason to believe that their repackaged schemes will be any less catastrophic than the earlier models. To be sure, most industrial policy enthusiasts have noble concerns. But their arguments are replete with internal contradictions that draw into question the movement's intellectual foundation. While several specific policy proposals warrant examination by Congress, mainly because they attempt to correct problems with existing policies, much of what has been proposed as "national industrial policy" is a 1980s version of the social politics of the late 1960s and early 1970s. It calls for more federal money and more federal intervention in the activities of workers, businessmen, investors, and consumers. Strangely, the lessons painfully learned in the past decade seem to be willfully ignored. What is most alarming is that backers of these policies fail to acknowledge, or choose to ignore, a critically important and central point in such debates: government control of capital ultimately translates into control of people, whether the control is instituted by democratic or by authoritarian means.

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2 Ibid., p. 4.

3 Ernest Hollings, "Statement of Candidacy," remarks presented at Midlands Technical College, Columbia, South Carolina, April 18, 1983.

4 Reich, op. cit., p. 20.

5 Ibid., p. 21.

MAJOR POLICY PROPOSALS[6]

As evidenced by the array of policy proposals, national industrial policy (NIP) means different things to different people, a point that may go far in explaining the political appeal of calls to join the movement. Consider several of the major proposals of frequently cited industrial policy advocates.

The Hart Proposals

Senator Hart offers a reasonably complete, broad-based policy menu:

*To encourage investment in physical and human capital, the tax code should be changed to a progressive expenditure tax, exempting savings from taxes and thus stimulating investment.

*To encourage new investment and to reduce the tendency of the 1981 tax cut to favor existing firms over emerging firms that have limited capital bases and, therefore, have minimal depreciation allowance to deduct from taxable corporate profits, the tax code should allow capital expenditures to be treated as an expense. Further, a new form of common stock should be created. Called "new capacity stock," it would be used to finance new plant, equipment, and research and be exempt from capital gains taxes.

*To encourage "new entrepreneurial frontiers," federally financed "Venture Development Centers" should be established to provide technical assistance and seed money to small businesses. The corporate income tax rate would be reduced for small businesses, and small business shareholders would be allowed to deduct company losses from their taxable personal income.

*To stimulate research and development, federal support of science and engineering schools would be increased, the patent laws would be strengthened, and government procurement policies would "pull technological progress forward."

*To expand global markets for American goods, the federal government would free international trade of tariff and nontariff barriers and eliminate export subsidies provided to other countries' industries.

*To reduce the crowding out effect of government deficits, the 1983 tax cut was to have been postponed, while defense expenditures would be trimmed by $20 billion. To reduce inflationary pressures, a "Tax-Based Incomes Policy" would impose a tax penalty on price

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6 For a description of specific legislative proposals before Congress, see an accompanying paper by Gregory L. Klein, "Industrial Policy: A Summary of Bills before Congress," Heritage Foundation Issue Bulletin No. 96, July 12, 1983.

and wage increases exceeding a "pre-established target" and would focus on the 2,000 largest firms in the country.

Hart would also revise anti-trust laws to allow for more joint research and development projects among competing domestic companies, impose a "security fee" on imported oil that would reflect the now-hidden cost of our "energy vulnerability," and expand federal aid to education, incorporating a "GI Bill in Reverse," meaning a program under which students would pay back their federally subsidized loans by work in areas of "national need."[7] Generally speaking, Hart's NIP is designed to ease what he sees as the adjustment process of "old line basic industries," commonly called "sunset industries," and to facilitate the emergence of small high tech firms in what are described as "sunrise industries."

The Reich Proposals

Robert Reich believes that the key to revitalizing the American economy is "adaptation" to the new economic realities of production. These he defines as flexible production processes, highly skilled workers (the presumed source of America's comparative advantage in international commerce), and "precision, custom, and technology-driven products." Such adaptation, for Reich, requires a number of policies similar, but not identical, to those of Senator Hart:

*To reduce structural unemployment and to speed the "adjustment process," Congress would enact an unemployment voucher system by which the federal government would pay half of firms' costs for training people unemployed for longer than three months. Even larger subsidies would go to those firms training workers in areas of high unemployment. Retraining vouchers for those unemployed for more than two years would be redeemable at universities and technical colleges. In addition, companies could establish "human capital reserves"--funds set aside to reflect the depreciation of the skills of the company's employees. These reserves would lower corporate profits and would be used to upgrade worker job-related skills, just as similar reserves now are used to replace worn-out equipment.

*To reduce the "inequity" in the current disparity in tax treatment of human and physical capital and the inclination of physical capital to move, a "human capital tax credit," in connection with training costs, similar to the investment tax credit on physical capital, could be instituted, which would lower the after-tax training and retraining costs incurred by businesses.

*To reduce forms of "paper entrepreneurship" (specifically, mergers and acquisitions and tax avoidance), the tax code could

7 Hart, op. cit., pp. 1-35.

allow an interest deduction only for purchasing new or modernizing old plants and equipment.

*To reduce cyclical unemployment, unemployment insurance taxes would be more directly related to the unemployment experience of firms.

*To ease the decline of decaying industries, such as textiles, steel, automobiles, and rubber, "regional development banks," along the lines of the Reconstruction Finance Corporation of the Great Depression era, would be organized to provide low interest rate, subsidized loans to companies promising to retool and retrain workers or, in Reich's words, "to restructure themselves to become more competitive."[8] With their federal subsidies, such banks could redistribute investment funds among regions, urban and rural areas, and industries with the intent of enhancing social justice and job security and facilitating the adjustment process.

*To reduce the adversarial relationships that now presumably exist among businesses, labor groups, and government, tripartite councils would be organized. Such councils would seek consensus (which Reich acknowledges may be difficult to achieve) on how capital investment would be allocated differently than it is in free capital markets.

*To relieve unemployment and other social problems, the federal government would offer grants to entice firms to hire the unemployed, handicapped, or other groups subject to discrimination and unfortunate circumstances. Washington also would fund, through firms, such social services as "health care, social security, day care, disability benefits,...and relocation assistance."[9] In short, "firms will become the agents of their employees, bargaining for different packages of government-supported social services."[10]

*To ensure that the programs negotiated by firms with government are run with the workers in mind, a form of "industrial democracy" would be imposed. The employees "will elect representatives who will select the combination of benefits and choose the providers. Through labor-management councils, also including worker representatives, workers will participate in company decisions about physical capital, helping to choose the direction and magnitude of new investment in research, plant and machinery."[11]

In summary, Reich starts with the propositions that the economy, as now organized, is insufficiently adaptive and that

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8 Reich, op. cit., p. 243.
9 Ibid., p. 248.
10 Ibid.
11 Ibid.

even now there is no "free market" due to extensive federal subsidies to businesses and government protection from domestic and international competitors. In Reich's view, the federal government already has an "industrial policy." Yet it lacks sufficient coordination to serve the broad general public. No expanded involvement in the economy by the federal government is necessary, says Reich. He maintains that Washington simply could use the subsidy and protection resources already at its command to extract public benefits from businesses.

The Mondale Proposals

Having acclaimed Reich's book as "one of the most important works of the decade," former Vice President Walter F. Mondale has not sketched in the details of his own brand of industrial policy. Instead he complains that the country's industrial policy is "destroying industry--not building it."[12] The broad outlines of his NIP include five strategies:

*First, he believes something must be done to reduce "wasteful mergers and acquisitions."

*Second, he suggests altering the anti-trust laws to allow more joint research and development ventures to "enhance international competitiveness without reducing domestic competition."[13]

*Third, "we've got to shape a policy to keep high technology here at home," because companies are shipping high technology production jobs abroad and "leaving the lower-end jobs here at home."[14]

*Fourth, he endorses the call of other liberals for the creation of an "Economic Cooperation Council" with functions similar to those of the old Reconstruction Finance Corporation.

*Fifth, he wants federal aid to "those communities and regions hit hardest by economic change," which for him means "targeting infrastructure programs and impact aid--automatically triggered by measures of distress" and adopting plant-closing restrictions.

Though insisting that he is a "profound believer in our free enterprise system," Mondale hastily adds that "government must work in partnership with the market."[15]

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12 Walter F. Mondale, address to the Twenty-First Constitutional Convention of the United Steel Workers of America, September 11, 1982, p. 5.

13 Walter F. Mondale, excerpts from a speech to the Industrial Union Department Legislative Conference, May 4, 1983, p. 2.

14 Ibid.

15 Ibid., p.4.

The Rohatyn Proposals

Felix Rohatyn is a New York investment banker, who wants to revitalize the national economy by applying principles he learned while heading the New York Municipal Assistance Corporation, the agency established to prevent New York City's bankruptcy. Like other NIP enthusiasts, he wants to expand the economic role of government. Examples:

*Along with Reich, Rohatyn advocates establishing a reinvigorated Reconstruction Finance Corporation (RFC) to allocate capital as directed by a council of labor, business, and government leaders. The bank's activities would be financed by a higher gasoline tax. The central task of the council would be to "allocate sacrifice."

*To reduce problems caused by unexpected inflation and to moderate competing claims on the national income realized in strikes, "Annual negotiations resulting from one year contracts with no cost-of-living escalators" should be institutionalized.

*To improve labor-management relations, a "larger share of the compensation package [would be] in the form of profit sharing."

*To better coordinate U.S. domestic policies with Western Europe and Japan, the U.S. should consider recreating "something like the Bretton Woods agreements," providing for central bank intervention within certain bands of exchange rates, like the European monetary system.

*To permit underdeveloped countries to develop, to "avoid enormous distress in those countries," to enable underdeveloped countries to repay their loans, and to avert protectionist measures, the International Monetary Fund should be "reliquified." This means increasing U.S. contributions to the IMF.[16]

Rohatyn admits that he tends to "look at money as a tool or a weapon...to leverage concessions from unions, suppliers, banks, management, legislatures."[17] He justifies this by arguing that "the basic issue to me is whether we have a government with a philosophy that will look upon intervention as a philosophical imperative when disparities in the country become too great, or whether government's philosophy is simply to take its hand off the steering wheel and let the market work its will."[18]

The Thurow Proposals

MIT economist Lester Thurow bases his prescriptions on his diagnosis "that our economy and our institutions will not provide

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16 These positions are discussed in Jeremy Bernstein, "Profiles: Allocating Sacrifice," The New Yorker, January 23, 1983, pp. 45-78.

17 Ibid., p.78.

18 Ibid.

jobs for everyone who wants to work" and that "we have a moral responsibility to guarantee full employment."[19] To him, the federal government must be employer of last resort paying wages above the minimum and (in agreement with other NIP advocates) expanding training and retraining programs. He acknowledges that this would "create a socialized sector of the economy."[20] Quips Thurow: "[m]ajor investment decisions have become too important to be left to the private market alone....Japan Inc. needs to be met with U.S.A. Inc."[21]

Seconding Reich, Thurow wants to use the government to accelerate the transition from sunset to sunrise industries.[22] To the extent that government helps people make the transition, the risk of economic change is "spread" among all citizens--a point also emphasized by Reich above and in the Bluestone/Harrison proposals considered below.[23] He believes that private investment banking should once again be made legal and that public investment banking, such as Rohatyn's new Reconstruction Finance Corporation, could be organized to lengthen private managers' time horizons that, according to Thurow, "are too short to encompass projects that will not pay off for a decade and too many benefits cannot be captured by the firm making the initial investments."[24] Thurow advocates the establishment of a "Ministry of Technology" to encourage civilian industrial research.[25]

The Ford Proposals

Practically every two years for the past decade, Representative William Ford (D-MI) has introduced a proposal to restrict plant closings. The first proposal, which was introduced in the Senate in 1974 by Walter Mondale, concentrated primarily on the problem of the "runaway shop"--those firms that pull up stakes in one locality and reestablish elsewhere. More recently, Ford has been attacking plant closings in general, even those resulting from firms going out of business altogether. Closed plants cause unemployment, says Ford, and create many economic and social problems for the workers and communities involved. As such, he wants to restrict closings to ameliorate these problems. At issue is the basic right of firms to open and close, expand and contract their businesses.

Ford's current proposal, called the National Employment Priorities Act of 1983, embodies a number of industrial policy concepts:

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19 Lester C. Thurow, The Zero-Sum Society: Distribution and the Possibilities for Economic Change (New York: Penguin Books, 1981), pp. 203-204.

20 Ibid., p. 206.

21 Ibid., p. 192.

22 Ibid., pp. 191-193.

23 Lester C. Thurow, testimony prepared for the House Subcommittee on Economic Stabilization, June 14, 1983, p. 2.

24 Ibid., p. 3.

25 Ibid., p. 4.

*To remedy the social and economic problems felt by workers and their communities when a plant closes, Congress would require firms that close plants

1) to give up to one year's notification of a pending closing,

2) to provide severance pay equal to 85 percent of one week's average pay for up to fifty-two weeks, not to exceed $25,000,

3) to continue the employer's contribution to employee benefit plans for up to fifty-two weeks, and

4) to provide restitution payments to the communities where plants are closed equal to 85 percent of the average tax payments of the three years prior to closing.

*To discourage firms from moving outside the U.S., such firms would have to pay community restitution of 300 percent of the average tax payment of the three years prior to closing.

*To prevent plants from closing, the federal government would provide

1) technical assistance helpful in avoiding closure,

2) aid to firms in the form of "loans, loan guarantees, interest subsidies, and the assumption by the Secretary [of the Treasury] of any outstanding debt of such concern,"

3) subsidies to employee groups interested in buying their plants and keeping them open, and

4) targeted procurement plans that would save faltering industries.

*To ease the adjustment process when plants do close, federal assistance would be provided workers to cover training programs, job placement services and job search, and moving expenses.[26]

The Bluestone-Harrison Proposals

Economics professors Barry Bluestone (Boston College) and Bennett Harrison (Massachusetts Institute of Technology), in their book The Deindustrialization of America, accept the contentions of Congressman Ford that plant closings cause social problems that extend beyond the private spheres of managers, their workers, and even their immediate community. They believe also that private firms, interested almost exclusively in making profits, are recklessly "deindustrializing" the country. As such, many of

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[26] National Employment Priorities Act, H.R. 2847, U.S. House of Representatives, 98th Congress, 1st Session, May 2, 1983.

these problems can be remedied by increasing the cost of closing via closing restrictions, because closing restrictions convert into operating costs, and they make continued operations relatively less costly than closing for many firms. Though Bluestone and Harrison endorse the basic precepts of Ford's National Employment Priorities Act, they have advocated even tougher restrictions on closings.[27] What Bluestone and Harrison explicitly want is the radical reform, if not outright socialization, of the U.S. economy. Their panacea is called national economic democracy and planning, in which "a rising standard of living for working people, more equally shared" will be substituted for private profit as the guiding criterion for economic decisions and in which "humanization of the workplace should be the major objective of any truly democratically planned restructuring of the economy" (emphasis in the original).[28] Their industrial policy entails worker buyouts, government bailouts, and "selective" nationalization of industries. Central to their NIP scheme are "'planning agreements' between the public and private 'partners,' on policies concerning pricing, location (and relocation), sourcing, automation, affirmative action in hiring and promotions, health and safety, environmental protection, and the maintenance of the workplace environment conducive to greater experimentation with new forms of internal economic democracy."[29]

Bluestone and Harrison conclude that the principles of any newly established industrial policy should include, at a minimum:

* spreading the burden over all the citizens of the society;

* public disclosure of company data to enable democratically constituted bodies to decide whether and to what extent assistance is needed;

* research by and consultation with workers in the affected plants and advisors of their own choosing;

* planned agreements with companies receiving bailout, specifying a quid pro quo with respect to increased democratic management of production, restrictions on the subcontracting of components or supplies to nonunion or foreign shops, the phasing in (and control over the use) of new technology, new plant location, and product pricing; and

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27 The National Employment Priorities Act of 1979 required firms to give up to two years notice of a pending closure. The length of notice then depended upon the number of employees affected by the closure, as it does today.

28 Barry Bluestone and Bennett Harrison, The Deindustrialization of America: Plant Closings, Community Abandonment, and the Dismantling of Basic Industries (New York: Basic Books, 1982), pp. 244 and 245.

29 Ibid.

* some government ownership of the subsidized corporation.[30]

More explict than other NIP proponents, Bluestone and Harrison chart a course for centralized economic planning, tempered by the demands of active worker participation in the decision making of their firms.[31]

The Hollings Proposals

Drawing on his experience as Governor of South Carolina from 1958 to 1962, Senator Ernest Hollings sees expanded educational opportunities, especially technical and science education, as a central ingredient of any industrial policy recipe. This implies, however, a return to past policies--more federal money for nutrition, child care, community health centers, student loans, as well as more federal dollars for science, math, and on-the-job training, including a $5,000 across-the-board federal pay hike for all teachers in the country (which would add $14 billion to the federal budget, virtually doubling federal outlays on education). At the same time, Hollings wants to freeze aggregate spending and opposed the individual tax reductions. He argues that the federal deficit must be cut to make more private savings available for investment. He also strongly supports greater protection from imports, especially textiles, a dominant industry in his home state. Although his program lacks specifics, Hollings talks of government becoming involved in "planning" and acting as a "catalyst in bringing business, labor and agriculture into partnership." He says: "We would not have a fixed industrial policy. But the many facets would amount to the best industrial policy."[32]

The Wirth "Yellow Brick Road" Proposals

After months of hearing proposals for industrial policy, the House of Representatives Democratic Caucus Committee on Party

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30 Ibid., p. 256.

31 The Bluestone/Harrison proposals are not the most extreme in the industrial policy movement. Professors Samuel Bowles (University of Massachusetts), David Gordon (New School for Social Research), and Thomas Weisskopf (University of Michigan) advocate "An Economic Bill of Rights" that includes the right to "a decent job,...public child care and community service centers, a shorter standard workweek and flexible hours, flexible price controls,...public commitment to democratic trade unions,...democratic production incentives,...democratizing investment, money, and foreign trade,...environmental democracy,..conservation and safe energy,...good food, a national health policy." Samuel Bowles, David M. Gordon, and Thomas E. Weisskopf, Beyond the Waste Land: A Democratic Alternative to Economic Decline (Garden City, New York: Anchor Press/Doubleday, 1983), p. 270.

32 Hollings, op. cit., p. 3.

Effectiveness issued a wide-ranging report that, because of the color of its cover, is known as "The Yellow Brick Road."[33] It is packed with platitudes and vague generalities. Congressman Timothy Wirth (D-CO) is emerging as the primary spokesman for the package. According to Wirth, the "Yellow Brick Road" rests on four cornerstones:

*Boosting the level of gross national product spent on research and development to a goal of 3 percent, providing new incentives to entrepreneurs, helping universities upgrade their research equipment, and encouraging innovation in the economy.

*Improving the education and training needed to compete in the world economy, including making computer literacy a goal for all students, and attracting talented teachers and professors in areas of special needs such as science, mathematics, and foreign languages. A major public-private effort to train and retrain workers in sectors of declining employment so they can become productive in areas of increasing employment.

*Rebuilding the decaying public infrastructure.

*Investing in energy resources with the goal of becoming a net exporter by 1990, through expanding coal exports, building on solar technologies and conventional and unconventional drilling techniques, and returning to an aggressive energy conservation effort.[34]

These programs would be funded by higher taxes for segments of the population and by shifting a greater share of the burden of defending the West to our allies. These programs would also be coordinated by an "Economic Cooperation Council to help our country gather the right information and improve our ability to make long-term economic decisions--not as a centralized monolithic planning agency, but as a national arena to clarify complex choices and build broad support for national initiatives."[35] Given its description in a bill being prepared (at this writing) for introduction, we must assume that the Council will be composed of interest groups, such as the AFL-CIO, National Association of Manufacturers, the Chamber of Commerce. It would raise legitimate fears of economic policies being guided in the interests of the established "corporate state." Suggestions in the proposal that the Council will seek and recommend a consensus by those in the assembly imply that Congress will, if the bill is passed, delegate a portion of its policy-making duties to the interest groups fortunate enough to be represented on the Council (which will

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33 Democratic Caucus Committee on Party Effectiveness, Rebuilding the Road to Opportunity: A Democratic Direction for the 1980s (Washington: Committee on Party Effectiveness, September 1982).

34 Timothy E. Wirth, "A Democratic Policy Agenda for the Future," Wall Street Journal, October 19, 1982, p. n.a.

35 Ibid.

necessarily exclude the interests of many groups). And it means that economic issues, like the allocation of capital or which industries will "win," will have to adjust their economic behavior to the consensus, which will reflect "truth" as seen by the political power structure. Economic behavior will be further standardized in a very large nation noted for diversity.

Other Proposals

Among the less ambitious industrial policy proposals suggested, Joel Kotkin and Dan Gevirtz, co-authors of a forthcoming book entitled A Business Plan for America, focus on policies designed to encourage entrepreneurship. They suggest that the federal government should (1) eliminate the capital gains tax, (2) dispense with the corporate income tax on profits of less than $500,000, (3) relax the unwritten but enforced formula relating bank loans to firm equity that banks must follow in making loans to emerging companies, (4) expand the research and development tax credit to offset the implied tax bias in favor of larger companies involved in the current investment tax credit, and (5) launch a major federal effort to train workers for new industries.[36]

Former Governor of Florida Reuben Askew, on the other hand, flirts with centralized planning. He calls for "government policies, especially targeted tax policies, which give direction to the pattern of investment by making full use of market forces in a constructive way. We need a conscious, concerted, coordinated, and comprehensive policy for economic growth in the United States...."[37]

George Hatsopoulos, founding member of the American Business Conference, and Chairman, Thermo Electron Corporation, argues that the critical difference between economic growth in the U.S. and Japan is that in the U.S. the real rate of interest (the nominal market rate of interest minus the current inflation rate) is three times higher than it is in Japan. To narrow this, he suggests: (1) that the federal government revamp the tax code to allow cumulative preferred stock dividends to be treated the same for tax purposes as interest on debt so that equity capital flows into companies; (2) the federal government must restore the benign macroeconomic conditions of the 1960s, which included a 4 percent inflation rate and low equity risk.[38]

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36 Joel Kotkin and Dan Gevirtz, "Why Entrepreneurs Trust No Politician: Who Needs Friends Who Ruin Your Business While Aiding Corporate Dinosaurs?" Washington Post, January 16, 1983, pp. B1 and B2.

37 Reuben Askew, "The Democratic Alternative," speech prepared to be presented to the Democratic Business Council, French Lick, Indiana, April 24, 1982, p. 12.

38 The Economist, April 30, 1983, pp. 118 and 119.

A number of giant firms seem tempted by NIP. Edward Jefferson Chairman of E. I. DuPont de Nemours Company, recommends a "cherry-picking" (i.e., selective) approach to industrial policy, one providing special tax incentives, loans, and loan guarantees for research and development efforts.[39] Believing that the promise of high tech jobs will not replace the need for jobs in basic industries, Jefferson maintains that such subsidies will "shore up your industrial base and ease the unemployment problem at a time when the economy is in transition."[40] He adds, "The kind of government involvement I'm talking about should be highly selective, limited to asserting the national interest on behalf of our declining industries. That's no different from the concern we expressed for agriculture when it was in great difficulty."[41]

THE PREMISES OF NIP

Proposals for a national industrial policy rest on three common premises:

Premise One. The U.S. economy is in serious decline, which will remain unchecked unless America changes the way it does business.

Reich, for example, begins his book with a depressing and very questionable observation:

> Since the late 1960's America's economy has been slowly unraveling. The economic decline has been marked by growing unemployment, mounting business failures, and falling productivity. Since about the same time America's politics have been in chronic disarray. The phenomena are related. Economics and politics are threads in the same fabric....This link is perhaps stronger today than at any time in America's past because we are moving into an era in which economic progress depends to an unprecedented degree upon collaboration in our workplaces and consensus in our politics.[42]

Similarly, Bluestone and Harrison open their book by approving the Business Week conclusion that "the U.S. economy must undergo a fundamental change if it is to retain a measure of its economic viability, let alone leadership in the remaining 20 years of this century. The goal must be nothing less than the reindustrialization of America," a feat that would require a

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39 "How to Turn Recovery into Long-Term Prosperity," U.S. News and World Report, May 2, 1983, pp. 51-52.
40 Ibid. p. 52.
41 Ibid.
42 Reich, op. cit., p. 3.

"conscious effort to rebuild America's productive capacity."[43] Lester Thurow maintains that "Interest in industrial policy springs from a simple four letter word--fear. American industry is being beaten up by its international competition and business and labor are both afraid that American industry is going down for the count."[44]

The perceived causes of the decline vary. Gary Hart is convinced that government policy efforts have been misdirected because "we have remained mired in an irrelevant debate about the wrong issues" when the U.S. economy has been going through an industrial transformation, inspired to a major extent by the emergence of a global economy.[45] While agreeing with Hart and others that "false choices" have been addressed, Reich focuses on the extent to which American management has remained wedded to highly structured, mass production processes of the past.[46] Senator Hollings, meanwhile, blames Reaganomics, Carternomics, and the failure of presidents to "build and head a consensus of Americans for the common good."[47]

Bluestone, Harrison, Thurow, and Reich, among others, believe that the acceleration in technological change, the growing mobility of capital on a world scale, and the profit motive are key sources to what they insist is U.S. economic decline. Almost all NIP advocates believe that foreign imports, based in part on low wages and protectionist policies of other countries, have narrowed markets for many American goods. According to them, the collapse of the economy, especially the industrial Frostbelt, will continue unabated unless measures are taken to protect basic industries from foreign competition. Crystallizing the sentiments of many industry and political policy advocates, Wolfgang Hager, visiting professor at Georgetown University's School of Foreign Service writes:

> Without trade barriers rich countries are bound to suck in cheap imports from low-wage countries, destroying the domestic industries that used to make those products. There will never be enough 'high tech' jobs to employ those who lose more traditional jobs. Therefore, unrestricted trade would eventually destroy the economies of all high-wage, developed countries.[48]

Premise Two. Other countries have charted the industrial policy course that should be followed, with modifications, by the U.S.

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43 "The Reindustrialization of America," Business Week, June 30, 1980, special issue, p. 58, as quoted in Bluestone and Harrison, op. cit., p. 3

44 Thurow, testimony, p. 1.

45 Hart, op. cit., p. 1.

46 Reich, op. cit.

47 Hollings, op. cit., p. 2.

48 Wolfgang Hager, "Let Us Now Praise Trade Protectionism: It's Free Trade That Would Bring Disaster Today," Washington Post, May 15, 1983, p. B1.

Virtually all NIP backers cite Japan as a model. Hollings argues that 12 million Americans are out of work in part because of other countries that "are using government as an active partner in coordinating business and labor, agriculture and science to compete in the international marketplace."[49] Reich concludes, "The recent progress achieved by Japan and several other European countries, and America's relative decline, require no convoluted explanations....These countries are organized for economic adaptation....America is not."[50] Ford, Bluestone, and Harrison point out that European countries that have plant closing restrictions have grown more rapidly than the U.S. This, they say, proves that such restrictions have no negative effects on the economy. Thurow adds, "In Japan the banking system is heavily influenced by decisions of the government. MITI (Ministry of International Trade and Industry) tries to develop a consensus for its industrial policies, and 'administrative guidance' is a way of life."[51] Other advocates use the Chrysler bailout and American agriculture programs as quintessential examples of the kinds of industrial policies that can be pursued.[52] By saving Chrysler, proponents of industrial policy contend, many other firms, and even the City of Detroit, were probably saved from bankruptcy.[52]

Premise Three. Through the democratic process, a consensus on the industrial makeup of the country can be achieved.

To NIP's champions, the culprit today is, to a large extent, the profit motive. It mistakenly focuses firms' attention, it is argued, on their individual circumstances and diverts their concern for "a broader economic perspective"--meaning the community's interests. Profit-making firms, according to this perspective, systematically close plants and ignore the effects such shutdowns have on workers' investment in their jobs, the community's tax base, home prices, and the viability of other businesses in the community and country.

For reasons not always clear, NIP advocates possess a near religious faith in the sobering effects of public discussions on industrial issues, on the extent to which the ballot box rather than consumer and investment choices reveal community preferences, and the willingness of people to set aside private interests when asked to vote on policies reflecting the national interest. Reich writes that government should not necessarily be asked to become larger (although it is difficult to understand how that can be avoided), only "more open, more explicit, and more strategic."[53]

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49 Hollings, op. cit., p. 2.
50 Reich, op. cit., p. 17.
51 Thurow, testimony, p. 1.
52 Bluestone and Harrison, op. cit., pp. 74-75.
53 Reich, op. cit., p. 14.

THE EVIDENCE

Industrial policy proposals are founded on a variety of empirical claims:

* that the private sector of the economy is calcifying, due mainly to attitudes and inclinations of private profiteers;

* that the decline in many industries is due to an unprecedented rate of technological change;

* that without governmental direction the economy, especially the manufacturing sector, will continue its decline;

* that supply-side economics or, more generally, Reaganomics has failed, thus requiring new institutional relationships;

* that industrial policy programs in Japan and elsewhere have contributed significantly to the economic success of other countries;

* that low wages and foreign subsidies of industries explain the loss of markets for U.S. firms in basic industries;

* that industrial policy efforts of the past, specifically the Reconstruction Finance Corporation, the wide range of agricultural programs, and the Chrysler bailout, clearly indicate the potential success of an expanded industrial policy;

* that the government actually can "create" jobs by enacting additional money bills, designed to rebuild, for example, the nation's "infrastructure" or that an industrial policy can be instituted without increases in the government's budget and regulatory authority; and

* that expanded governmental efforts to enhance economic security can contribute to social justice and economic growth.

Discussions of industrial policies generally start with the reasonable observation that several important industries--steel, rubber, textiles, and automobiles, among others--have experienced serious difficulties in recent years. Virtually no one denies this. It is quite another matter, however, to maintain that these difficulties are symptoms of structural rigidities that can be remedied only by government initiatives. Such a conclusion dissolves when the premises upon which NIP rests are scrutinized. A growing body of literature suggests that these premises reflect half-truths and massively distorted interpretations of what is actually happening in the economy. Consider the following:

* Brookings Institution Senior Fellow Robert Crandall notes, in his review of Robert Reich's book, that the presumed demise of the manufacturing sector in the United States is based on the careful selection of the years used in his analysis:

> German and French readers of his [Reich's] book will be amazed to read of their government's success in industrial policy. Since 1975, industrial production has grown even more slowly in France and West Germany than in the United States.
>
> The industrial sector of the United States did not decline markedly from the mid-1960s to 1980. In fact, basic industry accounted for roughly 22 percent of our GNP in 1980 precisely the same share as in 1947. Our output per person remains above that of all but a few countries, such as Sweden and Switzerland (which have not exactly been refuges for the world's dispossessed over the 20th century). Reich's contrary conclusions are drawn from a period ending in 1979. Were he to extend his calculations to 1981, he would find that the United States has outperformed every major industrial country in the world except Japan since 1975.[54]

Few NIP proponents even note the upturn in U.S. manufacturing jobs, even in Frostbelt states, during the late 1970s, before the 1980-1983 recessionary period. With little attention to what is happening to jobs in other industries, proponents of new industrial policies, intent upon making their case as dramatic as possible, conclude that the relative growth in the service sector must mean that high-paying jobs of automobile and steel workers are rapidly being supplanted by low-paying jobs for janitors and fast food waiters. This simply is not the case.[55]

* National Journal columnist Robert Samuelson, as does Crandall, questions whether or not countries with industrial policies have actually, on average, done any better in terms of employment and economic growth over the last two decades than the United States. Several countries with industrial policies may well have performed much worse because of their industrial policies.[56]

Former Council of Economic Advisors Chairman Herbert Stein contends that Reich's conclusions concerning the economic decline of the U.S. relative to other countries are based on calculations Stein published in 1982. Observes Stein:

> I saw the evidence as saying that what has been happening to the U.S.--the slowdown in growth of output and productivity and the rise of unemployment--has been happening in other industrial countries as well....Reich

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54 Robert W. Crandall, "Can Industrial Policy Work?" Book World, May 22, 1983, p. 8.

55 This point is developed at length in Richard B. McKenzie, "National Industrial Policy: Six Major Myths," Policy Review (forthcoming).

56 Robert J. Samuelson, "The Policy Peddlers," Harper's, June 1983, p. 62.

uses the figures from my article to show that "other nations are gaining at a rapid clip." But the rate at which they are gaining on us is also declining rapidly. Take Japan. Between 1960 and 1979 Japanese real per capita output rose from 31.5% of ours to 70.2%. But the rate of gain on us fell sharply. If it continues to fall at the same pace, Japan's real per capita GNP would still be only about 74% of ours in 2083.[57]

* George Mason University economist Dwight Lee explains how Reich and others discount the lack of private investment as a source of deteriorating growth in the U.S. economy, thus giving credence to his claims that slowdown is due in substantial measure to the inability of U.S. businesses to adapt and to avoid totally government tax and regulatory policies.[58] Lee points out that Reich focuses on gross private investment, which as a percentage of GNP has changed little over the last two decades. However, net private investment (that is, gross investment minus replacement investment) as a percentage of GNP declined by over 40 percent during the same period, and much of this decline can be explained by past government policies.[59]

* David Henderson, senior economist at the Council for Economic Advisors; Philip Trezise, senior fellow at the Brookings Institution; and Katsuro Sakoh, director of International Economics at the Council for Competitive Economy, writing independently of one another, question the extent to which Japan's MITI has been responsible for Japan's economic success.[60] Most government investment funds go for urban and regional development, environmental protection, and infrastructure, causing economist Sakoh to conclude, "There is no evidence that manufacturing industries, in general or any particular manufacturing sector, have been targeted by the JDB [Japanese Development Bank]. In fact, the share of loans that manufacturing industries has received is negligible."[61] Much of Japan's public funds, moreover, were wasted on supporting "losers." Even more telling is that a major part of the Japanese government industrial policy efforts has subsidized coal mining,

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57 Herbert Stein, "Industrial Policy, a la Reich," Fortune, June 13, 1983, p. 202.

58 Dwight R. Lee, "Mr. Reich Shows Us the Way: A Review Article," Journal of Contemporary Studies (forthcoming).

59 See John W. Kendrick, "International Comparisons of Recent Productivity Trends," in William Fellner, ed., Essays in Contemporary Economic Problems (Washington: American Enterprise Institute, 1981), pp. 125-170.

60 David Henderson, "Behind the MITI Myth: The Real Japanese Miracle," Fortune (forthcoming). Philip H. Trezise, "Industrial Policy Is Not the Major Reason for Japan's Success," Brookings Review, Spring 1983, pp. 13-18. Katsuro Sakoh, "Japanese Industrial Policy," Backgrounder (Washington: The Heritage Foundation, 1983 forthcoming).

61 Sakoh, op. cit.

agriculture, and public railways, hardly examples of success. In fact, in the 1960s the Japanese government attempted to discourage the emergence of a competitive automobile industry in Japan on the grounds that it did not believe the industry would be a "winner" in international competition. Had Japan truly had an NIP, it probably would not be much of a threat to the U.S. today.

* Attorney James Hickle argues in Reason magazine that the Chrysler bailout has not saved jobs or even averted the bankruptcy of Chrysler. Chrysler has, for all practical purposes, gone bankrupt. Over 60,000 jobs at Chrysler have been eliminated since the bailout, and Chrysler has been allowed to discard $600 million of its debt at 30 cents on the dollar.[62]

* The arguments underpinning proposed restrictions on plant closings have been so flawed, from both empirical and conceptual perspectives, that more than one book was needed to balance the debate.[63]

Granted, the U.S. economy suffers from high unemployment and virtually zero productivity growth in recent years. Yet the rise in unemployment and the slowdown in productivity growth occurred simultaneously with dramatic increases in government intervention in the economy in the form of higher taxes and regulation. This should be a danger signal for those who now call on Washington to "guide" free enterprise or to "manage" capitalism. It would seem that remedies for cyclical and structural economic problems are not to be found in the institutional changes in private-public relationships envisioned in many venturesome programs offered by industrial policy advocates.

NIP's CONCEPTUAL PROBLEMS

Advocates of industrial policy romanticize the democracy of economics, maintaining that the results of a democratically determined industrial policy would be superior to the results of the democratic market system. They see the market system as founded on "greed and fear" rather than on "equity, security, and participation."[64] NIP advocates also tend to describe the nation as suffering from economic rigor mortis, brought on by entrenched monopolists who are protected from market competition by government franchises, regulations, tariffs, and subsidies. They tend to believe that the

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62 James Hickel, "Lemon Aid: Debunking the Case for the Chrysler Bailout," Reason March 1983, pp. 37-39.

63 Richard B. McKenzie, Restrictions on Business Mobility: A Study In Political Rhetoric and Economic Reality (Washington: American Enterprise Institute, 1978); Plant Closings: Public or Private Choices? (Washington: Cato Institute, 1982); and Fugitive Industries: The Economics and Politics of Plant Closings (San Francisco: Pacific Institute for Public Policy Research and Ballenger Press, Inc., 1983 forthcoming).

64 Reich, op. cit., p. 20.

political process that has served these special interests (also a major concern of conservative economists), when given more authority, somehow could be restricted from using this greater authority to provide even more special interest benefits. The dismal history of government aid to business teaches--or should teach--that government rarely accomplishes the noble goals that often originally prompt the policies.

The case for an industrial policy is founded in part on the belief that motives and results form a logical link: "good" motives (i.e., concern for the community, equity, and fairness) necessarily inspire "good" results, whereas "bad" motives (i.e., concern for profits and self-interest) often, if not always, give rise to "bad" results. Dismissed by NIP backers is the historically confirmed central point of the market system: that even in the worst of worlds, one driven exclusively by greed (and no real world society even approximates such a state), good results can be expected so long as property rights are respected and enforced. The drive for profits induces people to produce what others want at the lowest possible price, hence serving the community interest. Even if raw greed dominates private sector behavior--and no convincing case has been made that it does--such greed is contained and directed by competitive market forces toward a commonly shared goal: the production of goods and services that people, not government agencies, want. At the same time, a market system ensures individual freedom, for individual behavior remains largely undirected by government.

Cases made for an industrial policy are replete with horror stories of market system performance. These are contrasted with visions of how a collective of well-meaning people would handle economic tasks. The word "cooperation" is used loosely, as if the presumed lack of cooperation in the market system could be expunged simply with good intentions. Little is said of the waste and corruption in government and the extent to which government "industrial policy" in the past has been shaped by the political imbalance between, on the one hand, the private interests that seek protection, subsidies, and special privileges and, on the other, the general public that must pay the bills through price increases and taxes. Furthermore, virtually nothing is said about the resources tied up in the lobbying efforts of the 15,000 registered lobbyists in Washington and the thousands of other unofficial lobbyists who regularly ply the streets of Washington and the halls of Congress. NIP advocates do not explain how these private interests will be made less harmful. If greed is the root problem even in an unfettered market system, as NIP advocates argue, then this root will not vanish by assuming it away. Yet this precisely is what is done by NIP backers when they propose political institutions as market substitutes.

Industrial policy proponents seem to understand that the three arbitrary divisions of the electorate--workers, managers, and government officials--have competing interests: each wants a larger share of a growing economic pie. But they still perceive politics as a civilizing or harmonizing process, one in which such competing interests can be reconciled through reflective and sober discussions concerning their common interest, which is to increase the size of the economic pie and to modulate the "adversarial relationships" that exist among them in market settings. NIP proponents seem to believe that social welfare is an objective truth that can be deduced by well-meaning people through the voting process. The implicit assumption is that Americans operating in their political capacities are different from Americans operating in their market capacities. Given the extensive use of pork-barrel politics, their claims remain unconvincing. Furthermore, competitive markets are a system for picking "winners." What NIP advocates seem to be complaining about, at least to a degree, is that the market has not picked their chosen "winners," and there is no reason to believe they should be satisfied with the economic system until "their winners" are picked.

Adam Smith noted in his Theory of Moral Sentiments more than two hundred years ago that, "The man of system...seems to imagine that he can arrange the different members of a great society with as much ease as the hand arranges the pieces upon a chess board."[65] Smith would recognize today's industrial policy advocates who claim that they can rearrange the "smokestacks" of American industries across the industrial matrix of the country. All they need, they say, is to collect "good" information on what people can produce, feed this data into a "properly" constructed computer program, and then hold votes on what particular configuration of industries should be developed. NIP advocates ignore what Smith explained: that chess pieces have "no other principle of motion than that which the hand impresses upon them," whereas "in the great chess-board of human society, every single piece has a principle of motion of its own, altogether different from that which the legislature might choose to impress upon it."[66]

A critical problem with NIP is that information on what people want is not objective or determinable outside the market process. Centralized planning, whether called industrial policy or industrial democracy, is bound to fail to produce what people want because it cannot obtain the information needed to make the calculations without the markets it seeks to supplant.

Supply and demand identify the limits of what producers and consumers, respectively, are willing to do in markets. Suppliers will hardly reveal they are willing to accept as little as $50 for a widget if, in the absence of competition, they can get by with offering it for $100. Similarly, buyers will rarely voluntarily offer to pay $100 for the widget if they can get it for $50. Perhaps more than anything else, the competitive market is

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65 Adam Smith, The Theory of Moral Sentiments (Indianapolis: Liberty Press, 1976), pp. 380-381.

66 Ibid.

a process for revealing people's limits. Aside from suggesting that reputable people will discuss the issue, perhaps from the banks of the Potomac, and then vote on it, NIP advocates say little about how industrial policy engineers will secure the information they need to achieve goals of what must be construed as "plans." To simply talk of improved statistics, as is done in proposed legislation for an Economic Cooperation Council, is to beg the question; it assumes that the statistics gathered outside of markets overcome people's inclination to hide their true economic limits until forced to reveal them when striking a bargain. To assume that government officials can, with reasonable clarity, assess the wants and needs and calculate acceptable trade-offs of those living across this enormous nation is to assume cognitive skills so far undemonstrated by any group of men or cluster of computers. At the very least, industrial policy advocates should acknowledge that, as government intervention in the economy mounts--and industrial policy proposals are not modest on this count--the cognitive skills of government officials are bound to wane because prices will become progressively distorted and, accordingly, less useful in guiding policy. Industrial policy proposals will distort drastically the economic data that is needed to undertake the government guidance that is tendered.

NIP advocates will have limited information at their disposal and a limited capacity to handle it. How are they to pick and favor those industries destined to emerge in the intermediate future, much less the distant future? How are they to identify the industries that will "win" in the competitive struggle for resources and the pocketbooks of the consumers? What will happen is that the managers of NIP will only be able to subsidize "winners" after they have been picked by the market or, even worse, impose their own vision of what should "win." A national industrial policy thus discriminates against firms not "chosen" by the political process. Like any centralized planning process, NIP will limit the "plans" to the mental acuity of the planners and, in the process, limit economic growth.

If votes are to be taken on the allocation of capital, then NIP advocates must make the case not merely that the market has defects, but that industrial democracy and central planning are <u>less</u> defective. Do not proponents of industrial policies recognize by now that government imposes considerable costs and that greater foul-ups invariably follow extension of government authority? Do they not recognize that democracy, while important when other decision-making forms are unavailable, has its limits and limitations?

National industrial democracy will not alleviate but only exacerbate America's economic difficulties.

* The historical record reveals a strong coincidence between growth in government economic intervention and growing severity of inflation, unemployment, and lagging productivity improvements. While this statistical fact may prove little, it suggests strongly that new government efforts to manipulate the economy should be viewed with suspicion.

* Industrial democracy will introduce new layers of bureaucratic obstacles for firms seeking to adapt to economic changes.

* Decisions made on the allocation of capital will be subject to the influence of politically powerful interest groups. Established firms will tend to be treated favorably because they exist, have supporting votes from their laborers and suppliers, and have the profits available to sway the allocation decisions. Because many new companies have only limited constituencies, they will tend to bear the burden of the subsidies given to established firms. Many potentially profitable firms will be thwarted by the potentially heavy tax burden that will be imposed on them if or when they emerge.

Advocates of industrial policy earnestly believe that the burden of economic change should be shared across the country. When a plant shuts down, for instance, people other than the workers and community residents directly affected should pay part of the price of helping the plant reopen or of retaining the workers. Such forced subsidies encourage workers to raise their wages and induce firms to ignore production costs. After all, the costs of adjustment, if or when it comes, is partially imposed on others, many of whom have nothing to do with the shutdown. An industrial policy that "spreads the risk" encourages workers, especially the politically powerful, to raise their wages in the knowledge that if their firms fail, they will be helped by government through the problems of adjustment. In other words, it allows workers and firms to impose their production costs on others, just as polluters do. Any industrial program designed to "spread the risk" is a program that will encourage failure and waste of the nation's resources.

A central lesson of environmental economics is that a stream will be used and abused, i.e., polluted, when property rights to it are not defined and people are allowed to use the stream free of charge for waste disposal. In the vernacular of the environmental literature, the stream is a "common access resource." The cost of the waste is "externalized" on others--those who have to clean the water before it can be reused. Industrial policy proposals designed to "spread the risk and cost of social adjustment" make the national income stream a "common access resource," just like the water stream and effectively allow people in their private dealings to tap into other people's income by their own private decisions, which is hardly a democratic means of making decisions.

To insure over time that people do not "externalize" their production costs to the rest of the population, the controls envisioned under various industrial policy proposals will spawn in turn their own controls. This is why Nobel Laureate Economist Friedrich Hayek has called efforts toward even limited national planning as "The Road to Serfdom" (in a book by that title).[67]

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67 Friedrich Hayek, The Road to Serfdom (Chicago: University of Chicago Press, 1944).

The trip down this road already has begun. A major argument offered in support of industrial policy has been that, if the federal government does not engage in buyouts, bailouts, and selective nationalization, it will have to provide unemployment compensation and welfare benefits. Buyouts and bailouts are seen as cheaper public policy substitutes. Of course, such controls will foster other unforeseen consequences that must be controlled, if goals of the program are to be realized. Because costs can be externalized to the rest of the population when government buys or bails out firms, failure is encouraged. Additional controls then can be justified, on economic efficiency grounds, just as the initial forays into industrial control are justified on efficiency grounds.

CONCLUSION

Much that is vaunted as national industrial policy translates into more of the same sort of government policies that have given rise to America's current economic difficulties--more protection of domestic industries from foreign competition, more subsidies for failing businesses, more welfare benefits for workers whose wages have been raised far above the national average, more spending on social services, and more proposals for the federal government to centralize control of the economy. Several of the policies included in the spate of industrial policy reforms warrant further and serious consideration. Shifting current income taxation to consumption taxation, changing to a flatter tax-rate structure, treating preferred stock dividends as interest, reducing or eliminating the corporate income tax, and replacing current government employment retraining programs with a retraining voucher program--all merit study.

In so doing, however, Congress should be vigilant to policies that disproportionately and unknowingly benefit one set of industries at the expense of other sets, that choke off entrepreneurial efforts that may make U.S. industries more competitive in international markets, and that shorten the investment time horizons of businessmen. The industrial policy movement should be watched carefully because NIP advocates are seeking many profound changes in the structure of the U.S. economy. This alone requires that their conceptual framework be scrutinized for consistency and cogency. They must be confronted with their factual errors and internal contradictions. Robert Reich, for example, maintains that a major source of U.S. economic difficulties lies in the inability and/or unwillingness of U.S. businesses to adapt to new realities of a world economy. At the same time, he and others propose to democratize workplaces and the allocation of capital. Given the difficulties Congress has in voting on the budget--the inability of government bureaucracy to carry out its assigned tasks efficiently--the worry becomes that the proposed solution, industrial democracy, will do nothing but further reduce the capacity of U.S. industry to adapt and to meet demands of the changing world economy.

Reich, Bluestone, Harrison, Hart, Hollings, Mondale, Askew, and many others contend that the American economy is in the midst of an agonizing industrial transformation, spurred by an accelerating rate of technological change and capital mobility, that supersedes in impact on people's livelihoods, the Industrial Revolution. One must wonder how standards of logical consistency can be met when the solution, changeability, is also believed to be the problem. As Dwight Lee has observed, "[I]n dismissing the obvious [explanation of our economic difficulties, faulty government policies, that, if acknowledged, would have drawn into question his solution], Reich has substituted the absurd argument that the creativity behind paper entrepreneuralism is explained by the inability of American businessmen to adapt."[68] If businessmen are willing and quite capable of creating a "paper economy," why are they not equally able to adapt their production techniques? What seems to concern Reich and others is that businessmen have adapted to obvious incentives built in to the tax code and to a political system that allows government to cater to special interests, but not in ways that he and others would prefer. Industrial policy advocates appear to propose more of the same. At the very least, they fail to tell us how the political system can be enlarged and, at the same time, closed to further exploitation. A government with enlarged powers to allocate the nation's capital stock--with the selective capacity to aid some industries at the expense of others--would likely be viewed by entrepreneurs as a valuable resource (incorporating coercive powers) that can be enlisted through the political process in their pursuit of their narrow private interests.

Finally, advocates of industrial policy presume an immense stupidity on the part of profit maximizing entrepreneurs, workers, and consumers. Advocates contend that entrepreneurs are systematically willing to close profitable plants, grossly mistreat workers who are needed for production and the profits they seek and are unwilling to adapt when adaptation can translate into survival, if not substantial profits. Workers are unable or unwilling to make tolerably intelligent decisions regarding training and retraining, say NIP theorists, and consumers are poorly informed about many of the decisions they make daily. At the same time, advocates of a national industrial policy call for democratization of industrial decisions, which in the end must rely not on the advertised wisdom of the self-appointed industrial policy sages but on citizens who are presumed by advocates of industrial policies to be inept at handling their private affairs.

The rhetoric surrounding the debate over a national industrial policy is enticing. There is much talk of "cooperative efforts of labor, business, and government leaders to pick winners." The suggestion is that the markets, which political institutions organized under a national industrial policy would supplant, are devoid

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[68] Dwight R. Lee, op. cit., p. 13.

of cooperation and fail to pick winners. Nothing could be further from the truth. The purpose of markets is to do both: to further cooperation among people with compatible interests and to pick winners through competition. Given the insistence of industrial policy advocates that we need additional means of picking winners, we must be concerned that they possess a preconceived view of which firms or industries should be winners.

Under private market arrangements, these advocates have a grand opportunity for insuring that "their" chosen industries can be winners--by using their own resources to invest in their chosen companies or (if they happen to be workers or suppliers) by keeping their costs competitive, making the investment of others attractive. A national industrial policy of the kind advocated will tend to replace such voluntary arrangements, constrained by the sobering effects of competition, with political institutions that have at their disposal the coercive taxing and regulatory authority of government. In the industrial policy debate, there is no dispute over whether or not government policies affect industrial development in this country. The dispute is over whether or not industrial development and stability can be, and should be, enhanced through voluntary or coercive institutions.