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The MITIzation of America?

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From half a dozen Democratic study groups, caucuses, a think tank, and—more indirectly—from statements by several Democratic presidential hopefuls, a new theme is rising: industrial policy. It calls for the next Democratic administration, in consultation with business and labor, to formulate a set of industrial priorities. Chosen industries (high tech, especially computers, usually lead the list) are to be showered with public funds and benefits. Losing industries (autos and steel, for example) are to be "sunset" and their workers moved to other industries after "retraining." (Some suggest reconstructing the losing industries—with public funds and guidance—to become winners.) In these ways the government is to help American business adapt more rapidly to the changing technological environment and to the petitive world overseas. An often repeated line is, "We did Ja- and Germany a favor by bombing out their steel mills; now we must take out our own obsolescent ones."

The model that several proponents of industrial policy seek to emulate is Japan. The Ministry of International Trade and Industry (MITI) of Japan is credited with successfully managing Japan's economy as if it were one corporation. Hence references to "Japan, Inc.," and a standard question from the left: "If corporations have a planning committee, what's wrong with having one for the U.S.?" Indeed, the MITIzation of America is openly advocated.

One American version of MITI calls for the Department of Commerce to be transformed into a Department of Trade and Development, with a desk and a trilateral committee (made up of government, business, and labor) for each industry, from ball bearings to shoes. Each desk would analyze its industry and determine whether it had a promising future in terms of productivity, export potential, technological innovation, labor intensiveness, "added-value," and other such criteria. The industries ranked at the top would be granted whatever they need to thrive, based on trilateral consultations. ("Consensus" is another Japanese characteristic the new industrial world is to emulate.)

The people who most explicitly call for an industrial policy based on identification of winners and losers are the left-liberal Gar Alperowitz, co-director of the Center for Economic Alternatives, and Arny Packer, an Assistant Secretary of Labor in the Carter administration. Robert Reich, a former planning director of the Federal Trade Commission and currently a professor at Harvard's Kennedy School of Government, is widely considered the spokesman for Democratic industrial policy. A book he co-authored with Ira C. Magaziner, *Minding America's Business*, is often cited in discussions of industrial policy. Reich does not use the terms "winners" and "losers" and objects to being identified with the Alperowitz-Packer position. Nevertheless, he does call for identifying and assisting those industries with a "high added-value."

Reich never clearly defines what "high added-value" is. The problems in predicting which industries will have a high added-value in the future are similar, if not identical, to those of picking winners and losers. Indeed, in their book, Magaziner and Reich talk about "declining" and "growing" businesses as if there were labels pinned to their smokestacks or written on their laboratory flat-roofs. While it might be relatively easy to tell who is currently on the decline, this is by no means an easy business to predict. Losers turn into winners in a few short years, and vice versa, a catch Reich and others ignore.

As I see it, America cannot be MITI-ized, nor should it be. Before indicating why, I ought to make it clear that the Democratic Party has not adopted the idea as part of its platform or official policy, both because Democrats are still actively debating the idea and because the 1984 elections still seem far away. Now, before a commitment has been made, is the best time to raise questions about industrial policy. (Republican readers may feel that they could not care less—or would even find it welcome—if the Democrats lock into a wrong-headed strategy. But there is always a certain statistical probability that the Democrats will win, and the last thing the country needs is another round of experimentation with faulty economic theory.)

The cultural gap

Before evaluating what MITI has to offer America, we ought to ask how well it has done for Japan. In the mood of self-flagellation which prevailed on these shores in the late 1970s, Japan was credited with almost unbelievable prowess. For instance, Harvard sociologist Ezra Vogel found Japan first not only in economic achievement, but also in education, crime control, equality of income distribution, environmental protection, and health. The guiding spirit in this account—the consensus-builder, the administrator-coordinator, the promoter of productivity, export, research and development (R&D), good labor relations and wise investment decisions—is, you guessed it, MITI.

Others disagree. They point to MITI failures. For example, in 1955 MITI wanted Japanese auto makers to concentrate on a single car model, the "People's Car," and it took lobbying in the Japanese parliament to allow the auto makers to keep a more varied line, which has been part of their marketing success. Not long before, MITI officials had told Japanese auto makers not to waste resources trying to export—on the assumption that they could never penetrate foreign markets! In the 1960s, Honda and Mitsubishi succeeded by staying out of MITI-guided cartels and going it alone. More recently, Japan's MITI-ized steel mills have been operating for years at 70 percent of capacity.

But more to the point, whatever MITI does or does not do for Japan, it cannot be Xeroxed and shipped to the U.S. Major institutions do not travel well across international boundaries. It suffices to remember that our Constitution has been copied by some of the ublics of Latin America, which have frequently used it to im- the rule of generals, not to sustain democracy. Japan is a far more homogeneous society than the U.S., and its people have a strongly shared national mentality, fostered by a sense of vulnerability due to their isolation and the absence of most natural resources. They pull together much more readily than do the people of continent-sized, pluralistic America. Executives in Japan often

have secure, lifelong employment commitments. Many employees live on corporate campuses and many labor unions are, in effect, company-controlled. To put it succinctly, there probably is not a major industrial country from which the U.S. can copy *less* than from Japan.

The essential feature of MITIzation is that it presupposes an intensive and extensive role for government in planning and managing the economy. Nothing could be further from the political philosophy to which most Americans subscribe. The American antipathy for government, and the corresponding belief in individualism, competition, and the marketplace, go back to the days of the founding. In recent years, in a reaction to the liberal decades of the New Frontier and the Great Society, these beliefs have been strongly reaffirmed. After all, not just Reagan but Carter, too, rode on an anti-big-government wave. If Reaganomics fails, some backlash may develop, which could carry us either to *greater* opposition to government, or to some new willingness to draw on it for economic revitalization. But I cannot imagine that by 1984 or 1988 the public will embrace a MITI-ized economy. To advocate it is, at least politically, a losing proposition.

The political gap

Nor is a MITI compatible with the way America is governed. In Congress we find a strong expression of local interests and, increasingly, of other special interests. We may leave to another occasion the question whether this makes for a wholesome, pluralistic, representative system or for a semi-corrupt PACed Congress. The fact is that a national economic plan cannot be formed and implemented under our political institutions, if it can be done at all. When our social engineers wanted to test the Model Cities plan in six sites during the 1960s, members of Congress, long before the data were in, demanded the program for "their" cities, extending it to 75, soon 150, cities. The Economic Development Administration was to allot funds for selected economically depressed counties; soon, under Congressional pressure, 84.5 percent of *all* U.S. counties qualified, turning the program into an open pork barrel and completely defeating its purpose. Essentially the same thing happened to Trade Adjustment Assistance and to the tax code, the latter becoming so riddled with special favors that some have proposed turning to a flat rate tax.

Moreover, the "losing" industries are usually the oldest and best-established ones, and therefore have the most political influence, while newer, more innovative industries often have relatively little. Bio-engineering is lost among the farm, bank, labor, real estate, steel, and auto lobbies. Thus the American political process tends to channel resources to obsolescent industries, to the relative neglect of the new, with-it ones. President Carter's short-lived 1980 economic revitalization drive started with the auto and steel industries—both obsolescent and in need of being scaled back—not because his staff believed they were the engines of America's future, but because their labor unions were flirting with the idea of endorsing Senator Kennedy.

It has been suggested that the American MITI, like the Federal Reserve, would be an independent authority, insulated from Congress. But would Congress agree to keep its hands off a comprehensive national planning and management agency? And could the economy run if we had *two* economic policy-making institutions independent from one another—and from general national policy making? (Some feel one is too many.) Sometimes the bark of the proponents of industrial policy is worse than their bite. Reich calls for "government management" of capital markets, which is enough to drive most American businessmen, investors, and voters up the wall (and over it, to relocate overseas). Actually, he does not quite mean a government-run investment decision-making apparatus for the American economy, only introduction of "public investment criteria" into allocations of loan guarantees, insurance subsidies, and tax and credit subsidies.

The knowledge gap

Other advocates of industrial policy, such as Lester Thurow and Felix Rohatyn, are much more moderate. They favor directing *some* capital to where it is needed—perhaps through a Reconstruction Finance Corporation (RFC) on the order of $50 billion a year—which is a long way from "managing the American capital market." Indeed, the size of the intervention is as important as its tightness of grip. A small RFC might be wasteful, a nuisance, a symbol of relying on government rather than the market; a major one would constitute an attempt to plan the economy through a central financial authority. Gar Alperowitz, for instance, recently called for "coordinated overall planning." Recognizing that this notion is not very popular, he has returned to an old-left chestnut, expecting the forthcoming crisis to raise people's "consciousness." He writes, "Probably the new approach will have to linger on the sidelines . . . until the economic disarray explodes into crisis and the people demand that something be done."

Last but not least, the identification of "winners" and "losers," the cornerstone of industrial policy, is a near-impossible task. To identify a winning industry requires predicting the future, determining what product line will succeed, taking into account future technological developments, changes in the general level of economic activity, actions by our competitors, and so on. The fact is that American industries that in the past were considered sure losers—textiles, shoes—have become winners, *without* industrial policy, and an industry that until recently seemed an American winner—airplane manufacturing—may turn sour (and then again may not). It is hard to foretell. I find it very revealing when people who put their faith in forecasting do not engage in studies of the validity of past forecasts. (Do not trust a broker who will not provide—or keep—a performance record.)

At one point Magaziner and Reich announce that, "the governments must be capable of distinguishing between major structural declines and temporary problems that can be overcome with adequate funding." Maybe they must, maybe they do not—but *can* they? So far as one can tell from historical and anecdotal information, and as the preceding examples illustrate, successful long-run identification of winners or losers is beyond our current intellectual and technical capacity.

Learning from the American experience

All this does not mean that the only alternative is to sit back and await the results of the vicissitudes of the marketplace. As long as there is a government (even for defense only) there will be a tax system and public policy decisions as to how to distribute its burdens, not only among various social groups, but between consumption and investment and production. (For instance, shall there be a tax on corporations or only on individuals? On capital gains or only on earned income?) Similarly, monetary policy and the level of government activities, especially deficits, affect the availability of credit to the private sector. In effect, both the tax and the credit systems are used daily by the government—including the Reagan administration—to transmit national priorities to the economy.

These sorts of signals differ from those sent by MITI in that they are economic incentives, not administrative decrees, regulations, or public financing. Moreover, these incentives are focused on wide sectors of the economy, not specific industries. For example, to favor investment in capital goods over collectibles and residential real estate (as most items of the 1981 Economic Recovery Act do) is not to favor tin over silver, or slurry pipelines over railroads. Because they are broad, these incentives are much less subject to political pork-barreling; most political corruption enters when economic incentives are tied to a narrow, specific constituency. In addition, they can work well even if we cannot forecast precisely. To favor R&D in general, for instance, does not require forecasting *which* specific R&D projects, or even which line of investigation, will "win," or which new technology will pay off.

A major study of "industrial innovation policy" published in *Science* illustrates the point.[1] The authors identified three ways the U.S. government historically has supported R&D. Before one rushes to condemn all government support for R&D it should be noted that a good part of this support is directly related to U.S. national security. And all but the most extreme free market purists recognize the need for the government to support some shared goods which have no profit potential, among which basic scientific research ranks second only to defense. Support, of course, does not mean government administration, production, or control. Support of R&D currently takes the form of appropriation of needed funds. The question under study is what kind of government guidance—if any—should be built into the ways the funds are allotted.

The study found two ways that worked well and one that clearly does not. Support for items in which the government has a "strong and direct procurement interest" (e.g., missiles) works well, as does support for "generic" research *between* basic and applied (e.g., accelerating the transition of basic work in chemistry and biology to applied R&D carried out by the private sector). What "unequivocally" did *not* work, say the researchers, is the government's trying to "pick winners." In the SST project and Operation Breakthrough (a HUD housing development), the government "did not attempt to create a framework in which scientific and user interests could guide allocation; rather than federal agencies attempting to insert themselves directly into the business of developing particular technologies for a commercial market in which they

[1] Richard R. Nelson and Richard N. Langlois, "Industrial Innovation Policy: Lessons from American History," *Science* (February 18, 1983): 814-818.

had little or no procurement interest." This "targeted" form of support for R&D failed, while the indirect—or *semi*-targeted—approach worked quite effectively.

All specific economic decisions can be left to the private marketplace within a framework that encourages what I have called reindustrialization—that is, shoring up the infrastructure and capital goods sectors, the sectors favored by the first industrialization of America. Others may call such an approach "industrial policy II" or "MITI-minus." By whatever name, such an economic policy may foster American economic reconstruction, as long as it does not look like or attempt to work like MITI in Japan. Incentives and broad-gauged signaling of priorities might help; national planning and managing the economy will not.