Michigan Journal of International Law

Volume 6 | Issue 1

1984

# Building the Case for Industrial Strategy

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The argument for an industrial strategy begins with the failures of present policies. The indictment is not concerned with the relative simplicity or elegance of competing economic theories but with actual results in the world marketplace.

The case for an industrial strategy is not primarily about compassion, or about full employment, or even about economic growth. While we desperately need a compassionate economic policy, full employment, and sustained economic growth, these are goals. The industrial policy debate is not a debate about goals, but means. The argument rests on the premise that the old means must be changed because the world marketplace has changed fundamentally during the last three decades. Industrial strategy concerns how the United States (U.S.) should adjust to the new world market.

America also needs sound and consistent macroeconomic policies, a tax policy that is not at war with fiscal policy, and a fiscal policy that allows for a more expansive monetary policy. Yet macroeconomic policies alone will not protect America's position in a world marketplace where the primary issue is the relative competitiveness of individual industries.

## I. The U.S. Position in the World Market

Following World War II, the international dominance of the United States allowed us to avoid, for a time, an explicit national strategy to sustain our industrial lead. As Bluestone and Harrison have noted, "[t]he United States emerged from the Second World War with the only major functioning army, with more than half of all the usable productive capacity in the world, and as the banker and creditor to both former allies and former enemies".[1]

Today, that era is over. In the past twenty years, the world economy has become more integrated and competitive. As other nations have surged forward in the new economic order, the influence of the United States has ebbed.

Indicators of this transformation are striking. In the early 1960s, a mere 25

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1. B. Bluestone & B. Harrison, The Deindustrialization of America: Plant Closings, Community Abandonment, and the Dismantling of Basic Industry 112 (1982).

percent of all goods produced in this country faced international competition for U.S. domestic markets. Today, the figure is 75 percent.[2] The problem is not limited to the industrial heartland or even to the so-called "basic" industries. In almost every capital goods and high technology industry, the United States' share of the world market dropped in the 1970s.

More is at stake in this decline than America's world influence. As a recent report by a House Banking Subcommittee concluded, "...ten years ago, we defined the 'structural unemployment' rate at three or four percent. Today, the Council of Economic Advisers estimates that rate to be about seven percent, that is, over seven million Americans who would not be able to find jobs, even after a full economic recovery."[3] This structural problem is aggravating the episodic swings of the business cycle. As a result, recessions are becoming deeper and our recoveries more precarious.

It would be easy to blame our problems on one President or one political party, but the twenty year pattern bridges too many administrations. It also bridges too many different macroeconomic policies to sustain the thesis that one more attempt at fine tuning will solve our problems.

In the future, global economic leadership and our domestic prosperity will depend on America's ability to adapt to the changing conditions of the world marketplace. If the trends and policies of the past continue, the U.S. world role will be diminished and our economic prospects will decline. The argument for industrial strategy is, above all, an argument about how we can meet this urgent national challenge. The United States must recognize that it cannot sustain prosperity through economic isolationism or through its previous pattern of economic dominance. Our nation must address the changing international context, and we must learn from other nations which have, for decades, been more self-conscious in their efforts to achieve economic growth and international advantage.

## II. The Japanese Model

Japan is the starting point for many arguments about industrial policy. Due to its impressive growth rate, its favorable balance of trade with the United States, and the penetration of its products into the American domestic market over the last two decades, Japan's "success" has stimulated the industrial strategy debate in this country.

As has been carefully catalogued by the General Accounting Office, the Japanese Diet has adopted measures for both emerging and mature industries. Two "Extraordinary Measures," for example, helped guide promotion of the electronic, information and machinery industries. The first was effective as early as 1971. Mature industries have received similar attention. In addition to several generations of Textile Acts, in 1978 the Diet passed the "Structurally Depressed Industries Law." These measures are matched by several laws specifically focused on the needs of displaced workers.[4]

2. House Comm. on Banking, Finance, and Urban Affairs, 98th Cong., 1st Sess., Forging an Industrial Competitiveness Strategy 5 (Comm. Print 1983).

3. *Id.* at 1.

Industries Law." These measures are matched by several laws specifically focused on the needs of displaced workers.[4]

At the center of the Japanese industrial strategy process lies the Ministry of International Trade and Industry (MITI). MITI functions through national and regional bureaus that develop and coordinate policies both to help specific industries and to address problems that cut across all industries. In essence, MITI institutionalizes a process, not a plan. Its most basic role is to facilitate consensus. This consultative process is reflected in the "Industrial Structure Council," an advisory group first created in 1964. Representatives of management, labor, academia, and consumers sit on the Council. Once each decade, the Council issues a major report, usually referred to as a "Vision Statement." The Vision Statements seek to articulate a broadly shared consensus on Japan's fundamental economic strategy. Because of the Council's wide representation, the Vision Statements are the product of careful negotiation which balances the economy's potentially competing interests.

The Council's most recent report, *The Vision of MITI Policies in the 1980s,* reveals a nation reaching for a strategic consensus responsive to new problems. Having achieved rapid industrial development, manufacturing growth is not directly mentioned at all in the three proposed national goals. Instead, economic growth is sought through a policy promoting Third World consumption and moving Japan aggressively forward as the world's most technologically intensive producer.[5]

It is an extraordinary document which expresses the potential power of a cooperative strategy. It marries a clear vision of the world marketplace with an equally clear vision of Japan's future role in that market. The document gains its power, however, not merely from the consensus it reflects, but from the ease with which the Japanese draft their government to the service of the new vision. Given the consultative process, government action in support of industrial strategies in Japan cannot easily be derided as government intervention. More accurately, the government sits, with its own resources, as one party at the table. As required by the evolving consensus, those resources, like the resources of the other parties, can be used on behalf of any strategic plan.

For example, the development of an industrial robot industry required a large domestic market. That, in turn, required that small and medium size firms become potential buyers. Yet it is difficult for smaller firms to finance large, long-term loans like those required for industrial robots. Enter the Japan Development Bank. The Bank lent money to help create a new financing institution which in turn made loans at rates below market to small and medium size firms to help purchase industrial robots. Today, Japan has one-half of the world's installed industrial robots.[6] This increases the productivity of other Japanese industries,

4. GEN. ACCOUNTING OFFICE, GAO/ID-82-32, INDUSTRIAL POLICY: JAPAN'S FLEXIBLE APPROACH (1982).

5. LOOK JAPAN, May 10, 1980, at 10 (reprinting a summary of The Vision of MITI Policies in the 1980s, Recommendation of the Industrial Structure Council (Mar. 1980)).

6. The General Accounting Office did a special study of the Japanese robot industry as part of its review of Japanese industrial strategy. *See* GEN. ACCOUNTING OFFICE GAO/ID-83-11, *Japan Gears up for Robots*, in INDUSTRIAL POLICY: CASE STUDIES IN THE JAPANESE EXPERIENCE 19-31 (1982).

helping Japan become the world's most technologically intensive manufacturer. It also gives Japan a significant edge in the potentially enormous industrial robot market. Japanese firms are now exploring plans for export promotion.

The Japan Development Bank did not pick one firm over another or one robotic design over another. Instead, it expanded the available pool of buyers by easing financing, and then let new purchasers make their own decisions. This is market intervention of a special sort. It is intervention to expand the market.

The United States need not borrow Japan's specific institutional arrangements. We need to look beyond the details to the two notions that animate the system: the conviction that government has a positive role to play in economic development and the firm belief in cooperative decision making. These are values, not institutions, but they are the values that underlie and make possible an industrial strategy that would meet America's needs.

## III. The Unique American Setting

Pointing to America's decline, some industrial strategists assume that current U.S. economic problems alone justify an industrial policy. Yet that argument skips an important point. Proving the failure of our present policies does not, by itself, prove that an industrial strategy will be effective. International comparisons are sometimes used to fill the gap in the argument. Proponents contend that the value of industrial strategy is proven by its success elsewhere. Yet those comparisons provide only half an argument. While comparative analysis is essential, it is also difficult because of the United States' distinct political and cultural traditions. The question of the viability of foreign answers to the American setting remains.

Japan's success cannot be explained without acknowledging distinct Japanese traditions. As Magaziner and Hout emphasize in their seminal book on Japan's industrial strategy, a "clear sense of common purpose" pervades Japanese society. While conflicts of interest have always existed between the government and business leaders, as well as between the competing business leaders themselves, there is a "commonly accepted and extremely well-developed process to resolve conflict."[7]

The Japanese people's particular cultural view of the state helps to ease the direct role of the Japanese government in resolving conflict and reaching consensus. K. Haitani illustrates the importance of Japanese cultural traditions:

> In the traditional view, the whole nation is a family; what the house is to a biological family, the state is to the national family. The state is not merely a part of the system, but the very framework of it ....To the Japanese way of thinking, then, the state does not "interfere" with the affairs of private business. It merely manages itself, exercising authority and control over its constituencies.[8]

These cultural traditions seem foreign to America. From the time of the nation's founding, American political ideology has emphasized the inevitability

7. Magaziner & Hout, *Japanese Industrial Policy*, 15 Pol'y Int'l Aff. 39 (1980).
8. *Id.* at 37.

of conflict rather than the possibilities for consensus. The public interest is best guarded, it has been assumed, by encouraging the free competition of a multiplicity of individual and group interests.

Federalist No. 51 stated this thesis when describing how a federal republic can protect its citizens from injustice:

> Whilst all authority in [a republic] will be derived from and dependent on the society, the society itself will be broken into so many parts, interests and classes of citizens, that the rights of individuals will be in little danger from interested combinations of the majority.[9]

The U.S. Government was structured to incorporate this kind of competition of interests through the establishment of three separate branches. It was believed that the checks and balances inherent in the separation of powers would prevent any branch from attaining overwhelming power and would, in turn, prevent government itself from achieving the kind of singlemindedness that would allow it to trample on any one group in the name of any other.

Over time, this political ideology became wedded to an economic view which extolled the virtues of the free market. Economic competition was viewed as the preeminent forum for the competition among interests that protected the public welfare. The market became the guardian of both individual freedom and the general prosperity.

Today, at times, our political debate seems framed solely by the belief that America's economic growth has been wrought by the free market and that government action is "intervention" and almost definitionally wrong. At best, government is defended as the well-meaning purveyor of the welfare state. At worst, it is criticized as a burdensome bureaucracy threatening to stifle business. Critics of industrial strategy point to this ideological tradition as a fatal obstacle to the development of an explicit industrial strategy in this country. Even proponents concede that the real barriers to adopting an American industrial strategy are political, not economic. The most difficult issue is not whether an industrial strategy is economically necessary but whether it is politically feasible.

Yet the currently visible attack on government is not the real heir to the traditional American distrust of concentrating power in any one interest group. A closer examination of American history reveals another, even more durable, ideological tradition. Americans have not always viewed the government's economic role with suspicion. Indeed, it was not until the end of the nineteenth century that a significant sector of American society vigorously championed the doctrine of laissez-faire.[10] Alexander Hamilton's "Report on Manufacturers," from the early years of the republic, was among the first to argue that the government should play an active role in the promotion of promising sectors of

9. The Federalist No. 51, at 351 (A. Hamilton) (J. Cooke ed. 1961).

10. The following discussion owes much to Andrew Shonfield's authoritative comparison of economic policy and institutions in Western Europe and the United States. *See* A. SHONFIELD, MODERN CAPITALISM (1965) (especially ch. 8). Also of interest are Chandler, *Government Versus Business: An American Phenomenon*, in BUSINESS AND PUBLIC POLICY (J.T. Dunlop ed. 1980), and Vogel, *Why Businessmen Distrust Their State: The Political Consciousness of American Corporate Executives*, 8 BRIT. J. POL. SCI. 45 (1978).

the economy. Throughout the first half of the nineteenth century, the entrepreneurial role of government, either independently or in tandem with private enterprise, was widely accepted.

After the Civil War, the rise of vast industrial corporations fundamentally altered the character of the nation's economic development. These corporations no longer faced the kinds of capital shortages that prompted government action in earlier years. While the government subsidized railroad construction, enacted tariffs, and provided other vital support for industry, the new corporate leaders no longer viewed the government as a real, in other words, financial, partner.

When, near the turn of the century, government leadership was again sought in economic affairs, it was to restrain the abuses of corporate giants. Riding a wave of anti-monopolistic sentiment, government was championed as the trustbuster which would preserve the competitive world. Trustbusting reflected the American concern with concentrating power in the hands of any limited interest, but the enemy was not the government. Indeed, it was government that promoted the competition among interests. For the trustbusters, the basic problem was how to put government to the service of the economic need of the moment. Yet the result was an unusually clear vision of the relationship between government and business. Government stood against and separate from business as the regulator of the public interest. From this period, more than any other, we derived the view of government and business as adversaries.

This regulatory view carries important implications. From the business perspective, the least government is the best government. For the new government regulators, the immediate problem is no longer how to help the differing business interests in the service of national growth, but how to ensure compliance from potentially hostile industries.

The Great Depression shook the nation's faith in continued economic growth. Despite the attraction of the rising ideology of limited government action in the economy, the government was given rein to engage in bold experimentation to revive a shattered economy. New government programs underpinned a new era of economic prosperity.

In the period since World War II, our tremendous productivity in agriculture was stimulated, in large part, by government policies. These included support for the price of agricultural commodities, government irrigation projects to open up otherwise untillable lands, agricultural research, and efforts to assist farmers in adopting modern production techniques. Our massive commitment to an interstate highway system, justified as a measure to improve our national defense, not only facilitated commerce but was, in effect, a subsidy to the automobile industry at the expense of the railroad industry. Our commitment to place a man on the moon stimulated aerospace, electronics, computers and other industries.[11]

In contrast to the rigidities of free market theories, each of these programs was an experiment. Each was extemporized to meet a pressing need, yet involved a conscious, pragmatic policy decision with significant microeconomic effects. The future of whole industries was shaped by the gambles of these programs. In

11. T. Magaziner & R. Reich, Minding America's Business 223 (1982).

no case could the free market alone have provided the necessary resources, expertise and incentives.

America has been a country of two minds. Its deep distrust of concentrated power has been quoted in the name of limited government while at the same time the nation assumes that its government should do what is necessary to ensure economic growth. A tendency to debate economic policy in highly ideological terms derived from free market theories has coexisted with a pragmatism devoid of ideologies or any rigid theoretical frameworks. Compared to the ideological tradition that argues against government action, the pragmatic tradition is relatively mute precisely because it is suspicious of theories and committed to experimentation. Yet the pragmatic tradition, whatever its intellectual handicaps, is the dominant tradition in American government, as reflected in the persistent willingness to mobilize the government to spur prosperity.

The success of Japan counsels Americans to listen to their pragmatic roots and to respond creatively to the competitive problems created by the new world marketplace. American history suggests that the American people will take the risk. Industrial strategy is today's experiment, the heir to the pragmatic tradition in American government.

## IV. Building a Consensus for an Industrial Strategy

An industrial strategy is built through consensus. "Consensus," however, is merely the latest buzzword designed to hide a hard process. An industrial strategy is about sacrifice: wage concessions, dividends foregone, spent tax dollars. Consensus occurs when competing interest groups agree on a formula for shared sacrifice in pursuit of common goals. Yet America's government institutions are designed to protect each group against sacrifice. Reflecting our distrust of concentrated power, American politics is characterized by a fragmentation of government power and a proliferation of special interest groups each free to fight for itself against all others. In our nation, competitive, even adversarial systems pit labor against management, business against government. When government acts, it seldom plays the neutral broker arbitrating between special interests. More often, it merely commits its resources to the needs of each interest in turn.

American history suggests that the present ideological debate over industrial strategy is ultimately irrelevant. Americans have been willing to draft their government to meet their needs despite almost any theoretical problem. Yet the likelihood of government action does not prove the action will be effective. The final argument against industrial strategy is that it will inevitably fail given the structure of America's government institutions.

Magaziner and Hout emphasize the "competitive realism and economic logic" that has allowed Japan to consciously seek advantage in the international market.[12] But if America's political institutions continue to subvert shared sacrifice, then our country will fail in an effort to define problems realistically and to accept economic facts of life. In Congress, the tendency toward "log-rolling,"

12. Magaziner & Hout, *supra* note 7, at 2.

abetting parochial concerns through pork barrel politics, combined with the difficulty of coordinating the decisions of a wide range of committees with competing interests work against the development of an explicit industrial strategy.

The Executive Branch also lacks the necessary institutional arrangements to coordinate policies.[13] The Council of Economic Advisers (CEA) was created in 1947 to improve the quality of economic advice the President receives, but, since that time, even macroeconomic decision making has become difficult to coordinate.

The Federal Reserve retains autonomous control over monetary decisions, while the Secretary of the Treasury, Chairman of the CEA, and Director of the Office of Management and Budget all compete in setting tax and budget policy. Meanwhile, microeconomic decisions have become increasingly important and involve almost every agency in the federal government. Fragmentation in the Executive Branch reinforces fragmentation in Congress by nearly ensuring that each competing Congressional faction and organized special interest will have its own Executive Branch supporter.

Critics of industrial policy argue that special interest politics in particular presents an insurmountable obstacle to the development of a consensus-based industrial strategy. Some argue that any effort to make industrial policy in a more explicit fashion will cause an even greater mobilization of special interests, and exacerbate the tendency to substitute political for economic criteria in decision making.[14]

Other critics argue that the current fragmented and decentralized system provides essential protection for economic rights. Fragmentation may be inefficient, the argument goes, but it is not as dangerous as the possibility that corporate-government collusion at the public expense or, even worse, joint corporate and union collusion, could arise from cooperative modes of economic decision making.[15]

The first criticism ignores the fact that advocates organize their power in response to the structure of political institutions. A fragmented, decentralized system creates huge incentives to organize along narrow lines. That allows groups to focus on just those points in the system important to each narrowly drawn interest.

As Shonfield observed nearly two decades ago, "it is the competitive theory of administration inside the government, rather than any ungovernable competitiveness outside it, which makes the American case special."[16] Rather than bemoaning special interests as inevitable, it is possible to organize government in forms less likely to require special interest advocacy.

The second criticism ignores the fact that the current pattern of special interest advocacy has done little to restrain the power of well funded special interest

13. *See* Porter, *The President and Economic Policy*, in THE ILLUSION OF PRESIDENTIAL GOVERNMENT 203-07 (H. Heclo & L. Salaman ed. 1981).

14. *See, e.g.*, Schultze, *Industrial Policy: A Dissent*, BROOKINGS REV., Fall 1983, at 3; *see also* Kantrow, *The Political Realities of Industrial Policy*, HARV. BUS. REV. Sept.–Oct. 1983, at 83.

15. In addition to classic conservative critiques of government intervention, see the progressive critique of Lekachman, *The Limitations of Industrial Policy*, NEW LEADER, Sept. 19, 1983, at 5.

16. *See* A. SHONFIELD, *supra* note 10, at 353.

groups, including corporations and unions. Indeed, when decisions about the expenditures of public funds are fragmented and decentralized, they are more likely to be dominated by special interests. The federal government has become a vast and extremely crowded battlefield. With dozens of subcommittees, agencies and White House offices to choose among, a well-funded interest able to focus on a special need with persistence will sooner or later find at least one path to its goal. With so many battles going on at once, the chance that any single skirmish will be discovered is small. Its chance of being publicly reported is even smaller and the profusion of national media coverage has reduced most reporting to one day stories with little or no public impact.

Our government institutions do frustrate some action, but it is not the action of special interests that is particularly vulnerable. It is action in the general interest, broad in its implications and requiring the coordination of our dispersed government, that has been made almost impossible.

Our nation's long list of industrial policies reflects the problems in our existing political arrangements. Fear of government involvement has not prevented enactment of such policies. Instead, it has created an environment where industrial policies emerge from the pattern of special interest politics.

The most important set of these "back door" industrial policies lies in the U.S. tax code. Corporations receive extensive aid through tax breaks, technically called "tax expenditures." In fiscal year 1984, corporate tax breaks will cost $70 billion. Yet decisions concerning who shall benefit under the tax code are not even subject to the regular budget process that sets priorities in other spending areas. Today, the energy industry, the commercial banking industry, and the paper and wood industry—to pick just three winners—pay essentially no taxes. The auto and pharmaceutical industries—to pick two losers—face a tax rate near the legal limit. Is this rational? More to the point, against what standards of the national interest have such policies been judged?

No industry opposes a gift from its government. Given the logic of special interest politics, no industry opposes a gift to another industry unless the gift would create competition. The essence of special interest politics is to satisfy each interest in turn while postponing competition. The result is not less government involvement, but rather policies that are ad hoc, inefficient and undisciplined by any overriding public purpose.

America is historically suspicious of the power of special interests and has sought to write that distrust into its governmental institutions. In fact, in the name of fighting special interests, our existing institutions create an environment where the special interests operate at a distinct advantage.

Proponents of industrial strategy are not necessarily arguing for a greater government role, or a greater corporate role, or a greater union role. Rather, they are arguing for a forum that would allow economic decisions to be evaluated against a consensually derived criteria of what would most improve the competitive capacity of the nation as a whole.

## V. Conclusion

As the mute tradition in American politics, the pragmatic tradition operates at a disadvantage against free market theories. Industrial strategy, proposing to meet that disadvantage, offers a theory of the government's role in assisting economic growth. That theory has powerful implications. It would subject the long list of government favors to industry to an exacting standard. Some would survive the test and others would not.

Free market advocates say that any review process will produce a list of winners and losers, and so it will, but that is hardly a new problem. The existing system produces winners and losers as well. Industrial strategy is only controversial because some of today's winners might become tomorrow's losers.

Industrial strategists have acted as if their principal problem was their support for government action in the face of a free market current in contemporary American politics. The real problem, however, is not that industrial strategy proposes government help to industry but that industrial strategy conditions government help on a consensus for progress.

The search for consensus does not presume good intentions. It tests the parties' willingness to compromise by making the application for aid voluntary and requiring that each request be jointly reviewed by each constituency: labor, management, government, and consumer. If there is not consensus, there will be no action. No one is hurt by failure. But if there is consensus then industrial strategists argue that the government should not only be able to convene the discussion but should also be able to back its conclusions. The government should be free today to experiment in the search for a better future just as it has, so successfully, in the past.

The United States need not mimic the Japanese institutional arrangements—our traditions are hardly so poor as to require us to imitate others. What is needed is merely to learn new ways to work together for the common good. What is needed is merely to remember that we should not be embarrassed by government action, but should be proud that acting together as one nation we can address our needs.