The First and Second Reich: The Taming of an Industrial-Policy Advocate

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Introduction

Retired Harvard University economist John Kenneth Galbraith developed an illustrious career arguing that the public sector should be expanded and that the private sector—especially dominant large firms that make up the "new industrial state"—should be more tightly controlled by government (Galbraith 1967). With wit and a writing style that remains the envy of novelists, Galbraith has argued for four decades that an "affluent [capitalistic] society" would be beset with problems of a dominant business sector and upper income class, an anemic public infrastructure, and an impoverished underclass unless a caring and enlightened electorate used the power of their votes to do what was right (Galbraith 1958). Doing what was right generally meant making government a "countervailing power," or an offsetting social force, to the large and growing multinational corporations (Galbraith 1952). It meant fine tuning the economy with macroeconomic fiscal and monetary controls, even national planning that would supplant corporate planning; increasing tax rates on the rich; and expanding government expenditures on a variety of social programs.

By the early 1970s, much of Galbraith's social agenda had been tried.[1] However, by the late 1970s and early 1980s, much of the

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[1]Between the publication of Galbraith's theory of countervailing power in 1952 and his retirement from Harvard in 1978, total government outlays doubled in constant dollar terms and expanded as a percentage of gross national product (GNP) from 27 to 31 percent. Government's regulatory agencies' authority had expanded far more than expenditures. From the mid-1960s through the late 1970s, 20 major federal (social,

public appeared to have become disillusioned with the Galbraithian social agenda. After all, decades of government's fine tuning had left the country deep in "stagflation" and mired in debt. Poverty had not been relieved by a vast increase in social programs, and Congress continued to waste a lot of money catering not so much to broad and laudable national goals but to the narrow special interests of the politically powerful (who rarely included representatives of the poor).

In the early 1980s, it looked as though Galbraith's policy mantle had been dropped with no apparent heir to pick it up. Nevertheless, his mantle was retrieved and retained at Harvard. Robert B. Reich, on the faculty of Harvard's John F. Kennedy School of Government, is a student of Galbraith, either by way of Galbraith's classes or just his writings. Whatever the connection, Reich draws directly from Galbraith's work on industrial organization and shares many of the social, if not socialist, sympathies and political, or Democratic, leanings of his mentor: higher tax rates on what he calls the "fortunate fifth" of Americans, more government spending on social welfare programs for the disadvantaged and the working classes, and greater government controls on industry. He also shares his mentor's literary flare and his penchant for striking a responsive chord with a broad segment of the media and the public policy establishment in Washington.

However, in contrast to the consistency of Galbraith, Reich has articulated, within less than a decade, two, largely distinct, philosophical foundations for relieving the problems of what is perceived to be the not-so-fortunate four-fifths of the country's population. The purpose of this study is to compare and contrast Reich's two world views, the first articulated in the early 1980s in *The Next American Frontier* (1983) and the second in *The Work of Nations* (1991). We will find that the dire predictions Reich makes in the first book never materialized, even though his reform agenda was never adopted. That is just as well, for in the latter book Reich repudiates much of the industry-based government control and subsidy policies advocated with vigor in the former. We will also find that his remaining, and somewhat revised but still expansive, social agenda forged with

environmental, and economic) regulatory agencies were created, raising the total count of major agencies by two-thirds (Weidenbaum 1981, p. 54). The total administrative costs of all federal regulatory agencies expanded in constant dollar terms by 142 percent in one decade alone, the 1970s, for an average real growth of over 14 percent a year. The costs businesses incurred from complying with the added regulations escalated even faster than the cost of administering the programs (Warren and Chilton 1990, p. 4).

equal vigor in *The Work of Nations* is no longer consistent with his analytical framework. Nevertheless, Reich's early political predisposition, heavily weighted toward making government the nursemaid of American industries, has been tamed by time and the global technological trends he identifies. He has, in effect, shifted from being one of the nation's leading exponents of industrial policies to one of the leading exponents of freer markets, except in the provision of educational services and the rebuilding of the country's infrastructure. While hardly a conservative, he is no longer the Galbraithian liberal he once was.

Reich's Next American Frontier

Robert Reich literally burst onto the national public policy stage with the publication of *The Next American Frontier* (1983). In that book, Reich set himself up as a leading academic guru and foilsman for what, in the 1980s, became known as the industrial policy movement. That movement, and Reich's book, was grounded in the proposition that America was, as it had been for more than a decade, in relentless economic decline. Indeed, Reich starts his book with an ominous assessment: "Since the 1960s America's economy has been slowly unraveling. The economic decline has been marked by growing unemployment, mounting business failures, and falling productivity" (Reich 1983, p. 3). He was not concerned simply with the recent problems that emerged with the recession of 1980–81 or with a narrow sector of industry or a particular income class, but with the fate of the country—the full breadth of the economy—during the rest of the century, if not beyond. His goal was to revive the Galbraithian policy tradition to provide the intellectual inspiration for an economic rebirth of the American economy by a fundamental redirection of the way economic policies are formulated. A centerpiece of his economic strategy was the supplantation of government social agencies by private firms, which would be more efficient, effective, and pervasive conduits for government subsidies than government agencies could ever hope to be.

Reich argued that the country's GNP per capita had, by the early 1980s, fallen below levels achieved in other countries, and that the country's life expectancy was lower and its unemployment and infant mortality rates higher than those of most other advanced industrial economies. He claimed that long-term (15-year) trends would "worsen unless we act deliberately and strategically to speed the movement of capital and labor into higher-valued production" (1983, p. 238). America's next frontier would be, Reich argued, one of adaptation, of acknowledging changes in the world economy, reorganizing the way Americans do business, and adopting a role for government that would stand in sharp contrast to the free-market agenda of the Reagan administration.

Reich (1983, p. 21) noted that the process of adaptation would be made all the more difficult if the economic decline were allowed to continue "because then change threatens the economic security of people who are desperately trying to hold onto what they have." Nevertheless, any failure to adapt along the lines recommended would "rend the social fabric irreparably."

The seeds of America's decline that, supposedly, became patently evident in the late 1970s and early 1980s, according to Reich, had been sown a long time before, perhaps starting as early as 1870. The American economy began its trek toward being an industrial power during the last third of the 19th century because it had been blessed with an abundance of natural resources and a reasonably well-skilled labor force that, through immigration, had been extensively imported from abroad. Somewhat fortuitously, in Reich's theory of economic development, between 1870 and 1920, a major new invention (such as the typewriter and the electric light bulb) "made its appearance in America, on average, every fifteen months," fueling further industrial expansion (1983, p. 26). Being as large and unified as it was, the country was well suited for the development of large-scale industrial enterprises that relied on long runs of standardized products.

Problems emerged along the way, but most were partially rectified, de facto or de jure, by government action or acquiescence. "Ruinous price competition" set in. The vast company labor forces required by the technology of high-volume production "strained the average company's ability to manage, resulting in wasted effort and labor unrest" (1983, p. 32). The urbanization of workers also taxed the "government's limited capacity to ensure a minimum level of public health and safety" (1983, p. 32). In general, American firms had grown lethargic and uncompetitive, mainly because they had been overly protected from market forces by international trade barriers or by industrial collusion.

Pervasive price competition in the late 19th century was extensively solved by informal trade associations bent on collusion and by formal trusts and cartels among major market competitors. "Individual firms did not need to worry that their competitors might suddenly introduce a new innovation that would render current technologies obsolete since they already knew what their rivals were planning," a process that, Reich (1983, pp. 89–90) reasoned, ensured continued reduction in per unit costs . As a consequence, sometime during the first half of the 20th century, "market competition ceased to be the main force behind the evolution of American industry; nor were there many businessmen who could contemplate an unmanaged economy with anything but anxiety" (1983, p. 56).

In the 1920s, the birth of "management science," which fostered simplification of workplace tasks, predetermined rules for decision-making, and relied on an expanded information system internal to firms, enabled large firms to become larger and achieve further cost reductions with economies of scale. Those firms' potential overcapacity problems were remedied for a time by managing demand through advertising and by the development of conglomerates, which added stability through the addition of "new products and markets to compensate for the declining ones" (Reich 1983, p. 84).

The rise of unions across industries further reduced price competition by reducing wage competition. According to Reich (1983, p. 92):

> With labor increasingly organized along industry lines, a similar structure on the management side facilitated collective bargaining. Industry-wide coordination of investment and production also made firms more generous with wage increases because—if all companies granted them—wage concessions would not harm any one firm's competitive position and could safely be passed on to purchasers in the form of higher prices.

Franklin Roosevelt's New Deal sought to relieve many of the growing social problems that firms encountered with the growth of cities and industrial work forces. By the 1960s, the burning social issue, Reich maintained (as had Galbraith 16 years earlier), was no longer whether there would be planning (or the explicit control and direction of market forces), but who would do the planning—private firms or the government.[2] Both Galbraith and Reich made the case for their favored forms of government-directed national planning by maintaining, in so many words, that planning would be nothing new, only the motivation would be elevated and the results improved. "A

[2]Reich (1983, p. 232) writes, "America's free market has been supplanted by interlocking networks of subsidiaries, conglomerate headquarters, and financial institutions, through which industrial assets are rearranged and managers are recirculated, but from which new products and processes rarely emerge." Galbraith (1967, p. 6) had, in *The New Industrial State*, already declared that

> we have an economic system which, whatever its formal ideological billing, is to a substantial part a planned economy. The initiative in deciding what is to be produced comes not from the sovereign consumer who, through the market, issues the instructions that bend the productive mechanism to his ultimate will. Rather it comes from the great producing organization which reaches forward to control the markets that it is presumed to serve and, beyond, to bend the customer to its needs.

social organization premised on equity, security, and participation will generate greater productivity than one premised on greed and fear" (Reich 1983, p. 20).

In spite of government growth in a variety of areas, the American economy began to come unraveled around 1970, according to Reich, not because of the then-growing government deficits or the expansion of environmental and social regulation or the lack of investment in physical assets and research, as many others had suggested, but because of changes in the world economy. Key American industries had become uncompetitive at the same time the world economy had become more competitive. As a consequence, the U.S. economy had stagnated and then had begun its inexorable decline.

Why the decline? Reich argued that the American polity was, regrettably, still wedded to the outmoded free-market ideology; the polity was unable or unwilling to recognize the social benefits of explicit government intrusion in the economy. The result was a patchwork of business policies that were not very effective. Furthermore, American industries remained tied to old ways of doing business, most notably mass production of standardized products that, because of the advent of international trade, could be produced more cheaply with low-wage labor elsewhere in the world. That practice was causing America's manufacturing base to erode precipitously (Reich 1983, p. 127).

America's competitive position was also hampered because its businesspeople had become enraptured with "paper entrepreneurialism" (dubbed the "bastard child of scientific management") that involved the largely unproductive "manipulation of rules and numbers that in principle represent real assets and products but in fact generate profits primarily by the cleverness with which they are employed" (Reich 1983, p. 141). Never mind that changes in ownership might improve the efficiency with which the business resources are used. Never mind that the buying and selling of businesses might have been the result of a new competitiveness in the country, brought on by the expanding global economy. Never mind that in order for sales to go through, entrepreneurs and firms must expect a higher income flow from their assets than did the previous owners.

Reich was confident that shifts in the ownership of businesses and their assets through mergers and takeovers had no benefits. In Reich's words (1983, p. 145), paper entrepreneurs "do not enlarge the economic pie; they merely reassign the slices," increasing the cost of American products. Similarly, American businesses had become, by the late 1960s, overly enthralled with the building of conglomerates that "served no useful purpose" (1983, p. 151) and had sought to cover over their growing ineptitude by relying more and more on public relations activities that were no more productive than paper entrepreneurialism (1983, p. 154). Those bold claims were made with little or no supporting evidence and certainly with no attempt to counter opposing arguments concerning the positive economic and social benefits of mergers and takeovers.[3]

America's competitive problems were exacerbated by the Europeans and Japanese, especially, who had been far more effective in coordinating their structural adjustments via formal industrial policies. "Instead of the *ad hoc* scatter of separate industrial superstructures that developed in the United States, the tendency in continental Europe and Japan was to unify and coordinate economic policymaking across industries," that policy rendered their decisions more flexible than those of U.S. regulatory agencies and their government work far more attractive to talented university graduates than was the case in the United States (Reich 1983, p. 110).

The Industrial Policy Agenda

In *The Next American Frontier*, Reich's reform agenda amounted to a plea for the American polity to change its political inclinations and for American industries to change their ways, to stop seeking protection from competition, to shuck their reliance on standardized production processes, and to become more flexible in their structural arrangements. More important, he advocated a far-reaching industrial policy agenda that would make businesses and their workers the conduits for strategic implementation of government largess, protection, and tax incentives.

In general, his program was premised on the presumption that "America and in a similar sense Britain are victims of their own past success" in mass production (Reich 1983, p. 231). He maintained on more than one occasion that

> the only way industrialized nations can increase their citizens' standards of living in the future is to concentrate on the high-value niches within those industries [for example, textiles, automobiles, rubber, and chemicals that were then, supposedly, in rapid decline] and to seize and keep world leadership in new industries based on advanced and emerging technologies" [Reich 1983, p. 231].

The U.S. government, argued Reich, should follow Japan's lead with its Ministry of International Trade and Industry (MITI). According to Reich, the United States should be given the authority to

[3]Many of the benefits of so-called paper entrepreneurship are covered in Weidenbaum and Chilton (1988).

orchestrate the much-needed adjustment in the country's industrial structure:

> America must have the institutional capacity to marshal precise information about the needs of the declining industries and their dependents and to negotiate adjustment agreements that preserve the interests of the emerging industries. In both these aspects of industrial policymaking—acquiring strategic business information and negotiating adjustment agreements—the superstructures of management [in government] are sorely lacking [Reich 1983, p. 195].

While Reich complains that critics have far too glibly caricatured his industrial policy agenda as one of "picking [industrial] winners and losers," he boldly claims that the key to MITI's success lies in

> the explicit subsidies given to firms that agree to scrap excess capacity and in the firms' use of these subsidies to retrain and relocate their workers for more profitable endeavors. The subsidies for scrapping thereby accomplish two related objectives: They induce the least competitive firms to exit from the industry, thereby improving the profitability of more competitive firms; and they provide workers with adjustment assistance that is geared to cushioning and accelerating industrial change [Reich 1983, p. 199].

Reich (1983, p. 204) proposed the next American frontier could be conquered only by a dramatic increase in government expenditures on worker training, relocation allowances, unemployment compensation, workers' compensation, and health insurance—all of which are designed to eliminate dead-end jobs and to ease "the transition of its [America's] work force into skill-intensive production." Nevertheless, the novelty of his social agenda lay in the strictly industrial policies, ones designed to aid and abet an industrial transformation by manipulating the behavior of firms. In 1983, he advocated subsidies for firms locating in areas of high unemployment, tax incentives that would encourage firms to provide worker training (especially for older workers), tax penalties that would discourage layoffs, government procurements from businesses that would be undertaken explicitly to induce structural readjustments across industries, and selective international trade restrictions that would also encourage structural change (1983, pp. 239–47). He foresaw the development of a brand of industrial democracy in which workers would participate not only in training decisions but also in decisions about physical investment, reinvestment, disinvestment, and plant closings.

More generally, he proposed that firms become the social agents of the state. The state need not become larger, Reich (1983, p. 248) assures his readers on occasion (although it is difficult to see how it would not):

> Public funds now spent directly on these services [health care, Social Security, day care, disability, unemployment, and relocation] will instead be made available to businesses, according to the number of people they employ and the number of chronically unemployed they hire. Government bureaucracies that now administer these programs to individuals will be supplanted, to a large extent, by companies that administer them to their employees. . . . In this way, firms will become the agents of their employees, bargaining on behalf of their workers for different packages of government-supported social services. . . . Business enterprise, therefore, will largely replace geographic jurisdictions as conduits of government support for economic and human development. Companies, rather than state and local governments, will be the agents and intermediaries through which such assistance is provided.

While he does not always say so explicitly, it is quite clear that Reich was talking about the next American frontier being forged by American firms aided and abetted by the American government.

He also supported the creation of regional economic development—banks whose capital allocation decisions would be made by what came to be known as "tripartite councils" composed of representatives from management, labor, and government—and the creation of a "public board," located in the White House's Office of Management and Budget. Together, they would monitor all of the government's industrial efforts and "each year recommend to Congress and to the president what changes should be made in programs that may be retarding national economic development" (1983, p. 245). Still, Reich claimed that his agenda would not make government more "extensive," only "more open, more explicit, and more strategic" (1983, p. 14).

The Work of Nations

A series of books soon followed the tone set by *The Next American Frontier*. They all argued that the country was on a slippery economic slope and that the only possible remedy was a new, strategic, broad-based industrial policy, funded by greater taxes, mainly higher marginal tax rates on the wealthy.

Daniel Sharp (1988, p. 5), president of the American Assembly, stated flatly, "America can't compete." Harvard University economist Benjamin Friedman (1988, p. 300) joined the chorus with the lament, "The saddest outcome of all would be for America's decline to go on, but to go on so gradually that by the time the members of the next generation are old enough to begin asking who was responsible for their diminished circumstances, they will not even know what they have lost." And Yale University historian Paul Kennedy (1987, p. 534), the most prominent and widely read of the decline theorists, attested that the main "task facing American statesmen over the next decades, therefore, is to recognize that broad trends [of lost economic and political hegemony] are under way [for the United States], and that there is a need to 'manage' affairs so that the *relative* erosion of the United States' position takes place slowly and smoothly."

Nevertheless, the ensuing years were not kind to Reich's and others' predictions of continued economic decay. The Reagan administration was openly hostile to practically all industrial policy agendas, thwarting the passage of every serious proposal at nearly every turn. Instead of raising tax rates, Reagan lowered them, even for the rich. Government expenditures continued to rise in real dollar terms but stagnated as a percentage of GNP. Government regulatory agencies also had budget increases in constant dollar terms, but many saw their budgets contract as a fraction of the national economy and their labor forces fall in absolute numbers or, at least, relative to the expanding civilian labor force. Some rechanneling of federal government expenditures occurred, but it was mainly from Reich's favored social programs to defense outlays and interest payments on the mounting federal debt.[4]

Nevertheless, the country did not continue along the path of decline, or "deindustrialization," that was presumably afoot in the early 1980s. Indeed, real GNP was 27 percent higher at the end of the decade than it was at the beginning, real per capita disposable income grew by 17 percent throughout the 1980s, and total employment grew by over 18 million, or 18 percent, during the decade. At its peak in 1990, before the advent of the current recession, the industrial production index stood 24 percent above its 1980 level. Even manufacturing output, which was supposed to be evaporating with import competition, continued to rise in real terms and to remain at more or less the same percentage of GNP that it had been during the four previous decades, in spite of the fact that the number of U.S. manufacturing employees fell by about 2 million. (At the same time, employment in the foreign affiliates of U.S. manufacturing firms more than offset the domestic decline in employment.)

[4]The changes in the role of the U.S. government in the economy during the 1980s are charted in McKenzie and Lee (1991, chap. 8).

Contrary to what might have been inferred from Reich's and others' assessments of what was happening and would continue to happen, U.S. production did not even decline relative to the output of the rest of the world. Total production in the United held its own, relatively speaking, in the world economy during the early 1980s. It rose slightly, relatively speaking, in the late 1980s (despite the obvious overstatement of the level and growth of production in the Soviet Union and other, now former, communist countries in Eastern Europe).[5]

Such facts notwithstanding, in 1991, Reich returned to print with *The Work of Nations*, in which he makes a major effort to reinterpret the recent economic history of the United States and the world and to forewarn of pending economic calamity if public policy is not reconstituted. By 1991, however, he had shucked, and for good reason, much of the explicit firm-centered industrial policy agenda that he had advertised as crucial. His analytical framework had changed, mainly because his vision of world conditions had changed radically since the publication of *The Next American Frontier*.

In *The Work of Nations*, Reich (1991, p. 4) starts by appearing to assume the role of the detached observer of political commentators, noting the "numbing regularity" with which other political partisans, pessimists and optimists alike, appeal to economic data to make the case for their favored policies, never admitting that he may have been one of the partisan commentators. "The optimists point ever upward: Look at the number of new jobs! Marvel at all the small entrepreneurial firms! . . . The economy is booming as never before. . . . The pessimists point downward: Bemoan the loss of manufacturing. Bewail the trade deficit. . . . The economy is collapsing around us."

Who is right? Without saying so, Reich is forced to concede that the metaphor of the sinking economic ship of state that he exploited (in various forms) with great care in his earlier book no longer applies. The problem of picturing national economies as a "worldwide regatta whose prize is economic preeminence," which he had in no small way fostered, is, bluntly put, all wrong (1991, p. 5). Granted, the picture of the ship of state may have been appropriate, say, when Galbraith wrote *The New Industrial State* or even as late as 1983 when Reich wrote *The Next American Frontier*, but no longer. According to Reich, the world and its national economies have become fractured and, at the same time, integrated.

[5] The details of those arguments are covered in McKenzie (1988).

Admittedly, Reich seeks to make his new work appear to be an extension of *The Next American Frontier* by recasting much of the earlier historical analysis, articulated in the best of Galbraithian traditions, without explicitly conceding that his policy conclusions were misdirected. Rather, he simply repeats his earlier claim that, at one time, America's industrial might expanded because of the growing dominance of America's large corporations that became even larger because of their successful efforts to suppress competition through collusion, mergers, and consolidation (although he offers only a rudimentary and confused theory of how collusion and the monopolization of markets, which normally lead to higher prices, actually lead to lower prices).[6] At that time, "the well-being of citizens was linked to the success of the national economy" (1991, p. 34), which in turn was tied inextricably to the success of the dominant corporations. In strict accord with Galbraith's much earlier work, Reich notes that 500 major corporations represented the core of the American economy, mainly because they produced half of the country's output and owned the vast majority of the country's industrial assets. Those 500 "were the champions of the national economy; their successes were its success. They *were* the American economy" (1991, p. 47; emphasis in the original).

However, the world has changed, Reich correctly argues. Production has become globalized and integrated. The image of the economic fates of American citizens rising and falling together, as if in a single boat, is no longer apt, mainly because the boat is no longer American made, or at least not totally so. Indeed, " 'American' corporations and 'American' industries are ceasing to exist in any form that can be meaningfully distinguished from the rest of the global economy" (1991, p. 77). The question, "Who is us?" can no longer be answered simply.

Technology has made capital, especially, far more mobile than it once was. "Money, technology, information, and goods are flowing across national borders with unprecedented rapidity and ease" (Reich 1991, p. 6). The result is that General Motors, General Electric, IBM, and a host of other American-grown companies produce

[6]Reich (1991, p. 67) writes, "[T]he core American corporation would plan and implement the production of a large volume of goods. The large volume of goods would create significant economies of scale, thus reducing the cost of producing each unit. By coordinating with other core corporations, prices could be set high enough to ensure substantial revenues," which would be shared with managers and union members alike. Reich does not say where the core corporations get the power in the first place to plan and implement long production runs. Presumably, they must engage in price and nonprice competition to take over a major share of the market, which hardly represents the type of power normally associated with monopolies or cartels.

products that are only part American. At the same time, the German firm Seimans produces products that are only part German; they are also part American.

Those simple observations obviously had a profound impact on Reich, for without ever acknowledging the changes in his own thinking, he writes, in *The Work of Nations*, that "few ideas are more dangerous than good solutions to the wrong problems." He then adds, again as if he had never been a party to the earlier industrial policy debate, "Politicians and pundits talk loosely of 'restoring' or 'restarting' American business. . . . Others offer plans for regaining America's competitive edge and revitalizing the American economy. . . . [A]ll suffer from vestigial thinking about exactly what it is that must be restored . . . or revitalized" (1991, p. 243).

Then, repudiating much of his earlier industrial policy agenda, which made American-grown corporations the policy pivots, Reich concludes that "there is no longer any reason for the United States—or for any other nation—to protect, subsidize, or otherwise support its corporations above all others, as some have argued. . . . Neither the profitability of a nation's corporations nor the successes of its investors necessarily improve the standard of living of most of the nation's citizens" (1991, p. 8). If the country tries to subsidize companies, the policy benefits will not necessarily be retained in the United States; the government largess will simply be allocated, as are all other company funds, to the most profitable venue in the world, which may be the United States but may also be Sri Lanka or New Zealand.

Instead of government benefits being routed to "American" corporations, writes Reich, they should be routed to the heart and soul of the economy, and society, the immobile infrastructure, which includes the education, transportation, communication, and utility systems. The benefits should also be routed to the equally immobile American people, specifically American workers, not all of whom are in the same economic boat (1991, p. 173). In fact, Reich (1991, pp. 174–80) distinguishes three boatloads of people, the "routine production workers" (those engaged in repetitive tasks in high-volume production processes), the "in-person service" providers (those working directly with other people mostly in repetitive tasks), and the "symbolic analysts" (those involved in problem identification and solving and in "strategic brokering" of resources). From an array of data on changes in income distribution, Reich deduces that his critics were right: "America" is not in long-term decline. On the other hand, he concludes that, while the aggregate income and production figures show continued progress, the income-distribution statistics reveal regression for the four-fifths of the population who are, for the most part, from the ranks of the routine production workers and the in-service providers and who must compete vigorously for work with low-paid labor in underdeveloped countries. Only the top fortunate fifth of all income earners—who in the aggregate receive more than half of the nation's income and who are mostly university-educated symbolic analysts—have prospered over the past two decades, mainly by selling their high-demand services to the highest bidder in the global marketplace and by being the principal beneficiaries of the Reagan tax cuts and other policy shifts.

A return to economic prosperity for most Americans means a substantial increase in government expenditures on formal education, on-the-job training, and basic transportation and communication systems on which businesses of all national origins thrive. For the wealth of a nation is no longer businesses that are now footloose on a global scale. Rather, "the skills of a nation's work force and the quality of its infrastructure are what make it unique, and uniquely attractive, in the world economy. Investments in these relatively immobile factors of worldwide production are what chiefly distinguish one nation from another; money, by contrast, moves easily around the world" (Reich 1991, p. 264).

The Problems Inherent in the New Vision

My purpose here is not to critique in detail Reich's newfound policy conclusions drawn from income-distribution statistics, although his statistics and conclusions are worthy of challenge. I will simply note that his conclusions should be studied with healthy skepticism. The relayed facts on income distribution may be no better interpreted today than were the facts on industrial organization and the usefulness of industrial policies in the early 1980s. I will simply note that Reich (1991) is able to conclude that four-fifths of Americans have not been progressing economically. He arrives at that conclusion partly because he ignores the growth in nonwage benefits, uses the flawed consumer price index for computing changes in real income, often fails to adjust for changes in the characteristics of the labor forces and the jobs that are filled, focuses on the average incomes of the five quintiles of income distribution, and at times juxtaposes discussions of reductions in the shares of the nation's income going to the lower quintiles with discussions of decreases in their absolute income levels. For example, he points out that the average wages and incomes (not including fringe benefits) of a sizable segment of the population (mainly in-service providers who account for about 30 percent of the labor force) did not rise during the 1980s and that the average income of another sizable segment (mainly routine production workers who make up about a quarter of the labor force) actually fell. He then concludes that four-fifths of the population (the entire labor force minus the 20 percent who are symbolic analysts) are no better off than they were a decade or more earlier.

However, the appeals for changes in income shares often hide real income increases, and the stagnant or falling averages employed ignore the number of Americans in the lower four-fifths whose economic lots actually improved during the 1980s as much, if not more, than the economic lots of Americans in the fortunate fifth. Furthermore, the fact that the average income of the fortunate fifth went up in the 1980s does not mean that some of its members did not regress. Very likely, some members of the fortunate fifth experienced increases, while others experienced declines. Indeed, the history of American income distribution has been one of considerable shuffle among the quintiles of the income spectrum. For example, a study of changes in income distribution during the 1970s found that 50 percent of the people in both the top and the bottom quintiles in 1978 had changed places in the income distribution since 1972.[7]

Such issues must await more study. My purpose here is to recognize the partial but striking convergence of economic and political thinking that the advent of the global economy has imposed on public policy commentaries. Reich, in *The Work of Nations*, and Dwight Lee and I, in *Quicksilver Capital: How the Rapid Movement of Wealth Has Changed the World*, both of which were released within two months of one another, begin with many of the same premises:

1. Developments in technology have drastically reduced the cost of international transportation and communications and have greatly increased capital mobility.
2. National economies have become integrated and interdependent, so much so that "nation " and "national economies" have lost their meaning.
3. Business has become global because competition has forced firms to seek low-cost production venues without regard to exact location.
4. Businesses and people must do what is necessary in the way of upgrading their education and product quality and in the way

[7]As reported in Browning (1989).

of minimizing costs to meet not just national standards but world standards.[8]

5. Industry-based industrial policies, whether in the form of import protection or subsidies, will not, in the context of the global economy, improve the living standards of people.
6. Financial and physical capital, in general, is more mobile internationally than human capital. However, some human capital, including the skills of symbolic analysts, is just as mobile internationally, if not more so, than financial and physical capital.
7. The economic fates of Americans are no longer moving together. As they diverge, "the top may be losing the long-held sense of connectedness with the bottom. . . . Ironically, as the rest of the nation grows more economically dependent than ever on the fortunate fifth, the fortunate fifth is becoming less and less dependent on them" (Reich 1991, p. 250).
8. Most Americans (and Germans and Italians) already bear a heavy tax and "cannot afford to shoulder the added burden of higher levels of public spending [implied by Reich's social agenda]. It would have to be borne instead by the one group of Americans whose earnings have been increasing—our symbolic analysts" (Reich 1991, p. 250).

Where we part company is on the policy conclusions. Reich says, in so many ways, that the cuts in federal taxes and expenditures orchestrated by the Reagan administration are the source of many of our current national maladies and that the social policies of the 1980s must be reversed. Government social expenditures on everything from education to care for the homeless must be treated as outlays on the national infrastructure and must be greatly expanded. To finance the greater social expenditures, the marginal tax rates paid by people with "princely incomes" must be drastically raised.

In contrast, Lee and I argue that the technological and capital mobility conditions that Reich identifies were the cause of the policy course of lower tax rates, deregulation, and privatization observed during the 1980s in the United States and in most other major countries around the world. Capital mobility had made the United States and other countries competitors for the world's capital base, and they

[8]Lee and I could not agree more with Reich (Reich 1991, p. 265) when he writes that higher skills and higher compensation go hand in hand and that "without adequate skills and infrastructure, however, the relationship is likely to be reversed—a vicious circle in which global investment can be lured only by relatively low wages and low taxes. These enticements in turn make it more difficult for the nation to finance adequate education and infrastructure in the future."

had to start competing for the capital base by lowering taxes and making production in their respective countries more cost effective. We suggest that governments' fiscal and regulatory hands are tied as never before for the very reason Reich notes in passing but then virtually dismisses as irrelevant to the development of policy: The people with symbolic-analytical skills and princely incomes will be the ones who will be forced to bear the burden of the expanded government programs (Reich 1991, p. 250), but they will also represent some of the most mobile of all capital (in fact, they have been using their newfound mobility to secede from the rest of the nation) (Reich 1991, p. 251).

Conclusion

In the early and mid-1980s, public policy debates were conducted extensively along ideological, normative, and empirical lines. Policy partisans from the left and the right articulated and defended well-honed sets of principles. Partisans on the right paid their respect to the market principles laid down by Adam Smith and Milton Friedman, while partisans from the left appealed to the collectivist principles of Galbraith, if not Karl Marx. Empirical claims regarding the fact and extent of deindustrialization were made, defended, and challenged. Everyone was ultimately interested in specifying, in the name of fairness, equity, or efficiency, what governments should do. Robert Reich and I know that debate all too well. We were partisans in it, although almost always from polar analytical and political positions.

The character of the debate in the 1990s has changed for all of us. We have noted the considerable agreement on the facts of the global economy. In that regard, our views have converged. Accordingly, the debate among partisans has become less grounded in ideological and empirical concerns. At the same time, some divergence remains, but the debate has been solidly joined on grounds that will ultimately be resolved not by partisan writings but by events in the world economy. The current debate appears to be over not what we all would like or what ideology would prescribe but rather over what governments can do and will be able to do for people, given the rapidly escalating mobility of capital and, for that matter, people. That escalating mobility may very well prevent governments from enacting the type of expansive aid for the not-so-fortunate four-fifths of the income distribution that Reich would have the fortunate fifth finance. I suspect that when Robert Reich goes to print with his next best seller, he too will have seen this basic point: Transnational economic forces are imposing tight controls on the political affairs, even the democratic affairs, of people whose allegiances to countries are being relentlessly dissipated.

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