LABOR CENTER REPORTER

Number 117
April 1984

UNIVERSITY OF CALIFORNIA, BERKELEY
CENTER FOR LABOR RESEARCH AND EDUCATION
INSTITUTE OF INDUSTRIAL RELATIONS
BERKELEY, CA 94720
(415) 642-0323

ECONOMIC CRISIS AND INDUSTRIAL POLICY: AN INTRODUCTION

by Tom Larson

The general economic stagnation of the past ten years and the decline of major industries in the U.S. (auto and steel, for example) have generated widespread interest in how to revitalize U.S. industry. This is the first of a series of articles that will examine the government's role and responsibility in economic recovery and growth and programs for combating high levels of unemployment and declining levels of real wages and industrial investment. This article summarizes major crisis tendencies in our politico-economic system that have contributed to economic stagnation, and discusses the nature and importance of the government's role in the economy.

International Competition and the Fiscal Crisis – Fear that our economic system is prone to economic crisis is based on evidence of long-term decline. In the new international economic order, U.S. firms are often at a competitive disadvantage. Older industries in the U.S. seem to be especially vulnerable to foreign competition, with aged and inefficient plants competing with modern foreign plants. Billions of dollars in earnings and millions of jobs have been lost to international competition. We can expect more competition in the future and we need policies to deal with changes in international markets.

The government has always played an important role in the economy. For instance, in the 19th century, the federal government helped finance canal and railroad construction, regulated businesses through legislation such as the Sherman Anti-Trust Act, and established the first national regulatory agency, the Interstate Commerce Commission, in 1887. Today, the government is seen as being responsible for aggregate economic performance, as exemplified by the Full Employment Act of 1946, the Humphrey-Hawkins Act, and current concerns about deficits. While economic crisis tendencies suggest the need for strategic national planning, there are fiscal, social, and political crisis tendencies that limit the ability of the government to respond to economic problems.

The fiscal crisis—the tendency for government expenditures to outpace revenues—leads to a gap between what the government is expected to do and what it can do. This threatens to restrict the ability of the government to pursue even short-run policies. The government has helped to hold down the costs of private firms by providing a variety of social services: social security, unemployment insurance, welfare, etc. This has helped generate growth in the private sector by subsidizing benefit programs, but has greatly expanded the need for federal revenues in order to fund social security and other income transfer programs. The rising expense of maintaining government obligations (a problem that will only increase as the population ages) has contributed to the tax revolt. The tax revolt has reduced the ability of the government to provide services, but demands on the state for services have continued to increase. Unable to substantially reduce social security and seeking to boost military spending, the present administration has responded by cutting social services, but they are only a small part of the budget. Cuts in welfare, employment and manpower training programs not only directly increase poverty and unemployment levels, but also reduce the government's ability to use such programs to stabilize the economy during business downturns. During a recession unemployment and welfare benefits increase, helping to maintain total purchasing power and to buoy the economy. The fiscal crisis threatens the ability of the government to respond to cyclical economic downturns.

Social and Political Crises Tendencies – The ability of the state (i.e., the federal government) to respond to economic crisis depends on its ability to institute change through the political process. In order to implement industrial policy, the state must deal with three major social and political crisis tendencies if it is to engage in long-range economic planning. First, there is a rationality crisis. The state has acquired responsibilities for satisfying the economic and social needs of society, but the state seems

unwilling or unprepared to accept fully its responsibilities, since mechanisms for rational decision making have not been established, leaving goals uncoordinated and unranked. As a result, long range planning is either minimal, fragmentary, unrealistic, or non-existent. Even where plans are formulated, techniques of enforcement are lacking. Thus, the state is seen as being responsible for the direction of the economy, but proceeds on an ad hoc basis. The bailouts of Chrysler and Lockheed cause firms to expect such action in the future, but do not reflect any particular policy. If firms are to be subsidized, some criteria as to which firms can qualify for aid should be developed.

Second, there is a legitimation crisis: the intrusion of the state into all spheres of society increases its need for legitimation. The state is unprepared to exercise its public responsibility but must hide this fact from the public. As the public senses that things are wrong with the economy (unemployment and inflation cannot be hidden) it challenges the government to accept its responsibilities and address these problems. But support is withdrawn just as the government needs it. President Carter sought labor's aid in fighting inflation and asked unions to hold down wage demands. Knowing that the state could not or would not also hold down prices, labor justifiably refused to go along. As the government fails to legitimate itself by solving problems, public support dwindles.

Third, there is a motivational crisis (this is linked to the problem of alienation). Ties to family and community are important sources of motivation, but are torn apart in our modern industrial society, as the labor market favors small and highly mobile families. Family members are highly segregated. Husbands and wives see little of each other during the day. Children are kept in school until old enough to leave home. Grandparents live in retirement homes and communities. Traditions that are important for the reproduction of family and community are eroding while the social system is being overloaded by new needs. Isolated even from family and community, individuals are especially apathetic concerning the political process. This diminishes the possibility of democratic planning.

Conclusion – The stagnation of the U.S. economy may result from inherent crisis tendencies that cannot be solved by the private sector. International competition threatens to accelerate decline in major industries. The fiscal crisis threatens the ability of the government to provide services that are essential to the functioning of a modern industrial society and to stabilizing the economy. The rationality, legitimacy and motivational crises suggest that the state, and the electorate, may be unable and unwilling to respond to economic crisis with support for long-range strategic planning. Given social, political and fiscal obstacles, is it possible to develop and implement long-range planning? If long-range planning is not now possible, we still need to deal with the problems of adjusting to industrial decline, seeking to ease the pain of industrial displacement and of long-term unemployment. The failure of the private sector to meet the challenge of foreign competition, the inability of the government to generate growth using ad hoc measures, and the difficulties of adjusting to massive structural changes suggest that we seriously consider rationalizing our ad hoc and chaotic policies. No industrial policy could solve all our problems, but developing one could identify the appropriate role of the government in the economy. This would help to legitimate the state's role and make economic policy more effective.

--Tom Larson