PLANNING AMERICA: GOVERNMENT OR THE MARKET? INTRODUCTION

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The question of whether the future of American industry should be left to the "blind forces of the marketplace" or whether "rational" economic development requires "better" government planning and greater "cooperation" among government, business, and labor is of fundamental importance. In order to address this question and to consider the various criticisms of the market system, the Cato Institute sponsored the conference "Planning America: Government or the Market?" in Washington, D.C., April 27–28, 1984. The conference papers, along with articles by Sakoh, Trezise, Vieira, and DiLorenzo, provide a comprehensive treatment of the major issues surrounding the industrial policy debate.

The current notion that America's future economic development cannot be left solely to market forces is by no means novel. It has long been argued that industrial development requires "rational" and "better" government planning, and that a "cooperativist" approach to planning is superior to the perceived "individualistic" approach of the market.[1] This was the position taken in the 1930s when legislative activists of the New Deal era tried to institutionalize "codes of fair competition" as part of the National Industrial Recovery Act, later declared unconstitutional in *A.L.A. Schechter Poultry Corp. v. United States*.[2] It was further represented by the Reconstruction

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[1]In fact, the individualistic approach of the market is wholly consistent with cooperation, properly understood as the *voluntary* exchange of goods and services. The free market is a mechanism for generating cooperation and mutually beneficial exchanges. On the difference between "true individualism" (which is characterized by "the spontaneous collaboration of free men") and "false individualism" (which is characterized by collectivism and the use of government coercion to achieve some preconceived plan), see Hayek (1948, chap. 1).

[2]295 U.S. 495 (1935). For a discussion of this case, see Vieira (1976, pp. 601–4).

Finance Corporation (RFC) as it operated during the 1932–53 period to influence the allocation of capital (see Yeager 1977). More recently, it found expression in the Balanced Growth and Economic Planning Act of 1975 (see Hayek 1978, pp. 245–46).

Current proponents of industrial policy such as Robert Reich, Felix Rohatyn, Lester Thurow, Lee Iacocca, and Congressman John J. LaFalce continue the cooperativist tradition. All call for a tripartite council consisting of representatives from government, business, and industry, whose function would be to create a "national consensus" for industrial development. Proponents of industrial policy also advocate a development bank that could help channel investment funds to those areas targeted by the tripartite council or some other agency. The private sector would provide the bulk of investment funds, but the development bank—a type of RFC—would help allocate credit to where the "planners" thought it was most productive.

These ideas have found content in the 1984 Industrial Competitiveness Act (H.R. 4360), whose primary architect was Congressman LaFalce. The key provisions of that act are the establishment of a Council on Industrial Competitiveness and a Bank for Industrial Competitiveness. The tripartite council would seek to adopt a strategy for industrial development that would replace the current patchwork of government development programs—regulations, tax incentives, subsidies, trade policies, and so on—with a coordinated and consistent set of policies designed to achieve a broad consensus and foster economic growth. The development bank would be a major tool for implementing this new industrial policy.

Throughout the literature on industrial policy, one can find repeated references to the notion that the world is too complex to allow the market to determine the future industrial pattern of the United States. The government must impose order on an otherwise chaotic market system, and it can do so without sacrificing personal and economic freedoms. What is proposed, say advocates of the new industrial policy, is not comprehensive central planning but a type of "indicative" or "voluntary" planning. Furthermore, these proponents claim that since we already have government planning, we should at least try to make it more efficient. Lee Iacocca, for example, recently stated: "[A]ny debate over *whether* the [United States] should have an industrial policy is outdated and way off course. We already have one but it's all messed up. The real issue is should we have a *rational* industrial policy" (1984, p. 4). Thurow has argued in a similar vein: "The most compelling argument for industrial policies is ... the argument that we already have industrial policies and that it is in fact impossible for a democracy not to have industrial policies. Every

tariff, every quota, every allocation of credit, every bail-out is an industrial policy. It is just a terribly inefficient back door industrial policy" (1983, p. 178).

Industrial policy advocates, however, are not simply rejecting the current piecemeal approach to development planning; they are also expressing their distrust of the free market, especially in the area of investment decision making. Thurow, for example, argues that "[m]ajor investment decisions have become too important to be left to the private market alone.... Japan Inc. needs to be met with U.S.A. Inc." (1981, p. 192). The same distrust is found in Reich's proposal for a "national bargaining arena" where the distribution of the benefits and costs of adjustment policies could be determined and where "government, business, and labor" could "fashion explicit agreements to restructure American industry" (1983a, p. 107).

Nevertheless, advocates of a cooperativist approach to industrial policy deny they are anti-market; they would argue only for limited government planning and against comprehensive central planning of the economy. Rohatyn, for instance, stated in congressional testimony: "I am opposed to government planning and to government-owned industries. I believe that the free market is usually the best market. However, the free market is not always adequate and not always right" (1984, p. 97). According to Thurow: "The problem is not 'the market' versus 'planning', but how planning can be used to improve one's market performance.... Whatever one believes about the virtues of unfettered free enterprise, empirical feedback indicates that 'success' is not occurring automatically. What used to work won't work. For the world has changed" (1983, p. 173).

We are left with the feeling that somehow unconstrained markets cannot work as well as government-aided markets; that free markets do not generate adequate information and fail to coordinate economic activity; that cooperation is better achieved via tripartite councils than via market competition; and that Adam Smith's invisible hand of competition must be supplemented with the visible hand of government to achieve industrial growth (see Nutter 1983, chap. 15).

One becomes suspicious, however, that underlying all these criticisms of the market is a basic dissatisfaction with the distribution of income and the pattern of production generated by the competitive market process. This is confirmed by Reich: "[I]n the emerging era of productivity, *social justice* is not incompatible with economic growth, but essential to it. A social organization premised on equity, security, and participation will generate greater productivity than one premised on greed and fear" (1983b, p. 20; emphasis added). The implication, of course, is that "equity, security, and

participation" can best be achieved by the type of industrial policy advocated by Reich and his fellow travellers, while the market, which is characterized by "greed and fear," is largely responsible for the demise of U.S. productivity growth.

In contrast, advocates of the free market argue that in a world of scarcity, where knowledge about wants, resources, and technology is costly, some type of planning is inevitable. But, market proponents claim, it is individual planning via the use of market prices, profits, and mutually beneficial adjustments to changing conditions—not greater government planning—that is essential for economic coordination and development in line with consumer preferences. The idea that greater "cooperation" between government officials and market participants can somehow improve the flow of information and resources is a red herring—it ignores the fact that the market process and the political process are necessarily different.

Market cooperation (competition) is based on *voluntary* exchange: There must be consent among all parties to an exchange for the exchange to take place; that is, there must be unanimity. The fact that third parties—those outside the direct exchange—are harmed by changing prices and patterns of production is irrelevant, for these parties have no legitimate right to prevent consumers from choosing a preferred combination of resources and products. The competitive market process, which Hayek has called a "discovery procedure," is based on private property rights with prices and profits providing the information and incentives necessary to guide resources to where they have their highest-valued uses, as determined by *consumers*.[3]

From the Hayekian perspective, the economic problem is basically a knowledge problem: "[H]ow to secure the best use of resources known to any of the members of society, for ends whose relative importance only these individuals know. . . . a problem of the utilization of knowledge which is not given to anyone in its totality" (Hayek 1948, p. 78). Thus, according to Hayek (pp. 83–84):

> If we can agree that the economic problem of society is mainly one of rapid adaptation to changes in the particular circumstances of time and place, it would seem to follow that the ultimate decisions must be left to the people who are familiar with these circumstances, who know directly of the relevant changes and of the resources immediately available to meet them.

Awareness of the limitations of human knowledge, the impossibility of centralizing all the information that would be relevant for

[3]According to Hayek, competition is "a procedure for the discovery of such facts as, without resort to it, would not be known to anyone, or at least would not be utilized" (1978, p. 179).

allocating resources in line with consumers' preferences, and the danger to individual freedom that arises from government planning led Hayek to conclude that the major function of government should be to protect private property rights, including freedom of contract. Hayek argued that if the government limited itself to "the enforcement of universal rules of just conduct, protecting a recognizable private domain of individuals, a spontaneous order of human activities of much greater complexity will form itself than could ever be produced by deliberate arrangement" (1967, p. 162).[4]

Hayek would dispute Reich's claim that "social justice"—by which Reich means distributive as opposed to commutative justice—is a necessary condition for economic growth. For Hayek the pursuit of social justice must disrupt the market order, which depends on private property and freedom of choice. Moreover, the very notion of social justice (as a public policy goal) is misleading for Hayek because there is no way to arrive at an objective measure to determine beforehand the distribution of income that is deemed socially optimal. From this it should be clear that any attempt to rearrange the market distribution of income, which is the result of a voluntary process of serving consumers' interests, must of necessity result in coercion. And, if individuals value freedom because it provides them the greatest opportunity to utilize their talents, the necessary information to satisfy their wants, and the incentive to serve other consumers in an efficient manner, then the loss of this freedom can be expected to reduce—rather than increase—individual and social welfare.[5]

The political process under government planning would be fundamentally different from the impersonal market process. Public choice theory teaches that the absence of residual claimants in government and the incentive to cater to special interest groups result in the rent-seeking activity we are witnessing today. Bureaucrats, like other individuals, are self-interested—they pursue those activities

[4]"That we have been able to achieve a reasonably high degree of order in our economic lives despite modern complexities," says Hayek, "is *only* because our affairs have been guided, not by central direction, but by the operations of the market and competition in securing the mutual adjustment of separate efforts. . . . What the marketplace and its prices give most particularly is a continuing updating of the ever changing relative scarcities of different commodities and services. . . . the complexity of the structure required to produce the real income we are now able to provide for the masses of the Western world . . . could develop *only* because we did *not* attempt to plan it or subject it to any central direction, but left it to be guided by a spontaneous ordering mechanism, or a self-generating order, as modern cybernetics calls it" (Hayek 1978, p. 237).

[5]For a fuller discussion of the notion of justice in general and social justice in particular, see Hayek (1982, chap. 9; 1978, chap. 5 and p. 238; 1972, pp. 231–33). Also see Dorn (1981), Nozick (1974), and Pilon (1981, 1982, 1983).

that will increase their net benefits, subject to the constraints facing them. The rewards they can capture and the costs they must bear for different activities will largely shape their behavior. With no profit/loss test within government, there is no reason to believe that government officials will follow the so-called public interest. Without strict constitutional limits on the scope of government action, it is difficult to see how Reich-type industrial policy proposals could avoid increasing this rent-seeking behavior.[6] When tripartite councils are substituted for the decisions of private market participants, the marketplace necessarily becomes politicized, and special interest groups will use the political machinery to impose their will on the general public.

Before we can accept the claims of Reich and other proponents of an activist industrial policy, the following questions must be considered in more detail. What type of institutional arrangement—government or the market—would best protect economic liberties and best satisfy consumer preferences? What are the effects of each planning arrangement and each type of competition—political competition and price competition—on the coordination of individual plans; and what planning mechanism would provide a more stable framework for making rational decisions about production, employment, consumption, and investment? Is the role of the government one of setting the rules of the game and then letting the market allocate resources? Or should the government push the market in the direction favored by some tripartite council dominated by large corporations and major unions? Most important, how will government planners or tripartite council members utilize the relevant information about wants, resources, and technology that is only available to individual market participants, and that can only be transmitted through the market process? Finally, how will alternative modes of competition and economic organization—one based on political or forced cooperation and the other on market or voluntary cooperation—affect the types and costs of information generated and the incentive to innovate and discover new information in a dynamic economy?

In addition to these questions, any serious discussion of industrial policy must consider the following five points.

1. In choosing between alternative industrial policies, or alternative methods of organizing economic activity, one must avoid falling into the trap of taking what Demsetz (1969, p. 1) calls the "*nirvana*

[6]For a useful discussion of the current developments in public choice theory, the nature of the rent-seeking argument, and the benefits of constitutional limits on the power of government, see Buchanan and Tollison (1984).

approach": The view that the relevant policy choice is "between an ideal norm and an existing 'imperfect' institutional arrangement." For example, economists who attack the existing market mechanism because it deviates from the static model of perfect competition and then point to that deviation to justify government intervention are committing the nirvana fallacy. A more effective approach to policy appraisal, says Demsetz (p. 1), is the *"comparative institution* approach," in which the relevant policy choice is between existing institutions, all of which are imperfect. We can then ask how different ways of organizing industry and commerce would affect incentives and economic behavior, as well as consumers' sovereignty.

Taking a comparative institution approach does not mean we have to throw out all our theoretical models. It does mean, however, that we should examine existing institutions as they are and then use our theory to try to improve those institutions. This approach to policy questions, for example, would have us consider whether we can improve existing institutions so they approach more closely the requirements for a competitive market process. The comparative institution approach warns us that if the behavior of market participants deviates from the norm of perfect competition, the behavior of government agents also deviates from the results predicted by the public interest theory of government.

2. We must remember that generating consensus for economic change via the political process is significantly different from reaching agreement via the market process. These two processes for cooperation represent the difference between a discretionary approach to resource allocation and one based on constitutional rules that provide a framework for individual choice. Public choice theory has shown that in a democracy, majority rule does not guarantee results consistent with individual preferences. Likewise, there is no reason to believe that imposing democratic (majority) rule on the marketplace through tripartite decision making would lead to an allocation of resources that satisfies consumer preferences better than the free-market alternative based on a unanimity rule for each individual transaction.[7]

[7]Drawing on Hutt's work (1975, chap. 5), it could be argued that tripartite councils are inconsistent with true democratic government—since they interfere with constitutional rules that would minimize coercion—and with what Hutt calls "*democratic* consumers' sovereignty." On this latter point, Hutt argues: "[W]hen the framework of institutions releases and safeguards the loss-avoidance, profit-seeking incentives as far as is practicable, we can call the *consumers' sovereignty* exercised 'democratic.' The adjective 'democratic' is apt when the sovereignty expressed reflects the forecast choices of all income receivers through a system of voting under which each person's vote about how the community's resources shall be utilized is weighted in proportion to the value of the productive services that he and his property (whether acquired through his

3. It is an illusion to think that a government-business-labor council (or even a council of saints) could outperform the market in gathering the information relevant to satisfying consumer preferences for both present and future consumption—the information simply is not available to a centralized body, nor could it be discerned from statistical data (see Hayek 1948, chap. 4). Moreover, in reality, the council would be subject to political pressures and would redistribute resources and income to where it was most politically expedient. In the process information that is politically valuable will come to the surface, but information that is of value to consumers and resource owners will remain submerged—distorted by government meddling in the price and profit system.

The market is a process of trial and error, and one in which it pays individuals to correct their errors as quickly as possible. Consequently, although specific errors will always exist in the market economy, we can expect these errors to disappear as new information is generated and individuals adjust to new patterns of prices and profits. If private property rights are well defined and protected and there is a stable monetary framework, the market system will not allow errors to accumulate—crises will be minimized and resources will flow to their highest-valued uses. Under government planning, however, both the lack of a profit/loss test and bureaucratic inertia would slow the adjustment process. Errors would accumulate until a crisis occurs. Government planning would be characterized by politically motivated adjustments to periodic large-scale crises, while market planning would be characterized by continuous voluntary adjustments through a system of markets and prices, which would prevent serious crises. Of course, if the free-market process is impeded by price controls or overregulation, it too will fail to bring about smooth adjustments to changes in the basic economic data.

G. Warren Nutter has considered the above differences between the market adjustment process and government planning as they affect the use of knowledge. According to Nutter: "The effort to impose conformity on the market's multitude of forecasts has many adverse consequences, a serious one being the compounding of probable error. . . . That is, the likely mistake inherent in a centralized forecast will have a more harmful impact on the economy than the variety of mistakes distributed among individual forecasts, since the very spread in the latter, involving overlapping margins of error, generates

thrift—or his parents') are contributing to the common pool of output" (p. 82). Hutt (1936) was apparently the first to use the term "consumers' sovereignty" (see 1975, p. 95, n. 11).

differential market adjustments that diminish average forecasting error over time" (1983, pp. 118–19).

For Nutter, "to predetermine 'growth' is to forestall it" for "[w]e cannot know in advance the 'optimum' way out [of a "jungle of ignorance"] or what lies on the other side. We grope our way forward" (1983, p. 46). Carrying this point further, he states: "There is no mystery as to why efforts to forecast economic structure . . . should fail in complex Western economies. In the West, the great engine of progress has been innovation, which by its very nature cannot be foreseen or planned in detail. The best path of progress is the one that unfolds as the economy moves along . . ." (1983, p. 122).

Given the choice between adjustment mechanisms, Nutter would opt for the market—he sees it not only as a faster adjustment process, but as one that is more responsive to consumer choice and hence more compatible with freedom of choice. In commenting on the Balanced Growth and Economic Planning Act of 1975, which has certain features in common with current cooperativist proposals for industrial policy, Nutter says that if such a scheme were implemented "consumer sovereignty would go out the window. All important economic decisions would be made politically. . . ." And "[p]rivate enterprise might become so weakened and circumscribed that the market itself would cease to be an effective coordinative mechanism" (1983, p. 126).

Because of the grave dangers posed by a movement away from voluntary planning through the market process and toward democratic planning through the political process, Nutter emphasizes that the burden of proof ought to rest with those who want to change the market system. As it stands, "[t]he planners try to place the burden of proof on those who wish to preserve the traditional American economy—and then they rule out all possible proof." But, Nutter argues: "In proposing such a profound and far-reaching transformation of American society, they bear the responsibility for proving that the new order will be better than the one to be displaced" (1983, p. 128).

4. The claim often heard among advocates of an activist industrial policy is that the cost of implementing their policy proposals would not be prohibitive. But this is misleading. Underlying many of the arguments about how inexpensive a cooperativist industrial policy would be is the myth that in a less than fully employed economy, there is a zero opportunity cost for expanding government control over resources. But this argument fails to recognize the nature of opportunity costs: Even at less than full employment, the use of resources by government means that those resources are being diverted

from alternative uses. If these alternative uses are preferred by consumers to the government's uses, there will be a net loss of wealth for consumers; that is, the new industrial policy will have cost society (consumers) more than it is worth.

5. Finally, the notion that a little government intervention does not pose a threat to economic and personal freedoms must be questioned. Both Hayek and Friedman, among others, have shown that once the government interferes in the market process, there is a high probability that further intervention will be necessary to carry out the "plan."[8]

Those who favor a free-market approach to organizing economic activity (or to "planning America") argue that these five points seriously challenge the conventional wisdom that activist industrial policy, or a consensus imposed by the political process, can improve the pattern of development generated spontaneously by the market order. The burden of proof must rest with Reich, Thurow, Iacocca, LaFalce, Rohatyn, and others who propose to change the current system. It is true that the existing system falls short of the free-market ideal, but these individuals wish to move away from, not toward, a more competitive market economy. Market advocates, on the other hand, seek to move closer to a free market by lowering marginal tax rates, getting rid of the regulatory apparatus that stifles innovation, protecting property rights, and enhancing freedom of choice.

Those who favor an activist/cooperativist industrial policy must convince us that the government is superior to the market in satisfying consumer preferences. Otherwise, they must revert to crude arguments for social justice. Of course, it may well be that those arguing for an activist industrial policy do so precisely because they are dissatisfied with the existing distribution of income and would like to impose their ideal of social justice on the market order via the political process. Indeed, the earlier reference to Reich (1983b, p. 20; supra, p. 367) implies that he would readily accept social justice as a public policy goal. Reich is at least being honest, though he naively believes the pursuit of social justice is compatible with (indeed, is necessary for) economic growth.

Once the various arguments for industrial policy are brought into the open, individuals can decide on the type of resource adjustment mechanism they prefer, in full knowledge of the consequences of each. Thus, it is clear that the industrial policy debate is really a debate about the future direction of the U.S. economy. It is a question of whether we want more direction from the center—from

[8]See Hayek (1944, chap. 10) and Friedman (1962, chap. 1).

government, business, and labor—and greater politicization of economic life, or whether we want consumers to direct the economy via their free choices in the marketplace.

The papers in this volume discuss the above issues in detail. Kirzner's paper discusses what he calls the "basic knowledge problem"—"an individual's simple ignorance of the circumstances relevant to his situation"—and shows why this problem has important implications for both central economic planning and industrial policy. He emphasizes the key role profits play in stimulating the entrepreneur to overcome the basic knowledge problem, and shows that government planning—whether comprehensive or more limited—interferes with the "entrepreneurial discovery process." As such, government planning makes it more difficult to deal successfully with the basic knowledge problem. Current proponents of industrial policy, however, seem blissfully ignorant of this problem.

Lavoie draws on the lessons learned from the earlier debates on the possibility of rational economic calculation under socialism to critique the industrial policy proposals of Reich and Rohatyn. He cites both the knowledge problem and the political problem confronting planners; that is, the difficulty of centralizing the information necessary for allocating resources in line with consumers' preferences and the threat to a free society that arises from concentrating economic decision making in a tripartite council or planning board. Lavoie provides an interesting critique of New York City's Municipal Assistance Corporation ("Big MAC"), which Rohatyn uses as an illustration of successful investment planning, and dispells Reich's claim that Japan's Ministry of International Trade and Industry (MITI) provides us with a useful blueprint for planning U.S. economic growth.

DiLorenzo, in commenting on current industrial policy proposals, uses the theory of public choice to derive the implications of substituting bureaucratic decision making for competitive markets. He draws on historical episodes of activist industrial policy (especially the RFC experience) to illustrate the adverse effects of market interventions. He also disproves the notion that the market process is necessarily conflictual while the political process is cooperative. Vieira's paper discusses the impact current industrial policy proposals would have on economic liberties, and explains how constitutional chaos might result if cooperativist proposals were implemented. The consequences of imposing discretionary authority on the market order and disregarding the rule of law are thoroughly discussed here as well.

Pejovich shows that changes in the system of ownership rights and contractual rights affect the incentive to innovate and hence,

economic development. He emphasizes the importance of private property rights and freedom of contract for economic development and argues that true economic development—in line with consumers' sovereignty—is characterized by *voluntary* innovation. Under the Yugoslav system of market socialism, in which no one can acquire private property rights to the flow of innovation but workers have claims to the increased net income from successful innovation as long as they remain employed with their firm, Pejovich finds a stronger incentive to innovate relative to that found in Soviet bloc economies. However, the incentive to innovate in Yugoslav firms will be weaker than that found in private, for-profit firms in the West.

Bartlett draws on economic theory and historical evidence to counter the claim of industrial policy proponents that technological unemployment is a serious problem in a growing economy. According to Bartlett, technological progress, innovation, and capital formation—or anything that increases labor productivity—can only benefit workers in the long run. Because as productivity increases so will real wages and job opportunities. Thus, under private enterprise, Bartlett finds innovation to be job-creating rather than job-destroying.

Brada discusses the experience with industrial policy in Hungary as the economic system moved from Soviet-style central planning in the 1950s to a more decentralized, market-oriented system after the New Economic Mechanism (NEM) was introduced in 1968. In recent years, Hungarian planners have been able to target sectors for development, but the lack of overall success in Hungarian development policy must be attributed to the problems Pejovich discusses in his paper; namely, the lack of private property in the means of production and the limitations on freedom of contract. Without real capital markets, the discipline of bankruptcy and the rewards for successful risk-taking will be absent or greatly reduced; entrepreneurs will then have a weaker incentive to innovate.[9] Brada recognizes the incentive problem in Hungarian enterprises, but also mentions the following sources of inefficiency: the rigidity that is introduced into the economic system by centralized investment and economic planning; the politicization of economic decision making in Hungarian enterprises; the rent-seeking activity that characterizes Hungarian industrial policy; and the inflationary bias in the Hungarian system. On this last point, Brada mentions that Hungarian officials have been reluctant to redistribute investment funds from less productive to more productive enterprises. Instead, the government has financed new investment by creating new money, thus fueling inflation. Brada

[9]For an interesting discussion of this point, see Nutter (1983, chap. 13).

also notes that Hungarian industrial policy has been successful only to the extent it encouraged production of products for which it has a comparative cost advantage. But this is precisely the function of the competitive market process. These are all important lessons for industrial policy advocates in the West.

Sakoh presents a case study of Japanese post-World War II economic growth and addresses four questions: (1) What was the role of the Japanese government in the period of rapid economic growth? (2) What was the extent of targeting and its success? (3) Was investment largely guided by business-government consultation? And (4) What has been the role of the market in the postwar "economic miracle"? He finds that there was a minimum of government intervention; that the high-growth manufacturing sector was not targeted; that private investment provided the bulk of funds for financing economic growth; that private entrepreneurs not government officials made the key investment decisions; and that Japanese economic success can be attributed primarily to a political and economic environment that placed a greater emphasis on individual initiative and market forces. It was the breaking of barriers to social and economic mobility, the low tax rates on capital, the small and balanced budgets, the low rate of inflation, and low interest rates that helped provide the favorable climate for economic growth in postwar Japan. Sakoh concludes that "Japan's success has been in spite of, rather than because of, government tinkering." His paper dispels the myth, therefore, that Japan's economic growth can be attributed to targeting and better government planning.

The papers by Kendrick, Albertine, Niskanen, and Miller consider the problem of lagging productivity growth in key sectors of the U.S. economy and ask how America's competitiveness can be enhanced. Kendrick points out the difficulty of establishing a coherent U.S. industrial policy given the wide variation in the growth of productivity among industries. Some industries will always fall below the economy-wide average productivity growth and others will exceed that average. No one is knowledgeable enough to predict which firms and industries will be above and which below the national average at any point in time. And even if this knowledge were available, no one would know why some industries were advancing and others lagging because the causes of economic growth and decline are too complex. Thus, it makes little sense to try to promote high-growth industries or to target ailing industries. Instead, Kendrick recommends that policymakers concern themselves with establishing a stable framework for the efficient operation of the market process,

which is a proven mechanism for picking winners and disciplining losers.

Albertine advocates breaking the tax and regulatory barriers to U.S. economic growth. He would lower the cost of capital and increase the efficiency of investment by removing the double taxation of corporate income, lowering the capital gains tax, and ultimately abolishing the corporate income tax. He also would undertake regulatory reform and revamp U.S. trade policy to allow smaller, innovative enterprises to compete more successfully in the international marketplace. Niskanen advocates a supply-side industrial policy that would provide for a stable monetary and fiscal policy environment, less regulation, fewer trade barriers, and more secure private property rights so that entrepreneurial talent could be fully utilized for the benefit of consumers.

Miller's paper questions the merits of having an activist industrial policy that attempts to achieve consensus for economic development via tripartite councils. Such a policy ignores the fact that innovation and economic progress require a departure from the status quo. The benefit of the market system is that it rewards those risk-taking entrepreneurs who break with tradition and discover new production methods, and who introduce new and better products to satisfy consumers' preferences at lower opportunity costs than heretofore. Innovation requires foresight; and the profit motive of the market—not the consensus of a tripartite council—would provide the incentive to innovate. Miller thinks the idea of consensus in government-business-labor decision making is overplayed. Given the existing institutional arrangement, the tripartite council would find it very difficult to reach a consensus on development policy. Thus, Miller argues that the consensus claimed by proponents of an activist/cooperativist industrial policy is an illusion. He sees the free-market process as the best way to utilize scarce knowledge and spur economic growth. Finally, he contends that U.S. economic performance has not been as dismal as the critics claim, and that advocates of industrial policy have neither good economic arguments nor good political arguments to buttress their claims against the market.

These papers and the comments by Hurwicz, Roberts, Horvath, Trezise, Rabushka, Milenkovitch, McKenzie, and Yeager are a valuable contribution to the discussion of the key issues surrounding the industrial policy debate and pave the way for further research.

Whether we agree that what lies behind the recent proposals for activist industrial policy is "nothing more sinister than sheer intellectual muddle," or whether we see these proposals as means to override the market process with a political process designed to

achieve social justice, will be determined, in part, by how carefully we analyze the effects of alternative institutional arrangements on economic development.[10] The papers in this volume will assist this process, since they will improve our understanding of the role of property rights in shaping incentives and behavior. We will see that what often appears an innocent proposal turns out to have adverse and unintended consequences for resource allocation and consumers' sovereignty. In the words of Justice Brandeis:

> Experience should teach us to be most on our guard to protect liberty when the government's purposes are beneficial. Men born to freedom are naturally alert to repel invasion of their liberty by evil-minded rulers. The greater dangers to liberty lurk in insidious encroachment by men of zeal, well-meaning but without understanding.[11]

This is sound advice, well worth bearing in mind while considering the effects of government involvement in industry—or any other sector.

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[10]After reading accounts of the evolution of the Balanced Growth and Economic Planning Act of 1975, Hayek concluded, "one feels reassured that nothing more sinister than sheer intellectual muddle is at work" (1978, p. 246). While this may be true of the current efforts for a coherent industrial policy, it is also plausible that more "sinister" motives are at work; namely, motives to redistribute income and property to achieve "social justice." Nevertheless, the "intellectual muddle" argument should not be dismissed. As Buchanan (1983) has emphasized, knowledge of the market process and its institutional requirements is sorely missing from academic training. The low level of understanding of the role of prices and profits, and private property rights in generating an efficient allocation of resources in line with consumers' preferences is certainly evident in the arguments used by proponents of an activist/cooperativist industrial policy.

[11]Olmstead v. United States, 277 U.S. 479 (1928).

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