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Discussion

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Discussion After the Speeches of Peter G. Morici and J. Laurent Thibault

QUESTION, Professor King: One of the problems in connection with the competitiveness situation is the legislative branch. There has been talk that we should have competitive impact statements on legislation that is proposed. I want to ask both of you what you think of the value of that type of approach. Some of these problems require legislation. For example, in terms of taxes, the investment tax credit was wiped out and some of the tax benefits for research and development were more limited. Some of the competitiveness compulsion may have to come from the legislative branch. I want to ask you about the awareness in the legislative branch of this problem and whether we are probing forward or going backwards?

ANSWER, Mr. Morici: It is important to recognize that the problems in this area are very different in the United States than they are in Canada. In Canada it is an issue of an economy one-tenth the size of the U.S. economy being perceived as a favorable location for investment. There we are talking about the environment for investment.

In the United States the problem is very different. For the United States the problem is the lack of savings and the cost of capital. Americans just do not save enough. The tax reform legislation that we had did a terrible job of addressing that problem. We tax nominal interest on savings as opposed to real interest on savings. We treat the inflationary component of a ten year capital gain the same as we would ordinary income. This is not a very good approach. I am not talking about going back to the old tax rate, the capital gains maximum or anything of that nature. The Treasury won the first tax reform proposal that came down from the administration and was going to try to rationalize the process of taxation on savings. Comparison of the U.S. and Canadian experience indicates that that might be a very good approach to take. But when it got over to the legislative branch where they were trying to get the rates down to make compromises here and there, one of the first things that went was the rationalization plan because taxing only the real income from savings and real capital gains looks like a concession to the wealthy as opposed to an investment in wealth creation. It is very difficult for them to accept the notion of taxing only real income on savings as opposed to nominal. It is a basic problem that the administration tends to look at taxation from the point of view of efficiency and the legislative branch tends to look at taxation from the point of view of equity. As we know, those two areas do not necessarily mesh.

COMMENT, Mr. Thibault: In principal the notion of focusing on competitiveness in all public policy is very sound. But in saying that, I would go back to a theme that has been driving us for many years now and that is a very simply "self help is the best help." By and large public policy in Canada is heading in the right direction and we do not have a lot of fundamental problems, other than the areas that I mentioned.

It is important to think that we can solve the problems through public effort, that somehow it is not a government problem. We have a lot of work to do in industry as well and that has to be recognized. It has to be a total effort.

QUESTION, Professor King: One question that occurs to me in connection with Peter Morici's thesis is the question of whether or not the horse is already out of barn on some of these approaches. In other words, are not there certain industries to which so much damage has been done that we perhaps are foreclosed in getting back into the competitive circle?

I assume that your approach would be toward fresh new industries. In terms of the limitation of your prescription, is the patient partially dead in certain areas?

ANSWER, Mr. Morici: It really depends on the industry and within the industry, on the individual firm. If you look at the automobile industry and you look at the changes in market sharing that have taken place, the difference between the performance of Ford and GM has been dramatic. If you look at the difference in the way they approach the problem of making a car, you can start to see why that is the case.

In steel we have new producers that are very effective, the mini mills. Certainly they are not a majority of the steel industry, but soon they will be fifty percent of the industry. It is more than just the fact that they grasp for technology and to some extent their labor is cheaper. A lot of mini mills are unionized. It has to do with the fact that large integrated steel mills did not have the kind of management that IBM or Xerox has. In other industries it is hard to say that a company stays in the same industry. For example, General Electric views itself as being in the business of being in business. GE is a major captial company which is constantly acquiring small new companies and merging industries that are related to its core of business. These blossom, it buys them out, or buys a larger share, and at the same time it is shedding the things that it does not do very well. It seems to me that it depends on the industry. It is just too difficult to generalize about an economy of this size. But it is fair to say that there is still a lot of investment going on and that there just is not an industry where you can point to a couple companies that are not doing very well and say, "Well, there's a model." The question is, are we willing to accept some of the ramifications of this? In some cases it entails regional shifts because the competitors are in different parts the country than the old industry.

In other cases it is a function of accepting things that Americans have told everyone else they should accept for the last twenty years, such as foreign investment. For example, many think there is no analogy in the automobile industry to the mini mill. Basically, we have an old, declining industry that has been unable to reform itself from within and we have a new industry emerging alongside it with a different technology and totally different managers.

Yet, there is an analogy to the mini mill in the automobile industry. It is the Honda factory. Are we willing to accept, as we have asked the Canadians to do all these years, foreign investments and foreign managers running some of our industries when we cannot run them ourselves? It is not that way universally. American multinationals are doing very well abroad. It is that we not only have specialization by country in what we make, we seem to be having specialization by country in what we manage.

QUESTION, Ms. Wheeler: This is for Peter Morici. I agree that we have to make it in the near future in order to be competitive. But I am curious as to what, other than our starting out position in this race, you find advantageous for America. How long do you think it will really take us to make all these idealistic changes you have proposed?

ANSWER, Mr. Morici: I do not view the changes that I am proposing as idealistic. The issue of doing something about education, for example, is one that has been taken up by both Democratic and Republican candidates for President. It has been taken up by this administration. The issue of technology is one that has been taken up by the National Academy of Sciences and by hard-headed businesspersons within their labor and business panels. It took a very long time to get ourselves in the mess that we are in: at least twenty years. So we can look forward to an equally long period to get ourselves out of this mess. But just as things were gradually eroded as we got into the problem, things will gradually get better. We can get out of it if we do improve. The real question is, will we?

In Kennedy's book, *THE DECLINE OF NATIONS*, he talks about societies becoming overextended and getting involved with military commitments abroad, exceeding their industrial capabilities and finding industrial capabilities as the ultimate foundation of one's ability to project power and influence in the world. When you overextend your commitments, you fall into decline. He draws these parallels and lets you draw your own conclusions about the United States. One of the things that he points out is that no society has ever been able to regain the glow of its loss; that each world leading economy in the history of nation states that has experienced this kind of decline has found it impossible to terminate. I do not view it that way. This is the most self-critical society that the world has ever encountered. It is not a society in which people are willing to accept a decline in their role in the world very graciously. There is

a great deal to be optimistic about and the most important element here is the American character.

COMMENT, Dr. McNiven: I just wanted to follow up on Ms. Wheeler's comment. We have a computerized manufacturing plant that just opened a year ago outside of Fairfax, making parts for aircraft engines. First they put it in an area that has what they call the industrial tradition, not unions. They do have a huge plant in Montreal that is highly unionized, but that was not the point. The point was the kind of work force they would get from three or four generations of people used to working a certain way. They made a very big point that they wanted to deal with people in a new way, so it needed new people. We put up a training and installation program at the cost of \$16 million dollars, and we are training people for this plant. Essentially it is a totally automated warehousing facility. When I say totally, there is nobody in it. Little machines go up and get goods and bring it back down to other little machines. Meanwhile, there are a couple people tapping on computers upstairs. Who got jobs?

First you had to have at least two years of university, these are Peter's "blue-collar workers," preferably four in an engineering college. Then you had to go for a nine month training course, then you got the job. The average salary from pushing the broom to head manager is above \$30,000 a year.

Furthermore, the people in each work area not only set their own tasks, they set their own pay packages. They have a budget each year in terms of pay. They take the pay, the holidays, or benefits, but they can mix and match and come up with their own package. When you get into work groups of highly qualified people, they are not really blue-collar workers anymore, but they are really high paid and they produce like mad. It is a very interesting thing that is going on, and this is the wave of the future in terms of plants. There is no other way.

COMMENT, Mr. Epling: I found your remarks strangely negative. I saw an article recently in the paper talking about what economists complain about, and it changes over time. They always complain about something, whether it is inflation rates or interest rates, there is always negation. Twenty years ago I was working in research and development. The complaint about the Japanese then was that they did not invest that much in research and development and they were exploiters of the net sums that we invested in both government and corporation research programs in the world. The Japanese were accused of being exploiters, using the fruits of our investment. Now the argument seems to have flipped to the other side. Now the suggestion is that they spend more than we do.

COMMENT, Mr. Morici: The economists do not do a lot of complaining about Japanese adopting our American technology. Economists tend to take the view that technology information should be open, yet patents and things like that should be protected. I am not complaining about the Japanese. I am saying that we should emulate them, but not in

the way that the advocates of industrial policy say that we should emulate them. There are things that they do very well and one of them is keeping track of what is going on all around the world. They probably understand our own marketplace as well as we do now.

At the National Institute of Health there are 1700 foreign nationals working in research, 400 of them Japanese. The question is, how many Americans are studying engineering abroad?

COMMENT, Mr. Epling: We have probably the finest engineering system beyond a doubt at the graduate level in the world, and medical training, too, for that matter.

COMMENT, Mr. Morici: Our big problem is that we have the slots in the universities in the United States for people to study these disciplines, but we do not have children to go into that.

We are living in a world, as Jim McNiven pointed out, where people have to be numeric. If we want to make things with the technology they use in Taiwan, or in Indonesia, then we need to give students the kind of global system we have spawned. We are going to have to expect to earn the wages that people earn in Taiwan or Indonesia. If we want to earn \$30,000 a year at the factory floor, then we are going to have to be talking about the kinds of workers Jim has just described.

QUESTION, Professor King: I want to ask Larry Thibault one question. You said that one of the solutions for Canada is to upgrade the teaching of science and technology, that you needed more educational backup. Has the Canadian experience been in the past that people move south after they get that type of technological training or do they stay up in Canada and develop up there? I was curious because sometimes we see a brain drain in certain areas where people are pushed southward. What is your forecast on that?

ANSWER, Mr. Thibault: I am not sure I can answer that in detail. Bell-Northern is probably one of the best organizations able to answer that question. The point we were making is that many of our universities now in Canada are severely underfunded. The laboratories are not properly equipped. They do not have the funds required to attract the kind of faculty they need and to really be the center of excellence that we need to have. So that was primarily our point.

COMMENT, Mr. Salembier: I want to accuse Peter Morici of being too negative, too. You paint a picture whereby mature industries of North America are becoming important by default because there will be a comparative advantage increase somewhere. In the case of the automobile industry that was developed and used earlier, the link between that and the quality and quantity of investment that you described is not so strong. In Canada, for instance, last year there was \$1.2 billion in investment in the automobile industry by the American corporations, who have always considered North America one market.

General Motors has state-of-the-art plants and a 200,000 vehicle fa-

cility going into Ontario, which is a joint venture with a Japanese firm. All of these automobile companies have minority positions in Japanese automobile manufacturers. Unless that worries you from a nationalist point of view, that is quite a positive offer. It is not really just by default that these industries, and the automobile industry in particular, is the favorite of industrial decorum in America.

COMMENT, Mr. Morici: The question is, will a mature industry become more important by default or will it become more important because it will become more effective by using reforms and investments? We can name in any sector important examples of where things are being done right or where investment is inadequate. The real question is whether or not investment is adequate and being done right. I do not think that is the case.

The issue is not whether or not the mature industry will become more important, the question is how. That is still a blank page. It can go either way. It depends on how seriously we take changing the way we do business. Some businesspersons have recognized it. GM is so large that generalizing about GM, which I just did for the purposes of brevity, is really not the correct thing to do. Within GM there are some plants that are run very well and there are others that are not doing very well at all, each with the latest technology being available to them.

QUESTION, Professor King: I have one question about defense research and development. Is there any way that some of that could be turned to improve our competitiveness? Is there any public policy that needs to be adopted? For example, we spend a good part of our budget on defense, we do a lot of research, but it does not always turn into something valuable from the standpoint of commerce. Is there more we can do on that?

ANSWER, Mr. Morici: First of all, I do not want to say that the defense research and development does not have commercial benefits. They are there and they are substantial. They are just not as large as those that the money spent for direct commercial purposes produces. There are some things that we can do. For example, in the area of export controls, there are examples of export controls in which American firms in technologies that are only marginally related to defense activities are denied the ability to sell abroad, only to find that their foreign competitors are taking a share of the market away.

An important issue to recognize is that while defense research and development drives up the cost of undertaking research and development throughout the economy by bidding up the cost of science, if we stop undertaking all that research and development in the defense area it would not necessarily move over on a dollar for dollar basis to commercial purposes. It is a more complex problem than that. We need to take away some of the impediments that are presently in the way of achieving commercial benefits. We also need to recognize that creating a good environment, addressing the fundamentals, namely the availability of

young engineers in the same proportion as the population and studying engineering as the Japanese do, and providing the kind of business environment where people are encouraged to invest in research and development is very important. Clearly the cost of capital in the United States is very high, and research and development spending is a capital investment, just like the investment in a machine. You have to achieve a higher rate of return when you have a higher cost of capital to undertake, otherwise you are discouraged from investing. We have to get back to some of those basics, such as having an adequate pool of savings as well as an adequate supply of engineers.

COMMENT, Mr. Epling: There is a peculiar wrinkle in this in terms of the difference between the Canadian and American culture and research and development. You would not think that it has a cultural aspect to it, but there is one. The Canadian university presidents complained loud and long to the Federal Government about the inadequacy of the support for research and development. However, in terms of university funding or public funding for university research and development, Canadian funding is on a par with American funding, a ten to one ratio. Also, the number of recipients of funding in the United States is only about four times as large as it is in Canada. The only conclusion they could come to was that in the peculiar Canadian style where everybody gets a prize, the Canadian research money is doled out very carefully to make sure that all kinds of people, whether they are any good or not, manage to get money because of regional and other considerations. The total dollar amount is not too bad, given the country, but the way it is spread out, everybody got \$49.50 for their research, so not much is getting done.

COMMENT, Professor King: I wanted to thank Larry Thibault and Peter Morici for bringing us into this world of public policies and showing what we have to do to make ourselves more competitive. Their talks meshed well, although there was not any particular coordination beforehand.

