OUR INDUSTRIAL POLICY IS THE F-35

Lockheed photo.

With the news of Donald Trump's deal to keep 1,100 of 2,100 Carrier jobs in Indiana, coastal elites appear to have just discovered tax-supported Midwestern manufacturing jobs, even as they continue to ignore tax-supported defense contractor (manufacturing) jobs.

As best as I can understand it from the details released so far, the deal may be best understood as a mix of typical state-level efforts combined with the leverage of a federal level effort. Over 25% of the jobs saved will be engineer and headquarter jobs — important for retaining technological capacity in the US, but not a big help to blue collar workers.

The package is reportedly substantially similar to one IN Governor and soon to be Vice President Mike Pence already offered.

> UTC agreed to retain approximately 800 manufacturing jobs at the Indiana plant that had been slated to move to Mexico, as well as another 300 engineering and headquarters jobs. In return, the company will get roughly $700,000 a year for a period of years in state tax incentives.
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> Some 1,300 jobs will still go to Mexico, which includes 600 Carrier employees, plus 700 workers from UTEC Controls in Huntington, Ind.

That has commentators on all sides — from economists to Bernie Sanders — complaining that Trump just made it more likely companies will demand bribes to retain US based jobs in the future.

That's of course a fantasy. Companies *already* demand bribes to keep jobs in particular states (or in the US generally).* This is just a typical deal — indeed, it was a typical failed deal until the guy making it became Vice President-elect thanks in part to his new boss' running on making a better deal.

The way companies arbitrage states and countries to get the best deal to preserve jobs is not a good thing — at all. But it's one that must be solved at a systematic level, a point Jared Bernstein made in the WaPo.

> This sort of production cannot be sustained as some sort of non-competitive museum model, where we push back on trade-induced job losses through tax breaks and government contracts. True, governors and mayors commonly dole out such goodies as bribes to factories to settle in one state vs. another, but that's a zero-sum game, and often ends up as a big waste of precious resources. Meanwhile, it's also a game of corporate whack-a-mole. While Trump et al. were brokering this deal, nearby factories were packing up for Mexico.
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> As I recently wrote, we've generally failed to even try to implement a solution to this problem of global competition eroding our manufacturing base. A systemic approach, as opposed to what Trump is up to here, will require reducing our trade deficit in manufactured goods by pushing back against countries that manage their currencies to make our exports expensive and their exports cheap. It will require investments in advanced manufacturing so we can close the wage gap with

> productivity. It will require systemic state and older city economic development of the type economist Tim Bartik describes here and here. It may require direct job creation to employ displaced workers when none of the above comes through.

The key twist on this story, however, is that Carrier was convinced to deal when Trump started threatening that federal contracts with Carrier's parent company, United Technologies, might be at risk if they didn't.

> John Mutz, a former Indiana lieutenant governor who sits on the [Indiana Economic Development Corporation's] 12-member board, told POLITICO that Carrier turned down a previous offer from IEDC before the election. He said he thinks the choice is driven by concerns from Carrier's parent company, United Technologies, that it could lose a portion of its roughly $6.7 billion in federal contracts.
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> "This deal is no different than other deals that we put together at the IEDC to retain jobs, but the fact is that the difference is that United Technologies depends on the federal government for lots of business," Mutz said.

Kevin Drum — while citing a lot of health care and finance jobs (both heavily supported by federal policy) as the true job leaders in Indianapolis — considers the pressure on United Technologies to be an outrage.

> This would be a massive abuse of power, of course, but who wants to take a chance that Trump cares? Probably not UT.

I actually think the deal ought to elicit a more interesting discussion of industrial policy —

the kind of systematic intervention that Bernstein talks about that might actually do something about the hollowing out of America's manufacturing base.

Such a discussion has long been forbidden in American political discourse, in part because the same economists pretending such whack-a-mole bribes haven't become the norm in American political life also pretend that an unfettered "free" market (always defined to include mobile capital and goods, but not labor) will benefit everyone.

Yet even during the period when any discussion of industrial policy has been forbidden, we've had one.

Our industrial policy consists of massive US investments in manufacturing war and intelligence toys that we then sell to foreign governments. When done with Middle Eastern petro-states like Saudi Arabia, that trade goes a long way to equalize our foreign trade deficit, but it contributes directly to instability that then requires us to intervene and build more war toys. That investment in war leads, in turn, to a disinvestment in publicly funded infrastructure that could also provide jobs in the heartland.

The most obvious symbol of our unacknowledged industrial policy is the F-35, a trillion dollar federal investment for a plane that has yet to meet basic requirements, one beset by years of rework. As it happens, one of many causes of problems with the F-35 is big reliability problems with engines used in the plane. That makes those faulty engines, made by United Technologies subsidiary Pratt & Whitney, just another direct taxpayer investment in UTC jobs. Yet reliability problems didn't prevent P&W from getting another contract for the F-35 engine earlier this year. Nor did P & W's provision of attack helicopter technology to the Chinese via a Canadian subsidiary.

Our current industrial policy, you see, feeds so few prime contractors that they are virtually immune from the competition that might pressure them to deliver quality goods. Which leads, in turn, to rework, contract overruns, and contractors walking out of the building with our government's most closely guarded secrets, all with no consequences.

Let's stop pretending (as this piece does) that America's manufacturing, increasingly dominated by the production of war toys, exists in a a real market, shall we?

Once we do that, we might begin to address the diseases of our defense contracting and — more importantly — rediscover the value of investing in other kinds of manufacturing that our country needs to have. Justify these investments by some future defense need, I don't give a damn (though there are military officials who will soberly explain the risks of the hollowing out of our manufacturing base). But invest in the technologies the US needs to stay competitive and retain a manufacturing base.

There was a brief moment when Obama tried to do this by investing in battery factories in MI and other Rust Belt states, an investment justified because the US lagged so far behind South Korea on this critical technology. The investments were badly executed, and then later undermined by the KORUS trade deal. Republicans made them toxic with the Solyndra faux scandal. And so, rather than siting one after another killer app in locales whose older economies had failed, such efforts largely ended.

Imagine how the climate change negotiations might have changed, though, if they came with key investments in alternative energies in coal mining areas of West Virginia and Kentucky?

But this Carrier deal — no matter how much of a gimmick — should be an opportunity to shift the discussion. Trump (and Pence) just federalized the kind of deal every state makes out of desperation, pitting states against each other and Mexico and China. If they can do that, in part by leveraging federal contracting, then they can also pursue an honest industrial policy, one not dependent on selling war toys to our belligerent authoritarian friends overseas.

I doubt Trump will do that. But his Carrier deal ought to at least invite a debate about it.

Update: Added a link to the deferred prosecution for when Pratt & Whitney dodged export restrictions to provide technology to China.

Update: The other day Bloomberg did a review of the Department of Energy's Loan Program Office, which funded Solyndra (but which, as was covered at the time, actually dates to W's Administration) actually has been very successful.

> Not only has the program's loan portfolio generated about $1.65 billion in interest payments to date, its mission to support major energy projects fits into Trump's goal of stimulating investment in the U.S., said Jonathan Silver, a former head of the loan programs office.
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> "The President-elect was talking directly about significant investments in infrastructure," Silver said in an interview Monday at Bloomberg headquarters in New York. The program is intended to support not just clean-energy projects, but also industries Trump championed during the campaign, including coal, among other advanced fossil fuels. "This is infrastructure. It doesn't get any more infrastructure-ish than this."
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> The office dates to the George W. Bush administration and was designed to offer loan guarantees to innovative energy projects that struggle to get financing from commercial and investment banks. In some cases it also approved loans funded through the Federal Financing Bank.

> It supported the first big solar farms in the country and helped commercialize solar-thermal systems, advanced nuclear designs, molten-salt storage and other technologies. It has yet to finance an advanced fossil-fuel project.

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*Disclosure: My spouse works for a manufacturing company often touted, locally and nationally, as a huge success; it receives state tax credits.