National Foundation for American Policy

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Research: Industrial Policy Likely to Harm U.S. Innovation

Arlington, Va. – Using industrial policy to compete with China in technology or for other purposes would likely harm U.S. innovation and leave the United States worse off, according to a new analysis by the National Foundation for American Policy, a nonpartisan policy research organization. The conclusion follows a review of U.S. government policies and the economic literature on industrial policy.

The study, "Industrial Policy and U.S. Innovation," can be found at https://nfap.com/.

Supporters of industrial policy believe trade protection and giving the government an economic planning role will increase innovation and the competitiveness of U.S. companies. The research does not support that conclusion.

Industrial policy has resulted in the use of subsidies, trade protection and a focus on increasing exports. Japan, South Korea and China have been cited as models. However, past experience shows an emphasis on imports and the removal of trade barriers is a better policy.

Economic growth is crucial to enhancing the standard of living in a country. Economic growth "is made up of growth in the workforce plus growth in labor productivity," according to Robert S. Kaplan, president and CEO of the Federal Reserve Bank of Dallas.

Imports increase the growth in labor productivity. That is because competition from foreign companies may increase the quality of domestic companies.

Economists Robert Lawrence and David Weinstein found that in Japan, increased competition from imports of electrical machinery raised productivity in electrical machinery by approximately 35%. "This suggests that competing imports were very important in understanding the success of that sector," according to Lawrence and Weinstein.

"Greater imports of competing products spur innovation," wrote Lawrence and Weinstein. "Our results suggest that competitive pressures and potentially learning from foreign rivals are important conduits for growth." They found similar results examining South Korea and the United States.

The findings argue against industrial policy and protectionism.

Recent examples illustrate the shortcomings of industrial policy include that it cannot be separated from politics. Lacking the discipline of the marketplace, it can result in costly government failures.

The Trump administration and the governor of Wisconsin applauded taxpayer subsidies directed at Foxconn, a manufacturer based in Taiwan, which was supposed to build a factory in Wisconsin and create 13,000 jobs. As Josh Dzieza wrote in *The Verge*. "In exchange for billions in tax subsidies, Foxconn was supposed to build an enormous LCD factory in the tiny village of Mount Pleasant, creating 13,000 jobs. Three years later, the factory – and the jobs – don't exist, and they probably never will."

As the NFAP study illustrates, a review of U.S. government policies and the economic literature on industrial policy should caution policymakers: Using industrial policy to compete with China in technology is likely to harm U.S. innovation.

About the National Foundation for American Policy

Established in 2003, the National Foundation for American Policy (NFAP) is a 501(c)(3) non-profit, non-partisan public policy research organization based in Arlington, Virginia focusing on trade, immigration and related issues. The Advisory Board members include Columbia University economist Jagdish Bhagwati, Ohio University economist Richard Vedder, Cornell Law School professor Stephen W. Yale-Loehr and former INS Commissioner James W. Ziglar. Over the past 24 months, NFAP's research has been written about in the *Wall Street Journal*, the *New York Times*, the *Washington Post* and other major media outlets. The organization's reports can be found at www.nfap.com. Twitter: **@NFAPResearch**

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