

Competitiveness: A Dangerous Obsession

Paul Krugman

THE HYPOTHESIS IS WRONG

IN JUNE 1993, Jacques Delors made a special presentation to the leaders of the nations of the European Community, meeting in Copenhagen, on the growing problem of European unemployment. Economists who study the European situation were curious to see what Delors, president of the EC Commission, would say. Most of them share more or less the same diagnosis of the European problem: the taxes and regulations imposed by Europe's elaborate welfare states have made employers reluctant to create new jobs, while the relatively generous level of unemployment benefits has made workers unwilling to accept the kinds of low-wage jobs that help keep unemployment comparatively low in the United States. The monetary difficulties associated with preserving the European Monetary System in the face of the costs of German reunification have reinforced this structural problem.

It is a persuasive diagnosis, but a politically explosive one, and everyone wanted to see how Delors would handle it. Would he dare tell European leaders that their efforts to pursue economic justice have produced unemployment as an unintended by-product? Would he admit that the EMS could be sustained only at the cost of a recession and face the implications of that admission for European monetary union?

PAUL KRUGMAN is Professor of Economics at the Massachusetts Institute of Technology. His most recent book is *Peddling Prosperity: Economic Sense and Nonsense in the Age of Diminished Expectations* (W. W. Norton).

Competitiveness: A Dangerous Obsession

Guess what? Delors didn't confront the problems of either the welfare state or the EMS. He explained that the root cause of European unemployment was a lack of competitiveness with the United States and Japan and that the solution was a program of investment in infrastructure and high technology.

It was a disappointing evasion, but not a surprising one. After all, the rhetoric of competitiveness—the view that, in the words of President Clinton, each nation is “like a big corporation competing in the global marketplace”—has become pervasive among opinion leaders throughout the world. People who believe themselves to be sophisticated about the subject take it for granted that the economic problem facing any modern nation is essentially one of competing on world markets—that the United States and Japan are competitors in the same sense that Coca-Cola competes with Pepsi—and are unaware that anyone might seriously question that proposition. Every few months a new best-seller warns the American public of the dire consequences of losing the “race” for the 21st century.¹ A whole industry of councils on competitiveness, “geo-economists” and managed trade theorists has sprung up in Washington. Many of these people, having diagnosed America's economic problems in much the same terms as Delors did Europe's, are now in the highest reaches of the Clinton administration formulating economic and trade policy for the United States. So Delors was using

¹ See, for just a few examples, Laura D'Andrea Tyson, *Who's Bashing Whom: Trade Conflict in High-Technology Industries*, Washington: Institute for International Economics, 1992; Lester C. Thurow, *Head to Head: The Coming Economic Battle among Japan, Europe, and America*, New York: Morrow, 1992; Ira C. Magaziner and Robert B. Reich, *Minding America's Business: The Decline and Rise of the American Economy*, New York: Vintage Books, 1983; Ira C. Magaziner and Mark Patinkin, *The Silent War: Inside the Global Business Battles Shaping America's Future*, New York: Vintage Books, 1990; Edward N. Luttwak, *The Endangered American Dream: How to Stop the United States from Becoming a Third World Country and How to Win the Geo-economic Struggle for Industrial Supremacy*, New York: Simon and Schuster, 1993; Kevin P. Phillips, *Staying on Top: The Business Case for a National Industrial Strategy*, New York: Random House, 1984; Clyde V. Prestowitz, Jr., *Trading Places: How We Allowed Japan to Take the Lead*, New York: Basic Books, 1988; William S. Dietrich, *In the Shadow of the Rising Sun: The Political Roots of American Economic Decline*, University Park: Pennsylvania State University Press, 1991; Jeffrey E. Garten, *A Cold Peace: America, Japan, Germany, and the Struggle for Supremacy*, New York: Times Books, 1992; and Wayne Sandholtz et al., *The Highest Stakes: The Economic Foundations of the Next Security System*, Berkeley Roundtable on the International Economy (BRIE), Oxford University Press, 1992.

a language that was not only convenient but comfortable for him and a wide audience on both sides of the Atlantic.

Unfortunately, his diagnosis was deeply misleading as a guide to what ails Europe, and similar diagnoses in the United States are equally misleading. The idea that a country's economic fortunes are largely determined by its success on world markets is a hypothesis, not a necessary truth; and as a practical, empirical matter, that hypothesis is flatly wrong. That is, it is simply not the case that the world's leading nations are to any important degree in economic competition with each other, or that any of their major economic problems can be attributed to failures to compete on world markets. The growing obsession in most advanced nations with international competitiveness should be seen, not as a well-founded concern, but as a view held in the face of overwhelming contrary evidence. And yet it is clearly a view that people very much want to hold—a desire to believe that is reflected in a remarkable tendency of those who preach the doctrine of competitiveness to support their case with careless, flawed arithmetic.

This article makes three points. First, it argues that concerns about competitiveness are, as an empirical matter, almost completely unfounded. Second, it tries to explain why defining the economic problem as one of international competition is nonetheless so attractive to so many people. Finally, it argues that the obsession with competitiveness is not only wrong but dangerous, skewing domestic policies and threatening the international economic system. This last issue is, of course, the most consequential from the standpoint of public policy. Thinking in terms of competitiveness leads, directly and indirectly, to bad economic policies on a wide range of issues, domestic and foreign, whether it be in health care or trade.

MINDLESS COMPETITION

MOST PEOPLE who use the term “competitiveness” do so without a second thought. It seems obvious to them that the analogy between a country and a corporation is reasonable and that to ask whether the United States is competitive in the world market is no

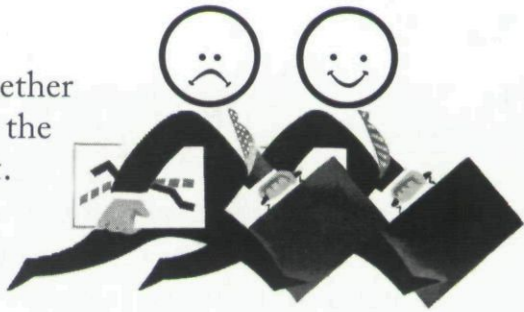
different in principle from asking whether General Motors is competitive in the North American minivan market.

In fact, however, trying to define the competitiveness of a nation is much more problematic than defining that of a corporation. The bottom line for a corporation is literally its bottom line: if a cor-

poration cannot afford to pay its workers, suppliers, and bondholders, it will go out of business. So when we say that a corporation is uncompetitive, we mean that its market position is unsustainable—that unless it improves its performance, it will cease to exist. Countries, on the other hand, do not go out of business. They may be happy or unhappy with their economic performance, but they have no well-defined bottom line. As a result, the concept of national competitiveness is elusive.

One might suppose, naively, that the bottom line of a national economy is simply its trade balance, that competitiveness can be measured by the ability of a country to sell more abroad than it buys. But in both theory and practice a trade surplus may be a sign of national weakness, a deficit a sign of strength. For example, Mexico was forced to run huge trade surpluses in the 1980s in order to pay the interest on its foreign debt since international investors refused to lend it any more money; it began to run large trade deficits after 1990 as foreign investors recovered confidence and began to pour in new funds. Would anyone want to describe Mexico as a highly competitive nation during the debt crisis era or describe what has happened since 1990 as a loss in competitiveness?

Most writers who worry about the issue at all have therefore tried to define competitiveness as the combination of favorable trade performance and something else. In particular, the most popular definition of competitiveness nowadays runs along the lines of the one given in Council of Economic Advisors Chairman Laura D'Andrea Tyson's *Who's Bashing Whom?*: competitiveness is "our ability to produce goods and services that meet the test of international competition while our citizens enjoy a standard of living that is both rising and



A trade surplus may be a sign of national weakness, a deficit a sign of strength.

sustainable." This sounds reasonable. If you think about it, however, and test your thoughts against the facts, you will find out that there is much less to this definition than meets the eye.

Consider, for a moment, what the definition would mean for an economy that conducted very little international trade, like the United States in the 1950s. For such an economy, the ability to balance its trade is mostly a matter of getting the exchange rate right. But because trade is such a small factor in the economy, the level of the exchange rate is a minor influence on the standard of living. So in an economy with very little international trade, the growth in living standards—and thus “competitiveness” according to Tyson’s definition—would be determined almost entirely by domestic factors, primarily the rate of productivity growth. That’s domestic productivity growth, period—not productivity growth relative to other countries. In other words, for an economy with very little international trade, “competitiveness” would turn out to be a funny way of saying “productivity” and would have nothing to do with international competition.

But surely this changes when trade becomes more important, as indeed it has for all major economies? It certainly could change. Suppose that a country finds that although its productivity is steadily rising, it can succeed in exporting only if it repeatedly devalues its currency, selling its exports ever more cheaply on world markets. Then its standard of living, which depends on its purchasing power over imports as well as domestically produced goods, might actually decline. In the jargon of economists, domestic growth might be outweighed by deteriorating terms of trade.² So “competitiveness” could

² An example may be helpful here. Suppose that a country spends 20 percent of its income on imports, and that the prices of its imports are set not in domestic but in foreign currency. Then if the country is forced to devalue its currency—reduce its value in foreign currency—by 10 percent, this will raise the price of 20 percent of the country’s spending basket by 10 percent, thus raising the overall price index by 2 percent. Even if domestic *output* has not changed, the country’s real *income* will therefore have fallen by 2 percent. If the country must repeatedly devalue in the face of competitive pressure, growth in real income will persistently lag behind growth in real output.

It’s important to notice, however, that the size of this lag depends not only on the amount of devaluation but on the share of imports in spending. A 10 percent devaluation of the dollar against the yen does not reduce U.S. real income by 10 percent—in fact, it reduces U.S. real income by only about 0.2 percent because only about 2 percent of U.S. income is spent on goods produced in Japan.

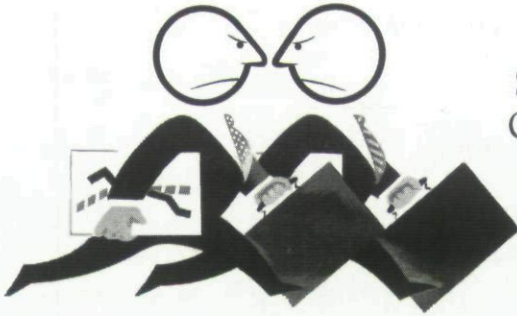
turn out really to be about international competition after all.

There is no reason, however, to leave this as a pure speculation; it can easily be checked against the data. Have deteriorating terms of trade in fact been a major drag on the U.S. standard of living? Or has the rate of growth of U.S. real income continued essentially to equal the rate of domestic productivity growth, even though trade is a larger share of income than it used to be?

To answer this question, one need only look at the national income accounts data the Commerce Department publishes regularly in the *Survey of Current Business*. The standard measure of economic growth in the United States is, of course, real GNP—a measure that divides the value of goods and services produced in the United States by appropriate price indexes to come up with an estimate of real national output. The Commerce Department also, however, publishes something called “command GNP.” This is similar to real GNP except that it divides U.S. exports not by the export price index, but by the price index for U.S. imports. That is, exports are valued by what Americans can buy with the money exports bring. Command GNP therefore measures the volume of goods and services the U.S. economy can “command”—the nation’s purchasing power—rather than the volume it produces.³ And as we have just seen, “competitiveness” means something different from “productivity” if and only if purchasing power grows significantly more slowly than output.

Well, here are the numbers. Over the period 1959-73, a period of vigorous growth in U.S. living standards and few concerns about international competition, real GNP per worker-hour grew 1.85 percent annually, while command GNP per hour grew a bit faster, 1.87 percent. From 1973 to 1990, a period of stagnating living standards, command GNP growth per hour slowed to 0.65 percent. Almost all (91 percent) of that slowdown, however, was explained by a decline in domestic productivity growth: real GNP per hour grew only 0.73 percent.

³ In the example in the previous footnote, the devaluation would have no effect on real GNP, but command GNP would have fallen by two percent. The finding that in practice command GNP has grown almost as fast as real GNP therefore amounts to saying that events like the hypothetical case in footnote one are unimportant in practice.



Countries do not compete with each other the way corporations do.

Similar calculations for the European Community and Japan yield similar results. In each case, the growth rate of living standards essentially equals the growth rate of domestic productivity—not productivity relative to competitors, but simply domestic productivity. Even though world trade is larger than ever before,

national living standards are overwhelmingly determined by domestic factors rather than by some competition for world markets.

How can this be in our interdependent world? Part of the answer is that the world is not as interdependent as you might think: countries are nothing at all like corporations. Even today, U.S. exports are only 10 percent of the value-added in the economy (which is equal to GNP). That is, the United States is still almost 90 percent an economy that produces goods and services for its own use. By contrast, even the largest corporation sells hardly any of its output to its own workers; the “exports” of General Motors—its sales to people who do not work there—are virtually all of its sales, which are more than 2.5 times the corporation’s value-added.

Moreover, countries do not compete with each other the way corporations do. Coke and Pepsi are almost purely rivals: only a negligible fraction of Coca-Cola’s sales go to Pepsi workers, only a negligible fraction of the goods Coca-Cola workers buy are Pepsi products. So if Pepsi is successful, it tends to be at Coke’s expense. But the major industrial countries, while they sell products that compete with each other, are also each other’s main export markets and each other’s main suppliers of useful imports. If the European economy does well, it need not be at U.S. expense; indeed, if anything a successful European economy is likely to help the U.S. economy by providing it with larger markets and selling it goods of superior quality at lower prices.

International trade, then, is not a zero-sum game. When productivity rises in Japan, the main result is a rise in Japanese real wages; American or European wages are in principle at least as likely to rise as to fall, and in practice seem to be virtually unaffected.

It would be possible to belabor the point, but the moral is clear:

Competitiveness: A Dangerous Obsession

while competitive problems could arise in principle, as a practical, empirical matter the major nations of the world are not to any significant degree in economic competition with each other. Of course, there is always a rivalry for status and power—countries that grow faster will see their political rank rise. So it is always interesting to compare countries. But asserting that Japanese growth diminishes U.S. status is very different from saying that it reduces the U.S. standard of living—and it is the latter that the rhetoric of competitiveness asserts.

One can, of course, take the position that words mean what we want them to mean, that all are free, if they wish, to use the term “competitiveness” as a poetic way of saying productivity, without actually implying that international competition has anything to do with it. But few writers on competitiveness would accept this view. They believe that the facts tell a very different story, that we live, as Lester Thurow put it in his best-selling book, *Head to Head*, in a world of “win-lose” competition between the leading economies. How is this belief possible?

CARELESS ARITHMETIC

ONE OF THE REMARKABLE, startling features of the vast literature on competitiveness is the repeated tendency of highly intelligent authors to engage in what may perhaps most tactfully be described as “careless arithmetic.” Assertions are made that sound like quantifiable pronouncements about measurable magnitudes, but the writers do not actually present any data on these magnitudes and thus fail to notice that the actual numbers contradict their assertions. Or data are presented that are supposed to support an assertion, but the writer fails to notice that his own numbers imply that what he is saying cannot be true. Over and over again one finds books and articles on competitiveness that seem to the unwary reader to be full of convincing evidence but that strike anyone familiar with the data as strangely, almost eerily inept in their handling of the numbers. Some examples can best illustrate this point. Here are three cases of careless arithmetic, each of some interest in its own right.

Trade Deficits and the Loss of Good Jobs. In a recent article published in Japan, Lester Thurow explained to his audience the importance of

reducing the Japanese trade surplus with the United States. U.S. real wages, he pointed out, had fallen six percent during the Reagan and Bush years, and the reason was that trade deficits in manufactured goods had forced workers out of high-paying manufacturing jobs into much lower-paying service jobs.

This is not an original view; it is very widely held. But Thurow was more concrete than most people, giving actual numbers for the job and wage loss. A million manufacturing jobs have been lost because of the deficit, he asserted, and manufacturing jobs pay 30 percent more than service jobs.

Both numbers are dubious. The million-job number is too high, and the 30 percent wage differential between manufacturing and services is primarily due to a difference in the length of the workweek, not a difference in the hourly wage rate. But let's grant Thurow his numbers. Do they tell the story he suggests?

The key point is that total U.S. employment is well over 100 million workers. Suppose that a million workers were forced from manufacturing into services and as a result lost the 30 percent manufacturing wage premium. Since these workers are less than 1 percent of the U.S. labor force, this would reduce the average U.S. wage rate by less than $1/100$ of 30 percent—that is, by less than 0.3 percent.

This is too small to explain the 6 percent real wage decline *by a factor of 20*. Or to look at it another way, the annual wage loss from deficit-induced deindustrialization, which Thurow clearly implies is at the heart of U.S. economic difficulties, is on the basis of his own numbers roughly equal to what the U.S. spends on health care every week.

Something puzzling is going on here. How could someone as intelligent as Thurow, in writing an article that purports to offer hard quantitative evidence of the importance of international competition to the U.S. economy, fail to realize that the evidence he offers clearly shows that the channel of harm that he identifies was *not* the culprit?

High Value-added Sectors. Ira Magaziner and Robert Reich, both now influential figures in the Clinton Administration, first reached a broad audience with their 1982 book, *Minding America's Business*. The book advocated a U.S. industrial policy, and in the introduction the authors offered a seemingly concrete quantitative basis for such a policy: "Our

standard of living can only rise if (i) capital and labor increasingly flow to industries with high value-added per worker and (ii) we maintain a position in those industries that is superior to that of our competitors.”

Economists were skeptical of this idea on principle. If targeting the right industries was simply a matter of moving into sectors with high value-added, why weren't private markets already doing the job?⁴ But one might dismiss this as simply the usual boundless faith of economists in the market; didn't Magaziner and Reich back their case with a great deal of real-world evidence?

Well, *Minding America's Business* contains a lot of facts. One thing it never does, however, is actually justify the criteria set out in the introduction. The choice of industries to cover clearly implied a belief among the authors that high value-added is more or less synonymous with high technology, but nowhere in the book do any numbers compare actual value-added per worker in different industries.

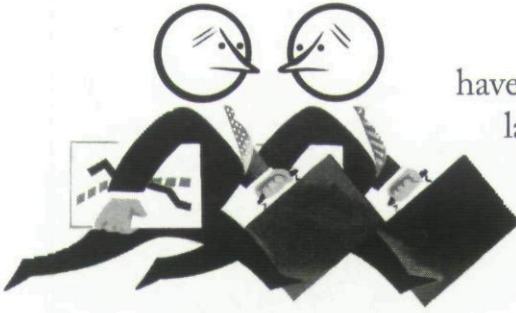
Such numbers are not hard to find. Indeed, every public library in America has a copy of the *Statistical Abstract of the United States*, which each year contains a table presenting value-added and employment by industry in U.S. manufacturing. All one needs to do, then, is spend a few minutes in the library with a calculator to come up with a table that ranks U.S. industries by value-added per worker.

The table on this page shows selected entries from pages 740-744 of the 1991 *Statistical Abstract*. It turns out that the U.S. industries with really high value-added per worker are in sectors with very high ratios of capital to labor, like cigarettes and petroleum refining. (This was predictable: because capital-intensive industries must earn a normal return on large investments, they must charge prices that are a larger markup over labor costs than labor-intensive industries, which means that they

Value Added Per Worker, 1988
(in thousands of dollars)

CIGARETTES	488
PETROLEUM REFINING	283
AUTOS	99
STEEL	97
AIRCRAFT	68
ELECTRONICS	64
ALL MANUFACTURING	66

⁴ "Value-added" has a precise, standard meaning in national income accounting: the value added of a firm is the dollar value of its sales, minus the dollar value of the inputs it purchases from other firms, and as such it is easily measured. Some people who use the term, however, may be unaware of this definition and simply use "high value-added" as a synonym for "desirable."



**Competitiveness advocates are eerily inept
in their handling of the numbers.**

have high value-added per worker). Among large industries, value-added per worker tends to be high in traditional heavy manufacturing sectors like steel and autos. High-technology sectors like aerospace and electronics turn out to be only roughly average.

This result does not surprise conventional economists. High value-added per worker occurs in sectors that are highly capital-intensive, that is, sectors in which an additional dollar of capital buys little extra value-added. In other words, there is no free lunch.

But let's leave on one side what the table says about the way the economy works, and simply note the strangeness of the lapse by Magaziner and Reich. Surely they were not calling for an industrial policy that would funnel capital and labor into the steel and auto industries in preference to high-tech. How, then, could they write a whole book dedicated to the proposition that we should target high value-added industries without ever checking to see which industries they meant?

Labor Costs. In his own presentation at the Copenhagen summit, British Prime Minister John Major showed a chart indicating that European unit labor costs have risen more rapidly than those in the United States and Japan. Thus he argued that European workers have been pricing themselves out of world markets.

But a few weeks later Sam Brittan of the *Financial Times* pointed out a strange thing about Major's calculations: the labor costs were not adjusted for exchange rates. In international competition, of course, what matters for a U.S. firm are the costs of its overseas rivals measured in dollars, not marks or yen. So international comparisons of labor costs, like the tables the Bank of England routinely publishes, always convert them into a common currency. The numbers presented by Major, however, did not make this standard adjustment. And it was a good thing for his presentation that they didn't. As Brittan pointed out, European labor costs have not risen in relative terms when the exchange rate adjustment is made.

If anything, this lapse is even odder than those of Thurow or Mag-

aziner and Reich. How could John Major, with the sophisticated statistical resources of the U.K. Treasury behind him, present an analysis that failed to make the most standard of adjustments?

These examples of strangely careless arithmetic, chosen from among dozens of similar cases, by people who surely had both the cleverness and the resources to get it right, cry out for an explanation. The best working hypothesis is that in each case the author or speaker wanted to believe in the competitive hypothesis so much that he felt no urge to question it; if data were used at all, it was only to lend credibility to a predetermined belief, not to test it. But why are people apparently so anxious to define economic problems as issues of international competition?

THE THRILL OF COMPETITION

THE COMPETITIVE metaphor—the image of countries competing with each other in world markets in the same way that corporations do—derives much of its attractiveness from its seeming comprehensibility. Tell a group of businessmen that a country is like a corporation writ large, and you give them the comfort of feeling that they already understand the basics. Try to tell them about economic concepts like comparative advantage, and you are asking them to learn something new. It should not be surprising if many prefer a doctrine that offers the gain of apparent sophistication without the pain of hard thinking. The rhetoric of competitiveness has become so widespread, however, for three deeper reasons.

First, competitive images are exciting, and thrills sell tickets. The subtitle of Lester Thurow's huge best-seller, *Head to Head*, is "The Coming Economic Battle among Japan, Europe, and America"; the jacket proclaims that "the decisive war of the century has begun . . . and America may already have decided to lose." Suppose that the subtitle had described the real situation: "The coming struggle in which each big economy will succeed or fail based on its own efforts, pretty much independently of how well the others do." Would Thurow have sold a tenth as many books?

Second, the idea that U.S. economic difficulties hinge crucially on

our failures in international competition somewhat paradoxically makes those difficulties seem easier to solve. The productivity of the average American worker is determined by a complex array of factors, most of them unreachable by any likely government policy. So if you accept the reality that our "competitive" problem is really a domestic productivity problem pure and simple, you are unlikely to be optimistic about any dramatic turnaround. But if you can convince yourself that the problem is really one of failures in international competition—that imports are pushing workers out of high-wage jobs, or subsidized foreign competition is driving the United States out of the high value-added sectors—then the answers to economic malaise may seem to you to involve simple things like subsidizing high technology and being tough on Japan.

Finally, many of the world's leaders have found the competitive metaphor extremely useful as a political device. The rhetoric of competitiveness turns out to provide a good way either to justify hard choices or to avoid them. The example of Delors in Copenhagen shows the usefulness of competitive metaphors as an evasion. Delors had to say something at the EC summit; yet to say anything that addressed the real roots of European unemployment would have involved huge political risks. By turning the discussion to essentially irrelevant but plausible-sounding questions of competitiveness, he bought himself some time to come up with a better answer (which to some extent he provided in December's white paper on the European economy—a paper that still, however, retained "competitiveness" in its title).

By contrast, the well-received presentation of Bill Clinton's initial economic program in February 1993 showed the usefulness of competitive rhetoric as a motivation for tough policies. Clinton proposed a set of painful spending cuts and tax increases to reduce the Federal deficit. Why? The real reasons for cutting the deficit are disappointingly undramatic: the deficit siphons off funds that might otherwise have been productively invested, and thereby exerts a steady if small drag on U.S. economic growth. But Clinton was able instead to offer a stirring patriotic appeal, calling on the nation to act now in order to make the economy competitive in the global market—with the implication that dire economic consequences would follow if the United States does not.

Many people who know that "competitiveness" is a largely meaningless concept have been willing to indulge competitive rhetoric precisely because they believe they can harness it in the service of good policies. An overblown fear of the Soviet Union was used in the 1950s to justify the building of the interstate highway system and the expansion of math and science education. Cannot the unjustified fears about foreign competition similarly be turned to good, used to justify serious efforts to reduce the budget deficit, rebuild infrastructure, and so on?

A few years ago this was a reasonable hope. At this point, however, the obsession with competitiveness has reached the point where it has already begun dangerously to distort economic policies.

THE DANGERS OF OBSESSION

THINKING AND SPEAKING in terms of competitiveness poses three real dangers. First, it could result in the wasteful spending of government money supposedly to enhance U.S. competitiveness. Second, it could lead to protectionism and trade wars. Finally, and most important, it could result in bad public policy on a spectrum of important issues.

During the 1950s, fear of the Soviet Union induced the U.S. government to spend money on useful things like highways and science education. It also, however, led to considerable spending on more doubtful items like bomb shelters. The most obvious if least worrisome danger of the growing obsession with competitiveness is that it might lead to a similar misallocation of resources. To take an example, recent guidelines for government research funding have stressed the importance of supporting research that can improve U.S. international competitiveness. This exerts at least some bias toward inventions that can help manufacturing firms, which generally compete on international markets, rather than service producers, which generally do not. Yet most of our employment and value-added is now in services, and lagging productivity in services rather than manufactures has been the single most important factor in the stagnation of U.S. living standards.

A much more serious risk is that the obsession with competitiveness will lead to trade conflict, perhaps even to a world trade war.

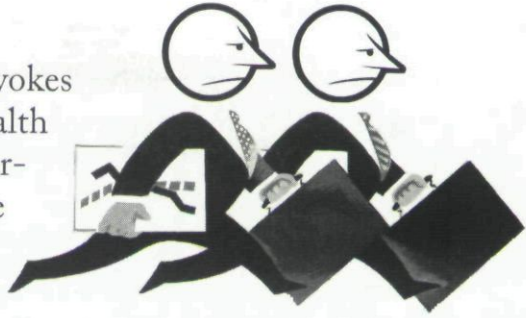
Most of those who have preached the doctrine of competitiveness have not been old-fashioned protectionists. They want their countries to win the global trade game, not drop out. But what if, despite its best efforts, a country does not seem to be winning, or lacks confidence that it can? Then the competitive diagnosis inevitably suggests that to close the borders is better than to risk having foreigners take away high-wage jobs and high-value sectors. At the very least, the focus on the supposedly competitive nature of international economic relations greases the rails for those who want confrontational if not frankly protectionist policies.

We can already see this process at work, in both the United States and Europe. In the United States, it was remarkable how quickly the sophisticated interventionist arguments advanced by Laura Tyson in her published work gave way to the simple-minded claim by U.S. Trade Representative Mickey Kantor that Japan's bilateral trade surplus was costing the United States millions of jobs. And the trade rhetoric of President Clinton, who stresses the supposed creation of high-wage jobs rather than the gains from specialization, left his administration in a weak position when it tried to argue with the claims of NAFTA foes that competition from cheap Mexican labor will destroy the U.S. manufacturing base.

Perhaps the most serious risk from the obsession with competitiveness, however, is its subtle indirect effect on the quality of economic discussion and policymaking. If top government officials are strongly committed to a particular economic doctrine, their commitment inevitably sets the tone for policy-making on all issues, even those which may seem to have nothing to do with that doctrine. And if an economic doctrine is flatly, completely and demonstrably wrong, the insistence that discussion adhere to that doctrine inevitably blurs the focus and diminishes the quality of policy discussion across a broad range of issues, including some that are very far from trade policy per se.

Consider, for example, the issue of health care reform, undoubtedly the most important economic initiative of the Clinton administration, almost surely an order of magnitude more important to U.S. living standards than anything that might be done about trade

policy (unless the United States provokes a full-blown trade war). Since health care is an issue with few direct international linkages, one might have expected it to be largely insulated from any distortions of policy resulting from misguided concerns about competitiveness.



Competitiveness risks distorting the quality of domestic economic policy.

But the administration placed the development of the health care plan in the hands of Ira Magaziner, the same Magaziner who so conspicuously failed to do his homework in arguing for government promotion of high value-added industries. Magaziner's prior writings and consulting on economic policy focused almost entirely on the issue of international competition, his views on which may be summarized by the title of his 1990 book, *The Silent War*. His appointment reflected many factors, of course, not least his long personal friendship with the first couple. Still, it was not irrelevant that in an administration committed to the ideology of competitiveness Magaziner, who has consistently recommended that national industrial policies be based on the corporate strategy concepts he learned during his years at the Boston Consulting Group, was regarded as an economic policy expert.

We might also note the unusual process by which the health care reform was developed. In spite of the huge size of the task force, recognized experts in the health care field were almost completely absent, notably though not exclusively economists specializing in health care, including economists with impeccable liberal credentials like Henry Aaron of the Brookings Institution. Again, this may have reflected a number of factors, but it is probably not irrelevant that anyone who, like Magaziner, is strongly committed to the ideology of competitiveness is bound to have found professional economists notably unsympathetic in the past—and to be unwilling to deal with them on any other issue.

To make a harsh but not entirely unjustified analogy, a government wedded to the ideology of competitiveness is as unlikely to make good economic policy as a government committed to creationism is to

make good science policy, even in areas that have no direct relationship to the theory of evolution.

ADVISERS WITH NO CLOTHES

IF THE OBSESSION with competitiveness is as misguided and damaging as this article claims, why aren't more voices saying so? The answer is, a mixture of hope and fear.

On the side of hope, many sensible people have imagined that they can appropriate the rhetoric of competitiveness on behalf of desirable economic policies. Suppose that you believe that the United States needs to raise its savings rate and improve its educational system in order to raise its productivity. Even if you know that the benefits of higher productivity have nothing to do with international competition, why not describe this as a policy to enhance competitiveness if you think that it can widen your audience? It's tempting to pander to popular prejudices on behalf of a good cause, and I have myself succumbed to that temptation.

As for fear, it takes either a very courageous or very reckless economist to say publicly that a doctrine that many, perhaps most, of the world's opinion leaders have embraced is flatly wrong. The insult is all the greater when many of those men and women think that by using the rhetoric of competitiveness they are demonstrating their sophistication about economics. This article may influence people, but it will not make many friends.

Unfortunately, those economists who have hoped to appropriate the rhetoric of competitiveness for good economic policies have instead had their own credibility appropriated on behalf of bad ideas. And somebody has to point out when the emperor's intellectual wardrobe isn't all he thinks it is.

So let's start telling the truth: competitiveness is a meaningless word when applied to national economies. And the obsession with competitiveness is both wrong and dangerous. 🌐

The contents of *Foreign Affairs* are protected by copyright. © 2004 Council on Foreign Relations, Inc., all rights reserved. To request permission to reproduce additional copies of the article(s) you will retrieve, please contact the Permissions and Licensing office of Foreign Affairs.