development by three to one. Its research laboratories in both industry and the universities are second to none.

Where the United States falls on its face, he argues, is in quickly translating basic research into "products and processes for designing, manufacturing, marketing and distributing such products." Experience seems to bear this out. American scientists invented the transistor, but in 1953 Western Electric licensed the technology to Sony. The rest is history. In 1968, another U.S. firm, Unimation, licensed industrial robot technology to Kawasaki Heavy Industries. And who has heard of Unimation since? During the year ending in March 1987, Reich reports, Japanese firms spent $1 billion to buy technological information in the United States; U.S. firms spent less than half as much in Japan. Between 1956 and 1978, Japanese firms paid $9 billion for technologies that cost between $500 billion and $1 trillion to develop.

Reich just happens to have a handy six-point program to turn things around. U.S. industry must search the globe for inventions with commercial potential, and it must learn to integrate the work of laboratory and factory floor more effectively. Washington must work harder to make the fruits of government research and development available to industry, and it must set uniform technical standards for new technologies, such as high-definition television, so that corporate research efforts are not wasted. Finally, government must invest more in basic education and industry must invest more in worker training. Unfortunately, these are not strategies that lend themselves to headlines and ballyhoo. And that, Reich says, "may prove to be the major stumbling block."

Corporate Makeover

"Eclipse of the Public Corporation" by Michael C. Jensen, in *Harvard Business Review* (Sept.–Oct. 1989), Boston, Mass. 02163.

The boom in leveraged buyouts (LBOs) and other kinds of corporate takeovers has provoked cries of outrage in the executive suites of the *Fortune* 500 and even in Congress. Now, from the Harvard Business School, the high church of corporate capitalism, comes a lusty cheer.

The publicly-held corporation, declares Jensen, a Harvard professor of business administration, "has outlived its usefulness." We are in the midst of a massive restructuring of the U.S. economy.

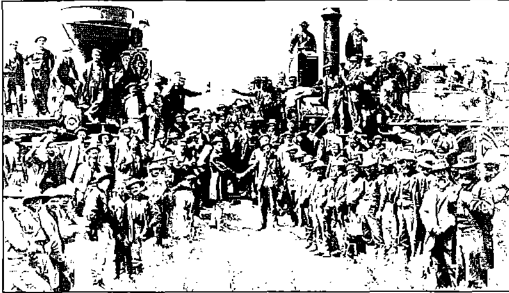
The chief agent of change is the LBO; the chief result is that large corporations whose stock was once traded on the nation's stock exchanges are "going private." In 1988 alone, the $77 billion of LBOs (mostly financed by "junk bonds") shrank the supply of stock in public corporations by 2.5 percent.

Behind it all is not the greed of buyout artists like TWA's Carl Icahn or Wall Street investment banks, Jensen argues, but the "widespread waste and inefficiency of the public corporation and its inability to adapt to changing economic circumstances." Because the owners of stock in big publicly-held corporations can rarely supervise their investments effectively, corporate managers have grown fat and lazy. They have ignored stockholders' interests. Thus, Ford Motor Company executives have hoarded an amazing $10.5 billion war chest. It ought to be distributed to shareholders, Jensen says, but Ford executives are sure to use it for "diversification," otherwise known as empire building. The reason is simple. In Corporate America, executive pay, perks, and prestige are linked to corporate size rather than to corporate performance.

How do LBO's help? Jensen maintains that the substitution of "junk bond" debt for stock changes everything for the better. The need to meet payments "creates the crisis atmosphere managers require to slash unsound investment programs, shrink overhead, and dispose of assets that are more valuable outside the company."

And since executives in privately-held companies have bigger ownership stakes in the business, rewards are more strongly

linked to performance. Finally, bloated bureaucracies are reduced. In 1988, when Kohlberg Kravis Roberts took RJR Nabisco private in a $25 billion deal, RJR Nabisco's entire 470-person headquarters was replaced by 16 professionals and 44 support personnel at KKR.



During the late 19th century, the creation of railroads and other capital-hungry enterprises spurred the rise of the public corporation.

Jensen says that LBOs make the most sense in mature industries—such as steel, chemicals, broadcasting, and brewing—where little further investment can be justified. Public stock ownership still makes sense in fast-growth sectors where opportunities outstrip company resources, such as computers and pharmaceuticals.

Private ownership of industry helped propel West Germany and Japan to economic success, Jensen believes. And today's corporate revolution in the United States is essential to meet their challenge.

Rich and Stupid

"Problems and Non-Problems in the American Economy" by Herbert Stein, in *The Public Interest* (Fall 1989) 1112 16th St. N.W., Washington, D.C. 20036.

All political discussion in America today seems to begin and end with the "twin deficits"—the U.S. budget and trade deficits. Nobody seems to know exactly why they are bad, observes Stein, an economist at the American Enterprise Institute and chairman of the Council of Economic Advisers under President Ford. "The fact that they are called 'deficits' seems sufficient."

Not to Stein. Our obsession with these two "non-problems," he argues, has led us to overlook larger issues.

He is particularly dismissive of the $95 billion trade deficit. During the early 1980s, people worried that the trade deficit would depress U.S. output and employment. That proved false. Now people worry that foreigners are "buying up" America. But capital is flowing into the United States because of attractive investment opportunities here that exceed U.S. savings. "It is as natural that we should import capital from countries that are good at saving," Stein remarks, "as that we should import coffee from countries that are good at producing coffee."

Some people insist that foreign capital is merely financing the U.S. budget deficit. Wrong again, according to Stein. Even if foreign investors underwrite $60 billion of the $115 billion budget deficit, that only means that $60 billion of U.S. investors' money is freed for productive investments.

Well, some may persist, if foreign investments don't break us today, then paying the interest and dividends on them eventually will. In fact, Stein responds, foreign investments generate the income to pay those bills. And the United States still earns more from its overseas investments than it pays out to foreigners who have invested here.

Finally, some worry that the trade deficit reflects declining U.S. "competitiveness." Strictly speaking, this is not true either. Taiwan's industrial productivity is far lower than ours, yet it has a substantial $10 billion trade surplus with us.

So what is the "real" problem? In Stein's view, it is the growing American taste for consumption rather than saving, which dropped from about 17 percent of GNP in 1980 to 14 percent in 1988. As a result, we are underinvesting in business, in education, in help for the poor, in national defense—in real "competitiveness." Lost in today's dead-end debates is the fact that the current low tax/big budget deficit regime increases consumption and depletes savings. Stein's prescription: Raise taxes.