

Racing to the Top: Building and Preserving Assets in a Global Economy

Robert Reich - November 2005

More permeable borders seem to make it more difficult for a nation to maintain a mixed economy, regulate capital in the public interest, provide decent wages, and foster a political coalition to defend all of the above. Indeed, there is an extensive conservative literature contending that the global market renders the role of the state moot, and good riddance. Yet it remains entirely possible to maintain a domestic social contract while developing a robust internationalism with rules that benefit everyone, not just the elite, and to build a wealthy and competitive nation that boasts the most productive citizens on the planet.

Global commerce in goods and services does make it easier for a dominant elite in Washington to pursue its preferred brand of laissez-faire and seek to remake America into a low-tax, low-regulation, low-wage nation. All of it seems to be happening by chance – but, of course, specific policy choices are driving it.

Financial capital, abetted by laissez-faire rules, is becoming ever more footloose, while governments are rooted in particular places. This asymmetry enables global owners of capital to conduct bidding wars, playing off one country, state, or locale against others in an international race to the bottom. In this race, countries with higher taxes and more public services — as well as higher wages and higher labor standards — are put at a competitive disadvantage, all other things being equal. Global financial players can (or credibly threaten to) park their profits where taxes, wages, and regulatory requirements are lowest or nonexistent.

The result is a downward spiral: As tax bases shrink, the government cannot deliver high-quality services. The successful secede, demand even lower taxes, and the ranks of secessionists grow. The cycle is magnified by revenue cuts cascading from the federal government to states and local governments, further eroding tax bases, and imposing particularly large costs on poor communities with already small tax bases. The downward spiral occurs in too many locales, dispersed all over the nation, for the citizenry to see the pattern and to draw the connections. All the public knows is that government no longer seems to work. The current administration, rather than leaning against these trends, is serving as their enabler.

The United States finds itself in ever more intense competition with every other nation to attract and hold capital, a strategy that provides no means of maintaining high living standards for its citizens. If nothing is done to reverse the strategy, the public sector will eventually shrink to the point that it can do almost nothing other than defend the nation. Most of what is now provided by government will be turned over to the private sector, available to individuals depending on their ability to pay. The wages and benefits of ordinary workers will continue to drop. Economic security will vanish as individual incomes will depend on continuous spot auction bids for each individual's services. At some point, as capital and labor move ever more freely across the nation's borders, the spectrum of exceedingly rich to exceedingly poor in the United States (and other nations) will exactly reflect the widest spectrum of wealth and poverty in the world. American society will be sharply sorted and pulled apart. But there is an alternative strategy by which we can embrace globalization and at the same time maintain a high, broadly distributed standard of living. It's a strategy that builds and preserves the assets of the nation and its citizens.

One place to begin would be by reversing the game by which corporations play off nation-states in a competition to reduce taxes. The United States could collaborate through "capital treaties" with Europe and Japan in order to prevent zero-sum payoffs to corporations and investors, as the European Union already does internally. The federal government would prevent states and locales from striking their own separate deals with global capital. We would further agree with other advanced nations to refrain from competitive rounds of tax cuts in order to attract capital, and would enter into a tax treaty for preventing offshore tax havens.

We also need international agreements on behalf of tighter, rather than looser, social and economic regulation. Again, the European Union does this on one continent. In Europe, the cushion of a strong welfare state coupled with public investment seems to be the political price the electorate demands in exchange for tolerating the vagaries of the open economy, where jobs are always at risk. If the advanced nations got together to recreate the mixed and regulated brand of capitalism that we have fought for in many of our individual societies, trade agreements would reflect the importance of social and environmental regulations. Goods, services, and capital would still flow plentifully across international boundaries, but social rights would have equal place with property rights.

In short, the best way to prevent a race to the bottom among advanced nations is to call off the race. In this “Great Common Market,” as we might call it, global companies would no longer be able to play one jurisdiction against another because access to virtually all the advanced economies of the world would require that they play by common rules that balanced property rights against social rights. As a result, tax revenues collected from corporations and wealthy investors would increase substantially. Hence the second part of the strategy: Those revenues would be invested in the productive capacities of Americans.

With adequate revenues for social investment, we would create first-class schools with small classes and well-paid and highly skilled teachers, even in the poorest of communities. Working families would be able to give their preschoolers high-quality early-childhood education. We would invest in our great public universities and research institutions in order to maintain their leadership in the world. Workers who lost their jobs because of global competition would have a system of wage insurance and retraining opportunities, with income assistance during retraining. The infrastructure that connects our people and improves our productivity – highways, ports, public transportation, energy grids – would be kept up to date. And every American would have access to at least a minimum quality of health care, not only because that is the right thing to do but also because it would enable more of our people to lead full and productive lives.

In this way, the essential strategy for attracting and keeping global capital would be to become more productive rather than to lower our wages and standards and cut taxes on capital. Global investors would still get a sufficiently high rate of return to be fully satisfied, thanks to high and rising productivity. This two-pronged approach – seeking collaboration among advanced nations to avoid zero-sum games and races to the bottom, while investing revenues in the productivity of our citizens – is, of course, the exact opposite of the prevailing orthodoxy. Ultimately, that prevailing orthodoxy will wreck American society. But although alternatives are painfully absent from public debate, the current model is not the only possible form of globalism.

We need a globalism that promotes a race to the top to build and preserve assets and opportunity. This kind of globalism is sound policy – and, with some leadership, it could be good politics.

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