

Real Economy Support by the United States in Response to the Economic Crisis

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Why an Industrial Strategy (policy)?

Three Reasons Why Governments today need to have an Industrial Strategy (policy):

1. There is more capacity than demand globally,
2. Underemployment requires wisely positioning existing industries and supporting industries of the future, and
3. Other countries are doing it.

Observation

Economic Theory

must give way to

Economic Strategy

Four Elements of an Industrial Strategy

1. Policy
2. Decisions
3. Execution
4. Managing and Exiting the investments

Applying the Four Elements to the US Auto Industry

1. Policy

- Confusing
- Most likely – the US must have a strong manufacturing industry to remain a super power.

2. Decision

- The US Auto industry is essential to maintain a strong manufacturing industry.
- Chrysler and GM will fail without urgent and significant government support.

Applying the Four Elements to the US Auto Industry (continued)

3. Execution

- Must make fundamental changes for financial support.
 - Shareholders must be wiped out
 - Most of Top management must change
 - Restructured company must have low leverage and strong business prospects
 - President Obama “We will not simply kick the can down the road.”

Applying the Four Elements to the US Auto Industry (continued)

- Top outside professional brought into US Treasury to form Auto Industry taskforce.
- Must use Chapter 11 to accomplish goal . . . Very quick Chapter 11
- Result was US government owned 60% of the new GM and 80% of the new Chrysler

Applying the Four Elements to the US Auto Industry (continued)

4. Managing and Exiting the Investments

- No active management by the US government
- Appoint strong independent directors
- Execute the equity positions “as soon as possible”.

Observations – Auto Bailout

1. Policy unclear

- Will other industries receive same treatment?
- Who will decide?
- Will auto industry be supported at any cost?

2. Decisions sound

- Good to focus on industries, not simply on a company or companies.
- Ford does not appear to be hurt by the support to Chrysler and GM

3. Execution Excellent

- Real fix, not simply given money to fix balance sheet and cash flow.

Observations (continued)

4. Managing and Exiting the Investments – Challenging
 - Will there be continuity of team...many independent professionals have left.
 - Congressional oversight Committee – should put interests in an independent trust, similar to AIG, to avoid conflicts.

Example of US Support of a Growth Industry of the Future – Electric Vehicles

Three key provisions of the American Recovery and Reinvestment Act of 2009 (“ARRA”)

1. Battery development

- 2 billion dollars of grants
- Ion batteries, hybrid electric systems, component manufactures and software designers

2. 30% tax credit for manufacturing facilities for electric / hybrid batteries

3. Tax credit for vehicle purchase

- Hybrid plug in
 - \$2,500 – \$7,500
 - First 200,000 vehicles
- Slow electric vehicles, 2 and 3 wheel electric vehicles
10% up to \$2,500

Policy to Support Investment in Electric Vehicles

1. Large potential market
2. Battery technology is key to success
3. High-tech manufacturing that can be done in the US
4. US can lead research and development
5. US assistance essential to build industry before the market develops

A Few Observations Regarding Industrial Strategies

1. Successful execution requires collaboration of government, industry, banks and the academic community.
2. Support at the highest political level is important.
3. Danger: Do not chase failed strategies
4. Governments must enter to help and exit to preserve.

Note: I recommend the following paper: “Industrial Policy for the Twenty-First Century” by Dani Rodrik, Harvard University; September 2004