ARTNeT Symposium

"Towards a Return of Industrial Policy?"

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Summary of discussions

by

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The purpose of this note is to draw lessons for policymakers and for the ARTNeT from the discussions on industrial policy meeting held in Bangkok on 25 and 26 July 2011.

Any discussion on industrial policy in the Asia-Pacific region ought to start with a caveat. That is, while this subject may "be back" for some, to others it "never left." In this respect, this region has probably given more credence to industrial policy for longer than others. Still, the profile of industrial policy has risen over the past few years.

One reason for that greater profile is the fallout from the global financial crisis on the "battle for ideas." Each major economic crisis has the potential to undermine the credibility of the reining policymaking orthodoxy. In present circumstances, this probably amounts to the final nail in the coffin of the Washington Consensus. Policymakers are looking for alternative schema around which to organise economic development strategies, and industrial policy seems to signal an intention to intervene in markets more often, but not necessary to replace all markets with state allocation of resources.

Listening to some of the participants at the ARTNeT symposium, who are echoing similar comments made by senior policymakers, the search for an alternative paradigm may be driven by other factors too. As labour forces expand more quickly, and productivity growth limits employment growth in agriculture and manufacturing, increasingly the service sector is being called upon to absorb more employees. But somehow the service sector is seen as being less respectable than manufacturing, and industrial policy is seen effectively as bolstering the latter. Policy failures here are really important as growing unemployment is a recipe for political instability, as events in the Middle East and North Africa have shown this year.

What is for sure is that the service sector is far less well understood than agriculture and manufacturing. Some might ask what's different about services and that's a good question to ask. Still, no country has ever made promoting high quality services as the principal driver of its development and, without precedents, no doubt policymakers are nervous about the role of the tertiary sector. There is a substantial knowledge gap here which the ARTNeT community and others could fit. Knowing how to stimulate productivity growth in the service sector would take the "manufacturing versus services" debate forward, certainly beyond the recent debate between Professors Bhagwati and Chang.

Having established the importance of industrial policy in development policymaking, I now turn to certain aspects of industrial policy that are deserving of comment. The first comment relates to the objectives of **industrial policy**. Having listened to participants' interventions I am quite worried about whether we are expecting industrial policy to deliver too much. There seems to be no limit to the objectives that governments have attributed to industrial policy. Some of those objectives are vague, even if they are very popular. "Inclusive growth" being a good example of the former. Objectives should be clearly stated and related to observable outcomes.

Moreover, having multiple objectives inevitably creates trade-offs in implementation and evaluation. There are no guarantees that officials or the private sector will treat each objective with equal attention. Nor is it easy to come to an assessment of a policy measure that delivers on one criteria but not the other. Just because the world is a complicated place doesn't provide the rationale for a laundry list of objectives. Focus has plenty of advantages.

Another way to think about the legitimate objectives of industrial policy is to ask what problem an initiative seeks to correct. As Professor Deardorff showed in his presentation it could relate to a market failure. Or it could relate to dynamic economies of scale. I would add that missing markets--essentially the core of any concern about inadequate financing of small and medium sized enterprises--to the list. Knowing which problem to fix also raises the question as to just how far current outcomes fall below the desirable and what the knock on effects of sub-par performance are. Governments may not be able to fix every problem, they need to know which problems are paramount. One doesn't get the sense that such prioritisation is very common.

Many important matters relating to the **implementation of industrial policy** could have received greater attention. The information necessary to successfully implement such policies is a case in point, as misleading or incorrect information is unlikely to lead to good outcomes. Moreover, the fact that governments have alternatives in implementing industrial policy implies that sensible policymaking needs to contrast across alternatives. In this regard it was disturbing that some speakers erroneously assumed that industrial policy provides a general rationale for discriminating against foreign commercial interests. A case for intervention is not necessarily a case for restricting foreign commerce. Governments should be encouraged to adopt the most effective and least costly measures and this requires careful analysis.

One concern that was hinted at in presentations was that industrial policy could benefit some interest groups that, in turn, will organise themselves to retain the policy measure even if circumstances evolve, as they inevitably do. Industrial policy should not become a tool of entrenched incumbents. Nor of those government ministries responsible for their implementation. Reviews of industrial policy, conducted at regular intervals by technocrats, are required.

The availability of alternative market mechanisms to fix identified problems is another important lesson. If the upgrading of firms is to be encouraged, then **more vigorous competition between firms** is an alternative to offering a subsidy. Several participants noted the importance of promoting competition within their economies, without considering the extent to which this step might be preferable to other forms of state of intervention. Once again this highlights the importance of comparing policy alternatives at the time of implementation as well as conducting ex-post evaluations to assess the effectiveness of implemented measures.

With respect to **ex-post evaluations of industrial policy interventions**, there is a major knowledge gap here. Much of the literature that claims to show industrial policy has been effective in the Asia-Pacific region shows no such thing. Is it one thing to show that governments intervened---it is quite another to show that that intervention had its intended effects. Proper quantitative assessments are needed here and these assessments should take account of all of the other relevant factors, so that any success is not incorrectly attributed to the industrial policy interventions under consideration. Insisting on such assessments on a regular basis is essential if industrial policy measures are to deliver on their promise. Forcing proponents of industrial policy to specify precisely what constitutes success--in measurable terms--over what timeframe would focus minds. Without such assessments, the potential for waste is substantial.

Finally, it became clear during the discussions that the **substantial knowledge gaps** concerning industrial policy imply that there are no ready off-the-shelf recipes for success. Descriptions of government initiatives are not enough, we need to know what government objectives can be met by which policies. We need to know when to intervene directly into markets or whether to intervene to alter how the markets architecture and so how firms compete. Given the totemic status given to industrial policy by many in this region the existence of such knowledge gaps may come as a surprise. Worse, while those gaps clearly exist for manufacturing, our understanding of how to derive greater benefits from service sector growth for development is desultory. Much remains to be done to identify policy packages that will deliver for the Asia-Pacific region in the 21st century.