

MUTING OF EXPECTATIONS:  
SOME CURRENT HETERODOX  
THINKING  
ON  
INDUSTRIAL POLICY

# Introduction

- Thought leadership piece
  - Access to new thinking
  - Exposure to new ideas
  - Prompting new questions
  - Interesting pragmatic and practical examples
- Date for new is post 2007
  - NIPF comes into effect
  - Financial crisis

# Outline

- Point of Departure
- Foundation work of Mann, Wade and Evans
- New Heterodox thinking of Kholi, Khan and Chang
- New work around ideas
  - 2<sup>nd</sup> best institutions
  - Island of excellence
  - Joint discovery – IP as process

# Point of Departure

- 1980's and 1990's about understanding the South East Asian Industrial Policy success story
- 2000's – trying to understand unsuccessful IP based on SEA model in Latin America and Africa
- 2 groupings of underperformance literature:
  - New Global Order Literature
  - Statehood literature

# New Global Order

- Causality and logic remain but operating environment so changed that cant use SEA countries as blue print or benchmark or road map
- 5 Biggest changes:
  - Increased globalisation and production sharing
  - Dilemmas of the food, fuel and financial crisis
  - Climate change
  - Shrinking policy space
  - Asian Drivers

# Additional Post 2007 change

- Washington consensus finally admits that all nations undertake IP
  - Heterodox economists can refocus away from justification towards fine grained content and pragmatic suggestions
  - IP becomes normalised

# Foundations (1)

Mann  
Wade  
Evans



Kholi  
Khan  
Chang



Work Around Idea

## MANN:

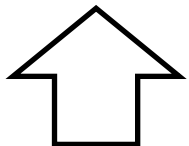
State Power

Despotic  
Power

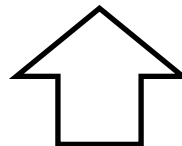
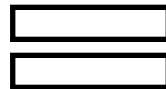
Infrastructural  
power

Power of state over  
Society i.e.:  
Non state actors

Organs, channels and mechanisms  
Of state to pursue goals and plans



**DESPOTIC POWER**



**AUTONOMY OF ACTION**

# Foundations (2)

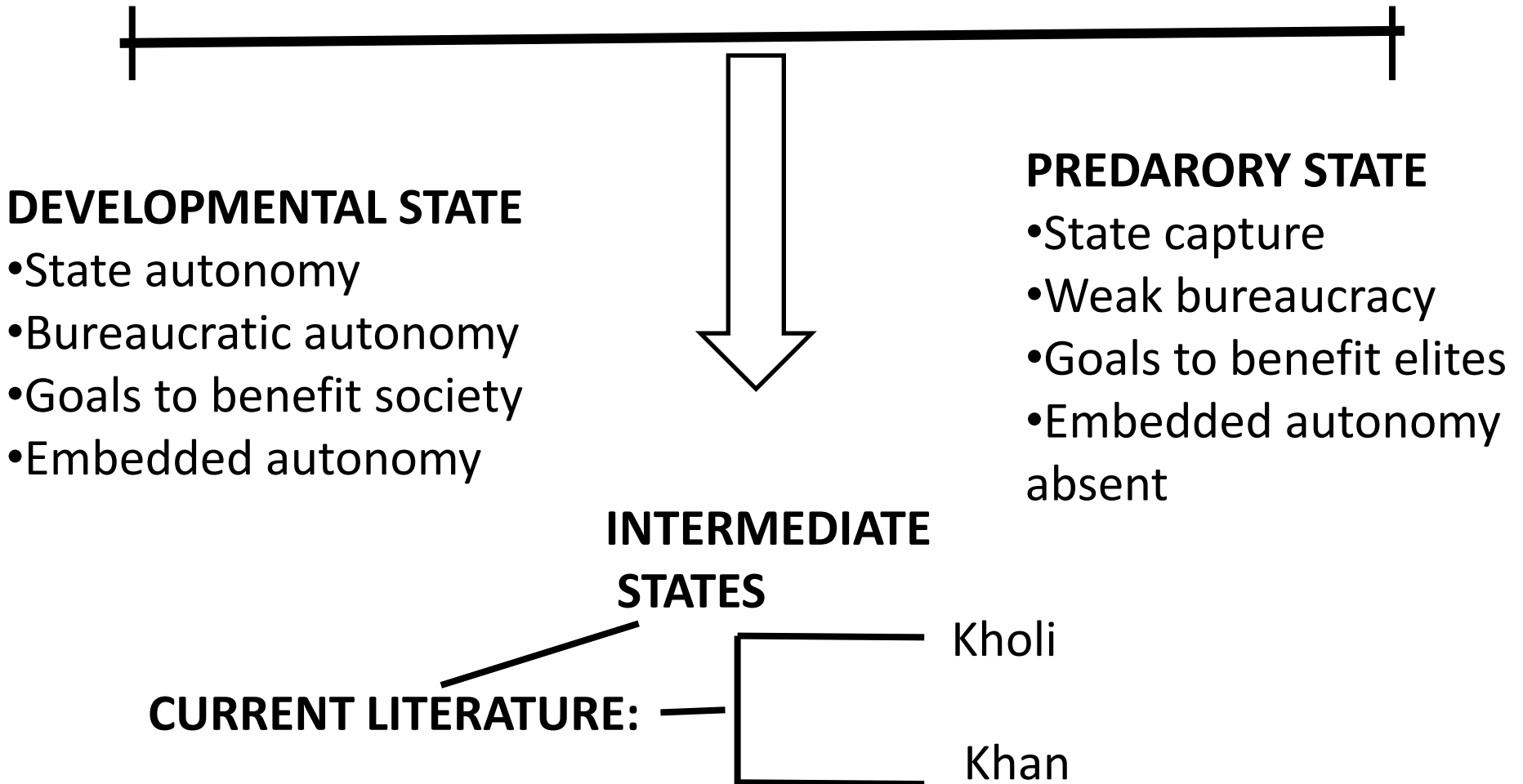
- WADE: to understand how Mann's authoritarian state provides a basis for guiding the market:
    - 1st : state confers adequate autonomy to the bureaucracy for it to effect resource allocation
    - 2<sup>nd</sup> when conflict btw state goals and profit max; despotic power sufficient to ignore bus and maintain credibility
- “state effectiveness in IP is a function of the degree of insulation from the surrounding social structure”***



# Foundations (3)

- Evans: understanding goal setting in SEA IP model
- 3 key findings:
  - State elite determine national interest in isolation. Benefit of society -Developmental state.
  - High levels of institutional power. Bureaucracy is autonomous because the state confers such independence
  - State and business enjoy intimate relationship but no state capture due to independent bureaucracy

# Foundation (4)



# Current Literature (1)

- Most Latin American and African states who failed to achieve SEA outcomes after state led IP were mostly intermediate states

*“The challenge in developing countries is not getting the content and application of IP right; but getting the content and application right in circumstances where the country is run by flawed leaders presiding over a politically weak and internally fragmented state”*

# Current Literature (2)

- Kholi : concentrates on political economy
- **Cohesive capitalist state**
  - Run economy with iron fist
  - Favours narrow business elite at expense of labour et al
  - Most often repressive authoritarian regime
- **Neo Patrimonial state**
  - Public officers treat state resources as personal patrimony
  - Fragmented population
  - State worries about accommodating conflicting interests little attention on economy
- **Fragmented Multiclass state**
  - State commands some authority over pop and held to account
  - Very broad array of alliances with non state actor groupings
  - State must keep multiple parties happy thus raft of agendas and goals
  - State spread too thin, legitimacy issues promises more than it can deliver

*“an attempt to implement a complex state led IP in this context is so fraught with compromise that most states will be middling to poor IP performers”*

*“rapid and effective industrialisation is incompatible with broader social and political empowerment goals”*

# Current Literature (3)

- Khan: economic rent management
- State provides rent/subsidy to narrowly defined population for a period of time in return for a reciprocal behaviour
- For effective rent management :
  - Ability to monitor and make judgments about performance
  - Capacity to reallocate resources, subsidies and rents away from non performers
- 2<sup>nd</sup> requirement ( reallocation) requires political capabilities not institutional capabilities
- IP options and instruments must be compatible with the country's internal power configuration
- In most developing economies the contextual political economy constraints will only allow for very very limited industrial policies

# PRAGMATIC SOLUTIONS (1)

## 2<sup>nd</sup> BEST INSTITUTIONS

- Orthodox view on institutions: optimise market freedom and property rights, Anglo Saxon, quantifiable, generic benchmark
- **Chang** : (a) economic development drives institutional change not the other way round, (b) good institutions are expensive, ( c ) wealth creates new agents for change and better institutions
- **Aoki**: can't change just 1 institution need critical mass
- **Stiglitz, Dosi**: institutions meant to be stable by definition
- **Fafchamps, McMillan, Dixit, Woodruff and Rodrik** – 2<sup>nd</sup> best option

# 2<sup>nd</sup> best institutions

- Ghana and Vietnam
- Informal substitution from legal based formal contracting to relational contracting
  - Invest heavily in I/t relationship building
  - Demand immediate payment for G&S
  - Careful screen prior to contracting
  - Proactive renegotiation
- 2<sup>nd</sup> best option: improve relational contracting ( better info on firms, better firm info dissemination, registers of behaviour)
- Or only reform legal system in sectors where relational contracting weak
- Better to do the second best option well than the first best option badly
- Better value for money, more doable, more compatible with PE context

# Islands of Excellence

- Geddes: no unitary concept of state bureaucracy: regime, the president, the cabinet, state elite, collection of agencies and depts.
  - All have different levels of isolation/autonomy
  - Machine human inputs + material inputs + human agency = policy implementation
  - Increase insulation of each component gets you better implementation
- 60's Brazil – fragmented multi class state; corrupt legislature and bureaucracy; insufficient despotic power to change – look for ad hoc help to assist in delivering some election promises
- Small groupings called pockets of excellence



# Islands of Excellence (2)

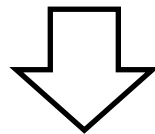
- President set 30 economic goals
- Each goal became a programme run by an executive group
- Executive groups set up by Presidential decree
- Leader appointed by president
- Group has total autonomy over budget and personnel
- Report directly to president – must by pass bureaucracy and legislature
- Co-ord with other groups only if necessary

102% completion rate across all 30 projects; hey day of Brazilian IP

Downside: expensive and short term BUT in a sea of dysfunctionality they achieved substantial wins because their policies and tools were compatible with the internal and external power balance of the state (Kholi and Khan)

# Joint Discovery IP as a process

- Modern day compromise of embedded autonomy for countries with low despotic power and weak bureaucracies
- About picking winners
- Picking winner today difficult:
  - Production sharing ( task not product)
  - See large amount of chance in how sectors get selected
  - Need to be more specific these days ( 4 or 6 digit SIC)



***NEED THICKER BANDWIDTH BTW STATE AND PRIVATE SECTOR***

# Joint Discovery

- **PC:** entrepreneur discovers Prod X can be produced locally at a competitive price: crowd in and emulate; initial entrep small % of social value created thus always undersupply of discovery entrepreneurship
- **Hetero:** Prod X discovered by state and entrepreneur is a systemetised process that creates rents for the discoverer while gov simultaneous creates support measures for growth
- Increases the flow of new products and product lines with proven competitive edge – increase specialisation and diversification
- Strategic collaboration by both parties to grow the economy
- **Adv:** no ex ante picking winner; works around lack of bureaucracy shortcomings
- **Disadv:** Khan's argument about reallocating rents for non-performance. Gov needs to learn to let losers go
- Maybe like islands of excellence works in some sectors and not others

# CONCLUSION

- Current heterodox literature is forcing developing nations to look at themselves in the mirror and honestly assess what IP tools and expectations are relevant for their current extant circumstances.
- Overall it seems that developing nations can do less rather than more at this stage
- Normalised literature still nascent hopefully more insight in time
- 4 take away ideas:
  - Realism about political economy and hence compatible IP
  - Seriously rethink the idea of 1<sup>st</sup> best solutions and think about how 2<sup>nd</sup> best options may be more relevant and workable
  - Limit expectations of undertaking massive, complex, state led IP a la SK - look for small areas of success and improvement knowing that every bit of growth allows for better institutions which in turn allow for more IP
  - Some IP can be done even in the most challenging of constrained parameters – ju st need to be realistic