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POLICY BRIEF

ADVANCING THE POST-2015 DEVELOPMENT AGENDA REQUIRES A DEVELOPMENT POLICY RETHINK

Buoyant demand at the global level and effective industrial policy at the national level have been key ingredients of successful development in recent decades. With the risk of "secular stagnation" in developed countries limiting the export opportunities for developing countries for a protracted period of time, developing countries will need to find new growth drivers. Industrial policy will have an important role to play, but a more inclusive multilateral approach is needed to obtain the desired changes in policy, particularly in light of the ambitious and transformative post-2015 agenda envisioned by the proposed sustainable development goals.

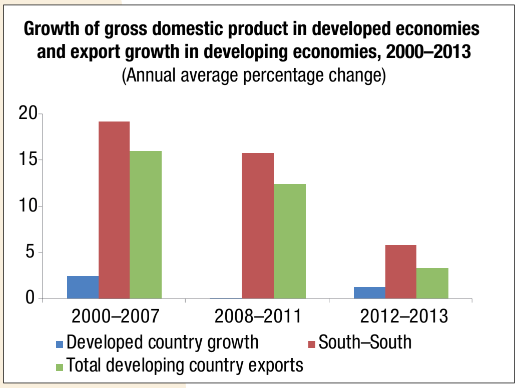
Between the early 1960s and the late 1980s, successful catch-up economies in East Asia could count on buoyant export markets. These economies also enjoyed significant flexibility in terms of pursuing the trade and industrial policies that they deemed most suitable to achieving the structural transformation and technological upgrading needed to support higher levels of productivity.

From the start of the millennium, some developing countries succeeded not only in achieving further industrialization and expanding their exports, but even increased the pace of this expansion. The fact that multilateral trade agreements maintained some flexibilities for all World Trade Organization members and incorporated some special and differential treatment for least developed countries, has played a role. But more importantly, the increase in the proportion of exports, and especially that of manufactured exports, in the composition of developing countries' aggregate demand strongly benefited from rapid global demand growth and expanding imports, particularly by developed countries.

As highlighted in the UNCTAD *Trade and Development Report, 2014*, the effectiveness of flexibilities built into multilateral trade agreements and strong external demand for underpinning successful development strategy appear to have weakened since the financial crisis. The past few years have seen a proliferation of regional trade agreements and international investment agreements that include a wide range of rules and restrictions that go beyond the provisions of multilateral agreements.

Some developing country policymakers may have agreed to these in the belief that accepting stricter policy and regulatory commitments is necessary to attract foreign direct investment and secure participation in global value chains. However, while these commitments may provide short-term trade and employment benefits, in the longer run they run the risk of trapping producers into commodity enclaves or low-value niches of manufacturing. Additionally, the cost in terms of sovereignty loss of some international investment agreements can also be high. In some cases, these agreements allow ad hoc arbitrage tribunals to assume important law-making functions usually allocated to States, but without the institutional balances and legitimacy associated with State judicial functions. In addition to the lack of transparency and coherence often observed in the operations of some tribunals, this set-up follows a model developed for resolving disputes between private commercial actors, and thus these tribunals may have no reason to consider the broader interests of a host country and its development strategy.

Buoyant import demand, particularly in the new millennium, has depended on rising levels of debt in many advanced economies, leading to unbalanced balance sheets in their private sectors and subsequently in their public ones. The slow recovery of advanced countries from the financial crisis has accordingly reduced developing countries' export prospects. Moreover, statistical evidence points to a considerable weakening of the import elasticity of demand in these countries since 2012. This weakening has strongly contributed to the continued slowdown in the pace of developing countries' total exports, given that over the period 2012–2013, developing country exports were pushed ahead mainly by trade with other developing countries (see chart).



Source: UNCTAD secretariat calculations, based on data from UNCTADStat.

Note: The data shown are averages of annual growth rates.

This unfavourable turn in the external economic environment poses a risk not only to sustained economic growth in developing countries, but more generally to attainment of the goals of an ambitious development agenda with structural transformation at its centre. A very different policy mix needs to be applied. Given that global demand is unlikely to return to a rapid and sustained growth path any time soon – unless there is a significant shift in the policy mix of advanced countries[1] – a less constraining external economic environment is required in other dimensions. To achieve this, it is important that developing countries have enough policy space, in particular in the areas of trade, finance, and industrial development, and that they have the fiscal revenues to match their ambition.

Against this background, four elements of a more ambitious and flexible policy approach will be required to spur growth and attain the goals of a post-2015 development agenda:

- First, with the developmental effects of export-led growth strategies based on demand from the North running out of steam, a greater role will need to be given to domestic and regional demand. In addition to redistributive measures, employment creation and rising wages to help bolster the growth of domestic consumption, many countries need to raise their levels of domestic investment, including in the public sector.
- Second, the effectiveness of rebalancing developing countries' growth strategies would be strengthened by industrial policies. A number of developing countries, including the largest ones, have already adopted new industrial policy initiatives, in some cases responding to a failure to achieve the economic transformation promised by structural adjustment programmes, in others as an effort to replicate the success of the East Asian economies. But that success was very strongly export oriented, and any new initiatives will need to be matched by appropriate macroeconomic and financial policies aimed at adjusting developing countries' productive capacity and competitiveness so as to respond to rising domestic and regional demand without excessive pressure on prices or the trade balance. Developed countries are also again acknowledging the role of industrial policy in boosting productivity growth, encouraging innovation and creating decent jobs. For example, the approach of the United States of America to industrial policy combines an "entrepreneurial State" with a "coordinating State" to skilfully use sector-specific measures to support the manufacturing sector.
- Third, in commodity-dependent economies, converting natural resource rents into sustained growth and industrialization will require a high level of investment and a virtuous link between trade and capital accumulation. The sharp increase in commodity prices that started around 2002–2003 has raised fears of premature deindustrialization in some middle-income developing countries. An industrial policy that supports the private sector in identifying and expanding activities in promising manufacturing sectors could greatly facilitate such diversification efforts. Moreover, in many developing countries, increasing the generation of public revenues from natural resources will be essential for the financing of such efforts.
- Finally, integrating into international production networks should not be seen as the only element in a country's industrialization strategy. Doing so may provide opportunities for countries at an early stage of structural transformation to accelerate industrial development in some sectors. But the evidence that integration into these networks spurs sustained industrialization is at best ambiguous. Structural transformation episodes, even if initially successful, are often linked only to "thin" industrialization that offers few opportunities for economic and social upgrading. Developing countries that have achieved some degree of industrial development will still need to maintain policy flexibilities if their further participation in international production networks is to deepen and widen the firm and cross-sectoral level linkages needed to promote economic and social upgrading.

Effectively pursuing such more ambitious policies could be greatly supported by strengthened global trade governance that focuses on two elements. First, reinforcing inclusive multilateral mechanisms would help maintain the public good character of multilateral rules and preclude competitive liberalization that may be ill-suited to developing countries' development prospects. Second, refocusing trade negotiations on multilateral agreements would imply reconsidering the developmental character of the growing number of regional trade agreements and international investment agreements and could help make further headway in the ongoing Doha Round of multilateral trade negotiations.

Developing countries will also need to leverage the greater economic and political power they have achieved over the past two decades. In particular, a more robust South–South integration architecture (already emerging at the regional level and with the New Development Bank established by the BRICS countries[2]) could help buttress a more ambitious post-2015 agenda.

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1 UNCTAD, 2014, *Trade and Development Report, 2014* (New York and Geneva, Sales No. E .14.II .D.4, United Nations publication), chapter II.
2 Brazil, the Russian Federation, India, China and South Africa.