Industrial policy: stimulating the dynamic forces of markets. Linking organics agriculture and tourism in Laos.

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National policy goals Laos ...(1)

1. Increase productivity and revenues in the clean agriculture - organic sector.

2. Increase productivity and revenues in tourism sector – investment in new assets; increase arrival numbers; increase revenues per arrival.

3. Increase demand for organics in tourism – 1 & 2 of above PLUS usual issues of “linkages not leakages” PLUS special features of ORGANICS.
National policy goals ... (2)

- Economic transformation, structural change, diversification
- Build resilience – BOP stability, reduce reliance costly inputs, formalise the ‘green economy’.
- Job creation, decent work, value-added...
- Sustainable and inclusive growth
- Build on natural comparative advantages
- Target dynamic new market opportunities – tourism and organics
- Needs engaged State and enabled Private Sector
Industrial policy reappraised

- After WWII, many countries adopted policies aimed at:
  - Promoting new (infant) industries, Protecting traditional industries from international competition

- Since early 1980s, growing scepticism, arguing that
  - Governments are unsuccessful in ‘picking winners’
  - Such policies invite corruption and rent seeking

- Washington Consensus: improve investment climate through liberalization, macro stabilization, strong legal framework foster private economic activities

- Today, agreement that rapidly growing DCs did not followed “Washington” but pursued industrial policy

Key question not whether but how to pursue industrial policy
National policy challenges ... generic

- Targeted at loosely-defined market imperfections
- Implemented with little capacity to identify where imperfections are or their size
- Potential for corruption and rent-seeking by powerful lobby groups
- Policy space is constrained (national & int’l)
- And yet ... industry unlikely to take off without developmental state interventions
3. Tourism trends, Implications for Laos

- Global growth predictions (=ve) but slower; fastest in SE Asia.
- Tourism currently 69% share of exports of services; 19% share of exports goods & services.
- Similar to some G20 economies Australia, Mexico, South Africa, Turkey) and many LDCs.
- Slowdown in global trade volumes as world economy d-coupling is volatile.
- New centres of gravity, multi-polar world.
- Competition for investment and for markets.
4. The goal:

- Identify **selective** intervention or policy that attempts to **alter the sectoral structure** of production towards sectors that are expected to offer **better prospects for economic growth** – organics and tourism...

  - Selective intervention
  - to create new production capacity and new comparative advantage
  - enabling an economy to move upwards in the international division of labour
Activities where FDI more likely to occur
FDI occasionally occurs
Primarily domestic investors

UNCTAD (2011)
4. Lessons from other countries...

(1)

- Strategic policies to strengthen the linkages between (domestic and international) tourism enterprises and domestic economy (organics).
- Financial measures (WTO examples)
- Fill gaps credit market, reduce costs innovation
- Coherent policies - Tax and fiscal policies, VAT
- Incubators, procurement etc
- Human Resources (training, FT support (IFC))
- “joined up ’ PPP projects - Berimbau
4. Lessons from other countries

- **Investment:** Southern investors are “different”; Investors in LDCs are “different”
- Incentives are less important than everything else in the long run. Excessive incentives (-ve)
- **Linkages:**
- Local investors don’t create more linkages than foreign. What matters more – company “offer”, authenticity vs price competition; what’s available
- **Infrastructure** – wholesalers, cold chain, quality regulation - Length of time
- **Marriage brokers** – full-time extension services
The attractiveness and feasibility of tourism and organic sector activities

**Attractiveness of activity**

**Growth dimension**
- income elasticity of demand (+)
- market potential (+)
- technology-upgrading potential (+)
- number of potential competitors (-)

**Employment dimension**
- industry-specific employment creation
- linkages

**Environmental dimension**
- Green-economy potential (+)
- CO2-emissions (-)

**Feasibility of activity**

**Country-specific factor endowment**
(fixed and human capital, natural resources, population size)

**Sector-specific technology requirements**
4. c) Theoretical justification ...(1)

- Marshallian externalities: dynamic scale economies giving rise to increasing returns of scale at the firm level (much of productivity growth results from investment and learning by doing)

- Complementarities in investment, production and consumption that, if unchecked, result in coordination failures (importance of linkages)

- Information externalities associated with investment in new goods or new technologies (profitability of innovative investment and speed of imitative entry)
4. c) Theoretical justification ...(2).

- **Supply side**: strong potential for productivity growth and technological upgrading; climate change.

- **Demand side**: high income elasticity of demand and favourable global market and price conditions

- **Balance-of-payments constraint**: Per capita income growth implies rising domestic demand for imports; reliance petrochemical
HOW? The pattern of industrial policy in an open economy (1)

- Strategic trade integration, which
  - Represents a mix between
    - Import substitution through temporary protection and
    - Export promotion through temporary subsidies
  - Embeds industrial policy in a wider outward-oriented industrialization strategy
  - Involves change in product categories that receive public policy support, with their skill, technology and value-added content gradually increasing
HOW (2)...Long-term policy strategy needs to identify comparators

- Country role models
  - Not necessarily the most successful economies
  - Look at similar, but more advanced economies

- Sector-specific benchmarks
  - Advanced, yet technologically similar
  - Impact of trade preferences etc.

- Additional factors
  - Change in global demand structure (new growth poles)
  - In large economies, changes in domestic demand (structure) can play important role
HOW ... (3). Support policies may follow latent comparative advantage: growth identification and facilitation (Lin)

- **Step 1:**
  - Identify rapidly growing tradable sectors in fast growing countries with a similar endowment structure but 100% higher per capita income
  - Scale-up successful private domestic innovation in new industries

- **Step 2:**
  - Identify private domestic firms already in those industries and remove constraints to quality upgrading and further firm entry
  - If there are no domestic firms in those sectors, seek FDI from countries in step 1
HOW…. (4). Problematic aspects in growth-identification-and-facilitation strategy

- Risk of fallacy of composition as:
  - Many countries may get into the same sectors
  - Global demand structure may have changed significantly through move towards multiple growth poles (past no guide to future)

- Risk of undue reliance on low wages in developing export activities

- Ignores demand potential on domestic market
HOW ...(5) Support policies target more advanced, yet technologically similar sectors: economies evolve across the product space (Hausmann)

- Step 1: Locate economy in product space where proximity between products is defined by probability of a country having a comparative advantage in one product given it has a comparative advantage in the other product

- Step 2: Facilitate private companies’ moving across the product space in larger jumps than they would on their own
Value added raw commodity
Value added  consumption
good
Value added consumer experience
5. Problematic aspects in moving-across-product-space

- Product space evolves over time: emergence of new technologies which may imply changes in the match between capabilities and technologies.

- Ignores services whose availability may be as important as skills in moving across product space.

- But overall, preserves significant flexibility to incorporate country-specific circumstances, as well as changes in global demand structure.
5. Overcoming practical difficulties (2)

- Main objection 1: governments cannot pick winners, because they cannot identify with any degree and certainty the relevant firms, sectors, or markets that are subject to market imperfections.

- However, objective is not to pick winners but to identify and sanction losers.

- If there are no losers, the process of industrial policy making is too restrictive.
5. Overcoming practical difficulties (3)

- Main objection 2: industrial policy invites corruption and rent-seeking

- Support must be
  - temporary (not open-ended)
  - based on clearly established operational and achievable goals
  - monitored on basis of observable criteria (e.g. exports)

- Key design features are embeddedness, carrots and sticks, and accountability
6. Stylized representation of open-economy support polices

RL: Resource-based and labor-intensive manufactures
LT: Low technology-intensive manufactures
MT: Medium technology-intensive manufactures
HT: High technology-intensive manufactures
• Many countries have policies to attract tourism investment. It is one of the least restricted sectors.

• But, fewer have policies to benefit fully from it – especially with regard to linkages.

• Domestic investment is equally important, but seldom emphasised, often neglected.

• Integrate tourism investment policies within the overall policy framework.

• Sustainable – green – organic – highly linked - tourism does not necessarily mean ‘doing’ a different kind of tourism, but rather ‘doing tourism differently’.