



Why Structural Transformation Matters: The Role of Industrial Policy

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The difference between Structural Change and Structural Transformation

- ▶ What happens when a country embarks on economic development?
 - ❑ The structure of its economy begins to change
 - ❑ The share of the primary sector in domestic output diminishes and increasingly secondary-sector activities gain importance
 - ❑ More and more of the population begins to live in towns/cities – ‘urbanization’
 - ❑ And more and more of the labour force engages in productive activities
- ▶ Does this mean the country is undergoing a structural transformation?
- ▶ Not necessarily!
- ▶ Especially if the structural change keeps the economy locked in low production and productivity trap.

What do we mean by Structural Transformation?

- ▶ Structural transformation takes place when policies are used to shift labour and capital (but also technology and natural resources) from:

- **Traditional** → **Modern economic activities or sectors;**
- **Low-productivity** → **High-productivity sector or economic activities;**
- **Low-Value** → **High-value sector or economic activities;**
- **Low-technology** → **High-technology sector or economic activities;**

- ▶ **Two Key messages:**

- Structural transformation represents **a movement up the productivity, value and technology ladders.**
- Structural transformation takes place **both across sectors and within sectors.**

Key Drivers of Structural Transformation

- ▶ Expanding **productive capacities**;
- ▶ Equally important is **productivity**, which is **central** - **because different sectors or activities have different levels of productivity**, along with varying potential for innovation, economies of scale, etc
- ▶ Thus, **differences between sectors**, and between activities within sectors, **has important implications for growth, competitiveness and structural transformation.**
- ▶ A key policy instrument for animating the movement capital, labour technology and other resources in the right direction to foster structural transformation is **“Industrial Policy”**.

A New Generation Industrial Policy

- ▶ A taboo subject for a long time but **now acknowledged as central to recovery**.
- ▶ Ethiopia is currently formulating a new industrial policy.
- ▶ Important to learn from recent Ethiopian experience, but also from **new perspectives in industrial policy**:
 - ❑ **Not only manufacturing**: but also other sectors; and the central objective is to foster structural transformation.
 - ❑ **Building capabilities, not only sectors**: capabilities include education, infrastructure, energy, technological capacity etc) that move the country into higher productivity and higher value activities.
 - ❑ **Making effective use of financial institutions to build productive capacities**: The need for re-evaluating the role of a Development Bank.
 - ❑ **Avoid selective intervention**: unless accompanied by sunset clause, performance indicators and effective institutions for implementation.
 - ❑ **The need for policy coherence**: even the best industrial policy will fail if trade, investment, services and macroeconomic policies are not aligned with its objectives

Ethiopia's "New" industrial policy – learning from recent experiences (2)

▶ Three important lessons from recent experience:

- ▶ (1) **Policy sequencing**: Implementing policies that lay down the favourable conditions for the success of other policies.
- ▶ (2) **Policy coherence and consistency**: particularly among, **industrial, trade, investment and macroeconomic policies**.
- ▶ (3) **Clarity of purpose in policy implementation: Basically knowing**:
 - ❑ "What" policies should be implemented when;
 - ❑ "Who" should implement them;
 - ❑ "How" should they be implemented;
 - ❑ "When" should they be implemented; and
 - ❑ "What" are the key performance indicators of success.
- ▶ (4) **Policy coordination and accountability**: are critical for successful implementation of industrial policy.