



Industrial Development and Diversification -
new approaches for Africa?

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Overview

- Beyond ideology
- Two broad approaches:
 - Enabling policies, pro-competition
 - Resource-shifting policies

These are complementary, but sequencing may matter
- “Traditional” industrial policy
- A more horizontal orientation and other emphases
- Likely ingredients of successful industrial policy
- Are GVCs an opportunity?
- Role of services

“Traditional” industrial policy

- Import substitution
- Export policy-driven industrialization
- Outward-oriented industrialization, including export processing zones

Import substitution

- Build diversification/industrialization on domestic demand: degree of success depends crucially on domestic market size
- Tariffs and quantitative restrictions on imports structured to combine cheap inputs and expensive competing products
- Problems with anti-export bias – limits of the domestic market, a lack of competitiveness, and negative exchange rate effects leading to foreign exchange rationing
- In its purest and most persistent form, a policy *cul de sac* with high economic costs

Export policy-driven industrialization

- Diversify on the back of the domestic market, but by using export restraints on industrial inputs rather than import restrictions – indirectly a production subsidy
- Need to have the necessary domestic natural resources
- Assume capacity to produce at world prices over time, or else no different from the import substitution policy *cul de sac*
- The terms-of-trade issue
- Tariff peaks and escalation in major markets that can frustrate this strategy to the extent it is export-driven

Outward-oriented industrialization

- Export-led growth model, but domestic market also available
- Inputs at world prices, add value domestically, mostly labour
- Equalize cost structures for domestic and export sales – elimination of the anti-export bias, strive for backward and forward linkages
- Need to pick winners and ensure time-limited support
- Assumes a range of prior conditions present relating to infrastructure, skill levels, governance etc.

Export processing zones

Export processing zones (EPZs) are enclosed policy spaces dedicated exclusively to production for exports

- May foster:
 - Job creation
 - Additional economic activity
 - Possible technological spillovers
- But:
 - Favour foreign firms
 - Race to the bottom competition
 - Sustainability in terms of labour standards and environment
 - Lack of backward linkages
 - Attract foot-loose industries mostly with infrastructure subsidies, tax-less environment and cheap labour

Choice of policy instruments matters

- Policy choice and efficiency/effectiveness:
- Taxes
- Subsidies
- Quantitative restrictions (QRs)
- Trade-related investment measures (TRIMs):
 - Obligation to buy local inputs
 - Minimum export obligations
- Regulations

More recent industrial policy orientations

Horizontal supporting policies

- **Essentially economy-wide**
- **Connectivity:** infrastructure, ICT, competitive key services
- **Ease of doing business** e.g. business registration regulations, contract enforcement, import export documentation, improved transparency + promotion of entrepreneurship
- **Trade facilitation** – services are the vehicles for facilitation
- **Financial access** – inclusivity
- **Focus on innovation**, R&D and science and technology policy.
- **Stable macro-economic environment** e.g. manageable rate of inflation, competitive exchange rate
- **Regional and multilateral cooperation** – enhanced market opportunity, rule setting, specific initiatives e.g. economic corridors, harmonization

Many of these policies are enabling first, resource-shifting later

Modern emphases in industrial policy

- Increasingly from trade-policy-dependency to FDI
- Understanding services
- Role of public-private partnerships
- The importance of discovery/technological frontier
- Policy fixes aim to:
 - Disseminate information
 - Coordinate and create networks
 - Manage information asymmetries
- Preferences for support and subsidies rather than trade restrictions
- Capabilities

The pre-conditions for successful industrial policy

Industrial policy effectiveness – implementation is key

- Clear-sighted focus on design, purpose, objectives, means and key performance indicators (KPIs)
- Consistency and good governance
- Systematic reporting, monitoring and evaluation
- Picking winners, maybe, but letting losers go, certainly

Do Global Value Chains (GVCs) offer additional diversification and industrial development opportunities?

Why are GVCs different when it comes to industrial policy?

- Possibility of insertion at different points on a chain, no need to produce a good or service from beginning to end
- A lot of focus on intermediates – fragmented production processes
- Possibility of a regional orientation, but not as market enlargement for import substitution
- Integrated nature (complementarity) of markets on the supply chain modularization/bundling possibilities for first (+) tier suppliers and beyond

Opportunities for industrialization, specialization and diversification

- Diversification through specialization
- No need for 'full' specialization
- But how to escape bottom end low-skill specialization through upgrading and adding additional value?
 - No magic bullet
 - A combination of an enabling environment and lead firm cooperation

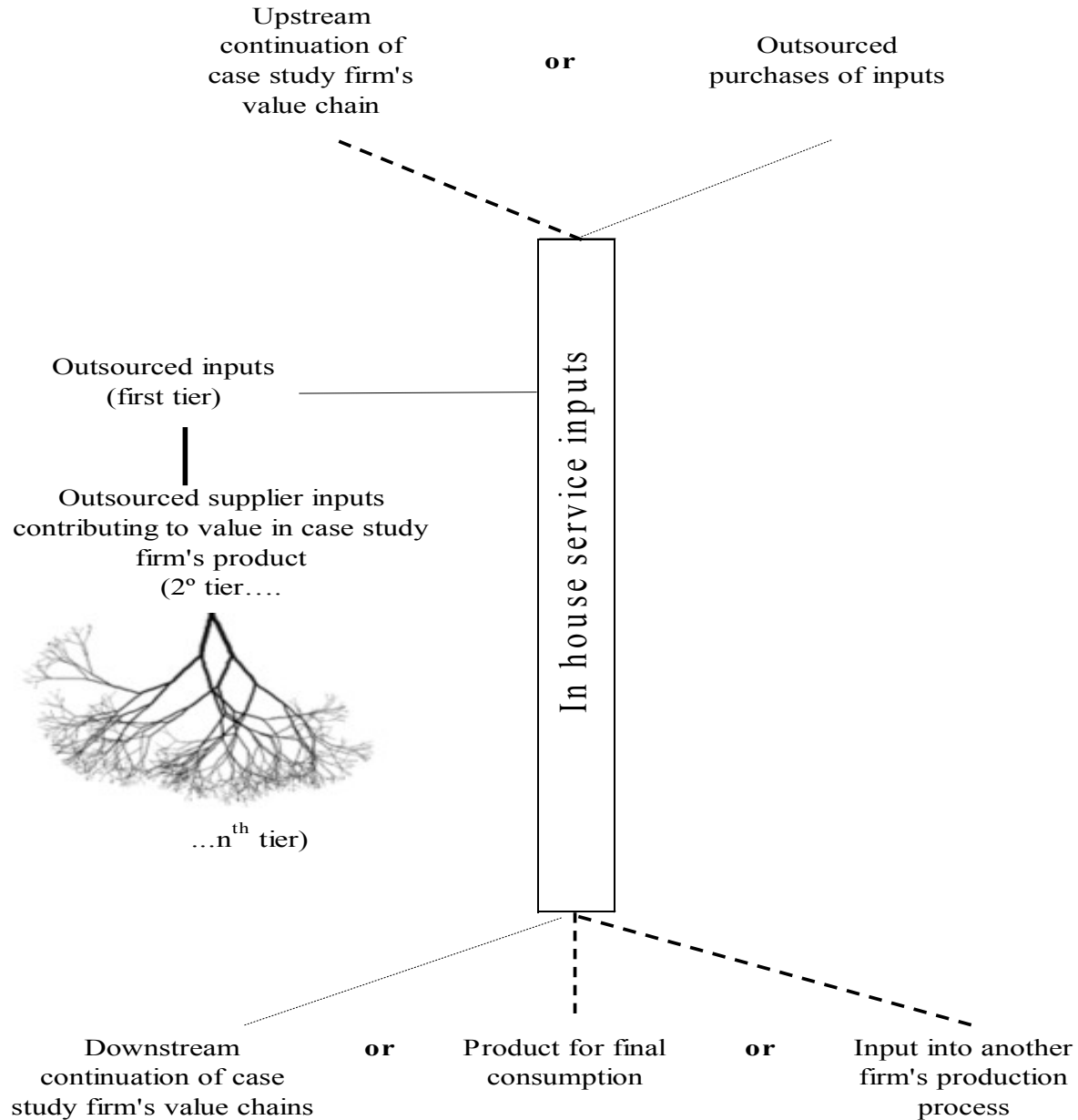
Are there risks with GVC involvement?

- Static, low-level engagement with limited added value opportunities:

OR

- Opportunities for upgrading
 - Process
 - Product
 - Technological
- Scope for intra-African economic integration via GVCs
- Complementarities in regional trade content – intra-sectoral as well as inter-sectoral trade
- No magic bullet
- A combination of an enabling environment and lead firm cooperation

Figure 1: Mapping Services along Value Chains



The role of services in GVCs

Services in the global economy

The historical neglect of services:

- Classical economic thought and the theory of value

'The labour of a menial servant...adds to the value of nothing...services generally perish in the very instant of their performance, and seldom leave any trace or value behind' Adam Smith (1776)

- Story from the 1960s – Baumol's disease and services as the poor cousin, allegedly zero contribution of services to innovation and productivity growth
- But growing "servicification" in global economy

Data challenges:

- Measuring intangibles
- "Service science", linked to intangible assets and value acquisition literature
- Significant heterogeneity in offerings (very hard to identify unit prices)
- The bundling phenomenon (especially services embedded in goods)
- The missing link, measuring trade as value-added

Services are becoming increasingly important in all economies

On the
consumption
side

Typically services
consumption rises
with income levels

Services offer more
variety and product
choice than goods

Services are more
customized than
goods

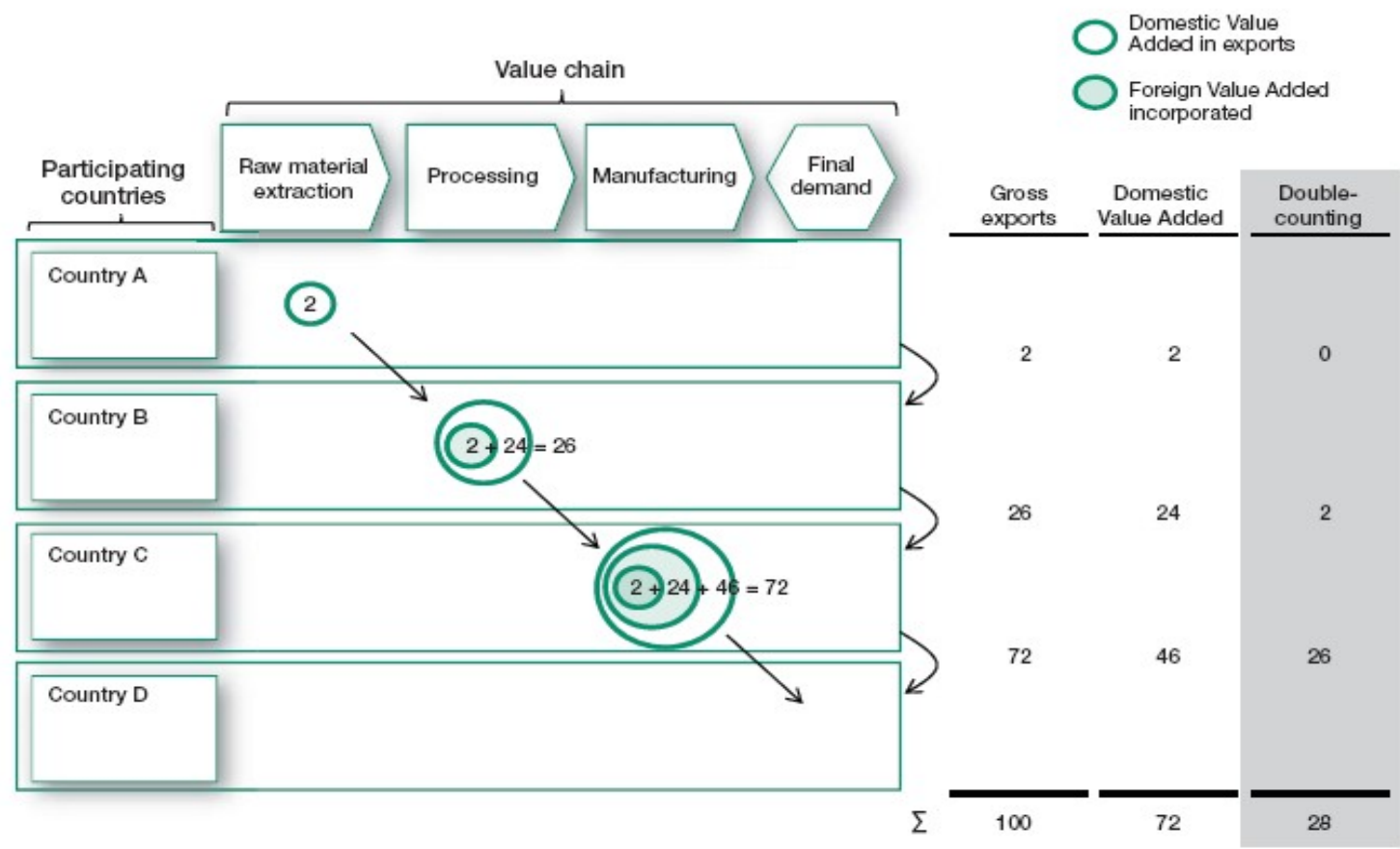
On the
production
side

Globalization, or the
internationalized
economy, has increased
demand for services,
especially along GVCs

As output expands,
there is more than
proportionate demand
across every activity in
the economy for
certain kinds of
services - telecoms,
ICT, finance, insurance,
energy, transport etc.

How does value-added measurement of trade work?

Figure 1. Value added trade: how it works

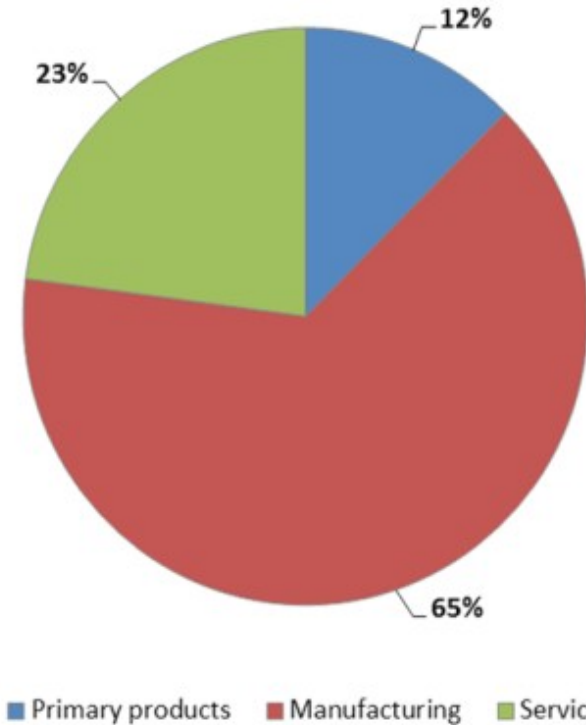


Source: UNCTAD.

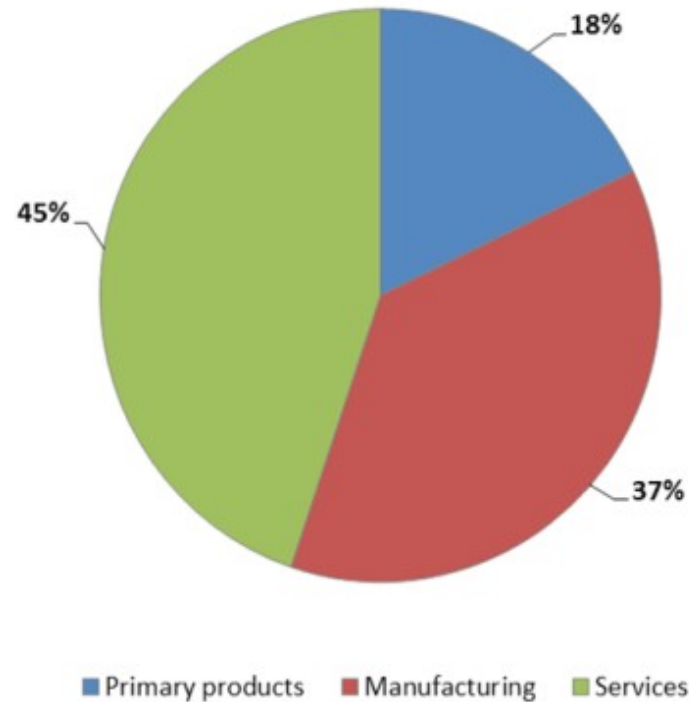
1. Sectoral contribution to total trade, gross and value-added measures (2008)

(Source: WTO Secretariat estimates based on OECD-WTO data)

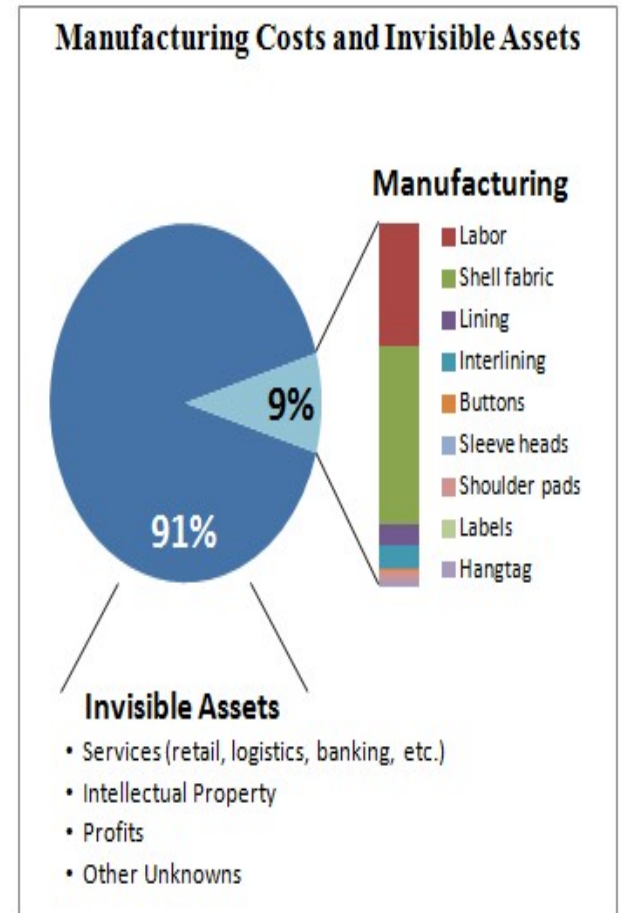
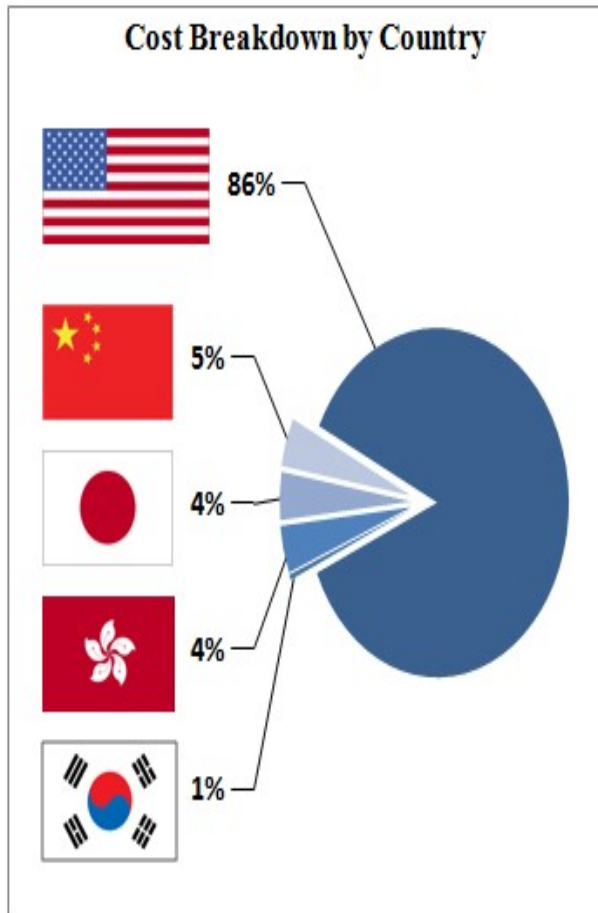
Structure of world exports in gross terms, 2008



Structure of world exports in value added terms, 2008



1. Value-added attribution: Jacket



Services as innovation

- Services innovation via product differentiation
- Services an important source of process innovation, as well as in bundled combination with goods-driven R&D
- Services as part of networked technology, innovation, entrepreneurship and consumption

Numerous services enter the value chain

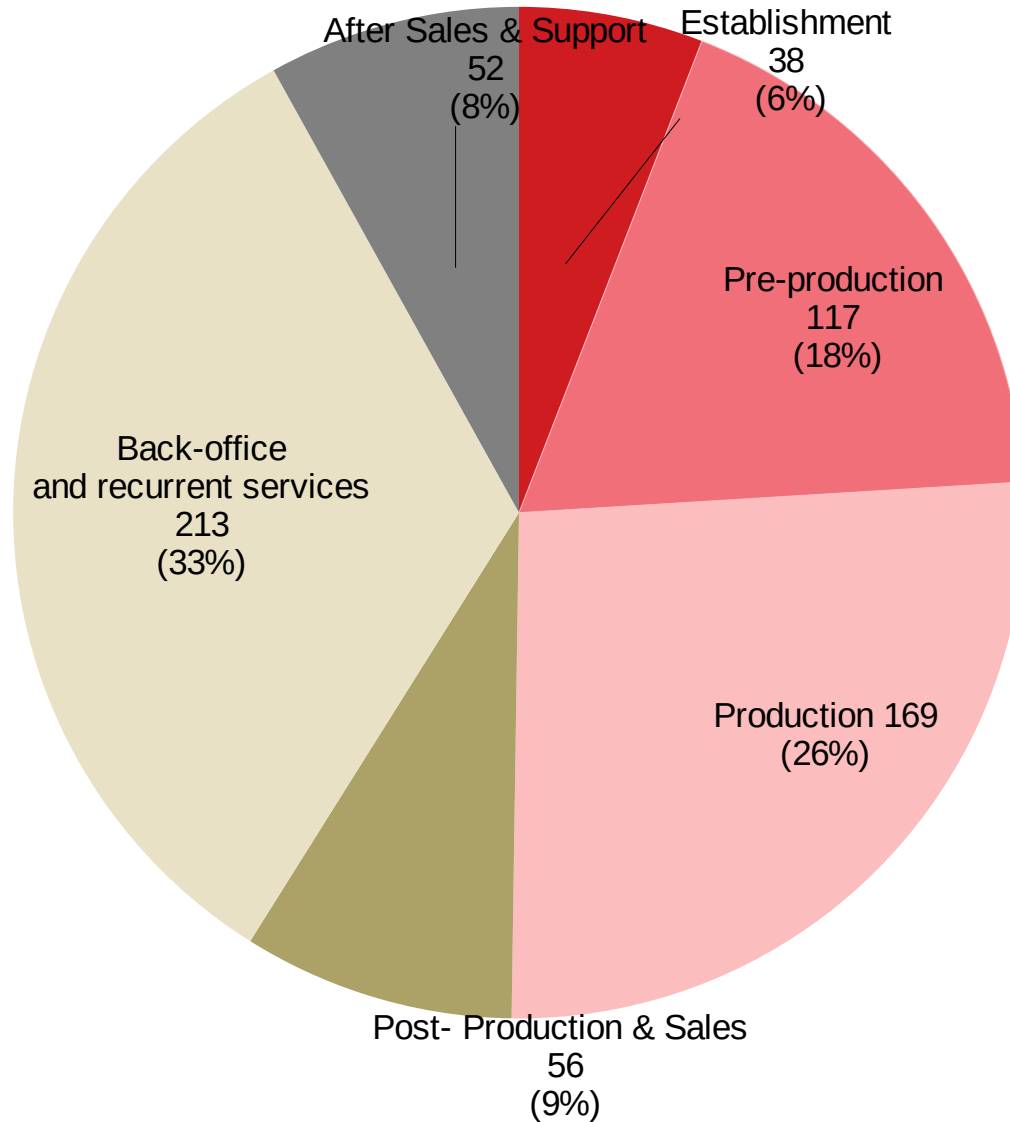
Stages/Cases	Total Number of Services
Aircraft parts, Philippines	53
Automotive components, Japan	<u>37</u>
Car manufacturer, Philippines	70
Construction machinery, Japan	72
Die makers, Thailand	38
Home appliance Japan	55
Oil and gas extraction equipment, Singapore	55
Power plant equipment, Japan	<u>77</u>
Server manufacturer, Taiwan	53
Wastewater treatment, Thailand	54
Watch manufacturer, Hong Kong	43
Welding Alloys, Thailand	38

Numerous services enter the value chain

Services Entering a Manufacturing Value Chain for Construction Machinery

Establishment Stages		Pre-manufacturing		Manufacturing		Post-manufacturing		Back-office and recurrent		After-sales	
1.	Business liaison services	6.	Raw material procurement agent	16.	Production management services	31.	Land transport of vehicles to distributors	38.	Auditing on financial accounts	63.	Customer complaints and compliments handling
2.	Company registration and licensing services	7.	Customs-related services	17.	Quality control and standards compliance	32.	Sea transport of vehicles to distributors	39.	Financial services	64.	Technical support for customers
3.	Information and statistical services	8.	Quality inspection services of inputs	18.	Cleaning services of factory	33.	Retail trade services - By distributors	40.	Internal auditing	65.	Information services for customers
4.	Visa and immigration services	9.	Freight transportation services of raw materials	19.	Engineering Services	34.	Retail services on a fee or contract bases	41.	Insurance for machinery	66.	Satellite services for remote monitoring
5.	Business establishment consultants	10.	Fleets repair and maintenance	20.	Gardening services for factory lawn	35.	Retail operation management	42.	Insurance for staff	67.	Data center services for remote monitoring
		11.	Storage - general storage	21.	Security guards services	36.	Storage and warehousing services for machineries	43.	Business and management consultancy services	68.	Ground radio communication services for remote monitoring
		12.	Storage - tank farm	22.	Sewage water treatment services	37.	Hire purchases and financing services for customers	44.	Company secretary	69.	Global Positioning System (GPS) services
		13.	Conception and design of product	23.	Equipment maintenance			45.	Corporate communications,	70.	Repair and maintenance of machines for customers
		14.	Patent acquisition	24.	Waste collection and recycling			46.	Courier, postal and local delivery services	71.	Buy back services to buy used parts and machines from customers
		15.	Product development/ R&D for new technology	25.	Government safety/ environmental inspection			47.	Estate management	72.	Remanufacturing and refurbished services
				26.	Catering services			48.	Human resources management		
				27.	Workers' dormitory			49.	Personnel search and referral services		
				28.	Medical services			50.	I.T maintenance and support		
				29.	Recreation facilities and services for workers			51.	Safety and security		
				30.	Employees transportation services			52.	Telecommunication		
								53.	Uniform -Design and alternation		
								54.	Uniform -Laundry		
								55.	Legal services		
								56.	Advertisement administration		
								57.	Advertisement agencies services		
								58.	Advertisement designers' services		
								59.	Advertisement - cameramen, directors, photographers and models.		
								60.	Electricity supply		
								61.	Gas supply		
								62.	Water supply		

Numerous services enter the value chain



END