

## **LLDC Conference**

### **Value Addition and Structural transformation in LLDCs in the context of the Vienna Programme of Action and the 2030 Agenda for Sustainable Development**

#### **UNIDO intervention**

Thank you Mr. Chairman.

Good morning Honorable Ministers, Excellencies, ladies and gentlemen

Allow me to first thank the Organizers for inviting UNIDO as a panelist to this important conference. UNIDO accords great importance to the socio-economic development of LLDCs – we have a variety of engagements with LLDCs, as a group as well as at country level.

UNIDO is in essence a technical assistance agency, and we have a range of support services:

- in supply side capacity building –for manufacturing but also for agribusiness and for industry-related services,
- we also offer technical assistance in trade facilitation –focusing on capacities for testing, inspection and certification, and more generally assistance to build up a National Quality Infrastructure.
- And we offer services in industrial policy.

I do not want to turn this speaking opportunity into a UNIDO commercial, but will be happy to meet with interested countries later today to discuss our cooperation.

In the time that I have been given, I would like to make **two main points**:

1. Industrial development is still crucially important. In essence because manufacturing is key for structural change
2. Sector-specific, focused policies are needed for industrial development and for structural transformation—not just general investment climate reforms

To start with the first point: manufacturing matters crucially.

Over the years, some have questioned the role of industry – seeing industry as something of the past, not that relevant any longer in today's new (services- driven) economy – and with practices of social exploitation and environmental pollution.

I have brought with me copies of two UNIDO reports that discuss the role of industry in development – past and future, and more particularly the role of industry in structural transformation.

So, I will not bore you with details – you can consult the evidence and read the arguments in all detail in the reports. In essence however, what we demonstrate in these reports is that:

*Certain sectors matter more than others for structural transformation—because of greater opportunities for technological development—and technological development underlies structural transformation.*

The manufacturing sector drives technological development and innovation --in the sector itself but ALSO in other sectors.

Technological advance is concentrated in the manufacturing sector and diffuses from there to other economic sectors such as the service sector and agriculture.

That is largely because of *linkage and spillover effects* which are stronger for manufacturing than for other sectors.

Linkage effects refer to the direct backward and forward linkages between different sectors.

Spillover effects refer to the knowledge flows between sectors.

Linkage and spillover effects are presumed to be stronger within manufacturing than within other sectors.

Linkage and spillover effects between manufacturing and other sectors such as services or agriculture are also very powerful.

Even though technological advance in service sectors continues to accelerate, this aspect of manufacturing continues to be very important for developing countries engaged in catch up.

To be clear: the old manufacturing/services divide is no longer a really useful distinction: over time, many service-like activities such as R&D, marketing and sales and customer support have been delinked from the entities actually producing the goods. Still, these services are intrinsically linked to manufacturing.

So, in sum, industry matters for structural transformation — in developed countries, as well as more importantly in developing countries -be they coastal or indeed landlocked.

We are therefore glad to see -- after years of political neglect-- that structural economic transformation, and industrialization is back. It features prominently in the VPoA –just like it does in Agenda 2030, with Agenda 2030 having a specific goal dedicated to industrialization, SDG 9.

On to my second point: stimulating structural transformation requires a specific policy focus on sectors –not just economy-wide changes in business regulations and uniformly distributed investments in infrastructure and skills.

Sectoral targeting has a name: industrial policy.

In fact, the very objective of industrial policy is stimulating structural change - not only to favor manufacturing industry but generally non-traditional, higher productive activities.

The dominant paradigm for the last decades in PSD, especially among Development Partners, has been to promote horizontal, non-sector-selective interventions aimed at improving the general business environment —thus fostering competitive markets.

The problem with that is that the list of issues to address is *not only long*, the goal is *also* to introduce a whole set of *first-best* institutions. A

government may not have the capacity to introduce all those changes and the first best institutions may be different at different stages of development.

Furthermore, and importantly, research undertaken by the Mc Kinsey Global Institute reveals that, collectively, *industry-specific issues* are the most important constraints to growth.

The theoretical debate about the advantages and disadvantages of selective policies will still continue for a while –no doubt,

But fact is that policy makers the world over, from the EU over the US to Japan and in emerging economies as well as developing countries alike, have clearly made their choice in favor of selective interventions. This is the reality. The key issue therefore is rather: *how to make sure this role is played right.*

Analyst –at UNIDO and in academia- generally agree on the following 4 aspects:

**(1)** Political leaders must have the firm will to pursue a national project of economic transformation – not only to conceive it, but importantly to pursue its implementation. Such a project:

- needs to be defined through an inclusive stakeholder process, and
- collaborative and coordinating implementation mechanisms need to be established.

**(2)** The strategy needs to be realistic, analytically well-founded, with short-, medium-, and long-term sectoral priorities.

The economic feasibility of sectors or activities needs to be well scrutinized. Starting from the current base of capabilities and factor endowments, it is essential to establish *feasible rates of improvement*, in line with technological capabilities and comparative advantages.

**(3)** The process is important- *how* you do it is almost as important as *what* you do. Indeed, new industrial policy is viewed as a ‘discovery process’ where entrepreneurs, governments and other relevant stakeholders get together to learn from each other about cost and opportunities and to

engage in strategic coordination to select best options for industrial diversification.

Close and sustained consultation –including at sub-sector level- - needs to take place. At the same time, it is important not to lose oneself in processes, keep the cost for policy-making to a minimum and target quick-wins—so as to ensure commitment. The approach should be results-oriented and not a talking shop.

**(4)** Evaluation and impact measurement are key. Performance measurement was probably the most important factor in explaining the success of East Asian countries. Support to certain sectors and firms should only be provided on a temporary basis and should be focused on supporting *innovative ideas* for upgrading and diversification, not for well-established firms in traditional industries, to *avoid rent-seeking behavior* and effectively encourage economic transformation and structural change.

With this Mr. Chairman, I would like to conclude. I will be happy to answer any questions and would like to reiterate my interest to discuss bilaterally our cooperation with Ministers and country representatives.