Which policies support growth and diversification?

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Cambridge, MA April 14, 2016
When the world looks good, we all feel good

**GDP growth by region 2003 to 2014, %**

**Poverty headcount by region, %**

<table>
<thead>
<tr>
<th>Poverty headcount rate (%)</th>
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<tbody>
<tr>
<td>1990</td>
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<tr>
<td>East Asia and Pacific, EAP</td>
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<tr>
<td>Europe and Central Asia, ECA</td>
</tr>
<tr>
<td>Latin America and the Caribbean, LAC</td>
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<tr>
<td>Middle East and North Africa, MENA</td>
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<tr>
<td>South Asia, SAR</td>
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<tr>
<td>Sub-Saharan Africa, SSA</td>
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**World**

| 37.1 | 29.1 | 12.7 |

Source: World Bank staff’s estimates from PovcalNet.
But inequality is emerging as a challenge for many developing countries.

Gini index for select major developing countries

- South Africa
- China
- Indonesia
- India

2005 or later vs. 1993 or earlier
Structural change has been limited in Africa...

Value added by sector Africa 1995 to 2014, % of GDP
In the “New Mediocre”, problems appear worse than we previously thought

- IMF April growth forecasts revised down for 2016 to just 3.2% globally
  - Contraction of 0.5% forecast in Latin America in 2016
  - Growth forecast revised down to 3.0% in 2016 for Sub-Saharan Africa
  - Significant slow down in China
  - Weak commodity prices may prolong or worsen the slow down

- McKinsey Global Institute forecasts 2.1% global growth for 2014–64 compared to 3.8% from 1950 to 2014
  - Secular stagnation in developed countries
  - Threat of protectionism
  - Growing inequality within countries creates additional challenges

- Have policies around macro stability and economic diversification been impactful and fast enough?
This issue is made more complex by new external factors

- Urbanization is far outstripping the typical source of jobs in cities – manufacturing
- This is creating pressure in cities, more unemployed and underemployed
- Refugee flows in the Middle East and Africa add further urgency to the need for jobs in cities
So how to accelerate? Countries have two policy options

1. Get better at what they do
   - Steps may include:
     - Better business environment (incl. Macro)
     - Attraction of FDIs
     - Value chains and Factor costs
     - Finance

2. Generate a Supply side response
   - Steps may include:
     - Support to self-discovery
     - Attraction of FDI in new sectors
     - Agglomeration approaches to stimulate growth (SEZs, GPs, Cities)
     - Skills set upgrading (innovation)
Get better at what you do – Doing Business and factor costs

Doing business and GDP, ranking

Access to electricity in SSA, % households

Easy, but hard to credit
Ranking*, selected countries, 2014

Factors conditions are difficult to change

Sub Saharan Africa

Sources: IMF; World Bank

*Out of 183 countries
1Purchasing-power parity

Economist.com
Generate a supply side response, but how?

- Diversification: ask Harvard!

- Typical tools of new industrial policy
  1. Matching grants
  2. Special Economic Zones
  3. Larger agglomeration approaches e.g. growth poles and growth corridors
  4. Exchange rate policy
Policies to diversify are difficult, but important

- Industrial policy is *difficult*
  - Many attempts to pick sectors have failed in both SSA and LAC e.g. Ghana canned fruit, LAC import substitution

- But governments are ‘doomed to choose’ anyway according to Hausmann and Rodrik
  - Even horizontal reforms may have differential impact

- Many value chain specific constraints need to be resolved, but with limited resources only some value chains can be focused on, which ones?
66 programs assessed and about 55% of these programs restricted eligibility to SMEs

Focus on investments to improve business development services e.g. marketing, certification, trade fairs, production design

Reasonably successful even when held to a high standard but doesn’t help ‘missing firms’

Matching grant project ratings, %

- Highly Satisfactory
- Moderately Satisfactory
- Satisfactory
- Moderately Unsatisfactory
- Unsatisfactory
Choosing instruments: Zones effectiveness also depend on the context

**WB SEZ projects**

- Pre-1995 focused on East Asia and Latin America with objective of exports and regional growth
- Post-1995 focused on sub-Saharan Africa and targeted at jobs and growth
- 25 zones assessed

**Pre-1995 results**

- Pre-1995 Projects: 9 out of 14 (64%) achieved positive outcomes

**Post-1995 results**

Post-1995 Projects: 3 out of 11 (closed) projects achieved positive outcomes (27%) for their zone components
Choosing instruments: much to learn about growth poles

- Twenty agglomeration projects were assessed
- Project designs overestimated the intellectual clarity of the agglomeration approach.

- While agglomeration interventions may ease coordination failures, entry and investment does not always increase.
  - Madagascar project: attributing all new jobs in project areas to project---average cost/job =$13,000, four times the K/L ratio for SSA firms in enterprise surveys
  - Thresholds (in terms of lower costs and risk) may need to be reached to spur private investment.
  - Agglomeration projects can have a large effect on land values, raising issues of ownership, control and allocation

- Developing cities around the private sector is still not clearly understood (how can one create clusters?)
What 60 years of development economics have brought us are fashions and counter fashions, with a common point: a common obsession for the blueprint.

What increasing anecdotal evidence is telling us is that identical policies have varying degrees of success: variables are infinite (are RCTs really helpful?).

What we are seeing is that countries with established processes to learn and refine approaches are the ones that are succeeding: Malaysia, South Korea and China (Heilmann). Countries with perfect institutions and legislation may not do as well: Rwanda, Pakistan.

Moving on from policy obsession to an implementation culture (the anti-French model)