

Building on Bali

A Work Programme for the WTO

Edited by Simon J. Evenett and Alejandro Jara



A VoxEU.org eBook

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The Return of Industrial Policy: A Constructive Role for the WTO

Vinod K. Aggarwal and Simon J. Evenett

One prominent feature of crisis-era policymaking is the resurgence of industrial policy. Until recently, industrial policy had been taboo in Anglo-Saxon countries such as the US and UK. Yet even in these economies, since the crisis began some senior policymakers have made the case for state intervention to promote economic activity in specific sectors. Rather than debate the pros and cons of industrial policy, the primary goal of this chapter is to examine the implications of its return for the future work programme of the WTO.

Evidence on the resort to industrial policy during the crisis era is beginning to pile up. Aggarwal and Evenett (2012) demonstrate how pervasive sectoral – as opposed to across-the-board – intervention has been in seven large trading powers. Furthermore, they show that there is considerable variation across those powers in the degree to which sectoral interventions discriminate against foreign commercial interests *and* between domestic firms. ‘Propping up losers’ as well as ‘picking winners’ are prominent features of crisis-era policy choice. In addition, in 2013, Aggarwal and Evenett commissioned a series of sectoral studies to better understand intervention across the globe in the same area of economic activity.¹ Finally, the OECD, World Bank, and UNCTAD have taken an interest in examining industrial policy choice, and in some cases, promoted selective intervention.

¹ The sectors examined include automobiles, banking, steel, biofuels, petroleum, wide-bodied aircraft and wind power. These papers are currently being revised and are available from the authors upon request.

The momentum behind industrial policy

Broadly speaking, four explanations have been advanced for the industrial policy measures taken during the crisis era when, at the very minimum, national economic growth rates fell below trend. First, intervention has been rationalised on defensive grounds – that is, limiting or slowing down adjustment or mitigating associated costs. Second, some measures have been explained in terms of improving the long-term growth prospects by promoting certain sectors, of which so-called green growth is perhaps the highest profile example.

A third rationale is similar to the second. Here the goal appears to be to restore nationwide economic growth by promoting an activity – innovation is a leading example – that is said to benefit many sectors. Finally, fixing market failures is sometimes used as a rationale for industrial policy intervention.

While these purported rationales for industrial policy existed long before the recent global economic crisis, for many WTO Members their salience and relevance grew once the crisis began. Advocates of industrial policy – long on the defensive – believe that the tide had turned in their favour. Moreover, the imperative of restoring economic growth has been used by some to brush aside objections to industrial policy. What could possibly go wrong?

Why the return of industrial policy matters for the WTO

Given the many ways in which firms seek to supply customers located abroad, any wave of government intervention that affects commercial opportunities should be of interest to WTO Members. The principal concern is not government intervention *per se*, given that such intervention is to be expected during systemic economic crises. Rather, the concern is that such intervention violates the WTO's principle of non-discrimination, including in ways that go beyond what is necessary to attain the policy objectives at hand.

Even where discrimination against foreign commercial interests is necessary to attain an industrial policy goal, it is of interest whether governments have put in place deliberative processes that identify the correct government intervention and that withdraw that intervention when its job is done. Just because a discriminatory industrial policy measure is thought to have worked in one context does not provide *carte blanche* for its uncritical application elsewhere.

These are not hypothetical concerns. Resort to industrial policy in previous eras has involved substantial discrimination against foreign commercial interests, most notably when governments sought to promote so-called national champions, infant industries, and the like. These matters require particular attention because so many discussions of industrial policy are ideological, rather than evidence-based. Can the renewed emphasis on industrial policy be conducted in a manner that does the least violence to the principle of non-discrimination?

Fortunately, the WTO has experience in dealing with forms of government intervention that are pervasive and that are said to be motivated by concerns other than favouritism towards domestic commercial interests. The science-based WTO rules on sanitary and phytosanitary (SPS) regulations come to mind. While the SPS agreement may not be perfect, certain elements of its underlying approach to evaluating policy might be usefully employed in assessing industrial policy initiatives. Likewise, the approach that the competition law community typically uses to assess state interventions that compromise short-run market efficiency could serve as a model as well.

A work programme for the WTO on industrial policy

Over the next two years, the WTO Membership could adopt a constructive work programme that sought to inform state decision-making on industrial policy by examining in depth crisis-era measures taken in key sectors of the global economy. This work programme could draw upon the evidence collected by other international organisations and by independent analysts and researchers. The goal would not be to

negotiate new WTO rules – although the fact-finding and deliberative phase may well identify matters where existing rules need amendment or where new rules might be desirable.

A Working Group open to all WTO Members and supported by the WTO Secretariat could examine crisis-era policy interventions in leading sectors of the global economy. The sectors considered could be chosen so as to be of interest to the broadest range of WTO Members, bearing in mind their different stages of development and sectoral specialisations. For example, given that car assembly is undertaken in many WTO Members and the billions of US dollars of trade in cars, a better understanding of intervention in that sector might be of interest. WTO Members could propose sectors for analysis.

For a given sector, the first stage would involve establishing the factual record concerning several decisions by governments to intervene, bearing in mind that some governments may have contemplated intervention and decided against it. The fact-finding phase would do the following:

- Describe the factors that triggered consideration of government intervention, including possibly intervention by foreign governments in the same sector.
- Identify the purported rationale for government intervention.
- Identify the options a government considered when intervening.
- Identify the metrics used by a government in assessing those interventions.
- Describe the process used by the government in assessing options for intervention, including use of objective evidence, consultation with trading partners, and expertise employed during this process.
- State the decision(s) taken, the form and scope of intervention chosen (where relevant), the financial resources employed, and the duration of the intervention.
- Where a measure was imposed, identify whether the intervention *de facto* or *de jure* discriminates between rival domestic and foreign commercial interests. Here

it would be important to establish whether the discrimination violates the national treatment principle, the most-favoured nation principle, or both.

- Where a measure taken was discriminatory, describe whether the design of the measure deliberately sought to limit the harm done to foreign commercial interests.
- Describe any mechanism used to review the intervention after implementation, the terms of that review, and whether the review was actually undertaken. When a review was undertaken, its findings and any steps taken in the light of the review would be described.
- Describe any evaluation of the effectiveness of the policy intervention undertaken by the implementing government or by a third party.
- Describe whether and when the policy intervention was unwound and the rationale given for unwinding the measure.

Separately, the Working Group should examine the factors responsible for the speed with which government interventions were unwound in those major sectors of the world economy where many measures were imposed during the turbulent decade of the 1970s or the sharp global economic downturn of the early 1980s. During that era, the OECD took the leading role in promoting the unwinding of government intervention in certain sectors and that experience could be drawn upon.

With this evidence, the Working Group could do the following:

- Identify, for each broad motivation for industrial policy, the types of government intervention that do not raise concerns from the perspective of non-discrimination. ‘Safe harbours’ for industrial policy interventions could then be established, which if followed by a WTO member might provide reassurance to trading partners.
- Identify under what circumstances effective industrial policy intervention does not involve violating the most-favoured nation principle.
- Identify and articulate better practices for the processes that WTO Members should follow when considering industrial policy interventions, in particular those interventions that might harm foreign commercial interests.

- Establish principles for the periodic review of industrial policy interventions, including the potential for the removal or amendment of the intervention being reviewed.
- Consider ways to encourage the phasing out of discriminatory industrial policy interventions taken in recent years or, where possible, the substitution of more discriminatory policy instruments with less discriminatory alternatives.

Execution of this work programme would be part of the deliberative function of the WTO. Execution would encourage evidence-informed policymaking by WTO Members as well as the careful consideration of the necessity and form of any discrimination against foreign commercial interests. In so doing, this would reassure trading partners, potentially reduce the number of disputes between WTO Members, and provide government officials with good arguments when resisting self-serving attempts to jump on the industrial policy bandwagon.

Reference

Aggarwal V K and S J Evenett (2012), “Industrial policy choice during the crisis era”, *Oxford Review of Economic Policy* 28(2), pp. 261-283.

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