

The New Economics of Industrial Policy

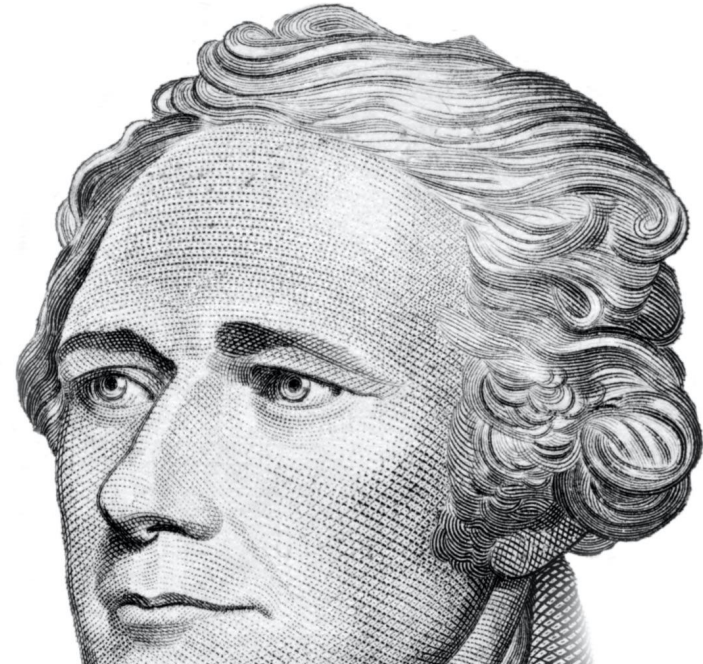
Réka Juhász

October 27

UBC, NBER, CEPR, IPG

Should states shape the composition of economic activity ?

This idea—[industrial policy](#)—has been controversial since 18th century.



Should states shape the composition of economic activity ?

Long history of advocacy.

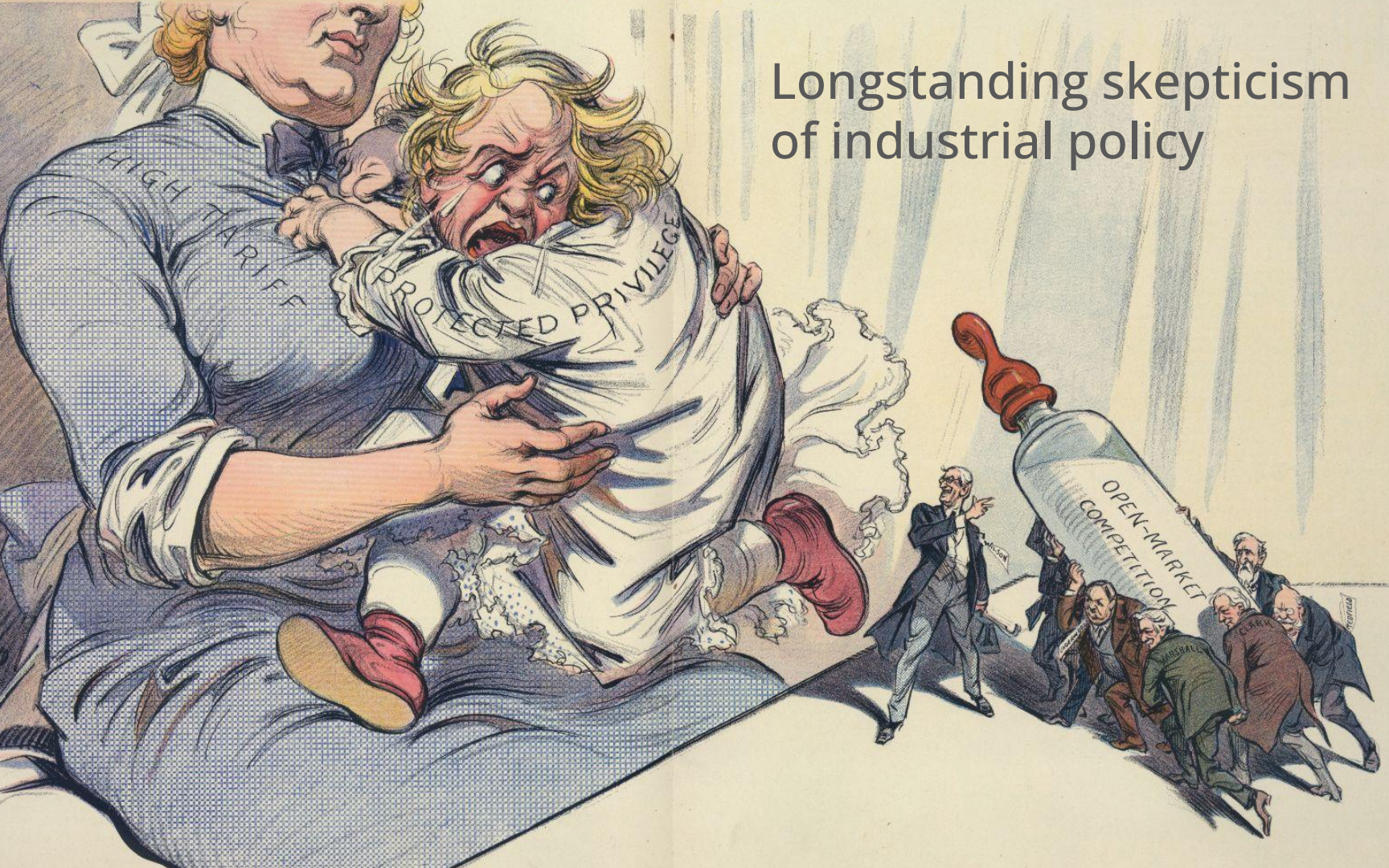
*(**Hamilton 1790**, John Stuart Mill 1848, List 1856, Amsden 1989)*

Long history of skepticism.

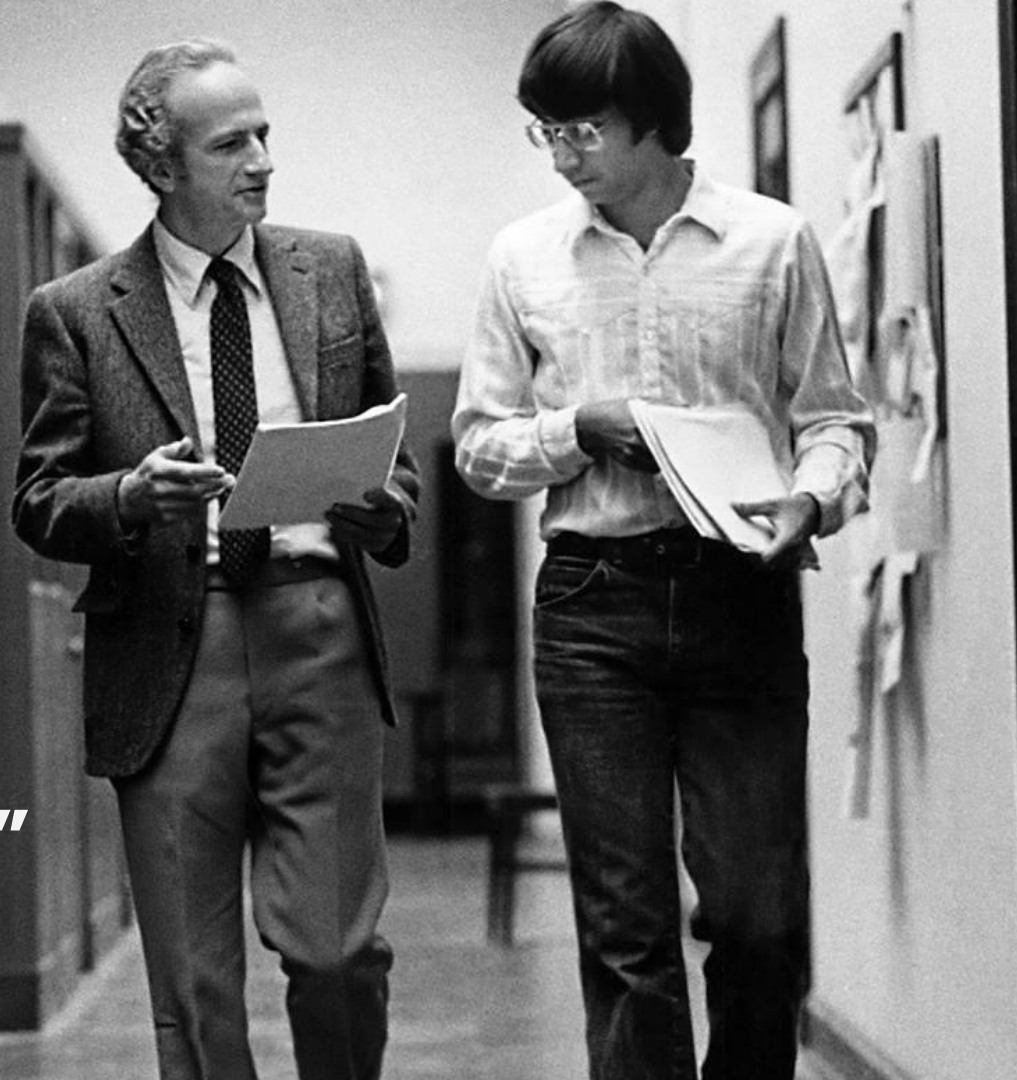
(Smith 1776, Marshall 1903, Becker 1985, Bhagwati 1989)



Longstanding skepticism of industrial policy



**“ The best industrial
policy is none at all ”
Gary Becker, 1985**



BIDENOMICS



INVESTING
AMERICA



BRING
ERS

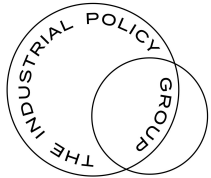


POWERING
COSTS

WEST CO



- Industrial policy is a reality that economics can no longer ignore
- We need less ideological opposition and more careful, work
- The [new economics of industrial policy](#) is an attempt to do just that

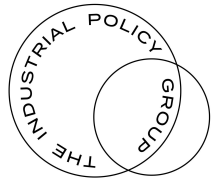


Today

1. What is industrial policy?
2. What is the economic rationale for industrial policy?
3. Why the skepticism?
4. What do we know?
5. Towards a modern political economy of industrial policy

1. What is industrial policy?

Government action that explicitly seeks to transform the structure of economic activity in pursuit of some goal (*e.g.*, defense, energy transition, structural transf.).

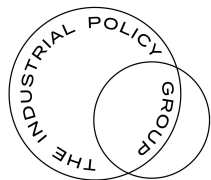


Juhász, Lane, and Rodrik
(2024)

This definition has implications

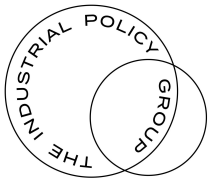
Industrial policy is not necessarily,

- based on specific policy levers (*only tariffs*)
- only sectoral targeting (*only vertical policies*).
- protectionist (*import substitution policy*).
- *'Stuff I don't like'*



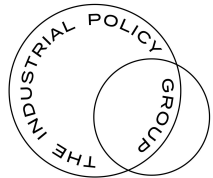
2. What is the justification for industrial policy?

- Scope for policy intervention when there is a market failure
- Similar to any other policy domain
- Justifications are numerous and widely accepted



Theoretical justifications

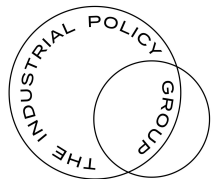
1. *Externalities* - Activity produces externalities not recouped in the revenues generated for those who carry out the activity
2. *Coordination failures* - profitability of an individual producer depends on the level of related economic activities undertaken by others.
3. *Activity-specific public inputs* - Private production depends on the provision of public goods. Implicitly, infrastructural policy often has *de facto* targeted benefits.



3. Objections are practical

- Information problem
- Political capture

Government failure >>> Market failure



A black and white photograph of two men walking down a hallway. The man on the left is older, wearing a suit and tie, and holding a folder. The man on the right is younger, wearing a light-colored button-down shirt and dark pants, and also holding papers. They appear to be in a professional setting, possibly a university or government building. The hallway has wooden paneling on the left and a bulletin board on the right.

**Economists' consensus around industrial
policy emerged before **our discipline's
empirical turn****

The new economics of industrial policy challenges this consensus with

Better measurement

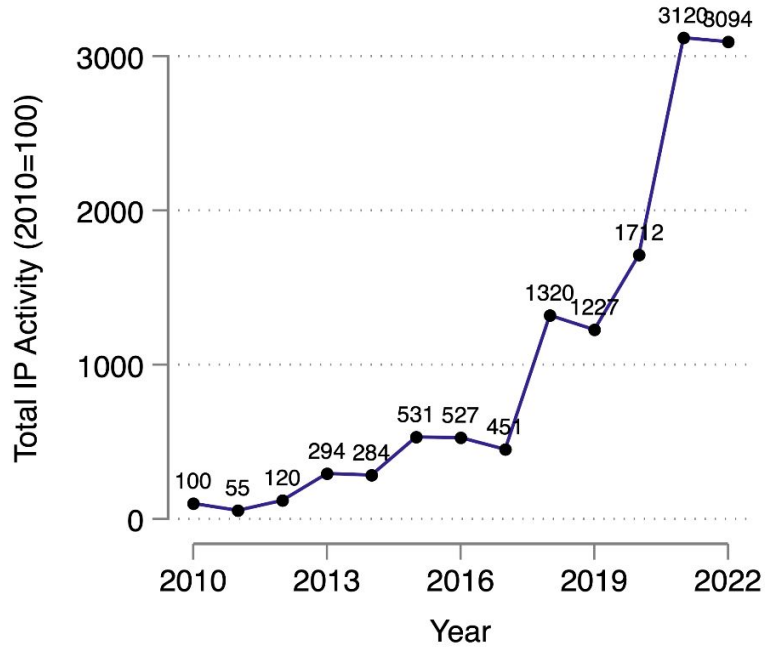
- IP is on the rise, but it never went away
- Widely practiced in advanced economies

Better econometrics

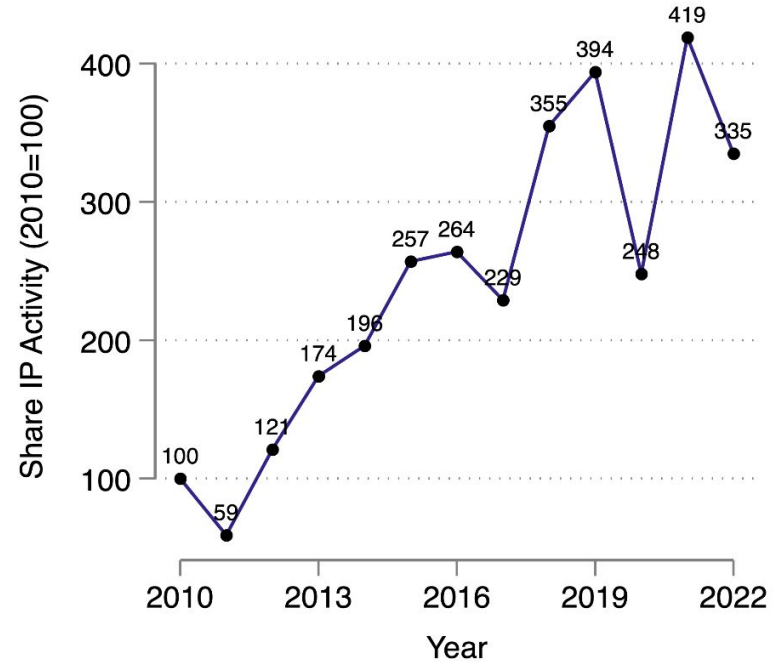
- Overall much more positive take on the effects of IP

Industrial policy is on the rise - across measures of activity

Total number policy activity



Share of total policy activity

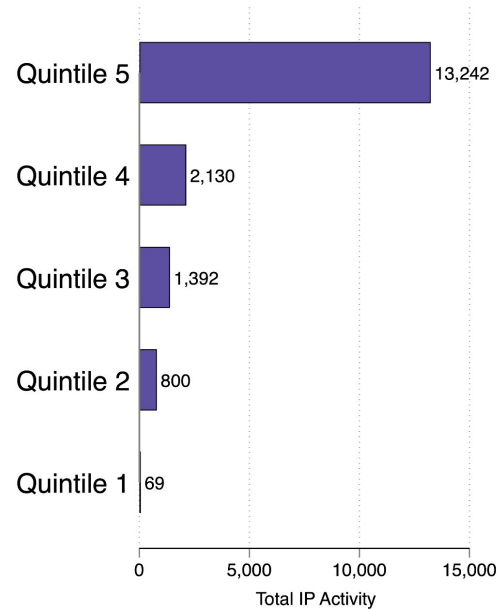


Total and share of industrial policy activity, indexed (2010 = 100)

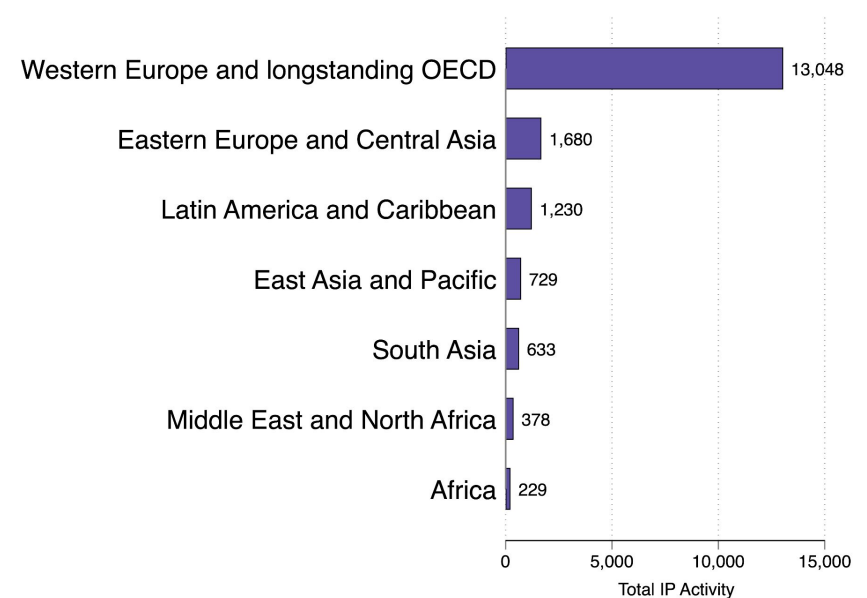
Juhász, Lane, Oehlsen and Perez (2022)

Industrial policy skews toward high-income countries in data

Industrial policy activity, by income quintile



Industrial policy activity, by income region



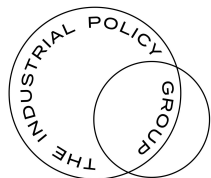
Quintiles based on 2010 GDP per capita. Higher quintiles are higher income.

Juhász, Lane, Oehlsen and Perez (2022)

Empirical evidence

1. Public R&D
2. Place-based industrial policy
3. Infant industry policy

For each, we have some evidence of positive effects
with nuance and conditions



Public R&D: Positive local effects and *crowding-in*?

- (Micro) public R&D *crowds-in* private R&D (Myers Lanahan 2022 AER)
- Canonical US “moonshots” may have had positive effects
 - WW2 R&D effort created *local innovation hubs* and changed the *direction of US technology* (Gross and Sampat cond. acc. AER 2023).
 - Apollo mission had effects on *manufacturing value-added* consistent with other fiscal multipliers (Kantor and Whalley 2023 R&R AER).

“(...) the U.S. government seemed capable of picking technologies, places, and firms that could deliver the desired outcomes, often with long-lasting positive local effects.”

Place-based industrial policy

- Boosting manufacturing in distressed/lagging regions:
 - Evidence from multiple contexts suggests some positive effects on employment, and in some cases wages.
 - [US WW2 manufacturing push](#): Garin and Rothbaum (R&R QJE) finds long-lived, intergenerational effects.
 - Little evidence of local spillovers, but some leakage through multiplant firms.

Infant industry

- New work finds positive effects for traditional infant industry: textiles (Juhász AER 2018, Liu JEH 2019), shipbuilding (Hanlon 2020 JEEA), and heavy industry (Lane 2024, QJE).
- Learning-by-doing seems important:
 - Experimentation and demonstration effects (Juhász, Squicciarini and Voigtlaender 2024, JPE).
 - Microdata can be misleading if there are externalities.
 - **BONUS:** If LBD spillovers have a cross-country component, subsidies may be global complements (vs. race to the bottom) (Goldberg et al. 2024)

5. Towards a modern political economy of IP (Juhász and Lane JEP 2024)

Old view: Government failure >>> Market failure

Deterministic. Does not allow for variation in IP or its success.

Towards a modern political economy of IP (Juhász and Lane JEP 2024)

Political constraints shape policy choice and outcomes.

Green industrial policy vs. “first best” carbon pricing

State capacity constraints shape implementation.

All successful episodes of industrial policy involve investments in building state capacity (see IRA today)

Industrial policy more likely to succeed when it is pursued within governance constraints

Takeaways

- Successful industrial policy works within the local political environment and within state capacity constraints
- Thoughtful policies chosen with an eye towards relaxing future constraints
- In some contexts, `activity-specific public inputs' may be a powerful alternative to subsidies (e.g., Juhász, Sakabe and Weinstein 2024)