



Lessons from Asia for US Industrial Policy

Marcus Noland says that industrial policies favoring “national champions” have produced mixed results for Asian countries—and a cautionary tale for the United States in such areas as autos and “green” technologies.

Edited transcript, recorded November 23, 2009. © Peterson Institute for International Economics.

- Steve Weisman: This is Steve Weisman at the Peterson Institute for International Economics. Marcus Noland, deputy director of the Institute, is here to talk today about whether countries in the recession can use industrial policy to try to export their way back into growth. Marc, thanks for joining me.
- Marcus Noland: It’s my pleasure.
- Steve Weisman: You have studied the example of countries in Asia that are certainly successes in the export field, or have been on and off for decades. President Obama has said that the United States needs to rebalance its economy toward exports and away from imports. Can countries, based on your studies, use industrial policy to try to accomplish that objective?
- Marcus Noland: That’s an interesting question. Historically, countries have used industrial policy, or attempted to use industrial policy, to increase their income by moving into sectors of greater technological sophistication and higher value added. Exports were actually almost a side issue with respect to the Asians in the following sense: The industrial policy planners in these economies realized that the local markets, especially in some of the smaller economies like Korea or Taiwan, were subject to being rigged and exports actually provided a neutral standard by which they could judge whether firms were actually meeting their productivity targets, so to speak. So the exports per se were really not the focus of the policy, but it was something that was used. Some of the specific techniques that were used, including export subsidies, are now banned by the WTO. But I suppose countries again today, if interested, could pursue industrial policies and use export performance as one metric of judging performance.
- Steve Weisman: You studied the examples of Taiwan, Korea, and also Japan. You noted that there is a popular conception that these countries mobilize resources and use their policies to develop so-called national champions. And of course American policymakers say, some of them, that China is doing exactly that now. What do you see when you look at the East Asia Region happening right now in this area?
- Marcus Noland: I think what’s happening in Asia is actually happening all over the world. For at least 10 years, if not longer, there has been a perception in many developing countries and middle-income countries that they had tried the prescriptions of the Washington consensus. It hadn’t worked or it hadn’t generated the type of economic performance they wanted so they were looking for something else.

Steve Weisman: Let me interrupt you and remind our readers and listeners what the Washington consensus is.

Marcus Noland: Actually the phrase was coined by one of our colleagues, John Williamson. It is a series of prescriptions or a primer for economic policy that emphasizes things like relatively low and uniform tariffs, relatively low and even taxes, a competitively valued exchange rate and so on. It's kind of a good governance guide for economics but it's more of a hands-off, nonstate, intervention type prescription. Whether countries actually implemented the Washington consensus or not is something that academics debate. But what I think is simply not debatable is that there is a perception in these countries that they did—that the results were not what they wanted and now, they're looking to these older, more statist models that Asia is associated with.

The other thing that's gone on is in the last year and a half during the economic crisis, you've had governments around the world, including the United States, making all sorts of interventions in the economy—in the financial sector, in the automotive assembly, and so on. And so there is an element of, “do as we say, not as we do.” And I think, broadly, the terrain has been broadened ideologically for what is now considered acceptable by economic policy. You see these sorts of interventions not only in China, as you mentioned, but other countries around the world such as Brazil. I just came back from South Africa and South Africa's policy stance in this field is a hotly debated topic there. So it's something all over the world where people are reconsidering a much broader menu of microeconomic interventions.

Steve Weisman: Do [these interventions] work?

Marcus Noland: Sometimes. I think that one of the great misconceptions is that picking winners was a key to Asian success. If you actually look at the data, what is really striking about Asia is that the resources that were channeled into different sectors were largely channeled into sectors with a lot of organized employment. In Japan, for instance, virtually all of the on-budget subsidies went to either farming or coal mining, not super computers. In fact, the manufacturing sector was taxed on net to support these highly inefficient agriculture and service sectors. And then, some of those funds were sort of recirculated back into these high-tech initiatives.

There are, however, some policy interventions that appear to have worked. In Japan—again to use an example— some of the research consortia that were promoted by the government seemed to have positive payoffs.

Steve Weisman: In what sectors?

Marcus Noland: In sectors like chip development, generally electronics, computers and so on. But what's interesting about those policies is that it does not appear to be the case that simply establishing a research consortium—we tried to emulate that with Sematech here in the United States—is not the key. The key is that the policy was responding to a market failure. In the case of Japan, the way the educational system is organized and, most importantly, the way employment was organized—with a lack of portability of pensions and lifetime employment in a single firm—meant

that the sort of way of circulating ideas that we have, say, in the United States simply didn't exist in Japan. The expertise was bottled up within individual firms. So the consortium was basically a way of generating the type of flow of ideas that we generated in the United States or other economies through other sets of institutions.

So I think the real lessons there are twofold. Number one, whatever intervention you design has to be locally designed to deal with local conditions. And secondly, thinking back to the example of the rice farmers and coal miners, more than textbook economics, it may be important to get the politics right. Picking winners is prone to political capture by special interest groups and even a well-designed policy can go awry because of these basic political factors.

Steve Weisman: Let's discuss two cases of industrial sector intervention in the United States in the last year or two. First, automobiles, which it would appear [that intervention] is more directed at rescuing so that it can produce for domestic consumption, not exports. But still, what's your judgment about whether it's going to work?

Marcus Noland: I think you and I may have somewhat differing instincts on this one. I think that if an industrial policy was justified in the case of the automobile sector, it's basically a downsizing policy, which was also used extensively in places like Japan—they had so-called recession cartels. Basically, the industry had too much capacity. There are clearly certain facilities that can't compete under any reasonable scenario. But what you want to do is provide or cushion the adjustment—especially of local communities. So I think that there is probably a policy to support a rational downsizing, a rationalization of the industry. I'm not sure that's the policy we actually got and again, it has to do with politics.

Steve Weisman: It's certainly not the policy as they discuss it.

Marcus Noland: No, and I think the recent estimates are that the American taxpayer probably is not going to get their money back on the money that's been put into the automobile assemblers. So I think this is the case where maybe there's a justification for public policy intervention. It's probably not the public policy we actually adopted, which for understandable reasons was highly conditioned on the politics in the United States.

Steve Weisman: Now, the other sector is energy. We've heard for years that the United States was going to use its resources to support various different types of energy production, from ethanol to so-called green technologies. And President Obama has even said that these could become part of a new export industry. What's your judgment about that sector?

Marcus Noland: Again, I think it's a very interesting case and I think there are both a kind of textbook economics case to be made and a political economy judgment to be made. The textbook economics case would be to argue that, like the case of Japan where you had institutions and practices in the economy that had this particular effect of keeping ideas and technology bottled up within individual firms. There was a justification for a kind of compensatory policy. You could argue for a number of these energy transportation technologies that we have a history of public policy

interventions that have tilted the playing field in one particular way, that there may be some big kind of upfront costs associated with developing alternatives that we could all agree are desirable in the long run.

And so, there may be public policy justifications for intervening, doing things like perhaps guaranteeing a certain market demand for something like fuel cell technology by making certain public sector vehicles or something, mandating that they use the type of technology and encouraging private firms to invest and compete to meet that almost-guaranteed public sector demand. I can imagine policies like that. At the same time, I think there's a real danger, which is that precisely because we all want to be green, and there is such a moral and ethical kind of endorsement of that, these are arguments that are particularly prone to political capture and twisting in ways that are undesirable. I think just simply looking at the history of the US ethanol program would be a good cautionary tale for green planners over the next decade here in the United States.

Steve Weisman: But in this sector, are there any countries either in Asia or Europe that have had some success?

Marcus Noland: Well, one can argue that other countries around the world developing, for example, high-speed trains have been very successful. Their technology has greatly outstripped ours and one of the reasons is we face, again, particular local historically contingent situations—in our case, the fact that the right of ways are owned by freight companies, not passenger rail companies. So, I mean, there are all sorts of interventions that one might be able to design that would both be productivity enhancing and green.

And I think that the tenor of the times is much more sympathetic to thinking about these sorts of interventions versus the way things may have been, say, 10 years ago. Nevertheless, I think in the United States—in a representative democracy industrial policy is inherently about distribution and in a representative democracy these are intrinsically political decisions. And when one thinks about going down the road of making these interventions, one not only has to think about the textbook economics but one has to ask for some hard judgments about: Do we have a political system and political institutions that are capable of delivering these policies in a relatively efficient manner or are these likely to be twisted and distorted by parochial politics?

Steve Weisman: Marc, let's let our listeners and readers ponder that. Thanks very much for joining us and come back soon.

Marcus Noland: Thank you very much.

