Why Europe needs a return to industrial policy

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The polarisation of Europe

The crisis of 2008 has brought Europe to a depression. The continent has been divided between a »centre« with financial and political power, and a »periphery« with no political influence, high public debt, high unemployment and no hope for recovery. This polarisation is evident in Eurostat data about industrial production. With 2010 data equal to 100, in June 2013 Germany's index was 110.2, Austria's 105.8, Denmark's 106 and France's 102.6. Conversely, Italy's index was 96.9, Spain's 95.9, Portugal's 95.3 and Greece's 93.7 (Eurostat 2013). Taking 2010 as the year of comparison, however, ignores the effects of the first years of the crisis. In Italy industrial production is now 25% lower than in 2008, a fall that is common to most countries of the »periphery« and is leading to a permanent loss of production capacity in most industries. As the »centre« has largely preserved its industrial base and increased its exports to the »periphery«, we are likely to face mounting trade imbalances within Europe that might be addressed either by continuing austerity policies – depressing incomes and imports –, or by renewed capital inflows further expanding private and public debt. In both cases, Europe's periphery is heading towards a spiral of losses of income, jobs, production and exports.

Such a reshaping of Europe's economy is primarily driven by large firms with international systems of production and is affected by national and EU policies. Operating in the pursuit of short term profits, market power and financial rents, firms' responses to the crisis have included the following: drastic downsizing and plant closing; reduction of R&D, innovation and investment; concentration of production in the areas of greater strength and in core businesses; consolidation and acquisitions, leading to more oligopolistic market structures; and a further wave of international relocation of production towards emerging and developing countries with cost advantages and a large potential for growth in domestic markets. These negative consequences have been concentrated in the countries of the »periphery« where the recession has hit hardest.

In a context where European macroeconomic policies resist pressures to stimulate new demand and redistribute income, a generalised return to growth is unlikely. The aftermath of the crisis is likely to be marked by a more polarised industrial structure, where weak countries, regions, industries and firms become weaker, and where also the »centre« may be left with lower demand, and a reduced ability to develop new technologies and economic activities. With a slowdown of overall growth in Europe and economic decline affecting several areas of its »periphery«, change is likely to become more difficult. Europe as a whole would be stuck in its traditional economic trajectory – with sluggish markets, a heavy environmental burden, and growing inequality. .

The return of industrial policies

There is no need, however, to accept such an outcome as inevitable. The twin challenges of the crisis and the need to build a »greener« economy represent an opportunity for orienting economic change towards more desirable and sustainable directions. The tool for achieving such change is simple, well known and effective – *industrial policy*. In Europe, it has driven the highly successful expansion of industrial production from the 1950s to the 1970s. In new industrialised countries it combines public and private efforts to develop knowledge, acquire technologies, invest in new activities, and expand to foreign markets. As argued by Rodrik (2008), the question is not whether industrial policy makes sense, but the way in which it has to be carried out (see also Cimoli et al. 2009; Aghion et al. 2011; Mazzucato 2013).

Industrial policy fell out of fashion in Europe in the last two decades, when governments largely left decisions on the evolution of the economy to markets – that is, to large multinational firms -with waves of liberalisations and privatisation of public enterprises. The argument of such neoliberal policies was that markets are able to operate efficiently both in the short term – concerning the allocation of given resources – and in the long term – when the challenge is developing new activities, resources and markets. Policies lost their selectivity and were limited to automatic mechanisms, such as across-the-board tax incentives for R&D and acquisition of new machinery, or incentives to producers and consumers of goods. The result has been no change in the direction of industrial change and development in Europe.

European policies on the evolution of economic activities have been framed in the Europe 2020 strategy with its three priorities – »smart growth«: an economy based on knowledge and innovation; »sustainable growth«: a resource efficient, greener and more competitive economy; and »inclusive growth« a high-employment economy with social and territorial cohesion. Two »flagship« initiatives are particularly relevant – the »Innovation Union« and »An integrated industrial policy for the globalization era« (European Commission 2010a; 2010b; Lundvall/Lorenz 2010). However, Europe 2020 accepts the neoliberal view that desirable change can result from the operation of markets and that fiscal consolidation and debt reduction create appropriate conditions for long term growth. As a result, the policy directives imposed since 2011 on Greece, Portugal and other countries have put austerity first, cutting public expenditures, R&D and investment and resulting in a weakening of the industrial base.

A different policy perspective is needed that addressed at the European level the joint needs to end the depression and rebuild economic activities in a less polarised continent. Decisions on the future of the industrial structure in Europe have to be brought back into the public domain. A new generation of policies has to overcome the limitations and failures of past experiences – such as collusive practices between political and economic power, heavy bureaucracy, and lack of accountability and entrepreneurship. They have to be creative and selective, with mechanisms of decision making based on the priorities for using public resources that are more democratic, inclusive of different social interests, and open to civil society and trade union voices. They have to introduce new institutions and economic agents, and new rules and business practices that may ensure an effective and efficient implementation of such policies.

The general principles of industrial policy are simple enough. It should favour the evolution of knowledge, technologies and economic activities towards directions that improve economic performances, social conditions and environmental sustainability. It should favour activities and industries characterised by learning processes – by individuals and in organisations -, rapid technological change, scale and scope economies, and a strong growth of demand and productivity. An obvious list would include activities centred on knowledge and information and communication technologies (ICTs), the environment and energy, and health and welfare.

Industrial policies can rely on different policy tools. On the supply side, public funds could support selected R&D, innovation and investment efforts. A public investment bank – as well as nonprofit foundations – could support business start-ups in key fields with credits and venture capital and manage the restructuring of major production activities. A new role could be played by public, community and cooperative enterprises in fields – such as knowledge-based activities, environmental and local services – where public goods and public procurement are prevalent.

On the demand side, far-sighted public procurement, the organisation and regulation of markets with high growth potential, and support and incentives for early users of new technologies could help »pull« innovation and investments, shifting production and consumption towards more sustainable patterns. Policies could also »empower the users«, letting them define specific applications of existing technologies that may lead to new goods and services with large markets. Finally, policies have to build closer relationships among all actors of national and European systems of innovation – firms, financial institutions, universities and policy makers – helping to coordinate decisions of public and private actors.

Knowledge, the environment, and health

Clear priorities for these policies include the following activities.

Knowledge and ICTs: Current change is dominated by the diffusion throughout the economy of the paradigm based on ICTs. Its potential for wider applications, higher productivity and lower prices, and new goods and social benefits should be supported. However, ICTs and web-based activities are reshaping the boundaries between the economic and social spheres, as the success of open source software, copyleft, Wikipedia and peer-to-peer clearly show. Policies should encourage the practice of innovation as a social, cooperative and open process, easing the rules on the access and sharing of knowledge, rather than enforcing and restricting the intellectual property rules designed for a previous technological era.

Environment and energy: The current industrial model has to be deeply transformed in the direction of environmental sustainability. The technological paradigm of the future could be based on »green« products, processes and social organisations, that use much less energy, resources and land, have a much lighter effect on climate and eco-systems, move to renewable energy sources, organise transport systems beyond the dominance of cars, rely on the repair and maintenance of existing goods and infrastructures, and protect nature and the Earth. Such a perspective raises enormous opportunities for research, innovation and new economic and social activities; a new set of coherent policies should address these complex, long-term challenges.

Health and welfare: Europe is an aging continent with the best health system in the world, rooted in its nature of a public service outside the market. Advances in care systems, instrumentation, biotechnologies, genetics and drug research have to be supported and regulated considering their ethical and social consequences. Social innovation may spread in welfare services with a greater role of citizens, users and non-profit organisations, renewed public provision and new forms of self-organisation of communities.

All these fields are characterised by labour intensive production processes and by a requirement of medium and high skills, with the potential to provide »good« jobs. The funding for such policies may be organised in a variety of forms, preferably at the European level. One the one hand, financing through EMU resources could be considered, Eurobonds could be created to fund industrial policies, and a new European Public Investment Bank could be able to borrow funds from the ECB. Funds should in any case be provided beyond the constraints of EMU treaties on national public finances. On the other hand – as suggested by the DGB proposal »A Marshall Plan for Europe« (DGB, 2013) – funds could be raised on financial markets by a new public agency that could obtain the Europe-wide receipts of a once-for-all wealth tax and of the newly introduced Financial Transactions Tax. Moreover, funding arrangements could be different for public investment in non-market activities – such as public goods provision, infrastructures, knowledge, education and health; for public investment in new »strategic« market activities, such as the provision of public capital for new activities in emerging sectors; and for public support to investment by private firms and non profit organisations in »good« market activities that could more easily repay the investment.

These new approaches to industrial policies could play a key role for pulling Europe out of the current crisis. The politics behind such a new departure has to be based on a wide social consensus over the distribution of the productivity and welfare gains deriving from new activities. In the past, firms have benefitted from higher profits and financial rents. Now, workers and citizens should obtain the benefits of new secure jobs, higher real wages, greater economic and social rights and a better quality of work and life.

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