

Industrial Policy in Europe over the Last Century

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What is Industrial Policy?

- Overlaps supply side and regional policies.
- “State intervention that affected, or was intended to affect, industry but not other economic activities directly”
- Allows industry as an instrument as well as a target
- But excludes monetary policy
- Why restrict ‘industry’ to manufacturing?
Infrastructure a traditional intervention point.

Theory of Industrial Policy

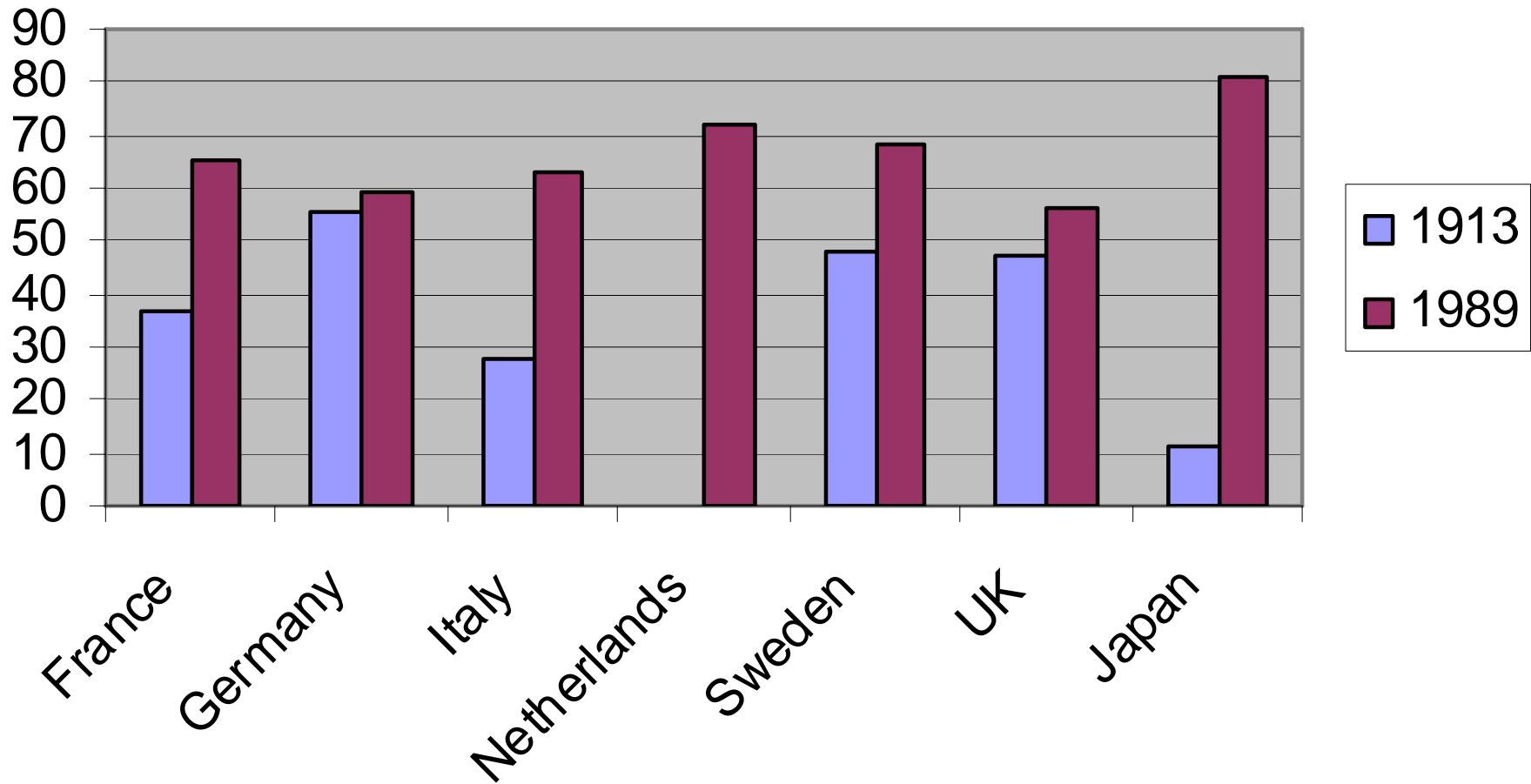
- Explains and predicts effectiveness and efficiency of policy intervention.
- Controversy over completeness and efficiency of markets and
- Pervasiveness of increasing returns and externalities
- Generate different views about consequences of intervention.

A 'Natural Experiment' for IP

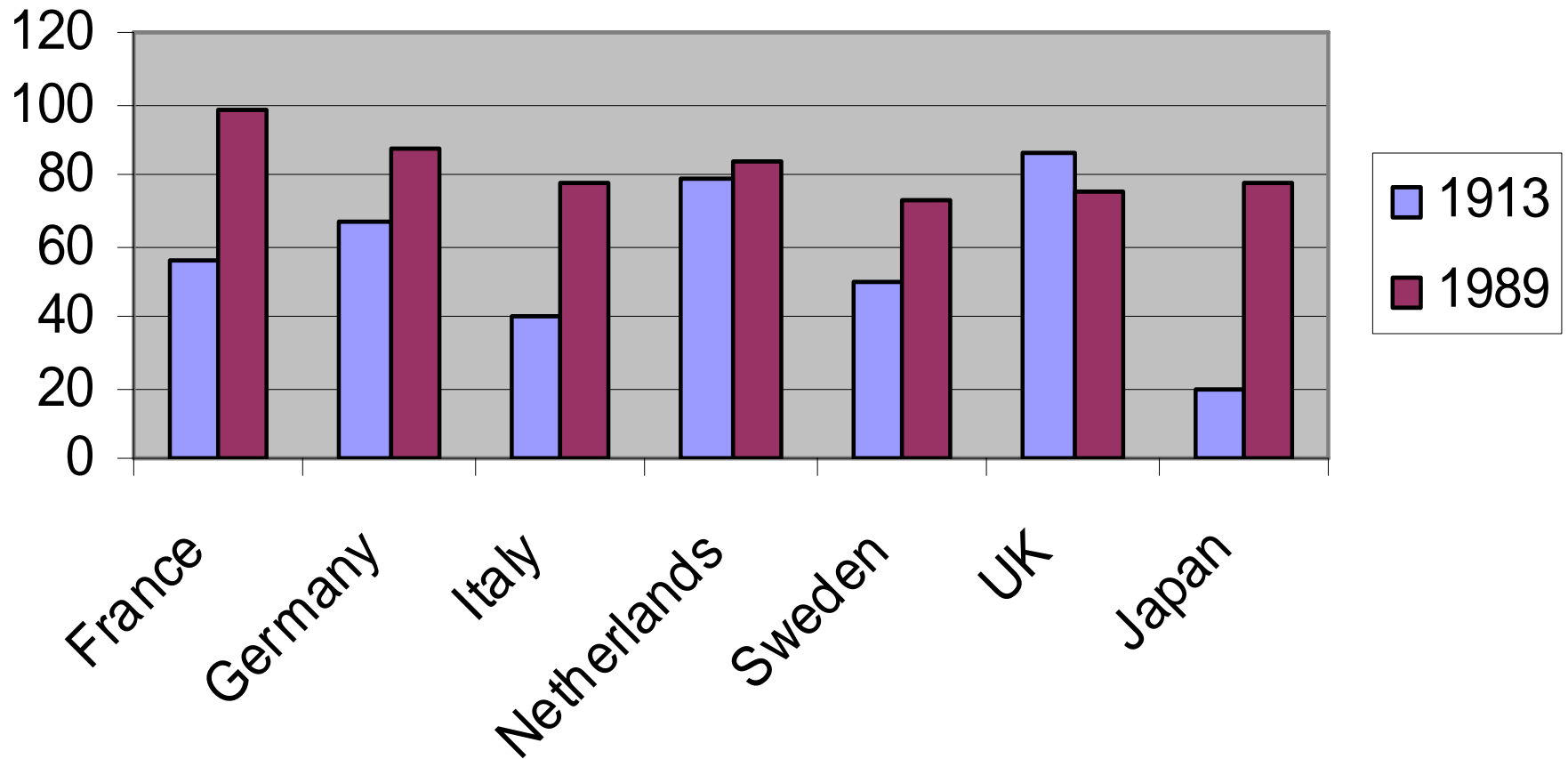
Impact: Europe v US

- Free trade area size, gains from trade and increasing returns
- US manufacturing labour productivity and TFP usually higher than Europe's 1913
- Natural resource abundance?
- In Europe Britain achieved highest GDP per head by specialising
- Despite Germany and Sweden's higher manufacturing productivity

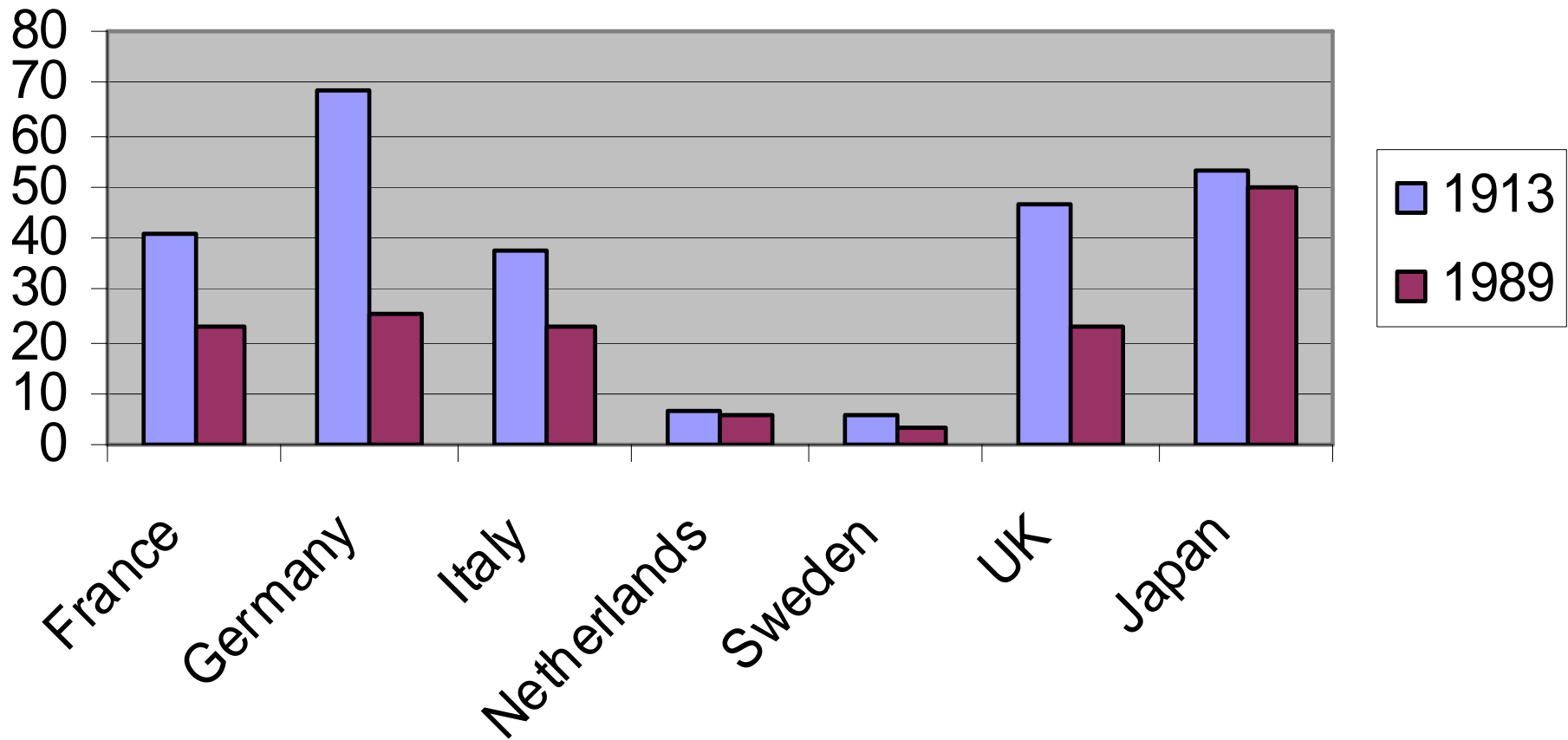
Comparative Labour Productivity in Manufacturing 1913 and 1989 (US=100)



Comparative Labour productivity for the Whole Economy 1913 and 1989 (US GDP per employee =100)



Comparative Population 1913 and 1989 (US=100) (unadjusted for boundary changes)



- Strongest catch up when transport and trade costs fall in Europe
- Despite faster population growth in US.
- European productivity grew faster than US 1970-2000
- Output per head in Europe is 30% lower than in US because
- fewer people work and employees work fewer hours.
- One third due to taxation (Blanchard 2004)
- The rest is preferences- work is not everything

Drivers of Industrial Policy

- **Political economy of industrial policy** - 'Capture' by special interest groups and lobbies,
- Lobbyists were unlikely to find general subsidies worth pressing for;
- Instead they pushed up sector- and firm-specific support
- More **capital rents in large countries**; Britain, France, Germany, Italy, Russia, could afford more intervention
- Also cover more easily the largely fixed costs of hi-tech defence.
- Larger free trade areas so IP cost less

Other motives for, or principles behind, industrial policy intervention;

- a) belief in effectiveness (peak 1940s-1970s)
- b) promotion of national defence and order (inc. bail outs),
- c) budgetary stringency (German rail nationalisation pre-1WW, privatisations from 1980s).

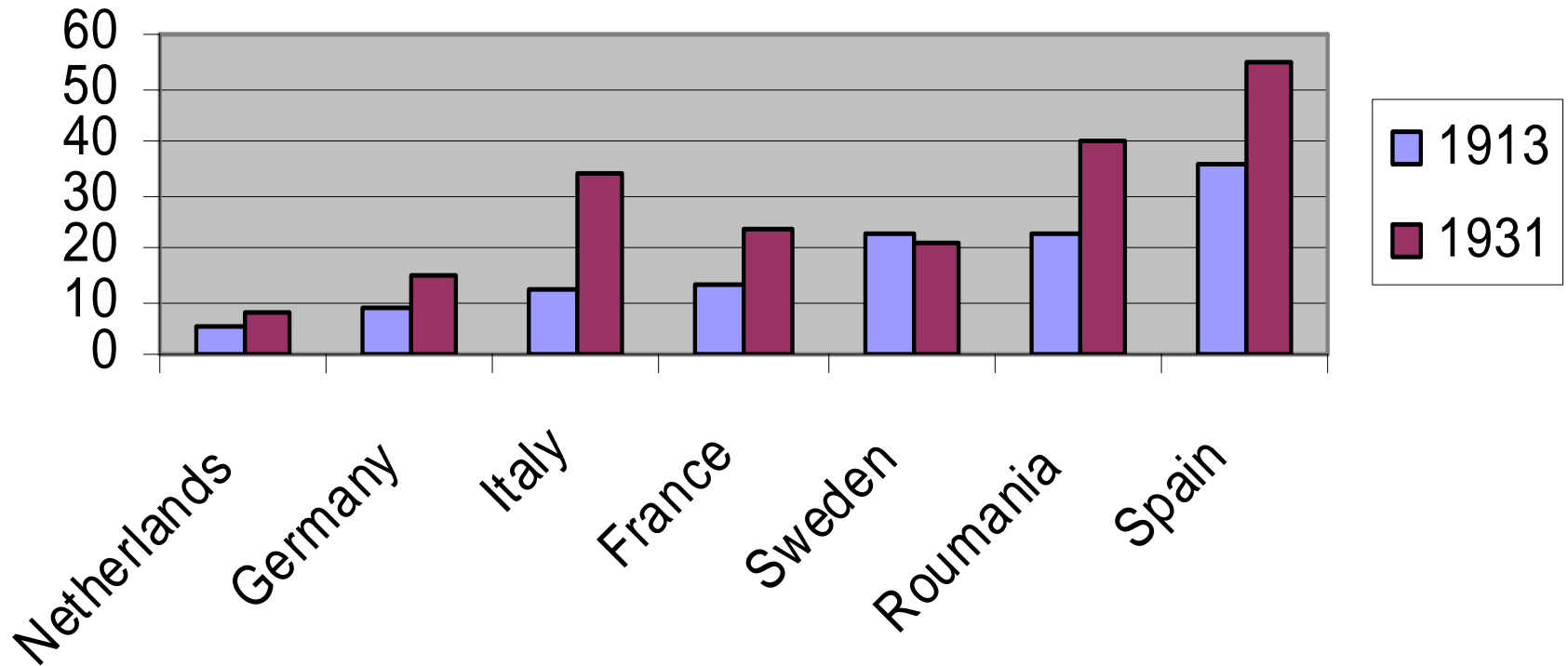
Phases of Industrial Policy in the Long Twentieth Century

- Phases or epochs are distinguished by the challenges or environment of industrial policy and the different policies pursued.
- ***Phase (i) Liberal Industrial Policies to 1914***
- Trade Controls as an Industrial Policy Instrument
- Infrastructure Policy- Freycinet , Baudin Plans
- Manufacturing Industry: State Ownership and Purchasing (Spain, Russia shipbuilding)
- Technology and Patents Policy- Dutch and Swiss free rides

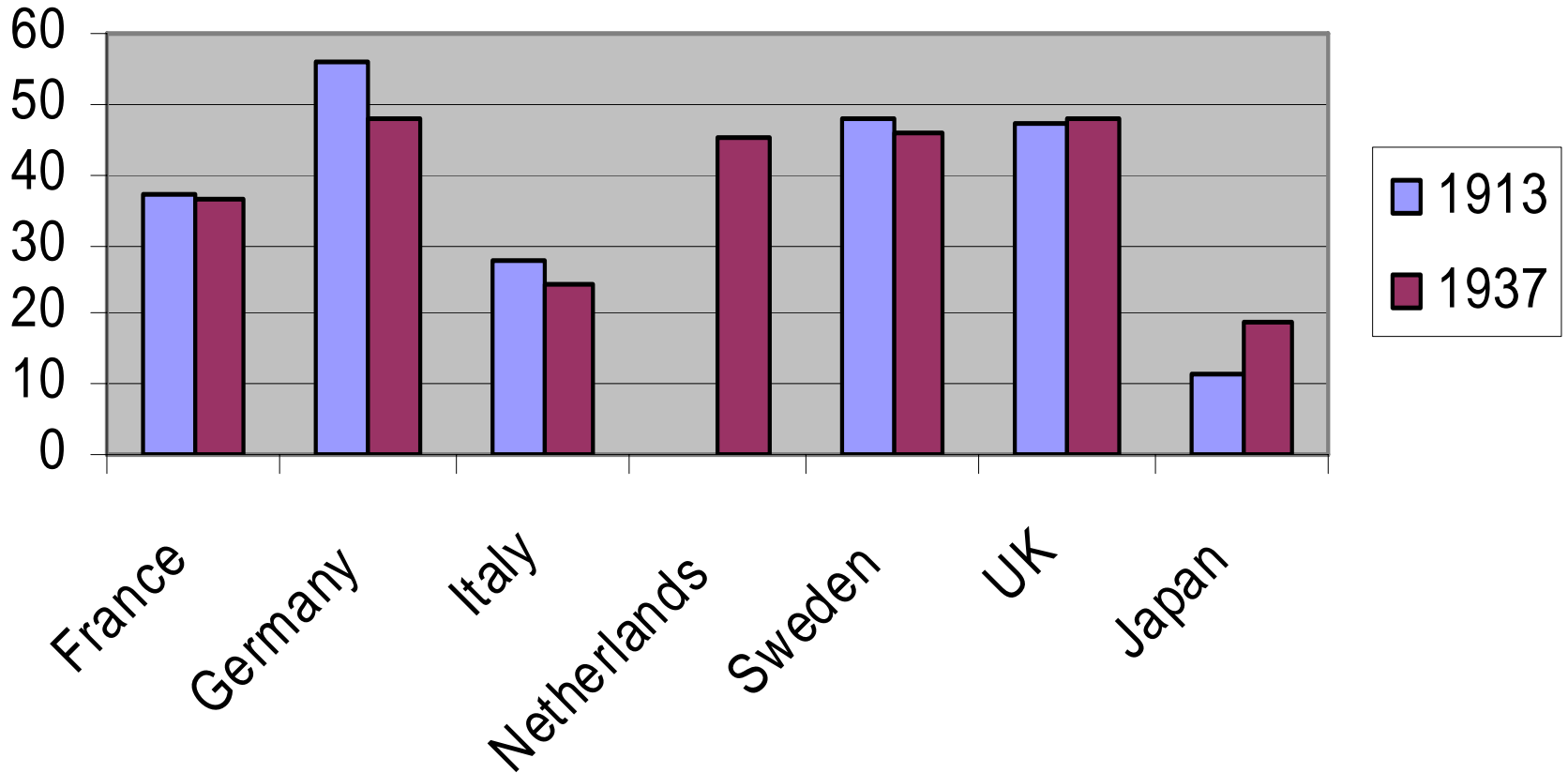
Phase (ii) Wars and World Depression: the Spread of Interventionism 1914-50

- More aggressive nationalism with lengthened boundaries a pervasive basis for industrial policy.
- Military demands and
- bankruptcy of large employers (Citroen bail out 1934), coupled with
- a discrediting of free markets,
- raised the proportion of national income that the state directly influenced.
- Mussolini's IRI holding company for large bankrupt manufacturers, bailed out by the state in the 1930s,
- The model for Franco's INI, the core of Spanish industrial policy from the 1940s for a generation.

Most Favourable Minimum General Tariff as a Percentage of International Price 1913 and 1931 (UK)



Comparative Manufacturing Labour Productivity 1913 and 1937 (US=100)



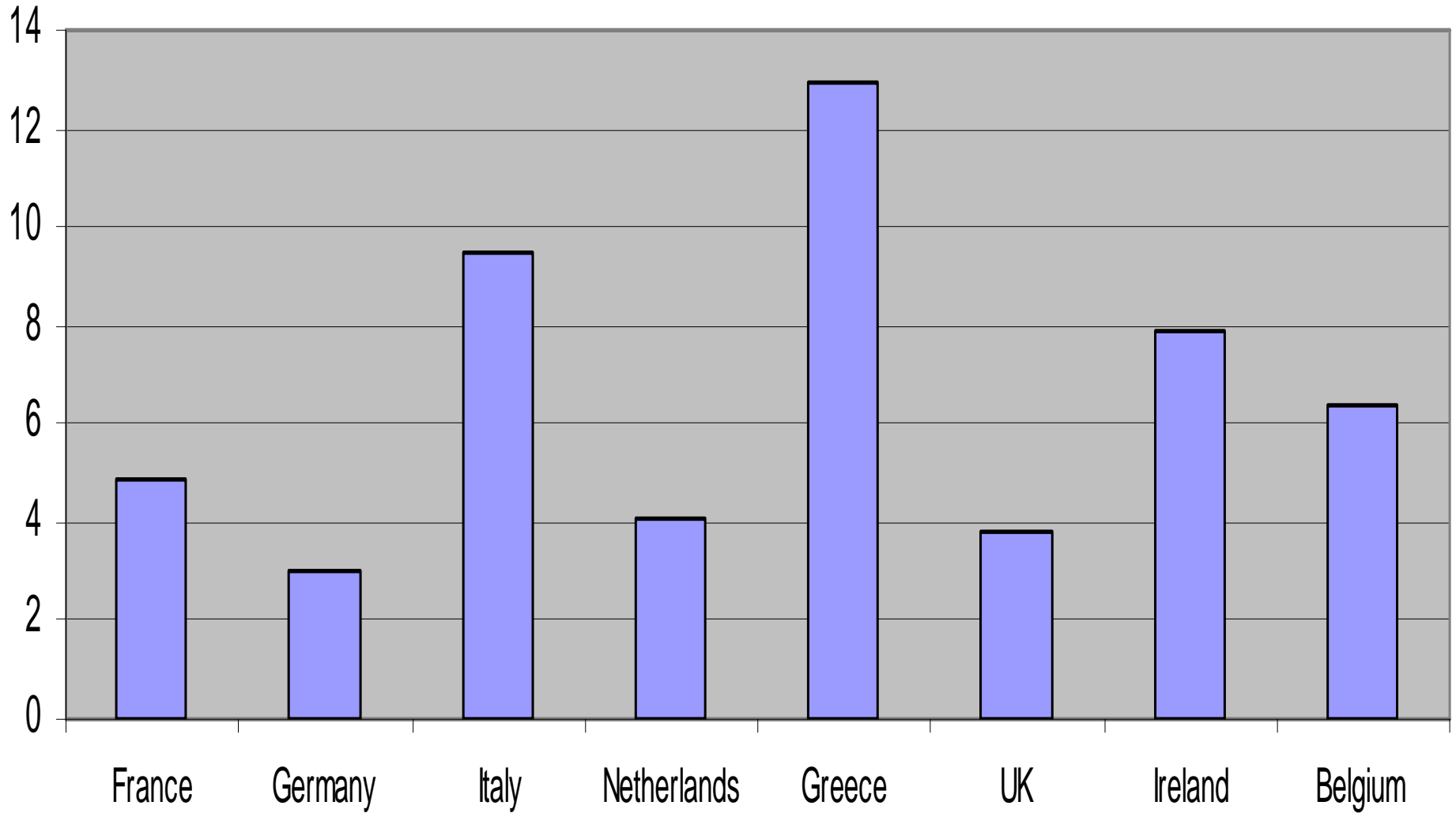
Phase iii The Great Post-War Boom: Reintegration in the West 1950-1973

- The European economies grew uniquely fast.
- International capital, trade and migration flows increased more than proportionately with the growth of production
- Yet independent national economic policies pursued. (eg 3i predecessors filled market gap in UK)
- Cost of military and defence-related technologies - jet aircraft, computers, nuclear reactors – soared. ‘Grand projects’
- All strong reasons for European cooperation and coordination
- 1950: the European Coal and Steel Community

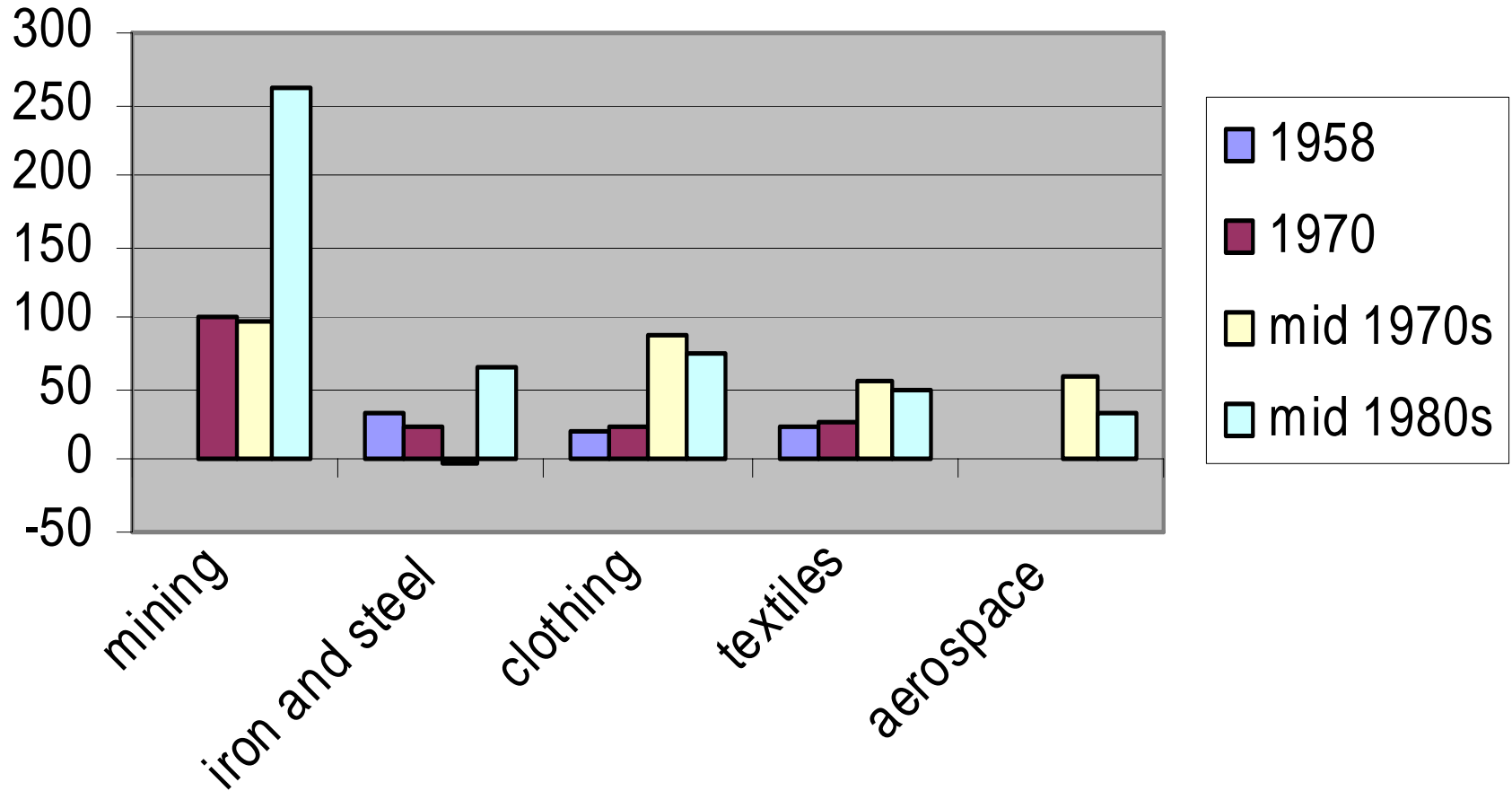
Phase (iv) Globalisation and Deindustrialisation: Euroclerosis 1973 +?

- Oil shocks 1970s
- Productivity slow down
- Wage pressure
- Industrial crises and subsidies (BL v VW)
- Deindustrialization and unemployment
- Governments held stakes in the motor industries in Austria, France, Britain, Italy, the Netherlands, and West Germany.
- State ownership of railways and the postal service was complete

Manufacturing Subsidy as Percentage of Sector Value Added 1981-6



Effective Rates of Assistance to Selected Sectors of West German Industry



Privatisation in the 1980s

- State-owned industries in Portugal and Greece produced over 20 % of GDP, and France and Italy were not far behind.
- By contrast, privatization had radically altered Britain's position in 1991 compared with the 1970s.
- Most European governments disposed of some State assets in the 1980s,
- But only Britain and France (at a considerable distance) shifted the private-public industrial boundaries

Lessons

1. Policies to boost free trade and competition enhance productivity judging by differences between US and European industrial geography at the beginning of the twentieth century,
 - Gap narrowed when Europe integrated.
 - Britain leant the least against the wind of market specialization and had the highest gains from trade.
 - More workers were in higher productivity sectors, although Britain was not a European productivity leader in all sectors. Human capital policy deficiency?

2. 'Grand projects' are very expensive in all epochs and never efficient even when effective- Concorde, VFW, Baudin, Freycinet, AGR nuclear programme (probably even Airbus)..
3. Filling gaps in markets and institutions efficiently does seem possible. 3i and perhaps ECGD.
4. In such cases, autonomy, trust and competency necessary – Netherlands policy, in Italy 1950s Mattei, Singaglia. But problematic given need for accountability for public money

- **5. Drivers-** Beware of special interests
- Ensure crisis subsidies taper off rapidly
- Seek more efficient international cooperation on hitech projects (Airbus, Tornado, Jaguar)
- Acknowledge constraints imposed by internationally mobile capital (eg when taxing and subsidizing footloose industry)