



# COMPETITIVENESS AND STRUCTURAL CHANGE

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This project is supported by  
the European Union

Istanbul, 28 January 2014





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# **How does competitiveness relate to growth, economic development, and industrial policy?**



# Competitiveness I

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- Not a concept based on mainstream economic theory, other from economics trade, development economics or growth theory
- For economists companies not countries compete among themselves
- Governments are expected to build an enabling environment fostering fair competition domestically and internationally, so that companies will become more competitive



# Competitiveness II

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- Country competitiveness: no zero sum game, but actually the contrary. See impact of China's growth on SEA or Brazil
- The concept of country competitiveness comes more from the strategic management literature
- It is a catching but imprecise term, an “umbrella” definition useful to cover many different but complementary policy areas, but is underpinned by productivity dynamic



# Economic glossary

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- The concept of country competitiveness is often related or mixed up with other economic concepts:
  - Economic growth
  - Economic development
  - Industrial policy



# Agenda

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# Economic growth

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- **Economic growth** is the increase in the amount of the goods and services produced by an economy over time. It is conventionally measured as the percent rate of increase in *real gross domestic product*, or *real GDP*.
- Different ways to measure it: International prices or Purchasing Power Parity . Preferable measure: Income per capita (inter. Prices, PPP)
- GDP or GNP (gross national product)?



# Economic growth

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- What generates economic growth? huge debate among economists.
- Broad consensus: productivity dynamic underpins economic growth
- Factor productivity and total factor productivity

$$y = a + bL + cK + \text{error} \quad L = \text{Labor} \quad K = \text{Capital}$$





# Economic growth

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- What is in the error or residual called total factor productivity?
- Technological innovation
- Quality of the investment climate?
- Measurement errors

*Technological innovation + better investment climate*   
*higher productivity*  *Country more competitive*



# Economic Growth

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- The rate of technological innovation is independent or correlated to the level of economic growth?
- What about the quality of the investment climate? Countries become richer because have better institutions or have better institutions because are richer?
- Different answers lead to different policy recommendations.
- Are free markets and open generating automatically more economic growth?



# Agenda

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  - Economic growth
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# Economic development

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- Broader concept than economic growth
- Welfare indicators
- Sustainability
- Inequality and poverty reduction

 Agenda

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- The concept of country competitiveness is often related or mixed up with other economic concepts:
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# Industrial Policy (I): different definitions

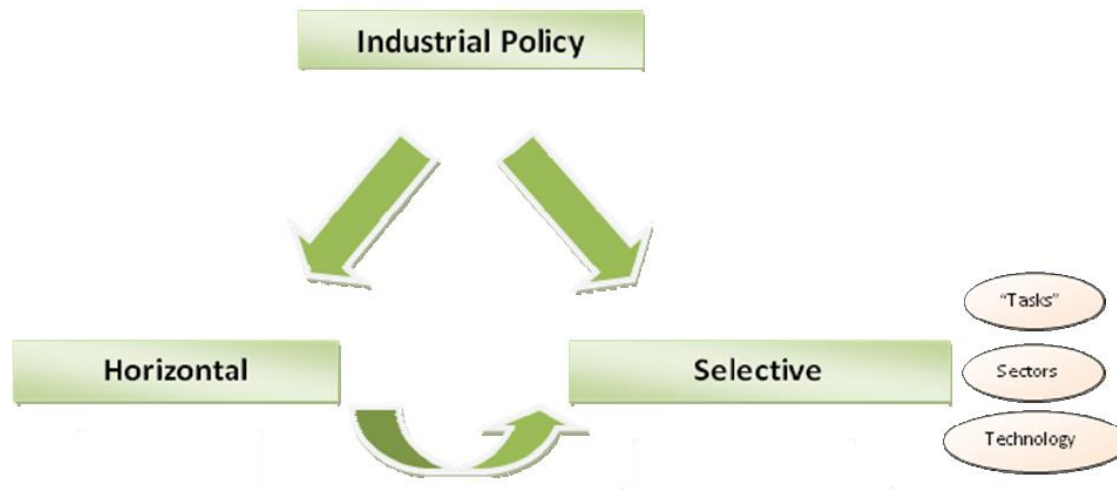
*“Industrial Policy is any type of intervention or government policy*

- that attempts to improve the business environment or*
- to alter the structure of economic activity*

*toward sectors, technologies or tasks*

- that are expected to offer better prospects for economic growth or*
- societal welfare*

*than would occur in the absence of such intervention, i.e., in the market equilibrium.”*





# The Resurgence of Industrial Policy (II)

## Other Definitions

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### Industrial policy is ...

- bringing together a horizontal basis and sectoral application with considerations for the whole value and supply chain and emphasising the need for cooperation and coordination of efforts between the European Commission and the Member States. (European Commission, 2010)
  - any policy that stimulates economic activities and promotes structural change. (Rodrik, 2008)
  - the activity which creates a favourable environment for European business in general, the manufacturing sector and its industries, in specific. (Aiginger and Sieber, 2005)
  - a set of measures taken by a government and aiming at influencing a country's performance towards a desired objective. (Pitelis, 2006)
  - any policy that shapes or influences the competitiveness of a country's firms and industries. (Beath , 2002)
- In brief: industrial policy is **economic growth PLUS structural change**



# The Resurgence of Industrial Policy (III)

## The Rationale

### 1940-1960s

Industrialisation is necessary for development. Industrial policy is needed to go against market failures.

### 1970s-1990s

Government failures are considered to be worse than market failures. Washington consensus. There is no need for an “active” industrial policy.

### 2000s to present

There are market and government failures. The focus is not on the “why” of industrial policies, but on “how” industrial policies should be designed.

**Policies:** infant industry protection, promotion of national champions, subsidies, preferential procurement policies, etc.

**Policies:** the role of the government is only to ensure “framework conditions” (e.g. macroeconomic and financial stability).

**Policies:** focus on the institutional setting, the government and the private sector should coordinate, target on activities, etc.





# The Resurgence of Industrial Policy (IV)

## Addressing the Risks

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- Industrial policy implies risks related to **the lack of government omniscience** as well as to **rent-seeking** or corruption of government officials.
- In order to address such risks, the new industrial policy seeks to apply the following **institutional design features** (Rodrik, 2008):

- **Embeddedness**

Need for a strategic collaboration and coordination (“embedded autonomy”) between the private sector, the government and society at large

- **Carrots and Sticks**

Provision of necessary incentives (subsidies, tax incentives, etc.) to encourage new industrial activities; introducing criteria for success and failure (ex. conditionality, sunset clauses, program reviews, etc.)

- **Accountability**

The need for transparent design of policies and decision making



# The Resurgence of Industrial Policy (V)

## Relevance for Middle-Income Economies

Globally, the ranks of **middle-income economies** have increased over the last 20 years, with low income countries catching-up at higher rate than middle-income economies graduating to the high income group.

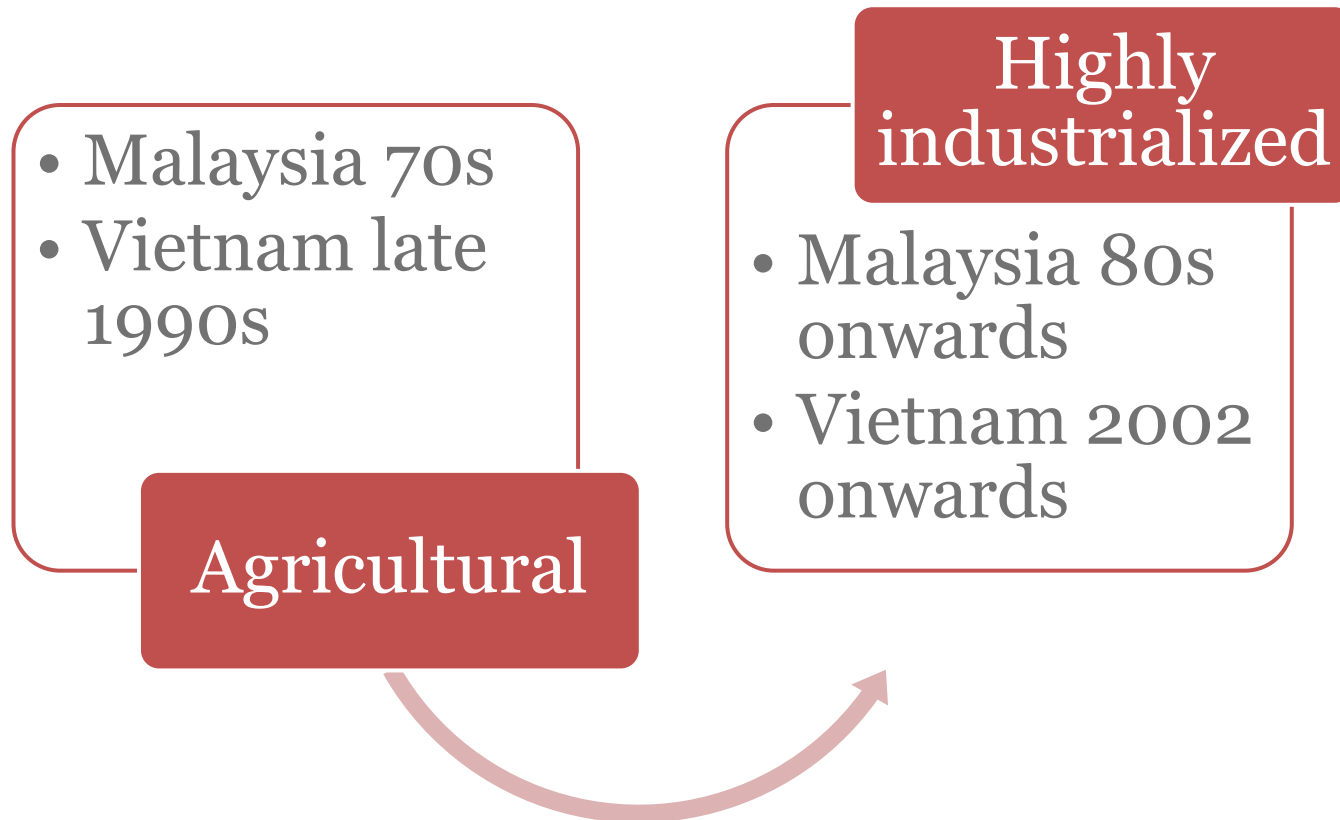
From both practitioner and academic circles, there are increasing concerns about **the middle-income trap**, as economies find that they cannot compete with lower-wage countries and cannot yet compete in technology-intensive good and services with higher-wage countries.

Typically, countries trapped at middle-income level have:

- 1) lower investment ratios
- 2) slower manufacturing growth
- 3) limited industrial diversification
- 4) poor labor market conditions

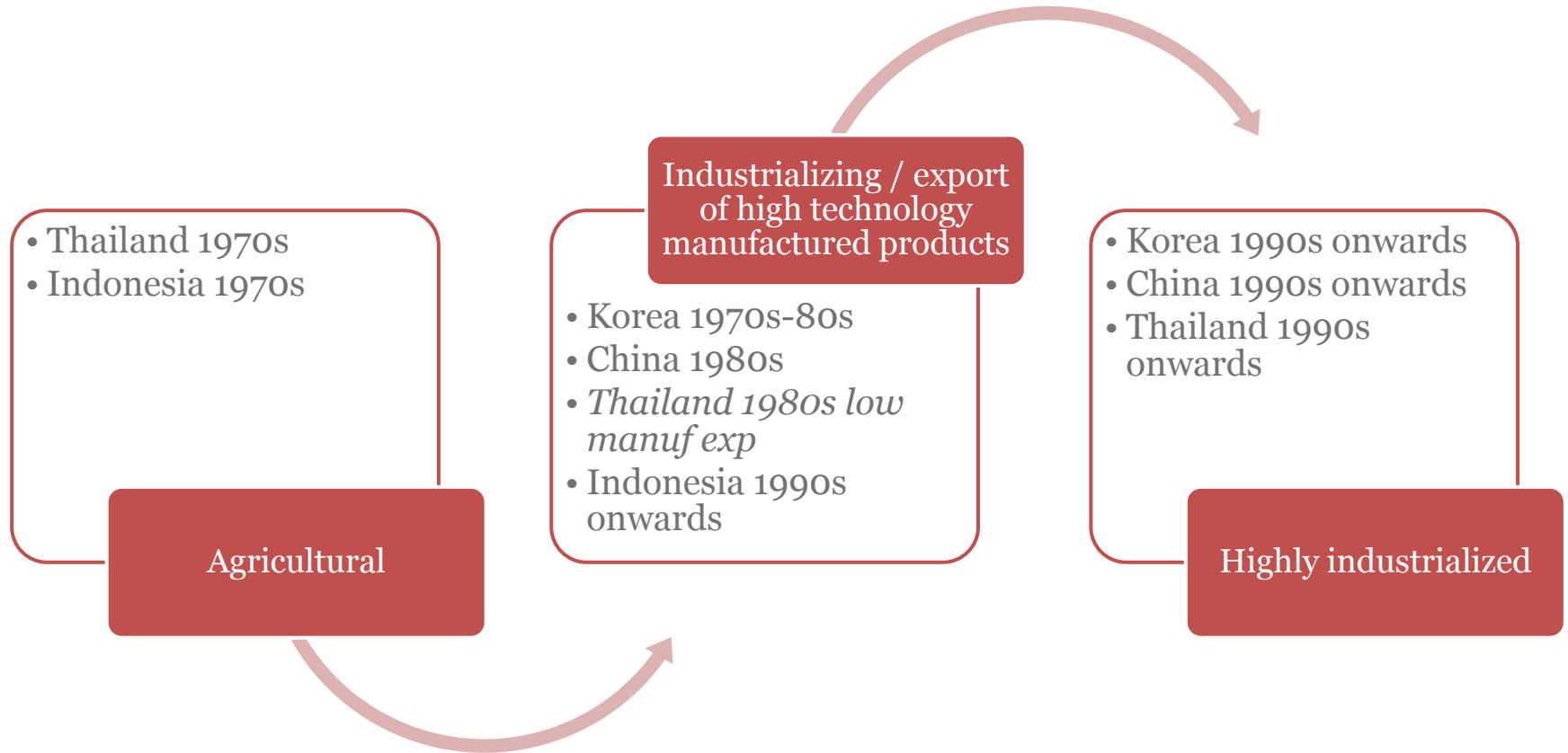


# Successful trajectories of structural change (1)





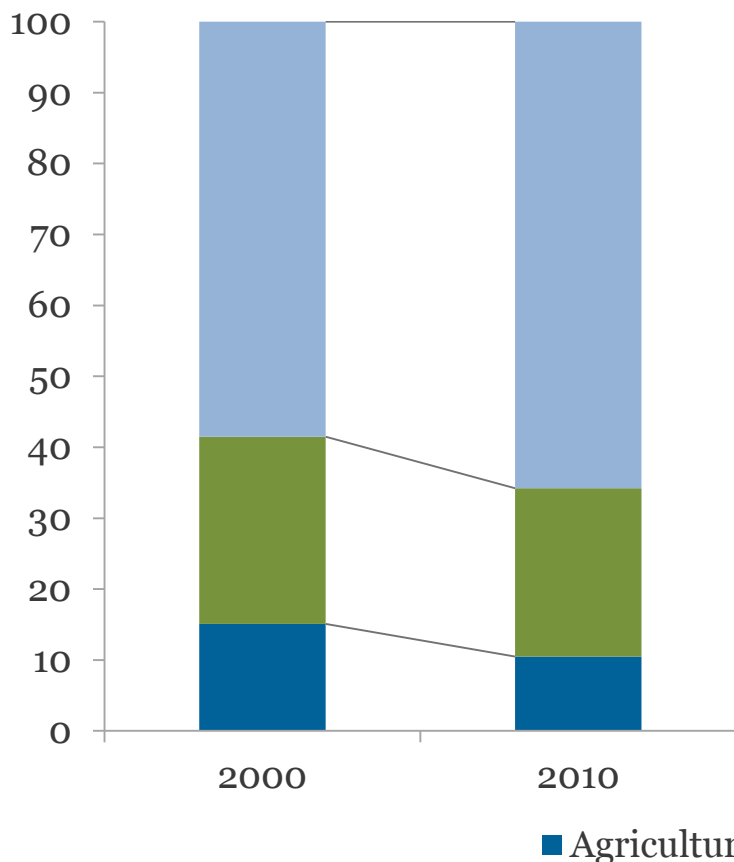
# Successful trajectories of structural change (2)



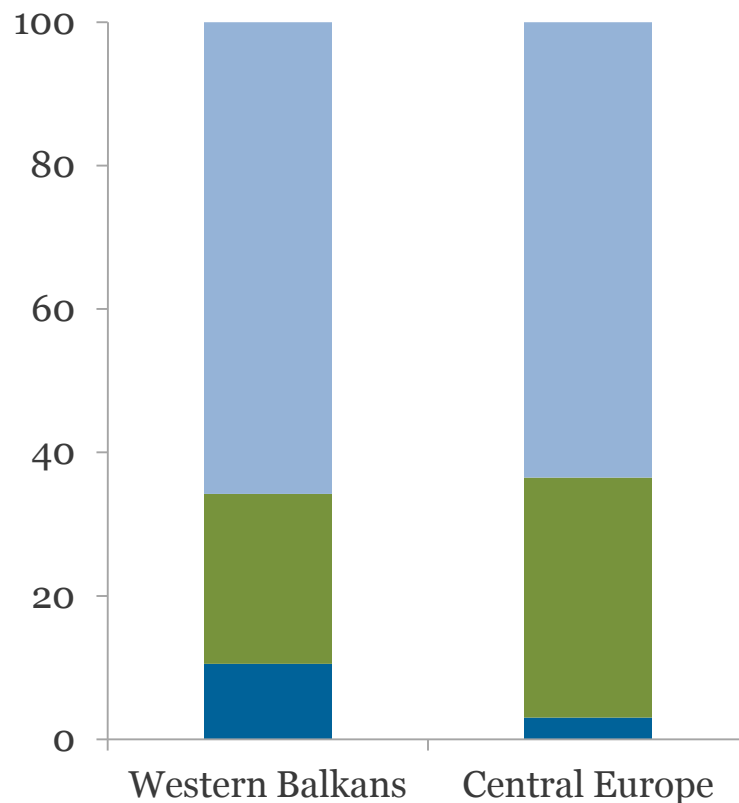


# The case of Western Balkans (1): Services account for the largest and increasing share of GDP

**Sectors' share of GDP in  
the Western Balkans**



**Sectors' share of GDP in 2010  
in the WB and CE**





# The case of Western Balkans (2): Food, metals and chemicals account for most of manufacturing turnover

## Top 10 manufacturing sectors in CEFTA by turnover (yearly average 2008-10)

Industry	Turnover (EUR bn)	Share	Employment	Share
Food products and beverages	12.0	28%	222521	21%
Basic metals	3.7	9%	46582	4%
Fabricated metal products	3.5	8%	98772	9%
Chemicals and chemical products	3.4	8%	46816	4%
Non-metallic mineral products (glass, ceramics, cement, stone products, etc.)	2.8	7%	60206	6%
Coke, refined petroleum and nuclear fuel	2.8	7%	10593	1%
Textiles, apparel and leather	2.0	5%	207988	19%
Rubber and plastic products	1.7	4%	43452	4%
Electrical machinery and apparatus, nec	1.4	3%	37509	3%
Furniture and other manufacturing	1.2	3%	52953	5%

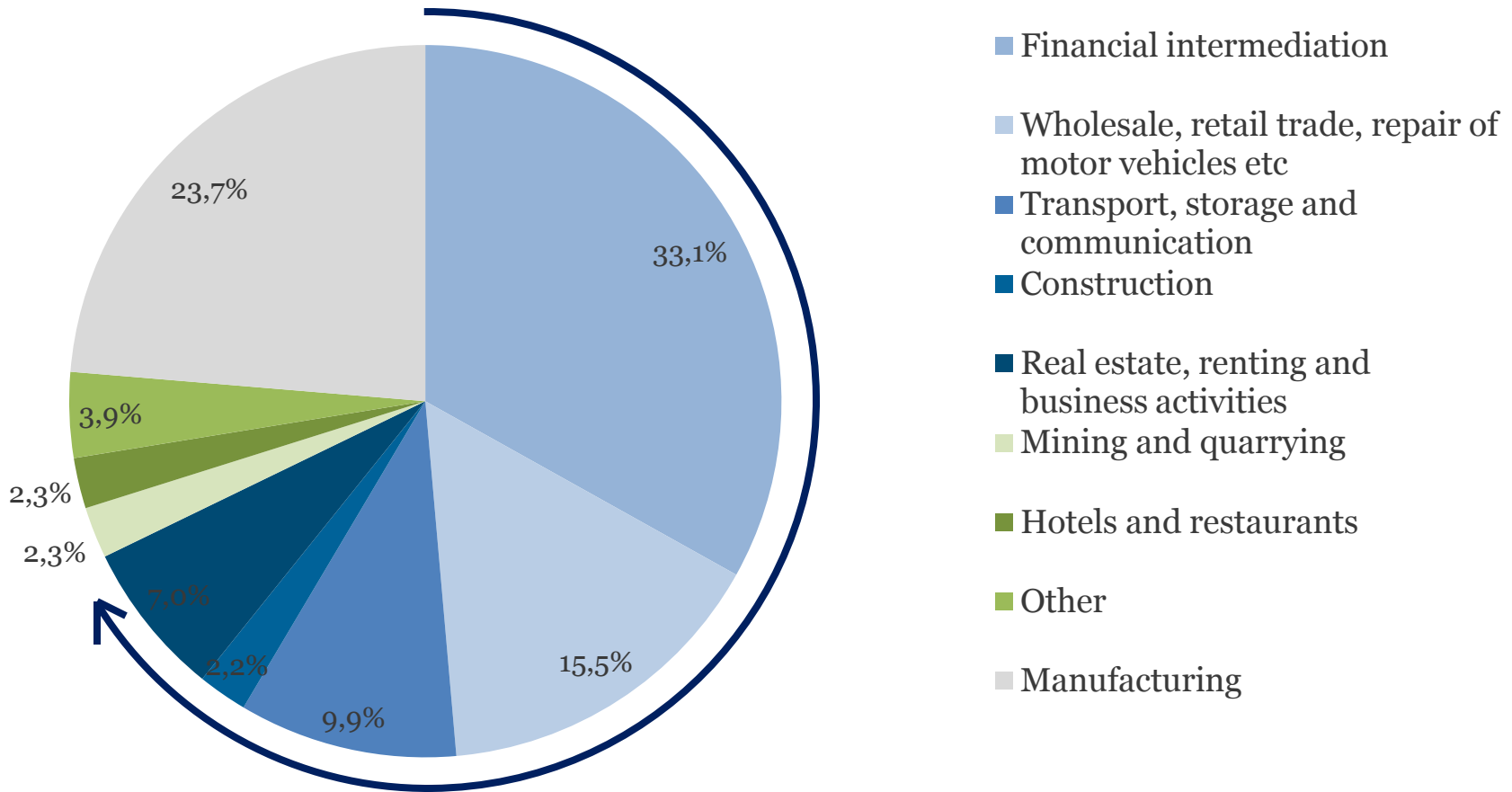
Source: OECD (2012)

Nb- CEFTA includes Moldova as well as the Western Balkan economies.



# The case of Western Balkans (3): FDI has been mainly market-seeking and concentrated in services

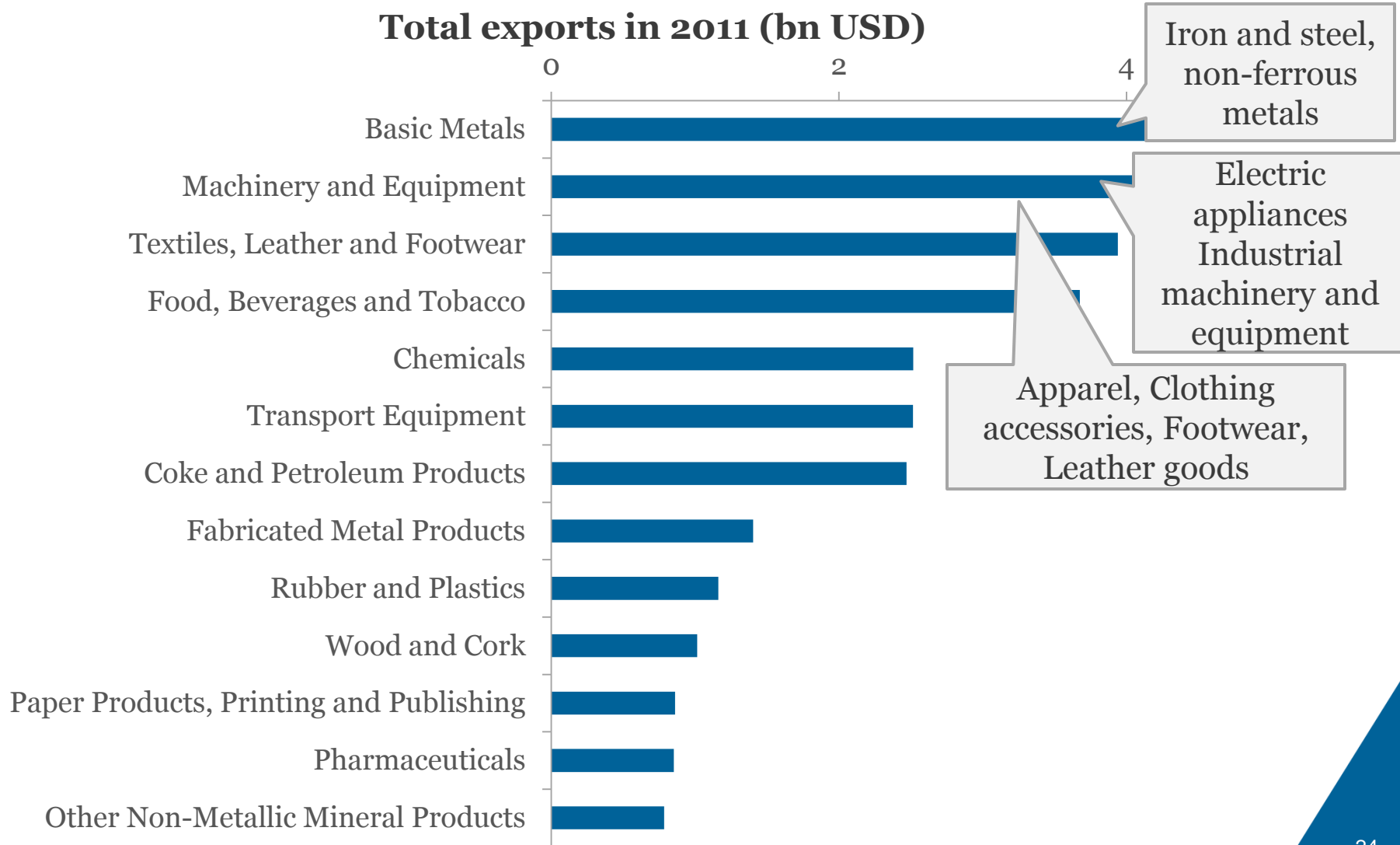
**FDI Stocks by Activity in 2010 (% of Total FDI Stocks)**



NB: Data include Albania, Bosnia and Herzegovina, Croatia and the FYR Macedonia



# The case of Western Balkans (4): The top exporting industries are basic metals, machinery and equipment and textiles

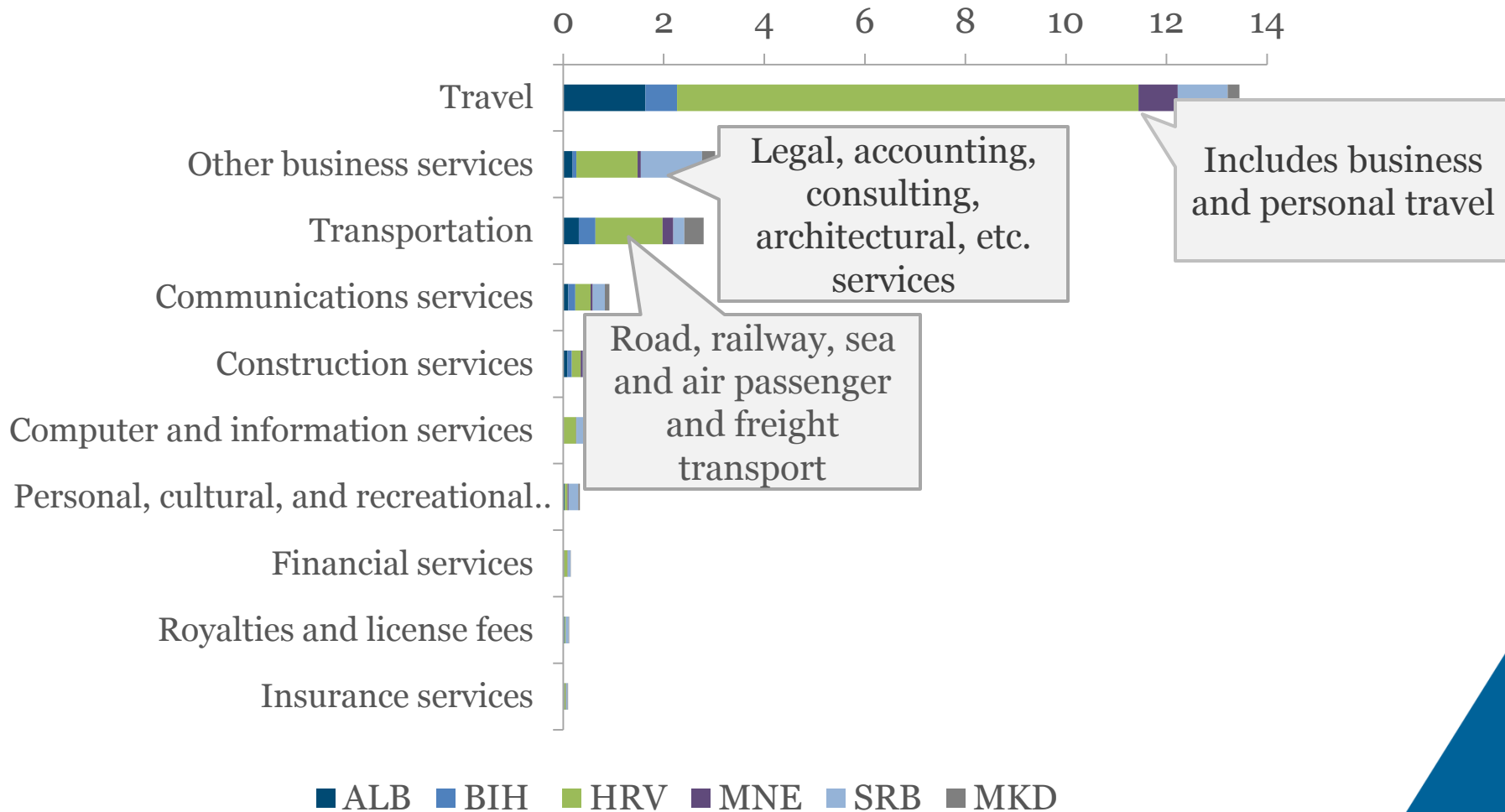






# The case of Western Balkans (5): Travel accounts for the largest share of service exports

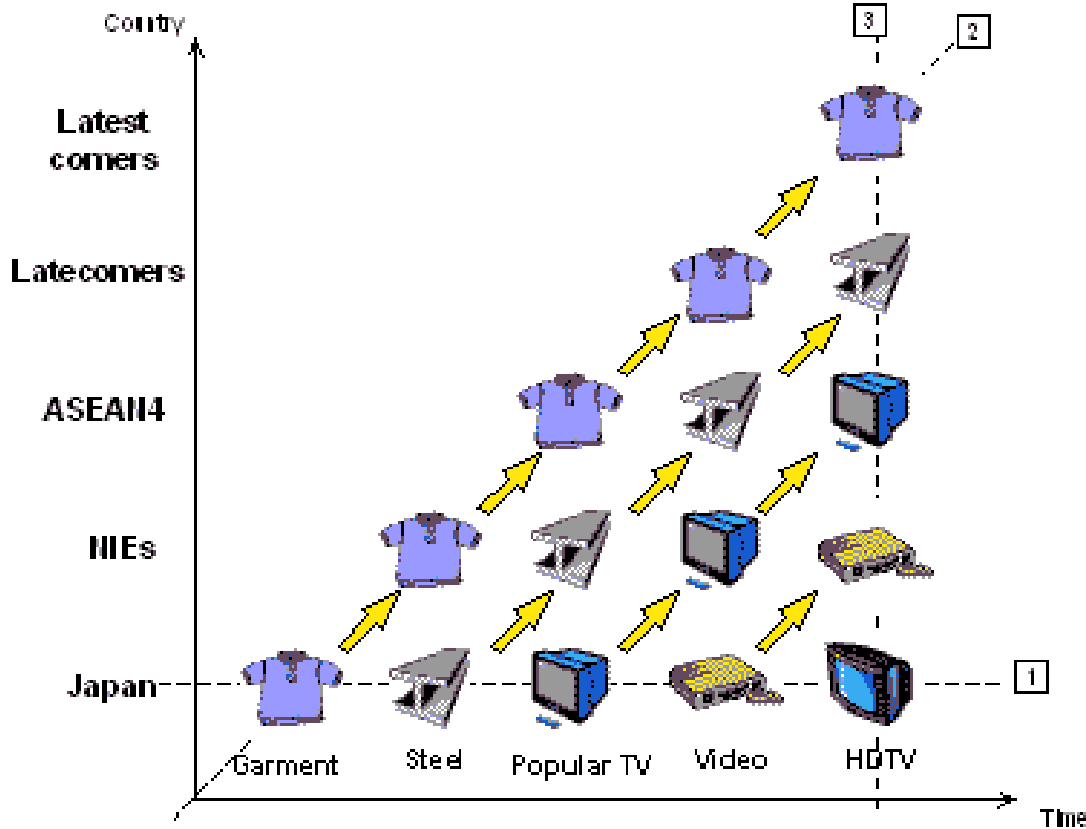
Service exports in 2011 (bn USD)





# The 'flying geese' paradigm (1): a model of dynamic comparative advantages

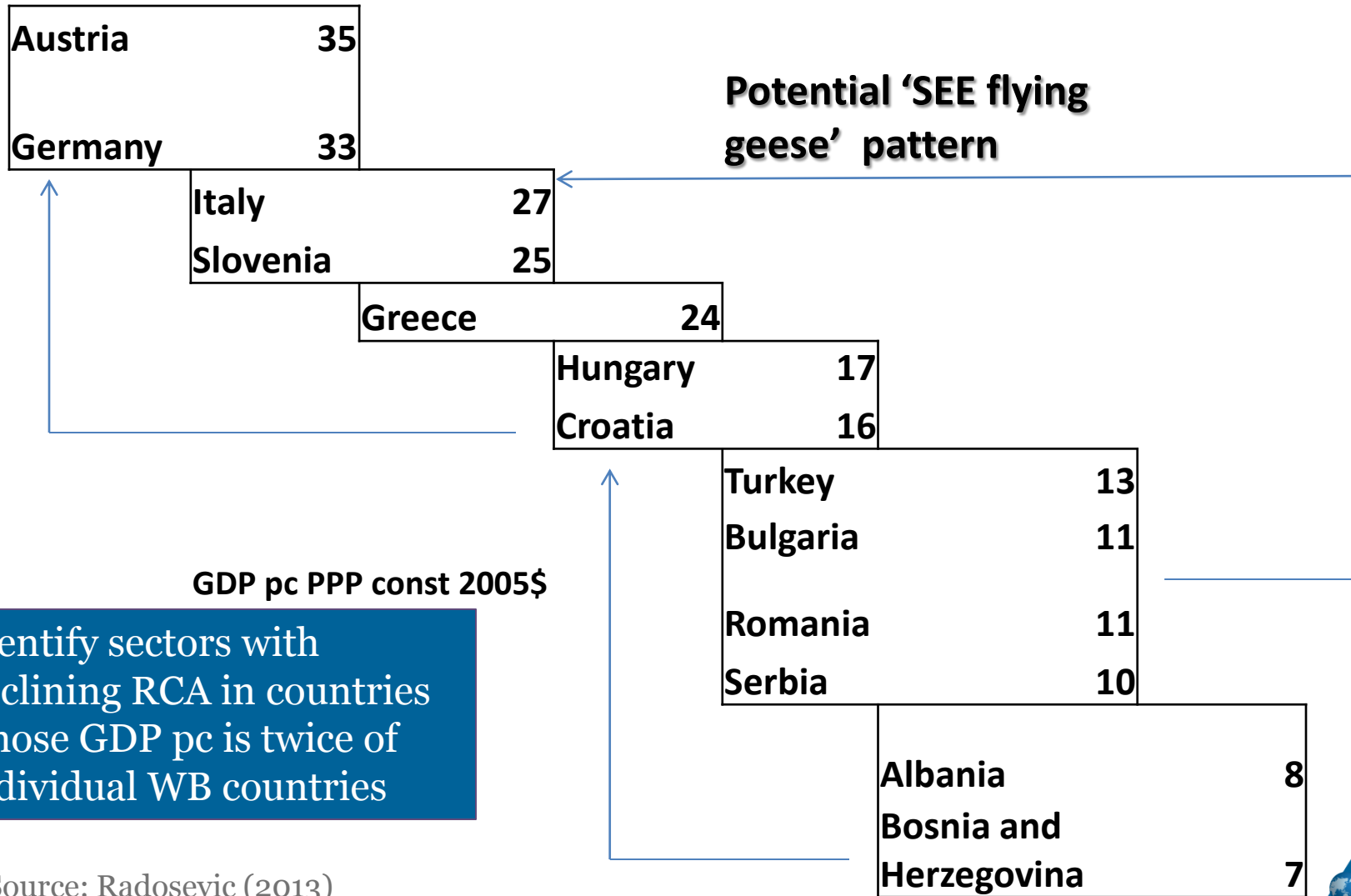
## Structural Transformation in East Asia



- Look at the development path of new EU member states
- Identify the sectors in which their competitiveness is decreasing



# The 'flying geese' paradigm (2): a model for the Western Balkans?



Source: Radosevic (2013)

**Thank you for your attention.**

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