Gulf Research Centre Cambridge

Knowledge for All

Workshop 5

Industrial Policies in the Gulf

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Abstract

As they consider the inevitable transition of a post-oil world, the coming waves of disruptive technologies, and the prospect of losing out in an increasingly competitive environment, the Gulf countries have adopted blueprints for economic transformation more ambitious than anything attempted in the past. The "vision" statements of the GCC countries, in particular, envisage the development of industries that would propel them closer to the frontier of technological innovation. It is not evident, however, that these amount to coherent and viable industrial strategies. The plans have not adequately addressed the market failures that any meaningful industrial policy needs to overcome. Nor have they established the robust institutional mechanisms and procedures necessary for realization of their industrial aspirations.

Arriving at a better understanding of the industrial policies of the Gulf countries is the primary objective of this workshop. While studies of industry in these countries abound, many aspects of their industrial *policies/strategies* have received little scholarly

attention. There are few in-depth studies of even such basic questions as the process in which those policies were formulated and adopted. The workshop will undertake an intensive examination of central issues in industrial policy – the rationales behind the choices that have been made, their prerequisites, their limitations, their potentials, and the prospects for alternative pathways for industry in the region.

Description and Rationale

Contrary to what is often supposed, even in the academic literature, the Gulf countries have made major strides in industrialization. That most of the industries they have established are based on or are tied to oil and gas does not negate the achievement. There has also been progress in diversification even if the mainstay of diversification has been in hydrocarbon industries, the product of substantial upstream and downstream investments. The industries, all capital-intensive and energy-intensive and many supported by favorably priced feedstock, include a variety of petrochemicals as well as steel, aluminum, building materials, and electrical machinery. In the process, world-class stalwarts such as SABIC (the Saudi Basic Industries Corporation) and ALBA (Aluminum Bahrain) have emerged. Some countries, notably Saudi Arabia and the United Arab Emirates, are also moving aggressively into renewable energy, especially solar. Yet other areas such as maritime logistics are expanding capacity and operations and providing a spur to manufacturing. All in all, the industrial base of these countries has widened and their industrial capabilities have grown.

Such progress notwithstanding, the Gulf countries are today more conscious than ever before of their limitations in the world of industry. With the possible exception of the UAE, none of the Gulf countries can make credible claims to having made substantial headway in diversifying merchandise exports: the export of non-hydrocarbon manufactured products is lacking in both depth and scale. And although there has been a growing private sector role in industry, even petrochemicals, state-owned enterprises still rule the roost. The professed intention of making private industry the engine of growth and development – a common thread in all the “vision” manifestoes that have proliferated in the Gulf – is nowhere close to realization. Few private entities, most of which are small and medium enterprises, are beneficiaries of financial or technical assistance from government, and few are generators of employment or incubators of skills. The region's industrial policies are statist through and through: the suggestion that industrial policy be used as a process of discovery -- a "dialogue" with the private sector devoted to eliciting information in order to identify and remove binding constraints to development – finds little, if any, correspondence in reality. Moreover, in general, productivity has not seen appreciable increases and entrepreneurship remains weak, while efforts to stimulate innovation through initiatives such as industrial clusters have not yielded much success. The GCC countries are low in the ranks of UNIDO's Competitive Industrial Performance Index. Whatever its successes, the industrial strategy of every country in the Gulf country continues to be tethered to the rentierism of its national economy.

Hence, it is hardly surprising that there is something close to a universal consensus among policy-makers throughout the region that their industrial strategies are unsustainable. Today, these countries find themselves in a liminal juncture in the world economy – a world with economies still dependent on fossil fuel and at the same, slowly but surely, transitioning to alternative sources of energy. The rethinking of industrial policy has intensified with the diminished wherewithal, thanks to the fall in world prices of crude and the resultant revenue declines, to maintain the government largesse that has been an essential ingredient of the "social contract" that has prevailed for decades. The advantages once conferred by low-cost energy and low-cost labor have waned. The felt need for a new set of policies is also galvanized by the lures of "the new industrial revolution" – NIE or I4.0 – which promises to usher in a wave of new technologies and to upend many existing ones. Hence, the Gulf countries are eyeing developments in such areas as artificial intelligence (AI), advanced robotics, the Internet of Things (IoT), cloud computing, big data, digital fabrication, additive manufacturing, augmented reality, 3D printing, and nanotechnology. These technologies and the global value chains that help to produce and distribute them have far-reaching implications in realms ranging from energy and investment to national competitiveness and social stability.

Concomitantly, the world has seen a sea-change in thinking about industrial policy. Once banished by the Washington Consensus and its singular preoccupation with liberalization, deregulation, stabilization, and privatization, industrial policy has undergone a resurgence since the turn of the century. It has shed its erstwhile emphasis on "picking winners" as well as import substitution and economic protection. Instead, it gives pride of place to innovation in production, development of entrepreneurship, human capital development, foreign direct investment (FDI), and multinational enterprise involvement. The scope has widened to include a broad range of measures designed to support entrepreneurship and competitiveness. Industrial policy is no longer regarded as a fool's errand. Even development banks and development funds, once castigated as purveyors of patronage, cronyism, and rent-seeking, are back in fashion.

The Whys and Hows of Industrial Policy

Hardly any country has succeeded in making the transition to a developed economy without some industrial policy. Great Britain did not industrialize in the eighteenth century by following an Adam Smithian rule-book. Indeed, the industrial revolution has been called "the mother of all industrial policies." According to the United Nations Conference on Trade and Development, no less than 101 countries, together accounting for 90 percent of world GDP, have formal industrial policies, even if they are not designated as such.

As Dani Rodrik notes, the debate on industrial policy is no longer about "Why?", but about "How?" Industrial policy is generally understood to involve government interventions in sectors or industries aimed at shifting the structure of production to areas of higher productivity. Its essence is structural transformation. It is not confined to manufacturing: its ambit includes tourism and services. The premise behind industrial policy is that having strong institutions and getting the economic fundamentals right (captured by the World Bank's "ease of doing business" scorecard) is not adequate. Nor is macroeconomic stability, a primary concern of the International Monetary Fund. Markets alone will not lift developing countries to the ranks of front-runners in the world economy. Rather, the burden of industrial policy, its leading proponents maintain, is to deal with market failures and coordination problems. If knowledge and learning are the essential ingredients separating rich and poor countries, markets may underperform in the production and transmission of these ingredients. And, without a coordinator, investors might not commit to large-scale industrial projects as the projects would not be commercially viable unless ancillary projects, infrastructure, and services were undertaken. Hence, it is argued, the state needs to intervene to deal with market weaknesses and coordination externalities.

However, while the consensus on industrial policy has broadened, there are disagreements on several aspects even among its champions. These disagreements are directly relevant to any inquiry about industrial policy in the Gulf and beyond. What is the proper scope of industrial policy? Should the policy tools be "vertical", focusing on specific firms or industries? Should they be "horizontal", applied indiscriminately, targeting technological development and capacity building across sectors and thereby enhancing the overall business environment? Or should they combine horizontal and vertical elements? How should industrial policy deal with a country's comparative advantage? Should it conform to comparative advantage? Should it defy comparative advantage? Or should it strike a balance between the two? Then there are a host of imponderables or unknowns. Ascribing outcomes to specific industrial policy measures is anything but straightforward. Counterfactuals are hard to come by and selection bias is all but unavoidable. Hence the risk of falling into the *post hoc ergo propter hoc* trap. Even among the putative paragons of the East Asian "miracle", there are contending interpretations of the role industrial policy played – if it had a role at all.

Essential Questions

As the foregoing discussion suggest, any inquiry into industrial policy is bound to encounter a welter of empirical, analytical, theoretical, and prescriptive questions. Even identifying a country's industrial policy can be challenging. For example, what the Saudi government calls its industrial strategy, with its National Industrial Development and Logistics Program and plans for a raft of clusters ranging from automotive and pharmaceuticals/biotechnology to renewables and machinery/equipment, each with a myriad of sub-clusters, is arguably more of a wish-list rather than operational policy.

What we seek to investigate in this workshop are three sets of questions about industrial policy in the Gulf. They are grouped below in the following categories: policy sources and processes; policy choices and instruments; and policy outcomes. It goes without saying these questions do not cover issues of concern to industrial policy exhaustively.

Policy sources and processes

*What explains the industrial strategy in place today?

*What is the process by which industrial strategy was formulated and adopted?

*Who were the architects of the strategy? What entities are involved in its execution?

*What assumptions and projections have policy-makers made about their nation's industrial future?

*What is the institutional framework in which policy is implemented?

*What have been the critical junctures in the evolution of industrial policy?

*Is there a consensus among and between public and private actors on ends and means?

*What mechanisms of interaction and consultation between public and private entities exist?

*What is the regulatory and supervisory organizations for industrial policy?

*Are there dedicated dispute settlement rules and procedures?

Policy choices and instruments

*What are the economic and technical underpinnings of the strategy?

*How coherent and credible is the policy package?

*What are the provisions for productivity, diversification, entrepreneurship, employment, technological development, and export facilitation?

*How much emphasis is there on FDI?

*What incentives are offered to private investors?

*What conditionalities and performance criteria are attached to loans and other forms of government support?

*What benchmarks are used to evaluate whether industrial policy is meeting development objectives?

*Are there measures to curb or prevent rent-seeking, patronage, and state capture?

*Does the East Asian record of industrialization, what has been called the "flying geese" model, hold any lessons for Gulf countries?

Policy outcomes

*What accounts for the limitations of the industrial strategies of countries of the Gulf?

*What have been the effects of industrial policy on areas such as innovation, technological sophistication, diversification, and exports? Is it achieving professed goals?

*How has industrial policy affected investment behavior? What has been its impact on the private sector?

*What evidence is there that companies or organizations that have been the beneficiaries of government support have had superior performance, compared to those who did not, as measured by such indicators as productivity, profitability, and exports?

*What have been the determinants of successes and failures in industrial policy implementation?

*How has industrial policy coped with coordination problems, informational asymmetries, and transaction costs?

*Which industries, if any, have the potential of generating spillovers through the diffusion of knowledge and learning by doing?

*Is the resurgence of state capitalism in Gulf countries inimical to or supportive of the achievement of industrial strategy goals?

*Have the industrial strategies of individual countries in the region inhibited the creation of a regional division of labor that reduces duplication and encourages complementarities in industry?

Anticipated Participants

The workshop is designed to attract a group of scholars who will engage in a rigorous, theoretically informed, exploration of seminal concerns in the under-studied subject of the industrial policies of the Gulf. Our ultimate objective is to make a substantial contribution to the literature on the political economy of the Gulf through a landmark edited volume based on the workshop papers.

We welcome both qualitative and quantitative papers, but it is essential that sweeping generalization or pure description are avoided. Papers may analyze industrial strategy in a historical and comparative framework or explore the implications for public policy and/or further research. As industrial policy straddles multiple domains, our inquiry cannot be reduced to a single discipline: the perspectives of not only economics and political science but also of anthropology and business may have direct relevance. Although much of the foregoing description has focused on the GCC, we welcome papers on the two other Gulf countries, Iran and Iraq, as well. We are also interested in comparisons with not only the non-Gulf Middle East but also with other regions, especially East Asia, which has been central to discussions of industrial policy in recent decades.

Workshop Directors' Profile

Dr. Don Babai is a lecturer in international political economy at Harvard University and a research associate at its Center for Middle Eastern Studies. His publications include works on international economic institutions, including the International Monetary Fund, the World Bank, and the World Trade Organization. He has also published articles on topics such business ethics in the Middle East and the evolution of thinking about development as reflected in "Washington Consensus." He is currently working on two projects: a book under contract with Edward Elgar, titled *Business and the State in Saudi Arabia: Beyond Patriarchy?*, and a *festschrift*, consisting of twelve essays on business history, in honor of Roger Owen, dean of economic historians of the Middle East. He has also served as editor of *Harvard Middle Eastern and Islamic Review*, Harvard's principal journal dealing with the Middle East and the world of Islam. He has done consulting work for several organizations, including the World Bank and the Japan Economic Research Institute. Besides Harvard, he has taught at Boston University, the University of Maryland, College Park, the University of California, Davis, and the University of California, Berkeley. He has a doctorate in international relations from the University of California, Berkeley.

Dr. John Sfakianakis is a Senior Scholar at Pembroke College, University of Cambridge, Chief Economist and Head of Research of the GRC, and Associate Fellow of Chatham House in London. He is a board member of the Cambridge Middle East and North Africa Forum at the University of Cambridge. He has more than twenty years of experience in senior positions in government, banking, and private family offices. He has advised public and private clients on investment strategy, macroeconomic outlook, and asset allocation strategies. He was formerly Middle East Director for Ashmore, a FTSE 100 asset manager, where he served as a member of the Investment Committee and a board member of the firm's funds in Saudi Arabia, which are regulated by the Capital Market Authority. His other previous positions have included Chief Investment Strategist of MASIC, one of the oldest family offices in Saudi Arabia; Chief Economist of Credit Agricole C.I.B. for the Middle East; Chief Economist and Group General Manager of Banque Saudi Fransi; Group Chief Economist of Saudi British Bank; and Chief Regional Economist of Samba Financial Group. Among the public and private institutions he has advised in Europe, the US and the Gulf are BCG, McKinsey, PwC, EY, Berkley Research Group, Burohappold, and Deloitte Monitor. For the last sixteen years, he has lived in Riyadh, Saudi Arabia.

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