



# The Post-Covid Consensus

SHAHID YUSUF

## Abstract

Development economics is turning a full circle with a difference. This paper addresses the circling back to the policies in vogue during the 1980s and earlier, including industrial policies, coupled with protectionism; accounts for the regression to earlier certitudes after an extended spell of globalization underpinned by market fundamentalism; and indicates how a transforming global environment has enlarged the policy agenda. There is a new policy consensus in the making, which borrows some elements of the Washington Consensus but goes beyond to encompass a broader policy agenda.

## The Post-Covid Consensus

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## Return of an unwelcome past

During the 2020s, the world confronts risks that “feel both wholly new and eerily familiar.” A few “older risks [have reappeared]—inflation, cost-of-living crises, trade wars, capital outflows from emerging markets, widespread social unrest, geopolitical confrontation [that has magnified the risk of conflict], and [raised] the specter of nuclear warfare... These are being amplified by comparatively new developments in the global risks landscape, including unsustainable levels of debt [for developed and developing countries alike],<sup>1</sup> a new era of low growth, low global investment and de-globalization, a decline in [the] human development [index in 2020/2021] after decades of progress, rapid and unconstrained development of dual-use (civilian and military) technologies, and the growing pressure of climate change [with global mean temperatures approaching levels that could trigger several tipping points]<sup>2</sup>... Together, these are converging to shape a unique, uncertain and turbulent decade to come.” (WEF 2023).<sup>3</sup>

## First came the golden years, then stagflation

From the current vantage point, the third quarter of the twentieth century was an economic golden age (Marglin and Schor 1990). Both the industrialized economies and newly independent developing countries achieved relatively high rates of growth. Among the former were several that were rebuilding industrial systems severely damaged during the Second World War and in the process incorporating productivity enhancing, state of the art technologies. The latter included countries many newly independent, that initiated the long-delayed process of state-led industrialization behind high tariff barriers. Although tariff negotiations launched by the GATT (1947), had begun stimulation international trade, this was the heyday of inward looking, state-led, import substituting industrialization (ISI; Baer 1972).

By the mid 1970s, following the first oil crisis (1973), this great economic spurt was beginning to falter. European economies and Japan had largely regained their industrial footing, were drawing abreast in technological terms with the United States and their growth rates were ebbing. Developing countries were discovering the limits of comparative advantage denying ISI, and the costs of

- 1 The levels to which debt burdens have risen point to heightened risk from crises and defaults extending far into the future. In the past some countries were able to reduce indebtedness by running budget surpluses but that was in the nineteenth century. For countries to grow out of acute indebtedness in the current circumstances is less feasible unless digital technologies/AI deliver a large increase in productivity and facilitate trade, and/or interest rates on debt can be repressed as was done in the 1950s with savers bearing the costs. Persistent inflation is not a solution. Trimming some expenditures will become a necessity even as ageing populations and climate change compel governments to increase spending in other areas. Some hiking of taxes, where it is politically feasible may be unavoidable, but the burden of adjustment might have to be carried by expenditures. Mitchener and Trebesch (2021); Ferencz et al. (2022); Arslanalp and Eichengreen (2023); Alesina, Favero and Giavazzi (2019).
- 2 July 2023 was 1.54C warmer than the pre-industrial average during 1850–1900, and the warming trend is inexorable because of the CO<sub>2</sub> already released and annual additions to come. Average global temperatures could exceed 1.5C within a few years. Tollefson (2023); McKay et al. (2022).
- 3 WEF (2023) *Global Risks Report*. This is echoed by the UNDP *Human Development Report 2021/2022*. (p.3). “Acute crises are giving way to chronic, layered, interacting uncertainties at a global scale, painting a picture of uncertain times and unsettled lives.”

resource misallocation were beginning to take their toll with diminishing returns setting in and growth trending downwards.<sup>4</sup>

The economic doldrums starting in the 1970s and extending into the early 1990s, initiated a rethinking of development strategies and of key industrial and macroeconomic policies (Figure 1). This gathered impetus as stagflation worsened with global inflation rates averaging 11.3 per annum, and starting in the early 1980s,<sup>5</sup> debt accumulation began stoking crises (World Bank 2022).<sup>6</sup> Mexico succumbed in 1982. Soon thereafter, debt crises engulfed fifteen others in the Latin American region and spread beyond to indebted developing countries in Africa.<sup>7</sup> Bailouts, restructured bank loans, debt rescheduling, and write-offs tested the global financial markets through the latter part of the 1980s and into the 1990s. Latin America lost a decade or more and many countries in SSA were not spared either.

**FIGURE 1. Decadal average per capita growth rates (%) by region**

Geographical Region	1960s	1970s	1980s	1990s	2000s
East Asia and Pacific	3.9	3.3	3.2	3.0	3.6
Europe and Central Asia	4.7	3.5	1.8	0.5	3.6
Latin America and Caribbean	2.2	2.7	-0.6	1.5	2.2
Middle East and North Africa	3.7	2.7	-0.9	2.0	2.0
North America	3.1	2.5	1.9	1.8	0.9
South Asia	1.6	1.4	2.1	0.5	4.5
Sub-Saharan Africa	1.8	1.3	-0.2	-0.4	1.8
World	2.8	2.4	0.6	0.9	2.7

Source: Johnson and Papageorgiou (2020).

## Which paved the way for neoliberalism, and a market/statist hybrid export led growth model

From the 1980s and accelerating thereafter, the statist approach and industrial policy fell into disrepute and development guided by market forces with minimal intervention by the guiding

4 Resource misallocation led to a widening gap in productivity between advanced and developing countries and a divergence in per capita GDP between developing and developed countries. Banerji and Moll (2009); Pritchett (1997); Misch and Saborowski (2020); Boonzaaier et al. (2017).

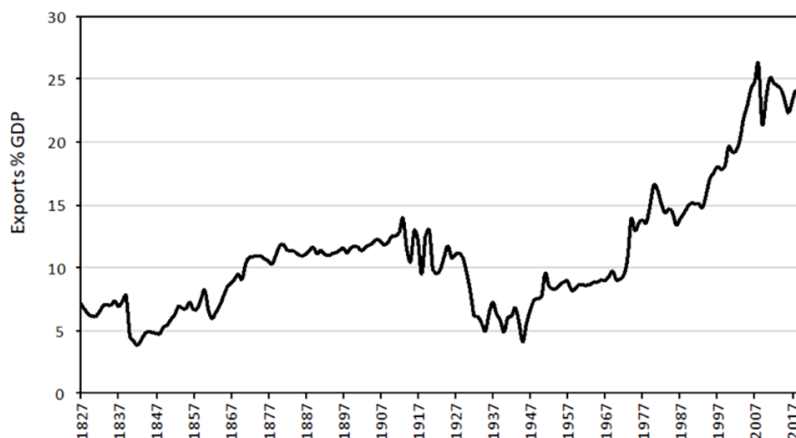
5 The second oil shock, which struck in 1979–1980, exacerbated stagflationary pressures.

6 Stagflation is again a risk but by no means a given. Ha et al. (2022); World Bank (2022) "The origins of the 1980s Debt Crisis can be traced back to the acute shocks to the international monetary system in the 1970s: the collapse of the Bretton Wood system; the major oil prices hikes; and the substantial liberalization of international finance. The associated build-up of imbalances and vulnerabilities during this period ended abruptly in the early 1980s, and the IMF had to deal with its first systemic debt crisis." <https://www.elibrary.imf.org/display/book/9781484371329/ch001.xml>

7 <https://www.federalreservehistory.org/essays/latin-american-debt-crisis>; [https://www.fdic.gov/bank/historical/history/191\\_210.pdf](https://www.fdic.gov/bank/historical/history/191_210.pdf)

hand of the state, acquired currency. This neoliberal turn<sup>8</sup> accelerated deregulation as well as the dismantling of barriers to trade and capital flows, which were ongoing but acquired momentum and helped to fully launch the Third (or Second) Globalization (Boughton 2002; Goldberg and Larson 2022; Baldwin 2018; Figure 2 shows how exports as a percent of GDP rose after the 1980s).

**FIGURE 2. Trade globalization(s): Exports as percent of GDP**



Source: Goldberg and Larson (2022). [https://cpb-us-w2.wpmucdn.com/campuspress.yale.edu/dist/6/3741/files/2022/08/Goldberg\\_Ohlin-manuscript.pdf](https://cpb-us-w2.wpmucdn.com/campuspress.yale.edu/dist/6/3741/files/2022/08/Goldberg_Ohlin-manuscript.pdf).

A handful of East Asian countries were among the earliest to capitalize on the crumbling of impediments to trade, and on an increase in the flow of capital from advanced countries. By harnessing FDI, building manufacturing capabilities and taking advantage of opportunities to expand trade, these countries rapidly pulled ahead of the pack and crafted the export-led growth model (see Figure 3, shows the tight correlation between GDP growth and manufacturing value added).<sup>9</sup> Ever since, it has served as a template for virtually all late starters seeking to jump start growth.

This new breed of East and Southeast Asian developmental states succeeded by adhering selectively to the prevailing neoliberal orthodoxy (Haggard 2018; Woo-Cummings 1999). Having observed Japan’s effective manipulation of industrial, trade and exchange rate policies, developing Asian

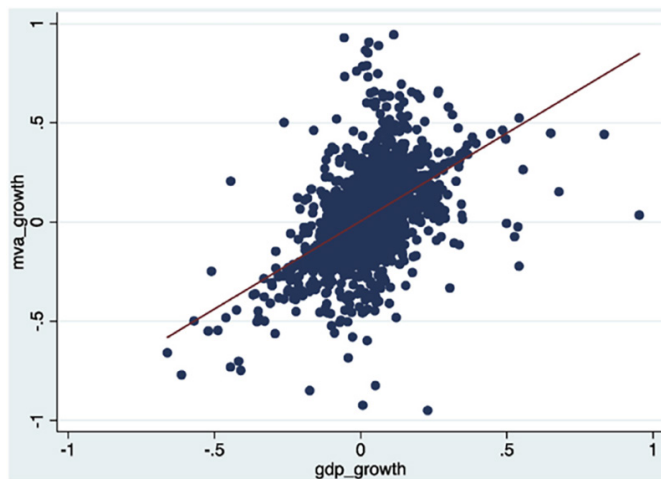
8 Neoliberalism is associated with the work of F.A. Hayek, M. Friedman, K. Popper, and J. Buchanan among others. “Neoliberalism holds that a society’s political and economic institutions should be robustly liberal and capitalist, supplemented by a constitutionally limited democracy and a modest welfare state [providing social insurance and public goods]. Neoliberals endorse liberal rights and the free-market economy to protect freedom and promote economic prosperity [but] they are skeptical of the regulatory state, extensive government spending, and government-led countercyclical policy.” <https://plato.stanford.edu/entries/neoliberalism/>; or more succinctly Gerstle (2022) “Neoliberalism, seeks to release capitalism from its fetters—and to use state power only insofar as it strengthens free markets and protects them from those who want to make them ‘less free.’” Menand (2023).

9 The Four East Asian Tigers acquired legendary status and they continue to inspire others across the developing world even though their halcyon years have receded into the distance.

economies guided investment—much of it private<sup>10</sup>—into outward oriented manufacturing industries and supporting infrastructure. This was combined with a host of fiscal and financial incentives that encouraged firms to export. Policies and cultural proclivities also contributed to the deepening of human capital, which enabled the early movers to transition from less to more technologically complex and higher value adding activities. Market forces complemented state signaling and disciplined resource allocation. To survive and grow, Asian firms venturing overseas were compelled to rapidly ascend the learning curve and to compete on equal terms if not better with the incumbents.

Codification of the export-led model was initiated by *The East Asian Miracle*, a publication of the World Bank issued in 1993 that highlighted the market conforming features of the model and soft pedaled the dirigisme (Rodrik 1994). This unleashed a torrent of books and articles that have examined every facet of the East Asian experience and explored its replicability.<sup>11</sup> Thirty years later, export performance remains the touchstone of economic success for developing economies large and small. The export of services many of which were an outgrowth of industrialization, now supplements that of commodities, but no country has discovered an alternative pathway to rapid and sustained growth other than through trade. Furthermore, the creation of a competitive manufacturing sector is intrinsic to every success story (Haraguchi et al. 2018).

**FIGURE 3. Growth of MVA and GDP 1950–2005 for 88 countries**



Source: Haraguchi et al. (2018). [http://www.unido.or.jp/files/UNIDO\\_What-factors-drive-successful-industrialization-Evidence-and-implications-for-developing-countries.pdf](http://www.unido.or.jp/files/UNIDO_What-factors-drive-successful-industrialization-Evidence-and-implications-for-developing-countries.pdf).

10 Even China owes much of its three decade long double-digit rate of growth to the entrepreneurial energy of private or quasi private businesses.

11 Among the most noteworthy are Perkins (2013); Hanushek and Woessmann (2016); Campos and Root (1996); Root (1996); Page (1994); Stiglitz (1996); Rodrik (1994).



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## The troubled 1980s and the neoliberal turn led to a Washington Consensus

The embrace of neoliberal market fundamentalism in the 1980s also gave birth to the Washington Consensus (WC). With the troubles of the preceding decade serving as a backdrop, the WC tabled by John Williamson (1990; 2000; 2004), proposed ten policies, which much like Luther's 95 theses,<sup>12</sup> attracted immense attention and sparked debate that sputters on to this day (Serra and Stiglitz 2009; Chang 2004). The WC called for a reduction of budget deficits—partially responsible for the crises that had wracked Latin America—together with the needed reform of tax systems and privatization of inefficiently run and frequently loss-making public enterprises. With an eye to the experience of East Asian economies, the WC recommended reducing trade restrictions, taking steps to promote FDI, and it extolled the merits of a single competitive exchange rate. To ensure that these measures elicited the desired supply response, the WC backed a set of policies that would improve allocative efficiency by strengthening market institutions (e.g., protection of property rights, contract enforcement, dispute settlement), render markets more competitive with the help of deregulation, and enable the financial sector to increase resource mobilization and channel investment into industries and sectors promising the highest returns. All very sensible sounding prescriptions given the circumstances. Their application helped quell the global economic turbulence and restore growth. Chile emerged as one of the standard bearers of neoliberal policies. Rigorous implementation of these policies by the 'Chicago Boys', resulted in rapid growth (1984–1997) and a steep reduction in poverty (Edwards 2023).<sup>13</sup>

## Dynamism imparted by market fundamentalism received a (temporary) boost from a new GPT<sup>14</sup>

The spread of computerization from the 1980s and the onset of digitalization from the 1990s, gave rise to a belief that technology could serve as a driver of productivity and innovation and reinforce or augment other market directed sources of growth. The use of computers, of mobile telephony, and access to the Internet have all increased dramatically since the turn of the century and there is no doubting the scale of the technological change.<sup>15</sup> Even the least developed countries have benefitted. But after an all too brief spurt from the mid 1990s through the mid 2000s, which was largely the

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12 The Ten Theses of the WC were presented at a conference and not posted on the door of the Washington National Cathedral.

13 The Chilean Miracle found its stride more than ten years after the takeover by Pinochet. Per capita GDP in 1983 was about the same as in 1973. Edwards (2023) notes that alongside the successes there was neglect—of increasing inequality, which sowed the seeds of troubles to come. (p.270). As its economic and social problems have mounted, Chile has ceased to be the emblematic Latin American success story. OECD (2022); Ffrench-Davis (2010); Financial Times (2023). <https://www.ft.com/content/757c6d01-7dfd-41c0-8804-feb2415c3fe4>.

14 GPT—a general purpose technology with manifold applications and the capacity to breed innovations in many different areas. Bresnahan and Trajtenberg (1992).

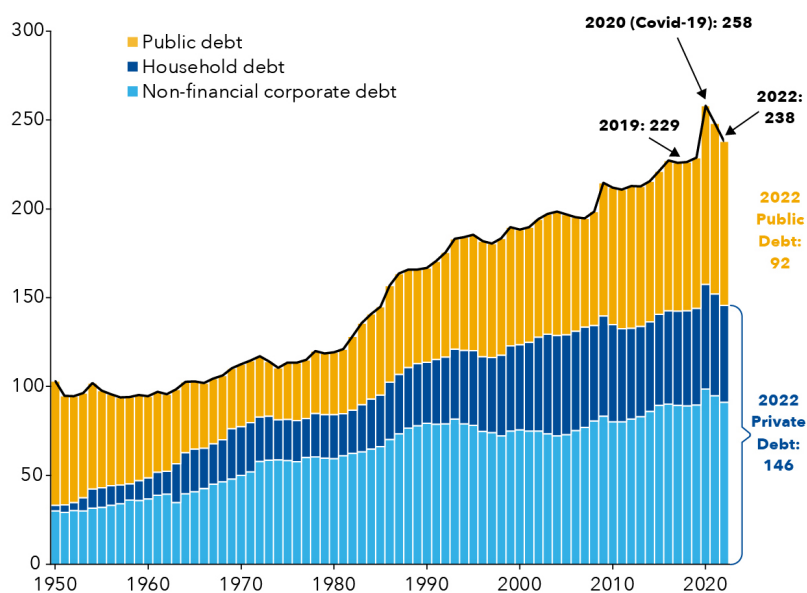
15 According to some calculations, digital goods may have generated trillions of dollars' worth of consumer's surplus. Brynjolfsson et al. (2023). Possibly cold comfort for those in developing countries who need to put food on the table and pay for transport and accommodation.

result of globalization, GDP growth once again slowed (Crafts 2004). Technological change did not impart the sustained acceleration of growth that many anticipated. Computers, mobile devices, innovative products, and services flourished but total factor productivity gains were surprisingly elusive (Solow 1987).<sup>16</sup>

## Post Covid countries struggling with stagflation, debts, climate change and other pressures look to the past and to technology for solutions

Fast forward to 2023. The global economy is recovering from the Covid induced economic and humanitarian crises.<sup>17</sup> Many countries are having to cope with ballooning deficits, the loss of fiscal headroom, and a few have either succumbed to debt crises or are struggling to avoid the risk of default. Global debt is on a rising trend. It increased by \$200 billion between 2021 and in 2022 reaching \$235 trillion or 238 percent of global GDP (Figure 4). Inflation is again a worry after the Great Moderation,<sup>18</sup> which spanned almost three decades.

**FIGURE 4. Global debt on a rising trend**



Source: IMF (2023). <https://www.imf.org/en/Blogs/Articles/2023/09/13/global-debt-is-returning-to-its-rising-trend>.

<sup>16</sup> "You can see computers everywhere but in the productivity statistics". Solow (1987).

<sup>17</sup> The memory of the Financial Crisis of 2009 lingers. It was the event that brought the almost three-decade long boom in trade and growth to a close. It also initiated the geo-political fracturing that has steadily worsened since and has hastened the partial unwinding of globalization. Brookings (2023). [https://www.brookings.edu/wp-content/uploads/2023/07/global\\_20230731\\_state\\_of\\_the\\_global\\_economy\\_uncorrected\\_transcript.pdf](https://www.brookings.edu/wp-content/uploads/2023/07/global_20230731_state_of_the_global_economy_uncorrected_transcript.pdf).

<sup>18</sup> <https://www.federalreservehistory.org/essays/great-moderation>; A long period of stable prosperity lulls policymakers and can set the stage for a Minsky Moment—"stability is destabilizing". Kohn (2018). <https://www.rethinkeconomics.org/journal/minskys-moments/>.

The growth potential of the major economic engines of the global economy—China,<sup>19</sup> the US, and the EU—looks to be significantly diminished. Moreover, the longer-term prospects of all countries are clouded by geopolitical tensions affecting trade and FDI, the ongoing effort to restructure supply chains and enhance their resilience,<sup>20</sup> the cost of adaptation and mitigation necessitated by climate change, loss of biodiversity and erosion of nature's capital,<sup>21</sup> and demographic trends (Alfaro and Chor 2023; Fajgelbaum et al. 2023).<sup>22</sup> Sluggish growth and inflation have again aroused fears of stagflation. Income and wealth inequalities are deep and worrisomely persistent. Trade barriers have begun inching upwards (Figure 5).<sup>23</sup> And the worldwide drought in factor productivity is well into its second decade with no immediate end in sight (Dieppe 2020; Kose and Ohnsorge 2023; Figure 6). As productivity gains are the principal source of long-term per capita GDP growth, the World Bank fears

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19 Deflation, the high indebtedness of local governments and real estate developers (Evergrande; Country Garden), and the diminishing reflationary potential of infrastructure spending are all weighing on China's near term growth prospects. Washington Post (November 3rd 2022) [https://www.washingtonpost.com/business/how-chinas-property-developers-got-into-such-a-mess/2022/11/03/2842fbca-5b61-11ed-bc40-b5a130f95ee7\\_story.html](https://www.washingtonpost.com/business/how-chinas-property-developers-got-into-such-a-mess/2022/11/03/2842fbca-5b61-11ed-bc40-b5a130f95ee7_story.html). A declining and ageing population is a headwind that will blow more strongly over the longer turn. In 2022, China's fertility rate had fallen to 1.09 and according to one estimate its population might be closer to 1.28 billion not 1.43 billion. Achieving carbon neutrality will weigh on growth prospects as will low levels of domestic household consumption. Perkins (2023); Peschel and Liu (2022) also project a decline in the potential growth rate as the working age population shrinks and this is not offset by an increase in the growth sourced from capital or TFP; Technological decoupling, the turning inward and the relative importance afforded to the public sector, could affect private entrepreneurship and dynamism; WSJ (August 21, 2023) <https://www.wsj.com/world/china/china-economy-debt-slowdown-recession-622a3be4>; WSJ (August 28th 2023) <https://www.wsj.com/world/china/communist-party-priorities-complicate-plans-to-revive-chinas-economy-84a156d7>; <https://www.nytimes.com/2023/08/09/business/china-economy-inflation.html>; M. O'Hanlon (2023); M. Pettis (2023); Yi Fuxian (2023).

20 This is bound to be costly. The transfer of production from China to other countries and the reshoring of strategic activities will take time and efficiency will suffer. It seems to be off to a slow start. Freund et al. (2023) state. "But US import diversification of tariffed goods, or of goods with declining import shares from China, did not increase markedly.... A full reshuffling of global supply chains is not only a long-term process, it is also costly and could only be induced by pronounced and prolonged government intervention. Moreover, decoupling in direct trade may only serve to deepen the indirect linkages between US and China through the industrial supply chains of their trade partners."

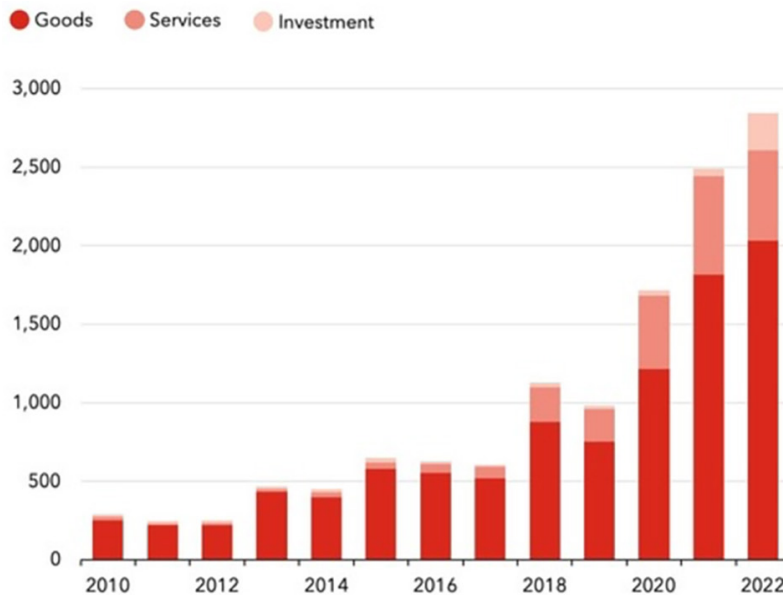
21 Dasgupta (2023) reminds us that the demands on Nature's goods and services far exceeds what is sustainable. To support the current global standard of living, the need is for 1.7 Earths.

22 The World Bank's reading of the tea leaves is unusually bleak. "Global trade in 2010–19 grew only as fast as overall economic growth, down from twice as fast during 1990–2011. Factor reallocation from less to more productive firms and sectors has also slowed. Gains from better education and health have faded as improvements in education and health care systems have leveled off. Continuing a decade of weakness prior to the pandemic, EMDE investment growth in 2022–24 is projected to average 3.5 percent per year, about half its 2000–21 average. After rising over the preceding decades, the growth of the working-age population relative to overall global population growth declined to a three-decade low in 2017. Global policy uncertainty has risen while attitudes towards trade integration have turned more cautious." M.A. Kose and F. Ohnsorge (2023); Kotschy and Bloom (2023) add to the gloom by reinforcing the evidence pointing to a decline in growth because of population ageing, which will be severe in parts of East and Southeast Asia.

23 <https://www.bcg.com/publications/2023/protectionism-pandemic-war-and-future-of-trade>; [https://www.wto.org/english/news\\_e/news22\\_e/tmwto\\_06dec22\\_e.htm](https://www.wto.org/english/news_e/news22_e/tmwto_06dec22_e.htm); WSJ (August 15th, 2023) <https://www.wsj.com/articles/global-economy-economic-losers-fba30b53>

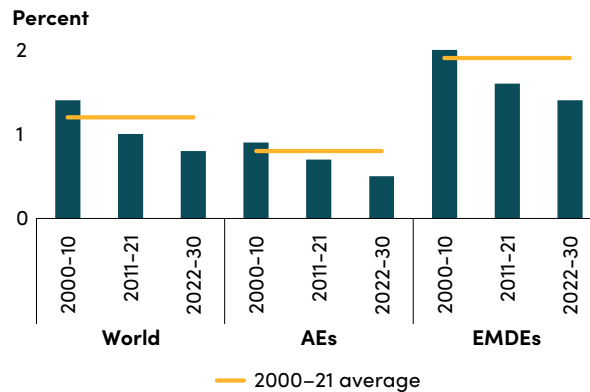
that the maximum speed at which the global economy could expand, is heading down with China serving as a bellwether (Kose and Ohnsorge 2023; Jones 2015; Figure 7).<sup>24</sup>

**FIGURE 5. Number of trade restrictions imposed annually worldwide**



Source: <https://www.imf.org/en/Blogs/Articles/2023/08/28/the-high-cost-of-global-economic-fragmentation>.

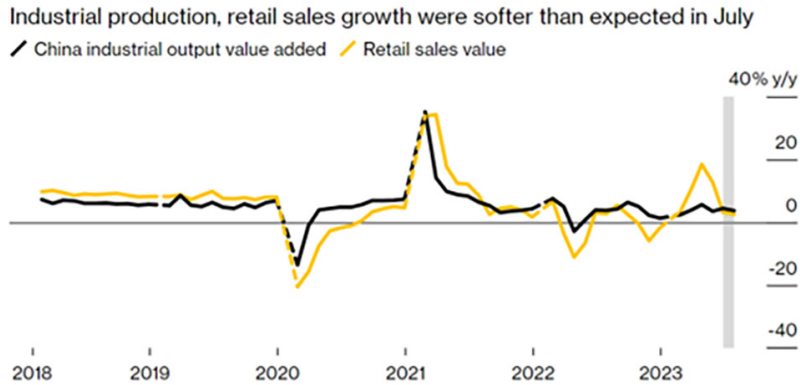
**FIGURE 6. TFP growth**



Source: Kose and Ohnsorge (2023). <https://openknowledge.worldbank.org/server/api/core/bitstreams/fe0880d1-ffbf-430f-bab4-d3dbdda7470e/content>.

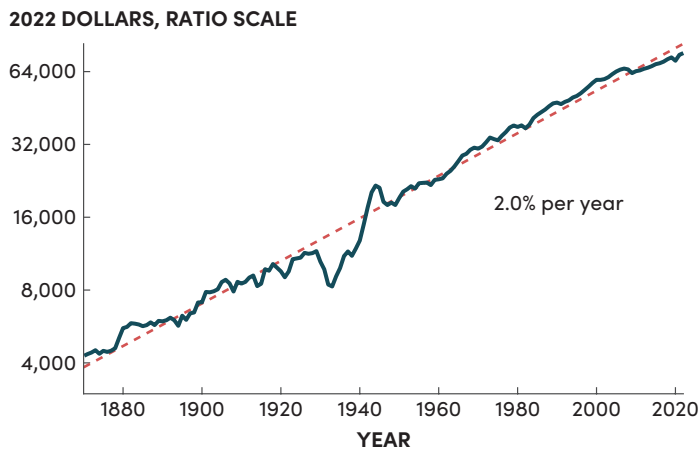
24 The fears expressed by the World Bank and others echo earlier warnings. Predictions by Dixit (2013) ring true. "In the course of the next century there will be several financial and economic crises.... When the crisis hits, policymakers everywhere will be shocked and unprepared. Their panicked responses will merely paper over the real problems and sow the seeds of the next crisis a few years down the line. Another fairly safe prediction pertains to international coordination for policies on global public goods, especially precautionary measures to reduce the risk of catastrophic climate change and mitigate its consequences. Reaching and implementing agreements will remain problematic." He goes on to wonder whether "Dysfunctional politics and continued adverse demographic trends will trap the former economic giants [the EU and the US] into relative mediocrity in the world."

**FIGURE 7. China’s economy drifting down**



Some of the troubles that plagued the global economy during the 1970s and the early 1980s seem to have resurfaced. However, relief could be at hand in the form of a new GPT—Artificial Generative Intelligence (AGI)—which offers promise comparable to that of digital technology in the late 1980s. And the hype cycle is in overdrive with assorted experts promising a resurgence of productivity (TFP) and growth and the appearance of new occupations that will mop up many of those likely to lose their jobs to labor displacing/augmenting technologies (Baily, Brynjolfsson, and Korinek 2023; Brynjolfsson 2022; Autor et al. 2022; White House 2022). Much depends on how rapidly the new technologies diffuse and uses and innovations multiply. It is off to a slow start, which may be inevitable. (Acemoglu et al. 2023). Jones warns against harboring exaggerated expectations. Although automation has been ongoing for 200 years and the US has benefitted from several GPTs, the trend growth of per capita GDP has remained stable at 2 percent per annum for close to 160 years. AGI might do no more than maintain that rate for another decade or two (Jones 2023; Figure 8).

**FIGURE 8. US long run growth 1860–2020**



Source: Jones (2023). <https://www.kansascityfed.org/Jackson%20Hole/documents/9744/Jones-handout.pdf>.

This concatenation of developments—incipient stagflation, debt distress, inequality, the chill of a new Cold War, uncertainty besetting trade and FDI flows, the rising tempo of climate change, widespread environmental degradation, and the apparent dawning of a new technological epoch, are reviving policies that were shelved decades ago—with a difference. Industrial policy (IP) has resurfaced although parting shots from the remaining neoliberals continue to rain down on all those who support measures to rebuild manufacturing capacity<sup>25</sup> and restore better paid industrial jobs using subsidies and trade barriers.<sup>26</sup> The policy that “could not be named” has emerged from the attic.<sup>27</sup> The shock to supply chains administered by the pandemic, the desire to minimize dependence on strategic adversaries in a tense global environment, and the urgent need to adapt to climate change and tackle associated market failures suggests that industrial, technological, and associated trade policies are here to stay (Cherif and Hasanov 2019).<sup>28</sup> In fact, they never completely exited the stage in western countries and were put to fruitful use by China and others.<sup>29</sup> Now the desirability of industrial policy is being acknowledged in neoliberal strongholds that had allowed manufacturing to melt away and are coming to terms both with the strategic vulnerabilities caused by industrial hollowing and the political discontent of those who paid the price of globalization (Dippel et al. 2022).<sup>30</sup> The losers blame the elites for their misfortune and are receptive to the promises of authoritarian politicians who claim that they will dismantle the system and dispossess the (exploitative) elites (Eichengreen 2018).

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25 Summers (2023) doubts that a renaissance of US manufacturing is of importance for US prosperity. He claims that “the idea that we can build an economy on growing our manufacturing sector is just not realistic and potentially counterproductive.”

26 The use of subsidies by developed countries to reshore industry is creating problems for others. Wall Street Journal (2023); Critiques of industrial policies are abundant. See Hufbauer and Jung (2021); Irwin (2023); Bartelme et al. (2021) <https://www.bostonreview.net/forum/industrial-policys-comeback/>; Economist (2022). Lane (2021); both Irwin (2019) and Summers (2023) reaffirm the benefits of freer trade for economic efficiency and growth.

27 This is how Robert Wade (2015) explains why IP is back. “Many advanced and developing countries are worried about the erosion of manufacturing in the face of Chinese competition, many middle-income countries are worried about being stuck in the middle income trap, many lower-income countries are worried about being stuck as commodity exporters, running faster to stand still, while many governments—developed and developing—are trying to target investment in “green” industries. These trends have helped to rekindle a broad interest in industrial policy, and national strategy more generally, in developing countries.”

28 Juhasz, Lane and Rodrik (2023) offer a positive take on the latest manifestations of industrial policy and a brief tour of the voluminous literature; the effectiveness of industrial policy instruments is the topic of an exhaustive survey by Criscuolo et al. (2022); Andreoni, Chang and Scazzieri (2018) also provide a broad ranging and positive read on the topic.

29 The industrial policies pursued by Korea, Taiwan, China, and others in East Asia were not motivated by market failure—the conventional justification for remedial action by the state. Instead, leaders in these countries were motivated by the belief that industrialization was essential if a country was to develop and catch up with the ‘West’. They were also motivated by security considerations, which loomed large for some of the Tiger economies in the troubled 70s and especially following President Nixon’s announcement of a new doctrine in 1969 calling upon the East Asian allies to shoulder more of their defense burdens. The efficacy of industrial policies by Korea and China has been challenged, most recently by Kim, Lee, and Shi (2021); Barwick et al. (2019); Branstetter and Li (2023). The researchers maintain that these policies misallocated resources, gave rise to persistent excess capacity, and did not improve total factor productivity. Excess capacity from over investment has been endemic in China affecting the auto industry, solar panel, wind turbine, iron and steel, shipbuilding, and other industries.

30 Cox (2018) notes several reasons for the rise of populism: finding meaning in a runaway world; identity crisis; powerlessness; increasing inequality; immigration, the fear of cultural dilution and loss of privileges; among others; Broz et al. (2021); Bardhan (2017).

The industrial policy now in vogue is more elaborate than what was practiced by the Four Tigers in the 1960s and 1970s, and it comes in different flavors. In the 1960s, the objective of developmental states was the rapid creation of an industrial base using state of the art technologies. East Asian firms were quick to cultivate the skills required in-house and leverage skills from abroad to adapt and utilize the technologies they borrowed. However, at that catching-up stage, little effort was expended in pushing the technology frontier.

The 'new' industrial policy has at least two principal variants (and there are subvariants as well). The advanced countries are attempting to selectively rebuild manufacturing capabilities using a mix of tax, subsidy, trade, technology, and manpower policies and market signals to galvanize private investment. They and a few upper middle-income countries assign greater importance to RD&I recognizing that domestic research accelerates technological assimilation, innovation drives productivity and coping with climate change via economic greening will be impossible absent technological advances across a broad front. Techno-industrial policy is the new normal. These countries have adopted the so-called soft industrial policy (Harrison and Rodriguez-Clare 2010).

An approach that combines 'soft' with 'hard' industrial policies is the rule in countries where the share of the public sector in industrial activity remains significant and the state has a major say in the allocation of financial resources through state owned or controlled banks and sovereign wealth funds. The state targets priority sectors and their development becomes the priority of SOEs and of private conglomerates allied with the government. To realize its objective, the state makes liberal use of carrots and sticks (Bailey et al. 2019). Japan and the Four Tigers pioneered the 'hard' variant and directed techno industrial policy has since been adopted by other Asian and a few Middle Eastern countries. China has also assigned primacy to digital, AI, biotech, and other technologies in development (Ling and Naughton 2016). Countries that have been slow to join the technology race as in the Middle East, have paid a penalty in terms of GDP growth (Arezki et al. 2019).

With the advent of AGI, techno industrial policies—soft and hard—have acquired an engine with the potential equivalent to electricity if the instant punditry is believable. Undoubtedly, AGI will spawn multiple innovations and find many uses not all of which will be welcome, but so long as positive outcomes substantially surpass the negative ones, it could very well put additional wind in the sails of industrial policy. By yoking the pursuit of technological advances to other policy initiatives, governments have enhanced the utility of industrial policy for the current era. AGI could further improve the design of policy, implementation, speed of midcourse correction where needed, and the learning from outcomes.<sup>31</sup> Because digital and AI technologies straddle and closely link many services with manufacturing, the ambit of industrial policy has been greatly widened to encompass much of the economy. With the value added by services constituting an increasing share of the value of manufactured products, it is difficult

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31 How governments can profit from technology are examined by Hinkley (2023); Whether this improvement will come to pass is uncertain given the absence of measurable gains in efficiency despite widespread adoption of digital technologies. Devarajan (2019).

to separate one from the other. Now a government pursuing industrial policy is not merely focused on manufacturing. Policies must accommodate the role of services and take account of an agricultural sector that overlaps with both manufacturing and services.<sup>32</sup>

We can see developmental policymaking circling back to the maxims of the 1960s, enlarging the sectoral scope of policy and in the process merging industrial with technology policy.<sup>33</sup> But this turning back to the future has retained some if not all the policies that took root starting in the mid 1980s. In fact, the prescriptions spelled out in the Washington Consensus have acquired renewed pertinence in the aftermath of the pandemic.

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## The Washington Consensus is reborn as one strand of a Post-Covid Consensus

After enduring a barrage of criticism, the WC much like industrial policies, tipped into the netherworld—not quite forgotten but largely banished from conventional discourse (Krugman 1995; Rodrik 1997; Rodrik 2006). As the creator himself observed (Williamson 2002), “the Washington Consensus is a damaged brand name. Audiences the world over seem to believe that this signifies a set of neoliberal policies that have been imposed on hapless countries by the Washington-based international financial institutions and have led them to crisis and misery. There are people who cannot utter the term without foaming at the mouth.” It is back in the form of a post-Covid Consensus that incorporates industrial policy.

A workable export-led strategy necessitates a single competitive exchange rate (Irwin 2021; Sachs 1987; Chung and Eichengreen 2016). This was integral to the approach adopted by Japan, the Tigers and China. An overvalued exchange rate inhibits exports, can lead to current account deficits, depletes reserves, invites a crisis, and eventually compels painful adjustment. Lowering barriers to trade and policies incentivizing FDI can facilitate the growth of tradable activities, integrating with the global economy, raising productivity, and increasing exports. Countries, several in South Asia, can improve their export performance by removing impediments to intermediate imports (Handley et al. 2020; Narain and Varela 2017; Ahn et al. 2016). Those that are raising these barriers (e.g., India, the US)<sup>34</sup> must weigh benefits against the longer-term costs.

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32 Agriculture is poised for a second great leap with the entry of smart agricultural equipment, AI, analytics, and connected sensors (embedded in farm machinery and drones), which could stimulate agricultural productivity, conserve inputs, and make the cultivation of crops and animal husbandry more resilient.

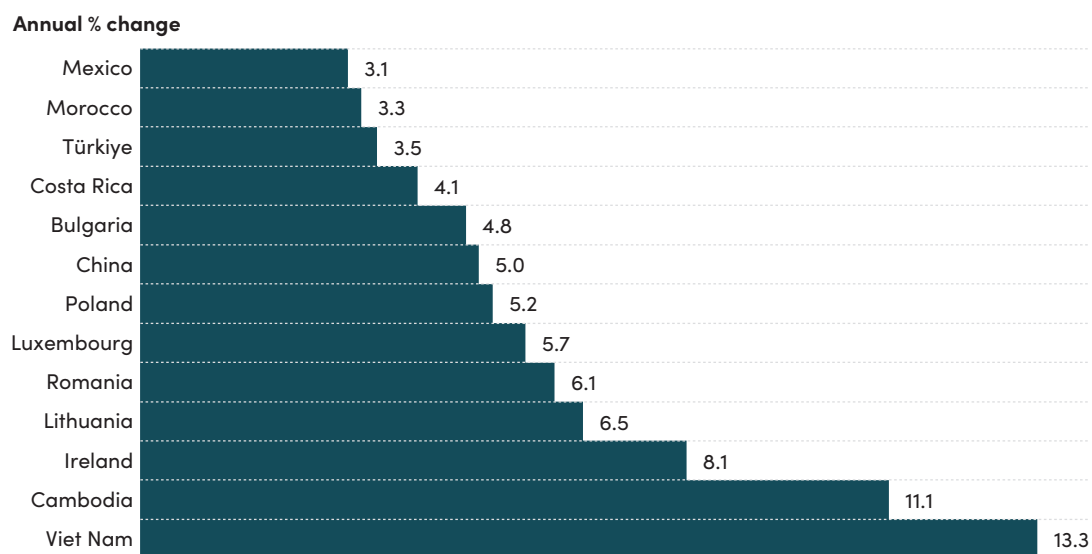
33 The return of IP has predictably aroused alarm. Those that can remember only the costly mistakes committed by policymakers “who love industrial policy” doubt that any government can be trusted to target wisely. At best, they would in Ruchir Sharma’s words prefer only “a pinch of industrial policy” believing that anything more could overpower market forces and prolonged use could cause lasting harm. Sharma (2023).

34 <https://www.reuters.com/article/us-india-trade-duties-exclusive/exclusive-india-plans-extra-tariffs-trade-barriers-on-300-imported-products-sources-idUSKBN23P2C1>; <https://www.reuters.com/world/asia-pacific/india-plans-measures-curb-chinese-imports-trade-gap-concerns-mount-sources-2023-01-30/>; <https://www.uschina.org/tariffs-china-weigh-american-economy-critical-time>; <https://www.cfr.org/blog/cost-trumps-trade-war-china-still-adding>; <https://www.wsj.com/articles/india-restricts-laptop-imports-to-boost-local-manufacturing-244cf56a#>



FDI in manufacturing and infrastructure was instrumental in launching the East Asian Miracle during the last quarter of the 20th century with Singapore and Taiwan among the leading beneficiaries. It also initiated export led growth in Southeast Asian economies such as Malaysia, Thailand and more recently, in Vietnam. Although Latin American countries also attracted such investment, import substituting industrialization and natural resource development were the primary focus and this muted the impact on growth.<sup>35</sup> FDI will be just as critical for the next stage of development in those countries where industrial diversification is marking time and in late starters where industrialization has failed to acquire much traction or is declining as a share of GDP (Babu and Vinita 2019).<sup>36</sup> Therefore, attracting FDI that would promote export and growth prospects, deserves priority. Countries such as Vietnam, Ireland and Cambodia that took this recommendation on board in the 1980s and 1990s increased their participation in GVCs and made rapid progress (Figure 9). The ones that were less welcoming lost ground. This Consensus dictum has surrendered none of its relevance.

**FIGURE 9. Average annual growth of GVC participation 2010–2020**



Source: WTO (2023). [https://www.wto.org/english/res\\_e/booksp\\_e/wtr23\\_e/wtr23\\_e.pdf](https://www.wto.org/english/res_e/booksp_e/wtr23_e/wtr23_e.pdf).

Note: GVC participation is measured as the sum of foreign value added in exports and domestic value added in other economies' exports. Preliminary data for 2020.

Domestic investment in productive assets must complement FDI and in virtually all cases, domestic capital accumulation is the primary driver of growth. How much investment finds its way into the most rewarding activities is strongly influenced by the business environment. An excess of

<sup>35</sup> <https://blogs.iadb.org/integration-trade/en/foreign-direct-investment-in-latin-america-and-the-new-global-outlook/>

<sup>36</sup> Asian countries are actively wooing foreign investors. Some such as Sri Lanka to revive crisis hit economies, others such as India to accelerate industrialization and still others such as China, to sustain technology transfer. <https://www.reuters.com/markets/asia/sri-lanka-expects-fdi-jump-13-bln-with-india-taking-lead-2023-05-24/>; <https://www.csis.org/analysis/agenda-india-re-ignite-interest-among-foreign-investors>; <https://www.china-briefing.com/news/foreign-investment-in-china-august-2022-round-up/>

regulation and red tape that breeds corruption, entry barriers that discourage new starts, and barriers to exit including financing from public entities, that permit zombie firms to survive, waste resources and hamper growth.<sup>37</sup> A pruning of the regulatory overburden together with measures to strengthen market institutions to protect property rights (including intellectual property) enforce contractual obligations and regulate market conduct, are essential strands of a growth strategy.<sup>38</sup> They need to be buttressed by two other policies: competition policies, which favor creative destruction and a churning of firms, and systematic efforts to privatize those public enterprises that ought to be in the private domain. Competition, when not excessive, boosts productivity and innovation (Aghion et al. 2021).<sup>39</sup> All countries can benefit from more of both. And such policies judiciously implemented also curb the concentration of dysfunctional market power and crony capitalism, which is rife in many countries.

Troubled SOEs are an economic and social burden for many countries. Many are propped up by subsidies that eat into government budgets (World Bank 2021).<sup>40</sup> Those that break-even are frequently less productive and profitable than comparable private businesses. With fiscal pressures mounting, privatizing or corporatizing (as in China, Vietnam, Singapore and throughout Latin America mostly from the 1990s) the viable SOEs and shuttering the ones that cannot be salvaged should be high on national reform agendas.<sup>41</sup> Privatization can be a thankless and politically perilous endeavor for elected officials, and it is not guaranteed to deliver positive outcomes. Nevertheless, by neglecting to grasp the nettle and to tackle the failings of SOEs, governments store problems for the future when a reform of public enterprises might be no easier.

Capital accumulation is the principal source of growth deep into economic maturity.<sup>42</sup> The Tiger economies and others that sustained high rates of growth for extended periods did this by dint of resource mobilization from domestic sources supplemented by FDI and overseas borrowing. Private saving can be encouraged through financial deepening and interest rate policies that provide savers

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37 The Covid Pandemic led to an increase in zombification, which is bad news for allocative efficiency and productivity. Albuquerque and Iyer (2023): <https://www.oecd.org/economy/growth/exit-policies-and-productivity-growth.htm>

38 Dixit (2015) maintains that countries can reach middle income levels with mediocre institutions, but to rise beyond requires better institutions and the adequate and accessible supply of public goods.

39 The several different facets of creative destruction are covered in detail by P. Aghion et al. (2021). And by the contributors to U. Akcigit and J. Van Reenen eds (2023).

40 The problem of SOE inefficiency and indebtedness is especially acute in South Asia. (World Bank 2021). <https://openknowledge.worldbank.org/server/api/core/bitstreams/9c7716eb-d498-5406-b95d-d03f5e0b8754/content>; <https://www.dawn.com/news/1748923>; <https://thediplomat.com/2022/07/sri-lankas-state-owned-enterprises-are-a-big-part-of-its-economic-problems/>

41 Such a move can be beneficial as it can release entrepreneurial energy and resources held captive by SOEs as happened in China following the downsizing of the SOE sector in the late 1990s (Fang et al. 2023). However, privatized Chinese SOEs remain less profitable and innovative than their private counterparts and receive larger subsidies. Harrison et al. (2019); Kikeri (2022) reviews the mixed experience with privatization, which is not necessarily the ideal solution in all cases. Del Castillo (1995); Musacchio et al. (2015) examine how SOE performance in Latin America can be improved through measures that fall short of privatization.

42 China has probably extracted most of the mileage it can from massive capital investment and is encountering diminishing returns, which explains the fixation with innovation and productivity. Garcia-Herero (2023); World Bank (2019); Weinstein (2022).

with a decent return and promote allocative efficiency.<sup>43</sup> Financial reforms along these lines and governance measures that increase public confidence in the capabilities of the state, are the only levers available to governments.<sup>44</sup> Once growth accelerates, private savings generally trend upwards as consumption propensities tend to lag the increase in incomes. Digitalization has accelerated financial development (Fintech) in SSA and Asia.<sup>45</sup> The tempo needs to be maintained because climate change plus the associated greening and spatial restructuring of economies, will require a huge increase in investment.

Public saving can supplement the resources generated by the private sector. How this can be done has not changed in four decades. The standard recommendations include simplifying and broadening the tax base, that increases revenue elasticity, strengthening the tax administration and collection infrastructure (electronic filing) and making more effective use of digitalization, Big Data and data analytics.<sup>46</sup> These plus expenditure reduction can contain public indebtedness and increase public savings. The desirability of avoiding or narrowing fiscal deficits following the Covid related splurge in public spending, is greater than ever.<sup>47</sup> With longer term interest rates trending higher and growth rates during the near term likely to slow, governments face increasing fiscal pressures as revenues will be growing more slowly if at all and debt servicing will reduce the fiscal headroom. It already exceeds 50 percent of government revenue in Pakistan and is close to that level in Egypt. Ghana, Costa Rica, Iran, and others are also under budgetary stress (Wolf 2023). Fiscal prudence is the watchword for all countries as black swans will continue to materialize<sup>48</sup> and countries will need all the fiscal firepower they can muster and build domestic savings to augment potential growth.

The worrisome spike in inflation during the Covid pandemic has been slow to subside. This is in part because of higher energy and food prices courtesy of the Ukraine conflict. Monetary policy is also to blame, which after years of subdued price increases had become relatively lax (Gopinath 2023). Governments need to anchor inflation expectations using monetary and exchange rate policies. By doing so, they will be able to respond more quickly to shocks, avoid the deflation that can accompany a negative shock, and restore equilibrium.

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43 Estrada et al. (2015) survey the literature and extend the findings. Effective regulation and supervision of banks can build confidence and avert crises.

44 Greater financial literacy and awareness of the need to save for old age can also motivate higher saving. Others include saving to purchase a home, finance children's education and dowries, and cover expenses during retirement as social safety nets are insufficient in most countries.

45 World Bank (2023). <https://blogs.worldbank.org/voices/fintech-and-financial-services-delivering-development>

46 The VAT and property taxes are regularly touted, the latter can be a good source of revenue especially for subnational governments, but the authorities face strong political and taxpayer resistance—including in China. <https://www.adb.org/sites/default/files/publication/751846/assessment-tax-capacity-southeast-asia.pdf>; <https://www.imf.org/en/Publications/fandd/issues/2018/03/akitoby>

47 China finds itself in a policy pickle because total debt is equal to 300 percent of GDP and the cumulative debt of the central and local governments has risen to 90 percent of GDP.

48 Talk of polycrisis and permacrisis might be exaggerating the frequency and magnitudes of problems to come but nevertheless, fiscal repair ought not to be delayed. The Lancet (2023) warns against excessive public health catastrophism.

On evaluating research on macro policy, Irwin (2020) concludes that standard neoclassical policies consistently implemented, “produced tangible benefits while unorthodox populist policies have entailed significant economic costs. A key challenge for policymakers is to ensure that the benefits of economic reform are widely shared so that the divisions that lead to economic populism do not arise and erase those gains.” He echoes two stylized facts reported by Easterly (2019): that reforms have made substantial and remarkably encouraging headway since the 1990s; and that this is supported by a strong correlation between policy improvements and growth outcomes.

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## **There is a workable strategy, however, implementing it will test the leadership, resolve and capabilities of governments**

The economic development that took place between the mid 1950s and 2008 was unprecedented. As Steven Pinker (2011; 2018)<sup>49</sup> recounts, life has become a lot better. The incidence of wars has diminished “rates of disease, starvation, extreme poverty, illiteracy and dictatorship, when they are measured by a constant yardstick, have all decreased—not to zero, but by a lot.” To which Dasgupta (2023) adds that global GDP has grown 15 times since 1950 and global per capita GDP at \$18,000 (in PPP terms) is five times higher although the global population has increased from 2.5 billion to 8 billion.

The Financial Crisis brought an era to a close. Ever since, the pillars of the post Second World War prosperity are under siege. Democracy has eroded,<sup>50</sup> capitalism is blamed for a host of ills including inequality<sup>51</sup> and the benefits of globalization are increasingly contested by the losers whose rage and insecurity has contributed to an upsurge in populism worldwide.<sup>52</sup> There is greater (but still insufficient) awareness of the environmental cost of prosperity and of the dangers

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49 <https://www.washingtonpost.com/news/inspired-life/wp/2018/02/13/a-famed-harvard-professor-explains-why-the-world-is-actually-becoming-a-much-better-place/>; Pinker’s views are elaborated in two publications (2011; 2018).

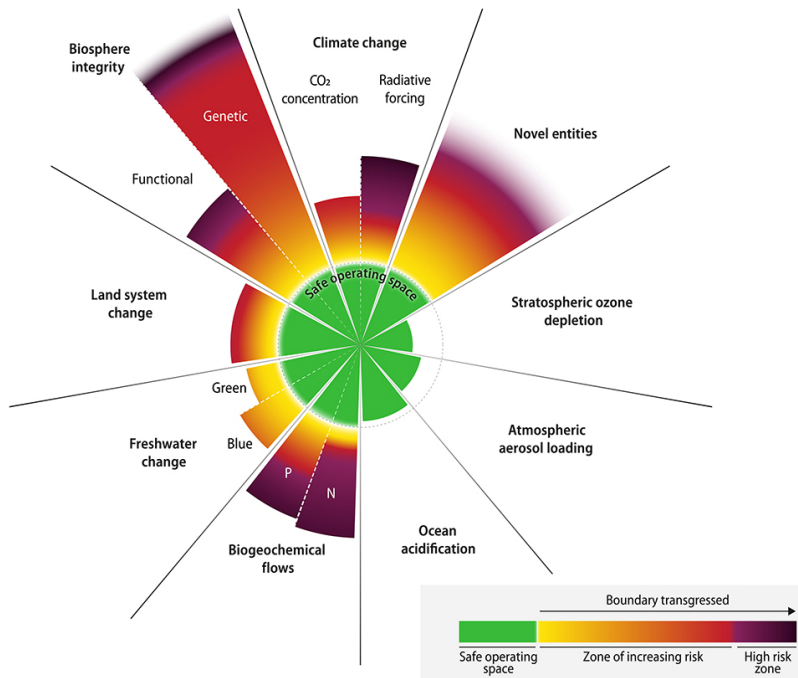
50 Liberal democracy according to V-Dem peaked in 2012 and it is now down to the level last seen in 1989 with only 34 countries accounting for 13 percent of the world’s population, making the cut. *V-Dem Democracy Report 2022*. [https://v-dem.net/media/publications/dr\\_2022.pdf](https://v-dem.net/media/publications/dr_2022.pdf)

51 A survey of economists concluded that increasing inequality was casting a shadow over capitalism. <https://www.promarket.org/2022/05/04/chart-of-the-week-income-inequality-threatens-capitalism/>; T. Piketty (2014) argued that the inequality was inherent to capitalism because the rate of return on capital and wealth ( $r$ ) owned by a small minority exceeded the growth rate of the economy ( $g$ ). A. Kling examines the pros and cons of capitalism and how it affects the distribution of income and wealth. He writes, “I believe that capitalist dynamism does produce losers in the short run. I believe that some winners are merely lucky. I believe that some winners acquired much of their wealth by cheating the system. I believe that wealth enables the rich to get more than their share of positional goods. And I believe that the wealth/power feedback loop is problematic. I think that it is beyond debate that capitalism is imperfect. However, the more interesting question concerns how to try to improve it”. <https://www.econlib.org/library/Columns/y2016/Klingcapitalism.html>

52 The benefits conferred by globalization have been catalogued by many. E.g., Martin Wolf, Jagdish Bhagwati etc. and more recently by Irwin (2022). In his Richard Cooper lecture at PIIE, Summers (2023) called on America to underwrite, underpin, undergird an increasingly integrated and prosperous global economy. The link between globalization and populism is examined by Rodrik (2021); labor displacing technological change and the financial crisis both appear to have fueled the rise of right-wing extremism. Milner (2021).

inherent in climate change that are undermining human development.<sup>53</sup> A report published by Science (September 2023) states that having transgressed six of nine boundaries, the Earth is now well outside the safe operating space for humanity—it is a state without analog in human history (Figure 10). But denialism and the resistance from powerful interests with a stake in the continued use of fossil fuels, in deforestation and the exploitation of natural resources, is a brake on the required rapid transition to green and sustainable development (Bohr 2023).<sup>54</sup> The persistence of fossil fuel subsidies even as mean temperatures set new records, speaks for itself (Figures 11 and 12).

**FIGURE 10. The nine planetary boundaries and the status of transgression**

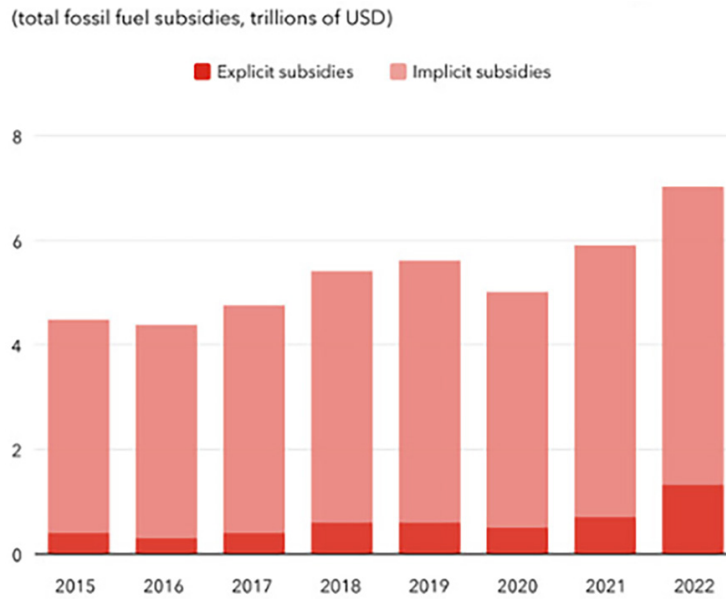


Source: Richardson et al. (2023). <https://www.science.org/doi/10.1126/sciadv.adh2458>.

53 The unsustainable mining of nature's resources is the subject of the Dasgupta report (2021). The Planetary Pressures Adjusted HDI is an attempt to capture the true gains in development. <https://hdr.undp.org/planetary-pressures-adjusted-human-development-index#/indicies/PHDI>

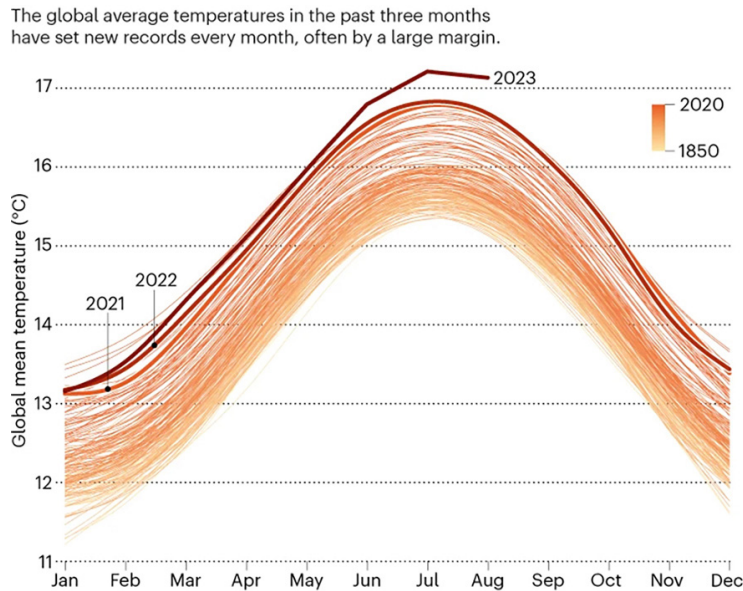
54 Whether denialism is in its death throes is not easy to gauge. To paraphrase Mark Twain, 'Rumors of death can oftentimes be exaggerated.' Washington Post (2023) <https://www.washingtonpost.com/politics/2023/07/07/climate-denialism-gone/>

**FIGURE 11. Fossil fuel subsidies rising**



Source: Black et al. (2023). [https://www.imf.org/en/Publications/WP/Issues/2023/08/22/IMF-Fossil-Fuel-Subsidies-Data-2023-Update-537281?utm\\_medium=email&utm\\_source=govdelivery](https://www.imf.org/en/Publications/WP/Issues/2023/08/22/IMF-Fossil-Fuel-Subsidies-Data-2023-Update-537281?utm_medium=email&utm_source=govdelivery).

**FIGURE 12. Temperature soaring**



Source: Sanderson (2023).

From the foregoing one could reasonably claim that governments have the knowledge and policy instruments needed to forge a viable growth strategy. The pros and cons of techno-industrial and neo-liberal policies have been debated and empirically scrutinized for decades. With this knowledge countries could avoid many of the pitfalls and thread their way to a growth that is both sustainable

and inclusive—the two most frequently cited adjectives. But experience indicates that although research by social scientists has deepened the fund of knowledge and policymakers are potentially far better equipped than they were fifty years ago, learning seems to be matched by forgetting and the wealth of (conflicting) information can weaken or drown the signal.

Developmental elites committed to inclusive growth appear to be outnumbered virtually everywhere by elites for whom government policies are a means of maximizing rent with development something of an afterthought.<sup>55</sup> Elites in authoritarian states with strong institutions—where the rule by law overrides the rule of law—are doing no better at pursuing development than the ones in countries where the institutional underpinnings of state capabilities are weaker, and elites jockey and bargain to gain control often temporarily over the levers of the state.

Strong states, which can quickly change direction and take a long view, are more likely to embark on policies without much by way of consultation with key elements of civil society and often with little regard for the general welfare. History shows that top-down policies have an exceedingly mixed record. More democratic systems, with weaker governance processes that are slower to act and less capable of enforcing accountability and monitoring policies, can overall make fewer major policy errors. But consistent application of strategies poses a challenge in the face of elite contestation. On balance, relative to authoritarian states able to exercise tight control, systems that disperse and balance the power of rival interests, are more likely to iterate towards a minimax strategy that probably is the only one that is practicable.

Politics aside, which Acemoglu and Robinson (2012) blame for the failure of nations, all governments must cope with myriad societal, market, legal, and fiscal issues some anticipated some not. Translating policies into action is the job of government bureaucracies, which with few exceptions (Singapore is an oft cited example), are technically ill-equipped, often corrupt, undisciplined, demoralized and enjoying scant public trust.<sup>56</sup> Thus, for a strategy that seems plausible on paper to work can entail persuasive leadership and elite commitment. Neither is in excess supply anywhere however, elites can be incentivized to pursue the kind of techno-industrial cum neo-liberal strategy over the longer term. They can “gamble on development”<sup>57</sup> when they see their own interests and those of the community at large to be aligned; they can be compelled by the seriousness of a crisis and the threat it poses to their grip on power and resources; and they can be induced to prioritize development by external factors and pressures that make it imperative to undertake measures to avoid becoming trapped in a precarious low level equilibrium, and in a few cases, to safeguard a country’s very existence (two of the Four Tigers endured that predicament).

The shock administered by the Covid pandemic and the likelihood that it will not be the last, was a wake-up call for elites the world over. Accelerating climate change and biodiversity depletion are

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55 Elites matter because they own or control resources and institutions.

56 The causes of government failure and some cures are discussed by Schuck (2013) and by Glazer and Rothenberg (2001).

57 This is how Stefan Dercon (2022) visualizes the emergence of elite bargains.

existential threats. Deglobalization, geopolitical pressures, regional tensions, and debt crises among others are an increasing source of worry. These grim realities demand a renewed attention to state capabilities and to reinvigorating democratic institutions on the retreat in too many countries. The post-Covid Consensus presents countries with a menu of options.

To summarize, the emerging post-Covid Consensus comprises the following ten ‘theses’:

1. Fiscal and monetary policies that assure macroeconomic stability, and longer-term budgetary balance to check and where needed, reduce the national debt burden.
2. Financial development and regulation (to achieve good governance) that increases resource mobilization, improves allocation, and minimizes risks from crises.
3. Trade, FDI and infrastructure policies that promote outward orientation.
4. Industrial policy that targets activities with growth potential in all three sectors using a mix of incentives provided by the state and market forces to steer investment both domestic and foreign.
5. Private sector led growth that is disciplined by market competition is less likely to run afoul of the problems that have plagued industrial policy. Hence a contestable market environment and measures facilitating entry (e.g., access to venture capital) can maximize creative destruction tilted towards the creative.
6. Technology and skill development policies that complement industrial ones, enhance innovation and competitiveness.
7. With climate change gathering momentum, minimizing GHG emissions and adapting development in the face of what will undoubtedly be a harsher environment, is a necessity.
8. A spatial strategy that factors in the displacement of populations and the infrastructures needed to accommodate a managed retreat. The displacement will be driven by (i) rising temperatures; (ii) unpredictable weather patterns; and (iii) water scarcity that constrains agriculture and the viability of some urban centers.
9. State capacity—technical, organizational, and political—to mobilize resources,<sup>58</sup> implement policies and provide public goods and services (the Berggruen governance index presents the various components of state capacity Figure 13). This can require a degree of political unification to arrive at a coherent institutional framework because the weakness of shared common interests in divided societies and polities discourages investment in state capacity (Bardhan 2016).
10. The widely shared perception that risks (and uncertainty<sup>59</sup>) are mounting, argues for building of anticipatory resilience in health, finance, and a variety of critical soft and hard infrastructures.

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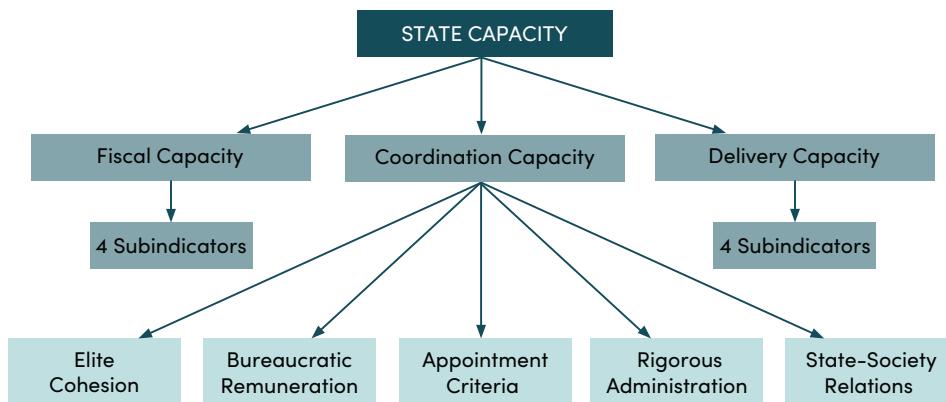
58 The need for increased revenue effort is greater than ever as demands on the government are on the rise and will keep on mounting. Gaspar et al. (2023) note that since 2010, tax revenues have stagnated across all country groupings. “Half of emerging market economies and two thirds of low-income ones had tax/GDP ratios in 2020 lower than 15 percent—a tipping point above which growth has been found to accelerate.” (Figure 14).

59 The economic uncertainty index has been moving upwards since 2016. Bloom et al. (2022).



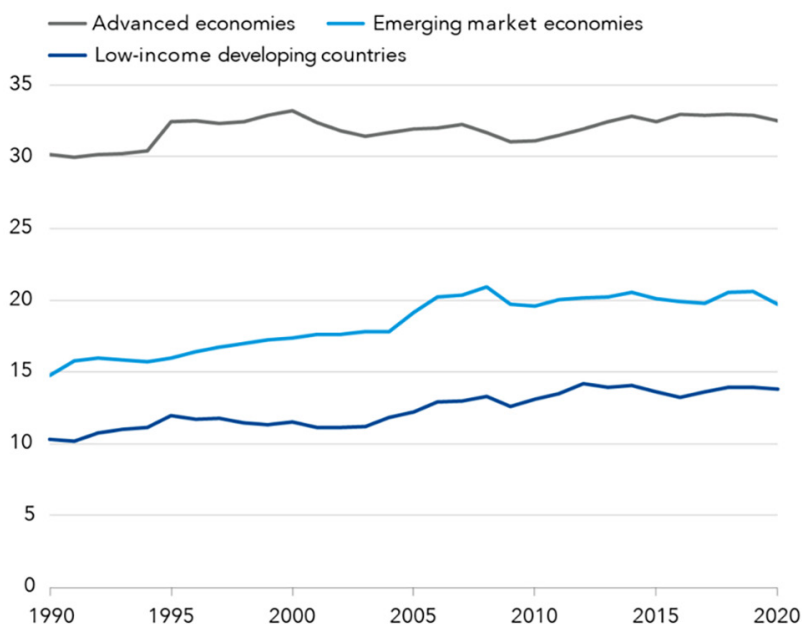
No country has perfect institutions, no system of governance is ever optimal, and the visionary leader, who can deliver perfection, is an extinct species. Dixit (2015) observes that “Property rights and contracts are never 100 percent secure. Legislative and administrative institutions are everywhere plagued by multidimensional problems of asymmetric information and agency. [Therefore] a sensible strategy for reform will look for opportunities to improve institutions and processes but pay due attention to unavoidable limits. [A strategic leader must not reject a reform because it is not perfect]. Nothing is perfect ...We must settle for the feasible least imperfect.”

**FIGURE 13. Factors contributing to state capacity**



Source: Berggruen Governance Index (2022). <https://www.berggruen.org/2022-governance-index/#/>.

**FIGURE 14. Tax revenues across all country groupings (1990–2020)**



Source: Gaspar et al. (2023).

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