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Book Review

Industrial Policy and Development: The Political Economy of Capabilities Accumulation, by Cimoli, M., Dosi, G. and Stiglitz, J.E., Oxford: Oxford University Press, 2009; pp. xix, 575.

Amidst a growing body of scholarly work on the economics of development, this book makes a major contribution not only to this field but also to our understanding of economics. Its most important achievement lies not in the rich tapestry of experiences of nations, or even in the breadth and depth of expertise of its 27 contributors, but by reconnecting economics with the complementary disciplines of history, politics, and political economy, and setting it within the context of culture, institutions and organizational behaviour. This represents a refreshing reversal of the trend of "scientification" of economics that began with the marginalist revolution and continued with the quantification of practically every aspect of economic behaviour. In the process, simplifying assumptions like economic rationality and convergence towards equilibrium have given the discipline the mathematical elegance of the physical sciences but at the cost of realism. In rejecting this approach to economics, this book issues a stark warning that it has gone too far. In doing so, the book's authors give greater substance to what one of them, Stiglitz (2005: 132), noted earlier: "In a market economy with imperfect … information and incomplete markets – which is to say, every economy – the reason that Adam Smith's invisible hand is invisible is that it does not exist." This re-orientation could not have come at a better time, as the onset of the current Global Crisis is calling into question the many dogmas of market fundamentalism that has dominated current economic thinking, and indeed, the very relevance of economics itself.

The tone of the book is set by the broad definitions accorded to its theme – industrial policy. Unlike the conventional understanding of this topic to mean policy interventions by government in industry, the book defines this to encompass education and training, trade and technology policies, as well as targeted industrial interventions (Cimoli, Dosi and Stiglitz – Chapter 1). It rejects the widely held orthodoxy of such policy as a necessary evil in the context of market failure but treats it as a part of the development process. The book's title refers to "political economy" rather than "economics", while

"technology upgrading" is discussed in the broader context of "capacities accumulation". And in its discourse on institutions, non-market institutions like public agencies play as vital a role as market institutions (Cimoli, Dosi and Stiglitz – Chapter 2). Even for market institutions, intangibles such as trust and reputation play an important role (Mayer – Chapter 16).

Incorporating all disciplines pertinent to development also resolves the debate over exceptionalism, which, in the latest incarnation has taken the form of "Asian values". Its detractors may have a point insofar as Asian values, taken in isolation, represent a far-fetched explanation of the East Asian miracle. However, taking into account the mix of conditions that fostered in these countries' high savings, investment in human capital, and technology upgrading, the East Asian experience is no more and no less exceptional than Europe's leadership in the industrial revolution that Landes (1998) and others explain through a "Protestant work ethic" and "scientific attitude". Indeed, as de Maio (Chapter 5) argued, East Asian countries follow paths, given their own institutions and the external environment they face given they were latecomers, not dissimilar to those followed by advanced countries.

The book puts forward three main lines of argument. First, relying exclusively on "getting the price right" can go wrong for latecomer countries' development. This is because the many "truths" of market fundamentalism have been shown to hold no water. Thus, globalization will not lead to international convergence (Castaldi *et al*. – Chapter 3). Indeed, that it will not "lift all boats" has already been quite well documented (for example Birdsall, 2007, Polaski, 2006, 2007), while even the World Bank has revised downward drastically the expected benefits of WTO membership (Blustein, 2005). This is because incentives alone, released by letting the markets rip, are not by themselves sufficient. The evidence marshalled in various chapters of the book (Chapters 2, 8, 13) in contrasting the Latin American with the Asian experience speaks eloquently to this reality. In particular Singh (Chapter 11) refuted the conventional view that it was liberalization that brought on India's growth spurt after 1990.

Second, leaving aside the many developing countries that have pursued policies that stifle development, even sound macroeconomic policies are not sufficient. Kosacoff and Ramos (Chapter 9) showed that in Argentina, exclusive focus on macro management with little regard for micro-management (where technological capabilities are developed) in situations of volatility had adverse consequences for long-term growth. By way of contrast, Brazil actually was successful enough with its macro stabilization policies to begin to focus on industrial policies only to face the challenges of a new environment posed by a rising China (de Castro – Chapter 10).

Third, the inadequacy of relying solely on the market and/or macroeconomic policies to promote growth clears the way for the primary role

of proactive industrial policy, in which institutions, including those of government and education and training, provide vital support (de Maio – Chapter 5 and Mazzoleni and Nelson – Chapter 14). Development then depends on how well "the productive forces are constructed" (p. 3) by these institutions. Government's role is in moving resources to product diversification towards growth enhancing activities, by compelling companies to devote resources in this direction. Especially in the context of production diversification through technology enhancement, the book's authors (for e.g. Reinert – Chapter 4) argue that governments must play a proactive role in enabling emulation before opening up to allow comparative advantage to take its course. Unfortunately, as Akyuz (Chapter 6) noted, advanced nations, through institutions like the WTO, are doing their best to deny merging economies seeking technological catch-up the very opportunities they themselves enjoyed to get ahead. Intellectual property regimes, ostensibly instituted to protect the creators of new technology, have in effect served to preserve the technological edge of existing leaders over late-comers (Cimoli, Coriat and Primi – Chapter 19).

Viewed from this (more comprehensive) perspective, many existing policies are shown to be wrong-headed. A policy prescription that is associated with the neo-liberal view of the "state under the surveillance of the market" (Palma – Chapter 8) is the primacy of competition policy, in which industrial policy is seen as detracting from the former's role. Possas and Borges (Chapter 17) argue, however, this trade-off does not exist if a dynamic view of competition in which market success comes from innovation and adaptation to changing environments rather than in terms of static efficiency, is taken. In similar fashion, empirical evidence from developing countries also rejects the Schumpeterian concept of entrepreneurship based on risk-taking and innovation that shapes and misguides many governments' SME policies today (Hobday and Perini – Chapter 18).

Since the empirical basis for contradicting neo-liberal notions of the role of government in general and industrial policy in particular rests essentially on the East Asian (and Indian) experiences, several caveats need be noted in interpreting these experiences collectively. First, the inclusion of the "continental" states China and India in the group should not diminish the fact that there exist important differences between these behemoths and smaller nations. There exist capabilities that are available to countries of this size and complexities that are not available to smaller countries. In the context of industrial policy, they have the advantage of the size, actual or potential, of the domestic market to force technology transfer by foreign firms, and the depth of human capital to assimilate what is transferred (Dahlman – Chapter 12). Their complexities also allow for examination of issues that are generally absent or are much less significant among smaller countries. For instance,

China's technology scene is characterized by the simultaneous existence of high- and low-tech sectors (World Bank, 2007) that is a direct contradiction of the "flying geese" model other East Asian countries had adopted. In India's case, the existence of technologically capable elites, sizable in number but very small as a proportion of the population, is able to drive a productive service sector more commensurate in size to countries much more advanced in terms of overall technological capacity.

Second, in reviewing the growth performance of these two countries, it should not be forgotten that their present states is being shaped by their very different past. Most strikingly, while both the Indian and Chinese civilizations are ancient, the millennia-old Chinese "civilization state" has been credited as being a source of strength, thanks to the relative homogeneity of its population (Jacques, 2009) whereas the ethnic and cultural diversity in India has produced political bargains, institutions and governance that had to manage these inequalities (see for instance Jayal, 2006; Kasturirangan, 2008). These, and other factors, help explain the vast differences in social structure, institutions and political governance between the two countries. Direct comparisons between them, especially of the genre of who will do better (e.g. Huang and Khanna, 2003) are not particularly helpful. These comparisons also fail to recognize government's ability to reshape comparative advantage through the kind of industrial policy the book's authors emphasize.

Finally, the comparison of East Asia with Latin America does neither region full justice. The East Asia repeatedly cited as successful examples of technology catch-up through proactive industrial policy consists of Japan, the NIEs and China, countries that have invested heavily in human capital and produce a high proportion of graduates in the hard sciences. For the other countries of Southeast Asia, a different reality exists. For example, Palma's (Chapter 8) characterization of the Latin American elite – that they were able to "appropriate large income streams through rent-seeking in a political-institutional settlement with the leadership" fits Southeast Asia's situation to a tee and is a contributory factor in the Asian Crisis of 1997-98. In Malaysia, education policies that produce an inadequate supply and quality of graduates, with a low proportion being in the physical sciences, have left the country with limited technology capacity despite its head start in hosting FDI (see for instance Rasiah, 2002). At the same time, through strengthening institutions including in education, Chile has achieved sufficient progress to be invited by the OECD in December 2009 to become a member, a first for Latin America (Forero, 2009).

None of the arguments advanced by the book's authors is novel, having been discussed by them in earlier work and by others (e.g., Birdsall, 2007; Chang, 2002; Easaw and Savoia, 2009; Milanovic, 2003; Polaski, 2006). However, by drawing together these diverse arguments, the book's authors are

able to propose a coherent "novel international consensus" (Cimoli, Dosi and Stiglitz – Chapter 20) as an alternative to the failed Washington consensus. Will this new consensus fare better? At least, as detailed in the book, it has history on its side.

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