THE PRODUCTIVITY CHALLENGE: GROWTH BEYOND THE COMMODITY BOOM

Dani Rodrik
November 2017
A new world…

- Commodity super-cycle has ended
- (Premature) deindustrialization is well underway
- Globalization has peaked
And new priorities…

• Domestic productive integration (vs. international integration)
• Employment generation (vs. technology/innovation)
• Pragmatic government-business collaboration (vs. “neoliberalism”)
Peru in comparative perspective: GDP growth
Proximate sources of economic growth

Overall growth =

- employment growth
- upgrading of labor skills
- physical capital investment
- total factor productivity (TFP) growth
  (an amalgam of increased efficiency in resource use and technological progress)

labor productivity growth
Peru in comparative perspective: labor productivity growth

Note: All data on labor productivity and its sources are from Conference Board, Total Economy Database.
Peru in comparative perspective: TFP growth
Where does productivity come from?

- **Advanced countries:**
  - technological innovation, R&D, new products and processes

- **Developing countries:**
  - adoption and adaptation of existing technologies
  - structural change
    - creation (or expansion) of industries that exist elsewhere but are new to country
    - movement of resources (labor) from traditional to modern activities
      - from traditional agriculture to modern industry and services
      - from informal to formal activities
Where does productivity come from?

• Advanced countries:
  • technological innovation, R&D, new products and processes

• Developing countries:
  • adoption and adaptation of existing technologies
  • structural change
    • creation (or expansion) of industries that exist elsewhere but are new to country
    • movement of resources (labor) from traditional to modern activities
      • from traditional agriculture to modern industry and services
      • from informal to formal activities
Labor productivity gaps across sectors
Labor productivity gaps among firms

Figure 24. There are large differences in productivity levels across firms in Peru

(percentage difference in productivity between the 90th and 10th percentile of the productivity distribution)

Source: Peru data are from a background paper prepared for this report by Iacovone and Tran (2015); data for other countries are from Inter-American Development Bank (2010).

Labor and capital move to more productive firms in manufacturing, but not in services.

Figure 29. Allocation of factors in manufacturing has improved, boosting productivity growth

Source: Authors’ calculations: Background paper prepared for this report by Iacovone and Tran (2015), based on Annual Economic Survey (Encuesta Económica Anual, EEA) by INEI.

Figure 30. Services have seen no improvement in allocation, dragging down aggregate productivity growth

Source: Authors’ calculations: Background paper prepared for this report by Iacovone and Tran (2015), based on Annual Economic Survey (Encuesta Económica Anual, EEA) by INEI.

De-industrialization despite a more productive manufacturing
Employment has moved to services

Can de-industrialization be reversed?

• The global context: not very favorable
• This is not a new (or temporary) phenomenon, but a secular one
  • due to technology, global competition, and demand shifts
The manufacturing curve: how manufacturing evolves over the course of development
Peru is at or past the turning point.
Moreover, manufacturing has been trending down everywhere at a rapid clip over long term

Employment

Estimated coefficients on decade dummies from a regression where manufacturing shares are regressed on income, population (and their squares), country fixed effects, and period dummies
Except for output shares in a handful of manufacturing exporters

Output

Estimated coefficients on decade dummies from a regression where manufacturing shares are regressed on income, population (and their squares), country fixed effects, and period dummies
Intermediate conclusions and implications

- The most productive parts of the economy (tradables, agribusiness, mining) unable to grow sufficiently to absorb workers from traditional agriculture and informality
- Usual remedy for this problem: rapid industrialization
- Peru is unlikely to re-industrialize
  - premature de-industrialization is a secular, global phenomenon
- Focus of productivist policies has to shift to services and non-tradables
- Integrate most productive parts of the economy with the less productive segments
  - across multiple divides: spatial, size, export-orientation, formality
- Much, much harder: no blueprint exists
Standard remedies for improving productivity

- Increase innovation
  - enhance market competition, R&D spending, human capital, non-traditional agriculture
- Improve education
  - spending on education, teacher training
- Enhance infrastructure
  - roads, ports, energy
- Improve governance
  - better regulation, courts, administration
- …

Standard remedies for improving productivity

- Increase innovation
  - enhance market competition, R&D spending, human capital, non-traditional agriculture

- Improve education
  - spending on education, teacher training

- Enhance infrastructure
  - roads, ports, energy

- Improve governance
  - better regulation, courts, administration

- A long laundry list of demanding tasks
  - like saying, “if you want to become Sweden, look like Sweden…”
  - not helpful since country needs to generate productive jobs for today’s workforce and with today’s institutional capabilities
Standard remedies for improving productivity

- **Increase innovation**
  - enhance market competition, R&D spending, human capital, non-traditional agriculture
- **Improve education**
  - spending on education, teacher training
- **Enhance infrastructure**
  - roads, ports, energy
- **Improve governance**
  - better regulation, courts, administration
- **Not very well targeted**
  - problems and obstacles tend to be highly specific to industries
Setting priorities: two styles of policy

• General purpose, top-down, presumptive
  • focus on deregulation and cutting red tape
  • comparative benchmarking to identify areas of underperformance (using WEF, WB. etc, indicators)
  • government agencies as providers of a package of predetermined services
    • skills training, credit, tax exemptions (free trade zones), marketing/promotion assistance, free-trade agreements,…

• Problem-driven, experimental, interactive
  • ask what's blocking new activities from emerging, modern firms from expanding
    • address specific obstacles
    • monitor
    • revise as needed
  • government agencies as problem solvers for private sector

• Different requirements for how public and private sectors should organize themselves
Setting priorities: two styles of policy

• General purpose, top-down, presumptive
  • focus on deregulation and cutting red tape
  • comparative benchmarking to identify areas of underperformance (using WEF, WB. etc, indicators)
  • government agencies as providers of a package of predetermined services
    • skills training, credit, tax exemptions (free trade zones), marketing/promotion assistance, free-trade agreements,…

• Problem-driven, experimental, interactive
  • ask what's blocking new activities from emerging, modern firms from expanding
    • address specific obstacles
    • monitor
    • revise as needed
  • government agencies as problem solvers for private sector

• Different requirements for how public and private sectors should organize themselves
Setting priorities: two styles of policy

- General purpose, top-down, presumptive
  - focus on deregulation and cutting red tape
  - comparative benchmarking to identify areas of underperformance (using WEF, WB. etc, indicators)
  - government agencies as providers of a package of predetermined services
    - skills training, credit, tax exemptions (free trade zones), marketing/promotion assistance, free-trade agreements,…
- Problem-driven, experimental, interactive
  - ask what's blocking new activities from emerging, modern firms from expanding
    - address specific obstacles
    - monitor
    - revise as needed
  - government agencies as problem solvers for private sector
- Different requirements for how public and private sectors should organize themselves
The new “productive” policy mindset

- Move away from traditional industrial policy pre-designated sectoral priorities and incentives
- Think of productive policy as a process of strategic collaboration between private and public sectors
  - learning: what are the constraints faced by firms in different activities?
  - experimenting: what are the best ways of removing/compensating for the constraints?
  - coordinating: are all relevant branches of govt around the table and on board?
  - monitoring and evaluation: how well are we doing?
  - revising: does the learning get incorporated into new policies?
- government’s relationship to firms: neither arms’ length, nor captured
- firms’ responsibility: developing plans of action that are in line with public objectives (e.g., employment expansion)
- public accountability through clear set of objectives, assignment of political responsibility, transparency and public communication
Policies for domestic productive integration: general illustrations

- Promote backward integration of modern, productive firms
  - technology dissemination to suppliers (including services)
- Competitive provision of customized services for medium-sized firms
  - in return for monitoring, evaluation, employment commitments
- Publicly funded, professionally managed venture fund(s)
  - to invest in potential clusters with clear social/economic objectives
- Public-private sectoral roundtables to identify and remove specific obstacles
Peruvian illustrations

- Initiatives in **agribusiness** since 1990s: public investment in irrigation, relaxing land use restrictions, reduced corporate tax rate, labor flexibility
  - => diversification into nontraditional fruits and vegetables
- **Mesas Ejecutivas**: working groups with private & public actors organized around a production sector to identify a “list of bottlenecks that affect productivity … and focus on removing those with the understanding that much will be learned during execution” (Ghezzi 2106)
  - Iterated problem solving; deadlock kicked to ministerial level
    - “your problems,” versus “my problems”
  - critical: ability of private sector to identify root problems specific to their domain, beyond generic ones (“too much bureaucracy,” “high taxes,” “energy prices,”…)
- Some early successes in forestry, aquaculture
  - streamlined registration, better financing, reduced lags in permits
Can the success be replicated elsewhere, or is agribusiness special?

- latent comparative advantage
  - land, sun, cheap energy, temperate climate
- social capital and entrepreneurship
  - e.g., role of “visionary producers” and the regional Ica Producers’ Association (IPA) in the development of asparagus cluster
  - perhaps facilitated by experience in providing public inputs (e.g. phytosanitary standards, logistics of cold storage)
- ease of creating special policy regimes in agriculture
  - e.g., corporate taxation, labor rules
- advanced technologies travel easier in agriculture than in manufacturing
  - complements are sun and soil rather than skills
- WTO regime/trade agreements provide fewer constraints on policy autonomy in agriculture than in industry
Concluding remarks

- Last 30 years have reinforced the lesson that globalization is not a development strategy
  - a lesson that could have been avoided by learning from positive examples elsewhere
- But new global context also means policy lessons of the past are less relevant going forward
- Economy-wide structural change remains critical challenge
  - from traditional, low-productivity firms to modern, larger firms
- But will need to focus less on manufacturing and tradables, and more on services and non-tradables
- Importance of pragmatic, non-doctrinaire, experimental policies
  - institutionalized dialog/collaboration between public and private sectors still key