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Review Article

INDUSTRIAL POLICY FOR THE NEW GLOBAL ECONOMY

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***Abstract**: Exceptional global changes in the last few years have led to the emergence of a new economic reality that shapes all parts of the economy and society. The latest technological and global trends have led to a strong increase in the importance of industrial policy. The Fourth industrial revolution, globalization and human capital are the main drivers of today's economic development. Environmental, digital and social transitions shape new types of jobs, services and business models. The changing geopolitical environment greatly affects the industry. The confluence of the COVID-19 pandemic and the Russian-Ukrainian conflict ultimately marked a turning point for the global economy as these key events laid bare economic vulnerability and at the same time made global political tensions worse. Global market competition, protectionism, market disruptions and trade tensions are increasing challenges. Their combined influence gives a new direction to the development of industrial policy and encourages the formation of a system of public instruments to support priority industrial areas. Policymakers in developing economies are increasingly adopting green industrial policies based on the production of green technologies and services. The main goal of the research in this paper is to identify the key features of the new reality that determine the necessity of industrial policy's approach to new trends. Understanding the major changes in the economic environment will help countries and businesses navigate global economic uncertainty with active industrial policies.*

***Key words**: industrial policy, economic development, globalisation, new economic reality.*

***JEL classification:** L520*

1. INTRODUCTION

After the world economic crisis of 2008, the global economy experienced significant changes. Increasing trade conflicts and protectionism have emerged as a result of the changing global economic balance. The confluence of the COVID-19 pandemic and the conflict in Ukraine are key events that have exposed economic vulnerability while greatly exacerbating existing geopolitical tensions. This has led to changes in global trade and dominant investments in safe investments. The conflict between Russia and Ukraine has had a major impact on the movement of goods and people, on the global supply chain, increasing costs, as well as product shortages that have led to food shortages around the world. In addition, the war in Ukraine has not only led to an unprecedented economic separation between the Group of Seven (G7) and Russia, but has further exacerbated existing tensions between the US and China, significantly raising the risk to global supply chains and production networks. Amid new economic and geopolitical realities, new strategies are needed to mitigate growing risks and take advantage of emerging opportunities.

As a result of these growing geopolitical tensions, countries and businesses around the world are intensifying efforts to reduce economic dependencies and eliminate concentrated supply chains, often along emerging geopolitical blocs. Policies to reduce occasional globalization shocks, which are focused on security and resilience rather than efficiency, come with significant risks of fragmenting the global economy. Furthermore, it signals a shift away from liberal economic policies towards increasing government intervention, potentially resulting in weakened global growth. The movement of people, goods and information accelerated by globalization has shaped new economic conditions to which all national economies and governments must adapt in order to achieve economic growth. There was a need for proactive government policies that would overcome the problems and simply improve the economy. Industrial policy has risen to the top of the national agenda in advanced industrial economies. This represents a radical departure from recent economic history and reignites a debate that was waged more than 30 years ago. One of the lessons of the global financial crisis was that countries with a higher share of industry in their GDP were less affected by the crisis. An industrial renaissance began. This, at the same time, changed the discourse of industrial policy. After the long dominance of the laissez-faire approach, economists again began to deal with selective industrial policies. However, this debate is not just a revival of old concepts about the specifics of sectoral industrial policy or a lesson to be learned from the experience of Asian countries (the East Asian miracle). One significant difference is that industrial policy is now being aligned and facing new global challenges. The most prominent example of this new trend is green industrial policy.

The first part of the paper is dedicated to identifying threats and opportunities in the new economic reality. The second part of the paper deals with the role of industrial policy in the economy. Concluding remarks are given in the last part of the work.

2. NEW ECONOMIC REALITY: IDENTIFYING RESTRICTIONS AND POSSIBILITIES

2.1. RESTRICTIONS

Extraordinary global disruptions in the last few years have led to a new economic reality that shapes today's national economies and business results. The global economy is entering a period of slower growth and high inflation, while energy pressures, the rising cost of capital, an unstable labor market, geopolitical risks and the consequences of globalization contribute to greater challenges and uncertainties.

Slower economic growth and rising inflation are key features of global short- and medium-term economic forecasts. Global GDP growth is projected to remain subdued in 2023 and 2024 at 3% and 2.7%, respectively, constrained by the tightening of macroeconomic policies needed to contain inflation (OECD, 2023).

In 2023, the global economy grew at a rate of 3% in real terms, which is among the lowest rates since 1993, if we exclude the recession years of 2009 and 2020. Inflation is expected to decrease to 5.8% in 2024. year, and to 4.4% in 2025, but will remain far higher than the historical trend (4.1% on average during 2010-2020) (IMF, 2024).

In 2024, global real GDP growth is expected to be 3.1% (IMF, 2024). This slowdown is the result of high interest rates, rising business costs and global spending. Nevertheless, predictions are that the global economy will experience a gradual normalization of economic conditions, especially in the second half of 2024, with expectations of further easing of inflation and the conduct of a restrictive monetary policy. This will accelerate growth until 2025, when global growth is forecast to rise to 3.2% (IMF, 2024).

Annual GDP growth in the United States is forecast by the OECD to slow from 2.2% in 2023 to 1.3% in 2024, as tighter financial conditions ease demand pressures. In the Eurozone, where demand is already subdued, GDP growth is forecast to increase from 0.6% in 2023 to 1.1% in 2024 as the negative impact of high inflation on real incomes weakens. Growth in China will be constrained by reduced domestic demand and structural changes in the housing market, and will decrease from 5.1% in 2023 to 4.6% in 2024. (OECD, 2023).

The OECD forecasts that inflation will gradually ease through 2024, but will remain above central bank targets in most economies. Inflation in G20 economies is expected to decrease to 4.8% in 2024, while core inflation in G20 advanced economies is expected to decrease to 2.8% in 2024. Monetary policy should remain restrictive until there are clear signs that underlying inflationary pressures have been permanently reduced.

Manufacturing growth around the world has been hit by slowing growth in China. This permanent slowdown in growth was conditioned by a series of crises. More than fifteen years have passed since the beginning of the global financial crisis, but it is still reflected in the policy choices made by advanced economies. The corona virus pandemic and the quarantine that followed are an additional cause of the increase in the level of public debt and a reversal in global development.

Geopolitical tensions and conflicts have reshaped the international order, which is increasingly multipolar, with far-reaching implications for technology, economic growth and development. These developments pose serious long-term dangers for humanity. Governments are facing growing fiscal pressures due to rising debt and increased defense spending. However, concerns about economic security should not prevent us from taking advantage of opportunities to reduce trade barriers, especially in service sectors.

The short-term challenge for policymakers is to successfully manage the reduction of inflation to the set target, gradually adjusting monetary policy to a less restrictive stance. At the same time, in many cases, they will have to absorb the effects of fiscal tightening, a renewed focus on fiscal consolidation to restore budgetary capacity to face future shocks, increase revenue for new spending priorities, and curb the growth of public debt.

Targeted and carefully timed structural reforms would strengthen productivity growth and debt sustainability and accelerate convergence towards higher income levels. More effective multilateral coordination is needed to resolve debt, create space for necessary investments, and mitigate the effects of climate change (OECD, 2023).

2.2. POSSIBILITIES

The key topics at the annual meeting of the World Economic Forum in Davos, which was held from January 15 to 19, 2024, were "Achieving security and cooperation in a divided world", "Creating growth and jobs for a new era", "Artificial intelligence as a driving force for the economy and society" and "Long-term strategy for climate, nature and energy". "Creating growth and jobs for a new era" was one of the key themes (WEF, 2024).

The meeting provided a platform for the dialogue, research and collaboration needed to avoid a decade of low growth and put people at the center of a more prosperous trajectory. Putting people at the center of a more prosperous growth trajectory, providing economic opportunity and meeting climate goals as well as the UN's Sustainable Development Goals requires investment, which in turn requires a strong global economy (WEF, 2024).

Amid continued economic uncertainty and geopolitical instability, global growth – as measured by gross domestic product (GDP) – has been slower than in previous years.

For the first time this year, the report introduces a Framework for the Future of Growth, structured around four key pillars, to underline the fact that GDP as a metric does not indicate the quality of that growth and its impact on the health of people and the planet.

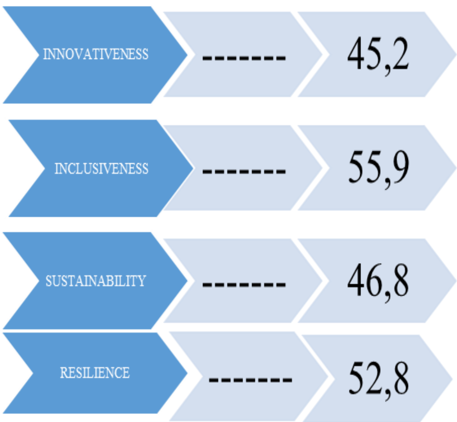
The Growth Futures 2024 report introduces a multidimensional framework for assessing the quality of economic growth in 107 countries around the world. It characterizes a nation's economic growth through four dimensions: innovativeness, inclusiveness, sustainability and resilience (WEF, 2024b).

One of the conclusions of the forum was that in the new economic reality, a simple "return" to GDP growth is not enough, but instead, each country must take a unique and complex path towards achieving innovative, inclusive, sustainable and resilient growth.

As the report states, the key question is how future growth can be better aligned with other important priorities.

In graph 1, we see that the world is only halfway to innovative, inclusive, sustainable and resilient growth.

Graph 1. Global findings of the Future of Growth Report World average score across four dimensions (0-100 scale)



Source: World Economic Forum (2024a). Growth and Jobs at Davos 2024: What to know. WEF.

The forecast of the World Economic Forum's chief economists gives a divided picture for the coming year. Slightly more than half of the chief economists polled (56%) expect the global economy to weaken, and slightly less than half of those polled (43%) foresee unchanged or tougher conditions. The Forum's Global Risks Report 2024 reveals that "a lack of economic opportunity" is ranked as one of the top ten risks over the next two years. In the long term, barriers to economic mobility could grow (World Economic Forum, 2024a).

At the same time, artificial intelligence is having an impact on jobs. An International Monetary Fund (IMF) staff discussion note, Gen-AI: Artificial Intelligence and the Future of Work, reveals that nearly 40% of employees globally are exposed to the impact of artificial intelligence, while in advanced economies that share is 60% of employees (Cazzaniga et al. 2024). College-educated workers and women are more exposed to the impact of artificial intelligence, but they are still more likely to take advantage of its benefits first. At the same time, the increase in productivity could stimulate the growth of wages.

3. THE ROLE OF INDUSTRIAL POLICY IN THE ECONOMY

More recently, there has been a revival of the role played by industrial policy, partly due to the international financial and economic crisis of 2008, partly as a response to structural adjustment processes resulting from the impact of rapid international economic integration. Development literature that deals with the successes and failures of various forms of state intervention and business-government relations observed in developing countries has contributed to this.

After the 2008 crisis and the failure of the free market, there is a widespread re-examination of the importance of industrial policy. In developing market economies, extensive public policies were at the root of industrialization. The experience of conducting industrial policy shows that in most cases, it is difficult to assess whether government policies have been effective in achieving certain outcomes. The dilemma has long been present, would even better results be achieved with a more active industrial policy? (Lutovac Đaković and Medan, 2021).

Andreoni and Chang (Andreoni, Chang, 2019) and Rodrik (Rodrik, 2008) have given convincing arguments in favor of conducting industrial policy. Cimoli, Dosi, and Stiglitz (Cimoli et al, 2009) discussed the importance of industrial policy for developing economies. Industrial and innovation policy, as well as industrial policy in Europe, were dealt with by Pianta (Pianta, 2014), Foster MacGregor (2013) and Aiginger (Aiginger, 2014). Mazzucato (Mazzucato, 2013) emphasized the need for a broad role of "transformative" public action in innovation and industrial change. The role of green industrial policy for accelerating structural changes towards rich green economies was pointed out by Rodrik, Altenburg (Rodrik and Altenburg, 2017).

Based on the debate in the literature, there are five main reasons for the development of a new industrial policy, especially in Europe.

The first is rooted in macroeconomics. Getting out of the current stagnation requires a significant increase in demand, which could arise as a result of public investment. The second reason is related to the changes in the economic structure that are the result of the crisis. The biggest losses occur in "problem" industries. Economic activities that could offer new jobs are needed, while the bloated financial sector should be reduced.

The new industrial policy should encourage the rise of new ecologically sustainable economic activities such as: environmental protection, sustainable transport, energy efficiency and renewable energy sources, dissemination of knowledge, application of ICT and web-based activities, as well as health, population welfare and care activities. All these activities will create jobs that require a high degree of qualifications, but the wages for these jobs will be above average.

Third, a new industrial policy is needed in order for public enterprises to start activities that are unprofitable and therefore unattractive to private investors. There is a need for significant public sector action in setting priorities, investing and creating jobs. Public action could support the organization of new markets, development of competences and entrepreneurship, access to capital, dissemination of knowledge, environmental protection, well-being, social integration and territorial cohesion. The new industrial policy should reverse the situation that arose as a result of mass privatizations in previous years.

The fourth reason for the new industrial policy is related to the regional dimension. A growing gap is emerging within Europe and across the world, which is becoming multipolar. Fifth, a new industrial policy could be the main tool to address the urgent need for environmental transformation.

Making advanced economies sustainable is a transformation that concerns the entire economy and the entire society. Reducing the use of non-renewable resources, developing renewable energy sources and energy efficiency, protecting ecological systems, reducing carbon dioxide and greenhouse gas emissions, reducing waste and recycling are not only environmentally, but also socially acceptable new activities.

A combination of direct public action to provide environmental services and appropriate regulations for private activities is needed, including environmental protection, taxation, incentives, public procurement and the organization of new markets. A new industrial policy could provide a framework for the integration of different instruments of all policies that are needed for sustainable economic development (Pianta, 2015).

Industrial policy has come into disrepute since the 1980s mainly on the basis of two arguments.

First, governments were considered to have no more information than actors in the private sector about the direction in which structural change should be encouraged.

Second, the industrial policy measures used could be subject to lobbying and rent-seeking behavior of economic subjects. "Rent-seeking" or "rent-seeking" is the use of the resources of a company, organization, or individual to obtain economic gain from others, without reciprocal benefits to society through wealth creation.

An example of "rent enjoyment" is when a company lobbies for subsidies, grants or customs protections. These activities do not create any benefit for society, but only redistribute resources from taxpayers to the company (Lutovac, 2020). Partly for the purpose of recognizing the danger of "rent-seeking", the trend in the new industrial policy is to abandon traditional forms based on subsidies and turn towards a "soft" industrial policy based on a facilitating, coordinating role, in accordance with a systemic approach. Government failures are more common in developing countries due to the weaker capacity of governments to design and implement industrial policy (Lutovac, 2020).

A different perspective on industrial policy is needed today, one that focuses on activities to end the depression, finance the necessary public investment and restore sustainable economic activity. Part of the decision on the future development of the industry must be returned to public ownership. The new generation of industrial policies must overcome the limitations and failures of the past, such as collusion between political and economic powerhouses, excessive bureaucracy, lack of accountability and lack of entrepreneurs.

Decision-making mechanisms should be creative, with priority criteria for the use of public resources that include various social interests and are open to the voices of civil society and trade unions.

The general principles of industrial policy are simple. They should favor the evolution of knowledge, technology and economic activity in directions that improve economic performance, social conditions and environmental sustainability, as well as favor activities and industrial sectors characterized by learning processes (individuals and in organizations), rapid technological changes and strong growth . This would include activities focused on knowledge and information and communication technologies (ICT), environment and energy, health and well-being.

Current changes are dominated by ICT. Industrial and technological policies should encourage innovation as a social activity and open process by facilitating rules on access and knowledge sharing, rather than enforcing intellectual property rules designed for a previous technological era. Open source software, copyleft, peer-to-peer activities, Wikipedia make this clear. The potential of ICT and web-based activities have the possibility of wider application, contribute to higher productivity and lower prices, create new goods and social benefits. ICT erases the boundaries between the economic and social spheres.

Current industrial models must be transformed in the direction of environmental sustainability. The technological paradigm in the future will be based on "green" products, processes and social organizations that use much less energy, resources and land, will have much less impact on climate change and the ecosystem, will switch to renewable energy sources; will organize transportation systems based on autonomously driven cars; will rely on the repair and maintenance of existing assets and infrastructure and protect nature and the Earth. Such a perspective opens up enormous opportunities for research, innovation, and new economic and social activities. A new industrial policy should address these complex, long-term challenges (Pianta, 2015).

Green growth requires green technologies: new production techniques that conserve non-renewable resources and emit fewer greenhouse gases. The availability of green technologies simultaneously reduces the social costs of transitioning to a green growth path and helps to achieve a satisfactory level of progress along that path.

The importance of using industrial policy to enable green growth is quite large. The main task facing policy makers is to secure investments in green technologies. Industrial policy can play a significant role in achieving this goal (Rodrik, 2014). The practice of new industrial policy can improve the design of institutional frameworks that counter both informational and political risks.

CONCLUSION

Industrial policy drove the very successful expansion of the economies of European countries from the 1950s to the 1970s. After that, there followed a period when industrial policy became marginalized. During the 1980s, the neoliberal revolution put an end to the old approach to industrial policy. The new ideology even led to the dropping of the term "industrial policy". The result was a general loss of influence over the direction of industrial change and structural adjustment. Interest in proactive industrial policy revived at the beginning of the new millennium.

The most significant reason was that the most successful developing countries, especially the newly industrialized countries of East Asia, were those that led an active policy of industrial development. Another reason was that the policies associated with the Washington Consensus did not sufficiently support economic development and produce the expected results. In recent decades, the dynamics of the world economy have been changing, which is of key importance for the way in which industrial policies can stimulate economic development. Industrial policy lost its selectivity and limited itself to horizontal instruments, such as tax incentives for research and development. In addition, it refers to the prediction of long-term technological trends and market development, as well as providing incentives for the structural adjustment of the national economy to new changes. Policies that facilitate structural adjustment must be reinvigorated to strengthen growth prospects. Lowering labor market barriers and improving skills development could help increase investment, productivity and make future growth more inclusive. A key priority is the revival of global trade, which is an important source of long-term prosperity for both advanced and developing economies. Increased international cooperation is needed to ensure better coordination and faster progress in efforts to reduce carbon dioxide emissions. As climate change mitigation and other environmental challenges increasingly influence the future direction of economic development, environmental considerations should become a key element in creating a new green industrial policy. Finally, it is necessary to consider the implications of recent geopolitical changes, new industrial policies and the development of artificial intelligence for the formation of a new economic framework aimed at avoiding a decade of low growth.

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