Peterson Institute for International Economics

The new age of Western industrial policy: Is there a new playbook?

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[00:00:19.01] - Cecilia Malmström

Good morning, good afternoon, good evening. Welcome to this episode of Trade Winds, where we're going to talk about industrial policy. My name is Cecilia Malmström. I'm a non-resident senior fellow at the Peterson Institute for International Economics. Industrial policy is back again with full strength. Many countries across the world are now adopting new industrial strategies, and we also see, and we've seen that for quite some time, an increase in global subsidies. In the European Union, in the United States, we have Buy America, Buy European, Made in Europe, Made with Europe, made for Europe, and they are all aiming to strengthen innovation and competitiveness. As opposed to the industrial policies in the '70s or early '80s, these new ones also have a very strong economic security element as well. We talk about strategic autonomy with a clear aim of reducing dependencies and vulnerabilities for its own sake, but also because of course many countries, especially in Europe, need to reduce their reliance vis-à-vis China in many key technology areas— life science, nano, batteries, solar, semiconductors, EVs, etc. As a matter of survival for their own industry, according to some voices, a clear element of protectionism according to others.

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So how shall we understand what is happening and what would be the consequences for global trade and economy? To help us sort this out, we have a wonderful panel today. Sean Doherty, who is the Head of International Trade and Investment and member of the Executive Board of the World Economic Forum. He has a long experience also from the private sector. We have Alicia García Herrero, who is a senior fellow at Bruegel in Brussels and adjunct professor at Hong Kong University of Science and Technology and chief economist for Asia-Pacific at Natixis. And we have Peter Rashish, who is vice president and director of economics, geoeconomics program at the American German Institute, a member of the board of directors at the Jean Monnet Institute and former vice president for Europe and Asia at the US Chamber of Commerce. They have, of course, very long CVs, all of these people, but as you can hear, they are very suitable for this panel. A big welcome to all of you. Thank you so much for joining. So when we talk about industrial policy, we often refer to governments making strategic interventions designed to shape the economy by supporting selective industries or technologies or firms to foster competitiveness, growth, innovation, or other goals that the markets fail to address.

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It could be the green transitions, supply chains resilience, for instance. And this can be done by a variety of tools, subsidies, taxes, loans, protection of trades, rules for public procurement, or other regulatory initiatives. So lately we've seen a renaissance of industrial policy all over the world. We see it in subsidies and we see it in the strategies. Of course, the Inflation Reduction Act under President Obama, President Biden in the US, and we have Buy European in the new Industrial Accelerator Act that has been proposed in Europe as well as a response from increased competition, mainly from China, but also as a way to increase independence and divert from, from the US economy. So let's dig into this a little bit and see what, what do we see happening here and what is the new Western industrial playbook look like? Peter, why don't you start? What is happening in the US? I mentioned the IRA by President Obama that has now been sort of killed, even if it lives on in several states. But there's a lot of industrial policy happening in the US as well. Or has it just changed name and now it's called tariffs?

[00:04:21.22] - Peter S. Rashish

Well, thank you, Cecilia. Good to be with you and to be with Alicia and Sean. You're right. I mean, I think the Biden White House really did raise the profile of industrial policy. And in a conscious way as a kind of alternative to trade policy, or at least as a precursor to a trade policy that someday would open US markets. But the idea was, under Biden, was to make the US— make the US manufacturing sector fit to face what it saw as unfair competition from China, as you were alluding to, before the US would engage in trade negotiations. So you had, as you mentioned, you had the Inflation Reduction Act. The CHIPS Act for semiconductors. There was the infrastructure bill, and Biden wanted to deal with the climate crisis, create jobs, face up to Chinese competition. There were a couple of other things. There was the US-EU Trade and Technology Council, which was kind of a non-binding, soft kind of trade policy, as well as something, uh, a little more ambitious, the Global Agreement on Sustainable Steel and Aluminum, which was aimed at creating a kind of club for domestically made and climate-friendly steel. But I mean, I think you, you did see, uh, that something was changing when, when the Biden administration came in and made— pushed industrial policy so, so far to the front.

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Now, under Trump, I, I think there has been some use of industrial policy and some kind of, uh, sense of the term, but instead of subsidies or tax breaks as we saw under Biden, It has really taken more the form of US government, of the US government taking stakes in firms as it's done with Intel, with MP Materials, which is a, I think it's the sole US firm that produces rare earths, US Steel, or also we've seen it take a sort of share of the profits of NVIDIA's chip sales to China. In addition to that, as you mentioned, economic security, there has been some focus on that in industrial policy, for example. You've seen a lot of action on critical minerals. The Treasury Department and the State Department both held meetings recently, uh, the Treasury kind of in a G7+ context. But I would say that the main emphasis or the main tool, uh, that the Trump administration is using to get at some of these industrial policy goals really, um, really is trade and tariffs. And I think that's partly because It is, it is, you know, found it useful to, uh, as part of these trade deals that signed with a number of countries, he's found it useful to use them as leverage to oblige partners to make investment pledges in the U.S. And some of those pledges are in very targeted areas, you know, U.S. manufacturing that are in some very strategic sectors that are sort of really look like industrial policy goals.

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But I think it's also because the administration sees tariffs as so multifunctional. You know, they think it can— they can promote industrial policy goals. They can by raising the share of manufacturing in U.S. GDP, but they can also reduce the trade deficit or generate revenue for the Treasury. So overall, I'd say that the energy during the Biden administration was on industrial policy, specifically subsidies and tax breaks, while the energy now under Trump is on trade policy and especially tariffs.

[00:07:49.22] - Cecilia Malmström

Hmm. We'll come back to a lot of that in a moment. Alicia, in Europe, we have this newly released Industrial Accelerator Act, which is in a way also an inflation reduction act, but focusing a lot on public procurement and the greening of the economy as well. How do you see that as a tool and how important is the China aspect in this, the competition from China?

[00:08:15.03] - Alicia García-Herrero

Yeah, so Cecilia, you stole my headline because I was about to say that this looks very much, with much less money though, very much like some sort of Inflation Reduction Act rather than, of course, going the Trump way tariff-wise. So indeed, a lot of what is, what the Industrial Accelerator Act tries to achieve is first to reindustrialize Europe. So there's a clear target there, 20% from around 14% today manufacturing share to GDP. So that's to start, and that's a clear objective. And again, it's not too different from what we saw from Biden in terms of the scope. Sorry about that. Yeah, sorry, sorry. I turn off the phone, but I guess it doesn't matter. My computer still finds a way to disturb me. So I wanted to say that beyond this industrialization, there is clearly an attempt to especially protect Europe from Chinese dominance in procurement. So procurement is clearly a way to kind of insulate our, if you want, infant industry, I would put it this way, on anything that is green energy. But beyond, because there's also a lot of old sectors there, cement, you know, We're trying to, in a way, protect whatever we can protect, to be frank.

[00:10:02.23]

And there is also, and I think this is very interesting, and in this regard, different from the IRA in the sense that there's a clear part that puts conditions on Chinese FDI into Europe. So we make it difficult for you to come to our procurement, you name it. And on top of that, if you want to be here as part of us, then you need to comply with certain criteria. And those criteria are mostly on tech transfer, even use of European workforce. So, you know, it, it's pretty intense. And I think the big difference from previous versions— and I finished here— is that before there was no, um, it was obviously country agnostic as everything in Europe, uh, but there could be a doubt that we, we really meant made in Europe only. And I think by now it's clearly about China. Because there is a number of targets per sector around 40%. So it basically applies to countries whose global market share is above 40% for that specific sector. And in most cases, I would say in all cases, you can only find China there.

[00:11:14.01] - Cecilia Malmström

So we heard a little bit about this. There are of course other countries who have similar strategies as well, Sean. But looking at it from a more helicopter perspective or the business view, How do you see this and why is it emerging now? Of course, China plays a very, very important role, but that didn't happen yesterday.

[00:11:34.09] - Sean Doherty

Well, and thanks a lot for inviting me to this discussion, Cecilia. So, look, business is clearly very interested in industrial policy. We just had our World Economic Forum annual meeting in Davos a few weeks back, and industrial policy was a big topic on the agenda there. I admit it was a little bit drowned out in the media by interest in Greenland, Prime Minister Carney's speech, President Macron's sunglasses and so forth. But the actual discussions between business, many, many of them focused on industrial policy. And I think that the word Renaissance, which you used earlier, really kind of captures how businesses are seeing this issue. It's not a new one, but these new perspectives are coming to the fore, predominantly resilience, as you mentioned. So clearly there's been a bit of a warm-up to this over the past couple of years. We had COVID when there was massive state intervention, and that was seen to be a legitimate response to, to a crisis. We've seen this reflowering of some forms of industrial policy on environmental grounds as governments try and support industry through an environmental transition. And then also, as you referred to, there's been something of an almost innovation infant industry argument with regards to the digital transition.

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But that has all been now superseded to an extent by firstly a national security logic, which is then broadened into this economic economic security discussion. I think kind of the starting point which business has in this conversation is that they view generally the more short-term operational matters are an area of business competency, whereas when we're talking about long-term economic strategy, that's more the government domain. But there's this gray area in between, I guess you could say, between kind of microeconomics and macroeconomics, but the mesoeconomics where there's this industrial policy interplay happening. And so I think within this world, there's a recognition that maybe trade is not purely about comparative advantage, but it's also a little bit about strategic positioning and where governments are trying to intentionally shape sectoral economic outcomes and at the same time reducing dependence on what they see as potential vulnerabilities. And broadly, you know, the purpose of economic policy is shifting a little bit from just growth and efficiency into this more security and resilience domain. And so firms are needing to learn, you know, how they can interact with that, develop a little bit of geopolitical literacy so they can interact effectively with governments.

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I think, of course, they recognize that there's a number of longstanding traditional questions around industrial policy about how it was historically done, and some of those play out in a purely domestic setting. You know, is this a good use of resources? There are governance questions about essentially the risk of capture of regulators, the fact that sometimes it's hard to turn off the subsidy tap once you've turned it on. But there's also these international questions, as we've heard, you know, where is there potential for harmful spillovers or escalatory response between different governments who are each applying industrial policy tools. I think maybe I'll finish with this, the kind of a particular concern from business at the moment is that industrial policy tends to create uncertainty, particularly if it's not done with very clear governance. And so it tends to divert resources from innovation and working with customers to really spending time lobbying governments, frankly. And, you know, this is a little bit, I guess, compounded by the fact that's an issue which tends to have this issue of concentrated benefit and more diverse costs. And so you quite often have a, you know, fairly vocal voices from those businesses which stand to benefit from industrial policy, where it's a little bit more of a muted choir of a larger number set of firms who worry that this may not be optimal or in the public interest.

[00:15:40.15] - Cecilia Malmström

Well, one can of course understand policymakers and politicians. They see that a lot of jobs are at stake in old traditional manufacturing. Competition is not fair always. And then there is this willingness, at least in most countries, to contribute to the greening of the economy and facilitating the transfer of green technology and so on. But as you all mentioned, we have seen this before. Now, of course, it's a different context and that the challenges are bigger and vaster and there's the security element as well. But Will this work? Is it actually realistic to hope for reindustrialization, or just do we have to interpret that word in a new sense today? What do you think? Who wants to start?

[00:16:23.04] - Peter S. Rashish

Well, I have one thought, which is that I think, you know, in the United States, you know, it could work to a certain degree, but one big constraint is finding the labor force and making sure that labor force is trained and continues to be trained. I mean, I think that is something that we're we're seeing that companies are already bumping up against. And so that, that to me is, is, is when you ask, you know, can it work? I mean, that's a big question mark. I won't— I'm a little cautious speaking about Europe, but I think if I had to think of something across the Atlantic, maybe there is an issue of financing because I don't think industrial policy can entirely rely on government spending and subsidies and tax breaks. You need the private sector to step up too. And that sort of relates to that whole issue of a capital markets union. But I think there are constraints for sure.

[00:17:13.13] - Cecilia Malmström

What do you think, Alicia?

[00:17:14.26] - Alicia García-Herrero

Sure, maybe, um, let's bring a little bit of, you know, this idea of what industrial policy really means in China and what we're talking about here in, in the West. I think for China, industrial policy is really a way to upgrade the industry. That's the industrial policy we refer to when we talk about China. So it's innovation policy. It's, you know, think about AI, it's all about vertical AI for the industry. It's not about GenAI, or at least to a lesser extent. But I think there's also a part of China that maybe we do not call industrial policy because that's maybe not the way we define it, which is actually saving the companies that would not be saved by market forces. Yeah. So if you look at actually the number of subsidies, we think all subsidies are going to build, I don't know, the new sodium batteries. Well, not really. Most of the subsidies, 85%, go to the old sectors. So when we say that, you know, China is very inefficient in the use of subsidies, actually I would say, well, when they use them for the proper sector, maybe not, because the amount is much smaller.

[00:18:34.29]

So in other words, I think we need to also kind of understand what we mean by industrial policy. What is it upgrading the key sectors? And then maybe it is much more similar to maybe government-led innovation rather than industrial policy all the way. So The question is, what are we trying to do here, at least in Europe? Is it all about new sectors? Is it also about old sectors that, you know, anyway we would lose? Think about electric vehicles, sorry to say, but we're really behind. So I would argue that understanding which are the sectors we're really trying to put the money on would make a big difference in the success of these policies beyond the labor force. I mean, the, as you were saying, Peter, whether we have enough labor force to, to deal with this. I would say that increasingly will be less of a problem because unfortunately there, there is probably less of a need of that labor force, um, to our dismay, if you think about the labor consequent, the employment consequences of AI. But I do think it's important to, to choose the right sectors, to think forward, not backward.

[00:19:50.04] - Cecilia Malmström

Yeah, yeah, sure, come in. Because of course, shall government appoint those sectors, or is this the market or the industry or companies? Very briefly.

[00:20:01.10] - Sean Doherty

I mean, if I can—

[00:20:02.03] - Cecilia Malmström

Sorry.

[00:20:02.22] - Alicia García-Herrero

Sure, sure, go ahead.

[00:20:05.11] - Cecilia Malmström

Sorry, Alicia, yes.

[00:20:08.07] - Alicia García-Herrero

I was about to say that most people think it's only the government appointing the sectors, Made in China 2025 and la la la. But actually, interestingly, when you look in detail, like a program called 10,000 Little Giants, a lot comes from the companies too. So, you know, there is a retrofeeding of the sectors at the grassroots level. So it is not all decided 10 years in advance. Some of it is, but not all of it. And I think that's very important because we always think it's just the government up there figuring it out. But I don't think that's correct. So I stop here. Thank you.

[00:20:47.05] - Cecilia Malmström

Sean, you've been patient.

[00:20:48.29] - Sean Doherty

Just build on Alicia's point with two quick thoughts. One is I think governments are not in general pushing for whole-scale reindustrialization in most cases, right? They're trying to be a little bit more targeted, as Alicia said. You know, they're trying to prevent deindustrialization for sort of unfairness issues related to the environmental transition, or they're trying to industrialize in some specific vital sectors. But I think there's This raises a great question about is it possible to be that targeted or do you need a broad industrial base? So, for example, if you want to have a competitive defense sector, do you therefore need to also have an IT sector, an aerospace sector and so forth? And I think the answer to that is it's clearly not possible to have scale across all this many sectors, particularly for smaller economies. If you're part of a larger economy, Yes, maybe it's possible. The question is what is the cost of that and who pays that cost? But for smaller economies, you're going to need to partner up with allies in certain cases. And so perhaps there's a need for two separate playbooks. And the one is about, you know, where do you team up and where, where not?

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Maybe just one quick comment on your second question about whether government should be appointing the winners. Obviously, I think the general preference is for winners to emerge through some kind of competitive process. But perhaps even more important is that we ideally don't want to end up in a situation where we have unchallengeable winners for all time. So even if a winner emerges through whatever process now, is the market, does the market remain contestable over the longer term? And so that we can have some churn and competition still happening.

[00:22:31.17] - Cecilia Malmström

Peter, you heard and you looked quickly through the new industrial policies of the European Union, and without focusing on all the details in the industrial accelerator, because it will change through the legislative process with the Parliament and the member states, of course. But it is clearly very much directed as, as a protection vis-à-vis China and the US, regardless of the administration. I would say the last 20 years have complained that Europe is too naive or too relaxed vis-à-vis China. How do you see— is this something that would correspond more to the criticism that the US has voiced vis-à-vis Europe?

[00:23:11.29] - Peter S. Rashish

Yes, I think, I think it, you know, if you want to be objective and try to look at why the— why of the Industrial Accelerator Act, I think you have to be fair and say that it's based on some of the same consumptions and concerns that, that the last few administrations have had in the US. And so maybe it's taken us— taken the EU a little longer, but it certainly seems like they're catching up. I mean, as you say, there's the question of, um, or as we've been discussing, there's a question whether it's going to be, you know, the emphasis is going to be made in Europe or made with Europe. And the fact that, um, I think it's very interesting, uh, when you talk about, uh, in the transatlantic context, I think it's very interesting that at least the draft that the Commission put out would, would include free trade partners and, and countries that have signed up to the WTO government procurement agreement because To me, that almost has a little bit of a ring in an informal sense of a kind of coalition of the willing or a club on these kinds of issues, right, without actually going through the, you know, the effort and mechanics of a trade agreement.

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It's kind of a backdoor way of doing that. And, you know, I don't exaggerate it, but as I mentioned, that, you know, this administration, which of course has very distinct, uh, you know, kind of unilateral trade policies, has put some effort into creating a club for critical minerals. So it'll be very interesting to see whether what the EU is doing, you know, to see how that will change the sort of transatlantic debate about the how, you know, will this administration see this Industrial Accelerator Act as coming closer to not just to the concerns, but also to the current mechanisms the US administration is using.

[00:24:54.19] - Cecilia Malmström

You've all pointed to the risks with industrial policy, and we know from 30, 40, 50 years ago, that there are certain risks and things that we need to be aware of. And finding that balance between openness and resilience is, of course, extremely tricky. But do you agree that we have a new kind of industrial policy playbook today, or is it just a small adjustment to, to the current date as compared to— or is it something totally different? And if yes, what characterizes that? Sean, this was part a little bit of the seminars you had in Davos, right? To try to identify the— Exactly.

[00:25:40.13] - Sean Doherty

And I think maybe the kind of short answer to your question is clearly we have, you know, very complicated supply chains nowadays, but we also have more sophisticated tools for analyzing and understanding those supply chains. And so that kind of both opens up the possibility for and perhaps requires more sophisticated industrial policy in terms of responding to that. And I think that's a little bit behind what the US has been doing and, you know, really trying to look into the details of semiconductor supply chains, for example, and, you know, really make these quite, quite targeted interventions. The other thing which perhaps has changed is you go back a decade or two, probably there was a general view that open trade is almost inevitably going to lead to greater competition as you have more players can enter the market. More recently, there's perhaps a view that actually in certain sectors there is a risk of having global dominance by, you know, a couple of firms which are actually based outside of the regulated market, which is a concern for politicians. And so this thought that although there's little chance perhaps of much progress on a kind of global antitrust approaches in the near term, this has been one of the things which has been prompting some of the industrial policy actions particularly I think if we look at the kind of dynamic between the EU and the US.

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And, you know, I totally agree with what was said earlier. You know, a lot of this discussion is focused on China. But I think it's important to remember that the discussion would be still alive even if China wasn't in the picture. You know, you referred to EU fears of dependency on, on, on the US on the security front. I think the same applies a little bit in terms of EU dependency on the US on the technology front. So kind of where this all leads to is I really think it's important that discussions around kind of the way forward here really involve all players. And of course, there'll be some discussions which take place behind closed doors. But it's also very important that we don't forget to have those discussions which involve China and the EU and the US and Japan and all the players if we really want to come up with effective solutions here.

[00:27:55.24] - Cecilia Malmström

Alicia, yes.

[00:27:56.29] - Alicia García-Herrero

Yeah, I really like, Sean, what you said about these major companies dominating as, in a way, ironically, a reason for industrial policy. So in other words, you know, in the good old times in Europe, your question, Cecilia, is how far are we from where we were. We are very far because because in the good old times, our competition policy was all about defending ourselves from our own big companies. So you were a small country and, you know, you would fear that big company coming from a neighboring, um, a neighboring country, or maybe not very neighboring, but still that fear. That's not the fear now. Actually, our companies are too small, to be very frank. If you look at Fortune 500 European, you know, share of European companies coming down So if anything, it's all about other companies out there. So in a way, ironically, the idea of contestability is no longer about us. It's much more about the others. And that in a way changes radically the underlying reason why we're doing this. And therefore, maybe we use the same instruments, put it this way, but actually the end goal is very different from the past.

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In my view.

[00:29:14.26] - Peter S. Rashish

Yeah, I would say that whether it, you know, this question is it all about China, I mean, for Biden, it was clearly also about climate. And I think in a bipartisan way, I'm not sure if this is as much the case in the EU, maybe it is, but I think in a bipartisan way lately, there's also a sense that manufacturing is somehow special. You know, it's good for the cohesiveness of communities, let alone sort of, you know, in a macro sense for the US economy. And so I think that, there's this sense that we need to promote manufacturing because of some economic but also some non-economic benefits. And that has not— is indirectly tied to China, but not directly.

[00:29:54.11] - Cecilia Malmström

And how is this looked upon in China, Alicia? Have they at all reacted, or is it part of any debate, or has it just been dismissed?

[00:30:03.29] - Alicia García-Herrero

Well, it's part of the facts, I would say, because we had The work report, so basically the economic report within the two sessions which just ended, and it, except for a target that we were all fearing of China's manufacturing share of GDP, of global GDP, reaching 45%, which was kind of the target that we, that we had heard. So our 20% is peanuts compared to where China expects expects to be by 2030, except for that target, which is not on the paper, all of the, you know, all of the things needed to get there are on paper. And I think that's what we need to realize, that even if the world is not a zero-sum game, when you talk about manufacturing as a share of global GDP, it is, because it's a share of all of us.. And if China wants to be at 45— yeah, 45— I'm afraid that Europe will find it very difficult to reach that 20. That's the way it is. And therefore, um, why is China there? Because I think by now China, I think, is convinced that consumption will not lead the way, for that there will not be any rebalancing.

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And China is convinced because You know, all, all of the things you need for that rebalancing aren't there. Wages are growing below 1% for an economy that is growing 5%. I mean, the whole thing is, is really not happening as it should happen. And the only way out is to export. That's what it is. So in that regard, I think how China sees this is as a major threat as a consequence, because that's— they can't change their growth model. They are still waiting for the real estate to recover, maybe never. Consumption is not back, it will not back, it was never there and it probably won't be. So in, I think, you know, they, again, the Industrial Accelerator Act in a way is a recognition of what I just said. That absolutely, because if we knew that China were to change and this, you know, import from China would become massive and la la la maybe we wouldn't have this conversation. But I think by now there is this realization and China is not showing any sign that our realization is wrong on the country. It's doubling down.

[00:32:31.17] - Cecilia Malmström

Yes, of course, because increased exports with overproduction and so on, and that is threatening many key European industries, of course. So it is, I mean, it's a shared analysis, but maybe with different tools to address it. This is the— this is program on trade. And of course, industrial policy is very much about trade as well. But how is this affecting the rest of the world, especially in the Global South, if the rich industrial countries are focusing more and more on industrial policy, you know, trying to balance and to a certain extent close some avenues? What effects will this have for the Global South? For the rest of the world. This is something you've been looking at, Sean.

[00:33:23.07] - Sean Doherty

Yeah. So a couple of thoughts here. I mean, first, going looking at the China perspective, if you look at a micro-level kind of Chinese businesses, obviously many of them are looking to expand overseas as they look for growth. And they're very aware of, you know, what Alicia was saying earlier around the various conditionalities being imposed on investment. And so they're very keen, many of them, to try and understand, you know, what does FDI best practice look like in this environment? How can they try and ensure that they receive some kind of welcome in the economies they invest in? Clearly, you know, they're also looking particularly at economies in the Global South for that, which are, you know, seen as somewhat more welcoming for the moment. And clearly, we've seen a lot of the, you know, although from a low base, a lot of the growth in China's exports have been to Africa, ASEAN over the past year or so. I mean, the other thing I would say is I think if we're going to see cooperation on this topic in the short term, then it's more likely to come from those smaller and middle powers who, because they need to and they don't have this option of really being, you know, just fortress economies.

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And so they will be looking at what the possibilities for cooperation are. I think if there is any ability to have some kind of collaboration around some of the underlying topics around competition policy, around environmental policy, around digital policy to an extent that reduces a little bit the pressure for the more overt industrial policies. So that's what I would be looking to see.

[00:34:59.02] - Cecilia Malmström

Peter, any views on this?

[00:35:01.20] - Peter S. Rashish

Well, sort of taking a kind of trade policy perspective, I think a lot of what we're seeing in industrial policy is a result of the fact that the trading system has been disrupted a bit. And so one question in my mind is, you know, well, will this— will the fact that the industrial policies are proliferating lead, you know, to some kinds of reforms or changes in the trading system? To the extent that those changes happen in the WTO, excuse me, that's easier for— that's beneficial for smaller and poorer countries. To the extent that the changes happen in the kind of, you know, these sort of the way the Industrial Accelerator Act might suggest with sort of free trade partners of certain countries or maybe in the kind of club initiative that the US has been pushing for on critical minerals, you know, then the question is, are these countries going to be part of those clubs or part of those agreements, right? And so I think the answer is uncertain, but that would— if we're moving in this kind of direction where away from where the— if the action is a little bit less on the multilateral level and it's a little bit more what you might call the plurilateral level, then it's a question of can these countries find a way to be in, you know, part of that action.

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And so that's a challenge, you know, in terms of economic diplomacy for them, but I don't think it means it's impossible. It just means that the terrain is shifting for them.

[00:36:29.01] - Cecilia Malmström

I remember the Director-General of the WTO, Dr. Ngozi, she warned I think 2 years ago when the debate on friendshoring was very high on the agenda, that she said that it all makes a lot of sense. But remember that those who are not friends are maybe not enemies, but they're still not in the club. And they are mainly countries in the Global South. And that the WTO came up with figures that this could actually reduce global GDP with, you know, 5-6% if this is pushed through a longer term. So, so So how do we deal with that?

[00:37:06.04] - Alicia García-Herrero

Yes, maybe just a note, and it may sound a bit harsh, but there you go. It is also true that by, you know, pushing that argument, nothing changes. And let me give you the example, which is in the International Accelerator Act, this WTO government procurement agreement. So in other words, by mere status quo, not many countries are going to jump on it because why do it? So what I'm trying to say is that maybe by just trying to push a reform of the WTO, we didn't get anywhere. And the question is, can some of this legislation in a way induce countries to jump on things that they wouldn't have done otherwise?. So in a way, as long as there is, uh, for me, as long as there is a clear rule and it is achievable, I think it's, for me, it is still moderately positive for these countries. Because the problem is when it, there's no rule. I mean, I'm of course referring to, to the US in, in, and you know, in this case I think it's very different because this could actually lead other countries to join— not clubs, the club is there, it's just that you didn't sign the agreement.

[00:38:26.03]

And so for me, there is some room for improvement, possibly even of the working of the WTO, because if we continue like this, nobody will jump on anything and all of these agreements will be void of meaning. So I would say this is a plus in my view, uh, for even for those countries that are not in, there is now a reason to be in. And I think that's, that's positive.

[00:38:57.09] - Cecilia Malmström

Any views on that, Peter, Sean?

[00:39:00.06] - Sean Doherty

I would perhaps say, you know, it's important to remember that we're not starting from scratch, as you say, you know, in some ways this is not a new topic. And in history, there have been many rules here, right? Clearly within the WTO on subsidies, agricultural export subsidies, government procurement agreement, as you mentioned, the EU has its state aid rules and so on and so forth, right? Transnational subsidies regulation and so forth. The point is that the consensus around what forms good policy or bad policy has been a little bit overtaken by events over the past decade or so, as a number of these industrial policy interventions have increased. So I think where we are now is we need to have a, I think, a good, informed, open conversation around this. You know, one of the things that we're doing, we're working with the consultancy Kearney to just try and put out a little bit of, you know, it's just in the form of very simple infographics, communications to policymakers, to businesses about what actually is happening in the space of industrial policy. What are some of the instruments being used? What are some of the effects of that?

[00:39:58.15]

You know, what are some proposals for guardrails?

[00:40:04.21] - Alicia García-Herrero

Hmm.

[00:40:04.22] - Peter S. Rashish

Yeah, I would also say that You know, it does seem important to continue to focus on mapping supply chains because, you know, there may be more interdependencies than the EU or the US or other large economies are realizing when they think about industrial policies. And so having all those facts before you get too far along in your approach does seem to be important. And my guess is that if you do get a sense of, a very granular sense of the supply chains, there'll be some recognition that a number of smaller and developing countries, you know, do play important roles, at least in some sectors.

[00:40:43.20] - Cecilia Malmström

Hmm. What would be the forum for that cooperation? Because, of course, we all know, and it's very sad to note, that the WTO has had enormous difficulties lately to deliver decisions and to come forward. There are lots of explanations to this, of course, unanimity, 166 countries need to agree, and also big countries, US, China violating the rules, et cetera. So this creates sort of a vacuum of international organizations. And we see globally, I mean, the United Nations, G20, World Bank, IMF, G7, they're all weaker than they used to be as international platforms. And the US administration has withdrawn from a lot, I think 60 or 65 big international organizations as well. So there's certainly a case full cooperation. I think you mentioned, Sean, the critical minerals, for instance, where there's absolutely a case to cooperate, to identify, to see how we can reduce dependence from China, how we can do it in a cleaner way, how we can sort of maybe joint investments. There have been talks about that with some countries as well. Subsidies, another area. I remember a couple of years ago when I was Trade Commissioner, we had actually a cooperation, US, EU, and Japan, to try to rewrite a proposal for rules on subsidies in the WTO.

[00:42:06.22]

And that, that work went rather, you know, it went well and we advanced quite, quite rapidly. It never really resulted in anything concrete, but there was a draft that could have been taken forward. And a couple of last year, there was also increased cooperation between OECD, World Bank, IMF, UNCTAD, WTO to try to map and come up with some sort of principles on subsidies as well. So there's certainly a lot there, but there needs to be a forum, there needs to be an institution or some sort of basis where this cooperation can happen. And WTO is ideally the place, but it is not really, really working. How do you see that? Or shall we rely on a little club of willing and then everybody can join if they want to? So open plurilaterals, as it's called.

[00:43:00.28] - Sean Doherty

I would suggest Cecilia, we're looking to you again for leadership on this. As you said, you know, you had that collaboration with the three—

[00:43:07.12] - Cecilia Malmström

In the good old times, 10 years ago.

[00:43:09.08] - Sean Doherty

But now Peterson Institute, you know, can clearly come up with a set of principles, recommendations for us all on what does good industrial policy look like? Because I think there are a number of principles we can probably— many of us can converge around, around, you know, I mean, clear goals, timelines, measuring. You know, where we stand in regards to whatever goal it is that we're trying to achieve. What are the governance mechanisms to prevent instrumentalization? I think maybe there's a need for the pump to be primed through some kind of provocative proposal.

[00:43:45.07] - Peter S. Rashish

I mean, I like your idea of reviving the trilateral effort because then you capture, you know, the three big like-minded industrial economies. I mean, I will say, to be, I guess, realistic is the word I would use, you know, that a lot of it, these, at least for the kind of short, medium term, is going to be driven by economic security concerns. So if the U.S. and there are some overlapping economic security concerns among the U.S., Japan, and the EU. And so even though that's not going to— that'll capture a limited part of the economy, doing the kind of things you were outlining among the three of them, you know, maybe that's not just nostalgia for those days, but also maybe that trilateral does have a future.

[00:44:31.08] - Cecilia Malmström

Do you think so? I mean, there's lots of things happening. There's a lack of trust today and, you know, tariff wars and new tariffs being threatened and IEPA. And the situation is clearly different.

[00:44:46.27] - Sean Doherty

Yeah, quite.

[00:44:47.29] - Peter S. Rashish

The situation requires more compartmentalization than it did 10 years ago, that's for sure, I think, to get things done.

[00:45:01.11] - Alicia García-Herrero

Alicia? No, I think I wouldn't start with subsidies. Maybe I would put it this way, because that's going to be tough first, because I imagine given what's happening in the world today, that we'll have more subsidies rather than less subsidies on energy. And everybody will be very careful not to commit before, you know, the wave comes to you and takes you away. But I think critical raw materials, rare earths, I think that's a rather easy area of collaboration. We already had actually at Bruegel and with a couple of other think tanks, Japanese and American, a lot of discussions on, on collaboration in the run-up to Peter's point on, you know, this proposal. But I think the, the whole point here is that everything that has been discussed is, in my view, is not market-driven in the sense that what you need is a big offtake. You need shadow prices in a way that are higher than what China can offer. So in a is collaboration, but not towards what, what used to be the targets of the WTO, but actually collaboration against those, if you ask me, but for a purpose that in a way is needed.

[00:46:23.11]

Yeah, because we need more than a single, um, if not extractor, but certain refiner of rare earth. But to get there, we need to do things that are somehow not market-based. And I think that you can't do with big stuff. That's why I think rare earth is probably the easiest area where we could find that collaboration, because if you really look at the numbers, the numbers are not big. It's a huge problem, but it's not a big number. So I think it's easier to agree on an offtake, it's easier to, you know, So if we want to start somewhere on, you know, trying out our ability to collaborate, I think that's the easiest way out to try it out.

[00:47:10.17] - Cecilia Malmström

Well, it would need very little convincing because every country on earth, independent on how it's run, recognizes this increasing need and dependencies that were there. We have a question from the audience, from Alex in Brazil, who says, how to reconcile industrial policy with global value chains? Has the role of efficiency, productivity decreased? It's a good question. Who wants to give it a try?

[00:47:44.09] - Sean Doherty

Let me jump in and say something and just maybe link it to the point that Peter just raised, where he reminded us that one of the toughest nuts to crack is around economic security. And ultimately, it's kind of looking at this trade-off between efficiency and global value chains versus that economic security question. And I think economic security, you know, has many of the classic attributes of industrial policy, but perhaps with a few extra things added on, a little less transparency, you know, in that some of these government pressures are coming in the form of a whisper in a back room as opposed to something which is laid out there transparently. And this, you know, extra flavor of technological sovereignty added on. But I think the key point is that, you know, underlying we have this risk pricing problem, this trade-off between, you know, what is the cost of dependency versus the cost of this economic security. And it's all very well getting insurance, but you know, how much do you want to pay for that insurance and who bears that cost? And if ultimately the person bearing the cost is the final consumer, are we having honest political conversations in a time where there's a lot of fear about the cost of living, about adding to that through adding economic security insurance, essentially?

[00:49:01.03] - Cecilia Malmström

Anybody wants to add anything?

[00:49:03.18] - Alicia García-Herrero

Just very quickly, I think I would not really go with the idea that every industrial policy is creating inefficiencies and, you know, having cost in terms of productivity. I don't know, we could look at again that part of China which is, you know, pushing innovation. It's hard to argue that that, that's very unproductive, at least based on value-added exports, you name it. But you— we could also look at Airbus in Europe as an example of, you know, a forward-looking project for an industry that, uh, yes, there was a space, there was only the US. Still, I mean, it, it, it, it shows that if you choose, if you look forward and, you know, you're careful with not just kind of with the choice of, of the players and, and so on, in the sense that you, you don't take just the, you know, whoever was there before and you try to create new companies. And I think that's China's success, is all of these are to a large extent new companies. So this is not subsidizing all companies. 85% is about that, but I'm talking about the, the new sector. So in that regard, I think there are ways to do this in a more productive and efficient way.

[00:50:19.27]

And I think that's what needs to be, that should be the objective in essence. So, so again, it's what kind of industrial policy are we talking about here?

[00:50:30.15] - Cecilia Malmström

But we are approaching that moment now. What kind of industrial policy are we talking about? What kind of it would we ideally want to see? We know that in the past there were several mistakes made. There sort of challenges of not repeating those mistakes. You started, Sean, to list a few principles on the goals, the governance, evaluation, I think transparency as well. Usually there has to be a quite clear timeline as well now to see that we do this for a limited time so it doesn't go on forever and then we lose it. So if you were going to— if you were to decide this is the ideal industrial policy, what, what, what, what What other elements would you put into it? Peter?

[00:51:17.20] - Peter S. Rashish

Well, I'm not— I won't answer immediately the elements because, I mean, when I think about what the ideal industrial policy could look like, I have to say that I— what comes to mind mostly is this US-EU, this attempt at a US-EU global steel arrangement.

[00:51:39.27] - Alicia García-Herrero

Management.

[00:51:40.20] - Peter S. Rashish

Why do I say that? Because it was cooperative. So that would be one principle— was it cooperative? It was also open because it was, you know, it wasn't just going to be transatlantic, it could be open to other countries. Um, and it had— I mean, a detriment probably was it had two goals, which was climate and fighting back against, uh, unfairly subsidized steel and aluminum production. Um, but maybe you could simplify that and just go with the latter for the moment. So if you had— so it would be, you know, would have more focus. Now, I do know— and so I like that idea because it provides, you know, it could provide increasing certainty to operators in the market. Because I think the risk is you have this kind of industrial policy, you know, initiative over here and another one over there, maybe a couple countries do it together here and others over— and then And there's a lot of uncertainty that's produced by that. But if you can have a kind of prime mover like the US and the EU, and then others join that, that would give something to companies to look forward to and say, okay, maybe this will be the way we're going to determine things.

[00:52:53.15]

Now, of course, one element of what we call GAS over here, and you guys call GSA, I think, in Europe, was the question about WTO consistency. So without answering that question, I will say that I see there are already questions being asked about whether the Industrial Accelerator Act will be WTO consistent. So that just strikes me as an issue that's not going to go away in the future. But I like that initiative of the Biden administration, again, because it's cooperative and open.

[00:53:29.26] - Cecilia Malmström

But it didn't really bring any results.

[00:53:33.17] - Peter S. Rashish

It didn't bring any results. I, you know, we can argue about it maybe in another session about why that happened. There was also an election that came up pretty soon, you know, around the deadline.

[00:53:42.02] - Cecilia Malmström

The high steel tariffs are still there, 50%.

[00:53:44.08] - Peter S. Rashish

And the steel tariffs are still there, but that doesn't mean that in another context— context is very important— in another context that I couldn't provide a model.

[00:53:57.09] - Cecilia Malmström

Alicia, I think you already outlined a few things, but you can actually learn from China as well, especially the sort of innovative part of the Chinese industrial base.

[00:54:07.02] - Alicia García-Herrero

This, I mean, the most obvious is of course tax breaks on R&D. China uses that massively with some unintended consequences, basically that it is cheaper to file a patent than not to file it. And that means that when you look at the number of Chinese patents domestically, it's like you wouldn't take that very seriously. Yes. For the reason I just mentioned. But of course, as everything in life, I'm sure that within that mountain of patents, yeah, there have to be some good ones and we see it in the product. So, you know, I think really, um, making clear that innovative companies are going to be supported more is a very important message. Now, again, you can have tax breaks, you can have other options. One that China has pushed and that the US doesn't need, but we need desperately, Cecilia, in Europe, is the link between being innovative and showing you are, and the ability to list. So China has created a lot of stock markets just for innovative companies. Yeah, you have Centren, you you have another one onshore, you have a new one in Hong Kong only for tech. So, you know, we don't have that in Europe.

[00:55:23.14]

And I think that would be something that is much more market-based, that you can find certain rules easier. I don't know, we did have many, many years ago, more than 20, maybe 25 years ago, the Neuer Markt, if you remember, and it had this easiness to list. All of that is gone at the wrong time we need it. So linking the ability to finance yourself with some form of industrial policy for innovation would be very important for Europe.

[00:55:53.18] - Cecilia Malmström

Sean, you started this sort of listing of what a good policy would look like.

[00:56:00.00] - Sean Doherty

Well, I mean, maybe just to take it in a slightly different direction, I think maybe there is space to shift some of, you know, what we see as vertical sector-specific industrial policy, which maybe, you know, makes sense in the short term, over time to shift it towards more horizontal economic policy to address those sort of non-economic objectives we're aiming for, whether that's environmental or resiliency goals. I mean, so I think, for example, on the economic security, you know, there's things you can do in workforce development, in innovation, in education, which can be very useful to get you to those goals over time as well. I think there is space for us to do better public-private dialogue to try and better fine-tune our policies and perhaps even, you know, over the longer term as we see how individuals move between the private sector and the public sector in terms of their careers. You know, what is best practice there? What has worked well in certain economies? You know, we don't want to have a silo where these are two completely different tribes of people, but nor do we want this sort of swamp revolving door where people are jumping easily from one to the other and perhaps having undue influence.

[00:57:07.25]

I think there are things we can do at that horizontal level which can be very helpful as ultimately we're looking to try and see be how can governments play a role in creating and shaping markets and recognizing that there's some sectors, health, infrastructure, in which they've long played exactly that role of, you know, being a buyer, being an investor, and being a regulator.

[00:57:30.01] - Cecilia Malmström

Wow, thank you. That has been a really interesting conversation. I've learned a lot and a lot to think about. Let's see if policymakers all over the world listen to you as well and take your advice. But certainly we see a lot of attempts thrown out there in an attempt to find the appropriate balance, of course. And it's certainly not the last proposals we have seen with the one that came from Europe. There will be others coming as well. Peter Ashish, Sean Doherty, Alicia García Herrero, thank you so much for joining us. And to those of you who have listened, thank you for joining us as well, and wishing you a nice afternoon or morning. Goodbye.

[00:58:13.06] - Peter S. Rashish

Thank you.

[00:58:13.17] - Cecilia Malmström

Bye-bye.