The New Industrial Policy: Shifting the Prism of Economic Policy Making?

Lessons from a Transatlantic Exchange of the Progressive Economics Network

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I. Introduction
Following the signing of the US Inflation Reduction Act (IRA) in August 2022, industrial policy has become a priority for economic policy makers. The EU—which had already devised its own industrial policy agenda—has responded to the IRA with the Green Deal Industrial Plan, a package intended to upscale green technologies in the EU and strengthen Europe’s global supply chains.

The renaissance of industrial policy has been hailed by some as a new era of economic policy making, where government policy and public investment support national industry. The aim of progressive governments is to facilitate the shift to a carbon-neutral economy, strengthen economic resilience and address social inequalities. Moreover, it is a huge opportunity for countries to provide private investors with the certainty needed to transform carbon industries. But many gaps remain and urgent policy questions still need to be answered.

On the fringes of the IMF Spring Meetings 2023, Das Progressive Zentrum (DPZ), the Foundation of European Progressive Studies (FEPS) and the Friedrich-Ebert Foundation (FES) with support by the Centre for American Progress (CAP), organised a roundtable on industrial policy convening economic advisers and policy makers from the US, the EU, Mexico and the UK. This forms part of an ongoing series of events - the Progressive Economics Network - aimed at bringing together leading progressive economic thinkers and policy makers from Europe and North America to exchange best practices and develop solutions for a more progressive macroeconomic policy making.

This discussion paper builds on the discussions at the roundtable and reflects on some of the key issues around industrial policy in the U.S. and Europe. It starts with (1) an introduction to and definition of industrial policy, then (2) discusses the cross-border aspects of industrial policies and (3) discusses social justice aspects. It concludes with considerations for policy makers. As this is a discussion paper - aimed at starting debate - we hugely welcome feedback on it.

II. How is New Industrial Policy a new type of economic policy making?

Industrial policy can be defined as “any type of intervention or government policy that attempts to improve the business environment or to alter

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the structure of economic activity towards sectors, technologies, or tasks that are expected to offer better prospects for economic growth or societal welfare than would occur in the absence of such intervention" (Warwick 2013). According to this definition, arguably, industrial policy has been present in the US and Europe throughout most of the 20th century until today—though in different shapes and forms and with varying degrees of ambition. We introduce below the concept of New Industrial Policy as rising to new types of challenges and building on novel state of the art analytical approaches.

As the above suggests, industrial policy is a type of economic policy that focuses on medium to long term outcomes – seeking to shape the structure of economic activity. Crucially, the type of industrial policy pursued by the Biden Administration, next to supporting growth, has at its heart the pursuit of social objectives. In particular, the Inflation Reduction Act, the CHIPS and Science Act, and the Infrastructure Investment and Jobs Act (IIJA) are designed to support the creation of good jobs by including job quality measures and registered apprenticeships. In other words, New Industrial Policy explicitly seeks to make the economy work better for society. As such, if designed right, industrial policy is an opportunity to renew economic democracy, where citizens and parliaments contribute to setting the direction and shape of the economy.

We argue that the huge economic challenges liberal democracies are facing at this moment call for a step change in policy. The energy transition is an economic undertaking unparalleled in speed and the underlying transformative nature of existing economic structures. This requires an all-government approach for ensuring the transition happens in a rapid manner and without social disruptions. Moreover, for the first time, key supply chains are hugely concentrated in a small number of regions, with increasing geopolitical risk associated with them. Old tools (increasing competitiveness horizontally) have not been able to counteract such tendencies. So, new thinking and approaches are needed to ensure economic resilience and more predictable conditions for key challenges like the energy transition.

Below, we propose a working definition for this New Industrial Policy (NIP) thinking. We argue that it is different from the status quo of economic policy making by (1) setting new types of objectives, (2) conducting a new type of analysis and (3) delivering policy differently.

The component parts of this definition can be explained as follows:

Mission-based policy making. While governments do, of course, have a range of concrete targets associated with policy measures (e.g. Germany’s 400,000 per year homes building targets), these are often short term. What NIP can offer is medium term targets that are ‘specific yet ambitious’. This can for example include achieving a target for diversifying supply chains, decarbonising transport or, say, achieving a target level of affordable housing. The bold proposition inherent in this approach to economic policy—and of the democratic governments that set it—is that it makes promises to citizens about how the economy could look like in the future, and that it will deliver them. In addition, missions can also spur private sector investment, their long-term and clear commitment to achieving a certain outcome can aid to channel ideas, investments and other resources into solving it. Arguably, parts of climate policy are already taking the shape of a mission. But, as we argue below, current approaches are often patchy and, despite having
big ambitions, are backed up by limited analytical and institutional capacity.

**New metrics & goals:** Most governments do not explicitly have macroeconomic targets other than macroeconomic stability. In practice, tracking economic growth, unemployment and inflation is the bedrock of macroeconomic policy debate. While these still remain critical for assessing the wellbeing of the economy, a narrow focus on them ignores other crucial aspects of economic prosperity such as high-quality jobs, social cohesion and the geographical distribution of economic activity.

What NIP seeks to do is to break some of these social goals down into quantifiable targets and to measure progress against them. Moreover, as the semiconductor shortage and associated inflation following the pandemic showed, monitoring supply chain vulnerabilities in order to ensure price stability arguably should play an important role even for ‘standard’ macro policy debates about growth and inflation.

**New objects of analysis:** As a result, NIP focusses not just on key macroeconomic indicators, such as growth and inflation, but also on ‘meso-level indicators’. These are concepts that lie between micro and macro analysis, such as supply chains (see chart below). This could be analysing the evolution of entire supply chains (such as the IEA’s Energy Technology Perspectives 2023 report), domestic production systems such as industrial clusters, supply chains or other cross-sectoral input output linkages.

**New analysis of economic processes:** In order to analyse these meso-level entities, new types of analysis are needed. (1) To understand production systems and supply chains, careful analysis is needed that explores the *complementarities* between sectors and technologies. (2) Data driven analysis of how systems work will have to replace high level economic principles. (3) Consistent definitions will have to be developed in order to ensure comparability and analytical rigour. (4) All of these then have to feed into scenarios that explore under what policy constellations the objectives set through industrial strategy are achieved.

**An all-government-approach to policy:** Many of the tools used in the NIP - such as in the IRA – are not new. Subsidies and other incentives are already being deployed widely. What is new is the way in which they are deployed. IRA-type policies are implemented to achieve medium-term missions through a range of government departments. For example, the CHIPS Act includes the CHIPS Program Office, which has the capacity and authority to help coordinate centrally between the various
government agencies involved to ensure delivery. The IRA (which lacks a centralised coordination aspect) was devised based on the bottom-up work from various ministries, such as the Department of Energy in cooperation with the Treasury. Moreover, the IRA conditionalities (such as on work standards and diversity criteria) are of cross-cutting relevance but are again ultimately implemented by the Treasury. An all-government approach also requires multiple departments working in the same direction through a range of policy tools (Tucker et al. 2023). This is needed to set in motion feedback loops between research and innovation, in combination with a certain degree of demand stability for new technologies (Mazzucato 2018). In a similar vein, the International Energy Agency (2023) refers to an all-government approach as a ‘mixture of technology-push’ policies and ‘demand pull’ policies.

Subsidies are already deployed in the EU to encourage for example home insulation and innovation in certain sectors. But this often falls short of the all-government approach described above, and often there is not enough investment into new analytical approaches, such as data-driven systems analysis. And NIP is not yet used in other policy areas beyond climate – such as supply chain resilience or industry diversification.

III. How can progressive industrial strategies deliver global synergies?

There is a huge degree of market concentration of supply chains, for instance in clean industries. This is true across the value chain, starting with mining, up to technology manufacturing (see Illustration III). It has prompted the US and EU to emphasise diversification of supply chains and ‘homeshoring’.

But there is a risk that nationally focussed industrial strategies fail to generate the benefits that deep global cooperation can achieve (e.g. between the US and the EU). Merely ‘matching’ each other’s strategies might miss benefits from
complementarities in supply chains. Moreover, there are serious and justified concerns by many countries in the Global South that industrial strategies could leave them at a significant disadvantage.

The current state of the debate and key questions for policy:

The IRA debate has already brought this issue to the fore in US-EU relations, but other countries have also started paying particular attention to it, South Korea for instance. Here the main concern lies with clean tech in general and electric vehicle and battery production in particular (Jansen et al. 2023). With regards to the clause that requires supply chains to be in the US (or other countries that the US has a trade agreement with). A US white paper suggests negotiating an agreement that would allow European companies to access at least a share of IRA subsidies. Yet, some of the issues around this will likely remain. The IRA foresees that at least half of the electric car’s battery components need to be manufactured or assembled in North America in order to qualify for subsidies. This will increase to 100 percent by 2029.

This requirement would not be affected by the above discussed partnership. Moreover, countries from the Global South have criticised such an approach of predominantly rich countries negotiating individual exceptions.

A possible trajectory in the next few years is that various countries implement industrial policies to support national industries. But go-it-alone strategies might create inefficiencies and have to forego possibly significant synergies that can stem from global cooperation. Industrial strategies challenge parts of the prevailing WTO paradigm, except that they should still be deployed with the benefits of global trade and cooperation in mind. For instance, it might create inefficiencies if every economic block created its own wind and solar industry. To avoid inefficient industrial development, the best solution would be to start with a global analysis of supply chains and

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2 Jansen et al. (2023) estimate that even with an agreement in place, the EU will have to spend about €264 billion over the next decade to match US production subsidies.
There is currently no institution that is conducting such an analysis. The IEA is partly filling the gap, but more diversity of analytical approaches is direly needed. Currently, both on an EU level and in the US, there is limited analytical capacity to analyse supply chains, develop scenarios and assess comparative advantages in different countries.

The second, and perhaps more likely approach is that individual industrial strategies are devised and then complemented through some trade policies. This is already starting to happen, through bilateral trade deals. For example, the US just agreed to a deal with Japan, similar to the EU one mentioned above, through which Japan could access some of the IRA subsidies. There are also proposed sector specific global deals, such as, for example, the Global Arrangement on Sustainable Steel and Aluminium (GASSA), initially proposed by the US. This envisions setting import limits on high-carbon steel and include technology transfer and other bespoke collaborations. But, also here, they seem incomplete unless some global analysis is developed first, which could inform some principles for how such arrangements should be developed. There have also been tensions with regard to, for example, what WTO compliance should mean in the context of selective cross-border collaborations.

Thirdly, there is an urgent need to put more emphasis on the Global South in industrial strategy development, including resource rich countries. Not considering the need to foster development in these countries would be a critical omission. Moreover, there is a geopolitical aspect to this—and the question of whether the Global South becomes incorporated into the orbit of liberal democracies or that of authoritarian countries. Making industrial policies work for the Global South will mean (1) fair conditions for access to raw materials and (2) helping them develop some upstream industries for raw material processing themselves. One idea could be to provide more comprehensive partnership agreements that include the development of raw material contracts (between governments or between governments and the private sector) to set up processing facilities accompanied by capacity building for workers and the public sector. This could also be an important area to involve International Financial Institutions such as the IMF and international development banks. Such an approach, aimed at fostering industrial development in the Global South, would help counter recent complaints on their behalf that the West is providing “only lectures” instead of concrete economic benefits. Such an approach could build on the lessons learned from recently established Just Energy Transition Partnerships.

IV. How can we hardwire social justice into the design of industrial strategies?

As wide-ranging frameworks for industrial policy are being developed, it is important to ask how social justice can be hardwired into their design. Key questions in this area include:

What are best practices for conditionalities of subsidies? This refers to making subsidies not just conditional on a company performing a certain activity, but also on achieving wider societal goals, such as ensuring decent jobs and training opportunities are provided. One suggestion for Europe is to link conditionalities around working conditions to the institution of labour unions, which play a much bigger role in wage setting than in the US (Krebs 2023). There is of course a question regarding how much enforcement of social standards should be achieved

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3 Ongoing analysis of this kind would also shed light on sectors and technologies not yet covered by existing initiatives. For example, it has been argued that intermediate goods and their supply chains should receive more policy attention.
through industrial policy rather than through regulations. Nonetheless, if subsidies become a more important part of the policy toolkit, further analysis is definitely needed on how carrot (subsidies) and stick (regulation) policies can be optimally combined.

What can be done so that industrial policy does not exacerbate regional inequalities—including for instance between EU member states? The three main bills of US industrial policy passed recently all included some provision to ensure that economic activity is spread regionally. But further research is needed to understand what kind of provisions are most effective. Moreover, as the EU is developing its industrial strategy response to the IRA, more work is needed to project what the likely impact could be on industrial development. Governmental resources—financial, administrative and planning—are unequally distributed in the EU. The NGEU fund could in the short term address the financial aspect, and the proposed Sovereignty Fund could ensure continuation of centralised funding in the medium term. But administrative differences could still mean that even if a joint strategy is deployed, actual policy deployment might still be very unequal. This is already partly borne out with current pandemic era investment programmes: several countries do not have the sufficient resources to develop projects in which to invest available funds. So a Europe-wide strategy would require ensuring that delivery capabilities are developed in tandem.

How should they link to skills policies to ensure good jobs are widely shared? When developing industrial policies, it is important to include the availability of skilled labour as a crucial factor. As current labour market tightness in some sectors demonstrates, this can be a binding constraint. Therefore, given industrial policies are built on medium-term scenarios for industrial and economic development, there is an argument for mirroring a similar strategy with regards to training and education. Some of this is already being put into practice. For example, the CHIPS and Science Act provides $13.2 billion to fund apprenticeships and workforce training programs for skilled workers in advanced manufacturing and research and development, with the aim of building a competent workforce in the critical semiconductor sector. But more scenario analysis is needed on how training programmes could better be synched with industrial strategy plans.

IV. Next steps - Areas for policy makers to consider

- **Build analytical capacity.** Consider how new international institutions can be built or existing ones equipped—to conduct meso-level analysis of key industrial strategy questions. More widely foster research and dialogue around all the building blocks of NIP.
- **Conduct analysis on sectoral and technology gaps** in current policy frameworks.
- **Ensure analysis of national comparative advantages** is developed to inform industrial strategy development and to consider how trade deals can be aligned with industrial strategy.
- **Develop fair industrial strategy agreements with countries in the Global South** that ensure that some local refining and manufacturing capacity can be developed to foster development.
- **Build stronger conditionalities** into the EU industrial strategy approach, including linking incentives to good jobs criteria.
- **Conduct scenario analysis of how industrial strategy affects regional inequality, under a range of policy scenarios.**
Bibliography


About the Author

Carsten Jung is a Senior economic advisor at Das Progressive Zentrum. He is also senior economist at the UK's Institute for Public Policy Research (IPPR), where he leads the work on macroeconomics and structural economic reform. He is also a lecturer in economics at University of Bayreuth in Germany. Before joining IPPR, Carsten worked for six years at the Bank of England. There he first worked on international macroeconomics and financial regulation, then led their work on financial risks from climate change. Carsten went on to lead the Bank's work on regulating artificial intelligence.

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Its thematic priorities are situated within the four programmes Resilient Democracy, Green New Deal, The Modern State and Political Strategy, with a particular focus on European integration and the transatlantic partnership. The organisation is based in Berlin and also operates in many European countries as well as in the United States.

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This discussion paper was developed in cooperation with

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