Mises Wire

Industrial Policy Is Back—and It's a Gigantic Mistake

Tags: Big Government, Cronyism and Corporatism, Politics, Taxes and Spending

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Since the financial crisis, policymakers in Western economies have turned increasingly toward large-scale industrial policies. So-called mission-oriented policies are launched as a response to many perceived problems, notably climate change and the recent urge among Western countries to reduce their dependence on China.

This renaissance of state capitalism implemented in many Western countries today, which are expressed in large-scale government programs, need to be scrutinized in a broader macroeconomic and ideological context. We do so in our new book *Moonshots and the New Industrial Policy: Questioning the Mission Economy*, published by Springer and available for free download. In total, twenty-three researchers from different parts of the world contribute with theoretical approaches and in-depth descriptions of industrial policy dilemmas.

Our common conclusion is that the resurrection of large-scale industrial policy is a major historical mistake.

During the 1990s, a broad consensus developed that the role of policy was to design well-balanced, generally effective framework conditions for business. These conditions should, as far as possible, create conditions that were independent of company size, age, sector, financing structure, form of ownership, and ownership category. The creation of the European Union internal market and the opening up of previously monopolized sectors to competition increased the pressure for change and stimulated economic development.

These economic policies were to a large extent a reaction to the disastrous industrial policies of the 1970s. Entire industries had been kept alive by extensive direct and indirect subsidies for decades. Necessary reforms had been postponed via devaluations of currencies, tariffs, and subsidies. The lesson was learned: top-down industrial policy prevents structural change, benefits special interests, and fosters stagnation.

Three decades later, these lessons seem forgotten. The 2008–9 financial crisis, the protracted euro crisis of 2009–12, and the pandemic brought back active, interventionist industrial policy back to the fore.

This renaissance is skillfully promoted under slogans such as "mission-oriented innovation policy" and "the entrepreneurial state," touted by celebrity economists such as Italian-British Mariana Mazzucato and Harvard professor Dani Rodrik. They are regularly invited to Davos and similar events to give legitimacy to the large-scale initiatives of those in power.

These academics argue that in the same way that the moon landing program boosted United States economic development, similar "moonshots" should be initiated in other areas, mobilizing private and public actors toward common goals such as eradicating homelessness or curing cancer.

In our book, researchers identify several reasons why this ostensibly appealing policy is in fact problematic. The list of grandiose moonshot projects that have failed is long. A few examples: the US war on homelessness and the home ownership program (which was a factor in the financial crisis), Brazil's attempt to rebuild its shipbuilding industry, the Swedish "million program" to boost housing supply, the attempt by the US to use aid to build up developing countries, and Richard Nixon's "war on cancer."

We identify seven reasons why these missions generally do not work well in practice:

1. Missions cannot solve "wicked" (i.e., highly complex) problems.
2. Politicians and government agencies are not exempt from self-interest.
3. Decision-makers lack sufficient information to design missions appropriately.
4. Missions are subject to rent seeking and mission capture.
5. Missions distort competition.
6. Government support distorts incentives and creates moral hazard.
7. Opportunity costs are ignored.

These seven factors permeate the industrial policy failures analyzed in our book. They are also applicable to the megainvestments and so-called green deals now rolled out around the world, which are often unprecedented in industrial history.

A market economy is based on a decentralized process with room for experimentation, evaluation, and selection. Companies and individuals interact spontaneously and test the economic viability of different solutions. The main task of policy should be to create the rules of the game that give relevant actors proper incentive to find cost-efficient and appropriate solutions to society's major challenges.

The return of industrial policy means a renaissance of the symbiosis between the state and capital owners. Both economic theory and historical experience show that this is a mistake. The sooner we recognize this and make a U-turn, the less costly and painful the recovery will be.