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World Institute for Development  
Economics Research

Working Paper No. 2011/41

## Can Industrial Policy Work under Neopatrimonial Rule?

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August 2011

### Abstract

Technological latecomer countries face a dilemma, they need to pursue pro-active industrial policies to compensate for manifold disadvantages vis-à-vis established competitors, but at the same time, due to neopatrimonial politics and capacity constraints, their institutions are rarely in a position to correct market failure effectively. Do the risks of misallocation outweigh the benefits and should these countries abstain from industrial policies? Country studies show that selective industry support is indeed frequently used as a source of patronage and clientelism, and implementation is often ineffective. Two of the surveyed countries—Tunisia and Ethiopia—with neopatrimonial traits nevertheless pursue ambitious agendas of industrial modernization and implement them fairly effectively. Scarcity of fossil energy and mineral resources, the need to build legitimacy on increasing social welfare, and committed leadership distinguish them from worse performers.

JEL classification: L52, O14

Keywords: industrial policy, political economy, neopatrimonialism, developing country, Tunisia, Ethiopia

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This study has been prepared within a joint project of UNU-MERIT, UNU-WIDER, and UNIDO on Pathways to Industrialization in the 21st Century: New Challenges and Emerging Paradigms.

UNU-WIDER gratefully acknowledges the financial contributions to the project by the Finnish Ministry for Foreign Affairs, and the financial contributions to the research programme by the governments of Denmark (Royal Ministry of Foreign Affairs), Finland (Finnish Ministry for Foreign Affairs), Sweden (Swedish International Development Cooperation Agency—Sida) and the United Kingdom (Department for International Development—DFID).

ISSN 1798-7237      ISBN 978-92-9230-406-5

## Acknowledgement

The author would like to thank Steffen Erdle. The section on Tunisia is summarized from Erdle (2011).

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## 1 Introduction

Technological latecomer countries suffer from more pervasive market failure than early industrialized countries. Their business environments lack most of the cluster synergies that more advanced locations offer. Sectorally targeted industrial policies are needed to overcome these disadvantages and create the preconditions for economic diversification and technological development. Industrial policies, however, affect the productivity of economic activities and thus create rents and, consequently, incentives for political capture. The development challenge is to manage rent creation in a way that maximizes public welfare and keeps political capture to the minimum. Yet, this is difficult when the ruling elites employ patronage and political clientelism systematically to create and preserve their legitimacy. This is the core of neopatrimonialism, a common characteristic of most developing countries. Industrial policies in particular can easily be employed to gain political support from specific constituencies, given that the criteria for establishing which activities merit protection and subsidies, and which ones do not, can be interpreted creatively.

Hence, latecomer countries face a dilemma. They need industrial policies more urgently than mature economies do, but they are also the most likely candidates for political capture. This section explores the practical implications of this problem. Do the risks of misallocation outweigh the benefits of correcting market failure? Should these countries confine their economic policies to sector-neutral measures for improving their investment climates, or can industrial policy work under neopatrimonial rule?

The first section carves out why technological latecomer countries suffer from more pervasive market failure than early industrialized countries, and which particular problems call for industrial policy solutions. It argues that, even when industrial policies are needed, governments may have insufficient capabilities and inappropriate incentives for implementing them efficiently. Neopatrimonialism is then introduced as a concept to explain the behaviour of interest groups in industrial development. We argue that neopatrimonialism greatly enhances the risks of political capture, but we also highlight the fact that some countries with strong neopatrimonial traits have made extraordinary economic progress. Section 2 provides empirical evidence of industrial policy-making in four Sub-Saharan African (SSA) and three countries in the Middle-East and North Africa (MENA) region. It shows that neopatrimonialism is indeed pervasive in these countries and affects the way industrial policies are designed and implemented. Overall, industrial policy effectiveness is fairly weak, although some programmes succeeded in developing new activities. Ethiopia and Tunisia stand out for pursuing long-term strategies of industrial transformation and implementing them fairly effectively, and are therefore described in greater detail. The concluding third section then draws general conclusions about industrial policy under neopatrimonial rule and discusses why the policy performance varies so significantly among the countries.

## 2 Theoretical considerations: industrial policy, latecomer development, and neopatrimonialism

### 2.1 The case for industrial policy in latecomer countries

Developing countries are latecomers to industrial development and other forms of knowledge-based production. In a globalizing world, their economies have to compete with others that initiated their industrial development decades or even centuries earlier. Catching up with the frontrunners becomes more and more difficult, because products and processes turn out to be increasingly complex and dependent on complementary assets provided by other companies and institutions. Early industrializing countries have been able to create many of these assets through a cumulative process of business specialization and sophistication of supporting institutions. Their firms can thus build on a range of network externalities that give them a substantial competitive edge over isolated newcomers in other locations. This makes it very difficult for the latter to compete in any kind of tradable goods—not only in export markets, but also at home, given that international investors and traders are penetrating their domestic markets. Referring to Africa, Collier and Venables (2007: 1) illustrate the disadvantages of latecomer development in the following way:

Africa has lagged behind partly because its economic reforms lagged those of Asia. When export diversification started to boom in Asia in the 1980s, no mainland African country provided a comparable investment climate. Now a number of African cities ... offer reasonable investment climates, but they cannot compete with Asian cities that have comparable investment climates since the Asian cities have established clusters of firms in the new export sectors. Such clusters provide firms in the cluster with the advantages of shared knowledge, availability of specialist inputs and a developing pool of experienced labour. ...Until African cities can establish such clusters, firms located in Africa face costs that will be above those of Asian competitors, but because costs are currently higher individual firms have no incentive to relocate.

The larger the gap vis-à-vis more advanced countries, the more difficult it is to build competitive industries. Of course, poor countries may build on comparative advantages in natural resource endowments and/or low wages, but industrial upgrading towards more productive and profitable activities is not easy. In low-cost manufacturing it is difficult to compete against China and other established (mainly Asian) export locations that benefit from economies of scale and network synergies *cum* low wages, and growth paths built on exports of natural resources imply a range of well documented economic and political challenges.<sup>1</sup> Latecomers thus face a number of competitive disadvantages which can hardly be overcome without pro-active government action. Low-income countries in particular suffer from severe market failure, as the following three examples illustrate:

First, **coordination failure** is far more frequent than it is in mature economies. Coordination failure occurs when market actors refrain from investing because activities are interdependent. Any new branch requires simultaneous investments in

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<sup>1</sup> See the 'resource curse' literature, e.g. Auty (2001) and Mehlum, Moene, and Torvik (2006).

complementary activities to become viable, so that no investor dares taking the first step unless they can be sure that others will provide the interrelated assets. This, of course, is a very common situation at the beginning of a country's industrial development. The quote from Collier and Venables illustrates the problem. Thus latecomers need a coordinated 'big push'—e.g. simultaneously attracting and/or nurturing providers of key inputs and investing in infrastructure, skills, and technological services—if they want to establish cluster synergies in order to make up for the advantage of established competitors.

Second, there is typically a **lack of opportunity entrepreneurship**. While Naudé (2011) suggests that poor countries may have as many citizens with the necessary personal traits for entrepreneurship as any other country, the institutional set-up of pre-capitalist societies typically discourages entrepreneurial behaviour in a number of ways. This holds for social norms as much as for economic incentives. Social norms, as reflected inter alia in school curricula, may not be supportive of curiosity, creativity, and search. Some societies do not promote the pursuit of personal achievements, e.g. they have built-in social norms that oblige those who have earned an extraordinary income to share it with their community, thereby discouraging the search for business ideas and constraining capital accumulation. Also, the weakness of institutions providing risk assurance leads to risk-averse attitudes. Last but not least, would-be entrepreneurs in poor countries live in an information-scarce environment where managerial role models, sophisticated customers, and new business ideas are in short supply.

Thus governments have an important role in nurturing entrepreneurship. They need to foster a societal consensus on the desirability of entrepreneurship for the society at large, to create a cultural and business environment that encourages risk-taking behaviour and fosters an 'achievement culture', and to facilitate training of entrepreneurial and managerial skills. Moreover, they need to create a learning environment that balances protection and competitive challenge, on the one hand, the nascent entrepreneurial class needs a certain degree of protection to avoid that imports and direct investments from more advanced economies asphyxiate the emerging companies, on the other hand, competition needs to augment gradually to ensure that national enterprises continuously improve their performance.

Even in mature capitalist societies with advanced entrepreneurial and managerial skills, there is a case for subsidizing the search for new business options, because the social value of discovering new products or processes can be far greater than the return on investment for the innovator. Developing a new business idea is costly and involves the risk of failure. When the idea materializes, however, competitors may quickly copy it. While this may offer enormous advantages to the local economy, the copycats dissipate the rents that the risk-taking innovator could have obtained from his innovation. Due to this non-appropriability, innovative business models are typically undersupplied. This calls for government programmes to stimulate the discovery of new business opportunities (Hausmann and Rodrik 2003).

Third, the **enterprise structure** of latecomer countries is typically **fragmented**. In well-functioning market economies, companies that bring a superior product or process to the market obligate their competitors either to make comparable improvements or to exit the market. This process of 'creative destruction' (Schumpeter 1942) homogenizes factor productivity across all surviving companies. In developing countries, however, it does not work well. Here, the initial productivity gap between modern enterprises (e.g.

foreign corporations) and traditional cottage industries is so huge that the latter cannot simply emulate the sophisticated business models of the former. At the same time, the latter employ the bulk of the workforce (OECD 2009), and it is impossible for the more efficient firms to absorb additional workers at the same rate at which inefficient firms disappear (unless GDP grows at very high rates over several decades). As a consequence, owners and workers of these firms typically retain their economic activities even at minimal levels of productivity. Contrary to Schumpeter's assumption, the productivity of newly established firms does not exceed that of exiting firms (Tybout 2000). As a result, a large, mostly unregistered, survivalist economy persists alongside modern firms, and the productivity spread is much greater than it is in mature market economies. Moreover, due to low productivity, low quality, and lack of proper registration, modern, scale-intensive and registered firms only rarely engage in business transactions with small informal enterprises. Governments have an important role in narrowing the productivity gap and reducing fragmentation. This implies helping micro and small enterprises to increase their productivity, linking them to clusters and value chains, and improving the employability of those engaged in survivalist activities.

## **2.2 The necessary capabilities for successful industrial policy-making**

In sum, neoclassical standard assumptions about the allocative efficiency of markets apply much less to low-income countries than they do to rich countries with their more sophisticated institutions. It is therefore hard to imagine a catching up process without a pro-active government that helps to manage structural change, supporting diversification, and the development of new activities that promise to generate more and better paid jobs and other social benefits. This is what industrial policy is about. For the purpose of this section, we define industrial policy as any government measure, or set of measures, to shape structural change in ways that the government views as desirable. This implies selectivity, i.e. certain economic activities are favoured over others that are regarded less promising for national development.

Neoclassical theorists criticize such selectivity for distorting the allocative efficiency of markets. Bureaucrats, they argue, should not 'pick winners'. In practice, however, all governments provide differential support in favour of particular new technologies, regions or sectors. More interventionist governments even support selected groups of firms at the micro-level, which greatly increases the risks of collusive behaviour.

In any case, making the right policy choices is not an easy task, and implementing policies in ways that help to overcome market failures rather than creating new costs of doing business is equally demanding. For the following analysis we distinguish two key capabilities that the political leadership needs to have to shape structural change in a welfare-enhancing way.

First, policy makers need *strategic capability* to develop a 'national project' of productive transformation that is viable and widely accepted and supported by the society. Such a 'project' includes strategic choices about investment priorities, which in turn implies value-based judgements, e.g. how much external pressure is acceptable, whether growth takes precedence over distribution, and who deserves protection for how much time. Furthermore, it presupposes a good understanding of the changing requirements of the global economy, the ability to observe industrial developments at

home and abroad in order to identify ‘latent’ comparative advantages,<sup>2</sup> and to translate the observed phenomena into a strategy of incremental socio-economic transformation. It further requires the ability to create a social contract in support of this strategy. Where external actors play key roles, such as large foreign investors or donor agencies, it is important to align them with the strategy. Ohno (2009) has highlighted how important the ability to define a clear policy vision and strategy has been in the industrialization of Asian countries.

Second, policy makers must be able to set up service agencies and devise incentive schemes and verifiable performance measurement systems for them to ensure effective and customer-oriented implementation of regulatory and supporting services. Meritocratic recruitment and promotion systems are key to improving such *implementing capability*. Furthermore, ‘embedded autonomy’ (Evans 1995) is needed, i.e. policy makers need to interact closely with the private sector to gain a thorough understanding of business opportunities and constraints and identify market failure, but they must also have the autonomy to withdraw or reallocate rents before they become unproductive—often against the resistance of incumbents.

### **2.3 The risks of industrial policy**

Industrial policy increases the profitability of some activities and reduces the profitability of others. This necessarily involves risks of government failure. Such failure may come from two sources: *inability* and/or *intentional political capture* of rents.

With regard to *inability*, critics of industrial policy frequently claim that governments are unlikely to identify promising future investments that market actors do not recognize (Pack and Saggi 2006). This critique is plausible as far as immediate business opportunities are concerned. Governments should therefore not intervene in micro-level investment decisions. They may, however, have a facilitating role in organizing sector groups, pulling information together, and initiating participatory search processes to identify market failures that hamper the long-term development of a particular activity. Moreover, they may advocate public interests, such as the quest for socially inclusive and environmentally sustainable patterns of production. As regards the implementation of policies, reviews have shown that the services that state agencies are expected to deliver to the private sector are often quite inefficient, mainly because their incentive systems do not stimulate them to operate in a business-like and customer-oriented manner (Committee of Donor Agencies 2001). The challenge would thus be to reform the incentive systems for these agencies, e.g. allowing for more competition among service providers, privatizing certain services, or introducing results-based management.

The issue of incentives takes us to the next point: the existence of political interests and power relations, and the related risk of *intentional political capture* of rents. As Chang (1996) observed, it would be naïve to assume that governments always and only try to maximize public welfare. Three interest groups typically try to make use of industrial policies for their own interests:

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<sup>2</sup> The term is borrowed from (Lin and Monga 2010). It refers to advantages that are principally in line with the existing factor endowments but have not yet been fully exploited by market actors due to existing information, coordination or externality problems.

- *Beneficiaries in the private sector* are interested in influencing rules and regulations in such a way that economic rents are increased, for example via subsidies, restriction of market entry for competitors, and decreasing contributions to the society (taxes, severance payments, etc.);
- *Politicians* may use industrial policies as an instrument of patronage in order to enhance their legitimacy and win elections;
- *State agencies* are interested in maximizing their budgets, hiring more employees, and paying them higher salaries. Hence they have an incentive to implement programmes, regardless of their efficiency.

Industrial policy effectiveness is thus not primarily a technical issue that can be solved with education and training of stakeholders; the main challenge is political, namely how to create and withdraw economic rents with a view to technological capacity building and productivity enhancement. These mechanisms can easily be captured by interest groups, unless a strong system of checks and balances is in place.

#### **2.4 When political systems build on political capture: neopatrimonialism**

Both problems—the inability to design and implement appropriate policies as well as political capture—can be expected to be particularly serious in poor countries. Those countries’ *ability* is more limited, *ceteris paribus*, due to resource constraints. Therefore, subsidies tend to be modest, agencies understaffed, and the outreach of programmes low. The fact that public pay scales are usually not competitive implies that the best trained personnel often prefer to work for private companies or international (donor) organizations.

There are also good reasons to assume that *political capture* occurs more frequently in developing countries, because these typically lack many of the checks and balances that hold politicians and executive organs accountable in mature democracies—including electoral competition, an independent judiciary, an autonomous central auditing authority, critical feedback from independent media, as well as monitoring and evaluation routines, e.g. 80 per cent of all low- and lower middle-income countries rank below the median on the topic of ‘judicial independence’ (Kaufmann, Kraay, and Mastruzzi 2008). Public officials thus have more discretionary power. The combination of low salaries in the public sector—officials usually depend on additional sources of income—and considerable discretionary power stimulates favouritism and bribery. Governance indicators in fact confirm that these phenomena are especially pervasive in low- and lower middle-income countries. According to the same source, 71 per cent of these countries rank in the bottom half regarding ‘favouritism in decisions of government officials’. The Corruption Perception Index (Transparency International 2008)<sup>3</sup> ranks 82 per cent in the bottom half with regard to ‘control of corruption’.

To gain a better understanding of the way policies are designed and implemented in developing countries, we refer to the concept of ‘neopatrimonialism’. The last decades

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<sup>3</sup> Available at: <http://www.infoplease.com/world/statistics/2008-transparency-international-corruption-perceptions.html>



have witnessed remarkable transitions from non-democratic to democratic regimes and from centrally planned to market economies. This has occurred in all developing regions. In most cases, however, the new political and economic institutions did not fully replace those that existed before the transition. Instead, 'hybrid regimes' (Diamond 2002) emerged, in which the state is often formally shaped after the principles of modern statehood, but permeated to a high degree by informal institutions that are based on arbitrary decision-making or at least non-codified and non-actionable rules. Over the last twenty years, many attempts have been made to analyse and classify these hybrid regime types.<sup>4</sup> While the authors mostly agree on the increasing relevance of such hybrids between modern rule-based democracies and traditional political systems, no consensus has been reached in terms of terminology and classification. Instead, new concepts have proliferated, such as 'partial' (Epstein et al. 2006), 'illiberal' (Zakaria 2003) or 'defective democracies' (Croissant and Merkel 2004).

For the purpose of this section, the concept of neopatrimonialism captures the most important elements that help to explain the phenomenon of political capture in industrial policy-making. While some authors conceptualize neopatrimonialism as a subcategory of hybrid regimes (and thus distinct from democratic and authoritarian regimes), this section follows Erdmann and Engel (2006) who identify *elements of neopatrimonial rule* in different regime types, including 'illiberal' democracies and authoritarian regimes.

The following characterization integrates the main characteristics of neopatrimonialism identified in the work of Bratton and van de Walle (1997) and Erdmann and Engel (2006). According to them, neopatrimonialism is a mixture of two systems: (1) a *patrimonial* system of personal relations, where the private and the public realm are not separated, with the effect that 'obedience is owed not to enacted rules but to the person who occupies a position of authority or tradition or who has been chosen for it by the traditional master' (Weber 1978: 227, cited in Erdmann and Engel 2006: 8), and (2) a *legal-rational* system that clearly separates these realms and consistently applies codified and actionable rules. Building on Weber (1978), legal-rational bureaucratic rule is characterized, among others, by the following elements: officials are hired and promoted according to proven technical qualifications; they receive a fixed salary according to their rank in the hierarchy; promotion is dependent on the judgement of superiors; each office has a clearly defined sphere of competence; the office is the only or primary occupation of the employee and they are controlled in the conduct of their office. In neopatrimonial systems, such norms may *formally* also be valid, but their *social practice* is often personalized and informal.

The following elements characterize neopatrimonialism:

1. *Presidentialism with strong concentration of power*, whereby the ruler and inner circles of power partly exercise power in a privatized and discretionary way. Decision-making is thus frequently not based on laws and regulations, and only *few institutional checks and balances* exist to hold decision makers accountable. The president is a 'strongman' and the 'centrifugal force around which all else revolves' (Sandbrook 1986: 323).

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<sup>4</sup> See e.g. Croissant and Merkel (2004).

2. *Political clientelism and patronage.* *Clientelism* refers to the award of personal favours, such as public employment, personal promotion or preferential treatment in the bureaucracy, in exchange for votes or other forms of loyalty. Rulers appoint members of the political elite to hold key positions in the bureaucracy and the state economy. These in turn assign positions or give other favours to their personal clients and so on, thus creating a cascading system of patron-client relationships that ensures loyalty with the political elite. While clientelism refers to personalized relations, *patronage* means the strategic use of state resources to win the electoral and other political support from larger, anonymous societal groups, but also to enhance political cohesion among regions, social and/or ethnic groups.

The concept of neopatrimonialism suggests that two different spheres of government—politicians and the state bureaucracy—may employ state resources to buy political support. Even though both are part of an encompassing system of patron-client relationships, they may pursue different, even contrarian, aims. For example, politicians may have an interest in making services for the general public cheaper and better, whereas bureaucracies may prefer to maximize their budgets and focus support on their personal clients.

Industrial policy plays an important role in stabilizing neopatrimonialism as it creates political space for politicians and bureaucrats to allocate government resources to specific groups of beneficiaries. These can be employed to strengthen ties of loyalty between individual politicians or bureaucrats and private beneficiaries, but also to buy political support from specific social and ethnic groups that are considered important for the survival of the incumbent regime. As we have argued in the previous section, governments of industrial latecomer countries need to create, protect and nurture a national entrepreneurial class. This implies the creation of rents for a selected social group. If governments derive their legitimacy systematically from patronage and clientelism, it greatly increases the risk that rents are created for political supporters rather than to maximize welfare. This risk is further aggravated as policy choices among sub-sectors and technologies build on assumptions about dynamic scale economies and future knowledge spillovers that are necessarily subjective and debatable. Consequently, politicians and bureaucrats who want to employ industrial policy for patronage and clientelism can easily find technical justifications to mask their political objectives.

For these reasons, many researchers and practitioners doubt that industrial policies can work under neopatrimonial rule. Proponents of public choice theory especially deny this, as they assume that the relevant stakeholders—governments, bureaucrats, business people—act as simply self-interested individuals who create rents for their own material interests or to increase their legitimacy and political power. Hence, the public sector would try to expand activities that increase its discretionary power for rent creation, using differential trade and tax regimes, direct subsidies, licenses and so on, whereas the private sector would lobby for access to such rents, and those who benefit would oppose any liberalization that might reduce their rents (for instance, Krueger 1974). Political systems that owe their legitimacy to the distribution of specific benefits to their clients are of course especially susceptible to rent-seeking behaviour, especially when the number of large enterprises is fairly small, relationships between politics and business are highly personalized, and checks and balances are weak (Bräutigam 2000). Even scholars, who defend the need for industrial policies in principle, are often sceptical about their applicability at early stages of industrialization. Soludo and Ogbu

(2004: 27), for example, state that ‘only when the state is capable and developmental, and has a vibrant capitalist class can industrial policies be effective’.

The assumption that all stakeholders simply pursue self-interests, however, needs to be qualified on two grounds. First, politicians and bureaucrats are not only driven by short-term interests of revenue maximization. They are, to different degrees, also motivated by elements of social responsibility, personal reputation, and professionalism. Altruistic considerations, the quest for social recognition, the need to ensure legitimacy in the longer term as well as prevailing ideologies and paradigms all play important roles. Second, the assumptions of public choice theory are challenged by empirical evidence. Some Asian countries with strong neopatrimonial traits—such as Indonesia under Suharto and Malaysia under Mahathir—have extensively applied industrial policies and achieved rapid industrialization combined with considerable welfare gains (Khan and Jomo 2000; Moore and Schmitz 2008). Such success can hardly be explained under the assumption of indiscriminate pursuit of self-interests.

### **3 Evidence: industrial policy in Sub-Saharan Africa and the MENA region**

This section explores the performance of industrial policies in SSA and the MENA region. These two regions are most frequently associated with neopatrimonialism (e.g. Bratton and van de Walle 1997; Bank and Richter 2010; Pawelka 1985), and both are among the least competitive regions in non-resource based industries. Not surprisingly, the (unfortunately scarce) literature on industrial policy in these regions is mostly very critical with regard to effects and prospects of industrial policy.<sup>5</sup> Recently, however, some dissenting voices started to reinterpret informal public-private ties as being (partly) functional for development. Kelsall et al. published a paper on ‘developmental patrimonialism’ in SSA, arguing that ‘centralized, long-horizon rent-seeking, when combined with broadly pro-capitalist policies, can generate dynamic growth’ (Kelsall et al. 2010: 26). Along similar lines, Abdel-Latif and Schmitz (2010) discover public-private ‘growth coalitions’ in Egypt.

Against the backdrop of these inconsistent findings, the German Development Institute (DIE) conducted a comparative analysis of industrial policy performance in four SSAs and three MENA countries; a synopsis of overall findings follows. For most countries, these confirm the critical views on industrial policy under neopatrimonial rule. Two countries, however, challenge the standard assumptions about the inability of neopatrimonial systems to contain rent-seeking and manage successful productive transformation: Tunisia and Ethiopia. These cases are therefore presented in some detail.

#### **3.1 Industrial policy in seven countries: main findings**

The following analysis includes the Sub-Saharan countries Ethiopia, Mozambique, Namibia, and Nigeria as well as Egypt, Syria, and Tunisia in the MENA region.<sup>6</sup> All of

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<sup>5</sup> See e.g. Soludo, Ogbu, and Chang (2004) for SSA and Galal (2008) for the MENA region.

<sup>6</sup> See Altenburg (2011) for a synthesis report (which excludes the case of Nigeria and includes Vietnam). Most country case studies have been, or will soon be, published as DIE Discussion Papers, available at: [www.die-gdi.de](http://www.die-gdi.de).

these countries apply selective support programmes for particular technologies and groups of firms, defined either by sub-sector, value chain, region, or target market. The research explored to what extent neopatrimonial patterns impinge on industrial policy decisions and what this implies for their effectiveness.

The case studies confirm that neopatrimonialism is indeed pervasive in industrial policy making. Interview partners frequently mentioned cases where decisions regarding public contracts, credit allocation, jobs in the public sectors etc., had been taken on the basis of arrangements that did not correspond to the stipulated rules and regulations. It goes without saying, that these informal practices cannot be corroborated easily, precisely because neopatrimonialism implies the coexistence of formally valid legal-rational norms with informal social practices that function beyond the legal surface. The following observations are therefore based upon qualitative information gathered from experts, published case studies, grey literature, and own observations. All these sources mainly capture perceptions rather than hard evidence. To avoid mistakes or unfair judgements, information has been carefully cross-checked with country experts in different positions.

*Presidentialism* with a high degree of *concentration of power* is a common element in all seven countries. Decisions about industrial policies can often be directly attributed to the president, with fairly limited influence of the parliament. Presidents often personally preside over the most important committees related to industrial development, use personal media appearances to promote industrialization programmes, and personally visit business associations to urge their members to join government initiatives. In some cases they intervene directly in industry-specific decisions. Ethiopia's President Meles Zenawi, for example, stepped in to resolve problems in the emerging cut flower industry, including the negotiation of more favourable freight tariffs with the national airline and the allotment of land under favourable leasing conditions. Business tycoons often directly approach the presidents if they need to solve a specific problem rather than using formal channels. Furthermore, members of elites with trustful personal relations with the president are appointed to key positions of the public administration and state-owned enterprises or parastatals. In some cases, the presidents and intimates are directly involved as shareholders in large national investment projects, for example in the case of Mozambique's president Guebuza.

In all seven countries, institutional *checks and balances* are weak. They all rank clearly below OECD standards on governance indicators, although with substantial differences between countries. Namibia and Mozambique rank remarkably higher on the relevant indicators of 'voice and accountability', 'political participation', and 'rule of law' than Nigeria, Egypt, Ethiopia, Nigeria, Tunisia, and Syria. With regard to the World Bank indicator for 'voice and accountability', for example, the latter five all rank below the 25th percentile (2009).<sup>7</sup> Looking at industrial policy in particular, programmes are not rigorously evaluated in any of the countries, with the exception of some programmes

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<sup>7</sup> See: <http://info.worldbank.org/governance/wgi/index.asp>. The Bertelsmann Transformation Index (BTI) for 'political participation' (2010) more or less confirms this picture. (See: <http://www.bertelsmann-transformation-index.de/bti/>) With regard to 'rule of law' World Bank and BTI data are inconsistent. Here, the World Bank ranks the MENA countries fairly high, similar to Namibia and Mozambique, whereas the BTI gives the lowest scores to the three MENA countries and Ethiopia, but ranks Nigeria fairly high.

with strong financial involvement of donors. Some countries do conduct regular and detailed indicative planning, e.g. to prepare five-year plans, which may entail mid-term and final reviews (e.g. in Ethiopia). These, however, tend to monitor activities, rather than outcomes or impacts. Moreover, they are not carried out by independent parties and rarely challenge the fundamentals of how programmes and institutions are organized.

The case studies also revealed widespread *clientelism and patronage* in industrial policy operating through a variety of channels. One important channel is the assignment of jobs in the public administration and state-owned enterprises on the basis of political loyalty rather than professional merits. In Mozambique, it is well-known that positions in the civil service are almost entirely reserved for members of the ruling FRELIMO party. In some cases, organizations affiliated with the ruling party also have considerable influence on the award of jobs, such as the National Union of Namibian Workers. Typically, those employed in the public sector and state-owned enterprises receive a range of benefits, such as higher wages, pension and insurance schemes, severance payments and public holidays, which are not granted to other citizens.

Another mechanism of clientelism is privatization of state enterprises. In Mozambique, after the civil war FRELIMO transferred privatized companies to politically associated persons and supported them with subsidized credit, with the dual objective of creating a national class of entrepreneurs and enhancing political loyalty. In Egypt, state enterprises, e.g. in the steel and cement industries, have been transferred to intimates of President Mubarak who have been able to reap considerable rents from these protected industries.

In addition to such collusive practices of privatization, politically connected companies have often taken many of the business opportunities left for private engagement. Examples include companies owned by members of the ruling party (e.g. in Mozambique), the military (as in Egypt and Syria) or party-affiliated endowment funds (as in Ethiopia). As a result, the borderline between business and politics is often blurred. Entrepreneurs who compete with state-owned and politically connected enterprises frequently claimed that those enterprises get preferential treatment when it comes to operating and import licences, public purchasing, and credit from the state banking system, or that they are bailed out in times of crisis. As government decisions in these fields are often not transparent and may not be subject to checks and balances, however, it is very difficult to verify such allegations. Moreover, the case studies suggest an overall shift towards economic liberalization, albeit not necessarily with increased political freedom. Most notably in the three MENA countries, new technocratic and industrial elites emerged that depend less on oil and gas revenues, international aid and other rents.

How do these neopatrimonial practices influence the effectiveness of industrial policies? In this regard we found remarkable differences. This is particularly true for *strategic capability*. All countries have formally laid down their industrial development objectives in plans or ‘vision’ documents that outline medium-term targets until 2025 or 2030, but the practical relevance of these plans varies greatly. In most cases, the national strategies express overall targets (e.g. to increase value-added or to develop new export activities) and in some cases identify priority sectors (such as ‘agro-industries’ or ‘the textile industry’), but they do not provide a clear perspective with regard to where the countries may have a latent comparative advantage, what the most

binding constraints are, and what concrete steps should be taken to gradually move into more rewarding activities. Moreover, plans are often not well harmonized with the budgeting process. In smaller countries, planning documents are sometimes drafted by international consultants rather than developed in a participatory national planning process. In several cases, not even the main implementing agencies and competent private sector associations attributed any importance to these strategies. The two exceptional cases are Ethiopia and Tunisia.<sup>8</sup> As the following sections show, both countries have operationalized strategies for industrial upgrading and diversification, and the top leadership is clearly committed to follow up on these agendas.

With regard to *implementing capability*, the project encountered numerous examples of poor performance in all countries, but also some fairly successful projects. Due to attribution gaps and lack of counterfactual evidence it is generally difficult to assess the effectiveness of industrial policies. In many cases, however, failure was obvious. For example, most programmes aimed at promoting investments in export processing zones fell clearly short of their targets and often failed to attract more than a handful of investors (e.g. in Nigeria and Namibia). Similarly, several investment promotion agencies performed miserably, not only because they failed to attract much foreign investment, but also because many companies that did invest stated that they did not make use of any of their services except for compulsory licensing issues (e.g. in the case of Ethiopia). In Mozambique, efforts to transfer state-owned enterprises to private entrepreneurs and support them with subsidized credits largely failed, and large parts of the credits were never paid back. SME promotion agencies were generally rated as highly inefficient in terms of impact and outreach<sup>9</sup> and several SME development funds were discontinued due to dissatisfactory performance.<sup>10</sup> In some cases, government sources admit policy failure. A Nigerian government report assessed that the country's system of fiscal incentives was lacking in focus and poorly administered. Overall, industrial development programmes are typically initiated without defining an exit strategy, which may make it difficult to withdraw rents when they are no longer needed.

Some industrial policies, however, seem to have been quite successful. Tunisia's industrial upgrading programme is a case in point. The long-term effort to support the competitiveness of enterprises with the aim of tapping into outsourcing opportunities from Europe successfully strengthened and diversified the export industry. Increases in manufacturing investments in Egypt and improved export performance could also be traced back to industry modernization and investment promotion programmes. In the Sub-Saharan countries, the case studies identified a handful of successful initiatives in particular sub-sectors. These were usually related to areas of latent comparative advantage where powerful investors pushed for supporting measures and regulatory reforms. Examples include the development of the aluminium smelter and supporting industries cluster in Mozambique and the Ethiopian cut flower industry. In some cases,

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<sup>8</sup> The research referred to Tunisia under Ben Ali, who was ousted in January 2011. It is not clear, to what extent the new government will deviate new directions from the authoritarian take.

<sup>9</sup> Such as the Instituto de Desenvolvimento da Industria Local in Mozambique, the Small Scale Enterprise Development Agency in Nigeria, and the Federation of Medium and Small Enterprise Development Agencies in Ethiopia.

<sup>10</sup> Including the Fundo de Fomento a Pequena Industria in Mozambique and the Small and Medium Enterprises Equity Investment Scheme in Nigeria.

donor support facilitated successful initiatives, e.g. supporting incipient clusters of pharmaceutical and leather industries in Ethiopia and Namibian exporters of plant products for the cosmetics and pharmaceutical industries.

Tunisia and Ethiopia are particularly interesting due to their clear commitment to an agenda of industrial transformation and reasonably effective implementation. In Tunisia, this commitment resulted in sustained economic growth relative to the rest of the Maghreb/Mashriq region, an increasing share of manufacturing in GDP and a rapidly growing urban middle class. Tunisia today scores far higher on the global competitiveness index than any other country of its region. Ethiopia achieved sustained growth of over 10 per cent annually in the period 2005 to 2010 and is one of the few Sub-Saharan countries on track to achieve the Millennium Development Goals. Its industrial development and economic diversification are not satisfactory, but progress in terms of human capital formation and firm productivity are expected to spur industrial development in the near future.

The strong development commitment and above-average performance of Tunisia and Ethiopia is somewhat unexpected, because both governments are quite authoritarian and score particularly low on political participation.<sup>11</sup> Ethiopia, furthermore, ranks clearly below the average of SSA on indicators of rule of law and regulatory quality.<sup>12</sup> Why did these two countries—despite weak governance and typical characteristics of neopatrimonialism—manage to foster productive transformation better than the other countries? According to almost any governance indicator, policy processes should be much more effective in Namibia and Mozambique—but none of these countries makes visible progress in terms of industrialization, enterprise upgrading, and diversification.

The following sections summarize the industrial policies and the performance of Ethiopia and Tunisia. The two countries are at very different stages of economic and institutional development. Ethiopia is one of the poorest countries in the world, ranking 119th in terms of global competitiveness (2010–11). Its challenge is to create the very basic preconditions for industrial development in an agrarian post-war society. Tunisia is a middle-income country ranking 32nd on global competitiveness, and it is in the middle of a transformation from a rent-based, state-driven, and inward-looking economy to a modern industrial market economy which is increasingly integrated into European value chains.

### **3.2 Ethiopia: creating conditions for industrial development in an agrarian post-war society<sup>13</sup>**

Ethiopia is one of the world's least developed countries. The country is still largely agrarian, with 85 per cent of the workforce engaged in the rural economy. Its main resources are agrarian, but the potential for commercial crop production is limited as only small areas are irrigated and rainfalls are irregular. From 1974 until 1991, the country was ruled by a pro-Soviet military junta that nationalized most industries and

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<sup>11</sup> On the BTI 2010 ranking of political participation, Tunisia scores 2.5 and Ethiopia 3.0 (against a maximum of 10 points).

<sup>12</sup> World Bank Governance Indicators for 2009.

<sup>13</sup> Altenburg (2010) provides more background information on Ethiopia's industrial policy.

private urban real-estate holdings. Mismanagement and the junta's violent rule provoked a protracted civil war.

When the civil war ended in 1991, the incoming government under President Meles Zenawi was confronted with a situation of multiple market failure; it recognized the private sector as the main driver of economic growth, but there was very little private sector to build upon, as the better educated and entrepreneurial persons had mostly fled the country during the years of socialist dictatorship and civil war. Moreover, the new regime distrusted the old elites which it regarded as rent-seekers interested in making quick money from trade and financial transactions rather than investing in industrial infrastructure and technological capabilities. Also, the main potential lay in improved agricultural productivity and agro-processing, but the rural areas lacked irrigation and roads, let alone cold chains to market perishable products. After the previous socialist government's failed effort to collectivise farmers, land was returned to smallholders, which additionally made it difficult to attract large-scale investments in agriculture. Finally, the education system was unable to supply the skills needed both in government and the private sector.

In this situation, the government embarked on an ambitious top-down transformation project. Its aim was to industrialize the country with a focus on export-led growth. Big public investments were made in infrastructure and education, including the foundation of about twenty new universities and the establishment of a system of technical and vocational education and training (TVET) which, by 2010, had 815,000 enrolled students. Specialized institutions for sector-specific technology development were created. Simultaneously, the government pushed for technological upgrading and export-orientation of national industries that would absorb the skilled workforce once it had graduated from the university and TVET systems. Leading companies were involved in an upgrading programme in which the government set export targets and offered consulting and credit on the basis of performance.

While encouraging private investments, the government made sure that it kept control of the economy and established clear limits to liberalization. It privatized many state-owned enterprises, but defined narrow boundaries for private engagement in the financial sector and maintained its monopoly in telecommunications. It facilitated long-term lease contracts for investors in agriculture, but refrained from liberalizing rural land markets; it invites donor support, while carefully avoiding aid dependency, so as to retain control over its economic policies.

The government applies an authoritarian command and control style of policy-making. It distinguishes 'developmental entrepreneurs' from 'rent-seekers' and interferes to support the former and limit the scope for the latter; it favours producers over traders, and exporters over producers for the local market; and it handpicks companies for its enterprise upgrading programmes. Business associations are used to convey the government's messages and educate their members rather than to engage in an open dialogue. When opposition forces gained influence in the 2005 elections and started to seriously challenge the government, the leadership of the Ethiopian Chamber of Commerce was replaced. The overall attitude towards the private sector is to educate, guide, and train, rather than to encourage creativity and competition. The ambiguity of government policy is also reflected in its public sector reform. A business process re-engineering programme has been implemented to strengthen meritocracy and improve



performance; below the surface of this programme, however, critics claim that the restructuring process was used to remove political dissenters from office.

Hence, Ethiopia's policy can be characterized as an authoritarian, politically controlled, and state-led attempt to create a competitive economy. In this attempt, informal ties with parts of the business community have an important role. Following the civil war, endowment funds were created from remaining war funds and incoming aid, which were allocated to ex-combatants. Their dual purpose was to reward and reintegrate combatants and to reconstruct the country. As the liberation fronts were organized along ethnic lines, so are the endowment funds. How exactly these funds were allocated, and how big they are, is not transparent. Although they operate as non-governmental public charity organizations, they have never been audited and there is no transparency with regard to management structure, or profits and losses. Private competitors claim that endowment companies have preferential access to credit facilities of the state-owned Commercial Bank of Ethiopia and that indebted companies have been bailed out, but due to the discretionary character of many government policies it is not possible to verify these allegations. In any case, due to their head start, the endowment companies seized many unfilled business opportunities and are now among the largest investors.

Industrial policies often provide support on a case-by-case basis. Leading agro-industries, textile, garment, and leather product companies are targeted to become role models for their respective sectors and make inroads in export markets. Beneficiaries may receive land, buildings, or consultancies at highly subsidized rates. While subsidy allocation is discretionary, it generally seems to be based on assumptions about spillover effects and benefits different types of enterprises. While state-owned and endowment companies are among the beneficiaries, there is no strong bias in their favour. In exchange for support, the government expects companies to support its development programmes. This is particularly true for endowment companies. When the government launched a cooperative vocational training programme, for example, these companies were expected to accommodate students.

Ethiopia's is now starting to reap the benefits of its coordinated effort to develop infrastructure, human capital, and the private sector. It achieved extraordinary economic growth of over 10 per cent annually in the period 2005 to 2010, increasing per capita GDP from US\$682 to 1,120 (PPP). In 2010, 29 per cent of the about 81 million population were estimated to live below the poverty line of US\$1.25 a day (PPP)—a considerable improvement compared to the 61 per cent reported in 1995. Industrial development is stagnating at a low level, and export competitiveness and diversification are increasing only slowly. However, progress has been made in terms of human capital formation and productivity of its larger enterprises, which is likely to spur industrial development in the near future.

Ethiopia's industrial development strategy blends different ideological elements. As in Western market economies, the private sector is recognized as the main driver of growth. At the same time, carrots and sticks are used to develop specific groups of enterprises and push them towards exporting. Korea, Taiwan, and Japan are Ethiopia's role models in this regard. Moreover, the preference for manufacturing industries and disdain of trade and commerce can be seen as a legacy of the Marxist roots of the liberation movement. Overall, the regime deserves to be characterized as 'developmental'. Government interference in the economy is strong, but generally with the intention to achieve government targets rather than for personal enrichment.

Enterprise surveys confirm that corruption is clearly below Sub-Saharan levels. Still, non-transparent state-business relations and the lack of institutional checks and balances give cause for serious concern and may derail the developmental course of the government any time.

### **3.3 Tunisia: managing the transition from a state-led pre-industrial society to an export-driven market economy<sup>14</sup>**

When Tunisia became independent in 1956, it hosted only 290 enterprises of more than 50 employees; 85 per cent of the firms were owned by foreigners. The incipient national entrepreneurial class was mainly engaged in small agricultural and commercial activities. Industry employed only 2 per cent of the workforce. Aside from some phosphates and iron ore, Tunisia did not possess significant fossil and mineral resources, and its farming sector was heavily dependent on seasonal rainfall. The country had inherited an educated middle class and a fairly professional civil service from the French, but it lacked many of the skills needed for industrial development. At the time of independence, Tunisia did not have a single institution of higher education. Hence, although Tunisia at independence was not as poor as Ethiopia after the civil war, but it was confronted with similarly adverse conditions for economic development.

Today, the country has an export-led market economy based on competitive private companies. Over the last 15 years, Tunisia has achieved sustainable economic growth of about 5 per cent annually, which compares favourably with other countries of the region. In 2010, industry accounted for 34.6 per cent of GDP, up from 11.9 per cent in 1980. Manufacturing exports are gradually shifting from simple garment assembly to more demanding electronic and mechanical products. Recently, the country has intensified its efforts to advance towards an innovation-oriented economy, with new support schemes, including ‘techno-cities’ and business incubators, and considerable investments in new activities, such as information and communication technologies and solar energy. Tunisia’s industrial development programme was labour-intensive and relatively inclusive, enabling the emergence of a considerable middle class; 80 per cent of the Tunisian population are officially rated ‘middle class’. The US\$2/day poverty rate fell to 3.8 per cent (2005).

This success was achieved on the basis of an authoritarian system. From 1956 until 2011, only two presidents ruled the country—Bourguiba until 1987, and Ben Ali until 2011—whose power was close to being absolute, building in particular on a dominant party system, a professional palace administration, and a repressive security apparatus. While their rule is best characterized as authoritarian, both presidents resorted to neopatrimonial politics to reinforce their power. Leading positions within state institutions were reserved for party members (and, under Ben Ali, increasingly also loyal technocrats). Important policy decisions were taken by a very small circle of top decision makers from the ruling party and the key institutions of the central state. Bourguiba had created a largely uncontrolled presidential ‘shadow’ budget, which allowed him to create personal links to key social actors, including the country’s business elites. An extended clientelist network clustered around the presidential family itself. Furthermore, the social security schemes and subsidized commodities and utilities

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<sup>14</sup> This section summarizes the DIE project’s country case study by Erdle (2011).

were used to grant privileges to state officials and public sector employees. Patronage resource was employed to buy support from specific societal groups. Examples include preferential customs rates for small cars, subsidized personal computers for low-income families, and subsidies for the interior provinces. Some of these schemes operated outside the state budget and were granted in an ad hoc fashion.

Tunisia is thus another interesting case of successful structural change under neopatrimonial rule. This development, however, was not straightforward. Following independence, president Bouguiba initially tried to avoid every step that could possibly scare investors away, many of them still foreigners. It soon became apparent, however, that it would not be possible to unleash economic growth and create sufficient employment for the rapidly growing population unless the government would undertake pro-active measures to develop indigenous productive capabilities. In the early 1960s, the government therefore embarked on an import-substitution strategy. In parallel, Bourguiba enacted social reforms, e.g. liberating women from their religiously sanctioned dependency on male family members and enabling them to participate in the modern labour market. As a result of this new policy, the number of state-owned enterprises and public sector organizations increased from less than 25 in 1960 to about 185 in 1970, and their share of national investment grew from 2 to 34 per cent.

As in many other countries, import-substituting industrialization proved to be financially unsustainable. In the early 1970s, Tunisia therefore started to complement import-substitution with export promotion, with a focus on labour-intensive manufacturing. About 800 new industrial ventures emerged in the following years, effectively doubling industrial capacity. The private share in industrial investment, which was only 22 per cent in the 1960s, rose to 43 per cent in the mid-1980s. Still, loss-making state enterprises and the negative trade balance of import-substituting industries increased the external debt. When droughts, decreasing remittances, and an increasing dollar price exacerbated the debt crisis and austerity measures provoked public rioting, Bourguiba was finally dispossessed in 1987.

The incoming president Ben Ali recognized the need to create new employment opportunities in order to absorb the country's growing workforce and maintain socio-political stability. The crisis had consolidated a consensus among the 'inner circle elites' that economic development should be achieved through market forces rather than state planning. Ben Ali increasingly brought technocrats into leading positions who would have the expertise to manage the necessary transition, but who were also loyal followers. In the absence of easily extractable natural resources, the future was seen in increasing the insertion in European value chains. Industrial policies reallocated resources from import-substituting production to export industries as well as the foreign exchange earning service, mainly tourism. The domestic market was increasingly liberalized, and most 'strategic' sectors were opened for privatization, including transport, energy, telecoms and banks. WTO accession and agreements with the European Union (Euro-Mediterranean Partnership in 1995; Euro-Mediterranean Association Agreement in 1996) made economic liberalization virtually irreversible, enhancing the legal security of private investors. In parallel, an ambitious export industry upgrading programme—the *programme de mise à niveau*—was launched. To date, about 4,400 enterprises have received consultancies and financial support to enhance their productivity. In 2009, manufacturing accounted for 75.4 per cent of exports (up from 36 per cent in 1980).

Tunisia's industrial transition is a remarkable success story, especially when compared with the slow increase of manufacturing competitiveness in most other Maghreb and Mashriq countries. Although the national transformation project of export-led industrialization was implemented under authoritarian rule, it was not only about shifting from an agrarian to an industrial society; it also changed the composition of the elites, with increasing power of private entrepreneurs and technocrats; it created a broad urban middle class; and it changed the pattern of economic governance, from informal to increasingly rules-based decision-making. Political liberalization, however, did not keep up with the economic transformation. Also, jobs could not be created at the pace necessary to employ the rapidly growing workforce and conform to the social aspirations of the emerging middle class. Public discontent with the economic situation and political repression led to a revolution in early 2011.

#### **4 Conclusions**

Latecomer countries face more severe market failure than mature market economies. Many of them still have to create a societal consensus on the need for industrial transformation and diversification; they need to encourage entrepreneurship and economic experimentation; nurture a nascent national entrepreneurial class; invest in skills development at all levels; set up regulatory institutions and quality assurance systems; and develop many other aspects that investors can already build on in established market economies. It is difficult to imagine how latecomers should be able to build new and internationally competitive industries unless their governments adopt pro-active policies to tackle some of the most problematic development constraints in a coordinated way. With limited state resources, such activities necessarily have to focus on the most binding constraints in the most promising sectors.

At the same time, our case studies corroborate the pervasiveness of neopatrimonialism in industrial policy-making. The risks of making industry-specific choices under these circumstances are well-known. Where decision-making is informal and personalized, where institutional checks and balances are weak and the whole political system is built on granting favours in exchange for loyalty, political capture is unavoidable. Lack of enforceable property rights creates uncertainty and thereby discourages private investments. Innovation is held back, because the alliance between governments and incumbent economic elites discourages competition with outsiders, and engaging in rent-seeking is often more lucrative for incumbents than concentrating on productive investments. Also, clientelism in the assignment of public employment runs counter to the principles of a meritocratic civil service, thereby reducing the effectiveness of policy implementation. In fact, the case studies confirm the pervasiveness of anti-competitive alliances between government and economic elites as well as principal agent problems leading to ineffective policy implementation.

While these observations confirm conventional wisdom, two remarkable research findings call for a more differentiated consideration of the effects of neopatrimonialism. First, all of the seven economies considered attract substantial, and generally increasing, private investments and achieved considerable economic growth—ranging from 4.3 per cent (Syria) to 7.9 per cent (Ethiopia) annually in the 2000–08 period. Many investors have obviously not been scared away by the informality of policy-making and limited enforceability of contracts, suggesting that it is possible to make arrangements with the authorities that provide sufficient investment guarantee. This is perfectly rational,

because patron-client relations usually imply *mutual* commitments; politicians provide investment guarantees in exchange for political support or job-creating investments that help to enhance their legitimacy. In Egypt, Abdel-Latif and Schmitz (2010) found that informal ‘growth alliances’ between policy makers and specific groups of investors in fact lowered barriers to investment. In the same vein, clientelism and patronage may strengthen social ties in larger groups and thereby facilitate collective action among firms. In the Arab world, the term *wasta* (‘favouritism’) therefore has a partly positive connotation.<sup>15</sup> By definition, these arrangements are exclusive and therefore neither fair nor very efficient in terms of stimulating innovation, but the interesting finding is that they may still be able to bring about private sector-led economic growth.

Second, while the concentration of political power in the hands of strong presidents with considerable discretionary power may stimulate nepotism and corruption, the cases of Tunisia and Ethiopia suggest that this does not rule out the possibility of rulers pursuing ambitious projects of productive transformation. On the contrary, a neopatrimonial leader may need to make fewer compromises than a government in a mature democracy with complex political checks and balances, and thus be better able to organize big targeted investment programmes or to grant lavish subsidies to industry upgrading programmes for the existing economic elites. The fact that power is exercised in a personalized way further increases the scope of political leaders for engaging in arm’s length relations with key investors; e.g. to negotiate tailor-made subsidies for particular strategically relevant investors and to demand their moral commitment to actively support the governments’ development programmes.

More research is needed to understand why some neopatrimonial leaders, in Leftwich (2009) terms, become ‘developmental’ and create growth coalitions with the private sector, whereas others become ‘predatory or collusive’. Our country case studies point to three important interrelated determinants:

1. The *endowment with easily extractable natural resources* seems to be one important determinant. The fact that the governments of countries with high oil, gas or mineral resource rents—Nigeria, Egypt, Syria<sup>16</sup>—do not seem to be as highly committed to a national project of productive transformation as those in resource-poor Tunisia and Ethiopia supports the resource curse hypothesis. Governments in resource-poor countries have only few patronage resources at their disposal and therefore need to offer a convincing perspective of economic growth that benefits the population at large in order to ensure their legitimacy. Rents need to be created through productive sectors before they can be distributed.
2. The *ruler’s time horizon* seems to be another differentiating factor. As Olson (1993) analysed in his seminal paper on dictatorship, democracy, and development, purely self-interested rulers would have an incentive to immediately extract as many rents as possible if they assumed their tenure to be short. When they expect a long tenure, in contrast, they have more incentives to

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<sup>15</sup> See the discussion of favouritism in Loewe et al. (2007).

<sup>16</sup> Mozambique receives considerable rents from the Cabora Bassa hydro-electric power project which in turn attracted an aluminium smelter industry.

invest in economic development that would pay off in future rents and simultaneously buy political support from the electorate. The long reign of authoritarian rulers Ben Ali in Tunisia (1987-2011) and Meles Zenawi in Ethiopia (since 1995) enabled them to invest in long-term transformation projects that would inevitably take more than a decade to materialize in economic growth—such as the creation of a new system of technical universities and vocational training almost from scratch in Ethiopia, and the creation of a new export-oriented light manufacturing industry complex in Tunisia. Both presidents pushed their projects with an explicit long-term perspective in mind, and both started from a position of authoritarian rulership that was (with the exception of Ethiopia's 2005 election) never seriously challenged by electoral competition. Nigeria is a counter-example, where presidential terms have been much shorter and no societal agreement on national transformation strategies was achieved. It should be noted, however, that long tenures by no means guarantee developmental attitudes of the rulers, as the large number of long-lasting predatory regimes in the region shows.

3. Hence, the *intrinsic development orientation* of the national leadership makes a big difference. The assumption of purely self-interested surplus-extracting leaders (Olson 1993: 574) makes for analytical purposes is obviously simplistic, as he himself recognizes. In practice, individuals act out of very different motives. Political leaders are, to different degrees, also guided by values and convictions that include elements of altruism, nationalist convictions and are influenced by the predominant development ideas of their times. As shown for the example of Ethiopia, different ideological components can be traced back to specific historical lessons and international role models that impressed the top leadership.

The above factors are highly interrelated and dependent on a many other context variables. The case studies point out, however, that the political convictions of the presidents and the top leadership as well as the way they seek to create legitimacy and secure their power are key determinants of the quality of industrial policy-making and explain more of the country variation than structural characteristics of the economy or the administration. This is why a thorough understanding of the political logic of neopatrimonialism and its local specific manifestations are important to predict whether and how industrial policy may function.

At the same time, it needs to be stressed that an enlightened, developmental leadership that is not subject to political checks and balances provides a fragile basis for sustainable development. As Kelsall et al. point out, developmental experiments were not sustained in any of the African cases they studied, and they raise the question 'to what extent degeneration is an evitable consequence' (Kelsall et al. 2010: 27) of a model that encourages rent-seeking and lacks institutionalized controls. The recent revolutions in Arab countries confirm the latent instability of authoritarian regimes, even when they have been able to manage a fairly successful economic transition, as in the case of Tunisia.

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