BACKGROUND NOTE

What role do governments have in reallocating investment?

Today, governments are called on to create the necessary conditions for the transition of the social and economic model to bring it into line with a sustainable view of development. To do so, they need to move back into policy areas where the State's influence has declined: innovation, finance, redistribution... This then raises the question of private-sector recognition of the government's role. Does a "social contract" need to be redefined concerning the role of government? Should the State limit itself to a regulatory function or act as a strategist that sets goals and mobilises resources for this transition? What type of public institutions, centralised or decentralised, and what tools should the government mobilise for its actions?

1. CONTEXT

During the last quarter of the 20th century, the State—accused of inefficiency in resource allocation and production-related decisions—saw its weight in the economy decline. Various sectors that had been previously nationalised as they were considered to be public services were gradually privatised (telecommunications, energy, transport, heavy industry, etc.). Even in countries where the prevailing vision was one of an industrial, centrally planned and interventionist State, this has given way to a vision of a State with a narrower scope of action and budget deficits, serving as the custodian of rules for market competition among private players.

Yet, industrial policy has not disappeared from the spectrum of public action, notably in some States that are pioneering the promotion of energy transition, but also in developing and emerging countries that over the past twenty years have attained high economic growth. Now that protection of the environment presupposes sometimes major changes in the way society and production are organised, the government's role is again becoming pivotal. The concept now foregrounded is that of the State as a strategist steering policies that enable stakeholder expectations to converge: the British Foresight in the United Kingdom, Energy Transition *(Energiewende)* in Germany, and the National debate on energy transition in France.

Today, governments have to reconsider their areas of intervention, their institutional organisation and the tools they have to hand to steer investment decisions and modes of production and consumption.

2. ISSUES/SOLUTIONS

The effective transition of a society based on the use of limited natural resources towards a society whose consumption of natural resources remains within the limits of the planet's ecosystem (e.g., under 2 °C) cannot be taken for granted if left to private-sector initiatives alone. Yet, the private sector does not always recognise the importance that public action can have, despite the fact that in some cases government inaction can adversely impact the profitability of private business activities. Governments nonetheless have to hand unique positions and tools that can help facilitate a "smarter" and less costly transition for society as a whole, whilst also ensuring the protection of the most vulnerable.

Government action can then:

- aim to regulate the use of natural resources to improve the efficiency of their utilisation and limit the environmental damage caused by the actions of private agents;
- focus on the "classical" responsibilities of the Welfare State: create and maintain social and educational models that provide protection and inclusiveness. In a context of transition, these levers make it possible to build the skills needed for the future, improve individual wellbeing and bolster the acceptability of change;
- take on the responsibilities of a State that is a strategist and innovator, supporting research and development for new technologies and investing in the infrastructure required to deploy them. Rather than simply being in charge of making technology choices, the State seeks to promote and encourage collective risk-taking and ensure that costs and benefits are shared among societal actors. As such, it critically needs to have the capacity to minimise for society the costs of bad solutions, once these come to light.

These visions of the State's role are not mutually exclusive. Clearly, however, if the costs of externalities are to be integrated, this precludes taking a number of societal gambles, when: the initial cost is too high, the actors lack the necessary expertise; or the legal framework is poorly adapted. A renewed partnership between governments and all societal actors seems necessary.

Only governments can fix the political framework for transition, which generally involves defining laws and medium- or long-term objectives. This framework may be called into question by political reversals and changes in government. The State can then have the role of initiating domestic dialogues among societal actors, enabling these long-run visions to gradually converge and become anchored. In addition, the degree of public institutional decentralisation needs to be reconsidered, given that environmental protection and the solutions proposed often respond to local-level logics.

Access to and affordable capital is vital to channelling investment into new technologies and infrastructure. In this setting, the State can choose to go beyond its fiscal prerogatives and become a direct investor in some industries and technologies. It can also use financial regulation to steer investment flows in line with a vision that is more compatible with long-term objectives.

Lastly, the State has an active role to play in promoting research and development for new technologies. The sharing of costs and benefits between the public authorities and private sector needs to guarantee a fair return on investment and avoid privatisation of the benefits of innovations for which the public sector has borne the development risk.

3. OBJECTIVES OF THE SESSION/QUESTIONS

The objective of this session is to identify the roles expected of the State and the successful cases where tensions were successfully managed between the need to stabilise stakeholder expectations and the need to leave stakeholders room for creation and flexibility. The session also aims to identify the most appropriate tools and forms of action that governments have to hand in order to channel investment towards the desired transition.

- Should governments limit themselves to a regulatory function or play a strategic role and define the objectives and means used for the transition?
- What types of public institutions, either centralised or decentralised, should be mobilised?
- What role can be played by co-defining transition objectives and trajectories through dialogues among societal actors?
- What investment rationales and what structures for public finance institutions? What financial regulation is compatible with the transition?
- How can one prevent the benefits of innovations whose development risks were borne by the public sector from being privatised? What lessons can be drawn from the recent development of innovative industries (digital, renewable energies...)?
- What experiences can be applied in developing countries and what role can international cooperation play in institutional capacity building?

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This event has received financial support from the French government in the framework of the programme "Investissements d'avenir", managed by ANR (the French National Research Agency) under the reference ANR-10-LABX-01