

How can bold government work with the private sector to create the markets of tomorrow?



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The debate about the market vs the state was a false dichotomy. The new focus must be on how a bold, capable and well-structured state can unleash the full power of markets and the private sector in solving the problems of our time. To help and direct growth so that it is inclusive and sustainable, governments can help set priorities that have societal legitimacy, act as an investor of first resort and use all tools governments have at their disposal to crowd in solutions from multiple sectors and actors and create the conditions to grow niches of innovation into well-developed markets that can provide solutions to today's most pressing problems.

The challenges we face today require an economic transformation of a depth, scale and speed unmatched by any in human history. The urgency to compress change into meaningful time frames requires creative policy-making and bold leadership. Recent unprecedented global disruptions have forced governments into action. Now they must direct this openness to deploying state capabilities to responsibly shape our collective economic future.

Bolder government leadership is needed in a variety of ongoing crises: **increasing inequality, climate change and environmental degradation, new and old health crises, and shifting geopolitical contexts**. All these challenges require socio-technical systems to adapt, design and grow new solutions. For the first time in the past three decades there is a growing consensus that the private sector alone cannot drive this economic transformation and a new contract between the state, capital and labour is necessary to create a more equitable stakeholder form of capitalism.

Despite commitments, progress has been too slow in two key respects:

1. In the vast majority of cases **the public and private sectors have not found a symbiotic way of working together**. The focus of policy-makers and public officers remains largely limited to de-risking and facilitating private investments rather than actively participating with and thereby emboldening the private sector, sharing the risks and rewards of market creation activities.

2. **Directed market creation remains underused** to bring about the transition to a new and more sustainable techno-economic paradigm (the way economic value is produced and the incentives that shape markets). While mechanisms to adjust relative prices and internalize externalities (such as carbon pricing) are powerful and necessary tools, they are insufficient alone to establish the conditions necessary for new markets to emerge.

Radical change seems more possible than ever because societies have been forced to question existing paradigms. Governments and businesses have an opportunity to lay new foundations for long-term, shared prosperity, with a bold new approach to active economic policy.

How we get there – with bold leadership from the public sector

1. Dynamic public sector

Over the past few decades, many advanced economies have progressively reduced investment in the capabilities of the public, focused on reducing the size of public budgets rather than making them more dynamic and solution-oriented. The debate about the role of government in the economy remains focused on “how big” it should be rather than “how bold”. There needs to be a new narrative on the role of the public sector, shifting away from that of “burdensome bureaucracy” to one of “agile facilitator”. In turn this will also help make public employment more attractive for talented and innovative public servants.

Strategies for operationalizing this pathway include:

- **Encouraging a new approach to public administration** based on experimentation, learning-by-doing and mission-oriented market creation

- **Establishing new norms of sharing rewards and develop skills in the public sector** in terms of portfolio setting and risk taking, coherently and with an approach to public investment as the investment of first resort
- **Designing new metrics to evaluate public investments** that capture the dynamic spillovers that occur with bold policies, which are hard to capture with static cost-benefit and net present value analysis
- **Limiting the outsourcing of key capabilities** and ramp up investment within the public sector to enable it to become more capable and develop “absorptive capacity”
- **Adapting the measurement and accounting frameworks used to account for economic value** – at both the micro and macro levels – to assign a proper value to parts of the economy in which prices do not fully reflect their economic and societal contribution
- **Piloting new solutions and public-private governance models** to embed societal values in the development of new technologies and business models

2. Symbiotic public-private partnerships

The combined efforts of the public and private sectors are needed to transform techno-economic paradigms and bring better and broader growth. Yet public-private partnerships in innovation and market creation have often been too unbalanced and the benefits of successful projects have not been fairly distributed within the population.

Strategies for operationalizing this pathway include:

- **Introducing conditionalities for public investments, subsidies, guarantees and bailouts** to shift practices and behaviours within companies towards lower carbon emissions, better working conditions and fewer share buybacks
- **Establishing a new legal blueprint for patents and other intellectual property (IP) rights** that better balances private incentives and public interest for transparency and diffusion of knowledge
- **Rebalancing risks and rewards** in specific cases where the government provides support for research, such as through equity stakes or golden shares of IP rights
- **Developing initiatives that can diffuse knowledge and IP** necessary to address specific challenges, through pools, pledges and mandatory licensing
- **Increasing scrutiny of anti-competitive practices**, most notably patent trolls, through dedicated legislation and changes in the breadth of coverage granted to IP

3. Rethinking value

There is a growing tension between techno-economic systems (the way economic value is produced and the incentives that shape markets) and societal institutions (the set of values, formal and informal rules and beliefs shared in communities). Innovation in governance has been slower than innovation in technology and business models.

Strategies for operationalizing this pathway include:

- **Scaling hybrid methodologies for innovation** – such as social impact ventures – that better align economic and societal value, embedding a different approach to governance and transparency

What needs to happen – turning the problems of today into the markets of tomorrow

1. Production scale-up

In addition to a long-term pipeline of R&D, there is a tremendous opportunity to accelerate the uptake in different contexts, sectors and geographies of products and technologies that are already mature. With declining competition levels across all sectors government support is vital to go beyond incumbents and foster new entries that can reduce monopolies.

Strategies for operationalizing this pathway include:

- **Strengthen supply through subsidies, capital grants, government loans and other tools** that can help new entrants and trigger economies of scale
- **Target specific market niches that can help address future challenges**, especially those that do not get attention from current investors and industries
- **Shift government support** from incumbent players and sectors to new entrants
- **Encourage partnerships among businesses**, including SMEs, to align on common production and innovation challenges, pool knowledge and diffuse benefits
- **Use demonstration effects** through pilots and prototypes that can inspire local producers and help localize global solutions

2. Co-creating demand

The creation of new markets often requires a parallel approach on supply and demand. New products may struggle to find a space in the market even when they present superior characteristics, especially if they represent a new paradigm in terms of complementary know-how, infrastructure and other sunk costs. Governments can support demand for key products, but transformative change requires a change in behaviour by entire communities and a coordinated shift by actors, regimes and institutions.

Strategies for operationalizing this pathway include:

- **Change relative prices** through taxes, subsidies or other forms of economic incentives

- **Ensure initial market demand** through public procurement, public works or other forms of direct public spending
- **Align leading stakeholders, most importantly governments**, in regard to politically feasible solutions that are a win-win within the broader ecosystem
- **Work with communities to co-shape the broader techno-economic system** that influences their behaviours, preferences and perceptions
- **Establish clear key performance indicators and rigorous assessment** of the relative performance of goods and services brought to the market

3. Patient finance

The economic transformation required today builds on the scientific and technological developments of over a decade. Only a patient approach to innovation financing can deliver a continuous pipeline of new discoveries that can shape tomorrow's markets in the direction we need, protecting people and the planet. The public sector has the ability to absorb significant amounts of risk and to support projects over long time horizons – provided a fair sharing of the rewards is ensured as well.

Strategies for operationalizing this pathway include:

- **Setting up dedicated vehicles through public funding**, such as national investment banks or innovation funds specialized in the provision of long-term, patient funding (10-plus years)
- **Creating urgency on missions of vital importance in the long term**, starting with ensuring all actors agree on the statement of a problem, highlighting the fundamental threat it might pose to society and developing a clear plan
- **Rewiring private investments**, building on the growing success of ESG (environmental, social and corporate governance) and embedding “patience” much more strongly in the incentive mechanisms that drive the decisions of funders and investors, throughout the full spectrum that includes venture capitalists and philanthropists
- **Strengthening available metrics**, including adding qualitative dimensions (e.g., the time horizon of R&D projects) to existing indicators in ESG standards and national statistics

Difficult times require bold choices. The public sector that it can and must step up in times of crisis, but it must also work with and energize business for longer-term transformations that are more critical than ever before. With an active approach to economic policy-making – one founded on an ambitious mission-oriented approach rooted in public value – new markets can be created to solve the problems of our time, in our time.



Acknowledgements

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