GLOBAL FINANCIAL CRISIS: LESSONS FOR STRENGTHENING INNOVATION CAPACITY

As the dust starts to settle on the near meltdown of the world’s financial systems, it’s becoming increasingly clear that weak regulation is to blame. Does this mark the beginning of the end for public policy’s love affair with unrestrained private sector-led development?

In this edition of LINK LOOK Andy Hall wonders whether there aren’t some parallels and lessons for efforts to strengthen agricultural innovation capacity in the South.

THE WONDERS OF HINDSIGHT

In the US congressional hearing into the financial crisis, former head of the Federal Reserve Alan Greenspan explained that in the early 2000s he believed that markets would self-regulate. In this laissez-faire environment, faced with a desperate need for new customers, the American banking sector innovated, coming up with a range of financial products aimed at ever-more risky customers.

Greenspan claimed that it wasn’t until 2005 that he realised that markets were “undervaluing risk” — in plain English, they weren’t self-regulating and, instead, banks were selling cheap credit to customers who under normal circumstances would be rejected as borrowers. The unwinding of the subsequent credit-driven boom has literally brought the world to its knees and Greenspan’s earlier idea that markets would self-regulate now seems almost laughable.

This analysis is simplistic and it’s easy to be wise after the event. However, in an era of globalised, innovation-driven development there seem to be some lessons for public policy more generally.

The first and most obvious is that the market — the private sector — can and will innovate in response to opportunities and this can lead to economic growth. However, don’t expect the private sector to behave responsibly! Its power is derived from its unbridled self interest. Social and environmental concerns are not part of the equation. It would also seem that business time horizons can sometimes be very short — profit today and who cares if it all collapses tomorrow.

The second and related point is that public policy needs to play a much stronger role in managing "Continued on Page 2"
A recent working paper from the UK’s Overseas Development Institute (ODI) (www.odi.org.uk/resources/odia-publications/working-papers/285-science-complexity.pdf) by Ben Ramalingam, Harry Jones, Toussaint Reba and John Young (2008), titled “Exploring the Science of Complexity: Ideas and Implications for Development and Humanitarian Efforts”, and a series of articles in a relatively new and excellent bi-monthly publication, The Broker (see issues 7 and 9 at www.thebrokeronline.eu) have discussed the merits of complexity theory as a way of better understanding and supporting the development process. Complexity theory will be instantly recognisable to students of innovation systems - interconnections and interactions produce non-linear outcomes, the centrality of learning, etc. In addition to the intellectual parallels, the innovation and the complexity communities might want to start sharing experiences on how these non-linear systems perspectives can be introduced into the dominant (and mainly linear) development policy paradigm. Only when this paradigm changes can these exciting old, new and reworked ideas start to make a difference.

The third point, if it wasn’t obvious already, is that we now have a global economic system. Weak regulation in America’s financial system has affected the whole world. This means that regulation, and public policy more generally, has to be thought of in global terms. Of course, international institutions such as WIPO and WTO are both a response and a cause of that need. Ironically if we are moving toward an era of a more proactive role for public policy in managing the power of markets — i.e., subsidising the private sector to behave responsibly — world trade rules will need to accommodate this. Do either developed or developing countries have the latitude to manage their markets in this way? Can protectionism be avoided?

The fourth point relates to the way governments have responded to the current crisis. Put simply, they have thrown tax-payers’ money at it. They have bailed out the banks (and maybe the auto industry) and are talking of a 1930s style protectionism. This might be viewed as subsidising the private sector — no doubt, it’s an idea that simultaneously offends free trade advocates and left wing thinkers alike. However, in the long run it would be cheaper to pay the private sector to act responsibly than to pick up the bill for sorting out the consequences of it not behaving — $5000 billion to bail out banks in the US alone and the likelihood of a protracted global recession and the social and economic costs that goes with it.

Are we likely to see such a shift in global public policy? Will the next few years really see the birth of an era that will be remembered for the emergence of fundamentally different forms of partnership between the public and the private sectors? Will the tax payer-funded bail out make enterprise more accountable to society? The financial crisis illustrates why new public policy perspectives are needed. The new political climate in the US, with the election of the Democrat President-Elect Barack Obama may be the signal of a period of changing policy perspectives with global ramifications.

Maybe!

PARALLELS IN AGRICULTURAL DEVELOPMENT

Agriculture’s own crisis — a crisis of rapidly-rising food prices — has been bumped off the headlines by the turmoil in the financial markets and it is still not clear what this new crisis will mean for agriculture. The international community’s response to the food crisis has already been played out. It included increased supplies of food aid and calls for increased investment in agricultural research. Both are required and welcome. However, as we have argued in a number of earlier LINK LOOKs (visit www.innovationstudies.org to download previous issues) what’s really needed are interventions to strengthen innovation capacity.

What this means in practice is the development of an integrated web of research, private sector activity, technical and market support services and a supportive policy environment that can nurture innovation.

Some of LINK’s recent research conducted by Laxmi Prasad Pant (Pant et al, 2008) on the Indian mango sector has illustrated what happens when public policy fails to take a proactive role in developing this sort of integrated capacity — the...
A SPOTLIGHT ON CURRENT WORK BY LINK RESEARCHERS

DATE: 17 January 2009

Critical questions
Actors’ roles are fixed and not challenged
New and diverse actors become involved as needs dictate
Process is actively coordinated and facilitated

The progressive change barometer

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Comments/observations: The key relationships in the project are largely ‘old’ relationships and there is little evolution in rules and practices. Most project partners are assigned to their tasks in light of history rather than in light of needs and current capacity. Erosion of influence and introduction of new partners is strongly resisted by some key stakeholders. Partners not treated or regarded as equals but overpowering influence by public service officials.

DATE: 9 March 2009

Critical questions
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The progressive change barometer

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Tracking and monitoring change: Two simple approaches to operationalise process monitoring

Previous LINK Research in Focus articles discussed the idea that social and economic outcomes are mediated through the process of institutional change — changes in the rules, routine and ways of working. The argument is that if impact is increasingly about institutional change, one needs to be far more serious about how such change is to be monitored. This, by extension, requires an expansion in the perspective of traditional Monitoring and Evaluation and Impact Assessment exercises, which tends to underestimate change because it views this in terms of short-term, tangible economic goals, rather than the wider behavioral changes that underpin current and future impact. Since there is generally a long lag-time before tangible benefits — which can be assessed — arise, there is a growing interest in approaches for monitoring changes in process.

LINK’s work under FAO’s Pro-Poor Livestock Policy Initiative (PPLPI) has been trying to explore some of these issues in relation to facilitating changes in the policy process. As explained in earlier LINK News Bulletins, the emphasis in PPLPI has not been on promoting livestock policies that are pro-poor or pro-innovation. Rather, it has been about promoting changes in policy processes and trying to make these processes more pro-poor and pro-innovation — i.e., more inclusive, more joined up, more coherent across policy domains, etc. To help promote change in policy processes as well as monitoring how processes are changing, a number of approaches have been tested.

A key idea here is that the identification of some typologies of desirable institutional change and institutional change trajectories allows the monitoring of such trajectories over time. A number of methodologies have been proposed. One that LINK has been testing is called Stages of Progress/ Monitoring Domains.

Process monitoring: Instructions for use

Most processes (R&D process, policy process, etc.) are too complex to monitor or analyse in their entirety to obtain any meaningful and useable results. It is thus useful to break them up into a number of distinct monitoring domains. To operationalise these two simple approaches seem to be useful — ‘artisanal’ and ‘flat-pack’.

The ‘artisanal’ approach requires a brainstorming meeting with partners and other key stakeholders with a purpose of agreeing on the baseline situation in respect to the process under discussion. Following agreement on the current state characteristics, the meeting moves to brainstorm about what the future vision for each of the agreed characteristics of the current process would be. Once consensus has been reached on such a ‘vision of the future’, intermediate progressive stages need to be identified and agreed upon. Next, the critical questions — which will have to be asked to be able to assess progress through progressive stages, from each of the identified baseline characteristics to their future vision — need to be enumerated. The results from this continuous assessment drive the adjustment of activities and the revision and redefinition of the essential questions as the process evolves and institutional learning and change proceeds. There are many parallels here with the action research approach.

The ‘flat-pack’ approach, on the other hand, makes use of standard monitoring domains that encapsulate the four-point analytical framework developed by the World Bank (2006) to investigate agricultural innovation capacity. Assessments are made through the use of standard questions for each domain. A standardised progressive change barometer allows process evolution in each domain to be assessed (for example, see the guide to this approach at www.innovationstudies.org).

The power of process monitoring lies in the fact that not only does it help track change, but it also promotes iterative learning and subsequent change among stakeholders and the explicit linking of policy processes to operational activities and impact. Whilst the ‘flat-pack’ approach’s pre-fab sheets should thus be used in this manner, they can, in principle, also be used in smaller groups or by individuals. Even if used in the latter way, the assessment can still form the basis for interaction among the different stakeholders and for the dialogues that accompany processes.

The brief operational guides to the two approaches can be downloaded from http://innovationstudies.org/images/stories/link%20processmonitoringversion.pdf. We hope that you will be tempted to go out and use them and provide us with your feedback.

REFERENCES:

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Continued from Page 2
sector fails to export to lucrative markets and this becomes yet another missed opportunity for agriculture-dependent poor people in mango-growing areas. This is clearly a case where public policy needs to subsidise the development of largely private sector innovation capacity in order to achieve social goals. Certainly, there is a danger that such an approach is vulnerable to capture by the non-poor, but this is where the role of public policy is to provide incentives to make sure this doesn’t happen.

Some of LINK’s case studies conducted for the World Bank’s book, “Enhancing Agricultural Innovation” (World Bank 2006), suggested that just like with the case of mangoes, market incentives are not enough to persuade the private sector to develop the sorts of links that underpin the capacities to innovate — the export sectors for shrimp in Bangladesh and vanilla in India were examples of this.

But we are now seeing cases where the private sector is developing links and networks to allow it to respond through innovation. LINK researchers Ekin Keskin (Keskin et al 2008) and Mirjam Steglich (Forthcoming) have recently been studying patterns of innovation response capacity in the livestock and horticulture industries in Kenya. They make three broad conclusions:

• Firstly, both sectors have done quite well, coping with both regional competition and disease outbreak (in the case of the livestock sector) and with increasingly stringent trade standards (both sectors, but particularly the horticulture sector).

• Secondly, this capacity to respond and innovate relies almost on no public sector support — neither in terms of technical support from public research organisations nor from favourable policies or other incentives. The two sectors have relied on their own networks within their sectors for support and have often accessed technology and expertise from international partners.

• Thirdly, while the social impacts of this pattern of livestock innovation response capacity are unclear, it seems that in the horticultural sector there have been negative social consequences. So while the sector has developed a capacity to innovate and respond to competition and trade standards, often this has been at the expense of smallholder segments of the production base. For example, it is easier to implement production innovation to cope with labour standards in large production facilities, for example. This is particularly problematic in a context where few alternative rural employment opportunities exist for those households that have abruptly moved out of agriculture.

Of course, the Kenya horticulture response capacity story is much more nuanced than that. The headline story from both these cases, however, is one of private capacity-driven success but public policy (and thus social) failure. So, even in a case where the private sector is sufficiently well-organised to develop the sorts of networked capacities to respond to change that we would view as innovation response capacity, it would be unrealistic (and unfair) to expect that these patterns of innovation capacity are either going to protect the poor or provide new opportunities for them.

The other part of the story is the glaring absence of public policy in efforts either to build innovation capacity or to provide incentives for these capacities to contribute towards social development goals.

THE END OF LIGHT-TOUCH PUBLIC POLICY?

The logical conclusion that one must draw from the above is that if one accepts that the private sector is going to be a key driving force in economic development (even in the poorest countries), public policy must take a much stronger role in managing and directing the power of market. There are two overarching priorities:

• Strengthen the resilience of economic systems: This means public policy must subsidise the development of private sector-led innovation capacity by investing in the linkages and institutions that join up ideas, opportunities, creativity and profit. Without such capacities, economic systems have no resilience to shocks and this has high social costs (unemployment, hunger and underdevelopment) to vulnerable segments of society.

• Provide incentive for responsible behaviour: This means public policy may need to subsidise innovation and business strategies that are uncompetitive or sub-optimal in a purely economic sense, but which address social and environmental concerns. Subsidising the private sector is not cheap or politically attractive in some countries, but neither is cleaning up the mess of unregulated private enterprise.

If we really are to move into an era of more proactive public policy of the sort discussed here there are many challenges ahead for the international community. Are there global policy regimes that can help the world achieve its social and environmental goals and responsibilities? How can developed economies work with policymakers in emerging economies to help align national policies to deal with national issues that have global significance? How can donors realign their programmes to support a new and (even) more critical role for public policy in the development process? Will the Washington consensus accommodate and support the new form of public-private alliance — the public-regulated, private-managed market — that seems to be needed?

The only thing that is sure right now is that, to borrow Alan Greenspan terminology, the market is under-investing in capacity and its under-valuing social and environmental risk of current patterns of innovation capacity development. Better to start and tackle this soon before we have another global crisis on our hands.

REFERENCES:

