



## CHAPTER 2

# INDUSTRIAL POLICY IN THE MENAAP REGION

### KEY MESSAGES

- Over the past decade, the number of active industrial policies—government action expected to increase strategic business activity—has increased more than threefold in high-income and middle-income MENAAP (Middle East, North Africa, Afghanistan, and Pakistan) economies.
- Industrial policy often operates through indirect and less visible channels in the region, not only through ministries and formal policy announcements but also through state-owned enterprises, sovereign wealth funds, and other quasi-public institutions.
- Differences in fiscal space, government bandwidth, market size, and exposure to conflict mean that Gulf Cooperation Council (GCC) economies, developing oil exporters, oil importers, and fragile states face very different industrial policy options and constraints.
- GCC countries, given their larger resources, make more use of subsidies and localization measures, while developing oil exporters and oil importers depend more on import-related measures, reflecting more limited fiscal and institutional capacity.
- Industrial policy in MENAAP follows a “stepping stone” approach. Across the region, policymakers aim to move toward higher complexity industries that are close to existing capabilities while creating future growth opportunities.

*Continued*

**KEY MESSAGES (continued)**

- Four case studies across the region in Dubai, the Arab Republic of Egypt, Morocco, and Pakistan highlight the heterogeneity in industrial policy experiences. From these experiences, two main elements emerge: an effective institutional setup for public-private dialogue and a public workforce with the expertise to engage in that dialogue.
- Industrial policy can help, but it cannot substitute for broader reform. Industrial policy is most likely to succeed when it addresses genuine market failures and is backed by capable institutions, clear objectives, discipline, and extensive data collection and rigorous evaluation. Where weak governance, macroeconomic instability, or political capture are the deeper constraints, industrial policy is unlikely to deliver lasting results.

**Introduction**

Industrial policy has returned to the center of economic policy debates worldwide, but its role in the MENAAP region is shaped by a set of characteristics that make the region unique. In addition to increased fragility, MENAAP economies face a particularly difficult combination of challenges: weak private-sector productivity, chronically underperforming labor markets, limited job creation for rapidly growing populations, and, in many countries, a heavy dependence on hydrocarbons or other narrow sources of growth. At the same time, the region is highly heterogeneous. High-income Gulf economies, middle-income oil importers, developing oil exporters, and conflict-affected states differ sharply in their fiscal space, institutional capacity, market size, and exposure to external shocks. These differences matter because they shape not only why governments turn to industrial policy but also which tools they can realistically deploy and through which institutions those policies are carried out.

There are many definitions of industrial policy. The working definition employed throughout this chapter is the one offered by Fernandes and Reed (2026): *Industrial policy is a government action expected to increase strategic business activities.* Based on this definition, this chapter shows that industrial policy in MENAAP is both more widespread and more distinctive than standard measures often suggest. In line with global trends, official announcements—an accepted measure of industrial policy—have risen sharply over the past decade, faster than among comparable countries elsewhere. Furthermore, industrial

policy in MENAAP often operates through less evident channels, including state-owned enterprises (SOEs) and sovereign wealth funds (SWFs), meaning that counts based on official announcements may understate its true prevalence.

The mix of industrial policy tools also differs across country groups. GCC economies make more use of subsidies and local sourcing requirements, while developing oil exporters and oil importers rely more on import-related policies. Across the region, governments tend to target sectors already viewed as strategic in national development plans (NDPs)—the strategic blueprints that outline a country's economic and social goals—such as tourism and chemicals. However, actual policy support is often clustered around a narrower set of activities, following a gradual “small steps” logic that favors sectors closer to existing capabilities while seeking entry into more complex products with higher long-term opportunity gain.

The chapter argues, however, that the effectiveness of industrial policy in MENAAP depends less on ambition than on fit. Countries with greater government bandwidth, more fiscal space, and larger effective markets can deploy a broader set of instruments, including more targeted ones with fewer unintended consequences. Where those conditions are absent, governments are more likely to rely on second-choice tools such as tariffs or broad market incentives. This prioritization is also recommended by Fernandes and Reed (2026). However, industrial policy is not a substitute for sound macroeconomic management, stronger governance, or broader private-sector reform. Moreover, in environments marked

by weak institutions or close ties between political and business interests, industrial policy can be captured, poorly targeted, or used in ways that reinforce existing distortions.

The main conclusion is, therefore, an optimistically cautious one. Industrial policy can help MENAAP countries diversify, build capabilities, and support structural transformation, and the region offers important examples of partial success—from Morocco’s automotive industry to Dubai’s digital ecosystem. But industrial policy works best when it is selective and disciplined, embedded in credible public-private coordination, matched to country capabilities, and subject to clear objectives. Rigorous data collection and monitoring and evaluation must be part of the industrial policy design from the initial stage. Finally, policies should be governed by a sunset mechanism, with a clearly defined end date that is strictly adhered to unless a transparent review justifies extension. In conclusion, the question is not whether industrial policy should be used in MENAAP. It increasingly is. The relevant question is whether it is being used in ways that are feasible, accountable, and aligned with the region’s deeper economic constraints and long-term development objectives.

The road map for the chapter is as follows. It begins by defining industrial policy and showing why, in the MENAAP context, the concept extends beyond formal policy announcements to include the role of SOEs, SWFs, and other quasi-public institutions. It then examines why governments in the region turn to industrial policy, focusing on key challenges: weak productivity, limited job creation, and slow diversification. Next, the chapter documents the increase in industrial policy use across MENAAP and shows how the mix of instruments differs across GCC economies, developing oil exporters, oil importers, and fragile states according to differences in fiscal space, government bandwidth, and market size. It then explores which sectors are being targeted and argues that industrial policy often follows a stepping-stone logic in the region, favoring activities close to existing capabilities while also seeking future gains in complexity. Finally, it assesses the institutional vehicles through which industrial policy is implemented and argues that, while industrial policy can support diversification

and structural transformation, its success depends on strong institutions, clear objectives, and disciplined implementation and is based on complementary reforms in governance, competition, and macroeconomic management.

## Industrial policy: An elusive concept

Industrial policy “means different things to different people.”<sup>1</sup> The late economist Paul Geroski opined in 1989 that a “random collection of six economists is sure to produce at least a dozen different opinions on the subject” of industrial policy. The definition used in this chapter—industrial policy is a government action expected to increase strategic business activities—is broader than generally used in academic literature. It focuses on the expected impact of the implemented policies in terms of increasing certain types of economic activity in a certain sector rather than any other objectives stated when policies were announced.

This definition has three elements: The first is “government,” which includes the institutions that design and implement industrial policy. Government comprises official entities, ministries, and agencies but also less common ones like national development banks (NDBs), SOEs, and SWFs when it comes to implementation of industrial policy. The second element is “actions”—the policies themselves, the tools that are deployed. The third element is “strategic business activities,” which present the notion that an industrial policy is expected to affect some activities and not others.

### Element 1: Government

Government institutions charged with undertaking industrial policy should have the best managerial talent with the right academic and professional

<sup>1</sup>This is a sentiment voiced by the OECD’s competition committee in their Series Roundtable on Competition Policy No. 96, “Competition Policy, Industrial Policy and National Champions” and echoed in Evenett (2003) in “Study on Issues Related to a Possible Multilateral Framework on Competition Policy”; Vyshnevsky and Dementiev (2011) in “Industrial Policy for Ukraine: Theoretical Aspects”; and Pack and Saggi (2006) in “Is There a Case for Industrial Policy? A Critical Survey.”

credentials. These technocrats should be shielded from politics—which can be difficult to achieve in the MENAAP region because political power and business interests are closely intertwined. In addition to formal government institutions, such as ministries, a number of other entities can play roles in industrial policy: (1) NDBs, (2) SOEs, (3) SWFs, (4) cluster initiatives, (5) public-private dialogue and coordination agencies, (6) innovation and research and development (R&D) agencies, (7) investment promotion agencies, and (8) export promotion agencies. This chapter examines the roles played in carrying out industrial policy by SOEs, because they are so ubiquitous in the region, and SWFs, because of their importance in GCC economies.

## Element 2: Policy tools

Industrial policy tools cover three broad categories: (1) tailored public inputs, (2) market incentives, and (3) macroeconomic interventions.

### *Tailored public inputs*

In general, public inputs, such as skills development programs or industrial parks, can affect all industries. But when they are designed for a specific industry, they become an industrial policy tool. They are often referred to as “soft” industrial policy and encompass skills development programs, industrial parks, quality standards, and market access assistance. MENAAP countries regularly use tailored public inputs as part of their industrial policies.

### *Skills development*

In Morocco, with a wide range of industrial policies targeting the auto industry, professional training centers were created to offer apprenticeships and firm-specific training for the automotive workforce. These programs are closely aligned with industry needs; the centers operate under a public-private partnership model in which training programs are developed in collaboration with the companies.

In the Arab Republic of Egypt, personnel training is one of the core activities of tourism-sector development. State-led workforce training, public-private joint initiatives, and multisectoral partnerships enhance service quality and strengthen human

capital in Egypt’s accommodation and hospitality sector. For instance, in 2024, nearly 43,000 tourism workers were trained across various fields, including hospitality, food safety, and sustainable tourism. Moreover, public-private training collaborations are helping expand workforce capacity. For example, joint initiatives among the Ministry of Tourism and Antiquities (MoTA), industry associations, and private companies trained hundreds of hospitality professionals in such important destinations as Cairo, Sharm el-Sheikh, and Hurghada on the Red Sea.

### *Industrial parks*

Dubai Internet City was created as a specialized “ecosystem” to host the information and communications technology (ICT) sector. It provided such tailored inputs as solid telecommunication connections with much lower faults rates and offered technology companies access to digital networks at a price other advanced economies could (or would) not match. In so doing, the government created an environment specifically optimized for the operational and connectivity needs of global technology firms as part of Dubai’s desire to become a digital hub.

Industrial clusters were at the heart of Morocco’s effort to grow an auto industry. Six industrial parks host auto suppliers in the country. Around Tangier, the Tanger-Med Industrial Platform connects local free zones with the Tanger-Med port. These free zones combine features of industrial parks—such as the infrastructure needed for production and distribution—and the features of special economic zones, which include tax and customs benefits, efficient customs procedures, and access to capital flows. The areas near special economic zones have seen an increase in economic activity, as proxied by nighttime light intensity (box 2.1).

### *Quality standards*

In 1999, Tunisia enacted national organic regulations, delineating requirements in production, processing, handling, and marketing of organic food. In setting standards, Tunisia referenced international standards, such as the European Union’s organic regulation, which facilitated the European Union’s

### BOX 2.1 Special economic zones drive growth in surrounding areas: Evidence from nighttime lights' intensity

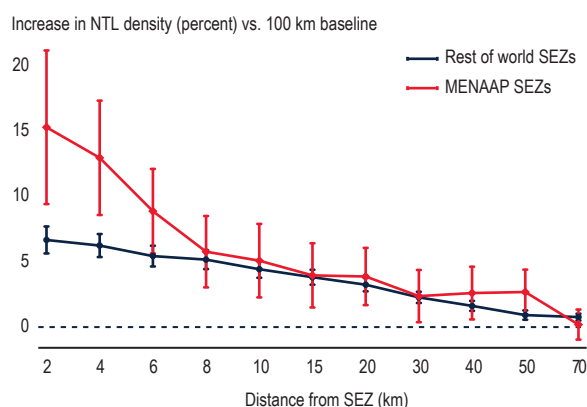
Evidence suggests that special economic zones (SEZs) are linked to higher economic activity in nearby areas, as measured by growth in nighttime lights (figure B2.1.1). The analysis covers 132 SEZs in MENAAP countries and 1,821 SEZs in 22 other countries from a sample created by the European Bank for Reconstruction and Development (EBRD) for which the year of establishment—or, if unavailable, the year of announcement—is known. It combines SEZ location data with a harmonized global data set on nighttime lights covering 1992–2021 (Li et al. 2020).

To see how effects vary with distance, the analysis looks at a set of rings around each SEZ. It starts with

the area within 2 kilometers of the zone, then moves outward in bands of 2–4 km, 4–6 km, 6–8 km, and so on, using the outer 70–100 km band as a benchmark. It then compares the change in nighttime light intensity in each band between the year before the SEZ was established or announced and three years later.

Figure B2.1.1 shows that the economic effects of SEZs are strongest close to the zone and fade with distance. In MENAAP countries, these effects appear stronger than in the European countries in the comparison group. As in the rest of the EBRD sample, the largest growth spillovers in MENAAP are found within about 40 km of the SEZ.

**FIGURE B2.1.1 Association between the establishment of SEZs and the growth in nighttime lights**



Sources: EBRD (2024) data set on SEZs, Li et al. (2020), and World Bank calculations.

Note: To estimate the spatial spillover effects of SEZs, we use a harmonized global NTL data set (1992–2021) as a proxy for localized economic growth, restricting our analytic sample to SEZs established between 1993 and 2018. For each SEZ, we construct concentric, donut-shaped distance bands at 0–2, 2–4, 4–6, 6–8, 8–10, 10–15, 15–20, 20–30, 30–40, 40–50, 50–70, and 70–100 km, calculating the log difference in mean NTL density for each ring between the year prior to establishment ( $t-1$ ) and three years' post-establishment ( $t+3$ ). We estimate a two-way fixed effects regression—controlling for SEZ-level and establishment year fixed effects to isolate macroeconomic and temporal shocks—using the outermost 70–100 km ring as the baseline counterfactual to capture standard background growth. Using conditional marginal effects, the resulting plot displays the relative distance band estimates alongside their 95 percent confidence intervals separately for the MENAAP region and the rest of the world. The EBRD sample consists of select countries in the MENAAP region and ECA region. ECA = Europe and Central Asia; km = kilometers; NTL = nighttime lights; SEZs = special economic zones.

endorsement of Tunisia's regulations. In addition to setting standards, Tunisia gave a 30 percent subsidy of the cost of equipment used in organic agriculture and subsidized 70 percent of certification fees—which helped farmers absorb the costs of transitioning from traditional to organic production (ISO FAR 2016). In 20 years, by 2019, Tunisia had become the world's largest exporter of organic olive

oil—accounting for 65 percent of global exports (CBI 2024). Tunisian organic dates have also had a significant growth in exports.

#### Market access assistance

In Egypt's tourism sector, MoTA has also expanded market access through sector-specific promotional