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Innovation and European Regional Policy

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When the European Community is created (1957) the attention to the regional issues is minimal.

Three main reasons for that (Manzella 2009):

✓economic orthodoxy: optimistic feeling that integration would contribute to reduce regional disparities;

✓ unwillingness to grant responsibilities in a politically-sensitive field such as regional policy to a newly established sovranational institution;

✓ choice to entrust European Investment Bank with the role to finance projects to redress imbalances in Europe.

During the 60’s and 70’s, regional policy is essentially a competence of the national governments.

Policy instruments aim at influencing the allocation of labour and capital between regions and industries (incentives for investments).

Emphasis is placed on policies designed to move capital into areas of high unemployment (Armstrong, Taylor 2000).

In the 70’s, however, the issue of a European regional policy comes to the European agenda.

Why?

✓ The economic crisis draws more attention to the existence of a “regional” question in Europe (regional convergence stops; new problems of regional industrial decline).

✓ The debate on Economic and Monetary Union emphasizes the link between the process of monetary integration and the need for a regional policy (Werner Report 1970).

✓ Community enlargment.

In 1975, the European Regional Development Fund (ERDF) is created. But its role is still very small: it finances infrastructural projects chosen by Member States. It is also due to the need of reducing UK contribution to the EC budget

It is the Single European Act (1986) which lays the basis for a genuine European Regional Policy. The Policy seems needed to reduce the burden of the single market for Southern Member States (Greece, Spain and Portugal join EC) and other less favoured regions.

The strengthening of regional policy is essential for the ambitious project of a “Single Market”, since the potential costs for less developed regions of the European deeper integration (Padoa-Schioppa Report and Cecchini Report).

Reducing non-tariff barriers to trade, and the barriers to the exchange of services and capital, may increase concentration of economic activities in the leading cities and regions.

The “new economic geography” models (starting from Krugman 1991) set the theoretical basis for the European regional policy.

One crucial common result of the “new economic geography” models is the prediction that, due to market size effects (pecuniary and non-pecuniary externalities; economies of scale), an asymmetric spatial structure may emerge endogenously even from a situation with ex-ante identical regions as trade barriers are removed.

So, an ambitious Europe is launched with the Delors Report and the “Delors package” for the European budget.

An era of pro-Europe optimism.

More Europe.

More balanced Europe.

With the 1988 Reform of Structural Funds four main principles are established:

✓ **concentration**, which implies that the measures are concentrated on priority regions (Objective 1 and 2);

✓ **programming**, which results in multi-annual development programmes;

✓ **partnership**, which implies the closest possible co-operation between the Commission and the appropriate authorities at national, regional or local level in each Member State from the preparatory stage to the implementation of measures;

✓ **additionality**, which means that Community funding complements that of the Member States.

The idea of “**Community value added**”:

✓ the achievement of **Community goals** (economic and social cohesion, balanced and sustainable development, Community priorities);

✓**Community resources** (redistribution, concentration, integration, multiplier effect);

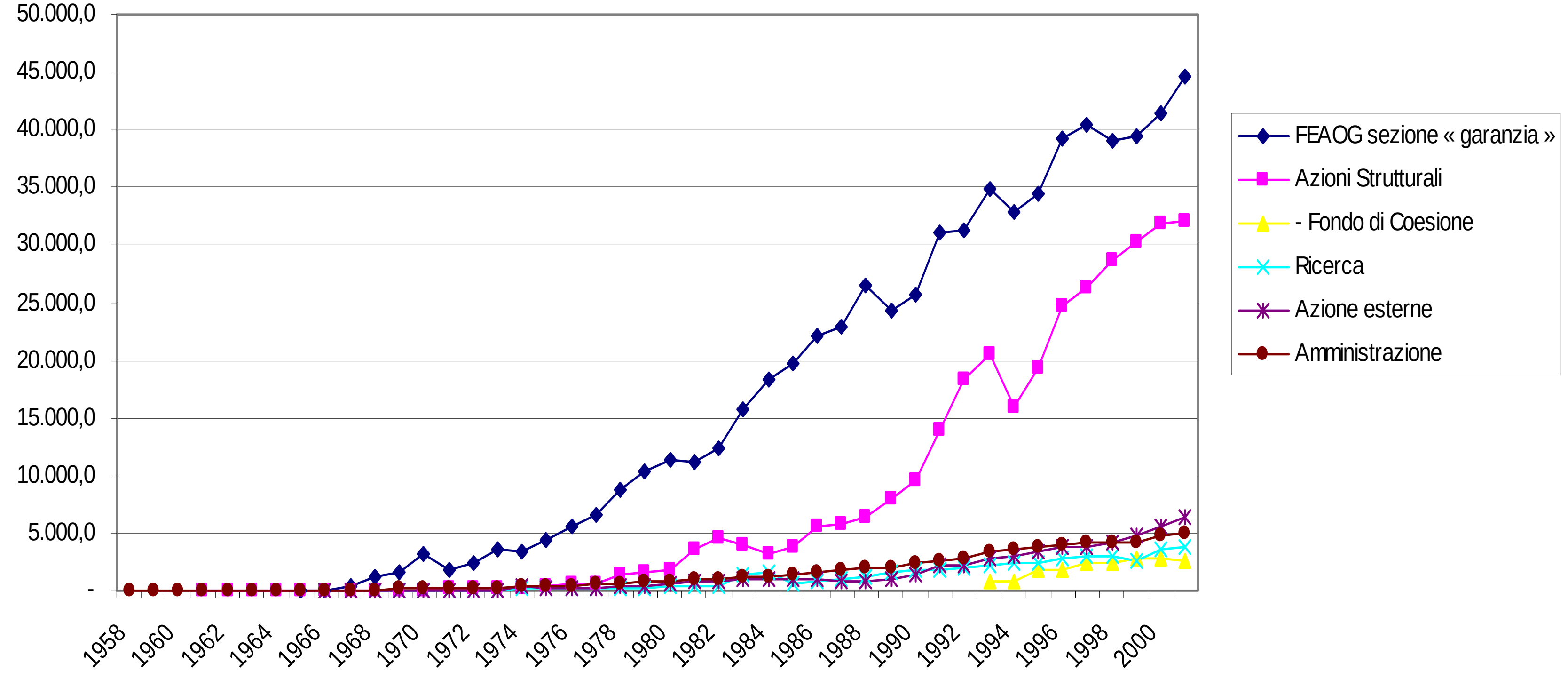
✓Structural Funds are implemented on **common rules** and **principles**;

✓ **cooperation** and **networking**.

The 1993 and 1999 reforms are more modest in scope, with the main focus on fine-tuning the new principles, particularly to improve policy effectiveness and decentralise responsibilities to Member State authorities.

Regional policy becomes, together with CAP (Common Agricultural Policy) one of the key European-level policies

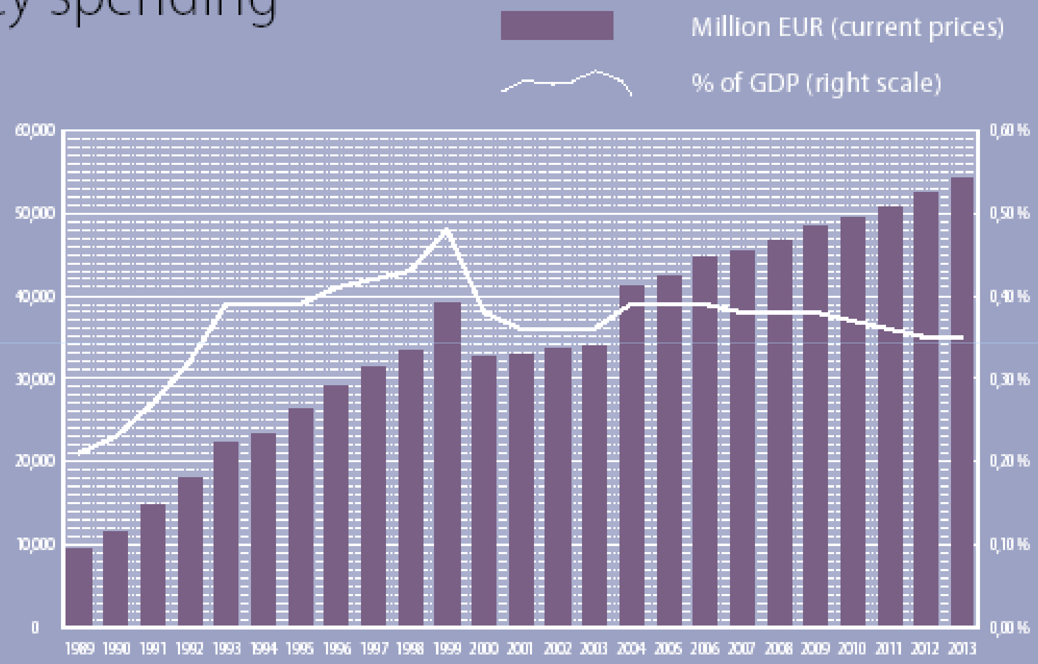
Evolution of Community expenditures 1958 - 2001 (million of euros)



Source: Vademecum di bilancio 2000

1989-2013: Cohesion Policy spending

The graph shows the development of Cohesion Policy spending between 1989 and 2013 in absolute and relative terms. While amounting to just under €10 billion in 1989, the payments from the Structural and Cohesion Funds will have increased to some €54 billion by 2013 or one third of the EU budget. In relative terms, however, the size of the funds has hovered around 0.4 % of the EU GDP since the end of the 1990s.



On May 1998 Europe’s leaders take the decision to introduce the single currency. The move to the last phase of EMU on January 1999 marks a watershed in European integration.

But in the absence of a European fiscal policy (the EU budget is only 1% of EU GDP), the monetary union can increase, again, disparities within Europe and reduce regional possibilities to respond to shock (European Commission 1990).

MONETARY UNION

CONVERGENCE OF INFLATION RATES
and
NO EXCHANGE RATE RISK

+ CAPITAL MOBILITY

+ CONCENTRATION

MONETARY UNION

IT IS NOT POSSIBLE TO USE THE EXCHANGE RATE

− REACTION TO ASYMMETRIC SHOCKS

Cost and benefit of a monetary integration

Costs

- ✓ Loss of exchange rate as adjustment mechanism
- ✓ Loss of monetary policy independence
- ✓ (Partial) loss of fiscal independence
- ✓ Conversion costs

Benefits

- ✓ Elimination of exchange rate risk
- ✓ More price transparency
- ✓ Price stability
- ✓ More trade
- ✓ Lower interest rates
- ✓ International role of the currency
- ✓ Stronger position in international policy negotiations

Between 2001 and 2003: large debate, organized by the Commission, on future priorities of European Regional Policy with Member States, regions and other players.

February 2004: Commission adopts the Communication on Financial Perspectives 2007-2013 allocating 336 billion euros to Cohesion Policy. The 3rd Cohesion Report lays down the framework for the policy's reform. This approach is largely supported by the European Parliament and a majority of Member States but partly contested by six of them.

17 December 2005: the European Council finds a compromise on the Financial Perspectives 2007-2013, which allocates 307.6 billion euros (35.7% of the total) to Cohesion Policy.

But the debate on European Regional Policy is open.

Cohesion policy is effective?

The evidence is mixed: some studies report a positive, some an insignificant and some even a negative effect.

There is not clear evidence about the impact of cohesion policy on convergence; but there is evidence on its impact on growth; and **it is not possible to say that the regional policy is uneffective** for two main reasons:

1. we don’t have a counterfactual scenario;
2. the regional policy by itself cannot determine economic convergence between regions.

Sapir Report (2003)

Give priority to growth. There is a trade-off between growth and cohesion. Europe needs more innovation. We should devote more EU resources to innovation and industrial policies, regardeless of regions.

Convergence policy should focus on low-income countries rather than low-income regions; EU convergence fund allocated to low-income countries should be used for: (*i*) improving the administrative capacity of Member States; (*ii*) investment in human and physical capital.

Sapir Report

Restructuring of the EU budget to support the growth agenda (three funds; a sharp reduction in EU agricultural expenditure; resources for growth allocated on a competitive basis; resources for convergence allocated to countries on the basis of their income level; resources for restructuring allocated to individuals anywhere in the EU based on their economic circumstances).

Lisbon

The central importance of innovation for the performance of the European economy is stated in the Lisbon Agenda 2000.

Employment rate to 70% in 2010. Youth education attainments R&D expenditures

Separating cohesion and innovation policies?

The choice is, on the contrary, to use regional policy to implement the Lisbon Strategy

From 2005 onwards the Lisbon National Reform Plans are linked to the Cohesion Policy programmes for 2007-2013.

Reducing the innovation deficit in European regions is a key task for the new cohesion policy.

Advantages in promoting innovation through cohesion policy:

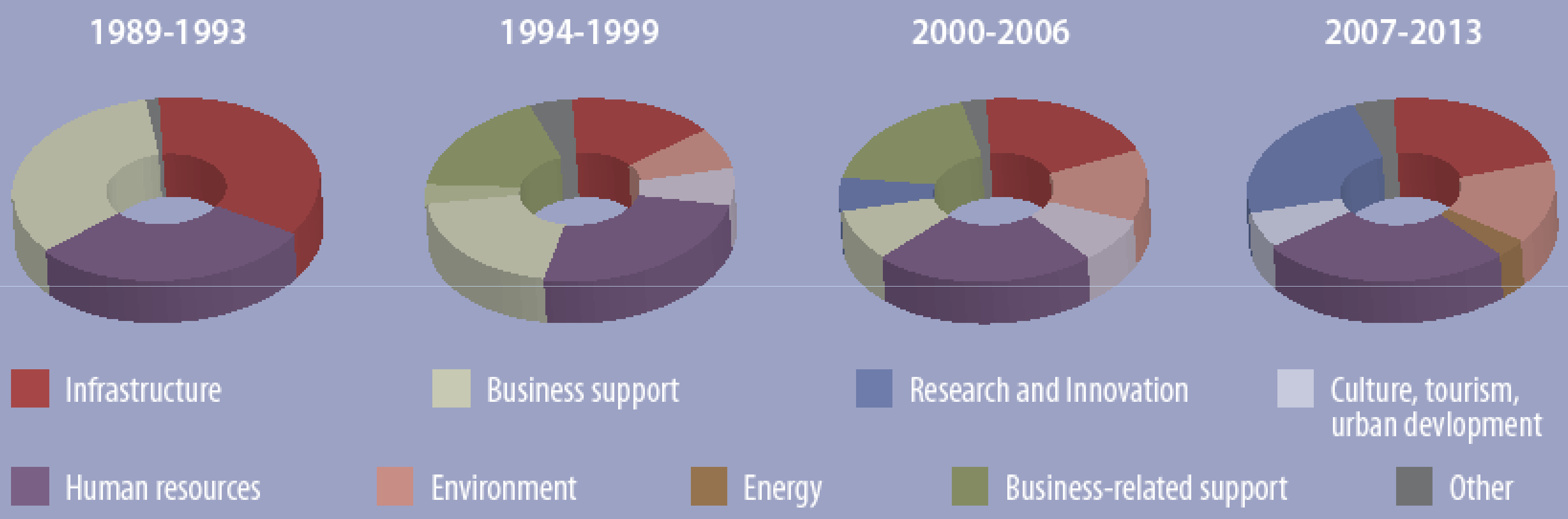
- ✓ facilitate regional and multi-level governance;
- ✓ facilitate the design and delivery of integrated innovative regional development strategies;
- ✓ concentrate finances on regions with the highest growth potential;
- ✓ increase exchange of good practices among regions.

The goals of regional policy change.

Less emphasis on incentives to business investments;

more funds to human capital, R&D and innovation.

From infrastructure to innovation



The idea is to spread innovation possibilities all over Europe.

To add new innovation poles to older ones.

To exploit human capital and scientific local knowledge in all regions to increase EU overall innovation and growth.

Research and technology development (RTD)		
Innovation and entrepreneurship expenditures		
in European regional policy 2007-13 (EU-15)		
	total amount (billion euros)	**RTD%**
Austria	1,5	77,5
Denmark	0,6	73,6
Sweden	1,9	63,8
Belgium	2,2	59,2
Finland	1,6	59,2
United Kingdom	10,6	58,0
Germany	26,3	46,9
Ireland	0,8	41,7
Netherlands	1,9	39,0
France	14,3	36,9
Portugal	21,5	30,2
Spain	35,2	30,1
Italy	28,8	29,5
Greece	20,4	11,8
Source: European Union		

Research and technology development (RTD)		
Innovation and entrepreneurship expenditures		
in European regional policy 2007-13 (EU-10)		
	total amount (billion euros)	**RTD%**
Cyprus	0,6	25,2
Estonia	3,4	21,8
Lithuania	6,7	19,1
Poland	67,3	18,8
Czech Republic	26,7	18,3
Latvia	4,6	17,9
Hungary	25,3	16,3
Slovakia	11,6	12,2
Romania	25,2	12,0
Bulgaria	6,9	11,6
Source: European Union		

It is not easy

- ✓ Remarkable differences across EU regions both in terms of knowledge potential and capability to exploit it.
- ✓ Too much emphasis on knowledge creation and research infrastructures could be ineffective;
- ✓ In the medium term, the less developed regions should pay particular attention to higher education, especially for improving their absorption capacity.

The debate is still open.

EU is performing the mid-term review of the 2007-13 budget and is already discussing of the next budget.

Which role for regional policies? Which link between regional and innovation policies?

World Bank Report (2009).

Very influencial. Against regional policy. In the opinion of the WB, regional policy reduces growth. Resources must freely concentrate to stronger places.

The issue is disparity among people NOT disparity among regions.

So <u>migration</u> is the key solution: let people go where they can earn more.

And less developed regions? They only need schools and social services.

Barca Report (2009):

There is a strong case for allocating a large share of the EU budget to a “place-based development strategy”.

The strategy must be implemented in all European regions (not only in those backward).

Cohesion policy provides the basis for this strategy, but a comprehensive reform is needed (a renewed policy concept; a concentration of priorities; a change of governance);

- no Union (with unified markets) without a development policy:
  - the EU is blamed if expectations of equal access to opportunities created by market unification and of equal chance to cope with its risks are not met
  - common market rules erode national identities and bonds and call for a “feeling of community” to be built at a supra-national level
  - it is NOT a “cost to pay” to preserve market and currency unification, BUT a complementary means to achieve the EU's aim of growth and peace
- place-based strategy objectives are the modern way to interpret the EU Treaty tasks of promoting “harmonious development” and “reducing disparities”
- a place-based strategy is the only policy model compatible with the EU’s limited democratic legitimacy

Three conditions:

- a new high-level political compromise;
- some changes should start in this programme period;
- the negotiation process must be adjusted;

The debate on the relationship between the innovation and European regional policies is open and will be at the center of political confrontation in the next years