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NOTE	
From:	Presidency
То:	The High Level Working Group on Competitiveness and Growth
Subject:	Lunch Debate: Is Europe ahead or behind in industrial innovation?
	Is a European Industrial Policy a missing link?

Delegations will find in Annex a discussion paper from the Presidency on: "Is Europe ahead or behind in industrial innovation? Is a European Industrial Policy a missing link? " in view of the Lunch Debate of the High Level Working Group on Competitiveness and Growth meeting on 26 January 2017.

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# Lunch Debate: Is Europe ahead or behind in industrial innovation?

## Is a European Industrial Policy a missing link?

#### 1. Industrial innovation: state of play, challenges, perspectives

One of the conclusions agreed by the European Council on 15 December 2016 stated: *"The European Council calls on the Council and the Commission to evaluate the impact of mainstreaming industrial policy into the EU strategic initiatives and to consider concrete actions to strengthen and modernize the industrial base of the Single Market.<sup>1</sup>" The Council Conclusions on Better Regulation<sup>2</sup> to strengthen competitiveness stresses that, when considering, developing or updating EU policy or regulatory measures, the 'Innovation Principle' should be applied. This entails taking into account the impact on research and innovation in the process of developing and reviewing regulation in all policy domains. European industry and its competitiveness have been in the spotlight in the European institutions over the past few years.* 

Great attention to industrial competitiveness has been given in the recent years and Member States have repeatedly called for this. Innovation is an important game-changer if it creates new markets and scales up quickly. This sort of innovation does not fit neatly in existing sectors but is at the interface. Market creating innovation can flourish if the right regulatory environment in place. Catalysers for innovation are: completed Single Market, better access to finance, access to competitively priced energy and raw materials, dynamic and responsive labour market inspire the much needed long-term confidence to investments in Europe.

<sup>&</sup>lt;sup>1</sup> http://www.consilium.europa.eu/en/press/press-releases/2016/12/15-euco-conclusions-final/

<sup>&</sup>lt;sup>2</sup> http://www.consilium.europa.eu/en/press/press-releases/2016/05/26-conclusions-better-regulation/

#### Facts and Figures

Industry accounts for 80% of Europe's exports and some 65 % of private sector research and development (R&D) investment takes places within the manufacturing sector. European industrial innovation needs to be broad-reaching and include: (a) the successful commercialisation of product and services innovations; (b) the industrial exploitation of innovative manufacturing technologies; and (c) innovative business models.

The European Innovation Scoreboard<sup>3</sup> of 2016 states that at a global level the EU continues to be less innovative than South Korea, the United States and Japan, but the performance gap with the last two countries has become smaller.

South Korea has managed to improve its performance at a much faster pace than the EU over the last eight years. The European Union still retains a considerable performance leadership over many other countries, including China. China is catching up, with a performance growth rate five times that of the EU.

<sup>&</sup>lt;sup>3</sup> The European Innovation Scoreboard 2016 uses 12 indicators for its international comparison which are categorised under 3 main headings, namely: enablers, firms activities and outputs. These main headings are subdivided into Human Resources, Open, excellent and attractive research systems, Finance and support, Firms investments, linkages and entrepreneurship, Intellectual assets and Economic effects. The main sources of the data are the OECD, the World Bank, Eurostat, Web of Science, the UNESCO Institute for Statistics and the United Nations. More information is found on page 31 of the European Innovation Scoreboard http://ec.europa.eu/DocsRoom/documents/18062.

The overarching question being *Thinking about the commercialisation of your country's innovative goods or services since January 2012, have any of the following been a major problem, a minor problem or not a problem at all?* The micro questions asked covered: (a) Market dominated by established competitors; (b) Lack of financial resources; (c) Cost or complexity of meeting regulations or standards; (d) Lack of human resources; (e) Administrative or legal issues; (f) Low demand for innovative goods or services; (g) Lack of marketing expertise; (h) Weak distribution channels; (i) Finding or using new technologies: and (j) Difficulties in maintaining intellectual property rights. The results of the study are illustrated graphically below:

The main finds of companies that introduced at least one innovative good or service since 2012 to commercialise their innovation (s) ranged widely. The findings being: (a) 65% of the companies mentioned that the market was dominated by established competitors; (b) 60% faced a problem of a lack of financial resources; (c) 57% has a problem of meeting regulatory and standardization costs. In fact, more than one quarter stated that each of these issues was a major problem; (d) 40% lacked human resources and there were administrative and legal issues; (e) 43% registered a low demand for innovative goods or services; (f) 39% registered lack of marketing expertise; (g) 36% registered weak distribution channels; (h) 33% flagged a concern with finding and using new technologies and (i) finally, just one in five (that is 21%) companies had problems maintaining their intellectual property rights.

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<sup>&</sup>lt;sup>4</sup> Base: Those companies that have introduced innovative goods or services since January 2012 (n = 7 961, 61% of total base).

#### 2. Questions to steer the discussion at the High Level Group

Given the importance of innovation for European industrial competitiveness and the economy and given the challenges coming from third countries, both the European Union and its Member States are looking into ways of spear-heading their position in this area. The aim of the discussion in the HLG is to have an exchange of views industrial innovation in the context of the ongoing debate on a European industrial policy.

#### *Objective, scope and perspective*

Industry is of critical importance for growth and jobs in Europe and contributes substantially to exports and innovation. It also plays an important role in dealing with societal challenges. Competitiveness factors in both costs and innovation. Minimising costs for European industry and safeguarding a level playing field with other economies can be seen as an important goal. In some areas reducing costs is not controversial, as minimizing the unnecessary cost of regulation has clearly a positive influence. In other areas reducing costs can be more complicated since they may be harder to change (for instance the impact of shale gas on energy costs in the US), or because reducing cost has a trade off in the realisation of other policy objectives (for instance on climate or health). It is on the other hand little disputed that long term competitiveness of European industry will depend on its ability to innovate, not only to reduce costs but also to develop new products and services. It is important to make clear which of these possible goals European industrial policy should pursue.

Services and industry are increasingly intertwined in global value chains, with value added in industry often being in part-servitised, and the competitiveness of industry being critically dependent on the supply of high value services. For an effective European industrial policy, clarity over the scope is important. Currently, the cornerstone of European industrial policy is the mainstreaming of industrial competitiveness across all policy areas.

Such a horizontal approach to industrial policy aims to ensure that effects on competitiveness of all policy measures are duly taken into account. The recent European Council conclusions<sup>5</sup> called for an evaluation of the results of Industrial policy. Characteristics of sectors or technologies may require more specific attention, for instance through sectorial action plans aimed at delivering concrete results for individual sectors.

Question 1: What should be the scope and objectives of European industrial policy? Should European industrial policy be primarily horizontal and generic, or should it also include sectorial and more specific actions?

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<sup>&</sup>lt;sup>5</sup> http://www.consilium.europa.eu/en/press/press-releases/2016/12/15-euco-conclusions-final/

#### Industrial innovation

It is essential for European industry to be well positioned in the value chains, to ensure that high value jobs and activities for which Europe holds a competitiveness edge can flourish. Such a strategy for industry focuses on open global markets whilst ensuring a level playing field, and on a deepening of the Single Market for both goods and services. To boost innovation investment is needed both at a national and a pan-European level. Investment should focus on both research and on creating value through innovation, whilst considering large scale demonstration projects for new technologies to deal with societal and relevant initiatives of common European interest (so called "lighthouse projects").

For a vibrant and competitive European industry, industrial innovation is essential. Just competing on costs alone typically leads to a race to the bottom. Value added would then be reduced, means for reinvestment would be scant, and due to typically higher factor prices in Europe, European industries would lose competitive battles with competitors from outside the EU. It therefore is essential that the EU creates the best possible conditions for industry to innovate, not just for competitiveness reasons but also to deal with global societal challenges.

European industry operates in global value chains, where competitiveness is the result of the interaction between firms within and between sectors (including between manufacturing and services). To accelerate the modernisation of Europe's industry, the uptake of product and service innovations, the use of innovative manufacturing technologies and the introduction of new business models are all necessary.

Question 2: What are the main barriers to European industrial innovation? What policies, incentives and best practices are being adopted by Member States to address these barriers?

### Conference on European Industrial Competitiveness

During the last COMPET Council under the SK Presidency in November 2016, the Commission informed the Member States that they will be organising a conference on European Industrial competitiveness in March 2017.

#### Question 3: What could be the Member States' contribution to the European

Industry Conference being organized by the Commission?

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