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NOTE

From: European Commission
To: The High Level Working Group on Competitiveness and Growth
Subject: Competitiveness check-up on regional dimension and inclusiveness

Delegations will find in Annex a Commission discussion paper on a competitiveness check-up on regional dimension and inclusiveness, in view of the meeting of the High Level Working Group on Competitiveness and Growth on 7 September 2018.

A regional dimension for Competitiveness Policy?

Competitiveness check-ups help us to get new insights into the evolution and drivers of competitiveness by approaching it from new or different perspectives. For instance, by looking at the lifecycle and demise of firms (and not just the creation of start-ups) we learned about the importance of policies for scaling-up firms. Value chain analysis provided a new perspective enhancing the importance of competitiveness in services by showing us that most of the value added incorporated in our exports of manufactured goods comes from the services sectors.

In this September HLG meeting, we propose to look into the importance of the regional dimension in our work on competitiveness. Why?

The EU has been dubbed a “convergence machine”¹ with convergence in per capita income among EU Member States showing again a positive trend after the hard brake of the long recession. Different drivers have been operating at different points in time shaping this convergence process. At present, the catching up by Member States that joined the EU in the last 15 years is the main driver. Furthermore, between 2000 and 2015, regional inequalities in the EU have been reduced by around 14 %. On the other hand, within Member States, the gap between leading (often, the capital city) and lagging regions has broadened in several Member States, including in those Member States that joined since 2004².

Why are these findings relevant to design competitiveness enhancing policies?

¹, Indermit S.; Raiser, Martin. 2012. Golden Growth : restoring the lustre of the European economic model (Vol. 2) : Main report (English). Europe and Central Asia Studies. Washington DC ; World Bank . The matter was also revisited in March 2018 by the World Bank: Ridao-Cano, Cristobal; Bodewig, Christian. 2018. Growing United : Upgrading Europe's Convergence Machine. World Bank, Washington, DC. © World Bank. <https://openknowledge.worldbank.org/handle/10986/29448>Gill

² See 2017 Seventh Cohesion Report - http://ec.europa.eu/regional_policy/en/information/cohesion-report/

The rationale for convergence policies

Reducing regional economic, social and territorial disparities is as a key objective of the Union. The existence of large disparities is a clear signal that some regions and groups of citizens are not benefiting from EU integration. Social and political arguments plead in favour of taking into account the uneven distribution, rightly or wrongly perceived, of the costs and benefits of economic growth and integration across regions³. Equity and fairness considerations have often been the main justification for policies to foster convergence, especially since the Single Market Act, and they remain extremely pertinent today. Political developments, such as the rise of populism movement across Europe, show clearly the importance of reducing regional divides across EU regions and fostering income convergence, in order to raise political support for competitiveness policies.

One way to structurally foster convergence across regions is to reduce the productivity gap between frontier and lagging regions. Nowadays, the identification of the sustainable and inclusive growth objective has replaced the approach based on seeking trade-offs between efficiency and equity in economic growth. It is important to foster convergence among regions in Member States and within the EU as a means to strengthen sustainability and long-term growth and render the EU more stable and resilient to shocks.⁴

³ The reflection paper on harnessing globalisation stressed that the benefits of globalisation are unevenly spread among people and regions, some of which are less adaptable to change and competition than others. https://ec.europa.eu/commission/sites/beta-political/files/reflection-paper-globalisation_en.pdf. See also: Ridao-Cano, Cristobal; Bodewig, Christian. 2018. Growing United : Upgrading Europe's Convergence Machine. World Bank, Washington, DC. © World Bank.

<https://openknowledge.worldbank.org/handle/10986/29448Gill>

⁴ See Seventh Cohesion report and the discussion in Chapter 1 on economic Cohesion : http://ec.europa.eu/regional_policy/sources/docoffic/official/reports/cohesion7/7cr.pdf

Competitiveness has been, for over one decade, part of the list of social, economic and political reasons justifying convergence efforts with the alignment of the 2007-2013 programmes. In the programming period 2014-2020, competitiveness clearly appears amongst the key priorities for the programming of the ESIF, when competitiveness related investment themes were prioritised under “thematic concentration” rules.

Economic evidence has revealed the importance of regional convergence as a factor contributing to overall increasing productivity growth and competitiveness. There is a circular line of causation linking economic convergence and competitiveness. Productivity growth is at the centre of that circle.

- Productivity growth is the main determinant of competitiveness in the long term. It ensures sustained income and wage growth. In the EU, productivity in the most advanced regions is growing faster than in the median regions. If this trend continues, there will be an increasing gap in income and wages between those frontier regions and the rest. In this context, productivity growth is relevant for regional convergence and cohesion
- In turn, convergence patterns have an impact on productivity growth - and hence competitiveness.
- Productivity growth in a limited number of productivity-frontier regions (usually the capital-city region) has a very significant importance on the productivity of growth of the whole country. However, productivity growth in Member States will be higher and more robust, if other regions tend to converge towards the higher productivity growth rates of the frontier regions. In fact, the contribution of the laggard regions to the productivity growth tends to be higher in those countries where there is regional convergence.

This circular relationship underlines the importance of regional convergence within countries for the overall productivity performance of our Member States. This calls for increased attention to convergence in the monitoring of competitiveness and the design competitiveness policy.

Policy considerations

The divide between regions still persists in terms of per capita income but also in terms of economic performance and competitiveness. Weaknesses in the diffusion of new technologies explain a large part of Europe's slow aggregate productivity growth.⁵ The divide between more technologically advanced regions and those that are less advanced risks widening, unless governments invest in education, equip their citizens with the right skills, encourage innovation, ensure fair competition and regulate smartly where needed.

The productivity performance of Member States could be improved if benefits of innovative technologies and digitalisation in particular could spread across regions. Additional efforts are thus needed to accelerate the uptake of innovation in less developed regions and in more traditional sectors. Investments need to be made more efficient, effective and better tailored to regional and local needs, as it is already the case in Cohesion Policy.

⁵ Science Research and Innovation Performance of the EU 2018" (https://ec.europa.eu/info/support-policy-making-eu-and-horizon-2020-associated-countries/srip-report_en)

EU funding has been instrumental in developing regional innovation eco-systems that give Small and Medium Enterprises easy access to infrastructure and expertise to experiment with new technologies. To support these efforts, Smart Specialisation Strategies are key to ensuring that all EU regions can harness their potential and succeed with innovation-based industrial transition.⁶

Regional authorities frequently have a major influence on policy choices and framework conditions. Regional and local authorities are often responsible for decisions affecting innovation ecosystem, investments in infrastructures, role of training and education institutions, innovation, granting different types of permits and other administrative and policy functions configuring the environment business are confronted with. These are all factors having a considerable impact on productivity growth and competitiveness.

The important role that regional authorities play in the implementation of reforms and policies having an impact on competitiveness must also be born in mind at EU level when formulating recommendations to Member States at EU level. Taking into account the regional dimension will be helpful to provide better-targeted recommendations to Member States. The effectiveness of structural reform efforts to increase productivity and competitiveness could be limited if convergence issues are neglected. Cohesion Policy will therefore need to be more closely linked to the European Semester in the future.

⁶ See: Commission Communication on Strengthening Innovation in Europe's Regions: Strategies for resilient, inclusive and sustainable growth, COM(2017)376 final. The concept of Smart Specialisation has been strengthened in the proposals for the next European Regional Development Fund Regulation (See https://ec.europa.eu/commission/publications/regional-development-and-cohesion_en). The Entrepreneurial Discovery Process that underpins the identification of the specific priorities and brings together business, academia, education, civil society and public sector, should become permanent. Digitalisation and skills aspects will need to be taken aboard in the strategies. The focus on research and innovation will be complemented by a strong industrial transition dimension. The ERDF investments should thus focus on enabling SMEs to reap the benefits of globalisation, circular and low-carbon economy, digitisation, and advanced technologies.

Consistency and coordination across different administrations are important to ensure that national objectives of sustainable growth can be compatible with specialisation choices made at regional level, but this cannot be taken for granted. Some cases have been identified where difficulties of coordination between national and regional authorities have hampered progress in the reform process. Good coordination between administrations is therefore critical to ensure progress in the implementation of reforms.

Finally, in the wake of the launching of a new programming period under the new Multiannual Financial Framework, these considerations become particularly relevant given the new role that structural reforms, institutional issues and EU supported investments will have to play in the future.

The Commission is already anticipating these changes and increasing attention is already being paid to the regional and territorial dimension in the Semester but considerable work remains to be done.

Questions:

- 1. What are Member States currently doing for the coordination of competitiveness policies at the different levels of the administration?*
- 2. How are the regional or territorial dimensions taken into account in the definition of competitiveness policy in your Member State?*
- 3. How could this regional dimension be incorporated in a useful way in our work on competitiveness issues at EU level?*