

# Innovation policy at regional level

## Craft and SME priorities for the new Innovation Strategy

Discussion paper from UEAPME secretariat

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### 1. Introduction

The EUROPE 2020 document of the European Commission put a focus on innovation as one of the factors that should help Europe to recover from the economic crisis and face the societal challenges like globalisation, pressure on resources, climate change, ageing society etc. With the “Innovation Union” R&D and innovation policy re-focuses on major challenges, while closing the gap between science and market to turn inventions into products. This approach is highly welcomed by UEAPME.

Innovation is a decisive factor for the competitiveness and growth of businesses and regions. For the period 2007-2013 all Member States have devoted a significant amount of their total financial allocations to R&D, innovation and development of a knowledge-based economy. The cohesion policy has become a major source of European support for this field, in addition to the budget of both FP7 and CIP. While CIP and FP7 are centrally managed by the Commission the responsibility for the implementation of Structural Funds lies with national and regional authorities. It is important to identify the decision-making level which is most effective and to foster effective synergies and to identify and promote the most suitable means at European level of supporting local and regional investment in innovation. However, it is up to the regions themselves to define their proper innovation strategy adapted to their respective circumstances.

Considering the fact that 99% of the businesses in the EU are SMEs it is clear that they will play a crucial role in overcoming the economic crisis and creating an “Innovation Union”. A survey in Germany<sup>1</sup> has shown that already during the economic crisis a large number of SMEs increase their innovation activities. The difficult economic situation provokes many businesses to question established things and open up the own technological basis for further development, e.g. in order to find their way into new markets. It is clear that all kinds and sizes of enterprises can innovate and that it is necessary to focus on innovation in all SMEs not only in high-tech SMEs.

### 2. Broad Definition of Innovation

Properly defining innovation is a precondition to promoting innovation. Innovation must include all forms of innovation and all phases of the innovation process. Innovation in a broader sense is not only R&D and high-tech. The “High-Tech Sector” counts even in highly developed economies for about 3% of the GDP. That means 97% of all economic activities and most of the innovative processes in Europe happened in sectors defined by the OECD as “Mid-Tech” or “Low-Tech”. However, when measuring innovation it is difficult to formulate realistic and

<sup>1</sup> 1: DIHK Umfrage “Innovationsverhalten deutscher Unternehmen in der Krise – erstaunlich offensiv. (2009)  
[http://www.dihk.de/inhalt/download/innovation\\_in\\_der\\_krise.pdf](http://www.dihk.de/inhalt/download/innovation_in_der_krise.pdf);  
[http://www.dihk.de/inhalt/download/innovation\\_in\\_der\\_krise\\_engl.pdf](http://www.dihk.de/inhalt/download/innovation_in_der_krise_engl.pdf) (English summary)

meaningful quantitative and qualitative targets. The indicators used so far have put too much emphasis on the input and not enough on the output. Often the evaluation and reference documents also do not include all sizes and types of enterprises.

A supportive policy needs a quite broad approach to exploit the capacity of SMEs to innovate and become more competitive, which includes the development of new products and services, the introduction of new production processes for goods and services as well as the acquisition of new markets.

### **3. Broad Definition of SME, including craft enterprises**

The overwhelming majority of SMEs (above 92%) are micro enterprises with less than 10 employees and in some countries they include a huge number of craft type enterprises. Also these companies have the potential to innovate, if innovation is seen in a broad definition as described above. Policy maker, especially at regional level have to recognise also this potential and to react on the fact that these type of enterprises proceeding innovation in a different way and have different needs as regards a favourable policy framework and support measures.

### **4. Innovation - Strengths and weaknesses of SMEs**

The specific way in which SMEs perform innovation has to be recognised when designing policy. Innovation processes in crafts and SMEs in Europe are characterised more by on-going permanent processes and less by linear technical-driven inventions. In most of the SMEs the innovation process is based on available technologies, which are used in a new and sophisticated way; based on the experiences and the knowledge of persons in and around the company; supported by highly qualified employees and the entrepreneurial spirit of the business owner; based on highly flexible, but long lasting, customer and supplier relations and supported by existing networks and clusters.

A number of surveys have shown that SMEs have certain weaknesses when it comes to innovation, but, they also have several considerable advantages, e.g. high motivation if the manager is also the owner, flexible, non hierarchic structures, fast decision-making processes, flexibility of production, proximity to the market, direct contact to customers and flexibility to react on market and customers' demands (demand driven innovation) as well as fast adaptation to changes in the business environment.

In order to exploit their full innovation potential SMEs need the right framework conditions as already set out in the Small Business Act. The capacity of SMEs to innovate depends mainly on:

- well qualified entrepreneurs and staff members
- necessary capacities to manage innovation processes
- access to existing technologies
- access to financial means, which can carry some risks
- access to necessary infrastructure (technical facilities, training centres, ...)
- regulatory framework for innovation (subsidies, taxation, intellectual property rights, standards, etc)
- existence of networks and clusters
- existence of support structures

The factors listed above are also reflected in the main problems SMEs have to exploit their capacity to innovate:

- SMEs report shortage of qualified personal they need and don't have the resources to qualify their staff themselves.
- SME owner often have difficulties to manage innovation processes, especially if bigger changes in technologies and production process are involved, and would need adequate support services.
- The main barriers as regards access to existing technologies seem to be the high information costs for SMEs and the expensive and complicate patent systems.
- SMEs, especially on the continent, depend to a large extent on debt financing, but more and more of them complain that on the one hand banks are less and less able or willing to finance riskier projects, like innovation and start-ups, with credits and loans and on the other, the market does not provide sufficient equity finance at all and especially not below 2 Million Euro, which would be needed by most of the SMEs.

At the same time, SMEs and financial intermediaries complain that European financial support instruments (CIP, FP7 and Structural Funds) are no accessible for SMEs or not adjusted to their needs.

## 5. Coordination between the Different Levels

In order to solve these problems and create the right framework conditions and synergies between the European, national and regional innovation policies it is necessary to have a better coordination between the innovation policies at different levels. An administrative culture that promotes cross-sectoral co-operation and continuous dialogue between different policy communities contributes to the strengthening of policy coherence.

Moreover, a coordinated approach in innovation policy needs the involvement of all stakeholders, including representative Craft and SME associations, at all levels. Political guidelines, priorities and actions have to be decided and applied in an open and transparent process including the business community.

It is also important to clearly allocate the responsibilities to the competent levels. Initiatives at European level should focus on a clear European added value. Other forms of innovation are most effectively addressed at regional level with the proximity of actors, such as universities, private and public research organisations or industry, promoting partnerships in knowledge transfer, and the exchange of good practices between regions.

### Defining an Innovation Strategy for a Region

Investment in innovation, education and resource-efficient technologies, will benefit traditional sectors and rural areas as much as it will high-skill service economies, and will therefore reinforce economic, social and territorial cohesion. The cities and regions should pursue smart and sustainable specialisation by defining a few innovation priorities based on the EU objectives and on their needs as their Regional Innovation Strategies. These priorities have to be identified with all social and economic partners. Coherent policy portfolios of policy instruments have to take into account both regional situations and specific SME needs in terms of innovation. The regions should always keep in mind their strength in order to make best use of the regions comparative advantage in a global competition. There is no "one size fits all" solution. Regional differences in innovation capabilities call for a tailored mix of policy instruments.

## 6. Concrete Measures

Business Clusters and Networks for example encourage innovation in SMEs. The existence and the development of business clusters and networks with specific competences create positive spill-over effects for innovation, especially for smaller enterprises. The development of such clusters and networks should be managed by regional institutions and publicly supported by related training facilities. In areas that the different Member States cannot manage on their own or that have a European dimension (e.g. energy, climate, environment, space technology) the Commission should bundle her resources and look for European wide solutions. However, any support for such networks and clusters has to be designed in a way that also SMEs can profit from them.

The added value of cohesion policy, particularly to small and medium-sized enterprises, could be in offering easily accessible support and the necessary infrastructure as well as providing improved access to research and the transfer of technology and innovation, oriented towards practical application. The existence of high quality innovation support services is especially crucial for SMEs to increase their innovation capacity and has to become an integrated part of each regional innovation strategy. For example, accompanying innovative projects through intermediary organisations could offer advice and support for SMEs by specialised advisers, reinforcement the cooperation between the different actors at regional, national and EU level (SMEs, universities and research centres etc.) and encourage an innovative culture in SMEs. Examples can be found for instance in France<sup>2</sup>.

To tackle the problem of access to finance the programmes have to be reviewed to better support the new need of SMEs for risk financing. The existing financial support instruments at European level have to be streamlined and better coordinated. Furthermore, the development of new financial instruments, which are able to carry risks better like Mezzanine Instruments, will be necessary to ensure financing of innovation in future. In addition, any financial instrument for SMEs has to be adapted to their needs and must be made attractive for SMEs and intermediaries. Instruments which are not taken-up by the market are useless and a waste of money. In the area of State aid regulation, the new framework for R&D and Innovation from 2006 includes SME relevant aspects of innovation and the integration of the SME relevant part of the framework into the General Block Exemption Regulation reduced also the administrative burden for State aid provider.

In general, European Programmes have to be simplified as far as possible and may create better results, if they are used to improve the innovative environment for SMEs (training centres, laboratories, incubators, etc.) rather than to finance single small innovation projects. In this context it is important that the regions are better informed which possibilities and chances are offered by the programmes. This is a fundamental prerequisite to define their own proper innovation strategy.

## 7. Main Policy Recommendations

To conclude we would like to summarise the main policy recommendations that should be taken into consideration to exploit SMEs capacity to innovate:

- Innovation policy has many dimensions and the competences are divided between European, national, regional and even local levels. Therefore, a clear allocation of responsibilities in line with the subsidiarity principle is necessary in order to foster competition between “innovative regions” and to formulate European policies, which have a clear added value.

<sup>2</sup> APCM « Eléments sur l'utilisation des fonds structurels dans le financement des projets d'innovation au sein du réseau des chambres de métiers et de l'artisanat »

- The existing financial support instruments at European level have to be streamlined and better coordinated. Furthermore, the development of new financial instruments, which are able to carry risks better like Mezzanine Instruments, will be necessary to ensure financing of innovation in future.
- Furthermore, any financial instrument for SMEs has to be adapted to their needs and must be made attractive for SMEs and intermediaries.
- In the area of State aid regulation, the new framework for R&D and Innovation from 2006 includes SME relevant aspects of innovation and the integration of the SME relevant part of the framework into the General Block Exemption Regulation reduced also the administrative burden for State aid provider. Now it has to be made sure that these extended possibilities are used.
- The existence of high quality innovation support services is especially crucial for SMEs to increase their innovation capacity and has to become an integrated part of each regional innovation strategy. In this context, intermediary organisations have to play a crucial role in providing innovation advisors, mediators etc.
- Networks and clusters create a very fruitful environment for innovation in SMEs. Any support for such networks and clusters has to be designed in a way that also SMEs can profit from them.
- European Programmes, which are by nature complex and administrative burdensome, have to be simplified as far as possible and may often create better results, if they are used to improve the innovative environment for SMEs (training centres, laboratories, incubators, etc.).
- All relevant stakeholders, including SME representatives, have to be involved in the development of innovation strategies and support instruments at all levels.
- All relevant stakeholders, especially the decision-makers at regional level, need to be fully informed about the possibilities they have within the existing programmes. Only when they know what is possible they can define the tailor-made innovation strategy for their region.

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