STEELACTION

CONSULTATION STATE AID FOR INNOVATION

SteelAction is a network of 18 local authorities, established at the height of the 1993 steel crisis in order to seek 'A Fair Deal for UK Steel'. Its membership represents existing and former steel making communities throughout the UK. It also forms part of the Alliance for Regional Aid, which brings together three local authority associations (SteelAction, Coal Field Communities Campaign, Leading Action for Textiles, Clothing and Footwear) for the purpose of securing the regeneration of the UK's traditional industrial areas.

SteelAction has achieved a number of important successes but is perhaps best known for its high profile initiative to tackle illegal subsidies paid within the European Union's steel industry and the winning of a ten-fold increase in spending for the UK from the EU'S Resider II steel area regeneration programme. It was also instrumental in establishing Steel Partnership Training (SPT), an initiative aimed at retraining former and existing steel workers.

The association works in close collaboration with the main steel unions, the UK Steel Association and the Corus Group, but is also able to pursue an independent line in support of steel community interests.

Although we have a special interest in helping to secure a viable interest for the steel industry and the communities which are still dependent upon it, we are acutely aware of the need to diversify and strengthen local economies through the development of a wider range of high value-added activities. This is essential to the process of maintaining a competitive edge whilst at the same time reducing the vulnerability of communities to the external economic shocks often associated with over-dependence on a single industry. No less important is our commitment to ensure that former steel communities are also fully supported during the inevitable transitions which they are having to make in developing new and sustainable economies. Innovation is a key element in this transition and it is for this reason that we welcome the Commission's report on State Aid for Innovation, our response to which is set out below.

- In overall terms there are several key issues which any revisions to the state aid rules need to address if they are to benefit the older industrial regions. These include the following: the need to close the regional R&D gap with higher 'top-rates' of intervention for companies in these areas; affording a higher priority to assisting the development of skills and the capacity to innovate; extending eligibility to the service sector to reflect the structure of the economy; the need to target support towards SMEs; placing greater emphasis on supporting networks and the sharing of knowledge; provision of support for innovative actions leading to sustainable environmental outputs.

- Regarding the regional R&D gap, DTI data shows that employment and expenditure on this activity is heavily concentrated in the South East and Eastern regions, which together account for nearly half of the UK total. R&D expenditure per head in these regions is higher than Wales, Yorkshire and Humberside and the North East by a factor of ten. Overall, there is little difference in innovation rates across the regions against more broadly defined measures such as new processes and products and the main differences arise from industrial location effects i.e. sectors with high R&D are poorly represented in the regions outside of the SE. **In this respect the state aid rules for innovation need to reinforce the wider regional guidelines aimed at addressing market failures in the poorer regions. This could be achieved through permitting higher grant rates for companies in such regions with further enhancements for those in the under-represented sectors.**

- Recent DTI evidence seems to suggest that, in general, access to finance for innovation is not a major issue given the well-developed capital markets in the UK. In fact the primary reason for low levels of innovative activity is seen as stemming from the limited capacity of many companies to absorb knowledge and new ideas – 20% of the productivity gap can be attributed to low skills whilst shortages of technical and management skills place severe constraints on the ability of enterprises to introduce new products and processes. In contrast the UK science and technology base in universities is well developed and compares well with its major competitors, but low levels of knowledge transfer can be attributed for the large part to the capacity of companies to innovate. **The suggested emphasis in the consultation paper on assistance for recruiting researchers and engineers and facilitating personnel exchanges is therefore welcome, but eligible activates need to be extended to support the wider development of the work force in those companies with a demonstrable commitment to innovate.**

- Traditionally, policies aimed at supporting innovation have concentrated on the manufacturing sector, which though well-represented in the regions outside of the SE is declining in its share of total economic output. In many areas it is also characterized by firms which are locked into the low value-added, low skills, low innovation cycle. Whilst helping companies to break out of this cycle remains an imperative, the state aid rules also need to recognize that the service sector now accounts for 70% of output in the UK. Although the service sector is less likely to undertake R&D there is evidence of increasing activity in areas such as IT, supply chain management and e commerce. **Again however, the service sector is under represented in the poorer regions of the UK and extending eligibility for innovation support in this sector would benefit these areas on two levels; firstly, it would help to attract and retain the higher value service industries and, secondly, it would assist in expanding the overall volume of innovative/R&D activity.**

- SMEs are now accounting for a significant proportion of job growth in the EU and their contribution to diversifying the employment base gives added strength and sustainability to local, regional and national economies. Evidence suggests that schemes that target support for innovative SMEs result in greater additionality than that directed towards larger enterprises**. In principle,**

therefore, the eligibility criteria for state aid should be based on targeted beneficiaries where there is an identifiable market failure in the SME sector.

- Networks and knowledge sharing partnerships can have an important role to play in helping to stimulate innovation and the spread of good practice. In the UK, their impact appears to be limited because they are often of insufficient scale and there are large variations between the regions, the latter being attributed to factors such as the relative absence of head quarter functions and over concentration on those sectors where there are fewer opportunities for innovation. Data also shows that UK firms are more likely to collaborate with customers and others in the supply chain rather than concentrate on sources of knowledge within their own enterprise. **The guidelines should, therefore, enable state aid to be provided for the purpose of initiating innovation networks which can play a pivotal role in encouraging companies to access and develop innovative processes and products. On the related issue of clusters, care should be taken to ensure that state aid is used address market failures in those regions where their formation requires an initial stimulus, rather than reinforcing well-established concentrations**.
- With the increasing attention being placed on environmentally sustainable technologies and the particular emphasis on the need for low carbon economies to combat climate change, there is an obvious role for support to be targeted on those innovative processes and products which are likely to result in long term benefits to the environment. As an emerging sector with global market potential, environmentally-related technologies and processes are of particular interest to those regions which are still making the transformation from economies based on traditional heavy industries and manufacturing to those encompassing a broader range of new technologies. **The state aid rules should therefore recognize and support the development of this potential by ensuring that innovative actions with clear environmental outputs are priority areas for support.**