
report title

SBAC response on EU
State Aid for Innovation

ref

SBAC-COM-PPR-05-
1024 (1.0)

issue

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date

21/11/05

Introduction, unique characteristics of the aerospace sector

1. SBAC is the national trade association representing over 2,500 companies throughout the UK, supplying the civil air transport, aerospace defence, homeland security and space markets operating in the UK economy.
2. The aerospace sector has many unique characteristics that distinguish it from the general business sector. The nature of innovation and research projects within the aerospace sector are large in scale, highly technical and few in number. Projects have very long lead times and a research and development programme may not lead to an innovation that is marketable for a considerable period. These factors affect the ability of the sector to attract investment from the commercial markets particularly for research and development programmes.
3. The aerospace sector faces unique challenges in attracting finance and has been supported by governments through launch investment and research and development programmes. As a highly technical sector committed to innovation and delivering new technology that delivers greater environmental performance, state aid support will continue to remain important to the sector for the foreseeable future.
4. Extensive research has been conducted into the economic benefits of the aerospace sector. Of particular note is the extensive benefits of new spill-over technologies that cannot be captured by the sector for example engine development, composites, wind-turbines and high-speed yachts. Research undertaken by Oxford Economic Forecasting in this area demonstrates the significant high social return from investment in aerospace research and development.

Question 1

5. SBAC supports the Commission's proposal to incorporate innovation rules into other guidelines; this removes the need to develop a separate framework for state aid for innovation.

Question 4 and 12

The pattern of research and development within the aerospace sector

6. Aerospace is one of the few globally competitive and growth areas of UK manufacturing. The sector is diverse comprising a supply chain of SMEs that develop components, who supply mid-range companies making equipment, such as landing gear, and who in turn supply large multi-national companies who make visible end-products such as the Airbus A380 or Eurofighter. 70 per cent of SME aerospace sales are to larger companies within the UK aerospace sector.
7. Research and development leading to innovation within the sector tends to be driven by large scale investment. There are opportunities for SMEs to be involved in large-scale projects but the general pattern is that they are driven by a small number of prime contractors. Recent applications to develop an environmentally friendly engine and a project to develop electrical landing gear, if successful, will contribute to reducing the weight of the aircraft, thereby reducing environmental emissions through achieving greater fuel efficiency are examples of such projects.

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8. The sector works as a unit, to ensure the competitiveness of UK industry, and companies in the sector work together on initiatives to improve productivity through the promotion and development of lean processes and techniques, as well as industry initiatives to tackle skills shortages.
9. SBAC supports the two overriding principles that the Commission has set out, under which innovation activities may be funded:
 1. **Activities that support risk-taking and experimentation and help bridge the gap between technological knowledge and the market**
 2. **Activities (business services and infrastructure) which improve the general business environment for innovation.**

The need for an additional exemption for a clearly defined national programme of investment

10. In its proposals the Commission has made a clear distinction between state aid support for SME's and large companies. SBAC appreciates the reasoning behind this approach, but is concerned that without modification this could lead to unintended consequences that are to the detriment of the UK aerospace industry.
11. SBAC's concern is that the principles governing the control of state aid could prejudice government and or regional bodies against supporting aerospace applications. Under the proposals, there would be a marked difference in the complexity of processing support for larger scale projects, as they would require specific approval by the Commission. This is in contrast to support for SMEs which requires no notification, this exemption in isolation could make a considerable difference to the availability of funding for large-scale aerospace research and development projects. Such an outcome would have an adverse impact for the sector that could significantly affect aerospace SMEs, because of the pattern of research and development investment is driven by large-scale projects.
12. SBAC believes that the state aid rules could themselves distort aid provision if they are not adjusted to respond to the unique characteristics of the aerospace sector. In the UK considerable government investment in research and development is channelled through regional development agencies. The practical implications of the Commission's proposals of a blanket exemption for SMEs but full notification for larger applications will provide a disincentive for these bodies to support aerospace applications. The process that state aid rules leads to is likely to have some bearing on the investment decisions taken by regional bodies and governments who will have fewer resources and less expertise in managing this type of complex application process.
13. To prevent this unintended consequence, SBAC proposes that the Commission should include an additional block exemption for any project that is part of a clearly defined investment programme as part of a national or European strategy to help secure the future competitiveness of the sector. In the UK, the government and industry have agreed a National Aerospace Technology Strategy; this strategy clearly defines areas where investment for research and development should be targeted in aerospace over the next 20 years. Due to the nature of the industry, namely long product life-cycles, limited numbers of new programmes and rigorous safety and security regulation, this was found to be the most effective means of harnessing the resources from companies, government and regional development agencies.
14. An exemption for applications under the National Aerospace Technology Strategy complies with the other parameters defined by the Commission:
 - a) well defined market failure has to exist
 - b) the aid instrument has to target market failure
 - c) distortions of competition and the effect on trade should be limited to ensure that the aid measure is not, on balance, against the general interest.

15. The UK aerospace industry is a national cluster operating in a highly competitive global market. The sector operates across all regions and devolved administrations. The extent and complexity of the supply chains supporting aerospace manufacture do not always sit comfortably with the concept of a regional cluster.
16. The UK has created a number of centres of excellence and support networks that provide knowledge and practical experience for all companies, irrespective of where they operate. State aid for these initiatives is extremely important, and future support should not be unnecessarily constrained by tight geographic qualifying criteria.
17. Aerospace is a highly specialised sector, the number and type of clusters should be focused. It is difficult to envisage how an aerospace cluster could be generated in the EU without drawing away expertise from those that are already in existence. Such an outcome would be a concern to SBAC.
18. Any focus to develop aerospace clusters should be in accordance with the national strategy for the sector, in the UK's instance, the National Aerospace Technology Strategy.

Question 7 and 8

19. Tax incentives can encourage investment but are not the major drivers of innovation within aerospace and are no replacement for a properly funded programme of research.
20. Repayable launch investment: a repayable loan provided by the government, has been crucial in the process of helping to move projects from the drawing board into production. Large-scale projects that characterise the aerospace sector are few in number and come with high-levels of risk attached. Due to this, the financial markets have been reluctant to support projects of this nature and there is no available evidence that suggests that this is likely to change. Government support for the launch of large scale projects will continue to remain important for the foreseeable future.
21. Innovative start-ups within the aerospace sector are not on the same scale as other sectors. This further emphasises the need to ensure that the different characteristics of the sector are recognised in some way through the exemption process and can therefore continue to be supported by the UK government.

Conclusion

22. It is the aim of the Commission to achieve less and better targeted state aid. SBAC supports this objective but is concerned that without modification the proposed rules will not succeed in reducing the administrative burden of applications associated with aerospace. Furthermore, they could have the unintended consequence of prejudicing some bodies against investment in this important area.
23. Government support for investment in research and development will continue to remain crucial to address market failures in the aerospace sector. The recently published research and development scoreboard produced by the UK's Department of Trade and Industry demonstrates the importance of sustained investment in this area. The report shows aerospace as one of the most rapidly growing investors in research and development, investing proportionately more in research and development than any other sector (within the top seven hundred and fifty companies recorded by the R&D scoreboard). In addition, aerospace

companies spend on average nearly 4.5 times the average company spend on R&D.]

24. A blanket exemption for SMEs, but full notification for larger applications, provides a disincentive for government and regional investment in the aerospace sector. Most of the innovation within aerospace is driven by large companies.
25. To prevent this unintended consequence, SBAC proposes that an additional exemption is developed for any project that is part of a clearly defined investment programme or as part of a national or European strategy to help secure the future competitiveness of the sector. In the UK, the government and industry have together agreed a National Aerospace Technology Strategy; this strategy clearly defines areas where investment for research and development should be targeted in aerospace over the next 20 years.
26. Under this SBAC proposal, applications for all projects that are part of the National Aerospace Technology Strategy could be granted without notification to the Commission. This fits well with the Commission's aim to encourage innovation through targeting state aid where there are market failures and would increase the efficiency of the process.