

Manufacture

— HLG

EU State Aid Strategy
for Research &
Innovation

Consultation Document – Dec 2021

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Table of Abbreviations:

Abbrev.	Description	Abbrev.	Description
RD&I	Research, Development & Innovation	EFFRA	European Factories of the Future Research Association
HLG	High Level Group	ETP	European Technology Platform
EU	European Union	GBER	General Block Exemption Regulation
E-DIH	European Digital Innovation Hubs	MNC	Multinational Corporation

About ManuFUTURE:

ManuFUTURE is a European Technology Platform (ETP) established in 2003 as “an industry-led stakeholder forum recognized by the European Commission as a key factor in driving innovation, knowledge transfer and European competitiveness”. The mission of ManuFUTURE is to propose, develop and implement a strategy based on Research and Innovation, capable of speeding up in manufacturing industry the rate of industrial transformation to high-value-added-value products, processes, and services, securing high-skills employment and winning a major share of world manufacturing output in the future knowledge-driven economy. As the governing body of the ManuFUTURE Platform, the HLG (High Level Group) sets-up the strategy related to maintaining European leadership in Manufacturing.

1.

Executive summary

1. Executive Summary

In a world of increasing complexity and competition, the EU free market remains one of the European Union's biggest assets. The premise being that all members have access to an open, fair (level-playing field) market and that state aid is allowed under limited, defined, circumstances where the benefits outweigh potential negative effects on competition. In effect the EU state aid system provides a legal umbrella in which certain types of state aid can be provided by public authorities lawfully. These state aid structures are currently under review, with some stakeholders questioning their effectiveness in the context of the global realities of the 21st century. In reality the basic framework of state aid mechanisms within the EU has been in place since the 1980s and has evolved slowly in the intervening years. Some detail and complexity have been added but even the current considerations may be viewed as an evolution of the existing procedures, rather than a revolution in Commission or member states thinking. In truth there is merit in both approaches, on the one hand it is important that state aid does not distort the single market which is generally better off being regulated along competitive lines. On the other hand, how is Europe going to accelerate key strategic initiatives (example Hydrogen research), to transition to a more economically, environmentally, and socially sustainable Europe, in the twin transition journey?

A key sector within this context is manufacturing, which continues to be the backbone to the European economy. Manufacturing companies employ nearly 30 million people in 2.1 million enterprises and generating EUR 1710 billion of value added. It represents 14.2% of the total European workforce and 20% of the value added of the EU-28's non-financial business economy. This paper looks at the broader setting of state aid policy within the EU, the practical consequences of this policy for manufacturing, innovation, technology diffusion, particularly in the face of increasing global competitive pressures and the challenges facing this key sector. To that end we consider The New Industrial Strategy for Europe (2020), the more recent communication from the Commission (Framework for State Aid for Research and Development and Innovation (2021), and the latest extension of scope of GBER adopted recently (Jul 2021) by member states under the Horizon Europe framework. The paper focusses on the specific perspectives and unique contributions of the manufacturing sector in Europe and concludes with a number of key recommendations from the ManuFUTURE HLG.



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3.

Introduction

3. Introduction

Manufacturing continues to be the backbone of the European economy. As detailed in the ManuFUTURE 2030 Vision Document, manufacturing companies employ nearly 30 million people in 2.1 million enterprises and generating EUR 1710 billion of value added. It represents 14.2% of the total European workforce and 20% of the value added of the EU-27's non-financial business economy. These impressive figures belie the fact that manufacturing globally, not just in Europe is undergoing a significant transition, usually labelled Industry 4.0 (or digitisation of industry) and that Europe's relative dominance in this sector is under threat. In 1995, European manufactured products accounted for 31% of the world's manufactured products, in 2013 this fell to 27%. During the same period, this EU's global value-added contribution fell from 23% to 17%.

The impact of Covid-19 is apparent to all who have lived through the harsh experiences of the pandemic. No country, social class or race has been spared the consequences of the Covid virus on our daily lives and experiences. But manufacturing as a sector has been one of the leading lights internationally. Whether its medical supplies, ventilator production, critical PPE, food supplies or even toilet paper, manufacturing has been able to continue to deliver excellence in these difficult times. In its own unique way, manufacturing has been a real example of human endeavour in a time of crisis. However, one key lesson learnt from Covid (and more locally in Brexit) is the fact that manufacturing is very much a global activity and any considerations pertaining to taxes, levies, subsidies and related policy and strategies need to be reflective of same.

The focus topics of the future will be dominated by concepts such as supply chain resilience and sovereign capability. These challenges are heightened by significant progress made by countries like China who have executed an impressive strategy on research focus in innovation and technology on a global level. Nearer to home the EU remains committed to the twin transition strategy, which will require the greening and digitisation of European industry. Underpinning all this transition activity is the significant challenge associated with reskilling and upskilling the European traditional workforce. This interesting and challenging period for manufacturing is the backdrop for this position paper on state aid strategies in Europe.

This paper looks at the broader setting of state aid within the EU, the practical consequences of this policy for manufacturing, innovation, technology diffusion and more, in the face of increasing global competitive pressures and the challenges facing this key sector in context of the Industry 4.0 transition. Whilst the broader considerations pertaining to competition policy, such as mergers and acquisitions form an important narrative for the context of the wider discussion, the focus of this position paper is on the specific needs and impacts relating to state aid for RD&I. To that end we consider The New Industrial Strategy for Europe (2020) and the more recent communication from the Commission (Framework for State Aid for Research and Development and Innovation (2021), currently under discussion with member states and the latest extension of scope of GBER adopted recently (Jul 2021) by member states under the Horizon Europe framework. The paper concludes with some recommendations from the ManuFUTURE HLG.

4.

Commentary on Current State Aid status

4. Commentary on Current State Aid status

A key tenet in the European project is the single market, which remains one of the European Union's biggest assets. The basic premise being that all members have access to an open, fair (level-playing field) market and that State Aid is allowed under limited, defined, circumstances (including to address genuine market failures), where the benefits outweigh potential negative effects on competition. State aid rules are structured in a hierarchical manner beginning with the EU treaty which sets out the legal structures (articles 107(2) and 107(3) of the Treaty). The Treaty also provides a framework regarding aid to promote research, development, and innovation (under article 107(3)C), where state aid facilitates economic development, without adversely affecting trading conditions within the community. The treaty structures are supported by the RD&I Framework document (currently under consultation for update) and further by the Regulations layer (including detail on GBER/Di Minimis) which provide safe harbour definitions of permissible aid. It is important to note at this point that financial support for activities of a non economic nature (broadly those where there is no commercial market) does not qualify as state aid in the first place and therefore is not subject to the regime.

Currently the EU structures on competition policy including the state aid rules pertaining to the single market and indeed the overarching European Industrial Policy are experiencing some scrutiny. Developments in the mergers and acquisitions space (for example the Siemens Alstom proposed merger and indeed the Chinese led acquisition of the German automation company Kuka) has led to different European stakeholders, questioning the ongoing validity of the current policy (reference Franco-German Manifesto for a European Industrial Policy fit for the 21st Century and Made in Germany: National Industrial Strategy 2030). This in turn has fed different narratives on the role of state aid within the European Union. On the one hand it is important that state aid does not distort the single market which is generally better off being regulated along competitive lines. On the other hand, how is Europe going to accelerate key strategic initiatives (example Hydrogen research), to transition to a more economically, environmentally, and socially sustainable Europe, in the twin transition journey?

A key component within this higher order strategic review process, is the role of state aid in RD&I. The New Industrial Strategy for Europe (2020) sets out that Europe 'needs an industrial policy based on competition, open markets, world-leading research and technologies and a strong single market which brings down barriers and cuts red tape'. In keeping with the broader discussions on state aid applications and constraints, it acknowledges that 'Europe must resist the simplistic temptations that come with protectionism or market distortions, while not being naive in the face of unfair competition'. It also acknowledges that 'stepping up investment in research, innovation,

deployment and up-to-date infrastructure will help develop new production processes and create jobs in the process’.

Against this backdrop the EU Commission has undertaken a review of state aid for RD&I with member states (Framework for State Aid for Research and Development and Innovation, 2021). The document under review, whilst providing more clarity on specific elements of existing guidelines, does not offer a significant shift in either approach or framework for engagement with States on the state aid. This is perhaps a consequence of the political reality of getting agreement amongst the member states. The Commission is perhaps mindful also of the ‘subsidiarity principle’ and its implications for EU intervention in the first instance. However, this is a delicate balance to achieve, as the EU is facing

5.

Commentary on Manufacturing Challenges

5. Commentary on Manufacturing Challenges

The global competition currently facing manufacturing in Europe is immense. The sector is undergoing an industrial revolution on a scale never before witnessed in human history. The inherent challenges in delivering a green and digital transition, particularly for the SME sector are significant. All of this is set against a backdrop of somewhat sluggish European business performance in absolute terms against the rest of world. At the beginning of this century 41 of the world's 100 most valuable companies were based in Europe, where only 15 remain today (ref: Economist, July 2021, 'The land that ambition forgot'). The arguments that articulate particular challenges in a European context (nationalities, languages, cultures etc), the progress the Union has made (historically as well as culturally) and the true nature of global leadership (e.g., green & regulatory agendas) are well made and well meaning, but global pressures are having real economic impacts on the EU zone.

The manufacturing sector is also feeling the winds of this reality. For example, in our well-established car manufacturing sector, it is an astonishing truth that Tesla is worth roughly as much as all other American and European car manufacturers combined. China for example has developed an impressive strategy in research paper output in the area of technology and innovation. Over the past 20 years China has grown to becoming the highest research output generator on the planet. This is driving changes on many levels. For example, Airbus and Boeing, who have been embroiled in a legal battle over state subsidies for nearly two decades, have agreed a truce (initially for 5 years) in part to focus on greater challenges arising from the Chinese progress in their sector.

As a Union we have a significant challenge to address and while some elements are more structural in nature, some political and others at a more strategic level, all have their relative importance, and one size will certainly not fit all. The structural nature of how States interact and engage in state aid rules as a collective is well understood and is again under consideration at present. Some political consideration in this area will need to be extended to member states who are experiencing vastly different regulatory conditions on the borders with regions outside the EU (for example on the eastern border region). A fair competitive environment will need to be facilitated to accommodate these countries. From a strategic perspective, we will need to support industrial uptake of advanced technology, digital platform development and integrated approaches (e.g., interoperability) in a practical manner. Here the links between RD&I activities and industrial requirements become ever more important.

The Commission has established an EU target of 3% of state GDP to be spent on R&D (and public sector spend 1.4%) by 2030, a target that will perhaps challenge most

member states. This is compounded in the difficulty in making the right decisions on sectors and technologies to prioritise within that spend, as it is important to use state aid spending as effectively as possible. Perhaps a more strategic derogation could be applied to key strategic initiatives, for example as the EU already does with the Horizon programme, and whilst one does not want to open the doors to abuse of this type of approach, it could be better applied to the green and digital transition agendas. This would have a significant impact in the main manufacturing goals into the next Framework program period. If Europe is to maintain its global standing in manufacturing, if we are to achieve our goals on digital resilience and autonomy, we need a strongly enabled manufacturing sector and some bold steps may need to be taken.

6.

HLG

Recommendations

6. HLG

Recommendations

The overarching balance to be achieved by the Commission in any consideration in respect to state aid rules, is between the aspiration to encourage the ‘right’ activities in as effective a manner as possible, whilst not unduly distorting the wider marketplace. The recommendations outlined herein are positioned within that context and indeed presented as an ideation function to the wider discussions on State Aid for a 21st century Europe.

1. There may be an opportunity to consider the possibility of adding a ‘mid-tier’ designation to the current SME and Multinational definitions that apply in state aid nomenclature. This tier could be designated by size (between current SME and MNC definitions) but also identifying those companies who are critical to the strategic value chain for Europe. These companies are crucial to the regions they populate, often in less population dense locations, providing much needed employment, training and opportunities for the citizens of that locality. These so called ‘mid-tier’ companies have a scaling challenge which is not adequately supported by the current state-aid conditions, as they no longer qualify for the SME sized options and certainly do not have the larger financial clout of a true multinational corporation. There should be a consideration to extend the definitions under the current state aid rules to accommodate a mid-tier level, with a specific focus on interventions to support expansion and scaling activities. This would be an extension or extrapolation of the existing rules and funding levels, between the MNC and SME levels.
2. Another relatively simple adjustment could be in extending the De Minimis levels from €200,000 over 3 years to €500,000 over 5 years. This type of approach would be particularly helpful in gaining proper traction for manufacturing SMEs in the evolving E-DIH program. All the current existing auditing checks and balances could remain in place, but an EU-wide agreement to allow this increase in levels, to accommodate ambition in the industrial sector to invest in Industry 4.0 technologies and research. It would be related to the ambition of the companies themselves and managed at a state level, thus minimising any distortions between member states.
3. International best practice and learnings could be applied in member states as part of the overall EU supported approach. E.g., “indirect” state aid for companies, particularly SMEs, could be based on the funding of applied research and technology transfer projects developed by public research institutions in cooperation with companies, so as to support their business innovation capacities. As an example, the Innosuisse model running in Switzerland can be referred to. According to such a model the company would provide the business model, to sustain its own costs, and to apply for funding of the research partner activities, which is funded by the innovation agency by means of public funds, in order to support the company business innovation. In short: companies do not

receive direct public funding but receive research contributions from research centres funded by the state.

4. One of the more recent agreements in this space has been the adoption of the extension of scope of the GBER, allowing member states to implement state aid measures supporting projects they have received a 'seal of excellence' under Horizon Europe and co-funded R&D projects (July 2021). This is an example of extending and simplifying current rules to allow for flexibility within member state jurisdictions. We welcome this initiative as part of the evolving discussion and process but note that manufacturing specific elements should be considered in future iterations and discussions.
5. A more ambitious suggestion is the development of a dual-system rule which would consider the relative size of Member State economies, and would facilitate smaller countries having more generous structures, so as not to be overwhelmed by larger states with deeper pockets. For example, an EU-wide rate could be established after which an economy weighting could be added but ensuring that there is an absolute cap to the amount permissible. This could be applied to all state aid ratings or specifically for activities of strategic importance to the European ambition. Such a system would encourage more generous conditions for technology research and development to be undertaken at a state level but deter subsidy friction between States.

7.

Conclusion

7. Conclusion

Europe needs to find a balance between ensuring there is a level playing field between members states in terms of access to (and support within) its single market, the wider need to compete on a global scale with increasing competition and meeting its own socio-economic charter priorities (such as climate change, resilience and autonomy). As we have outlined in this paper, manufacturing remains a key driver for European ambition. It is a sector which contains complex, embedded and truly global value chains, which makes the aspiration for regional containment policies increasingly untenable. In order to maintain its relative position at a global level, Europe must maintain a high degree of technological and innovation leadership, across enough sectors in order to be relevant in that global sense.

Whilst the wider discussions on the European context for state aid are evolving, it is important to note that state aid considerations for the RD&I activities are critical for industrial development and advancement on a practical scale. Whether the focus is on the twin transitions required by industry on digitisation and the green agenda, or in more specific sub sections of same, such as hydrogen research, RD&I remains a key driver for European success. Our competitors recognise this need, as witnessed by the US Biden administration's recent bill to increase US federal spending by \$250bn on research and development on new technologies. European ambition can be measured by the scale of the new Framework program, but equally in its ongoing commitment to member state targets of up to 3% of GDP spending on research and development.

The purpose of this paper is to present the ManuFUTURE perspective on the critical importance of state aid initiatives within the RD&I community for the advancement of European manufacturing. We have outlined a number of practical measures which would help facilitate a more coherent alignment between Commission objectives and industrial execution at scale.



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