

AGORADA 2007

Brussels, 31 May & 1 June 2007

IS THERE ANY FUTURE FOR INDUSTRIAL ACTIVITIES IN THE EUROPEAN REGIONS ?

Working Document of the Secretariat

1. The Stakes

Most EU regions are facing an actual, supposed or future loss of manufacturing industry competitiveness. The consequence of this is the relocation of certain labour-intensive production activities and low value-added repetitive tasks, or even the closure pure and simple of such production units.

This should motivate public authorities and RDAs to reflect upon about the future of their industrial sector and think about ways of helping manufacturing companies preserve or generate competitive advantages.

Such a review needs to both reckon with the different competitive contexts in which regional SMEs, subsidiaries of multinationals and subcontractors of large industrial groups operate, and seek to identify the strengths and weaknesses of each of those three categories of businesses when facing competition either through costs or innovation.

2. Measuring Business Sensitivity to the Globalisation of Competition

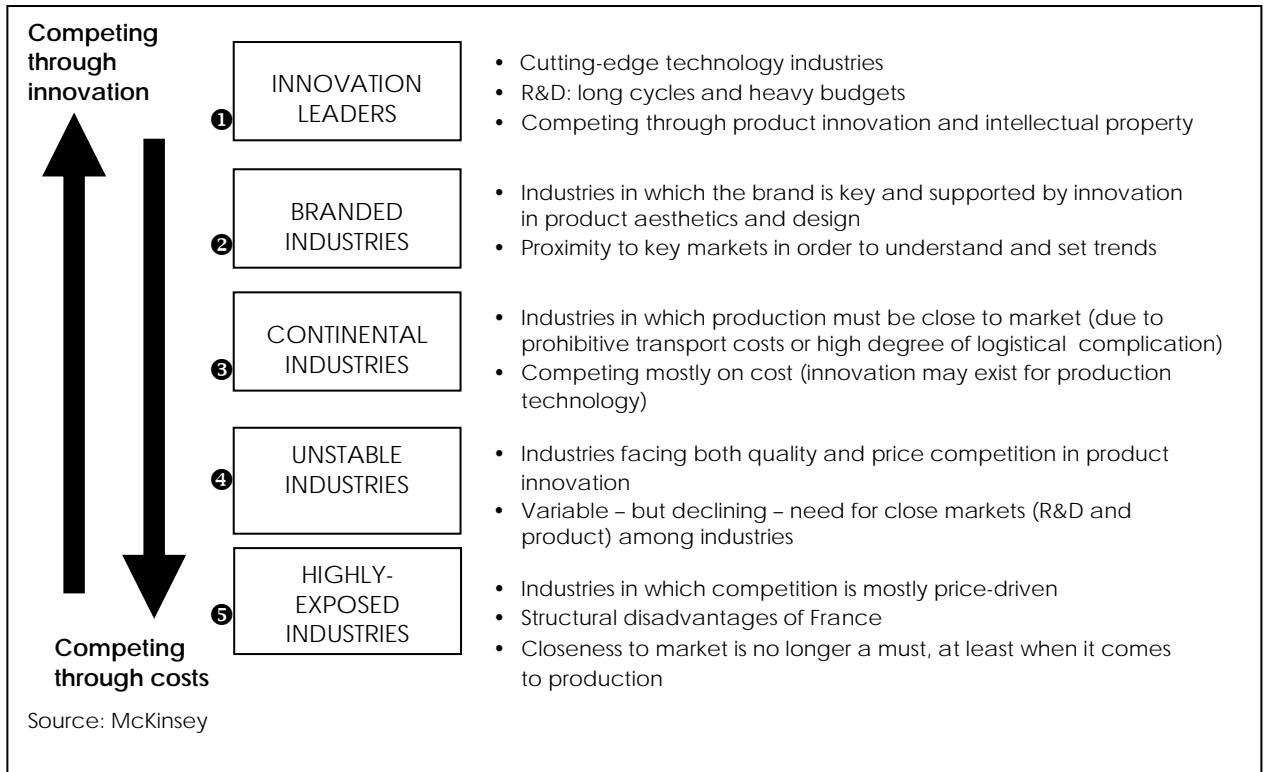
For several decades, the factors governing the establishment of manufacturing units included:

- ✓ the cost of production factors, including labour quality;
- ✓ labour productivity;
- ✓ closeness to markets
- ✓ the quality of infrastructure;
- ✓ quality of life;
- ✓ financial incentives.

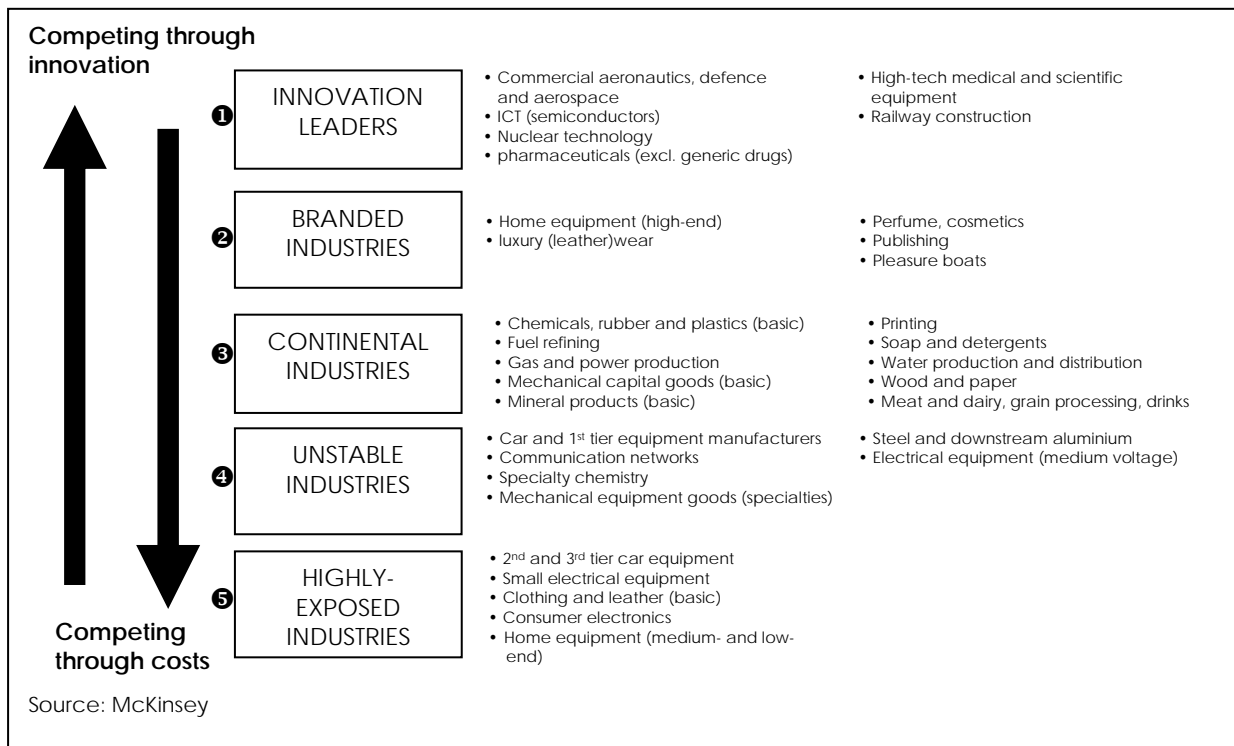
Economic globalisation and the emergence of new markets (BRIC: Brazil, Russia, India, China) have considerably altered the first three factors above, at least in those industries that are exposed to competition through cost. However, Europe temporarily retains undeniable advantages compared to emerging countries – as far as the top three factors above are concerned – when it comes to companies competing through innovation.

For the purpose of measuring territorial (national, regional, urban) sensitivity to these two forms of competition, consultants McKinsey France worked out and published in a report entitled *Donner un nouvel élan à l'industrie en France* ("Creating a new impetus for industry in France") the evaluation matrices presented below.

Five groups of industries with specific competitive issues



Examples of industries per group



3. A European Policy Framework

Also worth considering is that in 2005, the EU Commission published a communication entitled "A New Integrated Industrial Policy: To Create the Conditions for Manufacturing to Thrive" (see the document called "A new integrated industrial policy: to create the conditions for manufacturing to thrive", which analyses 27 industrial sectors, completed by the document entitled "European Industry: a Sectoral Overview – Technical Update 2006").

The EU Commission expects to present a new interim report in mid-2007, addressing the competitiveness of the ten industries below: Car, Biotech, Shipbuilding, ICT, Mechanical, Pharmaceutical, Textile & clothing, Wood, Defence and Space.

However, in recognition of the vulnerability of some companies to globalisation, the EU Commission developed a new instrument in 2006 to mitigate the social cost of restructuring in companies affected by globalisation, i.e. the "European Globalisation Adjustment Fund" (EGF) which includes provision of Community financial support (see OJ L 406, 31 December 2006).

4. Job Losses in the Manufacturing and Services Industries

Quite aside from the fleeting emotions caused by job losses as a result of restructuring among large industrial groups, some regions face a "silent" unravelling of the local fabric of small and medium-sized enterprises. Indeed, the latter can be affected by one or more of the factors below:

- loss of sectoral competitiveness;
- domino effect following restructuring or closure of large regional principal contractors;
- drastic reduction in the number of subcontractors;
- absence of successors.

The few figures below illustrate the structural loss of manufacturing jobs.

- In 2005, 7,147 jobs were lost in 14 of the 23 largest Belgian companies¹. Concurrently, the 9 companies that did open new positions only created 1,782 new jobs. Worth noting is that in 2006², more than 63,000 new businesses were set up. This confirms that the bulk of new employment is created by SMEs.
- Job losses in the automotive industry³ between 2000 and 2006 totalled 1,175,000, i.e. 6% of the sector's payroll. Among the EU15, the only country where employment grew during that period was Austria.
- In the fourth quarter of 2006⁴, the ERM (European Restructuring Monitor) recorded some 455 instances of restructuring, causing 95,661 jobs to be lost.

According to the ERM, these were lost to:

- internal restructuring (57,007);
- bankruptcies and takeovers (13,510);
- mergers and acquisitions (11,426);
- delocalisation (8,468);
- relocation (1,524);
- outsourcing (900);
- other causes (2,790).

¹ *Trends-Tendances Top 5000* – December 2005.

² Euler Hermes: Radio interview.

³ Euler Hermes: global restructuring of the automotive industry.

⁴ ERM Quarterly Issue 4 – Winter 2006.

Relocations are no longer limited to manufacturing: both services and RTD activities have become mobile too. This is how 18.5% of the total payroll of Accenture⁵ is now employed in India (i.e. more than the company's US based staff) compared to 14.6%, 12.8% and 6.7% respectively in the cases IBM, Avira (Insurance, UK) and Citigroup. In recent months, the kinds of positions that open there are no longer for call centre operators but rather for IT specialists, actuaries and credit rating and risk evaluators. As far as RTD is concerned, noticeable is for example the ever larger RTD amounts invested in sectors such as NICT in China and India.

5. Trends in FDI (Foreign Direct Investment)

According to the findings of Ernst & Young's "European Attractiveness Survey", it is clear that FDI in Europe creates more jobs in the new EU12 compared to the old EU15. While 20% only of the roughly 3,000 new FDI projects located in the EU12, a full 50% of the new jobs they generate are created there.

6. Key Technologies and High-Potential Markets

In 2006, the EU Commission ordered a report entitled "Creating an Innovative Europe" from an expert group coordinated by Mr Aho. This report underscored that Europe can boast innovative potential in sectors including:

- eHealth;
- Pharmaceuticals;
- Environment;
- Digital contents.

Following this report, the EU Council mandated the EU Commission to initiate a reflection on "lead markets", whose findings should be published toward the end of 2007.

Since then, the concept of "lead markets" has been used on different occasions, including in a report compiled as part of the Europe-Innova Initiative, which identified seven high-potential markets including:

- Aeronautics;
- Eco-innovation;
- Energy;
- Automotive;
- ICT;
- Biotechnology;
- Textile.

In addition, the report mentions the potential contribution of gazelles.

At national level, foresighting initiatives have been launched, which are often called "Key Technologies for the Future". Worth mentioning in this respect is the French example: the French Department of Industry published a report entitled *Technologies-clés 2010* ("Key Technologies 2010"), which examines the potential represented by 83 technologies ranked in eight sectors⁶. This report mentions similar exercises conducted in Germany, the UK, etc.

While Europe does have innovation and research potential indeed, there is reason to wonder where the products resulting from research will be manufactured and whether Europe can produce significant numbers of gazelles.

⁵ Source: Le Monde – Herald Tribune 14 February 2007.

⁶ Life sciences, health, transport, retail/consumption, technology and production methods

Worth dwelling upon in this context is that the regional ability to encourage the development of entrepreneurial growth companies (EGCs or gazelles) becomes a key factor of regional competitiveness. Indeed, such businesses are often geared toward international operations right from the start. Thus, innovative businesses tend to better survive globalisation than those with declared national or regional ambitions.

Several studies argue that comparatively more newly-developed US than EU businesses achieve market dominance in their industry. It appears that in 2000, out of those businesses from among Business Week⁹'s Top 1000 that were set up after 1980, 64 were US companies while only 9 were European. Of the 64 US businesses, 45 operated in just three industries: (i) electronics & computers; (ii) telecom; and (iii) business services.

Notable is that regions now develop industry-specific strategies that aim to either help regional businesses invest in RTDI or adjust to the new requirements of large industrial groups.

⁹ A Policy for Industrial Champions: From picking the winners to fostering excellence and the growth of firms. Industrial Policy and Economic Reform Papers N° 2