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EUROPEAN INDUSTRIAL POLICY AS AN INSTRUMENT TO SUPPORT ECONOMIC GROWTH

Introduction

State intervention in the functioning of the industry has a long history. It has been developed in highly industrialized countries, at varied speeds and in different ways. Over time, the perception of the industrial policy has changed. From acceptance during the time of mercantilism, over the phase of import-substituting industrialization between 1950s and 70s[2], to the rejection in 1980s and 90s through a neo-liberal doctrine[3]. Officially, the industrial policy as a form of intervention has been recognized in the OECD Report in 1975[4]. Despite the fact that since then, in most countries, the share of the industry in the creation of domestic product has remained at the same level or even has decreased in favor of services, changes in industry are critical in shaping the structural transformations in the economy. Additionally recent decades have been characterized by significant changes in productive structures and international competition. The entry of new competitors (such as Japan, China, India), technological changes (the diffusion of ITCs) and scientific turn (genetic engineering and biotechnologies), climate changes, the deepening and widening of the European integration process and eventually social changes and demographic trends - all these developments have underlined the need for structural adjustment of economies. As a consequence the interest in the industrial policy is growing currently. Furthermore, these changes have forced the redefinition of industrial policy.

New approaches to industrial policy have been tried out in the formulation and implementation of "from the bottom" policies (local and regional), while the traditional assumed direct interventions by the central state in market to pick winners and support the development of particular sectors. Thus, the industrial policy means variety of public actions aimed at guiding and controlling the structural transformation process of the

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[2] The basic assumption of the mercantilism's philosophy proclaimed that a development is possible only if the export is highly expanded and higher than the import. While imports substitution approach was to shift demand from foreign products in to the goods produced in the country. This method would prevent the national economic downturn, help reduce unemployment in the country and strengthen the position of the country.

[3] T. Altenburg, *Industrial policy in developing countries. Overview and lessons from seven countries cases*, Deutsches Institut für Entwicklungspolitik, Discussion Paper 4/2011, p. 10.

[4] M. Klamut, *Polityka przemysłowa* [in:] *Polityka gospodarcza*, B. Winiarski (ed.), PWN, Warszawa 2006, p. 246.

economy[5]. Highlighting the revival of industrial-policy thinking in the era of globalization, the main objective of this paper is to define the role and importance of industrial policy in solving the contemporary economic problems. The analysis will cover the stages and directions of the evolution of European industrial policy and the establishment of a new approach. It attempts to assess the efficiency of existing industrial policy, and to identify key actions needed for the development of a sustainable industrial policy to improve the competitiveness of the European internal market.

The statements of industrial policy

The industrial policy is based on the assumption that markets are fallible. Free market should achieve Pareto efficiency (efficient allocation of resources), i.e. a situation where there is no way to reallocate goods so that the new allocation would make everyone better off[6]. However, this model assumes ideal conditions which rarely exist in reality. There is a huge literature documenting how market forces will not produce optimal results and that some kind of state intervention is necessary to promote industrialization. Therefore government should prevent the failures of the market process, that is, situations in which operators are not able to achieve the potential efficiency in the sense of static and dynamic. The market's weaknesses in the sense of static rely on the fact that the company is satisfied with a lower production, which does not use the owned production capacity. In turn, dynamic failures describe the situation when the company does not invest enough in the sphere of research or the development of the productive capacity. Consequently the enterprise does not achieve the potential benefits of lower costs and more efficient production. As a result of poor performance in an open economy it may be unable to compete in world markets. A key argument for using the industrial policy is to prevent dynamic failures of the market by financing certain areas of scientific research, particularly in the area of innovation[7]. The current interest in industrial policy is the result of the discussion on the benefits of free trade and the role of the state in the economy. No one does believe that central planning and nationalization give better results than the competition and market self-regulation. At the same time no one assumes that the market liberalization, and a lack of government involvement in allocation of resources are a sufficient impulse generating economic growth[8]. In this context the industrial policy describes government interventions at the supply side, aimed at encouraging structural changes.

Industrial policy can take the form of two types of actions: horizontal (general) or vertical (selective). Horizontal policy is devised to influence the entire economy through innovation promotion and knowledge sharing. Vertical policy aims to support specific sectors, industries or companies. This approach is most criticized because it distorts competition and discriminates some operators by picking winners. Similar instruments of industrial policy can be divided into two main categories: monetary and structural. Monetary measures involve transfers of funds from the government to companies and

[5] P. Bianchi, S. Labory (ed.), *International Handbook on Industrial Policy*, Edward Elgar Publishing Limited, Massachusetts 2006, p. 3-4.
[6] D. Geradin, I. Girgenson, *Industrial Policy an European Merger Control – a reassessment*, Fordham Competition Law Institute, Juris Publishing Inc. 2011, p. 355-356.
[7] M. Klamut, *Polityka przemysłowa…*, op. cit., p. 246-247.
[8] E. Cohen, *Theoretical Foundations of Industrial Policy* [in:] *An Industrial Policy for Europe. Context and concepts*, EIB Papers, volume 11 No 1 2006, p. 85.

include various forms of subsidies, while structural measures do not involve a transfer of funds but contain tariff and non-tariff barriers to trade, regulatory measures and government policies promoting "national champions"[9].

The evolution of the European Industrial Policy

The industrial policy for the mid-80s did not have the nature of the Community and remained a matter for individual Member States. There was no direct reference to industrial policy in the Founding Treaty of the European Economic Community. Only the steel, coal and nuclear industry have been the subject of Community action in the separate communities (European Coal and Steel Community, EURATOM).
However, the Treaty of Rome contained indirectly provisions related to the industry. A removal of barriers in trade between member states require a guarantee from a company and an administration that these barriers would not be replaced by the unfair practices, which could distort free competition. Community competition rules related to[10]:

- agreements between companies and the abuse (by them) of their dominant market position (article 85-86);
- dumping, or protection against unfair foreign competition (article 91);
- activity conditions of state monopolies of a commercial nature (article 37 and 90);
- state aid (article 92-93), including a ban on any state aid, which disrupt competition by favouring companies or industries in trade between members (article 92/1).

No direct reference to industrial policy meant that national policy in the area had prevailed in fact until 1985. What is more, between 1975 and 1985 a general tendency towards interventionism was observed - as a response to the worse economic situation.
The first major initiatives for collective action to promote industrial development are reflected in the Commission White Paper published in 1985, containing a program for the establishment of the common internal market by 1992. The objective of this program was to stimulate a competition forcing mechanism, including restructuring and modernization of industry. The Single Market, considered to be the framework of European industrial policy, places systemic obstacles to a return to old interventionism. The first paragraph of article 130 states that: "The Community's aim shall be to strengthen the scientific and technological basis of European industry and to encourage it to become more competitive at international level"[11]. The above paragraph is referenced then in the Maastricht Treaty in the title XIII – *Industry.* It emphasizes the need for ensuring that the conditions necessary for the competitiveness of the Community's industry exist. For that purpose it established the following objectives[12]:

- speeding up the adjustment of industry to structural changes;
- encouraging an environment favourable to initiative and to the development of undertakings throughout the Community, particularly small and medium-sized undertakings;
- encouraging an environment favourable to co-operation between undertakings;

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[9] D. Geradin, I. Girgenson, *Industrial Policy…,* op. cit., p. 355.
[10] J. Anusz, *Polityka konkurencji w Unii europejskiej. Integracja Polski z UE*, Instytut Koniunktur i Cen Handlu Zagranicznego, Warszawa 1996.
[11] *The Single European Act*, Luxembourg, 17 February 1986, OJ L 169 of 29.6.1987, p. 15.
[12] *The Maastricht Treaty*, Maastricht, 7 February 1992, OJ C 191 of 29.7.1992, p. 32-33.

- fostering better exploitation of the industrial potential of policies of innovation, research and technological development.

Thus, for the first time the industrial policy was explicitly mentioned in EC Treaties. However the unitary concept of this policy for the European Union appeared in the European Commission's proposal of 1990 entitled *Industrial Policy in an Open and*

Competitive Environment.

The communication paved the way for a new perspective of industrial policy which established the division of responsibilities between businesses and public authorities (whose role is to create a dynamic environment favourable to an industrial development) and abandoned the defensive protectionist sectoral approaches.
The next stage of formulating the basis of industrial policy within the European Union was the adoption by the Council in December 1993 of *The White Paper on Growth Competitiveness and Employment.* The document envisaged the joint action of the EU and its member states in promoting industrial development as a prerequisite for economic growth and employment in terms of international competitiveness. A year later, the European Commission presented to the Council a communication entitled: *An Industrial Competitiveness Policy for the European Union* concerning the promotion of[13]:

- intangible investments, i.e. investments in research and development, intellectual property, education and training;
- the development of industrial cooperation, by removing barriers to such cooperation;
- ensuring fair competition, in particular the reduction of state aid and focusing on horizontal support;
- modernizing the role of public authorities, by simplifying legislation and administrative procedures, especially for small and medium-sized enterprises.

Community approach to industrial policy therefore aimed to improve the competitiveness of European industry as a whole in the international market and it has been implemented by respecting six basic principles[14]:

- subsidiarity – the European Union is only responsible for solving problems in the area of industrial policy which can be better approached at the European level;
- the public-private partnership – the responsibility of implementing and promoting the industrial policy should be shared between the public authorities and the private sector;
- competitiveness, accelerating the structural adjustments, creating an environment favourable for cooperation and encouraging the R&D or innovation activities;
- dominance of the horizontal model, aimed for a favourable business environment with free market rules and without protectionist practices;
- correcting the market failures, by interfering in case of monopoles, public commodities and common property rights;
- a compromise between efficiency and social cohesion, activities aimed at sustainable development.

The European industrial policy was thought as a concept. However, some solutions introduced at the national level, could interact selectively on some sectors, regions or

[13] Commission of the European Communities, *An Industrial Competitiveness Policy for the European Union,* COM (94) 319 final, Brussels, 14. 09.1994.
[14] P. Nica, *Industrial Policy in the European Union*, CES Working Papers II(2), 2010, p. 23-24.

industrial objectives. Certain industrial sectors are more vulnerable internationally, due either to market saturation, or to the insufficient development of the European industry in comparison with the world level. That is why sector policies were developed for: steel industry, naval industry, textile and clothing, aeronautic industry, automotive and pharmaceutical industries[15].

So far the Maastricht Treaty underlined the role of research and innovation in determining competitiveness. This emphasis was repeated in the declaration of the Lisbon Strategy at the European Summit of 2000 when EU took strong position in favour of research and innovation to ensure higher competitiveness of European industry.

The Strategy set objectives of transforming the European Union into the most competitive and dynamic knowledge-based economy in the world until the horizon of 2010.
Another challenge which EU faced was to broaden its membership to countries of Central and Eastern Europe. In December 2002 the European Commission adopted the document on *Industrial Policy in an enlarged Europe*[16]. It underlined sizeable differences between the structure of manufacturing industry in the existing Member States and in the candidate countries. This is due to the fact that industry in the candidate countries is less specialized and more centred on low-technology. Still the industry plays a key role in the economy and can draw significant benefits from a larger internal market. An optimal solution is to use horizontal industrial policy which takes into account the specific needs and characteristics of individual sectors.

The enlargement of 2004 offered to the European industry significant opportunities and challenges as well. In response the Commission established the main action lines of industrial policy in the communication entitled *Fostering structural change: an industrial policy for an enlarged Europe*[17]. The Commission's objective, in line with the priorities set out in the 2002 communication, is to rally public stakeholders around three areas of action for fostering change in European industry:

- better lawmaking – bring legislation into line with the needs of businesses, the attention should be paid to competitiveness and to analyzing the combined effects of different regulations on each sector of activity;
- interaction with other policies for the common purpose of improving productivity gains and promoting the use of knowledge;
- the sectoral dimension of EU industrial policy, to make EU industrial activity more visible in key sectors by involving interested parties.

Generally the industrial policy means a variety of policies aimed at a creation of an environment that is favourable to industry development and at awaking the process of industrial change.

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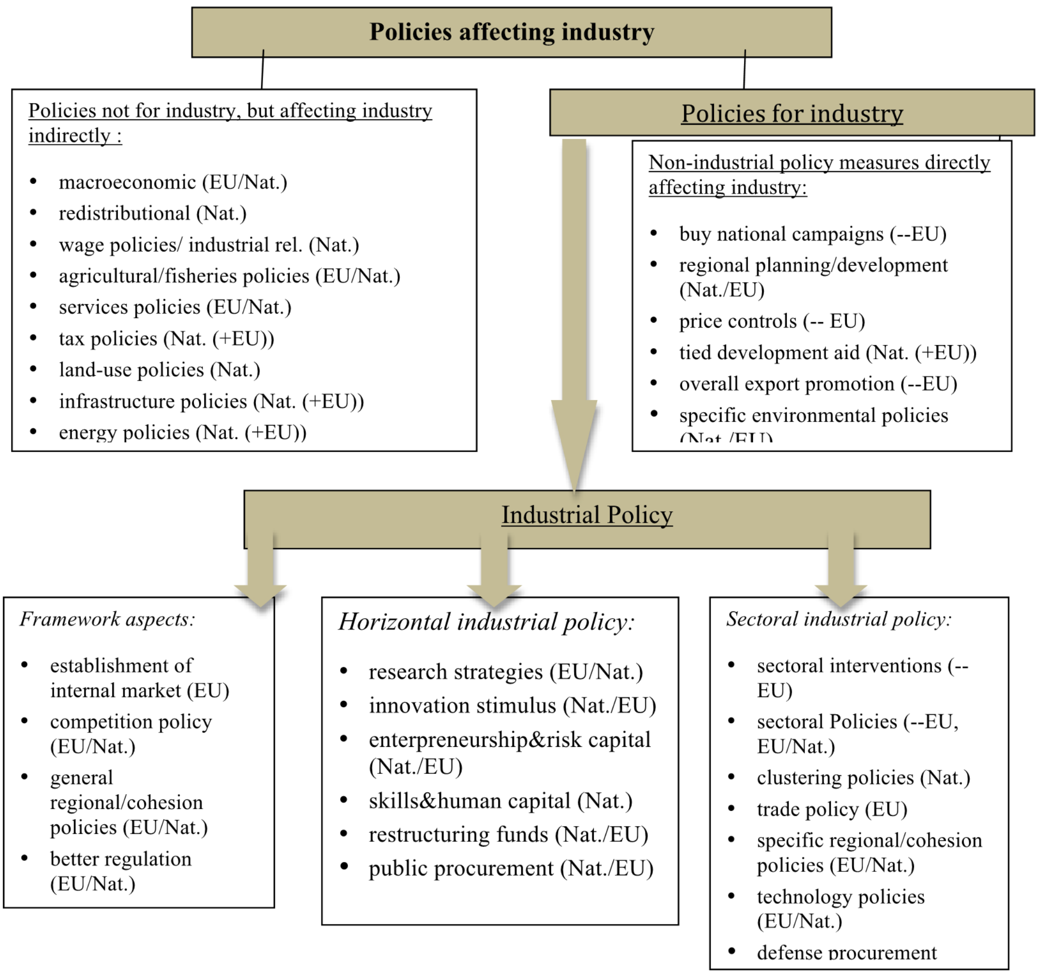
[15] Ibidem.
[16] European Commission, Communication of 11 December 2002 on: *Industrial Policy in an enlarged Europe*, COM (2002) 714 final.
[17] European Commission, Communication from the Commission of 20 April 2004: *Fostering structural change: an industrial policy for an enlarged Europe*, COM(2004) 274 final.

The industrial policy in EU that has emerged over the years has been finally determined. It is closely linked to the overall socio-economic policy and its content consists of actions taken in other areas. Figure 1 combines a comprehensive classification of industrial policy and of other policies influencing directly or indirectly the industry and relation between EU and national level of power[18]. The classification begins with distinguishing two sets of policy that somehow influence the industry and the third – industrial policy. "Policies not for industry" (such as macroeconomic, redistribution tools, wages, agriculture, services, tax, land-use, infrastructure and energy policies) are not formulated specifically for the industry, but affect it for obvious reason.

Figure 1
EU and National Powers of Industrial Policy



Notes: EU – EU powers Nat./EU – shared powers, mainly national EU/Nat. – shared powers, Nat (+EU) – national, EU constraints o marginal inputs Nat. – Member States' power--EU – little national leeway, strict EU constraints
Source: J. Pelkmans, European Industrial Policy [in:] Bruges European Economic Policy Briefings no15, College of Europe 2006, p. 4.

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[18] J. Pelkmans, *European Industrial Policy* [in:] Bruges European Economic Policy Briefings no15, College of Europe 2006, p. 2-5.

The second group consists of non-industrial policies which directly help or constrain industry but are not meant for industry (such as price controls, buy-national campaigns, regional planning and tied development aid, export promotion and environmental policies). Eventually it is defined a wide concept of industrial policy which has three major aspects.

The first one is to improve the regulatory framework through programs facilitating the operation of enterprises and improving their efficiency (undertaken at both European and national level). The second issue refers to the synergies between different European policies having impact on industry's competitiveness. Apart from policies aimed at enhancing innovation and entrepreneurship, which are two major drivers of competitiveness, many other EU policies also have an impact on the business environment and enterprise performance. All horizontal initiatives should make the best possible contribution to competitiveness. The third aspect regards sectoral policies, namely the adjustment of measures to the specificities of the sector due to the process of structural changes. For all elements listed in Figure 1 is given a combination of the impact of EU and Member States regulation (see notes).

Since 2004, leading politicians of countries such as France, Germany or Italy have occasionally called for a return to a more aggressive industrial policy. Their appeals have been mainly due to frustration about prolonged, low growth in Western Europe since late 2001[19]. Then the 2008 economic crisis inspired a growing number of interventions of public authorities. It has been a theme to the current discussion of the new industrial policy, which was launched as part of the *Europe 2020 Strategy*. It highlights actions needed to strengthen the attractiveness of Europe as a place for investment and production. The aim of the EU's strategy is to overcome the crisis and prepare the European economy for the next decade. To achieve its objectives the Commission proposes a program - which consists of a number of flagship initiatives - in the industrial policy for the globalization era: to improve the business environment and to support the development of a strong and sustainable industrial base able to compete globally[20]. Continuation of the so called a fresh approach to industrial policy is what the Commission proposes in *An Integrated Industrial Policy for the Globalisation Era Putting Competitiveness and Sustainability at Centre Stage*[21].
A strategy framework for the industrial policy should put competitiveness and sustainability of European industry at centre stage. It was stressed again that other policies have an impact on the cost, price and innovative competitiveness of industry and it is necessary to consider effects of all other policies initiatives (such as transport, energy, environmental, social and consumer-protection, single market or trade policies). In addition, the fresh approach assumes the following:

- bringing together a horizontal basis and sectoral application, a continuation of applying a tailor made approach to all sectors;

[19] A. Gouglas, *EU Industrial Policy: Sticking to the Dogma Won't Restart the Economy,* "Social Europe Journal, 01/11/2011
[20] European Commission, Communication from the Commission: *Europe 2020. A Strategy for smart, sustainable and inclusive growth*, COM(2010) 2020 final.
[21] European Commission, Communication from the Commission to the European Parliament, Council, the European Economic and Social Committee and the Committee of the Regions, *An Integrated Industrial Policy for the Globalisation Era Putting Competitiveness and Sustainability at Centre Stage,* COM(2010) 614 final.

- the whole value and supply chain must be considered, including energy resources, raw materials and access to them, recycling of materials as well;
- regular review on the EU's and Member States industrial policy performance.

The above actions would translate directly into increased growth and the number of jobs as well as the improved international competitiveness of Europe's industry. In this new industrial policy it is understood that the main factors for economic growth are competitive companies of all sizes. To achieve this goal, they require a favourable environment; therefore six areas were distinguished where progress must be made towards meeting the 2020 goals [22]:

- structural changes in the economy
- innovative industry
- sustainable industry and resource efficiency

<u>Improving industrial competitiveness</u>

- business environment
- promoting industry and services within the single market
- small and medium size enterprises

Towards more business friendly Europe

It is argued that in order to achieve sustainable growth and to stimulate the economy, coherent and coordinated industrial policies from the Member States are required. A considerable impact may be achieved by facilitating deep structural changes, enabling innovation, promoting sustainability, improving the business environment especially for small and medium size enterprises and benefiting from the single market. Previous changes in the industrial structures of the Member States allow to divide them into four groups[23]:

1. Countries, in which industrial structure is dominated by technologically advanced sectors (Austria, Belgium, Denmark, Finland, France, Germany, Ireland, Netherlands, Sweden and United Kingdom - the value added contribution of industry varies from 10,6% in France to 24,2% in Ireland).

2. Countries with industry specialization in less technologically advanced sectors (Cyprus, Greece, Italy, Luxembourg, Portugal and Spain - with industry value added varying from 6,5% in Luxembourg to 16,1% in Italy).

3. Countries that are catching up in terms of GDP per capita, and whose trade specialization is in high-innovation intensity sectors and technology driven industries (Czech Republic, Hungary, Malta, Poland, Slovakia and Slovenia – the industry value added between 13,3% and 23,6%).

4. Countries that are catching up, but with trade specialization in technologically less advanced sectors (Bulgaria, Estonia, Latvia, Lithuania and Romania - with industry value added between 9,9% and 22,4%).

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[22] European Commission, Communication from the Commission to the European Parliament, Council, the European Economic and Social Committee and the Committee of the Regions, *Industrial Policy: Reinforcing competitiveness*, COM(2011) 642 final.
[23] Ibidem.

Within each group of countries there are competitive industries and growing companies. It is important to improve their development by using the findings from endogenous growth models, in which R&D is a key factor in determining a firm's competitiveness. A support for innovation and investment in education and training are necessary. An integrated approach should be used, taking into account a bridge that must be built for the gap between research and markets needs by greater coordination and pooling of national resources.

As outlined above, it is crucial to make preference for energy and raw materials efficiency and promote innovation in cleaner technologies. A competitive business environment is a catalyst for growth, in order to improve it, the administrative burden must be reduced. The high quality and availability of infrastructure also make an important contribution to a business-friendly environment. Specialized services are used for managing the production and distribution processes; therefore a growing support for innovative services plays a significant role. Eventually the emphasis was placed on facilities for small and medium-sized enterprises through easier access to financing and reduction of administrative obstacles and fees. The economic crisis has caused particular problems with raising capital for SMEs and large investments. Industrial policy therefore needs to support innovative financial solutions and increase the efficiency and effectiveness of financial markets.

Conclusion

The European industrial policy, since the establishment of the Single Market in 1986, refers to a wide concept based on the principles of pro-competitiveness and deeper market integration[24]. The Single market is the basis for a European industrial policy by establishing the system which prevents the returning to the intervention. The proposed industrial policy measures are directed to support adaptability and structural change allows to increase the efficiency of EU manufacturing. The main objective focuses on improving competitiveness and thus the economic growth and increased jobs creation. State aid to companies is allowed only if they have to contribute to the long term viability. The concept of the integrated approach to the industrial policy means the interaction of different areas and encompasses related policies, the look at the whole value chain (from infrastructure, raw materials, after-sales service) and promoting the creation and growth of small and medium-sized enterprises. The most effective and quickest way to adapt to new market conditions is a structural adaptation and assurance that EU measures in different areas that have an impact on industry, particularly research, competition, employment and regional development, are better coordinated. In more general terms, greater synergy between the EU's different policy areas will boost the competitiveness of European businesses. The horizontal initiatives are identified as critical for development of industrial competitiveness. They focus on improvement in innovation and technological advances, enhanced quality of human resources and breaking administrative and legal barriers that limit economic growth.

It is becoming more evident that Europe needs the integrated approach to the industrial policy. However, it remains an open question - how these recommended concepts would be actually implemented in the market at times of recession.

[24] A. Gouglas, *EU Industrial Policy…,* op. cit.

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SUMMARY

Despite the fact that we live in post-industrial age, in which biotechnology, information technologies and high-value services become engines of economic growth, countries cannot ignore their industries, because it is critical in shaping the structural changes in economy. There is no doubt that competitiveness of European Union and their members depends on industrialization. The need for the coherent approach in this area has been noticed in the late 80s of the twentieth century and since then the concept of the integrated industrial policy has been developed systematically.