

Innovation

BETTER INNOVATION POLICIES FOR BETTER LIVES

- ▶ Stronger innovation is imperative for Ireland to support future productivity growth, job creation and higher living standards. This requires comprehensive government action, extending beyond research and innovation to include business, entrepreneurship, skills and digital economy policies.
- ▶ Future innovation requires a stronger contribution of Ireland's domestic firms. This involves strengthening the domestic capabilities of the Irish innovation system through well-designed direct supports and a greater role for the public sector as an innovation partner, complementing the existing R&D tax incentives that are more suited to multinational firms. There is a need to focus more on the evaluation of existing policy instruments to ensure they meet their goals and provide value for money.

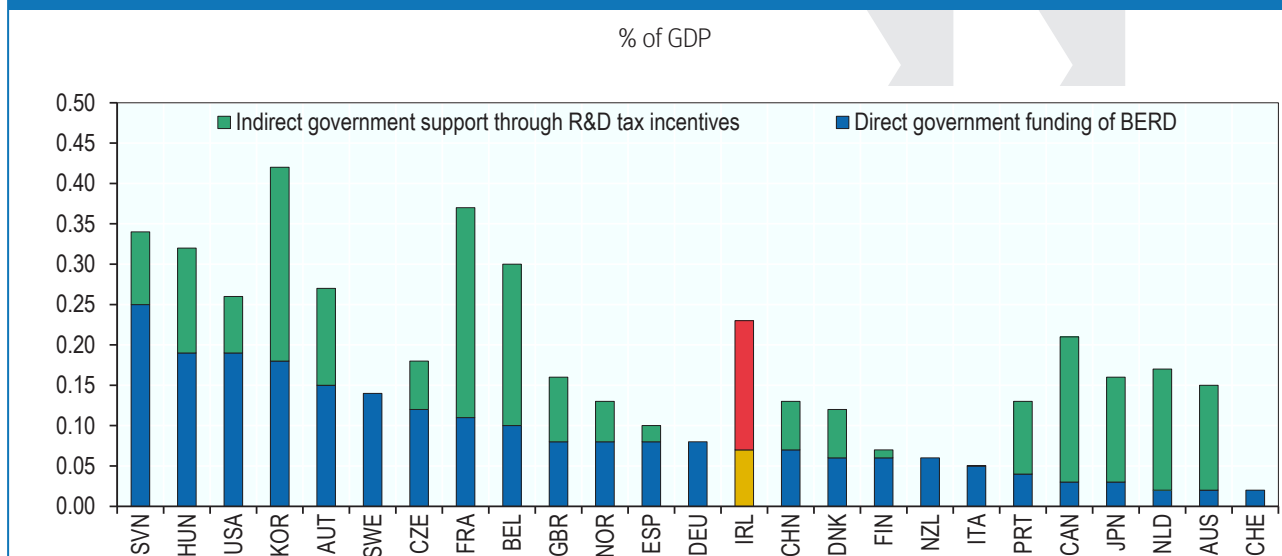
What's the issue?

More and better innovation can improve productivity, provide new sources of competitive advantage, create jobs, and support broad socio-economic development across Ireland. In a context of slowing productivity growth, the challenge is to make Irish-owned firms more dynamic and innovative, while maintaining the country's attractiveness to foreign investment.

Why is this important for Ireland?

Productivity growth in Ireland has been falling for some time. Although Ireland's multinational sector thrived through the crisis, the domestic SME sector is still lagging behind, with much lower levels of competitiveness, productivity and R&D spending. Recent OECD research shows that leading global firms, such as in Ireland's multinational sector, continue to have strong productivity growth, but other firms are falling behind. Strengthening

Ireland relies disproportionately on indirect support to encourage R&D investment



Source: OECD, R&D Tax Incentive Indicators, (www.oecd.org/sti/rd-tax-stats.htm) and Main Science and Technology Indicators, (www.oecd.org/sti/msti.htm), June 2015.

the performance of domestic firms will help rebalance the Irish economy, generate new sources of growth and jobs, and further enhance the country's attractiveness for foreign direct investment.

The government can help strengthen Ireland's domestic sector by rebalancing its innovation policies towards more direct forms of support. Over the past decade, Ireland's public backing for business R&D has come increasingly in the form of R&D tax credits, that accounted for some 70% of all government supports in 2013 (see Figure).

The R&D tax credit was reviewed by the Department of Finance in 2013, and is considered to be well designed and efficient in promoting business R&D. However, OECD research finds that such support is not always well suited to the needs of domestic and young firms. Direct government funding of business R&D in Ireland lags behind many competitor countries. OECD work finds that such direct support – contracts, grants and awards for mission-oriented R&D – is also important to stimulate innovation, particularly for young innovative firms that lack up-front funds. A well-designed, competitive and transparent system of direct supports can complement existing tax incentives and can direct public funding to areas of high social and economic returns. It can also help address specific barriers in the Irish innovation system, e.g. lack of science-industry cooperation, which is particularly important to improve the performance of low-productivity firms. More attention should also be devoted to developing the innovation capacity of the public sector, enabling it to partner with domestic firms to foster innovation in areas such as health, energy, transport and social services. Ireland's forthcoming *Strategy for Science, Technology and Innovation* offers an opportunity to strengthen the focus on these areas and scale up those instruments that are particularly valuable for innovation.

The government should also further improve the environment for Ireland's young, innovative firms. Even if only some of these firms reach a large scale, they account for the bulk of job creation, help drive renewal in the economy, and enable the growth of emerging areas. However, Ireland has relatively few young patenting firms and young firms do not scale very well as in many OECD countries, limiting their contribution to innovation, growth and jobs. The government should therefore carefully assess whether any policies (inadvertently) constrain the growth of such firms. These may include barriers to entrepreneurship, which remain relatively high in Ireland, but also access to public procurement. Other examples include regulations which only affect firms above a certain size, as well as supports for which only smaller firms are eligible. Improving the business environment for young firms can also strengthen linkages to multinational firms. Support for business accelerators and incubators, and better access to research and technology are particularly valuable for young firms and SMEs, highlighting the importance of Enterprise Ireland's new Technology Centres.

While R&D is essential, investment in innovation goes beyond R&D. It includes software, computerised information, intellectual property (e.g. patents and designs) and economic competencies, such as firm-specific skills and organisational capabilities. Innovation therefore requires a broad set of policies, including policies that strengthen the digital economy. The *National Digital Strategy* rightly emphasises the importance of digital technologies for Ireland.

What should policy makers do?

- ▶ Continue improving framework conditions for innovation and entrepreneurship, with a particular focus on the business environment for young, innovative firms.
- ▶ Improve the balance between indirect support for business innovation – through R&D tax incentives – and direct support, which is better suited to the needs of domestic and young innovative firms. Ensure that innovation programmes have sufficient scale to be efficient.
- ▶ Strengthen the innovation capacity of the public sector, enabling it to partner with domestic firms to foster innovation in areas such as health, energy, transport and social services. Evaluate support programmes to ensure they meet their goals and provide value for money.



Further reading

OECD (2015), *The Future of Productivity*, OECD Publishing. <http://www.oecd.org/economy/the-future-of-productivity.htm>

OECD (2015), *Digital Economy Outlook 2015*, OECD Publishing. <http://www.oecd.org/internet/oecd-digital-economy-outlook-2015-9789264232440-en.htm>

OECD (2015), *The Innovation Imperative in the Public Sector – Setting an Agenda for Action*, OECD Publishing. <http://www.oecd.org/publications/the-innovation-imperative-in-the-public-sector-9789264236561-en.htm>

OECD (2015), *Science, Technology and Industry Scoreboard 2015 – Innovation for Growth*, OECD Publishing. <http://www.oecd.org/science/oecd-science-technology-and-industry-scoreboard-20725345.htm>