



Asia-Pacific
Economic Cooperation

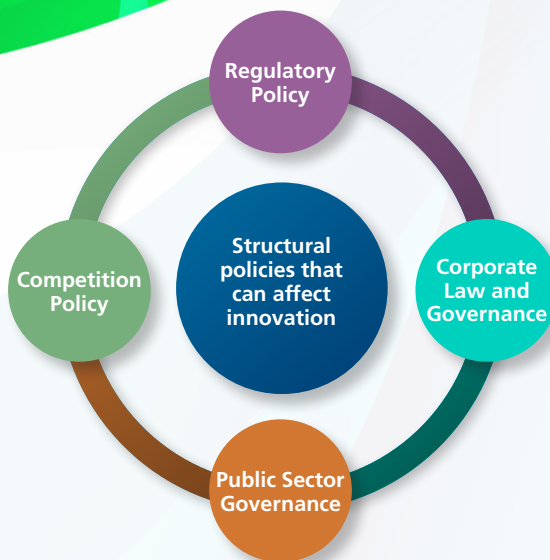
Structural Reform and Innovation

Advancing Free Trade
for Asia-Pacific Prosperity

2015 APEC Economic Policy Report

Innovation – in products, processes, designs, marketing, and **organisational approaches** – is important to economic growth and firm productivity. Productivity, and sometimes survival, of firms benefit from continued investment in innovation. While innovation is widely acknowledged as a key driver of growth, the links between structural reform and innovation have yet to be fully explored.

This year's APEC Economic Policy Report (AEPR) examines the links between structural policy settings and innovation across APEC member-economies of varying levels of development, and explores the ways in which these economies harness the growth potential of innovation through implementation of effective structural policies. Eighteen Individual Economy Reports (IERs) were submitted by member economies providing overviews of their policy mechanisms in the structural policy areas on the right.



How can APEC economies implement structural reform policies to promote innovation?

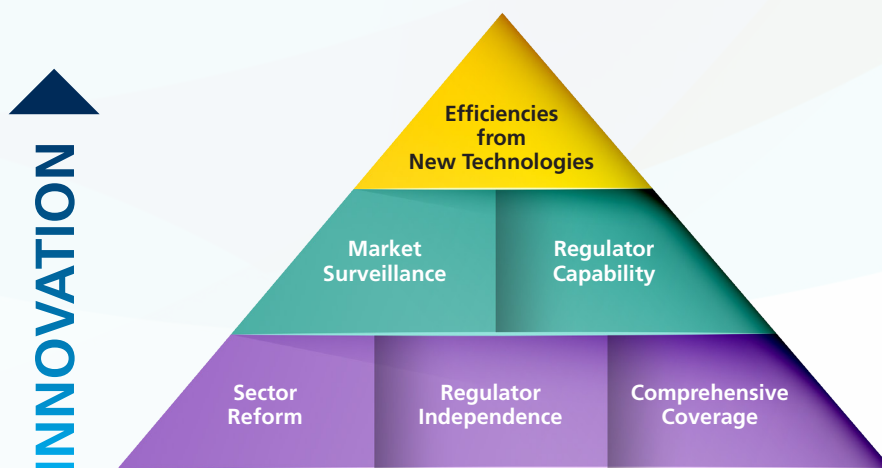
Governments – in a range of ways through **regulatory activities** – can affect variables such as risk, market opportunity, and availability of funding, and therefore, the level of innovation in an economy. The relationship between regulation and innovation is complex and multi-faceted, and defies simple characterisation. Governments need to identify and recognise the effects their policies have on innovation so that they can mitigate or remove impediments to firm-level innovation.

Competition policy for innovation starts with getting the basics right...

APEC economies have followed a development path for competition policy that starts with putting the basics in place. The diagram below indicates that comprehensive coverage, independent enforcement, and a focus on bringing competition to the least competitive sectors, take economies a long way toward jump-starting innovation, and eventually, reaping the benefits it brings. As economies build up their competition policy capabilities, there is a move towards developing a system that incorporates market intelligence and regulatory capability.

...then develops into a more nuanced focus on efficiencies from new technologies

Once economies have in place the key elements of competition law, the emphasis shifts to considering competition policy with a focus on efficiencies from new technologies. This involves a deeper assessment of competition cases, which includes predicting and allowing for the far-reaching benefits that disruptive innovation can bring to markets. It can also involve more proactive surveillance and strategic targeting of markets for their innovation potential.



Building blocks of competition policy

Regulatory policy has both direct and indirect impacts on innovation

Institutional regulatory systems that are designed to support flexible and responsive regulations encourage business innovation. APEC economies are making progress on implementing good regulatory practices. These practices, including the implementation of Regulatory Impact Analysis (RIA), promote innovation through consideration of a range of options during regulatory development. As institutional settings become more stable, economies are focusing on building up their analytical toolbox to strengthen RIA in areas such as competition policy. Economies are also recognising that improving capability is just as important as establishing the right institutional arrangements.

As economies seek to remove regulatory impediments to business growth and innovation, there is growing focus on administrative simplification to reduce compliance costs for businesses. This can remove barriers that slow down the speed of innovations to markets. APEC economies have taken a range of approaches to reduce these barriers including targeted reductions in the number of regulations, institutional mechanisms to improve regulatory quality, and removal of outdated regulations.

Good corporate governance enables innovation

A good corporate governance framework enables innovation. Ease of doing business initiatives are widespread across APEC and can encourage innovation by smoothing the transitions in the life cycles of businesses. The responses from economies indicate that:

- Majority have mechanisms in legislation that encourage managers to act in the interests of owners.
- There is a broad spectrum of approaches to the forms of capital raising used in their jurisdiction.
- Economies with advanced financial markets tend to have a greater range of options for firms to raise capital.
- An interesting trend is the move towards regulating to enable raising equity by crowdfunding using an online platform. This will allow micro and small enterprises to raise capital to grow.
- Insolvency laws can affect risk-taking and entrepreneurship.



Stable and predictable public institutions are important to innovation

Governments can have major impact on the level of innovation in an economy by putting in place a suitable legal framework and by providing a coherent national innovation system. Having a strong rule of law and supporting institutions are common themes across advanced economies and a growing number of middle income economies. The significance of state owned enterprises tends to decline as economies move up the levels of development. This indicates that placing government- and non-government-owned businesses on a level playing field opens up competition, therefore encouraging innovation. The nature of national innovation systems also evolves as economies develop, with more advanced economies tending to have separate public sector bodies for delivering an innovation policy and knowledge and innovation infrastructures.

The table below illustrates common aspects of structural reform policies and the challenges that economies of different levels of development may face:

Structural policies and challenges	Developing economies <i>(learning/ factor driven)</i>	Middle income economies <i>(catching-up/ efficiency driven)</i>	Advanced economies <i>(frontier/ innovation driven)</i>
Regulatory policy	Developing institutions to support robust regulatory policy development and implementation. Creating public participation procedures to involve stakeholders in the rulemaking process.	Implementing frameworks to identify and manage impacts of regulatory reform. Working to ensure that regulation does not inhibit firm innovation.	Implementing advanced tools to support transparency and robust regulatory policy. Using regulation to promote innovation and the adoption of new technologies.
Competition policy	Establish a competition authority to enforce competitive markets.	Establish comprehensive competition policy framework.	Sophisticated competition framework to encourage long term efficiencies from new technologies.
Corporate governance	Providing basic legal infrastructure to support the birth, life, and death of firms.	Refining corporate governance systems to enable increased capital raising and more complex corporate structures.	Advanced and flexible legal infrastructure to support firm governance and risk taking, incentivise growth and enable raising of capital.
Public sector governance	Implementing governance frameworks to support the rule of law and remove corruption or administrative abuse.	Administrative simplification, improving coordination between government agencies.	Sophisticated governance arrangements to incentivise efficient and effective public spending, taxation, and ownership (where applicable).

Innovation challenges vary depending on an economy's level of development

Several economies have reviewed or updated their innovation priorities since the Global Financial Crisis in 2008. Common priority areas now include improving the performance of the science and innovation system by strengthening the transfer of knowledge from academia to industry, and increasing the recruitment and development of skilled people to meet industry and public research needs.

The APEC region can provide an illustrative study on factors affecting the implementation and practice of innovation policy that economies, of varying levels of development, share. The IERs show that there is no 'one size fits all' approach to this end. Economies will need to tailor their policy reforms to reflect their respective circumstances and innovation challenges. In many cases, economies need to take into account their unique contextual factors (including domestic market size, firm size/structure, proximity to export markets and factor endowments) in developing the right mix of policies to support innovation.