Leveraging R&D and innovation policies to foster productivity in Czech Republic

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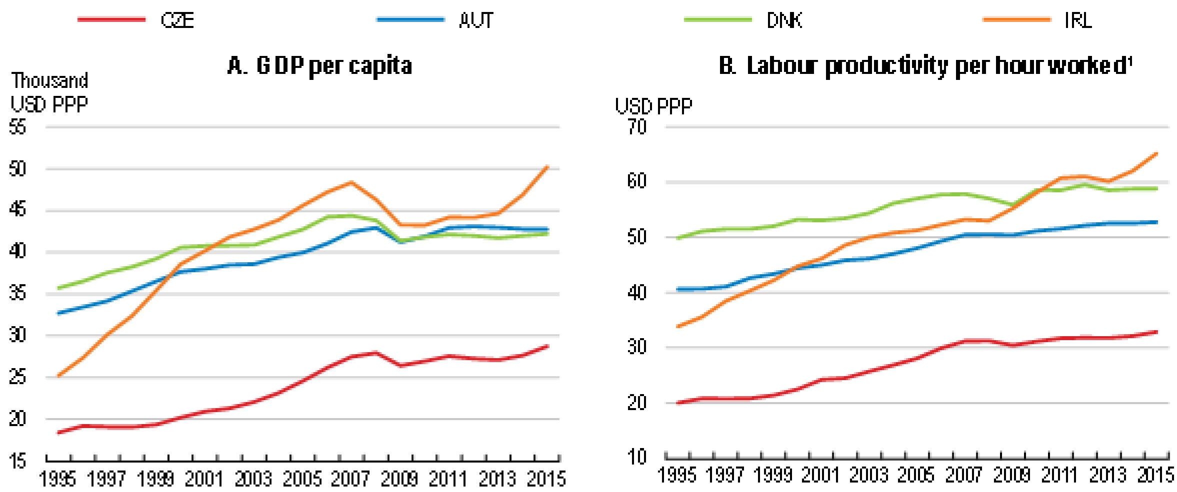
Productivity catch-up along with deeper integration into the global economy played a central role in the convergence of the Czech incomes toward OECD countries before the 2008 financial crisis. However, since then the convergence process has stalled. Labour productivity trends show a clear break in 2008 at the beginning of the crisis (Figure 1). The growth rate of labour productivity fell from 4.3% per annum in 2001-07 to 0.4% between 2008-14, and affected all sectors except finance and insurance. The strongest decrease was in manufacturing. As a result productivity is 21% below its pre-crisis trend, and potential productivity is 16% lower (OECD, 2016; Fall and Lewis (2016, forthcoming)). While cyclical developments are at play, the drop in productivity in all sectors indicates that the productivity shortfall is mainly structural. This suggests scope for improved structural policies to boost productivity in the Czech Republic.

Figure 1. Stalled convergence of the Czech Republic



1. 2015 data for the Czech Republic and Ireland are estimates.

Source: OECD Productivity database; OECD National Accounts database; OECD calculations.

Until 2008, inward foreign direct investment, international linkages of firms and credit availability had a significant impact on productivity growth. As the Czech economy is already one of the most integrated in global value chains, reviving the productivity catch-up process has to be domestically-driven. In particular, there is a need to boost productivity of Czech firms not affiliated to foreign firms and to facilitate the expansion of SMEs and the creation of new firms (Adalet McGowan et al., 2015).

More effective R&D and innovation (RDI) policies are needed to foster domestically-driven productivity growth. So far, R&D and innovation performance has been low despite a noticeable increase in spending. The increase in RDI spending should be continued as it is a key element for upgrading the economy in the global value chains. The Czech Government has put in place programmes to encourage higher business R&D spending by intensifying collaboration between businesses and research institutions. However, direct government funding of business RDI is modest, representing 0.1% of GDP in 2013. More co-financing should be developed to incentivise firms to mobilise their own resources. Well designed and properly administered tax incentives (fiscal deductions) for RDI should also be used to complement direct support. However, a balance should be maintained between different types of government funding through grants, loans, co-financing, loan guarantees and tax provisions.

Furthermore, streamlining the administration and implementation of innovation policy would increase the effectiveness of the different programmes. The organisation and administration of RDI policies is too complex. The fragmentation of innovation policies seems to be partly driven by the specialisation of the different government bodies along with a limited set of financial instruments available to each. The respective role of the different stakeholders (ministries, agencies, research institutions, councils and businesses) should be further clarified as they all intervene in the same areas. Also, it is necessary to unify the design, assessment and coordination of implementation of research and development and innovation policies in a single institution.

Reference

Adalet McGowan, M., D. Andrews, C. Criscuolo and G. Nicoletti (2015), *The Future of Productivity*, OECD Publishing, Paris, See: http://www.oecd.org/economy/the-future-of-productivity.htm

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