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# **The Use of Structural Funds for Enterprise Competitiveness Growth in the Czech Republic**

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## **The Use of Structural Funds for Enterprise Competitiveness Growth in the Czech Republic**

### **Abstract**

The competitiveness of enterprises depends not only on their strategies and operations but also on the macroeconomic and microeconomic environment in which they operate. The various instruments for business support can be found in industrial policies of EU member states, which were often successful due to co-financing from EU structural funds. The Operational Programme Industry and Enterprise uses the structural funds as the main financial source of the Czech national strategies for industry development in 2004-2006. The paper summarizes the main policies for both business environment and enterprise competitiveness development in the Czech Republic which focus mainly to the infrastructure for industrial research, innovation, industry clusters, human resources and business development.

**Key words:** Structural funds, competitiveness, enterprise development, innovation

**JEL Classification:** H50, O18, O25, O31

### **1. Introduction**

The Czech Republic is a landlocked country situated in Central Europe. The Czech Republic is a small, open and trade-dependent economy, which means that the future growth perspectives are strongly related to the performance of the European economy. Although, in the past ten years, the Czech Republic has made significant progress in becoming competitive in its relations with the outside world, particularly in relation to EU Member States, it is still below 75% of the European Union's average Gross Domestic Product (72 % in 2005). This means that the Czech Republic as a new EU member state has access to EU Structural Funds, which are the basic instruments for the implementation of EU Regional and Structural policy aimed primarily at reducing gaps among the EU regions. The Regional and Structural policy is focused to three main streams of interventions: productive environment, infrastructure and human resources development, the first of which is very important for entrepreneurship and business. Even though on the one hand the public subsidies can bring about imbalance in the market conditions of the country, on the other hand recent history of EU countries proves the positive impact on the productivity growth namely in the lagging regions.

The elementary condition for drawing on EU Structural Funds assistance is working out the applicable programming documents as requested by the Commission for that purpose. The Czech Republic drew up the National Development Plan in 2003 that further served as the basis for allowing the Commission to shape its Community Support Framework (CSF), which, in fact, is an agreement between the Commission and the government of a particular member country. This agreement defines the targeted objectives and the financial participation of the EU for the period 2004-2006. On the basis of an approved Community support framework in 2003, the implementation of the five operational programmes started after Czech Republic EU accession in May 2004. The four operational programmes have sector coverage:

- Industry and Enterprise (Ministry of Industry and Trade-MIT),
- Infrastructure (Ministry of Environment - MoE),
- Human Resources Development (Ministry of Labour and Social Affairs - MLSA), and
- Rural Development and Multifunctional Agriculture (Ministry of Agriculture - MoA).

The regional coverage is a feature of the Joint Regional Operational Programme (Ministry for Regional Development - MRD).

All programmes specified the global and specific objectives. The global objective of the Community Support Framework is “sustainable development based on competitiveness”. Public investment supported by the EU structural funds can make a significant contribution to the global objective of the CSF. The CSF strategy will strengthen the factors that contribute to productivity growth through the promotion of entrepreneurship and SMEs, the diffusion of innovation, human resources qualifications and improvements in transport infrastructure thus also paving the way for the attraction of investment and firms in structurally weaker regions. Infrastructure reducing the costs of commuting and qualifications responding to market needs will also enhance professional flexibility and geographical mobility. In addition, vocational training and life-long learning will help tackling structural unemployment.

In the context of the general development strategy for the Czech Republic are the following three specific objectives distinguished:

1. Creating conditions for business environment, i.e. improvement of the business infrastructure, improvement of institutional structure for business development, improvement of facilities for technology transfer, strengthening co-operation mechanisms between research departments and industry, boosting the innovation capacity of the private sector and increasing the added value and labour productivity.
2. Increasing labour market flexibility in order to: reduce the gap between supply and demand on the labour market, upgrade the training infrastructure in order to adapt to demands on the labour market in an effective way.
3. Improving the quality of infrastructure, i.e. transport, environment and other technical infrastructure.

For the period 2004 – 2006 the sources allocated to the programmes are given in Table 1.

**Table 1: Structural Funds Allocations in Operational Programmes**

<b>Community Support Framework (Obj. 1)</b>	<b>2004-2006</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>
Current prices – EC in mil €	1 454	339	485	630
<b>Operational Programme</b>	<b>2004-2006</b>	<b>2004</b>	<b>2005</b>	<b>2006</b>
Industry and Enterprise	261	61	87	113
Infrastructure	246	57	82	107
Human Resource Development	319	74	106	138
Rural Development and Multifunctional Agriculture	174	41	58	75
Joint Regional Operational Programme	454	106	152	197
<b>Total</b>	<b>1 454</b>	<b>339</b>	<b>485</b>	<b>630</b>

Source: Community Support Framework Czech Republic

The operational Programme Industry and Enterprise is the only one which is totally devoted to the entrepreneurship and business support. However some measures for these fields can be found in Human Resource Development and Joint Regional Operational Programmes.

## 2. Operational Programme Industry and Enterprise

The Operational Programme Industry and Enterprise for the years 2004-2006 has been launched by the Ministry of Industry and Trade. Programmes within the Operational Programme provide complex support especially to SMEs while making use of the EU Structural Funds. European funds (75 percent) will be supplemented by funds from the state budget (25 percent). Applications for financing may be submitted from 1 July 2004.

The global objective of the OP Industry and Enterprise is to contribute to a competitive Czech business sector on the European common market with a high labour productivity and efficient production. The OP Industry and Enterprise is based on three priorities in the fast track programme period from 2004 to 2006:

- Priority 1: Business Environment Development, the measures of which focus on the construction, revitalisation and development of business infrastructure, the improvement of environment for human resources development in business sector, development and improvement of informative and advisory services as well as infrastructure support for industrial research, development and innovations.
- Priority 2: Development of Enterprise Competitiveness, the measures of which focus on assistance to new entrepreneurs and new enterprises with development potential, support of innovation processes leading to the development of new products, technologies and services, support of efficient low-cost and environment friendly energy management in business sector.
- Priority 3: Technical Assistance, the measures of which focus on financing provision for the management, performance, monitoring and control of OPIE operations as well as on studies, pilot projects, information system, publicity.

There will be coordinated application of funding from the European Regional Development Fund (ERDF) and other financial instruments of the Czech Republic. There will be compliance with the Czech Republic's Industrial Policy and Regional Development Strategy.

There are eleven programmes within the OPIE that are subject to financial support. The following table presents their brief overview:

**Table 2: Specific Programmes in Operational Programme Industry and Enterprise**

No.	Measure	Programmes	Form of support
1.1	Infrastructure for industrial research development and innovation	1. PROSPERITY	Grant
1.2	Development of business infrastructure	2. REAL ESTATES	Grant
1.3	Infrastructure for the development of human resources in the industry	3. TRAINING CENTRES	Grant
1.4	Development of information and consulting services	4. CLUSTERS	Grant
2.1	Establishing and development of SME	5. START 6. CREDIT 7. DEVELOPMENT 8. MARKETING	Loan Loan ) Grant
2.2	Support of innovation of products, technologies and services	9. INNOVATION	Grant/ Loan
2.3	Reducing energy consumption and higher use of renewable sources of energy	10. ENERGY SAVINGS 11. RENEWABLE ENERGY SOURCES	Grant Grant

\*) suspended on September 2004

Source: Entrepreneur's Guide to the Operational Programme Industry and Enterprise

Enterprises may apply for support on the basis of compliance with the conditions of the programmes. If an enterprise meets all the eligibility requirements, the application is formally acceptable and when the requested appendices have been submitted, the project will be submitted to the Evaluation Committee along with the application for the grant or the combination of grant and loan.

### **3. Innovation Strategy for Industry and Enterprise**

Almost three fourths of the small and middle enterprises in the Czech Republic do not pursue any innovations, i.e. they either keep on maintaining the existing production or stagnate. The innovating enterprises, however, do not fund the innovations sufficiently. A factor analyses shows significant conclusions, which prevent the entrepreneurs from introducing innovations. Major reason for low innovation activities present high costs for innovations. Another barrier while introducing innovations feel the enterprises also in a too high economic risk. It is thus recognisable that among the innovation barriers prevail the economic factors.

Innovation is predominantly a company business. The state may assist the innovation processes by creating framework conditions for conducting business and eliminating all sorts of barriers of institutional and/or legal character. Direct interventions or measures taken by the state are admissible only in cases when the free market environment is not able to solve the problems spontaneously.

By its Resolution No. 270 of 24 March 2004 the Czech Government adopted the cornerstone document for the field of innovation – the National Innovation Strategy. The national innovation policy is (or rather should be) a part of the whole system of conceptual documents under the roof of the (prepared) Economic Growth Strategy. This strategy lies on five pillars; one of them is the chapter Research, Development and Innovation (others are Institutional Environment, Sources of Funding, Infrastructure, and Human Resources). By its character, innovation is closely connected with following two activities:

- research and development, the results of which are realised in the form of the so called technological innovation; and
- business activity, preferentially activity in the field of manufacturing, as well as services, where innovation is realised.

The Ministry of Industry and Trade (MIT) and the agency CzechInvest under its control published several documents dealing with innovation or close topics. These are in particular the Concept of innovation for industry and enterprise for 2005-2008 and Strategy of CzechInvest for 2004–2008.

### **4. The specific Structural Funds programmes for innovation in the Czech Republic**

The innovation process in CR was influenced to a considerable extent by the accession of the Czech Republic to the European Union and resulting support from the EU Structural Funds and the Cohesion Fund. Innovation is supported within Objective 1 by key OP Industry and Enterprise (programmes PROSPERITY, INNOVATION, CLUSTERS) and OP Human Resources Development. Also parts of the Joint Regional Programme of the Ministry for Regional Development (MRD) titled Regional support to enterprise, Regional development of infrastructure and Development of human resources in regions are of certain relevance. The description of these programmes is given below.

## **PROSPERITY**

The programme targets enterprises - legal entities that have proof of co-operation with a tertiary educational institution (TEI), research centre, etc. For the public sector the programme targets e.g. municipalities, associations of municipalities, regions, tertiary educational institutions, and research centres.

The objective of the programme shall be the support of infrastructure for industrial development, particularly science and technology parks, business incubators and centres for technology transfer. Support will be granted to start and develop such facilities, establish their activities, and provide preferential price services and rentals to small and medium-sized innovative enterprises.

An applicant will build or reconstruct facilities to establish an business incubator, science and technology park that will further be let out at preferential prices to innovative companies.

In the case a project involves construction work, the minimum amount of support is CZK 3 million, and the maximum CZK 150 million. For projects not involving construction work, the minimum amount of support is CZK 500.000, and the maximum CZK 30 million. The support shall be granted to the tune of 75 % of eligible costs.

## **INNOVATION**

The programme is intended for enterprises of all sizes. Generally, the objective of the program is to support the realisation of projects focused on the betterment of technical and consumer-oriented features of products and services or features enhancing efficiency in processes of production and services or to update managerial methods, restructuring or changes in strategic goals of an enterprise or some other non-technical innovation “innovative projects”, enhancing the long-term competitiveness and sustainable growth of enterprises.

Two types of projects are supported within the programme. Innovations of technical nature can include the innovation of a product and/or the innovation of a technological process. The general rule is to launch a new product or new technology on the market. Mere modernisation will not meet the requirements. An ideal project shall be focused on the phase between a prototype (semi-production) and serial production, e.g. production set out and completion of project design, implementation of a new technology to improve the product features. Projects for upgrading the quality of service are also within the scope of the programme - the purchase of any necessary technologies, licences and patents, production line, technical equipment, etc. must be exclusively related to the introduction of a new product on the market.

Innovations of non-technical nature are supported too. The programme is focussed on the introduction of new managerial methods, e.g. improvement of production process or supply logistics or the purchase of hard- and software related to the introduction of new managerial methods.

Small or medium-sized enterprises can draw on grant or loan. A combination of grant and loan is also permissible. Large enterprises may apply only for grant. The maximum rate of grant is 46 % of the eligible costs. In the case of innovation of a technical nature the minimum amount of grant is CZK 3 million, the maximum is CZK 50 million, in the case of innovations in services the minimum amount of grant is CZK 1 million, the maximum is CZK 25 million.

The SMEs can draw on support in the form of a soft loan of up to 60 % of the eligible costs of a project, the repayment period based on a provision that the loan shall be up to nine years with a deferment possibility of a maximum period of four years when the fixed interest rate is 3 % per year. In the case of innovation of a technical nature the minimum amount of the loan is CZK 3 million, the maximum is CZK 50 million, in the case of innovation in service the minimum amount of loan is CZK 1 million, the maximum is CZK 25 million.

## CLUSTERS

Potential aid recipients are regions or delegated companies, tertiary educational institutions, research institutions, and legal entities or associations of persons founded in order to carry out a cluster. Objective of this programme is to enhance economic growth and competitiveness of the economy through the promotion of sector the credits were granted aggregations - clusters.

The two types of projects are supported: search of companies suitable for clusters and foundation and development of clusters.

- The applicant in the chosen region and sector will undertake the process of cluster identification. During this process workshops, meetings, interviews, data analysis, etc. will take place. The project will result in the cluster of members, action plan, cluster strategy, etc.
- Enterprises carrying out business in a specific sector in a particular region, their suppliers and final manufacturers, and a tertiary educational institution will establish a legal entity whose purpose is to achieve suitable environment for mutual co-operation of companies, co-ordinate corporate research, development, production, and market. Such a legal entity can apply for a grant to cover costs of rent and furnishing of offices, managerial wages, other salaries, consulting services, marketing, competitive intelligence, and innovation within the individual clusters.

The minimum amount of grant is CZK 200,000 and the maximum CZK 1 million for projects of search for companies suitable for clustering. The minimum amount of grant is CZK 3 million and the maximum CZK 45 million for projects of the establishment and development of clusters. The rate of support is up to 75 % of the eligible costs of projects in search for clustering purposes and 50 % eligible costs of cluster development.

There are two types of financing in the programmes of OPIE, i.e. grants and loans. By the end of 2005 the grants were awarded for 356 projects in total sum of 2.619.701.220 CZK and bank credits were granted to 980 projects in total sum of 1.099.446.417 CZK.

**Table 3: Projects for Innovation Support**

Programme	No. of applications	No. of approved projects	No. of rejected projects
Prosperity	32	8	8
Innovation	219	35	150
Clusters	28	13	6
Total	279	56	164

Source: CzechInvest

## 5. Supplementary programmes for enterprise support

In the Joint Regional Operational Programme (further referred to as JROP) for enterprise support (within the competency of the MRD) the enterprise is subject for support within the

scope of the two priorities: firstly, it is support provided to small and medium-sized enterprises in the selected regions, secondly, the support aims at businesses active in tourism.

The priority 1 “Regional support of enterprise” is complementary to the Operational Programme Industry and Enterprise. While the OPIE aims most of all at the promotion of the entrepreneurial environment and at enhancing the competitiveness of the Czech enterprises (by means of direct and indirect support of enterprises and improvement of the entrepreneurial environment), the JROP aims at supporting the small and medium-sized enterprises and services with emphasis on the creation of new jobs in the selected problem regions. Part of this priority is also the support of non-agricultural enterprises located in the rural areas.

The enterprises active in tourism are subject for support in the scope of Priority 4. The priority “Development of tourism” is complementary to the OP Human Resources Development (HRD), in which the training of human resources in tourism is also dealt with. A more detailed information of these programmes can be found in the Programme annex to the JROP on the MRD website..

Human Resources Development in the industry is mostly subject for the support of the European Social Fund (ESF) through the Operational Programme Human Resource Development (further referred to as OP HRD) in the competency of the MLSA. The overall objective of the OP HRD is the achievement of a high and stable rate of employment based on a skilled and flexible work force as well as the competitiveness of businesses. There are again two specific programmes for human resources development in enterprises: Profession and Standard.

### **PROFESSION**

The programme is intended for enterprises in the processing industry, industrial and environmental services, and other services directly related to the above sectors. The objective of the programme is to support the professional growth of business employees needing expertise, special knowledge and skills for their work. The programme is aimed at the professional training of middle management and of other professions, such as technicians, production management, marketing, and commercial and customer services. The programme supports two types of projects: realisation of training courses and other educational activities and preparation for educational activities (teaching aids, training materials directly related to a particular educational activity).

### **STANDARD**

The programme is intended for enterprises in the processing industry, industrial and environmental services, and other services directly related to the sectors in question. The objective of the programme is to enhance competitiveness and efficiency of business through the introduction of well-established systems of management and the development of human resources. The whole system of support intends that businesses accomplish certification on a high standard in management and the development of human resources. This standard will be relevant to the best practices in European enterprises.

## **7. Conclusion**

The support of enterprises with EU structural Funds started in the Czech Republic as early as in November 2004. That manifests both the readiness of the entrepreneurial circles and the quality of preparations of the whole system for utilising the European funds through the Operational Programme Industry and Enterprise. Within a few months the programme has



unquestionably become the leading programme of support for Czech enterprises. Consequently the national programmes that were originally dominant have lost their cardinal importance, and are now playing only a supplementary role.

The Structural Funds are a valuable instrument of the EU for serving the development of the entrepreneurial sector. While in the first period 2004-2006 the enterprises were in the process of learning how to utilise the funds, in the new EU planning period 2007-2013 with a manifold larger volumes of grants the subsidies can become the real factor affecting competitiveness and growth of their beneficiaries.

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