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Towards a Unified Innovative Market

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Building a Platform for a Common EU and Russian Economic Space

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Resume A unified Euro-Russian innovation market is capable of ensuring a multiplication effect for any individual investor. Instead of an integrated European energy grid, which has been suggested by the European Union as an artificial incentive for competition, it would be better to create an integrated Euro-Russian innovation network.

The drive towards innovation is probably the only force unifying both Russia and the European Union today. In the modern world it is not the production of knowledge (in the broad sense of the word) that makes a country powerful, but the effectiveness of its use in the economy. The recent financial crisis was a particularly emphatic reminder, with the threat of further recession still hanging over the world like the sword of Damocles.

The conservative approach to fighting economic recession is dictated by protectionist measures. The national markets of EU countries were suddenly concerned about borders; these countries isolated themselves and closed themselves off from the outside world, as if the European community had never existed. Yet the establishment of the EU had required tremendous efforts and decades of difficult work. Indeed, it proved to be the most outstanding event of the 20th century.

In actual fact, however, a return to isolation and autarchy is unrealistic. The more effort we put into raising living standards, the more we are aware of mutual dependence. Russia, not being the strongest element in the world economic system, was one of the first to realize the truth of this. In its bid towards integration – be it local, regional or international – both the state and business are ready to pool their efforts.

Russian Prime Minister Vladimir Putin urged his European colleagues, while leaning on “progressive forms of economic integration,” to abandon a conservative approach to partnership relations in favor of an innovative one. For example, he called for joint industrial policy, based on concentrating the technological and resource potential of Russia and the European Union.

Putin suggested that special attention be paid to opportunities for pooling efforts in innovative business. Russia has stated firmly that modernization is a key priority of its industrial policy. Skolkovo, the innovative research center being set up outside Moscow, should be the first move towards building an innovative economy. As initiator of the project, the government assigned the decisive role in its implementation to business. For its part, the business community saw the tremendous potential of this idea, which provides for long-term development.

Curiously enough, Great Britain has also announced plans to start similar innovative research centers – with tax breaks, liberal legislation for immigrants and other incentives. This is not a coincidence, as the drive towards innovative breakthroughs becomes commonplace in modern economic policy.

Few may have noticed, however, that the initial idea is innovative partnership on a global scale, aimed at creating conditions for bold innovation and launching such innovation on the broadest scale. Truly innovative developments cannot have national constraints; otherwise they would not have come into existence and, most importantly, would not have found a market for their use. It is

business – Russian and European – that is ready to start building relations aimed at forming a common Euro-Russian innovative space.

Our experience shows that the perception of traditionally conservative European investors preferring to channel money into high-tech innovation in the final stages is outdated now. After all it was Europe that implemented the Large Hadron Collider project, which brought together scientists and specialists from many countries into one creative team. The participants in the project are developing their own programs, whose combined result yields a tremendous effect in reaching the common objective. Although the Collider experiment is unique in itself, the mechanism of its organization and implementation can be applied in other fields.

The time has come to set the task of forming a unified European innovative market. The practical development of innovation begins with the search for innovation, whereas creative work is hidden from potential consumers. According to various estimates, research takes from 30 to 60 percent of time and funds. The risks, inherent in any innovation, are incurred in case of errors in selecting innovations that can ensure the return of invested money and labor. Venture capitalists increasingly have to do with the decile return rate, i.e. just one project out of ten yields an effect that covers all expenses.

All this leads to the market's most important institution – demand, which exists independently of another institution – supply. This causes a dissonance that defies regulation. On the one hand, a tremendous number of potential innovations are created, which gain true significance only on the market as a result of purchase/sale operations. Yet such operations are scarce, because it is impossible to tell in advance if this or that innovation will be needed or how useful it will be.

On the other hand, innovation is needed in the production of goods and services to expand market niches. Up until now the search for innovation that meets the market's expectations has been unsuccessful. The more closed and localized this sphere of trade turnover is, the more difficult it is to resolve this contradiction.

The process of creating and developing innovation requires a fresh look. We suggest that the search for innovation be carried out by a specialized market, i.e. the innovative market. Broadly speaking, this would imply the free turnover of innovative products ready for sale. The winner is the one who is the first to manufacture an innovative product. In other words, competition in coming up with innovation is replaced by competition among users.

At the stage of the innovative product's development, competition slows down the entire process and sometimes leads to duplication and numerous dead ends. This situation can be remedied by cooperation, as it provides for bringing together representatives of various fields of knowledge and engineering, thus cutting back on R&D time.

At the commercial stage another factor plays a key role; namely, the level of perfection of the entire corporate system. This includes marketing, banking and operational and strategic management. The competitive mechanism does not slow down innovative development at this stage: it is rather a catalyst, a sweeping force that fully mobilizes all the reserves, taking hold of the missing elements in management and practices, as well as in the use of advanced information technologies.

The Russian business press describes another systemic contradiction in building an innovative economy. Schematically, innovation can be represented as follows: a subject of innovation (a company) funds R&D and gets an innovation in return, which either increases the value of the goods the company produces for its consumers, thus boosting its revenue; or reduces its costs. In this way a company creates added value which it keeps as profit. Alternatively, it may go to competitors and customers who get better quality products for the same or even lower price.

Thus, there is a seemingly paradoxical conclusion: the economic appeal of innovation for a subject of innovative activity depends on how effective the barriers are to the spread of the created

innovation, as it directly affects the innovator's profit share. The longer a company derives it, the more attractive is the return on the capital invested in innovation.

However, the growth of the economy (not just one company) requires a high rate of the spread of innovation, so the barriers against this must be reduced. The state of the economic environment may have a considerable influence on the innovator. It might be even depressing: a state budget deficit may cause changes in the tax code.

If we consider the global market from this point of view, we have to say that its innovative component comes under pressure from these contradictions. Consider the development of information technologies for example. The wide-scale distribution of technology lowers its price on local markets, but increases the cost of the key technologies of its use on global markets, as well as the standard costs, algorithms and harmonizing elements. It follows that the faster the innovative product gets to the world market, the more effective it is. The less time spent on winning local markets, the faster the product is promoted to the global sales level. It is this opportunity that a unified innovative market provides.

Due to the specifics of innovative products this market is characterized by a range of special features. Having no opportunity to fully analyze them, I will name only a few.

First of all this market should be open, i.e. its participants are exempt from payment of duties on exports/imports of innovative products, similar to the EU's liberalization of the market of air transportation (under the Open Skies agreement). Even such a sensitive sector as defense and security has undergone a surprising change as Great Britain and France have pooled their efforts to defend their national interests. Specifically, the two countries have agreed on joint technical maintenance of nuclear weapons; that is, on interaction in the innovative development of their nuclear potential. The liberalization of the innovative market does not sideline national interests; innovation simply ceases to be an exclusive, solely scientific discovery as it enters national innovative systems that provide the conditions for the manufacturing sector to develop innovation in the global (European) market.

For example, head of the Nokia Research Center Dr Henry Tirri is an ardent supporter of the model of open innovation, even though he believes it should be limited to the corporate level. Yet it is the key motive behind this openness that is important – it is not sufficient to just create an innovation, it must be promptly launched into mass production.

The innovative market is very special in that consolidation is contraindicative to it. The market is for individuals, even if there are large players on it. As a rule, the market needs consolidation to maintain liquidity and requires a continuous reserve of huge funds. The innovation market does not require liquidity because it is inherent in the market, therefore special provisioning is unnecessary.

Incidentally, the export of capital, which causes serious concern among financial officials, is largely explained by a lack of investment targets in the domestic market or because these targets are not attractive enough. In the same way, the export of innovation to external markets compensates for insufficient demand in the national economy, but eventually it will stimulate production much more effectively than any administrative measures.

Countries that have accumulated tremendous reserves have set an objective to conquer external commodity markets. The innovative market will not be very attractive until consumers start to appreciate an innovation as a commodity, and then the market of such innovation will turn into a commodity market. That is why, despite its specifics, the exchange of innovative development, distribution and use meets all the requirements of a market institution.

Another distinctive feature of the innovative market is that its subjects are the centers of competence, not centers of profit. Admittedly, the former have far greater capabilities for cooperation and that is why the innovative market should be created as a unified one, with national frameworks being conventional (or informative at best).

As for the legal protection of intellectual property, there are acknowledged procedures to transfer any patented innovation on the international market to the national domain, for example, the Patent Cooperation Treaty (PCT) procedure. In 2008 alone, Russia transferred more than 80,000 applications to its market through the European Patent Office. In copyright law, the concept of "copyleft," as opposed to copyright, has been gaining momentum, as it envisions free use of an invention without registering it as an object of copyright law. Similarly, innovation can receive "citizen of the world" status.

The recent financial crisis forced the EU to create a huge stabilization fund. The EU can use this fund to resolve short-term socio-economic development problems, but this does not mean that the EU is exempt from rescheduling debt payments. The need then appears for an effective mechanism to ensure economic growth, unrelated to fiscal policy and protected from speculative attacks. Designing a unified innovative market stimulates the desire to set up an integrated fund to finance innovation. This market can be a virtual one, i.e. money can be managed by national innovative systems.

The structure of the innovative market can be virtual as well, similar to a social network, as the innovative capability of the modern economy is not created by large organizations, but by a network of entrepreneurs which brings together individual groups of developers.

The network theory shows that it is a network exchange of information as a result of spontaneous interaction that contributes to the implementation of economically effective projects in innovative communities. In this sense, a unified Euro-Russian innovation market is capable of ensuring a multiplication effect for any individual investor. Instead of an integrated European energy grid, which has been suggested by the European Union as an artificial incentive for competition, it would be better to create an integrated Euro-Russian innovation network.

The joint Partnership for Modernization initiative has fixed the parties' resolve to remove barriers on the way to innovation. By way of response, business communities might take steps towards creating conditions for the joint development of innovation. Back in 2009, the EU-Russia Industrialists' Round Table submitted a proposal to a Russian-EU summit to begin a new innovative dialogue, whose mid-term objectives include the establishment of a common innovative market.

This dialogue might help draw a "road map" to establish a unified innovative market. The parties should pay special attention to the development of new forms of private-state partnership, specifically to functional clusters. The idea is quite simple: to consolidate structures linked functionally, not enterprises that are located close to one another, that operate in various branches of the economy.

This would help prepare optimal conditions for both inter-state and inter-branch interaction among various spheres of knowledge and production, as well as for the rapid mass production of innovation. It would facilitate the diffusion of innovative approaches, ideas and solutions with respect to new tasks, and also contribute to a competent and professional management of all these processes.

The establishment of clusters has long been part of the global practice of industrial policy. Clusters cannot be formed by forcing companies to work together by administrative levers, without taking into account the real prospects for implementing economic activities. The fact that several companies from a certain sector of the economy use or tend to use the same technologies does not imply that these companies will make a real cluster; cooperation between them is required, as well as the involvement of the services sector.

None of these objectives can be achieved by the force of administrative levers without objective market prerequisites. Furthermore, overemphasizing administrative regulatory measures can create additional barriers to innovative clusters. Such regulation can effectively become a straitjacket for business instead of a fruitful playing field.

The key factor in creating an atmosphere of trust and ensuring broad and stable demand is the participation of large businesses in the clusters. Innovative clusters play a dual role: as innovators that attract subcontractors to implement their projects and as generators of demand for the services of innovative companies among small and mid-sized business. Companies also provide orders and markets for intellectual development. Clusters made up of small and mid-sized businesses have a smaller potential for dynamic development, mostly due to a lack of access to considerable financial resources and an inability to generate stable demand for products of associated economic sectors.

Support by the European Union and Russia for such functional clusters would help fulfill another key task – to involve regional and sub-regional authorities in each of the EU countries and Russia in shaping and implementing an innovative policy.

For example, CIS countries, while pursuing the goal of boosting the competitiveness of their economies in general, are working on an inter-state program of innovative cooperation and want to integrate all countries working in science, technology, innovation and education. As a result, the fledgling innovative market could be truly unified.

We expect an adequate response from our business partners and believe they are ready to jointly build a platform for cooperation if only because it is equally advantageous to all. A unified Russian-European innovative market should become a joint project for the economic policy of Russia and the European Union and a platform for real integration.