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**Research Report**

Socio-economic assessment of the Danube Region: State of the region, challenges and strategy development. Final Report Part II: Summary and recommendations

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# **„Socio-Economic Assessment of the Danube Region: State of the Region, Challenges and Strategy Development”**

## **Final Report Part II**

**October 2015**

## **Summary and recommendations**

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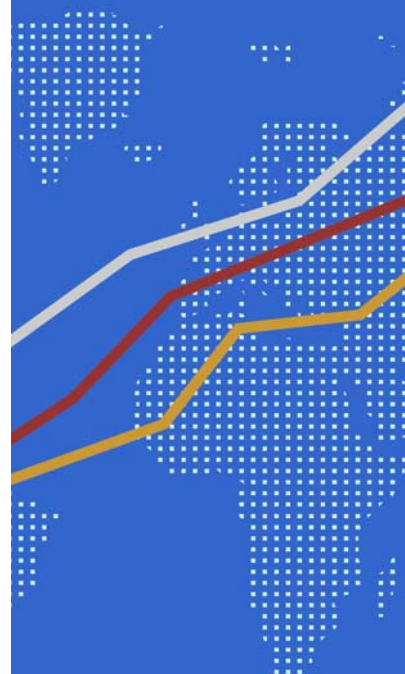
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## **Remark**

This is the last chapter of the second part of the study on the socio-economic development of the Danube Strategy. The full report will be made available as soon as it is approved by the client of the study.

## **7 Summary and recommendations**

### **7.1.1 How did we proceed?**

This policy formulation exercise is based on the outcome of the focus group and the online discussion. Both processes are used to get a meaningful understanding of the shortcomings, problems, and threats, but also visions, hopes, and communalities in the perceptions of people in the Danube Region, as well as hints for potential projects to be launched under the DR banner. Participants have been involved in some way or another with the EUSDR by implementing, analysing or being addressed by the strategy. This heterogeneity is intended, and helps to get a better understanding of the diverse and maybe also diverging views of the strategy.

Both the focus group and the online discussion were analysed in detail. The most salient features are the starting point for the formulation of suggestions. With hindsight, participants in the focus groups were very open in addressing problems, shortcomings and omissions of the EUSDR directly, with little moderation but in a very constructive way. Other participants mostly agreed or presented their points of view. There were no unresolved issues left over in the focus groups.

The document discussed online presented an overview of opinions raised during focus groups. The online discussion intended to validate these statements with a larger crowd.

Of course, the participation (i.e. voting and commenting) on [discuto.io](https://discuto.io) – which was the discussion platform used – often reflected the personal situation and opinions of participants. The specific insights of participants help to move away from generalised statements toward a more focussed analysis of the real issues that drive developments.

Still, the task here is not to simply mirror what the community suggested but to better understand the problems and then come up with suggestions for solutions/measures/action and projects. The proposed measures may overlap with ideas from the community, but may also reject some of the suggestions or frame them differently, or make them dependent on the fulfilment of other criteria. In any case, the reasoning for suggestions is given here.

The proposed measures — and this is very important — are seen as untested hypotheses although great care was taken to make them evidence-based and responsive to the actual problems of the EUSDR. Knowing the problems is an important part of crafting solutions but not a sufficient one. There must also be a mandate and a drive to actually change the situation. This is probably the most important task left for the people involved in the DRS: to find out which of the suggestions “fly”, i.e. get enough support from actors throughout the Danube Region Area. Not only investing sufficient resources, but also having a chance to see implementation. In other words, the problems tackled should be real and on the agenda of decision-makers so that they are willing to invest time and money. Testing may encompass getting a political mandate as well as reaching out to enterprises, ministries, research institutions etc. Self-mandated activities without “testing the market” are necessary in some areas, but — given limited time and resources — now seems the time to focus on activities that are already seen by all actors as a problem that needs to be solved.

In the following section we briefly summarise the main insights and suggestions from the focus group and evaluate how the community responded. We then analyse which policy level they are addressing and what responses the DRS might deliver.

### **7.1.2 Between Olympus and despair**

The Danube region comes with many attributes: a large, diverse and creative region that is a huge market with the potential to develop into a major supplier for European and global markets. The Danube Region is of importance for many people, although there is no commonly shared narrative behind the region. Instead there are many facets that let people personally and emotionally connect to the region. The participation in this process — particularly in the online discussion — is a clear indication that people are interested in the future course of the Danube Region.

The DRS is seen as a major vehicle to create attention for the region. “Without EUSDR the region would be almost forgotten” is one view often encountered. In the worst case, if all other things underperform, it keeps the region visible and on the agenda of policy-makers in the European Union.

### **7.1.3 Problems at home — salvation from abroad**

Creating attention for the situation and challenges in the regions is relevant because many participants count on outside help for mastering the change process ahead. It is clearly the European layer — in the frame of the DR, Austria and Germany — expected to lead in this catching-up exercise. Local governments and public administrations are not perceived as a stable factor in economic development. This is because strategies — if existent at all — are not being implemented, priorities are being changed frequently, responsibilities and responsible persons are moved around in unpredictable ways, there is corruption, short-term policy-making etc. Changes in the administration and erratic moves are mirroring developments in the political sphere. This is not the sole responsibility of local administrations and not valid for all to the same extent, but a reality in many regions.

For a functioning catch-up process and to knit closer ties within the Danube Region, the public sector must be in the driving seat — relying on efficient structures, well working processes and fast decisions. This includes being responsive and accountable to citizens. Many of our participants from catching-up countries — and probably also in the more advanced regions — would not see a large overlap between the present functioning of the public sectors and these demands.

While local public administrations and the political system only get lukewarm cheers, many of the projects to be taken on by companies, entrepreneurs, researchers, and the civil society need public support. This is presently not available locally; only at the European, and sometimes at the bilateral, level.

This creates a dilemma for those that would like to act. European initiatives are far away with high thresholds for participants, and thus for many not an option. This would be exactly where the Danube Strategy could have come in: just in between the demanding European programmes and the (not yet fully) working local initiatives.

This constellation has set the bar high for the Danube Region Strategy. Maybe too high. The Danube Region Strategy has not filled this gap and is consequently — for the right or wrong reasons — not spared from critical comments. Four years into operation, the number of critical statements and overt criticism is substantial throughout all countries of the Danube Region. Despite

visible activity in the political sphere, high-level conferences and meetings, the “trickle down” effect seems to be pretty small, if notable at all, for those involved in focus groups and the online discussion. This concerns both cross-country cooperation projects as well as the business climate in Danube Region countries. None has seen substantial change, nor grand momentum-building that could be attributed to the DRS.

Interestingly, both representatives from advanced countries as well as from catching-up countries are critical of the DRS — but for different reasons. Actors in Austria and Germany — countries that could support development in other regions of the Danube Region — are frustrated by slow progress made in framework conditions and by the unpredictable moves by politicians and public administrations. Those on the “receiving end” are frustrated by the great difficulties encountered when trying to integrate into value chains or scientific networks, as well as by the slower than expected and unevenly distributed economic development.

#### **7.1.4 Aiming high**

At the same time the ambitions for economic development are high throughout the region. Statements that suggest focussing first on medium- and low-tech industries meet strong resistance or are at least controversial. An immediate transition to the level of the most-developed countries seems far more attractive and the only acceptable way forward for the discussants. Of course, this must be the long-term objective but until then a lot of steps have to be taken. It is unclear if such a gradual catching-up process would meet much support. It is not yet fully acknowledged that solid fundamentals — i.e. rule of law, property rights, functioning administration, little corruption, working infrastructures, etc. — increase the return on investment of public and private investments substantially, and also create room to manoeuvre for citizens, institutions, investors and enterprises. Aiming at a more inclusive development process should be one of the prime tasks.

#### **7.1.5 Projects, or what?**

The Danube Region Strategy is broad in scope and already addresses a variety of topics. Scouting for projects was one of the motivations for the focus groups and the online discussions. Actually, the definition of a project is de-



batable. A project can be a big change process for the country or region as well as a piece of research done by a group of researchers.

The present scope of the DRS — a look at the priority areas will confirm this — could accommodate the big change processes (macro level), programmes that focus on particular issues (meso level) and actual projects that are set up by individuals in enterprises, research institutes, universities, administrations, etc. (project level). The further up in this hierarchy, the more planning and strategic thinking is demanded, as well as some top-down management of the issues. The further “down” one is, the stronger is the bottom-up principle in developing proposals and setting up projects. Without further delving into this matter, we received suggestions for projects mostly for the macro and meso levels, i.e. big change projects and programmes that could help to bring about change.

The focus groups and also the online discussion clearly showed huge demand for improvements and reforms across the Danube region. Here are the main, unfiltered macro **topics** that should be on the reform agenda as seen by the participants:

- **Public sector** is not helpful in developing projects, nor in creating conditions for companies and the economy to prosper. The state is not a catalyst but a brake. Not effective in sorting out problems but being part of the problem. The intervention logic is not thought through, and consequently neither efficient nor effective in intervening — instead hampering all other players. This view points out problems but ignores the workload that is handled by the public sector on a daily basis.
- **Strategies** are rarely developed or not implemented if developed. Activities in the public sector are not coordinated and frequent political changes, shifting responsibilities and persons create an unreliable partner over time.
- **Corruption** is a huge problem within many countries and for foreign companies that would like to locate in the region. It also increases the number of people that leave the country.
- **Lack of trust** is also a big impediment to (cross border) cooperation.
- **Property rights** are not clear and are difficult to enforce.

- **Short-term perspective** dominates long-term perspective.
- **Education system** supply and demand are not coordinated. This already slows down FDIs and entrepreneurship.
- Lacking tradition of **entrepreneurship** and non- or only partially existing eco-systems for start-ups. Entrepreneurial success is not valued by society but seen as indication of wangling with elites.
- Upgrading and integration of local companies into existing high-end **value chains** is seen as almost impossible by some, while high on the agenda for others. This stands for the overall ambitions in the catching-up process: being on a par with the most developed countries rather than locked into catching-up mode.
- Foreign direct investments often do not connect with local companies; skimming support and then leaving.
- Even local governments buy almost exclusively from large foreign-owned companies.
- Products from catching-up Danube Region countries don't yet achieve the same quality level as their international competitors and thus have to compensate by offering a lower price.

The above list of problems is, of course, a good starting point for a reform agenda that has to be tackled by national, regional and local governments. Any projects on the macro level that should be done within the framework of the Danube Region Strategy would need a strong mandate from political decision-makers to stand a good chance of being implemented. But there were also suggestions for a number of other **programmes** at the meso level:

- Establishing exchange programmes for students, public sector employees, trainees etc.
- Mentoring programmes for the public administration
- Establishment and expansion of town twinnings
- Programmes that strengthen local SMEs
- Introduction of a system of dual vocational training

- Mentoring programmes for SMEs
- Organising start-up weekends
- Establishment of start-up incubators and accelerators
- Using crowdfunding as a means for selecting promising companies
- Training for developing project applications for EU projects
- Helping accession and neighbouring countries with EU standards
- Creation of a fund for feasibility studies
- Establishment of a state guarantee scheme for SME loans
- Establishment of the German model of public-private equity investment companies ('Mittelständische Beteiligungsgesellschaften')
- Mapping of the value chains in the Danube Regions
- Harmonising regulations between countries

The third group of **projects** — those that we were actually looking for — are those that could be financed by European programmes. Almost no ideas that fall into this category were discussed in focus groups or online. These projects are obviously not floating around but will actually be developed when a suitable tender is advertised or viable cooperation opportunities arise. We assume that there is not a lack of ideas, but that potential ideas for such application are not openly discussed.

A recent observation that corroborates this view is a tender for Eureka projects that was advertised throughout the Danube Region and resulted in 88 projects from 287 participants. It is yet unclear how many will pass scrutiny but nonetheless this is a strong sign of the potential that is in the region and has to be kindled.

#### **7.1.6 How does this all fit with the EUSDR?**

The Danube Region Strategy is addressing the big issues for all catching-up countries as well as some more down-to-earth aspects of managing common

resources, i.e. concerning the Danube, energy, tourism and the environment<sup>1</sup>. It comes with governance structures that manifest themselves on three separate governance layers (European, national, regional, see European Commission, 2014) and has involved administrations, business, research and education organisations and the civil society in both catching-up and more advanced countries.

Nonetheless, the activity “on the ground” has been limited due to the three NOs (no new funds, no new structures, no new legislation) and difficulties in accessing existing funding mechanisms, particularly the European Structural Funds that came with programming objectives and logic that was not compatible with the DRS (i.e. focussing at the country level and not at cross border cooperation). Thus the DRS has predominantly been a “motivation machine” to take up issues that are high on the European policy agenda, to cooperate on finding solutions and to knit closer ties between the countries in the Danube Region. In some areas the DRS was also a continuation of work that had already started before the strategy was enacted. Cooperation on water transport and environmental issues was continued in the framework of the DRS and resulted in projects. The progress made there was substantial but expectations were high and different.

The high visibility of the DRS, despite the inability to invest in change processes, may explain some of the frustrations observed. This may be due to overenthusiastic communications that created expectation that could not be met or did not explain the working of the DRS and its likely impact in a realistic way. At the same time, the bulk of cohesion policy is executed through structural funds and most tangible results should have been achieved through this channel. If there were too few results, the blame should go to cohesion policy actors rather than the DRS. The latter may consider a different approach to communicating the merits of its activities.

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<sup>1</sup> Here we are almost exclusively concerned with the big questions that are related to catching-up issues. Thus PA7 to PA11 are in the limelight. This is a result of the topics that were raised by the focus groups and in the online discussion and should not be interpreted as an attempt to belittle the importance of other DRS PAs.

### **7.1.7 ESI Funds — an afterburner?**

This situation has somewhat changed: The Danube Strategy has become integral part of the partnership agreements for the use of ESI funds between Member States and the EU. There are other programmes on the European level that can be used to fund initiatives from the Danube Region (e.g. Danube Transnational Programme). Still, the overall endowment of the DRS is poor if compared to ESI funds. Many observers see this as a major flaw in the design of this strategy, and thus strive for new funds.

Actually, the present setup of the Danube Strategy should rather be seen as a challenge. The Danube Region Strategy is not the only initiative in the region. South East Europe 2020 Strategy (SEE2020), the Strategy for the Adriatic and Ionian are two other initiatives which cover part of the DR countries and are — if it comes to general development goals — overlapping with the DRS. European Bank Reconstruction and Development (EBRD) and World Bank Group are also active in the region and the largest tranche of European funding is available through the European Structural and Investment Funds (ESIF).

Given this situation, some of the countries can decide where to launch and support activities. The recent initiative to set up a Western Balkans Research and Innovation Center, supported by Albania, Bosnia and Herzegovina, Croatia, Montenegro, Serbia, Kosovo, and the former Yugoslav Republic of Macedonia, is a good example for the options at hand. It might be an indication that another grouping of countries is a better setting for some of the big issues in the region than the Danube Strategy.

From the outset, it is not obvious which arrangement is best suited to deliver progress in terms of catching-up policies. A first indication of the relevance of the Danube Region Strategy, and the services offered by this macro strategy, is the importance given to the DRS in the partnership agreements between Member States and the Commission for the use of ESI funds. If there is only lip service paid, this should be taken as a clear indication that the services are not valued by this country. Formulated differently, the Danube Strategy is of relevance. But only if decision-makers in catching-up countries consider the services it renders — i.e. cross country cooperation, learning from more advanced regions, creating synergies by tackling problems in a coordinated way etc. — to create added value for the cohesion process. It is up to these coun-

tries to allocate resources, to decide on the course and to shape the programmes. In this sense salvation must come from within, must be based on cooperation and must be mandated by the highest political level.

The same logic applies to accession and neighbouring countries. If they do not come with a convincing change agenda, working governance structures, and have to be drawn into projects that are then half-heartedly executed, no big change projects should be started.

To put this line of argument as bluntly as possible: the main driving force in the DRS should be the reform agenda in the catching-up countries, shaped by clearly voiced demands, the willingness to invest and to reform structures in the countries. There cannot be salvation from outside if there is no will to embrace reform among the elites of the catching-up countries. Any other approach would fall in the “rent seeking” category.

It may be added, that catching-up processes take a long time. They take even longer if reforms are not done, or done half-heartedly. East Germany may be a good illustration of this issue, where decisive and sustained initiatives were taken to modernise this part of Germany. Although big progress was made in the past 25 years, this is still an ongoing process.

#### **7.1.8 Inclusive or extractive?**

Presently, the elites are weighing their returns in a reformed system vs. the present arrangement. The lack of reforms/visible changes in some of the catching-up countries simply mean that the present situation is preferred by those taking decisions. This is in preference to yet-to-develop future arrangements that might create more opportunities for more people at the expense of present privileges. The inability to understand the challenges ahead, or lack of knowledge of how to change systems or to secure support for system changes, is rarely the root cause for missing reforms.

Changing these patterns is crucial for long-term development. Otherwise countries may be locked in or stay in a vicious circle caused by man-made political and economic institutions. One that does not create incentives to invest in education, does not reward innovation, and does not allow everyone to participate in economic opportunities and maintain governments and admin-

istrations that are accountable and responsive to citizens (see for the full story Acemoglu and Robinson, 2012).

The frustrating interactions with public administrations and governments, the level of corruption, etc. reported in the focus groups and the online discussion by a great number of participants already hint that the economic and political institution are far from inclusive<sup>2</sup>. The responsibility for changing the situation is with (local) governments, with help from European Union, assisted by the actors in the DRS. Civil society, which should be another driver of change, seems not to be in a position to accomplish this task on its own and thus has to receive more support. Intensifying ongoing activities in the DRS is definitely advisable.

#### **7.1.9 And now for something completely different**

So, to summarise the top-down approach, the large change agenda that is behind the Priority Areas of the DRS can only be tackled if there is a political consensus what DRS and consequent action should accomplish.

Four years into the strategy — or six years after the main decision — seems to be a good moment to demonstrate that the framework under the Danube Region Strategy is able to deliver.

A prime task would be to reform the public sector, with the intention to increase the capacity to process the workload associated with a large-scale change process. The composition of DRS partner countries is well-suited to accommodate such a process by setting up twinning and exchange programmes based on a solid strategy.

Additionally, it would be just in time to formulate, until the end of the 2015, six projects that have broad political backing — at least the foreign ministers are fully behind the DRS (see their joint statement from May, 13<sup>th</sup> 2015, EUSDR, 2015) — a network of motivated partners that wants to move the area forward, is able to secure funding for the projects and start implementation ASAP. The just-started Danube Strategy Point should play a pivotal role in this

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<sup>2</sup> It might, of course, also be discussed to which side Europe as a whole has been leaning in the past years.

endeavour and coordinate joint action across Priority Areas. There is a clear need for horizontal policies instead of isolated silos.

The emphasis should be on projects that solve real problems in the DR and should employ a strictly opportunistic selection mechanism. If there is no support from the ground and from political decision-makers — and support here means willingness to act — then no projects should be started. It is up to the proponents to identify the necessary contributions from different players, right at the beginning and to get their commitments arranged accordingly.

The nature of projects is important but should not be the main concern. Preferably, projects should tackle those issues that are the fundament of modern competitive economies, i.e. rule of law, property rights, functioning administration, little corruption, working infrastructures, etc.

A change process to improve the efficiency and effectiveness of the public administration should be high on the agenda but may lack political backing. Cross-border learning with respect to qualification and advanced education would be also interesting if the focus on implementation is strengthened. For example, cooperation between scientific, public and private institutions, exchange programmes for students, trainees and public sector employees, and support in the introduction of dual-vocational training. Last but not least, strengthening SMEs in the region is of great importance. All may already build on some initiatives already started, with the overall aim to increase knowledge absorption and thus the speed of catching up. This list is of course far from being exhaustive and should be adopted through discussions across Priority Areas.

Accessing and neighbouring countries should be particularly motivated to join with the intention to modernise their structures so that action match ambitions. The latter point is also true for other countries.

Actually, and this brings us to the meso and project level, the financial restrictions in place during the first years of the DRS are mostly gone. It is still a challenge to set up programmes but the opportunities to fund projects have grown substantially.



At the project level, the ESI funds should allow funding in almost all areas where projects under the EUSDR<sup>3</sup> umbrella might pop up. Funds for community-led local development (CLLD) are another source as well as the Danube Transnational Programme that was designed to support implementation of the DRS. Furthermore European programmes like Horizon 2020, Erasmus+, COSME, LIFE, CEF, EU Investment Plan are other options. The planned Danube Region Research and Innovation Fund will not materialise — at least not as a funding organisation (see for more information the feasibility study by EY, 2015) — because of financial constraints. The DRS itself is thus equipped with limited resources but should be helpful for potential applicants in accessing other funds.

Experience with participation in some of the above-mentioned programmes is mixed. In general, there are no indications of a shortage of projects emanating from DR countries — rather the opposite. If the Start programme is taken as an example, the funding opportunity organised by PA 10 resulted in 635 applications, of which 25 got funding. In the recent Eureka for the Danube Region call, 88 proposals were submitted by 287 institutions. In 2012 the number of ideas and projects within the EUSDR itself amounted to 491 (see Metis, 2012).

In stark contrast, the participation in past Framework Programmes and now Horizon 2020 is below average (see EY (2015), Kutlača et al. (2015)). The latter is not surprising: Recent FPs and now Horizon 2020 have been striving for excellence and not for cohesion. Horizon 2020 is thus not intended to fund “standard” research and innovation projects but excellent research and innovation projects. This might create problems for applicants from less advanced countries. Any ambitions to foster participation of Danube Region countries must be preceded (!) by strong investments in science and education to attain noteworthy improvements in participation rates. While there is some support

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<sup>3</sup> Strengthening research, technological development and innovation; Enhancing access to, and use and quality of, information and communication technologies; Enhancing the competitiveness of small and medium-sized enterprises; Supporting the shift towards a low-carbon economy in all sectors; Promoting climate change adaptation, risk prevention and management; Protecting the environment and promoting resource efficiency; Promoting sustainable transport and removing bottlenecks in key network infrastructures; Promoting employment and supporting labour mobility; Promoting social inclusion and combating poverty; Investing in education, skills and lifelong learning; Enhancing institutional capacity and an efficient public administration.

in Horizon 2020 for scientific catching-up, the main impulse to modernise science and scientific infrastructures must come from the national level.

As far as mastering the administrative requirements, forming competitive consortia, or the ability of drafting competitive proposals are concerned, the DRS organisation could do the following actions:

- Analyse the current situation: Which projects were accepted, which were rejected, and for what reasons
- Provide assistance in formulating project proposals and managing successful projects
- Define topics that will be eligible for funding under established EU programmes and inform potential applicants about tenders and funding opportunities
- Establish mentoring programs for the public administration and businesses
- Install trainings for developing applications, especially for EU projects
- Create communities of practice and online communities to communicate efficiently and to make this a self-propelled process
- Conferences and large-scale events of the DRS might be used to form consortia and develop projects

Initiating, mentoring and supporting these projects is a formidable activity for the DRS and the — newly founded — Danube Strategy Point (DSP)<sup>4</sup>. In combination with the newly added funds in the Danube Transnational Programme and the technical serviced contracted through this programme, this might significantly speed up developments. The main aim should be to increase the “project flow”, i.e. the number of projects that are developed with support from the DRS to create competitive institutions and enterprises, and funnel

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<sup>4</sup> The director of the newly created Danube Strategy Point (DSP) just announced that the main task will be to “...ensure stronger coordination and long-term synergies with the broader EU Strategy for the Danube Region (EUSDR). In the coming year the DSP will aim to bring together a large number of stakeholders and potential project partners to facilitate the success of the Strategy.”

more resources to the DR. Of course, these activities have to be coordinated with National Contact Points that also strive to support applicants.

Projects that were supported by measures set up in the framework of the Danube Region should get the EUSDR label, as a signal for high-quality standards in writing project applications. It is evident that this support could be extended to the operational phase of the project, with the aim to ensure the proper working of project management and administrative services. In the medium-term the Danube Region quality label could also be used to evaluate the impact of the support generated under the Danube Region Strategy. The control group for the projects running under the DR banner would be those that were supported by other institutions or were not supported at all.

Mastering participation in EU programmes would be a good topic to actively encourage communities of practice across the region. This of course is valid for many of the other topics raised. After initial support these communities should become self-propelled and lead to rapid proliferation of experiences and knowledge.

Building a DRS online community that helps create momentum for the Danube Region, coordinate activities, generate ideas and validate suggestions would be also a formidable objective. The community active during the online discussion in this project would be a good starting point.

Eventually, the structures under which the Danube Region Strategy operates allow quite some freedom in setting up coordinated activities. It is up to the actors from all governance layers to fill the vastly open space, and act on the many challenges in the region. The hopes associated with the DRS were inflated right from the start although most people and regions were working hard to make them happen. Particularly the hope of accelerated catching-up or even leapfrogging did not materialise.

Given the circumstances, it is fair to say that the DRS could not have fulfilled the aspirations kindled by the ambitious topics it has in its working programmes. Changes of such magnitude cannot be achieved by fostering collaboration as the main strand of activity. Now the DRS stands the chance of having financial resources at hand that allow stimulating tangible investments that might generate substantial returns for the region — if coupled with sustained reform efforts. More input and leadership and willingness to cooperate

across borders is needed from catching-up countries to make this work. If this development mode is not an option for the region than the DRS has to start managing expectation. It will then — at best — be a soft instrument to coordinate a bunch of very heterogeneous actors that have chosen to take the long way to prosperity. Everything is on the table now — make your bets!

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