

**Review of the Literature on the
Effectiveness of Economic Development
Policy**

Executive summary

Background

1. This study was commissioned by the Welsh Assembly Government to ascertain the extent, robustness and relevance to Wales of evidence about policies to promote economic development that would be of interest and value to policy makers in Wales. Associated with this final report is an Access database of all of the evidence collected, which can be filtered, sorted and summarised across a variety of classifications.

Research method

2. It was agreed that an evidence-led research methodology would be used. Rather than pre-selecting geographical comparator areas or a limited number of specific policy fields, the research would follow an open approach, exploring as wide a range of sources as possible. The only defining research parameters were the two key objects of WAG's economic policy: 'more jobs' and 'better jobs'. In principle, all policy measures directly or indirectly contributing to one or both of these two objectives could be included in the research.
3. Having completed this trawl of what was available and after discussions with the Welsh Assembly Government, we were then able to narrow the focus of the study to specific themes and comparator countries. In the process, we have captured a lot of interesting material, including primary research, literature reviews, general and theoretical studies about factors influencing economic development and feasibility studies for policies, as well as reports containing evaluation evidence. This other material has been recorded with sources and brief abstracts and included in the database.
4. The five themes chosen for the dimensions of economic policy were:
 - Business support;
 - Innovation;
 - Trade development, Export Promotion and Inward Investment;
 - Workforce Development; and,
 - Welfare to Work.
5. We derived a taxonomy that was based on economic activities in the product and labour markets and their factors of production and homed in on five themes central to economic development policy, recognising that all of the other policy areas are critical to the effectiveness of policy delivery in the five selected themed fields of policy.

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6. The geographical areas from which we drew comparative evidence to include the database alongside evidence for specific Welsh policy initiatives were:
 - North East England;
 - Scotland;
 - United Kingdom;
 - Finland;
 - The Netherlands; and
 - New Zealand.
 7. Our focus was determined by the relevance for the Welsh policy and economic context, the availability of comparator data (focus on UK countries and regions and OECD countries only) and a tradition of evaluation research which would provide a spread of evidence.
 8. A total of 503 documents were identified on the basis of the perceived relevance of their title. After a brief assessment of their aims, we discarded those that were not sufficiently focused on the topic area, were not about policy evaluation or were not considered robust and succeeded in collecting 314 of them. These were then subject to a more thorough examination.
 9. We established criteria from the outset in order to assess the robustness of the wide range of studies involved:
 - Not robust: sample sizes too small, lacks analysis of outcomes, is a literature review;
 - Useful but not very robust: decent sample size, discussion of impacts in gross terms or process terms; and,
 - Robust: assesses additionality, sample sizes 50+ or population over 30, outcomes by client group.
 - Doesn't directly meet research objectives: these studies were typically literature reviews or other studies which did not specifically focus on assessing an economic impact. They were included in the evaluation typically because they gave a useful overview of the policy context or made an important contribution to the broader policy debate.
 10. According to these broad standards, 13% of the studies were assessed to be robust, 38% useful but not very robust, 37% not robust and 21% not directly meeting research objectives.

Key findings

Business support

- The literature evaluated a wide range of very diverse projects. The entrepreneurship development studies allow a very tentative conclusion with regard to a benchmark average cost of about £2,500 per business start-up.
- Of the studies which evaluated subsidised external business advice services only one compared total costs with productivity gain, with the costs of participating in the *Manufacturing Advisory Services* programme estimated at £50,000, compared to productivity benefits averaging £45,000 per year and continuing for at least three years.
- A number of grant-support studies contained quantitative estimates of productivity benefits. For example the study *An Analysis of Current DTI Industry Support Patterns* reports average company productivity benefits of 4.3% following participation in Regional Selective Assistance.
- Measures of the additionality of these schemes are limited. Quantitative estimates for additionality in studies evaluating subsidised external business advice services are typically quite high, ranging from 66% to 85%; the loan guarantee scheme evaluation mentions 60-70% additionality, one of the capital investment readiness projects has just under 50% additionality. Displacement is quite high, around 75% in both a capital investment and a loan guarantee scheme evaluation.

Innovation

- There are some clear benefits to the firm with R&D tending to raise a company's market profile, increase exports and value added, create some new jobs and can also reduce costs. Clustering helps raise the awareness of what R&D can achieve and can make it easier to disseminate good practice.
- However creating innovation should not be the focus of policy. Firms that innovate have highly skilled staff and are willing to bring in outside experts when appropriate to assist in the development and testing.
- There are probably too many initiatives, with firms often complaining that they are confused about the range and purpose of the variety of provision. There is also a need to test the validity of the rationale of some initiatives.

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- The main barriers to innovation were found to be; a lack of research establishments and of high quality research; low value added industry structure; no technology transfer activity; too great a focus on shareholder value and subsequent lack of support for R&D; but, recruiting skills is not seen as a problem.

Trade Development, Export promotion and Inward investment

- FDI generally leads to increased exports and reduced imports
- The spillover effects taken together are significant
- Inter-industry spillovers can be both positive and negative, but intra industry spillovers are small
- Larger projects are more capital intensive and less employment intensive
- The degree of embeddedness of FDI projects tends to be limited – for companies with overseas headquarters, FDI is lower than for indigenous firms
- Support, whether financial or otherwise, speeds up the process and can encourage expansion, but it is a minor factor in the (national/regional) location decision
- Headquarters and Science and Technology FDI can bring higher value added jobs and activities. However, much of manufacturing and call centres in particular, are low skill jobs and do not develop in-company training provision. A positive side to this is that the skills are easily transferable and not dependent particularly on the sector

Workforce Development

- There is only limited evidence in the literature in relation to who is training. There is however evidence that some workforce development programmes are failing to meet their stated objectives by failing to ensure that programmes target disadvantaged groups such as the unemployed.
- The benefits of training provision to individuals have largely been measured through a qualitative assessment of their opinions surrounding the quality of training provision and its outcomes.
- The returns to post school education are high and reasonably stable over time although there is considerable variation by subject. The evidence also shows that there a significant impact from higher level

vocational qualifications on employment with those at level 2, raising the employment rate of those men who left school with nothing to 89%. However level one qualifications have a more marginal impact.

- There is a lack of quantitative evidence on the benefits of training provision to companies. Qualitative evidence suggests that training is generally viewed in a positive light by companies however the added value of such training is questionable with many companies saying that they would fund similar training themselves.
- Training within SMEs is highlighted as a particular issue although the level of informal training that is done within firms should not be understated.
- There were some limited quantitative findings. The Investors in People Impact Assessment estimated the profit gap by measuring an increased profit as a result of changes made over the last three years by Investors in People recognised organisations of 7.16% of sales or £505 per employee per year, as opposed to 3.78% of sales or £197 per employee per year for other companies.
- Employer-provided training has a significant positive impact on the earnings of both male and female employees but firms are able to 'cherry pick' those most likely to benefit. Expanding training provision either internally or externally would not necessarily have the same benefits – one study showed that employees who did not take up training provided would not have benefited if they had.
- In general, returns to training decline the older or less skilled are the trainees.

Welfare to Work

- Two of the main weaknesses of ILMs are that they may substitute or displace employment from the open labour market, and they run the risk of providing costly support to those who would have found work without assistance. ILMs have been shown to offer the most value when they are targeted at the long term unemployed or other disadvantaged groups however job search assistance is not effective for these groups.
- The literature has highlighted the need to focus on tackling multiple barriers to employment.
- In the UK the New Deal Programmes are central to the policy to support participation in the labour market. A cost benefit analysis of the New Deal for Young People showed that the national programme resulted in over 26,000 additional job entries from lone parents with a

net gain to society of nearly £4,500 per job, and a total net benefit of £115 million.

- There are a number of evaluations of supply side measures that provide quantified estimates of impact. An evaluation Working Families Tax Credit concluded that the changes in in-work incomes through the introduction of WFTC increased labour supply of lone mothers by around 4.6 percent, slightly reduced labour supply of mothers in couples by 0.2 percent, and increased the labour supply of fathers in couples by 0.8 percent.
- Evaluations of demand side measures have included evaluations of impact of wage subsidies on employment. In the Finnish literature little added value was revealed with public subsidies appearing to substitute private employment expenditure.
- Some active labour market policies can be effective in assisting people into employment, especially those focusing on job search and work incentives. They are more effective when the target group is more 'job ready'. The promotion of a work-first ethic, such as in Employment Zones, can be effective for harder to help groups.
- Evidence from other active labour market policies indicate that the hardest to help need customised supported participation to resolve pre-employment barriers and build the confidence and motivation to enter the world of work, such as Intermediate Labour Markets.

Overall assessment

11. There is a considerable amount of interesting material in the public domain, not all of which is directly relevant to policy design and performance but is informative about how the underlying processes work. However, this is rarely followed through to say what and how policies might work better.
12. There is limited robust evidence in the public domain for business support, innovation and trade development policies. Many of the studies focus just on project beneficiaries and do not attempt to assess deadweight and displacement. However, those that do tend to show that deadweight and/or displacement can be quite large.
13. Only 42 percent of the 302 studies which were analysed contained any quantitative findings which reflects the general paucity of in depth, robust programme assessments. Where quantitative findings were available they varied greatly in relation to robustness and very few studies calculated an overall net economic impact. Other measures, such as increases in productivity, profitability or number of beneficiaries were more common although lacking programme cost data and detailed information on who the

beneficiaries were made calculations of added value and cost per beneficiary unreliable or impossible.

14. Just over 13 percent of the studies were assessed to be adequately robust. That is, they measured additionality in sample sizes of 50 or more cases, and analysed outcomes by different groups of clients. Another 37 percent were useful in that their sample size was large enough to give credible results about gross impacts and process effects.
15. Studies tend to be thematically narrow, that is focused on one theme of economic development. There is no discussion of the 'big picture' in terms of how policies for the different thematic areas should or could fit together. That raises issues for policy – access to work has seen policy changes but it has had very little impact on workforce development, so that most of the job entry remains in churn in entry level jobs, albeit with jobs sustained for somewhat longer. Two themes that do often interact are business support and trade development, because where measures of final outcomes are secured, attributable sales increases can be distinguished between export and domestic growth.
16. The themes of welfare to work and workforce development give more opportunity to explore issues, largely because the processes have been quite heavily researched. Policy has been developing rapidly recently in the access to work field and that is reflected in the resources that have been put into this field. To some extent, this is because their outcomes are fairly close to delivery and of central policy importance.
17. Business support, and to a lesser extent trade development and innovation, tend to focus on independent evaluations of small projects or initiatives. Their main concerns are about the effectiveness of delivery of support such as advice and guidance and networking. There needs to be more tracking introduced into these studies to demonstrate that the support leads to economic outcomes
18. Many of the findings we have presented are generic to the processes and the themes, and are relevant to Wales in a general learning sense. Where policies strayed into areas of policy where Wales does not have jurisdiction, it is difficult to disentangle what is relevant to Wales and what is not. For example, a number of studies in inward investment had a strong fiscal component.
19. The lack of 'off the shelf' policies that have been robustly researched and shown to be effective suggests that there is a need for robust evidence to better design, target and implement policy. Therefore, the main conclusion for policymakers is that interventions to promote economic development should be piloted and carefully evaluated to provide robust evidence of their effectiveness before they are rolled out nationally. By piloting changes, policy can evolve organically.

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20. Additionality as a concept runs through much of the research literature but much weight is given to general consideration of the counterfactual with only a limited attempt to estimate this quantitatively with most focus on what would have happened anyway – deadweight. There is very limited consideration of displacement and substitution and ultimately net additionality partly because of the methodological difficulties in disentangling and assessing the impact of process change but also because of the relationship to the terms of reference and design of programmes.