

Introduction:

1. The following evidence draws from our forthcoming Regional Studies Association Policy Impact Book which looks at how policymakers can leverage Global Value Chains (GVCs) and Global Investment Flows (GIFs) for regional upgrading. Its title is *Move On Up! Building, Embedding and Reshaping Global Value Chains through investment Flows: Insights for regional innovation policies*. It the expansion of a workshop paper submitted to OECD's 'Broadening innovation policy' workshop series.
2. The nature of the evidence particularly leads itself for Terms of Reference question including **'How does the Government's Investment Strategy relate to its Industrial Strategy, its regional policy and the "levelling up" agenda?'** as well as **'What advice, support and assistance should the Government be providing to inward investors – and how can it most effectively communicate with investors?'**
3. The organisations we both represent are academic, however both The Department of Geography and Environment at the London School of Economics focuses and The Blavatnik School of Government at the University of Oxford focus on application of evidence and public policy. The Policy Impact Book from which this evidence stems is subsequently policymaker focused. The primary reason for submitting evidence is therefore to share the results of this work. The pre-publication manuscript is available upon request.

Short summary:

4. This *Regional Studies* Policy Impact Book brings together the latest academic evidence and public policy insights with global value chains (GVCs) and global investment flows (GIFs). It comprises a comprehensive description and explanation of why they matter for regional policy. It focuses on how sub-national regions can leverage them for innovation and upgrading, or "levelling up". Specifically, its attention is on how regions can build, embed and reshape GVCs to their local enhancement. This brings value to their communities and allows them to Move on Up!
5. **The book makes the case for proactive sub-national public policy, (or industrial policy) on the engagement of GVCs.** Vertically engaging with GIFs (via Investment Strategies) rather than setting the ground and letting manna drop from heaven. Its chosen approach is three-fold. First, it looks at why. Why GVCs and GIFs matter and why sub-national policymakers should focus their attention on upgrading. It critically reviews different streams of research and evidence. This is in order to identify key definitions and conceptual foundations for the analysis of the link between GVCs, GIFs and

innovation at the sub-national and local level. Second, it looks at what. This is through new conceptualisations and critical insights on the regional drivers and impacts of global connectivity, bridging macro-international and micro-firm level approaches. Third, is the critical how. **How policymakers can leverage GVCs and GIFs for their regional benefit.** It aims to review empirical evidence and available policy evaluation in order to highlight what works (and what does not) when leveraging these concepts to shape public policies with **particular reference to less developed regions.**

Detailed evidence:

6. *The following extract is from the Policymaker and Practitioner Summary of the Policy Impact Book. It consolidates the six key messages that our academic framework and the empirical evidence points towards. Key messages 1 – 3 assist with Investment Strategy, regional policy and levelling up. Key messages 4 & 5 assist with advice, support and assistance to inward investors. Key message 6 highlights the broad need for global connectivity and active internationalisation.*
7. GVCs and GIFs can seem large and unwieldy. Therefore, the method taken is one of specificity. It draws specific links from the GVC, through the governing Multinational Enterprise (MNE) and its controlling arm of Foreign Direct Investment (FDI). Through this approach, regional decision-makers can utilise some key actionable lessons. One key lesson throughout is a need to change the paradigm in regional thinking. **Rather than directing FDI into sectors of choice, it should be directed to value-added tasks and activities within sectors.** For example, rather than manufacturing, instead a focus on the R&D of a production technique. Or, for example, perhaps a certain type of wood processing instead of forestry.

Connectivity is key

8. The broader lesson from the evidence on GVCs and regional innovation policy is that connectivity is key. This connectivity is both in terms of firms building links to the GVC in their home region and firms building connectivity to the GVC in a foreign region. Putting up walls and retreating into domestic markets will not make regions better off. Evidence-based cautious openness and internationalisation are important. Undertaking any protectionist measures within the connected and reliant globalised context have much higher negative fallout costs. This fallout is due to such policies not only impacting final goods but also on intermediate components. For the OECD, these components represent on average half of the imports of any given country.¹

¹ Stephenson, S. and A.-K. Pfister (2017). "Who Governs Global Value Chains?" *The Intangible Economy: How Services Shape Global Production and Consumption*: 55.

9. However, being open, although an essential component, is not enough. The Washington Consensus view is that areas simply need to have macroeconomic stability and open to investment.² However, this misses critical insights into locational specific differences³ as well as into the interaction between firm-level strategies and local characteristics.⁴ Improvement in areas such as human and institutional capacity are critical to ensure competitiveness along the task-driven service section of the value chain. To deliver these improvements requires active public policy and this, in turn requires governance input^{5,6}.

All GVCs are different

10. At the regional level, all GVCs are different. There are also significant regional disparities within countries regarding GVC participation. In order to incorporate the relevant benefits of globalisation, regions need to develop a value capture strategy, that is, to benefit from their advantages in a sustained, competitive way.⁷ To do so, they must first understand the differentiated preferences and strategies of MNEs. These differences are in terms of sectors, GVC stages, as well as the desire for knowledge and entry mode. All these complexities result in very varied sub-national geographies of GVC connections.⁸

Fine grained specialisation is necessary

11. This policy book's diagnostic lends itself to discussion with smart specialisation strategies (S3). These strategies can be two-fold. Firstly, looking at boosting current skills and capabilities within the regions' industries, in the GVC story – that of upgrading. Secondly, it is the fostering of new regional diversification strategies within technological domains and potential arising from innovative opportunities,^{9,10} - or in the GVC story, that of building and embedding. Smart specialisation echoes modern thinking about industrial

² Williamson, J. (2004). *The Washington Consensus as Policy Prescription for Development*. Practitioners of Development, World Bank, Washington DC.

³ Ponte, S. and T. Sturgeon (2014). "Explaining governance in global value chains: A modular theory-building effort." *Review of International Political Economy* 21(1): 195-223.

⁴ Crescenzi, R., Dyevre, A. and Neffke, F. (2020) *Innovation catalysts: how multinationals reshape the global geography of innovation*. Geography and Environment Discussion Paper Series (7). Department of Geography and Environment, LSE, London, UK. [http://eprints.lse.ac.uk/105684/1/Crescenzi_Dyevre_Neffke_Paper_7_innovation_catalysts_2020.pdf]

⁵ Elms, D. K. and P. Low (2013). *Global value chains in a changing world*, WTO/FGI/TFCTN.

⁶ Drake-Brockman, J. and S. Stephenson (2012). "Implications for 21st century trade and development of the emergence of services value chains." *Prepared for IADB and ICTSD E-15 experts dialogue on GVCs*. Geneva.

⁷ Bailey, D., C. Pitelis and P. R. Tomlinson (2019). "Strategic management and regional industrial strategy: cross-fertilization to mutual advantage." *Regional Studies*: 1-13.

⁸ Crescenzi R., Pietrobelli C. & Rabellotti R. (2014) "Innovation Drivers, Value Chains and the Geography of Multinational Corporations in Europe", *Journal of Economic Geography*, 14 (6), 1053-1086

⁹ McCann, P. and R. Ortega-Argilés (2015). "Smart specialization, regional growth and applications to European Union cohesion policy." *Ibid.* 49(8): 1291-1302.

¹⁰ Cortinovis, N., R. Crescenzi, F. van Oort, Multinational enterprises, industrial relatedness and employment in European regions, *Journal of Economic Geography*, Volume 20, Issue 5, September 2020, Pages 1165–1205,

policy as a 'process of discovery'^{11,12}. However, necessity is not just to discover and innovate, but to capture this at a regional level. Smart specialisation is a crucial necessary element, but it is not enough.¹³ This lack is particularly evident when it comes to less developed regions that suffer from an endemic absence of supportive institutions, and technological, administrative and managerial capabilities that becomes apparent when adopting an evidence-based approach to policy evaluation.

12. A critical analytic and diagnostic tool advocated in this book is to connect GVC thinking and a 'smart specialisation' approach to regional innovation policies via GVC analysis and mapping. Mapping regional GVCs is critical for informed decision making on building, embedding and reshaping GVCs. The smart specialisation framework also highlights the importance of this process. The diagnostic focuses on existing and evolving competitive advantages and deciding how to compete on existing strengths, or whether indeed to develop new ones. Learning how to work with current and future GVC actors and their potential integration is also critical. With each region being unique in its circumstances. This exercise will help regions understand how they, in particular, want to engage with GVCs. Approaches for regions on the technological frontier will differ from those in lagging regions. The former focuses on knowledge connectivity abroad, whilst the latter on product or process upgrading at home. Evidence shows both high income and lagging can grow faster or slower than average.¹⁴ Being behind, does not mean you have to remain behind. However, a solid evidence-base on how to mobilise relevant GVC actors should shape well-targeted interventions.¹⁵

Building institutional and informational bridges help

13. Once regions have an approach, investment promotion agencies (IPAs) can be a useful tool at the disposal of policymakers for attracting the 'right' kind of FDI. Evidence has shown that inward IPAs (IIPAs) orchestrated at both the national and regional level can enhance flows of FDI, however, they have a certain critical mass to operate and therefore, must be resourced appropriately.¹⁶ With this ability to target, rather than doing this into sectors of choice, the changing paradigm will mean regional decision-makers can direct FDI into value-added task-driven activities within sectors. Again, these targeted tools can integrate with regional specifics.

¹¹ Rodrik, D., J.-M. Lozachmeur, P. Pestieau and Centre for Economic Policy Research (Great Britain) (2004). Industrial policy for the twenty-first century. London, Centre for Economic Policy Research.

¹² Rodrik, D. (2008). Normalizing industrial policy. Commission on Growth and Development. World Bank, World Bank.

¹³ Bailey, D., C. Pitelis and P. R. Tomlinson (2018). "A place-based developmental regional industrial strategy for sustainable capture of co-created value." Cambridge journal of economics 42(6): 1521-1542.

¹⁴ OECD (2011). OECD Regional Outlook 2011: Building Resilient Regions for Stronger Economies. O. Publishing. Paris, OECD: OECD.

¹⁵ Crescenzi, R, G. de Blasio & M. Giua (2020) Cohesion Policy incentives for collaborative industrial research: evaluation of a Smart Specialisation forerunner programme, Regional Studies, 54:10, 1341-1353, DOI: 10.1080/00343404.2018.1502422

¹⁶ Crescenzi R., Di Cataldo M. and Giua M. (2019) FDI inflows in Europe: does investment promotion work? LSE-Institute of Global Affairs Working Paper #9/2019

14. Similarly, outward investment promotion agencies (OIPAs) may have a role to play. Looking external to the region will allow regional decision-makers to target related areas of the GVC, seeing as the region itself should benefit from FDI outflows. These benefits are the knowledge connections and access to foreign markets. Regional leaders should be encouraged to make these connections or engage with national policymakers to make the case. Public authorities can contribute to this knowledge diffusion process, one case being in providing advice on how to enter foreign markets.¹⁷ A recent example of this is the UK Department for International Trade's new insurance policy helping UK companies invest abroad with confidence.¹⁸
15. By utilising IIPAs and OIPAs, regional policymakers can address the market failures associated with information problems and take a more long-term view on FDI. This long-term view becomes a give and take relationship with both the inward and outward FDI potentially benefitting the region, rather than a view of FDI as a one-off transaction or as a purely macro-economic flow.

Leveraging linkages

16. Outlined throughout the discussion is the criticality of linkages to facilitate the GVC connection through to the region. To complement IPAs and in order to bring efficient linkages between the GVC and region, local content (or linkage) units (LCU) are useful to set up. LCUs are the flexible alternative to implementing rigid laws and legislation. Rather than just written legislation, this relational based approach, working with MNEs, can help facilitate local supply chain spillovers. The LCU can account for regional differences. LCUs are useful in lagging regions. When combined with enterprise mapping, the distance in understanding between MNEs and regions can reduce. These institutional bridges are useful in attracting Emerging [country] Multinational Enterprises (EMNEs). They account for the EMNEs differences in investing preferences. These EMNEs have shown to represent a significant and rising GVC opportunity for regional policymakers in the OECD. Since EMNEs tend to locate where other MNEs are present and engaged in the same activity, regional policymakers should attempt to gain a first-mover advantage.
17. These institutional bridges are further evidence that institutions (of many shapes and forms), matter. Although evidence is prominent at the national level, there are further implications for institutional quality at the regional level – it being a vital location driver of FDI. Regional policymakers need to be aware of institutional factors in order to influence GVCs.

¹⁷ OECD (2018). Productivity and Jobs in a Globalised World: (How) Can All Regions Benefit? O. Publishing. Paris, OECD.

¹⁸ Fox, L. (2017) "Supporting overseas investment by British companies can bring vast benefits to the UK."

The proactive pursuit of knowledge

18. The final implications for regional policymakers involve the proactive search for new knowledge abroad. Most effective is the active internationalisation of firms and connecting globally with each other. This outward seeking activity is key to regional innovation and development, rather than the limitation of firms' internationalisation through the encouragement of reshoring.

19. Building and embedding a region into the GVC does not come without its potential drawbacks. GVCs and FDI are very integrated and enjoy strong complementarities. Policies and programmes require coordination, integration and consistency for their success.¹⁹ However, if approaches outlined by the evidence discussed throughout this book are incorporated in regional policy maker's decisions, they will be able to help reshape their region and its interaction with the GVC. For regions, it is, "*not only a matter of whether to participate in the global economy, but how to do so gainfully.*"²⁰

¹⁹ Crespi, G., E. Fernández-Arias and E. Stein (2014). A world of possibilities: Internationalization for productive development. [Rethinking Productive Development](#), Springer: 233-278.

²⁰ Gereffi, G. and K. Fernandez-Stark (2016). [Global Value Chain Analysis: A Primer](#). <http://hdl.handle.net/10161/12488>, Duke University.