

Sub-regional Innovation Policy Outlook 2020: Eastern Europe and the South Caucasus



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UNITED NATIONS

Geneva, 2021

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This publication is issued in English and Russian only.

United Nations publication issued by the Economic Commission for Europe.

**The Sub-regional Innovation Policy Outlook project
was funded by the Government of Sweden.**

ECE/CECI/26

ISBN: 978-92-1-117261-4
eISBN: 978-92-1-005365-5
Sales: No. E.20.II.E.44

FOREWORD

Innovation – or the systematic experimentation with new ideas – will be essential for countries in Eastern Europe and the South Caucasus (EESC) in creating new points of competitive advantage and consolidating and strengthening existing ones to form the foundation and growth engines needed to reach the ambitious Sustainable Development Goals. With their high education levels, histories of research excellence, and strong political and societal commitment to innovation, the EESC countries carry substantial potential for innovation-driven growth. Realizing this potential requires sound, flexible and evidence-based policy interventions that, put simply, enable and promote broad experimentation across the economy and society. EESC countries have put such interventions high on their policy agendas, engaging in a broad range of support mechanisms, such as incubators, technology parks, public research and fiscal incentives – but our research shows substantial room for reform to target innovation in a concerted fashion. As the COVID-19 pandemic demonstrates the need for resilience and further constrains fiscal space, and as social spending and public debt grow, the imperative to maximize the positive impact of public support is clearer now than ever.

This first iteration of the UNECE Sub-regional Innovation Policy Outlook (IPO) supports the EESC countries through a comparative assessment of the quality and scope of innovation policies, institutions and processes and offers actionable policy recommendations at the national and sub-regional levels. EESC policymakers can draw on the IPO to identify strengths and weaknesses in policies and institutions, to enlarge the evidence base for policy dialogue and learning among EESC countries, and to set priorities and design effective interventions.

The IPO represents one step on the path of improving the EESC countries' innovation policies, institutions and processes in line with good policy practices and principles, as elaborated through UNECE work on innovation and competitiveness. I look forward to continuing to strengthen UNECE's cooperation in support of EESC governments' policy priorities.



Olga Algayerova
Executive Secretary
UNECE

PREFACE

The Sub-regional Innovation Policy Outlook (IPO) of the United Nations Economic Commission for Europe (UNECE) was developed on the basis of a mandate from the UNECE Committee on Innovation, Competitiveness and Public-Private Partnerships. It aims to offer policymakers in Eastern Europe and the South Caucasus (EESC) a framework for identifying strengths and weaknesses in their national innovation systems and setting up effective innovation policies and support mechanisms, as well as the institutions and processes to design and run them efficiently. The IPO also provides guidance to international donors and private investors on opportunities to support and invest in innovation for sustainable development in the EESC sub-region.

Importantly, the IPO complements international composite indices and other benchmarking frameworks, such as the Global Innovation Index (GII, World Intellectual Property Organization) and the Global Competitiveness Index (GCI, World Economic Forum), in two ways:

- 1.** By assessing the role of policies, support mechanisms and institutions in translating innovation inputs, such as infrastructure and educational attainment, to outputs, such as private sector innovation and intellectual property registrations. As innovation policy often involves targeted public support for specific projects, which can be expensive and involve substantial, unintended trade-offs, assessing these elements is important to ensure that scarce public resources are put to optimal use, that policies systematically contribute to innovation for sustainable development and that institutions, processes and incentives are able to put them into practice.
- 2.** By applying an assessment framework adapted to the economic, political, structural, historical and institutional factors that strongly influence innovation-led development in a specific sub-region. Common factors that set EESC countries apart from other countries at comparable output levels include a legacy of economic planning, an atrophying yet tangible tradition of applied and frontier research, and high levels of educational attainment overall and in science, technology and engineering in particular, as well as the potential for further economic integration among the EESC countries and with the Eastern and Central Europe region.

The underlying research involved a comprehensive assessment process, including government self-assessments, independent and parallel expert analysis, and broad consultations. The findings were discussed, further developed and reconciled through national and sub-regional meetings involving hundreds of innovation stakeholders.

The IPO has three pillars. Pillar I, innovation policy governance, assesses the overarching strategic, institutional and legal frameworks supporting innovation policy, as well as coordination and collaboration linkages among government agencies in charge of innovation. Pillar II, innovation policy tools, looks at the range and quality of support mechanisms in place. Pillar III, innovation policy processes, examines the scope, nature and effectiveness of rules, processes and mechanisms and, in particular, the role of evidence and data throughout the policy cycle.

By engaging the EESC countries in an intensive process with high-level buy-in and strong national ownership, the IPO has already created momentum. Scoring and evaluating countries across a range of indicators forms the basis for sustained peer learning. I strongly hope that this dynamic will continue and intensify, as innovation is essential for the EESC countries to progress towards the Sustainable Development Goals. UNECE's Economic and Trade Division stands ready to support the implementation of the IPO's recommendations with the support of donors and the aim of building back better after COVID-19.



Elisabeth Tuerk

Director, Economic Cooperation and Trade
UNECE

EXECUTIVE SUMMARY

Context for and objectives of the Sub-regional Innovation Policy Outlook

Countries in the Eastern Europe and the South Caucasus (EESC) sub-region have considerable potential for sustainable growth and development. The post-independence transition process has been rocky: after half a century of central planning, it took decades to regain the output levels of 1990 and to set up the fundamental elements of a functioning market economy. With many of these elements now in place, as well as high levels of educational attainment, a relatively diversified production structure in some countries, a tradition of public research, a strong commitment to innovation and a range of opportunities for trade and investment, these countries should hold substantial potential for sustainable growth.

Yet, this potential will not happen automatically with the current trends: several growth drivers are reaching the point of diminishing returns and look increasingly unlikely to underpin progress towards the Sustainable Development Goals (SDGs) in the medium term. The boom many countries saw in the first decade of the century was driven mainly by market- and resource-seeking investment and credit- and remittance-fuelled consumer spending. Most countries have seen total factor productivity slow or even decline, in part due to negative reallocation of factors of production from more to less capital-intensive activities, such as from manufacturing to domestic services. Manufacturing has declined substantially in terms of output, employment and diversification, and most countries rely on low value added commodity exports and remittances for foreign revenue. The COVID-19 pandemic is the latest, and potentially the most severe, of a long series of external shocks that have hit the region.

Against this background, making the most of each country's potential requires systematic and continuous experimentation with new ideas that could make more out of human and natural resources – in other words, innovation. Such experimentation is under way, with the rise of export-oriented services in information and communication technology (ICT) and business-

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