

## THE PERMANENCE OF THE EFFECTS OF CORPORATE AIDS

This audit concerns the permanence of the effects of corporate aids (investment and development aids) granted to SMEs by the Employment and Economic Development Centres. The enterprises covered by the audit operate in eastern and northern Finland, which have the nation's highest unemployment rates. The 50 enterprises reporting the largest number of secured or renewed jobs in aid decisions that were made in 1995 in the Object 6 area during the EU's first programme period (1995-1999) were selected for the audit on the basis of employment effects. In selecting enterprises the YRTTI corporate aid reporting system was used. Corporate aids and their effects were monitored up to 2003. The enterprises included in the audit were granted 24 million euros of investment aid and 3 million euros of development aid in 1995-2003.

The audit's first main question was how the effectiveness of corporate aids has been measured. Effectiveness was defined in terms of how well the results and effects achieved with corporate aids correspond to the intended effects. So far most studies concerning the functioning and effectiveness of the corporate aid system have concerned projects that were conducted during the first programme period (1995-1999). The results of studies concerning the present programme period will be used to prepare the next programme period (2007-2013) and to develop evaluation and guidelines.

The audit indicated that the risk in interview and questionnaire studies is respondents' subjective views concerning the effectiveness of corporate aids. Results should be confirmed using other sources. The Ministry of Trade and Industry should emphasize the reliability of results in commissioning evaluations and studies.

The Employment and Economic Development Centres' monitoring systems have become more systematic during the present programme period. The amendment of corporate aid legislation that

came into effect at the beginning of 2001 has clearly increased project monitoring and the measuring of effectiveness.

In the application stage it is difficult for the Employment and Economic Development Centres' coordinators to evaluate the effects of corporate aids in advance. There have also been inconsistencies in defining permanent jobs. A permanent job is expected to last anywhere from five to ten years, depending on the definition. On the basis of the Ministry of Trade and Industry's need to monitor the effectiveness of corporate aids and the results of an econometric analysis that was conducted during the audit, a five-year period is sufficient to evaluate effectiveness. Defining work in person-years rather than permanent jobs is an adequate indicator to describe employment effects.

The audit indicated that information on application forms and in the payment stage was not collected systematically. Collecting different information makes it more difficult to utilize statistics. Follow-up evaluations of projects have been meagre so far.

Delays and inconsistencies have occurred in verification guidelines during the present programme period. The Employment and Economic Development Centres should be guaranteed sufficient resources for verification work. Resource problems can also lead to undesirable work combinations. If tasks cannot be separated because of a lack of personnel, steps must be taken to ensure adequate compensatory control.

The second main question was what have been the effects of corporate aids. Effects were evaluated with the help of aid observations as well as enterprises' financial statements and annual reports, which were obtained from the National Board of Patents and Registration. In previous evaluations based on questionnaires and interviews, the positive effects of corporate aids have generally been emphasized, but these have not been detected by econometric analyses.

The number of persons employed by the enterprises included in the audit was about 22% higher in 2003 than in 1995. Turnover rose during the same period by about 85% at 2003 values. Average productivity (turnover divided by personnel) varied during the first programme period (1995-1999), but significant growth did not take place. This was due to relative changes in average personnel and turnover. At the beginning of the present programme period average

productivity turned up as a result of growth in average turnover and was at the highest level at the end of the audit period in 2003. The enterprises included in the audit had an average personnel of about 75 in 1995-2003. Average turnover was 10.7 million euros and average productivity about 144,000 euros.

The development of turnover and productivity was influenced by the general growth in industrial production beginning in 1992. The slowdown in industrial production in 1996 and 1999 was visible in a drop in enterprises' productivity. During the slowdown in 2002-2003 industrial employment fell sharply. The same phenomenon was visible in the enterprises included in the audit. In 2001 the enterprises included in the audit had an average personnel of 90, but in 2002 and 2003 the figure was 70, which was lower than the average for the audit period as a whole. The effect of corporate aids on growth in turnover and productivity is difficult to separate from the general development of industrial production.

The third main question was how permanent the effects of corporate aids have been. The effects of corporate aids on personnel, turnover and profit were evaluated with an econometric analysis. The analysis was also used to determine other factors that influence business operations.

The analysis showed that corporate aids (investment and development aids) have had a small but statistically significant effect on employment that lasted for at least five years in the regions that are in the weakest position (eastern and northern Finland). The effect of corporate aids on turnover was small and transitory. Aids did not have a statistically significant effect on profit.

The enterprises included in the audit were classified in four categories: wood-based industry, metal industry, electronics industry and other industry. The analysis showed a significant effect on personnel only in the electronics industry. There was also a significant effect on profit in the electronics industry.

Turnover was not dependent on industry. Foreign trade had a significance effect on turnover regardless of industry, however. Through turnover foreign trade indirectly influences profit and personnel. Foreign trade was not observed to have a direct net effect on profit and personnel. A risk that faces enterprises engaging in foreign trade is changes in the world market situation. Enterprises engaging in foreign trade were more likely to go out of business than

other enterprises. According to the analysis the age and location (eastern or northern Finland) of enterprises did not have a significant effect on turnover, profit or personnel.

In the opinion of the State Audit Office, factors influencing the development of the electronics industry have been global. The development of personnel and profit in the industry were of a worldwide nature and depended on general market development in the 1990s. The problem in evaluating the effectiveness of corporate aids in a particular growth industry is to separate effects from general development in the field. Personnel reductions and the shifting of operations to countries with cheaper labour have been typical of enterprises in the electronics field in the early years of the present decade.

The analysis of financial statements supported the effects of external market factors on enterprises' development. On the basis of notes to the financial statements, enterprises' turnover, profit and personnel often depend on the (world) market situation in the industry. On the basis of enterprises' annual reports, external market factors that influence turnover and profit are mainly the demand and competition situation in the industry as well as the price level of raw materials and products. Changes in exchange rates have also caused variations in enterprises' turnover and profitability. Enterprises try to adjust their production and personnel to the market situation. In order to improve profitability, enterprises have cut costs mainly by reducing personnel.

During the new structural fund period (2007-2013), when aid decisions are made emphasis should be placed on employment effects in the regions with the highest unemployment rates. New combined forms of aid could be used to develop regional expertise. Recipients should be required to present adequate information on corporate aids in annual reports.