Innovation Diffusion in Latvia

A Regional Approach







Information Note:

This report was prepared as part of an OECD project to develop a self-assessment toolkit for barriers to regional innovation diffusion that aims provide policy makers a tool to assess strengths and weaknesses of innovation diffusion channels in their regions. It is based on data analysis, surveys and workshops among stakeholders and further desk research. The report was prepared by OECD officials as a background document and should not be reported to reflect the views of OECD member countries or those of the European Union who co-finance the project.

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1 Introduction

1.1. The concept of innovation diffusion

Innovation is of crucial importance for countries and regions, to strengthen economic growth and find solutions to societal challenges. Innovation does not only take place by "creating" knowledge (for instance through research and development) but also by learning from others. Such learning processes enable the diffusion of innovation, and can help companies, regions or countries to catch-up to higher productivity levels. Innovation diffusion is of particular importance for small- and medium-sized enterprises (SMEs) and start-ups and reflects the process through which these firms gather knowledge, information and innovations from outside and use them to introduce their own innovative products or processes. It refers for instance to the adoption of new-to-the-firm technologies, the introduction of new management techniques, the digitalisation of certain processes, or the introduction on the market of a new product.

1.2. What drives innovation diffusion?

Innovation diffusion is a complex phenomenon that relates to three sets of factors:

- The local and national **framework conditions**, which affect firms' incentives and capacities to adopt innovations. Examples of framework conditions are the regulatory framework, market conditions, access to finance and skills, and infrastructure.
- The functioning of the channels through which the diffusion can take place. These channels
 include supply chains, workers careers and mobility, academic-business collaboration or
 knowledge intensive business services.
- The presence and functioning of a variety of intermediary organizations that help companies build the capacity for innovation adoption, identify external resources, and share knowledge among peers. Intermediaries include peer-network building intermediaries (e.g. employer associations, chambers of commerce, managed clusters, science & technology parks), partnership-building intermediaries (e.g. technology transfer offices, RTOs, investment promotion agencies), and capacity-building and funding agencies.

Understanding innovation diffusion, and the potential to foster this, requires an assessment of the strengths and weaknesses in these three sets of factors (framework conditions, diffusion channels and intermediaries), and the possibilities for policies to strengthen this.

1.3 Purpose and overview of the report

The aim of this report is to apply the concept of innovation diffusion and provide insights into its enablers and barriers within Latvia, in particular with respect to SMEs and start-ups.

This report is divided into four different sections. After the introduction, section 2 discusses the framework conditions that impact the creation and spread of knowledge in Latvia, followed by an overview of the main channels through which innovation diffusion takes place and the main intermediaries that support

innovation diffusion in Latvia. Section 3 brings together relevant suggestions for policy that have been brought forward by the project. Finally, further background on the analytical framework, methodologies and data used can be found in Annex.

1.4. The report is part of a wider project

The output is part of a wider European Commission-OECD project to develop an interactive policy self-assessment toolkit on innovation diffusion across regions and cities. The aim of this overall project is to help policy makers in the European Union and beyond to gain a view of the strengths and weaknesses of their regional innovation challenges and policy support that is provided.

The self-assessment toolkit will provide each region with a regional innovation profile (relative to other OECD and EU-27 regions), quantifying the strengths of different innovation diffusion channels in the region and allowing policy makers to engage local stakeholders to gather their views on the (regional) innovation system that the toolkit summarises and consider actions for improvement.

Innovation diffusion processes and obstacles in Latvia have been assessed as part of this exercise with the support of national authorities and stakeholders. The repeated interactions with key stakeholders in the country and this report summarising main findings, will serve as input to identify the dimensions to be examined in the toolkit and on how to get the questions right. It will also support Latvia to design future regional innovation policies based on an evidence-based assessment and stakeholder consultation.

Whereas the other three pilots in the project focus on regions (Blekinge in Sweden, North Central Bulgaria and Northern and Western Region in Ireland), the pilot on Latvia is at national level, which in the context of European cohesion policy is considered as one region. Data availability on aspects of innovation diffusion at national level is generally better, whereas on the other hand the number and variety of relevant stakeholders is much larger, making it harder to gather a representative view through the pilot's survey and workshop.

1.5. Process and methodology

A number of consultation meetings, discussions and a workshop between the OECD and relevant stakeholders of Latvia took place in the first half of 2021, underpinning this report. Contacted stakeholders include policy makers in the region, representatives of higher learning institutions, cluster organisations, accelerators and incubators, entrepreneurs and business owners. The process included:

- The filling-in of a background survey by the regional counterparts, with information on the innovation ecosystem, intermediary organisations and existing policies, in combination with desk research by OECD staff.
- The organisation of a virtual workshop on innovation diffusion in Latvia and the role of framework conditions, diffusion channels and intermediaries and policies. In total, 18 stakeholders participated in the workshop. The workshop generated valuable insights on innovation diffusion through structured discussion and polls on aspects of innovation diffusion among participants.
- A detailed questionnaire on the framework conditions for innovation diffusion, the different actors and how they interact, the channels through which innovation diffusion takes place, and the relevant policy initiatives, from different levels of government in this area. Seven responses were received. Half of respondents indicated that they were from the public sector while the remaining respondents were from private sector, academic, and other types of institutions.

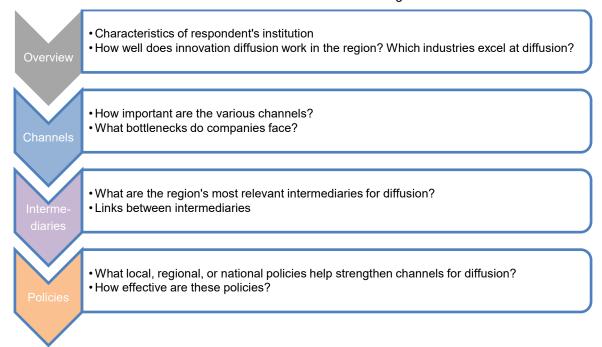
The information collected this way was processed and scrutinised by analysts of the Centre for Entrepreneurship, SMEs, Regions and Cities (CFE) at the OECD. This report reflects their insights and opinions, complemented by desktop research and independent analysis.

Stakeholder questionnaire

A stakeholder questionnaire was developed and tested during the pilot study. The survey includes questions on the state of play of innovation diffusion in the region, the functioning of innovation diffusion channels, and views on intermediaries and policies in support of innovation diffusion (Figure 1.1).

Figure 1.1. Survey overview

Questionnaire about innovation diffusion sent to stakeholders in a region



Innovation diffusion indicators

The report shows a variety of indicators related to innovation diffusion. Below is a guide to interpreting the graphs, which illustrate the position of the considered region relative to other OECD regions for each indicator. The higher the figure in the circle, the higher (better) the ranking.

- Red plain dot indicates the considered region or country
- Light red dots indicate the other comparison regions or countries, which were selected in consultation with Latvia's project leaders. Specifically, Estonia (EE00), South Sweden (SE22), Eastern Slovenia (SI03), and Western Slovenia (SI04). Data were not available for Lithuania.

Example graph: Latvia is the region of interest, in red

The region is in position 3/8 (above the median) of comparison regions; it is in the top 40% compared to the OECD.



Measuring innovation diffusion in Latvia

2.1 Background and setting

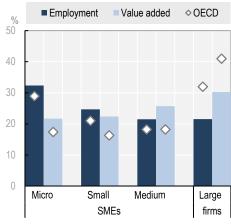
Economic structure

With a population of 1.9 million, Latvia is the fifth smallest EU-27 country. Its GDP per capita is 45% lower than the best performing countries within the OECD. The European Innovation Scoreboard 2021 marks Latvia as an emerging innovator, lagging behind the two other Baltic States and similar to countries like Poland and Slovakia. It has a (compared to the EU-27) relatively low share of employment in manufacturing, in particular medium and high tech, and a lower share of knowledge-intensive services.

SMEs

The share of SMEs in employment and value added in Latvia is higher than in the OECD as a whole. Medium sized firms in Latvia are more productive than their counterparts in other OECD countries (Figure 2.1). The share of self-employed in total employment in Latvia is 11.6%, which is lower than in the OECD at large (15.6% in 2019).

Figure 2.1. Size of the SME sector in Latvia



Source: (OECD, 2021[1])

¹ https://www.oecd.org/economy/latvia-economic-snapshot/

² https://ec.europa.eu/growth/industry/policy/innovation/scoreboards_en_

Start-up rates

Start-ups can embody innovation diffusion because entrepreneurship often brings existing ideas to new places or industries. Therefore, the rate of new business creation can indicate a higher rate of innovation in a given region. An active entrepreneurial culture is both an outcome and a driver of a strong innovation ecosystem.

Start-up rates in Latvia are extremely high relative to other places in the OECD, whether measured as a percent of businesses or as a percent of employment (Figure 3.10). This suggests that the country has a very dynamic, entrepreneurial culture. On the other hand, the average size of start-ups (number of employees) is small, suggesting that micro and smaller firms are over-represented in Latvia's start-up businesses.

Figure 2.2. Business start-up rates

Percent of startups: The region is in position 1/5 comparison regions Average firm size of startups: The region is in position 2/5 comparison regions EE00 EE00

Latvia compared to other regions

Note: Number in circle is percentile compared to OECD.

Source: OECD calculations based on Regional Innovation database https://stats.oecd.org/Index.aspx?DataSetCode=REGION_INNOVATION

Regions Objective Region : Latvia

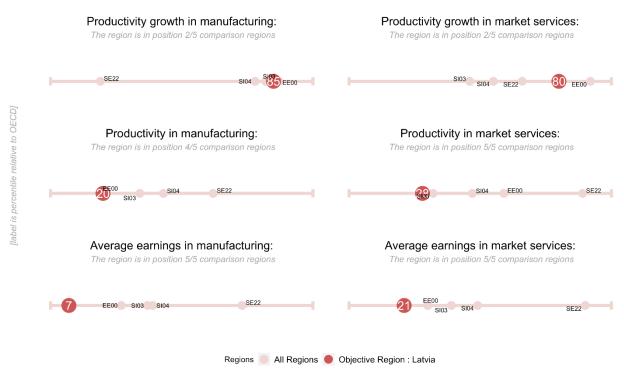
Productivity and wages

Latvia's productivity level is lower than many regions in the OECD, and 42% lower than the best performing countries within the OECD.³ This is particularly the case in manufacturing, less so in services. However, productivity growth in Latvia is very strong – in the top 20 percent of OECD regions – for both manufacturing and services.

³ https://www.oecd.org/economy/latvia-economic-snapshot/

Figure 2.3. Productivity and wages

Latvia compared to other regions



Note: Productivity and wage measures are for 2017 and exclude financial services. Growth is the annualised rate for 2007-2017.

Source: OECD calculations based on Regional Economy database https://stats.oecd.org/Index.aspx?DataSetCode=REGION_ECONOM

Similar to Latvia's productivity levels, wages in Latvia are relatively low compared to other places in the OECD. The 2019 OECD economic survey underlines the importance of further raising productivity to improve well-being for instance by strengthening competition and fostering the availability of skills needed for the uptake of digital technologies.⁴

2.2 The functioning of innovation diffusion

The initial block of OECD survey questions ask respondents about their general views on innovation diffusion. These questions capture the subjective experiences and perceptions of the region's stakeholders.

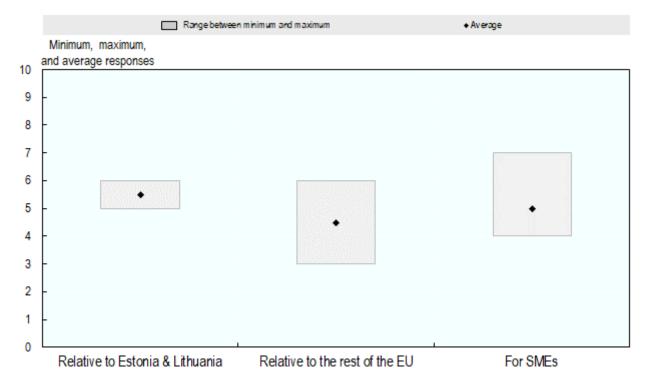
On average, respondents indicated that Latvia has similar innovation diffusion performance to Estonia and Lithuania (score 5.5/10) but slightly below-average performance (score 4.5/10) relative to the rest of the EU. During the workshop, most stakeholder answered "neutral" on the question if innovation diffusion in Latvia worked very well, with one third disagreeing with the statement. The range of answers was larger for Latvia's performance relative to the rest of the EU, with answers ranging from 3 to 6. For SMEs, innovation diffusion was seen as middling (average score 5/10) in Latvia, with some variation across respondents (Figure 2.4).

⁴ https://www.oecd.org/economy/surveys/latvia-2019-OECD-economic-survey-overview.pdf

Industries where companies excelled in adopting innovations that were developed elsewhere include include biotechnology, construction, electronics, ICT, pharmaceuticals, processed food, processed wood products, processed metals, and robotics.

Figure 2.4. Stakeholder views on innovation diffusion in Latvia

Survey responses to the question, "How well does innovation diffusion work in your region..."



Source: OECD Stakeholder survey

During the workshop, most stakeholder answered "neutral" on the question if innovation diffusion in Latvia worked very well, with one third disagreeing with the statement. Opinions on innovation diffusion to SMEs and start-ups were considerably more negative, with over half of participants disagreeing with the statement that innovation diffusion to SMEs and start-ups works very well. A considerable majority of workshop participants think that local firms benefit from innovation diffusion from universities. However, fewer participants think that local companies benefit from innovation diffusion from multi-national corporations (MNCs), with one third answering that local companies do not benefit.

2.3 Framework conditions

Framework conditions in a region influence the pace and probability of innovations being widely disseminated and adopted by firms. Important framework conditions include the availability of finance for SMEs and start-ups, access to foreign and domestic markets, availability of skilled labour, digital infrastructure and entrepreneurial culture. The most pertinent of these issues will be discussed below.

Institutions and physical infrastructure

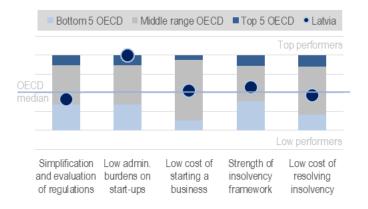
Latvia scores well for non-highway transportation infrastructure, but in part due to its less-central geographic position, is in the bottom 40% of market access via roads connectivity (Figure 2.5).

Figure 2.5. Latvia's road connectivity relative to other OECD regions



Source: OECD transportation indicators, https://www.oecd-ilibrary.org/urban-rural-and-regional-development/roads-market-access-and-regional-economic-development/8b9eca17-en

Figure 2.6. Entrepreneurial regulatory framework in Latvia



Source: (OECD, 2021[1])

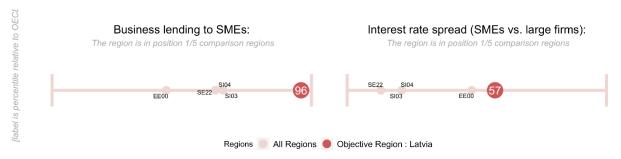
The regulatory framework for entrepreneurship in Latvia is on par with OECD practices. As for market regulation, Latvia is in the top 40% best performing countries within the OECD and administrative procedures for start-ups are particularly low (Figure 2.6). During the workshop, red tape was not seen as a significant obstacle for innovation diffusion.

Access to finance

Financing conditions throughout Latvia appear relatively favourable to SMEs in terms of loan volume (Figure 2.7). However, since Latvia has a high proportion of SMEs in its economy, smaller companies may find financing conditions to be somewhat restrictive. Indeed, Latvia has a higher-than-average interest rate spread between SMEs and large companies (i.e. the gap between rates paid by SMEs compared to large firms is greater in Latvia than in many other OECD regions).

During the workshop, access to finance was marked as the main barrier for innovation diffusion.

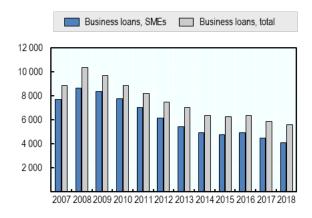
Figure 2.7. Financing conditions



Source: OECD SME Financial Scoreboard, https://stats.oecd.org/Index.aspx?DataSetCode=SMES SCOREBOARD#

Interestingly, loans to SMEs in Latvia declined gradually over the ten years from 2007 to 2018 (Figure 2.8), also indicating a problem in access to finance.

Figure 2.8. SME loans and total business loans in Latvia (drawn and undrawn)

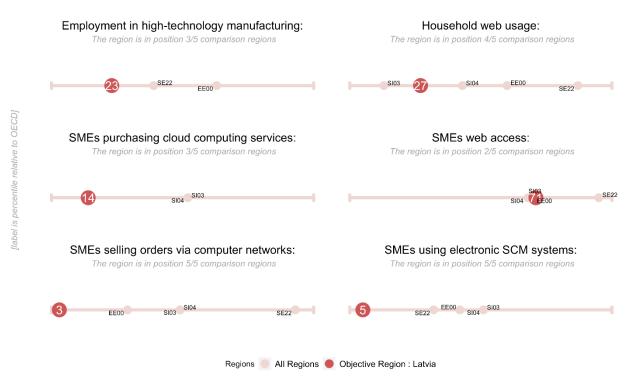


Source: (OECD, 2020[2])

Digital infrastructure

Digital infrastructure emerges as a potential weakness of Latvia. In terms of internet connectivity, the percent of households using the internet – nearly 90% – is still low compared to other places in the OECD whereas SMEs' fast broadband access is relatively high, which possibly explains the positive sentiment on digital infrastructure as an asset for innovation diffusion in the workshop (Figure 2.9). Regarding SMEs' digital adoption of new technologies – Latvia is generally in the bottom 20 percent of the OECD. This may be related to Latvia's aforementioned prevalence of micro firms and small start-ups (Figure 2.2).

Figure 2.9. Digitisation of households and SMEs



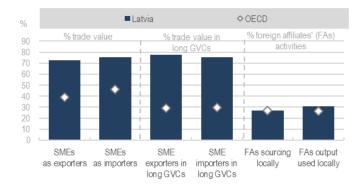
Sources: Household internet measures from OECD Regional Statistics http://dx.doi.org/10.1787/region-data-en; SME broadband from OECD ICT adoption database, https://stats.oecd.org/Index.aspx?DataSetCode=REGION_INNOVATION; Employment from OECD Regional Innovation database https://stats.oecd.org/Index.aspx?DataSetCode=REGION_INNOVATION;

According to the SME and Entrepreneurship Outlook 2021, small firms in Latvia are moving towards the digital world but remain behind OECD averages in many aspects of the transition (OECD, 2021[1]).

Global value chains

As a small country, Latvia has an open economy with a relatively large share of exports and imports in GDP, in particular in manufacturing. Latvian SMEs participate in international trade (both directly and indirectly through GVCs) considerably more than SMEs from other OECD countries (Figure 2.10). Selling and sourcing by foreign affiliates in Latvia is on par with other OECD countries.

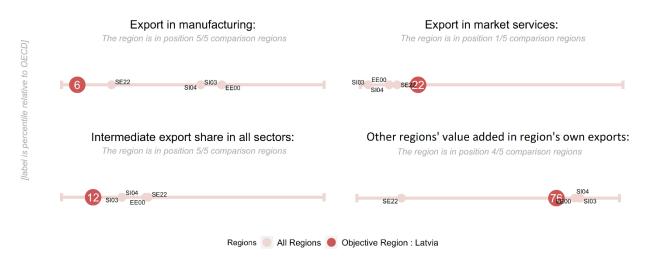
Figure 2.10. International trade and GVC exposure of SMEs in Latvia



Source: (OECD, 2021[1])

As for indirect trade, Latvia appears to have strong upstream linkages: the value-added by other regions embodied in Latvia's exports ranks in the top 25 percentile of OECD regions (Figure 2.11).

Figure 2.11. Integration in global value chains

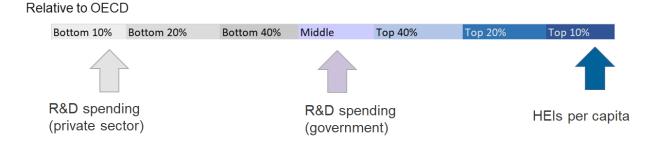


Note: All trade data (imports, exports, and intermediates) uses estimates of trade across regions within the same country. Source: OECD calculations from Trade in Value Added data.

Innovation assets

R&D spending indicates the extent to which the public and private sector invests in the production and diffusion of innovation. Public R&D spending in Latvia is lower than the average for EU countries; however, as compared to regions within the OECD the score is average (Figure 2.12). Private R&D is particularly low compared to regions in other OECD countries. Latvia has a relatively high number of higher education institutes (HEIs), being in the top 10% across the OECD.

Figure 2.12. Innovation assets in Latvia



2.4 Channels

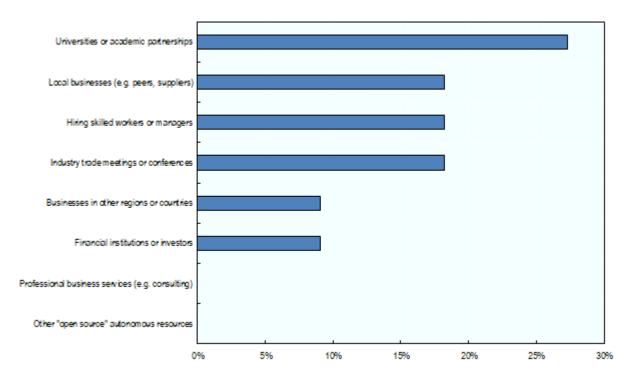
Knowledge and ideas can flow through different channels. These channels include collaboration between SMEs and foreign direct investors (FDI) and supply chain relationships in global value chains, workers changing jobs between firms and between firms, HEIs and public research institutions (PRIs), collaborations between firms and HEIs, including university spin-offs, and knowledge exchanges in clusters and peer-to-peer learning networks.

Based on responses to the OECD survey, stakeholders in Latvia identify universities and HEIs as the most important channel of innovation diffusion. Various workshop participants saw the excellence of universities in Latvia as an important asset for innovation diffusion and a large majority of participants esteemed that local businesses benefit from innovation diffusion from universities.

Local businesses, skilled workers, and trade meetings or conferences were also highly-regarded sources of information (Figure 2.13). The workshop echoed this sentiment, and underlined the need for further strengthening of this business learning channel.

Figure 2.13. Importance of channels in Latvia

Weighted average of stakeholders' ranked survey responses



Source: OECD Stakeholder survey

EE00 99

Hiring skilled workers

llabel is percentile relative to OECD]

SE22

Latvia's **tertiary education** rate is slightly above the OECD median and Latvia's HEIs have a very high prevalence of international students (Figure 2.14). Latvia also scores well in terms of worker **mobility**, with high job-finding and industry mobility rates but the share of workers in digital occupations is low.

Figure 2.14. Educational attainment; worker skills and mobility

Employees in digital occupations: The region is in position 3/5 comparison regions Employees with tertiary education: The region is in position 4/5 comparison regions Labour force with tertiary education: The region is in position 3/5 comparison regions Number of HEIs with high students mobility per inhabitant: The region is in position 1/5 comparison regions Number of HEIs with high students mobility per inhabitant: The region is in position 1/5 comparison regions Job-to-job change of industry: The region is in position 4/5 comparison regions The region is in position 1/5 comparison regions The region is in position 1/5 comparison regions

SI03 SE22 SI04

Latvia compared to other regions

Source: OECD calculations from EU Labour Force Survey data and European Tertiary Education Register (ETER) Note: Job finding rate refers to worker flows from unemployment to employment

SI03

The 2019 OECD Economic Survey of Latvia shows that Latvia has a low supply of researchers, the third lowest within the OECD (Figure 2.15), and more generally underlines the need to reduce skills shortages in the country. Work-based learning, in particular in small firms, is a point for improvement according the OECD Economic Survey.⁵ Stakeholders in Latvia suggest that universities could also offer more flexible, agile type programs (e.g. mini-MBAs) aimed at preparing students to meet the needs of industry.

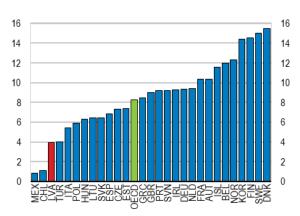
Regions Objective Region : Latvia

The workshop marked skills as the most important Latvian asset for innovation diffusion and put forward that education and skills policies are key in supporting knowledge diffusion to SMEs. At the same time, participants underlined the need to further improve education and skills policies as a priority challenge.

⁵ https://www.oecd.org/economy/surveys/latvia-2019-OECD-economic-survey-overview.pdf

Figure 2.15. Supply of researchers in Latvia

Per thousands of total employed, 2017



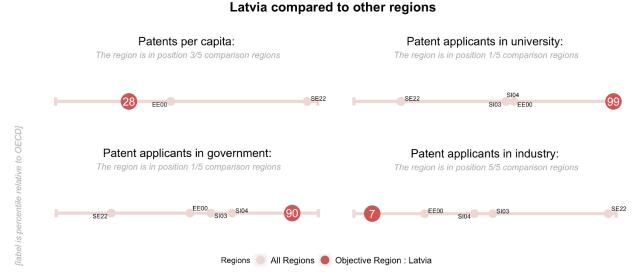
Source: https://www.oecd.org/economy/surveys/latvia-2019-OECD-economic-survey-overview.pdf

Learning from other businesses

While the number of **patents per capita** reflects a region's frontier innovations, places with effective innovation diffusion also have more patenting activity. Since innovation knowledge is often local, places that produce patents can also help encourage adoption. Moreover, the production of patentable inventions often requires substantial knowledge about previous innovations; thus successful patents indicate spill-overs of embodied knowledge from other places.

Patenting activity in Latvia is lacklustre, especially in the private sector. This is consistent with Latvia's relatively low levels of private sector R&D spending (Figure 2.12). However, Latvia compares favourably to other OECD regions on patenting activity in universities and in government (Figure 2.16).

Figure 2.16. Patenting activity

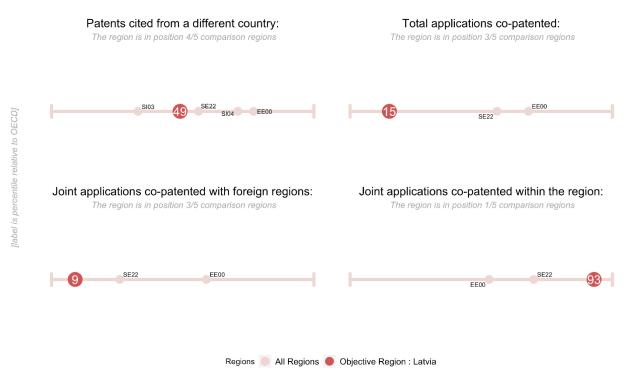


Source: OECD calculations from PATSTAT and OECD Regional Innovation database https://stats.oecd.org/Index.aspx?DataSetCode=REGION_INNOVATION

Co-patenting patterns can capture the degree of research and innovation collaboration across firms and with other innovating entities.⁶ Patent collaboration (co-patenting) *within* Latvia is very high. However, relative to other OECD regions, it has less collaboration with outside places (Figure 2.17). This is unsurprising because other OECD countries have multiple regions whereas for Latvia, any collaboration across regions would necessarily entail cross-country collaboration. Finally, although patent citations are high, the extent of co-patenting in Latvia is lower than other OECD regions.

Figure 2.17. Patent collaboration

Latvia compared to other regions



Source: OECD calculations from PATSTAT and OECD Regional Innovation database https://stats.oecd.org/Index.aspx?DataSetCode=REGION_INNOVATION

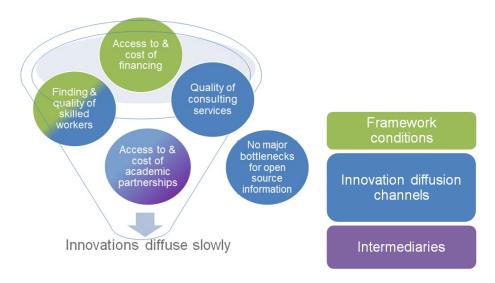
Academics, consulting, and open sources

In Latvia, skilled workers and other businesses are the most relevant channels cited by survey respondents and links to academics appear to be next in importance (Figure 2.13). However, nearly all respondents said that there were **bottlenecks** in finding skilled workers and many said it was difficult to access academic institutions (Figure 2.18). Indeed, the workshop highlighted the role of students that through apprenticeships can bring new ideas to companies.

⁶ Patent applicants can be registered in different locations; therefore, for each region one can calculate the shares of patent co-applicants registered in the same region, different regions of the same country, and those registered in foreign countries.

Figure 2.18. Main bottlenecks in Latvia's channels

Based on modal survey responses



Source: OECD Stakeholder survey

The 2019 OECD Economic Survey of Latvia⁷ notes that various measures to promote knowledge transfer are in place but researchers have too little incentive to collaborate with industry. It marks science-industry collaboration as weak in particular, and indicates that 'strengthening the innovation ecosystem by improving the quality of research and collaboration between firms and research institutions would help to diffuse digital technologies more widely across the economy'. The government has reformed institutional financing to reward performance and promote consolidation. According to the survey, taking these reforms further would improve efficiency and make room for higher wages and better working conditions for researchers to attract more qualified personnel.

2.5 Intermediaries and policies

This section explores the role of innovation diffusion intermediaries, i.e. organisations that are key in facilitating the transfer of innovation, such as chambers of commerce and business associations, public business support providers, technology transfer offices and accelerators, incubators and technology parks. Key attention is paid to how these organisations link different actors together and allow innovation to flow from one segment of the economy to another.

Latvia has a very rich system of support for businesses. It has five main intermediary types and at least four additional intermediary types, the latter of which were identified through the stakeholder survey (Table 2.1).

Table 2.1. Latvia's intermediaries

Main intermediaries/types	Website/organisations
Latvian Investment Development Agency (LIAA)	https://www.liaa.gov.lv/en

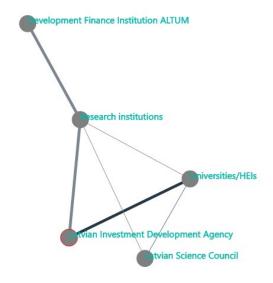
⁷ https://www.oecd.org/economy/surveys/latvia-2019-OECD-economic-survey-overview.pdf

Universities/HEIs	University of Latvia; Riga Technical University; Riga Stradins University
Research institutions	Institute of Organic Synthesis; Institute of Solid State Physics; Institute of Electronics and Computing; State Forest Research Institute
Latvia Science Council (LZP)	https://lzp.gov.lv/en/home/about-us/
Development Finance Institution ALTUM	https://www.altum.lv/en
Additional intermediaries/types	Details
Business incubators	University-led incubators
Competence centres	Eight Competence Centres in RIS3 areas/ subareas
land, and a second of the second	Chamber of Commerces Freelesses Confederation Start on Association
Industry associations	Chamber of Commerce; Employers' Confederation; Start-up Association

Source: OECD Stakeholder survey

The stakeholder survey also asked about communication and coordination between all of Latvia's main types of intermediaries. Latvia's research institutions⁸ appear to have links to all other types of intermediaries; their links to the Latvian Investment Development Agency (LIAA) and Development Finance Institution (ALTUM) are particularly strong (Figure 2.19). Universities/HEIs are also linked to many other intermediaries, whereas the Latvian Science Council (LZP) and ALTUM are less-connected to other intermediaries. In fact, links between LZP and LIAA appear to be weak and stakeholder responses suggest that more cooperation between these two intermediaries could be beneficial for innovation diffusion.

Figure 2.19. Intermediaries and their links in the innovation diffusion support system



Source: OECD Stakeholder survey

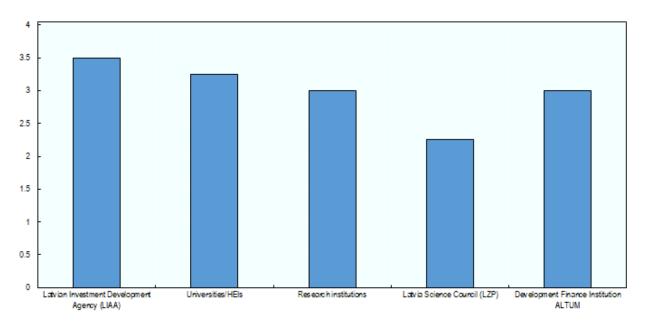
Survey respondents indicated that LIAA is one of Latvia's most effective agencies for innovation diffusion (Figure 2.20). Although research institutions and universities/HEI intermediaries were also highly-rated by

⁸ Please note that Research Institutions and Universities are included separately in Figure 2.19.

survey respondents, in follow-up questions, respondents indicated that both of these types of intermediaries could potentially play larger roles in Latvia's innovation support system.

Figure 2.20. Stakeholder views of intermediaries

Stakeholders' average assessment of effectiveness for innovation diffusion



Note: The minimum score was=1; the maximum score was=4.

Source: OECD Stakeholder survey

Based on survey responses, LIAA is viewed as particularly effective for innovation diffusion. Technology scouts appear to be a well-known way that LIAA maintains close links with universities/HEIs. Indeed, survey respondents provided very extensive information about policies that promote innovation diffusion, particularly policies designed and administered by LIAA (Table 2.1).

Table 2.2. Latvia's policies to promote innovation diffusion

Policies from the Latvian Investment Development Agency (LIAA)		
Ecosystem approach		
Innovation vouchers		
Labs of Latvia		
Research commercialisation projects		
Start-up visas and work with diaspora		
Strengthening international competitiveness for SMEs		
Technology scouts		
Technology transfer programme		
Other Initiatives and Programmes		
Deep Tech Atelier and iNOVUSS conferences		
Digital innovation hubs		
Innovation Motivation Programme		
Joint research programme		

Source: OECD Stakeholder survey

During the workshop, many participants were pleased with government support for innovation diffusion, although one third of participants were more critical. Views were somewhat mixed regarding policies that are most effective to boost innovation diffusion to SMEs: education and skills policies and science and technology policies were highlighted. Education and skills also rank high in policies that need most urgently improved, followed by strengthening access to finance and advisory services. The majority of workshop participants view national policies as most important for innovation diffusion.

Most participants thought that the Latvia's challenge does not lie in a lack or excess of policy instruments for innovation diffusion. Rather they suggested a stronger focus on the demand/business side instead of the predominant current supply side /academic focus. This requires an ecosystem perspective with flexible governance mechanisms and including an international dimension. Participants indicated that there are many intermediaries, and that awareness of their role should be raised, with a greater focus on management skills among SMEs to make use of them. Support to businesses also needs to be more accessible.

3 Conclusion and policy discussion

Various aspects of the regional innovation diffusion system in Latvia function well...

The pilot showed that Latvia has a vibrant start-up system and a strong presence of SMEs, which are important in supporting innovation diffusion. Its regulatory framework seems mostly favourable, as are access to finance conditions for SMEs and start-ups, although these were marked as needing attention in the workshop. Skills are considered an asset, although skills shortages are also seen as a challenge. Strong personal engagement and a high level of trust, where 'everybody knows each other' were also put forward as an asset for innovation diffusion.

....although a number of challenges exist

At the same time, challenges exist. The quality of the digital infrastructure was identified as an important point for improvement. Low private R&D expenditure was also an area of concern, as was the availability of R&D skills and public R&D spending compared to other EU countries. More generally, the functioning of innovation diffusion was considered to function less well for SMEs and start-ups than other actors.

Strengthening academic business cooperation

The importance of strengthening the cooperation between business and academia is widely acknowledged among policy makers and stakeholders in Latvia. Achieving successful tech transfer and interconnection is also considered to be a tough and complex challenge, which involves a wide variety of intermediaries and interactions. Better understanding and measuring these interactions is seen as an important aspect of Latvia's innovation challenge.

Systemic approach

During the workshop, at various instances the need for a more systemic approach to innovation diffusion was emphasised, including the business-academia nexus. This relates for instance to the changing nature of the Latvian innovation ecosystem itself, where there is a trend towards open innovation, as well as to the many intermediaries involved, with (the fostering of) innovation diffusion a responsibility of all actors together. It was also reflected in the observation that what is at stake is a mismatch between the supply and demand for knowledge and the need for a better alignment and interconnectedness of the factors that relate to this. Skills was put forward as an example, where supply and demand do not sufficiently meet. The need to include a demand side perspective (next to a supply side perspective) in matters of innovation diffusion was emphasised at various occasions, as was the need for dynamic and flexible governance structures, with adequate coordination and feedback loops for learning. The need to develop a roadmap that includes these various factors was advanced as well, as a means to provide a more coherent approach and more clarity to entrepreneurs.

Awareness

SMEs may not be sufficiently aware of opportunities innovation diffusion may generate and of support measures open to them. "All is there, but we do not use it", as it was put during the workshop. Suggestions

made to address this barrier related to better communication, more flexibility in support systems to changes and differences in needs. Support through Horizon Europe and other European programs was listed as an example where awareness is limited.

Absorption capacity

The issue of absorption capacity for innovation diffusion, in particular for SMEs and start-ups, was also raised at several occasions. Smaller entities may lack the knowledge or time to engage in innovation diffusion and consume the knowledge developed elsewhere. The different needs between SMEs (customers, markets) and start-ups (investors) was also discussed.

Municipalities

In Latvia, innovation policy is primarily the task of the central government. During the pilot, the relevance of adequate support mechanisms at municipal level was emphasised as well, for instance for the engagement with young entrepreneurs.

4 Annex: Methodology and data sources

Methodology and analytical framework

Innovation diffusion can be defined as the process through which firms gather knowledge, information and innovations from outside and use them to introduce their own innovative products or processes. It is a broad concept, referring, among other things, to the adoption of new-to-the-firm technologies, the introduction of new management techniques, the digitalisation of certain processes, or the introduction on the market of a new product.

According to the Oslo Manual 2018 "innovation diffusion encompasses both the process by which ideas underpinning product and business process innovations spread (innovation knowledge diffusion), and the adoption of such products, or business processes by other firms (innovation output diffusion)". (OECD/Eurostat, 2018).

Innovation diffusion is a complex phenomenon that relates to three sets of factors:

- The local and national **framework conditions**, which affect firms' incentives and capacities to adopt innovations.
- The functioning of the **channels** through which the diffusion can take place.
- The presence and functioning of a variety of **intermediary organizations** that help companies build the capacity for innovation adoption, identify external resources, and share knowledge among peers.

Framework conditions

Local and national framework conditions shape the environment for innovation diffusion. These conditions affect firms' incentives and capacities to adopt innovations. The six framework conditions for innovation diffusion are:

- 1. The **institutional and regulatory framework** (e.g. judicial system, patents, taxes, administrative rules) for business investment.
- 2. **Market conditions**, such as product demand (domestic and foreign), along with uncertainty and interest rates.
- 3. **Access to financing** for firms in general and start-ups and SMEs in particular (e.g. loans, debt, various forms of equity).
- 4. Physical and digital **infrastructure** (e.g. transportation and logistics networks; fast, reliable internet connections, and digital assets such as retailing platforms and cloud computing).
- 5. **Access to skills**, which includes managerial skills, technical and digital skills and entrepreneurial know-how.

6. Presence of **innovation assets** such as R&D and innovative businesses that contribute to an entrepreneurial culture.

The first three framework conditions characterise the business or regulatory environment; the other three conditions describe infrastructure and innovation assets. The business/regulatory environment affects firms' costs and benefits of adopting innovations. Infrastructure and innovation assets are another important factor for innovation diffusion, as they shape firms' technological capacity and define the quality of their interactions with other companies, workers, and markets. These framework conditions all form a region's innovation ecosystem that determines firms' ability and willingness to learn about and adopt existing innovations.

Channels

Innovation diffusion channels are sources of information that firms may encounter in their normal business operations. Channels expose companies to new ideas and help them develop (or find) the know-how to source and implement the innovations. They represent direct ways through which businesses acquire ideas from outside and use them to adopt innovations.

This report highlights five channels:

- 1. **Workers' career mobility** through which workers and managers changing jobs or firms can draw upon the knowledge acquired in previous jobs to the benefit of their new firms.
- 2. **Supplier relationships** through which firms exchanging products or services can share their knowledge with each other to increase the competitiveness of the supply chain. Customers can also provide critical feedback that make firms aware of innovations at the frontier.
- 3. Academic-business collaboration (ABC) that helps firms source the knowledge needed for R&D.
- 4. **Knowledge-intensive services** (e.g. consulting, IT, accounting), which can help firms identify and adopt innovative practices.
- 5. **Autonomous learning,** which relies on open knowledge, and as such does not typically require direct interaction with other firms or innovating entities. It could be websites, publications, or indirect observation and imitation of competitors.

Intermediaries

The final pillar of innovation diffusion, intermediaries, consists of entities that facilitate the diffusion of innovation without being directly involved in its production or adoption. Instead, intermediaries facilitate connections between companies and diffusion channels and also support collaboration. The three types of intermediaries are:

- a) University and research-related intermediaries facilitate knowledge transfer from higher education institutions (HEIs) and public research institutions (PRIs) to businesses and other actors in the surrounding innovation ecosystem. Indeed universities and HEIs perform a variety of functions for innovation diffusion; some host incubators or accelerators that play all three roles in supporting diffusion. Governments can use policy to encourage the formation and success of university and research-related intermediaries.
- b) Public sector innovation and local development agencies aim to increase the innovation output and uptake of technologies by the business sector. A survey of innovation agencies in ten different countries finds that the main tasks of innovation agencies are providing support to other intermediaries such as business incubators or science and technology parks, and organising capacity- and institution-building activities. In Europe these agencies are often partly or jointly responsible for administering innovation vouchers aimed at encouraging academic-business collaboration (ABC) partnerships.

c) Private sector-led intermediaries include many types of "enterprise-led" networks. These networks include chambers of commerce, science parks and cluster associations. Large "anchor" firms can also serve as intermediaries that coordinate private sector businesses within the regional innovation system.⁹ Industry clusters and science and technology parks often play multiple roles in diffusion.

Intermediaries help connect firms to innovation channels but they are not institutions that companies necessarily encounter during their normal business operations. Unlike individual businesses, intermediaries may be very responsive to policy interventions because their missions are usually connected to innovation creation and diffusion. Their roles in diffusion include:

- a) Funding. Some intermediaries specialise in mediating academic-business or business-business investment relationships for small and large businesses. Other intermediaries administer public funding to promote innovation production and diffusion.
- b) **Capacity building.** Many public agencies and higher education institutions provide advice and workshops to support business development, especially for smaller businesses.
- c) Networking. Employer associations and chambers of commerce often help businesses learn about innovations and share knowledge with their peers. In addition, public sector and academic institutions and even individual firms — ranging from small entrepreneurs to large established "anchor" firms — can serve as intermediaries.

Sources of data

The analysis relies on different sources of data that are generally available at the subnational level, using NUTS2 (also known as TL2) regional classifications. The measures displayed in the report were chosen in part based on data availability because some measures are not available for particular countries or regions.

Framework conditions

A broad range of indicators can be used to measure the strength of framework conditions at the regional level (Table 4.1). These indicators reflect the business and regulatory environment and a variety of infrastructure and innovation assets that are relevant for innovation diffusion at a regional level. Measures of regulations are generally based on survey responses while the other measures are based on economic indicators such as trade patterns, labour force characteristics, financing conditions, and R&D expenditures.

Table 4.1. Indicators measuring framework conditions in regions

Name of indicator	Notes	Data sources (see table note)
	Institutional and regulatory framework	
Institution fairness and quality	Regional indicators of governance quality. Measures are based on surveys administered by the University of Gothenburg and include (1) Lack of corruption; (2) Quality and accountability; and (3) Impartiality.	RCI
Administrative burdens on start-ups*	Component of the composite index "Barriers to domestic and foreign entry". Covers the administrative burden on joint-stock companies and personally-owned enterprises, as well as administrative burden related to licenses and permits procedures. Higher values indicate lower administrative burdens.	PMR

⁹ The presence of a large, R&D-intensive "anchor" firm helps the regional innovation system better absorb university research output and stimulate local R&D.

Complexity of regulatory procedures*	Composite index that captures the government's efforts to reduce and simplify the administrative burden of licenses and other administrative procedures. Higher values indicate less complexity.	PMR
Quality of judicial process*	The quality of judicial processes index measures whether each economy has adopted a series of good practices in its court system in four areas: court structure and proceedings, case management, court automation and alternative dispute resolution. Higher values indicate a more sophisticated and streamlined court structure.	DBI
	Market conditions	
Trade openness	(Imports + Exports)/ GDP	Reg
Share of exports by SMEs**	Exports by SMEs/Total exports	TBE
Barriers to trade facilitation*	The barriers to trade facilitation index captures the extent to which a country recognizes foreign regulations, uses international standards and has international transparency of domestic regulation. Scores from most to least restrictive.	TFI
Services Trade Restrictiveness*	Composite index that quantifies restrictions on trade in services across five standard categories: 1) restrictions on foreign entry, 2) restrictions on the movement of people, 3) barriers to competition, 4) regulatory transparency, and 5) other discriminatory measures. Scores from completely closed to completely open.	STR
Public procurement market**	Expenditure on public procurement/GDP	GG
	Infrastructure	
Population accessible via highways	Total population residing in the neighbouring regions of a given region where regions count in a way that is inversely related to their reciprocal distance.	Adler
GDP accessible via highways	Ibid.	Adler
Employment accessible via nighways	Ibid.	Adler
Share of population		
with internet broadband	Population with internet broadband access/Total population	Reg
with download speed greater than 200mbps	Population with download speed greater than 200mbps/Total population	Reg
using internet	Population using internet /Total population	Reg
	Access to skills	
Share of prime-age population with tertiary education	Population between 25 and 64 years old with tertiary education/Population between 25 and 64 years old	Reg
Share of young adult population with tertiary education	Population between 25 and 34 years old with tertiary education/Population between 25 and 34 years old	Reg
Share of population within 10km of a higher education institution	Population near a higher education institution (within 10km)/Population	ETER
Share of workers with tertiary education	Workers with tertiary education/Total employment	LFS
Share of workers that received training in the past four weeks	Workers that received training in the past four weeks/Total employment	LFS
	ing self-employed) and the entire economy in	
the share of workers with tertiary education	SMEE Employment with tertiary education/SMEE Employment - Employment with tertiary education/Employment	LFS
the share of workers that received training in the past four weeks	SMEE Employment that received training in the past four weeks/SMEE Employment - Employment that received training in the past four weeks/Employment	LFS
Shortage of digital workers	Ratio between the number of vacancies in digital occupations and employment in digital occupations	BG & LFS
	r Company of the Comp	

the implicit tax subsidy rate on R&D expenditure**	Model-based estimates of implied marginal R&D tax subsidy rates	RDTI	
the interest rate on loans	Exact definitions differ by country. SMEE		
Share of total business lending going to SMEs**	Business lending to SMEs/Total business lending (amounts in local currency)	SMEE	
Share of total loan applications going to SMEs**	Loan applications by SMEs/Total number of SMEs	SMEE	
Access to innovation assets			
R&D expenditure			
in the business sector	R&D expenditure in the business sector/GDP	Reg	
in higher education institutions	R&D expenditure in higher education institutions/GDP	Reg	
in the business sector	R&D personnel in the business sector/Total employment	Reg	
R&D personnel in higher education institutions	R&D personnel in higher education institutions/Total employment	Reg	

Note: (*) = indicator available at national level, (**) = indicator available at national level, could be constructed analogously at the regional level. LFS indicators refer to workers aged between 25 and 64.

Data sources: (Adler et al., 2020_[3]) (Adler), Burning Glass Technologies (**BG**), World Bank Doing Business Indicators (**DBI**), **ETER** Database, OECD Government at a Glance (**GG**), OECD **ICT** Access and Usage by Businesses Database, Labour Force Survey (**LFS**), **PATSTAT**, OECD Product Market Regulation Indicators (**PMR**), European Regional Competitiveness Index (**RCI**), OECD R&D Tax Incentive Indicators (**RDTI**), OECD **Regional** Database, Regional Innovation Scoreboard (**RIS**), OECD SMEE Financial Scoreboard (**SMEE**), OECD Services Trade Restrictiveness Indicators (**STR**), OECD Trade by Enterprise Characteristics Indicators (**TBE**), OECD Trade Facilitation Indicators (**TFI**)

Innovation diffusion channels

A variety of indicators can be used to measure the functioning of innovation diffusion channels across regions. These indicators measure trade linkages, worker flows, and the presence of academic institutions and business services that could help companies learn about and adopt innovations (Table 4.2). Most of the measures are available at the regional level.

Table 4.2. Indicators measuring the strength of innovation diffusion channels

Name of indicator	Notes	Data sources (see table note)	
Supplier relationships			
Domestic value added content of gross exports	Value added embodied in gross exports of the region divided by total gross exports of the region	Los	
Participation in GVC – backward linkages	Intermediate inputs produced abroad embodied in the region's exports	Los	
Participation in GVC – forward linkages	Value added produced in the region embodied in trading partners' exports	Los	
Inter-regional trade patterns	Export shares and trade in intermediate goods by industry sector. Each region is viewed as independent from other domestic regions.	Regl-O	
FDI penetration in terms of GDP***	Ratio between FDI turnover and total turnover in the region	***	
FDI penetration in terms of employment***	Ratio between FDI employment and total employment in the region	***	
Local linkages with MNE affiliates/subsidiaries***	Share of turnover of SME located in the region exported to local MNE affiliates/subsidiaries	***	
	Worker and researcher mobility		
Job-to-job transitions***	Share of workers having changed job since the last period	***	

Job-to-job transitions from large to small firms***	Share of workers having moved during the last period from a large to a small firm	***
Job-to-job transitions from MNE affiliates/subsidiaries to local firms***	Share of workers having moved during the last period from a MNE affiliate/subsidiary to a small firm	***
Geographical and cross-industry mobility	Share of workers working in year y in a different region (within the same country) or different industry from the one they worked in year y-1	LFS
Share of mobile academics	Share of academics who do not have the nationality of the higher education institution in which they work.	ETER
Share of mobile researchers	Share of researchers who do not have the nationality of the higher education institution in which they work.	ETER
Share of mobile students	The share of students who have physically crossed a national border for their tertiary degree studies	ETER
	Academic-business collaboration	
Access to higher education institutions	Number of HEIs per capita	ETER
Access to higher education institutions with high student mobility	Number of HEIs with high student mobility (per capita). Mobile students are those studying in a different country than their previous residence.	ETER
Share of university-industry patent applications	Number of patent applications filed jointly by (at least) a university and (at least) a business/Total number of patent applications	PATSTAT
Public-private co-publications per capita	Number of public-private co-authored research publications (excluding medical and health industries) divided by total population.	RIS
Share of academic start-ups**	Number of start-ups with at least an academic among its co- founders/Total number of start-ups	
	Knowledge-intensive business services	
Share of employment in knowledge- intensive services	Number of employees in knowledge-intensive services divided by total employees	Reg

Note: (*) = indicator available at national level, (**) = indicator available at national level, could be constructed analogously at the regional level, (***) = not existing indicator, could be constructed – better if at regional level.

Sources: European Tertiary Education Register (ETER), Labour Force Survey (LFS), (Los and Chen, 2016_[4]) (Los), PATSTAT, OECD Regional Database, Regional Innovation Scoreboard (RIS), Regional Input-Output Data for Europe (RegI-O)

Innovation diffusion outcomes

A number of indicators can be used to measure the extent of regional growth and sustainable progress (Table 4.3) and the strength of innovation diffusion at the regional level (Table 4.4).

Table 4.3. Indicators measuring the extent of regional growth and sustainable progress

Name of indicator	Measures	Data sources (see note)	
	Productivity		
Productivity level	Total economy; Manufacturing; Services (all ex-finance)	Reg	
Productivity growth rate (ten-year annualised)	Total economy; Manufacturing; Services (all ex-finance)	Reg	
Wag	es and earnings		
Average wages (Total compensation per employee)	Total economy; Manufacturing; Services (all ex-finance)	EUROSTAT	
Environmental progress			
Renewable energy generation	% capacity used of renewable energy generation	Reg	
Greenhouse gas emissions	GHG from generated electricity per capita	Reg	

Data sources: EUROSTAT SBS, OECD Regional Database

The table below shows indicators of innovation production and adoption of existing innovations. It uses the Oslo Manual definition to group innovation adoption indicators into those that are: (a) not at the frontier but (b) build on outside knowledge. Finally, many of the outcome indicators relate to the activity of SMEs because smaller firms play important roles in a region's innovation diffusion ecosystem and typically have a great need to catch up to larger firms.

Table 4.4. Indicators measuring the extent of regional innovation diffusion, especially for SMEs

Name of indicator	Does it capture (1) innovation that is (a) not at the frontier but (b) builds on outside knowledge?	Data sources (see table note)
Adoption of products or proc	esses with no or little modification	,
Average share of small and medium enterprises		
selling orders via computer networks**	a, b	ICT
with broadband speed at least>100 Mbit/s**	-	ICT
purchasing cloud computing services**	a, b	ICT
using electronic SCM systems**	a, b	ICT
selling orders via computer networks**	a, b	ICT
Innovation building on but differing substantially fro	om products or processes offered or used by othe	r firms
Number of patents per capita	1, b	Reg
Share of SMEs introducing a product or process innovation	1	RIS
Share of SMEs introducing a marketing or organisation	1	RIS
innovation Share of workers in digital occupations	-	BG
Difference between the share of workers in digital occupations among SMEs and self-employed and the share of workers with tertiary education across the entire economy	-	BG & LFS
Share of SMEs collaborating in research and innovation	1, b	RIS
Share of patent applications		
filed together with other patent applicants	1, b	Reg
filed together with applicants located outside of the region	1, b	Reg
filed together with applicants located outside of the country	1, b	Reg
citing other patents	1, b	PATSTAT
citing other patents filed also outside of the region	1, b	PATSTAT
citing other patents filed also outside of the country	1, b	PATSTAT
Number of patents per capita in specific high-tech fields (biotech, nanotech, medical, ICT, pharmaceuticals)	1, b	Reg
	reneurship	
Birth rate of employer firms	1	Reg
Growth rate of young firms	<u>-</u>	Reg

Note: (*) = indicator available at national level, (**) = indicator available at national level, could be constructed analogously at the regional level, Data sources: Burning Glass Technologies (**BG**), OECD **ICT** Access and Usage by Businesses Data, Labour Force Survey (**LFS**), **PATSTAT**

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