

Preface

Innovation is a major driver of productivity and long-run growth. However, fostering innovation is a complex policy issue because factors that affect firm incentives to innovate are varied and do not necessarily work in tandem. On the one hand, the level of competition bears upon pre- and post-innovation profits and may encourage or discourage innovation depending on the overall effect. Similarly, firm- and country-specific factors such as corporate governance, economic governance institutions, regulatory frameworks, and macroeconomic variables may also encourage or deter innovation as they create different incentives and constraints that affect the innovative effort differently. Furthermore, market structure and firm/country characteristics are likely to interact and create complementary or offsetting effects that call for careful consideration of policy choices.

This volume aims to disentangle the complex relationship between innovation and its potential determinants, paying special attention to the roles of governance and regulatory frameworks and the ways in which the latter interact with the market structure. Its findings call for careful policy choice and design. One general conclusion is that innovation may be associated with deadweight losses due to a positive relationship between market power and innovation – especially when market power is initially high. Another conclusion is that regulation is not necessarily harmful for innovation, especially when regulation imposes standards that firms, left to their own devices, may not be willing to comply with. The third conclusion is that the quality of economic governance institutions matters for innovation, on its own and in interaction with the market structure. Finally, corporate governance rules also matter but not necessarily in line with the predictions of the agency theory – which takes the level of product-market competition as given. Hence, this volume suggests that policy-makers must tread carefully through a long menu of policy alternatives, paying attention to the costs and benefits of innovation and to the quality of governance institutions and regulatory frameworks.