1. Objectives of the study

In order to comply with the mandate laid down in Council Resolution 92/12182 which calls for an overall analysis of the effectiveness of measures taken to complete the Internal Market, the Commission contracted with EAG to undertake a study on the exploitation of economies of scale associated with the Internal Market programme.

The consultancy team represents a collaboration between EAG, the SPES academic group (coordinated by the University of East Anglia) and PIMS Associates. This collaboration provides access to valuable data to supplement that available through Eurostat. Nevertheless the analysis involved in the study remains dependent on the overall availability of sectoral data which is not comprehensive, and the limitations of Eurostat data as discussed in Appendix A.

In particular, data on engineering estimates of Minimum Efficient Technical Scales (METS) for production facilities are not comprehensively available. Neither can these be extrapolated satisfactorily from previous estimates. It has therefore been considered more valuable to examine data that are available on the actual size (scale) of firms, and the extent to which this has changed by
industrial sector since 1981.

It was also considered important that the role of technical change was recognised in terms of its influence on economies of scale. This kind of change is independent of the elements that comprise the Internal Market (IM) programme, but clearly makes the isolation of the IM effect more difficult. As part of the study, some assessment of technological change was therefore necessary (see Appendix B).

However, the primary goal has been to evaluate the impact of the IM on changes in firm size by type of industry, and to draw conclusions with regard to shifts in the cost curve for the industry types most affected.

The study overall has therefore reflected the following approach:

a. A comprehensive review of the economic literature, focusing on the theoretical expectations regarding the realisation of economies of scale that might result from the increased integration resulting from the IM programme.

b. A detailed analysis of changes in the actual size of firms over the period 1986-91, as compared with the period 1981-86.

c. An econometric analysis of the effect of the IM programme on these changes and on changes in industrial concentration.

d. An examination of firm-specific data held on the PIMS database to identify important shifts in performance related to scale between the pre-1985 and post-1985 periods.

e. Case study research into the impact of the IM on dynamic economies of scale (related to R&D, marketing and training) and external economies of scale (related to geographic concentration of activity). Further case studies are currently in progress.

Following review of this Draft Report by Commission officials, appropriate amendments will be made and an Executive Summary of the findings will be produced as part of this introductory chapter.

2. Background: the Eurostat Opinion Survey

In March 1996 EAG received the results of the Eurostat survey of business opinions relating to the impact of the IM. A limited number of questions asked in this survey may relate to the question of exploitation of economies of scale. In particular, the questions concerning manufacturing production capacity, and efficiency in the provision of services may be indirectly relevant to production economies of scale. The results of these survey questions are given in Figures 1.1-1.3 (manufacturing) and Figures 1.4-1.6 (services).

It can be seen that, whilst manufacturing companies in Greece, Belgium, Italy and Ireland consider the IM to be more important to their domestic production strategy than do firms in the rest of the EU, there is little variation by sector or by size of firm. Overall, less than a third of firms consider the IM to be either very important or quite important.

In services, there is slightly more variation by sector and size of firm, with larger firms considering the IM to be more important to their efficiency in product/service provision than smaller firms. However, the overall proportion
of firms considering it to be very important or quite important is less than a quarter.

Figures 1.7-1.9 (manufacturing) and Figures 1.10-1.12 (services) relate to new product development. Strategies in this area are of course influenced by a wide variety of factors including competitive pressure, demand growth in particular product sectors and the introduction of new technology. However, the IM may have exerted an influence on firms’ ability to develop new products and services more efficiently through the exploitation of dynamic scale economies.

It is noticeable that firms in the same countries (Greece, Belgium, Italy and Ireland) as those in Figure 1.1 consider the IM to be important in their product development strategy. Figures 1.7 and 1.10 also suggest that the geographic dimension is little different between manufacturing and services as far as the IM impact on innovation is concerned. However, this impact is again oriented towards the larger firms in services, whereas the impact across size classes in manufacturing is fairly even.

Overall, more than a third of manufacturing firms consider the IM to be very important or quite important to their new product development, and more than a quarter of services firms believe the same.

The present study on economies of scale is particularly concerned with sectoral differences and, on the basis of the survey results, these appear to be more marked in services than in manufacturing and slightly more marked in innovation as opposed to production areas. However, it should be noted that services sectors are substantially less well covered by existing Eurostat data than are manufacturing sectors.

The present study relies primarily on official data available through Eurostat, although this has been augmented through opinion-based data available on the PIMS database and that generated through special case studies.