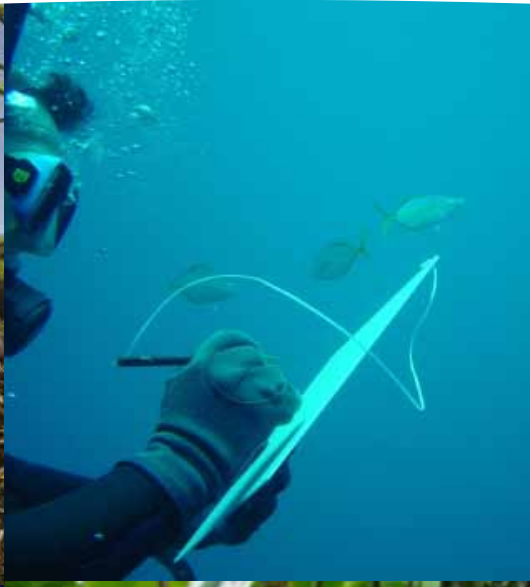




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Growth Factors in the Outermost Regions



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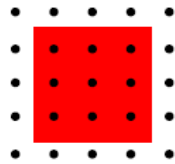
CONTRACT N°2009.CE.16.0.AT.101

Growth Factors in the Outermost Regions

Executive Summary

Version: final

Submitted by:



ISMERI EUROPA

In cooperation with



March 2011

Growth Factors in the Outermost Regions

EXECUTIVE SUMMARY

INTRODUCTON AND BACKGROUND

The outermost regions of the European Union are islands or archipelagos scattered in the Caribbean Sea (Guadeloupe, Martinique), in the Atlantic (the Canary Islands, Madeira and the Azores) and the Indian Ocean (Réunion), except for French Guiana, which is a small enclave in the Amazon region.

The study of growth factors in the outermost regions (ORs) is aimed at deepening the understanding of the process of economic development, identifying strategies to improve competitiveness and reduce dependence on imports and transfers. To analyse the development process of the ORs, an analytical framework to identify the drivers of growth as well as the vulnerabilities and opportunities has been established. This analysis was the basis for identifying new patterns of growth founded on unexploited potential and new sectors. The study consisted in the qualitative and quantitative analysis of data and literature as well as interviews of local stakeholders which took place during spring 2010. In this phase, flagship projects and policy proposals from the local stakeholders were collected.

In 1997, the Treaty of Amsterdam first introduced the legal basis of the concept of Outermost Regions. This was reinforced by the treaty of Lisbon which recognised the special nature of ORs and the need for specific action to foster their development. The ORs have set up a political unity of action to establish systematic cooperation with the European Union and make sure that their common problems are dealt with in a consistent and systematic way, by regional and other development policies and initiatives of the Union.

Several Communications of the European Commission have been issued since 2004 to boost growth policies in the OR. The first 2004 Communication (COM 343) defined a common strategy to reduce the impact of remoteness and improve accessibility, make the regions more competitive and strengthen their integration. The second 2004 Communication (COM 543) complements the strategy, providing

recommendations in terms of specific objectives to be pursued in the field of Cohesion Policy, RTDI Framework Programmes etc. The 2007 Communication (COM 507) points out how to grasp the opportunities of the common strategy and identifies specific targets within the new sectors, infrastructural needs related to transport and energy, environment, human capital and RTDI including the relationship with neighbouring regions. Moreover, this Communication deals with the issue of regional trade agreements, proposing specific arrangements that included ORs concerns in the EPAs. Finally, it addresses the ORs' opportunities in the EU maritime, agriculture and climate change policy. The 2008 Communication (COM 642) highlights the ORs' opportunities and potential, their comparative advantage on which development can be based. In October 2009, a Memorandum presenting the position and their shared priorities of ORs in the next programming period was signed. In 2010, the commitment to contribute to the establishment of the objectives and priorities within the framework of the Europe 2020 Strategy and for the post-2013 period, led to the signature of a new memorandum of Spain, France, Portugal and the ORs, in Las Palmas de Gran Canaria on the 7th of May 2010. Furthermore, the conference on 27-28 of May in Brussels allowed ORs' delegates to present their demands to the EU. The groundwork was laid for a cooperative approach in which the needs and interests of these regions are taken into account in all areas where EU policy can have a strong impact on the territories. The development policy of the ORs will be directed towards fostering a more independent and self-sufficient growth.

From 1997 to 2010 the ORs and the EU have paved the way for a cooperation in which the ORs' interests and needs are taken into consideration in all the relevant sectors in which policy has a strong implication for these territories. Within this institutional framework the ORs' development policy will be oriented towards a more autonomous and self-sufficient growth path to reduce the need for substantial and systematic support to the present pattern of development and to the traditional sectors. In particular, an agenda of events for 2010 and 2011 was drawn up, leading to a new strategy for the period 2014-2020.

MAIN HANDICAPS OF THE OUTERMOST REGIONS

ORs share most of the features of the small economies: small size of the domestic market, greater tendency to monopolistic structures in production and trade, scarce domestic natural resources and labour supply, narrow domestic output as well as little diversification, inability to

influence international prices, small export base and high import ratio to GDP, high degree of structural openness to trade, higher transport and communication costs of islands or land-locked territories etc. Such features have implications for the economic performance of small economies, in line with the endogenous growth theory which identifies key drivers such as private investments, human capital, sector specialization and competitive advantage, openness to trade, as the necessary conditions for growth.

The specific handicaps of ORs are addressed by the above mentioned Treaties and Communications. They consist of remoteness, insularity, small size, difficult topography and climate, economic dependence on a limited number of products. These handicaps do not affect all ORs with the same intensity and past policies have substantially changed the economic and social structure in which the handicaps impact.

Remoteness, insularity and small size

ORs are far from the main European markets and scarcely integrated even with their mainland; tourism and agricultural products link the local economy with mainland EU. Remoteness has a negative impact on most sectors because of the transport costs, which affect mobility of factors (labour and capital), trade and in general all forms of integration with the EU.

To deal with remoteness however in the past transport infrastructures have been built and a mildly positive trend in the maritime transport of freight can be observed in the last decade in all ORs except the Portuguese Islands. Air transport of freight increased in the late 90ies but then remained stable. At the same time air transport of people increased substantially almost everywhere thanks also to the opening of low cost routes. These trends helped to mitigate the isolation of the regions. Apart from Guiana, the ORs are archipelagos of small islands. Accessibility issues affect ORs not only in their trade and exchanges with the EU but also within their geographic areas and within the same archipelago.

Small size of the domestic market is an economic disadvantage which discourages private investment and produces a tendency to develop monopolistic structures and higher costs for the consumers for many goods and services, lowering the standard of living and penalizing the competitiveness of the regions.

Remoteness however does not affect Tourism, a sector for which the ORs' environmental and cultural diversity can be a competitive advantage. Tourism is particularly developed in Madeira and the Canary Islands but less in the Azores. In the French ORs, the hosting capacity remains

underutilised and the sector has not been able to pull the local economic growth. The data on tourism indicate that the sector's impact on the development of ORs differs greatly in size and performance.

Difficult topography and climate

The climate of these regions varies from maritime (e.g. the Azores) to tropical (e.g. Guadeloupe, Martinique and Réunion), to equatorial (Guiana). Most ORs are of volcanic origin and are characterised by very diverse relief from steep to flat, sometimes within the same region. Most of the social and economic life is concentrated in the coastal areas which are particularly exposed to extreme climatic events. Environmental risks are therefore high and the consequences of natural events such as floods, droughts etc. can be dramatic (e.g. the flood in Madeira in 2010). Furthermore, ORs must deal with other natural risks such as earthquakes, cyclones and tsunamis. Availability of drinkable water and problems linked to waste disposal are amongst the most important issues. The population density is very high in all ORs except Guiana and the Azores. It ranges from 260 inhabitants per square km in Guadeloupe and the Canary Islands to 350 in Martinique, while the EU27 average is approximately 114. The weight of agriculture, fishing and forestry in total gross value added provides an indication of exposure to climate change risks such as increased frequency of droughts with negative impacts on crops, reductions in the fish stocks etc. From this point of view, the Azores are very vulnerable but the issue is also relevant in the other ORs insofar as they aim at strengthening the productivity of their agricultural sector to lessen the external dependence on food supply.

Economic dependence on a few products

The traditional economic activities in the ORs are livestock farming (meat and dairy products), fishing, agricultural products such as sugar cane and rum, bananas, tomatoes and potatoes, plant and flower cultivation etc. On average agriculture, forestry and fishing generate less than 5% of gross value added but the traditional economic activities are important for the regional cultural identity, for the preservation of the landscape and tourist attraction and for their employment intensity. On average 80% or more of gross value added is generated by the service sector and over 15% is produced by industry. The Azores are the only exception with nearly 15% of gross value added generated in agriculture, forestry and fishing, while the service components account for approximately 70% of the total. Within the service sector, the share of public administration is particularly high in the French ORs. The structure of output and employment indicates a

dependency on food imports and income transfers in most regions.

POTENTIAL OF OUTERMOST REGIONS

Unique features and opportunities

Despite their handicaps, ORs benefit from specific drivers based on their endogenous potential. They have exceptional biodiversity and marine ecosystems, good potential for the development of renewable energies and leading-edge agro-environmental research, they can act as laboratories for studying and mitigating the effects of climate change. Moreover, they belong to the European Union and benefit from the EU funds as well as from the mainland support; they have a better skilled workforce, public services, and more advanced know-how than the other small islands or regions of their geographical area. This works as an opportunity to develop trade but also as a competitive obstacle since the cost structure is much higher than that of the other islands.

Growing and catching up economies

The potential of ORs materialized in a fast growth experienced during the last fifteen years. The real GDP increased at a substantially higher rate than in continental Europe (except in Guiana)¹. The high rate of growth explains their catching up speed, and is mostly due to the size of public investments and to rising private consumption acting as drivers of growth.

During 1995-2000, the annual growth rate of the ORs was higher than the EU average; 9.4% in Madeira was the top performance with the other ORs much in line with higher than average growth and Guiana the only exception with a negative growth of -0.5%.

In the 2001-2007 period, the average annual growth rate of the ORs varied between 4.3% in Madeira and Réunion to 3.2% in the Canary Islands, 3% in Guadeloupe, 2.9% in Guiana, 2.6% in Martinique and 2.1% in the Azores. The long term trend of higher than average growth continues during this period, except for the Canary Islands which experienced a slowdown of their catching up process with the mainland after reaching the average EU income p.c.

In the ORs, investments are mostly public driven and financed through transfers from the mainland which have compensated for the scarce impact of

¹ Average annual real GDP growth rates in 1995-2000: 3.1% in the EU27, 4.5% in Spain, 3.7% in the Canary Islands, 3% in France, 4.7% in Guadeloupe, 3.4% in Martinique, -0.5% in Guiana, 5.3% in Réunion, 4.4% in Portugal, 4.1% in the Azores, 9.4% in Madeira. Growth rates in 2001-2007: 2.3% in the EU27, 3.7% in Spain, 3.2% in the Canary Islands, 1.9% in France, 3% in Guadeloupe, 2.6% in Martinique, 2.9% in Guiana, 4.2% in Réunion, 1% in Portugal, 2.1% in the Azores, 4.2% in Madeira.

the integration and liberalisation of their markets, mitigating the effects of market price rigidities, imperfect mobility of factors and higher transport costs, which, to different extents, have prevented the ORs from fully benefiting from the Single Market and globalisation and from attracting private capitals.

Different patterns: intensive vs. extensive growth

In the French overseas departments, particularly in Guadeloupe and Martinique, the 2001-2007 income growth reflected a productivity increase, driven by the high salaries of the PA and the growth of its employment share while the increase in total employment was low. In Guiana and Réunion the determinants of growth were different and the employment increase was more substantial.

The other ORs experienced more extensive growth. In Madeira and the Azores, both labour productivity and employment increased. In the Canary Islands, the growth rate in labour productivity was negative while the GDP growth largely reflects a fast increase in employment.

Positive population dynamics: further growth potential and pressure on the labour market

The ORs' demographic features are characterized by a mildly positive population dynamics, lower than EU27 average growth (+0.4% per year in the period 2000-2007), except in the case of Guiana (+4%) and, to a lesser extent, the Canary Islands (+2.3% in 1998-2008). The dependency ratio is below the EU average (38.1%) especially where the combination of natural growth and mortality is "favourable" (e.g. the Canary Islands, Réunion, Madeira and the Azores).

In the French ORs, the employment rate is approximately 44% (2001-2008 average), about 20% lower than EU27 average (64% in the period 2003-2008). In the other ORs the employment rate is approximately in line with the European figure (the Canary Islands) or higher as regards male workers (the Azores) or both males and females (Madeira). The unemployment rate is much higher than the European average in the French ORs (i.e. 23.3%², approximately 4 times the EU27 level). In the Canary Islands unemployment was twice the European level in 2007 but experienced a sharp increase afterwards (i.e. 29.48%³). In the Portuguese islands, unemployment has been lower than EU average in recent years (i.e. about 7.2% in 2010⁴) but is increasing. The share of population with tertiary education is higher than average in the French

² INSEE, 2nd quarter 2009.

³ INE, 2nd quarter 2010.

⁴ INE, 2nd quarter 2010.

and Spanish ORs while it is lower in Portuguese ORs.

VULNERABILITY TO EXTERNAL ECONOMIC CONDITIONS

A synthetic indicator of vulnerability is a part of the quantitative analysis of regional data carried out within this study. Vulnerability is defined as the sensitivity to suffer from the exposure to economic conditions in the rest of the world, from trade vulnerability, to natural disasters and other factors associated with small size and insularity. Regions with low vulnerability are better able to deal with current (e.g. related to the economic crisis) as well as future challenges (e.g. related to environmental preservation and climate change). The index is affected by the availability of homogeneous regional indicators which cover up to 2007, however, it provides a first estimate of sensitivity which would be more precise if the ORs' data coverage were as detailed as those of the mainland European regions (see paragraph 2.3.3 and ANNEX B – Vol. I).

The variables used in ranking the EU27 regions on the basis of their socio-economic vulnerability are:

- GDP per head (level and % variation)
- Average population growth rate
- Dependency ratio
- Employment rate
- Share of population with tertiary education
- Population density

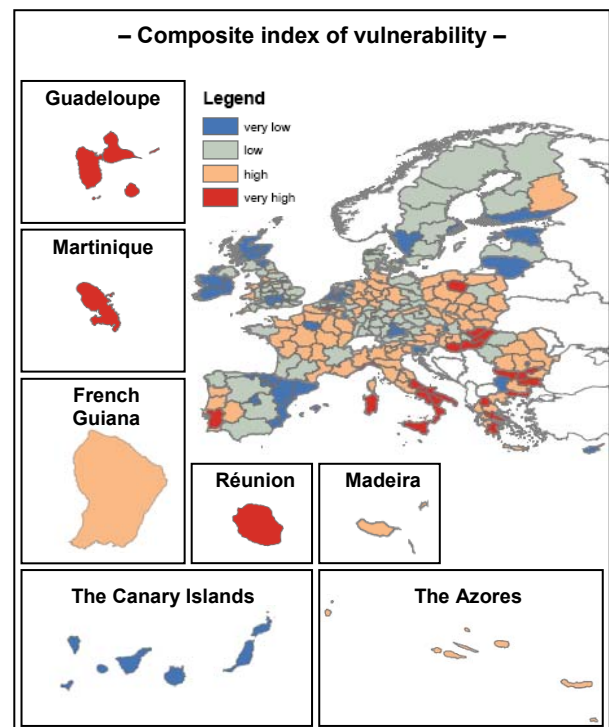
The remoteness handicap has deliberately not been included in the vulnerability index aimed at analyzing how and to what extent other constraints have penalized the socio-economic performance of the different ORs. In particular, we wanted to verify if a growing population with a balanced age structure and its educational attainments can be associated with a capacity to generate growth and employment and make these regions less vulnerable to negative economic conditions in the rest of the world. In this framework we implicitly assumed that a region with a dynamic labour market and a well educated labour force is better able to assure faster growth, compete in a globalised world and gain trade shares of the world markets. Finally, population density, a variable which captures anthropogenic impact on the environment, has been introduced⁵.

⁵ Unfortunately, it was impossible to consider more environmental variables (e.g. regions' vulnerability to droughts, change in population affected by 100 year return river floods, share of population living in coastal areas – below 5m elevation etc.). There are no homogeneous indicators of this type in the ORs.

This, together with GDP per head, can be considered as a proxy for the regions' ability to deal with climate change risks.

The results⁶ show that socio-economic indicators penalize the French ORs which are very vulnerable. Only Guiana, benefits from a positive population dynamics. The Portuguese ORs perform relatively better, especially Madeira which is exclusively penalized by its low education achievements, whereas the Canary Islands score well, due to the overall positive economic and social parameters. However, the recent deterioration of the economic conditions, resulting in increased unemployment and clandestine immigration, has in part mitigated these positive results.

The vulnerability index confirms that ORs differ greatly and that, even the most vulnerable, are not necessarily in a more disadvantaged position with respect to other continental EU27 regions or other islands such as those belonging to the convergence objective, in the Greek and Maltese archipelagos etc.



⁶ In relation to the computation methodology, the considered variables, each one representing a facet of vulnerability, were first normalised and then averaged in order to obtain the composite index. The index varies between 0 and 1, with higher values corresponding to higher vulnerability.

– Examples of vulnerability levels of EU Regions –		
Region - NUTS2	vulnerability index (1=max: 0=min)	vulnerability rank
ITG1 - Sicily	1.00	1
BG31 - Severozapaden	0.92	6
ES64 - Ciudad Autónoma de Melilla	0.85	11
FR91 - Guadeloupe	0.76	19
FR92 - Martinique	0.75	20
BE32 - Prov. Hainaut	0.75	22
MT00 - Malta	0.75	25
FR94 - Réunion	0.73	27
PT18 - Alentejo	0.72	30
GR25 - Peloponnisos	0.72	32
FR93 - Guiana	0.71	33
FR22 - Picardie	1.00	34
PL32 - Podkarpackie	0.70	37
PT20 - The Azores	0.68	46
FR83 - Corse	0.67	51
DE92 - Hannover	0.56	118
PT30 - Madeira	0.56	119
PT15 - Algarve	0.55	126
ES62 - Región de Murcia	0.30	235
ES70 - The Canary Islands	0.29	236
ES53 - Illes Balears	0.22	249
CY00 - Cyprus	0.17	258
UKM6 - Highlands and Islands	0.07	267

In fact two main results emerge: firstly that some ORs are performing better than others and consequently, were more able to deal with the various handicaps that they have in common; secondly, that, with the exception of the French ORs, the other members of the group (the Canary Islands, the Azores and Madeira) are not more vulnerable than many other Spanish, Portuguese and EU regions.

STRUCTURAL SIMILARITIES AND MAIN DIFFERENCES

The quantitative analysis and the results of the fieldwork highlighted that there are some common features that hinder the development of these regions and that a varying ability to deal with them has emerged in the past 15 years. Their main disadvantages are due to their heterogeneity and lack of integration with respect to the regional markets which they belong to geographically.

More than other penalizing factors, such as market size or exposure to various risks, from climate to extreme natural events, or external dependence on strategic sources of energy, this displacement from their natural regional market has affected their mode of development and has, up until now, prevented most ORs from fully exploiting their diversity with respect to mainland Europe. The displacement is not only a result of EU membership, which may limit or penalize their regional market integration, it is also due to their much higher living standards and higher wages (in comparison with their geographical locations) which undermines competitiveness and contributes to high unemployment. On the other hand, EU integration and the Single Market rules, inevitably connected with a different economic and social pattern of development, poorly adapt to their needs and stage of development which require more extensive growth and labour-intensive specialization. Thus trade integration, the most powerful driver of growth in the world economy and in the EU since the early 50ies, has not affected ORs as positively as it could have, given their geographical location. If we look at aspects such as market size, there are very small regions or cities or islands in the EU which do not suffer from the same problems and have enjoyed fast growth and a rising income; they were able to specialize their economies and integrate, irrespective of their size or geographical features.

The handicaps however have given rise to different features and performances within the ORs which do not allow us to consider these regions as homogeneous. Apart from the different social and cultural integration features which cannot be fully solved with generous welfare provisions alone, ORs are deeply affected by the pattern of development of the country to which they belong, even more so when they depend on investment and public consumption decisions often taken in their national capitals.

Similarities

The main structural similarities which characterise the regions are:

- Higher living standards in their respective geographic areas, which has been a factor of

attraction but also a source of higher costs and lack of competitiveness.

- A productive structure based on services and on construction while the manufacturing sector is weak and subsidized. The excess weight of the public sector in total employment leaves little room for entrepreneurial spirits and social dynamics to develop new emerging sectors.
- A large flow of transfers from the mainland and the EU have sustained private consumption and disposable income⁷.
- Private and public consumption are the main determinant of income growth.
- Significant structural low participation rate and long term unemployment caused by a mismatch between demand and supply of labour⁸.
- In manufacturing, only productions in the agro-food sector can face external competition, though to a different extent in the various regions.
- Private investments are insufficient to specialize in competitive productions and create new jobs in competitive sectors⁹.
- The lack of qualified manpower and of specialized skills acts as a self-perpetuating mechanism preventing the development of productions and services which need more intensive knowledge productions to counterbalance the remoteness and size handicaps. Moreover, this mechanism tends to encourage the brain drain.
- The lack of regional integration has created self-centred, protected and dependent economies which cannot develop their potential unless these main socio economic and structural factors are radically changed.
- Population needs and social standard aspirations are rising faster than domestic production.

Financial protections and subsidies, though necessary to sustain the present production pattern, cannot alone make a change in the right direction and often may risk crystallizing the "status quo" in which some economic and social groups, both inland and outside, may be better off. As a consequence the resistance to the necessary changes may be strong.

- The significant population growth is ill adapted to the typical labour-saving specialization of their mainland and of the EU, where growth is

⁷ These transfers varies and in some ORs may well be around 30 to 40% of the GDP.

⁸ It is worth noting that rates of unemployment significantly differ among the ORs.

⁹ R&D investments carried out since 2000 have still to show some impact on the productive and employment side.

based on productivity gains, high salaries and social standards.

- Environmental services for water as well as waste disposal and treatment are a common problem; at the same time there has been a greater use of renewable energies, but significant room for increasing their weight and lessening their dependence remains.
- Small islands (with the exception of Guiana) are very fragile from the environmental point of view given the scarcity of land and the conflict over its use for different functions, from residence to production, from infrastructure to agriculture. All functions are concentrated in the small coastal strips and flat portions of land which are congested and over utilized.
- These common environmental and land-use features require special attention to sustain the development patterns which limit the boundaries for development, and require a careful exploitation of the endogenous resources, within strict land use regulations, which at present are not adequate to assure sustainability.

The more sustained growth experienced by the ORs during the eighties and nineties is more closely linked to the national cycle than to the exploitation of their intrinsic characteristics. This has made a significant catching up possible for all the ORs and has permitted Madeira to overtake the national per capita income. Since the end of 2008 all the ORs have been suffering from the ongoing crisis, though to a lesser extent than most of the other EU regions, more exposed to external competition (see unemployment data presented in the regional analysis of the ORs - § 3 Vol. II and summarised in the regional outlook below). However, in perspective the flow of external transfers might have to be significantly slowed down as a result of the budgetary policy stance to reduce deficits.

Differences

The differences among the ORs are not less relevant than their similarities; they are mainly structural and concern the degree of autonomy in external trade and their ability to develop internal specializations.

- The natural growth rates of the population are, lower in Portuguese and Spanish ORs; where structural unemployment is much less pronounced, at least until 2008.
- Employment and value added sector shares differ significantly in agriculture, construction and tourism. As regards agriculture, these shares are higher in the Azores and Madeira; in relation to construction, employment and value added shares are higher in Madeira and the Canary Islands.

- The degree of dependence on imports is much higher in the French than in the other ORs, as a result of the past heritage of colonial economies on the one hand and of a long term orientation toward self-sufficiency on the other. The coverage of import with export varies from 6% in the French regions to more than 50% in the Portuguese and Spanish ORs which also have a larger tourist sector except for the Azores.
- The degree of self-sufficiency in local food consumption in the Canary Islands, Madeira and the Azores is much larger than in the other regions and guarantees greater economic independence and lower prices for low income brackets. The Spanish and Portuguese ORs are, on the whole, less dependent on transfer forms from the other EU regions.
- Development patterns between French regions and the other ORs differ, since the former tried to develop an import substitution strategy which was not really successful, while the latter focused on private construction and tourism to achieve more autonomy from public transfers. The higher productivity growth in the French ORs, has in fact been generated by a sudden drop in the activity rate in 2003 , and had an impact on internal prices fuelled by high public salaries, rather than on competitiveness of tradable production. On the other hand the other ORs were characterized by an extensive growth of the private sector and lower factor prices.
- The degree of dependence on major infrastructure investments from the mainland and, in general, on public transfer is significantly more pronounced in the French ORs than elsewhere; partly due to a generous welfare system and social standard equalization policies, that are less evident in Portugal and Spain, though still relevant.
- The development pattern based on tourism and related services and a relatively greater weight of agriculture has favoured the Canary Islands and Madeira. The Azores also have a more balanced pattern of production among sectors, which show less dependence on public service employment. In the French regions the tourist sector did not emerge as a driving force for development and as a specialization able to compete in the fast rising world tourist market, as a result of high costs and, sometimes, lack of skills and quality.
- Guiana is a special case since its fast development has attracted a large flow of migrants from the surrounding regions; a positive natural population growth and this migratory flow have created an excess labour supply that the small local economy cannot possibly absorb in a short time.

TRADITIONAL AND NEW EMERGING SECTORS

Over the last years the official development strategies have started to change in order to overcome the patterns sustained in the past.

From the interviews with stakeholders and official documents it has emerged that new fields of development are being pursued to focus on the potential of each region. At the present initial stage of development these fields cannot offset the structural imbalances and especially the large employment gaps. However, this approach to development that focuses on the strengths of the ORs can be considered the most effective to ensure a less dependent and a more competitive growth pattern, if and when the ORs succeed in developing these new fields in a competitive way.

Furthermore, this strategy is conducive to a very similar pattern of development in all the ORs where potential fields are similar; this could lead to synergies and complementarities which at the moment do not appear in their concrete development.

The present transition phase is based on a mix of old and new sectors, in which a modern agriculture, tourism and private services progressively increase their competitiveness and become tradable on a wider regional market. In addition the ORs aim to develop new sectors in manufacturing and advanced services (e.g. financial, technology transfer etc.). In this respect significant public investments in research and knowledge have already been carried out.

In economic terms the concept of growth potential is connected to untapped resources both human and/or natural which the production process of a region can rely upon, developing new technologies and skills or a new form of organization of the production factors. This definition fits well with the strategy needed for exploiting the ORs' potential. The mix of endogenous resources and new technologies and factor organization can give rise to a competitive advantage in the production of a set of goods and services.

Potential growth in the ORs can come from restructuring the traditional sectors of tourism, agriculture and fishery and new specializations which stem from the application of RTDI to old and new sectors. New and high profile skills, well focused and market oriented applied research as well as improved marketing need to sustain the process.

Traditional sectors

A high proportion of the workforce of most ORs is employed in **Agriculture**, maintaining the unique

environmental and cultural landscape and assuring a supply for the local food market and, an export good. Given the difficult accessibility and isolation of these regions, agriculture cannot be progressively dismissed if the ORs want to lessen the local dependence on imports and to preserve the landscape. Production and employment in agriculture, however, are declining and can only be enhanced by differentiating and enlarging the product specialization. This can be achieved with the support of the ongoing RTDI investments. The use of new techniques and discoveries can enlarge the variety and quality of the products and strengthen integration and competitiveness of the agro-food manufacturing value chain.

This strategy to develop the regional potential linked to climate, environment and local know-how is pursued by most ORs with different results and impact on the regional income. Specific opportunities have emerged from alternative uses of sugar cane, production of new fruits and vegetable species, livestock, fish farming, etc. These developments can be enhanced by more focused and market oriented research and by forms of clustering and networking to link weak private sector actors. The existing trade-off between the support of existing production or the acceleration of a change of cultivation has to be carefully considered by the authorities dealing with the agricultural and fishery policy.

Tourism has a relevant potential in most ORs and in some of them is a key sector for employment and external trade. It is based on an exceptional natural and cultural environment. The conflict between tourism and environmental preservation of the coastal areas and of the green areas need to be seriously tackled by these regions as a necessary condition for making tourist development sustainable in the long term and allowing the take off of alternative tourism products. Although tourism is well developed in most cases, its products are still traditional and weakened by increasing external competition; its potential is based on a product differentiation to adapt to the trend of demand segmentation away from the standard products for mass tourism. This should increase the quality, the value for money and should allow the tourist supply of the ORs to occupy new niches. At present, areas of specialisation such as eco, environmental, social, cultural and health tourism are still not fully exploited. The restructuring of the tourist service supply gives an opportunity to invest in new, small and more flexible establishments for tourist reception, more sustainable from the environment viewpoint. In this respect ad hoc professional training to sustain product differentiation and upgrading is fundamental in most ORs.

Emerging sectors

In addition, a host of new sectors and products can emerge from the application of RTDI to the development of the biodiversity which characterizes the ORs' natural environment, from the forest to the marine eco-systems. A list of applications are envisaged by local authorities in the area of health, natural medicine as well as cosmetics and many other sectors like food or energy or materials for eco-construction and wood.

Opportunities of the green economy can be pursued drawing upon the unique natural environment and its rich land and marine biodiversity. The development of competitive advantages in this area is a potential for growth and employment but is also very demanding, in terms of economic and social conditions to fulfil, from the availability of the scientific and technological skills to the market orientation of the RTDI, to assure the exploitation of the findings through spin offs of the research. On the whole, these have not yet been met and the ongoing regional policies based on innovation and RTDI, fall short of stretching the value chain of research to link to business applications, to create a critical mass for developing new products and services. This difficulty is however common to most of the convergence regions in the EU, and particularly to those which do not have significant knowledge based manufacturing firms to lead the process. This policy in the OR's is however still too young and results can be perceived only in the medium term if the above conditions are met, and if the obstacles are overcome by well focused policies. The regional policies need to focus and concentrate human and material resources, make them more market oriented, rather than disperse them in too many potential fields and thus will not reach the necessary critical mass to spill over the regional economy.

The ORs have had severe problems to assure the regular supply of fossil fuels and are penalized by higher cost of provision, due to accessibility and distribution handicaps. During the past years, the development of **renewable energies** has been pursued and favourable natural and environmental conditions exist in different regions to develop different renewable sources from bio-fuels to wind, solar and photovoltaic. In addition, in some ORs there is a growing experience in RTDI on renewable energies which to draw upon for their development. The insularity and small size encourage a wider development of small plants of renewable energies, which could aim to satisfy a much more significant share of total energy demand, given the higher cost of traditional sources and their unreliability. At the present time a number of experimental plants and of good practices may set the conditions for a

more planned and organized development of these sources at the regional level.

At this stage of development, **environmental services** dealing with the water and waste disposal are unavoidable since these issues have not yet been solved in any satisfactory way in most ORs, despite efforts to do so. Relevant investments are needed to satisfy those needs and give the opportunity to create local skills and equipment which can be exported to those geographical region where they do not exist, provided that they are cost-effective.

In most ORs, **maritime services** and port activities can be developed in relation to both cruise and nautical tourism, to shipbuilding maintenance and trans-shipping services. To make these developments financially sustainable they need to have a significant positive impact on local products and services provision. Most of these developments draw upon the geostrategic position of the islands in the Caribbean sea, in the Atlantic and in the southern Indian Ocean. However, these developments need to be supported in most cases by heavy investments which, if not properly accompanied by accurate feasibility and marketing plans, are in danger of being underutilized and impose a high opportunity cost, preventing the regions from investing in other useful infrastructures.

At the same time the **health, medical and social personal services** are well developed and supported by research and appropriate skills. Their potential for ORs development is linked to the opportunity to export these services and the skills developed for the local market. The geographical regions where the ORs are located have a much lower standard of such services and this creates opportunities for increasing their trade. However, these services generated within a public sector environment need to undergo substantial changes to turn towards a market and export oriented service.

The geopolitical location of the ORs and especially of the French regions and of the Canary Islands allows for the development of geostrategic investments to exploit the proximity to key markets in the Caribbean and Latin America, in West Africa and in the Indian Ocean. This potential need to be developed through an initial phase of regional cooperation involving local stakeholders, firms, and private actors; once the cooperation gives a concrete opportunity to exploit in some particular area or product their function of portals of the EU to increase their trade, the external policies need to support these opportunities.

In conclusion, these opportunities, and the conditions for their development briefly described above, leaves room for a positive view of the

future, provided that they materialize and that coherent and systematic policy implementation in the long term assures a balance between a radical improvement of the traditional sectors and the creation of a sufficient space of growth for the new products and sectors. To find a viable balance between new and old is the most difficult part of the strategy as resistance and obstacles to change are likely to arise. The policy needs to resist long enough to assure that changes take place with sufficient speed and effectiveness. To this aim they have to be shared by the stakeholders and by the most interested social groups through adequate partnerships. At present, the new sectors are starting to emerge in different ways in the ORs' economies but they have not yet reached any significant economic dimension and are not represented in a comprehensive set of "flagship" projects in which the regional public and private stakeholders can invest their energies.

In brief, from the analysis it emerges that ORs cannot be considered as a *unicum*. The handicaps can be adequately addressed with appropriate policy approaches. Minimizing handicaps is not only desirable but also possible.

REGIONAL OUTLOOK

Guadeloupe

Main features

The general features of Guadeloupe are similar (with nuances and differences) to the other ORs: a small economy with a low critical mass for key activities (industry is very weak; the innovative sector of new technologies / renewable energies is emerging). The population numbered 404,000 people in 2009 and the population density stands at 260 inh./km².

The growth in the income per capita during the last 15 years has been high, jumping from 46% to 76% of the EU regional average income per head. Still, the economic situation is characterized by:

- a 23.5% unemployment rate (2nd quarter of 2009; 46.7% for the young)
- a lack of qualified skills: 33% of the 25-34 age group leave school with a diploma
- an economic pattern made of a pervasive service sector mostly public administration, welfare, education and health on the one hand, and tourism and related services and a small share of business services on the other.

The economic development has long been supported by agriculture on the one hand and tourism on the other hand. Both sectors are facing a crisis and need to be adapted to the current challenges.

The manufacturing sector has always been weak, manufactures are undersized and the current strategy alternates between import substitution and export oriented productions. New strategies have been launched regarding incubators and technology transfer.

Biodiversity is a main feature of the development in Guadeloupe, being both an advantage – rich and diversified vegetation that could be exploited through RTDI investments – and a challenge because it has to be preserved in spite of a high population density.

Key issues and constraints

A new economic pattern of development has to be defined. In Guadeloupe the regional stakeholders realize that the emerging sectors need to spring from the endogenous potential and from research and new and innovative solutions applied to existing sectors and exploiting endogenous resources in agriculture and forestry: applications to environment biotechnology and the marine ecosystem; agro-food industry in tropical environment, health service, renewable energy development; new forms of sustainable tourism; the application of new technologies to the production of local goods and services.

The current system is not competitive and not sustainable in the long term (based on public transfer). It has furthermore a huge social cost, with a high unemployment rate and insufficient education and training of the workforce, in particular for young job seekers. Inequality is a major feature of the regional economy, even if the welfare system goes a long way towards alleviating disparities.

Spatial organization, with specific focus on the urban functions and urban renewal, utilities and environmental services for water, waste, renewable energy etc., also need to be addressed in order not to stall the economic development of the island.

Vulnerable and high potential sectors

With the exception of the protected sectors (public administration, personal services), most sectors are vulnerable, in spite of their high potential:

- The agricultural sector with its traditional production and insufficient technical skills is highly vulnerable to the external competition of low salary countries and to climate risks. The agro-food sector development would require profound transformations.
- Tourism also suffers from a loss of competitiveness. It needs to undergo a profound re-positioning in the Caribbean market in a more competitive position, which requires significant private investments,

discouraged by the perspective of a low demand.

- Biodiversity and energy are also high potential sectors: the first through the development of new products based on the use of natural plants (pharmaceuticals, cosmetics or building), the second with renewable energies and the ongoing RTDI activities carried out by the “*Pôle de compétitivité*”.

Martinique

Main features

The socio-economic development in Martinique is characterized by the following features:

- The domestic market is rather small (400,000 inh.), but the tourism sector attracts around 600,000 visitors each year, offering opportunities for regional products and services.
- A relatively high GDP and high standard of living, with respect to the regional context, reflect the catching-up trend of the region with the French and EU average, despite being affected by a strong and structural unemployment rate (22.0% in the 2nd quarter of 2009) with consequently fragile social cohesion and social inclusion.
- The fast economic growth during the last decade (1998-2008) mainly relies on the internal consumption of the domestic market rather than on investment. Since 2008, Martinique has been going through a stagnation phase due to the world financial crisis and the local social crisis (February 2009).
- The economic structure is overwhelmingly focused on the service sector, including the public administration and non-profit sector, and the traditional retail sector, boosted by the tourism industry which is a driving sector in the regional economy. However, this latter declined over the period 1998-2008, affected by several challenging issues: high labour costs compared to other Caribbean Islands, ageing infrastructures and equipments, lack of diversification of the product.
- There are few industrial activities, except the construction sector, and a dynamic agro-food industry already export-oriented in the mainland, Guiana, and Europe, not only focused on traditional products, such as sugar and rum, but also on products with higher added value.
- The qualification of the human resources has made significant progress in the last 10 years. However, education and training still remain a challenge for the region as there is a strong link between the level of education and

qualification and the ability to find a job on the regional labour market.

Key issues and constraints

Local actors classically insist on structural factors that hamper growth: the small size of the market that fosters the development of oligopolies (pressure on higher prices); the lack of a scale economy; and the dependency on a small range of strategic imported products. In addition, several major issues emerge.

The high level of the unemployment rate remains the key issue that tends to privilege the sectors which are characterised by intensive job creation (tourism, personal services) and to support the diversification of the economy (agro-food sector).

The lack of organisation and structuring of the main economic sectors make the dissemination of innovation processes, the transfer of know-how, the development of competences and lifelong learning programmes, the business-research cooperation more difficult, but also reduce the gains than can be potentially realized through the mutualisation of equipment in strategic sectors.

If innovation is relatively high on the policy agenda, there is still a need to convince businesses to develop innovation processes and to develop stronger business-research cooperation, not only in the agro-food sector

The private sector doubts the potential of the regional integration of the regional SMEs in the Caribbean market; the EU/CARIFORUM Economic Partnership Agreement (EPA) is clearly perceived as a threat; whereas opportunities really exist for developing an export strategy in the service sector (ICT, environment, engineering, energy).

Environmental issues concern the pollution of agricultural land, water and waste recycling, but also the management of the use of the scarce land for different needs (agricultural production, tourism, industry, urban, transportation) which often conflict and result in a negative impact on the production costs

Vulnerable and high potential sectors

Construction and tourism are vulnerable sectors. However, the latter remains a fundamental component of the regional economy because of its spillover effect on the construction, transport, agro-food and services sectors and because it is labour intensive hence providing opportunities to the young people. It urgently needs to be more professional and well trained, in order to diversify the portfolio of products and to update the equipment and infrastructures to European standards.

The following sectors benefit from high growth potentials:

- Agriculture and agro-food industries: in spite of a declining share in total employment and added value, it maintains an important potential with objectives on food auto-sufficiency and on the diversification of higher added value food products. The agro-food sector is offering promising perspectives with the development of a research (PRAM) and a technology transfer pole (PARM) that potentially meet the conditions of developing an innovative cluster.
- Personal services target elderly people based on providing health and bespoke services and the development of hosting infrastructures. The sector is however facing several challenges: the strong dependency on public funding; the solvability of the beneficiaries; the financial difficulties of the local public authorities; the lack of professionalization and training of the workforce (a master in management of health administrations has just been set-up at the University).
- Environment related services such as services in water and waste management. Strong competences and know-how already exist on these issues in Martinique and address local needs. There is also a real potential for export in the regional area.

French Guiana

Main features

Similar to the other outermost regions - a small economy with a low critical mass for key activities - the region remains specific in terms of demographic trends, migration, and geographic positioning. The presence of the Kourou space centre is also a very specific asset; it was the motor of growth during the seventies and eighties and continues to be a factor of stabilization of the regional economy and could be a factor of diversification on niche markets. Main features of the socio-economic development are the following:

- With only 221,500 inhabitants, the region is going through a period of fast demographic growth (+4% per year on average during the last decade) that entirely absorbed the growth of the regional GDP per capita resulting in an increasing gap with the French average¹⁰
- The region is affected by a relatively high unemployment rate (20.5% in the 2nd quarter of 2009) and by illegal migration from neighboring countries (Suriname, Northern Brazil) which is difficult to control.

¹⁰ its GDP per capita was 62% of the French average in 1993, it falls to 47% in 2007.

- The economic structure is dominated by the public administration sector (including education, health and social services), and the aerospace sector and related services. The economic fabric is weak lacking competitiveness, it is characterized by high production costs, and fragile enterprises.
- Whereas there are few and limited manufacturing activities (construction, an emerging but promising wood sector, a very small agro-food sector); the primary sector is rather weak and still underexploited (including the mining sector) despite the rich natural resources.
- The strong deficit of the trade balance reflects the high level of dependency from the mainland but also the lack of legal trade relationships with the neighboring countries. The EU/CARIFORUM EPA, and the building of the bridge on the Brazilian-Guianese border offer new opportunities of business but may also expose the region to risks (immigration, increased commercial competition etc.).

Key issues and constraints

Several major issues and constraints emerge, showing that French Guiana is still in a catching-up phase.

Demographic growth is seen both as a positive motor of growth and as a challenge. It offers a clear perspective of enlarging the internal market, and giving rise to a growing demand for basic infrastructures in education, social services, housing, energy, etc. However, it also puts great pressure on the labour market (absorption of new job seekers), and on the local public funding.

The lack of qualification of the active population implies enterprises and public administrations lack competences in management and in project engineering, making it more difficult to boost the innovation process within companies. In addition, even if the University has developed a larger offer of training, Guianese students are often obliged to study abroad.

Combined with the external remoteness, difficult internal accessibility hampers easy access to the primary resources (forests, agricultural products, fish, gold, plant biodiversity) and impacts the social cohesion of the territory by offering basic services to the population in the forest area.

Finally, the lack of structuring of the main economic sectors currently prevents endogenous development by stimulating local productions, and the potential for boosting the regional trade by establishing new distribution circuits for basic products and the exportation of added value services. The economic fabric is overwhelmingly made up of very small businesses, with limited competences and financial capabilities. The

smallness of the market and the limited number of enterprises in the same sector hamper the development of strong cooperation between enterprises.

Vulnerable and high potential sectors

There are a number of vulnerable sectors in French Guiana for different reasons. The aerospace and gold sectors are highly depending on the international market. However, whereas the aerospace sector should certainly not develop strongly in the coming years, the gold sector is still offering a considerable potential of growth, depending on a strong political willingness and on a consensus among the population. The construction sector is also highly dependent on local public investments (therefore vulnerable), however the local needs for basic infrastructures (due to the demographic growth) should support its development and the creation of jobs in the medium term.

The high potential sectors offering a higher added value are the following:

- Anticipating demographic growth (double the population in 2030) agriculture, agro-food and wood are promising sectors addressing the growing local demand for local products. The new «cluster» organisation “Maison de la Forêt et des Bois de Guyane” demonstrates that professionals are interested in organizing themselves, with the support of the public sector, to diversify their production and develop new products for the internal market. It could serve as a replicable model for other sectors (e.g. agriculture and agro-food).
- Four types of service offer a promising perspective of diversification of the local economic fabric: the valorisation of biodiversity (including the production of local plants) which depends on the capacity of the scientific base to “market” its knowledge and on the local actors to attract foreign investors; the renewable energy supply by addressing both the local demand and the regional market; the tele-technologies services (derived from satellite technologies) and ICT services applications; and the tourism sector which is still under-exploited and insufficiently “marketed”.

Réunion

Main features

Réunion is characterized by the following features:

- It is an isolated island, in the Indian Ocean, not located on the main maritime routes going

through the Mozambique canal. It is the furthest from the EU mainland of all ORs.

- A significant concentration of population (802,000 inhabitants, density over 300 inh/km²).
- The domestic market is not a small one *per se* (over 400,000 visitors / year).
- Rich nature and landscape, but challenging (an asset for tourism, a challenge for agriculture and infrastructure).
- The GDP and the standard of living are high, even if affected by unemployment and inequalities (e.g. 27.2% unemployment rate in the 2nd quarter of 2009).
- The construction sector is an important part of GDP and employment (16% of jobs).
- There are few manufacturing activities, except in the agro-food sector.
- The services sector has increased significantly (64% of jobs). The public sector plays a key role in maintaining communities in the mountainous and rural part of the island.
- The tourism sector is facing a difficult situation due to several factors: the sanitary crisis (chikungunya, 2004-2005) and the world crisis in particular.
- Human resources are in general sufficiently qualified to address new challenges and develop new activities; the level of education has improved; the University plays a crucial role.
- High vulnerability to natural disasters, above all of volcanic and seismologic sources.

Key issues and constraints

The economic growth in Réunion can be weakened by its dependency on the final consumption of the household and by the weight of the construction sector. Generally speaking, it also lacks competitiveness compared with the countries of the Indian Ocean. Infrastructures are also a weak point, the island is extremely remote from other countries and EU and the cost of transportation is particularly high. Demographic data also shows the pledge of the population growth and density on the sustainable development perspectives and on the social welfare (unemployment, illiteracy, ageing population).

There is a global awareness of the need for radical changes in the direction of a more competitive and market-oriented economy and that the oversized public sector cannot continue to grow as a response to the crisis. The strategic vision is that regional development needs to be based on a balanced integration of different sectors in which each contributes to the regional income, rather than following a specialized pattern with one sector acting as leading factor for development. The strategy aims at sustainable

development both by lowering dependence on fossil fuels for energy use and by changing the consumption and investment patterns by developing more knowledge intensive manufacturing and services, and being a laboratory for renewable energies experimenting and testing processes and plants.

Vulnerable and high potential sectors

Construction, which has to be renewed and adapted to new challenges (sustainable development), and manufacturing industries with their high production costs are vulnerable sectors. The lack of competitiveness affects both the local market and the external markets.

On the other hand, the following sectors benefit from high growth potentials:

- Agriculture and agro-food industries: in spite of a declining share in total employment and added value, agriculture maintains an important potential for prospective food auto-sufficiency and sugar cane production which can benefit from RTDI.
- Marine resources (fisheries and aquaculture): the potential is mainly related to the French "Exclusive Economic Zone" and the abundant resources. Aquaculture relies for an important part on RTDI. There is a project of *Pôle Recherche Mer* which aims at coordinating research organizations and research labs and should contribute to the development of the sector, including in fields such as cosmetics.
- High added value services (expertise, know-how, education and training as well as RTDI). They concern primarily agro-nutrition-environment, health, energy, ICT and may provide innovation to the regional economic fabric and have a high potential in terms of exports to the Indian Ocean region.

The Canary Islands

Main features

The socio-economic development in the Canary Islands is characterized by the following features:

- It is an archipelago made up of seven major islands, quite far from one another, giving rise to problems in terms of cohesion and economic efficiency (cohesion and efficiency may be in contradiction leading to difficult political choices).
- With a population of 2 million, and 10 million visitors per year, the domestic market is the largest of the outermost regions offering the strongest economies of scale for the local producers.
- The Canary Islands grew strongly during the 90ies resulting in the highest GDP per capita

among the outermost regions in 2008. However, the economy has been deeply affected by the world crisis since 2008 impacting on the two motors of the economy: tourism and construction¹¹.

- The regional economic fabric strongly depends on tourism and related services, and accordingly is highly exposed to external risks. The tourism sector is facing a very difficult situation due to the global crisis and an economic model which is focused on seaside resorts and is poorly diversified.
- The construction sector is driven by public works (infrastructures such as ports, airports and highways) – due to external financial transfers from the EU and national budget – and by private investments in housing/hotels/building stimulated by the tourist demand.
- There are few manufacturing activities, except the agro-food and tobacco industries, and oil refineries. The primary sector (agriculture and fisheries) is declining despite being a part of the regional identity.
- The services sector has increased significantly (81% of the employment) but has a high proportion of public activities (regional administrations in Tenerife and Gran Canaria, local administrations, social services, para-public agencies).
- Human resources are in general not sufficiently qualified – insufficient to address new challenges and develop new activities, even if the level of education has improved.

Key issues and constraints

The main challenges that need to be addressed are: social issues related to the increase of the unemployment rate (29.48% in the 2nd quarter of 2010); the environment; opening up to cooperation with African countries; diversification of tourism through niche markets; development based on endogenous RDTI capacities. To exploit opportunities, one “sectoral” and three “transversal” issues are at stake:

- Education and training: qualification of jobs is generally low and vocational training is insufficiently developed; too many young people leave school without a diploma.
- Innovation: there is an important potential in marine resources, renewable energies, biotech, ICT services. However, innovation is mainly perceived as technological, and insufficient attention is paid to innovation in services and to entrepreneurship. The regional cluster policy does not seem to be sufficiently promoted and focused. In addition,

the innovation process is also hampered by the small size of firms, their poor financial capacity, the difficulty of local public research labs in participating in large-scale research projects.

- Internationalisation: the objective is to build up and develop an offer of high added value services (public and private, through co-operation or market) for the neighbouring countries and Africa.
- Tourism-Construction: it is widely accepted that the “Canary model” based on tourism and construction must be maintained due to the number of jobs at stake, but has to be re-oriented: rehabilitation of ‘old’ buildings, especially rental buildings, introduction of eco-friendly criteria, improved urban planning, diversification of the tourist product (segmentation of the market), better trained workforce, marketing.

Vulnerable and high potential sectors

The vulnerable sectors in the Canary Islands clearly raises the question of the sustainability of the regional economic model – tourism, construction, and agriculture – and calls for a re-invention or a reform of the socio-economic model of regional growth which should be based on higher added value services and innovation support.

Several niche market sectors are considered promising; these are mainly based on innovation and RTDI activities:

- Renewable energies (wind and water energies)
- Biotechnologies, bio-pharmacy and bio-medicine are supported through the cluster policy. There is a scientific base in the universities, however a real critical mass is lacking; there are also a few innovative businesses in the pharmaceutical sector and in bio-medical engineering. Research on algae may have an impact on the agro-food industry, agriculture and the pharmaceutical/cosmetic sector.
- Sea-based activities (marine biotechnology, deep-sea water resources management and transportation services).
- High added value services: there is a potential for developing and exporting engineering services (water, waste treatment, desalination etc.) and other diverse high added value services to neighbouring African countries (e.g. expertise in health and sanitary systems, Geographic Information System, services to sea transportation, education).

¹¹ For instance the employment share of the construction sectors has declined to 10% in 2009 after a decade of relative stability.

Madeira

Main features

The socio-economic development in Madeira is characterized by the following features:

- From 1995, Madeira experienced a sustained catching-up with the Portuguese mainland with a higher growth rate (GDP and GDP per capita), good economic performance and a relatively low unemployment rate (approx. 5% over 2005-2007, it increased to 8.2% in the 2nd quarter of 2010). However, since 2008 Madeira has been going through a serious economic crisis like the whole Portugal.
- With only 247,000 inhabitants, Madeira offers a small market and consequently low possibilities for economies of scale, in spite of 1 million visitors per year.
- The regional economy fabric is to some extent similar to that of the Canary Islands, predominantly based on tourism, construction, and public administration. This high dependency upon tourism means a high vulnerability to the erratic and uncertain movements of tourism – influenced by the international context (world economic crisis) and natural hazards (e.g. rainstorm on February 2010)
- The construction sector is mainly driven by public works – due to external financial transfers from EU and national budget – and by private investments in housing/building stimulated by low interest rates since Portugal became member of the Euro Area.
- In spite of the limited contribution of agriculture (banana, vegetables, fruits and flowers) to the GDP (2%), it has an important role in the social fabric (identity) and for maintaining an attractive environment and landscape for the tourism industry. In addition, it still represented around 10% of the jobs in 2008.
- The limited number of manufacturing industries are mainly focused on traditional products (embroidery, wicker products), goods for the domestic market (food and drinks), and wine production which is one of the main export-oriented sectors on the international markets.
- In spite of the progress made during the last decade, human resources in the region are still not sufficiently qualified, compared to the EU27 (e.g. three times fewer people with higher education).

Key issues and constraints

To some extent, the world economic crisis showed the limits of the Madeira economic fabric,

by strongly impacting the motors of growth (tourism and construction). It also highlighted the difficulty of the public sector to stabilize the economy, due to the constraints on public budget expenditure. There is a local consensus on the need for: more sustainable development and more permanent jobs; a switch from a public to a business based economy (employment, investments, consumption, financial transfers); preventing the decline of the traditional sectors and fostering competitive, higher added value, and export-oriented activities.

The challenges and potentials in this 'new model' are as follows:

- the tourism industry, which will remain a "basic" sector of the economy, must be modernized; at the same time the economic diversification must be boosted (with a special focus on new high value added activities and advanced services).
- There is room for improvement both for workers and for training schools, hence, strengthening qualification of human resources is crucial for economic development.
- Moving towards a more competitive and market oriented economy less dependent on public demand means betting on actors and potentials of health services and new areas (creative industries, sea cluster, biotechnologies and natural resources) based on innovation and RTDI.
- Energy is a strategic sector for economic development, society and wellbeing. Renewable energies and improving consumption standards must be pursued.

Vulnerable and high potential sectors

Due to their exposure to the external context and negative trends, the vulnerable sectors in Madeira are clearly tourism (stronger competition and declining trend), construction (declining trend with an expected decrease of public transfers) and agriculture (structural difficulties and negative impacts of the European regulatory framework). However at the same time, the tourism industry still remains a high potential sector in terms of job creation provided that the tourism products and infrastructures are "refined".

Other high potential sectors are mainly related to innovation and R&D based activities for which the strengthening of the University of Madeira is essential (by achieving a critical mass and developing international partnerships). The fields characterised by the best prospects are:

- Biotechnologies and exploitation of natural resources (including marine resources)
- Energy
- Health/medicine
- Creative and cultural industries.

The Azores

Main features

The socio-economic development in the Azores is characterized by the following features:

- With only 245,000 inhabitants (living on 9 islands), the Azores offer a small market and consequently low possibilities for economies of scale, in spite of 350,000 visitors per year.
- Compared to Madeira, there has been no drop in economic performance, even though the GDP per capita grew higher than the national average in the period 1995-2008 and they experienced a catching-up.
- Historically, unemployment levels have been relatively low (3% during most of the 90ies but have increased more recently: 6.2% in the 2nd quarter of 2010) compared to both mainland Portugal and the rest of the EU. This reflects some dynamics of employment creation (building, public works) as well as significant levels of under-employment, particularly in the agriculture and traditional handicraft activities.
- The agriculture sector still contributes significantly to the GDP (10%) and employment (13%) and plays an important role in the social fabric; as a crucial element in the environment and landscape – all key-aspects for the tourism sector. However, the sector is strongly dependant on milk/animal production.
- The services sector has increased significantly, but reflects the role played by the public administration and social sectors, with a large proportion of public employment.
- Contrary to Madeira, tourism is weaker (4% of the GDP) and is a niche sector (aqua sports, trekking and excursions, nature sightseeing).
- There are few manufacturing activities, except the agro-food industry, focused on traditional products and goods for the domestic market. The construction sector is driven by public demand – due to external financial transfers from EU and national budget – and housing/building is stimulated by low interest rates.
- Human resource are limited, especially the skilled workforce for emerging activities that could be key activities for the future growth of the region.

Key issues and constraints

The world economic crisis had an impact on the construction sector and reduced the public

transfers from the mainland, due to the constraints on public budget expenditure. There is a consensus on the need for attaining a more sustainable development and creating more permanent jobs; the dependence from the public sector must be reduced and the agricultural sector must be diversified.

Challenges and potentials in this 'new model' are the following:

- The qualification of human resources need to be strengthened.
- A diversification of the economic fabric must be pursued to overcome mono-production; tourism and new advanced services need to be developed (sea and marine cluster, biotechnologies, valorization of natural resources) are referred to as 'windows of opportunity'.
- A reduction of energy dependency is already being achieved (geothermic and hydro sources represent around 43% of the regional supply) but a further step in this direction could be beneficial.
- The market of health and medical care services have a great development potential (also thanks to returning immigrants).

Vulnerable and high potential sectors

Due to their exposure to the external context and negative trends, the vulnerable sectors in Azores are the agro-livestock sector, exposed to international competition and changes in the regulatory framework, and the construction sector which was facing a negative trend investment well before the world economic crisis. Based on traditional and basic products, the manufacturing industries remain globally vulnerable due to higher production costs and a lack of competitiveness with regards to imports.

High potential sectors identified by local actors are:

- Tourism which is growing and has great potential for developing diversified niche markets based on the natural assets (UNESCO Heritage site).
- Environment and energy sectors (geothermal, renewable energy, energy efficiency management, RDTI, waste management).
- Health and medicine services: the Azores can count on the *diaspora* to invest in the Archipelago which offers a good location for senior citizens (residences and health care) as well as for diagnosis and treatment. The University of the Azores and a new Biotechnology and Biomedicine Centre on Terceira Island might play an important role.
- Biotechnologies/Natural Resources/the Sea: there are opportunities in several biotech

fields related to biodiversity and natural resources, including the marine resource – the potential is mainly linked to the Portuguese EEZ (exclusive economic zone) and the abundant sea resources available in the archipelago.

- High added value services: there are opportunities arising from the health and tourism development (ICT/customer relationship management at micro as well as middle/macro levels) and from activities developed in the university with international partners.

FLAGSHIP PROJECTS

Discussion with the regional actors in each outermost region stimulated ideas for a number of “flagship” projects, without necessarily a clear hierarchy among them, resulting in a catalogue of heterogeneous and potentially strategic projects that have not been completely elaborated¹². One region (Réunion), preferred to emphasise the importance of a comprehensive strategy rather than highlight specific projects. As a consequence, the role of the experts in proposing or selecting flagships projects was more important than expected, and accordingly, projects were less detailed than expected.

The following list of projects is not exhaustive (for more information see Vol. II of the study). Many of these flagship projects consist in urgent interventions, mainly public, which are necessary to realign the regions to EU and national standards in terms of basic infrastructures: transport infrastructures, waste management and treatment, tourism infrastructures, education infrastructures etc.

However, the list of projects reveals common features (and common needs):

- Supporting economic diversification through innovation related activities and structuring of key economic sectors (both in traditional and emerging sectors).
- The willingness to build the future economic growth on local assets and natural resources (agricultural, natural, marine and biodiversity).
- The inclusion of environmental and energy concerns, in particular the necessity to ensure a greater self-dependence in energy production by using renewable energies and promoting energy efficiency management.

¹² The Flagship projects presented in the report have been suggested by the interviewed regional officials and stakeholders. The list of stakeholders was discussed with the regions and open to their suggestions

- The re-building of the regional tourism strategy in the regions already tourist oriented (Guadeloupe, Martinique, Madeira, the Canary Islands), and the greater emphasis on the tourism sector as a provider of growth and jobs in the other regions (the Azores, French Guiana, Réunion), in a context of economic crisis that strongly impacts the attractiveness of the regions.

Guadeloupe

Many of the current and future projects in Guadeloupe consist in urgent interventions, mainly public, which are necessary to realign the region to EU environmental standards. These for example include: water distribution and waste treatment, the renovation of cultural heritage buildings, the extension and management of preserved land and marine areas, the improvement of the safety and environmental standards of existing constructions, the development of public transport networks, utilities and facilities that assure an acceptable living standard and quality of life.

This typology of flagship projects includes a host of activities, mainly infrastructure which will indirectly promote tourism, cultural activities, intelligent and high tech building techniques (RTDI investments are being carried out in this field) and accelerate the demand for skilled work and new technologies.

Public interventions aimed at improving the infrastructure endowment of the region are not a sufficient condition to stimulate the desired change of the regional development patterns. They should be accompanied by initiatives that encourage private investments. We can distinguish two areas in which there are opportunities to develop marketable services and to attract private capital:

- The first area includes: the development of port facilities in deep water for transshipment and related services; a yachting port with maintenance and repairing facilities for medium and large size yachts. Both projects have been finalized by the port authority of Guadeloupe. They were preceded by an economic feasibility study and are based on public and private financial support.
- The second area concerns the creation of some sort of cluster through an incubator in which the public research centres in agriculture, fishing and forestry cooperate with local manufacturing firms in the agro-food sector. The goal is to develop new products for the local market and sustain alternative uses of the traditional agricultural products as inputs for final manufacturing and food-stuff

(e.g. the use of banana flour in livestock production etc.).

Martinique

Some of the identified flagship projects are already relatively precise and are accompanied by preliminary studies. Some projects are simple and concentrate on a large investments, others are more complex and embrace various types of actions. The four projects listed below would support the consolidation and diversification of the economy addressing major challenges such as the structuring of economic sectors, the development of higher added value activities and the creation of jobs.

- Revitalization of the tourism industry by creating a second tourist pole in Saint Pierre that should become the showcase of the Martinique tourist offer (heritage and natural environment) and lead to the diversification of tourist activities toward higher added value niches competitive with respect to regional competition (e.g. cruises).
- Setting up an entrepreneurial cluster programme to improve competitiveness and to structure sectors, in order to foster inter-enterprise collaboration and to develop innovation processes within companies: in traditional sectors such as tourism and agro-industry and in emerging sectors such as valorisation of biodiversity, green technology and environment, personal services.
- Supporting the innovation processes for the diversification of agricultural products and agro-industries/agro-food products towards an innovative agro-food cluster (Technical Institute for Banana plant, creation of the Technical Institute for Tropical Products, development of agro-food products with the support of the agricultural research pole - PRAM - and the technology transfer pole - PARM).
- Creating a logistic platform for imports aimed at reducing production and transportation costs through "mutualisation" of containers and storage capacity and integration of logistic tools in SMEs.

French Guiana

In order to stimulate the desired change in the regional development patterns, interventions which reduce the dependence on public expenditure and encourage private investments are necessary. The following projects aim at stimulating the productive structure and private investments:

- The structuring of primary sectors (agriculture, fisheries, forestry, mining), aimed at supporting a clustering process, guaranteeing supply and quality of basic products,

developing niche products with higher added value (based on a first successful experience in the forestry sector).

- The establishment of the European Centre for Biodiversity (still in a feasibility study stage). The project is based on three pillars: strengthening research activities and economic valorisation (technology platform, pre-industrial platform); training human resource (training courses at the University) and promoting a scientific culture (pedagogical dimension); developing tourism related services (promoting the Guianese biodiversity as a tourism product). While it offers interesting opportunities, the project also raises some critical issues regarding its business model, its management and the political will to support it in a long term perspective.
- The setting-up of renewable energy production units (biomass, wind and solar energy, small hydroelectricity unit in the countryside) that should enable diversification of the energy mix and reduce the dependence on oil, delivery of energy supplies in the whole territory, valorisation of wood; and also should offer opportunities for export of services and know-how in the regional area.
- Attracting international investors to gold mining (Project HARMONIE, based on the former experience of the "Camp Caiman") through the exploitation of the gold mine on Camp Caiman in a sustainable manner (including re-forestation of the zone and co-operation with the support provided by the "Pôle Technique Minier" to SMEs and small producers).

Réunion

There is a strong and explicit consensus among local actors on strategic objectives. The latest expression of this consensus is to be found in "*La Réunion Ile Verte*" and in the Regional Innovation Strategy. Some of these projects are quite precise and are accompanied by preliminary studies. All proposals need to be carefully confronted with the economic analysis in order to assess their adequacy with the determinants of growth and to be discussed with public authorities to build up a concrete, detailed and realistic strategy.

The projects concern the following policy areas:

- Economic consolidation and diversification:
 - Repositioning of the construction sector in a perspective of sustainable development (actions on training, certification, business-research collaborations, financial engineering).
 - Development of a RTDI agro-nutrition-environment platform (strengthening the research base, mutualisation of instruments

for technology transfer and commercialization of research, investment in industrial and semi-industrial pilots).

- Creating a “Fisheries & Sea Resources” Pole (support to the fishery industry and to sustainable fishing, development of research and experimentation in aquaculture).
- Defining a tourism strategy.
- Infrastructures endowment:
 - Setting-up an optical fiber cable Réunion-Madagascar with connection to EASSY (Eastern Africa Submarine Cable System) to ensure a back-up.
 - Ensuring energy self-dependence (energy efficiency management, developing biomass energy, and experimenting marine energy production pilots).
 - Renewing airport infrastructures for hosting the AIRBUS A380 (linked to the tourism strategy to be determined).
 - Harbour infrastructures turning the port into a feeder for container ship.
- Setting up a regional (Indian Ocean) Health-Humanitarian platform of education, training and services with the creation of a regional school of Health and Medicine; transforming the “Centre Hospitalier Régional” (CHR) into a University Hospital (CHU) and strengthening the existing Red Cross Intervention Platform (PIROI) in the field of public health.

The Canary Islands

All identified flagship projects are coherent with the latest strategic documents, some of them are already relatively precise and are accompanied by preliminary studies; the feasibility of others still has to be verified.

- Renovating the tourism model, not only by supporting the renovation of tourism infrastructures but also by taking into account the entire value chain of the tourist sector. Tourism has lagged behind in terms of competitiveness since the second half of the year 2000 and the model is threatened. The importance of the investments and the share that tourism has in regional employment require a strong response from public policies (private investment alone will not be sufficient). Needs concern the renovation of ageing tourist infrastructures, the improvement of territorial planning, the upgrading of the service quality, the diversification of tourism products (eco-tourism/sustainable tourism, ‘health tourism’ etc.)
- Setting up and implementing a comprehensive cluster policy in a perspective of competitiveness that would be more focused on key economic sectors, covering

the ‘traditional’ sectors such as tourism and construction as well as the emerging ones such as biotech/biomedicine/biopharmacy. Services to production activities in each cluster and the ‘innovation’ dimension (including non-technological innovation) need to be reinforced; for each specific cluster, the ‘eco-efficiency’ dimension should be integrated into the strategic plan.

- Developing and implementing a programme of internationalisation. The rationale of such a programme relies on the small size of the regional market, a weak competitiveness that hampers exports of goods, and the regional capacities for developing exports of knowledge, expertise, and high value added services to neighbouring countries. Within this perspective, co-operation actions (non-profit) and export should combine and support each other through the development of partnerships. At the same time, internationalisation requires an upgrading of port infrastructures and services for freight and for developing cruise tourism, which can be an element of diversification of the tourism offer. There are already rather well identified fields in which the Canary Islands can export: eco-technologies (in particular water resources and desalination); health and sanitary systems; exploitation of marine resources; marine services (logistics, naval repair); and ICT.

Madeira

Most of the identified flagship projects have not been completed yet. They are ‘strategic options’ rather than definitive projects accompanied by preliminary studies. The economic crises encouraged such debate on future options. Some projects are simple and concentrate on a large investment. Others are more complex and embrace various types of actions. Proposals of flagship projects in Madeira consist in:

- The modernisation and renovation of the Tourism ‘model’ (with a systemic and integrated approach), that means: focusing on key-markets; adjusting to changes in distribution and transports as well as to new customers (re-understanding travellers); investments in marketing; preserving and reinforcing historical heritage sites; raising the quality of services; training human resources.
- The development of a coherent and comprehensive energy strategy including renewable energies. It is necessary to rely on the following strategic orientations: reducing the dependence on oil and diversifying by introducing natural gas and renewable energies; developing hydro-electric projects; looking for potentials sources in the medium

term (ethanol from sugar cane; geo-thermal; photovoltaic); and starting a sensitisation campaign to change the attitudes and behaviour in energy consumption.

- Building an international medical care cluster. The three fields that the future hospital in Madeira could investigate are: hereditary and allergic diseases; clinical tests; tropical diseases resulting from climatic change.
- The implementation of other projects with a potential for growth and a systemic impact (a sea cluster, biotechnologies and natural resources / the University / a cluster of cultural and creative industries / the Madeira Free Zone / a Monitoring Satellites Centre).

The Azores

Also in this case, most of the identified flagship projects have not been completed yet. The feasibility of all proposals will have to be checked in the light of the economic analysis in order to assess their adequacy with the determinants of growth. Proposals of flagship projects in Azores consist in:

- A coherent and comprehensive energy strategy based on renewable energies with an integrated approach, based on the "Green Island programme"¹³ involving universities and companies (120 people of which 60 PhD). Research activities are combined with concrete realisations of geothermic energy installations, wind power and storage technologies, energy inter-connection of the Azores by under-seawater cable etc.
- A better management of waste with the following objectives: prevention in the production of waste/residues, recovery of their value and minimisation of their negative impacts; promotion of eco-efficiency in firms; financial support to waste/residues management and recycling.
- The development of the tourism sector through a systemic integrated approach. The focus should be on niche markets such as: nature tourism, resort tourism, golf, health tourism, cruises, sports, culture, etc.
- The development of an international medical care cluster (extension of the medicine degree at the University, linked to the creation of a medical cluster specialised on senior citizens, diagnosis, treatment, recovery). The creation of the Centre of Biotechnology and Biomedicine of the Azores, on Terceira Island (a university / hospital / government

¹³ It intends to develop new methodologies to identify cost-effective sustainable energy solutions and options utilizing natural resources that are indigenous to these areas.

partnership) could be a major element in this health cluster.

- Projects with a growth potential and a systemic impact such as the sea cluster focused on biotechnologies and natural resources, the development and internationalisation of the University and the setting-up of a Technology Park.

CONCLUSION

Because of their structural handicaps, the ORs suffer from their scarce integration in the EU and world market. However, through tourism and other service exports some regions managed to lessen those constraints, develop local productions and are well integrated into the international tourist market. For instance, in the Azores the economy is more balanced in sectors with a relevant residual employment in agriculture (concentrated on meat/milk).

Those regions which were less successful in developing an export oriented production, had to rely on increasing external transfers from the public sector or public development projects, which absorb an ever increasing portion of the workforce (approx. 40% in the French Antilles). The weight of the public sector remains significant also in the former better integrated or balanced ORs.

This pattern of growth is not self-sustainable in the medium-long run and may even become a structural and cultural obstacle to a development pattern based on competitiveness, which may require more investments and less consumption in the short term.

ORs need to become progressively more autonomous from the public sector and increase their ability to develop their endogenous resources and their potential on the basis of private investments either local or external. The present specializations need restructuring and re-positioning and new productions in manufacturing and services need to widen the regional export basis or at least fill the external trade gap, in particular in the perspective of the EPAs (economic partnership agreements).

At the present time ORs enjoy some forms of protection and structural aid, though to different degrees depending on their country, which compensate for their disadvantages in costs and relative size, as well as for their remoteness. The crisis is at the same time lowering the employment and income growth trends, and the tightening national budgetary policies worsen the overall scenarios of public transfers. Since financial supports have now become even more urgent than before the crisis, the question is not

whether or not to continue support, but what to support and how long it will take to reach which objectives in the medium term.

If the policy mix is not linked to results it will not stimulate those transformations which are deemed necessary to create a self-sustained and autonomous pattern of development in the medium term; furthermore, the achievement of the necessary social and economic changes may become more difficult.

The strategic priorities and a clear set of quantified policy objectives and the time span to achieve them need to emerge clearly from the political debate, and the support policies to the economy designed accordingly.

The present situation gives all EU regions and ORs in particular the imperative to revise their strategy and adapt it to the new growth paradigms based on competitiveness and trade. The development policy needs to focus on these transformations in a coherent and systematic way with a clear perspective of the objectives and of the choices to make, which in most cases require profound cultural and social changes. The ORs must respond to this imperative and in doing so they have the same opportunities and performance expectations of other growing EU regions.

Responsible editor: Ana-Paula Laissy, European Commission, Regional Policy DG, Coordination of Outermost Regions Unit.
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