

A dynamic splash of bright orange liquid, resembling paint or juice, forms a circular shape around the central text. The splash has various droplets and streaks extending outwards, creating a sense of movement and energy.

PUBLIC POLICIES FOR CREATIVITY AND INNOVATION:

Promoting the
Orange Economy in
Latin America and
the Caribbean

August 2017

José Miguel Benavente | Matteo Grazzi

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**Cataloging-in-Publication data provided by the
Inter-American Development Bank
Felipe Herrera Library**

Benavente, José Miguel. Public policies for creativity and innovation: promoting the orange economy in Latin America and the Caribbean / José Miguel Benavente, Matteo Grazzi.

p. cm. — (IDB Monograph ; 557)
Includes bibliographic references.

1. Economic development-Technological innovations-Latin America. 2. Economic development-Technological innovations-Caribbean Area. 3. Creative ability- Government policy- Latin America. 4. Creative ability- Government policy- Caribbean Area. I. Grazzi, Matteo. II. Inter-American Development Bank. Competitiveness, Technology and Innovation Division. III. Title.
IV. Series.
IDB-MG-557

JEL Codes: O39, O54, Z11, Z18

Keywords: creative ecosystem, creativity, innovation, Latin America and the Caribbean, orange economy, public policies

Publication Code: IDB-MG-557

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Washington, D.C. 20577
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The Institutions for Development Sector was responsible for the production of this publication.

Production Editor: Sarah Schineller (A&S Information Specialists, LLC)

Editor: Sheila Mahoney

Design: Miguel Lage Martínez

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Abstract

The orange (or creative) economy is an increasingly important driver of economic development in Latin America and the Caribbean. This study presents the main challenges that the region faces in terms of definition, measurement, and market and government failures, introducing a novel conceptual framework to understand its linkages with innovation and analyze the role of the public sector. In particular, the study builds on the concept of creative ecosystem to propose a systemic approach to design public intervention in the area, based on a policy mix to simultaneously stimulate supply, demand, and interaction among the various actors of the ecosystem.

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* This publication is the result of cooperation between the Competitiveness, Technology, and Innovation (CTI) and the Cultural, Solidarity, and Creativity Affairs (CSO) Divisions of the IDB. The opinions expressed in this publication are those of the authors and do not necessarily reflect the views of the IDB, its Board of Directors, or the countries they represent. The authors wish to acknowledge the substantial contributions of Leonardo Ortega and Juan José Price. They are especially thankful to Trinidad Zaldívar and her team for her technical inputs and valuable suggestions, as well as their colleague Ignacio de León.



1. Introduction and Motivation

The term **orange economy** is commonly used in Latin America and the Caribbean (LAC) to refer to what is also called the creative economy. First introduced in Buitrago and Duque (2013) to represent the particular set of activities based on creativity, the orange economy is becoming even trendier than innovation in the region.¹ However, although attractive, the concept is still fuzzy. Is there any part of the economy that is not creative? It could be that some products are routinely delivered without any major content of creativity at the production or distribution phases. But supplying new goods and services and improving existing ones, which adds value for consumers, involves a large amount of creativity. And this definition is not that far from what has been traditionally used to characterize innovation.

The difference lies in the focus of the changes. On one hand, creativity is generally related to aesthetics (i.e., the appearance of goods and services) and the changes in the emotions that these products generate in consumers. On the other hand, traditionally, innovation has been related to scientific and technological progress, and associated with changes in product functionality that can be directly linked to generating economic value.

But if a good or service is aesthetically or emotionally desirable (socially and/or privately), this does not mean that it has no economic value or that it does not follow economic rules. On the contrary, its production process requires capital, labor, and knowledge that could have been used for other activities. In other words, it is clearly part of the traditional economic problem.

However, often the real contribution of creative activities to the aggregate economy is not recognized. Further, it is difficult to clearly identify what inputs are required and the impacts such activities generate. Characterizing creative activity is not a trivial task, but this does not mean that it does not exist or that it is not generating value for producers and, in particular, consumers.

We recognize that there is still no adequate conceptual framework for the creative economy that could help assess the relevance of creative activities and to discuss and evaluate the role of different economic and social stakeholders in promoting and developing such activities.

This document is designed to respond to this need by presenting a comprehensive discussion of the Creative Economy from an economic perspective. In the next section, we briefly discuss the definition of the concept and related activities. Afterward, we discuss the relationship between innovation and creativity. Then we

¹ For example, *The Orange Economy* (Buitrago and Duque, 2013) is by far the most visited document on the IDB website, with more than 180,000 downloads as we write this article.

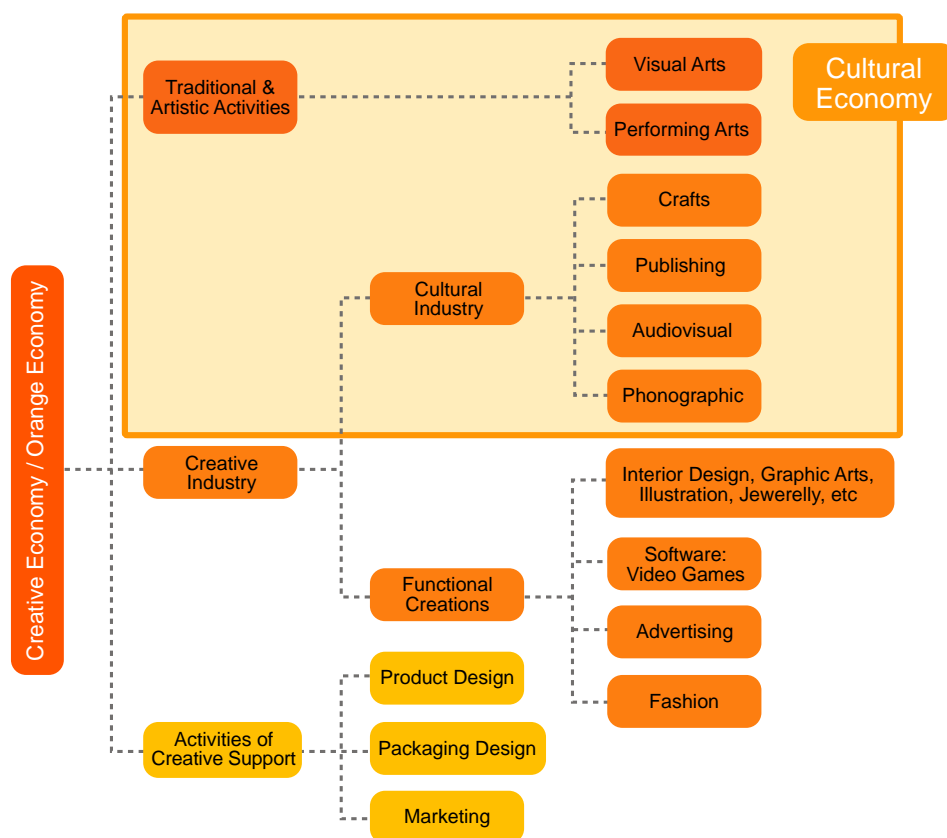
describe the methodologies commonly used to measure the economic contribution of creative activities and the key available figures for the region. We then introduce the concept of a Creative Ecosystem and assess the role of each of its agents in promoting the development of a creative economy. In two sections, we focus on the role of the public sector by analyzing the economic rationale of public intervention and available policy instruments. Then we consider the institutional designs necessary to allow the public effort to yield the expected results and not generate involuntary obstacles or duplicate efforts of different agents in the ecosystem. Finally, we provide some policy recommendations based on the experiences of countries more advanced in creative activities and the body of knowledge accumulated by the IDB.

2. What Is the Creative Economy?

Trying to avoid being too simplistic, for the purposes of this document, we consider the orange (or creative) economy the group of activities through which ideas are transformed into cultural and creative goods and services whose value is or could be protected by intellectual property rights (IPRs). This approach builds on the commonalities among the previous work of the IDB (Quartesan, Romis, and Lanzafame, 2007; Buitrago and Duque, 2013; Oxford Economics, 2014) and definitions produced over the years by a variety of organizations worldwide (see Box 1). Specifically, these commonalities include: (i) the recognition of creativity, arts, and culture as productive endeavors; (ii) the relationship with generating and exploiting IPRs, in particular copyright; and (iii) the direct role of these activities in the value chain that transforms ideas into products.

Following this approach, the creative economy includes activities related to three main concepts: (i) traditional and artistic activities, (ii) the creative industry, and (iii) activities that provide creative support to traditional industries (see Figure 1).

Figure 1. Definition of Creative Economy



Source: Authors' elaboration based on the taxonomy presented in Buitrago and Duque (2013).

Traditional and artistic activities consist of efforts related to preserving and transmitting the material and immaterial cultural heritage of a society. This component of the creative economy includes activities such as literature, visual arts (e.g., ceramics, painting, and sculpture) and performing arts (e.g., theatre, dance, and opera). **Creative industry** comprises business activities where the value of the final output is mainly due to its creative content, including *cultural industry* (activities recognized to be strongly related to culture, such as publishing, audiovisual, and phonographic), and *functional creations* (output is creative but not necessarily related with culture, such as video games, advertising, or fashion). We have called the sum of traditional and artistic activities and cultural industry the **cultural economy**. Further, it is possible to identify **activities of creative support**, which are part of the value chains of other industries. In this case, the output of the creative activity is used as an intermediate input in the production process of a good or service that is not necessarily in itself creative. Typical examples are product design, packaging design, and marketing.

Progressively, the creative economy has been recognized as an important driver of economic development (Potts and Morrison, 2009), directly contributing to the economy of a country in terms of value added, exports, employment, investment, and productivity growth. Recent estimates show that creative and cultural industries² generate revenues of US\$2,250 billion and 29.5 million jobs worldwide, employing approximately 1 percent of the world's active population (Ernst & Young, 2015) and presenting high innovation and productivity rates (Bakhshi and McVittie, 2009; Müller, Rammer, and Trüby, 2009). However, many creative professionals work outside creative industries,³ and official figures for the United Kingdom indicate that the whole creative economy accounted for 8.2 percent of gross value added and 8.8 percent of total jobs in 2014 (DCMS, 2015). The economic contribution of creative activities is both direct and indirect, both within and outside creative industries. In fact, creative outputs are closely related to the innovation dynamics of a society as a whole and often their benefits spill over to other sectors.

² The sectors considered in the Ernst & Young (2015) study as belonging to cultural and creative industries are television, visual arts, newspapers and magazines, advertising, architecture, books, performing arts, gaming, movies, music, and radio.

³ Cunningham and Higgs (2009) indicate that there are more creative workers outside creative industries than within them.

Box 1. Definitions of Creative Economy and Related Concepts

There are many definitions of creative economy. Some overlap in the sectors considered creative, others propose unique sectors.

UNESCO (2013): “[cultural industries] has come to encompass a wide range of fields, such as music, art, writing, fashion and design, and media industries (e.g., radio, publishing, and film and television production). Its scope is not limited to technology-intensive production, as a great deal of cultural production in developing countries is crafts-intensive. Investment in the traditional rural crafts, for example, can benefit female artisans by empowering them to take charge of their lives and generate income for their families, particularly in areas where other income opportunities are limited. All of these productive domains have significant economic value, yet also are vectors of profound social and cultural meanings. (...) The term creative industries is applied to a much wider productive set, including goods and services produced by the cultural industries and those that depend on innovation, including many types of research and software development.”

UNCTAD (2008): “...the ‘creative economy,’ ... can be summarized as follows:

- The creative economy is an evolving concept based on creative assets potentially generating economic growth and development;
- It can foster income generation, job creation, and export earnings while promoting social inclusion, cultural diversity, and human development;
- It embraces economic, cultural, and social aspects interacting with technology, intellectual property, and tourism objectives;
- It is a set of knowledge-based economic activities with a development dimension and cross-cutting linkages at macro and micro levels to the overall economy;
- It is a feasible development option calling for innovative, multidisciplinary policy responses and inter-ministerial action;
- At the heart of the creative economy are the creative industries.”

The ‘creative industries’:

- are the cycles of creation, production and distribution of goods and services that use creativity and intellectual capital as primary inputs;
- constitute a set of knowledge-based activities, focused on but not limited to arts, potentially generating revenues from trade and intellectual property rights;
- comprise tangible products and intangible intellectual or artistic services with creative content, economic value and market objectives;
- are at the cross-road among the artisan, services and industrial sectors; and
- constitute a new dynamic sector in world trade.”

Box 1. Definitions of Creative Economy and Related Concepts (Cont.)

WIPO (2003): “The core copyright industries are industries that are wholly engaged in creation, production and manufacturing, performance, broadcast, communication and exhibition, or distribution and sales of works and other protected subject matter. Four points could be mentioned in relation to this definition:

1. It reflects functional complexity: (a) creation, production, and manufacturing (i.e., producing); (b) performance, broadcast, communication, and exhibition (intangible forms of disseminating); and (c) distribution, sales, and services (distribution or tangible dissemination).
2. All three functions in the proceeding point cover individuals and firms whose activities are entirely related to works and other subject matter for copyright protection.
3. The core copyright industries as a category could not exist or would be significantly different without copyright in works or other subject matter. Therefore for the industries in that category, 100 percent of the value added should be assigned as copyright contribution to the national economy.
4. Only that share of the distribution industry which is entirely dedicated to distributing copyrightable materials is included in the core copyright industries.”

DCMS (2001): “[creative industries are] those industries which have their origin in individual creativity, skill, and talent and which have a potential for wealth and job creation through the generation and exploitation of intellectual property.”

3. Innovation and Creativity

Innovation is a key determinant of long-term economic development. Empirical evidence shows that about half of the variation in income levels and growth rates among countries is due to differences in total factor productivity (Hall and Jones, 1999). Previous research found that investment in innovation explains up to 75 percent of the differences in total factor productivity growth rates, once externalities are considered (Griliches, 1979).

In its essence, innovation is the transformation of new ideas into economic and social solutions (Navarro, Benavente, and Crespi, 2016; Crespi, Fernández-Arias, and Stein, 2014). Innovation can be a new way of doing things more efficiently (a more effective use of resources), a new or significantly improved product (good or service) or process, a new marketing practice, or a new organizational method in business practices, workplace organization, or external relations (OECD, 2005).

Traditionally, this definition has been interpreted with a focus on changes in functionality and with an emphasis on technical improvements. However, there is increasing consensus that a broader scope needs to be considered in defining innovation that includes transformations that do not necessarily improve the objective functionality of a good or service, but modify its aesthetic and appeal. In other words, the transformation changes how people perceive the product or service. This has been defined as *soft innovation* (Stoneman, 2010).

On this basis, two types of soft innovation can be identified (Stoneman, 2010). First is innovation within creative industries, where the value of the final output is mainly aesthetic and not functional (Miles and Green, 2008). For example, a firm operating in the fashion industry may improve its performance by introducing technological innovations in the production process of clothes, but the core of its activity will always depend on the capacity to create new, appealing designs. Evidence from Europe shows that, on average, creative firms are more innovative than the rest of the economy, including firms in knowledge-intensive sectors (Müller et al., 2009).

Second is innovation resulting from activities of creative support. In industries where the final product is mainly functional, aesthetic inputs can be key components of the production process, determining how consumers perceive the functionality. For example, in the automotive industry, between the new model of a car and the previous one there are only a few functional (sometimes very innovative) improvements. Most of the differences are external and interior aesthetical changes, usually the result of design activities. Under the traditional scope of innovation theory, none of these changes would have been considered innovation (specifically technical innovation) and none of these activities would have been considered innovative. Yet, it is the way the car looks and how consumers feel when they drive it that substantially determine car sales and, consequently, a model's value.

Evidence of the impact of such activities on firm performance is still limited but there is a growing body of research analyzing returns on copyright, trademarks, and design. In particular, design activities are found to be linked to significant improvements in terms of productivity growth, innovation, and export sales (Gemser and Leenders, 2001; Haskel et al., 2005; Sentance and Clarke, 1997).

However, the link between the creative economy and innovation is complex and goes beyond soft innovation. The creative industry also contributes to a society's innovation performance by increasing demand for state-of-the-art technology. In particular, cutting edge, tailor-made information and communication technologies (ICTs) developed by creative firms could influence the overall market, promoting new technology diffusion in other sectors of the economy. Creative activities that produce intellectual property are also an important source of external knowledge and ideas that enable other innovation activities in traditional sectors.

Finally, creative industries can support innovation through the mobility of their workforce. Creative workers take ideas, knowledge, and creative potential with them when hired in other industries (Müller et al., 2009).

4. Measuring the Economic Contribution of the Creative Economy

Even if the creative economy is recognized worldwide as a more and more important driver of development, measuring its economic contribution is challenging.⁴ Clearly, information is limited. Further, there is neither an agreed framework nor a shared definition of the creative economy to guide estimation exercises (Oxford Economics, 2014).

4.1. Commonly Used Indicators

Three main indicators of economic activity are commonly used: GDP, employment, and international trade flows.⁵ GDP, usually in per capita terms, is the most accepted indicator of economic growth. Occupation is a good measure of how inclusive a development strategy based on creative sectors can be and, along with GDP, is required to measure labor productivity (Bille, 2012). Measuring trade flows is consistent with a development strategy based on openness and with concern for cultural diversity (Janeba, 2004; Rauch and Trindade, 2009).

However, accurate measurement requires adequate data, which in this case is not generally available at the needed level of detail or is not comparable across countries⁶ (Oxford Economics, 2014; Throsby, 2010). There are a wide array of technical reasons for this deficiency, such as an inadequate classification system and the high level of informality in the creative economy. Classification systems designed to account for traditional economic activities—such as manufacturing, mining, and agriculture—often overlook services by grouping them into broad general categories, without the level of detail needed for an accurate analysis of emerging sectors, such as the creative economy. Also, informality makes creative activities underrepresented in the official data collected by national statistical agencies and other entities specialized in data collection.

⁴ Oxford Economics (2014) comprehensively reviewed data availability, noting that only five of the 45 countries examined published data at a 3- to 4-digit level of disaggregation, the level required to make good estimates of the economic contribution of a sector. Five countries reported statistics at a 2-digit level of disaggregation, 22 countries at only the 1-digit level, while the other 13 countries did not report these figures at all.

⁵ Some countries complement these indicators with variables related to other dimensions, such as creative consumption and/or infrastructure (e.g., consumption patterns for video games, advertising, and films, and number of museums, theatres, libraries, and publishers). But such indicators are usually irregularly produced and scattered across a range of sources (Oxford Economics, 2014).

⁶ In an effort directed to compare innovation performance and potential of worldwide countries, the Global Innovation Index (2017) includes a “creative outputs” pillar built on several indicators measuring intangible assets, creative goods and services, and online creativity.

Moreover, other factors—less technical in nature but equally important—impede proper assessment based on these indicators. First, budget constraints and unstable political commitment often prevent consistent accumulation of statistics over time. Second, there is often strong opposition to measurement by part of the cultural community, which dislikes the idea of a quantitative economic analysis of culture. Finally, the absence of a common definition for the creative economy undermines the accuracy of international comparisons.⁷

4.2. Sources of Information and Limitations

Measures of contribution to GDP reported by national public agencies and international organizations such as the United Nations Conference on Trade and Development (UNCTAD), the World Intellectual Property Organization (WIPO), and the United Nations Educational, Scientific and Cultural Organization (UNESCO) come mainly from National Accounts Systems (NAS). The main sources of information for employment estimates are labor force and household surveys, and population censuses. The most comprehensive data for trade flows is provided by UNCTAD based on national data reported by the central statistics offices of different countries.⁸ These data come from balance of payment surveys or international transaction reporting systems.

Regarding GDP estimates, it is worth pointing out that exercises that rely on NAS are especially difficult. In fact, creative activities generate mostly intangible value and consequently there is a serious risk of under-estimation. For this reason, several countries have started to develop Satellite Accounts of Culture (SAC), which allow for better accounting of the creative economy.⁹ Satellite accounts are simply an expanded and more detailed version of the NAS in a particular sector; therefore, they are conceptually and statically consistent with the figures that are reported by the NAS. The concept, which was developed in the 1970s as a statistical tool to complement the NAS (thus the name satellite), uses the United Nation's System of National Accounts as a frame of reference (Oxford Economics, 2014). SAC provide key information for policymakers by estimating the economic contribution of the cultural sector, identifying changes over time and over subsectors, and allowing performance to be compared with other economic sectors.

⁷ For example, architecture is included in the statistics of the United Kingdom (which uses “creative industries” in its terminology), Germany (cultural and creative industries), and France (cultural sector). Spain uses the term culture industries and does not include architecture. Design, advertising, and fashion are only considered creative in the United Kingdom and Germany, not in Spain or France. The opposite happens with libraries and museums and cultural heritage in general. See Oxford Economics (2014) for more detail about sectors included in creative industries and terminology.

⁸ See also UNCTAD's creative goods and services databank, which provides detailed information on a country-by-country basis and analyses of bi-lateral creative trade flows.

⁹ The first country to develop a SAC was Colombia in 2002, consolidating the first SAC in the world in the year 2007. Finland and Spain followed in 2008, and Chile in 2009. Then came Argentina (2010), Uruguay (2012), Costa Rica (2013), the United States (2013), Mexico (2014), Australia (2014), and the Czech Republic (2015). In May 2016, the Dominican Republic published the results of its first measuring exercise. Bolivia, Ecuador, and Peru are currently in the initial stages of the process (Oxford Economics, 2014).

Employment figures also have advantages and shortcomings. Labor force surveys are specifically designed to generate employment figures, rely on accepted international criteria, are carried out frequently and by a large group of countries, and have disaggregated coding systems. Nevertheless, there are important limitations in this source of information. In many cases, labor force surveys do not represent the entire labor population (sampling problems) since people who are self-employed and workers in the informal sector are often not covered.¹⁰

Also there are limitations regarding the employment status definition and delimitation of the labor market (Bille, 2012; Frey and Pommerehne, 1989; Higgs, Cunningham, and Bakhshi, 2008). Censuses do not have sampling problems because they are applied to the entire population, but different countries use different methodologies, they are not carried out very frequently (usually every ten years), and they tend to define employment in terms of main occupation, which is at odds with the reality that creative workers often have many occupations or sources of income, some in non-creative sectors (Benhamou, 2003; Throsby, 2010; Towse, 2010).

For trade data, the intangible value of creative goods and services makes measurement difficult,¹¹ particularly in the case of small volumes. In fact, some countries collect data on the total value of exports and imports of creative goods and services, but this data is not disaggregated by subsector. Moreover, the different sources of national trade data (balance of payments or international transactions reporting systems) affect the reliability of comparisons.

Over the past few years, web data has emerged as a new important source of information.¹² Even though such data is severely limited in terms of reliability and coverage because it only gets information from those that use the internet, it can be very rich in terms of information (e.g., it is highly disaggregated in time and geographically). Further, collection costs are relatively low. These features are very convenient for a sector such as the creative economy, where official information is still very limited. For instance, Mateos-Garcia and Bakhshi (2016) used data from Meet-up, an online events platform that congregates people with a common interest (e.g., photography, cooking, or running), to explore the networking of creative activities in different cities of the United Kingdom.

¹⁰ UNESCO (2013) recognizes that the informality of the creative economy is particularly important in developing countries, specifically for creative workers such as musicians, artisans, performers, craftspeople, and designers.

¹¹ Nurse and Nicholls (2011) explain that “[s]ome creative services flows are...not registered in trade accounting reports because payment is difficult to capture and the criteria guiding their inclusion in the balance of payment vary across countries. For instance, some countries include data on royalties and license fees while others do not. The same happens with other services such as advertising, market research, public opinion polls, cultural and recreational services, audiovisual, and architectural, engineering, and other technical consultancies.”

¹² For example, social networks like Facebook and Twitter have information about the people interested in creative activities, such as the most popular play in the city, the age of the people interested in the play, where they come from, etc. Google Trends shows how often a term is searched using Google. This simple and powerful information can show how the interests of people in creative activities evolve over time or how they differ across cities.

4.3. A Further Challenge: Measuring Non-market Value

The previous sections show that traditional ways of assessing the economic relevance of the creative economy rely on indicators that measure the market value of creative goods and services. However, there is an important subsector of the creative economy—especially cultural goods and services—for which the total economic value is not well reflected in prices or measures of economic activity¹³ simply because many of those goods and/or some of their attributes are not traded in (well-defined) markets.¹⁴ Typical cases of activities and institutions that fall into this category are the performing arts, cultural and natural heritage, public libraries and museums, cultural festivals, and even the film industry, as well as other cultural goods related to economic activities such as tourism. For such goods and services, conventional indicators fail to reflect their real economic value, making it necessary to find alternative methods.

The Contingent Valuation Method uses surveys to get information about the value that people place on some goods and services.¹⁵ Although this method allows the value of non-market goods to be measured, it still has flaws. In particular, given the hypothetical nature of the exercise, the reported valuation might differ (sometimes significantly) from the real value, producing potential bias in the valuation.

Other methods commonly applied in the cultural sector (particularly culture and natural heritage) are the Hedonic Price Method and the Travel Cost Method. Both are non-survey, indirect willingness to pay methods. To derive a measure of the economic value of a particular good or service, they rely on market information about a related good or service (Seaman, 2006).

The Hedonic Price Method assumes that the market price of a particular good or service is a weighted average (linear combination) of the individual prices of its attributes. The Travel Cost Method presumes that the time and travel cost expenditures that people incur to visit a site can represent the value of a cultural asset. The Travel Cost Method has been widely employed to value recreational sites, even if its explanatory power is limited to the use value (i.e., it presumes that non-visitors do not place a value on the site).

¹³ The value of these goods is not determined by the market, but by society (Cuccia, 2011).

¹⁴ Total economic value could be defined as the monetary expression of a change in individual (and thus social) well-being (Pearce and Turner, 1990). When observable (market) data are available, the economic value of a particular good or service can be measured using traditional valuation methods (Seaman, 2006). The problem occurs when the value is not observable (in the absence of a market for that good or service) and/or when what one wishes to capture are the various non-use values, which by their nature are not observable. The specific components of non-use value have been identified as existence, option, altruism, and bequest (Throsby, 2006, 2010).

¹⁵ Originally developed in the field of environmental economics, increasingly, the Contingent Valuation Method has been applied to cultural resources. Good examples include Mazzanti (2002), who valued the Galleria Borghese in Rome; Bille (1997), who applied the method to the Royal Theatre of Copenhagen; and Maddison and Foster (2003), who valued the congestion at the British Museum. See Noonan (2003) for a comprehensive review of applications in sports, culture, and the environment. In Latin America, Beltrán and Rojas (1996) conducted a Contingent Valuation Method analysis at three archaeological sites in Mexico and in seven Mexican cities and explored revenue-maximizing pricing strategies. Roche (1998) applied the method to analyzing the total economic value of the Colon Theatre in Buenos Aires, Argentina. Hett and Mourato (2000) and Mourato et al. (2004) interviewed visitors to the Machu Pichu historic sanctuary in Peru. More recently Báez and Herrero (2012) applied this method to restoration of the urban cultural heritage of Valdivia in Chile and Báez et al. (2016) to Chile's National Network of Public Libraries.

Finally, there is the Economic Impact Method, which measures the proportion of economic activity in a particular well-defined territory (influence area) that can be accrued to a particular event or organization. It is useful to illustrate inter-sectorial dynamics at the local or regional level. This method has proven very useful for estimating the impact of cultural institutions and events on the local economies and can be implemented whenever there is reliable data describing the structure of the affected economy (influence area).¹⁶

4.4. The Creative Economy in Latin America

Since 2002, the WIPO has released information on the economic relevance of the creative economy, defined as copyright industries.¹⁷ Data collected from 2002 to 2013 show that the creative sector makes a significant overall contribution to GDP, with a world average of 5.20 percent. It is interesting to notice that countries that have experienced rapid economic growth typically have an above-average share of GDP attributed to copyright industries. However, the estimates of the contribution of the creative economy vary depending on how it is defined. In fact, other exercises based on more restrictive definitions show figures ranging from 1.5 percent to 4.8 percent (UNESCO, 2013),¹⁸ which is consistent with the most recent estimation made by Ernst & Young (2015) of 3.0 percent for 2013.

In LAC, recent estimates show that creative industries generate revenues of US\$124 billion, or approximately 2.2 percent of regional GDP (Ernst & Young, 2015). While in some countries the sector appears to still represent only a small proportion of economic activity, the sector's importance is increasing, achieving double digit per annum growth rates in many subsectors over the 2002–11 period (Oxford Economics, 2014).

In general, the contribution of the creative economy to national employment is slightly higher than its contribution to GDP, with a global average of 5.3 percent (WIPO, 2014), and with three-quarters of the countries between 4 percent and 7 percent. A strong positive correlation between contribution to GDP and employment is observed. Most countries with an above-average contribution from creative industries to GDP also exhibit above-average contributions to employment.¹⁹ In LAC, the creative sector generates around 1.9 million jobs (Ernst & Young, 2015), positioning

¹⁶ This information includes input–output matrices, occupation figures, and activity flows by sector. Again, the level of detail of the data as well as its periodicity are of critical importance.

¹⁷ The WIPO methodology distinguishes between four different groups of copyright industries based on the level of dependence on copyright material: core, interdependent, partial, and non-dedicated support industries.

¹⁸ GDP figures from SAC reports information for cultural GDP as a percentage of the whole economy in some countries. These data must be interpreted cautiously because definitions guiding the estimation exercises differ and different countries report information for different years. For example, Spain's SAC includes a different set of subsectors than other countries, making comparisons difficult. Therefore, although in 2007, Spain's cultural sector is recorded in its SAC as 2.9 percent of GDP, this is not directly comparable with the 1.8 percent recorded in Colombia.

¹⁹ Other estimates of employment contribution that follow alternative definitions of the creative economy include the 2013 UNESCO *Global Survey of Cultural Employment*.

creative industries as important providers of employment and showing relatively high labor intensity. In Mexico, for example, approximately 11 percent of total employment is considered to be due to copyright industries (WIPO, 2014), which have a higher percentage of youth employment than the rest of the economy and are forecast to grow.²⁰

Finally, there are interesting figures regarding international trade flows of creative goods. Figures for 2003–12 indicate that the creative economy on average represented 2.0 percent of total exports of goods in LAC countries. The main exporting creative sector was design activities (architecture, fashion, glassware, interior, jewelry, and toys), representing 61.2 percent of the region’s creative exports, followed by publishing (books, newspapers, and other printed material), representing 13.4 percent. The new media sector (recorded media and video games) experienced the highest growth rate, increasing from 0.7 percent in 2003 to 7.8 percent in 2012.²¹

²⁰ Detailed results by country indicate that the creative economy explains 3.0 percent of national employment in Argentina, 3.1 percent in Panama, 4.5 percent in Peru, 5.8 percent in Colombia, and 11.0 percent in Mexico (Oxford Economics, 2014).

²¹ Calculations based on UNCTAD figures accessed from http://unctadstat.unctad.org/wds/ReportFolders/reportFolders.aspx?IF_ActivePath=P,10&cs_ChoosenLang=en.

5. The Creative Ecosystem

A novel approach to characterizing the creative economy is through the lens of a creative ecosystem. An ecosystem is a set of different and interrelated actors that has certain properties that cannot be ascribed to and are not the result of a particular participant in the system. By adapting the concept of a national innovation system,²² it is possible to define a creative ecosystem as the set of entities and rules that govern the production, diffusion, and consumption of creative goods and services. The analogy between a creative ecosystem and a national innovation system appears valid as long as creative output is usually the result of the interaction of multiple, often very heterogeneous, actors (Bakhshi, Hargreaves, and Mateos-Garcia, 2013; Green, Miles, and Rutter, 2007).

The concept of creative ecosystem emphasizes not only the importance of the links between the public and the private sector, but also those with local communities, end-users, and the fundamental role of educational institutions. It also helps to understand diversity, interdependence, and collaboration between different actors, and this understanding in turn can be used to better inform development strategies for creative industries (Bakalli, 2014).

In this context, despite the increased reliance of business models on internet and other ICTs, locational proximity still appears to be important for collaboration and co-creation. In fact, the creative process is stimulated by the closeness of peers, providers, and consumers, as it often relies on tacit knowledge (Work Foundation, 2007) that is difficult to transmit from a distance.

Therefore, the concepts of creative clusters (Flew, 2002; Kelly and O'Hagan, 2007) and creative cities (Florida, 2002), which are subsystems of a creative ecosystem, have gained importance worldwide. Creative clusters include creative firms that take advantage of geographic concentration to enhance collaboration that benefits all members. This collective action increases the innovation and productivity of firms as long as they can access better inputs in the form of labor, knowledge, technologies, and new opportunities.²³ In particular, creative cities are characterized by a high density of educated professionals with very diverse backgrounds and preferences that are attracted to the open and tolerant urban way of life and that are usually employed in creative occupations. Such diversity (Landry and Bianchini, 1995; Markusen and King, 2003) is expected to favor business formation in the creative sector and in related sectors (Lazzeretti, 2012; Santagata, 2006).

²² A national innovation system is defined as the set of economic agents and institutions (e.g., government, universities, research units, and the private sector) whose interaction determines the performance of a society in terms of innovation outputs. Such interaction is key to generating, diffusing, and using knowledge in the production system and society, determining the long-run economic development of a country (Freeman, 1989; Lundvall, 1985, 1992; Nelson, 1993).

²³ Sometimes clusters develop spontaneously in response to locational advantages. In other cases, coordination problems and other market failures make public intervention necessary (Bille and Schulze, 2006; Santagata, 2006).

The creative ecosystem combines the private sector (individual and corporate agents), academia, government (at the local, regional, and national levels), organized civil society, and consumers. All of these agents engage in synergies around creative projects and perform different functions in the process of spreading culture and creativity into the production system and society as a whole (Arnold et al., 2014; Hernández, 2014; OECD, 2014). Depending on their role, it is possible to classify agents as (i) supply-side (those that produce creative goods and services), (ii) demand-side (either final consumers or users of creative inputs in their production process), (iii) institutions dedicated to human capital formation and knowledge production, and (iv) governance institutions that regulate and promote relations between actors.

Both for-profit and non-profit producers operate on the supply side. On one hand, non-profit organizations²⁴ are generally prevalent in traditional and artistic activities, where external funding is required to cover high costs.²⁵ In this case, financing is usually provided by public grants and private donations.

On the other hand, for-profit entrepreneurs and enterprises generally work in the creative and cultural sectors where markets are well defined in that there is observable demand reflected in the willingness to pay for creative goods and services. However, high fixed and sunk costs mean there are only a few producers (individuals or corporations) that are financially successful, while the majority have very low earnings and market share. This situation, called the *superstar* phenomenon (Adler, 2006; Rosen, 1981), has been pervasive not only in the arts but also in more commercial creative industries, such as video games (Bakhshi, Hargreaves, and Mateos-Garcia, 2013).

These large companies, generally called *majors*, have global reach and financial capacity and usually represent the most visible and lucrative artists and franchises. Smaller companies and individuals usually provide services to or support the majors, representing or developing less known and/or alternative artists and franchises (also known as *indies*), or intermediating between creative and non-creative businesses. Individuals rarely create formal companies and often act as freelancers, in many cases working informally, and thus are not registered in official statistics.²⁶ In this scenario, collective interest organizations, such as chambers of commerce (for formal creative firms) and guilds or other formal and semi-formal mid- and long-term alliances²⁷ (for individual artists) play a particularly important role in the ecosystem by coordinating the interests of many small agents and centralizing the interaction with other institutions (Heilbrun and Gray, 2001).

²⁴ In general, non-profit organizations are represented by cultural foundations, non-governmental organizations, or groups organized around museums, theaters, and historical sites, among others.

²⁵ High costs can be related to Baumol Cost Disease, which occurs when an economic sector experiences an increase in wages not related to improvements in productivity, but in response to increased wages in the rest of the economy (Baumol and Bowen, 1966). Heilbrun and Gray (2001) noted that it only takes four musicians to perform a Beethoven string quartet today, as it did back in 1800.

²⁶ Some such individuals have been depicted as deriving utility from their artistic occupation. Frey (2007) refers to this as intrinsic motivation. Caves (2000) calls it the art-for-art's-sake principle. Throsby (1994) developed a theoretical model stressing this idea. See Bille (2012) for empirical evidence.

²⁷ These alliances are sometimes called *collectives*, other times *troupes* or *studios*.

This market structure can be very detrimental to societal wellbeing. In fact, a variety of creative content (and therefore cultural and creative diversity) is at risk when many niche markets are not profitable.²⁸ However, digital technologies have allowed producers to use new collaborative business models that reduce fixed costs by sharing them. These models are based on the open source principle, which relies on the free exchange of knowledge and information among producers as a basis for the joint development of or improvement in a product. Having emerged in the software sector, open source is now expanding to other industries and it can be very relevant for creative industries.

On the demand side, consumers validate creative content and signal value through consumption and appropriation (Buitrago and Duque, 2013). The vast majority of consumers are individuals making decisions on the basis of personal preferences.²⁹ Others are companies using creativity as intermediate supply, such as mixing the sound track for a movie, editing or translating a magazine, or designing the sets for a theatrical production.³⁰ Also, intermediate creative inputs are becoming increasingly important in generating value in traditional industries. In these cases, enterprises can decide whether to buy the creative inputs in the market or to directly hire people to produce these inputs.

So far, consumers and producers have been clearly distinguished, but the digital revolution has allowed so-called prosumers—simultaneously producer and consumer—to emerge. These new actors contribute significantly to increase the value of cultural and creative goods and services.³¹ The current transformation of the recorded music culture into a networked on-demand culture is a good example of opportunities to develop co-created value, where new digital networked media allow more artists and consumers to act as producers, distributors, publishers, critics, etc. (Winter, 2012). New technologies constantly change the way producers and consumers behave and interact, generating value through social networks in production and consumption.³²

²⁸ Interestingly, new technologies have improved this situation in many sectors. For example, platforms selling books online offer more variety than physical bookstore chains (see Peltier and Moreau, 2012).

²⁹ Although buying decisions in most sectors are influenced by social and peer group pressures, in the cultural and creative industries, these effects are more marked because of the inherently social dimension of creative offerings. Examples are word-of-mouth and specialized reviews (Caves, 2000).

³⁰ An example of a simple creative process chain is creating an original sculpture, drawing, or photograph that is then sold directly by the artist to the final consumer. In many cases, however, the creative process is more complex and consists of many stages, from production through manufacturing and dissemination to consumption. An example is an original piece of music being created and then distributed to differing points of demand, either intermediate or final. The process may start with composing a music score/song, which is then orchestrated. Then it is performed (by musicians) and recorded. A CD (or some related product) is then designed, manufactured, and packaged. The CD is distributed, marketed, and licensed to other platforms (e.g., TV, films, games, internet platforms, or music compilation). At the end of the chain, there are the consumers.

³¹ Some examples of prosuming are Facebook, Wikipedia, and Amazon, where people buy and contribute with product reviews (Ritzer, 2014).

³² According to this idea, markets and social information networks are important environments where consumers make their choices and engage in creating symbolic and economic value (Caves, 2000; Potts and Cunningham, 2008; Potts, Cunningham, and Hartley, 2008).

In fact, social networks allow creative workers and entrepreneurs to engage directly with consumers, reducing barriers of access and lowering intermediate costs. Moreover, this interaction creates signals about preferences and affinities that go beyond the creative content, generating a feedback loop with spillovers across a wide range of topics, from climate change to humanitarian crises to technological adoption (Potts, Cunningham, and Hartley, 2008).

Another important component of the creative ecosystem is represented by the institutions engaged in human capital formation and knowledge production, such as universities and research centers. On one hand, they provide individuals with relevant skills and competencies by offering formal comprehensive education programs or more specific training aimed at expanding or updating the abilities of creative workers. On the other hand, they are a continuous source of new ideas and solutions, nurturing innovation across all the segments of the creative economy.

As in any other productive system, governance is crucial. The public sector provides the system with stability and legitimacy by leveling the playing field and establishing the rules of the game (Buitrago and Duque, 2013). Government can also contribute to solving coordination failures among agents and removing obstacles to developing the ecosystem.

Given the heterogeneity of the actors in a creative ecosystem, there are many public institutions and agencies involved. Centrally, they include Ministries of Culture (or their equivalent, e.g., National Councils for the Arts) as well as several others, such as the Ministries of Economy, Production, Science and Technology, Finance, Education, Tourism, and International Affairs.³³ Moreover, the importance of proximity implies a key role for subnational governments, regionally and locally. The multiplicity of relevant public institutions poses a serious challenge in terms of coordination horizontally and vertically.³⁴

An area where public action is particularly important is regulating IPRs.³⁵ The implicit assumption is that, in order to stimulate creativity, society must grant creative producers a temporary monopoly over their creations because the social cost of this monopoly is greatly compensated by the social benefit of counting on new creative products and services. The debate on the best form of protection required to maximize the social benefit is getting more and more relevant given that new technologies have greatly facilitated reproducing creative content.

Digitalization and exchange can be done practically at zero cost, thus increasing the risk of illegal reproduction (Throsby, 2010).³⁶ Clearly, this poses challenges to the

³³ See Madden (2009) for details of the different institutional frameworks in the creative sector.

³⁴ See Throsby (2010), particularly Sections 2, 3, and 4, for more details. An application for Chile can be found in Benavente and Larraín (2016).

³⁵ Creativity and intellectual property appear to be two sides of the same coin. Potts and Cunningham (2008) noted that “creativity is an input and content or intellectual property is the output.”

³⁶ The effects of digitalization are particularly prevalent in the music industry, new art forms, museum images, broadcasting, the press and journalism, publishing, and film production (see Towse [2006] and references therein).

IPR system, both at national and international³⁷ levels, where IPRs are usually managed by specialized independent bodies.

There are five main types of IPRs: patents, trademarks, designs, geographical indications, and copyrights.³⁸ Patents protect inventions. Trademarks are distinctive signs that identify certain goods or services and protect firms from having others use their name either as a trade name or as a trade or service mark.³⁹ Designs intend to protect the appearance (the ornamental or aesthetic aspects) of a creative product. A geographical indication is a sign used on goods that have a specific geographical origin and possess qualities or a reputation related to that place. Copyright protects the expression of creative ideas fixed or expressed in the form of, for instance, literary works, plays, newspaper articles, computer programs, databases, films, music, paintings, photographs, sculptures, architecture, advertisements, maps, and technical drawings (Throsby, 2010). Most creative industries—to a greater or lesser extent—use copyright in their business models (Work Foundation, 2007).

In order to collect royalties and monitor the use of their works, copyright holders rely on collective management arrangements because it would be prohibitively expensive to do individually. Therefore, a key role in the copyright system is played by collecting societies⁴⁰ such as non-profit organizations that monitor the use of copyrighted works and their commercialization,⁴¹ and manage collection and distribution of revenue to members (rights holders).

In conclusion, in line with the latest advancements in the entrepreneurship literature, it is not possible to understand the promotion of new firms, sectors, or regions without a systemic approach. This is particularly relevant for the creative economy, where most products are intangible, rooted in the territory, and the result of the constant interaction among different actors of the ecosystem. In fact, creative production requires a permanent evolutionary process where all agents must be involved.

³⁷ The WIPO is leading an international effort to clarify norms aimed at preventing unauthorized access to and use of creative works on the internet.

³⁸ For many creative goods and services, usually more than one type of IPR is involved (see Foray, 2004; Hölzl, 2005; Towse, 2008).

³⁹ This right of exclusive exploitation is theoretically indefinite, as long as it remains in use.

⁴⁰ In some countries, there are many collecting societies while in others there is only one organization, licensed by the state, administering copyright. In LAC, there are collective societies in different sectors, although they tend to be monopolies (natural monopolies, mainly in response to the limited size of the markets in these countries). See Towse (2008) for a more detailed discussion of regulating collecting societies.

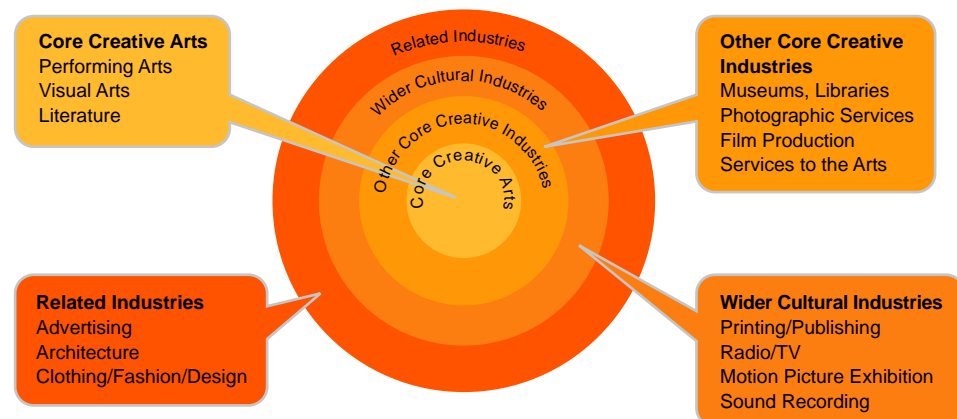
⁴¹ Many types of works protected under the laws of copyright and related rights require mass distribution, communication, and financial investment for successful dissemination. Hence, creators often license, assign, or sell these rights outright or in part. Or, in return for compensation, they may transfer rights to an agent or company that is better able to develop and market the works. Only the author's moral right in the work may not be sold or transferred. (Caves, 2000).



6. The Rationale for Public Intervention

Traditionally, the main argument justifying government intervention in the creative economy—particularly the cultural industry—has been that the goods and services produced in this sector are valued both by producers and consumers for social reasons that exceed their economic valuation in terms of their contribution to a society’s cultural identity: the *cultural value* of a good or service as opposed to its *economic value*. For example, some cultural organizations, such as museums, libraries, and theaters, fulfill an educational role in the form of general knowledge and identity (Frey, 2000). Hence making such cultural organizations and events accessible to a broad range of the population is a clear policy objective. Various theoretical frameworks have been proposed to provide a systematic understanding of the complex relationship between these two concepts. Considering the degree of cultural value of a good or service relative to its economic value, Throsby (2008) defined a concentric circles model, where at the center are core industries whose cultural content is judged to be relatively high compared to their economic value, with layers extending outward as cultural content falls relative to economic value (Figure 2). Therefore, if an industry is close to the center, its cultural value is not mirrored by its economic value and it would need government intervention to operate. In this case, the state usually guarantees the provision of goods and services, either directly (e.g., through foundations and companies) or indirectly—where delegation is possible—by regulating and financially supporting private (non-profit) institutions that provide these goods and services at a discount or free of charge.

Figure 2. Throsby’s Concentric Circles Model



Source: Based on Throsby (2008).

Note: Referring back to Figure 1, **Traditional and Artistic Activities** are mainly in the inner circle (“Core Creative Arts”). Some activities in the **Creative Industry**, such as photographic and audiovisual, belong to the “Other Core Creative Industries.” The rest of the Creative Industries are included in what is called the “Wider Cultural Industries.” Finally, the **Activities of Creative Support** are mainly in the outer circle as “Related Industries.”

However, there has been a progressive shifting in the literature toward using economic arguments to justify public action in creative activities based on the specific economic features of goods and services of the creative economy. In fact, from an economic perspective, the activities included in the creative economy share a set of properties that make them deeply different from other economic activities and that prevent markets from producing socially efficient outcomes.

First, most goods and services resulting from these activities present some degree of non-rivalry⁴² and non-excludability,⁴³ which are characteristics that define public goods. These features may generate market failures that are prevalent for many forms of cultural goods, such as the arts and cultural heritage. For example, it is not possible to exclude listeners from enjoying radio broadcasting (if they have a radio) and listening to a program does not exclude others from listening. This is even more true in the digital era. For example, listening to a song on a vinyl record was in some way rival since the number of records produced was limited. Now, however, digital files are easily reproduced and potentially infinite listeners can play the same music at the same time.⁴⁴ A direct consequence of the non-excludable nature of the outputs of creative activities is that the person or firm producing the good or service cannot fully appropriate its returns, limiting the incentive to the private sector to provide such goods. This appropriability problem is present either because the consumer can enjoy the good without paying for it or because other producers can easily imitate the goods' features without investing in the creative process.

Second, creative activities are very likely to produce positive externalities in the form of knowledge, product, and network spillovers (Cunningham and Potts, 2015). In terms of knowledge, cultural and creative goods often embody intangible content in terms of ideas, concepts, or information that can inspire, be developed, or be copied by others (without compensating the original idea), facilitating innovation in an economy.⁴⁵ Product spillovers happen as a creative industry fosters growth in other sectors through its role in production processes (Tafel-Viia et al., 2011). This can happen mainly in two ways. On one hand, a firm's development of a product can create or expand the market for complementary products. For example, blockbuster movies generate ancillary markets for merchandising goods. On the other hand, creative industries often demand cutting-edge technologies, especially ICTs, generating new markets (i.e., over-the-top services such as YouTube and Netflix) or deepening existing ones that require faster and unlimited mobile internet access options from traditional carriers.

⁴² A good is said to be non-rival if consumption by one consumer does not prevent or affect consumption by other consumers.

⁴³ Non-excludability refers to the inability to exclude a person from consuming a good or service.

⁴⁴ However, there are some exceptions. For example, in fashion design, exclusive pieces are only accessible to those who can afford them; though counterfeiting undesirably circumvents this limitation.

⁴⁵ This is typically the case for information goods, whose economic value depends on the information they convey.

Network spillovers are related to the positive effects of a particular activity on other actors sharing the same location. For example, cultural and creative goods, such as heritage sites or public architecture, benefit the inhabitants by attracting highly educated professionals and foreign investment, as well as tourism, which benefits the entire area. According to Florida (2002), a “creative class” composed of intellectuals, artists, researchers, and other creative professionals are now key to urban economic development (see also Wojan and Lambert, 2007).

Third, the cost structure of many creative activities can be a hindrance. For instance, films, publishing, music, and media industries produce the first output (or the master copy) at a generally high cost, whereas the marginal costs of the following copies is low (in the case of digital outputs, it approaches zero) and sunk costs tend to be high (Caves, 2000). As mentioned, this economic structure generates barriers to entry and allows incumbents to take advantage of their position. This may result in a high level of market concentration, which penalizes consumers in terms of higher prices, lower quality, and less variety.

In other cases, such as broadcasting, infrastructure is required to operate the creative activities, which involves high sunk costs and thus turns them into natural monopolies (Heilbrun and Gray, 2001; Towse, 2010).⁴⁶ Another argument indicates that many creative endeavors, mostly in the traditional arts, are prone to Baumol Cost Disease, making them uncompetitive over time against substitutes (e.g., opera versus rock and roll concerts) or outright alternatives (e.g., ballet versus sports). While it could appear as an example of Schumpeter’s creative destruction process—less productive enterprises are replaced by newer, more efficient enterprises—the dynamics of creative industries are different. In fact, the competitiveness of more modern, popular, and productive industries often depends on the concurrent existence of traditional industries—potentially affected by the Baumol Cost Disease—that provide the necessary skill sets, experimentation mentality, and technical development. Clear examples include visual arts aesthetics for video game designs or theatre acting training for television and film productions. This is true not only for cultural goods, but also for more commercially oriented (for profit) creative activities and may justify either direct or indirect fiscal support.

Fourth, activity based on human creativity is by definition uncertain in many aspects. The creativity process depends on talent, inspiration, past experience, and exposure to other creative works, among other factors. But none of these factors determine the time this process will take. Furthermore, the value of a creative product will vary substantially depending on consumer reaction, which is very difficult to predict.⁴⁷ This implies that the risks associated with creative activities are very high and hard to determine before the process starts. If we add to this the fact that new creative businesses usually need small sums of money to start (creating an additional cost to

⁴⁶ For an empirical analysis highlighting the problems posed by the high fixed and sunk costs in the film industry, see Vogel (2011).

⁴⁷ Caves (2000) refers to this uncertainty as the “nobody knows” principle.

banks), that the creative goods and processes are generally intangible and/or intellectual (mainly in the form of knowledge and human capital), and that they are often tailor-made to customers (making them difficult or even impossible to store), it is easy to understand why access to traditional financing is so difficult in these industries.⁴⁸ On one hand, it is difficult for financial institutions to value an intangible asset and monitor changes in their value. On the other hand, intangible goods are easier to copy or reproduce and therefore the appropriability of the investment return could be compromised. All this makes investments in creative industries risky (Arnold et al., 2014; Skantze, 2014), especially for new firms, which are usually the most innovative.

Various information and coordination failures affect the creative economy. For example, demand for skills in these industries changes very quickly, generating a constant mismatch between knowledge and training provided through formal education and that needed in the market (Arnold et al., 2014). Also, creative industries often ignore demand from other sectors and, at the same time, traditional industries are not aware of the potential gains available from incorporating creative inputs into their production process.

From another perspective, information asymmetries can also affect the creative and cultural industry through the demand side. In fact, culture has been considered a “merit good” (Heilbrun and Gray, 2001), meaning that people are not completely aware of the benefits that these goods convey to both consumers and society overall. It could be that people do not have the information or the education needed to develop the “taste for the arts” and therefore do not value them appropriately (Throsby, 1994). Thus, it is difficult to get individuals to consume creative goods, particularly emerging forms of art performed by infant cultural enterprises. In this case, public intervention is needed to make consumers aware of the true value of cultural goods.

Moreover, even if they were fully aware of the benefits provided by access to cultural activities, most households cannot afford to participate. In fact, low and medium income families, with strong budget constraints, are forced to prioritize consuming essential goods and basic services over other choices (Heilbrun and Gray, 2001). Therefore, given that access to cultural goods is considered important for the wellbeing of the entire population but that it tends to be expensive, some form of public support targeted specifically to low and middle income families is the only possibility of guaranteeing that a larger part of the population has the opportunity to consume cultural activities.

⁴⁸ Notice that all these points correspond to access to traditional financial institutions. Alternative funding methods have gained popularity, such as crowdfunding and philanthropic donations. This is particularly important for the creative industry. According to Boeuf, Darveau, and Legoux (2014), the largest amounts raised on crowdfunding platforms correspond to projects related to music, film, and video games.

7. Public Policies in the Creative Economy

The above described market and coordination failures constitute a compelling rationale for public intervention in various aspects of the creative economy. Many countries have implemented a large array of public policies and programs in order to support the production and consumption of cultural and creative products (Arnold et al., 2014; Bakhshi and Windsor, 2015; Ginsburgh, 2003; Seaman, 2006; Throsby, 2010; Traub, 2005).

Programs have varied a lot depending on the justification for public intervention and include direct and indirect financial support provided to the supply and demand of goods and services; human capital formation (through formal education systems and training programs); regulatory infrastructure (most notably copyright law and oversight of print and media industries, including TV quotas); and mechanisms to improve circulation of information, technology, and market development.

Many policies are not tailor-made for creative industries but adapted from more traditional policy contexts. Considered individually, none of the policies are expected to be sufficient to foster development of creative industries. A comprehensive policy set is necessary to promote development of a creative ecosystem.

Crespi et al. (2014) provide a useful framework to conceptualize policy interventions. In particular, they emphasize two dimensions of policies: scope and type. First, the scope of the intervention can be intended for the economy as a whole, without bias for a particular productive sector (horizontal policies) or it can focus on a particular sector or activity, such as value chains or clusters (vertical policies). Second, the intervention can take the form of public inputs or market intervention to affect incentives for private agents, especially through prices. Table 1 gives examples of how this framework can be applied, through both horizontal and vertical policies in the creative economy.⁴⁹

⁴⁹ An application in the context of public policies aimed at promoting a knowledge-based economy can be found in Crespi et al. (2014).

Table 1. Public Policies in the Creative Economy

	Horizontal	Vertical
Public Input	<ul style="list-style-type: none"> - Human capital formation and training programs in STEAM* - Regulatory framework (e.g., IPR, antitrust law, contract law) - Cultural infrastructure and heritage - Festivals, national or regional events - Accelerators and incubators - Research infrastructure - Entrepreneurial education 	<ul style="list-style-type: none"> - Sector-specific training programs - Creative industries research centers (e.g., marketing, design, audiovisual) - Information and marketing intelligence services for creative sectors - Awards and contests
Market Intervention	<ul style="list-style-type: none"> - Grants and subsidies to cultural and creative activities - Fiscal incentives - Financial measures (e.g., guarantees for intangible values and technology investment) - Public financing of seed, angel, and venture capital, directly or through private venture capital funds 	<ul style="list-style-type: none"> - Grants and subsidies to a targeted sector - Innovation vouchers - Tax incentives for a particular sector - Public procurement - Demand incentives (e.g., cultural and creative vouchers)

Source: Authors' compilation based on Crespi et al. (2014).

* Science, Technology, Engineering, Arts, and Math.

The idea of this taxonomy is not to list and classify all possible policy instruments but to raise awareness of the benefits and costs associated with the four possible cases. For example, the first quadrant provides examples of policies that, if they do not work, are less harmful, or those where state failures (a concept that will be discussed in the next section) are less severe. On the contrary, the forth quadrant (where, among others, all sectorial tax exemptions lie) includes the more controversial interventions since, despite their economic potential, the risks of rent-seeking behavior and political capture are higher.

7.1. Supply-Side Policies

The public good nature of cultural and creative goods and services, externalities and network effects, as well as the uncertainty and cost structure related to high fixed and sunk costs all prevent private finance from providing adequate funding for cultural and creative activities. In this situation, the public sector is called to facilitate and complement private financing,⁵⁰ through direct and/or indirect support instruments. However, in order to avoid crowding out investments that the beneficiary would make even in the absence of public support, it is necessary to understand the specific reasons for the market failure and design the intervention such that those issues are resolved (Borgonovi and O'Hare, 2004; Brooks, 2006; Netzer, 2006; Schuster, 2006).

Direct support can take the form of grants, subsidies, or other kinds of financial assistance to creative for-profit or not-for-profit individuals and organizations (Throsby, 2010). This support is usually allocated either by public officers or by committees of experts responsible for deciding what and who receives public support (peer-review principle). There are many examples of different versions of this type of intervention, which has traditionally been a key instrument of cultural policy. In general, they can be classified as sector-specific funds, such as the *Fondos Culturales* program in Chile, which offers competitive grants in different cultural sectors (e.g., visual arts, crafting, design, photography, and theater) or cross-sectorial funds, such as the *Fondo Argentino de Desarrollo Cultural y Creativo* program in Argentina, which co-finances projects that aim to improve the marketing and distribution of cultural and creative products.

As this financing constraint is particularly severe for new entrepreneurs, it is particularly important to support creative startups through dedicated entrepreneurship policy instruments. For example, the Brazilian Development Bank has been a direct lender to the audiovisual, music, media, and video game industries since 2006. Moreover, this bank has also set up an investment fund for distribution (UNESCO, 2013). The United Kingdom has encouraged private equity investment in two principal ways: (i) through tax schemes allowing investors to claim income and capital tax relief on their equity investments on qualifying companies, and (ii) through publicly backed venture capital funds operating under the umbrella of Capital for Enterprise, a fund management company owned by the Department for Business, Energy, and Industrial Strategy.

Indirect support is common in the cultural sector and in creative industries. In the cultural sector, support usually takes the form of special tax regimes or tax breaks (i.e., tax deductions, tax credits, or a combination of both) to stimulate private donations. In the more commercial creative industries, support may take the form of a preferential tax scheme for targeted firms. In Europe, as of December 31, 2014, 26 fiscal incentive schemes were identified in 17 European countries. Most of these

⁵⁰ Financial institutions are rarely at ease with the sector's innovation-driven character, notably when its copyright content is high. However, despite these difficulties, collateralization and securitization of individual IPRs is increasingly becoming a more viable option for financing ventures in the creative industries (UNESCO, 2013).

schemes have been introduced since the 2000s, particularly during the 2010s (see Goto [2016] and references therein). The US National Endowment for the Arts' model favors fiscal incentives, which are also used in many other countries. In fact, even when other cultural policy models favor other forms of support (e.g., UK Arts Council or the French model), they still offer tax incentives to private agents who support the creative industries (see Klamer, Petrova, and Mignosa [2006] and Schuster [2006] for a reference to tax breaks in the European Union). France, the United Kingdom, Singapore, Australia, and Ireland have used fiscal incentives to stimulate the film and video game industries. Indirect support may be directed to copyrights for creative products since ownership of copyrights is one of the most common barriers to entry into creative industries.⁵¹ Tax breaks may also focus on artistic activity, justified by very particular features of the labor market for artists, particularly low and highly variable earnings combined with the multi-job phenomenon (Benhamou, 2003; Throsby, 2010). For instance, in Colombia, all artistic activities related to performing arts are exempt from the Value Added Tax. Also, it is very common in LAC for tax deductions to be provided to private businesses that invest in artistic activities or infrastructure.

Similar to traditional innovation policy, fiscal incentives have also been used to stimulate research and development (R&D) in the creative industries. The underlying idea is that uncertainty can lower investment in R&D in the creative sector. In the provinces of British Columbia, Ontario, and Quebec in Canada, tax incentives are used to foster R&D investment in video games. The growth in this sector is in great part due to the R&D tax credits, which added to a strong education and university research system. Other creative sectors in Canada that benefit from these credits include music and sound recording, book publishing, and film and TV production.

7.2. Demand-Side Policies

On the demand side, different support schemes have been implemented to incentivize consumption of cultural and creative goods and services, especially among disadvantaged segments of populations. Cultural vouchers are considered well suited to coping with access, which is biased toward high education, occupation, and income status groups.⁵² Under these schemes, the decision on which cultural activities are worthy of public support is shifted from the bureaucracy and experts to consumers, who directly evaluate what cultural goods and services are most valuable to them.⁵³ An interesting initiative based on vouchers is the *Vale Cultura* program, implemented by the Brazilian Ministry of Culture in 2013. This program provides workers from associated firms a monthly voucher equivalent to approximately US\$20 to be used

⁵¹ The only way a competing firm can obtain existing copyrights is to buy them or acquire a license to use them (Towse, 2010).

⁵² For an excellent review of the literature on the determinants of cultural participation, see Seaman (2006). See also O'Hagan (1996); Throsby (1994). For the way voucher schemes function, see Peacock (1993, 1994); Towse (2010).

⁵³ Those that argue against this kind of program suggest that demand will be driven by middle-of-the-road tastes, and thus such programs do not benefit the most innovative products, which are generally those with the highest potential. One way to tackle this is to narrow the set of alternatives among which people can choose. However, to what extent should the range of services be restricted? That is still an open question.

exclusively on cultural goods and services. A network of 40,000 cultural companies around Brazil was created to provide different cultural options, including cinemas, scenic arts, museums, books, and concerts. The government and the associated firms share the cost of the ticket, while the government provides tax incentives to the firms that are associated with the program.⁵⁴ Recently, the government of Italy announced a cultural voucher scheme focused on 574,000 teenagers, each receiving 500 euros for their 18th birthday to purchase cultural goods or services. This program will be managed through a web platform combined with a mobile app to reduce administrative costs.

7.3. Systemic Policies

Coordination failures and the uncertainty derived from the intangible nature of creative content may hinder collaboration between different actors (OECD, 2010; Sala, Landoni, and Verganti, 2016). Therefore, public interventions can also focus on correcting these failures by strengthening the links between agents participating in the creative economy. In this area, a different form of voucher (a credit voucher) is the most common instrument. This scheme usually consists of identifying a specific sector (e.g., small- and medium-sized enterprises [SMEs] or startups) and providing them with a voucher that can be used to buy specific services or goods. In particular, the credit voucher serves to create linkages between creative firms and traditional sectors by conditioning traditional firms to use the voucher at creative firms.⁵⁵ The best example is the UK Creative Credits, a scheme that aims to turn creative businesses into a source of innovation and to support potentially powerful business-to-business knowledge exchanges. This program provides eligible SMEs with vouchers with a value of £4,000 to purchase services from a network of creative suppliers to develop innovative projects. The program was first implemented as a pilot in Manchester, and it is now available in eight regions in the United Kingdom. An evaluation conducted by NESTA shows that the program succeeded in creating linkages between traditional SMEs and creative firms. In addition, the program increased the innovation rates and sales of the participant SMEs (Bakhshi et al., 2013).^{56,57}

Another interesting initiative that was implemented in response to coordination and information failures is Creativeworks London, which is one of four Knowledge Exchange Hubs for the Creative Economy funded by the Arts and Humanities

⁵⁴ Other schemes include low scale and experimental efforts, such as The Twin Cities Metropolitan Alliance in Minneapolis-St. Paul (Glover, 1975; Heilbrun and Gray, 1993; Kranz, 1975); The Voucher Program for the Support of Off-Off-Broadway in New York (Baumol, 1979); The New York City Cultural Voucher Program, which targeted museums (Bridge and Blackman, 1977); the CKV: Arts Education and Vouchers in the Netherlands (see Bamford, 2007; Damen and Van Klaveren, 2013; Haanstra and Nagel, 2002).

⁵⁵ Skantze (2014) analyzed six voucher schemes—three that supported innovation within creative industries (in Sweden, Germany, and Austria) and three that stimulated demand for creative services from other economic sectors (in Denmark, Austria, and the United Kingdom)—and discussed their relative advantages.

⁵⁶ See Bakhshi et al. (2013) and NESTA (2011) for more details on creative vouchers.

⁵⁷ The VINCI (Vouchers in Creative Industries) program is similar to the UK Creative Credits and was implemented and run by Austria Wirtschaftsservice GmbH, Austria's national business support agency. The results indicate that more than 50 percent of the small- and medium-sized enterprises that applied have not received any funding in the past 5 years, 90 percent said that without the voucher it would not have been possible to implement their project as planned. Moreover, 80 percent admitted that the connection with the creative firms will continue in future projects (Skantze, 2014).

Research Council.⁵⁸ These hubs work as consortia, connecting research with creative and cultural organizations. A good example at the European level is the European Creative Industries Alliance (ECIA), an integrated policy initiative that brings together policymakers and practitioners from 28 partner organizations and 12 countries. ECIA has not only promoted using vouchers but also developing clusters and better access to finance (ECIA, 2014).

Coordination failure is also the rationale underlying policies supporting creative clusters. In fact, geographical proximity of firms, input suppliers, and research facilities, among other actors, are considered to be key factors in developing creative industries (Santagata, 2006), but sometimes coordination failures hinder the spontaneous emergence of clusters, calling for public intervention. In this regard, Bakhshi, Hargreaves, and Mateos-Garcia (2013) highlight the role of universities as anchor institutions playing a central role in a creative cluster development strategy, as suppliers of talent, research, networks, support services, entrepreneurialism, and other facilities. An example of this is the International VFX Hub at the National Centre for Computer Animation at the University of Bournemouth, which combines working with local schools, knowledge transfer through PhDs in industry, support for graduate entrepreneurship, and access to facilities in an effort to boost the animation and post-production industry.⁵⁹

7.4. Human Capital Formation Policies

A particularly severe coordination failure is that between the creative economy's demand for skills and the education system. There are many ways governments can address this failure. For instance, by signaling quality through accreditation, governments can induce a higher return to accredited people, which increases incentives to accumulate targeted skills. Another major issue is the mismatch between the knowledge and skills needed to succeed in the creative industries and the formal education and training provided (Arnold et al., 2014). This mismatch calls for state intervention, such as a regulation that provides enough incentives to the education system to support creativity by promoting STEAM (Science, Technology, Engineering, Arts, Math), not just STEM. Governments can also offer scholarships and grants to students to follow academic careers in the creative economy.

The benefits of such policies are twofold: (i) they create a critical creative labor force and (ii) they increase the research capabilities that support new developments in this sector. Also, stimulating arts education appears to be important as long as it is directly related to acquiring creative skills (supply side) and it helps form a taste for culture that stimulates long-term demand for cultural goods (demand side).⁶⁰

⁵⁸ This Hub is led by Queen Mary University in partnership with 21 London-based higher education institutions and independent research organizations and 22 creative and cultural industry organizations.

⁵⁹ For more details visit <http://www.btxfestival.com/partners/>.

⁶⁰ For evidence supporting the positive correlation between arts education and long-term demand for culture, see Champarnaud, Ginsburgh, and Michel (2008); Cuccia (2011); Haanstra and Nagel (2002); Leroux and Moureau (2006); Zakaras and Lowell (2008).

8. Institutional Challenges

As discussed in previous sections, there exist various justifications for public intervention in the creative economy and different channels through which the public sector can operate, either offering public goods or directly intervening in the market. However, public intervention is not exempt from problems in efficiency and effectiveness, which in some cases can be so serious they nullify any beneficial effect of the intervention.

These problems, whose solutions are mainly determined by the way the supporting public institutions (including the state) are structured, are known in the institutional economic literature as state failures.⁶¹ This literature suggests that there are at least three well-defined state failures or situations where there is not consistency between the goals the public sector pursues and the behavior of the public agents in charge of their implementation. In general, state failures arise whenever the incentive scheme or the legal framework is not consistent with the purpose for which it was designed.

The most recognized state failure in the creative economy is dynamic inconsistency, which refers to situations where a time consistent public policy program is needed (like for the creative economy) but for some reason (usually due to a change in authorities) there are radical changes in the direction of the policy.

In fact, one of the main features of the creative and cultural sector is that, in many cases, the effects of public support are not contemporaneous with the support itself or it is difficult to attribute the results to previous efforts given the intangibility of many public interventions (e.g., promotion, diffusion, and networking activities). Further, there may be conflict between public interventions that generate tangible effects in the short run (generally preferred by authorities) and the most efficient way to achieve long-term objectives.

Another common state failure is agency problems, which were first discussed by Williamson (1964) when he identified potentially different incentives between the owners of a firm and those who manage it. In Williamson's original formulation, the owner (known as the principal) wants to maximize the value of the firm, whereas the manager (known as the agent) may be more interested in the stability of its administration. In this situation, a problem arises because an information asymmetry exists: the manager has more detailed information about the firm's performance than the owner.

In government, an agency problem might arise when a minister plays the role of the principal and the person in charge of an implementing agency plays the role of the agent. This coordination problem between the minister and the agency can be avoided

⁶¹ See Benavente and Larraín (2016) for a discussion of state failures in the context of arts and culture economics.

if mechanisms provide the principal access to information about the agent's role. In that way, not only can the minister ensure that long-term objectives are still being targeted, but they can also prevent inefficiencies, overlap, and lack of coordination across agencies.

Finally, capture, the most complex state failure to address, occurs when an institution that has established a relationship with a group of beneficiaries cannot withhold the support once it is no longer justified. Capture results from potential political retaliation or scandals, or possibly because the legal framework does not allow for changes. For instance, programs that support arts and other cultural activities are often criticized because the potential beneficiaries are too close to the institutions in charge of designing and implementing the programs.

Moreover, when it comes to implementing any of the above-described policies, policy framework and institutional coordination appear to be additional challenges. In fact, usually multiple public institutions—sometimes with very different priorities, approaches, and constituencies, such as Ministries of Culture, Economy, and Science and Technology—are simultaneously in charge of relevant aspects of the sector, making it difficult to design and implement effective policy instruments in the absence of a formal articulation mechanism.

Therefore, countries that have acknowledged the importance of the creative economy as an engine of economic development have also recognized the importance of creating new institutional arrangements to solve the described state failures and to guarantee a coordinated response to the sector's necessities, both in terms of policy design and implementation.

For example, in 2011, the United Kingdom established the Creative Industries Council, which integrates the government, the creative private sector, and non-profit organizations.⁶² The main objective of this council is to provide a platform to discuss barriers to growth faced by the sector, such as access to finance, skills, and international markets; regulation; IPR; and infrastructure. Similarly, in Latin America in 2014, Chile created the Inter-Ministerial Committee for Creative Economy, which integrates the National Council for Culture and the Arts and the Ministries of Social Development, Economy, Agriculture, and External Relations. The committee's objective was to draft a National Plan of Creative Economy, which was released in May 2017.

⁶² The *government* is represented by the Department of Culture, Media, and Sport; the Department for Business, Innovation, and Skills; and by Innovate UK, which is the UK's innovation agency. The *creative private sector* is represented by UK Music on behalf of the recorded and live music industry; the Advertising Association, representing the advertising sector; PACT, representing independent television, film, digital, children's, and animation media companies; the Design Council, representing the design economy; the Publisher Association on behalf of books, journals, audio, and electronic publishers; the British Fashion Council, representing the fashion industry; the British Photographic Industry; and the UKIE, representing the games and interactive entertainment industry. In addition, there are representatives from important companies such as Warner Bros, BBC, Facebook, Playdemic, and King. The *non-profit institutions* include NESTA, Creative Skillset, and the Royal Institute of British Architects.

In summary, a proper institutional design is crucial to minimize inefficiencies related to public intervention in the creative economy. There are many clues that indicate a design is not adequate, such as (i) not having clearly identified the public agency responsible for these activities, (ii) the lack of coherence between goals and objectives and the resources allocated, and (iii) the absence of systematic monitoring and evaluation of the implemented initiative, which could allow the public sector to repeat and improve successful programs or to discontinue ineffective ones. Therefore, it is necessary not only to assess the resources and instruments used by the public sector to promote the creative economy, but also to evaluate whether the institutional arrangement helps achieve the established objectives.



9. Final Remarks

This document provides an overview of the Creative or Orange economy, highlighting its role in promoting economic growth, inclusive development, and innovation. A number of key points have been made. First, creative sectors appear to be characterized by high productivity growth. Second, they are an important source of job creation for youth, not only in purely creative sectors, but also in traditional industries. Finally, creativity is a main driver of society's process of innovation. In fact, creative outputs are unique and disruptive, and they have the potential to inspire people across society, generating ideas and, therefore, innovations.

In particular, even if the creative economy already contributes significantly to LAC's economy, the richness and uniqueness of the cultural history and tradition of the region indicates that it constitutes a still substantially unexploited opportunity. Multiple market failures prevent countries from producing the socially desired amount of creative activities, calling for active public intervention. However, designing and implementing effective policies related to the creative economy is not easy. To successfully design policy interventions, governments need to follow a systemic approach, meaning that it is essential that programs operate on all the components of the creative ecosystem. This requires a policy mix comprising different instruments to simultaneously stimulate supply, demand, and interaction among the various actors.

Moreover, the varying degree of maturity of the creative ecosystems in Latin America creates an additional challenge for policymakers since different policy approaches are required. While some countries have started to build on their heritage and talent, developing modern creative sectors—such as video games or audiovisuals—others still mainly rely on traditional activities. This diversity is reflected in the composition of creative ecosystems, where countries show a variety of institutional arrangements and IPR regimes.

In this context, countries with an emerging ecosystem should first consolidate its core by focusing on the supply of creative goods and services by targeting instruments that aim to upgrade selected creative industries. At the same time, governments need to prioritize programs that promote the formation of creative human capital with the required skills for those industries.

As well as more sophisticated instruments to stimulate development of creative industries and provide skilled human capital, countries where the ecosystem is at an intermediate level need to focus on systemic policies to improve coordination among ecosystem actors, particularly those that operate in creative clusters. This is particularly important to promote integration of the creative sectors in global value chains.

Countries with more mature creative ecosystems should focus on systemic policies to strengthen linkages between a well-developed creative industry and other sectors in order to improve the economy's overall productivity. Moreover, policies should

also enhance connections with the knowledge sector (e.g., universities and research centers) to fully exploit the innovative push of the creative activities. In countries with a potentially attractive domestic market, demand-side stimulus packages can also play an important role.

No matter the level of development of a country's creative economy, an adequate institutional setting is required to effectively coordinate the necessary policy interventions. In most LAC countries, the policy responsibility related to developing the creative economy is still shared by many institutions, and, in absence of long-term coherent strategic plans, public actions are often ineffective. To solve this problem, collaboration platforms need to be established between public agencies operating in different aspects of the creative economy, as well as between public and private agents. Drafting adequate regulations, particularly for IPRs, is key to fostering creative investment.

Also, in order to promote evidence-based public policy programs and deepen the understanding of their performance determinants, collecting and analyzing information related to the creative economy is a priority. In particular, authorities need to design relevant indicators and collect data to rigorously evaluate programs, possibly using experimental or quasi-experimental methodologies.

Finally, it is important to recognize that digital technologies are changing the creative economy. Technology provides new tools to transform ideas into creative products and new channels to spread those products. Providing the infrastructure and training to build new skills is crucial to take full advantage of the creative economy's potential and to prepare LAC countries for the challenges of the digital economy.

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