

REGIONAL POLICY AND STRUCTURAL FUNDS IN THE EUROPEAN UNION: The Problem of Effectiveness

*Nagihan OKTAYER**

Özet

Avrupa Birliđi'ndeki yapısal politikaların en temel hedeflerinden biri Birlik genelindeki bölgesel farklılıkları azaltmak ve ekonomik büyüme hızlandırmaktır. Söz konusu amaca ulaşmada en çok başvurulan araç ise Yapısal Fonlardır. Özellikle son dönemlerde, Avrupa Birliđi'nin bölgesel politikaları çerçevesinde bu fonların yoğun bir biçimde incelenir ve kısmen de eleştirilir hale geldiđi görülmektedir. Yapısal fonların etkinliđine ilişkin ciddi bir literatür bulunmakla birlikte, gerek teorik gerekse amprik çalışmalar bu alanda oldukça çelişkili sonuçlar vermektedir. Bu çalışmanın amacı, mevcut teorik ve amprik çalışmalardan hareketle yapısal fonların etkilerini incelemek ve söz konusu fonların Birlik ülkeleri arasında ne ölçüde bir yakınsama sağlayabildiđini, bir diđer ifadeyle kendilerine verilen bu görevi ne ölçüde yerine getirebildiklerini tespit etmeye çalışmaktır.

Anahtar Kelimeler: *Avrupa Birliđi, Bölgesel Politika, Yapısal Fonlar, Yakınsama, Genişleme*

Abstract

One of the basic goals of the Structural Policy is to decrease the regional disparities and to promote economic growth within the European Union. Structural Funds are the most intensively used policy instrument by the Union to achieve this goal. In the recent years, Structural Funds has become one of the most intensively evaluated

* Assist. Prof., Istanbul University, Faculty of Economics.

and partly criticized policies of the Union in the context of Regional Policy. There is a considerable literature on the effectiveness of Structural Funds. There are many conflicting theoretical and empirical studies in this context. The purpose of this study is to examine the effects of Structural Funds and to look for an answer if these Funds help the Member States in achieving greater economic cohesion.

Key Words: *European Union, Regional Policy, Structural Funds, Cohesion, Enlargement*

Introduction

Greater equality in productivity and income across Europe has been one of the central goals of the European Union since the early days of integration. In achieving this goal, various policy measures have been introduced over the years. Structural funds are the most favorite instrument used by the European Union to reach this goal.

In 1993, the leaders of the Union made a historical decision that the associated countries in Central and Eastern Europe were allowed to become European Union members if they so wished. According to this decision, twelve new member countries joined the Union in the recent past. No doubt that, this enlargement increases regional disparities within the Union. The new member countries are relatively less wealthy and have a GDP per capita that is less than the European Union average. In addition, all these countries face a wide range of internal regional problems and are economically and socially behind the former members. In short, enlargement of the Union made regional policy much more important than ever before.

Another point which should be taken into account is that, the European Union that the accession countries are joining is very different from the European Community that the catching up countries joined in the 1970's and the 1980's. As the internal market and economic integration are much deeper now than they were before, membership is also likely to increase economic links more than it did earlier¹.

Structural funds are the most powerful policy tool used by the European Union to combat with the regional disparities within the Union. European structural support has grown in parallel with European Integration. Today, these funds cover nearly one third of the total European Union budget.

To what extent the Structural Funds have succeeded in their objective of reducing disparities between the levels of development of the various regions? Do they help the Member States in achieving greater economic and social cohesion and in reducing the gap between the centre and the periphery of the European Union? Although Structural Funds cover an important share of the Union budget, these Funds

¹ Ville Kaitila, **Convergence of Real GDP per capita in the EU 15**, ENEPRI Working Paper No. 25/ January 2004, p.2.

and Regional Policies have come under increasing criticism based on the lack of upward mobility of assisted regions, and the absence of regional convergence².

There are also some criticism over the criteria used to assess whether or not regions are eligible for funds, and how these funds are then used? Objective one funding, which makes up two thirds of the structural funds, is only available in those European Union regions (NUTS level 2) where GDP per capita is lower than 75% of the European Union average. These criteria do not allow for inter regional disparities, and regions can find that they lose their eligibility for funding despite still having some very needy areas within them³.

The purpose of this study is to examine the effectiveness of Structural Funds and to look for an answer if these Funds help the Member States in achieving greater economic cohesion. In this context, after the exposition of different theories, reasoning behind the Regional Policy, existing regional disparities within the European Union, development of Structural Funds, some empirical studies and improvements of Cohesion countries will be analyzed.

Economic Growth Theories and the Convergence

When one mentions real convergence⁴ between countries/regions, it generally means the approximation of the levels of economic welfare across those countries/regions. Economic welfare of a country is generally proxied by GDP per capita. For that reason the question of real convergence is related to economic growth.

There are conflicting views in the literature regarding the relationship between convergence and economic integration. Two main economic growth theories arriving at opposite conclusions can be cited, the neoclassical growth theories and the endogenous growth theories. The differences in points of view are caused by diverging beliefs in the underlying assumptions on economic growth.

The neoclassical Solow theory points out the importance of the capital accumulation and technological progress in the process of economic growth of countries⁵. Assuming of constant returns to scale of each input and of diminishing returns to capital, the model states that output per worker can rise if and only if the technological progress takes place. Hence the economy does not grow in the long-run without any technological advance. The Solow model predicts absolute convergence in the sense that the growth rates between the poor and rich countries will be equalized in

² Andreas Rodriguez-Pose ve Ugo Fratesi, "Between Development and Social Policies: The Impact of European Structural Funds in Objective 1 Regions", **Regional Studies**, Vol. 38.1, February, 2004, p.99.

³ <www.openeurope.org.uk/research/budgetoutcome> (16.05.2007)

⁴ While real convergence means the convergence of income levels, nominal convergence describes the convergence of price levels and institutional convergence implies harmonisation of legislation.

⁵ Robert M. Solow, "A Contribution to the Theory of Economic Growth", **The Quarterly Journal of Economics**, V. 70. 1, 1956, p.65-94.

the long-run. The convergence mechanism occurs because the capital is subject to diminishing return and the marginal productivity of capital is higher in the poor countries than the rich ones.

According to the view that is based on comparative advantages, if the factors of mobility and diffusion of technology are not restricted, improvements in economic convergence among countries/regions occur. Put it differently, by technological improvements and the presence of free trade and market competition, convergence would take place. Thus opening up the country/region would accelerate the convergence process, as capital flows to capital-scarce countries/regions to benefit from higher returns. As the theories related to economic integration allege, through trade and international factor mobilities between the member countries, prices, costs and income levels tend to converge. Consequently economic integration would lead to a greater economic development through a convergence process.

Endogenous growth theories developed in the 1980's, on the other hand, emerged as an attempt of understanding the forces behind technological progress which the Solow model leaves it out as unexplained. Asserting that income convergence between rich and poor countries/regions may not be the only possible outcome, they emphasize the research and development efforts in the accumulation of new ideas⁶ (Romer, 1990) and the role of human capital⁷ (Lucas, 1988) in the production of goods. Assuming of unbounded accumulation of ideas and human, capital both model generate an unbounded growth in the long-run which all the factors affecting economic growth is explained in the model itself. Lastly, in the same vein as Romer's, some other endogenous growth models emphasize the importance of commercially oriented research and development efforts as the main engine of growth, explaining the permanent technological and income gaps between countries. For that reason economies need surely not to converge and convergence may not occur. Nonetheless there is another group of endogenous growth models which assumes the existence of knowledge spillover effects. If it is considered that imitating is a cheaper way of using a new technology than by innovating, these models imply that convergence through technological diffusion is a possible outcome.

The Concept of Cohesion and Regional Policy

The European Union is an integration which has some deep political, economic and social goals. One of the fundamental objectives of the Union is cohesion; the reduction of economic and social disparities between richer and poorer regions within the Union. However, it should be noted that cohesion is not an easy notion to define and although there is often a tacit understanding of what it means, it is open to a variety of interpretations. It includes inequalities, whether in income, living standards,

⁶ Paul M. Romer, "Endogenous Technological Change", *Journal of Political Economy*, V. 98, 5, 1990, p. 71-102.

⁷ Robert E. Jr. Lucas, "On the Mechanics of Economic Development", *Journal of Monetary Economics*, V. 22, 1, 1988, p.3-42.

employment, or environmental conditions, and also has to be seen in terms of opportunities as well as outcomes⁸.

The concept of cohesion is not defined in the founding Treaty, but Article 158 of the Treaty makes clear that this concept requires, in particular, the reduction of disparities between the levels of development of various regions. Cohesion was accepted as one of the main objectives of the Union by the Maastricht Treaty. Since the mid 1980's, the structural funds have provided the main instruments for promoting cohesion in the European continent⁹.

Regional Policy has been introduced for a mix of *economic motives* such as utilisation of production factors and congestion costs; *social factors* such as commitment to full employment and welfare considerations; environmental arguments such as over-crowding and pollution in congested areas; and political reasons such as consequences of disparities for voting patterns¹⁰.

Since the mid 1970s regional policy has existed at the EU community level. The regional policy's main aim is to make redistribution among regions and countries. It is clear that, there is an equity argument for community action in favour of weak economic regions. In addition, in the presence of externalities even efficiency might require intergovernmental grants from the community to member states¹¹. It is believed that, because of externalities, excessive disparities in the level of socio-economic development between member countries and the regions hit not only poorer areas, but also richer ones. For this reason, cohesion and regional policy is recognized as one of the foundations of European integration in the Treaty of Rome and in other treaties.

The objectives of regional policy are often discussed as a trade-off between aggregate national efficiency, involving a more efficient allocation of regional resources to maximize net national benefit; and inter-regional equity, involving a more equal distribution of income, employment or infrastructure over space. Over the long term, European Union Member States tended to introduce regional policies for

⁸ Iain Begg, **Complementing EMU: Rethinking Cohesion Policy**, Oxford Review of Economic Policy, Vol. 19, No:1, 2003, p.163.

⁹ Pere G. Porcheras ve Enrique Garcilazo, **EU Structural and Cohesion Funds in Spain and Portugal: Is Regional and National Inequality Increasing?**, Miami European Union Center, Working Paper Series, Vol. 3, No: 11, 2003, p.1.

¹⁰ Norbert Vanhove, **Regional Policy: A European Approach**, Ashgate Publishing, Aldershot, 1999, German Institute for Economic Research and European Policies Research Centre, **The Impact of European Union Enlargement on Cohesion-Background Study for the 2nd Cohesion Report**, 2001, p.17.

¹¹ Robert Fenge ve Matthias Wrede, **EU Regional Policy: Vertical Fiscal Externalities and Matching Grants**, CESifo Working Paper, No: 1146, München, 2004, p.1.

reasons of equity but have progressively given greater priority to efficiency since the mid-1970s¹².

Regional policy goals are increasingly concerned with optimising the contribution of regional resources to the creation of economic growth by promoting competitiveness and reducing unemployment. This is true for smaller European Union countries where regional differences are comparatively small (Austria, Denmark, Netherlands, Switzerland), as well as larger Member States which have suffered relatively high, nationwide unemployment for much of the past 20 years and which have extensive areas experiencing deep-seated industrial decline and social problems. However, the equity goals of regional policy still exist: concern with spatial equality as an objective of regional development remains to some degree in the Nordic countries, France (in part) and in Germany, where the aims of regional policy continue to advocate the reduction of inter regional disparities in relation to income generation and employment opportunities¹³.

Regional Disparities within the European Union

Regional disparities existing between member states constitute the policies towards cohesion implemented in the European Union. Despite the significant achievements of cohesion policy to date, major disparities still remain across the Union. Begg identifies four main types of regional problems that cause regional disparities and lists them as follows:

- lack of development,*
- peripherality, remoteness or inaccessibility,*
- loss of competitiveness,*
- the consequencess of economic integration.*

The first reason behind the regional differences is lack of development. Because of lack of development many regions became deficient in the dynamic sectors of activity that have supported economic advances. In some parts of the Europe, until quite recently, agriculture remained a dominant industry and there was relatively little industrialization. Secondly geographical disadvantages of some countries like peripherality, remoteness or inaccessibility are important for that those kinds of disadvantages are permanent and cannot easily be countered. Being most of the regions that are designated "less-favoured" on the periphery of the EU is a significant reason for support. Thirdly, loss of competitiveness can arise within the member state countries and it can be hard to reverse the cumulative processes that reinforce the initial loss. While regional problems are associated mainly with the contraction of old staple industries like coal-mining, steel-making, textiles and shipbuilding in northern Europe,

¹² German Institute for Economic Research and European Policies Research Centre, **The Impact of European Union Enlargement on Cohesion-Background Study for the 2nd Cohesion Report**, p.17-18.

¹³ **Ibid.**, p.17-19.

some regions have adversely been affected by the relative decline of newer manufacturing industries like motor vehicles. Finally consequences of economic integration may also be a reason of regional disparities. Sometimes dismantling of barriers or a reconfiguration of the policy or regulatory frameworks may in themselves precipitate regional problems¹⁴.

It is important to consider, when trying to evaluate the success of the Structural Funds on reducing regional disparities within the EU, that changes in regional disparities are not, by themselves, a sufficient test of the effectiveness of EU cohesion policy. This is because regions have been affected in different ways both by large-scale economic changes and by the processes of European integration. The Community's regional policy is not on a comparable scale to these factors. However, trends in regional development can provide a background against which to judge the effectiveness of the Community's regional policy.

Disparities in GDP per head between the 25 Member States are considerable. In 2003, levels of GDP per capita (measured in purchasing power parities) range from 41% of the EU average in Latvia to 215% in Luxembourg. Ireland is the second most prosperous country in these terms with GDP 132 % of the EU average. In all new Member States, GDP per head is below 90% of the EU 25 average, while it is less than half of this level in Poland, Latvia, Lithuania and Estonia, as well as Romania and Bulgaria¹⁵.

In 2002, the most recent year for which regional data are available, levels of GDP per head ranged from 189% of the EU-25 average in the 10 most prosperous regions to 36% in the 10 least prosperous ones. Over one quarter of the EU's population in 64 regions have GDP per head below 75% of the average. In the new Member States this concerns 90% of their total population, the exceptions being the regions of Prague, Bratislava, Budapest, Cyprus and Slovenia. In the EU15, this concerns only 13% of the population. Among the EU15, the low-income regions are concentrated geographically in southern Greece, Portugal, southern parts of Spain and Italy, as well as in the new Lander in Germany¹⁶.

Average per capita GDP in the EU fell substantially with enlargement to ten relatively poorer new Member States. In certain regions, this has meant GDP per capita rising above 75% of the new EU 25 average, although they remain below 75% of the average for the EU15 around 3.5 % of EU population live in such regions. A further 4% live in regions which had GDP per head below 75% of the EU 15 average in the 2000-2006 period but which have grown beyond this level even in the absence of the effect of enlargement¹⁷.

¹⁴ Begg, *Complementing EMU: Rethinking Cohesion Policy*, p.163-164.

¹⁵ European Commission, *Third Progress Report on Cohesion: Towards a new Partnership for Growth, Jobs and Cohesion*, 2005.

¹⁶ *Ibid.*,

¹⁷ *Ibid.*,

The Structural Funds as a Tool of Cohesion Policy

The European Union attempts to reduce these differences between its regions. It does so by funding programmes in regions that lag behind in production per capita, over-rely on industries in decline, or face high unemployment. These programs, in general, intend to enhance infrastructure, restructure industries, or modernise education¹⁸. While this practice is known as cohesion policy, the funds used for this aim is called as Structural Funds.

The origins of the European Union structural funds are to be found in the Treaty of Rome. The preamble of the founding treaty set out the commitment of the member states to “ensure their harmonious development by reducing the differences existing between the various regions and the backwardness of the less favoured regions”.

The European Regional Development Fund was established as an embryonic regional policy with a limited budget. By establishing it, the European Union aimed to redistribute part of the Member States’ budget contributions to the poorest regions. It was not intended primarily to promote cohesion but was nonetheless expected to help the Union’s poorer regions. Until the first enlargement of in 1973 with Britain, Denmark and Ireland, the regional disparities were not that striking. But especially Ireland’s accession caused some regional imbalance within the Union. Although Ireland was the poorest accession country, the European Regional Funds were not established with the intention to end the regional disparities in Ireland. The Fund was to compensate Britain for its poor return from the Common Agricultural Policy¹⁹.

Nearly, a decade later, the Single European Act provided the impetus for a more substantive regional policy, introducing the concept of “economic and social cohesion”. The Single European Act took the lead from the original clause in the Treaty of Rome, declaring that “in order to promote its overall harmonious development, the Community shall develop and pursue its actions leading to a strengthening of its economic and social cohesion. In particular the community shall aim at reducing the disparities between the various regions and the backwardness of the least favoured regions, including rural areas” (Art. 158).

The Single European Act was a very important step in this context. This reform was implying the coordination of the three Structural Funds (ERDF, ESF, and EAGGF-Guidance Section) under the principles of territorial and financial concentration, programming, partnership, and additionality. This step implied not just the coordination of all existing funds under the umbrella of Structural Funds and a comprehensive restructuring of the principles that guided their action, but also the

¹⁸ Sjef Ederveen ve Joeri Gorter, **Does European Cohesion Policy Reduce Regional Disparities?**, CPB Discussion Paper, No: 15, 2002, p.7.

¹⁹ Maaïke Beugelsdijk, **Should Structural Policy be Discounted? The Macro-economic impact of Structural Policy on the EU-15 and the Main Candidate Countries**, De Nederlandsche Bank, Research Memorandum WO No: 693, 2002, p.8.

doubling in relative terms of the money committed to regional development, from 15.1 % of the European budget in 1988 to 30.2% in 1992²⁰.

On the other hand, with the inclusion of economic and social cohesion as one of the Union's priorities alongside the single market and economic and monetary union, the Treaty of the European Union took the commitment one step further²¹. In 1992, the European Union decided to the creation of the Cohesion Fund to support the least prosperous Member States in their efforts towards economic convergence for preparation of economic and monetary union. Ireland, Greece, Spain and Portugal were the poorest Member States who had a gross national product of less than 90%. Together, the Structural and Cohesion Funds represent the Union's regional policy. Commonly known as cohesion policy, it entails the funding of infrastructure and employment projects in lagging regions of the European Union member states.

Some reforms were made regarding Structural Funds by the Union over the years. The strategy of the Union in the reforms of the Structural Funds was to pursue the objectives of a concentration of resources and a simplification of procedures. But above all the reform was needed in order to make room for the new Member States in a framework where the overall budgetary availability will be limited. Agenda 2000, as decided at Berlin, proposes a reform of the Funds, with the basic objective of not exceeding an expenditure limit of 0.46% of EU GDP. The core of the reform is the strict application of conditionality for access to the funds. This will automatically lead to many regions which have formerly received structural funds losing them in the future. As the Community begins to build up transfers to the new Member States, transfers to the existing Member States will decline²². The period 2000-2006 is therefore a transitional one, with a large allocation of transitional financial support to regions losing their status as transfer recipients.

To avoid transfers rising to unmanageable levels, the Union has decided to limit the transfers from the Structural Funds and the Cohesion Fund to 4% of the recipient country's GDP. This limit appears to be on the low side for the new Member States, which as mentioned above might have expected much higher transfers under the old rules of the Funds. Three points are worth noting however²³:

- None of the existing Member States have received transfers above this level from the Structural Funds (through Ireland received considerably higher levels if transfers from the CAP are also included)

²⁰ Andreas Rodriguez-Pose ve Ugo Fratesi, "Between Development and Social Policies: The Impact of European Structural Funds in Objective 1 Regions", **Regional Studies**, Vol. 38.1, February, 2004, p.98-99.

²¹ Stefaan De Rynck ve Paul McAleavey, "The Cohesion Deficit in Structural Fund Policy", **Journal of European Public Policy**, 8:4 August 2001, p. 542.

²² Alan Mayhew, **The Financial and Budgetary Implications of Accession of Central and East European Countries to the EU**, SEI Working Paper, 2000, p.13.

²³ **Ibid.**, p.14.

- The cofinancing of higher levels of transfers requires national budgetary funds to be made available

- The management of large unrequited transfers can lead to problems of macroeconomic instability, as the example of Greece demonstrates (though the good example of Ireland shows that such transfers can be consistent with macroeconomic stability)

- Successful use of transfer requires appropriate and efficient institutions in the recipient state.

European Union structural policy is the second biggest item in the Union budget, making up about one third of total expenditure. Structural policy is transferred into financial framework with two main instruments; the Structural Funds (90%) and the Cohesion Fund (10%). During the 2000-2006 period, the Agenda 2000 package allocated a total of € 213 billion to cohesion policy. € 195 billion of this was allocated to the Structural Funds and € 18 billion to the Cohesion Fund which targets Greece, Spain, Ireland and Portugal. When we add in the € 22 billion earmarked for new Member States in the period 2004-2006, the total structural expenditure comes to € 236 billion for the whole period, which is about 34% of the total European Union budget²⁴.

Over the 2000-2006 financial period, the bulk of the Structural Funds was allocated according to three "Objectives"²⁵.

-Objective 1 is to help lagging regions catch up with the rest of Europe by providing basic infrastructure and encouraging business activity. Regions with a GDP per capital of less than 75% of the Union average qualify for this type of funding.

-Objective 2 is to help the economic and social restructuring of regions dependent on industries in decline, agriculture, fishery or areas suffering from problems specific to urbanisation. Eligibility for objective 2 funding is complex. In order to qualify industrial regions must have an unemployment rate above the Union average, a higher percentage of jobs in the industrial sector than the Union average, and a decline in industrial employment. For rural or other types of regions, similar sets of requirements apply. In addition, regions must not be eligible for objective 1 support.

-Objective 3 is to modernise education and increase employment. This type of funding is Union wide. Any region may qualify, provided that it does not receive Objective 1 funding.

Instead of just giving money to the member states, the structural funds cofinance policy measures by the member states according to common rules laid down by the European Union authorities. The funding system in the European Union uses the matching grants instead of unconditional grants. It is generally accepted that, especially in supporting regional investments in infrastructure, matching grants are

²⁴ <<http://europa.eu.int/pol/reg/>>, (14.02.2007)

²⁵ Ederveen ve Gorter, **Does European Cohesion Policy Reduce Regional Disparities?**, p.9.

very important part of an efficient granting system. A pure system of unconditional grants in the Union is neither efficient nor the outcome of political processes. For this reason, in many cases, the Union finances most of the cost of Project but not all of it. For example, the poorer member states receive 85 per cent of the cost from the Cohesion Fund and finance rest of the cost themselves²⁶.

During the 2007-2013 financial period, the key priority of the cohesion policy is the promotion of growth and jobs in all EU regions and cities. For this purpose, EUR 308 billion was earmarked from the budget. This is very significant and the greatest investment ever made by the Union through the Structural Funds and the Cohesion instrument. 81.5% of the total amount is allocated to the “Convergence” objective, under which the poorest Member States and regions take place. In the remaining regions, 16% of the Structural Funds is concentrated on supporting innovation, sustainable development, better accessibility and training projects under the “Regional Competitiveness and Employment” objective. The final 2.5% of the Funds supports cross-border, transnational and interregional cooperation under the “European Territorial Cooperation” objective.

Effects of the Structural Funds on Cohesion Countries

Greece, Spain, Portugal and Ireland whose per capita incomes were significantly below the EU average during the 1990s are those referred to as “cohesion countries”. In assessing the effect of the cohesion fund on their economy, it is generally looked at the trend of their respective gross domestic product growth rates. The table below shows the evolution of this indicator for each of four countries and the EU average over the 1988-2004 period.

Table 1: Annual Gross Domestic Product Growth Rate in Cohesion Countries (1988-2004)

	1988	1989	1990	1991	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
Greece	4.3	3.8	0.0	3.1	0.7	-1.6	2.0	2.1	2.4	3.6	3.4	3.4	4.3	4.1	3.8	4.7	4.2
Spain	5.1	4.8	3.8	2.5	0.9	-1.0	2.4	2.8	2.4	4.0	4.3	4.1	4.2	2.8	2.0	2.5	2.6
Portugal	4.0	6.4	4.0	4.4	1.1	-2.0	1.0	4.3	3.5	4.0	4.6	3.8	3.7	1.6	0.4	-1.1	1.0
Ireland	2.1	6.0	6.3	1.4	4.2	1.4	5.8	9.9	8.1	11.1	8.6	11.3	10.1	6.2	6.9	3.7	5.2
EU-15	4.2	3.5	2.9	1.5	1.3	-0.4	2.8	2.4	1.6	2.5	2.9	2.6	3.3	1.6	1.0	0.8	2.2

Source: Leonardi, 2006, p.157.

²⁶ Fenge ve Wrede, EU Regional Policy: Vertical Fiscal Externalities and Matching Grants, p.1-2.

If we compare the average growth rates of cohesion countries with the EU average, it is clear that almost all four countries have succeeded in catching up. However, the experience of these countries in this period is very different. In terms of GDP growth, the EU average for the 1988-2004 period is 2.1%. In the same period, the Irish average Gross Domestic Product growth is 6.3 %. Spain and Portugal also began to grow at better than expected rates from the outset of the Cohesion policy. In general, with the exception of Greece, the cohesion countries showed a better performance of growth after their membership. Greece had a very uneven level of performance between 1989 and 1995.

It is generally questioned that if these impressive convergence rates are linked just on the existence of the Cohesion Policy or to other factors in combination with cohesion.

No doubt that, Ireland, whose income level is now above the EU average, is the most successful of all cohesion countries. Over the 90s no other EU member has been able to match its impressive growth performance. Before 1989, she was stuck for decades at a level of GDP per capita that fluctuated between 62 and 66 % of the EU average. The outstanding change took place in 1989 due to a prolific interaction of the Single Market²⁷. It took off immediately in 1989, and after that she never went back. The expectations and opportunities generated by the Single Market were helpful in transforming Ireland from a peripheral country to a well-developed one.

This impressive catch-up process of Ireland is often linked to the Structural Funds. On the other hand, most scholars link Irish success to the capacity to attract foreign direct investment. No doubt that, its strategy to invest in education and life long learning is a primary factor for the success in attracting foreign direct investment. The direct effect of the Structural Funds on the Irish growth rate was estimated to have added nearly 0.5% to the GDP growth rate over the 1990s. This is a relatively modest number when compared to the scale of the Irish growth rate during this time. However, it should be noted that, indirect effects are not included in these estimates. The indirect effects of the Structural Funds are related (i) to the fact the Structural Funds allowed the implementation of infrastructure projects that would not have been implemented otherwise due to fiscal constraints, and (ii) it aided investment in education and life-long learning. The indirect effects are related to the fact that good administrative capacities permitted the channelling of Structural Funds into projects that were consistent with national and regional growth strategies.

Beside gross domestic product growth rate, economic improvements can be gauged along many other different dimensions. Employment and unemployment rates are major indicators of general welfare. Table 2 shows data on employment rates between 1992 and 2003. While the employment rate within the European Union is fairly flat, the shift in Ireland has been from 51.2 to 65.4 %, in Spain from 49.0 to 59.7 %, in Greece from 53.7 % to 57.8 %, and in Portugal from 66.6 to 68.1 %. Portugal,

²⁷ Denis O'Hearn, "Economic Growth and Social Cohesion in Ireland" in Dauderstadt, M. and Witte, L. (Eds.) **Cohesive Growth in the Enlarging Euroland**, 2001, p. 80-90.

which began with an employment rate higher than the EU average, has made the least gains, but it should be noted that this is also the case in many more developed countries.

Table 2: Total Employment Rate in Cohesion Countries (1992-2003)

	1992	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003
Greece	53.7	53.7	54.2	54.7	55.0	55.1	55.5	55.3	55.7	55.4	56.7	57.8
Spain	49.0	64.6	46.1	46.9	47.9	49.4	51.2	53.7	56.2	57.7	58.4	59.7
Portugal	66.6	65.1	64.1	63.7	64.1	65.7	66.8	67.4	68.4	69.0	68.8	68.1
Ireland	51.2	51.7	53.0	54.4	55.4	57.6	60.6	63.3	65.2	65.8	65.6	65.4
EU-15	61.2	60.1	59.8	60.1	60.3	60.7	61.4	62.5	63.4	64.1	64.3	64.4

Source: Leonardi, 2006, p.163.

Another important economic and social indicator that has changed greatly since 1988 is unemployment. Spain and Ireland are the countries which have made good progress in that sense. (Table 3) Unemployment rates in Spain and Ireland were close to one-fifth of working population in pre-1988 period. But now, while unemployment rate is close to EU average in Spain, Ireland has an unemployment rate significantly lower than the average. On the contrary, Greece has experienced increases in unemployment from 1998. Unemployment levels peaked in 1999 at 12 % and then have remained at 2.5 percentage points above the EU average. Therefore, it is clear that the social situation in the countries and regions benefiting from Cohesion policy has not deteriorated as a result of market integration and economic growth and on most indicators it has improved significantly since the beginning of the policy²⁸.

Table 3: Total Unemployment Rate in Cohesion Countries (1993-2004)

	1993	1994	1995	1996	1997	1998	1999	2000	2001	2002	2003	2004
Greece	8.6	8.9	9.2	9.6	9.8	10.9	12.0	11.3	10.8	10.3	9.7	10.5
Spain	18.6	19.8	18.8	18.1	17.0	15.2	12.8	11.3	10.6	11.3	11.3	10.8
Portugal	5.6	6.9	7.3	7.3	6.8	5.1	4.5	4.1	4.0	5.0	6.3	6.7
Ireland	15.6	14.3	12.3	11.7	9.9	7.5	5.6	4.3	3.9	4.3	4.6	4.5
EU-15	10.0	10.4	10.0	10.1	9.8	9.3	8.5	7.6	7.2	7.6	7.9	8.0

Source: Leonardi, 2006, p.164.

²⁸ Robert Leonardi, "The Impact and Added Value of Cohesion Policy", *Regional Studies*, Vol. 40.2, 2006, p.163.

Although Structural Funds cover an important share of the Union budget, recently questions have been rising about their effectiveness. To what extent the Structural Funds have succeeded in their objective of reducing disparities between the levels of development of the various regions? Do they help the Member States in achieving greater economic and social cohesion and in reducing the gap between the centre and the periphery of the European Union?

Instead of looking at from country level, when we look at from the regional level the picture is slightly different. There are two factors behind these doubts in that sense. First comes the remarkable stability of the regions eligible for Objective 1, as 43 of the original 44 regions that qualified for the Objective in 1989 remain in it 14 years after the reform. Only Abruzzo in Southern Italy managed to come out at the end of 1997. Four other original regions (Corsica, Lisbon and the Tagus Valley, Molise, and Northern Ireland), plus parts of the Republic of Ireland, were phased out of the Objective and lost their support at the end of 2006. The second factor behind the scepticism over the capacity of European regional policies to deliver has been the lack of convergence across European regions since the implementation of the reform of the Structural Funds²⁹.

Empirical Studies on the Effectiveness of Structural Funds

Several studies have been conducted to analyse the relation between European structural policy and convergence of member states by economists. Some of them are negative on convergence within the European Union, but some of them have positive findings on convergence. There are some conflicting views in that sense. In this last part we will review some of these studies and the empirical findings.

Barro and Sala-i Martin (1991, 1992) studied income convergence across countries in a neoclassical framework by using the concept of β convergence³⁰. In the analysis of convergence, β and σ convergence concepts are important. The simplest indicator for assessing convergence between countries or regions within an area is to test whether the relative per capita GDP of a country or region has approached the average of the area. The two most popular measures are the β -convergence and σ -convergence in that sense. β -convergence occurs where there is a negative correlation between initial levels of real GDP per capita and its average annual growth rate. This implies that the poor countries grow faster than the richer ones and it is generally tested by regressing the growth in per capita GDP on its initial level for a given cross-section of countries. According to this, if a country starts with a lower income per capita compared to the average, it can have a higher income relative to other countries after T period. This is called as catching up. After controlling for other

²⁹ Rodriguez-Pose ve Fratesi, "Between Development and Social Policies: The Impact of European Structural Funds in Objective 1 Regions", p.99.

³⁰ Robert, J. Barro ve Sala-i Martin, "Convergence Across States and Regions", *Brookings Papers in Economic Activity*, No:1, 1991, pp 107-182, Robert, J. Barro ve Sala-i Martin, "Convergence", *Journal of Political Econ.* **100** (2), 1992, pp 223-251.

variables, if the negative relationship still holds, in that case conditional β -convergence takes place³¹. Another widely used convergence concept is σ -convergence. This concept means that the dispersion of real per capita income tends to decline over time³². In their analyses Barro and Sala-i Martin measured the β -convergence. According to their empirical results, poor countries tend to catch up with rich countries if the poor countries have high human capital per person. In their common study, their empirical results document the existence of convergence in the sense that economies tend to grow faster in per capita terms when they are further below the steady state position³³.

Another empirical research was done by Boldrin and Canova in 2001. They analysed the impact of the structural policies on the income disparities between countries and region for the period 1980-1996. They found some opposite results of those by Barro and Sala-i Martin. Their result is negative on convergence within the European Union. According to their results, there is no real tendency for the regional per capita income to grow to their central base of attraction. The gap between the upper and the lower part of the distribution did not really change over time. They claim that, "regional and structural policies serve mostly a redistributive purpose, motivated by the nature of the political equilibria upon which the European Union is built. They have little relationship with fostering economic growth. A successful European Union enlargement calls for an immediate and drastic revision of regional economic policies"³⁴.

Martin (1999) argues that, regional policies face a trade-off between equity and efficiency at the spatial level. According to him, if the existence of positive localised spillovers and of returns to scale explain the phenomenon of self sustaining agglomeration, then agglomeration must have some positive efficiency effects. He also argues that because infrastructures financed by regional policies have an impact on transaction costs and therefore on the location decision of firms, the long term effect of certain regional policies may be unexpected and unwelcome. In this analysis, it is claimed that policies that reduce agglomeration may then also reduce efficiency and growth³⁵.

³¹ Beta convergence covers two types of convergence: absolute and conditional (on a factor or a set of factors in addition to the initial level of per capita GDP); for more information see Barro and Sala-i Martin (1995).

³² Maaik Beugelsdijk ve Sylvester Eijffinger, "The Effectiveness of Structural Policy in the European Union: An Empirical Analysis for the EU 15 in 1995-2001", **Journal of Common Market Studies**, Volume 43, Number 1, 2005, p.39.

³³ Barro ve Martin, "Convergence Across States and Regions", p. 107-182, Barro ve Martin, "Convergence" p. 223-251.

³⁴ Michele Boldrin ve Fabio Canova, "Inequality and Convergence in Europe's Regions: Reconsidering European Regional Policies, **Economic Policy**, No 16, April, 2001, p.207-253.

³⁵ Philippe Martin, **Are European Regional Policies Delivering?**, CEPR Discussion Series, 1999.

In another analyse, building on a standard neoclassical growth framework, Ederveen, Groot and Nahuis (2002) find that European support did not improve the countries' growth performance. However, they reach some evidence that it enhances growth in countries with the "right" institutions³⁶.

Crespo-Cuaresma, Dimitz and Grünwald (2001) performed an empirical study to detect if the European Union membership has a convergence-stimulating effect on long term growth. In this study, European membership is found to have a significant positive and asymmetric effect on long term economic growth. On the other hand, results of this study show that, relatively less developed countries profit most from access to the broader technological framework supplied by the regional integrated unit³⁷.

Beugelsdijk and Eijffinger (2005) studied empirically on the effectiveness of structural policy in the European Union for the old 15 member states. In this study, convergence of the old Member States was tested for the period 1995-2001 by touching on the problem of moral hazard. They conclude that, structural funds do indeed appear to have had a positive impact and poorer countries like Greece appear to have caught up with the richer countries. Secondly, according to their results, users of structural funds in some cases are not really eligible and may therefore use the funds inefficiently³⁸.

Bradley (2004) emphasizes the importance of taking account of other factors; research suggests that the direct impacts of the Structural Funds in isolation are modest, and that the real, long-term benefits of EU Cohesion policy are associated with the responsiveness of lagging economies to external opportunities for trade and investment³⁹.

Ville Kaitila (2004) researched convergence in GDP per capita levels adjusted for purchasing power in the European Union 15 area for the period 1960-2001. In this study, at first, he analyses both β and σ convergence in context of European Union membership, foreign trade and investment and than uses this results in discussing the developments in the Poland, the Czech Republic, Slovakia, Hungary, Estonia, Latvia and Lithuania during the last decade. There are two periods which convergence occurs in this long period. Convergence takes place in 1960-1973 and 1986 and 2001. There is an interim period of stagnation between these years. Stagnation period is explained by the first oil crisis and decline in investment rates. According to Kaitila, the

³⁶ Sjeef Ederveen, Henri L.F. Groot ve Richard Nahuis, **Fertile Soil for Structural Funds?: A Panel Data Analysis of the Conditional Effectiveness of European Cohesion Policy**, CPB Discussion Paper, No: 10, August 2002.

³⁷ Jesus Crespo-Cuaresma, Maria Dimitz ve Doris Ritzberger-Grünwald, **Growth, Convergence and EU Membership**, Österreichische Nationalbank, Working Paper Series, 2001.

³⁸ Beugelsdijk ve Eijffinger, "The Effectiveness of Structural Policy in the European Union : An Emprical Analysis for the EU 15 in 1995-2001", p.37-51.

³⁹ John Bradley ve Edgar Morgenroth, **A Study of the Macroeconomic Impact of the Reform of EU Cohesion Policy**, Economic and Social Research Institute, Dublin, 2004.

developments in the EU 15 countries are a good indicator of the future economic development of the accession countries⁴⁰.

According to the evaluation research reported in the Third Cohesion Report, GDP in real terms at 1999 was between 2.2 and 4.7 per cent higher than it would otherwise have been in the four EU-15 Cohesion countries: Greece, Spain, Ireland and Portugal⁴¹. The Commission claims that the Structural and Cohesion Funds do not only stimulate demand by increasing income in the regions assisted. By supporting investment in infrastructure and human capital, they also increase their competitiveness and productivity and so help to expand income over the long-term.

All these empirical findings on economic convergence within the Union reflect a very different picture depending on whether one looks at the 15 Member States or at the more than 200 administrative regions across the Union. If we look at for the period 1980-2000, there is a tendency of per capita GDP to converge at the Member State level. In this period, initially low income countries grew faster, on average, than high income ones. However, when we look at convergence in terms of within each country, we see that the picture is different. Within each country, GDP levels have tended to diverge across regions, increasing inequalities⁴².

Table 4: GDP Growth Rates (in percent)

	1980-1990	1991-2000	1991-1995	1995-2000
6 macro regions	2,6	3,3	2,8	3,7
Rest of Europe	2,3	1,9	1,3	2,4
EU-15	2,4	2,1	1,5	2,6

Source: Sapir Report, p. 60

Table 5: Index Per Head (GDP/head in PPS)

	1980	1990	1995	2000
6 macro regions	69,3	70,7	73,5	76,8
Rest of Europe	109,5	109,1	109,9	108,7
EU-15	100	100	100	100

Source: Sapir Report, p. 60

⁴⁰ Kaitila, *Convergence of Real GDP per capita in the EU 15*.

⁴¹ European Commission, *A New partnership for Cohesion: Convergence, Competitiveness, Cooperation, Third Report on Economic and Social Cohesion*. Office for Official Publications of the European Communities, Luxembourg, 2004.

⁴² Andre Sapir & et. al., *An Agenda For a Growing Europe*, July 2003, p.59.

In that sense, findings indicate that both “country convergence” and “region divergence” is experienced within the Europe. An important share of the cohesion funds (68% of total funds) are sent to six macro regions: Greece, Spain, Ireland, Portugal, the six eastern German Lander and the Mezzogiorno in Italy. In terms of convergence of these macro regions, their average GDP did converge. This is true both for β and σ convergence. These regions displayed annual growth of 3.3% between 1991 and 2000. In that period, rest of the European Union produced annual growth of 1.9%. On the other hand, the Italian Mezzogiorno didn't converge, while Spain, Portugal and Greece grew only slightly faster than the European Union average. Ireland converged very impressively by moving from the bottom group of the poorest four European Union countries to become one of the top four in terms of GDP per capita⁴³.

Conclusion

Like today's new member states, all potential new member states in the future will still be relatively poor at the time of their accession. For this reason, probably all of them will be eligible for structural assistance which in turn increases European Union expenditure significantly. Therefore, the structural funds and the Union's regional policy will continue to be one of the key elements of enlargement.

In the light of above, it is not possible to answer the key question in a certainty of to what extent the structural assistance will improve the competitiveness of peripheral regions in the long term and whether they will have lasting positive effects after the transfers will have come to the end.

However, most of the empirical results and the economic situation of some of the old member states benefiting from the structural funds show that, the importance of structural funds can not be neglected. This means that channelling an important part of the funds to new and candidate countries in 2007-2013 period will probably contribute to higher economic growth rates in these countries. We can say that the structural funds will be an important helping hand for the new member states if the microeconomic and macroeconomic conditions in these countries are favourable to economic growth. On the other hand, we should keep in mind that, successful use of these funds will require appropriate and efficient institutional framework in the recipient states.

⁴³ *Ibid.*, p.59-60.