



EU Regional Policy. Realities and Perspectives on the Absorption of European Funds

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ARTICLE INFO

Article history:
Accepted June 2012
Available online 1 August 2012
JEL Classification
E61, F02, F15, P47

Keywords:
Regional policy; Cohesion policy;
Disparities; Economic growth;
Competitiveness

ABSTRACT

EU expansion to 27 Member States has generate challenges in terms of its competitiveness and internal cohesion. The already existing disparities between the Member States and among their regions have deepened. These disparities are generated by the structural deficiencies in key factors of competitiveness, i.e. inadequate endowment with physical and human capital (infrastructure and workforce), insufficient capacity for innovation, business support and low level of environmental capital (natural environment and / or urban pollution). The purpose of the paper is to determine whether the cohesion policy reduced or increased the disparities between regions. Therefore in order to achieve this goal of the cohesion policy, the Member States and regions need significant financial help to solve various structural problems and achieve their potential of growth.

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1. Introduction

Tackling the issue of regional disparities in economic growth stirs up lengthy discussions due to the various ways of defining the regional growth. The most common refer to the increase of the total output of a region, output increase per employed person, output increase per capita. In turn, the output can be assessed by the total (gross) production of a region, the region's gross domestic product or net domestic product of that region.

It is very important the way regional growth is defined because, according to this definition, different conclusions can be drawn about the real situation of a region's economy. For example, a region may show, at the same time, a small increase of total output and a rapid increase in output per capita if the process of emigration from those particular region records significant levels during the period the study is conducted [Jan Timbergen 1965].

Thus:

- increase in total output is used as an indicator of the productive capacity increase of a region, which partly depends on the extent to which that particular region attracts capital and labor force from other regions;
- increase in output per employed person is often used as an indicator of the changes occurred in regional competitiveness due to the productivity increase;
- increase in output per capita indicates changes occurred in the economic welfare of that region.

Therefore none of these measures can be regarded as the best, each of them is useful in its own way.

Another controversial issue related to disparities in regional growth refers to the medium to long-term vision upon the consequences of regional growth. According to the neoclassical model, which emphasizes the role of the supply, the regional economic growth leads to convergence in economic and social development of regions. On the other hand, in the vision based on the models of post-Keynesian approach of demand (model based on export potential, the cumulative causes model), the regional economic growth emphasizes the divergence.

Regional growth-related theories have evolved gradually, marked at the beginning by the opinion according to which regions had been regarded as non-spatial elements of the national economy, later on space was taken into consideration explicitly.

In the first category the following models are included: the neoclassical model (based on the principles issued by Marshall), the model of cumulative causation [Myrdal 1957], the model based on export potential [Bolton 1987], econometric models [Czamanski 1964], [Klein 1955] [Harris 1970], input-output models [Leontief 1966], [Richardson 1970].

As an alternative perspective to the traditional models, recognizing the spatial component importance can be seen in theories and models such as:

- the center peripheral model and that of the development corridors [Friedman 1966];
- spatial variants of the growth poles theory [Boudeville 1966];
- analysis of the influence of congestion and the "hinterland" effects on the size and distance of urban areas [Böventer 1963];
- discussing the role of transport and polarizing forces in regional growth [Siebert 1969];
- development axes theory [Pottier 1963];
- analysis of the spatial diffusion of innovations. [Hägerstrand 1967]

As a consequence of the comparative approach of the two major trends, a widely-discussed theory resulted, whose practical implications are obvious in the field of regional policy. It refers to the competitive or generative character of the regional growth.

Competitive growth models imply that the possible rate of the national economic growth is known and that it examines the forces that determine the way in which the given rate of the economic growth between regions of the system will be distributed. In these models, the growth of a region will always take place at the expense of the other. Many of the traditional theories on regional growth (cumulative causality, neoclassical theory, etc.) belong to the category according to which regional growth is regarded as a competitive growth. The national growth rate is determined exogenously and regional economic analysis function is only to distribute this growth between regions. The need to include these spatial variable models is very low since every region is treated as if it were an economic sector.

Nevertheless, according to the generative growth models, the regional dimension is much more emphasized. This type of models considers that the national economic growth rate is a result of the growth rates of the regions. In this view the entire increase is spatially oriented, i.e. the increase in any part of the national economy is based on a particular location. The growth performance of a region can be improved without inducing any adverse effects on the growth rates of neighboring regions. Thus the increase induced by the innovation process can be included in this context: congestion and spatial proximity of activities in certain cities or regions may induce innovation rates higher than the one that would be recorded in the absence of congestion. Similarly, changes that may occur in intra-regional distribution of production factors, facility, for instance, by an efficient intra-regional transport system, can also increase production efficiency and regional growth rates.

The importance of this spatial impact on regional growth is overlooked when dealing with models that are focusing on competitive growth. This particular phenomenon, in which intra-regional spatial efficiency of a region can have a feedback effect upon the rate of aggregate economic growth, is called generative growth.

The importance of this dichotomy, besides highlighting the fact that the spatial distribution of resources within the national economy has a significant impact on dynamic efficiency, consists of focusing on intra-regional efficiency to a greater extent than the inter-regional efficiency. Thus while the competitive growth models advocate for the idea that if the production factors are distributed efficiently across regions (achieving, for example, a balance of profitability), the economic growth rate should be maximum, the generative models reinforce the need for commitment to stimulate favorable conditions for economic growth within each region, rather than to divert the resources from other uses which are possibly even more productive, in other regions.

2. Efficiency versus equity in regional economic growth

According to this model, regional policy objectives can be reduced to only two, namely [Constantin 2010]:

1. Maximizing the economic growth on the national economy level (efficiency);
2. Reducing interregional disparities in terms of income, welfare and economic growth of regions (equity).

The classical analysis of the regional growth and of the corresponding regional policies refers to the possibility of working out the conflict between efficiency and equity. If the low-income regions provided the prospect of a higher efficiency of capacity use, these purposes would not be opposed to each other. However the agglomeration economies, market opportunities and other factors are in favor of richer regions. Therefore, a series of "compensations" should be accepted between efficiency and equity.

A primordial purpose can be selected that should usually be maximized, while the other purpose will be treated as a restriction. For instance, in a simplified economy with two regions, with efficiency being the dominant purpose, the model of decision at national level will be the following:

$$\begin{cases} \max y_n \\ \frac{Y_{r1}}{Y_{r2}} \geq \bar{Z} \end{cases}$$

in which: y_n = national income increase ratio; Y_{r1} and Y_{r2} = income level of the two regions, $Y_{r1} < Y_{r2}$; \bar{Z} = minimum accepted ratio of inequity.

If equity at regional level is the primordial purpose, the model will be the following:

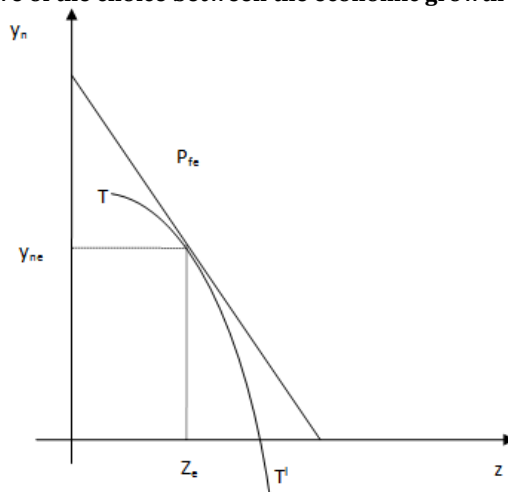
$$\begin{cases} \max \bar{Z}_n \\ y_n \geq \bar{y}_n \end{cases}$$

Where \bar{y}_n = minimum accepted rate of economic growth;

Z_n = minimum accepted ratio of inequity in regions.

It is not necessary to accomplish a hierarchy of the two purposes or to adopt the hypothesis of the linear programming problems. A less restrictive approach is to achieve an indifference curve between alternative rates of economic growth and regional equity index. Thus in a simplified manner, it is assumed that every growth rate implies certain interregional distribution. In fact, there are many alternative interregional distributions that can lead to the same rate of economic growth.

Figure no. 1. The indifference curve of the choice between the economic growth and interregional equity



Source: Daniela-Luminița Constantin Regional economy. Theories, models, policies. Ed. ASE, București 2010

An indifference curve of this type is shown in Figure 1. However, the shape of the TT' curve is not certain. Normally z , the equity index is expected to be inelastic with respect to changes displayed in the growth rate, y_n . This is due to the fact that regional income convergence can be achieved, but very slowly due to persistent differences in regional growth rates over a long period of time and not due to short-term reallocation of resources. Although the curve can be drawn starting from statistical observations on the economic growth rate and of equity index, there are however certain risks in its use for forecasting and planning purposes. Another problem is that national development programs horizon is much narrower than the corresponding one, which is more appropriate for regional policies and programs.

The optimal point is reached where the highest of preference functions (P_{fe}) is tangent to TT' . It offers the optimal combination between the economic growth rate (Y_{ne}) and regional equity index (Z_e).

3. Regional Policy and European funds

EU expansion to 27 Member States has raised challenges in terms of its competitiveness and internal cohesion. The already existing disparities between the Member States and among their regions have deepened. These disparities are generated by the structural deficiencies in key factors of competitiveness, i.e. inadequate staff with physical and human capital (infrastructure and workforce), insufficient capacity for innovation, business support and low level of environmental capital (natural environment and / or urban pollution).

Table 1. IMF forecasts for Europe on economic growth

	Growth rate				Forecast
	2008	2009	2010	2011	2012
Europe	1.4	-4.5	2.4	2	0.2
European countries with advanced economies	0.4	-4.0	1.7	1.4	-0.3
Emerging economies	4.2	-5.9	4.2	5.3	1.9
Euro zone	0.4	-4.1	1.7	1.6	-0.3
France	0.1	-2.5	1.5	1.6	0.5
Germany	0.7	-4.7	3.5	2.5	0.6
Hungary	0.8	-6.7	1.2	1.7	0
Italy	-1.3	-5.2	1.3	1.1	-1.9

	Growth rate				Forecast
	2008	2009	2010	2011	2012
Poland	5.1	1.7	3.8	3.8	2.6
Romania	7.3	-7.1	-1.3	1.5	1.5
Russia	5.2	-7.8	4.0	4.8	4
Spain	0.9	-3.7	-0.1	0.8	-1.8
Sweden	0.8	-4.8	5.8	4	0.9
Switzerland	1.9	-1.9	2.6	2.4	0.8
Turkey	0.7	-4.7	8.2	4.6	2.3
Ukraine	1.9	-14.8	4.2	4.5	3
Great Britain	-0.1	-4.9	1.3	1.7	0.8

Source: IMF, World Economic Outlook

The cohesion policy aims to reduce the disparities between EU regions. In order to achieve this goal of the cohesion policy, the Member States and regions need significant financial help to solve various structural problems and achieve their potential of growth.

The regional policy (or cohesion) of the European Union promotes economic prosperity and social cohesion in all its 27 Member States and in the 271 NUTS2 regions. In the current financial year, the budget for regional policies works out at 347 billion euros over a period of seven years, which is more than one third of the overall EU budget for this period. Regional policy spending is channeled through three funds - often called "structural funds". These are the European Regional Development Fund (ERDF), the European Social Fund (ESF) and the Cohesion Fund (CF).

According to the *acquis communautaire*, each Member State has to draw up a National Strategic Reference Framework (NSRF) as a reference document for programming Structural and Cohesion Funds.

The National Development Plan (NDP) is the strategic planning document and multiannual financial programming, which aims to guide and stimulate economic and social development of a country in order to accomplish the objective of achieving economic and social cohesion.

The Structural Funds contribute to three strategic objectives of the Economic and Social Cohesion Policy of the European Union:

1. **Convergence or diminish of the development discrepancies between regions.** States may apply for funding for the regions that have a GDP/capita below 75% of the European average (NUTS areas level II). It is financed by the ERDF, ESF, Cohesion Fund.
2. **Regional competitiveness and employment.** States may apply for funding for the regions that are not eligible for the Convergence Objective. It covers NUTS areas level III (county-level) or less, including socio-economic areas in industrial and service sectors, declining rural areas, urban areas in difficulty and areas that are dependent on fisheries. It is financed by the ERDF and ESF.
3. **European territorial cooperation.** Thematic objective to support adaptation and modernization of policies and systems of education, training and employment of labor. It covers NUTS areas level III (county-level) that are internal EU borders as well as certain external borders. It is financed by the ERDF.

Integration of Central and Eastern countries in EU assumes obtaining certain benefits. Upon joining the EU internal market and free movement of labor, absorption of EU funds could help the convergence go on and reduce disparities between countries.

EU integration requires promoting radical reform in economic and social areas, expanding transfer of modern technologies, through trade and foreign direct investment, increased labor mobility, including highly skilled, administrative and institutional reform.

An efficient use of structural funds is generally conditional on the quality of governance and public administration. One of the reasons that obstruct reducing disparities and achieving convergence is the inefficient use of structural funds by recipient countries, by using untrained personnel in public institutions directly involved, allocation of EU funds in areas with low economic impact, use of inappropriate government policies.

The absorption capacity is the extent to which a Member State may spend the financial resources granted from structural and cohesion funds in an efficient and effective manner. The absorption capacity in terms of demand refers to the real capacity of applicants who submit projects. Concerning the supply side, the absorption capacity may be determined by the following three main factors:

- macroeconomic absorptive capacity, defined and assessed as GDP;
- financial absorptive capacity, defined as the capacity of co-financing programs and projects supported by the EU, of planning and guaranteeing these national contributions in multi-annual budgets as well as collecting the contributions from the partners involved in various programs and projects;
- administrative capacity, which lies in the central and local authorities ability and qualifications to prepare appropriate programs and projects, to take decisions concerning these projects and programs, to ensure coordination of the involved partners, to meet administrative and reporting requirements, to fund and monitor the implementation of programs and projects and to avoid irregularities.

Table 2 Cohesion Policy 2007-2013: Financial allocations (mil. EURO)

	Cohesion Fund	Convergence	Regional Competitiveness and Employment	European Territorial Cooperation
Belgium			1425	194
Bulgaria	2283	4391		179
Czech Republic	8819	17064	419	389
Denmark			510	103
Germany		11864	9409	851
Estonia	1152	2252		52
Greece	3697	9420		210
Spain	3543	21054	3522	559
France		3191	10257	872
Ireland			293	151
Italy		21211	5353	846
Cyprus	213			28
Latvia	1540	2991		90
Lithuania	2305	4470		109
Luxembourg			50	15
Hungary	8642	14248		386
Malta	284	556		15
Netherlands			1660	247
Austria			1027	257
Poland	22176	44377		731
Portugal	3060	17133	490	99
Slovenia	1412	2689		104
Slovakia	3899	7.013	449	227
Finland			1051	120
Sweden			1626	265
Great Britain		2.738	6014	722
Romania	6552	12.661		455
Interregional				445
Technical Assistance				
Total	69578	199322	43556	8723

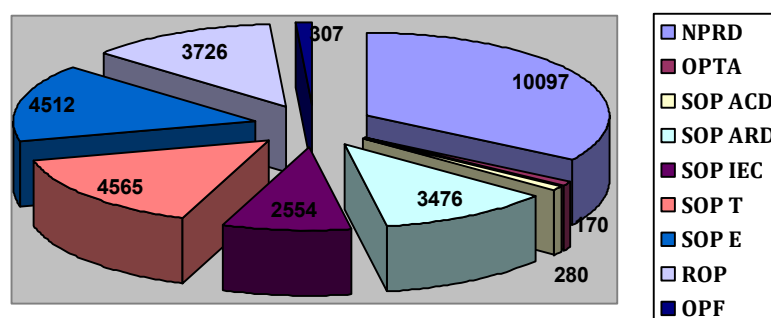
Source: http://ec.europa.eu/regional_policy/policy/fonds/pdf/annexe-recto.pdf

The Member States whose average GDP per capita (PPS) between 2001 and 2003 was less than 40% of the EU-27 average are entitled to receive transfers of Structural Instruments of maximum 3.7893% of their GDP.

The entire territory of Romania is eligible under the "Convergence" objective, taking into account that GDP per capita in each NUTS II region is less than 75% of the EU-25. Romania receives funding within the "European Territorial Cooperation" Objective as well, for actions of transborder, transnational and interregional cooperation. As a Member State whose GNP per capita (PPS) is less than 90% of the EU-25 average, Romania benefits from the Cohesion Fund.

The total amount of Structural and Cohesion Funds allocation for Romania for 2007-2013 works out at 19.668 billion euro, out of which 12.661 billion Euros represent the Structural Funds within the "Convergence" Objective, 6.552 billion euro are allocated through the Cohesion Fund and 0.455 billion euro are allocated to the "European Territorial Cooperation" Objective.

Figure 2. Budgetary allocations during 2007-2013



Source: data from eufinantare.info

There are several main factors that contributed to the current absorption funds in Romania: this is the first exercise of accessing European funds at the national level (except SAPARD during pre-accession period), there are different rules applied by the management authorities, the analysis/selection of the eligible projects is often a very slow process, the eligibility criteria do not always match the bank's specific requests, some of the consulting companies are interested mainly in the approval of the project and not in the implementation of the respective project, and last but not least, the economic and financial crisis delayed some of the private initiative.

4. Conclusions

Study of theories on regional development is an important aspect, a starting point for further observation of different trends. Any balanced spatial structure is the result of progressive development. Regional disparities and North-South dualism is typical of initial stages of development, followed by regional convergence and reducing disparities. The growth stages, with large discrepancies in the beginning and subsequent reduction, is widespread in regional policy. Growth was not only the result of interaction of a limited number of economic, social or political factors, but also the consequence of a process in which social, political and cultural factors, together with economic factors. When capital and technology become mobile and traditional economic factors can not explain how and why economic activity flourishes in some areas and stagnant in others, the explanation lies in the social, political and cultural environment. This helps us to explain why, despite profound changes, long-term growth trends suffer only minor alternations, and economic disparities tend to persist. Regional economic policy addresses different regions within a country. Apart from purely economic arguments, there can be distinguished social, political and environmental factors. Economic reasons are usually considered as the most important and are quite numerous, but their relative importance varies, however, from country to country, depending on local circumstances.

The most immediate policy challenge is to restore confidence and put an end to the crisis in the euro area by supporting growth, while sustaining fiscal adjustment, containing deleveraging, and providing more liquidity and monetary accommodation. Product and labour market reforms can boost productivity, and they are paramount in economies with competitiveness problems and internal or external imbalances. When implemented, they can support market confidence and the sustainability of fiscal positions.

Banks need to increase their capital to restore financial markets' confidence in their ability to weather the downturn. Wherever possible, this should be done by raising capital from private sources, but public funding should be available for this purpose when needed. In other major advanced economies, the key policy requirements are to address medium-term fiscal imbalances and to repair and reform financial systems, while sustaining recovery. In emerging and developing economies, near-term policy should focus on responding to moderating domestic growth and to slowing external demand from advanced economies. For the moment, the focus should be on measures that increase demand. Looking forward, however, the focus should also be on measures that increase potential growth. A better absorption of EU funds can lead to growth and economic development and thus reduce regional economic disparities. The objective to absorb as much financial support as possible within this context requires continuous efforts from the Member States and also regional and local government involvement in every stage of the process.

ACKNOWLEDGEMENTS

This paper of Valentin Neculita was supported by Project POSDRU - Quality and continuity of training in the doctoral cycle - TOP ACADEMIC 107/1.5/S id 76822

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