



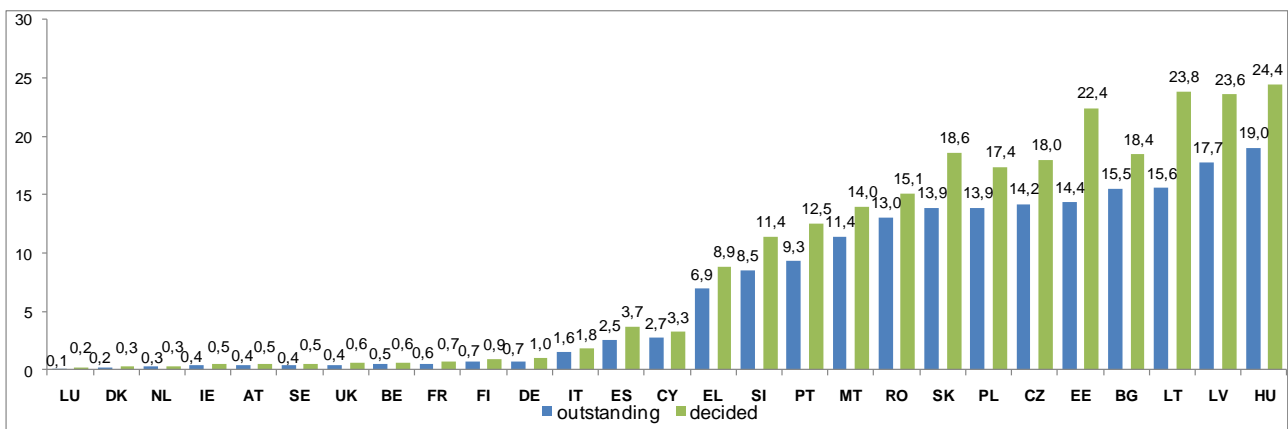
A EUROPEAN FUND FOR ECONOMIC REVIVAL IN CRISIS COUNTRIES

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Highlights

- Structural and Cohesion Funds that have been pre-allocated but remain undisbursed or uncommitted are significant in size. In Portugal they amount to 9.3 percent of GDP, in Greece close to 7 percent and to about 15 percent of GDP in the New Member States (NMS). They should be part of a temporary European Fund for Economic Revival (EFER) for 2011-2013 that promotes economic growth in crisis countries and facilitates the passage of structural reform.
- Especially in countries under financial assistance, the European Commission has a role to play in identifying the 'right' objectives for which the funds shall be used. All the DGs in close cooperation may decide to manage the funds directly with the support of an executive agency.
- Stronger effort should be also put into exploiting synergies between EU grants and EIB loans, allowing EIB loans to finance the total costs of a project or programme in small countries, and leveraging the whole EU Budget to attract private investment.

CHART 1: TOTAL AND OUSTANDING COMMITMENTS FROM MFF 2007-2013 (AS OF END 2010), % OF GDP



Source: Bruegel's own calculation based on European Commission data.

1. INTRODUCTION

Over the 2011-2013 period Greece has still to absorb Structural and Cohesion Funds in the order of 7 percent of GDP, Portugal about 9.3 percent of GDP, the New Member States (NMS) come close to an average of 15 percent of GDP (see Chart 1)¹. In the current debate on the European crisis, insufficient attention is being paid to the possible use of these immense resources for crisis management and resolution. They could in fact serve three purposes: i) compensate for the recessionary impact of fiscal consolidation, whether countries have received financial assistance and are thus under strict conditionality (ie Greece, Hungary, Latvia, and Romania) or are indeed consolidating to avoid having to recourse to financial assistance (eg Portugal and Spain); ii) preserve essential public investment in infrastructure, human capital and research and thereby promote potential output growth; and facilitate the passage of structural reform in countries that are under strict conditionality.

This policy contribution builds on two key messages concerning the role of EU funds in bad times. The first one is that the size of Structural and Cohesion Funds has been so far underestimated and that the numbers are indeed far from trivial². The second message is that the reason why their full potential remained unexpressed for so long relates to issues of governance. The empirical support for positive effects from EU transfers is weak not necessarily because they are too small to make a difference but because they have been poorly and badly absorbed in the individual EU member states³. We suggest that the governance of EU grants needs reformed by revising their objectives and delivery even contemplating, for certain types of projects, that the funds are directly administered by the European Commission with the support of an executive agency.

Section 2 describes the size of Structural and Cohesion Funds under the current multiannual financial framework (MFF) of 2007-2013. Section 3 looks at their absorption compared with the previous programming period of 2000-2006. Section 4 looks at the general issue of governance addressing the questions of absorption, objectives and delivery. Section 5 briefly considers the role of loans granted by the European Investment Bank (EIB) compared with EU grants. Section 6 offers some concluding remarks.

2. THE SIZE OF EU FUNDS

The current MFF running from 2007 to 2013 allocates to EU27 a total of about 348bn EUR under heading 1B of the EU Budget, equal to 2.8 percent of EU GDP or 0.4 percent per year on average. The standard argument is that, due to their size, EU funds are not as powerful an instrument for resource allocation as the national budget of a federal State. This is but the wrong way to look at Structural and Cohesion Funds. First, the EU is not a proper federal system, hence the comparison is unwarranted. Second, EU support for cohesion represents a significant amount when compared, for example, with the size of the rescue packages to Greece (110bn EUR) and to Ireland (85bn EUR). Third, Marshall Plan aid from 1948 to 1951 was only about 2 percent of the GDP of all recipient countries but made a substantial contribution to Western European growth by altering the political economy environment⁴. If their objectives are clarified and their delivery is somehow improved and reformed, Structural and Cohesion Funds can offer an important contribution to growth and convergence that goes well beyond their face value.

¹ We measure total outstanding commitments as the sum of the outstanding for each year as a proportion of that year GDP. For 2011 and 2012, we use the GDP forecasted by the European Commission and for 2013 our own estimate.

² On the other hand, the EU Budget as a whole has played an important but mostly unnoticed role in the current crisis. The European Financial Stabilization Mechanism (EFSM) is an extension of the existing medium-term financial assistance (MTFA) in favour of non euro area member countries to the euro zone and sees the EU Commission borrowing up to 60bn EUR on capital markets under implicit EU Budget guarantee.

³ On the economic impact of Structural and Cohesion Funds, see Section 4.

⁴ See De Long and Eichengreen [1991].

All the funds are pre-allocated country by country on the basis of the recipient's level of economic development, population size and area surface and subject to the submission of so-called Operational Programmes (OPs). Table 1 shows national commitment appropriations between 2007 and 2013, as agreed at the beginning of the programming period. Table 2 displays commitment appropriations as a proportion of the receiving country's GDP per year. The column for total is the simple sum of each year's allocations over the entire programming period. Put this way, the figures show the strong distributional component of Structural and Cohesion Funds, with in fact the NMS, Greece and Portugal receiving higher amounts of funds relatively to the size of their national economy than the other EU member states.

TABLE 1: PRE-ALLOCATED STRUCTURAL AND COHESION FUNDS UNDER THE MULTIANNUAL FINANCIAL FRAMEWORK 2007-2013 (MILLIONS OF EUR)

<i>EUR million</i>	2007	2008	2009	2010	2011	2012	2013	TOTAL
BE	364.8	355.1	338.9	324.0	308.4	292.0	274.7	2,257.9
BG	514.2	737.4	991.8	1,044.1	1,116.2	1,188.6	1,260.6	6,852.9
CZ	3,062.7	3,736.7	3,640.9	3,809.5	4,057.2	4,225.3	4,396.4	26,928.7
DK	82.2	83.9	85.6	87.5	89.4	91.3	93.2	613.0
DE	3,664.8	3,696.9	3,729.7	3,763.1	3,796.3	3,828.5	3,860.5	26,339.8
EE	375.8	410.0	446.4	486.2	530.4	578.2	628.8	3,455.8
IE	211.6	180.7	148.5	115.0	80.1	81.8	83.5	901.4
EL	3,081.8	3,030.4	2,965.7	2,900.5	2,831.9	2,814.5	2,795.0	20,419.8
ES	6,286.2	5,754.6	5,190.3	4,713.8	4,449.8	4,426.4	4,395.8	35,217.0
FR	1,903.7	1,979.6	2,002.0	2,043.8	2,086.9	2,129.8	2,173.1	14,318.9
IT	3,926.5	4,107.2	4,066.8	4,098.6	4,132.6	4,204.6	4,275.4	28,811.8
CY	167.2	139.4	109.8	79.1	47.2	48.1	49.1	640.0
LV	506.3	554.2	603.9	655.7	710.4	766.4	823.6	4,620.4
LT	765.4	833.4	902.5	975.2	1,053.3	1,136.2	1,219.0	6,885.0
LU	8.8	8.9	9.1	9.3	9.5	9.7	9.9	65.3
HU	3,034.1	3,229.3	3,437.7	3,625.5	3,785.2	3,991.5	4,204.1	25,307.4
MT	112.9	118.7	119.8	122.6	125.1	127.2	129.1	855.4
NL	254.1	262.4	266.4	272.2	278.1	283.9	289.9	1,907.0
AT	201.8	204.0	206.3	208.7	211.1	213.5	215.8	1,461.1
PL	8,115.6	8,664.5	9,213.7	9,441.4	10,241.1	10,822.8	11,417.5	67,916.6
PT	2,971.5	3,005.0	3,038.7	3,072.6	3,106.7	3,140.8	3,175.0	21,510.6
RO	1,328.9	1,915.6	2,576.3	3,092.0	3,333.6	3,583.4	3,837.9	19,667.6
SI	554.6	569.3	584.5	600.0	615.9	632.2	648.9	4,205.3
SK	1,299.1	1,407.2	1,526.1	1,662.3	1,831.4	1,953.1	2,046.5	11,725.6
FI	259.8	257.6	251.9	245.9	241.1	234.4	225.7	1,716.2
SE	253.2	259.1	264.4	269.9	276.0	281.6	287.1	1,891.3
UK	1,593.6	1,598.7	1,533.5	1,489.3	1,442.8	1,465.9	1,489.3	10,613.2
TOTAL	45,061.0	47,266.8	48,427.2	49,393.5	50,985.5	52,759.6	54,523.6	348,417.2

Note: Allocations per Member State include all possible items under convergence, cohesion, regional competitiveness & employment and territorial cooperation, financed under the ERDF, ESF & Cohesion Fund. Bold = n+3 countries.

TABLE 2: PRE-ALLOCATED STRUCTURAL AND COHESION FUNDS UNDER THE MULTIANNUAL FINANCIAL FRAMEWORK 2007-2013 (% GDP)

% GDP	2007	2008	2009	2010	2011	2012	2013	Total□
BE	0,11	0,10	0,10	0,09	0,08	0,08	0,07	0,64
BG	1,67	2,08	2,83	2,91	2,96	2,96	3,02	18,43
CZ	2,41	2,53	2,65	2,60	2,60	2,58	2,60	17,98
DK	0,04	0,04	0,04	0,04	0,04	0,04	0,04	0,26
DE	0,15	0,15	0,16	0,15	0,15	0,14	0,14	1,04
EE	2,37	2,55	3,22	3,43	3,49	3,60	3,76	22,41
IE	0,11	0,10	0,09	0,07	0,05	0,05	0,05	0,53
EL	1,37	1,29	1,27	1,26	1,25	1,22	1,19	8,86
ES	0,60	0,53	0,49	0,45	0,42	0,40	0,39	3,27
FR	0,10	0,10	0,10	0,10	0,10	0,10	0,10	0,72
IT	0,25	0,26	0,27	0,26	0,26	0,26	0,26	1,82
CY	1,05	0,81	0,65	0,45	0,26	0,25	0,25	3,72
LV	2,40	2,41	3,26	3,68	3,84	3,94	4,07	23,58
LT	2,68	2,58	3,40	3,63	3,74	3,82	3,93	23,78
LU	0,02	0,02	0,02	0,02	0,02	0,02	0,02	0,16
HU	3,01	3,04	3,70	3,68	3,62	3,62	3,74	24,41
MT	2,06	2,07	2,08	2,01	1,96	1,90	1,89	13,96
NL	0,04	0,04	0,05	0,05	0,05	0,05	0,05	0,32
AT	0,07	0,07	0,08	0,07	0,07	0,07	0,07	0,51
PL	2,61	2,39	2,97	2,66	2,66	2,63	2,67	18,58
PT	1,76	1,75	1,81	1,79	1,81	1,80	1,81	12,52
RO	1,07	1,37	2,22	2,54	2,63	2,59	2,67	15,09
SI	1,60	1,53	1,65	1,67	1,67	1,64	1,64	11,40
SK	2,37	2,18	2,42	2,52	2,62	2,63	2,63	17,36
FI	0,14	0,14	0,15	0,14	0,13	0,12	0,11	0,93
SE	0,07	0,08	0,09	0,08	0,07	0,07	0,07	0,54
UK	0,08	0,09	0,10	0,09	0,08	0,08	0,08	0,59
Total□	0,36	0,38	0,41	0,40	0,40	0,40	0,41	2,77

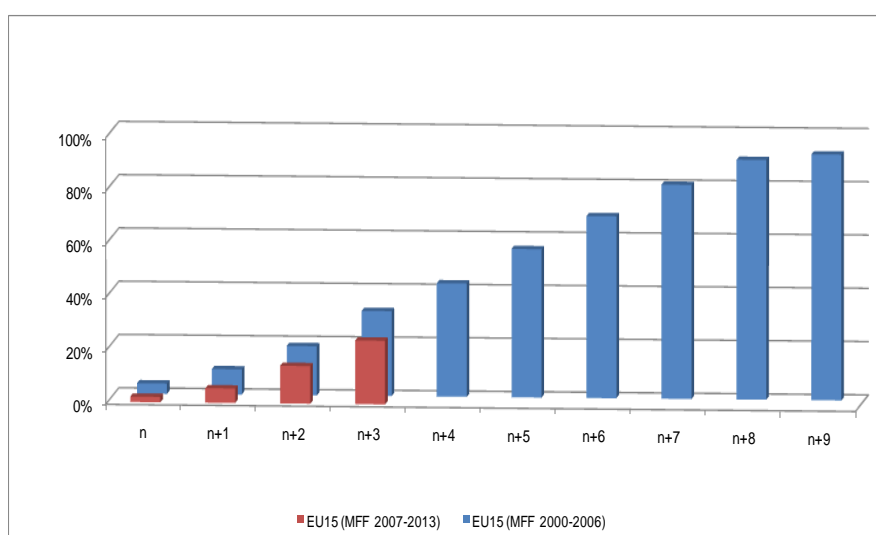
Note: Allocations per Member State include all possible items under convergence, cohesion, regional competitiveness & employment and territorial cooperation, financed under the ERDF, ESF & Cohesion Fund. Bold = n+3 countries.

3. THE POOR-ABSORPTION PROBLEM

It was recently observed that EU funds are only partially and in any case too slowly absorbed⁵. A country's absorption capacity is captured by the evolution of the difference between commitment appropriations and executed payments (ie the so-called RAL).

Out of the total allocation for the period 2007-2013 there are in EU27 about 270bn EUR still outstanding and 134bn EUR uncommitted (ie coinciding with the sum of the financial envelopes of 2011, 2012 and 2013)⁶. Absorption has been progressing more slowly than in the previous programming period. Chart 2 displays figures for the current and the previous MFF just in the old member states to allow comparability across the two programmes. The delay in the absorption of EU funds is of about 1 year compared with 2000-2006. Two factors may have contributed to the markedly slower disbursement this time: i) the relaxation of the n+2 rule in 2007 which has probably relieved some countries of the pressure to accelerate the production and implementation of EU-funded projects⁷; and ii) the difficulty in securing domestic resources to cover an average of 20 percent of the total costs of convergence projects, as required by the co-financing principle⁸.

CHART 2: THE PACE OF ABSORPTION IN EU15 ACROSS PROGRAMMES



Source: Bruegel's own calculation based on European Commission data.

⁵ One example is the Financial Times' survey on Structural Funds.

⁶ EU Member States have committed all the resources they had available until the end of 2010 and will proceed by committing again the full amount in the three remaining years. Payments, on the other hand, are executed more gradually year after year due to the multiannual character of most projects and are expected to reach a cumulative execution rate of 95 percent by 2015.

⁷ The n+2 rule implies that countries lose the funds that are still unused two years after they have been allocated (ie de-commitment).

⁸ An additional explanation may relate to delays in the approval of Management and Control Systems (MCS). The MCS are additional audit requirements for the evaluation of EU-funded projects by Member States introduced under the current MFF.

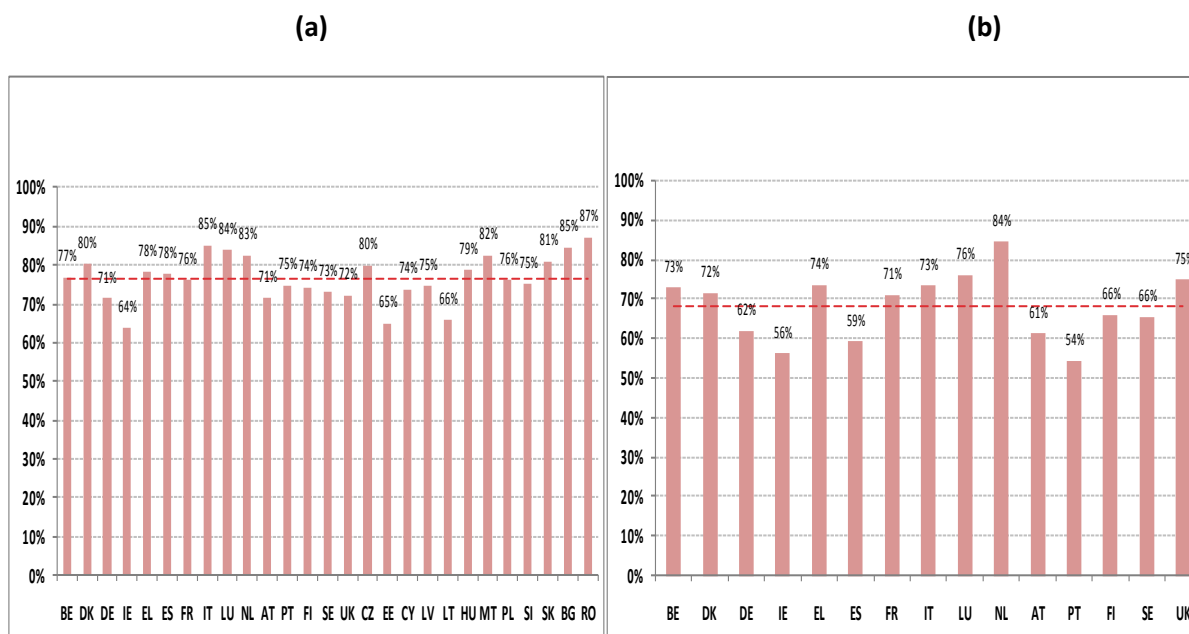
3.1. Absorption by country

Data on outstanding funds as a proportion of each country's national GDP provide a good indication of the potential role of EU Structural and Cohesion Funds for crisis management and resolution (see Chart 1). As they are a share of the initial allocation, outstanding commitments are obviously significant for the main beneficiaries of redistribution in the EU (ie NMS and some Southern European countries). Amongst euro zone current crisis countries there is some variation. For Greece, outstanding funds are about 7 percent of GDP over the 7-year programming period. For Portugal, they come close to 9.3 percent of GDP. Spain has about 2.5 percent of GDP in usable financial resources, but Ireland only 0.4 percent of GDP.

The problem of poor absorption is one of governance. Hence, absorption rates vary from one country to the other reflecting differences in national institutional and political contexts. Chart 3 (a) shows the share of outstanding funds as a percentage of the total allocation for the period 2007-2013. Most of the countries for which the n+2 rule was relaxed in 2007 are characterised by below-average absorption (ie NMS and Greece). But the emergency changes that were introduced in EU regulation in response to the crisis are certainly just one part of the explanation. The absorption of EU funds is worse than in the rest of EU27 also in Italy, Luxembourg, Netherlands and Denmark.

Chart 3(b) allows comparing the current situation with that of the previous financial framework. Three years after the beginning of the programme undisbursed funds were higher-than-average in the Netherlands, Luxembourg, the UK, Greece, Italy, Belgium and Denmark. All in all, chart 3 provides only limited support to the other hypothesis according to which poor access to EU funds shall be related to the difficulty in finding domestic resources to match co-financing of EU-funded projects in times of crisis and of imposed fiscal rigour. First, the Netherlands and Denmark underperformed in the new programme as well as in the previous one but are not currently facing particularly tight fiscal constraints at home nor were they under strong austerity measures in 2000-2006. Second, the performance of Greece compares badly with that of other EU countries whether in times of crisis or not. The problem of poor absorption thus goes well beyond that of concrete domestic fiscal constraints.

CHART 3: OUTSTANDING COMMITMENTS COMPARED TO INITIAL ALLOCATION FOR THE PERIOD 2007-2013 AT THE END OF 2010 (a) AND FOR THE PERIOD 2000-2006 AT THE END OF 2003 (b)



Source: Bruegel's own calculation based on European Commission data.

4. GOVERNANCE: ABSORPTION, OBJECTIVES AND DELIVERY

The empirical literature on the economic impact of EU Funds has produced mixed results. On the negative or neutral side, Boldrin and Canova [2001] find that Structural and Cohesion Funds are on average ineffective. Checherita et al [2009] show that they help reducing income disparities at the regional level but are incapable of promoting output growth⁹. Interestingly enough, Ederveen et al [2006] find that EU funds become effective only when accompanied by an appropriate institutional framework (ie strong institutional quality, lack of corruption, etc.). All in all, there is no doubt that the economic success of EU funds is conditional on issues of governance. The following dimensions of governance deserve special attention: absorption; the identification of the objectives for which Structural Funds are used; and their actual delivery, which is the umbrella under which both absorption and objectives should be treated. We argue in fact that, depending on the type of project they support, Structural Funds may be better delivered in a centralised or in a decentralised manner.

4.1. Absorption targets

That EU countries have only poorly and slowly absorbed EU funds is not a new argument. Different types of absorption problems have been so far identified. On the demand side, national authorities have been unable to put together a sufficient number of projects eligible for EU funding. On the supply side, the co-financing principle has at times constrained countries that have weak fiscal

⁹ For a discussion of the problems associated with econometric growth regressions testing the role of Structural Funds, see European Commission [2004].

planning capacity¹⁰. Moreover, poor administrative capacity has delayed or even impeded the execution of already approved projects.

As evident from Chart 1, available EU funds are a potential booster for economic revival in most NMS as well as in Greece and Portugal. In that respect, they potentially offer an important contribution to recovery and stronger long-term economic growth in these countries¹¹.

The European Commission has included higher absorption of EU funds as a condition for the disbursements of EU loans to three financially assisted countries: Latvia, Romania and Greece. Latvia is expected to receive total funding for 7.5bn EUR, of which 3.1bn EUR under the MTF scheme. Romania receives 20bn EUR, of which 5bn EUR under MTF. Disbursements to both countries started in 2009 and will continue until 2012. The adjustment programmes for Latvia and Romania require, as a condition for the disbursements, that governments implement various deficit cutting measures but also put aside resources to match co-financing of EU projects and demonstrate efficient spending of EU funds by meeting specific expenditure targets laid down in the adjustment programme itself. Greece, on the other hand, obtained a special loan of 110bn EUR, of which 80bn EUR from the EU that will be distributed between 2010 and 2013. As in the case of Latvia and Romania, the economic adjustment programme for Greece contains a list of actions the Greek government should undertake in order to raise the absorption rates of Structural and Cohesion Funds. These include i) an accelerated process of selection and production of project proposals, whose results will be assessed based on the number of projects that are submitted to Commission services; ii) the establishment of a special central account that collects budgetary appropriations intended to co-finance Structural and Cohesion Funds; and iii) the creation of a special government task force that is in direct contact with Commission Services. All of these interventions address the most typical absorption problems already described above: lack of proposals, weak fiscal planning and poor administrative capacity.

Raising effective absorption is a valuable policy objective and should indeed represent one of the elements of conditionality in all financial assistance packages. Nevertheless, higher effective absorption as such is not sufficient. The key question is whether EU funds are used for the right projects and whether they are successful in meeting the objectives for which they have been conceived. The first issue is resolved by identifying systematically a country's weaknesses and needs knowing how one or the other project contributes to solving them. The second concerns the funds' delivery and is especially relevant for redesigning the next MFF.

4.2. Objectives: the right solution for the right problem

EU funds are mostly used under four different headings: i) infrastructure spending; ii) support to agriculture, industry and services; iii) investment in human capital; and iv) investment in R&D. Not all projects are worth embarking on. Higher absorption turns into an economic success only if the projects undertaken truly address the country's structural weaknesses and short-term needs. Hence, adjustment programmes for countries under financial assistance should not only include spending targets for EU funds so as to incentivise absorption but also provide indications of how Structural and Cohesion Funds can and should be used¹².

¹⁰ This is more than just facing fiscal constraints in austerity.

¹¹ That EU funds have a stimulus potential was already recognised in the European Economic Recovery Plan (EERP), on the basis of which 6.25bn EUR were advanced from the EU Budget to EU member states in the form of advance payments.

¹² Under the Marshall Plan, funds were being actually disbursed only upon acceptance by US authorities of the individual projects they were used for.

For example, not all crisis countries have poor infrastructures or uncompetitive product markets or poorly skilled labour forces, or a weak capacity to innovate. It is crucial to identify priorities and provide EU countries with guidelines, whether rigid or soft, on the types of projects that can be implemented and, if necessary, technical assistance to realise them. For example, in Greece, the railway system suffers from structural deficiencies and other bottlenecks; product markets are uncompetitive due to high entry costs; the education system is excessively rigid, R&D spending and, as a result, high-tech exports well-below average. In Portugal, the labour force is poorly skilled and R&D spending is below the European average but not as low as in Greece. In Spain, there is a mismatch between skill demand and supply that needs to be addressed and, just like Greece, a problem of poor R&D spending and poor competitiveness in high-added value sectors.

EU guidelines should not only consider each country's structural weaknesses, but also short-term needs including the necessity to counteract the recessionary impact of otherwise necessary fiscal adjustment. Different categories of EU-funded projects come in fact with a different short- and medium-term economic impact.

Table 3 provides a snapshot of how the four different project headings identified above can be modelled and summarises the size and time profile of their macroeconomic effects. Measures supporting agriculture, industry and services reduce entry costs for firms and allow investment in tangible assets (eg machineries and equipment). They have very strong effects in the short-term and moderately strong in the long-term. Infrastructure spending is mostly modelled as government investment and tends to have a moderately strong economic effect in the short-run and in the medium-term. Investment in R&D also reduces entry costs for start-ups that would have been otherwise unable to finance themselves. The short-term impact is ambiguous and depends on the actual measures being introduced but the long-term effects are significant. Investment in human capital comes as a form of government spending and its short-term impact is ambiguous, as it may be associated with negative immediate effects if workers are taken out of the labour market to be trained, but has a very strong long-term impact¹³.

Project selection needs thus to emerge from an evaluation of both structural weaknesses and macroeconomic needs. Greece, for example, has committed to an ambitious fiscal consolidation plan that foresees discretionary measures from 2010 to 2013 worth 10.9 percent of national GDP, with 3.8 percent of GDP in revenue increases and 7.1 percent of GDP in expenditure cuts. The potential recessionary impact will be important¹⁴. The 7 percent-of-GDP EU funds still available to Greece should be absorbed on projects that address structural weaknesses and thus contribute to raising the country's potential output, but also combat the contractionary impact of such a far-reaching fiscal retrenchment. In view also of the significant frontloading of fiscal consolidation, preference should be given, for example, to measures that support agriculture, industry and services (eg IT support services to firms) and to the required infrastructure spending. R&D and human capital investment are crucial to the economic survival of Greece and can be put in place after the strong initial fiscal effort has been relaxed.

The EU Commission should indeed select few priorities from those identified in the already approved OPs making sure they are consistent with the main messages in the new Annual Growth Survey, the country-specific Broad Economic Policy Guidelines (BEPGs) and EU2020. It should also offer technical assistance on the ground. The next question is, however, whether these measures can be really

¹³ The snapshot is an adaptation of results obtained in Varga and in't Veld [2010].

¹⁴ Our calculation is based on IMF estimates of the contractionary effect on output of expenditure- and revenue-based fiscal consolidations [IMF, 2010].

implemented if poor absorption remains. For certain types of projects, absorption problems may be harder to eradicate. This poses the question of delivery.

TABLE 3: SIZE AND TIME PROFILE OF MACROECONOMIC EFFECTS OF FUNDS, BY PROJECT TYPE

PROJECT TYPE	MODELLED AS	SHORT-TERM	LONG-TERM
1. Support to agriculture, industry and services	Low entry costs and capital cost for tangible investment	++	+
2. Infrastructure spending	Government investment	+	+
3. R&D Investment	Low entry costs and capital cost for intangible investment	+/-	++
4. Human capital investment	Government spending	+/-	++

Source: Bruegel based on results from Dynamic General Equilibrium (DGE) model in Varga and in't Veld [2010].

4.3. The delivery of EU funds

The governance of Structural and Cohesion Funds is a matter of shared competence between the EU and the Member States. Priorities and the Operational Programmes (OPs) that should realise them are negotiated between the European Commission and the Member States but the implementation of the OPs is managed by the Member States.

For certain types of projects, however, absorption problems in the individual Member States are difficult to overcome. One such example is spending on infrastructures. This is a policy area where EU funds are typically used under strong political incentives due to the projects' high visibility and due to the role of public procurement. Moreover, infrastructural projects are more likely to be delayed along the process either due indeed due complex public procurement regulations, or delayed environmental impact assessments or because the co-financing principle requires national governments to have large amounts of available domestic resources to get them started.

Quite appropriately, a special status is granted to projects with a total cost of over 50mio EUR in the area of transport and energy infrastructures, as Member States need to conduct ex ante a Cost-Benefit analysis and to receive approval by the Commission services before starting spending on the projects. However, amending regulation introduced in 2009 allowed Member States to start spending even before the Commission's green light. By contrast, this is an area in which it would have been desirable to temporarily centralise delivery by delegating the management of EU funds to the EU Commission and creating a body similar to the Trans-European Transport Networks Executive Agency to manage the funds and implement projects in favour of crisis countries¹⁵. Under this scenario, there would be no need to maintain the co-financing principle as a means to preserve the good quality of the selected projects.

¹⁵ The Trans-European Transport Networks Executive Agency was created in 2006 to implement and manage the TEN-T programme on behalf of the Commission.

5. THE SIZE AND DISTRIBUTION OF EIB LOANS

EU member states have also the option of applying for EIB loans and guarantees to finance large-scale projects and programmes on favourable terms. The EIB's strategic objectives include amongst others fostering convergence, offering support to Small and Medium Enterprises (SME) and sustaining the development of alternative energies. To some extent, they overlap with those of Structural and Cohesion Funds. Yet, the nature of the available funds and the delivery structure are obviously different.

The EIB funds are not aid but loans granted on 'reasonable terms'; the quality of the proposed projects is evaluated in depth; and technical assistance is often provided for the project's planning and execution. They are generally easier to activate than EU Funds and cover up to 50 percent of a project's total costs, reflecting a co-financing principle, just as in the case of EU Funds. They can be combined with EU grants, and recent years have indeed witnessed an increasing use of these loans to pre-finance EU-funded projects or to just match co-financing¹⁶.

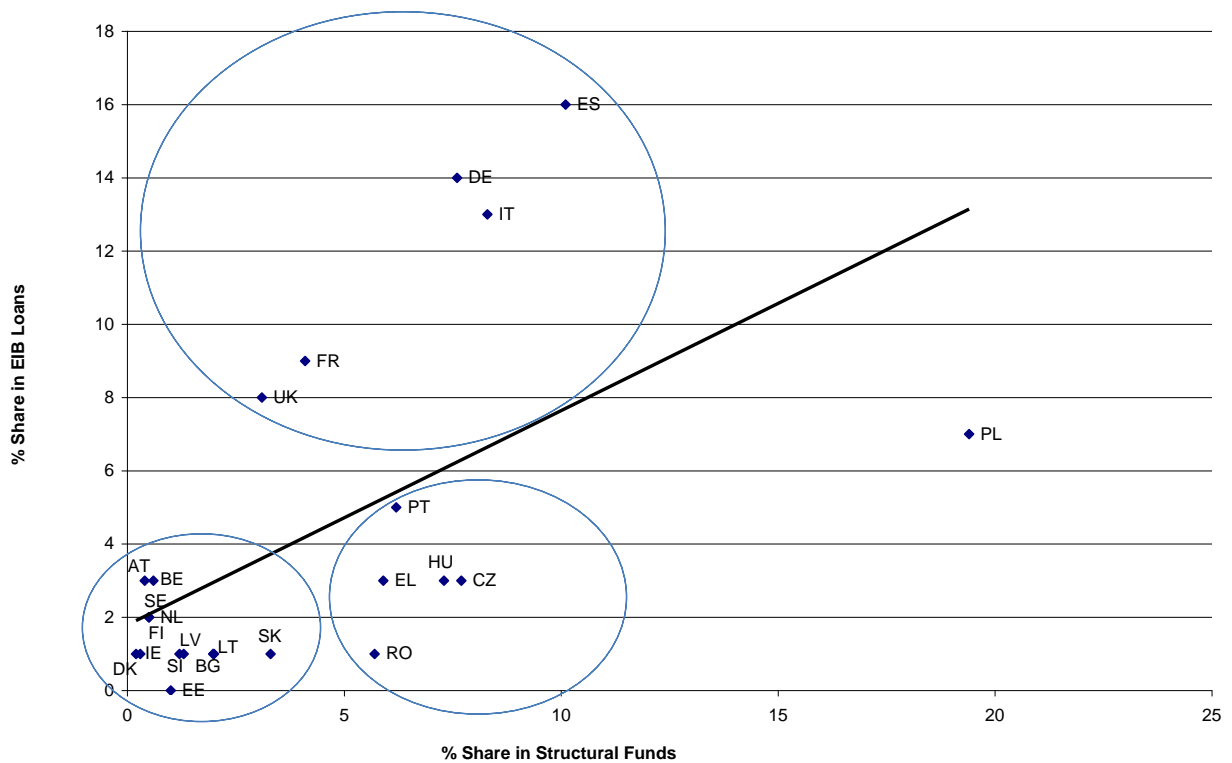
Currently outstanding EIB loans amount to about 344bn EUR¹⁷. They are differently distributed across member states. The largest recipients are Spain, Germany and Italy. The Statute of the EIB formally refuses the concept of national quotas. Nevertheless, there is a strong country-size dimension with large EU members receiving more than small countries, be it because of the number of potential applicants or the fact that they have been mostly involved in expensive Trans-European Networks projects.

Chart 4 compares each member state's share in EIB loans (2006-2010) with the share in total Structural and Cohesion Funds (2007-2013). Three clusters of countries can be isolated. The most populated one consists of countries that receive relatively less than others of both cohesion grants and EIB loans. The group is composed mainly of small countries. Ireland belongs to this group. This is unsurprising in the case of Structural Funds and Cohesion Funds, as the allocation method foresees that funds are distributed according to relative income per capita multiplied by the population of each region and by the surface area. On the other hand, small countries' limited access to EIB loans is less self-explanatory. It could be related to the potential number of applicants, their more modest involvement in large Trans-European Networks, but it could also be that poor access to EU grants is limiting the need and the opportunity to apply for EIB loans that pre-finance or co-finance EU-funded projects. The second cluster includes countries that receive more in loans than they do in EU grants. Spain is one such example and in fact the largest recipient of EIB loans. Finally, the third cluster consists of countries that receive relatively more in Structural Funds than in EIB loans. Greece belongs to this category.

¹⁶ EIB loans have been also used to finance technical support to improve EU funds absorption. An example is JASPERS, a joint initiative of the European Commission, the EIB and the EBRD to provide this type of technical support to the 12 Member States that joined the EU between 2004 and 2007.

¹⁷ The EIB's shareholders are the EU member states. Their contribution to subscribed capital is a function of their economic weight in the EU. As of March, 2009, the subscribed capital of the EIB was 232,4bn EUR. As the Bank's Statutes fixes an upper bound on its leverage ratio of 2.5, there is still about 240bn EUR available for loans.

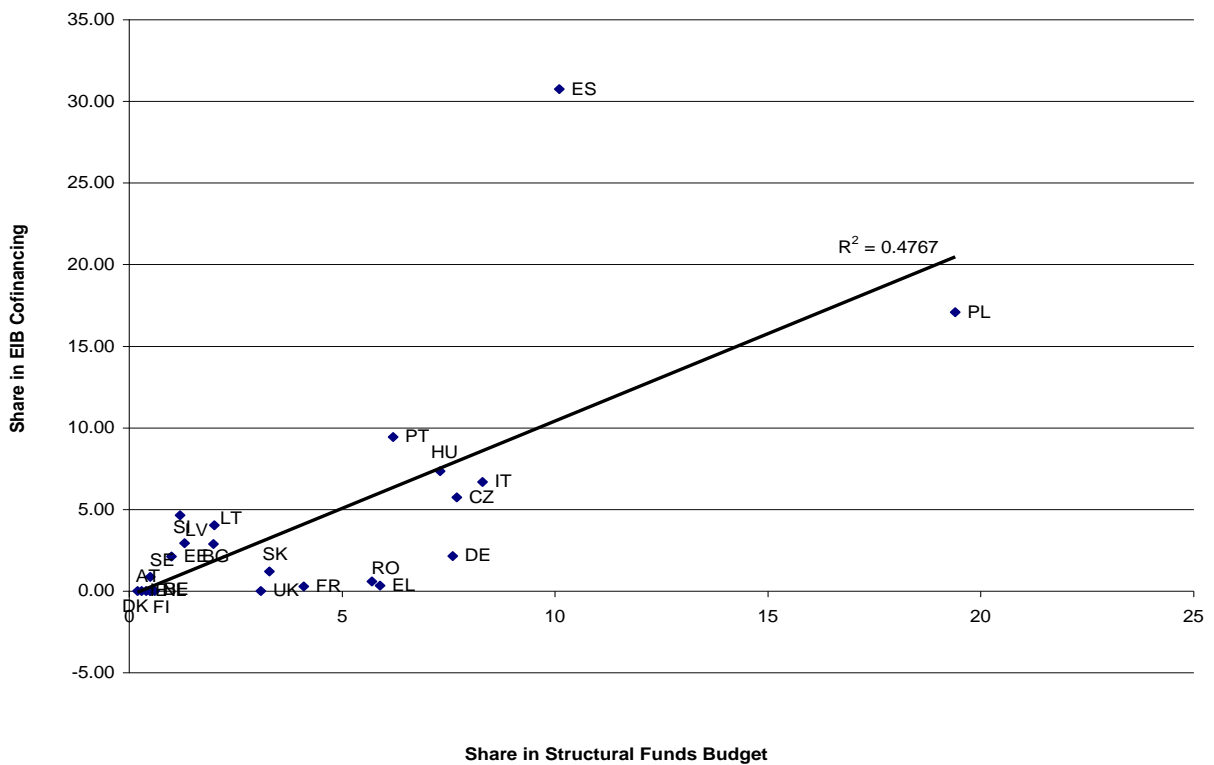
CHART 4: ACCESS TO STRUCTURAL FUNDS RELATIVELY TO ACCESS TO EIB LOANS



Source: Bruegel’s own calculation based on European Commission and EIB figures.

The idea that countries may exploit (or are unable to exploit) synergies between grants and loans is a suggestive one. To check for its robustness, we compare each member state’s share in total Structural and Cohesion Funds (2007-2013), as above, with the share in EIB loans that co-finance projects already supported by funds from the European Commission (2006-2010). Chart 5 shows indeed a positive relationship between the actual availability of EU funds and the practice of using EIB loans in conjunction with EU grants. Spain is an exceptionally active applicant of EIB loans and arguably much more capable than others at exploiting synergies between European loans and grants to support large infrastructural projects. In Greece, on the other hand, there is room for improving the use of loans from either the EIB or more generally from private investors to co-finance already EU-funded projects given the little incidence of projects financed and funded by the EIB and the EU Budget respectively (see vertical axis of Chart 5).

CHART 5: ACCESS TO STRUCTURAL FUNDS RELATIVELY TO ACCESS TO EIB COFINANCING



Source: Bruegel's own calculation based on European Commission and EIB figures.

6. SOME CONCLUDING REMARKS

The EU in the past could afford to manage its development funds without much regards to their macroeconomic effects. At a time when the Southern part of the euro area is struggling and badly needs policy instruments for economic revival, this has become an unaffordable luxury. Some EU countries have large amounts of usable Structural and Cohesion Funds. These shall be put to good use within the framework of a temporary 2011-2013 European Fund for Economic Revival (EFER). It is a welcome development that the adjustment programmes of Latvia, Romania and Greece mention a higher absorption rate of EU funds as one of the elements of conditionality. But absorption per se is not sufficient to deliver economic growth.

EU funds should turn into a booster fund for economic revival in crisis countries. In particular, adjustment programmes negotiated with financially assisted countries should include precise references to the types of projects that need to be financed, taking account of the target countries' structural weaknesses but also of short-term needs recognising the funds' countercyclical function.

The European Commission should be empowered with the direct management of certain types of projects. The delivery of projects such as local infrastructure spending listed in the OPs should be temporarily delegated to the European Commission and carried out by an special inter-service task force involving DG ECFIN, as the latter is in charge of conditional assistance. Under this scenario, co-financing by the Member States may be temporarily suppressed.

The EU should promote ways of taking advantage of the flexibility of EIB loans and of strengthening synergies with the EU Budget. The evidence seems to be that recipients of small amounts of Structural Funds also apply for small amounts of EIB loans. Small countries are in turn less able to exploit positive synergies between the two instruments. Whilst the EIB finances more than 50 percent of a project's total costs only under exceptional circumstances, it should in fact apply this rule to small EU Member States and especially those in difficulty.

There is room for using the EU Budget to leverage financing of strategic investments by the private sector with the support of the EIB. The EU Budget can serve the purpose of improving credit rating and of obtaining therewith support from the private sector to finance cohesion-enhancing strategic investments in Europe¹⁸.

Excellent research assistance was provided by Lucia Granelli and Christophe Gouardo.

¹⁸ The idea of strengthening synergies between public and private funding is well present in the Monti Report and in the latest European Commission's Communication of 19 October 2010 on the EU Budget Review.

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