The impact of the EU Cohesion Policy on regional inequalities

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Extended Abstract

The EU represents a unique case of a supranational organization that undertakes an explicit commitment to the exercise of Cohesion Policy. Diachronically, Cohesion Policy – the regional policy of the EU – remains an overriding EU political priority, aiming to enhance economic, social and territorial cohesion in a development-enhancing context and within an economic integration framework. Under this perspective, regional policy may be considered as the market's "visible hand" supporting growth and a more balanced pattern of spatial development. Yet, despite the serious and well-funded interventions, the EU experience with respect to the reduction of regional inequalities is not very encouraging, as the latter appear to be consistently high – and in several cases increasing.

Studies conducted at the country level confirm that, prior to the eruption of the economic crisis the EU has experienced a persistent between countries convergence process. However, such a process may mask a pattern of divergence within each country. This is because convergence at the European level has been partly driven by the dynamism of the metropolitan centers, causing dualistic phenomena at the national level. This spatial pattern of development indicates that during the period of economic crisis, the EU started to experience either trends of "reverse convergence" or trends of divergence.

This unbalanced spatial pattern of development in the EU has raised concerns about the effectiveness (and even about the necessity) of the EU Cohesion Policy. Since the EU Cohesion Policy is confronted in the last period with new challenges, such as the pandemic, the climate change, the war and the AI revolution, it is clear that policymakers face multiple pressures and priorities, which make policy choices even more difficult.

The paper studies the impact of the EU Cohesion Policy on regional inequalities, which has become a subject of intense discussion in both academia and policy. Even though there is an extensive body of literature available, the empirical findings remain rather inconclusive and, therefore, the policy messages remain to some extent ambiguous. This is so as there are studies that find positive long-term impact, there are studies that find positive but only short-term, impact, and there are studies that find neutral (i.e., statistically non-significant) or, even, negative impact of the EU Cohesion Policy.

The empirical analysis of the paper focuses on three areas of research where the evidence is not yet very solid. First, the report examines the impact of the EU Cohesion Policy on three types of inequality that may be related to each other: within-country regional inequalities, between countries inequalities and within-countries income inequalities. Second, the report examines what policy tool (i.e., investment, infrastructure, human capital, or environment) is more likely to reduce spatial inequalities or income inequalities. These policy tools are to some extent related to pre-market, in-market, or post-market policies and help identify which mix is more likely to reduce

different types of inequalities. Third, the paper examines whether administrative efficiency and the absorbing capacity of Managing Authorities at the national or regional level affect the effectiveness of the EU Cohesion Policy to reduce inequalities. The paper sheds some light into the implementation experience of the EU Cohesion Policy during the last two decades and provides new evidence related to its impact on the three types of inequality examined.

The evidence of the paper indicates that trade imbalances reduce directly or indirectly the effectiveness of the EU Cohesion Policy at the spatial within-countries and between-countries level. In a European terrain with large trade imbalances between core and peripheral countries, the EU Cohesion Policy may not be able to reduce internal or external inequalities in countries where import penetration and demand leakages are high and public investment multipliers low. Given that external imbalances are shaped by the performance of both advanced and lagging countries, it is clear that the EU Cohesion Policy needs to be supported by a shift in economic policies in the advanced countries. This shift would boost domestic demand and reduce excessive trade surpluses with the other EU countries, as part of a new growth strategy that is not based exclusively on foreign demand. In general, the findings suggest that critical drivers of the broader economic environment affect, in one way or another, the effectiveness of the EU Cohesion Policy. The process of EU integration appears to have diverse effects on inequality along geographical and developmental lines. Although the SEM provide benefits to all, core-periphery trade may not be very friendly to the weaker economies that experience pressure in their domestic markets and sometimes resort to defensive or sheltered specializations. It is interesting to note that the EU Cohesion Policy might be more successful in reducing inequalities between countries, rather than inequalities within countries. The available evidence suggests that EU Cohesion Policy in countries with low to modest levels of development supports them to converge to the more advanced EU counterparts. Paradoxically, although the design of EU Cohesion Policy is based on the needs and realities of the regions, it appears to have a more robust impact and fewer conditionalities at a higher level of aggregation.

In addition, the evidence suggests that different types of inequality may be related and feed each other. Spatial and social inequalities in the EU tend to increase with the level of development and they are interrelated in a vicious cycle, where income inequalities contribute to spatial imbalances, while spatial imbalances trigger higher income inequalities. On the other hand, the catching-up of a number of countries (mostly new Member States) towards the EU average level of development has taken place primarily through the development of their metropolitan or western regions that has increased dramatically internal spatial and income inequalities. It seems that part of the contradictions of the market-driven dynamics is to generate a trade-off, where national convergence at the EU level can be achieved only at the expense of higher domestic social and spatial imbalances. This pattern of convergence at the higher and divergence at the lower level of aggregation (or vice versa) provides evidence that the two levels interact with each other, unfortunately in an undesired way, raising a number of market-driven limitations and a major challenge for the EU Cohesion Policy.

Moreover, the evidence indicates that the impact of the EU Cohesion Policy on inequality is conditional on a number of economic and structural or institutional characteristics of the countries. These conditionalities define limits for the effectiveness of EU Cohesion Policy, but also reveal the factors that regulate its impact, either as enabling factors or as barriers to overcome.

Notably, the evidence suggests that different policy instruments have a different impact on different types of inequality, with some of them having the opposite impact in the two levels of aggregation. Investment policies and infrastructure policies, the two major, in terms of funding, priorities of EU Cohesion Policy have the opposite effects on the three types of inequality. Investment, which is primarily an in-market policy, tends to decrease the between countries development gap, but increase regional inequality and income inequality. On the other hand, infrastructure policies that are primarily pre-market tend to increase the between countries development gap, but decrease all other types of inequality. In general, it seems that pre-market policies tend to increase domestic inequality, while in-market policies tend to decrease the between countries inequality. Although the evidence for a negative impact is an important confirmation of the significance of the EU Cohesion Policy, the evidence for a positive impact on inequality is the one that maters more for policy makers. It will allow them to examine in a more systematic way conditionalities and trade-offs and design a policy mix that responds better to different needs and can counterbalance the contradictions and dilemmas of “policy insensitive” market dynamics.

Finally, although more efficient administrations tend to reduce development gaps and income inequality, this is not the case for regional inequality. The difficulty of Managing Authorities to reduce regional inequalities may be an indication of weaker administrative structures in the regions or a highly centralized governance system that leaves limited decision-making power and limited ownership of policies at the regional level.