EU Structural Funds and Growth Prospects - a Sobering Experience

New research shows that regional funding of the European Union - currently amounting to 450 billion Euros - has no positive effect on economic growth

In the financial framework period of 2014 to 2020, for the first time the European Structural Funds represent the main share of the European Union's (EU) budget. Previous evaluations on the funding's effectiveness reveal contradicting results. A new and robust RWI study does not find any positive effects of the program on economic growth. In fact, impacts indicate that highly funded regions might have to overcome structural problems first before growth programs can take effect. Also, a high intensity of funding in the immediate regional neighborhood has a strongly negative influence on a region's growth prospects.

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MAIN FACTS

Despite a funding volume of hundreds of billions of Euros the EU Structural Funds do not have a positive effect on regional economic growth.

When designing an overall funding scheme, it should be considered that neighboring regions appear to be poaching private investors from one another.

Regional funding clusters reveal structural and technological backwardness which can only be dispersed by reforms.

Why is it important to evaluate the effectiveness of the EU Structural Funds?

The EU Structural Funds are one of the world's most extensive regional funding programs. In the financial framework period of 2014 to 2020, this funding forms the largest share of the EU budget (450 out of 960 billion Euros) for the first time. Every year, billions of Euros are invested in structurally disadvantaged regions to foster employment and economic growth as well as to strengthen competitiveness. However, there is debate on the effectiveness of the subsidies at realizing these goals.

Why do previous evaluations show contradicting results?

The contradicting results on the effectiveness of the EU Structural Funds can be explained by the difficult position of compiling a causal evaluation. Factors which are a criterion for granting the funding may at the same time affect the future economic growth of this region. Due to this mutual influence it is challenging to identify the growth effects of the subsidies. To avoid such issues, a new RWI study is using data on a funding program with certain eligibility criteria: funds are allocated to regions with a low level of economic output, while their growth prospects are not taken into consideration. In the RWI study, spatial influences are considered as well as new data on the amount of the actually paid grants. Previous studies were often based on funding approvals (which are not always implemented in the granted amount). In contrast, the RWI study design is very robust, and the results are quite sobering.

Which reasons lead to the negative conclusion?

All in all, there is no evidence for a positive funding effect on growth. This is mainly due to the fact that the economy in regions with many funded neighbors grows far less than in regions where little or no neighbors receive subsidies. An obvious explanation could be that neighboring regions lure private investors away from one another. At a national level this is fatal as the EU funding was supposed to provide additional impulses and not shift the impulses within an area. Another interpretation of the analysis' results is that highly funded regional clusters suffer from structural and technological backwardness. If this is true, rather short term growth programs like the EU Structural Funds are not able to take any effect, until before reforms have eliminated structural barriers.

IMPACT NOTES

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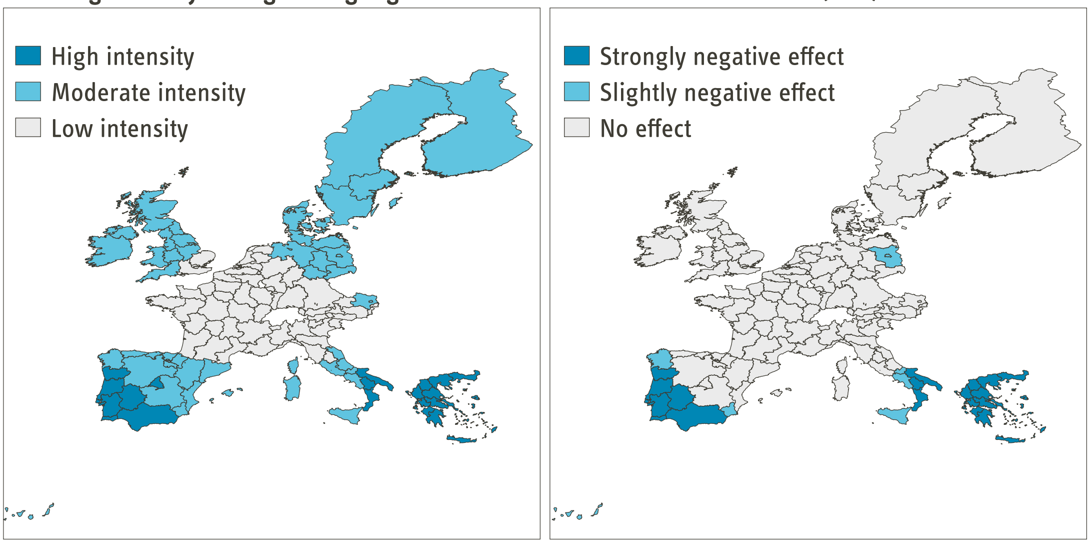
A high intensity of funding in the immediate regional neighborhood negatively affects growth prospects

Funding intensity in neighboring regions | **Overall funding effect on the regional Gross Domestic Product (GDP)**



Sources: RWI calculations based on Eurostat (2010) and GD Budget.

Policy Recommendations

- Countries with many structurally backward regions ("highly funded clusters") should implement reforms in order to reduce structural obstacles like those within the labor market. Additionally, they should establish more favorable incentives for private investors.
- Institutional investors such as the EU Structural Funds need to consider potential impacts within neighboring regions when granting funding. They should only subsidize those private investments that will not be cut down in another region in return.

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