COHESION POLICY REFORM PROCESS: SOME IMPLICATIONS FOR SPAIN AND ITS REGIONS*

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Abstract

The recent negotiation of the EU budget and the associated reform of EU Cohesion policy have had major policy implications for Spain, the country in receipt of most Cohesion policy support in the previous programming period. EU enlargement, combined with relatively rapid growth in Spain, impacted on the eligibility of Spanish regions for Cohesion policy support while also taking the country as a whole beyond the eligibility threshold for the Cohesion Fund. This paper reviews how it carried out the reform of Cohesion policy, what were the results of the negotiations for Spain and its regions in terms of budgetary allocations, as well as the policy and institutional implications. It also reviews the literature on the economic effects of Cohesion policy in the past (1989-2006) and present (2007-2013) periods, which play a part in current debates under the EU budget review.

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I. INTRODUCTION

Initial Commission proposals regarding the Financial Perspective 2007-13 were published in February 2004[i]. These proposals represented the start of the formal negotiation process of the EU budget 2007-2013. The assumptions underpinning these proposals (and their implications) were then discussed and developed in the Friends of the Presidency Group on the Financial Perspectives which, in the course of the next year, considered almost 100 technical documents (fiches) produced by the Commission.[ii] Following the approach adopted in the run-up to the 1999 Berlin European Council, a first Negotiating Box was produced by the Luxembourg Presidency. This was "designed to provide a solid framework and give focus and momentum to the discussions" by distinguishing between areas (in normal typeface) where there was a degree of agreement (at least at the level of principles) and problem areas (in italics) which remained to be progressed. Four further Negotiating Boxes were considered in April, May and June. Areas of disagreement were narrowed and budgetary ranges became proposed figures. A final set of proposals was made in the last stages of the European Council on 17 June. However, the proposals did not receive the required unanimous approval of the Member States. Three of the main net contributors – the United Kingdom, Sweden and the Netherlands – rejected the package, as did, for different reasons, Finland and Spain. Spanish concerns centred particularly on the net balance position of the country.[iii] Two other Member States – Denmark and Italy – abstained.

The United Kingdom Presidency delayed producing a further Negotiating Box until before the December European Council.[iv] This left the results of the June negotiations unchanged as they related to the EU15, and tried to satisfy the net contributors by reducing the expenditure flowing to the new Member States by over 8 percent. By way of "compensation", various concessions were made to the new Member States to ease their absorption of EU spending (by, for instance, increasing the co-financing rate from 80 percent to 85 percent, setting the automatic commitment rule at n+3 rather than n+2 for 2007-10 and making housing projects eligible for ERDF support). As no doubt anticipated by the Presidency, the proposals were not accepted and, indeed, generated considerable adverse comment. Further concessions were made in a second UK Negotiating Box to try to bring the parties closer to agreement.[v] A final Negotiating Box was withheld until the Presidency felt that agreement could be reached. This made more concessions all round. Expenditure committed under the final set of proposals was 1.0459 percent of EU GNI compared to 1.03 percent under the first UK Negotiating Box and 1.056 percent under the 17 June proposals of the Luxembourg Presidency. Also important to the final agreement were developments on the revenue side of the equation. The United Kingdom agreed to reduce the UK rebate by up to €10,500 million (an increase of €2,500 million compared to the second UK Negotiating Box) and additional concessions were made to Austria and, particularly, the Netherlands.

An overview of the Financial Perspective at key stages of the negotiations is set out in Figure 1.

Figure 1: Financial Perspective by Heading (€mn at 2004 prices)

Heading	2006 bench-mark	As % EU total	COM alloc'ns	As % EU total	Lux NB6 alloc'ns	As % EU total	UK NB3 alloc'ns	As % EU total	UK NB3 as % COM	UK NB3 as % 2006
1	**316764**	**38.2**	**463256**	**45.1**	**381604**	**43.8**	**379739**	**44.0**	**82.0**	**119.9**
1a	53662	6.5	121685	11.8	72010	8.3	72120	8.4	59.3	134.4
1b	263102	31.8	341571	33.2	309594	35.5	307619	35.7	90.1	116.9
2	**388486**	**46.9**	**400679**	**39.0**	**377801**	**43.3**	**371244**	**43.0**	**92.7**	**95.6**
Of which: agric	306145	37.0	301074	29.3	295105	33.9	293105	34.0	97.4	95.7
3	**14049**	**1.7**	**20945**	**2.0**	**11000**	**1.3**	**10270**	**1.2**	**49.0**	**73.1**
4	**53613**	**6.5**	**84649**	**8.2**	**50010**	**5.7**	**50010**	**5.8**	**59.1**	**93.3**
5	**48013**	**5.8**	**57670**	**5.6**	**50300**	**5.8**	**50300**	**5.8**	**87.2**	**104.8**
Comp	7287	0.9	800	0.1	800	0.1	800	0.1	100.0	11.0
Total	**828212**	**100.0**	**1027999**	**100.0**	**871515**	**100.0**	**862363**	**100.0**	**83.9**	**104.1**
GNI	75121480		82448058		82448058		82448058			
% GNI	1.10		1.25		1.06		1.0459			

Sources: The Commission allocations and related 2006 data are drawn from Fiche 29 Rev1, as updated to take account of the latest available data, Fiche 17 and Fiche 92. The 2006 benchmark figures consist of 2006 commitment appropriations multiplied by 7. The Luxembourg Presidency figures come from CADREFIN 130 of 15 June 2005 (10090/05), as amended and the UK Presidency data from CADREFIN 268 of 19 December 2005 (15915/05)

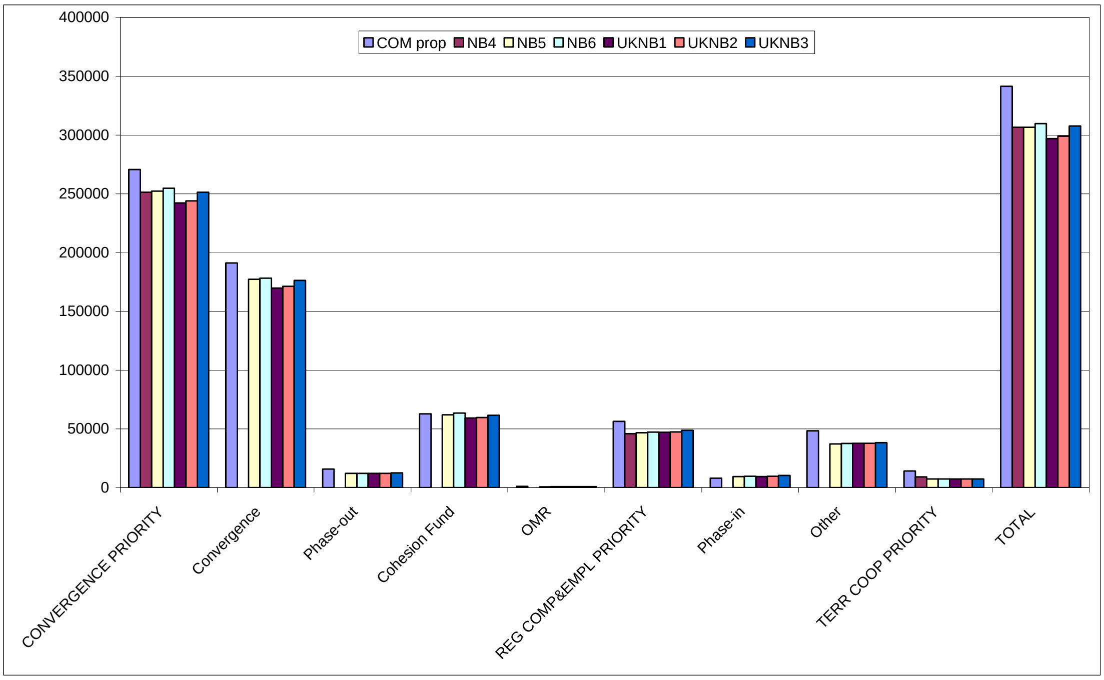
Although the overall budget was much reduced compared to the original Commission proposal, the key expenditure headings for the net recipients held up well during the negotiations. The final Cohesion policy budget (Heading 1b) was cut by less than 10 percent compared to the overall fall in commitment appropriations of more than 16 percent. The allocations to headings of less direct benefit to net recipients - Headings 1a (Competitiveness), 3 (Internal policies) and 4 (EU as a global partner) - were reduced by between two-fifths and a half. Of the other headings, administration (Heading 5) was cut by almost 13 percent while spending on natural resources (Heading 2) fell by just over 7 percent. The agricultural component of Heading 2 was largely unchanged in line with the agreement reached at the October 2002 European Council; the decline recorded reflected the inclusion of Bulgaria and Romania within the October 2002 ceilings. In global terms –see Figure 1-, there was relatively little difference between Cohesion policy funding under the fourth Luxembourg Negotiating Box (€306,508 million) and the final agreement (€307,619 million). At this level, the budget was broadly midway between the 2006 benchmark figure (around €263,000 million) and the original Commission proposal (over €341,000 million).

With respect to *Cohesion policy*, a number of key issues had to be resolved in the course of the negotiations: the allocation of funding between the Convergence priority, the Regional Competitiveness and Employment priority and the Territorial Cooperation priority; related, the split between the new Member States and the EU15 (as determined primarily by the level of absorption

capping applied to the new Member States and the assumed future growth rates for these countries); the transitional provisions for regions losing their previous designated status (the Phase-out regions under the Convergence priority and the Phase-in regions under the Regional Competitiveness and Employment priority); provisions relating to the Cohesion Fund (in particular, from a Spanish perspective, whether transitional provisions should apply to countries losing Cohesion Fund eligibility); and the treatment of special geographic areas under the Treaty – specifically, the Outermost regions (OMR), (Canarias in the Spanish context) and regions of sparse population (in the Nordic Member States)-.

Figure 2 shows a similar pattern for most components of the Cohesion budget. However, a number of differential points emerge. First, while the Convergence priority suffered by far the lowest percentage fall compared to the original Commission proposal (just over 7 percent), it was the Regional Competitiveness and Employment priority (13.6 percent decline) which gained funding at virtually every subsequent stage of the negotiations. In contrast, the Territorial Cooperation budget almost halved in the course of the negotiations (to €7,500 million). Under this priority, by far the greatest stress came to be placed on cross-border cooperation. Second, funding for transitional regions proved to be relatively robust during the negotiations – especially the budget for the Phase-in regions which rose from €8,103 million in the initial Commission proposal to €10,385 million. No other component of the Cohesion policy budget increased beyond the original Commission proposal. Finally, Figure 2 shows that the Cohesion Fund held up well during the negotiations. This was at least in part due to the special transitional provisions gained by Spain.

Figure 2: Cohesion Policy Commitment Appropriations 2007-13 (€mn at 2004 prices)



Following this introductory overview about the EU budget and Cohesion policy allocations at different stages of the budget negotiations, the remainder of this article reviews in detail the Cohesion policy negotiations, the main results for Spain and its regions in terms of budgetary allocations, as well as the policy and institutional implications based on interviews with national and regional programme managers in late 2005/2006 (Section II). In addition, a review is provided of the literature on the economic impacts of Cohesion policy in the 1989-2006 period as well as the economic implications of the new policy framework in 2007-2013 (Section III). the final section presents the main conclusions of the paper (Section IV).

II. COHESION POLICY REFORM: NATIONAL AND REGIONAL OUTCOMES OF THE NEGOTIATION

The financial implications for Spain of the reform of Cohesion policy post-2006 flow from two main factors: first, changes in eligibility for Cohesion policy support, which are partly, but not entirely, due to enlargement and shifting EU averages; and second, changes in the overall budget allocation and the architecture of the reform. This section begins by looking at the *national level* implications of Cohesion policy reform before considering the implications for the *regional level* in those areas of policy where financial allocations are disaggregated[vi]. Finally, it provides some reflections on the more qualitative aspects of the reform of Cohesion policy, such as its regulation, its practical application and its coordination with other regional instruments of national policy.

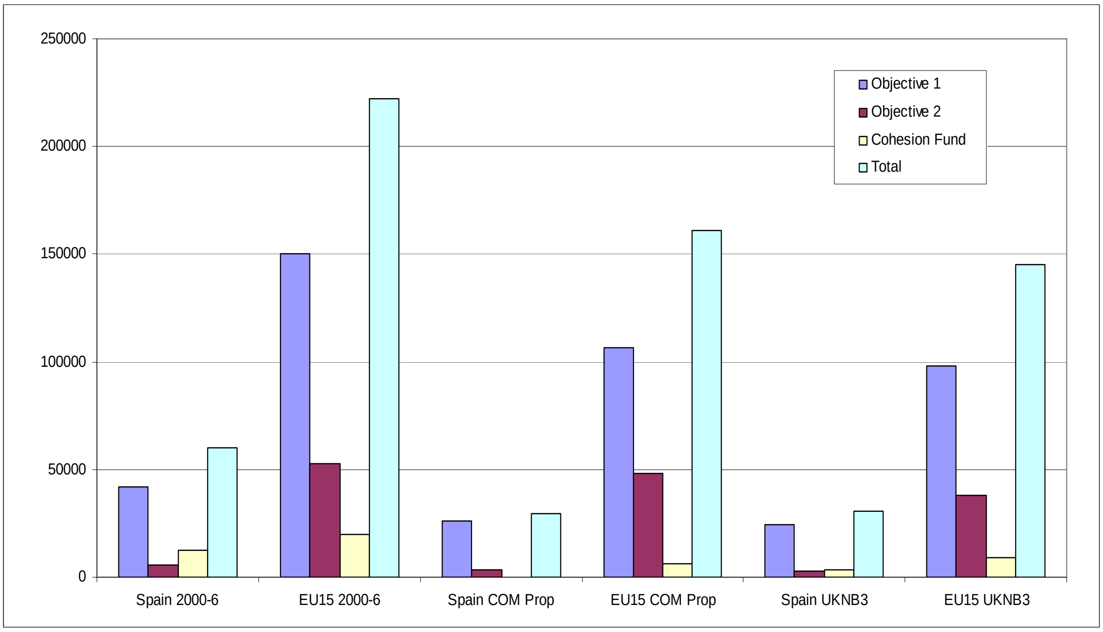
II.1. Overall Cohesion policy allocations

Spain was the single largest beneficiary of the structural actions budget in the 2000-06 Cohesion policy planning period, accounting for almost 27 percent of total commitment appropriations. The different architecture proposed for Cohesion policy in 2007-13 complicates direct comparisons with 2000-06. However, setting the new structure aside and grouping spending in various categories, a clear picture of the significance for Spain of the new proposals can be obtained. This is illustrated in Figure 3 which covers just the EU15 Member States. For Spain, it can be seen that there was a sharp decline in commitment appropriations in each category of expenditure. On the other hand, and as already discussed, in the course of the negotiations, Spain managed to maintain (and indeed increase) its overall level of funding (compared to the original Commission proposal) – and this despite significant cutbacks in funding flows to the EU15 as a whole-.

Figure 3 shows that the proposed allocation to Spain fell significantly in absolute terms – from around €60 billion (2004 prices) in 2000-06 to under €30 billion of the Commission proposal (but over €30 billion under UKNB3). It also fell in relative terms. Expressed as a proportion of the EU15 commitment allocations, Spain received a significant reduction in its share of overall EU15 funding compared to the 2000-06 period (27% to 22% approximately). Against this, in the course of

the negotiations, Spain managed to increase its funding share to more than one-fifth of the EU15 total.

Figure 3: Impact of COM Proposals and UKNB3 on Commitment Appropriations for Spain (€m, 2004 prices)



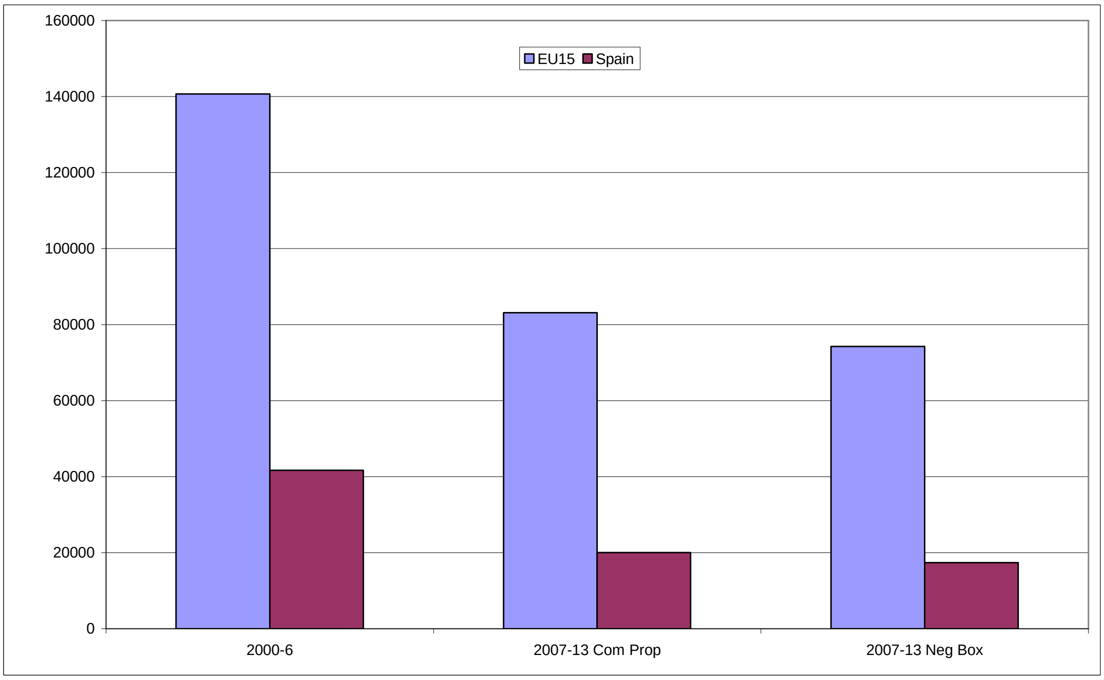
Notes: (i) For the 2000-06 period, spending has been grouped as follows: Objective 1 includes Objective 1 Phase-out; Objective 2 includes Objective 2 Phase-out, Objective 3 and FIFG outside Objective 1; **(ii)** For the 2007-13 proposals, Objective 1 includes Phase-out, Phase-in and OMRs (Outermost regions); **(iii)** Community Initiatives (2000-06) and the Cooperation priority (2007-13) are excluded from these figures.

Source: EPRC calculations from Eurostat data, data on Inforegio and RAPID release IP/99/442

Objective 1 / Convergence

One of the main reasons for the scale of the impact on Spanish commitment appropriations concerns changes in the eligibility of the Spanish regions for Convergence support, due both to enlargement and the growth of the Spanish economy. Less than one-third of the Spanish population is now located in regions qualifying for full Convergence status, compared to almost three-fifths for the 2000-06 period. Related, transitional status has become important for Spain, with almost 6 percent of the population in Phase-out regions and over one-fifth in Phase-in regions. Because of the changes in eligibility and the impact of enlargement, comparisons between the 2000-06 period and the outcomes under UKNB3 for 2007-13 are not straightforward. Nevertheless, it is clear that, within the EU15, the new proposals (both COM prop and UKNB3) involved a significant reduction in Convergence funding. The Spanish share in total EU15 Convergence funding is estimated to have fallen from over 29 percent in 2000-06 to around 24 percent under UKNB3 (see Figure 4).

Figure 4: Implications for EU15 Convergence Region Total Allocations (€m, 2004 prices)



Source: EPRC calculations.

The reforms introduced in respect of EU Cohesion policy also implied a decline in aid to Convergence regions measured in *per capita* terms. This reduction is much less marked than in the overall budget allocations. Spain continues to receive a higher per capita allocation than the EU15 average.

Cohesion Fund

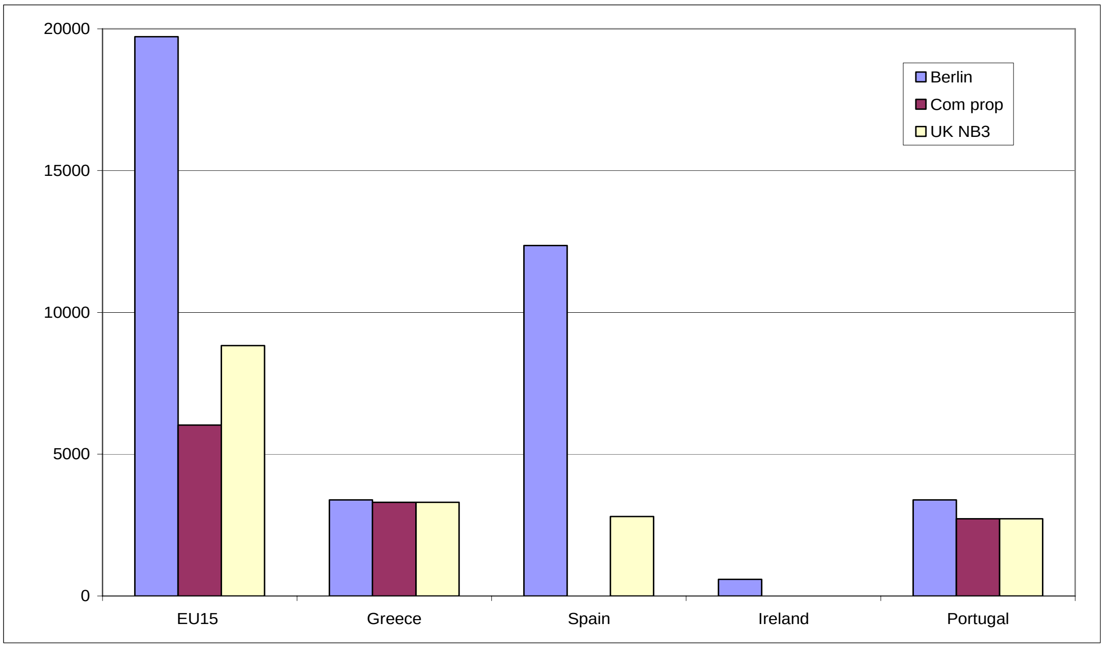
Another key element from the Spanish perspective concerned eligibility for the Cohesion Fund. The Cohesion Fund contributes to the Convergence priority under the new architecture. Eligibility for the Cohesion Fund is defined in Article 5(3) of the draft Regulation as concerning Member States whose per capita Gross National Income (GNI), measured in purchasing power parities and calculated for the last three years available, is less than 90 percent of the Community average, and which have a programme for meeting the economic convergence conditions referred to in Article 104.

The current recipients of the Cohesion Fund are Greece, Portugal and Spain, together with all of the new Member States (with effect from 2004). Ireland ceased to be eligible at the end of 2003 following the mid-term review. Using GNI data for 2001-03 [vii]. It seems clear that all of new Member States, plus Greece and Portugal, would qualify for the Cohesion Fund post-2006, but that Spain would cease to be eligible.

The implications for Spain of the reform proposals for the Cohesion Fund are illustrated in Figure 5. This shows a dramatic shift in the Spanish situation: from having been the main

beneficiary in 2000-06, no allocation was initially proposed by the Commission. Transitional arrangements were sought and, as already discussed, resulted in funding of €3.25 billion (compared with over €12.3 billion in 2000-06)[viii].

Figure 5: Implications for Cohesion Fund Total Allocations (€m, 2004 prices)



Source: EPRC calculations

Outermost regions

Reflecting the changes to the Treaty regarding the Outermost regions (OMRs), the draft Structural Funds Regulation provides for a special budget line for the seven regions concerned; there was no such special treatment in the 2000-06 period. In the Spanish context only Canarias is designated as an Outermost region.

The allocation for the Outermost regions was around €1100 million for 2007-13 under the Commission proposal, of which about €493 million was for Spain. During the negotiations, these allocations fell to around €983 million and €437 million respectively. In addition, however, a sum of €100 million was allocated specifically to Canarias, although the budget line was not specified. Taking the OMR and the Phase-in allocations together, the allocation for Canarias is about 50 percent more in per head terms as for the other Phase-in regions (Castilla-León and Valencia).

Regional Competitiveness and Employment

The Regional Competitiveness and Employment Objective contains two strands: Phase-in regions (former Objective 1 regions now above the 75 percent threshold even without the statistical effect); and Regional Competitiveness and Employment regions (all regions not classified under the

Convergence, Phase-out and Phase-in headings). For 2000-06, Objective 2 is targeted at areas of industrial, rural or urban change. Objective 3 is not strictly a spatial objective, but rather channels European Social Fund (ESF) monies to all regions not covered by Objective 1 (in Objective 1 areas, ESF monies are incorporated into the overall programmes). By contrast, for 2007-13, it was proposed to abandon spatial targeting of the Objective 2 type in favour of a more thematic, all-region approach. In looking at 2007-13, a key point is that Spain is the single largest beneficiary of Phase-in status, accounting for over 45 percent of the EU population falling into this category (see Figure 6).

Figure 6: Objective 2/3 and Competitiveness & Employment Coverage (% of population)

	2000-6		2007-13	
	Objective 2	**Objective 3**	**Phase-in**	**Competitiveness & Employment**
EU25	15	62.6	4.0	65.1
EU15	18	74.1	4.1	77.1
NMS10	0.9	3.3	3.8	3.3
Belgium	12	87.3		87.6
Czech Rep	3.5	11.4		11.4
Denmark	10	100		100
Germany	13	81.1		81.4
Estonia				
Greece			7.8	0.1
Spain	22	40.2	20.7	41.7
France	31	95.4		97.1
Ireland			26.5	73.5
Italy	13	65.8	2.9	66.9
Cyprus	30	100		100
Latvia				
Lithuania				
Luxembourg	23	100		100
Hungary			27.8	
Malta				
Netherlands	15	98.2		100
Austria	25	96.6		96.6
Poland				
Portugal			2.3	26.1
Slovenia				
Slovak Rep	3.3	11.1		11.1
Finland	31	79	13.0	87
Sweden	14	89		100
UK	24	87.9	4.4	91

Note: Objective 3 covers all areas, except those covered by Objective 1.

Source: Inforegio; EPRC calculations from Eurostat data.

In 2000-06, Objective 2 regions were selected by the Member States in cooperation with the European Commission, subject to a national *quota* – in the Spanish case around 22 percent of the population (8.8 million inhabitants). Regarding Regional Competitiveness and Employment regions, the key difference for the 2007-13 period is that assistance will not be limited to designated areas

but, instead, will be allocated on a thematic basis. In effect, this means that the eligible areas will rise from 22 percent of the population under Objective 2 to 41.7 percent under the Regional Competitiveness and Employment Objective. Nevertheless, combining Objective 2 and 3 funding for 2000-06 and comparing this with 2007-13 show a clear decline in funding in the course of the negotiations. EPRC calculations suggest that Spain's share of EU15 Objective 2/3 funding would fall from around 10.5 percent in 2000-06 to around 8 percent in 2007-13.

II.2.Regional-level implications of Cohesion policy reform

Turning to the sub-national level, the overall fall in Convergence allocations to Spain is closely related to the changing eligibility of the Spanish regions for Cohesion policy support. As can be seen from Figure 7, only four of the current 12 Objective 1 regions (Galicia, Castilla-La Mancha, Extremadura and Andalucía) retain Convergence region status. Of the other full Objective 1 regions, four are due to be classified as Phase-out regions (Asturias, Región de Murcia, Ceuta and Melilla) and two as Phase-in regions (Castilla-León and Valencia) while, despite being a Phase-in region, Canarias will receive significant extra funding due to its Outermost region status.

It is not possible to determine the ultimate impact of the above changes in eligibility and allocations on the funding provision for individual regions. The main reason for this is that there is not a direct relationship between the Berlin funding methodology and levels of support distributed to the regions, notwithstanding the fact that the Berlin methodology for the allocation of Objective 1 support is determined 'bottom up' on the basis of NUTS II disparities in GDP per head and unemployment rates. The lack of a direct relationship partly reflects the operation of multi-regional programmes and partly national government decisions on the distribution of funds. These arrangements are defended by the central government on the grounds that the internal distribution of funding is largely a Member State responsibility (the Commission's allocations are only "indicative") and also because it has important competencies in policy areas within the remit of Cohesion policy. Moreover, as the Structural Funds represent only one of the instruments within the overall architecture of central government investment activity in the regions (others include the Inter-Territorial Compensation Fund, domestic regionalised or non-regionalised sectoral investments, and investment from other public sector agencies/bodies), the national view is that it is the aggregate "policy-mix" that should guide decisions over redistributive outcomes rather than a strict adherence to EU funding formulae under a single instrument.[ix]

Nevertheless, because of the 'bottom-up' nature of the funding formulae, it is possible to establish the *theoretical* allocations to each region for 2007-13 and to compare these with the *theoretical* allocations under the Berlin formula in 1999 and the actual allocations for the 2000-06 period. The theoretical allocations should be treated with caution since they do not represent

actual outcomes; however, they do illustrate the impact of changes in eligibility and prosperity, as well as negotiating prowess, on the distribution of funding.

Figure 7: Changes in Objective 1 Status 2000-06 / 2007-13

	2000-6	**2007-13**
Andalucía	Objective 1	Convergence
Castilla-La Mancha	Objective 1	Convergence
Extremadura	Objective 1	Convergence
Galicia	Objective 1	Convergence
Asturias	Objective 1	Phase-out
Murcia	Objective 1	Phase-out
Ceuta	Objective 1	Phase-out
Melilla	Objective 1	Phase-out
Castilla y León	Objective 1	Phase-in
Valencia	Objective 1	Phase-in
Canarias	Objective 1	Phase-in; OMR
Cantabria	Objective 1 phasing-out	Competitiveness & Employment

Source: Inforegio and FP Working Document Fiche 57, Rev 2.

Convergence regions

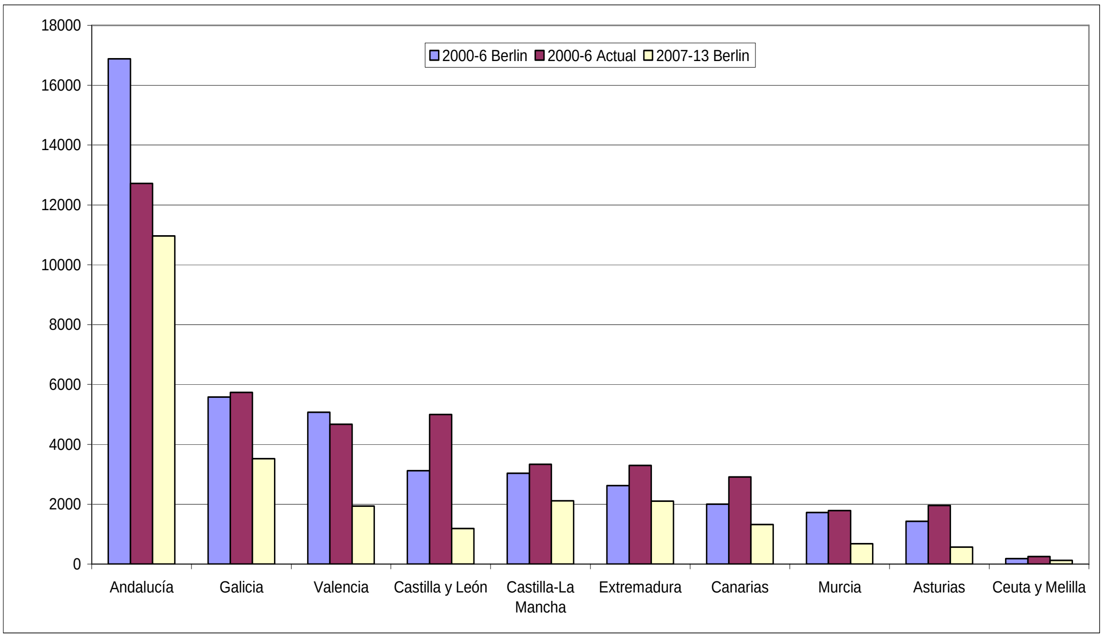
The discussion that follows focuses on the theoretical funding allocation to Objective 1 regions in Spain, set in the context of actual funding allocations for 2000-06. These regions account for just over 58 percent of the Spanish population and almost 70 percent of Spanish commitment appropriations for 2000-06. A further 20 percent is accounted for by the Cohesion Fund, but as this is not explicitly regionalised, it is not possible to draw conclusions for the regions about changes in the Cohesion Fund allocation.

A key point to note is that the overall decline in funding in Spain derives from a fall in Convergence funding which is, itself, largely a product of the relative improvement in prosperity of the Spanish regions. As such, all the traditional Objective 1 regions see a significant decline in their allocations under the formula for 2007-13 (see Figure8). It is of note that there is a large degree of variation depending on whether the calculations are based on 2000-06 Berlin-method allocations or actual allocations.

Under the 2000-06 Berlin methodology scenario, most regions fall into one of two groups: those where the decline in allocations is around 60 percent – Valencia, Castilla-León, Murcia and Asturias-; and those where the reduction is around 30 to 35 percent – Andalucía, Galicia, Castilla-La Mancha, Canarias and Ceuta and Melilla-. The impact of the special additions in mitigating the reduced allocations to Canarias and Ceuta and Melilla is clear from these groupings – their reductions have been pegged at the levels of those applicable to most Convergence regions-. When the theoretical allocations for 2007-13 are compared with the *actual* regional allocations for 2000-

06, the magnitude of decline is different, particularly in the cases of Andalucia, Asturias, Castilla-León, Extremadura, Canarias and Ceuta and Melilla. Under this scenario, three main groups can be identified: Extremadura, Castilla La Mancha and Galicia (where the decline is around 35-40 percent), Ceuta and Melilla, Canarias, Valencia and Murcia (where the range is from 50 percent to over 60 percent) and Asturias and Castilla-León (with falls of 70-75 percent). In contrast to the previous scenario, it is now the region of Andalucía which sees the lowest theoretical fall (around 15 percent), reflecting the significantly lower actual allocation in 2000-06 compared to the Berlin methodology allocation - and this despite its relatively strong growth performance over the period[x].

Figure 8: Allocations to Objective 1 Regions 2000-06 and 2007-13 (€m, 2004 prices)



Source: EPRC calculations and Marco Comunitario de Apoyo (2000-2006) para las Regiones Españolas del Objetivo 1.

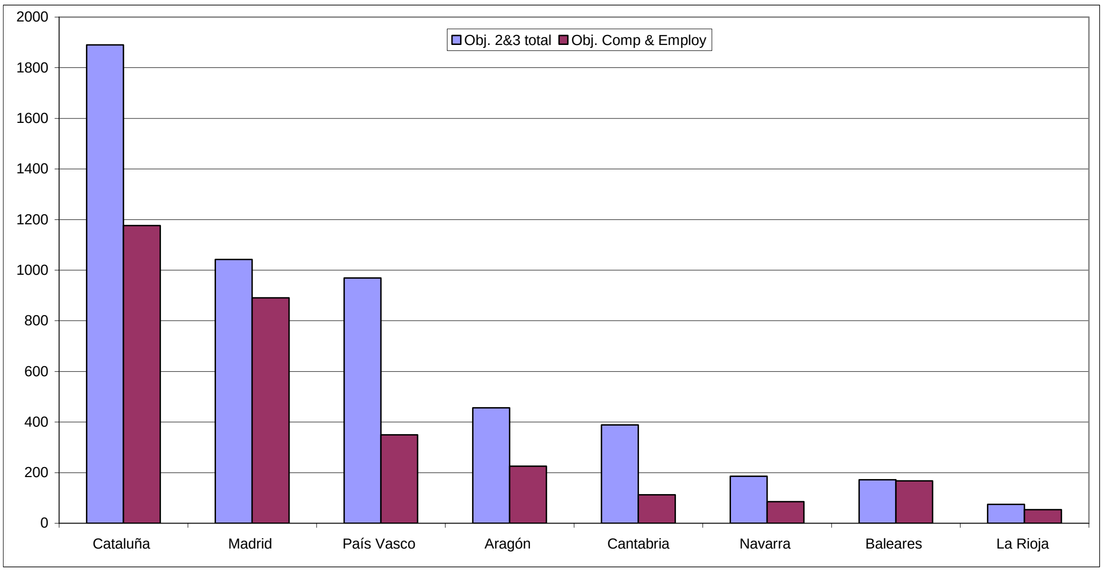
Regional Competitiveness & Employment

The basis for allocating funding under the Regional Competitiveness and Employment strand is significantly different from that under Objective 2; in particular, there are no specifically-designated assisted areas. This is not, however, to say that, in practice, funding will be allocated on a flat per capita basis; as for the Convergence regions, the actual allocation will doubtless take account of a number of criteria. Nevertheless, because Competitiveness & Employment region coverage is almost double Objective 2 coverage, and overall funding has declined, the impact on the existing recipients is likely to be significant (see Figure9).

Cantabria aside (where the ending of Objective 1 transitional arrangements implies a 70 percent decline in actual receipts), the most significant differences between (Objective 2 and 3) allocations and those implied by the allocation keys used for the Regional Competitiveness and Employment Objective concern País Vasco, Navarra and Aragón where the percentage decline is in

the order or 65, 55 and 50 percent respectively. At the other end of the scale, the relative decline in Baleares (2 percent) and Madrid (15 percent) is much lower, mainly reflecting the significantly lower Objective 2 eligible population coverage in the 2000-06 period. In the remaining two intermediate regions, Cataluña and La Rioja, the decline is in the order of 40 to 30 percent respectively. The differential impact on the regions is also clearly in the per capita allocations[xi].

Figure 9: Allocations to Objective 2/3 Regions 2000-06 and Competitiveness & Employment Regions 2007-13 (€m, 2004 prices)



Note: The region of Cantabria was a transitional Objective 1 region in 2000-06.
Source: EPRC calculations, Plan Objetivo No.2, Zonas españolas incluidas en el Objetivo nº 2 de los Fondos Estructurales Europeos and Marco Comunitario de Apoyo 2000-2006 España Objetivo nº 3: Apoyar la adaptación y modernización de las políticas y sistemas de educación, formación y empleo.

However, as stressed earlier, there is not necessarily a direct connection between the allocation keys produced on the basis of theoretical allocations under the Commission methodology and actual receipts. Indeed the Commission has written to all the Member States suggesting an alternative allocation, based on weightings that it considers are more appropriate for the country concerned.[xii] Moreover, in practice, it will be for the Member States to decide how to share out Regional Competitiveness and Employment funding.

II.3. Some reflections about policy and institutional impacts

This section provides some reflections on the policy and institutional impacts of the reform based on interviews with national and regional programme managers in late 2005/early 2006.

In general, the Spanish regions welcomed the Commission's regulatory proposals relating to the future of Cohesion policy. The regional view was that they did not represent radical change but were rather a progression of current arrangements. While, based on past experience, there were some doubts about whether simplification would be achieved in practice, the steps taken to

streamline programming were viewed positively. This includes the dropping of the Programme Complement, the Community Support Framework and Regional Development Plans. The National Strategic Reference Framework was also broadly welcomed, as was the less onerous approach to Financial Tables. There was less of a common regional view with respect to mono-fund programmes, some feeling that this would lead to a less coordinated approach while others considered that the new approach was more in line with the realities of the situation. However, most other key changes generated a positive regional response: including the integration of the Cohesion Fund with mainstream programmes; the move to coordinate audit controls and reduce duplication in line with the proportionality principle; and the proposal to decentralise decisions on expenditure eligibility to the national level.

From a regional perspective, the budgetary impact of the new financial agreement is obviously of considerable potential significance, especially for those regions losing full Convergence status – with Asturias, Murcia and Ceuta and Melilla becoming Phase-out regions; Castilla-León, Valencia and Canarias qualifying as Phase-in regions (though Canarias was also designated an Outermost region); and with Cantabria, a current Objective 1 Phase-out region, becoming a Regional Competitiveness and Employment region. In addition, there are other potential "knock-on" effects for the regions concerned. For instance, nationally-funded regional incentives in Spain were restricted to areas qualifying for regional aid under Article 87(3)(a) of the EU Treaty (that is, the full Convergence regions) in 2000-06; regions which lost this status may not have qualified for national regional aid in 2007-13. In similar vein, the Inter-Territorial Compensation Fund, which operates as a fiscal equalisation mechanism in Spain, was restricted to Objective 1 regions with GDP (PPS) per head of less than 75 percent of the EU average.

However, within the devolved Spanish system, there is a keen awareness of these issues – both the direct impact of the reduced availability of the Structural Funds (and associated increased demands for domestic co-finance) and related impacts in terms of regional aid and access to the Inter-Territorial Compensation Fund. There was also seen to be scope to take steps to offset (at least some of) their negative effects. In this context, it is interesting that some regions (eg Castilla-León) had requested a change of treatment, while others (eg Cantabria) claimed to have negotiated continued eligibility for both regional aid and the Inter-Territorial Compensation Fund despite the change in designation status. It will be interesting to see to what extent and in what way national "buffers" will be introduced to moderate the impact of the proposed changes to Structural Funds flows. Certainly Spain has a number of levers which it can pull in this regard – relating to the domestic distribution of the mainstream Structural Funds, the Cohesion Fund and the Technological Fund, not to mention various domestic adjustments, not least in the form of the forthcoming reforms to the regional government financing model in Spain.

Moving on to consider implementation issues, the process of developing the National Strategic Reference Framework (NSRF) was perceived to be going well from a central government perspective (where the Directorate General for EU Funding has always played a strong coordinating

role in the development of programmes) but received more mixed reviews from the regions. While the regions were asked to make strategic inputs in the first half of 2005, this was not always easy to achieve given the uncertainty at the time about levels of Cohesion funding and the fact that not all of the domestic policy building blocks were in place. Moreover, a number of regions expressed some dissatisfaction with transparency and feedback levels, though others viewed the process as being well on track given the uncertainties and delays at the EU level. Overall, the view was that the potential for a timely start to the next programme phase was higher than last time round.

The Lisbon agenda already has a degree of prominence in Spain and indeed within the current generation of EU programmes. The expectation was that there would be few difficulties in meeting the Lisbon targets set under Cohesion policy. If there are challenges then they will tend to be in the Convergence regions where the general view was that there remains a need for broader infrastructure support and that there may be dangers if this is diluted for Lisbon-related reasons[xiii].

III. ECONOMIC IMPLICATIONS

While the previous section of this paper have focussed on the quantitative results – (budgetary allocations committed to Spain) and qualitative aspects (related to the negotiations that preceded the adoption of the 2007-2013 financial perspective), this section examines the economic implications of the new policy Framework, not least because of the importance of such issues in the context of current Cohesion policy reform debates. The significant cuts in EU Cohesion policy allocations over the 2007-13 period are likely to have important economic consequences although, as yet, only a limited number of studies have explored the potential future impacts. Before reviewing the results of the Impact Analysis for the 2007-13 period, a comparative overview of the scale and scope of funding allocated to Spain over the last three programming periods is provided, followed by a discussion of the main results of the impact evaluations over the same period.

III.1. Scale and scope of funding in Spain

The Structural Funds have contributed substantial amounts of aid to the least developed countries and regions of the EU. Spain has been the main beneficiary with total receipts over the last three funding cycles amounting to €131.3 billion (Figure 10).

Figure 10: EU Cohesion Policy Allocations to Spain 1989-2006 (€m, 2004 prices)

	1989-93	1994-99	2000-06	1989-2006
Objective 1	13,371	31,668	42,061	87,100
Structural Funds Total	18,707	41,080	49,569	109,356
Cohesion Fund		9,574	12,322	21,896
Total	18,707	50,654	61,890	131,251

Source: Cordero Mestanza, G (2005).

While Spain has been the largest beneficiary in absolute terms, the flows to other Cohesion countries have been greater in relation to GDP or investment.[xiv] As illustrated in the Second Cohesion Report (Figure 1), in the Cohesion countries the Structural Funds averaged 1.4 percent of GDP over the 1989-93 policy phase (0.7 percent for Spain). Following a doubling of resources under the Delors-II package, this share increased to 2 percent over 1994-99 (1.5 percent for Spain), before falling to an estimated average of 1.6 percent of GDP in the current 2000-06 programming period (1.3 percent for Spain). The funds also represent significant amounts of total investment in the Cohesion countries (again, see Figure 1), particularly in Greece and Portugal.

Figure 11: Economic Effects of EU Structural Funds on Cohesion Countries

	Share in GDP (%)			Share in Fixed Capital Formation (%)		
Policy Phase	**1989-93**	**1994-99**	**2000-06**	**1989-93**	**1994-99**	**2000-06**
Greece	2.6	3.0	2.8	11.8	14.6	12.3
Ireland	2.5	1.9	0.6	15.0	9.6	2.6
Portugal	3.0	3.3	2.9	12.4	14.2	11.4
Spain	0.7	1.5	1.3	2.9	6.7	5.5
Total	**1.4**	**2.0**	**1.6**	**5.5**	**8.9**	**6.9**

Source: Second Cohesion Report, p122.

The receipt of sizeable amounts of Structural and Cohesion Funds has spurred significant interest from academics and policymakers alike on the economic impact of EU Cohesion policy in Spain. The key studies are reviewed in the following two sections: first, impact analyses over the last three programming cycles are considered, followed by an overview of more recent evaluations which analyse the potential impact of the cuts in EU Cohesion policy funding post 2006.

III.2. Present and past impacts: 1989-2006

The techniques and methods used to analyse the impact of the Structural Funds have varied widely, ranging from bottom-up (micro-level) to top-down (macro) impact analyses.[xv] A significant body of research has employed macroeconomic modelling techniques to model economy-wide interactions and to establish counterfactual scenarios with the aim of quantifying the impacts of interventions (particularly in terms of GDP) in the absence of EU Cohesion policy. Three main types of macroeconomic model can be distinguished: econometric models (e.g. HERMES, HERMIN, Wharton-UAM or QUEST II); general equilibrium models; and input-output models.[xvi]

Beginning with econometric models, the official evaluations of the Objective 1 Community Support Framework in Spain have utilised the so-called Hermin model.[xvii] The results of simulations by Sosvilla and Herce (2004a) for the last three programming periods (Figure 12) show that the Structural Funds have had positive effects on a range of economic variables, generating greater impacts over time in line with the increased allocations from period to period.[xviii] It is estimated that the Objective 1 Community Support Framework (CSF) has led to an average annual increase in the growth rate of 0.38 percent between 1989 and 2006. This represents a yearly increase in GDP of

€25.7 billion, which has allowed the total level of income per capita in Objective 1 regions to rise by an additional €637.7 per annum over the last 18 years.

With respect to employment, it is estimated that almost 299,000 jobs were created or maintained each year as a result of the CSF, implying that the unemployment rate would have been 0.17 percent higher in the absence of EU structural funding between 1989 and 2006. Turning to the impact on productivity, the model estimates a cumulative increase in labour productivity (expressed as an index) by 2006 of 4.8 percentage points compared to a no-CSF baseline scenario. This represents around one quarter of the total increase in the labour productivity index over the 1989-2006 period. Considering the contribution of the Structural Funds to the stock of capital, the model estimates an increase of €77.2 billion in the average private capital stock and €25 billion in public capital as a result of the implementation of the CSF over the three funding cycles.

Last, in terms of impacts on convergence with the EU, the model estimates that around a third of the convergence witnessed between Spain and the EU15 between 1989 and 2006 (from 74.3 percent to 89.4 percent of the EU15 average) can be attributed to the impact of the Structural Funds.

Figure 12: Hermin Model Results for Spain (Deviation from No CSF Scenario)

	1989-1993	1994-1999	2000-06	1989-2006
Real Output*	7.90	25.80	42	25.70
Income p.c.**	200.35	654.15	1027.15	637.73
Income p.c. Index***	1.33	4.01	5.76	-
Employment****	153.53	317.07	492.13	298.63
Unemployment rate *****	-0.12	-0.26	-0.15	-0.17
Labour productivity	1.2	3.3	0.3	4.8
Private capital stock[2]	17.06	65.35	141.38	77.23
Public capital stock	5.31	21.74	45.43	25.0

Notes: (*) Difference in absolute values (annual average in €bn, 1999 prices). (**) Difference in absolute values (annual average in €, 1999 prices (***) Difference in average index (EU15 = 100). (****) Difference in absolute values (annual average, thousands employed) (****) Difference in percentage of active population. (1) Difference in productivity index (index base of 100 in 1988) (2) Difference in average stock over the period (in €bn 1999 prices)
Source: Sosvilla and Herce (2004a)

The HERMIN-Spain model has also been used to estimate the regional impacts of the Objective 1 CSF,[xix] and has been adapted in order to allow its application to specific Objective 1 regions (e.g. Andalucía and Castilla-La Mancha) and certain Objective 2 regions (e.g. Madrid). For example, for the 1989-2006 period, it is estimated that the Structural Funds made a contribution to annual real output growth of 0.02 percent in Madrid[xx], contrasting with 0.64 percent in Castilla-La Mancha over the 1989-99 period where much higher levels of funding have been received.[xxi]

A range of other econometric studies have employed different methodologies to the Hermin model, focussing on different time periods, specific regions or groups of regions (see Figure 3). Most studies have tried to determine the contribution to economic and social convergence through macroeconomic variables such as output, income per capita and employment, or to quantify the reduction in the gap between the richest and poorest regions. In general, the results are in line with those of the Hermin model, underlining the positive effects of the Structural Funds on economic growth and national/interregional convergence.

For example, a study by De la Fuente (2003a,b), involving the estimation of an aggregate production function and an employment equation, found an average contribution to GDP growth in Objective 1 regions of 1 percent per annum (over the 1994-99 and 2000-06 programming periods) and 0.4 percent per annum to employment growth (1994-99).[xxii] This accounts for two thirds of the convergence between Spain and the EU (over the 1993-2000 period) and has reduced the increase in inter-territorial disparities between the richest regions and poorest Objective 1 regions by around a half (between 1993 and 2001)

Another study in this tradition is provided by Murillo (2005), also based on the estimation of an aggregate production function for the public and private sectors of the economy but restricting itself to the study of Structural Funds impacts in Andalucía over the 1994-99 period.[xxiii] The author finds that EU funding (including the Community Initiatives and the Cohesion Fund as well as the Objective 1 CSF) have contributed an annual average of 1.08 percent to GDP growth over the period analysed, slightly above De la Fuente's results for all Objective 1 regions. A different econometric approach is used by María-Dolores and García (2002), who employ beta convergence contrasts and selectivity models to estimate the impact of the Structural Funds on convergence. The estimated results suggest that the Structural Funds have made a positive, but modest, contribution (0.27 percent) to regional convergence in the Spanish regions over the 1987-97 period.

Figure 13: Overview of Selected Impact Studies

Authors	Objective	Domain	Period	Methodology	Sources	Key resuts
Morillas, Moniche and Castro (1999)	Analyse the effects of the Structural Funds on industrial sectors within the Andalusian economy	Andalucía	1989-1993	Input-output	Instituto de Estadística de Andalucía (IEA) and INE	1) Increase in public works investments 2) Increase in GVA and employment 3) A more fragmented production structure and economic activity spillovers
Dones and Pérez (2002)	Evaluate the impact of the Structural and Cohesion Funds on regional demand	All regions	1995-1999	Input-output	Banco de España	1) Average effect in Obj1 regions of 2.1% (GVA) and 2.6% (employment), 0.7% and 0.9%, respectively in Obj2 regions 2) Spillover effects on more developed regions
María-Dolores and García (2002)	Estudiar los efectos de las ayudas europeas sobre la convergencia regional	All regions	1987-1997	Conditioned beta convergence contrasts and selectivity models	Series Fundación BBVA	Positive, but modest, contribution to regional convergence
Bosch, Espasa and Sorribas (2003)	Analyse the contribution of the Structural Funds to technical efficiency	All regions	1986-1996	Production frontier techniques	Correa y Maluquer (1998), INE and Fundación BBVA-IVIE	Positive effects on levels of efficiency
De la Fuente (2003)	Evaluate and analyse the impact of the Structural Funds on real convergence with the EU and internal cohesion	Objective 1 regions	1994-99, 2000-06	Econometric model (production function and employment equation. Panel data.	Fundación BBVA-IVIE, Fundación Bancaja, DGFCFT	1) Contribution to GDP growth in Obj1 regions of 1% and to employment growth of 0.4%. 2) Reduction in inter-territorial disparities and increasing EU convergence
Murillo (2005)	Analyse the effects of investment co-financed by the Structural Funds on the economy of Andalucia	Andalucía	1994-1999	1) Input-output 2) Econometric model (production function for private sector. Co-integration techniques for time series and dynamic panel.	Fundación BBVA-IVIE, IEA (TIOAND-95), DGFCFT (2001), DGFE J. Andalucía (2001 and 2002).	1) Contribution to average GDP growth of 1.08% p.a. (supply-side effects) 2) Concentration in construction sector (infrastructures). Deepening of traditional specialisation and fragmented production system.
Sosvilla and Murillo (2005)	Analyse the supply-side effects of Structural Funds support for infrastructure	Andalucía	1994-1999	Econometric model (co-integration techniques with time series of a production function	Series de la Fundación BBVA-IVIE, DGFCFT(2000) and DGFE J. Andalucía (2000 and 2001)	Growth of the Andalucian economy of 0.27% above growth without support for infrastructures
Cardenete and Lima (2005)	Measure the impact on total output and income of economic activities related to the receipt of Structural Funds	Andalucía	1989-93, 1994-99, 2000-06	Applied General Equilibrium Model	Social Accounting Matrices	Comparing 3 periods, the effects on regional output, prices and net income over the 1994-99 period are emphasised

A second well-known approach used to evaluate the impact of the Structural Funds is based on input-output techniques.[xxiv] Morillas *et al.* (1999) and Dones and Pérez (2002) focussed on measuring the demand-side effects of the Structural Funds using the input-output tables of a specific region (Andalucía, in the former instance) or all Spanish regions (in the latter case). In addition to the positive impact on gross value added and employment which was observed, both studies drew attention to the economic spillover effects on other more developed regions, which can work against the objective of regional convergence.[xxv]

A last group of studies have used alternative methodologies or variables to evaluate the impact of Structural Funds support. For instance, Cardenete and Lima (2005) constructed an applied general equilibrium model with social accounting matrices to compare the effects of the Structural Funds over the last three programming periods in Andalucía.[xxvi] The authors highlighted significant impacts, particularly in terms of output and prices during the second programming period (1994-99). Bosch *et al.* (2003) applied production frontier techniques to assess the impact of the Structural Funds on technical efficiency in all Spanish regions over the 1986-96 period.[xxvii] The results of their analysis suggest that the Structural Funds have made a positive contribution to efficiency although, given the nature of the model, it was not possible to measure the magnitude of this contribution.

However, there are also other papers that put into question the positive contribution of the structural aid in the results achieved in terms of convergence within the EU. In this line, Martin (1999)[xxviii] predicts -using a theoretical model of endogenous growth with two regions, where industrial location and public infrastructure play a key role - that transport infrastructure between rich and poor regions will produce an increase in the concentration space. Boldrin and Canova (2001)[xxix] found no clear evidence that European regional policy achieves a significant impact on the convergence between European regions, and proposes a thorough review of the same for its application to new Member States. Finally, Ederveen et al. (2006)[xxx], show - through an analysis of panel data for 13 countries in the European Union - that the fact that Cohesion policy contributes to economic growth depends crucially on the institutional capacity of regions to which it is addressed.

III.3.Future impacts: 2007-13

Looking at the current 2007-2013 programme period, some studies have begun to analyse the potential impact of the reduction in EU Cohesion policy funding for Spain. A report for the European Commission by Bradley *et al.* (2004) reviewed the macroeconomic impacts of Cohesion policy reform based on the financial proposals contained in the Third Cohesion Report.[xxxi] The study, which used the HERMIN model developed for the Cohesion countries (Greece, Portugal, Ireland and Spain), included methodological modifications in order to estimate future impacts in the ten new Member States. In particular, it attempted to quantify the differential impacts between resources assigned to the Convergence objective and the Cohesion Fund. In this respect, one of the report's conclusions concerned the need to find an appropriate balance between funding for

infrastructure and human capital investment in order to achieve greater levels of convergence amongst countries and regions in the future.

In terms of its main results, the study estimated that the Structural Funds allocation to Spain (including domestic finance) for the 2007-13 period will account for 0.7 percent of GDP, just under half the share for the current 2000-06 period (see Figure 11). This contrasts with around 2 percent in Greece and Portugal and 5-6 percent in the new Member States. Considering impacts, the model simulations suggested that the increase in the level of GDP by the year 2020 in Spain (relative to a no Structural Funds baseline position) was of the order of 0.3 percent. Comparable results for other EU15 countries and regions included: 0.15 percent for East Germany; 0.3 percent for Greece; 0.7 percent for the *Mezzogiorno*; and 1.7 percent for Portugal.

The study also estimated "cumulative multipliers" for the Member States (defined as the cumulative percentage increase in GDP over the cumulative CSF share in GDP). The aim was to try to model the longer-term increases in GDP through supply-side processes which extend beyond the next programming period (captured through the incorporation of externality parameters within the model). The multiplier for Spain (1.7 percent) placed it within an intermediate group of countries, including Portugal (2 percent), Latvia (1.8 percent), Romania (1.8 percent) and Hungary (1.6 percent)); the results for this group were interpreted as small "but still very significant".

The above results show the future impact of the Structural and Cohesion Funds in a positive light by comparing the impact estimations of a given future allocation of resources for 2007-13 with a "zero-funding" baseline. An alternative baseline scenario could be the continuation of current (2000-06) levels of Cohesion policy support; for the EU15 this would obviously present the results in a more negative light due to their significantly lower levels of Cohesion policy funding post 2006. Although this second scenario was not simulated in the above study, due to the conceptual difficulties involved,[xxxii] other studies have compared future Cohesion policy impacts with those expected under a funding regime similar to that for the present period.

An early study to do this was Martin *et al*. (2002), as part of a broader project investigating the impact of enlargement on the Spanish economy.[xxxiii] Comparing a future reduced funding scenario (for 2007-13) with a baseline of continued Cohesion policy support (equivalent to 2000-06 funding), the Hermin-Spain model simulations for Objective 1 regions estimated a future reduction in GDP of 0.8 percent over the 2007-13 period. The magnitude of decline was somewhat lower (0.3 percent) under a more generous future funding scenario. A more recent analysis (Sosvilla and Herce 2004a), with more realistic assumptions on future levels of Cohesion policy support,[xxxiv] considers two different baseline scenarios (no funding and continued 2000-06 levels of funding) and two different future funding scenarios for 2007-13 (one including transitional support and the other, least likely scenario according to the authors, excluding such support).[xxxv] The results of the simulations suggested that the annual growth rate in real output over 2007-13 would increase by 2.81 percent under the transitional support funding scenario (2.58 percent without transitional

support). If this is compared with a baseline of current levels of funding, where the estimated annual growth rate is 3.10 percent, the implied reduction is of the order of 0.29 percent in annual growth in real output over the 2007-13 period (representing an annual fall in total GDP of €2.66 billion).[xxxvi]

Similar scenarios have been simulated to measure the impact of the funding decline on per capita income. Compared to the current Structural and Cohesion Funds allocation baseline for Objective 1 regions, the estimates suggest a fall of €282.2 in per capita annual income over the 2007-13 period, equivalent to a 0.29 percent reduction in the annual income per capita growth rate. This implies a decline in per capita income convergence between Spain and the EU15 of 2 percentage points by 2013.[xxxvii]

Apart from the Hermin model estimates, other econometric studies have explored the future impact of reduced Cohesion policy funding by region or category of region. For example, De la Fuente's (2005)[xxxviii] estimates suggest significant impacts, with a fall in average annual growth of 0.25 percent for the whole of Spain. For regions losing full Convergence status the fall is greater still (-0.38 percent for Phase-out regions; -0.42 percent for Canarias; and -0.48 percent for Phase-in regions). Last, Flores de Frutos *et al.* (2005) estimate that the reduction in EU Cohesion policy funding for Spain over the 2007-13 period will lead to a 4.4 percentage point reduction in potential output growth (0.6 percent annually). At the regional level, the relative loss (as a percentage of regional GDP) is estimated to be greatest in Extremadura (-14 percent), Castilla-León (-11 percent), Murcia (-9.4 percent), Asturias (-9 percent), Canarias (-8.9 percent) and Galicia (-8.5 percent). In terms of employment, the reduction over the 2007-13 period is estimated at 1,564,822 jobs (223,546 annually)[xxxix].

IV. MAIN CONCLUSIONS

Spain was the single largest beneficiary of the structural actions budget for 2000-06, accounting for almost 27 percent of total commitment appropriations across the EU15. Enlargement, shifting EU averages and domestic growth have impacted on the eligibility of Spanish regions for Cohesion policy support, reducing the available allocation to Spain from around €60 billion (in 2004 prices) for 2000-06 to under €30 billion for 2007-13 under the Commission's initial proposal and just over €30 billion in the final UK Presidency agreement. All Cohesion policy categories experienced significant cutbacks; on the other hand, there were some notable additional funding sources won during the negotiations, including transitional Cohesion Fund support of €3250 million, an extra €2000 million of ERDF assistance for Spanish R&D and specific provisions of almost €537 million for Canarias and €50 million for Ceuta and Melilla. Overall, the fact that the Spanish Cohesion policy budget increased in the course of negotiations which saw a reduction of almost 10 percent in total Cohesion policy funding was a significant achievement.

Even so, the implications for Spain of a budgetary cutback of the order of one-half are obviously major. Moreover, the reduced funding does not apply uniformly but has potentially significant differentiated regional impacts. Thus, in most continuing Convergence regions (Extremadura, Castilla-La Mancha and Galicia) a theoretical funding decline of the order of 35-40 percent is experienced, the exception is Andalucia where the cutback is closer to 15 percent due to the significantly lower 2000-06 allocation relative to the Berlin-based methodology. For those regions losing Objective 1 status, two groups can be identified: those where the decline ranges from 50 percent to around 60 percent - Ceuta and Melilla, Canarias, Valencia and Murcia - with Ceuta and Melilla and Canarias at the lower end of the range due to the additional provisions in the latter stages of the negotiations; and those witnessing a decline of 70 to 75 percent - Asturias, Castilla-León and Cantabria - largely because of the significantly greater actual 2000-06 allocation than under the theoretical Berlin method in the former two regions and the ending of transitional arrangements in the latter.

With respect to the traditional Objective 2 (actual Regional Competitiveness and Employment Objective) regions, the magnitude of decline is greatest in País Vasco, Navarra and Aragón (65, 55 and 50 percent respectively). This is followed by an intermediate group comprising Cataluña and La Rioja where the fall is in the order of 40 percent and 30 percent respectively. At the other end of the scale, the decline in Madrid (15 percent) and, particularly Baleares (2 percent), is much lower, reflecting the relatively lower Objective 2 eligible population coverage in the 2000-06 period.

Such differential impacts obviously increase the pressures on the Spanish government to modulate the impact of the Cohesion policy funding changes; it remains to be seen, however, just what will be done in this regard.

On the other hand, in general, the assessment by the evaluation studies reviewed above is that EU funding does appear to have contributed significantly to the economic growth experienced since the late 1980s. Evaluations employing the so-called HERMIN model have estimated that the Objective 1 Community Support Framework (which accounts for the bulk of EU funding in Spain) has led to a 0.4 percent average annual increase in the GDP growth rate between 1989 and 2006. Other studies using different models and focussing on the last two programming periods (where there were significantly higher levels of funding allocated to Spain) have estimated an annual contribution to growth of around 1 percent per annum. The effects on employment have also been significant, with some estimates suggesting that an additional 299,000 annual jobs have been created or maintained between 1989 and 2006.

As a result, the relative position of Spain (and most of its regions) has improved markedly when set against EU averages. Indeed, some of the studies reviewed above estimate that as much as 20 to 30 percent of the convergence between Spain and the EU15 is due to the impact of EU Cohesion policy. As discussed in detail in earlier sections, this, plus the impact of enlargement, has

had a major impact on the future eligibility of the Spanish regions for Cohesion funding and, consequently, on overall funding levels for Spain. Indeed, funding for the 2007-13 period is only just over half that for the previous policy phase. With levels of funding set to fall to this degree, the future impact of EU Cohesion policy on the Spanish economy is likely to be significantly lower too.

Compared to a situation where current levels of support would continue, Hermin model estimates suggest that annual growth in real output over the 2007-13 period would be almost 0.3 percent lower (representing yearly decline in total GDP of €2.66 billion). In line with previous sections, the impact of the funding decline is likely to have quite varied impacts. Estimates by De la Fuente suggest that, while the average decline in annual growth in Spain is around 0.25 percent (similar to the Hermin model results), the impact is significantly greater in those regions losing full Convergence status (-0.38 percent for Phase-out regions; -0.42 percent for Canarias; and -0.48 percent for Phase-in regions).

It is important, however, to be cautious with regard to the exact magnitudes of the quantified impacts and the comparability of the results of the different models, given the different methodologies and assumptions upon which they are based. In addition, it is important to bear in mind that the true impact of the Structural Funds could only be formally established if it were possible to determine what would have occurred without them (the 'counterfactual problem'). This is no easy task as the impacts appear only after long periods, beyond a five or six-year programming cycle, and are extremely difficult to disentangle from other factors, notably other Community (or national) policies and economic cycles.

Finally, it also seems essential to stress here that the adoption of the 2007-2013 financial perspective, in general, and of the Cohesion policy regulations, in particular, involved a long process of negotiation among EU Member States. Throughout these negotiations, changes were not only made to Cohesion policy budget allocations and priorities - as we have seen in section II.2 and II.1- but also to important aspects of the Commission's regulatory proposals at a more qualitative level.

In the current context, and as agreed during the adoption of the 2007-2013 financial perspective, a review of the EU budget is being currently undertaken. In April 2008, a major conference was held in Brussels discussing reform issues and the challenges posed by the adoption of a common budget by 27 countries. The contributions to the discussion were wide-ranging. Some normative approaches have made proposals about how the budget should be spent and financed, such as a study by De la Fuente *et al.*, 2008[xl] which proposes a generalized compensation mechanism that relates Member State net balances to relative prosperity in order to break the link between the overall budget and redistributive questions. Following the approach of this article, other studies, such as the work of Mojmir *et al.* (2008)[xli], have analysed how the budget has been negotiated in practice and the dominant role of national interests in determining negotiation

outcomes in 2007-2013[xlii]. It is still to be seen whether the budget review will have any impact on the rules governing negotiation dynamics in the future.

Notes and References

[i] European Commission, *Building our common future. Policy challenges and budgetary means of the enlarged Union 2007-2013*, COM(2004) 101 final, 10 February 2004

[ii] See the Temporary Committee on Policy Challenges and Budgetary Means of the Enlarged Union 2007-2013 at http://www.europarl.europa.eu/comparl/tempcom/finp/default_en.htm

[iii] For a more detailed discussion of the Spanish position on the Luxembourg presidency negotiations see: Navarro, A and Viguera, D (2005) 'España y las perspectivas financieras de la UE', Política Exterior, No.106, July/August 2005.

[iv] UK Presidency Website, European Union Financial Perspectives 2007-13, United Kingdom Presidency Negotiating Box available at http://www.eu2005.gov.uk, 5 December 2005. Although this may seem late in the day, it should be noted that the Luxembourg Presidency did not produce detailed figures until the Fourth Negotiating Box in early June.

[v] UK Presidency Website, European Union Financial Perspectives 2007-13, United Kingdom Presidency Negotiating Box available at http://www.eu2005.gov.uk, 14 December 2005.

[vi] In both cases, it compares the outcome of the 1999 Berlin European Council with the third UK Negotiating Box (UKNB3) and, at the national level, with the Commission proposals (COM prop).

[vii] EPRC calculations based on the DG ECFIN AMECO database (Yuill *et al.*(2006) "Cohesion Policy Reform: the implications for Spain", *Documento de trabajo nº30/06*, IEF, Madrid).

[viii] Check in figure 5 the difference between the Berlin European Council (corresponding to the allocation for the period 2000-06), the Commission proposal, and finally the approved allocations for the Cohesion Fund 2007-13 (third proposal the British presidency).

[ix] This view is also supported by the current government. See the intervention by Pedro Solbes in the parliamentary committee for Economy and Finance, 24 April 2006.

[x]The per capita allocations mirrors the impact of the special pleading made in the budget negotiations for Ceuta and Melilla and Canarias; these receive more funding than the phase-out and phase-in regions, respectively.

[xi] For more information see Yuill *et al*.(2006) "Cohesion Policy Reform: the implications for Spain", *Documento de trabajo nº30/06*, IEF, Madrid.

[xii] These letters are not in the public domain and it is not known what breakdown the Commission has suggested to Spain.

[xiii] To understand policy and institutional impacts, see Yuill *et al*.(2006) "Cohesion Policy Reform: the implications for Spain", *Documento de trabajo nº30/06*, IEF, Madrid, P. 44-64.

[xiv] Cordero Mestanza G (2005) 'La rentabilidad económica y social de los Fondos Estructurales: experiencia y perspectivas' *Presupuestos y Gasto Público*, Secretaría General de Presupuestos y Gastos, Instituto de Estudios Fiscales

[xv] Bradley J (2006) 'Evaluating the Impact of European Union Cohesion Policy in Less-Developed Countries and Regions' *Regional Studies*, Vol. 40.2, pp. 189–199

[xvi] Lolos S (2001) 'The Macroeconomic Effect of EU Structural Transfers on the Cohesion Countries and Lessons for the CEECs' Interim Report IR-01-044/October 2000, International Institute for Applied Systems Analysis. For a different categorisation and a comparative literature review of the different models see: Mairate A and Hall R (2001) 'Structural Policies' in Hall R, Smith A and Tsoukalis L (eds.) Competitiveness and Cohesion in EU Policies, Oxford University Press, Oxford; and Ederveen S, Gorter J, de Mooij R and Nahuis R (2002) Funds and Games: The Economics of European Cohesion Policy, CPB working paper, Netherlands

[xvii] The model was developed jointly by the Fundación de Estudios de Economía Aplicada (FEDEA) in Spain, the Economic and Social Research Institute in Ireland and the Portugues Catholic University in Portugal. For a detailed description of the Hermin-Spain model see: Herce J.A and Sosvilla S (1995) 'HERMIN Spain', *Economic Modelling*, Vol.12, nº3, pp.295-312; Sosvilla-Rivero S and Herce J.A. (2001) 'HERMIN-España, versión 2001', mimeo, FEDEA. For a comparison between the Hermin model and other official models used in Spain, including ex-ante results for 2000-06, see: Ministerio de Hacienda (2001) 'Marco Comunitario de Apoyo (2000-2006) para las regiones españolas del Objetivo 1' Ministerio de Hacienda, Madrid.

[xviii] Sosvilla-Rivero S and Herce J.A. (2004a) 'La Política de Cohesión europea y la economía española: evaluación y prospectiva', Documento de Trabajo 2004-20R, FEDEA, Madrid.

[xix] Sosvilla-Rivero S and Herce J.A. (2004b) 'Efectos de las ayudas europeas sobre las regiones objetivo 1 españolas: un análisis basado en el Modelo Hermín', Papeles y Memorias de la Real Academia de Ciencias Morales y Políticas, Nº12, 136-155.

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[xxi] Sosvilla-Rivero S, Bajo O and Roldán C (2004) 'Assessing the effectiveness of EU's regional policies: a new approach', Economic Working Papers at Centro de Estudios Andaluces, E2004/39.

[xxii] De la Fuente A. (2003a) 'El impacto de los Fondos Estructurales: convergencia real y cohesión interna', Hacienda Pública Española/Revista de Economía Pública, 165, 129-148, Instituto de Estudios Fiscales; De la Fuente (2003b) 'The effect of Structural Fund spending on the Spanish regions: an assesment of the 1994-99 Objective 1 CSF' Documentos editados por la Dirección General De Presupuestos, Ministerio de Economía y Hacienda, Madrid.

[xxiii] Murillo, E. (2005): La política regional europea: un análisis de sus efectos sobre la economía andaluza. Período 1994-2001, Investigaciones N2/05, Instituto de Estudios Fiscales, Madrid.

[xxiv] For cross-national harmonised evaluations over the last three periods at the European level see: Beutel J (1993) The Economic Impacts of the Community Support Frameworks for Objective 1 Regions 1989-93, Report for the European Commission, Brussels; Beutel J (1995) The Economic Impacts of the Community Support Frameworks for Objective 1 Regions 1994-99, Report for the European Commission, Brussels; Beutel J. (2002) 'The Economic Impact of Objective 1 Interventions for the Period 2000-2006' Final Report to DG REGIO, European Commission, Brussels.

[xxv] For other regional impact evaluations in Spain using input-output techniques see the Objective 1 Mid-Term Evaluation Update for Castilla-Leon: Quasar (2005) 'Actualización de la Evaluación Intermedia del Programa Operativo Integrado de Castilla y León 2000-2006' Informe Final, Consejería de Hacienda, Junta de Castilla y León. A more extensive and long-term evaluation of impacts using input-output techniques on the Aragón Objective 2 region is provided in: Sosvilla S, Dolores M, Herce J and Montañés J (2002) Los Efectos de las Ayudas Comunitarias en Aragón, Monografías del Consejo Económico y Social de Aragón, Zaragoza.

[xxvi] Cardenete A.M. and Lima M.C. (2005) 'Impact Assessment of European Structural Funds in a Regional Economy: a CGE approach', VIII Encuentro de Economía Aplicada, Murcia.

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[xxxii] Bradley et al (2004) *op.cit*.

[xxxiii] Martín C, Herce J.A., Sosvilla-Rivera S and Velásquez F.J. (2002) 'La ampliación de la Unión Europea: Efectos sobre la economía española', Colección Estudios Económicos, Nº 27, La Caixa, Barcelona.

[xxxiv] Although the authors assume that Spain would receive 40 percent less funding than under the current period (compared to the 50 percent decline in practice) and Castilla-La Mancha is grouped within the Phase-out category (instead of the Convergence Objective).

[xxxv] Sosvilla-Rivero S and Herce J.A. (2004a) 'La Política de Cohesión europea y la economía española: evaluación y prospectiva', Documento de Trabajo 2004-20R, FEDEA, Madrid.

[xxxvi] This result is similar to the second (more generous) future funding scenario estimates in Martin *et al*. (2002) reviewed above.

[xxxvii] For a regional application of the HERMIN model to Madrid in the 2007-13 period see: Sosvilla-Rivero S and García E (2006) 'Efectos de las ayudas europeas sobre la Economía Madrileña 2007-2013' Un análisis basado en el Modelo Hermín, Documento de Trabajo 2006-07, FEDEA.

[xxxviii] De la Fuente, A. (2005) "El impacto de la reducción de las ayudas estructurales europeas: una primera aproximación", *Instituto de Análisis Económico*, mayo 2005.

[xxxix] Flores de Frutos *et al.*(2005) "Análisis de los efectos económicos de las nuevas perspectivas financieras de la Unión Europea para las Comunidades Autónomas Españolas", *Documentos faes.*

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[xlii] For contributions to the discussion, see http://ec.europa.eu/dgs/policy_advisers/discussions_papers_en.htm