ANALYTICAL ARTICLES
Economic Bulletin

3/2021

BANCO DE ESPAÑA
Eurosistema

HISTORICAL DEVELOPMENT OF THE EUROPEAN STRUCTURAL AND INVESTMENT FUNDS

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ABSTRACT

In December 2020 the European Council approved the regulation establishing the European Union (EU) Multiannual Financial Framework for 2021-2027 and the Next Generation EU recovery facility. Both mechanisms will help provide in the coming years for financing worth €1.8 trillion to sustain the EU's post-pandemic recovery and its long-term priorities. To set the scale of these funds and the challenge of managing them in context, this article firstly describes the European Structural and Investment Funds. It then offers a detailed analysis of the amount and composition of the resources received to date under these funds, along with their distribution by type of expenditure in the biggest EU countries, with particular emphasis on Spain. Lastly, given the regional focus of the allocation criteria, the final section of the article dissects the course, composition and distribution by type of expenditure of these funds among Spain's different regions.

Keywords: structural funds, European investment funds, Next Generation EU, regional governments.

JEL classification: E60, H30, H50.

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Introduction

The COVID-19 health crisis has posed a challenge of historic proportions globally. The scale of the challenge has prompted an exceptional reaction by the authorities at both the national and supranational levels. An important element of the response to the pandemic at European level is the recovery instrument known as Next Generation EU (NGEU), with a very large envelope (€750 billion). This is a temporary mechanism designed to mitigate the fallout of the pandemic.[1] Simultaneously, the European Council approved on 17 December 2020 the Regulation laying down the EU Multiannual Financial Framework (MFF) for 2021-2027. The MFF is a mechanism that has been in place for several decades, which defines the roadmap for the EU budget. The MFF includes the budgetary allocations of the European Structural and Investment Funds (ESIF). The NGEU and the MFF have joint funds amounting to €1.8 trillion. They are designed, in the short-term, to mitigate the socioeconomic effects of the crisis and support the recovery and, over a longer time horizon, to contribute to fund projects fostering the economy's potential growth and structural transformation.

To put the new NGEU instrument into context, this article presents a description of the ESIF. A substantial part of the EU budget funds is channelled through these instruments (five in total), with the aim of promoting economic, social and territorial cohesion in the European Union. The interest in analysing the use of these funds lies in the fact that the priority investment areas in the context of NGEU are in line with the objectives of some existing ESIF, such as the European Regional Development Fund (ERDF) and the European Social Fund (ESF). However, the NGEU envelope (€750 billion) is much bigger, nearly twice that for the ESIF in the 2021-2027 MFF for the EU as a whole (€414 billion). In the case of Spain, that difference is even starker, since the amount of the funds allocated under the NGEU is three times the total volume under the ESIF in any of the previous completed seven-year MFFs (for 2000-2006 and 2007-2013). Consequently, particularly as regards Spain, given their large scale, the efficient absorption of these funds for carrying out projects capable of truly transforming the economy and achieving potential long-term growth poses a major challenge.

1 Council Regulation (EU) 2020/2094 of 14 December 2020 established a recovery instrument. Subsequently, on 11 February 2021 the Council approved the Regulation establishing a Recovery and Resilience Facility (RRF), a key instrument at the heart of the NGEU.

According to this article's analysis, under the MFFs for 2000-2006 and 2007-2013, the total ESIF fund absorption rate was high – around 90% – with no substantial differences across countries. A characteristic of the time pattern of fund absorption is that part of it takes place once the seven-year reference period of the related MFF concludes. Also, although there are no major differences between countries in historical absorption capacity, greater heterogeneity is observed in the composition by type of expenditure in the MFF for 2014-2020. Specifically, as regards the average for the three largest euro area economies, Spain allocated a greater proportion of funds to investments relating to I&D and information and communication technologies (ICT) and a smaller proportion to investments relating to the green transition and to promoting SME competitiveness. A final conclusion of the article is that the distribution of funds by region in Spain is characterised by a high degree of heterogeneity both in terms of the composition across ESIF and of the types of expenditure financed by each of the ESIF.

European Structural and Investment Funds

MFFs are spending plans which set the EU's priorities for a seven-year period. MFFs include the ESIF, which are funds jointly managed by the European commission (EC) and the EU countries. The five ESIF have experienced substantial transformations since the creation of the first one, the European Social Fund, for various reasons. These include changes in political and economic priorities at European level, changes in funding sources and the successive EU enlargements.

The main features of each of the five funds are as follows:

— The European Social Fund (ESF) was created in 1957 under the Treaty of Rome establishing the European Economic Community (EEC), and is the main EU instrument for supporting job creation and investing in human capital. All European regions are eligible for ESF funding, albeit in different degrees, depending on their relative GDP per capita. The 2021-2027 MFF establishes a budget for this fund of €88 billion, which accounts for 21.3% of the ESIF total.

— The European Regional Development Fund (ERDF) was created in 1975 with the aim of correcting the main regional imbalances within the EEC, whether caused by a lower level of development than that of other areas or because the decline in an activity makes the economy's sectoral reconversion necessary. This has been the most important fund for Spain, in quantitative terms, until the 2014-2020 MFF. As in the case of the ESF, all European regions may benefit from the available funds, although in varying degrees depending on the regional GDP per capita. The 2021-2027 MFF allocates €200 billion to this fund, i.e. 48.3% of the ESIF total.

— The Cohesion Fund was set up following the signing of the Maastricht Treaty in 1992 to provide the basis for a regional policy of solidarity at EU level. Its goal is to carry out public investments in environmental and communication infrastructures in regions lagging behind in these areas and with a gross national income (GNI) of less than 90% of the average income of the EU. Spain ceased to be eligible in 2014. Under the new 2021-2027 MFF, the envelope of this fund is €43 billion (10.4% of the overall ESIF amount).

— The objective of the European Maritime and Fisheries Fund (EMFF) is to ensure environmental, economic and social sustainability in the fisheries and aquaculture sectors. It was created in the early 1990s to mitigate the imbalance between fishing fleet capacity and fishing opportunities, under the Financial Instrument for Fisheries Guidance. Allocations are decided based on criteria such as size and socioeconomic importance of aquaculture and fishery in each region. It's budget for 2021-2027 was set at €5 billion (1.2% of the overall ESIF amount).

— The European Agricultural Fund for Rural Development (EAFRD), which was created in the setting of the reform of the common agricultural policy (CAP) in the early 2000s, promotes rural development and uses the low environmental impact of the projects presented as a criterion for granting financial assistance. The distribution of this fund depends on the regional level of development measured by per capita GDP and the proportion of agricultural and forest areas in the total. An allocation of €78 billion was established for the 2021-2027 period (18.8% of the total ESIF volume).

Two new financial instruments were created under the NGEU programme which was approved by the European Council in June 2020 and formally established by a Regulation in December 2020. The first one, with an envelope of €672.5 billion, is the Recovery and Resilience Facility (RRF). It aims to provide grants and loans to Member States to finance a coherent set of investment and reform projects in six areas: green transition; digital transformation; employment and smart, sustainable and inclusive growth; social and territorial cohesion; health and resilience; and the so-called policies for the next generation, including, in particular, education. The second one, with an envelope of €47.5 billion, is the Recovery Assistance for Cohesion and the Territories of Europe (REACT-EU). This initiative will be implemented in part through the ERDF and the ESF, underlining how NGEU's and the ESIF's objectives do not differ much.[2]

One of the challenges historically faced by the ESIF has been the agile channelling of available funds to the different investment projects. In particular, funds are

2 NGEU will also reinforce the EAFRD budget.

allocated through national and regional "operational programmes" (OPs), which are approved by the EC and establish both specific investment priorities and targets, and their multiannual funding plan. The OPs are part of the MFFs, which, as mentioned above, cover a seven-year period and may be co-financed with national and regional funds. However, it is possible for projects to be implemented up to three years after the end of the programmed period.[3] In practice, this has led to significant overlaps between the MFFs and to delays in the approval of OPs, which have slowed fund absorption, as analysed in the following section.

Absorption of structural funds in Spain in the European setting

This section draws on a database with detailed information on the five structural funds for the 28 EU countries' 271 regions over the period 2000-2020.[4] Specifically, this database was constructed by aggregating all the individual operational programmes included in the three successive MFFs that have been in place since 2000. Relevant variables included in the database are the annual volume of EU payments that a region has received and the expenditure under each ESIF in that region for each year of each MFF, along with the total commitments made under each programme as a whole (i.e. the volume of resources committed but not necessarily disbursed).

According to this information, Spain received ESIF financing in the 2000-2006 and 2007-2013 MFFs which far exceeded, as a percentage of GDP, that of the other large economies of the current EU. However, on the information available, this gap appears to have narrowed significantly in the 2014-2020 MFF (see Chart 1.1). In nominal terms, Spain received funding of around €40 billion in each of the two programmes (2000-2006 and 2007-2013). This volume was significantly reduced in the 2014-2020 MFF to €17.5 billion. There are two reasons for this. First, Spanish regions are no longer eligible for the Cohesion Fund, as their per capita income exceeds the EU average. Second, additional funds can still be received until 2023 under this third programme.

Comparison of these figures with the volume of funds allocated to Spain under the NGEU (€140 billion) reveals the considerable challenge that management of these funds entails for the different tiers of government in Spain, as they amount to more than three times the ESIF volume managed, for example, under either of the two programmes for the 2000-2006 and 2007-2013 periods.

As it is no longer possible for Spain to apply for the Cohesion Fund in the last programming period, it may be interesting to see how the resources received were distributed, both among the three remaining larger ESIF (the ESF, the ERDF and the

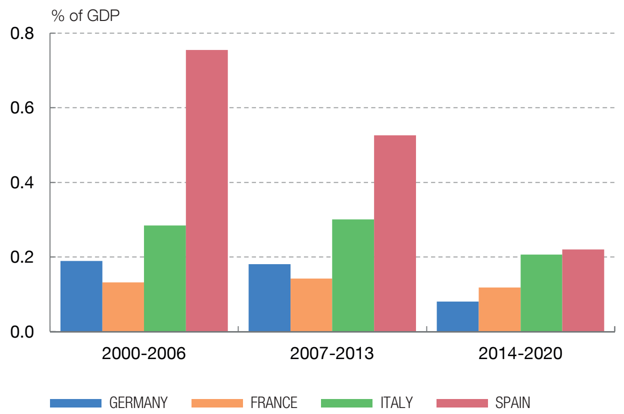
3 Since the 2000-2006 MFF it has been possible to carry out projects up to two years after the end of the programme. This rule was extended for an additional year (up to the current three) in the MFF for 2014-2000.

4 The 271 regions of the current 27 EU Member States plus the United Kingdom, according to the NUTS-2 classification (equivalent to Spain's autonomous regions).

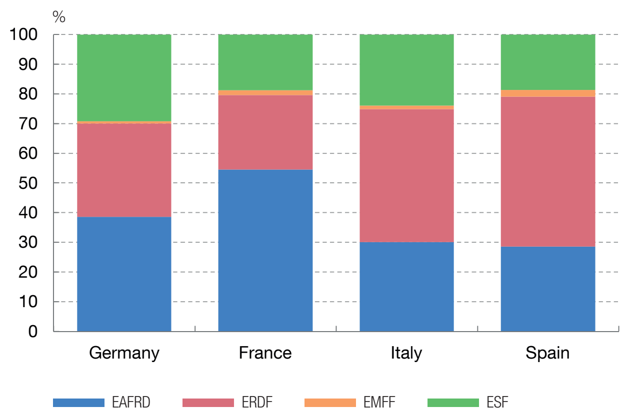
Chart 1
DISTRIBUTION OF STRUCTURAL FUNDS, BY COUNTRY, PROGRAMME AND TYPE OF FUND

The volume of funds received by Spain as a percentage of GDP has steadily decreased over the course of the three successive multiannual programmes since 2000. 50% of the structural funds received by Spain under the 2014-2020 programme came from the ERDF.

1 VOLUME OF FUNDS, BY COUNTRY (a)



2 DISTRIBUTION OF THE FINANCING RECEIVED, BY TYPE OF FUND (2014-2020 PROGRAMME) (b)



SOURCE: European Commission.

a Cumulative percentage of GDP over the course of each programme (seven years).
b Refers to the seventh year of the programme.

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EAFRD) and by specific programme. This analysis could help discern to what extent expenditure in the MFFs would be similar to the foreseeable expenditure under the NGEU. To date, in the 2014-2020 MFF, approximately half of the resources received by Spain come from the ERDF (see Chart 1.2). Two-thirds of the remaining 50% come from the EAFRD and one-third from the ESF. This pattern is similar to that observed in Italy where, as in Spain, there are also important regional divergences in GDP per capita, which is the main criterion for ESF distribution. By contrast, in France the focus is more on projects aimed at rural development. The predominant programme is therefore the EAFRD. Lastly, in Germany, so far the resources are distributed fairly evenly among the three ESIF.

In addition, information is also available on the distribution by category of the expenditure implemented with ERDF and ESF financing in the 2014-2020 MFF.[5] In the case of the ERDF, the information available classifies expenditure into 13 main areas. Chart 2.1 looks at the five main areas in terms of their volume (R&D&I, ICTs, infrastructure, supporting SME competitiveness and a green economy). These categories are considered to be investment expenditure.[6] The remaining headings

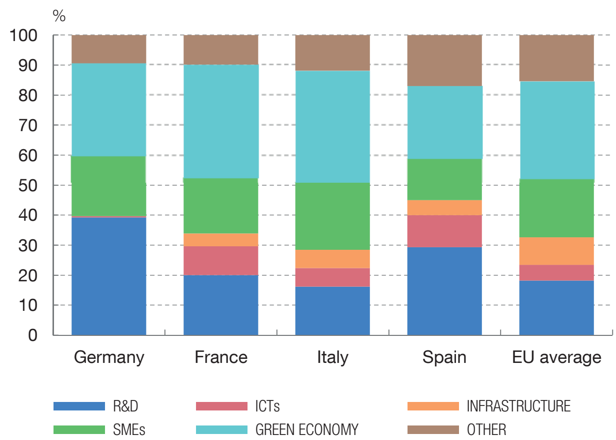
5 Specifically, national authorities propose a distribution by category of expenditure that must subsequently be approved by the EC.

6 The available statistical information for the four large countries only classes expenditure into current and investment in the case of Italy. The classification made by the Italian authorities confirms that the ERDF is almost entirely used for investment expenditure and the ESF for current expenditure.

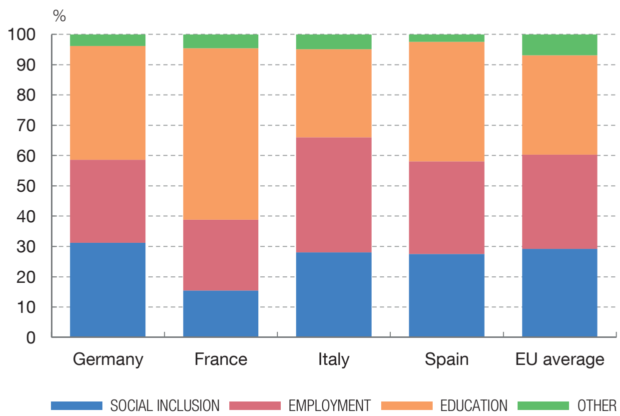
Chart 2
COMPOSITION OF SPENDING FINANCED WITH FUNDS FROM THE 2014-2020 PROGRAMME

Spain has spent 29% of ERDF financing on R&D, more than the EU average (18%). Under the ESF, Spain has spent 39% in education, roughly the same percentage as Germany (38%) but less than France (57%).

1 COMPOSITION OF FINANCED SPENDING - ERDF



2 COMPOSITION OF FINANCED SPENDING - ESF



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SOURCE: European Commission.

are for current expenditure and are grouped under "other", which includes categories such as education, employment and transfers to households. In the EU as a whole, around 85% of ERDF funds were allocated to investment projects and only 15% to current expenditure (see Chart 2.1). Within investment, the most relevant items were those related to the green economy, supporting SME competitiveness and R&D, which accounted for around 70% of expenditure on average in the EU. By country, in Germany, France and Italy committed expenditure in investment projects accounted for around 90%, while in Spain it was slightly below 85%. In terms of the composition within investment, there are divergences between the large countries. Germany and Spain are the countries that allocate the largest share to R&D, whereas France and Italy focus their efforts on the green economy. Specifically, in Spain R&D financing represents almost 30% of the total, around 10 pp more than in the EU as a whole. Lastly, Spain is below the EU average in the share of ERDF funds allocated to supporting SME competitiveness and infrastructure, and above in ICT investment.

Regarding the ESF, the resources obtained by Spain in the 2014-2020 MFF have been allocated in similar proportions to finance education, employment and social inclusion expenditure (see Chart 2.2). The distribution is very similar for the EU average. Among the large economies, projects relating to education are more prominent in France.

In addition to the total volume and use of the funding received, it is interesting to analyse the percentage of initial spending commitments that actually materialise in projects implemented during the programme period, i.e. the rate of absorption.[7] In the two programmes completed since the turn of the century, the rate of absorption of the large countries stood at over 90%, with minimal differences across programmes, funds and countries (see Charts 3.1 and 3.2). Thus, Spain, which has implemented around 92% of its spending commitments, appears to have absorbed slightly less than France and Germany (95%) but more than Italy (90%).

These cross-country similarities are also apparent when analysing the time pattern of absorption, which accelerates as the MFF progresses. Specifically, between 9% and 11% of the total spending committed under the programme as a whole had been implemented by the four large euro area countries during the first two years of the 2000-2006 and 2007-2013 MFFs. Over the following two years, the pace at which spending was implemented increased, with rates of absorption of between 20% and 33%. Finally, in the seventh year of the MFF (the last year in which it is possible to commit expenditure), implementation of funds under the 2000-2006 and 2007-2013 programmes accelerated to 58% and 74% of the total spent over the entire MFF. In the case of Spain, this figure reached 69% for the ESIF total. When broken down by type of fund, in the case of the ERDF, the average absorption for these two MFFs ranged from 70% in Germany to 54% in Italy (68% in Spain) (see Chart 3.3). As regards the ESF, the rate of absorption for the first two MFFs of this century ranged from 75% in Germany to 61% in France (see Chart 3.4). In Spain it was 68%.

It is not yet possible to determine the total absorption rate for the 2014-2020 programme, as it will not fully conclude until 2023. For this reason, it is also interesting to analyse the rate of absorption in the seventh year of each of the MFFs, in order to have a metric of the rate of absorption which can be compared with past programmes. In this regard, by the seventh year of the 2014-2020 MFF, Spain had implemented a percentage of available funds similar to Italy and somewhat lower than Germany and France. Specifically, in 2020 Spain had implemented 40.1% of the available ERDF funds compared with 38.5% in Italy, 44.6% in Germany and 47.4% in France. Moreover, the implementation figures for the seventh year of the programme are below the equivalent figures for the 2000-2006 and 2007-2013 programmes. This is due to two reasons: the extension by one year of the implementation period of the programmes, to a total of ten years, in the last MFF, and the delay in the approval of the 2007-2013 MFF, which also delayed the implementation of the 2014-2020 MFF.

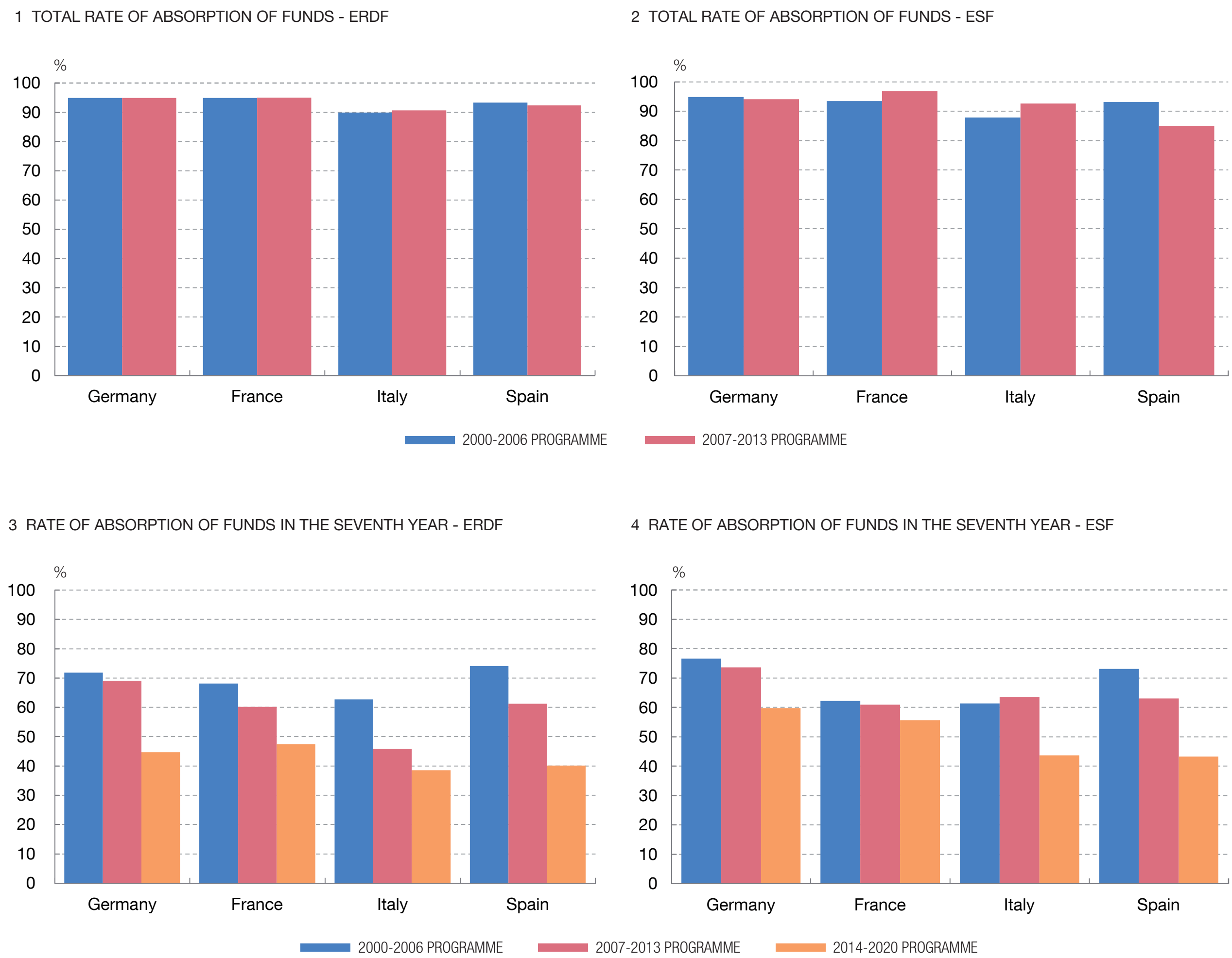
Regional heterogeneity in Spain

Since their inception, the ESIF have focused on actions with regional objectives. Recently, moreover, most of the OPs which are the basis for channelling the ESIF are

7 In this article, the ESIF rate of absorption is approximated for each year as the ratio of the cumulative sum of the payments made to each country by the EU to total spending commitments.

Chart 3
ABSORPTION OF FUNDS, BY COUNTRY, PROGRAMME AND TYPE OF FUND (a)

The rate of absorption of ERDF funds in the 2000-2006 and 2007-2013 programmes was similar across countries; in the case of the ESF, heterogeneity is somewhat higher. The rate of absorption in the seventh year of the 2014-2020 programme was lower compared with earlier programmes, for both the ERDF and the ESF.



SOURCE: European Commission.

a The rate of absorption is defined as the ratio of cumulative total payments to cumulative total commitments up to the end of the corresponding programme or seven-year period.

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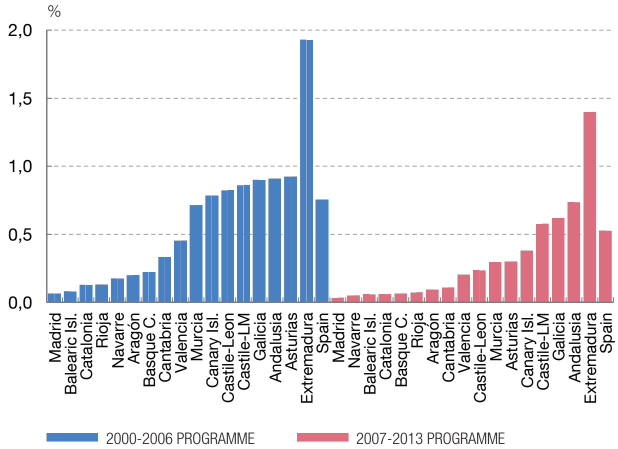
being drawn up directly by regional and even local governments. As a consequence of this focus on the regional level, heterogeneity across regions is very high in a number of aspects, including the volume of resources that each region receives as a share of its GDP, the distribution of these revenues among the different ESIF and the nature of the expenditure funded. This is also the case in Spain. Chart 4.1 illustrates the first of these three aspects. As can be seen, the disparity in the cumulative volume of funds received by Spanish regions in the two MFFs that have already concluded (2000-2006 and 2007-2013) as a percentage of GDP over their seven years is very high. The main reason for these differences is the heterogeneity

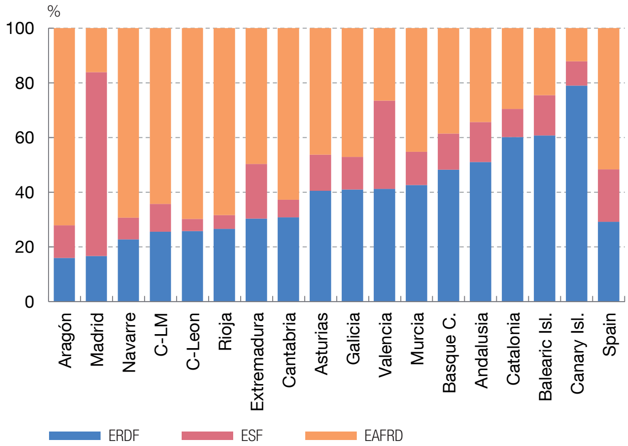
Chart 4
DISTRIBUTION AND COMPOSITION OF STRUCTURAL FUND SPENDING, BY REGION, PROGRAMME AND TYPE OF FUND

There are major differences in the type of spending financed with European funds by regions. In the case of the ERDF, half of the regions spend more than 50% of their funds on R&D projects. In the case of the ESF, the type of spending differs across regions.

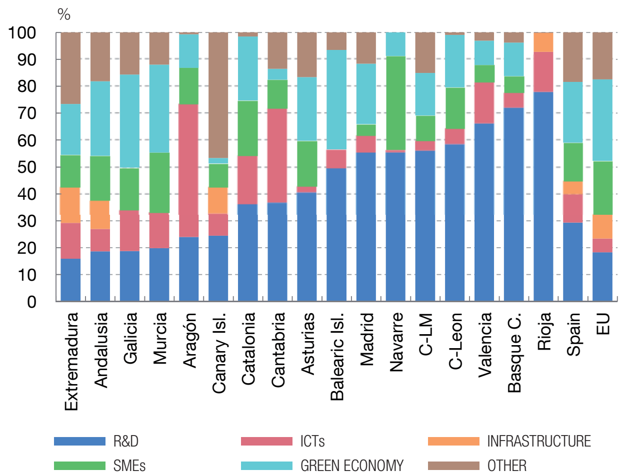
1 VOLUME OF FUNDS, BY REGION (% OF GDP) (a)



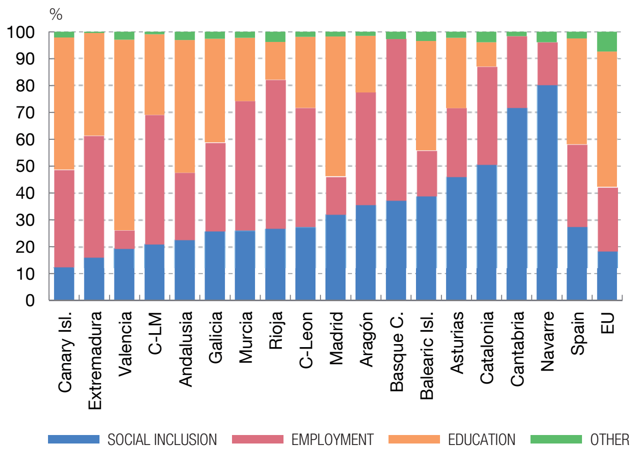
2 2014-2020 PROGRAMME (b)



3 COMPOSITION OF FINANCED SPENDING - ERDF



4 COMPOSITION OF FINANCED SPENDING - ESF



SOURCE: European Commission.

a Cumulative percentage of GDP over the course of each programme (seven years). Only ERDF and ESF financing is considered in the chart.
b Refers to the seventh year of the programme.

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in terms of GDP per capita. In particular, regions with lower incomes (such as Extremadura, Andalusia and Galicia) have received amounts well above the national total in terms of GDP, whereas the opposite is true of those with higher income (such as Madrid, Catalonia and the Balearic Islands).

Regional heterogeneity is also high in terms of the distribution among the different ESIF, as illustrated by Chart 4.2 for the 2014-2020 programme. Specifically, the share of EAFRD resources in the total is greater in regions in which the value added of the primary sector accounts for a higher proportion of their overall economic activity. The composition of the funds received by the regions with a lower per capita income is more evenly balanced between the EAFRD and the ERDF. Lastly, the weight of the ESF in the total is more similar across the different regions.

There are also significant differences in the type of expenditure financed with European resources by the Spanish regions, as shown in Charts 4.3 and 4.4 for ERDF and ESF allocations in the period 2014-2020. In the case of the ERDF (Chart 4.3), half of the regions allocate more than 50% of its funds to R&D. This percentage approaches 70% in the Basque Country, Valencia and Rioja, in contrast to percentages below 20% in Andalusia, Galicia, Murcia and Extremadura. Instead, these regions allocated a greater proportion of their ERDF financing to projects related to the green economy and support for SMEs. Aragon and Cantabria allocated a higher share than the rest to investments linked to ICTs.

As for the differences in the ESF, there is a certain disparity by region in the allocation of resources among the three main headings: social inclusion, employment and education. In some regions, spending is more concentrated in one of these three categories, notably Cantabria and Valencia, where spending on social inclusion and education, respectively, accounts for almost 70% of total ESF funds received, and the Basque Country, where 60% of spending is on employment (see Chart 4.4).

23.6.2021.