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THE SINGLE MARKET AND COHESION POLICY DYAD: BATTERED BY THE CRISIS AND GLOBALISATION

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SUMMARY

The alliance between the "four freedoms" of movement and cohesion policy has always been a major selling point for candidate countries, given that the benefits of the single market amplify the benefits of investments made possible by EU structural interventions, and vice versa. The 2014-2020 programme, however, has begun amid doubts stirred by six years of the crisis's disturbing effects. National growth curves have brutally halted or been significantly hampered. Regional convergence has slowed; and social inequalities between people have increased. As for the single market, which European citizens accuse of speeding up globalisation, it appears less attractive to major, multinational economic partners. Its weight has been relatively weakened by trends in global trade. Since the enlargement in 2004, the share of intra-EU trade in EU27 exports has steadily declined.

Are the limitations of the single market/cohesion policy dyad in a slowdown temporary or may they last? In other words, if there were a recovery, would it result in convergence? Many signals force us to doubt.

"WHAT RELATIONSHIP BETWEEN THE POLICIES TO REDUCE REGIONAL AND SOCIAL DISPARITIES AND THOSE TO OPEN THE EUROPEAN MARKETS?"

This Policy Paper aims at understanding the current relationship between, one the one hand, the policy to reduce regional and social disparities, and on the other hand, the policy aimed at ensuring the opening of European markets.

To do so, Part 1 recalls the nature of the strong bond between these policies for over twenty years, as they were launched almost simultaneously. Section 1.1. reviews the first few years: not only did the single market yield good results in terms of growth and employment for EU12 countries; results were also significant for major recipients of structural funds, namely Ireland, Spain, Portugal and Greece. Section 1.2. studies the virtuous mechanism which accompanied each enlargement in the 1990s and 2000s. In Central and Eastern European countries, the most optimistic estimates were largely confirmed throughout the period preceding the 2008 crisis, as regards growth, employment and foreign direct investments. Moreover, the catching-up mechanism provided by European structural interventions is an ongoing source of the secondary movement of capital, whereby 30-40% of EU funds are transferred to the more developed contributing countries.

Part 2 analyses the recent shifts in this relationship and the structural reasons behind the current impasse. Beyond the crisis which created numerous economic disruptions, section 2.1. shows that several underlying factors have halted the usual momentum of the single market/cohesion policy dyad. For the last decade and since the institution of the single currency, border effects, agglomeration effects, and specialisation effects have combined impacts on national and regional economies of which are sometimes doubled; at others, cancelled out. Section 2.2. concentrates on the link between globalisation and the development of poverty in the EU. As the way to stop rising social inequalities primarily involves fiscal reform and the regulation of major network and banking sectors, and marginally the areas covered by cohesion policy, the dyad appears particularly depleted.

Finally, in order to restore cohesion which remains a major challenge for the EU, exploring other non-strictly economic ways is required. This would confirm the divorce between the single market and cohesion policy.

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INTRODUCTION

Twenty years after the scheduled completion of the single market, an assessment of the rapport between the "four freedoms" of movement and cohesion policy may come as a surprise. After all, this alliance has always been a major selling point for candidate countries, given that the benefits of the single market amplify the benefits of investments made possible by EU structural interventions, and vice versa. The positive knock-on effects of this dyad for both new and old members, confirmed repeatedly with each enlargement, have also been used as a tool of persuasion to conclude the final negotiations for each new multi-annual financial framework since 1989.

The 2014-2020 programme, however, has begun amid doubts stirred by six years of the crisis's disturbing effects. National growth curves have brutally halted or been significantly hampered. Regional convergence has slowed; and social inequalities between people have increased. Has the well-oiled machine jammed? Is one of the two policies to blame, or have both shown simultaneous weaknesses? Is this deadlock a temporary side effect of the crisis, or is it a structural problem caused by globalisation?

In this paper, we will try to understand the current relationship between, one the one hand, the policy to reduce regional and social disparities, and on the other hand, the policy aimed at ensuring the opening of European markets. To do so, part one reviews the nature of the strong bond between these policies for over twenty years. Part two studies the recent shifts in this relationship and the structural reasons behind the current impasse. We will conclude by assessing the future potential of the single market/cohesion policy dyad.

1. A solid couple for over twenty years

1.1. A twin birth

The cohesion policy was launched in 1988 as a direct continuation of 'Objective 92', the project to complete the single market, and of institutional reform with the Single European Act. The proposal to integrate all existing European funds (EAGGF, EDRF and ESF[1]) for regional development strategies aimed at further reducing regional inequalities was based on the arguments of Tommaso Padoa Schioppa[2], commissioned to complement the now famous report on the costs of "non-Europe" and the benefits of the single market, written by the team of Paolo Cecchini[3].

In his report, Tommaso Padoa-Schioppa presented the risks of pursuing market integration without parallel progress on macro-economic stability and income redistribution. He called for a specific form of redistribution via budgetary solidarity given the limited geographic mobility of Europeans: at other times in history, mobility quickly absorbed socio-economic disparities between regions in a given free-trade area (in the 19th century in Germany or still today in North America, for example). In this case, however, persistent or even greater gaps at the national or regional level – despite the opening of national borders – appeared more likely[4]. To ensure that

1. European Agricultural Guidance and Guarantee Fund (EAGGF), European Regional Development Fund (EDRF), European Social Fund (ESF).
2. Tommaso Padoa-Schioppa, *Efficacité, stabilité, équité*, Paris, Economica, 1987 (in French).
3. Paolo Cecchini (coord.), *Research on the Cost of non-Europe – Basic Findings*, Brussels, Commission of the European Communities, Documents, volumes 1 to 16, 1988.
4. Paul Krugman,"European Economic Integration: Some Conceptual Issues", in T. Padoa-Schioppa, *ibid*.

everyone – regions and social segments alike – accepted the disruptions that the single market programme would surely prompt, Tommaso Padoa-Schioppa concluded that efficiency gains must be shared evenly via specific mechanisms and that policies were needed to promote growth in the regions and for the populations which were less favoured.

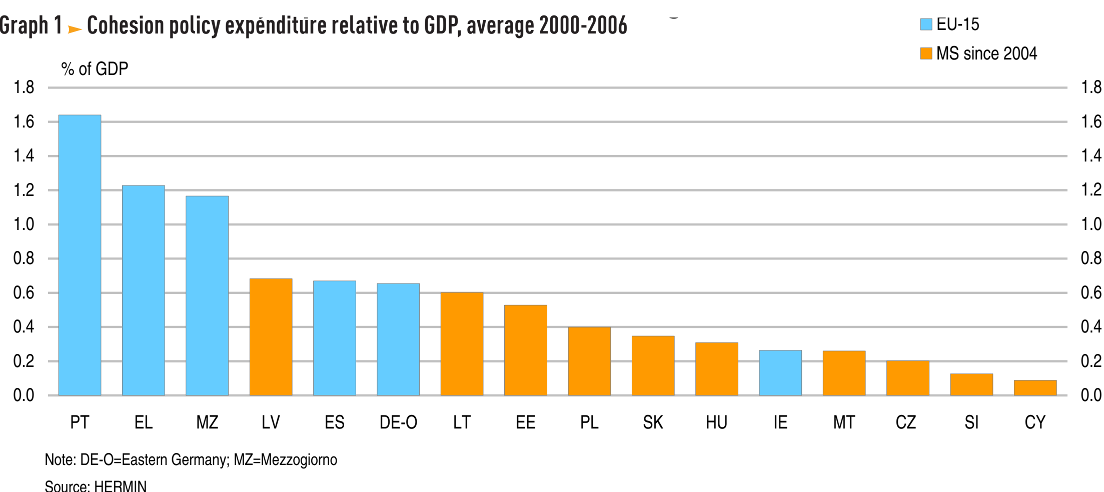
The creation of cohesion policy was presented by Jacques Delors as a "flanking policy" designed to enhance solidarity between member states by focusing on solidarity between regions and : or other areas seized in their social and economic characteristics. EU regional policy aimed at creating a dynamic convergence mechanism by expanding the scope of intra-European solidarity beyond its traditional forms[5], and at "*stopping to consider community instruments as components of a financial compensation system*"[6].

Financial transfers to recipients were substantial over the first two programming periods *(see Table 1)*. Thereafter, following the accession of Central and Eastern European countries, these transfers were modified to meet a) the needs of countries and regions with vastly different levels of existing infrastructure, b) the varying abilities of countries and regions to absorb these financial flows based on their economic profile, and, particularly, c) the limits set for the European budget *(see Graphs 1 and 2)*. In fact, the budget earmarked for cohesion policy, which represented approximately 0.4% of annual gross national income (GNI) in the 1990s, was not revised upwards as substantially as it should have been in 2004 when less-developed countries joined and mechanically lowered average per-capita GDP to 12.5%. Instead, from 2007 onwards, cohesion policy funding was capped and represented only 0.37% of European GNI in 2013.

Table 1 ► Cohesion policy spending as a percentage of GDP in the four main recipient countries (1989-1993 and 1994-1999)

GDP (%)	GREECE	IRELAND	SPAIN	PORTUGAL
1989-93	2,6	2,5	0,7	3,0
1994-99	3,0	1,9	1,5	3,3

Source: European Commission, *Second report on economic and social cohesion*, 31.01.2001.

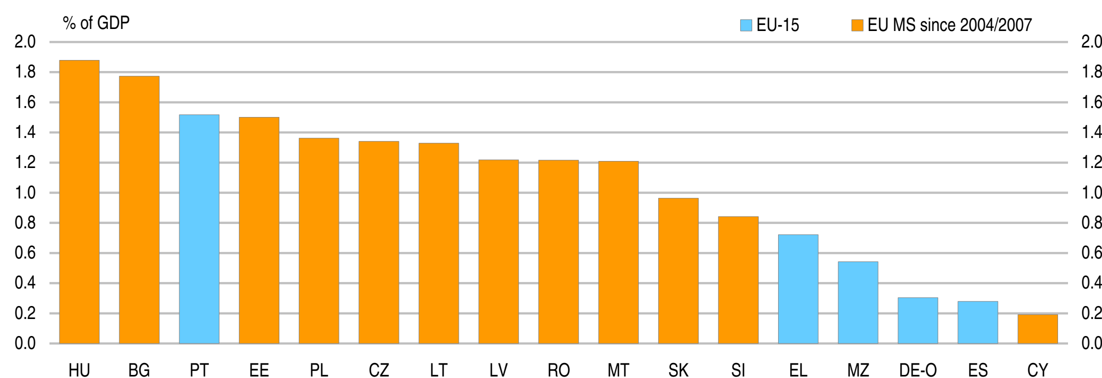


Graph 1 ► Cohesion policy expenditure relative to GDP, average 2000-2006

Source: European Commission, *Fifth report on economic, social and territorial cohesion: Investing in Europe's future*, November 2010.

5. This refers to solidarity between social categories, usually the remit of member states, seen following the depression in the U.S. (Roosevelt's New Deal) and in post-war Europe (creation of social welfare systems).
6. Jacques Delors, "Discours Réussir l'Acte unique de 1987", *Le nouveau concert européen*, Odile Jacob, 1992 (in French).

Graph 2 ► Cohesion policy expenditure relative to GDP, average 2007-2013



Source: European Commission, *Fifth report on economic, social and territorial cohesion: Investing in Europe's future*, November 2010.

To maximise the effects of EU funds to less-developed regions, cohesion policy was subject to relatively strict rules which were upheld and even enhanced with each new programming period[7].

Hence, over the first few years, not only did the single market yield good results in terms of growth (a 0.5% annual increase between 1985 and 1992) and employment (11 million new jobs) for EU12 countries; results were also significant for recipients of structural funds. During the first programming period (1988-1993), as much as 600,000 jobs were created in Ireland, Greece, Spain and Portugal. In areas undergoing industrial and rural conversion (in other member states), small and medium enterprises were able to generate 470,000 jobs.

Over the course of the following period, from 1994 to 1999, the trend grew: in the four poorest countries and the new German Lander, an additional 1.7 million jobs were created. The pace at which countries caught up was such that per capita GDP in Ireland went from 64% of the EU average in 1988 to 118% in 2000 thanks to annual growth of 6.5% for over ten years[8]. Over the same period, Spain, Portugal and Greece together performed somewhat less – but still noticeably – well: per capita GDP increased from 68% of the EU average in 1988 to 79% in 1999[9].

Various explanations for this success have been offered. Certain experts[10] have questioned the role of structural funds, pointing out the small amount they represent in comparison to other national funds, and the extensive impact of other sectoral or national policies on different regions. Conversely, other researchers have emphasized the qualitative and quantitative leverage these European funding instruments have provided[11]. Joining the single market is generally viewed by anyone evaluating regional development programs as having been a determining factor in the creation of new export opportunities for less developed countries and regions. Eliminating borders in these areas also increased imports, due in part to flows generated by major development projects co-funded by structural funds, but in particular thanks to an increase in household purchasing power and domestic consumption[12].

7. Marjorie Jouen, *La politique européenne de cohésion*, DILA, Paris, 2011 (in French).
8. For the case of Ireland, see Marjorie Jouen, *ibid*, p. 40-41
9. European Commission, *Second report on economic and social cohesion*, 31.01.2001.
10. Xavier Sala-i-Martin, "Regional cohesion: Evidence and theories of regional growth and convergence", *European Economic Review*, vol. 40 (6), pp. 1325-1352, June 1996; Angel de la Fuente, "Convergence Across Countries And Regions: Theory And Empirics", *CEPR Discussion Papers* 2465, November 2002.
11. Herta Tödtling-Schönhofer and OÏR (Ed.), *The leverage effects of European cohesion policy under the structural funds*, Report for the Committee of the Regions of the European Union, Luxembourg, Publications Office of the European Union, 2007.
12. Sophie Baudet-Michel and Jean Peyrony, "Développement territorial et politique régionale : quelques pistes pour l'Union européenne après 2006", *Territoires 2020*, n° 7/1, 2003 pp. 61-74 (in French) A. Aadne Cappelen *et al*., "The impact of EU regional support on growth and convergence in the European Union", *ECIS Working Paper*, 2002.

Table 2 ► GDP per head (in PPP) in cohesion countries (1988-2003)

PERIOD	GREECE	SPAIN	IRELAND	PORTUGAL	EU15*
1988	58.3	72.5	63.8	59.2	100.0
1989	59.1	73.1	66.3	59.4	100.0
1990	57.4	74.1	71.1	58.5	100.0
1991	60.1	78.7	74.7	63.8	100.0
1992	61.9	77.0	78.4	64.8	100.0
1993	64.2	78.1	82.5	67.7	100.0
1994	65.2	78.1	90.7	69.5	100.0
1995	65.9	78.2	93.3	69.7	100.0
1996	66.6	79.3	93.5	70.0	100.0
1997	65.9	79.9	103.7	73.3	100.0
1998	66.9	79.2	106.1	72.2	100.0
1999	68.2	82.1	112.2	71.9	100.0
2000	67.7	82.2	115.2	68.0	100.0
2001	64.7	84.1	117.9	69.0	100.0
2002	69.0	83.4	119.1	72.5	100.0
2003	70.4	83.8	119.9	72.1	100.0

*: Growth rates 88-98 and 88-93: excluding new German Länder

Source: Eurostat / European Commission, *Second progress report on economic and social cohesion*, COM (2003) 034, 30.01.2003

1.2. A repeatedly proven alliance

Each enlargement in the 1990s and 2000s has shown that this virtuous mechanism, which combines the promise of structural funds and access to the single market, was, undoubtedly, a very strong incentive for accession countries (the less well-off ones in particular). Though more developed than the average, Sweden and Finland were not an exception: before they joined in 1995, both countries negotiated for recognition of the specific problems in their sparsely-populated Arctic areas, making them eligible for aid to develop these areas.

In Central and Eastern European countries, the most optimistic estimates were largely confirmed throughout the period preceding the 2008 crisis. Between 2000 and 2007, GDP in the EU12 grew at twice the rate of the EU15. In Latvia, Lithuania and Estonia, per-capita GDP in PPS grew annually by 9.6%, 8.6% and 8.2% respectively. Unemployment rates fell by 4.6 points in all “convergence regions” (regions with a per-capita GDP of less than 75% of the EU average and which coincide in large part with the EU12), but fell only half a point in competitiveness regions (which are richer)[13].

In terms of foreign direct investment, as soon as accession was confirmed, a true decoupling occurred between a) countries furthest to the East (Bulgaria, Romania and even Greece), which were previously excluded from the previous boom and became highly attractive to investors, and b) their Central and Western European neighbours, which had already benefitted from already established capital flows *(see Table 3)*.

13. European Commission, *Sixth progress report on economic and social cohesion*, 25.06.2009.

Table 3 ► Foreign direct investment at the national level

	FDI MARKET SHARE IN THE EU27 2000-2006 (%)	GROWTH BETWEEN SUB-PERIODS 2000-02 AND 2003-2006 (%)
Austria	2.5	66.7
Belgium	11.2	107.4
Bulgaria	0.5	512.8
Cyprus	0.3	36.3
Czech Republic	1.3	5.1
Denmark	1.8	-36.3
Estonia	0.2	218.0
Estonia	0.2	218.0
Finland	1.9	36.0
France	18.2	70.3
Germany	12.9	-67.3
Greece	0.4	803.0
Hungary	1.0	174.9
Ireland	1.8	-132.2
Italy	3.9	954.8
Lithuania	0.2	96.7
Luxembourg	1.0	-43.0
Latvia	0.1	154.9
Malta	0.1	516.3
Netherlands	5.8	-91.5
Poland	2.4	105.0
Portugal	1.4	7.5
Romania	0.6	4369.6
Spain	7.0	-60.1
Sweden	4.9	-2.6
Slovenia	0.2	122.8
Slovakia	0.8	136.9
United Kingdom	17.5	150.2
EU	***100***	***2.0***

Source: José Villaverde and Adolfo Maza, *Inward Foreign Direct Investment in the European Union Regional Distribution and Determinants*, SIEPS, 2012.

This trend increased from 2005-2007. Average annual net foreign direct investment equalled just over 5% of GDP in all EU12 countries, but was negative in the EU15. Record rates were seen in Bulgaria (19% of GDP), Estonia (8% of GDP) and Romania (7% of GDP).

The link between the single market and cohesion policy was made all the stronger over time by the benefits it brought to more developed member states. During negotiations for the first Financial Framework (the "Delors 1 Package"), one argument used to convince richer members to accept the doubling of the cohesion budget was that money given to poorer regions would indirectly benefit the economies of others. In addition to the immediate prospect of new markets, export opportunities could also be expected as a result of increased demand in developing regions.

This theory was confirmed in the early 2000s in a study conducted by the Directorate-General for Regional and Urban Policy[14], which estimated that 28% of structural funds given to the four least developed member countries (Spain, Portugal, Greece and Ireland) "leaked" to other member states between 2000-2006 in the form of imports. This knock-on benefit occurred because recipient countries were obliged to use European suppliers[15] and because commercial ties between member countries were strong. In its third report on economic and social cohesion, the European Commission confirmed these positive effects: *"On average, around a quarter of structural expenditure returns to the rest of the Union in the form of increased imports, especially of machinery and equipment. This 'leakage' is particularly large in the case of Greece (42% of expenditure) and Portugal (35%)."*[16]

Table 4 ► Trade effects of Objective 1 intervention, 2000-2006

	LEAKAGE TO EU COUNTRIES (% OF OBJECTIVE 1 INTERVENTION)	LEAKAGE TO NON-EU COUNTRIES (% OF OBJECTIVE 1 INTERVENTION)
Greece	42.6	3.8
Spain	14.7	13.2
Ireland	26.7	11.1
Portugal	35.2	6.7
New Länder	18.9	9.4
Mezzogiorno	17.4	8.6
Total	***24.3***	***9.1***

*: Imports as % of expenditure under the Structural Funds.

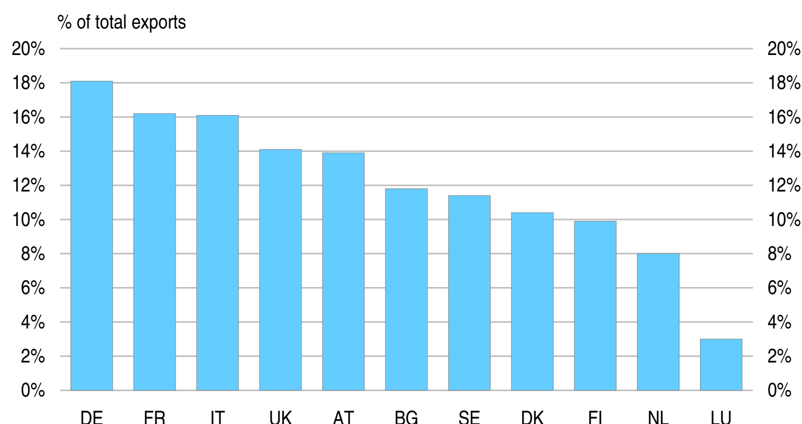
Source: Eurostat / European Commission, *Third report on economic and social cohesion: A new partnership for cohesion*, January 2004.

More recently, the Polish Ministry of Regional Development tried to evaluate the benefits for EU15 countries of funds allocated to Poland under cohesion policy, including contracts obtained by companies as part of projects co-financed by the EU, as well as additional exports to Poland tied to increased demand of intermediate and consumer goods. The study[17] concluded that for the 2004-2009 period, around 27% of the funds received by Poland found their way back, either directly or indirectly, to EU15 countries. Germany was the big winner with nearly €2 billion in additional exports, ahead of Italy and France, which each gained €500 million in exports. Forecasts for the 2004-2015 period are even higher because they are counting on an accelerated recovery of the Polish economy. *"From each euro spent on the implementation of cohesion policy in Poland, EU15 countries will receive the return of 36 cents in the form of additional export of goods and services (direct benefits) or even 46 cents if we deduct their own payments under cohesion policy from the cost (indirect benefits)"*[18]. By extrapolation, it is plausible that funds allocated to the EU12 will bring "returns" to the EU15 of approximately €70 billion over seven years.

14. Jörg Beutel, "The economic impact of objective 1 interventions for the period 2000-2006", *ECFIN working papers*, 2002.
15. This community-level practice is along the lines of "tied aid", which is often used in development aid policies. See Corinne Balleix, *L'aide européenne au développement*, DILA, Collection "Reflexe Europe", Série "Institutions & Politiques", Paris (in French).
16. European Commission, *Third report on economic and social cohesion: a new partnership for cohesion. Convergence, competitiveness, cooperation*, January 2004.
17. Skrok Lukas, *Evaluation of benefits gained by EU15 states as a result of the implementation of cohesion policy in Poland*, Study prepared by the Institute for Structural Research, Warsaw, Ministry of regional development, Warsaw, 2010.
18. Skrok Lukas, *ibid*.

The HERMIN model used by the Commission confirms the extent of gains for most net contributor countries based on exports from cohesion policy recipient countries *(see Graph 3)*.

Graph 3 ► Share of main export member states towards recipient countries (2008)



Source: Eurostat, COMEXT database

Source: European Commission, *Fifth report on economic, social and territorial cohesion: Investing in Europe's future*, November 2010.

Concretely, while the direct recipients of cohesion policy funds have changed over the last 25 years, the catching-up mechanism provided by European structural interventions is an ongoing source of the secondary movement of capital, whereby 30-40% of EU funds are transferred to the more developed contributing countries.

2. A partnership sorely tested by two major developments

2.1. The crisis reveals the limited leveraging capacity

In its eighth progress report on cohesion, published in June 2013[19], the European Commission took note of the breach: "*The crisis brought to an end a long period during which regional disparities in GDP per head and unemployment were shrinking*".

2.1.1. Numerous disruptions to national and regional progress

This report, which uses statistics from 2007 to 2011 to assess the impact of the crisis on GDP and employment in regions and cities, reveals a large number of disruptions to national and regional progress.

The first set of data on the impact of the crisis at the national level indicates major differences from country to country.

Most affected are the Baltic countries: over the specified period, average annual GDP shrank by 4.5% in Latvia, 2% in Estonia and 1.5% in Lithuania. Employment rates fell by 6.4%, 2.7% and 2.7% respectively. Average annual GDP also shrank considerably in Greece (-3.9%), Ireland (-1.8%) and Spain (-0.7%). While Italy's gross domestic product shrank more than Spain's (-1.1%), it did not experience a similar drop-off in employment (-0.4%, as opposed to -2.7% in Spain).

19. European Commission, *Eighth progress report on economic, social and territorial cohesion: the urban and regional dimension of the crisis*, June 2013.

With average annual growth of 3.7% between 2007 and 2011, Poland is an exception: it came out of this five year period unscathed, despite the catching-up process previously underway in other CEECs being stalled.

If this analysis is extended to 2004- 2011 for the purpose of comparing per capita-GDP across all EU countries, variations are even more striking *(see Table 5)*.

Table 5 ► Impact of the crisis on per-capita GDP growth in the EU27 between 2004 and 2011

MEMBER STATE	PER-CAPITA GDP (2004)	PER-CAPITA GDP (2007)	PER-CAPITA GDP (2008)	PER-CAPITA GDP (2009)	PER-CAPITA GDP (2011)
Luxembourg	251	275.2	279	273.4	274
Czech Republic	75.2	80.1	80	81	80
Malta	74.4	76.4	78	78.7	83
Slovakia	56.7	67.7	72	71	73
Estonia	55.7	68.8	68	67.7	67
Lithuania	51.1	59.3	61	58.6	62
Poland	50.7	54.4	56	57.1	65
Latvia	45.5	55.7	56	54.3	58
Romania	34	41.6	47	45.1	49
Bulgaria	33.2	37.7	44	42.5	45
Ireland	141.4	148.1	133	136.2	127
Netherlands	130	132.2	134	132.9	131
Austria	128.7	122.8	124	124.3	129
Denmark	124.5	121.3	123	123.4	125
Belgium	124.4	115.7	115	116.4	118
United Kingdom	123	116.7	115	113.1	108
Sweden	120.3	122.8	122	122.8	126
Germany	115.8	115.8	116	115.8	120
Finland	115.5	118	118	117.1	116
France	112.3	108.5	107	107.6	107
Italy	107.4	103.4	104	104.2	101
Spain	100.7	105	103	103.9	99
Cyprus	91.4	93.6	97	97	92
Greece	84.8	92.8	94	92.3	82
Slovenia	83.3	88.6	91	88.9	84
Portugal	74.8	75.6	78	78.9	77
Hungary	64	62.6	64	63.4	66
European Union	*100*	*100*	*100*	*100*	*100*

Source: Eurostat data, adapted by author

Over the seven-year period studied, every EU12 country gained 10-15 points on the EU average (with the exception of Hungary, which levelled off). Among older member states, only Luxembourg saw significant growth of 25 points on the EU average, more than double the per-capita GDP in the next three highest-ranking countries: Netherlands, Austria and Ireland. Most EU15 countries remained stable, with the exception of France, Belgium and Italy, which lost just over 5 points on the EU average, and notably the United Kingdom, which lost 15 points.

The effects of the crisis became visible in 2009. In every EU12 country except Poland, Romania and Bulgaria, convergence towards the EU average slowed. In the EU15, the time at which the crisis hit national economies and the extent of its effects varied. From 2008, Ireland experienced unusual but fluctuating levels of growth, while in Spain, Greece and Portugal, impact came later. By 2011, after several additional years of progress, these three countries were back to where they were in 2004.

In its eighth progress report, the Commission also tried to measure (without developing extensively) the impact of the single market, based on the fact that cohesion policy was not substantially modified between 2008-2011. The report analysed changes in trade flows between member states. Overall, in 2009, the volume of exports and imports in the EU fell 15% to near 2005 levels. Imports to EU12 countries fell steeply between 2008-2009 – by 20%, on average (-28.8% in Latvia, -27% in Lithuania, -26.4% in Romania, -25.1% in Estonia, -23.9% in Bulgaria). Sometime later, the volume of exports then dropped, particularly in richer countries (-26.1% in Finland, -19.6% in Sweden, -18.8% in Italy, -18.4% in Austria). Export rates picked up in 2010, but given that imports to member countries remained sluggish, the increase is attributable to emerging countries outside the EU and only benefitted EU countries which are focused on these markets.

Since 2008, the single market has been neither the buffer nor the driving force it was expected to be in the large majority of the member states *(see Table 6)*.

Table 6 ► Changes in intra-European and extra-European trade in recent years

	%	CHANGE 2005/2006	CHANGE 2006/2007	CHANGE 2007/2008	CHANGE 2008/2009	CHANGE 2009/2010
Total exports in all member states	Intra-UE	12.7	6.5	2.1	-19.1	15.4
	Extra-UE	10.2	6.9	5.6	-16.2	23.0
Total imports in all member states	Intra-UE	12.9	7.2	1.8	-19.5	15.5
	Extra-UE	14.7	6.1	9.1	-22.9	25.0

Source: Eurostat, *External and intra-EU trade, a statistical year book* (2011 edition).

The eighth progress report also looks at the regional impact of the crisis. The gap between average per-capita GDP in the 20 richest and 20 poorest regions, which shrank from 4.9 to 4.6 between 2007 and 2009, deepened in 2010 and 2011. The Commission does not offer a general explanation for these developments, however. Nor does it identify any significant new trends, aside from the heightened volatility of metropolitan economies, where there has been a particular "*pattern of faster GDP growth in growing economies and faster decline in declining economies*".

2.1.2. Underlying factors: border effects, agglomeration effects, specialisation effects

The crisis seems to have halted the usual momentum of the single market/cohesion policy dyad. The reasons for this can be sought by expanding upon the Commission's findings and providing explanations based on studies of longer periods. Doing so uncovers certain inherent weaknesses in both instruments and in how they interact, which were hidden by the significance of the 2004 and 2007 enlargements.

An analysis[20] of regional cycle synchronisation based on two decades' worth of data (1988-2008) uncovers the structural causes of the halt in regional convergence, which the crisis did not prevent – and even made worse. This phenomenon is caused by two simultaneous mechanisms, the combined effects of which are sometimes doubled; at others, cancelled out.

- The first of the two are border effects: these effects explain the strong synchronisation of economic cycles in regions within the same country regardless of production factors and structural (social, geographic) characteristics. These effects have faded, though, following the creation of the single currency.
- The second of the two are agglomeration effects: these effects are mainly seen in high innovation, densely-populated regions. In the last twenty years, a new economic geography has clearly reflected the source of these changes in our post-industrial economies in which immaterial factors play an instrumental role. Synchronisation of economic cycles occurs between the most developed regions, independently of the country in which they are located. This is why tremendous growth (of two to three times the national average) has occurred in capital city regions of the most-populated member states of the EU12 since 2000. Per-capita GDP rose by 67 points in the Bratislava region between 2000 and 2010; by 54 points in Bucharest, and 34 in Prague. The downside to the combined effects of the mechanisms described above is that peripheral regions, which are no longer protected by national borders and are too far from dynamic regions to enjoy the benefits of this growth, are left behind.

The national impact of the crisis and the breakdown seen since 2008 can be explained by looking at other research. At the height of Europe's monetary crisis, certain experts were quick to point out that without an effectively functioning monetary union in the preceding ten years[21], cohesion policy was unable to correct the widening gaps between euro zone countries caused by fiscal adjustment plans and serious structural imbalances. According to Andrew Watt, this gap was caused by differences in per-capita productivity and job markets, which lead to highly divergent trends in unit labour costs.

Others consider that imbalances in per-capita GDP are more a symptom than a cause[22]. A comparative analysis of trends in sectoral specialisation[23] in EU countries from 1995 to 2007 confirms and clarifies Krugman's predictions[24]. Krugman believed that the single market would push less developed countries towards specialisation while more advanced ones (e.g. France, Germany, Netherlands and Denmark) would grow stronger and more diversified. Peripheral countries would be more exposed to asymmetrical shocks. Between 1995 and 2007, for example, hotel and restaurant services expanded considerably in Italy, Spain and Greece, and in Spain, the construction sector acquired a major role to the detriment of other sectors. Indeed, economic integration by way of the single market concentrated production in central regions after the accession of the 10 CEECs shifted the EU's centre to the East (from Eastern Belgium to Bavaria, exactly). The main losers were peripheral countries to the West and South, located far from consumer markets and unable to offer a significant competitive advantage in terms of labour costs or innovation.

As a result, since 2000, cohesion policy has not enabled remote regions to invest as needed to counteract the effects of agglomeration. Much has been said about the relatively small sums which structural funds represent (0.37% of EU GDP) and their inability to play a significant distributive role, but the question of strategy in the use of these funds remains. After encouraging the pursuit of excellence and advocating a rather vague goal of competitiveness between 2007 and 2013[25], the Commission suggested a new approach for 2014-2020 which recommends that regions adopt a less ambitious, but more realistic investment strategy that is adapted to their profile: a "smart specialisation strategy"[26]. Time will tell if this approach is more effective.

20. Fabien Labondance, "Synchronisation des cycles régionaux dans la zone euro", *Revue d'économie régionale & urbaine*, n°2, 2013, pp. 267-294 (in French).
21. Andrew Watt, "Solidarity and cohesion within and between countries in a Europe in crisis"; in *Solidarity: for sale? The social dimension of the new European economic governance*, Europe in Dialogue 2012/01, Bertelsmann Stiftung, Gütersloh, 2012.
22. Daniel Gros, "Macroeconomic imbalances in the euro area: Symptom or cause of the crisis?", *Policy Brief* n°266, CEPS, 2012.
23. Mouhamadou Sy, "Convergence des économies européennes : vingt ans après", *Note d'analyse du Centre d'analyse stratégique* n°286, 2012 (in French).
24. Paul Krugman, "Lessons from Massachusetts for EMU" in Torres F. Giavazzi F (Eds), Adjustment and growth in the EMU, London CEPR and Cambridge University Press, 1993.
25. Marjorie Jouen op.cit.
26. See the European Commission document "Cohesion Policy 2014-2020" and a France-specific guide (in French).

Further analysis of the integrating effect of the single market over the last five years can be bolstered by comparing current statistics with the changes that appeared following the ten-country enlargement, as from 2005.

At the time, a new "European division of labour" was clearly emerging which reflected both specialised production in different countries and the intensity of trade relations between countries[27]. A review of bilateral trade flows in an enlarged Europe[28] (adjusted for size effects) confirmed the existence – similarly pinpointed a few years earlier – of five major, highly-integrated zones: North-West Europe, the Baltic Sea, the Western Mediterranean, Central Europe and the Eastern Balkans[29]. Within these five zones were a few particularly integrated hubs formed by two to three countries, most often as a result of historical ties.

A longitudinal study of 1994-2004 data highlighted the relative stability of these zones following an adjustment to the new post-communist era. This continuity illustrated the importance of geographical, cultural and linguistic proximity in transnational exchange. Such an analysis provided a less monolithic vision of Europe as a territory structured according to a centre-periphery model and outlined new opportunities not only for economic partners, but for infrastructure network designers and those promoting transnational cooperation as well.

Nevertheless, it did not challenge the driving force of economic integration in the four most-populated countries – Germany, Italy, France and the United Kingdom – whose combined economies dominated the other 21 countries. Not only did the Continent offer the prospect of a great single market in the making, based on a traditional centre-periphery model; it also heralded polycentric trade integration structured around five major zones.

Recent data on intra-EU trade contradicts this relatively optimistic vision of economic integration, however. From 2003 to 2010, Germany's weight grew considerably as economic activity – and, by extension, external trade – slowed significantly in the three other member states. The role played by the Port of Rotterdam makes the Netherlands an exception to this trend. Conversely, certain central and eastern European countries are progressively emerging as significant production centres in the EU *(see Table 7)*.

Table 7 ► Share of certain member states in intra-EU trade in 2003 and 2010

	SHARE OF INTRA-EU EXPORTS (%)		SHARE OF INTRA-EU IMPORTS (%)	
	2003	2010	2003	2010
Germany	22.5	22.5	19.4	20.5
France	12.1	9.5	13.6	12.8
Italy	8.6	7.6	9.1	8.2
United Kingdom	8.4	6.5	11.0	8.9
Spain	5.4	5.0	7.0	5.6
Netherlands	11.0	13.2	7.0	7.4
Czech Republic	2.0	3.3	1.8	2.9
Poland	2.0	3.8	2.3	3.9
Romania	0.6	1.1	0.8	1.4

Source: Eurostat, *External and intra-EU trade, a statistical year book* (2011 edition).

27. Lucia Bogaerts, Marjorie Jouen, "Les échanges commerciaux sur le continent européen et leurs conséquences territoriales", Paper for the Jean Monnet Seminar, Université de Bordeaux – Sciences économiques, 2005 (in French).
28. This definition of enlarged Europe includes 29 countries: the EU-25, Switzerland, Norway, Romania and Bulgaria.
29. Marjorie Jouen, Solenne Moutier, Katy Welsch, "Cinq petites Europe, des flux commerciaux recomposés" in *Le courrier des pays de l'Est* n°1039, La Documentation française, 2003 (in French).

An analysis of bilateral trade flows between member states in 2012[30] shows that with the notable exception of Ireland (with the UK), Spain (with France) and Portugal (with Spain), Germany is the biggest trading partner in the Union. The volume of trade between Italy and Romania, Poland and Slovenia has fallen substantially, and trade between France and Romania – and with Central European countries in general – has also dropped off. The United Kingdom remains an important trading partner of Nordic and northwest EU countries only.

This post-crisis overview identifies structural gaps which the single market tended to exacerbate, and which cohesion policy did not help close. Inversely, when economic activity –and therefore trade – slowed, the effects were quicker and more substantial in the most open countries. Public aid –the European Social Fund (ESF) for example[31] – has subsequently been steered in their direction, leaving less dynamic regions alone to launch their recovery. It is not surprising that the least developed and peripheral regions have bottomed out or, worse, fallen behind.

The situation endured since 2008 does not invalidate the importance of cohesion policy as a medium- to long-term investment tool, or the crucial role it plays in boosting public investment in the Union's weakest economies. This crisis has demonstrated, however, that the urge to use cohesion policy as a counter-cyclical instrument[32] (as seen in certain actions taken by European leaders between 2009 and 2011[33]), could only be misleading and disappointing in the absence of rapid results.

The easing of co-financing rules for "programme" countries no doubt alleviated some of the pressure on national budgets and provided the fresh money needed for certain projects. Nevertheless, access to funding did not modify the European funds adopted for the 2007-2013 period. The rules governing cohesion policy, such as multiannual programming (though a strength which protects it from cyclical and political fluctuations) prevent it from having quick effects.

It must therefore be recognised that cohesion policy, as it was designed, can be complementary to the single market – and to growth – but cannot substitute them when they fail.

2.2. Globalisation generates new inequalities which the two policies cannot correct

Pointing out the limitations of the single market/cohesion policy dyad in a slowdown does not resolve the question of what will happen tomorrow. In other words, if there were a recovery, would it result in convergence?

This question was already present in the preparatory work for the adoption of the Europe 2020 Strategy, and led to the "European Platform against Poverty" flagship initiative. Poverty, which by the end of the 20th century had seemingly become a residual phenomenon in developed Western countries, is now a major problem which cannot easily be solved by regional growth.

Over more than a decade, a correlation has been found between certain regional contexts and income levels. In its 2011 report[34], the Commission points out that in the United Kingdom, Spain, Italy, Germany and Poland, the percentage of the population whose income levels expose them to poverty is over two times higher in less prosperous regions than in the richest ones. In Bulgaria, Romania and Latvia, over 30% of the population lives in poverty (and over 50% in three regions in Bulgaria). In outlying southern regions (like Sicily 49%), eastern regions (with the exception of Czech Republic and Slovakia) and western regions (e.g. Ireland), over 23% of people are poor. This analysis demonstrates once again the need for "territorialised" social policies and

30. Thierry Chopin, Michel Foucher (dir.), *Schuman Report on Europe, State of the Union 2013*, Fondation Robert Schuman/CES, 2013.
31. European Commission, *Proposal for a regulation amending Council Regulation (EC) No 1083/2006 as regards certain provisions relating to financial management for certain member states experiencing or threatened with serious difficulties with respect to their financial stability*, COM (2011) 482 final, 01.08.2011.
32. Marjorie Jouen, "Cohesion policy and the role played by structural funds in austerity" in D. Natali & B. Vanhercke Eds, *Social developments in the European Union 2011*, OSE-ETUI, Brussels, 2012.
33. Joint letter from Nicolas Sarkozy and Angela Merkel to Herman Van Rompuy on the joint French-German proposals to protect and enhance economic and monetary union as well as the stability of the single currency, 17 August 2011.
34. European Commission, *Seventh progress report on economic, social and territorial cohesion: the urban and regional dimension of Europe 2020*, 2011.

validates the proposal to combine all five structural and investment funds[35] within a strategic framework for the 2014-2020 programming period. However, such a reform seems compromised by the retention of specific and differing management rules for each fund.

Rather than be completely dismissed, this option should be compared against a more general trend mentioned in the eighth progress report, which provides new information on trends in poverty and social exclusion in the wake of the crisis. Household income grew in central and eastern European countries before the crisis; since 2008 it has fallen. Between 2008 and 2012, another 6 million people joined the ranks of those at risk of poverty or exclusion[36], bringing the current total to nearly 124.5 million – 24.8% of Europe's population. Of course, the crisis – which entailed job losses and cuts in social spending – played a major role in this impoverishment. In Latvia, disposable income per capita fell by nearly one-fifth in 2009; in Ireland, the percentage of people at risk of poverty exceeded 15% in 2011; in Spain, this figure was 21%; in Greece, 23%. Looking past the current downturn, however, poverty must be linked to a growing trend towards inequality in European countries.

According to the OECD[37], the phenomenon became particularly visible in developed countries in the mid 1980s and increased at the turn of the century. The Gini Coefficient, for example, rose from 0.25 in 1985 to 0.26 in 2000 and 0.30 in 2008 in Germany. In Sweden, it went from 0.21 to 0.24 to 0.26 in the same periods, and in France, from 0.29 in 1985 to 0.32 in both 2000 and 2008. In less well-off countries, the situation generally improved until the crisis, reflecting a positive development of the Gini coefficient between 1996 and 2007 from 0.43 to 0.39 for the EU27. This trend was reversed, however, in countries hard hit by the crisis, such as Greece and Spain.

Several scientific studies[38] in Europe have shown that this is the result of structural changes to the European economy and the kind of jobs it creates, as well as certain policy decisions – fiscal ones in particular. More recently, the new wave of globalisation has been blamed[39].

In this vein, François Bourguignon[40] points out that in the last two decades, the increased trade of goods, services and capital has closed income gaps at historical levels around the globe. It has also deepened inequalities within nations: either between regions or within a single region. According to Bourguignon, earnings of the wealthiest people in developed countries have soared as a result of technical progress: high salaries are paid by multinationals which have become global firms, and in the culture sector, worldwide audiences secured by information technology generate outstanding profits. At the opposite end of the spectrum, the lowest incomes are directly hit by the globalisation of trade: after low-end industrial production, delocalisation now affects services and, as a result, the educated middle class. Deregulation, which facilitates the emergence of private monopolies to replace public ones (large networks of public services and the financialisation of the economy – in other words an increase in the share of profit in world GDP), accentuates this trend even more.

In light of these pressures, the cohesion policy/single market dyad appears particularly depleted. In fact, the solutions offered by experts to contain rising inequalities, which are damaging to all[41] and strongly rejected in EU15 countries[42], primarily involve fiscal reform and the regulation of major network and banking sectors. Their proposals only marginally involve the areas covered by cohesion policy, insofar as they guarantee access to public services (education, transportation, health, etc.) for the less wealthy. The obligation of member states to allocate 20% of their 2014-2020 ESF endowments for initiatives to promote social inclusion and the fight against poverty seems to fall short of what is needed.

35. The ERDF, ESF, cohesion fund, EAFRD and the EMFF.
36. According to the European definition, people are at risk of poverty or exclusion either because their income does not allow them to meet their needs, because they are materially deprived, or because they live in a household with low work intensity.
37. Taken from L'Observatoire des inégalités (December 2011) (in French).
38. See the work of the INEQ and PROFIT projects, discussed in European Commission, DG for Research, *Why socio-economic inequalities increase? Facts and policy responses in Europe*, 2010.
39. Joseph Stiglitz, *The Price of Inequality*, W.W. Norton & Co., June, 2012.
40. François Bourguignon, *La mondialisation de l'inégalité*, La République des idées, Paris, 2012 (in French).
41. Richard Wilkinson and Kate Pickett, *The Spirit Level: Why Equality is Better for Everyone*, Penguin, 2010.
42. See IPSOS survey for Accenture and CESE, *Vivre ensemble, entre richesse et pauvreté*, 2013 (in French).

As for the single market, which European citizens accuse of speeding up globalisation, and which defenders of equality criticise for its link to excessive deregulation, appears less attractive to major, multinational economic partners. Its weight has been relatively weakened by trends in global trade[43]. The share of the EU in world exports fell from 45% in the early 1990s to only 36% in 2008. In the same period, the share of East and South-East Asia increased from 10 to 24%. Import data is similar: The EU's share of worldwide imports went from 45% in the 1990s to 40% in 2008, while imports to countries in East and South-East Asia jumped from 12 to 19%.

Since enlargement, the share of intra-Community trade in EU27 exports has steadily declined: 68.7% in 2003, 67.5% in 2008 and 65% in 2010. A comparison of 2003-2010 data on Europe's four historically biggest exporters reveals a comparable decline *(see Table 8)*.

Table 8 ► Shares in exports to the EU27 as a percentage of total exports (of certain member states)

%	2003	2010
Germany	64.9	60
France	66	60.9
Italy	62	57
United Kingdom	59	53

Source: Eurostat, adapted by author

Inequality, and its effects at both the individual and infranational level, appears subject to forces that are more sustainable and more powerful than the capabilities of the single market and cohesion policy.

43. Michel Fouquin, Houssein Gimbard, Colette Herzog et Deniz Unal, *Panorama de l'économie mondiale*, CEPII, December 2011.

CONCLUSION: ON THE PATH TO DIVORCE?

The crisis (the word refers to the idea of 'turning point' and 'opening opportunities'), has played its role perfectly, by calling into question the effectiveness of policies designed to re-launch European integration in the mid-1980s. For quite some time, criticism of cohesion policy focused on its minor role in comparison with the single market. Today, however, economic and social conditions have made observers critical of both. In the last twenty years, the single market and cohesion policy worked closely together to ensure that the immediate benefits of some became the longer-term benefits of others. The partnership's strength ensured the solidity of an ever-growing European Union. The bond only worked in economic realms, however (and, to a lesser extent, social ones).

In recent years, attempts to renew this approach, with the introduction of the notion of territorial cohesion, on one hand, and the single market Act on the other, have not been frankly successful. The cohesion policy/single market dyad has lost steam and appears to be nearing the end of the line.

Despite this, cohesion remains a major challenge for the European Union: it is the foundation of the affectio societatis between citizens. If the current economic "detour" becomes a dead end, is it not time to explore other ways of uniting Europeans, rather than divide them? Should cohesion policy not be invested with a broader role than simply increasing GDP?

Among all the possible exits from the crisis, the most pressing is no doubt the transition to new ecological and energy models. This would confirm the divorce between the single market and cohesion policy – a risk which, until now, no one has dared take. It may be an obligation today.

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