

**EUROPEAN UNION REGIONAL POLICY  
MEETS THE CHALLENGE OF ENLARGEMENT:  
INERTIA OR REFORM?**

**Paulo Vila Maior**

Professor Auxiliar - Faculdade de Ciências Humanas e Sociais (UFP)

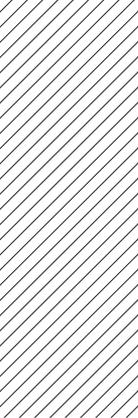
[pvm@ufp.pt](mailto:pvm@ufp.pt)

### **Resumo**

O último alargamento é um acontecimento singular na vida da União Europeia (UE). A consequência mais notória é o acréscimo de heterogeneidade no interior da UE. Como as assimetrias de rendimento entre os Estados membros são mais acentuadas, interrogamo-nos se o funcionamento equilibrado da União não está em perigo. Faz sentido questionar o papel desempenhado pela política de coesão económica e social (em especial pela política regional). O artigo analisa duas soluções alternativas: a preservação do actual *statu quo* e a reforma da política regional.

### **Abstract**

The recent enlargement is unprecedented for many reasons. One of the most visible implications is the sizeable heterogeneity that characterises the European Union (EU). Since income differentials between member states have widened, the question is whether the EU is affected by this intense heterogeneity. Therefore, the role of cohesion policy (especially regional policy) is at stake. The paper examines two alternative solutions: the preservation of the existing *statu quo* and the reform of regional policy.



## INTRODUCTIO

When viewed from an economic perspective, the recent enlargement (2004-2007)<sup>1</sup> is the most demanding of all. The number of member states increased from fifteen to twenty seven (membership increased 80%). The figures of the new member states in the overall economic, demographic and geographic structures of the Union are, nevertheless, less impressive (see table 1).

Member states	Area (1,000 km <sup>2</sup> ) - 2005	Population (million) - 2004	GDP (million €) - 2005
EU15 member states (together)	3,236	384.8	10,284,860
New member states (together)	739	74.2	557,053
% of new member states on EU25	18.6%	19.2%	5.13%

**Table 1** - Member states' absolute and relative weight: geography, demography, and economy [Source: European Commission (2006a)].

One of the unresolved issues is EU cohesion policy. I follow the definition of cohesion policy put forward by the Sapir Report (Sapir et al. 2003). Cohesion policy encompasses three distinct vectors: regional (or convergence) policy, social policy and the Common Agricultural Policy (CAP). Distinct government layers interact in these vectors. From shared competences (regional policy), to national powers (social policy), and EU exclusive competence (CAP), complexity emerges when the institutional architecture of cohesion policy is at stake (Alesina, Angeloni and Schuknecht 2001). In practice both the EU and national governments are important players in cohesion policy.

The paper is structured as follows. Section one presents the context underlying the recent enlargement. It emphasises the opportunities and constraints, notably the opportunistic behaviour of the fifteen member states in the negotiation process. Section two focuses on the challenges EU regional policy faces, exploring two alternative solutions: to keep the current *statu quo* or to change the rules in order to deliver enhanced inter-regional redistribution.

## 1. THE CONTEXT

The membership of the ten Central and Eastern European Countries (CEECs), as well of the two small Mediterranean countries, brought important consequences for the homogeneity of the Union.

The gap between the richest and poorer countries has dramatically worsened, as table 2 shows. While before enlargement the gap was 79.6 percentage points, with the redefinition of poorer countries after enlargement the gap rose to 114.6 points. If this index is seen as a measure of heterogeneity within the EU, enlargement produced a deteriorated pattern. In relative terms, the gap has risen almost 44%.

UE15 (member states)	GDP per capita (PPP), 2005 (EU25=100)	UE25 (member states)	GDP per capita (PPP), 2005 (EU25=100)
<b>3 poorer</b>		<b>3 poorer</b>	
Portugal	71	Latvia	46
Greece	83	Poland	50
Spain	98	Lithuania	51
(1) Non-weighted average	84.0	(1) Non-weighted average	49.0
<b>3 wealthier</b>		<b>3 wealthier</b>	
Luxembourg	230	Luxembourg	230
Ireland	138	Ireland	138
Netherlands	123	Netherlands	123
(2) Non-weighted average	163.6	(2) Non-weighted average	163.6
(3) Gap (2-1)	79.6	(3) Gap (2-1)	114.6

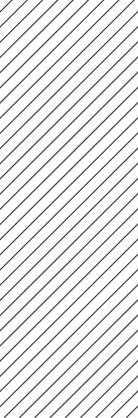
**Table 2** - Gap between the wealthier and the poorer member states before and after enlargement [Source: European Commission (2006b) and own calculations]

Two remarks about the methodology. On the one hand, I am aware that the non-weighted averages are questionable. It would be more accurate to weigh each member state economy and add a coefficient to the income disparities observed. Anyway I am just trying to compare the richest with the poorer member states before and after enlargement. The purpose is not so much to reach a sound statistical inference, but only to provide a clear picture of the increased income gap between the two groups of countries. On the other hand, I have chosen a group of three member states for both ends of the spectrum. This option is also open to criticism: why three and not more? The answer is that such option was arbitrary.

Assuming that there are minimum standards of inter-state solidarity in the EU, the question is whether the enlargement is a challenge to EU cohesion policy. The perception that the massive income gap that emerged with enlargement might be an enduring seed of instability within the Union makes it reasonable to discuss how desirable (and feasible) is the reform of EU cohesion policy. In the remainder of the paper I will focus only on one of the three aspects of cohesion policy – regional policy. Important questions emerge: is the current EU regional policy equipped to deal with enlargement? Will the ambitious enlargement call for change in the goals, characteristics and operation of regional policy? Is the enlarged EU likely to work smoothly with such sharp differences, thereby removing any rationale for reform?

The challenges from enlargement encompass a trade-off. On the one hand, the current *statu quo* is encouraged by those member states that were in the Union. They look at the enlargement as a matter of self-interest. Indeed they are not very much concerned with the specific interests of the new member states (Gillingham 2003). Although politicians' rhetoric emphasises an opposite conclusion, negotiations were driven bearing in mind each member state's egocentric interests. There is, however, a problem with this strategy. *When individual national governments face the implications of an enlarged EU, they neglect the overall impact on the Union.*

<sup>1</sup> Most of the new member states (Poland, Hungary, Czech Republic, Slovakia, Slovenia, Estonia, Lithuania, Latvia, Cyprus and Malta) became members of the European Union in 1 May, 2004. The accession of Bulgaria and Romania was delayed until 1 January, 2007.



This is the flipside of the trade-off. An enlarged EU is not only an ambitious project that highlights the grandeur of politicians. If national governments' priorities also address the future of the Union, they should devote their attention to the enlargement effects to the EU as a whole. They should accordingly recognise that a larger Union with additional heterogeneity has a potential for turmoil.

Maybe the process of European integration is giving reason to the architects of liberal inter-governmentalism (Moravcsik 1993, 2001). National governments make their calculations bearing in mind the costs and benefits of EU developments, and increasingly measure them against a domestic yardstick. National interests are the main priority for a vast majority of national governments. Cooperation – not to mention supranational governance – is not as powerful as before. There are several motivations behind this sceptical assessment. One of the most powerful is the reluctance to take the interests of other member states into consideration, particularly when economics sound bad. Furthermore the EU lacks strong political leadership committed with the future of European integration. Consequently, member states incorporate their own interests and bypass an overall assessment of European integration. Therefore, the promises behind the ambitious enlargement are fading away. They are, at best, a glimpse of the past that was lost throughout the years (Gillingham 2003).

Behind the curtains of national egoism (of the fifteen member states) lies a deceptive outcome with two negative implications. First, the new member states might feel betrayed because the promises of enlargement are far from being met. Second, while the EU witnessed an unprecedented enlargement, its institutional apparatus and budgetary framework remained untouched. The creature risks blowing out the straitjacket that suffocates it. The homework seems that has not been duly prepared. The blame is endorsed to the member states that opened the doors of the EU to the accession countries.

## **2. REGIONAL POLICY AND ENLARGEMENT: KEEP THE RULES OR CHANGE THE STATU QUO?**

The integration of twelve new member states represents a considerable challenge for the EU. The main test comes from mixing two groups of countries with sharp economic differences and large income differentials. Even the new member states are far from being a homogeneous group (Mayes 2001). Diversity and confusion loom vigorously. The outcome is a heterogeneous EU – more than it already was.

The Treaty on the European Union (TEU) establishes, in article 2, that sustainable development is undertaken at the national and supranational levels. If this aim is taken seriously (together with the particular objective of cohesion within the EU territory, according to article 158 of the TEU), it provides a clear picture of the challenges ahead. At least in theory, the EU presupposes a minimum degree of inter-state solidarity. This is the starting point for a different approach to the deep challenges related with heterogeneity within the EU, both for the countries that opened the doors of EU membership to the new member states, but especially for these. If it is true that enlargement to the Eastern countries has a political nature tied to an historical mission – to remove the sequels of the cold war that artificially split the continent (Sedelmeier 2000, Friis 2003, and Glenn 2003) – the duties of the EU cannot be disregarded.

The new member states expect to leave behind the daunting consequences of the past. It is also expected that the Union warmly welcomes them but, at the same time, has something to offer. The EU and its fifteen member states feel proud of the historical achievement beneath the enlargement. This is the evidence that the EU already gained a lot with the membership of the new member states. It is wrong to assume that the twelve new member states are the only net gainers.

Assuming the strategic challenges that come to the surface, as well as the specific context of the enlargement process, it is worthy to discuss the role that the EU regional policy might play to help the smooth transition from fifteen to twenty seven member states. It is not only large income differentials that are at stake. It is the operation of the EU that might be in danger if the enlargement doesn't bring change in regional policy.

Several reasons encourage the preservation and a profound change of regional policy. The goals underlying both alternatives differ. The supporters of the current *statu quo* argue that EU regional policy works well enough to accommodate the new member states without further tensions (Sapir et al. 2003). They dig into the past to claim that regional policy worked well for the laggard member states. Spain, Portugal, Greece and above all Ireland narrowed the gap vis-à-vis the EU average (see table 3).

	1988-93	1993-98	1998-2000
Greece	1.2	2.6	3.6
Ireland	4.4	8.5	8.7
Portugal	2.6	3.4	3.3
Spain	2.0	3.1	3.9
UE12*	1.7	2.3	2.4
UE15	1.7	2.4	2.9

**Table 3** - GDP growth (%) in the cohesion member states (1988-2000) [Source: European Commission (2001)].

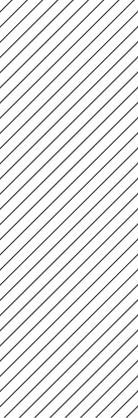
\* UE12: member states of the Euro-zone.

Furthermore, empirical evidence shows that structural funds provided a crucial input to these countries' growth (see table 4). If EU regional policy performed well in these cases, why should it be changed?

	Demand effects			Supply effects			Total effects		
	1994	1999	2020*	1994	1999	2020*	1994	1999	2020*
Greece	1.1	4.8	1.5	0.1	4.6	8.0	1.2	9.4	9.5
Ireland	6.2	5.9	4.0	-	3.4	8.4	6.2	9.3	12.4
Portugal	7.0	8.1	7.6	-	1.1	1.3	7.0	9.2	8.9
Spain	1.9	2.9	1.9	-	1.4	6.8	1.9	4.3	8.7

**Table 4** - Impact of the structural funds (additional GDP growth effects, in %) [Fonte: European Commission (1999)].

\* Estimation.



Interestingly, these arguments provide the intellectual support for changing regional policy. First the recent enlargement is substantially different from previous enlargements, not only for a reason of scale (a massive enlargement) but especially because the new member states brought intensified heterogeneity to the EU. In addition, the new member states are more distant from the EU average than Ireland, Greece, Portugal and Spain when they became members of the European Communities (Kuznetsov 1999). Not to mention that EU regional policy was changed (the Delors Package II) with the purpose of helping the cohesion member states in the eve of Economic and Monetary Union (EMU) (Tsoukalis 1997). Now that the challenges are deeper a fundamental change in EU regional policy makes sense. Especially because past changes were linked to side payments for member states that were net losers with EU developments (Fenge and Wrede 2004).

Aside the differences of arguments, one aspect is common to the contrasting approaches: they both accept that the goal of economic and social cohesion is instrumental to a sustainable EU now that it became enlarged. The differences are a matter of degree. The supporters of the *statu quo* maintain that the current regional policy is well equipped to meet the challenges from enlargement. Conversely, those who call for change anticipate that the existing regional policy is not able to cope with such challenges. Therefore change is needed to avoid turmoil within the EU. Granting EU membership to the new member states might not be enough to get them out from poverty inherited from the communist era (in the CEECs case).

## 2.1. THE RATIONALE AGAINST THE REFORM OF EU REGIONAL POLICY

The reasons presented by the opponents of change are powerful. First, the current state of art of European integration, dominated by *each member state's individualistic needs and interests*, does not promote change. Since interests towards the accession countries are varied across the fifteen member states, it is difficult to anticipate a consensus encouraging change in EU regional policy rules. It is important to remember that changing these rules requires unanimity (Bache and George 2006). Hence, the obstacles are burdensome. This is a policy arena where inertia is likely to prevail over the next years (again assuming the current context of absent political willingness to foster change). Member states' aversion to prompt change, coupled with the institutional complexity that dominates the rules of regional policy, provide a forceful argument for keeping the rules.

Second, the *statu quo* in the EU is also influenced by a *deadlock in budgetary reform* (Blankart and Kirchner 2003). Inertia was inherited from the previous bargaining round for multi-annual budgetary package for 2000-06 (Agenda 2000). The outcome was marked by minimum agreement. The reason was national governments' unwillingness to feed the EU with more resources. At that moment it was particularly noticed contributor member states' fierce opposition (Galloway 1999).

The same tendency flooded the negotiations about the budgetary deal for 2007-13 (EUObserver, 30 March 2004). Again contributor member states resisted to increase the size of EU budget revenue. As before, key member states refused to reform the expenditure side of the budget (notably by reducing the big item devoted to Common Agricultural Policy). The deadlock seems more problematic than before because (pre-enlargement) cohesion countries refuse any cut in the funds they receive. New member states ask for more transfers to tackle structural difficulties they still face. At the end the EU is immersed on a dilemma.

Institutional complexity characterises the EU, notably when unanimity is required. Low speed European integration, if not paralysis, is the expected outcome (Salmon 2003). Budgetary multi-annual packages require unanimity (Ginsberg 2007). Since donor member states are not willing to increase contributions to the EU budget, conditions for upgrading regional policy are absent because this outcome depends from revenue increase in the EU budget. Furthermore net recipients (pre-enlargement cohesion countries) can block any decision against their particular interests.

Consequently, changing EU regional policy seems out of question. Maybe with a different constitutional context change is possible. The Treaty of Nice established that from 2007 onwards decisions on regional policy can be taken by qualified majority vote (Galloway 2001). Nevertheless the implementation is delayed until the 2014-20 budgetary package is enforced. In practice, the reform of EU regional policy is postponed for the medium term.

The third reason that encourages the current *statu quo* is *macroeconomic turmoil that still affects the European economy* (Grimwade 2003). All member states were affected by sweeping recession. The leeway for adjustment through fiscal policy is hampered by fiscal consolidation in Euro-zone member states. This is not the appropriate scenario for changing EU regional policy. Many member states are trying to deal with the cumbersome fiscal situation they fell into. They are not interested in expanding the mess by saying yes to EU regional policy reform that would ask them to supplement their contribution to the EU budget.

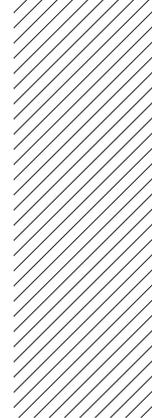
Fourthly, some studies point that *the existing regional policy is well equipped to help the new member states* (Sapir et al. 2003). The resources currently available through regional policy are likely to produce a positive effect. It is suggested that cohesion policy must be re-focused. The goal is to drive resources away from CAP and concentrate them on regional policy. The prediction is that the new member states will be able to seize the funds and to narrow the gap between them and the EU average.

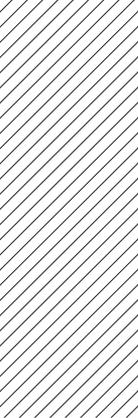
## 2.2. THE REASONS FOR CHANGING EU REGIONAL POLICY

Despite the persuasiveness of the previous arguments, it is important to examine the rationale of different regional policy. On the one hand, *heterogeneity is a powerful reason for intense inter-regional redistribution*. The motivations are twofold. First, the EU is a polity with minimum solidarity standards among member states. This does not imply that the EU gets closer to nationhood bonds that characterise federations elsewhere. The EU is not supposed to evolve towards a statehood dimension, anyway (Weiler 1999). A minimum degree of internal cohesion is a pre-condition for the proper operation of the EU. Therefore, huge income imbalances between different regions cannot be neglected.

Secondly, *deep heterogeneity between member states and regions can affect EU sustainability*. It might be difficult to envisage the EU made of a group of member states where far-reaching, long-lasting income heterogeneity persists. Social forces in poorer member states might push for change. If their overall situation doesn't improve, and the catching-up process delays, it is likely these member states put the blame on the EU.

The path-dependence of inter-regional solidarity is inextricably linked with European integration. It exerts strong pressures for changing EU regional policy. Certain societal forces might trigger this kind of pressure. They are likely to emerge in the new member states, but





they can also emerge in wealthier member states. A powerful wave of change might rush. Then it will be difficult to stop it. For reasons of domestic political agendas, more and more national governments will gather the momentum for change.

On the other hand, a reformist rationale is anchored to *the urgency to undertake structural and administrative reforms in the new member states*. They were initiated with the transition towards EU membership. The successful accession into the EU does not necessarily signal that the job is already done (Gillingham 2003). Much remains to be accomplished. Only naïve spirits would conclude that membership is the endgame of structural adjustment these countries began. To stop the process entails dangerous implications. It could reverse the wave of change that was triggered some years ago when these countries were set on track to be full members of the EU.

Hence funds must be channelled to the new member states to support their unfinished reform. The funds are designed to help the new member states' long-run development. They do not, however, generate immediate effects to the catching-up process. For this reason regional policy needs to be reformed to allocate resources for structural and administrative reforms, but also to distribute funds that alleviate poverty in these countries (Gillingham 2003).

The final reason is connected with the ontological meaning of European integration. As it was highlighted before, *the membership of the EU is a mutually beneficial business*. The new member states expect positive effects from EU membership. The fifteen member states and the EU itself also take advantage of enlargement. Reciprocity not only feeds solidarity within the EU and among its member states, but also unfolds the nature of European integration: it is a *contract* that ties all member states.

As a contract it involves rights and duties. It is unfair that these rights and duties are evenly distributed across member states, irrespective of their size, population, income, and responsibilities in European integration. According to this contractual approach, the fifteen member states have special obligations when enlargement is envisaged as a successful outcome. To emphasise that enlargement is one of the most ambitious ventures of European integration is only rhetoric. Its practical implications require more than scanty statements that embellish official ceremonies and politicians' apparent commitment towards a larger and deeper EU.

Solid steps must be taken in order to accommodate the new member states. This is the special duty that the EU and its member states must recognise. They should meet the new member states' expectations. It is therefore crucial that regional policy undergoes a fundamental reform to become suitable for the specific needs of the new member states. Otherwise the coherence of the EU might be at risk in the future.

## CONCLUSIONS

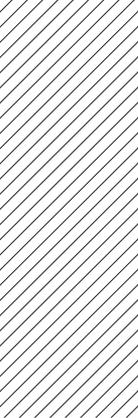
The increased heterogeneity that characterises the EU after the recent enlargement puts some important questions. Is this heterogeneity likely to affect the coherent operation of the EU? Do large income imbalances between member states frustrate European integration? Is it likely that inter-state solidarity comes to the forefront, conveying alternative solutions to address such heterogeneity?

The paper examined the answers EU cohesion policy might offer. From the three parcels of cohesion policy (regional, social and agricultural policies) the paper focused on the first one. Two alternative solutions were assessed. The first accepts the current *statu quo*, concluding that the existing regional policy is well equipped to deal with the challenges ahead. The second argues for a more interventionist regional policy. This solution envisages active inter-regional redistribution, at the supranational level, as the panacea for the problems arising from enlargement.

After discussing the pros and cons of each solution, and bearing in mind the distinctive context in which the EU moves, my conclusion is that the (theoretically) desirable solution is not feasible. Theory divorces from practice. Although persuasive arguments might push for a reform of EU regional policy, the awareness that member states' interests are the key priority and the macroeconomic rationale beneath EMU are the powerful obstacles to such outcome. The future days will tell whether persistent income asymmetries (if they are not corrected in the meantime) will not jeopardise the EU.

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