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Briefing Note

May 2017

CPMR supporting briefing for the conference

'Which place-based approach to EU investments? A case study on Islands and Outermost Regions'

SUMMARY:

This Briefing note has been drafted to help stimulate a fruitful discussion in relation to the SEARICA conference 'Which place-based approach to EU investments? A case study on Islands and Outermost Regions' organised on 18 May

It is organised as follows:

- **Section 1** provides background and contextual elements for the conference
- **Section 2** presents the main issues linked to future EU policies and instruments supporting investment at territorial level
- **Section 3** lists considerations and proposals for the future

1. Introduction and background

This briefing note provides an analysis and background elements from the CPMR General Secretariat to stimulate a debate at the SEARICA conference entitled 'Which Place-Based Approach to EU Investments?' on 18 May.

Discussions on the future of the European Union, including its budget and policies after 2020, are in full flight. This conference aims to contribute to the discussion on the future of Europe by focusing on the need for a place-based approach to EU investments in the post-2020 period.

This issue is central to the Conference of Peripheral Maritime Regions (CPMR) and its Members, which include island regions and outermost regions.

The risk of a spatially blind approach to investment policies and programmes at European Union level which would primarily rely on financial instruments (loans, guarantees) is becoming a very real one, particularly in a context of a shrinking EU budget post-Brexit.

Peripheral and Maritime Regions – and islands and outermost regions in particular - would be the first to miss out on a centralised approach to EU policies towards investment, jobs and growth.

The CPMR starts with the premise of territorial, economic and social cohesion as Community objectives at the service of EU solidarity. Such principles allow the inhabitants of the different territories of the Union to benefit in an equitable way from the basic freedoms set out in the Treaty and implemented through the Community's policies.

3.5% of the European Union's population that lives on island and outermost regions know first-hand that in practice people's ability to travel, their access to goods, services, capital or knowledge, or to put it simply their access to basic freedoms and the internal market, are influenced to a large extent by the geographic characteristics of these territories.

In light of this, the conference will address the following issues:

- Will the EU budget be an investment budget after 2020?
- How to ensure that the principles of balanced territorial development and territorial, social and economic cohesion are at the core of a reformed European Union?
- Which strategie(s) for investment at European level for the post-2020 period?
- How does one ensure that the unique challenges faced by specific territories (islands and outermost regions for instance) are taken into account for the post-2020 period?

The case studies presented by the three CPMR regions will address these issues directly. Many of the issues and considerations below will be presented by the CPMR secretariat during the conference.

2. Which future for EU support to investment at territorial level?

This section analyses recent developments linked to future EU support to investment at subnational level.

2.1 What do the White Paper on the Future of Europe and reflection papers say about possible future EU investment policy(ies)?

The 60th anniversary of the Treaty of Rome in March this year marked the beginning a long-term reflection on the future of Europe. The European Commission broke with tradition by proposing five scenarios exploring different avenues for reform for the European project in its White Paper on the future of Europe. Since then, two other reflection papers have been published to look at the social dimension of Europe and harnessing globalisation.

White paper on the future of Europe
Each of the scenarios put forward in the White Paper on the Future of Europe question the historical 'raison d'être' and missions of the European Union, leaving no stone unturned. With regards to the EU supporting territorial development, there are two opposing views, encapsulated by Scenario 4 and Scenario 5:

- In Scenario 4 "Doing less more efficiently" it is stated that "the EU27 stops acting or does less in domains where it is perceived as having more limited added value, or as being unable to deliver on promises. **This includes areas such as regional development…"**

Whereas…

- Scenario 5 "Doing much more together" includes the sentence "**Additional EU financial support is made available** to boost economic development and **respond to shocks at regional**, sectoral and national level"

Social dimension reflection paper
The European Commission published its first reflection paper on the social dimension of Europe on 26 April 2017.

The rather excellent analysis under section 2 of the paper ('Today's social realities') includes the following points:
- the **'convergence'** towards higher living standards is part of Europe's model and is achieved via single market integration and thanks to support from EU funds
- **disparities of development between Member States and regions** persisting and increasing gaps of development between capital cities and other regions

While the CPMR can generally agree with the analysis provided in the paper, it cannot support all scenarios presented in the same paper:
- Scenario 1 ('Limiting the social dimension to free movement') recommends **shrinking or abolishing European regional funds**

- Scenario 3 ('Deepening the social dimension of Europe') talks about EU funding supporting human capital issues, but these funds would be made conditional for Member States to adopt certain structural measures

Harnessing globalisation reflection paper
The second reflection paper published on 10 May 2017 provides some interesting insights as to what future EU investment policies could look like:
- Terms such as **'solidarity', 'social cohesion', 'redistributive policies'** feature heavily under section 4, which also includes a dedicated section on 'empowered regions' and the need to 'target regional and local investment needs, skills gaps and regulatory obstacles to ensure that all regions can benefit from the internal market'
- **Cohesion policy and EU Structural and Investment Funds being key to supporting investment**, innovation and long term 'conversion' strategies

What it means for peripheral and maritime regions?

- **EU (grant) support to investment in regions cannot be taken for granted in the future.** Scenarios resulting in a 'two speed Europe' or a refocus of EU action on core priorities (as alluded in Scenario 4 of the White Paper) would be particularly detrimental to peripheral regions

- Rather than choosing a preferred course of action for the European Union and proposing for instance a follow up to the Europe 2020 strategy for growth and jobs, the European Commission seems to prefer leaving all options open for Member States and the European Parliament to ultimately decide between different (and sometimes radically opposed) options

- On the bright side of things, Cohesion Policy and ESI funds (and the added value that they bring) have started reappearing in recent Commission communications, most notably in the 'Harnessing Globalisation' reflection paper.

2.2. Are discussions related to the post-2020 EU budget focused on territorial investment?

The CPMR has long defended key principles anchored in the EU Budget, particularly those relating to **solidarity and subsidiarity**. These two principles are translated in operational terms in parts of the EU budget under the term 'programmes under shared management', currently covering the five European Structural and Investment Funds of the Cohesion Policy.

At present, 80% of the EU budget is spent under 'shared management', which means that the responsibility for distributing funding is shared between the EU, national governments and (for some Member States) regional authorities. 94% of the EU budget is spent on projects in the Member States[1], with a large portion of these being investment projects.

[1] See European Parliament dedicated factsheet

Will it continue to focus on infrastructure projects…

In February 2015, the CPMR adopted a declaration warning the Commission against the risks associated with a lack of a long term European vision to deliver EU public policies, and asked for proper resources to be made available to support investment[2]. The declaration was targeted at the newly created European Fund for Strategic Investment (EFSI) adopted earlier that same year.

Two years on, such warning signs have become a reality:

- there are no plans to renew Europe's strategy for growth and jobs (Europe 2020)
- the EFSI has been extended (and 'increased') until the end of 2020, with plans for further extension after 2020
- the Commission introduced crafty mechanisms in its September 2016 mid-term review package making it easier for other EU policies and programmes to support the EFSI

This new reality point to a European approach to support investment less based on grants but more on financial instruments:

- This seems true already regarding **Transport Policy funding**. The EU Budget mid-term review proposes to transfer an additional €155 million from the Connecting Europe Facility (CEF) to the EFSI, and proposes to raise the share of financial instruments for the Connecting Europe Facility from 10% to 20% via a new 'CEF Blending Facility', which would combine CEF grants with EFSI loans and guarantees[3]. As a reminder, €2.2 billion had already diverted from the original CEF Transport budget to finance the Juncker Plan. Of this amount, the EU Budget mid-term review only proposes to reallocate €400 million to the CEF Transport budget to be spent on grants.

- Infrastructure financing used to be the 'bread and butter' of **Cohesion Policy**. Today's Cohesion Policy still allocates €59 billion to transport and energy network infrastructure, but that is 21% less than what the policy supported for that theme in the 2007-2013 period. The post-2020 Cohesion Policy reform is likely to carry out with that trend. This was confirmed by Regional Policy Commissioner Corina Crețu who stated recently that Cohesion Policy will 'invest with priority research and innovation, digital and [will] slow down with infrastructure'[4].

… or will it focus more on EU-added value initiatives?

Some are asking for the EU budget to focus on 'European' added value initiatives and not finance projects which would otherwise have been financed by national governments. This view is shared by influential German Finance Minister Wolfgang Schäuble who would rather use EU monies to **help Member States implement the so-called country-specific recommendations and carry out structural reforms**. Others find little added value in Cohesion Policy financing projects in richer European regions.

[2] See February 2015 CPMR Declaration on Juncker Plan adopted in Nantes
[3] See Article 217 of the Omnibus Regulation
[4] See Euronews interview with Commissioner Crețu (14 February 2017)

What it means for peripheral and maritime regions

The reality is that deep divisions exist between Member States (and within the Commission) on whether (or how) the EU budget should be an investment budget in the future. There is hope reading through the Monti Report, which says the following about the EU Budget:

'The EU Budget serves to support Common EU policies and provide seed money for medium to long-term investments. It also has some redistributive functions between Member States.'

There is no denying that the European Commission has done its utmost to boost the use of financial instruments in the current Juncker Commission: via the newly created EFSI (and to the detriment of existing EU programmes) and through common EU policies.

But there is now **widespread criticism on the limits of such an approach**: from the CPMR's very own study on the territorial dimension of Cohesion Policy financial instruments to the EIB evaluation of the EFSI published last October, all pointing to a need for grants and in particular when it comes to supporting public goods.

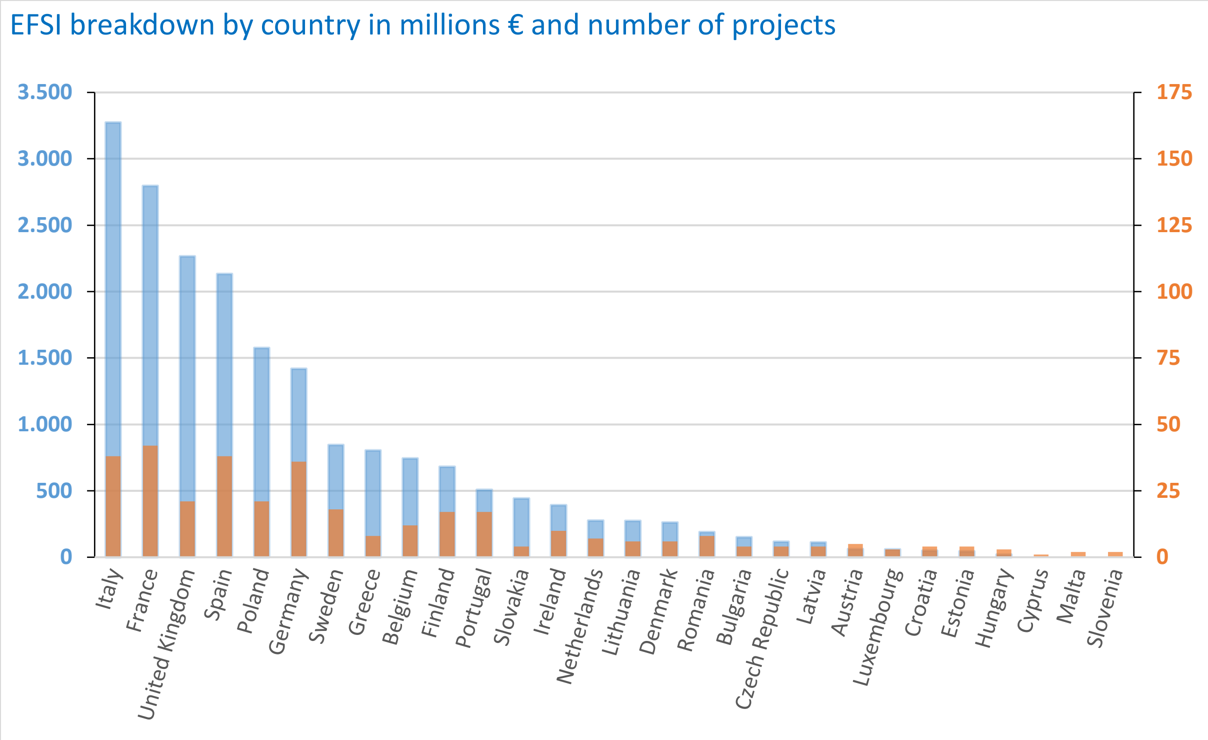
2.3 Will the future EFSI have a territorial dimension?

The European Fund for Strategic Investments (EFSI) shares with the ESI funds one of its primary objectives, promoting investments. Unlike the EFSI which remains an instrument, Cohesion Policy is a much broader long-term development strategy for all European member states and regions whilst the EFSI does not need any programmatic input.

In contrast to ESI funds, **the distribution of EFSI is geographically and sectorally highly imbalanced**. Some member states that have not yet seen any EFSI projects developed in their territories, in part due to low interest rates of commercial banks. The centralised governance of the EFSI contrasts with the programming approach of Cohesion Policy funds, which is based on a wider partnership.

The first impact of an instrument that was never designed with a territorial dimension in mind is that projects tend to be financed in wealthy and well developed Member States, both in terms of number of projects (shown on right hand axis below) and sheer financial volume (left hand axis)[5].

[5] The analysis of EFSI projects in this document considers exclusively data published until March 2017 on the EFSI Project list and considers all the projects: Signed, Approved and Pre-approved.



Comparing distribution of EFSI vs distribution of ESI funds

It is difficult to represent what the EFSI actually means at regional level as many of the projects financed involve more than one Member State, or because some of the EFSI financing is delivered through platforms (which are often set up at national level and therefore do not involve a specific project located in one region).

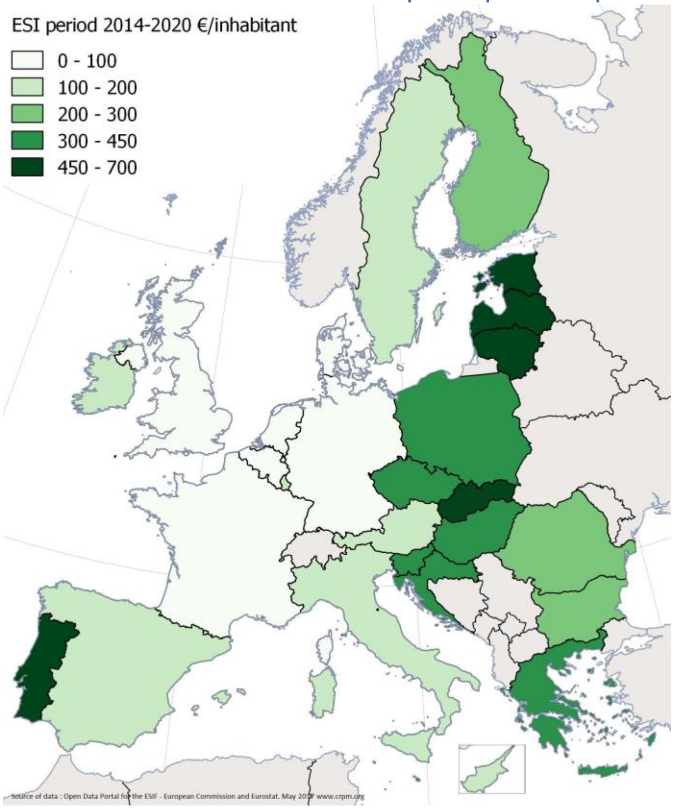
But it is possible to visualise and compare the distribution of EFSI with that of ESI funds per capita and per GDP, as the following maps show.

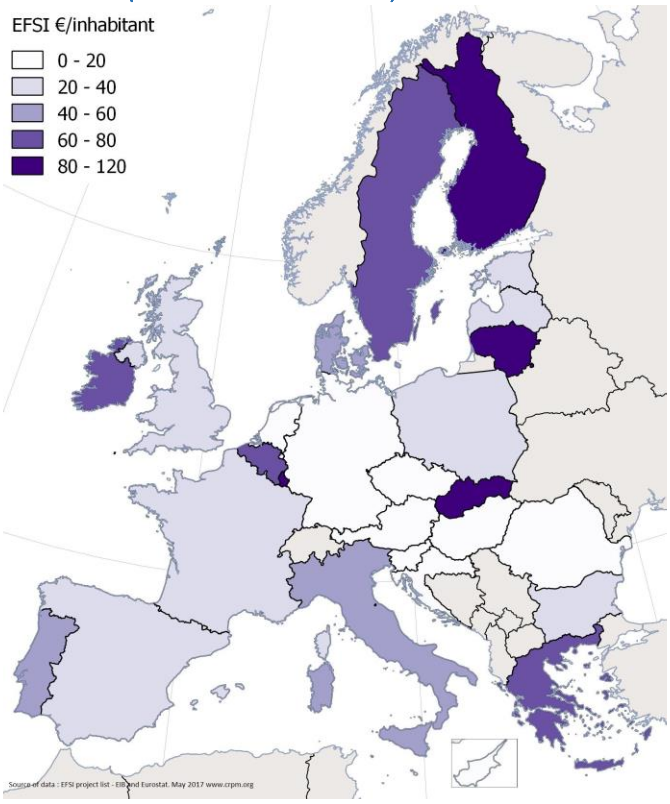
Clearly there is a dichotomy between traditional 'Cohesion' countries for which Cohesion Policy represents a substantial share of investment (per GDP and per capita), and other EU Member States.

The independent evaluation of the EFSI published by Ernst and Young in 2016 shows several potential reasons as to why this dichotomy exists, and therefore why 'Cohesion' countries failed to attract substantial EFSI financing so far:

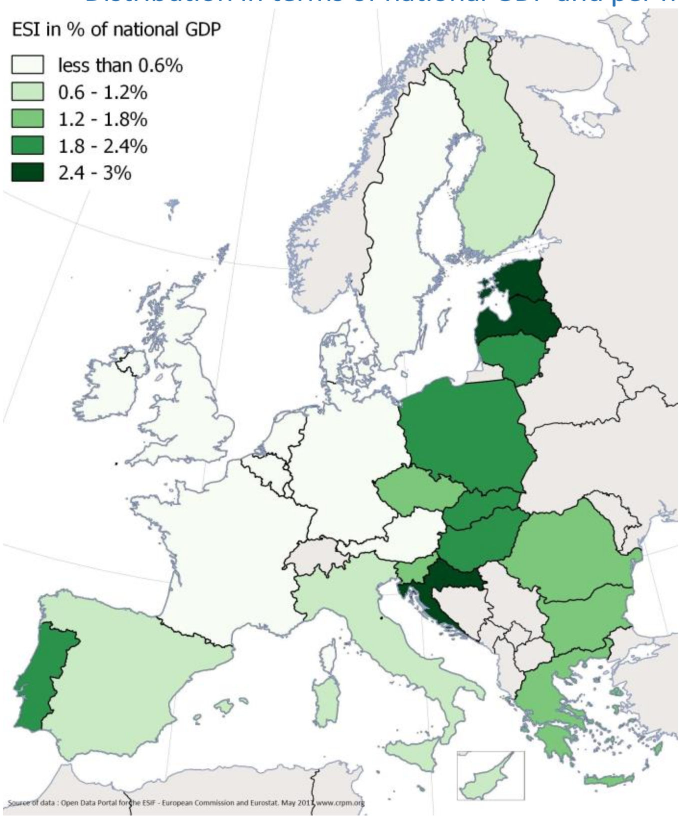
1. competition with ESI Funds;
2. lower capacity to develop large bankable projects;
3. lack of experience with public private partnerships (PPP);
4. insufficiently developed venture capital culture;
5. excessively small size of projects

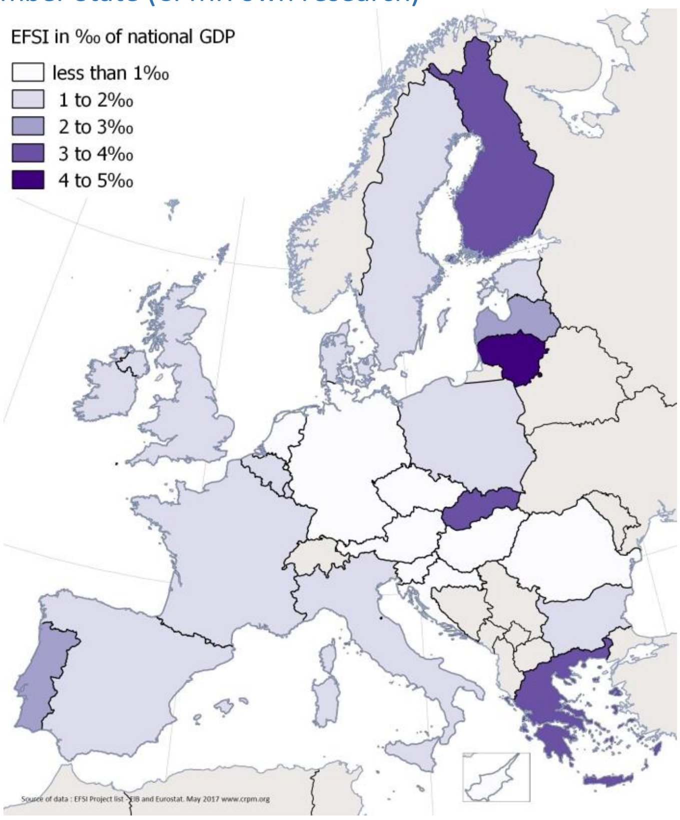
Distribution in terms of € per capita and per Member State (CPMR own research)[6]





Distribution in terms of national GDP and per Member State (CPMR own research)



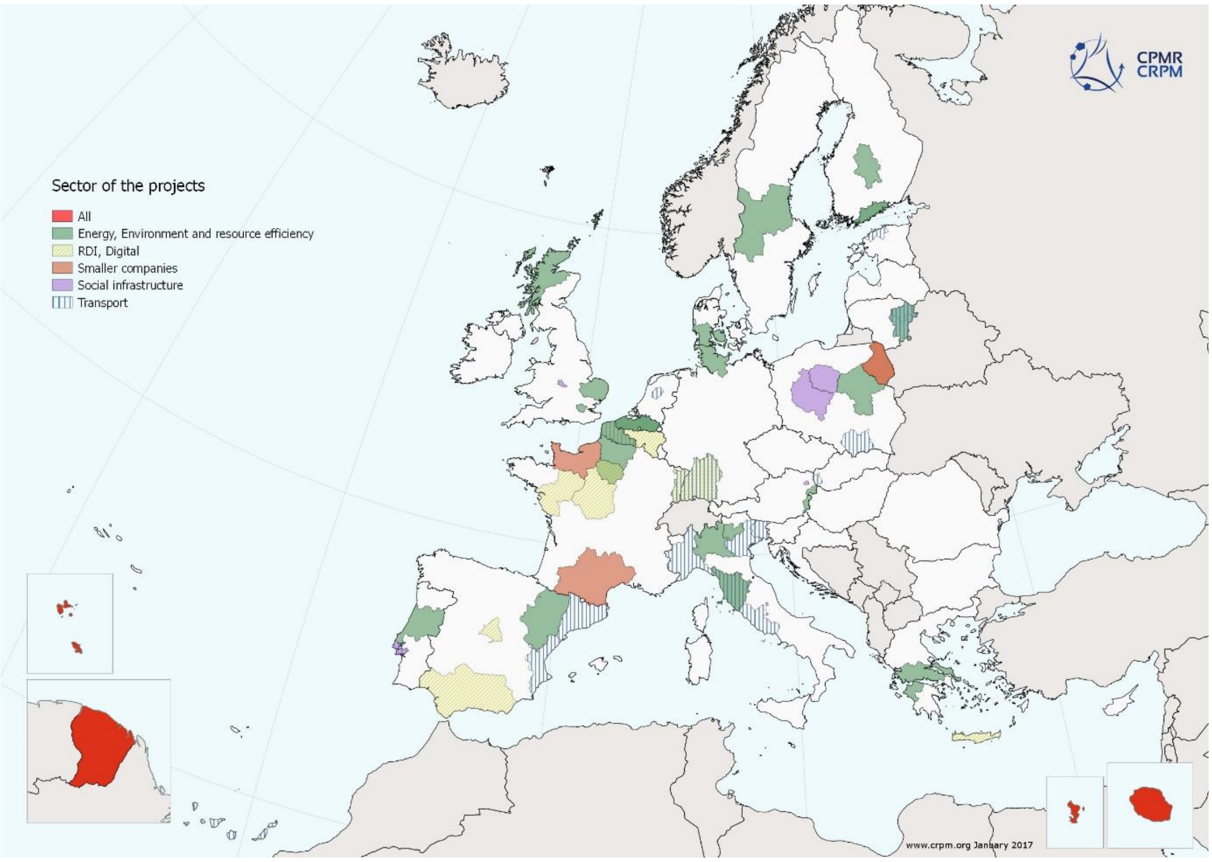


[6] Source of data: the EFSI Project list – EIB, the Open data portal for the ESIF – European Commission and Eurostat

Can the EFSI include an objective of territorial cohesion?

As mentioned above, some of the EFSI financing can be traced at NUTS II level. The map below represents EFSI supported projects which could be located in a particular region. The key learning point from this map is that there is no distribution logic (in terms of geography or type of sector supported) to the EFSI, which confirms the above analysis.

Representation of EFSI projects per sector at NUTS II level[7]



The EFSI's investment guidelines include a sectoral and geographical diversification that is not defined beforehand and should avoid geographical concentration with the aim of covering all the Member States at the end of the period. The project selection committee can prevent geographical concentration at European level when selecting projects, but it is unclear as to whether national investment platforms financed by the EFSI (in particular for SMEs) ensure a regionally balanced distribution.

However, there are instances of EFSI projects which have been designed to address the needs of specific territories:

- The French Overseas Territories (RUP) Risk Sharing project was put forward by the Agence Française de Développement as a risk-sharing framework guarantee scheme for investments in the French Outermost regions

[7] Source: EIB project database. All projects which could be located at NUTS II level are represented

- The Przewozy Regionalne rolling stock modernisation project in Poland aims to purchase and modernise existing rolling stock for a regional rail passenger operator and targets less developed regions in Poland

This means that there is nothing preventing a Member State submitting projects for EFSI financing which have a territorial dimension in the current framework. But given the 'raison d'être' of the EFSI, there are no obligations or incentives for these types of projects to be financed at the moment.

2.4 What will happen to the future of Cohesion?

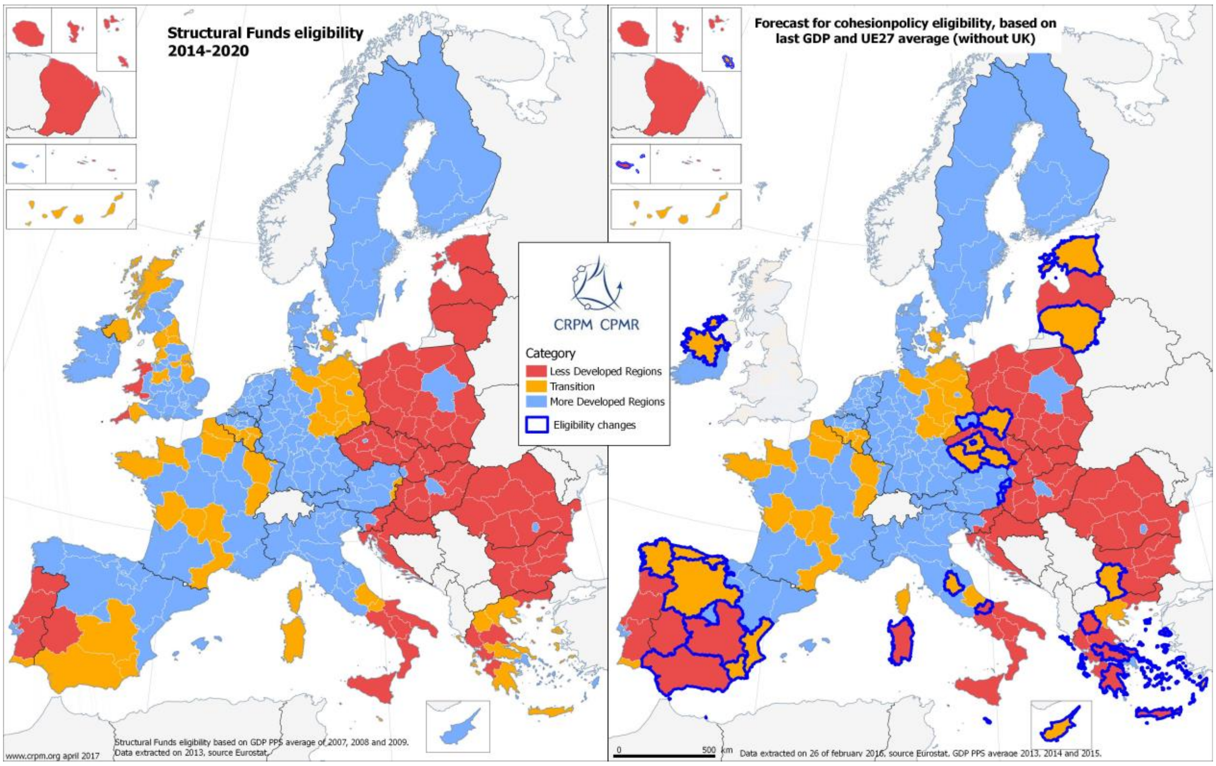
Cohesion Policy has fallen out of fashion at European level. The late start of the 2014 – 2020 programmes resulting in only 3.2% of the ESI funds having been spent as of May 2017 makes it an easy target for policy makers at European and national level alike.

But there is substantial evidence pointing to the relevance of EU action needing to enshrine the objectives of territorial, social and economic cohesion in today's world.

Several pointers in the Commission's latest two reflection papers with regards to the need for redistributive policies addressing the rising rise of disparities are encouraging. Spatially blind policies or instruments at European level – such as the EFSI in its current state – will do nothing but encourage the acceleration of regional disparities, leaving certain types of territories such as outermost regions and islands further behind.

The most recent set of regional GDP statistics confirm the rise of regional disparities as presented in the Social dimension reflection paper published by the European Commission last month. When used in the context of a theoretical Cohesion policy eligibility projection, the picture is most striking. The map on the right below shows what Cohesion policy eligibility would look like if it used the latest set of regional GDP statistics (average of 2013, 2014 and 2015), compared to the Cohesion Policy eligibility for 2014 – 2020 as agreed in February 2013[8].

[8] The UK leaving the European Union would result in lowering the European average. A scenario of the UK staying in the EU would have a small but not inconsiderable impact on Cohesion Policy eligibility projections (6 regions would be affected)



This map shows that most regions in Central and Eastern European Countries are showing sustained growth, whilst many Southern EU Member States are falling further behind (Spain and Greece in particular).

Many islands (all Greek islands, Sardegna to quote a few) would plunge down a category, and whilst the picture is more mixed with regards to outermost regions, the example of the region of Madeira theoretically dropping for more developed to less developed region status is worth mentioning.

3. Some considerations for future EU investment policies

The CPMR is in the process of developing its position paper on the future of Cohesion Policy, with comprehensive and practical proposals to modernize the policy for the post-2020 period. The CPMR already adopted a position paper on principles guiding Cohesion Policy reform in November 2016.

The Islands Commission of the CPMR has developed concrete proposals to boost the island dimension of Cohesion policy in the future, which are not listed here but can be accessed following this link.

This section presents ideas and considerations for the future of the EFSI and Cohesion Policy *(please note that the proposals below do not necessarily reflect the views of the CPMR as not all proposals have been adopted yet).*

Adding a 'cohesion' objective to the EFSI

- The EFSI is here to stay and changes will need to be made to ensure that it **does not exacerbate regional disparities** and leave some Member States and regions behind. Doing so would run against the 'convergence' model praised by the EC Social Dimension reflection paper.

- **The EFSI does have an impact on regional development.** Despite the EFSI having been conceived as a spatially blind instrument to boost investment volume in Europe, it is important to note that EFSI supported projects do have an impact on regional development and spatial planning. EFSI supported projects are linked to competences that are traditionally at local and/or regional level. This would require changes in the way regional authorities are involved in some way in terms of the project selection process.

- A potential solution to reconcile the EFSI with the territorial cohesion objective of the European Union would be to **add a 'development window' within the future EFSI**. The idea, proposed by the CEPS in a recent paper on the EFSI[9], would be to cover country-specific or region-specific operational and market risks to ensure that less developed regions can benefit from the EFSI. This would potentially help island and outermost regions access EFSI financing better.

Clarifying missions and objectives for EFSI vs ESI funds

- **Many of the areas of interventions and sectors supported by the EFSI and ESI intertwine**: SME support, energy and transport infrastructure projects being two of many examples.

- The solution praised by the Commission is to maximize potential for synergies between the two policies/instruments. **Evidence from CPMR regions is that this has failed**, as the EFSI and ESI funds were never designed to work together in the first place. Radical changes would need to be made to the functioning of the EFSI for such synergies to be made effectively in the future.

- A better solution would be to **establish clear boundaries** between what sectors and types of projects the EFSI should support and the areas of intervention of Cohesion Policy funds

- **The lack of a clear vision at European Commission level with regards to investment creates an uneven playing field between the EFSI and Cohesion Policy funds:**
    - EFSI financing (even when handled by national or regional promotional banks) is not subject to state aid, whereas regionally managed ESI funds are
    - ESI funds co-financing is taken into account in calculations of member States' public debt whilst EFSI contributions by member States are not
    - ESI funds are subject to complex (but comprehensive) auditing and performance requirements, whereas the EFSI is only subject to one criteria, which is 'additionality'

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[9] D. Rinaldi and J. Nunez Ferrer, The European Fund for Strategic Investments as a New Type of Budgetary Instrument, April 2017

    - Article 125 of the proposed "omnibus regulation" represents a potential one-way redirection of agreed upon Cohesion policy funding to other policies' instruments (either directly or indirectly managed), including EFSI

- **EFSI financed projects should indeed be additional investments** generating a clear European value added and contributing to job creation and economic growth, in line with the established performance-based character of Cohesion Policy. Many EFSI transport infrastructure projects (e.g the financing of motorways or airports) are not in line with EU policies supporting sustainable and environmental transport modes. The Commission must ensure the additionality, European added value and contribution to job creation and economic growth of EFSI financing, in line with the established performance-based character of Cohesion Policy

On financial instruments as a EU tool to stimulate investment

- Financial instruments play an ever more important role in Cohesion Policy. The CPMR believes that the best approach for the post-2020 period is a constructive one: rather than opposing grants and financial instruments, it is more appropriate to define where financial instruments add most value within a **future Cohesion Policy that should continue to rely primarily on grants in the future**.

- **Financial instruments should be targeted to respond to evidence of ''real economy''**. It is clear from recent CPMR analysis that financial instruments seem to be most effective when they support projects linked to research, development and innovation, SME support actions and the low carbon economy (Thematic Objectives 1, 3 and 4). Evidence suggests that Cohesion Policy financial instruments have been used successfully in a number of European regions to realise specific Cohesion Policy objectives but less so for social issues.

- There are significant issues preventing some regions to develop financial instruments, owing to their remoteness or small market size, including island regions and outermost regions.

On the future of Cohesion Policy as an investment policy for Europe

- Cohesion Policy is not a mere funding pot, but **a policy anchored in the EU Treaties at the service of European solidarity and investment**. The key for the future is to consolidate its original objectives whilst reinforcing its legitimacy to realise EU priorities across Europe.

- **Cohesion Policy is vital for EU objectives to be realised everywhere in Europe and delivers just as many benefits to the European Union as it does to individual regions.** A key example is the contribution of Cohesion Policy as a counter cyclical policy to help with the completion of the Single Market.

- **The territorial dimension of Cohesion Policy needs to be strengthened and improved,** and particular attention should be paid to the territories identified in the Treaty on the Functioning of the European Union (TFEU). **The specific challenges inherent to outermost regions should also be given particular attention.**

- A level playing field at EU level requires that all Europe’s citizens are treated equally irrespective of where they live. This is the spirit of Articles 174 and 349 of the Treaty for the Functioning of the European Union (TFEU) and must be reflected in a comprehensive way in Cohesion Policy as well.

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The Conference of Peripheral Maritime Regions (CPMR) brings together some 160 Regions from 25 States from the European Union and beyond.

Representing about 200 million people, the CPMR campaigns in favour of a more balanced development of the European territory.

It operates both as a think tank and as a lobby group for Regions. It focuses mainly on social, economic and territorial cohesion, maritime policies and accessibility.

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