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Accompanying the document

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on the 9th Cohesion Report

{COM(2024) 149 final}

Box 1.3 Cohesion cycles in the 2000s: a regional snapshot

In broad terms, four cohesion sub-periods can be distinguished in the two decades 2001–2022.

The 'convergence years' (2001–2008)

Between 2001 and 2008, nearly all regions experi- enced growth in GDP per head. Overall, growth was above average in both the less developed and the transition regions, with rates of over 5 % a year in many eastern Member States. This is in line with traditional economic growth theories, which predict that growth will tend to be higher the lower the in- itial level of GDP per head. Most of these regions are in less developed and moderately developed Member States, where for the most part growth was faster than the EU average. In Romania and Bulgar- ia, where growth was particularly high, catching-up was not uniform across the country but was driven by the capital city region. Regions in southern Italy, however, did not follow this pattern of catching up. They already experienced a decline in GDP per head in the 2000s even though their GDP per head was well below the EU average.

The 'low employment period' (2009–2013)

The global recession of 2009 led to GDP per head in the EU declining between 2009 and 2013, with many of the less developed and transition regions growing more slowly (or shrinking more quickly) than the EU average, so reversing the earlier ten- dency towards convergence. Around 60 % of the EU population lived in regions with a declining GDP per head. The regions hit hardest were mainly in the southern EU, though also in Romania, Ireland and Finland. In most Greek regions, the reduction in GDP per head averaged over 3 % a year. Notable excep- tions were most regions in Poland and some in Bul- garia and Romania.

The 'delayed recovery' (2014–2019)

The 2014–2019 period shows a clear recovery from the Great Recession. Almost all regions experienced growth in GDP per head, though at a lower rate than in the pre-recession period. High growth rates were restored in most eastern regions, so leading again to convergence. Growth in many north-western regions also remained below pre-crisis rates, Ireland being the main exception. In many regions in the hard-hit southern Member States, especially in Portugal and Spain, growth rates recovered, but in Greece and many regions in Italy growth remained low. Overall, 10 years after the 2009 financial crisis, over a quar- ter of the EU population still lived in regions where real GDP per head had not returned to pre-crisis levels. This includes the entire population of Greece and Cyprus, 80 % of the population of Italy and a third of that of Spain, but also 75 % of the popula- tion of Finland and over a third of that of Austria. In most of the eastern Member States, GDP per head had returned to pre-crisis levels in all or nearly all regions. However, in Romania and Croatia, 40 % and 25 % of the population, respectively, lived in regions where this was not the case.

The 'quick rebound' (2020–2022)

The 2020–2022 period is characterised by the dou- ble shock of the COVID-19 pandemic and Russia's war of aggression in Ukraine. Due to the nature of these shocks, they affected some regions more than others and – within them – some workers and sectors more than others (e.g. tourism, cultural ac- tivities, and industries affected by supply chain dis- ruptions and high energy prices). Again, southern Europe was on average more heavily affected. How- ever, as discussed below, the ensuing economic re- covery was faster and more broad-based than after the 2009 recession.

1. The short-term impact on economic cohesion of the COVID-19 pandemic

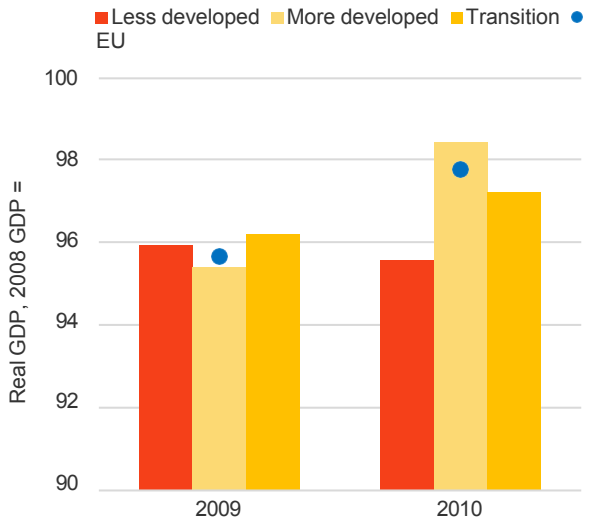
The COVID-19 outbreak had a severe impact on the EU economy and society, but GDP rebound- ed strongly in 2021 after a massive downturn in 2020. GDP fell in all but three EU regions. The unprecedented, bold and co-ordinated economic policy actions taken, including through Cohesion Policy, mitigated the economic and social impact of the pandemic. GDP at EU level already exceed-ed the pre-pandemic level by the last quarter of 2021, whereas it took seven years for it to exceed the pre-recession level after 2009. The regional data also indicate a more broad-based recovery in 2021, with less developed, transition and more developed regions all rebounding (Figure 1.12).

Southern Europe, however, was more heavily af- fected by the 2020 recession, with GDP falling by 10 %. Despite a stronger rebound, GDP in 2021 was still 5 % below the pre-COVID peak. North-western and, more especially, eastern regions have fared significantly better than southern ones in terms of GDP in the wake of the two crises. However, this has not prevented GDP in the EU as a whole falling behind that of the US and other advanced econo- mies (Figure 1.13).

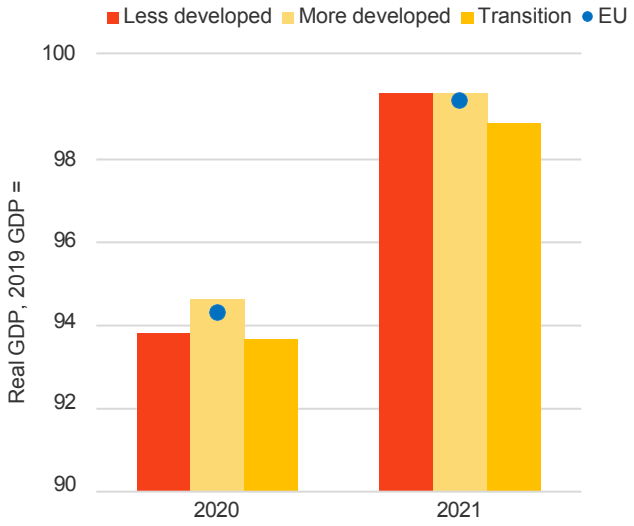
It is too early to be able to fully assess the longer- term impact of the COVID-19 outbreak on eco- nomic cohesion, but so far less developed regions have recovered more quickly than from the 2009 recession. The data available confirm the substan- tial size of the shock in 2020. Overall, the fall in GDP was much larger than during the recession of 2009. As already highlighted in the 8th Cohesion Report[31], some regions were hit more than others and – within them – some workers and sectors (such as tourism, cultural activities, and industries affected by supply chain disruptions) more than others. However, the ensuing economic recovery was more broad-based and faster than in 2010, when GDP continued to fall in around a quarter of EU regions (Figure 1.14). In 2021, this was the case in only four regions[32]. In 2010, the de-cline was largest in less developed and transition

Figure 1.12 Real GDP in NUTS 2 regions by level of development, 2009–2010 (2008=100) and 2020–2021 (2019=100)

a) Real GDP in NUTS 2 regions by level of development, 2009–2010 (2008=100)



b) Real GDP in NUTS 2 regions by level of development, 2020–2021 (2019=100)

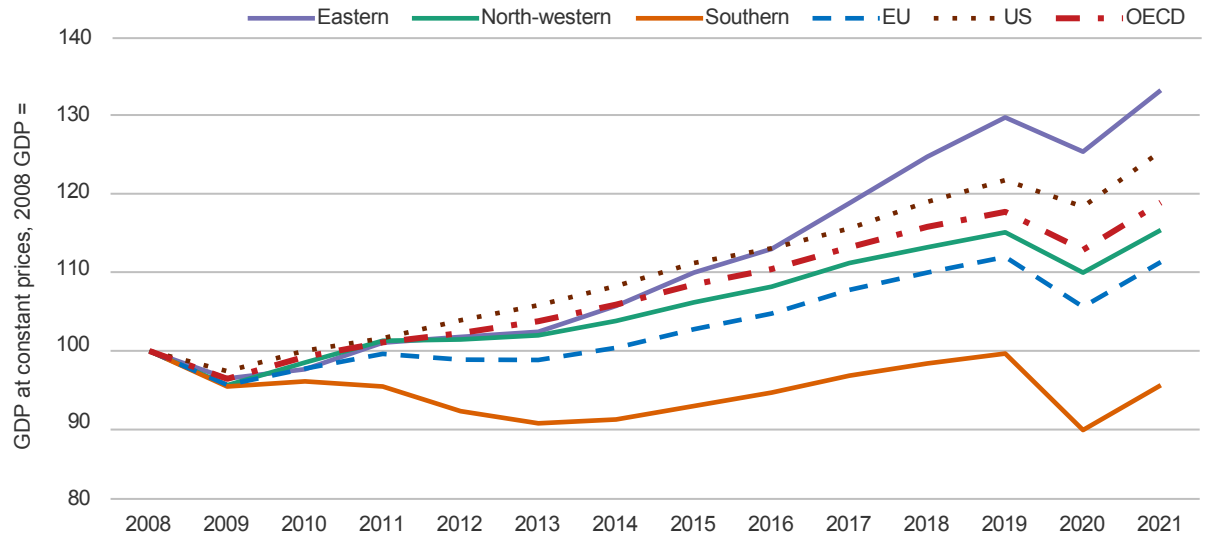


Source: Eurostat and Ardeco.

1 European Commission (2022).

2 There is even a slightly negative correlation between regional growth rates in 2020 and 2021, meaning that regions experiencing a deeper fall in GDP in 2020 were, on average, also the ones that experienced a stronger rebound in 2021 (Figure 1.16).

Figure 1.13 GDP at constant prices in the EU, US and OECD, 2008 GDP=100



Source: Ameco.

regions. In 2021, the regions where GDP fell by most in 2020 were, on average, the ones where the rebound was strongest[33].

Despite the broad-based recovery, there are again very large differences in growth rates across re- gions (last panel in Map 1.3). These may reflect differences in the structure of economies, with sectors more heavily affected by restrictions and supply chain disruptions taking longer to recover. Despite the strong rebound, the impact of the cri- sis on economic cohesion was severe and will need to be monitored in the future together with the ef- fect on overall growth in the EU.

The pandemic reduced employment in all regions, but this was largely offset by a strong rebound in 2021. The reduction in the number employed in more developed regions was similar (1–2 %) in both 2009 and 2020 (Figure 1.15 and Figure 1.16). However, eastern, southern and less developed re- gions still had 5 % fewer people in employment one year after the global recession. This was not the case in 2021 and 2022. Employment in the regions most affected began to recover sooner and it had already reached its pre-crisis peak in 2021 in nearly all of them. Thanks to job-retention schemes and other policy initiatives, the negative impact of the pandemic on employment was much smaller too than in 2009[34]. Indeed, the rapid eco- nomic recovery led to labour shortages reaching or even exceeding pre-pandemic levels in several Member States by the end of the year[35]. This is in stark contrast with the employment dynamics after the 2009 recession, where employment con- tinued to decline in eastern and southern Europe two years after the recession.

Both the 2009 recession and the 2020 pandem- ic hit household income in southern EU regions in particular (Figure 1.17). Unlike GDP and employ- ment, household income did not decline markedly in the two periods in the EU as whole, suggesting that automatic stabilisers and discretionary meas- ures played an important role in cushioning the im- pact[36]. However, there are large differences across the EU. Southern regions experienced a significant decline in household disposable income in the two years following the global recession (2010 and 2011). In the rest of the EU, by contrast, it was

3 This is suggested by the slightly negative correlation between regional growth rates in 2020 and 2021.

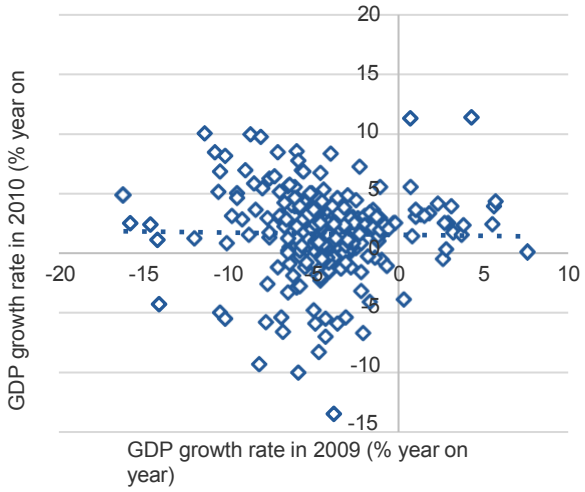
4 Giupponi et al. (2022).

5 European Commission (2022) and Chapter 2 of this report.

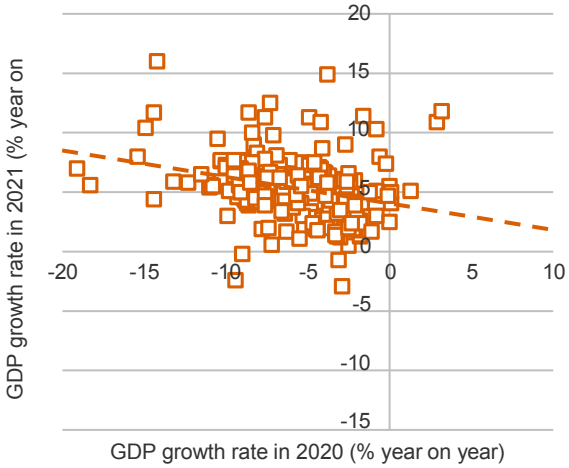
6 Bökemeier and Wolski (2022).

Figure 1.14 Real GDP growth rate in 2009 and 2010, 2020 and 2021, NUTS 2 level, year on year % change

a) Real GDP growth rate in 2009 and 2010



b) Real GDP growth rate in 2020 and 2021



Note: data for Polish regions are not yet available and not included.

Source: Eurostat.

above the pre-recession level. In 2020, the year of the COVID-19 outbreak, household income con- tinued to grow during the recession in eastern and north-western regions. Southern regions, on the other hand, were hit particularly hard, with a larger decline in household income than in 2009, reflect- ing the much larger impact on GDP (5 % in 2009 against 10 % in 2020). The post-pandemic recovery in household income in the southern EU, however, was stronger in 2021, whereas in 2010 income con- tinued to decline. Nevertheless, in 2022 it declined again, largely because of high inflation and a slower adjustment of wages than in the rest of the EU.

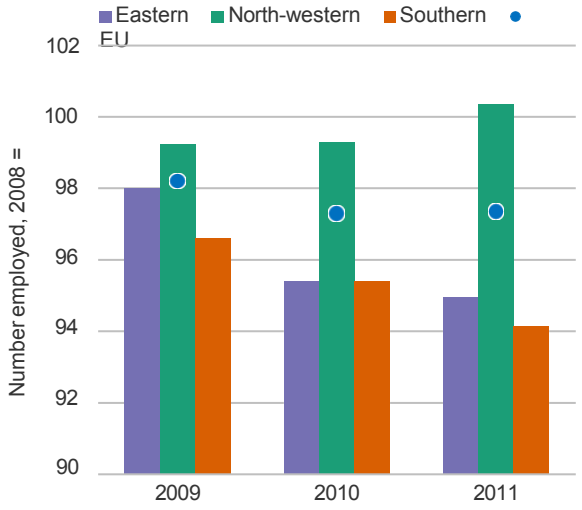
The post-pandemic rebound in investment was ex- ceptionally strong, especially in less developed and southern European regions. The fall in investment in 2020, though large (around 5 %), was less than half of that in 2009 (11 %) (Figure 1.18). This con- trasts with the contraction in GDP, which was larg- er in 2020. The difference was even larger in the year following the recession. Investment remained some 11 % below the pre-recession level in 2010, whereas it rebounded to nearly reach the pre-re- cession level in 2021. Significantly, less developed and transition regions performed, on average, bet- ter than more developed regions after the pandem- ic, while the opposite was the case after 2009. The

difference in the two periods partly reflects the ex- ceptional nature of the 2009 recession, when the decline in investment was deeper and more per- sistent than in previous ones (Figure 1.19) and the rebound much slower than in the US and other ad- vanced economies (Figure 1.20).

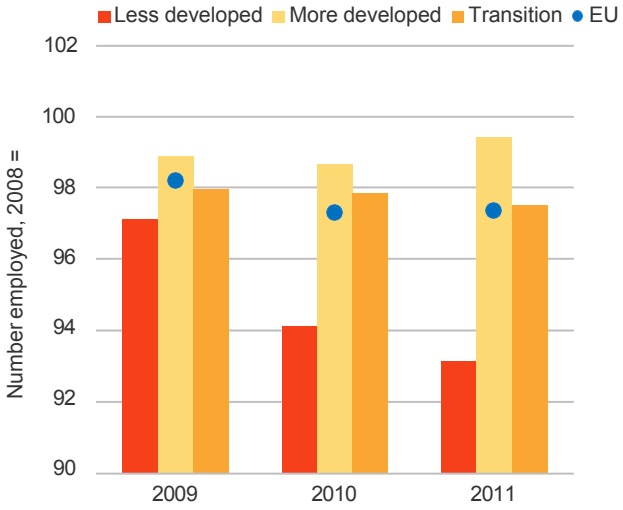
Both recessions had a substantial adverse im- pact on fiscal balances in the short term, but the COVID-19 pandemic was followed by a more modest increase in public debt over the subse- quent three years (Figure 1.21). During the period 2009–2011, public debt relative to GDP went up by 17 pp in the EU (15 pp in the eastern EU, 13 in the north-western EU, and 24 in the southern EU). By contrast, the increase between 2020 and 2022 was a much smaller 6 pp (6 pp in the eastern EU, 7 in the north-western EU, and 8 in the southern EU). In both periods the US and Japan adopted a more expansionary fiscal stance, resulting in larg- er and more protracted fiscal deficits (Figure 1.22), which ultimately led to an increase in public debt relative to GDP of 51 pp and 78 pp, respectively, between 2008 and 2022 (Figure 1.23). This con- trasts with a more restrained 20 pp increase in the EU over the same period, though in the south- ern EU the increase was 49 pp (as against 12 in the eastern EU and 18 in the north-western EU).

Figure 1.15 Number employed, by geographical area and level of development 2009, 2010 and 2011, 2008=100

a) Number employed by geographical area



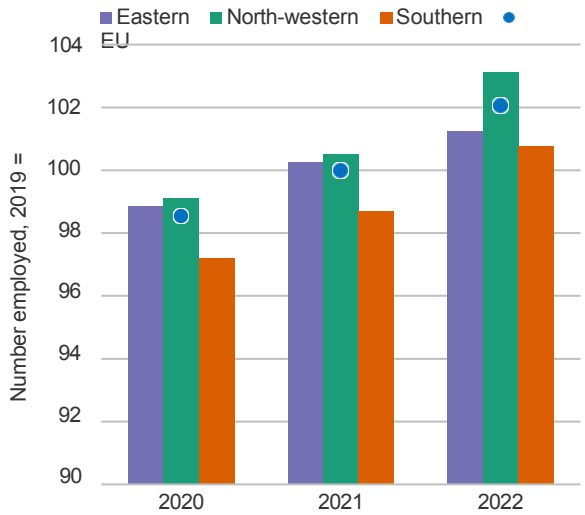
b) Number employed by level of development



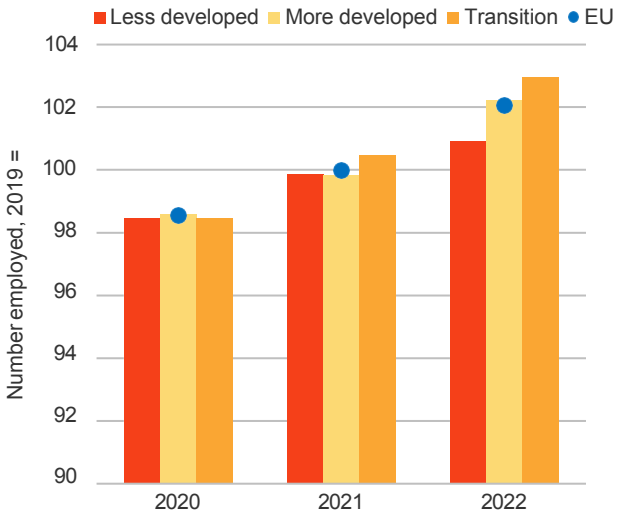
Source: Eurostat and Ardeco.

Figure 1.16 Number employed, by geographical area and level of development, 2020, 2021 and 2022, 2019=100

a) Number employed by geographical area



b) Number employed by level of development



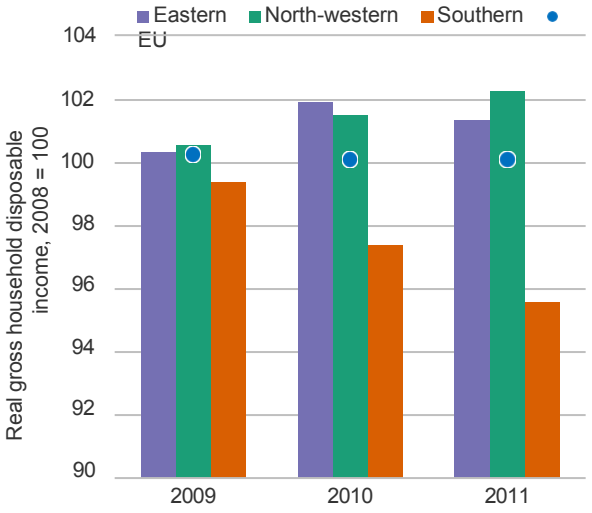
Source: Eurostat and Ardeco.

Although the increase in the southern EU was much the same as in the US, it was not associat- ed with the same economic performance. Follow- ing the 2010 recovery, several EU Member States front-loaded fiscal consolidation measures in an at- tempt to curtail budget deficits. This yielded mixed results, as GDP often failed to rebound as fore- cast[37]. However, in the wake of the 2020 COV- ID-19-induced recession, the EU introduced the NextGenerationEU scheme, making available financial aid of some EUR 750 billion to Member States severe- ly affected by the crisis to support cash-strapped

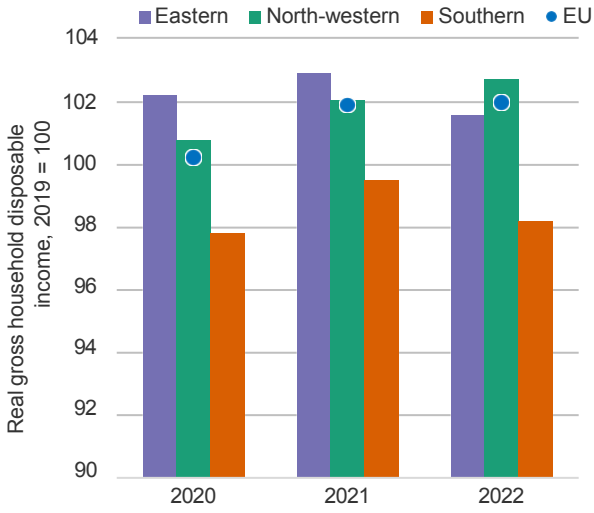
7 Blanchard and Leigh (2013).

Figure 1.17 Real gross household disposable income by geographical area, 2009–2011 (2008=100) and 2020–2022 (2019=100)

a) Real gross household disposable income by geographical area, 2009–2011 (2008=100)



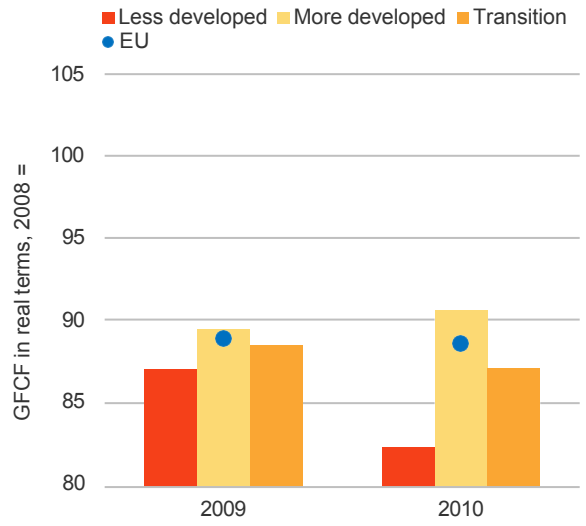
b) Real gross household disposable income by geographical area, 2020–2022 (2019=100)



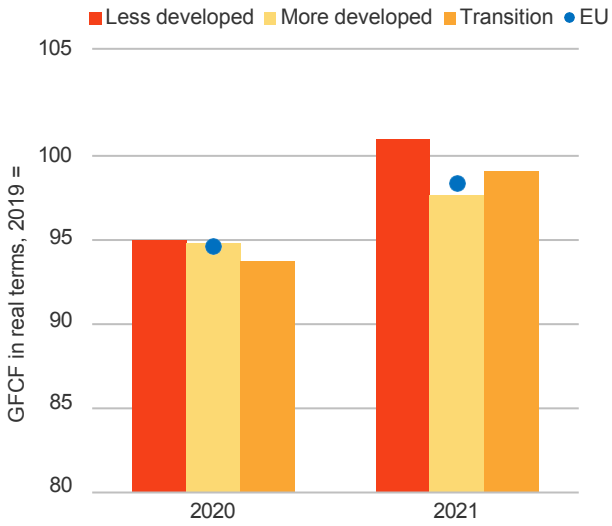
Note: Income is deflated by the harmonised consumer price index; data for MT and BG are missing.
Source: Ameco.

Figure 1.18 Gross fixed capital formation, in real terms, by level of development, 2009–2010 (2008=100) and 2020–2021 (2019=100)

a) Gross fixed capital formation, in real terms, by level of development, 2009–2010 (2008=100)



b) Gross fixed capital formation, in real terms, by level of development, 2020–2021 (2019=100)

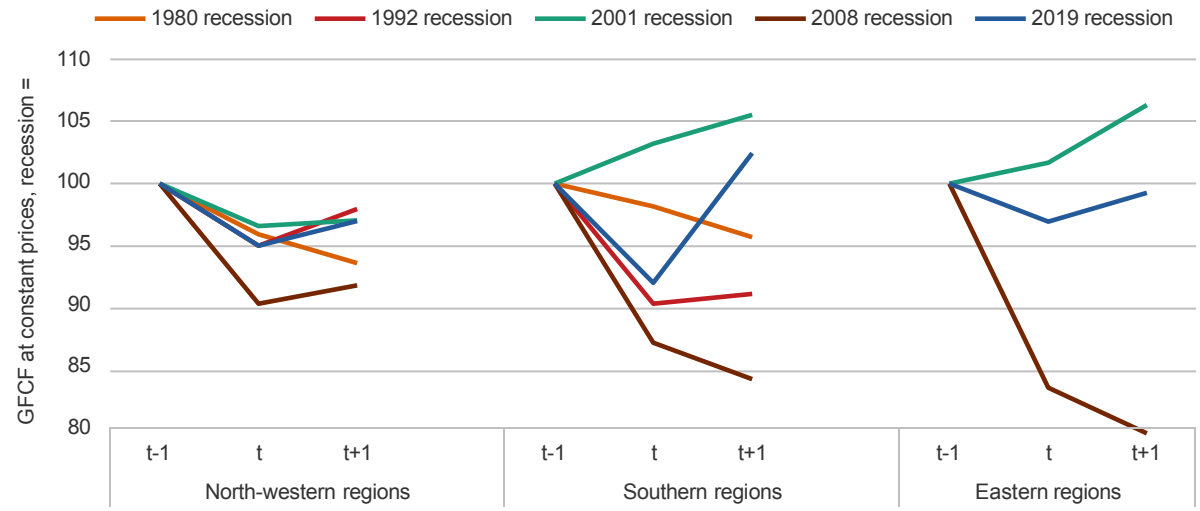


Source: Eurostat, Ameco and Ardeco.

national budgets and to stimulate positive expec- tations for the economy. This collective response appears, so far, to have not only spurred a stronger recovery and mitigated any widening of disparities than after previous recessions but also restrained the increase in public debt.

In sum, the immediate impact of the two reces- sions was deep and broadly similar as regards the macro-economic effects. But the recovery of GDP, employment, household income and investment was stronger and more regionally balanced after the pandemic. The main proximate reason for this

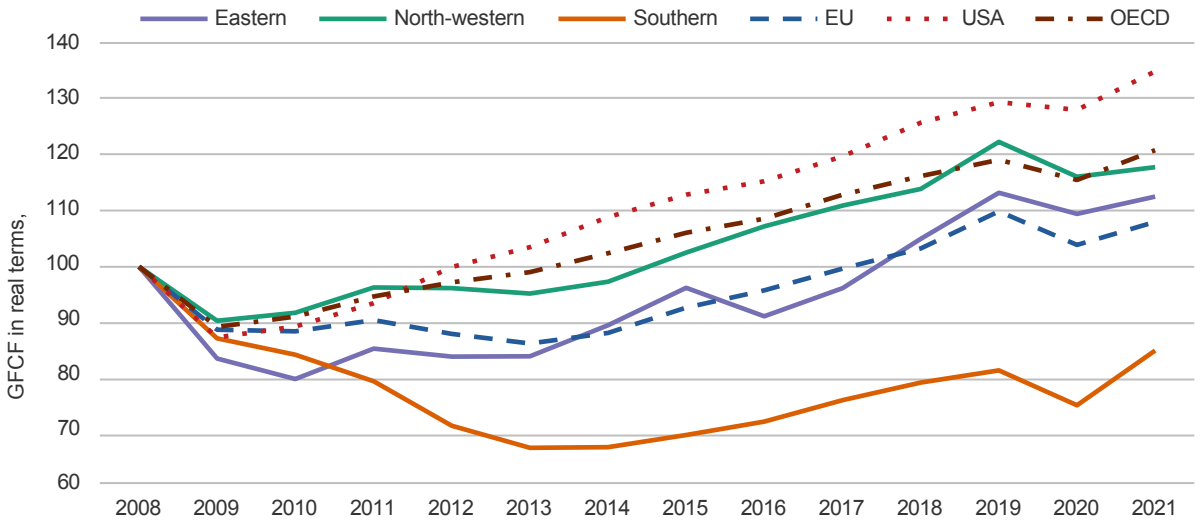
Figure 1.19 Gross fixed capital formation in the EU after the five major recessions since 1980, in real terms, by geographical area, year of recession=100



Source: Eurostat, Ameco and Ardeco.

is that the performance of eastern, and more es- pecially southern, regions was more similar to that of north-western ones. This, in turn, is partly due to the different nature of the two shocks. The 2009 recession stemmed from a global financial crisis, with a severe impact on the banking sector ham- pering the credit channel in the midst of a major de-leveraging process from both the private and the public sector. This, in turn, exerted a prolonged drag on real economic activity, investment, prices and household income. This was the case through- out the EU, especially as compared with the more robust recovery in the US, and especially in EU re- gions most exposed to the twin de-leveraging pro- cess. By contrast, the 2020 recession was triggered by a different kind of external shock, the spread of a pandemic. The restrictions and disruptions to supply chains that ensued proved more transitory than the 2009 financial crisis. In line with the dif- ferent nature of the two shocks, the price dynamics

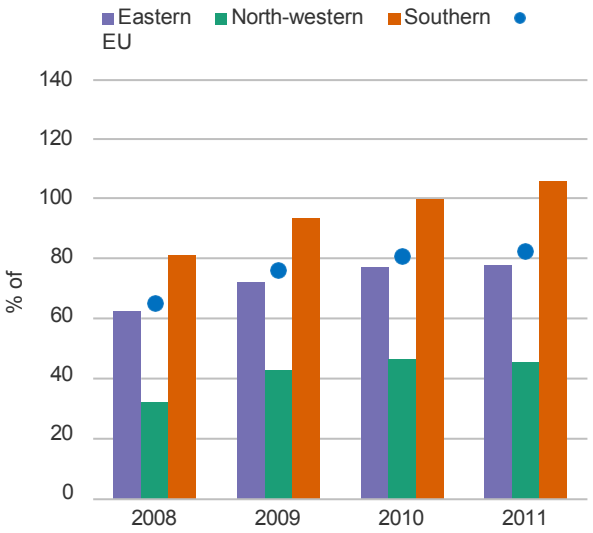
Figure 1.20 Gross fixed capital formation, in real terms, by geographical area, 2008=100



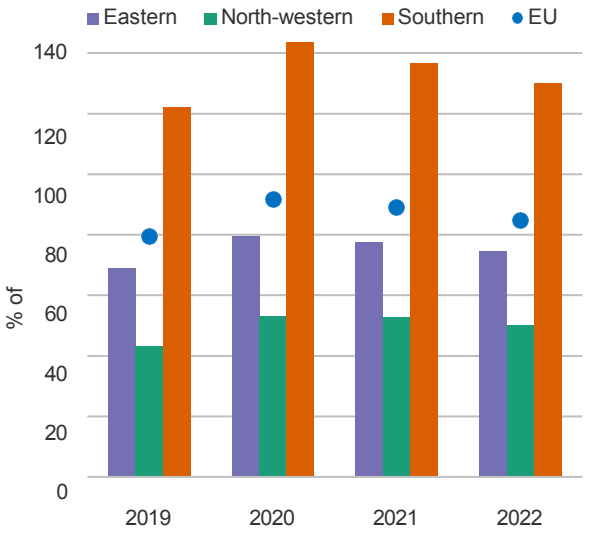
Source: Eurostat, Ameco and Ardeco.

Figure 1.21 General Government consolidated gross debt, by geographical area, 2008–2011 and 2019–2022

a) General Government consolidated gross debt, by geographical area, 2008–2011



b) General Government consolidated gross debt, by geographical area, 2019–2022



Source: Ameco.

during the recovery phase were also different. In addition, novel and swift policy action – the rapid deployment of Cohesion Policy, new instruments such as SURE (Support to Mitigate Unemployment Risks in an Emergency) and the NextGenerationEU recovery fund – helped to prevent a protracted re- duction in investment. Together, they made available up to EUR 750 billion in financial support to Member States severely affected by the 2020 recession.

The longer-term prospects for economic cohesion, however, remain hard to predict. The addition- al shocks that have occurred since the COVID-19 pandemic pose potentially longer-term challenges to the EU growth model. It is too early to fully as- sess the regional dimension of these shocks, partly because of a lack of regional statistics in many of the areas affected. Several regions, economic sec- tors and categories of workers have suffered sig- nificantly and the current situation remains fragile and volatile, with a risky and uncertain economic outlook. But there are also opportunities. For in- stance, regional economic disparities between the EU-27 and current candidate countries point to a large potential for upward convergence in the future; see Maps 1.5. and 1.6 comparing the 2004 enlargement with the current relative position of candidate countries vis-à-vis EU regions.

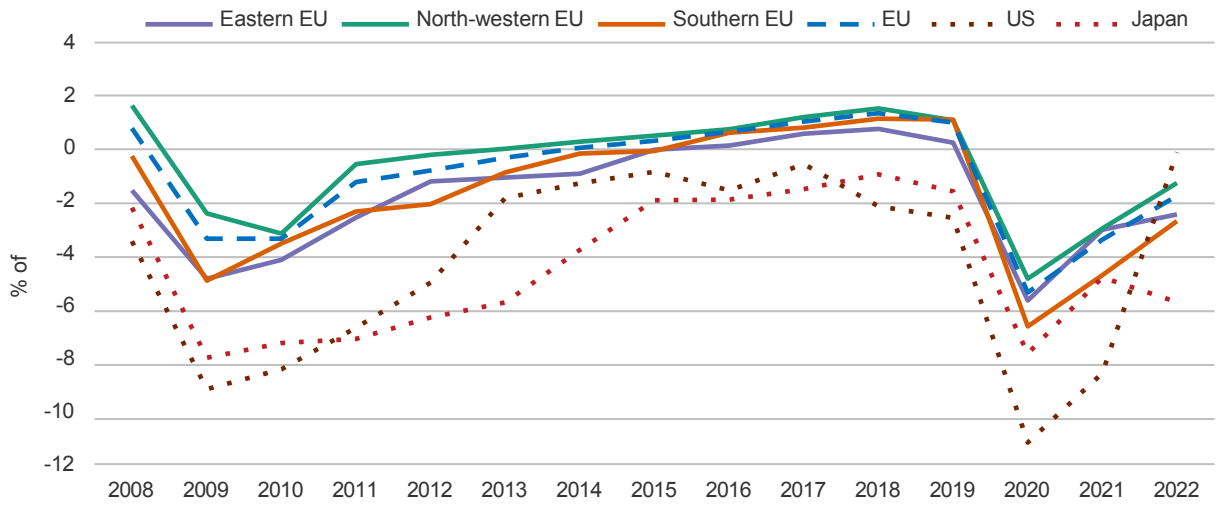
2. The geography of growth, stagnation and discontent: high-growth paths and development traps in Europe

Over the past two decades many regions have experienced a prolonged period of economic stag- nation leading to growing popular discontent. The regions concerned seem to have fallen into a de- velopment trap, a state of sub-par performance of GDP, productivity and employment[38]. Such a state is empirically correlated with an increase in polit- ical discontent and a decline in support for demo- cratic values and the EU[39]. Regional development traps are not just an economic concern. The sub- par economic performance and lack of job oppor- tunities have social costs and give rise to political resentment towards what is increasingly regarded as a system that leaves many people behind.

8 European Commission (2022).

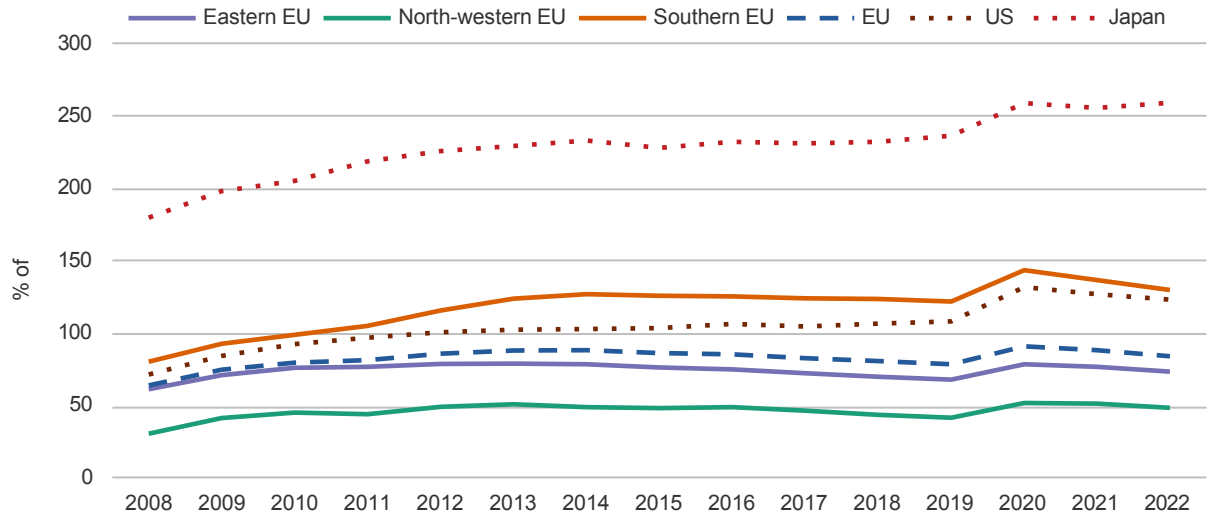
9 Dijkstra et al. (2020, 2023b).

Figure 1.22 General Government net lending (+) or net borrowing (-), excluding interest payments, 2008–2022



Source: Ameco.

Figure 1.23 General Government consolidated gross debt

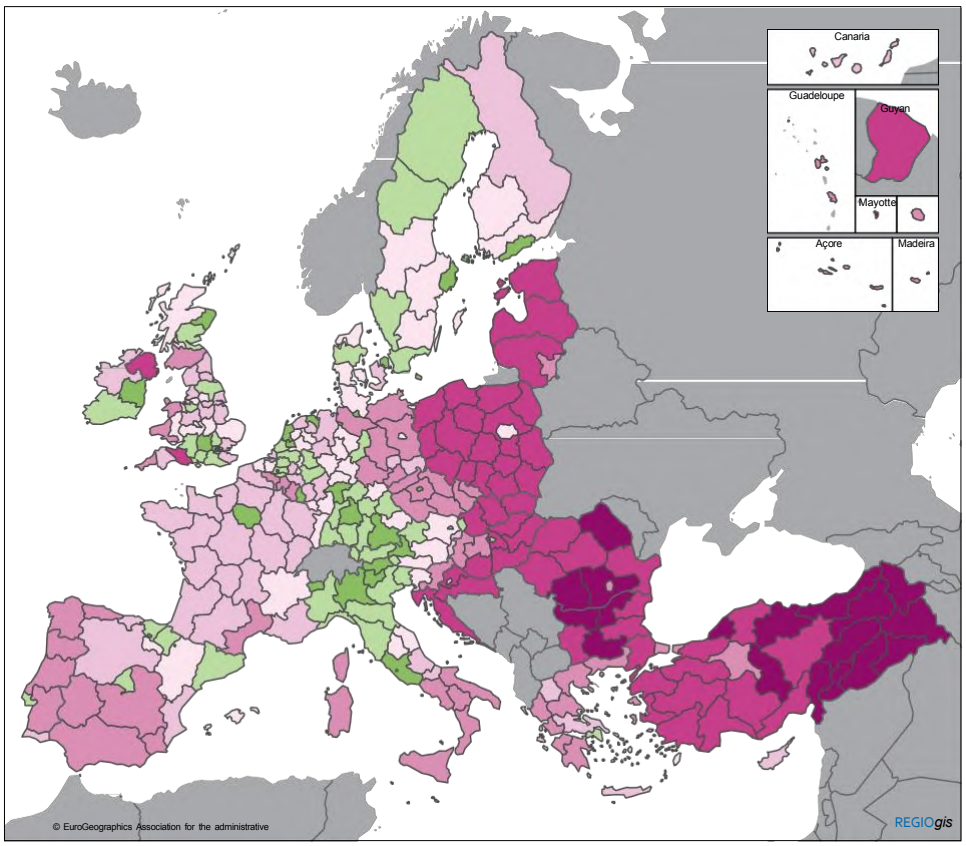


Source: Ameco.

On the positive side, though many regions have been persistently trapped, several have succeed- ed in moving from a low-growth to a high-growth development path. This has generally coincided with a shift of specialisation towards more com- plex economic activities linked to local strengths and characteristics, often through integrating into global value chains (see Chapter 5). This section builds on the concept of a development trap pre- sented in the 8th Cohesion Report[40] and extends it in three ways. First, it develops a high-growth path index to identify the best regional performers. Second, it presents a novel approach to determin- ing the characteristics of regions stuck in a devel- opment trap and the ways of escaping from it[41]. Third, it sets out evidence linking the risk, intensity,

10 European Commission (2022).

11 Balland et al. (2019).



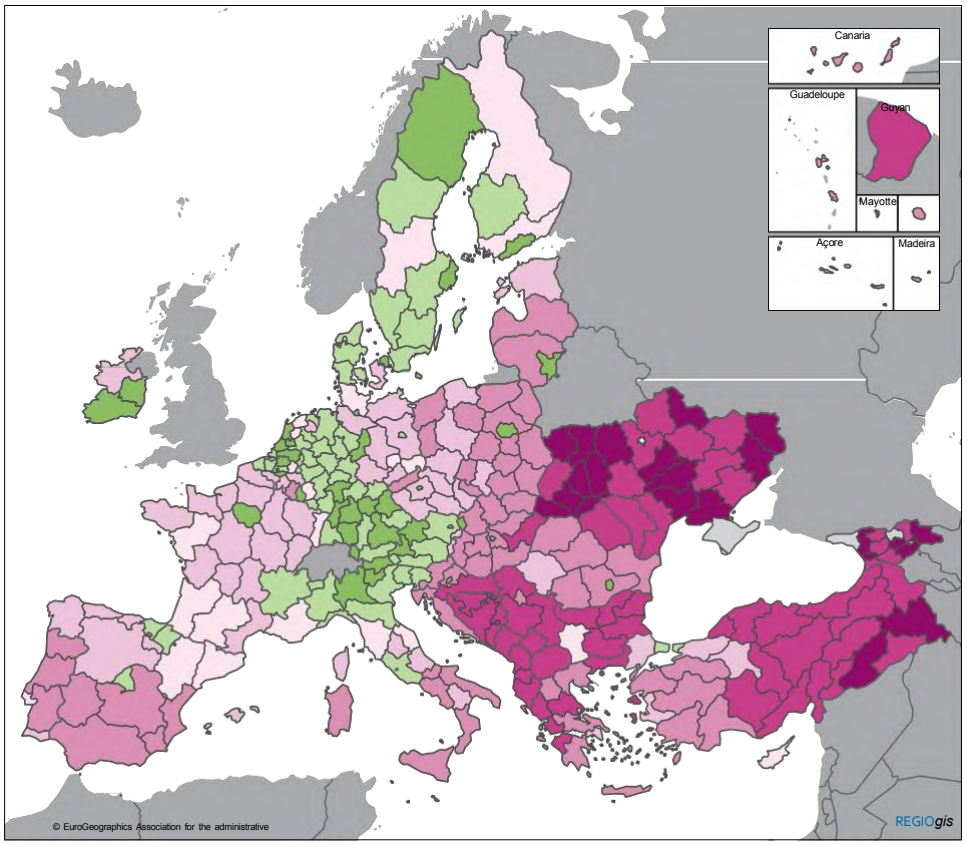
Map 1.5 GDP per head in PPS in the EU-15 and candidate countries in 2004, % EU-15

Index, EU-15 = 100

- <= 25
- 25 – 50
- 50 – 75
- 75 – 90
- 90 – 100
- 100 – 125
- > 125

Source: Eurostat [nama_10r_2gdp, nama_10r_3popgdp], JRC

0 500 km



Map 1.6 GDP per head in PPS in the EU-27 and candidate countries in 2021, % EU-27

Index, EU-27 = 100

- <= 25
- 25 – 50
- 50 – 75
- 75 – 90
- 90 – 100
- 100 – 125
- > 125
- no data

Source: Eurostat, World Bank, national statistical institutes and DG REGIO

0 500 km

Box 1.4 Regional cohesion and Russia's war of aggression against Ukraine

Russia's war of aggression against Ukraine sent shockwaves throughout the EU. Some of the EU's poorer regions are likely to be more affected. This box discusses three reasons: the concentration in richer regions of the economic contribution of work- ing-age refugees; the vulnerability of poorer, rural areas to the sharp increase in energy and food pric- es; and the rise in geopolitical uncertainty, which has pushed up military spending particularly in poorer countries in eastern Europe.

The integration of refugees will probably raise av- erage growth in the EU, but not regional cohesion. Immigration tends to benefit host regions that suc- cessfully integrate refugees in local labour markets. Under the Temporary Protections Directive, Ukraini- an refugees can choose in which EU country to work, and most choose countries with an existing Ukraini- an diaspora and dynamic labour markets: Germany, Poland and Czechia. Working-age Ukrainians added on average 2.5 % to the labour force aged 20–65 in eastern Europe, 1 % in western and northern Europe, and 0.5 % in southern Europe[1]. Taking into account that language barriers inhibit their integration into labour markets – surveys point to employment rates of about one third – Ukrainian refugees are likely to contribute on average about 0.5 % to the GDP of eastern countries in the short term, and somewhat less in the rest of the EU. The longer these refugees stay, and the better the policies facilitating their in- tegration, the more likely their labour market partic- ipation is to rise. For example, as of August 2022, half of the working-age refugees had found em- ployment in Poland, which currently hosts close to a million Ukrainian refugees, who can benefit from a particularly large existing diaspora and relatively low language barriers.

Even though eastern countries' living standards tend to lie below the EU average, it is mostly the richer regions that are likely to benefit from their integra- tion into local labour markets. Refugees tend to set- tle in the dynamic regions with better employment prospects within those countries, such as Prague or Warsaw, whose GDP per capita already substantially exceeds the EU average.

The energy and food price shocks triggered by the war have lowered wealth throughout the EU, but poorer, rural areas were more affected. Prices for energy and food have declined from their peaks, but have had a significant impact on real disposable in- come. Since rural regions within the EU tend to be poorer than urban ones, households living in rural areas tend to spend relatively more on transport, and those that are poorer spend relatively more on energy and food. For example, households in rural areas in Bulgaria spend 35 % of their consumption on food, those in Bulgarian cities 23 %.

Finally, eastern countries bordering Russia, Ukraine or Belarus have raised their military spending more than other Member States since Russia's invasion of Crimea. With a GDP per head about half that of countries in the north and west, these countries raised their military spending by 0.7 % of GDP be- tween 2014 and 2022, twice as much as those in the west and north. This increase risks crowding out spending that could have been used to advance regional cohesion. Being more intertwined with the Russian economy before the war, these economies are more affected by the sanctions imposed on Russia. The war has been a major disruption to the implementation of cohesion programmes, notably Interreg programmes. External border regions, in Finland and the Baltic States, as well as some Polish border regions, have lost their cross-border co-oper- ation partners. Previous exchanges and cross-border flows have been replaced by closed borders and no co-operation. The Commission introduced changes allowing for the integration of these regions into other co-operation programmes, but the negative border effect is stronger than ever and they must be further supported to look for other co-operation and development opportunities.

1 All figures referenced in this box stem from Eurostat as well as various reports from the International Organization for Migration (https://dtm.iom.int/reports?search=ukraine).

and length of regional development traps to the rise of political discontent in the EU[42].

2.1 Regions on high-growth trajectories

The picture of convergence shown by the indicators above gives an overall view of macro-regional de- velopments, but it does not lend itself to identify- ing specific features and success stories at a more detailed level. To shed light on these, the meth- odology used to determine the regions stuck in a development trap also enables us to calculate an economic development index (EDI) for regions that have persistently outperformed others[43]. A large number of EU regions, defined here at the NUTS 3 level, have been on a high-growth trajectory (EDI above 0.5 in Map 1.7) over the past two decades. As expected, these are disproportionally located in eastern Europe, reflecting higher growth during the catching-up phase noted above (beta conver- gence). However, regional success stories are not limited to this broad area of the EU. Indeed, most EU Member States have at least one NUTS 3 region on a high-growth path over the period 2001–2021 (EDI higher than 0.5). This is true not only of most capital city regions, but also of some regions in centre-north Portugal, north-western Spain, coastal France and, to a lesser extent, Italy and Greece, as well as some more developed regions in Germany, Belgium, the Netherlands and Sweden. Overall, this confirms that economic performance has varied substantially across the EU and within countries[44].

2.2 Regions in a development trap

A novel approach to determining the character- istics of regions in a development trap has shed light on possible links with a new typology of eco- nomic complexity traps[45]. In addition to the stand- ard characteristics of regions in a development trap[46], self-reinforcing dynamics could limit the capacity of regions to innovate and develop new growth paths[47]. Regions might become trapped in low-complexity activities because of a lack of capability to develop highly complex products[48]. An analysis of the structural evolution of develop- ment traps over a long period of time has provided systematic empirical evidence on how many re- gions in the EU fail to overcome a ‘low-complexity’ structure, on the extent to which these are high- or low-income regions, and the kinds of traps they have fallen into. The definition of ‘evolutionary traps’ centres around the structural inability of re- gions to develop new activities, because their ca- pabilities prevent them from moving into new and more complex activities that could increase their prosperity. Based on this, it identifies regions that once performed well but have become trapped, as well as those that have managed to escape from being so and how.

The characteristics of regions in a development trap are highly varied in terms of development levels, but the limited capacity of a region to edu- cate people and retain them is a common feature across all levels of development. The reasons for falling into a development trap differ between re- gions depending on the initial level of development,

12 Dijkstra et al. (2023b).

13 Using the methodology to measure the likelihood of being in a development trap developed by Iammarino et al. (2020), high-growth paths are identified when regions have outperformed their peers in terms of GDP, productivity and employment growth (when the likelihood of so doing is greater than 50 %). The conventional development trap indicator denotes when a region's growth of GDP per head, productivity and employment is lower than that of the EU, its country, or the region itself over the previous five years. A region scores 1 for each time its growth is higher than the three benchmarks. The score between 0 and 9 is then rescaled to 0 and 1. To identify regions on high-growth paths, the inverse of the average yearly development trap score of each region is taken over the period 2001–2021. This ensures consis- tency and symmetry with the analysis based on the development trap indicator, while pointing to regions outperforming their peers.

14 In eastern Member States, economic performance has been strong in capital regions but also across the majority of other regions. In south- ern Europe, regions outperforming their peers are mostly located in Spain and Portugal – cases of catching up again because they were relatively poor regions – but there are positive examples also in Greece and Italy. Coastal regions in France have also generally performed much better than central ones (except for the capital city region). In the rest of Europe, there is a broadly balanced presence of regions in terms of their economic performance.

15 Balland et al. (2019).

16 Iammarino et al. (2022).

17 Arthur (1994).

18 Pinheiro et al. (2022)