DIFFICULTIES REGARDING THE ABSORBTION OF STRUCTURAL AND COHESION FUNDS IN ROMANIA

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Abstract:
Cohesion and structural funds absorption in the EU is one of the most debated issues at hand in terms of macroeconomic management and financial development of the MS. This direction results in the development of funds and all the related structural and cohesion policies as to assure structural adjustment and harmonize operations by homogenizing and sustaining the economic standards of MS. Central national budgets have to mold and be structured in order to ensure the co-financing in the projects appliance and also the fine implementation of growth through fund allotment and absorption.

Keywords: structural funds, cohesion policy, absorption rate, operational programmes.
Jel Classification: E22, G31, H12, H19, H43.

Introduction

In terms of data made available by the European Commission out of the total funds given only 10% are focused in the cohesion part of this aspect. This is mainly due to the fact that the focus is on mutual aid and solidarity with a close eye on how the economy can be better molded and could function in a leaner way. In the current debate on the European crisis, insufficient attention is being paid to the possible use of the immense resources of the Structural and Cohesion Funds for crisis management and resolution.

1. The cohesion policy

European Union Structural Funds may represent the possibility of stimulating the economy in a sustained recovery. Banks looking for investment opportunities could benefit on the one hand of the fact that they may take advantage of a recovery in investment and growth, which eventually will increase the demand for loans in all sectors and on the other hand, at the microeconomic level, banks can contribute directly to the financing of projects eligible for EU funds. In terms of pre-financing and co-financing in the absorption of EU funds, the focus of this paper is on the role of banks and how their power influences a better absorption of these funds. This is mainly valid also for the functions in the administrative segment and project monitoring and selection. There are three objectives under the 2007-2013 cohesion policy: Convergence, Regional Competitiveness and Employment as well as Territorial Cooperation. For the 2007 - 2013 period the European Union made available to the new MSs EUR 178 billion (approximately 19% aggregate 2010 GDP, see Table 1) compacted within three different instruments:

- The European Regional Development Fund (ERDF), which finances:

(i) direct aid to investments in companies (in particular SMEs) to create sustainable jobs;
(ii) infrastructure linked notably to research and innovation, telecommunications, environment, energy and transport;
(iii) financial instruments (capital risk funds, local development funds, etc.) to support regional and local development and to foster cooperation between towns and regions;
(iv) technical assistance measures.

- The European Social Fund (ESF) which seeks to improve employment by supporting actions in the following areas:

(i) adapting workers and enterprises through lifelong learning schemes and innovative working organisations;
(ii) access to employment for job seekers, the unemployed, women and migrants;
(iii) social integration of disadvantaged people and combating discrimination in the job market and
(iv) strengthening human capital by reforming education systems.

- The Cohesion Fund (CF) is aimed at Member States whose Gross National Income per inhabitant is less than 90% of the Community average (this includes all ten new member states) and finances activities under the following categories:

(i) trans-European transport networks and
(ii) environment including renewable energy, rail and public transport.

Table 1: Structural funds available to the new Member States compared to EU as a whole

	2007-2013			2010		2011	
New Member States	bn EUR	% of 2010 GDP	% of total	bn EUR	% of GDP	bn EUR	% of GDP
Structural funds for growth and convergence							
Bulgaria	6.9	19.3	3.8	1.0	2.9	1.1	3.0
Czech Republic	26.7	18.3	15.0	3.8	2.6	4.0	2.6
Estonia	3.5	25.0	1.9	0.5	3.5	0.5	3.6
Cyprus	0.6	3.7	0.4	0.1	0.5	0.0	0.3
Latvia	4.6	27.7	2.6	0.7	3.9	0.7	4.2
Lithuania	6.9	26.7	3.9	1.0	3.8	1.1	3.9
Hungary	25.3	26.2	14.2	3.6	3.8	3.8	3.8
Malta	0.9	14.5	0.5	0.1	2.1	0.1	2.0
Poland	67.3	19.0	37.8	9.4	2.7	10.0	2.7
Romania	19.7	16.0	11.0	3.1	2.5	3.3	2.5
Slovenia	4.2	11.7	2.4	0.6	1.7	0.6	1.7
Slovakia	11.6	17.6	6.5	1.7	2.5	1.8	2.5
Total	178.1	19.0	100.0	25.6	2.7	27.1	2.7
Other funds							
Rural development	37.6	4.0		5.6	0.6	5.5	0.6
Fisheries	1.4	0.1		0.2	0.0	0.2	0.0
All funds	217.0	23.2		31.4	3.4	32.8	3.3
The EU budget	bn EUR	% of 2010 GDP	% of total	bn EUR	% of GDP	bn EUR	% of GDP
Total	975.8	8.0	100.0	141.0	1.2	143.0	1.1
Struct. funds for growth and conv.	346.1	2.8	35.5	49.4	0.4	50.6	0.4
Rural development	96.4	0.8	9.9	14.4	0.1	14.4	0.1
Fisheries	4.3	0.0	0.4	0.6	0.0	0.7	0.0
All funds	446.8	3.7	45.8	64.4	0.5	65.7	0.5

Source: European Commission

2. European aspects regarding the absorption of structural and cohesion funds

Even though there are large sums of funds available to MS – especially for the ones from the Central and Eastern Europe – the lack of absorption is more than obvious in Romania and Bulgaria, with only 13% and respectively 15% as the absorption degree of funds from the ERDF, ESF and CF in the Financial Perspectives 2007-2013 has been mobilized. This absorption rate is in reality even smaller with the subtraction of payments of cash advances reaching a level of 3% and respectively 5% in the two countries. Due to the fact that for the 2007–2009 period the cash advances disbursed were unconditional and unrelated to individual projects progress implementation these figures show a better progress in this project implementation.

The absorption delays for the EU27 in the 2007–2013 period, are due to the fact that the multi-annual financial framework is agreed upon at a later stage, and this has resulted in negotiation delays of the National Strategic Reference Frameworks and of the Operational Programmes. Out of these programmes most were adopted in 2007 and only a hand full at the end of 2007. And in these terms, also given the nature of the policy, the first year of the programme's period will be characterized by a definite slow absorption. Even more so, the late start of programmes in the 2007–2013 period was, is and will also be influenced by the economic and financial crisis.

The use of these funds is currently not focused in terms of resources for the management and resolution of the current financial crisis. These funds could be used for:

i) counterbalance the recessionary impact of the fiscal consolidation, whether the respective countries have received financial assistance and are thus under strict conditionality (i.e. Greece, Hungary, Latvia and Romania) or are counterbalancing just to avoid the use of financial assistance (i.e. Portugal and Spain);

ii) keep at a steady level the public investment in infrastructure, human capital and research, resulting in a potential output growth as well as focusing and promoting structural reform in countries that are under strict conditionality.

In these times the Structural and Cohesion Funds have been underestimated and thus the numbers attributed to them are of no relevance. At the same time the funds have not been used at a full potential due to issues of governance. On the basis of the empirical data the positive effects of EU transfers is weak, but this means that the data is not necessarily too small to account for a difference but maybe it is due to their bad and poor absorption by MS. This paper states the obvious necessity that Structural and Cohesion Funds governance needs to be modified through the revision of objectives and methods of delivery. At the same time for certain projects the funds should be directly supervised by the European Commission with the support of an executive agency in times of crisis.

There is a total sum of EUR 348 billion under 1B of the EU budget which is made available to MS by the MFF for the 2007–2013 period. This represents a percentage of 2.8 of the EU GDP on average for every year this is 0.4% for the 2007–2013 period. Because of their size, EU funds are not such a powerful instrument for the allocation of resources, as for example the national budget of a federal state is. But this comparison is not valid, firstly due to the fact that the EU is not a per say federal system, and secondly the support for cohesion of the EU is represented by a large sum in comparison to, some rescue packages, like for Greece or Ireland – EUR 110 billion and respectively EUR 85 billion. Due to its nature the Marshall Plan support from 1948 to 1951 represented only 2% of all the receiving's country GDP and it was the trigger in modifying the political economy environment and thus making a significant contribution to the western European countries growth. Structural and Cohesion Funds can have a greater impact on growth and convergence over their face value if their objectives and their delivery are reestablished. On the basis of the agreement of Operational Programmes (OPs) all funds are pre-assigned to each country depending on that country's economy, population and surface levels.

The poorly and slow absorption rate of EU funds is the biggest problem of any country which is reflected by the development of commitment credits and made payments (i.e. *reste à liquider* or RAL). There is EUR 134 billion not contracted from the total EUR 270 billion for the 2007–2013 period for the EU27 which represent the sums allotted for the 2011–2013 period. Compared to the 2000 – 2006 period the absorption rate is clearly slower with apparently one year delay and this is due to:
i) the n+2 rule relaxation in 2007 which aided countries to not pressure the planning and implementation of the EU funded projects;
ii) the fact that under the co-financing principle a percentage of 20% of the total costs of the projects have to be assured through domestic resources. In the not so distant past the EU paid no great interest to macroeconomic effects when dealing with development funds. Currently, due to the fact that the southern part of the euro zone is facing difficulties and is in dear need of policy instruments for the revival of the economic environment, this approach is no longer proper for this period. Also the large sums of unused Structural and Cohesion Funds which some EU countries have at their disposal should be used for the framework of a temporary 2011-13 European Fund for Economic Revival (EFER). These funds could be administered by the European Commission through the support of an executive agency similar to the Trans-European Transport Networks Executive Agency. Even though there is a mention of a higher absorption degree for the EU funds within the adjustment programmes of Greece, Latvia and Romania this is not enough to ensure the desired economic growth.

3. Aspects regarding structural funds

The European Community stipulated that the "cohesion policy has been recognized as a key instrument at the Community level contributing to the implementation of the growth and jobs strategy – not just because it represents one third of the Community budget, but also because strategies designed at local and regional levels must also form an integral 33 part of the effort to promote growth and jobs. The role of SMEs, the need to meet local skill demands, the importance of clusters and the need for local innovation centers are such that in many cases strategies also have to be built from below, at the regional and local levels". The Fourth Report on Economic and social Cohesion form 2007, shows preliminary estimates for the 2000-2013 period which suggest an increase in GDP compared to a baseline scenario without cohesion policy, of around 3.5 % in Greece, and 3.1 % in Portugal and larger ones for the new Member States (2004 – 2013): 9 % in the Czech Republic and Latvia, 8.5 % in Lithuania and Estonia, 7.5 % in Romania, 6% in Bulgaria and Slovakia and 5.5% in Poland. In addition, it is estimated that by 2015 around 2 million additional jobs will be generated due to these levels of investments.

According to one of the European Commission's *Report on Budgetary and Financial Management - Financial Year 2003,* the main **Structural European Funds** are as follows:

(i) The largest of the four structural funds is represented by the European Fund for Regional Development (ERDF), which is focused on the financial monitoring of the regional development activities and the regional imbalances correction. It most frequently directs resources to "hard" transport infrastructure but also gets into other profit-creating investment such as to help SMEs.

(ii) The European Social Fund (ESF) is meant for the labor market, the encouragement of mobility among the human production factors and the financing of various forms of training and development of the labor force.

(iii) The third structural fund is the EAFFG, which deals with issues in the agrarian policy, but at the current state this fund focuses with the even out of regional differences in agricultural production (the Guidance Department, as it is called).

(iv) Out of the four funds, the ones presented above are also known as *the traditional structural funds.* The fourth fund is The Financial Instrument for Fisheries Guidance (FIFG), with jurisdiction for fisheries inside the EU.

The Cohesion Fund (CF) was established for the additional needs to achieve social and economic cohesion inside the EU. Thus, this fund is destined as an aid only to the MS which have GNI per capita fewer than 90%. These aids were given to Greece, Ireland, Portugal and Spain before the enlargement of 2004. The biggest part of this fund is focused towards transport and environmental protection. This fund's resources are *conditional* in comparison with the resources of the structural funds which are *supplementary.* This means that once a MS has passed the 90% GNI per capita that MS has no longer the right to receive these funds.

Financial engineering promotion for start-ups and microenterprises has been made through combining these financial mechanisms with technical assistance, grants, non-grants instruments like loans, equity, venture capital or guarantees: **JEREMIE**, for SMEs and micro-credit, and **JESSICA,** for urban development. The financial assistance will be granted only with the agreement and cooperation of the European Commission and the Institutions of the European Investment Bank Group and other International Financial Institutions.

Programmes:

1) URBACT II Programme – is thought for the 2007-2013 period and the principal objective of this program is to exchange experiences between cities all EU MS, the key-element of this program is the cooperation between the cities participating in projects. Considering the fact that from the 1st of January 2007, Romania is an EU MS, the cities of our country are able to build and present projects to obtain funding for economic and social, development the less-fortuned and sustainable development in urban areas. The program has a budget of around EUR 68 million. Thus in this perspective, 10 Romanian cities - Alba Iulia, Brasov, Blaj, Bucharest (Sector 2), Iasi, Odorheiu Secuiesc, Sacele, Sighisoara, Piatra Neamt, Timisoara and - have participated in the "*Aid for Cities*" project – URBACT in the 2002-2006 period, with the collaboration of an expert and the city or municipal decision makers who have requested assistance in helping them define and develop strategies for urban development at different levels (city, district / area within the city). For this project urban areas (with less than 20,000 inhabitants) in the new MS and cities of the old MS, in duly justified cases, were considered eligible for this project.

2) MICRO-CREDIT Programme represented a series of 80 micro-credits granted by the Opportunity Microcredit Romania Office (OMRO) - the first microfinance institution with which the European Bank for Reconstruction and Development (EBRD) signed a loan agreement – amounting to EUR 263,396, which were granted before Romania joined the EU, to start-up micro-enterprises and companies. Out of the total 80 micro-credits only one was of over EUR 10,000 and 36 of them, with a total value of EUR 109,449 were awarded in the North-West area, and the other 44, with a total value of EUR 153,947 in the Central region.

4. Particularities of the Romanian framework

There are three mechanisms of transmission of cohesion policy with long-term effects:

a) increase the stock and physical infrastructure, which is an entry for the entire productive activity;
b) increase the stock and quality of human capital through education and training investment, which is generally an effective factor of labor productivity growth;
c) financial assistance to SMEs by stimulating investment initiatives, research and innovation and management and marketing, eventually making it to increase productivity of all factors, while reducing production and capital costs. Therefore we can explain the aggregation of cohesion measures by different categories with different economic significance, which is to support the relevance of the three transmission mechanisms:
   1. Investment in technical infrastructure;
   2. Investments to improve human capital;
   3. Direct financial support for industry, services and agriculture.

Therefore, a possible distinction between funding sources is quite necessary, as an important operation in the work to access and absorb EU funds:
i. transfers from the EU, as subsidies for public authorities;
ii. co-financed by public and private sources, as set out in the Structural Funds Treaty.

5. Conclusions

The full potential of these funds is not used to its maximum as these funds could be used to counterbalance the recession's impact, keep under control investments and growth, and at the same time, increase stimulation for the need to use and increase the absorption degree of this funds as they represent a very big step in the right direction.

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