Regional transformation processes in Central and Eastern Europe

Contributions of the TRANSFOR(U)M network members

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2.1 The discrepancy between competitiveness and cohesion: Is economic growth always accompanied by growing disparities?

Hans Kramar

The conflicting goals of competitiveness and cohesion

All political bodies act in the dichotomy between the conflicting goals of competitiveness and cohesion. It is not easy to meet the requirements of both at the same time, since public efforts in economically lagging regions, aimed at reducing disparities, tend to be less effective than in highly developed areas. Due to different regional conditions (for example, qualification of labour, infrastructure supply, productivity, economic structures), competitiveness and economic growth can be achieved more easily by promoting projects in urban agglomerations than by supporting the lagging areas. At European level, this conflict becomes evident even in the basic treaties of the European Union: according to Article 2 of the EC Treaty, the Community strives to promote "a high degree of competitiveness and convergence of economic performance". Article 3 states that the activities of the Community shall include "the strengthening of economic and social cohesion" as well as "the strengthening of the competitiveness of Community industry" (EC 2002). Yet the Lisbon Strategy, which aims primarily at making the European Union the most competitive economy in the world, is often considered to have partly overruled the idea of cohesion. This conflict between contradictory policy objectives leads to the question of whether growing markets and changing political conditions in Europe have mainly enhanced the concept of competitiveness or rather supported the idea of territorial cohesion. The answer is not trivial and needs closer examination of the changing disparities at different spatial levels: Generally speaking, competitiveness is attained by public investment in highly developed centres, while territorial cohesion requires the financial support of lagging regions. Nevertheless, activities intended to encourage regional cohesion at European level may increase disparities within a state or a region at the same time. With this in mind, it may be highly instructive to examine the interrelation between disparities and economic growth: there is some evidence that rapid economic growth in the less developed member states is often accompanied by growing disparities within these countries.

Regional and national disparities in the European Union

An analysis of economic disparities within the European Union depends to a large extent on the regional level considered. As far as national differences in GDP per capita are concerned, the gap between the rich and the poor member states of the EU15 has clearly decreased over the past two decades. Between 1988 and 2001, the "old" cohesion countries have significantly converged to the European average (see European Communities 2004): GDP per capita in Portugal has increased from 58.9% to 70.7% of the EU15 average, Greece from 58.1% to 67.1%, Spain from 74.0% to 84.2% and Ireland has even become one of the richest countries, almost doubling its economic performance in comparison to the EU15 from 65.9% to 117.6%. At the same time, the catching up process of the accession countries in Central and Eastern Europe, which began long before they joined the EU in 2004, has also developed very rapidly over the past few years: recent data published in the Fourth Report on Cohesion (European Communities 2007) indicates that with the exception of the Czech Republic (2.2%) the average annual economic growth rate in these countries between 1995 and 2004 was significantly above the EU27 average of 2.3% (Estonia: 6.8%, Latvia: 6.4%, Lithuania: 6.0%, Hungary: 4.5%, Poland: 4.3%, Slovenia:

3.9%, Slovakia: 3.8%). At the same time, the wealthier countries were able to maintain their competitive edge to a large extent without improving their privileged position. These different developments have induced a reduction of national disparities, which is displayed by a decreasing standard deviation of national GDP per capita between 1995 and 2002:[3]

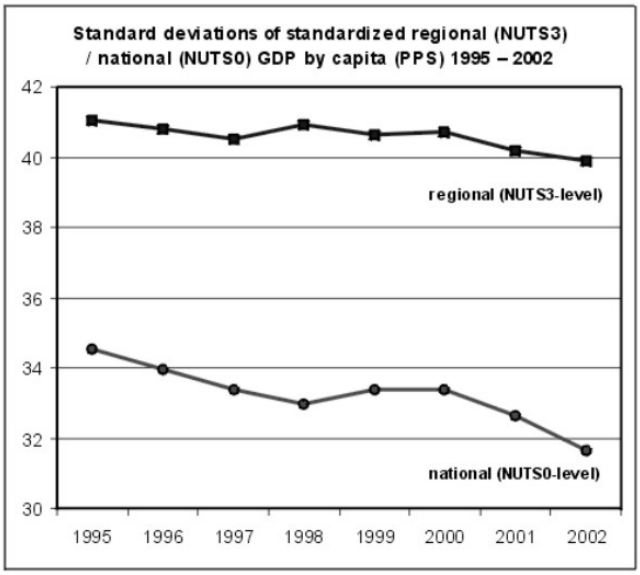

Figure 1: Change in disparities at regional and national level (EU25). Data source: Eurostat (2005), own calculations4

While the economic gap between the member states has clearly narrowed since 1995, regional disparities have developed differently. As shown in Fig. 2, the highest growth rates between 1995 and 2000 were in the richest NUTS2 regions.

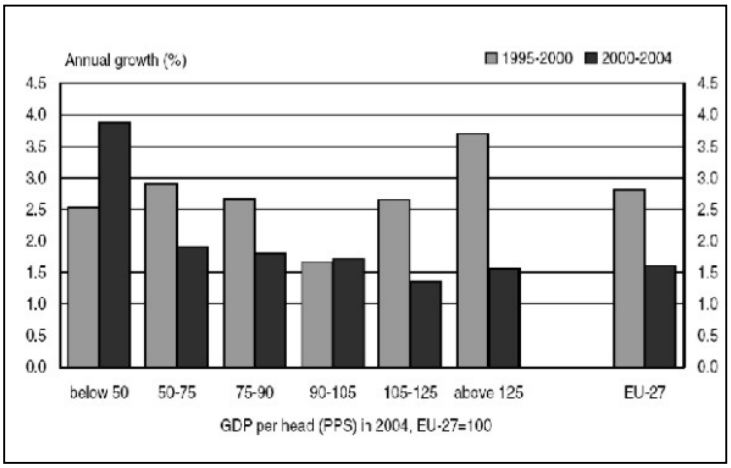

Figure 2: Regional growth in GDP per capita, 1995 – 2004. Source: EC (2007)

[3] The big differences in country size pose the problem of comparability and make interpretation of national disparities difficult. Consequently the three smallest countries (Luxembourg, Malta and Cyprus) were not considered in the analysis.

[4] The regional function only considers NUTS3 regions with complete data for the whole period and therefore does not include Portugal, Malta and parts of Poland. The national function does not include Luxembourg, Malta and Cyprus.

From 2000 to 2004, however, this clear trend of growing inequalities completely turned around: In this period, the poorest regions showed the most dynamic development, which could be interpreted as a slight tendency towards regional convergence. Nevertheless, the observation period is too short to take these figures as a clear sign of a turnaround. In order to throw light on these controversial results, the change in regional disparities was also examined in a more complex way and at a lower spatial level: similarly to the analysis of national disparities, standard deviation of GDP per capita for the NUTS3 regions was calculated for the period between 1995 and 2002. The results shown in Fig. 1 indicate that unlike the inequalities between the member states, regional disparities at NUTS3 level did not significantly decrease in that period. Therefore, even when considering the problem of comparability of spatial units, it can be stated that the reduction of national disparities in the European Union is not in fact accompanied by growing cohesion at regional level. The reason for these contradictory findings at different spatial levels can be found in the increasing disparities within several member states: Due to the uneven distribution of economic conditions (for example, highly-skilled labour, infrastructure, private investment, research and development), the gap between urban centres and the rural periphery tends to widen particularly in growing economies. While regional disparities within the majority of highly developed countries in Central and Western Europe did not change significantly (in Germany and Italy the gaps even decreased), the cohesion countries are facing growing inequalities: the growth rates of Spain (3.7%) Portugal (2.6%) and Greece (3.8%) between 1995 and 2004 were backed up by the dynamic development in the capital regions of Madrid (4.2%), Lisbon (2.8%) and Attiki (4.0%) (see European Communities 2007). This uneven distribution of economic growth, which mainly concentrates on the main urban centres, can be seen particularly at NUTS3 level. As can be seen from the results in Fig. 3, the standard deviation of GDP per capita of the NUTS3 regions has grown between 1995 and 2002 within each of the "old" cohesion countries.

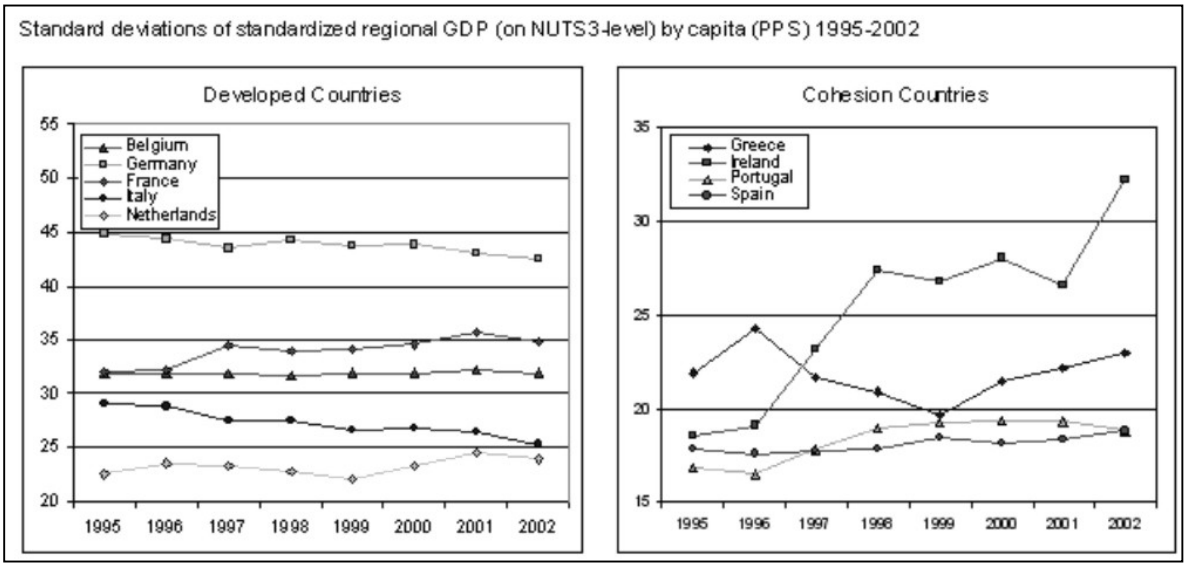

Figure 3: Change in disparities within selected developed and cohesion countries. Data source: Eurostat (2005), own calculations

The same phenomenon is even more obvious in the Central and Eastern European accession countries that joined the Union in 2004. With the exception of Poland, which is characterised by a rather polycentric settlement structure, these countries are economically dominated by their capital cities. Due to better economic and

social conditions, the capitals have consolidated their leading position by growth rates that greatly exceed the respective national average: Prague, for example, had an average growth rate of 3.8% between 1995 and 2004, while the economic output of the Czech Republic only increased 2.2% per year. The same is true for Hungary, where the high economic growth rate of 4.5% was mainly determined by the development of the Közép-Magyarország region (+5.0%). (See European Communities 2007.) The growing concentration of economic development in a few national centres is impressively illustrated by Fig. 4, which shows that the standard deviation of regional GDP per capita (at NUTS3 level) has increased in each of these eight new member states since 1995. This trend, which has continued over the past 10 years definitely poses a dangerous threat to cohesion within economically lagging countries in their catching up process. Increasing disparities within these growing economies can largely be explained by the accelerating competition between regions, which has been introduced by the integration of the accession countries into the European market and could hardly be influenced or controlled by national policies. As mentioned above, the reason for this trend towards intrastate divergence is to be found in different production conditions between urban centres and rural peripheries. In lagging countries, only a few locations are able to meet the new challenges of European or even global competition. Thus, research and development activities, educational programmes and infrastructure investments are highly concentrated in selected urban areas, while the remainder of the country is largely neglected. This kind of economic policy amplifies the economic trend, initiated by growing competition, and consequently reinforces the competitive edge of a small number of urban agglomerations in terms of labour force, physical and social infrastructure (particularly with regard to transport and communication networks) and innovative power.

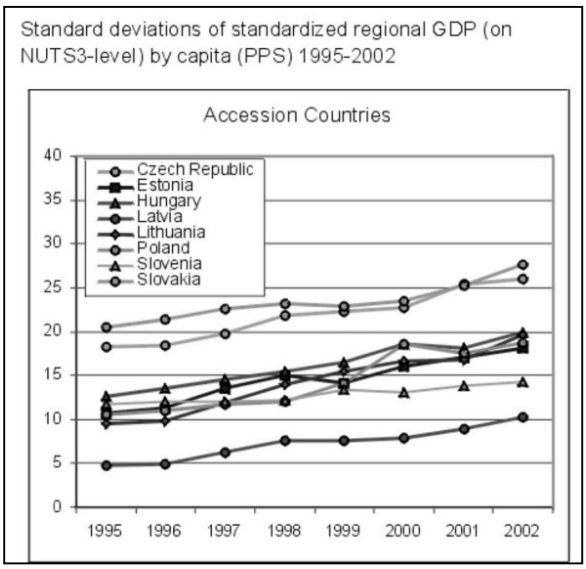

Figure 4: Change in disparities within accession countries. Data source: Eurostat (2005)

Disparities and economic growth

These conditions, which are crucial location factors for production, are responsible for making the big urban centres more competitive and attractive to foreign investors. As shown in Table 1, the spatial concentration of foreign direct investment (FDI) is much more pronounced in the less developed countries. Although in Germany and Italy FDI is significantly greater in the more highly developed parts (western and northern respectively) of the countries, a reasonable number of the

other provinces are also able to attract foreign investment, whereas in Spain the two dominating cities Madrid and Barcelona account for more than 80% of all FDI. This phenomenon is also evident in the accession countries (as demonstrated for the Czech Republic, Hungary and Slovakia), where it has become a serious problem in achieving balanced economic development.

Germany	**1998-2000**	**Spain**	**1999-2001**	**Italy**	**2000**
Nordrhein-Westfalen	37.5	Madrid	69.5	Lombardia	43.5
Hessen	21.6	Cataluña	13.5	Piemonte	14.9
Baden-Württemberg	11.7	País Vasco	5.5	Lazio	8.4
Bayern	9.0	Com. Valenciana	2.7	Emilia-Romagna	7.8
Czech Republic	**2001**	**Hungary**	**2001**	**Slovakia**	**2001**
Praha	49.3	Közép-Magyarország	67.7	Bratislavský	63.2
Stødní Cechy	10.7	Közép-Dunántúl	9.4	Východné Slovensko	18.8
Jihozápad	7.6	Nyugat-Dunántúl	7.5	Západné Slovensko	10.3
Severozápad	8.2	Észak-Magyarország	6.2	Stredné Slovensko	7.7

Table 1: Concentration of FDI in selected EU15 and accession countries. Source: European Commission (2004)

These findings give rise to the assumption that there is a correlation between total economic growth and the change in disparities within the member states. While the more highly developed countries show modest but constant growth rates in most regions, the dynamic economic development of the lagging states largely concentrates on a few locations. Due to the growing international competition between regions, it seems that in these developing countries only the large urban agglomerations are able to compete with highly developed regions in Central and Western Europe, whereas smaller regional and local centres and particularly rural areas constantly lose economic attractiveness and productivity. These results suggest that the catching up process of the lagging countries seems to be intrinsically tied to growing disparities on a national scale. Fig. 5 reveals a significant positive correlation (R = 0.795) between national economic growth and the change in intranational disparities for the member states of the EU25.

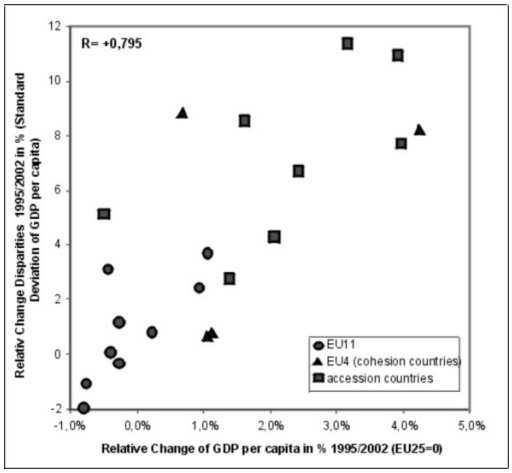

Figure 5: Correlation between economic growth and disparities within the member states of the EU25. Data source: Eurostat (2005), own calculations

These clear results indicate that the political bodies in these countries were unable to deal with the negative cohesion effects of growing competition. The most recent data presented in the fourth cohesion report (European Commision 2007), however, point out that the uneven distribution of economic growth seems to have slightly decreased over the last few years, which could mean that the lagging regions will finally start participating in the economic boom.

Conclusions: Challenges for national policies

The results of the empirical analysis suggest that strategies which aim at enhancing national competitiveness put the goal of regional convergence at risk. This is especially true for the lagging member states, where fast economic growth is mostly accompanied by growing regional disparities within their national territories. EU policies, however, are mainly directed at reducing disparities on a European scale (see Kramar 2006). Assuming that the efficiency of public funding rises with the quality of specific location factors, they focus on selected locations instead of granting relief all over the country. Thus, EU cohesion policies combine the idea of redistribution with the efficient application of funds and therefore give consideration to overall economic growth as well as to regional cohesion from a European perspective. At the same time, however, they abet the problem of intranational and intraregional disparities.

Particularly the economically lagging countries, which receive the major share of subsidies, are increasingly confronted with growing inequalities between a few prospering urban regions and a majority of provincial areas. Nevertheless, according to the principle of subsidiarity, this trend cannot be considered as a failure of EU cohesion policies. Empirical data demonstrating that the lagging countries have reduced their handicaps prove that the European Union has been successful in this respect over the past few decades. It is highly plausible that this development has been supported by the effective use of subsidies by focusing them on national and regional centres. At the same time, this strategy has certainly aggravated the problem of increasing economic disparities within the less developed member states. Since solving this problem is certainly not the task of the European Union, the political bodies in the member states have to face these facts and meet the challenge of enhancing cohesion within their territories.

Consequently, national and regional governments cannot be let off the hook regarding their responsibility for existing regional inequalities. In order to allow all regions to benefit from the economic boom in the centres, they would be well advised to adapt their national policies to the European strategies. On the one hand, the regional and structural programmes of the member states must be directed at improving general conditions in the rural and underdeveloped regions, making use of endogenous potentials. On the other hand, national transport planning departments have to provide an adequate secondary road and rail infrastructure supplementing the high-level Trans-European Networks, so that the growth effects induced in the regional centres can spread to the surrounding areas (see Kramar 2002). Considering the fact that growing international competition has accelerated the spatial concentration of investment and economic growth, the accession countries in particular will have to meet this challenge in order to guarantee a balanced development and to prevent further decay of the underdeveloped regions.

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