



**COLLANA DEL
DIPARTIMENTO DI ECONOMIA**

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DOES A BOTTOM-UP APPROACH WORK IN ALL REGIONS?**

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ISSN 2279-6916 Working papers

(Dipartimento di Economia Università degli studi Roma Tre) (online)

Working Paper n° 206, 2016

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Per ciascuna pubblicazione vengono soddisfatti gli obblighi previsti dall'art. 1 del D.L.L. 31.8.1945, n. 660 e successive modifiche.

Copie della presente pubblicazione possono essere richieste alla Redazione.

**esemplare fuori commercio
ai sensi della legge 14 aprile 2004 n.106**

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EU Cohesion policy in context: does a bottom-up approach work in all regions?

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Abstract

This paper looks at the European Union as a laboratory to study how ‘spatially-targeted’ policies (i.e. the EU Cohesion and Rural Development Policies) interact with sectoral ‘spatially-blind’ policies (i.e. the Common Agricultural Policy - CAP), jointly shaping regional growth dynamics. The analysis of the drivers of regional growth shows that the EU Regional Policy has a positive influence on economic growth in all regions. However, its impact is stronger in the most socio-economically advanced areas and is maximised when its expenditure is complemented by Rural Development and CAP funds. The top-down funding of the CAP seems to be able to concentrate some benefits in the most deprived areas. This suggests that bottom-up policies are not always the best approach to territorial cohesion. Top-down policies may – in some cases – be effective in order to channel resources to the most socio-economically deprived areas. Territorial cohesion requires the flexible integration and coordination of both bottom-up and top-down approaches.

Keywords: Regional Policy, European Union, Regional Growth, Rural Development, Common Agricultural Policy

JEL Classification: O180, R110, R580.

Acknowledgements

The authors are grateful to Roberto Esposti, Vassilis Monastiriotis, Andrés Rodríguez-Pose and to participants in the seminars held in London, Rome and Palermo for their comments to earlier drafts of this paper. The authors are solely responsible for any errors contained in the paper.

1. Introduction

At the peak of the Economic Crisis the European Commission launched a sophisticated and multi-dimensional strategy to boost growth and jobs in the European Union (EU) over the next decade: the Europe 2020 (EU2020) strategy (European Commission, 2010). EU2020 targets a large set of drivers of economic growth and employment in a co-ordinated and systemic fashion promoting, at the same time, gradual reforms in existing EU policies. In this context, EU2020 identifies the EU Cohesion Policy as a key delivery tool for its objectives. The EU Cohesion Policy is not simply aimed at inter-regional income redistribution, its key objective is to support long-term sustainable development in all EU regions including the most disadvantaged areas. While giving Cohesion Policy a central role in shaping the economic future of the Union, EU2020 has also assigned all other EU policies (including Agricultural and Rural Development Policies) the objective to contribute to the achievement of the developmental goals of the strategy. In other words, all EU policies (including sectoral policies) have been asked to contribute to economic growth and development in all areas of the EU in a coordinated fashion.

This fundamental shift in the objectives of all EU policies and the unprecedented emphasis on their coordination to serve a common set of overarching objectives poses a number of key conceptual and empirical questions. What is the actual impact of fundamentally different policies on the economic performance of a highly heterogeneous set of EU regions? What are the benefits arising from better policy coordination? What is the optimal combination between the traditional top-down approach of sectoral policies and the bottom-up nature of rural and regional development policies?

Notwithstanding the importance of these questions for the economic growth prospects of the EU regions over the next decade, very little is known on all these aspects. Very limited attention has been paid so far to the interaction between the EU Cohesion Policy and other EU policies. The EU Cohesion Policy is a 'spatially targeted' policy: eligibility and funding are granted on the basis of geographical criteria and its outcomes are also assessed in terms of the performance of well-defined spatial units (administrative regions). The EU Rural Development Policy is also 'spatially targeted' although its targets are defined in terms of a combination of geographical, sectoral and socio-economic attributes that define 'rural areas'. Finally, while some policies can be considered 'space neutral' in terms of both their intent and outcomes (e.g. competition policies) others, albeit neutral in their intent exhibit a considerable spatial impact: this is the case of the Common Agricultural Policy. As a consequence the EU Cohesion Policy does not operate in a vacuum but it interacts at the territorial level with other EU policies that – intentionally or unintentionally - might magnify or curb its influence on regional economic performance. In this sense, the 'New Regional Policy' paradigm (OECD, 2009b) advocates that all European policies, irrespective of whether they are 'spatially targeted' or 'spatially blind' (Dühr et al, 2010) should support territorial cohesion and promote growth in regions with "different social, institutional, and technological features" (Barca, McCann and Rodríguez-Pose, 2012, p. 143).

This paper makes a threefold contribution to this scholarly and policy debate.

First sectoral and territorial policies have traditionally been analysed in separated streams of research. As a result, the existing literature has frequently overlooked the potential territorial/spatial impacts of sectoral policies, failing to take into account these relevant drivers of regional economic performance. This paper cross-fertilises different streams of literature by developing a conceptual framework for the joint analysis of the impacts of sectoral and territorial policies. The paper makes use of the European Union as a laboratory to study how sectoral/'spatially blind' policies interact on the ground with 'spatially targeted' policies, jointly shaping regional growth dynamics. This approach to policy-induced growth dynamics has significant implications for public policies not only in the European Union: relevant lessons can be learned for the USA (where Agricultural Policies still absorb relevant shares of public funds – see Alston, 2007; OECD, 2015) as well as for emerging countries (such as China and India) where agricultural and rural development policies are often the main source of funding for territorial development actions (OECD, 2015);

Second, the conventional wisdom in the existing scholarly and policy literature posits that bottom-up policies are better equipped to promote regional development by tailoring the programmes to local conditions and maximising local involvement and ownership (Pike et al, 2010). However, the empirical evidence also suggests that regional policies often fail to deliver in the most disadvantaged areas (e.g. Kline and Moretti, 2014; Neumark and Simpson, 2014) due to their more limited planning (and lobbying) capabilities. This paper innovatively tests the hypothesis that top-down policies (such as the EU Common Agricultural Policy) may – in some cases – be more effective than bottom-up policies in order to channel resources to the most socio-economically deprived areas, benefitting territorial development. More automatic mechanisms and simplified procedures may allow actors in the most disadvantaged contexts to access key resources to support basic investment. The EU context is used as a laboratory – having experimented with both approaches for over 50 years – in order to compare for the first time in a systematic fashion the economic growth impacts of major top-down and bottom-up policies. The multidimensional policy structure of the EU makes it possible to test strengths and weaknesses of the two approaches, the interactions among them and their impacts in different territorial contexts.

Third, scholars and policy makers in both developed and developing countries are asking for sound empirical evidence to support fact-based policy choices. This paper applies state-of-the-art econometric techniques to an innovative database with regional-level expenditure for both territorial and sectoral EU Policies in order to assess their impact on regional economic performance. The convergent use of panel data methods with Instrumental Variables, spatial econometric techniques as well as quantile regressions makes it possible to inform the ongoing scholarly and policy debates by means of robust credible evidence as well to shed light on previously under-explored aspects of the link between the EU Regional Policy and economic growth (e.g. how this link changes for different regional GDP levels).

The empirical results – robust to a large number of checks - show that the EU Regional Policy has a positive and significant influence on economic growth in all regions. However, they also suggest that this impact is stronger in the most socio-economically advanced regions and is maximised when Regional Policy expenditure is complemented by Rural Development and Common Agricultural Policy (CAP) funds, in line with the expectations of the EU2020 strategy. The top-down funding of the CAP seems to be able to concentrate some benefits in the most deprived areas. Conversely only the most dynamics rural areas are capable of leveraging the bottom-up measures of the EU Rural Development Policy. This suggests that EU policy makers in all fields should constantly look for the best mix of bottom-up and top-down measures in order to tackle structural disadvantage.

2. Existing evidence and gaps

There is a consensus in the literature on economic convergence that the analysis of the relationship between the EU Regional Policy and economic performance needs to consider a broad set of conditioning factors. As a result, different contributions have focused their attention upon a very heterogeneous set of territorial characteristics.

The most relevant territorial factors conditioning the policy impacts are institutional and structural. With respect to the institutional elements, the EU Regional Policy impact is positively influenced by the degree of decentralization in the countries in which it is implemented (Bahr, 2008) as well as by the presence of national-level ‘supportive Institutions’ in terms of inflation controls, trust, openness and the lack of corruption (Ederveen, De Groot and Nahuis, 2006), the degree of openness of the economies (Ederveen, Gorter Mooij and Nahuis, 2002) and national “institutional quality” in terms of the rule of law, corruption, bureaucracy, expropriation risk and governments’ treatment of contracts (De Freitas, Pereira and Torres, 2003).

With respect to the role played by regional structural characteristics for the impact of the EU Regional Policy, one of the discriminants is the geographical position of the beneficiary regions with respect to either the geographical ‘core’ of the European Union or national decision-making centres (Soukiazis and Antunes, 2006). The initial level of economic development of the regions is also a relevant factor. Regional Policy effects are positive in less developed European regions (‘Objective 1’ regions and cohesion-country regions) in terms of GDP per capita levels, GDP growth, employment (Bouayad-agma, Turpin and Védrine, 2010; Esposti and Bussoletti, 2008; Mohl and Hagen, 2008; Ramajo, Màrquez, Hewings and Salinas, 2008) and cumulative job creation (Martin and Tyler, 2006). Convergent results were found by analyses that pooled the regions of all the 27 European countries together (Eggert et al., 2007). Furthermore, country-level effects are also relevant. Once regions are clustered by country, the positive impact on convergence is not confirmed for Germany, Greece or Spain (Esposti and Bussoletti, 2008). The policy impact is stronger in European areas with stronger absorptive capacity and weaker in the most disadvantaged areas (Cappelen, Castellacci, Fagerberg and Verspagen, 2003). Finally, innovative capacity and Social Filters (broader regional socio-economic environment) are relevant conditioning factors for the impact of European Territorial Infrastructural Policies (TEN-T) financed by the EU Regional Policy funds (Crescenzi and Rodríguez-Pose, 2012). There is also consensus on the idea that the effect of total expenditure is not positive in absolute terms but individual areas of policy intervention may produce heterogeneous effects

(Dall'erba, Guillain and Le Gallo, 2007). Only 'education and human capital' investments have actually sustained medium term growth. Instead, support for 'agriculture and rural promotion', 'infrastructure' and 'business' was less effective (Rodríguez-Pose and Fratesi, 2004).

In the existing literature on the role played by the EU regional policy in shaping regional conditional convergence, very limited attention has been paid to the role of other EU policies that co-exist and interact with the EU regional policy on the ground. From a conceptual standpoint this may hide relevant processes in the understanding of regional growth dynamics and policies (Duhr et al., 2010; OECD, 2009b). From a methodological point of view, overlooking (some of) the elements that influence the relationship between the EU Regional Policy and regional economic performance, entails *omitted variable* and *reverse causality* biases (Mohl and Hagen, 2010) in part possibly explaining the conflicting conclusions reached by existing studies¹

During their historical evolution, the EU Regional Policy and the CAP have influenced each other. Together they represent roughly 80% of the total 2014-20 EU budget and the EU Regional Policy alone accounts for approximately 3% of the Gross National Income (GNI) of the less advanced Member States (European Commission, 2014). For a long time, CAP market measures were at the most important EU policies. Instead, Regional and Rural Development Policies were underfunded and marginally developed (Crescenzi, de Filippis and Pierangeli, 2015; Saraceno, 2002). With the Reform of the Structural Funds (1989) and Agenda 2000, the CAP and the EU regional Policy became closely interdependent. In the 2000-2006 policy programming period, regional and rural development policies were part of the same joint programmatic framework and their different measures were implemented by the same Institutions (Mairate, 2006; Manzella and Mendez, 2009). In the 2007-2013 EU budget period they were again separated from one another in terms of programming and managing authorities. However, both EU institutions and researchers continue to stress – in principle - their joint contribution towards territorial cohesion (Barca, 2009; Crescenzi et al. 2015).

Given their 'spatially targeted' nature, the strongest relation is that between regional and rural development policies. However, it is increasingly recognized that the CAP market measures have also spatial implications. In line with the sectoral aim of agriculture support, CAP resources are 'captured' by dynamic, higher specialized and productive agriculture (Duhr et al., 2010) with potentially perverse impact in terms of 'distributive equity' favouring the polarization of agricultural income and preventing less developed areas from benefiting from its support (ESPON, 2004).

In the absence of proper coordination between different policies the literature has highlighted the risk of a counter-treatment effect on overall economic growth whereby one policy area may counterbalance the pro-cohesion effects of the other (Barca, 2009; European Commission, 2010; Duhr et al., 2010). Sectoral policies such as the CAP are designed to sustain a strategic sector rather than to promote cohesion and the former objective could have a completely countervailing effect on the second (Bivand e Brundstad, 2003; Bureau and Mahè, 2008).

¹ Mohl and Hagen (2010) reviewed at least 15 other quantitative studies, which with similar approaches to those discussed above reached altogether conflicting conclusions on the impact of cohesion policies.

Conversely, other research suggests that the CAP does not counteract the impact of the EU Regional Policy (Esposti, 2007) and once regional characteristics are appropriately controlled for, its contribution to cohesion is even greater than 'Objective 1' funds (Montresor, Pecci and Pontarollo, 2011). In addition, rural development policies can also contribute to economic development in the most disadvantaged areas (Shucksmith et al., 2005).

This highlights a fundamental set of gaps in the existing literature. Regional and agricultural economists very rarely work together and sometimes this lack of cooperation is exacerbated by the lack of integration of different data sources as also by the sharp division in responsibilities between different administrations at the EU, National and Regional levels (Kilkenny, 2010).

3. A policy-augmented model of Regional Growth

In order to analyse in a systematic and integrated fashion the interactions and regional impacts of 'spatially targeted' and 'space blind' policies it is necessary to extend 'standard' regional growth models in order to account for: a) a broad set of policies that operate in the same territory; b) the territorial characteristics that shape (or condition) the impacts and the interactions of the policies, thus defining the territorial context in which the policies operate. Following this line of reasoning the standard regional growth model of conditional convergence (Cappelen et al. 2003; Camagni and Capello, 2010 & 2013; Capello and Lenzi, 2013; Crescenzi and Rodriguez-Pose, 2011 and 2012; Paci and Marrocu, 2013; Petrakos et al. 2005a and b, 2011) is augmented by: a 'policy matrix' that includes expenditure under the EU Regional Policy, Rural Development and the CAP; a 'territorial conditioning factors matrix' that includes proxies for regional structural conditions that influence policy outcomes; and a 'Policy interactions matrix' that includes the interaction terms between the different policies and between the policies and regional contextual conditions.²

The model is specified as follows:

$$\Delta Y_{it-1} = \beta_0 Y_{i0} + \beta_1 X1_{it-1} + \beta_2 X2_{it-1} + \beta_3 X3_{it-1} + \beta_4 WX_{it-1} + \beta_5 C_{it-1} + \varepsilon_{it} \quad (1)$$

Where:

ΔY is the regional GDP average growth rate over the period from t-1 to t;

Y is the natural logarithm of the level of regional GDP per capita at the beginning of each period;

$X1$ is the 'EU policy matrix';

$X2$ is the 'Territorial conditioning factors matrix';

$X3$ is the 'Policy interactions matrix';

WX is the spatially-lagged variables matrix;

C is a matrix of standard control variables;

ε is idiosyncratic error

and where i represents the unit of analysis and t the policy programming period (1994-1999; 2000-2006; 2007-2013/09).

² For the sake of clarity, Beta coefficients reported in model (1) stand for vectors of coefficients. The model will estimate a separate coefficient for each variable included in each matrix.

In greater detail, the variables included in the model are as follows:

Regional GDP Growth rate per capita (dependent variable): the growth rate of regional GDP is the dependent variable and is used as a proxy for regional economic performance. It is computed as the logarithmic ratio between average GDP per capita (expressed in PPP - Purchase Power Parity) for the first three years of the period t and the correspondent value for the period t-1. As is customary in growth analyses, GDP growth rate is hence computed over multiannual periods rather than on a yearly basis in order to minimize the influence of external macro trends and shocks (the robustness checks confirm that results are robust to different methodological choices in this regard).

'EU Policy matrix'

The role of EU policies in regional growth dynamics is captured by examining the corresponding expenditure in each region for the EU budget programming periods 1994-99; 2000-06 and 2007-13 for Regional Policy, Rural Development Policy ('spatially targeted' policies) and CAP ('spatially blind' policy with territorial implications). With respect to the resources of the EU Regional Policy, the funds allocated to each region in each programming period depend on strict eligibility criteria that earmark a relevant share of the funds to the regions whose GDP per capita is below 75% of the EU average (named 'Objective 1 Regions' until 2006; 'Convergence Regions' in the 2007-2013 period; 'Less Developed Regions' in the 2014-2020 period).

'Territorial conditioning factors matrix'

This matrix aims to include the key territorial features that shape policy success and failure under the strong constraint of data availability for all EU regions. It includes structural socio-economic conditions in terms of demographics, productive structure and the labour market as well as regional innovative capacity and infrastructural endowment.

In particular, socio-economic conditions are captured by a Social Filter Index - a composite index extensively used in existing studies on innovation and regional growth (Crescenzi and Rodríguez-Pose 2009 and 2011) combining a set of proxies for territorial structural preconditions conducive to favourable environments for the genesis of innovation and its translation into economic growth. The Social Filter Index covers two main domains: educational achievement (Crescenzi, 2005; Iammarino, 2005; Lucas, 1988; Lundvall, 1992; Malecki, 1997; Rodríguez-Pose and Crescenzi, 2008) and the productive employment of human resources (Fagerberg et al., 1997; Rodríguez-Pose, 1999). With reference to the first domain, the index accounts for human capital accumulation (share of tertiary educated population in relation to the population aged 15+) and the skilled labour force (share of tertiary educated employees in relation to total employees). For the second domain, employment in agriculture is included in order to account for the composition of the local productive structure. The long-term component of regional unemployment (long-term unemployment percentage) is included in the index in order to account for such local labour market conditions as the rigidity of local labour markets and the stratification of inadequate skills (Gordon, 2001) that hamper innovation and economic growth³.

³ The index is calculated by using Principal Component Analysis (PCA) and accounts (considering only its first component) for around 50% of the total variance in the single variables that it synthesizes (Tables B.1 and B.2, Appendix B). It prevents collinearity problems potentially generated by the simultaneous inclusion of all the variables in the model (Duntenam, 1989). The four variables considered enter the composite index with the expected sign: human capital

Other two important features influencing policy impacts are: a) the level of R&D activities (R&D's share of GDP at the territorial unit level, Eurostat) that "captures the existence of a system of incentives (in the public and the private sector) for intentional innovative activities" (Crescenzi and Rodríguez-Pose, 2011, p. 14); b) the level of regional infrastructural endowment (regional kilometers of motorways standardized by 'total regional surface'⁴) as a proxy for a region's existing physical capital endowment.

Interactions matrix:

This matrix includes two key types of interactions: interactions between the individual components of the 'EU policy matrix' – in order to capture synergies or trade-offs between different EU policies – and interactions between the 'policies' and the 'conditioning factors' matrices in order to identify factors conditioning the policies' impacts. The elements of this 'interactions matrix' can capture the existence of synergetic/countervailing forces able to influence the policy's impact by augmenting or diminishing its magnitude. In particular, in line with the conditioned impact literature (Ederveen et al., 2002; Ederveen et al., , 2006), the overall impact of the policy is evaluated by assessing the sign and joint significance of the coefficient of the policy itself (i.e. the coefficient of the variable of interest indicated in the 'policy matrix') and the coefficient of the term of interaction with the identified conditioning factors (i.e. the 'interaction matrix')⁵

Spatially lagged variables

In order to account for interactions between neighbouring regions, this additional matrix introduces the spatially lagged values of 'conditioning factors'. These values enable us to explicitly model spatially-mediated inter-regional spillovers while, at the same time, minimising the spatial autocorrelation of the residuals. In particular, the spatially lagged variables included in the model are calculated by multiplying each territorial variable by a spatial matrix computed with the k-nearest neighbours (with k=4) criterion, which can minimize not only 'endogeneity' induced by travel-time distance weighting but also potential bias due to differences in the number of neighbours as between central and peripheral European regions. In particular, the 'spatially lagged matrix' includes the spatially lagged value of the social filter index, spatially lagged R&D activities and the spatially lagged infrastructural endowment.

These spatially lagged indicators place each region in the broader European space, thus making it possible to assess their interactions with neighbouring regions. They can capture spillovers of various kinds influenced by geographical accessibility or peripherality. Favourable socio-economic conditions in neighbouring regions (spatially lagged social filter index) influence indigenous economic

and skilled labour force – which also displays the greatest relative weighting – have a positive sign, while long-term unemployment and the agricultural share of employment, by contrast, figure in the social filter index with a negative sign. The Index is computed for each year (time variant indicator) holding constant the PCA coefficients (computed on the longitudinal dataset). The stationarity of the variables was preliminarily tested: The tests confirmed the stationarity of the series, allowing us to implement the PCA analysis on the panel dataset and assure the comparability of the index across programming periods.

⁴The standardisation proposed is used in order to purge potential biases linked to the different geographical sizes of the EU regions. Even if this is the customary proxy used in the existing literature, it should be noticed that it is uninformative on the quality and condition of the infrastructures themselves and nor does it reflect differences in construction and maintenance costs.

⁵In the paper, in line with the existing literature on conditioned impact, we focus on the sign and significance of coefficients, rather than on the size of specific point estimates. In general, following Wooldridge (2003), the magnitude of the overall effect can be computed by plugging in interesting values of the interacted variable (e.g. the mean or the lower and upper quartiles in the sample) to obtain the partial effect.

performance thought imitative effects and the mobility/movement of human capital/skills facilitated by geographical proximity. Accessibility to extra-regional innovative activities (spatially lagged R&D variable) can also influence internal economic performance through localised knowledge spillovers while the infrastructural endowment of neighbouring regions insures adequate accessibility to the region and the lack of transport bottlenecks.

Control matrix:

The “initial conditions” of the regions are controlled for by including in the model the log-level of GDP per capita (Eurostat) at the beginning of each period (OECD, 2009a): this is the term Y on right-hand side of Equation 1. The ‘control matrix’ is included in all specifications of the model and contains a set of additional control variables. The national annual growth rate accounts for the link between the national economic context and regional economic performance (Monastiriotis, 2014) while minimizing the effect of spatial autocorrelation by accounting for some of the common trends that characterize groups of territorial units; the Krugman index of specialization controls for the specialisation in local employment (Midelfart-Knarvik and Overman, 2002) by giving territorial unit i a zero rating if it has an industrial structure identical to other units, and by attributing a maximum value of 2 if it has no industries in common with other territorial units,⁶ and finally the population density controls for the local economy’s degree of agglomeration.

3.1 Units of analysis and data sources

In terms of geographical units the analysis is based on a combination of NUTS-1 and NUTS-2 regions⁷ in order to maximise the homogeneity of the territorial units in terms of the degree of autonomy and administrative roles as also to capture the relevant target area in which the policies under analysis are being implemented.

Consequently, the sample contains NUTS-1 regions for Belgium, Germany and the United Kingdom and NUTS-2 for the other European countries (Austria, Finland, France, Greece, Italy, the Netherlands, Portugal, Spain and Sweden). Denmark, Ireland and Luxembourg are excluded from the analysis because they do not have a relevant or equivalent sub-national divisions for the whole period of the analysis. In addition, lack of data prevents the French Départments d’Outre-Mer (FR9) and of Trentino-Alto Adige from being introduced, while, given the introduction of spatially-lagged variables, remote islands or enclaves could not be included. The analysis is necessarily limited to the EU-15 countries that have been recipients of EU Regional Policy, Rural Development and CAP funding for a sufficiently long time span.

Therefore, the final database comprises 139 territorial units (European NUTS-1 and NUTS-2) belonging to 12 European EU-15 countries (Austria, Belgium, Finland, France, Germany, Greece,

⁶ The Krugman Index is computed – as customary in the existing literature - following Midelfart-Knarvik and Overman (2002). We compute: a) for each region, the share of industry k in that region’s total employment: $V_i^k(t)$; b) the share of the same industry in the employment of all other regions: $\bar{V}_i^k(t)$; and c) the absolute values of the difference between these shares, added over all industries: $K_i(t) = \sum_k abs(V_i^k(t) - \bar{V}_i^k(t))$ with $V_i^k(t) = \frac{\sum_{j \neq i} x_i^k(t)}{\sum_k \sum_{j \neq i} x_i^k(t)}$. The index takes the value zero if region i has an industrial structure identical to the rest of the EU regions, and takes the maximum value of two if it has no industries in common with the rest of the EU

⁷ This combination of Eurostat NUTS regions corresponds to the TL2 classification developed by the OECD.

Italy, the Netherlands, Portugal, Spain, Sweden and the United Kingdom).⁸ The analysis has been performed over 3 EU-Budget programming periods (1994-1999; 2000-2006; 2007-2013).

Structural Fund (ERDF and ESF) data (per capita ‘commitments’ for each policy programming period) have been provided for by the Directorate General for Regional Policy of the European Commission (DG REGIO) in May 2009. Data referring on Rural Development Policy are based on per capita ‘commitments’ for each policy programming period. The first-pillar CAP data are instead, based on actual expenditure based on CAP total subsidies on crops and on livestock and CAP decoupled payments included in the Farm Accountancy Data Network (FADN). The details of the computation of the regionalised expenditure data for Rural Development and CAP are discussed in Crescenzi et al. 2015.⁹

The data for all territorial variables (dependent and independent) come from Eurostat.¹⁰ The values assigned to each of the three periods are computed as the average of their annual values over the policy programming period itself. With respect to the latest programming periods (2007-2013) all the territorial data are computed as an average of their annual values from 2007 to 2009, as 2009 is the last year for which data are available.

The choice of aggregating all expenditure/commitment data by programming period is customary in the literature due to the lack of reliability of annual expenditure data, in its turn a consequence of the complexity of EU budgetary and reporting rules: i.e. expenditure reported in a specific year might not necessarily be spent in that year. In addition, this choice allows us to minimize reverse causality (Mohl and Hagen, 2010) much more effectively than with annual data. Whole-period commitments are in fact assigned at the beginning of a multiannual period and, consequently, they do not depend on any subsequent shock (e.g., economic macro trend) that could occur over the period under analysis, thus leading to adjustments to annual expenditure (EU Commission, 2015). The same multiannual specification is also generally preferred for the “regional growth rate”, which instead of being computed as the ratio between the level of GDP per capita in two consecutive years, is usually considered as the ratio between average GDP per capita levels over a period of at least 5-years (OECD, 2009a). The analysis conforms strictly to the literature and in this sense adopts the most common specification for the model: regional growth rate between time t and time $t-1$ is regressed on the policy at time $t-1$, where t stands for the policy programming periods.

4. Empirical Results

The model specified in Equation 1 is estimated by means of Fixed Effect panel data (FE). In estimating the model, Fixed Effects-FE were found to be preferable to both Random Effects-RE and

⁸ Due to lack of data on R&D Activities and on the variables composing the Social Filter Index finally, the effective number of observations in the analysis turned out to be 121.

⁹ Since data on the first pillar of the CAP are based on effective expenditure, they are available only until 2009. Therefore, for the 2007-2013 programming period we have a partial coverage. This is not an issue in terms of the quantitative analysis because the policy variables enter the model only with one period of lag i.e. the policy data related to the 2007-2013 period never enter the model.

¹⁰ Data on GDP Growth Rate for the Austrian and the Italian regions and data on Population density for the Spanish regions come from national sources because they are not available on the Eurostat System

Correlated Random Effects-CRE specifications¹¹ (Wooldridge, 2002). Standard tests (such as Wald, R-squared and F-test) were carried out on the estimated FE model. Moreover, the model controls for heteroschedasticity and the spatial autocorrelation of the residuals. Finally, time/programming period Fixed Effects have been captured by including time dummy variables in the analysis after obtaining evidence on their joint significance. The time/programming period dummies account for the evolution of the policies over time and ‘clean’ the estimated coefficients from influence of factors specific to individual programming periods.

The presentation of the results is organised as follows. Table 1 presents some key descriptive statistics. Table 2 looks at total commitments/expenditure for all EU policies (regional, rural development and CAP together) while table 3 looks at each policy separately and at their interactions. The test statistics carried out for all versions of the model (reported at the bottom of the tables) confirm the significance of the regressions (F-test) and their predictive capacity (R Squared). Furthermore, the Wald test confirms not only the significance of the single coefficients but also the joint significance of the coefficients of the variable of interest (policy) and the interaction terms coefficients (Ederveen, De Groot and Nahuis, 2006). The inclusion of the spatially lagged variables allows us to remove spatial autocorrelation with no impact on the significance of the key variables of interests. Moran’s Indexes are computed for residuals of all specifications, rejecting the presence of Spatial Autocorrelation after the inclusion of the spatially lagged explanatory variables. In the robustness checks section the key specification of the model is re-estimated by means of spatial panel data models, confirming the results reported in the main tables and allowing us to exclude any bias due to spatial autocorrelation.¹²

This is an exploratory analysis aimed at uncovering territorial dynamics linked with the EU Policies rather than identifying causal relationships – consequently, in what follows, we focus mainly on the sign and significance of coefficients, rather than the size of specific point estimates.

Table 1 shows the magnitude and distribution of the policies’ commitments over time: the most significant part of the total EU funding is represented by the CAP and Regional Policy. Rural Development Policy’s role in terms of the amount of resources is still relatively small (Table 1).

Table 1 - Policy Commitments (in Euro values, per capita) and Regional Growth (average rate). Financial Periods 1994-1999; 2000-2006 and 2007-2013.

		Mean	Std. dev
CAP	1994-99	813.47	631.47
	2000-06	1118.44	847.91
	2007-13	1042.24	834.57
Regional Policy	1994-99	413.61	481.23
	2000-06	652.84	707.95
	2007-13	531.17	540.32
Rural Development Policy	1994-99	78.82	95.52
	2000-06	202.25	213.91
	2007-13	206.26	181.36
Regional GDP per capita average growth rate	1994-99	0.0198	0.0017
	2000-06	0.0255	0.0010
	2007-13	-0.0124	0.0026

Source: authors’ elaboration using European Commission Data

¹¹ FE results were compared to RE’s by applying the Hausman Tests (Hausman and Tylor, 1981). In addition, when comparing FE estimations to the “Modified Random Effect” estimator (Hajivassiliou, 2011) for CRE it was concluded that the FE estimator captures all exogenous variability available in the model and that FE was not only a consistent but also an efficient estimator for the regression coefficients (Hajivassiliou, 2011). These additional results are available upon request.

¹² In the main tables we prefer to report the standard panel data models in order to maximise comparability with other existing research and facilitate interpretation of the key coefficients.

Moreover, both the CAP and the EU Regional Policy increased their resources from the first to the second programming period but underwent a reduction in the latest period (2007-2013) as a consequence of the extension of the policies to the New Member States of the EU (EU Commission, 2008). Funds for Rural Development Policy increased over the whole period studied (1994-1999; 2000-2006 and 2007-2013).

In contrast to the positive trend registered across the first two policy programming periods, the growth rate during the period 2007-2013 diminished, and actually turned negative. As expected, the correlation between the policy commitments (considered as a whole) and GDP growth rate was also positive (0.6) and significant. In considering the negative sign for GDP growth rate over the period 2007-2013, account must, of course, be taken of the major economic crisis that has befallen the European and the world economy since 2008, which most likely driving the general economic growth downward.

Table 2 offers the key initial diagnostics for regional growth dynamics and EU expenditure. Total EU funding is positively and significantly correlated with regional economic growth. There is no evidence of a composition effect neutralising the overall impact of total EU funding: when considering total committed expenditure for EU Regional Policy (ERFD and ESF), the Rural Development Policy and the CAP together, the link with regional economic growth is positive and significant.

When looking at the role of other key drivers of regional economic performance, table 2 shows that the coefficient of initial conditions (level of GDP at the beginning of the period) is negative and highly significant, confirming the process of conditional convergence detected in existing literature (Bouayad-gha, Turpin and Védrine, 2010; Esposti and Bussoletti, 2008; Mohl and Hagen, 2008; Ramajo, Màrquez, Hewings and Salinas, 2008). The social filter – the broader set of socio-economic conditions – has also a positive but only marginally significant correlation with economic growth. The key controls behave as expected. National growth exerts a positive and significant influence on regional growth, confirming the importance of national framework conditions for regional performance (Monastiriotis, 2014). The Krugman Index – negative and highly significant - confirms that diversification is a key strength for EU regions. When spatially lagged variables are introduced into the regression (column 2) the high significance of Total EU funding is confirmed and inter-regional knowledge spillovers emerge as a key driver for regional growth in line with previous literature (Moreno et al. 2005a and b; Rodriguez-Pose and Crescenzi 2008).

Table 2 - EU Regional Growth and overall EU Spending (All Policies).

Dependent variable: GDP per capita Average Growth Rate		
	1	2
Ln of initial GDP p.c.	-0.8016*** (0.0676)	-0.7570*** (0.0670)
Total EU Funding	0.0570*** (0.0122)	0.0520*** (0.0125)
Social Filter Index	0.0190* (0.0102)	-0.0002 (0.0176)
R&D Activities	0.0055 (0.0208)	0.0070 (0.0195)
Infrastructural endowment	1.5220 (1.1194)	0.8422 (0.9630)
Spatially Lagged Social Filter		0.0249 (0.0168)
Spatially lagged R&D Activities		0.0330** (0.0167)
Spatially lagged Infrastructure		2.1387 (1.4234)
National Growth Rate	0.1270*** (0.0141)	0.1352*** (0.0147)
Krugman Index	-0.0670** (0.0286)	-0.0771** (0.0304)
Population Density	0.0001 (0.0000)	0.0001* (0.0000)
Constant	7.7730*** (0.6841)	7.2372*** (0.6717)
Obs	242	242
R squared	0.902	0.908
Prob>F	0.000	0.000

Robust and clustered standard errors in parentheses *** p<0.01, ** p<0.05, * p<0.1.

Table 3 opens the ‘black box’ of total EU funding. The first specification (column 1) relates the dependent variable to the initial level of GDP, the policy variables, the territorial conditioning factors (social filter index, R&D activities and infrastructural endowment), the spatially lagged terms and the control variables (coefficients not reported in the table as in line with table 2). Columns 2, 3 and 4 show the results obtained by considering the interactions between the various EU Policies and the territorial conditioning factors: column 2 shows the interaction between each EU policy and the social filter index; column 3 shows the policy’s interaction with R&D Activities; column 4 shows the policy’s interaction with the infrastructural endowment. Finally, column 5 shows the results obtained by considering the interactions within the ‘EU policy matrix’ referring with interactions between the regional, the rural development and the common agricultural policies.

Column 1 shows that the positive influence of total European funding should be attributed to the positive and significant role played by the EU Regional Policy while the coefficients of both Rural Development Policy and CAP are not significant. The EU Regional Policy is the only EU budget heading delivering a positive influence on regional growth. The ‘spatially targeted’ approach of the EU Regional Policy has been successful in supporting regional growth. Conversely, the CAP – notwithstanding the relevance of the financial resources distributed in each region – has not produced any relevant influence on average regional growth (Esposti, 2007). Furthermore, the results for rural development are not more encouraging: even if rural development policies should, in principle, combine an emphasis on rural areas with a bottom-up approach, they seem unable to do better than ‘traditional’ CAP interventions in terms of territorial cohesion.

Table 3. – Regional Growth and the EU Regional Policy, Rural Development Policy and CAP.

Dependent variable: GDP per capita Average Growth Rate					
	1	2	3	4	5
Ln of initial GDP p.c.	-0.7320*** (0.0786)	-0.8060*** (0.0760)	-0.7320*** (0.0778)	-0.6710*** (0.0847)	-0.7350*** (0.0778)
Regional Policy	0.1028*** (0.0301)	0.1365*** (0.0359)	0.1095*** (0.0354)	0.1184*** (0.0354)	-0.0569 (0.0551)
Rural Development Policy	0.0026 (0.0236)	0.0172 (0.0273)	-0.0649 (0.0358)	-0.0400 (0.0282)	0.1116 (0.0734)
CAP	0.0308 (0.0235)	0.0245 (0.0305)	0.0804 (0.0348)	0.0458* (0.0254)	-0.0060 (0.0385)
Social Filter Index*Regional Policy		0.0414** (0.0205)			
Social Filter Index*Rural Development Policy		0.0067 (0.0397)			
Social Filter Index*CAP		-0.0129 (0.0120)			
R&D Activities*Regional Policy			-0.0014 (0.0353)		
R&D Activities*Rural Development Policy			0.0264*** (0.0001)		
R&D Activities*CAP			-0.0410** (0.0178)		
Infrastructure*Regional Policy				-2.0114 (1.5513)	
Infrastructure*Rural Development Policy				3.8648** (1.4986)	
Infrastructure*CAP				-2.8016** (1.1935)	
Regional Policy* Rural Development Policy					0.1452** (0.0638)
Regional Policy*CAP					0.0422** (0.0185)
Rural Development Policy*CAP					-0.1056*** (0.0376)
'Territorial Conditioning Factors', 'Spatially Lagged terms', Controls and constant	X	X	X	X	X
Period Dummies	X	X	X	X	X
Obs	242	242	242	242	242
R squared	0.913	0.921	0.916	0.917	0.922
Prob>F	0.000	0.000	0.000	0.000	0.000

Robust and clustered standard errors in parentheses *** p<0.01, ** p<0.05, * p<0.1, 'territorial conditioning factors' (Social Filter Index, R&D Activities, Infrastructural endowment Spatially Lagged Social Filter, Spatially lagged R&D Activities, Spatially lagged infrastructure) and the same control variables (Constant; National Growth Rate; Krugman Index and Population Density) reported in Table 1 are included in all regressions but not reported in the table.

The analysis of the interaction terms makes it possible: i) to explore how the role of regional policy depends on the whole structure of the EU policies and of the territorial conditioning factors; ii) to capture potential synergies or conflicts between Regional and other EU policies of different nature and iii) to understand how these interactions can change depending on the territorial context.

The links between expenditure for the various policies and socio-economic contextual conditions are depicted by the interaction terms between the individual EU policy variables and the social filter index. The corresponding results are reported in column 2. Similarly to what Cappellen et. al (2003) suggested in a different framework, socio-economic conditions turn out to be a positive conditioning

factor for regional policy impacts. The relationship between Regional Policy funding and regional growth is stronger for areas with more favourable socio-economic conditions: both the coefficients of the EU Regional Policy and that for the term of interaction 'regional policy*social filter index' are positive and significant. This makes it possible to reinforce and generalise existing evidence so far restricted to the impacts of EU investment in infrastructure (Crescenzi and Rodríguez-Pose, 2012). Overall, regional policy generally supports growth but with stronger benefits for areas with favourable socio-economic conditions. It also emerges that the impact of Rural Development Policies and CAP is totally independent of socio-economic contextual conditions: their impact is not significant generally and nor is it conditioned by the socio-economic conditions of the regions.

The interactions between EU policies and regional R&D activities and infrastructural endowment are presented in columns 3 and 4 respectively. The coefficients of the corresponding interaction terms (and the joint significance of the direct and interacted coefficients) suggest that both R&D activities and infrastructure matter when Rural Development and CAP funds are considered. In particular, Rural Development funds might influence economic growth when targeted at regions with a comparatively stronger innovative and infrastructural environment (i.e. the most dynamic rural areas in Europe). Conversely, CAP funds – with their spatially blind approach, uninfluenced by the a priori quality of the region in the allocation of the funds – work better in the most disadvantaged areas, characterised by limited infrastructural and innovation endowment. This section of the analysis, therefore, confirms that 'spatially blind' policies do have spatial implications (Montresor et al., 2011). Given that CAP funding is not influenced by the capabilities of the different regions to 'bargain' for resources - these are allocated in a top-down fashion by means of subsidies largely linked to 'historical' production data¹³ – they are able to exert a positive influence on economic growth in most of the structurally disadvantaged regions. In addition CAP and Rural Development policy, even if funded by the same financial source, seem work in opposite directions when interacting with contextual conditions at the local level. In this sense, Rural Development policy behaves in a manner more in line with a 'spatially targeted' approach (Regional Policy).

The results in column 5 of Table 3 provide new evidence on the links within the 'EU policy matrix': the model specification now includes the terms of interaction between Regional Policy and the other EU policies. The EU Regional Policy's role is positively conditioned by synergies with all other policies: all interaction terms are positive and capture the marginal benefit from the policies on cohesion determined by such synergies. Instead, the interaction between the two 'agricultural' policies (CAP and Rural Development policy) shows a negative sign. When both CAP and Rural Development funds are targeted at regions that also benefit from more generous EU Regional Policy resources, the positive influence on regional growth is - ceteris paribus – maximised. But the same is not true for the interaction between Rural Development and CAP: when both 'agricultural' policies channel a high level of funding to the same region they tend to generate sectoral distortions detrimental to long-term economic growth. Consequently, it seems to be that synergistic use of

¹³ The progressive de-coupling of support from production introduced since 2003 by the so called Fischler Reform and the further move of the CAP 2014-2020 towards a first pillar with a fully decoupled support progressively based on a flat rate per hectare reinforces the top-down nature of this policy

different sources of funding and tools of a diversified nature can boost economic growth, while 'specialisation' in one single policy area is likely to generate decreasing returns and reinforce inconsistencies.

4.1 EU policies in regions of varying economic performance: Quantile Regression analysis

The use of interaction terms made it possible to study how the impact of the policies varies according to the characteristics of the regions in which they are implemented. However, the inclusion of the initial GDP per capita among the interacted terms is technically problematic due to endogeneity and simultaneity since initial regional GDP is also the key eligibility criterion for Regional Policy Expenditure. Therefore, we rely on Quantile Regression (QR) techniques in order to measure the effect of the policy not only at the centre but also for different quantiles of the distribution (Koenker and Bassett, 1978; Chernozhukov and Hansen, 2004). By estimating QR models we can investigate how the link between the EU Regional Policy and regional growth changes with the distribution of regional growth. This additional analysis captures if and to what extent areas with different regional growth rate (three distribution's quantiles: 0.10, 0.5 and 0.75) benefit from the EU Regional Policy. Unfortunately, the current state-of-the-art in the literature does not allow us to apply QR in a Fixed Effect panel data framework (Kato, Galvao and Monte Rojas, 2012; Ponomareva, 2011) and, given the importance of omitted variable bias in this context, we prefer to keep FE estimates as our main results and present QR results as ancillary evidence. The results are reported in Table A.3 in Appendix A¹⁴. The coefficients of the key variables confirm that the link between EU Regional Policy spending and economic growth is stronger in relatively richer and faster-growing areas. This finding suggests that although the policy's role is generally positive, it is not working completely in line with its main aim, namely to remedy the gaps between the disadvantaged and the relatively more dynamic areas of the Union. The strength of the relationship between the EU Regional Policy and growth is maximised in the already best performing EU regions.

5. Robustness checks

The robustness of the results is tested in a number of ways and the corresponding additional tables are included in Appendix A available on line.

5.1 Measurement error and endogeneity bias

In order to test for measurement error problems the analysis was reproduced with the use of an alternative measure for the key independent variable of interest. The policy variable adopted in the main analysis (whole period Commitments) is replaced by annual payments. Whole-period Commitments are considered in the literature more reliable policy indicators than annual Payments (OECD, 2009a; Mohl and Hagen, 2010). Whole-period averages are more accurate than annual data given that annual payments largely reflect reporting and accounting rules rather than actual expenditure patterns. In addition, whole-period commitments are more exogenous with respect to external shocks that can simultaneously influence both economic growth and expenditure. An

¹⁴ More methodological details for these additional sections of the empirical analysis are reported in Appendix A together with the key results.

example of this problem is the well-documented increase in Structural Funds actual expenditure in response to the Crisis started in 2008 (European Parliament, 2014).

The key regressions have been replicated with a specification, sample and time period that enable us to make comparisons as between the results of the estimation of equation 1 obtained by using Commitments (as in previous tables) and actual payments. Further details on these additional estimations are reported in Appendix A. The additional regressions confirm that the impact of the EU Regional Policy on regional economic growth is positive and significant when commitments from this alternative database as well as when payments are used as an alternative policy measure, provided that their endogeneity is appropriately accounted for in an IV framework.

In order to address any potential endogeneity issues, and identify the parameter of interest more accurately, we explicitly allow actual payments to be an endogenous variable and use commitments (decided a priori and well before actual economic growth is observable) as the corresponding instrument in an Instrumental Variable analysis. The choice of the instrument is confirmed by the first stage regression, and justified by the fact that Commitments, strongly correlated with Payments, only influence the economic performance of regions when transformed into expenditure (through the payments channel). Consequently, they represent an exogenous and relevant instrument to permit the model to correct the endogeneity bias likely to affect Payments.

The Hausman test confirms our intuition as concerns the 'endogeneity' of Payments. The IV regression that instruments Payments with the Commitments is preferred to OLS, as the latter considers Payments exogenous. The results of the IV regression are set out in Table A.2 column 3.

Overall these tests confirm the choice of our key policy variable. Commitments are not only capable of acting as a proxy for the policy by delivering the same results that would have been produced by considering the effective expenditure, but also that the Payments by themselves are unlikely to account for policy in a coherent manner insofar as identified as endogenous by the Hausman test¹⁵ for endogeneity.

5.2 Misspecification of the dependent variable

The specification of the model is in line with the standard panel data literature on regional economic growth and regional policy analysis (OECD, 2009a; Mohl and Hagen, 2010). In order to control for the robustness of the results with respect to the specification of the outcome variable, the model is re-estimated with an alternative version of the GDP growth rate. In particular, the main regression is re-estimated with a GDP growth rate computed as the natural logarithmic of average annual GDP growth rate over the first three years of each programming period t . This outcome variable is regressed on the independent variables taken at the time $t-1$ so that the GDP growth rate can be computed with respect to an initial period that is successive to the period to which the policy is related rather than coinciding with it. This eliminates any time overlap between the dependent and explanatory variable and reduce any simultaneity bias likely to affect the model: in this case, the idiosyncratic shocks occurred during the policy multiannual programming period ($t-1$) do not enter in the computation of the GDP growth rate determined within the following policy multiannual programming period (t). These robustness tests confirm the results of the main analysis (Tables A.3.a

¹⁵The p value of the test is equal to 0.0041.

and A.3.b. in Appendix A): even when the outcome variable is changed, the role of EU Regional Policy as well as that of overall European support remains positive and significant.

5.3. Spatial dependence and spatial panel data analysis

The main specification of the Regional Growth model presented in the paper includes the spatial lags of the key conditioning factors: after their inclusion there is no evidence of residual spatial autocorrelation in the regression residuals. However, in order to further check the robustness of the proposed results, other forms of spatial autocorrelation are controlled for by means of alternative specifications of the model. The Spatial Autoregressive (SAR and DURBIN) specifications of model (1) account for the spatial dynamics of the dependent variable with spatially lagged Y (Spatial lag models) coefficient. The Spatial Error Model (SEM) will, instead, account for the dependence determining the spatially inter-correlation between the error terms. The technical details of these additional estimations are discussed in Appendix and Results are reported Table A.4 in the same Appendix. These additional regressions confirm the key results of the analysis: spatial dependence related to Y is not statistically significant while signs and significance of the main coefficient of interest (Regional Policy) are all confirmed.

6. Conclusions

The launch of the EU2020 strategy by the European Commission placed the economic growth impacts of both territorial and sectoral policies at the centre of a lively scholarly and academic debate. Understanding if and under what (territorial) conditions different policies can contribute to regional economic growth is key not only to the future of EU policies but – more generally – to all countries and regions where similar policy tools co-exist and interact (e.g. in the USA).

The results presented in the paper show that regional policies can achieve higher regional growth. The EU Regional Policy expenditure is associated with stronger regional growth rates in all regions. This key result emerges clearly in all specifications of the model and is robust to a large number of tests. However, the positive influence of the EU Regional Policy is stronger in the regions with the most favourable socio-economic environment. This reveals a potential paradox of the EU Cohesion policy that works better in the relatively stronger (and better performing) regions with comparatively smaller (although still positive) gains for the most disadvantaged areas of the Union. The Rural Development policy, that is attracting increasing resources from the progressive reduction in funding of the more traditional market-based agricultural policies of the CAP, is not systematically linked with regional economic growth. Some positive influence of Rural Development funding only emerges in the most advanced and better endowed areas: the rural areas of the 'core' of the EU not the most disadvantaged and peripheral. The 'traditional' agricultural market-related CAP funding has also no direct link with regional growth. However, there is no evidence of a counter-treatment effect working against cohesion. Conversely, where the influence of CAP on growth emerges it is in the most disadvantaged areas of the Union (those with a poor infrastructural endowment and less innovation). This result sends an important message on the possibility that traditional top-down policies (such as the CAP) might be capable to channel their funds towards the most deprived regions of the Union with some positive influence on economic growth. On the contrary the complexity of the programming of bottom-up interventions might lead to a concentration of the benefits in stronger areas. Finally, the analysis also shows that policy coordination is of paramount

importance: returns from the EU Regional Policy are maximised where funding from the other policies is also concentrated. This confirms the OECD (2009) and Barca Report (2009) intuition on the importance of a synergic use of the funds from all EU policies, fully incorporated in the EU2020 strategy (EU Commission, 2010).

Although robust to a large number of tests, some key limitations should be borne in mind when interpreting these results. First, regional economic growth is not the only outcome of interest for the EU policies. All EU policies produce a number of other tangible and intangible outcomes (and public goods) that cannot be captured by the proposed analysis. Second the analysis is unable to unveil causal links: a number of techniques and checks have been adopted to minimise any potential bias due to endogeneity but we still this is not a fully causal analysis. Third, the time period covered by the analysis remains relatively limited and more data will be need for more long-term analysis. The now completely digitalised and harmonised collection of expenditure data will make this possible in the near future.¹⁶

Having acknowledged these limitations it is still possible to make some relevant policy considerations based on the results presented in the paper. The reinforcement of the local socio-economic environment is a crucial pre-condition for the success of any regional policy. This is of fundamental importance in order to maximise the returns to regional policy expenditure in the most deprived areas. Addressing this potential paradox is even more relevant to Rural Development interventions whose pro-growth potential is totally conditioned upon the pre-existing conditions of the target areas.

In order to address the structural conditions of the most disadvantaged regions purely bottom-up tools might be insufficient. Tailoring the various policies to local needs is certainly crucial. However, the analysis of the territorial effect of 'traditional' top-down agricultural CAP expenditure unveils a relevant story: top-down interventions might be very effective in order to channel resources to the most deprived areas. Where institutions are weak and local lobbies can form strong anti-growth coalitions the identification of local needs and the planning and implementation of bottom-up actions might be difficult. In these contexts, top-down policies might be more effective in earmarking resources to support basic investment in physical and human capital in the most deprived areas. As a consequence, a bottom-up approach to regional development policies is not necessarily the best possible solution for all regions. The experience of the EU suggests that it is necessary to carefully assess the best mix of bottom-up and top-down interventions to match the conditions of the various countries and regions. In the same vein a national-level coordination and agenda-setting might also favour the coordination among the various policies on the ground: at the local level conflicts and contrasts between the various agencies and offices might make this more difficult to achieve. The coordination between 'spatially targeted' and 'space blind' policies – that our analysis has shown to be key in order to maximise regional growth – might require the flexible integration of both bottom-up and top-down approaches.

¹⁶ Due to data limitations at the regional level we have been unable to include into the analysis EU expenditure under the Framework Programmes for Research and Technological Development to support and foster research in the European Research Area (ERA). The amount of resources absorbed by the Framework Programmes (55 billion euros in 2007-2013) is not comparable in magnitude to the funding for Regional, Rural Development and the Common Agricultural Policies considered in the analysis (roughly 90% of the total EU budget, i.e. approximately 900 billion euros in 2007-2013). However, the study of this complementary area of EU policy remains in our agenda for future research.

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APPENDIX A – Extension and Robustness checks

A.1 Quantile Regression analysis

This extension is based on Quantile Regression (QR) Techniques. As discussed in the paper QR has a number of advantages over standard linear regression analysis. However, when QR is combined with Fixed Effect panel data in order to control for unobserved heterogeneity constant over time (a primary concern in a policy assessment framework), its identification and estimation become very complex (Kato et al., 2012). In particular, when the number of observations on each individual/region is limited on account of the limited number of available time periods, it is difficult to allow for the effect of an individual FE to change across quantiles in the same way as we can allow for the effects of the X covariates. This difficulty stems from the fact that the standard methods used to cancel out FE are no longer applicable: the quantile of the difference in general is not equal to the difference in quantiles but instead become ‘intractable objects’ (Ponomareva, 2011).

Most of the literature that studies QR models for panel data with FE tries to deal with this difficulty by assuming that the number of periods t reaches infinity with sample size n and then considers individual heterogeneity a “pure locations shift effect” on conditional quantiles (Canay, 2010; Koenker, 2005) or by allowing it to vary across quantiles (Galvao, 2008). Instead, in relation to a relatively short panel, an attempt to estimate QR has been made by applying correlated random coefficients model (Abrevaya and Dahl, 2008), or by focusing on the identification of the coefficients for a single conditional quantile restriction rather than on the whole set of quantiles (Rosen, 2009) or even by estimating the moment of the conditional distribution of either continuous or discrete covariates (Ponomareva, 2011).

Nevertheless, most empirical QR applications prefer a cross-section framework for analysis (Buchinsky, 1994; Powell, 2011; Powell and Wagner, 2011). The robustness check proposed here proceeds accordingly. In particular, pooled OLS models that regress the regional growth rate at time t on the policy and on the other usual covariates at time $t-1$ are implemented: the average annual growth rate over the period 2007-2009 is regressed onto the Regional Policy Commitments and onto the other covariates related to the 2000-2006 period and the average annual growth rate over the period 2000-2003 is regressed onto the Regional Policy Commitments and other covariates related to the period 1994-1999. As stated earlier, QR analysis focuses on the 0.10, 0.50 and 0.75 quantiles of the Y distribution.

Table A.1 - Quantile Regression

	Quantile 0.10		Quantile 0.50		Quantile 0.75		Mean regression	
Dependent variable: average regional GDP growth rate 2007-2009								
Initial	-0.0550	0.0320	0.0060	-0.0002	0.0028	-0.0002	0.000	0.0001
condition	(0.0677)	(0.0273)	(0.0058)	(0.0088)	(0.0055)	(0.0092)	(0.0127)	(0.0149)
Regional	0.0211	0.0020	0.0057**	0.0048	0.0050**	0.0048	0.0096*	0.0090
Policy	(0.0000)	(0.0000)	(0.0000)	(0.0000)	(0.0000)	(0.0000)	(0.0000)	(0.0000)
Covariates*	No	Yes	No	Yes	No	Yes	No	Yes
Dependent variable: average regional GDP growth rate 2000-2003								
Initial	-0.0072	-0.0144	-0.0021	-0.0149**	-0.0091	-0.0093	-0.0028	-0.0070
condition	(0.0139)	(0.0122)	(0.0059)	(0.0066)	(0.0064)	(0.0087)	(0.0047)	(0.0057)
Regional	0.0051	-0.0038	0.0137***	0.0106**	0.0090**	0.0119*	0.0114***	0.0091**
Policy	(0.0000)	(0.0000)	(0.0000)	(0.0000)	(0.0000)	(0.0000)	(0.0000)	(0.0000)
Covariates *	No	Yes	No	Yes	No	Yes	No	Yes

*Covariates included in the model are the variables of the Territorial conditioning factors matrix and of the EU policy matrix plus the Control variables.

** Standard errors in parentheses *** $p < 0.01$, ** $p < 0.05$, * $p < 0.1$

A.2 - Measurement Error in the policy variable and Endogeneity

The additional dataset that makes it possible to test for potential measurement errors in the policy variable includes actual payments for all NUTS-2 regions in the EU27 and includes annual Commitments and Payments for the EU Regional Policy and Rural Development (together and not separable) over the period 2000-2009 only. As customary in the economic growth literature the test avoids annual GDP data to measure economic growth and relies on 5-year periods (OECD, 2009a), annual policy data from 2000 to 2009 are aligned to this, and the model was estimated as a cross section, where regional GDP pro capita growth rate over the period 2007-2009 is regressed onto the ‘spatially targeted’ policies’ payments over the 2000-2009 period. The same model was estimated by making use of Commitment data from the previous analysis by linking the regional growth rate of GDP per capita over the period 2007-2009 with ‘spatially targeted’ policies’ Commitments for the last two programming periods (2000-2006 and 2007-2013) in order to maximise comparability.

The results of the model estimated on both datasets are shown in Table A.2 below. In particular, the first column of the table shows the results obtained by running the model on the main dataset of the analysis (and as a consequence policy data refer to the whole period of Commitments). The second column shows the corresponding results obtained by running the model on the actual payments dataset. Finally, column 3 sets out the results obtained by considering Payments as endogenous and, consequently, instrumented by the corresponding Commitments an Instrumental Variable framework.

The check conducted on the main dataset confirms the impact of ‘spatially targeted’ policies on regional growth: i.e. the coefficient of the ‘spatially targeted’ policies is positive and significant.

The policy variable coefficient in column 2 is positive but not significant. However, once the endogeneity of actual payment is accounted for in column 3 by means of an appropriate IV strategy the key results of the paper are confirmed. In addition the results of this IV analysis confirm that the key conclusions of the paper are robust to endogeneity bias.

Table A.2 - Measurement Error in the Policy Variable and Endogeneity

Dependent variable: GDP per capita Average Growth Rate			
	1 - OLS	2 - OLS	3 - IV
Spatially Targeted Policies	0.0004*** (0.000)	0.0001 (0.000)	0.0001* (0.000)
Constant	-0.7320*** (0.1563)	-0.0260*** (0.003)	-0.0260*** (0.003)
N of Regions	139	198	198
R-squared	0.149	0.170	0.170
Prob>F	0.000	0.000	0.000

Standard errors in parentheses *** p<0.01, ** p<0.05, * p<0.1

A.3 - Measurement Error in the outcome variable

Table A-3.a - Measurement Error in the outcome variable (Total EU Expenditure)

Dependent variable: GDP per capita Average Growth Rate		
	1	2
Ln of initial GDP p.c.	-0.1484*** (0.0270)	-0.1493*** (0.0284)
Total EU Funding	0.0093* (0.0047)	0.0042 (0.0034)
Social Filter Index	0.0014 (0.0040)	-0.0038 (0.0037)
R&D Activities	0.0030 (0.0051)	0.0020 (0.0044)
Infrastructural endowment	0.2808 (0.3082)	-0.0188 (0.3340)
Spatially Lagged Social Filter		0.0046 (0.0041)
Spatially lagged R&D Activities		0.0225*** (0.0037)
Spatially lagged Infrastructure		0.1500 (0.5357)
National Growth Rate	0.0356*** (0.0050)	0.0410*** (0.0046)
Krugman Index	0.0010 (0.0082)	-0.0020 (0.0092)
Population Density	0.0001** (0.0000)	0.0001** (0.0000)
Constant	1.3974*** (0.2636)	1.3861*** (0.2751)
Obs	242	242
R squared	0.870	0.899
Prob>F	0.000	0.000

Robust and clustered standard errors in parentheses *** p<0.01, ** p<0.05, * p<0.10

Table A.3.b - Measurement Error in the outcome variable (Regional Policy, Rural Development Policy and CAP).

Dependent variable: GDP per capita Average Growth Rate					
	1	2	3	4	5
Regional Policy	0.0277*** (0.0066)	0.0223** (0.0091)	0.0038*** (0.0085)	0.0355*** (0.0070)	0.0003 (0.0206)
Rural Development Policy	0.0093 (0.0085)	0.0031 (0.0066)	-0.0028 (0.0113)	-0.0078 (0.0120)	0.0412** (0.0201)
CAP	-0.0198*** (0.0056)	-0.0115* (0.0068)	-0.0120 (0.0095)	-0.0173 (0.0070)	-0.0303*** (0.0089)
Social Filter Index*Regional Policy		-0.0128** (0.0054)			
Social Filter Index*Rural Development Policy		0.0215* (0.0115)			
Social Filter Index*CAP		-0.0048* (0.0026)			
R&D Activities*Regional Policy			-0.0096 (0.0085)		
R&D Activities*Rural Development Policy			0.0104 (0.0083)		
R&D Activities*CAP			-0.0055 (0.0057)		
Infrastructure*Regional Policy				-1.2217*** (0.3197)	
Infrastructure*Rural Development Policy				1.7491*** (0.4157)	
Infrastructure*CAP				-1.4444*** (0.2981)	
Regional Policy* Rural Development Policy					0.0145 (0.0221)
Regional Policy*CAP					0.0111** (0.0051)
Rural Development Policy*CAP					-0.0187 (0.0133)
Log of Initial GDP, 'Territorial Conditioning Factors', 'Spatially Lagged terms', Controls and constant	X	X	X	X	X
Period Dummies	X	X	X	X	X
Obs	242	242	242	242	242
R squared	0.919	0.927	0.921	0.939	0.924
Prob>F	0.000	0.000	0.000	0.000	0.000

Robust and clustered standard errors in parentheses *** p<0.01, ** p<0.05, * p<0.1 - The log of initial GDP, 'territorial conditioning factors' (Social Filter Index, R&D Activities, Infrastructural endowment Spatially Lagged Social Filter, Spatially lagged R&D Activities, Spatially lagged infrastructure) and the same control variables (Constant; National Growth Rate; Krugman Index and Population Density) reported in Table 2.a are included in all regressions but not reported in the table.

A.4 - Spatial Heterogeneity and Spatial Panel Data Analysis

The recent spatial econometrics literature has identified three different types of interaction effects that could affect local economic phenomena and consequently their analysis: endogenous interaction effects linked to the dependent variable (Y), exogenous interaction effects among independent variables (X) of the units of analysis, and interaction effects among error terms. Hitherto, by inserting spatially-lagged independent variables (spatially-lagged variables matrix) into the key model specification the regressions only included controls for the second types of these spatial interactions. However, the analysis implemented in the paper has not yet fully controlled for the spatial dependence of the dependent variable and error terms. These forms of spatial dependence can be treated in a panel data framework. By accounting for the unobservable spatial and time-period specific effects, the panel data and spatial econometric literatures offer a common setting, enabling us to account for the cross-sectional and state dependence of the Y and the Xs, while at the same time controlling for unknown heterogeneity. We can also account for them simultaneously through 'Spatial Dynamics Panel Data Models' (SDPDM). Such models can easily identify the dynamic responses over time and space of the space-time diffusion of policy impacts

through cross-partial derivatives related to changes in the explanatory variables and in the dependent variables (Elhroost, 2005). Once the need to account for spatial dynamics has been identified, the most serious issue seems to be the identification, among the Spatial Panel Data Models, of that model that can best capture and represent the spatial dependence of the data. Some analyses of European regional convergence processes have found evidence of model misspecification if the spatial interdependencies of regional growth are ignored. The most common approaches that address the issue of spatial dependence (Anselin, 2006) adopted in the existing literature refer to 'spatial error autocorrelation' (Arbia and Piras, 2009) and 'spatial lag' models. The latter, often considered a spatial autoregressive model, would seem to be more appropriate for quantifying how a region's growth rate is affected by the growth rate in surrounding regions (Anselin, 2006). The addition of a spatially-lagged dependent variable ('spatial lag; models), however, causes simultaneity and endogeneity problems that GMM (Badinger et al., 2004) and maximum likelihood (Elhorst, 2005) methods can address.¹⁷ As in classical panel data literature, a fixed-effects model is largely preferred (Elhroost, 2005) because the unobserved component is allowed to depend on the other regressors included in the model.

Within this FE spatial panel data framework, this section extends the main analysis of the paper by allowing the model (1) to account, in addition to the spatial dependence of the Xs, for Y and for error-term dependencies. For this purpose, model (1) will assume three additional specifications (SAR, DURBIN and SEM) and the results provided by the estimation (via maximum likelihood) of each of them will be analysed in a comparative sense in order to a) decide the best way to model the spatial dependence of the phenomena analysed and b) test if the results of the main analysis are robust, given the overall spatial dependence of the phenomena under analysis.

In this manner the Spatial Autoregressive (SAR and DURBIN) specifications of model (1) will account for the spatial dynamics of the dependent variable that estimates the spatially lagged Y (Spatial lag models) coefficient. The Spatial Error Model (SEM) will, instead, account for the dependence determining the spatially inter-correlation between the error terms (LeSage & Pace, 2009). Among the Spatial Autoregressive models, DURBIN could be understood as a special case of SAR as besides including the spatially lagged Y it also includes other exogenous spatially-lagged regressors. The choice of the regressors is unconstrained: both Xs and additional variables could be inserted in their spatial lag version. On the basis of the results reported in the literature, the DURBIN version of the model is considered the most appropriate and informative for regional analysis insofar as it is a "Spatial lag" specification that, moreover, makes it possible to control for Xs spatial dependence (LeSage & Pace, 2009).

As already seen for the previous robustness checks, both the data's and the model's structure needs to be adjusted to take due account of the setting in which the robustness check is to be performed, which, in this case, is the framework provided by the spatial panel data model.

In this sense, the panel was reset to comprise two periods: for the first period the independent variables refer to the first period of the main analysis (policy programming period 1994-99) whereas the dependent variable is the GDP Growth rate in the second period of the main analysis (2000-06). For the second period, the data used for the regressors refer to the period 2000-06 whereas the outcome variable is that used in the third period of the main analysis (2007-13). By performing the analysis on such a panel, we deploy

¹⁷ In this sense, a variety of estimators have been recently proposed by the literature: Yu et al. (2008) and Lee and Yu (2010) provide the asymptotic properties of a quasi-maximum likelihood for an SDPD model with exogenous explanatory variables. More recently, Korniotis (2010) proposed a solution based on the Least Square Dummy Variable and instrumental methods (Anderson and Hsiao, 1982) extended to allow for the spatial effect.

explanatory variables with a one-period-lag with respect to the dependent variable, even if the SPDM framework lags prevents us from taking lags directly into account in estimating a model.

Results from the SAR, DURBIN and SEM models, presented in Table A.4 below, refer to the version of model (1) estimated by considering Regional Policy, Rural Development Policy and CAP separately. The estimated models includes all regional conditioning factors, spatially lagged terms and controls included in the main results presented in Tables 2 and 3 of the paper. The analysis was carried out by implementing the STATA routine “XSMLE” (Hughe et al., 2012) and using a “Rook Contiguity” matrix as a spatial weight.

Table A.4 shows that the spatially lagged Y coefficient is never significant. Spatial influences on regional growth rates seem to be fully accounted for by the spatial correlation among the explanatory values (already included in the main specification of the model reported in tables 2 and 3 in the paper) while the endogenous spatial dependence in terms of Y seems to be irrelevant. This robustness check highlights that the main analysis has already accounted for the overall spatial dependence characterising regional growth. Even by accounting for the additional and potentially strong source of spatial dependence related to Y, the results obtained by the main model do not change. The findings on the main coefficient of interest (Regional Policy) are all confirmed. Moreover, the signs of the other explanatory variables are also generally confirmed, albeit with a different level of significance.

The results from the three different models (SAR, DURBIN and SEM) are coherent with each other. For each variable the coefficients used always have the same signs. By making comparisons between them, the different ways of modelling spatial dependence are shown to lead to similar conclusions. The SEM model, which accounts for the spatial dependence affecting the regression’s residuals, leads to very similar results with respect to those (SAR and DURBIN) provided by directly accounting for the spatial dependence of Y.

Table A.4 - Spatial Panel data models

Dependent variable: GDP per capita Average Growth Rate			
	SAR	DURBIN	SEM
Spatially lagged Y	-0.1396 (0.1807)	-0.1973 (0.1630)	
Ln of initial GDP p.c.	0.0706 (0.1041)	0.1195* (0.0677)	0.0760 (0.0617)
Regional Policy	0.0001** (0.0000)	0.0001*** (0.0000)	0.0001*** (0.0000)
Rural Development Policy	0.0001 (0.0000)	0.0001 (0.0000)	0.0001 (0.0000)
CAP	-0.0001 (0.0000)	-0.0001 (0.0000)	-0.0001 (0.0000)
Social Filter Index	-0.0176 (0.0143)	-0.0177 (0.0112)	-0.0160 (0.0109)
R&D Activities	0.0378 (0.0309)	0.0391** (0.0193)	0.0322* (0.0189)
Infrastructural endowment	2.7138* (1.4307)	3.2375** (1.3450)	2.9897** (1.3417)
Spatially lagged Social Filter Index		-0.0610* (0.0372)	
Spatially lagged R&D Activities		-0.1299 (0.1006)	
Spatially lagged Infrastructure		4.6522 (6.1640)	
Control	x	x	x
Obs	242	242	242
R squared	0.157	0.108	0.144

** Standard errors in parentheses *** p<0.01, ** p<0.05, * p<0.10

A.5 - Additional References cited in the Appendix

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APPENDIX B – Computation of the Social Filter Index

Table B.1 Principal component Analysis. Eigen analysis of the Correlation Matrix.

Component	Eigenvalue	Difference	Proportion	Cumulative
Component 1	2.35352	1.37195	0.5884	0.5884
Component 2	0.981569	0.319494	0.2454	0.8338
Component 3	0.662075	0.659236	0.1655	0.9993
Component 4	0.002839	-	0.0007	1.0000

Table B.2 Principal component Analysis. Principal Components' Coefficients.

Variable	Comp 1	Comp 2	Comp 3	Comp 4
Agricultural share of employment	-0.3963	0.4757	0.7852	-0.0094
Long term unemployment	-0.3132	0.7339	-0.6026	0.0105
Human Capital	0.6103	0.3407	0.1101	0.7066
Skilled labour force	0.6102	0.3449	0.0905	-0.7074