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What Brexit would mean for regional and cohesion policies in Europe

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Brexit affects regional policy both in the UK and in the EU27. It has a direct impact via financial adjustments for the individual funds, and indirect effects, possibly influencing the budgetary debates to come and adjusting regional policy priorities.

Regional and cohesion policy accounts for about a third of the EU budget. It is a major spending item and the EU's main investment policy. Up until now, the UK has contributed to the budget and UK regions received funds. Also, macro-economic averages used to determine eligibility for funds are based on the EU28. Thus, Brexit could mean losing a net contributor to the budget, UK regions as recipients and adjustments to economic averages for an EU27. However, the effects are highly contingent on the timing of Brexit and the planning processes and preparations for the new EU budget beyond 2020.

The biggest stakes are potential changes to the structural funds which invest all across the EU. Here, changes need to be assessed region by region and against the background of Brexit arrangements yet to be defined. For the cohesion fund, we expect continuity.

For the UK one of the key challenges is to map out what a renationalised regional policy is going to look like. This includes funding and definition of priorities but also drawing up new programmes and scale up capacities to administer them.

For the EU27, given that Brexit may take place within the current Multiannual Financial Framework, the upcoming years may prompt the need for further discussions and revisions in addition to the routine steps of EU budgetary planning. Beyond adjustments, Brexit may well stimulate the discussion about the design and effectiveness of EU regional transfers and strategies to best support convergence.

Finally, there is the issue of possible future cooperation between the EU27 and the UK after a Brexit. In principle, regional policy programmes already provide for some options here, e.g. as part of cross-border cooperation programmes. However, the specific arrangements and conditions are only going to be defined as part of the negotiations to structure the new relationship.

EU regional and cohesion policy: A quick introduction

EU regional and cohesion policy funds 1

Fund name	Fund target
ERDF *European Regional Development Fund*	Focus on reducing regional disparities, e.g. via investment in R&D or infrastructure
ESF European Social Fund	Focus on employment and education measures
CF *Cohesion Fund*	Focus on EU member states with less than 90 % of average EU income p.c., aims to reduce economic and social disparities
YEI *Youth Employment Initiative*	Education and employment programmes for 15-24 years-old people

Source: Deutsche Bank Research

Regional and cohesion policies are the EU's main investment policy and account for about one third of the EU budget. Financial resources are allocated via different funds, which have specific criteria to define eligibility for financial support to regions and member states. In total, the EU provides about EUR 350 bn during the period 2014-2020 via different funds.

Targets and instruments of regional and cohesion policy

Regional and cohesion policy is as much about "big picture goals" as it is about their implementation at local level. The key objective is to promote economic development and convergence across the EU. The goal of "economic, social and territorial cohesion" is fixed in Art.174 of the Lisbon treaty. In order to achieve these, the current programmes focus on supporting education, research and development, and infrastructure as well as strengthening the competitiveness of SMEs and environmental protection.

The instruments for regional and cohesion policy in the EU are the funds (ERDF, ESF and CF)[1] and the Youth Employment Initiative (YEI). Regional policy basically covers all EU member states but regions are classified according to their economic development to define priorities for allocation. In order to access regional funds, member states need to conclude partnership agreements with the European Commission and provide some co-financing for projects at national or regional level.[2]

EU budget 2014-2020 for regional and cohesion policy

Out of the total regional and cohesion budget (EUR 349.4 bn for 2014-2020), the major amount, EUR 282.7 bn, is allocated via the structural funds and EUR 63.4 bn through the cohesion fund to member states. Regarding the structural funds, the ERDF accounts for EUR 196.3 bn and the ESF for EUR 86.4 bn in EU financing. Of ERDF funding, the major share (about 95 %) is invested in programmes with the target 'Investment in growth and jobs' and about 5 % allocated to 'European territorial cooperation (ETC)'.

Regional and Cohesion Policy 2014-2020: A look at the UK

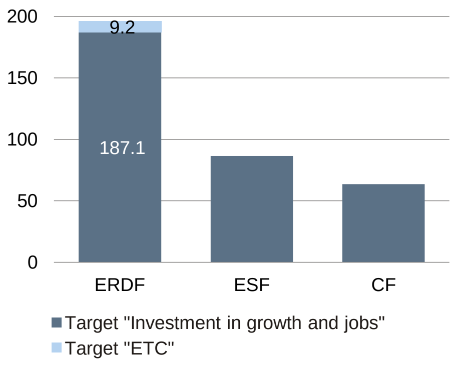
For these instruments and based on the planning period 2014-2020, about EUR 10.8 bn of EU regional policy budget have been earmarked for the UK (approx. 3.1% of total funding). The shares for the individual funds vary considerably reflecting differences in policy focus and promotional targets. The UK receives EUR 5.8 bn from the ERDF and EUR 4.9 bn from the ESF (about 3% of total ERDF and 5.7% of total ESF funding) but does not get support from the

[1] Whereof the structural funds are the ERDF and the ESF. Together with the European Agricultural Fund for Rural Development (EAFRD) and the European Maritime and Fisheries Fund (EMFF), they make up the European Structural and Investment (ESI) Funds.

[2] Partnership agreements are concluded between the European Commission and the individual member states. The agreements set out national authorities' plans on how to use the funding from structural and investment Funds 2014-2020. As such, the agreements set strategic orientation, define investment priorities and link member states priorities to the EU 2020 strategy.

EU budget for funds 2014-2020 2

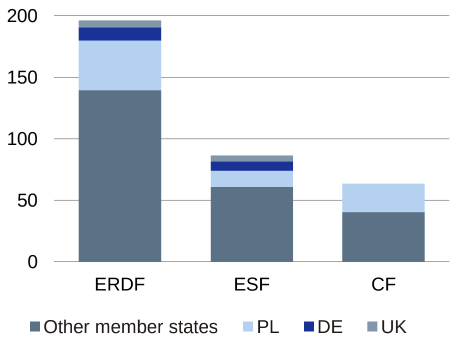
In EUR bn, update 1 July 2016.



Sources: European Commission Cohesiondata, Deutsche Bank Research

EU Regional Policy: Changes after Brexit? 3

EU funding 2014-2020 by funds, in EUR bn



ERDF: European Regional Development Fund
ESF: European Social Fund
CF: Cohesion fund

Sources: European Commission, Deutsche Bank Research

Lower income, lower threshold 4

EU member states	Per capita GNI 2015 (avg.)	Threshold for CF eligibility
EU-28	25,038	22,534
EU-27 (w/o UK)	24,531	22,078

Simulated values based on 2015

Sources: Ameco, Eurostat, Deutsche Bank

cohesion fund, which aims to support convergence of EU member states themselves at relatively less advanced stage of economic development. For comparison: Germany benefits by a total of EUR 18.3 bn from the structural funds (ERFD and ESF), a somewhat higher amount than the UK (i.a. due to higher population and funding for regions in former East Germany) while Poland receives EUR 53.4 bn from structural funds and EUR 23.2 bn from the cohesion fund. In addition to the structural funds, the UK gets about EUR 206.1 m from the YEI initiative.

Potential effects of Brexit on regional and cohesion policy: Timing will be key

First, the potential adjustments to regional and cohesion policies are going to be intertwined with the larger debate about needs for adjustment in the EU budget due to Brexit.

Second, the possible consequences on regional and cohesion policy are highly dependent on the timing and the exact circumstances of Brexit. A key question is whether a Brexit would take effect during the current budgetary planning period (2014-2020) or thereafter. This would for instance affect the need to adjust allocation of funds (when? how much?) as well as the need to define transition periods (until 2020 and/or thereafter?).

As part of the exit negotiations, issues such as the future of cross-border regional projects involving UK participants would also need to be addressed. In addition, one open question at this point is the potential for future cooperation on regional policies. EU regional policy already contains arrangements to cooperate with partners beyond the EU at regional level, for example as part of cross-border projects. Yet to what extent these would fit for a new EU-UK relationship remains to be further discussed.

A look at impact for the different instruments

Cohesion fund – expect continuity

The cohesion fund aims to support convergence of EU member states at relatively less advanced stages of economic development. Member states with per capita GNI lower than 90% of EU average are eligible for funding. In 2014-2020, the UK does not receive any funding from the cohesion fund.[3] Thus, regardless of the Brexit timing, there would not be a direct effect for the UK (regions) here.

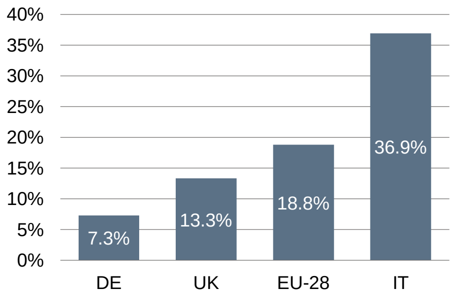
As for the EU27, a Brexit would lower the average GNI per capita by about 2%.[4] Theoretically, this could change the group of eligible member states due to the lower threshold. While Brexit might prompt the need to take another look at the arrangements for the current period before 2020, simulation based on current data suggest that the group of member states benefiting from cohesion funds would likely stay the same. From a budgetary planner's perspective, the easiest scenario would be a Brexit to take effect simultaneously with the end of the current budgetary period in 2020 with new calculations and eligibility to be reassessed anyway for the years thereafter.

[3] Eligible in 2014-2020 are BG, HR, CY, CZ, EE, EL, HU, LV, LT, MT, PL, PT, RO, SK and SI. In addition, due to transition provisions, some member states no longer eligible in the current period still receive funds for a certain period.

[4] Estimates based on 2015 values. Data: Eurostat Ameco, 5 National Income.

Youth unemployment rate in Europe 5

In % of active population (less than 25 years). Data seasonally adjusted, Apr. 2016.



Sources: Eurostat, Deutsche Bank Research.

Youth unemployment initiative – some changes possible

To strengthen employment of young EU citizens (15-24 years old), the EU provides EUR 3 bn in the period 2014-2020 in combination with funding by the ESF of additional EUR 3 bn. The budget for the youth employment initiative is allocated to regions at NUTS 2 level[5] with a youth unemployment rate higher than 25% or to regions in member states with a youth unemployment rate higher than 20% in combination with growth of the unemployment rate of more than 30% in 2012.

Youth unemployment remains a pressing problem in the EU – the average share of young people without a job was about 18.8% in April 2016 – and an important issue for EU cohesion policy accordingly. However, there are significant differences across EU member states. In the UK, youth unemployment stands at 13.3% at present. While this is clearly below the EU average at country level, there are nevertheless some regions in the UK with a very high youth unemployment rate which have received funds, for example Tees Valley and Durham or West Midlands. For 2014-2020, support to UK amounts to EUR 206.1 m (of which EUR 61.8 m had been paid as of May 2015).[6]

If the UK would leave the EU before the end of 2020, it could lose its claim on funding for the current budget. Funds not paid yet could be stopped unless transition arrangements were established as part of exit arrangements.

With the current YEI only targeting EU members, ending membership would also end funding, i.e. if a Brexit would have taken place by 2020 any new YEI budget would be tailored to an EU27. Funding beyond 2020 would need to be discussed anyway as part of the negotiations for a new multiannual framework.

However, additional changes to YEI might well take place before that if the mid-term budgetary review results in budget increases to the programme reflecting prioritization of efforts to tackle youth unemployment in the EU.

Structural funds with the biggest stakes

EU funding from structural funds aims to support all regions in the EU. Although the regional policy focuses on economically weaker regions, developed and the so called "transition" also receive funding to support growth. For 2014-2020, a total of EUR 10.8 bn from the structural funds is assigned to the UK, thereof EUR 5.8 bn from the ERDF and EUR 4.9 bn from ESF. The funding targeted for 'Investment in growth and jobs' can be used in combination with national co-funding in 17 national and regional programmes in the UK. The funding targeted for 'European territorial cooperation' is distributed between the member states of the regions participating in the cooperation.

Funding of 'European territorial cooperation' by the ERDF

For supporting 'European territorial cooperation' 2014-2020, a total of EUR 9.2 bn is allocated to the three different categories: 71.7% to cross-border cooperation[7], 22.8% to trans-national cooperation and 5.4% to interregional cooperation (see table on next page for criteria).

[5] "NUTS" refers to "nomenclature des unités territoriales statistiques" i.e. the system to classify territorial units in the EU for statistical purposes. NUTS 2 are the basic regions for the application of EU regional policy. Currently, there are 276 NUTS 2 regions in the EU.
[6] Latest available.
[7] Without external instruments for pre-accession assistance (IPA) and for European neighbourhood (ENI).

Beyond EU members – European territorial cooperation with third countries and territories 6

Third countries and territories can participate in cooperation programmes if invited by an EU member state (MS) to join a cooperation programme. The participating MS has to consult the third country before submitting the programme to the Commission. The understandings of the consultation meeting need to be expressed in formally approved minutes. The European Commission selects appropriate programmes under the constraints that the operations implemented in the territory of third countries should serve primarily for the benefit of the regions of the Union. Thus, third countries interested in ETC participation cannot initiate programmes by themselves but depend on EU MS's interest in a cooperation programme.

Category of ETC	Cross-border cooperation	Trans-national cooperation	Interregional cooperation
Assigned funding	EUR 6.6 bn	EUR 2.1 bn	EUR 0.5 bn
Territorial classification	NUTS 3 level regions	NUTS 2 level regions	Member states
Eligible regions/MS	EU*	EU	EU
	Norway	Norway	Norway
	Switzerland	Switzerland	Switzerland
	Liechtenstein	Liechtenstein	Liechtenstein
	Andorra	Andorra	Andorra
	Monaco	Monaco	Monaco
	San Marino	San Marino	San Marino
	+ third countries with shared borders with EU member states/outermost regions of EU	Faroese	Faroese
		Greenland	Greenland

Source: Deutsche Bank Research

European territorial cooperation focuses on supporting regions in the EU but projects can also involve non-EU members and their regions. However, this is "by invitation" and with an emphasis on added value for the EU regions. Also, engagement as a non-EU partner would need to be funded by the UK.[8]

ETC in the UK at present and (partly) in the future?

The UK participates in 14 programmes, thereof five in cross-border cooperation (including the extra PEACE programme with Ireland), five in trans-national cooperation and four in interregional cooperation. Figure 7 shows the cross-border cooperation programmes with UK participation.

If the UK would cease to be an EU member, it could still partially continue participating in cross-border cooperation because there would be shared borders with the EU27. However, given current rules, this would only provide for continued participation of NUTS 3 level regions – i.e. rather small geographical units – directly located at the border. The other UK regions somewhat further away from a border, which are currently taking part in cross-border cooperation, would not be able to participate any more. Furthermore, participation in trans-national and interregional cooperation would be at stake. This would not only affect funding to the UK and its regions which could stop after Brexit but also ongoing trans-national and interregional cooperation programmes in the remaining member states which may need to be reviewed to comply with regulation because they currently involve the UK.

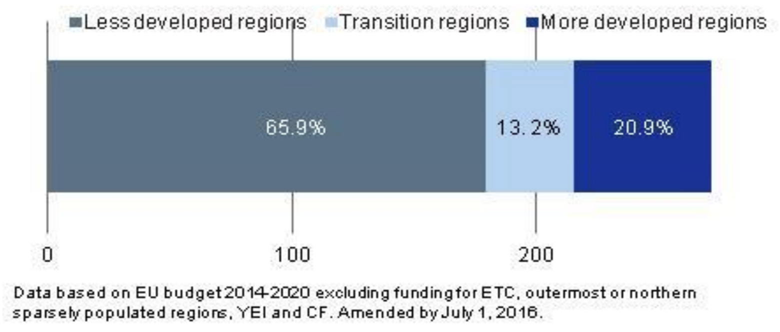
Funding of 'Investment in growth and jobs' by the structural funds

EU funding from the structural funds is allocated to the member states by classifying regions into less developed, transition and more developed regions. The classification depends on the per capita GDP in the regions (see table next page).

[8] See Bachtler and Mendez (2016).

Regional funding territorial distribution 7

Category	Less developed regions	Transition regions	More developed regions
Classification	< 75% of average per capita GDP	> 75% of average per capita GDP and < 90% of average per capita GDP	> 90% of average per capita GDP

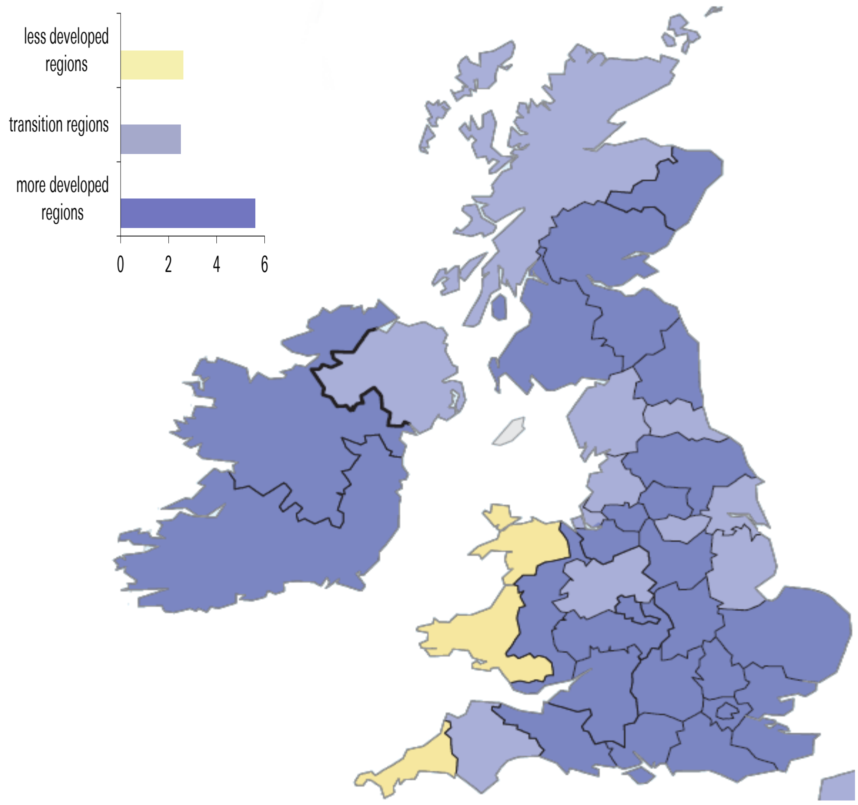


Sources: European Commission Cohesiondata, Deutsche Bank Research

All regions in the UK benefit from the structural funds, two of them particularly

Regional funding territorial distribution 8

In EUR bn



Sources: Eurostat regional yearbook (2015), European Commission Cohesiondata (update 1 July 2016), Deutsche Bank Research

The UK has a total of 40 NUTS 2 regions, of which only two are currently classified as “less developed”. These are West Wales & The Valleys and Cornwall & Isles of Scilly, which benefit disproportionately from structural funds. In total, they receive EUR 2.6 bn (2014-2020) from the EU funding, which is almost a quarter of the UK’s total regional policy funds. Transitions regions and more developed regions receive EUR 2.5 bn and EUR 5.6 bn. A Brexit and potential cuts in EU funds would thus affect UK regions to very different extents, depending on two key factors, i.e. their current benefits as well as domestic arrangements to substitute or mitigate the impact of a loss in EU funds.

The structural funds after Brexit: Biggest stakes, possible changes ahead

If the UK leaves the EU before the end of 2020 it could lose its claim of funding for the structural funds. Especially for the two less developed regions this could put access to considerable financial resources at stake. Reacting to growing concerns in the UK about potential funding shortfalls due to Brexit, Chancellor Hammond has stated that the UK would compensate for losses in EU funds. Notably, the funding for multi-year projects EU structural and investment fund projects, signed before the autumn statement 2016, is fully guaranteed by the Treasury even beyond a Brexit. For EU funded projects, which will be signed after the autumn statement 2016 but before the UK’s departure from the EU, the Treasury will put in place arrangements with further details to be set out ahead of the autumn statement.[9] Providing a “roadmap” for the medium-term is going to be important to manage a “smooth transition” and avoid a sudden stop of projects or reluctance of new ones being put forward. However, at this point it is still too early to tell what domestic regional policy strategies in the run-up to and eventually after a Brexit are going to look like.

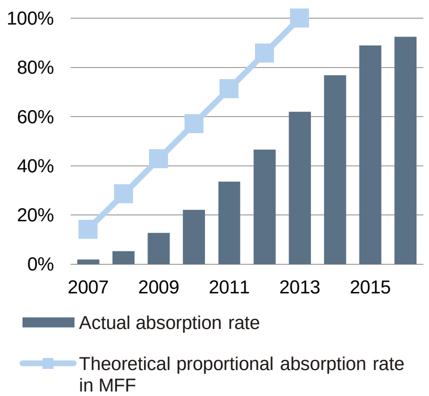
With regards to the EU27, regions may be in for changes as well. The reason is that Brexit would affect the numerical threshold levels to qualify for the different categories of the structural funds because the UK regions would no longer be part of the averages, which are used to define the eligibility. This would thus prompt needs for revision and some regions could be reclassified as part of this.

Given current uncertainties surrounding Brexit, these issues can hardly be fixed as part of the regular mid-term budgetary review upcoming for the end of this year. Also, there is no general reclassification scheduled. However, once the timeline for Brexit clarifies and if it were to take effect before 2020, some member states could ask for a re-classification hoping to receive higher funding after the revision. At this point, it is of course not set that a special review or reclassification of regions would take place in a “Brexit before 2020” scenario but it is very likely that this issue would at least come up in discussions among the remaining EU27. Again, beyond 2020 a new allocation would need to be discussed anyway. Changes in thresholds would then of course only be one of the factors influencing future allocation, alongside the size of the total budget to distribute and fixing spending priorities. Any new arrangement here will need to consider the sensible balance between net-payer and net-recipients of the EU budget, involve a review of both expenditures and revenues as well as re-evaluation of programmes. To that extent, the future of the structural funds and their distribution needs to be seen as part of the wider budgetary debate.

[9] Letter from the Chief Secretary to the Secretary of State for Exiting the European Union on EU funding, HM Treasury (13 August 2016).

Average absorption rates 2007-2013 9

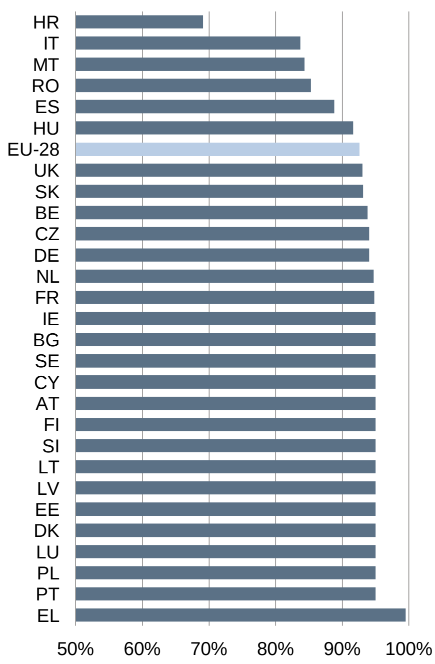
EU average in %



Sources: European Cohesiondata, Deutsche Bank Research

Absorption rates 2016 for MFF 2007-2013 10

Absorption in percent (Data Aug. 2016)



Sources: European Commission Cohesiondata, Deutsche Bank Research

What economic impact of regional and cohesion policy?

So far, most discussions have focused on potential losses or redistribution of funds due to Brexit. But what about the economic effects of (no longer) being part of regional and cohesion policies? After all, to what extent regional policy is efficient and effective, has been the subject of a long-standing and often controversial debate.

From a practical perspective, there is some indication that programmes perhaps work better than their reputation and also have improved during the last years. For example, absorption rates were lower than aimed for in the period 2007-2013 (see figure 9), a problem also flagged in the Commission strategic report on cohesion policy 2013. Several reasons for lower absorption were identified here, such as the impact economic crisis limiting capacities for public investment, insufficient administrative capacity and the late start of programmes due to the extension of the previous period.[10] Consequently, the Parliament and the Council decided on a prolongation of possible absorption and the low absorption rate was compensated until 2016.

A more detailed look at the absorption rates of member states for the previous multi-annual financial framework (MFF) 2007-2013 in 2016 shows that they have reached 92.5% (total EU) indicating that overall funds do get used (see figure 10). This has been the case for the UK (absorption 93%) as well as for most other member states.[11] While this cannot answer the question whether funds were put to good use and generated growth, it does suggest that by and large member states have been able to access them.

While high absorption remains a practical policy objective, the key goal is of course to use the funds well and effectively contribute to regional growth. Analyses on the economic impact of regional and cohesion policy overall suggest that regional transfers by the EU generate some value for money, even though the precise effects somewhat vary (see Box 11 for overview). Mostly, this is due to differences in datasets (periods and regions considered in studies), model choice and specifications. One of the methodological challenges is to account for both the influence and interplay of regions' (structural) characteristics, e.g. geographic position, openness, and national level factors such as growth 'supportive institutions', rule of law, corruption etc. Some of the data desirable for analyses may not be available or limited at regional level and there can be time-lags that make it difficult to capture full effects (e.g. spending on education measures to have an impact at a later point in time).

Relevant empirical analysis can be classified in four categories by the different methods used in the analysis, namely 1) macroeconomic models, 2) regression analyses, 3) micro-economic studies of beneficiaries and 4) control groups and more qualitative work using case studies. Researchers who applied macroeconomic models (mostly HERMIN or QUEST) tend to find significant positive effects. The focus of economic regression analyses is to test for convergence and the results vary widely, depending on the specific technical specification, time series and data sets. Some analyses find a significant positive effect on convergence, while others show no effect or positive results only conditional on exogenous factors. Results from micro-economic studies using control groups show positive effects of EU regional and cohesion funding on growth and case studies further report positive effects in general.

[10] See Ivana Katsarova, Library Briefing of the Library of European Parliament (1 November 2013): The (low) absorption of EU Structural Funds.

[11] The possibility to increase EU-co-financing shares for countries under stability support programmes may have contributed to increase absorbtion in several crisis countries in particular.

How effective is EU regional policy? A look at research findings 11

Crescenzi et al. (2014): The authors find that EU regional policy has a positive and significant effect on economic growth in all regions analysed. The effect is stronger in the most socio-economically advanced regions and even higher when regional funding is combined with rural development and common agricultural policy. Crescenzi et al. use a standard regional growth model augmented with some additional control variables for the MFF 1994-1999, 2000-2006 and 2007-2013 on NUTS 1 and NUTS 2 level of EU-15 countries and the result perform well to robustness checks.

Becker et al. (2012): The authors find a non-linear relationship between the treatment intensity of EU regional transfers and per-capita GDP growth. They identify a maximum desirable treatment intensity of about 1.3% of a region's GDP. Beyond this level, the null hypothesis of zero or even negative growth effects induced by additional transfers can no longer be rejected. Furthermore, the authors find an optimal treatment intensity of 0.4%. About 18% of NUTS 3 level regions received transfers above the maximum treatment and about 36% above the optimal treatment intensity. Thus, there is scope for greater efficiency regarding the growth-maximizing allocation of regional funding in the EU. The authors use generalized propensity score estimates on NUTS 3 level for the MFF 1994-1999 and 2000-2006.

Marzinotto et al. (2010): The authors find that EU regional policy in less developed regions has a positive and significant effect on growth. They use a regression discontinuity design to identify regional policy over the period 1995-2006 for EU-15. Annual per capita GDP growth is 0.6-0.9 percentage points higher. The results perform stable to different robustness checks.

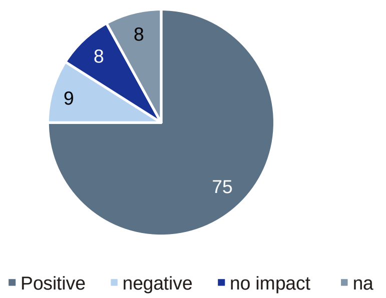
Mohl et al. (2010): The authors find not clear evidence for growth effects for all regions, but funding for less developed regions has a positive and significant impact on growth. Furthermore, they identified a time lag of up to four years. The authors analyze the relationship between EU regional policy and regional growth using a spatial panel approach on NUTS 2 and NUTS 3 level for the period 1995-2005.

Source: Deutsche Bank Research

While there are fewer analyses focusing on the impact of EU funds on the UK in particular, a recent paper (di Cataldo 2016, 2016a) examined effects on Cornwall and South Yorkshire using counterfactual methodologies to assess how the regions would have fared without financial support. Di Cataldo's results suggest positive effects on employment for Cornwall estimating that unemployment claimants declined over time (1992-2014) by more than 30 percent compared to a counterfactual region also controlling for a number of other factors to isolate the actual effects of EU funds. However, looking at South Yorkeshire he also finds that gains for regions can quickly disappear once they no longer benefit from high-intensity funding.

Liked by beneficiaries... 12

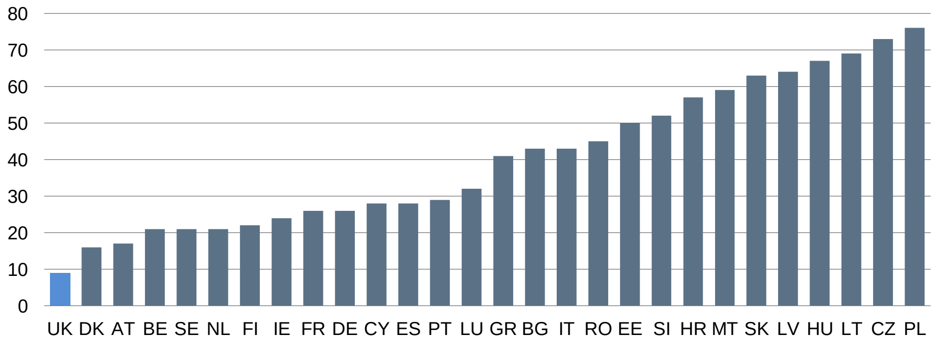
"Taking into consideration all the projects you have heard about, would you say that support had a positive or negative impact on the development of your city or region? " In % total EU



Sources: Flash Eurobarometer (2015), Deutsche Bank Research

...but with limited awareness 13

"Europe provides financial support to regions and cities. Have you heard about any EU-co-financed projects where you live?" Share of respondents answering "yes" in %



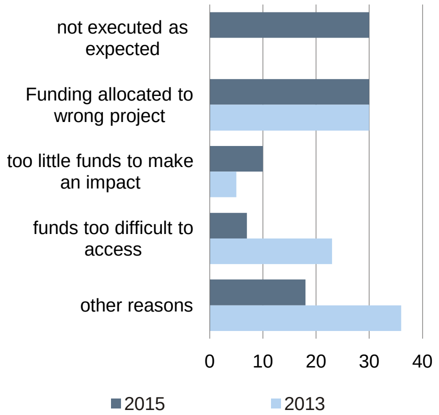
Sources: Flash Eurobarometer (2015), Deutsche Bank Research

An issue that is less in focus of most economic analyses of regional policy is its (optimal) organisation and implementation efficiency. Yet this point may receive more attention in the years to come given that Brexit prompts the UK to reorganise its regional policy.

Brexit and EU regional and cohesion policy – what way forward?

Room for improvement with implementation 14

Reasons of respondents who consider EU co-financed projects have had a negative impact



n=909, total EU

Sources: Flash Eurobarometer, Deutsche Bank Research

Brexit is going to impact on regional and cohesion policy in Europe over the years to come. There are several key aspects, i.e.

— For the UK to map out what a new domestic regional policy strategy would look like after exit, how to organize, administer, and finance programmes

— For the EU27 to consider potential needs for adjustments due to Brexit with respect to the remaining members

— For both the UK and the EU27 to negotiate the "nuts and bolts" such as for example transition periods for ongoing projects and potentially the possibilities for further cooperation, for example as part of cross-border projects or potentially beyond.

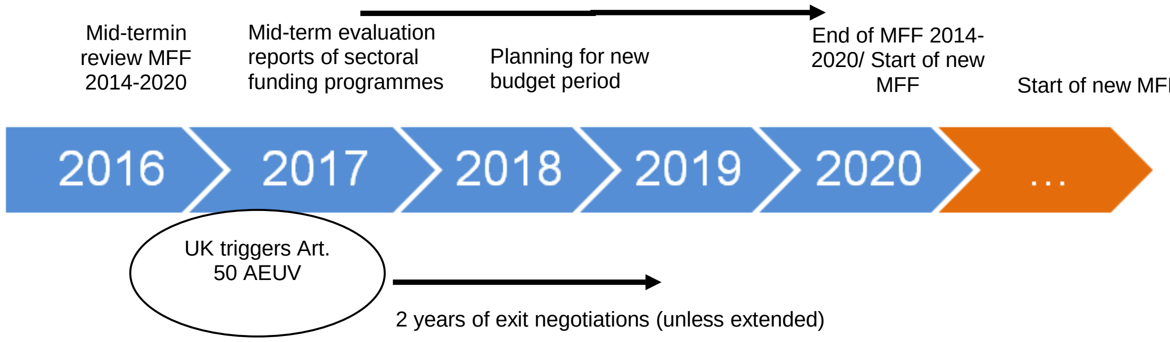
For the UK regions, the most pressing question is of course whether funds they used to receive from the EU budget and which would no longer be accessible post-Brexit are going be replaced by additional funding from national sources (short, medium and longer term-perspectives). Moreover, there are a number of additional issues involved in "renationalising" regional policies, including their future financing and organisation. Also, designing policy programmes to support regions is of course connected to wider economic policy and also (then national) regional and state-aid rules. Finally, the need to compensate or cushion spatial effects or Brexit via regional policy measures is to some extent intertwined with overall post-Brexit UK-EU arrangements. While it is too early to map out the spatial impacts of Brexit, changes to the status quo and particular redefining trade relations would certainly have localized effects, e.g. via exports or FDI.

For the EU27, given that Brexit may take place within the current MFF, the upcoming years may prompt the need for further discussions and revisions in addition to the routine steps of EU budgetary planning. Currently, it seems rather unlikely that the UK is going to trigger Art.50 until the end of the year, so the upcoming mid-term budgetary review might be finished before the timeline on Brexit becomes clearer. Given current uncertainties about the timeline and circumstances, the regular mid-term review scheduled for the end of 2016 cannot fully account for changes that may become necessary due to Brexit, even when only considering the time period until 2020. Nevertheless, the "Brexit shock" could result in discussions about spending levels and priorities for the next years. The core focus on "jobs, growth, and competitiveness" is unlikely to change but there might be greater emphasis to focus on issues such as reducing unemployment and strengthening measures to speed convergence.

In addition, an indirect effect of Brexit may well stimulate the discussion about the design and effectiveness of EU regional transfers all the more given that Brexit would also result in a lower total budget. This ranges from the use of promotional instruments (use of grants and/or other financial instruments for support), strategies to combine support from different programmes and initiatives such as regional development funds and the European Fund for Strategic Investments (EFSI)[12], to prioritization of policy goals. Finally, there is also a connection to the more conceptional discussion about EMU reform and what mechanisms would be adequate to foster convergence and macroeconomic stabilisation.

[12] See Wruuck (2016) for further assessment.

EU Budgetary planning and Brexit – possible timeline 15



Source: Deutsche Bank Research

Finally, there is the issue of possible future cooperation between the EU27 and the UK after a Brexit. In principle, regional policy programmes already provide for some options here, e.g. as part of cross-border cooperation programmes. Beyond regional policy, EFTA EEA countries for example also participate in educational programmes like Erasmus+ and support international student mobility. In order to finance such initiatives, participating countries contribute to an additional budget, which is earmarked for the corresponding programmes. This suggests that if there is interest in further cooperation, there might be ways to realize it for programmes in the area of regional policy. However, the specific design and conditions will depend on the negotiations between both parties. Thus, local (economic) prospects are going to be intertwined with political developments in Europe.

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