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## Comparative Analysis of the Use of Financial Instruments – Regional Perspective

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**Abstract:**

**Purpose:** The aim of the article is to indicate how provinces in Poland support regional development with European Union money, especially with repayable instruments. The article poses the following research hypothesis – repayable financial instruments can effectively support regional development and previous experience is useful in the implementation of this support nowadays. The article first addresses the essence of EU cohesion politics and explains the essence and role of financial instruments and the type of support used in every region in Poland. A key element of the article is the calculation of the share of repayable instruments which will be used in the years 2021-2027, and indicating reason, and aims using that kind of support.

**Design/Methodology/Approach:** A critical analysis of the literature and an observational method using argumentation to support generalized theses were used to achieve the aim. In addition, the induction and deduction method, the comparison and generalization method, and the synthesis method were used.

**Findings:** The analysis carried out allowed the identification of the kind of support used in the Polish regions. The analysis has shown that the popularity of using repayable instruments is growing in voivodeships in Poland, although grants are popular as well.

**Practical Implications:** Implementation of EU money is very crucial for regional development however there is a visibly increasing share of financial instruments, which have many advantages and should be introduced at a larger scale. Those politics in FI case will generate the regional financial institutions and regional support system.

**Originality/Value:** The article presents the results of its own desk research and calculations. The issue presented has not previously been addressed in discussions published internationally.

**Keywords:** Grants, repayable financial instruments, regional development.

**JEL codes:** G21, G23, R11.

**Paper type:** Research article.

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## **1. Introduction**

One of the objectives of cohesion policy is to ensure the conditions for economic growth, prosperity, and social inclusion in the European Union. As a result of this policy, disparities in economic development should decrease, resulting in the realization of one of the three goals: convergence, competitiveness and employment, and territorial cooperation. The realization of these goals is possible thanks to the Structural Funds, which finance the indicated objectives of cohesion policy.

At the beginning of Poland's presence in the European Union, the dominant form of increasing the economic condition of regions was non-refundable subsidies, which proved popular in the Polish reality.

However, with the change of policies and rules for supporting regional development, repayable support began to be introduced slowly in some regions and to a small extent, which, in addition to grants, was supposed to intensify development.

Nowadays repayable support is an increasingly popular form of implementation of these goals in place of popular subsidies in the past. Despite the need to give back the money, this form is evaluated favorably, and thanks to revolving generate more benefits, because the money once transferred returns, multiplying the value of support and the number of beneficiaries.

Between 2007 and 2013, only five provinces in Poland decided to pilot repayable instruments. The situation was similar in other European Union countries. The leaders at the time were Belgium and Italy, which allocated 18.5% and 17.9% of the total allocation of EU funds to repayable support, respectively. In the next period, 2014-2020, the popularity of repayable support was greater, with all provinces planning repayable instruments in their operational programs.

In contrast, the European Union was led by the United Kingdom (22%), Greece and Italy (18%). The 2021-2027 period in terms of the form of support for regional development represents a breakthrough in European Union policy, due to the widespread use of repayable instruments.

In Poland, the share of repayable support in the form of financial instruments has increased from less than 2% (in the period 2007-2013) to 7.5% (2021-2027) and is applied at both regional and national levels. Initially, most of the funds were allocated to the development of the SME sector and to a small extent to the revitalization and urbanization of urban areas.

Now, in the 2021-2027 period, financial instruments will also be dedicated to

energy transformation and energy-efficient construction. Loans and guarantees dominate, as well as increasingly popular mixed instruments combining credit and subsidy.

## 2. Literature Review

The European Union, as an international organization consisting of countries at different levels of development and facing different economic, social, and political challenges, pursues policies aimed at the development of each member country. Facing different challenges, it has its own budget from which projects are financed to solve common problems, an active policy of regional development (Cristea *et al.*, 2022; Thalassinos and Berezkinova, 2013).

Countries, and regions that make up the EU are diverse in terms of development, and there are disparities between them (Boldrin *et al.*, 2001), so the main objective of this policy is to reduce differences in the development of countries and regions, to initiate measures aimed at increasing their competitiveness.

According to the European Union (Lisbon Strategy), regional policy is a policy of convergence, i.e., reducing differences between regions. Strengthening weaker regions and countries is supposed to be the way to increase the competitiveness and economic potential of the Union as a whole (Tomaszewicz, 2014; Antonescu, 2014). Objectives and tasks that increase convergence and competitiveness are implemented through structural funds, programs, and financial instruments (Sorychta-Wojczyk and Musioł-Urbańczyk, 2016).

The effects of measures are the subject of studies and evaluations since the beginning of the implementation of cohesion policy affecting the development of regions (Debowski, 2013), and economies of countries (Gorzelać, 2019; Thalassinos *et al.*, 2015). The results have not always been unequivocal and highlighted important aspects necessary for a positive correlation.

However, most prove the positive impact of EU funds, for example, on the labor market (Di Cataldo, 2017), and the overall health of regions (Fidrmuc *et al.*, 2023; Grima and Thalassinos, 2020), or social inclusion (Giua *et al.*, 2022; Pociovalisteanu and Thalassinos, 2009). Becker *et al.* (2012), on the other hand, despite an overall positive assessment, indicate that exceeding a certain ceiling of funds can cause negative effects. The impact of structural funds and cohesion policy on the development of provinces (NUTS 2) has also been analyzed.

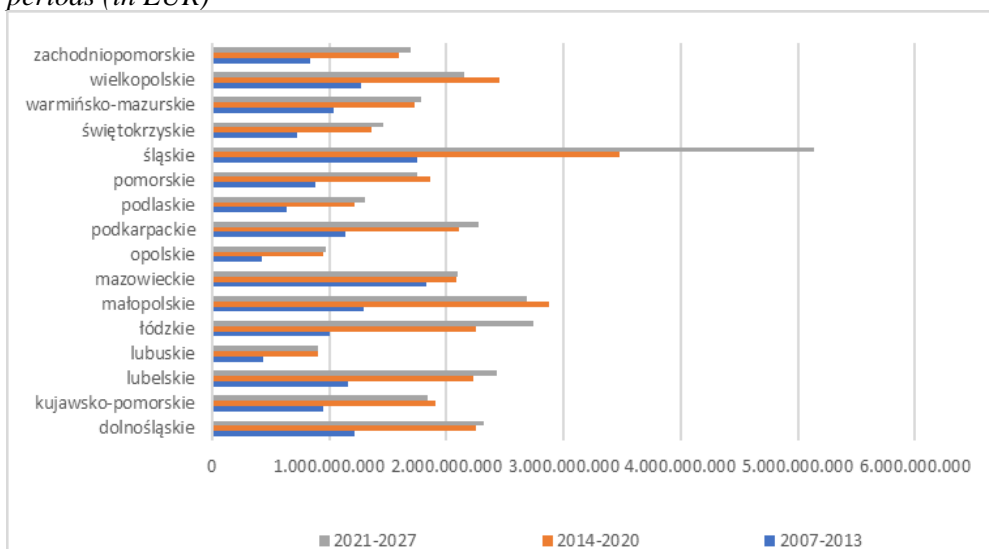
Scotti *et al.* (2022) proved that spending in the energy, research and development, and transport sectors stimulates higher GDP per capita growth, as well as produces lasting effects in the form of lower production costs, and increased innovation in recipient regions. Most of the new EU members positively assess the impact of EU money on their situation not only

economically, but also socially and culturally (Ahmed *et al.*, 2021).

### 3. Results

In Poland, each province has EU money, which it uses for the development of its region according to predetermined priorities. The allocation varies and is based on the level of development compared to the EU average (Figure 1).

**Figure 1.** Value of funds from the European Union by province in subsequent periods (in EUR)

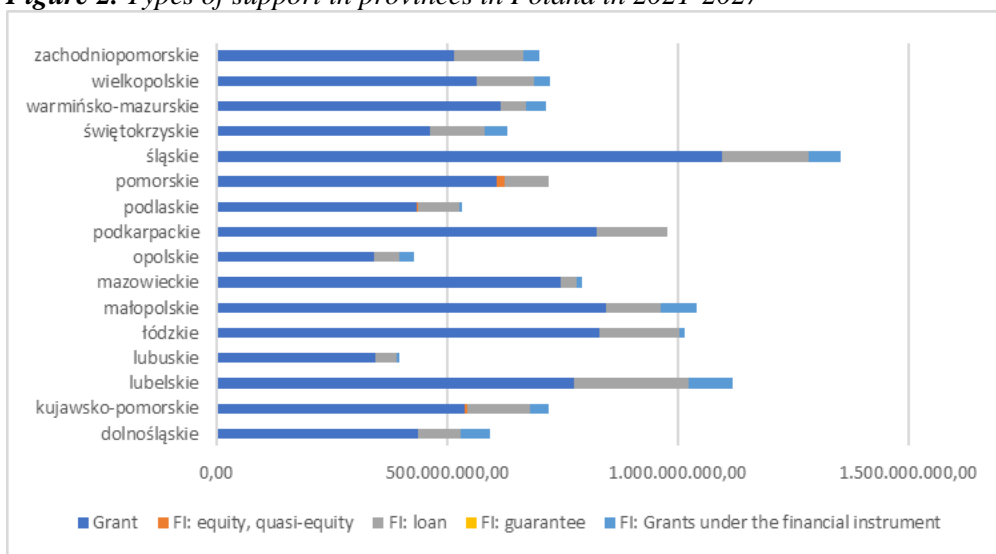


**Source:** Own calculations based on information from Voivodeships.

In the initial periods, regional repayable support predominated in supporting business development. In the next one, the emphasis was on their innovation, with a small share of financing for changing degraded areas and energy efficiency.

In the current period (2021-2027), in addition to supporting business innovation, the regions will support energy transformation and renewable energy sources, research and innovation, and integrated urban development

Financing of development policy goals is carried out in different ways. Initially, from 2007 to 2013, non-refundable grants dominated. In subsequent years, some countries began to innovate and use financial instruments in development policy (Zaharioaie, 2012), which in the period 2021-2021 will finance the sustainable development of regions, including in Poland (Figure 2).

**Figure 2.** Types of support in provinces in Poland in 2021-2027

**Source:** Ministry of Funds and Regional Policy.

Financial instruments under regional operational programs are an example of how commercial solutions popular in financial markets can be implemented at the level of public intervention. Financial instruments are supported with public funds in the form of loans, loan guarantees, or capital support programs for projects that would not have had a chance to be implemented without this support, which aim to overcome market failures experienced by micro, small, and medium-sized enterprises (Núñez Ferrer *et al.*, 2017; Rekkas, 2021; Brown and Lee, 2018).

Their task is to support cohesion policy with the simultaneous implementation of risk sharing and achieving objectives included in the development programs of member countries. The reorientation of the European Commission from grant instruments, toward repayable instruments in the effective use and management of structural funds was related to the possibility of obtaining much better economic and social effects.

The growing popularity of financial instruments in European Union policy is due to the benefits that can be achieved. Despite the high popularity of non-refundable grants among beneficiaries, repayable financial instruments have their advantages. Among those most often mentioned in the literature are (Cisilino and Licciardo, 2022; Wislade and Michie, 2018; Matshkalyan and Feher, 2017, Financial Instruments ..., 2014):

- revolving, which means the possibility of repeated use of funds, increasing the efficiency of the use of public funds and the possibility of previously set goals,

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- the maneuverability of funds, which results in the financing of better quality projects, investments,
  - the possibility of bridging market failures in access to capital (information asymmetry),
  - moving away from the culture of "subsidy dependence",
  - leverage through the involvement of private funds,
  - access to a wider range of financial services, and the experience of financial intermediaries.

The advantages of using financial instruments under the EU Structural Funds (ESIF) have been documented by Wislade *et al.* (2017), Nyikos and Laposa (2017), and Fi-Compass (Financial Needs in the Agriculture and Agri-Food Sectors..., (2020).

The value of repayable support in regional operational programs has increased compared to the years 2007-2013 and 2014-2020. Polish provinces use this form of financing for sustainable development to varying degrees. Most instruments will be used in the Lubelskie Voivodeship (44% of the allocation of funds under the European Funds for Lubelskie 2021-2027 program), the Świętokrzyskie Voivodeship (37%), the Lower Silesian and West Pomeranian Voivodeships (36%) and the Wielkopolskie Voivodeship (34%) (Figure 3).

These regions have recognized the advantages of revolving funds that can support the local economy for years. At the other extreme are the Mazowieckie<sup>2</sup> (6%), Lubuskie (15%), Warmian-Masurian (16%) and Subcarpathian (18%) provinces.

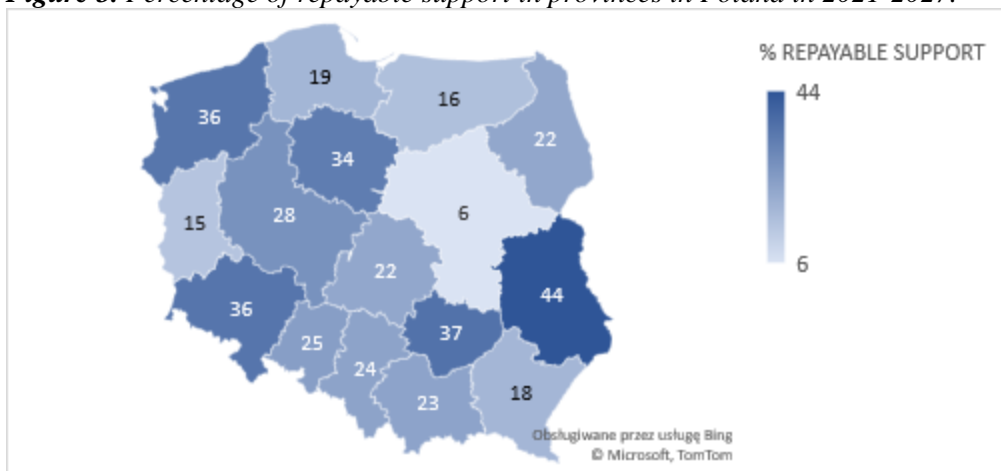
The financial instruments used in the regions in the 2021-2027 period are dominated by a loan and a repayable instrument combined with a grant, disbursed upon fulfillment of certain conditions. It will be used most often in supporting SME growth and competitiveness, energy efficiency and greenhouse gas reduction, and renewable energy accounting for less than 90% of the amounts allocated for repayable support in regional programs.

#### 4. Discussion

As presented above, the subject of the use of EU funds and their impact on beneficiaries is a popular one. Studies of their effectiveness indicated a positive impact on the competitiveness of enterprises first, then on their innovation, a positive impact on the labor market, and social inclusion. Absorption of EU funds among member countries is at varying levels and, according to Martin-Llaguno *et al.* (2022), depends, among other things, on the institutional efficiency of the country, the region, and the communication policy pursued in this regard.

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<sup>2</sup>Mazovia Province presents data for the city of Warsaw and the Mazovia region.

**Figure 3.** Percentage of repayable support in provinces in Poland in 2021-2027.

**Source:** Own calculations based on data of Ministry of Funds and Regional Policy.

However, not everyone believes that the convergence process is going well. According to Hapenciuca and Arionesei (2013), despite the fact that the Structural Funds are one of the main instruments of the EU to sustain regional development and reduce disparities between members, and regions, simple provision does not guarantee success, especially among new members. An important issue in their effective and efficient use is administrative capacity and the use of the learning effect.

Most of the research conducted has focused on non-repayable support in the form of grants, as this has dominated EU policy to date. The growing use of repayable support will certainly be studied in the future. The first analyses point to the greater effectiveness of repayable instruments that allow the same funds to be used repeatedly while involving private capital, which is impossible in the case of grants.

Projects financed by financial instruments should be characterized by profitability in order to repay at least partially the investment. Given the nature of investments financed by financial instruments, in justified cases, it is advisable to combine it with a different form of a grant, in the form of a success bonus.

Further detailed analysis would be needed to determine exactly the percentage of financial instruments and grants needed in each intervention. As an indicative benchmark, it can be considered that the grant component of many financial instruments/grant programs in the Member States should not exceed 40% of the overall investment, leaving the remaining part to be covered by financial instruments (The Potential for Investment ..., 2020).

## 5. Conclusions

Cohesion policy is yielding positive results. Regions, especially from Central and Eastern Europe, have caught up with the western part of Europe. Poland, since it has belonged to the EU, has effectively used the available funds. Initially, non-refundable grants prevailed, then in 2007-2013, the first provinces piloted repayable instruments for financing business competitiveness and revitalization of degraded areas.

In the following years, 2014-2020, the use of repayable instruments was greater, also in Poland at the regional level, support for the SME sector also prevailed. In 2021-2027, each province will use instruments to a different extent. In some, more than 30% of the money allocated to the regional operational program will be offered in repayable form.

Among the leaders are regions that were the first to use this form of support in 2007-2013. This shows that having gained the necessary and important experience, they have noticed the advantages and benefits achieved through this form of assistance.

Regions that were the first to implement financial instruments continue to use the funds allocated to them to support business development. The earmarked funds will work for the good of the region for many years, shaping regional financial institutions and the regional support system. Grants are needed and in many cases are the only form of financing, but repayable assistance also with incentive elements in the form of grants will be developed, and the funds allocated for this purpose will be used for the good of the region for many years.

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