European Cohesion Policy in Times of Fiscal Consolidation: A Comparison of Regions in Germany and Portugal

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By: Moritz Neujeffski, Moritz.neujeffski@wzb.eu, Berlin Social Science Center, Germany

Abstract:

The European cohesion policy (CP) is one of the most substantial expenditure items of the European budget. It is still considered the EU's most tangible form of solidarity by the European Commission (EC) as the CP's European Structural and Investment Funds (ESIF) redistribute financial resources from the economically stronger Member States to the EU's less developed regions. Yet, the cohesion policy has been transformed substantially in the aftermath of the European sovereign debt crisis. As part of the budget negotiations in 2013, the EC linked the policy area closer to the European Semester. However, while the compliance with the EU's stability and growth criteria has become a precondition for receiving ESIF funding, the new imperative also caused frictions with the CP's additionality principle, which demands a sufficient level of structural policy expenditure by regional and national governments to prevent substitution of domestic resources with EU funds. While power struggles between Member States and European institutions regarding the CP's alignment with the European Semester have been studied beforehand, it remains an open question how the European debt crisis has affected the concrete implementation of the EU structural funds within the European regions. This forms a crucial research gap, as the regional level plays an essential role in the cohesion policy architecture since it is here that the CP's social intentions are turned into concrete actions. This contribution, therefore, examines how the European debt crisis and the transformed CP regulations affected the implementation of the EU structural funds within the European regions. Based on a qualitative research approach, the paper contextualizes, examines and compares the ESIF implementation processes in two regions in Germany (Saxony-Anhalt and Thuringia) with two regions in Portugal (Centro and Norte). While the four regions differ in terms of economic development (more/less developed) and the degree of political autonomy (federal/centralized nation state), they have all been subject to far-reaching fiscal consolidation measures since 2007. By focusing on changes in CP funding modalities and spending objectives, the contribution finds a partial subordination of the EU fund implementation to regionally specific fiscal consolidation strategies. Both regional and national actors deploy two distinct strategies to align structural fund implementation with fiscal consolidation efforts: First, by expanding the usage of so-called financial instruments, which ensure financial returns to regional state budgets. Second, by attempting to substitute state funds with funding from the EU structural funds. In terms of the latter, regional policy actors tried to compensate those social groups that faced disproportionately large adverse effects due to the intended consolidation course by increasing their relative share of EU structural funds. In conclusion, the paper argues that the partial deployment of EU structural funds to safeguard austerity measures moved the policy area further away from its original intentions of reducing regional inequalities.

1. Introduction:

With a share of 32,5 % of 2014-2020 European budget, the European cohesion policy (CP) remains one of the most financially substantial policy areas of the European Union. Widely held to be the European Union's long-term "solidarity mechanism in action" (European Commission, 2021), the CP essentially redistributes financial resources from economically more developed Member States to the less developed regions of the European Union via the CP's five European Structural and Investment Funds (ESIF)[1]. Since its creation in 1988, the policy's overarching goals to strive for "reducing the differences existing between the various regions and mitigating the backwardness of the less favoured" (1957).

Yet, the cohesion policy has been transformed substantially in the aftermath of the European sovereign debt crisis. As part of the budget negotiations in 2013, the EC linked the policy area closer to the European Semester, introduced new reporting requirements and promoted new forms of financial instruments that rely on loans rather than the traditional grant approach.

Although the effects of the financial- and European debt crisis with regard to the welfare state in general (Lavinas 2018) and with regard to particular social policy regimes such as pension systems (Braun 2020; Rodrigues, Santos, and Teles 2018), infrastructure development (Singla, Shumberger, and Swindell 2019), health-care (Legido-Quigley et al. 2016) and social housing policies (Belotti 2021; Bohle 2018) have been studied quite extensively, crises effects on the European cohesion policy have received limited academic attention.

So far, critical examinations of the CP have observed increasing contradictions of demanding fiscal consolidation while maintaining the regional convergence approach (Hadjimichalis, 2019). Scholars attest a discursive shift from demanding "conversion" towards the aim of "regional competitiveness" (Czirfusz 2020). Others have examined the changing power dynamics at the EU level over the course of the European debt crisis. Mattia Casula (2021) and especially Felix Syrovatka (2022) have uncovered the power shift within the European Commission towards the DG ECFIN that demanded a stronger application of fiscal consolidation principles within the European Cohesion Policy. Furthermore, Souliotis and Alexandri (2016) showed how crucial aspects of policy-making which previously resided with regional administrative entities were scaled up to the European level over the course of the crisis.

These contributions have greatly advanced our understanding of how changing economic condition and actor coalitions have altered the cohesion policy and its governance system at the European level in various ways. However, it remains an open question how the European debt crisis has affected the concrete implementation of the EU structural funds within the European regions.

[1] These comprise the European Social Fund (ESF), The European Regional Development Fund (ERDF), the Cohesion Fund (CF)

The regional level, however, takes a unique role in the European cohesion policy, since regions, based on the CP's partnership principle, are important stakeholders in the strategizing and implementation process. It is at the regional level that that the CP's social intentions are turned into concrete actions.

To both examine common developments in cohesion policy across diverse institutional arrangements and differences with regard to changes to regional implementation strategies, this paper conducts a comparative case study of Saxony-Anhalt and Thuringia in Germany and the regions Norte and Centro in Portugal. The paper is structured along the following lines. The first section shortly presents the intention and function of the European cohesion policy and describes the main policy changes that the Commission and the Member States agreed upon for the 2014-2020 funding period. This contribution then continues by shortly describing the four case regions and presenting the main difficulties Germany and Portugal faced during the course of the European debt crisis. Third, the empirical part examines how the four regions have utilized the EU funding during the 2014-2020 funding period.

Besides comparing the changes to the overall implementation strategy, in terms of the geographic and thematic distribution of EU structural funds within each region, the paper also investigates concrete cases in which the regions used the funds in ways to consolidate their regional state budgets. To do so, the paper draws on two main data sources. I rely on the regional operational programs (OPs) - the main regional strategy descriptions - the regionalized **"**historic data on Structural funds" published by the European Commission[2] as well as regional beneficiary lists[3] to determine, how the regional implementation strategies have changed in terms of geographic distribution. In order to investigate concrete cases and strategies how policy-makers used the structural funds for fiscal consolidation efforts, I have conducted expert interviews with civil servants in the respective regions.

Ultimately, the contribution finds a partial subordination of the EU fund implementation to regionally specific fiscal consolidation strategies. Regional and national actors thereby deploy two distinct strategies to align structural fund implementation with fiscal consolidation efforts: First, by expanding the usage of so-called financial instruments, which ensure financial returns to regional state budgets. Second, by attempting to substitute state funds with funding from the EU structural funds. In regards to the second strategy, regional policy actors in Germany tried to compensate those social groups which faced disproportionately high adverse effects due to an intended consolidation

[2] The European Commission publishes and updates a list of datasets with A list with thematic distributions of funds per region for each funding period (2000-06,2007-13,2014-2020): https://ec.europa.eu/regional_policy/en/policy/evaluations/data-for-research/

[3] Since the funding period 2007-2013, regions are required to publish the lists of beneficiaries that have benefited from the various EU structural funds.

course by increasing their relative share of EU structural funds. In conclusion, the paper argues that the partial deployment of EU structural funds for safeguarding austerity measures moved the policy area further away from its original intentions of reducing regional inequalities.

2. Reforms of the European Cohesion Policy

With the crisis of Fordism in the mid-1970s and the subsequent conservative revolution, a new impetus grew for pushing the European project by expanding the European market. Yet, agreement to the Single European Act for establishing the European single market required convincing those Member States with less favourable economic conditions which did not expect to gain from competition-induced growth and efficiency gains.[4] Thus, if only Nixon could go to China, it required a socialist "veteran" to convincingly call for a Europe with a social dimension. As part of his attempt to bolster the Community's social policy, the Delors Commission reorganized the structural funds under one supra-national roof, establishing today's European cohesion policy in 1988. This went hand in hand with a strong increase of financial resources during the following decade.

Based on the principles of concentration, programming, partnership and additionality, the cohesion policy was established as a distinct, European redistributive mechanism to mitigate adverse market effects. Through the partnership principle, the cohesion policy established a complex multi-level system in which regional, national and supra-national institutions together with the social partners co-determine the design, implementations and monitoring of the structural funds.[5] While programming and concentration, demanded an efficient deployment of resources along policy goals and co-developed strategies, the additionality principle was introduced to regulate the relationship between EU investments and Member States regional policy investments. To function as a preferential treatment for less developed regions, structural fund expenditure should essentially "not result in a reduction of national structural expenditure in those regions but should be in *addition* to national public spending" (European Commission a).[6] As we will see in the empirical part, this principle came in conflict with the demands for fiscal consolidation during the European debt crisis.

The cohesion policy has however, been subject to far reaching changes since the 2007-2013 funding period. Faced with sluggish growth rates at the beginning of the 2000s, the EU MS adopted the Lisbon Strategy to turn Europe into the "most competitive and the most dynamic knowledge-

[4] Such prospects were advocated for example in the Padoa-Schioppa report (1983) and the Cecchini Report (1988).

[5] This can be interpreted as a shift from government to governance, in that "it promotes a change in governance from public steering of social processes to self-governing networks of public and private actors" (Hooghe, 1998, p. 460). The European Commission obtained the powers to review and approve the individual national plans and went from being a "a treasurer signing blank cheques" (Manzella and Mendez 2009, 12) to an agenda setting and gate-keeping agency.

[6] This includes the co-financing rates that regions or Member States always have to contribute to projects financed by structural funds (EC, 2017, p.8).

based economy in the world" (Lisbon strategy, 2000). The subsequent coupling of the cohesion policy with the Lisbon strategy in 2007 secured the concept of regional competitiveness a prominent place on the cohesion policy agenda and stipulated far reaching policy changes. For the first time, developed metropolitan areas such as Stuttgart or Munich also became eligible for funding.[7] This, was a major change to the original principle to concentrate CP spending on less developed regions. Secondly, through the so-called 'Lisbon-earmarking' mechanism, a certain threshold of funding had to be spent on projects that pursue predefined Lisbon objectives, targeting innovation, research and development or improving human capital, for example (Krieger-Boden 2016). This strategic turn shifted the focus towards investments into the knowledge-based economy (Bodirsky 2015) and partly away from infrastructures finance. Moreover, new partnership agreements between the European Commission, the Member States and regional authorities ensured that such conditionalities were incorporated in ex-ante national and regional spending strategies (Heinelt and Petzold 2017). Thus, the establishment but also the Lisbon-related policy reforms reveal, how strongly macro-economic developments shaped the regional development policy of the European Union. The financial crisis and the European debt crisis have been no exception to this.

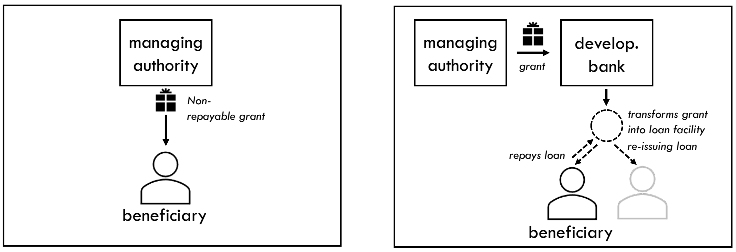
The cohesion policy came under severe political pressure during the European debt crisis and the disputes between crisis-ridden Member States and Northern economic power houses on how to respond to rising public debts (Matthijs and McNamara 2015). Quickly, two opposing political camps emerged during the politicized 2014-2020 EU budget negotiations in 2012, demanding opposing cohesion policy reforms. First, cohesion policy was deemed too expensive and ineffective by the net-contributing Member States of the cohesion policy. While the friends of better spending – the net-contributors to the EU budget –demanded strong contribution cuts and stronger conditionalities, the friends of cohesion – the net-beneficiaries – aimed at expanding the cohesion policy into a Keynesian fiscal stimulus instrument. Together with the Commission and the with support from the European Investment Bank (EIB), the friends of better spending succeeded. In summary, the Commission aligned the policy field more strongly to the Agenda 2020 strategy's goal of achieving "smart, sustainable, inclusive growth" and, on behalf of the DG ECFIN, integrated the cohesion policy into the European Semester (Syrovatka, 2022, p.303ff., Coman 2018). In essence, non-compliance with the Excessive Debt Procedure, could from now on, endanger MS to loose part of their cohesion policy allocations. This arguably turned the CP into "the 'conditional investment arm' of the EU's broader strategic orientations" (Heinelt and Petzold 2017) and led to the establishment of the Unit "Evaluation and European Semester" within DG REGIO.

Second, despite the economic turmoil of the crisis, the financial resources for the cohesion policy were not increased substantially. Moreover, the Commission started to advocate more

[7] This was made possible under the newly introduced objective of "regional competitiveness and employment".

strongly the usage of so-called financial instruments (FIs). Whereas structural fund resources are usually distributed in form of none-repayable grants, FIs rely on a loan structure. Throughout the financial crisis, the European Commission published two amendments and four guidance notes to encourage the take up of FIs by MS.[8]

Figure 1: Grant system versus the Financial Instrument system:



Although the Court of Auditors officially criticized the inefficiency of FIs and the increase in costs of PPP projects (2016, 2018), the EC and the EIB increased efforts to set up FI based programs and PPP-project as a solution to the European debt crisis. This established the regulatory leeway to experiment with new forms of cohesion policy programs involving more private actors and market-oriented development projects.

3. The role of Cohesion Policy in the Four Case Regions

The research design follows a maximum variance approach (Flyvbjerg, 2006) as Germany and Portugal differ strongly in their political system (federal, unitary) and economic development (leading, lagging).[9] Due to the latter, the cohesion policy has a different status in Germany and Portugal. While Germany has always been a net-contributing country to the cohesion policy, Portugal is a net beneficiary. All regions in the country have benefited strongly from the cohesion policy since Portugal's accession to the EU. Thus, in Portugal, the structural funds have been and still are one of the main resources for structural policies. Germany's total financial contributions to cohesion policy exceed the payments the regions receives for the seven-year period. A look at the regions, however, reveals a more differentiated picture. For the East German regions such as Saxony-Anhalt and Thuringia have been able to benefit from the structural funds to date.

Besides the different importance of structural funds, the two countries also differ in terms of their governance structures in the field of cohesion policy. Whereas Germany is a federal republic in which the sixteen federal states enjoy a high degree of legislative administrative competences, Portugal is highly centralized and represents a unitary state system. The cohesion policy is therefore shaped and implemented by different administrative actors within the two countries. In Germany, it is mainly the federal states that are responsible for the preparation of the Operational Programmes

[8] See for example Council regulation EC) No 284/2009;
[9] While the Purchasing Power Standard, (PPS) in 2016 Germany was 125% of the EU-27 average, the Portuguese one was only 78%.

and for the provision of co-financing[10]. Together with the Federal Ministry of Economics and Technology, the regions draw up the national strategy and have a major say in the negotiation of the Partnership Agreements.

In Portugal EU cohesion policy is coordinated at the national level by the Ministry of Planning. The five onshore regions which receive cohesion funding have an administrative character, while the two autonomous regions, the Azores and Madeira enjoy stronger political rights. Thus, the national level is most strongly involved within the administration of the cohesion policy, followed by the municipalities. The so-called Comissão de Coordenação e Desenvolvimento Regional (CCDRs) represent national planning bodies within the administrative regions (Caldas, Dollery, & Marques, 2018). They are responsible for designing the regional operational programs, monitoring the individual programs which are supported via the structural funds and engaging in promotional and administrative activities within the regions. This implies that in the case of Portugal, it is important to take the national level into account as well when analysing how the financial crisis has affected the implementation of the European cohesion policy in the regions.

Yet, besides these economic and governmental differences, the four case regions in Germany (Saxony-Anhalt, Thuringia) and Portugal (Norte and Centro) share three characteristics which make them particularly suitable for a comparative case study design. Firstly, the four regions have a similar economic composition in that they are characterized by large rural areas in which agricultural production and the primary sector in general plays the predominant role. In Centro and Norte these are the inland regions, while the costal areas – especially in Norte - represent the more urban (e.g. Porto) and industrialized (Braga, Guimarães) parts of the region. In Saxony-Anhalt and Thuringia, about 80% of the population lives in rural areas. However, most of the economic output in Saxony-Anhalt is generated in the industrial centres around Halle and Leipzig while in Thuringia industrial clusters exist in Jena and Erfurt. Moreover, in terms of the Purchasing Power Standard, (PPS) all four regions are below the EU average.

Table 1: Purchasing Power Standard per region

Region	PPS in 2016*
Portugal	**64%**
Norte	66%
Centro	68%
Germany	**135%**
Thuringia	86%
Saxony-Anhalt	89%

[10] Although national financial resources from the joint scheme for improving regional economic structures (GRW) have always played an important role for the provision of national co-financing means.

*Source: Eurostat; *PPS statistics after 2016 are only available as estimations for the German regions.*

Second, all four regions have been major recipients of EU cohesion funding since the 1990s. For Centro and Norte, the structural funds formed the most important source for engaging in structural development. During the 1990s both regions, used a high share of cohesion funding for improving the transportation system within and across the regions and to better connect the inland and the coastal areas. This was similar in Saxony-Anhalt and Thuringia where the first "mega-trend" – as an interview partner termed it – was to use ESI funds for economic development (60%) and infrastructure projects (40%). All four regions received a substantial increase of ESIF funding during the 2000-2006 and 2007-2013 funding period. For Saxony-Anhalt and Thuringia the financial resources. After the Eastern enlargement the two German regions already saw their financial resources declining while Norte

(9,7bn €) and Centro (7bn €.) experienced as second major increase in funding. Yet, also the financial means for Norte and Centro declined sharply in the following funding period. While Norte only faced a reduction of about two-thirds of its previous allocations (4.2bn €), Centro only obtained 2.6bn € for the 2014-2020 funding period. Thus, when talking to representatives and civil servants in the regions, most individuals stress the reduced role that the structural funds play for Portuguese structural investment policies.

Table 2: ESIF expenditure per region per funding period (in billion €)

Region / ESIF funding (bn €)	1994-99	2000-2006	2007-2013	2014-2020*
Norte	4.7	7.5	9.7	4.2
Centro	3.2	5.3	7.0	2.6
Thuringia	1.6	3.4	3.3	2.1
Saxony-Anhalt	1.9	4.1	3.6	2.5

*Data Source: Data from 1994 - 2013 stem from the Historic EU payments dataset published on the EU Cohesion data platform. Information for the most recent 2014-2020 funding period has been obtained through the ESF and ERDF operational programs. *While data for the previous funding periods represents actual expenditure data, information for the 2014-2020 funding period rely on planned expenditure data.*

Third, all four regions have been subject to far reaching fiscal consolidation policies, albeit in different contexts and for different reasons. Despite initial successes in transforming the economy in Saxony-Anhalt and Thuringia after reunification, an economic recession followed during the 2000s. Thus, the two regions experienced a toxic mix of economic decline, rising unemployment rates, declining tax revenues coupled with rising state budget debts. The pressure from breaching the EU deficit criteria in 2005/06, Gerhard Schröder's intensification of the conservative austerity project (Petzold,2020, Stützle 2013) and the constitutionalization of the debt brake in 2009 put fiscal consolidation on top of the agenda in Saxony-Anhalt but also in Thuringia. In case of the former, the region was put under the national excessive debt procedure in 2010. Subsequently Saxony-Anhalt engaged in strong public sector layoffs and investment cuts under the social democratic Minister of Finance.

Yet, while the austerity course in the two German regions was sparked most strongly by the accumulated debts of sluggish growth years during the 2000s, austerity measures in Portugal became introduced between 2010 and 2014 as a response to the financial crisis. Despite a strong economic recovery in 2010 and with mounting pressure from domestic banks (Stadheim 2020) and international financial institutions[11] the Portuguese, socialist government applied for an IMF- bailout-loan and the ESFS worth 78bn € in 2011. In turn, Portugal agreed to the Troika's economic adjustment program, which demanded a reduction of the from 9.8 percent of GDP in 2010 to 5.9 percent through drastic cuts in state expenditure through structural reforms. These reforms followed the previous competitiveness-enhancement approach of the Lisbon-Strategy and the Agenda 2020 a Commissioner Oliver Rehn "structural reforms to enhance competitiveness and boost growth and jobs"[12] demanded for Portugal (2012). To achieve this, the government foresaw spending cuts in the area of education and public health but also in terms of regional and local authorities, reduced public sector wages and wages, liberalized the national labour protection laws and privatized several state services which, among other things, resulted in a reduction in access, equity, and quality of health care (Petmesidou & Glatzer 2015). Although the country ended the Troika programme in 2014, Portugal remained under the Excessive Debt Procedure until 2017 (Murey, 2021). These austerity reforms must be understood as an intensified continuation of a long-term accumulation strategy oriented towards the export-oriented Nordic economies of the EU.

4. The European Debt Crisis and the Cohesion Policy Implementation in Portugal

Austerity politics in Portugal affected the institutional, strategic and financial dimension of the cohesion policy both directly and indirectly. Since the national level in Portugal plays an important part also in determining how the regions implement the structural funds, this contribution accounts for both the national and regional effects.

[11] The rating agency Moody reduced the Portuguese sovereign bond rating from a AA to A in the summer of 2010.

[12] As expressed in the country specific recommendations, such reforms aimed especially at "reducing labour costs, increasing flexibility and lowering entry barriers" (European Council, 2012, p.3).

Besides redundancies and the merging of CP administrative institutions[13], most importantly, on the Commission made a proposal in 2015 to suspend parts of the structural fund commitments to Portugal (and Spain), due to non-compliance with the stability and Growth pact. This was a direct result of the 2014-2020 CP policy reform which connected the structural funds to the European Semester[14]. For the Portuguese government and civil servants, this posed a serious threat, as structural fund remained an important source of investment for the Portuguese government. At the European level, potential reductions for Portugal (and Spain and France) evoked a political power struggle between the Commission, the Council and the European Parliament. Eventually, the Council decided not to impose sanctions on Portugal (Coman 2018, 551). This is a stark example of how the cohesion policy has been transformed into the "carrot" in the EU power struggle over economic policies.

Efforts to decrease the government deficit has also affected the cohesion policy in a second manner, as the government decreased funding for national structural and development policies. These efforts to cut national funding for regional and structural policies came into conflict with the cohesion policy's additionality principle, which demands a certain level of structural expenditure by the Member States themselves. Initially structural policy expenditure increased in Portugal (EC, 2013) as part of the anti-cyclical policy response after the crisis. Portugal allocated slightly less than 4% relative to its GDP in 2008 to public investments. Yet, public investments fell sharply to about 1.5% in the following years.[15] The 8th Commission's cohesion report critically remarked: "this implies that Member States most in need of the investment are the ones reducing it most" (2021, p.251). The reduction of public investments came into conflict with the additionality principle as Portugal did not meet the required levels of public expenditure as set out in the Partnership Agreement with the European Commission. As a response, the European Commission lowered the levels several times over the course of the European Debt crisis. Already in the previous funding period the Commission gave preference for fiscal consolidation efforts stating that the institution "ensured that the new

[13] The same happened to the CCDRCs in the statistical regions of Portugal. Here, too, jobs were cut in the course of the crisis (Interview #9).

[14] Through the adoption of regulation 1303/2013. Herein it states: "To ensure consistency with priorities established in the context of the European Semester, in preparing their Partnership Agreements, Member States shall plan the use of the ESI Funds taking into account the National Reform Programmes, where appropriate, and the most recent relevant country-specific recommendations adopted in accordance with Article 121(2) TFEU and relevant Council recommendations adopted in accordance with Article 148(4) TFEU in accordance with their respective roles and obligations. Member States, where necessary, shall also take into account relevant Council recommendations based on the Stability and Growth Pact and the economic adjustment programmes" (2013, p.412).

[15] Similar reductions in public investments occurred in most cohesion countries such as Spain but also Lithuania or Hungary.

levels of public spending to be maintained in 2007-13 are coherent with the policy conditionality of the Economic Adjustment Programmes [...]" (2017, p.5).[16]

These reduction of expenditure for public investments also affected the regions within Portugal. The economic adjustment program demanded that Portugal would "reduce transfers to local and regional authorities by at least EUR 175 million with a view to having this subsector contributing to fiscal consolidation" (2011, p.68). Concomitantly, with the reduction in national allocations to the regions and the municipalities, resources from the European structural funds grew in importance. As I was told in an interview with the CCDR in Norte, regarding the importance of the structural funds during the crisis years: "Tremendous! Because our regional funds were the main support for our infrastructures to work and to finance the small developments here and there" (interview #8). Essentially, the investments were used in a way to fill the financial gaps that the fiscal consolidation measures were creating. The Centro region replied in a similar way to the decrease of funding. Taking the risky road, the CCDR in Centro attempted to manage the situation via overbudgeting:

> "…we knew for sure from history because of these crisis circumstances, that there will be losses. I mean, some projects will not be able to be executed […] so we did overbooking. This means that you have more projects that have been approved than you can actually pay for. The beneficiaries knew that it's a conditional approval, meaning that they already go for the investment. And only if there are funds available, they will get reimbursed." (Interview #9)

Thus, also in the case of the Centro region the usage of structural funds was extended to cope with the insufficiency of national funding. But for the EU and the cohesion policy as a whole, the contradictions between reducing public deficits and maintaining pre-defined levels of public investments maintained. The European Commission solved this conundrum by giving more weight to the fiscal consolidation. After more than 30 years of practice, the Commission abandoned the additionality principle for the new 2021-2027 funding period.[17] Besides these strong effects of the European debt crisis on the financial base for conducting regional development policies, the adopted austerity politics also influence the concrete design of the operational programmes and the funding mechanisms through which the structural funds are dispersed within the regions. The following section takes a closer look at these substantive changes.

[17] DG REGIO Commissioner Ferreira wrote to the Italian government on 11.2.2021: "The new cohesion policy regulations for 2021-2027 do not include an explicit reference to the additionality principle, in contrast to previous programming periods." (p.1)

4.1. Competitiveness and Financial Instruments in the Area of Social Policy and Housing

Substantive effects of austerity policies on cohesion policy implementation can be traced back to the Memorandum of Understanding (MoU) and the Portuguese national cohesion strategy. First, the Troika suggested to maintain the "basic competitiveness approach" (p.) that the Portuguese government had already agreed upon with the Commission in the Partnership agreement and which has grown in importance since the Lisbon Strategy and the Agenda 2020. Thus, in line with the call to increase output of the export sector, the 2014-2020 Portuguese ESIF development strategy was termed "Competitiveness and Internationalization" (European Commission, 2021). In its reply to the MoU, Portugal stated that it was "exploring a new proposal to rationalise and redirect [funding] to the most productive segments of the economy" (2012, p.20). Compared with previous funding periods, such calls for increasing the focus on investments that target an increase of economic competitiveness replaced earlier efforts that target the reduction of regional disparities. Such renewed efforts to increase the focus on boosting competitiveness were also expressed in the regional operational programs of Centro and Norte. Here too, In the 2000-2006 period, the concept of convergence and the reduction of regional disparities still took primacy as an overarching goal to allocate ESIF investments. Yet, in 2014 a re-hierarchization took place. For example, in Centro OP it stated that: "the application of European funds […], will be oriented primarily towards the reinforcement of competitiveness of companies and the promotion of employment" (Centro, p.1). Social inclusion and cohesion were only mentioned as a secondary goal to attain (ibid.). To a similar degree, the Norte region promoted competitiveness as a major goal to attain as well. These also affected the geographic distribution of funding within the region. In Norte, funding for the greater Porto area increased by 10 percentage points between the 2000-2007 and 2014-2020 funding period, whereas resources for the rural and much less developed Douro region decreased from 8% to 3.8%.

The need to reduce government expenditure also affected the concrete funding mechanisms of the structural funds in Portugal. Traditionally, funds are dispersed as grants, meaning that they are none-repayable. One of the main objectives expressed in the Portugal 2014-2020 OP was to "promote private involvement that will allow a greater leverage of Structural funds allocations for the benefit of the Portuguese economy." (European Commission, 2021). The involvement of private actors, of course, creates the possibility to decrease the share of national means, while trying to keep with the necessary co-financing rates. The Troika had one direct recommendation, how to achieve this. In the 2014 MoU the institution advised Portugal to set up a national promotional bank, to increase the usage of financial instruments. Portugal had previously already offered the "setting up of a revolving mechanism to leverage EU structural funds" (2012, p.20). After obtaining approval of the Council of Ministers, Portugal established the Instituiçao Financeira de Desenvolvimento (IFD) in

2014 which eventually merged into the Banco Portuguese Formento (BPF). As a core institution, the BPF engaged in “streamlining and centralizing […] reimbursable part of the financial instruments of the EU structural funds for the 2014-2020 programming period” (IMF, p.12). In a case of institutional diffusion par excellence, the German KfW provided support and know-how for setting up the IFD.[18] While the institution currently focuses on offering preferential loans to SMEs, the bank also has plans to promote PPP projects in the area of infrastructure development in the future (interview #13).

Plans to increase the up-take of financial instruments were also rolled out throughout Centro and Norte. Interview partners in both regions explained that they planned to expand the resources for financial instruments and set up regional financial instrument programs:

> “I'm not a specialist on this topic, but what I was told is that at the beginning of the programing period, more than 1300 million euros were assigned to these financial instruments. The rationale is exactly […] the leverage effect because they are not grants, they are loans. So, actually, you get the funding back” (interview #9)

In Centro and Norte the share of FIs increased by 6 and 8 percentage points respectively to more than 20 %. Yet, at least in the Centro region the program did turn out to be unsuccessful, due to the severe lack of liquidity amongst potential investors. And, thus with the availability of grant-based programs, applications dropped. The situation in the Norte region was quite similar. The region teamed up with the Portuguese private banks to offer a financial instrument program to enterprises, “because we knew that they were decapitalized” (Interview #14). Yet, in Norte too the FI programs was too voluminous. Since, the private banks had to approve the enterprises for taking up loans, my interview partner speculated that, “probably the enterprises were not in a good situation to manage to have approved a loan”. (ibid.). A consequence in both regions was to combine the financial instruments with grants to establish more security for the companies. In this way, the regional CCDRs tried to increase the share of enterprises that were able to take-up loan-type instruments within the regions.

While the majority of funding for financial instruments went into support programs for SMEs, the government also expanded FI-programs into more traditional welfare state areas.

Coping with economic adjustments program, included far-reaching cuts to social policy expenditure (Hespanha, 2019, Casquilho-Martins, 2021). As a means for compensation, the government searched for market-conforming alternatives that could be combined with the EU structural funds. This connection was made explicit from actors from the social sector: “Due to strong austerity measures, social needs increased, and additional pressure was put on the limited public sector budget […] [i]t was in this context that the government of Portugal decided […] to promote

[18] Yet, due to unfavorable lending conditions, the IFD abstained from a global loan agreement with the German development bank (interview 14).

social innovation" (evpa, 2021) Together with the Gulbenkian foundation, the government set up the Portugal Inovacao Social program. The Inovacao Social used several financial instruments (FIs) to finance innovative projects that address specific social issues within the Portuguese regions. One of these is a Social Impact Bond (SIB), designed for investment projects worth more than 50.000 €. Financing instrument in which social services are privately pre-financed and publicly reimbursed in case of success. Funding for these SIBs came partly from the European Social Fund. These SIBs have been deployed in the field of health case (e.g. dementia treatment) or education.[19] SIBs have been criticized as a recent move in marketizing and financializing the third sector (Ogman 2016). Bound by the logic of FIs, SIBs hinge on the generate profits too. This finds expression in the Innovacao Social goals to "[s]trengthening the market for social investments by creating financing instruments" (website). It is further a direct response to the Commissions call to use more market-based instruments for financing national social infrastructures. What is important to contextualize here, is the fact that these social programs do not come on top of a fully functioning welfare state but are rather introduced at times of welfare state retrenchment, acting as a partial substitution. The Portuguese unions, therefore, vetoed against the program in the national cohesion policy advisory council as they perceived the program as a new experimentation with neoliberal welfare state models. A similar programme was set up in the area of housing policy which is presented in the following section. Here it is also clear how a stronger reliance on private financiers affects the geographical distribution of financial resources in the regions.

4.1.1 IFFRU: A Financial Instrument for Housing Redevelopment

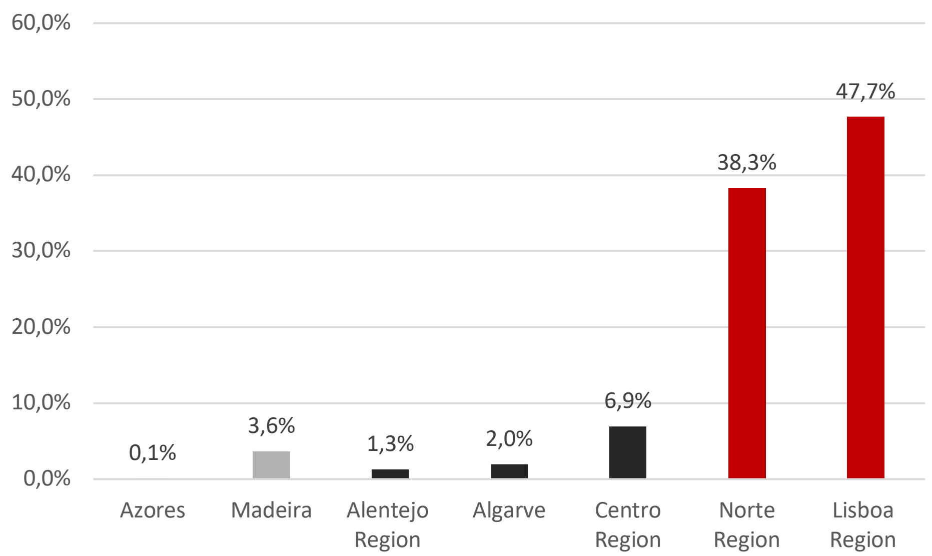
The small Portuguese housing development policy was not spared from fiscal consolidation efforts either. As Allegra et al. state in their historic assessment of housing policies in Portugal: "Indeed, the largest share of the remaining housing budget was destined to servicing the debt created by past operations, and primarily to subsidized mortgages" (Allegra et al. 2020, 2318). The Troika's economic reform packaged tight to the financial aid, demanded "a more market-based approach to housing issues" in combination with attracting more foreign capital investments (ibid.).

The Instrumento Financeiro para a Reabilitação e Revitalização Urbanas (IFFRU) can be considered one EU funded public housing instrument, which attempted to promote domestic and foreign investments in into the "revitalization of cities" (IFFRU,2022) in Portugal. The public tranches which consist of ESIF Portugal (102m. €), 20m.€ public contribution and 580m € by the EIB and CEB, thereby functions as funding for de-risking instrument which secures private investments by financial

[19] See for example the Khan Academy CENTRO: https://inovacaosocial.portugal2020.pt/project/khan-academy-centro/?doing_wp_cron=1664195653.6466860771179199218750

intermediaries (702m. €) and recipients (596m. €).[20] In times of austerity, this combination of public and private investments is attractive since it promises increased overall investments without burdening the public purse. Additionally, since the state investments represent preferential loans and not grants, the majority of state investments are expected to be repaid.

At the same time, the necessity of private investments came at a price. Steering capabilities of public institutions become delimited by the need for market demands, which can affect the geographic allocation of investments into housing but also the type of investments that become realized. In terms of the geographic distribution, IFFRU claims that the investment "covers the entire Portuguese territory" (IFFRUE, 2019). Yet, 72% (200) districts did not receive any IFFRU funding. These investments are highly unequally distributed throughout the Portuguese territory. As the Diagram 1 below reveals, 86% of investments went to the metropolitan area of Lisbon and the Norte region. In the latter, the vast majority of funding went into Porto; Portugal's second major urban center. Together, the three other mainland regions only obtained about 10% of IFFRU funding. Although Porto and Lisbon certainly represent large parts of the urban population in Portugal, the distribution of funding remains highly disproportionate.



This unequal geographic distribution is strongly driven by the private demand for investments. Similar to the regional financial instruments described above, the steering capabilities by the government decreased, as one of my interview partners critically reflected.

> "Especially in the beginning, we tried to advertise the program through more than 100 public sessions in municipalities. Every week we were at least in one or two different places in the country and in many countries with low density such as Braganza in the North […]" (Interview #19)

[20] According to the National Innovation Agency, "by September 2019, 151 funding contracts were signed with a total value of investment of € 479 million" (2021, p.49).

Moreover, the demand for secured IFFRU loans seems to be partly driven by the tourism boom in Lisbon and Porto. Thus, a substantial part of the loans went into the hotel industry or companies such as Up Down Lisbon LDA or Well-Senior II Investments that promote short term rentals. This practice however, accelerated rather than counteracts the current housing shortage, rapidly rising rents and displacement processes with which Porto and Lisbon[21] have been struggling since around 2014 (Allegra et al. 2020). Jover and Cocola-Gant regard the recent boom in tourism as a factor for "deepened inequalities between people and territories" (2022, p.10) in Portugal. The contribution that FIs can make to regional development and the reduction of regional inequalities was therefore viewed with skepticism by my interview partners. In conclusion, one interview partner assessed the future role of FIs as follows:

> "Of course, this will be an issue! When I go to our mayors and our municipality authorities, of course, they don't like to hear about that. They would like to receive money without having to pay it back. But in a certain way, this is how things will go now" (interview #8)

Thus, in Portugal FI projects had arguably a mixed success in terms of contributing to fiscal consolidation. The following section takes a closer look at the implementation of the structural funds in the two Eastern German regions, Saxony-Anhalt and Thuringia.

5. Cohesion policy implementation in Saxony-Anhalt and Thuringia:

As stated beforehand, in Germany the federal states entail strong autonomy in determining the course of the structural fund implementation. Thus, this section focusses predominately on changes at the regional level, in Saxony-Anhalt and Thuringia. Moreover, the impact of the financial crisis in Germany was much less severe than in Portugal. Nonetheless under Minister of Finance, Schäuble, the black zero and the and the reinstatement of the Maastricht criteria took primacy too.

In Saxony-Anhalt and Thuringia, too, a discursive strengthening of the idea of regional competitiveness can be seen in the Operational Programmes. [22] Whereas Saxony-Anhalt had already stopped framing structural fund investments in terms of achieving the German constitutional goal of attaining "equal living conditions" in the previous funding period, Thuringia stopped doing so from 2014-2020 onwards. Whereas in Thuringia explicit reference was previously made to possible points of friction between the promotion of competitiveness and cohesion, reference is now made to the fact that "the promotion within the framework of this OP is not oriented towards specific spatial requirements- The funding is geared towards strengthening regional competitiveness." (TH-OP, 2014,

[21] "In Lisbon, in particular, the urban pressure has become extremely intense due to the combined effect of a number of factors: the inflow of tourism and the development of a large industry of short-term rentals" (year,p.)

[22] In Saxony-Anhalt, for example, the majority of investments were henceforth legitimized either by increasing the "competitiveness of the economy in the region" (p.32), by removing "threats to the competitiveness of enterprises" (p.14) or specifically by strengthening the "competitiveness of SMEs" (130).

p.107). The greatest change compared to previous OPs is therefore also reflected in the spatial allocation of EU investment funds in the two German regions.

Even though Saxony-Anhalt considered "a spatially balanced and sustainable development of the European Union to be of central importance for spatial cohesion […]" (2021, p.125), this did not translate into a general prioritization of structurally weak and rural areas in the allocation of financial resources. To the contrary, in the 2000-06 funding period the rural area Hartz in Saxony-Anhalt still received the majority of ERDF funding (14%). Two funding periods later, Saxony-Anhalt already allocated 52,4% of the ERDF funding to large urban areas. In Saxony-Anhalt, these comprise the three cities Halle, Magdeburg and Dessau-Roßlau which together represent only 14.3% of the population.[23] [24] Consequently, the majority of the population who lives in rural and small towns (85.7%) received less than half of the ERDF funding (44.8%). Nor do the Magdeburg or Halle represent "regions with a particular need for structural interventions" (BMDV 2016, 11).

The prioritisation of urban areas was even more intensive in Thuringia. While the share of funding for the capital, Erfurt increased from 13% to 16%, funding for the economic stronghold, Jena, increased from 8% to 24%. More rural areas such as Sömmerda or Schmalkalden-Meiningen saw their relative share of funding declining.

In addition to promoting economic competition, the fiscal dimension of the neoliberal European political project was also given a place in Saxony-Anhalt's operational programme. Saxony-Anhalt declared that its overall ERDF strategy was in line with the European Semester's country-specific recommendation for Germany by contributing to "a growth-friendly fiscal policy […] ensuring a sound financial environment" (OP-SA, 2014, p.9). Thuringia, on the other hand, abstained from such direct references. In the following I will provide three examples in which the regional government of Saxony-Anhalt attempted to substitute regional state expenditures with financial resources from the ERDF with limited success.

5.1. Saxony-Anhalt: Budgetary replacement strategies in the area of primary, secondary and tertiary education and the cultural sector

In order to cope with the effects of the financial crisis Saxony-Anhalt intensified previous budget consolidation efforts, which the social-democratic Minister of Finance, had declared the region's main priority. Especially, the education system, the cultural sector but also the state administration faced the most severe budget cuts. Subsequently, Saxony-Anhalt experienced the largest

[23] Own calculations: In the year of 2020, the three cities Halle (237 865), Magdeburg (235 775), Dessau-Roßlau (79 354) were the only cities with more than 50.000 inhabitants in Saxony-Anhalt (Statistisches Landesamt b,2020, p.7). In 2020, counted 2,18 million inhabitants (ibid.).
[24] Thus whereas the allocations to the Hartz region decreased by 241 mio. Allocations to Magdeburg, Saxony-Anhalt's capital, increased by 241,3 mio. €.

demonstrations since the German reunification, driven by students, unions and cultural professionals.

The strategy of fund replacement comes to the fore most clearly regarding funding for higher education. As stated beforehand, Saxony-Anhalt presented the Agenda 2020 objective of improving the context for business sector and investing in promising projects of research institutions. However, prioritizing EU investments in higher education institutions stood in stark contrast to the region's own higher education policy. Saxony-Anhalt had reached an agreement with the presidents of the universities to cut expenditure by 24 million between 2013 and 2019. At the same time, EU investments in higher education increased by 22.3m € (8 percentage points) compared with the previous funding period (2006-2013). Thus, while EU expenditure for higher education increased, state funding in this area decreased.

Apart from the similarity in the amounts, there were also thematic overlaps in the use of the funds. Jens Bullerjahn, the Minister of Finance, had proposed to reduce state expenditure, especially for "construction projects and large-scale equipment" (Bullerjahn 2013, 8). Since the ERDF did not finance personnel at higher education institutions, ERDF-investments prioritized tangible R&D assets. The operational programme, therefore, stated: "The funding supports the construction, conversion and extension of R&D buildings at universities […] [and] equipment and instruments required for research"[25] (SA, 2021, p.33).

The government applied similar, yet, less successful strategies in terms of financing primary and secondary education facilities. However, the EU Commission's eligibility criteria for Germany did not foresee direct financing of school infrastructures as the Commission believed that no EU funds were needed to provide sufficient basic equipment for German schools (Interview #5). Therefore, the Ministry of Finance could not directly claim expenditure for school investments from DG REGIO. The solution was for the Ministry of Finance to claim EU funding for the state's schools under other, non-related expenditure headings, namely under the heading of Reducing greenhouse gas emissions by 20%. To put plans into action the government set up the Stark III program with a total investment volume of 327m. €.[26] According to one interview partner, Saxony-Anhalt started to use STARK III to finance the IT infrastructure of schools under the label of CO2 reductions. In addition, the government planned to finance entire new school buildings, for example, in Mansfeld, through the energy refurbishment programme. The fact that the STARK III funds were officially not earmarked for

[25] Funding for these expenditure items increased in particular in the 2014-2020 funding period. One of the ERDF lighting projects was, for example, the construction of a new science centre at the university of Magdeburg for "Dynamic Systems - Biosystems Engineering" (European Commission, 2014).

[26] To put the plans into action, the government set up the STARK III program with a total investment volume of 327m. €, which targeted educational facilities. STARK III aimed to deploy investments worth 86m €in rural areas via the EAFRD fund, while the other 241 m. € were supposed to be spent via the ERDF. STARK III was a flagship project launched by the Ministry of Finance.

such expenditure items was already pointed out in 2014 by the regional protest alliance "Schule vor Ort" (AG-SA, 2014). Thus, the showcase project STARK III quickly became a financial problem for Saxony-Anhalt. As one interview partner recalled it:

> "At some point, the EU found out about this after we had already spent a good three-digit million sum. And at that point, they said:" Folks, you're out of your minds!" […]”

Thus, while the European Commission recognized about 60% of expenditure, Saxony-Anhalt had to repay millions of euros to the Commission (Interview #5). Thus, while the fund replacement strategy was successful in the area of tertiary education, the government did not succeed in regard to replace state funds for primary and secondary education. As the last example will show, the federal state was also unable to assert itself in terms of increasing funding for cultural facilities.

In 2013 state funding for cultural facilities reached a low point. Saxony-Anhalt only committed 0.85% of the state budget compared to a previous average of 0.93% (LRH, 2013, p.24). In order to compensate for a proposed decrease of six million in annual funding for cultural institutions, the government advised cultural institutions to make more use of EU funding (MDR 2016). However, the cultural convention – the most important representative body of the cultural sector – pointed to severe limitations that the new EU guidelines entailed for cultural institutions. The Commission's assessments of the cultural institutions illustrate the central position supported cultural projects should be “beneficial in driving economic transformation towards knowledge-based economy” (DG REGIO 2021). Subsequently, the DG REGIO did not provide possibilities for funding theatres or orchestras, which represented those institutions in Saxony-Anhalt that were most affected by the austerity policy in the cultural sector. Saxony-Anhalt nonetheless initially argued for higher funding allocations for cultural institutions in the OP. According to one of my interview partners, this led to a major conflict between Saxony-Anhalt and the DG REGIO (Interview #4). The DG REGIO informed the managing authority in Saxony-Anhalt that if the funding for the cultural sector remained in the OP, the Commission would not approve the OP altogether. Ultimately, the plans for funding the cultural sectors had to be taken out of the OP to avoid further conflict with the EU Commission (ibid.).

5.2 Resistance to austerity in Thuringia?

In contrast to Saxony-Anhalt, the Thuringian government did not explicitly try to use the money from the EU Structural funds for budget consolidation purposes. Although my Interview partners agreed that in times of fiscal consolidation EU structural funds are high on demand, they denied that there were any explicit strategies that aimed at replacing regional expenditure via the funds. This is interesting, given that both the economic situation (high unemployment, low growth) and efforts to consolidate the state budget existed in both regions. My interview partners explained this different strategic orientation with reference to the different administrative structures in which the two federal states implement cohesion policy. Whereas Saxony-Anhalt had moved the structural funds administration unit to the Ministry of Finance in 2004, in Thuringia the unit remained with the Ministry of Economics. Apparently, such a re-structuring process was prevented by the resistance of the staff members themselves: “We have always been able to fend off such attempts so far successfully” (interview 15). Thus, while the Ministry of Finance in Thuringia recommended a spending strategy that did not place a heavy burden on the region's budget, there was no overall interference with how to implement the EU structural funds in Thuringia (Interview #18).

6. Conclusion

By conducting a comparative case study, this paper has examined how the European debt crisis and the subsequent fiscal consolidation measures have affected the European cohesion policy and specifically the national and regional implementation of the European structural funds. To do so, the paper traced policy changes in Norte and Centro region in Portugal and Saxony-Anhalt and Thuringia in Germany.

As the comparative analysis shows, fiscal consolidation affected the cohesion policy’s governance system, the funding modalities, and its strategic deployment. The differences between Germany and Portugal in terms of regional political autonomy (high/low), the importance of the structural funds (low/high) and the severity of the impact of the crisis (low/high) become apparent in the different responses to fiscal consolidation too. The sub-ordination of cohesion policy to the European Semester was used as a means of pressure on Portugal to comply with the SGP criteria. At the same time, the reductions in public investments put fiscal consolidation strategy into conflict with the cohesion policy’s additionality principle. Herein, the new prioritization of the neoliberal European austerity policy can be seen in the lowering of previously fixed expenditure levels for explicit compliance with the Troika requirements, as well as in the complete abolishment of the additionality principle for the current funding period (2021-2027).

In the context of a “fiscal crisis of the state” (Streeck, 2015), strategic realignments of ESI fund programs to consolidate public budgets gained attraction. Two different strategies were deployed in Germany and Portugal. Portugal attempted to align structural fund implementation with fiscal consolidation efforts by rolling out financial instrument (FI) programs in the regions and by strengthening the institutional capacities for FIs by setting up a national promotional bank. The FI induced ‘fiscalization’ (Petzold, 2018, p.70) of the EU’s regional development policy aimed at stabilizing a limited fiscal space through the involvement of additional private financial actors. Transforming EU grants into loan-instruments and blending private and public financial resources, lowers public expenditure and can create financial returns to national and regional state budgets. The analysis has also revealed that the stronger involvement of private actors decreased the steering capabilities of the state, as a high share of investments, e.g. for housing redevelopment, went into short-term rentals rather than into social housing projects.

While in the unitary state system of Portugal the FI programs were rolled out in both regions equally, regional responses to fiscal consolidation efforts were more heterogenous in the federal states of Thuringia and Saxony-Anhalt. Facing rising regional state debts in the aftermath of reunification, Saxony-Anhalt attempted to replace ordinary state expenditures with financial resources from the cohesion policy. By selectively increasing funding for EU expenditure items that targeted those social groups that expressed the toughest opposition against potential cuts of state funding, the government tried to appease social conflicts and maintain consent to continue the intensified fiscal consolidation agenda. In Thuringia, on the other hand, the administration rather attempted to resist such budgetary pressures.

Moreover, this regional case study has displayed the importance of analysing the implementation process to assess policy changes in the broader field of cohesion policy. Because it is at this stage of the policy process that the overarching ideas of cohesion policy – the reduction of regional disparities and the support of structurally weaker parts of the region – have experienced a qualitative change. In summary, the adaptations examined in this contribution, arguably, moved the EU's "bedrock of the anti-neoliberal programme"(Hooghe 1998, 459) further away from the original goal of achieving convergence as short-term fiscal policy pressures replaced long-term regional development strategies.

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