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Evaluation of EU Fund Dependency – Dead Weight Loss and Substitution Effect

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TERRITORIAL COHESION IN EUROPE

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Conceptualization

„Dead weight loss" effect: means that some enterprises funded through publicly supported measures would have obtained finance on the same terms even in the absence of state aid (EC, 2006).

„Substitution effect": is when an investment does not improve the output in national economic level (neither on European level) because of the "crowed out" effect in the national competition, nearly a "zero sum" game. (Béres, 2008)

(The only exceptions are when the supported company produces for export or creates new demand for its products, which is less common.)

Data and Methods

The online questionnaire was sent to all the enterprises registered at the regional chambers of commerce and industry in Hungary. (It is nearly 90% of the cc. 600,000 Hungarian operating companies.)

The data collection was made between 5th of January and 13th of February 2013.

We received 1351 responses, from which nearly 19% had to be eliminated due to uninterpretable or meaningless answers, so the final sample size was 1098.

Presumption

We regarded the *supplier activity* of an SME to multinational firms situated in Hungary as a kind of „indirect export”, since the majority of the multinational companies in Hungary are producing for export markets.

Results

The ***small and medium-sized enterprises are overrepresented in the sample group*** of EU-fund-winners (just like in the survey) compared to their share in the economy.

This is ***confirming the results of previous researches and evaluations*** (e.g. Béres 2008) that the majority of the winners of EU-funds are from among the most competitive enterprises (which are not the micro-enterprises).

Results

The average "dead weight effect" of the winners is 46%.

That of the companies which won (between 2004 and 2012) more than 40% subsidies as a percentage of their yearly turnover in 2012, this effect is just 24%.

There might be various explanations for this:

- either they are continuously applying for subsidies to "survive", because otherwise they would not be competitive and would disappear from the market;
- or they made one big or several small but sequential investments, which they would not have made without EU-subsidies.

Results

We have found a significant relationship between the **size of the company and the "dead weight loss" effect**:

- At micro-enterprises the average is 41.00%;
- at small enterprises 46.98%;
- while among medium-sized companies it is 58.33%.

and the ***ownership*** of the company:

- foreign owned enterprises generated an average of 63.89% "dead weight loss";
- SMEs with Hungarian majority ownership only 44.72%.

Results

The export activity (substitution effect) has a very significant relationship with "dead weight loss":

- companies with more than 10% export in their turnover produced a significantly higher "dead weight loss" average (53.70),
- than those with less than 10% export in the turnover (41.97).

(61% of the winners has less than 10% export in the turnover)

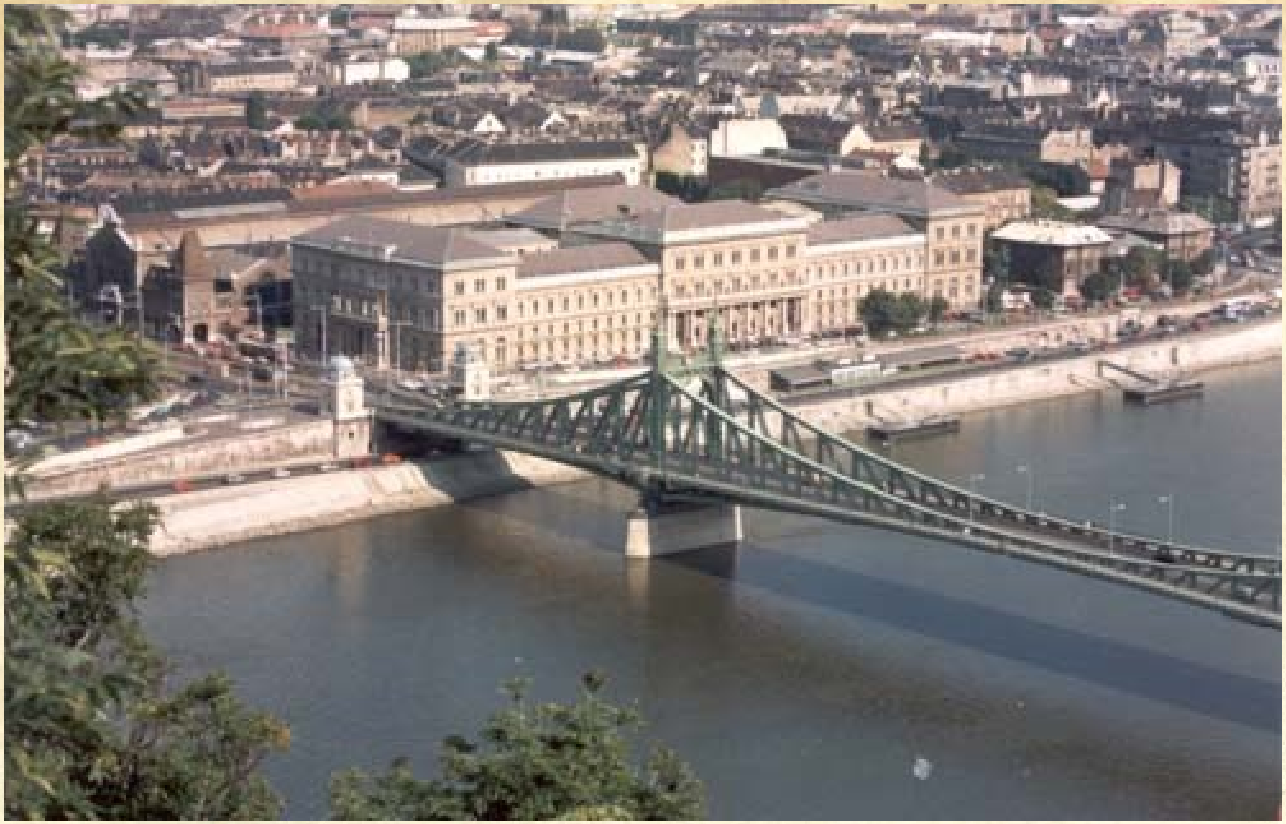
This is very controversial and highlights ***the negative correlation between "dead weight loss" and the „substitution effect".***

Policy suggestions

For the 2014-20 programming period the role of the non-refundable EU-grants should be decreased due to the high perverse effects and the low value added on national economic level.

The economic development should focus more on:

- *increasing access to finance* through refundable (JEREMIE type) EU-subsidies;
- *providing complex and targeted business and education services* to the SME sector on local (regional) ground (following international best practices e.g. the 2011 European Enterprise Award winner Barcelona Activa);
- *stimulating the internationalization* of the SME sector;
- *increasing „entrepreneurship" culture* in Hungary.



Thank You!

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