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# The impact of regional institutional quality on economic growth and resilience in the EU


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## Abstract

Long-term divergences in economic growth and resilience across European regions remain a key challenge for EU economic convergence and the smooth functioning of the euro area economy. Regional institutional quality can play a key role in addressing these disparities. Convergence to the EU median could raise annual GDP per capita growth by 0.5 percentage points over the medium-term in regions with poor institutional governance. Additionally, regions with high quality institutions are more resilient to adverse shocks and have a lower incidence of crisis. The findings underline the importance of institutional reforms at the regional level to support sustainable growth and economic resilience across the EU.

*Disclaimer*: This policy brief is based on ECB Working Paper No. 3045. This paper should not be reported as representing the views of the European Central Bank (ECB). The views expressed are those of the authors only.

## Introduction

Economic disparities across EU regions remain wide and persistent. While some regions, for example in the Baltics, have enjoyed dynamic economic growth, others, such as parts of Italy or Spain, continue to lag behind. Significant growth asymmetries exist also within individual European countries, resulting in overall mixed evidence of real convergence at the regional level in the EU (European Commission, 2024). These divergences complicate the transmission of common monetary policy in the euro area and have hindered economic resilience in the face of large adverse shocks, such as the COVID pandemic, the energy crisis or the increasing geoeconomic fragmentation.

This column, based on ECB Working Paper No. 3045, argues that differences in the quality of regional governance play a crucial role in explaining these disparities. High-quality institutions foster environments conducive to investment, innovation, and economic resilience. Conversely, weak institutions, marked by inefficiencies in public administration, corruption, or lack of impartiality, can stifle growth and increase vulnerability to shocks.

## What we study

We use different vintages of the European Quality of Government Index (EQI), which is based on a large citizen survey about perceptions and experiences with corruption, and impartiality and quality of public service delivery (Charron et al 2014, 2015, 2019, 2021). The EQI provides a detailed and harmonised indicator of institutional quality at regional level (NUTS1 or NUTS2) across 27 EU Member States.

The analysis draws on a panel dataset of 207 regions within the EU between 2010 and 2021. We estimate fixed-effects panel regressions, controlling for standard growth determinants such as GDP per capita, EU funds, employment rates, education levels, infrastructure density, and fiscal balance. We also apply robustness checks including instrumental variable approaches to address potential endogeneity in the relationship between institutional quality and economic growth.

## Institutional quality matters for medium-term growth

Our main result shows a clear and robust positive relationship between regional institutional quality and GDP per capita growth over a four-year horizon. This effect is not uniform across regions: it is particularly pronounced in low-income regions, highlighting the critical role of governance in enabling convergence (Figure 1). Interestingly, the information content of regional institutional quality for growth unfolds primarily over the medium term (three to four years). This suggests that the benefits of stronger institutions, such as improved innovation ecosystems, better public service delivery, and greater investor confidence, take time to materialise.

To illustrate the economic potential of institutional improvements, we simulate a scenario in which regions with low institutional quality converge to the EU median. Our estimations suggest that annual GDP per capita growth could increase by 0.5 percentage points over four years in these regions. In some regions in Romania, Bulgaria, Hungary, Greece, and Southern Italy, the gains could be even higher, reaching one percentage points annually (Figure 2).

**Figure 1.** Impact of an improvement of 0.1 in institutional quality on GDP per capita growth

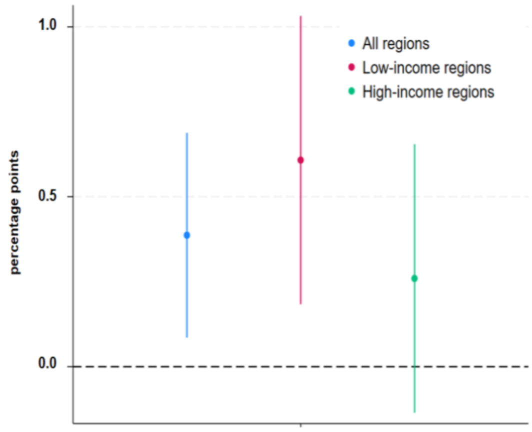
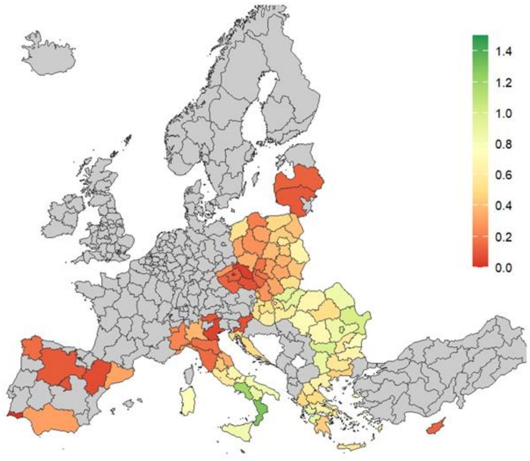



**Figure 2.** Annual GDP per capita increase in percentage points over 4 years from an improvement of institutional quality to the EU median




Source: Filip and Setzer (2025)

Notes: Left hand side chart: The dots represent the coefficients, and the lines represent the 90% confidence interval. Low-income (high-income) regions are those below (above) the median of GDP per capita in 2010. The quality of institutions indicator is scaled from 0 to 1.

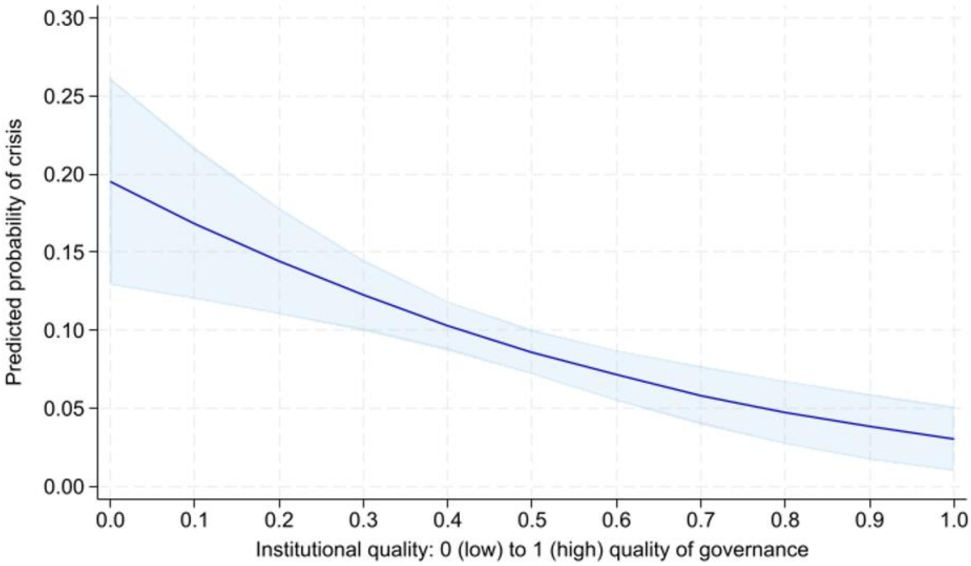
## Good governance enhances resilience to shocks

In addition to supporting economic growth, institutional quality plays a key role in enhancing economic resilience. Following Sondermann (2018), we assess resilience in two ways:

1. Response to common shocks, defined as correlations between a region's output change and a common shock.
2. Crisis likelihood, i.e. the probability of experiencing a severe economic contraction -defined as falling into the bottom decile of regional growth outcomes.

On both metrics, regions with better institutional governance perform better. First, they better withstand the negative effects of macroeconomic shocks on income growth. For instance, during the COVID-19 pandemic, regions with weaker institutions experienced an additional 4 percentage points drop in GDP per capita compared to the top-performing regions in terms of governance quality. Second, regions with better institutional governance are significantly less likely to undergo severe downturns -the probability of entering a deep crisis is three times lower than in regions with poor governance s (Figure 3).

**Figure 3.** Probability of strong decline in GDP per capita growth at different levels of institutional quality




Source: Filip and Setzer (2025)

Notes: The light blue shaded area represents the 95% confidence interval.

## Unlocking economic growth and resilience through better institutions

Our findings yield several policy messages. First, reforms aimed at enhancing governance should be central to cohesion strategies. Although institutional responsibilities vary depending on the degree of centralisation in each Member State, regional authorities often play a key role in shaping and implementing institutional reforms. Specifically, policies to reduce bureaucracy of public services, address the growing urban-rural divide, promote sustainable urban development, support the integration and inclusion of vulnerable and disadvantaged people, or improve the functioning of diverse neighbourhoods could create a more conducive environment for sustainable economic growth. These efforts would help ensure that all regions in the EU have the opportunity to thrive. The greatest gains from institutional improvements are in low-income regions. Support for administrative capacity-building in these areas should be prioritised. This approach aligns with broader goals of reducing regional disparities and promoting sustainable growth in the EU.

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