

February 2019

CESEE Research Update

Foreign Research Division

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The CESEE Research Update is released quarterly by the Foreign Research Division of the Oesterreichische Nationalbank (OeNB). The aim of this newsletter is to inform readers about OeNB analysis and research output on Central, Eastern and Southeastern Europe (CESEE) as well as past and forthcoming CESEE-related events.

Foreign Research Division
OeNB

Highlight of this Issue

Conference on European Economic Integration 2018 – snapshot

On November 26 and 27, 2018, more than 300 experts from national and international institutions (including the EBRD, EIB, European Commission, IMF, World Bank), central banks (including the ECB), academia, think tanks and the corporate sector, hailing from some 25 countries, came together in Vienna to discuss how economic and social cohesion in Europe can best be promoted and financed. Against the backdrop of Austria's EU Presidency, the OeNB's Conference on European Economic Integration (CEEI) put exploring ways to advance and fund the catching-up of economies in CESEE, the euro area and the EU front and center.

Following opening remarks by OeNB Governor Ewald Nowotny and a welcome address by Austrian Finance Minister Hartwig Löger, Benoît Cœuré, Member of the Executive Board of the ECB, pointed out that convergence in CESEE has stalled since the 2008 outbreak of the financial crisis – the significant improvement of living standards in the region over the past 30 years notwithstanding. In the face of digitalization and automation, the CESEE countries should therefore reconsider their growth model and step up innovations. The EU, in turn, should strengthen the Single Market, building a digital market, and deepen the capital markets union to complement funding by banks.



The role of monetary policy and central banks in catching-up took center stage in a panel discussion CEEI host Nowotny moderated with fellow central bank governors from Macedonia (Anita Angelovska Bezhoska), Romania (Governor Mugur Isărescu) and Bulgaria (Dimitar Radev). Making a case for continuous and real convergence, the panelists also pointed out that monetary policy with its focus on ensuring stability cannot be a substitute for structural, institutional and fiscal reforms.



Isabel Schnabel, Professor at the University of Bonn and Member of the German Council of Economic Experts, and Athanasios Orphanides, Professor at the MIT Sloan School of Management, presented what they consider preconditions for cohesion among states in a session, chaired by OeNB Executive Director Peter Mooslechner, dedicated to this important ingredient of the EU and euro area alike. Arguing that resolving financial issues is key to stabilizing monetary union, Schnabel identified five measures worth pushing: a credible bank resolution regime, a European deposit insurance scheme, an end to regulatory privileges for sovereign exposures, an integrated European banking market and well-developed European capital markets. Orphanides, in turn, deploring the lack of trust and goodwill – culminating in fragility – in the EU, contested both the EU's unanimity principle hampering much-needed reform and the ECB's hesitant policy entailing "lowflation" in the euro area.



Do we need new – including private – funding resources in the EU to advance convergence? Will EU budget funds have to be re-directed? These and similar questions were put to Michael Erhart from the European Commission, Margit Schratzenstaller-Altzinger of the Austrian Institute of Economic Research (WIFO), Sándor Richter of wiiw and Stéphane Saurel of the European Investment Bank (EIB) by OeNB Director Doris Ritzberger-Grünwald, who chaired a session on the role of the EU budget. While the Commission representative highlighted the success of the European Fund for Strategic Investment (EFSI), introducing a new proposal that builds on EFSI to mobilize private funds, the WIFO expert, in her analysis of the EU's multiannual financial framework, urged the EU to step up its efforts to foster economic, social and environmental sustainability to better address the long-term challenges of regional disparities, demographics, inequality, migration, climate change and enlargement. The wiiw expert pleaded for financial instruments-based funding (leveraged by private funds) wherever feasible and improving the ownership and allocation of EU funding. Saurel likewise stressed the importance of attracting additional investment by guarantees, equity, risk sharing, loans and the like, at the same time highlighting better synergies in future EU/EIB financing vehicles.



The first day was rounded out by a dinner speech eloquently presented by Frank Elderson, Executive Director of De Nederlandsche Bank and Head of the recently created Central Banks and Supervisors Network for Greening the Financial System. The transition to a low-carbon economy requires tremendous amounts of investment, the bulk of which must come from the private sector. Central banks have a role in making these projects bankable, while raising the awareness of climate risks impacting financial stability. Elderson called on national governments, the European Commission and central banks to join forces to meet the climate targets the EU committed to in Paris in 2015.



With Jeffrey D. Sachs one of the most influential economists opened the second day of the CEEI 2018 with a live streamed keynote. In the face of rising – and hopefully transitory – anti-Brussels sentiment in today's Europe, Sachs underlined the importance of strengthening EU-wide institutions und initiatives, such as establishing EU-wide infrastructure (single European grid and energy system), conducting EU-wide research and development to be able to compete with the U.S.A. and China in particular (Europe could be in the lead for zero carbon transport for instance), harmonizing corporate income

taxation to end the race to the bottom, and aiming for more vigorous coordination with the EU's neighbors.



In the session on industrial policy and investment, OeNB Executive Director Kurt Pribil welcomed Ralph De Haas, Director of Research at the European Bank for Reconstruction and Development, and Tomáš Sláček from the OeNB. De Haas highlighted two structural trends in emerging Europe: early de-industrialization and early ageing. These call for both a skills and health upgrade of the domestic labor force, migrants as well as automation. Reflecting on the rather heterogeneous de- or re-industrialization patterns worldwide and a somewhat paradoxical situation with respect to industrial policy, Peneder argued that dynamic industrial policy should target the system's ability to evolve through innovation, investment, and competition and regulation. Sláček then presented findings on the structural investment needs in CESEE and the use of EU funds, concluding that the link between allocated resources and structural reforms should be strengthened.



Helene Schuberth, Head of Division at the OeNB, chaired a session exploring how the investment climate of host countries might be improved. Linda van Gelder of the World Bank pointed out three areas: macroeconomic

stability, the creation of markets by deepening economic integration, and investment in human capital. The latter is particularly relevant in the Western Balkans, which suffers from very low employment ratios, as many people search for better job opportunities abroad. In the context of EFSI financing, Irmfried Schwimann, Deputy Director-General at the European Commission, emphasized the fruitful cooperation with National Promotional Banks, and she also underlined the importance of transparent public procurement to boost investments. Andrew Watt, Deputy Director at the Macroeconomic Policy Institute, proposed various measures to tackle the problem of low investment activity, including transnational strategic investments, economic governance reforms and continuing the EU Investment Plan.

The concluding panel discussion on corporate investment across Europe was chaired by OeNB Vice Governor Andreas Ittner and comprised the following panelists: Andrea Diamanti of UniCredit S.p.A., Franz Hiesinger of Mayr-Melnhof Karton AG, Birgit Reiter-Braunwieser of the Austrian Business Agency and Lukas Stühlinger of oekostrom AG. The tenor of this debate

providing insight into corporate investment decision making was that while CESEE has yet to fully guarantee investment security and legal certainty, it continues to be an attractive market given comparative stability and lower labor costs.



More information:

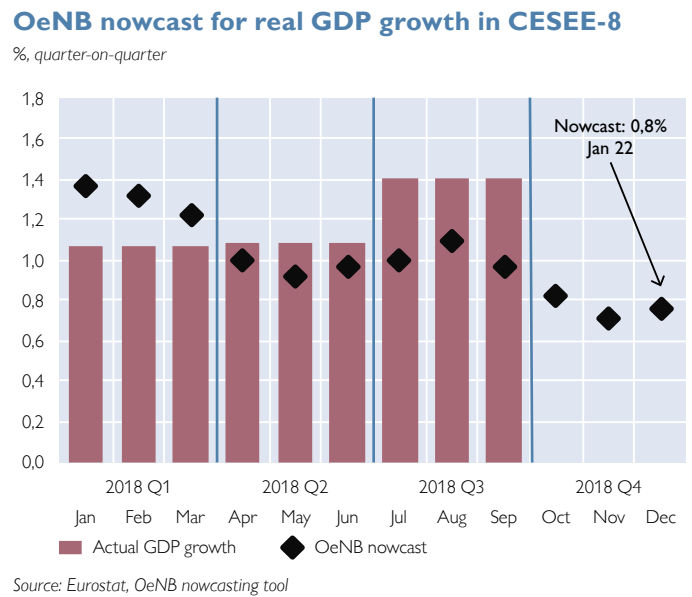
<https://www.oenb.at/en/Monetary-Policy/Central-Eastern-and-Southeastern-Europe--CESEE-/Conference-on-European-Economic-Integration-CEEI.html>

GDP growth in CESEE peaked in the 3rd quarter of 2018

2018 has been another year of strong growth in the CESEE EU Member states. In the third quarter, GDP growth peaked at 4.5% year on year in contrast to slowing dynamics in the euro area. With an increase of 5.7%, Poland surpassed the average by a margin, also Hungary and Slovenia recorded strong growth rates. Private consumption remained the most important driver of growth, benefitting from increasing credit growth, high growth of real wages and further improvements on the labor markets. Unemployment rates remain at historical lows while employment is rising steadily. In half of the countries employment rates are above the euro area average. Further, gross fixed capital formation profited from sound financing conditions, high orders, a record high capacity utilization rate and still improving sentiment indicators in the third quarter. Strong import demand coupled with weakening global trade dynamics implied a negative contribution from net exports. It remains to be seen whether strong wage growth has already translated into deteriorating price competitiveness of the CESEE economies.

Going forward, leading indicators point towards a flattening of growth dynamics. The average growth rate of industrial production is declining since January 2018 and amounted to 3.8% in November, a level last reached in December 2016. This is likely to be driven by weaker turnover in export markets. A similar development could be observed for retail trade turnover, while the construction sector continued to send positive signals: output grew by 11.8% in November 2018 in the CESEE region, Hungary, Poland and Slovenia even showed growth rates at around 20%. The economic sentiment indicator of the European Commission came in at 108.2 points in December 2018, posting a decline of two points compared to its peak in March 2018. A pronounced slowdown was also observed for the IHS-Markit Purchasing Manager Indices for Poland and the Czech Republic. In both countries the index dropped below 50, the mark which indicates an expansion. Increasing uncertainties in the external environment along with the economic slowdown in the euro area are likely to feed into lower growth rates in CESEE as well.

In line with this development, the OeNB's nowcast of January 2019 points towards a marked growth deceleration in the CESEE-8¹ countries compared to the unexpectedly strong third quarter of 2018.² Based on a set of carefully selected leading monthly indicators, the OeNB has developed a nowcasting tool for selected CESEE EU member states. The model is tailored to country-specific characteristics and makes use of forecast combinations. The GDP growth estimate for the 4th quarter 2018 stands at 0.8% (quarter on quarter). This would bring dynamics in CESEE more in line with recent developments in the euro area. Growth rates are expected to become somewhat more homogeneous across individual countries, as growth should decelerate especially in those countries, that reported extraordinarily strong growth figures in the 3rd quarter.



Visiting Researcher – Professor Francesco Zanetti



Francesco Zanetti visited the OeNB's Foreign Research Division from January 9 to 11, 2019.

He is an Associate Professor at the University of Oxford and also the editor of the prestigious journal "Oxford Bulletin of Economics and Statistics." Before joining the university, he worked as an economist and advisor at the Bank of England.

Francesco Zanetti's research interests cover monetary policy, news shocks, labor markets and fiscal policy. In his work, he tries to link structural and empirical models.

During his stay at the OeNB, Francesco Zanetti gave a presentation about state dependence in labor market fluctuations.

¹ CESEE-8: Bulgaria, Croatia, Czech Republic, Hungary, Poland, Romania, Slovakia, Slovenia.

² The OeNB's CESEE Nowcasting tool tracks economic activity of eight Central, Eastern and South-eastern European (CESEE) EU member countries and is up-dated on a monthly basis (at the 20th). Current quarterly GDP growth is estimated using a mix of models including simple AR-models, principal components models and bridge equations as well as model combinations thereof.

Save the Date

84th East Jour Fixe of the Oesterreichische Nationalbank (OeNB) and the Official Monetary and Financial Institutions Forum (OMFIF)

Long-run economic growth and development in CESEE: goals, priorities and implementation strategies

June 3, 2019

Oesterreichische Nationalbank (OeNB), Vienna

OeNB Kassensaal

The 84th East Jour Fixe focuses on long-run economic growth and development in Central, a very timely topic, given the high level of uncertainty surrounding the medium- to long-term growth outlook for the CESEE region. Potential growth estimates for many CESEE countries are currently low, putting into question the speed of convergence and raising concerns that CESEE might end up in a middle-income trap. Low potential growth also raises the question of whether the CESEE countries need a new and more sustainable growth model for the future.

Against this backdrop, the 84th East Jour Fixe will discuss the key goals, priorities and implementation strategies aimed at ensuring sustainable economic growth and development in CESEE in the long run. The keynote speech and session 1 will focus on current challenges for economic growth and development in the CESEE region, taking stock of past growth models and reflecting on future growth drivers. Session 2 will deal with the ecological sustainability of growth, discussing potential frameworks and opportunities for as well as potential obstacles to green growth in CESEE. The 84th East Jour Fixe will conclude with a panel on the relations between China and CESEE, focusing on the Belt and Road Initiative and its impact on trade and infrastructure investment.

Announcement

The OeNB's Conference Volume “Structural Reforms for Growth and Cohesion: Lessons and Challenges for CESEE Countries and a Modern Europe“

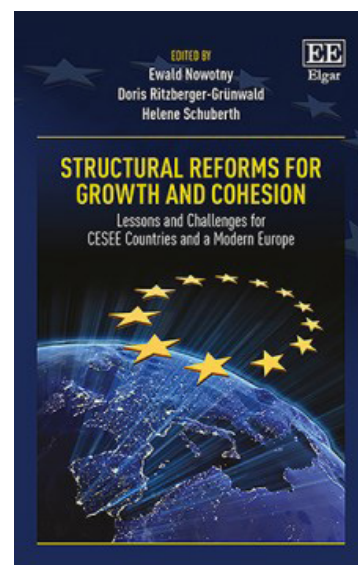
Edited by Ewald Nowotny, Governor, Doris Ritzberger-Grünwald, Director and Helene Schuberth, Head of Division, Oesterreichische Nationalbank, Austria

With formidable challenges facing Europe today, effective and well-designed structural reforms are key to shaping Europe's future. This book examines the achievements and failures of past structural policies so that new concepts can evolve to address remaining and newly emerging challenges with greater success.

Tangible policy advice is offered in the original contributions to this book, re-assessing past 'moments of truth' in European structural policy. The book focuses on the area of Central, Eastern and Southeastern Europe (CESEE), not least because this region has been largely successful through a profound transition period. Highlighting the social aspects and distributional effects of reforms that go beyond liberalization and deregulation, the book covers key issues facing Europe in the future, particularly those arising from technological innovation.

Structural Reforms for Growth and Cohesion will prove a useful book for academic researchers looking into European policy progress and reform. Indeed, it will also be a vital reference tool for policymakers seeking to deepen their understanding of the challenges facing a modern Europe and how these can be tackled.

<https://www.e-elgar.com/shop/structural-reforms-for-growth-and-cohesion>



Focus on European Economic Integration Q4/18 – latest issue [\(full version\)](#)

Recent economic developments and outlook

Developments in selected CESEE countries Economic activity still in full swing, but headwinds are increasing, *compiled by Josef Schreiner*

Outlook for selected CESEE countries CESEE-6 economic growth robust but moving sideways, Russia recovering only slowly, *compiled by Antje Hildebrandt*



Study

A simple approach to nowcasting GDP growth in CESEE economies, *Aleksandra Riedl, Julia Wörz*

Event wrap-ups

The OeNB's 82nd East Jour Fixe: Debt in Central, Eastern and Southeastern Europe: vulnerabilities and opportunities, *compiled by Katharina Allinger, Markus Eller, Mariya Hake*

The OeNB's 83rd East Jour Fixe: Catching the wind: current challenges and opportunities for European integration and convergence, *compiled by Katharina Allinger, Markus Eller*

23rd Global Economy Lecture: Caroline Freund on "Trade, inequality, and populism", *compiled by Maria Silgoner*

Upcoming Events

The following events are organized by the OeNB and cover CESEE relevant topics.

Please note that attendance is by invitation only. If you are interested in participating in one or more of the events, please send an e-mail to event-management@oenb.at.

June 3, 2019	84 th East Jour Fixe: “Long-run economic growth and development in Central, Eastern and Southeastern Europe (CESEE): Goals, priorities and implementation strategies” organized by the Oesterreichische Nationalbank (OeNB) in cooperation with the Official Monetary and Financial Institutions Forum (OMFIF)
September 12, 2019	85 th East Jour Fixe: “Ukraine: Political, economic and migration challenges” organized by the Oesterreichische Nationalbank (OeNB) in cooperation with the National Bank of Ukraine
November 25–26, 2019	Conference on European Economic Integration 2019: “Looking back on 30 years of transition – and looking 30 years ahead”
December 9–10, 2019	17 th ESCB Emerging Markets Workshop 2019 organized by the Oesterreichische Nationalbank

OeNB Courses at the Joint Vienna Institute (JVI) 2019

For further details see: [Course Schedule 2019](#)

January 14-17, 2019	Financial Stability and Supervisory Stress Testing for Banking Systems
January 21-25, 2019	Banking Supervision within the Basel Framework (in cooperation with Deutsche Bundesbank and JVI)
March 4-8, 2019	HR Issues and Compliance (in cooperation with the Deutsche Bundesbank)
March 11-15, 2019	Monetary Policy Implementation (in cooperation with Deutsche Bundesbank and JVI)
May 13-17, 2019	Challenges for Candidate and Potential Candidate Countries in the EU and EMU Accession Process (in cooperation with the Austrian Federal Ministry of Finance and ECB)
September 9-13, 2019	Integration in Europe: European Union and Eurasian Economic Union (in cooperation with the Austrian Federal Ministry of Finance)
October 14-18, 2019	Macrofinancial Stability in Central, Eastern and Southeastern Europe (in cooperation with the JVI)
November 4-6, 2019	Cash Circulation and Payment Systems in Austria
November 27-29, 2019	Financial Translation and Editing: New Skills for New Challenges