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# 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.

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## Highlight of this Issue

**A modern take on structural reforms – past and future challenges for CESEE and Europe at large: Conference on European Economic Integration (CEEI), November 20 and 21, 2017**

Structural reforms in Central, Eastern and Southeastern Europe (CESEE) and in Europe as a whole were the focus of this year's Conference on European Economic Integration (CEEI). Strategies for reform aimed at making Europe's labor, goods and capital markets fit for the future were discussed alongside the deep market reforms that the CESEE countries went through over the past decades.

The conference brought together high-ranking representatives of the central banks of the Czech Republic, Hungary, Poland, Slovakia and Slovenia as well as renowned speakers from international organizations, academia and the private sector: EBRD Chief Economist Sergei Guriev, Professor Sonja Puntscher Riekman from the University of Salzburg and Former Director of the European Commission's Directorate-General for Employment, Social Affairs and Inclusion, Georg Fischer, acted as keynote speakers.

## Main messages of the 2017 CEEI

Structural reforms are key to monetary policy transmission. Accommodative monetary policy, in turn, has supported fiscal measures (Jirí Rusnok). At the same time, structural reforms are necessary to mitigate the danger of misaligned incentives (potential asset bubbles) created by tjan Jazbec).



Europe is facing new social and economic challenges like globalization, digitization, demographic developments, inequality and divergence. In this context, Georg Fischer pointed out the “Pillar of Social Rights,” a collection of principles providing a vision for workers’ and civil rights at the European level. Social challenges need to be tackled with high priority to protect the people in the EU from the negative ramifications of globalization and to get their support for the necessary next steps of integration (Sonja Puntischer Riekmann).

Current imbalances are often blamed on institutions. While the need for reform in the EU is still urgent (Hubert Gabrisch), much has been achieved in recent years (László Csaba). The crisis provided the necessary impetus to go ahead with integration and implement a number of measures, such as strengthening the Stability and Growth Pact and creating the Single Supervisory Mechanism and the banking union (Puntischer Riekmann).

While structural reforms may promote growth and employment, they may also increase inequality in wealth, income and opportunity, as was the case in the transition economies (Sergei Guriev). Tradeoffs between growth and equality have been especially evident in social and labor market reforms, and less so in product market reforms (Orsetta Causa). In the wake of the global economic and financial crisis, the structure of the labor market in Europe has particularly affected wage growth.

Labor market dualities have weighed on wage growth, especially in CESEE (Paul Ramskogler).



The focus of structural reforms should also be on productivity-enhancing measures that foster amacha). Harmonized legal frameworks could improve funding for innovation in small economies and for small projects; in many cases, however, a shortage of human capital is the bigger obstacle to innovation (Johann Strobl, Tanja Tanayama).

The effectiveness of reforms is sometimes limited, in particular when it comes to anti-corruption measures. Greater transparency does not necessarily translate into less corruption; what is needed first and foremost is a change in governance structures (Alina Mungiu-Pippidi). Also, fears of losing out and weak trust in institutions are obstacles to reform progress (Klaus Masuch).

Emerging protectionism could affect the functioning of modern product markets that are linked through global value chains. However, a distinction must be made between nontariff trade barriers like, for instance,



antidumping lawsuits on the one hand and standardization and regulation, which could also be referred to as nontariff trade measures, on the other. The latter may actually foster trade and positively influence product quality, especially if they are coordinated at the international level (Robert Stehrer). That said, international standards are increasingly being set by corporations. Therefore, the public sector must implement structural reforms and create an adequate environment to ensure that profitable business models are socially and ecologically balanced and sustainable (Daria Taglioni).

A number of new instruments will be necessary to enhance the effectiveness of reforms but also to identify vulnerabilities in individual Member States (Lúcio Vinhas de Souza).

The contributions to the 2017 CEEI are available at <https://www.oenb.at/en/Monetary-Policy/Central--Eastern-and-Southeastern-Europe--CESEE-/Conference-on-European-Economic-Integration-CEEI.html>

## Joint CBK, EIB and OeNB conference on “Access to Finance, Bank Lending and the Banking Sectors in CESEE Countries”, Prishtina, November 14, 2017

On November 14, 2017, the Central Bank of the Republic of Kosovo (CBK) organized a conference in Prishtina on “Access to Finance, Bank Lending and the Banking Sectors in CESEE countries,” together with the European Investment Bank (EIB) and the Oesterreichische Nationalbank (OeNB).



Against this background, the conference provided a unique and rare opportunity for a far-reaching policy dialogue in Kosovo. Several key messages emerged from the day-long discussion:

- Economies in the CESEE region are developing favorably. Economic growth is back, inflation is moderate, employment is rising rapidly, financial sectors are broadly in a good shape and measures have been put in place to deal with high NPLs. However, some challenges remain. In particular, GDP growth remains below pre-crisis levels. Moreover, while robust growth is a necessary condition for convergence, it can not in itself address persisting structural challenges that several countries in the region are facing.
- There is a nonlinear, positive relationship between financial inclusion and the depth of the financial sector on the one hand and economic growth on the other;



The conference not only attracted a distinguished pool of speakers from Southeastern European central banks, international financial institutions (IFIs) and commercial banks but also a large local and international audience counting more than 150 people. Since it was the first time that the CBK organized a symposium of this size, the EIB and the OeNB were happy to share their know-how and experience with such events. In addition, the OeNB was represented at the conference by Elisabeth Beckmann, who gave a presentation on “Determinants of household credit access” (all Foreign Research Division, OeNB), who each chaired a panel discussion.



while the causality goes in both directions. Therefore, it is crucial for the countries in the region to deepen the financial market.

- Strong, credible and reliable institutions are of vital importance. Structural reforms and adjustment are necessary to deliver strong and transparent institutions, enhance investors' confidence, promote domestic savings, spur the development of local capital markets and improve access to finance. Special focus should be put on judicial efficiency and property rights.
- The currently strong economic performance provides a great window of opportunity to implement structural reforms and rebuild fiscal buffers. Unfortunately, this is not really happening. Fiscal policy is largely procyclical.
- Investment has suffered through the crisis, and a recovery in investment is necessary to boost competitiveness and productivity.
- Credit conditions in CESEE have been improving. Demand for credit, including its investment-related

components, has been increasing more strongly than supply. The strategic focus of cross-border banking groups has selectively increased, also backed by a higher profitability of CESEE operations.

- It is up to individual countries to develop a sense of ownership of reforms, to design and implement them, but also EU institutions and IFIs have a crucial role to play in assisting CESEE countries in promoting sound policies, supporting productive investment and enhancing institutional quality. The speakers were optimistic that irrespective of its current challenges the EU will continue to play this role as a crucial external anchor in the future.

The contributions and more information are available at <http://www.eib.org/infocentre/events/all/access-to-finance-and-banking-in-the-cesee-countries.htm>

## Presentation of the EBRD Transition Report 2017-18 – Sustaining growth



On January 31, 2018, Nathaniel Young, Principal Economist at the European Bank for Reconstruction and Development (EBRD), presented the main findings of the EBRD's

Transition Report 2017-18 on "Sustaining growth" at an event hosted by the Austrian Federal Ministry of Finance (BMF) in cooperation with OeNB. Harald Waiglein, Head of the BMF's Directorate General for Economic Policy, Financial Markets and Tariffs, opened the event and Konstantin Huber (BMF) chaired the panel discussion with Doris Ritzberger-Grünwald (OeNB) and Robert Stehrer (wiiw) that followed the presentation of the report.

After Waiglein's introductory remarks, Young outlined the key messages of this year's EBRD Transition Report which – in addition to its standard macroeconomic overview and the module on structural reforms – addresses some highly topical issues in four chapters.



In the first chapter, entitled "Beyond the middle-income trap," EBRD analysts find that middle-income countries typically experience weaker productivity growth and tend to have the most carbon-intensive production structures. Countries in this group find it difficult to switch from a growth model based on investment and the adoption of technologies to one involving innovation and the development of new technologies. That is why, inter alia, episodes of strong growth have historically

been difficult to sustain for more than a decade or two. The report argues that having achieved middle-income status, many economies in the EBRD region now need a new growth model. Prior to the crisis, economic growth in the region outperformed that in other emerging markets and was driven predominantly by rising productivity. Since the outbreak of the crisis, however, growth has slowed down as the contribution of total factor productivity has declined. While GDP growth in recent years has relied mainly on the accumulation of fixed capital, investment still lags far behind the levels seen in comparable economies.

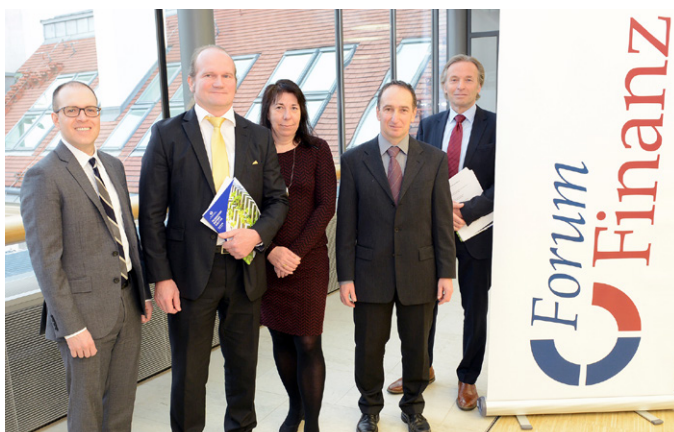
The second chapter, on “Firm dynamics and productivity,” looks at factors underlying productivity slowdowns and at the effectiveness of various policies in avoiding such slowdowns as countries transition from a low- to a high-income status. Within the Schumpeterian framework, this chapter analyzes how market incentives affect firm-level innovation and aggregate productivity growth. The report concludes that the economies in the EBRD region have disproportionately large numbers of small and non-innovative firms, which lag far behind larger firms in terms of productivity. Moreover, firms often fail to grow which translates into lower levels of aggregate productivity. And last but not least, while larger firms have achieved higher rates of productivity growth relative to their counterparts in developed economies, smaller firms have not caught up to the same extent. Against this background, productivity growth has to be supported by e.g. increasing cross-border integration, the integration into global value chains and the quality of economic institutions.

Young then moved on to discuss the third chapter, which deals with “Infrastructure and growth.” He stressed that most of the countries in the EBRD region have basic infrastructure. However, there is room for improvement in terms of sanitation and energy supply in poorer countries, and regarding broadband internet access in most of the region. Moreover, firms in many countries regard poor transport infrastructure as a major constraint on their business. EBRD economists thus estimate that infrastructure investment totaling EUR 1.9 trillion – equivalent to 9% of the region’s GDP – will be needed over the next five years. However, as the region is highly heterogeneous, infrastructure investment programs should be designed in the context of the relevant

country’s needs, taking account of the complementarity between infrastructure sectors.

The EBRD’s principal economist closed his presentation by talking about the report’s fourth chapter on “Green growth.” While greenhouse gas emissions have fallen in the region since the 1990s, they remain above levels observed in comparable emerging markets. Moreover, declines in emissions have been driven mainly by improvements in energy efficiency rather than by reductions in the carbon intensity of energy production. Therefore, stronger policies are required to put the region’s economies on the path to green growth, starting with the elimination of energy subsidies which distort incentives. Transition to green economies will be especially challenging for major exporters of fossil fuels. Yet, other parts of the EBRD region are relatively well placed to enjoy success in a low-carbon economy. According to Young, equity instruments are better suited to supporting green investment, while banks tend to provide funding for mature, older technology. As a result, rising importance of stock markets relative to bank credit is associated with declines in pollution.

Doris Ritzberger-Grünwald, Director of the OeNB’s Economic Analysis and Research Department, divided her discussion of the 2017 Transition Report in two parts. While appreciating its high quality and comprehensiveness, she went over it with a fine-tooth comb and challenged some of its statements. In particular, she was rather skeptical about its explanation for the decline in total factor productivity in the EBRD region and about the measurement of the investment gap. In her view, the latter is subject to high uncertainty. She also pointed out that some of the hypotheses put forward in the report lack convincing evidence and should be better substantiated. In the second part of her discussion, she presented some of the OeNB’s products and research results complementing the 2017 Transition Report. Robert Stehrer, Scientific Director of The Vienna Institute for International Economic Studies (wiiw), subsequently acknowledged the report’s broad coverage and perspective – including social and environmental aspects. He supported one of the main messages according to which it is crucial for the countries in the region to find a sustainable and balanced growth path. He extended, inter alia, Ritzberger-Grünwald’s critical point on total factor productivity and wrapped up by



pointing out one issue that had not been mentioned so far, namely that the EBRD had updated its methodology

of assessing the transition concept so that it should now better capture countries' development toward sustainable market economies.

The ensuing general discussion centered, inter alia, on the EBRD's policy response to countries' incapability to generate their own innovative growth, on the link between the financial sector's post-crisis recovery and the escape from the middle-income trap, on the implications of the middle-income trap for the likelihood of emigration and brain-drain as well as on the unclear relationship between the middle-income-trap and the global economic crisis.

[Report](#)

## Focus on European Economic Integration Q4/17 – latest issue [\(full version\)](#)

### Recent economic developments and outlook

Developments in selected CESEE countries - Strongest momentum in years, compiled by Schreiner, J.

Outlook for selected CESEE countries - Surprisingly strong rebound in CESEE-6, continued moderate growth in Russia, compiled by Hildebrandt, A.



### Studies

Migration intentions in CESEE – a descriptive analysis, Raggl, A. K.

The New Silk Road, part II: implications for Europe, Barisitz, S., Radzyner, A.

### Event wrap-ups

The OeNB's 81<sup>st</sup> East Jour Fixe: Nonperforming loans in CESEE – macroeconomic dimension and resolution strategies, compiled by Hildebrandt, A., Lahnsteiner, M.

22<sup>nd</sup> Global Economy Lecture: David Dorn on “The rise of machines – how computers have changed work”, compiled by Silgoner, M.

### Announcement

The OeNB's Conference Volume “Structural Reforms for Growth and Cohesion: Lessons and Challenges for CESEE Countries and a Modern Europe” will be published by Edward Elgar in fall 2018.

## Call for Applications: Visiting Research Program



The Oesterreichische Nationalbank (OeNB) invites applications from external researchers (EU or Swiss nationals) for participation in a Visiting Research Program established by the OeNB's Economic Analysis and Research Department. The purpose of this program is to enhance cooperation with members of academic and research institutions (preferably postdoc) who work in the fields of macroeconomics, international economics or financial economics and/or with a regional focus on Central, Eastern and Southeastern Europe.

The OeNB offers a stimulating and professional research environment in close proximity to the policymaking process. Visiting researchers are expected to collaborate with the OeNB's research staff on a prespecified topic and to participate actively in the department's internal seminars and other research activities. They will be provided with accommodation on demand and will, as a rule, have access to the department's computer resources. Their research output may be published in one of the department's publication outlets or as an OeNB Working Paper. Research visits should ideally last between three and six months, but timing is flexible.

Applications for 2018 should be e-mailed to [eva.gehringer.wasserbauer@oenb.at](mailto:eva.gehringer.wasserbauer@oenb.at) by May 1, 2018.

Applications (in English) should include

- a curriculum vitae,
- a research proposal that motivates and clearly describes the envisaged research project,
- an indication of the period envisaged for the research visit, and
- information on previous scientific work.

Applicants will be notified of the jury's decision by mid-June 2018. See also: [Visiting Research Program](#)

## 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](mailto:event-management@oenb.at).

March 14, 2018	Workshop: "Real analysis versus monetary analysis: Does it matter and what are its main implications for macroeconomic theory and policy?"
April 16, 2018	EIB-OeNB Workshop on financing investment
April 27, 2018	Austria 2018 Centenary Symposium: Debating the legacy of the 1918 proclamation of the Austrian Republic
May 4, 2018	Green finance, regulation and Central Banking!
June 12, 2018	82 <sup>nd</sup> East Jour Fixe: "Debt in Central, Eastern and Southeastern Europe: vulnerabilities and opportunities"
July 5–6, 2018	Conference organized by the Oesterreichische Nationalbank (OeNB) and the Austrian Federal Economic Chamber (WKO): „Economic and Monetary Union – Deepening and Convergence“

November 26–27, 2018	Conference on European Economic Integration 2018: “How to Finance Cohesion in Europe”.
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## OeNB Courses at the Joint Vienna Institute (JVI)

For further details see: [Course Schedule 2018](#)

January 15–18, 2018	Advanced Course on Financial Stability Stress Testing for Banking Systems
January 22–26, 2018	Banking Supervision within the Basel Framework (in cooperation with JVI and Deutsche Bundesbank)
March 5–9, 2018	HR Issues and Compliance (in cooperation with Deutsche Bundesbank)
March 12–16, 2018	Monetary Policy Implementation (in cooperation with JVI and Deutsche Bundesbank)
May 14–18, 2018	Integration in Europe: European Union and Eurasian Economic Union (in cooperation with the Austrian Federal Ministry of Finance)
September 10–14, 2018	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)
October 15–19, 2018	Macrofinancial Stability in Central, Eastern and Southeastern Europe
November 5–7, 2018	Cash Circulation and Payment Systems in Austria
November 19–23, 2018	Financial Education
November 26–30, 2018	Monetary and Financial Statistics Collected and Compiled by the ESCB