

November 2017

CESEE Research Update

Foreign Research Division

www.oenb.at/cesee-research-update

Content

OeNB's 81 st East Jour Fixe	2
Winners of the Olga Radzyner Award 2017	3
OeNB/ECB course "Macrofinancial Stability in CESEE" at the Joint Vienna Institute	4
Assessing spillovers from euro area monetary policy, Presentation at the Annual Conference of the Verein für Socialpolitik	5
Visiting Research at the Foreign Research Division	6
Focus on European Economic Integration Q 3/17	6
Visiting Research Program 2017 .	7
OeNB Courses at the JVI	8

<http://www.oenb.at>
<http://cesee.oenb.at>

Imprint/inquiries/copyright 2017:

Oesterreichische Nationalbank,
Foreign Research Division
Postal address: P.O. Box 61, A 1011 Vienna,
Austria

To subscribe or unsubscribe to our
newsletter, please visit our website

<http://cesee.oenb.at>

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 research and analysis 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

The OeNB's 81st East Jour Fixe: Nonperforming loans in CESEE: macroeconomic dimension and resolution strategies

On September 18, 2017, the Oesterreichische Nationalbank (OeNB) hosted its 81st East Jour Fixe, which was dedicated to nonperforming loans (NPLs) – an issue that has moved center stage in the European policy discussion after the global financial crisis. The debate on NPLs concerns many major institutions as well as regulators at the national level and the banking industry, a fact which was also reflected in the event's participants. The main takeaways from the East Jour Fixe were the following: efficient oversight and accounting standards are important for resolving the problem of NPLs; the valuation of collateral needs to be improved; the judicial system is crucial for bringing down NPL stocks and requires well-qualified staff; more efforts are needed to gain access to better and more comparable data; and finally, asset management companies seem to be an efficient option for dealing with NPLs as they can make use of economies of scale and have a certain bargaining power.

Session 1 focused on definitions of NPLs, NPL developments and macroprudential responses to NPLs. Stephan Barisitz, Senior Economist at the OeNB's Foreign Research Division, discussed the problems related to comparable analytical NPL definitions and suggested a qualitative extension of the IMF's quantitative criteria to harmonize the treatment of secondary elements, e.g. collateralized loans. Reiner Martin, Deputy Head of the ECB's Macro-Financial Linkages Division, highlighted negative effects of high NPLs at the national level and addressed the issue of cross-border spillovers at the euro area level. He also discussed a wide range of policy responses available to tackle the stock of NPLs – ranging from internal workouts, asset protection schemes, securitization and asset management companies to direct sales – and concluded by emphasizing that structural reforms, e.g. the compilation of standardized NPL data, are critical to resolving the NPL problem in the euro area. Miquel Dijkman, Coordinator at the Financial Sector Advisory Center (FinSAC) of the World Bank Group, argued that financial sector regulation in CESEE has become more proactive as policymakers realized that banks will not be able to cope with the NPL problem on their own. He highlighted recent technical assistance projects by the FinSAC in Albania, Slovenia and Ukraine and summarized three lessons from the World Bank's experience: first, the urgency of addressing the challenges related to structurally increasing NPLs are usually underestimated; second, NPLs are complex and call for a comprehensive approach; and third, an extensive restructuring of corporate borrowers is needed to effectively resolve the problem of NPLs. The discussion centered on the role of ex-ante measures, moral hazard issues and why the secondary market works better in the U.S.A. than in the EU.

Session 2 discussed the determinants and economic impact of NPLs. Elisabeth Beckmann, Senior Economist at the OeNB's Foreign Research Division, presented joint work with Helmut Stix, Senior Expert at the OeNB's Economic Studies Division, on how household, loan and bank characteristics affect households' repayment difficulties. Based on data from the OeNB Euro Survey and information on bank branch locations she concluded that income and income shocks are the most important determinants of households' NPLs but bank relations and bank proximity were found to also affect the probability of arrears. Peter Grasmann, Head of Unit, EU/Euro area financial system, DG for Financial Stability, Financial Services and Capital Markets Union of the European Commission, emphasized that the resolution of NPLs always implies an allocation of losses. He noted that in the EU, the situation has improved somewhat on the back of the economic recovery, proactive policies by banks and policy measures taken by the Member States, the ECB's Single Supervisory Mechanism (SSM) and the European Commission. The Ecofin Council e.g. adopted the EU action plan on NPLs in July 2017. This ambitious plan comprises 14 actions to be taken by various public stakeholders in Europe. Tomislav Ridzak, Director of the Financial Stability Department at the Croatian National Bank, focused on the case of Agrokor and its impact on Croatia's banking system and economy. He argued that the financial problems in the Agrokor Group may have a stronger adverse effect on economic growth than currently projected but that stronger-than-expected growth in the exports of tourist services will compensate for such an effect. The subsequent discussion touched on the specific problems of the highly indebted banking sector in Cyprus, where due to high financing needs, bailing out the banking sector was not feasible for the state – a situation which was comparable to that of Iceland. With regard to Croatia, Ridzak clarified that the impact of Agrokor on NPLs should already have subsided.

Session 3 focused on progress in NPL resolution. Ines Rocha, Associate Director of the Financial Institutions Department at the European Bank for Reconstruction and Development (EBRD), emphasized the work of the Vienna Initiative 2.0 and elaborated on the different layers of intervention and its NPL action plan. When summarizing best practices, Rocha highlighted the need for clarity on bank secrecy rules, adequate provisioning





policies, accurate collateral valuation, investor-friendly licensing requirements, removal of tax disincentives and the training of judges. Imre Balogh, CEO and Executive Director at DUTB, Slovenia's bank asset management company, discussed Slovenia's experience with NPL resolution and presented comprehensive facts and figures on Slovenia's bank rehabilitation process, which involved i.a. state capital injections and the establishment of DUTB. After providing some details on DUTB's portfolio structure, he shared his views on corporate

governance issues at DUTB and highlighted the importance of credibility for his institution. Anete Daukste, Associate Director at KPMG AG's Global Portfolio Solutions Group, dealt specifically with the question how markets for NPL sales have developed in CESEE.

In her view, one reason for the vivid NPL market activity in Romania has been peer pressure. While NPL volumes are largest in Poland, transactions primarily took the form of industrialized small-scale NPL sales. It is worth noting that more recently secondary NPL sales have increasingly gained importance. Greece and Ukraine are generally seen as interesting new markets. In the ensuing discussion, topics of interest were the statistical treatment of NPLs after banks sell them to an investor, the typically small size of NPLs in absolute terms as a frequent impediment for more active NPL markets in smaller countries and difficulties in selling cross-border portfolios stemming from legal differences between various jurisdictions.

In his concluding remarks, Thomas Richardson, Director at the Joint Vienna Institute, recalled the crucial importance of tackling the problem of NPLs: NPLs have a particularly strong adverse economic impact on SMEs because they largely depend on bank financing and, moreover, are very employment intensive. Furthermore, a high stock of NPLs in the banking sector can have negative repercussions on the monetary transmission mechanism.

The presentations and workshop program are available at <https://www.oenb.at/en/Monetary-Policy/Research/workshops.html>.

A more detailed summary can be found in FEEI 4/Q17 which will be published at the end of November.



Olga Radzyner Award Winners 2017

The Olga Radzyner Award is bestowed annually on young economists from Central, Eastern and Southeastern Europe (CESEE) for excellent scientific work on European economic integration. The Oesterreichische Nationalbank (OeNB) established this award in 2000, to commemorate the former head of its Foreign Research Division, Olga Radzyner, who pioneered the OeNB's CESEE-related research activities.

In 2017, the OeNB received 20 submissions for the Olga Radzyner Award from candidates from 16 countries. Of this total, the jury of OeNB reviewers chose to reward four papers they considered outstanding in terms of originality and quality of the analysis, including the use of state-of-the-art methods. OeNB Governor Ewald Nowotny will present the awards on November 20, 2017, on the occasion of the Conference on European

Economic Integration (CEEI). The winners are (in alphabetical order):

Piotr Denderski and Wojciech Paczos (Poland) will receive the award for their paper **“Foreign banks and the bank lending channel.”**

Mr. Denderski and Mr. Paczos both hold a PhD degree and are assistant professors at two different universities in the U.K. – at the University of Leicester and the University of Cardiff. In their paper, they carefully analyze the bank lending channel of monetary policy in 11 transition economies in the period 1998-2012 and show that, in line with theoretical expectations, banks curb their credit supply after an increase in the monetary policy rate and vice versa. Interestingly, they find that the bank lending channel is weaker for foreign owned banks and that the observed difference cannot be explained by parent bank characteristics but rather by the high profitability of foreign owned banks compared to domestically owned banks.

Arta Hoxha (Republic of Kosovo) will receive the award for her paper **“Explaining the impact of the global financial crisis on European transition countries: A GVAR approach.”**

Ms. Hoxha is a PhD student at the Staffordshire University in the U.K. In her paper, she examines how the Baltics, Balkan and CEE economies respond to shocks in advanced European countries (EU-15). Ms. Hoxha finds that a decrease in the EU's GDP and an increase in financial stress both depress output throughout the regions, but that the Baltic countries show the most pronounced responses. The shocks to this region tend to transmit through foreign credit flows, FDI and remittances.

Stjepan Srhoj (Croatia) will receive the award for his paper **“Getting ready for the EU Single Market – the impact of development grants on firm competitiveness.”**

Mr. Srhoj is a teaching and research assistant at the University of Dubrovnik and a PhD student at the University of Innsbruck. Based on a unique and carefully constructed firm level dataset, he analyzes the effects of public grants on firms' export, productivity and employment performance in Croatia. He finds a significant boost to exports and employment of smaller firms from public development grants, especially from larger grants, while there seem to be no noteworthy effects on large companies. Mr. Srhoj's results are thus in line with arguments in favor of industry support schemes and related theories.

Andrzej Torój (Poland) will receive the award for his paper **“Managing external macroeconomic imbalances in the EU: the welfare cost of scoreboard-based constraints.”**

Mr. Torój is an assistant professor at the Warsaw School of Economics. In his paper, he analyzes the welfare implications of the recently introduced thresholds on external imbalance indicators envisaged by the Macroeconomic Imbalance Procedure (MIP). Within the framework of a New Keynesian DSGE model, Mr. Torój employs both flexible exchange rate and common currency scenarios to evaluate the impact of implementing the lower bound on the current account deficit (-4%) for Poland. He shows that welfare loss remains very limited as compared to optimum unconstrained policy, but that these costs are lower under flexible exchange rates as compared to a common currency scenario. His results indicate that a scoreboard-based evaluation of external imbalances has some room for fine-tuning in the course of future MIP reforms.

OeNB/ECB course “Macrofinancial Stability in CESEE” at the Joint Vienna Institute, October 9–13, 2017

Together with the ECB's Macroeconomic Policy Division, the OeNB's Foreign Research Division organizes an annual seminar on “Macrofinancial Stability in Central, Eastern and Southeastern Europe” at the Joint Vienna Institute. The 2017 seminar with course directors Markus Eller (OeNB) and Reiner Martin (ECB) took place in the week of October 9–13.

The objective of the course is to help participants better understand the interactions between the real and the financial sector, the role of fiscal and structural policies and the way financial stability risks can be evaluated in the CESEE region. In 2017, the course also addressed topical issues such as new financial technologies, the

resolution of nonperforming loans, macroprudential stress tests and sovereign debt risks.

Besides lectures prepared by OeNB and ECB experts, the course also featured contributions from the OECD, the World Bank, the Bank of Lithuania and the banking industry. In group sessions, which are always an essential

part of the course, participants developed an adjustment program for sample countries subject to macrofinancial stress; they were asked to negotiate the program in role plays, representing international institutions (IMF, European Commission, ECB) and the countries involved (national central banks and ministries of finance).

The 2017 course's attendees included mid-level officials, senior economists and financial stability experts from central banks and ministries of a large number of CESEE and CIS countries, ranging from the Czech Republic to Tajikistan and from Latvia to Turkey.

Next year's seminar is scheduled to take place from October 15 to 19, 2018. The application deadline is July 15, 2018. For the 2017 course program and the 2018 course description and to apply online, please go to <https://www.jvi.org/training/course-schedules/course-schedule-2018/course/18ON06.html>.



Assessing spillovers from euro area monetary policy Presentation at the Annual Conference of the Verein für Socialpolitik

This year's Annual Conference of the Verein für Socialpolitik, one of the largest professional economics association in Europe, was dedicated to "Alternative Structures for Money and Banking" and took place at the University of Vienna, from September 3 to 6. It featured keynote lectures on issues related to crypto currencies by prominent central bankers (such as Michael Kumhof, Bank of England) and leading economists from academia (including Martin Hellwig from the Max Planck Institute and Albrecht Ritschl from the London School of Economics).

In a special session on Globalization and Spillovers, invited speaker Martin Feldkircher, principal economist at the OeNB's Foreign Research Division, presented ongoing research¹. Since the global financial crisis, the ECB has implemented several non-standard monetary policy measures. The latest of these measures constitute buying large amounts of securities issued by euro area governments, agencies and EU institutions, asset-backed

securities and covered bonds, which drives down longer-term yields. Not only can the actual purchase of these securities alter interest rates, but the successful commitment of the ECB to follow a certain policy path can also influence financial markets. As a consequence, euro area long-term yields decline and spreads between euro area long-term yields narrow. What are the international spillover effects of these financial developments?

The results of the empirical study reveal positive spillover effects on economic activity for neighboring EU Member States in Central, Eastern and Southeastern Europe (CESEE). These effects are driven by the financial channel: As investors face smaller yields in the euro area, they start investing more in neighboring regions. This international portfolio rebalancing effect causes yields to fall in CESEE and in turn pushes up demand for credit and spurs investment and output growth. The positive effect on economic activity is amplified by a rise in equity

¹ The presentation is based on Feldkircher, M., Gruber, T. and F. Huber (2017): *Spreading the word or reducing the term spread? Assessing spillovers from euro area monetary policy*. WU Working Paper Series Nr. 248/2017.

prices, both within the euro area as well as in neighboring CESEE countries. These effects are somewhat counterbalanced by a strengthening of CESEE currencies against the euro as a result of increased portfolio flows into the region. By contrast, there is not much evidence of significant effects on consumer prices, both inside

and outside the euro area. The study also yields evidence for a great deal of heterogeneity of spillovers. In a nutshell, output spillovers are stronger in countries that have historically witnessed boom-bust periods on the one hand or that are strongly integrated with the euro area on the other hand.

Visiting Research at the Foreign Research Division



From September 5 to September 21, 2017, Laura Solanko, Senior Adviser at the Bank of Finland Institute for Economies in Transition (BOFIT) visited the Foreign Research Division of the OeNB. Ms. Solanko has a long

experience in the research and analysis of the Russian economy, the Russian banking sector, and Russian energy markets in particular. During her stay in Vienna she worked on a research project examining bank failures. The study relies on unique monthly bank balance sheet data covering the recent period of intensive clean-up of the Russian banking sector. The results show that

changes in various accounting measures, not the levels, are significant in predicting bank failure.

Laura Solanko also used this visiting research period to continue her research on nowcasting with respect to the Russian economy. The aim of this study is to highlight a set of single high-frequency indicators that will be useful in nowcasting or short-term forecasting Russian GDP growth. The study points to the increasing importance of monetary and banking variables in nowcasting since the recession of 2009. Additionally, the visit offered an excellent opportunity to strengthen the ties between BOFIT and the Foreign Research Division on many fronts, and to exchange views and experiences on the region.

Focus on European Economic Integration Q3/17 – latest issue [\(full version\)](#)

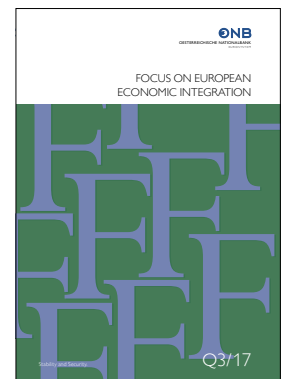
Studies

The new silk road, part I: a stocktaking and economic assessment, Barisitz, S., Radzyner, A.

Competitiveness of CESEE EU Member States: recent trends and prospects, Ritzberger-Grünwald, D., Schreiner, J., Wörz, J.

Fintechs and their emergence in banking services in CESEE, Stern, C.

Comparing market power at home and abroad: evidence from Austrian banks and their subsidiaries in CESEE, Feldkircher, M., Sigmund, M.



Save the Date

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

organized by the Oesterreichische Nationalbank (OeNB)

November 20 and 21, 2017

Vienna Marriott Hotel

Parkring 12a, 1010 Vienna, Austria

Amid today's formidable challenges, well-designed and effective structural reforms are key to shaping Europe's future and facilitating its return to balanced growth and convergence. The CEEI 2017 will revisit the profound market reforms carried out in Central, Eastern and Southeastern European (CESEE) countries, shedding light on individual privatization strategies as well as gradual versus shock transformation. In line with a modern understanding of structural reforms that goes beyond liberalization and deregulation, speakers will also highlight social aspects and distributional effects of such reforms. Given the quickening pace of technological change, the conference will moreover serve to assess the implications of future challenges arising from digitalization, deindustrialization and the emerging protectionist threat to Europe. Taking a forward-looking perspective, experts from academia and politics will discuss which reform steps are necessary to provide for prosperous labor, product and capital markets.

More information: https://www.oenb.at/en/Calendar/2017/20171120_21_ceedi.html

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 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.

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

OeNB Courses at the Joint Vienna Institute (JVI) – 2017

For further details see: <https://www.jvi.org/home.html>

January 23 – 26, 2017	Advanced Course on Financial Stability Stress Testing for Banking Systems
January 30 – February 3, 2017	Banking Supervision within the Basel Framework (in cooperation with JVI and Deutsche Bundesbank)
March 2 – 3, 2017	International Cooperation in Central Banks
March 13 – 17, 2017	Monetary Policy Implementation (in cooperation with JVI and Deutsche Bundesbank)
March 20 – 22, 2017	Financial Education
May 8 – 12, 2017	Integration in Europe: European Union and Eurasian Economic Union (in cooperation with the Austrian Federal Ministry of Finance)
September 11 – 15, 2017	Challenges for Candidate and Potential Candidate Countries in the EU and EMU Accession Process (in cooperation with the Austrian Federal Ministry of Finance and the ECB)
October 9 – 13, 2017	Macro-Financial Stability in Central, Eastern and Southeastern Europe (in cooperation with the ECB)
November 22 – 24, 2017	Financial Translation and Editing: New Skills for New Challenges
November 27 – 29, 2017	Cash Circulation and Payment Systems in Austria

OeNB Courses at the Joint Vienna Institute (JVI) – 2018

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