

The OeNB's 84th East Jour Fixe

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

In cooperation with the Official Monetary and Financial Institutions Forum (OMFIF)¹

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The Oesterreichische Nationalbank (OeNB) organized its 84th East Jour Fixe in cooperation with the Official Monetary and Financial Institutions Forum (OMFIF). The event took place on June 3, 2019, and discussed the topic of “Long-run economic growth and development in Central, Eastern and Southeastern Europe (CESEE): goals, priorities and implementation strategies.” Speakers from diverse backgrounds presented academic, political and other professional expertise to a selected, multinational audience.

In his welcome address, OeNB Governor *Ewald Nowotny* highlighted the OeNB's long-standing research focus on the CESEE region as well as related OeNB products and events. Moreover, he commented on a number of aspects affecting long-run growth in CESEE, such as demographic developments and difficulties in forecasting them, as well as on the increasingly important role of China.

Session 1 discussed long-run growth and resilience and was chaired by *Dubravko Mihaljek*, Head of Macroeconomic Analysis at the Bank for International Settlements (BIS). *Erik Berglöff*, Director of the Institute of Global Affairs at the London School of Economics and Political Science, gave the keynote speech on convergence. He pointed out that some economists and policymakers are concerned about the middle-income trap for CESEE. However, there is limited empirical evidence that such a trap exists. In Berglöff's opinion, the outlook for CESEE will depend largely on how the region deals with the new challenges it currently faces: (1) rapidly changing technologies, (2) social equity and rising populism, and (3) environment and sustainability issues. He argued that overcoming these challenges requires well-executed industrial policies and preferably sector-oriented horizontal policies that promote education or innovation relevant for specific sectors. In his opinion, one issue is that the countries that need such industrial policies the most are often those that lack the state capacity to execute them properly. Berglöff concluded on a positive note, stating that historically, countries that grew fast in initial transition periods – as many CESEE countries did – usually did well also in later periods.

The keynote was followed by a discussion by *Tomáš Slačák*, Senior Economist at the OeNB's Foreign Research Division, who picked up some of Berglöff's key hypotheses. Slačák provided evidence that the structural convergence of CESEE countries toward the EU average between 2007 and 2016 was rather limited. He

¹ The presentations and workshop program are available at www.oenb.at/en/Calendar/2019/2019-06-03-east-jour-fixe-84.html.

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found differences across countries when looking at five structural and competitiveness indicators. The information and communications technology (ICT) sector showed the highest convergence, while the human capital indicator diverged from the EU average. Using the example of the automotive sector, Slačik moved on to demonstrate CESEE's increased integration into global value chains. However, the automotive sector currently faces several challenges, in particular ever-stricter emission limits. These will certainly lead to massive structural changes in the industry. Against this background, Slačik argued that the strong reliance of some CESEE countries on automotive industries and their stronger integration into global value chains bear cyclical and structural risks to growth.

In the ensuing discussion, several members of the audience referred to industrial policy. One question was whether the rise of the automotive sector in CESEE resulted from dedicated industrial policies. Most people involved in the discussion agreed that it was. Moreover, given current challenges in the automotive sector, the question was raised whether this showed that governments were not good at picking the "right" sectors for long-term growth. Another question was whether industrial policy should be conducted at the national or EU level. According to Berglöf, in the end these policies need to be solved at the domestic level, but they could be promoted and subsidized by the EU. Berglöf also elaborated on some of the state capacities he considered most important for successful industrial policies: bureaucratic capacity, judicial independence and transparency in procurement.

A live survey of the audience conducted via Mentimeter showed that 50% of survey participants thought that potential growth in the CESEE EU Member States would remain broadly unchanged over the next 10 to 15 years. Of the remaining 50%, a somewhat larger group thought that potential growth would decrease rather than increase. Regarding the audience's views on which topics CESEE policymakers should prioritize, a clear majority voted for "institutional quality and governance," followed by "investment in digitalization/new technologies" and "demographics/emigration" on a close second and third rank. The answer "upgrading of the production chain" came in fourth.

Session 2 focused on green growth in CESEE and on related opportunities and obstacles. It was chaired by *Helene Schubert*, Head of the OeNB's Foreign Research Division. *Sigrid Stagl*, Head of the Institute for Ecological Economics at the Vienna University of Economics and Business, pointed out that emissions in the atmosphere have progressed well beyond what could be considered a "safe" level. She questioned the term "green growth," which she criticized as being ill defined. Stagl explained that output growth continues to imply an absolute increase in emissions, even though some progress has been made in terms of lowering emissions per unit of output. An absolute increase in emissions is still dangerous, given that we should actually lower the total amount of emissions. A "simple" law demanding a halving of emissions every decade would bring us back to a sustainable path – in the first decade, there will be some "low-hanging" fruits that facilitate achieving the goal. In the ensuing Q&A session, Stagl also elaborated on the effectiveness of different tools for greening the economy – in her opinion, some of the best policy tools are the discontinuation of all subsidies for fossil fuels, direct regulation, and taxes. Market-conform measures, such as emissions trading, tend to be somewhat less effective given uncertainties surrounding prices. Schubert raised the topic of lock-in effects and Stagl confirmed that these effects were particularly high in the

energy and transportation industries as the related infrastructure was often used for many decades.

Pieter de Pous, Senior Policy Advisor at E3G, shared some insights on just transition with regard to phasing out coal in CESEE. He pointed out that regarding the phaseout of coal, some CESEE countries were progressing faster (e.g. the Czech Republic, Poland and Slovakia) than others (e.g. Bulgaria and Romania). He then turned to coal transition in Canada, Germany, Spain and the United Kingdom to draw some lessons from their experiences. The Czech Republic is currently setting up a Coal Commission, and De Pous emphasized that the mandate and setup of such commissions is critical for their success. Moreover, he pointed out that generous compensations as planned by Germany can make coal transition very costly. He also highlighted the importance of EU funds and the need for stable policy frameworks to ensure investments in renewable energies. De Pous used the U.K. as an example to illustrate that if carried out properly, the transition away from coal could happen very fast.

The OeNB's 84th East Jour Fixe closed with a panel organized by OMFIF and headed by OMFIF Chairman *David Marsh*. *Vojtěch Benda*, member of the Bank Board of the Czech National Bank, *Andrzej Raczko*, Advisor to the President of Narodowy Bank Polski, and *Weixi Gong*, Chief of the Investment Promotion Division and Coordinator of the Investment and Technology Promotion Offices (ITPOs) Network at the United Nations Industrial Development Organization (UNIDO), discussed CESEE and China, and in particular China's Belt and Road Initiative (BRI). The panel covered topics such as the benefits of the BRI for China and CESEE, stronger financial linkages, central bank cooperation and the need for reciprocity in the relationship between China and CESEE. When the audience was asked about their views on Chinese investments in CESEE, most were critical. 50% of the audience participating in the live Mentimeter survey thought that CESEE governments should ensure reciprocity. 30% thought that CESEE governments should be wary about Chinese investments, monitor them closely and/or regulate them. Only 20% opted for the more positive answers about Chinese investments in CESEE.