

Q1/2014

CESEE Research Update

Foreign Research Division

Content

Summary: EBRD Transition Report 2013.....	2
Focus on European Economic Integration Q1/14.....	3
Euro Survey.....	4
Call for Applications: Visiting Research Program.....	5
Call for Entries: Olga Radzyner Award.....	5
Upcoming Events	6
OeNB Courses at the Joint Vienna Institute	6

<http://www.oenb.at>

<http://ceec.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

Highlights of this Issue

- Summary EBRD Transition Report 2013: Stuck in Transition? (see p. 2)
- Studies in: Focus on European Economic Integration Q1/14 (see p. 3)
- Euro Survey (see p.4)
- Event Wrap-Ups (see p. 5)
- Call for Applications: Visiting Research Program (see p. 5)
- Call for Entries: Olga Radzyner Award 2014 (see p. 5)

• Save the Date:

April 24 – 25, 2014: East Jour Fixe: 10 Years of Eastern Enlargement

November 24 – 25, 2014: Conference on European Economic Integration (CEEI) 2014

Summary EBRD Transition Report 2013: Stuck in Transition?

On January 27, 2014, the Oesterreichische Nationalbank (OeNB) and the Austrian Ministry of Finance (BMF) co-hosted the presentation of the 2013 Transition Report of the EBRD, including January 2014 GDP growth forecast updates for the "EBRD region." The event took place at the ministry's premises and was opened by *Harald Waiglein*, Head of the BMF's Directorate General Economic Policy and Financial Markets, and by *Doris Ritzberger-Grünwald*, Director of the OeNB's Economic Analysis and Research Department.



Copyright: BMF/Elisabeth Kessler

In his opening remarks, Waiglein emphasized the importance of the EBRD Transition Report as a source of up-to-date information about CESEE countries. Given the high share of trade between Austria and CESEE and the catalytic effect of eastward EU enlargement for the Austrian economy, Waiglein expressed some concerns about the latest developments in the region, as evidenced by the Transition Report, e.g. the stalling or even partial reversal of reforms in some countries.

Ritzberger-Grünwald stressed that the title of the 2013 EBRD Transition Report comes with a question mark, which would imply that the gloomy assessment of recent developments may leave some room for optimism. While economic convergence of CESEE with the euro area will without doubt be a more protracted process than expected and while CESEE countries have lost some of their price competitiveness, these aspects are only one side of the coin. Indeed, CESEE countries have seen some improvements in other fields. For example, they were able to improve the quality of their exports, which has more than compensated the loss in price competitiveness.

After the introductory remarks, *Jeromin Zettelmeyer*, the EBRD's Deputy Chief Economist and Director of Research, summarized the EBRD's latest growth forecasts for the countries in the EBRD region and outlined the major messages of the EBRD Transition Report 2013 "Stuck in Transition?"

Part I: The Short-Term Perspective: State of the Recovery and Outlook for 2014

In 2014, the EBRD expects real GDP growth in the transition region to reach 2.7%, compared to 2.0% in 2013. According to the forecast, Central Europe and the Baltic states will grow on average by 2.2% in 2014 (2013:

1.1%), largely driven by better growth prospects in the Baltics, Poland and the Slovak Republic. Slovenia, in contrast, is expected to remain in recession. Growth in SEE is almost unchanged in 2014 compared to 2013 (around 2%) while Turkey will see some deceleration of real GDP growth (from 3.7% in 2013 to 3.3% in 2014). In Russia economic growth will amount to 2.5% in 2014 (1.3% in 2013). Zettelmeyer summarized the first part of his presentation by stating that the overall picture for the 2014 outlook is blurred by a weak external environment, tight financing conditions as well as negative impacts of the crisis leading to slow economic recovery.

Part II: The Medium- and Long-Run Perspective: Resumption of Convergence?

Zettelmeyer explained that convergence is unlikely to take place in the absence of a reform of current economic and institutional policies. This negative view is largely driven by two facts: first, productivity catch-up is largely completed in CESEE and second, reforms have stagnated since the mid-2000s in many countries. Zettelmeyer elaborated that one cause of stagnation is an "underreform trap," which involves imperfectly democratic and autocratic regimes, weak economic institutions, and low growth outside the resource sector.



Copyright: BMF/Elisabeth Kessler

Zettelmeyer continued by raising the question how countries can break out of the underreform trap. In imperfect democracies, economic institutions can be influenced positively by moderate political shocks. Apart from political shocks, feasible political reforms, openness to trade and foreign direct investment as well as education, in particular higher education, can improve economic institutions.

Zettelmeyer concluded by highlighting the factors that are decisive for reforming a country successfully. Thus, the priorities of the political leaders matter for the reform path a country takes. Additionally, experience has shown that success depends on external anchors and support. For many of the relatively new EU Member States the prospect of EU membership spurred reforms. Similarly foreign financial and technical assistance supported the implementation of economic reforms. In other words, deeper international integration can promote economic reforms, income gains and democratic changes.

[Focus on European Economic Integration Q1/14](#)



Studies in: Focus on European Economic Integration Q1/14

Hake M. , Lopez-Vicente F. , Molina L., “Do the Drivers of Loan Dollarization Differ between CESEE and Latin America? A Meta-Analysis“ pp. 8-35

In this paper we compare the determinants of loan dollarization in two emerging market regions, namely Central, Eastern and Southeastern Europe (CESEE) and Latin America, through a meta-analysis of 32 studies that provide around 1,200 estimated coefficients for six drivers of foreign currency lending. As a common pattern, we find macroeconomic instability (as expressed by inflation volatility) and banks' funding in foreign currency to play a significant role in explaining loan dollarization in both

regions. In contrast, the interest rate differential appears to be a key determinant only in Latin America, while the positive impact of exchange rate volatility on dollarization implies a more prominent role for supply factors in the CESEE region. While the robustness of the results has been verified, our meta-analysis shows that estimates reported in the literature tend to be influenced by study characteristics such as the methodology applied and the data used. ([Full article](#))

Slačík T., Steiner K., Wörz J., “Can Trade Partners Help Better FORCEE the Future? Impact of Trade Linkages on Economic Growth Forecasts in Selected CESEE Countries“ pp. 36-56

For Central, Eastern and Southeastern European (CESEE) countries, the euro area is the most important export destination. Nevertheless, geographical export patterns differ among individual CESEE countries, and economic growth within the euro area has diverged in the run-up to and since the economic and financial crisis. We therefore examine the effects such heterogeneous developments have had on trade – and thus economic growth – in CESEE. Given the importance of such spillovers for macroeconomic projections, we evaluate the OeNB's macroeconomic forecasting model (FORCEE) for Bulgaria, Croatia, the Czech Republic, Hungary, Poland and Romania. The FORCEE model captures trade

spillovers via aggregate demand from the euro area. We challenge this simplification by introducing a more differentiated representation of the regional structure of trading partners. Our results show that such a modification improves the forecasting performance of our structural macro model in particular for the three Southeastern European countries in our sample. However, our tests do not yet account for the additional uncertainty introduced into the model by broadening the set of external assumptions, when we cover external demand from a wider range of partner countries. ([Full article](#))

Kabashi R., Olga Radzyner Award winner 2012, “The Cyclical Character of Fiscal Policy in Transition Countries“ pp. 57-73

This study investigates the cyclical character of fiscal policy in transition countries in Central, Eastern and Southeastern Europe (CESEE) in the period from 1995 to 2011, using system GMM as the preferred estimation method for the underlying sample and model specification. The study finds discretionary policy in the CESEE EU Member States and in the Western Balkan countries to have been procyclical, thus aggravating economic fluctuations, whereas automatic stabilizers

moved overall policy to an acyclical stance. In addition, the analysis indicates considerable differences in the cyclical character of fiscal policy between transition countries and the Western European EU Member States, where both overall fiscal policy and discretionary policy were acyclical. Finally, the study also offers several recommendations for policymakers, particularly in transition countries. ([Full article](#))

CESEE-Related Abstracts from Other OeNB Publications

Barisitz S., “Credit Boom in Russia despite Global Woes – Driving Forces and Risks “ pp. 74

After the crisis slump of 2008–2009, real year-on-year credit growth in Russia turned into a boom in 2011, with double-digit growth climaxing at +24% in mid-2012, before slowing down again. The ratio of domestic credit to GDP is, however, not high compared to peer countries. Retail lending, while still modest, developed most dynamically. Yet domestic deposits rose even more swiftly than domestic loans, and the loan-to-deposit ratio slightly declined. The driving forces of the Russian credit boom are (a) on the demand side: the oil price recovery (from early 2009 to early 2012) and relatively brisk domestic demand growth, partly driven by generous public salary and pension adjustments, and financial deepening in the highly profitable retail sector; (b) on the supply side: the “deposit boom,” increasing profits of resource enterprises, and official liquidity assistance. Risks related to the credit boom include surging unsecured consumer loans (+44% in real terms in 2012, thus

accounting for 60% of household credit), widespread connected lending, elevated levels of nonperforming loans (NPLs), and modest provisioning. The Central Bank of the Russian Federation (CBR) reacted to the (consumer) credit boom by moral suasion and some prudential measures. The deceleration of lending growth since mid-2012 was probably largely due to the general economic slowdown. Shock-absorbing factors are considerable, including growing deposits as well as satisfactory profitability and the banking sector's net external creditor position, but some factors, such as capital adequacy and loan loss provisions, have been eroding recently. In the current economic situation, the most probable outlook for the Russian lending boom is a soft landing.

Published in *Financial Stability Report 26*.

[\(Full article\)](#)

Feldkircher M., Fenz G., Ferstl R., Krenn G., Neudorfer B., Pühr C., Reiningger T., Schmitz S. W., Schneider M., Siebenbrunner C., Sigmund M., Spitzer R., “ARNIE in Action: The 2013 FASP Stress Tests for the Austrian Banking System“ pp. 74

In this paper we present the main concepts and methods of the stress tests that the Oesterreichische Nationalbank conducted in 2013 in close cooperation with the IMF under the latter's Financial Sector Assessment Program (FSAP). We cover solvency and liquidity stress tests as well as, as part of our contagion analysis, the interaction of solvency with liquidity. The paper's objective is to contribute to the growing literature on applied stress testing by (i) sharing our methodological approaches, in particular innovations to cash flow-based liquidity stress testing, and by (ii) discussing the calibrations employed in what were the most extensive stress tests conducted for Austria in the past five years. Moreover we (iii) provide

results at an aggregated level. The 2013 FSAP stress tests for Austria also mark the first public appearance of the OeNB's new systemic risk assessment tool, ARNIE (“Applied Risk, Network and Impact assessment Engine”). By covering recent methodological as well as operational progress, we also shed light on practical challenges. Finally, we identify the need for further work, in particular with regard to the interaction of solvency and liquidity stress testing, and contagion analysis more generally.

Published in *Financial Stability Report 26*.

[\(Full article\)](#)

Euro Survey

Beckmann E., Stix H., “Foreign Currency Borrowing and Knowledge about Exchange Rate Risk“ OeNB Working Paper 188 (forthcoming)

Foreign currency borrowing is widespread in many regions of the world. This raises the question whether unhedged borrowers do not understand the exchange rate risk emanating from such loans. Employing household level micro-data from eight Central and Eastern European countries we study how agents' knowledge about exchange rate risk affects the currency denomination of loans. Results show, first, that a majority of respondents is aware that depreciations increase loan installments. Second, we find that knowledge about the exchange rate

risk lowers the demand for foreign currency borrowing. To assess the causal effect of literacy on loan demand we utilize information on agents' exchange rate expectations. Overall, results suggest that financial literacy exerts a strong impact on the choice of the loan currency. However, from an aggregate perspective, a misunderstanding of the underlying risks is not the main cause of foreign currency borrowing.

Event Wrap-Ups

Conference on European Economic Integration 2013 – Financial Cycles and the Real Economy: Lessons for CESEE ([Full article](#))

Olga Radzyner Award Winners 2013 ([Full article](#))

Call for Applications: Visiting Research Program



The OeNB invites applications from external researchers 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 pursue 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 re-

search 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 (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.

Applications for 2014 should be e-mailed to eva.gehringer-wasserbauer@oenb.at by May 1, 2014.

Applicants will be notified of the jury's decision by mid-June. The following round of applications will close on November 1, 2014.

See also: [Visiting Research Program 2014](#)

Call for Entries: Olga Radzyner Award 2014

The OeNB has established an award to commemorate Olga Radzyner, former Head of the OeNB's Foreign Research Division, who died in a tragic accident in August 1999. The award is bestowed on young economists for excellent research on topics of European economic integration and is conferred annually. In 2014, four applicants are eligible to receive a single payment of EUR 3,000 each from an annual total of EUR 12,000.

Submitted papers should cover European economic integration issues and be in English or German. They should not exceed 30 pages and should preferably be in the form of a working paper or scientific article. Authors shall submit their work before their 35th birthday and shall be citizens of any of the following countries: Albania, Belarus, Bosnia and Herzegovina, Bulgaria, Croatia, the Czech Republic, Estonia, FYR Macedonia, Hungary, Kosovo, Latvia, Lithuania, Moldova, Montenegro, Poland, Romania, Russia, Serbia, Slovakia, Slovenia and Ukraine. Previous

winners of the Olga Radzyner Award, ESCB central bank employees as well as current and former OeNB staff are not eligible. In case of co-authored work, each of the co-authors has to fulfill all the entry criteria.

Authors shall send their submissions by postal mail – with the envelope marked "Olga Radzyner Award" – to the Oesterreichische Nationalbank, Foreign Research Division, Otto-Wagner-Platz 3, PO Box 61, 1011 Vienna, Austria. Entries for the 2014 award should arrive at the OeNB by September 19, 2014, at the latest.

For more information, please see www.oenb.at or contact Ms. Eva Gehringer-Wasserbauer in the OeNB's Foreign Research Division either by e-mail eva.gehringer-wasserbauer@oenb.at or by phone (+43-1-40420-5205).

See also: [Olga Radzyner Award 2014](#)

Save the Date

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 ceec@oenb.at.

April 24 – 25, 2014: East Jour Fixe: 10 Years of Eastern Enlargement

On the occasion of the 10th anniversary of eight CESEE countries joining the European Union, the OeNB will host the 75th East Jour Fixe “10 Years of EU Enlargement” on its premises on Friday, April 25, 2014. The Anniversary East Jour Fixe will be part of a two-day event on April 24 and 25, 2014, organized jointly by the OeNB, the Vienna Institute for International Economic Studies (wiiw) and the Institute for Human Sciences (IWM). The event will cover a broad range of topics associated with EU enlargement and the European integration process, such as: lessons learned from past EU enlargement rounds; prospects for the future; multi-speed Europe; reviving convergence after the crisis; monetary and exchange rate strategies; Euro-

pean integration and nationalism; and 1914–2014: a century of European disintegration and re-integration. The focus of the Friday morning session will be on monetary and exchange rate aspects. The program will comprise a keynote speech followed by a moderated panel discussion of central bank heads of research from Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia and Slovenia. The discussion will be organized in two rounds, the first one focusing on exchange rate strategies and competitiveness, the second one on financial stability challenges.

November 24 – 25, 2014: Conference on European Economic Integration (CEEI)

OeNB Courses at the Joint Vienna Institute (JVI)

For further details see: www.jvi.org

January 20-23, 2014	Advanced Course on Financial Stability Stress Testing for Banking Systems
May 12-16, 2014	Institutional Challenges for EU Candidate and Potential Candidate Countries on the Road to the EU and EMU
September 15-17, 2014	Cash Circulation and Payment Systems in Austria
October 13-17, 2014	Macro-Financial Stability in Central, Eastern and Southeastern Europe
October 20-24, 2014	Economic and Monetary Integration in Europe
November 17-21, 2014	Monetary and Financial Statistics Collected and Compiled by the ESCB
December 1-2, 2014	Financial Education in Central Banks: Initiatives and Activities

Imprint/inquiries/copyright 2014:

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://ceec.oenb.at>