



# **Where Is the Engine of Growth in the World? Role of the Transition Economies**

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**CERGE-EI**

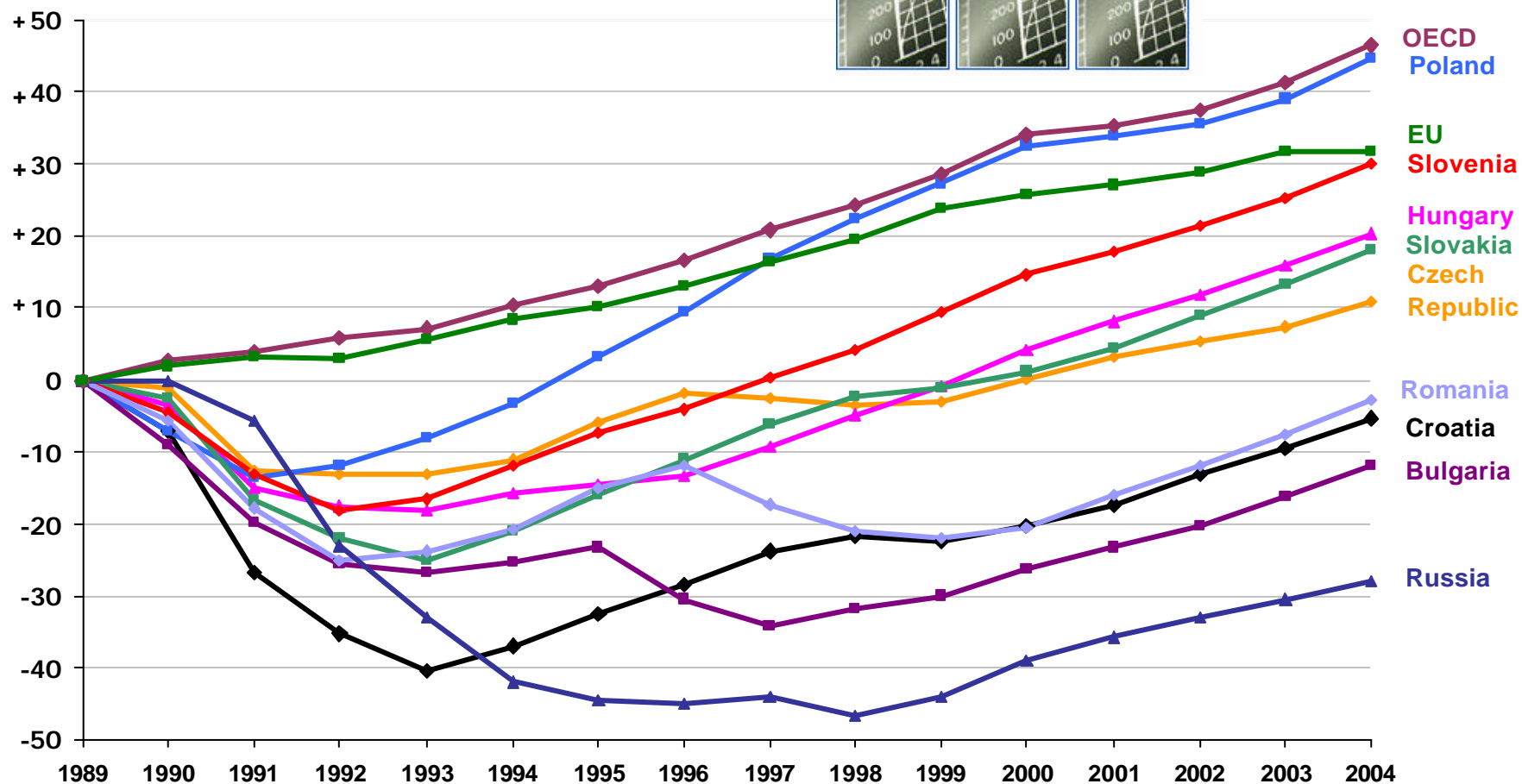
**Prague**

**May 2003**



# Real GDP Index

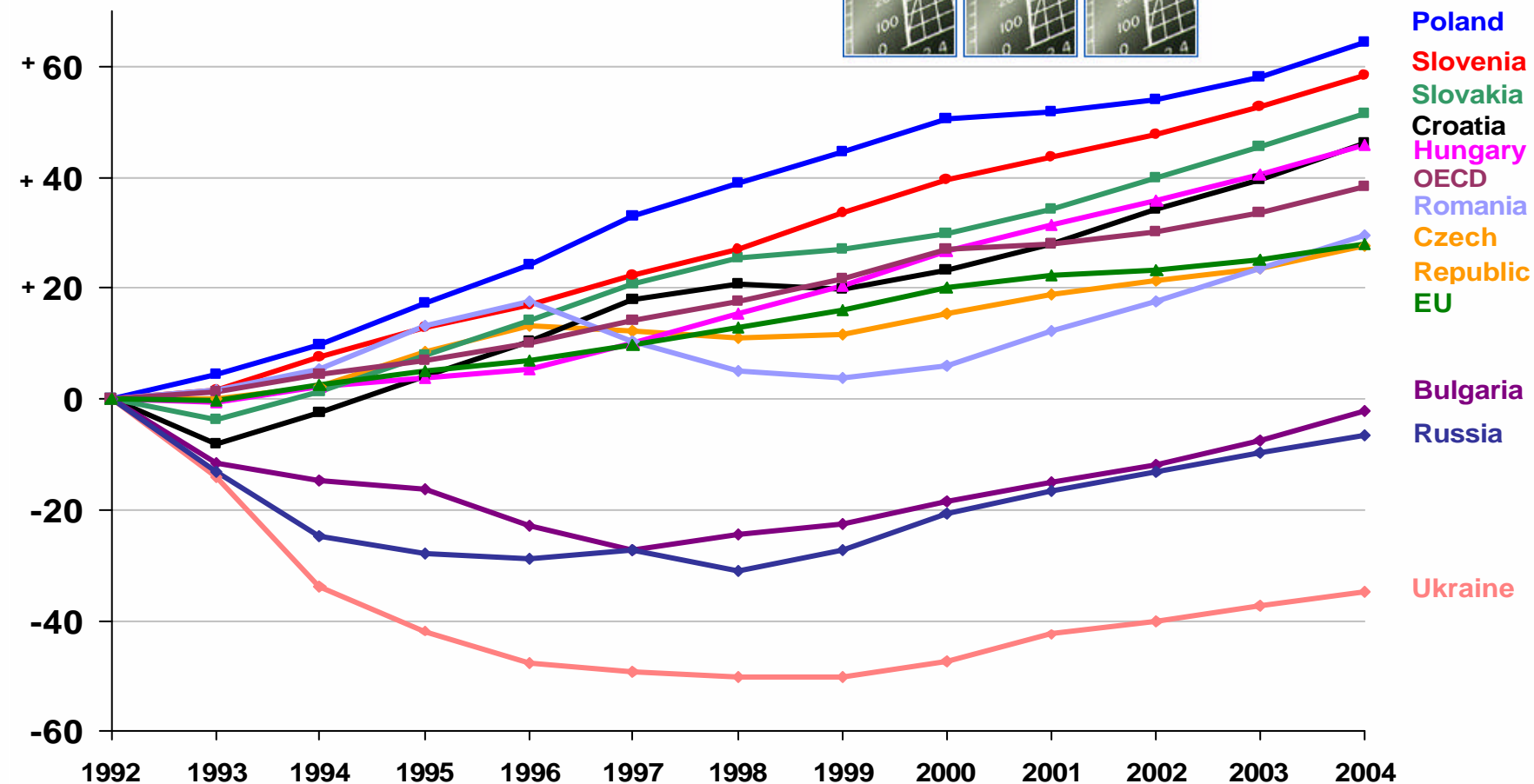
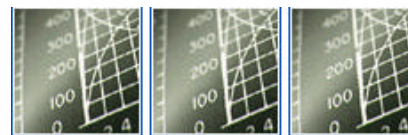
(1989 Base Year)



Sources: William Davidson Institute based on various EBRD Transition Reports, OECD Economic Outlook Vol. 72, and Davidson Institute Forecasts


# Real GDP Index

(1992 Base Year)



# Government Budget Balance

(as % of GDP)



	1995	1996	1997	1998	1999	2000	2001	2002*
Croatia	-1.4	-1.0	-1.9	-1.0	-6.5	-7.1	-5.8	-4.6
Czech Republic	-4.9	-4.3	-4.5	-5.0	-6.1	-3.2	-2.9	-5.2
Hungary	1.1	-1.6	-1.2	-6.5	-3.2	-3.5	-5.2	-9.7
Poland	-2.4	-2.4	-1.3	-2.4	-2.0	-2.2	-4.3	-5.1
Slovak Republic	0.4	-1.4	-4.0	-4.0	-3.2	-3.1	-4.0	-4.8
Slovenia	-0.3	-0.2	-1.7	-1.4	-0.9	-1.3	-1.2	-2.9
Estonia	-0.6	-1.9	2.2	-0.3	-4.6	-0.7	0.4	-1.0
Latvia	-3.9	-1.8	0.3	-0.8	-3.9	-3.3	-1.8	-2.5
Lithuania	-4.5	-4.5	-1.8	-5.9	-8.5	-2.7	-1.7	-1.4
Albania	-10.1	-12.1	-12.6	-10.4	-11.4	-9.1	-9.2	-8.0
Bulgaria	-5.6	-10.4	-3.0	1.0	-0.9	-1.0	-0.9	-0.7
Romania	-4.1	-4.9	-3.6	-2.8	-2.5	-3.6	-3.1	-2.8
Russia	-4.5	-6.9	-6.0	-4.6	-1.2	2.4	3.0	1.7
Ukraine	-6.1	-3.2	-5.4	-2.8	-2.4	-1.3	-1.6	-1.8
EU	-5.4	-4.3	-2.5	-1.7	-0.7	0.8	-1.0	-1.9

\*Estimate

Source: EBRD Transition Report May 2003; IMF World Economic Outlook April 2003



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# External Debt

(as % of GDP)

	1993	1996	1999	2000	2001
Croatia	14.8	32.3	44.1	54.3	54.5
Czech Republic	24.3	36.0	42.6	42.8	39.0
Hungary	63.7	61.9	56.6	67.3	57.1
Poland	54.9	35.3	42.1	42.9	34.8
Slovak Republic	26.6	38.8	53.4	56.3	55.6
Slovenia	14.8	21.1	26.9	34.3	36.8
Estonia	13.8	35.2	55.4	61.4	55.4
Latvia	16.3	40.7	57.4	65.9	36.7
Lithuania	12.2	26.4	42.5	42.9	30.0
Albania	78.9	27.3	26.6	27.5	na
Bulgaria	127.7	97.7	80.5	86.4	78.3
Romania	16.1	23.6	26.6	27.0	25.1
Russia	43.7	39.4	96.7	68.1	55.1
Ukraine	12.8	19.9	39.4	32.6	32.4

Sources: William Davidson Institute based on EBRD Transition Report 2002, World Bank World Development Indicators 2002, DataStream International (EIU), ISI Emerging Markets



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# Consumer Price Inflation

(annual percentage change)

	1991	1993	1995	1997	1999	2001	2002	2003*
Croatia	123.0	1,516.6	2.0	3.6	4.1	6.2	2.2	3.0
Czech Republic	52.0	20.8	9.1	8.5	2.1	4.7	1.8	1.6
Hungary	35.0	22.5	28.2	18.3	10.0	9.2	5.1	4.8
Poland	70.3	35.3	27.8	14.9	7.3	5.5	1.8	1.8
Slovak Republic	61.2	23.2	9.9	6.1	10.6	7.1	3.3	8.8
Slovenia	117.7	32.9	13.5	8.4	6.1	8.4	7.5	6.4
Estonia	210.5	89.8	29.0	11.2	3.3	5.8	3.6	3.4
Latvia	172.2	109.2	25.0	8.4	2.4	2.5	1.9	2.6
Lithuania	224.7	410.4	39.6	8.9	0.8	1.3	0.3	1.2
Albania	35.7	85.0	7.8	33.2	0.4	3.1	5.3	3.0
Bulgaria	333.5	73.0	62.0	1,082.0	0.7	7.4	5.8	4.2
Romania	161.1	256.1	32.3	154.8	45.8	34.5	22.5	16.2
Russia	92.7	875.0	197.7	14.7	86.1	20.7	16.0	13.4
Ukraine	91.0	4,743.0	377.0	15.9	22.7	12.0	-0.7	4.9
EU	5.2	3.9	2.9	1.9	1.4	2.5	2.3	2.2

\* William Davidson Institute Forecast (except for Croatia, Albania, Romania and EU)  
Source: William Davidson Institute, IMF World Economic Outlook April 2003, EBRD  
Transition Report May 2003 and OECD Economic Outlook Vol. 72.



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# Foreign Direct Investment

(Net inflows per capita, in Million of US Dollars)

	1990	1992	1994	1996	1998	1999	2000	2001	2002
Croatia	0.0	2.7	23.0	101.7	184.5	325.0	247.0	302.9	221.5
Czech Republic	12.7	94.9	72.6	123.4	348.0	605.2	435.1	468.9	681.6
Hungary	29.8	141.9	106.3	222.1	152.6	169.5	109.5	218.9	149.9
Poland	0.0	7.5	14.1	71.1	128.6	164.2	211.3	168.2	181.1
Slovak Republic	4.5	18.9	44.4	37.2	69.6	130.3	381.8	277.8	648.1
Slovenia	-1.0	56.5	65.5	94.5	125.6	72.4	55.6	169.8	65.8
Estonia	n.a.	51.0	137.7	74.0	395.9	155.2	229.8	251.8	219.0
Latvia	n.a.	10.9	106.1	148.6	121.7	134.0	162.4	124.5	105.5
Lithuania	n.a.	2.2	8.3	40.9	248.2	128.8	101.4	121.6	147.3
Albania	n.a.	6.1	20.4	30.0	13.6	15.3	42.0	65.1	68.9
Bulgaria	0.4	4.7	12.3	16.4	64.2	94.9	121.4	78.1	110.2
Romania	-0.8	3.1	15.0	18.3	92.0	45.5	46.7	51.4	56.6
Russia	n.a.	9.8	2.8	11.2	10.1	9.2	-2.4	13.7	27.5
Ukraine	n.a.	3.3	2.9	9.9	14.6	9.6	11.8	10.6	14.1

Source: Davidson Institute calculations based on the World Bank World Development Indicators 2002 and on the EBRD Transition Report May 2003.



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# Life Expectancy at Birth

(total years)

	1982	1990	1992	1994	1996	1998	2000
Croatia	70.48	72.17	71.24	n.a.	72.37	n.a.	73.28
Czech Republic	70.74	71.67	72.21	72.95	73.77	74.51	74.82
Hungary	69.56	69.30	69.04	69.39	70.30	70.55	71.25
Poland	71.10	70.89	71.09	71.70	72.25	73.00	73.28
Slovak Republic	70.69	70.93	71.80	72.30	72.65	72.57	73.05
Slovenia	70.27	73.25	73.30	73.38	74.43	74.77	75.26
Estonia	69.28	69.48	68.96	66.95	69.84	69.79	70.60
Latvia	69.23	69.27	68.91	66.65	69.35	69.66	70.38
Lithuania	70.78	71.28	70.31	68.70	70.41	71.57	72.62
Albania	69.93	71.21	71.33	72.48	71.68	n.a.	73.99
Bulgaria	71.38	71.37	71.17	70.96	70.76	71.06	71.55
Romania	69.53	69.74	69.78	69.51	69.10	69.30	69.86
Russian Federation	68.02	68.92	67.76	64.03	65.99	66.96	65.34
Ukraine	69.49	70.14	68.88	67.87	67.30	68.22	68.29
Germany	73.07	75.14	75.32	75.96	76.47	77.07	77.43

Source: William Davidson Institute based on World Bank Development Indicators 2002.



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# Assessment -- Central and Eastern Europe

- Transformation recession in the early 1990s
- Fairly rapid growth in most countries since about 1993-94 (later in CIS)
- Able to withstand EU slowdown (at least temporarily)
- Basic transition problems overcome
- Proceeding with integration into the EU
- Small open economies -- will depend on economic growth in the EU unless expand in the US



# Internal Challenges -- CEE

- Maintain high rates of economic growth (catch up)
  - Foreign firms and *de novo* firms often the engine of growth => watch out for SOEs and privatized firms
  - Maintain inflow of FDI, shifting to higher VA investment
  - Question of wage push (ex. Slovenia)?
  - Taxes/cost of doing business (social programs)
  - Invest in higher education (reforms needed)
- Maintain Macro Stability
  - Budget deficit
  - Unemployment
  - Currency fluctuation (Euroization?)



# External Challenge -- CEE

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- How to make EU more dynamic



# Nature of the EU Problem



- Late 1940s - early 1990s: Western Europe catching up with the US in productivity
- Catch-up or overtaking expected in the late 1990s or early 2000s
- Convergence stopped since the mid 1990s



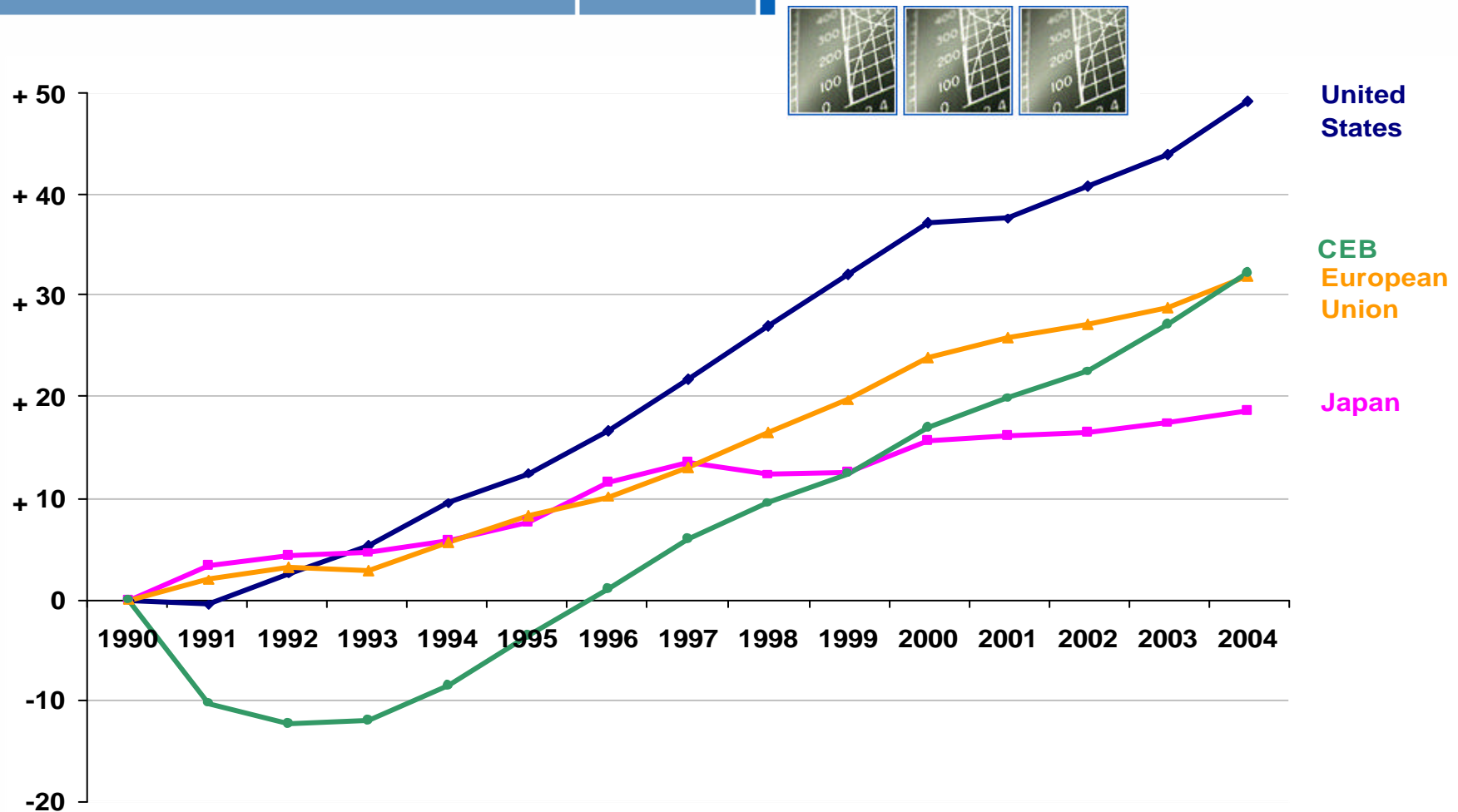
# Second half of the 1990s

- EU's relative position weakened in
  - GDP growth
  - GDP per capita growth
  - Growth in employment
  - Growth in labor productivity
  - Living standards
- Smaller EU states have done better, on average, than larger states in productivity and employment growth



# Real GDP Index

(1990 base year)



Source: IMF World Economic Outlook April 2003 and EBRD Transition Report May 2003



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# Assessment

- Early 1990s -- the US, Europe and Japan reached similar levels of development
- EU and US became similar size economies
- New dimensions increasingly started to matter in a more global world
  - Entrepreneurship & availability of venture capital
  - Regulation (cost of doing business)
  - R&D
  - Human capital
  - Leadership and perception of leadership



# Future Prospects

- The US is at or near its potential – hard to advance
- Japan acts as if paralyzed, unable to act
- Europe faces problems, but it has tremendous unexploited possibilities
  - Largest free trade zone in the world
  - Single currency
  - Increasingly able to act as a unified economic power
- Question: is Europe is ready to realize this potential?





# Key Steps for Europe

- Furthering economic and political integration
- Setting and realizing major goals
  - 2010 knowledge-based competitive challenge
- Being conducive to entrepreneurship and business leadership
- Handling budget deficits and strikes
- Integrating productively (not defensively) Central and East European Countries
- CEE members of the EU need to assume an active role to help EU realize its potential



# Near Term Prospects

- Germany slowing Europe down
- Latin America and Africa are in trouble
- US is the engine of growth among the large countries (2002 GDP growth: 2.5% in the US vs. 1% in Eurozone and decline in Japan)
  - US unemployment rate growing but still only about 6%
  - Inflation extremely low
  - US \$ depreciating vis a vis the Euro and Central and East European currencies => competitive advantage
- China, India, SE Asia and CEE/CIS will be the engines of growth in the emerging markets

