

Comments on “Real Convergence of the EU 27 and Croatia in the period 1995-2017

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What the paper does

- Poses the question of whether real convergence is occurring for transition countries that have already joined the EU and for Croatia
- Looks at the degree of real convergence by
 - Examining output and productivity levels
 - Calculating catch-up rates
 - Estimating unconditional Beta convergence regressions, including panel models
 - Calculating Sigma convergence

What is real convergence and why does it matter

- Often reduced to convergence of GDP per capita
- But there is at least a hint of convergence of economic structures
 - Sectoral (decline of agriculture and to a lesser extent industry, rise of services)
 - Technology levels
 - Preferences and consumption patterns?
- Importance for economic and social cohesion
- Importance for Euro
 - Reduction of asymmetric shocks
 - Nominal convergence (synchronization of cycles, convergence of inflation, interest rates)

Should we expect real convergence?

- Globally, results on real convergence are controversial and ambiguous
- What effects could EU membership have?
 - Increased capital flows due to membership in a free trade area
 - Scale effects of membership in FTA
 - Productivity effects of adoption of European legal and institutional frameworks (*acquis communautaire*)

Note the Krugman critique: divergence due to integration

- Increased integration allows greater specialization due to increased economies of scale
- Due to agglomeration effects, activities are spatially concentrated
- Trade integration does not lead to real convergence but to divergence

Do we expect convergence to accelerate with membership?

- Convergence before membership could be rapid
 - Anticipatory effects (FDI in anticipation of membership)
 - institutional harmonization efforts
- Convergence could slow after membership
 - Reform fatigue
 - Discipline of having to “qualify for membership” weakens
- Convergence could speed up after membership
 - Full implementation of capital and labor mobility
 - Full implementation of acquis (except for derogations)

The Great Recession, the Euro crisis and real convergence

- For most transition countries, the Great Recession started as an export shock
- But with credit growth faster than in old EU, and current account deficits often higher, New Member States may have been more vulnerable to the shock
- A few NMS' have had fiscal crises (Hungary, Latvia, Romania would qualify)
- Well-worth carefully looking at real convergence during the Recession

Some possible modifications to paper: periods and groups

- Break down periods differently
 - Look at 2008-11 separately
- Group countries differently
 - Look at Baltics vs CEE within EU 12
 - Look at EU 10 (remove Malta and Cyprus)
 - For 2008-11, look separately at countries receiving IMF/EU assistance
 - Look at countries in the Euro Area and countries outside (especially interesting 2008-11)

Conditional Beta convergence

- Traditional growth theory variables (Barro and Sala-I-Martin 1994)
 - Macroeconomic stability
 - Educational attainment
 - Trade openness
- Variables tried in Borys et al 2008
 - Institutions/reforms
 - FDI
 - Financial system development

Conditional Beta Convergence—ideas from Marelli and Signorelli

- Simply add one or two variables to the Beta regressions, such as
 - Krugman Specialization Index
 - Education (they use proportion of population aged 25-64 having completed secondary school, available from Eurostat)
- Consider whether convergence is occurring in other important variables such as productivity, employment or unemployment rates.

Correlation coefficients

- Another interesting exercise could be to look at whether there are changes in the relative ranks of countries (Veira 1999).
- One can simply rank the EU 27 + Croatia by GDP at PPS in each year since 1995 and calculate Spearman correlation coefficients with the initial year or the previous year.

The way forward

- Enough time has passed to update and modify Borys (2008) and/or Marelli and Signorelli (2009)
- Remove some of the more descriptive parts of the paper and add some new ones
- Skeptical about usefulness of projections to 2017