Central,
Eastern and
Southeastern Europe

Convergence:

ARE WE THERE YET?

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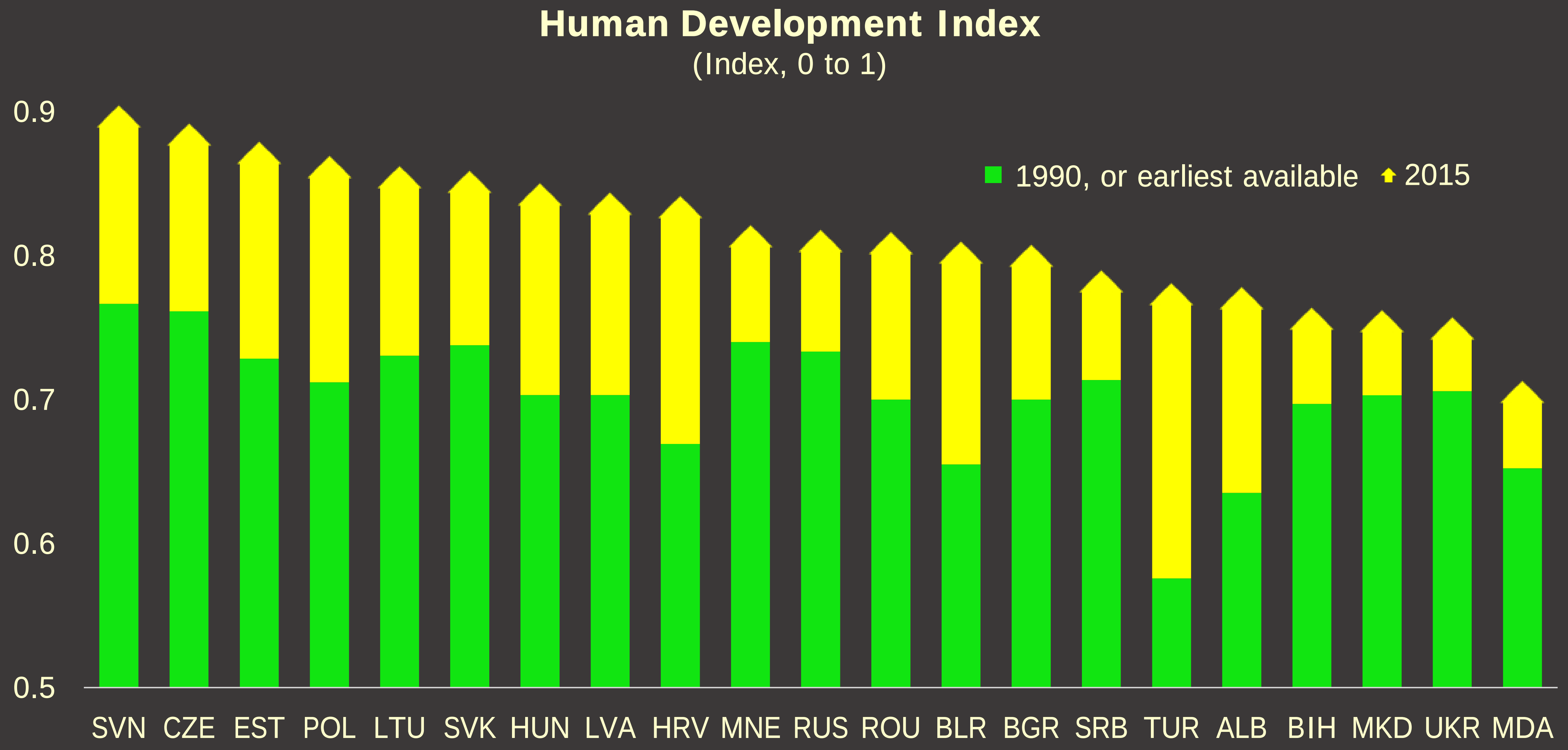
IMF – Croatian National Bank
Conference
Dubrovnik, 11 July 2017

1990s

NOW

Substantial progress has been made since 1990

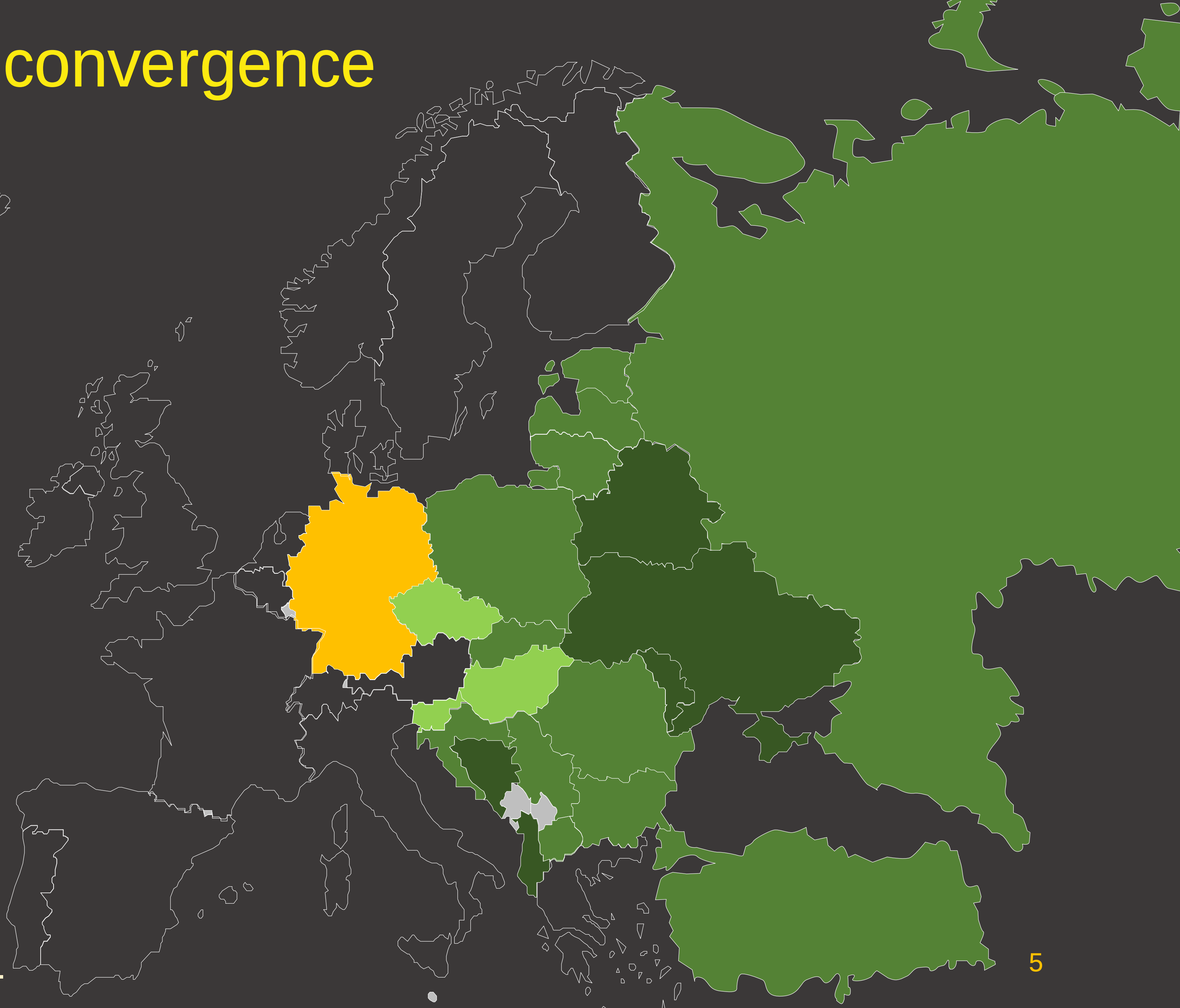


Source: UNDP Human Development Reports, Table 2: Trends in the Human Development Index, 1990-2015.

Substantial income convergence has been achieved

PPP GDP per capita compared to Germany’s

1995



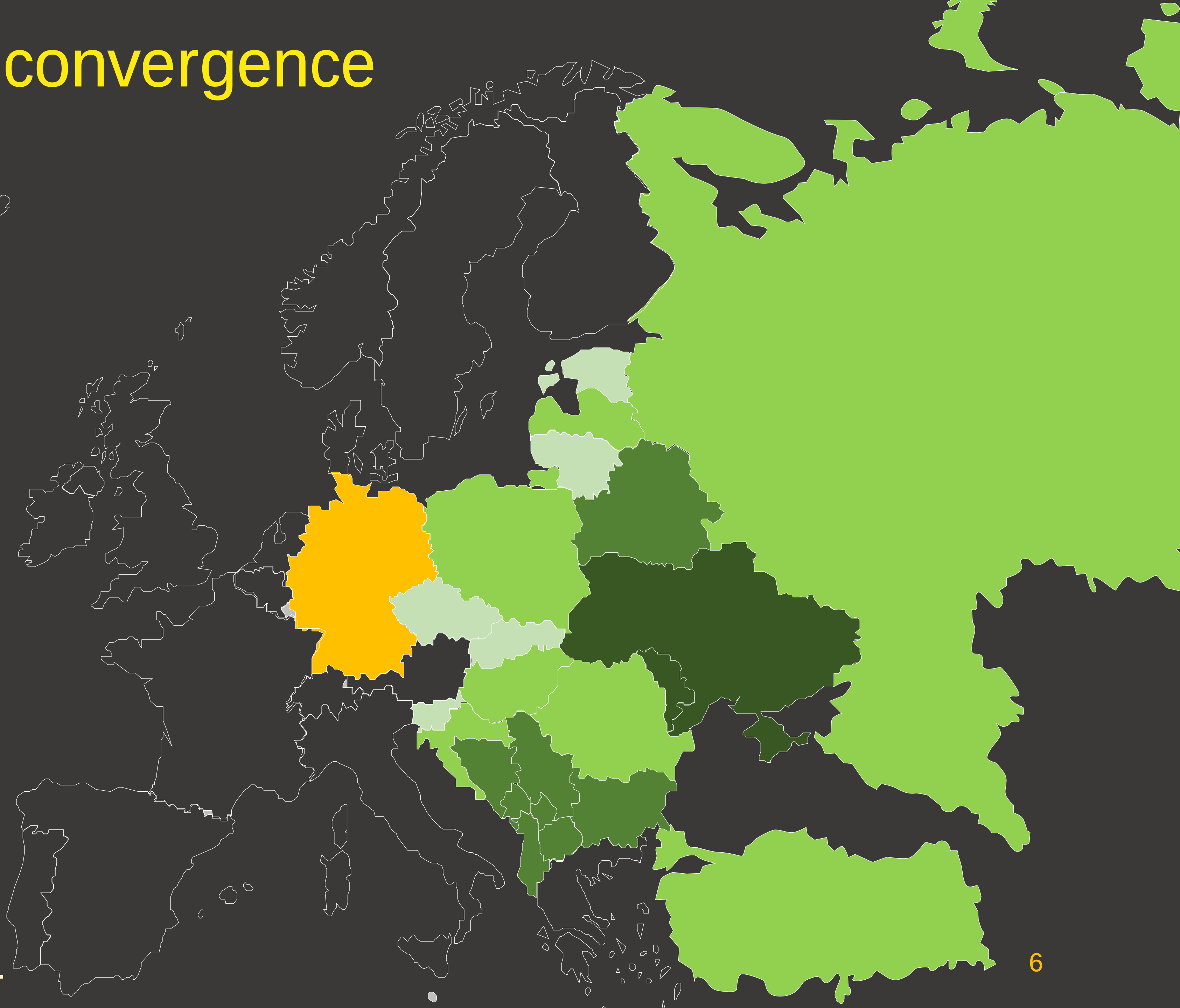
- Below 20 percent
- Between 20 and 40 percent
- Between 40 and 60 percent
- Above 60 percent

Source: World Bank Development Indicators.

Substantial income convergence has been achieved

PPP GDP per capita compared to Germany's

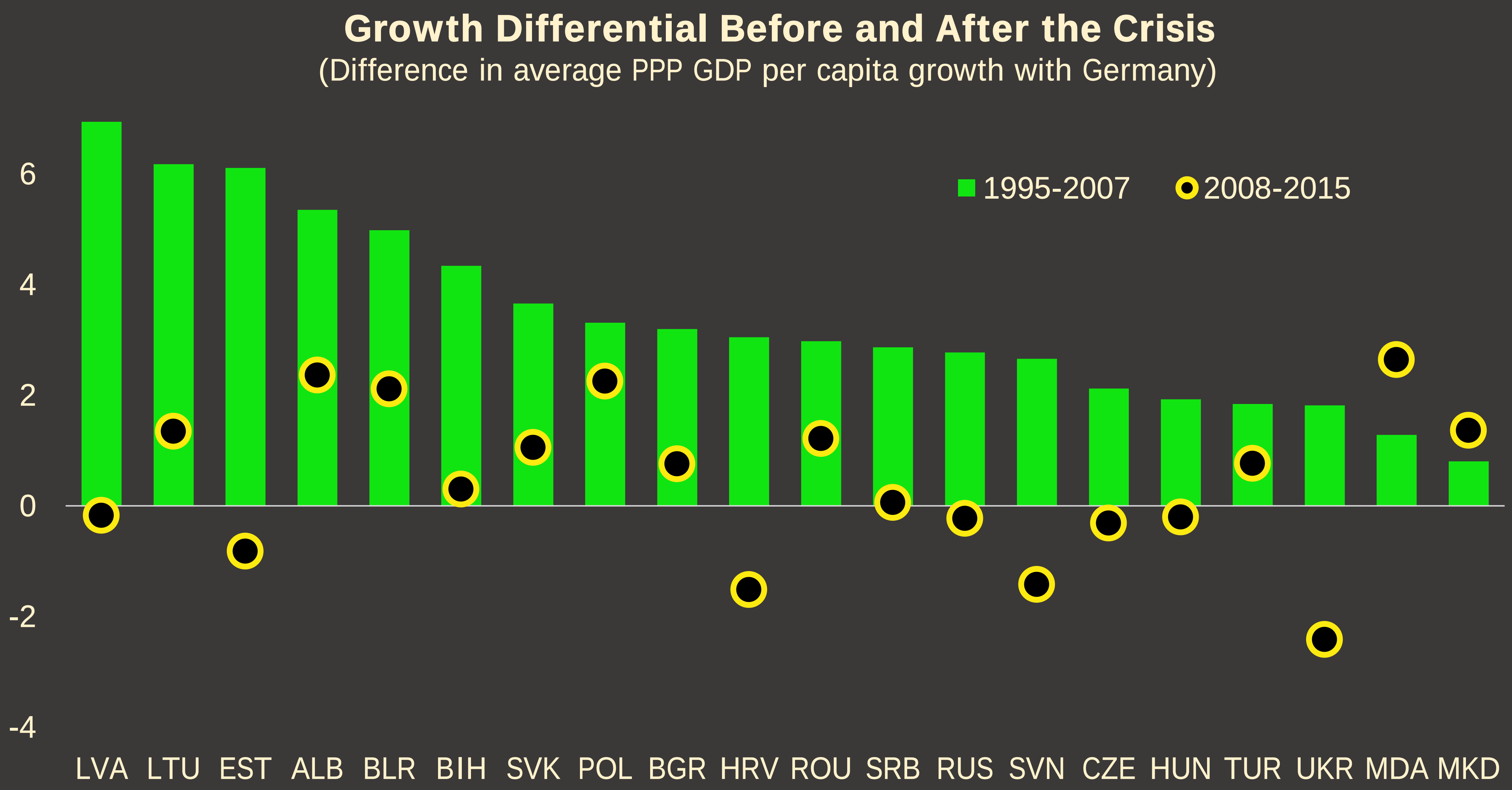
2015



- Below 20 percent
- Between 20 and 40 percent
- Between 40 and 60 percent
- Above 60 percent

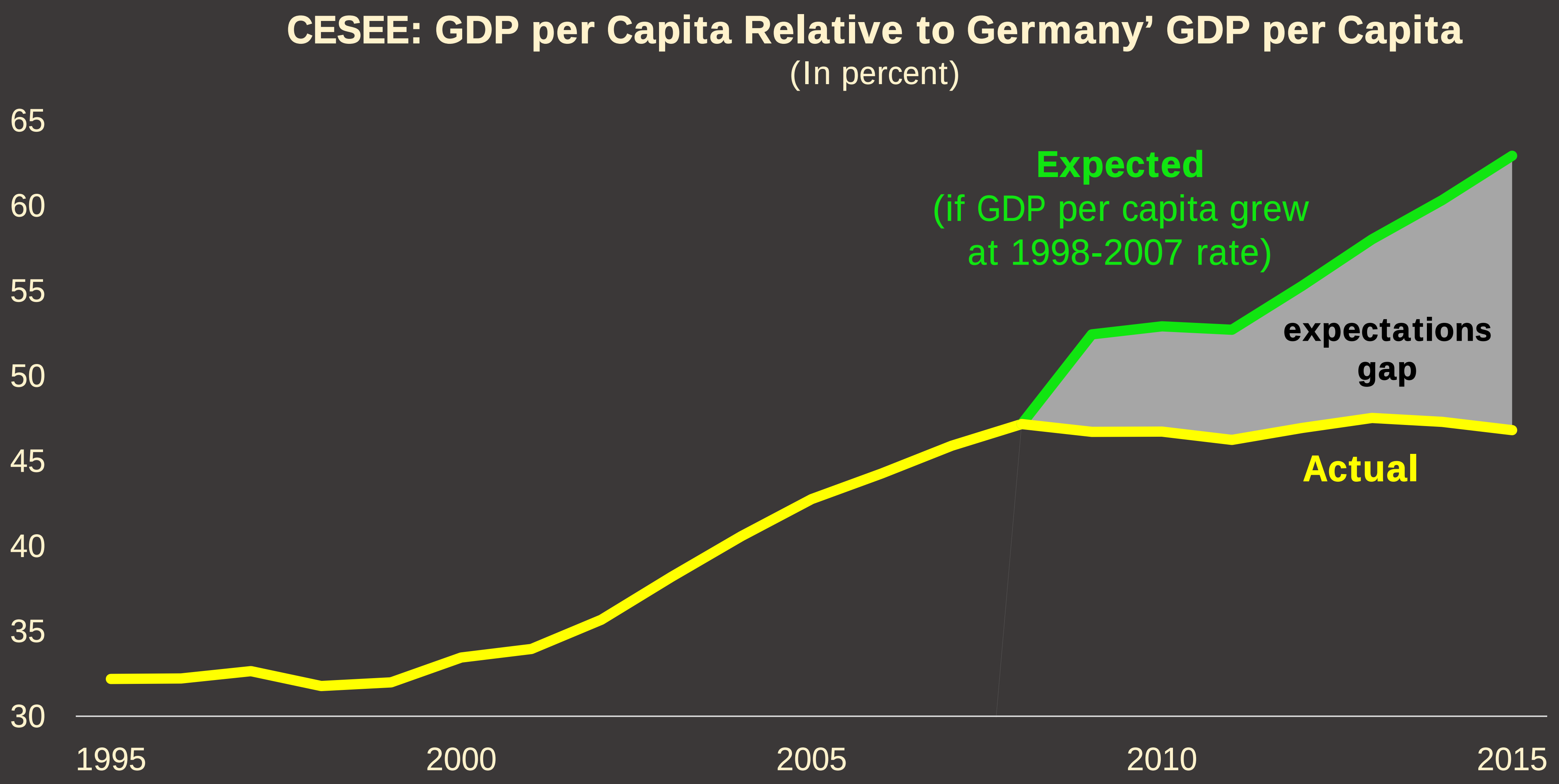
Source: World Bank Development Indicators.

But convergence has slowed. Some divergence



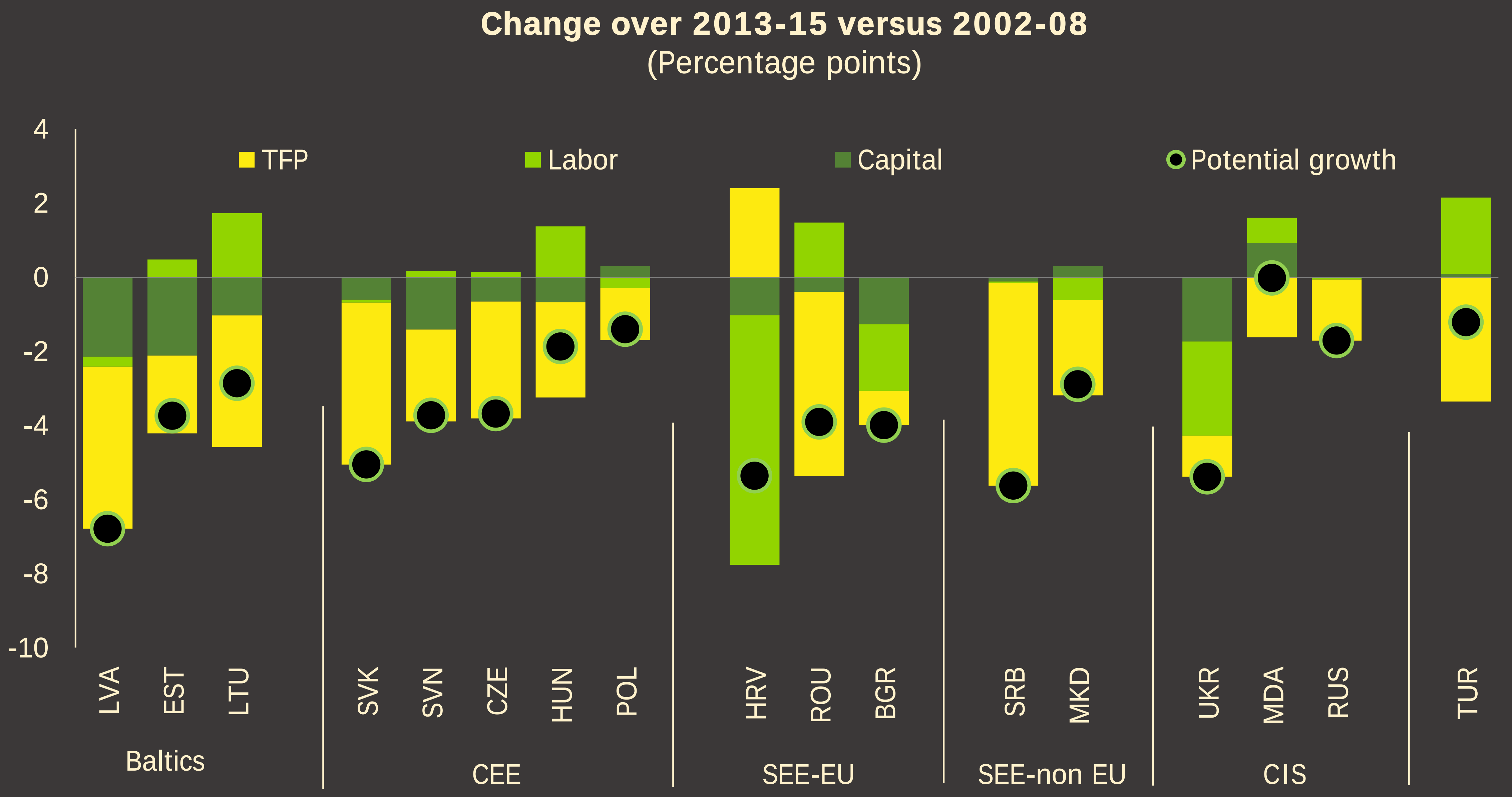
Sources: World Bank Development Indicators; and IMF staff calculations.

People have been disappointed



Sources: World Bank Development Indicators; and IMF staff estimates.

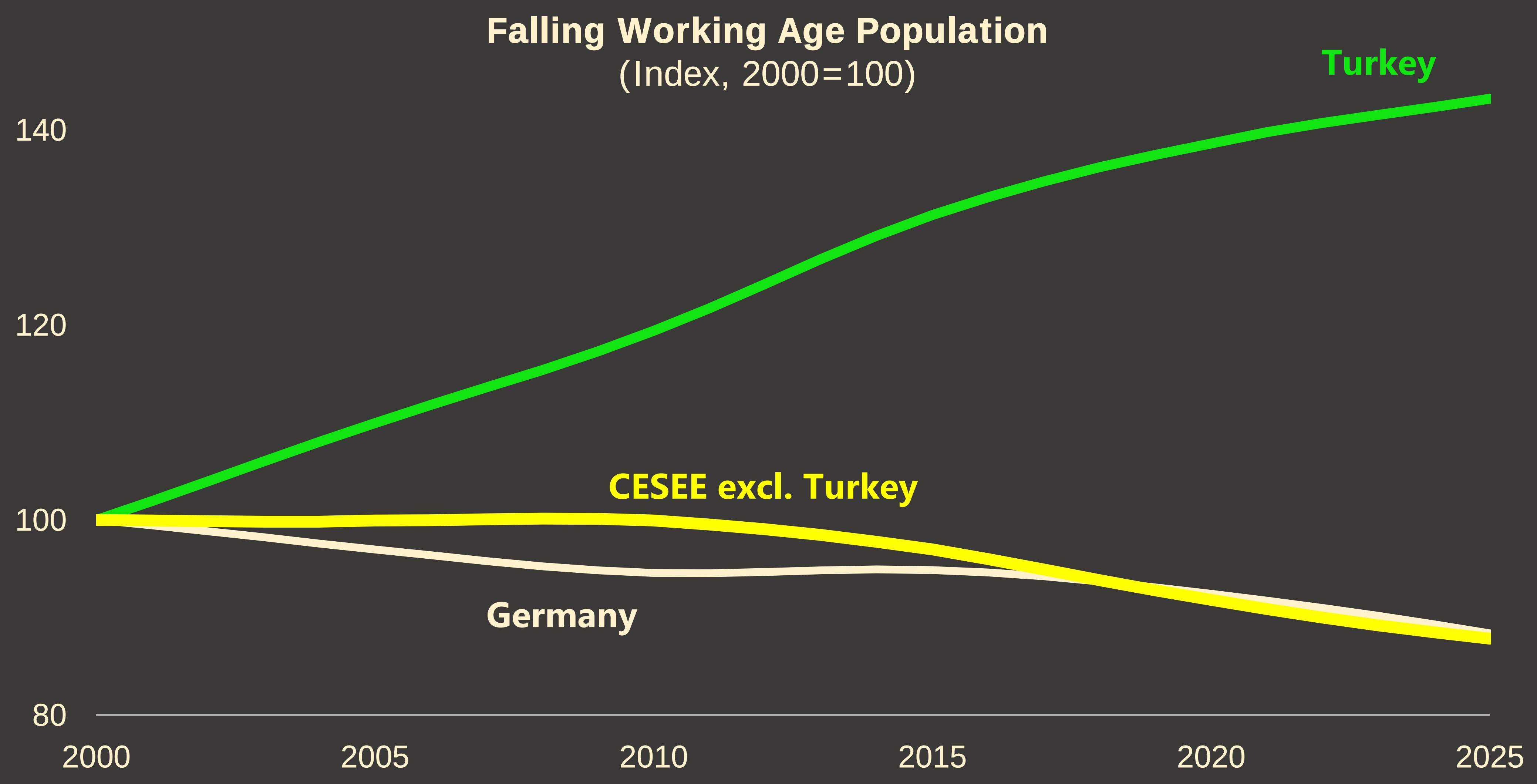
TFP behind the growth slowdown



Sources: Penn World Tables, Version 8.1; Haver Analytics; and IMF staff calculations.


Head winds

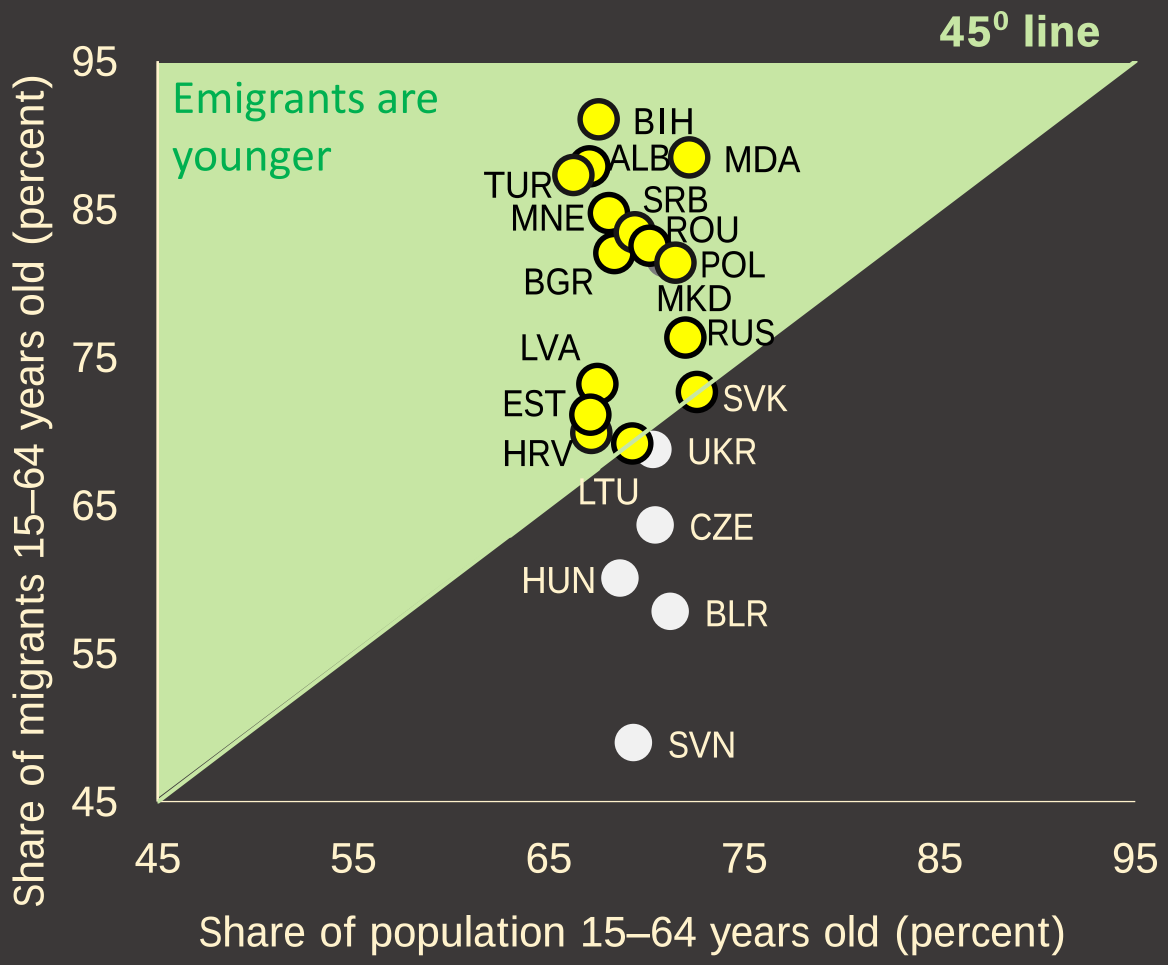
Major demographic headwinds ahead



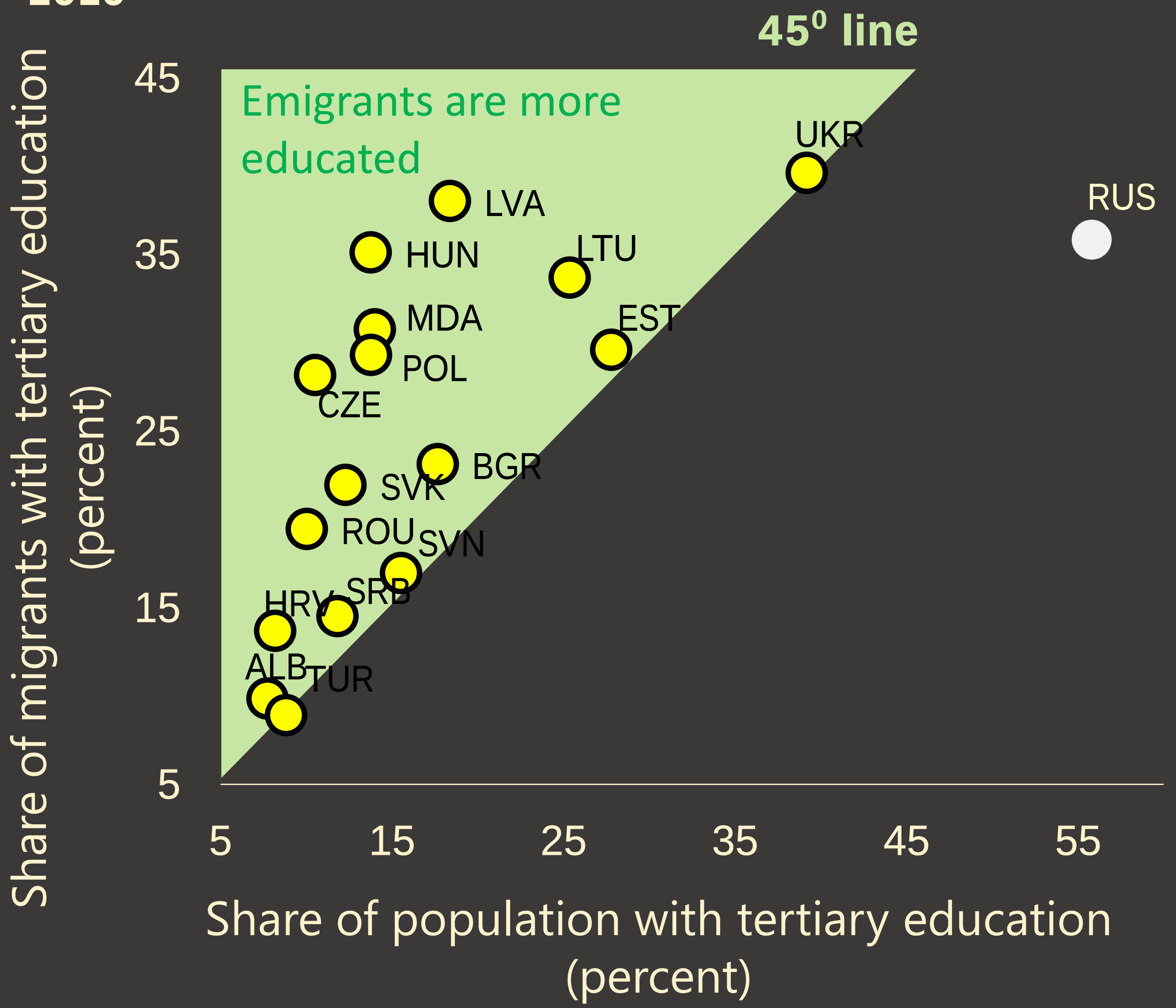
Source: United Nations World Population Prospects (2015).

Will emigration continue?

Age of Migrants and Sending Country Population, 2010

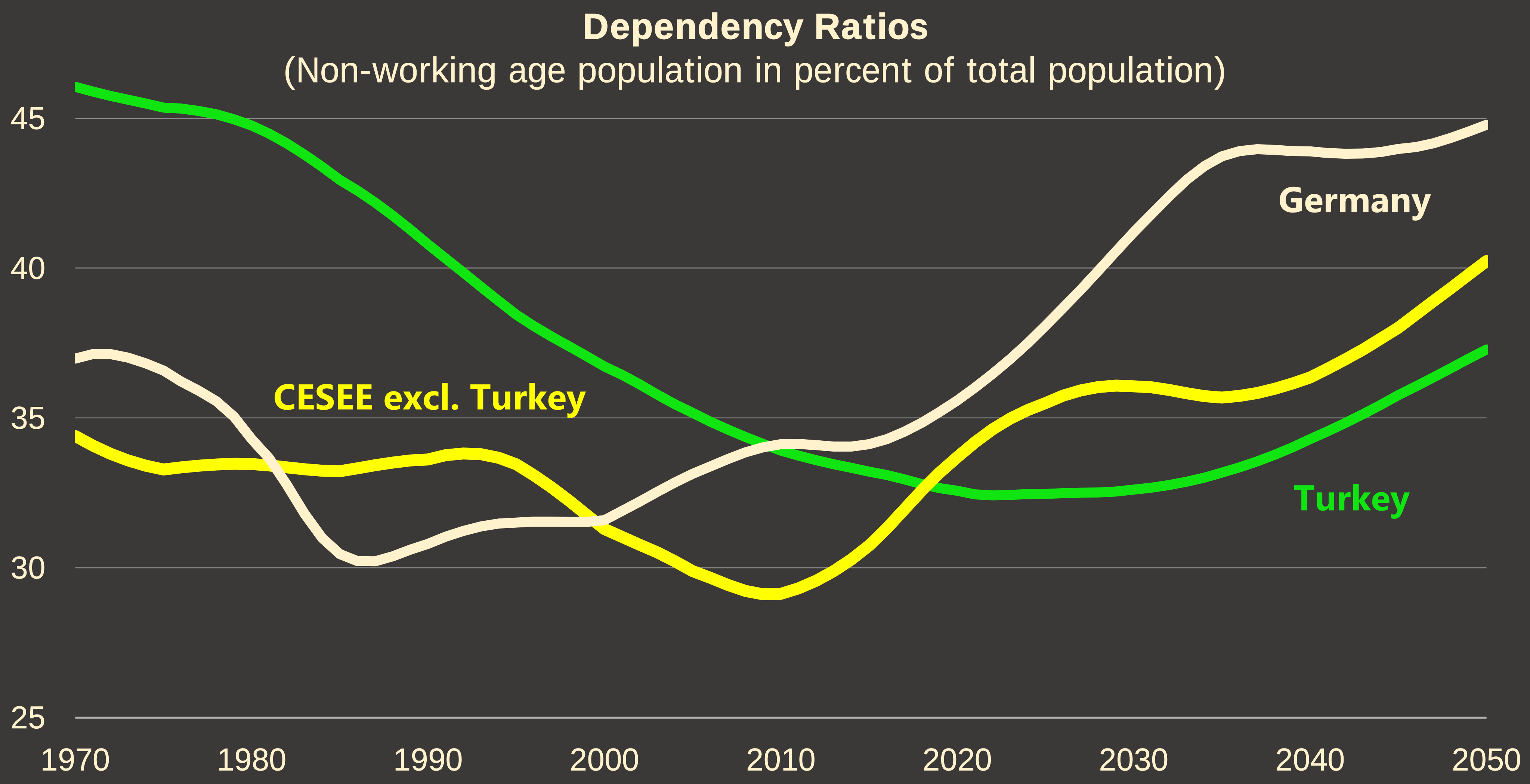


Education of Migrants and Sending Country Population, 2010



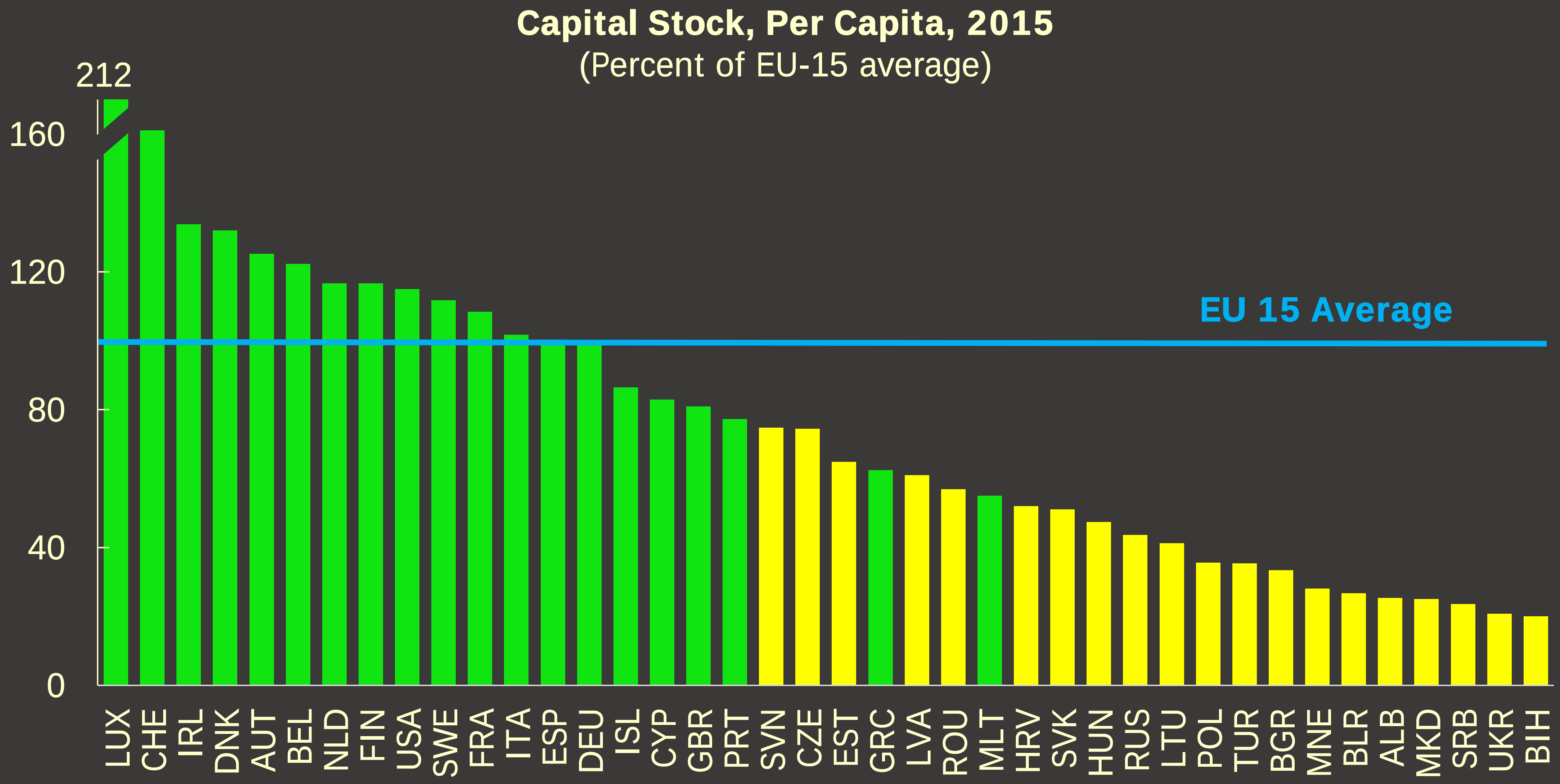
Sources: OECD Database on Immigrants in OECD Countries (2010); and World Bank World Development Indicators.

Rising dependency ratios lower saving



Source: United Nations World Population Prospects (2015).

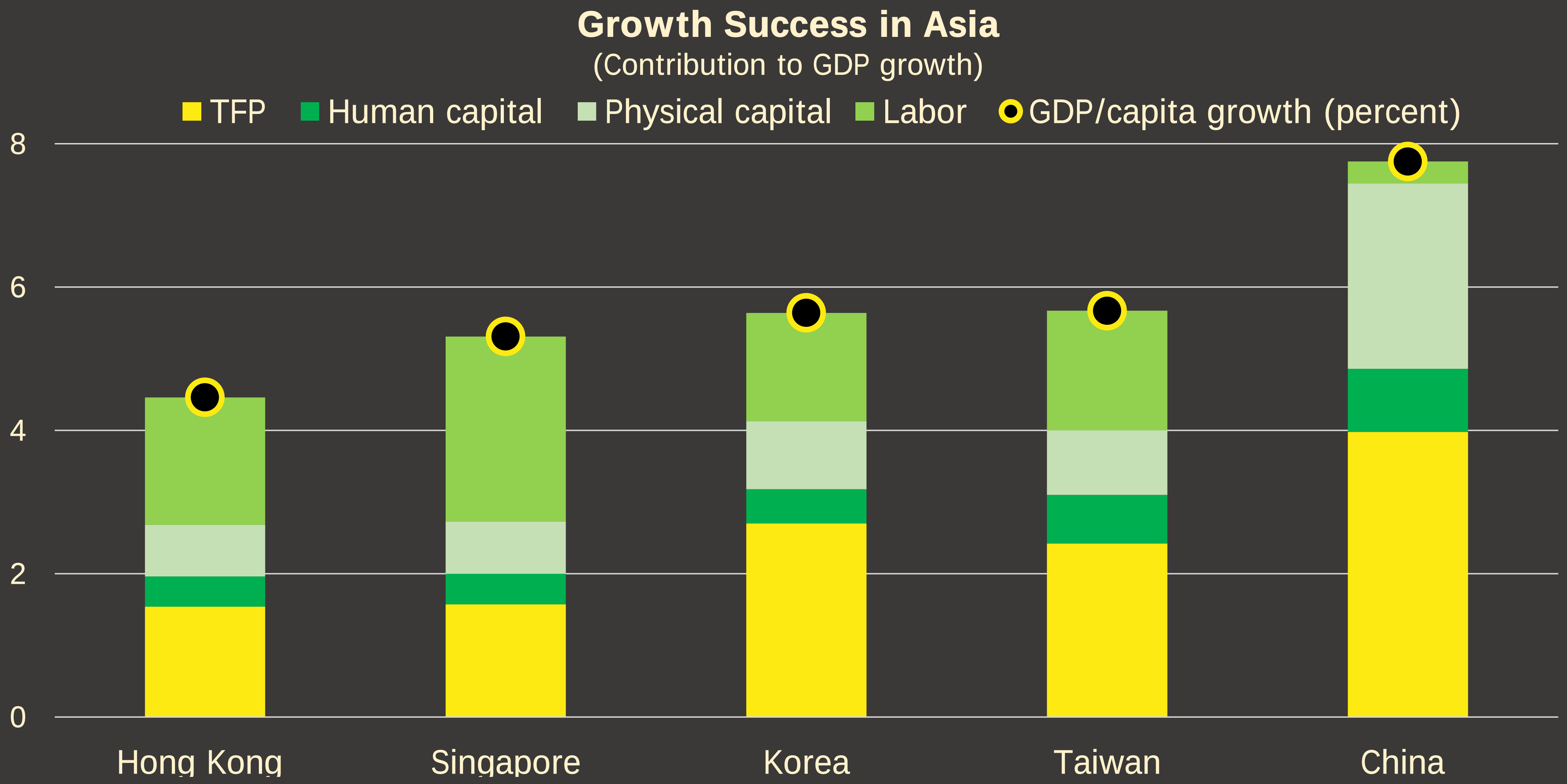
Investment is likely to remain weak



Sources: IMF Investment and Capital Stock Dataset; World Economic Outlook; and Eurostat.

Examples of convergence from Asia

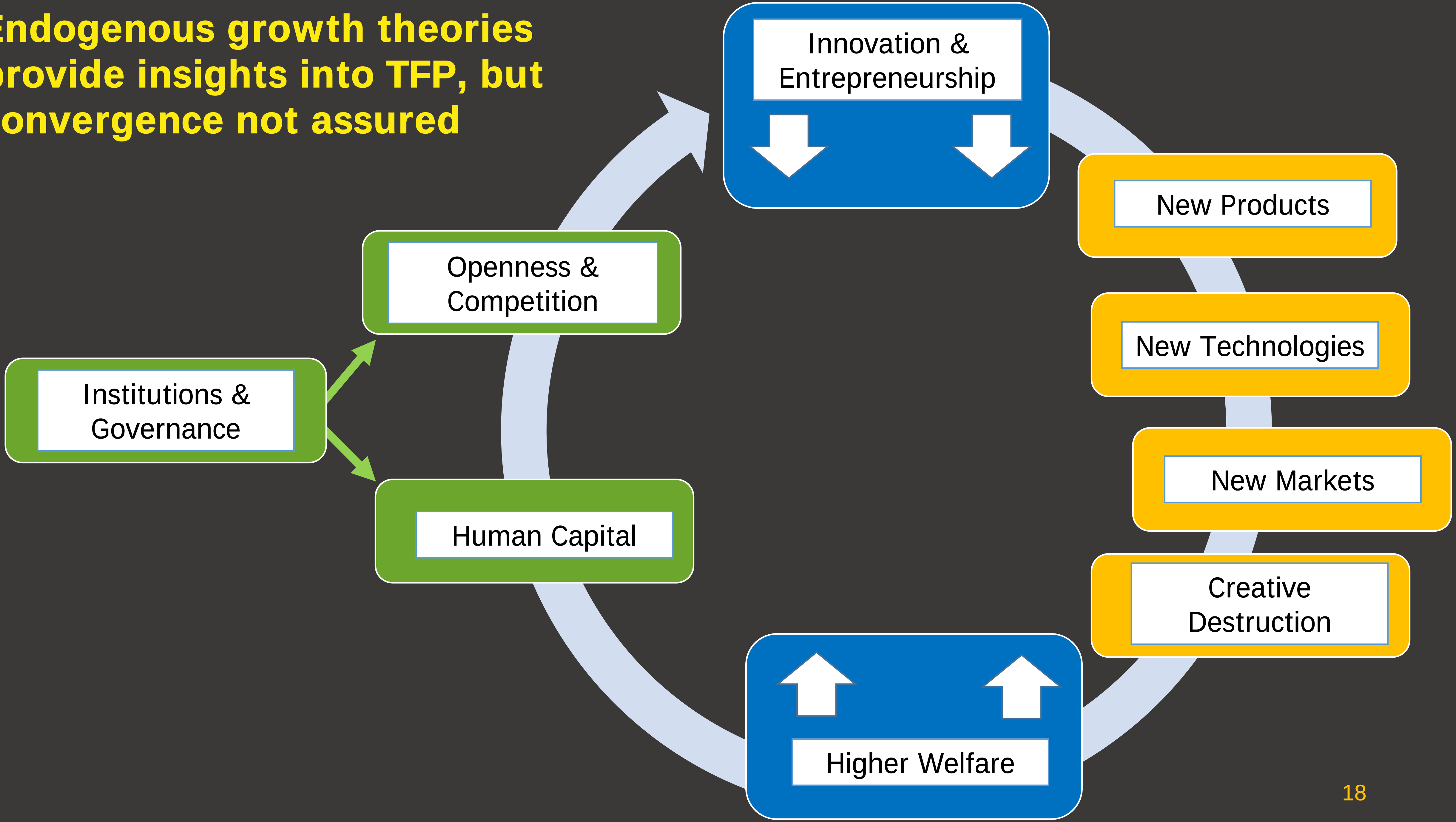
Sustained convergence requires robust TFP growth



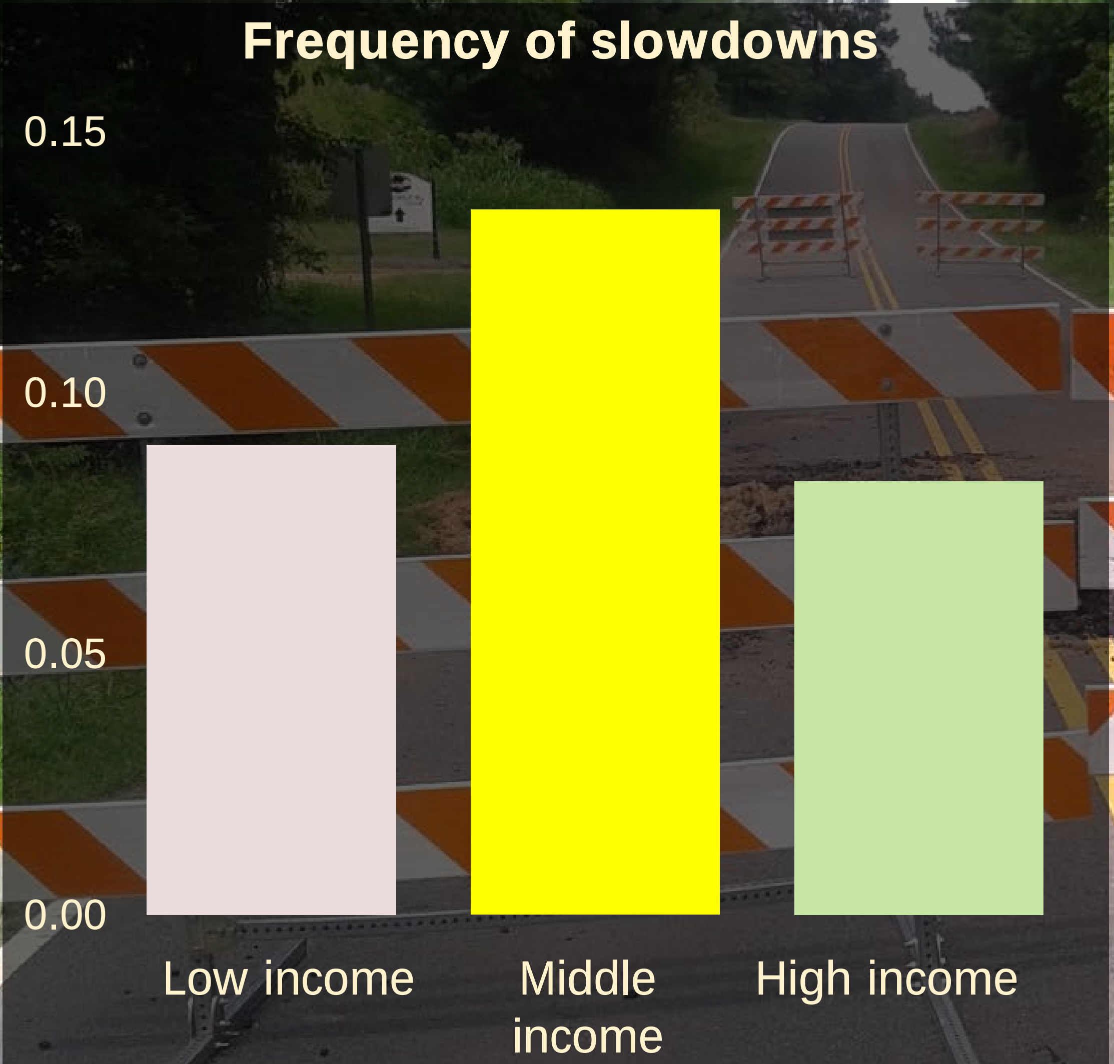
Sources: Aiyar and others, 2013, “Growth Slowdowns and the Middle Income Trap” , IMF WP/13/71; and IMF staff estimates.


HOW
TO INCREASE TFP?

Endogenous growth theories provide insights into TFP, but convergence not assured



IS THERE A MIDDLE INCOME TRAP?

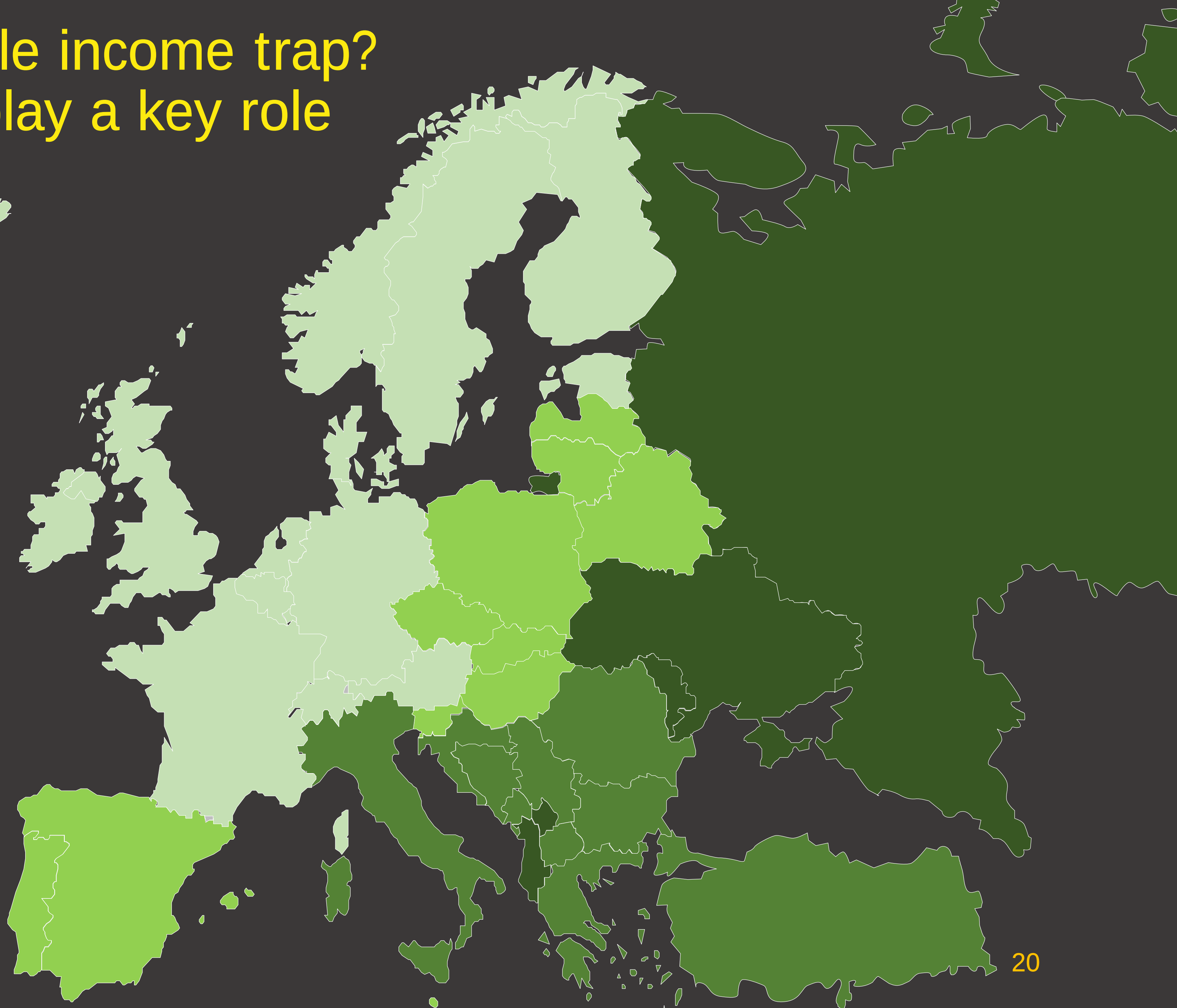


Source: Aiyar and others, 2013, “Growth Slowdowns and the Middle Income Trap” , IMF WP/13/71.

How to escape the middle income trap? Better governance can play a key role

Rule of Law,
Worldwide distribution,
2015

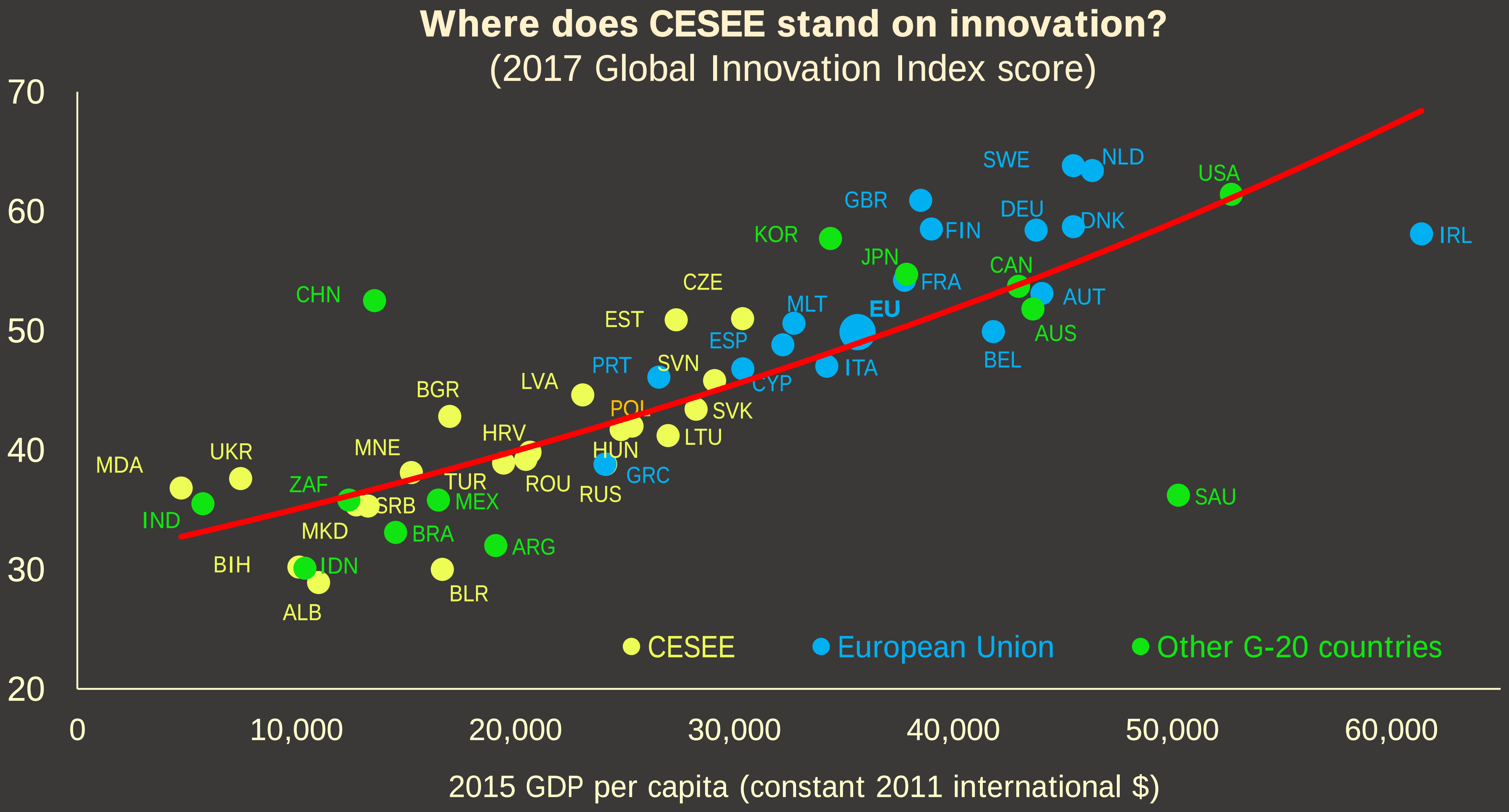
Lighter green is better



- Below 25 percentile
- Between 25 and 50 percentile
- Between 50 and 75 percentile
- Above 75 percentile

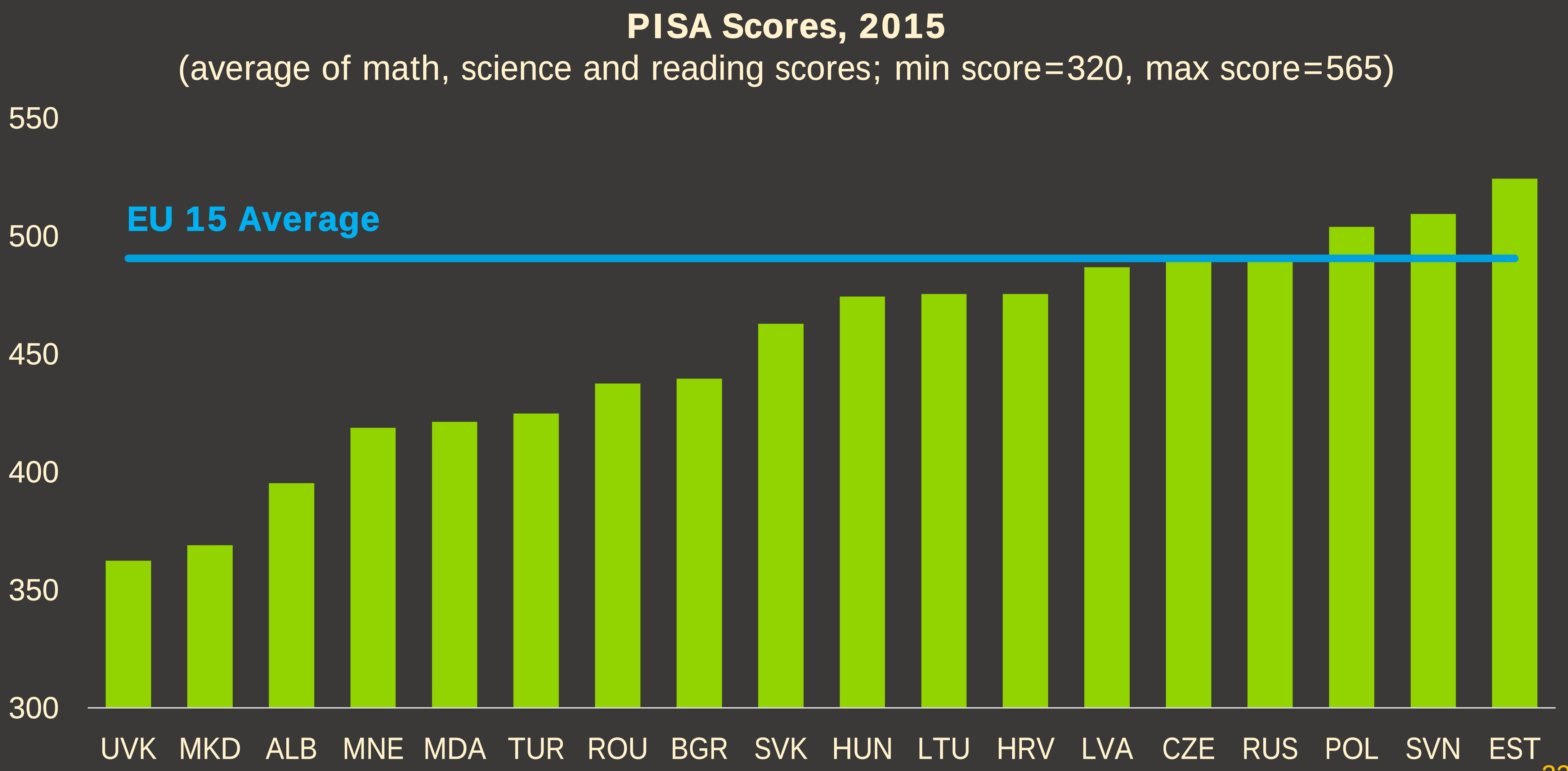
Source: World Justice Project.

The link between institutions and innovation



Sources: Global Innovation Index Report (2017); and World Bank Development Indicators.

Most of the region has a well educated labor force, which is more sensitive to institutions

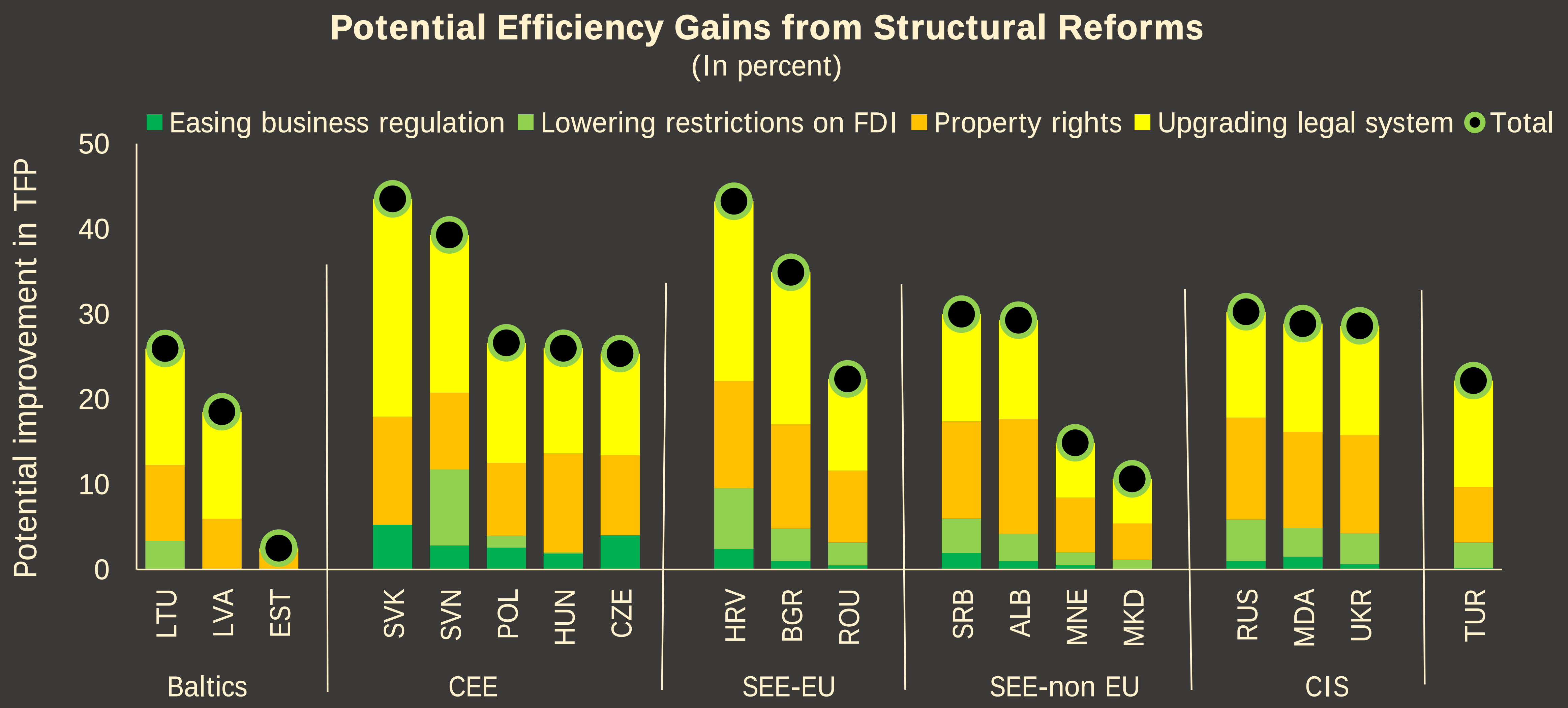


Source: OECD.

The importance of competition in fostering TFP

Source: World Economic Forum.

More effective legal systems key for moving to a higher growth trajectory



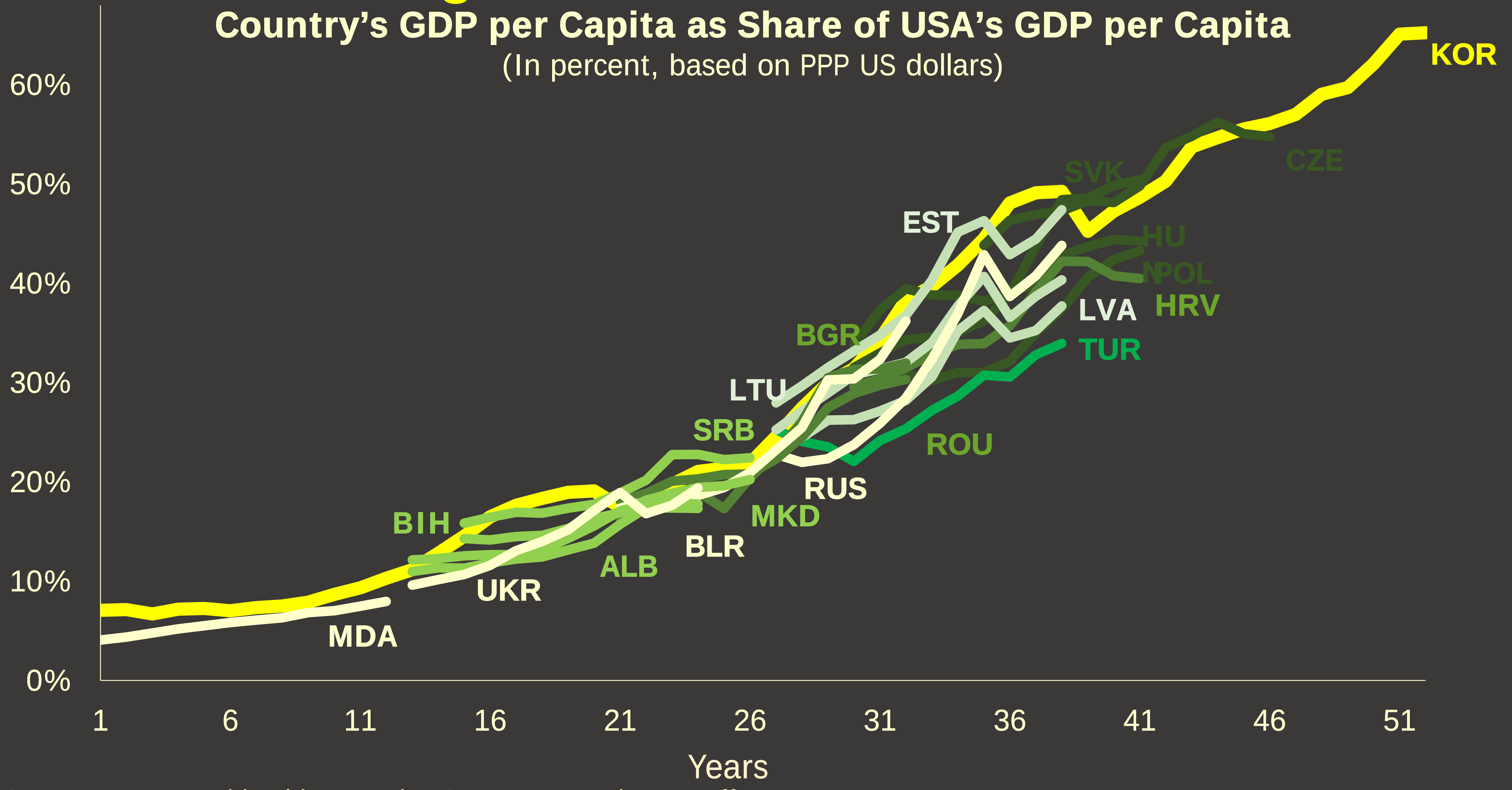
Sources: Penn World Tables, Version 8.1; and IMF staff calculations.

Key messages

- A lot of progress achieved, but convergence not assured
- Strong demographic headwinds ahead
- Productivity growth needed for higher incomes
- Better governance and institutions key to increasing productivity and spurring innovation
- Retaining/attracting skilled workers and fostering competition are the main economic channels through which governance helps

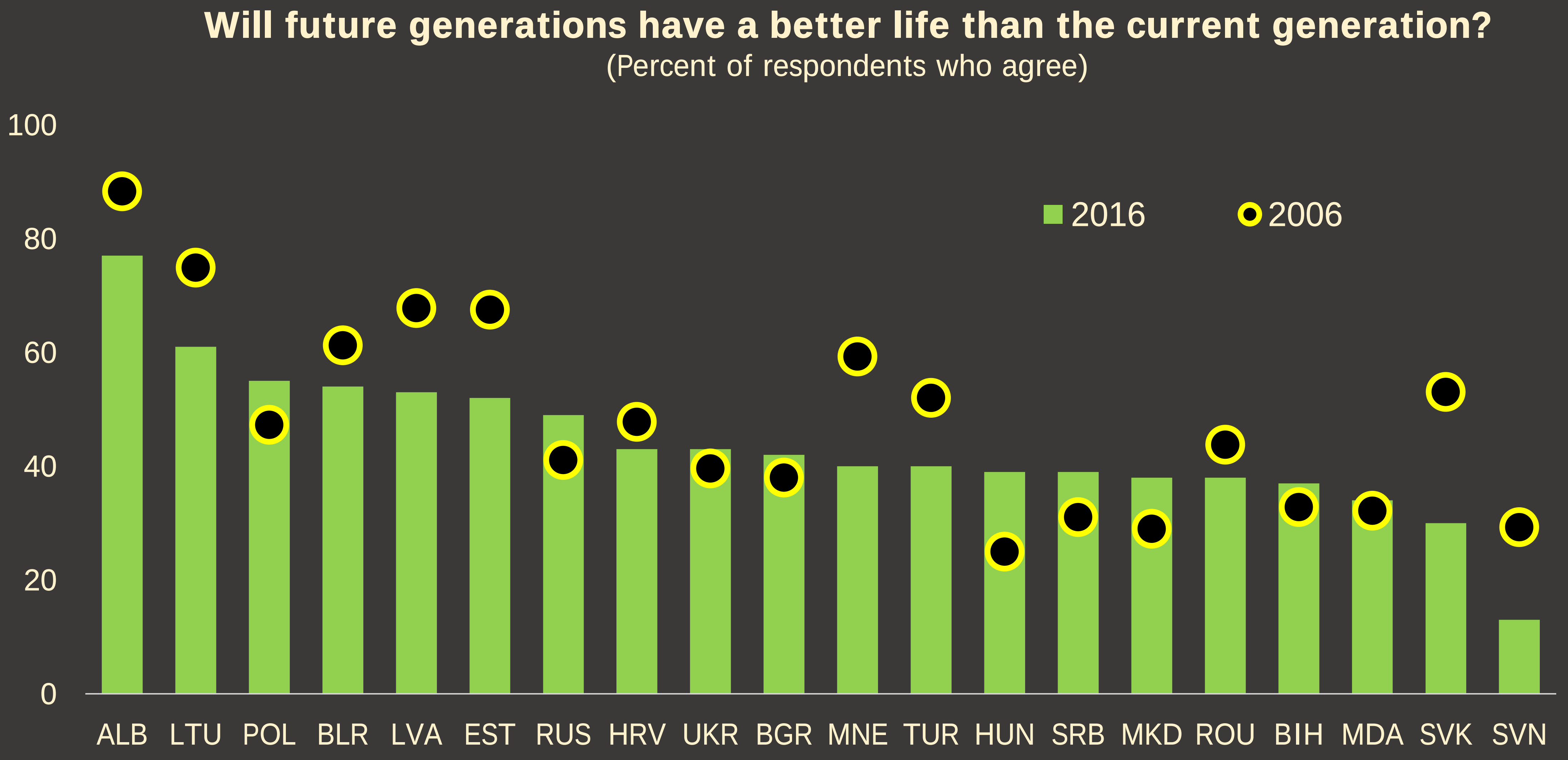
Additional Slides

CESEE: Convergence



Sources: Penn World Tables, Version 8.1, Haver, and IMF staff.
Note: Each short line represents the transition path of a CESEE country over 2000-2011. The position of each CESEE line shows how its transition path compared to Korea's, when Korea was at the similar level of development. The x-axis represents years of Korea's transition from 1960 to 2011.

People have mixed expectations about the future

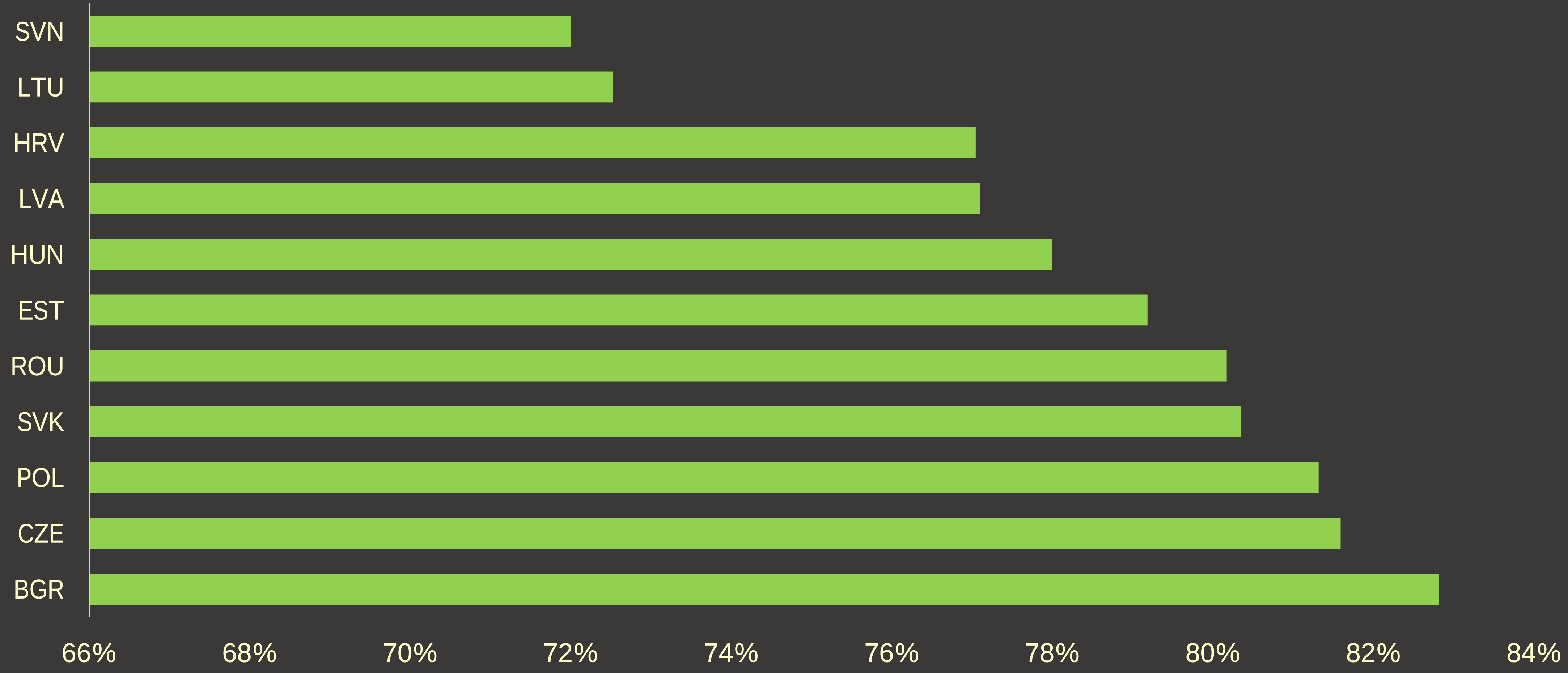


Source: EBRD Life in Transition Survey.

Investment

Reported Adequacy of Investment in the Last 3 Years

(Percent of all firms who report investing about right or more)



Source: European Investment Bank.