Wiener Institut für Internationale Wirtschaftsvergleiche

The Vienna Institute for International Economic Studies

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Central Europe's Convergence: 10th NBP CoFEE

Convergence in EU-CEE: A growth model reaching its limit

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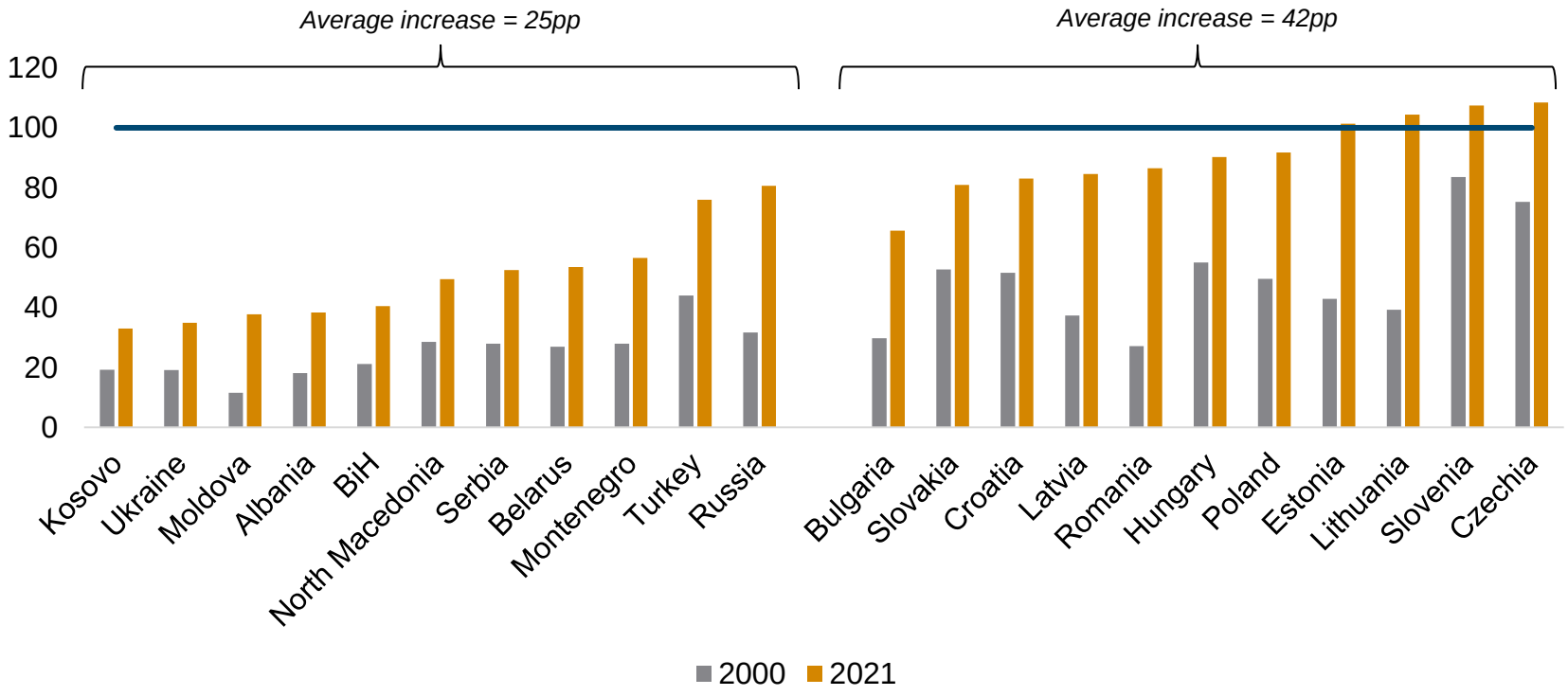
1. Both in level and speed of convergence since 2000, EU-CEE is the outperformer in CESEE, partly due to EU

Per capita GDP, PPS, Spain = 100



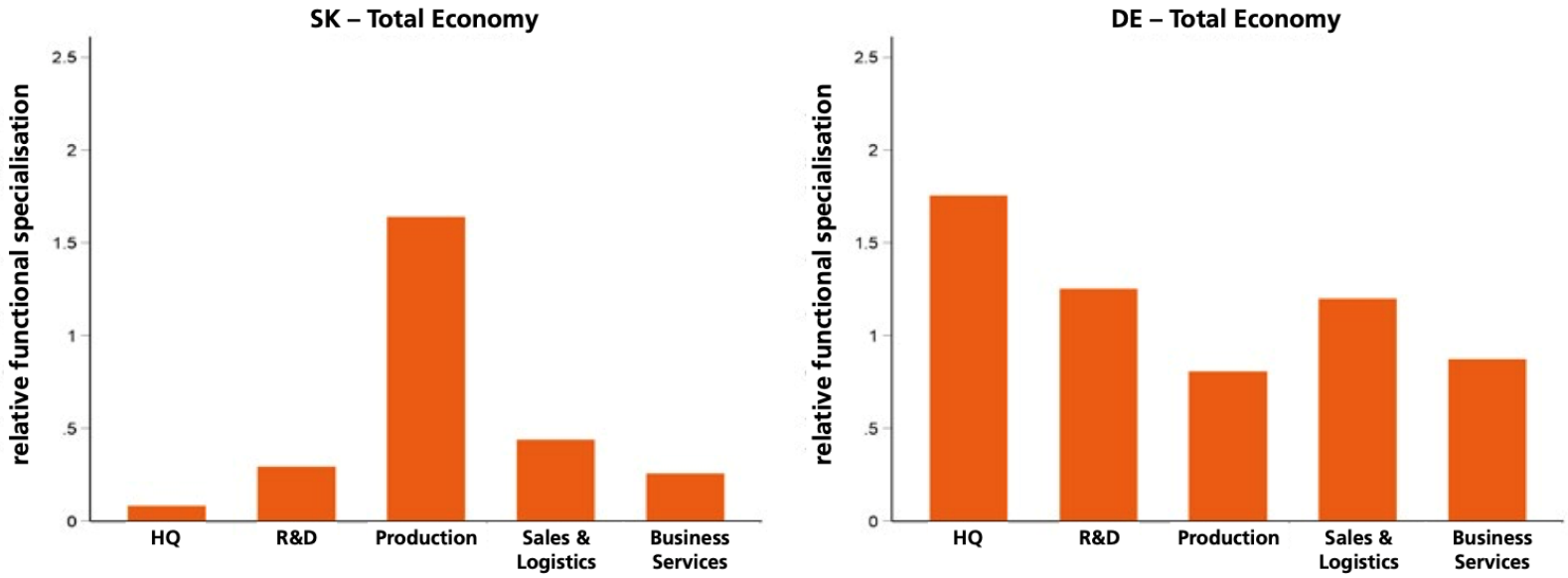
Sources: Eurostat, national sources, wiiw.

2. But…narrow + somewhat unbalanced model of convergence, with cracks appearing since 2008

- FDI-driven growth: Integration into CE manufacturing core, sophisticated + globally competitive export sector
- But convergence has slowed since 2008 (labour productivity)
- Disquiet about unequal spread of gains
- Big income gap versus Germany = outflow of EU-CEE population = labour shortages
- Lack of big spill-overs from FDI for domestic economy
- Institutional convergence has slowed (in some parts of EU-CEE in reverse)

3. Functional specialisation patterns suggest development „trap“ + indicate strong need for adaptation + innovation

Slovakia and Germany: Examples for functional complementarities in the EU, all industries, average 2003–2020



Note: The functional profiles are the relative functional specialisation (RFS) measures (relative to the EU average) based on jobs created by the inwards FDI projects in each country. Group averages are weighted by the number of jobs created by inward projects in each value chain function. A country with a functional share in any of the value chains functions equal to that of the EU average will have an RFS of 1 in that particular value chain function.
Source: fDi markets database; own calculations based on an adjusted methodology of Stöllinger (2021).

Source: fDi markets database; Penn World Tables PWT) Version 9.0; own calculations. Full report: http://library.fes.de/pdf-files/id-moe/17843.pdf.

4. Exogenous shocks since 2008 (and more recently) create further need for adapted growth model in EU-CEE

- EU-CEE has already started “second transition”: green, digital, trade/FDI, demographics.
- Main challenges/threats to convergence: 1) carbon intensity of production, 2) demographic trends, 3) automotive dependence, 4) weak innovation.
- Russian invasion has created more challenges. In short term 1) huge shock to industry, 2) inflation = far less policy space.
- Good news: NGEU – 1-3% of GDP per year for EU-CEE, mostly to support green and digital transitions.
- And 2008 and 2020 crises showed relative resilience of this region versus West and non-EU CESEE, should not be underestimated in this crisis as well.

Thank you for your attention!

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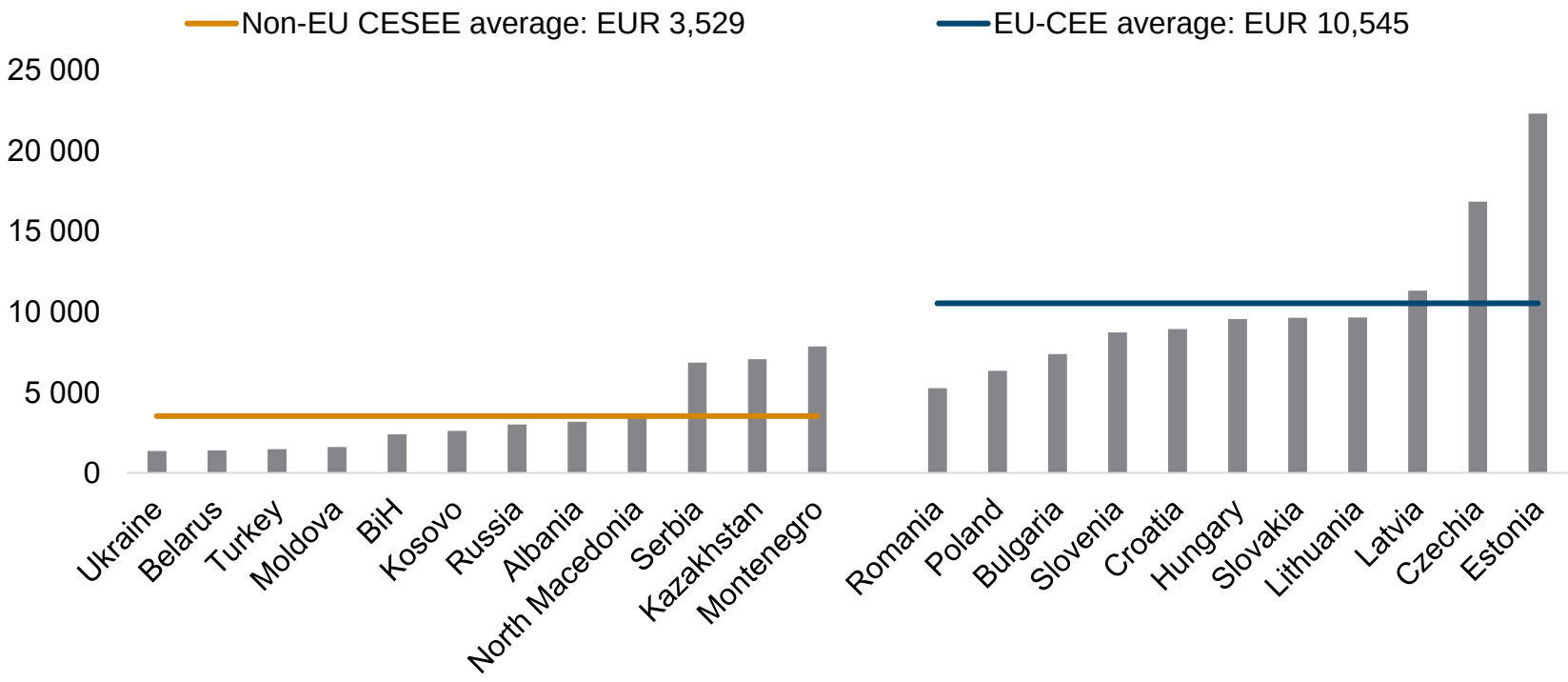
Extra slides for reference

(EU-CEE countries have received FDI inflows 3x higher than rest of region)

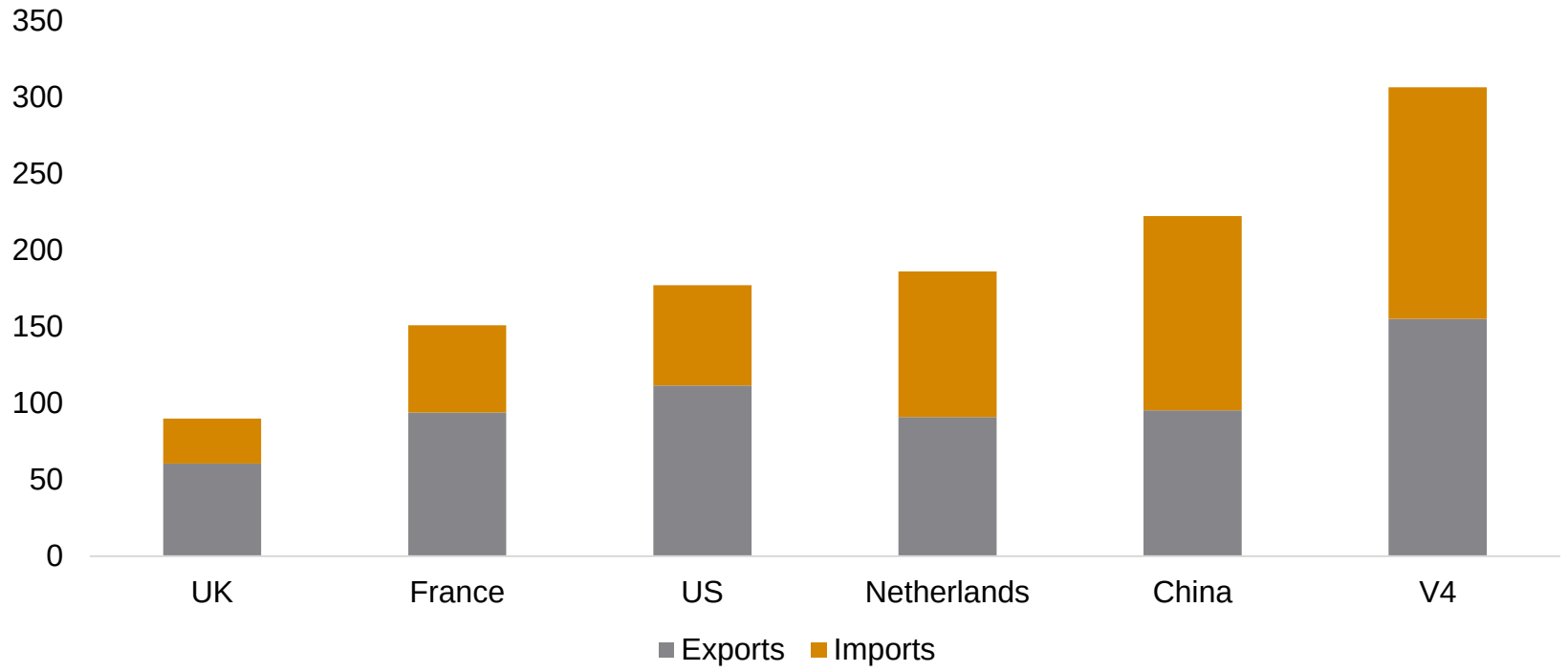
FDI inward stock per capita, EUR, 2021



Sources: Eurostat, national sources, wiiw.

(Visegrad countries in particular have fully joined the Central European manufacturing core)

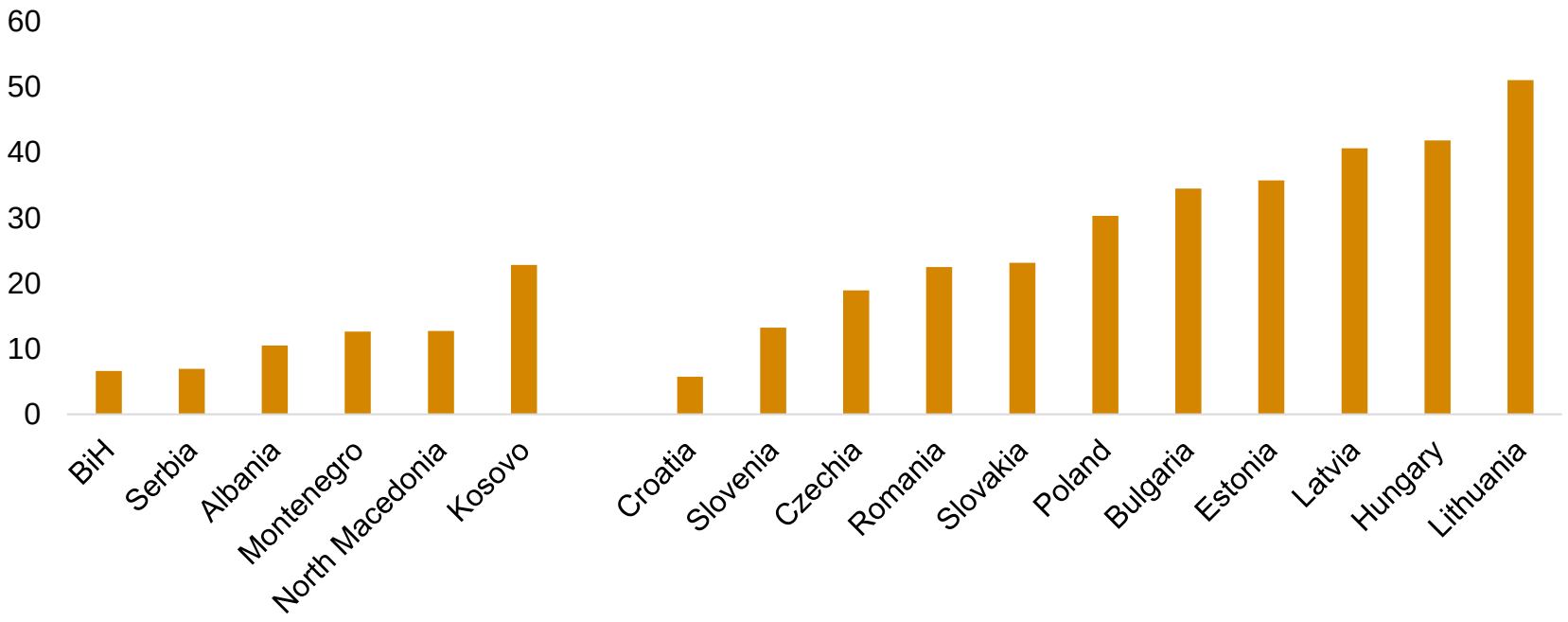
Total value of German external trade by partner, EUR bn, 2021



Source: German Federal Statistical Office (Destatis).

(Most EU-CEE countries have received 3-5x budget tranfers of candidate countries)

Cumulative transfers from the EU budget 2004-2018*, % of GDP



Sources: European Commission, national sources, wiiw. Note: For EU member states, data are transfers since 2004. For non-EU Western Balkan countries, transfers are IPA funds received during 2007-2018.

(Limited break-out from this specialisation pattern)

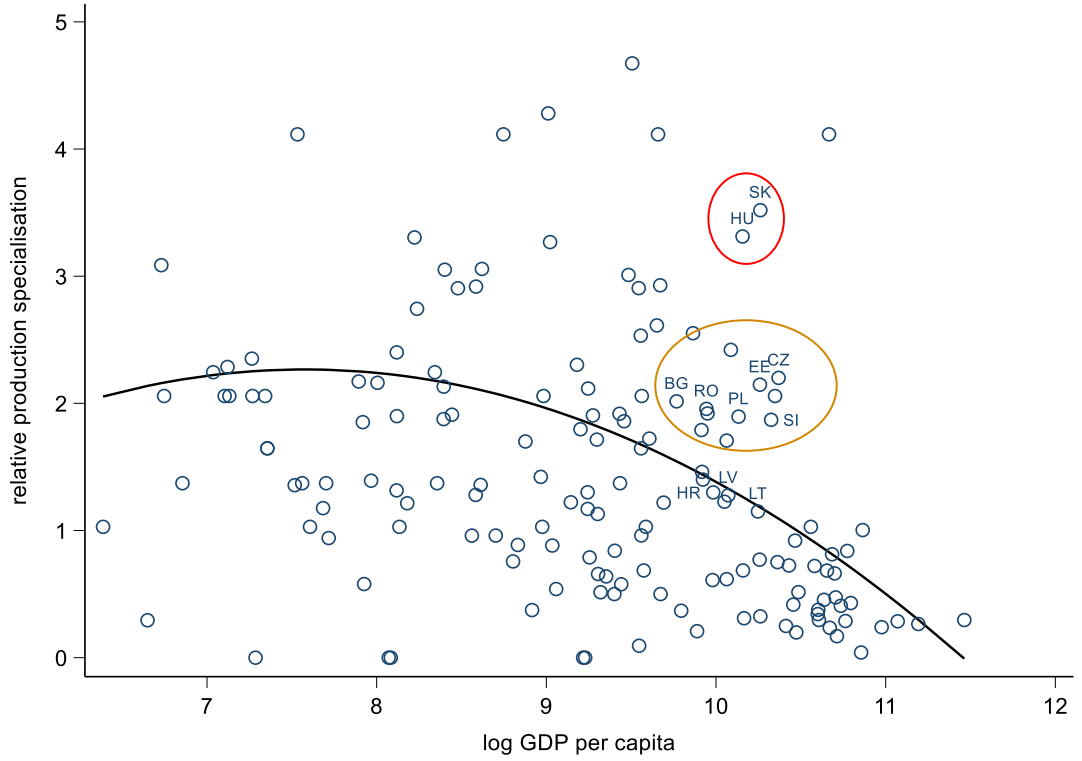
Functional profiles of EU-CEE, all industries, average 2003–2020

Country	Value chain function	Headquarter services	R&D and ICT* services	Production	Sales, logistics, marketing and support services	Business services and technical support
	Visegrád countries					
CZ		0.14	0.57	1.54	0.52	0.25
HU		0.09	0.43	1.53	0.55	0.39
PL		0.19	0.45	1.21	1.00	0.87
SK		0.08	0.30	1.64	0.44	0.26
Average		***0.16***	***0.46***	***1.44***	***0.80***	***0.69***
	EU Balkan countries					
BG		0.16	0.62	1.36	0.67	0.80
HR		0.13	0.75	1.11	1.28	0.37
RO		0.28	1.01	1.34	0.59	0.63
SI		0.40	0.69	1.39	0.58	0.67
Average		***0.26***	***0.93***	***1.34***	***0.66***	***0.68***
	Baltic countries					
EE		0.16	0.74	1.26	0.89	0.59
LT		0.16	1.37	1.04	0.88	1.16
LV		0.19	0.58	1.07	1.28	0.74
Average		***0.17***	***1.16***	***1.11***	***1.00***	***0.99***
	Selected EU-15					
DE		1.75	1.25	0.81	1.20	0.87
FR		0.96	1.17	0.68	1.15	2.16
IT		0.52	1.52	0.89	1.16	0.87
UK		1.73	1.43	0.60	1.32	1.49
AT		1.96	1.63	0.96	0.86	0.48

Source: fDi markets database; Penn World Tables PWT) Version 9.0; own calculations. Full report: http://library.fes.de/pdf-files/id-moe/17843.pdf.

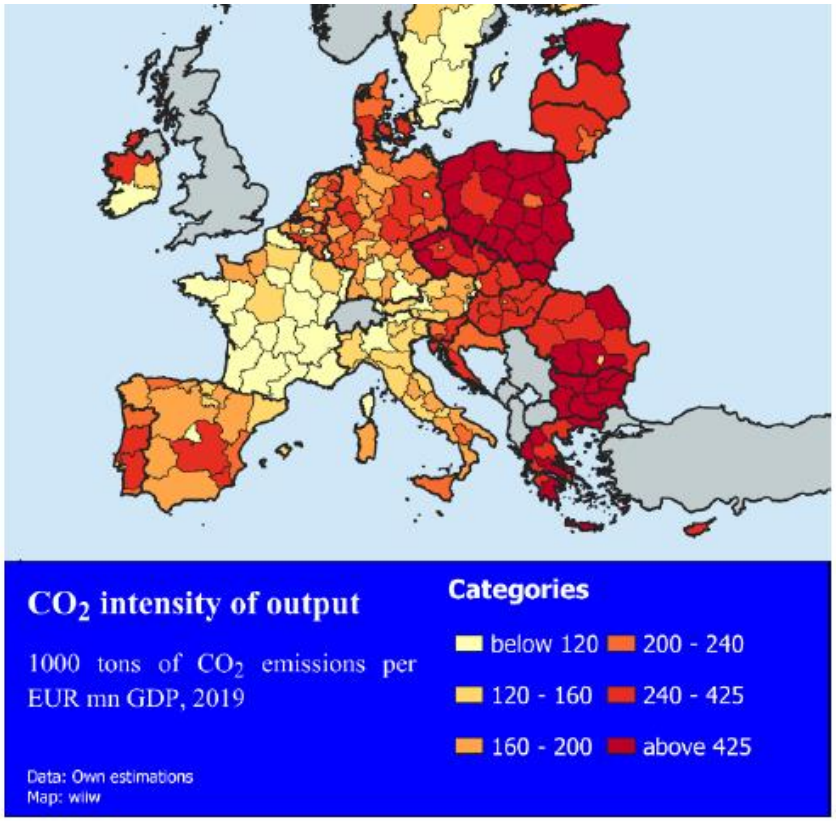
(And not changing over time – EU-CEE has extreme level of specialisation in production relative to income level)

Expected versus actual specialisation in production activities in a global comparison, average 2003-2018



Source: fDi markets database; Penn World Tables PWT) Version 9.0; own calculations.

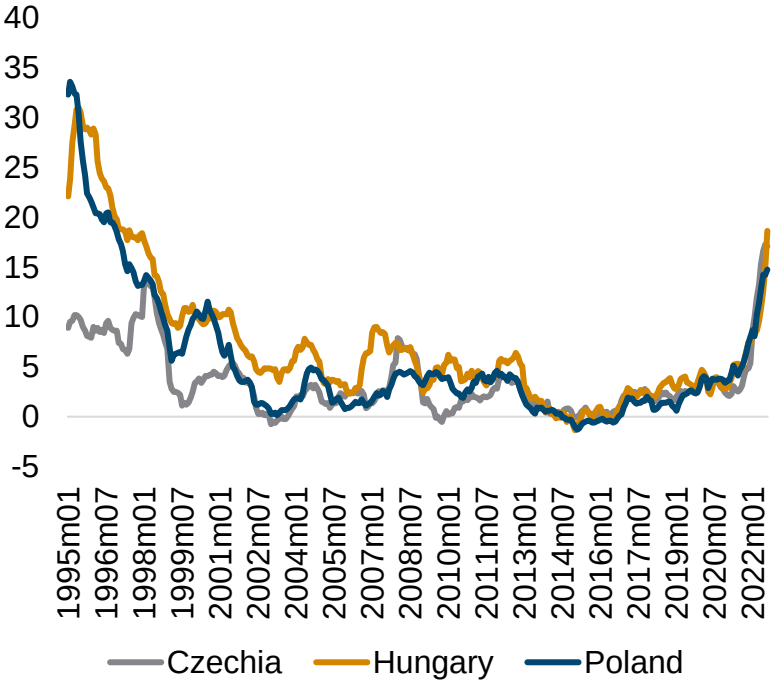
(Carbon intensity of production suggests green transition will be an enormous challenge for EU-CEE regions)



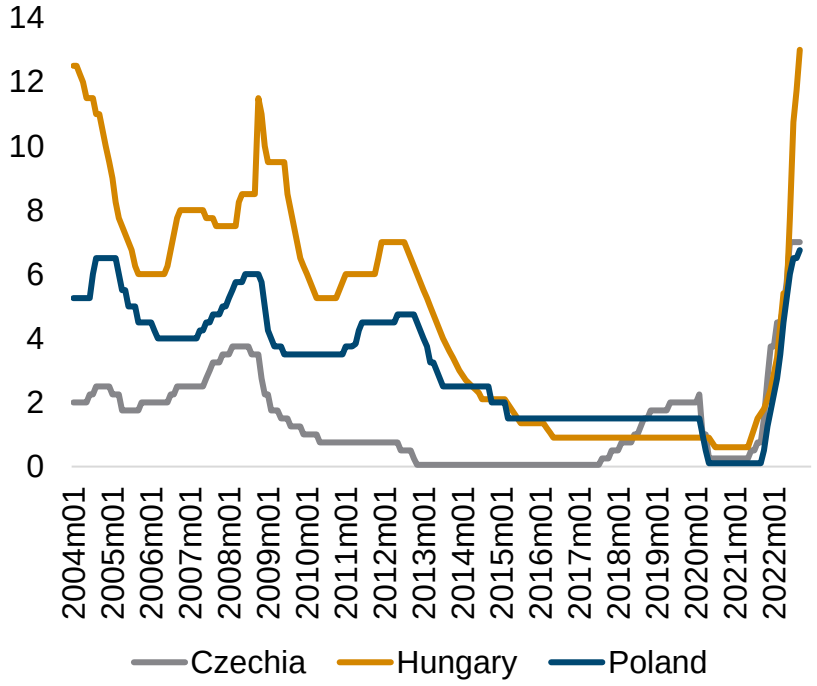
Source: European Commission, own calculations.

(The domestic policy to support the transition space has shrunk dramatically)

Consumer price inflation, % per year



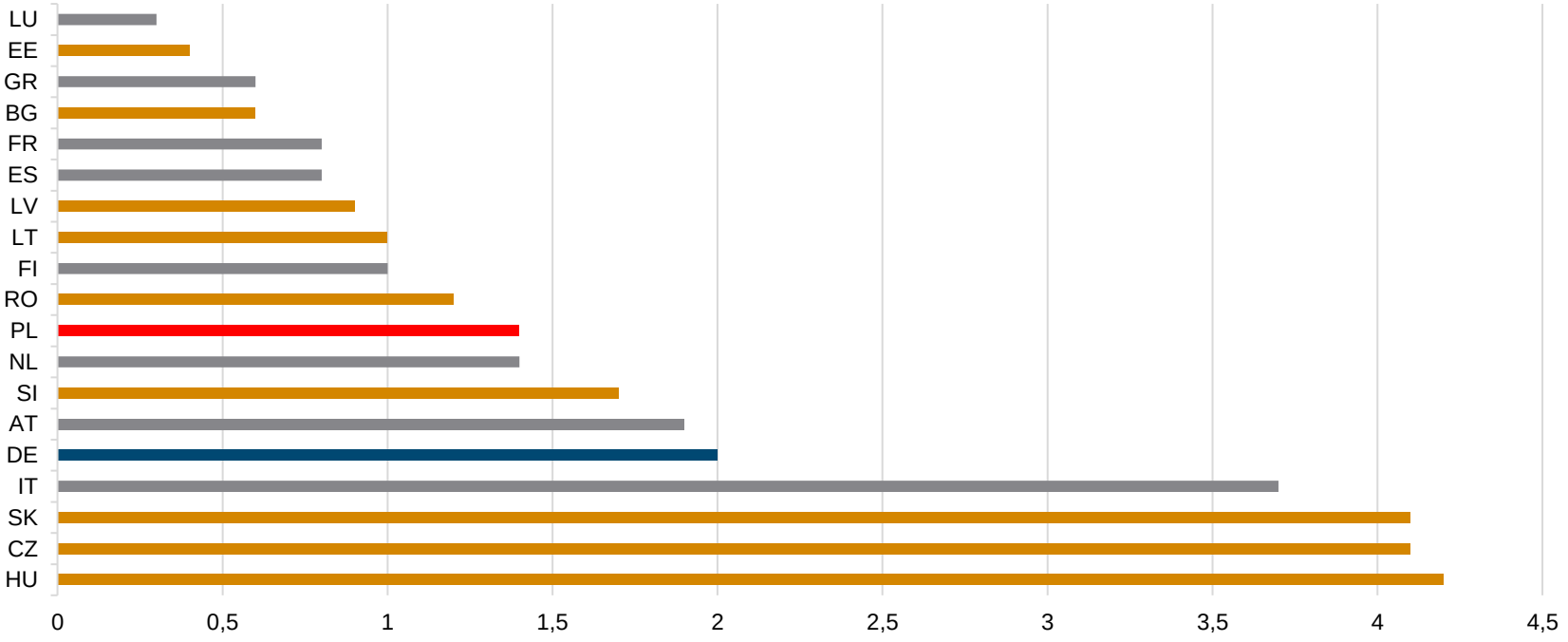
Policy rates, %



Sources: National sources.

(Jarring shock to industry in EU-CEE, but will speed up medium-term energy transition)

Estimated impact of a complete halt in Russian gas supplies on GDP, percentage points



Source: Di Bella et al. (2022)