Looking Through the Crystal Ball: For Growth and Productivity, Can Central Europe be of Service?

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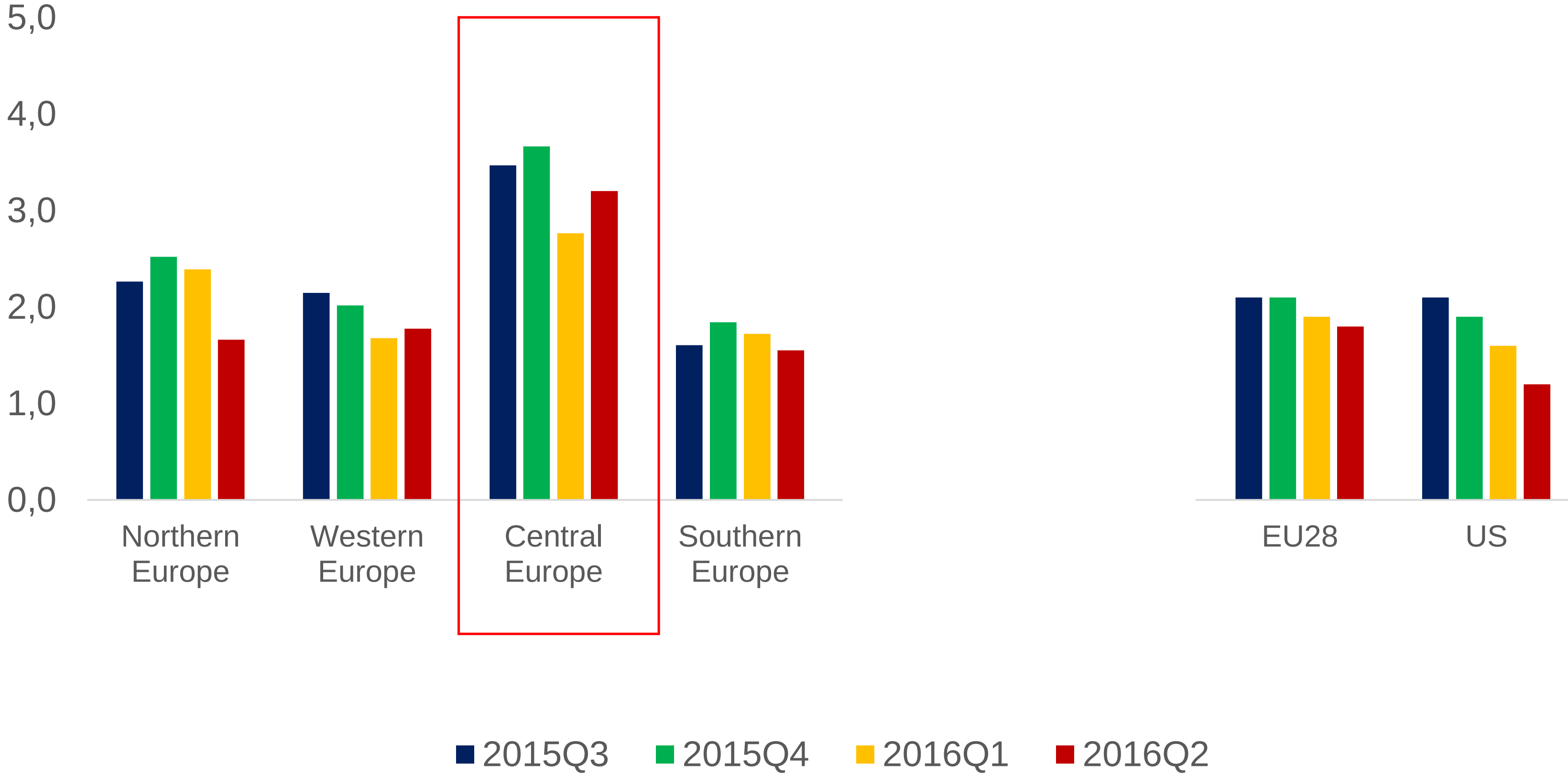
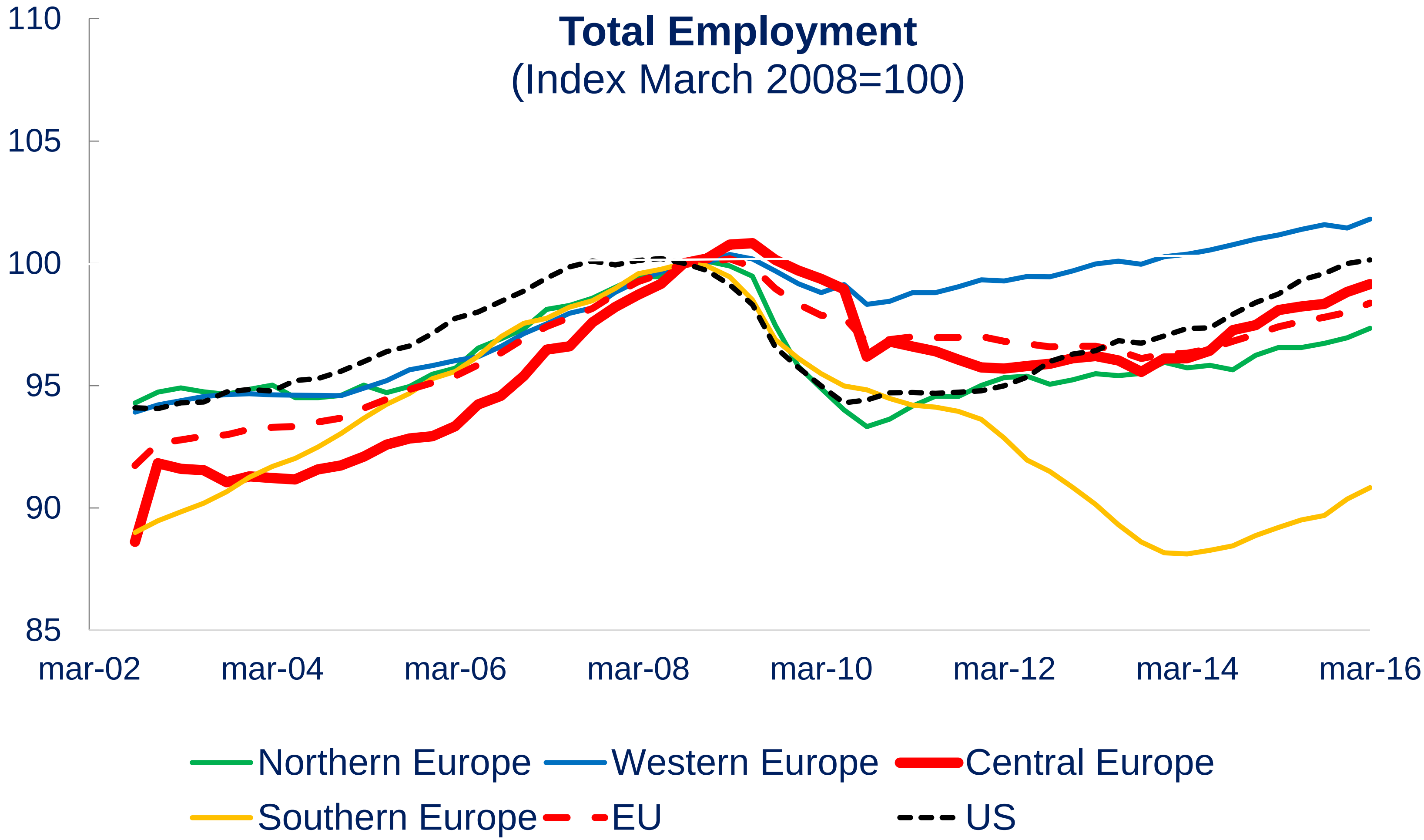
Central Europe beats the trend

Real GDP growth by quarters
(Annual change; CLV; NSA; in percent)



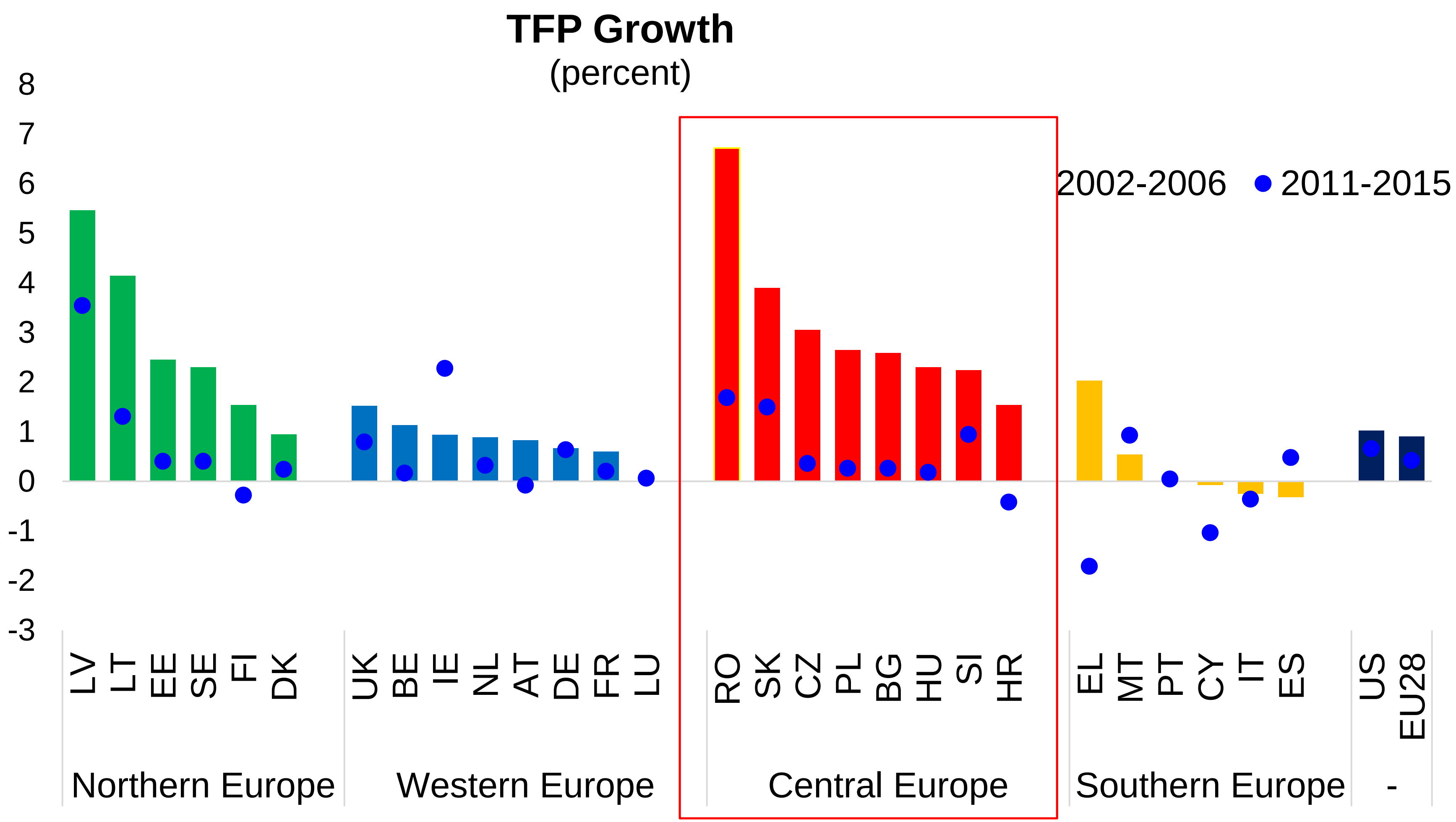
Source: Eurostat and OECD.
Note: CLV – Chain linked volumes; NSA – Not seasonally adjusted. 2016Q2 for EU28 and USA are flash estimates.

Employment is recovering faster than many…



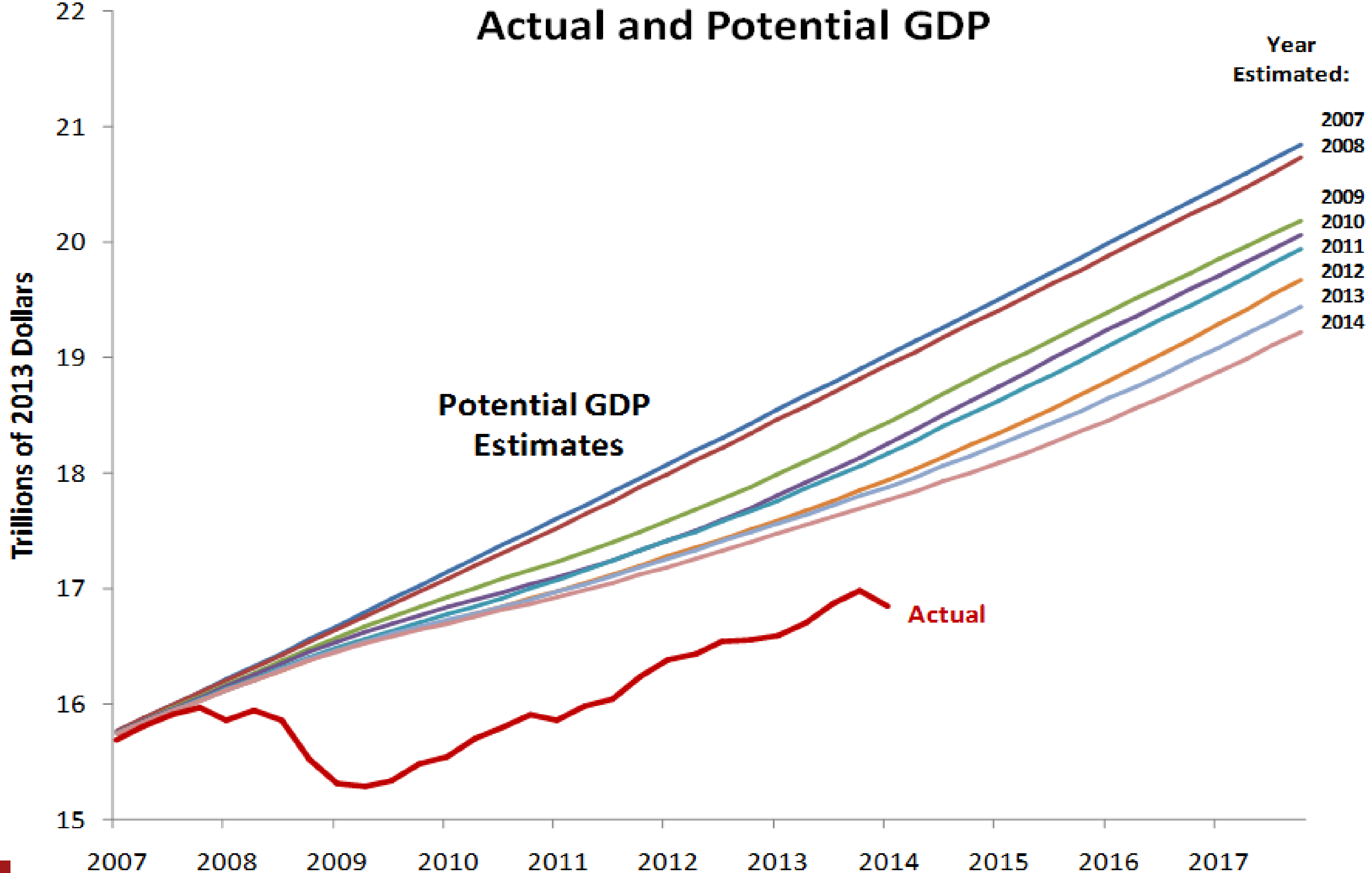
Source: Eurostat

TFP growth is higher than most, and higher than before



Source: Eurostat.

BUT… LARRY SUMMER WORRIES ABOUT SECULAR STAGNATION



MOHAMED EL-ERIAN IS GLOOMY ABOUT THE "NEW NORMAL"

Normal, old and new

- Globalization
- Laissez faire banking
- Debt-led consumption
- Smaller role for gov't
- Worry about **de**flation
- US GDP growth > 3%
- Modest tax burden

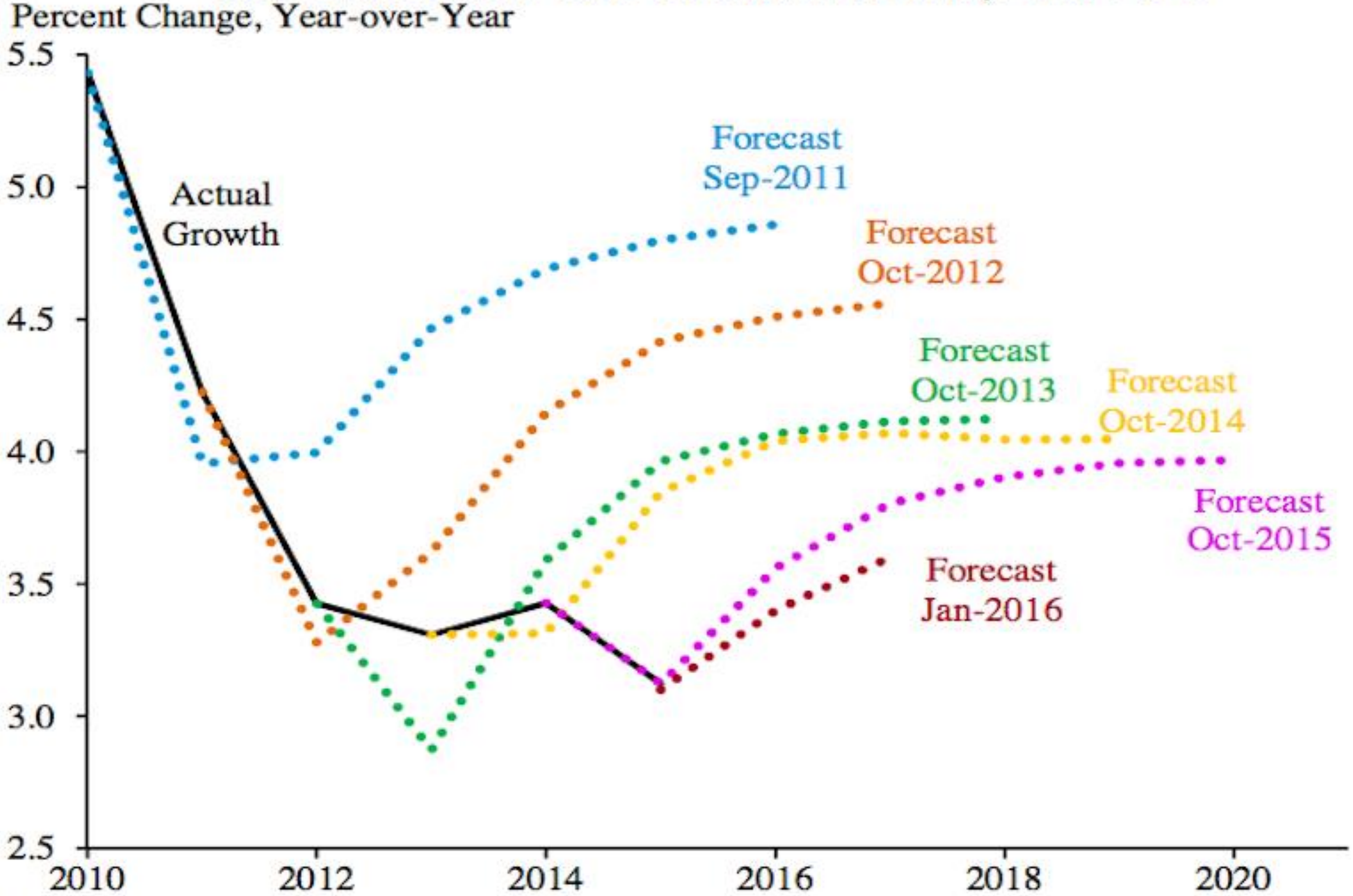
- Protectionism
- Banking **re**-regulation
- Fear-based savings
- Larger government role
- High risk of **in**flation
- US GDP growth ~ 2%
- Higher tax burden

Bill Gross and Mohamed El-Erian, PIMCO, May 2009

AND CHRISTINE LAGARDE SEES A "NEW MEDIOCRE"

Figure 3-1

IMF World Real GDP Growth Forecast, 2010–2020



Source: International Monetary Fund (IMF).

SO …FOR CENTRAL EUROPE, WHERE IS THE *FUTURE* PRODUCTIVITY GROWTH GOING TO COME FROM?

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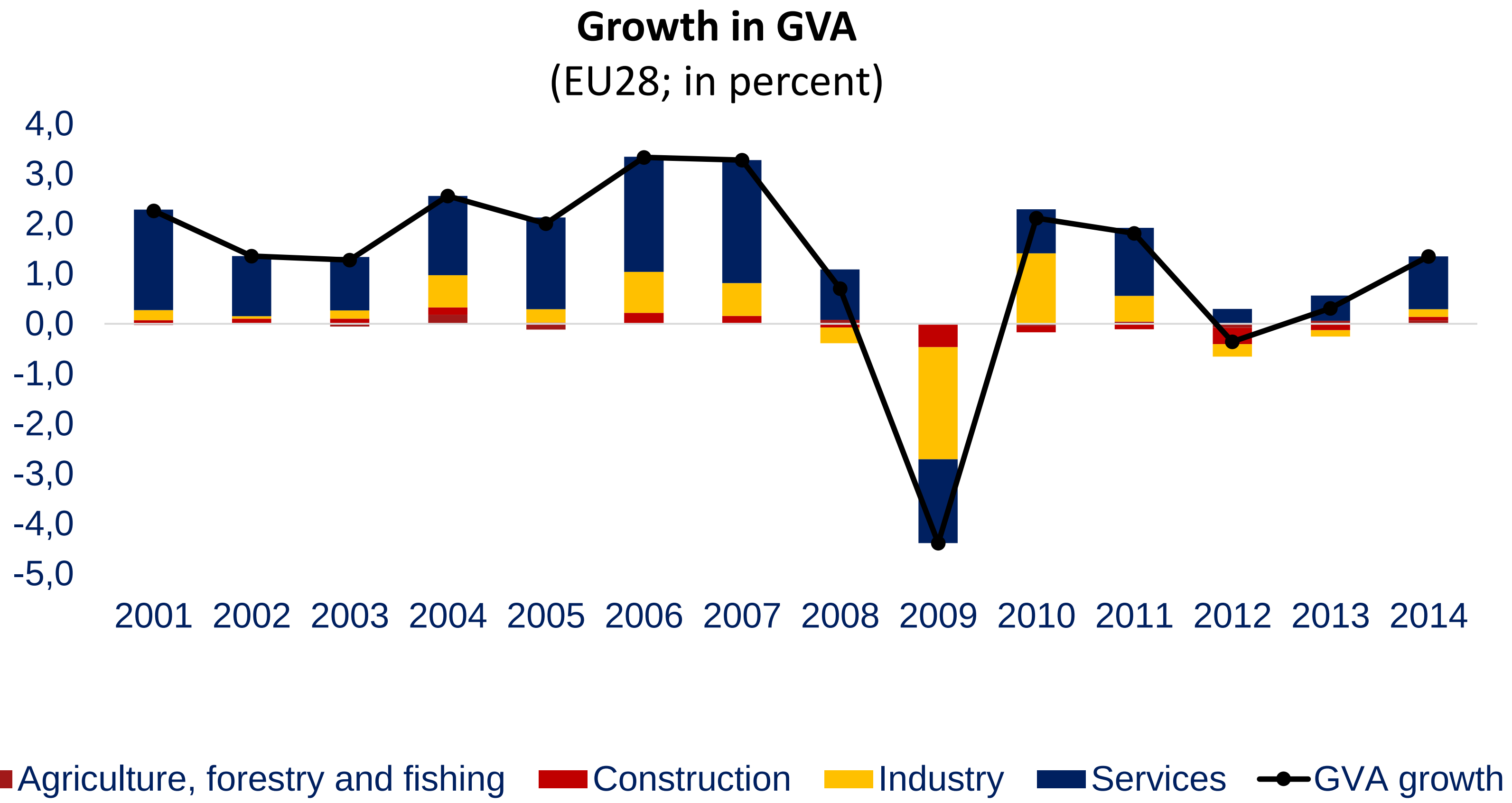
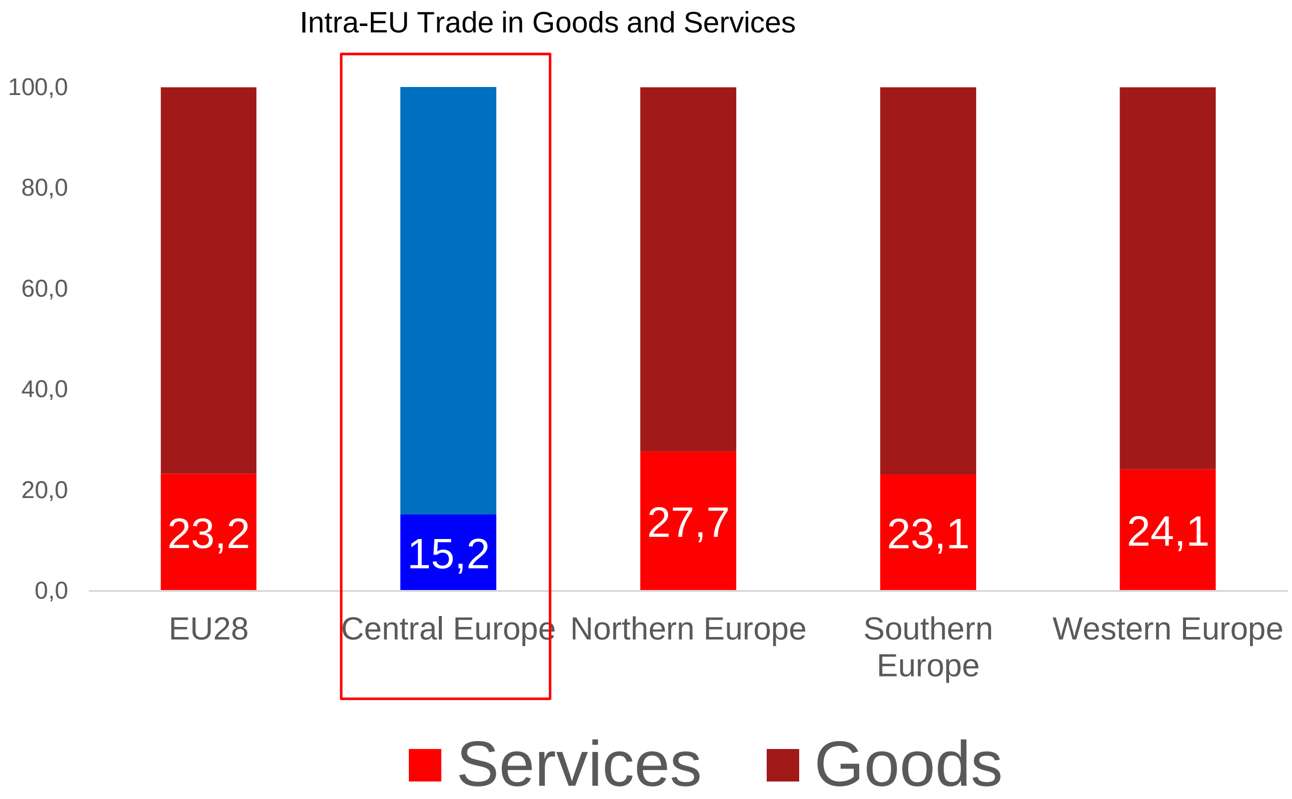
- SHORT-TERM, AND WITHIN THE EU: LOW HANGING FRUIT
  - SIMPLE BARRIERS TO TRADE, PREVENTING PRODUCT AND FACTOR-PRICE EQUALIZATION
  - SCALE OF EU MARKET SUGGESTS SIGNIFICANT POTENTIAL
- LONG-TERM: SERVICES AS A SOURCE OF GROWTH AND PRODUCTIVITY MORE UNCERTAIN
  - SERVICES NOT LIKE MANUFACTURING IN TERMS OF EXPORT POTENTIAL (RODRIK)
  - BUT WITHIN EU SINGLE MARKET: SERVICES MORE TRADEABLE THAN ELSEWHERE?

The Service Sector in Europe has been – and can continue to be a driver of growth

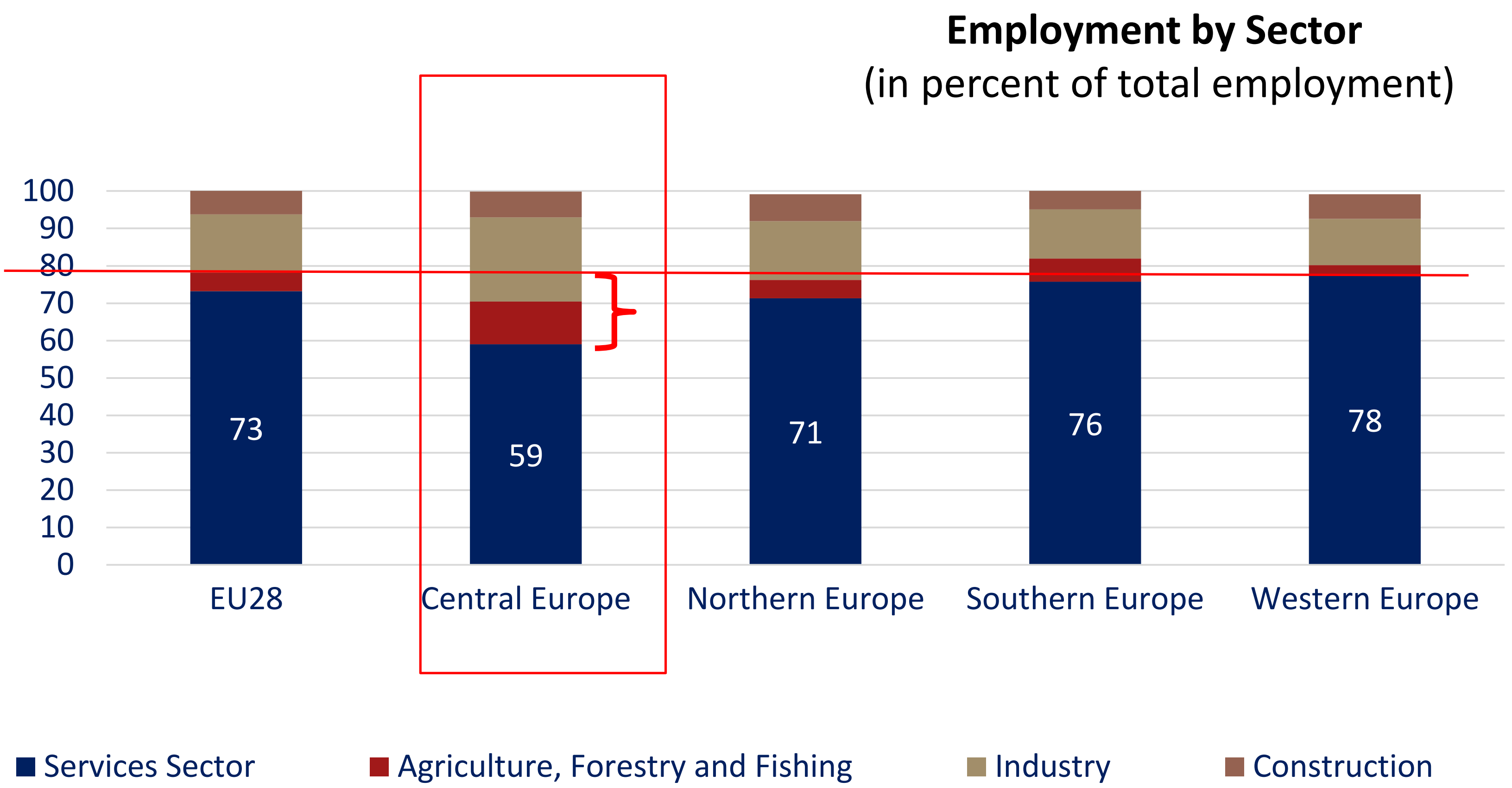


Source: Eurostat, WB staff.

But … Central Europe Has the Lowest Intra-EU Trade in Services

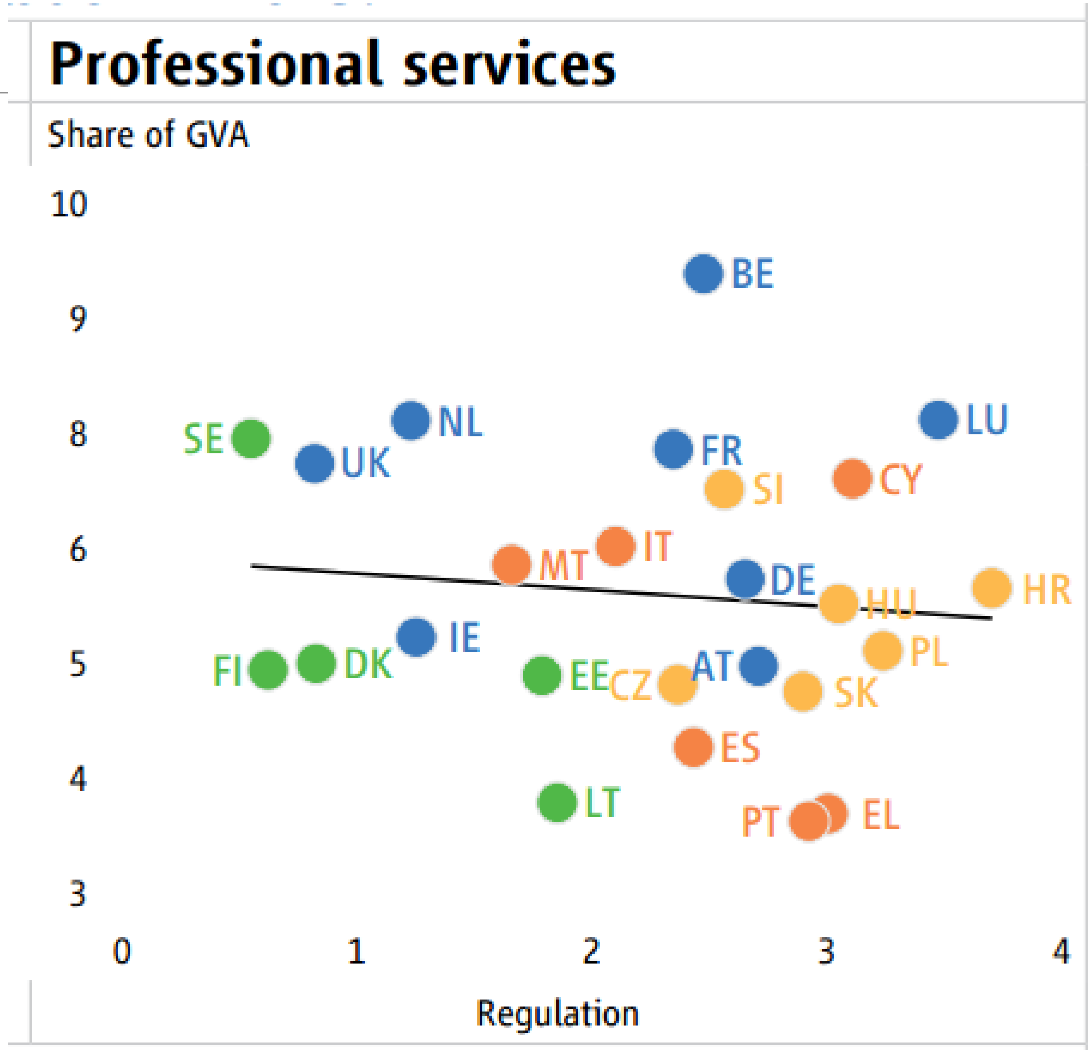


And in Central Europe, it has Untapped Potential as a Driver of Employment



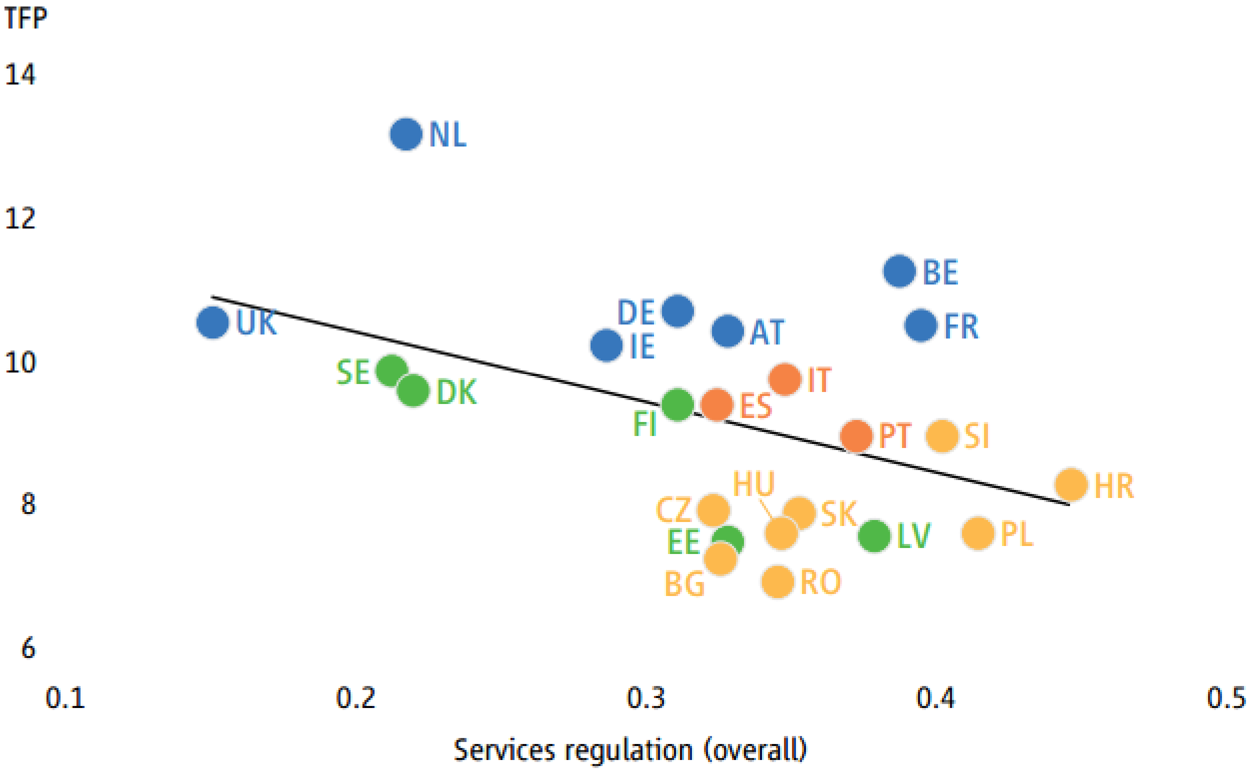
Source: Eurostat, WB staff.

Central European Countries are Among the Highest Regulators of Professional Services



Central European Countries Have More Regulated, Less Productive Service Firms

TFP level and overall services regulation level (2013)

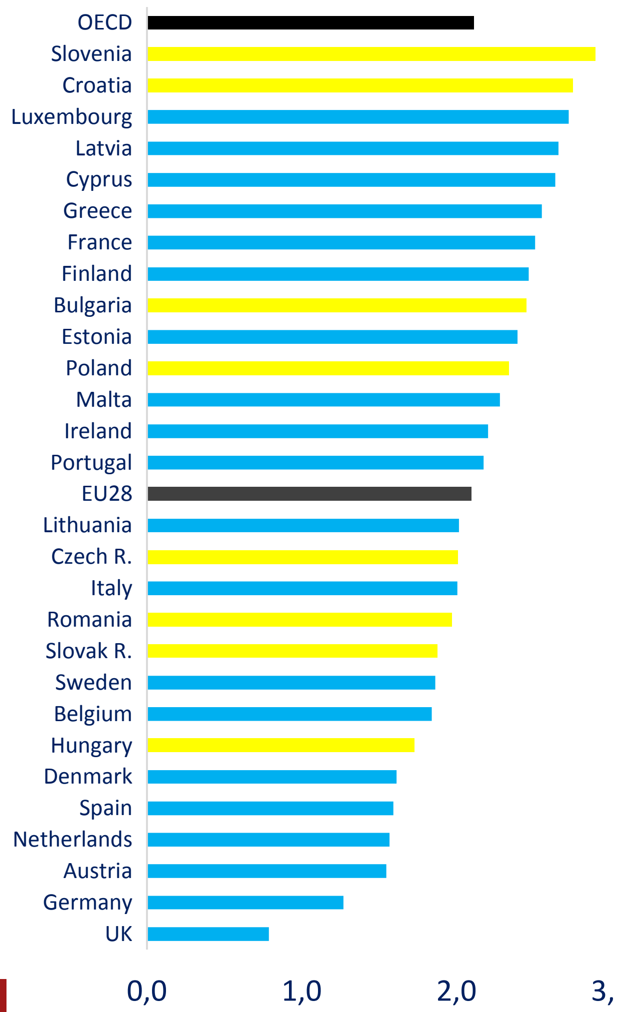


Source: Amadeus/Orbis, OECD, World Development Indicators.

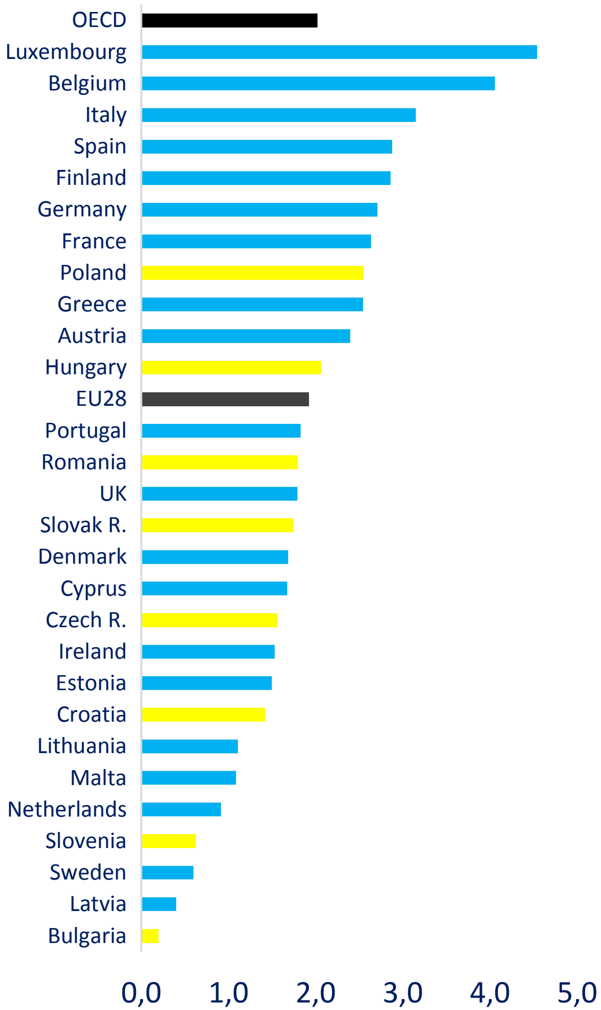
Source: Orbis; OECD; WB staff.

Regulations of Services are Relatively Rigid

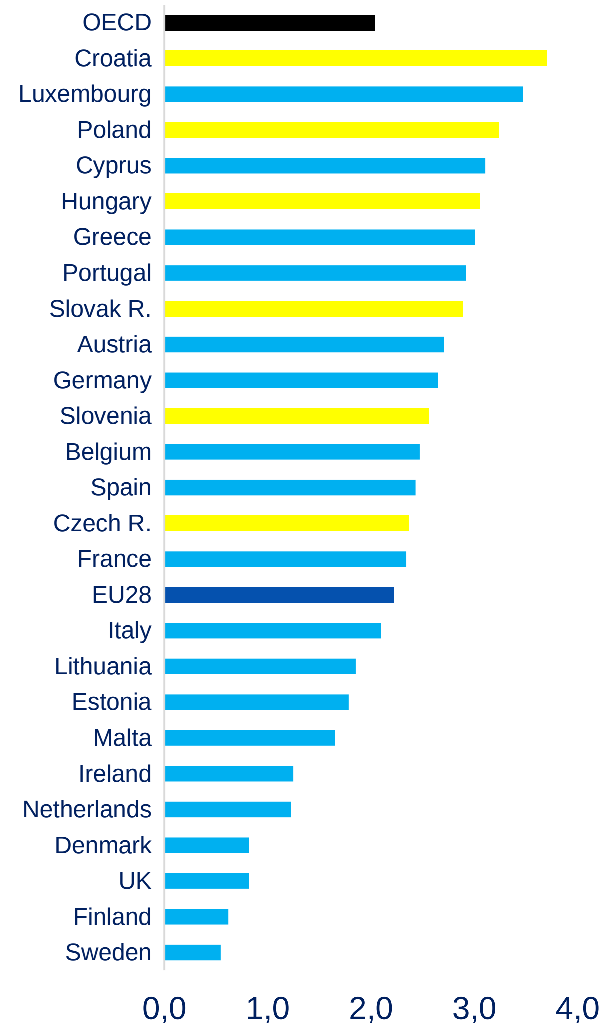
Network sectors



Retail

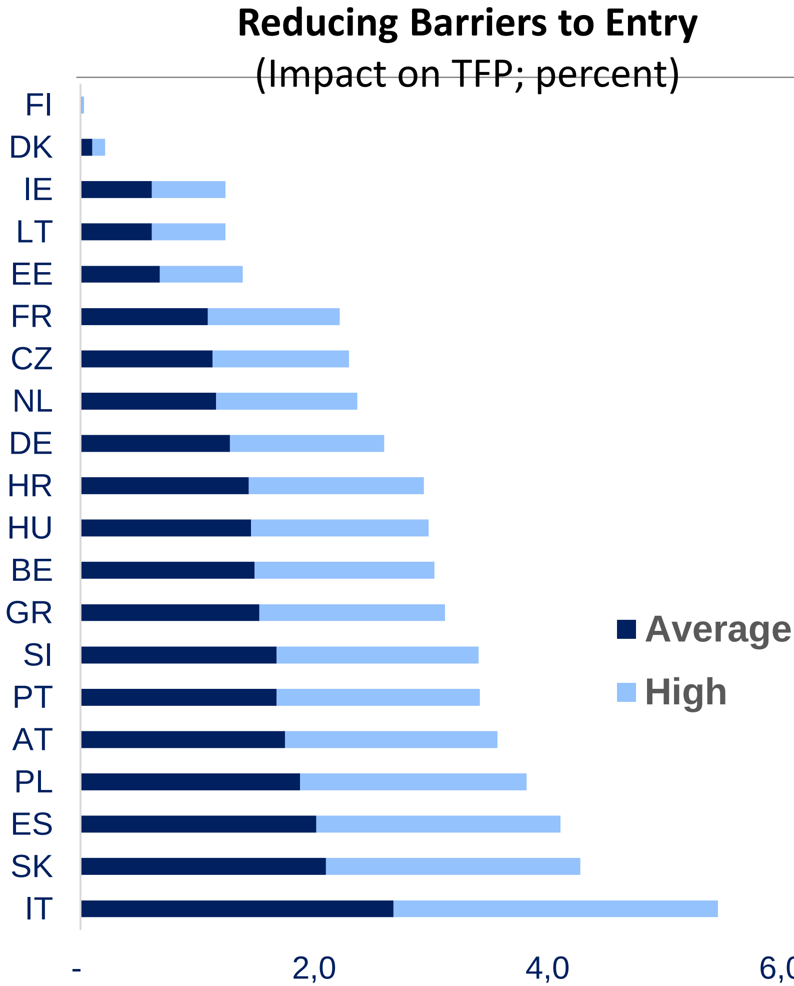


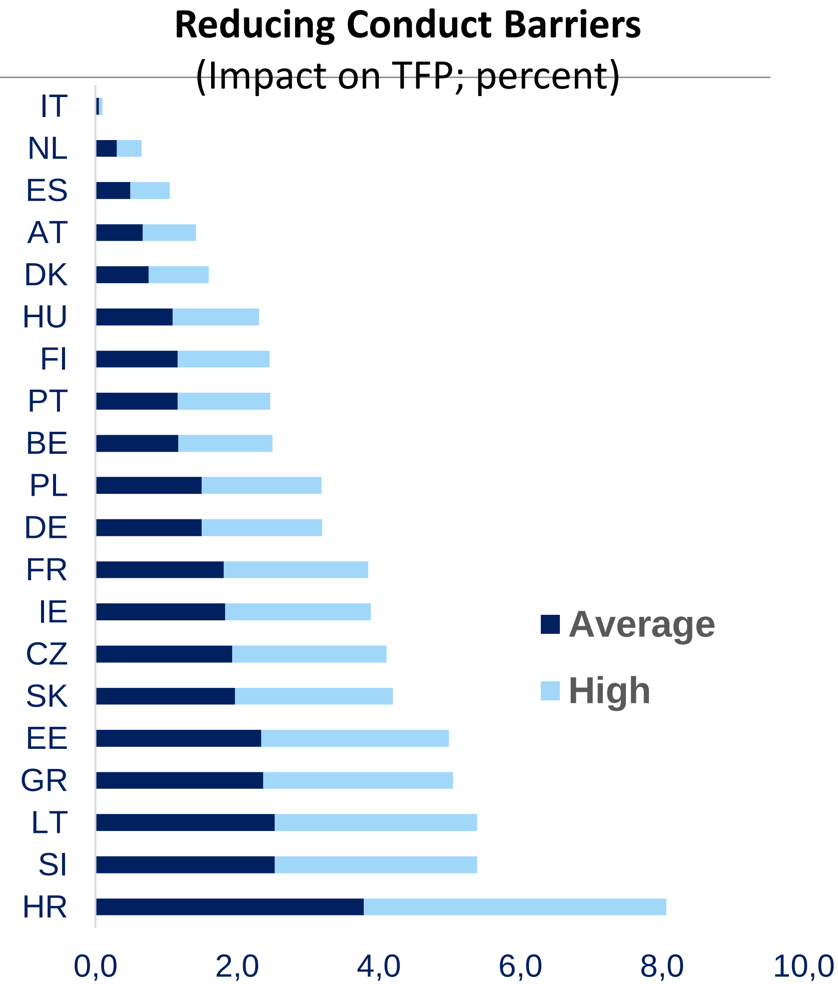
Professional services



Source: OECD

Reducing Entry and Conduct Barriers Increases Firm-level Productivity …

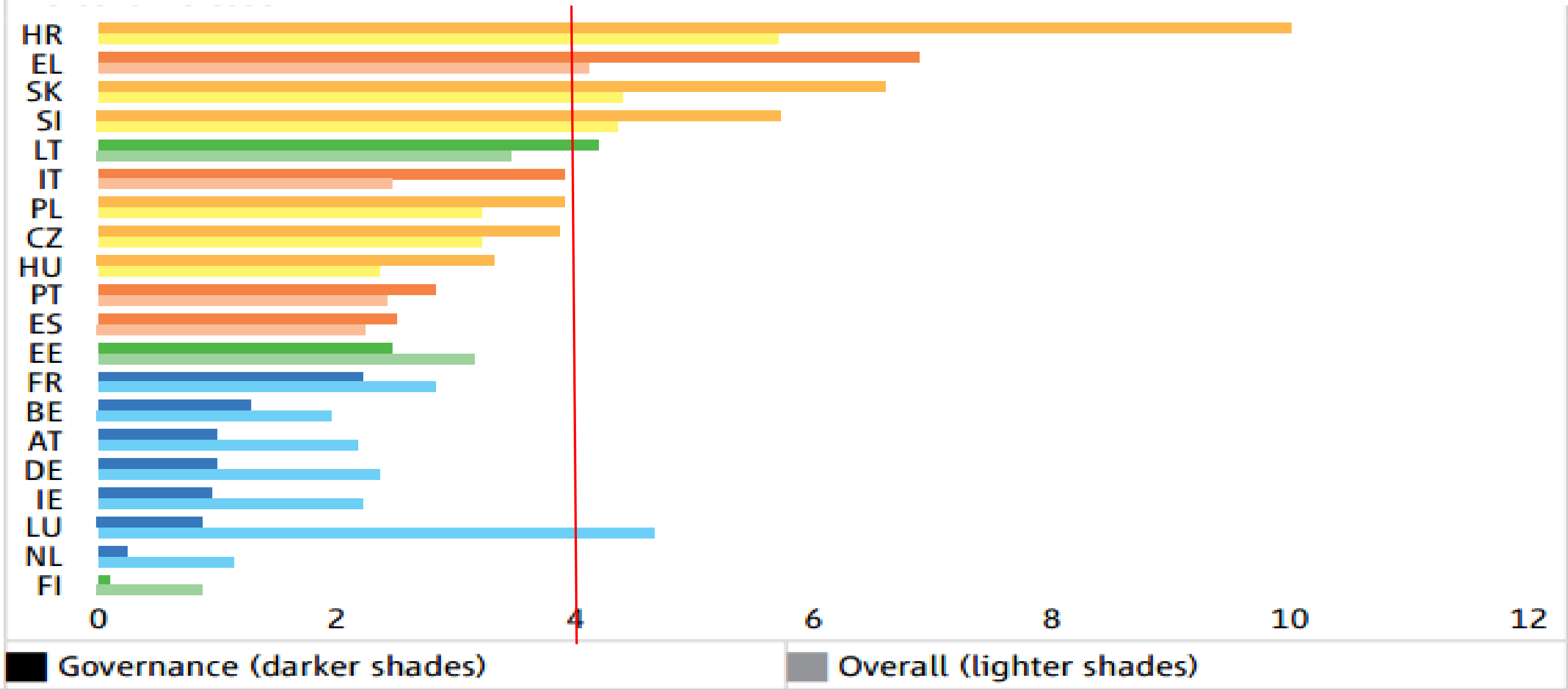




Source: OECD; WB staff. *Note*: Charts show the percent increase of TFP from reducing barriers to an average for EU or to the three least restrictive countries.

Reducing Service Sector Barriers will Increase Productivity in Central Europe

Percent increase of TFP from reducing service sector barriers to the level of the three least restrictive countries



Providers of services face many hurdles to offering their services in other EU member states

- Adoption of different ownership structure
- Change in insurance
- Find workers with different qualifications
- Become members of professional associations
- Face advertising restrictions

POLICY IDEAS

- Prioritize service sector reforms across EU member states and formalize it in a roadmap
- Create a common market for professional services
- Facilitate a debate about the benefits and costs of reform with service sector providers and users
- Retrain workers that could be negatively affected by the proposed reforms.

World Bank:

EU Regular Economic Report

Fall 2016

For more, see:

http://worldbank.org/eurerer