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...

Total Employment
(Index March 2008=100)

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 deflation
- US GDP growth > 3%
- Modest tax burden

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

Bill Gross and Mohamed El-Erian, PIMCO, May 2009
AND CHRISTINE LAGARDE SEES A “NEW MEDIocre”
SO ... FOR CENTRAL EUROPE, WHERE IS THE **FUTURE** PRODUCTIVITY GROWTH GOING TO COME FROM?
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“Increase freedom to deliver services in Europe”
– Mateusz Morawiecki, DPM Poland, October 14 2016
SO ...FOR CENTRAL EUROPE, WHERE IS THE **FUTURE** PRODUCTIVITY GROWTH GOING TO COME FROM?

**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.

Growth in GVA
(EU28; in percent)

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

**Employment by Sector**
(in percent of total employment)

- **EU28**: 73%
- **Central Europe**: 59%
- **Northern Europe**: 71%
- **Southern Europe**: 76%
- **Western Europe**: 78%

- **Services Sector**
- **Agriculture, Forestry and Fishing**
- **Industry**
- **Construction**

*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

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
• 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