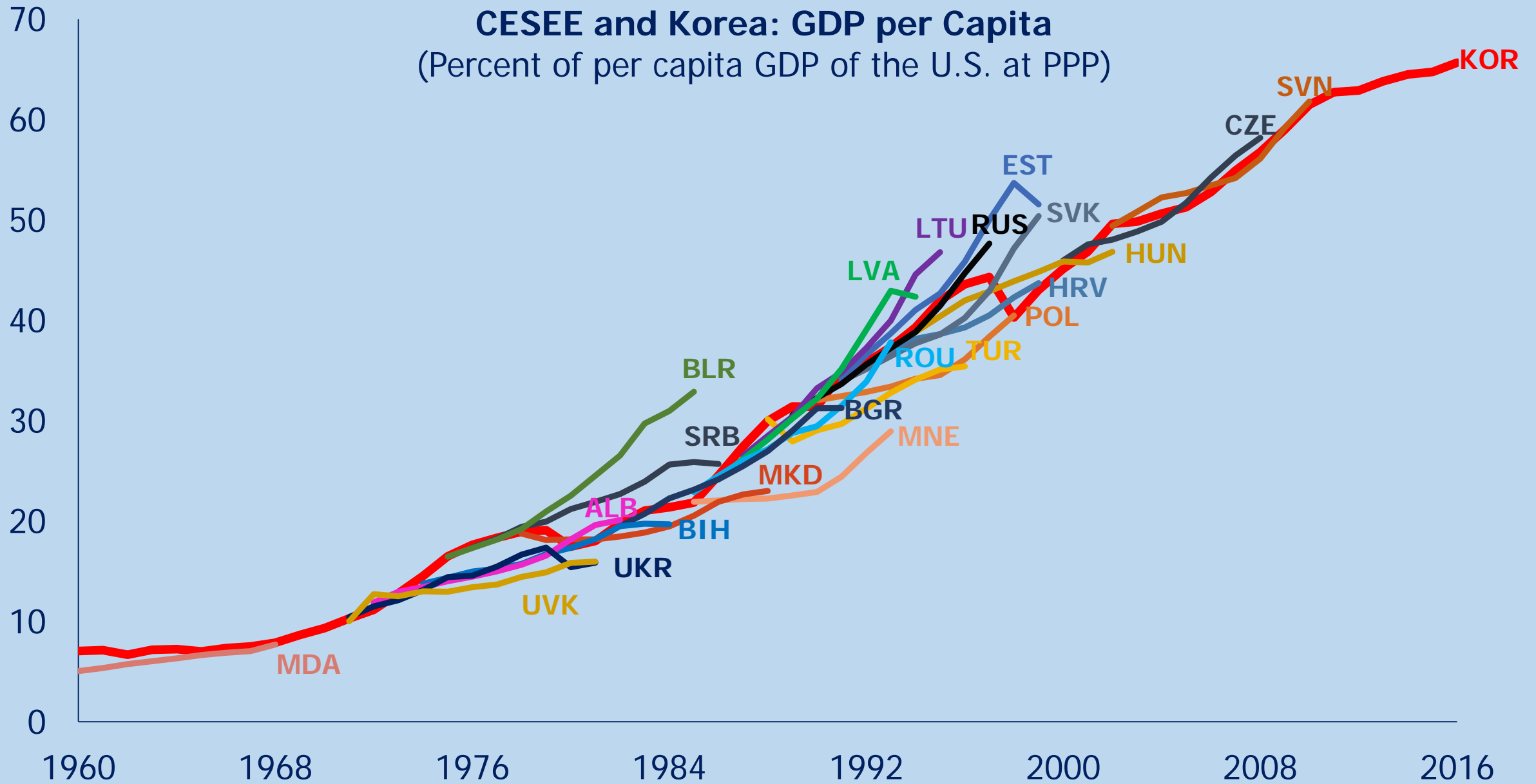


CONVERGENCE AND INSTITUTIONS



Jörg Decressin
European Department
October 5, 2017

The fast pace of convergence before crisis ...

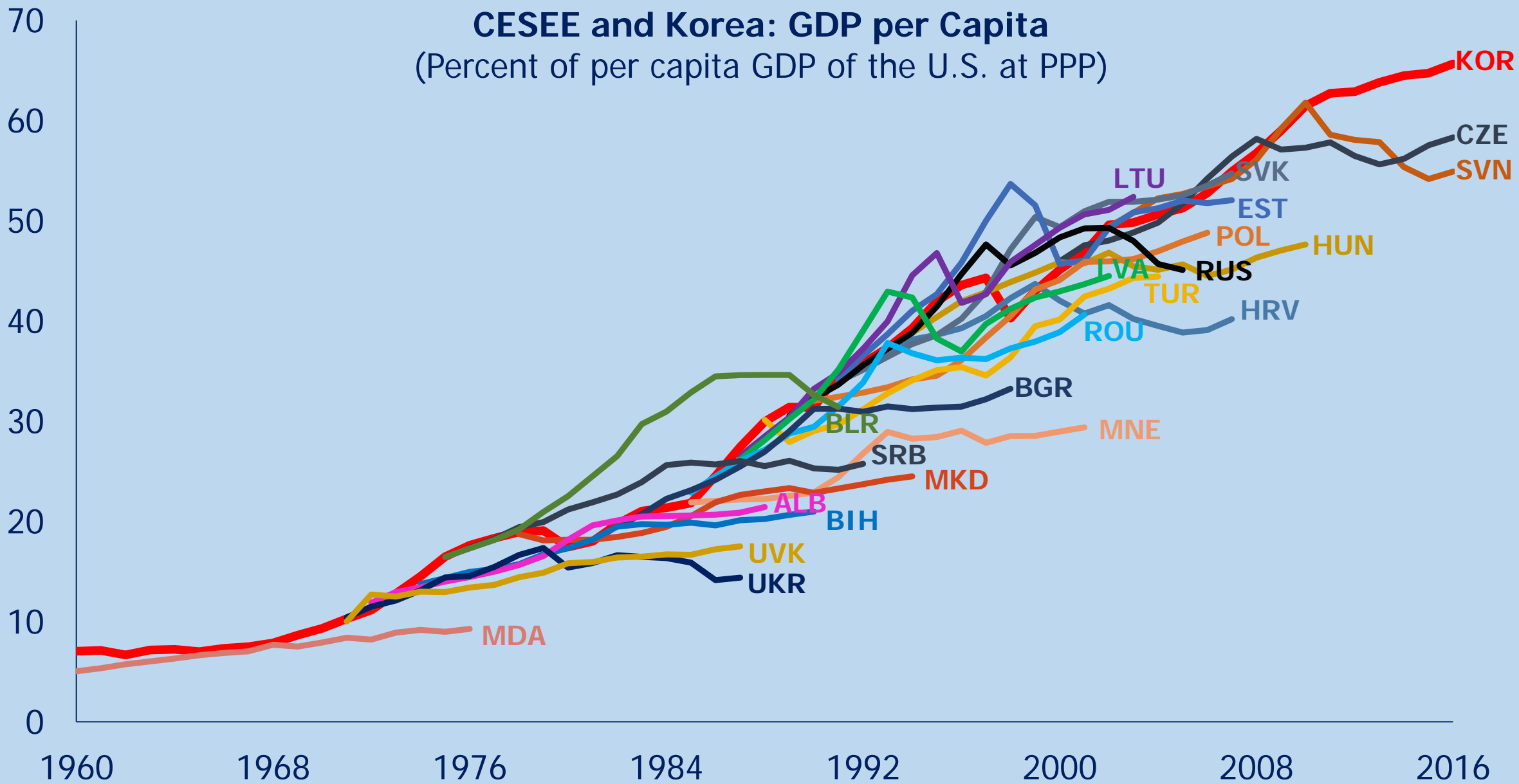


Data for CESEE countries are for 2000-2008 and are shifted back in time to comparable level of development of Korea.

... leveled off since 2009

CESEE and Korea: GDP per Capita

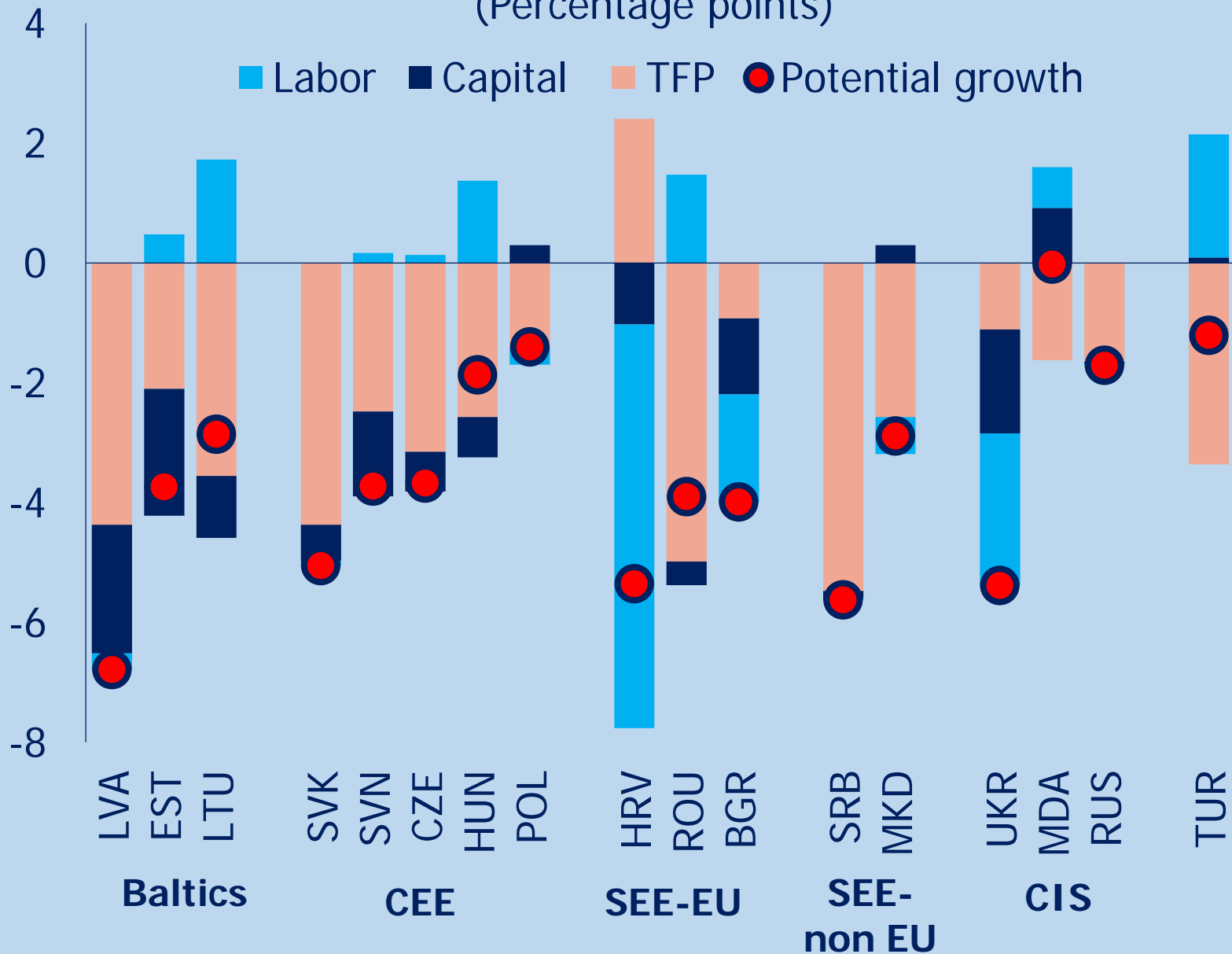
(Percent of per capita GDP of the U.S. at PPP)



Data for CESEE countries are for 2000-2016 and are shifted back in time to comparable level of development of Korea.

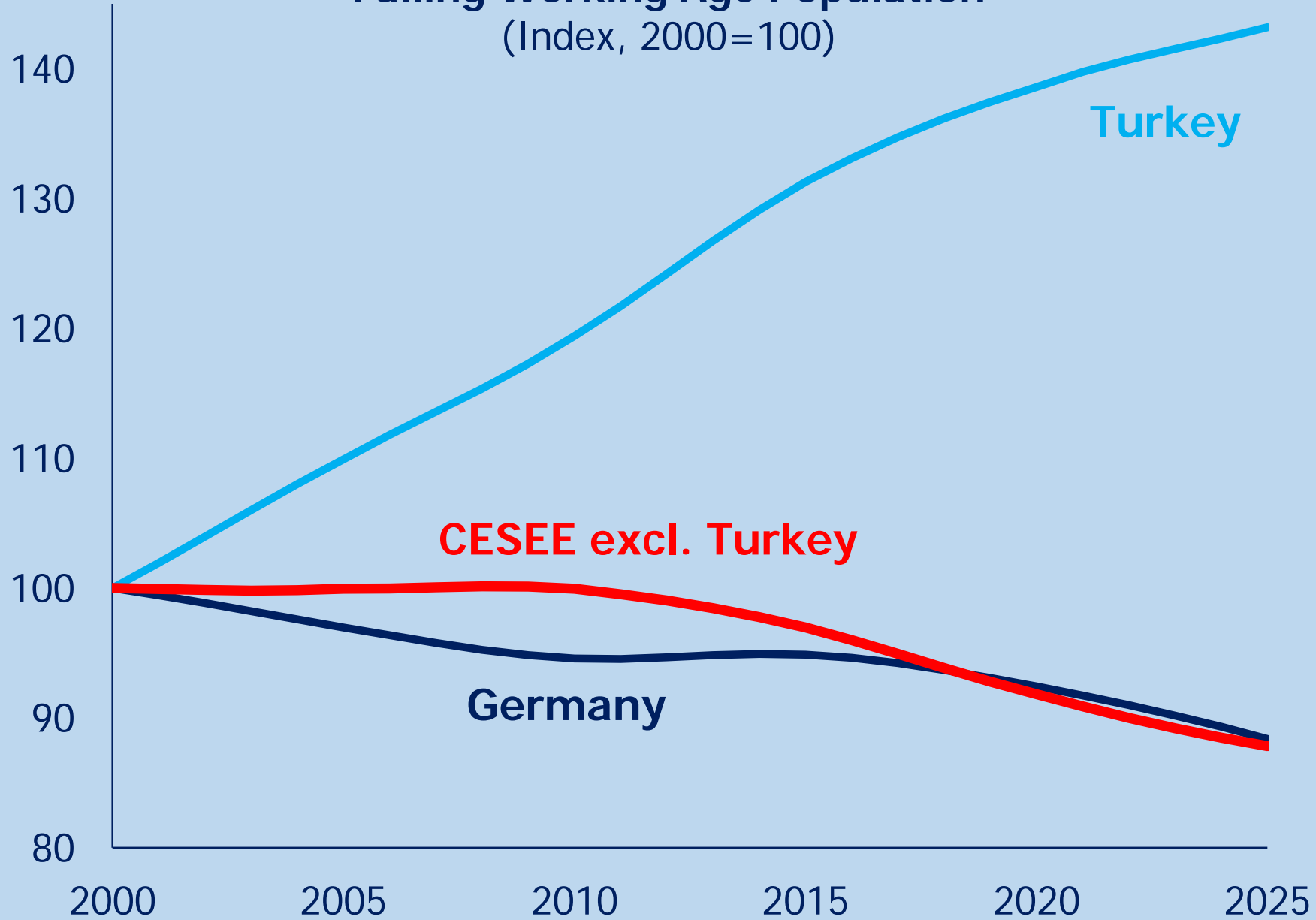
Lower TFP behind the growth slowdown

Change over 2013-15 versus 2002-08
(Percentage points)



Major demographic headwinds ahead

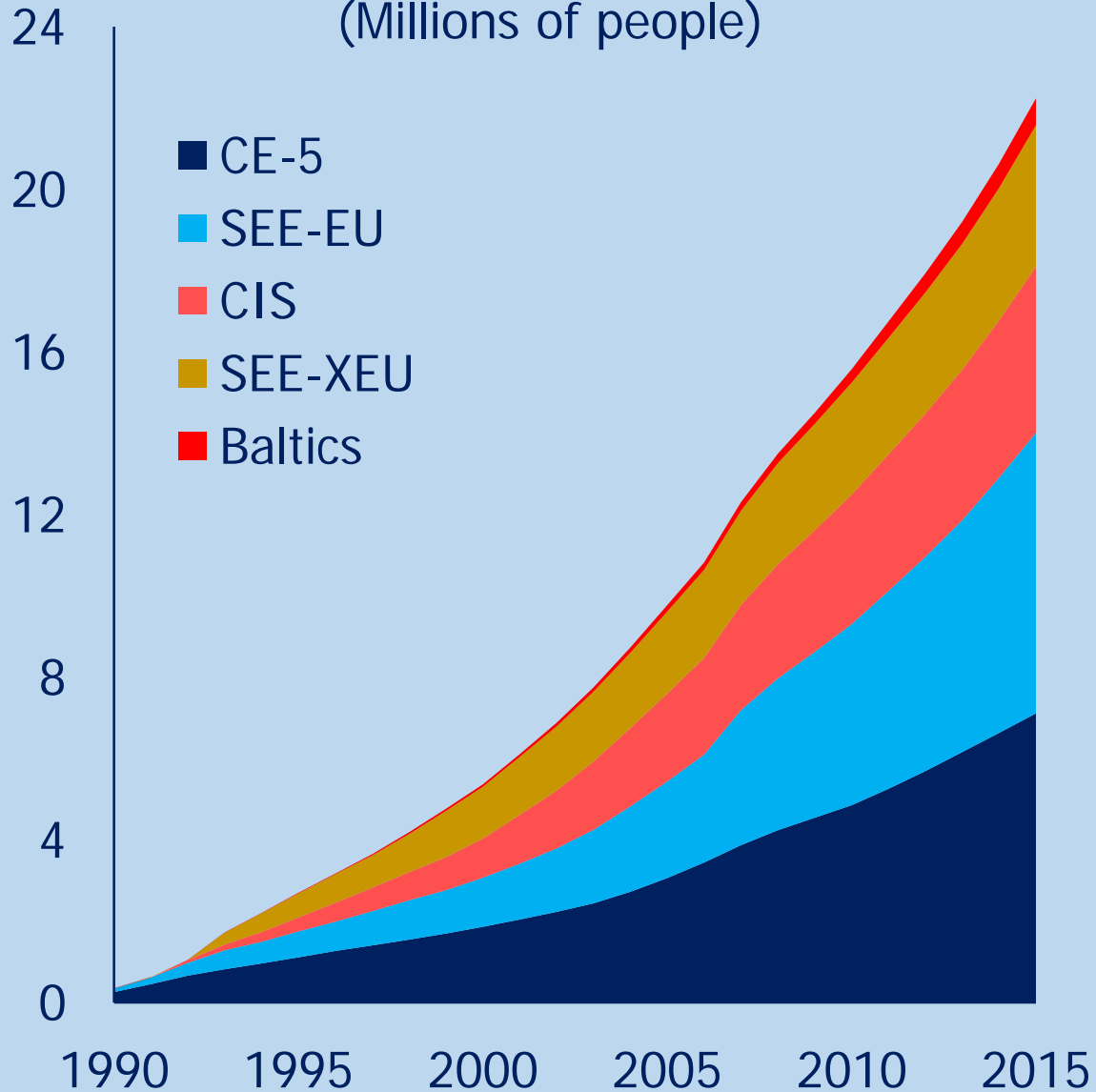
Falling Working Age Population
(Index, 2000=100)



Large emigration from the region impacts growth

Cumulative Emigration Flows by Region

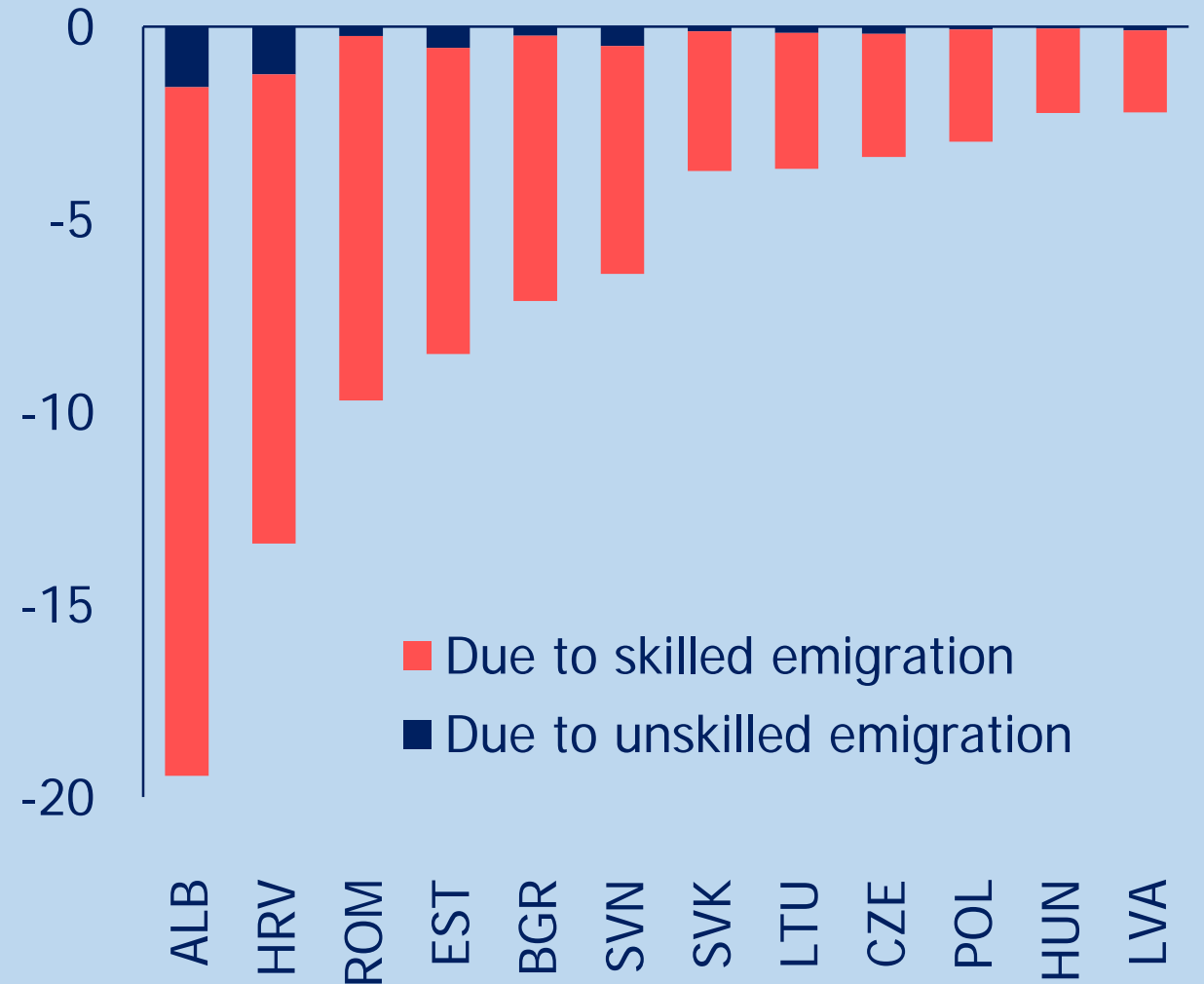
(Millions of people)



Emigration Impact on Real GDP Growth

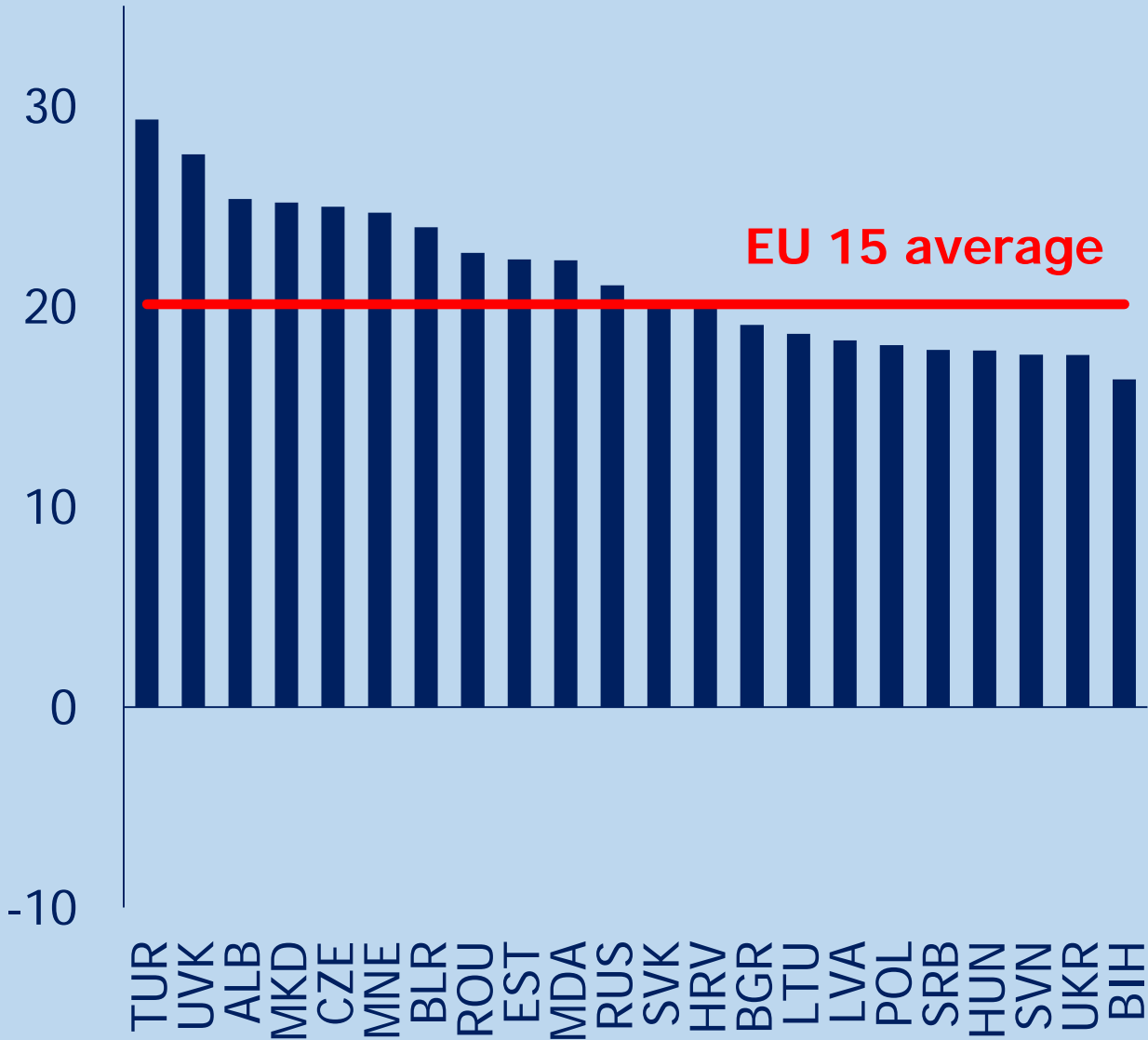
1995-2012

(Percentage points)

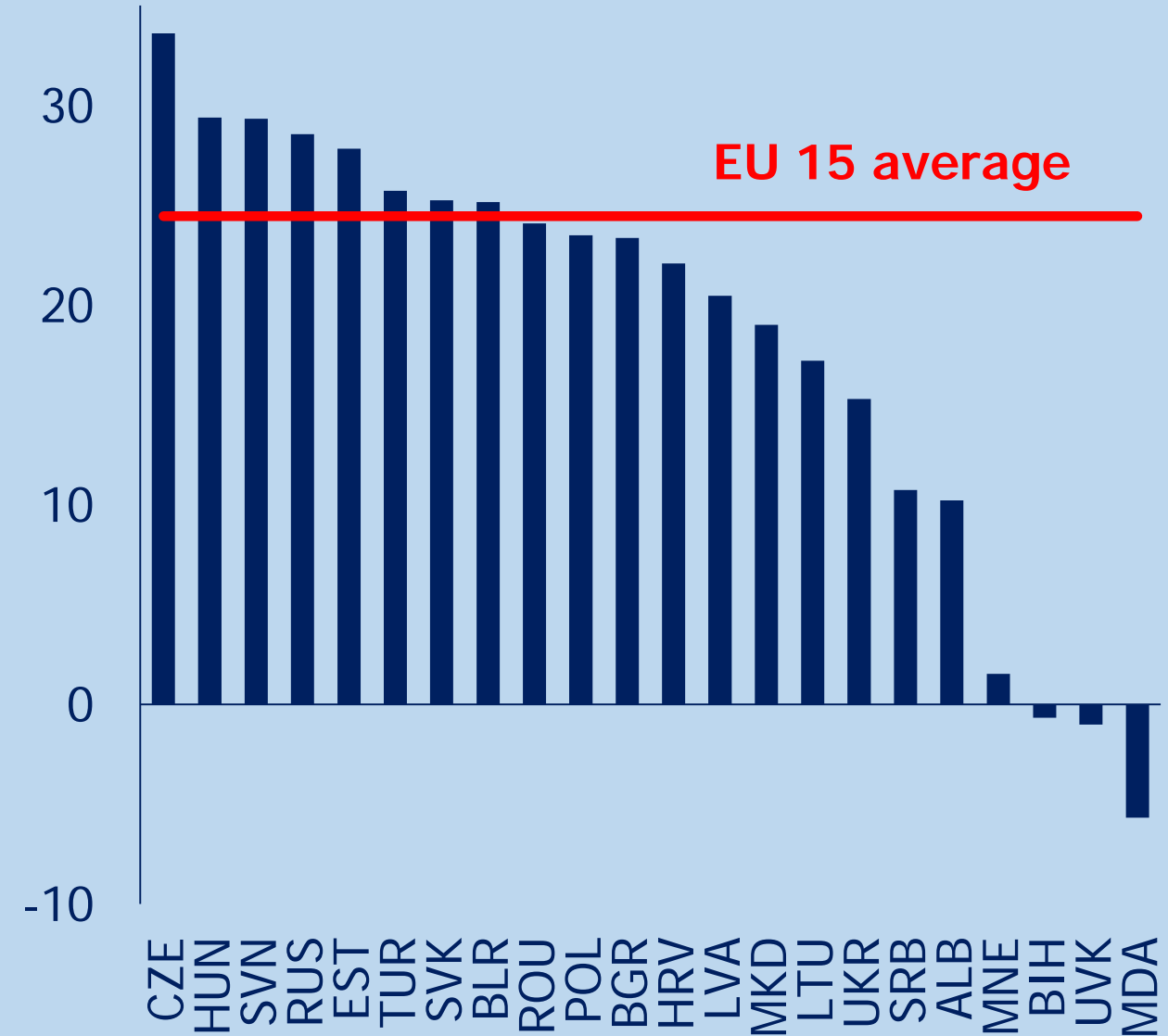


Low domestic savings and insufficient investment

CESEE: Gross Investment, 2016 (Percent of GDP)



CESEE: Gross Domestic Saving, 2016 (Percent of GDP)



Rule of law challenges for many European countries. A lot of progress in CESEE countries but remaining gaps

Rule of Law 2016

Protection of Property Rights 2015

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



Worldwide distribution excluding LICs

Room for improvement especially in judicial independence and impartiality

Judicial Independence 2015

Impartial Courts 2015

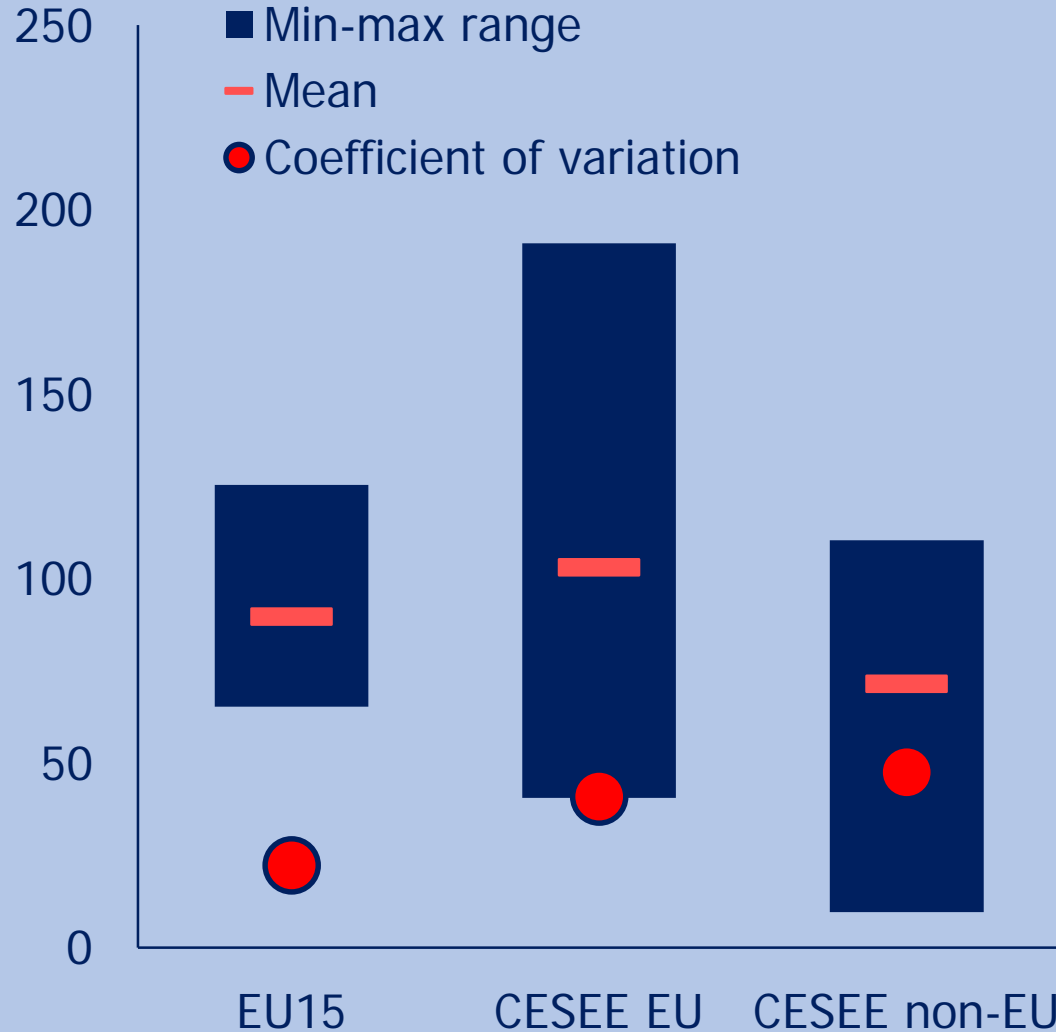
- Below 25 percentile
- Between 25 and 75 percentile
- Above 75 percentile



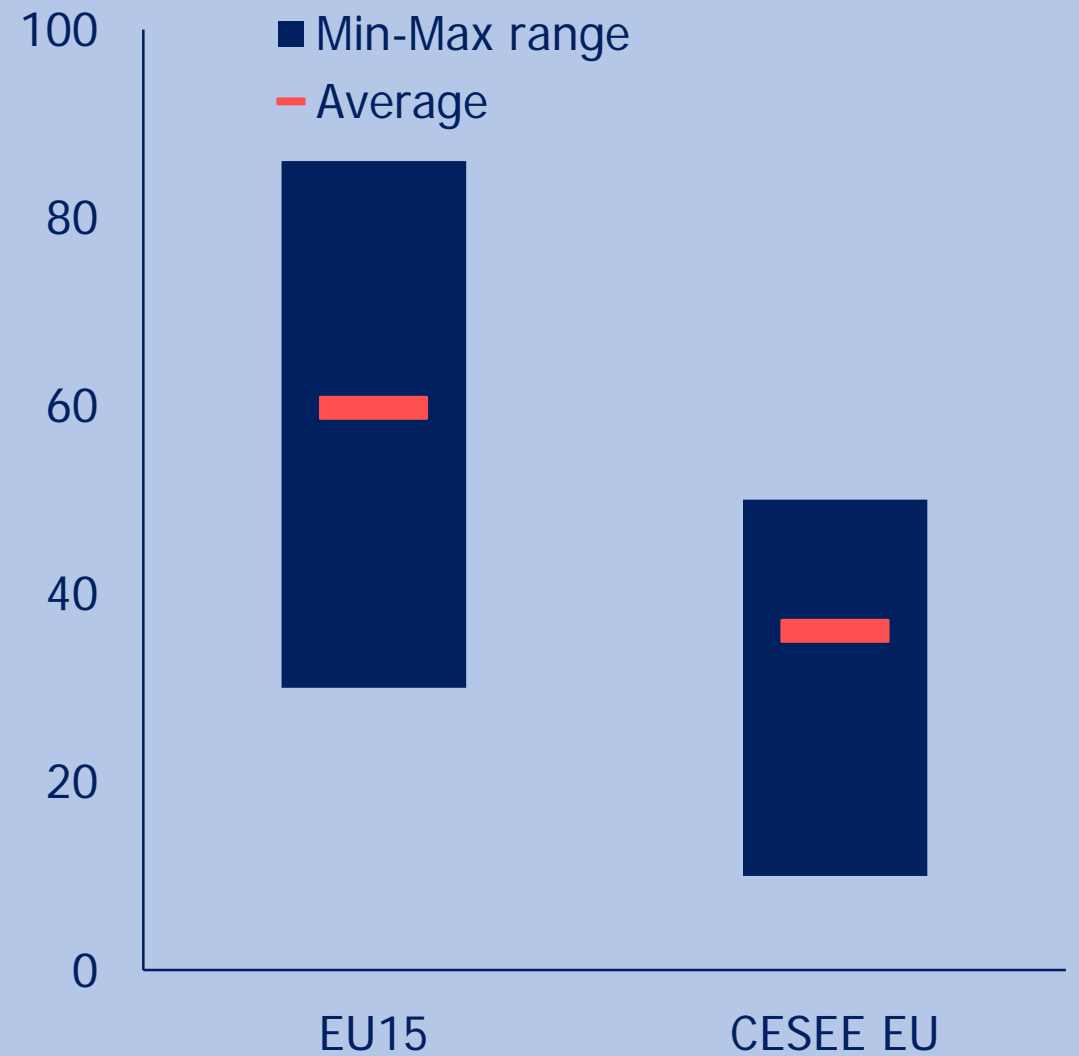
Worldwide distribution excluding LICs

CESEE's judiciary efficiency good but challenges in perceived independence

Resolution Rate: Insolvency Cases, 2014 1/



Perceived Independence of Courts, 2017 2/



1/ Values higher than 100 indicate that more cases are resolved than received, and suggest higher efficiency.

2/ Percent of responders that ranked independence of courts in their country fairly or very good.

CASE STUDIES:

BOSNIA AND HERZEGOVINA

CROATIA

ESTONIA

POLAND

ROMANIA

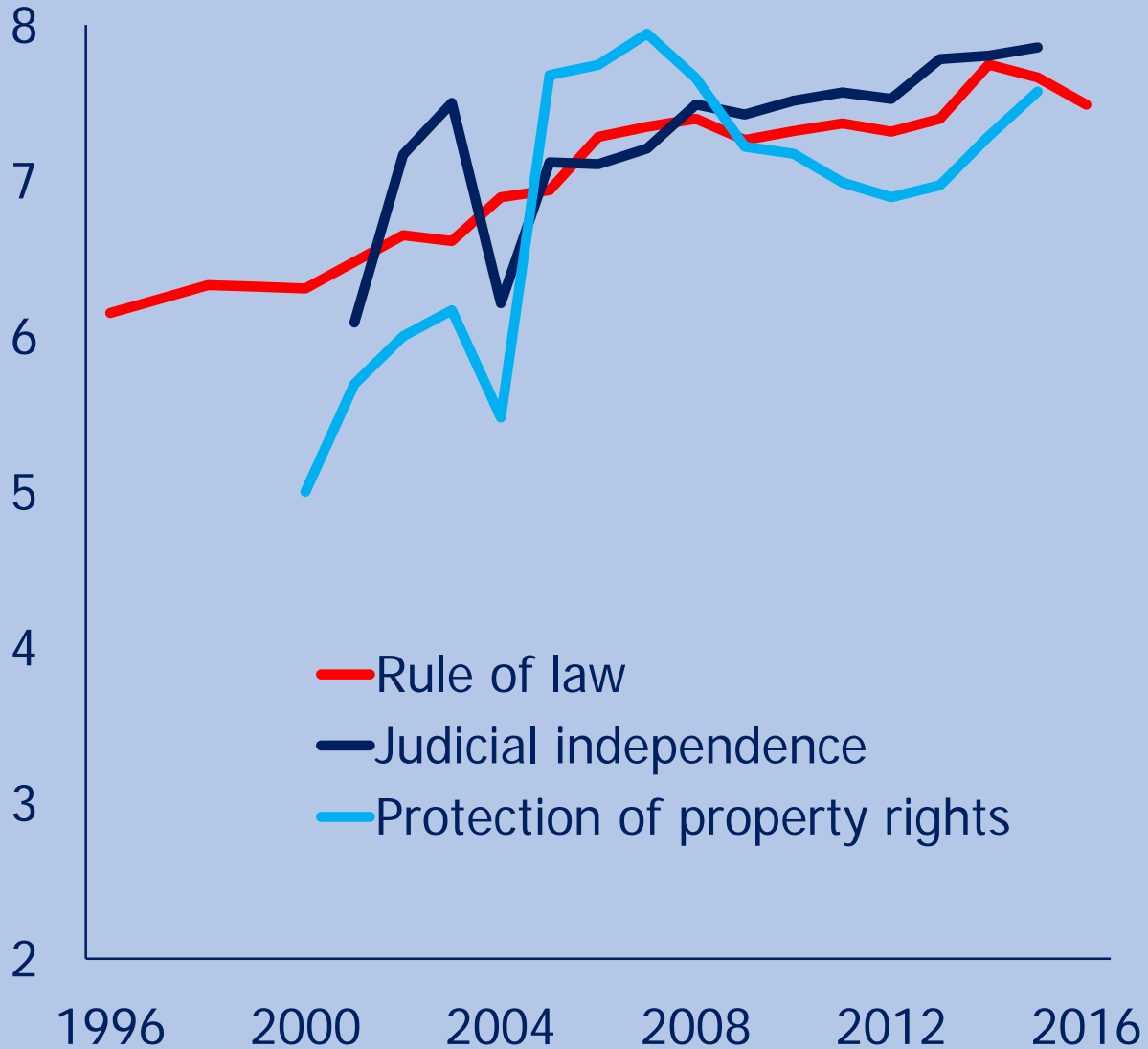
SERBIA



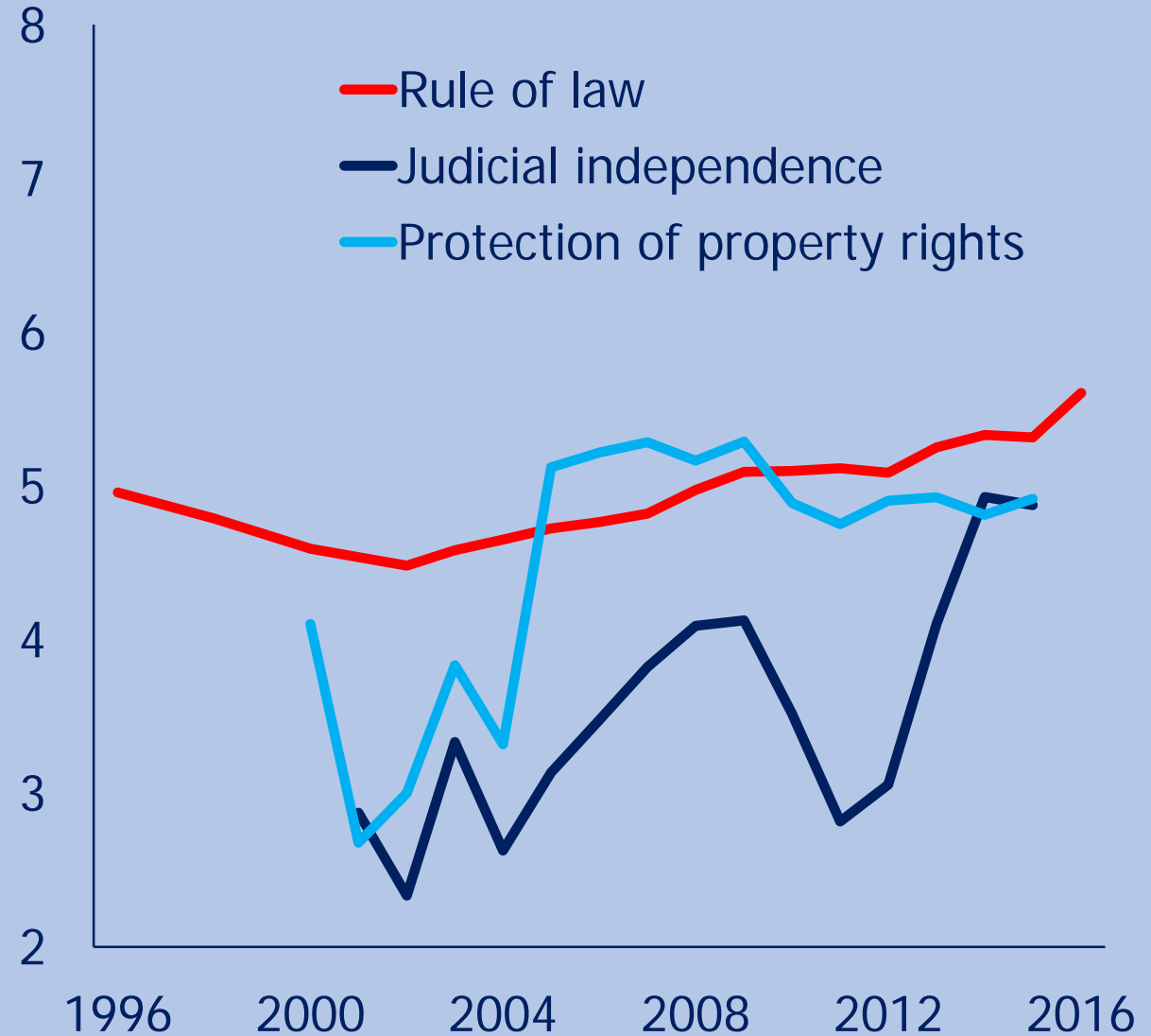
Factors Facilitating Reform

(Index = 0 to 10, 0=worst, 10=best)

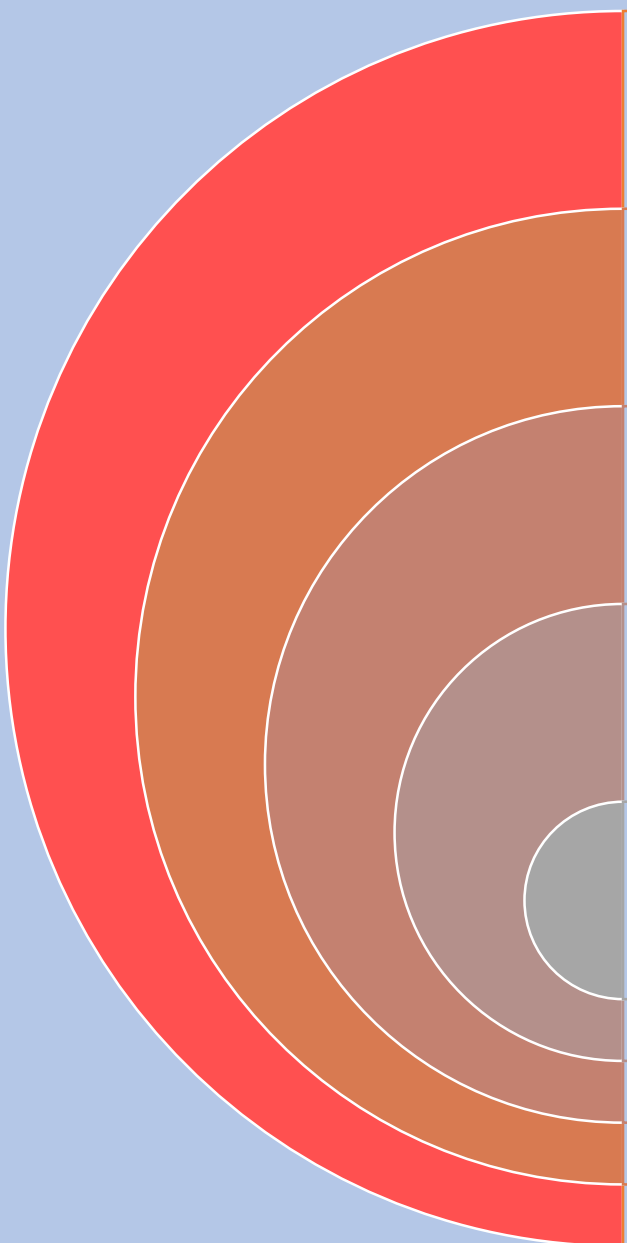
Estonia



Romania



Comparison of factors facilitating reform



A. Initial Conditions:	<ul style="list-style-type: none">• Estonia: Vibrant civil society; clean break from communism• Romania: New government still connected to old regime
B. Distribution of Resources:	<ul style="list-style-type: none">• Estonia: Inclusive privatization; economy opened up quickly• Romania: Privatization lead to concentration of resources and delayed liberalization
C. Transparency:	<ul style="list-style-type: none">• Estonia: Media freedom and e-government• Romania: Freedom of Information Law promoted by EU helped civil society
D. State capacity:	<ul style="list-style-type: none">• Estonia: New judges were chosen based on merit• Romania: Stop-and-go reforms but some improvement
E. Role of the EU:	<ul style="list-style-type: none">• Estonia: EU provided benchmarks for high standards• Romania: EU membership acted as a catalyst for reforms

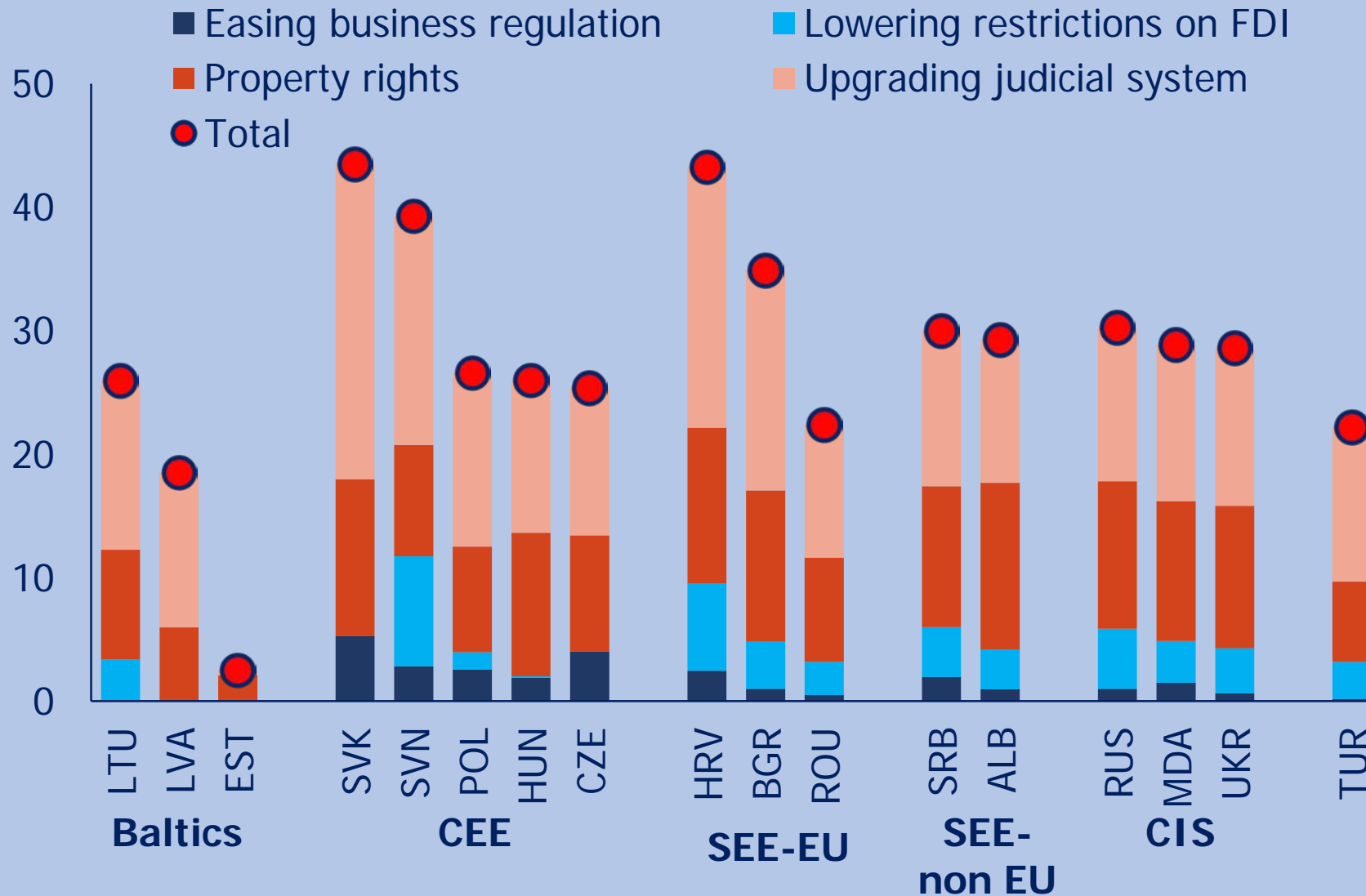
Key messages

- Strengthening institutions a priority for next generation of reforms
- Some countries successfully reformed, though reversals also occurred
- Distributional factors key to successful judicial reforms; privatization and opening up had notable effects
- Strengthened transparency and accountability conducive to improvements in judicial effectiveness
- The quality of the public administration was another critical factor
- The EU was a strong external anchor but sustainability of reforms appears to depend mainly on domestic factors

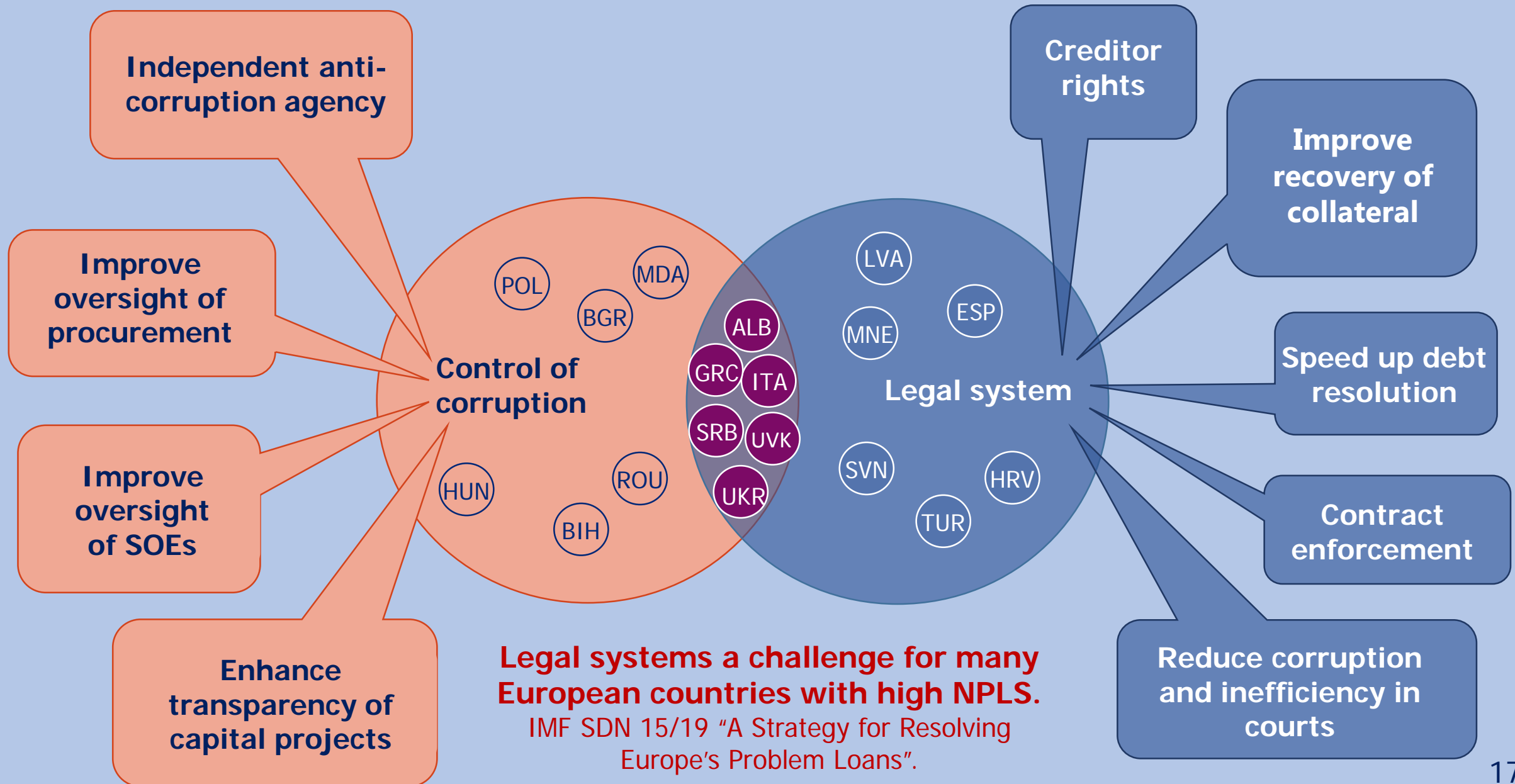
ADDITIONAL SLIDES

Upgrading institutions key for moving to a higher growth path

CESEE: Estimated Efficiency Gains from Institutional Reforms
(Percent; potential improvement in TFP)



The Fund's Recommendations on Governance and Institutions



Factors Facilitating Reform, 1993

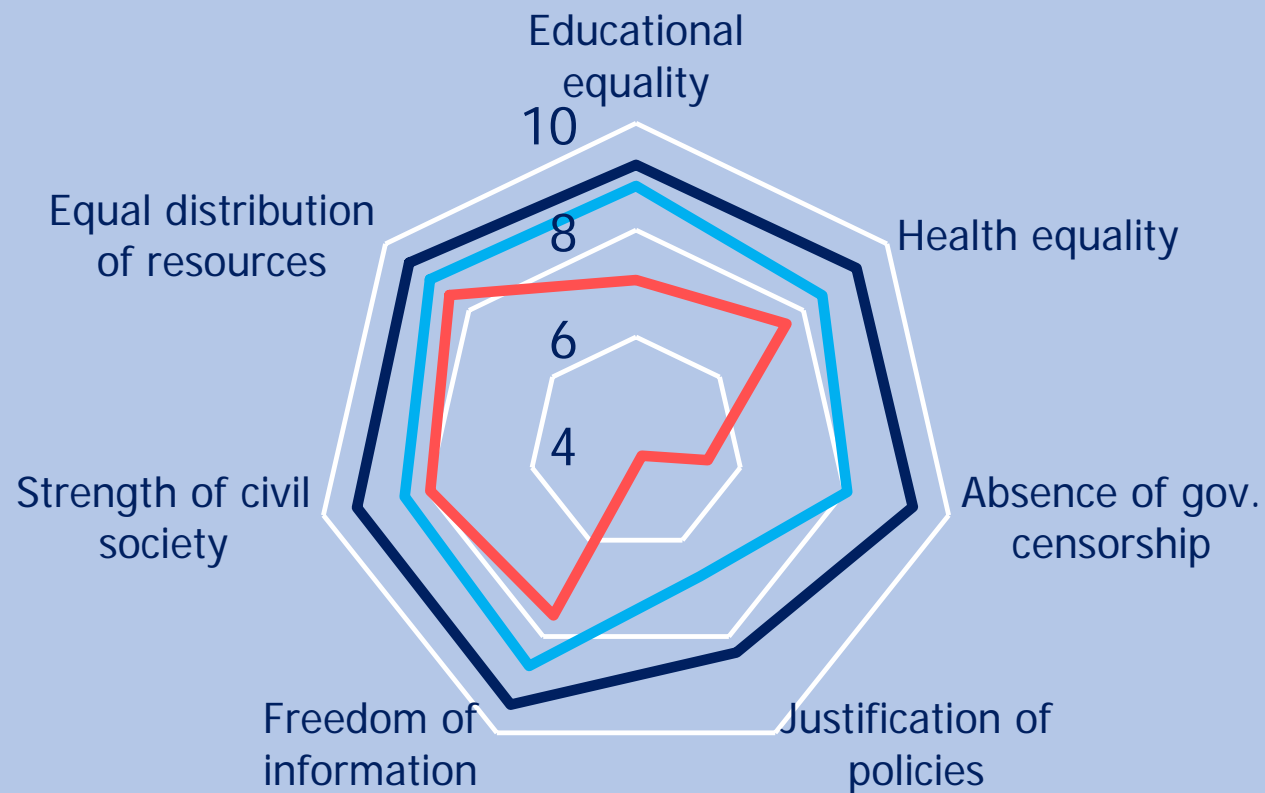
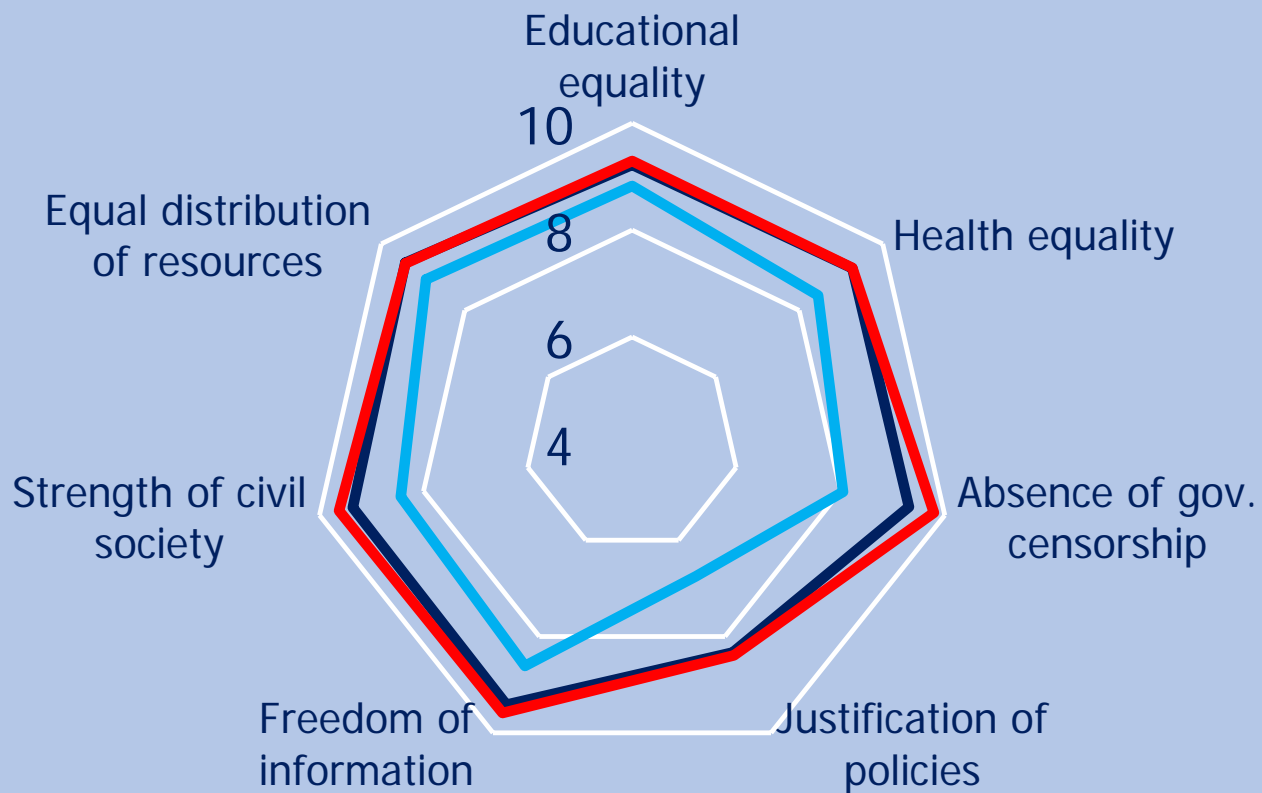
(Index = 0 to 10, 0=worst, 10=best)

Estonia

Romania

— EU15 — CESEE EU — Estonia

— EU15 — CESEE EU — Romania



CROSS- COUNTRY EVIDENCE

Conditional Correlations

Factors Affecting Institutional Quality						
	Judicial independence			Protection of property rights		
Equal distribution of resources	2.225** (1.076)	3.141** (1.283)	1.747* (1.033)	0.143 (0.846)	1.698* (0.991)	-0.405 (0.815)
Freedom of the press	0.00968 (0.00625)	0.0484** (0.0235)	0.0425*** (0.0140)	0.0114*** (0.00443)	0.0708*** (0.0167)	0.0545*** (0.0140)
Impartial public administration	0.875*** (0.224)	0.865*** (0.232)	1.251*** (0.248)	0.507*** (0.171)	0.462*** (0.179)	1.008*** (0.166)
Lower barriers to trade	0.194*** (0.0715)	0.183** (0.0722)	0.196*** (0.0737)	0.573*** (0.0972)	0.561*** (0.0975)	0.576*** (0.103)
Institutional quality of trading partners	0.396*** (0.131)	0.356*** (0.131)	0.356*** (0.129)	0.109 (0.106)	0.0284 (0.111)	0.0518 (0.103)
Old age dependency ratio	-0.0685** (0.0291)	-0.0648** (0.0295)	-0.0676** (0.0289)	-0.0469*** (0.0178)	-0.0458** (0.0179)	-0.0479*** (0.0180)
Control of corruption in politics	0.425*** (0.114)	0.407*** (0.113)	0.416*** (0.114)	0.349*** (0.107)	0.303*** (0.107)	0.300*** (0.0998)
GDP per capita, constant PPP	0.578** (0.244)	0.599** (0.244)	0.529** (0.246)	0.840*** (0.190)	0.920*** (0.181)	0.799*** (0.181)
Freedom of the press x Equal distribution of re	-	-0.0612* (0.0342)	-	-	-0.0965*** (0.0342)	-
Freedom of the press x Impartial public admini	-	-	-0.0150*** (0.00577)	-	-	-0.0203*** (0.00616)
Constant	-8.770*** (1.770)	-9.316*** (1.811)	-8.768*** (1.814)	-9.853*** (1.313)	-9.316*** (1.811)	-9.961*** (1.249)
Observations	204	204	204	204	204	204
Number of id	75	75	75	75	75	75
Time effect	Yes	Yes	Yes	Yes	Yes	Yes
Robust standard errors in parentheses *** p<0.01, ** p<0.05, * p<0.1						