

Economic Growth in ECA

Three Resources for the Region

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Europe and Central Asia Talk Organized by ECACE

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Based on work by World Bank Group economists

Three Valuable Resources

- B-Ready: Business Readiness Report
 - A resource for continuous dialogue
- Europe 4.0: Digital Technologies
 - A template for policy discussions about technology
- WDR 2024: The Middle-Income Trap
 - An opportunity for thought leadership on growth

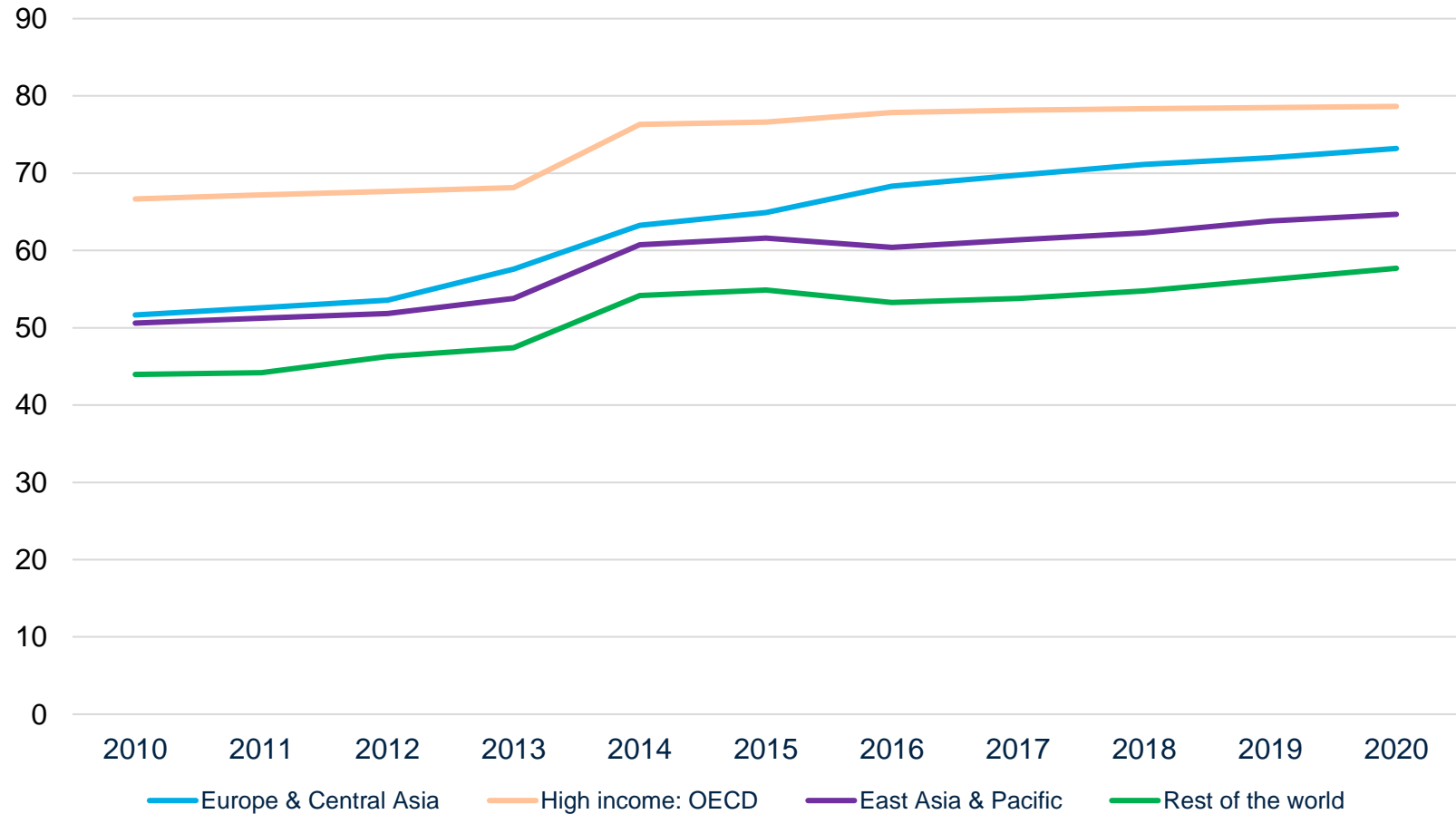
Recurrent themes: diagnostics, data, and destruction

- Better growth diagnostics are available
 - Economists still rely on X-rays when MRIs are available
- Successful strategies need good data
 - Don't do policy without decent data
- Crises aid the destruction of old structures
 - Capitalize on economic and ecological emergencies

B-Ready

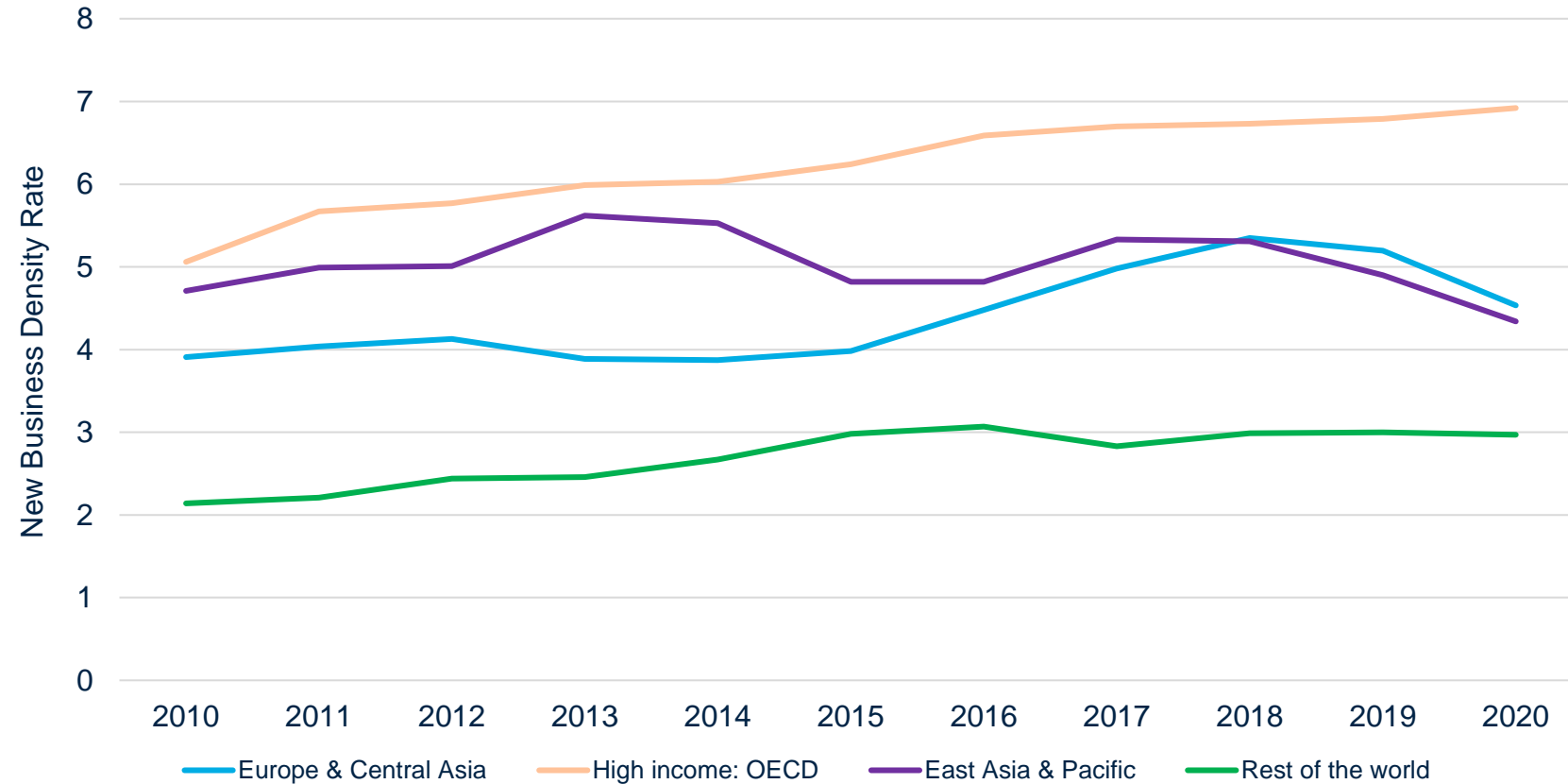
- **An even better Doing Business Report**
- **Tripling the scope and frequency of Enterprise Surveys**
- **Subnational Business Readiness**

More catch-up in ECA than elsewhere



Source: Doing Business database.
Note: The measure is normalized to range from 0 to 100, with 100 representing the best regulatory performance. Because of changes over the years in methodology and in the economies and indicators included, the improvements are measured year-on-year using pairs of consecutive years with comparable data.

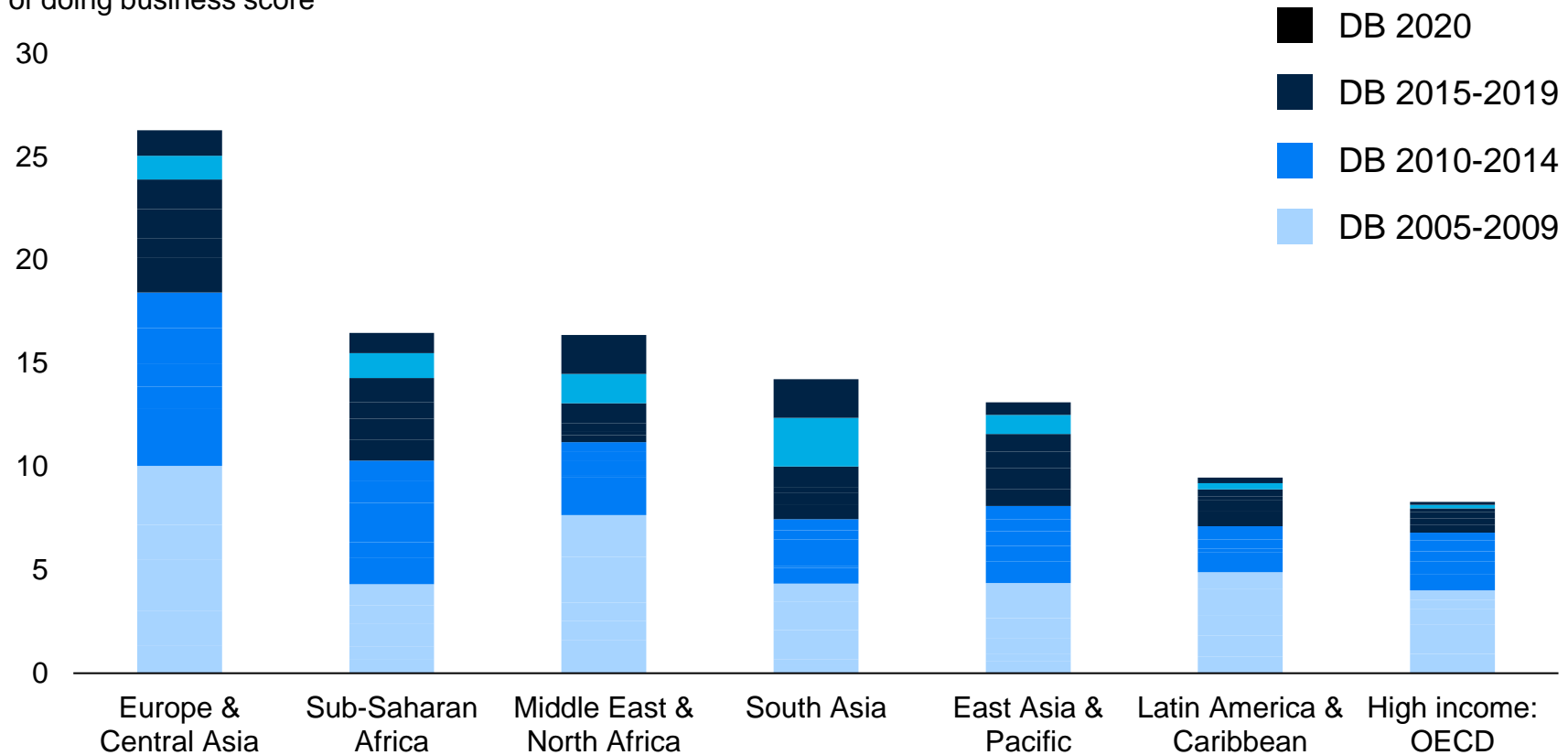
Business creation in ECA lags the OECD—and has fallen since 2018



Source: Entrepreneurship database.
Note: The new business density rate is the number of newly registered firms with limited liability per 1,000 working-age people (ages 15-64) per calendar year. Regional rates are calculated by taking the simple average of the economies within that region.

ECA improved business regulations more—until 2020

Average improvement in the ease of doing business score

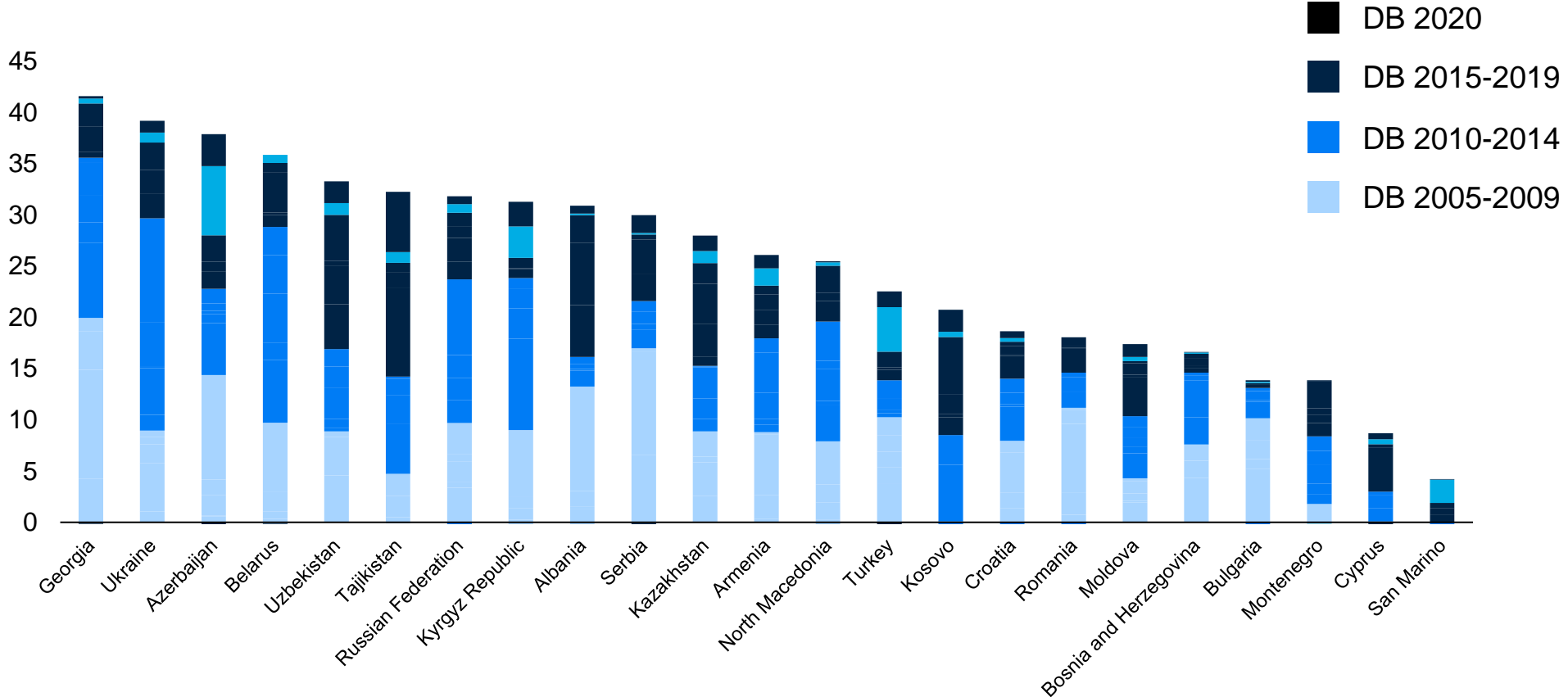


Source: *Doing Business* database.

Note: The measure is normalized to range from 0 to 100, with 100 representing the best regulatory performance. Because of changes over the years in methodology and in the economies and indicators included, the improvements are measured year-on-year using pairs of consecutive years with comparable data.

Big Variations Within ECA

Aggregate improvement in the ease of doing business score



Source: Doing Business database.

Note: The measure is normalized to range from 0 to 100, with 100 representing the best regulatory performance. Because of changes over the years in methodology and in the economies and indicators included, the improvements are measured year-on-year using pairs of consecutive years with comparable data.

Europe 4.0

- **Digital investments**
- **Business process innovation**
- **Tax and transfer mechanisms**

Europe 4.0

- **Main questions**

- How to be more precise about technologies
- What it takes to be strategic in responding to technological change
- Why Europe should be more optimistic than it is

- **Technology is complicated**

- But it can be understood well with economic methods.
- Use economics to think precisely about the nature of technical change
- Identify the effects of new technologies on economic activity: productivity, social distribution, and geographic location

- **Europe should be more strategic—and less pessimistic**

- Europe wants to do more than the US and China
- Europe also has some assets that the US and China do not

Distinguish between technology types

Three types of process technologies—*all driven by data*

- **Transactional technologies** better match supply and demand by lowering information asymmetries; examples include e-commerce platforms and blockchain.
- **Informational technologies** exploit the exponential growth of data and reduced cost of computing; examples include cloud computing, big data analytics, and machine learning.
- **Operational technologies** combine data with physical automation to reduce production costs; examples include smart robots, 3D printing and the Internet of Things (IoT).

Tailor strategy to objectives

- **Europe needs to do more than China and the US**
—*because it wants more things than them*
 - Transactional technologies increase **competitiveness** and tend to aid both **convergence** and **cohesion**.
 - Informational technologies increase **competitiveness**, are relatively neutral for **convergence**, but pose problems for **cohesion** [?]
 - Operational technologies increase **competitiveness** but generally weaken **convergence** and **cohesion**.

Calibrate policies

- **Speed** up the adoption and diffusion of Industry 4.0 technologies, **shape** new technologies to match Europe's strengths and weaknesses—and **smooth** their *destabilizing effects so there is less resistance to them*
 - **Speeding—Markets not champions:** Europe's regulatory institutions are more independent (some European countries are global leaders in operational technologies, but European higher education systems are not well-integrated with industry)
 - **Shaping—Data, the Fifth Freedom:** Europe's approach is a plus because data belong to individuals, not enterprises or the government (GDPR a good base, but it has to accord additional rights to Single Market participants since they have more responsibilities).
 - **Smoothing—Two-track Europe;** Equalize digital opportunities by completing the 3rd industrial revolution in lagging member states (many European countries have well-developed fiscal systems, but most also have weak labor markets).

WDR 2024

- **European Roots: Schumpeter, Aghion and Akcigit**
- **Europe's Preservation Problem: The Accession Exception**
- **ECA-relevant: The Report for Our Times**

Joseph Schumpeter, 1883-1950

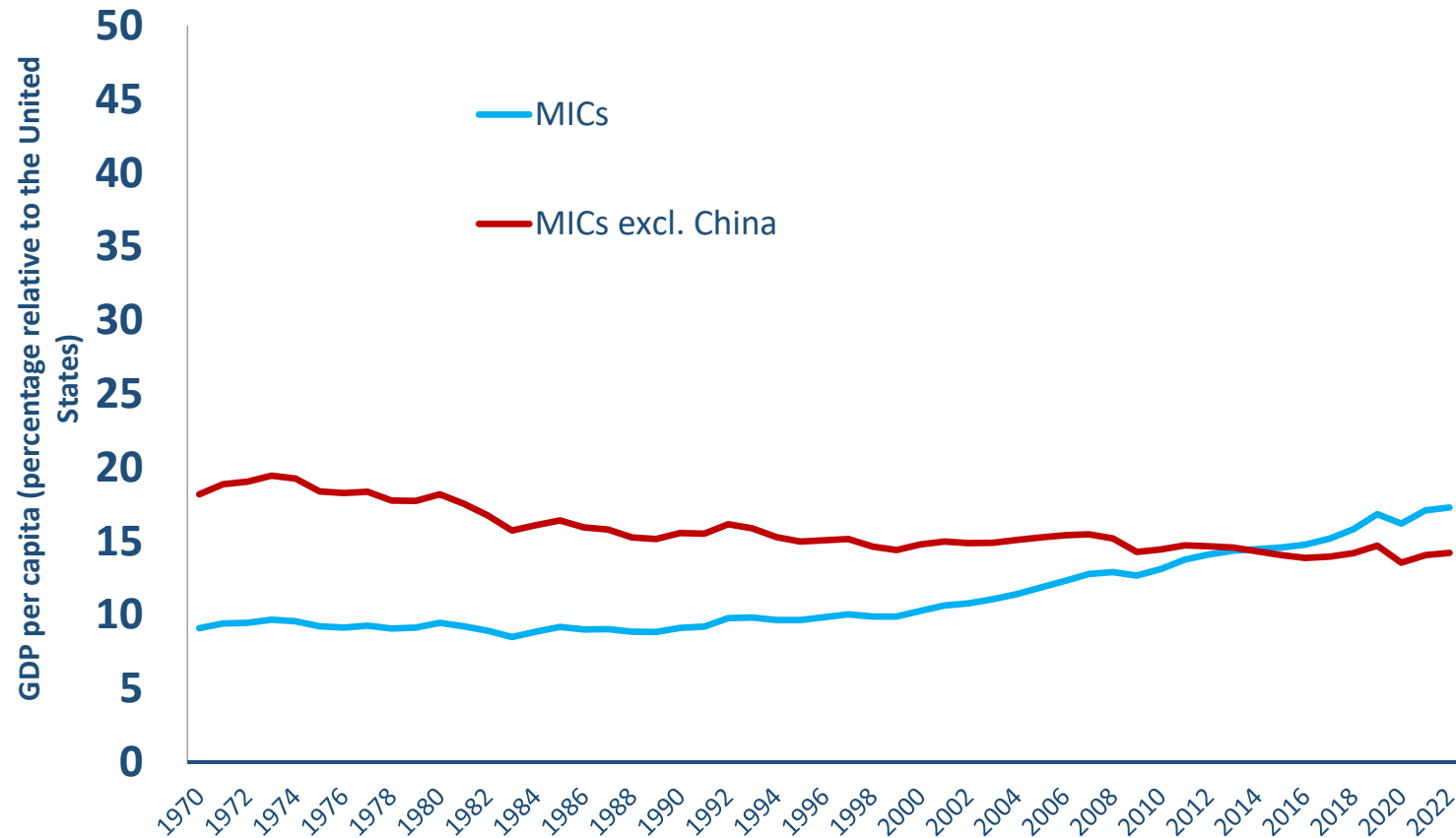
in Capitalism, Socialism and Democracy (1942)

“... the problem that is usually being visualized is how capitalism administers existing structures, whereas the relevant problem is how it creates and destroys them.”

Creative Destruction and the Middle-Income Trap

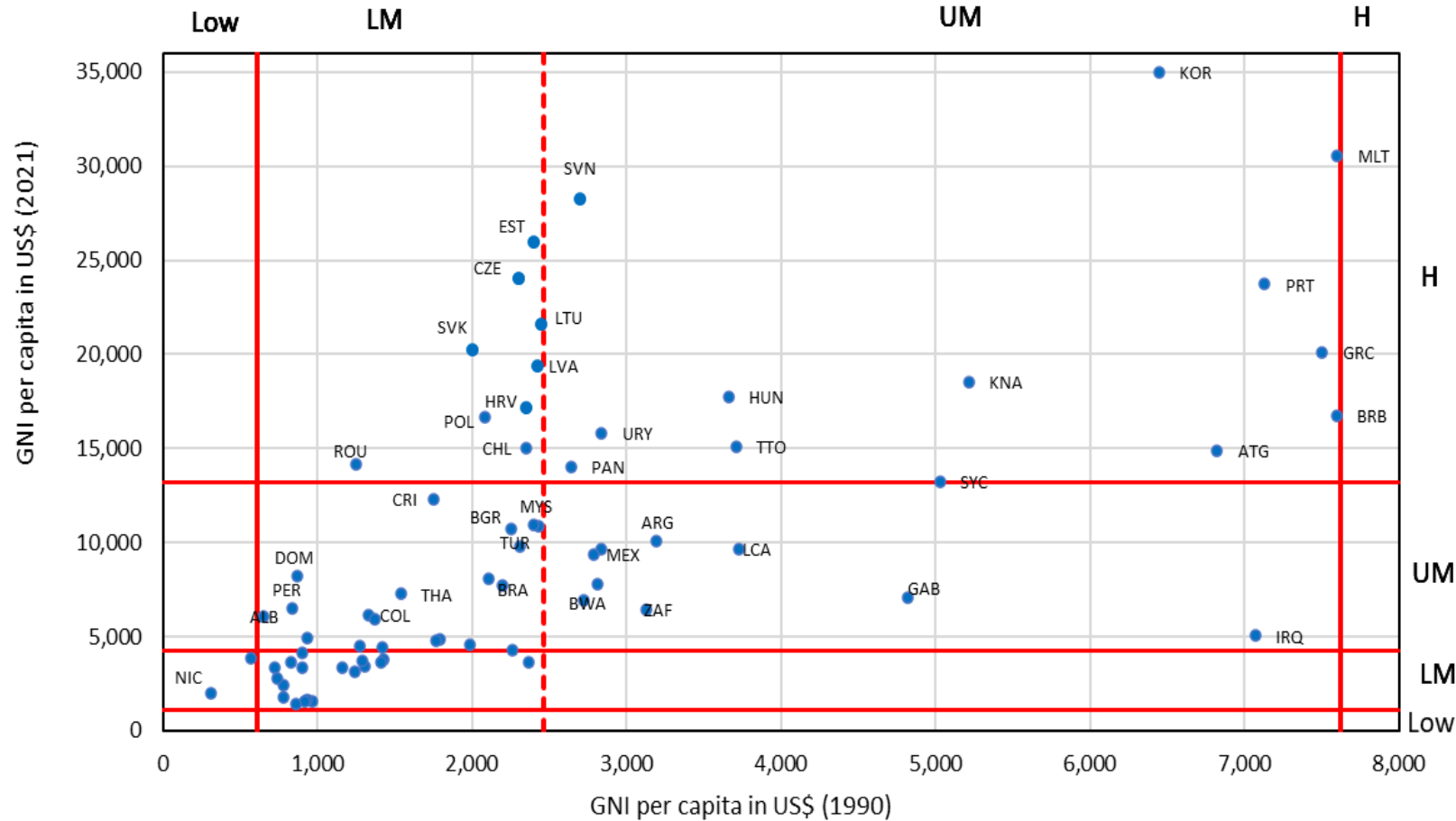
- Part I – Facts
 - Defining the Middle-Income Trap
 - Distinguishing Low and Upper MICs
- Part II – Analysis
 - Modern Schumpeterian Creative Destruction
 - Incumbency, Meritocracy, and Political Economy
- Part III – Policy
 - Enterprise, Equality, Energy
 - Bad data = bad policies

Convergence has never been easy— and it's not getting any easier



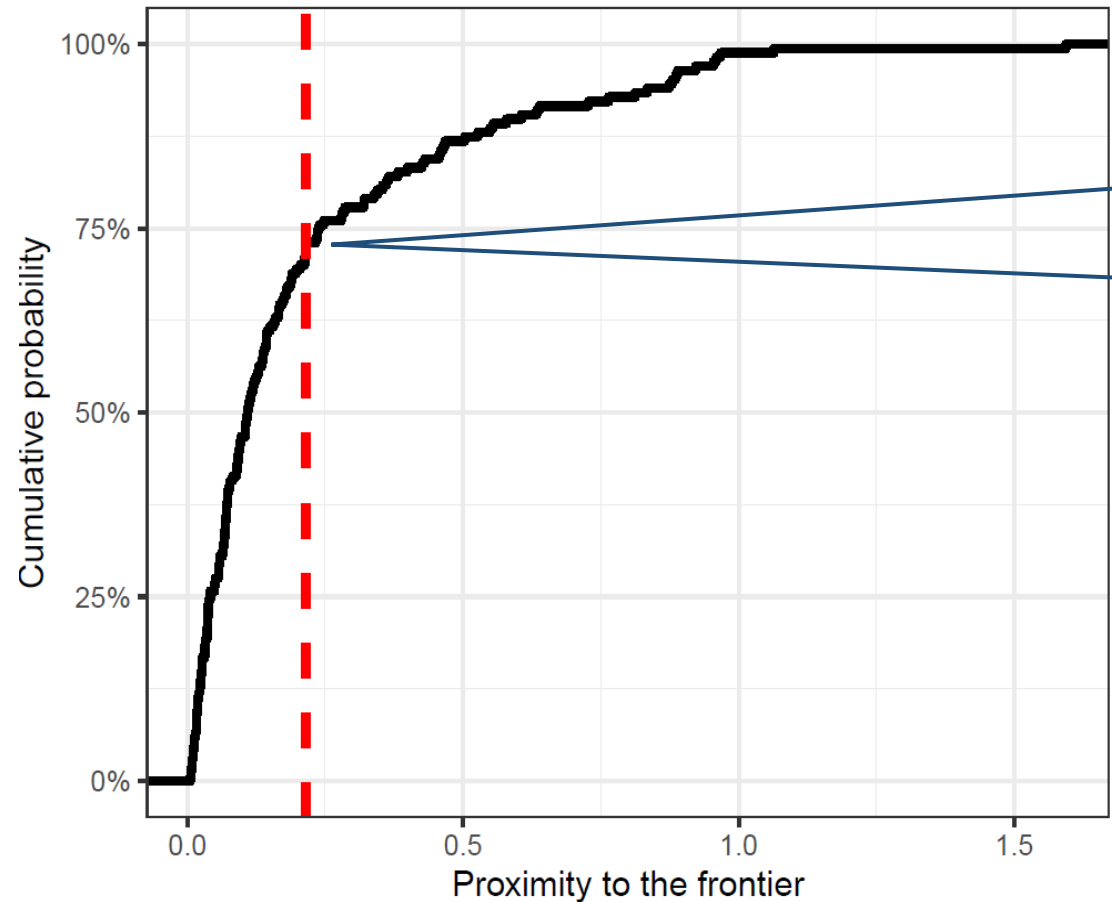
Source: WDR 2024 team using the World Development Indicators.

The Middle-Income Trap— and the European Exception



Source: WDR 2024 team using the World Development Indicators.

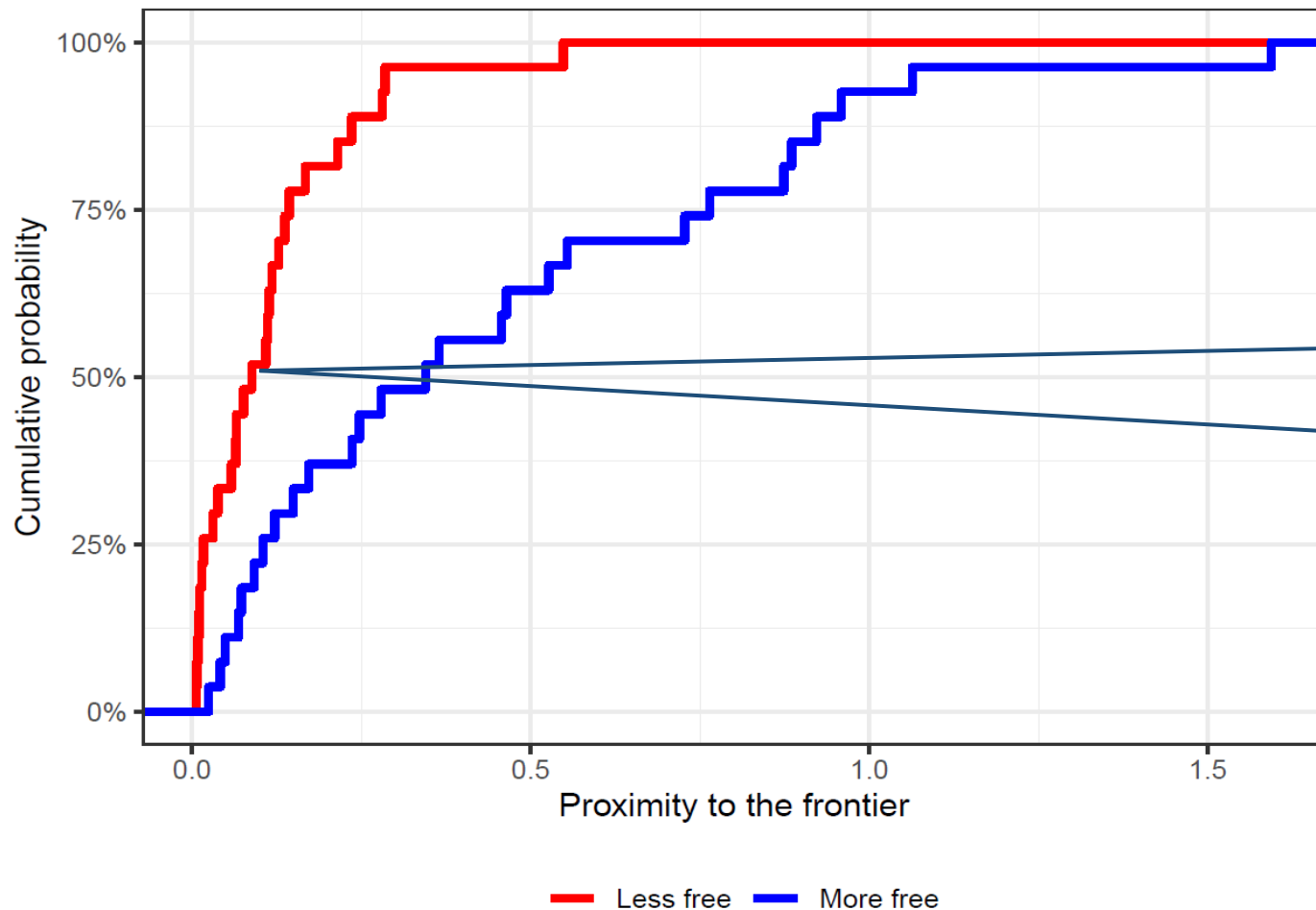
A discernible slowdown during middle income— at about 11-21 percent of US income



Mean growth
slowdown takes place
at GDP per capita of
about 20 percent of
that of United States

Source: WDR 2024 team using
team using data from the Penn
World Tables 10.01.

Low economic freedoms slow down convergence— much earlier in development

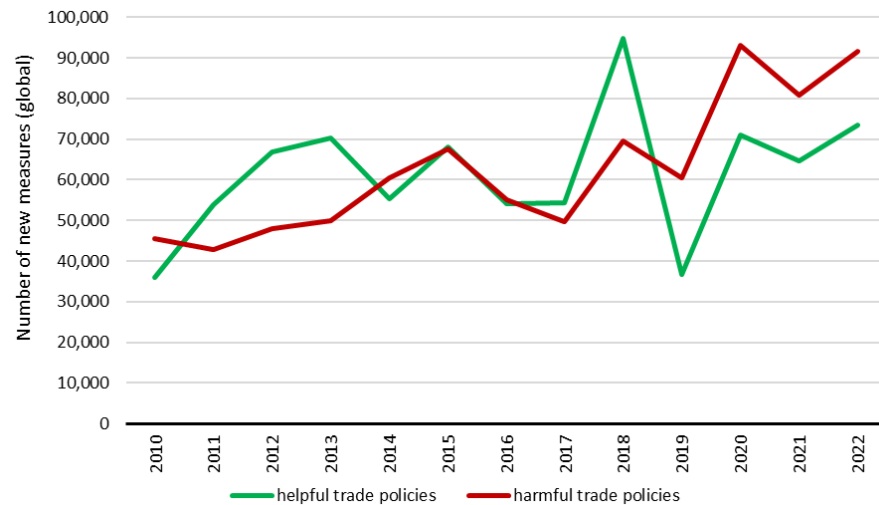


Less free economies
converge much
slower than freer
countries

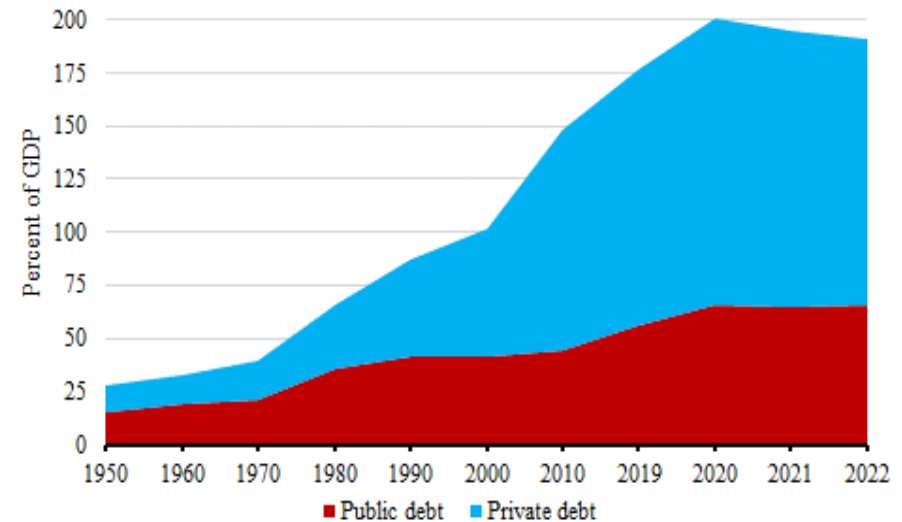
Source: WDR 2024 team using
team using data from the Penn
World Tables 10.01.

Shrinking spaces—for both technology infusion from abroad and structural reforms at home

Harmful trade policies globally outpace helpful trade policies

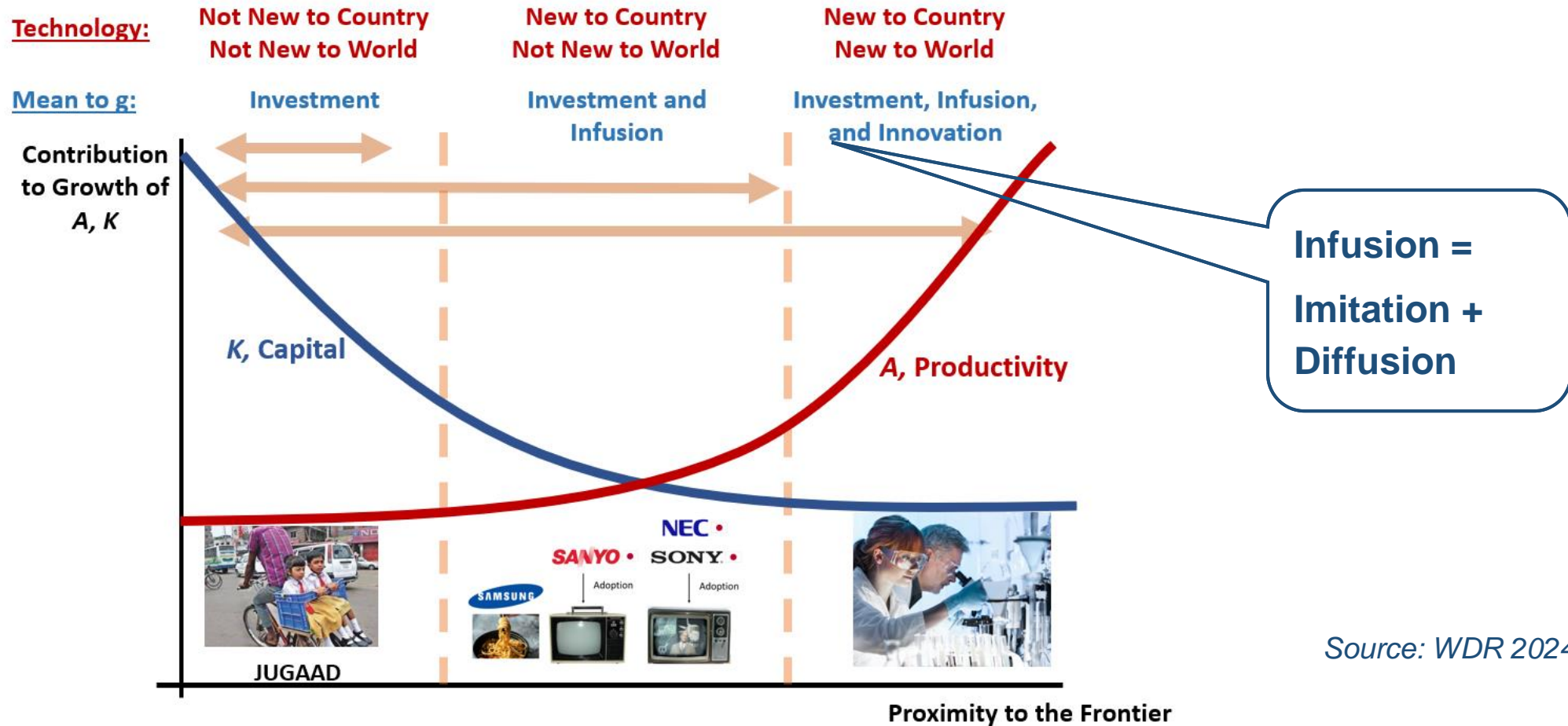


Most developing economies are severely indebted, reducing room for painful reforms



Source: WDR 2024 team using the Global Trade Alert database and IMF debt monitor data

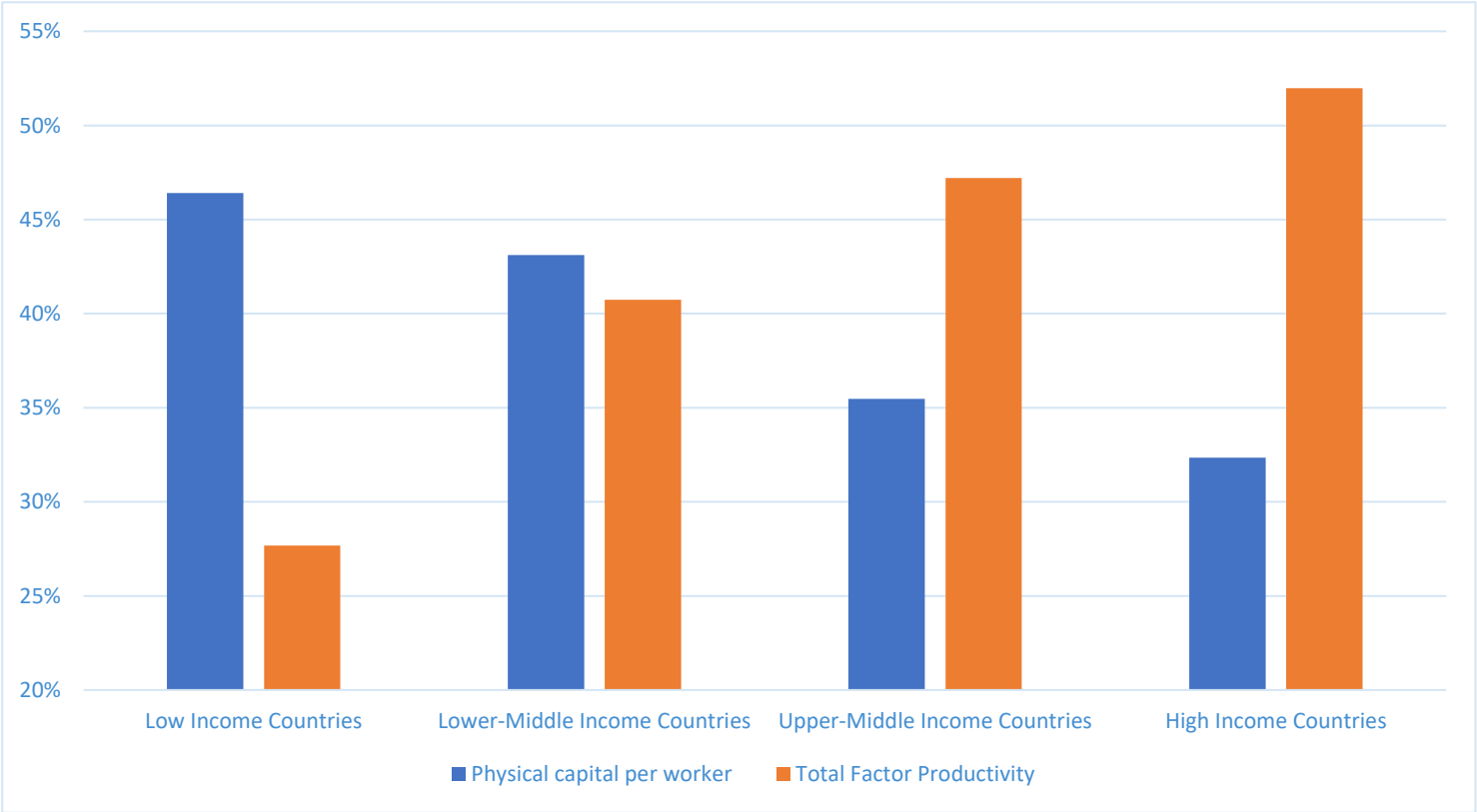
Growth is (mostly) cumulative— investment, “infusion” and innovation



No trap for Poland: 25 percent of Western European income in 1990, now 75 percent

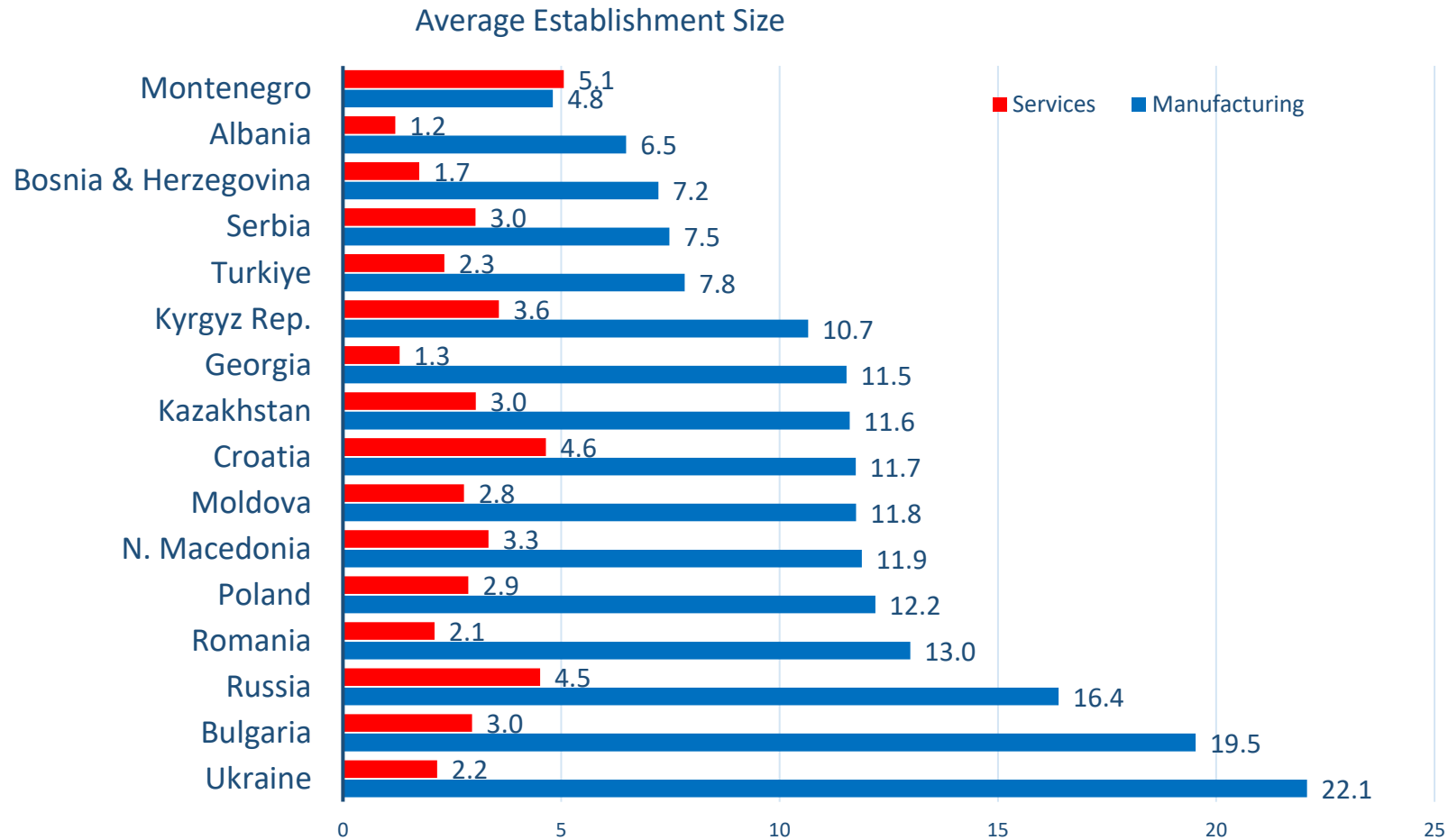
- **Investment first, then infusion, followed by innovation**
 - Poland first narrowed productivity gaps by adopting technologies from advanced economies.
 - Big increase in tertiary education from 15 percent to 42 percent between 2000 and 2012.
- **Comprehensive reforms, early on, to quicken productivity growth**
 - Trade competition as part of EU accession
 - Hardening budget constraints for state-owned enterprises domestically
- **Disciplining incumbency shifting to innovation**
 - Improving managerial incentives and capabilities in SOEs in anticipation of privatization
 - Managers at Polish SOEs shift from production targets to profitability and market share
 - Domestic investments in innovation accelerated Poland's move toward technological frontier.

Growth in middle-income countries is different—the rich are more productive



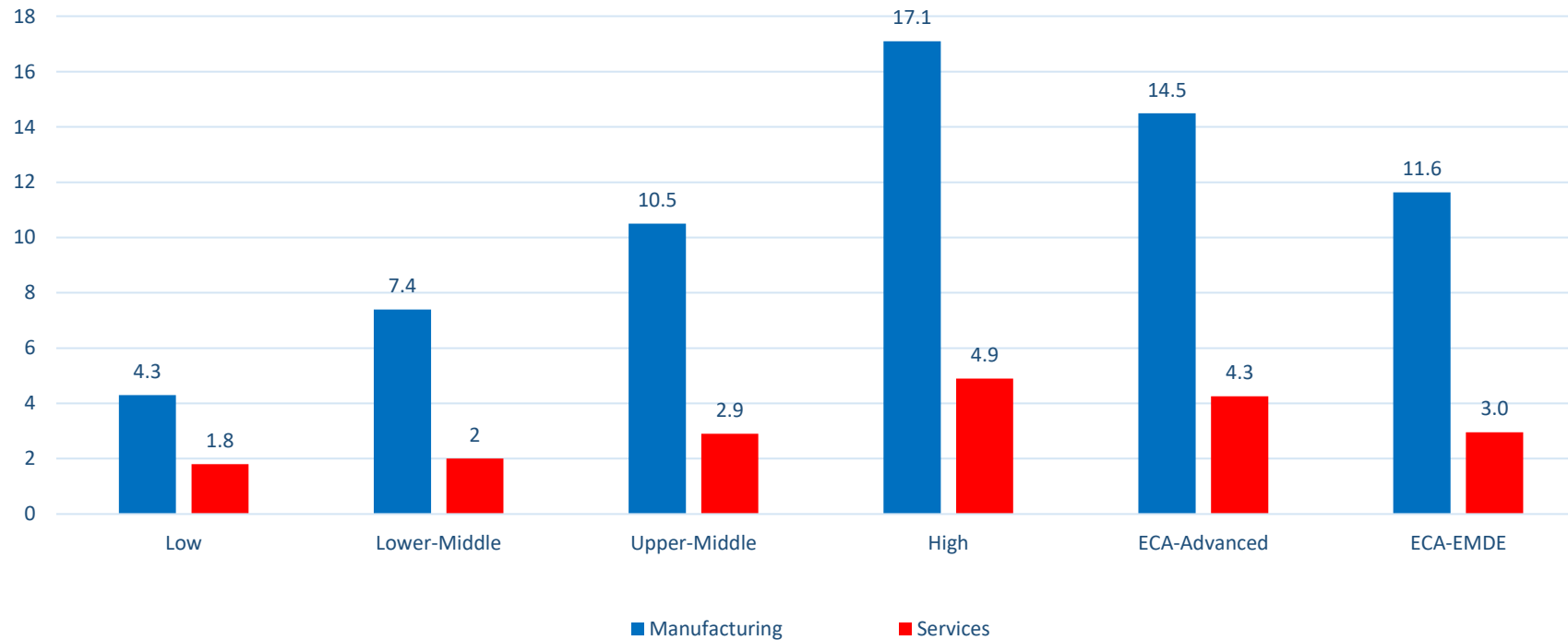
Source: WDR 2024 team calculations using the Penn World Table (PWT) version 10.01

Firm size increases with development, so big firms can't all be bad



Size is a wasteful preoccupation for policymakers

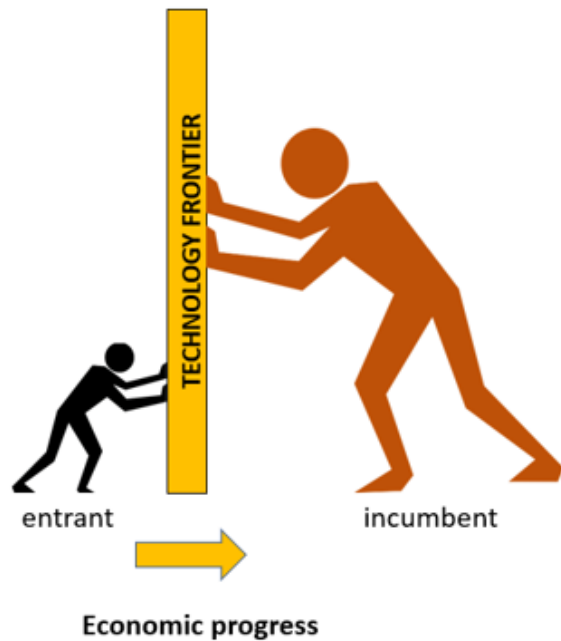
Average Establishment Size



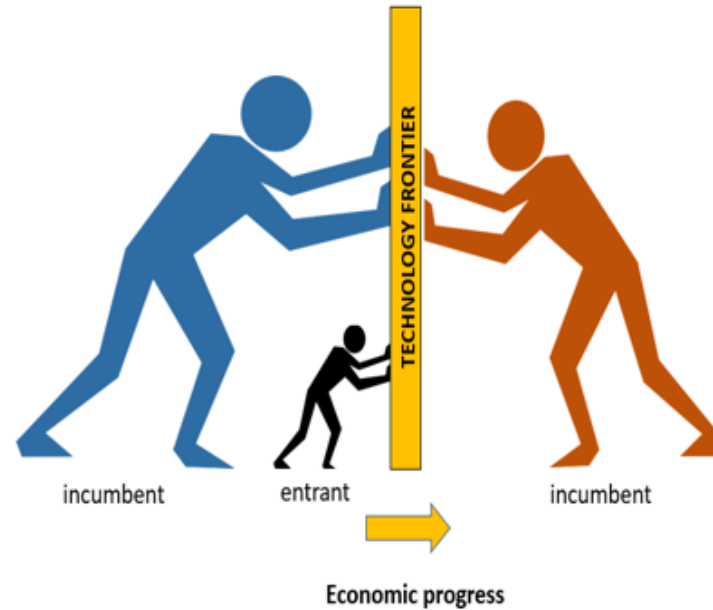
Balancing the forces of creation, preservation and destruction

- **Creation:** incumbents and entrants compete by creating economic **value**
- **Preservation:** economic, social and political structures are susceptible to capture by powerful **incumbents**
- **Destruction:** the forces of preservation are weakened only by the necessary evil of **crises**

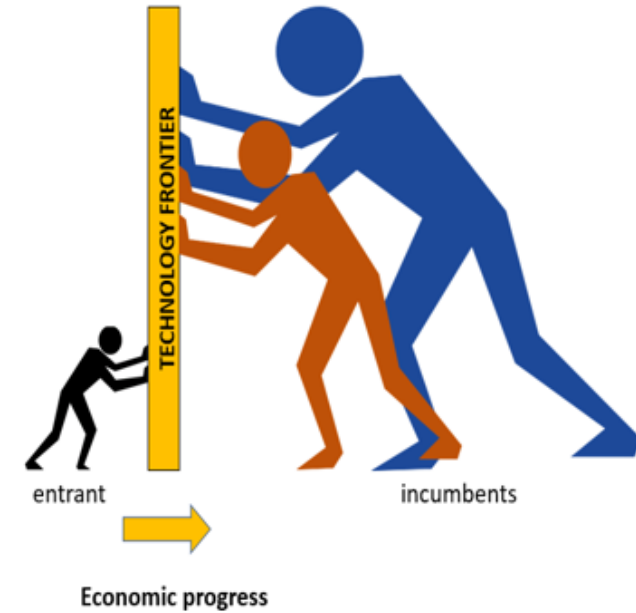
New priors: incumbents are not all the same



Schumpeter's view: entrants create value and displace incumbents



A modern view: Incumbents can also create value



A pessimistic view: Incumbents can collude and capture institutions to block all value creators

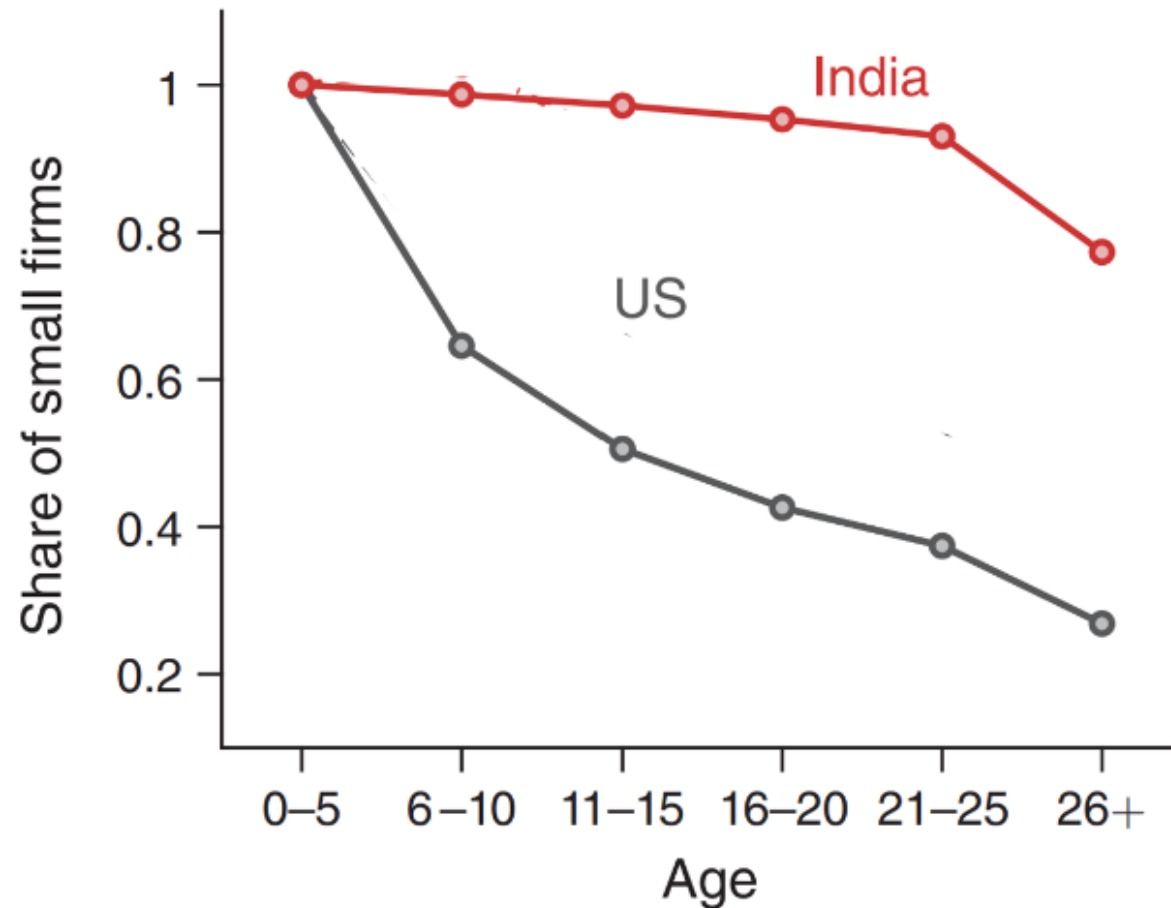
New diagnostic tools

- **Diagnostics typically focus on firm productivity, firm size distribution and market concentration**
 - What is the (domestic) market share of small, medium and large firms ?
 - Are there normal levels (relative to some benchmark) of firm turnover?
 - What factors determine whether small and medium enterprises export?
- **Growth diagnostics should instead assess value chains—the linkages between entrants and incumbents, between small and large enterprises, between domestic and multinational firms**
 - Are firms that exit the industry less or more productive than survivors?
 - Do leaders compete by upgrading technology through R&D and licensing?
 - Does market leadership change often or do incumbents maintain positions?

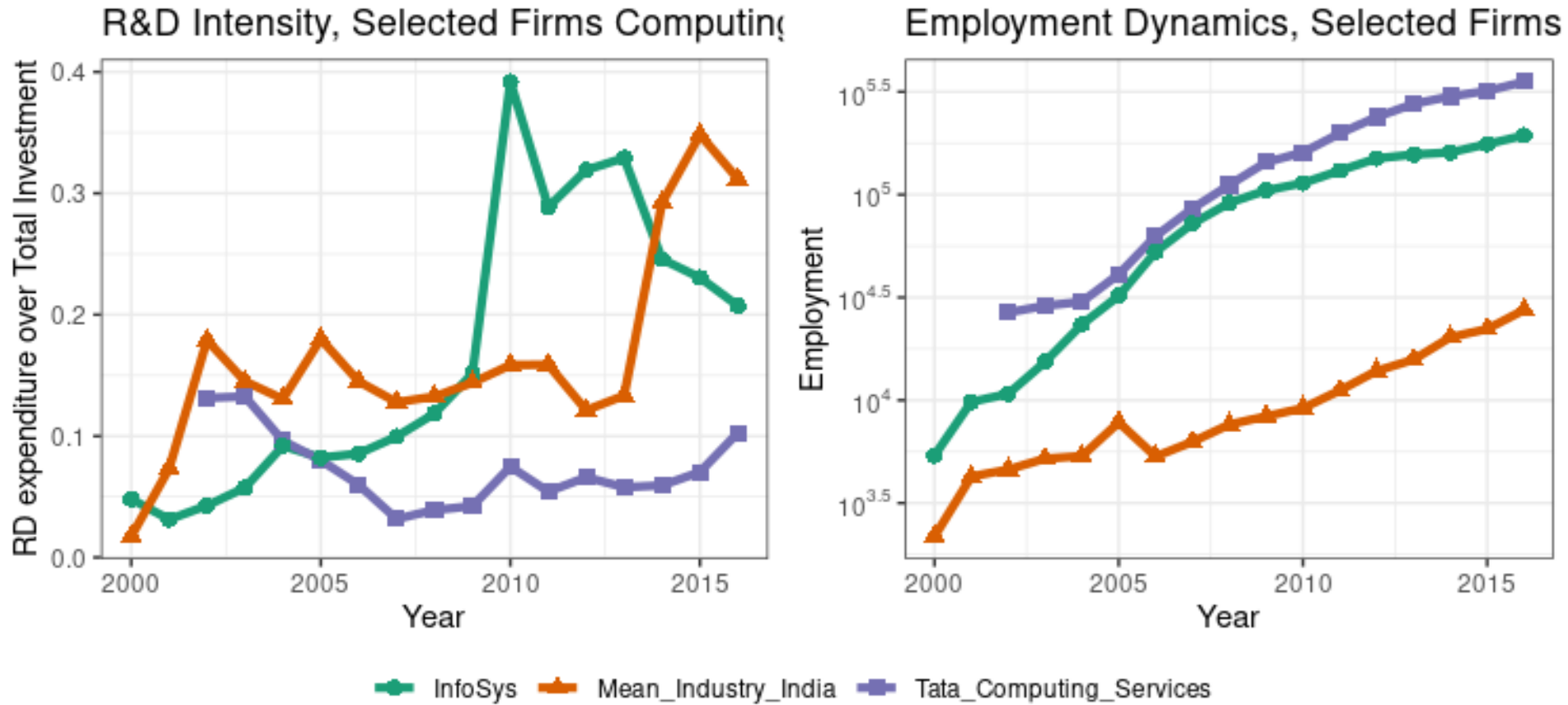
X-Rays

MRIS

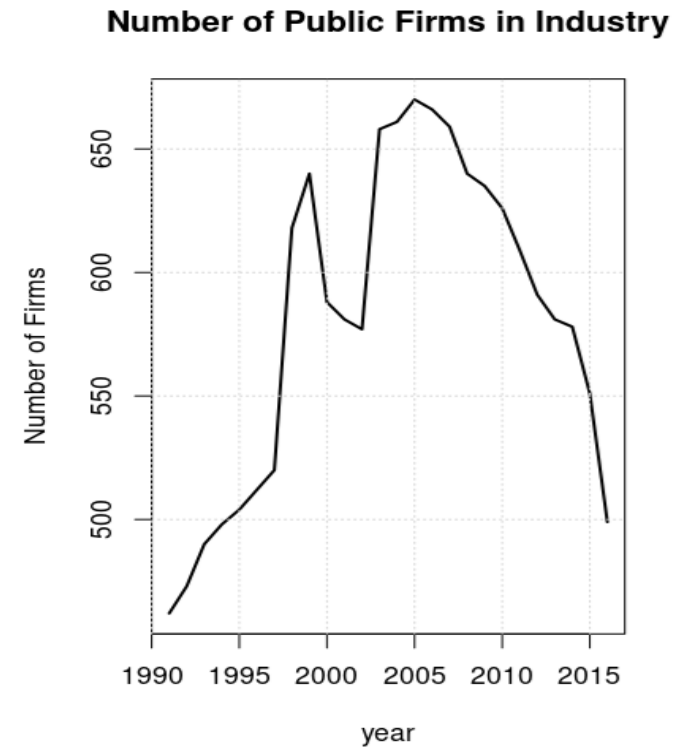
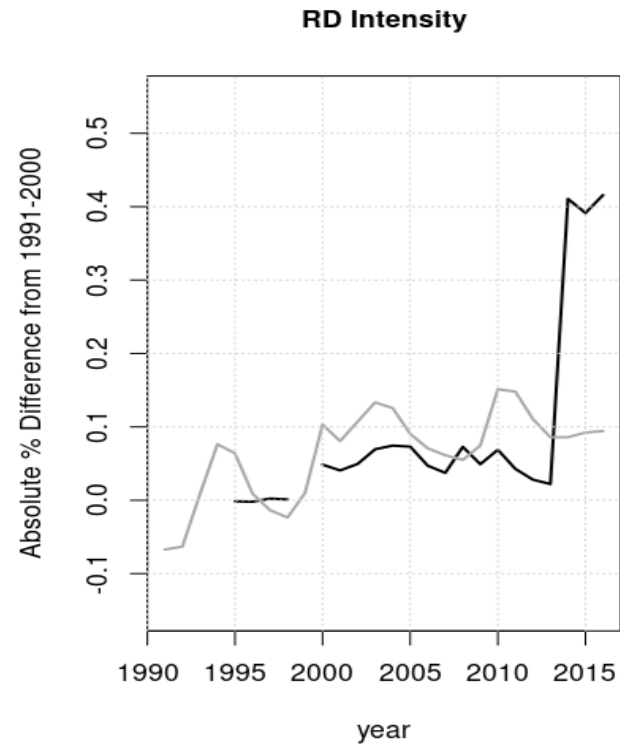
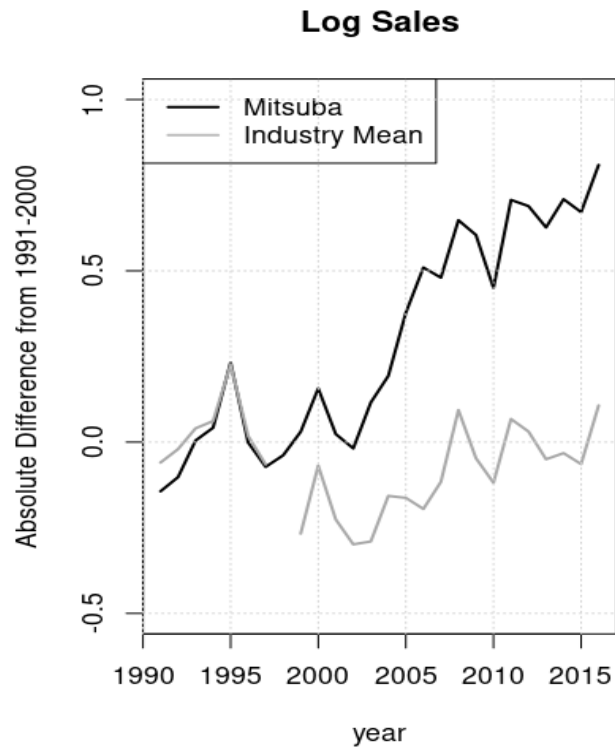
Grow up or get out



The more dynamic vs the better connected in India

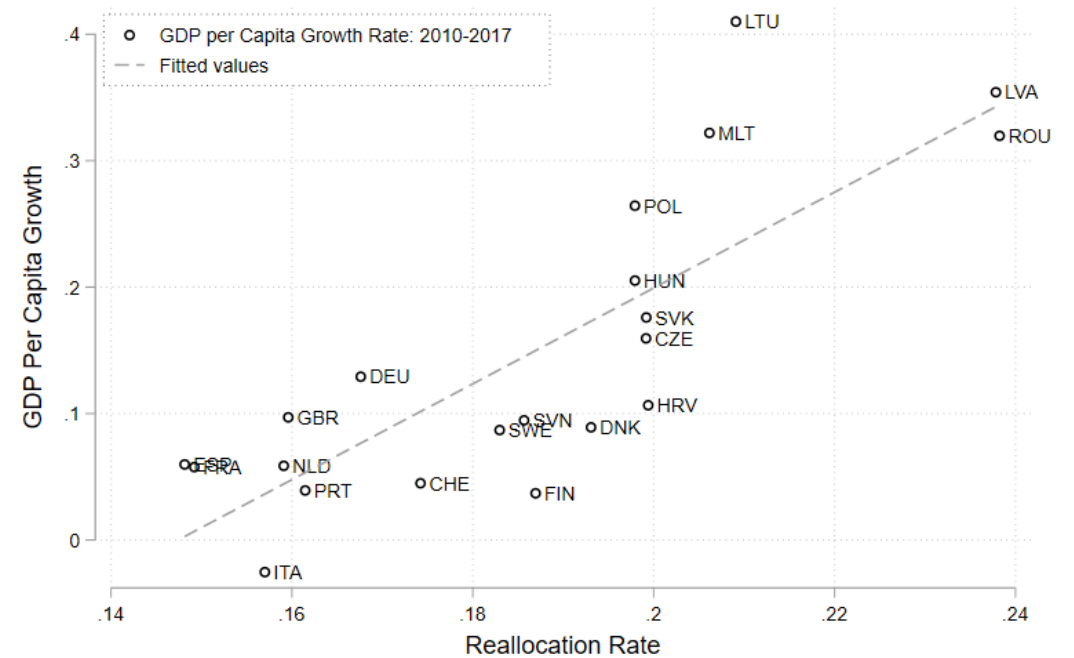
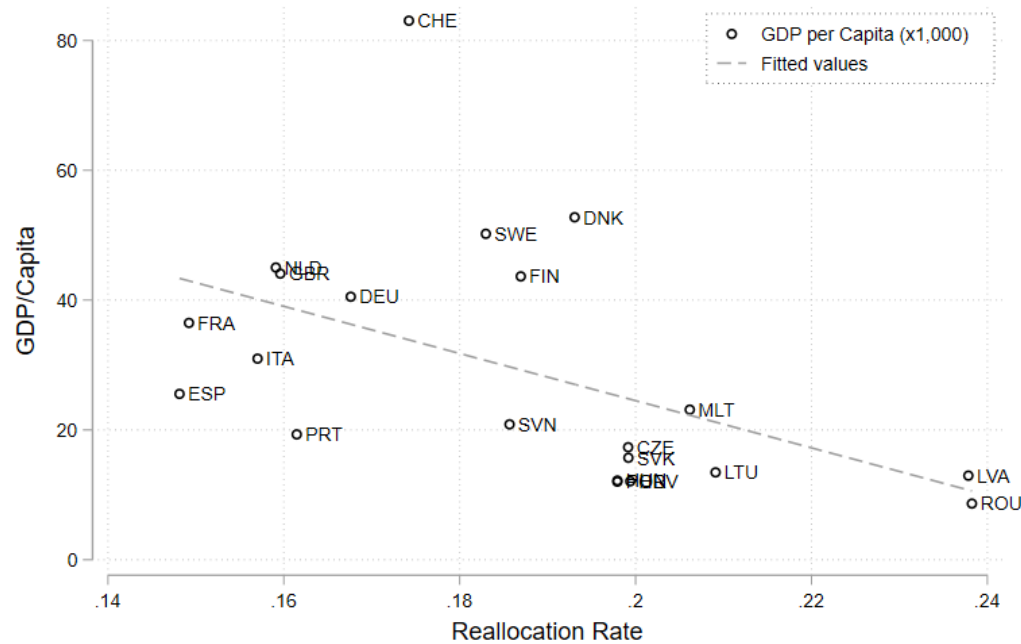


Competition and cartelization in the Japanese auto parts industry



Turnover in EU economies

Worker turnover is associated with accelerated economic growth, and the scope for turnover is higher in countries further away from the frontier



Miranda 2023, background paper for WDR 2024

New Rules for Policymaking

1. Reward value

- Forget about firm size
- The ASEAN model

2. Discipline incumbency

- Not all incumbents are bad
- The Korean model

3. Capitalize on crises

- Quick recoveries are not enough
- The US model



Recurrent themes

(and related resources)

- Learn the latest techniques
 - Becker-Friedman Institute's Growth Program (Somik Lall and Ufuk Akcigit)
- Utilize new data
 - DEC Enterprise Surveys (Jorge Meza and Normal Loayza)
- Capitalize on current crises
 - World Bank Institute in Rome (Gero Carletto and Ivailo Izvorski)

Three Resources

(and contacts)

- B-Ready: Business Readiness Report
 - Contacts: Valeria Perotti, Jorge Meza, and Norman Loayza
- Europe 4.0: Europe's Digital Dilemma
 - Contacts: Anwar Aridi, Gaurav Nayyar, and Wolfgang Fengler
- WDR 2024: Middle-Income Trap
 - Contacts: Joyce Ibrahim, Roberto Fattal-Jaef, and Somik Lall