GRINCOH project has crossed the halfway mark. This issue provides an overview of development patterns of the CEE economies since the start of the transition period, analysing in depth the patterns of structural change and the impact of policies both those formulated at the national level and linked to EU integration and within the EU framework.

Economic development patterns and structural change in the process of transition and EU membership

Four research papers on economic development patterns and structural change in CEECs, as well as a Policy Brief on alternative policy paradigms with regards to EU membership and cohesion policies, have recently been published. Four research papers cover various aspects of the three broader thematic subjects: economic growth and convergence at both country and regional level, structural changes in Central and Eastern European economies (CEECs) and the role of FDI as well as a critical evaluation of economic policies employed in the process of EU accession and EU membership.

The individual papers cover both periods before and after EU accession. Special focus is devoted to the impacts of the recent economic crisis. Perhaps not surprisingly, the authors do not provide an unequivocal assessment of convergence patterns, driving forces of growth and economic policies pursued by the CEECs during the process of transition and EU membership. The diversity of approaches and conclusions reflects both the heterogeneity of countries analysed and the complexity of cohesion processes.

Politecnico di Milano presents MASST 3 Model
Patterns of Structural Change in the New EU Member States
Peter Havlik

This paper analyses the extent and impact of structural changes on aggregate economic growth in CEECs and evaluates the impact of broader sectoral shifts on GDP growth, focusing on the period 1995-2011. By decomposing aggregate GDP/GVA growth and applying a conventional shift and share analysis, the author identifies a distinct North-South pattern of growth and restructuring, while the previous NMS-OMS divisions are becoming less relevant. He finds that, in the NMS-North, manufacturing and trade have fuelled growth while in the NMS-South, much less structural change took place. The analysis of structural changes during the recent crisis reveals similarities between (groups of) NMS and OMS in terms of both growth patterns and responses to the crisis.

FDI, Structural Change and Productivity Growth: Global Supply Chains at Work in Central and Eastern European Countries
Jože Damijan, Črt Kostevc and Matija Rojec

The authors look at the importance of global supply chains for export restructuring and productivity growth in CEECs during the period 1995-2007. By using industry-level data and accounting for technology intensity, they show that FDI has significantly contributed to export restructuring while, at the same time, the effects of FDI were heterogeneous across countries. While more advanced core CEECs succeeded in boosting exports in higher-end technology industries, the export specialisation of non-core CEECs is stuck in lower-end technology industries. The paper emphasises the key importance of FDI flows, not least for the potential for long-run productivity growth.

Macroeconomic Aspects of Macroeconomic Conditionalities. Growth Factors at Regional and National Levels
Roman Römisch

The author analyses macroeconomic aspects of growth and convergence in the EU and the potential effects of macroeconomic conditionalities implemented in the Multiannual Financial Framework 2014-2020. He applies a macroeconomic model linking aggregate supply and aggregate demand via capacity utilisation. The empirical analysis leads him to the conclusion that too tight application of fiscal rules might harm the less prosperous EU countries and slow down the growth and convergence processes. The paper suggests that in order to have growth and stability, the macroeconomic conditionalities should ideally be amended by a coordinated growth initiative focusing on private investment.

Policy Brief on Development Patterns of Central and Eastern European Countries
Leon Podkaminer

The author evaluates the development patterns in the CEECs during the transition period and following EU accession. These patterns were determined by the policies of the Washington Consensus and the requirements of EU membership. His assessment turns out to be more than critical: With the benefit of hindsight, the performance of the so-called ‘integrated growth model’ has been disappointing. After some growth acceleration prior to EU accession, which was preceded by deep transitional recessions, growth in the CEECs collapsed in 2009 and slowed down to unimpressive levels thereafter. Current growth rates converge to those prevailing in the ‘old’ EU. Such speed of convergence does not promise a rapid catching-up in income-level terms. Whatever progress made in the CEECs, it was achieved at a high cost in terms of unemployment, rising income (and social) polarisation – the opposite of cohesion. All this feeds political radicalism which the author fears is likely to explode sooner or later. The economic policy-making in the EU still boils down to the adherence to the original spirit of the Maastricht Treaty. The policy brief calls for a more radical overhaul of the basic paradigms of EU economic policy-making.
A tool for simulating scenarios: the MASST3 model

Roberta Capello, Ugo Fratesi, Andrea Caragliu, Giovanni Perucca

The Polimi team coordinates the efforts of GRINCOH partners aimed at providing a prospective analysis based on different assumptions of strategies that CEE countries can implement to address the main global challenges and oriented towards future policy options, and in particular Cohesion policy options, with scenarios up to 2020. This will in turn allow GRINCOH to derive policy recommendations in light of the main results and lessons learnt from the past, based on the analysis developed within the project.

Methodologically, the prospective analysis will be based on both a qualitative and a quantitative approach, the latter using a macroeconometric regional growth model called MASST (macroeconomic, social, sectoral and territorial model), capable of producing quantitative foresights on GDP, service employment, industrial employment and population growth at regional level.

The Polimi team has been focusing its efforts in the creation of a third generation of the MASST model. The new generation of the MASST model, expressly designed for the GRINCOH project, aims at encompassing several improvements needed for better modeling regional growth and cohesion policies in a more thorough structure. These changes include the modeling of:

• Public expenditure growth rates;
• Urban performance (population), in search for an equilibrium city size;
• Innovation patterns at regional level.

Figure 1. Regional GDP in 2030 in the simulated baseline scenario.
Besides, the MASST3 model also models the current economic/financial crisis’ effects on regional growth.

These additions enrich the logical structure of the model, which has been thus fully prepared for running the simulations needed to define the results of the scenarios for the GRINCOH project.

The MASST3 model now benefits from the availability of a complete panel data set covering the years 1990-2010 for the national sub-model, and an unbalanced panel for the regional sub-model, covering the years 1995-2009 (with gaps due to data availability constraints). The structural relations among the variables have also been tested and the ensuing parameters have been used to formalize the economic model (programmed in an econometric software) needed to perform the simulation stage.

Finally, in order to test the model resilience, the Polimi team has set up a baseline scenario based on the assumption of a continuation of the ongoing trends in the economic elements used as explanatory variables in the model.

The model is now ready to operate and use the inputs from other research teams in the project to simulate over the period 2012-2030 the patterns of growth of several different economic variables, including GDP, population, and employment (by major industries).

As a first exercise, a baseline scenario, based on extrapolating the current trends in the main variables, has been simulated with the MASST3 model. The result for the 2030 levels of regional GDP stemming from the baseline scenario is mapped in Figure 1 above.

In terms of the GRINCOH project, this first simulation yields extremely rich results. After a two decades-long process of convergence, if the current EU policies and the general context conditions will not deviate from their current trends, such process will definitely slow down. GDP growth rates will converge across Eastern and Western areas, and, again, ceteris paribus, such new generalized growth rate will be significantly lower than in the previous twenty years.

Besides, the current financial crisis will arguably have long-lasting impacts on the future economic performance of EU regions. In CEECs, this will in particular affect those countries being most hardly affected by the crisis in terms of employment rates (viz. the Baltic countries), as well as those being involved in the sovereign debt crisis (namely, Romania, Slovenia, and Hungary). On the contrary, other countries which either proved to be still success stories, the crisis notwithstanding (Poland), or else have been less affected in terms of lower employment and GDP growth (Czech Republic and Slovakia), will maintain a relative advantage, although overall economic performance will dramatically slow down.

This tentative simulation needs fine-tuning in terms of future cohesion and crisis scenarios specifically targeting the structural characteristics of CEECs and explicitly incorporating the findings of the other WPs within the GRINCOH project. Yet, even the first empirical findings suggest the need for a major restructuring of the EU governance, in particular in the way structural funds are conceived, target regions identified, and ex-post evaluation carried out.