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SPECIAL REPORT: LIFE IN TRANSITION 2017

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FROM THE EDITOR

ANDREW WROBEL
Editor-in-chief
Emerging Europe

For us, emerging Europe is a region that comprises 23 countries — some of them belonging to the European Union, some believing they will join the Bloc soon and still others having chosen the Eurasian Economic Union. Are they New Europe, New Eastern Europe, Eastern Europe, Central and Eastern Europe or maybe emerging Europe? Is it something else again?

"Back in the 'good old' Cold War days, defining Eastern Europe was easy. It was made up of all those losers who were on the wrong side of the Iron Curtain. Eastern Europe had those 'backward' communist countries, which were frozen in the Stone Age," Francis Tapon writes in his book *The Hidden Europe: What Eastern Europeans Can Teach Us*.

"Whether Eastern Europeans like it or not, the communist experience is still in their collective memory. (…) It's part of who they are. The legacy of slavery can still be felt in the southern regions of the US, even though slavery ended 150 years ago. Communism in contrast, ended [only] 25 years ago," Tapon continues.

Emerging Europe has already 'emerged' for the most and it's a transition to be proud of

But is this legacy something the emerging Europe countries should be ashamed of? On the contrary, I believe. The economies started their transition at the beginning of the 1990s and most of them can rightly say that they are no longer emerging markets. Slovenia and the Czech Republic, for example, have been referred to as developed economies for some time now and have a GDP per capita that is higher than in some of the older EU member states. What others have been building since WWII these countries have achieved within a quarter of a century.

But it's not only that — the decades of communism have also helped create a large pool of hard-working talent. Years of hardship have taught them creativity, entrepreneurship and persistence, all of which are highly appreciated, not only in the region but also across the Old Continent and beyond. Aren't these things the people of emerging Europe should be proud of?

In this *Life in Transition* special report, which is released during the EBRD 2017 Annual Meeting and Business Forum in Cyprus, we discuss the transition process in emerging Europe as well as in the EBRD region, which covers 36 countries. We look at key elements of a successful transition, the process in various areas, the advantages the region has, as well as the challenges it is facing. We also look at the future of the region, as well as of the European Union and all of Europe.

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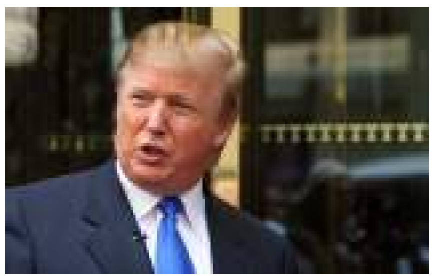

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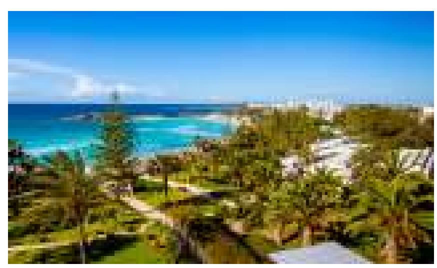

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Written by
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Globalisation needs to work, not only for the few but for the most and in demonstrable ways

Building a green economy is a new trend, now, for every country. But still, many countries are concerned about environmental limitations that can slow down the economic growth.

The emerging Europe countries are now entering a period of slower growth. Despite the fact that the income gap with Western Europe countries has become narrower, not everyone seems to have shared this prosperity. Enhanced policy structures and supportive reforms have helped these countries in the last decades, but nowadays the financial crisis is affecting these markets badly.

Competitiveness anew

The key factor to close the still existing gap is surely the level of competitiveness, which has been recently redefined.

"In an environment of rapid and unpredictable innovation, competitiveness is synonymous WITH flexibility and adaptability. Finding ways of acquiring and keeping a competitive edge ensures access to markets and global outreach," says Maria Demertzis, Deputy Director at Bruegel.

"Inevitably, competitiveness is tightly linked to the ability to deliver price-to-quality. That is not new. What is new in my view is the way of exploring innovative and previously un-thought of ways. A good example is the ability to explore connectivity, like in a sharing economy," she adds.

Cameron Hepburn, Director of Economics of Sustainability Programme at the Institute for New Economic Thinking at the Oxford Martin School, says trust in government and political institutions is vital for all sorts of reasons, and maintaining that trust is arguably an increasing challenge for many countries, including some of the most wealthy. "Sustainable development is very difficult without such trust, so this is a serious issue", he continues referring to the importance a green growth has acquired today."

We are all aware that the core of social capital is building trust between societies and governments.

"It is what we claim more and more", former Polish Minister of Finance, Professor Grzegorz Kołodko, tells *Emerging Europe*. "In 2017, Polish social capital is weaker than one decade ago. The most important thing nowadays is to be competitive and everyone is afraid that someone else can cheat. In this way there is a lack of trust in building partnerships because businessme are afraid."

Regaining trust

"There is only one way to restore or gain trust and that is to earn it. To do that, globalisation needs to work, not only for the few but for the most and in demonstrable ways. Globalisation does not need to eliminate inequalities, but it does need to distribute benefits in ways that are fairer," Breugel's Ms Demertzis adds.

"This lack of trust is weakening stability. There is an atmosphere of suspicion and illusion and this plays an important role on the long term orientation of the business sector. If people trust politics, if people trust management, it is always better. You cannot trust management in such an atmosphere. We need to accept the risk; the risk to expand, to invest money without guarantees but still while expecting some things to be solid and predictable," Professor Kołodko continues.

So what is the right political response? Anders Åslund, resident senior fellow in the Dinu Patriciu Eurasia Centre at the Atlantic Council, says that what matters are not specific policies that governments pursue but how a government can pursue policies that are adequate to the situation of the country. He gives Latvia's Prime Minister Valdis Dombrovskis as an example.

"He was re-elected twice after GDP had fallen 24 per cent during his tenure. He laid off one third of the civil servants and cut public wages by an average of 28 per cent. It is important that belt-tightening applies to the elite and not only to the general public. Justice and fairness need to be maintained," says Mr Aslund and referring to banks, he adds that "banks need to be properly capitalised and regulated so that bad debts are shown and written down. Bank ownership needs to be transparent."

It is not all about transparency. Banks need to be more digitalised, considering that young people are more used to digitalisation and can avail themselves of the benefits of financial inclusion. When asked about the recent surveys of happiness, where there are big differences between western economies being less happy and transition ones being more happy, Mr Isfandyar Zaman Kha, Financial and Private Sector Development Sector Leader for European Member States, explains the concept through a lens of behavioural economics: "When those in transition economies see the developed world in a sort of economic crisis, their own circumstances look less worse and thus, as a consequence, they respond by saying they feel happier."

Grow green

Building a green economy is a new trend, now, for every country. But still, many countries are concerned about these environmental limitations that can slow down the economic growth. For Ms Demertzis, this is sadly true but just in the short term because in the long run they ensure that we can sustain growth. "This is a typical example of how short-term benefits can jeopardise long term and sustainable objectives. However, since the environment is shared by all, it is necessary to manage it collectively and comprehensively," she says.

Mr Hepburn also underlines that many great minds have sought to address the question of whether there are environmental limitations to growth over recent centuries with detailed, focussed and empirical works.

"There is no firm evidence yet that protecting the environment needs to limit growth. On the contrary, the economic transformation involved in moving to a net-zero emissions economy will require a great deal of capital investment, and may even increase measured growth in GDP (if not welfare) in the short term. As another example, once renewable energy is cheaper than fossil fuel-based energy, and is widely available, economic activity is likely to get a boost," he says.

Obstacles to financial inclusion

The economic gap is closing and so too are the happiness and the gender gaps. According to the World Bank, in the majority of the most developed CEE countries the gender gap as it relates to basic financial inclusion is negligible.

Isfandyar Zaman Khan, Programme Leader for European Member States, says that in Ukraine for example, 52 per cent of females own a current account compared to 54 per cent of males.

"The situation is slightly different in Romania, where a gap still exists, with 65 per cent of males owning a bank account while the percentage of females stands at 57 per cent. However, there is not much difference in transition countries that have liberated economies. At least if we talk only about access to bank accounts. If we refer to more sophisticated financial services, such as the number of companies owned by women, then the situation is different. But we are going beyond the basic financial inclusion," he tells *Emerging Europe*.

When we refer to financial inclusion, Mr Zaman Khan explains that at one level it is all about the access to financial services and the access to opening accounts. "Thanks to surveys conducted globally, we know that there are five barriers indicated as such: costs, documentation, distance, trust and religion. Trust is the most affective one, since some people lack trust in the banking sector. Romania is a very good example, since 12 per cent reported costs and trust as a barrier and just three per cent reported it was documentation. Then there is Hungary, where just one per cent pointed out documentation as a barrier, while costs and trust are reported to be respectively 15 per cent and 11 per cent. Any government's primary role is to guarantee consumers' protection and thus alleviate the trust barrier. People cannot exercise their right as consumers if protection is low," he says.

War of the genders

However, when it comes to work inclusion in the field of green economics, the situation is much more different. Lots of women do not have access to those professions, mostly because the education system does not make them feel that it is a remunerative profession.

According to Professor Bipasha Baruah, Professor and Canada Research Chair at Western University, there are four major reasons for women's underrepresentation in the global renewable energy (RE) workforce.

"Firstly, there is systemic misperception and devaluation of women's technical abilities. Women in technical fields are deemed less competent than men even when they are more highly qualified than their male peers. Secondly, women are underrepresented in STEM fields (science, technology, engineering and mathematics) almost everywhere in the world, and employment in the most well-paid jobs in RE, namely, construction, installation, engineering and architecture tend to require STEM training. Thirdly, public policies and corporate policies, to enable equity in training and employment in RE, are either very weak or absent in many contexts. Finally, the persistence of patriarchal social norms and assumptions about breadwinning and caregiving make it difficult for women to assert themselves on a par with men in these fields," she explains.

Ms Baruah adds that women can gain optimal traction from RE initiatives only within the context of wider socially progressive policies, as well as more transformative shifts in societal attitudes about gender roles. "This is as true for developing countries and emerging economies as it is for industrialised nations. Simply creating opportunities for training and employment in new fields and suggesting that women are not unwelcome in them is not enough," Ms Baruah concludes.

She made a comparison study of the percentage of female engineers in the USSR. In the 1980s nearly 60 per cent of engineers were women while in 1998 the figure had decreased to 43.3 percent and in 2002, it was just 40.9 percent.

"I use the Russian example not to advocate a return to Soviet-style central planning, but rather to emphasise that state initiatives aimed at improving representation and removing barriers for career advancement for women in engineering and policy-making can be effective. They can benefit the RE sector in industrialised, emerging and developing economies. Such as what is happening in the Baltic nations of Estonia, Latvia and Lithuania, where female professional and technical workers still outnumber men two to one," she explains.

Step by step

There is no need for a shock therapy to take emerging countries to a positive transition process. As Professor Kołodko says, we should take gradual steps to reach this goal.

"The situation is more different today than in earlier times. Today, it is a big challenge, more in CEE countries than in post-soviet republics. In countries such as Slovenia, Slovakia, Poland and Hungary, we should be concerned about inequality and the rise of nationalism. It is more urgent for these countries than, for example, other emerging markets such as South America. Of course there is the other side of the coin, considering that these transfers are mostly supposed to be for families with more than one child or with disabled ones; sometimes they are just getting a salary without doing anything and enjoying life only because they have more children," the Professor adds.

"Inequality of opportunity is sizeable and it matters. In particular, we show that support for markets and democracy is higher in those transition countries where inequality of opportunity is lower. We also show that it is the inequality of opportunity rather than income inequality that matters for reform support. So we are also formulating policy responses such as fighting corruption, enforcing competition policies, promoting access to education and healthcare, supporting mobility and financial inclusion," Sergei Guriev, chief economist at the European Bank for Reconstruction and Development (EBRD) tells *Emerging Europe*.

Education and, again, education

However, Professor Kołodko and EBRD's Mr Guriev highlight the education system as one of the pillar for transition economies.

"The long term challenge, the most important one, is to invest in human capital and education. It has been proved that the better the education is and the more money is spent in education and training, the faster the economic growth," says Professor Kołodko.

"Our analysis shows that education indeed matters for income, well-being and career opportunities for children. However, in some countries the best-educated citizens work outside of their home countries. Their well-being is higher while the impact of education on the economy is less pronounced. Countries should invest in promoting entrepreneurship and investment in knowledge-based industries which provide jobs for the educated – as such sectors have substantial positive spill over for local economies," Mr Guriev adds.

Written by
ANDREW WROBEL

Published on April 25, 2017

Scan the QR code below to watch the entire video interview with Sir Suma Chakrabarti.

Sir Suma Chakrabarti (photos by Dermot Doorly)

Sir Suma Chakrabarti: the opportunities of challenge

"We need to really help the undeveloped regions in all our countries of operation."

"It's nearly 30 years since the fall of the Berlin Wall and I think there's been outstanding progress," says Sir Suma Chakrabarti, President of the European Bank for Reconstruction and Development (EBRD), in a video interview with *Emerging Europe*.

"You can see lots of areas of progress but we also have to recognise there's still a huge amount of work to do and if you look at the transition process, it was undoubtedly painful in some ways, [not only] socially, economically, but also physically. Of course, there's a huge agenda still in terms of trying to make sure that we have an inclusive transition going forward."

Sir Suma admits that not everybody has benefited equally and this remains a major economic – and also political and social – challenge that needs to be addressed urgently.

"But overall, without a doubt, the positives outweigh the negatives… although there is still a huge job ahead," he says.

The President also believes that the European Bank for Reconstruction and Development has played a key role in the transition process in the region over the last 26 years.

"One easy measure that people always use is the amount of investment and the number of the projects. It's €117 billion, or more in fact now, in terms of investment, and it's about 4,700 projects. But for me the greatest thing is to actually look at what we call transition impact, [so] I think we have been associated with a real period of success on that basis," the President adds.

In addition to finance, the bank offers policy dialogue, a variety of advisory services and engagement in institutional and legal reforms. The EBRD is now focused on continuing green and inclusive growth.

"In Central and Eastern Europe, we have one of the most energy intensive regions of the world and that is very much a legacy of the Communist era. We need to reduce energy costs in the region very, very quickly and substantially. The EBRD has made a major effort on this; we've been working through what we call a Sustainable Energy Initiative since 2006. We have now set ourselves this target to have 40 per cent of our investments by 2020 being focused on green energy, and we are already at one third of our investments. This agenda marries our desire to be environmentally friendly and to help deal with climate change issues with, at the same time, being very business-like about it," he says.

As far as inclusion is concerned, the EBRD is focused on supporting female entrepreneurs, helping youth into work and supporting less advantaged population groups. Women's access to finance remains a big obstacle in many countries where the bank invests and, together with donor countries and other agencies, the EBRD is working hard to overcome this issue.

"We need to take it further, [so] we need to really help the undeveloped regions in all our countries of operation," Sir Suma adds.

The dynamic political and economic situation in Europe and also around the globe brings about new challenges.

"One of the biggest challenges is the growth agenda. We need to grow faster," says the President.

But where there are challenges, there are always opportunities; and, for the EBRD President, they are everywhere across the regions where the bank invests and operates.

"These societies are rich in skills. The education level in many of these countries is very high compared to many other emerging markets, while labour costs often are still low. We can also see huge investment opportunities. We have nearly 400 projects a year; and that shows the investment opportunities because we're doing projects that commercial banks are still reluctant to do."

In the view of the EBRD, the largest institutional investor across emerging Europe, the future of the Old Continent lies in emerging Europe.

"The Central and Eastern European success story of the last thirty years has shown that contribution – and it will continue to do so in the future. We forecast for this year that Central Eastern Europe will be growing faster than Western Europe, and that's a sign of the potential of Central Eastern Europe. To tap that potential, I think we need to go beyond just thinking of ourselves as part of Europe. The great thing, I think, about many of these countries now, is that they have started seeing themselves in a bigger context. They are trying to tap investment from all over the world; they look at the Gulf, they look at Asia, they look at North America as well as Western Europe; and I think that's a game changer in that region, and that will make it very successful. And if they are successful, Europe as a whole will be successful," Sir Suma concludes.

Sir Suma Chakrabarti (photos by Dermot Doorly)

Emerging Europe makes great strides in improving business regulation for entrepreneurs

SANTIAGO CROCI DOWNES
Acting Manager Doing Business Unit, World Bank

Published on April 21, 2017

Emerging European economies offer a sound business regulatory framework. According to the World Bank Group's Doing Business report, four economies in emerging Europe are in the global top 20 for the ease of doing business rankings. They are the former Yugoslav Republic of Macedonia (ranked tenth out of 190 economies), Estonia (12), Latvia (14) and Georgia (16).

Moreover, the region has, in general, made great strides to improve the business climate for local firms. In the past five years alone all the economies in the region recorded reforms that benefitted entrepreneurs (see Figure 1). This is an important feat as countries with business-friendly regulations tend to attract more foreign investment and have lower levels of income inequality.

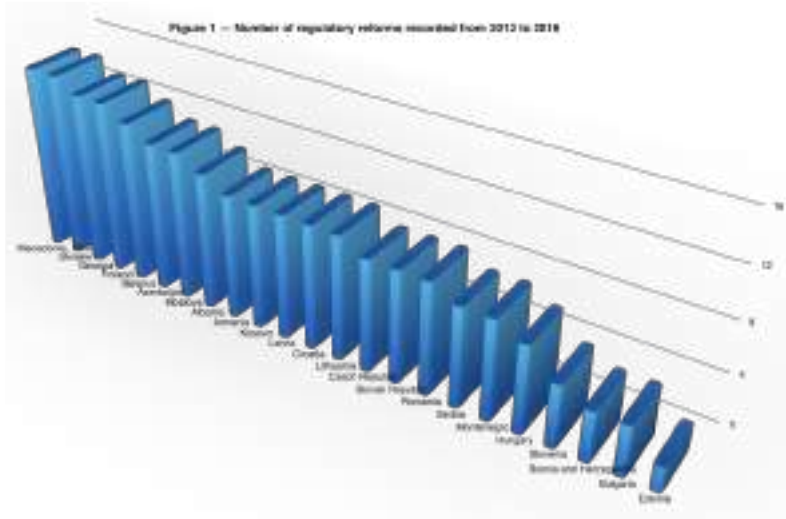
Georgia, Serbia and Belarus were among the ten economies that were highlighted in 2016, for making the biggest improvements in their business regulations. Owing to streamlined processes and time limits, Serbia reduced the time needed to start a business, obtain a building permit and transfer property. Belarus improved its business climate by – among other things – establishing a one-stop shop at the electricity supplier and by providing consumer credit scores to banks and financial institutions. Georgia implemented five reforms, such as easing export and import documentary compliance through an improved electronic processing system. It is the fourth time in 12 years that Georgia has joined the list of top improvers; during this period, output per capita in the country increased by two thirds and business density more than tripled, as shown in the World Bank's World Development Indicators database and Entrepreneurship database.

Looking back over the past five years, over half of the economies in the emerging Europe region undertook ten or more reforms, in the areas measured by Doing Business — from easing foreign trade to improving access to credit. In contrast, on a global level, less than a quarter of the economies achieved this milestone. While reform agendas have differed from one country to another, the areas that have seen the most improvement, in emerging Europe in recent years, are taxation and business incorporation (see Figure 2).

Properly developed and effective taxation are crucial for a well-functioning society. Overly complicated tax systems are associated with high levels of tax evasion, large informal sectors, more corruption and less investment. Therefore, it is encouraging to see that, from 2012 to 2016, 20 of the 23 economies in emerging Europe implemented reforms to make paying taxes easier, and reduced the time to comply with tax obligations by nearly ten per cent.

Albania was one such economy that carried out a slew of initiatives. In 2013, it allowed corporate income tax to be paid quarterly. In 2016, it introduced an online system for filing and paying taxes. As a result, the time to pay taxes was markedly improved for local firms, from 357 hours in 2012, to 261 hours on average in 2016. Thanks to this, today, businesses in Tirana have more time to dedicate to their operations.

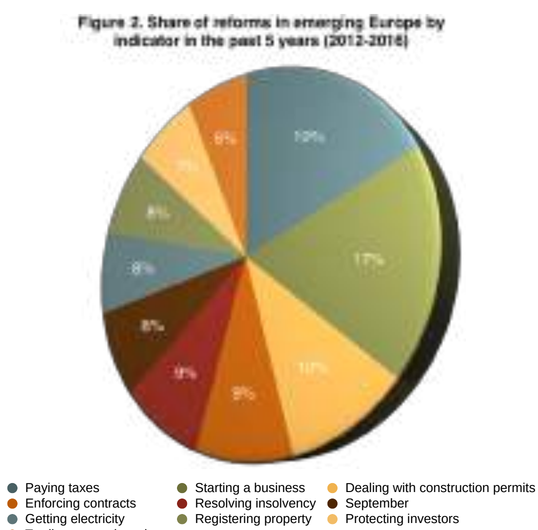
Skopje in Macedonia



Throughout emerging Europe, considerable improvements have also been recorded in the area of Starting a Business. This is a strategic area of focus as an easier start-up process has numerous benefits, such as higher levels of firm formalisation, economic growth and greater profits. Several countries in emerging Europe now set the best practices, when it comes to business incorporation. The former Yugoslav Republic of Macedonia, Georgia, Azerbaijan and Armenia are among the top ten countries, worldwide, where it is easiest to launch a business. Start-ups in these countries can incorporate and begin operations in less than five days, compared to a global average of 21. Moreover, throughout the region, budding entrepreneurs need not worry about gender barriers — unlike in some economies, worldwide, where women still need to jump additional hurdles compared to men.

While emerging Europe is competitive across several areas of business regulation, there remains room for improvement – especially with regards to the construction permitting process or obtaining a new electricity connection. Indeed, it takes an average of 116 days to get connected to the grid in emerging Europe compared to 76 days in OECD high-income economies. So, while emerging Europe offers a robust regulatory regime to firms, further improvements can be made to benefit local firms and improve national competitiveness.

The editorial was co-authored by Jean Arlet, Operations Analyst, Doing Business Unit, World Bank



The fight against corruption in Europe's emerging economies

FINN HEINRICH
Director of Research Transparency International

Published on April 21, 2017

Demonstrations in Bucharest in February 2017

In some countries, when their leaders have egregiously over-stepped their authority to shield themselves from accountability, citizens have taken to the streets with some success.

Corruption and impunity ignite public protest. Anger against corruption sparked the Arab Spring, it also forced Ukraine's former president Victor Yanukovych to flee and more recently brought tens of thousands onto the streets of Bucharest in Romania. Citizens want leaders who work in their interests. However, even when the message is delivered en masse the day-to-day task of fighting corruption is never easy.

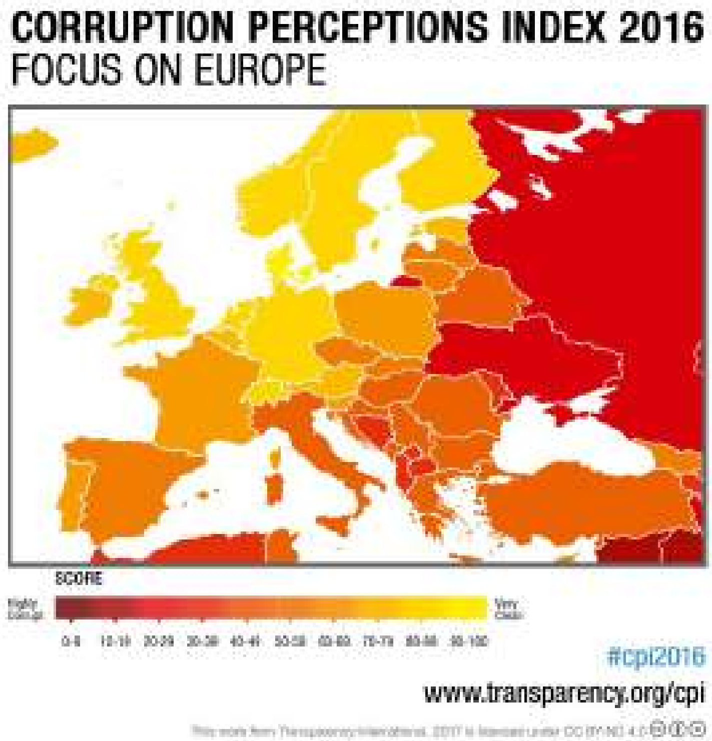
The successes and failures of the emerging European economies offer some reasons for hope but also reveal too many cases where powerful elites have co-opted the levers of power. This is true from the Balkans via the Bosporus to the Baltic. Strong institutions – the core of any anti-corruption programme — do not emerge fully-formed overnight, particularly in places that have lived through decades of single-party rule. Two decades on, there is still much work to be done and progress is under threat.

Successes and failures

Although some emerging economies have been more successful than others in building public institutions and empowering independent agencies that are fit for the purpose of taking on the corrupt, in many countries, such accountability systems have not yet emerged. In addition, solid independent media and a strong civil society are far from well-established and, with the lurch towards a new era of populism and authoritarianism taking hold, they may never get the chance.

The voices that speak truth to power too often find themselves behind bars. Russia and Turkey come to mind immediately.

The will was there in the beginning. Since the early 1990s, and with the ever-increasing prospect of enlarging the European Union that followed the collapse of the Soviet bloc, many of the post-Cold War emerging economies did take steps to develop and strengthen their anti-corruption systems. However, in a context of economic turmoil and persistent social fragmentation, the conditions for favouritism and an uneven application of the law still thrive. The end result is a situation where laws and anti-corruption policies, while good on paper, are selectively enforced and corruption in public office goes largely unsanctioned.



Lack of a serious approach

A consistent feature, across the emerging economies in Europe, and one which is blocking improvements in spite of better legislation is the phenomenon of state capture – whereby powerful executive branches and political parties dominate all the other institutions. This, coupled with a lack of cooperation and coordination among state actors, has undermined the ability of supposedly independent judicial, law enforcement and anti-corruption bodies to provide a meaningful oversight of government activities and to investigate and prosecute corruption effectively.

Emerging institutions are vulnerable to state capture, as has been the case in Hungary, for example, within the democratic context. Politicians with an authoritarian bent are quick to use corruption, which they link to social inequality, as a reason for insisting on more powers. The problem is that they usually have no intention of tackling corruption seriously: the track record of populist leaders fighting corruption is dismal because the concentration of power itself has never led to increased oversight or more fairness.

In some countries, when their leaders have egregiously over-stepped their authority to shield themselves from accountability, citizens have taken to the streets with some success. We saw that in Romania recently. However, there are also cases in Albania, Bosnia and Herzegovina and Serbia where powerful people have gotten off the hook for corruption because of their connections and a lack of will to apply the law without favouritism. Indictments are often poorly written and inadequately investigated and complex corruption cases are poorly understood by prosecutors and judges. We have seen this in Albania and Kosovo, also.

Judicial independence

Despite this bleak picture, there have been some important attempts to strengthen the independence of institutions, particularly the judiciary in some countries, demonstrating that, where the political will exists, reform is possible. There is a common understanding of what has to be done to combat corruption.

Montenegro, for example, is planning to introduce the principle of the immovability of judges. It has placed limits on the political influence over the process of appointing judges and has improved cooperation between the prosecution and the police by providing the grounds for the establishment of a special investigation team, when it is deemed necessary. We wait to see this in practice. Kosovo has given judicial and prosecutorial councils greater discretion in drafting and proposing their budgets and the judiciary has a more prominent role in appointing members to the judicial council, but it remains to be seen how these will work. The Georgian judiciary is showing signs of becoming more impartial in its decisions and more active in holding the government to account.

However, in the cases of Azerbaijan and Ukraine, corruption prosecutions tend to be either politically motivated or to target petty offences and those who oppose the government. In Armenia, the number of corruption prosecutions is limited. Moldova's much needed judicial reforms are lagging behind and are perceived to be highly politicised.

Perceptions of corruption: no change

There were few changes in Europe and Central Asia in the Corruption Perceptions Index 2016, which given the problems mentioned above is not a good sign. High-profile scandals associated with corruption, misuse of public funds or unethical behaviour by politicians, in recent years, has contributed to public discontent and mistrust of the political system.

The Ukraine's minor improvement this year probably benefitted from the launch of the e-declaration system that allows Ukrainians to see the assets of politicians and senior civil servants, including those of the president. Still, important cases of Grand Corruption against former president Yanukovych and his cronies are currently stalled because of systemic problems in the judicial system.

As stated above, the capture of political decision-making remains one of the most pervasive and widespread forms of political corruption across emerging economies and the rise of populism will do nothing to stop this. Companies, networks and individuals unduly influence laws and institutions to shape policies, and the legal environment and the wider economy to their own interests. That is why it is so important for civil society to be strengthened and for the media to remain free and independent. The promise of a democracy that delivers strong institutions — something that was considered a given in the heady days of the 1990s – is far from certain, though it can be achieved as long as citizens do act in defence of democratic principles and hold their leaders accountable.

Sergei Guriev: emerging Europe countries – happy alike and unhappy in their own ways

Written by

ANDREW WROBEL

Published on
April 21, 2017

We expect a negative impact of Brexit on the UK economy, and also on the EU countries in the EBRD region.

Inclusion and green growth are aspects that some emerging Europe countries have not really started taking seriously enough, so institutions like ours need to further increase support and to invest more in both aspects, says **Sergei Guriev, chief economist at the European Bank for Reconstruction and Development (EBRD)**. He spoke to Andrew Wrobel about global trends that might have an impact on emerging Europe, the region's prospects for growth and the challenges it is facing.

Which global trends do you think have the largest impact on emerging Europe and the broader EBRD region?

Well, there is one major global trend, which is the slowdown in global growth and, some even say, the secular stagnation; that is the fact that the global economy post the 2008 financial crisis is recovering slower than usual after a recession. Of course that affects our countries, because they are looking for advanced economies as a source of investment and export destination. So, the slowdown in the US, and in Europe, affects our countries of operations and we also see slower growth in them. There is also another side to the coin and that is China, which is also slowing. That affects other parts of our region, mostly the countries further east.

The second major trend that is related to the political economy is the debate about globalisation or rather to what extent globalisation has been inclusive or – on the contrary – to what extent it can explain the rise of populism, the slowdown in global trade growth, anti-reform policies, anti-market policies and protectionism etc.

Even if we look at countries that are still committed to globalisation – because many of our emerging Europe countries are small countries that had benefited from globalisation and cannot grow without globalisation – even those countries are hit by the rise of populism and protectionism. This makes it harder for them to export; it is harder to track investment and, therefore, harder for them to grow and develop.

Brexit and Trump's presidency result from that second trend too. How can these affect the region?

First of all, naturally we respect the choice of the American and British people. However, let's take these one by one. In terms of Trump's policies, it is still not clear what is going to happen. Some plans have already been scrapped. Therefore, the markets are already starting to ask questions: to what extent the expectations of tax cuts and infrastructure stimulus will actually go through? If they do go through, we should expect a stronger dollar and outflow of funds from emerging markets towards the United States, where interest rates will be increasing and, in that sense, there is also a direct impact on our economies.

Overall, of course, we would be happy to see some smart deregulation. Of course, some of the regulations that have been introduced in recent years have been extremely important for financial stability and preventing future crises. We hope this macroprudential regulation will stay in place. However, there are many regulatory barriers that could be removed and this would promote growth in the US and therefore in the global economy. So, where there are good policies they should be supported.

As for Brexit, it also is a sovereign choice, which was made on non-economic grounds. The economic arguments for Brexit are very weak. We expect a negative impact on the UK economy, and also on the EU countries in the EBRD region. A slowdown in the UK and a slowdown in Western Europe would also affect emerging Europe, so we are concerned. This is going to be an additional cost for our countries. In addition, there is also a lot of uncertainty about exactly how exactly Brexit will be administered.

So what are the prospects of growth for our countries?

We will publish our new biannual forecast during our annual meeting in May. The latest forecast which was published in November 2016, foresees growth in 2017, in general, of 2.5 per cent. Of course we are constantly monitoring developments very carefully; at the moment, we do not expect substantial changes to the November forecast.

In general, we see countries in emerging Europe growing at

Sergei Guriev (courtesy of the EBRD)

two or three per cent. Some will grow faster. We see growth in Greece. We foresee growth in Ukraine. We see Belarus and Russia emerging from their recessions, and these are, of course, welcome developments. Overall, 2017 is going to be the first year in a decade when we will see growth in EBRD's every single country of operation.

I spoke to Professor Leszek Balcerowicz, well-known for implementing the Polish economic transformation programme in the 1990s, about transitioning from a centralised to a market economy. His recipe is to increase the pressure for reforms, to be ready with a package and finally to move with maximum speed. What is yours?

In general, I agree with Professor Balcerowicz. I think it is important to prepare the package of reforms and the communication in a narrative that will increase the pressure for reforms per se. When we say 'a reform package,' we mean reforms that not only promote markets, but also provide social safety nets for those who lose out because of reforms. This is an extremely important lesson that we learned from the transition of the 1990s and 2000s. If you do not have inclusive policies, and if you do not communicate the positive longer-term implications of reforms, you may end up with populist politicians taking over and reversing those reforms.

Today, the debate about Poland is very difficult because opinions are polarised. I think the economy is still doing well even though there are many critics of the government: However, you can also suggest that what has been done in the last 25 years has created such a solid economic basis that any government policy cannot really destroy the strong economic fundamentals.

In principle, the figures are still quite good. Compared to other transition countries, Poland has been a great success, overall. Some people might say that Poland will face difficulties in 2018, when the debt to GDP ratio will reach 55 per cent, which, under Polish legislation, is a trigger for austerity measures.

We promote and support reforms that are sustainable in the long run. In many countries, including the West, increases of the retirement age are inevitable. Of course, this should be done ahead of time so that people have time to prepare, to save and to adjust. I think there is no easy way around it.

There are debates about whether retirement benefits should be paid based on need, rather than based on age. That is a separate debate, and if you think about inclusion, we want to allow people to save for their retirement themselves: If they are in need the government should provide social safety nets.

During the EBRD's annual meeting, we are going to talk about growth and transition and the six elements — competition, governance, green economy, inclusion, resilience and integration. What are the prospects of that in the region? Isn't there too much historical baggage that can somehow be an obstacle to this more sustainable growth?

Inclusion and green growth are two very different issues, and we actually devoted our latest Transition Report to inclusion. The next Transition Report will have a chapter on green growth. Both are very important issues for the region, and there is not enough awareness yet of environmental sustainability. Some countries have not really started taking it more seriously and institutions such as ours need to increase the support for and to invest more in green projects, which we are doing. Currently, about a third of our annual business volume is green. By 2020, this number is expected go up to 40 per cent.

Where inclusion is concerned it will be difficult to formulate the legacy, because for example, while some of our countries have actually been quite egalitarian in terms of their approach to women, we do have gender gaps in pay. We don't have gender gaps in education; women have the same level of education as men. Yet women with the same education earn less than men. I think there is a lot of unfinished business there.

There is also unfinished business in terms of opportunity and access to good education. High quality education is very much correlated with parental background as in the West, especially in the United States. The probability of your going to college is much higher if your parents went to college.

You said there isn't much awareness about these elements of growth. How can that be changed?

I think that people underestimate the importance of public debate and the media. I believe 2016 showed that these matter. The integrity of public debate has a clear impact on political outcomes and therefore on economic policies.

Unfortunately, in many of our countries media freedom is not unconstrained. I think awareness comes from public debate, political competition and media freedom. We understand multi-party democracy is something that includes high quality public debate, media freedom, political competition and civil society.

We were talking about inclusion. Professor Balcerowicz says that countries which have introduced economic market reforms have improved their social and economic situation far more than countries which have not done it. In the Transition Report you talk about height as an important parameter.

Yes, we used it to measure the hardship of the early transition years. Basically, if we look at income data, we see that the first few years of transition were extremely painful for the vast majority of population. In some countries, the incomes of 80 or 90 percent of the population fell. However, income is an imperfect measure because pre-transition incomes did not reflect the living standards fully.

That is why we looked at the height of people who were born at that time. Why? It is because, in developing economics, there is an established case for a relationship between height and the quality of life in the first couple of years of your life. If you are born into a family which is poor, and cannot assure that you have a high quality of life, then you are likely to grow up shorter. Now, this is the time when we can actually see the children of transition growing up to adult height and we can see that on average kids born during the beginning of the reform are one centimetre shorter than kids born before and after.

What are the other elements that show that some growth has been achieved, or that the social and economic situation has improved?

Now, we can actually trust income data that shows convergence. We can look at self-reported life satisfaction, which is also becoming normal in a sense, that is, if you take a person from our countries and compare them to a person from Western Europe, or non-post-communist countries which have the same income, then you see that these people report the same levels of life satisfaction.

Another issue which is probably related to the issue of height are the rates of mortality and life expectancy. In the 1990s some of our countries, especially Russia and Ukraine, experienced a decline in life expectancy and an increase in middle-aged mortality. These are very severe challenges which have been overcome now. Life expectancy has been growing in those countries and mortality has been declining. Now, this is a challenge that the United States is facing, and we are seeing a wide range of the middle-aged population suffering and experiencing higher mortality rates and lower life expectancy.

I would like to briefly touch on the ease of doing business across emerging Europe. If we look at the Doing Business ranking, we see that a lot of our countries have climbed up the ladder but that does not always seem to be reflected in the ease of doing business. Is it easy to do business in emerging Europe?

I served on the panel that revised the methodology of the Doing Business Survey in 2012 and 2013 at the request of the President of the World Bank, so I share some responsibility for the current methodology. I think it is a very cost-efficient and concise methodology and that we should understand what it measures and what it does not measure. It measures specific aspects, which are correlated with the ease of doing business but it actually targets certain kinds of businesses and looks at certain aspects of business operations.

The other issue is that people look at this as a rating. If you target improvements based on those ratings — create a task force, for example — you can do quite a lot and that will actually be reflected in tangible improvements in the business climate. Now, will that solve all the problems? No, but it is an extremely successful measurement tool in the sense that it drives a lot of improvements in business regulations around the world and in our region in particular.

Of course, if you move up or down five positions in this ranking that could be a measurement error. It could be noise. If you move up a hundred notches as Georgia did, in the 2000s, it reflects really drastic improvements in the business climate. Yet, in some countries, which actually scored pretty well on those ratings, you still see business people facing major challenges related to harassment by authorities, extortion, or bribes, etc. and which, of course, are not captured by this particular rating

So what are the main challenges that emerging Europe is facing now?

At the EBRD we currently have 36 countries of operation and each country is quite unique. Like Leo Tolstoy wrote in his novel Anna Karenina: "Happy families are all alike; every unhappy family is unhappy in its own way."

If we think about emerging Europe, especially about the western part of our region, and the countries that are on track to becoming European Union members, or already are EU members, the challenges are related to issues which are also common to Western Europe: ageing, a slowdown in technological progress, innovation and knowledge-based industries.

In the eastern part of the region, we have geopolitical risks, problems with governance and corruption, which result in a poorer investment climate and fewer incentives to reform, invest and develop the economies.

As I said, every unhappy country is unhappy in its own way. There is no one size-fits-all solution and that is why, when we think about a country, we try to figure out which aspects of a sustainable market economy are missing and what our country strategies should focus on.

All countries must learn from the transition experience not only those that are lagging behind

IVAN MIKLOŠ
former Minister of Finance and Deputy Prime Minister of Slovakia; in 2004, named the top business reformer by the World Bank's Doing Business report

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Transition reforms are much more of a political challenge and problem than a technical one.

It is now 27 years since the start of post-communist transition. The first complex and comprehensive transition program started on January 1, 1990, in Poland, followed by a similar one in Czechoslovakia, at the beginning of 1991. What are the most important experiences?

Well, a macroeconomic stabilisation and openness of the economy is necessary but not a sufficient precondition for success. Structural and institutional reforms that are based on liberalisation, deregulation, demonopolisation and privatisation, together with sustaining macroeconomic stability are of key importance. Speed and comprehensiveness matter – quicker and broader reforms bring much more positive and visible results. Transition reforms are much more of a political challenge and problem than a technical one. At the very beginning it was unclear which methods and approaches of the transition were working and which weren't.

The most important precondition of the successful transition reforms is leadership, ownership and communication. Leadership means having political leaders with strong vision, will and courage to make reforms, to oppose populist and demagogic politicians and the representatives of vested interests. It means also to take political risks to impose unpopular but necessary measures. Ownership means that leaders and their parties are making reforms because they are convinced that reforms are needed for their country and for a better life for their fellow-citizens, not because of pressure from outside (International Monetary Fund, World Bank, European Union, financial markets).

Successful transition countries such as Estonia, Slovakia or Georgia did even make some reforms (especially in tax area) that were not recommended by the IMF, at the time of their execution, because were considered too radical and risky. Communication means that reformers have to use every possibility and opportunity to explain people what and why they are doing; they have to fight publicly against populists and those who misuse the weak spots in the unreformed system.

A very important role is played by democracy and a strong civil society. Empirical data has confirmed that transition countries with a liberal democracy and a strong civil society are also more successful in making successful reforms, in spite of the changes in governments and political parties in power, that happen relatively often. Illiberal democracies and autocrats are usually also less effective in making reforms and competitiveness; they are more corrupt, less open and, last but not least, people in these countries are poorer and less content.

But other examples have shown that even in advanced transition countries it is not guaranteed that liberal democracy cannot be endangered. European Union membership, as well as the prospect of membership, plays a very important role for imposing and also speeding up the necessary macroeconomic, structural and institutional reforms. The enlargement of the EU also clearly showed that it is a win-win project that is very useful and beneficial, not only for the new but also for the old EU member countries.

The absence of the necessary reforms leads not only to inefficiency and backwardness but also to deeply rooted political distortions that are then very difficult to change. In Ukraine, for example, because of the absence of reforms for more than 20 years, an oligarchic, corrupted and non-functioning economic system was developed. It is much more difficult to change this kind of system than a situation where vested interests are not so deeply rooted and institutions are not so deformed and corrupted.

The business environment is of key importance, especially in countries such as Ukraine where the system is, to some extent, built on a rent seeking principle not a profit seeking one. Rent seeking means the acquisition of rent by misusing economic or/and political power and profit seeking means to create income under the conditions of free and fair competition and on a level playing field. We can say that a significant part of the content of the transition concerns decreasing the conditions for rent seeking behaviour. With this in mind the most important ways to do this are liberalisation, deregulation, demonopolisation and privatisation together with law enforcement and property right protection. What is also very important is proper, independent and professional regulation but only in areas where it is necessary, such as natural monopolies, information asymmetry, antimonopoly policy, negative externalities and conditions of social inclusion.

I agree that the green economy and inclusive economy play important and growing roles in sustainable human development. However, without a functioning and competitive market economy that has a friendly and "profit seeking" business climate, there is no chance to develop an environmentally friendly and inclusive economy and society.

Transition in government and the economy remains vital in CEE

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In reality, all economies are in transition, as the market is a dynamic and fluid series of interactions, with shifting preferences and demands eventually changing structures of production and choices.

As the European Bank for Reconstruction and Development (EBRD) holds its annual meeting in Cyprus, the political and economic landscape across transition economies is perhaps one of the most difficult that the EBRD has faced since the early 1990s. The rise of authoritarian populism, the acceleration of centrifugal forces in Europe, and the emergence of Russia as a source of regional instability have all threatened to unravel some of the hard fought gains seen in Central and Eastern Europe (CEE) and the former Soviet Union (FSU).

The key lesson of transition that recent turmoil has exposed is that the macroeconomic transition in the region was over quickly, but the institutional transition remains incomplete. Without renewed vigour in building the right institutions, and continuing to unravel the institutional structure of communism, these political and economic gains can be reversed. As Ronald Reagan rightly noted, "freedom is never more than one generation away from extinction…it must be fought for, protected, and handed on."

The right definition

While the term "transition" has been criticised, with some preferring to use the term "transformation" to refer to the process of change in the region, transition is in fact an accurate label to the events from 1989 onward.

In reality, all economies are in transition, as the market is a dynamic and fluid series of interactions, with shifting preferences and demands eventually changing structures of production and choices. The intermediaries in this sea of change, those mechanisms which channel the preferences and mediate interactions, are an economy's institutions. Further sub-divided into political, economic, or social institutions (as well as formal and informal), institutions may both constrain behaviour as well as facilitate certain processes.

A common refrain heard in the first decade of transition was that "institutions were neglected" in the rush to capitalism, a facile claim that has been thoroughly disproved. But this early criticism, more of the economics profession than of governments in transition, has a grain of truth in regard to the current state of affairs in the region. Of course, from the vantage point of nearly 30 years on, it is easy to say what should have been done, and what should have been left aside at the onset of transition; as they say, hindsight is always perfect.

But the transition process did not proceed in a vacuum, and it was well-known, simply from the experience of Western economies in the 1970s and 1980s, what worked and what didn't. Hybrid economies, with a nominally free market, but heavy state regulation of product and labour markets, did not deliver positive economic results, while freer ones did. Put another way, there was already knowledge on which institutions were necessary and which were a hindrance.

Unfortunately, due to lack of political will, incomplete political transitions, poor knowledge of voters, and the continued strength of communist parties, many of the requisite political and economic institutions were never allowed to fully develop. Part of this was

due to the misunderstanding of what transition was supposed to achieve: the goal wasn't growth or even the provision of consumer goods, but actually to transform institutions from those that facilitate a planned economy to those that facilitate a market economy.

Focussing on growth

Given that politicians in transition (and their Western advisors) were obsessed with returning to growth quickly, macroeconomic stabilisation became the first step in sequence and comprehensive institutional reforms were shuffled aside. The removal of some of the largest barriers to growth (i.e. price controls and total governmental control of the economy) unleashed productive forces in every economy, with high growth rates due to convergence effects; but without serious institutional reforms, including a much more comprehensive roll back of the state, the growth was not likely to be sustainable.

Ukraine is the poster child for this lack of institutional reform, as it underwent a halting macroeconomic stabilisation but was never able to rip out the plumbing of communism from the state, and thus the economy.

Of course, Ukraine has never had a history of market-facilitating institutions, a tradition which continued into its post-1991 independence. The Ukrainian parliament, elected in 1990, remained in place until 1994, meaning a preponderance of unreconstructed communists was charged with overseeing the changeover from communism to capitalism. After stabilisation in the mid-1990s, the shift to concentrated executive power under President Kuchma meant that crucial institutions, such as property rights, were ignored.

Other institutions, such as trade, were continuously trampled on in favour of the political rents that could accrue, with licenses and quotas instituted, repealed, and re-instituted. Even the Orange Revolution left political institutions with far too much power over the Ukrainian economy, a trend which accelerated exponentially under former President Yanukovych. The post-Maidan government of Petro Poroshenko is finding how difficult it is to reform institutions when they have taken root, and especially when they are able to create rent-seeking opportunities.

Future consequences

None of these points are necessarily new, but the consequences of not changing the apparatus of the state post-communism were in many ways unforeseen. The events of the past five years have brought them into clear view, however, and the importance of the roll back of the state should be apparent in today's populist world. Where countries did not disassemble the extensive administrative controls into the economy, the stage was set for populist or authoritarian leaders to use these controls to their own end.

Without proper protection of property rights, enshrined in law, property everywhere was threatened. Without a vitiation of the power of state to regulate, capricious regulations targeted at political enemies could easily be enacted. And, without the emergence of a series of checks and balances (typified in an independent judiciary), the executive could aggrandise power and further restrict liberty.

Hungary and, to a lesser extent, Poland's experience over the past few years, coupled with the much more standard authoritarian regimes in Belarus, Russia, and Central Asia, show that the institutional challenge for the region remains substantial.

The course for international donors, but more importantly for domestic governments, is to chart out how to be more like Estonia and less like Belarus; how to ensure that property rights are protected and defended; and how to roll back the state from its current vantage point. Only by addressing these points can the populist tide be rendered ineffective. Without the power of the state to close universities or prevent land sales, populists will be powerless to implement their anti-growth policies. This would be an excellent signpost to show that the transformation actually is complete.

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EU membership offers real prospects of social progress gains

The dividing lines between the 'old Europe' of the EU-15 countries and the 'new Europe' of the EU-13 members are blurring.

In recent years, the narrative around the EU has all too often been one of divergence: from the economic shockwaves that led to ongoing speculation about Greece's future in the Eurozone, to the UK's decision to leave the bloc. However, when it comes to measures of social progress, far from divergence, we are seeing a very different story – one of convergence between nations. Analysis by the Social Progress Index offers hope to nation states, of a promising future for the 500 million people living within the EU. Just as importantly, to candidate nations, the prize of EU membership offers the potential for improvements in the social conditions of their citizens.

Last year the Social Progress Imperative launched a new EU regional index. Building on the model of our global Social Progress Index, the EU Index measures the extent to which 272 regions of the EU are delivering social progress, and is focused on the core measures which define our lives: opportunity, basic human needs and well-being.

The findings are counter-intuitive and informative. We see wide divergence in wealth across the EU which masks a surprisingly consistent quality of life. Take Brussels, the capital of Europe – and one of the richest regions of Europe (GDP per capita of €55,600). However, when it is measured on its social progress this economically privileged region scores on a par with Eastern Slovenia, which has a level of GDP per capita less than a third of that of Brussels. When it comes to quality of life across the EU, GDP is not the sole determinant.

We are seeing a general trend in the data related to this: the dividing lines between the 'old Europe' of the EU-15 countries and the 'new Europe' of the EU-13 members are blurring. Far from a two tier Europe, the aggregate social progress across the regions of the new member states, such as Poland, Czech Republic and Slovakia who joined the EU in 2004, is actually comparable with that of the regions of old member states in Southern Europe, including Portugal, Italy and Greece. Specific elements of the regions' social progress offer further clarity. For example, performance on 'well-being' measures – such as basic education, access to information and environmental quality - show only small differences between the EU-15 and EU-13. Some EU-13 regions outperform regions in France, Germany and the UK on these measures. What's more, perhaps surprisingly, EU-13 countries outperform their EU-15 peers on education indicators.

One obvious question is why EU membership can help to drive improvements in social progress? There is a focus, at the heart of the EU, on improving the lives of its citizens, with data as its starting point. As the MEP, Nicola Caputo Member, has said, good data can help translate policy into an action-oriented agenda which advances both social and economic competitiveness in Europe's regions. That's precisely why we have been working so closely with the European policy-makers: so that people at all levels of government – from the

Commission to the local council – can use the SPI's findings as a performance management tool, helping to direct and improve the efficiency and effectiveness of public investment.

However, the picture is far from uniform and whilst EU membership would appear to be a key ingredient for success, it is by no means a panacea. On measures of tolerance, for example, the story for all EU nations — especially the EU-13 — is not nearly so encouraging. 'Opportunity' which includes personal rights, tolerance and inclusion is the worst performing aspect of social progress for the EU as a whole and scores are particularly weak for the majority of regions outside Northern Europe. Environmental quality is another area of concern: it tends not to improve as regions get richer.

Romania and Bulgaria – two countries which joined the EU in 2007 — offer a mixed picture. They still lag somewhat on the 2004 intake on many measures of progress. Just compare the results of Poland and Romania, from our 2016 Index: Poland comfortably finishes higher than Romania on 11 of the 12 components we measured. But despite this lag in progress, there's reason to think that they could emulate some of the more successful EU-13 countries and begin to catch up. When it comes to basic human needs, which includes measures such as housing, sanitation and safety, it would appear that the 'so-called *first stage convergence* with older EU nation states is already happening. We know that improvements in basic human needs are often a forerunner of social progress improvements across opportunity and wellbeing dimensions, so the early signs are encouraging.

But what about the nations in emerging Europe, outside of the EU, and their potential for improved social progress? Well, if one concludes that EU membership is at least, in part, a driver for improvements in social outcomes, then the future for candidate countries such as Serbia, Montenegro, Macedonia and Albania should be bright. In fact, Serbia's score on the overall 2016 Social Progress Index is almost identical to that of Romania and Bulgaria already, and it's still in the process of applying to join. Serbia actually registers a better social progress score than Romania and Bulgaria, on measures including personal rights, access to basic knowledge and water and sanitation. It's possible the process of applying for EU membership itself might even stimulate higher social progress outcomes.

The SPI's analysis is able to calculate which countries are over-performing and under-performing on social progress against countries with similar levels of economic growth. The good news is that, of the nations from emerging Europe, only one — Azerbaijan — is classed by the SPI 2016 as an under-performer. The rest register results broadly in line with what we'd expect based on the size of their economies. In our upcoming 2017 global Index, which will be launched later this year, we'll include a historical trend analysis assessing how countries perform on social progress over time, for the first time. Once we have this data it will enable us to make direct comparisons between EU and non-EU nations over the last four years.

Measuring social progress in Europe is still in its infancy, but as we aggregate more data year-on-year, I think it's highly likely that for European nations, EU membership will emerge as an important component in the quest to improve the life opportunities of its citizens.

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The top priority that women in our region look for when choosing an employer is opportunity for career progression.

A unique confluence of demographic, historical and cultural factors is changing the balance of power between Central and Eastern European companies and the women who work for them. As increasing automation drives up the relative demand for skills that have traditionally been seen as female, employers are moving from just paying lip service to inclusion, to actively competing to attract and retain talented women.

First, a quick history lesson: While it's always hard to generalise about all the societies that CEE covers, it's certainly true that at some level, encouragement of female participation in the workforce was a common theme for all of them, during the communist era. Of course, the reality never reached the lofty ideals from the propaganda films, where smiling women drove tractors, built roads and operated lathes, in their spare time between bearing children as Hero Mothers. Nevertheless, a fundamental acceptance of the idea that women are a necessary part of the workforce has remained a part of our region's business climate.

Consider the numbers: according to PwC's *Winning the fight for female talent* report on inclusive recruitment, only 17 per cent of women in Russia say they feel employers are too male biased when looking to attract talent, compared with 30 per cent of their female peers globally. 28 per

Winning the fight for female talent in Central and Eastern Europe

cent of Russian woman believe a gender-based pay gap exists in their country, the third-lowest figure (after Malaysia and Vietnam), compared with 50 per cent of women globally. Those figures reflect how deeply ingrained the idea of women in the workforce is in our part of the world.

Culturally, it's certainly fair to say that women in CEE have some distinct advantages over their counterparts in other regions when it comes to pursuing their careers. While women are often expected to carry the primary responsibility for childcare in many of our societies, they can rely on reasonably good crèches and pre-schools, and perhaps more importantly on close family networks, with grandparents who help shoulder some of the responsibility. My Russian colleagues tell me this is a key factor in how their families operate, and I see it to varying degrees around the region.

Meanwhile, conversations with our clients and our partners in government tell me that our region also faces demographic pressure from other factors, including falling birth rates and declining university enrolment, as well as a reluctance to accept immigrants to fill the gap. I'm convinced that the solution is staring us right in the face: get more women into the workforce, keep them there longer, and bring them back faster after maternity leave. Benefits for new mothers can be quite generous in this part of the world; rather than cutting them, companies and societies need to consider some form of incentives for women not to take the maximum options available. This should be combined with more generous paternity leave, to help families distribute childcare duties more evenly.

Those demographic pressures also give an added urgency, in our region, to the wave of automation that's sweeping the entire globe — both with robots for physical labour and, increasingly, with artificial intelligence for brain work. Clients tell me that it's pushing up the relative importance of the skill sets that have been traditionally seen as female, such as creativity, intuition and empathy: things the machines can't do (yet). Companies are starting to think about how they're going to win the competition to keep those workers on board.

Throwing more money at them won't be the solution; neither will a stronger emphasis on a work-life balance. Our research shows that women here aren't motivated primarily by money, and many companies are already quite flexible in the working arrangements they offer (thanks in no small part to the demands of the millennials, both male and female). Instead, our report on the fight for female talent found that the top priority women in our region look for when choosing an employer is the opportunity for career progression. (In contrast, work-life balance comes in third, while it is ranked globally at no. 1.)

That means that when it comes to female employees, companies need to broaden their focus to include more than just recruitment (where, roughly speaking, we have just about reached equality), and pour more effort and resources into retention. We know how to get women in the door of the building; the trick now is to ensure that they make it through the door of the boardroom.

The rise of the machines means that in the coming years, companies and societies around the world will be forced to re-evaluate their labour-market practices, actively competing for female employees rather than taking them for granted. Over the next few years, the fight for talent that business leaders rank as one of their top concerns will increasingly be a fight for female talent. Central and Eastern Europe, today, offers a glimpse of how that future may look, and the steps we can take to prepare for it.

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Cautious upturn in emerging Europe haunted by the spectre of uncertainty

Over recent quarters, GDP growth throughout almost the entire region has stabilised in positive territory.

For the economies of emerging Europe, the international economic environment appears generally positive. In 2017-2018, GDP growth in the Euro area is expected to hover at around 1.7 per cent. The international financial markets have stabilised and the current economic mood is improving. Because of the global recovery, the US Fed is expected to increase interest rates further in 2017, while oil prices are likely to rise. In the EU, disbursements from the payments' cycle of the European Structural and Investment Funds are only just beginning, indicating higher co-financed investments in the Central and Eastern European EU member states (EU-CEE) from this year onwards.

Over recent quarters, GDP growth throughout almost the entire region has stabilised in positive territory. The only exception is Belarus, where growth is still in negative territory (albeit less so than was the case in 2015). The country is going through a painful adjustment process that was triggered by accumulated macroeconomic imbalances and its excessive dependence on Russia.

Our current forecasts for GDP growth for 2017-2019, point to growth of around three per cent for most of the region, with a slightly upward trend. The EU-CEE sub-region and the Western Balkan economies, in particular, should manage to reach average GDP growth rates of up to three per cent and in some countries, such as Hungary, Romania, Slovakia, Albania and Kosovo, the levels may be even higher.

In Turkey, where growth has slowed down markedly, in 2016, to below two per cent (down from around six per cent in prior years) on account of the domestic, political turmoil and deterioration in foreign relations, we also expect growth to be closer to three per cent by the end of the forecast horizon.

The CIS-3 economies of Belarus, Russia and Kazakhstan will record increasing GDP growth rates, rising from more than one per cent in 2017 to over two per cent in 2019, given the higher oil prices. Over the same forecast period, economic growth in Ukraine is projected to accelerate gradually to three per cent by 2018-2019, barring all-out warfare in Donbas and the termination of the IMF programme.

Private consumption and increasing investment will continue to be the main drivers of growth over the forecast horizon. After the investment slump in 2016, which was attributable to the switch from the previous to the current, EU (co-)financing period, investment in the EU-CEE economies will recover in the years ahead. Meanwhile the mood among consumers is improving and, because of changing spending patterns in the EU-CEE sub-region, this trend should prove durable. Tightening labour markets are conducive to major wage increases.

Despite the general rise in unit labour costs, competitiveness does not seem to be endangered. Most of the latest industrial production figures for the CESEE countries are encouraging; they point to an ongoing improvement in industry structure and, in several cases, to re-industrialisation. Longer-term FDI trends hold particular promise for the Western Balkans. In Romania and Slovakia the prospects for future FDI increases are also quite good, especially in the automotive sector. Although the size of the labour force in the CESEE countries is more or less stagnant, a marked improvement in the level of education is evident, as a younger and better educated generation enters the work force. This hints at a potential, general increase in labour quality across the region's economies.

Nevertheless, the heightened uncertainties following the UK referendum on Brexit, in June 2016, and the US presidential elections, in November 2016, have cast a cloud over the improved economic conditions noted above. It is quite conceivable that a number of worrying scenarios could ultimately make our forecasts appear upbeat and overoptimistic.

For the EU-CEE sub-region, such a degree of uncertainty constitutes a major challenge, and the consequences could be both material and negative. Thanks to US President Trump, a rise in global protectionism is possible, which would harm industry in the EU-CEE countries, both directly and indirectly via the region's close integration with Germany. Mr Trump has also questioned post-war European security arrangements, in consequence causing consternation in some EU-CEE countries.

Meanwhile, the growing irritation with the EU-CEE sub-region among some older EU Member States, and the fallout from Brexit, could possibly pose a threat to west-east fiscal transfers and the free movement of labour in their current forms. In a

Donald Trump

broader context, the evidence of an EU-wide loss of faith in the EU project and its associated values and institutions will have important consequences. This uncertainty may well act as an impediment to growth in the EU-CEE in the near future. More importantly, it could cast doubt on the prospects of longer-term EU-CEE political and economic convergence.

Uncertainties in the Western Balkans are mostly linked to developments in the EU and the USA, as well as, albeit to a lesser extent, to developments in Russia and Turkey. The region is increasingly counting on the EU market and political stability in the EU, with its promise of membership, however distant. In terms of security, the region is not self-governing; NATO plays a vital stabilising role, hence any uncertainty about the US's commitment to supporting the region could have major consequences. Moreover, any confrontational interventions by Russia combined with uncertainties as to developments in Turkey could prove quite disruptive, were the influence of the EU and USA to decline.

Increasing uncertainties in the CIS region and Ukraine are mostly related to future commodity price developments (most importantly oil prices) and heightened geopolitical tensions. The current mood of uncertainty, concerning the future dynamics of oil prices is associated primarily with supply-side factors (namely the outcome of the OPEC deal and the resilience of shale oil producers). It has been one of the key concerns for the CIS countries that are dependent on petroleum exports. The election of Donald Trump has added to the uncertainties affecting the CIS region and Ukraine. The possibility of a Trump-Putin deal and a lack of EU unity may result in the West lending less support to Ukraine, which of itself may also lead to political destabilisation.

At the same time, a potential end to the sanctions would have a mildly positive impact on the Russian economy. The ever-deepening lack of EU unity, along with the slow progress towards reforms that have been aggravated by macroeconomic issues and geopolitical strains, may jeopardise the implementation of the Association Agreements with the EU in the signatory countries: Georgia, Moldova and Ukraine.

However, seen from a currently optimistic perspective, the emerging Europe region as a whole is back on a convergence track with an average growth differential of 1.2 percentage points vis-à-vis the Euro area, over the forecast horizon.

Written by
ANDREW
WROBEL

Published on
April 24, 2017

Authorities need to invest in having an efficient and independent judicial system if they want to attract more FDI

Investors are looking for yield and they cannot necessarily find that in some of the Western European countries, so they need to look at emerging Europe.

The judicial system in many emerging European countries is not a focus for the authorities and yet, it is vital for attracting foreign investors, says Panos Katsambas, Partner at Reed Smith, a law firm that counsels the world's largest financial institutions and other financial investors. Panos spoke to Andrew Wrobel about the development of emerging Europe and the perception of the region amongst international investors.

Over the last quarter of a century emerging Europe has been going through a transition from a planned to a market economy. How successful is that process from the legal perspective?

Well, I'd say the transition has been successful because we are talking about economies that were in a completely different environment a quarter of a century ago. There was no market and so the transition to where we are today has been a success. I don't think anybody would argue that we should go back to where we were at that time.

That said, if I were to use the analogy of the human life cycle, I'd say that most of the countries in emerging Europe are still in their teenage years; they're trying to figure out their way forward. The problem I see is a lack of 'parenting' from sponsoring countries, in terms of guiding them through this transitional time. When these countries were in the very early stages of transition there was a lot of excitement and there was a lot of interest from other countries who were willing to lend their knowledge and their know-how. They were seen as lands of opportunity. By contrast, today these countries are facing the challenges of transition on their own, and are required to find their own way out of the difficulties they're confronted with to continue the transition.

The biggest reason for the decrease in support is that the 'parents', or the countries that were sponsoring that change, are facing their own significant geopolitical issues and problems resulting from the 2008 financial crisis.

So where do you see the largest challenges for these sponsoring countries?

Well, there's a big political cloud above Europe. There are still difficulties resulting from the financial crisis that haven't been resolved. There are questions about whether a broader or tighter Union is achievable. When I say tighter, I don't mean in terms of the number of participants but in terms of having a more, let's say, federal Europe. Then there is Brexit and figuring out those next steps, as well as what the shape of Europe will be post-Brexit.

What do you think will be the impact of Brexit on emerging Europe or on Central and Eastern Europe?

For some emerging European countries, Brexit will be an opportunity. The UK was a traditional entry point for Europe and Brexit gives room for others to challenge this role. Some countries have interesting offers. Bulgaria for example, has very attractive corporate and tax regimes, and has seen many businesses relocate to the country because of the ease of doing business in the jurisdiction, as well as its highly skilled personnel, especially in the technology sector.

A difficult aspect to calculate is the impact that events such as Brexit will have on migration. At present there is a real trend for many skilled workers to make a go of careers in the UK or the US. If these skilled workers were to return back to Eastern Europe, this could have a hugely positive impact in terms of keeping talent in the region.

In terms of the UK, Prime Minister Theresa May's announcement about the general election was a surprise for many. Similar situations are also happening in emerging European countries.

Absolutely, and such events have an impact on investors' confidence and perception about the region. Perhaps it's not fair to put all of the countries of emerging Europe into the same basket but it does remain the case that they do not compare with the UK, Germany, the Netherlands or even Italy and Spain when it comes to political stability, rule of law, judicial system, corruption and so forth. What happened recently with the demonstrations in Romania is a perfect example. Investors will always be more skeptical about a country with which they're unfamiliar.

Is this political instability a result of an incomplete institutional transition?

Advanced countries have an established political landscape and have longstanding institutions that have been developed further over the years. In parts of emerging Europe, similar institutions are still very nascent, and it will take more time for those institutions to develop. Emerging markets need to know that their success cannot be based on only short-term gains. In order to maintain success they need to implement changes and maintain a stable environment.

How do you think investors see the region right now?

I believe investors are interested in the region and we've seen significant economic activity in a number of countries, which is a positive sign. Investors are looking for yield and they cannot necessarily find that in some of the Western European countries, so they need to look at emerging Europe.

Panos Katsambas (courtesy of Reed Smith)

How do you see opportunities in the financial sector across the region?

I think there are opportunities for niche players. 15-20 years ago, we saw a lot of the big financial institutions going into a number of countries and acquiring local banks, thus creating massive institutions with no strategy at a local level, but just adding to the balance sheet. I don't think this model worked out as originally expected. I think what you have now is an opportunity to find openings in a smaller region where financial institutions could be good dynamic players with an understanding of the local market and approaching the banking sector from a different standpoint.

We've seen a couple of banks withdrawing from Central and Eastern Europe. What about the energy sector?

In the energy sector, putting aside any country-specific opportunities linked to discovery of natural resources, I think the renewable space is one that should attract a lot more interest going forward. There is a clear trend towards clean energy and we see renewables being a core focus of the European Bank for Reconstruction and Development as well.

World Bank's Doing Business report provides measures of business regulations for local firms in various economies. Certain emerging European areas in this report have a low "ease of doing business" ranking. How do you see the development of entrepreneurship in the region?

Entrepreneurship is a big driver of a successful economy and still needs a boost in emerging European areas. It still hasn't reached the level that is seen in countries such as the US or the UK but, then again, it's not necessarily easy in other Western European countries either.

In many emerging European countries, the public sector is still in control of many areas and that is why we need to have as much privatisation as possible, to bring private companies to the economy. To a great extent this is already taking place, but it needs to happen across the board. In Greece for example, the biggest problem is not those single measures or whether to cut one per cent here or there; the biggest need is for structural reform, a structural intervention to bring about change.

There are some challenges in that area across the region, aren't there?

It can be challenging for a foreign investor that enters a country through investing in real estate, an infrastructure project, setting up a new business or opening a retail store belonging to an international chain. They want to know that if something goes wrong, they have legal recourse.

I think the judicial system in many countries is not of focus for the authorities. They say let's change regulations, let's change licences, let's change taxes, let's change other things, but they really need to invest in having an efficient and independent judicial system which is a very important consideration in the context of foreign investment.

Earlier we talked about the European Union. How can the EU help the emerging Europe countries that are outside of the Bloc?

EU membership is a huge boost for any country. Assuming countries want to enter the EU then also enter the Eurozone; that's a different discussion. There are examples of countries such as Greece for whom the euro is a problem, to a certain degree. However, there are many positive aspects related to even being associated with the EU such as improvements to institutions, democracy and independence.

From the investors' point of view there is the rule of law which means that if they decide to invest in a country that is part of the EU, there is a certain level of protection, in addition to local European laws.

This year's EBRD annual meeting is taking place in Cyprus, an EU member state. How do you see the development of the island going forward?

I think Cyprus has done a remarkable job of leading itself out of its financial banking crisis in the last four to five years. Cyprus worked hard to overcome the psychological factor of essentially having its deposits evaporate and its banking sector collapse. The government is doing all the right things, so far, to maintain its status as a business-friendly country where it is easy enough to set up entities and where there is a good level of local professionals who can do that, especially within the financial services and the corporate sector. There's also been a big effort in the tourism sector, in terms of innovation and the simplification of procedures. All of these are attractive elements for investors.

There still is the big elephant in the room: the unification of the island. I think that it will happen eventually. As to when or how? That remains to be seen. However, if it is the will of the people, politicians can only wait so long.

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IT Park will become a center for development of Lviv IT industry with everything needed to meet the needs of business environment: including business centers and offices for more than 10 000 IT specialists.

Moreover, there will be hotels for their business partners, a university campus with modern labs, a kindergarten, a fitness center and a shopping mall. The project will be finished by 2026.

KEY OFFERINGS FOR INVESTORS

- Project is initiated by IT companies and fully supported by industry and local authorities
- Unique and considered development taking into account the needs of businesses
- Phasing
- A tested occupier demand driven development
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LVIV IT PARK

CONTACT US

IT Park: partnership@itpark.eu
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- Shopping centre with food court, service area
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- Hotel, conference facilities
- Kindergarden
- Fitness centre
- Internal and external parking
- Open green areas for sports and leisure

110 m2	GLA office space
5 500 m2	Hotel
10 000 m2	Tech university
3 000 m2	Kindergarden
18 000 m2	GBA shopping center
33 000 m2	LOI approval

UKRAINIAN IT SERVICES MARKET HAS INCREASED BY 2.5 TIMES

	2011	2015
IT services market size	$1.1 billion	$2.7 billion
IT specialist employment in Ukraine	42.4 thousand	91.7 thousand

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JOHANN STROBL
CEO
Raiffeisen Bank International AG

Published on April 18, 2017

Lower imbalances should support more inclusive growth going forward

Currently, we see a solid economic momentum in the CEE region. This assessment is backed up by key sentiment indicators, as well as hard data. Therefore, we expect seven to nine economies in Central and South-eastern Europe (CE/SEE) to post GDP growth rates at or above three per cent in 2017.

At the same time, we expect the stagnation in the Eastern European (EE) countries to peter out. In other words, we see a return to a healthy economic growth in large parts of the CEE. Even in Russia, where we expect modest growth going forward, the industry and export-led recovery are finally spilling over into the domestic economy. In CE/SEE, the economic growth is becoming more balanced and sustainable, as well.

On the back of the previously sketched and fairly positive macroeconomic backdrop, the macro-driven banking sector performance indicators are in a recovery mode as well. Most importantly, we see the CEE banking sectors are willing and able to support positive development in the region. It has to be stressed that, within this context, the current economic and banking sector growth rates come with a much lower risk attached to them than they did in the past. Therefore, they should be also be much more sustainable.

On top of the favourable macroeconomic setting, there are six aspects worth highlighting that are also providing support for more inclusive regional growth patterns. Firstly, a more balanced economic growth pattern in the CEE should also support a more balanced distribution of economic wealth. This holds true, especially if export-led growth finally translates into a consumption-backed economic expansion and solid wage growth. In this context we do not see an overly aggressive fiscal stance in the region; an aspect that receives a lot of attention in Western Europe.

Secondly, the remarkable structural downtrend in inflation in the EE region should also support lower wage earners. Moreover, in most CE/

The current economic and banking sector growth rates come with a much lower risk attached than they did in the past.

SEE economies we do not expect a very strong bounce-back of inflation by historical standards: a development that should help to secure a decent increase of real wages. Nevertheless, modest unemployment rates in several key CE/SEE markets and tight labour markets should be supportive for solid wage growth.

Thirdly, a more balanced economic expansion should help to avoid boom and bust cycles going forward. In this context we have to remember how painful the previous boom and bust cycles were for larger parts of the population, be it in the CEE or inside the Euro area.

Fourthly, the return to decent economic expansion in the CEE: well above the levels of mature economies in most cases, should support a second lag of convergence in the CEE. That being said, regional and international experience shows that solid, overall economic growth remains a key driver for bringing better standards of living to a larger fraction of the population.

Fifthly, we expect that the structural improvements, seen in the CEE region over the past decades, will finally lead to a further compression of financing cost for all borrowers. Although this aspect imposes a lot of pressure on the banks that are operating in the region, more borrowers should be able to afford a loan, or will secure their next loan, at a much lower interest rate.

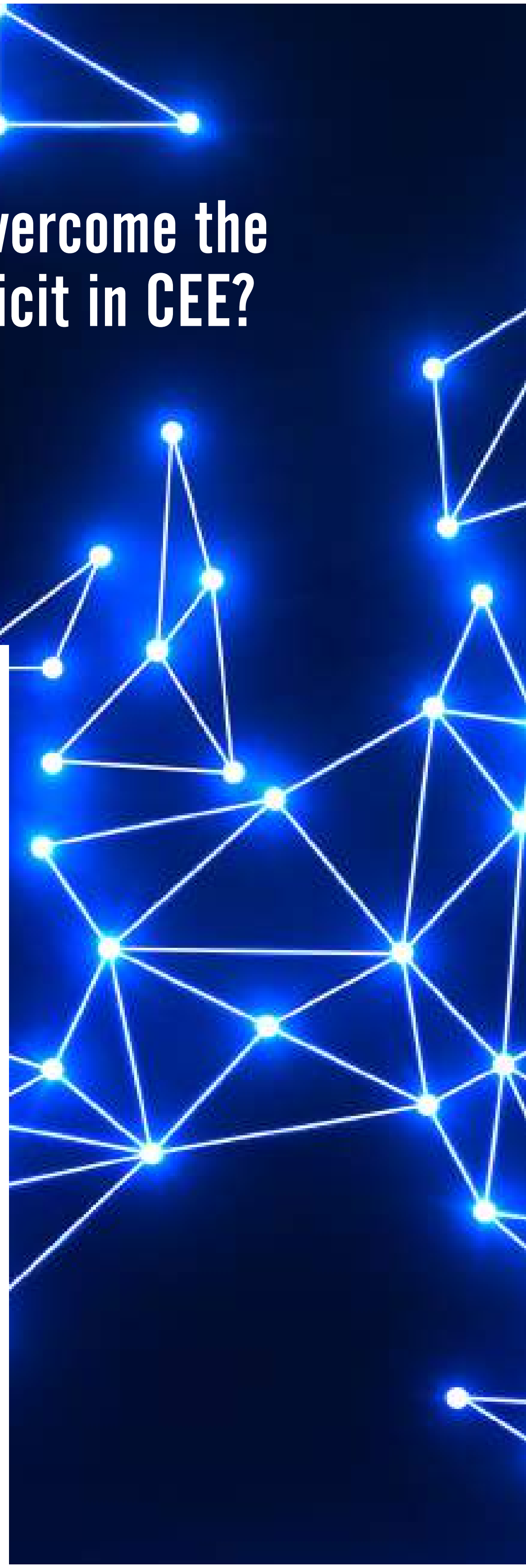
Last but not least, the overall solid standing of the CEE banking sectors and their more healthy balance sheets, at leading foreign-owned CEE lenders, should support more entrepreneurial and less pro-cyclical business strategies in future. The latter should also support the long-term growth and catch-up in the CEE. In recent years, banks were definitely forced to pursue rather pro-cyclical policies, which are not always be supportive for long-term growth strategies.

All in all, we see all the ingredients for a second lag of convergence are in place in the CEE region. As long as this convergence is based on sound fundamentals – such as it is at present – we expect sustainable wealth gains. Broad-based and sustained economic growth rates are still the most relevant drivers for inclusive economic growth. This holds especially true at lower income levels, as it is the case in most of the CEE economies.

PETER STRACAR
CEO
Central and Eastern Europe
GE

Published on
April 21, 2017

There is sometimes a conservative approach to innovation in CEE.



Will we ever overcome the innovation deficit in CEE?

The statement "if California were a country, by GDP it would be the sixth largest economy of the world ahead of France" has really proved my long-held belief that reading WEF reports is certainly not an ideal leisure activity.

If one adds to this that the Golden State produced its $2.44 trillion of economic output with six million fewer workers than France, any CEE-hearted global citizen would be close to having a heart attack after realising that the EU countries have a huge innovation deficit, with the CEE somewhere at the back of the line.

The CEE, with the V4 countries at its heart, has experienced unprecedented growth in the past 20 years. The source of that growth, however, has been low labour costs, robust internal consumption and Direct Foreign Investments. However a preoccupation with pure technology is not going to maintain economic growth in the long run and the increase in productivity is getting closer to the boundaries of technology. If the V4 countries continue to follow others, instead of creating their own ideas, growth will be soon replaced by stagnation. Further growth needs different drivers, otherwise the CEE is going to be stuck in the middle income trap.

CEE lagging behind

When it comes to listing the reasons, money always comes first. The V4 countries spend only one per cent of their GDP on R&D, while the OECD average is 2.4 per cent. This clearly shows that the support provided by CEE governments is really insufficient. Only the Czech Republic's two per cent spend on R&D is close to the EU average of 2.03 per cent, while Hungary (1.38 per cent), Slovakia (0.89 per cent) and Poland (0.94 per cent) are half as innovative as other EU countries.

I strongly believe, however, that the issue is not just about money. It is also about having a supportive public and political framework, which helps develop an innovation culture. This is a second area which could be improved in the V4. The Global Innovation Index ranked the V4 between 27th and 35th globally, when it came to how the regulatory environment supports innovation. Global excellence requires a stronger role for the private sector in order to raise efficiency, which means that increasing R&D spending also needs more products, which could be commercialised on a global level.

These issues have a snowball effect. One of the consequences of the less public and political framework is the weak Intellectual Property (IP) culture in the V4, which is clearly reflected in its patent application statistics. In 2016, for example, there were 408 European patent applications from Poland, 28 per cent fewer than in the previous year, and a very low number given the size of the country. The number in the Czech Republic was also down, by 13 per cent,

to 185, and in Slovakia there were fewer than 100 applications.

Only Hungary showed a slight increase, but with 108 applications it is still at a very low level. GE squeezed into the top ten companies, with the most European applications in 2016, i.e. 1,628 applications. This means that GE submitted more patent applications than the entire V4 combined, last year.

The weak IP culture is also embodied in what we call the "not functioning innovation linkages". Specifically, this means the level of research collaboration between universities and industry, the state of cluster development and the volume of joint ventures/strategic deals. In this respect, the CEE really underperforms relative to its real opportunities, and given the fact that it has a good higher education system and leading multinational companies are present in the countries.

Consequently, there is sometimes a conservative approach to innovation in CEE. Executives in the region are mindful of the threat of 'Digital Darwinism', with more and more companies becoming obsolete as technology evolves quicker than they can adapt. However, despite this awareness, CEE companies favour more conservative innovation strategies, preferring to rely on incremental innovation rather than breakthrough technologies.

Likely to overcome?

Let the private sector drive the car. €14 billion from EU structural funds will be spent on R&D in the V4 countries in the period leading up to 2020. If I had one request for governments across the region, and only one, it would be to invest this money in creating an efficient cooperation with the private sector. The truth is that there are only a handful of examples of products that have been developed in CEE, and which have gone on to be globally successful. This area — turning great ideas into products which can be commercialised on a global level — is one that the private sector understands better than anyone else.

This request is strongly linked to my digital belief: the WEF describes some CEE countries as economies that are transitioning from efficiency-driven (manufacturing-focused) to innovation-driven. I truly believe that for those transition countries, it's the digitalisation of the industry that offers the enormous potential to catch up with Western Europe and the US.

What we call the industrial internet represents an opportunity for Europe to add €2.8 trillion to the GDP of Europe by 2030. Given the three per cent annual increase in industrial output in CEE, we need to nurture this high manufacturing presence with digital. If there were Digital Hubs and Software Development Centres all over the region, CEE would be in an ideal position to win the race on the industrial internet — and the market is there. In the past, less than one in five manufacturing companies used high-performance enabling technologies, sustainable manufacturing technologies or IT-enabled intelligent manufacturing. I am more than impressed by some examples, which show how the latest technologies that have been adapted in our region are going to revolutionise today's methods of global manufacturing.

For instance, a third of the components being produced in the new GE Aviation turboprop engine manufacturing facility, in the Czech Republic, are going to be 3D-printed, which is what the industry calls Additive Manufacturing. The Czech government expects that facility to be the kick-off for high-tech investments that will create an entire industrial ecosystem involving suppliers and national R&D institutions.

I know that those technologies are real game changers for CEE. More highly qualified experts will be needed across the entire value chain. The challenge here is to avoid the often observed "boom and bust" cycle of prospering economies, which sees more investment, low unemployment and subsequent steeply rising salaries—without overall productivity being able to keep up. With productivity growing faster than salaries, if we want to stabilise growth, it will be essential to embrace the productivity opportunities of the industrial internet.

Countries and companies that adapt and change first will be the winners, and those who wait passively will be the losers. For CEE and the V4, strong collaboration with industry and the digitisation of industry and society are not just an option, but the only way to stay in business.

Written by
NIKODEM CHINOWSKI

Günter Verheugen: populist politics and euroscepticism will have an impact on CEE

Published on
April 2, 2017

I do not like the view that immigration and terrorist threats are two sides of the same coin.

With the European Union going through the most turbulent time in its history, new questions are coming up about its future, which, in fact, might be even more challenging. What impact will Brexit have on the EU, what changes will take place in Europe after this year's elections in France, the Netherlands and the Czech Republic; these are only a few of them.

Günter Verheugen, former European Commissioner for Enlargement and later Commissioner for Enterprise and Industry, who played an important role in the EU enlargement process in 2004, spoke to Nikodem Chinowski about the future of the European Union.

Are you surprised and/or concerned about the wave of populism and Euro-scepticism that is washing over the entire continent recently?

No, I am not too surprised. We have seen both phenomena in the past. The combination is new: populism and Euro-scepticism are reinforcing each other. My impression is that the populists are using the undeniable shortcomings of the European integration process as a scapegoat and an easy explanation for everything that is going wrong. The crisis of the European idea started in the 90s, of the last century, already, and to be precise it began with the treaty of Maastricht.

Has this wave reached its peak already or is a tough time still about to come?

A precise prognosis is not possible and experience tells us, that political and economic forecasts are notoriously inaccurate. Some American strategists, such as Brzeziński, were already saying that the world was approaching a period of uncertainty or even chaos, years ago, and they said that this period could last for decades. But there was another one, Francis Fukuyama, who stated that after the collapse of the Soviet system "the end of history" would mean permanent harmony and peace. If I look at the challenges of the future, which we already know about, I come to the conclusion that we have very little time to change direction. The famous doomsday clock is now fixed at 2.5 minutes before 12.

What about a further enlargement of the EU — which countries may join our European family and when? Or maybe that issue is beyond the foreseeable future?

For the time being, an enlargement of the EU, which incidentally is a term that I do not like because of its geopolitical connotation, is not on the agenda for the EU. The present commission has made it very clear that during its term no accession will happen. Things can change, of course, and a new window of opportunity may present itself. In my view, it is of the greatest importance that we maintain the principle of openness. As the treaty clearly stipulates, the European integration process is open for every European country that is willing and able to fulfil the conditions.

The West Balkan countries have had an accession perspective since 1999, and it has not been renounced. They will join eventually, but not in the near future. I actually wonder whether everything has been done to encourage the West Balkan countries to move forwards. The accession of the region has not been seen as a strategic priority as it should be, but rather as an uncomfortable promise from the past. In the present situation, my recommendation for the West Balkan countries would be to deliver as much as possible, as soon as possible –transformation is not necessary because Brussels wants it, but because there is no future for the region without it.

Does Brexit make the EU less attractive for the five recognised candidates for future membership of the EU?

No, I don't think so. For all those countries the UK's membership of the UK is important, of course, but not vital. Their strategic interests are not affected by Brexit.

You have mentioned the West Balkan countries in terms of the enlargement of the EU. What are the biggest advantages that the EU could offer to countries such as Albania, Macedonia, Serbia or Montenegro?

For these countries, membership of the EU would make their transformation processes irreversible and would strengthen their standards concerning democracy, the rule of law, human rights and good governance. But the most important advantage, in my view, is the fact that the traditional European nation state whether it is big or small, rich or poor will not be able to meet the challenges of the world of tomorrow, if it stands alone. If the idea of European unity did not exist already, we would have to invent it, now.

The same question related to Turkey…

Turkey has been negotiating accession since 2005, but the distance is growing. The perspective is very gloomy. For the other European countries accession is also not a realistic option right now.

… and Iceland? Why may the EU look attractive to such a wealthy country as Iceland?

Iceland has what it needs to have: the country is a member of NATO and a part of the European Economic Area and therefore fully integrated into the single market. I don't think that the accession question will be back on the agenda for Iceland, in the near future.

The unexpected result of the Brexit referendum — that is London eventually leaving the EU — is that a warning or a spur to the other member states' governments?

Good question. Since a so-called "hard" Brexit is what the UK wants, it is less likely that other countries may find the British

Günter Verheugen (courtesy of Günter Verheugen)

example attractive. A "soft" Brexit would have been a different thing. However, decisions of that kind are not the result of clear strategic thinking and good reasoning. They are very emotional, and as I already said: the combination of populism and Euro-scepticism is really frightening.

So you are concerned about the possible domino effect?

Yes, I am concerned that Brexit will not be an isolated event.

How might issues of internal security that are connected with terrorism and migration affect the unity of the European Union? Will those issues reunite the member states into one organism or will they make them work apart?

Clearly, this problem has the potential to weaken the EU because the interests of the member states are very different. Not all of them are target countries. I do not like the view that immigration and terrorist threats are two sides of the same coin. We need to have a reasonable policy, which regulates legal immigration; we need to have safeguards if we want to maintain freedom of movement; we need to make the control and protection of our external borders a responsibility of the community and we need to develop capacities which will allow us to prevent conflicts and to eliminate the causes for mass immigration: war, poverty, environmental disaster. It can be done – but I am not too optimistic if I take the present state of play in the EU into account.

Do you think that the fear of the negative impact of the USA – spurred by Donald Trump's win in the US elections – on the continued functioning of the European Union is justified or will the future prove that these fears were unfounded?

I could be wrong, but my impression is that the Trump presidency is a kind of eye-opener for the EU-countries. We have security and trade concerns after President Trump's declarations and the debate has started how we can defend our interests and maintain our way of life. In my view, the result of that debate must be a stronger EU that speaks with one voice in international affairs and that has an independent defence policy. It is important, now, that the EU member states do not try to make narrow national deals with the Trump administration but rather that they respond to the new challenge as a united and self-confident union.

Essentially, European integration has always been a trans-atlantic undertaking. Does Donald Trump's presidency change this attitude?

This is true for the beginning of the process. European integration was a western European project that was encouraged, and even sponsored, by the US. It was an element of the cold war, but that changed after 1989, and after the enlargement of 2004 and 2007. It is now a truly European project. I found it interesting that some US-think tanks – normally close to the neo-cons – made it very clear that a strong and united Europe is not in the interests of the US. Interesting, but wrong. The fact that we have Trump as president does not change our long-term interests: the EU and the US have to maintain their strategic partnership, which hopefully will develop as a partnership on an equal footing.

The year 2017 will witness major presidential and parliamentary elections in the EU. The most important choice – within the context of the future of the EU — will take place in France. How do you see the future of France and the European Union in case Marie Le Pen wins the elections?

That could be the beginning of the end. We must never forget that the whole idea of European integration was basically a new concept to overcome the traditional conflicts between Germany and France. Politically, the German-French relationship is still at the core of the integration. I do not see how a President Le Pen would go along with that. After the experience of 2016, when everything went wrong that could go wrong, we should not be complacent here. If the traditional voting pattern in France continues, a president Le Pen will be prevented, but the French problems will still be there.

Aren't you afraid that one of the most popular expressions among European politicians in 2017 will be the word "adieu"?

Not yet, but we will know that after the French election. As I have already said: expect the unexpected.

In mid-March, the Dutch chose a government. The favourite runner was the populist, far-right Geert Wilders but it was centre-right Mark Rutte, who eventually won.

Traditionally, the Netherlands is one of the most integration-friendly countries so it would create a serious problem, if Wilders and his party were the strongest party in the country. Even if not in the government, these populists — and nationalists — will clearly influence the agenda.

The least controversial election for 2017 seems to be the election in the Czech Republic. The favourite is the ANO 2011 party with Andrej Babis as the leader. Do you perceive a risk that the Czechs will copy the Hungarians and Poles and the anti-EU mood in the Czech Republic will increase?

No, I am not worried as far as the Czech Republic is concerned. This is a very stable and democratic country and by and large it is doing very well. It will remain in the pro-integration camp.

Let's recapitulate. Where do you see the greatest threat to the EU in 2017?

The threat is a further disintegration as a result of populist majorities in some member states and a lack of political courage.

And the greatest opportunity?

The opportunity is to use the new global and European environment for a renaissance of the idea of European unity.

Leszek Balcerowicz: the word "transition" is hugely misused and rarely defined

Written by
ANDREW WROBEL

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Leszek Balcerowicz (photo by Adam Golec)

First, increase the pressure for reforms; be ready with a package, and finally move with the maximum possible speed

In 1990, GDP per capita in Poland and Ukraine was roughly the same and amounted to some $1,600. By the end of 2016, Polish GDP grew to $12,700. In 2013, GDP per capita in Ukraine equalled $4,200 but the recent recession has caused it to fall again, to some $2,000.

Leszek Balcerowicz is a former Polish deputy prime minister, and he is known for implementing the Polish economic transformation programme in the 1990s: this was a shock therapy that is commonly referred to as the Balcerowicz Plan. He is a former governor of the National Bank of Poland. He also was Ukrainian President, Petro Poroshenko's, representative in the cabinet of ministers. He spoke to Andrew Wrobel about Poland's transformation in the 1990s and the current government's economic growth plans, as well as his ideas for the economic development of Ukraine.

Are you happy with the so called "Balcerowicz Plan" which you introduced at the beginning of the 1990s in Poland? I mean, if you look back at the transition that has taken place in the country over the last quarter of a century?

This is a classic question. I've been asked this plenty of times, by different people, and that is not a criticism.

No, not at all. I would like to know if you would have done something differently.

Yes, but first of all, I think the word "transition" is hugely misused and rarely defined. Usually it indirectly means that you have a change from one system to another system, call it a market economy or even more precisely, capitalism together with democracy, with highly developed civil rights and a high level of the rule of law.

So if you mean that transition, then you see huge differences. I think that Central Europe, including the Baltic States, has reached this different model. They are not all the same, but quite similar. Then if you look at Russia, reforms were started [by Yeltsin] but have been reversed under Putin. In Belarus, reforms were reversed even earlier by Lukashenko who has won several elections. What you see in Central Asia is more socialism, not transition.

Now, if I come back to your question: I try not to base my judgment on emotions, but rather on what careful, empirical, economic investigation can tell you. There is a lot of investigative research, so one can draw two sorts of conclusions. The first one is that the countries that started the transition earlier, as early as possible in fact, and that did not reverse it, are in much better economic situation now than countries which, for some reason, started it later and achieved fewer institutions in the market economy.

Professor Oleh Havrylyshyn compares Poland and Ukraine.

Yes, there are indicators; comparative studies of Poland and Ukraine. In 1999, these two countries were at the same level of per capita income. Now, I think Poland has a level of per capita income that is at least twice as high. Of course, there are non-economic aspects and there are some people who would wrongly imply that, "Yes, okay, radical market reforms are good, perhaps for the economy, but not so good for other aspects of life." They cannot find examples because in Poland, and in some other countries, – if you look at social statistics such as life expectancy, child mortality, etc. – you see that they have achieved very good results. Countries which have introduced economic market reforms are better than countries which have, for some reason, not done it.

In Poland, the social record improvement, which is a social indicator, is as fast so far as the economic growth. You can point to the mechanism which links market reforms with improvement with social indicators, including health. We have seen some interesting research in Poland, which links an improvement in health with huge changes in the diet, but which were not the result of any government programme, but rather the revolution in prices, as well as the ability to learn and recognise the value of more healthy food. There are also other aspects such as the level of fear, which is much higher under non-democratic regimes than under democratic regimes. That is a very important component of the standard of living; whether you are afraid of your own government, such as happens under communism or socialism.

So, once again; by looking at the available research, there isn't a single iota of proof that fewer market reforms are better for the economy. However there is still a lot of clamour about this which started with this nonsensical distinction between shock therapy and gradualism, or in other words — all at once or one by one.

Before we discuss this, would you say there is a reform that should have been introduced and wasn't, especially in the early 1990s?

It would have been better to have tackled the social sector early. I do not mean more social spending. I mean more reforms, but I very much doubt that would have been possible given the initial situation in Poland which was catastrophic – there was hyperinflation and a very high level of foreign debt and I only had a small team, which I directed. It would've been better but I don't know whether it would have been possible to do much more.

However, it's worth mentioning that Poland had a second period of reforms that is often forgotten, but which are equally important. This happened between 1997 and 2000, and when I was deputy prime minister and minister of finance. At that time we accelerated privatisation; we introduced a fundamental pension reform and an education reform. We also carried out a massive restructuring of mining.

You said that the Polish economy was in a catastrophic condition after the fall of communism.

Yes, there was hyperinflation, but there were still massive shortages because many prices were still controlled. There was a chaos in the pricing system. The economy declined because of this chaos. But there was one good outcome: Poland became free. There was also a feeling that since Poland had become free at the same time as the economic catastrophe then people were readier than normal to accept, say, radical changes.

I would have never accepted a government job just to be in the government. Prime Minister Mazowiecki asked me and I refused. Then, he asked me again. Eventually I accepted but I it was under the condition that I would make radical changes. Based on my previous research, which I had also done with a group of people in the late 1970s, only radical changes can succeed. The Prime Minister accepted my condition and we began.

Would you compare the freedom regained by Poles in 1989 in any way to what happened during Maidan? I remember a Ukrainian taxi driver in Kyiv who had come back from Moscow, to live in Ukraine, saying that Maidan had changed people and they wanted change now.

I thought then, and I think now, that they were similar, but remember such an atmosphere cannot last for a very long time. It can last for a year, but not longer. This is a gift and it should be used, but how? By rapid reforms. For me, this was an important non-economic reason for rapid reforms but there were also plenty of economic reasons.

I very often hear experts saying that the last three years have seen more reforms in Ukraine than the previous two decades. Do you think those 20 years were lost?

Not completely. It certainly could have been better, but there's no point in discussing what was missed. Rather one has to try to catch up.

Exactly. So if we were to compare Ukraine with Poland…

I would say that perhaps the biggest similarity would be between Ukraine in 2014 and perhaps Poland in 1997, in the sense that the second reforms have already been done, but one has to speed up the other reforms. What is specific to Ukraine, and not for the Poland of 1997, is the aggression, both military and economic. As much as the military aggression is obvious to everyone, the economic one is not — Russia used to be Ukraine's largest importer

Leszek Balcerowicz (photo by Adam Golec)

and then it introduced a ban on Ukrainian products. This alone was bound to produce a deep recession, which did happen and collectively was about 17 per cent.

However with new authorities' policies, there could have been a worsening catastrophe but they avoided it. Why? Well, they avoided a fiscal catastrophe. The budget deficit of 2014 was in the range of ten per cent and now it's about three per cent, with a simultaneous increase in military spending because Ukraine did have a proper army before.

Leszek Balcerowicz (photo by Adam Golec)

Then, there is the banking sector — Governor Gontaryeva did a tremendous job by reducing employment in the Central Bank by two-thirds, and then improving the banking sector. Finally inflation was reduced from around 60 per cent to around ten per cent.

I believe privatisation should have happened faster. I think privatisation is low-hanging fruit from the economic point of view. Demonopolisation definitely needs to come, which would involve the identification and elimination of the role of oligarchs, if they are not compliant with the rules that are in order. Another aspect would be improvements in the business climate, so that there's more investment including foreign investment.

If all the necessary measures were taken now, when do you think Ukraine could potentially catch up with countries such as Poland?

What matters is to grow faster at, say, more than three or five per cent. Unfortunately, Poland is starting to have its own problems, given the bad policies of the present government.

Yes, the new Polish government has been in power since mid-November 2015 and Mateusz Morawiecki, the deputy prime minister and the minister of economic development and finance has created a Responsible Development Plan which was approved of by the Council of Ministers in February 2017.

First of all, this is not a true plan in a technical sense. There are goals in it but they are the continued fast growth of Poland and catching up; however, the measures which are proposed are contrary to these goals.

Just to be more specific, Poland has an excessive budget deficit. In a booming economy there should be a surplus, or at least a balance, but not a three-per-cent deficit. Then, the forces that are responsible for longer-term growth are weakening in the country. Because of the ageing population, fewer people will be going to work, unless certain measures are taken, such as raising the retirement age. Then, the investment ratio, especially private investment, is low and, most importantly, the rate of growth of overall productivity has slowed down a great deal in the last few years and this is the main driver.

Two years ago, my younger colleagues and I presented three scenarios for Poland's development. The first one assumed that all challenges had been neutralised by proper reforms. The second one assumed no reforms were introduced and the third one assumed counter-reforms were introduced which would result in a slowdown. What has, and is, being done and is also listed in the so called Morawiecki Plan is the worst-case scenario: for example, not only nothing is being done to heal the public finances but additional expenditures are being introduced.

The government has also lowered the retirement age.

Yes, so this is not a plan, unless the goal is to slow down the growth of Poland's economy.

What, then, should be done in Poland to benefit from the growth of the last quarter of the century and even to further improve the situation?

If we look at ageing, which is a good thing in itself because it's better to live a longer than a shorter time, we need to remember that it has certain demographic consequences. You have to increase retirement age, which was done by the previous government but has been reversed by the present one. As a result, if no further action is taken, we will have even more people who are not working and who are drawing pensions in a pay-as-you-go pensions' system that is financed by younger people. It's difficult to imagine a greater sabotage to economic growth than that.

It was not very difficult to diagnose the challenges and to propose reforms. The main problem, as always, is it's a political economy. We have now a bad government. They should be democratically removed and this is a test for the Polish society.

Now the government is after the VAT mafia. Tax offenders can be imprisoned for 25 years.

I can refer to the economics of crime literature. From that, one learns that there has to be a certain gradation of crimes ascribed to different offences, because otherwise, it's chaos. Let me give you an example: imagine there is a VAT offender who committed a crime and there are witnesses who can prove that. What should this offender do if the penalty for murder is the same as for his VAT crime? Secondly, the very possibility of being wrongly accused and sentenced adds to uncertainty.

So if no proper reforms are introduced to address the key challenges we discussed earlier, how do you see Poland's economy in two or three years?

Poland is vulnerable, especially its public finances. If there's a strong external shock who would be hit the hardest? Countries with weak public finances. What is practically certain is that with these policies, which are intensifying and making challenges harder not easier, Poland cannot maintain its previous rate of growth, so there will be a serious slowdown. Whether it is dramatic or gradual depends on the external factors.

But speaking practically, what Poland has achieved so far was beyond the expectations of most people. Who would have had expected, in 1999, that Poland would be the best-performing country in Europe?

Why do people emigrate from poorer countries? I'm not speaking about refugees, because they are poorer and they have an economic direction. This is an old story. If there is a substantial or big gap, between what you can earn in your country and what you can earn elsewhere, and the standard of living is better, some people make a decision to leave.

The Polish governments want Poles to come back, for example, from the UK.

Yes, but the only effective way of halting this feeling of pre-emigration is to grow faster in a poorer country. The threat is that if Poland stops catching up, emigration will continue. These are usually the most entrepreneurial people. So policies which are bad for growth are very good for emigration.

Now, if again, we look at Ukraine and Poland, what lessons, perhaps, should Ukraine learn from what is happening in Poland today?

The lesson is first work to increase the pressure for reforms; be ready with a package, and finally move with the maximum possible speed.

I believe you shouldn't introduce counter-reforms because they result in a slowdown. In your recent book you call yourself a fighter, don't you?

Actually, somebody else suggested the title but I thought it matched me because, yes, I have had to fight. I am not speaking about my childhood fights, but fighting for reforms because they are not going to just drop down out of the sky.

There are many resistance forces and interest groups defending that system so one has to overcome them by mobilising other people. You have to be faster and more energetic and better at communicating your ideas.

Petro Poroshenko meeting Leszek Balcerowicz (courtesy of president.gov.ua)

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The dragon is knocking at our doors

As in the EU, almost all countries of the CEE region didn't prepare or present their own blueprints and strategy for China.

The assertive and ambitious leader of the 'People's Republic's fifth generation of leadership' and charismatic president, Xi Jinping (in power since the end of 2012) is attracting worldwide attention. However, because we are quite a distance from China, mixed unfortunately with a lack of strategic thinking and a certain neglect of the 'emerging markets' phenomenon on the European side, our understanding of the strategic impact of a China's new role remains below expectations and needs.

This is also visible in the Central and Eastern Europe (CEE) countries, even if the previous Chinese leadership (of the Fourth Generation) already came out with a new blueprint for their relationship with the region, in the form of the then-famous 12 steps, which was proposed by Prime Minister, Wen Jiabao, in Warsaw, in April 2012. Not much was implemented from this ambitious plan - to inaugurate stronger economic ties - but at least, since then, we have a new framework of cooperation known as 16+1, with its own Secretariat and annual summit meetings.

Even the flagship of this new cooperation - a high-speed Chinese bullet-train route from Belgrade to Budapest, which was announced with some excitement at the third Summit in 2014 - is not ready to start and the European Commission has expressed some doubt concerning the transparency of the deal, with its latest concerns being expressed in February this year.

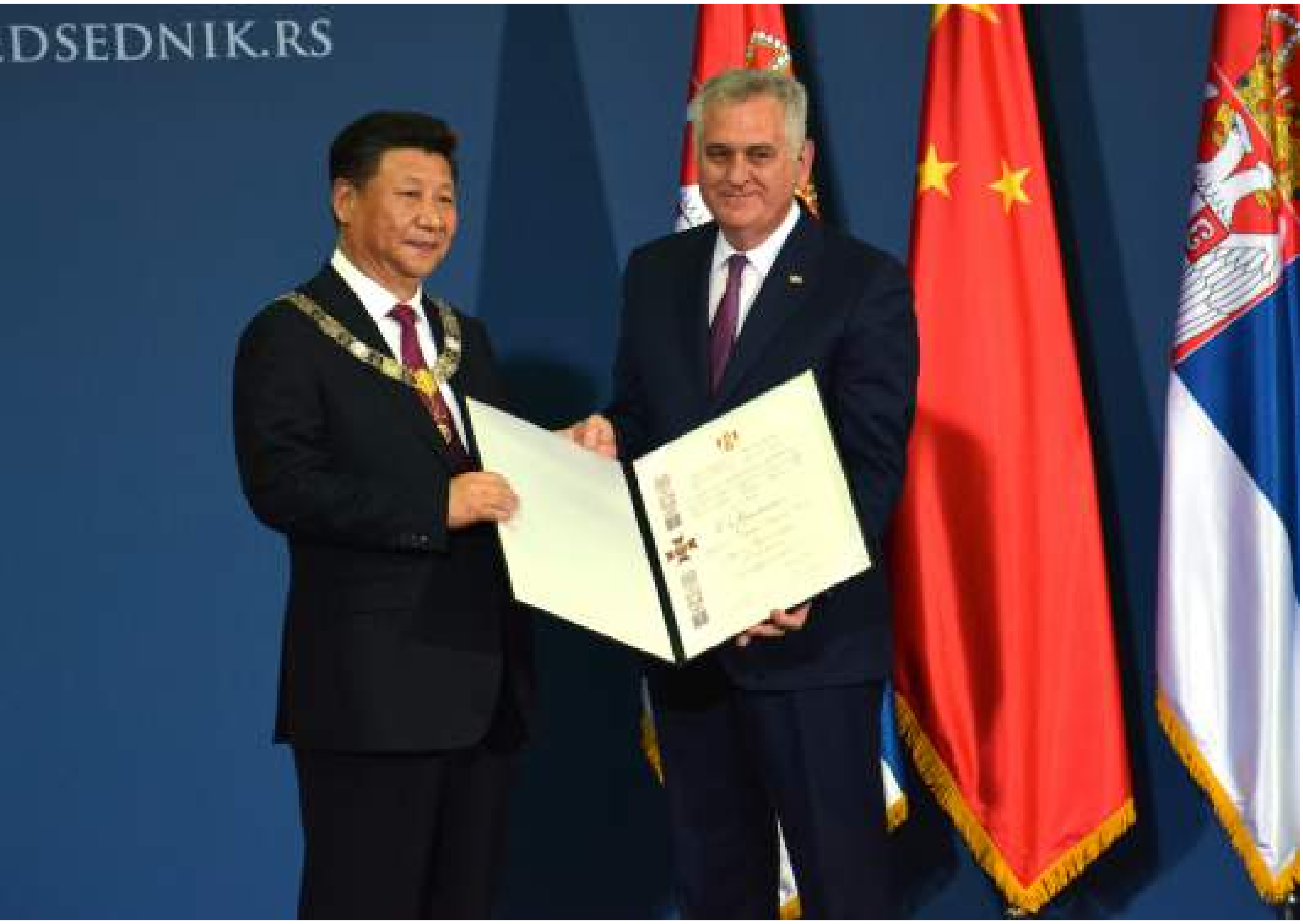
Nevertheless, and not taking into account such obstacles and complications, China is pushing forward - especially after the inauguration of another ambitious strategic project in late 2013; the visionary One Belt, One Road (OBOR). It is supported by an institutional framework and includes a special OBOR Fund. It is 'Asian' by name but Chinese by money and design and the funding comes from the Asian Infrastructure Investment Bank (AIIB). Thus, another important stimulus was added to the growing and ever-rich agenda of China-CEE cooperation.

The crucial problem is that, as in the EU, almost all the countries of the CEE region didn't prepare or present their own blueprints and strategy for China. Only Hungary under the leadership of Prime Minister Viktor Orbán - also a strong and charismatic leader (although controversial in the EU) - has announced its own 'keleti nyitás' meaning 'Opening to the East policy'. Results, up until now, have been disappointing and even foreign minister, Péter Szijártó, has publicly confessed, as late as last year that almost nothing from this strategy was implemented, least of all the 350 km of Chinese high-speed railway to Belgrade.

There is an array of difficulties and obstacles: we start from different business mentalities on both sides - we believe in institutions, rules and regulations, including public procurements and the Chinese believe in personal relations, mutual trust and win-win strategy, etc. Despite this, Hungar is pressing for further cooperation. In December 2016, a first step in the bilateral cooperation for OBOR was taken in Beijing, with Szijártó and his counterpart, Wang Yi's signatures, and earlier this year Hungary joined Poland to be the second country from the CEE region to be represented in the AIIB.

Budapest is ready to give two-year long visas to Chinese businessmen (others in the region are usually given around 90 days), and it is also expanding its programme of settlement for Chinese citizens (although it is not directly transparent: this will cost some 300-350 thousand Euro). It is not a coincidence then, that Hungary is emerging as a leading trade and investment partner for China in the region (true - Poland has replaced it in last two years, but no one knows for how long), and — on the other hand — it is also no surprise that a special think-tank network was just established in Budapest, on April 24th, with a prominent role being taken by the Chinese Academy of Social Sciences in Beijing's Institute of European Studies that published recently a series of important volumes (both in English and Chinese) on bilateral relationship with the CEE region.

From reading those publications, as well as the official announcements, we know that Poland will be a crucial partner for the Chinese because of its geopolitical position and location between Russia and Germany (this was once a curse historically, but now it is an advantage from the Chinese perspective). Poland also has the biggest economic potential in the region. This was confirmed



Xi Jinping with the Serbian President

by the visit of President Xi Jinping to Warsaw in June 2016, when the bilateral relationship was upgraded to the highest possible level, i.e. a comprehensive strategic partnership.

However, as we now see, not too many of the agreements that were signed were implemented, and the creation of a regional communication hub in the town of Łódź - very important in the Chinese plans - has been postponed. The Polish Minister of Defence decided not to allow the military territory, which belonged to the army, to be given over for new Chinese investments. However, the Chinese response is significant and pragmatic - if we cannot manage with the government, we will turn towards the alternative government (in the opposition's hands mainly), who are usually more eager to cooperate or invest. So, plans for the railway hub have shifted, recently, from Łódź to nearby Kutno and we can identify one local investment after the other beginning to take shape: after earlier investments in the steel works in Stalowa Wola or the rolling bearing factory in Kraśnik, we saw fusion and mergers with the Nuctech company (medical equipment), movement in the energy sector in Gdańsk (Piinggao Group) or Lublin (Sinohydro), and electronics in Żyrardów or plastic goods in Tarnów.

As for Western Europe, which is the main direction of the new Chinese investment fever (some $170 billion in 2016, as much as 44 per cent more than a year earlier) the Chinese are eager to get some trademarks established, which is not necessarily what the CEE partners expected. For instance, in Romania, only one greenfield project coming from Chinese investment was inaugurated, in the port city of Constanţa. All the other investments are fusions with existing industry or companies (such as air terminals, sea ports, etc.).

So, instead of a having a normal trade in goods, we in the CEE region have almost all the Chinese banks here already; we have new investment projects and visible activity. It is time to wake up and to respond in a more inclusive way to this new phenomenon.

Participation in the upcoming first Summit meeting of OBOR, scheduled for mid-May is probably is not enough, even at Prime Ministerial level, as in the case of Poland, the Czech Republic or Hungary. We should have our own think tanks and our own ideas about what to do with the new Chinese initiatives. Especially given that the lack of trust and mutual knowledge remains the main obstacle in this constantly growing exchange.

But what are the Chinese's expectations? We'd better be ready, because a dragon is knocking at our doors!

Belarus is bringing opportunities for European companies

Written by
JERRY
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A strategically located, eco-friendly SEZ with a well-integrated logistics platform is the trend of the future.

According to the EU statistics, China and Europe now trade well over €1 billion a day. The Asian giant is the EU's second trading partner behind the United States and the EU is China's biggest trading partner. At the same time the country accounts for a mere two or three per cent of overall European investments abroad. Why? Perhaps because some European investors are concerned about starting their own operations in China.

Ansgar Rudolph, project manager at InSite Bavaria, a German competence centre for industrial site development that is owned by the Technical University of Munich, says that instead of investing in a production plant in China, companies from Europe can have Chinese partners in Belarus.

"I see great opportunities for European companies to be closer to China; to be the neighbour of a Chinese company without facing the biggest disadvantages of operating a plant in China. The Great Stone [Industrial Park, located on the outskirts of Minsk] is the first transnational industrial area that provides a common ground for European and Chinese companies and that implements common standards for the two business worlds," he says.

"It is predicted that by 2030, nearly 66 per cent of the world's middle class will live in China," says Freddy Opsomer, Chairman of the Board of Directors at the Free Economic Zone in Kaunas, Lithuania. "That opens enormous prospects for the export of European goods to China but there are also new markets in India, Pakistan, Iran and Kazakhstan," he adds.

Between the East and the West

Dmitry Krutoy, First Deputy Minister of Economy, says that Belarus has long been considered a gateway to Europe on the one hand, and to Asia, on the other. "It is located on the largest Trans-European highways as well as trade routes between the West, East, North and South. Because of this beneficial location, as well as the development of the industrial park, not

Great Stone (courtesy of Industrial Park Development Company) only is Belarus a transfer-territory - as part of the concept of the Silk Road Economic Belt - but also a destination on its own for goods production, processing, packaging and storage," he tells *Emerging Europe*.

Frank Schuhholz, a logistics expert and the founder of FMS Advisers, points to the fact that the park is located close to Minsk airport and a two and a half hour drive from the Belarus-Polish border, which is the eastern border of the European Union.

"The project, which can be described as a large free trade and investment zone, covers an area of over 90 square km and will eventually hold workplaces for roughly 100,000 people. It is intended to attract local, as well as international investors to use this location as a manufacturing, trading and distribution hub which is closely tied to the railway corridor that links Europe and China," he adds.

"Great Stone is the largest project that has been implemented in Belarus," says Deputy Minister Krutoy. "It is an eco-city with a modern infrastructure and comfortable living and working conditions. A special management system provides investors with an opportunity to complete all the necessary administration procedures in a one-stop-shop scheme. We have also created conditions that facilitate the implementation of scientific and technical achievements such as a venture investment fund, as well as a centre for commercialisation of scientific research," Mr Krutoy adds.

Infrastructure in place

"However, in today's competitive environment, investors have many choices of where to invest and locate their businesses," says Deborah S. Porte, a Special Economic Zone expert with over 25

years' experience in the design and development of various types of economic zones, transport and cargo hubs and technology parks. She has worked for governments and international organisations such as the World Bank.

"What makes a SEZ and its associated country attractive to an investor is a transparent and accountable SEZ regime and well managed SEZs where land is readily available on a long-term basis, where power, water and ITC are reliable, and where there is access to a skilled and/or trainable labour pool. A strategically located, eco-friendly SEZ with a well-integrated logistics platform is the trend of the future," Ms Porte tells *Emerging Europe*.

Sergey Vaitekhovsky, Deputy Director General at the Industrial Park Development Company, says the company has invested $300 million in the development of the Park's infrastructure so far. "Currently, all of the infrastructure, such as main roads, a gas supply network, water intake stations, IT, water treatment facilities and a distributive electro-station have been completed. All contracts can be signed only with us. We now have eight residents registered and we expect 12 more to register by the end of 2017," Mr Vaitekhovsky adds.

"Great Stone is very attractive for foreign investors from a tax point of view," says Svetlana A Gritsouk, Tax and Law Director at EY Belarus. "Investors are free from any corporate taxes such as profit tax, land tax, real estate tax, for ten years, and for the following ten years they receive a 50 per cent discount from the existing rates," she adds.

Mr Vaitekhovsky adds that, because the Park operates as a free customs' zone, there is no need to pay VAT and customs duties. "Besides the corporate advantages there are several other benefits for attracting foreign labour, such as a rate of income tax for individuals that is fixed and constitutes only nine per cent - that is a third less than in the country, as well as social insurance payment benefits," he adds.

Belarus - investment-friendly potential for Poland

Kazimierz Zdunowski, Chairman of the Polish-Belarusian Chamber of Commerce and Industry, says that currently there are almost 550 Polish firms, or firms with Polish capital, in Belarus and they perceive it as an investor-friendly country and see growing potential.

"The Polish and Belarusian economies are very well adapted to manufacturing and trade collaboration. They complement one another not compete with one another. They are predestined to make use of their two great advantages: location and neighbourhood," says Mr Zdunowski.

He adds that the Great Stone Industrial Park is still at an initial stage of development but it already offers great opportunities and Poland and Belarus should make use of all the opportunities to develop their trade and investment.

In 2016, the bilateral trade between the two countries reached $2.5 billion. Poland is now the country's third biggest trade partner and ninth foreign investor and there's room for more, especially now, that Belarus' economy is growing again in 2017.

"Belarus is now ranked fourth across the globe among the countries, which have introduced significant reforms. Within the past ten years, Belarus has climbed up the Doing Business ranking by 92 notches. Significant improvements have been made, such as business start-up conditions, registration of ownership, tax payments, foreign trade, and protection of minority investors, electricity supply connections and insolvency resolution processes," says Industrial Park's Mr Vaitekhovsky.

Francis Malige, Managing Director for Eastern Europe and the Caucasus for the European Bank for Reconstruction and Development (EBRD), also points to the benefits from access to the Customs Union market. "Belarus is a good place to invest and to re-export," he concludes.

CEE NPL resolutions – now and then

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Governments and regulators have realised that comprehensive strategies are needed to address the NPL problem.

When the global financial crisis reached Central and Eastern Europe (CEE), in the fall of 2008, the era of easy, foreign-financed credit came to an abrupt end and export markets collapsed. The region's economy was plunged into a deep recession. Problems with the quality of banks' assets emerged soon thereafter and non-performing loans (NPLs) rose sharply. Additionally, the high level of local debt denominated (predominantly) in Swiss francs made local borrowers extremely vulnerable and led to them sub-performing. The first wave of NPL resolutions was borne within the Vienna Initiative 1, which aimed to keep western European banks committed to the CEE market.

NPL resolution since then has evolved substantially and the strategies that are available for banks range from internal work-outs to direct sales. The structure of the transactions will depend on various factors, such as the transferability of the portfolio, the legal and regulatory frameworks (including those applicable to servicing capabilities and the enforcement of debt), the nature of the asset, financing the acquisition and the security of the exposure. The disposal of a portfolio of secured loans is preferably structured as an asset sale because, depending on the law governing the loans and/or collateral, the security interest could be transferred together with the loan. Unsecured exposures might be transferred by way of a share sale, when the entire entity holding the relevant portfolios is sold. We have seen recent examples of investors purchasing an entire bank (e.g., in Serbia) in order to overcome licensing and servicing impediments.

A purchaser's licensing requirements have proved to be a barrier to entry into certain markets (e.g., Hungary). Innovative structures recently used 'EU-passported' fronting banks to purchase the NPL portfolios and in turn the investors acquired synthetic exposures to the portfolio by way of sub-participations or risk participations. Where servicing of NPL portfolios is a licensed activity (e.g., in Greece), investors are setting up their local servicing companies prior to entering the market. Alternatively, purchasing of a servicing platform together with the NPL portfolio could optimise recovery or overcome licensing obstacles.

The securitisation of loan portfolios has proved a success in the Polish market. Under the Polish legal regime, the portfolios are acquired by special securitisation funds and, financing such acquisition, the funds issue hybrid instruments called investment certificates. A nuance to this structure exists when investors acquire shares to access the economic interest of the fund.

Governments and regulators have also realised that comprehensive strategies are needed to address the NPL problem. The national schemes of asset management companies (AMCs) have been adapted to deal with bad assets in, for example, Slovenia (DUTB) and Hungary (MARK). History has proven that AMCs can swiftly clean up NPLs from banks' balance sheets and resolve them over a longer period of time. AMCs, however, must be supported by debt enforcement frameworks in order to achieve better recoveries than the originating banks. The promotion of the early restructuring of viable companies and the easy liquidation of collateral and non-viable companies was the aim of the new pre-bankruptcy legislation in Croatia. Serbia, on the other hand, has changed its enforcement procedure as part of the Vienna Initiative 2, to reduce time and improve efficiencies.

In its most recent NPL resolution guidance, the European Central Bank (ECB) outlines measures, processes and best practices which banks should incorporate when tackling NPLs. The ECB expects banks to fully adhere to the guidance in line with the severity and scale of NPLs in their portfolios. The ECB does not stipulate quantitative targets to reduce NPLs; instead, it asks banks to devise a strategy that could include a range of policy options such as NPL work-outs, servicing, and portfolio sales.

Lastly, the advantages of the establishment of an AMC at European level were highlighted in the guidance as it would facilitate raising private funding in the market and offer a quick clean-up of banks' balance sheets. The evolution of CEE NPL resolution is continuing…

The Innovation District IT Park will help Lviv become CEE's IT hub

Written by
EVA KELLER

Published on April 2, 2017

With the fast-developing IT sector and most IT firms occupying refurbished Soviet-era office buildings, demand for modern office space is sky-rocketing, says **Volodymyr Zhenchak, CEO and the owner of Galereja Centre Ltd**, which has developed the Forum Lviv shopping centre, and **vice-chairman of the board of the shopping centre.** He spoke to Eva Keller about Innovation District IT Park, which his company is developing and looking for partners for.

(all photos: courtesy of the Innovation District IT Park)

Today, there are about 15,000 IT specialists in Lviv alone, or 60 in every 1,000 inhabitants. Over 80 per cent of companies intend to increase the number of their employees in Lviv, within the next three years. How does that translate to the available office space in the city?

Yes, indeed there are about 15 000 IT specialists in Lviv alone, and for the past three years the annual growth of employees in IT companies has reached around 20 per cent. We expect that by 2020 there will be at least 25 000 IT specialists which, of course, will mean additional office space will be needed in the city. The IT industry, together with tourism, agriculture and manufacturing, are the key sectors of our region.

So, what is the current office space situation?

Well, currently about 90 per cent of office space in Lviv is made up of old buildings from Soviet Union times that have been refurbished. The existing office space cannot meet the demands of IT companies, whose employees want to work in

modern, well-equipped offices. This seems like a big problem for IT companies.

The construction of the Innovation District IT Park in Lviv was announced in September 2016. What is the structure of the project and how will the IT Park respond to the demand for more office space?

Yes, the construction was announced in 2016, together with the IT Cluster, which unites 60 of the largest IT companies. For us, such a close cooperation with the IT Cluster is critically important in order to carry out the project in the best possible way, in a number of areas: the concept, the engineering support and the project's promotion amongst IT Cluster members.

We are planning to build 110,000 sq. m GLA (gross leasable area) of office space. So far, and within just a few months, we have signed letters of intent for 40,000 sq. m with four companies. We already see that the implementation of the entire project will not meet the demand of IT companies within the next five years, which means that even more space is desperately needed.

You have looked at a number of similar examples such as the High Tech Campus in Eindhoven, Inforpark and Graphisoft in Budapest. What are the key findings from there?

Of course, we have studied progressive experience all over the world. We understand what the main components are which should be included in this project and what will create additional value for it. We have hired Bose International Planning & Architecture to design the concept. The company has a lot of experience in creating urban development projects, including projects for big IT companies such as Amazon.

The project is supported by the City of Lviv and the Lviv IT Cluster. Are you looking for an equity partner and an international developer, now?

Yes, this project has won the wide support of the Lviv Municipality, the IT Cluster and the Ukrainian Government.

However, even though we already have experience in implementing commercial real estate projects, such as Metro, Auchan and our last project shopping centre Forum Lviv, which we completed in partnership with Multi Corporation with a loan from the European Bank for Reconstruction and Development (EBRD), we clearly understand that for such a complex project we, as local partner, need to have a powerful equity partner and international developer beside us.

At the moment we already have preliminary consent from a large European institutional bank which will finance 50 per cent of the project's value. We have also completed the process of land allocation, have started the process of design, and we are looking for the right partner.

So, what is the timeline of the project?

We expect to open Innovation District IT Park to its residents and clients in 2019.

How can the development of the project contribute to the growth of the IT sector in Lviv?

It is clear that the most important element of the IT Industry is the person. As for today, the salary of IT specialists in different companies in Lviv is at almost the same level and the average is €1,500. It is important therefore that we provide the necessary support to facilitate the growth of that sector.

Taking all that into account, we are creating the IT Park, which will accommodate a university for IT specialists, the Ukrainian Catholic University intends to be part of the IT Park and a hotel. We have already received proposals from hotel chains such as the Marriot, Accor and CarltonRezidor.

Lviv is a western gateway to Ukraine as it is located only about 50 km from the border with the European Union. The city also hosts Central and Eastern Europe's largest IT conference (IT Arena). We believe that with the support of the Lviv Municipality and the IT Park, Lviv will become the CEE region's IT hub.

Andrew Pavliv, CEO and co-founder of N-iX and Lviv IT Cluster Chairman

I am confident about the Innovation District IT Park. It is the biggest infrastructure project in Lviv, in the last decade, and we are happy to join it. The N-iX office will be located in this innovative district, in a few years' time. Why have we signed the contract? We believe that it will help us to develop more dynamically, since there a unique ecosystem for the successful development of business and technologies will be formed, there. Another reason is that we focus, not only on our own development, but also on the development of the IT industry in Lviv, which is why we want to contribute to building this ecosystem.

Oleh Denys, Executive Vice President at SoftServe

Our company values an innovative approach to work. This is the main reason why we have decided to join the Innovation District IT Park. We see respect for business partners, responsibility and most importantly - a global goal, here. This is proof of the development of Lviv's IT industry and provides IT companies with a quality space for generating new ideas and cooperation. We believe that working side by side with the talented people, who will work in the IT Park, will contribute to our development and, thanks to that synergy, we will be further investing in the development of IT in general.

Oleksandr Kachmar, ES Head, Ukraine at GlobalLogic

The IT industry in Lviv is growing annually by several thousands of new employees. This means that all these people need to be accommodated somewhere and provided with a comfortable space to work (IT companies are already renting 71 per cent of the office GLA in Lviv). This new space hast to promote personal and professional growth and to help IT professionals create innovations. The IT Park will be exactly this kind of space. This is why we did not hesitate for a second, when we heard about the possibility of renting offices there. This is where the development of the IT industry will soon be happening and I am confident that GlobalLogic will play an important role in this process.

Written by
EVA KELLER

Published on April 21, 2017

Ukraine's banking sector reconstruction brings asset sales and opportunities in equal measure

We are not at the end of the road but the process of mass insolvencies of banks is already coming to a logical conclusion.

Valeria Gontareva, governor of the National Bank of Ukraine (NBU), might be leaving office, but is often commended for the banking sector restructuring and consolidation that has been long-awaited by foreign investors.

"We are still not at the end of the road, but compared to where we were a few years ago, when we had about 200 banks, the situation is much better," Dmytro Sologub, deputy governor of the National Bank of Ukraine tells *Emerging Europe*. "Most of the banks which we wiped out from the market were already "dead", by 2008. Some of them had been haunted by imprudent practices for 20 years, and their supervision was also pretty negligible. So, there was simply no other choice because the longer you wait, the larger the problem you face," Mr Sologub adds.

Assets' value

"As a result, 87 banks out of Ukraine's total number of 184 banks were declared insolvent in 2014. The Deposit Guarantee Fund (DGF) paid out more than UAH 85 billion (€2.8 billion) of guaranteed deposits to individuals who had accounts in the failed banks and now the DGF's main task is to recover the funds from the asset disposals," says Kostyantyn Vorushylin, managing director at the DGF.

"The process of mass insolvencies of banks is already coming to a logical conclusion," says Andriy Dovbenko, Managing Partner at N&D Law Firm. "Most of these banks are in the process of liquidation, which is accompanied by the sale of their various assets, including real estate and production facilities. At present, the Fund is actively increasing the volume of sales of their assets, which is significantly affecting the level of supply of property, which belonged to banks being liquidated, on the market, as well as their receivables. Therefore, the sale of relevant assets is taking place in economically favourable circumstances," Mr Dovbenko adds.

"The total book value of assets under management is UAH 471 billion (€ 15.7 billion). 20 per cent are physical assets such as bank premises, equipment and real estate. 80 per cent is loans, 95 per cent of the loan book is non-performing and half of the loan book consists of 600 big corporates," says Mr Vorushylin.

"At the same time, the approximate market value of such assets is about UAH 97 billion. The Fund puts up bank assets worth UAH 4-8 billion a week, for sale," adds N&D's Mr Dovbenko.

"As an example, in early April, the DGF put the assets of 55 banks undergoing liquidation up for sale. The total face value of the assets made up to UAH 7.6 billion," says Tamara Savoshchenko, chairwoman of the Management Board at Ukrsotsbank.

"The main type of such assets (about 80 per cent of the total volume) is receivables, where a lot of various corporate borrowers use property as collateral. It should also be noted that legislative amendments came into force, in early 2017 that removed the restrictions about the list of persons who can take part in auctions for the sale of receivables. So from now on, any legal entity or individual, except for the borrowers and guarantors of the relevant loans, can acquire the receivables. Due to these changes, the market for receivables of insolvent banks is expected to become more active in the near future" says Mr Dovbenko.

Who can buy?

"These assets can be acquired by any investor, from Ukraine or outside, but of course Ukraine needs as many foreign investments as it can get, to boost economy growth," says Ukrsotsbank's Ms Savoshchenko.

Mr Dovbenko explains that the acquisition of the assets of banks that are being liquidated is attractive because of their cost, which is extremely profitable in an era of financial crisis. However it is associated with some risks. "Despite this, many large Ukrainian banks, as well as foreign investors have shown strong interest in acquiring such assets, since the benefits from their acquisition often remain attractive even in view of the possible risks," he adds.

"Should DGF decide to sell a bank to the investor, the latter should meet the requirements set by the Ukrainian law "On the deposit guarantee system of individuals" and should obtain the NBU's approval, under the pre-qualification procedure of persons who may be involved in insolvent banks withdrawal from the market, as well as their participation approval," says Andriy Pyshnyy, chairman of the Management Board at Oschadbank.

"Therefore, the DGF mainly sells the assets as the rights of claim under loan contracts and also as property entered in the books of insolvent banks. They are sold at public auction, at the price set by assets evaluation methodology for a bank that has

been rated as bad or insolvent, and approved by the DGF," Mr Pyshnyy explains.

Under the current legislation, the sale of the assets of insolvent banks takes place by auction in the form of electronic trade, the subject of which can be both the assets, which are of direct interest to the buyer, and the receivables, secured by collateral (mortgage) on the relevant assets. There are two main ways of acquiring the assets of troubled banks: buying them at auction or foreclosing on them (as collateral) as a result of acquiring the receivables. Both methods are associated with the certain risks that can significantly complicate potential buyers' procurement of assets of interest.

Risks involved

"The main risk after acquiring the assets is the complications involved in foreclosing on the collateral because of the weak legal framework and protection of creditors' rights. To mitigate the risk, international buyers of NPL's need to use their resources to hire legal counsel and other professionals who can seize the assets," says DGF's Mr Vorushylin.

"Most of assets' value has been lost through the exchange rate differences, bankruptcy of borrowers, insider loans, loans with pledges in the form of "junk" securities as well as assets that are located in the anti-terrorist operation zone (ATO) in Donbas and Crimea," says Oschadbank's Mr Pyshnyy.

Mr Dovbenko says that the main risk that comes from the acquisition of assets directly at the auction is that a former owner of the assets may launch a judicial appeal against such an auction. This encounter can last for years and the outcome is by no means certain. In addition, it can be accompanied by a temporary return of assets to the previous owner only to have them transferred to other legal entities, which can make the return of such assets impossible.

"The procurement of assets because of foreclosure on collateral (mortgage) after the acquisition of receivables is also associated with certain risks. For this reason, Ukrainian legislation provides for an option that is convenient to the buyer, of extra-judicial foreclosure on collateral (mortgage) property, in particular, by obtaining a property right to it. However, following the implementation of these procedures, the previous owners can initiate an eviction law suit," he adds.

The acquisition of assets in the form of real estate is often associated with the risks of such properties simultaneously holding several mortgages or there are problems with the technical documentation (unauthorised extensions, unauthorised renovations) that require detailed research prior to the acquisition of such a property. In the case of acquiring an asset in the form of the corporate rights of a company, there is a risk of concealment of the company's real financial condition from the buyer, including arrears to third parties and budgets of various levels, which can cause the transaction to be accompanied by an audit of the enterprise being acquired.

The faster the better

Mr Vorushylin says the DGF advocates fast and transparent asset sales. "The main task is to sell the asset at the highest possible price for the benefit of the creditors in the failed bank. Anyone, with the exception of the original borrowing entity and the guarantee, can buy assets, including the NPL," he adds.

"An overall restructuring of the banking sector should be also used to foster the development of broader capital markets," concludes Gunter Deuber, Head of Economic, Fixed Income and FX Research at Raiffeisen Bank International (RBI) AG.

Written by
ANDREW WROBEL

Published on April 21, 2017

The Bucharest Stock Exchange has started the year on a promising note

Romania is now perceived as one of the most dynamic capital markets in the region.

In the first quarter of 2017, the value of transactions on the regulated market of the Bucharest Stock Exchange (BVB) climbed to a six-year high and reached €530 million while the number of transactions and traded volumes climbed to a seven-year high. **Ludwik Sobolewski, CEO of the BVB**, spoke to Andrew Wrobel, about the effects that could positively influence the country once it gains emerging market status, and the increased interest shown by private companies to be listed on the stock exchange.

The last two quarters seem to be very promising for the Bucharest Stock Exchange.

Indeed, the first quarter was very good but it started at the end of last year. First of all, in September 2016, Romania was put on the so called "watch list" for emerging market status by FTSE Russell, because of the progress it has made on modernising the capital market. Romania currently has the status of a frontier market and we would like to be upgraded to be among the emerging markets.

Secondly, we witnessed a very big transaction on the market: one of the largest companies, listed in Bucharest, sold a significant stake in OMV Petrom, another big company that is listed on the exchange. The market showed a good appetite and good strength, and this transaction was completed within a couple of hours, with a value of around €150 million.

Finally in December, we had an IPO of MedLife, a company operating in the healthcare sector. The value of the transaction was €50 million and it was the largest ever IPO of a private company (non-privatisation linked to) in the Romanian stock market. All of these events showed that the market is really evolving in a very good direction. We had rather better liquidity at the end of 2016 and it has continued throughout January, February and March. When we counted the number of transactions and the value traded, we saw that this is the best quarter we have had for the last six or seven years.

A big challenge for the Romanian capital market has always been characterised by the assets list which is undervalued. So, we are very happy to see that during these last three months, prices are going up and it has nothing to do with a superficial euphoria. It looks like a process with a certain thriving activity. It turned out that, when we look at index performances, Bucharest is the best in the entire region and one of the best in Europe. This is also partly because in 2015 and in 2016 we had the highest dividend yield in the world.

Let's briefly circle back to the upgrade to emerging capital market status. What would this upgrade entail?

We will have larger flows of capital investing in Romanian stocks, equities and also other instruments. This is taking into consideration that fact that the size of the firms that invest globally in emerging markets is much larger than the size of the firms which specialise in frontier markets. The emerging market status help us to be better perceived than a frontier one, where the level of risk commonly associated with this type of market is higher. But it will also be translated into larger flows and we think that this will provoke a chain reaction, allowing us to have get flows coming from all sources, domestic and from abroad.

Then, it will incentivise more retail investors. They will be more willing to invest money because they will see the market growing, with growing prices and an increase of new companies arriving to the market. Besides, in Romania we have pension funds and investment funds. These two types of institutional investors, would also feel a lot safer if the market becomes greater. There was always a challenge here, because, according to the MSCI's requirements, a market which wants to be an emerging market must have at least three companies that fulfil very demanding criteria related to the market capitalisation and the value of free float and liquidity.

At the beginning of February Romania began to have such companies thanks to the improved turn over. So, we now have these three required companies, which is also something we have never had before. We are also expecting a large IPO, probably to be launched end of April, of a private company, which will be much bigger than the MedLife one. Later, chances are that we will at last see a big state-owned company going public. I am talking about Hidroelectrica which is currently the largest Romanian company. So, there is a very serious chance that we will have even more than the three required companies to gain emerging market status, by end of this year.


Ludwik Sobolewski (courtesy of BVB)

Do you think these two IPOs, the one that happened in December and the upcoming one, can help to increase the interest of private companies in Romania, in being listed on the stock exchange, in order to raise the capital on the market?

Yes, this is exactly the effect we expected to be created after this IPO in December. Apart from these, we also know about at least two or three small or medium sized private companies that are preparing IPOs. They are much smaller, but still they decided to go public to raise funds. It will not have a very meaningful impact on the overall condition of the market, but this is very symptomatic because it shows a new culture. Of course, we at the Bucharest Stock Exchange are trying to build up this equities' culture through different promotions, education and so on. For instance, very recently we launched a project which is called 'Made in Romania'.

We invited companies to participate in a very developed programme that is aimed at education, training and coaching and was about how the capital market could be used for them, by them and for their development. It is structured as a competition with the objective of having 15 qualified companies. In the first stage, we had 166 applications that were submitted by small and medium sized companies, and by larger ones, as well. Then we chose 16 of them. But it is significant to see that 166 companies reacted to our initiative, which was thanks to a growing awareness, an activist culture and also to the example given by MedLife.

Romania is now perceived as one of the most dynamic capital markets in the region. I would even be tempted to say that it is perhaps the most dynamic market in the entire region, because everyone knows that there are some companies that debuted on the exchange, which is, apart from Poland, something that is virtually unknown in other countries in the region.

What is the impact of pension funds on the development of the capital market in Romania? You have experience from Poland, where the funds played an important role.

Pension funds are solidly established in Romania and the assets are growing. They have quite a solid financing because five per cent of salaries go into the fund. Basically it is different because they have now around €8 billion under management. Hence, the scale of assets this industry handles is much smaller in Romania, than it was and still is in Poland.

There is a significant difference as regards investment funds.

This is because for many years, in Poland, the money from investment funds was invested locally in domestic instruments and, increasingly, in equities. In Romania, only a small fraction of the assets are invested in equities and shares; literally only around five per cent of the total funds. The rest is invested in cash market instruments and in bonds. The second difference is that even this five per cent is mostly invested abroad, not in Romania. But I am now seeing changes; it is becoming a time when fund managers and clients will be convinced that there are many opportunities in Romania.

What is your development strategy right now? How do you see the stock exchange developing in the next couple of years?

The number one challenge is to do everything we can to accelerate the process of getting Romania an emerging market status. Another challenge is to continue current projects and efforts that are aimed at involving retail investors.

I venture that the set of projects that we have been running for the last two years is probably the most comprehensive programme in the domain of financial education in all of Europe. It is strategically important for us, because we want to have more retail investors.

We want Romania to resemble Poland and we, in Poland, have always had a very important group of individual investors. Unfortunately, the market at the moment is mainly focused on shares and debt instruments, or on bonds. We also have a clear goal, to start with derivative products. As a result, Romanian capital market will provide investors with additional opportunities, and when it happens, we will be able to say that the market is much more refined, is fully fledged.

Legal reforms are improving the existing problematic situation in the Ukrainian agro market

ANDRIY DOVBENKO
Managing Partner at N&D Law Firm

Published on April 12, 2017

State enterprises hold approximately 0.5 million ha of agricultural land, which may be of potential interest to investors.

The agricultural market is currently one of the most dynamic and profitable in Ukraine, providing 12 per cent of the national GDP. The country is also one of the leading producers and exporters of agricultural products in the world. Considering the latest developments in the agricultural sector (including legal reforms) it seems to be the right time for foreign investors to enter the agro market.

Currently, most of the agro producers lease their agricultural land rather than own it (a moratorium on the sale-purchase of agricultural land has existed in Ukraine from 2002). Although long-term lease agreements are allowed (up to 50 years), leasehold does not provide a sufficient comfort level, in the view of many foreign investors. The draft law of Ukraine "On Agricultural Land Circulation" is about to be passed (expected at the end of May 2017) and it will allow the sale-purchase of agricultural land, by Ukrainian individuals, from 2018 and by Ukrainian companies (including owned by foreign shareholders) from 2020.

When one plans to purchase or establish an agricultural enterprise in Ukraine, it is necessary to consider not only the target company itself but also the infrastructure that is required for storage, processing and transportation, i.e. connecting links to the railway, storage capacities, silos and or grain terminals etc. The last few years have demonstrated that there are some problems with railway transportation because of the lack, and condition, of hoppers. Therefore, it is planned to renew the hoppers and to purchase new ones so as to ensure the prompt transportation of agricultural products all over Ukraine. Considering the above, it is also recommended to make a preliminary estimation of the costs involved in the probable construction or modernisation of a silo or grain terminal.

When acquiring an agricultural business, you should consider the risks that are common in this sector: risks related to land lease (premature termination of land lease agreements / acknowledgement of land lease agreements as invalid) and assets (risks related to the history of assets acquisition, namely acquisition from the state). Due diligence should be paid to tax risks, in particular those related to VAT accrual and payment, including VAT credit. Considering this, it is strongly recommended that potential investors hire local advisors to carry out the due diligence, covering land/other assets, as well as taxes, in order to avoid the risks and to stay on the safe side.

The deal shall be structured based upon the results of the due diligence and subject to considerations of the BEPS regulations, in as far as Ukraine joined an Inclusive Framework for BEPS implementation, starting from 1 January 2017.

When structuring a deal, you should be careful to pay attention to compliance with antitrust requirements. In general, the purchase of 25 per cent or more in a Ukrainian company is considered as a concentration which shall require a permit from the Antimonopoly Committee of Ukraine (AMCU), if the financial thresholds are exceeded. In 2016, the respective thresholds were increased but are still relatively low. The permit is granted by the AMCU within 45 days (25 days within the simplified procedure) from the date when filing is completed. The establishment of a company in Ukraine may also require an AMCU permit if the company is being established jointly with either Ukrainian or foreign partners.

Resolution of disputes should also be one of the key considerations. When structuring a deal, it is always better to arrange for an arbitration clause to be included, so as to be able to submit any disputes that crop up to either one of international arbitrations or the International Commercial Arbitration Court at the Ukrainian Chamber of Commerce and Industry (ICAC). This is definitely more effective than seeking dispute resolution in court — over 75 per cent of cases are considered by ICAC within three months.

One should also note that agricultural enterprises are subject to the general taxation system; no tax benefits are applied (a special VAT-regime for agricultural companies was cancelled from 2017 onwards). However, some agricultural enterprises are entitled to state subsidies, but actually, this scheme is not yet working. Please note that the general income tax in Ukraine is 18 per cent and VAT is 20 per cent (0 per cent for export operations).

Currently, there are certain currency limitations in Ukraine: namely, companies must sell 50 per cent of their currency earnings. It is prohibited to transfer currency out of Ukraine in order to pay dividends to foreign shareholders etc. The good news is the National Bank of Ukraine is making progress on the elimination of such temporary limitations.

Ukraine is working out the issues concerning the privatisation of enterprises in different sectors, including agriculture. Currently, state enterprises hold approximately 0.5 million ha of agricultural land, which may be of potential interest to investors. The existing legal procedures are not that favourable, however, and the State Property Fund of Ukraine, along with the other state authorities, is developing new laws to make privatisation transparent, easy and beneficial for both the state and the investor. A new law on privatisation is to be adopted by the end of August 2017.

Summarising the above, it should be noted that we still have some problems, including legal gaps, ambiguity and overregulation. However, Ukraine is undergoing a period of active legal reforms to improve this situation. This is demonstrated by the envisioned cancellation of the moratorium on sale-purchase of agricultural land, the elimination of currency restrictions and the improvement of corporate governance etc. Moreover, in recent years Ukraine has also improved its position in the Doing Business ranking and is moving towards strengthening the national economy and attracting foreign investments.

Written by
JERRY CAMERON

Published on April 10, 2017

Unlocking Cyprus' investment potential and improving the business environment are among the main priorities of the Government, says **Harris Georgiades, Minister of Finance for Cyprus**. He spoke to Jerry Cameron about the country's economic performance, prospects for future growth and the sectors Cyprus plans on developing.

The 2017 EBRD Annual Meeting and Business Forum is taking place in Cyprus. How can the conference help the island both politically and economically?

First of all, let me say, that we are truly delighted that this year's EBRD Annual Meeting will take place in Cyprus. Cyprus is a founding member of the EBRD and we are looking forward to the opportunity to host this important event.

The Board of Governors of the EBRD's decision to start operations in Cyprus, made in Warsaw in May 2014, has contributed significantly to the recovery of our economy. The EBRD's activities have had a direct impact through investment, in the range of €220 million, but have also provided a very important signal to private investors about the prospects of the country. For this, we are grateful.

The EBRD's annual meeting is also a unique opportunity for us to demonstrate that Cyprus presents an attractive, safe and stable jurisdiction, which has achieved a remarkable economic recovery and which now offers excellent business and investment opportunities across the sectors. We will have the opportunity to showcase this to the representatives of 67 shareholder countries and up to 2,000 participants from governments, businesses, civil society and the media.

Let's briefly speak about the economy. The country's indicators, at the end of 2016, looked positive. How do you see the prospects for the Cypriot economy in 2017 and 2018?

The year 2016 was crucial for Cyprus, as we successfully completed the IMF/ESM assistance programme.

Our exit from the support programme came hand in hand with the strong recovery of the economy. Let me remind you that in 2013, we were facing a severe recession of six per cent. By 2016, we had achieved one of the highest growth rates

Finance Minister: Cyprus's restored business environment offers investment opportunities

Cyprus enjoys a restored reputation and this is a result of the determined combined efforts of the government and industry over the last few years.

in the EU, approaching three per cent. This growth was not fuelled by excessive deficit spending or credit expansion, but rather was a result of the strong performance of the key productive sectors of the economy, especially tourism as well as shipping and business services. Unemployment has started to decline, nevertheless, we acknowledge that at 12.9 per cent, it is still high.

The banking sector has stabilised and healed to a significant extent, though challenges still remain. We have also seen significant investment, either through government initiatives or through the private sector. Rating agencies have acknowledged these positive developments, which has led to multiple upgrades of the sovereign's credit rating, and has allowed Cyprus to access international capital markets with improved borrowing conditions.

The outlook for 2017 and 2018 remains very positive, with growth expectations in excess of 2.5 per cent of the GDP. Significant private and public investment is now in the pipeline, which will further support growth and job creation. I would also like to point out that there is a significant upside, over the medium to long-term, from the exploration of new gas fields in the Cyprus Exclusive Economic Zone.

What are the prospects for the budget, fiscal balance and public debt?

Despite the challenging economic environment, fiscal targets have been achieved with considerable margins. Since 2014 we have been operating with an essentially balanced budget. In 2016, we achieved a positive balance of 0.4 per cent and a primary surplus of three per cent, which is the highest in the EU.

We also expect 2017 to be yet another year with an essentially balanced budget. The combination of fiscal discipline and real economic growth has been the hallmark of our economic policy and it is one that has delivered tangible results, demonstrating that the "growth versus austerity" dilemma is not warranted.

This robust fiscal performance has undoubtedly supported debt sustainability. According to the Commission Winter forecast, public debt is expected to drop below 100 per cent of the GDP

Harris Georgiades (courtesy of the Ministry of Finance)

by 2018. We have accumulated significant cash reserves in order to pre-finance 2017 and early 2018, which has inevitably inflated the level of public debt.

The government has successfully implemented reforms to the pension system and the financial sector. What improvements are you planning in the short and long-term?

Indeed, the ambitious reforms of the financial sector and the welfare system, which have been implemented during the past few years, stand out. We also endorsed a significant reform of the tax administration and of public financial management. Most recently, the privatisation of the Port of Limassol has been completed; the largest of the island.

Even though we are already in the final months of our administration, we are maintaining the reform momentum. Our reform agenda includes the reform of local administration; of the health system; the establishment of a Sovereign Wealth Fund, which will manage future Natural Gas revenues on the basis of international best practices and also a reform of the occupational and private pensions' framework, which will also see a strengthening and consolidation of the supervision of insurance companies and occupational pension retirement funds.

Additional reforms are envisaged, in general, regarding the judicial system in Cyprus, which are expected to facilitate the business environment.

Another economic sector we are aiming to develop is the funds' industry in Cyprus. We have worked methodically in the past few years, to introduce a modern legal framework for collective investment schemes, and the last pieces of this legislative reform will be taking place within the next few months. We believe such a framework will provide more specialisation and added value to the financial services' industry, but it will also provide an alternative way to finance businesses; a much needed instrument.

With a GDP per capita of almost €20,000, Cypriots seem to be relatively affluent. How do you think their economic situation is improving?

The per capita income in Cyprus could be considered satisfactory enough but in relative terms, and compared with the EU average, our per capita income stands at around 82 per cent of EU28. This percentage is lower when compared to the pre-crisis levels, where our per capita income was above 90 per cent of the EU average. We are aiming for real convergence with the EU average, through higher real growth rates.

Cyprus has transformed itself from being considered an offshore tax haven, with a 4.25 per cent corporate tax rate for grey-area businesses to a unique EU jurisdiction with a standardised tax rate of 12.5 per cent — still the lowest tax rate in the EU. Does this help attract more business?

Yes, the corporate tax is still competitive at 12.5 per cent. Overall, we are aiming for a stable, attractive, transparent and effective tax regime, applied over a broad tax base. This framework is conducive for business and investment. In Cyprus the effective tax rate for business or individuals is around 20 per cent, which is not the lowest in Europe or the world, but is attractive enough. It is worth noting that we have fully eliminated a budget deficit which was persistently at a very high five-six per cent of the GDP, without raising taxes, but through a consolidation of public expenditure. Tax stability is of paramount importance.

Cyprus has also been implementing a comprehensive legal framework to ensure, inter alia, the avoidance of unfair competition in tax matters, guaranteeing transparency and combating tax evasion and avoidance, in accordance with the Global and EU initiatives (namely the BEPS project, the Global Forum on tax transparency and Exchange of Information standards and EU related directives). These initiatives aim to establish confidence in the business environment and give an impetus to entities, in order to establish a real physical presence and economic activity. For Cyprus, a blend of elements such as a generally favourable tax regime, an advanced level of business services provided and a well-regulated and transparent environment will serve as a conduit to elevate Cyprus as a business and financial centre, and hence to attract more business, for a positive impact in the real economy.

Attracting FDI is not only about tax. If we look at the World Bank's Doing Business 2017, the country is ranked 45th, four notches lower than in 2016. There are elements which have deteriorated significantly by 20 notches compared to 2016, such as getting credit. How would you like to improve the business climate?

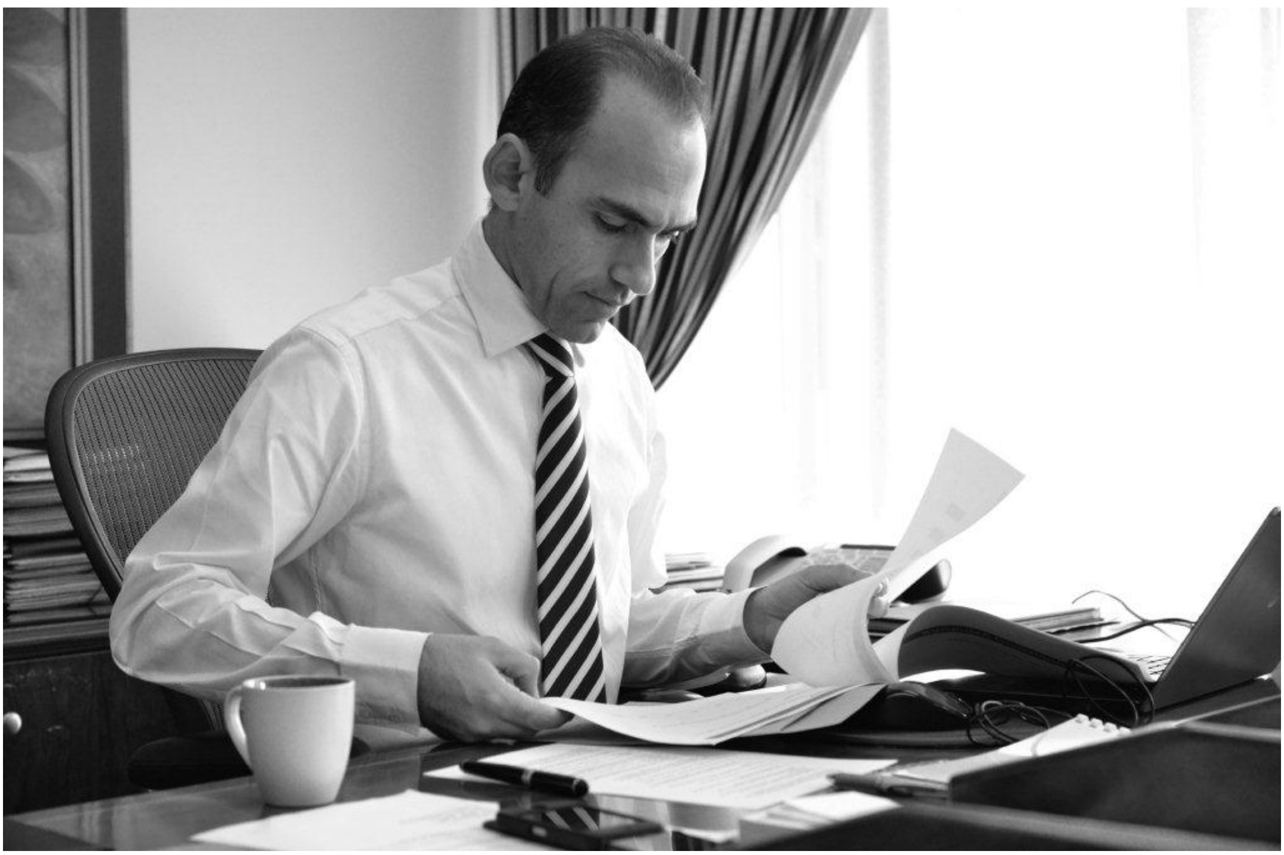
Monitoring Cyprus' performance in relation to international benchmarks, such as the Doing Business index, is an important instrument for steering actions towards a more attractive business environment. Unlocking the country's investment potential and improving the business environment, are among the main priorities of the Government. In order to achieve this, the Action Plan for Growth was approved by the Council of Ministers in February 2015, and updated in November 2016. It includes around 70 targeted actions with specific timeframes for enhancing the competitiveness of our economy.

Some of these actions include the creation of a Department for Growth and Competitiveness, headed by a deputy minister, the strengthening of the entrepreneurial ecosystem and the conducting of a competitiveness benchmarking exercise, so as to provide the necessary analysis for corrective actions.

Do you expect FDI to increase, in 2017 and 2018?

Cyprus is currently offering excellent investment opportunities across all sectors. Essentially, Cyprus enjoys a restored reputation and this is a result of the determined combined efforts of the government and industry over the last few years. Working together, I believe we have established a stable, safe, pro-business environment. Actually, the creation of an environment that facilitates investments, mainly through the simplification of procedures and developing an effective, stable and transparent regulatory framework is a top priority for the Government. This is exactly what investors need: stability, predictability and a pro-business economic environment. This is exactly what we have established.

This is reflected by the significant inward FDI that has been observed recently, such as in case of Limassol Port and the integrated casino resort (which is expected to be the biggest in Europe). Additional major investments include Marinas, the pharmaceuticals industry, renewable energy products, retail, hotels and real-estate.



Harris Georgiades (courtesy of the Ministry of Finance)

Cyprus: the green economy shows the way

LIBOR KRKOŠKA

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Published on March 31, 2017

The green economy in Cyprus has great potential. The level of solar irradiance in Cyprus is one of the highest in Europe. At the same time, the island is highly dependent on imported sources of energy, principally highly polluting oil and oil products: The energy system is isolated with no interconnections with neighbouring countries and renewables still account for just above five per cent of energy supply.

All of this means that a large variety of projects, related not just to renewable power generation but also to energy efficiency and energy security, are currently under consideration by domestic and foreign investors. They would not only be highly desirable, but today they are also financially viable.

Solar projects have top priority, not least because peak electricity demand coincides with peak production. However, the expansion of renewable power generation, both through small-scale dispersed photovoltaic production as well as in larger facilities, will also require the development of the recently discovered offshore natural gas reserves in order to support energy security through diversification.

High irradiance, the sharply falling prices of solar energy panels and energy security factors all mean that solar power generation in Cyprus could easily exceed ten per cent of the total power generation within a few years. The total renewable power production could reach 15 per cent of the total with the right set of policies. The recently amended legal and regulatory framework will be of critical importance to supporting renewable energy investments. The further liberalisation of the electricity sector, the unbundling of state-owned power company,

Many companies are still recovering from the economic crisis and need to focus not only on expansion of their export markets but also on their costs.

the upgrade of the power distribution network and significant investments in energy storage are all necessary steps to facilitating investment opportunities in order to achieve the renewable energy targets.

The EBRD has supported the expansion of renewable power generation in Cyprus by financing the construction of five solar energy power plants in 2016, including the single largest solar energy power plant on the island, to date. The completion of these investments will lead to an increase in total solar power generation of about 20 per cent.

Furthermore, the success will help attract more interest from other, private investors. However, while solar power generation in Cyprus continues to grow, investments may be constrained in the short to medium-term by a lack of cash-flow based financing.

Supporting increased renewable energy generation is just one aspect of the EBRD's aim to boost the sustainable use of resources in Cyprus. Many companies and households would benefit from a more efficient use of energy. Some other ways the EBRD can support investments in a green economy are: advisory services for small and medium-sized enterprises, as well as potential sustainable energy credit lines for businesses and households.

Such investments are highly desirable in Cyprus where many companies are still recovering from the economic crisis and need to focus not only on expansion of their export markets but also on their costs. Energy costs can be tackled relatively easily and this can result in significant savings with a very short payback period. The EBRD is actively assisting such efforts with tailored energy audits, provided by our Advisory for Small Businesses services.

In addition, the EBRD has also organised and participated in seminars and workshops to promote the green economy. The bank is working closely with the relevant authorities in Cyprus, and at European Union level, as well as with other stakeholders including academia, private companies and other experts in the field. Thanks to Aphrodite, Cyprus is also famous as the "Island of Love". It is the EBRD's ambition that in the future the island will also be known as 'green'.

The Cyprus dispute – recognising the changing rules of the conflict

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Published on
March 30, 2017

The consolidation of power, through regional alliances, increases the deterrence power of the Cypriot Republic by challenging Turkey's capacity to interfere in the south-eastern Mediterranean

Despite high hopes, negotiations between Cypriots of Greek and Turkish ethnicity came to an abrupt halt, earlier this year, when the Parliament in Cyprus passed a law to commemorate the 1950 Enosis referendum on political integration with Greece. This represents only the most recent occurrence of an issue which, while not sufficient to wreck the talks, still drives delegates away from the negotiating table.

The Cypriot government's recent decision not to block this legislation, which would almost certainly derail negotiations towards a durable peace settlement, showcases the apathy towards resolving the dispute between the two communities. Similarly weak commitment was behind the decision of the Turkish Republic of North Cyprus (TRNC) to draw a red line on the institutionalisation of commemorating Enosis. For a number of years now, the Turkish Cypriot community celebrates "Peace and Freedom Day" every July, which is anathema to Greek Cypriots, given its reference to the 1974 Turkish invasion.

The waning determination to surpass recent obstacles points to an increasing inability, or unwillingness, of the parties to share the same understanding as to the rules that govern the conflict. This shift is largely based on a series of events in the region that heightened TRNC's dependency on Turkey and have allowed the Republic of Cyprus to significantly consolidate their power.

Often, both policy-makers and international negotiators treat the Cyprus conflict as an "identity conflict." This classification overemphasises the disagreement of the belligerents over abstract cultural or historical dynamics, limiting the use of traditional negotiation tactics in the resolution of the conflict. Such a classification, although not completely erroneous, fails to explain the respective strategies, as well as the recent collapse of negotiations. Instead, in order to better understand the nature of the current intractability of the conflict, one could take four distinct events, that have shaped the terms of interaction between the Republic of Cyprus and the TRNC, under consideration.

Turkey partially offsets the isolation costs incurred by the TRNC from its actions, resulting in the TRNC viewing negotiations as a game of chicken with reduced stalemate costs. In particular, the UN sanctioned a trade embargo on the TRNC following its formation. The ensuing protracted isolation has forced the TRNC to be totally (economic and security) dependent on Turkey, which accounts for the perfect alignment of the community with Ankara. In this respect, the TRNC adopts the aims of Turkey, which is a revisionist state with claims on the south-eastern Mediterranean and its natural resources.

EU membership, which was achieved in 2004, upgraded the security profile of the Republic of Cyprus. This also brought significant economic benefits as the country became more integrated into the world economy through its adoption of the single European currency.

The Republic of Cyprus' negotiating position is strengthened by the irreversibility of the imposed isolation on the TRNC. The international community has repeatedly affirmed its condemnation of the 1974 Turkish invasion. Most notably, as recently as 2014, the European Court of Human Rights imposed a €90 million fine on Turkey for damages incurred during the invasion.

The consolidation of power, through regional alliances, increases the deterrence power of the Cypriot Republic by challenging Turkey's capacity to interfere in the south-eastern Mediterranean. Since 2014, the Republic of Cyprus has repeatedly capitalised on recent gas discoveries in order to foster closer economic and military cooperation with two regional powers: Israel and Egypt.

The above four developments motivate Greek Cypriots to view negotiations in a substantially different frame than the TRNC and Turkey. The Republic of Cyprus has little reason to be averse to a protracted stalemate; a position further supported by a weak domestic demand for reunification. As outlined by the 2015 findings, presented by the UN's Social Cohesion and Reconciliation Index, perceptions about reconciliation, in the Republic of Cyprus, are primarily driven by the fears that are associated with the worsening growth impetus and employment status. Moreover, Greek Cypriots are decidedly sceptic when it comes to sharing the right to govern, and they question the efficacy of such a regime, to mutually advance the interests of both communities.

In negotiations, it is essential for both parties to converge towards the same understanding of the conflict. The most recent breakdown in negotiations largely reflects Turkey and the TRNC's inability to recognise the rules that govern the Cyprus dispute today. This leads the TRNC delegation to push for a settlement that offers insufficient incentives to the Cypriot government to incur the costs of re-unification. The Cypriot government's decision, to abstain from the recent vote on the "Enosis law", only attests to the geostrategic shift in the region, which is further underpinned by the island's rising economic prosperity.

That is to say, the integration of the two communities into one state, with one nationality and two federations will become increasingly unattainable for as long as carrots remain out of season in Ankara.

Divided economy that may unite (or draw apart)

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Published on March 14, 2017

Northern Cyprus experiences the same economic consequences as unstable countries usually do.

Economy is a factor that may foster Cyprus' reunification, yet without a strong political will this issue may draw Greek and Turkish Cypriots further apart.

Although we tend to look at the Cyprus problem mainly from a political point of view, it is worth noting that the island's economy is also deeply divided. As a result of Cyprus' more than 40-year-long division, the country's economy is, in fact, composed of two relatively independent and disengaged economies.

The problem has become especially obvious since 2004, when the Republic of Cyprus joined the European Union. Since then it has been able to make full use of the various benefits that come with its membership. Thanks to that, it is now classified by the World Bank as a high-income country with a GDP that surpasses \$19 billion. This all happened in spite of the 2012-2013 financial crisis, which hit Southern Cyprus' economy heavily and which was followed by a recession that continued for three years (in 2011, on the eve of the crisis, GDP was around \$27 billion).

When it comes to economy the Turkish Republic of Northern Cyprus (TRPC) does not have so much luck. Its lack of recognition from the international community (TRPC is only recognised by Turkey) is a source of many barriers. Not only is Northern Cyprus not directly integrated with the global economy, but it also has huge problems in attracting foreign investors.

The fact that TRPC cannot be reached by direct flights from most countries is also a big hurdle. As a result, businessmen who want to get to the country need to travel through Turkey or the Republic of Cyprus. Obviously, a lack of direct flights is also a barrier to tourism; although the TRPC has recently been able to achieve modest success in this area (it is estimated that within the last decade, the tourism bed-capacity has grown by around 10,000 units).

All in all, Northern Cyprus experiences the same economic consequences as unstable countries usually do. Because of that the country's GDP reaches slightly above \$4 billion, and even though it is rising at a relatively high rate (the latest data shows four per cent growth), Turkish Cypriots' standard of living diverges sharply from that of Greek Cypriots'. Whereas in the north GDP per capita at nominal values stands at around 15,000 USD, in the south it surpasses 23,000 USD (according to TRPC's government and the International Monetary Fund respectively).

Given the above mentioned arguments, one might wonder why economy could be a factor that is fostering Cyprus' reunification. Problems may arise, especially from the fact that in these circumstances only one side of the table appears to benefit economically from peace negotiations.

Yet, this statement is only partially true. Maintaining the status quo may also bring huge long-term economic risks for Greek Cypriots. It may lead to a situation where the production of the two economies is similar and the countries would offer like services or products, provided at different costs; thus two economies would compete with each other. Obviously, this scenario is more favourable for the Turkish Cypriots whose cost of work is lower. It is worth noting that this economic competition is likely to result in a further strengthening of the island's division.

Various experts have been pointing out this risk for quite a long time, yet, for now, nothing has changed in this field. One reason for that may be a lack of political desire that still prevents both communities' leaders from finding common ground. Nevertheless, there is still hope that their attitudes will change before the economic problems become so dire that it will be impossible for Greek and Turkish Cypriots to forge a peaceful deal that will truly benefit both parties.

GRZEGORZ ZIELIŃSKI
Regional Director for Poland and the Baltics European Bank for Reconstruction and Development (EBRD)

Published on March 25, 2017

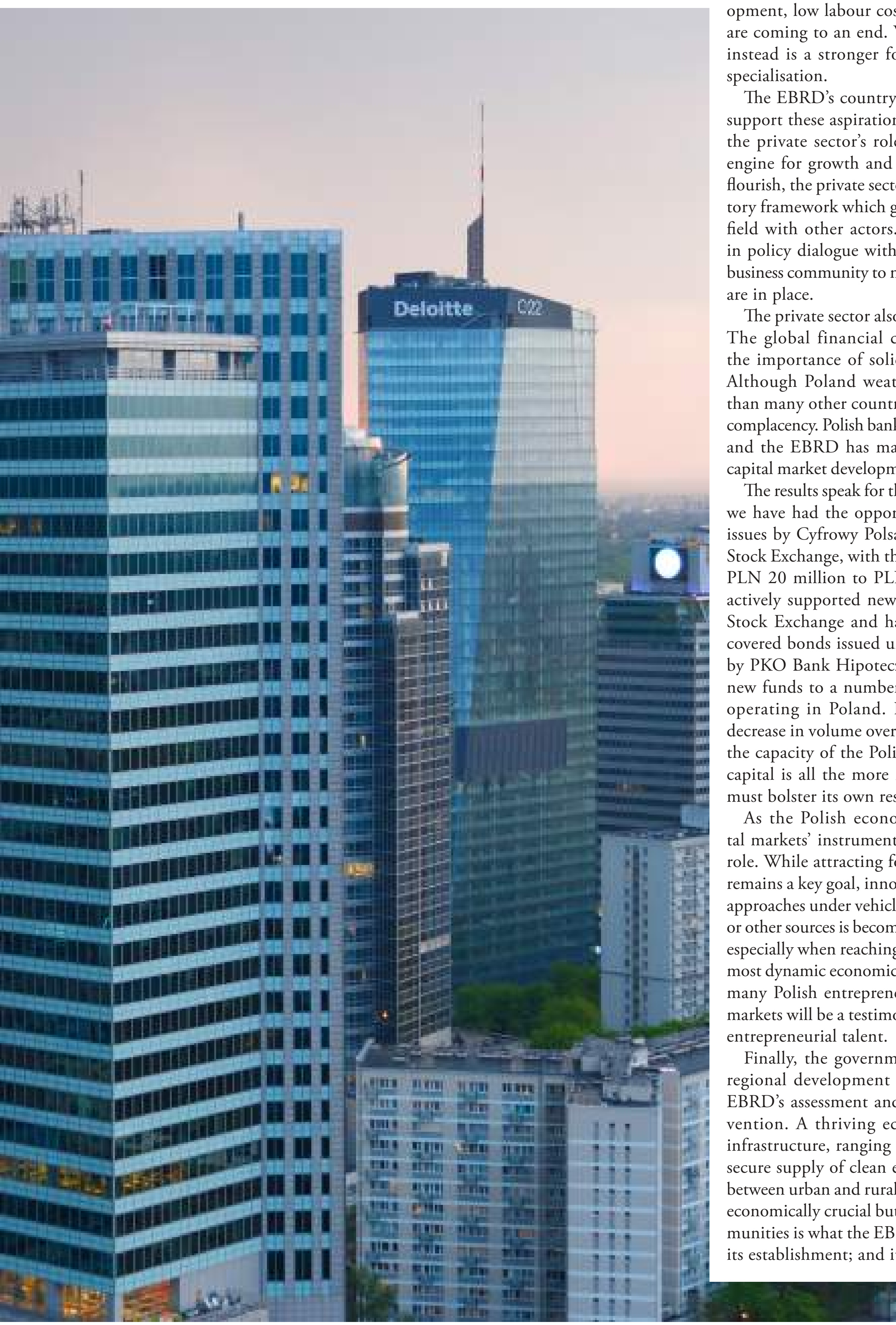
Poland government's development plan and the EBRD's role

Although Poland weathered the storm better than many other countries, there is no room for complacency.

Although Poland has been one of the best performing European economies for many years, the government wants the country to do even better. The sustainable development plan that was launched last year by Deputy Prime Minister, Mateusz Morawiecki, aims to make the economy "more dynamic". It is based on five pillars: reindustrialisation, development of innovative companies, capital for development, foreign expansion and sustainable social and regional development.

The EBRD has been investing in Poland since the bank's establishment in 1991. Not only did we sign our first ever project in Poland but the country has traditionally been one of our largest countries of investments. The progress it has made over the past 25 years has been remarkable, yet we share the view that today Poland is on the cusp of new challenges. The EBRD can still play a part in addressing those.

The government's plan rightly identifies one of its main goals as raising competitiveness. Poland has many good and successful companies, but too often their business model is based on simple products, sold at low prices. As the country is moving to the next stage of its economic devel-



opment, low labour costs as a source of growth are coming to an end. What the country needs instead is a stronger focus on innovation and specialisation.

The EBRD's country strategy for Poland can support these aspirations. Its goal is to enhance the private sector's role in the economy as an engine for growth and innovation. In order to flourish, the private sector needs the right regulatory framework which guarantees a level playing field with other actors. The EBRD is engaged in policy dialogue with the authorities and the business community to make sure such conditions are in place.

The private sector also needs access to finance. The global financial crisis has demonstrated the importance of solid local capital markets. Although Poland weathered the storm better than many other countries, there is no room for complacency. Polish banks have responded actively and the EBRD has made support of the local capital market development one of our priorities.

The results speak for themselves: In recent years we have had the opportunity to support bond issues by Cyfrowy Polsat, Orbis or the Warsaw Stock Exchange, with the amounts ranging from PLN 20 million to PLN 200 million. We also actively supported new listings on the Warsaw Stock Exchange and have invested in the first covered bonds issued under the new legislation by PKO Bank Hipoteczny. We also committed new funds to a number of private equity firms operating in Poland. Because EU funds will decrease in volume over the years, strengthening the capacity of the Polish economy to generate capital is all the more important. The country must bolster its own resources instead.

As the Polish economy evolves, new capital markets' instruments begin to play a bigger role. While attracting foreign direct investment remains a key goal, innovative solutions and new approaches under vehicles such as venture capital or other sources is becoming ever more important, especially when reaching out to the youngest and most dynamic economic actors. How successfully many Polish entrepreneurs compete in foreign markets will be a testimony to the country's huge entrepreneurial talent.

Finally, the government's goal of social and regional development is also in line with the EBRD's assessment and our capacity for intervention. A thriving economy needs a decent infrastructure, ranging from modern roads to a secure supply of clean energy. Bridging the gap between urban and rural development is not only economically crucial but reaching out to all communities is what the EBRD has been doing since its establishment; and it continues to do so.

Greener and more resilient: energy sector reforms in Serbia for the benefit of all

Modernising Serbia's energy system involves helping Serbia to create a functioning energy market.

When Serbia started excavating the first lignite mine in the Kolubara coal basin, and constructed the first lignite fired power plants, built with Soviet technology, in the 1950s, electrification was at the cutting edge of industrialisation and the development of the Yugoslav economy. The lignite mines in Kolubara were among the largest in Europe, producing 30 million tonnes of coal. Together with a second mining basin in Kostolac, these two lignite fields supplied the fuel for 55 per cent of Serbia's power generation capacity. In the 1970s and 1980s coal-fired power plants were built in Obrenovac, including the two huge units of the Nikola Tesla B power plant; built to supply the whole of Yugoslavia.

At the time that these lignite mines were excavated, and the power plants constructed, environmental standards were far below today's levels and global warming was completely unknown. Retrofitting and overhauls have reduced the environmental burden of emissions from these power plants, especially dust emissions which have been reduced by installing new filters. However, the legacy of the past has left Serbia with emissions from power plants that have had a real impact on the quality of life for the people living in the towns and villages near these power plants.

According to the European Environment Agency, Serbia (along with other Balkan countries) suffers from very high levels of particulate matter, associated with coal-fired power generation, that result in as many as 10,000 premature deaths per year.

The EBRD (together with other international financial institutions and donors) is helping Serbia to overcome this legacy through investment, reforms and improving energy efficiency in order to reduce the need for power in the first place.

One example is the work the EBRD began with Serbia's power utility EPS in 2001; firstly to stabilise and repair the power network after years of underinvestment and lack of maintenance. A second step was funding the purchase of smart meters which will improve energy efficiency in distribution while at the same time reducing power losses, including commercial losses from unpaid (and stolen) electricity.

Together with the German Development Bank, KfW, we funded a project in 2011, which helped EPS to reduce emissions and improve the efficiency of the Obrenovac power plants through a quality management system and the use of alternative fuel to supplement lignite.

Increasing the use of renewable energy is a key goal of the Serbian energy strategy, and helping Serbia to do this is an important part of the EBRD's work in the country. In 2011, the EBRD financed a project for a refurbishment and growth in capacity of a number of the small power plants of EPS, together with the construction of small

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new hydro units on existing water management dams.

The EBRD has also worked with the Serbian authorities to put policies and regulations in place that are needed to encourage private developers to build renewable energy projects, in particular wind, but also biomass and biogas. These are also prerequisites for EBRD's financing. In 2016, the Serbian government finalised amendments to Power Purchase Agreements, which should facilitate the financing of renewable energy investments.

This progress has already been translated into concrete projects: The first small windfarm is now up and running. The EBRD also financed its first biogas investments. 2017 should see the first major investments in non-hydro renewables as the Government licensed up to 500 MW of wind generation.

Modernising Serbia's energy system also involves helping Serbia to create a functioning energy market. This also includes putting policies and measures in place which improve energy efficiency and reduce cross subsidies. This is a particularly sensitive and difficult task, but it is vital that tariffs are fully cost reflective, while at the same time taking into account the needs of vulnerable consumers.

As part of the efforts to commercialise EPS, in 2015, EBRD provided funds for the restructuring of the company's debt, and — together with IMF and World Bank — agreed on a comprehensive programme of reforms to improve operational and energy efficiency as well as governance and transparency. At the same time, EPS is working on controlling costs and reducing losses and raising revenues through increased bill collection and tariff adjustments.

The EBRD is also working to make EPS more accountable to the citizens of Serbia. An action plan has been agreed that reinforces EPS' environmental and social policies, including its engagement with local communities. In January, the company agreed with the Environmental Protection Agency to monitor and report on emissions. All of these actions will make EPS more "open" and responsive.

What is ahead for the EBRD in 2017, and beyond? The bank will continue to work on new, renewable energy sources, particularly investment in wind power. We will also continue to support the EPS modernisation. The joint EBRD/EIB loan to purchase over 216,000 smart electricity meters (part of a programme to update 3.3 million meters in Serbia) should move ahead as soon as possible. These reforms are helping pave the road for a sustainable, secure and financially viable energy system, bringing significant benefits to the Serbian people.

IAN
BROWN
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Published on March 25, 2017

There is a lot of talent in Bosnia and Herzegovina and we want to see it prosper in the country for inclusive growth that benefits as many as possible.

Bosnia and Herzegovina is a country with great potential, but it also faces many challenges. With a population of 3.8 million it is a comparatively small country with a limited market capacity. This means that in order to prosper, the economy must succeed on external markets. Competitiveness and support for regional integration are therefore crucial for strengthening the resilience of the economy of Bosnia and Herzegovina.

The federal government took an important step towards this goal with the adoption of an ambitious "Reform Agenda" in 2015. This defines "rehabilitation and modernisation" of the economy as the key targets and aims to foster sustainable growth, create new jobs and to form a favourable and just social environment. The effort has been rewarded with a noticeable improvement in growth: for 2017 our economists expect three per cent growth as compared to only 1.1 per cent in 2014, the year before the current reform course started.

"Rehabilitation and modernisation" of the economy of Bosnia and Herzegovina can be built on three pillars. The country has a strong industrial tradition. It provides a skilled and well-educated workforce, often

Strengthening the resilience of the economy of Bosnia and Herzegovina

with work and life experience abroad which has equipped people with language skills and a high work ethic. In addition and thanks to an abundance of hydro power, the country has a strong potential to become a major producer and exporter of electricity.

The "Reform Agenda" has re-energised the economy, for example, by making the labour market more flexible. However, more needs to be done to lessen the burden on businesses and to improve the general climate for entrepreneurs. This includes the tax regime as much as administrative procedures. The repeatedly announced privatisation plans must finally be implemented, in order to generate growth and a dynamic economy.

More than 25 years of experience have provided us with ample evidence that the private sector is the main driver of economic progress. However, we also have to acknowledge the important role of the state, in the first place, as the framework under which economic development takes place. In our view, one of the main lessons of the transition process is that transition is not only about building markets but also about redesigning the state.

Modern markets rely on efficient state institutions. Market and state are not substitutes, they complement each other. Therefore, we should improve the quality of both state and market institutions. Hardly anywhere is this more valid – and timely – than in Bosnia and Herzegovina, with its complex constitutional design. While we recognise its importance and support its success, we also believe that it must not become an obstacle to economic progress.

In the past two years, the renewed reform commitment by Bosnia and Herzegovina has allowed the EBRD to significantly increase its investments, to €200 million each. With a total of €2 billion investments the country accounts for some 20 per cent of total EBRD investment in the Western Balkans. However, we are not resting on our laurels and we regard the coming period as crucial: this year a new country strategy is due and we have started our discussions with the authorities, businesses and other stakeholders.

Although this remains very much a work in progress it is not giving away any secrets when we state that support for the private sector will remain vital. There is a lot of talent in the country, and we want to see it prosper in the country for inclusive growth that benefits as many as possible. Combining investment with reform dialogue remains the way forward, and the EBRD is as committed as ever to supporting the success of Bosnia and Herzegovina.

Georgia on my mind – where beauty meets business

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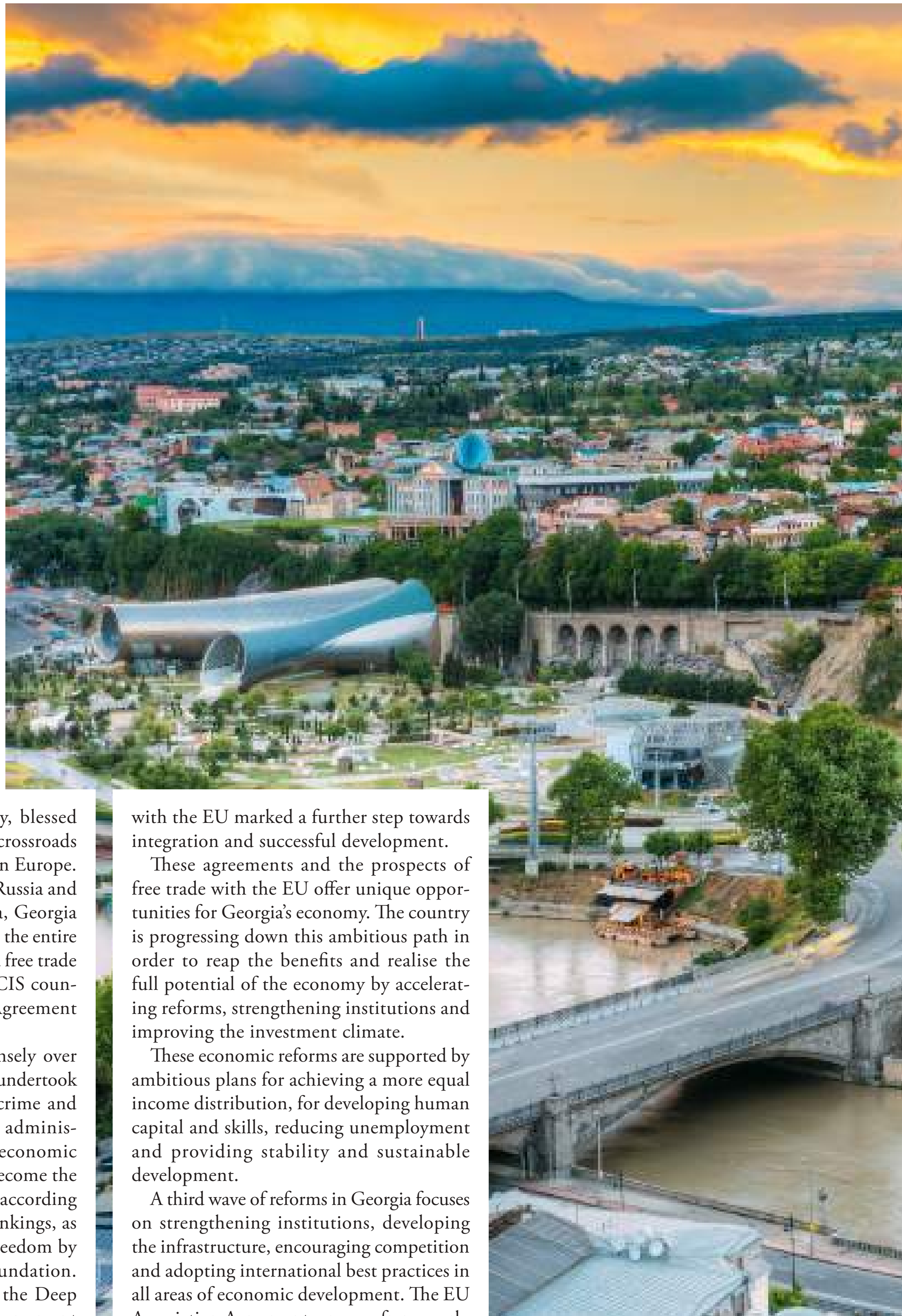
Published on April 21, 2017



Georgia has progressed immensely over the last two decades.

Georgia is a beautiful country, blessed with a favourable location at the crossroads between Western Asia and Eastern Europe. Bordering Armenia, Azerbaijan, Russia and Turkey and with access to the sea, Georgia has good transportation links with the entire region and beyond, and it enjoys a free trade agreement with Turkey and the CIS countries as well as an Association Agreement with the EU.

Georgia has progressed immensely over the last two decades. The country undertook significant changes to eradicate crime and corruption, to reform the state administration and to adopt a market economic model. As a result, Georgia has become the top reformer in the wider region, according to EBRD and the World Bank rankings, as well as the Index of Economic Freedom by the US think tank Heritage Foundation. The Association Agreement and the Deep and Comprehensive Free Trade Agreement with the EU marked a further step towards integration and successful development.

These agreements and the prospects of free trade with the EU offer unique opportunities for Georgia's economy. The country is progressing down this ambitious path in order to reap the benefits and realise the full potential of the economy by accelerating reforms, strengthening institutions and improving the investment climate.

These economic reforms are supported by ambitious plans for achieving a more equal income distribution, for developing human capital and skills, reducing unemployment and providing stability and sustainable development.

A third wave of reforms in Georgia focuses on strengthening institutions, developing the infrastructure, encouraging competition and adopting international best practices in all areas of economic development. The EU Association Agreement serves as framework,

roadmap and timeline for these structural reforms; the implementation will require persistence and determination, but the results will justify the effort.

The future of Georgia relies on strengthening its human capital, on adopting and embracing new technologies and on developing its technological standards. Georgia needs to make the most of its fertile land and improve its agricultural yields, to develop further the hospitality sector, nurture its small and medium-sized enterprises and to consolidate the development of essential sectors such as banking.

The EBRD plays a key role in the development of Georgia. We have invested more than €2.3 billion in the country since the start of operations 25 years ago. This represents one of the largest investments per capita in all the EBRD countries. We have successfully supported the development of the banking sector; the development of the renewable energy sector, with significant hydro investments and the growth of the private sector, while encouraging foreign investments. We have complemented our financial support with technical assistance in order to strengthen skills and with policy dialogue.

The EBRD's priorities in Georgia are developing the competitiveness of the private sector through innovation, enhancing value-add and convergence with DCFTA standards and deepening financial intermediation as well as developing local currency and capital markets. Another priority for the bank is expanding markets, through inter-regional connectivity; expanding Georgia's potential as a regional link, through a modernisation of the country's infrastructure; while supporting renewable energy, resource efficiency and climate change adaptation.

The EBRD is actively engaged in promoting the local currency lending and supporting the de-dollarisation of the Georgian banking system and economy. In early 2014, we were the first international financial institution to issue a bond in Georgian Lari, followed most recently by the second Lari bond. This was an important step in strengthening the local currency, increasing confidence in the local market, diversifying sources of funding and developing the local capital market.

In the energy sector, the EBRD was instrumental in assisting Georgia in becoming an electricity exporting country. While Georgia has no oil and gas resources, it is blessed with abundant sources of renewable energy: high mountains, rivers, wind and sunshine. Over the years, we have financed several strategic projects in the energy sector such as the rehabilitation of the Enghuri hydro power plant, the first private hydro power plant Paravani and the Black Sea Transmission Line.

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Published on March 25, 2017

The agribusiness sector accounts for 17 per cent of the country's GDP, 32 per cent of local employment and 31 per cent of foreign currency revenues. Given this potential one would assume that investors from all over the world would be flocking to Ukraine with projects in land farming, processing, packaging and retail.

Ukrainian agribusiness – a jewel in a crown

Ukraine's favourable geographical location; its extremely fertile black soil; decent infrastructure and relatively cheap labour force make the country's agribusiness sector highly competitive. A lot has been achieved in the country over the past 25 years to enable Ukraine to live up to its status as the "breadbasket of Europe" and to help, at least partly, address the global challenge of sustainable food supply and food security.

As a result the agribusiness sector is one of the main drivers of the Ukrainian economy: it accounts for 17 per cent of the country's GDP, 32 per cent of local employment and 31 per cent of foreign currency revenues. During the severe economic downturn of 2014/2015, the agrifood sector was the only one to increase its production and exports. In fostering Ukraine's agribusiness potential, the EBRD has provided over €2.2 billion of financing to the sector, to date, since the start of its operations in the country.

Given this potential one would assume that investors from all over the world would be flocking to Ukraine with projects in land farming, processing, packaging and retail. For now, however, this is not the case. Unfortunately, the complicated geopolitical situation, corruption and the slow pace of reforms (especially the land reform) dampen the overall investment mood.

For a number of years, the EBRD and the Food and Agriculture Organisation of the United Nations (FAO) have initiated and supported reforms and dialogue between regulators and private sector companies in the grain, dairy and meat sectors. This partnership has supported associations of producers of agricultural commodities in dozens of legislative initiatives such as crop receipts, food safety standards, veterinary services etc. – all aimed at improving sector regulation and investment climate. As a result the development of the grain sector has been particularly impressive, with annual grain yields of well over 60 million tonnes. With this Ukraine has firmly established itself as one of the key international players in this segment.

However, in addition to much needed reforms, Ukraine's agribusiness markets, and in particular small businesses, need to develop new approaches to business, to look for new markets and to concentrate on the production of high-value goods, in order to remain competitive on local and global markets and to maximise returns while tapping into export markets. A lot remains to be done in this respect. In 2014, Ukraine's agricultural exports were worth US$ 17 billion of which no less than 54 per cent were primary agricultural products. This highlights the need to find a more prominent role for added value in the total export structure of agricultural commodities. Domestic producers should also be more responsive to the preferences and demands of existing and new export markets.

The tasks may seem challenging, but Ukraine has a long-term partner in the EBRD and we are ready to offer financial support as well as expert advice. For example, the first results of an export promotion project with FAO, under which members of the association of Ukrainian millers promoted their products on trade fairs in South Asia, the Middle East, Africa and Eastern Africa, have been impressive. As a result some participants reported immediate increases in exports to those regions.

Teams of highly experienced local and international experts, commissioned by the EBRD and its international partners and in coordination with the Ministry of Food and Agriculture of Ukraine, have also developed strategies to improve the investment climate. These efforts will continue, while we will also continue to provide financing and to support local agribusiness associations and cooperatives.

Given these efforts and support, the private sector has a unique opportunity to increase the quality and range of its products; to coordinate with companies and associations and to dare to venture into new markets. The EBRD and all the other partners of Ukraine are ready to support the sector and its players.

MATTEO COLANGELI
Head of Albania European Bank for Reconstruction and Development (EBRD)

Published on March 25, 2017

Albania's agribusiness support facility – with a little help from your friends

The lack of finance makes investments difficult and this, in turn, is holding back innovation.

Albania boasts rich soil and favourable climatic conditions in the middle of both the Mediterranean and continental zones of Central Europe. This puts Albania in a unique position to grow and harvest a diverse amount of agricultural produce, ranging from fruits and vegetables to and dairy products, to medical and aromatic plants, as well as wheat.

Consequently, agriculture is a key sector of the Albanian economy. Around 50 per cent of employment is in agribusiness, and the sector accounts for approximately 20 per cent of the country's GDP. However, only around 2 per cent of total lending provided to the Albanian economy is allocated to this sector.

As a result, funding is one of the major obstacles for Albania's agribusiness sector. The lack of finance makes investments difficult and this, in turn, is holding back innovation. Albania's farmers are suffering from outdated technology and low productivity levels. This makes competing with market requirements more and more difficult for them.

The Albania Agribusiness Support Facility was launched in 2016 by the EBRD with the support of the government. It aims to facilitate access to finance for the entire agribusiness chain, in order to boost investment, innovation and growth in this vital sector for Albania. Its successful implementation is expected to benefit the country's rural economy and promote private sector development.

The framework, with a volume of €100 million for the account of the EBRD, plus €80 million, is expected to be mobilised by local partner financial institutions over a three-year period, has found a strong response in the market: Societe Generale Albania, ProCredit Bank Albania as well as the microfinance institutions NOA and Fondi Besa have already joined the programme.

Adela Leka, spokesperson of ProCredit Bank Albania, added: "This facility is an innovative product that will enable us to expand lending to the Albanian SMEs which operate in agribusiness. We strive to address their challenges and to help them invest in modern technology, engage in energy efficiency projects, and

expand their market share. We consider these as key factors for future development, not only for the individual businesses but also indirectly for the economy in which they operate."

The government's financial contribution for the implementation of the framework has made Albania a member of the EBRD donor community. In addition to finance, the EBRD will be offering technical assistance to the participating financial institutions to enhance their capacities in lending to the agribusiness sector as well as direct advisory services to the agribusiness borrowers through its Advice for Small Businesses programme.

Overall, the EBRD aims to support Albania's path from low productivity and subsidised farming towards becoming a sector highlighted by investments and sustainable development. The Bank recognises that these efforts will not come to fruition instantly, but it is fully behind the goal of innovating and expanding agribusiness in Albania and will continue to work alongside the government and partner financial institutions over the coming years to achieve this.

GIULIO MORENO
Head of Montenegro European Bank for Reconstruction and Development (EBRD)

Published on March 25, 2017

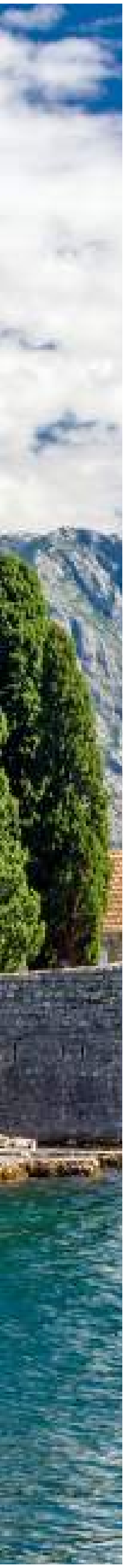
Montenegro joining up agriculture and tourism

Montenegro is a gorgeous country on the Adriatic coast and one of the most popular tourist hotspots in Europe. The country's economy — from big hotels and restaurants to small authentic cafes — relies heavily on the flow of tourists.

However, what many tourists do not realise, despite perhaps seeing lush orchards and vegetable gardens on their way to the seaside, is that they are more than likely eating imported food. Montenegro currently imports far more fruit and vegetables from the European Union (EU), and from neighbouring countries such as Serbia, than it exports.

The problem is not a lack of land or hard-working farmers to grow fruit and vegetables. Montenegro is endowed with favourable natural conditions to grow quality produce, including a mild climate, uncontaminated land and plenty of water for irrigation. Vegetable growing is a traditional business in some regions, especially around the capital Podgorica.

But the sector is dominated by small farmers who use traditional methods of agriculture, which means low productivity. In a modern economy, food processors and retailers need reliable flows of quality products. Currently, local farmers cannot guarantee a sufficient and/or reliable supply of produce. They also have difficulty



accessing finance to grow their businesses.

The EBRD believes there is great potential for Montenegro to substitute many of these imports with locally-grown quality produce, providing jobs for local farmers and reducing transportation and storage.

While there is significant export potential for Montenegro's horticultural sector, its main opportunity is in the domestic market, given the country's dynamic tourism sector. However, at present, growth in tourism tends to increase imports of fruit and vegetables rather than stimulate local agriculture.

The Montenegrin Ministry of Agriculture and Rural Development recognises the importance of developing the horticultural sector. It is already supporting producers' organisations and providing funds for farmers and food processors to invest in more efficient machinery and production facilities. There is discussion about developing specific quality standards for these markets, including Montenegro's own geographical indications, organic food certifications or GAP (Good Agricultural Practices) certification.

However, the EBRD believes that, in order to really unlock the sector's potential, Montenegro needs to develop sustainable value chains. Together with the UN's Food and Agriculture Organisation (FAO) we have already worked with meat producers and processors on upgrading the quality standards in Montenegro.

To build on this successful experience, the Montenegrin Ministry of Agriculture and Rural Development invited EBRD and the FAO to contribute to value chain integration for the fruit and vegetable sector. We are now working with retailers and wholesalers, in the country, on a technical cooperation programme to improve supply chain linkages, producer organisation and consolidation, as well as safety and quality standards.

One way of linking farmers and suppliers is the use of a national distribution centre.

The EBRD has provided equity financing to Voli, a leading supermarket chain, to build a new, state-of-the art distribution centre in Podgorica. Construction is already underway and the centre will open in June 2017. The centre will not only supply Voli's own supermarkets but other retailers too. The 13,000 sq m distribution centre will also create links between local suppliers and wholesale and retail customers. Over time, Voli is planning to purchase more fruit, vegetables and dairy products from existing local suppliers and attract new ones.

By entering into a contract with such a distribution centre, a local farmer will have a more stable income, which in turn will allow them better access to finance, and provide a wholesale customer — such as a hotel — with a reliable supply of local produce.

If these links are built, the whole country, as well as tourists and foreign investors who are interested in Montenegro's attractive tourism sector, will benefit from more local, fresh and delicious food. ●

Montenegro is endowed with favourable natural conditions to grow quality produce, including a mild climate, uncontaminated land and plenty of water for irrigation.

MATTI HYYRYNEN
Head of the Baltics
European Bank for Reconstruction and Development (EBRD)

Published on
April 10, 2017

Lithuania's focus on SME growth and the EBRD's role

The goal is to make Lithuania a hub for innovative technology and finance.

Lithuania's economy has been both consistent and resilient in recent years, effectively recovering from the 2008 financial crisis that affected many EU member states so heavily. Since 2011, the country has achieved an impressive growth rate of four per cent per year and it joined the Eurozone in 2015. In order to ensure further progress, the government plans to encourage increased public and private funding in business projects over the next three years. The goal is to make Lithuania a hub for innovative technology and finance in order to help new businesses and talented entrepreneurs grow.

The EBRD and Lithuania have been working together since 1992, when the Bank made its first investments in the country. Over the following 25 years the Bank has invested over €650 million into 79 projects in Lithuania. While the challenges and tasks underwent considerable changes during this period, the EBRD remains strongly committed to supporting Lithuania's further progress.

One example is the Bank's support of small and medium-sized enterprises (SMEs). An important source of finance for SMEs comes from the European Union Structural and Investment Funds (ESIF) programme, implemented in Lithuania by UAB "Investment and Business Guarantees" (INVEGA), an institution established by the Lithuanian government "to develop and implement effective solutions for promoting entrepreneurship". INVEGA implements and manages a range of global grant and financial instruments that are aimed at enhancing the financing available to local SMEs.

As a long-term investor in private equity and venture capital funds in Lithuania, the EBRD has signed a cooperation agreement with INVEGA. As part of this agreement, which is the first of its kind, the EBRD will play an important role in advising INVEGA on the establishment and ongoing implementation of four private equity and venture funds, supported by ESIF. These four funds will enable almost €60 million of ESIF funds to be deployed, together with additional financial resources, to the benefit of over 70 early- and growth-stage small and medium-sized enterprises in Lithuania.

The partnership between the EBRD and INVEGA will help enable the Lithuanian economy to continue to grow and innovate. The financial instruments will target development, venture capital and business angel funding, which is important for attracting young entrepreneurial talents and businesses.

Finally, Lithuania's goal of increasing its innovative approach and financial capacity is in line with the EBRD's priorities of promoting sustainable economic growth for the country. This is vital for the long-term plans of a country that has proven to be both economically stable and reliable, in recent years. The process starts from within; building up a domestic base in Lithuania that facilitates access to finance for SMEs and getting them "up and running". Building up a country's infrastructure and promoting sustainable growth is what the Bank does and will continue to do in partnership with Lithuania.

Small businesses – the backbone of the Egyptian economy

Women entrepreneurs are a source of great untapped potential in Egypt

JANET HECKMAN
Director for the Southern and Eastern Mediterranean
Director for Egypt
European Bank for Reconstruction and Development (EBRD)

Published on April 20, 2017

With its 90 million people, Egypt has a dynamic private sector that is a resilient and is innovative force within the economy providing 74 per cent of the nation's jobs.

From the start, the EBRD's focus in Egypt has been on tailored programmes that foster the development of the private sector. These include investment in infrastructure and services as well as measures to strengthen competitiveness, which is vital for addressing unemployment.

One of the region's biggest challenges is how to deal with unemployment, especially of women, young people, and the educated.

One priority for the EBRD is small- and medium-sized enterprises. SMEs make up more than 90 per cent of Egypt's active enterprises, yet they are held back. This obstruction comes primarily from limited access to finance, a cumbersome legal and regulatory environment and a lack of market information.

The EBRD's first project in Egypt addressed the financial problem with an SME's credit line to the National Bank of Egypt, NBE. In four years the EBRD has committed a total of $430 million to increasing the availability of finance to small enterprises and to enabling the banks to expand their SME lending activities within the country.

As well as financing, the Bank (with the support of the European Union) provides business advice to help micro, small and medium-sized enterprises, MSMEs, become catalysts for growth in the local and regional economies. To date, more than 500 Egyptian enterprises have received business advisory services that were delivered by local consultants and international experts.

Women entrepreneurs are a source of great untapped potential in Egypt. In 2013, the EBRD launched its Women in Business Programme in Egypt with a $20 million pilot facility through NBE. The programme addresses the challenges that female entrepreneurs face in obtaining finance. This comprehensive programme is designed to promote women's entrepreneurship by helping women-led SMEs access know-how through advisory services for their businesses, as well as training, mentoring and networking opportunities. 140 women-led companies have been supported to date.

In 2014, EBRD signed a pilot energy efficiency programme with NBE, which provided credit lines for private-sector investments in energy efficiency and renewable energy projects. This was a way of broadening our support for the private sector while at the same time contributing to Egypt's energy security. Projects that are financed under the framework contribute to Egypt's energy security by improving efficiency in the corporate sector and promoting the use of renewable energy.

Building on the success of the pilot programme, a new €140 million Green Economy Financing Facility was launched in March 2017, in Egypt. It is now providing loans for energy efficiency and small-scale renewable energy investments by private companies, through a group of participating banks, and also has the aim of achieving energy security.

AGRIS PREIMANIS
EBRD Head of Kazakhstan

Published on April 21, 2017

Kazakhstan is beginning to explore Belt and Road opportunities

Kazakhstan's non-oil and gas industries need to innovate and think creatively if Kazakhstan is to compete successfully on international markets.

It was in Kazakhstan that the world first heard about a new initiative from China to recreate the ancient Silk Road trading routes. During his visit, in 2013, the President of China, Xi Jinping, announced what has become known as the Belt and Road Initiative, for the first time. It is a giant project to build both a land and a maritime route to connect China with Europe and other trading partners.

From the outset the initiative focused attention on Central Asia, a vast region neighbouring western China, which is a priority area of development for China's central government. What new opportunities could the plan offer the economies and investors in Kazakhstan – a resource-rich but remote country looking to diversify its oil-based economy?

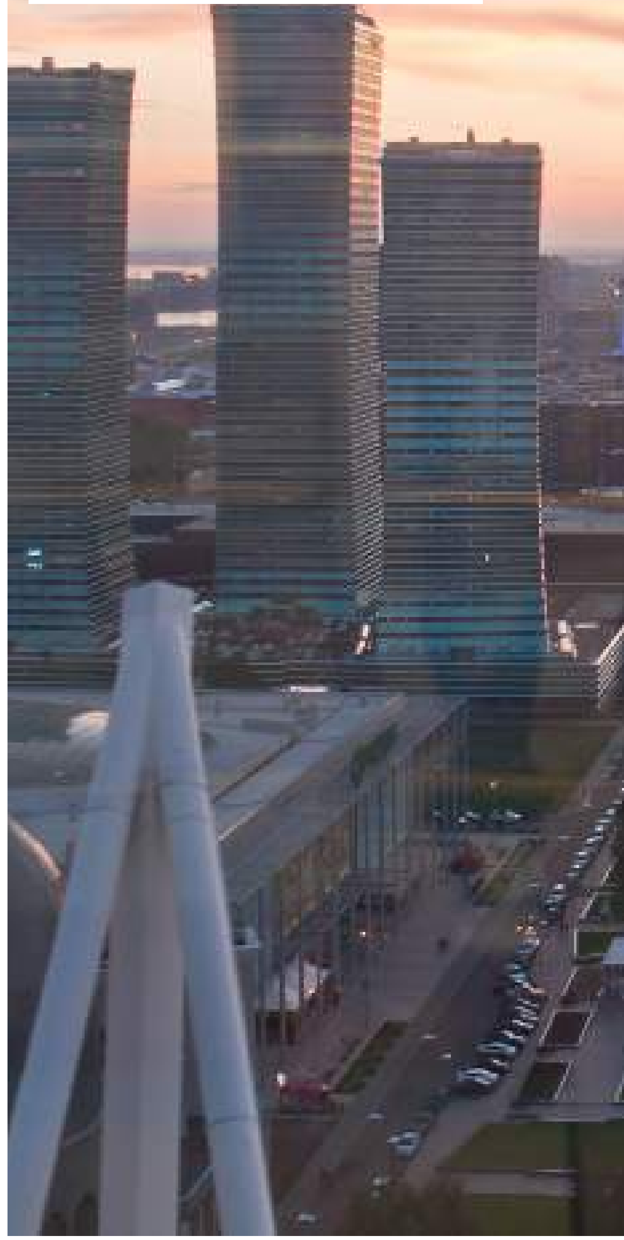
Today, we can see how these new opportunities are already beginning to change investors' view of Kazakhstan. Development of the transport infrastructure is obviously at the forefront. But we are also seeing many other new projects being discussed – with financing expected to flow in soon – in energy, telecommunications, e-commerce and other areas.

To support investments across the vast expanse of the Belt and Road countries, new financing institutions such as the Asia Infrastructure Investment Bank (AIIB) and the Silk Road Fund have been created recently. Chinese investors have already announced plans to invest over $75 billion along the new road, creating significant opportunities for investors and suppliers of services from the EU, the USA, the Middle East and many other countries. Now is the time to take advantage of this, but what does all this mean for Kazakhstan?

First of all, better cross-border links – and the opportunities that come with them. Kazakhstan is already looking to create a financial hub in Astana to serve the wider region, known as the Astana International Financial Centre. The country aims to offer new financial products and services for the new Silk Road, including a platform for domestic and foreign companies to raise finance though green bonds and for investors to fund Belt and Road-related projects. This will not only be an opportunity to raise capital but will also require significant participation from banks, rating agencies and other financial services' firms across the world; opening new opportunities for them.

Secondly, creating better connectivity will happen overnight and it will require both public and private funding, as well as expertise, particularly from foreign firms. The logistics sector is an area that will be, in my view, particularly interesting in the coming years and an area that foreign investors should pay close attention to. An increased flow of goods and services will create an opportunity for more value-added logistic services such as dry ports, multi-modal logistics centres and others. The EBRD is already investing in this growth area – one example is an investment in the development of the Khorgos Dry Port on the border between Kazakhstan and China.

Thirdly, there will be other export-based sectors that will benefit from the Belt and Road Initiative. Agribusiness will be one of them. Kazakhstan has vast arable land: it is already the largest flour exporter in the world and has been successfully diversifying the production of crops towards more



value-added oilseeds and feed grains, the demand for which has grown strongly in the past few years, across the region.

Kazakhstan also has vast potential to develop its agriculture processing capacity. Last year alone, the EBRD invested more than $130 million in five agribusiness projects across the value chain including cotton, poultry, dairy, confectionery and fast moving consumer goods. That is only scratching the surface of this industry's potential.

The EBRD is the largest foreign investor in the non-extractive sectors in many Belt and Road countries and is well-placed to support them in developing their infrastructure, energy and telecoms platforms and strengthening private sector companies to take advantage of improved opportunities.

We don't just offer investment: we work closely with governments and private sector partners to stimulate reforms, reduce barriers to cross-border trade and cooperation, and improve competitiveness. Competitiveness is going to be especially important for Kazakhstan as it opens up to new markets.

As the country has realised, its non-oil and gas industries need to innovate and to think creatively if Kazakhstan is to compete successfully on international markets. The Belt and Road Initiative is bringing those markets closer. We welcome this, as we do the government's drive to open up to the world and participate in global solutions to global challenges – including climate change.

In this context it is especially commendable to see a switch to a green economy in Kazakhstan. A number of renewable energy projects are being developed and the EBRD is considering financing several of them. We have already supported the first 50 MW stage of the Burnoye Solar plant, the first on such a scale in the country, and we will be supporting another 50 MW.

Kazakhstan has great potential for renewable energy, and is important not only to reduce emissions. In the future, and provided all the necessary links are in place, clean energy could be exported to countries that want and need it – including Kazakhstan's largest neighbour and trading partner, China.

DIMITRI GVINDADZE
EBRD Head of Moldova

Published on April 22, 2017

Moldova: a regional economic platform vision

The recent political and macroeconomic stability has enabled the Moldovan authorities to look beyond the short term.

Moldova has been working recently to foster investments and to address the accumulated challenges in the banking and the real sectors. The programme with the IMF is on track and it has been serving as an important anchor point for structural reforms, including the comprehensive transformation of Moldova's banking sector which is showing itself through improved regulations and front-loaded efforts to foster good governance and transparency.

The EBRD's current portfolio in Moldova is close to €500 million, split between dozens of public and private sector operations. The EBRD is helping Moldova to develop energy interconnections of cross-border significance (a natural gas pipeline and a high-voltage power transmission line with Romania), to improve the municipal and urban infrastructure, to foster energy efficiency, to develop a road infrastructure, to restructure the railways and to support viable and transparent businesses which represent the backbone of Moldova's economy.

The ongoing reforms to reinforce transparency and good governance in the banking sector will allow the EBRD to do more in, and through, Moldova's banks and in this way we can further extend our outreach to the small and medium size enterprises. We see the effort on the side of the Moldovan authorities to address the banking sector issues, and this drives our commitment to support Moldova.

Together with the financing, the EBRD delivers policy dialogue in a number of key areas, including energy sector reforms, banking and e-procurement etc. The EBRD has supported the work of the Secretariat of the Prime Minister's Economic Council, which provides a platform for discussing business climate related matters among the representatives of the government and of the private sector and of international development partners. The agendas are usually long and there is a willingness to engage and to succeed on all sides. Our operational and the policy dialogue-related work streams in Moldova are reinforcing and strengthening each other.

The recent political and macroeconomic stability has enabled the Moldovan authorities to look beyond the short term, and to think about how to address Moldova's structural constraints, in order to release sustainable private sector-driven growth.

As a small open economy, Moldova cannot fence itself in from external economic factors, although there is a general understanding that far-reaching structural reforms, including the increased integration with the European Union in the context of the DCFTA, could make Moldova more resilient, more stable and more successful. Continued macroeconomic stability and an improved business climate would allow firms – domestic and foreign alike – to spend and invest more. As much as Moldova needs lots of foreign direct investment to spark and retain high growth, the reforms which aim to foster the level playing field would unlock significant domestic investment opportunities.

Such opportunities do exist. In fact, there are many of them.

Moldova is very centrally located, its people speak multiple languages and are hard-working and well-educated: The European Union's huge market for goods and services is right next door, and the DCFTA arrangement facilitates a free movement of goods: Moldovans can travel to the European Union and to the Commonwealth of Independent States visa-free. The Giurgiulesti International Free Port, in Moldova's south, conveniently links with its regional roads and railway infrastructure and represents an important gateway to the Black Sea as well as a source of investment and of employment. Good air and road links exist with countries in Moldova's immediate neighbourhood and beyond.

In the recent years, Moldova has emerged as a hub for suppliers of the international car industry. Auto parts makers such as Germany's Dräxlmaier Group, Austria's Gebauer & Griller, Italy's La Triveneta Cavi and Japan's Sumitomo have discovered Moldova one-by-one: its educated, hard-working people and relatively lower costs. They produce in Moldova (cables, electric harnesses for cars etc.) and export – some in the real-time mode – to assembly lines elsewhere in Europe. The government has been supportive of this, through an access infrastructure and policies that are conducive, including efficient customs clearance and low taxes.

The automotive cluster has provided employment to thousands of Moldovans, and it represents a shining example of how and why Moldova could be a magnet for foreign investors in other sectors and clusters.

Such investors – who are ready to integrate themselves into Moldova, and produce and supply to the local market and export to other locations – promote Moldova's regional economic vision of its position. The authorities – and the EBRD as Moldova's largest institutional investor – are keen to support the duplication of similar projects, which integrate Moldova into the international value chains, create employment opportunities and thus help to address the population decline which has been an important challenge for Moldova.

In sum, the EBRD remains committed to Moldova. A number of important international investors have benefitted from Moldova's location and from the availability of the factors of production. We invite others to explore Moldova as the potential investment and doing business destination.

HEIKE HARMGART
Head of the European Bank for Reconstruction and Development (EBRD) in Jordan

Published on April 15, 2017

The EBRD helps Jordan's infrastructure to accommodate an influx of refugees

Creating jobs, for youth in particular, is critical for the host communities as well as the refugees.

The conflict in Syria is the worst humanitarian crisis of our time. To date, almost five million people have been forced to flee the country in six years of war. They are seeking a safe haven in Jordan, Lebanon, Turkey and beyond, while some 13.5 million people are displaced internally.

Desperate humanitarian efforts were always a race against time. They could not prevent the crisis from also affecting the economies of Syria's neighbouring countries. The unprecedented influx of refugees is a massive burden on the host countries and a strain on their infrastructure. At the same time, solutions are needed to empower refugees to participate in the economy.

In 2016, during the Supporting Syria and the Region conference in London, the international community — bringing together humanitarian aid organisations and international financial institutions — pledged its help. The EBRD joined this effort.

Our focus in doing this was to assign a key role to the private sector to provide sustainable livelihoods for refugees and to help the host countries to cope with the economic strain, and the strain on public services, of this huge challenge. Currently, Turkey is home to more than two million refugees from Syria alone, while Jordan has an estimated 1.4 million people who have fled from their homes.

We have brought our core competencies into play: infrastructure support, small and medium-sized enterprises and inclusion programmes to specifically support women and young people.

The population increase in Jordan, especially in the capital Amman, is overburdening its infrastructure on many levels.

One €22.5 million investment in the construction of a new 30 km wastewater pipeline will provide additional capacity to the wastewater system and will benefit 2.2 million people. Another €13.2 million investment, in the East Zarqa wastewater project, will benefit about 450,000 people by 2020. The Greater Amman Municipality will upgrade the solid waste infrastructure, in order to cope with the 25 per cent increase in waste generated by the rapid rise in population, thanks to a €102 million loan.

Creating jobs, for youth in particular, is critical for the host communities as well as the refugees. In Jordan, we have supported a training programme in retail skills for young Jordanians. The training centre was opened at the Abdali Mall in October 2016, and has already provided training to 150 young people. The majority of the trainees found jobs in the mall and the neighbouring shops and restaurants. This programme will expand to include Syrian refugees in the second half of the year.

Together with Microfund for Women, we are also supporting the entrepreneurial spirit of female refugees by scaling up the pilot programmes to include them.

While only a political solution will end the human suffering in Syria, as stated during the Supporting the future of Syria and the region conference, held in Brussels in April 2017, the need for economic development and to improve lives, as quickly and as efficiently as possible, is only becoming more pressing. Every institution which can make a contribution towards this goal is urgently required to do so.