

## RÄUMLICHE DISPARITÄTEN *SPATIAL DISPARITIES*

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### IS THERE A “CHINESE WALL” IN EUROPE? A GLANCE AT THE DEVELOPMENT OF SOCIO-ECONOMIC DISPARITIES IN EUROPE

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with 3 figures and 3 tables in the text

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#### *Zusammenfassung*

*Gibt es in Europa eine Chinesische Mauer? Ein Blick auf die Entwicklung sozio-ökonomischer Disparitäten in Europa*

*Dieser Beitrag analysiert Faktoren, welche auf die verschiedenen Pfade sozio-ökonomischer Entwicklung europäischer Länder nach dem Zweiten Weltkrieg möglicherweise Einfluss gehabt haben könnten. Es zeigt sich, dass es unterschiedliches Wirtschaftswachstum und wachsende sozio-ökonomische Disparitäten nicht nur zwischen Mitgliedsstaaten der*

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*Europäischen Union (EU) und Nicht-EU-Ländern, sondern auch innerhalb dieser Ländergruppen gibt. Nach dem Index der globalen Wettbewerbsfähigkeit (Global Competitiveness Index, GCI) ergeben sich drei deutlich unterscheidbare Gruppen europäischer Länder. Diese unterschieden sich nicht nur in der Vergangenheit, sondern auch noch zu Beginn des 21. Jhs. Entscheidend verstärkt werden heute die Unterschiede durch den Grad der Ausstattung mit digitaler Technologie. Die wichtigsten wirtschaftlichen und demographischen Indikatoren lassen in Summe den Schluss zu, dass die ungleiche globale Wettbewerbsfähigkeit der europäischen Länder mit dem historischen Erbe, der Wirtschaftspolitik und den institutionellen Strukturen erklärt werden kann. Obwohl die Grenze zwischen den drei analysierten Gruppen nicht immer scharf ist, kann man von einer „Chinesischen Mauer“ sprechen, die durch größere Unterschiede in Bezug auf Produktivität, ausländische Direktinvestitionen, Arbeitsmarkt und Demographie (Altersstruktur, Migration) wohl weiter anwachsen wird.*

*Schlagwörter: Wirtschaftswachstum, Entwicklungsmodelle, sozio-ökonomische Konvergenz, Europäische Union*

## Summary

*This paper analyses the potential factors underlying the different socio-economic paths of European countries after the Second World War. It is clear that divergent economic growth and increasing social and economic divides are still present not only between European Union (EU) and non-EU countries, but also inside these groups. Based on values of the Global Competitiveness Index (GCI), this paper deals with three clearly differentiated groups of European countries. These groups have divergent socio-economic development not only in the past, but still at the beginning of the 21<sup>st</sup> century. This is emphasised by the digital divide. The main economic and demographic indicators have been analysed, and they reveal that divergence in global economic competitiveness of European countries can be explained by different historical heritages, economic policies, and institutional structures. Although it is difficult to draw a strict line between the three groups, the rising “Chinese wall” is further expanding by the changing in the countries’ productivity, foreign direct investment structure, labour force, and demographics (population ageing, old dependency ratios, migration flows).*

*Keywords: economic growth, development models, socio-economic convergence, European Union*

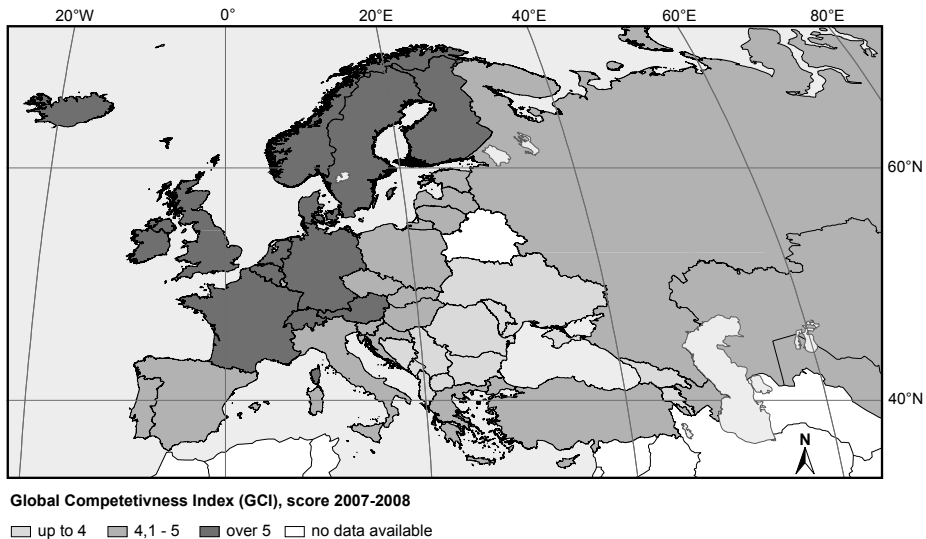
## 1 Introduction

The European Union (EU) and the European Monetary Union (EMU) are ongoing projects to unify Europe. Although the EU is trying to introduce common law, common institutions, and a large common market while removing boundaries, this is still a very complex and diversified region. European countries are characterised by diverging eco-

conomic performances, demographic dynamics and structures as well as cultural and historical differences.

The aim of this paper is to examine eventual convergence between the three groups of European countries in the context of their development and socio-economic characteristics. Considering the historical, demographic and economic background of these countries, one could ask if there are significant differences between them – especially as regards the level of economic and social development (VITALE 2015; MUSIL 2013). What are the factors of such differences and could they be driven by the changes in the last two and a half decades? To provide for answers, we used indicators of real and financial development, public finance, monetary and demographic indicators. We met methodological challenges when considering regionalisation of European countries in this context.

The countries analysed are divided into three groups according to Global Competitiveness Index (GCI) values (see Fig. 1). This index measures a country’s competitiveness and is derived from “the set of institutions, policies, and factors that determine the level of productivity of an economy, which in turn sets the level of prosperity that the country can earn” (PORTER, SALA-I-MARTIN & SCHWAB 2007, p. 12). Although the best indicator of regional socio-economic disparities would be the Regional Competitiveness Index (RCI), it cannot be applied, since RCI data for non-EU countries are not available. The GCI is suitable for the purpose of economic convergence/divergence analysis in Europe, because it considers almost all main socio-economic variables that influence a country’s economic development and that are also included in the RCI (institutions, infrastructure, macro-economic environment, health care, primary education, higher education and training, com-



Source: PORTER, SALA-I-MARTIN & SCHWAB 2007

Fig. 1: Global Competitiveness Index (GCI)

modity market efficiency, labour market efficiency, financial market development, technological readiness, market size, business sophistication, and innovation). The GCI values for 2007–2008 are chosen because this couple of years marks the transition in the world economic cycle from expansion to recession, i.e. the start of the world economic crisis. As it will be explained later, until 2007 all countries analysed in this paper had “the golden age of stable economic growth”. After this year, the rates of economic growth diverged and in many countries (especially of the Western Balkans) and became even negative.

The first group of countries (leaders) consists of the most developed EU-member states that show the highest performance in economic and social terms: Austria, Belgium, Denmark, Finland, France, Germany, the Netherlands, Sweden, the United Kingdom and Luxemburg. The second group (middle group) consists of countries that joined the EU in 2004: Cyprus, Czechia, Estonia, Hungary, Latvia, Lithuania, Malta, Poland, Slovakia, Slovenia, and five “problematic” southern or peripheral European Economic and Monetary Union (EMU) countries – Italy, Spain, Portugal, Greece and Ireland. Although they are old EMU members, they are placed in this group due to their weaker economic performances. The remaining countries constitute the third group (laggards). This group consists of some new EU members, who are still in the process of structural economic changes, on their road to accepting Euro and showing low performances (Romania, Bulgaria and Croatia) (see for Romania, e.g., RUSU & SCHREIBER 2013). The least developed European countries are in some phase of EU accession (Serbia, Montenegro, Albania, Bosnia and Herzegovina, Macedonia).

## 2 Different patterns of economic growth – a historical perspective

After the Second World War, European countries took different paths of economic development. This used to be analysed in terms of the West/East dichotomy. The countries that belonged to the European West passed through three periods: (1) 1950–1973 (“Golden Age of Economic Growth”); (2) slowdown from 1973 until the beginning of the 1990s; (3) “New Economy” after the mid-1990s. The countries of the European East also passed three clearly different periods: (1) until the beginning of the 1970s the Communist “Silver Age” growth period; (2) slowdown finished by collapse at the end of the 1980s; (3) transition to a market economy (CRAFTS & TONIOLO 2008).

The European West has seen fast economic growth from 1950 to 1973 during which the twelve economies grew by 4.7% per year. According to CRAFTS & TONIOLO, the main driving force for such fast economic growth was the emulation of American technology and business organisation (2008). Other reasons were the transfer of workers out of agriculture, post-war reconstruction and relatively small macro-economic fluctuations (during the Bretton Woods era of the international monetary system). This provided a highly favourable environment for fast increases in investment (BOLTHO 1982). Some researchers have also emphasised the importance of external trade liberalisation and the increased integration of the European market supporting capital net inflow through foreign invest-

ment and technology transfer (with chemicals, computers and transport equipment). This reduced the technology gap with the United States (NELSON & WRIGHT 1992).

From 1950 until 1973, the leader group had extensive growth that was fastest in Germany and Austria, while the slowest economic growth was reported in the United Kingdom (see Table 1). In the middle group, the “golden age” was most visible in Greece, Italy, Portugal and Spain, especially because they started the process of liberalising and opening to Europe and the world, and it was lowest in Ireland. During the same period, growth rates in Communist countries (laggards) were only a little below the leaders group and some countries from the second group. For example, the growth rate of 3.4% per year for this period in the Union of Socialist Soviet Republics (USSR) compares with the achievements of countries from the second group such as Italy or Spain, who started out with similarly low income levels. Similar evidence emerges when analysing Czechoslovakia

| Countries               | 1820–1870 | 1870–1913 | 1913–1950 | 1950–1973 | 1973–1992 | 1973–2005 |
|-------------------------|-----------|-----------|-----------|-----------|-----------|-----------|
| <b>1 – Leaders</b>      |           |           |           |           |           |           |
| Austria                 | 0.7       | 1.5       | 0.2       | 4.9       | 2.2       | 2.13      |
| Belgium                 | 1.4       | 1.0       | 0.7       | 3.5       | 1.9       | 1.87      |
| Denmark                 | 0.9       | 1.6       | 1.6       | 3.1       | 1.6       | 1.73      |
| Finland                 | 0.8       | 1.4       | 1.9       | 4.3       | 1.6       | 2.18      |
| France                  | 0.8       | 1.5       | 1.1       | 4.0       | 1.7       | 1.67      |
| Germany                 | 1.1       | 1.6       | 0.3       | 5.0       | 2.1       | 1.41      |
| Netherlands             | 1.1       | 0.9       | 1.1       | 3.4       | 1.4       | 1.72      |
| Norway                  | 0.5       | 1.3       | 2.1       | 3.2       | 2.9       | 2.78      |
| Sweden                  | 0.7       | 1.5       | 2.1       | 3.1       | 1.2       | 1.68      |
| Switzerland             | n.a.      | 1.5       | 2.1       | 3.1       | 0.8       | 0.74      |
| United Kingdom          | 1.2       | 1.0       | 0.8       | 2.5       | 1.4       | 1.96      |
| <b>2 – Middle group</b> |           |           |           |           |           |           |
| Italy                   | 0.6       | 1.3       | 0.8       | 5.0       | 2.4       | 1.88      |
| Greece                  | n.a.      | n.a.      | 0.5       | 6.2       | 1.5       | 2.10      |
| Ireland                 | 1.2       | 1.0       | 0.7       | 3.1       | 2.7       | 3.84      |
| Portugal                | n.a.      | 0.5       | 1.2       | 5.7       | 2.1       | 2.15      |
| Spain                   | 0.5       | 1.2       | 0.2       | 5.8       | 1.9       | 2.74      |
| Czechoslovakia          | 0.6       | 1.4       | 1.4       | 3.1       | -0.1      | 1.32      |
| Hungary                 | n.a.      | 1.2       | 0.5       | 3.6       | 0.0       | 1.45      |
| Poland                  | n.a.      | n.a.      | n.a.      | 3.4       | -0.6      | 1.46      |
| <b>3 – Laggards</b>     |           |           |           |           |           |           |
| Bulgaria                | n.a.      | n.a.      | 0.3       | 5.2       | -1.4      | 0.96      |
| Romania                 | n.a.      | n.a.      | n.a.      | 4.8       | -1.6      | 0.44      |
| USSR                    | 0.6       | 0.9       | 1.8       | 3.4       | -0.4      | n.a.      |
| Yugoslavia              | n.a.      | n.a.      | 1.0       | 4.4       | -0.5      | 0.79      |
| Albania                 | n.a.      | 1.4       | 0.6       | 3.6       | n.a.      | 1.34      |

Source: MADDISON 1996

Tab. 1: Real GDP per capita growth 1820–2005, in %

(as a middle group country) that performed almost two percentage points per year lower Gross Domestic Product (GDP) growth than Austria in this period.

After the beginning of the 1970s, i.e. in the second period, economic growth in all European countries slowed down. The main reasons were (1) diminishing returns to investment; (2) an increasing proportion of public spending and taxation in GDP (which had as a consequence a shifting of economic activity into the shadow economy); (3) a higher level of labour markets regulation. As a result, labour markets were not flexible enough, while capital found new exit options in a more globalised world (CRAFTS & TONIOLO 2008). According to EICHENGREEN, the main cause of this slowdown was the switch from extensive to intensive growth (growth through innovation) (EICHENGREEN 2006). As EICHENGREEN states, the “institutions tailored to the needs of extensive growth were less suited to the challenges of intensive growth” (2006, p. 24).

The Communist countries from the middle group and most of such countries from the laggards have levels of real GDP per capita well below those in the leader group. Over time, the gap widened, especially after 1973. This was partly the consequence of the collapse in output at the end of the Communist period and the delay before economic growth started to recover in the transition economies.

### **3 The process of economic integration in Europe 1990–2015**

The last decade of the 20<sup>th</sup> century was a period of great enthusiasm about EU enlargement. Since then, there were several waves of EU enlargement encompassing very different countries within the EU tissue.

Certain socio-economic disparities exist even between the “first twelve”, i.e. between southern and the northwestern member states. But the real serious problem as regards socio-economic spatial disparities arose with access of East-Central and Southeast European countries in 2004 and 2007. Economic and social differences within EU widened greatly and were emphasised even more by the economic crisis after 2007.

Accepting that diminishing of regional disparities within EU would be one of the biggest challenges, the EU developed and is still developing a significant number of disparity-equalisation instruments. To identify the optimal set of instruments and the best approach to balance regional development, the EU pays great attention to analysing social and economic determinants.

#### **3.1 Demographic processes in the EU integration area**

The population sizes of EU countries and of those countries on the accession path to the EU are quite different. Although the legal acts of the Union consider all members to be equal, population size gives certain “market power” to some countries. This results in one or more “population leader/s” (see Table 2). In the leader group, three countries dominate due to their population number (Germany, France and the United Kingdom). These coun-

|                                            | Population,<br>2015    | Population<br>density<br>(inh./km <sup>2</sup> ),<br>2014 | Crude rate<br>of population<br>change<br>(per 1,000<br>inh.) <sup>*</sup> , 2014 | Crude rate<br>of natural<br>change<br>(per 1,000<br>inh.), 2014 | Net migration<br>rate (per<br>1,000 inh.),<br>2010–2015 |
|--------------------------------------------|------------------------|-----------------------------------------------------------|----------------------------------------------------------------------------------|-----------------------------------------------------------------|---------------------------------------------------------|
| <b>1<sup>st</sup> group – Leaders</b>      |                        |                                                           |                                                                                  |                                                                 |                                                         |
| Austria                                    | 8,576,261              | 103.6                                                     | 8.1                                                                              | 0.4                                                             | 3.5                                                     |
| Belgium                                    | 11,258,434             | 370.3                                                     | 4.8                                                                              | 1.8                                                             | 4.9                                                     |
| Denmark                                    | 5,659,715              | 131.5                                                     | 5.8                                                                              | 1.0                                                             | 3.5                                                     |
| Finland                                    | 5,471,753              | 18.0                                                      | 3.8                                                                              | 0.9                                                             | 4.0                                                     |
| France                                     | 66,415,161             | 104.5                                                     | 4.6                                                                              | 3.9                                                             | 1.0                                                     |
| Germany                                    | 81,197,537             | 226.6                                                     | 5.3                                                                              | -1.9                                                            | 3.1                                                     |
| Luxemburg                                  | 562,958                | 215.1                                                     | 23.9                                                                             | 4.0                                                             | 18.0                                                    |
| Netherlands                                | 16,900,726             | 500.7                                                     | 4.2                                                                              | 2.1                                                             | 1.3                                                     |
| Sweden                                     | 9,747,355              | 23.8                                                      | 10.6                                                                             | 2.7                                                             | 5.7                                                     |
| United Kingdom                             | 64,875,165             | 266.4                                                     | 8.1                                                                              | 3.2                                                             | 2.0                                                     |
| <b>2<sup>nd</sup> group – Middle group</b> |                        |                                                           |                                                                                  |                                                                 |                                                         |
| Czechia                                    | 10,538,275             | 136.3                                                     | 2.5                                                                              | 0.4                                                             | 0.6                                                     |
| Cyprus                                     | 847,008                | 92.5                                                      | -12.9                                                                            | 4.7                                                             | 6.2                                                     |
| Estonia                                    | 1,313,271              | 30.3                                                      | -1.9                                                                             | -1.5                                                            | -1.6                                                    |
| Greece                                     | 10,858,018             | 83.3                                                      | -6.3                                                                             | -2.0                                                            | -2.5                                                    |
| Hungary                                    | 9,855,571              | 106.1                                                     | -2.2                                                                             | -3.3                                                            | 0.6                                                     |
| Italy                                      | 60,795,612             | 201.2                                                     | 0.2                                                                              | -1.6                                                            | 1.8                                                     |
| Ireland                                    | 4,628,949              | 67.5                                                      | 5.1                                                                              | 8.3                                                             | -6.1                                                    |
| Latvia                                     | 1,986,096              | 32.0                                                      | -7.7                                                                             | -3.4                                                            | -7.2                                                    |
| Lithuania                                  | 2,921,262              | 46.8                                                      | -7.6                                                                             | -3.4                                                            | -11.3                                                   |
| Malta                                      | 429,344                | 1,352.4                                                   | 9.3                                                                              | 2.2                                                             | 3.0                                                     |
| Poland                                     | 38,005,614             | 124.1                                                     | -0.3                                                                             | 0.4                                                             | -0.4                                                    |
| Portugal                                   | 10,374,822             | 112.8                                                     | -5.0                                                                             | -2.2                                                            | -2.7                                                    |
| Slovakia                                   | 5,421,349              | 110.5                                                     | 1.0                                                                              | 0.7                                                             | 0.1                                                     |
| Slovenia                                   | 2,062,874              | 102.4                                                     | 0.9                                                                              | 1.1                                                             | 0.4                                                     |
| Spain                                      | 46,449,565             | 92.5                                                      | -1.3                                                                             | 0.7                                                             | -2.6                                                    |
| <b>3<sup>rd</sup> group – Laggards</b>     |                        |                                                           |                                                                                  |                                                                 |                                                         |
| Albania                                    | 2,893,005              | 105.6                                                     | -1.0                                                                             | 5.2                                                             | -6.3                                                    |
| Bosnia and<br>Herzegovina                  | 3,825,334              | 74.8                                                      | -1.5                                                                             | -1.5                                                            | -0.1                                                    |
| Bulgaria                                   | 7,202,198              | 66.3                                                      | -6.0                                                                             | -5.7                                                            | -1.4                                                    |
| Croatia                                    | 4,225,316              | 74.9                                                      | -5.1                                                                             | -2.7                                                            | -0.9                                                    |
| Macedonia                                  | 2,069,172              | 83.0                                                      | 1.6                                                                              | 1.9                                                             | -0.5                                                    |
| Montenegro                                 | 622,099                | 45.0                                                      | 0.9                                                                              | 2.4                                                             | -0.8                                                    |
| Romania                                    | 19,870,647             | 86.5                                                      | -3.9                                                                             | -3.1                                                            | -4.4                                                    |
| Serbia                                     | 7,114,393 <sup>1</sup> |                                                           | -4.5 <sup>1</sup>                                                                | -4.5 <sup>1</sup>                                               | -2.2 <sup>2</sup>                                       |

<sup>1</sup> without Kosovo, which is under United Nations Security Council Resolution 1244/99

<sup>2</sup> with estimated data for Kosovo

\* The crude rate of population change is the ratio of population change during the year related to the average population in that year.

Sources: EUROSTAT, UNITED NATIONS 2015

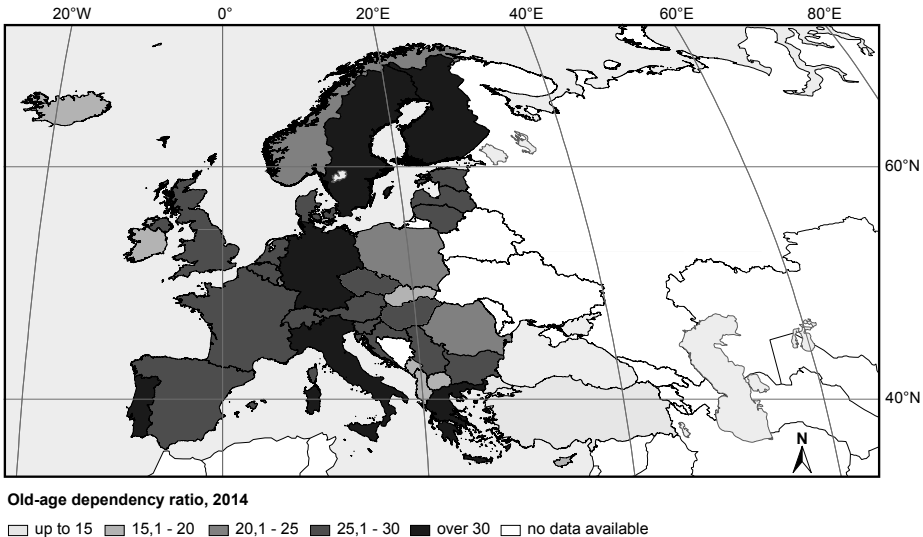
Tab. 2: Demographic indicators of EU-28 and EU accession countries

tries encompass a market of more than 200 million people, which is more than four times bigger than the rest of the group. These three countries are the economic “motors” of the EU, since population size cannot be neglected. Similarly, Italy, Spain and Poland amount to 150 million people.

Demographic characteristics of markets as well as labour force or some other relevant demographic issues are key inputs in economic development analysis. Analysing population change in the three country groups, we could not find common trends or characteristics of the group-member countries. Nevertheless, this indicator is important for social and economic convergence analysis, because it is the result of both components of population growth – natural and mechanical, which result from different economic and demographic processes in these countries.

The first group of countries (leaders) shows population growth. However, this is not the result of significant positive natural increase, but rather of the combined effects of positive trends in natural components as well as a high net migration rate. In some cases, such as the United Kingdom or France, a relatively high natural increase was followed by low net migration. In contrast, in Germany for example, natural depopulation was compensated by a larger number of immigrants.

In the middle group, there are more countries with negative population development (almost two thirds of them). This is the result of natural decrease and mostly positive net migration. Unfortunately, in most of the countries with natural decrease, immigration cannot compensate population losses. Only a few countries had emigration that led to a decline in population, despite a positive trend in natural population development (Ireland, Poland and Spain). This is due to economic changes – especially during the economic cri-



Source: EUROSTAT; authors' analysis

Fig. 2: Old-age dependency ratio, 2014



sis of 2007. Laggard countries (the third group) are all characterised by population decline (or very small positive growth) and all of them are the source of migration flows – mostly towards the leader countries.

Such population trends produced certain demographic structures and economic processes that resulted in serious social and economic disparities among all countries and among groups of countries (MANIĆ, POPOVIĆ & MOLNAR 2012). One of the most important consequences is demographic aging. Demographic aging is well underway in many European countries. The proportion of the population aged 65 and more grows in most countries with serious consequences for future labour force. While this could be smoothed by intensive immigration towards the most attractive countries (leaders), this is negative for the economic and social development of Europe in the long run.

The old-age dependency ratio represents the ratio between the number of persons aged 65 and more (the economically inactive part of population) and the number of persons aged between 15 and 64. An older population has a higher value. Countries with higher values of this ratio are (and will be in the future) the destination of migration flows from countries with a younger labour force (the lower values of the ratio) (see Fig. 2). This is an important impact factor on the labour market, because it directly influences the contingent of labour force, but also to the very economy of the country (MAYERHOFER 2014).

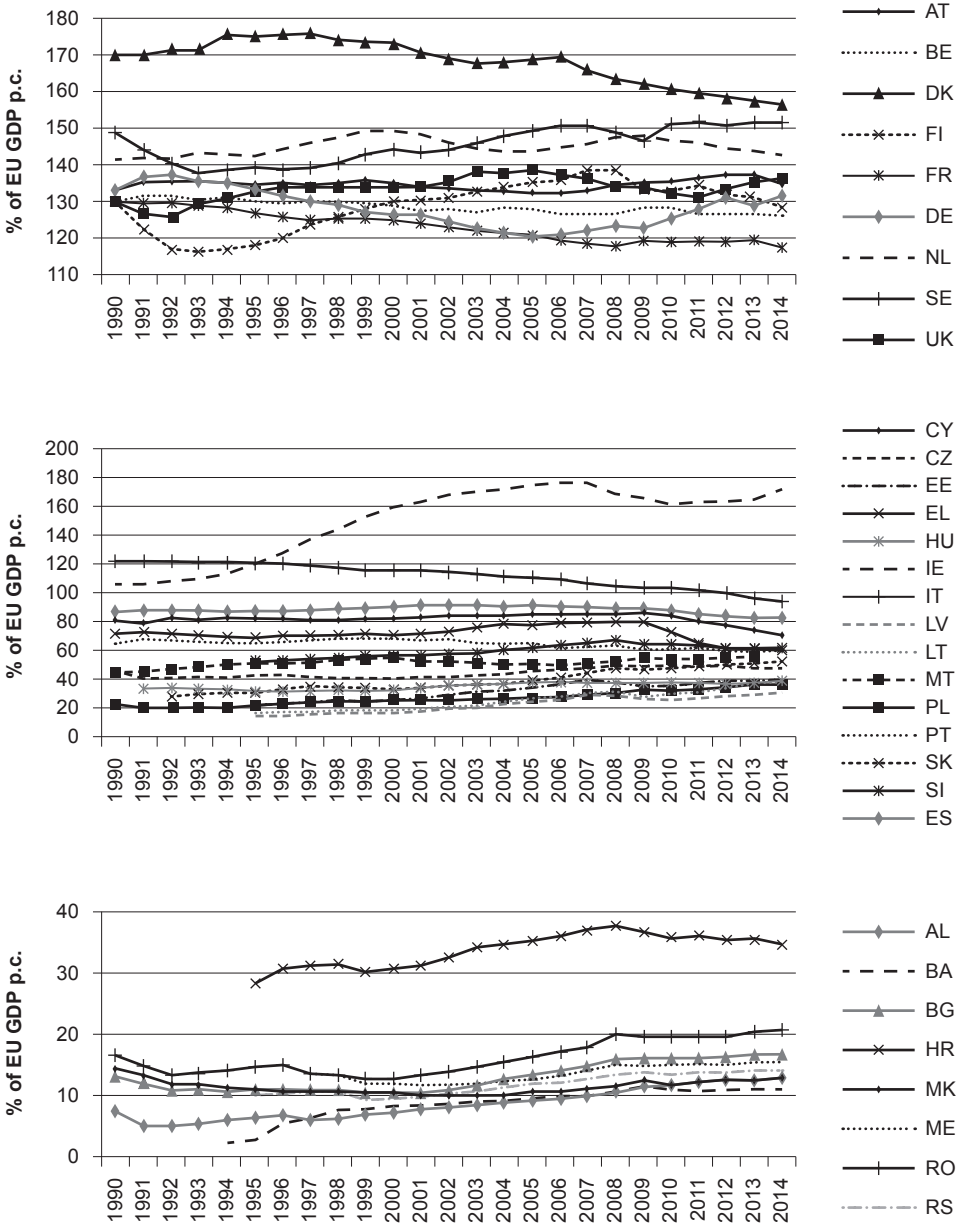
### 3.2 Economic characteristics and disparities

Considering some of the key economic indicators, such as GDP per capita, the most developed EU members remain significantly above the EU average (see Fig. 3).

However, the middle group (“new” EU members and five “problematic” EMU countries) is much more diversified. Only in the case of Ireland was there a true catching-up process. This reached almost 180% of the EU average until 2008. Thanks to that, Ireland crossed the boundary between middle-developed and most-developed EU countries. For all other countries in the second group, GDP per capita is below the EU average, and most of them are just above 30% of the EU average.

The third group (laggards), with the exception of Croatia, show very poor performance considering GDP per capita (not higher than 20% of EU average). Although they have been EU members since 2007, Bulgaria and Romania are still far away from the EU average.

There are several reasons for such a very slow catching-up process of East-Central and especially Southeast European countries (second and third group) during the transition period. All the countries from the second and third group suffered from “over-industrialisation” and an underdeveloped service sector during the Communist era. Essential market institutions were missing (protection of property rights and support of innovation and entrepreneurship) and the methods of privatisation were different. The main three types of privatisation were: (1) privatisation by sale (the sale of firms to outsiders), (2) mass privatisation (ownership is transferred at a zero or nominal price to the population at large) and (3) mixed privatisation (sale of firms to insiders, restitution or lease buyout). BENNETT, ESTRIN & URGÄ argue that “the sale privatization method never exerts a significant independent influence on growth, and the method of mixed privatization hardly ever has a



Source: THE WORLD BANK DATABANK

Fig. 3: GDP per capita, % of EU level (Data are in constant 2005 US Dollars to eliminate the impact of inflation on the growth of nominal GDP)

statistically significant effect. In contrast, the method of mass privatization is shown to be positively associated with growth” (2006, p. 672).

In the Southeast European countries (laggards), transition from Socialism to Capitalism was more turbulent than in Central Europe and in some cases followed by disintegration of the country and war. This was especially true for the former Yugoslavia that suffered from a drastic loss in GDP in just a few years. At the beginning of the 1990s, the decline in GDP was enormous and GDP reached only 40% of 1989 levels by 1993 in Serbia and Montenegro (60% in Croatia, and 70% in Macedonia) (GARFIELD 2001).

In Bulgaria and Romania, transition recession was also accompanied by a significant loss of GDP (GDP level in 1992 was slightly above 75% of the 1989 level) (UNITED NATIONS ECONOMIC COMMISSION FOR EUROPE 1999). In Albania, GDP in 1992 was just 64% of the level in 1990 (KNOEMA 2008). In most of these countries, GDP grew after 2000 – with an average growth rate of above 5% until 2009. Unfortunately, growth was not soundly based, but driven by demand increases and financed with cheap foreign loans, privatisation revenues and remittances. In the former Socialist and Communist countries, foreign investors were interested in former state-owned enterprises mainly because they could gain a profit through privatisation. Government policy supported them, because its aim was higher current income for financing the budget deficit – not the modernisation of production capacities, maintaining employment and building export capacities. During the first decade of the 21<sup>st</sup> century, the majority of banks and other financial institutions was privatised. This brought sizeable capital inflows and significant current account deficits. The banks invested heavily in national debt and consumer credit rather than productive investments. Although remittances are an important source of financing in the region (POPOVIĆ 2010), they were not used for capital formation.

General instability – together with high political and military instability – made the region unattractive to foreign direct investment (FDI) unlike the Central European transition economies. Although three of these countries are now EU members (Bulgaria, Romania and Croatia), their economic performances are quite weak, which indicates poor integration within the EU. The laggards, the third group of the countries analysed, had very low sustainable development performances during the accession period and came under increasingly strong pressure from significantly more developed EU and world markets. Their short-term economic prospects are quite weak, and their economies are increasingly vulnerable in the Euro zone crisis.

Transition recession in the middle group of countries (especially Central European and Baltic economies) lasted three to four years, and they started to recover after 1993 or, in some cases, even earlier. Depth of transition recession was much lower – the worst situation was reported in Latvia, where GDP per capita fell by 45%, while in Lithuania, Estonia and Slovakia it fell only by 25%.

The majority of countries in the second and third group are members of the EMU. Considering the current economic situation, significant differences in growth rates affect the formulation and implementation of the Common Monetary Policy. It is carried at the average level. This means that the Common Monetary Policy is not suited for either fast-growing countries or slow-growing countries. This leads to one of the biggest problems in economic convergence within EU – divergences in the real economy. This can easily be

| Countries              | 1990–2015 |        |      |     | 2000–2015 |      |      |     | 2015  |
|------------------------|-----------|--------|------|-----|-----------|------|------|-----|-------|
|                        | Aver.     | Max    | Min  | CV  | Aver.     | Max  | Min  | CV  | $\pi$ |
| Austria                | 2.0       | 3.6    | 0.4  | 0.4 | 1.9       | 3.6  | 0.4  | 0.4 | 0.8   |
| Belgium                | 2.0       | 4.5    | 0.0  | 0.5 | 2.0       | 4.5  | 0.0  | 0.6 | 0.6   |
| Denmark                | 2.0       | 3.4    | 0.5  | 0.4 | 1.9       | 3.4  | 0.5  | 0.5 | 0.5   |
| Finland                | 2.0       | 5.0    | -0.2 | 0.6 | 1.9       | 3.9  | -0.2 | 0.6 | -0.2  |
| France                 | 1.7       | 3.4    | 0.1  | 0.5 | 1.7       | 3.2  | 0.1  | 0.5 | 0.1   |
| Germany                | 1.9       | 5.0    | 0.1  | 0.6 | 1.5       | 2.8  | 0.1  | 0.5 | 0.1   |
| Luxemburg              | 2.4       | 4.1    | 0.0  | 0.5 | 2.5       | 4.1  | 0.0  | 0.5 | 0.1   |
| Netherlands            | 2.0       | 5.1    | 0.2  | 0.5 | 2.0       | 5.1  | 0.2  | 0.6 | 0.2   |
| Sweden                 | 2.0       | 8.8    | 0.2  | 0.9 | 1.5       | 3.3  | 0.2  | 0.6 | 0.7   |
| United Kingdom         | 2.5       | 7.5    | 0.1  | 0.7 | 2.1       | 4.5  | 0.1  | 0.5 | 0.1   |
| Cyprus                 | 2.8       | 6.5    | -1.5 | 0.7 | 2.1       | 4.9  | -1.5 | 0.8 | -1.5  |
| Czechia                | 3.3       | 10.7   | 0.1  | 0.9 | 2.3       | 6.3  | 0.1  | 0.7 | 0.3   |
| Estonia                | 8.3       | 47.7   | 0.1  | 1.4 | 3.7       | 10.6 | 0.1  | 0.7 | 0.1   |
| Greece                 | 5.7       | 20.3   | -1.4 | 1.0 | 2.4       | 4.7  | -1.4 | 0.8 | -1.1  |
| Hungary                | 11.5      | 34.2   | -0.2 | 0.9 | 4.8       | 9.8  | -0.2 | 0.6 | -0.1  |
| Ireland                | 2.1       | 5.3    | -1.7 | 0.8 | 2.0       | 5.3  | -1.7 | 1.1 | 0.0   |
| Italy                  | 2.8       | 6.4    | 0.1  | 0.6 | 2.0       | 3.5  | 0.1  | 0.5 | 0.1   |
| Lithuania              | 3.9       | 23.1   | -1.1 | 1.4 | 2.5       | 11.1 | -1.1 | 1.2 | -0.7  |
| Malta                  | 2.6       | 4.7    | 0.7  | 0.4 | 2.2       | 4.7  | 0.7  | 0.5 | 1.2   |
| Poland                 | 34.4      | 585.8  | -0.9 | 3.3 | 2.9       | 10.1 | -0.9 | 0.9 | -0.9  |
| Portugal               | 3.5       | 13.4   | -0.9 | 0.9 | 2.2       | 4.4  | -0.9 | 0.7 | 0.5   |
| Slovakia               | 5.2       | 13.5   | -0.3 | 0.8 | 3.9       | 12.2 | -0.3 | 0.9 | -0.3  |
| Slovenia               | 6.8       | 31.9   | -0.5 | 1.1 | 3.5       | 8.9  | -0.5 | 0.8 | -0.5  |
| Spain                  | 3.1       | 7.1    | -0.5 | 0.6 | 2.4       | 4.1  | -0.5 | 0.6 | -0.5  |
| Latvia                 | 21.3      | 243.3  | -1.1 | 2.5 | 4.1       | 15.4 | -1.1 | 1.0 | 0.2   |
| Albania                | 18.7      | 226.0  | -0.2 | 2.5 | 2.6       | 5.2  | 0.0  | 0.4 | 1.9   |
| Bosnia and Herzegovina | 2.3       | 7.4    | -1.0 | 1.1 | 2.2       | 7.4  | -1.0 | 1.2 | -1.0  |
| Bulgaria               | 75.0      | 1061.2 | -1.6 | 2.8 | 4.6       | 12.0 | -1.6 | 0.8 | -1.1  |
| Croatia                | 7.2       | 97.5   | -0.5 | 2.8 | 2.5       | 6.1  | -0.5 | 0.7 | -0.5  |
| Macedonia              | 8.4       | 126.6  | -1.3 | 3.2 | 2.4       | 7.2  | -0.7 | 1.1 | -0.2  |
| Montenegro             | 11.3      | 94.9   | -0.7 | 2.1 | 11.3      | 94.9 | -0.7 | 2.1 | 1.6   |
| Romania                | 54.1      | 256.1  | -0.6 | 1.3 | 11.4      | 45.7 | -0.6 | 1.1 | -0.6  |
| Serbia                 | 18.5      | 80.7   | 1.4  | 1.2 | 16.4      | 80.7 | 1.4  | 1.4 | 1.4   |

Source: INTERNATIONAL MONETARY FUND 2016

Tab. 3: Inflation rates measured by average consumer prices, in %

traced through the analysis of the basic economic indicators such as productivity, capital flow, inflation rate and current accounts.

Economic differences that exist between EMU members are the result of various factors including the selection of key policies and growth models. Germany implemented a growth strategy based on exports, moderate wage growth, increased mobility and productivity. Thanks to this, it achieved low production costs and a surplus in the trade balance. In “problematic” EMU states, growth was based on demand and consumption. After joining the Monetary Union, they were flooded with cheap capital from northern countries, which increased borrowing, wrong investment decisions and overinvestment in the private but also the public sector. This led to the accumulation of a growing budget deficit. High capital inflows financed the economic growth rates that were higher than in the countries of the North, but resulted also in higher inflation.

Although also some of the most developed countries had higher inflation levels in the first half of 1990s, they managed to reach monetary stability with rates close to 2%. However, during this period, the middle group of countries had much higher inflation rates than previously until 1999. The highest were in Poland – close to 600% and Latvia (almost 250% in 1992). Together with Estonia and Hungary, they had been struggling throughout almost the entire decade, achieving in the 2000s inflation rates remarkably lower (below 10%). Other countries in this group (with the exception of Poland, Hungary and Czechia) are members of the Eurozone. Until 2015, they had significantly higher inflation rates than the “core” EMU countries. This caused a significant loss in competitiveness. As a consequence, those countries have current account balance deficits due to higher imports of cheaper goods from more competitive countries with lower inflation rates. To finance their rising dependence on imports, they borrowed money from exporting countries. (Those countries used the model of development based on consumption financed by foreign loans similar to Balkan countries.) This led to a constant deterioration of their current accounts.

The third group of the countries (laggards) struggled with very high and unstable inflation during the last decade of the 20<sup>th</sup> century. (In some cases there was even high hyperinflation.) At the peak of hyperinflation (January 1994), the monthly inflation rate in Serbia reached 313 million percent. Inflation was very high in Bulgaria (reaching above 1000% in 1997), Albania (226% in 1992), Macedonia (almost 130% in 1994) and Croatia (close to 100% in 1994).

The majority of the most developed EU countries have surpluses in current accounts. The exception is the United Kingdom – and after the crisis emerged France and partially Belgium. The group of middle developed countries mostly had a deficit in current account until the crisis. After this situation, it reversed thanks to the drop in demand and saving programs. In the last three years, Cyprus and Latvia recorded the highest deficits.

The least developed European countries had very high current account deficits during the observed period. This shows the lack of sustained recovery, of an appropriate development model and competitiveness. The exception is Croatia, where the situation in current accounts has been improving since 2009, and in 2015 it recorded a surplus.

Social and economic EU convergence/divergence can also very well be analysed by the development and implementation of information and communication technologies.

In the period after 1995, EU countries (mostly from the middle group) lagged behind the United States regarding labour productivity and growth linked to investment in information and communication technologies (ICT). The share of ICT investment in EU countries in the GDP was relatively low during the 1990s and still at the beginning of the 2000s. Currently, it characterises a group of EU candidates in the third analysis group. Thus, the socio-economic development of European countries and the convergence/divergence paths are directed by the new digital divide (MITROVIĆ 2015).

In the domain of traditional economy, developed and wealthy countries differed in terms of the availability of raw materials, physical capital (machines, factories, roads) and human capital (skilled labour) from poor ones still in the development process. During the mid-1990s, there was strong polarisation between leaders and the other two groups in terms of access to ideas, knowledge and modern ICT. Countries of the laggard group lack the ideas and knowledge that are used in developed industrial countries to create economic values. Gaps that exist between countries in terms of access to raw materials and knowledge do not exclude each other but are rather complementary. However, the gap that exists between countries, regions and individuals in terms of access to ICT is usually defined as the digital gap.

The significance that the digital divide will have for the further development of the analysed economies can be compared to the importance of the division between the literate and illiterate. The countries from the third group with poorly developed infrastructure to serve information technology (such as Albania), can find themselves in the “technology trap”. The returns on investment in information and communication technologies infrastructure are very low. In such countries, the government argues that investment in basic physical infrastructure is more appropriate. This is the consequence of so-called “traditional poverty” that is still greatly expressed through the lack of basic infrastructure, drinking water, wastewater treatment, health and education services. This raises the question whether these countries should divert the already scarce resources to closing the digital divide.

## 4 Conclusion

At the end of the Second World War, Europe was divided into two groups of countries – East and West – based on their socio-economic model of development. However, this has begun to change during the last 15–20 years, when Eastern European countries went through a radical transformation in economic development, towards regional cooperation and integration into global economic and financial markets. In consequence, Europe is now clearly divided into three groups of countries. Developed Western European countries formed an economic and political union (the leader group). Some former Socialist and Communist countries managed to overcome strict political and economic boundaries after successful transition and joined the EU (the middle group). Unfortunately, some countries still lag far behind those within the developed part of Europe (the laggards).

Would it be justified to say that there is a sort of “Chinese Wall” between these groups? These countries differ greatly in geography, population size, and historical context. All of these issues create specific conditions for economic and social development and make these countries different actors in the European integration process.

Economic and demographic development are strongly connected and it is very hard to define the cause and consequence of these issues. The European population is generally in the process of demographic aging with differences between countries. In terms of demography, it is difficult to draw strict boundaries between the three groups. However, it is possible through the analysis of demographic aspects within each of these groups to recognise a certain correlation between economic convergence and demographic disparities. The structure of the labour force is one of the most important aspects of economic planning and managing as are the dependency ratios of old people and economic population structure.

The aim of the European project is a more balanced regional development through stronger cooperation as well as economic, financial and market integration. Unfortunately, economic data shows sizeable divide among European countries. Economic performances of the ten most developed countries are still unreachable for the majority of countries that belong to the other two groups. Contrary to expectations, there was no convergence of economic performances of EMU members. Instead, a process of polarisation (divergence) of economic results took place between the core countries and the peripheral or southern and southeastern countries. The EMU is not a homogeneous area and a common monetary policy does not fully suit it. EMU has various effects on the macro-economic results of individual countries. The economic results of some peripheral EMU countries are closer to Central European countries.

The worst economic situation (with no catching-up development process) occurs in the Southeast European countries. In Central European countries, opening of boundaries for foreign capital was used to facilitate a serious restructuring of the economy and a re-organisation of companies. In Southeast European countries, however, growth was not driven by productive investments. The world financial crisis of 2007 has highlighted all of the weaknesses of such development concepts and showed their unsustainability. One could say that the last two and half decades represent lost development time.

In the future, the European Union will face major challenges in overcoming economic, developmental, political, demographic, historical and other boundaries. This has to be done to be a true economic and political union.

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