Improving the Competitiveness in CEE Countries by Sustaining the Development of Financial Market

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Abstract: Through this paper we propose to realize an analysis of the global competitiveness index for the Central and Eastern European countries. In order to determine the competitiveness of a country we analyze the main factors that are influencing it. The objective of the paper is to identify if a developed financial market can improve the global competitiveness of countries. Also, as a second objective, we propose to identify which are the main problems faced by the CEE countries in increasing their competitiveness. The results of the paper show that: Estonia, Czech Republic and Slovakia are the countries with the best developed financial market from CEE and are best ranked by the competitiveness index. Also, the countries with problems in the development of financial markets are Hungary and Slovenia. Slovenia is ranked the last from the ten analyzed countries for all sub-indexes. In order to increase their global competitiveness, the countries from CEE have to improve the sector of institutions, labour market efficiency, health and primary education, business sophistication and innovation.

Keywords: Competitiveness; global competitiveness index; financial market development; CEE countries.

JEL Classification: F12; G14.

1 Introduction

The competitiveness of a country's economy and firms has become an important theme. Enhancing external economic relations have increased competition and determined the economies and, implicitly, the economic agents to pay more attention to international competitiveness.

Competitiveness can be analyzed by two dimensions: at national level and firm's level. It is important to distinguish between these two types in order to realize a comparison, but it is also essential to recognise that they are inseparable. Both parts of the competitiveness are more strengthened by communication and globalisation. Competitiveness creates the necessary conditions for sustainable development, for the creation of new production activities and new jobs, and for a better quality of life.

For our paper we have considered ten countries from Central and Eastern Europe (CEE): Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia and Slovenia. Despite considerable differences in the

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performance and policies of the CEE analyzed states, many problems are common. Examples include lack of investment, access to finance, access to markets, the price of energy, and the need for structural change.

In evaluating the competitive position of the selected countries we have used the data from the European Competitiveness Reports, Global Competitiveness Reports (WEF) and the World Competitiveness Yearbooks (IMD).

The firms from CEE countries have fought hard to maintain their competitiveness during the crisis that began in 2008. However, the effects of the crisis are still being felt today. The lack of credit is still observed in many countries. Financing conditions are different across the member states; bank lending is available for solid SMEs in countries that have been less affected by the crisis. In order to enhance competitiveness it is really necessary an industrial renaissance and this is difficult to obtain without industrial investment, which can be achieved by making credit available to business and companies to use credits for investment.

Based on the analysis of the international competitiveness of the economies from the ten considered CEE countries, the primary objective of our survey was to identify if a developed financial market is enhancing global competitiveness of countries. Also, as a second objective, we planned to identify which are the main problems for CEE countries in obtaining competitiveness. To achieve this goal, the paper is structured as follows: the first section presents the state of knowledge in the field; section two focuses on the analysis of global and financial market competitiveness of the CEE countries and the main problematic factors for doing business, revealing the factors by countries; the last section summarizes the conclusions and shows the limits and future directions of research.

2. Literature review

The complexity of contemporary economies, diversification and specialization, technical progress, increased dependency on raw materials, the crises and increasing concerns on risk reduction while maximizing the gains/benefits have redefined the role, dynamics and structure of indicators for assessing global competitiveness.Competitiveness is a concept with many facets, and although it is largely used in recent analyzes there is not an unanimity accepted definition of this concept.

OECD talking about competitiveness says: *As a starting point, competitiveness for a nation will be defined as the degree to which it can produce goods and services that meet the test of international markets, while simultaneously maintaining and expanding the real income of its citizens*(de Vet, 1993). In the World Competitiveness Yearbook we observe another definition: *Competitiveness analyses how nations and enterprises manage the totality of their competencies to achieve prosperity or profit*(Garelli, 2006).

Trabold has defined the international competitiveness of a country by its *ability to sell, its ability to attract foreign direct investment, and its ability to obtain gains* (Trabold, 1995).But in recent research the competitiveness was associated with economic welfare; thus Coldwell takes considers that we can talk about international competitiveness when the *economic welfare of a nation is surpassed by increasing trade flows* (Coldwell, 2000).

Other researches in this field consider competitiveness as a relevant indicator for evaluating countries and regions and as being *the ability to create wealth*(Kao *et al*, 2008; Onsel*et al*, 2008), or a *high standard of living in a country with the lowest rate of unemployment*(European Commission, 2010), or *a set of institutions, policies and factors that determine the level of productivity of a country*(Sala-I-Martin *et al*, 2009).

As shown by Liargovas and Skandalis, the competitiveness of an economy as a whole depends on the competitiveness of the firms from that country; also, the standard of living from a country is increasingly dependent on the competitiveness of its firms (Liargovas& Skandalis, K, 2005). The firms are the engine of an economy (especially the Small and Medium ones), and it is very important for achieving a country's competitiveness to ensure first the competitiveness of firms, because as we mentioned above the competitiveness of firms and countries are strongly related. So, the competitiveness of a firm can be taken as its ability to do better than comparable firms in sales, market shares, or profitability (Lall, 2001). Also, the competitiveness can be interpreted as the ability of a firm to cope with structural changes.

The European Competitiveness Report considers that, in order for European economies to recover from the deepest recession in the post-war history, firms need to be able to prosper and grow and the conditions must be right for new business ideas and start-ups to succeed. Growth of firms is not only a measure of the success of individual businesses but also a measure of the effectiveness of the industrial policy and the quality of the investment environment (European Commission, 2014a).

Taking into account the above analysis and according to the research methodology of the World Competitiveness Yearbook and Global Competitiveness Reports, the factors influencing competitiveness can be divided into four elements: economic performance, government efficiency, business efficiency and infrastructure.

3. Analysis of the Evolution of the Competitiveness in CEE Countries

In order to observe how CEE countries have managed to cope in the face of new economic challenges we relate to the ranking of countries on global competitiveness. This ranking is considered, on one hand, by analyzing the determining factors (called pillars of competitiveness), and on the other hand, by taking into account the development stage of each economy. The pillars o competitiveness used for calculating the Global Competitiveness Index (GCI) are: (1) basic factors (institutions, infrastructure, macroeconomic environment, health and primary education); (2) increase efficiency factors (professional development, efficiency and size of the markets - of goods, labour and financial - receptiveness to new technologies); (3) innovation factors (quality and complexity of business and innovation).

Also for determining the GCI is used the development stage of each economy: a) stage 1 - Orientation on the basic factors of competitiveness; b) transition from stage 1 to stage 2; c) stage 2 –competitiveness focused on efficiency; d) transition from stage 2 to stage 3; e) stage 3 – competitiveness based on innovation.

In order to respond to the question "How much progresses are making the analyzed countries towards increasing their competitiveness?", we can observe the data in table 1, where we present the score of the total competitiveness index obtained by the CEE countries in the last three years and the ranking of countries according to this score.

According to the European Commission the European Union countries are included in different groups regarding their level of competitiveness (European Commission, 2014b). The analyzed CEE countries are divided in two groups. One group contains the countries with modest but improving competitiveness Czech Republic, Estonia, Latvia, Lithuania, Hungary, Poland, Romania and Slovakia. These countries have been successful in improving their performance; however, many of them still perform relatively poorly on productivity and innovation. The second group contains countries with modest and declining competitiveness: Bulgaria and Slovenia. Countries in this group should focus on restoring the competitiveness of their economies since they suffer from both relatively poor performance and limited improvement.

From table 1 we observe that the biggest improvement of the competitiveness, in the last three years, was registered by Romania (0.23 variation of the CGI), Latvia (0.15 variation of the CGI), Bulgaria and Lithuania (0.10 variation of the CGI). Romania had the best ascending trend from the analyzed countries, raising 19 places in the ranking regarding competitiveness in the last three years.

The country that registered worsening of the competitiveness was Slovenia (-0.12 variation of the CGI) which in the last three years has decline 14 places in the ranking of countries regarding competitiveness. The other analyzed CEE countries haven't registered major changes regarding global competitiveness in the last three years.

To see if an improvement of the financing conditions has an important influence on the competitiveness of a country, we have analyzed the score obtained by the CEE countries on the eight pillar of competitiveness: financial market development.

Table 1. The ranking of CEE countries according to the value of the global competitiveness index (GCI)

Country	Rank			Score (GCI)			Variations of GCI		
	2012/ 2013	2013/ 2014	2014/ 2015	2012/ 2013	2013/ 2014	2014/ 2015	row6-row5	row7 – row6	row7 – row5
1	*2*	*3*	*4*	*5*	*6*	*7*	*8*	*9*	*10*
BG	62	57	54	4.27	4.31	4.37	0.04	0.06	0.10
CZ	39	46	37	4.51	4.43	4.53	-0.08	0.1	0.02
EE	34	32	29	4.64	4.65	4.71	0.01	0.06	0.07
HU	60	63	60	4.30	4.25	4.28	-0.05	0.03	-0.02
LV	55	52	42	4.35	4.40	4.50	0.05	0.1	0.15
LT	45	48	41	4.41	4.41	4.51	0	0.1	0.10
PL	41	42	43	4.46	4.46	4.48	0	0.02	0.02
RO	78	76	59	4.07	4.13	4.30	0.06	0.17	0.23
SK	71	78	75	4.14	4.10	4.15	-0.04	0.05	0.01
SI	56	62	70	4.34	4.25	4.22	-0.09	-0.03	-0.12

Source:Data processed after Schwab, 2012, 2013, and 2014.

From the recent financial and economic crisis we have learned the important role of a sound and well functioning financial sector for economic activities. An efficient financial sector allocates the resources saved by a nation's citizens, as well as those entering the economy from abroad, to their most productive uses. In order to have a sound financial market it is necessary that the resources to be channelled to investment project with high rates of return and to be made a proper assessment of risk. To increase the productivity there are also necessary important business investments. Therefore the economies need sophisticated financial markets that can make capital available for private-sector investment from different sources such as loans from a sound banking sector, well-regulated securities exchanges, venture capital, and other financial products. In order to fulfil all those functions, the banking sector needs to be trustworthy and transparent, and the financial markets need appropriate regulation to protect investors and other actors in the economy.

According to the World Economic Forum Global Competitiveness Report 2014-2015, *Estonia* has a competitive advantage in all the analyzed sub-indexes of the financial market development. So we can say that Estonia has the most competitive financial market from the CEE countries, fact sustained also by the ranking of this country on the Global competitiveness index, rank 29 at a distance of 8 place from the next country (Czech Republic) (see table 1). The only problem of this country in achieving competitiveness is on market size (were in ranked 100th from 144 countries).

Table 2. The ranking of countries according to the value of the subindexes regarding financial market development (2014-2015)

Country	*Subindexes 8th pillar: Financial market development*											
	Availability of financial services		Affordability of financial services		Financing through local equity market		Ease of access to loans		Venture capital availability		Soundness of banks	
	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank	Score	Rank
BG	4.2	85	4.0	85	3.0	95	3.0	53	2.6	79	5.0	62
CZ	5.1	38	5.1	31	3.2	84	3.3	36	2.1	42	5.9	24
EE	5.2	36	4.9	38	3.8	48	3.3	40	3.4	26	5.7	39
HU	4.5	62	3.8	98	2.8	106	2.0	126	2.1	121	4.8	73
LV	5.1	40	5.1	32	3.0	96	2.5	96	3.0	48	5.2	56
LT	4.9	45	4.9	39	3.5	67	2.6	91	2.7	73	4.2	113
PL	4.9	44	4.8	44	3.6	59	2.6	89	2.3	99	5.4	51
RO	4.1	93	4.2	66	3.2	83	2.9	59	2.6	78	4.5	91
SK	5.1	39	5.2	26	2.8	107	3.3	39	2.8	57	5.9	20
SI	3.6	125	3.5	120	2.3	122	1.6	140	2.0	125	2.2	144

Source: Data processed after Schwab, 2014.

Czech Republic is the next ranked country on the financial market development, it has a competitive advantage in terms of availability and affordability of financial services, ease of access to loans, venture capital availability and soundness of banks, but is lagging behind in terms of financing through the local equity market.

Slovakia has a competitive advantage in terms of availability and affordability of financial services, ease of access to loans and soundness of banks, but is considerably lagging behind in terms of financing through the local equity market and venture capital availability. Although on the competitiveness of financial market this country is ranked the third from the CEE countries, in the Global Competitiveness Index it is ranked the ninth, fact that shows that even though it has a good financial market it has important problems on other areas such as: institutions, labour market efficiency, health and primary education and innovation, that affect it's international competitiveness.

These three countries best ranked among with Slovenia are included in the third stage of development: innovation driven.

Latvia has a competitive advantage in terms of availability and affordability of financial services and venture capital availability, but is considerably lagging behind in terms of financing through the local equity market, ease of access to loans and soundness of banks. Regarding the Global Competitiveness Index Latvia it is also well ranked being among the third highest ranked countries. The biggest problems of Latvia competitiveness are in the area of market size, innovation and business sophistication.

Lithuania and *Poland* are in top three countries from CEE that provide financing through local equity market, also they are well ranked on the availability and affordability of financial services but are lagging behind on the ease of access to loans and venture capital availability. Regarding the soundness of banks Poland is well ranked but Lithuania has problems in this area being on rank 113 from 144 countries. The main problems Poland faces in enhancing competitiveness are labour market efficiency and innovation.

Lithuania, Latvia, Poland and Hungary are included in the transition stage of development from the efficiency driven stage to the innovation driven one.

Bulgaria and *Romania* are somewhat similar, being ranked in the middle, have a relative good development of the financial market. The main problems that Bulgaria faces in enhancing competitiveness are: institutions, business sophistication and innovation. For Romania the main problems are: institution, health and primary education, labour market efficiency and business sophistication. These two countries are the only ones from the CEE analyzed countries that are included in the stage 2 of development: Efficiency driven.

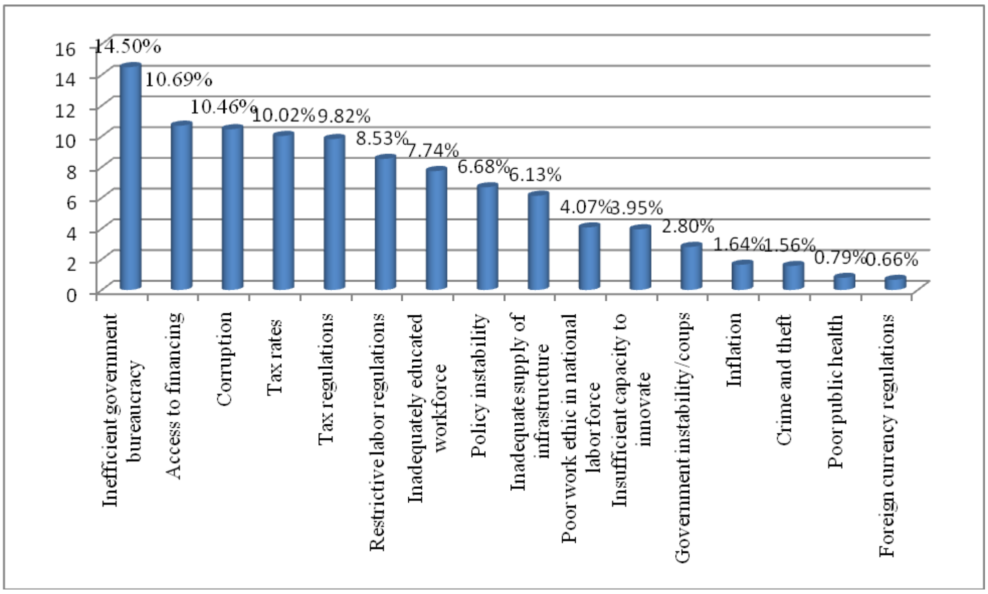
Hungary is relatively good ranked on availability of financial services and soundness of banks, but it is considerably lagging behind in terms of affordability of financial services, ease of access to loans, venture capital availability and financing through the local equity market. Besides this Hungry also have problems on institutions and business sophistication.

Slovenia has serious problems on the area of financial market development, being ranked the last from the CEE countries for all subindexes. On the soundness of banks is ranked the last from the all 144 analyzed countries. Other problem in enhancing competitiveness for Slovenia is the macroeconomic environment and labour market efficiency. From the fourth countries in CEE included in the third stage of development (innovation driven) this is the only country that is so worst ranked. The areas where Slovenia has very good results are: health and primary education, higher education and training.

In order to see if the availability of financial resources for firms has an important influence on the competitiveness of country, we have analyzed the most problematic factors for doing business in CEE in 2015. From the list of mentioned factors, the respondents were asked to select the five most problematic for doing business in their country and to rank them between 1 (most problematic) and 5. The bars in figure 1 show the mean of the responses for the ten countries analyzed from CEE. The top five problems faced by firms in CEE countries traditionally include inefficient government bureaucracy, access to finance, corruption, tax rates and tax regulations. Thus, two out of five problematic factors refer to taxation.

On an analyzes on countries we observe that access to finance is not a major problem for Slovakia, Czech Republic and Estonia, the countries that are best ranked in the access to loans sub-index (see table 2). For Romania and Slovenia the access to finance is mentioned as the most pressing problem for doing business.

Figure 1. The most problematic factors for doing business in CEE 2015



Source: Data processed after Schwab, 2014.

The business environment has an important influence on the development of the private sector and economic growth—end thus on the creation of jobs end better livelihoods. Where well designed end properly implemented, regulatory reforms can promote private sector growth by eliminating bureaucratic obstacles, reducing cost end time constraints to doing business and improving the efficiency of level institutions. They can also have an important impact on perceptions of an economy's business environment and the international competitiveness of that country (World Bank, 2015). Thus, in order to increase the competitiveness of the CEE countries we consider that it is very important to improve the business environment from these countries especially by improving the access to finance for the enterprises.

4. Conclusions

Competitiveness creates the necessary conditions for sustainable development, for the creation of new production activities and new jobs, and for a better quality of life. So, enhancing competitiveness should be a very important objective for the countries, especially for those with emerging economies.

From the analysis realized in this paper we observed that, despite considerable differences in the performance and policies of the ten CEE considered states, many problems are common. These problems are: lack of investment, access to finance, access to markets, the price of energy, and the need for structural change.

Thus, we can conclude that in order to enhance competitiveness it is really necessary a development of the industrial sector and this can be obtained only using industrial investment, which can be achieved by making credit available to business and companies to be stimulated use credits for investment.Analyzing the eight pillar of competitiveness, regarding financial market development, we observe that Estonia, Czech Republic and Slovakia are the countries best ranked. These countries are also included in the third stage of development: innovation driven, have good results on the value of the Global Competitiveness Index. The countries with problems in the development of financial markets are Hungary and Slovenia. Slovenia is ranked the last from the ten analyzed countries for all sub-indexes. Also, on the soundness of banks it is ranked the last from the all 144 analyzed countries.

The biggest common problems in enhancing global competitiveness for all ten analyzed CEE countries are in the areas of institutions, labour market efficiency, health and primary education, business sophistication and innovation.Regarding the activity on the financial market, an important factor that sustains the competitiveness is the ease of doing business. Analyzing the most problematic factors for doing business in CEE in 2015 we observe that the second biggest problem, after inefficient government bureaucracy, is the access to financing, and, also, two out of five problematic factors refer to taxation.So we observe that the financial market development and the ease of accessing finance have a major role on a country's international competitiveness. The CEE countries with a more developed financial market that offer an easier access to finance for the firms have a more competitive economy (according to the value of the global competitiveness index).

But, there are also countries with good results on the competitiveness of financial market and good access to finance but, on the global competevieness index, are ranked among the lasts, fact that shows that is not sufficient to have good financial market, they also have to improve other basic requirements (Institutions, Infrastructure, Macroeconomic environment, Health and primary education).

Limitations and future directions of research. The research analyses only a reduced number of countries, and on a short period of time. To overcome this limit in future research we will consider the analysis of all the European Union countries, and maybe to realize a comparison between areas of development. We also plan on making projections on the competitive potential of the EU Member States.

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