

Competitiveness in an Enlarged Europe: The Role of the EBRD

*La competitività europea dopo l'allargamento:
il ruolo della BERS*

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Sommario: Lo scopo di questo lavoro è quello di illustrare il ruolo svolto dalla Banca Europea per la Ricostruzione e lo Sviluppo (BERS) nei guadagni di competitività ottenuti dai paesi di operazione della Banca, otto dei quali sono recentemente divenuti membri dell'Unione Europea. Nella prima parte si esamina la competitività dell'Unione Europea dopo l'allargamento del 2004. L'analisi si basa prevalentemente sugli indicatori di competitività sviluppati dalla BERS. La seconda parte guarda al ruolo svolto dalla BERS nel processo di transizione verso l'economia di mercato di otto dei dieci nuovi paesi membri UE. Gli esempi forniti indicano come un'istituzione quale la BERS possa contribuire a colmare il divario di competitività fra nuovi e vecchi paesi UE.

Keywords: Competitiveness, EBRD.

Introduction

This paper is based on the assumption that the two processes of competitiveness enhancement and advancement in transition require broadly similar incentives and are brought forward by broadly similar policy measures. This hypothesis stays clear of any presumption that the equation “competitiveness equal transition” is bullet-proof from a scientific viewpoint, or of any ambition to establish causality relationships.

However, as we shall see, there is considerable overlapping between the factors, policies, institutions, market sectors and efficiency gains, which are targeted when trying to enhance competitiveness on the one hand and to foster the process of transition on the other.

The transition indicators developed by the EBRD are built largely on the same intellectual underpinning as several competitiveness indicators, so that it is reasonable to consider the former as a meaningful proxy for the latter. The analogy between transition and competitiveness indicators can cause a few eyebrows to be raised in the academic world, yet the aim of this paper is to provide a contribution to the debate on competitiveness from an operational vantage point.

1. Definition of Competitiveness

Competitiveness is not an easy concept to pin down. As put by Lawrence (2002): “Competitiveness”, particularly with reference to an entire economy, is hard to

define. Indeed, competitiveness, like love or democracy, actually has several meanings” (Lawrence 2002). The bad news is that we will not be able to provide a definition of competitiveness that everybody would agree upon. The good news is that the subject of this paper is not love or democracy.

Lawrence (2002) gives justice to misconceptions about competitiveness when saying “The most important concept of competitiveness is not [...] how national performances compare or even how well countries perform in international trade. The critical issue for each economy is whether it is making the best use of its resources.” In other words, competitiveness concerns understanding the sources of a country’s economic growth and the way to best exploit these sources by ensuring sustained input productivity improvements. When currency devaluation, state subsidies to sectors of the economy and artificially low wages are used to improve a country’s performance on international trade – often used as a synonym of competitiveness – the most likely effect is holding down prosperity. Measures that do not contribute to the most productive use of resources, and ultimately do not contribute to achieving better living standards as measured by real income per capita, have very little to do with increased competitiveness.

The European Commission’s “European Competitiveness Report” defines competitiveness as “a sustained rise in the standards of living of a nation and as low a level of involuntary unemployment as possible.” This concerns mostly the effects of competitiveness but does not tell much about the factors shaping competitiveness and growth in an economy or influencing country performance compared to other countries (European Commission 2004a).

The World Economic Forum’s (WEF) “Global Competitiveness Report 2005-2006” provides the following definition: “competitiveness is defined as that collection of factors, policies and institutions which determine the level of productivity of a country and that, therefore, determine the level of prosperity that can be attained by an economy. [...] A more competitive economy is one that is likely to grow faster over the medium to long term” (WEF 2005, 3).

The WEF’s definition provides the best fit for the purpose of this paper. Specifically, it is the relative importance of factors such as economic reforms, institutional structures, governance, and labour market institutions that allow for a country the best use of its resources and make it an attractive destination of foreign direct investments. We shall rely on this definition to provide a survey of EU competitiveness - both EU 15 and EU 25 - *vis à vis* the rest of the world and to present the EBRD’s contribution for enhancing the competitiveness of its countries of operation.

2. EBRD’s contribution to competitiveness: the ‘transition impact’

2.1 The Bank The EBRD is the youngest among the existing Multilateral Development Banks, i.e. those international financial institutions owned by governments, which act as specialised long-term lending intermediaries for developing countries at global and regional levels. The EBRD was set up in 1991 to foster the transition to market-oriented economies in its countries of operation in Central and Eastern Europe and the former Soviet Union.

The mandate of the EBRD largely coincides with enhancing competitiveness as defined by the WEF. In its 15 year of experience, the Bank has contributed to improving the collection of factors, policies, and institutions that determine the level of prosperity of its countries of operation. The Bank has been active in a wide range

of areas, such as the financing and strengthening of the banking system, the financial and non-financial support to business start-ups and small enterprises in general, privatisation and restructuring of large enterprises, and commercialisation of infrastructure. It has helped, through its intense policy dialogue activity and technical assistance, to significantly improve the commercial legal framework in the region. Bankruptcy law, concessions, corporate governance, financial market regulations, secured transactions, telecommunications and arbitration are all areas in which the EBRD has contributed significant improvements in many countries. These activities aim at equipping EBRD's region with the institutional framework required to successfully compete in the global market.

2.2 Transition Impact¹ The EBRD has developed a sophisticated system of measuring outcomes and outputs of its activities based on the concept of 'transition impact'. Transition impact is defined as the likely effects of a project on a sector or economy, which contribute to their transformation from central planning to well-functioning market-based structures. Transition impact is measured throughout the entire life of each EBRD project.

The Bank has identified the three main dimensions of transition impact, i.e.: i) project contributions to the structure and extent of markets; ii) project contributions to the institutions and policies that support markets; and iii) project contributions to business behaviour and practices.

A project can influence the structure and extent of markets in several ways. It can promote greater competition in its sector of activity, for instance making possible the entry of new foreign banks; the supply of higher quality products; the consolidation/restructuring of existing nonviable banks/firms; and the participation of additional domestic market players. This is likely to improve the efficiency with which resources are allocated and utilised, demand is satisfied and innovation is stimulated.

A project can also facilitate market expansion by helping to set up business relationships in other markets on a more competitive basis: for instance, through the development of input suppliers and distribution networks and through increased and better financial intermediation. A project can also promote international or regional integration of economic activity through trade integration and cross-border infrastructure investments.

In terms of institutions and policies that support markets, a project can contribute to more widespread private ownership through privatisation or new private provision of goods and services. A project may also help to create or reform both governmental or private institutions, and policies and practices that promote market functioning and efficiency.

As for business behaviour and practices, projects can also contribute to providing and improving the skills required for well-functioning market economies where such skills are spread so as to benefit non-project entities.

Important demonstration effects from innovation can be achieved through the following: the introduction of new products and processes (i.e., leasing, new environmental technology); new ways of successfully restructuring companies and institutions (i.e., pre-privatisation environmental restructuring); new ways and instruments to finance activities (i.e., mortgage bonds, warehouse receipts).

Finally, by setting standards for corporate governance and business conduct, a project may contribute to the spreading of behaviour and attitudes that enhance the legitimacy

¹ Details on transition impact and transition indicators are based on internal EBRD guidelines.

and functioning of the market economy (i.e., integrity checks, financial disclosure, improved board procedures, compliance with EU environmental standards).

2.3 Transition Indicators Assessments of project outcomes are provided also at the country level. Progress is measured against the standards of industrialised market economies covering the main elements of a market economy – markets and trade, enterprises, infrastructure and financial institutions. In brief, every country receives each year a numerical score ranging from 1 (little or no progress from a planned economy) to 4+ (standards of an advanced market economy), for various transition indicators. There are three indicators for enterprise reform (small-scale privatisation, large-scale privatisation and governance and enterprise reform), three for markets and trade (price liberalisation, trade and foreign exchange liberalisation and competition policy), two for financial institutions (banking reform and interest rate liberalisation, and securities markets and non-bank financial institutions) and one for infrastructure, which is an average of five separate scores for different areas (electric power, roads, railways, telecommunications and water and waste water).

The EBRD transition indicators provide a rather ‘crude’ measure of a country’s progress in its process of transition, as they are a set of mainly qualitative indicators used to track developments in reforms, and the score they produce reflects the assessment of the Bank’s country economists. A few issues arise when using the indicators in empirical work.

Falcetti et al. (2005) flags, among other issues, “the bounded and ordinal nature of the indicators”. This implies that marginal variations are not captured once the maximum score is achieved. In addition, scores do not have cardinal qualities, and the difference between a score of 1 and 2, for example, is not necessarily the same as between 2 and 3. As evidence shows, countries tend to be quicker at making the first steps but much slower at climbing the full ladder. Falcetti et al. (2005) also warn against the “high correlation amongst the different indicators, both cross-sectionally and across time” that makes it impossible to consider all of them in a regression because of multicollinearity (Falcetti et al. 2005).

Nonetheless, the transition indicators have been used in many studies about the relationship between reforms and growth in transition. They have proved to be a very useful tool for the EBRD, providing the Bank with crucial information about the extent of structural and institutional reform implementation needed for the region to continue in their catching up with advanced market economies.

3. Competitiveness in Europe: the EBRD’s experience

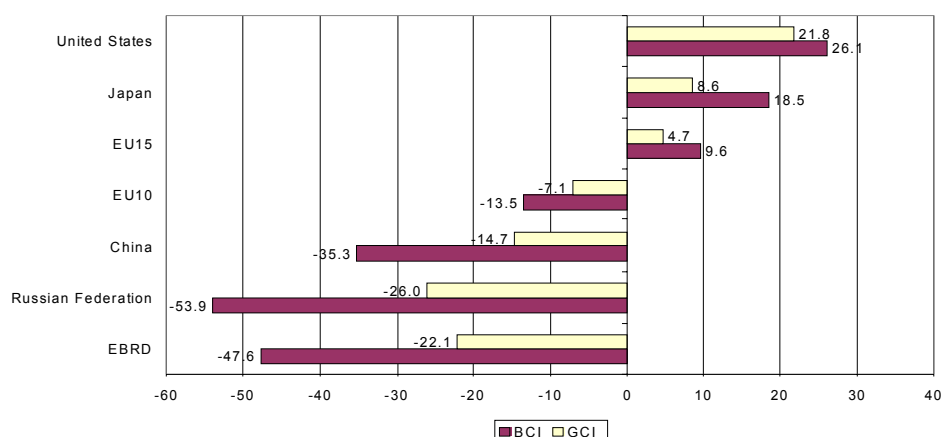
3.1 EU performance How competitive is the EU, before and after enlargement, *vis à vis* its main competitors? In March 2000, European leaders approved the so-called Lisbon strategy, whereby the EU would commit to becoming “the most dynamic and competitive knowledge-based economy in the world” by 2010 (European Commission 2000, quoted in European Commission 2004b). Six years on, this ambitious goal seems increasingly less realistic. In fact, the growth gap with North America and Asia has widened and GDP per capita in the EU 25 reached 65 per cent relative to the US by 2005. Similarly, labour productivity per person employed reached 73 per cent; unemployment rate was about 5 per cent in the US against 8.6 per cent in the EU 25 (Koopman 2006).

Is enlargement the cause of the slow progress of the European Union towards becoming a more competitive bloc? The most immediate consequence of the enlargement process is that the European Union population has become 125 per cent of the population in the EU 15, whilst the GDP per capita is slightly above 80 per cent of EU 15 average. In practice, a more populated but poorer area. However, enlargement does not change the European Union's relative ranking *vis à vis* its major competitors – whether considering the enlarged Europe of 25 members or the original 15 old members, Euroland still ranks below both the US and Japan (WEF 2005).

In particular, the WEF's "Growth Competitiveness Index" (GCI), which measures competitiveness on the basis of the quality of the macroeconomic environment, the quality of public institutions, and the level of technological change and innovation, shows a very marginal loss of competitiveness of the EU25 relative to the EU15 (see Chart 1). However, the loss of competitiveness of the EU25 is more marked on the microeconomic side. The "Business Competitive Index" (BCI), developed by the WEF as a complement to the GCI, points to a wider gap than for the GCI in order to measure the competitiveness of companies in terms of productivity, level of managerial and technological innovation, and quality of the business environment. The WEF points to the weak operations and strategies of companies from the new EU member states as a major factor for their lack of competitiveness (WEF 2005).

The Kok report on the Lisbon strategy identifies in accelerating employment and increasing productivity the recipe to improve living standards in Europe, especially as unfavourable demographics shrink the labour force. The evidence, though, is that EU average annual labour productivity declined from 2.1 per cent during the period 1987-1995 to 1.4 per cent during 1995-2004, whilst US productivity accelerated from 1.1 per cent to 2.5 per cent in the same period (Van Ark 2005). Contrary to 'old Europe', the new EU member states saw their average labour productivity rise by 4.2 per cent from 1995-2004. In the period 2000-2004, after the launch of the Lisbon strategy, average labour productivity increased by a meagre 1.1 per cent in the EU15 against the 4.5 per cent in the new EU10, ranging from -0.2 per cent for Italy to 11.5 per cent for Lithuania. This is just an indication, but a compelling one, of the enormous growth potential of the region, a potential that the EBRD has relentlessly tried to unlock.

Chart 1. Percentage change in competitiveness vs. EU25



Source: WEF 2005.

Eight of the ten new EU members are countries of operation of the EBRD. As shown in Table 1, these eight new EU countries have made striking progress on the EBRD's

transition indicators. At the country level, the prospect of EU accession has triggered a surge in economic reforms that has led some of the then accession countries to pursue economic policies even more liberal than those of several of the old members. At the enterprise level, enlargement had in many respects already taken place before May 2004; intensive trade relations of candidate countries with the EU were already a reality, in some cases accounting for more than two-thirds of total trade; there was strong integration of businesses into the EU, in most cases due to competitive advantages deriving from lower labour costs (EBRD 2005).

Table 1. Transition indicators scores 2005

Countries	Enterprises			Markets and trade			Financial institutions		Infrastructure infrastructure reform
	Large-scale privatisation	Small-scale privatisation	Governance & enterprise restructuring	Price liberalisation	Trade & foreign exchange system	Competition policy	Banking reform & interest rate liberalisation	Securities markets & non-bank financial institutions	
Czech Republic	4	4+	3+	4+	4+	3	4	4-	3+
Estonia	4	4+	4	4+	4+	3-	4	3+	3+
Hungary	4	4+	4-	4+	4+	3	4	4	4-
Latvia	4-	4+	3	4+	4+	3-	4-	3	3
Lithuania	4	4+	3	4+	4+	3	4-	3	3-
Poland	3+	4+	4-	4+	4+	3	4-	4-	3+
Slovak Republic	4	4+	4-	4+	4+	3	4-	3-	3-
Slovenia	3	4+	3	4	4+	3-	3+	3-	3

Source: EBRD 2005.

3.2 Determinants of performance:

What factors determined such an impressive performance of the new EU members? While the debate is still open and many theories have been put forward into literature, we will attempt a summary of the most recurrent determinants of the performance of the new EU members among EBRD's countries of operation.

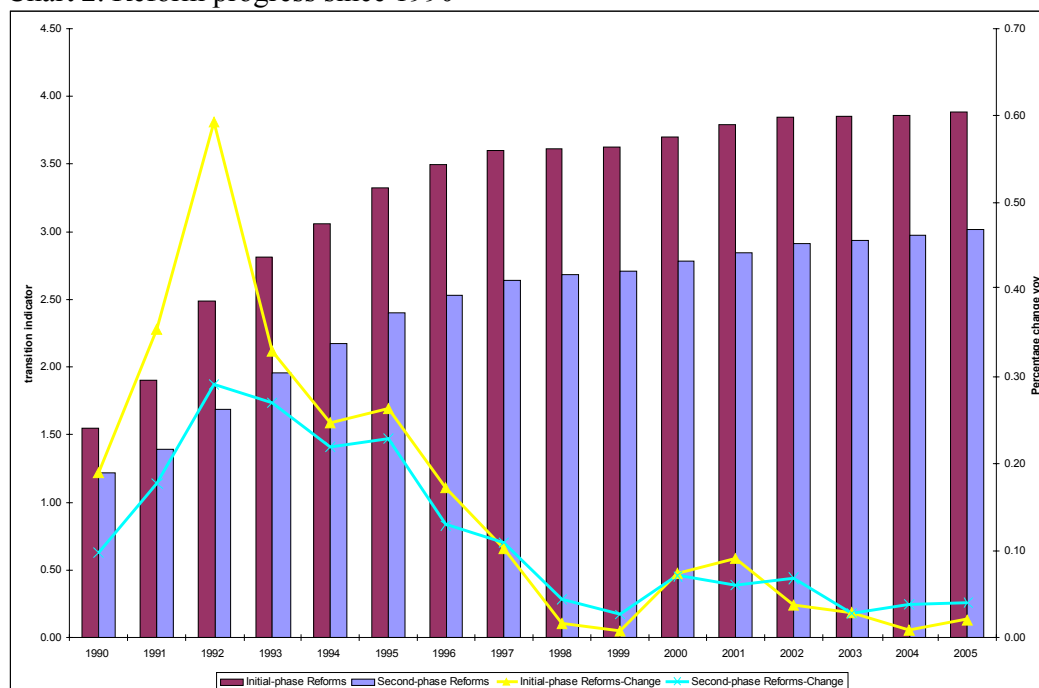
Reforms The evidence of 15 years of transition is that there is a clear link between reforms today and growth in the future. Thanks to their commitment for reforms, the EBRD's eight countries of operation, that recently joined the EU, have grown at a strong and sustained pace in the latest years outperforming the world economy and catching up with the richer members of the EU 15. However, further rapid growth and investment are needed to approach EU-15 living standards. The key is to enhance economic competitiveness by advancing structural reforms, enhancing the business environment, reforming public administration and the judiciary, and enhancing labour flexibility and skills.

Chart 2 shows how the EBRD's countries of operation have gone a long way in evolving into functioning market economies. During the first years of the transition process, progress in reform was fast, with initial-phase reforms (i.e., small-scale privatisations, prices liberalisation and trade and foreign exchange liberalisation) outpacing by far the more demanding institution-building reforms.

Governance The EBRD (together with the World Bank) conducts periodic surveys of enterprises to verify their perception of quality in economic governance, meaning both business institutions and property rights issues. Table 2 shows changes in seven aspects of the business environment between 2002 and 2005. With the exception of

labour regulations, perceptions in 2005 point to improved economic governance throughout the region, although with some noteworthy country variation. The EU accession process is deemed to have acted as a powerful stimulus for reform.

Chart 2. Reform progress since 1990



Source: EBRD 2005.

Table 2. Changes in perceptions of economic governance

Country	Judiciary	Crime	Corruption	Customs and Trade Regulations	Business Licensing and Permits	Labour Regulations	Tax Administration
Czech Rep.	0.58	0.24	0.50	0.48	0.24	0.65	0.77
Estonia	-0.39	-0.07	-0.01	-0.02	-0.25	0.66	-0.33
Hungary	0.11	-0.03	0.03	-0.07	0.03	0.23	0.24
Latvia	-0.06	-0.17	-0.19	-0.61	-0.12	-0.11	-0.11
Lithuania	0.05	-0.17	0.01	-0.09	0.09	0.25	-0.28
Poland	-0.15	-0.30	-0.32	-0.34	-0.04	-0.28	-0.13
Slovakia	-0.67	-0.45	-0.70	-0.75	-0.67	-0.32	-0.54
Slovenia	0.01	-0.12	-0.12	0.00	-0.01	0.21	0.68

Note: Notes: Firms were asked to report how problematic a series of governance dimensions are for their business on a scale of 1 (no obstacle) to 4 (major obstacle). The table reports the average change between responses received in 2002 and 2005. A negative sign indicates an improvement in perceptions of that dimension of the business environment. Statistically significant variations are shown in bold. Statistical significance was determined according to a two-tailed two sample t-test with a cut-off at 90 per cent confidence interval. Source: BEEPS 2002 and 2005.

One of the most notable weaknesses of the transition countries was the very poor quality of public administration. An efficient and streamlined public administration is one of the main keys for competitiveness. This is especially true because of the impact that the functioning of governments has on productivity in the private sector

through regulations, taxation and government spending on R&D, infrastructure and innovation (European Commission 2004a). An equally important challenge is the judiciary reform. The perceptions of effectiveness of the judiciary reform show some signs of improvement, although the confidence in the courts as a means of dispute resolution or enforcement of contracts and property rights is still low (EBRD 2005).

Labour Market Another equally important aspect of competitiveness is labour market flexibility and job creation. In this respect, as shown in Table 2, perceptions are, on average, negative throughout the EBRD's region of operation, including the 8 new EU member countries. This comes as a result of increased regulation relating to employment protection as transition progresses. The capacity to attract FDI because of competitive wage and corporate tax rates reduces over time, resulting in the most dynamic and privately-owned businesses not being able to realise their full growth potential.

Historically, most of the transition countries had high levels of education. The skills acquired under the past regime appear, however, to be less relevant in meeting the requirements of the new economic system that is gradually shaping up. This hinders competitiveness and the problem is slowly being addressed by way of innovation and skills enhancement, often assisted by foreign direct investment.

Foreign Direct Investment It is widely recognised that foreign direct investment (FDI) plays a key role in the transition process. During the early years of transition, FDI has sustained aggregate demand, thus enabling greater utilisation of production capacity, and has offset falling domestic saving rates by directly adding to available savings. FDI has also brought benefits in terms of price decrease, quality of output and higher productivity, stemming from unrestricted access to credit and better management. FDI has also positively contributed to the development of a transparent and predictable legal basis for contractual relationships.

A most important source of FDI in transition countries has been the wave of major privatisation deals that have characterised the transition process. In most cases, these deals, and often privatisation programmes, would not have been possible without the capital contribution and ability to turn around uncompetitive enterprises provided by FDI. Similarly, FDI is broadly deemed to play a key role in the diffusion of technological progress, know-how, management and marketing skills, as well as higher safety and environmental standards.

3.3 Contribution to FDI in the region: the EBRD projects

One of the most important contributions the EBRD has made to the establishment of market economies and promoting competitiveness in its region of operation is the Bank's participation in the processes of restructuring, commercialisation and privatisation of local firms. The EBRD has contributed significantly to cumulative FDI, being the largest single investor in its region of operations. In the new EU member states, cumulative FDI amounted to EUR 164.2 billion, or EUR 2,254 per capita between 1989-2005. At the end of 2005, the total cumulative EBRD commitments in the new EU member states, including all type of finance, amounted to EUR 9.2 billion, and leveraged EUR 25 billion.

By mobilising FDI, the EBRD has conspicuously contributed to improving competitiveness in its countries of operation. Main targets have been the development of modern banking sectors, which have fuelled the rapid increase in financial intermediation across the region by supporting the modernisation of infrastructure

services, particularly in the municipal and transport sectors; contributing directly to improving enterprise performance, through the support of foreign investment in sectors still dominated by un-restructured state-owned conglomerates (see Box 1). Through its projects, the EBRD has aimed at creating the right incentives for market entry and exit of firms, thus contributing to more competitive sectors and business environments.

Box 1. Examples of EBRD projects

In the *Czech Republic*, the Bank subscribed EUR 10 million new capital in SKV, a Prague based manufacturing subsidiary of Siemens. SKV is a newly established subsidiary of Siemens AG, which purchased assets of the bankrupt traditional Czech manufacturer of trams and locomotives, CKD DS, re-employed a large number of its former employees of CKD DS and started to restructure the operations of the company. As a result of the restructuring, SKV became an integral part of the Train Division of Siemens. The Bank's proceeds financed investments into technology and technical upgrade of the plant needed to bring it up to top industry standards. The transition impact of the project was rated good with high risk and stemmed from the demonstration effect of successfully restructuring a major industrial concern through a strategic investor. The introduction of new products, increase of share of higher value added products and engagement in research and development also contribute to a much needed increase of competitiveness of the Czech industrial sector.

In *Hungary*, the Bank contributed 20 per cent of the total fund capital of Euroventures Hungary III L.P. (the Fund), a Hungary-focused private equity fund. The Fund invests in medium-sized companies in the buy-out, expansion or development stage with the objective of achieving long-term capital growth. By means of a specially designed investment vehicle, the EBRD investment allowed local pension funds to access private equity investment for the first time. The transition impact of the project was rated excellent with high risk. The sources of transition impact were several and included increasing the amount of active equity available to medium-sized companies, and filling the supply gap for equity supply. In addition, the Fund contributed to the sustainable development of the private equity sector in Hungary. Finally, using the specially designed investment vehicle, the Hungarian pension funds will be able to invest in the private equity market in Hungary and the region. Investing in alternative asset classes such as private equity also contributed to the development of more sophisticated investment policies and practices of the Hungarian employees' pension funds.

In *Slovenia*, the Bank provided an equity investment of between 5 and 13 per cent in Nova Ljubljanska banka (NLB), largest banking group in the country, as part of NLB's privatisation. The NLB Group accounts for more than 45 per cent of the banking sector and comprises 108 domestic branches, seven subsidiary banks and two associate banks in Slovenia, as well as subsidiary and associate companies offering other financial services. The Bank's financing aimed at improving NLB's performance by achieving operational efficiencies, introducing new banking products and services and enhancing the corporate governance standards. The proceeds from the planned capital increase were used to fund NLB's further operational integration of its subsidiary banks and the bank's regional expansion. The transition impact of the project was rated excellent with high risk and stemmed from its contribution to developing the Slovenian banking sector, enhancing competition in the market and strengthening NLB's corporate governance standards. The successful completion of NLB's privatisation process strongly contributed to the smooth integration of the Slovenian banking sector in the European Union market.

In *Estonia*, the Bank provided equity and subordinated shareholder loan for a total EUR 19 million to AS Estonian Cell, a special purpose company, to construct and operate a green-field aspen Bleached Chemi Thermo Mechanical Pulp (BCTMP) mill with a daily capacity of 500 tonnes. The transition impact of the project was rated good with high risk. The project provided technology transfer by introducing to the country the first new pulp mill since 1960's with modern, state-of-the-art technology. By using under-utilised aspen resources, the mill added value to a local low cost raw material before exporting. The project also catalysed the market expansion for Estonian wood supply industry and contributed to inducing further competition. The significant local sourcing also had beneficial impact on the local forestry sector as the Sponsor's commitment to use sustainable wood procurement and standard terms and conditions for suppliers helped spread such practices in the region.

Source: EBRD public website.

Concluding remarks and recommendations for policy making

A well functioning market economy is characterised by a sound market structure (i.e. competition), a solid legal and regulatory framework, and good business conduct. As shown by the analysis above, Central European markets are increasingly competitive, although challenges remain in terms of market conduct (i.e. corporate governance, environmental, health and safety) and in the uneven implementation of regulatory rules. In addition, the business environment is improving but has not yet reached the level of mature market economies in terms of institutions, business regulation, infrastructure, and access to finance. A few indications can be drawn from the EBRD's activity in its countries of operations in order to bridge these remaining gaps and improve overall competitiveness to reach the levels of a modern functioning economy.

The first point to be made concerns the Bank's involvement in the processes of privatisation in the region. Transition economies were dominated, almost by definition, by the pervasive presence of large, inefficient, unaccountable and non-transparent state-owned enterprises. The EBRD has participated intensively in the privatisation of such enterprises, always trying to secure the political acceptability and legitimacy of the processes and the involvement of new capital, know-how and expertise. The way privatisations are carried out has proven to matter far more than the speed of the process. Insider and crony privatisations only bring about high concentration in asset ownership and weak impact on firm performance.

A second element of the EBRD's activity has been the steady commitment to reducing firms' entry and exit barriers. The largest contribution to the growth of jobs, output and productivity in the region has been brought about by new private firms and start ups. New firms can only enter the market if exit mechanisms, i.e. hard budget constraints, bankruptcy laws, etc., exist for inefficient enterprises. The same line of reasoning applies to the banking and financial sector. Financial intermediation is the key to the development of the real economy. Privatisation of existing banks, combined with liberalisation of access of foreign banks, has deepened the level of financial intermediation, whilst introducing superior banking technology and capital base.

In addition, the EBRD's private sector operations focus on sectors where returns to private investments depend significantly on government policies and practices – infrastructure, financial sector, enterprise restructuring and privatisation, etc. By mitigating the risks associated with such policies and practices, the EBRD strengthens the private investment response to reforms. Similarly, investments supported by the EBRD can generate positive externalities like the strengthening of the functioning of markets, the improvement of corporate governance and business practices, etc.

Finally, what remains one of the most serious challenges for transition countries, including the new EU member countries, is the improvement of energy efficiency. Former centrally planned economies systematically under-priced energy and natural resources as a part of misdirected social and industrial policies. Improving energy efficiency is a key to enhanced competitiveness, to the security of supply and to lower greenhouse gas emissions. Energy efficiency investments by large industrial energy consumers and an increased emphasis on energy efficiency in electricity generation, transmission and distribution, and district heating have constantly constituted an explicit target for the EBRD.

As a result, the key to productivity and competitiveness enhancement in the EBRD's countries of operation lies in a mix of policies aimed at favouring the adjustment

process towards a new industrial structure and a new system of resource allocation. Promotion and implementation of such policies - i.e. sound macroeconomic management, fostering technological change and innovation, building market institutions, targeting a higher education system - rests mostly with the governments themselves. Multilateral Development Banks (MDBs) like the EBRD are best placed to help governments, in the design and monitoring of reform conditions for financing, thanks to their multilateral shareholding structure. By including the countries of operation, MDBs shareholding structure makes the acceptance of conditionality and monitoring clauses politically more palatable than if the same conditions were imposed by outside entities.

The EBRD is one of the instruments at the disposal of policymakers to try and tackle the difficult issue of raising competitiveness. The Bank targets a specific set of countries and it is not automatic that the EBRD's *modus operandi* would prove successful for a different set of countries. However, I do believe that 15 years of the Bank's activity provide a wealth of information, expertise and lessons for the complex task of raising a country's competitiveness.

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