The European Union absorbs 63% of exports from the new European countries. Germany leads with a quarter of overall trade, followed by Italy, which is more oriented towards the Balkan region. The turning

Competitiveness and exports in the New Europe

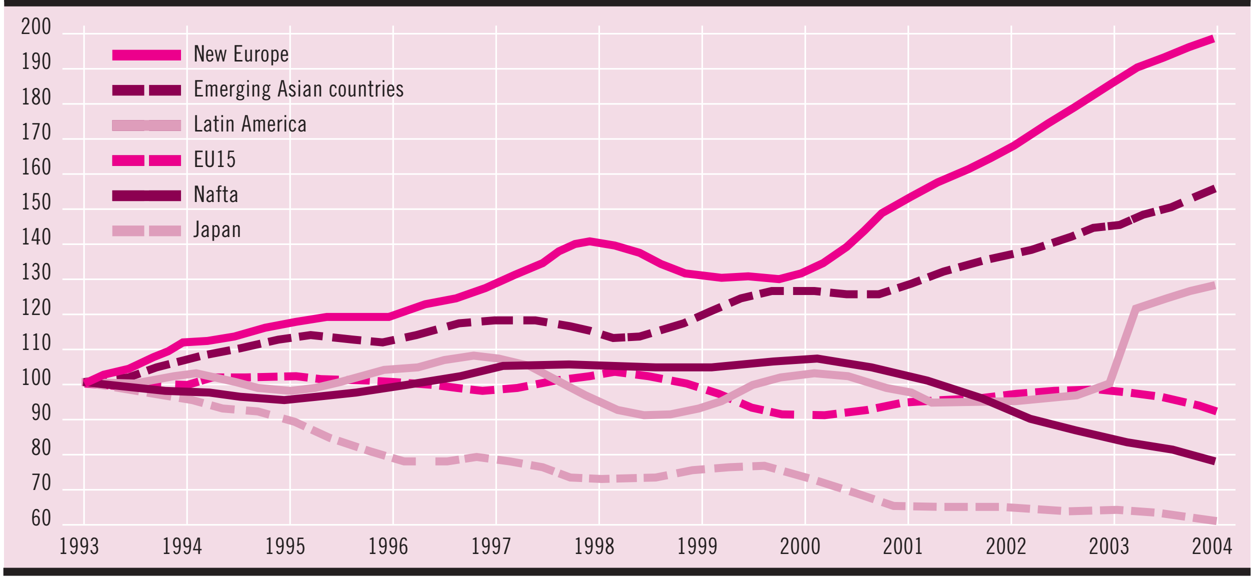
ECONOMY 1

by Matteo Ferrazzi

point has been the ability to adapt the industrial structure to the new competitive scenario, but the development of relations with more evolved economies has also allowed the region to...

Over the last 15 years the growth of international trade has seen the emergence of an increasing number of countries, many of which are "developing" or "emerging" as producers and exporters of manufactured goods. They have become particularly seasoned competitors of the older industrialised countries. The emerging countries of the so-called New Europe have also played a relevant role in this process – countries that are already EU members, such as the Czech Republic, Hungary, Poland, Slovakia, Slovenia and the three Baltic nations as well as the "convergent" countries (Bulgaria, Rumania, Croatia and Turkey). In fact, in just over a decade these countries have been able to double their importance in international trade. This evolution is a clear signal of the improvement in their competitive capabilities. Exports from the countries of the New Europe currently amount to nearly 4% of world demand – a little less than France and more than Italy – and the growth of their presence in trade has been even more substantial than that of all the emerging Asian countries combined, China and India included (*Figure 1*).

1. EXPORT SHARE TREND FOR VARIOUS AREAS AND COUNTRIES (1993=100)

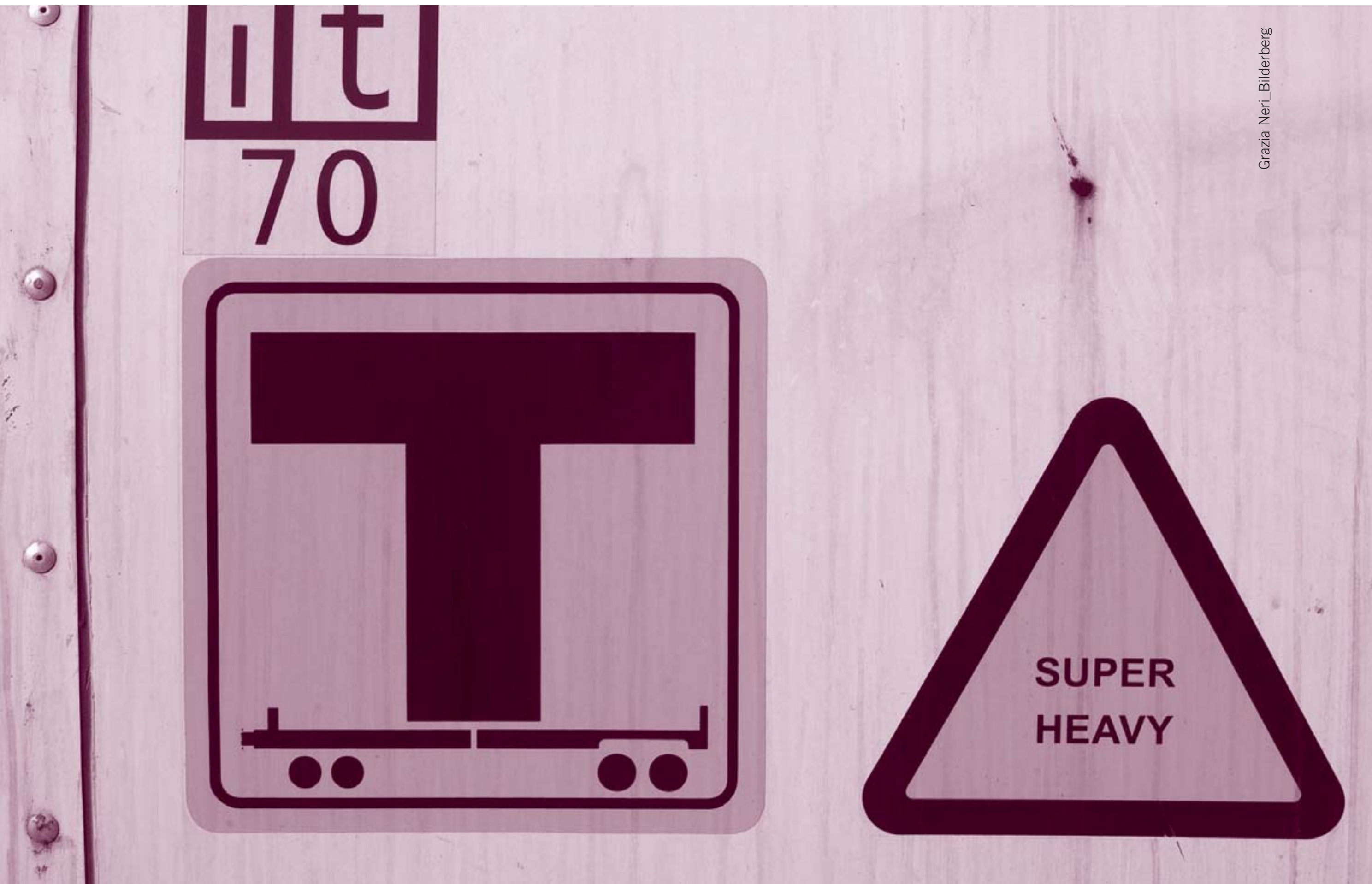


Note: Export share is calculated by comparing the exports of the area (or country) to world demand, where world demand is given by the sum of imports by all the countries in the world. Source: IMF-DOTS, current dollars

The countries of the New Europe are therefore becoming increasingly significant players in the international trade ambit, both in terms of dynamics (high growth) as well as importance (impact on world trade). This is not only true for exports. The countries of the New Europe have in fact also gradually increased their role as destination-markets and their imports now account for over 4.5% of total world imports. These economies, however, only account for 2.5% of world GDP.
Unlike many emerging countries, the countries of the New Europe appeared on the world market at the beginning of the 1990s already having a long industrial tradition behind them, developed even before they became market economies. Their integration into the worldwide competitive environment coincided with the growing recourse, by western companies in particular, to the strategy of out-sourcing production, which led to shifting some production

_Exports in the transport sector alone currently account for a quarter of total exports from Central and Eastern European countries. The main European carmakers also manufacture in Eastern Europe

phases abroad.
Also unlike other emerging countries, the countries of the New Europe went through the key process of convergence towards the European Union, which continues to assist trade, the process of attracting foreign investment, and adapting local industrial systems to European production standards. The EU absorbs no less than 63% of exports from the countries of the New Europe, with Germany, Italy and Austria in the forefront. German companies account for a quarter of overall trade with the countries of the New Europe, in terms of imports and well as exports. Italy is the second trade partner for the countries of the area, but is oriented to a greater extent to the Balkans.
It is not only proximity to the European countries that has played an important role. Rather, it is the evolution of sector-wise specialisation that appears to be the most significant transformation. The growing competitiveness of the countries of the New Europe at the international level has resulted in fact from their ability to adapt their industrial structures to the new competitive environment. The modes of production in the countries of the New Europe, traditionally based on more standardised, labour-intensive production, has acquired competitive advantages in some new sectors in the space of a decade, emerging in car industry-related production where some major European manufacturers are active, as well as in electronics and electro-technical production. Exports in the transport (mainly automobile) sector alone currently account for a quarter of total exports from Eastern and Central European EU member countries and, taken as a whole, the countries of the New Europe now form a significant international production hub. The main European carmakers (Volkswagen, Audi, Fiat, Renault and the PSA Group) produce in Eastern Europe, as do many Asian and American manufacturers. The car industry has in its turn sparked the growth of other types of production, particularly as regards components, leading in many cases to the creation of related industries in which companies of various sizes operate.
However the scenario is not uniform for all the countries in the area. In fact, there is a clear dichotomy between the Eastern and



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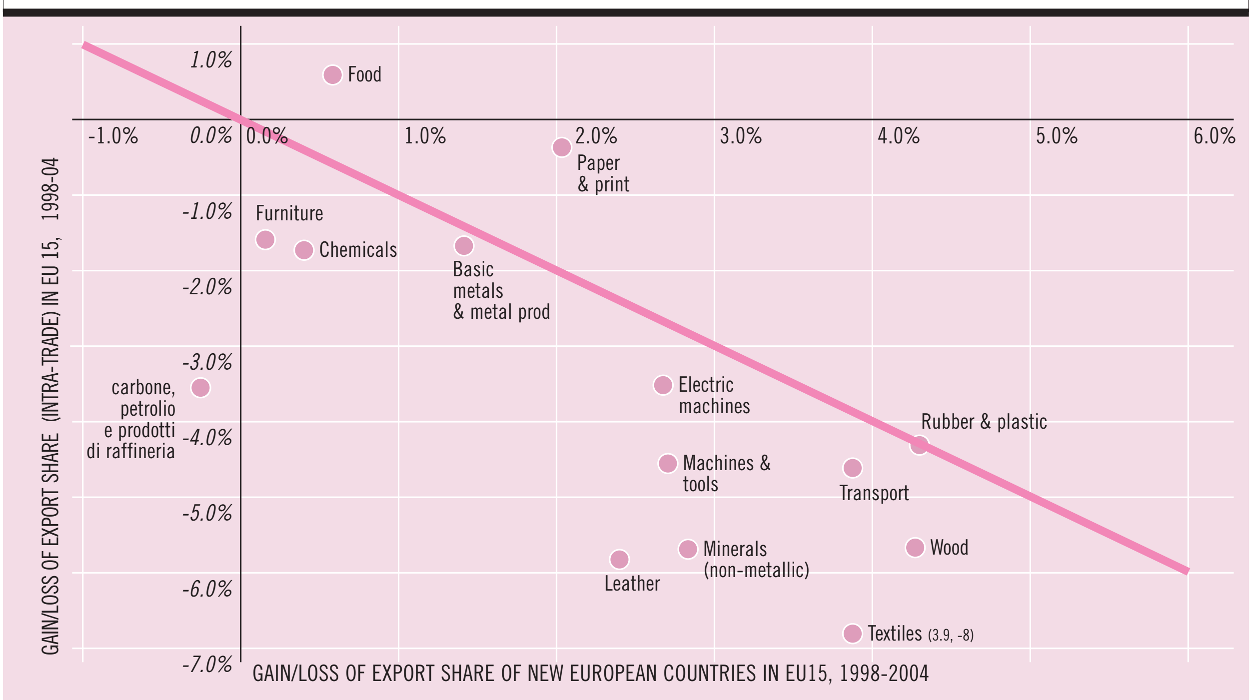
Central European countries on one hand, where the evolution towards sectors with greater added value is more obvious, and the Balkan countries, on the other, in which the industrial structure remains based on traditional sectors. Bulgaria and Rumania in particular have further emphasised their specialisation in the textile industry over the last decade as a result of greater cost advantages.
The competitiveness identified on the export and sector-wise evolution fronts is also strongly linked to the attractiveness of the countries of the New Europe in terms of Foreign Direct Investment (FDI), which has flowed into these countries in tandem with the process of liberalisation and the evolution of a legal context that regulates the presence of foreign companies. Through their production in the East, Western companies have also become one of the most important sources of technological innovation and development. Foreign Direct Investment, which has taken concrete shape in the form of a significant process of eastward production out-sourcing so as to take advantage of lower production costs, is increasingly linked to the search for new markets that are more dynamic than those of Old Europe. This is precisely why FDI is increasingly involving not only a few manufacturing sections, where goods are often produced in the East and then exported, but also services, oriented, for the most part, as a result of their non-tradable nature, to the internal market.
On the whole, as a result of the out-sourcing process and increasing international competitiveness, production in the East is tending to replace that of the Old European countries, at least in specific qualitative segments. An overview of the European market shows that the export share of the countries of the 15-member EU has undergone a generalised fall in all sectors over the last few years, which means that the 15-member Europe is increasingly consuming goods produced outside its own borders. It is however important to note how the fall in the 15-member EU's exports corresponds to a mirror-image gain of the countries of the New Europe (*Figure 2*). Specifically, these sectors are the more traditional segments (textiles, leather goods,

2. GAIN/LOSS OF SHARE IN EU-15 MARKET FOR EU-15 ITSELF AND THE NEW EUROPE (VARIATION % 1998-2004)



Source: Global Insight (current dollars) wood and wooden products) on the one hand and, on the other, car industry-related production (transport, tyres, rubber and plastic products). European manufacturers in the traditional sectors have also felt the impact of Asian competition. The fall in their share is therefore even greater than the gain that we can see for the countries of the New Europe (meaning that these sectors find themselves placed well under the diagonal shown in *Figure 2*) – while, for manufacturers in the second group (cars and components), there seems to be a strong phenomenon of substitution between production in the Old and the New Europe. It is interesting to note that the trade flows and foreign direct investment are not only the result of the new comparative advantages developed independently by the countries of the New Europe, but also reflect the characteristics of the main trade partners and foreign investors. The industrial model of many new European countries has shown a remarkable convergence towards those of their European partners over the last decade. In this sense, therefore, the growth of specialisation in the countries of the New Europe is both the effect and the consequence of links with trade partners and foreign investors. German manufacturers play an important role in the whole area and particularly in the nearby Eastern and Central European countries, where they have developed production linked to the German industrial structure. Car production is predominant in Hungary, the Czech Republic, Slovakia and Poland, together with production of mechanical and electro-technical goods. Austrian companies are mainly present in those countries nearest Austria and with which it shares the strongest historical and cultural links (Croatia, Slovenia and Hungary), in sectors with greater added value, not only through trade but also through long-term production-related investments. The internationalisation of Italian companies, for which Eastern Europe is one of the most significant areas, is marked on the other hand by a less stable presence, and therefore based mainly on export rather than direct investment; Italy's presence is more fragmented (mainly represented by small and medium-size businesses) and oriented to traditional sectors and the South-Eastern European countries. The latter still mainly specialise in labour-intensive production and are the destination of choice for the out-sourcing of some phases of the pre-production process. Because of the specificity of the model of Italian internationalisation – largely due to the composition of Italian industry's production structure – exports and Foreign Direct Investment are concentrated in the more traditional segments, particularly as regards the Balkan countries. It is sufficient to think that over two-thirds of Italy's overall trade with Rumania and nearly 40% of its trade with Bulgaria are in the textile and leather goods sectors alone.

In the light of these considerations, it is clear that the growing integration of individual New European countries into the world economy and the existing difference between the Central European and the Balkan countries are determined by different models of presence in terms of inter-trade and transfer of production to the East by the main European partners. The formation of a few areas of economic influence in the various countries obviously facilitates a further presence of companies in those same countries and in related sectors, as it reduces a significant part of the barriers to internationalisation.