

# Chapter 14

## Causes of Growth of MENA and East European Countries: Comparative Analysis

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### ABSTRACT

*This chapter provides comparative analysis of the proximate causes of growth of MENA and East European countries. The first section covers comparative sources of growth analysis for GDP. Apart from this conventional sources-of-growth analysis, both the demand and the industry side decomposition of the GDP growth rate is briefly given here too. In the demand side of the sources-of-growth analysis, special attention is devoted to the issue of the level of capital account liberalization and its influence on growth anatomy. Connected with this is the issue of industry / sectors side sources-of-growth analysis. The second section covers comparative source-of-growth analysis for GDP per capita as an approximation of growth of standard of living. The results of the above mentioned different sources-of-growth approaches present a good basis for further research of fundamental causes of growth of these countries.*

### INTRODUCTION

The purpose of this chapter is to provide a comparative analysis of the causes of growth of the MENA (Middle East and North Africa) and East European countries. The MENA countries are here further divided in two groups: oil-exporting countries and oil-non-exporting countries. Apart from these countries, for obvious reasons, an analysis of Turkey and Israel is also included here. Similarly, East European countries are here divided into those that belong to immediate

European periphery, which are further grouped into Central European countries (CE) and South East European (SEE) countries, and those that used to be a part of former Soviet Union (FSU) or were in the orbit of their economy (like Mongolia, for example). Indeed, Mongolia and some former Soviet Union member countries (such as Kyrgyzstan, Kazakhstan, Turkmenistan, Uzbekistan, Azerbaijan, and Tajikistan) are not part of Europe at all, but it is obvious that, due to common history and geographic proximity, their addition to the analysis is natural and insightful. The FSU

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countries are further divided in two groups: those that are exporters of energy and those that are energy importers.

The common practice within the modern theories of growth is to make a distinction between “proximate” and “fundamental” causes of growth (Acemoglu, 2008; Acemoglu et al., 2005). The Proximate causes, usually included in the sources-of-growth analysis, are based on and developed according to the Solow Growth Model. The end result of this analysis is a decomposition of the GDP (gross domestic product) growth rate into the absolute and relative contribution of the increase in employment, the increase in capital, and the increase in the total factor productivity (TFP). The growth rate of the TFP is further decomposed into the contribution of human capital (skills), advance in applied knowledge (sometimes referred to as embodied technological progress), and the contribution of organizational innovation, structural changes and similar factors.<sup>1</sup> In one or the other form, when short run variations in the level of activity are eliminated, it captures in the long run different kinds of knowledge and this is why the TFP is sometimes referred to as the advance in “broader knowledge”.

On the other hand, the so-called “fundamental” causes of growth refer mainly to institutional factors, but also to cultural, geographical, and other factors, including pure luck. These factors determine the rate of growth by determining the rate of formation as well as an efficient usage of proximate factors enumerated above. While differences in income levels can be attributed to differences in the proximate causes, the answer to the question of why growth rates differ among countries and within the same country at different times can be obtained only after additional insights from the analysis of fundamental factors. So it can be said that, as noticed by Abramovitz (1993), relationships among proximate causes of growth are not additive, but very complex indeed.

First, there are obvious direct inter-relationships among proximate causes of growth, like the one that exists between the accumulation of physical and human capital. And second, there are numerous complex indirect relationships that operate via fundamental causes of growth.

Finally, the state and development of fundamental factors are ultimately and primarily determined by what is known as the political economy of respected countries. The political economy here does not only refer to referred not only to power structures and power struggles within the respected country, but also to the international or, better, global power structure as well. In fact, it is not possible to understand the “domestic” political economy without connecting it to the political economy of international relations. This is especially important for small countries. And, as we know, both groups of countries that will be analysed here belong to this group of countries.

This chapter is primarily focused on the analysis of proximate causes of growth in the MENA and East European countries. In the absence of certain long-term data series, mainly related to “capital” as a measure of “number of machine”, and to some changes in national accounting systems that took place in different periods, these countries do not have a very comprehensive or comparable sources-of-growth analysis. Now, however, after more than two decades, there are some decent time span data and it seems appropriate to make such an analysis. Some data is still missing and, for that reason, it was not possible to make a detailed sources-of-growth analysis. For the beginning, this paper estimates only decomposition of the GDP growth rate into the contribution of capital, labour and TFP. This kind of sources-of-growth analysis will, nevertheless, provide some important insight into the anatomy of the economic growth of the MENA countries. Apart from that, results provided in this way will be compared with similar results for those East European countries that belong to

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