Financial and Economic Review, Vol. 18 Issue 1, March 2019, pp. 155–162.

Report on the 2019 Lámfalussy Lectures Conference*

Ferenc Tóth

On 4 February 2019, the Lámfalussy Lectures Conference was organised for the sixth time. At this year's conference, the world's leading financial experts and academic researchers examined the issue of convergence.

In his welcoming speech, *György Matolcsy*, Governor of the Magyar Nemzeti Bank, first greeted *Yves Mersch*, winner of the Lámfalussy Award, Member of the Executive Board of the European Central Bank and former governor of the Central Bank of Luxembourg, as well as *Katalin Novák,* winner of the Popovics Award, Minister of State for Family and Youth Affairs at the Ministry of Human Capacities. In his lecture he outlined that the first stage of the euro convergence process lasting until 2008 had been successful. However, in the following period – lasting from the financial crisis to 2012 – convergence stalled and the structural problems of the euro came to the fore. Although the global financial crisis emerged in the United States, the crisis in the euro zone was deeper, longer-lasting and more painful than in the USA. In the third stage of the euro lasting from 2012 to date we see a slow recovery. *György Matolcsy* emphasised that it would be worthwhile to learn the following lessons from all this: 1) Longer and more dynamic boom periods are needed to achieve sustained convergence. 2) We need a fully-fledged euro and eurozone to prevent a possible future financial crisis. 3) We need appropriate crisis management mechanisms, quick and pragmatic crisis management based on experiences in the USA, as well as close cooperation between the government and the central bank. In respect of Hungary, he explained that although we are outside the eurozone, we are inside the European Union, and as Europeans we are entitled to have a vision on the future of the eurozone, since Hungary will join the eurozone in the decades to come. Finally, he outlined again that another financial crisis might happen in the future, when we will need quick and efficient crisis management. This will require efficient cooperation between governments and central banks so as to avoid budgetary restraints that may have severe impacts on society and long-term economic growth.

* The papers in this issue contain the views of the authors which are not necessarily the same as the official views of the Magyar Nemzeti Bank.

Ferenc Tóth is an Advisor to the Executive Director at the Magyar Nemzeti Bank. E-mail: tothf@mnb.hu

Ewald Nowotny, Governor of the Oesterreichische Nationalbank praised *Yves Mersch* in his speech*,* and in a historical context he provided a detailed presentation of his work and extensive experience, as well as his commitment to European and also to national affairs. *Nowotny* presented *Mersch* as a highly competent expert who is one the most deserving persons selected for the award, and whose thinking complies with the spirit represented by *Alexandre Lamfalussy*. *Mersch* is also a truly European thinker and an excellent role model. Reflecting on the conclusion of *György Matolcsy* that there were ups and downs in the last two decades, he said that without the ECB it would have been much more difficult for small countries in the European Monetary Union to tackle the crisis.

In his speech, *Yves Mersch*, Member of the Executive Board of the European Central Bank and former governor of the Banque centrale du Luxembourg, praised *Alexandre Lamfalussy*, whom he saw in different roles in the last 30 years of his life, and he always admired his outstanding precision and professional competence. The main topic of his speech was the changing role of central banks.

The design of the modern central bank dates back to the consensus around the disinflationary path of the 1980s that central banks should be independent and have a narrow mandate restricted to focusing on the fight against inflation. In Europe, there was a second layer of consensus on how to share tasks, and how to allocate what is done at a national and regional level. Although political considerations relating to shared sovereignty also supported the monetary institutional setup, economic and fiscal issues were left to coordination and some common rules. This created a breeding ground for critics. Problems were exacerbated by the failure of economic cooperation, and the European Commission changed too: from a technocratic body it turned into a political one. The biggest test was the great financial crisis which is still shaking the foundations of our societies today. Major changes took place in monetary policy implementation during the crisis in the context of instruments, communication and accountability. In terms of strategic thinking and interaction with various policy fields, the biggest change concerned financial stability and macroprudential policy. In 2010, *Alexandre Lamfalussy* called for central banks to not regard their macroprudential duty as being less important than maintaining price stability. In conclusion, *Mersch* argued that the best solution is to integrate financial stability concerns into monetary policy at the European level, including possible corrections with instruments at national levels.

Morning session: "The decade of convergence in the EU"

The moderator of the discussion forum was *György Szapáry*, Chief Advisor to the Governor of the Magyar Nemzeti Bank, who provided a brief introduction to the subject, saying that the share of Southeast Asian countries in world GDP was four times higher in 2017 than in 1990, and China's share is continuously increasing. Of the 28 Member States of the European Union, the eight Central and Eastern

European countries are experiencing slow but continuous convergence. Europe's share in world GDP is declining more rapidly than the share of the USA. Eleven of the world's top 20 high tech companies are American, nine are Chinese, and there are none from Europe. Innovation and technological development will be key competition factors in the future (in particular regarding artificial intelligence and robotics). Europe must improve its education system. The PISA surveys clearly reveal the outstanding performance of Asian countries.

Lúcio Vinhas de Souza, Head of the Economics Team at the European Political Strategy Centre (EPSC) of the European Commission, talked about reviving convergence. Although the EU remains a "convergence machine", and one can see increasing standards of living in Member States, we need to do more. Central European countries have achieved real convergence, but they are facing new challenges that they must meet to continue this process. Central European Member States are also performing relatively well in macroeconomic terms. Although non-euro-zone members could easily meet most of the accession criteria, he thinks that Central European Member States will remain among the least competitive economies of the EU. The quality of governance remains below the EU and eurozone average, and in fact is becoming a little poorer. Adequate institutional capacity is crucial. A favourable investment environment requires quick and efficient administrative procedures, reliable and accessible data, legal certainty and planning capacity. The efficient functioning of domestic markets is also dependent on factors like the rule of law, quality and efficiency of institutions. If these are not adequate, it may lead to an outflow of capital or a lack of domestic and foreign investments. For some Member States, labour costs exceed productivity growth, which results in a decline in relative competitiveness, and investments largely depend on the EU Cohesion Fund. From the perspective of sustainable convergence, financial stability is crucially important. This has particular significance for euroised financial systems in Central Europe. On the whole we may conclude that there is economic convergence in the region, but there is a need for adjustments in a number of areas. The EU will always be a partner for dialogue in this field.

William R. White, former chairman of the Economic and Development Review Committee at the Organisation for Economic Co-operation and Development (OECD) and former economic advisor to the BIS, lectured on the decade of catching up within the EU. As regards convergence in the pre-crisis period, he said it was difficult to measure convergence. Not only per capita GDP is important, but well-being, too. Convergence slowed down after the crisis, as did the process of legal and institutional reforms. It is important to maintain the achieved results. Strong institutions and confidence facilitate cooperation, avoiding disturbances. There needs to be more focus on crisis prevention management and resolution. Preventive measures must be taken to handle domestic problems. He highlighted the excessive increase in private sector debt. Macroprudential policies are important, but there is no magic bullet. At the same time, the points of particular importance include long-term reforms in the budgetary framework, the support of domestic (local currency) capital markets and the continuation of the intensive legal and institutional reforms. Central and South Eastern European countries will not be able to avoid many external problems either (trade war, Brexit, weakening global economic growth) if they occur. In any case, it is worth preparing ourselves for tougher times, putting measures on improving crisis-management mechanisms in the forefront, and generally focusing on creating confidence and systemic resilience to remain capable of attracting investors and continuing with convergence.

*Christian Kopf***,** Managing Director at Union Investment Privatfonds GmbH, emphasised the importance of the European integration process and institutional system. Recalling the four freedoms embedded in the Treaty of Rome, he commented on their impacts on the economic convergence of Central Europe. On the free movement of people he remarked that in some cases this might have a negative consequence: young, highly qualified people leaving Central European countries. In terms of the labour shortage, Hungary has two options: a low growth path or inflows of foreign labour. He believes that the reason why Hungary was hit more severely by the crisis than the Czech Republic or Poland is partly because the yields of Hungarian government securities were higher. Another important factor was that due to the free movement of capital, Member States could not introduce limitations on capital flows during the financial crisis. The free movement of goods and services was one very positive element in the economic integration, particularly in terms of participating in supply chains.

Povilas Lastauskas, Director of Centre for Excellence in Finance and Economic Research at the Bank of Lithuania gave his personal opinion – 25 years after Maastricht – on the heterogeneity and convergence in the European Union. According to his calculations, 26 countries are approaching, albeit slowly, the same equilibrium level of real GDP per capita, and there is almost overall convergence in the EU. There are wide and persistent differences in terms of real labour productivity. Although there is some convergence at the macro level, there are more significant differences at the regional level where there is a lower degree of convergence. He finished his presentation by asking about the regional dimension, even if there is convergence at the macro level. Is it sufficient to track aggregate convergence?

Afternoon session: "The decade of convergence in Asia"

The afternoon session started with the keynote speech of *Kairat Kelimbetov*, Governor of the Astana International Finance Centre (AIFC), former governor of the National Bank of Kazakhstan on the subject of the cooperation between Europe and Asia. First he drew attention to the shift of power in the global economy, where the economic and political centre has shifted and is expected to further shift from the Euro-Atlantic power centre to Asia. During recent decades the economies of Asia have undergone enormous change. According to some forecasts, China will become the world's largest economy by 2050, with India in second place, and the USA will only be third. The Asian market comprises 62 per cent of the world's population. In addition, substantial industrialisation and urbanisation processes have taken place in China and India. China is also a leader in terms of the future, being a global force in the digitalisation of the world economy (e.g. in e-commerce and FinTech). A number of Chinese companies have developed to such an extent that they are competing with Silicon Valley companies. In Davos, special attention was paid to the topic of U.S.-China competition, in particular in the field of artificial intelligence. The reason for the success of Asian countries lies partly in their approach to innovation, in their demographic trends, and partly in the prudent regulatory environment and institutions. We need to focus on how to facilitate the financial connection between the European and Asian markets. Central European and Central Asian economies may play a key role in creating this connection.

The moderator of the afternoon discussion forum, *Dániel Palotai*, Executive Director and Chief Economist of the Magyar Nemzeti Bank, highlighted in his introduction to the debate that the global world order has changed. The evolution of new economic centres and the rebirth of the ancient trading routes have created a multipolar world order, in which Asian countries are becoming more and more important. Furthermore he confirmed that Hungary acts as a bridge-builder between the East and West. For the future, he emphasized that by 2030 three of the four largest global economic powers might be in Asia. Turning to competitiveness, he said that there is a considerable competitiveness gap across regions. In 2018, based on World Economic Forum survey and the IMD World Competitiveness Center's research three or two of the ten most competitive economies in the world have been Asian economies, respectively, while the others are European and North American. Policies aimed at boosting competitiveness have served for them as a basis for convergence. This is a major lesson for Hungary too.

Denis Hew, Director of the Asia-Pacific Economic Cooperation (APEC) Policy Support Unit, examined the catching-up decade of the Asian-Pacific region from the perspective of the APEC. The APEC is an informal, non-binding, consensus-driven forum with 21 member countries. It works towards achieving free trade and making investments in the region. The APEC region's GDP growth has consistently exceeded the world average since the crisis, and the APEC members' share of world GDP and trade is continuously growing. However, a study demonstrated that due to geopolitical tensions, trade is no longer considered a reliable driving force of APEC's economic growth. The opportunities of the digital economy – particularly e-ecommerce – the development of green technology, an increase in green-field investments as well as implementing reforms that improve productivity in education, health care and other social services, encouraging innovation, narrowing gaps in infrastructure and promoting women's participation in economic activities will likely be the engines of growth in the future. Current issues affecting future growth are as follows: demographic problems (aging population, distribution of resources to prepare for solving key economic issues like the lower labour supply and higher healthcare costs), issues relating to digitalisation and employment (medium-qualified jobs can be replaced with computers), and workplace polarisation (as most mid-skill routine jobs are being computerised, only non-routine and discretionary jobs are left at the low and high end of the skills spectrum). Furthermore, natural catastrophes and diseases may negatively affect future growth, since the need to provide temporary shelters and transitional livelihoods entails a significant budgetary cost. In his closing remarks, he said that APEC was developing a new vision for the future for the post-2020 period. It already takes into account the new trends and challenges: growing trade protectionism and tensions, tackling non-customs barriers and structural reforms, geopolitical risks, structural unemployment due to digital technologies and artificial intelligence, inadequate skills, issues relating to the middle income trap such as moving up the technological ladder, the environmental effects of fast industrialisation and urbanisation, anti-globalisation opinions and increasing inequality.

Khee Giap Tan, Co-Director of the Asia Competitiveness Institute of the National University of Singapore, Associate Professor at the Lee Kuan Yew School of Public Policy, and Chairman of the Singapore National Committee for Pacific Economic Cooperation (SINCPEC) talked about the East Asian economic development model, some elements of the One Belt, One Road Initiative, and the consequences of the US-China trade war. First, he provided a quick and updated overview of global economic development trends in respect of the US-China trade war, indicating that growth in the Asian-Pacific region is still expected to be higher than in developed economies, while the slump in the growth rate will remain marginal and decrease less than in developed economies. The second part presented the East Asian economic development model (EAED) for resolving bottlenecks. The experience and success of the robust EAED model show that overcoming the production bottlenecks through investments aimed at resolving production bottlenecks is a pre-condition for an economic recovery, and a useful tool for escaping the middle income trap. Effective leadership and good governance clearly have a prominent role in facilitating infrastructure investments. The third part was about the facilitation of regional and bilateral free trade agreements and the fact that OECD economies are still very important for the ASEAN states. In the fourth part, the lecturer addressed the importance of the ASEAN area in respect of the fragmentation of production in global value chains, and the transfer of production from China to ASEAN economies. Then he talked about the opportunities offered by China's One Belt, One Road Initiative for Hungary and Eastern Europe. As he said, Hungary can explore the opportunities provided by the One Belt, One Road Initiative if the government does not leave it to the market but takes over the duties of this project. Finally, he presented Singapore as the infrastructure centre of Asia, focusing on the cross-border cooperation in infrastructure development, investments and finance.

In his lecture *Hyeonjung Choi*, Director of the Centre for Global Governance at the Asan Institute for Policy Studies and a research fellow at the Asan Institute for Policy Studies pointed out what we can learn from the East Asian catch-up economies. Since the end of the 1980s these economies have continuously achieved higher growth rates than the world average, and to an increasing extent. He presented the features of the East Asian catch-up countries: the dominance of state bureaucracy and economic policy, the control of the domestic market, the "revolving door policy" of business and industry associations, the focus on selected key industries, the central role of finance, and the export-led strategy. He then went on to list the favourable external conditions for convergence: the Cold War era provided a kind of security umbrella, financial and technological support when a wide range of new market opportunities opened up for the allies. The existence of the American and liberal economies, the robust economic growth of the great powers in the 1960s to 80s, the target countries of the export-oriented economy, the accepted political intervention of authoritarian regimes in the economy, the onset of the era following the Cold War, and the twin deficits of major importers – all this stimulated growth.

His lecture continued with the challenges that catch-up economies face in the 21st century. The world market has become more mature, competitive and liberalised. In addition, free-trade rules and free market economies have also changed. The industry is undergoing a paradigm shift too. New enterprises with increasing profits are emerging, while the manufacturing industry is less profitable. "Sustainable development" has become the creed, including economic growth, environmental protection and social justice. He closed his presentation by drawing conclusions from predecessors' development: first he highlighted the important role of the government: it is necessary to create a future-oriented growth vision, well-defined national competitiveness, and well-structured, long-term objectives and industrial policies. Secondly, there has to be consensus on national economic development: it is necessary to have a well-supported political system and leadership, as well as a fair distribution of the national wealth. Thirdly, it is necessary to support the enterprises that generate increasing profits, as well emerging sectors. Fourthly, the liberal international order and markets must be utilised. Finally, environmental degradation must be avoided, and sustainability must be a priority.

Andrew Sheng, Distinguished Fellow of the Asia Global Institute at the University of Hong Kong and former Chairman of the Hong Kong Securities and Futures Commission viewed Asia from the perspective of a global system. At the beginning of his speech he paid tribute to *Alexandre Lamfalussy*. He considers Hungarian economists to be the best economists in the world, and as he sees it, the best ones work at the central bank. He believes that megatrends signal a paradigm shift, a move away from the neoliberal order, but the transition will be very chaotic. From a macroeconomic aspect, geopolitical risks will exceed financial risks. He mentioned six disrupting megatrend factors: the shift from a unipolar towards a multipolar world; the geographical shift from West to East; the shift in gender roles (women are getting richer and earning more and more); the shift of generations (the young facing a future without jobs); climate change (shortage of water, food and energy); and the technological shift which entails jobs and creative disruption. Even one single factor is extremely complicated. Moreover, each factor interacts with the others, and thus may result in very complex outcomes. This poses enormous challenges for politics, as well as for business models, since the policy of "America first" does not create a level playing field. The next topic touched upon the emerging opportunities and threats, and the issue that the strengthening of the US dollar, the trade war, and the whole neoliberal thinking endangers sustainable prosperity. If the US dollar strengthens, emerging economies suffer from enormous liquidity pressures. The trade war constitutes a setback – not only for trade itself. Another big question is who will implement the 5G technology. Finally, referring to the Hungarian economist, Karl Polanyi, he said that it had become clear that market self-regulation did not work and this might erode human society and destroy nature.

In his closing words*, György Matolcsy* thanked participants for their very high quality and exciting presentations and inspiring thoughts, and expressed his hopes that the collective thinking on the new paradigms that determine future development would continue within the framework of the Lámfalussy Lectures Conference.