

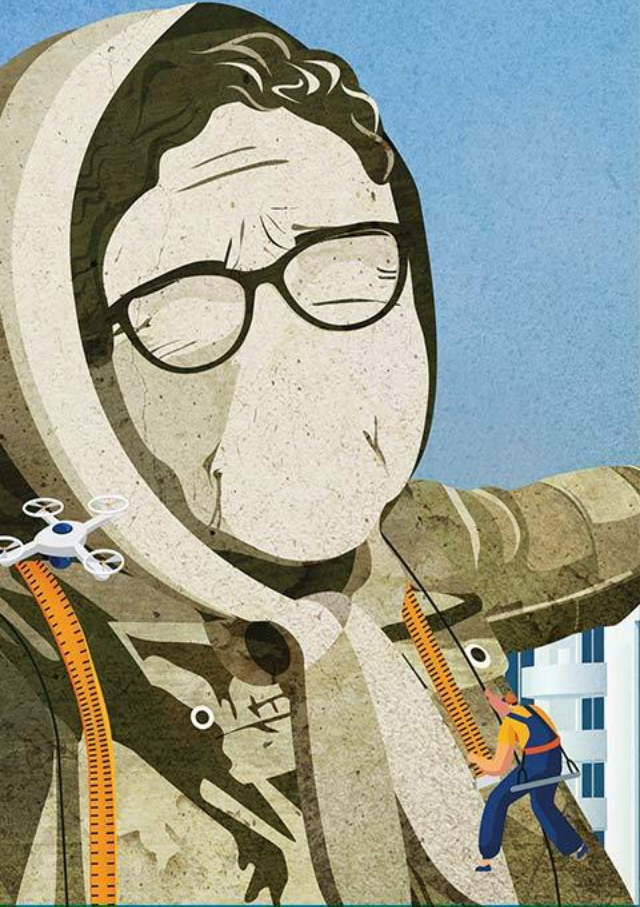
TRANSITION REPORT 2020-21



THE STATE STRIKES BACK



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[#ebrdt](#)
Interactive charts | online downloads | country assessments
1



1

HOW BIG IS THE STATE?



2

STATE-OWNED ENTERPRISES



3

STATE BANKS ON THE RISE

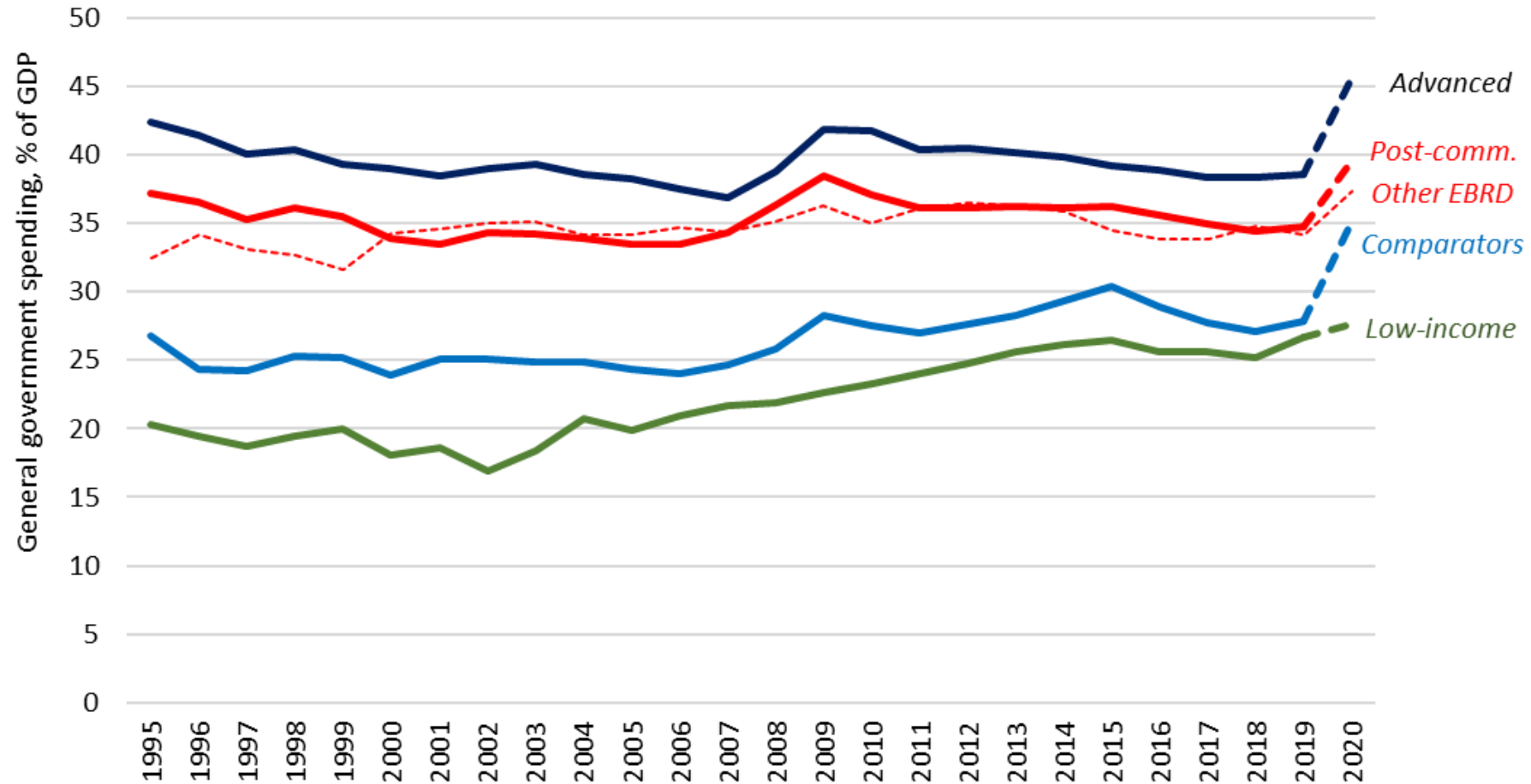


4

THE STATE AND THE GREEN ECONOMY

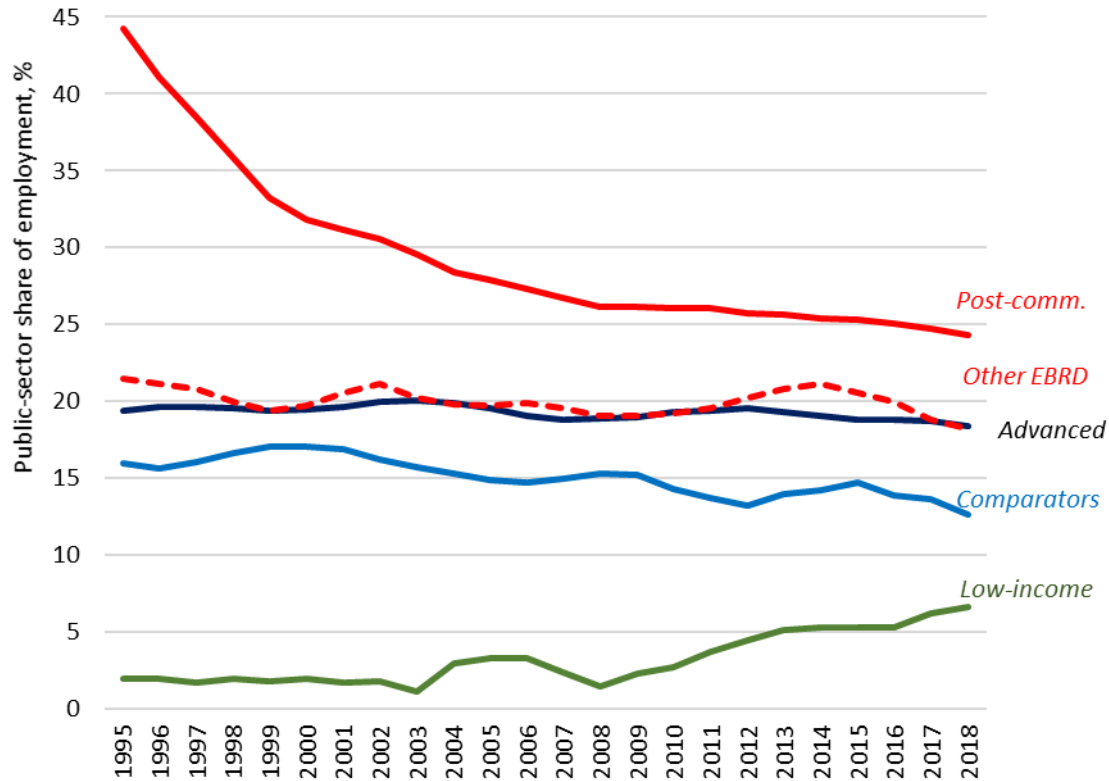
Government spending in the EBRD regions (at around 35% of GDP) is in line with their characteristics, including aging populations

Government spending as a share of GDP has been increasing in emerging-market and low-income economies

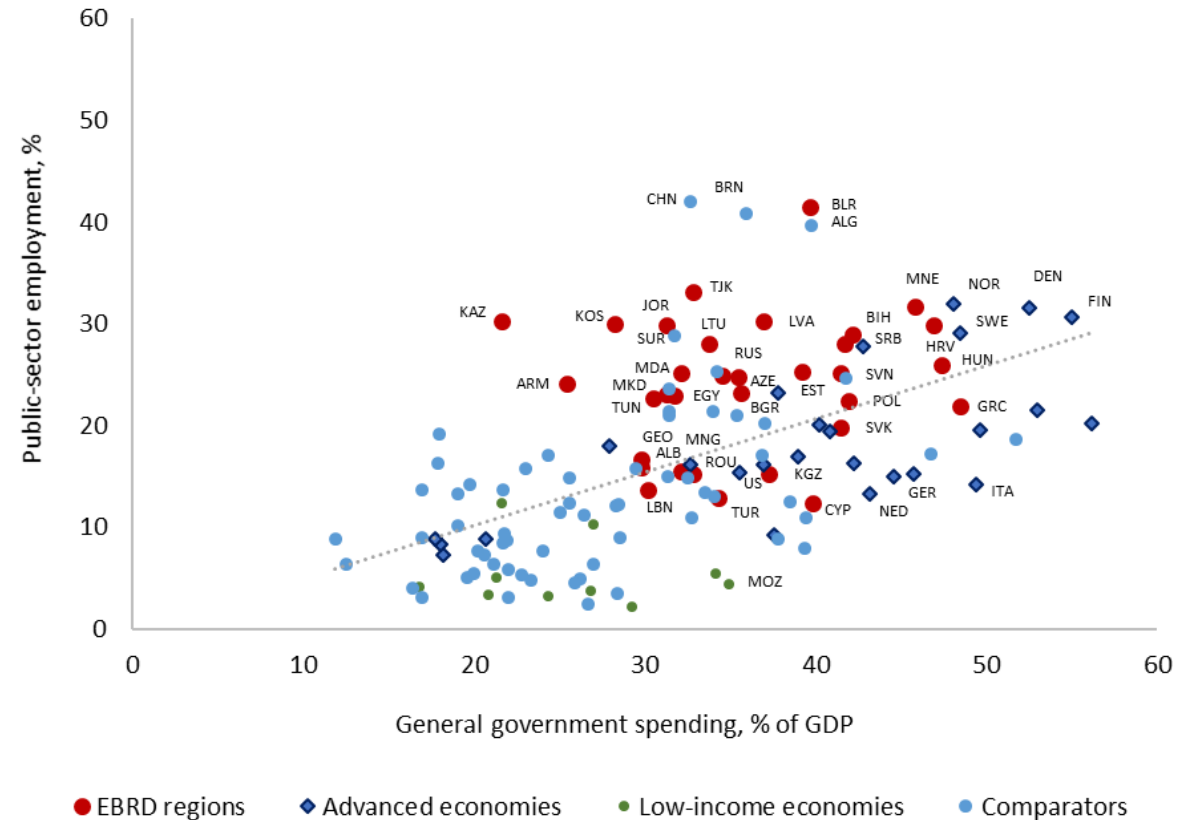


Declining state employment in post-communist economies: 45% in mid-1990s to 24% in mid-2010s, yet it remains 7pp higher than in comparator countries

Declining state employment in post-communist economies

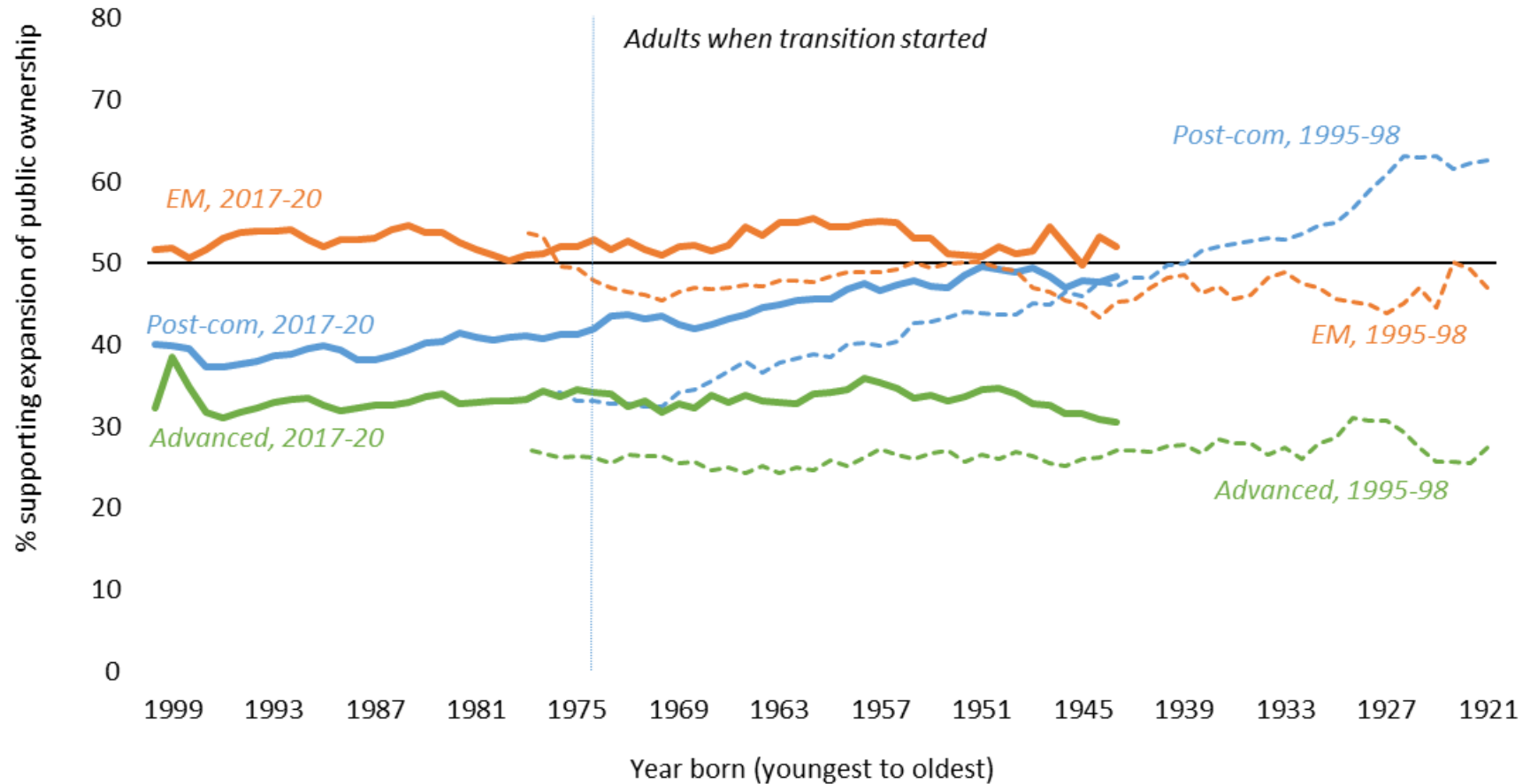


State employment in post-communist countries remain 7pp higher than in similar economies



As public share of employment has been declining, support for public ownership has been growing, reaching 45% in post-communist economies

In other emerging markets, support surged to 53%

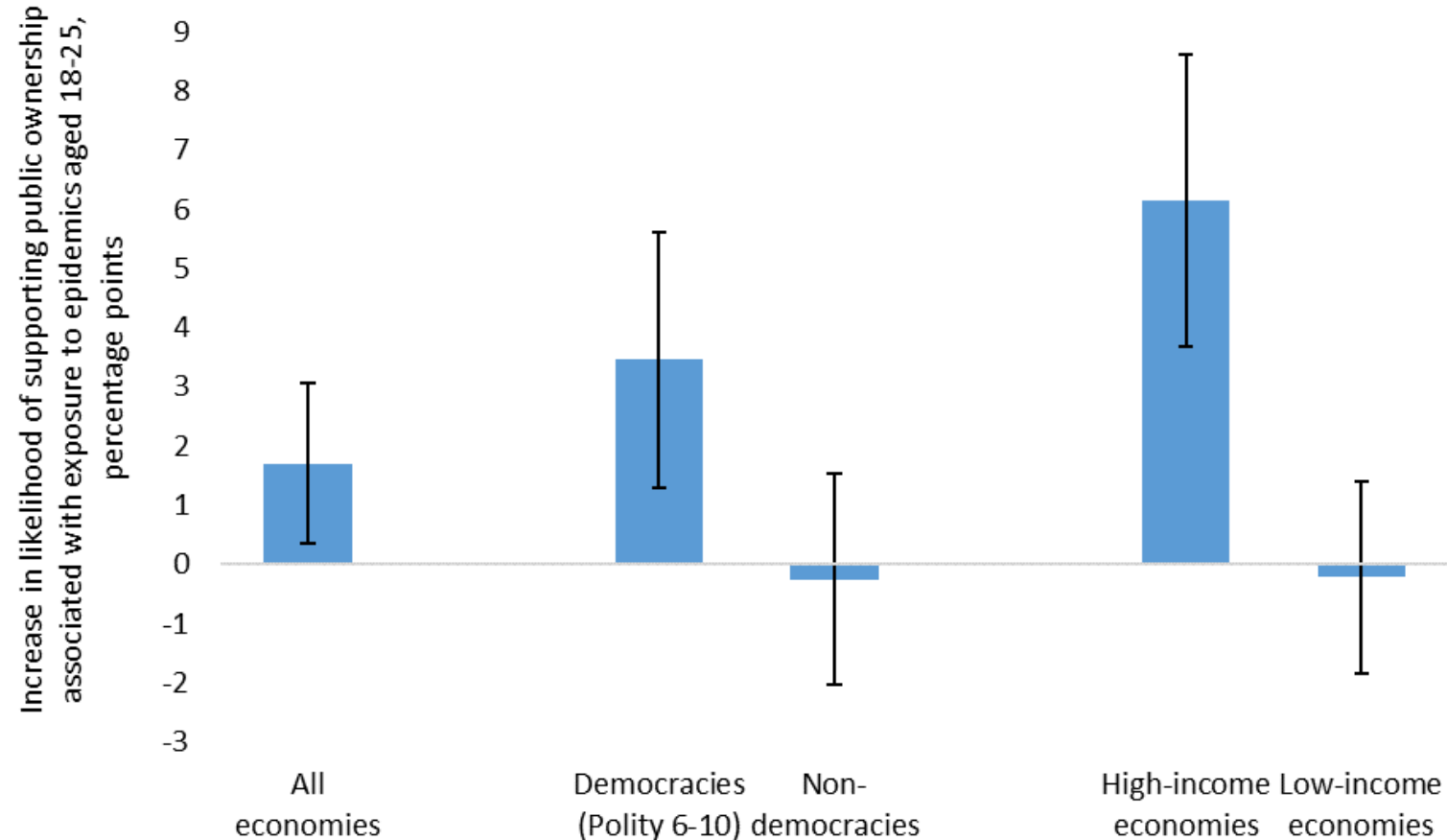


Past experiences suggest support for public ownership may rise due to Covid-19

Stronger support for expansion of public ownership among individuals exposed to epidemics in their formative years (18-25)

Previous epidemics dented trust in the economic institutions and democracy (Aksoy et al. 2020)

Those who reach adulthood during major recessions have a more positive view of public ownership and redistribution (Giuliano and Spilimbergo 2014)



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STATE-OWNED ENTERPRISES



State-owned enterprises (SOEs) have historically played an important role in the EBRD regions

SOEs account for almost **half of public sector employment**

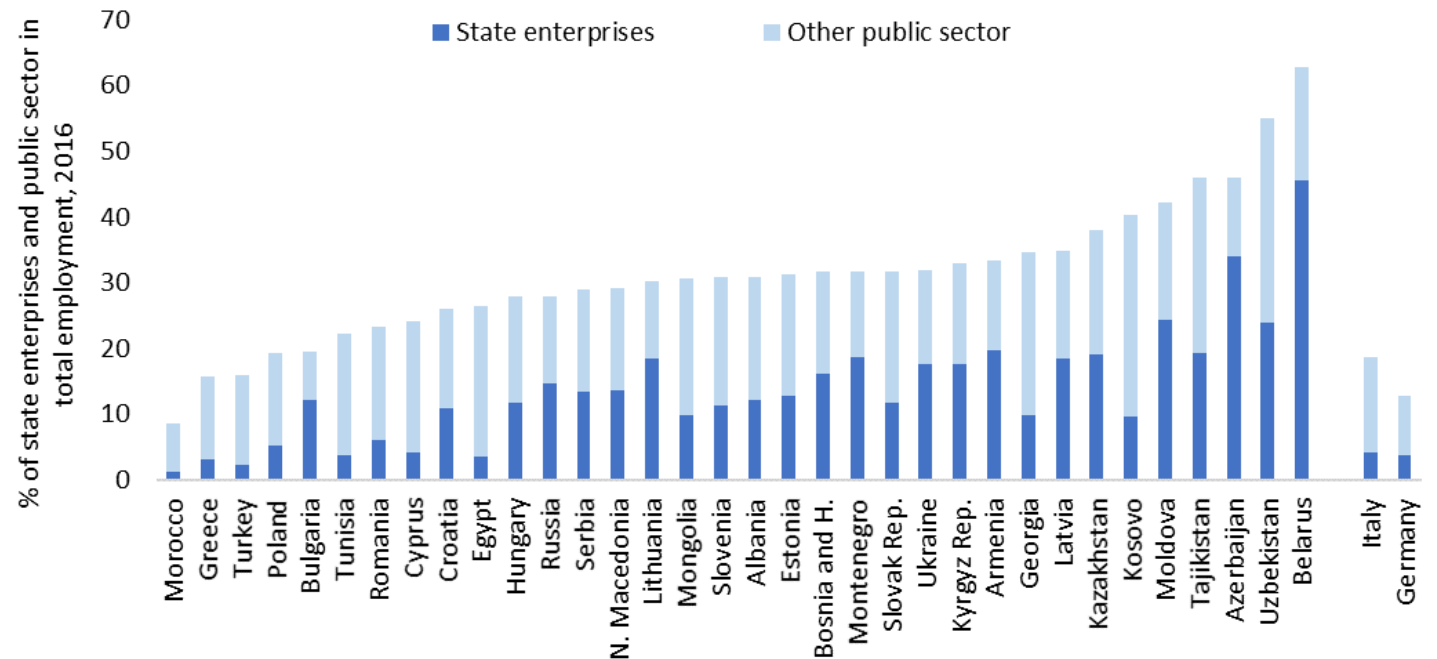
SOEs are concentrated in **utilities, transportation and energy**

SOEs often receive subsidies to provide **affordable service** in remote areas and for low-income households

SOEs act as **automatic stabilisers** providing more stable employer in lagging regions and during downturns

But governments often struggle to run SOEs efficiently

Employment at state-owned enterprises accounts for almost half of public-sector employment



SOE provision of services is common where administrative capacity constrains private-sector options

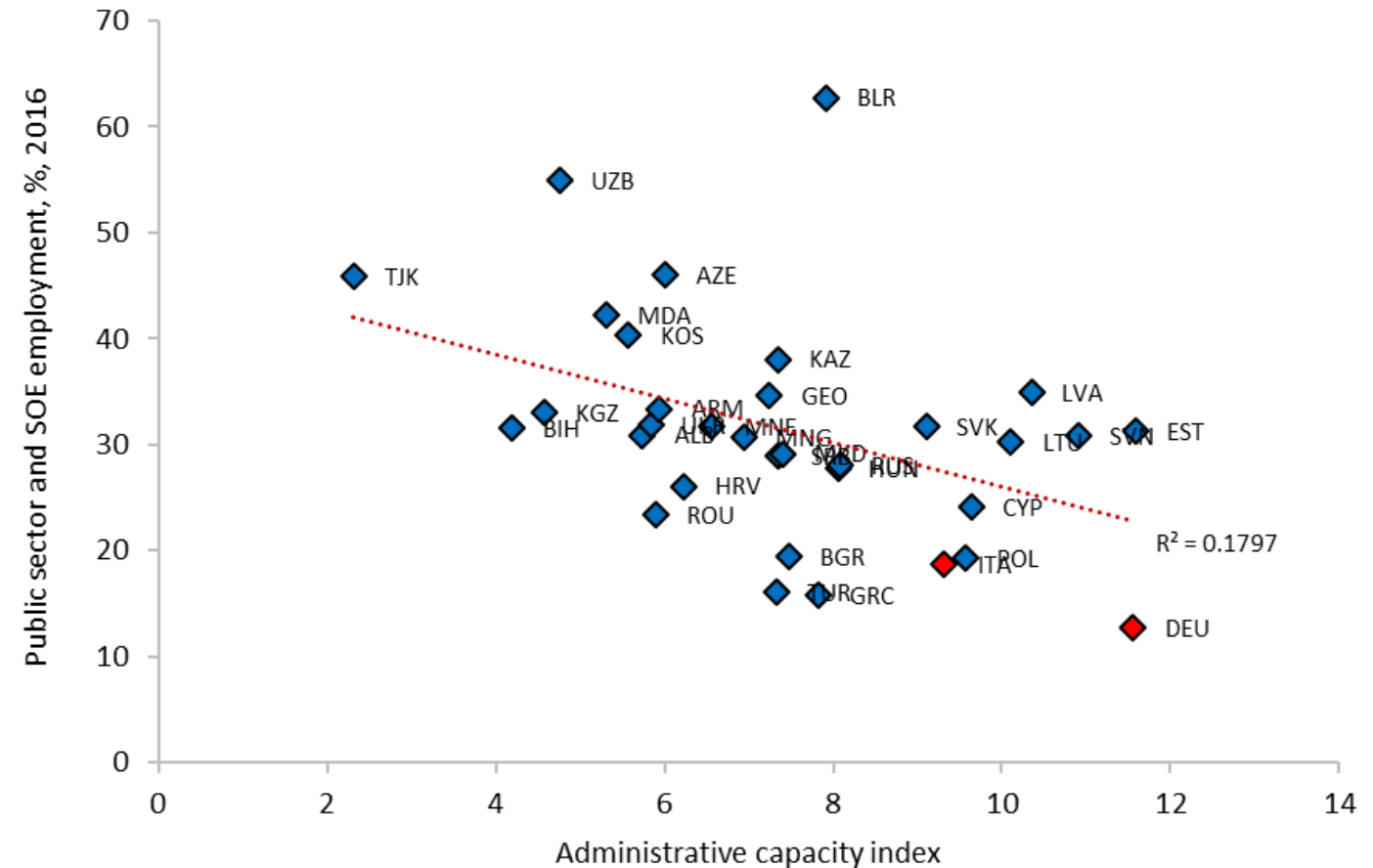
State enterprises step in where administrative capacity is more limited

Services can be provided by private companies, with government **subsidies** and **public service obligations** ensuring universal coverage

Poor households facing large utility bills can receive means-tested benefits

Fiscal transfers and targeted investment can attenuate regional disparities

Private-sector solution require capacity to set up and monitor such schemes, and to administer targeted means-tested benefits



Poor governance of state-owned enterprises in the EBRD regions

Need to **separate functions**:

- In almost half of countries SOE ownership and regulatory powers are combined
- **in 19% of countries SOEs have regulatory powers**

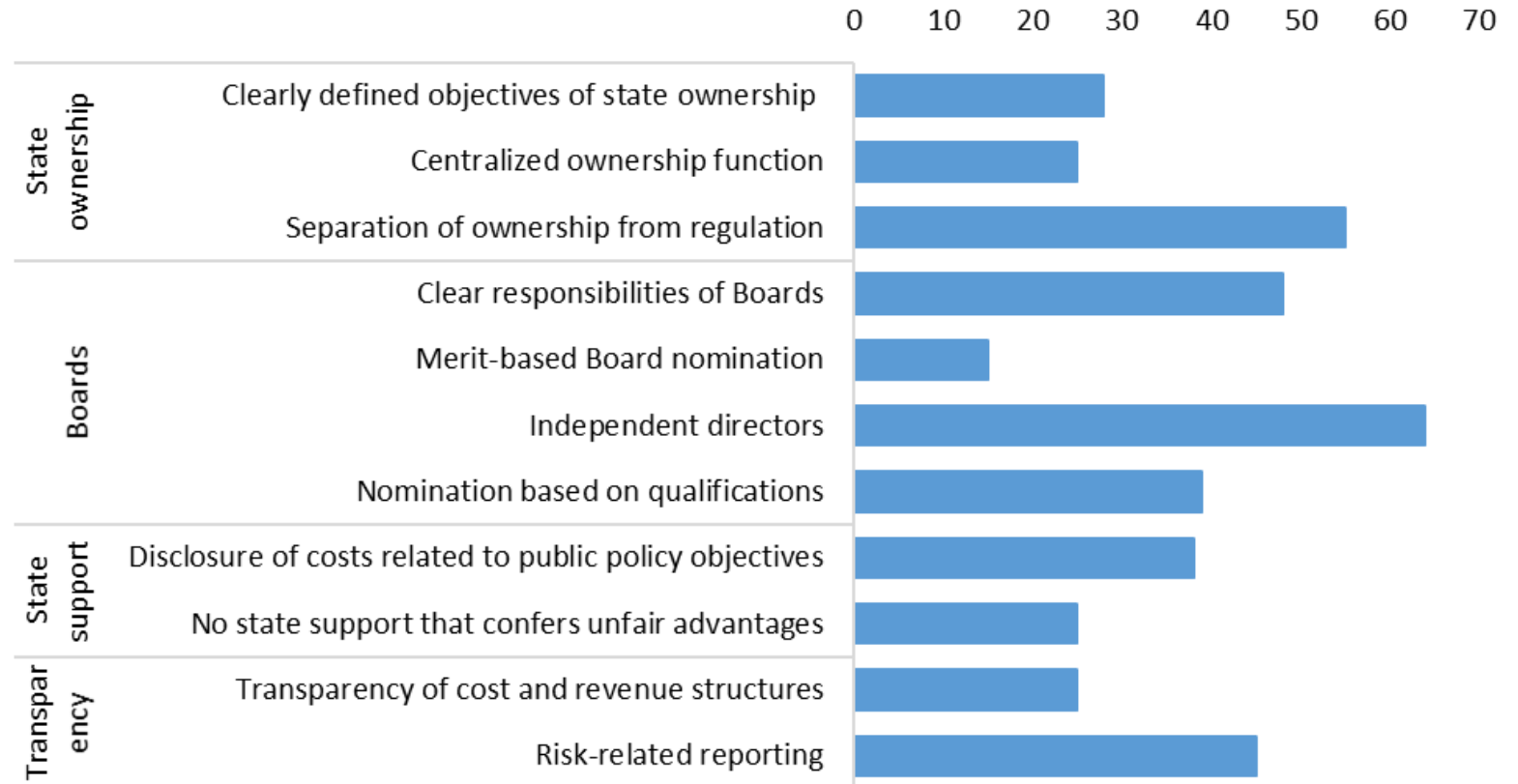
SOE management should be about **strategy, efficiency, not only compliance**:

- many SOE Boards do not have adequate powers to approve even company budgets

Disclose public service obligations and their costs. Non-disclosure leads to **vicious cycles of non-transparent subsidies, losses, bailouts, inefficiencies and more losses**

No subsidised inputs or preferential taxes, to **ensure level playing field**

% of EBRD economies that comply with OECD guidelines on corporate governance of SOEs



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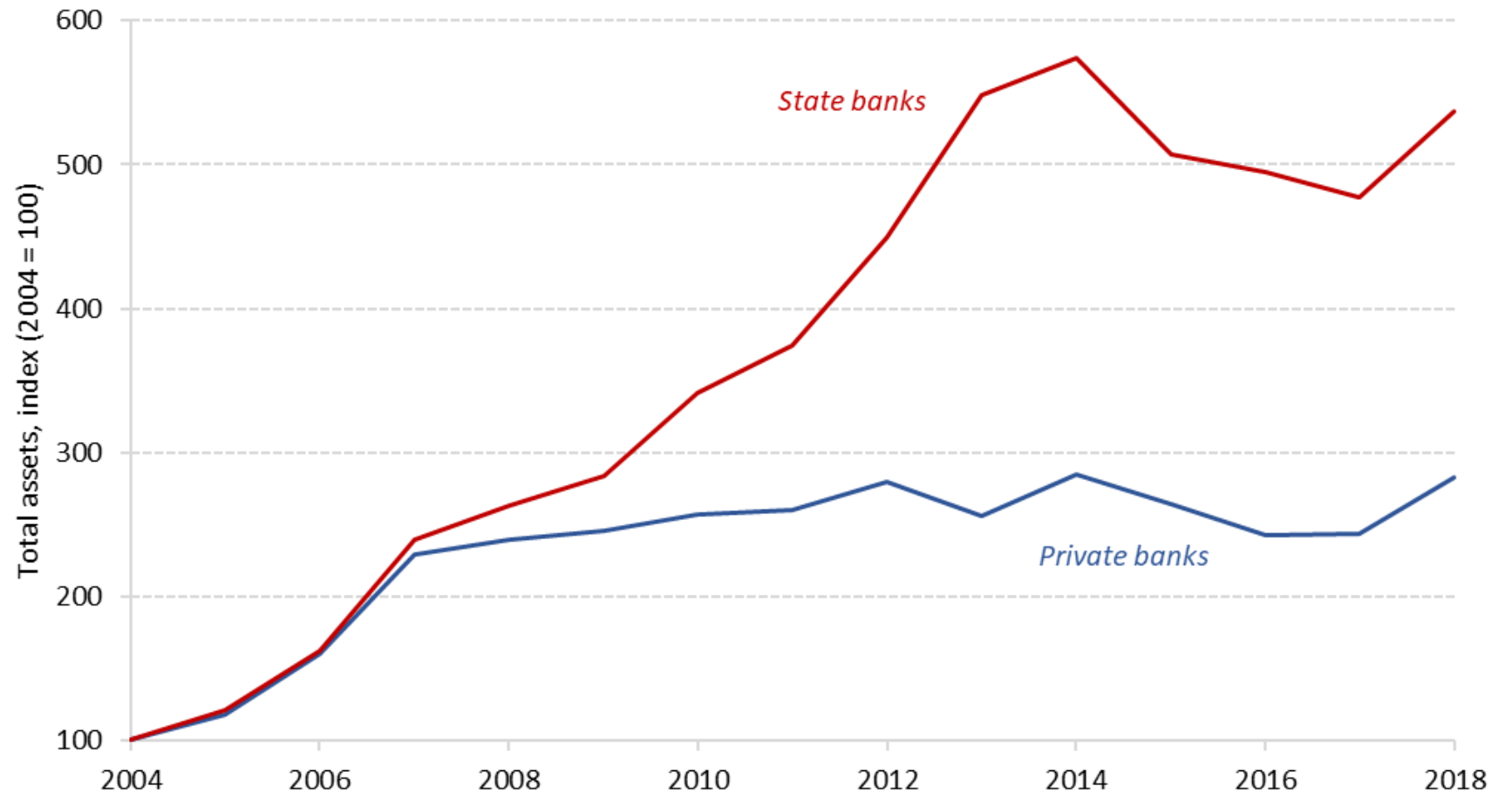
STATE BANKS ON THE RISE



State banks in the EBRD regions have been growing assets almost twice as fast as private banks since mid-2000s

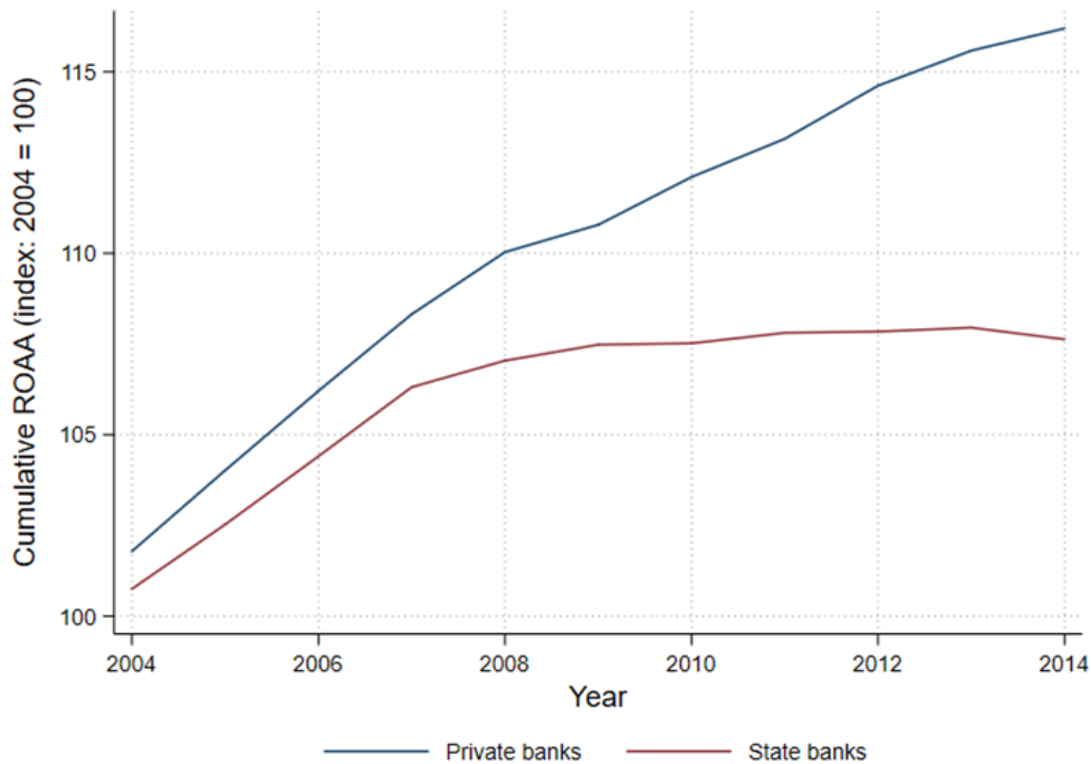
Expansion of assets of state banks vs private banks in the EBRD regions

State banks own 50%+ of banking assets in Belarus, Russia and Ukraine as well as in China and India



State banks tend to have less strict lending requirements and accept a lower return on assets and a higher level of non-performing loans

State banks in the EBRD regions have lower return on assets...

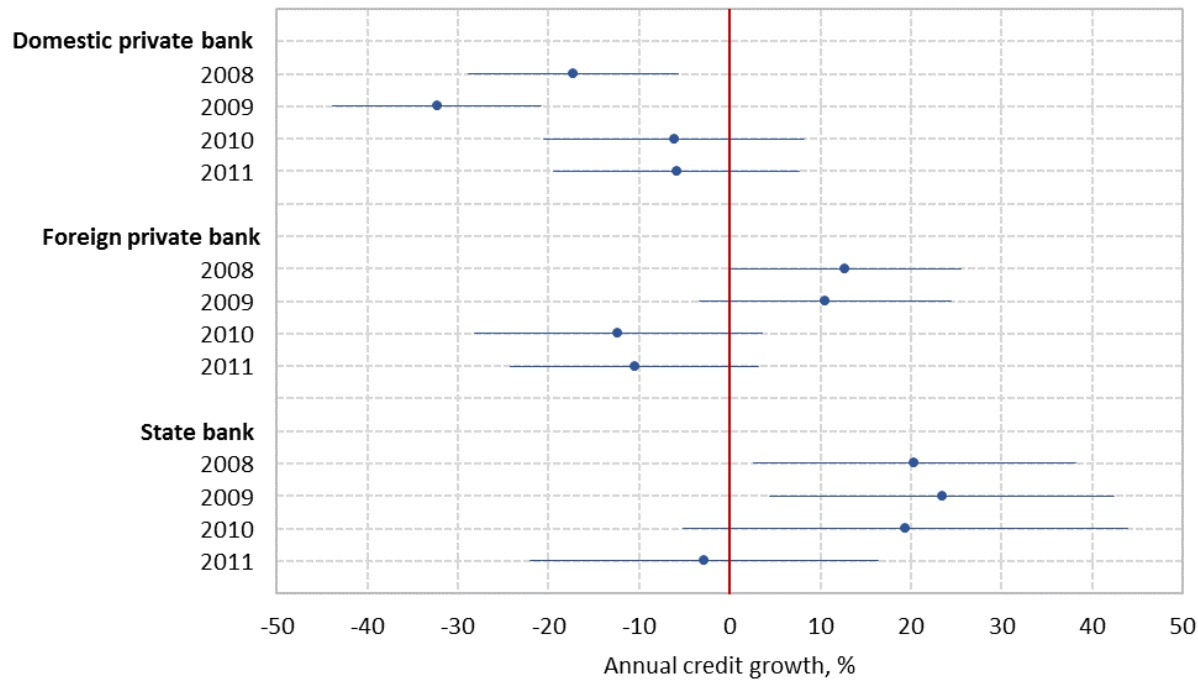


...and higher levels of non-performing loans

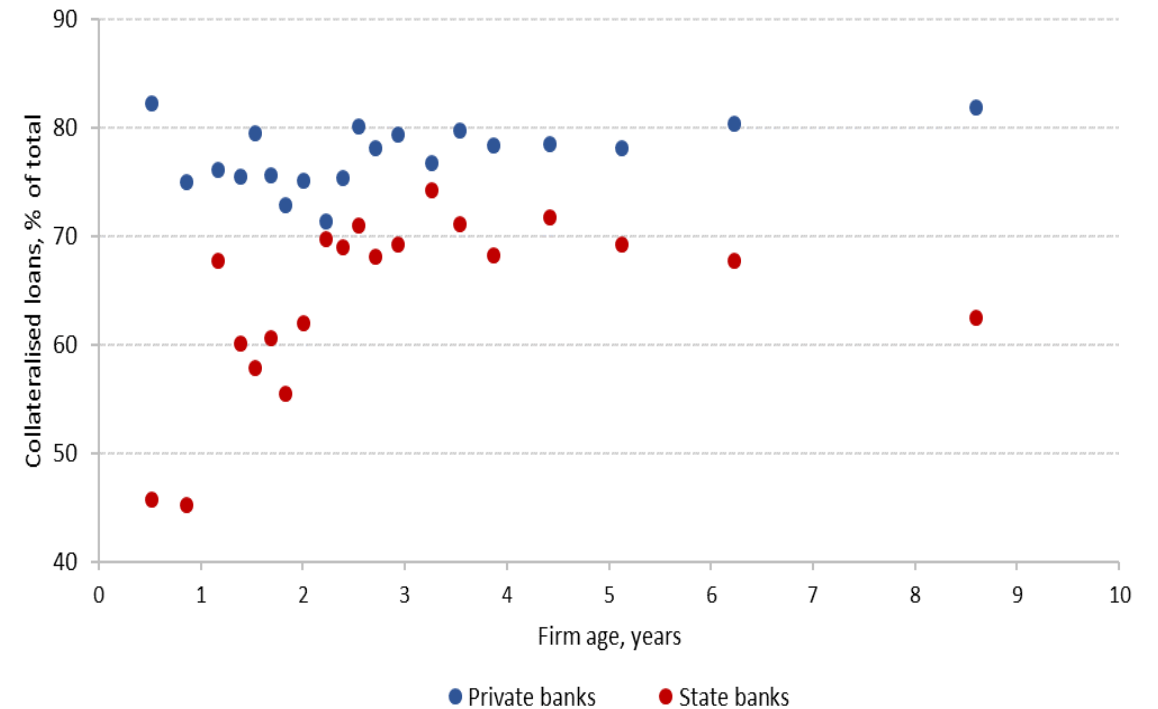


State banks greater risk appetite can soften the impact of crises and give young firms access to credit

Unlike private banks, state banks increased lending during the Global Financial Crisis



Share of collateralised loans in Turkey is lower for first-time borrowers at state banks

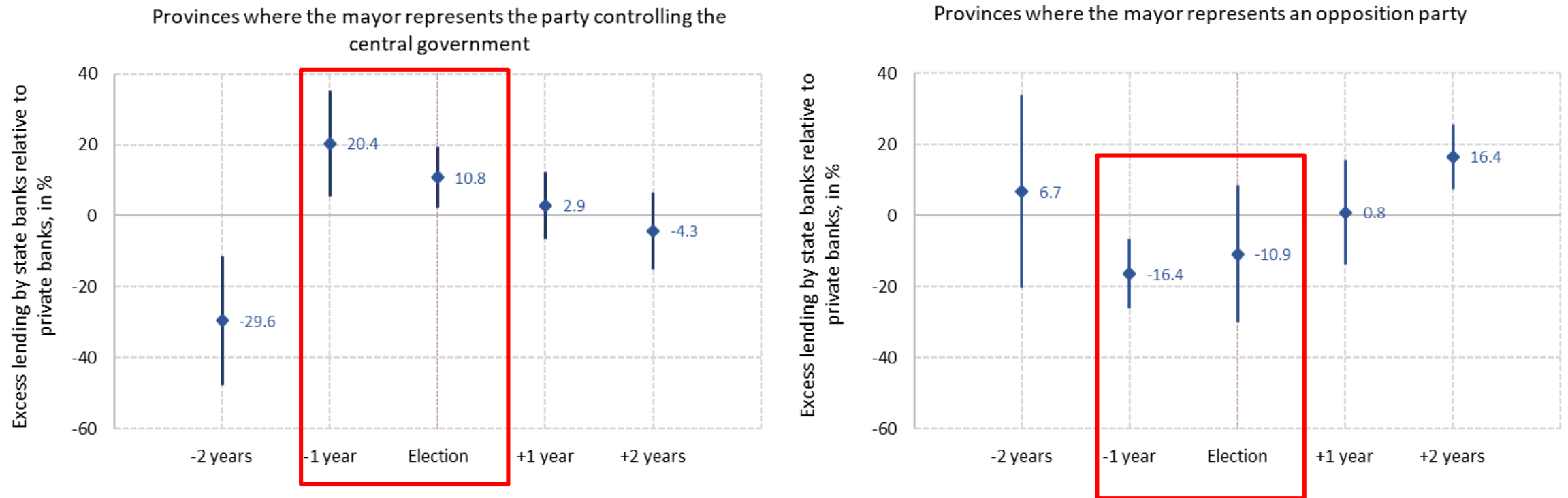


State banks may misallocate credit due to electoral cycles

Before local elections, state bank lending increases by more than private bank lending in provinces where an **incumbent mayor is aligned with the ruling party** and faces a close election

Closely contested provinces get relatively less credit from state banks if **the incumbent mayor is from opposition**

Tactical redistribution of state bank lending around the time of local elections in Turkey



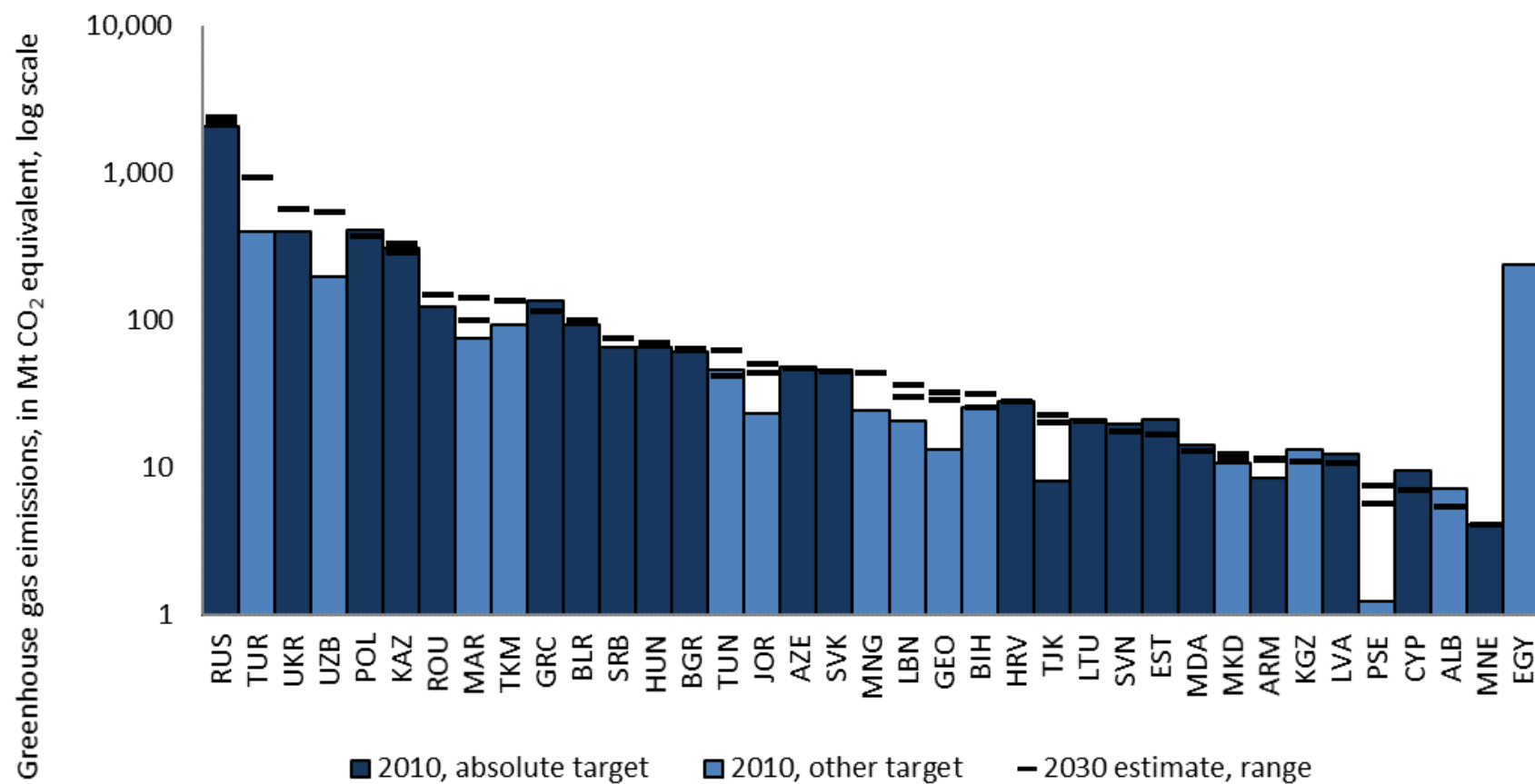
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THE STATE AND THE GREEN ECONOMY



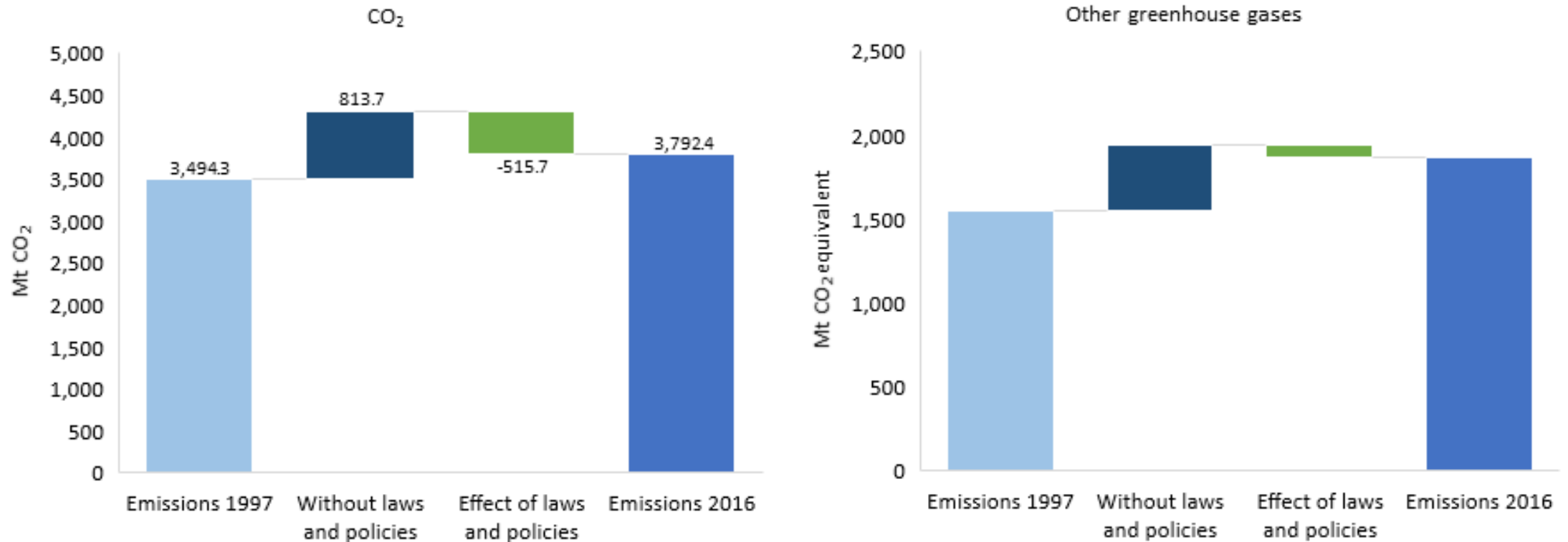
Emission reduction targets in the context of Paris Agreement lack the necessary ambition

Nationally determined contributions commitments in the EBRD regions mostly imply an increase in overall emissions between 2010 and 2030



Green policies and laws are estimated to have reduced EBRD regions' emissions by 12%, but more action is needed

Green laws and policies have not offset the rise in CO₂ emissions in the EBRD regions and the Czech Republic



The guiding hand of the state is needed to build a green economy

Short term	Medium term	Longer term
Retrofit government-owned buildings	Getting (energy) prices right: <ul style="list-style-type: none">• Eliminate fossil fuel subsidies• Apply cost to carbon pollution	Integrate environmental policies into a wider industrial strategy aimed at achieving clean growth
Invest in: <ul style="list-style-type: none">• Energy-efficient residential buildings• Infrastructure• Renewable energy• Energy management systems	Improve the dissemination of information about green technologies and associated funding options	Continue subsidising R&D in clean technologies
Spend on R&D (general or in the area of clean energy)		Foster the diffusion of clean technology
Free energy audits for firms, with access to subsidised financing		Strengthen social safety nets and provide targeted support to displaced workers
		Provide adequate social protection for low-income households

Conclusions

The EBRD regions find themselves at the crossroads

- Optimistic scenario: the Covid crisis will lead to improved governance and **the caring hand of the state** will guide countries through low carbon transition
- Pessimistic scenario: **the grabbing hand of the state** will lead to corruption & nepotism; increased state presence in the economy will **tilt the playing field against the private sector**

The governance gap in the EBRD regions

