

SOME PRINCIPLES OF STRATEGIC PLANNING

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One peculiarity of the economy of a small country is its strong link with the world economy. The more one-sided the economic activity of the country, the stronger the link. If external factors can have a significant impact on the main export and import articles then this can become an obstacle to economic success from time to time. Failures can be avoided or, at least, softened if we look further ahead and make plans for possible behaviour strategies. This is especially important for transition economies where ongoing economic restructuring is, one way or another, related to finding its place in the market economy system.

Starting Point

The global nature of the system, its complexity and rapid changes make it pointless to draw up detailed and comprehensive strategic development plans, which were earlier used in a number of countries, including Estonia during the Soviet period. **It is sufficient to fix the basic parameters and the dominating relations of the**

system, which will give a whole picture of the actual socio-economic state of the system. This creates an opportunity to continue, if necessary, along the path of either drafting the general vision of a comprehensive development plan or more detailed subprojects. One possible scheme for this is provided in Figure 1.

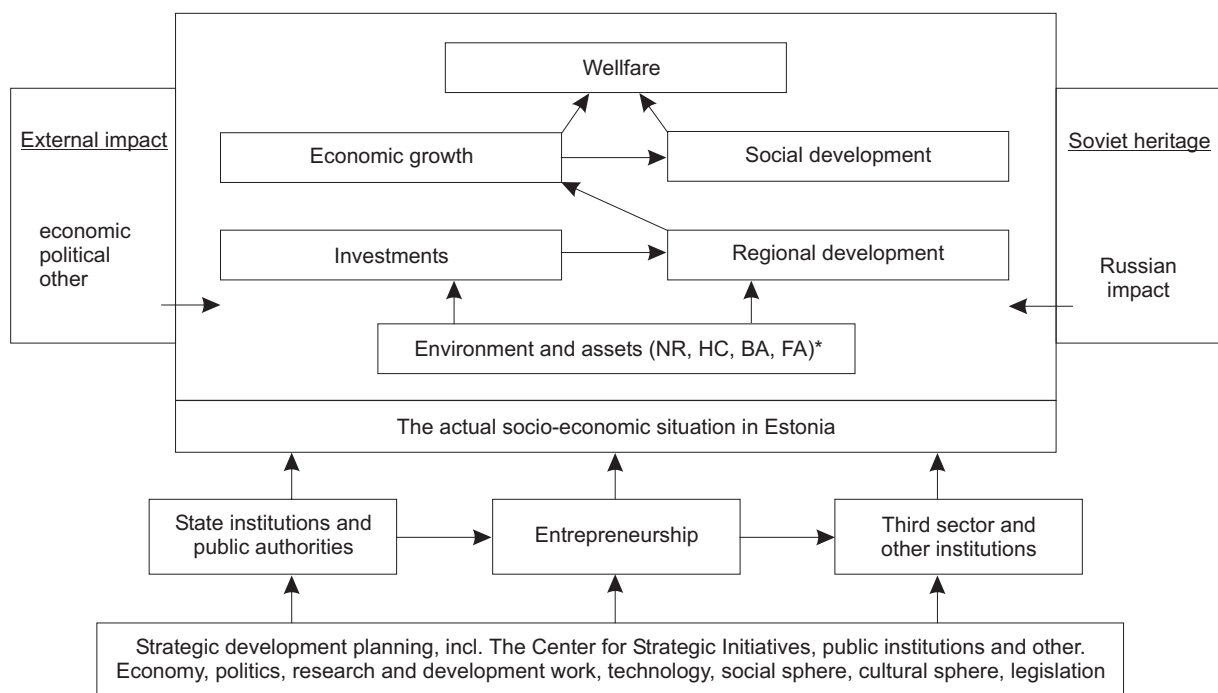


Figure 1. A scheme of a development plan assessing the actual socio-economic situation

* Meaning of abbreviations see on Page 8.

The central result indicator of a country's economic development, which reflects the impact of all inputs, is **economic growth**, measured by the gross domestic product (GDP) and changes in it. Growth is based on the **functioning environment¹, assets and their use**. The assets include natural resources (NR), human capital (HC),

basic assets (BA) and financial assets (FA). The central role in their development and utilization belongs to **investments**. In a small country, as we noted above, much attention has to be paid to the evaluation of the potential impact of the **external factors**, and in transition countries also to the inheritance of the previous economic system.

GDP Analysis² Gives a Preliminary Idea of the Possibilities and Needs of Estonia

A general picture of the nature and results of the restructuring that has taken place in the Estonian economy so far can be seen from economic growth in different spheres of activity (see Table 1). Summing up these changes we can say that the share of the agriculture-dominated **primary sector** has fallen from 11% to 5%. The share of the **secondary sector**, consisting mostly of the manufacturing industry, has decreased from 33% to 29%, mainly due to the declining volumes of the

food processing industry. Timber and furniture industry, however, have grown relatively quickly. The **tertiary sector**, which covers all kinds of services, has increased from 56% to 66%. The bulk of the growth derives from transport (particularly export) as well as real estate and business services. While evaluating these data it has to be emphasized that similar shifts, characteristic of a movement towards the market economy, were clearly evident already before 1993.

Table 1. Changes in the Estonian GDP (%), in constant prices of 1995)

Sphere of activity	1994	1995	1996	1997	1998	1999	2000
Agriculture and hunting	-12.1	-2.7	-6.6	-2.6	-4.7	-7.8	-1.7
Forestry	8.1	27.9	13.5	23.0	8.2	9.2	-1.5
Fishing	3.9	11.7	14.5	26.3	-3.5	-23.3	-18.0
Mining	-6.0	-6.8	7.4	13.4	-7.1	-10.5	8.5
Manufacturing	-3.5	10.3	2.6	16.9	6.3	-1.0	15.8
Energy, gas and water supply	1.2	-3.4	2.3	-2.2	-8.0	-7.4	0.1
Construction	0.8	15.6	6.7	15.6	19.7	-8.7	6.7
Wholesale and retail trade	0.0	9.6	8.4	3.2	5.7	0.3	7.7
Hotels and restaurants	0.8	-7.0	11.2	6.6	13.8	10.9	4.4
Transport, storage and communication	0.6	-3.8	8.3	17.8	9.7	5.3	7.4
Real estate, leasing and business activities	-4.6	-0.6	0.1	12.4	11.8	0.0	3.7
Financial intermediation	5.6	4.4	8.6	16.4	-9.6	8.2	9.4
Public administration, national defence, social insurance	1.1	1.1	0.1	5.4	0.6	0.8	1.2
Education	1.0	3.4	1.7	0.8	1.3	-0.1	-0.2
Health and social care	0.7	-0.2	-1.4	4.0	3.6	2.8	2.8
Other public, social and individual services	-5.3	1.9	11.9	5.7	-1.1	1.7	4.8
TOTAL	-1.7	4.1	4.3	10.0	5.3	-0.2	6.8
FISIM (-)	6.6	2.0	6.0	11.0	-25.7	10.0	10.0
GDP IN BASE PRICES	-1.9	4.1	4.2	10.0	6.0	-0.3	6.8
Net product taxes	-2.6	8.1	2.2	13.6	-1.5	-3.5	7.9
GDP IN MARKET PRICES	-2.0	4.6	4.0	10.4	5.0	-0.7	6.9

In an open economy the main driving force of development is demand – the accordance of demand and supply and the ability of the supplier to adjust to the changing conditions of the market. A more generalized picture of the demand and supply ratio to

the 2000 GDP is given in Table 2. Here we can see that the bulk of Estonia-provided supply is made up of services, dominated by transit and travel services. In a situation where domestic demand clearly outstrips production, the export of goods is dominated by re-export

¹ Functioning or economic environment. See *Results Depend on the Actual Economic Environment* by R. Hagelberg. Eesti Pank Bulletin No 2, 1997, pp 39–42

² All data on Estonia used in this article come from the databases of the State Statistical Office and Eesti Pank.

Table 2. Factors influencing economic growth in 2000 (GDP = 100)

SUPPLY	202	DEMAND	202
GDP	100	EXPORT	97
goods	34	goods	66
services	66	incl subcontracting	19
IMPORT	102	services	31
goods	82	incl transit	15
incl subcontracting	16	travel	10
services	20	DOMESTIC DEMAND	105
		goods	50
		services	55
		CHANGE IN ASSETS	1

and subcontracting. The added value earned through subcontracting was, however, modest – using a simplified comparison it accounted for 3% of the GDP. The main significance of subcontracting was in increased employment. **In general, the data given in the table indicate a great sensitivity of the Estonian economy to external conditions.** We can also see that **domestic demand exceeded the added value created.** This has been characteristic of all previous years as well, with the difference mostly covered by foreign investments used for restructuring and privatization. In the current situation this is logical and understandable, but GDP-exceeding domestic demand for a longer period and used for consumption, would mean dependency.

Problematic Key Issues should be in the Focus of Attention

A selective survey of the data characterizing these key issues is given in Table 3. Domestic demand and the structure of the GDP calculated by the income method have been **compared to Austria**³ in order to find evaluation criteria. Austria represents data of the member countries of the Organization for Economic Cooperation and Development (OECD) that are more characteristic of Estonia and it has been used as a comparison basis for Estonia in a number of earlier statistical studies. **It is**

worth mentioning that there is a remarkable coincidence in the majority of the ratios compared.

This coincidence indicates that the distribution proportions of the Estonian GDP are close to the respective figures of the developed countries. Hence the conclusion that **the main reason for our lower wages and other indicators is lower productivity.** And this is also the reason for the continued shortage of investments,

Table 3. Problematic key figures

DOMESTIC DEMAND IN 2000 (% of GDP)		Estonia	Austria			
Private consumption, households		58.6	56			
Government sector's end consumption		22.2	19			
Investments into fixed assets		23.5	24			
Change in assets		0.6	1			
TOTAL		104.9	100			
GDP IN 2000 BY INCOME METHOD (% of GDP)		Estonia	Austria			
Wages and social tax (37.5+11.9)		49.4	50			
Amortization of fixed assets		14.7	15			
Indirect taxes and subsidies		13.1	13			
Excess of revenues (profit)		22.8	22			
TOTAL		100.0	100			
REGIONAL ASPECT	North Estonia	Central Estonia	North-East Estonia	West Estonia	South Estonia	Estonia total
GDP per capita in 1998 (EEK thousand)	82.4	31.6	29.8	35.0	31.5	50.6
Unemployment rate in 1st quarter of 2001 (%)	11.7	12.0	20.7	12.4	16.6	14.2
Distribution of working age population (%)	40	11	14	12	23	100
INVESTMENTS IN FIXED ASSETS 1993-2000				1993-1996	1997-2000	1993-2000
INVESTMENTS (EEK billion)				37.9	78.6	116.5
o/w direct investments				10.3	34.2	44.5
share of direct investments (%)				27.2	43.5	38.2
RATIO OF INVESTMENTS AND GDP (%)				26.3	26.4	26.4

³ Statistik Austria. Volkswirtschaftliche Gesamtrechnung. Statistisches Jahrbuch 2001, p 286 etc.

despite the large foreign investments received so far. Restructuring and entering into the economic space of the European Union presupposes a considerably higher need for investments than under the normal conditions. The statistics of investments does not characterize expenditures that have to be made into the human capital, education, research, health care, social care, etc, except for investments into the respective fixed assets. In the conditions of transition these spheres have suffered the most from the general shortage of resources. One reason for this is that in developed market economies a large portion of the respective expenses is covered from private consumption and businesses. The use of this

possibility is still limited as well as uncustomary in the present Estonian conditions.

A very acute problem is regional disparity. This applies particularly to the northeastern and southern parts of Estonia. Due to the seriousness of the problems the general public has paid more attention to northeastern Estonia, although, in view of the number of working-aged population southern Estonia deserves equal attention. The seriousness of the problems there is somewhat reduced by the greater involvement in agriculture and some other circumstances.

Some Observations

In the survey above we tried to point to the following important connections:

- **The ratio of the added value created and investments**, which allows us to approximately estimate the efficiency of the investments, has remained more or less unchanged over the period in question. **The share of direct investments has, however, increased considerably.** This allows us to estimate at least indirectly the role of foreign investors in the Estonian economy so far.
- **The connection between economic growth, social development and welfare.** As we can see from Table 1, the GDP increased 1.3 times in 1993-2000 in constant prices. In current prices the increase was fourfold. The average real wage increased nearly 1.5 times over this period. The comparison of these figures, in view of the share of the wages and social taxes in the GDP, indicates that **there are no real ways for increasing wages and social benefits through changes in the distribution proportions. The main solution lies in the increase of productivity and understandably also employment.** And here, again, an important role belongs to investments.
- The complicated process of evaluating the sensibility and efficiency of the investments points to two sore issues through the data provided. These are the **relations between supply and demand** (see Table 2), where an important role belongs to the external market, and the **regional aspect** on which the creation of new jobs depends. Both are inter-related, as production for the internal market is relatively limited.