

**PRESS RELEASE****NOT TO BE RELEASED BEFORE 07-07-2009, 12.00 a.m.**

## **wiiw Forecast for Central, East and Southeast Europe, Kazakhstan and China:**

### **Where Have All the Shooting Stars Gone?**

The Vienna Institute for International Economic Studies (wiiw) has just published its latest **Analyses and Forecasts**. The report, titled *Where Have All the Shooting Stars Gone?*, analyses recent economic developments and short- and medium-term prospects of the countries of Central and Eastern Europe, Southeast Europe including Turkey, as well as Kazakhstan, Russia, Ukraine and China. Separate chapters present an overview of developments in the European Union's new member states (NMS) and in the future EU member states (FMS) of Southeast Europe, and deal with the changing role of the IMF in the region and the latest developments in foreign trade.

#### **Global crisis hits the region hard**

The region has been hit hard by the global crisis, particularly via diminishing exports and reduced external financing. The former star performers among the NMS, namely the Baltic States, Slovakia, Slovenia and Romania, suffered a severe shock after September 2008. The growth reversal was somewhat milder in Bulgaria, the Czech Republic, Hungary and Poland. The FMS in Southeast Europe (Croatia, Macedonia and Turkey; further Albania, Bosnia and Herzegovina, Montenegro and Serbia) experienced a dramatic drop of GDP in early 2009 as well. Falling commodity prices, the credit squeeze, currency devaluations and dwindling investments are the main reasons behind the strong contraction of the economy in Russia, Ukraine and (less so) Kazakhstan. In contrast, GDP growth in China remains robust – despite some recent slowdown.

#### **Fixed exchange rates and euro may hinder adjustment**

Countries with fixed exchange rates or the euro came off worse than those with flexible exchange rates in terms of GDP growth as the former are unable to adjust to the changed external environment through depreciation. Depreciation can provide some competitiveness gain as the recent export data testify. Another positive effect is the elevated level of protection for domestic producers and reduced import demand. For the export-oriented countries shrinking foreign demand is the main concern. In early 2009 exports dropped to only 60-80% of the January 2008 level. A very strong contraction of investments, a depletion of inventories and shrinking consumption led, together with lower energy prices, to an even more severe contraction in imports. These developments result in rapidly improving trade balances and, along with evaporating profits of foreign-owned enterprises, also improving current account positions. These changes coincide with sharply diminishing capital inflows.

### **Limited room for fiscal stimuli**

Among the NMS, only the Czech Republic, Slovenia and Bulgaria are pursuing an active anti-cyclical fiscal policy in order to ease the consequences of the crisis. Hungary, Romania and the Baltic States, however, are following a pro-cyclical fiscal policy. The latter countries had either a poor record of fiscal discipline (Hungary) or unsustainably high current account deficits (Romania, Baltic States) and must regain the confidence of international financial investors. This is also a cornerstone of the IMF stand-by agreements in force with Hungary, Romania and Latvia. Among the FMS the governments of Macedonia and Turkey have engaged in fiscal stimulation measures, nevertheless the realization of these programmes is questionable as deficit and debt are high anyway. In Russia considerable fiscal spending, financed largely by earlier accumulated reserves, has been launched to mitigate the extent of economic decline.

### **Deep recession in 2009, pronounced recovery not until 2011**

The wiiw forecast is based on the assumption that the global crisis is already bottoming out. Throughout 2009 the region will be affected by persisting limits on external financing, higher borrowing costs and weak foreign and domestic demand. wiiw expects that in most countries covered in this report, GDP decline will have bottomed out over the second half of 2009. A pronounced recovery, however, is not thought to set in before 2011. There are numerous downward risks which may render this scenario too optimistic: in order to gain strength, the recovery in the NMS, FMS and former Soviet Union will need to be backed by an improving global or at least European business climate. There is no guarantee yet that this situation will materialize. Finally, there is still the possibility of exchange rate crises (including the breakdown of fixed/pegged exchange rate regimes) with accompanying contagion effects.

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## Overview developments 2007-2008 and outlook 2009-2011

	<b>GDP</b>					<b>Consumer prices</b>					<b>Unemployment, based on LFS <sup>1)</sup></b>					<b>Current account</b>				
	real change in % against previous year					change in % against previous year					rate in %, annual average					in % of GDP				
	2007	2008	2009	2010	2011	2007	2008	2009	2010	2011	2007	2008	2009	2010	2011	2007	2008	2009	2010	2011
	<b>Forecast</b>					<b>Forecast</b>					<b>Forecast</b>					<b>Forecast</b>				
Czech Republic	6.0	3.2	-1.5	1	3	2.9	6.3	1.0	2.0	2.5	5.3	4.4	7	7.0	6.5	-3.2	-3.1	-1.8	-1.4	-1.9
Hungary	1.2	0.5	-6.5	-1.5	3	7.9	6.0	4.7	4.3	3	7.4	7.8	10.5	11	10	-6.4	-8.4	-4.4	-4.0	-3.9
Poland	6.6	5.0	0.8	1.5	3.0	2.6	4.2	3.3	2.6	2.5	9.6	7.1	9	10	9.0	-4.7	-5.5	-1.7	-2.2	-2.9
Slovakia	10.4	6.4	-5	0	1	1.9	3.9	2	2	3	11.1	9.5	13	14	14	-5.7	-6.6	-4.7	-5.1	-5.3
Slovenia	6.8	3.5	-4	1	3	3.8	5.5	1.5	2	2	4.8	4.4	7	7.5	7	-4.2	-5.5	-2.8	-3.2	-4.1
<i>NMS-5 <sup>2)3)</sup></i>	6.0	4.0	-1.5	0.8	2.8	3.5	5.0	2.8	2.6	2.6	8.5	6.9	9.2	9.9	9.1	-4.7	-5.5	-2.5	-2.6	-3.1
Bulgaria	6.2	6.0	-3	0	3	7.6	12.0	2	2	3	6.9	5.6	9	9	8	-25.2	-25.3	-13.9	-12.2	-10.7
Romania	6.2	7.1	-6	0	3	4.9	7.9	6	4	3	6.4	5.8	9	9	8	-13.5	-12.2	-5.0	-5.3	-5.9
Estonia	6.3	-3.6	-16	-10	-2	6.7	10.6	0	-4	-2	4.7	5.5	15	18	18	-18.1	-9.2	1.1	1.8	-0.9
Latvia	10.0	-4.6	-20	-12	-2	10.1	15.2	3	-5	-4	6.0	7.5	18	22	20	-22.5	-12.7	0.5	1.9	2.8
Lithuania	8.9	3.0	-16	-13	-3	5.8	11.1	4.5	-2	0	4.3	5.8	15	19	18	-14.6	-11.6	0.7	-2.1	-2.6
<i>NMS-10 <sup>2)3)</sup></i>	6.2	4.3	-3.3	-0.1	2.5	4.2	6.3	3.3	2.5	2.4	7.7	6.5	9.4	10.0	9.1	-7.7	-7.6	-3.1	-3.2	-3.7
<i>EU-15 <sup>3)</sup></i>	2.7	0.6	-4.0	-0.1	.	.	.	.	.	.	7.0	7.1	9.5	11.1	.	0.1	-0.3	.	.	.
<i>EU-27 <sup>3)</sup></i>	3.1	1.0	-3.9	-0.1	.	2.3	3.7	0.7	1.3	.	7.1	7.0	9.5	10.9	.	-0.5	-0.9	-1.9	-2.0	.
Croatia	5.5	2.4	-4	0.5	2	2.9	6.1	3	2.5	2.5	9.6	8.4	10.5	11	10	-7.6	-9.4	-6	-6	-6.5
Macedonia	5.9	5.0	-2	0	2	2.3	8.3	3	3	3	34.9	33.8	34	33	33	-7.2	-13.1	-7	-8	-8
Turkey	4.7	1.1	-7.0	1	3	8.8	10.4	6	5	4	9.9	10.6	16	17	17	-5.9	-5.6	-2.1	-2.5	-2.7
<i>Candidate countries <sup>2)3)</sup></i>	4.8	1.3	-6.7	0.9	2.9	8.2	10.0	5.7	4.8	3.9	10.7	11.2	16.5	17.4	17.3	-6.1	-6.0	-2.5	-2.9	-3.1
Albania	6.2	8	-1	1	5	2.9	3.4	2	2	3	13.5	12.8	15	16	14	-10.5	-14.4	-14.5	-13.7	-13.2
Bosnia & Herzegovina	6.8	5.0	-3	-1	1	1.5	7.5	-0.5	0	1	29.0	23.4	27	28	27	-10.4	-15.1	-9	-8	-8
Montenegro	10.7	8.1	-3	-1	2	4.2	7.4	3	3	3	19.3	17.2	19	20	20	-29.4	-29.2	-10	-10	-10
Serbia	6.9	5.4	-4	0	2	7.0	11.7	8	6	3	18.1	14.0	18	20	20	-15.7	-17.6	-10	-10	-11
<i>Potential candidate countries <sup>2)3)</sup></i>	7.0	5.9	-3.2	-0.1	2.3	5.0	9.1	4.9	3.9	2.6	19.2	15.7	19.1	20.7	19.9	-14.5	-17.3	-10.1	-9.8	-10.9
Kazakhstan	8.7	3.3	-2	2	4.5	10.8	17.1	9.5	8	7	7.3	6.6	7.5	7	6.5	-7.0	5.2	-4.6	-2.3	-1.7
Russia	8.1	5.6	-4.7	4.0	4.1	9.1	14.1	12	10	8	6.1	6.3	10.5	10	9	5.9	6.1	3.1	2.4	2.2
Ukraine	7.9	2.1	-11.0	1.5	4.5	12.8	25.2	16	12	10	6.4	6.4	8.5	8	7.5	-4.1	-7.2	-0.8	0.4	0.7
China <sup>4)</sup>	13.0	9.0	7	8	8.2	4.8	5.9	0.5	1	2	4.0	4.2	4.6	4.3	4.2	11.0	9.9	6.3	6.8	6.3

Note: NMS: The New EU Member States.

1) LFS - Labour Force Survey. - 2) wiiw estimate. - 3) Current account data include flows within the region. - 4) Registered urban unemployment rate, end of period.

Source: wiiw (June 2009), Eurostat. Forecasts by wiiw and European Commission (Economic Forecast, Spring 2009) for EU-15 and EU-27.