PRESS RELEASE **NOT TO BE RELEASED BEFORE 28-11-2013, 12.00 a.m.**

New wiiw forecast for Central, East and Southeast Europe, 2013-2015:

No take-off so far, wait for external push

The outlook for the Central, East and Southeast European (CESEE) countries– most of which are small and open economies – is crucially dependent on the acceleration of recovery in the euro area and particularly in Germany. Otherwise, the cross-country differences in economic performance will be to a large extent due to the differences in the fiscal policies pursued. Budget austerity is likely to dampen economic growth in Albania and Russia and may trigger outright recession in Serbia, while a welcome fiscal relaxation should be to varying degrees growth-conducive in the Czech Republic, Bulgaria, Romania and Kosovo. All in all, wiiw projects that economic growth in the new EU Member States (NMS) will pick up to 2% on average next year and to around 3% in 2015. Economic dynamics should also accelerate in several Western Balkan countries – though not in Serbia – and remain strong in Latvia, Lithuania and Kazakhstan, but will stay generally unimpressive in Russia and Ukraine.

The hesitant upturn in the euro area has had so far only a limited impact on the CESEE region. Wherever there has been an improvement in the export dynamics, this has been in many cases on account of exports to markets outside the euro area, which are generally more dynamic. At the same time, in the NMS – with the notable exception of the Baltic States – and in several Western Balkan countries domestic demand remains largely depressed, and in Poland it has weakened relative to the previous years. Their GDP growth continues to be too low to bring down unemployment and induce a meaningful increase in wages and incomes which could stimulate consumption, while investments are constrained by the uncertain economic prospects. As a result, their economic dynamics continues to be driven almost exclusively by net exports, and is accompanied by a further improvement in external balances.

Out of four NMS which were in recession last year, only Hungary has so far returned to positive growth, whereas in the Czech Republic, Croatia and most notably Slovenia the economy continues to decline. On average, the economies of the NMS should expand in 2013 by just 0.8% – the same rate as last year. However, as the recession in the 'old' EU is expected to be shallower this year, the speed of the real income convergence will further decline. At about 1 percentage point growth differential between the NMS and the 'old' EU, it currently adds little to EU economic and social cohesion.

A more balanced growth path is pursued by the Baltic States and also in Albania and Macedonia where domestic demand is generally more buoyant. Finally, the economies of Russia, Kazakhstan and Ukraine are driven primarily by private consumption, fuelled in part by rapid credit expansion.

A-1060 Wien, Rahlgasse 3 ZVR-Zahl
T: (+43-1) 533 66 10, F: (+43-1) 533 66 10-50, wiiw@wiiw.ac.at, www.wiiw.ac.at 329995655

However, in Russia economic growth has slowed down markedly (to below 2% in 2013) on account of stagnating domestic investment. The deceleration in Russia has also had an impact on neighbouring Ukraine, although other factors such as depressed steel markets and the recent politically motivated Russian trade sanctions have played a role as well.

Weak domestic demand and the recent cuts in administered prices in a number of CESEE countries have mitigated inflationary pressures, and those countries still retaining at least some degree of monetary policy autonomy – Poland, Hungary, Romania, Serbia, Albania, Russia and Ukraine – have cut policy interest rates in response. However, in Serbia and Ukraine the scope of interest rate cuts has been constrained by concerns over the exchange rate stability. In other cases, the effectiveness of monetary loosening is questionable given that the monetary transmission mechanism remains largely impaired, as tight Basel-3 capital adequacy requirements and overall risk aversion limit the commercial banks' willingness to lend. Besides, even falling interest rates may not necessarily induce additional credit demand in the face of still prevailing uncertainties – as has been the case for years in the Czech Republic with its very loose monetary policy. Finally, in Russia monetary relaxation is unlikely to address the structural weaknesses which are behind the recent stagnation of investments and the GDP growth slowdown. Addressing these weaknesses will require resolute institutional reforms aiming at economic diversification and political modernisation – both of which are currently not in sight.

Unlike monetary policy, the fiscal stance in the CESEE region remains by and large fairly restrictive, although in Poland, Bulgaria and Romania the austerity course has been softened somewhat. Also in the Czech Republic, where public debt is rather low and particularly cheap to finance, the new government will probably abstain from the previous ill-conceived austerity policies. On the other hand, fiscal consolidation features prominently on the government agenda in Serbia and Albania (in both cases motivated by the high public debt stocks approaching 70% of GDP), as well as in crisis-torn Slovenia. Also Russia continues to stick to its policy of balanced budgets by way of restraining social spending – despite the country's negligible public debt and available fiscal buffers in the form of sovereign wealth funds.

The main risks to the near-term forecast for CESEE stem from the global economic developments, particularly those in the EU and the United States. For instance, the forthcoming unwinding of the US quantitative easing (QE3) programme could result in a burst of stock market 'bubbles' which have been arguably growing over the past few years, as soaring stock prices have not been backed by corresponding developments in the real economy. Should this scenario materialise, any economic recovery in the euro area will almost certainly stall, with negative repercussions on the CESEE region as well.

wiiw, 28 November 2013

For questions please contact:

Vasily Astrov, tel. 533 66 10 – 30 astrov@wiiw.ac.at
Mario Holzner, tel. 533 66 10 – 28 holzner@wiiw.ac.at

Overview 2011-2012 and outlook 2013-2015

	GDP real change in % against previous year					Consumer prices change in % against previous year					Unemployment, based on LFS rate in %, annual average					Current account in % of GDP				
	2011	2012	2013	2014	2015	2011	2012	2013	2014	2015	2011	2012	2013	2014	2015	2011	2012	2013	2014	2015
			Forecast					Forecast					Forecast					Forecast		
NMS-11																				
Bulgaria	1,8	0,8	0,3	1,1	2,3	3,4	2,4	1,0	1,5	2,0	11,2	12,3	13,0	12,5	12,0	0,1	-1,3	1,0	0,0	-1,2
Croatia	0,0	-2,0	-1,0	0,8	1,5	2,3	3,4	3,5	2,5	2,0	13,5	15,9	17,5	17,0	17,5	-0,9	0,1	0,9	0,1	-0,6
Czech Republic	1,8	-1,0	-1,2	1,4	2,4	2,2	3,5	1,5	1,7	1,8	6,7	7,0	7,6	7,7	7,3	-2,7	-2,4	-1,2	-1,4	-1,6
Estonia	9,6	3,9	1,5	3,7	4,1	5,1	4,2	3,4	4,0	4,2	12,5	10,2	9,0	8,5	8,0	1,8	-1,8	-2,5	-3,0	-3,3
Hungary	1,6	-1,7	0,9	1,2	2,3	3,9	5,7	2,1	2,9	3,0	10,9	10,9	11,0	10,8	10,6	0,5	1,0	1,5	1,3	0,4
Latvia	5,3	5,0	3,6	3,9	4,1	4,2	2,3	0,4	2,0	2,5	15,4	15,0	12,0	11,0	10,0	-2,1	-2,5	-1,7	-2,5	-2,3
Lithuania	6,0	3,7	3,6	3,8	4,2	4,1	3,2	1,5	2,5	3,6	15,4	13,3	12,0	11,0	10,0	-3,7	-0,2	-0,3	-1,9	-3,0
Poland	4,5	1,9	1,0	2,3	3,5	3,9	3,7	0,7	1,9	2,0	9,7	10,1	11,0	10,8	10,5	-5,0	-3,7	-2,1	-3,0	-3,3
Romania	2,2	0,7	1,9	2,2	2,5	5,8	3,4	4,2	3,5	3,5	7,4	7,0	7,5	7,5	7,0	-4,5	-4,4	-2,8	-3,6	-3,6
Slovakia	3,0	1,8	1,0	2,4	3,0	4,1	3,7	1,6	2,1	3,0	13,5	14,0	14,5	14,0	13,0	-3,8	2,2	2,7	2,5	1,6
Slovenia	0,7	-2,5	-2,9	-1,0	0,5	2,1	2,8	2,5	2,0	2,0	8,2	8,9	11,0	11,5	11,0	0,4	3,3	3,4	1,7	0,5
NMS-11 [1]	*3,1*	*0,8*	*0,8*	*2,0*	*2,9*	*3,9*	*3,7*	*1,8*	*2,3*	*2,5*	*9,8*	*9,9*	*10,5*	*10,3*	*9,9*	*-3,2*	*-2,1*	*-0,9*	*-1,6*	*-2,0*
EA-17 [2]	*1,6*	*-0,7*	*-0,4*	*1,1*	*1,7*	*2,7*	*2,5*	*1,5*	*1,5*	*1,4*	*10,1*	*11,4*	*12,2*	*12,2*	*11,8*	*0,4*	*1,8*	*2,7*	*2,9*	*3,0*
EU-28 [1)2)]	*1,7*	*-0,5*	*0,0*	*1,4*	*1,9*	*3,1*	*2,6*	*1,7*	*1,6*	*1,6*	*9,7*	*10,5*	*11,1*	*11,0*	*10,7*	*0,4*	*0,9*	*1,6*	*1,7*	*1,8*
Candidate countries																				
Macedonia	2,8	-0,4	2,0	3,0	3,0	3,9	3,3	3,0	3,0	3,0	31,4	31,0	29,0	29,0	28,0	-2,5	-3,0	-4,0	-6,0	-6,0
Montenegro	3,2	-2,5	2,0	2,1	2,9	3,1	4,1	3,0	3,0	3,0	19,7	19,7	20,0	19,0	19,0	-17,7	-18,6	-15,5	-15,4	-15,4
Serbia	1,6	-1,7	1,4	-0,6	1,0	11,0	7,8	6,0	5,0	5,0	23,0	23,9	25,0	25,0	25,0	-9,1	-10,5	-7,0	-7,0	-8,2
Potential candidate countries																				
Albania	3,1	1,5	2,3	1,7	1,5	3,4	2,0	2,0	1,0	1,0	14,0	13,4	14,0	15,0	15,0	-13,0	-10,6	-9,0	-8,9	-7,7
Bosnia and Herzegovina	1,0	-1,7	0,8	1,9	3,0	3,7	2,1	1,0	2,0	2,0	27,6	28,0	28,0	27,0	27,0	-9,9	-9,6	-9,0	-9,0	-10,0
Kosovo	4,4	2,5	3,0	5,0	4,0	7,3	2,5	3,0	4,0	4,0	44,8	30,9	31,0	29,0	30,0	-13,8	-7,7	-10,6	-12,3	-12,9
Kazakhstan	7,5	5,0	5,0	6,0	6,5	8,3	5,2	7,0	6,5	6,0	5,4	5,3	5,0	5,0	5,0	5,4	0,3	1,1	1,9	2,0
Russia	4,3	3,4	1,7	2,1	2,9	8,5	5,1	7,0	5,5	5,0	6,5	5,5	5,5	5,5	5,5	5,1	3,6	2,9	2,5	2,2
Ukraine	5,2	0,2	-0,5	1,5	2,0	8,0	0,6	-0,3	3,0	4,0	7,9	7,5	7,5	7,5	7,5	-6,3	-8,1	-7,6	-8,1	-8,2

Note: LFS: Labour Force Survey. NMS: The New EU Member States. EA: Euro area 17 countries.
1) wiiw estimate. - 2) Current account data include transactions within the region (sum over individual countries).

Source: wiiw (November 2013), Eurostat. Forecasts by wiiw and European Commission for EU and euro area.(Autumn Report, November 2013).