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Economic Prospects for Central, East and Southeast Europe

Peter Havlik et al.

Recovery – in Low Gear across Tough Terrain

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Executive summary

The outlook for the world economy has improved in the course of 2010 and the recovery has gained strength in the EU as well. The Central, East and Southeast European countries (CESEE) have also recovered from the crisis; the majority of them recorded positive GDP growth. On average, the recent revival of exports has been even stronger than their growth before the crisis. By way of contrast, the trends in industrial output have so far remained more or less flat. The persistent decline in construction and fixed investments – both related to the still hesitant credit markets – represents one of the key downward internal risks to our moderately optimistic regional economic forecast.

The general outlook for the CESEE region in the baseline scenario reckons with a gradual strengthening of economic growth over the period 2011-2013, in most cases rarely exceeding 4% per annum. GDP growth will become more broadly based. The formerly predominant role of external demand will weaken somewhat, while both household consumption and gross fixed investments will ultimately contribute positively to GDP growth. With exports, industrial output levels and eventually also GDP growth having already recovered, the economy is seen as having largely returned 'back to normal' – yet with at least two important differences: (1) post-crisis growth will be slower. That slower growth, however, also implies that (2) the labour market situation will be 'very far from normal' as unemployment will remain high, with young and low-skilled workers being especially adversely affected, and any improvement only gradual and delayed.

Inflation rose throughout 2010 as food and commodity prices soared; in general, however, it will pose no (or little immediate) threat. The moderate economic upturn and a revival of capital inflows have resulted in renewed appreciation pressures. The forecasts point to a gradual deterioration of current account positions in all CESEE countries, yet the return (or persistence) of extreme imbalances are only expected for Montenegro, Albania and Serbia. The financing constraint with respect to both domestic and external loans will constitute one of the key brakes on future economic growth. Given the sorry state of public finances and the ensuing budget consolidation efforts, we cannot expect any new additional growth-stimulating measures from the public sector – on the contrary, owing to the limited fiscal space government deficits and public debts will be scaled back.

The sharp drop in GDP in most CESEE countries during the crisis resulted in both absolute and relative declines in their per capita GDP. The catching-up process of the previous decade was thus interrupted and income gaps vis-à-vis Western Europe widened. In the baseline GDP growth scenario wiiw reckons with a renewed catching-up process starting as early as 2011 (after losing 5 to 7 years in terms of income convergence).

Country summaries

In **Bulgaria**, GDP growth for 2010 was close to zero reflecting an ongoing painful rebalancing of the economy: for the most part, further curtailment of domestic demand and reduction of the current account deficit. The marked recovery of exports has been accompanied by a further contraction of both private consumption and, most pronouncedly, investment. The outlook for 2011 and the years thereafter envisages a modest recovery, with GDP growth likely to be curbed by both supply and demand constraints.

The acceleration of GDP growth over the past year in the **Czech Republic** may not necessarily continue in 2011. Growth in consumption and gross fixed investment will be anaemic and many unknown factors lurk in foreign trade. Monetary policy is doing its level best, but fiscal policy is governed by unreasonable consolidation objectives. This policy may be modified at a later juncture, possibly stimulating growth in 2012 and beyond.

In **Estonia, Latvia and Lithuania** alike, exports evolved much more strongly than expected. This has led to a substantial upward revision of the economic growth figures for both 2010 and 2011. In 2011, the revival of gross fixed investments will act as the main engine of growth in the Baltic States, while household consumption will also gain momentum. We expect GDP to increase between 2.8% in Latvia and 4.5% in Estonia in 2011 and between 3.5% and 4.5% in the subsequent two years. Nevertheless, as the rapid growth that marked the pre-crisis period is a thing of the past, the labour market situation will remain disappointing for a longer period of time. Unemployment rates, which in 2007 amounted on average to 5% in the Baltic States, more than trebled in the years leading up to mid-2010 and will remain double-digits throughout the period forecast.

In **Hungary** the economy is finally emerging from recession. Household consumption will increase at a very moderate pace in 2011 as income tax reductions primarily favour well-to-do families whose motivation to consume more is limited. Higher Forex debt service obligations in households will impose a drag on the recovery of consumption. Investment will recover from very low levels, mainly on account of three major FDI projects in the automotive sector. The highest contribution to GDP growth, however, will come once again from net exports. The outlook for 2012 and 2013 is extremely uncertain. While inertia alone would help the economy to achieve a gradual acceleration of the export driven growth, the massive uncertainties surrounding medium-term fiscal sustainability, future monetary policy and the attractiveness of the country for foreign investors leave important questions unanswered.

GDP growth in **Poland**, which was quite impressive during the crisis, has been accelerating at a rather moderate pace, without generating any identifiable imbalances to date – except for a large fiscal deficit which will be corrected. Undue currency appreciation and excessive capital inflows constitute the major associated risks. Under such conditions a competent monetary policy is more than called for.

After two years of contraction, the economy in **Romania** will start to recover in 2011. A return to the pre-crisis boom is impossible owing to constrained external financing; however, a mini-boom can be expected in the election year 2012. In all likelihood, this will be followed by a new wave of fiscal stabilization and growth deceleration. Drivers of this economic cycle are already visible in the current government plans, but the actual magnitude of economic growth will hinge on the economic policy selected and the response of the capital markets.

In **Slovakia** GDP growth was mostly driven by: (i) external demand for motor cars; and (ii) improved cost- competitiveness (such as real depreciation and lower ULCs). However, the unemployment rate also rose and impaired the purchasing power of households. If current circumstances prevail, the GDP may continue to maintain its current rate of growth in the years to come. However, the current account deficit and public debt will also increase. The main challenges for the new centre-right government relate to fiscal consolidation (a general government deficit at 8% of GDP in 2010), high unemployment, cronyism and corruption, as well as coping with low R&D funding over the long term.

GDP growth in **Slovenia** was subdued in 2010. Backed primarily by foreign demand, the economy should grow by some 2% in 2011, while a more pronounced upswing can only be expected in 2012, provided a recovery in investment and private consumption sets in. Household consumption will only increase, if labour market conditions improve. Developments in the European Union will be key to a sustained economic upswing.

In **Croatia** the economy faced another year of recession in 2010. The recovery expected for 2011 hinges on a further improvement in external demand. Employment will continue to contract as the labour market reacts rather belatedly to production growth, and unemployment is expected to stagnate or at best drop only slightly. It is thus expected that private consumption will recover only gradually. The current account deficit will remain within more moderate limits than before the crisis, ranging between 4-5% in the years to come. Servicing foreign debt will remain one of the key challenges.

In the short run, some speed-up of growth can be expected in **Macedonia** as external demand continues to improve and that feeds into investment and consumption. At the same time, some deterioration of external balances could be expected, but that should not threaten the exchange rate and the macroeconomic stability. Some growth of employment is also likely, though not enough to make a noticeable dent in the rate of unemployment. A significant acceleration of growth cannot be expected even in the medium term.

The speed-up of the recovery in **Montenegro** depends on the performance of the tradable sector. In the medium run, growth prospects will depend on the resilience of foreign investments. Montenegro continues to be attractive for investments in tourism and in real estate. As the country is expected to start negotiations for EU membership in the next year or so, that will certainly help. It will also be able to draw on EU funds more than before.

Economic performance in **Turkey** has been impressive, as evidenced by the GDP growth rate over the past year. Should things continue at this speed, continued high import growth will fuel fears of overheating. Even now the current account deficit is higher than ever before; it is predominantly funded by short-term capital inflows. The central bank is alert to the risk and has responded with a low policy rate in tandem with increases in reserve requirements. Fiscal support for this policy would be helpful, but moderation in terms of expenditures is not a popular topic in the lead-up to the general elections in June 2011. The government is thinking more in terms of boosting revenue via a privatization campaign (mainly related to the energy sector).

In **Albania** the political stalemate after clashes during a violent anti-government demonstration in January 2011 is not expected to have a major economic impact in the short term. However, if the political system is stymied by personal animosities among the country's leading politicians, this might prove to be a major stumbling block on the path to EU membership and subsequent EU transfers and integration into European production networks. For the period 2011-2013, we expect a gradual increase in the GDP growth rate. The forecast hinges on further recovery of the European economy and governmental stimulus of domestic demand.

Bosnia and Herzegovina is experiencing a mild upswing: a trend that is confirmed by statistics, but hardly registered by the general public. Unemployment that was already extremely high prior to the crisis has increased still further compared to the pre-crisis years. Other segments of society were far less hard hit (or not at all) by the crisis, especially those employed in the large government sector. An engine for stronger growth, however, is lacking; it is nowhere to be seen. For the most part, funds from the EU and IFIs keep investment in infrastructure on track. Exports are increasing thanks to a growing demand for metals; however, they cover but half of the country's imports. GDP growth may gradually increase to 3% by 2013; that is not much for a country ranked as an 'emerging market'.

In the medium term, macroeconomic and social stability in **Serbia** will present problems and will weigh on economic growth. The key issue is growth of industrial production, which has mostly stagnated in the last decade and has not yet recovered strongly after the crisis. Given that recovery of other sectors is either unlikely or cannot impact significantly the overall growth, medium-term prospects are rather mediocre.

In **Kazakhstan** the economy recorded a remarkable rebound in 2010. The driving force behind this rapid growth was an upsurge in external demand for oil and metals. Those two sectors will continue to play the dominant role in the Kazakh economy. We expect investment to pick up in the wake of plans to expand the network of pipelines and increase public spending on other infrastructure projects. The after-effects of the housing bubble and banking crisis are still visible and pose an impediment to growth. Inflation will remain within the 6%-7% range, while the tenge will be revalued somewhat during the period forecast.

Economic growth in **Russia** rebounded strongly along with the recovery of oil prices. However, the current forecast reckons with a much lower GDP growth rate than in the pre-crisis period. Both private consumption and investment are expected to grow slightly faster than GDP, while real exports will continue to be sluggish. That notwithstanding, imports will increase at a faster rate as both household consumption and investment fuelled by real currency appreciation start to pick up. Slim are the chances of a successful modernization and restructuring of the economy.

Ukraine is currently recording fairly robust economic growth matched by further political stabilization. This facilitates the implementation of IMF-sponsored fiscal reforms, which aim at diminishing the role of the state in the economy and reducing along sustainable lines the share of public debt to GDP . For the years to come, we expect a continuation of the current rate of growth, driven largely by private consumption and accompanied by a moderate increase in external deficits. Inflationary pressures are likely to intensify in the coming months, given the dynamics of global food prices and the planned hikes in energy and utility tariffs.

Keywords: Central and East European new EU member states, Southeast Europe, future EU member states, Balkans, former Soviet Union, Turkey, economic forecasts, employment, foreign trade, competitiveness, exchange rates, inflation, monetary policy.

JEL classification: G01, G18, O52, O57, P24, P27, P33, P52

Table I

Overview 2009-2010 and outlook 2011-2013

		GDP real change in % against previous year					Consumer prices change in % against previous year					Unemployment, based on LFS [1] rate in %, annual average					Current account in % of GDP				
		2009	2010	2011	2012	2013	2009	2010	2011	2012	2013	2009	2010	2011	2012	2013	2009	2010	2011	2012	2013
				Forecast					Forecast					Forecast					Forecast		
BG	Bulgaria	-4.9	0.3	2.5	3	3	2.5	3.0	4	4	4	6.8	10.2	9	8	7	-9.9	-0.8	-3.8	-4.5	-5.1
CZ	Czech Republic	-4.2	2.3	2.2	2.5	3.7	0.6	1.2	2.0	2.0	2.0	6.7	7.3	7.5	7.0	6.5	-1.1	-2.7	-2.5	-3.0	-3.0
EE	Estonia	-13.9	3.1	4.5	4	4.5	0.2	2.7	4	3.5	4.5	13.8	16.9	13.5	11.5	10	4.5	3.6	0.6	-1.7	-2.7
HU	Hungary	-6.7	1.2	2.5	3	3	4.0	4.7	3.9	3.5	3.5	10.0	11	10.5	9.3	8.5	-0.4	0.8	-1.6	-2.1	-2.4
LV	Latvia	-18.0	-0.4	3.2	3.5	3.8	3.3	-1.2	3	3	3.5	17.1	18.5	17	15	13.5	8.6	4.5	2.1	-1.5	-2.7
LT	Lithuania	-14.7	1.3	2.9	3.6	3.8	4.2	1.2	3	2.5	2.5	13.7	17.8	16	14.5	13	4.3	1.3	-0.7	-2.6	-3.6
PL	Poland	1.7	3.8	3.8	4.2	4.3	4.0	2.7	3.5	2.5	2.5	8.2	10.5	10	8.5	7.5	-2.2	-3.2	-3.5	-3.8	-4.1
RO	Romania	-7.1	-1.2	2	4	3	5.6	6.1	5.5	4	4	6.9	7.4	7.6	7	7	-4.2	-4.2	-5.2	-6.4	-6.3
SK	Slovakia	-4.8	4	4	4	5	0.9	0.7	2	3	3	12.0	14.8	14	13	12	-3.2	-3.0	-4.6	-4.9	-5.1
SI	Slovenia	-8.1	1.2	2	2.5	3	0.9	2.1	2.8	2.5	2.5	5.9	7.5	7.5	7	6.5	-1.5	-1.1	-1.6	-1.7	-1.7
	NMS-10 [2)3)]	**-3.6**	**2.1**	**3.0**	**3.6**	**3.8**	**3.3**	**3.0**	**3.5**	**2.9**	**2.9**	**8.5**	**10.2**	**9.9**	**8.8**	**8.0**	**-1.9**	**-2.3**	**-3.1**	**-3.8**	**-4.0**
	EU-15 [3)]	*-4.3*	*1.8*	*1.6*	*1.9*	.	.	.	.	.	.	*9.0*	*9.5*	*9.6*	*9.3*	.	*-0.1*	*-0.1*	.	.	.
	EU-27 [3)]	*-4.2*	*1.8*	*1.8*	*2.1*	.	*1.0*	*2.1*	*2.1*	*1.8*	.	*8.9*	*9.6*	*9.6*	*9.2*	.	*-0.2*	*-0.3*	.	.	.
HR	Croatia	-5.8	-1.5	1	2	3	2.4	1.1	2.5	2	2.5	9.1	12.0	11.5	10	9.5	-5.5	-3.1	-4	-5	-5
MK	Macedonia	-0.8	0.5	2	3	3	-0.8	1.7	3	3	3	32.2	32.5	33	33	33	-7.2	-1.4	-4	-5	-5
ME	Montenegro	-5.7	-1	2	3	3	3.4	0.6	3	3	3	19.3	20	20	20	20	-30.1	-23.3	-22	-21	-22
TR	Turkey	-4.5	7.5	4.4	4.0	3.7	6.3	8.6	6.0	5.5	5.5	12.7	10.9	9.9	10.0	10.2	-2.3	-6.2	-6.2	-5.7	-5.5
	Candidate countries [2)3)]	**-4.5**	**6.7**	**4.1**	**3.9**	**3.6**	**5.8**	**7.9**	**5.7**	**5.2**	**5.3**	**13.2**	**11.8**	**10.8**	**10.8**	**10.9**	**-2.9**	**-6.0**	**-6.1**	**-5.7**	**-5.5**
AL	Albania	3.3	4.0	3.2	4	5	2.3	3.5	3	3	4	13.8	15	15	14	13	-15.5	-10.2	-12.6	-13.7	-16.1
BA	Bosnia & Herzegovina	-2.9	0.8	2.2	3	3	-0.4	2.1	1	1	1	24.1	27.2	27	27	26	-6.8	-7.1	-7	-6	-6
RS	Serbia	-3.1	1.5	2.5	3	3	8.6	6.8	7	6	6	16.1	19.2	20	20	20	-7.0	-6.3	-8	-10	-10
	Potential candidate countries [2)3)]	**-1.8**	**1.8**	**2.6**	**3.2**	**3.4**	**5.4**	**5.1**	**4.9**	**4.3**	**4.5**	**17.2**	**19.8**	**20.2**	**19.8**	**19.3**	**-8.4**	**-7.2**	**-8.6**	**-10.0**	**-10.3**
KZ	Kazakhstan	1.2	7.1	5.5	5	5	7.3	7.4	7	6.5	6.5	6.6	5.8	5.7	5.5	5.5	-3.1	3.1	3.2	2.3	1.8
RU	Russia	-7.8	4.0	4.1	4.2	4.3	11.8	7.1	7	5	5	8.4	7.5	7.3	7	6.8	4.0	5.0	4.1	3.4	2.8
UA	Ukraine	-14.8	4.2	4.5	5	5	15.9	9.4	10	8	7	8.8	8.6	8.6	8.4	8.2	-1.5	-1.9	-2.5	-2.8	-3.1

Note: NMS: The New EU Member States.

1) LFS – Labour Force Survey. - 2) wiiw estimate. - 3) Current account data include flows within the region.

Source: wiiw (February 2011), Eurostat. Forecasts by wiiw and European Commission (Economic Forecast, Autumn 2010) for EU.

Table II

Central and East European new EU member states (NMS-10): an overview of economic fundamentals, 2010

	Bulgaria	Czech Republic	Estonia	Hungary	Latvia	Lithuania	Poland	Romania	Slovakia	Slovenia	*NMS-10* [1]	*EU-15*	*EU-27* [2]
GDP in EUR at exchange rates, EUR bn	36.76	145.94	14.70	99.46	18.20	27.66	357.97	124.04	66.20	36.56	*927.5*	*11316.2*	*12267.3*
GDP in EUR at PPP, EUR bn	80.01	208.88	20.91	156.46	27.63	43.94	569.81	232.87	98.14	43.30	*1481.9*	*10738.9*	*12267.3*
GDP in EUR at PPP, EU-27=100	0.7	1.7	0.2	1.3	0.2	0.4	4.6	1.9	0.8	0.4	*12.1*	*87.5*	*100.0*
GDP in EUR at PPP, per capita	10200	19900	15600	15600	12400	13400	14900	10800	18100	21100	*14500*	*27000*	*24400*
GDP in EUR at PPP per capita, EU-27=100	42	82	64	64	51	55	61	44	74	86	*59*	*111*	*100*
GDP at constant prices, 1990=100	128.1	140.4	140.1	127.9	100.4	110.4	188.0 [3]	131.5	163.0	157.2	*160.5*	*140.2*	*143.1*
GDP at constant prices, 2000=100	150.0	136.9	145.9	120.5	143.1	153.3	146.5	149.3	159.7	130.8	*143.3*	*112.4*	*115.5*
Industrial production real, 2000=100 [4]	142.5	146.5	161.6	141.8	145.0	169.4	175.0	126.1	191.6	118.8	*156.3*	*97.0*	*100.9*
Population - thousands, average	7560	10514	1340	10003	2235	3287	38190	21460	5430	2047	*102066*	*398426*	*501668*
Employed persons - LFS, thousands, average	3053	4885	571	3780	945	1345	15900	9200	2300	966	*42945*	*172733*	*216193*
Unemployment rate - LFS, in %	10.2	7.3	16.9	11.0	18.5	17.8	10.5	7.4	14.8	7.5	*10.2*	*9.5*	*9.6*
General gov. revenues, EU-def., in % of GDP	33.5	40.7	41.5	46.0	37.0	34.5	38.2	33.0	32.0	43.7	*38.2*	*44.4*	*43.9*
General gov. expenditures, EU-def., in % of GDP	37.4	45.5	42.8	50.0	45.0	42.5	46.2	40.5	40.0	49.7	*44.9*	*51.1*	*50.6*
General gov. balance, EU-def., in % of GDP	-3.9	-4.8	-1.3	-4.0	-8.0	-8.0	-7.9	-7.5	-8.0	-6.0	*-6.7*	*-6.8*	*-6.8*
Public debt, EU def., in % of GDP	15.3	38.9	8.0	78.5	50.0	40.0	53.2	30.5	42.1	38.5	*46.6*	*81.6*	*79.1*
Price level, EU-27=100 (PPP/exch. rate)	46	70	70	64	66	63	63	53	67	84	*63*	*105*	*100*
Compensation per employee, monthly, in EUR [5]	420	1279	1123	1023	805	790	875	739	1140	2017	*920*	*3214*	*2779*
Compensation per employee, monthly, EU-27=100	15.1	46.0	40.4	36.8	29.0	28.4	31.5	26.6	41.0	72.6	*33.1*	*115.7*	*100.0*
Exports of goods in % of GDP	42.3	65.8	59.5	71.1	37.9	56.0	34.1	30.0	73.3	50.2	*47.4* [6]	*28.8* [6]	*30.6* [6]
Imports of goods in % of GDP	48.8	61.2	61.2	65.9	44.0	60.7	35.9	34.8	72.5	52.9	*48.0* [6]	*29.0* [6]	*30.9* [6]
Exports of services in % of GDP	13.5	11.4	23.1	14.3	15.1	10.8	6.8	5.1	6.6	11.9	*9.1* [6]	*9.7* [6]	*9.7* [6]
Imports of services in % of GDP	8.3	10.9	13.6	12.0	8.8	8.0	5.9	5.7	7.9	9.0	*7.9* [6]	*8.4* [6]	*8.4* [6]
Current account in % of GDP	-0.8	-2.7	3.6	0.8	4.5	1.3	-3.2	-4.2	-3.0	-1.1	*-2.3* [6]	*-0.1* [6]	*-0.3* [6]
FDI stock per capita in EUR, 2009	4678	8053	8420	6810	3590	2931	3210	2329	6431	5212	*4265*	*11360*	*9950*

NMS-10: Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia, Slovenia. PPP: Purchasing power parity.

1) wiiw estimates. - 2) wiiw estimates and Eurostat. - 3) 1989 = 100, which in the Polish case is the appropriate reference year. - 4) EU-15 and EU-27 working day adjusted. - 5) Gross wages plus indirect labour costs, according to national account concept. - 6) Data for NMS-10, EU-15 and EU-27 include flows within the region.

Source: wiiw, Eurostat, AMECO.

Table III

Southeast Europe and selected CIS countries: an overview of economic fundamentals, 2010

	Croatia	Macedonia	Montenegro	Turkey	Albania	Bosnia and Herzegovina	Serbia	Kazakhstan	Russia	Ukraine	*NMS-10* [1]	*EU-15*	*EU-27* [2]
GDP in EUR at exchange rates, EUR bn	45.57	6.96	3.00	555.00	8.85	12.62	29.16	101.19	1103.95	103.10	*927.5*	*11316.2*	*12267.3*
GDP in EUR at PPP, EUR bn	66.13	17.65	6.13	835.00	21.72	24.68	64.89	149.82	1786.52	248.32	*1481.9*	*10738.9*	*12267.3*
GDP in EUR at PPP, EU-27=100	0.5	0.1	0.05	6.8	0.2	0.2	0.5	1.2	14.6	2.0	*12.1*	*87.5*	*100.0*
GDP in EUR at PPP, per capita	14900	8400	9700	11500	6800	6400	8900	9200	12700	5400	*14500*	*27000*	*24400*
GDP in EUR at PPP per capita, EU-27=100	61	34	40	47	28	26	36	38	52	22	*59*	*111*	*100*
GDP at constant prices, 1990=100	111.0	115.0	.	206.5	198.0	.	.	153.2	107.2	65.8	*160.5*	*140.2*	*143.1*
GDP at constant prices, 2000=100	130.9	126.1	137.8	144.3	171.7	142.9	150.0	220.6	159.5	152.4	*143.3*	*112.4*	*115.5*
Industrial production real, 2000=100	122.6	100.9	90.2	146.2	221.3	187.3	106.1	206.1	148.5	154.5	*156.3*	*97.0*	*100.9*
Population - thousands, average	4435	2100	632	72500	3210	3843	7300	16230	141000	45871	*102066*	*398426*	*501668*
Employed persons - LFS, thousands, average	1540	633	204	22600	1100	843	2397	8250	69803	20200	*42945*	*172733*	*216193*
Unemployment rate - LFS, in %	12.0	32.5	20.0	10.9	15.0	27.2	19.2	5.8	7.5	8.6	*10.2*	*9.5*	*9.6*
General gov. revenues, nat. def., in % of GDP	37.8	32.0	45.0	34.0 [3]	26.6	42.5	40.0	21.7	35.5	29.0	*38.2* [3]	*44.4* [3]	*43.9* [3]
General gov. expenditures, nat. def., in % of GDP	43.5	35.0	50.0	38.0 [3]	29.7	47.0	44.8	24.4	35.5	35.0	*44.9* [3]	*51.1* [3]	*50.6* [3]
General gov. balance, nat. def., in % of GDP	-5.7	-3.0	-5.0	-4.0 [3]	-3.0	-4.5	-4.8	-2.7	0.0	-6.0	*-6.7* [3]	*-6.8* [3]	*-6.8* [3]
Public debt, nat. def., in % of GDP	40.9	34.0	43.0	48.0 [3]	61.0	36.0	36.0	16.2	8.7	39.8	*46.6* [3]	*81.6* [3]	*79.1* [3]
Price level, EU-27=100 (PPP/exch. rate)	69	39	49	66	41	51	45	68	62	42	*63*	*105*	*100*
Average gross monthly wages, EUR at exchange rate	1050	488	715	771 [4]	246	621	446	388	523	213	*920* [4]	*3214* [4]	*2779* [4]
Average gross monthly wages, EU-27=100	37.8	17.5	25.7	27.7 [4]	8.8	22.4	16.1	14.0	18.8	7.6	*33.1* [4]	*115.7* [4]	*100* [4]
Exports of goods in % of GDP	19.5	34.5	11.7	16.1	13.0	28.9	24.7	44.5	27.3	38.1	*47.4* [5]	*28.8* [5]	*30.6* [5]
Imports of goods in % of GDP	32.5	57.5	55.7	23.4	35.6	54.7	41.2	23.1	17.1	44.2	*48.0* [5]	*29.0* [5]	*30.9* [5]
Exports of services in % of GDP	18.4	9.8	24.3	4.4	19.0	7.5	8.9	3.2	3.0	12.3	*9.1* [5]	*9.7* [5]	*9.7* [5]
Imports of services in % of GDP	5.7	8.9	10.3	2.5	16.7	3.3	8.9	7.7	4.9	8,9	*7.9* [5]	*8.4* [5]	*8.4* [5]
Current account in % of GDP	-3.1	-1.4	-23.3	-6.2	-10.2	-7.1	-6.3	3.1	5.0	-1.9	*-2.3* [5]	*-0.1* [5]	*-0.3* [5]
FDI stock per capita in EUR, 2009	5749	1530	5233	1300	800	1380	2004	3186	1879	789	*4300*	*11360*	*9950*

NMS-10: Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovak Republic, Slovenia. PPP: Purchasing power parity, wiiw estimates for Albania, Bosnia and Herzegovina, Montenegro, Serbia, Kazakhstan, Russia, Ukraine.

1) wiiw estimates. - 2) wiiw estimates and Eurostat. - 3) EU definition: expenditures and revenues according to ESA'95, excessive deficit procedure. - 4) Gross wages plus indirect labour costs, according to national account concept. - 5) Data for NMS-10, EU-15 and EU-27 include flows within the region.

Source: wiiw, Eurostat, AMECO.

Peter Havlik et al.[1]

Recovery – in low gear across tough terrain

Global economic climate warming, downside risks manageable

At the beginning of 2011, the global economic situation looked much more robust than it had a couple of months earlier. The outlook for the world economy has since undergone a corresponding improvement. In summer 2010 when wiiw was preparing its previous forecast, discussion raged over the shape that the ongoing recovery would take. At the time, a swift and robust upturn in the advanced economies was 'assumed to be most unlikely'; some pessimistic pundits even feared a double-dip recession. As for the countries of Central, East and South-east Europe (CESEE), we wondered whether 'exports [would] prevail over austerity'.[2] The latter scenario, it seems, has indeed been borne out by recent events. Moreover, the *shape of the recovery* in the eurozone that both the European Commission and the IMF had anticipated in their Spring forecasts for 2010-2011 (published in May 2010) proved correct: a mirror image of the radical sign √. However, recovery in 2010 showed itself to be much stronger than the Commission had expected in its Spring 2010 forecast (less than 1% GDP growth for the eurozone). The economic recovery in the EU, especially in Germany (but in Austria, France, Italy and the Netherlands as well) picked up speed in the course of the year. By the time it published its Autumn forecast in November 2010, the European Commission had already revised its 2010 GDP forecast for the eurozone significantly upwards.[3] That notwithstanding, the European Commission, IMF, OECD and EBRD have stressed the uneven pace of recovery, pointing to the high level of uncertainty with considerable downside risks and persistently high unemployment.

The latest global economic forecasts are even more upbeat. The IMF (World Economic Outlook Update, January 2011) has once again modestly revised its figures upwards for global output growth for 2011 compared to the forecast it had published in October 2010. That notwithstanding, it still reiterated its point that growth would remain subdued and unemployment high. Recovery has been a two-speed process, with distinctly lower growth in the advanced economies (+2.5% increase of GDP in 2011) and buoyant activity in many emerging markets (+6.5%). The *shape of current global recovery* would thus seem to have changed within the space of a year: shifting from a mirror image to a normal image of the radical sign, with the sign's right side somewhat elevated (Figure 1). Current downside risks include a renewed incidence of stress in the 'periphery' of the eurozone (debt, deficit financing and banking sector upheavals in Greece, Ireland, Portugal and possibly even Spain)

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1 The research on this overview was completed on 1 March 2011. Contributions by Vasily Astrov, Sebastian Leitner, Hermine Vidovic and Roman Stöllinger, all wiiw, are gratefully acknowledged. Thanks are due also to authors of the individual country reports who provided useful comments on the earlier draft. All remaining errors are the responsibility of the author.

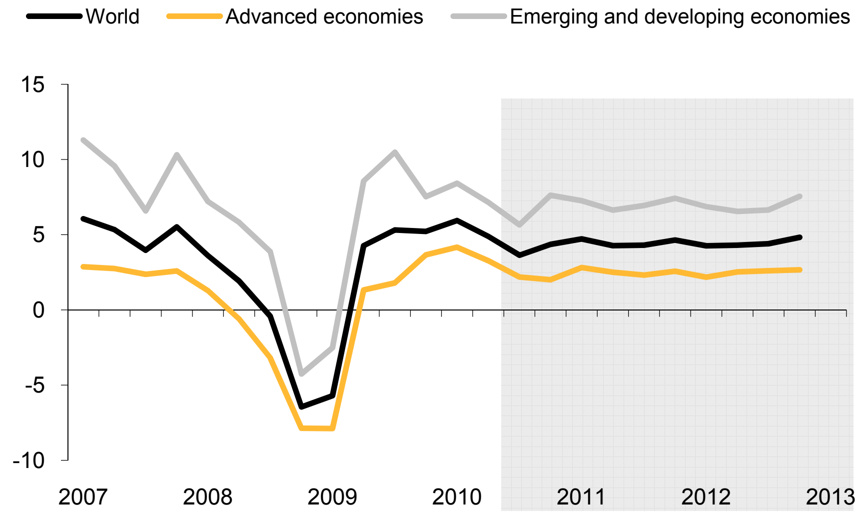
2 All quotations are from the wiiw forecast report prepared in mid-2010 – see V. Astrov, M. Holzner, K. Laski, L. Podkaminer et al, 'Will Exports Prevail over Austerity?', *wiiw Current Analyses and Forecasts*, No. 6, July 2010, p. 23.

3 From 0.9% GDP growth forecast in Spring to 1.7% in Autumn – see 'European Economic Forecast Autumn 2010', Commission Staff Working Document, *European Economy*, 7/2010. Similarly upward revisions were done by the IMF in October 2010 (*World Economic Outlook*, October 2010), OECD (*Economic Outlook*, No. 88, November 2010) and – for the transition countries – by the EBRD (*Transition Report 2010*, November 2010).

Figure 1a

Global GDP growth

change in % against preceding year

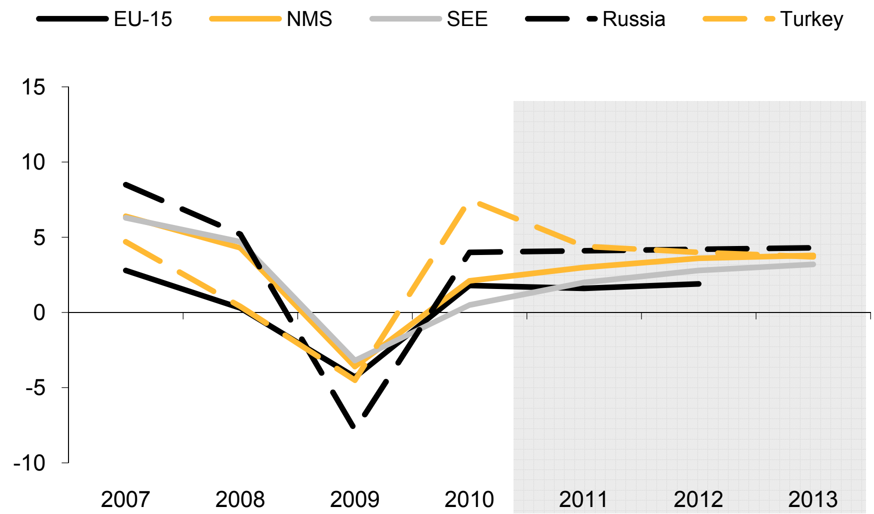


Source: IMF: WEO, Update, January 2011.

Figure 1b

GDP growth in Europe

change in % against preceding year



Source: wiiw, Eurostat. Forecasts by wiiw and European Commission (Economic Forecast, Autumn 2010) for EU.

and the need to reduce sovereign debt and fiscal imbalances on a more general scale not only in the eurozone, but in the advanced economies as well. In key emerging economies signs of overheating are becoming apparent (rising commodity and food prices heralding inflation), as are renewed external imbalances. Last but not least, in some cases potentially destabilizing excessive capital inflows to emerging markets may well call for some form of capital control.[4]

The IMF baseline scenario from January 2011 assumes that the financial turmoil will remain contained in the 'periphery' of the eurozone, with only limited financial spillovers elsewhere. Activity in the advanced economies is expected to increase by 2.5% in 2011-2012 (a slight upward revision for 2011 and a minuscule downward correction for 2012 relative to the previous forecast of October 2010). The recovery in advanced economies will remain too slow to bring about a marked reduction in unemployment. At the World Economic Forum in Davos in January 2011, several prominent speakers spoke of a 'three-speed' global recovery and even the erstwhile doomsayer Nouriel Roubini agreed that the 'glass was half full'.[5] Of significance to several CESEE countries with close trading links to Germany, growth in that country is expected to remain robust (2.4% - albeit lower than the level of 3.6% achieved in 2010), owing to stronger domestic demand and increasing exports; this bodes well for export growth in several CESEE countries. Last but not least, the latest (February 2011) EU Interim forecast is also upbeat regarding the strength of EU economic recovery.[6] Nevertheless, the potentially disturbing repercussions of sovereign debt restructuring in some eurozone countries cannot be dismissed either, although it is reassuring to note the progress achieved in respect of plans to strengthen the European Financial Stability Facility (EFSF) and economic governance in the EU that are currently under discussion.

The current wiiw forecast for the CESEE region for the period 2011-2013 assumes a relatively stable exchange rate of around USD 1.3 per euro, as well as oil prices not exceeding USD 100 per barrel. The latter assumption may appear especially contentious, given the recent events in North Africa and the upsurge in oil prices.

Moderate and multi-speed recovery in the CESEE

The CESEE countries have also been recovering from the crisis. The majority of CESEE countries covered in this report reported positive GDP growth in 2010; only in Latvia, Romania, Croatia and Montenegro did the economy continue to contract – albeit less dramatically than in 2009 when the crisis peaked (Table I).[7] The pattern of recent economic development in the CESEE countries closely matches the global trends described above: a major contraction of GDP in 2009 followed by recovery in 2010 (Figures 1a and 1b). However, nowhere will the growth predicted for the years to come be as high as before the crisis. In the CESEE region, Russia (and Ukraine even more so) was

[4] See IMF World Economic Outlook Update; IMF Global Financial Stability Report Market Update, January 2011. Controls of capital inflows were already introduced e.g. by Brazil and Thailand.

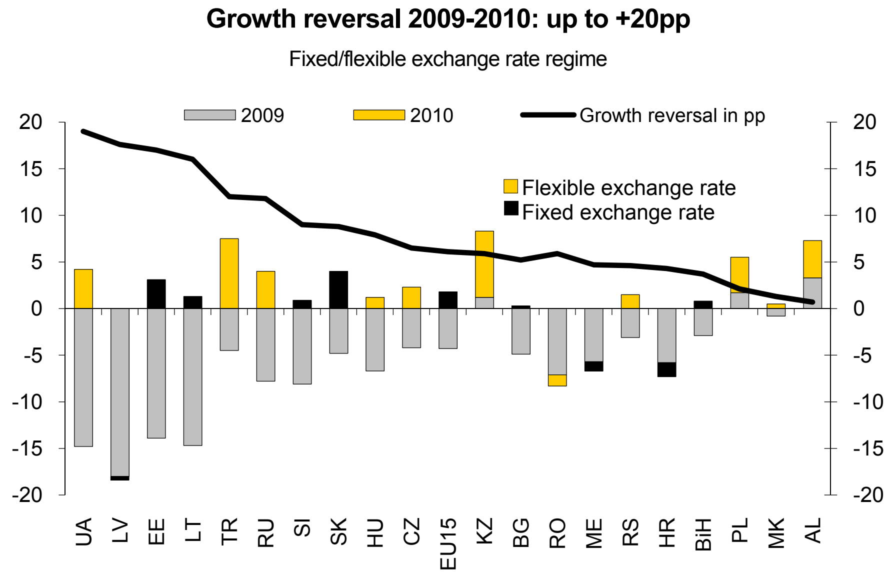
[5] Financial Times, 27 January 2011, p. 3.

[6] See EU Interim forecast, February 2011 (http://ec.europa.eu/economy_finance/articles/eu_economic_situation/2011-03-01-interim_forecast_en.htm)

[7] In 2009, only 3 countries in the CESEE region - Poland, Albania and Kazakhstan - could avoid a decline of GDP.

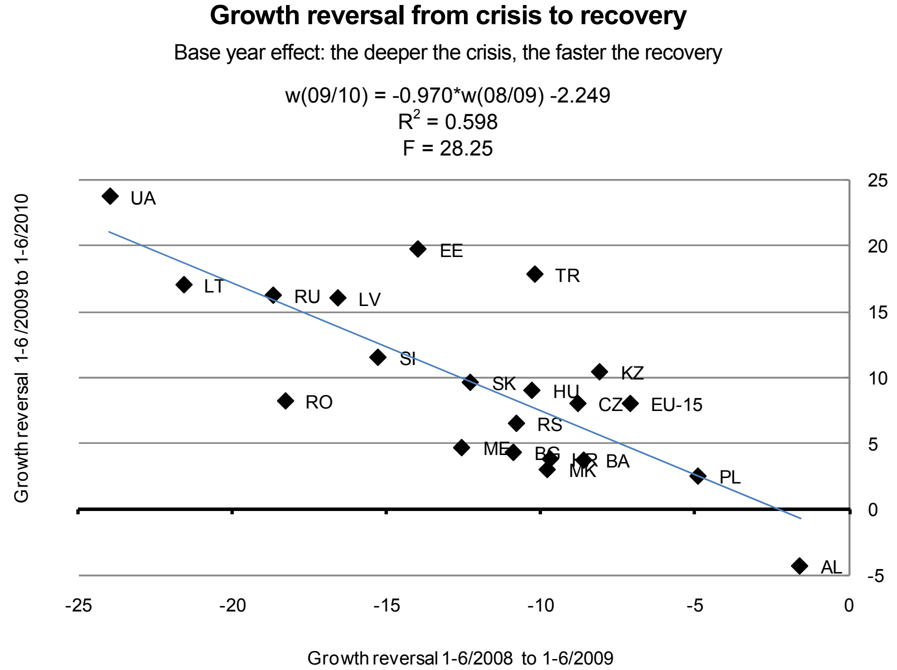
hit particularly hard, whereas the depth of the crisis in 2009, at least on average, was roughly similar in both the new member states (NMS) and the Southeast European region, as well as in Turkey (Figure 1b). Moreover, the expected post-crisis economic growth will also take on a similar shape in different regions of the world.

Figure 2a



Source: wiiw Database incorporating national and Eurostat statistics.

Figure 2b



Source: National statistics, Eurostat.

Differences in the impact of the crisis were especially visible at the country level (Latvia and Ukraine at one negative extreme in 2009, with Albania, Poland and Kazakhstan on the positive side). Patterns of recovery in 2010 were more evenly distributed: Turkey and Kazakhstan reported record GDP growth rates of more than 7%, while the rest of the region grew at a moderate pace (Slovakia, Albania, Russia and Ukraine each by about 4%). The median growth rate for the whole region was close to 2%. Comparing patterns of the crisis with those of recovery on a country-by-country basis suggests that the 'base year' effect played a significant role: those countries that were hit hardest during the 2008-2009 crisis tended to enjoy a more robust recovery during 2009-2010. Both the so-called 'growth reversal' and 'base year' effects are illustrated in Figures 2a and 2b. Figure 2a ranks the CESEE countries according to the extent of 'growth reversal' (measured as differences in their GDP growth rates between 2009 and 2010). 'Growth reversal' ranged between 20 percentage points (in Ukraine) and almost nil in Albania (Figure 2a).

Among the various factors which could possibly explain the depth of the crisis and the intensity of recovery (such as the share of industry and exports in GDP, various characteristics of the banking system, FDI penetration, institutional factors, most of which were not very conclusive during the crisis period owing to statistical and other problems),[8] the exchange rate regime seems to have played a more prominent role. Transition countries with a flexible exchange rate regime tended to master the crisis better than those with a more rigid regime, be it countries with a peg or currency board or those such as Slovenia already using the euro.[9] Out of 20 transition countries presented in Figure 2a, about half have flexible exchange rates. The question thus arises whether the exchange rate regime also played a role in the recovery phase. Ukraine, Turkey and Russia – all three with flexible exchange rates – enjoyed a fairly strong recovery over the period 2009-2010. Poland and Albania, which also have flexible exchange rates, did not suffer any drop in their GDP in 2009 and continued to grow in 2010 as well. On the other hand, the Baltic States with their currency boards and fixed exchange rates (as well as Slovenia with the euro) not only suffered extensively during the crisis (possibly the key reason for their pronounced 'growth reversal'), but their recovery to date has been far from impressive. This contrasts sharply with Slovakia, which first had a fixed exchange rate followed by adoption of the Euro in January 2009; in that country the economic rebound has been strong – largely thanks to improved productivity and labour market 'flexibility'.

Diverse ways out of the crisis – none of them painless

Of course, neither the exchange rate regime nor, for that matter, any other economic factor in isolation can explain the severity of the crisis or the strength of the ongoing recovery. Many other, fre-

8 See, for instance, EBRD Transition Report 2009, especially Chapter 2 'Understanding the crisis in the transition region', pp. 41-59 where econometric analysis is applied to reveal factors which explain cumulative output declines. wiiw also investigated some of the crisis factors in November 2009 (see presentation at the press conference on 6 November 2009 - http://www.wiiw.ac.at/e/upcoming_events.html). Later on EBRD Transition Report 2010 (Chapter 2, From crisis to recovery, pp. 29-42) investigated some of the driving forces of recovery, in particular the roles of exports and credit growth.

9 Flexible exchange rates proved to be shock absorbers' - see wiiw-Bruegel, 'Whither growth in central and eastern Europe? Policy lessons for an integrated Europe', 2010, Vienna-Brussels, p 55. The previous wiiw Forecast Report provided some evidence for a positive relationship between flexible exchange rate and growth –see Astrov, V., Holzner, M., Laski, K., Podkaminer, L., et al., op cit., p. 55.

quently interacting forces have been at play, not all of which are clearly evident or easily captured by the analysis. An obvious and robust factor positively correlating with the intensity of the recent 'growth reversal' is the 'base year' effect mentioned above. Figure 2b shows the transition countries according to the size of their 'growth reversals' at the peak of the crisis (negative 'growth reversal' between the first half of 2008 and the first half of 2009 (horizontal axis)) and in the recovery period (positive 'growth reversal' between the first half of 2009 and the first half of 2010 (vertical axis)). Many countries lie on (or are very close to) the regression line, the statistical relationship between both 'growth reversals' is highly significant and the role of the 'base year' effect in the strength of the recovery seems to be clearly established.[10]

The role of the 'base year' effect becomes even more evident, if we look at the trends displayed by other variables during the crisis-recovery cycle. In a nutshell, the crisis in the CESEE countries started in September 2008 with an abrupt drop in exports and capital inflows after the collapse of Lehman Brothers. This was followed, after a time lag of about two months, by a severe contraction of industry and construction. Largely external to the CESEE region, these demand and supply shocks were accompanied by a sudden stop in credit financing as uncertainties in the (primarily foreign-dominated) banking sector spread to the local real economy. The authorities in the USA and Western Europe, as well as a few CESEE countries, initiated various rescue measures in the financial sector and introduced demand stimulation packages in the course of 2008-2009. These measures differed in scope, intensity and detail, but in general, they contributed to widening fiscal deficits and rising public debt. Even in the CESEE countries, most of which adopted a more 'conservative' approach to demand-stimulation policies, the state of public finances deteriorated, not least on account of the recession-related shortfall in revenue (see below).[11]

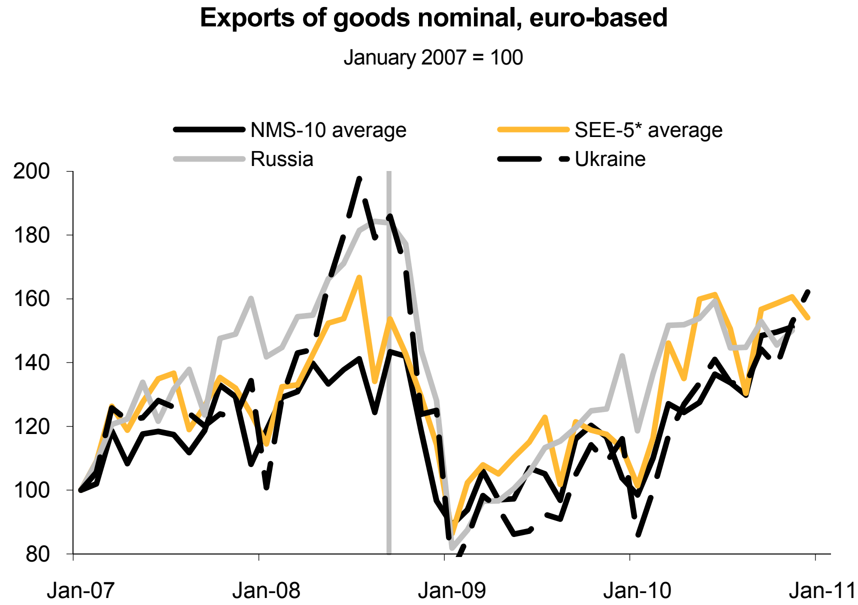
Figure 3a shows trends in CESEE exports immediately before and after the crisis. The abrupt drop in export values across the board after September 2008 was steepest in Russia and Ukraine. In both countries (as well as in Kazakhstan) negative demand effects were compounded by adverse price developments.[12] The exports bottomed out in January 2009 and, by the end of 2010, they had more than recovered in nominal euro terms compared to the pre-crisis period. On average, exports in both

10 More than other possible explanatory factors such as growth of exports, credits, etc. which were tested as well – see below.

11 Meanwhile, literature on the diverse policy responses to the crisis is extensive (e.g. 'Trade and Economic Effects of Responses to the Economic Crisis', OECD Trade Policy Studies, Paris, 2010; wiiw-Bruegel, op. cit, etc.). In several CESEE countries (Latvia, Hungary, Poland, Romania, Bosnia and Herzegovina, Serbia and Ukraine), the financial crises of late 2008 (which in many cases aggravated the already existing external and internal disequilibria) had to be resolved with the assistance of the IMF and/or the EU, EBRD and EIB. Private international banks were taken on board in CESEE stabilization efforts, inter alia within the framework of the so-called 'Vienna Initiative' - see Nitsche, W., The Vienna Initiative/European Bank Coordination Initiative: Assessment and Outlook. Austrian Federal Ministry of Finance, Working Paper 4/2010.

12 In both countries the predominant exports were commodities where the negative price effects were larger than the quantity effects (the latter prevailed in manufacturing) – see Haddad, M., Harrison, A., Hausman, C., (2010), 'Decomposing the great trade collapse: products, prices and quantities in the 2008-2009 crisis'. NBER Working Paper Series, No. 16253, August. See also EBRD Transition Report 2010, op. cit., Chapter 2, p. 31, as well as the special section on export doom and boom in Box 1.

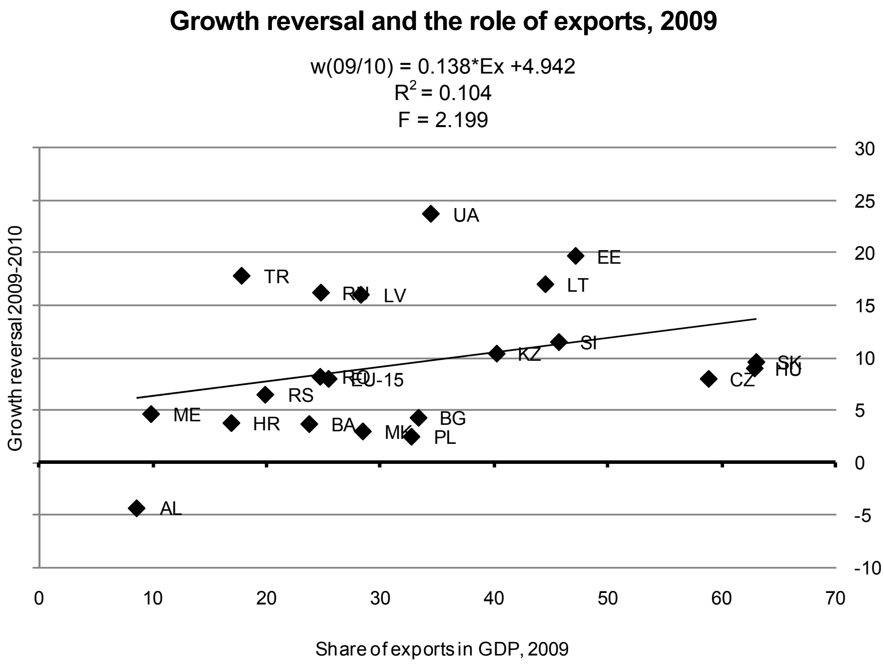
Figure 3a



SEE-5: AL, BA; HR, MK, RS

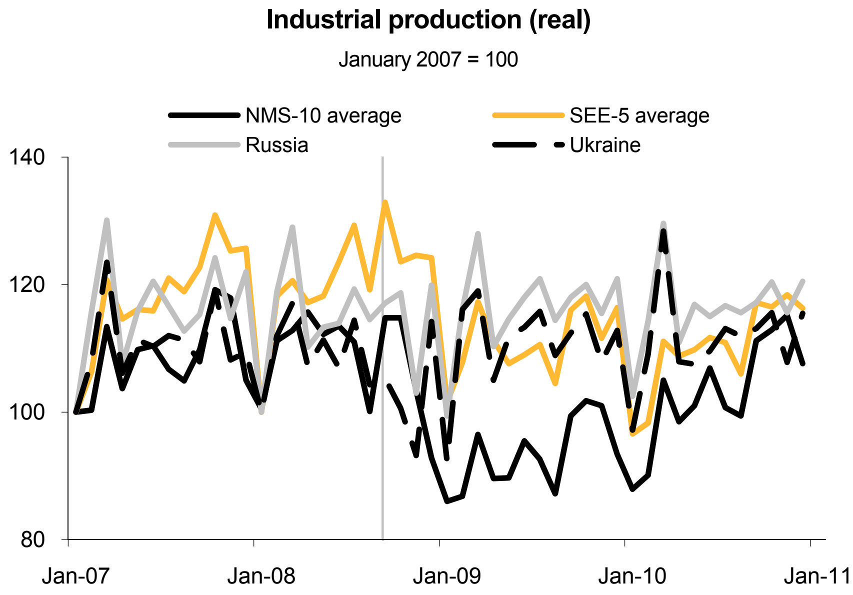
Source: wiiw Monthly Database incorporating national and Eurostat statistics.

Figure 3b



Source: wiiw Annual Database incorporating national and Eurostat statistics.

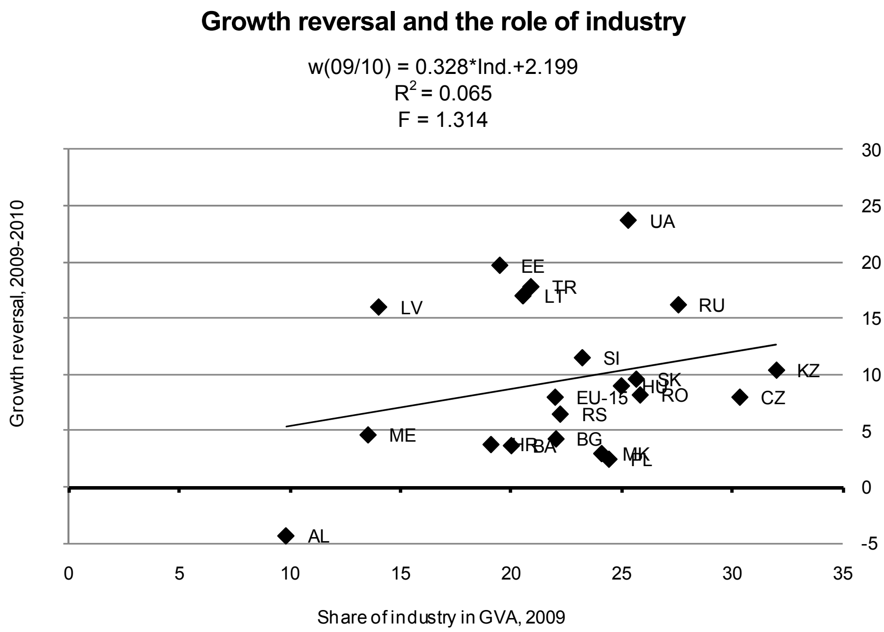
Figure 4a



SEE-5: AL, BA; HR, MK, RS

Source: wiiw Monthly Database incorporating national and Eurostat statistics.

Figure 4b



Source: wiiw Annual Database incorporating national and Eurostat statistics.

the NMS and the Southeast European region appear to have recovered more sharply than they grew before the crisis. On close inspection, the data (see also the respective country tables) reveal that only Hungary, Lithuania and Slovenia have yet to attain their pre-crisis (2007) export levels (the Czech Republic and Poland almost re-attained that level in 2010).[13] Exports thus played a major role in the recovery of the CESEE countries and in that sense, they did indeed 'prevail over austerity': an issue raised in the previous wiiw forecast from July 2010.[14]

In contrast to the swift recovery of exports, the trends in (real) industrial output have been more or less flat (Figure 4a). Basically, industrial output only started picking up to any marked degree in the course of 2010 in the NMS (particularly in Estonia and Slovakia), and in parts of the Southeast European region, especially in Bosnia and Herzegovina and Macedonia. In Croatia and Montenegro – the only two countries in the CESEE region – industry is still deeply depressed compared to the pre-crisis period.[15] Last but not least, in both Russia and Ukraine the level of industrial output in 2010 was still below the pre-crisis (2007) level – in marked contrast to Turkey and especially Kazakhstan.

Despite the weaker GDP growth and performance differences between individual countries mentioned above, industry in the CESEE countries bounced back markedly in 2010. This rebound stands in sharp contrast to the situation in the construction sector, which even in 2010 continued to fall quite dramatically in most CESEE countries. The construction industry is extremely seasonal in character; the output data on a monthly basis are only available for selected countries. Figure 5 illustrates highly volatile trends in construction output for selected country aggregates and Russia. On average, output fluctuation was particularly high in the NMS (excluding the Baltic States), yet both the bottom (January 2010) and the peak (November/December 2010) were lower than the year before. An analogous pattern, albeit smaller in amplitude, is visible in both Southeast Europe (only Croatia and Macedonia provide data on a monthly basis, the former reports huge drop in construction in 2010) and Russia (Figure 5). Data on the development of construction output on an annual basis are available for all CESEE countries (see the respective Country Tables). The pre-crisis construction bubble burst by 2009 at the latest (in Hungary it had already burst in 2006, and in Estonia and Latvia in 2008). In a number of CESEE countries, output in the construction sector continued to contract at double-digit rates in 2010 (for example, in Bulgaria, Estonia, Latvia, Lithuania, Romania, Slovenia, Croatia, Montenegro, Albania and Serbia). Poland is the only country that managed to avoid a decline in the construction sector throughout the crisis period. Positive growth in the construction industry in 2010 was also recorded in Macedonia, Turkey and Kazakhstan.

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13 A more detailed assessment of export performance both before and after the crisis is given in the Box 1 below.

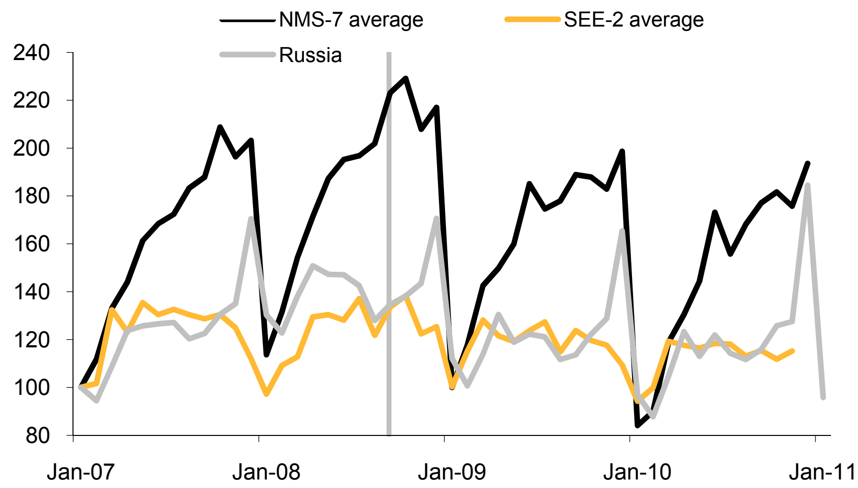
14 However, a simple OLS regression between the growth reversal and the share of exports in GDP does not yield conclusive results – see Figure 3b. For more on the recovery of exports see also EBRD Transition Report 2010, Chapter 2, p. 31.

15 In general, the underdeveloped industrial export sector is one of the constraints upon sustainable recovery in the South-east European region – see also Anastasakis, O., Bastian, J., Watson, M. (eds), 'From Crisis to Recovery. Sustainable Growth in South East Europe', South East European Studies at Oxford, 2011. At the same time, the relationship between the share of industry in gross value added (GVA) and the growth reversal is not statistically significant – see Figure 4b.

Figure 5

Construction output, real

January 2007 = 100



NMS-7 (CZ, HU, PL, SK, SI, BG, RO) NACE Rev. 2;
Russia, SEE-2 (HR, MK) NACE Rev. 1., HR from 2007 NACE Rev. 2

Source: wiiw Monthly Database incorporating national and Eurostat statistics.

Disappointing developments in the construction industry – even when recovering from the crisis – signal a fragility of current recovery as well as a generally cautious attitude on the part of both households and firms towards the strength and sustainability of the current recovery. The growth of credits to the non-financial private sector remains very slow; government spending on construction and investments is generally restricted (see below). The only expanding source of financing in construction and investment, at least as far as the NMS are concerned, has been transfers from the EU budget.

Indeed, the highly uncertain prospects for both the construction industry and fixed investments (of which construction outlays usually form a major part)[16] represent one of the key downward risks to our present regional economic forecast.

[16] Construction outlays usually account for more than half of gross fixed capital formation in the CEESE – see wiiw Handbook of Statistics 2010, Chapter II.6, pp. 210-228.

Box 1

Doom and boom in CESEE exports to the eurozone[17]

Decomposing the export slump and recovery for the CESEE regions

For the majority of CESEE countries, foreign trade was one of the main conduits for the spread of the crisis during 2008-2009. This was due to the countries' high degree of openness, with export-to-GDP ratios close to 70% in countries such as Slovakia, the Czech Republic or Hungary.[18] The trade channel also played a major role in the current recovery that began around mid-2009. In this section, we focus on trade linkages between the CESEE countries and the eurozone, the latter being a major trading partner for all the countries in the region.[19] We decompose the decline in export values over the crisis period and the subsequent rebound of exports into the 'intensive' and 'extensive' margins of trade.[20] The extensive margin refers to products that are no longer exported('exiting products') and new products entering the export basket of a country ('entering products'). The intensive margin of trade is measured as the change in the export value of a specific good. The intensive margin is decomposed into quantity and price effects.[21] This reflects the fact that a decline in the value of exports can be due to changes in the quantity or price of a good exported. If quantities decline and that decline is accompanied by decreasing prices, this can be interpreted as evidence of the decline in trade being due to a negative demand shock. Likewise, the quantities and prices should move in the same direction during the recovery phase, were the expansion of trade driven by strengthening external demand. By way of contrast, if quantities fall but prices rise, this would point to supply-side frictions such as a lack of finance for trade or the introduction of trade barriers.

We further decompose the 'net price' effect into: (i) a price effect of exports denominated in the domestic currency of the respective CESEE countries; and (ii) an exchange rate effect. The entire analysis considers changes in the value of CESEE country exports to the eurozone by comparing export values in the first half of 2008 to the export values in the first half of 2009 and so reveal the changes (along the different margins and effects) during the 'crisis phase'. Likewise, export values of the first half of 2009 are compared to values of the first half of 2010 in order to reveal changes during the 'recovery period'.

17 This section was written by Roman Stöllinger, wiiw.

18 Exceptions are Albania and Montenegro where the export of goods to GDP ratio is rather low – see Tables II and III above.

19 The share of exports destined for the eurozone range from 83% (Albania) to 22% (Latvia). For most countries the share is between one half and two thirds of total exports (according to UN Comtrade data, 2009 figures).

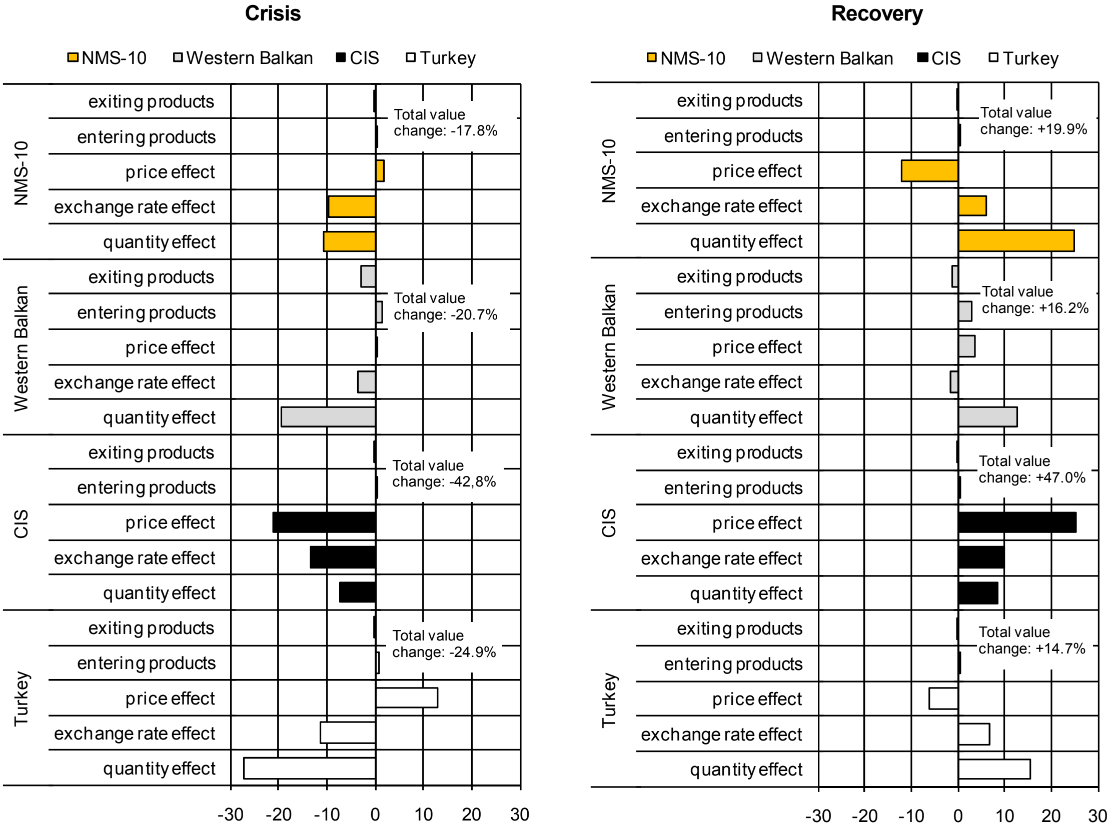
20 The use of COMEXT data implies that we have to rely on mirror statistics in order to cover the exports of all CESEE countries and the imports of the euro area from the CESEE countries are used as exports from the CESEE countries to the euro area.

21 The exercise is carried out at the level of 6-digit common nomenclature (CN6) products. The decomposition closely follows the methodology used by Haddad, M., Harrison, A., Hausman, C. (2010), op. cit. However, we extend the analysis in two ways. First, we further split the net price effect into an exchange rate effect and a national currency price effect which captures price changes of exports denominated in national currency (instead of euro). Secondly, we analyse the margin adjustments of exports for both the crisis period and the recovery period.

Box 1 (continued)

Figure 1

Decomposition of changes in export values of CESEE regions' exports to the eurozone



Source: Eurostat Comext, wiiw-calculations. Unobserved products not shown (i.e. products with missing or unreliable value or quantity data). NMS-10: Czech Republic, Hungary, Poland, Slovenia, Slovakia, Romania, Bulgaria, Estonia, Latvia, Lithuania; Western Balkan: Albania, Bosnia and Herzegovina, Croatia, Macedonia, Montenegro, Serbia; CIS: Russia, Ukraine and Kazakhstan. Quantity, price and exchange rate effects together build the intensive margin; entering and exiting products are the extensive margin. The crisis period compares the 1st half of 2008 with the 1st half of 2009; the recovery period compares the 1st half of 2009 with the 1st half of 2010.

The extensive margin did not really matter that much

The first observation is that for all CESEEs, the large drop in exports and the subsequent rebound were mainly due to changes along the intensive margin, with the extensive margin playing only a minor role. Figure 1 shows this trend for the NMS-10, the Western Balkan countries, three CIS countries and Turkey. Product exit and entry is somewhat higher for the Balkan countries; this could signal that in the small Balkan economies a relatively large number of products became uncompetitive and hence were no longer exported to the eurozone. Whole product lines would, of course, also be lost, if high trade barriers were set up. More likely, however, this is a statistical effect attributable to

Box 1 (continued)

the poor quality of trade data for those countries.[22] As for the extensive margin, it is also noteworthy that, despite its minor contribution, the net effect of product exit and product entry was negative during the crisis period and positive throughout the recovery period for all regions shown in Figure 1; the one exception is Turkey which is an outlier in this respect.

The export slump in the CESEE region was purely an external demand shock

The overwhelming adjustment of export values for all CESEE regions in both periods occurred along the intensive margin. As shown in Figure 1, all regions experienced a huge decline in quantities exported during the crisis. In the case of Turkey and the Western Balkan countries, export quantities declined by 27% and 20% respectively; this means that the quantity effect basically explains the entire drop in their exports. As for the NMS-10 the 11% decline in quantities exported is compounded by a negative net price effect of 8.1% (the sum of the exchange rate and price effects); in other words, their euro-denominated export prices declined. Driven by relatively strong devaluations in Poland, Hungary and Romania, which together account for more than 50% of NMS-10 exports to the euro area, exchange rates also moved substantially. To the extent that NMS-10 exporters (in countries with flexible exchange rate) seized on this beneficial exchange rate development to lower their export prices in euros, this contributed to the negative net price effect; on the other hand, however, it also bolstered their competitiveness.[23]

The commodity-exporting CIS countries find themselves in a completely different international trade setting since their export prices are dictated solely by world markets. Furthermore, commodity prices are much more volatile than those for industrial goods. Owing to the lack of diversification in the CIS economies (92% of Kazakh exports to the eurozone and 82% of Russian exports to the same markets comprise energy and metals), the high volatility of commodity prices translated directly into a major decline in export values during the crisis (and a subsequent rebound during the recovery phase).[24] As shown in Figure 1, CIS exports to the eurozone suffered from a huge net price effect of -34% during the crisis, accounting for more than two thirds of the overall drop in export values which was very severe (-43%).[25] The negative price effect resulted from the major drop in oil and other commodity prices at the onset of the crisis that affected export values that came on top of a devaluation against the euro during the crisis itself. The CIS countries thus found themselves in the unfavourable position of having their exports dwindle owing to a reduction in the volume of, and lower prices for, their export goods. Within the CESEE region, only Turkey experienced a slightly positive

22 The fact that in some of the Balkan countries ‘unobserved’ products, i.e. products for which no or only unreliable quantity data are available, contribute significantly more to the total change in value also speaks in favour of a statistical effect.

23 Note that exchange rate and price effects denominated in a national currency typically move in opposite directions. This is because, assuming that export goods are priced in euros, a devaluation of the domestic currency will – ceteris paribus (e.g. price reductions by the firm) - increase the value of exports denominated in the national currency. Obviously, for countries with a fixed exchange rate system against the euro, the exchange rate effect is nil.

24 The same is true for Montenegro that mainly exports metals.

25 The price effect in national currency is lower (-21%) because of the devaluation.

Box 1 (continued)

net price effect of about 1.7%, despite the Turkish lira suffering a devaluation of more than 10% over the period first half 2008 to first half of 2009. Most likely, this positive net price effect is at least partly the result of much higher inflation in Turkey compared to the eurozone.

In the ultimate analysis, the reason for the shifts in quantities and prices during the crisis and the related decline in trade values was mainly due to a decline in the quantities exported, compounded by negative price effects; this is in line with the interpretation of the trade crisis as a negative external demand shock. The absence of positive price effects suggests that supply-side factors, such as new trade barriers or scarcity of trade finance, did not play a major role (if any) in terms of the CESEE countries' exports to the eurozone.

What goes down must come up: export revival during recovery

A striking feature of export developments in the CESEE countries is that the rebound of exports in the recovery phase was basically the mirror image of developments in the previous year when exports were hit by the crisis. By mid-2010 exports from the NMS-10 and the CIS to the eurozone had more or less fully recovered from the crisis in value terms. Turkey and the Western Balkan countries suffered the same reversals in terms of the individual effects, although in mid-2010 export recovery along the quantity margin in those countries was still very much an ongoing process. The symmetry between trade margin changes in 2008/2009 and 2009/2010 also confirms that the speed of export recovery was strongly influenced by the base year effect. That means that in the recovery period those exports that had suffered a more severe setback also experienced a stronger rebound. The symmetry between export value decline during the crisis and export value growth during the recovery period is nicely maintained since the initial drop was almost exclusively demand-triggered without many additional structural or supply-side inherent barriers (such tariffs and non-tariff barriers and lack of trade finance). That could have hampered or further delayed trade recovery, once external demand had begun to grow once more. This does not rule out concern in countries such as Turkey over losing export market shares in the eurozone. Turkey's loss of market share, however, cannot be attributed to the crisis; it is due to the fact that Turkey faces stiff competition in labour-intensive export industries (above all in the textile sector) from Asian countries where wage levels are even lower.[26]

Domestic demand still weak

In contrast to the robust export upswing during 2010, the performance of key components in domestic demand – viz. the performance of both household and government consumption, and especially that of gross fixed investments – was weak even during the recovery phase (Table 1). According to preliminary data for 2010, final household consumption continued to decline in most CESEE countries, albeit less steeply than in 2009. Only Turkey and Kazakhstan (and less strongly so Poland, Albania and Ukraine) recorded noticeable consumption growth. Developments in terms of gross

[26] See for example Dinççağ, A. and Özlale, Ü. (2010), 'Export losses in the EU market', TEPAV policy note July.

fixed capital formation were even more disappointing. 2010 was yet another year of investment decline throughout the region – for a number of countries, it was the third such year in a row. With a massive rebound in fixed investments in 2010 (+24%), Turkey stands out yet again as a star performer in this respect. A reduction of fixed investments more or less across the board is obviously associated with the drop in construction activities mentioned above.

Table 1

Consumption and investment

real change in % against preceding year

	Household final consumption						Gross fixed capital formation					
	2008	2009	2010 1)	2011	2012	2013	2008	2009	2010 1)	2011	2012	2013
					Forecast						Forecast	
Bulgaria	3.4	-3.5	-6	3	3	3	21.9	-29.0	-8	9	8	8
Czech Republic	3.6	-0.3	1	1	2.5	3	-1.5	-7.9	-1	2	4	6
Estonia	-5.5	-18.8	-1.3	0.5	1	1.5	-15.0	-32.9	-8	7	8	10
Hungary	0.5	-8.1	-2	0.5	1.5	2.5	3.2	-9.3	-3	5	7	8
Latvia	-5.3	-24.1	-1.5	1	2.2	2.2	-13.5	-37.3	-20	8	8	9
Lithuania	3.7	-17.7	-3.4	1.5	2.5	3	-5.2	-40.0	-5	7	8	8.5
Poland	5.7	2.1	3.2	3.8	4.5	4.5	9.6	-1.1	-2.0	4	6	7
Romania	9.0	-10.5	-2	2	4	2.5	15.6	-25.3	-15	4	7	6
Slovakia	6.1	0.3	0	2	3	5	1.0	-19.9	1	5	8	8
Slovenia	2.9	-0.5	0.5	1	1.5	2	8.5	-21.6	-6.7	2	3	5
NMS-10	**4.9**	**-3.3**	**0.4**	**2.4**	**3.5**	**3.5**	**7.6**	**-12.9**	**-4.9**	**4.3**	**6.2**	**7.0**
EU-15	0.4	-1.5	0.8	1.1	1.4	.	-1.5	-12.0	-0.3	2.5	3.9	.
EU-27	0.7	-1.6	0.7	1.2	1.6	.	-0.8	-12.1	-0.6	2.8	4.2	.
Croatia	0.8	-8.5	-1.5	0.5	2	3	8.2	-11.8	-12	2	5	5
Macedonia	7.4	-3.1	2.5	2	3	3	5.4	-2.0	0	3	4	4
Montenegro 2)	7	-4	0	2	2	3	8	-6	-2	2	2	5
Turkey	-0.3	-2.3	6.5	3.7	3.0	2.8	-6.2	-19.2	23.9	14.9	10.4	10.0
Candidate countries	**0.0**	**-2.7**	**5.9**	**3.4**	**2.9**	**2.8**	**-4.3**	**-10.9**	**2.6**	**13.5**	**9.8**	**9.4**
Albania	6.7	3.0	3.0	5	7	9	9.5	5.0	-7	1	5	12
Bosnia and Herzegovina	5.9	-4.2	0	1	2	2	10.9	-24.0	0	2	5	5
Serbia 2)	6	-2	2	2	2	2	8	-5	-4	3	4	4
Potential candidate countries	**6.1**	**-1.6**	**1.7**	**2.3**	**2.9**	**3.3**	**9.1**	**-6.1**	**-3.9**	**2.3**	**4.5**	**6.2**
Kazakhstan	6.3	-3	7	5	5	5	1.0	1.9	-9	10	7	7
Russia	10.6	-4.8	2.7	4.5	5	4.5	10.6	-14.4	3.5	6	8	7
Ukraine	13.1	-14.9	5.8	5	5.5	6	-1.2	-50.5	3.2	12	10	8

1) Preliminary and wiiw estimates. - 2) wiiw estimate.

Source: wiiw Database incorporating national and Eurostat statistics. Forecasts by wiiw and European Commission (Economic Forecast, Autumn 2010) for EU-15 and EU-27.

Box 2

Calculation of contributions to the GDP growth rate: an example

The contributions of individual demand components to GDP growth depend on their shares in GDP in the previous year and their growth rate in the current year. Thus, for example, in Russia in 2010 final consumption accounted for 66.2% of the country's GDP; gross fixed investment for 20.0%; exports of goods and services for 31.9%; imports for 18.6% (at previous year prices). The real GDP growth rate in 2011 is forecast at 4.1%. In 2011 consumption, investment, exports and imports are expected to increase by 4.1%, 6.0%, 5.0% and 10.0%, respectively. The (rounded) contribution of household consumption to the 4.1% GDP growth is 2.7 percentage points (2.7 = 0.041 x 66.2%); of investment 1.2 p.p. (1.2 = 0.06 x 20.0%); of exports 1.6 p.p. (1.6 = 0.05 x 31.9%); of imports (minus) 1.9 p.p. (1.9 = 0.10 x 18.6%). The trade balance (of goods and services) will contribute -0.3 p.p. (= 1.6 p.p. – 1.9 p.p.). The sum of the contributions of final consumption, investment and the trade balance is 3.6 p.p. Other items (change in stocks and statistical discrepancy) contributed another 0.4 p.p. In Russia (as in a number of other CESEE countries), changes of stocks have fluctuated wildly, especially during the recent crisis years.

Taking all three main components of GDP demand together, we obtain the following broad picture for the economic growth in the CESEE region as a whole over 2010: a generally modest economic recovery resulting by and large from a strong rebound in terms of exports, while domestic demand components – final consumption of households and especially fixed capital formation – continued to decline (with above mentioned exceptions – see Figure 6). Furthermore, in most CESEE countries the replenishment of stocks apparently contributed to mitigating the decline in investments and/or helped to foster GDP recovery in 2010. The exceptions to this growth pattern were Croatia and Macedonia (in terms of the positive effect of changes in inventories), as well as Poland, Turkey, Russia and Ukraine (in terms of the positive contribution of net exports to GDP growth). Needless to say, data on inventories for 2010 are very preliminary; they will likely be subject to correction (together with errors and omissions).

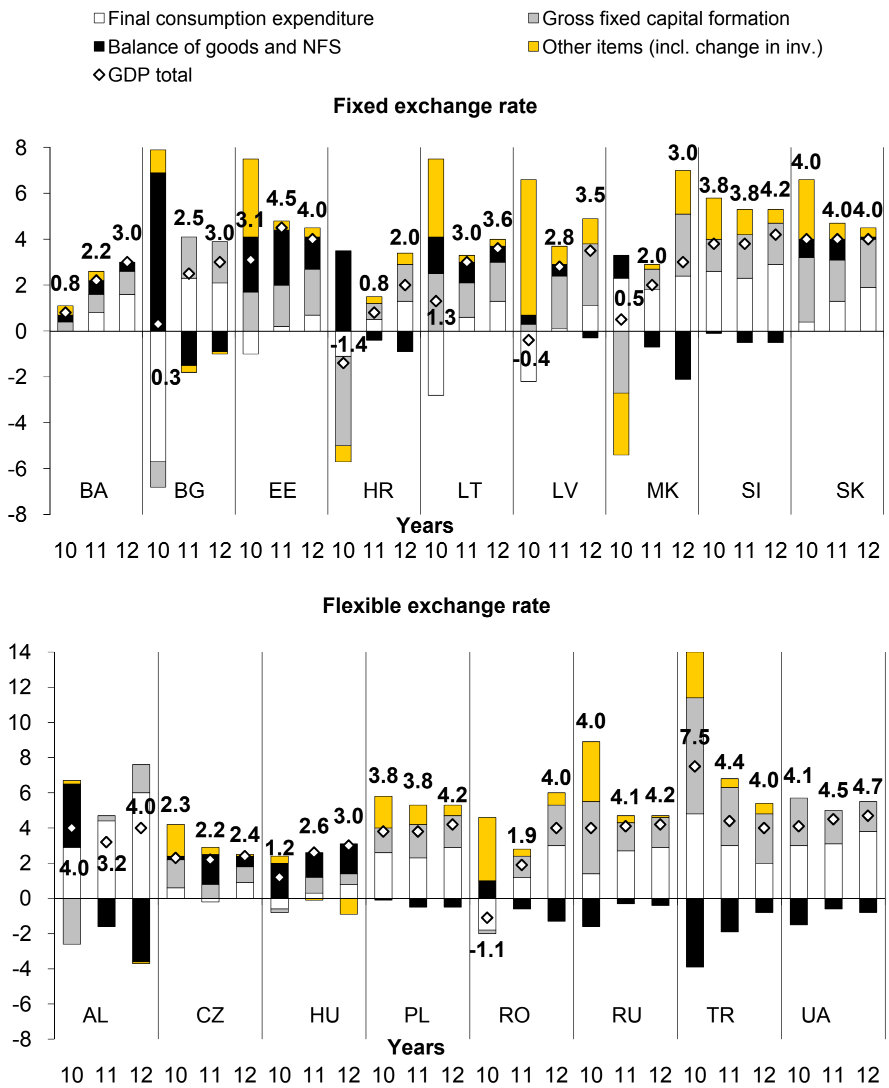
Looking ahead to the next 2-3 years, the general expectation for the CESEE region (assuming the above outlined baseline development scenario for the global economy, and especially that of Western Europe) is that there will be a gradual (yet unspectacular) strengthening of economic growth, in most cases rarely exceeding 4% p.a. The GDP growth will become more broadly based, with the former (2010) predominant role of external demand (net exports) weakening somewhat: slower export growth will be accompanied by the expansion of imports, resulting in a diminished or even negative contribution of net exports to GDP growth as of 2011. Simultaneously, both household consumption and, in particular, gross fixed investments over the period 2011-2013 will finally recover in all CESEE countries and contribute positively to GDP expansion.

The growth patterns forecast are shown in Figure 6 where the CESEE region is once again divided into two blocs according to the fixed/flexible exchange rate regimes. Unfortunately, neither group of countries apparently shows any distinct recovery pattern. Nowhere will GDP growth exceed 5% (N.B. this is far less than prior to the crisis and will also bear serious implications for labour markets – see below), with positive growth contributions coming largely from domestic demand (except Hungary). In a number of CESEE countries, largely irrespective of the exchange rate regime, the real contribution of net exports will tend to reduce future GDP growth (e.g. Bulgaria, Croatia, Macedonia and Slovenia as 'fixers' on the one hand, and Albania, Romania, Turkey and Ukraine as 'floaters' on the other). On closer inspection, those growth patterns suggest that the exchange rate regime is not expected to play any distinct role in the recovery period (in contrast to the previously mentioned crisis-mitigating properties of exchange rate flexibility). On the contrary, the importance of a strong and competitive export sector – which is generally lacking in Southeast Europe – comes to the fore once again.[27]

Figure 6

Contributions to GDP growth 2010-2012

in percentage points, adds up to GDP growth rate



Source: wiiw Database incorporating national and Eurostat statistics; wiiw own calculations.

[27] See wiiw-Breughel, op. cit and Anastasakis, Bastian and Watson, op cit.

The return of inflation? Not really – at least for the time being

Recent months have again witnessed appreciable increases in world market prices for energy, metals and foodstuffs; those same price increases have also spread to the CESEE countries. While representing a (mixed) 'blessing' for commodity exporters who benefit from rising export revenues (such as energy-producing Russia and Kazakhstan),[28] it has proven to be a 'curse' for importers (the majority of the CESEE countries). Similar to the situation before the crisis in 2008, the current increases in commodity prices cannot be attributed solely to rising demand (today even less so than before, since current global economic growth is still very subdued) and/or to 'loose' monetary policies. Rather, the explanation is probably to be found in speculative factors and supply bottlenecks (food supplies impaired by drought, floods in several major producer countries and surging oil prices in the wake of political turmoil in North Africa). In a number of countries, inflation has been also fuelled by the hikes in indirect taxes and administered prices.

Table 2

Consumer price inflation

change in % against preceding year

	2008	2009	2010 1)	2011	2012 Forecast	2013
Bulgaria	12.0	2.5	3.0	4	4	4
Czech Republic	6.3	0.6	1.2	2	2	2
Estonia	10.6	0.2	2.7	4	3.5	4.5
Hungary	6.0	4.0	4.7	3.9	3.5	3.5
Latvia	15.2	3.3	-1.2	3	3	3.5
Lithuania	11.1	4.2	1.2	3	2.5	2.5
Poland	4.2	4.0	2.7	3.5	2.5	2.5
Romania	7.9	5.6	6.1	5.5	4	4
Slovakia	3.9	0.9	0.7	2	3	3
Slovenia	5.5	0.9	2.1	2.8	2.5	2.5
Croatia	6.1	2.4	1.1	2.5	2	2.5
Macedonia	8.3	-0.8	1.7	3	3	3
Montenegro	7.4	3.4	0.6	3	3	3
Turkey	10.4	6.3	8.6	6	5.5	5.5
Albania	3.4	2.3	3.5	3	3	4
Bosnia and Herzegovina	7.5	-0.4	2.1	1	1	1
Serbia	13.5	8.6	6.8	7	6	6
Kazakhstan	17.1	7.3	7.4	7	6.5	6.5
Russia	14.1	11.8	7.1	7	5	5
Ukraine	25.2	15.9	9.4	10	8	7

1) Preliminary.

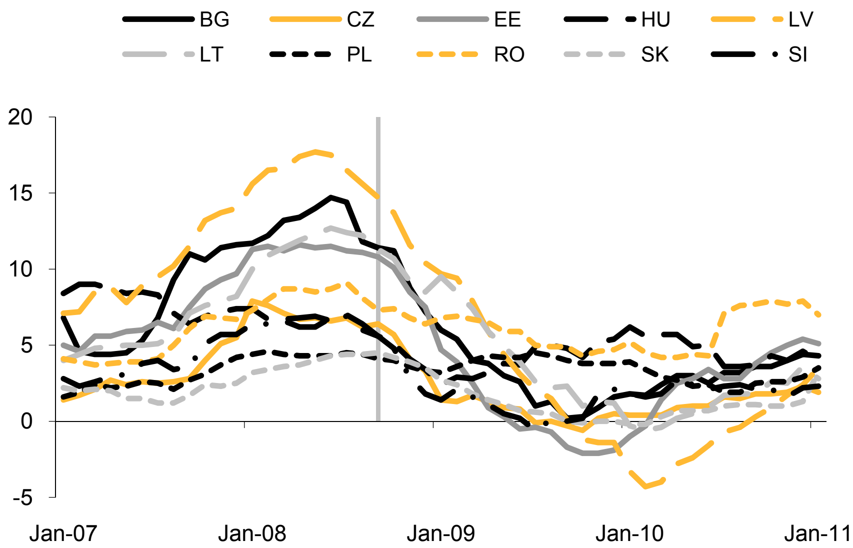
Source: wiiw Database incorporating national and Eurostat statistics. Forecasts by wiiw.

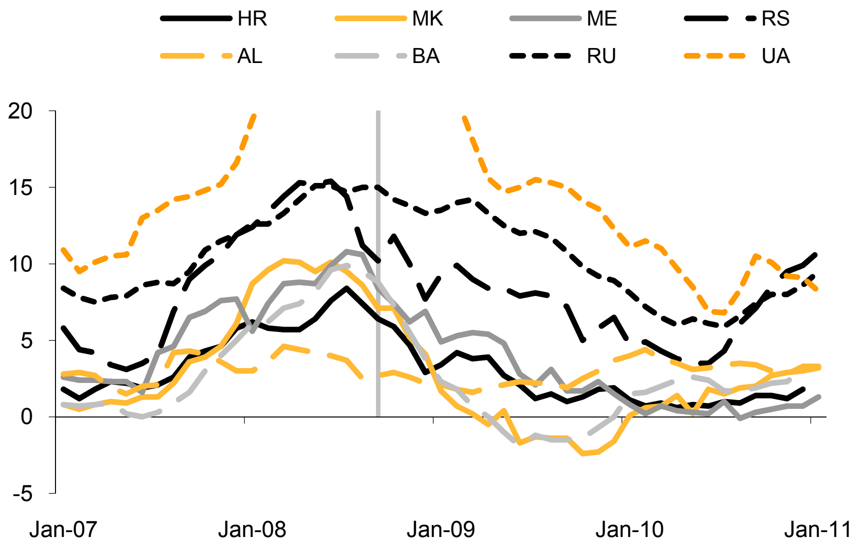
[28] Both countries struggle with the 'Dutch disease' syndrome and high commodity prices may discourage their efforts at economic modernization and diversification. The might possibly also hinder sustainable economic growth – see also Magud, N., Sosa, S. (2010), 'When and Why Worry About Real Exchange Rate Appreciation? The Missing Link between Dutch Disease and Growth'. IMF Working Paper, WP/10/271, December.

Figure 7a

Consumer prices

change in % against preceding year





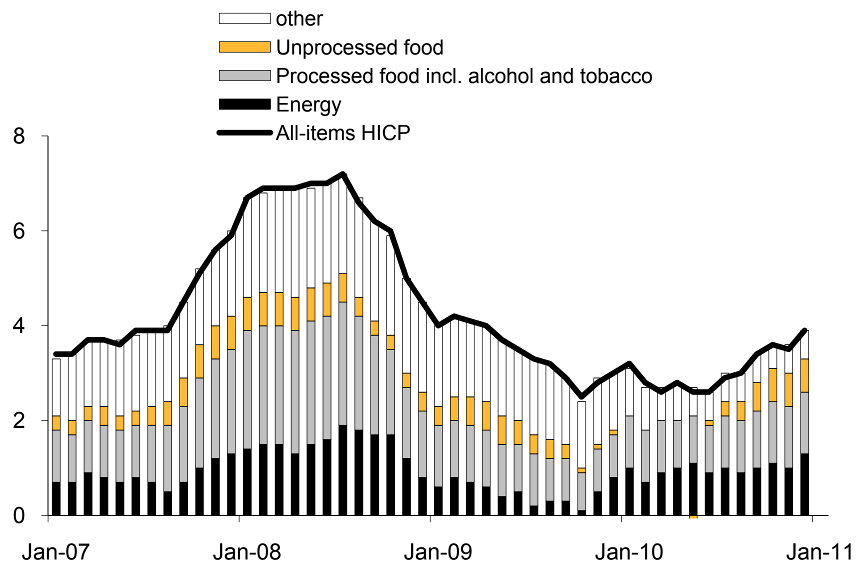
Source: wiiw Monthly Database incorporating national and Eurostat statistics.

Inflation did indeed rise in the course of 2010 (following on the deflationary tendencies observed towards the end of 2009 in a number of CESEE countries – see Figure 7a); however, in general it still poses no immediate threat. Even in countries with recent large CPI increases (such as Romania, Turkey, Serbia, Russia and Ukraine), core inflation remains fairly low (see Figure 7b for the key components of inflation in the NMS). However, a large gap yawns between the CPI (consumer price) and PPI (producer price) inflation – the latter as a rule being much higher and, moreover, rising faster than CPI (for example, in Bulgaria, Hungary, Croatia, Macedonia, Serbia, Russia and Ukraine). In this situation, especially if the current price spike is not as short-lived as expected, the risk arises of increased producer prices ultimately affecting CPI as well. Indeed, this is what wiiw expects in the near future. However, the forecasted inflation will probably not pose a major threat anywhere, and it is expected to lessen in the years to come (Table 2). Needles to say, the escalating turmoil in North Africa and the persistent rise in oil prices would eventually lead to higher inflation in the CESEE region as well.

Figure 7b

Contribution to inflation growth (based on HICP) in NMS-10

change in % against preceding year



Source: Eurostat statistics, wiiw own calculation.

Food price inflation is, of course, of prime concern to the authorities in poorer countries where the share of food items in the statistical consumer basket is higher and inflation hits larger parts of the population, with potential consequences for domestic political stability.[29] Therefore, it is hardly surprising that the authorities in some CESEE countries have been resorting to measures aimed at containing inflationary pressures. For instance, inflation in Ukraine (but also in Russia) would have probably been even higher, had those countries not imposed restrictions on grain exports following the poor harvest last summer. In Serbia, where unlike other countries inflation has been accompanied (and reinforced) by persistent currency depreciation, the national bank has repeatedly intervened in the foreign exchange market.

Monetary policy still generally lax, credit expansion sluggish[30]

At the same time, only a few countries have tightened their monetary policy in response to higher inflation.[31] Among the CESEE countries, only Poland, Hungary and Serbia (and more recently Rus-

[29] For instance in Ukraine food products account for 53% of the consumer basket.

[30] This section was drafted by Vasily Astrov, wiiw.

sia at end-February 2011) have raised policy interest rates. Most other countries have left them unchanged (sometimes at very low levels, such as in the Czech Republic), while Turkey and Macedonia have even reduced interest rates. In combination with rising inflation, this means that in most cases real interest rates have declined, signalling a reversal of the previous trend (Figure 8). In a number of countries – Estonia, Lithuania, Bulgaria, Czech Republic, Romania, Slovenia, Russia and Ukraine – the real policy rates of national banks have re-entered negative territory.

The general reluctance to tighten monetary policy appears justified given that nearly everywhere (with the possible exception of Turkey), inflation is driven largely by supply-side factors. So far there has been no need to 'cool' domestic demand, which is at best becoming merely tepid – and usually for reasons that are not credit-related. Figure 9 demonstrates that in most CESEE countries, the pace of credit expansion to the non-financial private sector (both companies and households) remains sluggish. The problem is that even though banks – contrary to the early stages of the crisis – are now generally awash with liquidity, the risks perceived are still high and credit terms are correspondingly tough.[32] Even in countries where the national banks' policy rates are comfortably low (e.g. the ECB 1% rate in Slovenia, Slovakia and Estonia or the 0.75% two-week repo rate in the Czech Republic), the interest rates on loans charged by banks are often prohibitively high. In some other cases, however, the demand for credit is also low: a trend that will continue as long as uncertainties about the future persist (especially, but not only, in Southeast Europe) and/or the construction bubble has not been accommodated.

Doubtless the credit dynamic observed is also shaped by the ever-rising share of non-performing loans (NPLs) in most CESEE countries (Figure 10). Only in Estonia, the Czech Republic, Poland, Slovakia, Lithuania, Turkey and Russia did the share of NPLs either stabilize or decline marginally throughout 2010, while Kazakhstan recorded a marked drop (albeit starting from a very high level of 30% at the end of 2009). The highest shares of NPLs (around, or close to, the 20% mark) are to be found in Kazakhstan, Latvia, Lithuania, Serbia and Montenegro. It is probably no coincidence that those are also the countries (as is Estonia) where the credit volume is still contracting – even in nominal terms. In the Baltic States and Kazakhstan, businesses and households remain highly indebted on account of earlier loans – the legacy of local real estate bubbles that burst even before Lehman Brothers collapsed. In Serbia, where the currency has been continuously depreciating against the euro and some 80% of the loans are indexed to the euro, the rising share of NPLs should come as no surprise either.[33] In other countries with widespread foreign currency-denomi-

[31] This applies first of all to CESEEs with flexible exchange rates, while CESEEs using the euro or on currency boards are deprived of monetary policy autonomy. The latter should also largely apply to countries with fixed exchange rate and free capital flows regimes – although Macedonia, which lowered its policy rate by half in the course of 2010 (from 8 to 4%), provides an example to the contrary.

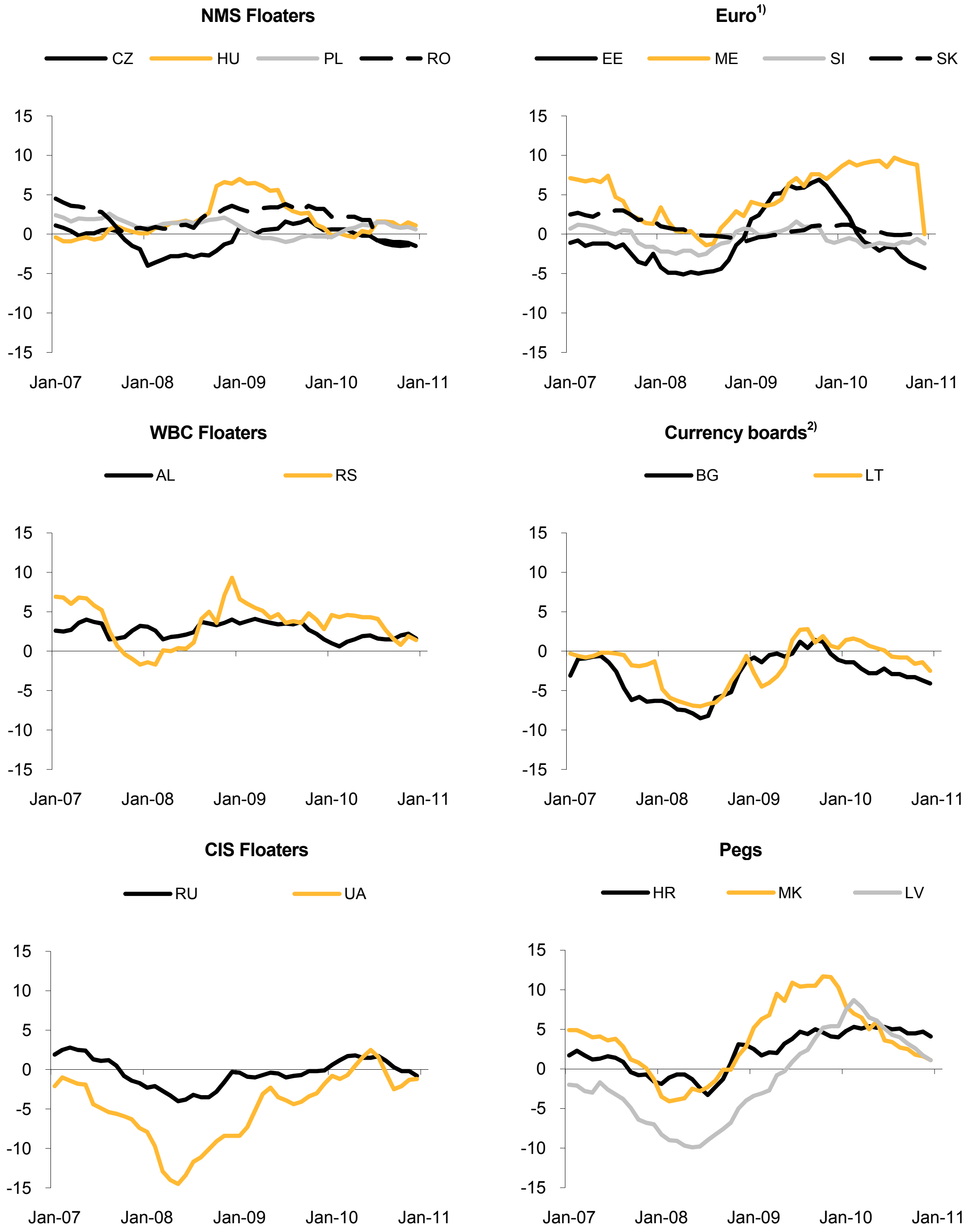
[32] In the case of firms, tough credit terms was a relatively important (compared to Western Europe) reason for non-applying for credit even prior to the crisis – see Brown, M., S. Ongena, A. Popov and P. Yesin, ‚Who needs credit and who gets credit in Eastern Europe?', in: Economic Policy, Vol. 26, Issue 65, pp. 93-130, January 2011. Anecdotal evidence suggests that the importance of this factor might have risen further after the crisis.

[33] For the same reason, the rapidly rising stock of loans in Serbia (in dinar terms) reflects to a large degree the valuation effect.

Figure 8

Real central bank policy rates

CPI-deflated, in % p.a.



1) For Estonia: One-month interbank lending rate (Talibor); for Montenegro: Weighted average interest rate of commercial banks. - 2) For Lithuania: One-month interbank lending rate (Vilibor); for Bulgaria: average interbank LEONIA rate of previous month.

Source: wiiw Monthly Database incorporating national and Eurostat statistics.

nated loans, the recent exchange rate developments have provided little relief to borrowers.[34] For example, in Ukraine, the exchange rate of the hryvnia vis-à-vis the US dollar has stabilized at some 60% below the pre-crisis level. In Hungary, the recent marked appreciation of the Swiss franc has put household borrowers in that currency under pressure. On the other hand, in the countries whose currencies have strengthened (such as the Czech Republic and Poland), the positive impact on credit quality has been limited by the relatively low incidence of foreign-currency loans.

In countries where the banking sector has low capital adequacy ratios, it is likely that bank re-capitalization will be needed in the near future to absorb the ever higher NPLs – on top of the capital injections already provided (by foreign-owned parent banks and, in some cases, by the national governments). State-sponsored bank re-capitalization programmes are reportedly in the pipeline in some countries, such as Slovenia, Ukraine and Kazakhstan.

Unlike most other countries, in Turkey and, to a lesser degree, in Poland, credit is expanding vigorously; in fact, it was never in decline – even during the acute phase of the crisis. In the case of Turkey, the current credit boom may well be pointing to the danger of a ‘boom-bust’ cycle looming on the horizon. Both countries, which currently offer a combination of appreciating currencies and nominal interest rates above those in the advanced economies, have recently become the main targets for capital inflows. Under such circumstances, the distinctly different measures recently adopted by the national banks of those two countries are likely to lead also to distinctly different consequences. The Turkish national bank cut its one-week repo rate from 7% to 6.25% in order to discourage excessive capital inflows. It has managed to weaken the lira somewhat: a step that should dampen imports and support the country‘s export sector.[35] By way of contrast, the recent – albeit modest – hike in interest rates in Poland (from 3.5% to 3.75%) may induce further inflows of speculative capital, with potentially damaging effects for the country’s external competitiveness. In Hungary, which has also raised its policy interest rate (from 5.25% to 6%), concerns over excessive capital inflows may be less relevant, given that the uncertainties surrounding the Orbán government’s future economic policy have led to the country‘s investment ratings being downgraded. Finally in Serbia, attracting additional capital inflows, which would strengthen the domestic currency and thus dampen inflationary pressures, has been one of the national bank’s main objectives. Between July and December 2010, the bank raised its main policy rate by 3.5 percentage points in toto to 11.5%.

Given the still (at best) fragile recovery of domestic demand in most CESEE countries, we do not expect a significant tightening of monetary policy in the near future. At the same time, the pace of credit expansion is likely to pick up somewhat, especially if the long-awaited recovery of fixed investments finally materializes, although the high shares of NPLs will in many countries continue to be a drag on credit growth.

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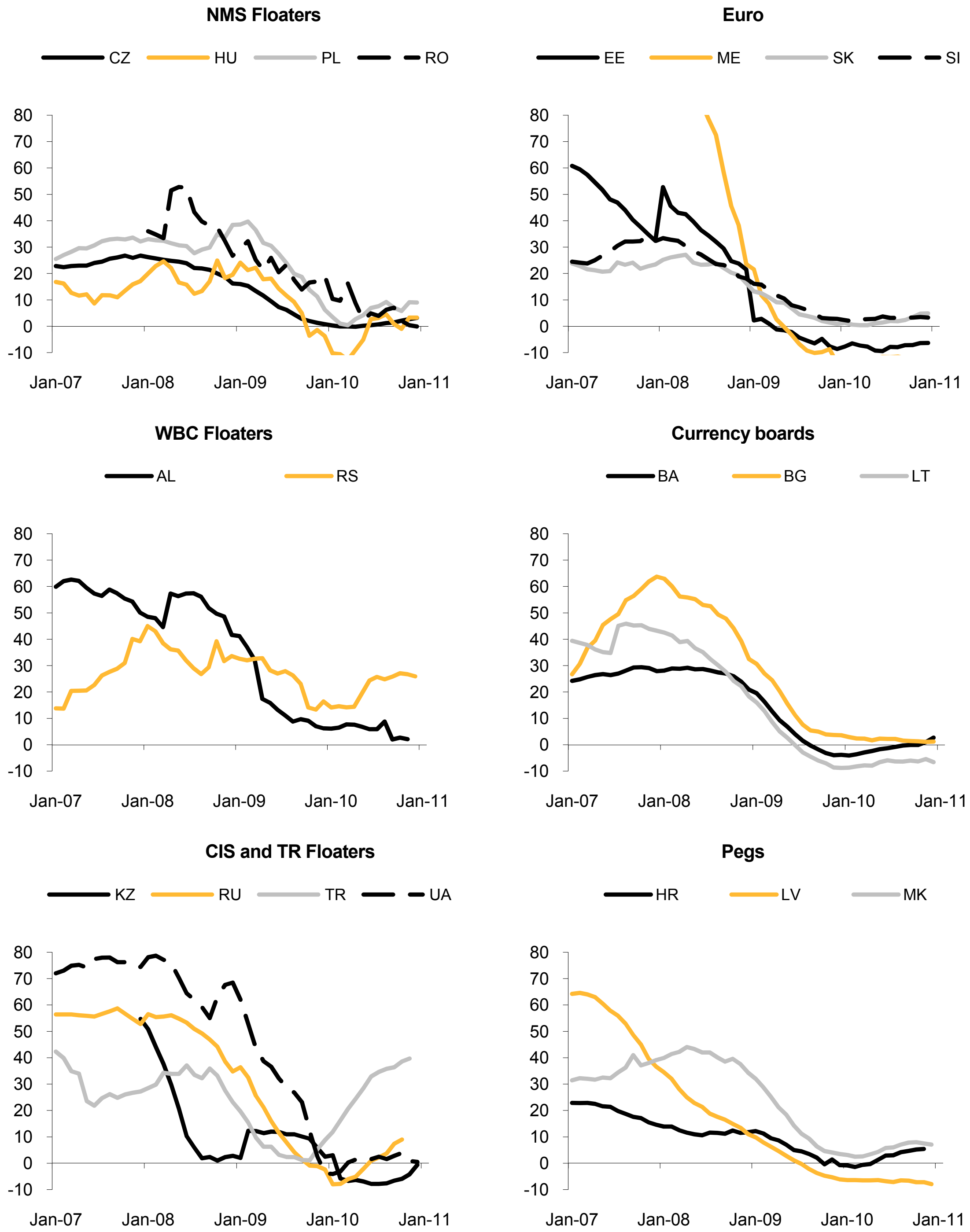
[34] Since the start of the crisis, borrowing in foreign currencies has been discouraged in a number of countries.

[35] In a parallel move, Turkey tightened the reserve requirements for banks in order to suppress the pace of domestic credit expansion.

Figure 9

Bank loans to non-financial private sector

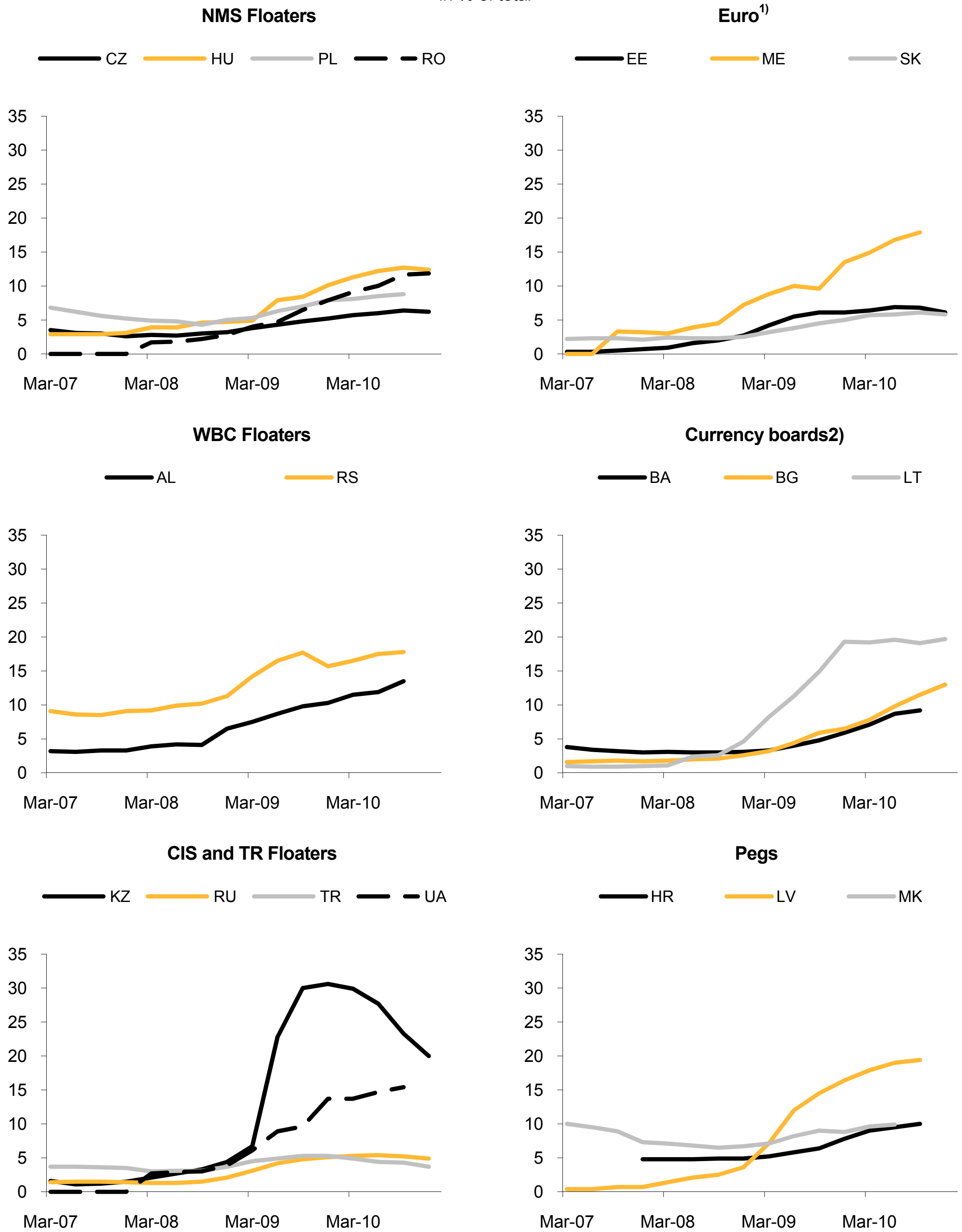
change in % against preceding year



Source: National Bank of respective country.

Figure 10

Non-performing loans
in % of total



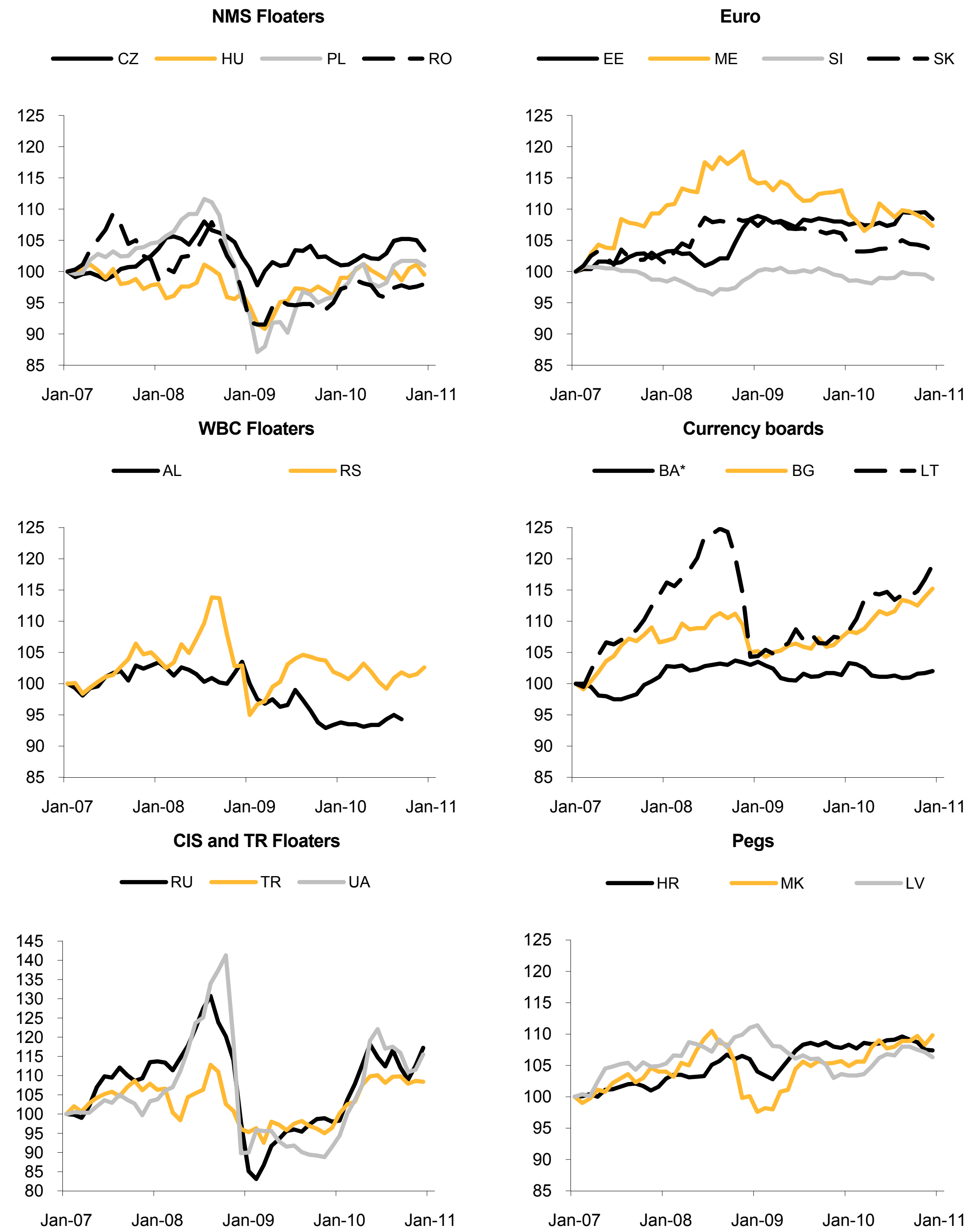
Note: Non-performing loans defined as credits more than 90 days overdue.
EE, LT: loans more than 60 days overdue. HU: loans for corporate sector only. UA: doubtful and loss credits. RU: referring to debt service, therefore not fully comparable with other countries.

Source: National Bank of respective country.

Figure 11

Real exchange rates[1)]

EUR per NCU, PPI-deflated, January 2007 = 100



1) Values above 100 indicate appreciation relative to January 2007.
*BA CPI-deflated.

Source: wiiw Monthly Database incorporating national and Eurostat statistics.

Currency appreciation and other challenges for competitiveness

One of the hotly discussed issues related to global imbalances, financial stability and competitiveness are the levels and movements of exchange rates. The recent economic upturn, together with a revival of (mostly short-term) capital flows (especially of foreign exchange credits and portfolio investments, less so foreign direct investments), have resulted in renewed (real) appreciation pressures on the CESEE currencies. Such pressures tend to be stronger in countries with flexible exchange rates (we have already pointed out the importance of an exchange rate regime in times of crisis). Figure 11 shows developments of real exchange rates in the CESEE region according to different exchange rate regimes, breaking down the countries in greater detail, beyond the simplified fixed/flexible scheme used above.[36]

The majority of CESEE currencies have indeed appreciated recently against euro. Real appreciation has been stronger in countries with flexible exchange rates ('floaters' in Figure 11) on two counts: either the local currencies appreciated in nominal terms (as in the Czech Republic, Poland and Russia) or domestic producer prices (PPI) rose more rapidly than in the eurozone (as in Hungary, Russia and Ukraine). By the end of 2010, the competitive 'gains' of earlier depreciations (late 2008-early 2009) had thus been largely eliminated. The real appreciation of 'fixers' (and the ensuing loss of competitiveness) has been most pronounced in Bulgaria and Lithuania, both of which employ currency boards (in the latter country, it nearly reversed the impact of painful 'internal devaluation' dating from late 2009) and do not enjoy the situation of being under the umbrella of the eurozone.[37]

Unit labour costs and responses to the crisis

Apart from exchange rates, unit labour costs (ULCs) have also been taking on importance in the ongoing discussion on global imbalances, competitiveness, macroeconomic policy coordination in the eurozone and strengthening EU economic governance in general.[38] In this section, we not only consider ULC developments in the CESEE region overall, but we analyse the individual components of labour cost competitiveness as well. We also address different responses to the crisis, productivity developments, the role of the exchange rate regime and compare developments before (2005-2008) and after the crisis.

Rapidly rising ULCs (and thus deteriorating cost competitiveness) have been a characteristic feature of most CESEE countries over the previous decade. Aggregate international ULCs (at the GDP level adjusted for the exchange rate – see Box 3 for definitions) have nearly doubled in most CESEE countries since 2000, irrespective of the exchange rate regime (Figure 12a). There have been two major exceptions to this trend: Poland (with a floating exchange rate) and Slovenia (with a tradition-

36 All nominal exchange rates (or euro resp. other fixed exchange rates) are deflated with the respective producer price indexes (note that PPI have been recently growing faster than CPI, and PPI in most CESEE countries – especially in those outside the eurozone – grew faster than PPI in the eurozone). For longer-term trends in real exchange rates and forecasts (both CPI and PPI deflated on annual basis) see Annex Indicators of Competitiveness.

37 After Slovenia and Slovakia and, largely unnoticed, Estonia joined the eurozone as its 17th member in January 2011.

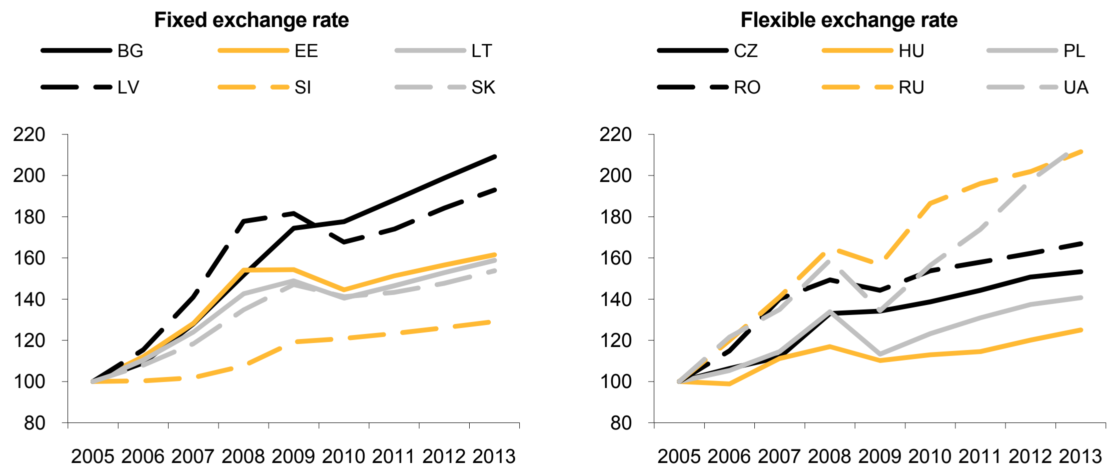
38 For an overview of key relevant issues currently under discussion see 'Macroeconomic coordination'. Deutsche Bank Research, 28 January 2011.

ally stable exchange rate and a 'fixer' that has used the euro since 1 January 2007). In both countries, the exchange rate adjusted ULC increased by less than 30% over the period 2000-2010.[39] During the boom years immediately preceding the crisis (2005-2008), ULCs were growing at double-digit average annual rates in most CESEE countries (and still faster in Russia and Ukraine), the exceptions being Hungary (5.6% p.a.) and Slovenia (1.8% p.a.). As the only country in the region,

Figure 12a

Aggregate ULC (at GDP level), EUR adjusted

2005 = 100



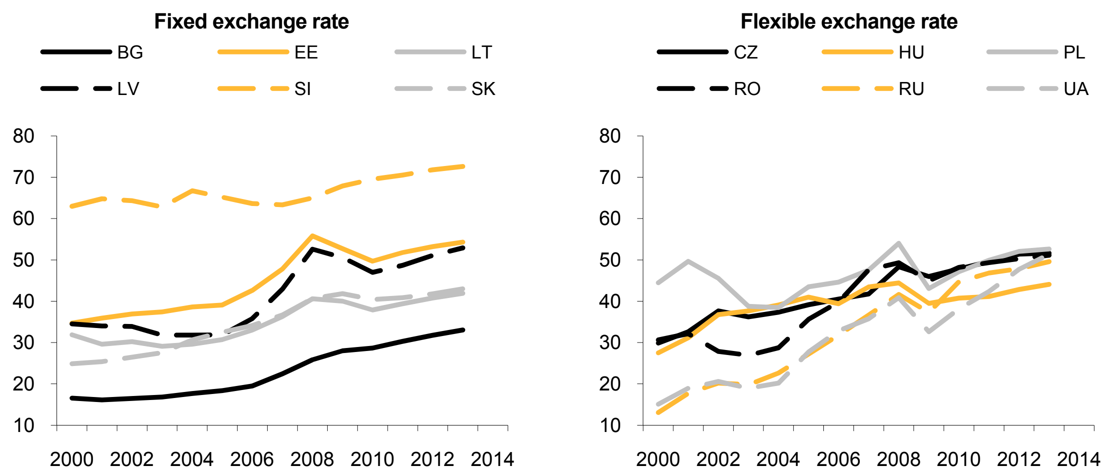
ULC: Unit Labour costs.

Source: wiiw estimates based on wiiw Annual Database incorporating national statistics and Eurostat; forecasts: wiiw.

Figure 12b

International comparison of aggregate ULC (at GDP level)

Austria = 100



ULC: Unit Labour costs.

Source: wiiw estimates based on wiiw Database incorporating Eurostat and national statistics; forecasts: wiiw.

39 For detailed data, also for other countries in the region, see Annex Table 2 and 3.

Slovenia even managed to improve its competitive-cost position relative to Austria over that period (Austria's ULC grew slightly faster – by 2.5% p.a. over the period 2005-2008). The international competitive-cost position (relative to ULCs) of all other CESEE countries in the region deteriorated as their ULCs increased much more rapidly than in Austria (or, for that matter, Germany) over that period. Obviously, such developments cannot not be sustained in the medium and long term, even though ULC levels in the CESEE countries are still relatively low. According to our estimates less than 50% of the Austrian level in 2010, with the exception of Slovenia and Croatia (Figure 12b).

The 2008-2010 crisis frequently resulted in a temporary and uneven drop in ULCs (both across countries and in time). It is interesting to note that the time pattern of individual countries' ULC adjustments differed – not least according to their exchange rate regime. In countries with flexible exchange rates (the Czech Republic, Hungary, Poland, Romania, Russia and Ukraine), ULCs dropped in 2009 as against 2008 (by as much as 15% in both Poland and Ukraine) – largely thanks to a substantial devaluation of the national currency (see Figure 13 and Annex Table 3). On the other hand, countries with fixed exchange rates (be it a currency board as in Bulgaria, Estonia, Latvia and Lithuania or use of the euro as in Slovenia and Slovakia) have, of course, been deprived of the devaluation option. This lack of exchange rate flexibility initially resulted in an increase in their ULCs (by as much as 15% in Bulgaria, 10% in both Slovakia and Slovenia in 2009) as their GDP and aggregate labour productivity (GDP per employed person) dropped and wages increased (the Baltic States proving an exception to the latter development). Restoration, albeit partial, of the cost-competitiveness (a reduction of ULCs) occurred in 2010 in most countries with fixed exchange rates (as opposed to an increase in ULCs and a deterioration of competitiveness recorded by the 'floaters', especially by Poland, Romania, Russia and Ukraine).[40]

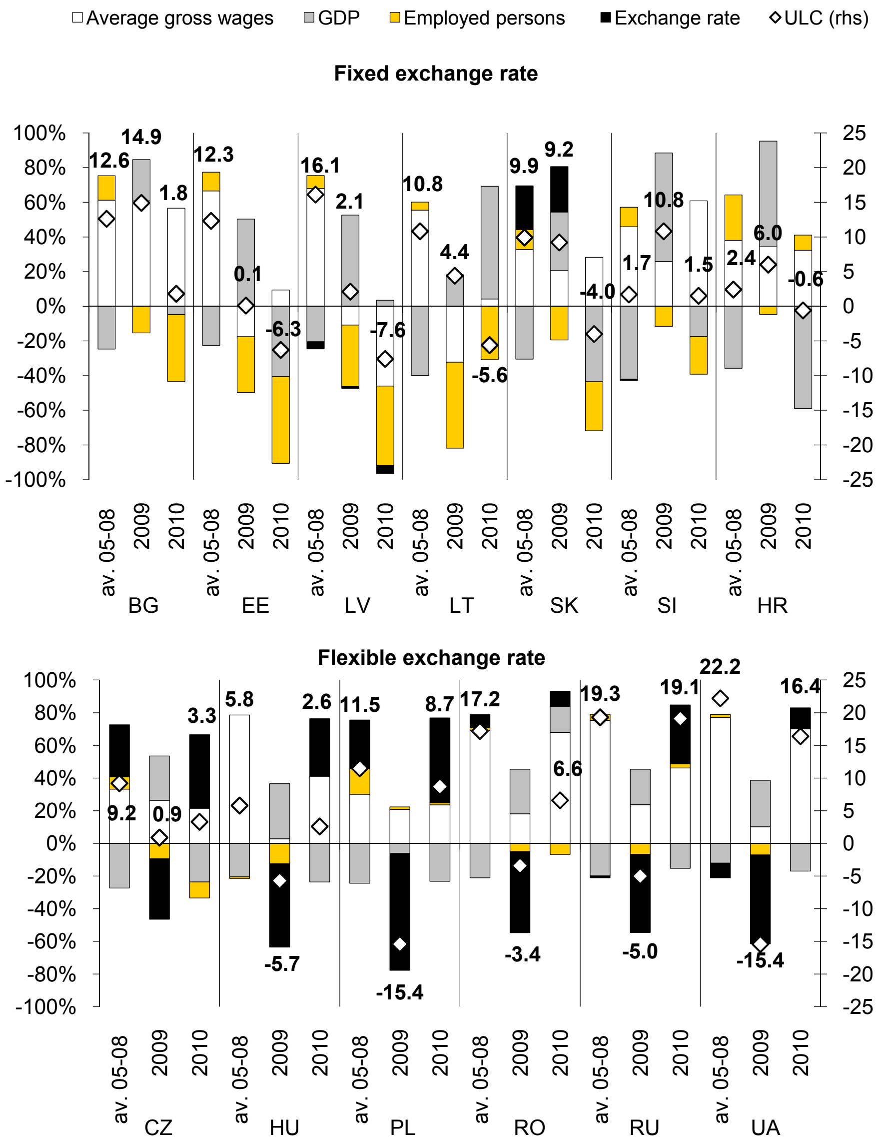
Apart from the varying spatial and time patterns of ULC adjustments between 'floaters' and 'fixers', it is also interesting to review ULC adjustment patterns in terms of their individual components. These are, apart from exchange rates, especially wages and labour productivity, with the latter decomposed into changes in output and employment (see Box 3 for details). As mentioned above, countries with flexible exchange rates managed to reduce their ULCs in 2009 largely thanks to exchange rate adjustments (currency depreciations). Usually those depreciations more than offset the adverse effects of declining labour productivity. Labour productivity dropped owing to the falling GDP, while employment cuts were initially kept in check. 'Competitive' devaluations even permitted a modest increase in nominal wages in some countries (Poland and Ukraine are extreme examples where devaluations absorbed most of the ULC adjustments in 2009 – see Figure 13, 'Flexible exchange rates').

[40] For the sake of simplicity, we do not use here trade-weighted real effective exchange rates. Yet for some CESEE 'fixers' (such as Slovakia) which trade a lot with 'non-euro flexible' exchange rate regime partners (such as the Czech Republic, Hungary, Poland and Russia), the recent depreciation of the euro improved their cost-competitiveness.

Figure 13

Unit labour costs and the contribution of components, 2005-2010

change in % against preceding year



Source: wiiw Database incorporating national and Eurostat statistics; wiiw own calculations.

Box 3

The concept of Unit Labour Costs (ULCs)[41]

Assuming that individual ULC components are defined on a comparable basis (in time and across countries/industries, respectively, or both), ULC can be defined as follows:

$$ULC = LC / LP$$

where LC are labour costs or gross wages (per employed person) and the labour productivity (LP) is defined as real output per employed person:

$$LP = OUT / EMP$$

Thus, unit labour costs can be rewritten as:

$$ULC = LC/LP = LC / (OUT / EMP) \qquad (1)$$

Accordingly, any change (Δ) in unit labour costs (ΔULC, measured either in logarithm or per cent) can be decomposed in the following way (time or country subscripts are omitted):

$$\Delta ULC = \Delta LC - \Delta LP = \Delta LC - \Delta OUT + \Delta EMP \qquad (2)$$

ULC will rise (that is, labour cost competitiveness will decline) when the labour cost increase is higher than the corresponding increase in productivity and vice versa. In turn, productivity changes are determined by the relative growth rates of output and employment: For instance, LP will increase if (real) output growth is faster than employment growth. And, with given labour costs, this will lower ULC and increase the cost competitiveness of the respective country or industry. Formula (2) is basically valid for comparisons in both time (ULC growth rates) and across countries (ULC levels).[42] In practice, it is much easier to compare growth rates rather than levels (productivity level comparisons are particularly problematic) since the available statistical data tend to be more consistent over time than across countries. In international ULC comparisons over time, the 'national' ULCs in formula (2) are frequently adjusted for the relative movements of exchange rates (ER). Labour costs in national currency are therefore converted into euro (at current exchange rates) and fluctuations of exchange rates have an impact on ULC as well.[43] The exchange rate effect has been substantial – see the differences in ULC performance of 'floaters' vs. 'fixers'.

On the other hand, the 'fixers' cannot by definition use exchange rates as a tool for restoring ULC competitiveness in the crisis. They thus have to resort to other policy instruments: either cutting nominal wages or reducing employment in order to offset the drop in output (these options are so-called 'internal devaluation'). As Figure 13 shows, employment has usually borne the main burden of restoring competitiveness in the absence of exchange rate flexibility (in Bulgaria and the Baltic

41 See P. Havlik (2005), 'Unit Labour Costs in the New EU Member States', *wiiw Statistical Reports*, No. 1, for details.

42 Changes in time (Δ) can be replaced by differences among countries.

43 Currency appreciation will push up labour costs expressed in euros and thus ULCs as well; currency depreciation ('competitive devaluation') will lower labour costs in euros and thus reduce the ULCs of the respective country. Alternatively, if one is interested in the (domestic) purchasing power of wages, PPPs can be used for the conversion of LC instead of ER. In the absence of branch-specific Unit Value Ratios, productivity levels are usually compared after conversion from the national currency using PPPs.

States, nominal wages were cut as well). A large part of the recent (2010) spectacular productivity improvements (in manufacturing industry in the Baltic States and Slovakia) was brought about by cuts in employment (see also section on labour market below).

In sum, one can see that flexible exchange rates not only permit a swifter adjustment of competitiveness in times of crisis, but the 'floaters' can achieve the same outcome with far fewer adverse effects on employment. This has been one of the reasons why we argued earlier that flexible exchange rates turned out to be the preferable option in times of crisis.[44] In the post-crisis period, the ULC are forecast to grow once again – more or less in line with the resumption of income catching-up (see below). However, like other macroeconomic variables forecast, ULCs are expected to grow at half the speed they displayed before the crisis (see Annex Tables 2 and 3).

Reducing external imbalances

Export-led recovery in 2010 (which was preceded by massive crisis-related import cuts in 2009) has contributed to a spectacular correction of previous (and, with the benefit of hindsight, often unsustainable) external disequilibria. The adjustment was dominated by an improvement in the balance of trade in goods: trade deficits were reduced considerably in all CESEE countries, most of all (in % of GDP) in Bulgaria, Estonia, Croatia and Serbia over the period 2008-2010 (Table 3 and Figure 14). As a result, the current account balance – one of the key additional indicators considered by the EU in the context of envisaged surveillance of economic governance[45] – improved markedly in all CESEE countries. The proposed lower limit of -3% (current account deficit in % of GDP) was exceeded in 2010 by just two NMS (Poland and Romania), as well as by a number of countries in Southeast Europe (Montenegro and Albania are two extreme examples with the largest current account deficits).

The current account developments forecast for the period 2011-2013 point to a deterioration of external balances in all CESEE countries; however, extremely high deficits (more than 10% of GDP – similar to the current situation in Greece and Portugal) are only expected in Montenegro, Albania and Serbia. The financing of those deficits is by no means secure, especially since capital flows are likely to remain volatile throughout the region and the political climate for foreign direct investments (including privatizations) in those particular countries will remain extremely challenging. That circumstance holds true for a number of other CESEE countries as well. External financing constraints will in general be one of the key brakes on future economic growth, even in countries where the external position is much more reassuring.[46] That having been said, we have to emphasize that the financial

44 See K. Laski and L. Podkaminer (2010), 'Long-term growth prospects in Central and Eastern Europe hinge on changes in the basic paradigms of EU economic policy-making', in: V. Astrov, M. Holzner, K. Laski, L. Podkaminer et al., 'Will Exports Prevail over Austerity?', *wiiw Current Analyses and Forecasts*, No. 6, July 2010, pp. 1-22, and M. Landesmann and V. Gligorov (2010), 'Redirecting the growth model in Central and Eastern Europe: Policy issues', in V. Gligorov, P. Havlik, M. Landesmann, J. Pöschl, S. Richter et al., 'Crisis is Over, but Problems Loom Ahead', *wiiw Current Analyses and Forecasts*, No. 5, February 2010, pp. 1-21.

45 See 'Enhancing economic policy coordination for stability, growth and jobs', European Commission, Brussels, 2010, COM 367/2.

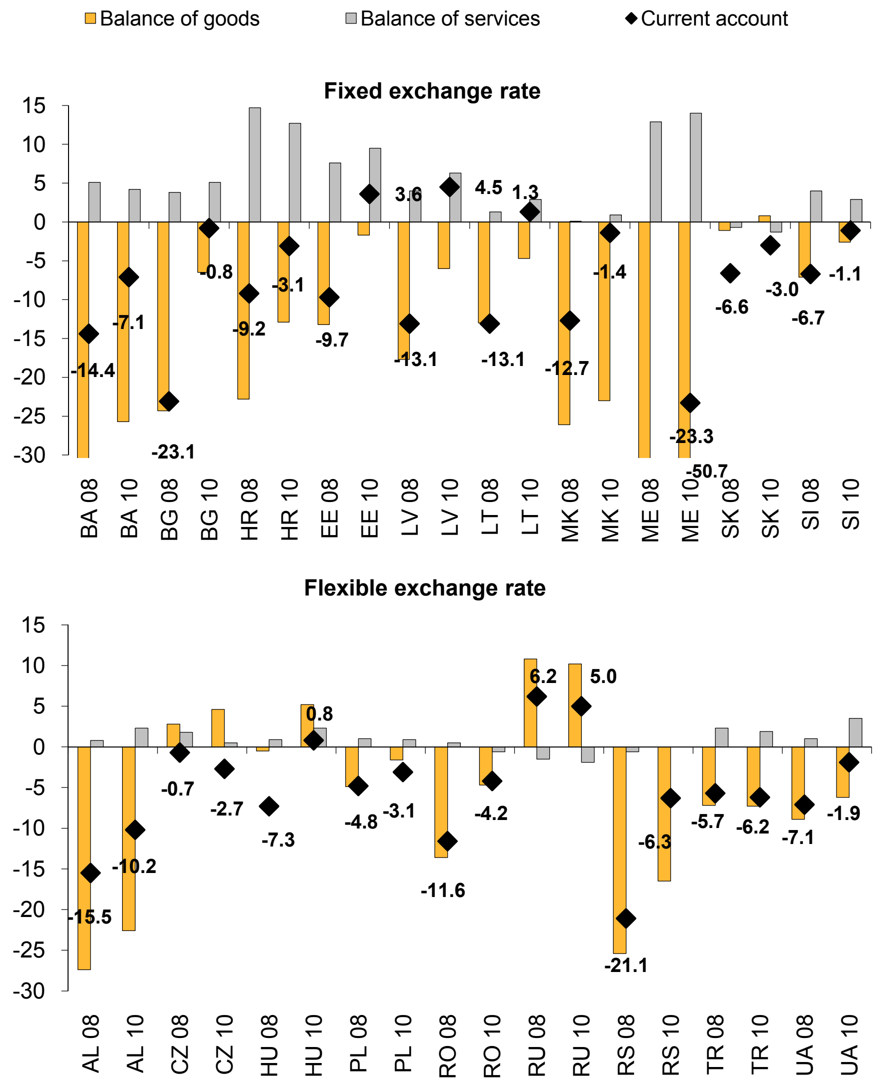
46 The (net) external position is one of the scoreboard indicators proposed by the Commission for macroeconomic surveillance in the framework of new economic governance ('EU economic governance: Commission sets the yearly priorities for EU growth', IP/11/22, Brussels, 12 January 2011). Unfortunately, in defining the scoreboard criteria

position of most CESEE countries (including that of the NMS) has been much more comfortable than elsewhere (especially compared to the 'periphery' of the eurozone).

Figure 14

Components of current account, 2008-2010

in % of GDP



Source: wiiw Database incorporating national and Eurostat statistics; wiiw own calculations.

(regarding both the above mentioned unit labour costs as well as the net external position, both of which should help to assess the external competitiveness) the necessary clarity leaves much to be desired. Thus, for instance, in the MEMO/11/11 ('Annual Growth Survey: Summary of economic analysis and messages', Annex 1) accompanying the above quoted economic governance proposal the net external account position (net borrowing in % of GDP) is wrongly indicated.

Table 3

Foreign financial position

in % of GDP

	Trade Balance (BOP)						Current account						Gross external debt		
	2008	2009	2010 1)	2011	2012	2013	2008	2009	2010 1)	2011	2012	2013	2008	2009	2010 1)
				Forecast						Forecast					
Bulgaria	-24.3	-11.9	-6.5	-8.2	-8.8	-9.3	-23.1	-9.9	-0.8	-3.8	-4.5	-5.1	104.7	107.9	100.4
Czech Republic	2.8	5.0	4.6	3.9	3.0	3.4	-0.7	-1.1	-2.7	-2.5	-3.0	-3.0	43.5	43.9	45.2
Estonia	-13.2	-4.0	-1.7	-0.6	-0.6	-1.6	-9.7	4.5	3.6	0.6	-1.7	-2.7	118.2	125.5	112.9
Hungary	-0.5	3.6	5.2	6.0	6.7	7.3	-7.3	-0.4	0.8	-1.6	-2.1	-2.4	123.1	140.9	138.0
Latvia	-17.7	-7.1	-6.0	-5.7	-5.8	-6.3	-13.1	8.6	4.5	2.1	-1.5	-2.7	130.2	158.1	157.8
Lithuania	-13.0	-3.1	-4.7	-5.1	-7.1	-9.4	-13.1	4.3	1.3	-0.7	-2.6	-3.6	71.4	87.0	86.8
Poland	-4.9	-1.0	-1.8	-2.4	-3.9	-4.7	-4.8	-2.2	-3.2	-3.5	-3.8	-4.1	56.8	59.6	65.3
Romania	-13.6	-5.8	-4.7	-5.1	-6.3	-5.8	-11.6	-4.2	-4.2	-5.2	-6.4	-6.3	56.5	69.1	74.0
Slovakia	-1.1	1.9	0.8	0.0	0.0	0.0	-6.6	-3.2	-3.0	-4.6	-4.9	-5.1	55.6	71.9	74.0
Slovenia	-7.1	-2.0	-2.6	-2.3	-2.0	-1.9	-6.7	-1.5	-1.1	-1.6	-1.7	-1.7	105.2	113.8	111.7
Croatia	-22.8	-16.3	-12.9	-12.5	-12.5	-13.3	-9.2	-5.5	-3.1	-4	-5	-5	85.5	97.8	100.1
Macedonia	-26.1	-23.0	-23.0	-21.8	-21.8	-25.4	-12.7	-7.2	-1.4	-4	-5	-5	49.3	56.8	58.9
Montenegro	-67.5	-46.0	-44.0	-43.1	-45.3	-47.5	-50.7	-30.1	-23.3	-22	-21	-22	15.6	23.5	31.3
Turkey	-7.2	-4.1	-7.3	-7.3	-6.8	-6.7	-5.7	-2.3	-6.2	-6.2	-5.7	-5.5	45.1	42.2	39.0
Albania	-27.4	-26.6	-22.6	-25.3	-25.6	-27.3	-15.5	-15.5	-10.2	-12.6	-13.7	-16.1	35.0	40.0	40.9
Bosnia & Herzegovina	-38.2	-27.8	-25.7	-24.9	-23.6	-22.0	-14.4	-6.8	-7.1	-7	-6	-6	17.2	21.8	25.3
Serbia	-25.4	-17.1	-16.5	-15.4	-15.6	-16.1	-21.1	-7.0	-6.3	-8	-10	-10	68.6	76.6	81.8
Kazakhstan	25.1	13.9	21.3	18.6	17.1	15.7	5.2	-3.1	3.1	3.2	2.3	1.8	84.3	99.5	82.4
Russia	10.8	9.1	10.2	9.1	7.9	7.0	6.2	4.0	5.0	4.1	3.4	2.8	34.2	36.4	33.1
Ukraine	-8.9	-3.7	-6.1	-6.6	-6.7	-7.2	-7.1	-1.5	-1.9	-2.5	-2.8	-3.1	82.6	90.3	80.8

1) Preliminary and wiiw estimates.

Source: wiiw Database incorporating national and Eurostat statistics. Forecasts by wiiw.

Fiscal adjustments without visible growth stimulus

The crisis also resulted in a massive deterioration of public finances in all advanced economies; the CESEE countries were no exception in this respect. Without going into detail, suffice it to say that the corresponding situation in the CESEE countries was again (and still is) much better than that in most advanced economies. As for levels of public debt and government fiscal deficits, the CESEE countries on average have fared better than others, although the fiscal deficits in Latvia, Lithuania, Poland, Romania and Slovakia are definitely excessive (about 8% of GDP in 2010 – see Table 4). On the other hand, public debt levels in the CESEE countries are (with the exception of Hungary) rather low. Not only are they lower than current levels in the eurozone, but they are also far below 60% of the GDP benchmark required by the Maastricht criteria (Table 4).[47]

[47] This indicator will likely form another part of the proposed European economic governance scoreboard.

Table 4

Fiscal balance and public debt, in % of GDP

	Fiscal balance in % of GDP						Public debt in % of GDP					
	2008	2009	2010 1)	2011	2012	2013	2008	2009	2010 1)	2011	2012	2013
					Forecast						Forecast	
Bulgaria	1.7	-4.7	-3.9	-3	-2.5	-2	13.7	14.7	15.3	17	18	19
Czech Republic	-2.7	-5.8	-4.8	-4.6	-3.5	-3.5	30.0	35.3	38.9	42.1	43	44
Estonia	-2.9	-1.8	-1.3	-1.5	-1	-1	4.6	7.2	8	9	8.5	7.5
Hungary	-3.7	-4.4	-4	-3	-3	-3	72.3	78.4	78.5	74	73	72
Latvia	-4.1	-10.2	-8	-5.5	-4	-3	19.7	36.7	50	53	55	53
Lithuania	-3.3	-9.2	-8	-6	-4.5	-3	15.6	29.5	40	43	45	43
Poland	-3.7	-7.2	-7.9	-5.5	-4	-3	47.1	50.9	53.2	54.2	53.5	52
Romania	-5.7	-8.6	-7.5	-6	-5	-4	13.4	23.9	30.5	33	34	35
Slovakia	-2.1	-7.9	-8	-5.4	-5.0	-4.5	27.8	35.4	42.1	45.1	47.4	47
Slovenia	-1.8	-5.8	-6	-5.5	-5	-4.5	22.5	35.4	38.5	44	48	50
Croatia	-1.4	-4.1	-5.7	-6.1	-5.6	-5	28.9	35.3	40.9	45.9	49.9	52
Macedonia	-0.9	-2.6	-3	-2	0	-1	28.7	32.0	34.0	35	34	33
Montenegro	1.7	-3.5	-5	-3	-1	-1	26.8	38.0	43.0	44	42	41
Turkey	-2.2	-6.7	-4	-3	-2	-2	39.5	45.4	48.0	49	48	47
Albania	-5.5	-7.0	-3	-3	-3	-7	55.2	61.6	61	61	60	62
Bosnia and Herzegovina	-2.2	-4.5	-4.5	-3.5	-2.5	-2	30.8	33.4	36	38	39	40
Serbia	-2.6	-4.3	-4.8	-3	-3	-2	27.9	32.6	36	36	36	35
Kazakhstan	-2.1	-3.1	-2.7	-2.5	-2	-1	8.3	12.9	16.2	14	12	12
Russia	4.9	-6.3	0	-2	0	0	5.7	8.3	8.7	10	10	10
Ukraine	-1.5	-4.1	-6	-4	-3	-3	20.0	34.8	39.8	43	43	41

1) Preliminary and wiiw estimates.

Source: wiiw Database incorporating national and Eurostat statistics. Forecasts by wiiw.

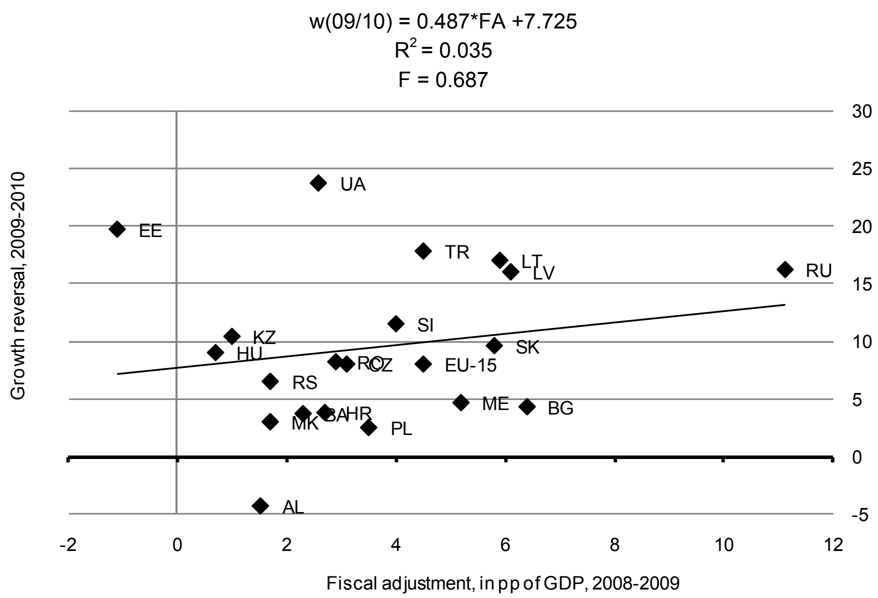
The recent deterioration in public finances did not come about primarily as a result of excessive government spending, but to a large degree it was the outcome of the crisis-related drop in fiscal revenues. In the NMS, government revenues dropped on average from 39.8% of GDP in 2007 to 38.2% in 2010. At the same time, government expenditure rose from 41.7% of GDP (2007) to 44.8% of GDP (2010), largely on account of the effects of automatic 'fiscal stabilizers' rather than deliberate fiscal stimulus programmes. In the same period, the aggregate GDP in the NMS increased by about 2% in real terms and more than 11% in current euros. The resultant increase in the fiscal deficit (that rose by more than 4 percentage points from less than 2% of NMS average GDP in 2007 to 6.6% of GDP in 2010 – see Table II) may have softened the adverse impact of the crisis, yet it has hardly contributed to the recent recovery. Figure 15 illustrates a rather weak (statistically insignificant, yet positive) relationship between the extent of recent fiscal adjustments and GDP growth reversal in the CESEE countries. Given the sorry state of public finances, the ensuing budget consolidation efforts and the limited fiscal space in general,[48] we cannot expect any new additional growth-stimulating

[48] For more details, see B. Bakker (2011), 'Limited Fiscal Space in CESEE', 68th East Jour Fixe, OeNB, February (mimeo).

measures from the public sector (such as a rise in public infrastructure investments or social spending) in most CESEE countries possibly (except Poland and Ukraine, both of which are implementing infrastructure projects related to upcoming European Football Championship in 2012 and highway construction in Slovakia). This offers yet another reason for rather restrained GDP growth forecasts for the next couple of years.

Figure 15

Growth reversal and fiscal adjustment



Source: National statistics, Eurostat.

Labour market distress: youth and low skilled suffer most[49]

The economic crisis has triggered a substantial drop in employment in the CESEE region. Once again, the incidence of job reductions differed substantially across regions and individual countries. In the Baltic States, which were hit hardest by the crisis, employment contracted by 13% between the third quarter of 2008 and the third quarter of 2010, while in the entire NMS region the decline was only 2.5% (similar to the drop experienced in the EU-15). In the Western Balkan countries employment fell on average by 8.7%; in Russia, where the supply of labour is shrinking owing to demographic factors, the impact of the crisis on employment has been moderate, with the number of jobs down by a mere 1.5%. Kazakhstan even reported some employment generation (0.4%). In Ukraine, the drop in employment (-3.9%) was much weaker than the drop in real GDP (about 11%).

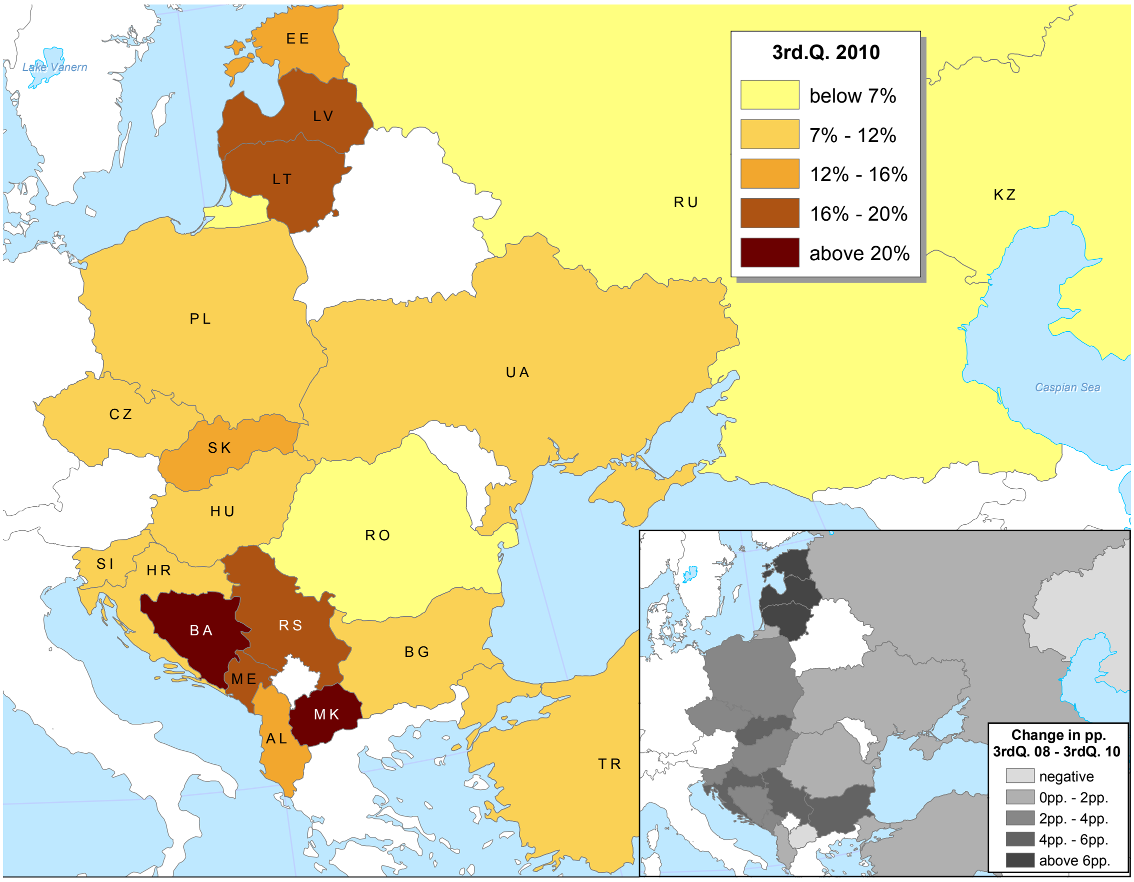
Employment growth resumed apace with economic recovery in most NMS in the second quarter of 2010. However, with the exception of Poland employment levels remained lower everywhere – and in some cases even much lower – than before the crisis. Job growth in Ukraine and Russia has also gained some momentum since the beginning of 2010, while Kazakhstan has been reporting con-

49 The Labour market section was drafted by Sebastian Leitner and Hermine Vidovic, both wiiw.

tinuous employment growth. By way of contrast, most Western Balkan countries, notably Serbia, Croatia, Montenegro and Bosnia and Herzegovina, still suffered noticeable employment cuts throughout 2010.

Map 1

Unemployment rates (LFS)



Source: Eurostat statistics; own calculations.

The drop in employment has had a disproportionate impact on young people (15-24 years): the unemployment rate in this age group in the NMS increased from 16% in mid-2008 to 24% in the third quarter of 2010 (in the EU-15 it is close to 20%). In the Western Balkans, where unemployment among the young had reached critical levels even before the recent crisis, the situation has deteriorated further. Unemployment rates among young people in the third quarter of 2010 ranged between 31% in Croatia and almost 60% in Bosnia and Herzegovina. Youth unemployment in Turkey was similar to the EU-15 level. In Russia and Ukraine, the unemployment rate among the young rose only slightly (to approximately 15% at the end of 2010), whereas the youth unemployment rate in Kazakhstan even dropped to 5.4%.

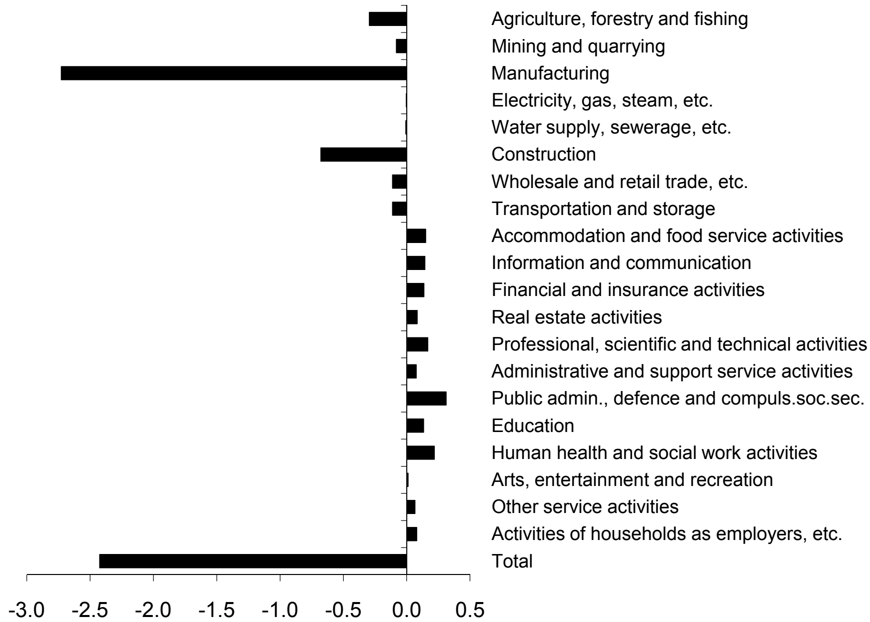
Shedding labour in manufacturing and construction

In order to analyse the structural effects of the crisis on labour markets, we again compare employment figures for the third quarter 2008 with those for the third quarter 2010. This period was chosen to eliminate seasonal effects that are most evident in the agriculture and construction sectors. Throughout the CESEE region, employment losses resulted mostly from a contraction in: (i) manufacturing (in the NMS it was most noticeable in textiles and wearing apparel, machinery and metal production); and (ii) construction as a consequence of bursting housing bubbles and the contraction in investments mentioned above. Developments in Poland stood in marked contrast to those in the other NMS; the country experienced job growth in all service sectors – and even in construction. As for the Western Balkan countries, apart from construction and manufacturing, job reductions in agriculture contributed significantly to overall employment losses.

Figure 16

Changes in employment in the NMS-10, 3rd quarter 2008 - 3rd quarter 2010

(weighted contributions to employment growth)



Source: Eurostat; own calculations.

The crisis also led to an acceleration of structural change in labour markets according to *levels of education*. Low-skilled employment fell by almost 10% between the third quarter 2008 and the third quarter of 2010; today it accounts for only 12% of total employment in the NMS. Medium-skilled jobs, accounting for about two thirds of total employment in the NMS, also declined remarkably (by 5.1%). At the same time, however, a significant rise in highly skilled employment (by 10.7%) was to be observed. The latter trend is driven foremost by a rise in employment in the services sector in Poland and the Czech Republic.

Labour market prospects not very encouraging

Taking into account the high losses in productivity suffered by many CESEE countries during the crisis, it is to be expected that economic recovery will be followed by a period of jobless growth; rising output will be associated with a rise in productivity and capacity utilization – not with a rise in jobs.[50] In addition, the GDP growth projected is too moderate to spur any marked additional labour demand.[51] The unemployment rate is thus expected to drop only gradually in the medium term. The risk of cyclical unemployment becoming structural is definitely on the rise. In the NMS, we expect employment to grow slowly by 0.5% in 2011 and by 1.5% in the two years thereafter. The unemployment rate will thus fall only gradually and will stay much above the pre-crisis level (6.5% in 2008). The outlook for the Western Balkan countries does not suggest any substantial improvements either. With the exception of Albania and Croatia where the number of unemployed should decline slowly, unemployment is expected to remain stagnant at high levels in most countries of the region. As for employment in Turkey, it is expected to grow by around 2% p.a. in the coming years and the unemployment rate will stabilize at 10%. A drop in unemployment is rather unlikely as close to one million people enter the Turkish labour market each year. Forecasts for Russia, Ukraine and Kazakhstan point to a slight decline in unemployment over the years to come. In Ukraine, given the announced staff reductions in public administration, employment will stagnate in 2011 and grow, if at all, only modestly in the years thereafter. For Russia, we expect a contraction of employment owing to the government phasing out sponsored schemes that were designed to keep workers in employment during the crisis, but also on account of productivity increases and demographic developments. In the medium and long term, declining employment due to the shrinking labour force will impose a major constraint on Russian economic growth.

Interrupted catching-up process expected to resume soon

The recent crisis not only abruptly interrupted the catching-up process in the CESEE countries, but it also set the whole region back a couple of years. The estimated economic development levels in the CESEE countries (measured in terms of GDP per capita at purchasing power parities) peaked in 2008, reaching about 60% of the EU average in the NMS (with major variances within the NMS group); 30%-40% of EU average in Southeast Europe, 53% in Russia and 24% in Ukraine – see Figure 16 and Annex Table 1. The abrupt drop in GDP in the majority of CESEE countries during the crisis (which, with few exceptions, was much steeper than in Western Europe) resulted not only in an absolute decline in per capita GDP, but also in widening of relative income gaps vis-à-vis the EU average. The wiiw medium- and long-term GDP growth scenario for the CESEE countries uses the GDP growth rates forecast for the period 2011-2013 (Table I), estimated GDP price deflators and extrapolated purchasing power parities (benchmark PPPs for 2009 from Eurostat). For the period after 2013, we expect a GDP growth differential of 2 percentage points relative to Western Europe (EU-15) and zero population growth.

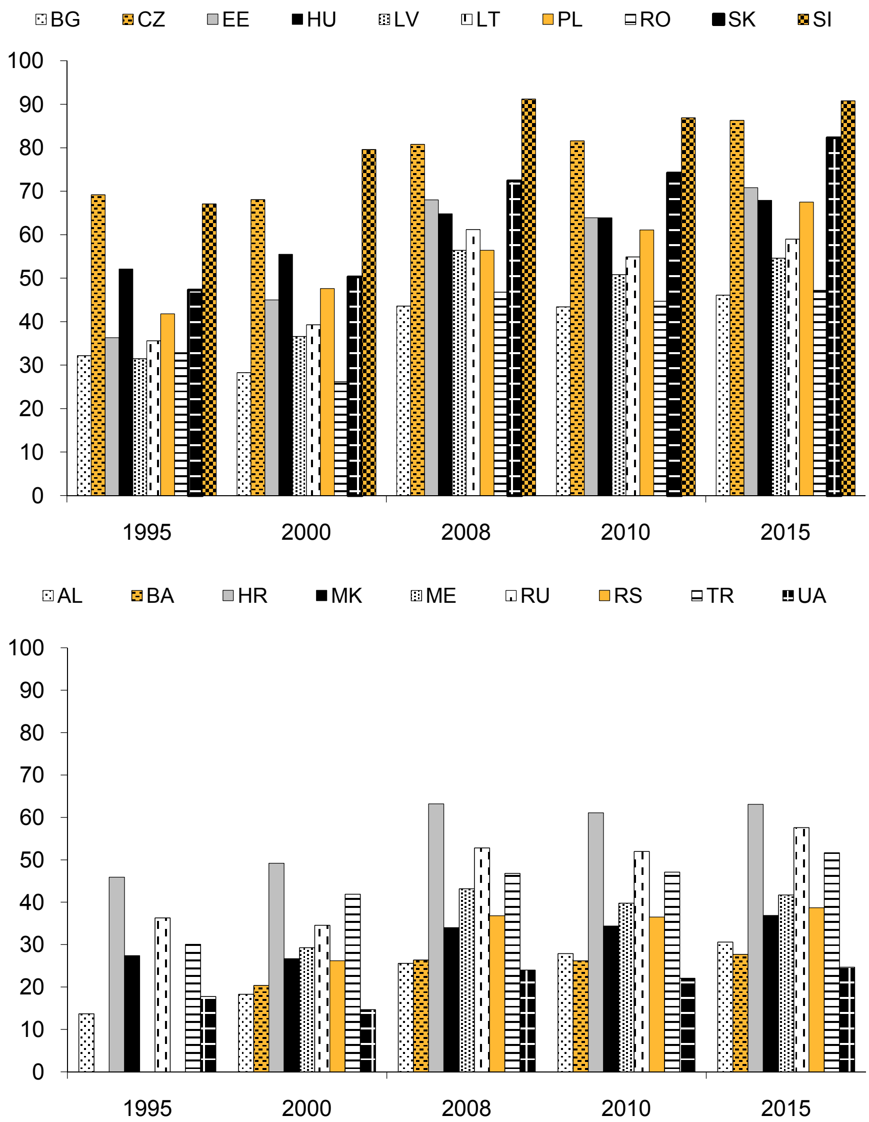
50 See, European Commission, COM(2011) 11 final, Brussels 12 January 2011.

51 The earlier estimated 'critical GDP growth rate' needed for employment to stay at least constant in the NMS was about 5% – see Havlik, P., (2008), 'Economic Restructuring in the New EU Member States and Selected Newly Independent States: Effects on Growth, Employment and Productivity'. In: Grinberg, R., Havlik, P., Havrylyshyn, O. (eds.), 'Economic Restructuring and Integration in Eastern Europe'. Nomos, Baden-Baden, pp. 47-72.

Figure 17

GDP per capita at current PPPs (EUR), from 2010 at constant PPPs

European Union (27) average = 100



Remark: From 2011 wiiw projections.

Source: wiiw Database incorporating national and Eurostat statistics; wiiw own calculations.

The findings of the income catching-up forecast are presented in Figure 17 (for details and longer-term projection see Annex Table 1). Besides deteriorating labour markets, the repercussions of the crisis in terms of income convergence have indeed been dramatic: several CESEE countries (Latvia, Lithuania, Romania, Slovenia, Croatia and Montenegro) have lost up to 7 years (sic) in their catching-up process. They will not attain their pre-crisis (2008) per capita GDP levels before 2015 (in Lithuania not even before 2020).[52]

Forecast summary: "back to normal" – but a slower and harder normalcy

The outlook for the world economy has improved in the course of the past year and the economic recovery has proceeded apace in the EU as well. The CESEE countries have also recovered from the crisis; the majority of them recorded positive GDP growth in 2010. Only in Latvia, Romania, Croatia and Montenegro did the economy continue to contract. On average, the recovery of exports appears to be even stronger than their growth before the crisis. By way of contrast, the trends in industrial output have remained more or less flat. The persistent decline in construction and fixed investments – both related to the still hesitant credit markets – represents one of the key internal downward risks to our moderately optimistic regional economic forecast at present.

The general outlook for the CESEE region in the baseline scenario reckons with a gradual strengthening of economic growth over the period 2011-2013, in most cases rarely exceeding 4% per annum. GDP growth will become more broadly based. The formerly predominant role of external demand will weaken somewhat, while both household consumption and gross fixed investments in particular will ultimately contribute positively to GDP growth.

With exports, industrial output levels and eventually also GDP growth having already recovered from the crisis, the economy is seen as having largely returned 'back to normal' with two important differences – (1) post-crisis growth will be slower (largely due to a more difficult financing as little has happened in terms of regulatory reform in the financial sector). That slower growth, however, also implies that (2) the labour market situation will be 'very far from normal'[53] as unemployment will remain high, with young and low-skilled workers being especially adversely affected, and any improvement only gradual and delayed.

Inflation rose throughout 2010 as food and commodity prices soared; in general, however, it will pose no (or little) immediate threat. The moderate economic upturn and a revival of capital inflows have resulted in renewed appreciation pressures on floating currencies. The developments forecast point to a gradual deterioration of current account positions in all CESEE countries, yet the return (or persistence) of extreme imbalances are only expected for Montenegro, Albania and Serbia. The financing constraint with respect to both domestic and external loans will constitute one of the key brakes on future economic growth. Given the sorry state of public finances and the ensuing budget consolidation efforts, we cannot expect any new additional growth-stimulating measures from the public sector in most CESEE countries – on the contrary, owing to the limited fiscal space government deficits and public debts will be scaled back.

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52 Note that this scenario implies an even more dramatic delay in the catching-up process for Greece and Portugal – see Annex Table 1.

53 To coin a phrase used by Christina Romer, former Chairman of the Council of Economic Advisors to President Obama, to describe the US situation a year ago (Romer, C.D., (2010), 'Back to a Better Normal: Unemployment and Growth in the Wake of the Great Recession', Princeton University, April).

The sharp drop in GDP in most CESEE countries during the crisis resulted in both absolute and relative declines in their per capita income levels. The catching-up process of the previous decade was thus interrupted and income gaps vis-à-vis Western Europe widened. In the baseline medium- and long-term GDP growth scenario for the CESEE countries, wiiw reckons with a renewed catching-up process starting as early as 2011 (after losing 5 to 7 years in terms of income convergence).

More detailed forecasts are to be found in the country tables in the following section of the report; the longer-term catching-up scenario as well as selected indicators of competitiveness are annexed hereto.

Anton Mihailov

Bulgaria:
A painful rebalancing

The most notable feature of Bulgaria's economic performance since the start of the global economic and financial crisis in 2008 was a spectacular macroeconomic adjustment which is best visible in the dynamics of the current account balance: the current account deficit dropped from unsustainable 25% of GDP in the years 2007-2008 to around 10% in 2009 and to some 1.5% in 2010. The dramatic rebalancing reflects a major re-positioning of economic growth drivers. For almost a decade, up to 2009, GDP growth in Bulgaria was nearly entirely driven by domestic demand (which, in turn, was fuelled by foreign borrowing) while net exports remained a drag on economic activity. In 2009-2010 this picture reversed dramatically and net exports turned out to be the only final demand item making a positive (and large in absolute terms) contribution to GDP growth while investments (especially in 2009) and household consumption (2010) fell sharply.

Concomitantly, there was a major re-orientation of sales by local manufacturers towards export markets: in current EUR terms, exports of goods in 2010 exceeded those of the pre-crisis in 2008 (and were up by one third from 2009 onwards), when real gross industrial output was about 20% higher than that in 2010. The ability to rapidly take advantage of emerging opportunities in international markets (on such a scale this happens for the first time in post-transition Bulgaria) is a sign of a maturing and vibrant private manufacturing sector. Among the export commodities that reported the highest growth in 2010 are both traditional items such as refined oil products (reflecting the newly installed production capacity in the LUKOIL refinery) and metals, but also mechanical and electrical engineering goods, which is a new development, thanks to new investment in these sectors in recent years. There are also new aspects in the directions of exports, with increasing share of emerging market countries, such as China, India, Brazil, and Korea.

However, the process of rebalancing has been rather painful: the cumulative decline of private consumption during 2009-2010 amounted close to 10% while gross fixed investment in this period dropped by some 35% in cumulative terms. The sharp fall in private consumption is difficult to rationalize in terms of macroeconomic performance indicators only. It comes against the backdrop of continued growth of real wages (by some 10% and 7% in 2009 and 2010, respectively) and of household savings (by some 13% year-on-year both in 2009 and 2010). Unemployment did jump in 2010 but not so dramatically as in other countries and not to the extent to explain the retrenchment in private consumption. As to fixed investment, apart from the drying up of the sources of external borrowing, the disproportionate fall also mirrors the drastic cutbacks in budgetary spending on public investment: domestically financed public investments were cut by more than 16% in 2010, after a reduction by 31% in 2009.

The chaotic management of public finances reflects the eclectic nature of the policy stance of the authorities. Since it came to power in July 2009, the (self-declared as "centre-right") GERB government never came up with any clearly formulated economic objectives and policies to pursue such objectives. At the same time, the government has already accumulated a record of ceding to pressures from interest groups, very often translating into openly populist moves. The management of public finances leaves the perception that it is not the government that seeks to lead the economy but instead is trailing behind it, in a crisis management pattern.

The few intentional policy moves in the area of public finances have been largely unproductive, resulting in outcomes exactly opposite to those originally targeted. Thus the above mentioned cuts in public investment had a highly damaging economic effect on economic activity in general. Another equally disastrous move was the increase in the tobacco excises in 2010. The net fiscal outcome of this move was negative due to increased tax evasion and a rise in grey economy tobacco sales: total net revenue from excises in 2010 dropped by more than 7% since 2009, despite the fact that the excise revenue from fuels increased thanks to higher prices. Overall, after years of improvements in the efficiency of tax collection, there has been a major reversal in this area in 2009-2010.

Although the outlook for the Bulgarian economy has been improving in the course of 2010, there are no signs of an imminent rapid recovery and robust growth in the short run. Thus the construction sector remained deeply in negative territory through 2010, mirroring the level of investment activity. While the decline in private consumer demand has been decelerating in the final months of 2010, it was still months away from a possible bottoming up. Both government consumption and public investment remained a major drag on economic activity throughout the whole year 2010. Given these trends, all main components of final domestic demand have been making negative contributions to GDP growth in 2010. It is thus only thanks to the robust expert performance that the rate of GDP growth for the year could move into positive territory.

The outlook for 2011 can be briefly characterized as an expectation for a modest recovery supported by an upturn in domestic demand. The gradual revival of the economy will mostly be driven by a recovery in private consumption and especially of private investment, whereas the public sector is not likely to give a boost to economic activity. The latter follows behind the 2011 budget targets, including the stipulated volumes and structure of public spending.

The 2011 budget envisages a further decline of consolidated budget revenue as a share in GDP which is an implicit recognition of a further deterioration in the efficiency of tax collection. Mirroring that, consolidated public expenditure would also drop as percentage of GDP, the target being to keep the budget deficit within the Maastricht range. The government has not given up on its declared objective to enter ERM-2 as soon as possible (and as early as the second half of 2011, according to recent statements) but it remains to be seen whether these are realistic goals or wishful thinking. The bottom line is that spending items key to economic activity such as public investment are expected to undergo further cuts in relative terms. The budget envisages also a freeze in public sector wages. These as well as other similar features underscore the unsupportive fiscal policy stance in 2011.

On the other hand, as noted earlier, both private consumption and especially fixed investment dropped to very low levels after two years of contraction. In purely statistical terms this suggests a very low base and hence a statistically measured recovery, say, in construction activity, that shows up as “strong” (in terms of the magnitude of the number) this could merely reflect a higher rate of capacity utilization. There are some first signs that capacity utilization in the construction sector is indeed starting to rise, which can be taken as an early indication of a forthcoming recovery in investment activity. An expected modest upturn in FDI would provide further support to fixed investment in 2011. Recent trends suggest that real retail sales in year-on-year terms could move into positive territory in the first or second quarters of 2011. If this trend continues, private consumption for 2011 as a whole should also be on a moderate rise.

Export performance is likely to remain strong in 2011, maintaining some of the accumulated momentum. However, it is difficult to expect rates of growth comparable to those seen in 2010 due to supply constraints. The fact is that manufacturers are already operating close to their production capacity limits (at least as regards exportable goods). Maintaining such high rates of export growth would thus require increases in production capacities, respectively, new investment and time. In view of this it is more likely that export growth will moderate in 2011 and in the following years. The revival of imports kept accelerating throughout the year and can be expected to continue in 2012 supported by the upturn in private investment and consumption. Overall – as a result of such trends – it can be expected that both the trade and the current account balance will deteriorate in 2011 but they will remain in a range that will not pose serious macroeconomic concerns.

Given the current domestic policy stance and the structural characteristics of the Bulgarian economy, it can be expected that similar macroeconomic trends will prevail in 2012 and 2013 as well. Overall GDP growth is likely to remain modest, curbed by both supply and demand constraints; on the one hand, supply constraints are likely to restrain the growth of manufacturing (hence exports); on the other hand the growth in private demand is likely to be contained by tight borrowing conditions, in particular abroad. It is highly unlikely that a demand-drive pattern of high growth similar to that seen in the period 2004 – 2008 could be repeated in the years ahead.

Domestic policy in coming years will continue to face a range of chronic structural problems, which have been neglected by several subsequent governments, including the current one. The healthcare sector – and the related health insurance system – present some of the most acute policy problems. Several ill-conceived reform attempts in this area already failed which not only contributed to further accumulation of problems but also damaged the credibility of the authorities in dealing with them. In addition, the solvency of the pension system was eroded by short-sighted populist moves; a major reform of this system is also urgently needed. Other chronic problems of the Bulgarian economy – and society in general – include corruption and crime. Although the present government largely came to power on an anti-corruption, anti-crime ticket, real progress in these spheres has been modest. Similarly, although the utilization of EU funds increased somewhat, the country’s absorptive capacity regarding such funds remains very low. Progress in any of these areas could bring considerable economic benefit; however, it appears that the current government does not have the political will and/or the capacity to undertake the necessary reforms.

Table BG

Bulgaria: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 [1)]	2011	2012 Forecast	2013
Population, th pers., average	7739.9	7699.0	7659.8	7623.4	7585.1	7560	7540	7520	7500
Gross domestic product, BGN mn, nom.	45483.8	51783.1	60184.6	69295.0	68537.2	71900	76500	82000	88000
annual change in % (real)	6.4	6.5	6.4	6.2	-4.9	0.3	2.5	3	3
GDP/capita (EUR at exchange rate)	3000	3400	4000	4600	4600	4900	.	.	.
GDP/capita (EUR at PPP)	8200	9000	10000	10900	10400	10600	.	.	.
Consumption of households, BGN mn, nom.	31309.0	34761.9	41300.8	45765.7	44985.6	44000	.	.	.
annual change in % (real)	6.9	8.7	9.1	3.4	-3.5	-6	3	3	3
Gross fixed capital form., BGN mn, nom.	11711.3	14297.5	17263.9	23282.6	16720.1	16500	.	.	.
annual change in % (real)	30.8	13.1	11.8	21.9	-29.0	-8	9	8	8
Gross industrial production [2)]									
annual change in % (real)	7.0	6.0	9.6	0.6	-17.4	1.2	6	8	8
Gross agricultural production									
annual change in % (real)	-6.0	-0.1	-21.0	33.0	-1.6	-3.3	.	.	.
Construction industry [3)]									
annual change in % (real)	31.9	23.9	27.9	26.5	-34.7	-17.3	.	.	.
Employed persons - LFS, th, average	2981.9	3110.0	3252.6	3360.7	3253.6	3052.8	3100	3150	3200
annual change in %	2.0	4.3	4.6	3.3	-3.2	-6.2	1.5	1.6	1.6
Unemployed persons - LFS, th, average	334.4	305.7	240.2	199.7	238.0	348.1	.	.	.
Unemployment rate - LFS, in %, average	10.1	9.0	6.9	5.6	6.8	10.2	9	8	7
Reg. unemployment rate, in %, end of period	10.7	9.1	6.9	6.3	9.1	9.2	.	.	.
Average gross monthly wages, BGN	323.7	360.3	430.6	524.5	591.8	642.0	.	.	.
annual change in % (real, gross)	5.4	3.7	10.4	8.4	9.8	5.9	.	.	.
Consumer prices (HICP), % p.a.	6.0	7.4	7.6	12.0	2.5	3.0	4	4	4
Producer prices in industry, % p.a.	7.9	12.0	7.7	10.9	-6.5	8.6	.	.	.
General governm.budget, EU-def., % GDP									
Revenues	40.7	36.2	40.8	39.3	35.9	33.5	.	.	.
Expenditures	39.7	34.4	39.7	37.6	40.6	37.4	.	.	.
Net lending (+) / net borrowing (-)	1.0	1.9	1.1	1.7	-4.7	-3.9	-3	-2.5	-2
Public debt, EU-def., in % of GDP	27.5	21.6	17.2	13.7	14.7	15.3	17	18	19
Central bank policy rate, % p.a., end of period [4)]	2.1	3.3	4.6	5.8	0.6	0.2	.	.	.
Current account, EUR mn	-2705.7	-4647.0	-7756.0	-8191.0	-3477.0	-282.7	-1500	-1900	-2300
Current account in % of GDP	-11.6	-17.6	-25.2	-23.1	-9.9	-0.8	-3.8	-4.5	-5.1
Exports of goods, BOP, EUR mn	9466.3	12012.0	13512.0	15203.0	11699.0	15554.2	16800	17800	18800
annual growth rate in %	18.6	26.9	12.5	12.5	-23.0	33.0	8.0	6.0	5.6
Imports of goods, BOP, EUR mn	13876.1	17575.0	20758.0	23800.0	15874.0	17955.3	20000	21500	23000
annual growth rate in %	26.9	26.7	18.1	14.7	-33.3	13.1	11.4	7.5	7.0
Exports of services, BOP, EUR mn	3564.1	4187.0	4760.0	5375.0	4915.0	4954.7	5250	5500	5750
annual growth rate in %	9.3	17.5	13.7	12.9	-8.6	0.8	6.0	4.8	4.5
Imports of services, BOP, EUR mn	2745.2	3264.0	3586.0	4045.0	3617.0	3062.4	3300	3500	3700
annual growth rate in %	5.3	18.9	9.9	12.8	-10.6	-15.3	7.8	6.1	5.7
FDI inflow, EUR mn	3152.1	6221.0	9046.0	6685.0	3283.0	1359.5	1300	1500	1800
FDI outflow, EUR mn	249.1	141.0	207.0	483.0	-90.0	149.8	.	.	.
Gross reserves of NB excl. gold, EUR mn	6813.9	8309.1	11215.9	11927.6	11942.9	11611.8	.	.	.
Gross external debt, EUR mn	15506.9	20690.9	29016.8	37112.4	37808.1	36918.3	.	.	.
Gross external debt in % of GDP	66.7	78.1	94.3	104.7	107.9	100.4	.	.	.
Average exchange rate BGN/EUR	1.9558	1.9558	1.9558	1.9558	1.9558	1.9558	1.956	1.956	1.956
Purchasing power parity BGN/EUR	0.7154	0.7454	0.7837	0.8357	0.8682	0.8987	.	.	.

Note: Gross industrial production, construction output and producer prices refer to NACE Rev. 2.

1) Preliminary and wiiw estimates. - 2) Enterprises with 10 and more employees. - 3) Private enterprises with 5 and more employees, all enterprises in public sector. - 4) Base interest rate. This is a reference rate based on the average interbank LEONIA rate of previous month (Bulgaria has a currency board).

Source: wiiw Database incorporating Eurostat and national statistics. Forecasts by wiiw.

Leon Podkaminer

The Czech Republic:
Growth slowdown after the 2010 speed-up

The positive GDP growth which started in the second half of 2009 accelerated in the second and third quarters of 2010. In the fourth quarter of 2010, the GDP growth rate may have even surpassed the 3% mark (year-on-year). Preliminary estimations suggest that in the whole year 2010 the GDP rose by 2.3%. Although representing a definite recovery (after a 4.1% contraction in 2009) the recent performance does not yet seem to signify the return of sustainable and more robust growth.

Rising inventories were the primary factor behind the 2010 growth. Replenishment of inventories could be a natural and welcome development (after their deep fall in 2008-2009) – paving the way for an expansion of gross fixed capital formation. However, it is hard to identify any signs of upcoming sustained expansion of fixed investment outside some selected segments of infrastructure (supported by EU funds). The overall investment stagnation is reflected e.g. in the fact that the output of the construction sector keeps contracting at accelerating speed. Worse still, much of the infrastructure investment which moderated the scale of the decline in the total level of gross fixed capital investment in 2010 is unlikely to get government backing of a comparable magnitude.[54] All in all, a further strong rise in inventories in 2011 may not occur if the return of proper pro-investment sentiments is postponed.

The return of such sentiments cannot now be predicted with any degree of certainty. Although in some sectors (e.g. industry) the business confidence indicator has returned to its pre-crisis levels, in other sectors that indicator either hovers at much depressed levels (in services) or continues a free fall (in construction). The latter fact may have something to do with the levels of interest rates (and fees) charged by banks on new housing loans to households (on average in excess of 6% p.a.). The fact that the interest rates on loans to business are reasonably low does not seem to matter: lending to business (at least from the domestic banks) keeps contracting. What seems to be missing to activate an expansion in the private sector (corporate) investment is the prospect of sustainably strengthening domestic (but also external) demand. Firms still name insufficient demand as the main worry. Besides, some segments of the business sector that could need external financing are cut off from borrowing because they are unable to service their debt obligations. Non-performing loans

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[54] 2009-2010 has seen a genuine government-sponsored investment boom in the solar power-plants sector. These investments inflated the rate of growth of fixed capital formation (contributing to the 2010 GDP growth). At the same time the requisite imports of solar panels lowered the trade surplus by about 1% of the GDP (thereby reducing foreign trade's GDP growth contribution). The net GDP growth effect of the solar energy project may be positive but small – and the environmental impacts problematic. Given its unexpected scale, the project's wisdom is now questioned. New capacities imply steep rises in electricity prices and extra costs of public investment and subsidy into the transmission grids. No wonder the government has recently taken steps to stop the boom.

account for 9% of the stock of loans to the corporate non-financial sector. (This does not endanger the stability of the banking system whose capital/assets ratio is 15.5%, very high by all standards.)

In contrast to investment by the government, it looks as if its consumption stagnated in 2010. Moreover, government consumption is to contract strongly in 2011-2012 (by 3.5% and 2.7% respectively). Cuts in government consumption are part of the fiscal consolidation plan of the centre-right coalition government of Petr Nečas whereby the deficit is to fall from 4.8% of the GDP (recently envisaged for 2010) to below 3% in 2013 (with the governmental debt/GDP ratio rising from the 2010 38.9% mark to the maximum of 44% in 2013). That the cuts in government consumption will slow down the overall GDP growth is quite obvious. Moreover, the envisaged fiscal tightening is also affecting various social security/health benefit schemes which face reforms. In addition the government has raised effective income taxation (e.g. by reducing some allowed tax deductions and by taxing the incomes of employed pensioners). All in all, the fiscal consolidation will slow down GDP growth both directly and indirectly.

Household consumption has risen by about 1% in 2010 – and that despite the slightly falling wage bill and the whole sector's stagnant real disposable income. The 'discrepancy' between disposable income and consumption is due to households' gross saving rate falling consecutively since 2007 when it stood at 10.9% to approximately 8.7% in 2010. Saving rates are likely to go down further in the future (also because the interest rates on household bank deposits will stay negative). Thus household consumption is likely to grow in 2011, if not very spectacularly, even if the wage increases remain subdued and employment stagnates. Of course, growth in employment, wages and household income could speed up more significantly if there is progress on fixed investment and/or net exports. Otherwise, some fiscal relaxation (intended or otherwise) may help – especially in 2012 and beyond. The demographic developments may support the acceleration of private consumption, even if indirectly: the Czech population aged 15-64 years has just started falling very fast (from a peak in 2009). The loss of manpower may be even bigger on account of the imminent opening of the German and Austrian labour markets to Czech (and most other NMS) nationals. This may favour a stronger rise in wages, incomes – and eventually in household consumption demand.

In real terms the imports of goods and services rose definitely faster than exports in 2010, resulting in a reduced (but still very large) trade surplus. The contribution of foreign trade to GDP growth was positive but rather small. These tendencies are likely to prevail also in 2011-2013 especially if (i) growth slows down in the main Czech export destinations (euro area first of all); (ii) the business sector's fixed investment happens to stagnate; (iii) the domestic currency strengthens unduly.

Throughout 2010 the consecutive international financial crises in the euro area (also the events in Hungary) coincided with sharply changing sentiments concerning the Czech currency (and also the country's long-term treasury bonds). More recently the Czech currency is strengthening again – amid the return of high net financial inflows. These inflows over-compensate the current account deficits that arise primarily due to high (and rising) profits of the foreign-owned sector. The financial inflows include FDI (primarily in the form of reinvested profits) as well as very large portfolio investment targeting first of all treasury bonds (which prove attractive despite fairly low yields). The appreciation pressures due to high inflows of FDI and portfolio capital are moderated somewhat via quite high external lending by (nominally) Czech banks and non-financial firms.

Under Miroslav Singer, the new Governor of the Czech National Bank, the monetary policy is likely to remain relatively relaxed. The traditionally cautious CNB will not rush to raise its policy rates in response to the currently higher (and still rising) inflation as the latter is acknowledged to represent primarily the effects of the hikes in indirect tax rates and in administered (regulated) prices. Also, the CNB is unlikely to alter its reservations concerning the switch-over to the euro.

Summing up, the GDP growth speed-up experienced by the Czech economy last year will not continue in 2011. Growth of consumption and gross fixed investment will be anaemic at best and there are many unknowns as concerns foreign trade developments. Given the circumstances the monetary policy seems to be doing its best. But this is not the case with the fiscal policy which seems to have been led by unreasonable consolidation objectives. But, given the political realities, this policy may be sufficiently modified later on, possibly stimulating growth in 2012 and beyond.

Table CZ

Czech Republic: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 1)	2011	2012 Forecast	2013
Population, th pers., average	10235.8	10269.1	10334.2	10424.3	10487.2	10514.0	10540	10580	10610
Gross domestic product, CZK bn, nom.	2983.9	3222.4	3535.5	3689.0	3625.9	3690	3800	3970	4200
annual change in % (real)	6.3	6.8	6.1	2.5	-4.2	2.3	2.2	2.5	3.7
GDP/capita (EUR at exchange rate)	9800	11100	12300	14200	13100	13900	.	.	.
GDP/capita (EUR at PPP)	17100	18200	19900	20200	19300	19900	.	.	.
Consumption of households, CZK bn, nom.	1442.7	1537.2	1659.6	1804.2	1804.3	1850	.	.	.
annual change in % (real)	2.5	5.1	4.8	3.6	-0.3	1	1	2.5	3
Gross fixed capital form., CZK bn, nom.	741.9	796.3	890.3	883.2	814.0	800	.	.	.
annual change in % (real)	1.8	6.0	10.8	-1.5	-7.9	-1	2	4	6
Gross industrial production									
annual change in % (real)	3.9	8.3	10.6	-1.9	-13.6	10.6	6	7	8
Gross agricultural production									
annual change in % (real)	-2.0	-4.2	3.1	6.8	-3.5	-4.4	.	.	.
Construction industry									
annual change in % (real)	5.3	6.1	7.0	-0.2	-0.8	-7.8	.	.	.
Employed persons - LFS, th, average	4764.0	4828.1	4922.0	5002.5	4934.3	4885.3	4890	4910	4930
annual change in %	1.2	1.3	1.9	1.6	-1.4	-1.0	0	0.5	0.5
Unemployed persons - LFS, th, average	410.2	371.7	276.6	229.8	352.2	383.7	.	.	.
Unemployment rate - LFS, in %, average	7.9	7.2	5.3	4.4	6.7	7.3	7.5	7.0	6.5
Reg. unemployment rate, in %, end of period	8.9	7.7	6.0	6.0	9.2	9.8	.	.	.
Average gross monthly wages, CZK 2)	18344	19546	20957	22593	23488	24000	.	.	.
annual change in % (real, gross)	3.1	4.0	4.3	1.4	2.9	1	0.8	1.5	2
Consumer prices (HICP), % p.a.	1.6	2.1	2.9	6.3	0.6	1.2	2.0	2.0	2.0
Producer prices in industry, % p.a.	0.5	0.1	2.6	0.4	-1.5	0	2.2	.	.
General governm. budget, EU-def., % GDP									
Revenues	41.4	41.1	41.8	40.2	40.2	40.7	.	.	.
Expenditures	45.0	43.8	42.5	42.9	46.0	45.5	.	.	.
Net lending (+) / net borrowing (-)	-3.6	-2.6	-0.7	-2.7	-5.8	-4.8	-4.6	-3.5	-3.5
Public debt, EU-def., in % of GDP	29.7	29.4	29.0	30.0	35.3	38.9	42.1	43.0	44.0
Central bank policy rate, % p.a., end of period 3)	2.00	2.50	3.50	2.25	1.00	0.75	1.5	2.0	2.0
Current account, EUR mn	-1346	-2745	-4090	-962	-1465	-4000	-3800	-5000	-5200
Current account in % of GDP	-1.3	-2.4	-3.2	-0.7	-1.1	-2.7	-2	-3	-3
Exports of goods, BOP, EUR mn	62781	75706	89379	99158	80675	96000	108000	119000	129000
annual growth rate in %	16.1	20.6	18.1	10.9	-18.6	19	13	10	8
Imports of goods, BOP, EUR mn	60797	73415	85038	95031	73842	89300	102000	114000	123000
annual growth rate in %	11.5	20.8	15.8	11.8	-22.3	21	14	12	8
Exports of services, BOP, EUR mn	9491	11086	12311	14849	14575	16600	18000	20000	22000
annual growth rate in %	22.3	16.8	11.0	20.6	-1.8	14	11	12	10
Imports of services, BOP, EUR mn	8254	9494	10526	12210	13578	15900	18000	20000	22000
annual growth rate in %	13.9	15.0	10.9	16.0	11.2	17	12	12	10
FDI inflow, EUR mn	9354	4363	7667	4467	1935	6000	.	.	.
FDI outflow, EUR mn	-12	1172	1187	2964	960	600	.	.	.
Gross reserves of NB excl. gold, EUR mn	24868	23684	23456	26377	28556	31250	.	.	.
Gross external debt, EUR mn	39379	43415	51642	59689	60069	66500	.	.	.
Gross external debt in % of GDP	38.3	37.0	38.9	43.5	43.9	45.2	.	.	.
Average exchange rate CZK/EUR	29.78	28.34	27.77	24.95	26.44	25.28	24.5	24	24
Purchasing power parity CZK/EUR	17.10	17.23	17.17	17.54	17.94	17.67	.	.	.

Note: Gross industrial production, construction output and producer price index refer to NACE Rev. 2.

1) Preliminary and wiiw estimates. - 2) Enterprises with 20 and more employees, including part of the Ministry of Defence and the Ministry of the Interior. From 2009 all enterprises covered. - 3) Two-week repo rate.

Source: wiiw Database incorporating Eurostat and national statistics. Forecasts by wiiw.

Sándor Richter

Hungary: Gradual recovery amidst persistent uncertainties

The Hungarian economy shows clear signs of a modest recovery from the severe recession. In 2010 GDP growth accelerated from quarter to quarter, the annual growth rate is estimated to have surpassed 1%, a result which compares positively with the country's past performance but lags behind both the EU-15 average and the performance of Hungary's peers in the region.

The recovery has been driven by the robust export-based expansion of the manufacturing industry. Agriculture and construction still reported declines last year, services must have closed with zero growth. In manufacturing domestic sales still declined in 2010 while sales abroad increased by about 16%. The 'flagship' industrial clusters – computers, electronic and optical equipment and transport equipment – have been the engine of the expansion. The recovery has been 'jobless' so far, employment in industry even dropped last year while productivity improved considerably.

Prime Minister Orbán outlined ambitious goals for the economy when he took over office nine months ago: stimulation of growth through radical tax cuts, more and cheaper credits, focused national and EU co-financed support for the predominantly domestic-owned SME sector. The government reckons with 1 million new jobs within ten years, an accordingly elevated wage bill and consequently additional tax revenues. A new growth path (5-7% annually), substantially higher than the one that characterized the last decade, a reinforced middle class and a handful well-positioned Fidesz-friendly industrialists and bankers as well as a substantial reduction of the number of social transfer recipients would be the outcome of this policy. Yet the key problem of the Hungarian economy beyond the slow growth, namely the outstanding reforms of the inefficient and wasteful redistribution systems in the public sector, the main cause of the country's structural fiscal deficit, was completely ignored in the original programme.

A precondition for the good start of a programme such as this is the existence of a leeway in fiscal policy, since the initial budget deficit will grow due to tax reduction. The hoped-for positive impact on growth with newly generated additional revenues for the budget appears only with a time lag. Right after its inauguration the Orbán government made serious efforts to sell the idea of a 6-7% fiscal deficit (relative to the GDP) for 2010 instead of a less than 4% one as prescribed in the country's convergence programme and the stand-by agreement with the IMF and the EU. This attempt, with regard to Hungary's miserable pre-2006 track record concerning fiscal deficits, coupled with the Europe-wide panic last summer caused by the developments in Greece, did not have the smallest chance to come through with the EU or the IMF. At that point the government had two options: (a) either to retreat from the central element of its programme, postpone the radical tax reduction plans and focus the efforts on other components of the programme while continuing the fiscal consolidation launched by the previous governments in 2006-2009; or (b) to push through the tax reduction while observing the deficit targets of the convergence programme. This option necessitates the raising of new resources to make up for the gap emerging on the revenue side of the budget due to the radical tax reduction. Orbán's government decided for option (b); this decision has determined the developments since then.

In early 2011 the radical tax reduction is reality: the personal income tax with its 16% rate became 'flat' (earlier there had been two rates, 17% and 32%). The corporate tax rate for the SME sector was cut from 19% to 10%. Some other minor taxes were reduced as well. The other side of the coin: first, financial institutions were charged with a temporary levy, then specific temporary taxes were introduced for the largest (predominantly foreign-owned) firms of the energy, telecommunications and retail trade sectors. As a next step, 14 months' employee contributions to private pension funds (the second pillar of the pension system) were re-channelled to the central budget in order to cover current expenditures. Finally, the quasi nationalization of the accumulated private pension fund savings (about EUR 11 billion) was announced, with 26% of this sum to finance current budget expenditures this and the next year.

Leaving aside all the political and legal (Hungarian and EU) concerns – which are far from irrelevant – the main economic problem of this construction is that these elements of the fiscal revenues all are temporary. The taxes on the financial institutions and the other three sectors were promised to phase out from 2013 onwards. That part of the savings accumulated in the private pension funds which will not be re-channelled to the budget is planned to be used for the reduction of the public debt, therefore no further resources will be available from this segment. In contrast, the revenue-diminishing effects of the tax reduction remain, raising the danger of severe fiscal imbalances in the medium run.

The uncertainties about the medium-run fiscal outlook resulted in a downgrading of Hungary's sovereign debt to a level that is just one category better than 'junk'. The abolishment of the independent Fiscal Council critical to the government's fiscal policy did not reinforce confidence either. As a successful rolling-over of public debt is highly dependent on the sufficient purchase of government securities by international financial investors and the interest paid on public debt is of macroeconomic magnitude, it is no wonder that the government announced the elaboration of a fiscal consolidation programme to be presented in March this year. (See a first review of the programme at the end of this country report.) Should this programme leave the rating agencies and potential foreign buyers of Hungarian bonds unsatisfied, a major disruption in external financing of the public debt cannot be excluded.

The other pillar of Orbán's new economic policy, namely providing cheap and abundant credits for firms and households, faces resistance on the part of the (still) independent central bank. The Monetary Council, after a two-year long interest cutting cycle, raised the policy rate in three steps from 5.25% to 6% within a two-month interval (between 30 November 2010 and 25 January 2011). These decisions were explained by the higher than targeted inflation in 2010 (4.9%) caused by cost shocks through high prices of unprocessed food and oil, respectively, and the risk that inflationary expectations remain unanchored due to a prolonged period of above-target inflation. In March 2011 four of the currently seven members of the Monetary Council will be replaced by persons delegated by the Fidesz-dominated parliament. After this change, supporters of a cautious monetary policy may become a minority and, theoretically, this opens up the way for a monetary policy less dismissive towards the government's effort to enforce lower interest rates.

In recent months the forint has remained weaker as compared to the pre-crisis level. The real problem, however, is the appreciation of the Swiss franc, as in December 2010 over 60% of the foreign currency housing and consumer loans (stocks) was denominated in CHF. This is a serious concern for the households involved, as servicing of the debt requires a remarkably higher share of disposable incomes than before. Delayed payment and non-performance have been on the rise, causing problems both for the households which are in ever growing numbers qualified as not creditworthy and the lending financial institutions which face the challenge of a deteriorating quality of their credit portfolio.

In 2011 the Hungarian economy will finally leave recession behind. Household consumption will increase at a very moderate pace as the income tax reduction favours primarily well-to-do families whose motivation to increase consumption is limited, and about 60% of the households will have equal or less net income as compared to the situation prior to the tax reform. Further, higher debt service obligations of households indebted in foreign currency will pose a drag on the recovery of consumption. Investment will recover at a faster pace than consumption but from very low levels. This will be partly the result of huge investment projects in the automotive sectors, as Daimler-Benz, Audi and Opel are in the process of a remarkable extension of their production capacities in Hungary. However, FDI inflows this year will substantially lag behind the pre-crisis level and, more importantly, the respective figures in the Czech Republic, Poland and Slovakia. This relatively poor performance is, without doubt, at least partly the consequence of the new specific taxes. These policies, together with the related rhetoric, as well as the uncertainties concerning the phasing-out of these taxes, may all have played a role. It must be added that the treatment of the private pension funds, the curtailment of rights of the Constitutional Court with regard to public finance, how severance payments in the public sector were retroactively taxed, have all weakened confidence in the legal stability. Another channel for foreign resources will, however, gain importance: increased (compared to 2010) transfers from the budget of the European Union will help fixed investment recovery.

The highest contribution to GDP growth will again come from net exports in 2011. The extent of this contribution will be smaller than in the past two years as the gap between export and import growth rates has started to close in the wake of gradually recovering investment and, to a smaller extent, consumption. As a consequence, the exceptional situation in 2010 when Hungary closed the year with a current account surplus will not be repeated in the coming years. The outlook for 2012 and 2013 is extremely uncertain. While inertia alone would help the economy achieve a gradual acceleration of the current export-driven growth, uncertainties concerning the medium-run fiscal sustainability, the future monetary policy, and the country's attractiveness for foreign investors make the baseline scenario (displayed in detail in the country table) less robust than it usually is.

* * *

On 1 March the Hungarian government announced its long-awaited plan for the fiscal consolidation in 2012-2013. This programme is a radical departure from the original Fidesz credo for an acceleration of economic growth without any regard to its price in terms of fiscal deficit and debt. From now on the new 'enemy of the people' is high public debt and the programme is set out to radically reduce it in the coming years.[55]

One component of the programme is a retreat from earlier planned measures: the extension of the 10% preferential corporate income tax rate for large enterprises was discarded, the phasing-out of the bank levy in 2012 was postponed. A central element of the programme is to decrease the number of social transfer recipients: unemployment benefits will be provided for a shorter period, disability qualifications will be revised, access to early retirement will be abolished. The people dropping out from the here mentioned social transfer schemes are intended to be absorbed by public works programmes – whose details have yet to be elaborated. State support for pharmaceutical products will be cut, but it is not clear how the increased burdens will be shared between producers and consumers. The Hungarian Railway Company's debt will be consolidated and the company reorganized so that it can cope without subsidies in the future; the details are nevertheless again unknown. Further elements of the programme are merely vague plans: freezing overhead charges of households, cost reduction coupled with reforms in the education system, cuts in various segments of public expenditures. Compared with the baseline 2011 budget, the country's fiscal stance is envisaged to improve by 2% of GDP in 2012 and by an additional 1% in 2013. Public debt is expected to drop from around 80% in 2010 to around 69% by the end of 2013.[56]

All in all, the government programme is a resolute step towards addressing Hungary's medium-run fiscal problems. Despite its many unclear details it will be sufficient to maintain a central government deficit of around 3% of GDP in 2012 and 2013. The government's goal for those years (2.5% and 2.2% deficit, respectively) seems overambitious, as the underlying assumption of a GDP growth rate of 4% or more is unrealistic. The current state of the economy and the unavoidable fiscal consolidation will probably not allow for GDP growth higher than 3% in any of the two years.

55 This approach is practically identical with that of the second Gyurcsány and the Bajnai governments (summer 2006 to spring 2010) mercilessly attacked by the then opposition Fidesz.

56 According to the Hungarian methodology, which is not identical with the Eurostat methodology used in the country table attached to this report.

Table HU

Hungary: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 1)	2011	2012 Forecast	2013
Population, th pers., average	10087.1	10071.4	10055.8	10038.2	10022.0	10003	10002	10000	9998
Gross domestic product, HUF bn, nom.	21970.8	23730.0	25321.5	26753.9	26054.3	27400	28900	30700	32600
annual change in % (real)	3.1	3.6	0.7	0.9	-6.7	1.2	2.5	3	3
GDP/capita (EUR at exchange rate)	8800	8900	10000	10600	9300	9900	.	.	.
GDP/capita (EUR at PPP)	14200	14900	15500	16200	15300	15600	.	.	.
Consumption of households, HUF bn, nom.	11825.2	12495.5	13306.0	14091.9	13487.9	13700	.	.	.
annual change in % (real)	3.2	2.1	0.2	0.5	-8.1	-2	0.5	1.5	2.5
Gross fixed capital form., HUF bn, nom.	5065.9	5182.9	5408.3	5727.3	5441.6	5500	.	.	.
annual change in % (real)	6.5	-3.5	3.7	3.2	-9.3	-3	5	7	8
Gross industrial production									
annual change in % (real)	6.8	9.9	7.9	-0.2	-17.6	10.4	12	12	12
Gross agricultural production									
annual change in % (real)	-7.3	-3.0	-12.5	27.7	-10.1	-5.6	.	.	.
Construction industry									
annual change in % (real)	15.7	-0.7	-14.0	-5.2	-4.3	-8	5	10	10
Employed persons - LFS, th, average	3901.5	3930.0	3926.2	3879.4	3781.8	3780	3820	3860	3900
annual change in %	0.0	0.7	-0.1	-1.2	-2.5	0	1	1	1
Unemployed persons - LFS, th, average	302.2	316.7	312.0	329.1	420.7	480	.	.	.
Unemployment rate - LFS, in %, average	7.2	7.5	7.4	7.8	10.0	11	10.5	9.3	8.5
Reg. unemployment rate, in %, end of period	9.3	9.1	10.1	10.9	13.6	13.3	.	.	.
Average gross monthly wages, HUF 2)	158343	171351	185018	198741	199837	204000	.	.	.
annual change in % (real, net)	6.3	3.6	-4.6	0.8	-2.3	2.5	.	.	.
Consumer prices (HICP), % p.a.	3.5	4.0	7.9	6.0	4.0	4.7	3.9	3.5	3.5
Producer prices in industry, % p.a.	3.1	6.6	0.3	4.6	4.5	6.3	.	.	.
General governm.budget, EU-def., % GDP									
Revenues	42.3	42.6	45.0	45.1	46.1	46	.	.	.
Expenditures	50.2	52.0	50.0	48.8	50.5	50	.	.	.
Net lending (+) / net borrowing (-)	-7.9	-9.4	-5.0	-3.7	-4.4	-4	-3	-3	-3
Public debt, EU-def., in % of GDP	61.8	65.7	66.1	72.3	78.4	78.5	74	73	72
Central bank policy rate, % p.a., end of period 3)	6.00	8.00	7.50	10.00	6.25	5.75	.	.	.
Current account, EUR mn	-6710	-6829	-6965	-7747	-404	800	-1700	-2400	-2800
Current account in % of GDP	-7.6	-7.6	-6.9	-7.3	-0.4	0.8	-1.6	-2.1	-2.4
Exports of goods, BOP, EUR mn	49671	58378	68362	72684	58414	70700	78100	85900	94500
annual growth rate in %	11.6	17.5	17.1	6.3	-19.6	21	10.5	10	10
Imports of goods, BOP, EUR mn	52212	60840	68500	73233	55033	65500	71900	78400	85800
annual growth rate in %	9.6	16.5	12.6	6.9	-24.9	19	9.7	9	9.5
Exports of services, BOP, EUR mn	10351	10876	12574	13804	13285	14200	15300	16800	18500
annual growth rate in %	19.4	5.1	15.6	9.8	-3.8	7	8	10	10
Imports of services, BOP, EUR mn	9219	9643	11524	12843	11920	11900	12900	14200	15600
annual growth rate in %	12.6	4.6	19.5	11.4	-7.2	0	8	10	10
FDI inflow, EUR mn	6172	5468	2861	4926	1549	600	2000	.	.
FDI outflow, EUR mn	1756	3118	2646	2084	1726	800	1500	.	.
Gross reserves of NB, excl. gold, EUR mn	15670	16384	16305	23807	30648	33570	.	.	.
Gross external debt, EUR mn	71770	86681	103988	123537	135802	136000	.	.	.
Gross external debt, in % of GDP	82.6	92.0	104.2	123.1	140.9	138.0	.	.	.
Average exchange rate HUF/EUR	248.05	264.26	251.35	251.51	280.33	275.48	280	275	275
Purchasing power parity HUF/EUR	153.56	157.75	161.71	165.00	170.11	175.13	.	.	.

Note: Gross industrial production, construction output and producer prices refer to NACE Rev. 2.

1) Preliminary and wiiw estimates. - 2) Enterprises with 5 and more employees. - 3) Base rate (two-week NB bill).

Source: wiiw Database incorporating Eurostat and national statistics. Forecasts by wiiw.

Sebastian Leitner

Baltic States:
Exports trigger broader based economic upswing

Estonia

In the second half of 2010, external demand gave a boost to overall economic activity in Estonia. Exports to the most important trading partners – Finland and Sweden – have risen by almost 60% nominally in the respective period year-on-year, while trade with other western European countries revived slowly in comparison. Trade with Scandinavia has benefited from the effects of the stimulus packages of public households, a stable household demand and a substantial rebound of trade in the region. Alike, the strong recovery in Russia has led to a 50% increase of Estonian exports. Simultaneously imports also picked up, although less than exports, due to the vivid process of restocking which has been the most important driver of GDP growth in 2010.

Household consumption, having dropped substantially in the two year period before, stabilized in the second half of 2010, and even showed some signs of upswing in the fourth quarter of the year. In the past four months of 2010 retail sales started to grow again compared to the respective period of 2009. At the same time investment activity of private and public actors was still on decline. Both enterprises and households are still in the process of deleveraging according to loan statistics.

After the unemployment rate climbed to almost 20% in the first quarter of 2010, affected not only by the economic slump but also by the introduction of the new, more liberal labour law at the beginning of 2010, the situation on the Estonian labour market ameliorated remarkably throughout the year. Up to the fourth quarter of 2010 the unemployment rate dropped to about 13.6%. An upswing in employment was mainly driven by manufacturing while a further reduction was to be observed in transport, education and health sectors.

The Estonian government kept track of the foreseen consolidation path. Although revenues fell nominally throughout the year, the budget deficit has been expected to be reduced to only 1.3% of GDP. With the upswing of the economy, rising government income should allow keeping the deficit low even when temporary expenditure reducing measures, introduced in the past two years, phase out.

For 2011 we expect the revival of economic activity to become stronger and broader based. The growth drivers of 2010, the building up of inventories and export activity, will still play an important role. However, after a long period of decline an upswing in gross fixed investments is to be expected, which should be the main trigger in GDP growth. Survey figures show, that the average degree of capacity utilization in industrial sectors rose substantially up to the end of 2010. Investments in replacements and expansion will therefore be necessary. At the same time investments in housing have reached a low. Although construction activity will remain sluggish for a longer period, overall investments will start to rise in 2011. An increase in employment and a slight rebound in wages shall help household demand to give an additional, however still small impulse. One effect of rising domestic demand will be a decline in the current account surplus. Nevertheless, the balance shall remain positive throughout the year.

In 2012 and 2013 we expect economic activity grow by 4% and 4.5%, respectively. The assumption is that the medium-term deleveraging process of households and enterprises will soon come to an end and allow private consumption to increase again more swiftly. However, the range of future GDP growth rates will in the forecast period be substantially below the pre-crisis levels. These high growth rates were caused by excessive inflows of foreign capital, blowing up subsequently real estate and consumption bubbles. In the medium-term unemployment will also remain high, since employment, having had losses in non-tradable services and construction will not be reshuffled swiftly to the tradable goods and services sectors.

No spectacular short and medium term effects are to be expected from Estonia's accession to the euro zone. The swift rise of capital inflows that could be observed in Slovenia and Slovakia after their accession to the euro zone has already happened in Estonia in the pre-crisis years and households nowadays need to deleverage. Besides, after the years of Estonia's currency board regime, the switch to euro was largely a technical – albeit highly symbolic – step. Nevertheless, the step may support a further deepening of production linkages to European, particularly Scandinavian, enterprises and thereby attract additional FDI inflows.

Latvia

Robust external demand lifted the Latvian economy out of it's through in the second half of 2010. While exports of goods rose by about 36% and services by 4% nominally year-on-year, also overall industrial production increased by more than 17% in real terms in the same period. Simultaneously, formerly depleted inventories were accumulated again. Thus, gross capital formation contributed positively to the GDP revival in the second half of 2010, although fixed investments were still declining. The process of restocking also effected a revival of imports. However, the current account balance still shows a substantial surplus for the year 2010. Due to the economic revival in the second half of the year GDP decline for 2010 as a whole turned out to be much less dramatic than previously expected.

Also the rebound of household consumption in the past few months was somewhat surprising. Although net monthly wages declined by another 6% in real terms throughout the year, consumption only decreased by about 1.5%, after having collapsed by 24% in 2009. Retail figures of the fourth quarter 2010 show that Latvian consumers start to spend again, especially on non-food items.

The economic upswing allowed the Latvian government to reduce the budget deficit in 2010 to 8% of GDP, slightly below the agreed ceiling fixed in the rescue package agreements with the IMF and the

EU. The budget approved for 2011 foresees consolidation measures of 2% of GDP. In January 2011 the VAT tax rate was raised from 21% to 22% (the reduced rate from 10% to 12%), while further provisions on the revenue side include inter alia the increase of social security contributions from 33% to 35% of salaries and higher real estate taxes. At the same time, the flat tax levied on personal income was lowered by one percentage point to 25%. One third of the consolidation resources are to be obtained via expenditure reductions, cutting e.g. public investments in road infrastructure, family transfers and health expenses. Stronger growth of domestic demand this year should make it possible to reduce the deficit well below the target of 6% of GDP. Although we expect that economic growth will facilitate the Latvian government to further consolidate the public household, the aim to reduce the deficit to 3% of GDP in 2012 might be too ambitious. Since public expenditures have already been cut to the maximum, the target would require another round of unpopular tax hikes. Therefore we expect the Maastricht deficit criteria to be attained later, possibly in 2013. However, the level of public debt, although having risen substantially due to the economic collapse and the need to nationalize, the collapsed Parex Bank should remain below the marker of 60% of GDP.

Towards the end of the last year the situation on the labour market has not improved. Although official figures state that emigration has picked up in 2009 and 2010 to on average 0.4% of the population annually, the unemployment rate has not declined and amounted to about 17% of the labour force by the end of 2010. We expect an improvement of the labour market situation to happen only gradually and only to some extent via a rise in employment. Part of the reduction in unemployment will again take place via emigration.

With the end of the depression period consumer prices picked up slightly in the past four months of 2010. Due to rising prices of imported goods, electricity tariffs and the above mentioned tax hikes, we expect consumer prices to increase more swiftly in 2011, although with 3% annually still quite moderately.

For 2011, we expect GDP to grow again by 2.8% in real terms, after three years of decline by cumulated more than 20%. External demand will again contribute positively to the revival of overall economic activity, although the momentum is likely to weaken. However, domestic demand shall start to rise again. Gross fixed investments, especially in industrial sectors, as well as the process of re-stocking are expected to act as the main growth drivers this year. The financial situation of indebted households and high unemployment will allow private consumption to increase only slightly, while the consolidation measures of the government will further reduce public consumption. For the years 2012 and 2013 GDP growth is likely to pick up further to 3.5% and 3.8% in real terms. A slight amelioration of the labour market situation and some revival of real incomes should allow households to expand consumption more swiftly again.

Lithuania

During 2010, the economic activity picked up slightly already in the second and third quarters, but with a surprisingly strong dynamism the annual GDP growth accelerated to 4.6% compared to the same period of 2009 in the fourth quarter. Again, one of the strongest drivers of growth was the revival in exports. However, these were not only driven by the upswing of demand in the EU countries, but much more so by Lithuania's easternmost neighbours. Exports to Russia, Ukraine and Belarus grew by almost 55% nominally throughout 2010. About 30% of the upswing in trade is due to rising exports of mineral fuels triggered also by the rebound of oil prices, while also the chemical industry, entrepreneurs in the automotive sector and furniture production benefited strongly from higher external demand.

Household demand picked up strongly in the fourth quarter of last year and retail sales grew by 8.5% year-on-year in the same period. However, real wages remain depressed. The upswing of nominal wages, which took place in the second half of 2010, was accompanied by the revival of inflation. Consumer prices rose by 3% in the fourth quarter of 2010 year-on-year, which kept the purchasing power of households unchanged. Nevertheless, compared to its Baltic neighbours Lithuanian households are less indebted, which makes a stronger upswing of consumer demand in the country in 2011 and thereafter more likely.

Also gross fixed capital formation grew again already in the third quarter of 2010. Credit market figures showed a slight upswing in new loans to the non-financial corporate sector and households respectively. Obviously, also in Lithuania the rebuilding of inventories was the main driver of domestic demand in 2010. Although the impact of this effect will diminish in 2011, inventories should still grow faster than gross fixed capital formation.

The budget plan for 2011 foresees to trim down the public deficit to 5.8% of GDP. On the expenditure side the government inter alia extended temporary consolidation measures to the end of 2011, e.g. the reduction of wages of public employees or the reduction of transfers to the second pillar pension funds. Finance minister Simonyte expects a swift rise in tax revenues due to the economic revival and the enhancement of tax compliance. Furthermore, the restructuring of state-owned enterprises is awaited to raise the government income. However, the plans how to reach the latter two goals are far from elaborated in detail. It may therefore well be necessary to approve a supplementary budget in the course of the year, should the aim to reduce the deficit to below 6% of GDP be kept on the agenda.

Although economic activity revived already in the second quarter of 2010, the reduction of unemployment was so far meagre. Registered unemployment peaked in August 2010 and fell by only one percentage point till December. In the coming three years an amelioration of the situation in the labour market will take place only gradually, whereby emigration will again play a role in reducing unemployment figures.

In 2011 we expect economic growth to accelerate to 3%. Still, gross capital formation will be the strongest driver of the upswing. However, also a slight increase of household consumption will back up domestic demand. In spite of a decreasing drive of exports and the move of the current account into deficit, we still expect a positive contribution of trade to overall growth. In 2012 and 2013 we expect a further pickup of economic activity to 3.6% and 3.8% in real terms, when domestic demand shall regain momentum due to rising wages and a revival of lending activity.

Table EE

Estonia: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 1)	2011	2012	2013
								Forecast	
Population, th pers., average	1346.1	1343.5	1341.7	1340.7	1340.3	1340.1	1339	1338	1338
Gross domestic product, EUR mn, nom.	11182	13391	15827	16107	13861	14700	16000	17200	18800
annual change, % (real)	9.4	10.5	6.9	-5.0	-13.9	3.1	4.5	4	4.5
GDP/capita (EUR at exchange rate)	8300	10000	11800	12000	10300	10900	.	.	.
GDP/capita (EUR at PPP)	13800	15600	17400	17000	15000	15600	.	.	.
Consumption of households, EUR mn, nom.	6070	7254	8470	8690	6993	7100	.	.	.
annual change in % (real)	9.9	13.8	8.6	-5.5	-18.8	-1.3	0.5	1	1.5
Gross fixed capital form., EUR mn, nom.	3586	4817	5452	4610	2991	2830	.	.	.
annual change in % (real)	15.3	23.2	6.0	-15.0	-32.9	-8	7	8	10
Gross industrial production									
annual change in % (real)	11.0	9.9	6.4	-5.2	-26.0	22.8	18	15	15
Gross agricultural production									
annual change in % (real)	7.2	-2.1	12.5	-1.2	2.8	-1.4	.	.	.
Construction industry									
annual change in % (real)	22.4	26.9	13.5	-13.3	-28.4	-13	.	.	.
Employed persons - LFS, th, average	607.4	646.3	655.3	656.5	595.8	570.9	595	610	620
annual change in %	2.0	6.4	1.4	0.2	-9.2	-4.2	4	3	2
Unemployed persons - LFS, th, average	52.2	40.5	32.0	38.4	95.1	115.9	.	.	.
Unemployment rate - LFS, in %, average	7.9	5.9	4.7	5.5	13.8	16.9	13.5	11.5	10
Reg. unemployment rate, in %, end of period	3.6	1.9	2.2	4.6	13.3	10.0	.	.	.
Average gross monthly wages, EUR	516	601	725	825	784	790	.	.	.
annual change in % (real, gross)	6.4	11.6	13.0	3.2	-4.9	-2.1	.	.	.
Consumer prices (HICP), % p.a.	4.1	4.5	6.7	10.6	0.2	2.7	4	3.5	4.5
Producer prices in industry, % p.a.	1.8	4.2	8.1	8.0	0.7	3.2	.	.	.
General governm. budget, EU-def., % GDP									
Revenues	35.2	36.0	36.9	37.0	43.4	41.5	.	.	.
Expenditures	33.6	33.6	34.4	39.9	45.2	42.8	.	.	.
Net lending (+) / net borrowing (-)	1.6	2.4	2.5	-2.9	-1.8	-1.3	-1.5	-1.0	-1.0
Public debt, EU-def., in % of GDP	4.6	4.4	3.7	4.6	7.2	8	9	8.5	7.5
Central bank policy rate, % p.a., end of period 2)	2.5	3.8	7.0	7.0	2.8	0.9	.	.	.
Current account, EUR mn	-1116	-2053	-2721	-1568	628	530	100	-300	-500
Current account in % of GDP	-10.0	-15.3	-17.2	-9.7	4.5	3.6	0.6	-1.7	-2.7
Exports of goods, BOP, EUR mn	6348	7774	8142	8539	6536	8750	10400	12300	14600
annual growth rate in %	33.2	22.5	4.7	4.9	-23.5	33.9	19	18	19
Imports of goods, BOP, EUR mn	7898	10078	10871	10664	7096	9000	10500	12400	14900
annual growth rate in %	24.7	27.6	7.9	-1.9	-33.5	26.8	17	18	20
Exports of services, BOP, EUR mn	2612	2871	3196	3513	3159	3400	3900	4350	4800
annual growth rate in %	13.9	9.9	11.3	9.9	-10.1	7.6	15	12	10
Imports of services, BOP, EUR mn	1773	1980	2245	2288	1814	2000	2250	2500	2800
annual growth rate in %	26.4	11.7	13.4	1.9	-20.7	10.3	13	11	12
FDI inflow, EUR mn	2307	1432	1992	1179	1209	1450	1800	.	.
FDI outflow, EUR mn	556	880	1276	760	1110	370	.	.	.
Gross reserves of NB excl. gold, EUR mn	1643.6	2115.3	2235.6	2814.0	2757.9	1914.0	.	.	.
Gross external debt, EUR mn	9671.9	12944.4	17350.5	19040.4	17389.5	16600	.	.	.
Gross external debt in % of GDP	86.5	96.7	109.6	118.2	125.5	112.9	.	.	.
Average exchange rate EUR/EUR	1.0000	1.0000	1.0000	1.0000	1.0000	1.0000	1	1	1
Purchasing power parity EUR/EUR	0.5995	0.6386	0.6833	0.7061	0.6903	0.7031	.	.	.

Notes: Estonia has introduced the Euro from 1 January 2011. Up to and including 2010 all time series in EKK as well as the exchange rates and PPP rates have been divided for statistical purposes by the conversion factor 15.6466 (EKK per EUR) to a kind of statistical EUR (euro-fixed). Gross industrial production, construction output and producer prices refer to NACE Rev. 2.

1) Preliminary and wiiw estimates. - 2) TALIBOR one-month interbank offered rate (Estonia has a currency board).

Source: wiiw Database incorporating Eurostat and national statistics. Forecasts by wiiw.

Table LV

Latvia: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 [1)]	2011	2012 Forecast	2013
Population, th pers., average	2300.5	2287.9	2276.1	2266.1	2254.8	2235	2220	2210	2200
Gross domestic product, LVL mn, nom.	9059.1	11171.7	14779.8	16188.2	13082.8	12900	13700	14600	15700
annual change in % (real)	10.6	12.2	10.0	-4.2	-18.0	-0.4	3.2	3.5	3.8
GDP/capita (EUR at exchange rate)	5700	7000	9300	10200	8200	8100	.	.	.
GDP/capita (EUR at PPP)	10900	12200	13900	14100	12200	12400	.	.	.
Consumption of households, LVL mn, nom.	5578.2	7184.2	9087.1	10052.4	7941.2	7700	.	.	.
annual change in % (real)	11.3	21.4	14.9	-5.3	-24.1	-1.5	1	2.2	2.2
Gross fixed capital form., LVL mn, nom.	2773.8	3644.1	4975.1	4748.5	2806.8	2200	.	.	.
annual change in % (real)	23.6	16.4	7.5	-13.5	-37.3	-20	8	8	9
Gross industrial production [2)]									
annual change in % (real)	7.1	6.5	1.1	-3.9	-16.2	14.3	12	9	8
Gross agricultural production									
annual change in % (real)	11.8	-1.9	10.8	0.2	-0.7	-1.7	.	.	.
Construction industry									
annual change in % (real)	15.5	13.3	13.6	-3.1	-34.9	-25	.	.	.
Employed persons - LFS, th, average	1033.7	1087.1	1118.0	1124.5	983.1	945	970	1020	1050
annual change in %	1.6	5.2	2.8	0.6	-12.6	-3.9	3	5	3
Unemployed persons - LFS, th, average	101.0	79.5	71.3	90.5	203.2	215	.	.	.
Unemployment rate - LFS, in %, average	8.9	6.8	6.0	7.5	17.1	18.5	17	15	13.5
Reg. unemployment rate, in %, end of period	7.4	6.5	4.9	7.0	16.0	14.3	.	.	.
Average gross monthly wages, LVL	246	302	398	479	461	443	.	.	.
annual change in % (real, net)	9.7	15.6	19.9	6.2	-5.6	-6	.	.	.
Consumer prices (HICP), % p.a.	6.9	6.6	10.1	15.2	3.3	-1.2	3	3	3.5
Producer prices in industry, % p.a.	8.0	10.3	16.1	11.4	-4.6	2.8	.	.	.
General government budget, EU-def., % GDP									
Revenues	35.2	37.7	35.4	34.6	33.7	37	.	.	.
Expenditures	35.6	38.1	35.7	38.8	43.9	45	.	.	.
Net lending (+) / net borrowing (-)	-0.4	-0.5	-0.3	-4.1	-10.2	-8	-5.5	-4	-3
Public debt, EU-def., in % of GDP	12.4	10.7	9.0	19.7	36.7	50	52	54	55
Central bank policy rate, % p.a., end of period [3)]	4.0	5.0	6.0	6.0	4.0	3.5	.	.	.
Current account, EUR mn	-1610	-3603	-4710	-3014	1598	820	400	-300	-600
Current account in % of GDP	-12.4	-22.5	-22.3	-13.1	8.6	4.5	2.1	-1.5	-2.7
Exports of goods, BOP, EUR mn	4165	4929	6020	6531	5253	6900	8200	9800	11900
annual growth rate in %	26.3	18.4	22.1	8.5	-19.6	31.4	19	20	21
Imports of goods, BOP, EUR mn	6643	9032	11074	10603	6575	8000	9300	11000	13300
annual growth rate in %	19.8	36.0	22.6	-4.3	-38.0	21.7	16	18	21
Exports of services, BOP, EUR mn	1743	2121	2707	3088	2747	2750	2800	3100	3500
annual growth rate in %	21.7	21.7	27.6	14.1	-11.0	0.1	2	11	13
Imports of services, BOP, EUR mn	1256	1586	1974	2169	1625	1600	1650	1800	2000
annual growth rate in %	32.5	26.3	24.5	9.9	-25.1	-1.5	3	9	11
FDI inflow, EUR mn	568	1339	1705	869	68	350	500	.	.
FDI outflow, EUR mn	103	136	270	169	-44	70	.	.	.
Gross reserves of NB excl. gold, EUR mn	1901.8	3346.2	3859.9	3514.0	4572.1	5700	.	.	.
Gross external debt, EUR mn	12807.7	18127.7	26834.6	29762.8	29159.4	28700	.	.	.
Gross external debt in % of GDP	98.4	113.1	126.4	130.2	158.1	157.8	.	.	.
Average exchange rate LVL/EUR	0.6962	0.6962	0.7001	0.7027	0.7057	0.7087	0.7087	0.7087	0.7087
Purchasing power parity LVL/EUR	0.3606	0.3999	0.4663	0.5057	0.4762	0.4668	.	.	.

Note: Gross industrial production, construction output and producer price index refer to NACE Rev. 2.

1) Preliminary and wiiw estimates. - 2) Enterprises with 20 and more employees. - 3) Refinancing rate of National Bank.

Source: wiiw Database incorporating Eurostat and national statistics. Forecasts by wiiw.

Table LT

Lithuania: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 1)	2011	2012	2013
								Forecast	
Population, th pers., average	3414.3	3394.1	3375.6	3358.1	3339.5	3286.5	3240	3210	3180
Gross domestic product, LTL mn, nom.	72060.4	82792.8	98669.1	111482.6	91525.9	95500	101200	107500	114400
annual change in % (real)	7.8	7.8	9.8	2.9	-14.7	1.3	2.9	3.6	3.8
GDP/capita (EUR at exchange rate)	6100	7100	8500	9600	7900	8400	.	.	.
GDP/capita (EUR at PPP)	11900	13100	14800	15300	12900	13400	.	.	.
Consumption of households, LTL mn, nom.	46312.0	53268.6	63508.4	73027.2	62814.5	61400	.	.	.
annual change in % (real)	12.3	10.6	12.0	3.7	-17.7	-3.4	1.5	2.5	3
Gross fixed capital form., LTL mn, nom.	16405.0	20840.8	27918.8	28370.0	15666.9	15100	.	.	.
annual change in % (real)	11.2	19.4	23.0	-5.2	-40.0	-5	7	8	8.5
Gross industrial production (sales)									
annual change in % (real)	7.1	6.5	2.4	5.5	-14.6	6.7	13	10	8
Gross agricultural production									
annual change in % (real)	10.5	-4.1	8.2	8.8	1.0	-5.0	.	.	.
Construction industry									
annual change in % (real)	9.9	21.7	22.2	4.0	-48.5	-7.7	.	.	.
Employed persons - LFS, th, average	1473.9	1499.0	1534.2	1520.0	1415.9	1345	1380	1420	1450
annual change in %	2.6	1.7	2.3	-0.9	-6.8	-5	2.6	2.9	2.1
Unemployed persons - LFS, th, average	133.0	89.4	69.0	94.3	225.1	290	.	.	.
Unemployment rate - LFS, in %, average	8.3	5.6	4.3	5.8	13.7	17.8	16	14.5	13
Reg. unemployment rate, in %, end of period 2)	4.1	3.7	3.3	4.4	12.5	14.4	.	.	.
Average gross monthly wages, LTL	1276.2	1495.7	1802.4	2151.7	2056.0	2070	.	.	.
annual change in % (real, net)	6.8	15.0	17.0	10.1	-7.2	-4.8	.	.	.
Consumer prices (HICP), % p.a.	2.7	3.8	5.8	11.1	4.2	1.2	3	2.5	2.5
Producer prices in industry, % p.a.	11.7	7.3	7.0	18.2	-13.5	10.3	.	.	.
General goverm.budget, EU-def., % GDP									
Revenues	32.8	33.1	33.8	34.1	34.5	34.5	.	.	.
Expenditures	33.3	33.6	34.8	37.4	43.6	42.5	.	.	.
Net lending (+) / net borrowing (-)	-0.5	-0.4	-1.0	-3.3	-9.2	-8	-6	-4.5	-3
Public debt, EU-def., in % of GDP	18.4	18.0	16.9	15.6	29.5	40	43	45	43
Central bank policy rate, % p.a., end of period 3)	2.5	3.7	6.8	7.8	1.6	1.1	.	.	.
Current account, EUR mn	-1481	-2551	-4149	-4227	1128	350	-200	-800	-1200
Current account in % of GDP	-7.1	-10.6	-14.5	-13.1	4.3	1.3	-0.7	-2.6	-3.6
Exports of goods, BOP, EUR mn	9490	11262	12509	16077	11797	15500	18500	21800	26200
annual growth rate in %	26.9	18.7	11.1	28.5	-26.6	31	19	18	20
Imports of goods, BOP, EUR mn	11849	14600	16788	20263	12628	16800	20000	24000	29300
annual growth rate in %	26.1	23.2	15.0	20.7	-37.7	33	19	20	22
Exports of services, BOP, EUR mn	2503	2879	2931	3240	2657	3000	3400	3800	4300
annual growth rate in %	27.1	15.0	1.8	10.5	-18.0	13	13	12	13
Imports of services, BOP, EUR mn	1655	2018	2471	2835	2140	2200	2400	2600	2900
annual growth rate in %	26.0	21.9	22.4	14.7	-24.5	3	9	8	12
FDI inflow, EUR mn	826	1448	1473	1396	124	350	700	.	.
FDI outflow, EUR mn	278	232	437	229	157	50	.	.	.
Gross reserves of NB excl. gold, EUR mn	3135.7	4307.5	5165.1	4458.4	4495.2	4900	.	.	.
Gross external debt, EUR mn	10586.5	14441.8	20547.2	23048.2	23051.8	24000	.	.	.
Gross external debt in % of GDP	50.7	60.2	71.9	71.4	87.0	86.8	.	.	.
Average exchange rate LTL/EUR	3.4528	3.4528	3.4528	3.4528	3.4528	3.4528	3.45	3.45	3.45
Purchasing power parity LTL/EUR	1.7752	1.8656	1.9821	2.1711	2.1316	2.1732	.	.	.

Note: Gross industrial production, construction output and producer prices refer to NACE Rev. 2.

1) Preliminary and wiiw estimates. - 2) In % of working age population. - 3) VILIBOR one-month interbank offered rate (Lithuania has a currency board).

Source: wiiw Database incorporating Eurostat and national statistics. Forecasts by wiiw.

Leon Podkaminer

Poland:
Continuing growth conditional on competent policy

GDP growth kept accelerating in the course of 2010. Accelerating growth of private consumption has been an important factor, eventually accounting for 1.9 percentage points (pp) out of the total estimated 3.8% GDP growth rate in the whole year 2010. Government consumption kept rising as well, contributing another 0.7 pp. The positive contribution of rising inventories was also highly significant (1.8 pp). The contributions of other expenditure items turned negative: falling gross fixed investment lowered the GDP growth by 0.4 pp and the developments in foreign trade (in goods and services) by another 0.2 pp. Gross value-added generated by industry rose 9.1%, by construction by 3.8% and by the sector of market services by 1.5%.

Individual GDP expenditure items will be following different paths in 2011 and later on. The budget for 2011 stipulates a 0.7% cut in the volume of government consumption (chiefly in the form of some reductions in the public sector's employment/wage bill). Because of the upcoming parliamentary elections (scheduled for October 2011) the cut in question may in practice be less pronounced than planned. In any case, it is reasonable to expect that government consumption will not contribute meaningfully to GDP growth in 2011 (and probably also not in 2012). In 2011 rising inventories may again contribute to the overall GDP growth – but the scale of the resulting contribution may be expected to be lower than recently.

Against expectations the volume of gross fixed capital formation did not rise in 2010. To some extent this may have been caused by particularly adverse weather conditions. However, in the second half of the year a recovery in investment seems to have started. There are many indications (apart from rising construction output) that the recovery of investment will be gaining momentum in 2011. First, already in 2010 sales of capital goods industries rose by 12.6% – faster than of the total industrial production (9.8%). Second, the non-financial corporate sector's profitability and liquidity positions are very good. Net (post-tax) profit earned by the entire sector rose by 12.5% year-on-year during the first nine months of 2010 (12.9% in industry). The sector, which on the whole is not significantly dependent on bank financing, disposes of large and growing cash balances. For some time now these balances have been idly accumulating as deposits. No doubt these money resources could be used more productively – such as for financing the expansion of fixed assets. Of course, for this to happen, the levels of uncertainty over e.g. sales prospects, exchange rates, market interest rates etc. must be further reduced. Third, in actual fact the most recent business climate poll conducted by the National Bank indicates that optimistic opinions are becoming prevalent among the corporate sector's managers. The role of identifiable barriers to the growth of firms (including the barrier of inadequate demand) is assessed to be falling quite substantially while the levels of production capacity utilization are high. Large and medium-size firms tend now to plan to expand (or renew) their capital stocks. This tendency appears to be quite pronounced especially among export-oriented (and foreign-owned) industrial firms.

The (hopefully materializing) expansion of the corporate sector’s fixed capital formation will be anyway supported by the continuing infrastructure investment (co-financed by EU funds) and by investments related to the European Football Championship (to be held jointly with Ukraine next year). Last but not least, after two fairly stagnant years the demand for housing is likely to grow again, even if modestly at first.

The improvements in the business climate and the revival of growth of fixed investment are expected to accelerate in 2011-2013, if not much. This should combine with rising employment levels and real wages, thereby allowing a further growth of household consumption. Nonetheless, because unemployment will remain high, the wage pressures will remain subdued. Given the ongoing labour productivity gains, the wage increases awarded will not erode the corporate sector’s profitability levels and cost gains. However, although currently firms are generally still satisfied with the prevailing levels of the exchange rates, their competitive advantages could be eroded quite quickly if the Polish zloty strengthens unduly.

The risk of an undue appreciation of the Polish currency – and the ensuing competitiveness losses – must not be underestimated. The zloty already strengthened vs. the euro by about 8% on average (2010 over 2009). No doubt this must have contributed to the external trade performing somewhat worse in 2010 than in 2009. Under a floating exchange rate regime the economic policy cannot fully control the exchange rate movements. Even if the levels of domestic interest rates (and the yields on government debt) are low, it is possible to observe high capital inflows and the emergence of appreciation pressures. Bearing these observations in mind, it may be still advisable that the economic policy avoids taking actions that can make things worse. In this context the recent (20 January 2011) decision of the Monetary Policy Council to raise the policy interest rates seems problematic. The interest rates had been high (given low inflation prevailing) even prior to that decision. No wonder Poland experienced very high inflows of portfolio (and other) capital throughout 2010 (seen in the massive increase in gross external reserves and in gross foreign debt). That tendency may now be strengthened – to the detriment of short-term real activity and long-term financial stability.

In contrast to the monetary policy, the fiscal policy does not overreact. The high fiscal deficits (recorded in 2009-2010) are to go down rather gradually. The macro and fiscal consequences of higher VAT rates and some cuts in public sector wages/employment envisioned in the budget for 2011 will on the whole be quite limited. More importantly, the government seems determined to substantially downsize the so-called Second Pillar of the pension system. The move should help improve public finances quite substantially without materially hurting practically anybody, except a couple of private firms managing the Second-Pillar pension funds.

In sum, so far Poland’s growth has been accelerating rather moderately, without yet generating identifiable imbalances. Undue currency appreciation and excessive capital inflows constitute the major (related) risks. Under such conditions a competent monetary policy would be quite essential.

Table PL

Poland: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 1)	2011	2012 Forecast	2013
Population, th pers., average	38165.4	38141.3	38120.6	38125.8	38151.6	38190	38180	38170	38150
Gross domestic product, PLN bn, nom.	983.3	1060.0	1176.7	1275.4	1343.7	1430	1540	1640	1750
annual change in % (real)	3.6	6.2	6.8	5.1	1.7	3.8	3.8	4.2	4.3
GDP/capita (EUR at exchange rate)	6400	7100	8200	9500	8100	9400	.	.	.
GDP/capita (EUR at PPP)	11500	12300	13600	14100	14300	14900	.	.	.
Consumption of households, PLN bn, nom.	614.3	652.8	701.6	773.8	809.4	860	.	.	.
annual change in % (real)	2.1	5.0	4.9	5.7	2.1	3.2	3.8	4.5	4.5
Gross fixed capital form., PLN bn, nom.	179.2	208.3	253.7	283.9	285.2	290	.	.	.
annual change in % (real)	6.5	14.9	17.5	9.6	-1.1	-2.0	4	6	7
Gross industrial production (sales) 2)									
annual change in % (real)	3.7	12.1	9.3	2.6	-3.7	11.1	8	7	6
Gross agricultural production									
annual change in % (real)	-0.7	-1.1	5.2	1.3	4.7	-10.6	.	.	.
Construction industry 2)									
annual change in % (real)	8.7	15.9	16.4	9.8	4.7	3.9	.	.	.
Employed persons - LFS, th, average	14115.6	14593.6	15240.5	15799.8	15868.0	15900	15950	16270	16680
annual change in %	2.3	3.4	4.4	3.7	0.4	0.2	0.3	2.0	2.5
Unemployed persons - LFS, th, average	3045.4	2344.3	1618.8	1210.7	1411.1	1720	.	.	.
Unemployment rate - LFS, in %, average	17.7	13.8	9.6	7.1	8.2	10.5	10	8.5	7.5
Reg. unemployment rate, in %, end of period	17.6	14.8	11.4	9.5	11.9	12.3	10.5	9.5	9.0
Average gross monthly wages, PLN	2360.6	2475.9	2672.6	2942.2	3103.0	3222	3460	3710	3960
annual change in % (real, gross)	1.8	4.0	5.5	5.9	2.1	1.2	2	3	4
Consumer prices (HICP), % p.a.	2.1	1.3	2.6	4.2	4.0	2.7	3.5	2.5	2.5
Producer prices in industry, % p.a.	0.4	1.8	2.0	2.4	3.9	2.3	2.5	2.5	2.0
General governm.budget, EU-def., % GDP									
Revenues	39.4	40.2	40.3	39.5	37.2	38.2	40	40.6	.
Expenditures	43.4	43.9	42.2	43.2	44.4	46.2	45.5	44.6	.
Net lending (+) / net borrowing (-)	-4.1	-3.6	-1.9	-3.7	-7.2	-7.9	-5.5	-4	-3
Public debt, EU-def., in % of GDP	47.1	47.7	45.0	47.1	50.9	53.2	54.2	53.5	52
Central bank policy rate, % p.a., end of period 3)	4.5	4.0	5.0	5.0	3.5	3.5	4.3	4.5	4.0
Current account, EUR mn 4)	-3016	-7443	-14701	-17399	-6752	-11614	-14000	-16000	-18000
Current account in % of GDP 4)	-1.2	-2.7	-4.7	-4.8	-2.2	-3.2	-3.5	-3.8	-4.1
Exports of goods, BOP, EUR mn 4)	77562	93382	105883	120953	101715	122134	134300	147700	156600
annual growth rate in %	17.8	20.4	13.4	14.2	-15.9	20.1	10	10	6
Imports of goods, BOP, EUR mn 4)	79804	98918	118249	138691	104817	128494	143900	164000	177100
annual growth rate in %	13.4	24.0	19.5	17.3	-24.4	22.6	12	14	8
Exports of services, BOP, EUR mn 4)	13105	16349	21018	24207	20717	24270	26700	29400	31800
annual growth rate in %	21.2	24.8	28.6	15.2	-14.4	17.2	10	10	8
Imports of services, BOP, EUR mn 4)	12520	15768	17583	20729	17294	21195	24000	27100	29800
annual growth rate in %	16.1	25.9	11.5	17.9	-16.6	22.6	13	13	10
FDI inflow, EUR mn 4)	8330	15737	17241	10135	9893	7538	13000	.	.
FDI outflow, EUR mn 4)	2767	7122	4018	3071	3711	3781	4000	.	.
Gross reserves of NB excl. gold, EUR mn	34535	35237	42675	42299	52734	66499	.	.	.
Gross external debt, EUR mn	112316	128870	159106	174265	195025	235000	.	.	.
Gross external debt in % of GDP	44.1	46.6	48.6	56.8	59.6	65.3	.	.	.
Average exchange rate PLN/EUR	4.0230	3.8959	3.7837	3.5121	4.3276	3.9947	3.9	3.9	4.0
Purchasing power parity PLN/EUR	2.2321	2.2640	2.2695	2.3742	2.4691	2.5096	.	.	.

Note: Gross industrial production, construction output and producer prices refer to NACE Rev. 2.

1) Preliminary and wiiw estimates. - 2) Enterprises with 10 and more employees. - 3) Reference rate (7-day open market operation rate) - 4) From 2006 including Special Purpose Entities (SPEs).

Source: wiiw Database incorporating Eurostat and national statistics. Forecasts by wiiw.

Gábor Hunya

Romania:
Election cycle ahead

The 2009-2010 contraction of the Romanian economy was one of the deepest and longest lasting in Europe. The austerity measures introduced in mid-2010 additionally suppressed domestic demand and caused an at least 1% decline of GDP for the year as a whole. Wage cuts in the public sector and a 5 percentage points VAT increase resulted in a 4% decline of net real wages. The reasoning behind these measures was in line with the IMF programme put in place in 2009. It aimed at curtailing the budget deficit to GDP ratio by improving the fiscal balance and taking GDP contraction as a side effect.

Private and public investment activity remained very much suppressed in 2010; gross fixed capital formation fell by about 15% after a similar contraction rate in the previous year. But stock building increased considerably, compensating the effect on gross capital formation, thus the latter had a largely neutral effect on GDP growth. Investments in buildings remained at a very low level, residential construction and the issuance of building permits continued to decline, while machinery investments recovered close to the previous year's level. Net exports made a positive contribution to the change of GDP due to strong export demand.

Industry and exports were growing quite rapidly in 2010 while agriculture and services suffered declining outputs. The production of motor vehicles, electrical machinery and metallurgy increased by about 30% and surpassed the pre-crisis level. The shift of production and related exports to higher value-added products continued. Machinery and transport equipment comprised about 42% of exports, up from 38% just two years before, while total goods exports in euro terms rose by 11% to a new peak. The Renault subsidiary Dacia was one of the most successful car producers in Europe and has good further growth prospects; in 2011, the production of Ford will start and add to the success of this industrial sector in Romania. The other side of the coin is that industries serving mainly the domestic market such as construction materials production continued to shrink. The whole corporate sector is split between the successful exporters and related suppliers and those trying to sell to the local customer. Payment arrears have disrupted the functioning of SMEs and the number of bankruptcies increased three-fold, mostly affecting trade and construction.

The unemployment rate has risen to about 7.4% (LFS end of 2010) – back to where it was four years ago, but still low in international comparison. A main reason for the low unemployment is the high employment level in public services and the generous labour protection legislation causing labour market rigidity. In order to economize on public funds, labour market and social benefit reforms are being introduced in the framework of the IMF agreement. Public employment started to be reduced already in 2010. Measures effective in 2011 include labour market flexibilization and streamlining unemployment benefits by changing the related laws. These extend the employers' right to establish differentiated working hours and to force employees to work extra hours with no extra payment. Employers can more easily send people on leave when there is not enough work and obtain more freedom with labour contracts. Another stipulation is eliminating the nine-month interdiction to hire new employees in the place of employees that were collectively fired. Such labour market flexibilization measures are bound to increase unemployment.

The tax surge drove end-2010 inflation up to 8% (the highest rate among the NMS); still inflation has so far not been considered a problem by the National Bank. The policy rate was reduced in May to 6.25% and has been left unchanged ever since. Major fluctuations of the exchange rate were avoided in 2010 by market interventions which kept the annual average close to the previous year's level. The effects of the VAT hike will continue in the first half of 2011, and also higher international commodity prices will exert additional inflation pressure. As a result, the average CPI may not come down below 4% even in 2012.

The general government budget deficit improved from 7.4% of GDP in 2009 to 6.6% in 2010 on a cash basis, somewhat below the government's target. (The deficit according to EU definition was substantially higher, 8.6% of GDP in 2009; the corresponding figure for 2010 is not yet available.) Budget revenues increased mainly due to VAT and excises hikes while income and profit tax related revenues declined. Expenditures rose mainly to co-finance EU projects. The budget plan for 2011 envisages a cash deficit of 4.4% of GDP based on conservative 1.5% economic growth forecast. Public sector wages were raised in February by 15% partially compensating for the cuts of last year. A good deal of improved efficiency of the public sector and an increasing inflow of EU structural funds are taken for granted, but bear downside risks. The government has a number of investment plans, especially in infrastructure, most of them to be financed from EU structural funds. Up to the end of 2010, Romania received only 10% of the EUR 20 billion European funds it is eligible for in 2007-2013. Measures have been taken to speed up disbursement but their effectiveness has yet to be seen.

The current account balance worsened slightly in nominal EUR terms in 2010 and stayed at a financeable level. The goods trade balance improved but all other items worsened. The deficit of the incomes account increased both due to higher interest payments and profits of foreign investors. The surplus of the current transfers, 4.3% of GDP in 2009, declined to 2.8% of GDP in 2010, meaning that Romanians working abroad earn and transfer home less during the crisis (there is little evidence of return migration). On the financial account FDI declined but portfolio investments and short-term capital inflows recovered. The main source of foreign inflow were funds from the IMF and a major part of it did not leave the reserves of the National Bank.

There is a lot of uncertainty concerning the future economic policy. None of the three governments of the past two years has been able to come up with a credible fiscal programme that could be actually implemented. The authorities have essentially shifted economic policy making to the IMF. The two-year agreement is going to expire in early 2011 and the question is what to put in its place thereafter. The planned new precautionary accord with a fund of EUR 3.6 billion from the IMF, EUR 1.4 billion from the EU and EUR 0.4 billion World Bank projects will span for two years from May 2011. This new agreement may provide some safeguard but will put a much weaker constraint on fiscal policy than the outgoing regime. Meanwhile, in order to finance the maturing loans, the government has to be more active on international financial markets where the country has little exposure. There are also plans for selling minority shares of state-owned companies included in a property restitution fund recently listed on the stock exchange. Improving efficiency of the state-owned enterprises which currently carry losses and eliminating the payment arrears will be part of the conditions of the new IMF agreement and will be supported by new programmes of the World Bank.

Nevertheless, there has been growing confidence in Romania's fiscal stability in the past few months. The five-year CDS-spreads moved together with those of Hungary until the end of November 2010 when both were about 300 basis points. The two countries disconnected later on with Romania staying flat and Hungary's CDS increasing. The IMF programme has been valued as a success and the fiscal plan for 2011-2012 as sustainable while in the case of Hungary markets were waiting for new structural policy measures. In January/February 2011 the ratings of both countries were improving and Romania continued faring better. Still Romania has a one notch worse credit rating, the worst among the NMS together with Latvia, presumably due to negative GDP growth. Risks may increase as soon as the role of the IMF to monitor and direct economic policy will decline.

For the coming years we reckon with an election cycle. We expect that the government will not stick to fiscal and wage restraint when approaching parliamentary elections in late 2012. The result can be stepped-up GDP growth to 4% in the election year. This will necessarily be followed by corrections in 2013 which will result in a lower GDP growth rate. Compared with the autumn 2010 forecast of the Romanian government we expect a somewhat faster recovery in 2011 and a similar growth in 2012. The main discrepancy is in 2013 for which we expect a deceleration of economic growth and a tense external financial situation while the government predicts acceleration of GDP growth with a contracting current account deficit.

In support to our boom-bust growth scenario we can refer to earlier experience. In the previous two election years 2004 and 2008, consumption growth was much higher than in the preceding and subsequent year. This will likely happen again but this time conditions allow only a smaller amplitude. First of all, the country's external financing capacity is more restricted in the wake of the financial crisis. It has to rely on market financing in the case of public debt whereas private sector financing is more expensive and less readily available than before the financial crisis. At the same time, public debt is still relatively low, leaving room for fiscal expansion and the country has also good prospects for FDI recovery.

Table RO

Romania: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 1)	2011	2012	2013
								Forecast	
Population, th pers., average	21634	21588	21547	21514	21480	21460	21440	21410	21400
Gross domestic product, RON mn, nom.	288955	344651	416007	514700	498008	522500	558500	615100	667100
annual change in % (real)	4.2	7.9	6.3	7.3	-7.1	-1.2	2	4	3
GDP/capita (EUR at exchange rate)	3700	4500	5800	6500	5400	5800	.	.	.
GDP/capita (EUR at PPP)	7900	9100	10400	11700	10900	10900	.	.	.
Consumption of households, RON mn, nom.	197069	233135	273418	327928	304699	317700	.	.	.
annual change in % (real)	10.1	12.9	12.0	9.0	-10.5	-2	2	4	2.5
Gross fixed capital formation, RON mn, nom.	68527	88272	125645	164279	130603	116600	.	.	.
annual change in % (real)	15.3	19.9	30.3	15.6	-25.3	-15	4	7	6
Gross industrial production 2)									
annual change in % (real)	-3.1	9.3	10.3	2.6	-5.5	5.5	5	6	5
Gross agricultural production									
annual change in % (real)	-13.1	2.4	-17.7	21.2	-2.2	-2.2	.	.	.
Construction industry 2)									
annual change in % (real)	6.1	15.4	33.2	26.7	-15.0	-13.2	.	.	.
Employed persons - LFS, th, average	9114.6	9291.2	9353.3	9369.1	9243.5	9200	9150	9200	9200
annual change in %	-0.5	1.9	0.7	0.2	-1.3	-0.5	-0.5	0.5	0
Unemployed persons - LFS, th, average	704.5	728.4	640.9	575.5	680.7	735	.	.	.
Unemployment rate - LFS, in %, average	7.2	7.3	6.4	5.8	6.9	7.4	7.6	7	7
Reg. unemployment rate, in %, end of period	5.9	5.2	4.0	4.4	7.8	6.9	.	.	.
Average gross monthly wages, RON	968	1146	1396	1761	1845	1940	.	.	.
annual change in % (real, net)	14.3	9.0	14.7	16.5	-1.5	-4.0	.	.	.
Consumer prices (HICP), % p.a.	9.1	6.6	4.9	7.9	5.6	6.1	5.5	4	4
Producer prices in industry, % p.a.	8.1	9.5	7.5	15.3	1.8	6.3	.	.	.
General governm.budget, EU-def., % GDP									
Revenues	32.4	33.3	33.6	32.5	32.4	33.0	.	.	.
Expenditures	33.6	35.5	36.2	38.2	41.0	40.5	.	.	.
Net lending (+) / net borrowing (-)	-1.2	-2.2	-2.6	-5.7	-8.6	-7.5	-6	-5	-4
Public debt, EU-def., in % of GDP	15.8	12.4	12.6	13.4	23.9	30.5	33	34	35
Central bank policy rate, % p.a., end of period 3)	7.50	8.75	7.50	10.25	8.00	6.25	.	.	.
Current account, EUR mn	-6888	-10220	-16758	-16178	-4933	-5158	-6800	-9000	-9500
Current account in % of GDP	-8.6	-10.5	-13.4	-11.6	-4.2	-4.2	-5.2	-6.4	-6.3
Exports of goods, BOP, EUR mn	22255	25953	29542	33656	29091	37251	41700	46700	52300
annual growth rate in %	17.5	16.6	13.8	13.9	-13.6	28.0	12	12	12
Imports of goods, BOP, EUR mn	30061	37765	47365	52729	35959	43115	48300	55500	61100
annual growth rate in %	23.9	25.6	25.4	11.3	-31.8	19.9	12	15	10
Exports of services, BOP, EUR mn	4102	5585	6885	8751	7061	6353	6700	7400	8100
annual growth rate in %	41.3	36.2	23.3	27.1	-19.3	-10.0	5	10	10
Imports of services, BOP, EUR mn	4451	5581	6475	8091	7352	7098	7500	8300	9100
annual growth rate in %	42.8	25.4	16.0	25.0	-9.1	-3.5	5	10	10
FDI inflow, EUR mn	5213	9060	7280	9501	3487	2598	3500	.	.
FDI outflow, EUR mn	-24	338	206	186	-60	158	200	.	.
Gross reserves of NB excl. gold, EUR mn	16785	21299	25325	25977	28249	32432	.	.	.
Gross external debt, EUR mn	30914	41196	58628	72354	81220	90766	.	.	.
Gross external debt in % of GDP	39.4	40.4	50.8	56.5	69.1	74	.	.	.
Average exchange rate RON/EUR	3.6209	3.5258	3.3353	3.6826	4.2399	4.2122	4.3	4.4	4.4
Purchasing power parity RON/EUR	1.6993	1.7599	1.8623	2.0481	2.1346	2.2438	.	.	.

Note: Gross industrial production, construction output and producer prices refer to NACE Rev. 2.

1) Preliminary and wiiw estimates. - 2) Enterprises with 4 and more employees. - 3) One-week repo rate.

Source: wiiw Database incorporating Eurostat and national statistics. Forecasts by wiiw.

Zdenek Lukas

Slovakia:
Despite export-driven growth, high unemployment will persist

The recovery observed in the Slovak economy already in the first half of 2010 continued in the second half of the year. The GDP expanded by 4% in 2010 and the country returned on the path of fairly strong economic growth, in fact the highest among the EU countries. The economic expansion has basically been the result of the revival in external demand supported by improved competitiveness. As a result, the contribution of foreign trade to GDP growth was again positive, albeit lower than in 2009. The earlier contraction in aggregate demand, in the wake of the global financial and economic crisis and concerns about the future, had slashed inventories at the end of 2008 and in 2009. However, already during 2010 inventories were on the rise again. While gross capital formation expanded by above 10%, gross fixed capital formation rose only modestly (1%). In total, the economic growth in 2010 was mostly driven by an ongoing recovery in external demand and by a gradual rebuilding of inventories. Rising unemployment impaired the purchasing power of households and provoked consumers' caution.

As in other eurozone countries, the weakening of the euro had a positive impact on the economy, in particular as compared to other non-euro Visegrad countries (V-3). Among those, the Czech Republic is Slovakia's second most important trading partner after Germany, with a share of about 14% in total Slovak exports. Poland and Hungary each account for 7% of total Slovak exports. All in all, the V-3 countries account for 28% of the total Slovak exports. In 2010 the euro depreciated on average compared to 2009 by 5% year-on-year against the Czech koruna, by 2% against the Hungarian forint and by 8% against the Polish zloty. The euro depreciation against a basket of currencies had also boosted the competitiveness of Slovak tradable goods in other markets outside the euro area (totally one-half of exports). Thanks to the above mentioned euro depreciation, exports to the Czech Republic and Poland expanded by some 30% and 27% respectively in 2010, while total exports rose by just around 20%. At the same time, the trade surplus with the V-3 countries expanded from EUR 3.2 billion to above EUR 4.5 billion. Apart from the depreciation, the exports were also boosted by impressive productivity gains in manufacturing (implying falling unit labour costs) and low producer prices as well. A considerable deterioration in labour market was the dark side of rising export competitiveness. However, since the second quarter of 2010, signs of a very slow recovery appeared with unemployment declining moderately and employment rising slightly. The increase in the number of those active in industry, construction, transport, administration and health service has somewhat relieved the pressure on the labour market.

Recovering external demand and rising competitiveness boosted growth in gross industrial output which expanded by nearly 20% in 2010. As a result, industrial production returned to the pre-crisis level. As in the past, foreign-owned enterprises in the automotive industry are the most important driving force of the economy. Expanding by 40% in 2010, the car output recovered significantly faster and more strongly than expected. Growth was exclusively export-driven as the amount of light vehicles (cars under 3.5 tonnes) nearly registered in Slovakia dropped by 22% in 2010. Above average growth was also recorded for machinery (48%), pharmaceutical products, electronic and optical equipments (both up by 23%). As opposed to industry, construction output continued to fall (by 5%) in 2010. However, the sector was slightly up in the last quarter of the year. Prospects are encouraging as highway construction (supported by EU transfers) could provide an important impetus to the construction industry.

Following outflows in 2009, foreign direct investments in Slovakia have not yet fully recovered. Most foreign investors repatriated the bulk of the profits abroad and just few of them reinvested their earnings in Slovakia. A number of investors had left the country in the last two years, with the consequences that investment was curbed, postponed or redirected to other more attractive destinations. Despite recovering economy, there is still not much room for a revival of FDI due to unused production capacities. Nevertheless, this year VW is starting production of the new small family car models in Slovakia and will invest here EUR 300 million. Besides, the Slovak electric utility company Slovenské elektrárne (66% of shares owned by the Italian energy company Enel) will complete the third and fourth units of the Mochovce nuclear power plant. This – the biggest – private investment in Slovakia (totalling EUR 2.7 billion) is to be spent up until 2013. Due to the lack of domestic R&D expenditure, the FDI are the basic source of modernization and new technologies in the country. Financial support of R&D activities in the Slovak Republic is among the lowest in the EU.

The new centre-right government (in power since June 2010) cut the public-private partnership (PPP) projects prepared by the previous government to construct highways in Slovakia, arguing that these procedures would be too expensive. The new highway construction project is in the pipeline. In addition, the government is re-opening the door to strategic partners in selected companies with state participation. The ones most frequently mentioned are the Rail Freight Transport ZSSK Cargo and the Bratislava Airport. (The latter was on the privatization agenda already in spring 2006.)

The present government inherited public finances in a very bad state. As budgetary expenditures rose faster than revenues, the general government deficit amounted to 8% of GDP in 2010. Despite the programme of medium-term fiscal stabilization, the costs of debt services are on the rise. Public debt 42% of GDP at the end of 2010. Gross external debt amounted to 74% of the GDP. The increase in the level of external debt is not surprising given the fact that the country is still recording current account deficits. The government intends to consolidate the budget through a mix of expenditure cuts and revenue enhancements. Budgetary revenues are to be supported by an increase of the VAT rate (from 19% to 20%). More money should be collected also by hiking excise taxes on tobacco and beer. In addition, the cancellation of many tax exemptions (mostly for craftsmen) should bring additional revenues. On the expenditure side, the budget of the ministries and other governmental agencies is to be cut by about 10% in 2011. The programme (taking effect in 2011) aims at gradually cutting the general government deficit to 3% of GDP by 2013. The higher VAT level is meant to be only temporary and should be eliminated after reaching that target. The government has not introduced sufficient structural measures aimed at long-term savings in budgetary expenditures. There are concerns, especially related to the long-term sustainability of the pension system (due to the ageing population and cuts in the private pillar of the pension system) and rising unemployment benefits. Past experience has shown that only several years of strong GDP growth have an effect on employment. Slovak cabinet approved a budget draft that envisages a general government budget deficit of 4.9% of the GDP in 2011. The envisaged cut in the deficit over the next three years is very large. The higher tax burden might undermine fragile growth prospects. Comprehensive reforms aimed at reducing public spending have not been on the agenda so far.

Driven by increasing confidence in industry and in trade, the economic sentiment indicator was up by 12 points in January 2011 year-on-year and so roughly reached the long-term average. It seems that there is sustained optimism in the ongoing recovery. As the companies expect continuing strong demand for the country's exports, stocks are being rebuilt. The expected recovery in FDI will be modest as there are better places to invest in the world (such as Asia or Latin America). As for sustainable economic growth in the future, the crucial point is to avoid any measures that would threaten Slovakia's regained competitiveness and thus might undermine its competitive position particularly within the EU. If the euro remains weak and Slovak productivity gains (low unit labour costs) persist, the GDP may continue to maintain growing by some 4% in 2011 and 2012. However, the economic growth powered by massive consumption appetite will not return to the high rates seen a few years ago, as long-term debt burdens will damp demand and the whole international environment has also changed. The current account deficit and public debt will rise slightly over the forecast period. The main challenges for the government relate to fiscal consolidation, high unemployment and last but not least cronyism and corruption. The long-term sustainable economic growth will call for Slovakia to expand its own R&D activities.

Table SK

Slovakia: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 [1]	2011	2012	2013
								Forecast	
Population, th pers., average	5387.0	5391.4	5397.3	5406.6	5418.6	5430	5440	5450	5440
Gross domestic product, EUR mn, nom.	49314.2	55080.9	61555.0	67007.3	63050.7	66200	69500	73000	78200
annual change in % (real)	6.7	8.5	10.6	5.8	-4.8	4	4	4	5
GDP/capita (EUR at exchange rate)	7100	8300	10200	11900	11600	12200	12800	13400	14400
GDP/capita (EUR at PPP)	13500	15000	17000	18100	17200	18100	.	.	.
Consumption of househ., EUR mn, nom.	27823.8	30891.1	33902.0	37604.3	37714.3	38100	.	.	.
annual change in % (real)	6.5	5.9	6.9	6.1	0.3	0	2	3	5
Gross fixed capital form., EUR mn, nom.	13089.5	14588.8	16096.5	16575.9	12991.1	13300	.	.	.
annual change in % (real)	17.5	9.3	9.0	1.0	-19.9	1	5	8	8
Gross industrial production									
annual change in % (real)	0.8	15.7	17.0	3.3	-13.8	18.8	8	8	6
Gross agricultural production									
annual change in % (real)	-8.7	-2.9	-4.5	10.6	-12.3	-9.9	.	.	.
Construction industry									
annual change in % (real)	14.7	14.9	5.7	11.9	-11.2	-4.6	.	.	.
Employed persons - LFS, th, average	2215.2	2302.3	2357.7	2433.7	2366.3	2300	2320	2340	2360
annual change in %	2.1	3.9	2.4	3.2	-2.8	-3	1	1	1
Unemployed persons - LFS, th, average	430.0	355.4	295.7	255.7	323.5	400	.	.	.
Unemployment rate - LFS, in %, average	16.3	13.4	11.1	9.5	12.0	14.8	14	13	12
Reg. unemployment rate, in %, end of period	11.4	9.4	8.0	8.4	12.7	12.5	12	11	10
Average gross monthly wages, EUR [2]	573	623	669	723	745	765	.	.	.
annual change in % (real, gross)	6.3	3.9	4.4	3.4	1.4	2	3	.	.
Consumer prices (HICP), % p.a.	2.8	4.3	1.9	3.9	0.9	0.7	2	3	3
Producer prices in industry, % p.a.	3.4	3.0	-1.4	2.5	-6.6	0.1	1	2	2
General governm.budget, EU-def., % GDP									
Revenues	35.2	33.4	32.5	32.9	33.6	32	32.6	32.4	.
Expenditures	38.0	36.6	34.3	35.0	41.5	40	38.0	37.4	.
Net lending (+) / net borrowing (-)	-2.8	-3.2	-1.8	-2.1	-7.9	-8	-5.4	-5.0	-4.5
Public debt, EU-def., in % of GDP	34.2	30.5	29.6	27.8	35.4	42.1	45.1	47.4	47
Central bank policy rate, % p.a., end of period [3]	3.0	4.8	4.3	2.5	1.0	1.0	.	.	.
Current account, EUR mn	-3268	-3636	-2912	-4279	-2023	-2000	-3200	-3600	-4000
Current account in % of GDP	-8.5	-8.2	-5.3	-6.6	-3.2	-3.0	-4.6	-4.9	-5.1
Exports of goods, BOP, EUR mn	25654	33349	42260	47722	39715	48500	51000	54000	56000
annual growth rate in %	15.3	30.0	26.7	12.9	-16.8	22	6	5	4
Imports of goods, BOP, EUR mn	27571	35817	42916	48435	38528	48000	51000	54000	56000
annual growth rate in %	17.4	29.9	19.8	12.9	-20.5	25	7	5	4
Exports of services, BOP, EUR mn	3542	4322	5140	5796	4522	4340	4800	5400	6200
annual growth rate in %	18.1	22.0	18.9	12.8	-22.0	-4	10	12	15
Imports of services, BOP, EUR mn	3285	3790	4751	6269	5768	5200	5700	6400	7400
annual growth rate in %	18.0	15.4	25.4	32.0	-8.0	-10	10	12	15
FDI inflow, EUR mn	1952	3311	2636	2395	-35	-100	1000	1500	2000
FDI outflow, EUR mn	120	292	441	177	311	100	400	500	500
Gross reserves of NB excl. gold, EUR mn [4]	12567	9639	12280	12674	481	550	.	.	.
Gross external debt, EUR mn	22705	24449	30156	37286	45338	49000	.	.	.
Gross external debt in % of GDP	57.9	50.7	54.6	55.6	71.9	74.0	.	.	.
Average exchange rate EUR/EUR	1.2813	1.2359	1.1211	1.0377	1.0000	1.0000	1	1	1
Purchasing power parity EUR/EUR	0.6759	0.6814	0.6720	0.6835	0.6753	0.6746	.	.	.

Note: Gross industrial production, construction output and producer prices refer to NACE Rev. 2.

1) Preliminary and wiiw estimates. - 2) From 2006 including wages of armed forces. - 3) From 2009 official refinancing operation rates for euro area (ECB), two-week repo rate of NB before . - 4) From January 2009 (euro introduction) foreign currency reserves denominated in non-euro currencies only.

Source: wiiw Database incorporating Eurostat and national statistics. Forecasts by wiiw.

Hermine Vidovic

Slovenia:
Impact of the recession still strongly felt

Slovenia's GDP started growing modestly in the second quarter of 2010 – after six quarters of steady and extremely deep decline – and ended up in a moderate 1.2% rise for the whole year. The modest increase was due to expanding foreign demand and rising inventories, while domestic demand – both consumption and particularly investment – continued to decline. Gross fixed capital formation fell by about 7%, affecting primarily construction. Households are cautious and are postponing purchases: due to declining disposable income as well as tight credit conditions consumption growth was only slightly positive. Also, government consumption reported a modest increase. The popularity of the government of Prime Minister Borut Pahor has slumped considerably over time; in the last opinion poll it was supported by only 18% of the population.

After a dramatic fall in 2009, industrial production growth gained momentum from month to month in the course of the year, rising by almost 7% in 2010. More than half of all industrial branches within manufacturing increased their output, most notably the export-oriented production of electrical equipment (24%) and cars (15%). In construction, where output had contracted significantly in 2009, the negative tendencies continued, with output down by 17% in 2010. Reasons behind this drop are the saturation of residential buildings due to the huge number of unsold flats and shrinking public works in the fields of transport and infrastructure and, finally the drying up of credit markets. As a consequence a number of building companies are in trouble, the most prominent being Slovenia's largest construction company SCT. In external trade, the positive tendencies prevailing in the first quarter of the year strengthened, with both commodity exports and imports up by 14% and 15%. A breakdown of exports by industrial branches shows that car exports and exports of electrical appliances contributed most to the overall increase, but car exports slowed towards the end of the year due to the expiration of measures to boost the purchases of cars in certain EU countries. Though rising somewhat, the trade deficit remained low. In services trade, exports and imports grew only moderately by 1% and 3.5% respectively; hence, the services trade surplus narrowed slightly. Owing to the decreasing trade deficit, the reduced income and current transfers' deficits, the current account ended up only with a small minus in 2010. As opposed to the pre-crisis years, when Slovenia was a net exporter of FDI, foreign investments in the form of debt financing between affiliated companies exceeded Slovenian investments abroad during 2010.

Labour Force Survey data indicate that the number of employed continued to decrease in 2010, while the LFS unemployment rate rose to 7.5%, which is still below the EU-27 average, but high by Slovenian standards. Conversely, unemployment based on registration data has shown a steady increase since September 2008, putting the unemployment rate at 11.6% by the end of December.

Unemployment may further increase in the coming months due to the possible closing-downs of large enterprises, for example in the construction and trade sectors.

Slovenia's banks' lending activities have been sluggish in 2010. The two largest banks, Nova Ljubljanska Banka (NLB) and Nova Kreditna Banka Maribor (NKMB), will need capital increases in the coming months. In 2010 Slovenia's banking sector posted close to EUR 50 million losses, which was mainly due to the past takeover policy, the poor financial situation of the clients as well as the global financial crisis. However, compared to other EU member states the share of bad loans is very low in Slovenia. According to the governor of the Bank of Slovenia, bad loans rose from 1.7% of the total portfolio in 2007 to 3.2% by the end of October 2010. The manufacturing sector is accounting for the biggest share of non-performing loans, while growth of non-performing loans was most striking in the construction sector.

In response to the demographic, economic and financial challenges the Slovenian parliament has recently approved a new Pension and Disability Insurance Act. The law envisages the maintenance of the solidarity principle, a gradual extension of working years and a rise of the retirement age to 65 years for both men and women. However, male and female manual workers with 40 and 38 years of service will still be allowed to retire at the age of 60 and 58 years on full benefit. However, the law is pending since opposition parties and trade unions want to hold a referendum on the issue. The government on the other hand is supporting a motion filed by a group of lawmakers to the constitutional court to reject a referendum on the issue.

The changing economic environment and reduced tax revenues prompted the Slovenian government to adopt a supplementary budget in July 2010 (the budget bills for 2010 and 2011 were initially passed in December 2009). Accordingly, the general government deficit was raised to an estimated 5.7% in 2010 and 4.2% in 2011. However, given the only slow economic recovery in 2010 and the moderate prospects for 2011 (2%), these targets were and will be difficult to achieve. First available results for 2010 are pointing to a deficit exceeding the 6% mark. Expenditures rose the most for interest payments, but also for social transfers – unemployment benefits in particular. Borrowing requirements to bridge the budgetary gap in 2011 and to enable the pre-financing of dept principal due in 2012 and 2013, are estimated at EUR 3 billion.

wiiw is sticking to its earlier GDP forecast of 2% in 2011 which should be driven mainly by foreign demand. More pronounced growth (2.5%) can be expected only in 2012, provided a recovery of investment and private consumption. Given the moderate growth prospects employment might stagnate in 2011 and increase slightly only from 2012 onwards. The unemployment rate (LFS) is expected to come down only gradually. Given fiscal consolidation, public investment will need some time to recover and will regain strength only in 2012. Key to a sustained improvement of Slovenia's economy will be the developments in the European Union – Germany in particular – as the country's main trading area. An export recovery to the countries of the former Yugoslavia, absorbing about 17% of total exports before the crisis, seems rather unlikely. In addition, the already high and rising unit labour costs may reduce Slovenia's export competitiveness. An improvement on the labour market is the main precondition for the recovery of household consumption.

Table SI

Slovenia: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 1)	2011	2012 Forecast	2013
Population, th pers., average	2000.5	2006.9	2018.1	2021.3	2039.7	2047.0	2050	2050	2050
Gross domestic product, EUR mn, nom.	28749.6	31050.4	34568.2	37304.7	35384.4	36560	38340	40280	42530
annual change in % (real)	4.5	5.8	6.9	3.7	-8.1	1.2	2	2.5	3
GDP/capita (EUR at exchange rate)	14400	15500	17100	18400	17300	17900	18600	19600	20700
GDP/capita (EUR at PPP)	19700	20700	22100	22800	20800	21200	.	.	.
Consumption of households, EUR mn, nom.	15331.2	16156.1	17944.2	19477.5	19355.9	19860	.	.	.
annual change in % (real)	2.8	2.9	6.7	2.9	-0.5	0.5	1	1.5	2
Gross fixed capital form., EUR mn, nom.	7321.3	8242.1	9571.3	10743.4	8471.6	8070	.	.	.
annual change in % (real)	3.7	9.9	13.0	8.5	-21.6	-6.7	2	3	5
Gross industrial production									
annual change in % (real)	3.5	5.7	7.1	2.4	-17.3	6.7	4	4	4.5
Gross agricultural production									
annual change in % (real)	-1.2	-7.4	3.9	-1.3	-1.3	1.9	.	.	.
Construction industry									
annual change in % (real)	2.0	15.7	18.5	15.5	-20.9	-17	.	.	.
Employed persons - LFS, th, average	949	961	985	996	981	966	966	976	985
annual change in %	0.7	1.3	2.5	1.1	-1.5	-1.5	0	1	1
Unemployed persons - LFS, th, average	66	61	50	46	61	78	.	.	.
Unemployment rate - LFS, in %, average	6.5	6.0	4.8	4.4	5.9	7.5	7.5	7	6.5
Reg. unemployment rate, in %, end of period	10.2	8.6	7.3	7.0	10.5	11.6	11	10.5	10
Average gross monthly wages, EUR	1157	1213	1285	1391	1439	1500	.	.	.
annual change in % (real, net)	3.5	2.5	4.2	2.0	2.5	2	.	.	.
Consumer prices (HICP), % p.a.	2.5	2.5	3.8	5.5	0.9	2.1	2.8	2.5	2.5
Producer prices in industry, % p.a.	1.9	2.3	4.4	3.9	-1.4	2.0	2.5	2.5	2
General governm.budget, EU-def., % GDP									
Revenues	43.8	43.2	42.4	42.3	43.2	43.7	43.5	43.5	43.0
Expenditures	45.2	44.5	42.4	44.1	49.0	49.7	49.0	48.3	47.5
Net lending (+) / net borrowing (-)	-1.4	-1.3	0.0	-1.8	-5.8	-6.0	-5.5	-5	-4.5
Public debt, EU-def., in % of GDP	27.0	26.7	23.4	22.5	35.4	38.5	44	48	50
Central bank policy rate, % p.a., end of period 2)	3.8	3.8	4.0	2.5	1.0	1.0	.	.	.
Current account, EUR mn	-498	-772	-1646	-2490	-526	-419	-600	-700	-720
Current account in % of GDP	-1.7	-2.5	-4.8	-6.7	-1.5	-1.1	-1.6	-1.7	-1.7
Exports of goods, BOP, EUR mn	14599	17028	19799	20048	16167	18362	20600	23300	26300
annual growth rate in %	12.9	16.6	16.3	1.3	-19.4	13.6	12	13	13
Imports of goods, BOP, EUR mn	15625	18179	21465	22699	16866	19326	21500	24100	27100
annual growth rate in %	12.1	16.3	18.1	5.7	-25.7	14.6	11	12	12.5
Exports of services, BOP, EUR mn	3214	3573	4146	5043	4300	4352	4600	5000	5500
annual growth rate in %	15.5	11.2	16.0	21.6	-14.7	1.2	6	8	10
Imports of services, BOP, EUR mn	2294	2580	3098	3549	3187	3297	3500	3800	4200
annual growth rate in %	9.5	12.5	20.1	14.6	-10.2	3.5	7	9	11
FDI inflow, EUR mn	473	514	1106	1330	-419	630	800	800	900
FDI outflow, EUR mn	516	687	1316	948	121	114	.	.	.
Gross reserves of NB excl. gold, EUR mn 3)	6826.2	5341.7	666.0	623.0	671.0	695.2	.	.	.
Gross external debt, EUR mn	20496	24067	34783	39234	40276	40851	.	.	.
Gross external debt in % of GDP	71.2	77.5	100.6	105.2	113.8	111.7	.	.	.
Average exchange rate EUR/EUR	0.9997	0.9998	1.0000	1.0000	1.0000	1.0000	1	1	1
Purchasing power parity EUR/EUR	0.7304	0.7462	0.7749	0.8086	0.8353	0.8443	.	.	.

Note: Gross industrial production, construction output and producer prices refer to NACE Rev. 2.

1) Preliminary and wiiw estimates. - 2) From 2007 official refinancing operation rates for euro area (ECB), main refinancing rate of NB before - 3) From January 2007 (euro introduction) only foreign currency reserves denominated in non-euro currencies.

Source: wiiw Database incorporating Eurostat and national statistics. Forecasts by wiiw.

Hermine Vidovic

Croatia:
Difficult to come out of the crisis

After six quarters of economic downturn Croatia's GDP growth stabilized in the third quarter of 2010, but in the whole year GDP dropped by another 1.5%. Gross fixed capital formation performed even worse than a year earlier, dropping by 12% and household consumption continued to contract due to shrinking disposable incomes. Government consumption, having almost stagnated in 2009, fell in 2010. Foreign demand, by contrast, contributed positively to GDP growth. In construction, where output had shrunk in 2009, the negative tendencies even strengthened, with output down by 17% in 2010. The reasons behind this drop were declining demand of households for apartments due to falling disposable income and relatively high interest rates on housing loans. In addition, large public infrastructure projects as well as the construction of private production facilities were postponed due to problems of financing. Industrial production was down by 1.4% in 2010. Output fell in all sectors and was particularly strong in the production of intermediate goods. As a consequence of large lay-offs productivity in industry increased by 6%.

In foreign trade, growth of merchandise exports strengthened from quarter to quarter, but import growth remained negative. The main reason behind the relatively strong export growth was the steep increase of the shipbuilding industry, Croatia's main (but highly subsidized) export sector. In 2010 the trade deficit fell to about EUR 5.9 billion, compared to EUR 7.4 billion a year earlier. Services exports stagnated and services imports recorded negative growth rates, thus the trade surplus improved slightly compared to 2009. Owing to the reduction of the trade deficit in particular, the current account deficit continued to shrink, representing around 3% of the GDP. As for FDI, inflows were one third lower than in 2009 and were directed primarily towards the financial sector, the chemical industries and other business activities. At the end of 2010 foreign debt stood at EUR 45 billion, only slightly more than in December 2009.

Unlike in other European countries, where the fall in employment and the rise in unemployment moderated or stabilized during 2010, registered unemployment in Croatia jumped to 18.8% by the end of December – the highest rate since 2005. Based on Labour Force Survey data, employment fell by about 4% in 2010, while at the same time the unemployment rate was close to 12%. Taking into account that a number of people decided to leave the labour market altogether, the unemployment rate may have been even higher. Since the beginning of the crisis about 141,000 jobs have been lost, most of which in manufacturing (67,000). This is approximately the same number of jobs that had been created in the period 2002-2008. The downward pressure on wages, which was felt already in 2009, has continued in 2010; real net wages were down by 1%.

Following the cuts in revenues as a consequence of the contracting economy and the simultaneous rise in public expenditures, the Croatian parliament approved a revision of the state budget in August 2010. Accordingly the general government deficit has been widened to 5.2% of the GDP from the earlier target of 3.3%. In October, the Croatian government presented the Economic and Fiscal Policy Guidelines 2011-2013, envisaging a gradual reduction of the general government deficit to 1.9% in 2013. Calculations are based on the assumption of 1.5%, 2% and 2.5% GDP increases in the respective years, driven primarily by foreign demand. According to the Minister of Finance about HRK 28 billion (slightly less than EUR 4 billion) will be needed to cover the budget deficit and to refinance outstanding debts in 2011. Additional financing should come from further privatizations. The fiscal responsibility law in force since January 2011 envisages the reduction of the general budget expenditures by 1 percentage point of the projected annual GDP every year until the primary fiscal balance becomes zero or positive. In addition the law stipulates that planned budgetary expenditures should be fully covered by revenues; this is to be ensured by the government.

In order to stimulate the economic growth the government presented ten large investment projects mainly in infrastructure which should start in March 2011. The funding for most of the projects is, however, still uncertain and the government is looking for investors. The growth impact of the programmes cannot be expected this year but only in the medium and longer run.

By the end of December 2010, 28 out of 35 chapters in the accession negotiations with the EU had been provisionally closed. Croatia's EU entry talks should be completed in (the first half of) 2011 – sensitive chapters like judiciary and competition are still in the negotiation process. Assuming that accession talks are going according to plan Croatia may join the European Union in 2013, considering the period needed for the ratification procedure in the parliaments of the current 27 EU member states. One of the still open issues will be fighting corruption, which has spread to all segments of society. (In December the former Prime Minister of Croatia, Ivo Sanader, was arrested in Austria on charges of corruption, money laundering and abuse of power.)

For 2011, wiiw expects GDP to rebound to 1% conditioned on a further improvement of external demand. In contrast to our earlier forecast, we expect a slower recovery of domestic demand mainly as a consequence of high unemployment. Considering 2011 is an election year there will be little room for essential reforms including an improvement of the fiscal situation – the compliance with the Fiscal Guidelines will become a big challenge. Employment will continue to contract as the labour market will react with a time lag to production growth and the unemployment rate is expected to stagnate or fall only slightly. This may trigger a further decline in household consumption. A more vigorous recovery of the labour market can be expected only from 2012 onwards. The current account deficit will remain within more moderate limits than before the crisis, ranging between 4-5% in the years to come. Restructuring and servicing the high foreign debt will remain one of the major challenges in the near future.

Table HR

Croatia: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 1)	2011	2012	2013
								Forecast	
Population, th pers., average	4442	4440	4436	4435	4429	4435	4435	4435	4435
Gross domestic product, HRK mn, nom.	264368	286341	314223	342159	333063	332000	343700	357600	377500
annual change in % (real)	4.2	4.7	5.5	2.4	-5.8	-1.5	1	2	3
GDP/capita (EUR at exchange rate)	8000	8800	9700	10700	10200	10300	10600	11000	11700
GDP/capita (EUR at PPP - wiiw)	12700	13500	15000	15800	15000	14900	.	.	.
Consumption of households, HRK mn, nom.	162165	172744	188952	202194	189638	189000	.	.	.
annual change in % (real)	4.4	3.5	6.2	0.8	-8.5	-1.5	0.5	2	3
Gross fixed capital form., HRK mn, nom.	65008	74792	82386	94281	82259	73300	.	.	.
annual change in % (real)	4.8	10.9	6.5	8.2	-11.8	-12	2	5	5
Gross industrial production 2)									
annual change in % (real)	4.6	4.2	4.9	1.2	-9.2	-1.4	3	3.5	4
Gross agricultural production									
annual change in % (real)	-8.7	4.4	-3.9	8.0	-0.8	.	.	.	.
Construction industry, hours worked 2)									
annual change in % (real)	-0.7	9.4	2.4	11.8	-6.6	-17	.	.	.
Employed persons - LFS, th, average	1573	1586	1615	1636	1605	1540	1525	1530	1550
annual change in %	0.7	0.8	1.8	1.3	-1.8	-4.1	-1	0.5	1
Unemployed persons - LFS, th, average	229	199	171	149	160	210	.	.	.
Unemployment rate - LFS, in %, average	12.7	11.1	9.6	8.4	9.1	12.0	11.5	10	9.5
Reg. unemployment rate in %, end of period	17.8	17.0	14.7	13.7	16.7	18.8	17	16.5	15.5
Average gross monthly wages, HRK	6248	6634	7047	7544	7711	7670	7700	7750	7800
annual change in % (real, net)	1.5	1.9	2.2	0.8	0.2	.	.	.	.
Consumer prices, % p.a.	3.3	3.2	2.9	6.1	2.4	1.1	2.5	2	2.5
Producer prices in industry, % p.a. 3)	2.7	2.7	3.5	8.3	-0.4	4.3	4	3.5	3
General governm.budget, nat.def., % GDP 4)									
Revenues	38.9	39.2	40.3	39.4	38.5	37.8	37.3	37.0	37.0
Expenditures	42.3	41.6	41.5	40.8	42.6	43.5	43.4	42.5	42.0
Deficit (-) / surplus (+) 5)	-3.5	-2.6	-1.2	-1.4	-4.1	-5.7	-6.1	-5.6	-5.0
Public debt, EU-def., in % of GDP 6)	38.3	35.5	32.9	28.9	35.3	40.9	45.9	49.9	52.0
Central bank policy rate, % p.a., end of period 7)	3.5	3.5	4.1	6.0	6.0	6.0	.	.	.
Current account, EUR mn	-1975.6	-2726.2	-3236.1	-4337.8	-2477.0	-1400	-2000	-2400	-2600
Current account in % of GDP	-5.5	-7.0	-7.6	-9.2	-5.5	-3.1	-4	-5	-5
Exports of goods, BOP, EUR mn	7220.3	8463.6	9192.5	9814.0	7703.2	8900	9600	10500	11400
annual growth rate in %	9.3	17.2	8.6	6.8	-21.5	15.5	8	9	9
Imports of goods, BOP, EUR mn	14738.3	16807.8	18626.5	20607.8	15090.1	14800	15500	16600	18300
annual growth rate in %	10.6	14.0	10.8	10.6	-26.8	-1.9	5	7	10
Exports of services, BOP, EUR mn	8052.6	8526.8	9114.8	10090.6	8453.9	8400	8700	9100	9600
annual growth rate in %	5.4	5.9	6.9	10.7	-16.2	-0.6	3	5	6
Imports of services, BOP, EUR mn	2734.9	2824.1	2847.4	3132.7	2778.3	2600	2700	2800	2900
annual growth rate in %	-4.6	3.3	0.8	10.0	-11.3	-6.4	2	3	3
FDI inflow, EUR mn	1467.9	2768.3	3679.0	4209.0	2128.6	1500	2300	2500	3000
FDI outflow, EUR mn	191.8	206.8	211.2	972.8	918.7	.	.	.	.
Gross reserves of NB excl. gold, EUR mn	7438.4	8725.3	9307.4	9120.9	10375.8	10660.3	.	.	.
Gross external debt, EUR mn 8)	25761.1	29273.9	32929.2	39950.2	44605.2	45000	.	.	.
Gross external debt in % of GDP 8)	71.9	75.1	76.8	85.5	97.8	100.1	.	.	.
Average exchange rate HRK/EUR	7.4000	7.3228	7.3360	7.2232	7.3398	7.2857	7.3	7.3	7.3
Purchasing power parity HRK/EUR	4.6756	4.7861	4.7280	4.8967	5.0111	5.0206	.	.	.

Note: Gross industrial production, construction output and producer prices in industry refer to NACE Rev. 2.

1) Preliminary and wiiw estimates. - 2) Enterprises with 20 and more employees. - 3) Domestic output prices. - 4) On accrual basis. - 5) Including change in arrears and non-recorded expenditures. - 6) According to ESA'95, excessive deficit procedure. - 7) Average weighted repo rates. - 8) From 2008 new reporting system (estimated data for non-financial enterprises).

Source: wiiw Database incorporating national statistics. Forecasts by wiiw.

Vladimir Gligorov

Macedonia:
Stable recovery, rising political tensions

Unlike most other countries in the Balkans, Macedonia did not experience either an investment or a credit boom before the crisis. The contraction of foreign trade was strong in 2009, but so was the recovery in 2010. Overall, the decline of GDP was less than 1% and the recovery will also be less than 1% in 2009 and 2010 respectively. More importantly, employment did not decline and in fact has been increasing, though the unemployment rate at above 30% is still catastrophically high.

Economic policy is anchored in the fixed exchange rate, which has proved to be biased towards stability rather than growth. However, given that foreign money has avoided Macedonia and given that for the most part wage increases have been subdued, the real exchange rate is probably not too overvalued and thus does not stand too much in the way of export recovery and growth based mostly on external demand. Indeed, some recovery of domestic demand, both private and public, is expected without significant threats to macroeconomic stability. Some speed-up of inflation is expected due primarily to rising food and energy prices.

Given the adopted policy mix – fixed exchange rate and balanced or slightly negative fiscal balance – growth depends on that in the main trading partners. Some of those are the immediate neighbours, who are mostly experiencing rather slow recovery. Thus, growth is constrained by the speed of recovery in the major exporting markets. Official expectations are for 3% growth in 2011, while a more realistic assessment would be in the vicinity of 2%. In any case, macroeconomic stability should not present a major problem.

Political stability, however, may be at risk because of the rather bad relationship between the two main ethnic Macedonian parties (parties tend to be organized along ethnic, mainly Macedonian and Albanian, lines but there are also parties of other ethnic groups) with the opposition Social-Democrats recently walking out of Parliament protesting the harassment of opposition media. Increased political tensions could lead to early elections, which would have an impact on the economy – though not necessarily a negative one. Early elections may prove stabilizing because of the growing tensions between the two ethnic communities. The recent spike of tensions has been triggered by mainly symbolic issues, first of all connected with religious differences, but the underlying causes are all of a social nature. Stagnation has in the past and will in the future lead to social problems and tensions and these will result in problems along ethnic lines. As a rule, in Macedonia, political conflicts are intra-ethnic while social tensions are inter-ethnic. Given that, early elections may be one way to try to politically resolve some of the social tensions, at least for a while.

Another political issue that has been plaguing the country is the long-standing dispute with Greece over the name of the country. This dispute is standing in the way of both NATO membership and the progress in negotiations with the EU. Macedonia has been a candidate country since 2005 and the European Commission has asked for the start of negotiations for two years now, but this cannot go past the Greek veto so far. There are no signs at this time that an agreement between Macedonia and Greece on this issue is any nearer now than it has been any time in the last twenty years.

In the short run, some speed-up of growth can be expected as external demand continues to improve and that feeds into investment and consumption. At the same time, some deterioration of external balances could be expected, but that should not threaten the exchange rate and the macroeconomic stability. Some growth of employment is also likely, though not enough to make a noticeable dent in the rate of unemployment.

In the medium run, a significant speed-up of growth cannot be expected. The policy mix is heavily geared towards stability and the external environment cannot improve all that much in order to spur a notable acceleration of growth. Indeed, continued weakness of growth and stability in the neighbouring Greece and the possible need to stabilize the Serbian economy will probably constrain growth and development in the medium run.

Table MK

Macedonia: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 [1)]	2011	2012 Forecast	2013
Population, th pers., average	2036.9	2040.2	2043.6	2046.9	2050.7	2100	2054	2056	2060
Gross domestic product, MKD mn, nom. [2)]	295052	320059	364989	411728	413351	427900	450000	477000	506000
annual change in % (real) [2)]	4.4	5.0	6.1	5.0	-0.8	0.5	2	3	3
GDP/capita (EUR at exchange rate)	2300	2500	2900	3200	3300	3300	.	.	.
GDP/capita (EUR at PPP - wiiw)	6600	7200	7700	8500	8500	8400	.	.	.
Consumption of households, MKD mn, nom. [2)3)]	227944	250309	279880	330399	316830	330000	.	.	.
annual change in % (real) [2)3)]	5.9	7.5	8.1	7.4	-3.1	2.5	2	3	3
Gross fixed capital form., MKD mn, nom. [2)]	48868	56485	71557	86403	81872	84000	.	.	.
annual change in % (real) [2)]	-6.1	7.7	17.1	5.4	-2.0	0	3	4	4
Gross industrial production [4)]									
annual change in % (real)	7.1	3.6	3.7	5.5	-7.7	-4.3	3	5	5
Gross agricultural production									
annual change in % (real)	0.3	4.8	-3.0	5.4	4.6	5.0	.	.	.
Construction industry									
annual change in % (real)	-20.5	-11.9	9.7	-9.6	-2.1	5	.	.	.
Employed persons - LFS, th, average	545.3	570.4	590.2	609.0	629.9	633	640	650	660
annual change in %	4.3	4.6	3.5	3.2	3.4	0.5	1.5	1.5	2
Unnemployed persons - LFS, th, average	323.9	321.3	316.9	310.4	298.9	305	.	.	.
Unemployment rate - LFS, in %, average	37.3	36.0	34.9	33.8	32.2	32.5	33	33	33
Reg. unemployment rate, in %, end of period	.	.	.	.	.	.	.	.	.
Average gross monthly wages, MKD [5)]	21330	23036	24136	26229	29922	30000	.	.	.
real growth rate, % (net wages) [5)]	2.0	3.9	5.5	1.9	25.0	1.5	.	.	.
Consumer prices, % p.a.	0.5	3.2	2.3	8.3	-0.8	1.7	3	3	3
Producer prices in industry, % p.a. [6)]	3.2	7.3	2.5	10.3	-6.5	8.5	.	.	.
General governm. budget, nat.def., % GDP [7)]									
Revenues	34.2	32.5	32.8	33.1	31.1	32	.	.	.
Expenditures	34.0	33.0	33.2	34.1	33.7	35	.	.	.
Deficit (-) / surplus (+)	0.2	-0.5	0.6	-0.9	-2.6	-3	-2	0	-1
Public debt, nat.def., in % of GDP	46.9	39.9	33.3	28.7	32.0	34	35	34	33
Central bank policy rate, in %, p.a., Dec [8)]	8.5	5.7	4.8	7.0	8.5	4.1	.	.	.
Current account, EUR mn	-122.5	-23.4	-421.2	-853.3	-483.3	-100	-300	-400	-400
Current account in % of GDP	-2.5	-0.4	-7.1	-12.7	-7.2	-1.4	-4	-5	-5
Exports of goods, BOP, EUR mn	1642.9	1914.0	2472.2	2684.2	1920.9	2400	2600	2900	3200
annual growth rate in %	22.2	16.5	29.2	8.6	-28.4	24.9	10	10	10
Imports of goods, BOP, EUR mn	2501.4	2915.5	3653.3	4434.9	3471.9	4000	4200	4600	5300
annual growth rate in %	10.7	16.6	25.3	21.4	-21.7	15.2	5	10	15
Exports of services, BOP, EUR mn	416.2	477.3	594.5	686.3	618.3	680	700	800	800
annual growth rate in %	14.4	14.7	24.5	15.4	-9.9	10.0	5	10	5
Imports of services, BOP, EUR mn	440.8	455.0	569.4	681.9	590.3	620	700	800	900
annual growth rate in %	8.3	3.2	25.2	19.8	-13.4	5.0	5	10	10
FDI inflow, EUR mn	77.2	344.8	506.0	399.9	181.0	150	200	200	250
FDI outflow, EUR mn	2.3	0.1	-0.9	-9.5	9.1	0	0	0	0
Gross reserves of NB, excl. gold, EUR mn	1028.0	1311.3	1400.1	1361.0	1429.4	1500	.	.	.
Gross external debt, EUR mn	2528.2	2503.4	2841.1	3304.2	3839.4	4100	.	.	.
Gross external debt in % of GDP	52.4	47.8	47.6	49.3	56.8	58.9	.	.	.
Average exchange rate MKD/EUR	61.30	61.19	61.18	61.27	61.32	61.52	61.2	61.2	61.2
Purchasing power parity MKD/EUR	21.96	21.93	23.14	23.57	23.78	24.25	.	.	.

1) Preliminary and wiiw estimates. - 2) According to ESA'95 (FISIM reallocated to industries, including non-observed economy, real growth rates based on previous year prices). - 3) Including Non-Profit Institutions Serving Households (NPISHs). - 4) Enterprises with 10 and more employees. - 5) From 2009 including allowances for food and transport, no comparable growth rates available. - 6) Domestic output prices. - 7) Refers to central government budget and extra-budgetary funds. - 8) Central Bank bills (28-days).

Source: wiiw Database incorporating national statistics. Forecasts by wiiw.

Vladimir Gligorov

Montenegro:
New government strives for stability

At the end of last year, the long-time prime minister stepped down and handed over the government to the vice-prime minister and the minister of finance in the previous government, Igor Lukšić. This has been the characteristic of Montenegrin adjustment to crisis. At the onset, early elections were held in order to garner the needed legitimacy to the government's policy responses to the crisis. Also, the application for membership in the European Union was handed in, which was approved in December 2010, so Montenegro is now a candidate country. Finally, the cabinet reshuffle is intended to further contribute to political stability and also increase the efficiency of the government. This concern with political stability proved appropriate because the effects of the crisis were strong and a number of unpopular measures had to be taken. The banking system went through a crisis and the same is true for industry. The government was able, however, to sustain the inflow of foreign investments and also had some fiscal reserves that it could use to support investments in infrastructure and did not have to resort to a significant decrease in employment. Still, the economy practically stagnated, with GDP growth of only 0.5% last year. This is mainly due to the recovery of industrial production and to the sustained performance of the tourist industry. However, in view of the decline of GDP of almost 6% in 2009, last year's small recovery is certainly not reassuring.

Employment has declined for two years in a row and unemployment has increased, but these effects are not as strong as in a number of other countries in the region. Similarly, real net wages have either not grown or have declined, but the adjustment is not strong due to the fact that Montenegro uses the euro and prices have been practically flat last year. Overall, the social effects of the crisis have been less strong than in other countries.

In the short run, the speed-up of the recovery depends on the performance of the tradable sector. As in other countries, imports have declined or stagnated, while exports of goods have been recovering following a steep decline in 2009. Exports o services have proved resilient and there are indications that those will do well this year and in the future. Foreign investments in tourism and public investments in infrastructure should also prove beneficial to growth and employment. Both foreign and public debts are not all that high and are not expected to be major constraints on economic policy. In the medium run, growth prospects will depend on the resilience of foreign investments. Montenegro continues to be attractive for investments in tourism and in real estate. As the country is expected to start negotiations for EU membership in the next year or so, that will certainly help. It will also be able to draw on EU funds more than before. The key risk is high dependency on the services sector and very weak industrial or any other production. In addition, regional risks are important and slow recovery of the Balkan economies will continue to drag the Montenegrin economy down. Thus, slow recovery is the most probably scenario in the medium run.

Table ME

Montenegro: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 1)	2011	2012	2013
								Forecast	
Population, th pers., average	623.3	624.2	626.2	628.8	630.0	631.5	632	633	634
Gross domestic product, EUR mn, nom. 2)	1815.0	2149.0	2680.5	3085.6	2981.0	3000	3200	3400	3600
annual change in % (real) 2)	4.2	8.6	10.7	6.9	-5.7	-1	2	3	3
GDP/capita (EUR at exchange rate)	2900	3400	4300	4900	4700	4800	.	.	.
GDP/capita (EUR at PPP - wiiw)	6900	8400	10000	10800	9700	9700	.	.	.
Consumption of households, EUR mn, nom. 2)	1268.0	1660.9	2369.0	2814.8	2503.7	2500	.	.	.
annual change in % (real) 3)	2.8	10	8	7	-4	0	2	2	3
Gross fixed capital form., EUR mn, nom. 2)	326.3	469.8	867.1	1180.2	797.6	800	.	.	.
annual change in % (real) 3)	12.0	8	10	8	-6	-2	2	2	5
Gross industrial production									
annual change in % (real)	-1.9	1.0	0.1	-2.0	-32.2	17.5	5	5	5
Net agricultural production	.	.	.	.	.	.	.	.	.
annual change in % (real)	-0.9	1.9	-11.0	10.0	3.0	2	.	.	.
Construction output total 4)	.	.	.	.	.	.	.	.	.
annual change in % (real)	18.4	28.0	23.6	20.7	-19.2	-10	.	.	.
Employed persons - LFS, th, average 5)	178.8	178.4	217.4	218.8	212.9	204	206	208	210
annual change in %	-4.5	-0.3	21.9	0.6	-2.7	-4	1	1	1
Unemployed persons - LFS, th, average 5)	77.8	74.8	52.1	45.3	50.9	51	.	.	
Unemployment rate - LFS, in %, average 5)	30.3	29.6	19.3	17.2	19.3	20	20	20	20
Reg. unemployment rate, in %, end of period 6)	25.2	20.5	16.5	14.4	15.1	17	.	.	.
Average gross monthly wages, EUR 7)	326	377	497	609	643	715	.	.	.
annual change in % (real, net)	6.7	12.0	15.0	14.6	7.6	3.0	.	.	.
Consumer prices, % p.a.	2.3	3.0	4.2	7.4	3.4	0.6	3	3	3
Producer prices in industry, % p.a. 8)	2.1	3.6	8.5	14.0	-3.9	-0.8	.	.	.
General governm.budget, nat.def., % GDP									
Revenues	39.4	45.4	61.1	49.1	45.5	45	.	.	.
Expenditures	42.0	42.7	52.9	47.5	49.0	50	.	.	.
Deficit(-)/Surplus(+)	-2.6	2.7	8.2	1.7	-3.5	-5	-3	-1	-1
Public debt, nat. def., in % of GDP	38.6	32.6	26.3	26.8	38.0	43	44	42	41
Central bank policy rate, % p.a., end of period 9)	12.1	9.9	9.1	9.4	9.4	9.5	.	.	.
Current account, EUR mn	-154.0	-531.2	-1060.6	-1564.3	-896.3	-700	-700	-700	-800
Current account in % of GDP	-8.5	-24.7	-39.6	-50.7	-30.1	-23.3	-22	-21	-22
Exports of goods, BOP, EUR mn	460.6	648.3	515.8	467.4	296.3	350	370	390	410
annual growth rate in %	1.9	40.8	-20.4	-9.4	-36.6	18.1	5	5	5
Imports of goods, BOP, EUR mn	974.3	1497.7	2090.0	2549.7	1668.0	1670	1750	1930	2120
annual growth rate in %	12.2	53.7	39.6	22.0	-34.6	0.1	5	10	10
Exports of services, BOP, EUR mn	329.8	418.0	673.0	750.6	680.5	730	800	880	970
annual growth rate in %	32.2	26.8	61.0	11.5	-9.3	7.3	10	10	10
Imports of services, BOP, EUR mn	134.2	220.9	234.0	351.2	295.9	310	330	360	400
annual growth rate in %	32.3	64.6	5.9	50.1	-15.8	4.8	5	10	10
FDI inflow, EUR mn	384.5	492.8	672.7	625.4	951.9	500	1000	1000	800
FDI outflow, EUR mn	3.6	26.1	115.0	73.7	32.9	50	50	50	50
Gross reserves of NB, excl. gold, EUR mn 10)	61.7	172.8	259.0	216.6	172.8	170	200	200	200
Gross external public debt, EUR mn	513.3	504.0	462.1	481.7	699.9	940	1000	1000	1000
Gross external public debt in % of GDP	28.3	23.5	17.2	15.6	23.5	31.3	30	29	29
Purchasing power parity EUR/EUR 11)	0.4198	0.4076	0.4293	0.4561	0.4864	0.4893	.	.	.

1) Preliminary and wiiw estimates. - 2) According to ESA'95 (including shadow economy, real growth rates based on previous year prices). - 3) wiiw estimate. - 4) Gross value added. - 5) Until 2007 as of October. - 6) In % of unemployed plus employment (excluding individual farmers). - 7) From 2007 wage data refer to employees who received wages (previously wages were divided by all registered employees in enterprises); comparable value for 2006: 433. - 8) Domestic output prices. - 9) Average weighted lending interest rate of commercial banks (Montenegro uses the euro as national currency). - 10) Refer to reserve requirements of Central Bank. - 11) Benchmark results 2005 from Eurostat and wiiw estimates.

Source: wiiw Database incorporating national statistics. Forecasts by wiiw.

Josef Pöschl

Turkey:
Calming-down of a growth bonanza

In the first three quarters of 2010, the GDP grew by over 8.9%. The fact that this was a swift response to an 8% GDP decline in the same period of the previous year does not spoil the positive impression: other crisis-hit countries were unable to achieve such a brilliant regain of lost terrain, and Turkey was the region's growth leader of the year 2010.

The contrast between decline in 2009 and growth in 2010 was even stronger in the first quarters of those two years (-14.6% against +11.8%). The engine of recovery was an increase in domestic demand. Household consumption started growing again soon after the slump. Later on, private gross fixed investment followed in line with substantially improved business expectations. Both the government and the central bank did their best to support these developments. The government acted on the revenue as well as on the expenditure side. This was a deliberate deviation from past years' efforts to secure substantial primary surpluses. The central bank has reduced its policy rate. The swift recovery should not be attributed to economic policy alone. In Turkey, private sector agents have a long experience with sudden crises, so they may have suffered less of a shock than was the case in other countries. At the same time, it seems that the banking sector felt less threatened than in other countries and maintained a relatively high degree of 'business as usual'. In 2001, this sector had triggered a severe crisis, and the reform steps thereafter have made commercial banking relatively crisis-resistant.

A 'meagre' 5.5% year-on-year growth in the third quarter of 2010 signalized a calming-down of a remarkable growth bonanza. The fourth quarter's rate is likely to be around 4 to 5%. This is also good news, as extremely high growth in the midst of close-to-stagnating trading partners has provoked an import expansion, which exceeded export growth by far. In euro terms, exports of goods in 2010 remained by about 6% below the pre-crisis level of 2008, whereas imports came very close to it. Consequently, the current account deficit has surpassed pre-crisis levels by climbing to about EUR 34 billion or somewhat over 6% of the GDP. At the end of 2010, the central bank's gross reserves were much higher compared to two years before, so it was inflow of capital, which covered the current account deficit. Loans rather than foreign direct or portfolio investments have closed the gap. The indebtedness of the government is moderate. However, as we have learnt in recent months from experience in other countries, in the end private sector debt can be dangerous too.

The central bank is eager to put a brake on capital inflows. To achieve this, the bank reduced its policy rate to 6.5% last December and to 6.25% last February. The exchange rate reacted, as expected, with something highly welcome – slight currency devaluation. More of the same could help to avoid an erosion of Turkish competitiveness. The country's favourable macro data tends to fuel appreciation pressure, and in view of the high current account deficit this would be dangerous. The central bank is much less scared about inflation, which has remained in a range between 5 and 10% annually for quite some time now. To prevent exaggerated credit growth, the central bank has increased the commercial banks' reserve requirements. The aim of this measure is not to fight inflation, but to contain import growth. The policy of low interest rate has positive spillover effects on the fiscal side, and the same is true for the relatively high rate of inflation. Currently, further decline of inflation is more likely than an upward trend.

From the extreme widening of the current account deficit we conclude that a growth differential against the main trading partners would not be sustainable in the longer run. For example, five percentage points above EU average could be problematic. Its tradable sector competes mainly in the low-price segment of international trade, and there competition is fierce. Turkey's revenues from exports to the EU stem mainly from clothing, transport equipment (predominantly for commercial use), textiles, electrical machinery and agri-food products. Among Turkey's competitors are Asian countries with cheap labour that are specialized on labour-intensive products and new EU-member states with specialization in capital-intensive production. In none of these product groups, Turkey surpassed the pre-crisis level (October 2009-March 2010 versus October 2007-March 2008). In this respect, Poland and China were more successful in clothing; India, Romania and South Africa did better in terms of transport equipment, and Malaysia, Korea and China were more successful in exporting electrical machinery. Some of those countries performed better than Turkey in spite of a real exchange rate appreciation. For example, real appreciation of China contrasted with Turkey's depreciation. Turkey lost shares in EU markets, but gained shares in Middle East Asia and Northern Africa. Nevertheless, Turkey's post-crisis exports grew less than the total world exports. It seems that Turkey's current account problem is of long-term nature and may turn into a major threat in the case of continuation of high growth. The central bank is aware of this and will continue its efforts to calm growth dynamics down. We expect a growth rate of at least 7.5% in 2010, 4.4% in 2011 and somewhat less than that in 2012 and 2013. Should the central bank's effort prove as not successful, so that high growth would continue to be accompanied by a widening current account deficit, Turkey could experience one more episode of sudden GDP drop, currency depreciation and swift recovery thereafter. Most likely, Turkey is part of the league of fast-growing emerging markets. Pessimists could, however, fear that there is a similarity to Spain in pre-crisis years, pointing to a level of relative prices which may prove to be not sustainable. If so, this could lead to a crisis at some point of time, with strong currency depreciation as a relief – for some time at least.

Turkey will go to the polls in June 2011. Most likely, Prime Minister Erdoğan's party will win a majority again. It will not necessarily be as strong as it has been up to now. The new government will probably start a tightening of expenditures in the second half of 2011, and continue that way in 2012-2013. This tightening could be less pronounced, should the government achieve high revenues from a privatization campaign mainly related to the energy sector, which is currently under preparation.

Challenges will be manifold. Urbanization has gone far and will progress further, and this will require high expenditures on infrastructure. The educational system will need an upgrade, and regional cohesion will remain a matter of concern.

Table TR

Turkey: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 1)	2011	2012 Forecast	2013
Population, th pers., average 2)	68582	69421	70256	71079	71861	72500	73200	73900	74600
Gross domestic product, TRY bn, nom.	648.9	758.4	843.2	950.5	952.6	1110	1230	1350	1480
annual change in % (real)	8.4	6.9	4.7	0.4	-4.5	7.5	4.4	4.0	3.7
GDP/capita (EUR at exchange rate)	5600	6000	6700	7000	6100	7700	8400	9100	9400
GDP/capita (EUR at PPP - wiiw)	9500	10500	11300	11700	10700	11500	12200	13000	14100
Consumption of households,TRY bn, nom.	465.4	534.8	601.2	663.9	681.5	790	.	.	.
annual change in % (real)	7.9	4.6	5.5	-0.3	-2.3	6.5	3.7	3.0	2.8
Gross fixed capital form., TRY bn, nom.	136.5	169.0	180.6	189.1	160.7	210	.	.	.
annual change in % (real)	17.4	13.3	3.1	-6.2	-19.2	23.9	14.9	10.4	10.0
Gross industrial production									
annual change in % (real)	5.6	7.3	7.0	-0.6	-9.7	12.7	10.0	7.0	7.0
Gross agricultural production									
annual change in % (real)	6.6	1.3	-7.3	.	.	.	.	.	.
Construction industry									
annual change in % (real)	21.5	18.4	5.5	-7.6	-16.3	14.0	12.0	9.0	9.0
Employed persons - LFS, th, avg.	20074	20433	20750	21193	21271	22600	23000	23450	23800
annual change in %	.	1.8	1.5	2.1	0.4	6.2	1.8	2.0	1.5
Unemployed persons - LFS, th, average	.	1950	2016	2278	3053	2760	2520	2600	2700
Unemployment rate - LFS, in %, average	.	8.8	8.9	9.8	12.7	10.9	9.9	10.0	10.2
Reg. unemployment rate, in %, average	.	.	.	.	.				
Average gross monthly wages, manuf.ind., TRY	1162	1301	1437	1590	.	.	.	.	.
annual change in % (real)	4.3	2.1	1.6	0	.	.	.	.	.
Consumer prices, % p.a.	8.1	9.3	8.8	10.4	6.3	8.6	6.0	5.5	5.5
Producer prices in industry, % p.a.	7.1	9.7	6.0	13.0	1.0	6.2	5.5	4.5	4.5
General governm. budget, EU-def., % GDP 3)									
Revenues	.	.	.	32.3	33.8	34	34	34	34
Expenditures	.	.	.	34.5	40.5	38	37	36	36
Deficit (-) / surplus (+)	.	0.8	-1.0	-2.2	-6.7	-4	-3	-2	-2
Public debt, EU-def., in % of GDP 3)	52.3	46.1	39.4	39.5	45.4	48	49	48	47
Central bank policy rate, %, p.a., end of period 4)	17.5	22.5	20.0	17.5	9.0	6.5	6.0	6.0	6.0
Current account, EUR mn	-17843	-25640	-27954	-28520	-10261	-34400	-37900	-38300	-38500
Current account in % of GDP	-4.6	-6.1	-5.9	-5.7	-2.3	-6.2	-6.2	-5.7	-5.5
Exports of goods, BOP, EUR mn	62989	74556	84174	95730	78697	89900	98900	108800	119500
annual change in %	14.3	18.4	12.9	13.7	-17.8	14.2	10.0	10.0	9.8
Imports of goods, BOP, EUR mn	89579	107255	118319	131779	96564	130500	143500	155000	167000
annual change in %	22.1	19.7	10.3	11.4	-26.7	35.1	10.0	8.0	7.7
Exports of services, BOP, EUR mn	21512	20348	21109	23677	18250	24500	26600	29500	32100
annual growth rate in %	16.6	-5.4	3.7	12.2	-22.9	34.2	8.6	10.9	8.8
Imports of services, BOP, EUR mn	9240	9507	11372	12036	8713	13800	15200	16400	17700
annual growth rate in %	13.3	2.9	19.6	5.8	-27.6	58.4	10.1	7.9	7.9
FDI inflow, EUR mn	8063	16076	16087	12421	5927	5000	8000	9000	7000
FDI outflow, EUR mn	855	736	1537	1733	1115	1100	1500	1500	1500
Gross reserves of CB, excl. gold, EUR mn	42820	46251	49804	51022	49088	61000	65000	68000	65000
Gross external debt, EUR mn	143994	157774	169452	199662	186482	209000	.	.	.
Gross external debt in % of GDP	35.3	38.8	34.5	45.1	42.2	39.0	.	.	.
Average exchange rate TRY/EUR	1.6800	1.8100	1.7900	1.9100	2.1600	2.0000	2.0000	2.0000	2.1000
Purchasing power parity TRY/EUR	0.9919	1.0402	1.0641	1.1454	1.2363	1.3293	1.38	1.41	1.41

Note: Gross industrial production and construction output refer to NACE Rev. 2.

1) Preliminary and wiiw estimates. - 2) TSI projections. - 3) According to ESA'95 excessive deficit procedure. - 4) From 2010 one-week repo rate, overnight lending rate before.

Source: National statistics (Central Bank, Turkish Statistical Institute - TSI, etc), Eurostat. Forecasts by wiiw.

Mario Holzner

Albania:
Something is rotten

After the killing of three persons during a violent anti-government demonstration in January 2011, it once again became clear that something is rotten in the state of Albania. The political class does not seem to act in a mature and responsible way. Communication with the political opponent is rude and uncompromising. This has already cost the country an opportunity to receive EU candidate status. However, in economic terms Albania is doing fairly well. In 2010, the estimated GDP growth of about 4% surpassed previously expected forecasts by some 1.5 percentage points, largely due to a spectacular export boom. In 2011, a similar export growth is unlikely to be maintained. The political stalemate is not expected to have a major economic impact in the short run; the GDP growth will accelerate in the coming 2-3 years.

While not meeting the highest standards for democratic elections, the June 2009 parliamentary elections marked tangible progress with respect to earlier elections. Still, the socialist opposition led by Edi Rama, the mayor of Tirana, is still questioning the lawfulness of the elections. Since then, in regular demonstrations the opposition demands new elections. After a recent case of blatant corruption in the government of conservative Prime Minister Sali Berisha, anti-governmental demonstrations flared up. On January 21st 2011 three protestors were shot dead at an opposition rally in Tirana in a melee close to the prime minister's office. The suspects are assumed to be members of the Republican Guard that was protecting the prime minister's office. However, Berisha rejected an order by the general prosecutor for the arrest of six high-ranking Republican Guard officers suspected of ordering the use of firearms against protesters. As a consequence, the political polarization is further growing and starts to bear strange fruits. The Prime Minister has declared that he was the victim of a failed coup attempt, organized by the opposition with the help of the general prosecutor, the president (paradoxically both close to the Prime Minister's conservative Democratic Party), as well as the secret service and the media. As a response Berisha has ordered the Ministry of Culture to organize a concert with Lady Gaga or some other top pop star in order to restore the country's image as 'Miss World for tourists from all over the world', as he put it. The representatives of the EU and the US are trying to calm the political actors. For the sake of Albania's EU integration process it can be hoped that the political conflict becomes defanged and stays under control until the next parliamentary elections which are scheduled for 2013 at the latest.

The political calamities, if not further escalating, should not be too damaging for the economy, at least in the short run. Foreign companies investing in Albania are well aware of the political risks and the wide spread corruption. For 2010 FDI inflows will most likely mark an all-time high of about EUR 740 million. However, if the political system remains characterized by personal animosities among the main political leaders reflecting particulate interests of clans and single provinces while disregarding the interests of the broad majority of population, the economy will be damaged in the medium and long run. Especially this might become a major stumbling block on the path to EU membership and subsequent EU transfers and integration into European production networks.

At the moment economic growth is mostly driven by the booming export sector. Main driver is the export of electricity due to exceptionally high water levels in Albania's hydro power stations. Only the energy exports from June to November 2010 are equal to the 2009 full year exports in this sector. However, latest export data for manufactured products and raw materials are equally exciting. Certainly the international trade rebound and a slight devaluation of the Albanian lek vis-à-vis the euro during 2010 was helpful in this respect. Cumulated exports until November 2010 have increased by more than 50% year-on-year (yoy), imports only by a few percentage points. Consequently it's the industry, the trade and the transport sectors that have most contributed to economic growth in 2010. Lately, domestic demand has developed quite sluggish. The construction sector has sharply decreased. Government demand is falling. In the third quarter of 2010 the sale of household equipment and the sale, maintenance and repair of motor vehicles has been declining by 5% and 7%, respectively. Especially the latter item is a good indicator for the future development of domestic demand. In addition, the consumer confidence indicator, although on a high level, was falling slightly in the third quarter of 2010. For 2011 this will result in a lower GDP growth rate. All the more that it will be impossible to increase exports much further in the short run. Rising energy prices might be helpful (with regard to second round growth effects) but one cannot expect a similar high level of rainfall as in 2010 to boost electricity production once again. The financing of a higher trade deficit should still be possible. In the first three quarters of 2010 data of remittances inflows shows a slight increase yoy. If this trend continues and if the government stops further expenditure cuts (which is quite likely due to local elections in May 2011), we can expect a growth rate of 3.2% in 2011. For 2012 and 2013 we forecast an improvement in economic growth to 4% and 5% respectively. Needless to say, that this depends on a further recovery of the European economy and an improvement of the political climate in Albania.

Table AL

Albania: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 [1]	2011	2012	2013
								Forecast	
Population, th pers., average	3142	3147	3161	3182	3194	3210	3220	3240	3260
Gross domestic product, ALL bn, nom. [2]	814.8	882.2	967.7	1088.1	1143.6	1220.0	1300	1390	1520
annual change in % (real) [2]	5.7	5.4	5.9	7.7	3.3	4.0	3.2	4	5
GDP/capita (EUR at exchange rate)	2100	2300	2500	2800	2700	2800	.	.	.
GDP/capita (EUR at PPP - wiiw)	5000	5500	5800	6400	6500	6800	.	.	.
Consumption of households, ALL bn, nom. [2]	634.5	680.3	775.1	861.9	910	909	.	.	.
annual change in % (real) [2]	6.0	4.7	10.7	6.7	3	3	5	7	9
Gross fixed capital form., ALL bn, nom. [2]	301.4	343.9	374.1	415.1	430	400	.	.	.
annual change in % (real) [2]	4.9	13.0	5.5	9.5	5	-7	1	5	12
Gross industrial production [3]									
annual change in % (real)	11.7	12.1	-9.7	9.4	0.6	20	5	15	7
Gross agricultural production [4]									
annual change in % (real)	0.9	3.1	2.7	7.3	3.3	9	2	3	3
Construction output total [3]									
annual change in % (real)	6.3	10.5	12.2	10.7	0.2	-25	1	3	8
Employed persons - LFS, th, Oct	.	.	1197.7	1123.3	1160.0	1100	1060	1100	1150
annual change in %	.	.	.	-6.2	3.3	-5	-4	4	5
Employment reg. total, th pers., end of period	932.1	935.1	965.5	974.1	899.3	916.9	900	930	970
annual change in %	0.1	0.3	3.3	0.9	-7.7	-2.0	-2	3	4
Unemployed persons - LFS, th, Oct	.	.	184.8	168.6	185.0	210	200	190	180
Unemployment rate - LFS, in %, Oct	.	.	13.5	13.0	13.8	15	15	14	13
Reg. unemployment rate, in %, end of period	14.1	13.8	12.9	12.7	13.9	13.5	13	13	12
Average gross monthly wages, ALL	19993	21842	27350	27951	31900	33870	.	.	.
annual change in % (real, gross)	2.6	6.7	21.6	-1.1	11.7	3	3	5	10
Consumer prices, % p.a.	2.4	2.4	2.9	3.4	2.3	3.5	3	3	4
Producer prices in industry, % p.a.	4.9	0.8	3.5	6.5	-1.6	0.1	3	4	6
General governm.budget, nat.def., % GDP									
Revenues	25.1	26.0	26.0	26.8	26.2	26.6	26	27	28
Expenditures	28.5	29.3	29.6	32.3	33.2	29.7	29	30	35
Deficit (-) / surplus (+)	-3.5	-3.3	-3.5	-5.5	-7.0	-3.0	-3	-3	-7
Public debt, nat. def., in % of GDP [5]	58.1	56.0	53.9	55.2	61.6	61	61	60	62
Central bank policy rate, % p.a., end of period [6]	5.0	5.5	6.3	6.3	5.3	5.0	5.0	5.3	5.5
Current account, EUR mn	-589.0	-470.9	-831.1	-1370.2	-1345.5	-900	-1200	-1500	-2000
Current account in % of GDP	-9.0	-6.6	-10.6	-15.5	-15.5	-10.2	-12.6	-13.7	-16.1
Exports of goods, BOP, EUR mn	530.2	630.6	786.3	917.5	750.7	1150	1200	1400	1600
annual growth rate in %	9.2	18.9	24.7	16.7	-18.2	53.2	4	17	14
Imports of goods, BOP, EUR mn	2006.9	2289.6	2890.4	3348.9	3054.4	3150	3600	4200	5000
annual growth rate in %	13.9	14.1	26.2	15.9	-8.8	3.1	14	17	19
Exports of services, BOP, EUR mn	967.3	1156.6	1415.1	1687.8	1718.4	1680	1900	2200	2400
annual growth rate in %	19.8	19.6	22.3	19.3	1.8	-2.2	13	16	9
Imports of services, BOP, EUR mn	1107.7	1188.0	1402.3	1618.4	1597.5	1480	1600	1800	2100
annual growth rate in %	30.6	7.2	18.0	15.4	-1.3	-7.4	8	13	17
FDI inflow, EUR mn	212.6	258.6	481.1	675.4	706.4	740	600	700	800
FDI outflow, EUR mn	3.3	8.3	11.1	55.4	26.1	-10	20	30	40
Gross reserves of NB excl. gold, EUR mn	1171.6	1329.2	1415.9	1626.1	1607.8	1842.1	.	.	.
Gross external debt, EUR mn [7]	1647.1	1874.2	2090.9	3078.9	3314.4	3600	.	.	.
Gross external debt in % of GDP	24.8	26.3	26.3	35.0	40.0	40.9	.	.	.
Average exchange rate ALL/EUR	124.19	123.08	123.63	122.80	132.06	137.79	137	127	122
Purchasing power parity ALL/EUR [8]	52.11	51.21	52.38	53.07	55.30	56.17	.	.	.

1) Preliminary and wiiw estimates. - 2) According to ESA'95 (including non-observed economy, real growth rates based on previous year prices). - 3) Gross value added. - 4) Gross value added of agriculture, forestry and fishing. - 5) Based on IMF data. - 6) One-week repo rate. - 7) Until 2007 based on IMF data. - 8) Benchmark results 2005 from Eurostat and wiiw estimates.

Source: wiiw Database incorporating national statistics and IMF. Forecasts by wiiw.

Josef Pöschl

Bosnia and Herzegovina:
The choice between take-off and slow growth

In previous forecasts, we predicted that in the case of Bosnia and Herzegovina (BiH) the international financial and economic crisis would trigger a relatively modest GDP decline. In fact, the GDP fell by 2.9% in 2009 and stabilized on that lower level in 2010 (our estimate is 0.8% growth). Regarding resumption of growth, we took a rather cautious stance – and still keep doing so (by predicting 2.8% growth in 2011 and 3% in the two subsequent years). The key question is which forces could initiate the return to a path of high growth.

The banking sector's focus switched from credit expansion to the collection of receivables. The sector is stable, whereas the micro credits industry is in deep trouble. Remittances from abroad have stabilized on a lower level; all levels of government as well as enterprises in the public utilities sphere were confronted with unexpectedly low revenues and had to economize on the expenditure side. Private investment dropped. As a result, employment has declined and unemployment rose. The number of poor has increased considerably. All this started in 2009 and became fully visible in 2010.

In 2010, signs of recovery became visible too, namely in that relatively small segment of the BiH economy which produces tradable goods. On international markets, the demand for metals and metal products and some other materials went up, something that provoked a boom in the country's exports. They rose by 25%. Imports rose too, but merely by somewhat less than 10%, while domestic income remained almost stagnant – the value-added creation of the export sector is too small to provoke a larger immediate move of the whole economy.

There are some burdens the country will have to live with for long time. One is the ratio between the number of persons with regular employment, which is low, and the number of retired persons, which is huge. An imbalance between the number of persons of working age and the availability of workplaces provokes high unemployment. The crisis has led to deterioration. Other burdens would be removable in the case of good-will of the main players. A new constitution could make the public sector less complicated, less costly and much more efficient and transparent. Ample space for reforms would also be in the field of business environment. A good example is the agrifood sector. Currently, net imports of agricultural products and processed food are high. Because institutional backstopping is lacking, the products of BiH farmers and food processors have very limited access to foreign markets. They do not have enough power to enforce a change, so they are scared about the recent removal of tariffs for EU food in the context of the Stability and Association Agreement. Repeatedly, international comparisons have confirmed that the business environment in BiH is less favourable than in many other countries. It is not supportive to business start-ups by domestic persons, and the country could be made more attractive to foreign investors in the manufacturing sector.

A good example for inertia, which is a common feature of West Balkan countries, has become visible in the CEFTA context. Under pressure from outside – especially the EU – the countries signed a free-trade agreement several years ago. To be able to continue with the protection of domestic interests, the governments kept non-tariff barriers untouched or made even stronger use of them than previously. A key barrier is non-recognition of the partner countries' certificates. Recently, BiH and Serbia have decided to take a pioneer role. They plan to introduce mutual recognition through a bilateral agreement.

In the elections of last October, a considerable part of the electorate expressed a wish for change. It was clear from the beginning that forming a new government on the state level would be difficult and time-consuming. In early March 2011, the old government was still running the show. From the very beginning, the social democrats, backed by many more votes than previously, have insisted on a joint programme as precondition for forming a coalition. The potential partners kept rejecting this approach, which for BiH would be a novelty. Soon, politicians and political parties got involved in power struggles, which they try to sell to the public as a fight for justice in ethnicity terms. This has led to a deadlock. The international community is concerned, and interventions are manifold, high-ranking German and US government representatives included. The influence of central government bodies is at stake: it was extremely limited from the very beginning, and it took a lot of efforts to pep it up, to some degree at least, over the last 15 years. The situation has invited the two entities, the Federation of BiH and Republika Srpska, to dominate the scene and expand their influence. Republika Srpska has managed to make use of this opportunity, whereas in the Federation, forming a government has proved as similarly difficult as on the central level. For the time being, those BiH citizens who have not disposed of their Croat or Serb passport feel relief after having got the right of visa-free travel to Schengen countries.

Where are the forces that could trigger a strong business upswing? Private consumption is not likely to become the engine of growth in the near future, as unemployment will remain high, wage growth will remain low and remittances from abroad are not likely to rise. We can count with a continuation of export growth, as we can see from favourable January 2011 data, but its GDP impact will remain moderate due to reasons mentioned above. The various governments (central, entity canton levels) will hardly be in a position to expand their expenditures largely. The remaining potential engine of growth resumption is private investment. To activate it, the governments on the different state levels would need to join forces to improve the business environment substantially. This should create better conditions for exports of goods and services with high value-added content and be supportive to the establishment of a regime of barrier-free intra-CEFTA trade. The fact that something, but not very much, will happen in this direction is the background for our forecast of 2.8% GDP growth in 2011 and 3% thereafter. Inflation will remain low and unemployment high. The current account in percent of GDP will not return to previous high levels.

Table BA

Bosnia and Herzegovina: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 1)	2011	2012 Forecast	2013
Population, th pers., average	3843	3843	3843	3842	3843	3843	3843	3843	3842
Gross domestic product, BAM mn, nom. 2)	17127.4	19252.5	21760.2	24702.5	23994.1	24690	25500	26500	27600
annual change in % (real) 2)	3.9	6.1	6.2	5.7	-2.9	0.8	2.2	3	3
GDP/capita (EUR at exchange rate)	2300	2500	2900	3300	3200	3300	3400	3500	3700
GDP/capita (EUR at PPP - wiiw)	5200	5700	6300	6600	6300	6400	.	.	.
GDP by expend. approach, BAM mn, nom. 2)	18338.2	21366.1	24689.1	28106.1	27427.5	.	.	.	.
Consumption of households, BAM mn, nom. 2)	16513.9	18064.3	19911.3	22451.3	21528.4	21980	.	.	.
annual change in % (real) 2)	6.2	4.5	5.9	5.9	-4.2	0	1	2	2
Gross fixed capital form., BAM mn, nom. 2)	4889.5	4756.8	6446.4	7521.0	5638.0	5760	.	.	.
annual change in % (real) 2)	18.5	-9.4	28.8	10.9	-24.0	0	2	5	5
Gross industrial production 3)									
annual change in % (real)	10.8	11.5	6.4	11.0	-3.3	1.6	7	10	10
Gross agricultural production									
annual change in % (real)	0.0	3.2	-1.6	.	.	.	.	.	.
Employed persons - LFS, th, April	.	811.0	849.6	890.2	859.2	842.8	840	845	850
annual change in %	.	.	4.8	4.8	-3.5	-1.9	-0.3	0.6	0.6
Employees total - reg., th, average	642.8	653.3	686.1	705.6	697.6	685	685	690	700
annual change in %	0.9	1.6	5.0	2.9	-1.1	-1.8	0.0	0.7	1.4
Unemployed persons - LFS, th, April	.	366.8	346.7	272.0	272.3	315.1	315	310	300
Unemployment rate - LFS, in %, April	.	31.1	29.0	23.4	24.1	27.2	27	27	26
Reg. unemployment rate, in %, end of period	44.1	44.1	42.5	40.6	42.4	43	43	42	42
Average gross monthly wages, BAM	796	869	954	1113	1204	1215	1250	1300	1400
annual change in % (real, net)	3.4	2.3	8.4	8.4	5.6	-0.9	.	.	.
Consumer prices, % p.a.	3.0	6.2	1.5	7.5	-0.4	2.1	1	1	1
Producer prices in industry, % p.a.	.	.	.	.	.	.	.	.	
General governm.budget, nat.def., % GDP									
Revenues	41.6	44.6	45.2	44.1	43.1	42.5	43.0	44.0	44.0
Expenditures	39.2	41.7	44.0	46.3	47.6	47.0	46.5	46.5	46.0
Deficit (-) / surplus (+)	2.4	2.9	1.2	-2.2	-4.5	-4.5	-3.5	-2.5	-2.0
Public debt, nat. def., in % of GDP 4)	25.6	22.0	29.8	30.8	33.4	36	38	39	40
Central bank policy rate, % p.a., end of period 5)	.	.	.	.	.	.	.	.	.
Current account, EUR mn 6)	-1499.6	-783.5	-1190.6	-1819.0	-840.0	-900	-900	-800	-800
Current account in % of GDP	-17.1	-8.0	-10.7	-14.4	-6.8	-7.1	-7	-6	-6
Exports of goods, BOP, EUR mn 6)	2059.7	2687.2	3091.5	3522.0	2920.2	3650	4000	4400	4850
annual growth rate in %	22.8	30.5	15.0	13.9	-17.1	25	10	10	10
Imports of goods, BOP, EUR mn 6)	6021.5	6092.9	7233.6	8344.6	6326.6	6900	7250	7600	7950
annual growth rate in %	12.5	1.2	18.7	15.4	-24.2	9	5	5	5
Exports of services, BOP, EUR mn 6)	798.5	904.3	1061.7	1125.6	1002.3	950	1050	1150	1260
annual growth rate in %	14.7	13.2	17.4	6.0	-11.0	-5	11	10	10
Imports of services, BOP, EUR mn 6)	352.4	369.9	422.3	482.7	453.3	420	440	460	490
annual growth rate in %	1.0	4.9	14.2	14.3	-6.1	-7	5	5	7
FDI inflow, EUR mn 6)	493.1	610.9	1519.8	636.3	176.8	200	220	300	400
FDI outflow, EUR mn 6)	0.4	3.2	20.5	9.2	-6.7	0	0	0	0
Gross reserves of NB excl. gold, EUR mn 7)	2160.0	2787.4	3424.9	3218.9	3143.8	3267.6	.	.	.
Gross external debt, EUR mn 8)	2217.9	2081.5	2025.4	2168.0	2676.2	3195.2	.	.	.
Gross external debt in % of GDP	25.3	21.1	18.2	17.2	21.8	25.3	.	.	.
Average exchange rate BAM/EUR	1.9558	1.9558	1.9558	1.9558	1.9558	1.9558	1.96	1.96	1.96
Purchasing power parity BAM/EUR 9)	0.8576	0.8751	0.9007	0.9698	0.9897	1.0003	0.95	0.95	0.95

1) Preliminary and wiiw estimates. - 2) According to ESA'95 (including non-observed economy, real growth rates based on previous year prices). - 3) wiiw estimates based on weighted averages for the two entities (Federation BH and Republika Srpska). - 4) Based on IMF data. - 5) Bosnia and Herzegovina has a currency board. There is no policy rate and even no money market rate available. - 6) Converted from national currency with the average exchange rate. - 7) Including investment in foreign securities. - 8) Gross external public debt. - 9) Benchmark results 2005 from Eurostat and wiiw estimates.

Source: wiiw Database incorporating national statistics and IMF. Forecasts by wiiw.

Vladimir Gligorov

Serbia:
Social tensions rise ahead of elections

The key adjustment mechanism during the crisis has been the exchange rate. Initial devaluation, in late 2008 and early 2009, was followed by steady depreciation, until the end of December 2010 and the beginning of 2011. This has led to growth of exports and to a decline or slow recovery of imports. That, however, goes along with a decline of private consumption and investment, with public consumption compensating only partially the shortfall in domestic demand. In addition, inflation has accelerated in part because of rising prices of food and energy since mid-2010. Altogether, this has resulted in growth of GDP of 1.5% (this is a preliminary figure) and in a decline of real incomes.

In addition, the fall in employment has been dramatic. From April 2008 to October 2010 (labour force surveys are taken twice a year, in April and October) about 450 thousand jobs were lost, which is about 16% of currently employed. The losses have occurred in the formal as well as in the informal sectors. Approximately one quarter of employed are working informally and about one quarter of the lost jobs are in the informal sector too. This indicates that the informal sector is not a safety valve but shares the growth prospects of the formal sector. This goes together with the labour mobility which is away from rural and into urban centres. That is caused by the widening regional disparities, in particular between the capital city and the regional centres and the rest of the country. There is also an increase in outward migration, but there are no reliable data on the current flows. However, there are reports from the receiving countries in Europe, but also oversees, that the number of asylum seekers is increasing as is the number of illegal immigrants.

Finally, there is a speed-up of inflation. Since the summer of 2010, the rise in food prices and rising inflationary expectations have pushed the headline rate of inflation into double digits (annualized). While the increase in food prices is mostly a supply problem, due to shortfalls in agricultural production in the country and abroad, inflationary expectations have been pushed up due to the expected lifting of the freeze on wages and pensions, which was put in place as part of a stand-by agreement with the IMF at the beginning of the crisis in late 2008. That has led the central bank to start raising its interest rate and to signal that it would continue doing so as long as the rate of inflation does not go down to the targeted one, which is 4.5% plus or minus 1.5%. So far, the effects on inflationary expectations have been nil.

These developments put together have resulted in a further impoverishment of those who were already poor but also of the middle classes, in particular those employed by the public sector. That accounts for the wave of strikes and political protests that have occurred at the beginning of 2011. Again, expectations play a part because general elections are due early next year and the government as well as the opposition parties are seen as being ready to approve wage and other income raises. Also, it is not expected that the central bank will tighten its monetary policy too much even in the face of increased inflationary pressures. Indeed, the expectation is that the central bank will try to strengthen the exchange rate of the dinar as the main instrument to tie down inflation. This is already happening with the appreciation of the dinar at the beginning of 2011. Of course, with entrenched inflation and high inflationary expectations, an appreciating currency is bound to wipe out the gains in competitiveness achieved with the former depreciation. That also will not help increase employment and it is also questionable whether it will quell the social tensions and protests.

In any case, in the short run, the growth prospects are improving mostly due to the recovery from the recession. The risks are on the downside if the financing of increased private and public consumption disappoints. For the period before the general elections, scheduled for March-April 2012 if the political pressures for early polls can be resisted, the main source of finance is the proceeds from the privatization of Telecom, which should take place in the spring of this year. However, that will lead to a deterioration of the trade balance and will not support the recovery of industrial production.

The main opposition party has set April 16 as the date for the start of mass protests which will end only if the government calls for early elections. This is in part because the Russian Prime Minister Putin is visiting the country at the end of March. Like the Croatian government some months ago, Serbian government is trying to deflect the calls for early elections with the reconstruction of the government. That has obviously come to late.

In the medium term, macroeconomic and social stability will present problems and will weigh on economic growth. The key issue is growth of industrial production, which has mostly stagnated in the last decade and has not recovered strongly after the crisis. Given that recovery of other sectors is either unlikely or cannot impact significantly the overall growth, medium-term prospects are rather mediocre. Those will also depend on the outcome of the upcoming general elections. At the moment, it is hard to say what the economic policy of the new government will look like.

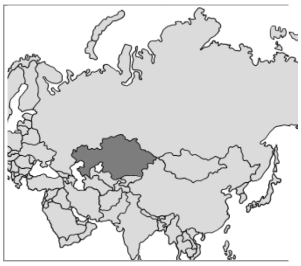
Table RS

Serbia: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 1)	2011	2012 Forecast	2013
Population, th pers., average	7440.8	7411.6	7381.6	7350.2	7320.8	7300	7280	7250	7220
Gross domestic product, RSD bn, nom. 2)	1683.5	1962.1	2302.2	2722.5	2815.0	3100	3400	3700	4000
annual change in % (real) 2)	5.6	5.2	6.9	5.5	-3.1	1.5	2.5	3	3
GDP/capita (EUR at exchange rate)	2700	3100	3900	4600	4300	4000	.	.	.
GDP/capita (EUR at PPP - wiiw)	7100	7700	8300	9200	8600	8900	.	.	.
Consumption of households, RSD mn, nom. 2)	1281.0	1492.7	1714.0	2023.6	.	.	.	.	.
annual change in % (real) 2)3)		5.4	6	6	-2	2	2	2	2
Gross fixed capital form., RSD mn, nom. 2)	319.9	412.8	552.3	632.4	.	.	.	.	.
annual change in % (real) 2)3)		15.2	12	8	-5	-4	3	4	4
Gross industrial production									
annual change in % (real)	0.8	4.7	3.7	1.1	-12.1	3.0	5	5	5
Gross agricultural production									
annual change in % (real)	-3.4	-2.6	-8.0	9.0	5.0	0	5	5	5
Construction output total 4)									
annual change in % (real)	2.0	7.7	10.8	4.6	-14.3	-10	0	5	5
Employed persons - LFS, th, Oct 5)	2733.4	2630.7	2655.7	2821.7	2616.4	2397.2	2400	2400	2420
annual change in %	-6.7	-3.8	1.0	.	-7.3	-8.4	0	0	1
Unemployed persons - LFS, th, Oct 5)	719.9	693.0	585.5	445.4	503.0	570.0	.	.	.
Unemployment rate - LFS, in %, Oct 5)	20.8	20.9	18.1	13.6	16.1	19.2	20	20	20
Reg. unemployment rate, in %, end of period	27.2	28.0	25.4	24.0	24.8	26.0	27	27	27
Average gross monthly wages, RSD 6)	25514	31745	38744	45674	44147	47450	.	.	.
annual change in % (real, net) 6)	6.4	11.4	19.5	3.9	0.2	0.7	.	.	.
Consumer prices, % p.a.	16.2	11.7	7.0	13.5	8.6	6.8	7	6	6
Producer prices in industry, % p.a. 7)	14.2	13.3	5.9	12.4	5.6	12.7	.	.	.
General governm.budget, nat.def., % GDP									
Revenues	43.0	44.2	43.5	42.0	40.7	40.0	.	.	.
Expenditures	42.0	45.8	45.5	44.6	42.9	44.8	.	.	.
Deficit (-) / surplus (+), % GDP	1.0	-1.6	-1.9	-2.6	-4.3	-4.8	-3	-3	-2
Public debt, nat.def., in % of GDP	52.1	37.3	29.8	27.9	32.6	36.0	36	36	35
Central bank policy rate, % p.a., end of period 8)	19.2	14.0	10.0	17.8	9.5	11.5	10	10	10
Current account, EUR mn	-1778.0	-2356.0	-5052.6	-7054.1	-2083.4	-1850	-2500	-3400	-3600
Current account in % of GDP	-8.8	-10.1	-17.6	-21.1	-7.0	-6.3	-8	-10	-10
Exports of goods, BOP, EUR mn	4009.0	5109.0	6382.5	7416.0	5977.7	7200	8300	9100	10000
annual growth rate in %	22.0	27.4	24.9	16.2	-19.4	20	15	10	10
Imports of goods, BOP, EUR mn	8287.0	10090.0	13451.3	15917.2	11096.2	12000	13200	14500	16000
annual growth rate in %	-2.4	21.8	33.3	18.3	-30.3	8	10	10	10
Exports of services, BOP, EUR mn	1320.0	1839.0	2304.0	2741.4	2500.1	2600	2900	3200	3500
annual growth rate in %	11.0	39.3	25.3	19.0	-8.8	4	10	10	10
Imports of services, BOP, EUR mn	1325.0	1880.0	2565.1	2926.1	2480.8	2600	2900	3200	3500
annual growth rate in %	25.5	41.9	36.4	14.1	-15.2	5	10	10	10
FDI inflow, EUR mn	1268.1	3392.4	2512.6	2017.5	1439.1	1000	1500	1500	2000
FDI outflow, EUR mn	17.9	69.8	691.8	193.1	37.6	100	200	200	200
Gross reserves of NB, excl. gold, EUR mn	4770.4	8857.9	9440.7	7938.5	10277.7	9300	10000	10000	10000
Gross external debt, EUR mn	12196.0	14182.0	17139.0	21088.0	22487.0	24000	26000	28000	30000
Gross external debt in % of GDP	61.9	57.1	59.0	68.6	76.6	81.8	84	83	83
Average exchange rate RSD/EUR	82.91	84.19	79.98	81.47	93.92	106.31	110	110	110
Purchasing power parity RSD/EUR 9)	31.72	34.41	37.58	40.40	44.47	47.77	.	.	.

1) Preliminary and wiiw estimates. - 2) According to ESA'95 (non-observed economy partially incuded). - 3) wiiw estimate. - 4) Gross value added. - 5) From 2008 extended survey as of April and October. - 6) From 2009 including wages of employees working for entrepreneurs. - 7) Domestic output prices. - 8) Two-week repo rate. - 9) Benchmark results 2005 from Eurostat and wiiw estimates.

Source: wiiw Database incorporating national statistics. Forecasts by wiiw.



Olga Pindyuk

Kazakhstan:
Fast growth is back, but sustainability problems remain

The Kazakh economy experienced a remarkable rebound in 2010: real GDP growth is estimated to exceed 7%. The driving force behind that fast growth was a revival of external demand for the country's key commodities – oil and metals (together they account for about 80% of Kazakhstan's exports). Growth of industrial production in these sectors accounted for almost two thirds of total industrial growth in 2010. wiiw forecasts that Kazakhstan's GDP growth will slow down in 2011, to 5.5%, due to the higher base for comparison in 2010; in 2012-2013 the economy will grow by 5% per annum.

The oil and metals sectors will continue to play a dominant role in the Kazakh economy during 2011-2013, as increasing global demand for these commodities will allow for fast growth of their exports. According to the recent forecast by the US Energy Information Administration, in 2011, the price of West Texas Intermediate crude oil will average about USD 93 per barrel, USD 14 more than in 2010. In 2012-2013, the oil price will remain above USD 90 per barrel, but is not likely to exceed USD 100 per barrel. China will further gain importance as an export destination for Kazakhstan – in particular, for exports of oil, non-ferrous metals, and uranium. China has been trying to ensure supplies of these commodities by signing long-term agreements on supply (recently a ten-year deal to supply uranium was signed), providing loans to the Kazakh government and investing into the country's oil extraction and energy transit infrastructure.

Private consumption also picked up in 2010, showing about 7% real growth after a 3% decline in 2009 on the back of an increase in household incomes and employment. Real wages are estimated to have increased by 7.4% in 2010, and employment by 4.4%. This also gave a boost to retail trade which expanded by about 12%, after a 2% decline in 2009. In 2011-2013, private consumption is expected to grow by 5% per annum owing to further increases in household incomes – in particular, due to wage increases in public administration, education and healthcare envisaged in the state budget. The share of household consumption in Kazakhstan's GDP remains quite low – around 40% – and will not increase significantly in the short run, when the economy will rely relatively more on net exports and investment as sources of growth.

Investment experienced a significant decline in 2010; according to our estimates, gross fixed capital formation fell by 9% last year. The sluggish construction sector, the lack of access to loans as sources of financing by many enterprises, and the postponing of investment by oil extracting companies contributed to those dynamics. During the forecasting period, however, we expect a revival of investment which will grow faster than private consumption. The major factors behind the expected investment pick-up are the following:

- Budget spending in 2011-2013 within the 'Programme of accelerated industrialization and modernization 2010-2014'. The programme envisages investment of about EUR 9 billion into infrastructure projects, in particular the building of the Western Europe-Western China corridor, upgrading railroads and agriculture infrastructure.
- Increase in investment into oil transit infrastructure. Shareholders in the Caspian Pipeline Consortium agreed to invest USD 5.4 billion to double capacity of the pipeline linking Kazakhstan with the Russian Black Sea.

The reviving economy allowed for rallying general budget revenues: in 2010, tax revenues rose by 32% year-on-year (y-o-y). Budget expenditures grew fast as well, but at a slower rate than revenues. We forecast that the government will continue to increase both current and capital expenditures. However, booming revenues would allow for fiscal consolidation, and the budget deficit will gradually decrease to 1% in 2013.

The consequences of the housing bubble and the banking crisis still remain visible in the economy and pose an impediment to growth. According to our estimates, value-added in financial services decreased by about 5% in 2010. Though there are no problems with liquidity in the banking sector now, the high share of non-performing loans (NPL), the still heavily leveraged non-oil sector and the lack of low-risk borrowers limit the possibilities of banks to issue loans and makes them invest in low-return money market instruments. In 2010, the loans stock decreased by 5.3% as compared with 2009; the decline in newly issued loans was even more profound, 7.2% y-o-y. Monthly dynamics showed some recovery at the end of 2010: in December, the decline in the loans stock slowed down to 0.6% y-o-y along with an increase in primarily short-term loans to the corporate sector. Yet growth in the banking sector is going to remain quite anaemic during the forecasting period, as resolving the problems with NPLs and deleveraging of the non-oil sector will require some time.

The construction and real estate sectors, which together accounted for 24% of Kazakhstan's GDP in 2009, also continued to suffer from the housing bubble consequences and remained stagnant in 2010. Closer to the end of 2010, a slight revival in construction and the real estate market started, partially due to state support to the construction sector; no new construction projects were started though. We expect that poor access to mortgage loans of households and ongoing deleveraging of the construction sector will make the sector's recovery slow.

High oil revenues allowed for an increase in forex reserves and national oil fund assets by about one third in 2010 as compared to 2009. The achieved financial stability and the good prospects for retaining it in the future caused the National Bank of Kazakhstan to announce the plan to switch from the exchange rate corridor to a managed float in 2011. It is expected that a small revaluation of the tenge will be allowed, in particular to deal with inflationary pressures. However, big changes in the exchange rate are not likely as the National Bank will watch attentively KZT/USD developments and will intervene if there is increasing pressure on the tenge in any direction. Therefore we envisage a slight revaluation of the tenge during the forecasting period, from an average rate of 147 KZT/USD in 2010 to 140 KZT/USD in 2013.

Inflation remains a concern for the National Bank, with food prices contributing the most to CPI growth. In 2011-2013, monetary sources of inflation will remain weak, but the expansionary fiscal policy and growing incomes of households, as well as high global food prices will continue to create an upward pressure on prices. We expect that inflation will remain in the 6-7% range during the forecasting period.

The 2011 survey 'Freedom in the World', released by Freedom House, shows that Kazakhstan, similar to Russia, remains a not free country in terms of both political rights and civil liberties, and the situation has been worsening. President Nursultan Nazarbayev and his Nur Otan party continue to maintain almost complete control over the political sphere, using tactics including arbitrary arrests, censorship of opposition media, and politically motivated prosecutions of opposition and human rights activists. Kazakhstan chaired the OSCE last year, which brought the country into the spotlight and attracted more attention of the West to the problems with human rights there. The initiative of the authorities in December 2010 to conduct a referendum which would extend the presidency of Nazarbayev by ten years until 2020 was finally cancelled by the President, who apparently decided not to further worsen the country's external image and called for early presidential elections. It is unlikely though that the opposition will have any chances of fair competition and winning the elections.

At the same time conditions for doing business in Kazakhstan have been improving as measured in the World Bank report: in 2010, the country's rank improved by 15 points to 59, with the biggest improvement recorded in the sphere of starting a business. The only deterioration concerned the possibility of obtaining credits. However, in the long run the authoritarian regime in the country, which creates vast incentives for corruption and thus poor governance, and also inhibits entrepreneurship, is likely to hurt Kazakhstan's economic competitiveness.

d in January 2010 has been still in the transitory phase, thus the effects of it on the Kazakh economy are yet to be seen. Among the issues that have not been solved so far are unharmonized standardization and certification standards, the division of customs revenues among the three states and the incorporation of energy-related sectors into the customs union framework. Besides, Kazakhstan was granted a transition period until 2015 for the harmonization of more than 400 tariff lines. The first effects can be seen only in those sectors which experienced a significant increase in import tariffs (mostly consumer goods such as furniture, footwear, pharmaceuticals etc.).

Table KZ

Kazakhstan: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 1)	2011	2012	2013
								Forecast	
Population, th pers., average	15147	15308	15484	15674	15910	16230	16500	16600	16600
Gross domestic product, KZT bn, nom.	7591	10214	12763	16053	16100	19800	23000	25600	28500
annual change in % (real)	9.7	10.7	8.7	3.3	1.2	7.1	5.5	5	5
GDP/capita (EUR at exchange rate)	3000	4200	4900	5800	4900	6200	7400	8300	9400
GDP/capita (EUR at PPP - wiiw)	7300	8000	8800	8800	8600	9200	.	.	.
Consumption of households, KZT bn, nom.	3686	4547	5468	6871	7200	8200	9200	10300	11500
annual change in % (real)	10.9	12.7	11.0	6.3	-3	7	5	5	5
Gross fixed capital form., KZT bn, nom.	2123	3084	3857	4309	4541	4800	5900	6600	7500
annual change in % (real)	28.1	29.7	17.3	1.0	1.9	-9	10	7	7
Gross industrial production									
annual change in % (real)	4.8	7.2	5.0	2.1	2.7	10	5	6	6
Gross agricultural production									
annual change in % (real)	7.3	7.0	8.4	-5.6	13.8	-11.7	12	5	5
Construction industry									
annual change in % (real)	47.4	28.6	5.7	1.8	-4.9	1	5	8	10
Employed persons - LFS, th, average	7261.0	7403.5	7631.8	7857.2	7903.4	8250	8420	8500	8590
annual change in %	1.1	2.0	3.1	3.0	0.6	4.4	2	1	1
Unemployed persons - LFS, th, average	640.7	625.4	578.8	557.8	554.5	460	.	.	.
Unemployment rate - LFS, in %, average	8.1	7.8	7.3	6.6	6.6	5.8	5.7	5.5	5.5
Reg. unemployment rate, in %, end of period	.	.	.	.	.	.			
Average gross monthly wages, KZT	34060	40790	53238	60734	67639	76000	.	.	.
annual change in % (real, gross)	11.7	10.3	17.8	-2.5	3.8	7.4	.	.	.
Consumer prices, % p.a.	7.6	8.6	10.8	17.1	7.3	7.4	7	6.5	6.5
Producer prices in industry, % p.a.	23.7	18.4	12.4	36.9	-22.2	15	12	5	6
General governm.budget, nat.def., % GDP									
Revenues and grants	28.1	27.9	22.6	25.1	21.8	21.7	.	.	.
Expenditures and net lending	22.3	20.4	24.3	27.2	24.8	24.4	.	.	.
Deficit (-) / surplus (+), % GDP	5.8	7.5	-1.7	-2.1	-3.1	-2.7	-2.5	-2.0	-1.0
Public debt, nat. def., in % of GDP	9.3	11.3	7.2	8.3	12.9	16.2	14	12	12
Central bank policy rate % p.a., end of period 2)	8.0	9.0	9.0	10.5	7.0	7.0	.	.	.
Current account, EUR mn 3)	-848	-1525	-5355	4742	-2400	3100	3900	3200	2800
Current account in % of GDP	-1.8	-2.4	-7.0	5.2	-3.1	3.1	3.2	2.3	1.8
Exports of goods, BOP, EUR mn 3)	22734	30881	35309	48905	31500	45000	51000	56200	60600
annual growth rate in %	37.1	35.8	14.3	38.5	-35.6	42.9	13	10	8
Imports of goods, BOP, EUR mn 3)	14442	19216	24288	26128	20636	23402	28400	32700	36000
annual growth rate in %	29.9	33.1	26.4	7.6	-21.0	13.4	21	15	10
Exports of services, BOP, EUR mn 3)	1790	2237	2596	2978	3100	3200	3400	3600	3900
annual growth rate in %	10.7	25.0	16.1	14.7	4.1	3.2	6	6	8
Imports of services, BOP, EUR mn 3)	6021	6947	8491	7474	7219	7808	9200	10300	11500
annual growth rate in %	46.5	15.4	22.2	-12.0	-3.4	8.2	18	12	12
FDI inflow, EUR mn 3)	1583	4958	7440	9882	9000	7200	8800	9500	10400
FDI outflow, EUR mn 3)	-117	-309	2369	2590	2200	2400	2300	2500	2700
Gross reserves of NB excl. gold, EUR mn	5965	14525	11970	13711	16184	21360	.	.	.
Gross external debt, EUR mn	36643	56252	65436	76417	77881	83428	.	.	.
Gross external debt in % of GDP	79.9	87.2	86.0	84.3	99.5	82.4	.	.	.
Average exchange rate KZT/EUR	165.42	158.27	167.75	177.04	205.67	195.67	189	186	182
Purchasing power parity KZT/EUR, wiiw 4)	68.78	83.19	93.40	116.41	118.11	132.16	.	.	.

1) Preliminary and wiiw estimates . - 2) Refinancing rate of NB. - 3) Converted from USD with the average exchange rate. - 4) wiiw estimates based on the 2005 International Comparison Project benchmark.

Source: National statistics (National Bank, Agency of Statistics etc). Forecasts by wiiw.

Peter Havlik

Russian Federation:
Oil-fuelled recovery stalls

Russian economic growth rebounded strongly in late 2009 along with the recovery of oil prices. With a time lag of about two months, the rising oil price brought about first stabilization and then an economic upswing fuelled by surging export revenues. A robust export-led recovery continued during the first half of 2010, helped by the low statistical base effect. GDP growth slowed down in the third quarter of 2010 as heat, drought and forest fires hit large parts of central Russia. Growth has accelerated in the final months of the year again. Preliminary official data published in January 2011 put the GDP growth for the whole year 2010 at 4% – identical to the wiiw forecast from June 2010. The official estimates confirm that domestic demand remained subdued as both consumer expenditure and gross fixed investments grew by just about 3%. Yet the overall gross investment jumped by more than 20% owing to the replenishment of inventories whereas, surprisingly, real net exports contracted by more than 25%. Such wide fluctuations in the two latter components of GDP (both account for about 30% of nominal GDP) are not quite unusual. In 2009, both components moved in the opposite direction as inventories were cut during the crisis and the export surplus surged by more than half. Needless to say, such large swings, related to valuation and other statistical problems, leave much room for uncertainty and future adjustments. On the supply side, the manufacturing industry largely recovered from the crisis whereas the contraction of construction continued (the latter accounts for about half of total investment outlays). Yet employment started to rise again and the unemployment rate has been gradually declining.

The latest economic data provide a mixed picture: the growth of industry, goods transport, exports has been fluctuating yet generally high; construction output is still contracting (albeit at a reduced speed); consumption expenditure is somewhat strengthening, yet still unimpressive. In both instances the statistical base effects play a role. The inflation slowdown (and the producer price deflation) which occurred during the 2009 crisis was short lived. Inflation remains stubbornly high and even accelerated in late 2010 – though annual and monthly data again present a mixed picture. There are huge producer price fluctuations, especially the prices of energy and metals shot up at the end of 2009-early 2010. In addition, the poor harvest resulted in rising food prices during the final months of 2010, especially prices of fruits and vegetables (grain exports were restricted by a government decree). Last but not least, as a by-product of surging export revenues, the rouble has appreciated again after a short-lived downward adjustment during the peak of the crisis at the turn of 2008-2009. The real appreciation – by some 15% against euro since the beginning of 2010 – has been one of the factors behind surging imports. Foreign exchange reserves are being gradually replenished; though the capital flight again accelerated towards the end of 2010. The banking sector has consolidated: both deposits and credits have been growing, bank profits have likely reached the pre-crisis level in 2010. The share of non-performing loans hovers at around 7% (though at least one third of credits is restructured); the volume of new mortgages more than doubled.

The crisis has not been used as a stimulus for an overhaul of economic policies. Restructuring, modernization and the 'innovation development' preached by the authorities already for a couple of years have so far been just slogans (see below). The anti-crisis measures announced and implemented from late 2008 resembled the standard fiscal packages adopted in the West. The aim was to improve the liquidity of the banking sector and restore the confidence, to support the exchange rate and domestic consumption. The costs of these measures added up to some 10% of GDP; judging by the sharp fall in consumption and particularly of investment during 2009, the effects of the measures adopted have been rather disappointing.

The government's long-term strategic target of economic diversification and modernization remains high on the agenda, yet it is facing numerous difficulties. President Medvedev's priority modernization areas, apart from the four "I's" (innovations, institutions, infrastructure and investments) announced already in early 2008 before the crisis hit, include energy, nuclear technologies, global information technologies, medical equipment and pharmaceuticals sectors. These modernization fields are allegedly backed by specific implementation plans which also count on the participation of foreign companies and researchers, including the highly publicized innovation centre Skolkovo near Moscow. Indeed, as one of the foreign policy breakthroughs, the EU–Russia summit in Rostov on Don in June 2010 adopted a joint statement on the Partnership for Modernization, with both parties pledging to encourage the sectoral dialogue and the implementation of specific joint projects. The trilateral meeting of President Medvedev with his French counterpart Sarkozy and German Chancellor Merkel in October 2010 confirmed the will to 'reset' EU–Russia relations as well. The invitation of Polish President W. Komorowski from February 2011 that Russia joins the "Weimar Triangle" (together with France and Germany) underlined the improved climate between Russia and Poland. Russia's accession to WTO (postponed once more in June 2009 on the pretext of forming a Customs Union with Belarus and Kazakhstan first) came back on the agenda.

The recent foreign and domestic policy advances (the latter including the sacking of Moscow's mayor Yuri Luzhkov) may have been instrumental in improving the investment climate, potentially consolidating and broadening the economic recovery. On the other hand, the outcome of Khodorkovsky's trial in December 2010, the terrorist attack at the Domodedovo airport in January 2011 and the anxiety surrounding the forthcoming Duma (December 2011) and presidential elections (March 2012) fuel uncertainty.

At the latest World Economic Forum in Davos (January 2011) President Medvedev, who attempts to strike a more liberal tone than the Prime Minister Putin, once again reiterated and summarized priority areas of his modernization agenda for Russia:

- Large scale privatization, even of some previously considered "strategic" assets such as banks (Sberbank, VTB) and energy companies (Rosneft);
- Establishment of a sovereign investment fund with the participation and risk sharing with foreign investors;

- Financial sector development, establishing Moscow as a regional financial centre;
- Accession to WTO and OECD in 2011, establishment of the common economic space with the EU;
- Establishment of Skolkovo innovation centre;
- Energy sector innovations;
- Technology transfer efforts;
- Development of broadband internet;
- Development of human resources, reversing brain drain, etc;
- Infrastructure projects, including Sochi Olympic Games 2014 and the Football World Cup 2018, using public-private partnership schemes and engaging foreign investors.

While containing hardly any news, a possibly interesting new political accent is the increased stress on integration and engagement of foreign capital and know-how in the envisaged Russian modernization.

The current wiiw forecast reckons with continued, yet unspectacular GDP growth during 2011-2013. Growth will be much lower than in the pre-crisis period and will be based on stabilized oil prices (Urals costing not more than USD 100 per barrel). This baseline scenario assumes no abrupt policy changes or external shocks. Both private consumption and investment are expected to grow a bit faster than GDP. Real exports will continue to be sluggish at best since the volumes of exported oil and gas will hardly increase in the forecasting period (and there will be not much else to export since the progress in export diversification will be limited), while imports will grow at a faster rate as household consumption and investment will pick up, fuelled by real currency appreciation. This implies hardly any contribution of real net exports to GDP growth in the coming years and, in nominal terms, a gradual reduction of the trade and current account surpluses. The current account surplus will gradually drop below 3% of GDP by 2013. The annual CPI inflation may stay in single digits and the budget deficit will soon turn into a surplus again.

The effects of the crisis on employment have so far been rather modest. They are being mitigated by demographic factors as the domestic labour supply is shrinking. Our previous assessment thus remains largely unchanged both regarding GDP growth prospects, sources of growth and labour market developments: GDP growth will stay below pre-crisis levels, labour shortages are likely to reappear soon and will definitely put a brake on economic growth already in the medium run. The chances for a successful modernization and restructuring of the economy remain slim – at least in the forecasting period up to 2013.

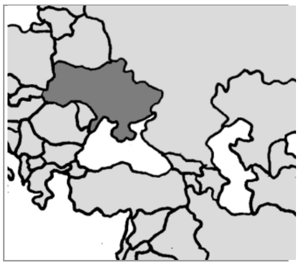
Table RU

Russia: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 1)	2011	2012 Forecast	2013
Population, th pers., average 2)	143114	142487	142115	141956	141902	141000	139500	139000	138500
Gross domestic product, RUB bn, nom. 3)	21609.8	26917.2	33247.5	41264.9	38797.2	44491.4	49500	55000	61000
annual change in % (real) 3)	6.4	8.2	8.5	5.2	-7.8	4.0	4.1	4.2	4.3
GDP/capita (EUR at exchange rate)	4300	5500	6700	8000	6200	7800	.	.	.
GDP/capita (EUR at PPP - wiiw)	10000	11200	12500	13200	12000	12700	.	.	.
Consumption of households, RUB bn, nom. 3)	10652.9	12974.7	16031.7	19968.1	20981.4	23130.2	.	.	.
annual change in % (real) 3)	12.2	12.2	14.3	10.6	-4.8	2.7	4.5	5	4.5
Gross fixed capital form., RUB bn, nom. 3)	3836.9	4980.6	6980.4	9196.8	8530.7	9348.8	.		
annual change in % (real) 3)	10.6	18.0	21.0	10.6	-14.4	3.5	6	8	7
Gross industrial production									
annual change in % (real)	5.1	6.3	6.3	2.1	-9.3	8.2	5	6	5
Gross agricultural production									
annual change in % (real)	2.3	3.6	3.4	10.8	1.4	-11.9	.	.	.
Construction industry									
annual change in % (real)	10.5	18.1	18.2	12.8	-13.2	-2.3	7	8	5
Employed persons - LFS, th, average	68169.0	68855.0	70570.5	70965.1	69284.9	69803.0	69500	69300	69000
annual change in %	1.3	1.0	2.5	0.6	-2.4	0.7	-0.4	-0.3	-0.4
Unemployed persons - LFS, th, average	5262.8	5312.0	4589.0	4791.5	6372.8	5645.0	5500	5300	5000
Unemployment rate - LFS, in %, average	7.2	7.2	6.1	6.3	8.4	7.5	7.3	7	6.8
Reg. unemployment rate, in %, end of period	2.5	2.3	2.0	2.0	2.9	2.1	.	.	.
Average gross monthly wages, RUB	8554.9	10633.9	13593.4	17290.0	18795.0	21090.0	23500	25800	28500
annual change in % (real, gross)	12.6	13.3	17.0	10.3	-2.8	4.2	4.1	4.5	5.2
Consumer prices, % p.a.	12.5	9.8	9.1	14.1	11.8	7.1	7	5	5
Producer prices in industry, % p.a. 4)	20.7	12.4	14.1	21.4	-7.2	12.2	10	8	8
General governm.budget, nat.def., % GDP									
Revenues	39.7	39.5	40.2	38.6	34.8	35.5	.	.	.
Expenditures	31.5	31.1	34.2	33.8	41.1	35.5	.	.	.
Deficit (-) / surplus (+), % GDP	8.1	8.4	6.0	4.9	-6.3	0.0	-2	0	0
Public debt, nat.def., in % of GDP 5)	15	9	7	6	8	9	10	10	10
Central bank policy rate, % p.a., end of period 6)	12.0	11.0	10.0	13.0	8.8	7.8	.	.	.
Current account, EUR mn 7)	67858	75474	56818	70732	35507	55013	50000	45000	40000
Current account in % of GDP	11.1	9.6	6.0	6.2	4.0	5.0	4.1	3.4	2.8
Exports of goods, BOP, EUR mn 7)	195545	241960	258930	321792	218221	301588	320000	343000	372000
annual growth rate in %	32.7	23.7	7.0	24.3	-32.2	38.2	6	7	8
Imports of goods, BOP, EUR mn 7)	100608	130948	163282	199148	137960	188530	210000	240000	270000
annual growth rate in %	28.4	30.2	24.7	22.0	-30.7	36.7	11	14	13
Exports of services, BOP, EUR mn 7)	20028	24791	28681	34889	29883	33417	40000	45000	50000
annual growth rate in %	20.9	23.8	15.7	21.6	-14.3	11.8	20	13	11
Imports of services, BOP, EUR mn 7)	31077	35643	42481	51495	44185	54104	60000	70000	80000
annual growth rate in %	16.1	14.7	19.2	21.2	-14.2	22.4	11	17	14
FDI inflow, EUR mn 7)	10336	23675	40237	51177	26434	35000	50000	55000	60000
FDI outflow, EUR mn 7)	10240	18454	33547	37934	32004	40000	40000	45000	40000
Gross reserves of NB, excl. gold, EUR mn	148094	224305	318840	291916	290432	335191	.	.	.
Gross external debt, EUR mn	216516	237669	316903	340688	325697	364951	.	.	.
Gross external debt in % of GDP	34.3	30.6	34.3	34.2	36.4	33.1	.	.	.
Average exchange rate RUB/EUR	35.26	34.11	35.01	36.43	44.14	40.30	41	42	42
Purchasing power parity RUB/EUR, wiiw 8)	15.06	16.93	18.73	22.03	22.81	24.90	.	.	.

1) Preliminary and wiiw estimates. - 2) Resident population. - 3) FISIM reallocated to industries, real growth rates based on previous year prices. - 4) Domestic output prices. - 5) wiiw estimate. - 6) Refinancing rate of Centralbank. - 7) Converted from USD with the average exchange rate. - 8) wiiw estimates based on the 2005 International Comparison Project benchmark.

Source: wiiw Database incorporating national statistics. Forecasts by wiiw.



Vasily Astrov

Ukraine:
Advancing state's withdrawal from the economy

The recent developments present a picture of a fairly robust growth accompanied by a further political stabilization. According to preliminary estimates, in 2010 the economy grew by 4.2%, albeit decelerating in the second half of the year due to a relatively poor grain harvest[57] and the domestic demand being increasingly covered by imports. The sources of growth have been shifting too in the course of the year; net exports, as the main growth engine at the beginning of the year, have subsequently been replaced by private consumption and the restocking of inventories. Household demand, which in 2010 soared by 5.8%, was supported by a combination of receding unemployment and an impressive growth in real wages (+7.4%) rather than by consumer credits, which actually declined. Fixed capital formation ceased to be a drag on growth in the second half of 2010, posting a 3.2% increase for the year as a whole. On the supply side, the economic growth was led by industry (+11.2% in gross output terms), particularly its export-oriented branches. Of the latter, machinery did particularly well (+36%), benefiting from the on-going recovery in Russia, with which the relations had improved markedly following the victory of Mr. Yanukovych in presidential elections in February 2010. The performance of sectors oriented towards the domestic market was generally less impressive. The dynamics of agricultural output was marginally negative, while construction posted another decline (by 5.4%), following the double-digit declines in both 2008 and 2009.

Meanwhile, the recent consolidation of political power facilitates the implementation of (partly unpopular) reforms, particularly those in the fiscal area. Some of these reforms result from conditionalities attached to the 2.5-year USD 15.2 billion IMF 'stand-by' package agreed in summer 2010 (of which USD 3.4 billion have already been transferred). However, and more generally, they reflect the 'pro-business' stance of the new authorities in economic policy terms – particularly when compared to the more 'left-leaning' and arguably populist economic policies pursued by the former Prime Minister Tymoshenko. Thus, the 2011 government budget is based on the idea to reduce both government revenues as a share of GDP *and* the fiscal deficit at the same time. On the revenue side, the budget reflects the newly adopted Tax Code which envisages some fundamental changes in taxation and tax administration. The profit tax rate will be cut as of 1 April 2011 from 25% to 23%, followed by further successive cuts to 16% by 2014. Besides, the new Code provides for a number of tax breaks such as the zero profit tax till 2016 for enterprises with an annual turnover less than UAH 3 million and no VAT rate for some agricultural and wood products. The new Code also stipulates an 'automatic' VAT refund procedure to exporters, which should help solve the long-standing problem of VAT refund arrears. The new Tax Code introduces, as of 2012, a tax on real estate (the rate of

[57] According to official estimates, the grain harvest in 2010 amounted to 39 million tons – 15% lower than the year before.

which will be set by local authorities) and a 5% tax on interest from household deposits starting from 2015. Meanwhile, the simplified taxation of small businesses has been left intact under the pressure from widespread popular protests. Besides, the overall VAT rate will be cut from 20% to 17% starting from 2014. At the same time, the excise taxes on gasoline and tobacco have been raised, and the 15% flat personal income tax has been replaced by a slightly progressive 15-17% scheme.

Despite only a marginal growth in the planned fiscal revenues (in real terms), the 2011 deficit of the general budget is to be contained at 3.5% of GDP (down from 6% in 2010), which implies an over-proportional reduction in government expenditures. The latter is to be achieved via a broad set of measures. Following the already implemented 50% hike as of 1 August 2010, the household gas tariffs are to be raised by another 30% in the course of this year, which should further reduce budget subsidies to the state-owned energy monopolist Naftohaz. Also, the deficit of the pension fund (also covered from the state budget) is to be reduced *inter alia* by gradually raising the retirement age for women from 55 to (ultimately) 60 years, although the corresponding legislation has not been passed yet. Finally, in the wake of the newly launched public administration reform, the government has been reshuffled and is undergoing a radical downsizing, by some 30% in personnel terms. The key idea behind these IMF-sponsored austerity measures is to bring the country's public debt as a share of GDP on a sustained downward path (below 30%). Ironically however, at least initially, it will almost certainly grow because of the arriving IMF tranches, which are expected to total USD 6.5 billion in 2011. In our view, given the country's reasonably strong balance-of-payments and the manageable fiscal situation, the need for IMF funds is far from obvious in the current circumstances. At the same time, the expected robust economic growth – in tandem with high inflation – would most probably enable at least a stabilization of the public debt to GDP ratio in the coming years at the current level of around 40% (which is not excessively high in any case) even without resorting to socially painful austerity measures, such as the effectively planned pension cuts.

In autumn 2010, capital flows to a number of emerging economies intensified, creating an upward pressure on their currencies. The repercussions on Ukraine, however, proved negligible so far. Quite on the contrary, in the last four months of the previous year, the country's National Bank was mostly *selling* foreign exchange in order to counteract persistent depreciation pressure on the hryvnia. This pressure stemmed partly from the re-emerging current account deficit (after the external sector had been broadly balanced in the first half of 2010), but more importantly, from the large-scale purchases of foreign cash, which totalled USD 6.1 billion between September and December 2010. The latter may be partly explained by the risen inflationary expectations, given the modest summer harvest, and the dynamics of global food prices. In September 2010, the consumer price inflation accelerated sharply, to 2.9% on the monthly basis. Although in subsequent months its pace was suppressed by the imposed export restrictions on grain and the delays in utility tariffs hikes, the inflationary pressures are likely to intensify in the coming months. Therefore, for 2011 as a whole, we expect consumer price inflation to reach around 10% on annual average. This and the currently abundant liquidity in the banking sector may prompt the National Bank to tighten somewhat its monetary policy stance. So far, the tightening of monetary policy has effectively taken place mainly through the sales of foreign exchange rather than via adjustments in the discount rate. However, the most recent developments suggest that this may change soon: in January 2011, the demand for foreign cash subsided, whereas otherwise capital inflows remained strong and the net purchases of foreign exchange by the National Bank turned again positive.

For the coming years, we expect a continuation of the current path of economic growth between 4 and 5% per year, driven largely by the growth in private consumption accompanied by a moderate widening of external deficits. Private consumption will be backed mainly by further improvements in real wages, whereas employment is unlikely to start growing before 2012, given the planned lay-offs in the public sector this year. Fixed investments should also pick up markedly, helped not least by the implemented infrastructure projects ahead of the European Football Championship in 2012. At the same time, the contribution of net exports to growth will be increasingly negative, even under an optimistic assumption that exports and imports grow at the same pace. Also, the ongoing public administration reform should suppress public consumption. The banking sector – which in 2010 recorded losses once again (albeit on a smaller scale than the year before) – is unlikely to become an important force behind the recovery of consumer demand, at least initially. Last year, the volume of consumer loans fell by 13.1% in nominal terms, and the overall credit dynamics was nearly stagnant, although trends in corporate lending have been more encouraging (+8.4%).

Politically, it appears that the country has entered a prolonged period of stability. Virtually all power is concentrated in the hands of Mr. Yanukovych and his Party of Regions, which – following the recent reversal of the constitutional reforms enacted at the onset of the 'orange revolution' – is now also less dependent on support from its initial coalition partners: the Communists and the centrist Lytvyn Block. This political consolidation has been accompanied by a strengthening of authoritarian trends, manifested inter alia in the reported reduction of media freedoms. In turn, the 'orange' opposition, (still) largely centred around Ms. Tymoshenko, remains generally divided and weak, and has increasingly become a target of criminal prosecutions (some of them probably politically motivated). These developments resemble to a certain extent those observed in Russia in the first few years of the past decade, when the persistent infighting and political paralysis throughout most of the 1990s was succeeded by a more authoritarian system, which tamed the oligarchs and ensured a higher degree of stability. Although Ukraine's pronounced cultural and linguistic East-West divide makes a repetition of the 'Russian scenario' more difficult, Mr. Yanukovych's regime could potentially benefit from sustained economic improvements. The deep disappointment of Ukrainian voters with the absence of any real prospects of EU integration has been another important factor behind Mr. Yanukovych's electoral success and may well continue to remain so for some time. The free trade negotiations with the EU are reportedly advancing very slowly, while the goal of a visa-free regime for Ukrainians entering the EU appears even more remote. Still, on 1 February 2011 Ukraine joined the EU Energy Community, which potentially means that it will have to gradually liberalize its gas and electricity sectors and adjust its energy legislation in line with the EU norms.

Table UA

Ukraine: Selected Economic Indicators

	2005	2006	2007	2008	2009	2010 1)	2011	2012	2013
								Forecast	
Population, th pers., average	47105	46788	46509	46258	46053	45871	45750	45600	45500
Gross domestic product, UAH mn, nom.	441452	544153	720731	948056	913345	1085935	1248300	1415600	1590400
annual change in % (real)	2.7	7.3	7.9	2.3	-14.8	4.2	4.5	5	5
GDP/capita (EUR at exchange rate)	1500	1800	2200	2700	1800	2200	.	.	.
GDP/capita (EUR at PPP - wiiw)	4700	5200	5800	6000	5100	5400	.	.	.
Consumption of households, UAH mn, nom.	252624	319383	423174	582482	581733	675023	.	.	.
annual change in % (real)	16.6	15.9	17.2	13.1	-14.9	5.8	5	5.5	6
Gross fixed capital form., UAH mn, nom.	96965	133874	198348	250158	167644	196286	.	.	.
annual change in % (real)	3.9	21.2	23.9	-1.2	-50.5	3.2	12	10	8
Gross industrial production									
annual change in % (real)	3.1	6.2	7.6	-5.2	-21.9	11.2	7	6.5	6
Gross agricultural production									
annual change in % (real)	0.1	2.5	-6.5	17.1	-1.8	-1.0	.	.	.
Construction industry									
annual change in % (real)	-6.6	9.9	15.6	-15.8	-48.2	-5.4	.	.	.
Employed persons - LFS, th, average	20680.0	20730.4	20904.7	20972.3	20191.5	20200	20200	20250	20290
annual change in %	1.9	0.2	0.8	0.3	-3.7	0	0	0.2	0.2
Unemployed persons - LFS, th, average	1600.8	1515.0	1417.6	1425.1	1958.8	1900	.	.	.
Unemployment rate - LFS, in %, average	7.2	6.8	6.4	6.4	8.8	8.6	8.6	8.4	8.2
Reg. unemployment rate, in %, end of period	3.1	2.7	2.3	3.0	1.9	2.0	.	.	.
Average gross monthly wages, UAH 2)	806.2	1041.4	1351.0	1806.0	1906.0	2239.0	.	.	.
annual change in % (real, gross)	20.4	18.4	15.0	6.8	-8.9	7.4	.	.	.
Consumer prices, % p.a.	13.5	9.1	12.8	25.2	15.9	9.4	10	8	7
Producer prices in industry, % p.a. 3)	16.7	9.6	19.5	35.5	6.5	20.9	.	.	.
General governm.budget, nat.def., % GDP									
Revenues	30.4	31.6	30.5	31.4	29.9	29	.	.	.
Expenditures	32.2	32.3	31.6	32.8	34.0	35	.	.	.
Deficit (-) / surplus (+) 4)	-1.8	-0.7	-1.1	-1.5	-4.1	-6	-4	-3	-3
Public debt, nat.def., in % of GDP	17.7	14.8	12.3	20.0	34.8	39.8	43	43	41
Central bank policy rate, % p.a., end of period 5)	9.5	8.5	8.0	12.0	10.3	7.8	.	.	.
Current account, EUR mn 6)	2030	-1289	-3849	-8721	-1242	-1927	-3000	-4000	-5000
Current account in % of GDP	2.9	-1.5	-3.7	-7.1	-1.5	-1.9	-2.5	-2.9	-3.2
Exports of goods, BOP, EUR mn 6)	28093	31048	36383	46274	28958	39268	43200	46700	50400
annual growth rate in %	4.4	10.5	17.2	27.2	-37.4	35.6	10	8	8
Imports of goods, BOP, EUR mn 6)	29004	35188	44100	57270	32046	45594	51100	56200	61800
annual growth rate in %	21.4	21.3	25.3	29.9	-44.0	42.3	12	10	10
Exports of services, BOP, EUR mn 6)	7503	9000	10337	12228	9936	12704	14600	16400	18000
annual growth rate in %	18.6	19.9	14.9	18.3	-18.8	27.9	15	12	10
Imports of services, BOP, EUR mn 6)	6054	7305	8571	11039	8248	9156	10100	11300	12900
annual growth rate in %	13.6	20.7	17.3	28.8	-25.3	11.0	10	12	14
FDI inflow, EUR mn 6)	6263	4467	7220	7457	3453	4500	5000	6000	7000
FDI outflow, EUR mn 6)	221	-106	491	690	116	200	.	.	.
Gross reserves of NB excl. gold, EUR mn	16058	16587	21634	21847	17824	25096	.	.	.
Gross external debt, EUR mn	33504	41391	54421	72109	72062	83000	.	.	.
Gross external debt in % of GDP	45.3	50.6	56.0	82.6	90.3	81	.	.	.
Average exchange rate UAH/EUR	6.389	6.335	6.918	7.708	10.868	10.533	10.5	10	10
Purchasing power parity UAH/EUR, wiiw 7)	1.986	2.227	2.656	3.405	3.909	4.373	.	.	.

1) Preliminary and wiiw estimates. - 2) Excluding small enterprises. - 3) Domestic output prices. - 4) In 2009 budget deficit reached 9.2% of GDP taking into account transfers to Naftohaz and accumulated VAT arrears. - 5) Discount rate of NB. - 6) Converted from USD with the average exchange rate. - 7) wiiw estimates based on the 2005 International Comparison Project benchmark.

Source: wiiw Database incorporating national statistics. Forecasts by wiiw.

Appendix

Selected indicators of competitiveness

Table A/1

GDP per capita at current PPPs (EUR), from 2011 at constant PPPs and population

	1991	2000	2005	2008	2009	2010	2012	2015	2020	2025	2030
									projection 1)		
Bulgaria	4400	5400	8200	10900	10400	10600	11200	12500	15200	18500	22500
Cyprus	10700	16900	20400	24400	23200	23600	24500	27600	33500	40700	49500
Czech Republic	8800	13000	17100	20200	19300	19900	20800	23400	28500	34600	42100
Estonia	5500	8600	13900	17000	15000	15600	17000	19200	23400	28500	34600
Hungary	6800	10600	14200	16200	15300	15600	16500	18400	22400	27200	33100
Latvia	6500	7000	10900	14100	12200	12400	13200	14800	18000	21800	26500
Lithuania	7100	7500	11900	15300	12900	13400	14300	16000	19400	23600	28700
Malta	9500	15900	17600	19500	19000	20000	20800	23400	28500	34600	42100
Poland	4500	9100	11500	14100	14300	14900	16200	18300	22300	27100	33000
Romania	4000	5000	7900	11700	10900	10900	11500	12800	15600	18900	23100
Slovakia	5800	9600	13500	18100	17200	18100	19600	22300	27100	33000	40100
Slovenia	8500	15200	19700	22800	20800	21200	22100	24600	30000	36400	44300
NMS-12	5400	8600	11700	14700	14200	14600	15500	17400	21200	25800	31400
Croatia	7000	9400	12700	15800	15000	14900	15300	17100	20800	25300	30800
Macedonia	4300	5100	6600	8500	8500	8400	8900	10000	12100	14700	17900
Montenegro	.	5600	6900	10800	9700	9700	10200	11300	13800	16800	20500
Turkey	3800	8000	9500	11700	10700	11500	12500	14000	17100	20800	25300
Albania	1400	3500	5000	6400	6500	6800	7300	8300	10100	12300	15000
Bosnia & Herzeg.	.	3900	5200	6600	6300	6400	6700	7500	9000	11000	13400
Serbia	.	5000	7100	9200	8600	8900	9400	10500	12800	15600	18900
Kazakhstan	.	4200	7300	8800	8600	9200	10200	11500	14000	17100	20800
Russia	7600	6600	10000	13200	12000	12700	13800	15600	18900	23100	28100
Ukraine	4600	2800	4700	6000	5100	5400	5900	6700	8200	10000	12100
Austria	18700	25000	28000	31100	29300	30400	31500	33400	36900	40800	45000
Germany	18100	22600	26300	29000	27400	29000	30200	32000	35400	39100	43100
Greece	12300	16000	20600	23300	21900	21300	20900	22100	24500	27000	29900
Portugal	10600	15400	17800	19500	18800	19400	19400	20600	22600	25100	27600
Spain	12800	18500	22900	25900	24300	24700	25300	26800	29600	32600	36100
USA	21300	30700	35700	36500	34500	36100	37800	40200	44400	49000	54100
EU-27 average	13700	19100	22500	25000	23600	24400	25300	27100	30100	33600	37500

European Union (27) average = 100

	1991	2000	2005	2008	2009	2010	2012	2015	2020	2025	2030
Bulgaria	32	28	36	44	44	43	44	46	50	55	60
Cyprus	78	88	91	98	98	97	97	102	111	121	132
Czech Republic	64	68	76	81	82	82	82	86	95	103	112
Estonia	40	45	62	68	64	64	67	71	78	85	92
Hungary	50	55	63	65	65	64	65	68	74	81	88
Latvia	47	37	48	56	52	51	52	55	60	65	71
Lithuania	52	39	53	61	55	55	57	59	64	70	77
Malta	69	83	78	78	81	82	82	86	95	103	112
Poland	33	48	51	56	61	61	64	68	74	81	88
Romania	29	26	35	47	46	45	45	47	52	56	62
Slovakia	42	50	60	72	73	74	77	82	90	98	107
Slovenia	62	80	88	91	88	87	87	91	100	108	118
NMS-12	39	45	52	59	60	60	61	64	70	77	84
Croatia	51	49	56	63	64	61	60	63	69	75	82
Macedonia	31	27	29	34	36	34	35	37	40	44	48
Montenegro	.	29	31	43	41	40	40	42	46	50	55
Turkey	28	42	42	47	45	47	49	52	57	62	67
Albania	10	18	22	26	28	28	29	31	34	37	40
Bosnia & Herzeg.	.	20	23	26	27	26	26	28	30	33	36
Serbia	.	26	32	37	36	36	37	39	43	46	50
Kazakhstan	.	22	32	35	36	38	40	42	47	51	55
Russia	55	35	44	53	51	52	55	58	63	69	75
Ukraine	34	15	21	24	22	22	23	25	27	30	32
Austria	136	131	124	124	124	125	125	123	123	121	120
Germany	132	118	117	116	116	119	119	118	118	116	115
Greece	90	84	92	93	93	87	83	82	81	80	80
Portugal	77	81	79	78	80	80	77	76	75	75	74
Spain	93	97	102	104	103	101	100	99	98	97	96
USA	155	161	159	146	146	148	149	148	148	146	144
EU-27 average	100	100	100	100	100	100	100	100	100	100	100

1) Projection assuming a 2 percentage point growth differential with respect to the EU-15 from 2014.

Sources: National statistics, Eurostat, wiiw estimates.

Table A/2

Indicators of macro-competitiveness, 2000-2013

EUR based, annual averages

	2000	2005	2008	2009	2010	2011	2012	2013
							Forecast	
Bulgaria								
Producer price index, 2005=100	78.6	100.0	133.8	125.1	135.9	141.0	146.8	152.9
Consumer price index, 2005=100	76.4	100.0	129.4	132.6	136.6	142.0	147.7	153.6
GDP deflator, 2005=100	78.7	100.0	126.6	131.7	137.7	142.9	148.7	155.0
Exchange rate (ER), NC/EUR	1.9522	1.9558	1.9558	1.9558	1.9558	1.9558	1.9558	1.9558
ER, nominal, 2005=100	99.8	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Real ER (CPI-based), 2005=100	84.9	100.0	119.3	121.1	122.2	124.4	127.1	129.6
Real ER (PPI-based), 2005=100	84.6	100.0	117.7	114.3	120.0	122.5	125.6	128.3
PPP, NC/EUR	0.6195	0.7154	0.8357	0.8682	0.8987	0.92	0.94	0.96
Price level, EU27 = 100	32	37	43	44	46	47	48	49
Average monthly gross wages, NC	225	324	525	592	642	690	740	790
Average monthly gross wages, EUR (ER)	115	166	268	303	328	350	380	400
Average monthly gross wages, EUR (PPP)	362	452	628	682	714	750	790	820
GDP nominal, NC mn	27399	45484	69295	68537	71900	76500	82000	88000
Employed persons - LFS, th.,average	2794.7	2981.9	3360.7	3253.6	3065.0	3100	3150	3200
GDP per employed person, NC	9804	15253	20619	21065	23458	24700	26000	27500
GDP per empl. person, NC at 2000 pr.	9804	12001	12815	12584	13405	13600	13800	14000
Unit labour costs, NC, 2005=100	84.9	100.0	151.7	174.4	177.6	188.1	198.8	209.2
Unit labour costs, ER adj., 2005=100	85.1	100.0	151.7	174.4	177.6	188.1	198.8	209.2
Unit labour costs, PPP adj., Austria=100	16.5	18.4	25.8	28.0	28.7	30.3	31.8	33.0
Czech Republic								
Producer price index, 2005=100	98.3	100.0	103.2	101.6	101.6	102.4	104.3	106.5
Consumer price index, 2005=100	90.6	100.0	111.7	112.4	113.7	116.0	118.3	120.7
GDP deflator, 2005=100	88.2	100.0	106.5	109.2	108.6	109.4	111.5	113.7
Exchange rate (ER), NC/EUR	35.60	29.78	24.95	26.44	25.28	24.5	24	24
ER nominal, 2005=100	119.5	100.0	83.8	88.8	84.9	82.3	80.6	80.6
Real ER (CPI-based), 2005=100	84.1	100.0	123.0	115.6	119.8	123.5	126.3	126.3
Real ER (PPI-based), 2005=100	88.4	100.0	108.4	104.6	105.7	108.1	110.8	110.8
PPP, NC/EUR	16.34	17.10	17.54	17.94	17.67	17.5	17.6	17.6
Price level, EU27 = 100	46	57	70	68	70	71	73	73
Average monthly gross wages, NC	13219	18344	22593	23488	24000	24700	25800	27100
Average monthly gross wages, EUR (ER)	371	616	906	889	949	1010	1080	1130
Average monthly gross wages, EUR (PPP)	809	1073	1288	1309	1359	1410	1470	1540
GDP nominal, NC bn	2189	2984	3689	3626	3690	3800	3970	4200
Employed persons - LFS, th., average	4732	4764	5003	4934	4885	4890	4910	4930
GDP per employed person, NC	462670	626335	737431	734829	755374	777100	808600	851900
GDP per empl. person, NC at 2000 pr.	462670	552324	610456	593561	613626	626500	639600	660500
Unit labour costs, NC, 2005=100	86.0	100.0	111.4	119.1	117.8	118.7	121.5	123.5
Unit labour costs, ER adj., 2005=100	72.0	100.0	133.0	134.2	138.7	144.3	150.7	153.3
Unit labour costs, PPP adj., Austria=100	29.9	39.2	48.3	46.0	47.8	49.6	51.4	51.6
Estonia								
Producer price index, 2005=100	90.6	100.0	121.7	122.6	126.6	131.8	136.3	142.5
Consumer price index, 2005=100	84.0	100.0	123.3	123.6	127.0	132.0	136.6	142.8
GDP deflator, 2005=100	80.7	100.0	128.4	128.3	132.0	137.5	142.1	148.7
Exchange rate (ER), NC/EUR	1.000	1.000	1.000	1.000	1.000	1.0	1.0	1.0
ER, nominal, 2005=100	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Real ER (CPI-based), 2005=100	93.2	100.0	113.7	112.8	113.5	115.7	117.6	120.5
Real ER (PPI-based), 2005=100	97.4	100.0	107.1	112.0	111.8	114.5	116.6	119.6
PPP, NC/EUR	0.5234	0.5995	0.7061	0.6903	0.7031	0.72	0.73	0.75
Price level, EU27 = 100	52	60	71	69	70	72	73	75
Average monthly gross wages, NC	314	516	825	784	790	830	870	920
Average monthly gross wages, EUR (ER)	314	516	825	784	790	830	870	920
Average monthly gross wages, EUR (PPP)	599	861	1169	1136	1124	1150	1190	1220
GDP nominal, NC mn	6160	11182	16107	13861	14700	16000	17200	18800
Employed persons - LFS, th., average	572.5	607.4	656.5	595.8	570.9	595	610	620
GDP per employed person, NC	10760	18409	24534	23264	25750	26900	28200	30300
GDP per empl. person, NC at 2000 pr.	10760	14858	15421	14632	15741	15800	16000	16400
Unit labour costs, NC, 2005=100	83.9	100.0	154.1	154.3	144.5	151.3	156.6	161.5
Unit labour costs, ER adj., 2005=100	83.9	100.0	154.1	154.3	144.5	151.3	156.6	161.5
Unit labour costs, PPP adj., Austria=100	34.7	39.1	55.8	52.7	49.6	51.8	53.2	54.3

(Table A/2 ctd.)

(Table A/2 ctd.)

	2000	2005	2008	2009	2010	2011	2012	2013
							Forecast	
Hungary								
Producer price index, 2005=100	86.9	100.0	111.9	116.9	124.3	127.9	131.9	136.0
Consumer price index, 2005=100	75.3	100.0	119.1	123.9	129.7	134.8	139.5	144.4
GDP deflator, 2005=100	73.7	100.0	115.6	120.7	125.4	129.0	133.1	137.2
Exchange rate (ER), NC/EUR	260.04	248.05	251.51	280.33	275.48	280	275	275
ER, nominal 2005=100	104.8	100.0	101.4	113.0	111.1	112.9	110.9	110.9
Real ER (CPI-based), 2005=100	79.7	100.0	108.3	100.1	104.5	104.6	108.3	109.9
Real ER (PPI-based), 2005=100	89.1	100.0	97.1	94.5	98.9	98.4	101.8	102.9
PPP, NC/EUR	124.06	153.56	165.00	170.11	175.13	177.1	179.9	181.9
Price level, EU27 = 100	48	62	66	61	64	63	65	66
Average monthly gross wages, NC	87750	158343	198741	199837	204000	213000	223800	237400
Average monthly gross wages, EUR (ER)	337	638	790	713	741	760	810	860
Average monthly gross wages, EUR (PPP)	707	1031	1204	1175	1165	1200	1240	1310
GDP nominal, NC bn	13369	21971	26754	26054	27400	28900	30700	32600
Employed persons - LFS, th., average	3856	3902	3879	3782	3780	3820	3860	3900
GDP per employed person, NC	3466859	5631367	6896403	6889398	7248677	7565400	7953400	8359000
GDP per empl. person, NC at 2000 pr.	3466859	4152926	4398216	4208551	4262925	4323700	4407300	4493000
Unit labour costs, NC, 2005=100	66.4	100.0	118.5	124.5	125.5	129.2	133.2	138.6
Unit labour costs, ER adj., 2005=100	63.3	100.0	116.9	110.2	113.0	114.5	120.1	125.0
Unit labour costs, PPP adj., Austria=100	27.5	41.0	44.4	39.5	40.7	41.1	42.9	44.1
Latvia								
Producer price index, 2005=100	81.6	100.0	142.7	136.2	140.0	144.1	148.4	153.7
Consumer price index, 2005=100	81.9	100.0	135.2	139.6	137.9	142.0	146.3	151.4
GDP deflator, 2005=100	77.8	100.0	151.2	149.0	147.5	151.8	156.3	161.9
Exchange rate (ER), NC/EUR	0.5592	0.6962	0.7027	0.7057	0.7087	0.7087	0.7087	0.7087
ER, nominal, 2005=100	80.3	100.0	100.9	101.4	101.8	101.8	101.8	101.8
Real ER (CPI-based), 2005=100	113.1	100.0	123.6	125.8	121.2	122.2	123.7	125.5
Real ER (PPI-based), 2005=100	109.2	100.0	124.4	122.7	121.5	122.9	124.7	126.7
PPP, NC/EUR	0.2864	0.3606	0.5057	0.4762	0.4668	0.47	0.48	0.49
Price level, EU27 = 100	51	52	72	67	66	67	68	69
Average monthly gross wages, NC	150	246	479	461	443	460	480	510
Average monthly gross wages, EUR (ER)	267	353	682	653	625	650	680	720
Average monthly gross wages, EUR (PPP)	522	681	947	968	949	970	1000	1050
GDP nominal, NC mn	4750.8	9059.1	16188.2	13082.8	12900	13700	14600	15700
Employed persons - LFS, th., average	941.1	1033.7	1124.5	983.1	945	970	1020	1050
GDP per employed person, NC	5048	8764	14396	13308	13651	14100	14300	15000
GDP per empl. person, NC at 2000 pr.	5048	6815	7401	6946	7195	7200	7100	7200
Unit labour costs, NC, 2005=100	82.1	100.0	179.5	184.1	170.7	177.2	187.5	196.4
Unit labour costs, ER adj., 2005=100	102.3	100.0	177.8	181.6	167.7	174.0	184.2	193.0
Unit labour costs, PPP adj., Austria=100	34.5	31.9	52.6	50.6	47.0	48.7	51.1	52.9
Lithuania								
Producer price index, 2005=100	90.1	100.0	135.7	117.3	129.5	133.3	136.7	140.2
Consumer price index, 2005=100	95.5	100.0	122.0	127.1	128.6	132.5	135.8	139.2
GDP deflator, 2005=100	92.3	100.0	126.9	122.2	125.8	129.5	132.8	136.2
Exchange rate (ER), NC/EUR	3.695	3.453	3.453	3.453	3.453	3.45	3.45	3.45
ER, nominal, 2005=100	107.0	100.0	100.0	100.0	100.0	99.9	99.9	99.9
Real ER (CPI-based), 2005=100	99.0	100.0	112.5	116.1	115.0	116.1	116.9	117.5
Real ER (PPI-based), 2005=100	90.5	100.0	119.4	107.2	114.4	115.9	117.1	117.7
PPP, NC/EUR	1.745	1.775	2.171	2.132	2.173	2.20	2.22	2.23
Price level, EU27 = 100	47	51	63	62	63	64	64	65
Average monthly gross wages, NC	971	1276	2152	2056	2070	2160	2270	2400
Average monthly gross wages, EUR (ER)	263	370	623	595	600	630	660	700
Average monthly gross wages, EUR (PPP)	556	719	991	965	953	980	1020	1070
GDP nominal, NC mn	45737	72060	111483	91526	95500	101200	107500	114400
Employed persons - LFS, th., average	1398	1474	1520	1416	1345	1380	1420	1450
GDP per employed person, NC	32721	48891	73344	64642	71004	73300	75700	78900
GDP per empl. person, NC at 2000 pr.	32721	45144	53380	48860	52120	52200	52600	53500
Unit labour costs, NC, 2005=100	105.0	100.0	142.6	148.9	140.5	146.4	152.7	158.7
Unit labour costs, ER adj., 2005=100	98.1	100.0	142.6	148.9	140.5	146.5	152.8	158.8
Unit labour costs, PPP adj., Austria=100	31.9	30.7	40.6	40.0	37.9	39.4	40.8	41.9

(Table A/2 ctd.)

(Table A/2 ctd.)

	2000	2005	2008	2009	2010	2011	2012 Forecast	2013
Poland								
Producer price index, 2005=100	88.8	100.0	106.4	110.5	113.1	115.9	118.8	121.2
Consumer price index, 2005=100	87.4	100.0	108.3	112.6	115.6	119.6	122.6	125.7
GDP deflator, 2005=100	88.1	100.0	108.7	112.7	115.7	120.0	122.7	125.5
Exchange rate (ER), NC/EUR	4.008	4.023	3.512	4.328	3.995	3.9	3.9	4.0
ER, nominal, 2005=100	99.6	100.0	87.3	107.6	99.3	96.9	96.9	99.4
Real ER (CPI-based), 2005=100	97.3	100.0	114.4	95.6	104.1	108.1	108.9	106.7
Real ER (PPI-based), 2005=100	95.7	100.0	107.2	93.9	100.6	103.8	104.9	102.2
PPP, PLZ/EUR	2.117	2.232	2.374	2.469	2.510	2.56	2.58	2.58
Price level, EU27 = 100	53	55	68	57	63	66	66	65
Average monthly gross wages, NC	1894	2361	2942	3103	3222	3460	3710	3960
Average monthly gross wages, EUR (ER)	472	587	838	717	807	890	950	990
Average monthly gross wages, EUR (PPP)	894	1058	1239	1257	1284	1350	1440	1530
GDP nominal, NC bn	744	983	1275	1344	1430	1540	1640	1750
Employed persons - LFS, th., average	14526	14116	15800	15868	15900	15950	16270	16680
GDP per employed person, NC	51245	69661	80725	84677	89937	96600	100800	104900
GDP per empl. person, NC at 2000 pr.	51245	61375	65417	66206	68497	70900	72400	73600
Unit labour costs, NC, 2005=100	96.1	100.0	116.9	121.9	122.3	126.9	133.2	139.9
Unit labour costs, ER adj., 2005=100	96.4	100.0	133.9	113.3	123.2	130.9	137.4	140.7
Unit labour costs, PPP adj., Austria=100	44.4	43.5	54.0	43.1	47.1	49.9	52.0	52.6
Romania								
Producer price index, 2005=100	39.3	100.0	135.7	138.2	147.0	154.0	163.1	171.7
Consumer price index, 2005=100	43.2	100.0	120.7	127.4	135.2	142.6	148.3	154.2
GDP deflator, 2005=100	37.0	100.0	144.7	150.7	160.0	167.6	177.5	186.9
Exchange rate (ER), NC/EUR	1.992	3.621	3.683	4.240	4.212	4.3	4.4	4.4
ER, nominal, 2005=100	55.0	100.0	101.7	117.1	116.3	118.8	121.5	121.5
Real ER (CPI-based), 2005=100	87.0	100.0	109.5	99.4	103.9	105.2	105.0	107.1
Real ER (PPI-based), 2005=100	76.8	100.0	117.4	107.8	111.6	112.7	114.9	118.6
PPP, NC/EUR	0.727	1.699	2.048	2.135	2.244	2.31	2.41	2.49
Price level, EU27 = 100	37	47	56	50	53	54	55	57
Average monthly grross wages, NC	284	968	1761	1845	1940	2090	2260	2410
Average monthly gross wages, EUR (ER)	143	267	478	435	461	490	510	550
Average monthly gross wages, EUR (PPP)	390	570	860	864	865	900	940	970
GDP nominal, NC mn	80985	288955	514700	498008	522500	558500	615100	667100
Employed persons - LFS, th., average	10508	9115	9369	9244	9200	9150	9200	9200
GDP per employed person, NC	7707	31702	54936	53877	56793	61000	66900	72500
GDP per empl. person, NC at 2000 pr.	7707	11733	14054	13234	13141	13500	13900	14400
Unit labour costs, NC, 2005=100	44.7	100.0	151.9	169.0	178.9	187.6	197.1	202.9
Unit labour costs, ER adj., 2005=100	81.2	100.0	149.3	144.3	153.8	158.0	162.2	166.9
Unit labour costs, PPP adj., Austria=100	30.6	35.6	49.3	44.9	48.2	49.4	50.3	51.1
Slovakia								
Producer price index, 2005=100	81.2	100.0	104.1	97.2	97.3	98.3	100.2	102.2
Consumer price index, 2005=100	75.3	100.0	110.4	111.4	112.2	114.5	117.9	121.4
GDP deflator, 2005=100	80.3	100.0	107.1	105.9	106.8	107.8	108.9	111.1
Exchange rate (ER), NC/EUR	1.4141	1.2813	1.0377	1.0	1.0	1.0	1.0	1.0
ER, nominal, 2005=100	110.4	100.0	81.0	78.0	78.0	78.0	78.0	78.0
Real ER (CPI-based), 2005=100	75.7	100.0	125.7	130.4	128.6	128.5	130.0	131.3
Real ER (PPI-based), 2005=100	79.1	100.0	113.1	113.7	110.1	109.4	109.9	109.9
PPP NC/ EUR	0.6045	0.6759	0.6835	0.6753	0.6746	0.67	0.67	0.67
Price level, EU27 = 100	43	53	66	68	67	67	67	67
Average monthly gross wages, NC	379	573	723	745	765	800	850	920
Average monthly gross wages, EUR (ER)	268	448	697	745	765	800	850	920
Average monthly gross wages, EUR (PPP)	628	848	1058	1103	1134	1200	1280	1380
GDP nominal, NC mn	31177	49314	67007	63051	66200	69500	73000	78200
Employed persons - LFS, th., average	2102	2215	2434	2366	2300	2320	2340	2360
GDP per employed person, NC	14834	22262	27533	26645	28783	30000	31200	33100
GDP per empl. person, NC at 2000 pr.	14834	17881	20655	20216	21644	22300	23000	23900
Unit labour costs, NC, 2005=100	79.8	100.0	109.2	114.8	110.2	111.9	115.2	120.0
Unit labour costs, ER adj., 2005=100	72.3	100.0	134.8	147.1	141.2	143.3	147.7	153.8
Unit labour costs, PPP adj., Austria=100	24.9	32.5	40.6	41.8	40.4	40.9	41.8	43.0

(Table A/2 ctd.)

(Table A/2 ctd.)

	2000	2005	2008	2009	2010	2011	2012	2013
							Forecast	
Slovenia								
Producer price index, 2005=100	85.1	100.0	110.9	109.4	111.5	114.3	117.2	119.5
Consumer price index, 2005=100	76.4	100.0	112.3	113.3	115.6	118.9	121.8	124.9
GDP deflator, 2005=100	77.0	100.0	110.6	114.2	116.6	119.8	122.8	125.9
Exchange rate (ER), NC/EUR	0.8622	0.9997	1.0	1.0	1.0	1.0	1.0	1.0
ER, nominal, 2005=100	86.2	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Real ER (CPI-based), 2005=100	98.2	100.0	103.5	103.4	103.4	104.1	104.8	105.3
Real ER (PPI-based), 2005=100	106.1	100.0	97.6	99.9	98.5	99.3	100.3	100.3
PPP, NC/EUR	0.6114	0.7304	0.8086	0.8353	0.8443	0.85	0.86	0.87
Price level, EU27 = 100	71	73	81	84	84	85	86	87
Average monthly gross wages, NC	800	1157	1391	1439	1500	1560	1620	1690
Average monthly gross wages, EUR (ER)	928	1157	1391	1439	1500	1560	1620	1690
Average monthly gross wages, EUR (PPP)	1308	1584	1721	1723	1777	1830	1880	1950
GDP nominal, NC mn	18481	28750	37305	35384	36560	38340	40280	42530
Employed persons - LFS, th., average	901	949	996	981	966	966	976	985
GDP per employed person, NC	20511	30288	37451	36081	37847	39700	41300	43200
GDP per empl. person, NC at 2000 pr.	20511	23335	26080	24346	25014	25500	25900	26400
Unit labour costs, NC, 2005=100	78.6	100.0	107.6	119.2	120.9	123.4	126.1	129.1
Unit labour costs, ER adj., 2005=100	91.2	100.0	107.6	119.2	120.9	123.3	126.1	129.1
Unit labour costs, PPP adj., Austria=100	63.0	65.2	65.0	67.9	69.3	70.5	71.5	72.3
Croatia								
Producer price index, 2005=100	90.9	100.0	115.1	114.6	119.5	124.3	128.7	140.4
Consumer price index, 2005=100	87.3	100.0	112.7	115.4	116.6	119.6	121.9	125.0
GDP deflator, 2005=100	83.4	100.0	114.4	118.2	119.6	122.6	125.1	128.2
Exchange rate (ER), NC/EUR	7.634	7.400	7.223	7.340	7.286	7.3	7.3	7.3
ER, nominal, 2005=100	103.2	100.0	97.6	99.2	98.5	98.6	98.6	98.6
Real ER (CPI-based), 2005=100	93.9	100.0	106.5	106.2	106.0	106.2	106.4	106.9
Real ER (PPI-based), 2005=100	94.7	100.0	103.7	105.6	107.2	109.5	111.6	119.4
PPP, NC/EUR	4.237	4.676	4.897	5.011	5.021	5.06	5.08	5.11
Price level, EU27 = 100	56	63	68	68	69	69	70	70
Average monthly gross wages, NC	4869	6248	7544	7711	7650	7880	8200	8660
Average monthly gross wages, EUR (ER)	638	844	1044	1051	1050	1080	1120	1190
Average monthly gross wages, EUR (PPP)	1149	1336	1541	1539	1524	1560	1610	1700
GDP nominal, NC mn	176690	264368	342159	333063	332000	343700	357600	377500
Employed persons - LFS, th., average	1553	1573	1636	1605	1540	1525	1530	1550
GDP per employed person, NC	113773	168066	209207	207477	215584	225400	233700	243500
GDP per empl. person, NC at 2000 pr.	113773	140102	152413	146275	150202	153200	155700	158300
Unit labour costs, NC, 2005=100	96.0	100.0	111.0	118.2	114.2	115.3	118.1	122.7
Unit labour costs, ER adj., 2005=100	93.0	100.0	113.7	119.2	116.0	116.9	119.7	124.4
Unit labour costs, PPP adj., Austria=100	54.1	54.9	57.9	57.2	56.0	56.3	57.2	58.7
Macedonia								
Producer price index, 2005=100	95.3	100.0	121.3	113.4	123.1	126.9	130.6	134.5
Consumer price index, 2005=100	91.9	100.0	114.3	113.4	115.4	118.8	122.4	126.1
GDP deflator, 2005=100	89.0	100.0	119.3	120.7	124.3	128.2	131.9	135.8
Exchange rate (ER), NC/EUR	60.73	61.30	61.27	61.32	61.52	61.2	61.2	61.2
ER, nominal, 2005=100	99.1	100.0	100.0	100.0	100.4	99.8	99.8	99.8
Real ER (CPI-based), 2005=100	102.9	100.0	105.5	103.5	102.8	104.3	105.5	106.5
Real ER (PPI-based), 2005=100	103.3	100.0	106.8	103.6	108.3	110.4	111.9	113.0
PPP, NC/EUR	22.77	21.96	23.57	23.78	24.25	24.6	24.9	25.2
Price level, EU27 = 100	37	36	38	39	39	40	41	41
Average monthly gross wages, NC [1)]	17958	21330	26229	29922	30000	31500	33100	35100
Average monthly gross wages, EUR (ER)	296	348	428	488	488	510	540	570
Average monthly gross wages, EUR (PPP)	789	971	1113	1258	1237	1280	1330	1400
GDP nominal, NC mn	236389	295052	411728	413351	427900	450000	477000	506000
Employed persons - LFS, th., average	549.8	545.3	609.0	629.9	633.0	640	650	660
GDP per employed person, NC	429919	541129	676056	656216	675987	703100	733800	766700
GDP per empl. person, NC at 2000 pr.	429919	481346	504256	483650	483712	488000	494900	502000
Unit labour costs, NC, 2005=100	94.3	100.0	117.4	139.6	140.0	145.7	150.9	157.8
Unit labour costs, ER adj., 2005=100	95.1	100.0	117.4	139.5	139.5	145.9	151.2	158.0
Unit labour costs, PPP adj., Austria=100	35.7	35.4	38.5	43.2	43.4	45.3	46.5	48.1

1) From 2009 including allowances for food and transport.

(Table A/2 ctd.)

(Table A/2 ctd.)

Montenegro

	2000	2005	2008	2009	2010	2011	2012	2013
							Forecast	
Producer price index, 2001=100	74.0	100.0	128.1	123.1	122.2	127.7	131.8	135.5
Consumer price index, 2001=100	63.3	100.0	115.3	119.2	119.9	123.5	127.2	131.0
GDP deflator, 2001=100	67.4	100.0	138.7	142.1	144.4	151.0	155.7	160.1
Exchange rate (ER), EUR/EUR	1	1	1	1	1	1	1	1
Real ER (CPI-based), 2001=100	64.7	92.1	97.9	100.3	98.8	99.7	100.8	101.8
Real ER (PPI-based), 2001=100	.	94.2	106.2	106.0	101.6	104.5	106.2	107.0
PPP, NC/EUR	0.3113	0.4198	0.4561	0.4864	0.4893	0.50	0.51	0.52
Price level, EU27 = 100	31	42	46	49	49	50	51	52
Average monthly gross wages, NC	151	326	609	643	715	750	790	830
Average monthly gross wages, EUR (PPP)	485	778	1335	1322	1461	1490	1550	1610
GDP nominal, NC mn	1065.7	1815.0	3085.6	2981.0	3000	3200	3400	3600
Employed persons - LFS, th., average	230.3	178.8	218.8	212.9	204	206	208	210
GDP per employed person, NC	4627	10150	14102	14002	14706	15500	16300	17100
GDP per empl. person, NC at 2000 pr.	4627	6846	6859	6647	6870	6900	7100	7200
Unit labour costs, NC, 2005=100	68.4	100.0	186.2	202.8	218.2	227.9	233.3	241.7
Unit labour costs, PPP adj., Austria=100	23.1	31.9	55.1	56.6	61.2	63.8	64.8	66.3

Albania

	2000	2005	2008	2009	2010	2011	2012	2013
Producer price index, 2005=100	85.5	100.0	111.1	109.2	109.3	112.6	117.1	124.2
Consumer price index, 2005=100	85.5	100.0	108.9	111.4	115.3	118.8	122.4	127.3
GDP deflator, 2005=100	85.4	100.0	111.1	113.1	116.0	119.8	123.1	128.2
Exchange rate (ER), NC/EUR	132.58	124.19	122.80	132.06	137.79	137	127	122
ER, nominal, 2005=100	106.8	100.0	98.9	106.3	111.0	110.3	102.3	98.2
Real ER (CPI-based), 2005=100	88.9	100.0	101.6	95.7	93.0	94.3	103.0	109.3
Real ER (PPI-based), 2005=100	86.1	100.0	98.8	93.8	87.1	88.7	98.0	106.0
PPP, NC/EUR	48.92	52.11	53.07	55.30	56.17	57.0	57.7	58.9
Price level, EU27 = 100	37	42	43	42	41	42	45	48
Average monthly gross wages, NC	13355	19993	27951	31900	33870	36600	40300	45700
Average monthly gross wages, EUR (ER)	101	161	228	242	246	270	320	370
Average monthly gross wages, EUR (PPP)	273	384	527	577	603	640	700	780
GDP nominal, NC bn	523	815	1088	1144	1220	1300	1390	1520
Employed persons - LFS, th., Oct 2)	1067	932	1123	1160	1100	1060	1100	1200
GDP per employed person, NC	490362	874565	968704	985871	1109091	1226400	1263600	1266700
GDP per empl. person, NC at 2000 pr.	490362	746612	744118	744318	816288	874200	876100	843300
Unit labour costs, NC, 2005=100	101.7	100.0	140.3	160.0	154.9	156.3	171.8	202.4
Unit labour costs, ER adj., 2005=100	95.3	100.0	141.9	150.5	139.7	141.7	168.0	206.0
Unit labour costs, PPP adj., Austria=100	22.9	22.7	29.8	29.8	27.8	28.2	33.1	40.2

Bosnia and Herzegovina

	2000	2005	2008	2009	2010	2011	2012	2013
Producer price index, 2005=100	.	.	.	.	.	.	.	.
Consumer price index, 2005=100	91.1	100.0	115.9	115.4	117.8	119.0	120.2	121.4
GDP deflator, 2005=100	83.7	100.0	121.1	121.1	123.7	125.0	126.1	127.5
Exchange rate (ER), NC/EUR	1.9558	1.9558	1.9558	1.9558	1.9558	1.9558	1.9558	1.9558
ER, nominal, 2005=100	100.0	100.0	100.0	100.0	100.0	100.0	100.0	100.0
Real ER (CPI-based), 2005=100	101.1	100.0	106.9	105.4	105.4	104.3	103.4	102.4
Real ER (PPI-based), 2005=100	.	.	.	.	.	.	.	.
PPP, NC/EUR	0.7893	0.8576	0.9698	0.9897	1.0003	0.99	0.99	0.98
Price level, EU27 = 100	40	44	50	51	51	51	50	50
Average monthly gross wages, NC	539	796	1113	1204	1215	1240	1280	1320
Average monthly gross wages, EUR (ER)	276	407	569	615	621	630	650	670
Average monthly gross wages, EUR (PPP)	683	929	1148	1216	1215	1250	1300	1350
GDP nominal, NC mn	11689	17127	24702	23994	24690	25500	26500	27600
Employed persons - LFS, th., April 3)	635.7	641.5	890.2	859.2	842.8	840	845	850
GDP per employed person, NC	18387	26697	27748	27926	29294	30400	31400	32500
GDP per empl. person, NC at 2000 pr.	18387	22345	19178	19292	19824	20400	20800	21300
Unit labour costs, NC, 2005=100	82.2	100.0	162.8	175.0	172.0	170.5	172.7	173.9
Unit labour costs, ER adj., 2005=100	82.2	100.0	162.8	175.0	172.0	170.5	172.7	173.9
Unit labour costs, PPP adj., Austria=100	26.9	30.9	46.7	47.3	46.7	46.2	46.5	46.2

2) Until 2006 registered employment data. - 3) Until 2005 registered employees.

(Table A/2 ctd.)

(Table A/2 ctd.)

	2000	2005	2008	2009	2010	2011	2012	2013
							Forecast	
Serbia								
Producer price index, 2005=100	37.6	100.0	134.9	142.4	160.5	176.8	186.4	195.2
Consumer price index, 2005=100	31.2	100.0	135.7	147.3	157.4	168.4	178.5	189.2
GDP deflator, 2005=100	29.3	100.0	136.3	145.4	157.8	173.8	183.2	191.9
Exchange rate (ER), NC/EUR	52.55	82.91	81.47	93.92	106.31	110	110	110
ER, nominal, 2005=100	63.4	100.0	98.3	113.3	128.2	132.7	132.7	132.7
Real ER (CPI-based), 2005=100	54.6	100.0	127.3	118.8	109.8	111.2	115.8	120.3
Real ER (PPI-based), 2005=100	63.7	100.0	120.8	114.9	110.6	115.7	120.2	123.4
PPP, NC/EUR	10.23	31.72	40.40	44.47	47.77	51.7	53.7	55.1
Price level, EU27 = 100	19	38	50	47	45	47	49	50
Average monthly gross wages, NC	3799	25514	45674	44147	47450	51790	56000	60550
Average monthly gross wages, EUR (ER)	72	308	561	470	446	470	510	550
Average monthly gross wages, EUR (PPP)	371	804	1130	993	993	1000	1040	1100
GDP nominal, NC bn	384	1683	2722	2815	3100	3500	3800	4100
Employed persons - LFS, th., average	3094	2733	2822	2616	2397	2410	2410	2430
GDP per employed person, NC	124197	615891	964822	1075891	1293172	1452300	1576800	1687200
GDP per empl. person, NC at 2000 pr.	124197	180652	207688	216981	240383	245100	252400	257900
Unit labour costs, NC, 2005=100	21.7	100.0	155.7	144.1	139.8	149.6	157.1	166.2
Unit labour costs, ER adj., 2005=100	34.2	100.0	158.5	127.2	109.0	112.8	118.4	125.3
Unit labour costs, PPP adj., Austria=100	13.6	37.5	55.0	41.7	35.9	37.0	38.6	40.4
Russia								
Producer price index, 2005=100	43.4	100.0	155.7	144.5	162.1	178.4	192.6	208.0
Consumer price index, 2005=100	50.0	100.0	136.7	152.8	163.6	175.1	183.8	193.0
GDP deflator, 2005=100	45.5	100.0	154.6	157.7	173.9	185.8	198.1	210.7
Exchange rate (ER), NC/EUR	26.03	35.26	36.43	44.14	40.30	41	42	42
ER, nominal, 2005=100	73.8	100.0	103.3	125.2	114.3	116.3	119.1	119.1
Real ER (CPI-based), 2005=100	75.1	100.0	122.0	111.5	128.0	131.9	132.8	136.7
Real ER (PPI-based), 2005=100	63.2	100.0	132.6	105.4	125.3	133.3	138.4	146.5
PPP, NC/EUR	7.53	15.06	22.03	22.81	24.90	26.2	27.5	28.6
Price level, EU27 = 100	29	43	60	52	62	64	65	68
Average monthly gross wages, NC	2223	8555	17290	18795	21090	23580	26000	28530
Average monthly gross wages, EUR (ER)	85	243	475	426	523	580	620	680
Average monthly gross wages, EUR (PPP)	295	568	785	824	847	900	950	1000
GDP nominal, NC bn	7306	21610	41265	38797	44491	49500	55000	61000
Employed persons - LFS, th., average	65070	68169	70965	69285	69803	69500	69300	69000
GDP per employed person, NC	112273	317003	581482	559966	637386	712200	793700	884100
GDP per empl. person, NC at 2000 pr.	112273	144166	171040	161524	166730	174300	182200	190800
Unit labour costs, NC, 2005=100	33.4	100.0	170.4	196.1	213.2	228.0	240.5	252.0
Unit labour costs, ER adj., 2005=100	45.2	100.0	164.9	156.7	186.5	196.1	201.9	211.6
Unit labour costs, PPP adj., Austria=100	13.0	27.2	41.7	37.3	44.7	46.8	47.9	49.6
Ukraine								
Producer price index, 2005=100	59.0	100.0	177.5	189.0	228.5	251.4	271.5	290.5
Consumer price index, 2005=100	68.0	100.0	154.1	178.6	195.4	214.9	232.1	248.3
GDP deflator, 2005=100	55.8	100.0	181.2	204.9	233.8	257.2	277.7	297.2
Exchange rate (ER), NC/EUR	5.029	6.389	7.708	10.868	10.533	10.5	10	10
ER, nominal, 2005=100	78.7	100.0	120.6	170.1	164.9	164.4	156.5	156.5
Real ER (CPI-based), 2005=100	95.9	100.0	117.8	95.9	106.0	114.6	127.6	133.9
Real ER (PPI-based), 2005=100	80.6	100.0	129.4	101.5	122.4	132.8	148.4	155.7
PPP, NC/EUR	1.2196	1.9861	3.4052	3.9090	4.3731	4.73	5.03	5.28
Price level, EU27 = 100	24	31	44	36	42	45	50	53
Average monthly gross wages, NC	230	806	1806	1906	2239	2590	2950	3350
Average monthly gross wages, EUR (ER)	46	126	234	175	213	250	300	340
Average monthly gross wages, EUR (PPP)	189	406	530	488	512	550	590	630
GDP nominal, NC mn	170070	441452	948056	913345	1085935	1248300	1415600	1590400
Employed persons - LFS, th., average	20175	20680	20972	20192	20200	20200	20250	20290
GDP per employed person, NC	8430	21347	45205	45234	53759	61800	69900	78400
GDP per empl. person, NC at 2000 pr.	8430	11921	13932	12329	12841	13400	14100	14700
Unit labour costs, NC, 2005=100	40.4	100.0	191.7	228.6	257.8	285.8	309.4	337.0
Unit labour costs, ER adj., 2005=100	51.3	100.0	158.9	134.4	156.4	173.9	197.7	215.3
Unit labour costs, PPP adj., Austria=100	15.1	27.7	40.9	32.6	38.2	42.3	47.7	51.4

(Table A/2 ctd.)

(Table A/2 ctd.)

	2000	2005	2008	2009	2010	2011	2012	2013
							Forecast	
Austria								
Producer price index, 2005=100	90.9	100.0	114.0	105.5	110.8	112.6	114.6	116.6
Consumer price index, 2005=100	90.3	100.0	107.1	107.6	109.5	111.8	113.8	115.9
GDP deflator, 2005=100	92.2	100.0	105.8	106.7	108.0	109.7	111.6	113.5
Real ER (CPI-based), 2005=100	100.2	100.0	98.7	98.3	98.0	98.0	98.0	97.8
Real ER (PPI-based), 2005=100	97.7	100.0	100.3	96.4	97.9	97.8	98.1	97.8
PPP, NC/EUR	1.0352	1.0585	1.0921	1.1213	1.1033	1.098	1.095	1.092
Price level, EU27 = 100	104	106	109	112	110	110	110	109
Average monthly gross wages, EUR	2389	2639	2923	2988	3020	3080	3150	3230
Average monthly gross wages, EUR (PPP)	2307	2493	2676	2664	2737	2806	2876	2958
GDP nominal, NC mn	207529	243585	283085	274320	283100	293900	305000	316600
Employed persons - LFS, th., average	3686	3824	4090	4078	4090	4110	4130	4160
GDP per employed person, NC	56306	63692	69214	67273	69200	71500	73800	76100
GDP per empl. person, NC at 2000 pr.	56306	58721	60291	58121	59091	60100	61000	61800
Unit labour costs, NC, 2005=100	94.4	100.0	107.8	114.4	113.7	114.0	114.9	116.3
Unit labour costs, PPP adjusted	0.53	0.56	0.60	0.64	0.63	0.64	0.64	0.65

NC = national currency (including euro-fixed series for euro area countries - EE, SK, SI, AT). ER = Exchange Rate, PPP = Purchasing Power Parity, Price level: PPP/ ER.

The development of unit labour costs is defined as gross wages in EUR relative to labour productivitiy (real GDP per employed person) .

PPP rates have been taken from Eurostat based on the benchmark results 2005. For Albania, Bosnia and Herzegovina, Montenegro and Serbia available data 2005-2009 have been extrapolated by wiiw with GDP deflators. Russia and Ukraine are estimated by wiiw using the OECD PPP benchmark results 2005 and extrapolation with GDP price deflators.

Real exchange rates: Increasing values mean real appreciation.

Sources: wiiw Database incorporating national and Eurostat statistics; WIFO; OECD for purchasing power parities, 2005 benchmark year, November 2007; wiiw estimates and forecasts.

Table A/3

Indicators of macro-competitiveness, 2000-2013

annual changes in %

	2000	2005	2008	2009	2010	2011	2012 Forecast	2013	2005-08 average
Bulgaria									
GDP deflator	6.6	7.3	8.4	4.0	4.5	3.8	4.1	4.2	8.0
Exchange rate (ER), EUR/NC	0.2	-0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Real ER (CPI-based)	8.5	3.6	8.0	1.5	0.9	1.9	2.2	2.0	5.4
Real ER (PPI-based)	13.6	3.4	4.4	-2.9	5.0	2.1	2.5	2.1	5.0
Average gross wages, NC	11.7	10.7	21.8	12.8	8.5	7.5	7.2	6.8	15.7
Average gross wages, real (PPI based)	-5.3	2.6	9.8	20.6	-0.1	3.5	3.1	2.5	5.6
Average gross wages, real (CPI based)	1.2	4.4	8.8	10.1	5.3	3.3	3.1	2.7	6.9
Average gross wages, EUR (ER)	11.9	10.6	21.8	12.8	8.5	6.6	8.6	5.3	15.7
Employed persons (LFS)	-2.8	2.0	3.3	-3.2	-5.8	1.1	1.6	1.6	3.6
GDP per empl. person, NC at 2000 prices	8.8	4.3	2.8	-1.8	6.5	1.5	1.5	1.4	2.7
Unit labour costs, NC at 2000 prices	2.7	6.2	18.5	14.9	1.8	5.9	5.7	5.2	12.7
Unit labour costs, ER (EUR) adjusted	2.9	6.0	18.5	14.9	1.8	5.9	5.7	5.2	12.6
Czech Republic									
GDP deflator	1.5	-0.4	1.9	2.5	-0.6	0.8	1.9	2.0	1.5
Exchange rate (ER), EUR/NC	3.6	7.1	11.3	-5.6	4.6	3.2	2.1	0.0	6.3
Real ER (CPI-based)	5.6	6.5	14.1	-6.0	3.6	3.1	2.3	0.0	7.0
Real ER (PPI-based)	9.2	3.2	5.2	-3.5	1.1	2.3	2.5	0.0	2.8
Average gross wages, NC	3.3	5.0	7.8	4.0	2.2	2.9	4.5	5.0	6.6
Average gross wages, real (PPI based)	-5.7	4.5	7.4	5.6	2.2	2.1	2.5	3.0	5.7
Average gross wages, real (CPI based)	-0.6	3.3	1.4	3.3	1.0	0.9	2.4	3.0	3.3
Average gross wages, EUR (ER)	7.0	12.5	20.0	-1.9	6.8	6.4	6.9	4.6	13.4
Employed persons (LFS)	-0.7	1.2	1.6	-1.4	-1.0	0.1	0.4	0.4	1.5
GDP per empl. person, NC at 2000 prices	4.3	5.1	0.8	-2.8	3.4	2.1	2.1	3.3	3.8
Unit labour costs, NC at 2000 prices	-1.0	-0.1	7.0	6.9	-1.2	0.8	2.3	1.7	2.7
Unit labour costs, ER (EUR) adjusted	2.6	7.0	19.0	0.9	3.3	4.0	4.4	1.7	9.2
Estonia									
GDP deflator	4.5	5.4	7.2	-0.1	2.9	4.2	3.4	4.6	7.9
Exchange rate (ER), EUR/NC	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Real ER (CPI-based)	2.1	1.9	6.7	-0.8	0.6	1.9	1.7	2.5	3.7
Real ER (PPI-based)	0.8	-2.3	1.7	4.6	-0.2	2.4	1.8	2.5	1.1
Average gross wages, NC	10.5	10.8	13.9	-5.0	0.8	5.1	4.8	5.7	15.4
Average gross wages, real (PPI based)	5.4	8.9	5.4	-5.7	-2.4	0.9	1.4	1.1	9.4
Average gross wages, real (CPI based)	6.3	6.4	3.0	-5.2	-1.9	1.0	1.3	1.2	8.4
Average gross wages, EUR (ER)	10.5	10.8	13.9	-5.0	0.8	5.1	4.8	5.7	15.4
Employed persons (LFS)	-1.2	2.0	0.2	-9.2	-4.2	4.2	2.5	1.6	2.5
GDP per empl. person, NC at 2000 prices	11.3	7.3	-5.3	-5.1	7.6	0.4	1.3	2.5	2.7
Unit labour costs, NC at 2000 prices	-0.7	3.2	20.2	0.1	-6.3	4.7	3.5	3.2	12.3
Unit labour costs, ER (EUR) adjusted	-0.7	3.2	20.2	0.1	-6.3	4.7	3.5	3.2	12.3
Hungary									
GDP deflator	9.5	2.3	4.7	4.4	3.9	2.9	3.1	3.1	4.3
Exchange rate (ER), EUR/NC	-2.8	1.5	-0.1	-10.3	1.8	-1.6	1.8	0.0	0.0
Real ER (CPI-based)	4.8	2.7	2.2	-7.6	4.4	0.1	3.5	1.5	2.7
Real ER (PPI-based)	3.8	0.4	-1.6	-2.6	4.6	-0.5	3.5	1.1	-0.6
Average gross wages, NC	13.7	8.8	7.4	0.6	2.1	4.4	5.1	6.1	8.1
Average gross wages, real (PPI based)	2.3	5.5	2.7	-3.8	-4.0	1.5	1.9	2.9	4.3
Average gross wages, real (CPI based)	3.5	5.1	1.3	-3.3	-2.5	0.5	1.5	2.5	2.6
Average gross wages, EUR (ER)	10.5	10.4	7.3	-9.8	3.9	2.6	6.6	6.2	8.1
Employed persons (LFS)	1.2	0.0	-1.2	-2.5	0.0	1.1	1.0	1.0	-0.1
GDP per empl. person, NC at 2000 prices	3.6	3.2	2.1	-4.3	1.3	1.4	1.9	1.9	2.2
Unit labour costs, NC at 2000 prices	9.8	5.5	5.2	5.1	0.8	2.9	3.1	4.1	5.7
Unit labour costs, ER (EUR) adjusted	6.7	7.0	5.2	-5.7	2.6	1.3	5.0	4.1	5.8
Latvia									
GDP deflator	4.2	10.1	14.4	-1.5	-1.0	2.9	3.0	3.6	13.6
Exchange rate (ER), EUR/NC	11.7	-4.5	-0.4	-0.4	-0.4	0.0	0.0	0.0	-1.4
Real ER (CPI-based)	12.5	-0.1	10.7	1.8	-3.7	0.9	1.2	1.5	5.4
Real ER (PPI-based)	9.3	-1.0	4.5	-1.3	-1.0	1.2	1.4	1.6	5.3
Average gross wages, NC	6.1	16.5	20.5	-3.8	-3.9	3.8	4.3	6.3	22.8
Average gross wages, real (PPI based)	4.2	7.9	8.1	0.9	-6.5	0.9	1.3	2.6	10.2
Average gross wages, real (CPI based)	3.4	9.0	4.5	-6.8	-2.7	0.8	1.3	2.7	12.0
Average gross wages, EUR (ER)	18.5	11.3	20.0	-4.2	-4.3	4.0	4.6	5.9	21.1
Employed persons (LFS)	-2.8	1.6	0.6	-12.6	-3.9	2.6	5.2	2.9	2.5
GDP per empl. person, NC at 2000 prices	10.0	9.0	-4.8	-6.2	3.6	0.1	-1.4	1.4	4.3
Unit labour costs, NC at 2000 prices	-3.6	6.9	26.6	2.6	-7.2	3.8	5.8	4.8	17.7
Unit labour costs, ER (EUR) adjusted	7.7	2.2	26.1	2.1	-7.6	3.8	5.8	4.8	16.1

(Table A/3 ctd.)

Table A/3 (ctd.)

	2000	2005	2008	2009	2010	2011	2012	2013	2005-08
							Forecast		average
Lithuania									
GDP deflator	0.9	6.7	9.8	-3.7	3.0	3.0	2.5	2.5	7.9
Exchange rate (ER), EUR/NC	15.6	0.0	0.0	0.0	0.0	0.1	0.0	0.0	0.0
Real ER (CPI-based)	14.6	0.5	7.1	3.1	-0.9	1.0	0.7	0.5	3.1
Real ER (PPI-based)	29.1	7.2	11.2	-10.2	6.7	1.3	1.0	0.5	6.4
Average gross wages, NC	-1.7	11.0	19.4	-4.4	0.7	4.3	5.1	5.7	17.0
Average gross wages, real (PPI based)	-15.4	-0.5	1.0	10.5	-8.8	1.3	2.5	3.1	5.4
Average gross wages, real (CPI based)	-2.7	8.2	7.5	-8.3	-0.5	1.3	2.5	3.1	10.6
Average gross wages, EUR (ER)	13.6	11.0	19.4	-4.4	0.7	5.1	4.8	6.1	17.0
Employed persons (LFS)	-4.0	2.6	-0.9	-6.8	-5.0	2.6	2.9	2.1	1.4
GDP per empl. person, NC at 2000 prices	7.6	5.0	3.8	-8.5	6.7	0.2	0.8	1.7	5.6
Unit labour costs, NC at 2000 prices	-8.6	5.8	15.0	4.4	-5.6	4.2	4.3	3.9	10.8
Unit labour costs, ER (EUR) adjusted	5.6	5.8	15.0	4.4	-5.6	4.3	4.3	3.9	10.8
Poland									
GDP deflator	7.2	2.6	3.1	3.6	2.7	3.7	2.2	2.3	2.8
Exchange rate (ER), EUR/NC	5.5	12.5	7.7	-18.8	8.3	2.4	0.0	-2.5	6.6
Real ER (CPI-based)	13.9	12.5	8.3	-16.5	8.9	3.8	0.7	-2.0	6.5
Real ER (PPI-based)	9.5	8.4	3.9	-12.5	7.2	3.2	1.0	-2.5	3.8
Average gross wages, NC	11.6	3.8	10.1	5.5	3.8	7.4	7.2	6.7	6.7
Average gross wages, real (PPI based)	3.4	3.4	7.5	1.5	1.5	4.8	4.6	4.6	4.9
Average gross wages, real (CPI based)	1.3	1.7	5.6	1.4	1.1	3.8	4.6	4.1	4.0
Average gross wages, EUR (ER)	17.7	16.8	18.6	-14.4	12.5	10.3	6.7	4.2	13.6
Employed persons (LFS)	-1.6	2.3	3.7	0.4	0.2	0.3	2.0	2.5	3.5
GDP per empl. person, NC at 2000 prices	6.0	1.3	1.4	1.2	3.5	3.5	2.1	1.7	1.9
Unit labour costs, NC at 2000 prices	5.3	2.5	8.6	4.2	0.4	3.7	5.0	5.0	4.6
Unit labour costs, ER (EUR) adjusted	11.1	15.4	16.9	-15.4	8.7	6.3	5.0	2.4	11.5
Romania									
GDP deflator	43.3	12.2	15.2	4.1	6.2	4.8	5.9	5.3	12.9
Exchange rate (ER), EUR/NC	-18.2	11.9	-9.4	-13.1	0.7	-2.0	-2.3	0.0	2.4
Real ER (CPI-based)	16.9	19.4	-5.8	-9.2	4.6	1.2	-0.2	2.0	6.9
Real ER (PPI-based)	23.3	16.1	-1.7	-8.2	3.5	0.9	2.0	3.2	8.1
Average gross wages, NC	47.8	18.3	26.1	4.8	5.1	7.7	8.1	6.6	21.1
Average gross wages, real (PPI based)	-5.7	9.4	9.4	2.9	-1.1	2.8	2.1	1.3	10.0
Average gross wages, real (CPI based)	1.5	8.4	16.9	-0.8	-0.9	2.1	4.0	2.5	13.1
Average gross wages, EUR (ER)	20.9	32.3	14.2	-9.0	5.8	6.4	4.1	7.8	24.0
Employed persons (LFS)	-0.3	-0.5	0.2	-1.3	-0.5	-0.5	0.5	0.0	0.6
GDP per empl. person, NC at 2000 prices	2.7	4.6	7.2	-5.8	-0.7	2.7	3.0	3.6	5.8
Unit labour costs, NC at 2000 prices	43.9	13.0	17.7	11.3	5.9	4.9	5.0	2.9	14.5
Unit labour costs, ER (EUR) adjusted	17.7	26.5	6.6	-3.4	6.6	2.7	2.6	2.9	17.2
Slovakia									
GDP deflator	9.4	2.4	2.9	-1.1	0.9	0.9	1.0	2.0	2.3
Exchange rate (ER), EUR/NC	3.6	3.7	8.0	3.8	0.0	0.0	0.0	0.0	6.4
Real ER (CPI-based)	13.8	4.3	8.3	3.7	-1.4	-0.1	1.2	1.0	7.0
Real ER (PPI-based)	10.5	2.9	4.2	0.6	-3.2	-0.7	0.5	0.0	3.9
Average gross wages, NC	6.5	9.2	8.1	3.0	2.8	4.6	6.3	8.2	8.3
Average gross wages, real (PPI based)	-4.0	5.6	5.5	10.3	2.6	3.5	4.2	6.1	6.3
Average gross wages, real (CPI based)	-4.9	6.2	4.0	2.0	2.0	2.5	3.2	5.1	4.9
Average gross wages, EUR (ER)	10.3	13.2	16.8	6.9	2.8	4.6	6.3	8.2	15.2
Employed persons (LFS)	-1.4	2.1	3.2	-2.8	-2.8	0.9	0.9	0.9	2.9
GDP per empl. person, NC at 2000 prices	2.9	4.5	2.5	-2.1	7.1	3.0	3.1	3.9	4.8
Unit labour costs, NC at 2000 prices	3.6	4.5	5.4	5.2	-4.0	1.5	3.0	4.2	3.3
Unit labour costs, ER (EUR) adjusted	7.3	8.3	13.9	9.2	-4.0	1.5	3.0	4.2	9.9
Slovenia									
GDP deflator	5.4	1.6	4.1	3.2	2.1	2.8	2.5	2.5	3.0
Exchange rate (ER), EUR/NC	-6.3	-0.2	0.0	0.0	0.0	0.0	0.0	0.0	-0.1
Real ER (CPI-based)	0.2	0.1	1.8	-0.1	0.0	0.7	0.7	0.5	0.9
Real ER (PPI-based)	-3.2	-2.4	-2.2	2.4	-1.4	0.8	1.0	0.0	-1.2
Average gross wages, NC	10.6	3.6	8.3	3.4	4.2	4.0	3.8	4.3	5.7
Average gross wages, real (PPI based)	3.0	1.7	4.3	4.9	2.2	1.5	1.3	2.3	2.5
Average gross wages, real (CPI based)	1.6	1.1	2.6	2.5	2.1	1.2	1.3	1.8	2.0
Average gross wages, EUR (ER)	3.7	3.4	8.3	3.4	4.2	4.0	3.8	4.3	5.6
Employed persons (LFS)	1.7	0.7	1.1	-1.5	-1.5	0.0	1.0	0.9	1.4
GDP per empl. person, NC at 2000 prices	2.6	3.8	2.6	-6.6	2.7	1.9	1.6	1.9	3.8
Unit labour costs, NC at 2000 prices	7.8	-0.2	5.6	10.8	1.5	2.0	2.2	2.3	1.8
Unit labour costs, ER (EUR) adjusted	1.0	-0.4	5.6	10.8	1.5	2.0	2.2	2.3	1.7

(Table A/3 ctd.)

Table A/3 (ctd.)

	2000	2005	2008	2009	2010	2011	2012	2013	2005-08
							Forecast		average
Croatia									
GDP deflator	4.6	3.3	6.3	3.3	1.2	2.5	2.0	2.5	4.3
Exchange rate (ER), EUR/NC	-0.7	1.3	1.6	-1.6	0.7	-0.2	0.0	0.0	0.9
Real ER (CPI-based)	3.5	2.4	3.9	-0.2	-0.2	0.2	0.2	0.5	2.2
Real ER (PPI-based)	4.8	-0.2	3.5	1.7	1.6	2.1	2.0	7.0	0.9
Average gross wages, NC	7.0	4.4	7.1	2.2	-0.8	3.0	4.1	5.6	6.0
Average gross wages, real (PPI based)	-2.5	1.7	-1.1	2.7	-4.9	-1.0	0.5	-3.2	1.6
Average gross wages, real (CPI based)	0.7	1.0	0.9	-0.2	-1.9	0.5	2.0	3.0	2.0
Average gross wages, EUR (ER)	6.3	5.7	8.7	0.6	-0.1	2.9	3.7	6.3	6.9
Employed persons (LFS)	4.1	0.7	1.3	-1.8	-4.1	-1.0	0.3	1.3	1.1
GDP per empl. person, NC at 2000 prices	-1.0	3.5	1.1	-4.0	2.7	2.0	1.6	1.7	3.0
Unit labour costs, NC at 2000 prices	8.1	0.9	5.9	6.5	-3.4	1.0	2.4	3.9	2.9
Unit labour costs, ER (EUR) adjusted	7.4	2.2	7.6	4.8	-2.7	0.8	2.4	3.9	3.8
Macedonia									
GDP deflator	8.2	3.8	7.5	1.2	3.0	3.1	2.9	3.0	5.5
Exchange rate (ER), EUR/NC	-0.2	0.1	-0.1	-0.1	-0.3	0.5	0.0	0.0	0.0
Real ER (CPI-based)	3.6	-1.6	4.3	-1.9	-0.7	1.4	1.2	1.0	0.9
Real ER (PPI-based)	6.3	-0.9	3.7	-3.0	4.6	1.9	1.4	1.0	1.4
Average gross wages, NC [1)]	9.0	2.7	8.7	9.0	0.3	5.0	5.1	6.0	6.0
Average gross wages, real (PPI based)	-1.5	-0.5	-1.5	16.6	-7.6	1.8	2.1	3.0	0.2
Average gross wages, real (CPI based)	3.1	2.2	0.3	9.9	-1.4	1.9	2.0	3.0	2.4
Average gross wages, EUR (ER)	8.8	2.8	8.5	9.1	0.0	4.6	5.9	5.6	6.0
Employed persons (LFS)	0.8	4.3	3.2	3.4	0.5	1.1	1.6	1.5	3.9
GDP per empl. person, NC at 2000 prices	3.6	0.1	1.7	-4.1	0.0	0.9	1.4	1.4	1.2
Unit labour costs, NC at 2000 prices	5.2	2.6	6.9	13.6	0.2	4.1	3.6	4.5	4.8
Unit labour costs, ER (EUR) adjusted	5.0	2.7	6.7	13.5	-0.1	4.6	3.6	4.5	4.8
Montenegro									
GDP deflator	.	4.3	7.7	2.4	1.6	4.6	3.2	2.8	9.7
Real ER (CPI-based)	.	0.1	3.6	2.4	-1.5	0.9	1.2	1.0	1.6
Real ER (PPI-based)	.	-2.0	7.3	-0.2	-4.1	2.8	1.6	0.8	2.5
Average gross wages, NC	.	7.8	22.5	5.6	11.2	4.9	5.3	5.1	19.1
Average gross wages, real (PPI based)	.	5.6	7.5	9.9	12.1	0.3	2.1	2.2	11.3
Average gross wages, real (CPI based)	.	5.4	14.1	2.1	10.5	1.8	2.3	2.0	14.3
Employed persons (LFS)	.	-4.5	0.6	-2.7	-4.2	1.0	1.0	1.0	4.0
GDP per empl. person, NC	.	13.9	14.4	-0.7	5.0	5.4	5.2	4.9	12.2
GDP per empl. person, NC at 2000 prices	.	9.1	6.2	-3.1	3.4	0.4	2.9	1.4	2.3
Unit labour costs, NC at 2000 prices	.	-1.2	15.4	8.9	7.6	4.4	2.4	3.6	16.5
Unit labour costs, ER (EUR) adjusted	.	-1.2	15.4	8.9	7.6	4.4	2.4	3.6	16.5
Albania									
GDP deflator	4.0	2.6	4.4	1.7	2.6	3.3	2.8	4.1	3.3
Exchange rate (ER), EUR/NC	10.8	2.8	0.7	-7.0	-4.2	0.6	7.9	4.1	1.0
Real ER (CPI-based)	8.8	3.0	0.3	-5.8	-2.8	1.5	9.1	6.1	1.1
Real ER (PPI-based)	13.5	3.5	0.9	-5.0	-7.2	1.9	10.5	8.2	0.6
Average gross wages, NC	10.2	5.0	2.2	14.1	6.2	8.1	10.1	13.4	10.1
Average gross wages, real (PPI based)	3.5	0.1	-4.1	16.0	6.1	4.9	5.9	7.0	5.9
Average gross wages, real (CPI based)	10.2	2.6	-1.1	11.6	2.6	4.9	6.9	9.0	7.1
Average gross wages, EUR (ER)	22.2	8.0	2.9	6.1	1.8	9.8	18.5	15.6	11.2
Employed persons (LFS) [2)]	-0.8	0.3	-6.2	3.3	-5.2	-3.6	3.8	9.1	-1.0
GDP per empl. person, NC at 2000 prices	7.5	5.4	14.8	0.0	9.7	7.1	0.2	-3.7	7.3
Unit labour costs, NC at 2000 prices	2.5	-0.3	-11.0	14.1	-3.2	0.9	9.9	17.8	2.6
Unit labour costs, ER (EUR) adjusted	13.6	2.5	-10.4	6.1	-7.2	1.5	18.5	22.6	3.6
Bosnia and Herzegovina									
GDP deflator	4.1	4.4	7.4	0.0	2.1	1.1	0.9	1.1	6.0
Exchange rate (ER), EUR/NC	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Real ER (CPI-based)	2.9	0.8	3.7	-1.4	0.0	-1.1	-0.8	-1.0	1.9
Real ER (PPI-based)	.	.	.	.	.	.	.	.	.
Average gross wages, NC	7.2	6.5	16.7	8.1	0.9	2.1	3.2	3.1	10.4
Average gross wages, real (PPI based)	.	.	.	.	.	.	.	.	.
Average gross wages, real (CPI based)	2.2	3.4	8.5	8.6	-1.1	1.0	2.2	2.1	5.7
Average gross wages, EUR (ER)	7.2	6.5	16.7	8.1	0.9	2.1	3.2	3.1	10.4
Employed persons (LFS) [3)]	-0.8	0.5	4.8	-3.5	-1.9	-0.3	0.6	0.6	2.8
GDP per empl. person, NC at 2000 prices	16.1	3.4	0.9	0.6	2.8	2.9	2.0	2.4	2.6
Unit labour costs, NC at 2000 prices	-7.7	3.0	15.7	7.5	-1.8	-0.8	1.2	0.7	7.6
Unit labour costs, ER (EUR) adjusted	-7.7	3.0	15.7	7.5	-1.8	-0.8	1.2	0.7	7.6

1) In 2009 wiiw estimate (including allowances for food and transport). - 2) Until 2007 registered employment data. - 3) Until 2006 registered employees.

(Table A/3 ctd.)

Table A/3 (ctd.)

	2000	2005	2008	2009	2010	2011	2012	2013	2005-08
							Forecast		average
Serbia									
GDP deflator	77.5	15.5	12.1	6.7	8.5	10.1	5.4	4.8	12.0
Exchange rate (ER), NC/EUR	-52.2	-12.5	-1.8	-13.3	-11.7	-3.4	0.0	0.0	-2.9
Real ER (CPI-based)	-15.7	-0.5	7.5	-6.7	-7.6	1.3	4.1	3.9	6.1
Real ER (PPI-based)	-6.8	-4.1	3.9	-4.9	-3.7	4.7	3.9	2.7	3.7
Average gross wages, NC	90.7	24.1	17.9	-3.3	7.5	9.1	8.1	8.1	22.1
Average gross wages, real (PPI based)	-5.9	8.7	4.9	-8.5	-4.6	-0.9	2.6	3.2	9.6
Average gross wages, real (CPI based)	6.2	6.8	3.9	-11.0	0.6	2.0	2.0	2.0	9.0
Average gross wages, EUR (ER)	-8.8	8.6	15.7	-16.2	-5.1	5.3	8.5	7.8	18.6
Employed persons (LFS)	-0.3	-6.7	6.3	-7.3	-8.4	0.5	0.0	0.8	-0.9
GDP per empl. person, NC at 2000 prices	5.6	13.2	-0.7	4.5	10.8	2.0	3.0	2.2	6.8
Unit labour costs, NC at 2000 prices	80.7	9.6	18.7	-7.5	-3.0	7.0	5.0	5.8	14.3
Unit labour costs, ER (EUR) adjusted	-13.6	-4.1	16.5	-19.7	-14.3	3.5	5.0	5.8	11.0
Russia									
GDP deflator	37.7	19.3	18.0	2.0	10.3	6.9	6.6	6.3	16.5
Exchange rate (ER), NC/EUR	0.8	1.6	-3.9	-17.5	9.5	-1.7	-2.4	0.0	-0.4
Real ER (CPI-based)	19.5	11.8	5.8	-8.7	14.8	3.0	0.7	2.9	8.1
Real ER (PPI-based)	42.1	17.7	9.8	-20.5	18.9	6.3	3.9	5.9	11.8
Average gross wages, NC	46.0	26.9	27.2	8.7	12.2	11.8	10.3	9.7	26.6
Average gross wages, real (PPI based)	-0.4	5.2	4.8	17.1	0.0	1.6	2.1	1.6	8.1
Average gross wages, real (CPI based)	20.9	12.8	11.5	-2.8	4.8	4.5	5.0	4.5	13.7
Average gross wages, EUR (ER)	47.2	28.9	22.3	-10.3	22.9	10.8	6.9	9.7	26.0
Employed persons (LFS)	3.4	1.3	0.6	-2.4	0.7	-0.4	-0.3	-0.4	1.3
GDP per empl. person, NC at 2000 prices	6.4	5.0	4.6	-5.6	3.2	4.5	4.5	4.7	5.6
Unit labour costs, NC at 2000 prices	37.2	20.9	21.6	15.1	8.7	7.0	5.5	4.8	19.8
Unit labour costs, ER (EUR) adjusted	38.3	22.8	16.9	-5.0	19.1	5.1	3.0	4.8	19.3
Ukraine									
GDP deflator	23.1	24.6	28.6	13.1	14.1	10.0	8.0	7.0	22.6
Exchange rate (ER), NC/EUR	-12.6	3.5	-10.3	-29.1	3.2	0.3	5.0	0.0	-3.8
Real ER (CPI-based)	9.9	14.9	8.4	-18.6	10.6	8.1	11.4	4.9	7.9
Real ER (PPI-based)	1.5	15.9	14.5	-21.6	20.6	8.5	11.7	4.9	10.7
Average gross wages, NC	29.6	36.7	33.7	5.5	17.5	15.7	13.9	13.6	32.3
Average gross wages, real (PPI based)	7.3	17.2	-1.3	-0.9	-2.8	5.2	5.5	6.1	10.3
Average gross wages, real (CPI based)	1.1	20.5	6.8	-8.9	7.4	5.2	5.5	6.1	15.0
Average gross wages, EUR (ER)	13.3	41.4	20.0	-25.1	21.2	17.6	20.0	13.3	27.3
Employed persons (LFS)	0.6	1.9	0.3	-3.7	0.0	0.0	0.2	0.2	0.8
GDP per empl. person, NC at 2000 prices	5.2	0.8	2.0	-11.5	4.2	4.4	5.2	4.3	4.2
Unit labour costs, NC at 2000 prices	23.2	35.7	31.1	19.3	12.8	10.9	8.2	8.9	27.0
Unit labour costs, ER (EUR) adjusted	7.6	40.3	17.7	-15.4	16.4	11.2	13.7	8.9	22.2
Austria									
GDP deflator	1.1	2.1	1.9	0.8	1.2	1.6	1.8	1.7	2.0
Real ER (CPI-based)	0.5	0.1	-0.5	-0.5	-0.3	0.0	0.0	-0.2	-0.3
Real ER (PPI-based)	0.0	-2.0	0.1	-3.8	1.5	-0.1	0.3	-0.3	-0.4
Average gross wages, NC	2.6	2.3	3.5	2.2	1.1	2.0	2.3	2.5	3.2
Average gross wages, real (PPI based)	-1.3	0.2	-2.7	10.4	-3.7	0.4	0.5	0.8	-0.7
Average gross wages, real (CPI based)	0.2	0.0	0.3	1.7	-0.7	-0.1	0.5	0.7	0.9
Employed persons (LFS)	0.4	2.1	1.5	-0.3	0.3	0.5	0.5	0.7	2.2
GDP per empl. person, NC at 2000 prices	3.2	0.3	0.6	-3.6	1.7	1.7	1.5	1.3	0.7
Unit labour costs, NC at 2000 prices	-0.6	2.0	2.9	6.0	-0.6	0.3	0.8	1.2	2.4
Unit labour costs, ER (EUR) adjusted	-0.6	2.0	2.9	6.0	-0.6	0.3	0.8	1.2	2.4

NC = national currency (including euro-fixed series for euro area countries - EE, SK, SI, AT). ER = Exchange Rate, PPI = Producer price index, CPI = Consumer price index. Positive growth of real exchange rates means real apprecaition.

Sources: wiiw Database incorporating national and Eurostat statistics, wiiw estimates. Forecasts by wiiw.

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