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Transition Countries Clamber Aboard the Business Boom in Western Europe

Upswing masks persistent transition-related problems

Josef Pöschl, Helen Boss, Vladimir Gligorov, Gábor Hunya, Zdenek Lukas, Leon Podkaminer, Sándor Richter and Hermine Vidovic are WIIW research economists; Peter Havlik is WIIW Deputy Director.

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Executive summary

This report provides an overview of macro-economic developments in 1999 and discusses the economic outlook for the next two years. It covers twelve transition countries: Bulgaria, Croatia, the Czech Republic, Hungary, Macedonia (FYRM), Poland, Romania, Russia, Slovakia, Slovenia, Ukraine and Yugoslavia (Serbia and Montenegro). In a few graphs and tables as well as in some passages of the text the Baltic States have been included, together with Germany as a reference country, so as to provide a broader view.

In the recent past, more or less all transition countries were confronted with a slowdown of economic growth or even an intensifying GDP decline. GDP growth rates tumbled from quarter to quarter. The trend bottomed out in late 1998 or early 1999. Despite this general tendency, the contrast between individual countries was striking. In the second quarter of 1999 growth rates started to rise once more in one group of countries – and GDP shrinkage diminished in the other. For all countries more recent data point to an improving business climate. Industrial output statistics reveal a quite similar tendency: a downswing in 1998 and an upswing in 1999 in all CEECs plus Russia. Labour productivity growth rates in industry behaved correspondingly: In most of the countries, they turned negative in 1998 and rose in 1999. Unit labour costs in euro terms rose in most of the countries during the slump but relaxed thereafter.

From a longer-term point of view, only three of the transition countries considered in this report – Hungary, Poland and Slovenia – give the impression of having been relatively successful. They were able to achieve and maintain GDP growth. Other economies started growing substantially at some point of time, only to experience severe setbacks later. The phenomenon of permanent or re-emergent transitional recession has appeared in countries where the transformation of the financial and non-financial corporate sector has been incomplete, thus restricting the efficiency of the new institutions and institutional settings. In most of the countries related problems are persisting, so that we can expect some temporary upswing for this and the coming year, but no smooth continuation of growth at high rates.

The WIIW forecasts a strengthening of the positive signals now visible. Thus, in 2000 in almost all transition countries GDP growth will be better than it was in 1999 and may strengthen further in 2001. Over the next few years, most of the countries will encounter difficulties in their attempts to secure high GDP growth, while simultaneously limiting their current account deficits. Countries with two-digit inflation rates will enjoy some measure of decline, while those that already enjoyed relatively low rates in the past will experience some increase. An unemployment rate of around 12% seems to be establishing itself as the norm for the transition countries.

Figure 1

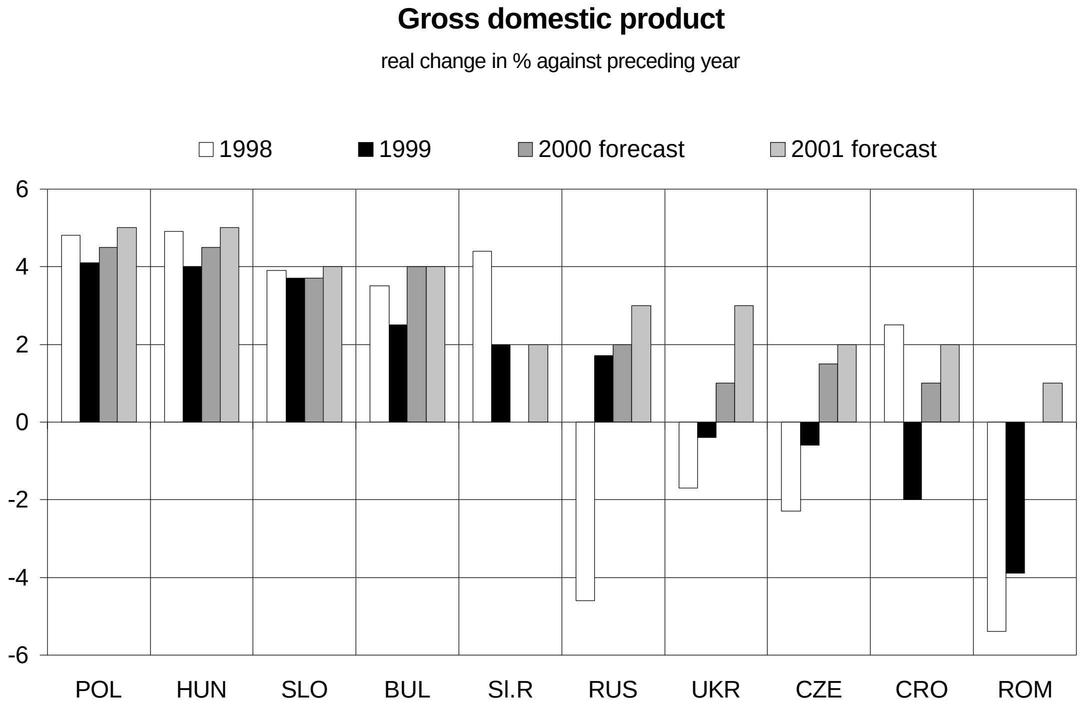
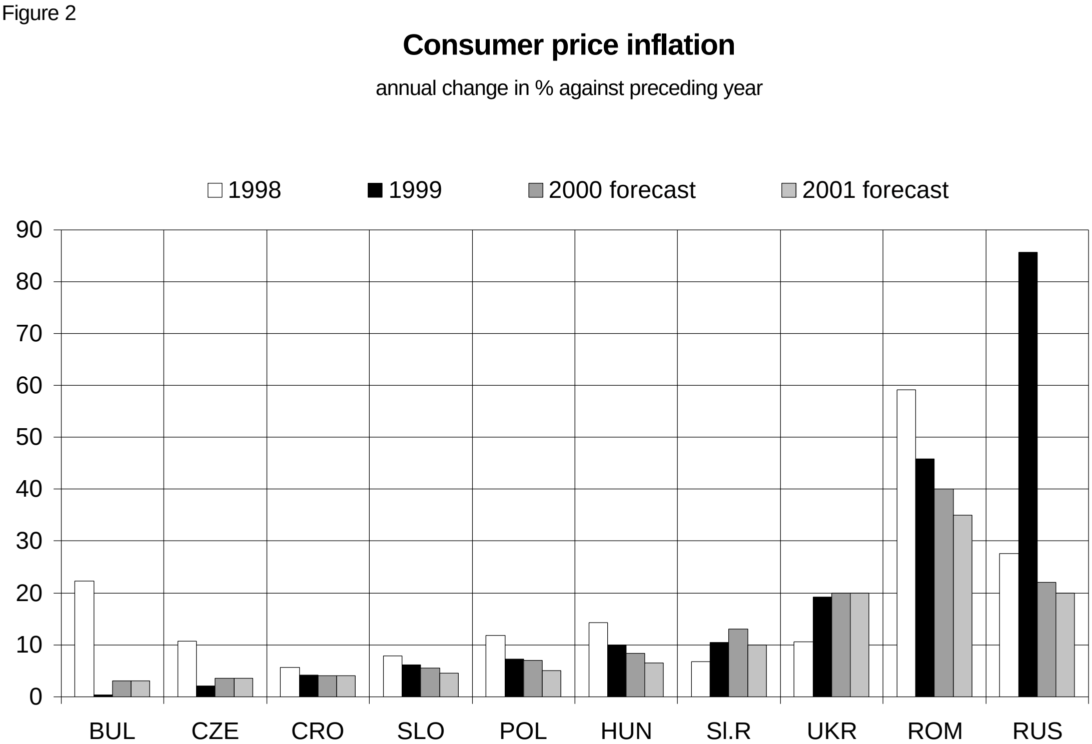


Figure 2



Josef Pöschl *

Transition countries clamber aboard the business boom in Western Europe. Upswing masks persistent transition-related problems

The world economy is **just recovering** from the damage inflicted by last years' financial crises and economic setbacks in East Asia, Russia and Brazil. For the EU, forecasts anticipate growth in 2000 being greater than the year previous. Apparently, the wave has also rolled over the countries of Central and Eastern Europe (CEECs), taking in its undertow the EU candidate countries in the region (the CEEC-7[1] plus the Baltic States), the non-candidate countries in the area of former Yugoslavia and – after a protracted period of economic decline – even Russia and Ukraine, the leading powers within the Commonwealth of Independent States (CIS). The latter fact is most remarkable, as it could presage a turnaround in the long-term trend.

This report provides an **overview of macro-economic developments in 1999 and discusses the economic outlook over the next two years**. It covers twelve countries: Bulgaria, Croatia, the Czech Republic, Hungary, Macedonia (FYRM), Poland, Romania, Russia, Slovakia, Slovenia, Ukraine and Yugoslavia (Serbia and Montenegro)[2]. At the present point in time, economic performance is improving in all the above countries, albeit under quite diverse conditions. The crucial tasks in the future will remain corporate restructuring and consolidating the financial system. The slow-down in growth that manifested itself in some countries in the past and the deep recession experienced in others have increased corporate debt and weakened the position of financial intermediaries. The growth prospects for 2000 and 2001 are mixed. Long-term growth will become more likely in countries where: (a) enterprises manage to make full use of the enhanced business climate as a basis for improving their productive assets, both physical and human; and (b) policy-makers seize the opportunity to ameliorate the legal and administrative infrastructure essential to efficient economic activity.

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* The author wishes to thank V. Gligorov, G. Hunya, P. Havlik, K. Laski, Z. Lukas and S. Richter for their valuable comments, and H. Rusková and B. Assenova for statistical support.

1 Bulgaria, the Czech Republic, Hungary, Poland, Romania, Slovakia and Slovenia.

2 In a few graphs or tables as well as in some passages of the text the Baltic States have been included, together with Germany as a reference country, so as to provide a broader view.

Figure 3a

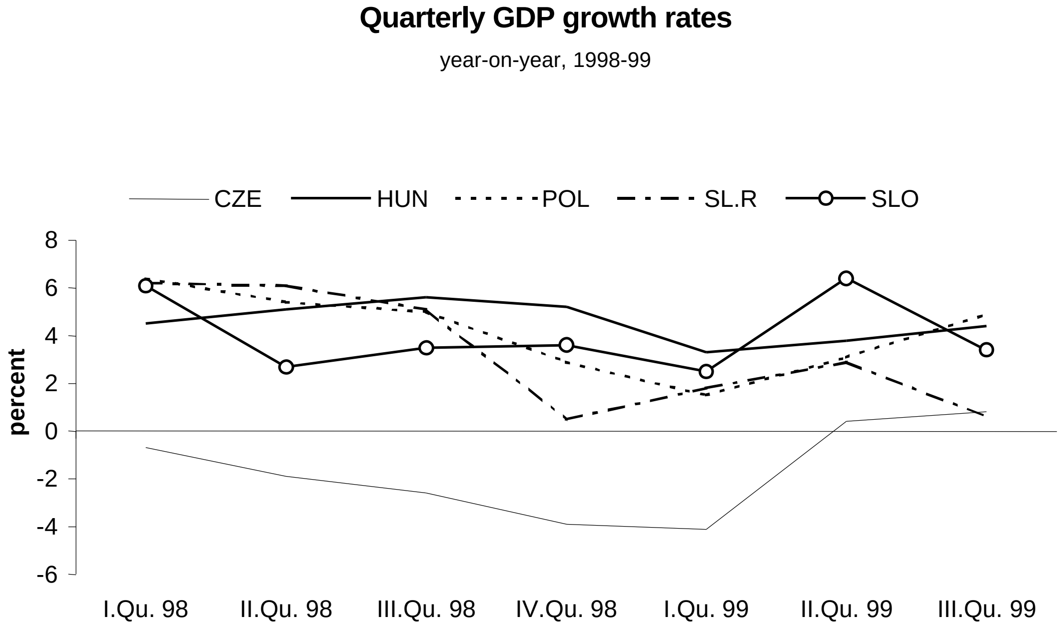
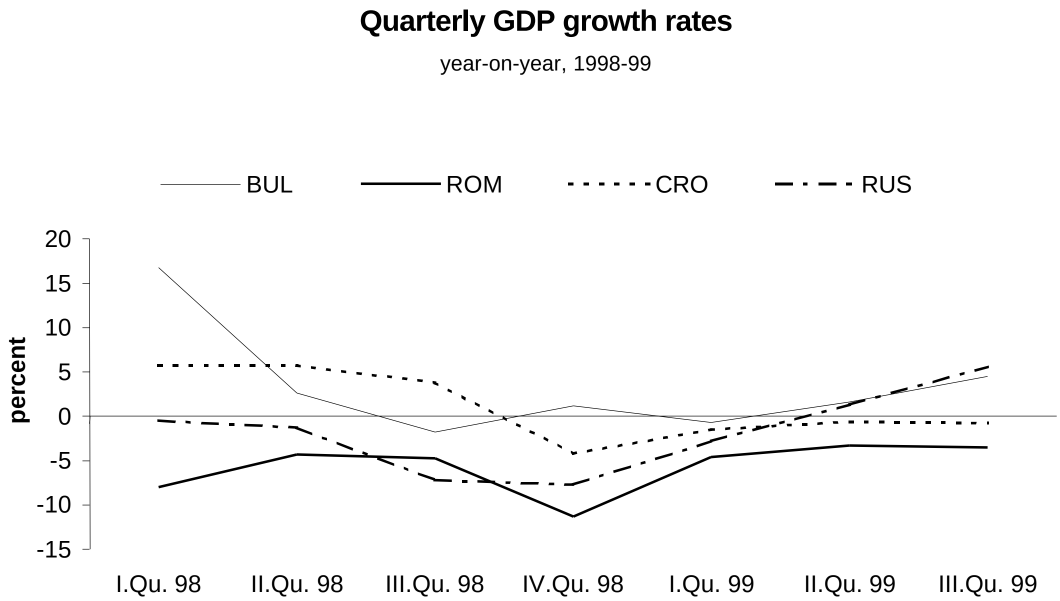


Figure 3b



Upswing from markedly different starting points

Exactly one year ago, GDP growth rates were seen to tumble in transition countries. Today, we realize that the trend was just bottoming out at the time. In the second quarter of 1999, **growth performance started to improve.**

Quarterly growth data (Figure 3, p. 2) show that the **slump in late 1998 or early 1999** was quite general in nature. Nevertheless, the **contrast** between individual countries was **striking**. On the one hand, Hungary's economy achieved considerable growth even during the overall slump: 3.3% year-on-year in the first quarter of 1999. Slovenia's growth rate also remained quite substantial: 2.5%. On the other hand, Romania experienced a major drop in its GDP, no less than -11.3% in the fourth quarter of 1998. The same held true for Russia, whose GDP dropped by 7.7% in the same quarter. The remaining countries ranged between these two extremes: Bulgaria (with a growth rate of -0.7% in the first quarter of 1999), Croatia (-4.2% in the last quarter of 1998), Czech Republic (-4.1% in the last quarter of 1998), Poland (1.5% in the first quarter of 1999) and Slovakia (0.5% in the fourth quarter of 1998)[3]. Recession in the Baltic States also bottomed out deep down in the negative zone. In the first quarter of 1999, they recorded extremely negative growth rates: Lithuania -5.8%, Estonia -5.6% and Latvia -2.3%.

Data for the second quarter of 1999 show signs of the business climate improving in all countries. **GDP growth accelerated** in Hungary, Poland, Slovakia and Slovenia; it **recovered at least slightly** in Bulgaria, the Czech Republic and Russia, while **GDP shrinkage diminished** in Croatia and Romania, as well as in the three Baltic States.

As can be seen in Figure 3 (p. 2) the growth pattern in the countries mentioned above is U-shaped. The vertical co-ordinates of each country's U, especially its lowest point, are indicative of the country's relative **resistance/proneness to recession tendencies**. In some cases, that particular low point was still in the positive zone, thus indicating that growth had not stopped. In others, however, it is to be found in the negative zone, thus indicating a decline in GDP. A high degree of resistance may be positively correlated with the progress towards transition that the country has actually achieved. On that basis, of the countries mentioned above, Hungary has been the most successful transition country and Romania the least successful over the period observed.

This simple attempt to **measure the degree of transitional success** should have some measure of validity; however, as with all things simple, a large dose of **caveats** is called for. The relatively good or bad growth performance that individual countries have recently displayed is also partly the result of influences that have no bearing on the outcome of the

[3] For Ukraine, quarterly GDP data were not available.

Figure 4a

Industrial production, 1998-99

annual change in %

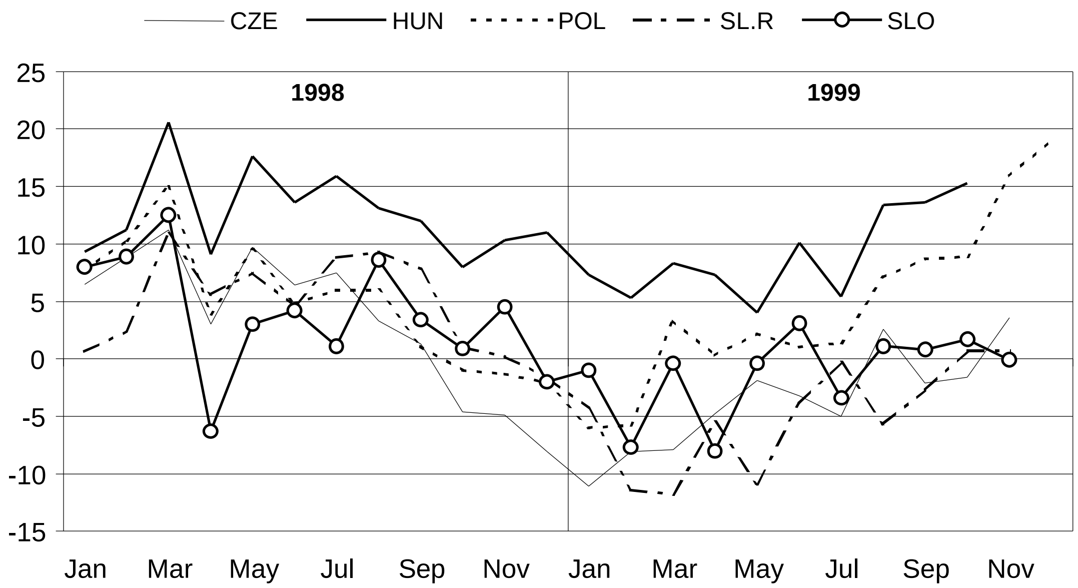
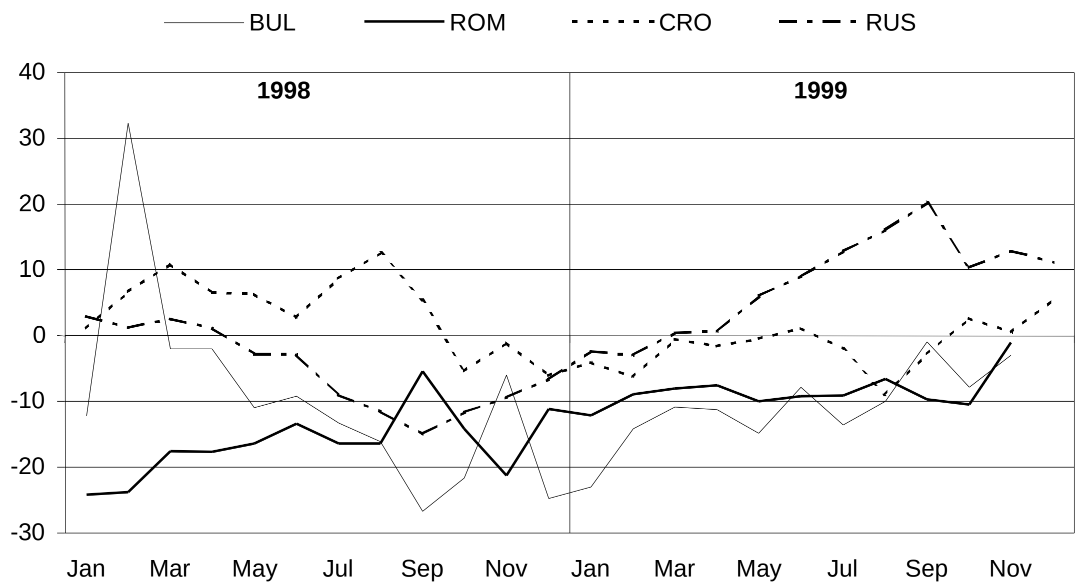


Figure 4b

Industrial production, 1998-99

annual change in %



transition process. For example, the massive devaluation of the rouble associated with the financial crisis in Russia in August 1998 brought about a drastic reduction in the exports of the Baltic States as well as an appreciable drop in Poland's exports. Under these circumstances, these countries' progress towards transition may well be more successful than the graph would indicate. On the other hand, Bulgaria's relatively good growth results are not rooted in the soundness of the corporate sector, but in the fresh loans provided by international financial institutions. Something similar also holds true for Slovakia whose previous annual GDP growth rates ranging between five and seven per cent have to be viewed in the context of massive borrowing from abroad. The loans were used to fund ambitious public infrastructure projects, but they were not matched by adequate structural change. When this policy was ultimately dropped, it was only thanks to a major currency devaluation that the growth rate did not plummet below zero. Moreover, when all is said and done, the curve for Russia fails to portray the country's extreme lack of success in terms of its transition over the past decade.

Slovenia is also a special case in this context. Its growth rates have hovered around 4% in recent years. The figures were thus considerably lower than in Poland or Slovakia, yet they represented stable growth of per capita incomes that was already quite high, be it measured in terms of current exchange rates or purchasing power parities (PPPs). In this sense, Slovenia can be regarded as the most-developed transition country, even though its curve in Figure 3 (p. 2) is no higher than all the others.

Upswing in industrial output

If taken alone, two quarters with improved GDP growth rates cannot be deemed firm evidence of an ongoing upswing. However, monthly data for year-on-year growth rates of industrial output, as portrayed in Figure 4 (p. 4), reveal a tendency that is quite similar: a **downswing in 1998 and an upswing in 1999** in all CEECs plus Russia.[4] The facts confirm the very specific position held by Hungary. It was the only country, which did not slip into negative output growth. Once again, it was Romania at the other extreme; its growth rate of industrial output never showed as positive in either 1998 or 1999. Towards the end of 1999, most of the countries had more or less re-attained the same level of production that they had displayed one year before. Only Hungary, Poland and Russia recorded industrial growth – moreover, at quite high rates.

In all transition countries, **labour productivity growth rates** in industry (Figure 5, p. 6) revealed a similar pattern of behaviour: **In the course of 1998** they first **declined and then turned negative, only to start recovering in 1999**. Here again, Hungary was the

[4] The selection of countries has been determined by the availability of data.

Figure 5a

Labour productivity in industry, 1998-99

annual change in %

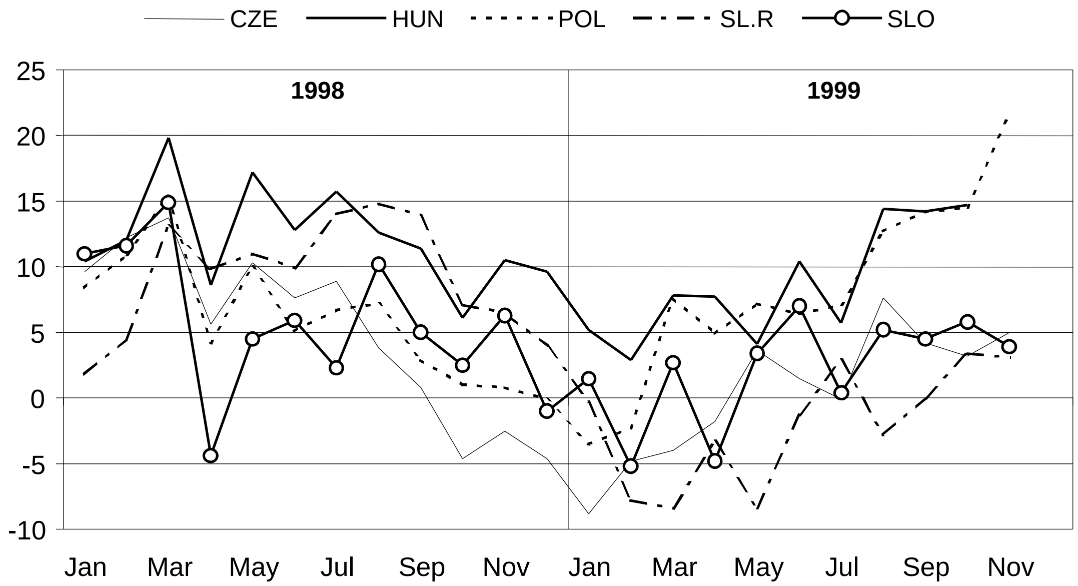
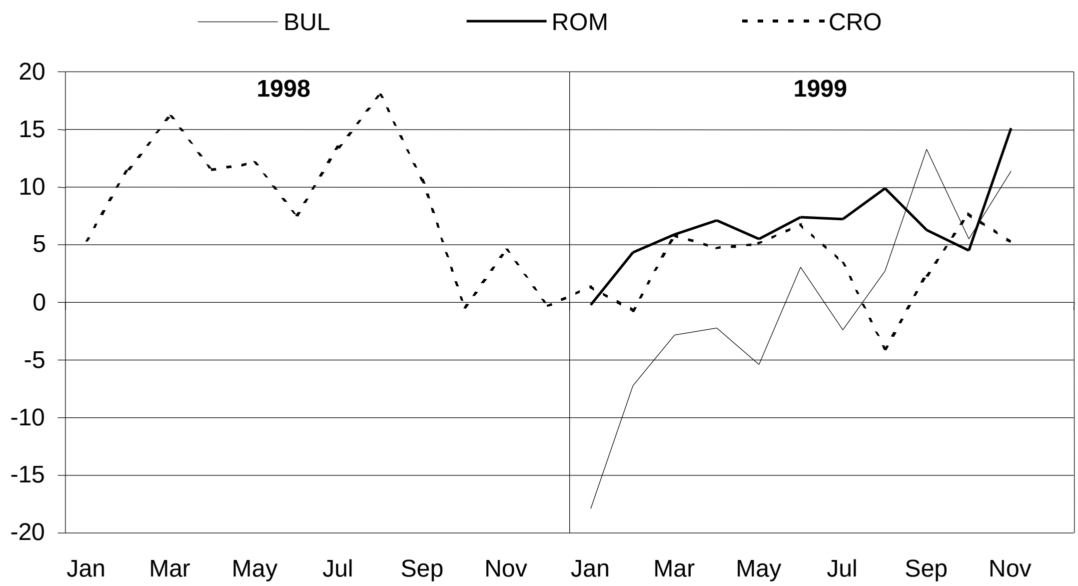


Figure 5b

Labour productivity in industry, 1998-99

annual change in %



only country to avoid stagnation or a negative growth rate of labour productivity. The marked downward trend in labour productivity, a customary symptom of a major recession, was more the result of less decline in employment than in output. Quite remarkable was the development in Romania: despite a continuous decline in industrial production, labour productivity increased appreciably throughout 1999. This points to strong structural changes and is consistent with the reported closure or streamlining of loss-making companies which also displayed low levels of labour productivity.

Unit labour costs in euro terms (Figure 7, p. 8) rose in most of the countries during the slump. This was especially true of the Czech Republic and Bulgaria where, however, the increase stopped once the subsequent upswing made itself felt.

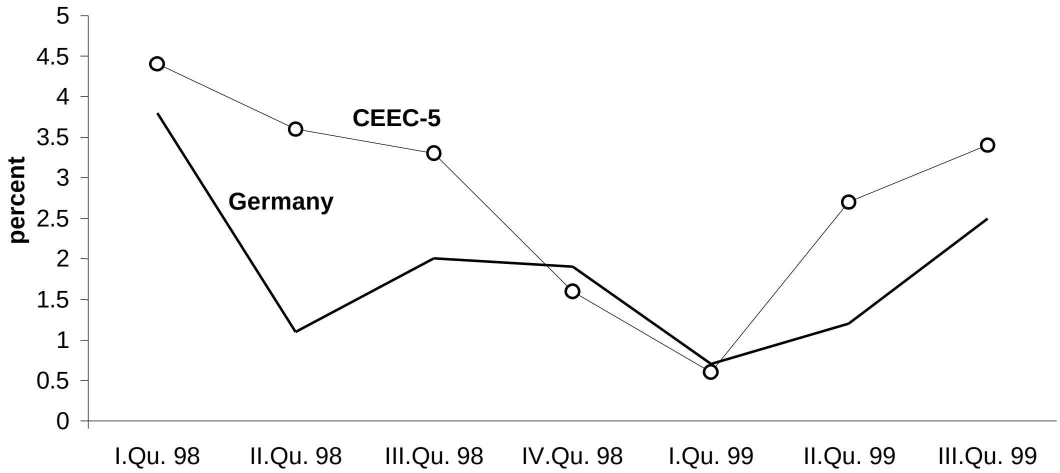
First down, then up: Western and Eastern Europe swing in parallel

A slow-down in growth in 1998 and recovery in 1999 was to be observed not only in the transition countries, but also in the major EU economies. This may have been the outcome of forces influencing economic developments on both sides of the Continent simultaneously, but to some degree it may also be that trends in the West had an impact on growth in the East. The prime source of such influence is Germany, the most important trading partner for the CEECs. Figure 6 (p. 7) compares German growth rates with aggregated growth rates in the CEEC-5 (Czech Republic, Hungary, Poland, Slovakia and Slovenia).[5] The similarity in the time paths is striking.

Figure 6

CEEC-5 and Germany: Average quarterly GDP growth rates

year-on-year, 1998-99



Source: WIIW; Statistisches Bundesamt Wiesbaden; *Financial Times*, 21 January 2000, p. 2.

5 The growth rate of the CEEC-5 is a weighted average.

Figure 7a

Unit labour costs, exchange rate (EUR) adjusted

annual change in %

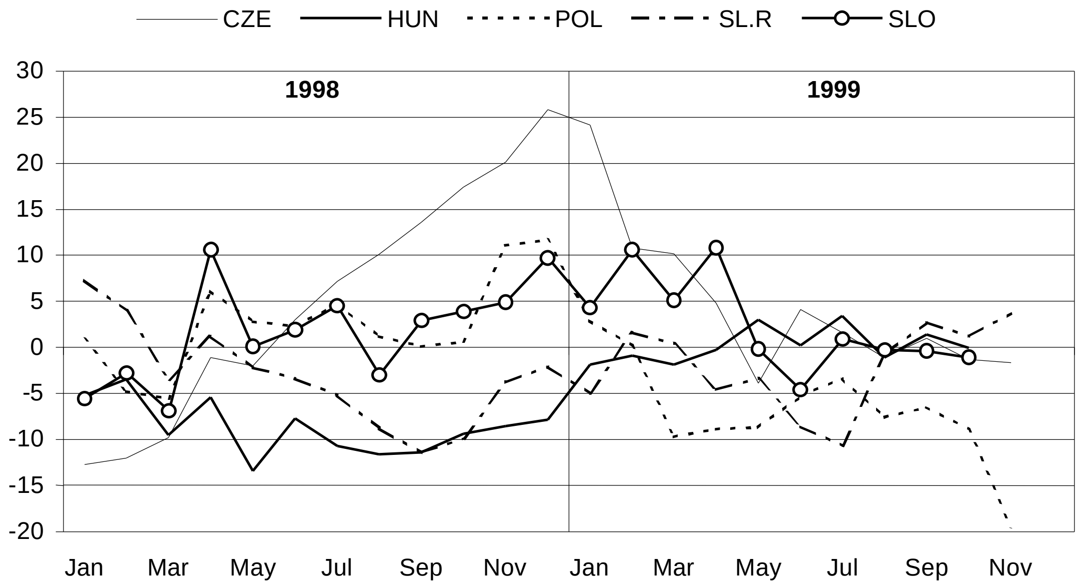
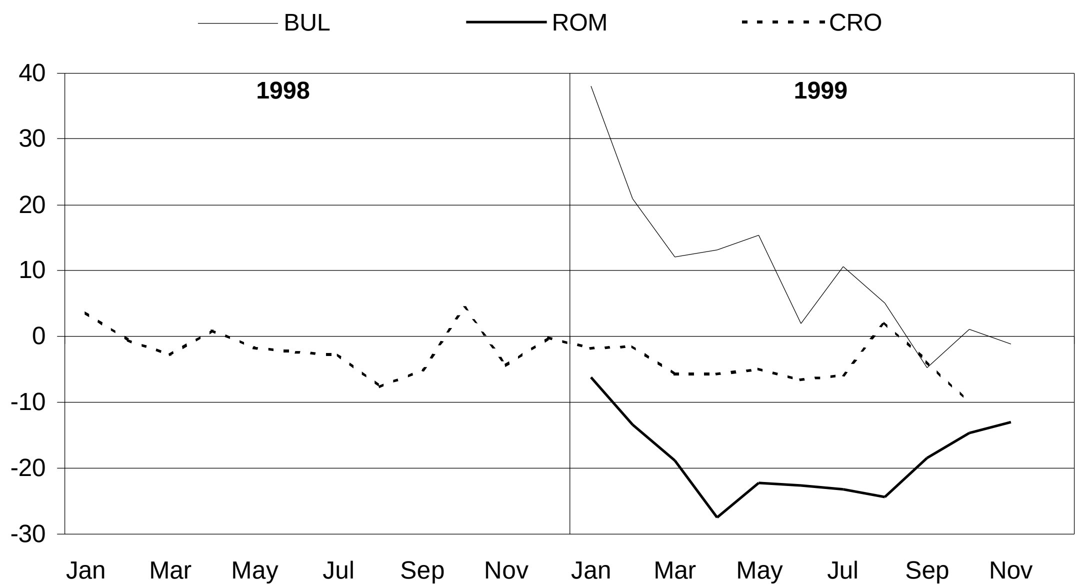


Figure 7b

Unit labour costs, exchange rate (EUR) adjusted

annual change in %



In the course of 1998, Germany's quarterly growth rates dropped. The rate fell below 1% in the first quarter of 1999. In that phase of near-stagnation, import absorption was probably weaker than during the period of recovery thereafter.[6] The business climate started to improve in the second quarter of 1999. Forecasts for 2000 predict comparatively strong growth for Germany and other EU countries. This will make it easier for the CEECs to export to the West.

Trade with the countries of Central and Eastern Europe still accounts for only a small fraction of total exports and imports in the EU. This indicates a potential for future trade expansion. This also holds true for Germany. For the CEEC-7, however, foreign trade with the EU, especially Germany, has already become very important.[7] In 1999, Germany absorbed between 36% and 42% of all Czech, Hungarian and Polish exports and between 28% and 32% of all Slovak and Slovene exports (see Table 9, p. 26).

Real depreciation or appreciation of CEEC currencies has most probably had an influence on foreign trade in those countries, thus strengthening or dampening the impact of the business cycle in Western Europe, especially in Germany. Real exchange rate figures, derived from DEM exchange rates and producer price indices, indicate whether domestic industrial products have become **costlier or cheaper compared to Germany**.[8] In Figure 8 (p. 10) every point on a curve located above the base line of 100 indicates real depreciation as compared to January 1998; those instances where the curve has a positive slope indicate real depreciation as against the previous month. The resultant picture is not uniform. Up to October 1998, Hungary's currency depreciated, a fact that may have had a positive impact on its exports and GDP growth.[9] In Poland and Slovenia, the changes remained within a rather narrow band. In the Czech case, marked real appreciation exacerbated recession tendencies in the second half of 1998, but less so in the second quarter of 1999. Slovakia switched to the depreciation mode in the second half of 1998 and reached its peak value in May 1999 – with more than 15% real devaluation compared to January 1998. This gradual real depreciation may be one of the prime reasons for the slow-down in Slovak growth turning out to be less severe than had been commonly

[6] Hungary suffered less than other countries from low growth in Western Europe; exporters – frequently large multinational companies – may have strengthened their market position.

[7] A press release issued by the Statistisches Bundesamt in Wiesbaden on 25 January 2000 states that Germany's foreign trade with all 13 candidate countries for EU membership has expanded rapidly in recent years. In addition to the CEEC-7, the candidate countries comprise the Baltic States, Cyprus, Malta and Turkey. Both imports and exports have more than doubled from 1993 to 1998. In 1998, imports from that group of countries represented 9% of the Germany's total imports and 10% of its total exports. The region's biggest exporter to Germany was the Czech Republic, whereas the biggest importer of German goods was Poland. As is customary with foreign trade statistics, the data can differ considerably from source to source in the various partner countries.

[8] Real appreciation makes domestic goods costlier compared to the reference country, real depreciation has the contrary effect.

[9] Despite the fact that this trend was gradually reversed in the months thereafter.

Figure 8a

Real exchange rates, 1998-99

national currency per 1 DEM deflated with PPI, Jan 1998 = 100

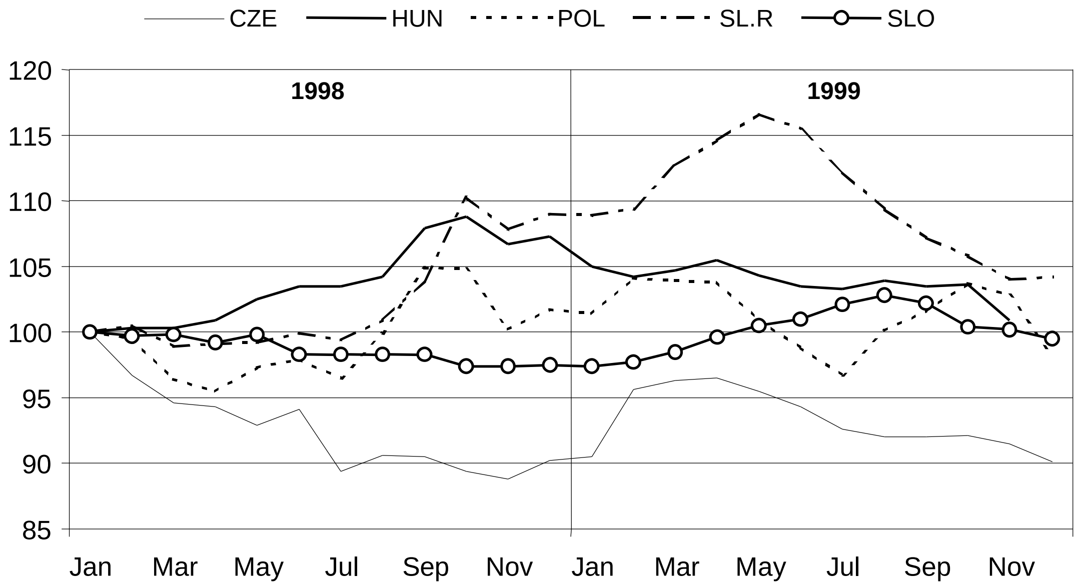
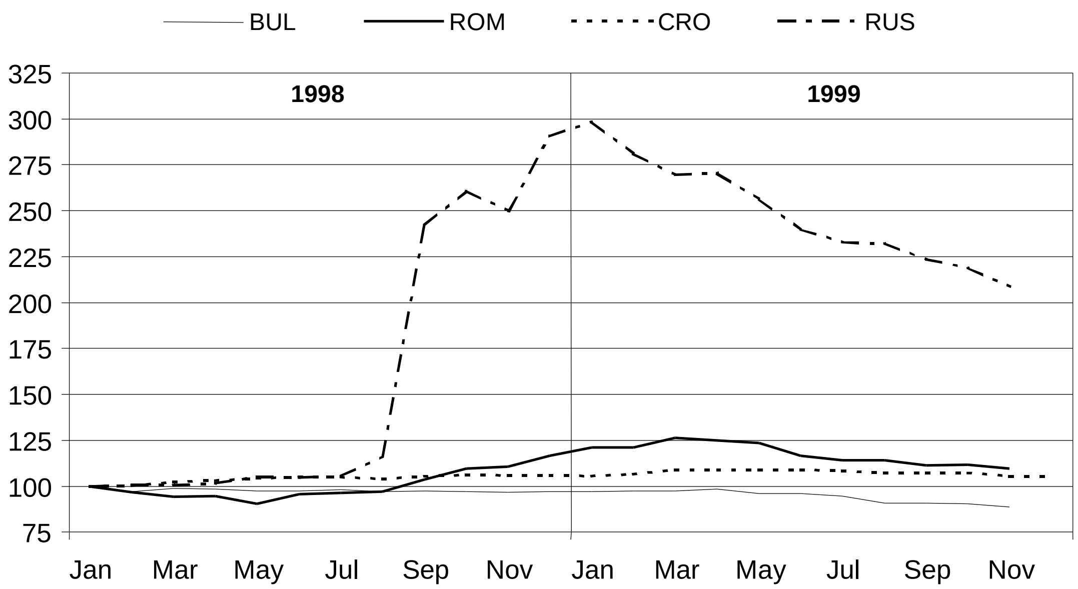


Figure 8b

Real exchange rates, 1998-99

national currency per 1 DEM deflated with PPI, Jan 1998 = 100



expected. Something similar also occurred in Romania, but it failed to prevent a decline in GDP. The most extreme instance of real depreciation came about in Russia: in January 1999 200% over the same month of the previous year.[10] This explains why the financial collapse had a comparatively positive impact on GDP growth in 1999 and it will probably also continue to do so in 2000. In the future, Russian inflation, which is still high, could gradually gobble up the favourable price gap vis-à-vis Western countries and most other transition countries. Since February 1999, Russia has re-entered the appreciation mode.

Changes in real interest rates are another potential factor affecting the business cycle. Figure 9 (p. 12), which shows PPI-deflated central bank rates, points to major variances in patterns. In most of the countries considered, real interest rates went up in the course of 1998 and were relatively high during the slump period. For example, in Hungary in January 1999 the real interest rate reached its peak level (about 12%). Nevertheless, thanks to the successful export activities of foreign-investment enterprises the downswing was not very pronounced. Apart from Russia, Poland was the exception. In November 1998 the real interest rate, which had stood at 14% for most of the year, started dropping down to around 8% in October 1999. This helped to dampen the downswing, mainly because it triggered off an expansion in consumer credits.[11] Reversal followed in November 1999. Real interest rates in the Czech Republic and Slovakia reached historically low levels in the second half of last year. In Russia, the decline in real interest rates has been most remarkable, down from over 100% annually. Figure 9 (p. 12) indicates negative real interest rates for the period after May 1999. Their computation reflects the massive leap in inflation that occurred immediately after the crisis; it does not reflect the present more moderate pace of inflation. In both Russia and Romania, it is difficult to say what the expected real interest rate might be now.

The longer-term view: no-growth, low-growth and high-growth countries in transition

On looking at GDP growth rates throughout the whole transition period (see Table 2, p. 18), only **three countries give the impression of having been relatively successful**. Poland enjoyed an early start and subsequently high rates of growth. Hungary entered the high growth phase at a very late juncture, but growth proved quite resilient and resistant to the general recession in 1998-9. For many years, Slovenia's growth has been in the range of 3.5 and 5.3% and gives every impression of being sustainable. As shown above, these three countries managed to maintain higher growth rates than the others, even during the recent recession.

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[10] The exchange rate RUB/DEM was 3.31 in January 1998, but 13.21 one year later. In the same period Russian producer prices increased by 30.5%, whereas German producer prices dropped 2.4%.

[11] To illustrate this, the CPI-deflated real exchange rate would be the appropriate variable. However, the results of both approaches do not differ fundamentally.

Figure 9a

Minimum real interest rates

NB leading rate deflated with annual PPI, in % p.a

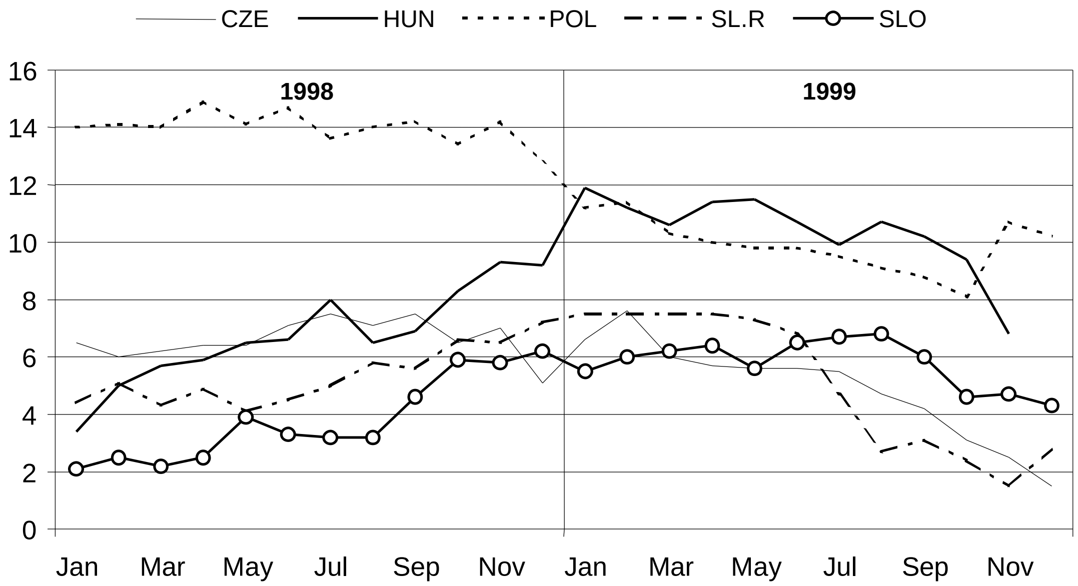
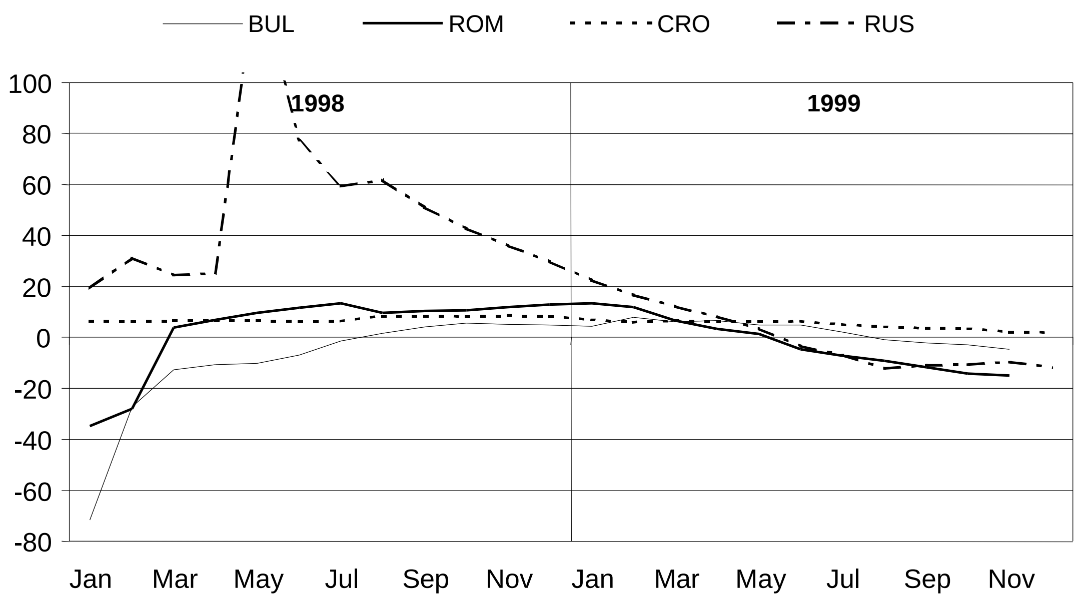


Figure 9b

Minimum real interest rates

NB leading rate deflated with annual PPI, in % p.a



Other economies **started growing substantially at some point of time, only to experience severe setbacks later**. In the latter group, the Czech Republic enjoyed 5.9% growth in 1995, but a 2.3% drop in 1998. Romania's economy grew by 7.1% in 1995, but shrank by 6.9% two years later. Bulgaria achieved 2.9% growth in 1995, only to be followed by a decline of 10.1% in GDP the year thereafter.

Slovakia lies between these two groups. For five years, it recorded growth rates between 4.4% and 6.9%. In 1999, however, this growth no longer proved sustainable and the growth rate fell drastically; none the less, it remained positive. A similar situation has also transpired in the case of Croatia. Judged simply on its GDP growth rates, Croatia would also seem to belong to the first group. Here again, however, the initial high growth rate did not prove sustainable.

A third group **never achieved high growth – or attained no growth at all –** throughout the transition decade. The Ukrainian economy never even started growing. Russia achieved an insignificant positive growth rate in 1997, followed by a steep decline in 1998. The Russian crisis in summer 1998 had a strong negative impact on the growth of many economies in the region, once the latter were closely linked to Russia through foreign trade. The crisis catapulted some of them into the group of countries that had started growing significantly, yet failed to maintain the pace. Whereas the Baltic States had enjoyed growth rates between 7.3% and 10.6% in 1997, they had to face a reduction in growth in 1998, followed by a decline in 1999. Belarus, Georgia and Kyrgyzstan also recorded high growth rates in 1997, which then more or less disappeared in the period 1998-99.

Reasons for permanent or re-emergent transition-related recession

Only a few transition countries in Central and Eastern Europe have thus achieved and sustained significant economic growth. The question arises why all the others had trouble in initiating the process or maintaining it once started? For an answer, one should probably look **at the enterprise level, the domain where most GDP is produced**. Each of the countries embarked on the transition process with a stock of technologically obsolete or obsolescent enterprises. Their backwardness encompassed deficiencies in many fields such as market-orientation and sales networks, technical equipment, logistics and process design, as well as financial instruments. The high levels of average education notwithstanding, the skills of the economically active population deviated widely from the requirements of a developed market economy. In each transition country, some of the deficiencies persist: in some of them massively, in others much less so.

Figure 10a

Consumer price inflation, 1999

monthly changes in %

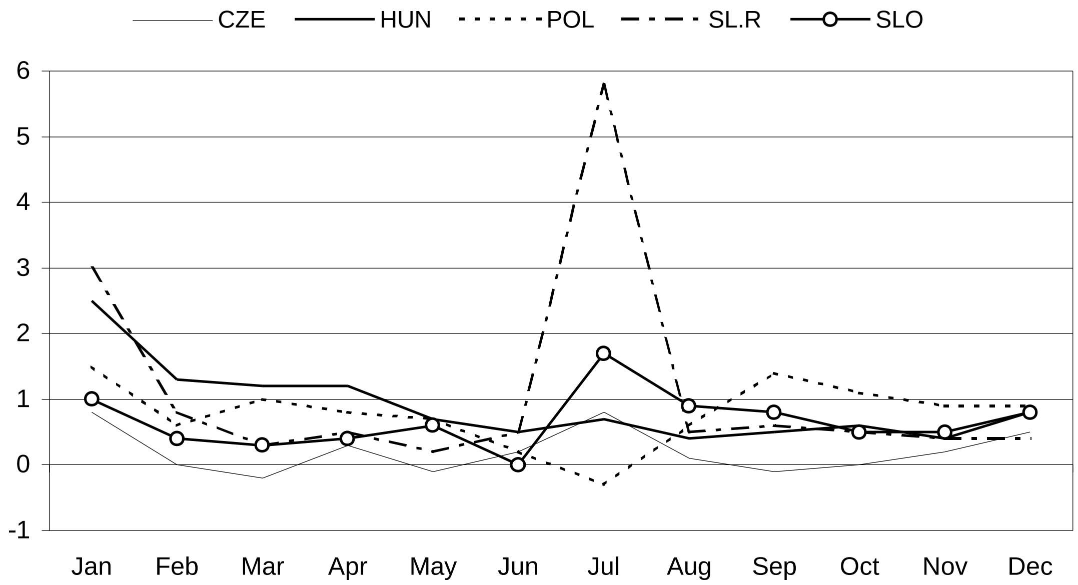
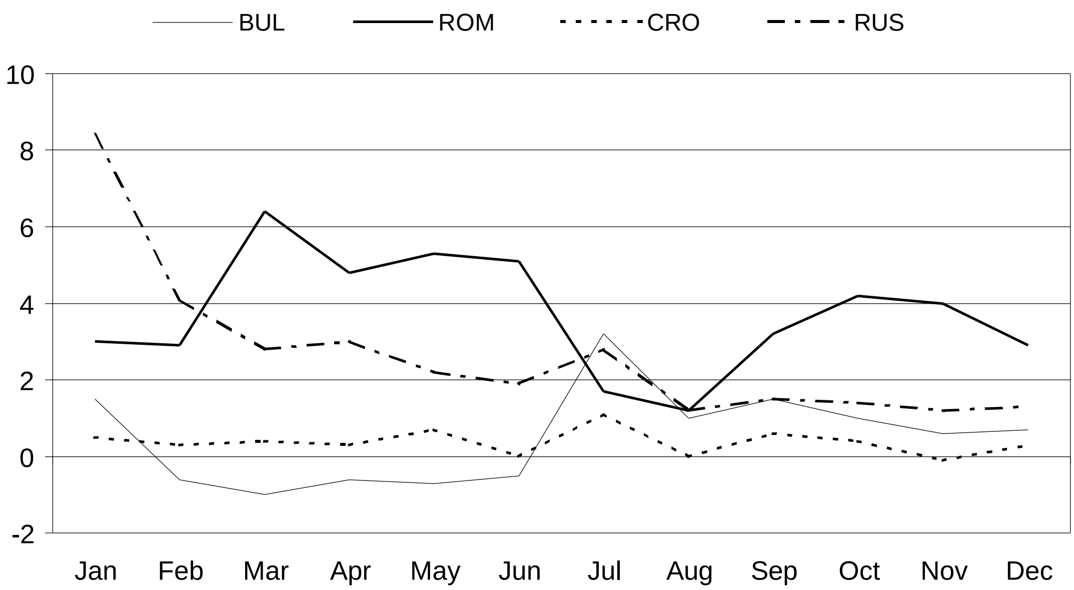


Figure 10b

Consumer price inflation, 1999

monthly changes in %



Transition has also provoked some degree of social resistance. Previously, people learnt to survive under a command economy by circumventing part of its rules. They created firm informal structures and practised a specific form of pragmatism that, in the ultimate analysis, kept the economy going. For individuals, these techniques represented intangible assets. The representatives of the official system accepted the situation and tried to make the best of it for themselves. At the very moment when the initial transition shock changed the whole set of formal rules in one stroke, people saw their intangible assets endangered and embarked on a process of trial and error to test the stringency or 'pliability' of the new rules. In countries where market experience was almost completely lacking, people lacked the time or willingness to acquaint themselves with the new set of rules that had been proclaimed. The economy might have collapsed immediately, had not established informal structures helped, once again, to keep things running. Since that initial phase, the 'rule of law' has never come into being in some countries: a fact that makes doing business there a risky proposition. Segments of the informal networks have since collapsed or been usurped by mafia-like business operations.

Successful transition hinges upon obtaining good results in three discrete processes: a short-term process of **making better use of existing capacities** and two longer-term processes involving the **gradual elimination of obsolete capacities** and the more or less simultaneous **creation of new capacities**, with market forces acting as the driving force in all three processes. In respect of all three, achieving success proved equally difficult, depending as it did on the quality of the new rules and institutions established at the onset of transition, their subsequent reinforcement and society's acceptance of reform[12]. Under the specific conditions prevailing in some countries, making better use of existing capacities has been slow and insufficient in its development. Whereas this has helped to keep employment levels high for the time being, it has also exacerbated the ever-increasing problems posed by unprofitable enterprises, including all the adverse implications they bear for internal financial structures. Among the more developed transition economies, the Czech Republic offers a good example in this respect; most of the major enterprises' efforts to restructure were neither swift nor radical enough. Where efforts to create new capacities were wanting, unemployment was simply boosted by the inevitable ultimate need to shut down obsolete capacities (Table 1, p. 17). This has been the case, and still is in some instances, in almost all transition countries; Bulgaria, however, can be cited as a prime example.

Companies capable of replacing obsolete equipment and increasing capacity are destined to become part of their country's industrial backbone. No matter in which field they are

12 Those capacities which became obsolete did so because of market processes, although government policy also played a role in the matter. At the one extreme, it could provoke the elimination of otherwise still useful capacities, on the other hand it could keep even moribund companies alive.

Figure 11a

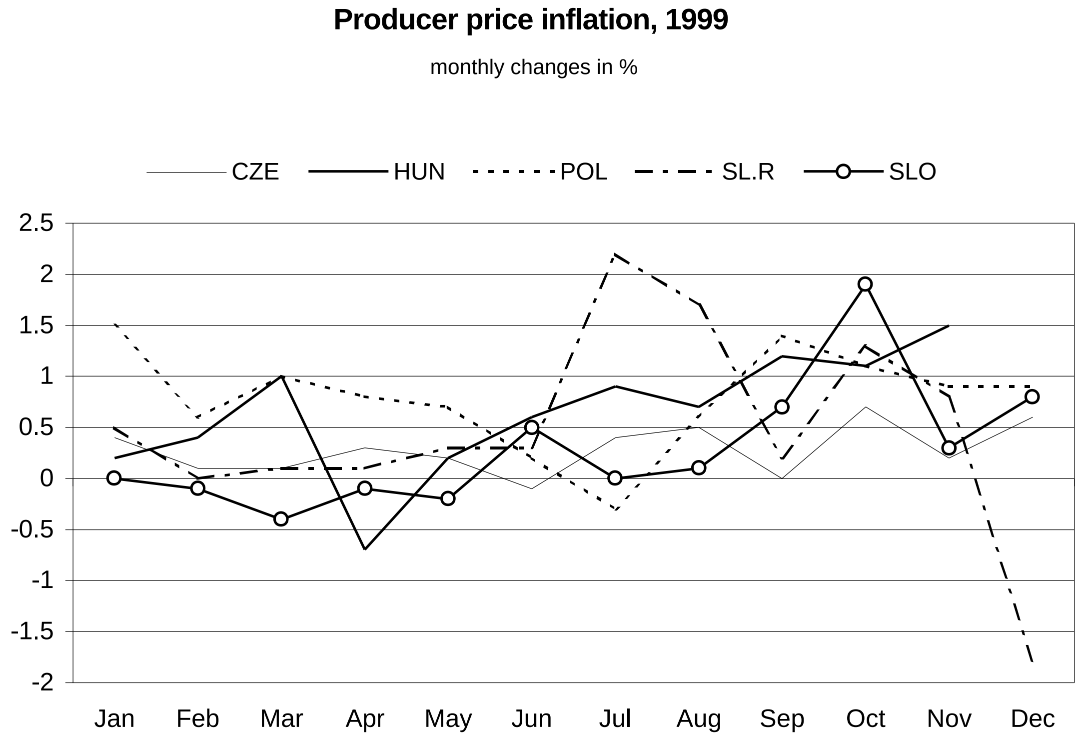
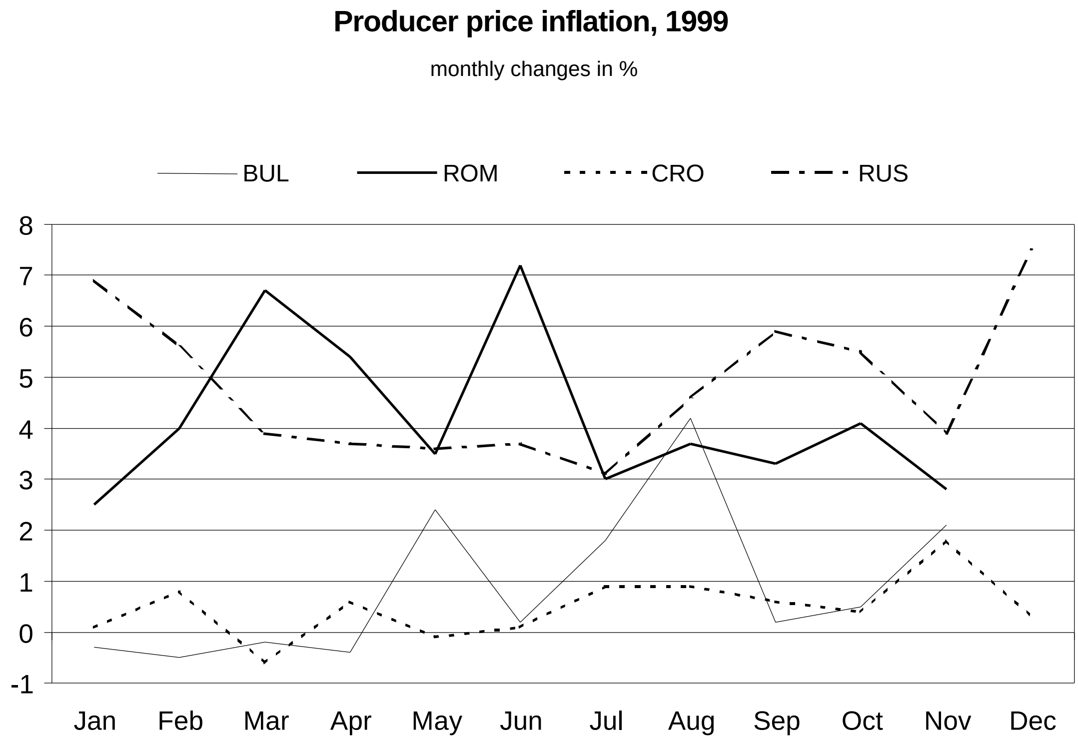


Figure 11b



active, be it manufacturing or services, they should become efficient by international standards.[13] This process leads to industrial specialization. Institutions, policies and regulations can either help or hinder this process. As experience shows, the decisive factor was not so much the mere installation and existence of certain institutions and policies as such, but the manner in which they had been designed and implemented. If well designed, privatization helped to build up an industrial backbone; if badly designed or implemented, it made no such contribution. Other instruments such as a currency board regime or the liberalization of capital markets should also be **assessed according to their contribution to the evolution of an industrial backbone**.

Table 1

Registered unemployment, end of period

	in 1000 persons				rate in % [1)]						
	1996	**1997**	**1998**	**1999 Sept.**	**1996**	**1997**	**1998**	**1999 Sept.**	**1999 est.**	**2000 forecast**	**2001 forecast**
Czech Rep.	186.3	268.9	386.9	469.8	3.5	5.2	7.5	9.0	9.4	11	12
Hungary	477.5	464.0	404.1	397.2	11.4	11.0	9.6	9.4	9.6	9	9
Poland	2359.5	1826.4	1831.4	2177.8	13.2	10.3	10.4	12.1	13	12.5	12
Slovak Rep.	329.7	347.8	428.2	497.5	12.8	12.5	15.6	17.8	19.2	19	18
Slovenia	124.5	128.6	126.6	115.3	14.4	14.8	14.6	13.1	13	12	12
CEEC-5 [2)]	3477.5	3035.6	3177.2	3657.6	11.3	9.9	10.4	11.8	.	.	.
Bulgaria	478.5	523.5	465.2	542.8	12.5	13.7	12.2	14.2	16	17	16
Romania	657.6	881.4	1025.1	1073.6	6.6	8.9	10.3	10.9	12	13	12
CEEC-7 [2)]	4613.6	4440.5	4667.5	5274.0	10.3	10.0	10.5	11.8	.	.	.
Croatia	269.3	287.1	302.7	326.5	15.9	17.6	18.6	19.6	20.8	21	22
Macedonia	245.1	257.7	.	.	39.6	42.1	34.5 [3)]	.	32.4 [3)]	32 [3)]	32 [3)]
Yugoslavia	826.8	793.8	849.4	777.0	26.1	25.5	27.2	25.5	32	35	35
Russia [3)]	7280	8133	9728	8650	9.9	11.2	13.3	11.7	12	12	12
Ukraine	351.1	637.1	1003.2	1124.1	1.3	2.3	3.7	4.1	5	6	8

Notes: 1) Share of unemployed in % of economically active persons. – 2) WIIW estimate. – 3) According to ILO definition.
Source: WIIW Database incorporating national statistics, forecast: WIIW.

The installation of the **institutions** typical for developed economies has proved to be a necessary, but insufficient condition for establishing standard business relations. In some cases, the institutional infrastructure was inappropriate; efficiency was thus low. For example, the creation of stock exchange markets was supposed to open up the way for companies to secure **equity financing for investment projects**, but somehow it failed. Likewise, the introduction of a two-tier banking system did not **channel liquidity** into the creation of new capacities, but rather into the accounts of loss-making companies. Thus,

13 In the case of non-tradables, a somewhat slower adjustment to international standards may help to keep unemployment manageable.

Table 2

Gross domestic product

real change in % against preceding year

	1992	1993	1994	1995	1996	1997	1998 [1)]	1988 Jan-Sept	1999 Jan-Sept	1999 est.	2000 forecast	2001 forecast	Index 1990=100 1999	Index 1995=100 1999
Czech Rep.	-0.5	0.1	2.2	5.9	3.8	0.3	-2.3	-1.8	-0.9	-0.6	1.5	2	96.3	101.1
Hungary	-3.1	-0.6	2.9	1.5	1.3	4.6	4.9	5.1	3.9	4.0	4.5	5	102.4	115.6
Poland	2.6	3.8	5.2	7.0	6.0	6.8	4.8	5.6	3.1	4.1	4.5	5	137.6	123.5
Slovak Rep.	-6.5	-3.7	4.9	6.9	6.6	6.5	4.4	5.8	1.8	2.0	0.0	2	104.3	120.9
Slovenia	-5.5	2.8	5.3	4.1	3.5	4.6	3.9	4.1	4.1	3.7	3.7	4	113.3	116.6
CEEC-5 [2)]	-0.2	1.5	4.1	5.7	4.6	4.8	3.1	3.7	2.3	2.8	3.4	4.0	117.0	116.2
Bulgaria	-7.3	-1.5	1.8	2.9	-10.1	-7.0	3.5	4.4	2.0	2.5	4	4	74.9	88.7
Romania	-8.8	1.5	3.9	7.1	3.9	-6.9	-5.4	.	-3.8	-3.9	0	1	79.0	88.0
CEEC-7 [2)]	-2.3	1.4	3.9	5.8	3.7	1.8	1.4	.	1.0	1.5	2.8	3.4	106.0	108.7
Croatia	-11.7	-8.0	5.9	6.8	6.0	6.5	2.5	5.0	-1.0	-2.0	1	2	82.2	113.4
Macedonia	-8.2	-1.2	-1.8	-1.1	1.2	1.5	2.9	.	.	2.7	3	5	92.5	108.5
Yugoslavia [3)]	-27.9	-30.8	2.5	6.1	5.9	7.4	2.5	.	.	-19.3	3	3	45.1	94.1
Russia	-14.5	-8.7	-12.7	-4.1	-3.4	0.9	-4.6	-3.0	1.5	1.7	2	3	58.7	94.6
Ukraine	-9.9	-14.2	-22.9	-12.2	-10.0	-3.0	-1.7	-0.5	-1.7	-0.4	1	3	40.8	85.4
Estonia	-14.2	-8.5	-2.0	4.2	3.9	10.6	4.0	5.8	-0.5	.	.	.	85.8	118.9
Latvia	-34.8	-15.0	0.8	-1.0	3.3	8.7	3.5	5.6	-1.3	.	.	.	56.8	114.7
Lithuania	-21.3	-16.2	-9.8	3.3	4.6	7.3	5.1	7.1	-4.9	.	.	.	65.0	112.2
Armenia	-41.8	-8.8	5.4	6.9	5.9	3.3	7.2	6.9	6.1	.	.	.	65.3	123.6
Azerbaijan	-22.6	-23.1	-19.7	-11.8	1.3	5.8	10.0	8.5	6.9	.	.	.	52.8	126.1
Belarus	-9.6	-7.6	-12.6	-10.4	2.8	11.4	8.3	10.0	2.0	.	.	.	81.8	126.5
Georgia	-44.9	-29.3	-10.4	2.6	11.2	11.3	2.9	7.3	2.4	.	.	.	36.8	130.4
Kazakhstan	-5.3	-9.2	-12.6	-8.2	0.5	1.7	-2.5	0.0	0.3	.	.	.	61.4	100.0
Kyrgyzstan	-13.9	-15.5	-20.1	-5.4	7.1	9.9	1.8	1.4	3.5	.	.	.	63.2	124.7
Moldova	-29.0	-1.2	-30.9	-1.9	-5.9	1.6	-8.6	-7.3	.	.	.	.	32.5	82.8
Tajikistan	.	-16.3	-21.3	-12.4	-16.7	1.7	5.3	6.5	0.9	.	.	.	51.0 [4)]	88.4
Turkmenistan	.	1.5	-16.7	-7.7	0.1	.	.	.	.	.	.	.	.	.
Uzbekistan	-11.1	-2.3	-5.2	-0.9	1.7	5.2	4.4	4.4	4.4	.	.	.	94.7	116.6
CIS	-13.9	-9.7	-14.2	-5.3	-3.3	1.0	-3.4	-1.7	.	.	.	.	.	.

Notes: 1) Preliminary. – 2) WIIW estimate. – 3) Based on GMP. – 4) 1992 = 100.

Source: WIIW Database incorporating national statistics, CIS Database, forecast: WIIW.

only those countries with high foreign direct investment (FDI) succeeded in their endeavours to create new capacity.[14] Otherwise, destruction prevailed over creation.

So far, three countries have been relatively **successful in attracting FDI**. By the end of 1999, Poland had accumulated a stock of USD 28 bn, Hungary USD 19.5 bn and the Czech Republic USD 17 bn. This stock represents a high proportion overall for Hungary, the smallest of the three countries in GDP terms, and a relatively low proportion for Poland, which produces about half of the total GDP in the CEEC-5 (for an international GDP comparison, see Table 3). The catching-up process of attracting FDI has been most

Table 3

GDP: International comparison, year 1999

	GDP at ER	GDP at PPP	GDP per capita EU-15 = 100 at PPP	GDP real 1990=100
	USD mn			
Czech Republic	53515	137482	63	96.3
Hungary	48896	114032	53	102.4
Poland	154610	344505	42	137.2
Slovak Republic	18617	56206	49	104.3
Slovenia	19640	31111	73	113.3
CEEC-5	295278	683336	48	116.9
Bulgaria	11982	42713	24	74.9
Romania	32598	132124	28	79.0
CEEC-7	339858	858173	41	105.9
Croatia	19691	31926	33	82.2
Macedonia	3273	9284	21	92.5
Russia	182778	994501	32	58.7
Ukraine	30825	167763	16	40.8
CEEC-10	576425	2061647	32	72.7
EU-15	8532935	7997763	100	117.8
Germany	2130020	1882292	106	126.1
Austria	211297	193827	113	121.1
Greece	125588	151794	69	120.6
Portugal	109029	150650	72	124.9
Spain	595153	654204	80	122.4
USA	9221794	8140090	143	132.3
Japan	4366913	3225656	120	112.8

Note: ER = Exchange rate, PPP = Purchasing power parity – see Annex.

Source: OECD, WIIW.

14 This is true despite the fact that most FDI initially represents acquisition of existing stocks rather than fixed investment in the GDP sense. Usually, the latter follows afterwards.

Table 4a

Foreign direct investment inflow

as recorded in the balance of payments, USD mn

	1992	1993	1994	1995	1996	1997	1998	1999 I-IX	1999 [1)]
Czech Republic	1004	654	869	2562	1428	1300	2720	3535	4000
Hungary	1471	2339	1147	4453	1983	2085	1935	1083	1500
Poland	.	1715	1875	3659	4498	4908	6365	5000 [1)]	6500
Slovak Republic	.	168	250	202	330	177	566	177	200
Slovenia	111	113	128	176	186	321	165	66	100
Total (5)	.	4988	4269	11052	8425	8791	11751	9861	12300
Bulgaria	42	40	105	90	109	505	401	465	700
Romania	77	94	341	419	263	1215	2031	691	1000
Total (7)	.	5122	4715	11561	8797	10511	14183	11017	14000
Estonia	82	162	215	202	151	267	581	231	300
Latvia	29	44	213	178	382	522	356	168 [2)]	300
Lithuania	10	31	31	73	152	355	926	306	500
Total (10)	.	5359	5174	12014	9482	11654	16046	11722	15100
Croatia	13	96	113	101	533	487	873	357	1300
Macedonia	.	0	19	9	11	16	118	21	0
Russia	.	1211	638	2016	2478	6639	2762	1977	2200
Ukraine	170	200	159	267	521	623	747	353	500
Total (14)	.	6867	6103	14407	13025	19419	20545	14430	19100

Table 4b

Foreign direct investment stock

as recorded in the balance of payments, USD mn

	1992	1993	1994	1995	1996	1997	1998	1999 Sept	1999 [1)]
Czech Republic	2889	3423	4547	7350	8572	9234	14375	15623	17000
Hungary	3435	5585	7095	11926	14668	15882	18255	19181	19500
Poland	1370	2307	3789	7843	11463	14587	22479	27000 [1)]	28000
Slovak Republic	.	459	770	1079	1379	1580	1938	1933	2000
Slovenia	.	954	1326	1759	2069	2297	2907	2950	3000
Total (5)	.	12728	17527	29956	38152	43579	59954	66687	69500
Bulgaria	101	141	247	337	446	951	1352	1818	1900
Romania	117	211	552	971	1234	2449	4480	5171	5400
Total (7)	.	13080	18325	31265	39832	46979	65786	73676	76800
Estonia	.	419	696	955	1026	1148	1822	2241	2300
Latvia	43	75	309	616	936	1272	1558	1682 [2)]	3900
Lithuania	20	153	310	352	700	1041	1625	1957	2100
Total (10)	.	13727	19640	33187	42494	50440	70791	79556	85100
Croatia	13	109	222	324	857	1344	2217	2631	3500
Macedonia	.	.	19	28	40	55	173	194	200
Russia	.	1211	1849	3865	6343	12982	15744	17721	17900
Ukraine	170	370	529	796	1317	1940	2687	3040	3200
Total (14)	.	15418	22260	38200	51051	66761	91612	103142	109900

Notes: 1) WIIW estimate. – 2) June.

Source: For Czech Republic, Hungary, Poland, Slovak Republic, Slovenia, Estonia, Latvia, Lithuania: the National Banks of the respective countries; for Bulgaria, Romania, Croatia, Macedonia, Russia, Ukraine: cumulated US dollar inflows based on Table 4a.

remarkable in the Czech Republic: Since 1997, the year the economic crisis broke out, the country has improved its position as an FDI target country beyond bounds. This proved feasible on account of the government having adopted a policy more kindly disposed towards FDI; it also shows that the market considers the country's present troubles transitory. At the end of 1999, Russia, whose GDP is almost as large as that of the rest of the countries in Central and Eastern Europe put together (see Table 4, p. 20), had attracted about the same volume of FDI as the Czech Republic. This fact alone indicates that hitherto foreign companies have not held the Russian business climate in high esteem, considering it unsound and hence preferring to maintain a holding position.

Burdened with a legacy comprising a bulk of mostly obsolete industrial capacities, the **transformation of the industrial sector** was a task of decisive importance to the success of the transformation process. A glimpse at the long-term development of industrial output offers a hint of the extent of destruction and creation within an economy. As Table 5 (p. 22) shows, gross industrial production in Hungary and Poland surpassed the 1990 level to a considerable degree, while all the other countries still languish at levels far below.

Industrial output in Bulgaria, the Czech Republic, Romania and Slovakia recorded an appreciable decline in 1999. This may not be primarily attributable to the business cycle phenomenon, but it does point to the existence of problems at the enterprise level and the need for a response in the form of restructuring measures to a greater or lesser degree. Admittedly, positive industrial growth rates of themselves do not guarantee the absence or avoidance of such problems, as both Russia and the Ukraine go to show. Another important indicator of structural change in industry is the longer-term development of labour productivity as shown in Table 6 (p. 22).

To sum up, the phenomenon of permanent or re-emergent transitional recession has appeared in countries where the transformation of the financial and non-financial corporate sector has been incomplete, thus restricting the efficiency of the new institutions and institutional settings. Though fashionable at the outset of the transition period, the notion of 'shock therapy' created the erroneous impression of the state implementing reforms in one painful stroke, to be followed by relaxation thereafter. However, in those instances where endeavours went no further than liberalizing trade and some of the prices, and hasty privatization to boot, the restructuring of the corporate sector remained half-hearted and the economy failed to reach the starting point essential to sustainable growth.

No hope of West European inflation rates in the near future

Throughout the whole transition period, combating inflation has attracted more attention than developing (or not developing) a firm industrial backbone. In all countries transition

Table 5

Gross industrial production

real change in % against preceding year

	1992	1993	1994	1995	1996	1997	1998 1)	1988 Jan-Sept	1999 Jan-Sept	1999 est.	2000 forecast	2001 forecast	Index 1990=100 1999
Czech Republic	-7.9	-5.3	2.1	8.7	2.0	4.5	3.1	6.4	-4.7	-3.0	2	2	81.3
Hungary	-9.7	4.0	9.6	4.6	3.4	11.1	12.5	13.6	8.4	9.0	10	11	126.5
Poland 2)	2.8	6.4	12.1	9.7	8.3	11.5	4.7	7.0	1.5	4.4	5	6	163.3
Slovak Republic	-9.3	-3.8	4.8	8.3	2.5	2.7	5.0	6.4	-6.3	-5.0	-1	0	83.7
Slovenia	-13.2	-2.8	6.4	2.0	1.0	1.0	3.7	4.5	-1.8	-1.0	2	2	84.0
CEEC-5 3)	-3.6	1.6	8.2	8.2	5.1	8.3	5.4	7.6	0.0	2.0	4.2	4.9	120.8
Bulgaria	-18.4	-9.8	10.6	4.5	5.1	-10.0	-12.7	-6.7	-14.1	-10.0	4	4	50.4
Romania	-21.9	1.3	3.3	9.4	6.3	-7.2	-16.8	-17.0	-9.0	-8.0	0	2	52.1
CEEC-7 3)	-8.6	1.0	7.2	8.3	5.4	3.8	-0.7	1.2	-2.8	-0.9	3.2	4.2	96.6
Croatia	-14.6	-5.9	-2.7	0.3	3.1	6.8	3.7	6.7	-2.8	-1.4	1	2	63.1
Macedonia	-15.7	-14.1	-10.5	-10.7	3.2	1.6	4.5	7.9	-2.6	-2.5	0	3	51.4
Yugoslavia	-22.0	-37.3	1.3	3.8	7.5	9.5	3.6	6.7	-25.8	-22.5	4	5	39.9
Russia	-18.0	-14.1	-20.9	-3.3	-4.0	1.9	-5.2	-3.7	7.0	8.1	3	3	49.7
Ukraine	-6.4	-8.0	-27.3	-11.7	-5.1	-1.8	-1.5	-0.3	2.3	4.0	3	5	50.3

Notes: 1) Preliminary. – 2) Sales. – 3) WIIW estimate.

Source: WIIW Database incorporating national statistics, forecast: WIIW.

Table 6

Labour productivity in industry

change in % against preceding year

	1992	1993	1994	1995	1996	1997	1998 1)	1998 Jan-Sept	1999 Jan-Sept	Index 1999 1) 1990=100
Czech Republic 2)	-2.2	-1.2	5.1	10.6	8.6	9.2	4.7	7.9	-0.4	120.3
Hungary 3)	-4.7	13.4	15.7	10.2	9.4	13.7	11.9	13.4	8.1	195.8
Poland	14.3	9.7	13.0	6.3	9.1	11.2	5.4	7.7 4)	6.1 4)	205.0
Slovak Republic	-2.9	1.8	7.2	4.0	2.5	4.8	9.5	10.3	-3.3	108.9
Slovenia	-3.3	5.8	13.2	6.3	9.2	4.4	5.4	6.4	1.6	149.3
Bulgaria 5)	-1.9	-0.2	16.2	7.4	7.0	-7.5	-6.0	-5.8	-4.8	103.9
Romania	-13.4	9.0	14.7	13.7	7.5	-1.8	.	.	5.9	.
Croatia 6)	0.3	0.3	3.0	6.6	11.3	11.9	8.7	11.6	2.8	134.3
Macedonia	-11.4	-11.9	-6.5	1.2	29.8	8.3	14.8	.	.	.
Yugoslavia 7)	-18.2	-34.7	2.1	8.3	9.6	13.9	6.6	.	.	.
Russia	-17.6	-8.8	-14.4	5.4	2.9	8.6	-0.1	.	.	.
Ukraine	-4.1	-3.2	-20.9	-4.2	3.0	7.1	6.0	.	.	.

Notes: 1) Preliminary. – 2) Enterprises with 100 and more employees, in 1992 to 1994 with 25 and more, from 1997 with 20 and more. – 3) From 1992 enterprises with more than 20, from 1995 with more than 10, from 1999 more than 5 employees. – 4) Enterprises with more than 5 employees. – 5) Up to 1996 public sector only. – 6) Enterprises with more than 20 employees. – 7) Excluding private enterprises.

Source: WIIW Database incorporating national statistics.

was initially coupled with high inflation, hitherto most of the countries have recorded rates of inflation far above those to be observed in developed market economies (Table 7, p. 23 and Figure 10, p. 14). In the more successful transition countries, inflation tended to **decelerate gradually**. However, of the countries under review certain countries saw inflation leap upwards when they had to tackle crises that led to their currencies being greatly devalued. In recent years, this was the case in Bulgaria, Romania and Russia. Slovakia's inflation rate has also increased recently, the rate of growth dropping from a comparatively high level down close to zero.

Table 7

Consumer price inflation

change in % against preceding year

	1992	1993	1994	1995	1996	1997	1998 1)	1998 Jan-Sept	1999 Jan-Sept	1999 est.	2000 forecast	2001 forecast
Czech Republic	11.1	20.8	10.0	9.1	8.8	8.5	10.7	11.8	2.2	2.1	3.5	3.5
Hungary	23.0	22.5	18.8	28.2	23.6	18.3	14.3	15.3	9.8	10.0	8.3	6.5
Poland	43.0	35.3	32.2	27.8	19.9	14.9	11.8	12.6	6.6	7.3	7.0	5.0
Slovak Republic	10.0	23.2	13.4	9.9	5.8	6.1	6.7	7.0	9.3	10.5	13.0	10.0
Slovenia 2)	207.3	32.9	21.0	13.5	9.9	8.4	7.9	8.4	5.6	6.1	5.5	4.5
Bulgaria	91.2	72.8	96.0	62.1	123.0	1082.3	22.3	30.4	-1.1	0.3	3	3
Romania	210.4	256.1	136.8	32.3	38.8	154.8	59.1	65.9	43.0	45.8	40	35
Croatia 2)	665.5	1517.5	97.6	2.0	3.5	3.6	5.7	5.6	4.0	4.2	4.0	4.0
Macedonia 2)	1690.7	349.8	121.7	15.9	3.0	4.4	0.8	1.4	-1.5	-1.0	3.0	5.0
Yugoslavia 3)	8926.4	.	3.3	78.6	91.5	21.6	29.9	24.2	42.8	44.9	35	50
Russia	1526.5	873.5	307.0	197.5	47.8	14.8	27.6	13.1	105.4	85.7	22	20
Ukraine	1210.0	5371.0	891.0	376.8	80.2	15.9	10.6	8.1	24.2	19.2	20	20

Notes: 1) Preliminary. – 2) Retail prices. – 3) In 1994 data refer to December/February.

Source: WIIW Database incorporating national statistics, forecast: WIIW.

Statistical data suggest that during the transition process, success in terms of nominal stability – low inflation, stable exchange rate – did not generally support real GDP growth. Of the more successful countries in terms of economic growth, all record relatively high, albeit decelerating inflation, although in each case a rapid acceleration in inflation was admittedly indicative of a more general deep crisis. In the Czech Republic and Bulgaria, an inflation rate close to nil in1999 went hand in hand with paralysis in the real sector.

In all likelihood, inflation – at least if it is gradually decelerating – assumes a **positive function** within the transition process. This makes it easier to overcome distortions in relative prices. The price relations, especially the ratio between tradable goods and non-tradable services, still differs markedly from ratios in the West. Adjustment is easier to

Table 8

Foreign trade of Central and Eastern Europe and the main CIS States in USD bn

(based on customs statistics)

		1996	1997	1998	*1998 / 1997 in %*	1998	1999	*I-IX 99 / I-IX 98 in % (USD)*	*I-IX 99 / I-IX 98 in % (EUR)* [1]	1999	2000	2001
						Jan - Sept					estimate	
Czech Republic	Exports	21.9	22.8	26.3	*15.6*	19.4	19.5	*0.3*	*2.7*	26.9	29.0	30.6
	Imports	27.7	27.2	28.8	*5.9*	20.9	20.4	*-2.0*	*0.4*	28.9	31.5	33.2
	Balance	-5.8	-4.4	-2.4	.	-1.4	-1.0	.	.	-2.0	-2.5	-2.6
Hungary [2]	Exports	13.1	19.1	23.0	*20.5*	16.5	17.6	*6.6*	*9.2*	24.9	27.9	31.0
	Imports	16.2	21.2	25.7	*21.2*	18.5	19.9	*7.5*	*10.1*	27.8	30.9	34.3
	Balance	-3.1	-2.1	-2.7	.	-2.0	-2.3	.	.	-2.9	-3.0	-3.3
Poland	Exports	24.4	25.8	28.2	*9.6*	21.0	19.8	*-5.4*	*-3.1*	26.7	27.5	28.9
	Imports	37.1	42.3	47.1	*11.2*	34.8	32.8	*-5.6*	*-3.3*	44.8	47.0	49.4
	Balance	-12.7	-16.6	-18.8	.	-13.8	-13.0	.	.	-18.1	-19.5	-20.5
Slovakia [3]	Exports	8.8	8.3	10.7	*10.7*	7.9	7.3	*-7.3*	*-5.0*	10.2	10.5	10.8
	Imports	11.1	10.3	13.0	*11.1*	9.5	8.1	*-14.8*	*-12.7*	11.3	11.5	11.6
	Balance	-2.3	-2.0	-2.3	.	-1.6	-0.8	.	.	-1.1	-1.0	-0.8
Slovenia	Exports	8.3	8.4	9.1	*8.1*	6.6	6.3	*-4.7*	*-2.4*	8.5	8.8	9.2
	Imports	9.4	9.4	10.1	*7.9*	7.3	7.3	*-0.5*	*2.0*	9.9	10.2	10.4
	Balance	-1.1	-1.0	-1.1	.	-0.7	-1.0	.	.	-1.4	-1.4	-1.2
CEEC-5	Exports	76.6	84.3	97.3	*15.5*	71.4	70.5	*-1.2*	*1.2*	97.2	103.7	110.5
	Imports	101.6	110.3	124.6	*13.0*	91.0	88.6	*-2.7*	*-0.3*	122.7	131.1	138.9
	Balance	-25.0	-26.1	-27.3	.	-19.6	-18.1	.	.	-25.5	-27.4	-28.4
Bulgaria	Exports	4.9	4.9	4.3	*-12.9*	3.2	2.7	*-13.5*	*-11.4*	3.8	4.2	4.4
	Imports	5.1	4.9	5.0	*1.0*	3.6	3.7	*4.0*	*6.5*	4.9	5.0	5.1
	Balance	-0.2	0.0	-0.7	.	-0.4	-1.0	.	.	-1.1	-0.8	-0.7
Romania	Exports	8.1	8.4	8.3	*-1.5*	6.2	6.1	*-1.5*	*0.9*	8.3	8.5	8.9
	Imports	11.4	11.3	11.8	*4.9*	8.6	7.3	*-15.4*	*-13.3*	10.0	10.3	10.8
	Balance	-3.4	-2.8	-3.5	.	-2.4	-1.2	.	.	-1.7	-1.8	-1.9
CEEC-7	Exports	89.6	97.6	109.9	*12.6*	80.7	79.3	*-1.7*	*0.7*	109.3	116.4	123.8
	Imports	118.1	126.5	141.4	*11.8*	103.2	99.6	*-3.5*	*-1.1*	137.6	146.4	154.8
	Balance	-28.5	-28.9	-31.5	.	-22.5	-20.3	.	.	-28.3	-30.0	-31.0
Croatia	Exports	4.5	4.2	4.5	*8.9*	3.3	3.2	*-5.7*	*-3.4*	4.2	4.4	4.6
	Imports	7.8	9.1	8.4	*-7.9*	6.2	5.6	*-9.7*	*-7.5*	7.6	8.0	8.2
	Balance	-3.3	-4.9	-3.8	.	-2.9	-2.5	.	.	-3.4	-3.6	-3.6
Macedonia	Exports	1.1	1.2	1.3	*6.0*	1.0	0.9	*-11.9*	*-9.8*	1.2	.	.
	Imports	1.6	1.8	1.9	*7.6*	1.4	1.2	*-11.7*	*-9.6*	1.7	.	.
	Balance	-0.5	-0.5	-0.6	.	-0.4	-0.3	.	.	-0.5	.	.
Yugoslavia	Exports	2.0	2.7	2.8	*5.7*	2.1	1.1	*-49.2*	*-47.9*	1.5	.	.
	Imports	4.1	4.8	4.7	*-1.9*	3.8	2.2	*-41.5*	*-40.0*	3.3	.	.
	Balance	-2.1	-2.2	-1.9	.	-1.7	-1.1	.	.	-1.8	.	.
Russia [4]	Exports	88.6	88.3	73.9	*-16.3*	54.8	50.8	*-7.3*	*-5.0*	73.0	78.0	82.0
	Imports	68.8	73.5	59.6	*-18.9*	49.4	29.5	*-40.3*	*-38.8*	42.0	46.0	55.0
	Balance	19.8	14.8	14.3	.	5.4	21.3	.	.	31.0	32.0	27.0
Ukraine	Exports	14.4	14.2	12.6	*-11.2*	9.6	8.3	*-13.7*	*-11.5*	11.2	10.5	11.5
	Imports	17.6	17.1	14.7	*-14.3*	11.3	8.4	*-25.1*	*-23.3*	11.4	10.4	12.0
	Balance	-3.2	-2.9	-2.0	.	-1.7	-0.2	.	.	-0.2	0.1	-0.5

1) In EUR terms. - 2) From 1997 including trade of firms with customs free legal status. - 3) From 1998 new methodology. - 4) Including estimate of non-registered trade.

Source: WIIW Database incorporating national statistics, WIIW forecast.

effect if prices for non-tradables are permitted to increase apace while those for tradables remain relatively stable. Something analogous also holds true for labour markets: In transition economies, average nominal wages display a continuous upward trend. This, however, is not due to proportional growth on all wage fronts: it is more on account of diversification. Wages paid to skilled labour, and managers' salaries in particular, are rising significantly. This exerts a cost-push on inflation. In the case of continuous or repeated nominal currency devaluation, an additional cost push derives from inputs imported, the prices of which tend to rise faster than those of domestically produced material. The same applies to durable inputs (capital goods). In both cases, the higher the imports content, the greater the cost-push on prices, thus inducing changes in the ratio between output prices. Market forces also play a role. Powerful restructured enterprises – for the most part companies known as 'foreign investment enterprises' – have shown themselves capable of achieving relatively high profit margins, thus earning more revenue which can then be re-invested in the companies' future.

Another topic in the context of prices, but not directly related to inflation, is the current difference between prices in the West and those in transition countries. For the EU candidate countries, the gap will in all likelihood shrink considerably, if not vanish completely – either prior to accession or during the first years of membership. Nobody is quite sure which processes will lead to this result. In Table 3 (p. 19) the gap is reflected in the difference between GDP at current exchange rates and GDP at purchasing power parities.

At present, one euro or USD buys more consumer goods in Eastern Europe than it can purchase in the West. Hence people in the transition countries can survive despite the relatively low (and in some countries extremely low) per capita incomes calculated at current exchange rates. The price differences between East and West are less pronounced in the case of 'international' brands, such as motor cars manufactured in the West. The price differences between tradable Western products and their Eastern counterparts are more significant, while the gap is largest in the case of non-tradable commodities. To mention but one example, metro tickets are much more expensive in the EU or the United States than in Central and Eastern Europe.

CEEC prices appear to be **slow in converging** to West European levels. Normally, the higher their inflation, the higher the rate of currency depreciation. Some real appreciation is to be observed, but it is insufficient to push CEEC prices up to Western levels in the near future. However, in addition to slow real appreciation **yet another process** is at work and supports convergence. In each CEEC, a number of people earn more or less Western incomes, have developed Western lifestyles and their consumer baskets contain predominantly Western goods. At the other extreme, a large number of people in the same

Table 9

Exports to Germany 1997-99

	USD bn			% of total exports			% of Germany's imports		
	1997	**1998**	**I-IX 1999**	**1997**	**1998**	**I-IX 1999**	**1997**	**1998**	**I-IX 1999**
Czech Republic	8.144	10.152	8.128	35.7	38.5	41.7	1.9	2.2	2.4
Hungary	7.116	8.419	6.703	37.3	36.6	38.1	1.6	1.8	2.0
Poland	8.465	10.238	7.150	32.9	36.3	36.4	1.9	2.2	2.1
Slovakia	1.616	3.087	2.085	19.6	28.9	28.3	0.4	0.7	0.6
Slovenia	2.460	2.572	1.957	29.4	28.4	31.2	0.6	0.6	0.6
Bulgaria	0.469	0.449	0.289	9.5	10.4	10.6	0.1	0.1	0.1
Romania	1.419	1.629	1.119	16.8	19.6	18.4	0.3	0.4	0.3
Croatia	0.746	0.767	0.511	17.9	16.9	16.2	0.2	0.2	0.2
FYR Macedonia	0.199	0.238	0.196	16.1	18.0	22.9	0.0	0.1	0.1
FR Yugoslavia	0.218	0.325	0.124	9.2	11.7	11.7	0.1	0.1	0.0
Russia	6.846	6.417	.	7.9	8.8	.	1.6	1.4	.
Ukraine	0.569	0.639	0.418	4.0	5.1	5.1	0.1	0.1	0.1
Total	38.266	44.931	28.681	18.6	22.1	31.0	8.8	9.7	8.6

Imports from Germany 1997-99

	USD bn			% of total imports			% of Germany's exports		
	1997	**1998**	**I-IX 1999**	**1997**	**1998**	**I-IX 1999**	**1997**	**1998**	**I-IX 1999**
Czech Republic	8.669	9.941	7.028	31.9	34.5	34.3	1.7	1.8	1.8
Hungary	5.719	7.252	5.898	27.0	28.2	29.7	1.1	1.3	1.5
Poland	10.195	12.032	8.322	24.1	25.8	25.4	2.0	2.2	2.1
Slovakia	1.560	3.353	2.135	15.2	25.9	26.4	0.3	0.6	0.5
Slovenia	1.936	2.089	1.496	20.7	20.7	20.5	0.4	0.4	0.4
Bulgaria	0.580	0.683	0.574	11.8	13.7	15.3	0.1	0.1	0.1
Romania	1.851	2.065	1.276	16.4	17.4	17.5	0.4	0.4	0.3
Croatia	1.841	1.616	1.076	20.2	19.3	19.1	0.4	0.3	0.3
FYR Macedonia	0.239	0.255	0.167	13.4	13.3	13.9	0.0	0.0	0.0
FR Yugoslavia	0.643	0.590	0.241	13.4	12.6	11.4	0.1	0.1	0.1
Russia	6.767	5.738	.	12.6	13.0	.	1.3	1.1	.
Ukraine	1.309	1.264	0.630	7.6	8.6	7.5	0.3	0.2	0.2
Total	41.308	46.877	28.844	19.4	21.8	24.7	8.1	8.7	7.3

Source: WIIW Database, IMF.

country still consume approximately the same basket of consumer goods as they did ten years ago. Indeed, the basket may well be even smaller now, but it still contains the same brands, the same flat and the like. The majority of the population find themselves between these two extremes: however, a continuous net shift towards the first group is perceptible. Over time, cheap low-quality brands will be marginalized. This process contributes to the convergence towards Western price levels. Some people will never be able to make the shift; as far as they are concerned, convergence towards Western standards will never materialize. Diversification within the individual societies, the rapid changes in the contents of the consumer baskets and the equally rapid change in commodity quality make it extremely difficult to **measure inflation** at all.

Interest and exchange rate dilemma

Though frequently regarded as a potential source of disruption, liberalized cross-border capital flows may well be able to transmit signals comparable to those of an early warning system. However, under the conditions prevailing in the transition countries, they give rise to a dilemma. The rate of inflation is relatively high in most of these countries, and the central banks thus regard it advisable to intervene where nominal interest rates are concerned so as to keep real interest rates positive – or even highly positive. In the absence of a threat of an imminent or sudden major currency devaluation, high nominal rates of this kind attract an inflow of foreign capital. Whereas it is quite true that capital is exactly what the country lacks, it is not guaranteed that this kind of short-term capital will yield anything positive for the real sector: it does not necessarily lead to more fixed capital formation. On the contrary, these inflows tend to **nudge the exchange rate away from the level that would keep the current account deficit in a sustainable range**. This has been the case in Poland. The situation in the Czech Republic is different: the country recorded an inflation rate of only 2.1% in 1999 and the dilemma was thus not so acute[15]. Nevertheless, it was there for all to see.

In the course of spring 1998, the Russian rouble came under pressure despite there being no significant external imbalance. Oil export revenues which had always ensured a huge trade surplus began to shrink in 1997. World market prices for oil also dropped. The exchange rate in the pre-crisis period was inappropriate to the manufacturing sector, leading to a large import surplus of manufactured goods. An attempt to defend the fixed exchange rate corridor depressed industrial production. At the same time, the market was not convinced that the policy could be sustained over time. When interest rates had to be pushed upwards to inordinately high levels in order to avert a huge net outflow of capital, confidence crumbled still more – it was only a question of time before policy followed suit.

[15] In September 1999 the deposit rate of Czech commercial banks was 4.9%, the lending rate 8.4%.

Table 10

Foreign financial position

USD bn, end of period

	Gross external debt [1]		Reserves of National Bank (excluding gold) [2]		Current account			
	1998	1999 Sept.	1998	1999 Sept.	1998	1999	2000 forecast	2001 forecast
Czech Republic	24.0	22.5	12.6	12.0	-1.3	-0.8	-1.3	-1.5
Hungary	26.7	28.3	9.3	10.3	-2.3	-2.1	-2.1	-2.2
Poland	56.9	57.4 [3]	27.4	26.0	-6.9	-11.7	-13.0	-13.0
Slovak Republic	11.8	10.4	2.9	2.9	-2.1	-1.0	-0.8	-0.5
Slovenia	4.9	5.6	3.6	3.2	0.0	-0.5	-0.3	-0.3
CEEC-5	124.4	124.1	55.9	54.5	-12.6	-16.1	-17.5	-17.5
Bulgaria	10.2	9.7	2.7	2.5	-0.4	-0.6	-0.6	-0.5
Romania	9.1	8.1	1.7	1.7	-3.0	-1.3	-1.6	-1.7
CEEC-7	143.7	141.9	60.2	58.6	-15.9	-17.9	-19.7	-19.7
Croatia	8.5	9.3	2.8	2.8	-1.6	-1.4	-1.5	-1.7
Macedonia	1.4	1.4	0.3	0.4	-0.3	-0.1	-0.3	-0.4
Yugoslavia	11.5	.	0.3	.	-1.2	0.6	-0.8	-1.0
Russia	145.0	.	12.2	11.2	2.1	17.0	15.0	10.0
Ukraine	11.5	.	0.8	1.3	-1.3	0.9	0.3	-0.5

Notes: 1) In convertible currencies for Bulgaria, Czech Republic. For more information see country tables respectively. – 2) Forex reserves, SDR and reserve position with the IMF. Including gold for the Czech Republic, Hungary, Poland, Russia, Slovakia, Ukraine. Figures for Hungary correspond to total reserves of the country. – 3) End of June.

Source: WIIW Database incorporating national statistics, forecast: WIIW.

Forecasters regard a smooth continuation of economic growth in Poland as the most probable scenario. If it is to come up to this expectation, the country will have to overcome problems arising in connection with the growing current account deficit. According to preliminary results, it amounted to 7.6% of GDP in 1999 and will probably increase still further. The high trade deficit, which is still rising, points to a lack of strength among Poland’s producers of tradable goods and their not being export-oriented enough to **cope with a hard currency policy**. In a manner reminiscent of the Czech Republic prior to the currency crisis in May 1997, the National Bank of Poland has started to increase interest rates, a move which will first and foremost attract an influx of capital. The Polish zloty could become rather strong temporarily and trigger off a further deterioration of the current account, thus heightening the risk of confidence on international currency markets suddenly eroding. There is some possibility of this or something like it occurring sooner or later; however, it is difficult to assess the amount of damage that such a development would cause in terms of a decline in GDP growth. Possibly, it may not be too excessive. The Polish authorities claim to be watching out for any market-induced volatility of the exchange rate, albeit more as a passive observer. Nevertheless, the National Bank of

Poland exerts a decisive influence on the exchange rate via nominal interest rates. As the authorities have not committed themselves to any heroic act of defence, they can change their policies without much hullabaloo – unlike Prague before May 1997 and Moscow before August 1998.

In general, as long as physical assets can be sold to foreigners the capital inflow accruing therefrom can more or less offset the deficit in the current account. After some time, sales effected at an earlier juncture tend to influence the current account negatively through profit repatriation. The question that thus arises will be whether the inflow of foreign direct investment has helped to build up sufficient competitive export capacities – as in the longer term the latter are the sole remedy for outweighing the high and ever-increasing import-intensity of domestic production, a typical feature of transition countries.

On the threshold to overall sustainable growth?

We have now reached a point where almost all transition countries have started to grow. The crucial question is whether the even less successful countries, the latecomers, are standing on the threshold to long-term growth. In their case, it would first amount to making up for lost ground, after a decade of permanent GDP decline. Some years hence, net expansion could follow.

Past experience in most of the CEEC-7 should **guard against our being over-optimistic**. As mentioned above, only three of these countries have managed so far to maintain significant growth without disruption – Hungary, Poland and Slovenia. In the others (Bulgaria, the Czech Republic, Romania and Slovakia), high growth has proved unsustainable over time. In these latter cases, serious deficiencies at the enterprise level were allowed to provoke a growing mismatch of internal financial relations; they also led to current account deficits that proved too high and thus unsustainable in the long term. This was not always linked to a high deficit in the state budget. Whereas this was the case in Bulgaria and Romania, it was not so in the Czech Republic and Slovakia – at least as long as we disregard quasi-fiscal deficits. The mismatch of internal financial relations surfaced as the low capital adequacy of commercial banks, mostly large state-dominated banks, became apparent, thus making it necessary for the state to step in and ultimately bail them out.

Knowing this, it is difficult to expect smooth and high long-term growth in the less developed transition countries. At the business level, **deficiencies still persist**. At the same time, it is also true that in most countries it is no longer that easy to consume electricity or other inputs without paying for them. Nor is it that easy any more to produce without paying wages and tax. Combating such avoidance tactics is still fraught with problems, as the local workforce is invariably upset if an enterprise folds or has to be streamlined/ shut down. It is especially hard in cases where the enterprise in question was the main or sole source of income for a whole region. In all probability, **regional questions** will take on particular significance in the years to come.

A positive outlook for 2000 and 2001

The WIIW forecasts a strengthening of the positive signals now visible (Table 11, p. 32). Thus, **in almost all cases GDP growth in 2000 will be better than it was in 1999**. The only exception among the countries under consideration will be Slovakia. For the Czech Republic, Croatia and Yugoslavia this will mean renewed growth. With the exception of Bulgaria, Poland and Yugoslavia, growth in most cases will accelerate further in 2001. Of course, some unforeseeable shock could spoil this positive outlook. On the other hand, should the recovery of the Russian economy strengthen apace, this will have a stimulating impact on the whole region in the long term. **In some cases, the forecast is rather robust; in others, uncertainty is high**. For Hungary and Slovenia, the probability of an economic crisis is not very high. Given its expanding current account deficit, Poland appears more vulnerable. In the case of the Czech Republic, it seems quite likely that the current slight recovery will continue, but here both a negative shock and stronger growth than forecast are feasible. The latter also holds true for Slovakia. For the most part, Bulgaria's growth is externally financed and the future is shaky given the problems persisting at the enterprise level. Romania could ultimately start to harvest some of the fruits of its recent radical restructuring measures.

Current developments in the economies of Macedonia and Yugoslavia have more to do with the recent Kosovo crisis than with the business upswing in Western Europe. The conflict has also had an influence on the economies of Bulgaria, Croatia, Hungary and Romania. If it is to achieve a substantial economic take-off, the Balkan region will still have to find a new modus vivendi, in which the countries stop impeding each other and undermining confidence in the region as a whole.

For this and the year to come, the WIIW expects **some convergence of inflation rates**. Countries with two-digit rates will enjoy some measure of decline, while those that already enjoyed relatively low rates of inflation in the past, viz. Bulgaria, the Czech Republic, Macedonia and Slovakia (see Table 7, p. 23), will experience some increase for a variety of reasons. In their case, however, increases in regulated prices assume a more significant role.

An **unemployment rate of around 12%** seems to be establishing itself as the norm for the transition countries. In 2001 it could come close to this level in the Czech Republic, Poland, Romania, Russia and Slovenia. After rates close to zero in the previous system, it reflects the introduction of labour-saving technologies as well as the failure during the transition period to offset the extensive closure of obsolete capacities by creating new capacities. Hungary has seen considerable formation of new capital and consequently the rate of unemployment dropped to below 10% in 1998 and will drop further to 9% this year and the year to come. On the other hand, until recently Bulgaria (1998) and Slovakia (1997) recorded rates not far from 12%, but they might be as high as 16-18% in 2001 – given the degree of destructive (as opposed to creative) restructuring. In the area of former Yugoslavia markets had already collapsed, links to foreign markets were disrupted and capacities were destroyed as far back as the first half of last decade; unemployment rates are thus correspondingly high, and this will not change in the near future. In 2001, it will still stand at more than 20% in Croatia and around 32-35% in Macedonia and Yugoslavia. In the official employment figures provided by the Ukraine, registered unemployment is just emerging. By 1999 it had reached 5%[16] and might go up a few points this year and next. In this case, however, the low rate is more a sign of delays in restructuring.

In 1999, some countries obviously experienced problems in maintaining the competitiveness of domestic goods and services at home and abroad; in brief, they encountered difficulties in terms of their imports and exports. The current account deficit was 7.1% of GDP in Croatia, 7.6% in Poland and 5.4% in Slovakia. For Croatia and Poland, the WIIW expects a further rise – at least in the event that their interest and exchange rate policies remain unchanged. Slovakia's deficit will probably decline under the weight of the present austerity policy.

Over the next few years, most transition countries will encounter difficulties in their attempts to secure high GDP growth, while simultaneously limiting their current account deficits. These problems will fade away, however, once the country has built up a strong industrial backbone.

[16] These figures do not reflect the full extent of unemployment. ILO figures, based on a different measurement concept, are higher.

Table 11

Overview developments 1998 - 1999 and outlook 2000 - 2001

	GDP real change in % against previous year				Consumer prices change in % against previous year				Unemployment rate in %, end of period				Current account in % of GDP			
	1998	**1999**	**2000**	**2001**	**1998**	**1999**	**2000**	**2001**	**1998**	**1999**	**2000**	**2001**	**1998**	**1999**	**2000**	**2001**
			forecast				**forecast**				**forecast**				**forecast**	
Czech Republic	-2.3	-0.6	1.5	2	10.7	2.1	3.5	3.5	7.5	9.4	11	12	-2.4	-1.5	-2.4	-2.6
Hungary	4.9	4.0	4.5	5	14.3	10.0	8.3	6.5	9.6	9.6	9	9	-4.8	-4.2	-4.0	-3.8
Poland	4.8	4.1	4.5	5	11.8	7.3	7	5	10.4	13	12.5	12	-4.3	-7.6	-8.1	-7.7
Slovak Republic	4.4	2.0	0.0	2	6.7	10.5	13	10	15.6	19.2	19	18	-10.1	-5.4	-4.1	-2.5
Slovenia	3.9	3.7	3.7	4	7.9	6.1	5.5	4.5	14.6	13	12	12	0.0	-2.5	-1.2	-1.1
CEEC-5	3.1	2.8	3.4	4.0	.	.	.	.	10.4	12.5	.	.	-4.2	-5.4	-5.7	-5.4
Bulgaria	3.5	2.5	4	4	22.3	0.3	3	3	12.2	16	17	16	-3.1	-4.6	.	.
Romania	-5.4	-3.9	0	1	59.1	45.8	40	35	10.3	12	13	12	-7.3	-4.2	-5.0	-5.3
CEEC-7	1.4	1.5	2.8	3.4	.	.	.	.	10.5	12.7	.	.	-4.5	-5.3	.	.
Croatia [1)]	2.5	-2.0	1	2	5.7	4.2	4	4	18.6	20.8	21	22	-7.3	-7.1	-7.3	.
Macedonia [1)2)]	2.9	2.7	3	5	0.8	-1	3	5	34.5	32.4	32	32	-8.1	-4.2	-8.6	-10.4
Yugoslavia	2.5	-19.3	3	3	29.9	44.9	35	50	27.2	32	35	35	-8.6	.	.	.
Russia [2)]	-4.6	1.7	2	3	27.6	85.7	22	20	13.3	12	12	12	0.7	9.3	8.2	5.0
Ukraine	-1.7	-0.4	1	3	10.6	19.2	20	20	3.7	5	6	8	-3.1	2.9	1.2	-1.9

1) Consumer prices correspond to retail prices. - 2) Unemployment rate according to ILO definition.

Source: WIIW (January 2000).

ANNEX

Indicators of competitiveness

Table A/1

GDP per capita at current PPPs (ECU), from 2000 constant PPPs

	1990	1993	1994	1995	1996	1997	1998	1999	2000	2005	2010	2015
									projection assuming 4% p.a. GDP growth and zero population growth			
Czech Republic	10136	9886	10325	11334	12025	12332	12194	12286	12778	15546	18914	23012
Hungary	7222	7384	7789	8297	8613	9231	9830	10424	10841	13189	16047	19524
Poland	4544	4931	5291	6235	6742	7349	7785	8185	8513	10357	12601	15331
Slovak Republic	7492	6331	6755	7461	8101	8802	9279	9572	9955	12112	14736	17928
Slovenia	10122	9944	10713	11561	12192	13052	13746	14362	14937	18173	22110	26900
Bulgaria	4866	4463	4656	4987	4600	4447	4629	4794	4986	6066	7380	8979
Romania	5344	4854	5163	5745	6113	5827	5585	5395	5610	6826	8305	10104
Croatia	5980	4360	4709	5189	5833	6236	6564	6518	6779	8248	10035	12209
Macedonia	3654	3478	3704	3755	3845	3958	4090	4212	4380	5329	6484	7888
Russia	8425	6907	6166	6140	6074	6275	6069	6258	6508	7918	9633	11721
Ukraine	5875	4567	3626	3324	3080	3074	3079	3101	3225	3924	4774	5808
									projection assuming 2% p.a. GDP growth and zero population growth			
Austria	15805	17800	18566	19557	20415	21284	21710	22144	22587	24938	27533	30399
Germany	15123	17196	18301	19365	19578	20096	20498	20908	21326	23546	25997	28703
Greece	8689	10250	10862	11724	12227	13093	13355	13622	13895	15341	16937	18700
Portugal	9079	10811	11588	12403	12746	13528	13798	14074	14356	15850	17499	19321
Spain	11148	12372	12643	13497	14007	15084	15385	15693	16007	17673	19512	21543
Turkey	4436	5161	4892	5224	5534	5961	6080	6202	6326	6984	7711	8514
Japan	16857	19197	19676	21189	22123	22665	23118	23581	24052	26556	29320	32371
USA	21018	22796	23894	24842	25676	27048	27589	28141	28703	31691	34989	38631
EU(15) average	14609	15923	16687	17699	18175	18907	19286	19671	20065	22153	24459	27005

European Union (15) average = 100

	1990	1993	1994	1995	1996	1997	1998	1999	2000	2005	2010	2015
Czech Republic	69	62	62	64	66	65	63	62	64	70	77	85
Hungary	49	46	47	47	47	49	51	53	54	60	66	72
Poland	31	31	32	35	37	39	40	42	42	47	52	57
Slovak Republic	51	40	40	42	45	47	48	49	50	55	60	66
Slovenia	69	62	64	65	67	69	71	73	74	82	90	100
Bulgaria	33	28	28	28	25	24	24	24	25	27	30	33
Romania	37	30	31	32	34	31	29	27	28	31	34	37
Croatia	41	27	28	29	32	33	34	33	34	37	41	45
Macedonia	25	22	22	21	21	21	21	21	22	24	27	29
Russia	58	43	37	35	33	33	31	32	32	36	39	43
Ukraine	40	29	22	19	17	16	16	16	16	18	20	22
Austria	108	112	111	110	112	113	113	113	113	113	113	113
Germany	104	108	110	109	108	106	106	106	106	106	106	106
Greece	59	64	65	66	67	69	69	69	69	69	69	69
Portugal	62	68	69	70	70	72	72	72	72	72	72	72
Spain	76	78	76	76	77	80	80	80	80	80	80	80
Turkey	30	32	29	30	30	32	32	32	32	32	32	32
Japan	115	121	118	120	122	120	120	120	120	120	120	120
USA	144	143	143	140	141	143	143	143	143	143	143	143
EU(15) average	100	100	100	100	100	100	100	100	100	100	100	100

Sources:
BENCHMARK RESULTS OF THE 1996 EUROSTAT-OECD COMPARISON BY ANALYTICAL CATEGORIES, OECD, 1999; National statistics; WIFO; WIIW estimates.
Benchmark PPPs for 1996 estimated from purchasing power standards for OECD (28) average and extrapolated with GDP price deflators. GDP per capita for OECD countries according to OECD *National Account* statistics converted into ECU.

Table A/2

Prices, exchange rates and unit labour costs (ULCs), 1990-1999

ECU based annual averages

	1990	1993	1994	1995	1996	1997	1998	1999 prelim.
Czech Republic								
Producer price index, 1989=100	104.3	213.3	224.5	241.6	253.0	265.4	278.4	281.2
Consumer price index, 1989=100	109.7	230.5	253.5	276.7	301.0	326.6	361.6	369.2
GDP deflator, 1989=100	109.5	202.8	229.9	253.5	278.1	296.2	328.5	335.1
Exchange rate (ER), CZK/ECU	22.89	34.10	34.06	34.31	34.01	35.80	36.16	36.88
ER nominal, 1989=100	137.9	205.4	205.2	206.7	204.9	215.7	217.9	222.2
Real ER (CPI-based), 1989=100	131.2	102.8	95.3	91.2	84.9	84.0	77.5	78.2
Real ER (PPI-based), 1989=100	138.0	111.1	107.7	104.5	101.0	103.4	100.6	102.6
PPP, CZK/ECU	5.96	9.99	11.08	11.79	12.68	13.22	14.50	14.65
ERDI (ECU based)	3.84	3.41	3.07	2.91	2.68	2.71	2.49	2.52
Average monthly gross wages, CZK	3286	5817	6894	8172	9676	10691	11693	12628
Average monthly gross wages, ECU (ER)	144	171	202	238	285	299	323	342
Average monthly gross wages, ECU (PPP)	551	582	622	693	763	809	806	862
GDP nominal, bn CZK	626.2	1020.3	1182.8	1381.0	1572.3	1680.0	1820.7	1850
Employment total, 1000 persons	5351.2	4848.3	4884.8	5011.6	5044.4	4946.6	4873.4	4700
GDP per employed person, CZK	117018	210441	242138	275568	311683	339629	373599	393617
GDP per empl. person, CZK at 1996 pr.	297149	288567	292861	302298	311683	318820	316233	326644
Unit labour costs, 1989=100	94.2	171.7	200.5	230.2	264.4	285.6	314.9	329.2
Unit labour costs, ER adj., 1989=100	68.3	83.6	97.7	111.4	129.0	132.4	144.5	148.2
Unit labour costs, PPP adj., Austria=100	17.40	17.48	20.07	21.73	26.33	28.16	30.86	31.03
Hungary								
Producer price index, 1989=100	122.0	199.8	222.4	286.7	349.2	420.4	467.9	491.3
Consumer price index, 1989=100	128.9	262.1	311.4	399.3	493.5	583.8	667.3	734.0
GDP deflator, 1989=100	125.7	232.5	277.9	348.8	422.7	500.9	564.1	620.5
Exchange rate (ER), HUF/ECU	80.48	107.50	124.78	162.65	191.15	210.93	240.98	252.77
ER, nominal 1989=100	123.7	165.2	191.8	250.0	293.8	324.2	370.3	388.5
Real ER (CPI-based), 1989=100	100.2	72.7	72.5	76.4	74.2	70.6	71.4	68.7
Real ER (PPI-based), 1989=100	105.8	95.3	101.6	106.5	104.9	98.1	101.8	102.7
PPP, HUF/ECU	27.94	46.76	54.69	66.25	78.67	91.29	101.67	110.73
ERDI (ECU based)	2.88	2.30	2.28	2.45	2.43	2.31	2.37	2.28
Average monthly gross wages, HUF	13446	27173	33309	38900	46837	57270	67764	77251
Average monthly gross wages, ECU (ER)	167	253	267	239	245	272	281	306
Average monthly gross wages, ECU (PPP)	481	581	609	587	595	627	667	698
GDP nominal, bn HUF	2089.3	3548.3	4364.8	5614.0	6893.9	8540.7	10086.0	11600
Employment total, 1000 persons	5385.8	3827.3	3751.5	3678.8	3648.1	3646.3	3697.7	3850
GDP per employed person, HUF	387928	927103	1163481	1526041	1889723	2342292	2727642	3012987
GDP per empl. person, HUF at 1996 pr.	1304540	1685732	1769797	1849582	1889723	1976503	2044130	2052702
Unit labour costs, 1989=100	129.4	202.3	236.2	264.0	311.1	363.7	416.1	472.4
Unit labour costs, ER adj., 1989=100	104.6	122.5	123.2	105.6	105.9	112.2	112.4	121.6
Unit labour costs, PPP adj., Austria=100	28.63	27.51	27.18	22.13	23.21	25.63	25.77	27.36
Poland								
Producer price index, 1989=100	722.4	1806.0	2262.6	2837.2	3189.0	3578.0	3839.6	4054.6
Consumer price index, 1989=100	685.8	2259.9	2987.6	3818.1	4577.9	5260.0	5880.7	6310.0
GDP deflator, 1989=100	580.1	1628.9	2091.3	2674.6	3174.9	3620.0	4043.5	4326.6
Exchange rate (ER), PLN/ECU	1.209	2.119	2.696	3.135	3.377	3.706	3.923	4.23
ER, nominal, 1989=100	758.5	1329.1	1690.7	1966.1	2118.3	2324.1	2460.5	2653.0
Real ER (CPI-based), 1989=100	115.5	67.8	66.7	62.9	57.7	56.2	53.8	54.6
Real ER (PPI-based), 1989=100	109.6	84.9	88.0	84.6	82.8	82.6	82.4	85.0
PPP, PLN/ECU	0.3229	0.8205	1.0307	1.2724	1.4797	1.6521	1.8253	1.9337
ERDI (ECU based)	3.75	2.58	2.62	2.46	2.28	2.24	2.15	2.19
Average monthly gross wages, PLN	103	390	525	691	874	1066	1233	1363
Average monthly gross wages, ECU (ER)	85	184	195	220	259	288	314	322
Average monthly gross wages, ECU (PPP)	319	476	509	543	591	645	675	705
GDP nominal, bn PLN	56.0	155.8	210.4	306.3	385.4	469.4	549.5	612.0
Employment total, 1000 persons	16280.0	14330.1	14474.5	14735.2	15020.6	15438.7	15800.4	15610.8
GDP per employed person, PLN	3441	10871	14536	20788	25661	30402	34775	39204
GDP per empl. person, PLN at 1996 pr.	18835	21188	22069	24677	25661	26664	27305	28768
Unit labour costs, 1989=100	584.0	1968.7	2541.8	2991.4	3640.1	4270.4	4823.4	5063.3
Unit labour costs, ER adj., 1989=100	77.0	148.1	150.3	152.2	171.8	183.7	196.0	190.9
Unit labour costs, PPP adj., Austria=100	19.01	30.01	29.91	28.75	33.97	37.86	40.54	38.72

(Table A/2 contd.)

(Table A/2 contd.)

	1990	1993	1994	1995	1996	1997	1998	1999 prelim.
Slovak Republic								
Producer price index, 1989=100	104.8	218.4	240.9	262.6	273.5	285.8	295.3	305.9
Consumer price index, 1989=100	110.4	241.1	273.4	300.5	317.8	337.2	359.9	397.7
GDP deflator, 1989=100	106.6	184.2	209.6	230.0	240.3	256.2	269.2	282.6
Exchange rate (ER), SKK/ECU	22.98	35.98	37.93	38.45	38.41	37.96	39.58	44.10
ER, nominal, 1989=100	138.5	216.7	228.5	231.7	231.4	228.7	238.5	265.7
Real ER (CPI-based), 1989=100	131.0	103.7	98.5	94.1	90.8	86.3	85.2	86.8
Real ER (PPI-based), 1989=100	137.9	114.4	111.7	107.7	105.5	101.8	103.9	112.8
PPP, SKK/ECU	7.00	10.95	12.19	12.91	13.22	13.80	14.34	14.91
ERDI (ECU based)	3.28	3.29	3.11	2.98	2.90	2.75	2.76	2.96
Average monthly gross wages, SKK	3217	5379	6294	7195	8154	9226	10003	10753
Average monthly gross wages, ECU (ER)	140	150	166	187	212	243	253	244
Average monthly gross wages, ECU (PPP	459	491	516	557	617	669	697	721
GDP nominal, bn SKK	278.0	369.1	440.5	516.8	575.7	653.9	717.4	770
Employment total, 1000 persons	2478.0	2012.3	1976.9	2019.8	2036.4	2040.9	2032.1	1991
GDP per employed person, SKK	112187	183430	222831	255872	282704	320394	353041	386651
GDP per empl. person, SKK at 1996 pr.	252942	239379	255494	267407	282704	300590	315215	328785
Unit labour costs, 1989=100	105.9	187.0	205.0	223.9	240.1	255.5	264.1	272.2
Unit labour costs, ER adj., 1989=100	76.5	86.3	89.7	96.7	103.7	111.7	110.8	102.5
Unit labour costs, PPP adj., Austria=100	20.80	19.27	19.68	20.13	22.60	25.37	25.24	22.91
Slovenia								
Producer price index, 1989=100	490.4	4218.9	4965.8	5601.3	5982.4	6347.2	6728.1	6869.4
Consumer price index, 1989=100	651.6	5721.7	6923.3	7857.9	8635.7	9360.9	10100.5	10716.6
GDP deflator, 1989=100	590.8	4865.6	5964.4	6869.2	7634.4	8304.0	8912.5	9447.3
Exchange rate (ER), SIT/ECU	14.39	132.28	152.36	153.12	169.51	180.40	186.27	193.63
ER, nominal, 1989=100	446.0	4099.7	4722.1	4745.5	5253.6	5591.0	5772.9	6001.1
Real ER (CPI-based), 1989=100	71.5	82.6	80.3	73.7	75.9	76.0	73.5	72.7
Real ER (PPI-based), 1989=100	94.9	112.0	112.0	103.4	109.5	112.0	110.3	113.5
PPP, SIT/ECU	9.73	72.50	86.96	96.68	105.26	112.11	119.02	124.91
ERDI (ECU based)	1.48	1.82	1.75	1.58	1.61	1.61	1.57	1.55
Average monthly gross wages, SIT	10172	75432	94618	111996	129125	144251	158069	172611
Average monthly gross wages, ECU (ER)	707	570	621	731	762	800	849	891
Average monthly gross wages, ECU (PPP	1046	1040	1088	1158	1227	1287	1328	1382
GDP nominal, bn SIT	196.8	1435.1	1853.0	2221.5	2555.4	2907.3	3243.5	3570
Employment total, 1000 persons	909.7	755.9	746.2	745.2	741.7	743.4	745.2	755
GDP per employed person, SIT	216283	1898598	2483125	2980876	3445175	3910621	4352690	4728477
GDP per empl. person, SIT at 1996 pr.	2794637	2979012	3178364	3312933	3445175	3595258	3728462	3821091
Unit labour costs, 1989=100	483.8	3365.6	3956.9	4493.4	4981.8	5333.0	5635.1	6004.4
Unit labour costs, ER adj., 1989=100	108.5	82.1	83.8	94.7	94.8	95.4	97.6	100.1
Unit labour costs, PPP adj., Austria=100	75.65	47.00	47.11	50.56	52.96	55.53	57.04	57.35
Bulgaria								
Producer price index, 1989=100	114.7	910.6	1600.0	2454.4	5645.0	62252.6	72773.4	74592.7
Consumer price index, 1989=100	123.8	1793.7	3515.4	5698.5	12707.6	150241.7	183745.6	184296.8
GDP deflator, 1989=100	126.2	1030.2	1780.2	2897.2	6402.5	67162.7	82092.5	82338.8
Exchange rate (ER), BGL/ECU	1.00	32.41	64.59	86.83	191.65	1895.81	1972.26	1955.83
ER, nominal, 1989=100	107.6	3485.9	6946.7	9338.4	20612.4	203894.4	212116.3	210349.5
Real ER (CPI-based), 1989=100	90.7	224.1	232.8	200.1	202.3	172.6	148.5	148.2
Real ER (PPI-based), 1989=100	97.9	441.4	511.5	464.6	455.3	416.6	374.8	366.3
PPP, BGL/ECU	1.07	7.91	13.37	21.00	45.46	466.98	564.57	560.66
ERDI (ECU based)	0.93	4.10	4.83	4.13	4.22	4.06	3.49	3.49
Average monthly gross wages, BGL	378	3231	4960	7597	13247	127909	187438	209931
Average monthly gross wages, ECU (ER)	378	100	77	87	69	67	95	107
Average monthly gross wages, ECU (PPP	353	409	371	362	291	274	332	374
GDP nominal, bn BGL	45.4	298.9	525.6	880.3	1748.7	17055.2	21577.0	22000
Employment total, 1000 persons	4096.8	3221.8	3241.6	3282.2	3285.9	3157.4	3106.2	2935
GDP per employed person, BGL	11079	92784	162127	268212	532187	5401601	6946505	7494899
GDP per empl. person, BGL at 1996 pr.	562252	576634	583098	592716	532187	514926	541768	582789
Unit labour costs, 1989=100	142.3	1185.9	1800.3	2712.7	5268.1	52572.7	73223.1	76237.3
Unit labour costs, ER adj., 1989=100	132.3	34.0	25.9	29.0	25.6	25.8	34.5	36.2
Unit labour costs, PPP adj., Austria=100	86.85	18.33	13.71	14.60	13.44	14.13	18.99	19.56

(Table A/2 ctd.)

(Table A/2 ctd.)

	1990	1993	1994	1995	1996	1997	1998	1999 prelim.
Romania								
Producer price index, 1989=100	126.9	3065.5	7372.6	9961.1	14928.8	37725.0	50287.4	70402.3
Consumer price index, 1989=100	105.1	3138.9	7431.5	9829.0	13643.6	34758.8	55301.2	80629.1
GDP deflator, 1989=100	113.6	3290.6	7862.4	10633.6	15453.6	38173.3	59311.1	84221.7
Exchange rate (ER), ROL/ECU	31.10	884.60	1967.56	2629.51	3862.90	8090.93	9989.90	16296.6
ER, nominal, 1989=100	189.1	5377.5	11960.9	15984.9	23482.7	49185.0	60728.9	99067.5
Real ER (CPI-based), 1989=100	187.8	197.5	189.6	198.6	214.6	180.0	141.2	159.6
Real ER (PPI-based), 1989=100	155.5	202.3	191.1	195.9	196.2	165.8	155.3	182.8
PPP, ROL/ECU	6.92	181.39	424.07	553.61	788.18	1906.48	2929.93	4119.31
ERDI (ECU based)	4.50	4.88	4.64	4.75	4.90	4.24	3.41	3.96
Average monthly grross wages, ROL	3381	78347	181694	281287	426610	846450	1357132	1954270
Average monthly gross wages, ECU (ER)	109	89	92	107	110	105	136	120
Average monthly gross wages, ECU (PPP	489	432	428	508	541	444	463	474
GDP nominal, bn ROL	857.9	20035.7	49773.2	72135.5	108919.6	250480.2	368260.7	500000
Employment total, 1000 persons	10892.6	10260.0	10036.5	9752.0	9436.0	9201.0	9017	8476
GDP per employed person, ROL	78755	1952799	4959219	7396995	11542984	27223150	40840803	58990360
GDP per empl. person, ROL at 1996 pr.	10717506	9170922	9747361	10749987	11542984	11020712	10641169	10824000
Unit labour costs, 1989=100	117.1	3170.7	6918.2	9711.4	13716.8	28505.8	47334.1	67009.7
Unit labour costs, ER adj., 1989=100	61.9	59.0	57.8	60.8	58.4	58.0	77.9	67.6
Unit labour costs, PPP adj., Austria=100	22.72	17.75	17.10	17.06	17.16	17.75	23.96	20.40
Croatia								
Producer price index, 1989=100	555.6	204130.0	362535.0	365072.8	370183.9	378698.3	374153.9	383881.9
Consumer price index, 1989=100	709.5	195909.3	387117.4	394858.7	408679.1	423391.3	447524.9	466321.0
GDP deflator, 1989=100	629.1	136511.0	289081.6	304472.2	315254.8	336898.1	362777.1	380915.9
Exchange rate (ER), HRK/ECU	0.01	4.13	7.09	6.76	6.80	6.96	7.14	7.58
ER, nominal, 1989=100	446.0	128111.3	219657.4	209442.2	210895.8	215699.6	221182.2	234924.4
Real ER (CPI-based), 1989=100	65.6	75.4	66.8	64.8	64.4	64.8	63.6	65.4
Real ER (PPI-based), 1989=100	83.8	72.4	71.4	70.0	71.0	72.5	76.0	79.5
PPP, HRK/ECU	0.00982	1.93	3.99	4.06	4.12	4.31	4.59	4.77
ERDI (ECU based)	1.47	2.14	1.77	1.66	1.65	1.61	1.55	1.59
Average monthly gross wages, HRK	9	848	2155	2887	3243	3668	4131	4544
Average monthly gross wages, ECU (ER)	598	205	304	427	477	527	579	599
Average monthly gross wages, ECU (PPP	877	440	540	711	787	851	900	952
GDP nominal, bn HRK	0.3	39.0	87.4	98.4	108.0	122.9	135.6	140
Employment total, 1000 persons	1567.6	1446.6	1437.1	1417.4	1329.5	1310.9	1384.8	1343
GDP per employed person, HRK	179	26962	60846	69410	81219	93756	97953	104224
GDP per empl. person, HRK at 1996 pr.	89668	62265	66355	71868	81219	87733	85121	86258
Unit labour costs, 1989=100	597.4	84771.1	202160.4	250051.1	248547.2	260247.9	302089.2	327918.0
Unit labour costs, ER adj., 1989=100	133.9	66.2	92.0	119.4	117.9	120.7	136.6	139.6
Unit labour costs, PPP adj., Austria=100	78.06	31.65	43.24	53.27	55.00	58.69	66.69	66.86
Macedonia								
Producer price index, 1989=100	493.9	86212.9	163202.7	170868.8	170357.8	177512.8	184667.8	182267.1
Consumer price index, 1989=100	696.6	109299.2	249239.6	288810.8	295307.6	302985.6	302690.3	299663.3
GDP deflator, 1990=100	100.0	15432.7	35126.7	41132.0	42324.8	43723.3	44356.7	43913.13
Exchange rate (ER), MKD/ECU	0.14	27.30	51.10	49.20	50.10	56.51	60.98	63
ER, nominal, 1989=100	446.9	84781.6	158693.8	152793.3	155588.3	175501.4	189391.6	195649.9
Real ER (CPI-based), 1989=100	67.0	89.4	75.0	64.6	65.7	73.7	80.5	84.8
Real ER (PPI-based), 1989=100	94.5	113.4	114.5	109.2	113.9	125.8	131.9	139.4
PPP, MKD/ECU	0.06531	9.1210	20.314	22.96	23.14	23.41	23.49	23.03
ERDI (ECU based)	2.20	2.99	2.52	2.14	2.17	2.41	2.60	2.74
Average monthly net wages, MKD	32	3782	7754	8581	8817	9063	9394	9627
Average monthly net wages, ECU (ER)	222	139	152	174	176	160	154	153
Average monthly net wages, ECU (PPP)	488	415	382	374	381	387	400	418
GDP nominal, bn MKD	0.5	65.5	146.4	169.5	176.4	185.0	193.2	196.4
Employment total, 1000 persons	522.5	457.2	433.1	391.9	374.5	354.3	343.7	347.1
GDP per employed person, MKD	926	143326	338029	432528	471130	522181	561986	565775
GDP per empl. person, MKD at 1996 pr.	392029	393078	407297	445071	471130	505480	536242	545311
Unit labour costs, 1990=100	100.0	11831.6	23410.7	23708.7	23013.3	22047.9	21542.2	21709.3
Unit labour costs, ER adj., 1990=100	100.0	62.4	65.9	69.3	66.1	56.1	50.8	49.6
Unit labour costs, PPP adj., Austria=100	37.16	19.02	19.75	19.73	19.67	17.41	15.83	15.14

(Table A/2 contd.)

(Table A/2 ctd.)

	1990	1993	1994	1995	1996	1997	1998	1999 prelim.
Russia								
Producer price index, 1989=100	103	61181	267281	899321	1356086	1559505	1670224	2669018
Consumer price index, 1989=100	105	32112	130695	388817	574672	659723	841807	1563235
GDP deflator, 1989=100	116	41646	169848	446730	644104	750274	837140	1381280
Exchange rate (ER), RUB/ECU	0.00	1.21	2.60	5.89	6.63	6.54	11.06	26.24
ER, nominal, 1989=100	107	174605	375047	848366	954960	941800	1592973	3778258
Real ER (CPI-based), 1989=100	106.3	626.9	338.0	266.4	207.2	181.6	243.4	313.9
Real ER (PPI-based), 1989=100	108.7	329.1	165.3	115.2	87.8	76.8	122.7	183.9
PPP, RUB/ECU	0.00051	0.1674	0.6679	1.6956	2.3950	2.732	3.015	4.925
ERDI (ECU based)	1.45	7.25	3.90	3.47	2.77	2.39	3.67	5.33
Average monthly gross wages, RUB	0.3	64.3	242.6	532.6	790.2	950.2	1049.3	1575
Average monthly gross wages, ECU (ER)	407	53	93	90	119	145	95	60
Average monthly gross wages, ECU (PPP	589	384	363	314	330	348	348	320
GDP nominal, bn RUB	0.6	171.5	610.7	1540.5	2145.7	2521.9	2684.5	4500
Employment total, 1000 persons	75325	70852	68484	66441	65950	64639	63642	65000
GDP per employed person, RUB	9	2421	8918	23186	32535	39015	42182	69231
GDP per empl. person, RUB at 1996 pr.	47524	37439	33819	33430	32535	33494	32455	32283
Unit labour costs, 1989=100	121.1	32588.8	136186.5	302503.3	461145.2	538634.2	613853.6	926309.9
Unit labour costs, ER adj., 1989=100	112.9	18.7	36.3	35.7	48.3	57.2	38.5	24.5
Unit labour costs, PPP adj., Austria=100	58.26	7.91	15.11	14.09	19.96	24.64	16.66	10.40
Ukraine								
Producer price index, 1989=100	105	274001	3382263	19914767	30290361	32622718	36928917	44314700
Consumer price index, 1989=100	105	143625	1423324	6786409	12229109	14172537	15674826	18684393
GDP deflator, 1989=100	113	142056	1495770	7715454	12819488	15140086	17135166	20562200
Exchange rate (ER), UAH/ECU	0.000	0.053	0.385	1.928	2.322	2.113	2.768	4.3
ER, nominal, 1989=100	107	758273	5537698	27739568	33408633	30401439	39821583	61870504
Real ER (CPI-based), 1989=100	106.8	608.7	458.3	499.1	340.7	272.9	326.7	430.1
Real ER (PPI-based), 1989=100	107.1	319.1	192.9	170.1	137.5	118.5	138.7	181.3
PPP, UAH/ECU	0.0000055	0.0062291	0.0641774	0.31954	0.52012	0.60150	0.67335	0.80002
ERDI (ECU based)	1.36	8.46	6.00	6.03	4.46	3.51	4.11	5.37
Average monthly gross wages, UAH	0.0	1.7	15.3	80.6	137.8	156.2	167.5	191
Average monthly gross wages, ECU (ER)	336	32	40	42	59	74	61	44
Average monthly gross wages, ECU (PPP	457	273	239	252	265	260	249	239
GDP nominal, bn UAH	0.0	1.5	12.0	54.5	81.5	93.4	103.9	123.3
Employment total, 1000 persons	25277.3	23923.7	23025.0	23725.5	23231.8	22597.6	22348.7	22000
GDP per employed person, UAH	0.066	62.0	522.8	2297.8	3508.9	4131.6	4647.7	5604.5
GDP per empl. person, UAH at 1996 pr.	7500.0	5593.0	4480.7	3817.9	3508.9	3498.4	3477.1	3494.1
Unit labour costs, 1989=100	118.9	108564.6	1220070	7529835	14012241	15930145	17187060	19497593
Unit labour costs, ER adj., 1989=100	110.9	14.3	22.0	27.1	41.9	52.4	43.2	31.5
Unit labour costs, PPP adj., Austria=100	66.13	7.00	10.59	12.39	20.02	26.07	21.56	15.44
Austria								
Producer price index, 1989=100	102.9	103.1	104.5	104.8	104.8	105.2	104.6	103.7
Consumer price index, 1989=100	103.3	115.0	118.4	121.1	123.3	125.0	126.1	126.8
GDP deflator, 1989=100	103.4	115.1	118.4	121.1	122.7	124.6	125.3	126.2
Exchange rate (ER), ATS/ECU	14.47	13.60	13.51	13.03	13.26	13.78	13.88	13.76
ER, nominal, 1989=100	99.3	93.4	92.7	89.5	91.0	94.6	95.3	94.5
Real ER (CPI-based), 1989=100	100.4	93.6	92.2	90.3	92.0	96.3	97.2	96.7
Real ER (PPI-based), 1989=100	100.8	104.4	104.5	104.2	108.3	114.4	117.2	118.3
PPP, ATS/ECU	14.85	14.94	15.02	14.84	14.72	14.65	14.58	14.53
ERDI (ECU based)	0.97	0.91	0.90	0.88	0.90	0.94	0.95	0.95
Average monthly gross wages, ATS	22252	26039	26908	27911	28430	28624	29369	30044
Average monthly gross wages, ECU (ER)	1538	1914	1992	2142	2144	2077	2115	2183
Average monthly gross wages, ECU (PPP	1499	1743	1791	1881	1931	1954	2015	2067
GDP nominal, bn ATS	1813.5	2125.3	2237.9	2328.7	2453.2	2522.2	2610.9	2685.9
Employment total, 1000 persons	3344.6	3446.0	3451.8	3439.5	3415.4	3424.5	3446.6	3477.6
GDP per employed person, ATS	542217	616744	648328	677046	718271	736516	757529	772343
GDP per empl. person, ATS at 1996 pr.	643289	657330	671733	685848	718271	725064	741427	750671
Unit labour costs, 1989=100	103.0	117.9	119.3	121.2	117.8	117.5	117.9	119.1
Unit labour costs, ER adj., 1989=100	103.7	126.3	128.6	135.4	129.4	124.2	123.7	126.1
Unit labour costs, PPP adjusted	0.42	0.51	0.52	0.55	0.53	0.51	0.50	0.51

ER = Exchange Rate, PPP = Purchasing Power Parity, ERDI = Exchange Rate Deviation Index (all in terms of national currency per ECU). Benchmark PPPs for 1996 were estimated from purchasing parity standards for OECD (28) average and extrapolated with GDP price deflators.

Sources: BENCHMARK RESULTS OF THE 1996 EUROSTAT-OECD COMPARISON BY ANALYTICAL CATEGORIES, OECD, 1999; National statistics; WIFO; WIIW estimates.

Table A/3

Wages, productivity and unit labour costs (ULCs), 1990-1999

annual changes in %

	1990	1993	1994	1995	1996	1997	1998	1999 prelim.
Czech Republic								
Exchange rate (ER), CZK/ECU	37.9	-6.9	-0.1	0.7	-0.9	5.3	1.0	2.0
Real ER (CPI-based)	31.2	-22.0	-7.2	-4.3	-7.0	-1.0	-7.8	0.9
Real ER (PPI-based)	38.0	-13.8	-3.1	-3.0	-3.3	2.3	-2.7	2.0
Average gross wages, CZK	3.7	25.3	18.5	18.5	18.4	10.5	9.4	8.0
Average gross wages, real (PPI based)	-0.6	14.7	12.6	10.2	13.1	5.3	4.3	6.9
Average gross wages, real (CPI based)	-5.5	3.7	7.8	8.6	8.8	1.8	-1.2	5.8
Average gross wages, ECU (ER)	-24.8	34.5	18.7	17.7	19.4	5.0	8.3	5.9
Employment total	-1.0	-1.6	0.8	2.6	0.7	-1.9	-1.5	-3.6
GDP per empl. person, CZK at 1996 pr.	10.1	1.7	1.5	3.2	3.1	2.3	-0.8	3.3
Unit labour costs, CZK at 1996 prices	-5.8	23.1	16.8	14.8	14.8	8.0	10.3	4.6
Unit labour costs, ER (ECU) adjusted	-31.7	32.2	16.9	14.0	15.9	2.6	9.2	2.5
Hungary								
Exchange rate (ER), HUF/ECU	23.7	5.3	16.1	30.3	17.5	10.3	14.2	4.9
Real ER (CPI-based)	0.2	-13.1	-0.2	5.4	-2.9	-4.9	1.1	-3.7
Real ER (PPI-based)	5.8	-3.9	6.6	4.8	-1.4	-6.5	3.8	0.9
Average gross wages, HUF	27.2	21.9	22.6	16.8	20.4	22.3	18.3	14.0
Average gross wages, real (PPI based)	4.3	10.0	10.1	-9.4	-1.1	1.6	6.3	8.6
Average gross wages, real (CPI based)	-1.3	-0.5	3.2	-8.9	-2.6	3.4	3.5	3.6
Average gross wages, ECU (ER)	2.8	15.8	5.6	-10.4	2.5	10.8	3.6	8.7
Employment total	-1.9	-6.3	-2.0	-1.9	-0.8	0.0	1.4	4.1
GDP per empl. person, HUF at 1996 pr.	-1.7	6.0	5.0	4.5	2.2	4.6	3.4	0.4
Unit labour costs, HUF at 1996 prices	29.4	15.0	16.8	11.7	17.8	16.9	14.4	13.5
Unit labour costs, ER (ECU) adjusted	4.6	9.2	0.6	-14.3	0.3	5.9	0.1	8.2
Poland								
Exchange rate (ER), PLN/ECU	658.5	19.9	27.2	16.3	7.7	9.7	5.9	7.8
Real ER (CPI-based)	15.5	-10.4	-1.7	-5.7	-8.2	-2.6	-4.3	1.5
Real ER (PPI-based)	9.6	-8.1	3.7	-3.9	-2.1	-0.3	-0.3	3.1
Average gross wages, PLN	397.9	34.8	34.5	31.6	26.5	21.9	15.7	10.6
Average gross wages, real (PPI based)	-31.1	2.1	7.3	4.9	12.6	8.6	7.8	4.7
Average gross wages, real (CPI based)	-27.4	-0.4	1.7	3.0	5.5	6.1	3.5	3.1
Average gross wages, ECU (ER)	-34.4	12.4	5.7	13.2	17.4	11.1	9.2	2.6
Employment total	-4.2	-2.4	1.0	1.8	1.9	2.8	2.3	-1.2
GDP per empl. person, PLN at 1996 pr.	-14.8	6.3	4.2	11.8	4.0	3.9	2.4	5.4
Unit labour costs, PLN at 1996 prices	484.0	26.7	29.1	17.7	21.7	17.3	12.9	5.0
Unit labour costs, ER (ECU) adjusted	-23.0	5.7	1.5	1.2	12.9	6.9	6.7	-2.6
Slovak Republic								
Exchange rate (ER), SKK/ECU	38.5	-1.8	5.4	1.4	-0.1	-1.2	4.3	11.4
Real ER (CPI-based)	31.0	-19.4	-5.0	-4.4	-3.6	-5.0	-1.2	1.8
Real ER (PPI-based)	37.9	-15.3	-2.3	-3.6	-2.1	-3.5	2.1	8.6
Average gross wages, SKK	4.1	18.4	17.0	14.3	13.3	13.1	8.4	7.5
Average gross wages, real (PPI based)	-0.7	1.0	6.1	4.9	8.8	8.3	5.0	3.8
Average gross wages, real (CPI based)	-5.7	-3.9	3.2	4.0	7.1	6.6	1.6	-2.7
Average gross wages, ECU (ER)	-24.8	20.6	11.0	12.8	13.5	14.5	4.0	-3.5
Employment total	-0.8	-0.1	-1.8	2.2	0.8	0.2	-0.4	-2.0
GDP per empl. person, SKK at 1996 pr.	-1.6	-3.7	6.7	4.7	5.7	6.3	4.9	4.3
Unit labour costs, SKK at 1996 prices	5.9	22.9	9.6	9.2	7.2	6.4	3.4	3.1
Unit labour costs, ER (ECU) adjusted	-23.5	25.2	4.0	7.7	7.3	7.7	-0.9	-7.5
Slovenia								
Exchange rate (ER), SIT/ECU	346.0	26.0	15.2	0.5	10.7	6.4	3.3	4.0
Real ER (CPI-based)	-28.5	-4.1	-2.7	-8.2	2.9	0.1	-3.3	-1.0
Real ER (PPI-based)	-5.1	4.8	0.0	-7.7	5.9	2.3	-1.5	2.8
Average gross wages, SIT	379.6	47.8	25.4	18.4	15.3	11.7	9.6	9.2
Average gross wages, real (PPI based)	-2.2	21.5	6.6	4.9	8.0	5.3	3.4	7.0
Average gross wages, real (CPI based)	-26.4	11.2	3.7	4.3	4.9	3.1	1.6	2.9
Average gross wages, ECU (ER)	7.5	17.3	8.9	17.8	4.1	5.0	6.1	5.0
Employment total	-3.9	-3.6	-1.3	-0.1	-0.5	0.2	0.2	1.3
GDP per empl. person, SIT at 1996 pr.	-0.9	6.7	6.7	4.2	4.0	4.4	3.7	2.5
Unit labour costs, SIT at 1996 prices	383.8	38.5	17.6	13.6	10.9	7.1	5.7	6.6
Unit labour costs, ER (ECU) adjusted	8.5	10.0	2.1	13.0	0.1	0.6	2.3	2.5

(Table A/3 contd.)

Table A/3 (contd.)

	1990	1993	1994	1995	1996	1997	1998	1999 prelim.
Bulgaria								
Exchange rate (ER), BGL/ECU	7.6	7.1	99.3	34.4	120.7	889.2	4.0	-0.8
Real ER (CPI-based)	-9.3	-37.3	3.9	-14.0	1.1	-14.7	-14.0	-0.1
Real ER (PPI-based)	-2.1	-15.6	15.9	-9.2	-2.0	-8.5	-10.0	-2.3
Average gross wages, BGL	37.8	57.8	53.5	53.2	74.4	865.6	46.5	12.0
Average gross wages, real (PPI based)	20.1	23.0	-12.6	-0.2	-24.2	-12.4	25.4	9.3
Average gross wages, real (CPI based)	11.3	-8.7	-21.7	-5.5	-21.8	-18.3	19.8	11.7
Average gross wages, ECU (ER)	28.1	47.4	-23.0	13.9	-21.0	-2.4	40.9	12.9
Employment total	-6.1	-1.6	0.6	1.3	0.1	-3.9	-1.6	-5.5
GDP per empl. person, BGL at 1996 pr.	-3.1	0.1	1.1	1.6	-10.2	-3.2	5.2	7.6
Unit labour costs, BGL at 1996 prices	42.3	57.7	51.8	50.7	94.2	897.9	39.3	4.1
Unit labour costs, ER (ECU) adjusted	32.3	47.3	-23.8	12.1	-12.0	0.9	33.9	5.0
Romania								
Exchange rate (ER), ROL/ECU	89.1	121.5	122.4	33.6	46.9	109.5	23.5	63.1
Real ER (CPI-based)	87.8	-37.1	-4.0	4.7	8.1	-16.1	-21.5	13.0
Real ER (PPI-based)	55.5	-15.5	-5.5	2.5	0.1	-15.5	-6.4	17.7
Average gross wages, ROL	10.4	208.1	131.9	54.8	51.7	98.4	60.3	44.0
Average gross wages, real (PPI based)	-13.0	16.3	-3.6	14.6	1.2	-21.5	20.3	2.9
Average gross wages, real (CPI based)	5.0	-13.5	-2.0	17.1	9.3	-22.1	0.8	-1.2
Average gross wages, ECU (ER)	-41.6	39.1	4.3	15.8	3.2	-5.3	29.9	-11.7
Employment total	0.2	-3.4	-2.2	-2.8	-3.2	-2.5	-2.0	-6.0
GDP per empl. person, ROL at 1996 pr.	-5.7	5.1	6.3	10.3	7.4	-4.5	-3.4	1.7
Unit labour costs, ROL at 1996 prices	17.1	193.2	118.2	40.4	41.2	107.8	66.1	41.6
Unit labour costs, ER (ECU) adjusted	-38.1	32.4	-1.9	5.0	-3.9	-0.8	34.5	-13.2
Croatia								
Exchange rate (ER), HRK/ECU	346.0	1115.1	71.5	-4.7	0.7	2.3	2.5	6.2
Real ER (CPI-based)	-34.4	-24.0	-11.3	-3.1	-0.6	0.7	-1.9	3.0
Real ER (PPI-based)	-16.2	-23.8	-1.4	-1.9	1.4	2.0	4.9	4.6
Average gross wages, HRK	481.9	1434.9	154.1	34.0	12.3	13.1	12.6	10.0
Average gross wages, real (PPI based)	4.7	-4.8	43.1	33.0	10.8	10.6	14.0	7.2
Average gross wages, real (CPI based)	-18.0	-5.1	28.6	31.3	8.5	9.2	6.5	5.6
Average gross wages, ECU (ER)	30.5	26.3	48.2	40.5	11.6	10.6	9.8	3.6
Employment total	-3.1	-2.3	-0.7	-1.4	-6.2	-1.4	5.6	-3.0
GDP per empl. person, HRK at 1996 pr.	-2.6	-5.8	6.6	8.3	13.0	8.0	-3.0	1.3
Unit labour costs, HRK at 1996 prices	497.4	1529.9	138.5	23.7	-0.6	4.7	16.1	8.6
Unit labour costs, ER (ECU) adjusted	33.9	34.1	39.1	29.7	-1.3	2.4	13.2	2.2
Macedonia								
GDP deflator	.	400.5	127.6	17.1	2.9	3.3	1.4	-1.0
Exchange rate (ER), MKD/ECU	346.9	306.6	87.2	-3.7	1.8	12.8	7.9	3.3
Real ER (CPI-based)	-33.0	-11.0	-16.1	-13.9	1.7	12.1	9.2	5.4
Real ER (PPI-based)	-5.5	14.8	1.0	-4.7	4.3	10.4	4.9	5.7
Average net wages, MKD	461.3	495.6	105.0	10.7	2.8	2.8	3.7	2.5
Average net wages, real (PPI based)	13.7	66.2	8.3	5.7	3.1	-1.4	-0.4	3.8
Average net wages, real (CPI based)	-19.4	28.9	-10.1	-4.5	0.5	0.2	3.8	3.5
Average net wages, ECU (ER)	25.6	46.5	9.5	14.9	0.9	-8.9	-3.9	-0.8
Employment total	-1.5	-5.5	-5.3	-9.5	-4.4	-5.4	-3.0	1.0
GDP per empl. person, MKD at 1996 pr.	.	4.5	3.6	9.3	5.9	7.3	6.1	1.7
Unit labour costs, MKD at 1996 prices	.	470.1	97.9	1.3	-2.9	-4.2	-2.3	0.8
Unit labour costs, ER (ECU) adjusted	.	40.2	5.7	5.2	-4.7	-15.1	-9.5	-2.4
Russia								
Exchange rate (ER), RUB/ECU	7.2	248.5	114.8	126.2	12.6	-1.4	69.1	137.2
Real ER (CPI-based)	6.3	-63.8	-46.1	-21.2	-22.2	-12.4	34.0	29.0
Real ER (PPI-based)	8.7	-66.2	-49.8	-30.3	-23.8	-12.5	59.7	49.9
Average gross wages, RUB	17.2	906.4	277.5	119.6	48.4	20.2	10.4	50.1
Average gross wages, real (PPI based)	13.8	-3.4	-13.6	-34.7	-1.6	4.6	3.1	-6.1
Average gross wages, real (CPI based)	11.3	3.4	-7.2	-26.2	0.4	4.7	-13.5	-19.2
Average gross wages, ECU (ER)	9.3	188.8	75.7	-2.9	31.8	21.9	-34.7	-36.7
Employment total	0.2	-1.7	-3.3	-3.0	-0.7	-2.0	-1.5	2.1
GDP per empl. person, RUB at 1996 pr.	-3.2	-7.2	-9.7	-1.2	-2.7	2.9	-3.1	-0.5
Unit labour costs, RUB at 1996 prices	21.1	984.2	317.9	122.1	52.4	16.8	14.0	50.9
Unit labour costs, ER (ECU) adjusted	12.9	211.1	94.6	-1.8	35.4	18.4	-32.6	-36.4

(Table A/3 contd.)

Table A/3 (contd.)

	1990	1993	1994	1995	1996	1997	1998	1999 prelim.
Ukraine								
Exchange rate (ER), UAH/ECU	7.2	1873.8	630.3	400.9	20.4	-9.0	31.0	55.4
Real ER (CPI-based)	6.8	-63.5	-24.7	8.9	-31.7	-19.9	19.7	31.6
Real ER (PPI-based)	7.1	-58.1	-39.6	-11.8	-19.1	-13.8	17.0	30.8
Average gross wages, UAH	14.7	2334.7	800.3	425.9	71.0	13.3	7.2	14.0
Average gross wages, real (PPI based)	9.7	-48.9	-27.1	-10.7	12.4	5.2	-5.3	-5.0
Average gross wages, real (CPI based)	9.4	-55.5	-9.1	10.3	-5.1	-2.2	-3.0	-4.4
Average gross wages, ECU (ER)	7.0	23.4	23.3	5.0	42.0	24.6	-18.1	-26.6
Employment total	-0.5	-2.3	-3.8	3.0	-2.1	-2.7	-1.1	-1.6
GDP per empl. person, UAH at 1996 pr.	-3.6	-12.2	-19.9	-14.8	-8.1	-0.3	-0.6	0.5
Unit labour costs, UAH at 1996 prices	18.9	2672.6	1023.8	517.2	86.1	13.7	7.9	13.4
Unit labour costs, ER (ECU) adjusted	10.9	40.5	53.9	23.2	54.5	24.9	-17.6	-27.0

Sources: National statistics and WIIW estimates.

Sándor Richter

The EU enlargement process after Helsinki: A political gesture towards countries in the 'second wave'

At its meeting in Helsinki, the European Council did away with the division of the candidate countries into two different groups, which had been set up when the accession negotiations began on 30 March 1998. From the beginning of this year Bulgaria, Latvia, Lithuania, Romania and Slovakia have, at least theoretically, the chance of acceding to the EU at the same time as or even earlier than the Czech Republic, Estonia, Hungary, Poland and Slovenia.[1] This change affects three discrete groups of countries: the former 'second wave' countries which have now been invited to join the first league; the former 'first wave' countries which have now lost their privileged position; and finally the 'left outs', those countries which have received no invitation to join the European Union, yet whose political aspirations, trade intensity, financial and other economic relations with the EU qualify them as potential candidates for EU membership at some time in the remote or not so remote future.

The unification of the two groups can be best interpreted as a political gesture. It bears little practical significance for the EU, except that a number of new negotiating teams will have to be set up. Most probably, the change involved will not yield any important concessions relating to the economic criteria of accession. From the standpoint of the EU one possible interpretation of the changes involved is that the EU has perhaps changed its tactical approach: unlike the earlier tactic of being banned to the 'second wave', the countries involved will be encouraged to make every effort to catch up. The trust now placed in those countries should pay off in terms of increased efforts; in brief, the carrot has replaced the stick.

For the group of countries in the former 'second wave' the merger of the two groups is a sort of present. The governments in the countries involved can present the gesture made by the EU to their constituents as a political masterstroke: an acknowledgement of the progress the country has achieved in strengthening democracy and facilitating transition to a market economy. Apart from this, coming closer to EU membership at least in virtual terms may have a positive impact insofar as it may secure the governments concerned the external political support they need to initiate new measures and accelerate the ongoing reform of the economy, legal and institutional systems. The onset of accession negotiations marks a good reference point in the struggle to introduce reforms more rapidly in the course of the customary domestic political skirmishes between adherents and

[1] Cyprus and Malta are in the group of twelve candidate countries but as none of them belong to the region Central and Eastern Europe their case will not be discussed here, just as the special case of Turkey.

opponents of reform. Similarly, the EU may serve, more effectively than hitherto, as a scapegoat for many difficulties that these and other reforms may entail for various groups of the society. (The EU may thus join the IMF and the World Bank in this role.)

The other side of the coin is that until recently sitting in the second row accorded these countries a relatively comfortable position. Whereas the 'first wavers' were forever in the limelight, the actual degree of preparedness for membership on the part of the 'second wavers' attracted less attention. Now, that they have lumped together in one group with the former 'first wavers', their economic performance and maturity for membership will be compared more frequently with those countries and more often than not the outcome may be unfavourable for the former 'second wavers'.

For the former 'first wavers' the change seems to be of limited importance. They enjoyed the advantage of being among the privileged few with whom accession negotiations had already begun. Though theoretically any of the former 'second wavers' may accede earlier than one or more of the 'first wavers', this is unlikely. As negotiations with the former 'first wavers' are at an advanced stage, even if the former 'second wavers' were to display better economic performance or greater readiness to introduce institutional reforms and stipulations of the acquis, this may not make up for the delay in starting the negotiations. Consequently, the division between the two groups will persist, even if only tacitly. Only a severe and lasting economic and/or political crisis in one or more of the countries in the 'first wave' may lead to their losing the initial advantage of an early start that they had over the 'second wavers'.

In the longer term, the beneficiaries of the Helsinki decision may well be those countries that have been left out: Albania, Bosnia Herzegovina, Croatia, Macedonia, Yugoslavia, and some of the successor states to the former Soviet Union. These 'left outs' enjoy intense economic relations with the EU but none of them has entered into an association agreement with the EU nor do any of them have even remote prospects of becoming members of the Union. Now that ten accession candidates have all become member of the 'first wave', the 'second wave' category can be interpreted as an empty box for the present, with the possibility of it being re-introduced at any time. Seen in a five to ten-year context, the more fortunate (or capable) 'left outs' may thus be able to leapfrog straight into that category.

Months prior to the Helsinki summit, the EU offered a stabilization and association agreement (SAA) to five countries in South-East Europe. The offer was related to the Kosovo crisis and not to the enlargement in any respect. These SAAs may have the potential to provide a solution similar to the Europe Treaties already concluded with the ten CEEC candidates, offering prospects of accession at the end of a very long road.

The other sub-group of the 'left outs', some successor states to the former Soviet Union, except Russia, are in a different situation: the trade and co-operation agreements that some of these countries have concluded (or may conclude in the future) with the EU bear no comparison with the European Treaties or the planned SAAs to be offered to the sub-group in South-East Europe. For the countries in that particular sub-group, the political, security and economic context of the whole issue is much more complicated in both global and local terms owing to the myriad uncertainties surrounding Russia's political and economic aspirations and opportunities in the future. Apart from the uncertainties related to Russia, this sub-group is too heterogeneous even to expect being treated in a standard and consistent manner by the EU. Anyhow, the very fact that the merger of the accession candidates into one group was politically motivated lends some hope to the latter countries. Notwithstanding their poor economic record, they can harbour the hope that the EU will conjure up some sort of 'carrot' for them so that they do not lose heart.[2]

[2] For a discussion on the future of EU relations with the 'left outs' in South-East Europe and the former Soviet Union, please visit the website on EU eastern enlargement run by the WIIW. In the recently started All-Round Inquiry pages http://eu-enlargement.org/discuss/ the following question is posed to the expert community: 'From the year 2000 on the EU will open accession negotiations with those eastern applicant countries that were left out from the first round of these talks. In the wake of this change how do you see the prospects, necessity and possibility of increasing the circle of EU applicant countries by further countries from the Balkans and the former Soviet Union?'. Answers and comments are available at the URL mentioned above.

Additional information on the relations between the EU and countries in South-East Europe is available in The WIIW Balkan Observatory at the URL: http://www.wiiw.ac.at/balkan/

COUNTRY REPORTS

Anton Mihailov

Bulgaria: Post-Kosovo recovery

The Bulgarian economy grew unexpectedly fast in the third quarter of 1999 (quarterly GDP increased by 4.5% over the same quarter of 1998) bringing the GDP growth figure for the first three quarters of the year to 2.0%. This piece of good news came on top of the EU decision in December to open accession negotiations with Bulgaria. This notwithstanding, some chronic problems continue to plague the economy, leaving little room for unconditional optimism as regards the outlook.

The very high rate of GDP growth in the third quarter came as a surprise to all observers; it exceeded even the (usually quite optimistic) government forecasts. Some favourable changes in external and domestic demand in the post-Kosovo period seem to have played the most important role for this upsurge. The start of reconstruction works in Kosovo resulted in the emergence of a new lucrative market in the region and gave an impetus to some local suppliers (in particular of construction materials). Since the end of the conflict Bulgarian suppliers of fuels have also benefited from a massive surge of deliveries to Serbia. The strengthening of West European import demand in the course of the year also supported the revival of some Bulgarian exports. Domestic demand factors contributed to the output rise as well. In particular, the strong recovery of investment seems to have been an important growth-enhancing factor: fixed investment in the first three quarters of the year rose by almost 30% compared to the same period of 1998 (mostly due to the surge in public investment in infrastructure projects).

Still, some doubts of an upward bias of the quarterly figures remain. As follows from the reports of the National Statistical Institute (NSI), the adjustments due to the estimates of informal economic activities account for a large and increasing share of the reported GDP. While the NSI claims that it is capable of capturing an ever increasing share of these informal activities – thus improving the overall statistical coverage of economic activity – the problem is that these adjustments are only added to the current period estimates while the estimates of previous periods are not revised.

In view of the reported growth in output, the recent rise in unemployment is rather confusing: within a period of just five months (between June and November) the rate of unemployment increased from 12.8% to 15.6%. In fact during the whole transition decade since 1990 there has never been a period of such rapid rise in unemployment. These numbers cast further doubts as regards the reliability of the GDP figures as it is somewhat difficult to reconcile the surge in unemployment with the reported output growth figures. The developments in the labour market most likely reflect the intensification of the process of liquidation and closure of inefficient state-owned firms; however, the speed of the process remains somewhat of a puzzle. Some observers have related the rise in unemployment with the ongoing reform in the social security and pension systems which imply a certain increase in labour costs starting from 2000, in particular. It has been suggested that since the announcement of these changes, the private sector – which before that was accommodating for the losses in public sector employment (the latter mostly resulting from the restructuring of state-owned enterprises) – has been reluctant to hire new labour.

Despite the high reported rate of GDP growth, the manufacturing industry remained deeply depressed. Both in the second and in the third quarters real industrial sales were declining by a rate almost 10% year-on-year, and during the first three quarters of 1999 gross industrial production dropped by some 14% year-on-year. Although some signs of deceleration of the output decline emerged in the last quarter, the output figures for the year will remain deeply in the red. The notable deterioration in the trade and current account balances in 1999, mostly as a result of a sharp drop in exports, is another source of concern. In the third quarter there was a certain recovery in exports (by some 5% over the same quarter of 1998) accompanied by the revival of output. This, however, did not bring about a reversal in the widening trade deficit, which is likely to come close to 10% of GDP for the year as a whole. Conversely, the current account deficit improved slightly in the third quarter; however, its 1999 dynamics is difficult to analyse due to a series of methodological changes introduced in the course of the year.

Notwithstanding this, the financing of the current account deficit does not seem to pose any serious problems in the short run thanks to the raising of additional sources of official aid. Apart from a balance-of-payments support loan of EUR 100 mn, at the end of December the EU granted Bulgaria a further EUR 125 mn to support its accession efforts. Also in December the World Bank approved a new structural adjustment (FESAL-2) loan worth USD 100 mn (disbursed in the same month) providing further assistance for the restructuring of the enterprise, banking and energy sectors. Financing from the three-year IMF programme is on track – despite delays in implementation – with half of the loan (totalling SDR 627.6 mn) already disbursed. Thanks to the extensive official disbursements, forex reserves were growing in the course of 1999 and by the end of the year came close to USD 3 bn, which is historically a record level. As official aid is likely to continue to flow in, there does not appear to be a short-run problem in the servicing of the foreign debt (debt service due amounts to USD 900 mn in 2000 and to USD 1200 mn in 2001).

Privatization notably gained momentum in 1999 and a number of large-scale deals were finalized in the second half of the year: the largest oil refinery, Heftohim, was sold to Lukoil (Russia); Zeevi Group (Israel) bought Balkan Airlines; the largest steel mill, Kremikovtsi, was sold to Daru Metals (a Bulgarian investor) while Voest-Alpine (Austria) acquired the copper mine Assarel-Medet. Two medium-sized state-owned banks were also sold to foreign investors: Société Generale of France acquired a 97.9% stake in Expressbank while Regent Pacific Group (registered in the Cayman Islands) purchased a 97.5% stake in Hebros Bank.

However, despite the marked progress and the efforts of the authorities, privatization is still behind schedule. The largest and most widely publicized deals that had nourished great expectation – the privatization of the Bulgarian Telecom and of Bulbank, the largest Bulgarian bank – brought the biggest disappointments. The Telecom deal, which – after a series of delays – was due to be finalized by the end of 1999, seems to be falling apart. The stumbling block is probably related to a package of additional concessions that the chosen strategic investor (the Greek–Dutch consortium OTE-KPN) has reportedly been trying to secure from the government as part of the deal. As to Bulbank, which the authorities had been hoping to sell to a major strategic foreign investor, the initial offer attracted only one bidder and the tender was cancelled; a second attempt is envisaged in 2000.

The 2000 budget was voted as planned in December, in line with the commitment of the government to finalize budgetary procedures before the start of the calendar year. The targeted consolidated budget deficit for 2000 is at 1.5% of GDP while the central budget deficit is envisaged to hit 2.3%. Some important pieces of tax-related legislation were also passed together with the budget package. The profit tax of large firms was reduced from 27% to 25% (small firms will continue to be taxed at 20%). Taking into consideration local and other taxes, the average effective profit tax rate for the large firms is expected to be reduced from 34.3% to 32.5%. As part of the reforms in the pension and the social security system, as of mid-1999 these contributions are being shared by the employers and employees; in 2000 the share of personal contribution will increase considerably. Some trade restrictions (such as export taxes on selected commodities) were eliminated and further steps to liberalize the foreign exchange regime were adopted (widening the range of unrestricted capital transactions).

In general, there has been a certain improvement in the short-term outlook for the Bulgarian economy. The unexpectedly strong recovery in the third quarter of 1999 has brought about hopes that the growth of GDP for the year as a whole might also turn out to be higher than previously expected (forecasts were revised downwards in the wake of the Kosovo war). However, it remains to be seen whether the upsurge in output will be sustained or whether it will remain a one-time event. Inflation seems to be in check despite a moderate hike in the second half of 1999. Despite the deterioration, the external balance does not raise concerns in the short term thanks to larger capital inflows. However, the Bulgarian economy relies on the 'life-support' system of official assistance; it has yet to face the test of self-sustained performance and it is not clear whether it is prepared for this.

Table BG

Bulgaria: Selected Economic Indicators*)

	1995	1996	1997	1998 [1]	1998	1999	1999	2000	2001
					January-September		estim.	forecast	forecast
Population, th pers., end of period	8384.7	8340.9	8283.2	8230.4	.	.	8185	.	.
Gross domestic product, BGL bn, nom.	880.3	1748.7	17055.2	21577.0	15702.7	16120.9	22000	23500	25200
annual change in % (real)	2.9	-10.1	-7.0	3.5	4.4	2.0	2.5	4	4
GDP/capita (USD at exchange rate)	1559	1189	1224	1484	.	.	1464	.	.
GDP/capita (USD at PPP - WIIW)	5365	4988	4822	5014	.	.	5218	.	.
Gross industrial production									
annual change in % (real)	4.5	5.1	-10.0	-12.7	-6.7	-14.1	-10	4	4
Gross agricultural production									
annual change in % (real)	16.0	-11.5	17.4	-1.1	.	.	.	.	.
Goods transport, public sector, mn t-kms	87210	79850	86543	75947	57523 [2]	59107 [2]	.	.	.
annual change in %	7.9	-8.4	8.4	-12.2	-12.2	2.8	.	.	.
Gross fixed capital form., BGL bn, nom. [3]	134.3	238.5	1841.0	2495.6	1777	2318	.	.	.
annual change in % (real) [3]	16.1	-21.2	-23.9	16.4	18.9	28.9	25	.	.
Construction output total									
annual change in % (real)	5.8	-14.0	-4.4	-15.4	.	.	.	.	.
Dwellings completed, units	6815.0	8099.0	7452.0	4942.0	.	.	.	.	.
annual change in %	-21.4	18.8	-8.0	-33.7	.	.	.	.	.
Employment total, th pers., average	3282.2	3285.9	3157.4	3106.2	.	.	.	.	.
annual change in %	1.3	0.1	-3.9	-1.6	.	.	.	.	.
Employees in industry, th pers., average [4]	770.4	728.1	838.7	778.8	787.6	710.3	701.3 [5]	.	.
annual change in % [4]	-5.5	-5.5	-2.7	-7.1	.	-9.8	-10.3 [5]	.	.
Unemployed reg., th, end of period	423.8	478.5	523.5	465.2	410.7	542.8	610.6	650	600
Unemployment rate in %, end of period	11.1	12.5	13.7	12.2	10.7	14.2	16	17	16
Average gross monthly wages, BGL [4]	7597	13965	127909	187438	174234	195635	197090 [5]	.	.
annual change in % (real, gross) [4]	-5.5	-17.6	-18.3	19.8	20.6	13.5	12.2 [5]	.	.
Retail trade turnover, BGL bn [6]	410.4	723.7	5469.3	6408.5	4521.7	4485.0	.	.	.
annual change in % (real) [6]	2.7	-8.4	-34.9	2.4	3.7	-1.4	-6.5 [5]	.	.
Consumer prices, % p.a.	62.1	123.0	1082.3	22.3	30.4	-1.1	0.3	3	3
Producer prices in industry, % p.a.	53.4	130.0	1002.8	16.9	23.9	1.2	.	.	.
Central government budget, BGL bn [7]									
Revenues	197.3	350.0	2983.3	4245.6	3196.8	3818.7	9644 [8]	5138 [9]	.
Expenditures	255.2	540.8	3650.0	3930.8	2754.7	3127.3	9869 [8]	5677 [9]	.
Deficit (-) / surplus (+)	-57.9	-190.9	-666.7	314.7	442.1	691.4	-225 [8]	-540 [9]	.
Deficit (-) / surplus (+), % of GDP	-6.6	-10.9	-3.9	1.5	2.8	4.3	-1.0 [8]	-2.3 [9]	.
Money supply, BGL bn, end of period									
M1, Money	107.9	236.6	2290.3	2826.1	2279.1	2653.7	3005.5	.	.
Broad money	583.7	1310.3	6018.6	6597.2	6064.2	6669.3	7366.9	.	.
Base rate of NB % p.a., end of period	38.6	342.1	6.8	5.2	5.2	4.6	4.5	.	.
Current account, USD mn	-25.6	15.9	426.7	-375.6	-185.9	-453.1	-550	-600	-500
Gross reserves of NB excl. gold, USD mn	1236.4	483.4	2121.0	2679.4	2400.6	2531.6	2892.0	.	.
Gross external debt, convert. curr.,USD mn	10148.0	9601.6	9760.2	10241.6	9943.2	9702.1	.	.	.
Exports total, fob, USD mn [10]	5354.7	4890.2	4939.7	4300.3	3165.4	2736.6	3800	4200	4400
annual change in %	34.4	-8.7	1.0	-12.9	-14.4	-13.5	-12	11	5
Imports total, cif, USD mn [10]	5657.6	5073.9	4932.0	4979.1	3603.1	3745.8	4900	5000	5100
annual change in %	35.2	-10.3	-2.8	1.0	2.8	4.0	-2	2	2
Average exchange rate BGL/USD	67.2	175.8	1676.5	1760.4	1792.9	1820.3	1836.1	.	.
Average exchange rate BGL/EUR (ECU)	86.8	191.7	1895.8	1972.3	1974.7	1955.8	1955.8	1955.8	1955.8
Purchasing power parity BGL/USD, WIIW	19.5	41.9	430.7	521.2	.	.	515.1	.	.

*) On 5 July 1999, the new Bulgarian lev was introduced (1 BGN = 1000 BGL). Data in this table are presented in 'old' BGL.
1) Preliminary. - 2) Excluding pipeline - 3) Based on GDP concept. - 4) Up to 1996 public sector only. - 5) January to November. - 6) Up to 1995 including public catering, from 1996 according to NACE classification. - 7) From 1999 and quaterly including some extrabudgetary funds and accounts. - 8) General government budget; surplus of cenral government budget would be 2.2% of GDP. - 9) Government draft budget. - 10) Converted from the national currency to USD at the official exchange rate.

Source: WIIW Database incorporating national statistics; WIIW forecasts.

Hermine Vidovic

Croatia: A difficult heritage

Croatia has undergone substantial political changes after the parliamentary elections held at the beginning of January 2000. The one-party government controlled by the Croatian Democratic Union (HDZ) – in office for almost ten years – was replaced by a broad coalition consisting of six parties, led by Social Democrats (SDP) and Liberals (HSLS). Apart from speeding up the integration process, e.g. the conclusion of an association (or similar) agreement with the EU, accession to the WTO and CEFTA, the new government headed by Ivica Racan (SDP) will have to come to grips with economic recession, mounting unemployment, poorly performing export industries, persistently high current account deficits and a growing debt service burden. In contrast, price and exchange rate stability has been maintained for almost six years.

The real GDP decline that had started in the final quarter of 1998 continued during the first nine months of 1999. Over that period Croatia's GDP fell 1% against the same pre-year period, with private consumption and public consumption down 4.8% and 1.4% respectively. The decline of industrial production slowed down somewhat in the second half of 1999, in the year as a whole output fell by 1.4%. Energy production grew by 7%, while manufacturing, accounting for 84% of total industrial output, dropped by 2.9%. Only a few branches were doing well, e.g. pulp, paper and paper products, coke, refined petroleum products and nuclear fuel, tobacco products and other transport equipment (mainly shipbuilding). The branches hit hardest by output drops were wood and wood products, textiles and leather. Labour productivity increased as layoffs continued.

Enhanced earnings from privatization in the final quarter of the year provided a substantial relief for the budget. With these receipts the general government came close to the targeted deficit of 1% to GDP in 1999. However, if deducting privatization earnings from current revenues, the general government deficit widened considerably, to an estimated 5-6% of GDP. Payment arrears in the enterprise sector rose from month to month and reached a record level of HRK 25.3 bn in November, affecting 30,000 companies with 170,000 persons employed.

In 1999 the Croatian currency depreciated by 5% against the German mark; this is somewhat less than in 1998, when it was 6.4%. In the first eleven months of 1999 the real effective exchange rate of the Croatian kuna depreciated by 6.1% (deflated with the retail price index) and by 5.1% (deflated with the PPI). The export performance could not benefit from the slight improvement in competitiveness due to depreciation and productivity gains. Instead, the foreign trade volume shrank considerably in 1999, with exports and imports down 8% and 9.2% respectively during the first eleven months of the year. The trade deficit narrowed to USD 3.2 bn, from USD 3.6 bn in the same 1998 period. Exports fell most pronouncedly to Germany (-13%) and Bosnia and Herzegovina (-16%), Croatia's main export destinations after Italy. The reasons for the poor foreign trade results are manifold; similar to other transition countries, Croatia suffered from the weak economic climate in the EU, but also from the absence of preferential trade agreements with that area. The contraction of trade with Bosnia and Herzegovina has been mainly caused by the erection of trade barriers between the two countries. Thanks to the lowering of the trade deficit, the current account deficit fell by about one third, to USD 604 mn in the first three quarters of 1999, from USD 900 mn in the same period one year earlier. In the January–September period the surplus in services trade was 14.5% lower than in the corresponding 1998 period. This was due to lower earnings from tourism, but also to a substantial decline in receipts from transportation in the aftermath of the Kosovo conflict. In 1999 as a whole the current account deficit to GDP ratio equalled an estimated 7% and remained at the same level as one year earlier.

Having reached a record level of USD 9.3 bn in September 1999, the growth of Croatia's external debt came to a halt (at least temporarily) in October, when the debt figures reported by the National Bank were almost USD 400 mn lower than a month earlier. The reduction was made possible through the repayment of a six-month bridging loan raised from Dresdner Bank in May, after receiving privatization earnings from selling a part of Croatian Telecom (HT). By the end of 1999 the external debt reached an estimated 40% of the projected GDP. In the three years to come, Croatia will face a heavy debt service burden (principal and interest repayments), ranging from USD 1.7 bn in both 2000 and 2001 to USD 1.4 bn in 2002. The newly appointed minister of finance, Mr. Crkvenac, has announced to enter into negotiations with the IMF on a new stand-by arrangement soon.

Total employment fell 3.4% during the first eleven months of 1999. The number of registered unemployed increased every month, with the average registered unemployment rate rising to 20.8% in December, up from 18.6% in the corresponding month a year earlier. Despite the mounting problems on the labour market, net wages increased by 10.2% in real terms in the January–November period, gross wages by 5.9%. Wage rises are to a large part the result of generous wage concessions to the public sector made by the former government in an attempt to regain losing confidence prior to the elections.

In the last quarter of 1999 the privatization of huge state-owned enterprises and banks started. After the sale of a 35% stake of Croatian Telecom (HT) to Deutsche Telekom at the beginning of October, in December a contract was signed to sell a 66.3% stake of Privredna Banka Zagreb (PBZ) worth EUR 301 mn to Banka Commerciale Italiana (BCI), Milan. Main projects ahead in 2000 are the privatization of Rijecka Banka and Splitska Banka and Croatia Osiguranje (insurer).

The new economic programme will reportedly consist of two parts: the first part is dedicated to the current year, while the second part covers the coming four-year term of office. According to representatives of the new government, it is envisaged to preserve the stability of prices and of the exchange rate; the 2000 annual inflation rate is anticipated at 3.5%, the GDP should grow by 2.5-3%. Public spending is planned to be cut by 5%, the central budget should be reduced by 17%, to HRK 42 bn. Transfers to the pension and health funds should be increased, while significant expenditure cuts are expected from the reduction of capital outflows to Bosnia and Herzegovina – which in the past were channelled through funds of the ministries of defence and reconstruction.

The programme is envisaged to be a combination of a shock therapy and a strategic part, which should provide a solution for the country's major economic problems, i.e. the budget, current account and poor export performance, the country's regional development, low production and employment.

Based on the announcements made by new the Croatian government officials, WIIW adheres to its earlier forecast. Taking into account the favourable economic climate in the EU, and assuming that there will be no devaluation of the kuna and there is some foreign exchange inflow from privatization, GDP may grow by about 1% in 2000. A continuation of the current exchange rate policy (which is strongly supported by the IMF) will allow to maintain the stability of the exchange rate and the inflation rate at 4-5%.

Table HR

Croatia: Selected Economic Indicators

	1995	1996	1997	1998	1998	1999	1999	2000	2001
					January-September		estim.	forecast	forecast
Population, th pers., mid-year	4669	4494	4573	4501	.	.	4500	.	.
Gross domestic product, HRK mn, nom.	98382	107981	122905	135645	102738	106320	140000	148000	159000
annual change in % (real)	6.8	6.0	6.5	2.5	5.0	-1.0	-2	1	2
GDP/capita (USD at exchange rate)	4029	4422	4362	4737	.	.	4376	.	.
GDP/capita (USD at PPP - WIIW)	5582	6325	6760	7109	.	.	7095	.	.
Gross industrial production									
annual change in % (real)	0.3	3.1	6.8	3.7	6.7	-2.8	-1.4	1	2
Gross agricultural production									
annual change in % (real)	0.7	2.0	4.0	10.2	.	.	.	.	.
Goods transport, public, mn t-kms	199730	213172	203428	170107	130932	108465	.	.	.
annual change in %	1.4	6.7	-4.6	-16.4	-14.0	-17.2	.	.	.
Investment outlays, HRK mn, nom. 1)	10474	18859	25838	27470	.	.	.	.	.
annual change in % (real)	-25.1	-14.1	.	.	.	.	.	.	.
Construction output, in effect.working time									
annual change in % (real)	-3.9	9.0	16.7	0.7	3.0	-6.4	.	.	.
Dwellings completed, units	7359	12624	12496	.	.	.	.	.	.
annual change in %	-24.2	71.5	-1.0	.	.	.	.	.	.
Employment total, th pers., average 2)	1417.4	1329.5	1310.9	1384.8	1387.1	1345.6	.	.	.
annual change in % 2)	-1.4	-6.2	-1.4	0.4	-0.2	-3.0	.	.	.
Employees in industry, th pers., average 3)	349.2	315.1	319.7	308.9	310.3	294.4	.	.	.
annual change in % 3)	-5.2	-9.8	-6.4	-3.4	-3.5	-5.1	.	.	.
Unemployed reg., th, end of period	249.1	269.3	287.1	302.7	286.8	326.5	341.7	.	.
Unemployment rate in %, end of period	15.1	15.9	17.6	18.6	17.1	19.6	20.8	21	22
Average gross monthly wages, HRK	2887	3243	3668	4131	4066.0	4482.0	.	.	.
annual change in % (real, net)	40.2	7.2	12.3	6.0	5.6	10.9	.	.	.
Retail trade turnover, HRK mn 4)	26054.9	29412.4	34613.6	35894.3	26764.2	25737.9	.	.	.
annual change in % (real) 4)	12.5	3.4	14.9	-0.4	1.8	-7.6	-6	.	.
Retail prices, % p.a.	2.0	3.5	3.6	5.7	5.6	4.0	4.2	4	4
Producer prices in industry, % p.a.	0.7	1.4	2.3	-1.2	-0.8	1.8	2.6	.	.
Central government budget, HRK mn									
Revenues	27981	31368	33846	43809	33102	29276	.	.	.
Expenditures	28696	31502	35006	42552	31908	33172	.	.	.
Deficit (-) / surplus (+)	-715	-134	-1160	1257	1194	-3896	.	.	.
Deficit (-) / surplus (+), % GDP	-0.7	-0.1	-0.9	0.9	1.2	-3.7	.	.	.
Money supply, HRK mn, end of period									
M1, Money	8235	11369	13731	13531	13852	13559	.	.	.
Broad money	24623	36701	50742	57340	56966	55317	.	.	.
Discount rate % p.a., end of period	8.5	6.5	5.9	5.9	5.9	7.9	7.9	.	.
Current account, USD mn	-1451.5	-1147.5	-2342.6	-1551.2	-901.1	-603.7	-1400	-1500	-1700
Gross reserves of NB excl. gold, USD mn	1895.2	2314.0	2539.0	2815.6	2757.3	2815.8	3024.8	.	.
Gross external debt, USD mn 5)	3660.9	4808.4	6661.6	8488.7	7838.7	9263.1	.	.	.
Exports total, fob, USD mn	4632.7	4511.8	4170.7	4541.1	3348.8	3158.6	4200	4400	4600
annual change in %	8.7	-2.6	-7.6	8.9	6.6	-5.7	-8	5	5
Imports total, cif, USD mn	7509.9	7787.9	9104.0	8383.1	6244.7	5640.8	7600	8000	8200
annual change in %	43.6	3.7	16.9	-7.9	-2.0	-9.7	-9	5	2
Average exchange rate HRK/USD	5.23	5.43	6.16	6.36	6.42	7.03	7.11	7.2	.
Average exchange rate HRK/EUR (ECU)	6.76	6.80	6.96	7.14	7.07	7.56	7.58	.	.
Purchasing power parity HRK/USD, WIIW	3.77	3.80	3.98	4.24	.	.	4.39	.	.

1) Legal entities. - 2) From 1998 including persons employed at the Ministry of Defence and Ministry of Internal Affairs. - 3) From 1997 according to NACE classification. - 4) NACE classification from 1996. - 5) Up to 1995 excluding portion of debt of the former Yugoslav Federation.

Source: WIIW Database incorporating national statistics; WIIW forecasts.

Josef Pöschl

Czech economy: Bouncing back?

The Czech economy is recovering from a severe recession. For more than a year, from the first quarter of 1998 up to that of 1999, GDP growth rates were negative; only in the second and third quarters of 1999 did they turn positive once again. This more recent development may well indicate a tendency towards recovery, albeit rather feeble hitherto. The pattern of decline and recovery was in line with the generally observable business cycle, with the exception of growth rates which were much lower than those in comparable countries: synchronous transitional recession, a specifically Czech feature, caused them to shift downwards. Table I shows quarterly growth rates and allows for an interpretation of their cyclical behaviour.

Table I

Contributions of GDP components to overall growth (in percentage points)

Quarterly GDP data (year-on-year), at constant 1995 prices, 1998-99

	1998				1999		
	Q1	**Q2**	**Q3**	**Q4**	**Q1**	**Q2**	**Q3**
Private consumption	-1.2	-3.9	-0.4	-0.7	0.4	0.7	0.8
Public consumption	-1.1	0.3	0.2	1.1	0.2	0.1	0.1
Gross fixed investment	-0.8	-1.8	-1.9	-0.2	-2.1	-2.0	-1.3
Change in inventories	-2.9	-0.2	-1.1	0.8	0.4	1.0	-1.4
Net export	5.3	3.7	0.6	-4.9	-3.1	0.6	2.6
Total: GDP growth rate	**-0.7**	**-1.9**	**-2.6**	**-3.9**	**-4.1**	**0.4**	**0.8**

Source: Own calculations.

As Czech exports and imports are rather high relative to GDP[1], their fluctuations exert a palpable influence on the aggregate growth rate. In the first half of 1998, in particular, significant improvements in net exports, i.e. a shrinking import surplus, protected the economy against even deeper recession, whereas a widening import surplus was the main reason for the alarming decline in GDP in the fourth quarter of 1998 and yet again in the

[1] According to the GDP concept, exports and imports contain both goods and services. If calculated at 1995 constant prices, exports from January to September 1999 make up 72% of GDP, with imports accounting for 78% in the same period. In a calculation based on current prices, both exports and imports over this period amount to about 62% of GDP.

first quarter of 1999[2]. In contrast to this, foreign trade results from April 1999 onwards showed an improvement once more and promoted GDP growth. The direction of the foreign trade impact can thus be seen to have changed twice – and that quite dramatically – within a short space of time. Two factors may have been responsible for these reversals.

One factor was the temporary downswing in the German business cycle in the aftermath of the East Asian and Russian crises – especially in the second half of 1998 up to the first few months of 1999. It hit Czech exports. The other factor was that in the course of 1998 the Czech koruna appreciated significantly: some 10% against the DEM[3]: This meant, vis-à-vis German products, a jump of approximately 10% in Czech producer prices and constituted an additional adverse effect on foreign trade results. The first half of 1999 brought about a partial reversal of the real appreciation mentioned above, which may have helped to re-establish a positive foreign trade impact on growth. Gradual appreciation set in again in May 1999, and at some point in time this could start to offset, at least partially, the positive effects of the improving international business climate. Over the first ten months of 1999, exports covered 95% of imports; in November, however, coverage was merely 87%.

In early 1999, the real exchange rate bounced back following repeated cuts in interest rates introduced by the Czech National Bank (CNB). Later in 1999, those cuts came more or less to a standstill. As things stand, a sudden major depreciation is not very likely: a fact conducive to capital inflow. The Czech koruna is currently under a certain degree of appreciation pressure. The expectations harboured by financial investors could well step up this pressure and nudge the exchange rate up to levels that are unsustainable from a current account point of view. To avoid such a situation developing, the CNB has tried to dampen appreciation expectations by signalling its readiness to intervene in order to combat high appreciation, as it has already demonstrated on several occasions.

In addition to foreign trade, gross fixed investment throughout the period 1998-1999 also had a major, permanently negative, impact on GDP growth. The Czech Republic has also suffered from transitional recession, and the negative fixed investment growth rates over the whole period (1998-99) reflect this fact. They were partly an outcome of the disruption suffered by the domestic financial system. For years local banks had been accustomed to providing established large-scale, loss-making enterprises and new wannabe

[2] This can be seen in Table I. For example 5.3, the net export figure for the first quarter of 1998, results from the following logic: all domestic demand positions are supposed to have remained at the level they had in the first quarter of 1997, while exports and imports are assumed to have moved as indicated in the GDP statistics. The GDP growth rate derived from these assumptions is 5.3%. This figure filters out the growth impact of foreign trade. All other figures in the table result from analogous calculations.

[3] In the second half of the year the real exchange rate, calculated using producer prices, was some 10% below the level in January 1998. The calculation is based on DEM, since in the period from January to September 1999 Germany absorbed 42% of total Czech exports, while accounting for 34% of Czech imports at the same time. The corresponding figures for the EU as a whole were 69% and 65%, respectively.

entrepreneurs, especially privatization-profiteers, with loans that never found their way back to the creditors and more often than not were, at least tacitly, never expected to do so. When in 1998, i.e. at a rather late juncture, the CNB introduced tougher banking regulations, the volume of new loans started to shrink drastically. A number of enterprises found themselves facing inordinate difficulties as they sought to finance raw material purchases or pay wages – not to mention funding purchases of new machinery and equipment. This was not so much the outcome of high interest rates – they were declining – but the impact of the new tougher banking regulations: In the ultimate analysis, the latter turned out to constitute 'non-tariff' barriers to loans.

A possibly even more important reason for the permanent decline in total gross fixed investment were the cancellations, reductions or postponements of state-funded investment projects. The poor GDP performance after 1996 implied correspondingly low budget revenues and provoked adjustments on the expenditure side. Fewer cuts were possible in the field of public consumption, as it funds the regular functioning of state institutions including the remuneration of employees in the public sector. Government decisions also had a massive influence on private consumption in another way: In 1998, major hikes in regulated prices had a negative impact on real incomes in the country. When the Social-Democrat minority government was faced with the decision whether to increase prices in 1999, it was quite adamant in its refusal to repeat the exercise, thus providing room for some growth in private consumption.

The recent signs of recovery as shown in the quarterly GDP figures are also apparent from monthly industrial production figures. The steepest decline in industrial output, over 12% year-on-year, was in December 1998, whereas from August 1999 onwards the corresponding percentage rates have always been positive[4]. Labour productivity, which even declined during the worst phase of the past recession, has started to rise again, and the corresponding rise in unit labour cost in EUR terms has come to a stop[5].

With a measure of good fortune, the recovery will last and even firm up somewhat. GDP growth could come close to 1.5% in 2000 and 2% in 2001. For several reasons it is improbable that the Czech Republic will soon display high GDP growth rates. First, this year the government has been more straightforward in dealing with increases in regulated prices; this will dampen private consumption once more. Secondly, in the previous year the government was repeatedly confronted with the threat of financial institutions or giant industrial enterprises verging on collapse. This was a sign of structural weakness, and related problems will call for major remedial efforts this year as well. Under these circumstances the government has no means of resuscitating state-funded investment

4 Czech industrial output figures suffer chronically from inconsistencies, a fact that reduces, at least to some degree, their reliability.

5 For a graphical presentation see the graphs in the overview article of this issue.

projects on a large scale. Thirdly, private gross fixed investment will recover only slowly, if at all, and then mainly on account of investments being effected in enterprises with foreign involvement. These investments will usually be related to the introduction of new labour-saving technologies. Even with some growth in gross fixed investment, future GDP growth will depend on whether foreign trade assumes the role of an engine of growth.

The biggest threat to recovery comes from a potential return of higher inflation rates. In 1998 and 1999 inflation disappeared completely, at least temporarily, especially where non-regulated consumer prices ('core inflation') and producer prices were concerned. This was mainly the result of a temporary decline in world market prices for fuel and food. Meanwhile, the situation has changed, oil prices have since surged to post-Gulf War highs. Czech inflation rates are still quite modest. In the event of a more pronounced re-emergence of inflation, say close to 5 percent in annual average, the CNB would most probably respond by raising interest rates, in this way putting the koruna under greater pressure to appreciate. The import surplus might thus increase again, so reducing or eliminating GDP growth.

The structural deficiencies of the Czech economy, one of the main reasons for poor growth performance over the past few years, will only disappear over time. Improvement has to come about in the business sector itself, although the government can facilitate things by assuring favourable preconditions. Privatizing the Czecho-Slovak Trading Bank (CSOB) several months ago was an important step, and recently the government decided to sell its shares in Ceská Sporitelna (Czech Savings Bank) to Erste Bank. The Komercní Banka (Commercial Bank) may follow in 2001. As a result, the loan business may gradually return to normal.

That notwithstanding, privatizing these major banks will lessen only some of the structural deficiencies. In order to provide a good institutional framework for economic activities, including reforming legislation, the court system and public administration, a comprehensive package of reforms is required. Among the economic and political elite awareness of the need for these measures has increased, but resistance to change is also unbroken. To all appearances, the government and senior civil servants have started placing emphasis on the design and promotion of such reform steps, in particular with a view to preparing for EU accession as well. However, under the given delicate political circumstances, nothing can be done without striking a compromise, while every step in the right direction tends to be time-consuming.

Table CZ

Czech Republic: Selected Economic Indicators

	1995	1996	1997	1998	1998	1999	1999	2000	2001
					January-September		estim.	forecast	forecast
Population, th pers., mid-year	10330.8	10315.4	10303.6	10294.9	10295.3	10282.7	10280	.	.
Gross domestic product, CZK bn, nom.	1381.0	1572.3	1680.0	1820.7	1355.3	1377.5	1850	1950	2060
annual change in % (real)	5.9	3.8	0.3	-2.3	-1.8	-0.9	-0.6	1.5	2
GDP/capita (USD at exchange rate)	5035	5615	5142	5479	.	.	5206	.	.
GDP/capita (USD at PPP - WIIW)	12194	13038	13370	13208	.	.	13374	.	.
Gross industrial production									
annual change in % (real) [1)]	8.7	2.0	4.5	3.1	6.4	-4.7	-3	2	2
Gross agricultural production									
annual change in % (real)	5.0	-1.4	-5.1	0.7	.	.	.	.	.
Goods transport, mn t-kms [2)]	35489	34396	63623	54411	.	.	.	.	.
annual change in %	4.4	-3.1	.	-14.5	.	.	.	.	.
Gross fixed capital form., CZK bn, nom. [3)]	442.4	500.6	506.9	501.4	332.7	311.7	.	.	.
annual change in % (real) [3)]	19.8	8.2	-4.3	-3.8	-5.3	-6.5	-5	0	2
Construction industry									
annual change in % (real)	8.5	5.3	-3.9	-7.0	-5.9	-7.8	.	.	.
Dwellings completed, units	12662	14037	15904	21245	12160	14051	.	.	.
annual change in %	-30.3	10.9	13.3	33.6	28.3	15.6	.	.	.
Employment total, th pers., average	5011.6	5044.4	4946.6	4873.4	4877.0	4708.0	.	.	.
annual change in %	2.6	0.7	-1.9	-1.5	-1.6	-3.5	.	.	.
Employment in industry, th pers., average	1628.1	1614.7	1605.5	1595.6	1604.0	1549.0	.	.	.
annual change in %	0.6	-0.8	-0.6	-0.6	-0.5	-3.4	.	.	.
Unemployed reg., th, end of period	153.0	186.3	268.9	386.9	350.7	469.8	487.6	.	.
Unemployment rate in %, end of period	2.9	3.5	5.2	7.5	6.8	9.0	9.4	11	12
Average gross monthly wages, CZK [4)]	8172	9676	10691	11693	11241	12200	.	.	.
annual change in % (real, gross)	8.7	8.9	2.0	-0.8	-2.5	6.2	.	.	.
Retail trade turnover, CZK bn	529.7	.	.	.	.	.	.	.	.
annual change in % (real)	4.8	12.1	-0.4	-7.1	-6.8	1.4	.	.	.
Consumer prices, % p.a.	9.1	8.8	8.5	10.7	11.8	2.2	2.1	3.5	3.5
Producer prices in industry, % p.a.	7.6	4.7	4.9	4.9	5.5	0.5	1.0	3	2
Central government budget, CZK bn									
Revenues	440.0	482.8	509.0	537.4	395.9	413.6	567.3	.	.
Expenditures	432.7	484.4	524.7	566.7	389.7	422.2	596.9	.	.
Deficit (-) / surplus (+)	7.2	-1.6	-15.7	-29.3	6.2	-8.6	-29.6	-30	-30
Deficit (-) / surplus (+), % GDP	0.5	-0.1	-0.9	-1.6	0.5	-0.6	-1.6	.	.
Money supply, CZK bn, end of period									
M1, Money	453.3	475.3	445.1	433.4	397.9	464.0	.	.	.
M2, Money + quasi money	1039.6	1120.5	1217.6	1280.8	1236.2	1336.8	.	.	.
Discount rate, % p.a., end of period	9.5	10.5	13.0	7.5	11.5	5.5	.	.	.
Current account, USD mn	-1369	-4292	-3211	-1336	-549	-167	-800	-1300	-1500
Gross reserves of NB incl. gold, USD mn	14023	12435	9774	12617	12358	12004	.	.	.
Gross external debt, convert. curr.,USD mn	16549	20845	21352	24047	24115	22535	.	.	.
Exports total, fob, USD mn [5)]	21646.8	21905.7	22784.6	26349.8	19419.2	19470.3	26870	29000	30600
annual change in % [6)]	19.9	1.2	4.0	15.6	17.2	0.3	2.0	8	6
Imports total, fob, USD mn [5)]	25252.2	27715.7	27176.6	28786.5	20849.8	20429.7	28890	31500	33200
annual change in % [6)]	39.5	9.8	-1.9	5.9	5.0	-2.0	0.4	9	5
Average exchange rate CZK/USD	26.55	27.15	31.71	32.27	33.14	34.44	34.57	35.6	36.0
Average exchange rate CZK/EUR (ECU)	34.31	34.01	35.80	36.16	36.53	37.05	36.88	36.0	36.0
Average exchange rate CZK/DEM	18.52	18.06	18.28	18.33	18.49	18.94	18.85	18.4	18.4
Purchasing power parity CZK/USD, WIIW	10.96	11.69	12.19	13.39	.	.	13.46	.	.

1) From 1996 new methodology. - 2) Up to 1996 public transport only. - 3) Based on GDP concept. - 4) Enterprises with more than 100, in 1992 to 1994 with 25 and more, from 1997 with 20 and more employees. - 5) Converted from the national currency to USD at official exchange rate; from 1995 new methodology of 1996. - 6) Up to 1995 based on old methodology.

Source: WIIW Database incorporating national statistics; WIIW forecasts.

Sándor Richter

Hungary: All's well that ends well . . . ?

The economic performance of Hungary did not give rise to too much optimism in the first months of 1999. External conditions seemed anything but favourable, from the business cycle in the EU to the uncertainties following the 1998 Russian crisis and due to the war in neighbouring Yugoslavia. Sharp deceleration of GDP growth (from 5.1% in the last quarter of 1998 to 3.3% in the first quarter of 1999), a soaring current account deficit and rapid accumulation of the public finance deficit, as well as floods and heavy rains put the government under pressure to undertake resolute measures to maintain stability.

By the end of 1999 the general picture of the Hungarian economy became much better. The GDP growth rate increased from quarter to quarter, attaining 4.4% in the third and certainly not less than that in the fourth quarter. Annual economic growth may have reached 4% or even slightly more. There was a gradual improvement in the current account deficit over the year, and finally the deficit for 1999 amounted to USD 2.07 bn only, less than the government target or any of the independent forecasts. The same gradual improvement, with a year-end rush, occurred in public finance and eventually both the central budget and the general government deficit remained below the original target. The latter may have amounted to about 3.9% of the GDP (target: 4%). In the last months of the year foreign investors turned again with increasing attention to the Budapest Stock Exchange and by the first days of 2000 the BUX surpassed its historically highest value registered back in April 1998. The inflow of FDI also remained considerable last year, thus non-debt-creating financing (FDI + equity portfolio investment) was 156% of the January–November current account deficit.

The spectacular turnaround compared to the beginning of the year 1999 can predominantly be explained by external factors: the upturn of the business cycle in the EU and especially in Germany (the former absorbed 75%, the latter alone 38% of all Hungarian exports) facilitated the export revival. The lag of import over export growth rates decreased over the year: in January–November the former amounted to 7.8%, the latter to 7.3% in current dollar prices. The modernization of the export structure carried on, with an increasing share of engineering products (55% of total exports). The increment in exports came predominantly from the same few multinationals which have been behind the rapid expansion of exports for the last couple of years. Their success, however, must be seen together with the continuing weak export performance in most of the 'rest' of the economy.

It is not easy to judge what role economic policy played in the turnaround. From spring onwards the government was widely criticized for not intervening to stop the increase of the budget deficit. In retrospect, this non-intervention may seem to have been a wise anti-cyclical policy to counterbalance the impact of lower foreign demand. However, we cannot really speak of a non-intervention. For political reasons (to avoid any similarity with the 1995 Bokros package) deliberately in silence, important corrective measures were made. State-initiated investments were postponed or cut, for the whole year they were 23% less than originally planned. Higher than expected revenues from sales of the Social Security Fund's assets and from concession fee from a mobile telephone tender also contributed to the good annual results. All in all, it is the government's merit that the deficit remained under control, but the anti-cyclical effects in question were confined to the first few months of the year and that cannot be regarded as the outcome of a conscious decision.

Concerning the main components of demand, the development of household consumption clearly indicates anti-cyclical effects, in as much as in the first two quarters its growth rate was 1 percentage point higher than that of the GDP, while in the third quarter, when GDP growth gained momentum (+4.4%), the increase of household consumption lagged slightly behind. Similar tendencies could be observed with gross fixed capital formation. Investments increased by 5.8% in January–September, but this modest rate is misleading, as it is the result of a sharp decline of state investment and continuing lively investment activity in the business sector, primarily in manufacturing. Contrary to the developments of these aggregates, net exports gained in importance from quarter to quarter.

CPI Inflation (annual average) dropped to 10.0% from 14.3% in 1998 but the December-to-December inflation was 11.2%, higher than the respective figure in 1998. Rising energy prices played a role in the slower than hoped for decrease of inflation last year. Monthly devaluation of the forint dropped from 0.6% in January to 0.4% in December. From January to December the Hungarian currency was devalued by about 5% vis-à-vis a basket of 70% EUR and 30% USD.

Despite the slowdown of economic growth, the number of employed increased by 3.5% in the first ten months; in the whole year the number of employed may have grown by about 100,000 persons. According to the Labour Force Survey, the unemployment rate dropped to 6.5% in 1999 compared to 7% a year earlier. The opposite tendency is indicated by data on registered unemployed, where the respective indicator was 9.6%, the same as last year. Productivity growth in industry remained strong: in January–November it amounted to 10%.

In early 2000 the international environment is much more favourable for the Hungarian economy than it was a year ago. Economic growth and consequently import growth will be stronger in the EU and especially in Germany than it was in 1999. The confidence of financial investors in the macroeconomic performance of the country seems to be firm. Inflation will be a central issue this year. The government planned 6-7% consumer price rises, the 2000 budget figures were calculated with the presumption of 6.3% CPI inflation.

Centrally set prices may not increase above 6%, the monthly devaluation rate of the forint will be reduced to 0.3% in April and likely to 0.2% some time in the second half of the year, concluding into 3.5-4% nominal devaluation of the forint in the whole year. The government projects an 8.5% nominal wage rise in the public sector, nevertheless this has only a limited influence on developments on wages in the private business sector.

The official inflation target for the year 2000 is too low. The government calculated with an oil price of USD 18/barrel while observers reckon with higher energy prices. End-1999 forecasts of Hungarian research institutes ranged between 7% and 9.2%, the WIIW expects 8.3%. If the wages in the private business sector, as likely, will accommodate to the expected inflation rather than to the official inflation target, this alone may lead to inflationary pressure through the higher wage bill, which in turn may either leave employees of the public sector with near-zero real wage growth. or the nominal wage target in the public sector will have to be adjusted in the course of the year. The WIIW reckons with 2.5-3% real wage growth in the whole economy at higher than the officially projected inflation.

Accelerating GDP growth (to 4-5%) will not conclude into accelerating consumption. Household consumption may increase by 3-4%, somewhat less than last year and lagging more behind the GDP growth rate than was the case in 1999. Higher growth of fixed investments and foreign demand will make up for this. The targets in public finance are very strict for 2000. Part of the 'rigour' withheld last year for political reasons was set free in the budget for 2000. The general government deficit is planned to amount to 3.5% of the GDP. This will be difficult to achieve, as significant 'one-off' revenues realized in 1999 will not be available this year. Higher than planned inflation may help to inflate the revenues while (non-interest) expenditures remain nominally unchanged but with smaller purchasing power; nevertheless the overall impact on the balance is hard to assess as the interest burden would probably be higher than calculated with. A longer-term consolidation of public finance is not in sight as outstanding reforms in health care, local governments, taxation, etc. are postponed or in delay.

Due to favourable external conditions, the WIIW expects 4-5% economic growth this year and assumes that it can likely be attained without substantial deterioration of the foreign balances. The forecast current account deficit of USD 2 to 2.2 bn will be more than compensated by non-debt generating inflow of capital. Inflation will be only somewhat lower than in 1999, and public finance remains a battlefield with a deficit to GDP ratio between 3.5% and 4%. The WIIW reckons with continuing favourable external conditions in the year 2001. This will help to maintain the momentum of export expansion. A slow catching up of the 'rest of the economy' with the modern 'islands' in the country may raise the GDP growth rate to 4.5-5.5%.

Table HU

Hungary: Selected Economic Indicators

	1995	1996	1997	1998	1998	1999	1999	2000	2001
					January-September		estim.	forecast	forecast
Population, th pers., end of period	10212.3	10174.4	10135.4	10091.8	10105	10059	10050	10010	10000
Gross domestic product, HUF bn, nom.	5614.0	6893.9	8540.7	10086.0	.	8293	11600	13000	14500
annual change in % (real)	1.5	1.3	4.6	4.9	5.1	3.9	4	4.5	5
GDP/capita (USD at exchange rate)	4367	4433	4504	4650	.	.	4865	.	.
GDP/capita (USD at PPP - WIIW)	8927	9339	10008	10647	.	.	11346	.	.
Gross industrial production									
annual change in % (real)	4.6	3.4	11.1	12.5	13.6	8.4	9	10	11
Gross agricultural production									
annual change in % (real)	2.6	6.3	-3.8	-2.1			.	.	.
Goods transport, mn t-kms 1)	23675	24874	24789	27144	19512	18937	.	.	.
annual change in % 1)	.	5.1	-0.3	9.5	14.3	-3.0	.	.	.
Gross fixed investment, HUF bn, nom.	1038.8	1337.6	1709.9	2137.9	1254.1	1431.0	.	.	.
annual change in % (real)	-5.3	5.2	8.5	12.7	14.1	5.8	7	9	10
Construction industry									
	-17.6	2.7	8.1	15.3	16.4	6.2	.	.	.
Dwellings completed, units	24718	28257	28130	20323	10994	9474	.	.	.
annual change in %	18.0	14.3	-0.4	-27.8	-28.6	-13.8	.	.	.
Employment total, th pers., average 2)	3678.8	3648.1	3646.3	3697.7	3673.6	3800.8	.	.	.
annual change in % 2)	-1.9	-0.8	0.0	0.7	.	3.5	.	.	.
Employees in industry, th pers., average 3)	833.0	789.0	783.5	795.9	.	831.9	.	.	.
annual change in % 3)	-5.4	-5.3	-0.7	1.6	.	0.7	.	.	.
Unemployed reg., th, end of period	495.9	477.5	464.0	404.1	398.5	397.2	404.2	.	.
Unemployment rate in %, end of period	11.7	11.4	11.0	9.6	9.5	9.4	9.6	9	9
Average gross monthly wages, HUF 3)	38900	46837	57270	67764	64422	73437	.	.	.
annual change in % (real, net)	-12.2	-5.0	4.9	3.6	3.5	2.5	.	.	.
Retail trade turnover, HUF bn 4)	2389.9	2793.2	3197.6	3682.8	2495.0	3014.2	.	.	.
annual change in % (real) 4)	-8.1	-5.0	-1.0	12.3	6.0	6.9	.	.	.
Consumer prices, % p.a.	28.2	23.6	18.3	14.3	15.3	9.8	10.0	8.3	6.5
Producer prices in industry, % p.a.	28.9	21.8	20.4	11.3	12.4	4.5	.	.	.
Central government budget, HUF bn 5)									
Revenues	1418.2	2079.3	2364.6	2624.4	1865.1	2218.3	3233.6	.	.
Expenditures	1728.9	2209.1	2703.1	2994.6	2142.7	2563.1	3565.2	.	.
Deficit (-) / surplus (+)	-310.8	-129.8	-338.5	-370.2	-277.6	-344.8	-331.6	.	.
Deficit (-) / surplus (+), % GDP	-5.5	-1.9	-4.0	-3.6	.	-4.2	-2.9	.	.
Money supply, HUF bn, end of period									
M1, Money	1036.3	1237.2	1517.6	1789.2	1602.8	1876.2	2098.0	.	.
Broad money	2736.4	3351.1	4009.5	4620.0	4271.4	4972.2	5355.0	.	.
Refinancing rate, % p.a., end of period	28.0	23.0	20.5	17.0	18.0	15.5	14.5	.	.
Current account, USD mn	-2480	-1678	-981	-2298	-1337	-1288	-2074	-2100	-2200
Reserves total, incl. gold, USD mn	12011	9718	8429	9341	8816	10297	.	.	.
Gross external debt, USD mn	31660	27617	23747	26747	25332	28270	.	.	.
Exports total, fob, USD mn 6)	12904.7	13119.6	19099.5	23010.0	16516	17603	24900	27900	31000
annual change in %	20.2	1.7	21.8	20.5	22.5	6.6	8	12	11
Imports total, cif, USD mn 6)	15406.1	16176.5	21211.1	25700.7	18505	19887	27800	30900	34300
annual change in %	5.4	5.0	17.1	21.2	21.9	7.5	8	11	11
Average exchange rate HUF/USD	125.69	152.57	186.75	214.45	213.59	234.23	237.24	246	.
Average exchange rate HUF/EUR (ECU)	162.65	191.15	210.93	240.98	235.63	251.81	252.77	.	.
Purchasing power parity HUF/USD, WIIW	61.58	72.55	84.20	93.87	.	.	101.73	.	.

1) Up to 1994 public transport organizations only. - 2) Based on labour force survey, excluding persons on child care leave; from 1998 new sample. - 3) Enterprises with more than 10, from 1999 more than 5 employees. - 4) From 1998 excluding catering. - 5) Excluding privatization revenues; in 1998 excluding expenditures fulfilled in bonds. - 6) Converted from the national currency to USD at official exchange rate. From 1997 including trade of firms with customs free legal status.

Source: WIIW Database incorporating national statistics; WIIW forecasts.

Vladimir Gligorov

Macedonia: Improved international position

Last year was less bad than was expected in view of the Kosovo crisis. GDP increased, though it looked stagnating in mid-1999. Industrial production declined, but only moderately. Imports contracted, as did exports. However, sales to non-residents increased. Those can be credited with the more positive production results. The fiscal deficit deteriorated, though the foreign budget support made this a non-problem. Also, the increased supply of foreign currency helped the stability of the Macedonian denar, which is effectively pegged to the German mark at the ratio of 31 to 1 (from mid-1997). Foreign direct investments underperformed as predicted. Also, reforms stalled as crisis management took over as the main concern of the government.

Prospects for the next two years are of intensified restructuring and more foreign direct investment. The government intends to deal with 13 or so large, loss-making enterprises, this year and the next. All will be offered to foreign investors, but it is not expected that all sales will be successful. Indeed, it is expected that a number of these enterprises will have to be closed down. The government has vouched that it will take over the bills and obligations of these enterprises. This will add to the fiscal burden and to the number of unemployed. If these plans are carried out, the next couple of years cannot be characterized by high growth. In fact, industrial production may continue to decline or grow only moderately. The growth may come from the increased demand in Kosovo where the reconstruction effort is expected to pick up in the short run.

Macedonia is to be the first to benefit from the newly established Stabilization and Association Agreement (SAA) with the EU. The negotiations should start early this year and should lead to an opening up of EU markets to Macedonian products. The benefits of free trade should be coupled with specific programmes designed to support the transition and accession process in Macedonia. It is, at this point, not altogether clear what the SAA will contain, but it should, at the very least, increase the attractiveness of this country to foreign investors. Indeed, Greece has emerged as a leading foreign investor in Macedonia (the recent deal is the sale of the largest Macedonian bank, Stopanska Banka, to the National Bank of Greece).

The international position of Macedonia has improved in other respects too. The country plays a leading role in the Stability Pact, has no problems with its neighbours and has been singled out as a leading country in the so-called Western Balkans by the EU. The episode with the establishment of diplomatic relations with Taiwan and the severance of diplomatic relations with China have been embarrassing for the government and have cost them in terms of credibility and votes in the presidential elections, but have not led to other costs –

though it has not resulted in the promised benefits either (in the form of huge investments from Taiwan).

While the international position has been strengthened, the internal political stability has been under pressure. The presidential elections led to conflicts and demonstrations, though the ruling coalition succeeded in getting one of their candidates elected. However, the Macedonian parties in the coalition lost their large public support and have had to change quite a number of ministers in their government. This year local elections will be held, and the opposition is expected to do well, though it is currently going through internal reconstruction. There have also been threats to internal security from groups of organized crime. Still, the internal equilibrium and ethnic coexistence is surviving.

Longer-term prospects are still dependent on the regional stability and on the restructuring of the Macedonian economy. Assuming the regional development takes a positive turn, the Macedonian economy is well-placed to profit from that.

Table MK

Macedonia: Selected Economic Indicators

	1995	1996	1997	1998 [1]	1998	1999	1999	2000	2001
					January-September		estim.	forecast	forecast
Population, th pers., mid-year	1966.0	1983.1	1996.9	2010.0	.	.	2025	.	.
Gross domestic product, MKD mn, nom.	169521	176444	185023	193153	.	.	196400	208400	229800
annual change in % (real)	-1.1	1.2	1.5	2.9	.	.	2.7	3	5
GDP/capita (USD at exchange rate)	2267	2225	1860	1765	.	.	1616	.	.
GDP/capita (USD at PPP - WIIW)	4040	4167	4291	4430	.	.	4584	.	.
Gross industrial production									
annual change in % (real)	-10.7	3.2	1.6	4.5	7.9	-2.6	-2.5	0	3
Gross agricultural production									
annual change in % (real)	3.9	-2.2	1.1	4.0	.	.	5	.	.
Goods transport, mn t-kms	1343	1067	1175	1280	890	741	.	.	.
annual change in %	-21.0	-20.6	10.1	8.9	17.8	-16.8	.	.	.
Gross fixed investment, MKD mn, nom.	24704.2	26484.7	27812.0	29592.0	.	.			
annual change in % (real)	7.0	8.9	4.3	2.6	.	.	.	.	.
Construction output, value added									
annual change in % (real)	-2.9	1.9	-8.9	-9.0	-9.9	-6.0	.	.	.
Dwellings completed, units	4640	5342	4300	.	.	.	.	.	.
annual change in %	-3.9	15.1	-19.5	.	.	.	.	.	.
Employment total, th pers., average [2]	391.9	374.5	354.3	.	.	.	.	.	.
annual change in % [2]	-9.5	-4.4	-5.4	.	.	.	.	.	.
Employees in industry, th pers., average	136.6	127.6	117.6	113.6	117.7	118.4	.	.	.
annual change in %	-13.4	-6.6	-7.9	-3.4	-0.5	3.9	.	.	.
Unemployed reg., th, end of period	229.0	245.1	257.7	.	.	.	.	.	.
Unemployment rate in %, end of period [3]	36.9	39.6	42.1	34.5	.	.	32.4	32	32
Average net monthly wages, MKD	8581	8817	9063	9394	9303	9578	9627	.	.
annual change in % (real, net)	-4.3	0.5	0.2	3.8	2.8	2.9	.	.	.
Retail trade turnover, MKD mn	31682.2	29893.0	32482.8	33782.1	25406.2	28392	.	.	.
annual change in % (real, calc.)	-4.4	-8.4	4.1	3.2	3.6	13.5	.	.	.
Retail prices, % p.a.	15.9	3.0	4.4	0.8	1.4	-1.5	-1	3	5
Producer prices in industry, % p.a.	4.7	-0.3	4.2	4.0	5.4	-1.3	.	.	.
General government budget, MKD mn [4]									
Revenues	64254	64445	41398	.	30255	36356	.	.	.
Expenditures	66032	65096	41393	.	29916	36167	.	.	.
Deficit (-) / surplus (+)	-1778	-652	4	.	339	189	.	.	.
Deficit (-) / surplus (+), % GDP	-1.0	-0.4	0	.	.	.	.	.	
Money supply, MKD mn, end of period									
M1, Money	12521	12143	13983	15178	14378	18670	.	.	.
M2, Money + quasi money	18703	18490	22724	26003	23864	31105	.	.	.
Discount rate, % p.a., end of period	15.0	9.2	8.9	8.9	8.9	8.9	.	.	.
Current account, USD mn	-232.2	-288.0	-276.4	-287.7	-163.1	-23.3	-136	-300	-400
Gross reserves of NB, excl. gold, USD mn	257.5	239.5	257.0	306.1	295.3	410.3	.	.	.
Gross external debt, USD mn [5]	1235.9	1172.4	1133.1	1398.6	1296.3	1444.4	.	.	.
Exports total, fob, USD mn	1204.0	1147.4	1236.8	1310.7	973.9	857.6	1207.4	.	.
annual change in %	10.8	-4.7	7.8	6.0	.	-11.9	-7.9	.	.
Imports total, cif, USD mn	1718.9	1626.9	1779.5	1914.6	1354.6	1195.6	1743.9	.	.
annual change in %	15.8	-5.4	9.4	7.6	.	-11.7	-8.9	.	.
Average exchange rate MKD/USD	38.04	39.99	49.83	54.45	52.84	57.74	60	60	60
Average exchange rate MKD/EUR (ECU)	49.20	50.10	56.51	60.98	59.06	60.62	.	.	.
Purchasing power parity MKD/USD, WIIW	21.34	21.35	21.59	21.69	.	.	21.16	.	.

1) Preliminary. - 2) Employees plus own account workers, excluding individual farmers. - 3) In % of unemployed plus employment, from 1998 according to ILO definition. - 4) From 1997 excluding extrabudgetary fonds. - 5) Medium and long-term.

Source: WIIW Database incorporating national statistics.

Leon Podkaminer

Poland: Structural weaknesses affect external equilibrium

According to provisional estimates in 1999 Poland's GDP increased by 4.1%, of which private consumption by 5% and gross fixed investment by 7%. The macro-economic goals set in the budget for 1999 were thus not achieved: the first shortfall since 1993. The government had originally targeted 5.1% GDP growth and a 6.1% increase in domestic demand (of which 14% growth in gross fixed investment and 4.3% in private consumption). Initially high budget deficits were progressively reduced: the year-end deficit was lower than assumed (its share in GDP was about 2% instead of the projected figure of 2.15%) The reduction was achieved by cutting expenditures (education, health) and raising indirect tax rates.

The inflationary acceleration, perceptible in the third quarter, was caused by several factors, of which relatively strong consumer demand was only one. Throughout 1999 several major increases in excise tax rates were introduced, particularly where fuel tax was concerned. Combined with the increase in world oil prices and a strong USD, the excise tax increases resulted in a steep rise in fuel prices (during 1999 the latter rose about 50%). This had an impact on costs and prices in general, most particularly in retail trade and transportation. Throughout 1999 these sectors recorded ever-increasing losses, necessitating some, albeit inadequate, price adjustments. In general, profits did not decline solely on account of higher fuel prices. Cost pressures came into play for other reasons.

The entire non-financial enterprise sector (firms with more than 50 employees in manufacturing and mining, and more than 20 in other activities) recorded a drop in profits in 1999. In the first three quarters of 1999 the net profit of the whole sector equalled PLN 1.4 bn (down from PLN 7.7 bn). The decline was not that steep in manufacturing (from PLN 5.2 bn to 1.7 bn). Foodstuff manufacture performed particularly badly. Its net profit of PLN 0.8 bn turned into net loss of 0.25 bn (on unchanged value of sales). Apparently, the demand for food was very weak. This may be indicative of stagnation of or decline in disposable incomes in the low-income groups. Net losses in retail trade (excluding retail trade in motor vehicles and automotive fuel) trebled[6].Profits stayed high in some service activities, such as retail sale of motor vehicles and fuel, post and telecommunications; they rose in the real estate business.

6 The share of large retail firms (20 or more employees) in total retail trade turnover rose from about 6% in 1993 to 19% in 1998. The process has been accelerated by the gigantic foreign-owned hyper-markets sprouting up across the country. This seems strange given the facts related to low (and in some cases, even dropping)- profitability. It is quite possible that the price policy currently pursued by foreign retail organizations, which have been recording losses as a result, is aimed at eliminating their small-scale retail competitors.

Overall, labour productivity trends were positive. In industry, labour productivity between January and November rose some 7% in real terms. At the same time, average gross wages in industry rose some 10% – and prices in industry increased by 5.4%. Given the manner in which unit labour costs developed, industry, and even more so manufacturing, should have earned higher profits than the year previous.

Another factor possibly responsible for weak profits may have had something to do with exchange rate developments in 1999. The average PLN/DEM exchange rate increased by 12.4%in the first quarter of 1999 (as against the first quarter of 1998), signifying a sizeable nominal devaluation of the PLN. In the second and third quarters, the corresponding PLN/DEM exchange rates increased by 6.2% and 1.8%, respectively. Cumulatively, the DEM prices rose approximately 8% in 1999 (as against 1998). As for the USD the PLN price increases were even steeper: 9% in the first quarter of 1999; 12% and 11.4% in the second and third quarters, respectively. Cumulatively, the PLN/USD exchange rate increased by 11.4% in 1999. Foreign exchange prices in respect of both currencies outstripped domestic consumer prices – and even more so in the case of producer prices. In real terms, the Polish currency depreciated quite strongly[7].

Devaluation of the PLN meant that imports were more expensive: a development that must have affected importers' profits. Prices for consumer *non-food goods*, however, moved roughly in line with the price of the DEM, at least from the end of the first quarter onwards. In 1999 these prices rose about 10.6% – more than the PLN/DEM exchange rate. Given that the bulk of consumer imports come from the euro zone, these imports continued to yield importers additional profits. The situation was vastly different for those importing raw materials and intermediate goods. On account of the rising cost of imported inputs, manufacturing profits came under pressure. Given the low share of exports in manufacturing output, the depreciation-related increase in profitability of exports could not offset the depreciation-related increase in costs of imported inputs.

Overall, the gains in terms-of-trade (for the entire foreign trade) were initially modest; during the year they evaporated (5.3% in the first quarter 1999, 2.5% in the first and second quarters, and 1% in the first three quarters). According to balance-of-payments statistics, both exports and imports declined, at least in the USD terms, in 1999: exports by 12.1%, imports by 6.8%[8]. In DEM (or euro) terms, the (calculated) rates of decline were lower: 6.9% and 1.3%, respectively. Regardless of the manner of calculation, the trade deficit expanded: from USD 13.7 bn to 14.5 bn (BOP statistics for 1999) and from USD 13.8 bn to 14.8 bn (customs statistics for the period January to September).

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7 Producer prices in manufacturing increased by 3.9% in the first quarter of 1999, 4.4% and 5.1% in the second and third quarters: leading to a cumulative figure of some 5% for the year.

8 Provisional estimates based on the customs statistics suggest lower rates of decline (in 1-3 Q 1999): exports by 6.4%, imports by 5%.

Broadly speaking, the disappointing foreign trade performance under conditions of real depreciation in 1999 can be explained by the high import intensity of manufacturing and its low level of export orientation[9]. Other factors were at work, too. First, the Russian market which had been an important outlet for Polish exports prior to the crash in August 1998 has failed to recover to any sufficient degree. This certainly depressed exports overall. Secondly, domestic retail prices for non-food consumer goods generally rose faster than the PLN/DEM exchange rates. As far as these goods go, appreciation has continued, supporting their importation. This has softened the overall decline in imports. Thirdly, ever since the crisis in Russia in August. 1998, exchange rates have become increasingly volatile. The PLN has experienced several bouts of strengthening and weakening since then. Changes in exchange rates were abrupt, the periods when the PLN was strong or weak differed in duration and the range of chaotic exchange rate movements was quite broad. Increased exchange rate volatility and heightened exchange risks negatively affected trade activities, particularly those of small and medium-sized firms. The underdevelopment of supportive trade credit and insurance agencies was certainly an additional contributory factor.

In the final instance, weaknesses of the Polish manufacturing sector have been responsible for the overall development of trade: high import-intensity coupled with a lack of export orientation, slow changes in production structures and exports, and insufficient improvement in quality and export prices are all well documented[10]. The weaknesses are unlikely to fade away soon. In periods of sustained appreciation, they will manifest themselves in the form of an unsustainable expansion of trade and current account deficits. In periods of depreciation, they will manifest themselves in the form of stagnating (or even falling) production, exports and imports – but not necessarily in the form of lower deficits.

Polish manufacturing weaknesses can be blamed on the policies pursued in recent years. There has been no meaningful promotion of structural change, research and development, and exports – or at least import-substitution. Foreign direct investment policy is patently irrational: projects that generate higher trade imbalances (e.g. retail hyper-markets) are not restricted and projects which promise genuine trade surpluses are not actively encouraged. Liberalization of trade with the EU and the removal of import tariffs were premature – and will also be damaging in the future. Moreover, major errors are to be

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[9] Raw materials and intermediate inputs, used primarily by manufacturing, are estimated to constitute 64% of all imports (investment goods 15%, consumer goods 21%). Rough calculations suggest that imported inputs account for 29% of all inputs to manufacturing. This contrasts with its propensity to export, recently equalling roughly 26%. Assuming fixed proportions between manufacturing output, exports and imported inputs, it can be concluded that rising manufacturing production generates a larger trade balance deficit. In this context it is clear that manufacturing profits are eroded by real depreciation – unless there are strong gains in manufacturing's terms-of-trade. (Otherwise, the decline in profits justifies lower levels of production, exports and imports).

[10] See *WIIW Structural Report 1999*, and the WIIW research covering individual manufacturing branches (see *WIIW Industry Studies*).

observed in the conduct of monetary and exchange rate policy that date back to the beginning of 1995.[11]

From the end of 1995 until about August 1998 (the crisis in Russia) the policy did not display obviously negative consequences: the PLN showed relatively little volatility and was 'strong' (it was being traded above the mid-point of the band). Furthermore, real appreciation was permanent – that, however, was generally accepted, partly on account of the market strength of the PLN. Under these conditions manufacturing – and much of the rest of economy – grew accustomed to ever cheaper imports and ever less profitable exports. Since industrial production, GDP and gross fixed investment were growing at impressive rates while inflation kept declining, little concern was shown for the long-term consequences of this import-fed growth. Constantly expanding trade and current account deficits were considered minor issues – largely because of continuing high capital inflows.[12] Moreover, it was believed these inflows did not pose much of a risk. To some extent, this attitude was justified by the rising share of FDI (as opposed to short-term capital) inflows.

After the crisis in Russia the PLN became volatile and exports to Russia plunged, giving rise to concern about possible recession. Authorities became increasingly aware of the possible negative consequences of short-term capital inflows (and domestic firms' excessive borrowing abroad). In November1998 the band widened further and then again in March 1999, the aim being to increase the risks to currency speculators (although they also heightened the risks to be borne by exporters and importers). The situation was considered grave enough (on account of continuing inflows and weakening production growth) to justify lowering the interest rates – this was duly done four times in the second half of 1998.[13]

The weakening of the PLN that followed had an impact on capital flows – but not on exports, nor on the current account deficit. The current account deficit in 1999 reached an estimated USD 11.7 bn or about 7.6% of the GDP. Official reserves declined for the first time since 1992. Though higher than the year before, FDI inflow in the first three quarters of 1999, amounting to USD 4.8 bn, was not impressive. Despite lower domestic interest rates and increased exchange rate risks, Polish firms (including the foreign-owned companies) incurred additional foreign debts amounting to USD 2.4 bn (total debt at the end of 1999 stood at about USD 20.5 bn).

[11] The main elements of that misguided policy are: maintenance of high real interest rates; steady liberalization of capital flows; progressive reduction of control of exchange rate – i.e. widening the band of permissible fluctuations in the exchange rate

[12] The rigid exchange policy prior to 1995 permitted occasional devaluation. The policy culminated in 1995 with a USD 5.1 bn current account *surplus.*

[13] Interest rates on bank loans to firms stood at approx. 29% in 1998 and 22% in 1999. In real terms, they were very high, even in 1999.

The National Bank of Poland (NBP) experimented with a relaxation of monetary policy; this is currently considered a failure. Expansion of consumer credit throughout much of 1999 (which certainly supported consumption) and a weakened PLN are held jointly-responsible for the inflationary acceleration in late 1999. In addition, the expansion of the current account deficit is also blamed on lower interest rates. In November 1999 the NBP corrected the 'error of its ways' by sharply raising its interest rates. This in turn may provoke high inflows of volatile capital once again and lead to a major revaluation of the PLN. Widening the band of exchange rate movements and the NBP resolving not to meddle in the exchange rate market may not prevent this happening. In due time, the inflows will be considered inflationary because they will expand the monetary base (as they have already done three times before -in 1995, in the first half of 1997 and the first half of 1998). As such, sterilization operations will be called for – i.e. still higher interest rates. Furthermore, they will result in real appreciation – hence increasing the current account deficit still further. In the meantime, Poland will be increasingly exposed to the possibly devastating effect of sudden flights of capital. At some point in time, the NBP will have to try to lower the interest rates once again.

Even if a crisis is avoided, the return to 'traditional' NBP policy will in the ultimate analysis prove costly. Real appreciation in the intervening period will reinforce the Polish economy's abnormal dependence on imports – and work against reorientation in favour of exports. Unfortunately, other elements of the overall economic policy also seem to suggest that Poland is actually heading in such a direction. The budget prepared by the Finance Ministry for 2000 envisages strong real appreciation – with scarcely any change in the average nominal PLN/USD rate in 2000 compared to 1999. This assumption may be based on expectations of massive foreign exchange earnings from the sale of privatized assets, and further increase in other sources of FDI. The Treasury (the ministry in charge of privatization) intends to earn a further PLN 20 bn (more than in 1998 and 1999 together) by selling off most of the 'family silver'[14] remaining. That can be easily achieved if, as in 1999, profitable and valuable assets are sold at 'bargain prices'. Problems will occur later on, when nothing is left to sell – and finance galloping current account deficits.

[14] In 2000 the Ministry intended to privatize the power sector, steel, armaments, chemistry and sugar industries, renowned distillers, the national airline and the largest insurance company (with a 60% share of the market). Moreover, it was planning to sell its shares in leading companies that had already been privatized (banks, copper giant KPHM, national telecom, and PKN (the largest producer and distributor of petroleum products). The Ministry's intention was to complete the overall privatization process by 2002. There is a growing opposition to that – also within the ruling parties. It is argued that the rush to sell everything off is inevitably combined with too low a price being obtained for individual items. Furthermore, it is deplored that most recent foreign take-overs amount to selling the market, without committing the new owners to expanding the capacities or increasing the capital, and that the loss of national control over firms with monopolistic position on the domestic market may be damaging in the long term.

Table PL

Poland: Selected Economic Indicators

	1995	1996	1997	1998 [1]	1998	1999	1999	2000	2001
					January-September		estim.	forecast	forecast
Population, th pers., end of period	38609	38639	38660	38667	38679	38665	38665	38670	.
Gross domestic product, PLN mn, nom.	306318	385448	469372	549467	395095	.	613800	686300	756600
annual change in % (real)	7.0	6.0	6.8	4.8	5.6	3.1	4.1	4.5	5
GDP/capita (USD at exchange rate)	3274	3702	3702	4067	.	.	3999	.	.
GDP/capita (USD at PPP - WIIW)	6708	7310	7968	8433	.	.	8910	.	.
Gross industrial production (sales)									
annual change in % (real)	9.7	8.3	11.5	4.7	7.0 [2]	1.5 [2]	4.4	5	6
Gross agricultural production									
annual change in % (real)	10.7	0.7	-0.2	5.9	.	.	.	.	.
Goods transport, mn t-kms	300807	309272	329737	317052	.	.	.	.	.
annual change in %	11.3	2.8	6.6	-3.8	.	.	.	.	.
Investment outlays, PLN mn, nom. [3]	47145	65622	90438	112814	44802	50250	.	.	.
annual change in % (real)	17.1	19.2	22.2	15.3	23.9	6.7	7	9	.
Construction output total									
annual change in % (real)	5.6	3.0	16.5	12.4	14.7 [2]	2.8 [2]	3.2	.	.
Dwellings completed, units	67072	62130	73706	80594	52120	45552	.	.	.
annual change in %	-11.8	-7.4	18.6	9.3	13.1	-12.6	.	.	.
Employment total, th pers., average	14735.2	15020.6	15438.7	15800.4	.	.	.	.	.
annual change in %	1.8	1.9	2.8	2.3	.	.	.	.	.
Employees in industry, th pers., average	3461.1	3436.0	3433.4	3378.7	3170.3 [2]	3031.8 [2]	.	.	.
annual change in %	3.0	-0.7	-0.1	-1.6	-1.6 [2]	-4.4 [2]	.	.	.
Unemployed reg., th, end of period	2628.8	2359.5	1826.4	1831.4	1676.7	2177.8	2350	.	.
Unemployment rate in %, end of period	14.9	13.2	10.3	10.4	9.6	12.1	13	12.5	12
Average gross monthly wages, PLN [4]	690.9	874.3	1065.8	1232.7	1499.8 [2]	1657.3 [2]	.	.	.
annual change in % (real, net) [5]	3.0	5.7	7.3	4.5	4.0 [2]	3.5 [2]	3.5	.	.
Retail trade turnover, PLN mn	169585	213241	258166	291197	.	.	.	.	.
annual change in % (real)	2.3	4.5	6.8	2.6	15.8 [2]	14.2 [2]	.	.	.
Consumer prices, % p.a.	27.8	19.9	14.9	11.8	12.6	6.6	7.3	7	5
Producer prices in industry, % p.a.	25.4	12.4	12.2	7.3	7.9	5.1	5.6	.	.
Central government budget, PLN mn									
Revenues	83722	99675	119772	126560	91048	88965	.	.	.
Expenditures	91170	108842	125675	139752	101458	100235	.	.	.
Deficit (-) / surplus (+)	-7448	-9167	-5903	-13192	-10410	-11270	-12400	-12700	.
Deficit (-) / surplus (+), % GDP	-2.4	-2.4	-1.3	-2.4	-2.6	.	-2.0	-1.9	.
Money supply, PLN mn, end of period									
M1, Money	37353	61056	72156	81484	77563	92382	.	.	.
M2, Money + quasi money	104255	136662	176437	220780	203524	245976	263762	.	.
Discount rate of NB % p.a., end of period	25.0	22.0	24.5	18.3	21.5	15.5	19.0	.	.
Current account, USD mn	5310	-1371	-4312	-6858	-3878	-7995	-11700	-13000	-13000
Gross reserves of NB incl. gold, USD mn	14963	18033	20670	27382	27083	26032	25500	.	.
Gross external debt, USD mn [6]	43957	47354	48914	56867	.	57359 [7]	.	.	.
Exports total, fob, USD mn [8]	22894.7	24440.0	25751.3	28228.7	20956	19820	26700	27500	.
annual change in %	32.8	6.7	5.4	9.6	12.4	-5.4	-5.4	3	.
Imports total, cif, USD mn [8]	29049.2	37136.5	42306.9	47054.3	34777	32834	44800	47000	.
annual change in %	34.7	27.8	13.9	11.2	14.1	-5.6	-4.8	5	.
Average exchange rate PLN/USD	2.42	2.70	3.28	3.49	3.50	3.90	3.97	4.30	.
Average exchange rate PLN/EUR (ECU)	3.13	3.38	3.71	3.92	3.86	4.19	4.23	4.75	.
Purchasing power parity PLN/USD, WIIW	1.18	1.36	1.52	1.69	.	.	1.78	.	.

1) Preliminary. - 2) Firms with more than 5 employees. - 3) Gross fixed investment plus some costs related to acquisition of land, used machinery, interest on investment credit etc. Quarterly data refer to firms with more than 50 (manufacturing & mining) or 20 (other activities) employees. - 4) From 1999 and quarterly data 1998 including premium for social security. - 5) From 1999 and quarterly data 1998 real gross wages. - 6) From 1996 according to IMF methodology. - 7) End of June. - 8) Converted from the national currency to USD at trade exchange rate.

Source: WIIW Database incorporating national statistics; WIIW forecasts.

Gábor Hunya

Romania: New government, old problems

In 1999, it proved possible to avoid the worst-case economic scenario, i.e. the country defaulting on foreign debts, by domestic borrowing and abandoning the inflation target previously set. GDP, however, dropped by 3.9% (after -5.4%, the revised result for 1998) and, as forecast by the WIIW, average annual inflation rose to 46, almost double the official target of 25%. Of the ten eastern EU-accession countries, Romania continues to display the worst growth performance and record the highest inflation rate.

Political and legal instability continued to be permanent features in the country. A new prime minister took up office and in December 1999 the government was reshuffled for the third time since the last elections. The new prime minister, a technocrat, Mugur Isarescu, is expected to refloat the stranded reform process and secure the support of international lenders. Mr. Isarescu enjoys wide respect as an economist and long-term governor of the National Bank of Romania (NBR). Local pundits claim this as evidence of the NBR having placed the government's economic policy under its surveillance. With parliamentary and presidential elections due between November 2000 and January 2001, Mr. Isarescu will have a hard time safeguarding economic stability against populist overspending which in earlier election years was customary practice.

In 1999, shrinking private consumption and investments depressed aggregate demand (no annual data available yet). Per capita net real wages increased slightly in the first three quarters of 1999, but the population's total real disposable income contracted. By November 1999, the number of wage-earners had diminished by 8% in the space of one year and the unemployment rate had increased from 9.5% to 11.1%. The share of fixed capital formation in GDP dropped from 23% in 1996 to 18% in 1998 and still further to 17.5% in the first half of 1999. Investment outlays declined by almost 13% during the first three quarters of the year compared to the same period in the previous year. Public sector investments suffered from the impact of budgetary reallocation, while private investments had to combat the effects of low demand and high interest rates, coupled with legal and economic uncertainties. For most of the year, real interest rates for non-bank customers stood at more than 20%, even higher in the middle of the year when intensive government borrowing competed for savings.

Maturing foreign loans were paid from domestic credits and by depleting forex reserves as foreign and multilateral arrangements ultimately proved unsuccessful. In all probability, the general budget deficit rose to more than 4% of GDP and a primary surplus of 2% was to be observed. The decline in foreign trade deficits was the only item mitigating the drop in GDP. In the period January-October 1999, the commodity trade deficit, with imports computed in CIF prices, declined to USD 1.37 bn from USD 2.79 bn in the same period in 1998. Whereas exports slipped one percent in ten months, imports declined by 15.4%. In the period January-September 1999, the current account deficit narrowed to USD 634 mn from USD 1.818 bn over the same period in 1998; the year-end result is expected to USD 1.3 bn. The floating exchange rate went into free fall at the beginning of 1999, only later in the year did it merely keep pace with the rate of inflation. Devaluation played an important role in diminishing consumer goods imports; however, it fuelled inflation. Further savings in imports were the result of decreasing energy and material intensity in the wake of structural change.

The decline in industrial output of some 8% in 1999 can be attributed in part to healthy structural change. Industrial activities which had incurred major losses and required a large volume of imports were streamlined. Export industries, such as clothing and furniture as well as tobacco, recorded increases in output in the first ten months of 1999. Recovery in the automotive sector which had been successfully privatized in co-operation with foreign investors is a further sign of a positive shift in the industrial structure. Metallurgy and chemical industries recorded the steepest decline in terms of both production and raw material imports, owing to their scraping worn-out capacities.

In order to solve the liquidity problems facing state-owned companies, the government resorted to a mix of sectoral policies ranging from partial bailouts and temporary direct subsidies to major indebted companies faced with the threat of closure to outright privatization. These measures were often applied on an ad-hoc basis and modified in the event of worker resistance becoming too fierce. The State Ownership Fund (FPS) sold off 1,705 companies in 1999, most of them small and medium-sized manufacturing enterprises; this reflects major progress in privatization. In 1999, only 79 contracts were concluded with foreign investors, 17 less than in the year previous. The inflow of FDI through privatization and other modes was about USD 1 bn in 1999. 64 companies were sold on the capital market, twice more than in 1998. Privatization in co-operation with domestic investors has not yet led to an improvement in corporate governance. Arrears in payments (inter-enterprise and budget arrears together) remained at about 20% of GDP.

The new government has drawn up a vague and rudimentary programme for 2000 with the aim of overcoming the crisis. It plans to continue privatization, reduce unprofitable production still further, keep fiscal policy tight and avoid an increase in imports. The programme assumes GDP growth of 1.3% at 27% inflation and a budget deficit of 3% to GDP: parameters that are most unlikely to be met. It is highly improbable that the budget deficit will decrease, as interest payment obligations are on the increase. In order to meet the budget deficit target, the primary surplus would have to increase from 2% in 1999 to 4% in 2000. The relevant budgetary legislation will only be enacted by late February at the earliest, following detailed negotiations with the IMF and a lengthy parliamentary debate.

The government programme’s strongest point is the proposal for fiscal reform comprising: a reduction in the corporate tax rate with the hope of turning part of the grey economy to taxpayer; the introduction of personal income tax so as to broaden the tax base; and a reduction in the number of special funds so as to make the budget more transparent.

At the beginning of 2000, the corporate tax rate was lowered from 38% to 25%; this offered major relief to about one third of the companies which currently make a profit. The government also expects that some hitherto unreported instances of profit will be declared. At the same time, most of the preferences granted to foreign investors and small enterprises were withdrawn, despite their just having been introduced over the past 13 months. The only incentive provided for under the new legislation is 10% tax credit accruing to those investing in new assets. Major investment projects, valued at more than USD 50 mn, will remain eligible for special treatment at the government's discretion. Another incentive is that the portion of the revenue earned through exports would only be subject to a levy of 5%.

The lower revenues expected in the corporate sector will be balanced out by higher revenues from consumer goods. The VAT rates of 22% and 11% were standardized at 19%. Higher rates already apply to foodstuffs and medicines, and at the beginning of April the higher rate will also be introduced for energy. Together, these items represent about 70% of the consumer basket. For the most part, it will be the more affluent members of society who benefit from the reduced rate on consumer durable. The new VAT regime will certainly increase the general price level, thus militating against the low inflation target set by the government.

In 2000, external financing will remain tight; however, it will be easier to manage than in the year previous. USD 1.4 bn will be spent on debt servicing (USD 2.2 bn in 1998). If the current account deficit can be kept in the range of USD 1.5-2 bn, no serious tension should emerge. The official exchange rate policy seems to have learned its lesson from the recent past; it will be used to support external equilibrium rather than as a means of meeting anti-inflation targets. Real appreciation may, thus, be very slow. The government counts on the international funding promised being available as a result of which foreign capital inflows should amount to USD 5.0 bn. From the EU Romania can expect about EUR 624 mn annually over the next six years as non-reimbursable pre-accession financial assistance. This is a substantial amount; it can only be disbursed, however, on the basis of effectively targeted and efficiently managed projects: this poses a real challenge to Romanian institutions. The IMF in its relationship with Romania has obviously abandoned its bailing-in condition of raising USD 250 mn in private loans before giving free the delayed instalment of the stand-by loan. Conditions for the delayed and new IMF facilities will include the basic indicators set in the budget for the year 2000.

Privatization revenues are an important source of domestic and foreign debt-servicing. Preparations have already been made to sell off the national oil company and airline. Privatizing two state banks, Banca Agricola and Banca Comerciala Romana, will still need some time and restructuring. However, once completed, the privatization of the commercial banks will be finished within the course of the current year. The deregulation of utilities is still in the preparatory stage.

In its forecast of the main indicators, the WIIW has taken into account the fact that foreign demand may pick up and towards the end of the year private consumption may follow suit, should the wage policy be relaxed in the run-up to the elections. Economic performance may level out in the course of 2000 and GDP may pick up slowly in 2001. Inflation would remain intransigent at around 40% a year on average owing to the effects of the tax reform, general expectations and import prices. Worse scenarios may occur in the event of renewed political instability.

Table RO

Romania: Selected Economic Indicators

	1995	1996	1997	1998 1)	1998	1999	1999	2000	2001
					January-September		estim.	forecast	forecast
Population, th pers., mid-year	22681.0	22607.6	22545.9	22502.8	.	.	22500	.	.
Gross domestic product, ROL bn, nom.	72136	108920	250480	368261	.	.	500000	700000	930000
annual change in % (real)	7.1	3.9	-6.9	-5.4	.	-3.8	-3.9	0	1
GDP/capita (USD at exchange rate)	1564	1563	1550	1844	.	.	1449	.	.
GDP/capita (USD at PPP - WIIW)	6181	6628	6318	6050	.	.	5872	.	.
Gross industrial production									
annual change in % (real)	9.4	6.3	-7.2	-16.8	-17.0	-9.0	-8	0	2
Gross agricultural production									
annual change in % (real)	4.5	1.3	3.4	-7.6	.	.	.	.	.
Goods transport, mn t-kms 2)	126719	106758	87590	62365	48189	34166	.	.	.
annual change in %	36.7	-15.8	-18.0	.	.	-29.1	.	.	.
Gross fixed investment, ROL bn, nom.	12995.5	20945.3	44134.7	45343.0	27731.8	39987.4	.	.	.
annual change in % (real)	10.7	3.1	-5.4	-18.6	.	-12.8	-13	0	5
Construction output total									
annual change in % (real)	13.2	3.7	-24.4	-18.0	.	-16.9	.	.	.
Dwellings completed, units	35822	29460	29921	29692	12780	13232	.	.	.
annual change in %	-2.5	-17.8	1.6	-0.8	.	3.5	.	.	.
Employment total, th pers., end of period	9493.0	9379.0	9023.0	.	.	.	.	.	.
annual change in %	-5.2	-1.2	-3.8	.	.	.	.	.	.
Employees in industry, th pers., average	2614.7	2586.0	2443.0	2327.9	2362.6	2030.1	.	.	.
annual change in %	-8.4	-1.1	-5.5	-4.7	-3.5	-14.1	.	.	.
Unemployed reg., th, end of period	998.4	657.6	881.4	1025.1	857.2	1073.6	.	.	.
Unemployment rate in %, end of period	9.5	6.6	8.9	10.3	8.7	10.9	12	13	12
Average gross monthly wages, ROL	281287	426610	846450	1357132	1282950	1847743	.	.	.
annual change in % (real, net)	11.8	9.2	-22.2	6.0	8.7	1.2	.	.	.
Retail trade turnover, ROL bn	22241.8	35316.3	83035.3	.	.	.	.	.	.
annual change in % (real)	29.0	15.3	-12.1	4.1	4.8	-2.5	.	.	.
Consumer prices, % p.a.	32.3	38.8	154.8	59.1	65.9	43.0	45.8	40	35
Producer prices in industry, % p.a.	35.1	49.9	152.7	33.3	38.3	35.9	.	.	.
Central government budget, ROL bn									
Revenues	12888	18373	43835	67216	47149	66936	.	.	.
Expenditures	15858	23732	52897	77617	54404	77735	.	.	.
Deficit (-) / surplus (+)	-2970	-5359	-9062	-10401	-7255	-10799	.	.	.
Deficit (-) / surplus (+), % GDP	-4.1	-4.9	-3.6	-3.1	.	.	.	.	.
Money supply, ROL bn, end of period									
M1, Money	7083	11173	18732	22110	18638	24341	.	.	.
Broad money	18278	30335	62150	92530	75068	114171	.	.	.
Refinancing rate of NB % p.a. 3)	47.2	40.3	52.6	35.0	35.0	35.0	.	.	.
Current account, USD mn	-1774	-2571	-2137	-2968	-1848	-634	-1300	-1600	-1700
Gross reserves of NB excl. gold, USD mn 4)	658.5	748.5	2530.0	1662.5	2212.2	1650.4	1546	.	.
Gross external debt, USD mn 5)	5482.1	7208.9	8584.3	9081.3	8699.3	8134.1	.	.	.
Exports total, fob, USD mn	7910.0	8084.5	8431.1	8302.0	6185.3	6093.4	8300	8500	8900
annual change in %	28.6	2.2	4.3	-1.5	-3.2	-1.5	0	2	5
Imports total, cif, USD mn	10277.9	11435.3	11279.7	11837.8	8624.2	7295.4	10000	10300	10800
annual change in %	44.6	11.3	-1.4	4.9	7.6	-15.4	-15	3	4
Average exchange rate ROL/USD	2033.3	3082.6	7167.9	8875.6	8520.9	14649.6	15338.4	22000	29000
Average exchange rate ROL/EUR (ECU)	2629.5	3862.9	8090.9	9989.9	9399.8	15709.0	16296.6	.	.
Purchasing power parity ROL/USD, WIIW	514.6	726.9	1758.4	2705.0	.	.	3784.3	.	.

1) Preliminary. - 2) From 1998 new methodology in road transport. - 3) Average of RNB lending rates, end of period. - 4) From 1995 foreign exchange reserves including reserves with banks located abroad. - 5) Medium and long-term.

Source: WIIW Database incorporating national statistics; WIIW forecasts.

Peter Havlik

Russia: Early elections improve prospects for stability and growth

The resignation of B. Yeltsin on 31 December 1999 was the most spectacular Y2K event worldwide. Though not completely unexpected – it had been discussed since early autumn as one of the speculative variants of how the Kremlin's family could hold onto power[15] – it further improved the chances of an increasingly popular Prime Minister V. Putin. After the disappointing performance of the Primakov–Luzhkov OVR bloc at the Duma elections, the new acting President V. Putin is now almost certain to win the contest on 26 March 2000 and to become the next Russian president. The early presidential elections will help not only Mr. Putin, whose star rise from obscurity can be attributed largely to his perceived efficiency and the tough dealing with Chechen 'terrorists'. The belated departure of Mr. Yeltsin and a shorter pre-election period will also help to reduce the political uncertainty which is an essential prerequisite for the recovery of investments as well.

Meanwhile, the Russian economy, especially the industry, has performed surprisingly well in the aftermath of the August 1998 financial crash. Industrial production expanded by 8% in 1999 and all branches recorded growth. The rouble devaluation boosted domestic production especially in areas substituting for imports. Ferrous and non-ferrous metals, chemicals, machinebuilding, wood and paper as well as the light industry grew by double-digit rates compared to 1998. The volume of freight transport and construction grew by about 5% each. The grain harvest (54 mn tons) was only slightly (+12%) better than in the disastrous year 1998 and total agricultural output reportedly grew by about 2% in 1999. In view of the fact that the estimated GDP increased only 1-2%, the volume of services (the latter form the bulk of GDP) must have stagnated at best. The picture from the demand side is even more contradictory: Retail trade turnover was down by some 8% as real incomes dropped by 15% and wages by almost one quarter in 1999. But wage and pension payment arrears were somewhat reduced. For the first time in a decade investments ceased to decline (an increase by 1% is reported) and government consumption might have increased as well. But the main factor outweighing the decreased domestic demand were rising net exports. Employment increased and the rate of unemployment declined by more than 1 percentage point within a year.

Another positive feature of last year's economic developments was the relatively stable financial situation. CPI inflation has been running at less than 2% per month since June so that prices increased by 86% on annual average in 1999 (but only by 36.6% December on December). Producer prices were growing faster during last year due to the lagged effects of devaluation and energy price increases (by 4% to 6% per month); the 1999 average

[15] *Kommersant-Vlast'*, 28 September 1999, pp. 7-8.

annual producer price inflation was 60%. Rouble M2 and the nominal exchange rate grew more or less in line with CPI inflation. The Central Bank of Russia successfully managed the rouble float and avoided excessive devaluation. In real terms, the rouble even slightly appreciated (more so if deflated with PPI) in the course of 1999, though the real exchange rate is still much below the August 1998 level. Thanks to the industrial recovery, better tax compliance, inflationary effects and higher rouble revenues from exports, the situation of the federal budget improved as well. The tax authorities collected 40% more revenues than envisaged by the 1999 budget law. Despite slightly increased expenditures, the federal budget deficit (2.1% of GDP in January-September 1999) was lower than planned. Without debt service (which amounted to 26% of total budgetary expenditure but was not met in full) the federal budget ran a primary surplus of about 1.7% of GDP. The budget for 2000 was adopted with a deficit of 1% of GDP and new foreign borrowing of USD 6 bn is foreseen. The envisaged primary surplus (3% of projected GDP) implies that foreign and domestic debt service will amount to 4% of GDP (or USD 6.7 bn at the targeted average exchange rate of RUB 32 per USD) and debt service arrears are thus again reckoned with. Like in previous years, there are serious doubts whether both underlying budget assumptions and its targets will be met.

Despite growing world market prices, Russian export revenues in USD slightly declined during 1999. This was due in part to a substantial reduction of exports to the CIS, as well as owing to the lagged adjustment of contract prices for commodities such as natural gas and metals (exports started to grow again only in the second half of 1999). The devaluation of the rouble in late 1998 – early 1999 brought about huge import cuts: imports were down by nearly one third in 1999; the trade balance recorded a surplus of about USD 30-40 bn. Both exports and imports started to recover in the final months of the year and the current account (in surplus of USD 14.5 bn in January-September 1999) is expected to reach a surplus of about USD 17 bn – almost 10% of GDP – for the year as a whole. FDI inflows remained low – less than USD 2 bn in the first nine months of 1999 – due to persisting political, legal and institutional risks. The nearly unchanged level of foreign exchange reserves (USD 12.5 bn as of end 1999), together with debt service payments of about USD 10 bn and a rising current account surplus, indicate continuing capital flight. Only the Japan government and the World Bank resumed its credits to Russia towards the end of 1999. Debt rescheduling negotiations with London Club creditors are stalled because of disagreements over the size of the debt reduction scheme. And the IMF suspended disbursements from the USD 4.5 bn standby loan in December 1999, formally because of insufficient progress in the implementation of structural reforms in Russia. In fact, western creditors have been hesitant because of political uncertainties on the eve of the parliamentary and presidential elections, as well as due to Russia's conduct in Chechnya. Again, the early presidential elections will likely speed up the resumption of talks with the IMF; debt rescheduling negotiations with the Paris and London Club creditors may start earlier than planned as well.

Acting President V. Putin has inherited a bunch of difficult problems. As far as the economy is concerned, he has to deal first of all with widespread corruption and crime, capital flight and disincentives for investment. The current economic recovery remains fragile, based largely on the temporary effects of devaluation and increased world market energy prices. The structure of the Russian economy is heavily distorted and domestic demand deeply depressed; in particular structural deficiencies are not going to be changed easily and soon. Government institutions hardly function and the society is disappointed with a decade of reform experiments which brought hardships for most. As illustrated by the coalition of the Communists and the Unity Bloc at the constitutory Duma session in January 2000 and the election of the communist G. Seleznyev as the new Duma speaker, the parliamentary elections resulted in a more coherent and less obstructive (from the Kremlin's point of view), though not necessarily more 'reform-oriented' assembly. The likely new president, Mr. V. Putin, is enjoying growing support and will probably be more efficient and less erratic than his predecessor. In the period before the parliamentary elections there were virtually no economic policy discussions, but it seems that after the August 1998 financial crash a new broad 'Moscow consensus' regarding economic policy is emerging. This new economic policy consensus appears to be less liberal, but still pragmatically pro-market, and it stresses Russian specifics as far as the role of the state and individual freedoms is concerned.

Mr Putin's economic programme, drawing on the conclusions of the newly established 'Strategic Reform Centre' think tank, was disseminated at the government webpage at the end of December 1999.[16] It acknowledges Russia's current backwardness and structural problems which result both from the past communist heritage and from mistakes of the last reform decade. Mr. Putin sees the way out of the current malaise not in a new radical reform push ('people would not withstand it'), but in gradual and sustained efforts without imposing more economic hardships on the population. There should be no copying of foreign abstract models. Instead, Russia should follow a way of its own along the lines pursued during the past two years (here Mr. Putin voices both an indirect criticism of the IMF and Western advice as well as a praise of the post-August 1998 pragmatic and centrist course initiated by Ye. Primakov). Mr. Putin has no quick fixes at hand and underlines the necessity of a broad political and social consensus for the required changes – the consensus which started to emerge after the August 1998 crisis. The Russians accept ideas of private property and free enterprise, but have own traditional values as well. These specifically Russian values include 'patriotism and national pride', belief in the 'greatness of Russia' and in a 'strong state', as well as 'paternalistic' sentiments. According

[16] See http://www.pravitelstvo.gov.ru, 27 December 1999. The non-profit fund 'Strategic Reform Centre' is headed by German Gref (first deputy minister of State Property) and staffed with experts from the Higher School of Economics, the Institute of Economic Forecasting of the Academy of Sciences, the Institute of Law and Comparative Legal Studies by the government, the Working Centre for Economic Reforms by the government and the Institute of Economic Analysis – see *Ekonomika i zhizn*, no. 2, 2000, p. 2.

to Mr. Putin, these are factors which – whether one likes it or not – make Russia 'special' and have to be reckoned with.

After the identification of the 'Russian idea', the first priority for Mr. Putin is to establish a strong (not totalitarian, as he explicitly says) state. Here his aim is to streamline the government apparatus, to intensify the fight against corruption and crime, to increase the authority of law and to improve the federative relations. The state must efficiently co-ordinate the economic and social policies and be more deeply involved in the economy. In order to foster economic growth, there is a need for more investment and for foreign investments in particular. The future industrial policy should focus on virtually everything: on high-technology sectors, domestic-market-oriented branches of the manufacturing industry and on export industries (energy and raw materials). Structural policy should focus on the development of large as well as medium-size and small enterprises and on the regulation of national monopolies. In the financial sphere, the budget, the tax reform and the non-payment problem should be addressed while maintaining low inflation and the stability of the exchange rate. Further tasks are the fight against the shadow economy and organized crime, and Russia's integration into the world economy. Last but not least, a modern agricultural policy should combine state involvement and regulation with market and ownership reforms in the countryside.

This ambitious and general programme appears to reflect the recently emerged Russian political and economic consensus. It is not exactly what the IMF would subscribe to but – if (and there is a big if) implemented – it could in principle form the foundation for a modest revival of the Russian state and economy. The starting conditions, including the likely new President Mr. Putin, are currently more favourable than in the past, but a sustained robust economic recovery would indeed require substantial improvements in the complex of factors which affect the investment climate; their implementation will definitely need time. For the coming two years, we thus expect only modest economic growth in the range of 2-3% per year as the current effects of better capacity utilization *cum* devaluation will gradually dry out before investment-led recovery may set in. With continued modest disinflation and strengthening of the rouble, domestic demand is expected to recover. The projected gradually declining current account surplus will not suffice to meet debt service obligations in full – a debt restructuring is needed.

Table RU

Russia: Selected Economic Indicators

	1995	1996	1997	1998 [1]	1998	1999	1999	2000	2001
					January-September		estim.	forecast	forecast
Population, th pers., end of period	147976	147502	147105	146714	.	.	146000	145500	145000
Gross domestic product, RUB bn, nom.	1540.5	2145.7	2521.9	2684.5	1850.7	3119.0	4500	6200	8000
annual change in % (real)	-4.1	-3.4	0.9	-4.6	-3.0	1.5	1.7	2	3
GDP/capita (USD at exchange rate)	2255	2835	3011	1882	.	.	1252	1253	1379
GDP/capita (USD at PPP - WIIW)	6605	6586	6804	6574	.	.	6812	.	.
Gross industrial production									
annual change in % (real)	-3.3	-4.0	1.9	-5.2	-3.7	7.0	8.1	3	3
Gross agricultural production									
annual change in % (real)	-8.0	-5.1	1.5	-12.3	-7.4	-2.0	2.4	.	.
Goods transport, bn t-kms	3533	3370	3256	3147	.	.	.	.	.
annual change in %	-1.0	-4.6	-3.4	-3.3	.	.	5.2	.	.
Gross fixed investment, RUB bn, nom.	267.0	376.0	408.8	402.4	262.9		.	.	
annual change in % (real)	-10.0	-18.0	-5.0	-6.7	-6.0	1.7	1	5	7
Construction output total									
annual change in % (real)	-9.0	-14.5	-6.4	-8.0	-3.6	0.5	3	.	.
Dwellings completed, th units	602.0	481.5	430.3	388.0	.	.	.	.	.
annual change in %	-1.5	-20.0	-10.6	-9.8	.	.	6	.	.
Employment total, th pers., average	66441	65950	64639	63642	63400	64333	65000	.	.
annual change in %	-3.0	-0.7	-2.0	-1.5	-1.5	0.9	2	.	.
Employment in industry, th pers., average	17182	16366	14893	14132	.	.	.	.	.
annual change in %	-7.5	-4.7	-9.0	-5.1	.	.	.	.	.
Unemployed reg., th, end of period [2]	6539	7280	8133	9728	8585	8650	8700	.	.
Unemployment rate in %, end of period [2]	9.0	9.9	11.2	13.3	11.9	11.7	12	12	12
Average gross monthly wages, RUB	532.6	790.2	950.2	1049.3	1058.9	1464.7	1575	.	.
annual change in % (real, gross)	-28.0	6.0	5.0	-13.0	-0.8	-32.4	-23.2	.	.
Retail trade turnover, RUB bn	554.2	763.8	887.2	1068.2	689.4	1214.2	1722.8	.	.
annual change in % (real)	-7.2	-2.8	4.0	-4.6	-0.8	-14.1	-7.7	.	.
Consumer prices, % p.a.	197.5	47.8	14.8	27.6	13.1	105.4	85.7	22	20
Producer prices in industry, % p.a.	236.5	50.8	15.0	7.1	3.4	54.6	59.8	45	30
General government budget, RUB bn									
Revenues	437.0	558.5	711.6	657.1	.	.	.	.	.
Expenditures	486.1	652.7	839.5	753.0	.	.	.	.	.
Deficit (-) / surplus (+)	-49.1	-94.2	-127.9	-95.9	.	.	.	.	.
Deficit (-) / surplus (+), % GDP	-3.2	-4.4	-5.1	-3.6	.	.	.	.	.
Money supply, RUB bn, end of period									
M1, Money	151.3	192.4	298.3	342.8	274.1	431.0	.	.	.
M2, Money + quasi money	275.8	357.3	457.2	628.6	520.0	823.5	.	.	.
Refinancing rate of NB % p.a., end of per.	160	48	28	60	60	55	55	.	.
Current account, USD mn	7736	12116	3924	2056	-4438	14579	17000	15000	10000
Gross reserves of NB, incl. gold, USD mn	17207	15324	17784	12223	12700	11212	12456	.	.
Gross external debt, USD mn	120500	125000	130800	145000	.	.	150000	.	.
Exports total, fob, USD mn [3]	81096	88599	88252	73871	54800	50800	73000	78000	82000
annual change in %	20.1	9.3	-0.4	-16.3	-13.3	-7.3	-1	7	5
Imports total, cif, USD mn [3]	60945	68828	73460	59573	49400	29500	42000	46000	55000
annual change in %	20.6	12.9	6.7	-18.9	-4.8	-40.3	-30	10	15
Average exchange rate RUB/USD	4.55	5.12	5.79	9.71	7.11	24.07	24.62	34	40
Average exchange rate RUB/EUR (ECU)	5.89	6.63	6.54	11.06	7.88	25.89	26.24	.	.
Purchasing power parity RUB/USD, WIIW	1.58	2.21	2.52	2.78	.	.	4.53	.	.

1) Preliminary. - 2) Based on Labour Force Survey data. - 3) Including estimate of non-registered trade.

Source: WIIW Database incorporating national statistics; WIIW forecasts.

Zdenek Lukas

Slovakia: Successful stabilization at the expense of employment

In Slovakia high GDP growth already set in as far back as 1994 thanks to an export boom. In subsequent years up to mid-1998 the Slovak koruna appreciated stepwise in real terms and the country's competitiveness deteriorated. Consequently, the current account shifted from an initial surplus to a deficit exceeding 10% of GDP. Gross foreign debt increased and accounted for over 60% of GDP at the end of 1998. With foreign trade losing its positive influence on growth, ambitious public projects and massive investments in large para-statal enterprises took over as the engine of growth. These enterprises also enjoyed easy access to foreign loans, backed up as they were by state guarantees.

Since taking up office in October 1998, the new cabinet has had to cope with an inordinately high external imbalance and a relatively low, but rapidly expanding state deficit. Given this situation, a special policy-mix emerged. The National Bank of Slovakia (NBS) switched to a floating exchange rate regime and the currency depreciated. The government introduced austerity measures designed to reduce domestic demand. As a result of this mix, both the current account[17] and budget deficits have diminished. At the same time, GDP growth has slowed down and the unemployment rate has increased considerably.

Standing at 19.2% or 535,000 persons, the unemployment rate reached an historic peak in December 1999: one of the highest unemployment rates in the transition countries. Apart from cutbacks in the construction sector, the rising unemployment figures reflect for the most part the decrease in the number of persons working in agriculture and industry. A major problem is that currently almost one third of the people under 35 are out of work. Furthermore, the average period of unemployment is on the rise, amounting to some 13 months per person. Funding unemployment benefits is proving increasingly difficult, further to which regional differences are also becoming more pronounced. Whereas the unemployment rate to the south in Rimavska Sobota is in excess of 30%, Bratislava reports a rate of only 5%.

Foreign trade re-emerged as a driving force of growth in the first three quarters of 1999, thus partially offsetting the decline in domestic demand. GDP rose by 1.8%. Given the depreciated domestic currency, which has been floating since 2 October 1998, exports of

[17] Whereas the current account deficit accounted for over 10% of GDP in 1996-98, in the first nine months of 1999 it was USD 0.8 bn or 5.7% of the GDP. Following some fluctuation, the foreign exchange (forex) reserves of the National Bank of Slovakia (NBS) rose to USD 3.5 bn on 12 January 2000, thus already providing coverage for four months of imports of goods and services.

goods and services have increased by 6.6% in real terms[18], while imports have dropped by 1.6%. The economic recovery enjoyed by those countries that constitute Slovakia's major trading partners has also supported export growth.[19]

As for domestic demand, private consumption rose only marginally (0.8%) between January and September 1999. Despite a rise in labour productivity (3.8%), real wages dropped by 1.9%. At the same time, gross fixed capital formation plunged by 15.8%. Within the framework of its austerity programme, the state drastically reduced funding of ambitious public works – primarily the building of motorways and the construction of the nuclear power station at Mochovce.

The austerity measures included a gradual increase in the ceilings set for regulated prices and the re-introduction of an import surcharge (in effect since 1 June 1999). These measures fuelled the inflation rate; in 1999 the consumer price index showed an increase of 10.5% year-on-year compared to 6.7% in the previous year. As of 1 January 2000, corporate income tax was lowered by 11 percentage points to 29 percent, and for certain firms a system was introduced whereby tax is to be paid in advance as a lump-sum. The government also reduced tax on lower individual incomes. The resultant decline in direct tax revenues is to be offset by higher levies on fuel, alcoholic beverages and cigarettes, while road tolls were increased, as were rents and heating costs in municipal housing. The central government deficit amounted to SKK 14.8 bn or 1.9% of GDP in 1999 compared to 2.7% in 1998. The general government deficit (central government, social security funds, local governments and extra-budgetary funds) may have dropped to below 4% of GDP in 1999 compared to 6% of GDP in 1998.

The construction sector was especially hard hit by the austerity programme. In the period January–September 1999, output in the construction sector plunged by 28% and the number of workers laid off soared. It is not quite clear whether this development is also reflected in the performance of the industrial sector. For the first three quarters of 1999, official statistical sources report a decline in gross industrial output (-6.3%) and at the same time a marked rise (9.6%) in industrial value-added. The rise in value-added coupled with a drop in gross industrial production would seem to indicate that the consumption of intermediate goods (material consumption) contracted very sharply relative to gross production. A sudden shift of this order would presuppose a massive short-term change in the composition of aggregate output, industrial restructuring or innovation. It is most unlikely that anything of the kind occurred in the period from1998 to 1999, as over that

[18] As a result of the depreciation of the Slovak koruna, the appreciable rise in exports as shown in GDP statistics, 6.6% at constant 1995 prices, contrasts with a sharp decline (-7.3%) in exports of goods in USD at current exchange rates (see SK country table).

[19] In the case of the Czech Republic, Slovakia's second most important trading partner, recovery was only rudimentary.

period the country experienced a slump in investment and only modest FDI inflow.[20] A small number of FDI companies, led by VW Bratislava, are performing excellently, but the increase in their value-added can hardly offset the worsening performance of the many (mostly domestic-owned) firms that now face growing financing problems. According to the Ministry of Economy, inter-company indebtedness continued to rise although in industrial firms employing more than 20 employees total pre-tax profits more than doubled, rising to over USD 500 mn in the first nine months of 1999.[21] It is quite probable that for the most part profits may have fallen in the domestic segments of industry, while FDI companies have succeeded in making full use of improved export possibilities.

Weaker economic growth and the firms' financial difficulties have had a negative effect on the banking sector as a whole, yet mostly on the three state-owned banks which have a high proportion of bad debts. As a result, the entire banking sector is becoming increasingly fragile, and the risk of a domino effect is increasing. Over three-quarters of the Slovak enterprises' capital needs are met by debt financing: a share that is significantly higher than that customary in Western countries. Furthermore, the primary source of credit are the loan facilities granted by commercial banks, whereas financial institutions such as the stock exchange, insurance and pension funds are underdeveloped. This fact has merely heightened the economy's vulnerability to knock-on effects. The most pressing tasks are a comprehensive restructuring of the financial sector accompanied by a realistic evaluation of the banks' assets and the preparation of all three state-owned banks for privatization. For this particular issue and in keeping with EU directives, the cabinet has selected White & Case Co. as its legal advisor and the J. P. Morgan investment bank as its financial advisor.[22] Before privatizing the three banks, the share of classified loans should drop to about 15-20% from the current level estimated at 38%.[23] Konsolidacná Banka, the sole state-owned bank specialized in collecting state debts, is heavily involved in this matter. The procedure started at the beginning of December 1999 as a result of which the banks' assets have increased by SKK 14 bn. Altogether, restructuring will cost an estimated SKK 93 bn (over USD 2 bn) or more than 10% of the GDP.

External imbalance will probably remain a matter of concern. The massive currency devaluation prior to May 1999 and the introduction of an import surcharge have reduced the foreign trade deficit considerably.[24] That notwithstanding, the currency has since re-appreciated, and in mid-January 2000 the nominal exchange rate vis-à-vis the EUR was

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[20] Amounting to a total of about USD 2.2 bn at the end of 1999, FDI in Slovakia is very low compared to Hungary, the Czech Republic and Poland.

[21] *Trend* (weekly), 12 January 2000, p. 4.

[22] *Hospodarske Noviny,* 10 January, 2000, p. 11.

[23] *Trend,* 15 September 1999, p. 4C.

[24] By USD 1.2 bn to USD 1.1 bn in 1999.

nearly back to the level of 2 October 1998, the day on which floating was first introduced.[25] If this trend continues, it will adversely affect the country's competitiveness and reduce its ability to benefit from the improving business climate in Europe. In order to check further appreciation, the NBS has intervened several times in the market. Nonetheless, some foreign investors are showing trust in the austerity measures introduced by the cabinet. They have taken note of the high interest rates and are confident that the Slovak koruna will remain stable, if not gain. Financiers investing in SKK on a short-term basis, take into particular account the present daily and monthly levels and current trends displayed by the interest and exchange rates. Recently, they achieved yields of some 2% per month. The Monetary Programme 2000 launched by the NBS envisages a decrease in interest rates, and corresponding expectations could stabilize or even weaken the exchange rate.[26]

Increases in regulated prices and the import surcharge (despite its being reduced from 7% to 5% on 1 January 2000) will push the average inflation rate upwards to close on 13% this year. Given the current austerity measures, GDP will stagnate this year. Only in 2001 does the WIIW expect growth to resume. Stagnation will keep the unemployment rate at a level of 19% this year. In all probability it will only decrease to any substantial degree a few years hence in the context of Slovakia's EU accession. Slovakia was invited to join the broader group of EU candidates at the Helsinki Summit in December 1999. Given favourable progress in the corresponding preparations and negotiations over the next few years, the country will start to attract more FDI. This improvement together with the accession-related influx of EU funds will also have a positive impact on employment and growth.

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[25] After massive depreciation of 16% prior to mid-May 1999, the koruna appreciated by 10.5% to SKK 42.32/EUR on 17 January 2000.

[26] The programme foresees an increase in M2 money supply of 9.3%. It expects the volume of loans granted to firms and households to expand by 3.4% and counts on a core inflation rate (excluding from the consumer basket items with regulated prices and the impact of changes in taxation) of 4.5% to 5.8%. See T*rend,* 5 January 2000, p. 5.

Table SK

Slovak Republic: Selected Economic Indicators

	1995	1996	1997	1998 [1]	1998	1999	1999	2000	2001
					January-September		estim.	forecast	forecast
Population, th pers., mid-year	5363.7	5373.8	5383.2	5390.7	.	.	5395	.	.
Gross domestic product, SKK bn, nom.	516.8	575.7	653.9	717.4	535.4	579.2	770	850	940
annual change in % (real)	6.9	6.6	6.5	4.4	5.8	1.8	2	0	2
GDP/capita (USD at exchange rate)	3240	3495	3613	3778	.	.	3451	.	.
GDP/capita (USD at PPP - WIIW)	8026	8784	9543	10049	.	.	10418	.	.
Gross industrial production									
annual change in % (real)	8.3	2.5	2.7	5.0	6.4	-6.3 [2]	-5	-1	0
Gross agricultural production									
annual change in % (real)	2.3	2.0	-1.0	-3.1	.	.	.	.	.
Goods transport, mn t-kms [3]	20390	18721	17672	18031	.	24989	.	.	.
annual change in % [3]	13.3	-8.2	-5.6	2.0	.	6.0	.	.	.
Gross fixed capital form., SKK bn, nom. [4]	141.5	212.7	252.7	292.4	196.9	178.6	.	.	.
annual change in % (real) [4]	5.3	39.8	14.5	11.0	12.5	-15.8	-15	0	5
Construction industry									
annual change in % (real)	2.9	4.4	9.2	-3.5	3.6	-28.0	.	.	.
Dwellings completed, units	6157	6257	7172	8234	.	.	10500	.	.
annual change in %	-8.2	1.6	14.6	14.8	.	.	.	.	.
Employment total, th pers., average	2019.8	2036.4	2040.9	2032.1	2029.2	1990.2	.	.	.
annual change in %	2.2	0.8	0.2	-0.4	-0.3	-1.9	.	.	.
Employment in industry, th pers., average	621.2	621.2	608.9	583.9	587.7	569.4	.	.	.
annual change in %	4.1	0.0	-2.0	-4.1	-3.6	-3.1	.	.	.
Unemployed reg., th, end of period	333.3	329.7	347.8	428.2	385.8	497.5	535.2	.	.
Unemployment rate in %, end of period [5]	13.1	12.8	12.5	15.6	13.8	17.8	19.2	19	18
Average gross monthly wages, SKK	7195	8154	9226	10003	9600	10302	.	.	.
annual change in % (real, gross)	4.0	7.1	6.6	2.7	2.8	-1.9	.	.	.
Retail trade turnover, SKK bn	262.1	296.5	328.8	379.4	276.8	324.1	.	.	.
annual change in % (real)	2.0	7.0	4.6	8.2	9.1	7.0	.	.	.
Consumer prices, % p.a.	9.9	5.8	6.1	6.7	7.0	9.3	10.5	13	10
Producer prices in industry, % p.a.	9.0	4.2	4.5	3.3	3.8	2.6	3.6	.	.
Central government budget, SKK bn [6]									
Revenues	163.1	166.3	175.8	177.8	131.2	140.9	216.7	.	.
Expenditures	171.4	191.9	192.8	197.0	139.6	153.3	231.5	.	.
Deficit (-) / surplus (+)	-8.3	-25.6	-17.0	-19.2	-8.4	-12.4	-14.8	.	.
Deficit (-) / surplus (+), % GDP	-1.6	-4.4	-2.6	-2.7	-1.6	-2.1	-1.9	.	.
Money supply, SKK bn, end of period									
M1, Money	148.4	173.9	166.1	147.2	149.0	138.2	.	.	.
M2, Money + quasi money	357.0	416.9	453.5	466.1	446.7	494.4	.	.	.
Discount rate, % p.a., end of period	9.8	8.8	8.8	8.8	8.8	8.8	.	.	.
Current account, USD mn	391	-2098	-1929	-2063	-1542	-791	-1000	-800	-500
Gross reserves of NB incl. gold, USD mn	3418	3473	3285	2923	3110	2935	3422	.	.
Gross external debt, USD mn	5827	7810	10700	11800	11900	10363	.	.	.
Exports total, fob, USD mn [7]	8579.0	8829.0	8252.1	10670.5	7912.7	7339.0	10211	10500	10800
annual change in %	28.2	2.9	-6.5	10.7	10.3	-7.3	-4.3	3	3
Imports total, fob, USD mn [7]	8770.5	11121.0	10261.9	12963.8	9539.8	8131.0	11316	11500	11600
annual change in %	32.7	26.8	-7.7	11.1	9.1	-14.8	-12.7	2	1
Average exchange rate SKK/USD	29.74	30.65	33.62	35.23	34.95	41.32	41.36	44	47
Average exchange rate SKK/EUR (ECU)	38.45	38.41	37.96	39.58	38.55	44.42	44.10	.	.
Average exchange rate SKK/DEM	20.76	20.39	19.41	20.06	19.51	22.71	22.55	.	.
Purchasing power parity SKK/USD, WIIW	12.00	12.20	12.73	13.24	.	.	13.70	.	.

1) Preliminary. - 2) According to EU methodology. - 3) Up to 1998 enterprises with 20 and more persons, from 1999 all organizations including those which do not have their main activity in transport. - 4) Based on GDP concept. - 5) From 1997 new methodology. - 6) From 1997 according to IMF methodology. - 7) Converted from the national currency to USD at official exchange rate, from 1998 new methodology.

Source: WIIW Database incorporating national statistics; WIIW forecasts.

Hermine Vidovic

Slovenia: Continuing on a path of moderate growth

The introduction of the VAT in mid-July 1999 had a far-reaching impact on Slovenia's economic performance. Driven by excessive domestic demand – in anticipation of VAT being introduced – GDP growth accelerated to 6.4% in the second quarter of the year, after a 2.4% increase in the first three months. It settled down to 3.5% in the third quarter. Thus, the first nine months of 1999 ended up with a 4.1% GDP growth as against the same period a year previous.

The whole year may close with a 3.5-4% growth. Foreign trade contributed negatively to this result; it showed the largest deficit for years and the current account closed with a record deficit (about 2.5% of the GDP expected).[27] Investment is estimated to have increased by some 14% in real terms in 1999, thus stimulating growth.[28]

A substantial increase in effective working hours in the construction sector (10%) and impressive production growth after several years of stagnation or even decline reflected soaring investment. Output increases went hand in hand with rising employment and wages, but also with a steep rise in labour productivity. Besides construction, the most markedly growing sectors were financial inter-mediation, energy and real estate. Retail trade turnover increased by about 3% in the January-September period, with car sales up by 27%. On the supply side, the decisive impetus for economic growth in 1999 came from favourable results achieved in the services and construction sectors.

Industrial production performance remained weak, though showing some signs of recovery in the second half of the year. Industry suffered from weak foreign demand, especially from the EU, but also from Russia and neighbouring Croatia, one of Slovenia's major trading partners. In addition low growth in labour productivity combined with a rise in real wages have further diminished the cost competitiveness of the manufacturing sector. During the first eleven months of 1999 industrial production fell by 1.3%, with production of capital goods up by 0.8%, while the output of intermediate goods and consumer goods fell by 0.5% and 3.2%, respectively. Manufacturing output remained almost stagnant over the same pre-year period. Only a few sub-sectors reported an increase in output: e.g. manufacture of coke, petroleum products and nuclear fuel (17.1%), manufacture of other non-metallic mineral products (4.5%) and manufacture of electrical and optical equipment (3.7%). The most pronounced declines were reported for the manufacture of leather and

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[27] In 'normal' years the current account ended up balanced or even showed a small surplus.

[28] See Institute for Macroeconomic Analysis and Development (IMAD), Autumn Report 1999, Ljubljana.

leather products (-21%) and the manufacture of textiles and textile products (-7%). Labour productivity slightly increased mainly on account of continued layoffs.

The introduction of VAT had only a minor impact on inflation. At the end of the year with an average annual inflation rate of 6.1%, Slovenia fell short of the rate (6.8%) the government had targeted at the beginning of 1999.

Real wages grew at a rate higher than the government target of 2%; during the first eleven months of 1999, real gross and net wages increased by 3% and 2.8%, respectively, as against the same pre-year period. The recent wage jump registered in November raises doubts whether the newly adopted Wage and Wage Adjustment Mechanism Act for the 1999-2001 period is as efficient as its forerunner.

Total employment increased by 1.6% compared with the first eleven months of 1998. Except for July, unemployment fell throughout the year. The number of registered jobless amounted to 114,700 persons (equivalent to a 13% unemployment rate) in November 1999. Apart from June and July 1996,this is the lowest level ever reached since late 1992. The increase in employment and the decrease in unemployment are partly the result of methodological changes in statistics: from 1999 onwards, persons participating in subsidised employment and in public work programmes are treated as being employed, unlike previously when they were registered as unemployed. Data obtained from the latest LFS (September) confirm the downward trend in terms of unemployment, but it is less pronounced than that shown in registration data. In contrast to registration data, employment measured using the same methodology shows a decline of -1.8% between the third quarters of 1999 and 1998. At the same time, the number of inactive persons increased by 4.5%.

Foreign trade showed divergent trends during the year. Available data for the first eleven months expressed in current USD suggest that an earlier export stagnation turned into a drop of 5.9%, while imports shifted from a 7% increase in the first half of 1999 to a decline of 2.1% in the January-November period. The turnaround was especially pronounced in trade with the EU: after reporting a 5% increase in the first half of the year, exports to the EU area went down by almost the same amount during the first eleven months. Among the main trading partners within the EU, the drop in experts was felt most in trade with France: almost 40% as against the same period a year earlier. The decline was mainly due to a drop in car deliveries (from Revoz, the main producer of the Renault Clio) to France. On the other hand exports to Germany – Slovenia's main trading partner – increased by 2%. In trade with the Yugoslav successor states exports were down by 7.5% (mostly due a 18%

drop in export trade with Croatia) and to Russia by roughly 50%.[29] As result of exports contracting more than imports, the trade deficit widened to USD 1.2 bn in the January–November period 1999, from USD 900 mn over the same period in the previous year. The increased deficit led to the highest current account deficit since gaining independence; it increased to USD 463 mn in the first eleven months of the year (from USD 48 mn in the same 1998 period). As for 1999 as a whole, the current account deficit may increase to about USD 500 mn, which is almost more than double the value anticipated by the Slovenian government. Apart from merchandise trade, trade in services also deteriorated compared with the previous year, primarily on account of the decline in revenues from tourism. Overnight stays of tourists fell by 5%, those of foreigners dropped by even as much as 12% (of which Germans by 20% and Italians by 11%). The drop in earnings from tourism was only partly due to the Kosovo conflict. The main reasons for this decline have their roots in the drop in revenue from duty free shops and 'petrol tourists' (especially from Italy and Austria), the decrease of cross-border shopping by Croatian citizens and the greater outlays by Slovene tourists abroad compared to the previous year. As in previous years, the inflow from foreign direct investment was negligible; it amounted to a mere USD 77 mn during the first eleven months of 1999. In order to offset sluggish FDI inflow, the Slovene government only recently adopted a programme to 'encourage' foreign investments. Information made available on the programme thus far creates more the impression of good intentions than of real action.

Having experienced an excess supply of foreign exchange since 1991, 1999 marked a turning point. In November 1999 the excess demand for foreign exchange was close to DEM 700 mn. This development can be partly explained by foreign exchange flows to the new foreign exchange accounts opened by the enterprise sector that became possible by virtue of the new Foreign Exchange Law that entered into force on 1 September 1999. Up until mid-December the foreign exchange deposited in these accounts increased to an equivalent of DEM 400 mn.[30] As a result of the strong domestic demand, but also on account of the rise in the US dollar, the Slovenian tolar depreciated in the first half of 1999. The fall of the tolar came to a halt in July after the Bank of Slovenia had imposed an intervention selling rate for euros and German marks. In the three months thereafter, the real effective exchange rate (deflated both with the CPI and PPI) increased, but weakened (slightly) once again in November.

The 1999 general government budget closed with a small deficit (reportedly less than 1% of GDP). A deficit of a similar magnitude is also envisaged for 2000, based, *inter alia*, on

[29] The share of Slovene exports to France as a percentage of total exports fell to 5.6% in the first eleven months of 1999, from 8.5% in the corresponding 1998 period. At the same time the share of exports to Germany went up to 30.8%, from 28.4% a year earlier. Exports to Croatia accounted only for 8% of Slovenia's exports, down from 9.2% in 1998.

[30] See F. Štiblar, 'Slovenia: Economic and Financial Developments and Comparison with other EU-candidates', paper presented at a WIIW Seminar, on 17 December 1999.

the assumption of a 3.75% growth in GDP, an annual inflation rate of 6.2% and a moderate current account deficit (about 0.8% of GDP). Apart from the major items, budgetary expenditures will focus on agriculture, regional development, employment and technology.

In 1999 some major changes in the country's financial legislation entered into effect upon the adoption of the new Banking Law (granting foreign competitors access to that sector, for example, by establishing branches of foreign banks); the Securities Market Law (permitting, *inter alia*, the establishment of foreign brokerage houses); and the Foreign Exchange Law (liberalising capital flows in accordance with the provisions of the Europe Agreement).

Apart from these achievements in the legal sphere, enterprise restructuring and privatisation of State-owned enterprises and banks remain weak points.[31] The (partial) privatisation of the country's two largest banks Nova Ljubljanska Banka (NLB) and Nova Kreditna Banka Maribor (NKBM) announced in July 1999 have failed to materialise. According to the president of the NKMB management board, bank privatisation in Slovenia will not start in 2000 either, because there is no chance of achieving political consensus prior to the parliamentary elections due at the end of the year. The bank located in Maribor just recently announced a merger with SKB, the third largest Slovenian bank, which will become effective on 1 January 2001. Currently, the two banks have a market share of about 12%, while that of NLB is about 35%.[32] After three years of debate, the Slovenian parliament adopted a new Law on Pension and Disability Insurance (three pillar system), which will enter into effect as of 1 January 2000.

Given the favourable forecasts for the EU in 2000-2001, WIIW expects the Slovene economy to grow by 3.5-4% in 2000. A similar growth rate seems feasible for 2001. The annual inflation rate may remain at about 6% as some price adjustments are still in the offing. Additional pressure on prices may come from an increase in the world market oil prices, but also from wages if the current upward trend cannot be checked. The current account may remain negative owing to the weakness of the composition of the trade in services, especially tourism as stated above, but also on account of insufficient competitiveness in merchandise exports. Future economic developments in neighbouring Croatia will have an additional impact on Slovenia's external performance. A decisive change in the current (floating) exchange rate regime cannot be expected in 2000.

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31 State-owned companies (e.g. public utilities) and non-privatised firms (e.g. to a big part loss-making enterprises under the umbrella of the Slovenian Development Corporation) still play a significant role in Slovenia's economy, accounting for more than 40% of total assets. See also, European Commission, 1999 Regular Report on Slovenia's Progress towards EU Accession.

32 An attempt by NKBM to merge with NLB – a letter of intent was signed in March 1998 – failed, being vetoed by both the Bank of Slovenia and the government.

Table SI

Slovenia: Selected Economic Indicators

	1995	1996	1997	1998	1998	1999	1999	2000	2001
					January-September		estim.	forecast	forecast
Population, th pers., mid-year	1987.5	1991.2	1986.8	1982.6	.	1986.6	1990	.	.
Gross domestic product, SIT bn, nom.	2221.5	2555.4	2907.3	3243.5	.	.	3570	3910	4250
annual change in % (real)	4.1	3.5	4.6	3.9	4.1	4.1	3.7	3.7	4
GDP/capita (USD at exchange rate)	9431	9481	9163	9847	.	.	9869	.	.
GDP/capita (USD at PPP - WIIW)	12439	13220	14151	14889	.	.	15633	.	.
Gross industrial production									
annual change in % (real)	2.0	1.0	1.0	3.7	4.5	-1.8	-1	2	2
Gross agricultural production									
annual change in % (real)	0.1	0.7	-0.6	2.1	.	.	.	.	.
Goods transport, mn t-kms	22595	22371	22563	22013	16470	17415	.	.	.
annual change in %	-2.8	-1.0	0.9	-2.4	-4.5	5.7	.	.	.
Gross fixed capital form., SIT bn, nom. [1)]	475.0	576.7	684.1	785.2	.	.	.	.	.
annual change in % (real) [1)]	16.8	9.2	11.3	12.9	.	.	14	8	.
Construction output, in effect. working time									
annual change in % (real)	0.9	-2.5	-5.2	1.7	1.2	9.8	10	.	.
Dwellings completed, units	5715	6228	6085	.	.	.	.	.	.
annual change in %	3.5	9.0	-2.3	.	.	.	.	.	.
Employment total, th pers., average	745.2	741.7	743.4	745.2	745.8	755.1	.	.	.
annual change in %	-0.1	-0.5	0.2	0.2	0.4	1.2	.	.	.
Employees in industry, th pers., average [2)]	252.4	239.2	248.5	246.2	226.4	222.4	.	.	.
annual change in %	-4.9	-5.2	-2.1	-0.9	-1.6	-1.8	.	.	.
Unemployed reg., th, end of period	126.8	124.5	128.6	126.6	124.7	115.3	.	.	.
Unemployment rate in %, end of period	14.5	14.4	14.8	14.6	14.3	13.1	13	12	12
Average gross monthly wages, SIT	111996	129125	144251	158069	155709	169486	.	.	.
annual change in % (real, net)	4.7	4.4	2.9	1.5	1.3	2.9	.	.	.
Retail trade turnover, SIT bn	705.8	871.3	1336.8	1610.2	.	.	.	.	.
annual change in % (real)	3.1	2.9	1.0	1.9	1.3	5.2	.	.	.
Consumer prices, % p.a.	13.5	9.9	8.4	7.9	8.4	5.6	6.1	5.5	4.5
Producer prices in industry, % p.a.	12.8	6.8	6.1	6.0	6.8	1.7	2.1	.	.
General government budget, SIT bn									
Revenues	958.2	1091.8	1222.6	1397.9	.	.	.	.	.
Expenditures	957.3	1083.6	1256.7	1423.5	.	.	.	.	.
Deficit (-) / surplus (+)	0.9	8.2	-34.1	-25.6	.	.	.	.	.
Deficit (-) / surplus (+), % GDP	0.0	0.3	-1.2	-0.8	.	.	.	.	.
Money supply, SIT bn, end of period									
M1, Money	203.9	235.1	270.5	332.7	307.4	371.2	.	.	.
Broad money	941.9	1135.3	1411.3	1689.5	1595.0	1856.1	.	.	.
Discount rate % p.a., end of period	10.0	10.0	10.0	10.0	10.0	8.0	8.0	.	.
Current account, USD mn	-22.8	39.0	36.6	-3.8	51.3	-439.4	-500	-250	-250
Gross reserves of NB excl. gold, USD mn	1820.8	2297.4	3314.7	3638.5	3821.8	3195.3	3158.8	.	.
Gross external debt, USD mn [3)]	2970	4010	4176	4935	4877	5584	.	.	.
Exports total, fob, USD mn	8315.8	8309.8	8368.9	9051.0	6582.1	6272.7	8500	8800	9200
annual change in %	21.8	-0.1	0.7	8.2	7.3	-4.7	-6	4	5
Imports total, cif, USD mn	9491.7	9421.4	9366.5	10111.0	7324.0	7290.0	9900	10200	10400
annual change in %	30.0	-0.7	-0.6	7.9	5.6	-0.5	-2	3	2
Average exchange rate SIT/USD	118.52	135.37	159.69	166.13	168.68	179.19	181.77	188	.
Average exchange rate SIT/EUR (ECU)	153.12	169.51	180.40	186.27	185.85	192.59	193.63	.	.
Purchasing power parity SIT/USD, WIIW	89.86	97.08	103.40	109.88	.	.	114.75	.	.

1) Based on GDP concept. - 2) Up to 1996 excluding persons employed by self-employed in enterprises with 3 and more employees. Quarterly data refer to enterprises with 3 and more persons. - 3) Up to 1995 excluding portion of debt of the former Yugoslav Federation.

Source: WIIW Database incorporating national statistics; WIIW forecasts.

Helen Boss

Ukraine: New government faces debt, energy crises

President Leonid Kuchma got his second five-year term and the new millennium off to a good start by nominating and getting parliament to approve leading reform politicians to key posts. The century date change took place without major embarrassment at Chernobyl or elsewhere in the power, coal and transport sectors. The well-regarded 45-year-old long-term head of the National Bank, Viktor Yushchenko, was confirmed as prime minister, and Serhiy Tyhypko is to lead an expanded Ministry of the Economy. Agricultural reforms to be put in place by April are to institute 'principles of land ownership' in the kolkhoz sector. Kuchma was cautioned in Washington in December to keep several corruption-tainted officials out of the policy-making process. Both Russia and Ukraine appear to be shifting power from 'fathers of their country' with mixed legacies towards younger leaders who are pro-market, realistic and 'patriotically' interested in tackling corruption and non-payment, 'even' in the energy sector. President Kuchma has announced a referendum for 16 April with six questions; if the vote goes his way, there could be new parliamentary elections, introduction of a tame upper house, and an end to MPs' immunity from prosecution. Thanks to Ukraine's parlous financial situation, with a minor default on 20 January and crisis negotiations with many scattered creditors in full swing, the new government has had a short honeymoon.

The economy appears to be turning around, though this may reverse if the financial strains worsen or if energy supplies are cut. GDP results were revised upwards throughout 1999, primarily because of the effect on industry of the over 60% devaluation of the hryvnia–dollar exchange rate since August 1998. Ukraine's recorded GDP growth went from minus 4.8% in January–March year-on-year to -3% in the first half, -1.7% in January–September, and -0.4% according to preliminary official data for the year as a whole. If the country manages to pass a budget acceptable to the IMF and to reschedule its foreign-currency debts to IFIs and western banks, continuation of the trend could mean 2000 records the first positive GDP growth in Ukraine since 1989.

Restructuring to date has taken the form of huge falls in output and man-hours, mainly in 1992-94. Effective employment in industry dropped 33% (by 1.85 mn workers) during Kuchma's first term; real wages were fairly stable but at about 33-35% of the 1990 level. Food production for own consumption plus transfers and other non-wage income failed to compensate: real consumption slumped over a fifth 1994-1998 (6% in the first half of 1999 year-on-year). Over 60% of the population are living in poverty according to a World Bank study. Population continues to fall.

Industrial production picked up in 1999. Preliminary official results indicate 4.3% real growth for the year, up from 2.3% in January–September. Measured output rose 6.6% year-on-year in electricity generation, 6.2% in ferrous metals, 8.9% in nonferrous metals, 23.6% in forest products, 5.7% in light industry and 7.8% in the food industry. Output continued to slump in the fuel sector, in chemicals including petrochemicals, and in machine-building and construction materials – the latter two unsurprisingly, given ongoing capital flight, depressed real investment and dismal sales of Daewoo passenger cars.

Agriculture, where Ukraine has potential comparative advantage, remains a shocking mess. Harvests and livestock herds have fallen by half since independence; the 1999 harvest came in at 24.4 mn t, below even the disastrous 1998 one, and 2000 may not be much better, though the minister has promised 35 mn t. Some 85% of kolkhozes are loss-making, in part because prices are distorted: input costs are as much as double world levels, reflecting the high risk of non-payment; output prices are artificially held down to 80-90% of world by remnants of the state order system. From being the breadbasket of the USSR, Ukraine has announced it may import 700,000 t of grain in 2000. Barter predominates, accounting for 56% of sales of sunflower seeds, 43% of sugar, 39% of sugarbeets and 34% of grains in January–September 1999, payment in kind being one way for loss-making farms to repay the state for advances of seed, fertilizer and diesel fuel. Kuchma's December 1999 decree gives ex-kolkhozniks the right to buy extra land, but says nothing about sale of that land or the right to pledge it as collateral – a major bone of contention between the IMF and World Bank and Ukraine, and between the new government and parliament.

The hryvnia has lost another nearly 15% of its value since the election, but remains revalued vis-à-vis the rouble cf. the situation prior to August 1998. Trade is finally adjusting to this, after showing some perverse trends earlier in 1999. According to preliminary official data for January–November, goods exports to the far abroad were down 3.3% year-on-year. Goods exports to the CIS, over half of which traditionally go to Russia, continued what is now several years of decline, falling 25% year-on-year in response to Russian protectionism and campaigns against non-payment, barter and tolling, but also to Ukraine's diminished competitiveness. Goods imports were down 29% with the ROW and 15% with the CIS. Energy dependence on Russia has barely fallen percentage-wise: about half of goods imports came from Russia in the first nine months; about half of goods imports by type were mineral products. The new Deputy Prime Minister in charge of fuel and energy, ex-Lazarenko associate Yulia Tymoshenko, caused a stir by stating that Ukrainian entities owe RAO Gazprom a total of USD 2.8 bn, not just the USD 780 mn maintained by Naftohaz head Bakai for the state company alone. President Kuchma is reportedly being pressured to declare a three-month state of emergency in the energy sector to boost his credibility in gas-debt talks with Russia and because the power grid is at risk of breakdown.

Official denials notwithstanding, there were some extra emissions to clear wage and pension arrears before the election. The consolidated budget deficit as of November was miles above target, and there was a price surge at yearend: consumer prices rose 19.2% in January–December 1999, several percentage points above the October official forecast for the year.

Ukraine's fragile financial situation is ultimately due to failure to harden budget constraints. In hybrid-economy fashion, factories, coal mines, electric utilities, central and local budget organizations, and households suffer few penalties if they pay late or not at all, or offer vouchers, tax offsets or overpriced barter goods in lieu of cash. The vast shadow economy does not pay taxes, rent or utility bills. Enterprise payables barely budged as a share of GDP in the first nine months of 1999, unlike in Russia, where they were much reduced. The IMF and the new economy ministers readily admit that the state itself is a prime generator of the non-payment cycle. Tax collections are regularly 15-20% below planned expenditures, but commitments to fund schools, hospitals, pensions and subsidies to agriculture and industry are not reduced in tandem. The state is both big and ineffective. Deputy Prime Minister Tyhypko has said the number of ministries and central government regulatory agencies should be halved, from over 80 at yearend; the new cabinet has 15 ministries, down from 18.

Parliament has rejected the second draft budget but gone on recess rather than revising it. Before unfreezing the EFF loan, the IMF insists on passage of a realistic budget as well as: cuts in the size and scope of the central government, reductions in tax loopholes particularly those giving special treatment to energy, agriculture and particular regions, removal of certain export restrictions, a plan for large privatization, and a prior deal with private creditors to restructure the eurobonds. Principal and interest payments totalling USD 3.04 bn fall due in 2000, USD 800 mn of which to the eurobond lenders in January, February and March; USD 480 mn in interest and principal is owed to energy suppliers, and USD 1.1 bn to IFIs, plus an additional USD 1 bn to private creditors in February 2001.

The slumping hryvnia is complicating these negotiations: even were it to recover back to 5 to the USD from 5.5, debt service due in 2000 would exceed 35% of second-draft budget revenues and nearly 10% of projected 2000 GDP unless it is rescheduled. On 20 January 2000 Ukraine failed to make a USD 18 mn payment on a Chase Manhattan note, though the grace period may prevent cross-default clauses from being invoked. Liquid reserves at yearend stood at a paltry USD 1.16 bn and have since fallen further. Negotiations with western banks under lead-manager ING Barings, with the IMF, and with Russia/Gazprom are set to go to the wire.

Were its immediate financial crisis to be resolved, Ukraine would still face a difficult balancing act in its relations with the west and Russia. The dilemma is real since Russia is too big, too unreformed and, some say, too 'Eurasian' to have any prospect of trying for EU membership itself. In theory Russia could be an attractive market for Ukrainian food exports, if there were any. Since January 1999 Ukraine has shared a border with NATO, two of whose new members are first-round EU accession countries. This has pointed up sorry contrasts in both initial conditions and policy achievements between Ukraine and its western neighbours. Poland e.g. has created 2 mn small businesses since 1989, cf. Ukraine's 200,000. Ukraine's westernized elite dreams of qualifying to be asked to begin accession talks in Brussels, a notion ridiculed in November by Enlargement Commissioner Verheugen. At the Helsinki summit on 11 December, the EU adopted a resolution welcoming Ukraine's 'pro-European choice' but was silent on the issue of membership. President Kuchma and his new government must prove they are serious about reform if those attitudes are ever to change.

Table UA

Ukraine: Selected Economic Indicators

	1995	1996	1997	1998 [1]	1998 January-September	1999 January-September	1999 estim.	2000 forecast	2001 forecast
Population, th pers., end of period	51334.1	50894.0	50499.9	50105.6	.	.	49700	49500	.
Gross domestic product, UAH mn, nom.	54516	81519	93365	103869	70333	92324	123300	148300	183000
annual change in % (real)	-12.2	-10.0	-3.0	-1.7	-0.5	-1.7	-0.4	1	3
GDP/capita (USD at exchange rate)	721	876	993	846	.	.	620	500	.
GDP/capita (USD at PPP - WIIW)	3576	3339	3333	3335	.	.	3376	.	.
Gross industrial production									
annual change in % (real)	-11.7	-5.1	-1.8	-1.5	-0.3	2.3	4	2.5	5.0
Gross agricultural production									
annual change in % (real)	-3.6	-9.5	-1.9	-8.3	1.8	-2	-2	0	.
Goods transport, bn t-kms	544.0	450.3	402.3	392.3	289	272.5	.	.	.
annual change in %	-8.3	-17.2	-10.7	-2.5	-0.1	-6.0	.	.	.
Gross fixed investment, UAH mn, nom.	9378.2	12557.0	12437.0	11543.0	7296	8890.1	.	.	.
annual change in % (real)	-35.1	-22.0	-8.6	4.8	6.0	-4.1	2.9	2	8
Construction output total									
annual change in % (real)	-35.2	.	.	.	.	.	.	.	.
Dwellings completed, units	118200	88100	80000	67100			.	.	.
annual change in %	-18.7	-25.5	-9.2	-16.1	.	17 [2]	.	.	.
Employment total, th pers., average	23725.5	23231.8	22597.6	22348.7	.	.	22000	21500	21000
annual change in %	3.0	-2.1	-2.7	-1.1	.	.	.	.	.
Employment in industry, th pers., average	5800.0	5300.0	4882.2	4700.0	.	.	.	.	.
annual change in %	-7.9	-8.6	-7.9	-3.7	.	.	.	.	.
Unemployed reg., th, end of period	126.9	351.1	637.1	1003.2	866.5	1124.1	1205	.	.
Unemployment rate in %, end of period	0.5	1.3	2.3	3.7	3.2	4.1	5	6	8
Average gross monthly wages, UAH	80.6	137.8	156.2	167.5	164.4	187	.	.	.
annual change in % (real, gross)	10.1	-5.1	-2.3	-3.0	-0.3	-8.4	.	.	.
Retail trade turnover, UAH mn [3]	11964.0	17344.4	27300.0	29200.0	.	.	.	.	.
annual change in % (real)	-13.9	-5.1	2.2	-4.0	.	-6.8	-5.4	.	.
Consumer prices, % p.a.	376.8	80.2	15.9	10.6	8.1	24.2	19.2	20	20
Producer prices in industry, % p.a.	488.8	52.1	7.7	13.2	6.7	36.9	20	20	20
General government budget, UAH mn									
Revenues	20425.4	30142.0	36889.6	37398.2	25366.8	30530.7	.	31470 [4]	.
Expenditures	24443.0	33759.0	43086.0	39416.5	27606.0	31555.8	.	31470 [4]	.
Deficit (-) / surplus (+)	-4017.6	-3617.0	-6196.4	-2018.3	-2239.2	-1025.1	.	0	.
Deficit (-) / surplus (+), % GDP	-7.4	-4.4	-6.6	-1.9	-3.2	-1.1	-1.5	0	.
Money supply, UAH mn, end of period									
M0, Currency outside banks	2623.0	4041.0	6132.0	7158.0	6310	9008	.	.	.
Broad money	6930.0	9364.0	12541.0	15719.0	14325	20468	.	.	.
Refinancing rate of NB % p.a., end of peric	110.4	39.6	34.8	74.2	82.0	45.0	45	35	.
Current account, USD mn	-1152	-1185	-1335	-1296	-1467	767	900	300	-500
Gross reserves of NB excl. gold, USD mn [5]	1051	1960	2341	761	1044	1332.1	1160	1800	.
Gross external debt, USD mn	8217	8840	9555	11483	10966	.	13500	14400	.
Exports total, fob, USD mn [6]	13128	14401	14232	12637	9556	8251	10233 [7]	10500	11500
annual change in %	27.8	9.7	-1.2	-11.2	-7.7	-13.7	-10.4 [7]	.	.
Imports total, cif, USD mn [6]	15484	17603	17128	14676	11263	8433	10385 [7]	10400	12000
annual change in %	44.1	13.7	-2.7	-14.3	-10.1	-25.1	-21.7 [7]	.	.
Average exchange rate UAH/USD	1.473	1.830	1.862	2.450	2.124	3.933	4	6	7
Average exchange rate UAH/EUR (ECU)	1.928	2.322	2.113	2.768	1.990	4.225	.	.	.
Purchasing power parity UAH/USD, WIIW	0.297	0.480	0.555	0.622	.	.	0.735	.	.

1) Preliminary. - 2) In square meters. - 3) Up to 1996 officially registered enterprises only. - 4) Current draft budget. - 5) Useable. - 6) Exports and imports of goods according to customs statistics. - 7) January-November.

Source: WIIW Database incorporating national and international statistics; WIIW forecasts.

Vladimir Gligorov

Yugoslavia: The aftermath

The Kosovo crisis was costly to Yugoslavia as a whole, though the costs were not spread equally. Undoubtedly, Kosovo itself suffered the most, though the full extent of the damages and other costs are not known. An early estimate commissioned by the World Bank put the damage costs at slightly above USD 1 bn. However, the survey of the damages was not comprehensive and in any case does not correspond in an obvious manner with the costs of reconstruction which are of course more important now. The population of Kosovo is also unknown; the census is planned for the spring of 2000. Other data are also not available, as there is still no statistical office functioning in the province. The budget has been drawn for this year, though it is not altogether clear what estimate of the economic activity is the basis for the budget projection. The donors have pledged over USD 2 bn at the conference in November, but the international agencies in Kosovo are constantly complaining that they are under-funded. All in all, it is fair to say that much more will be known about the economic situation in Kosovo once local elections are held and an administration is set up. The elections are planned for the autumn of 2000, but it will take time for the local government to start functioning, assuming that no major problems emerge during the whole process.

Montenegro has recorded a fall in GDP of about 8% for 1999. Inflation was, however, higher than in the rest of the country (where it was somewhat less than 50%) because of the legalization of the German mark as a parallel currency which has led to an one-time price shock of about 25%. The overall damage of the war was much smaller than that in Serbia, not to mention Kosovo. Indeed, the government has managed to convince the EU and the USA to lift some of the sanctions that still apply to Serbia. Both the USA and the EU have set money for budget support so that Montenegro has been able to finance its public expenditures and social and pension funds. This support is expected to continue. In addition, the government of Montenegro is planning to privatize some of its most valuable assets, e.g. the Telecom. This should bring enough money to support the speeding up of reforms and restructuring. The weak point is the fundamental institutional infrastructure because Montenegro is not an independent country and has difficulties conducting an independent economic policy and also securing the usual assistance from the international financial institutions. The government has indicated that the issue of the independence of Montenegro will have to be resolved in one way or another during the current year. This promises a busy political year, to say the least.

Serbia has recorded a loss of GDP of about 20% and of industrial production of about 25%. This does not include Kosovo, which is nominally part of Serbia. Exports have declined by close to 50%, imports by about one third. The estimates of the damages due to the NATO bombing campaign during the war have been estimated at somewhere between USD 3 to 4 bn, though no detailed survey and estimate of the damages has been done. The government has made an effort to secure the supply of electricity and heating during the winter and has been largely successful in that. In these efforts it has been helped by aid and credits by Russia and China (the latter apparently committed USD 300 mn). There are no food shortages, except for goods with price controls. Of course, these goods can be bought on the black market. Given that the inflation is measured at official prices, the actual inflation may be significantly higher than is officially acknowledged (the latter is around 50%). Since the war ended, the black market exchange rate has changed from about 10 dinars for one German mark to more than 20 dinars, though the official exchange rate is still 6 dinars for 1 German mark. The government has, for all intents and purposes, given up on the exchange rate anchor and has resorted first to inflationary financing and then to price controls. The latter policy is collapsing at the beginning of this year and it is to be expected that it will be abandoned once the government survives the winter.

What are the prospects for these three political units that are still nominally part of one country called Yugoslavia? The prospects for Kosovo will depend on the international effort and on the speed with which the local administration will be set up. It cannot be expected that any significant economic activity beyond services and agriculture can develop before the issues of security and public governance are resolved. Progress in those respects cannot be expected before the end of this year.

Montenegro will be another case of an aid economy at least as long as it does not make up its mind whether it wants to go alone or stay in a federation with Serbia. There are a number of other issues that will have to be resolved that may or may not prove to be politically popular (e.g. the introduction of a new currency, the privatization of state-owned firms and utilities). The country is small, so the cost of aid is not very large, but it is yet to be seen whether it contributes to the desired political end, whatever that might be.

The prospects in Serbia depend on the ability of the current government to survive. If it does, as is not altogether unlikely, then the economy will continue to stagnate in the semi-autarky that it finds itself in currently. The government may manage to get enough foreign support to keep the economy from collapsing completely, but there are no resources available for growth and development. The opposition is putting its faith on early or even regular elections, which should be held this year and the next, but whether their optimism is justified is difficult to say. If they fail to beat the government at the voting booths, that may present the country with very bleak prospects indeed.

Table YO

Yugoslavia: Selected Economic Indicators

	1995	1996	1997	1998 [1]	1998	1999	1999	2000	2001
					January-September		estim.	forecast	forecast
Population, th pers., mid-year	10547.0	10577.2	10597.0	8394.5 [2]	.	.	8372.2 [2]	.	.
Gross domestic product, USD mn, nom.	14681	15548	17000	14000	.	.	.	.	.
annual change in % (real) [3]	6.1	5.9	7.4	2.5	.	.	-19.3	3.0	3.0
GDP/capita (USD at exchange rate)	1392	1471	1600	1300	.	.	.	.	.
Gross industrial production [4]									
annual change in % (real)	3.8	7.5	9.5	3.6	6.7	-25.8	-22.5	4	5
Gross agricultural production [5]									
annual change in % (real)	4.2	1.3	7.2	-4.0	.	.	2.7	.	.
Goods transport, mn t-kms [6]	4206	31720	38097	.	.	.	.	.	.
annual change in % [6]	49.3	141.1	20.1	.	.	-46.5	.	.	.
Gross fixed investment, YUN mn, nom.	5348.7	9702.5	.	.	.	.	.	.	.
annual change in % (real)	-3.7	-5.7	.	.	.	.	.	.	.
Construction output, value of work done									
annual change in % (real)	-16.0	2.7	-3.0	-5.0	-4.8	-25	.	.	.
Dwellings completed, units	14337	15160	14768	13096	.	.	10841	.	.
annual change in %	-17.8	5.7	-2.6	-11.3	.	.	.	.	.
Employment total, th pers., average [7]	2379	2367	2332	2290	.	.	2076	.	.
annual change in %	-1.4	-0.5	-1.5	-1.8	.	.	-3.3	.	.
Employees in industry, th pers., average [8]	870	852	820	796	.	.	705	.	.
annual change in %	-2.7	-2.1	-3.8	-2.9	.	.	-5.1	.	.
Unemployed reg., th, end of period	777.0	826.8	793.8	849.4	850	777	.	.	.
Unemployment rate in %, end of period [9]	24.7	26.1	25.5	27.2	26.8	25.5	32	35	35
Average net monthly wages, YUN	340	658	803	1063	1004	1186	1304	.	.
annual change in % (real, net)	16.1	1.0	21.2	1.9	.	-16.5	-16.0	.	.
Retail trade turnover, YUN mn	14660.8	27895.7	35433.0	49360.0	.	.	.	.	.
annual change in % (real, calc.)	4.5	7.4	11.3	5.3	9.3	-25.0	-18.3	.	.
Consumer prices, % p.a. [10]	78.6	91.5	21.6	29.9	24.2	42.8	44.9	35	50
Producer prices in industry, % p.a. [10]	57.7	90.2	19.5	25.5	20.6	38.4	44.1	.	.
General government budget, YUN mn									
Revenues	17974.3	35412.2	47786.9	.	.	52363	.	.	.
Expenditures	17974.3	35412.2	47786.9	.	.	.	.	.	.
Deficit (-) / surplus (+) [11]	0	0	0	.	.	.	.	.	.
Money supply, YUN mn, end of period									
M1, Money	3256.1	5495.3	9148.0	10807.3	10286.1	14549	.	.	.
M2, Money + quasi money	27260.9	31512.6	39844.5	65520.0	.	.	.	.	.
Discount rate, % p.a., end of period	90.2	68.2	33.7	34.5	.	.	.	.	.
Current account, USD mn	.	-1317	-1837	-1200	.	.	-600	-800	-1000
Gross reserves of NB, excl. gold, USD mn	300	300	300	300	.	.	.	.	.
Gross external debt, USD mn	9000	9000	10500	11500	.	.	.	.	.
Exports total, fob, USD mn [12]	.	2018	2669	2820	2144	1090	1498	.	.
annual change in %	.	.	32.3	5.7	.	-49.2	-46.9	.	.
Imports total, cif, USD mn [12]	.	4117	4824	4732	3802	2225	3296	.	.
annual change in %	.	.	17.2	-1.9	.	-41.5	-30.3	.	.
Average exchange rate YUN/USD	1.79	4.97	5.73	9.34	9.10	10.98	17 [13]	45	63
Average exchange rate YUN/EUR (ECU)	2.34	6.30	6.48	10.33	10.02	11.81	.	.	.
Average exchange rate MKD/DEM	1.25	3.30	3.30	5.33	5.1	6.0	.	.	.
Purchasing power parity YUN/USD, WIIW	.	.	.	.	.	.	.	.	.

1) Preliminary. - 2) Excluding Kosovo and Metohia. - 3) Based on GMP in Dinar. - 4) Excluding private enterprises. - 5) Based on final net production. - 5) In 1995 and growth rate in 1996 excluding maritime transport. - 7) Employees plus own account workers, excluding individual farmers. - 8) Social sector. - 9) In % of unemployed plus employment. - 9) Excluding private sector; methodolological break 1996/1997. - 10) In 1993 there was a hyperinflation. Inflation in 1994 refer to February to December. - 11) Offical data, that do not report budget deficit. - 12) Converted from the national currency to USD at trade exchange rate. - 13) From 1999 black market exchange rate.

Source: WIIW database incorporating national and international statistics.

Herausgeber, Verleger, Eigentümer und Hersteller:
Verein "Wiener Institut für Internationale Wirtschaftsvergleiche" (WIIW),
Wien 1, Oppolzergasse 6
Postanschrift: A-1010 Wien, Oppolzergasse 6, Tel: [431] 533 66 10, Telefax: [431] 533 66 10 50
Internet Homepage: www.wiiw.ac.at

P.b.b. Verlagspostamt 1010 Wien