

July 7th 2021

Summer 2021 Forecasts for CESEE: Light at the end of the tunnel?

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Overview

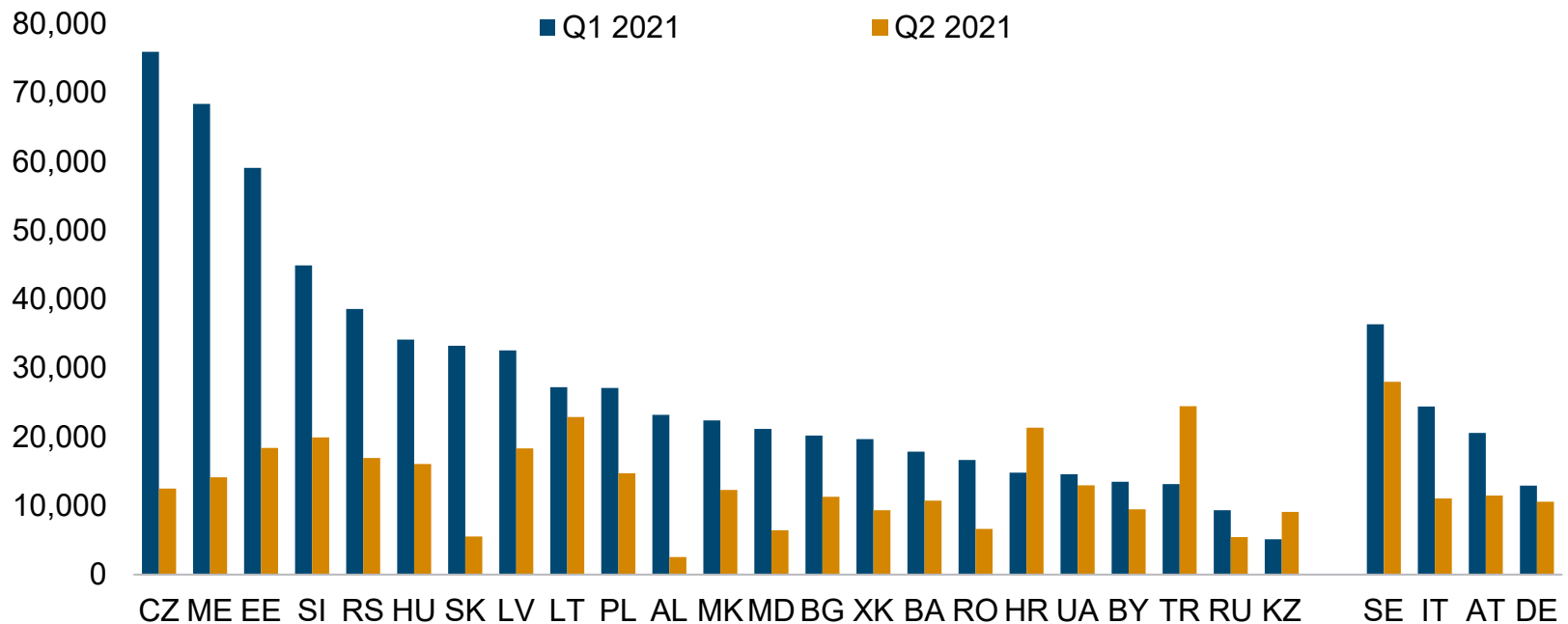
1. Global outlook
2. Pandemic developments
3. Growth in Q1 2021
4. Labour markets
5. Inflation
6. Monetary policy
7. FDI
8. Bank lending
9. Outlook for the future

Global economy is back on track

- US is growing strongly: +1.6% y-o-y in Q1
- China too: +18.3% y-o-y in Q1
- Both in line with expectations
- EU and euro area contracted in Q1: -0.4% and -0.6% y-o-y
- But this was better than the previous quarter
- And happened during a strong wave
- So, it was better than expected
- All major forecasters have upgraded their forecasts

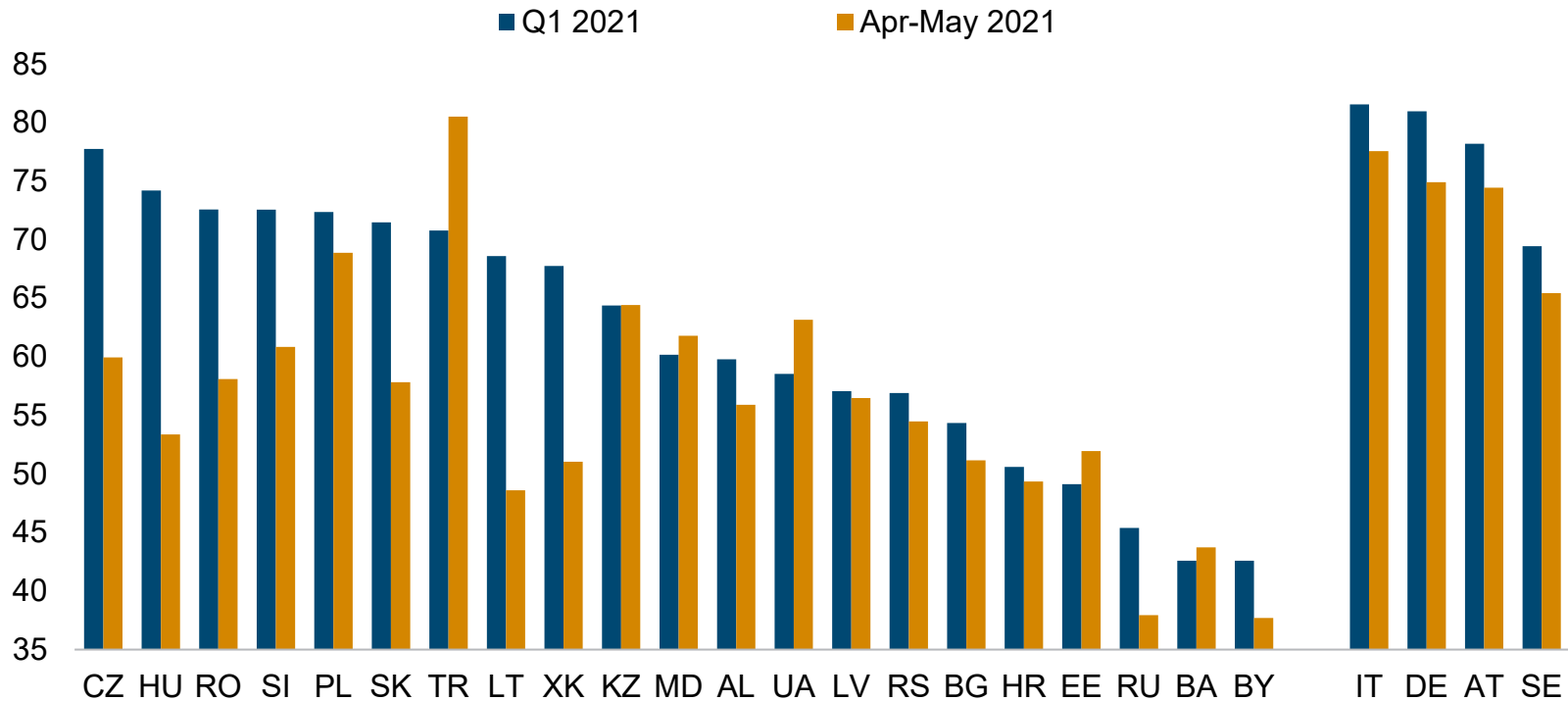
Strong pandemic wave in Q1 2021, stronger in CESEE than in EU

Number of new COVID-19 cases (per million population)



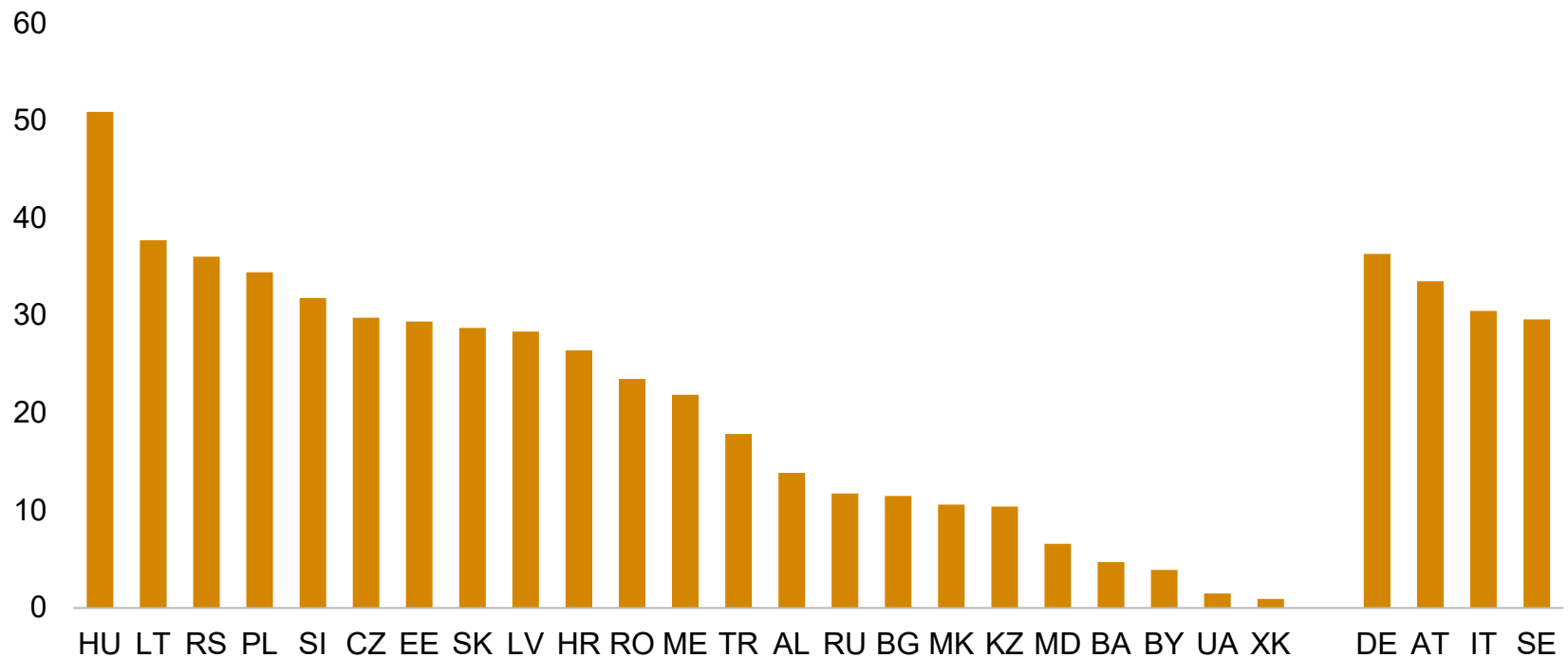
But restrictions in CESEE much milder than in EU

Stringency Index



Vaccination is under way, but very slow, and little promise of herd immunity

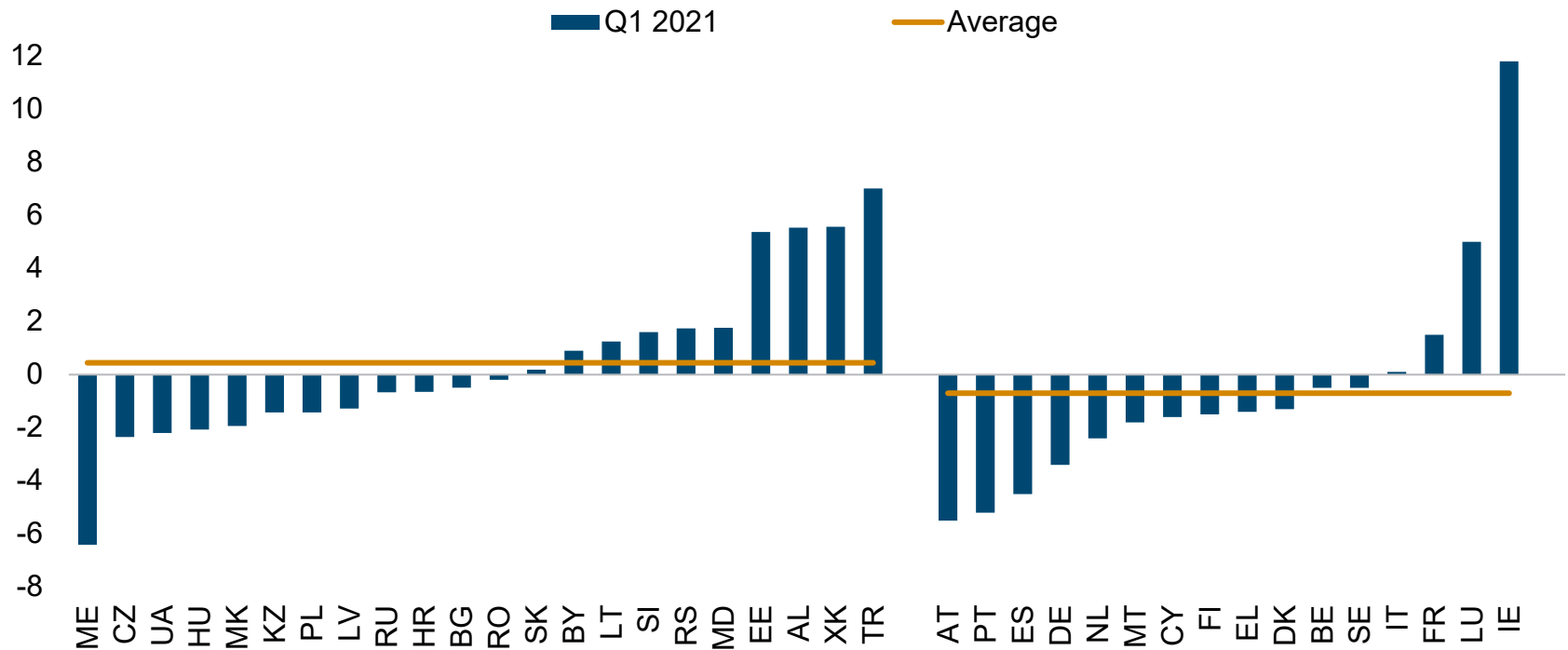
Share of population fully vaccinated against COVID-19 at end of June 2021 (%)



Source: Our World in Data, Oxford University. Data refer to 29 June, except for BA (25 June), BY (13 June), RS (20 June) and XK (20 June).

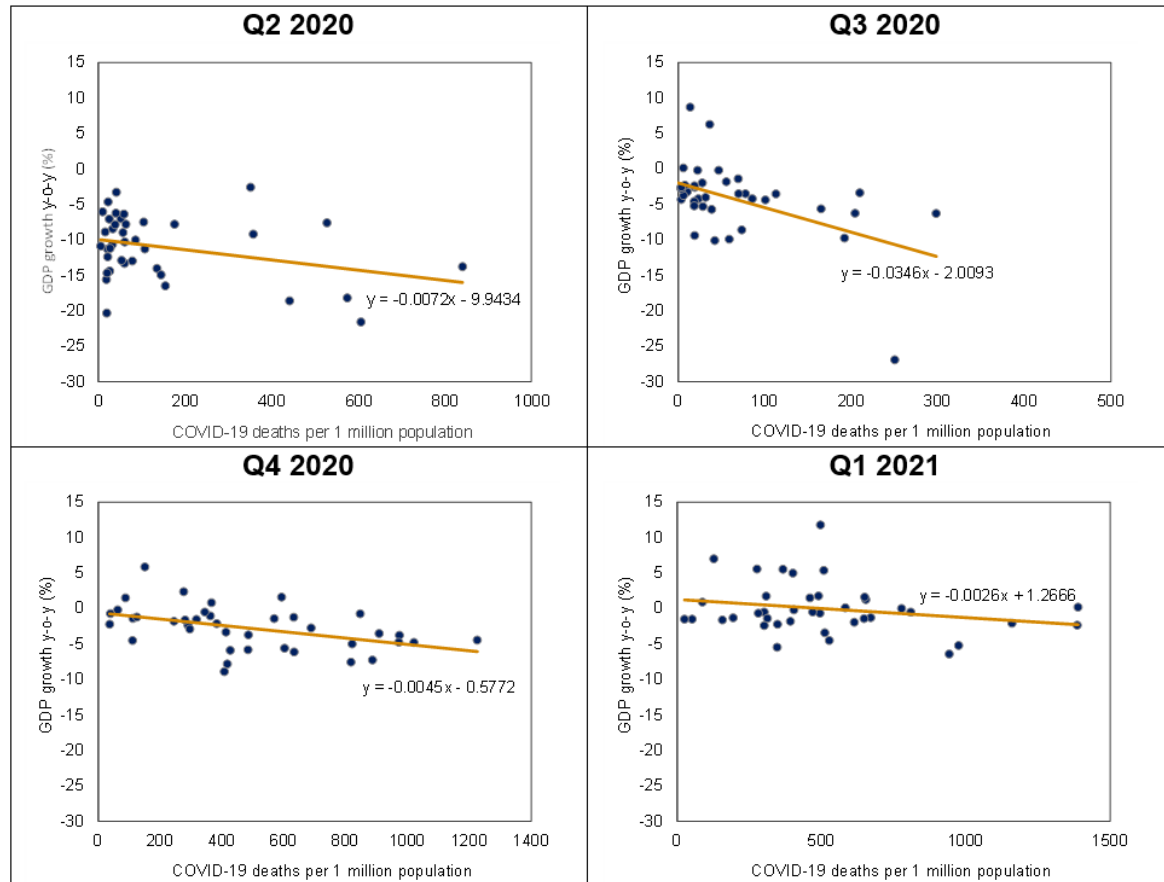
Despite the depressing health picture in Q1, economic results in CESEE better than expected

Real GDP growth in Q1 2021 (% , year on year)



Economies learned to live with the pandemic. GDP is not that sensitive to COVID-19 as it was.

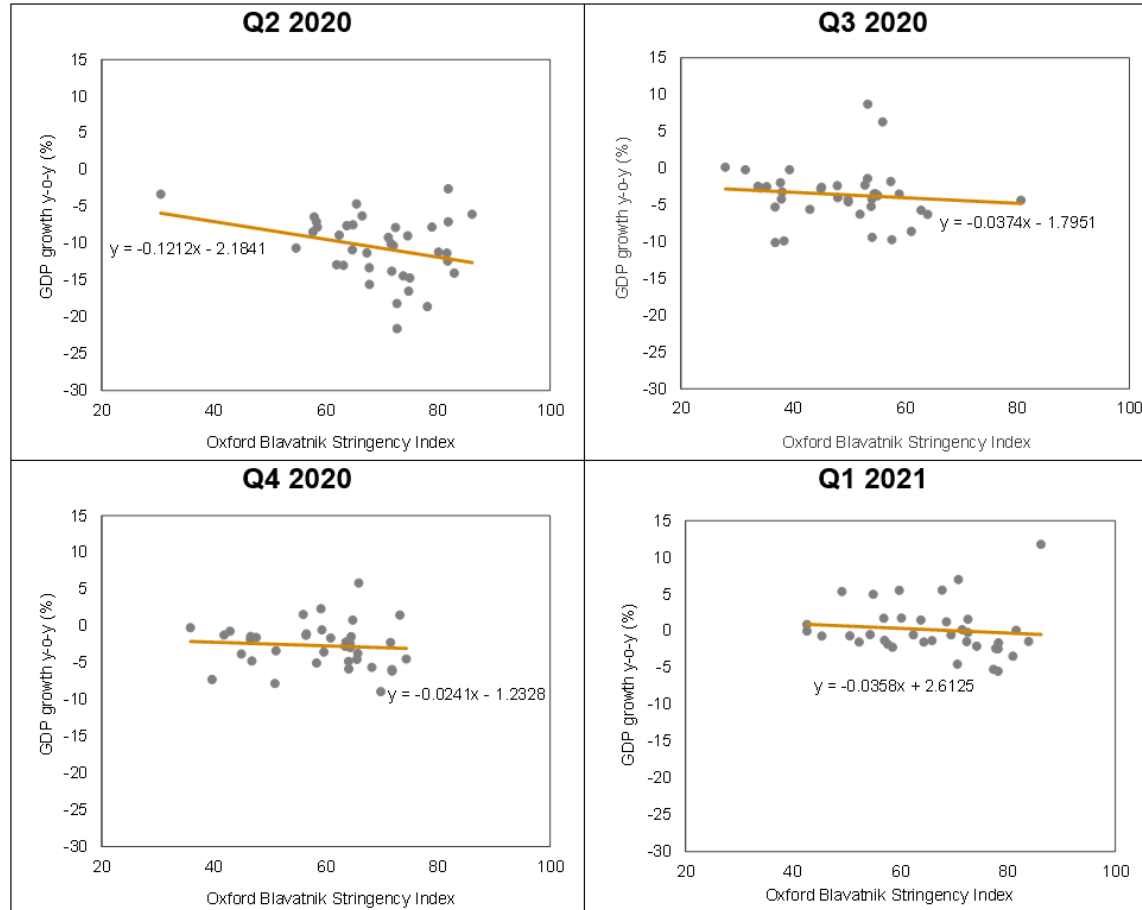
Relationship between real GDP growth and COVID-19 mortality



Source: COVID-19 deaths are from Oxford University's Our World in Data. GDP growth is from Eurostat and wiiw Monthly Database.

Similarly, government restrictions do not hurt the economy as much as they did before

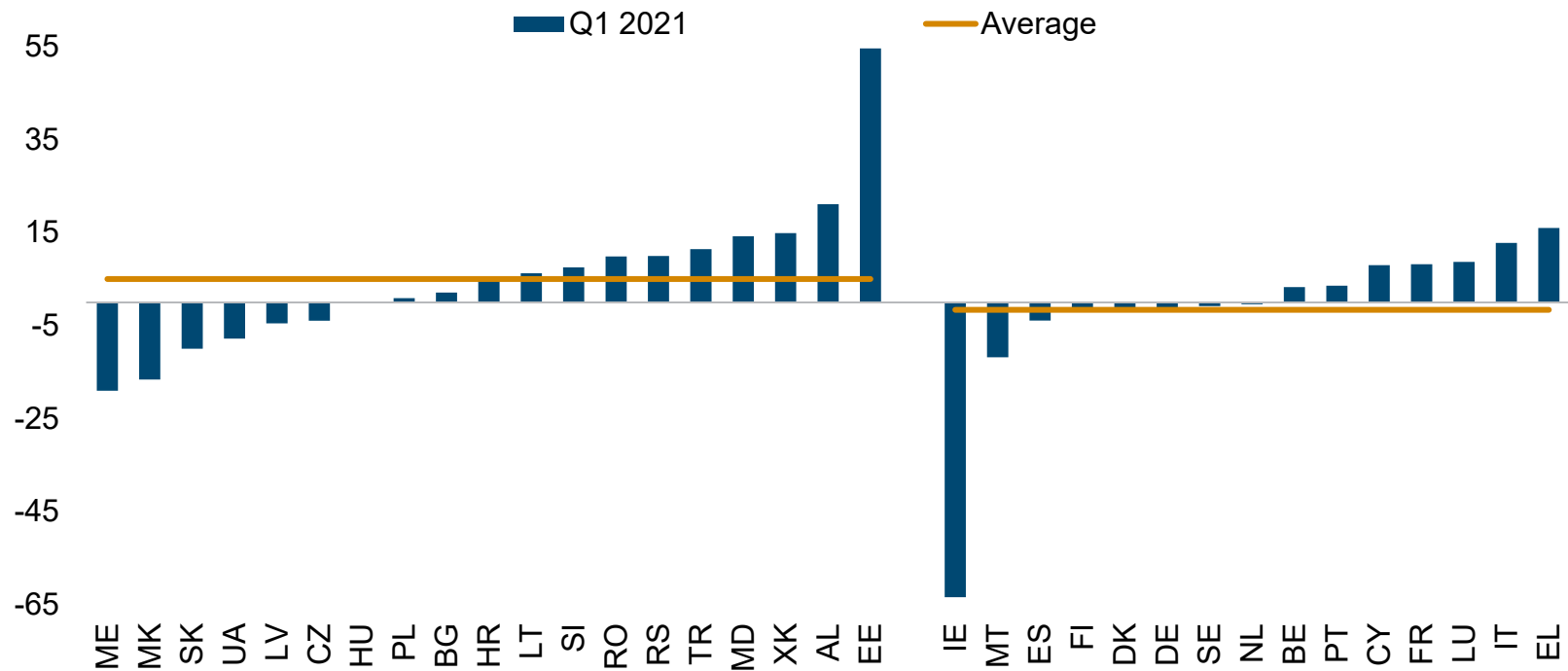
Relationship between real GDP growth and government restrictions



Source: Stringency Index is from Oxford University Blavatnik School of Government. GDP growth is from Eurostat and wiiw Monthly Database.

The good GDP figures from Q1 in CESEE are largely due to the strong rebound in investment

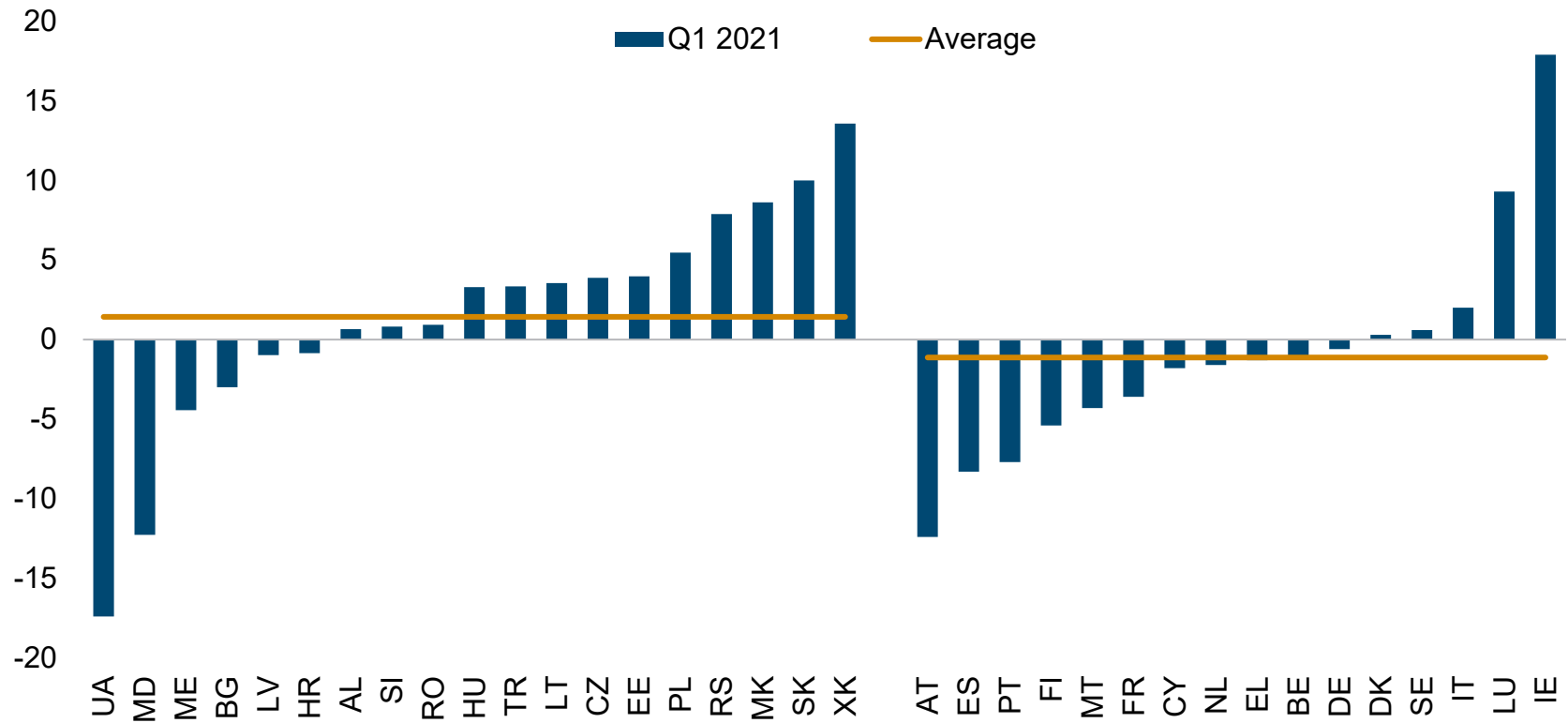
Real growth of gross fixed capital formation in Q1 2021 (% , year on year)



Source: Eurostat and wiiw Monthly Database. Data for BA, MK and XK refer to gross capital formation.

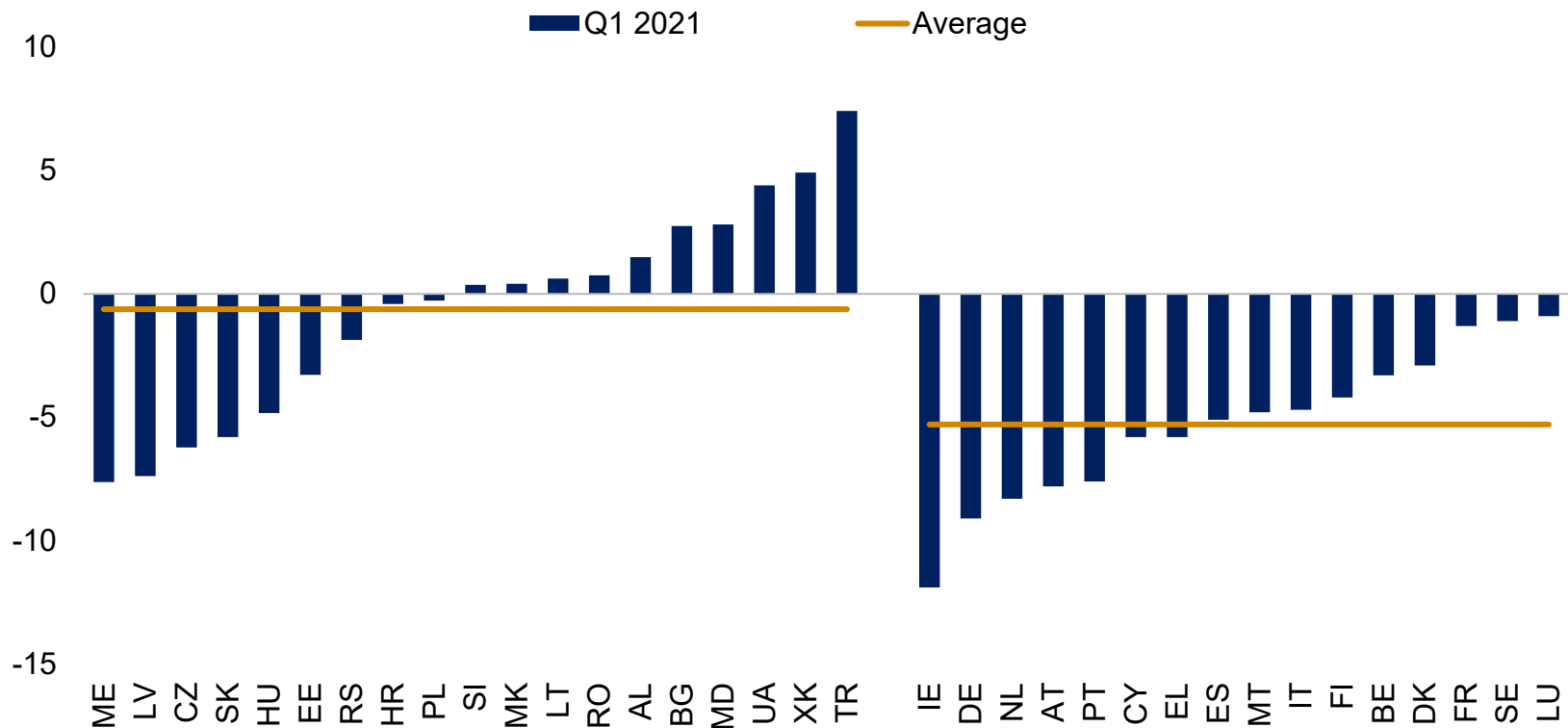
Exports of goods and services also performed well, due to increased demand from US and China

Real growth in exports of goods and services in Q1 2021 (% , year on year)



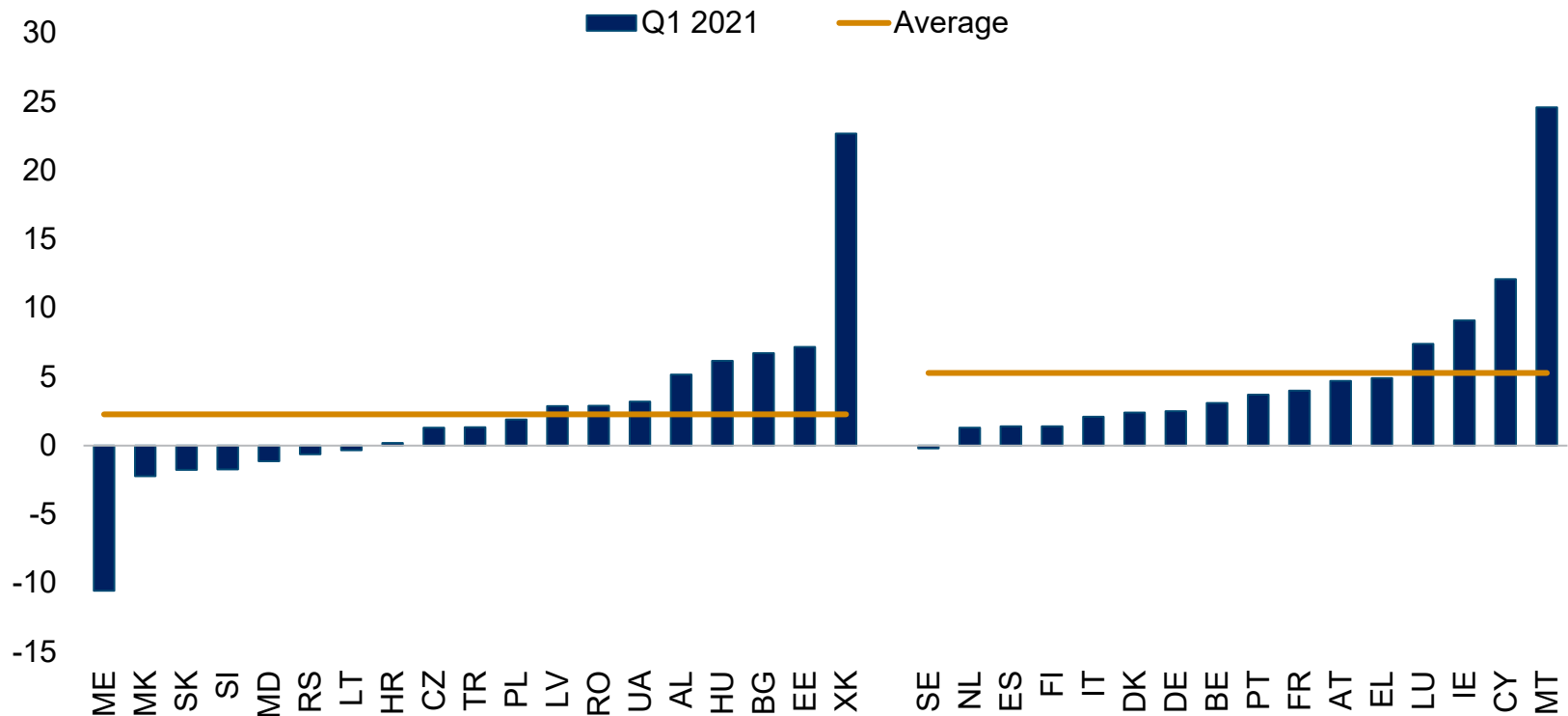
Household consumption still weak, due to the strong wave, but better than previous three quarters

Real growth in household consumption in Q1 2021 (% , year on year)



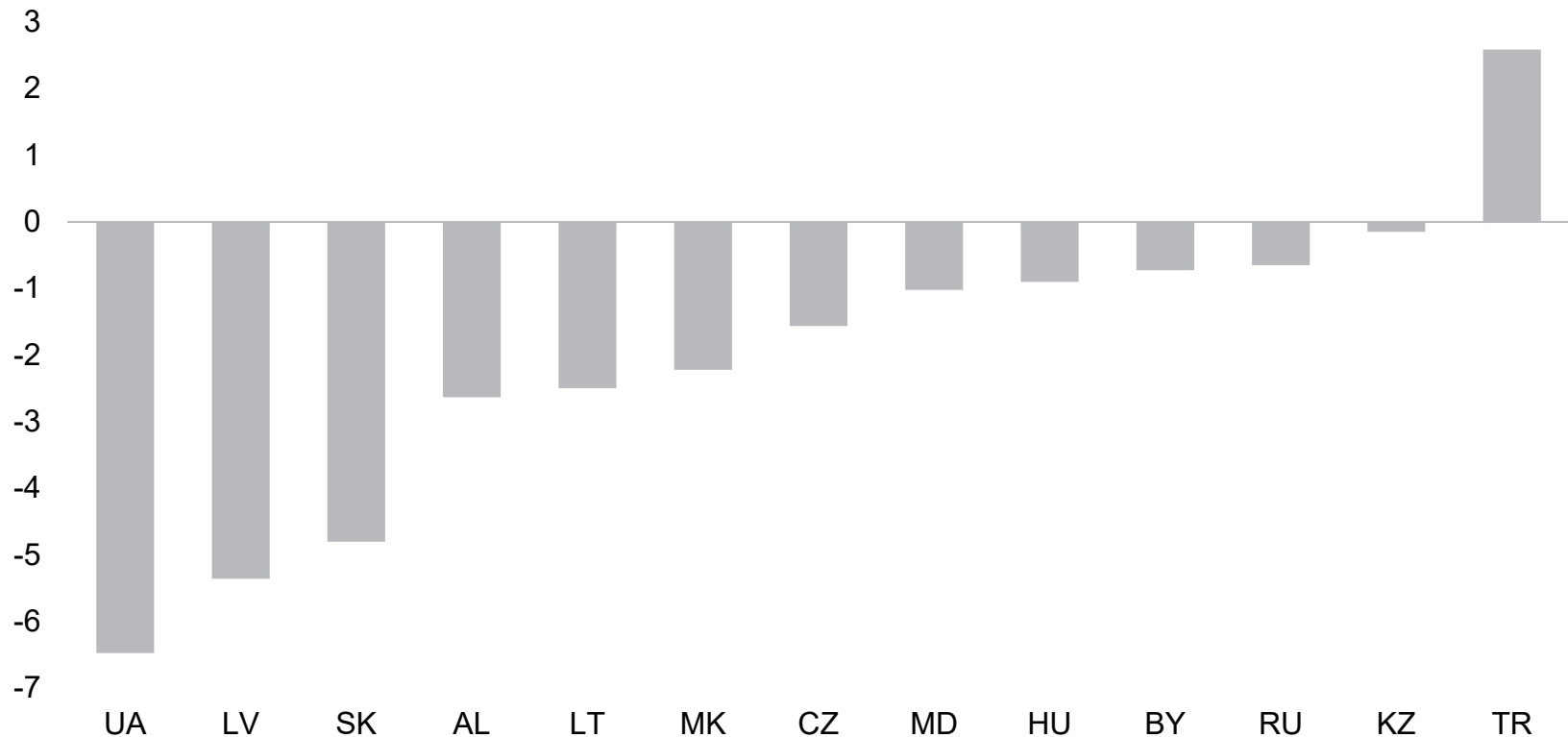
Government consumption positive, but less than in EU, reflecting limited fiscal space and fiscal conservatism

Real growth in government consumption in Q1 2021 (% , year on year)



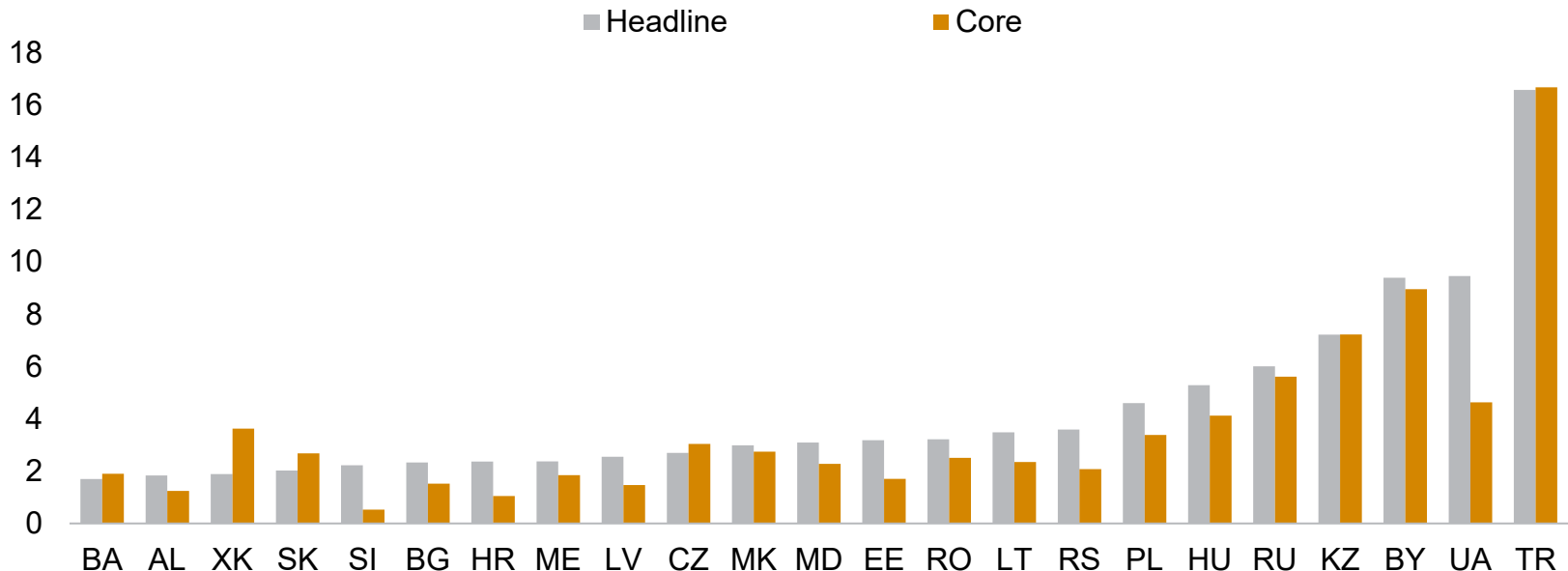
Labour market scarring visible – employment is down in 12/13 CESEE economies that have consistent data

Employment in CESEE in Q1 2021 (% , year-on-year change)



Inflation is back, but not here to stay. Higher global food and energy prices, but also spill overs to core inflation.

Headline and core consumer price inflation in CESEE in May 2021 (% , year on year)

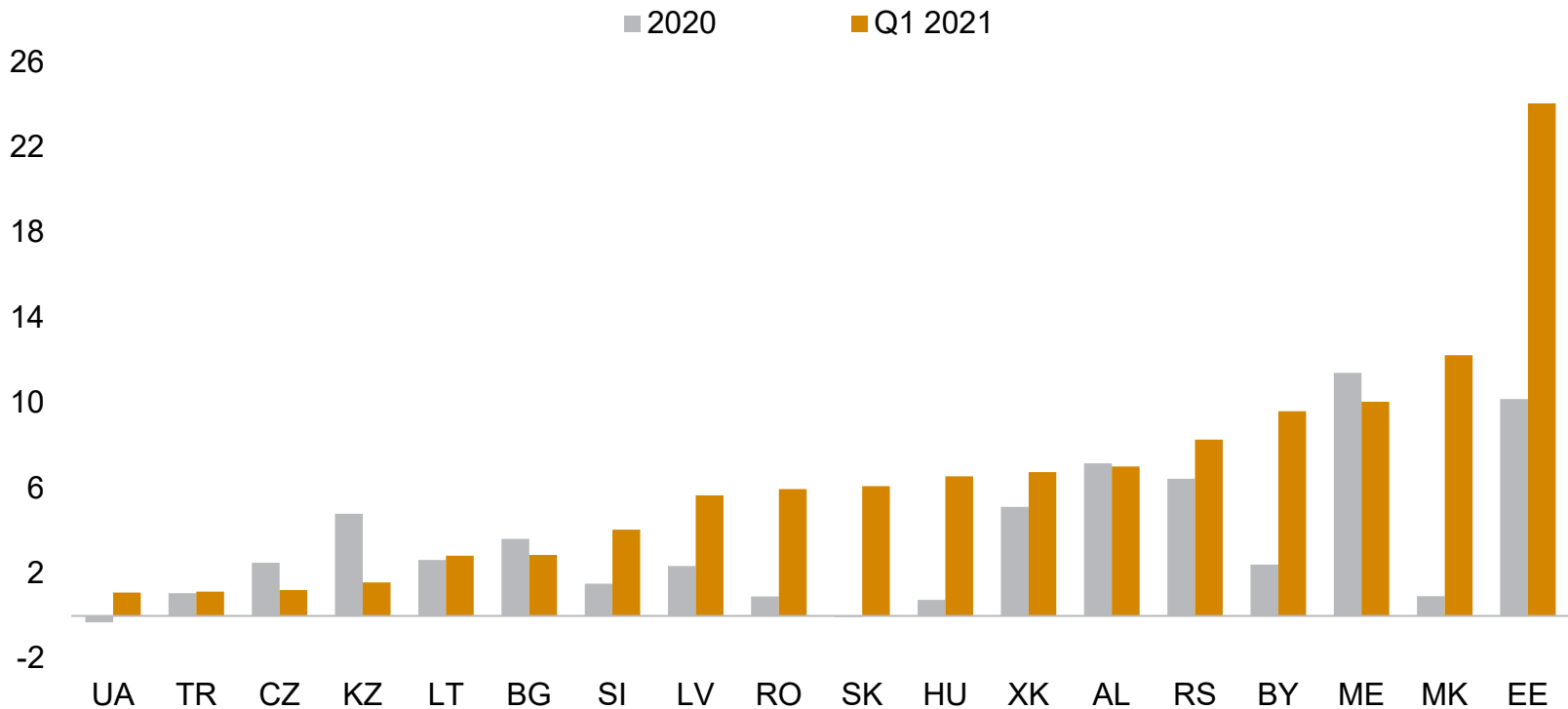


Due to the higher inflation, some CESEE central banks have raised their interest rates

- Belarus, from 7.75% to 8.5% in April
- Russia, on three occasions, from 4.25% to 5.5%
- Turkey, from 17% to 19% in March
- Ukraine, on two occasions, from 6% to 7.5%
- Hungary, from 0.6% to 0.9% in June
- Czechia, from 0.25% to 0.5% in June
- Several more may follow suit
- We don't expect these hikes to hurt the economy

After a drought of FDI in 2020, a flood in Q1 2021. Mostly projects that were postponed, but maybe also near-shoring.

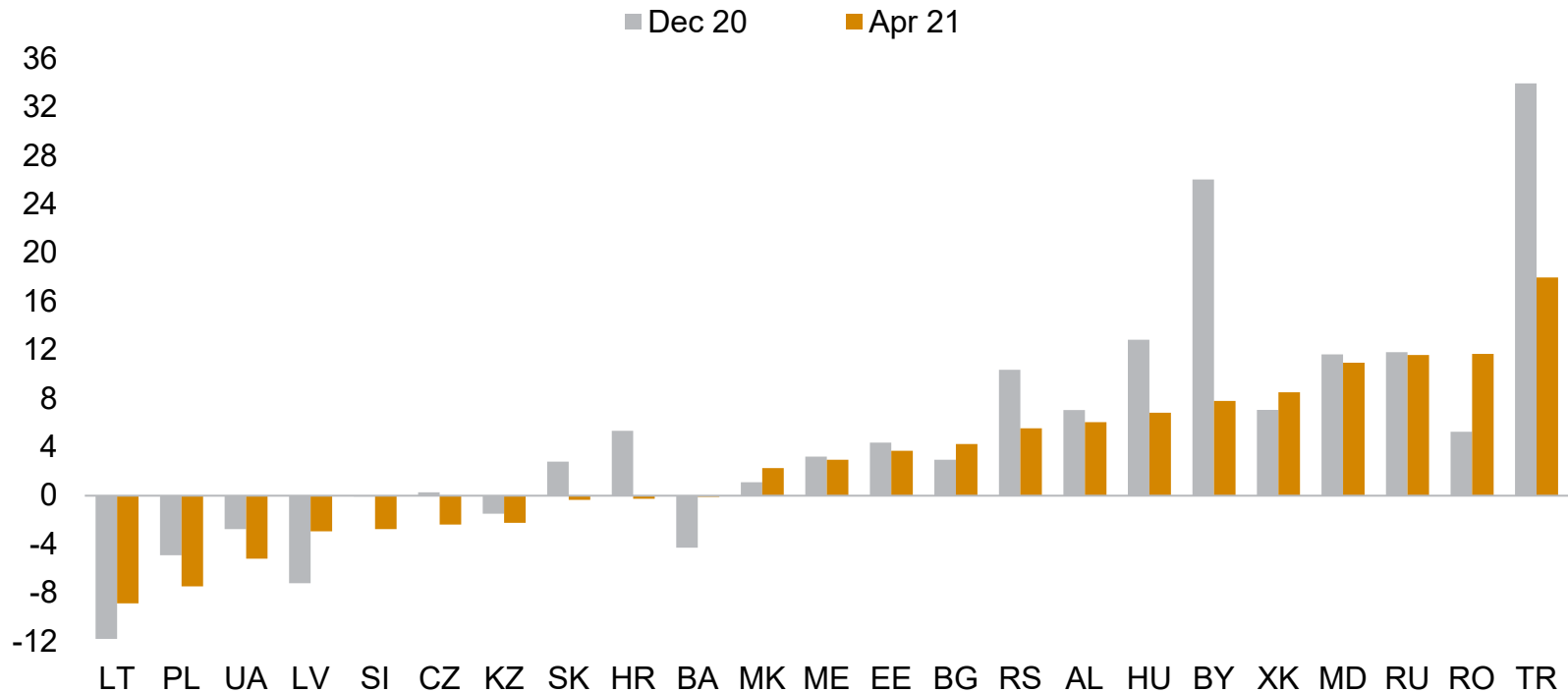
FDI inflows in CESEE countries in 2020 and Q1 2021 (% of GDP)



Source: wiiw Monthly Database. The data refer to FDI inflows (liabilities) from Balance of Payments statistics.

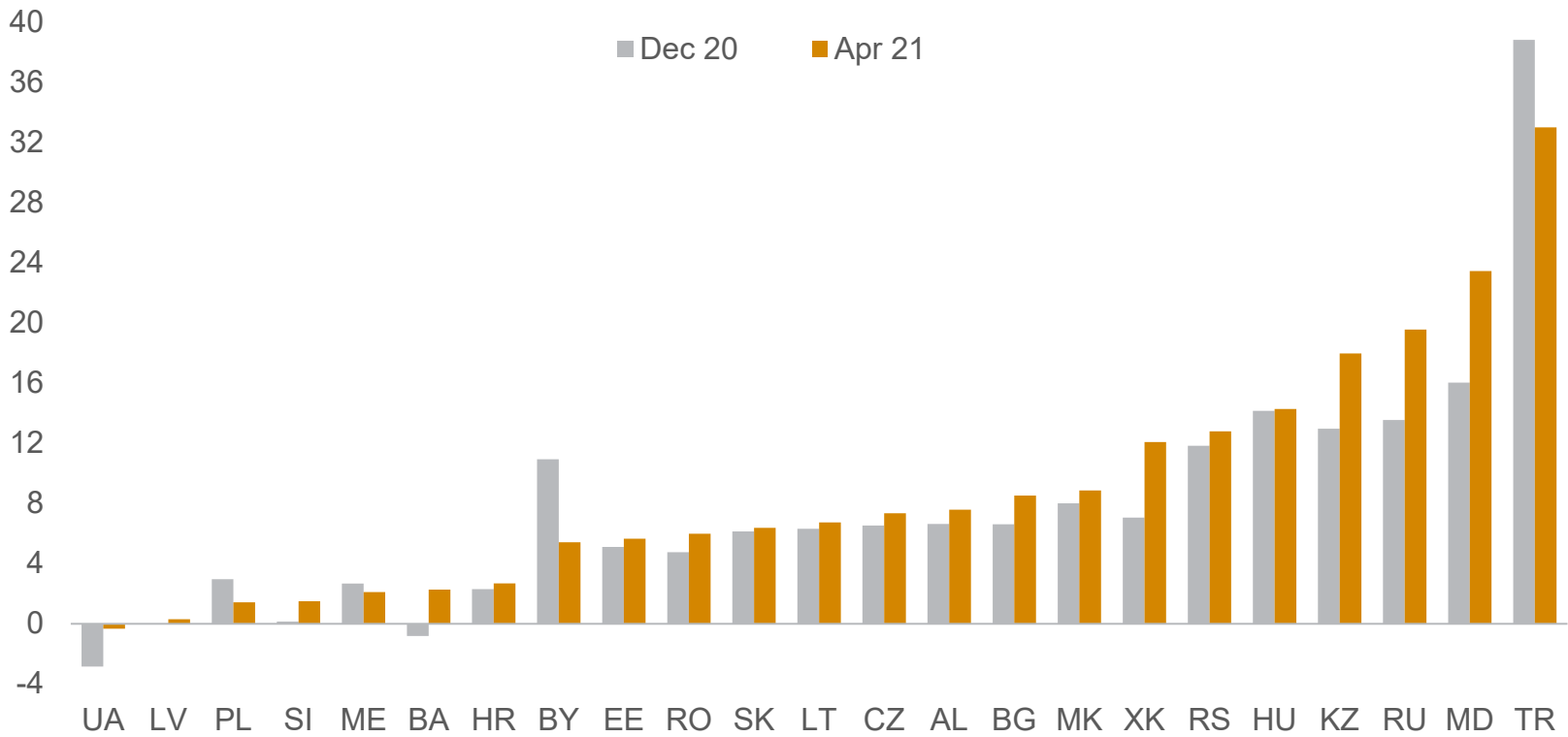
Credit activity remains robust, but shifts to households. Government credit lines for firms decline.

Growth in loans to non-financial corporations in CESEE in 2020 and 2021
(%, year on year)



Demand for credits from households increases, both for mortgages, and for consumption.

Growth in loans to households in CESEE in 2020 and 2021 (%, year on year)



Cautious optimism for the months ahead

- Improved global outlook for 2021
- Better-than-expected developments in Q1 2021
- We are thus upgrading our GDP forecasts for 2021 for 20 of the 23 CESEE economies

New forecasts and revisions

		Forecast, %			Revisions, pp	
		2021	2022	2023	2021	2022
EU-CEE	BG	3.0	3.5	3.8	↑ 0.5	↑ 0.4
	CZ	3.0	3.9	3.3	↑ 0.1	↑ 0.7
	EE	4.2	4.5	4.3	↑ 3.0	↑ 0.7
	HR	5.1	5.3	4.0	↑ 0.6	↑ 0.7
	HU	4.9	4.5	3.9	↑ 1.0	→ 0.0
	LT	3.0	4.0	3.5	↑ 0.9	↑ 0.2
	LV	3.2	5.0	3.8	↑ 0.4	↑ 0.8
	PL	4.0	4.5	4.4	↑ 0.6	↑ 0.9
	RO	5.2	4.5	4.5	↑ 1.4	→ 0.0
	SI	4.0	4.3	3.4	↑ 0.4	↑ 0.3
	SK	4.0	4.4	3.9	↑ 0.4	→ 0.0
Western Balkans	AL	5.0	4.4	4.2	↑ 0.5	→ 0.0
	BA	2.9	3.3	3.3	↑ 0.4	↑ 0.4
	ME	6.5	6.0	4.0	→ 0.0	↑ 1.0
	MK	4.1	3.4	3.2	→ 0.0	→ 0.0
	RS	6.0	4.2	4.2	↑ 1.0	↓ -0.2
	XK	5.3	4.7	4.4	↑ 0.5	↑ 0.1
Turkey	TR	5.8	3.4	3.5	→ 0.0	→ 0.0
CIS+UA	BY	2.5	1.6	2.1	↑ 1.0	↓ -0.3
	KZ	3.5	4.1	4.4	↑ 0.3	→ 0.0
	MD	7.0	4.5	4.0	↑ 3.0	→ 0.0
	RU	3.5	3.0	2.6	↑ 0.3	↑ 0.3
	UA	4.3	3.5	3.5	↑ 0.8	↑ 0.3

Growth in the remainder of the year

- Driven primarily by **household consumption**, which will boom as the pandemic moderates, fuelled by the accumulated savings from 2020 and supportive bank lending.
- **Business investment** will also contribute, with companies resuming the projects they postponed
- Strong inflow of **FDI** that we are already seeing
- **Exports** will also rise, driven by a favourable external environment and increased foreign demand.

Other sectors

- **Labour markets** will also improve, but this will depend largely on the fiscal support provided by governments
- **Inflation** will be higher than previously expected, and carry-over effects will raise it also in 2022. But will moderate afterwards.
- **Central banks might raise their interest rates** due to the higher inflation, following the six that already did that
- **Tourism** will improve, but will remain below pre-pandemic period. Countries with tourists from closer destinations will fare better.

Risks are on the downside

- **Main risk – the new pandemic wave** that is expected from Autumn. Experience from other countries (Chile, Israel) says that current levels of vaccination will not prevent it.
- **Some restrictions will be imposed**, but we don't expect hard lockdowns
- And economies have learned to cope with the pandemic
- So, it will bring a **slow down in economic activity**, but not a recession

The second risk refers to pre-mature fiscal consolidation

- Higher growth might push some CESEE governments to consider retrenching already in 2021
- This would be a mistake, since economies are still fragile
- And labour markets scarring is visible

Conclusions

- Global outlook is positive
- Economic results from Q1 2021 better than expected, despite strong wave
- CESEE economies have learned to cope with COVID-19
- We upgrade our GDP forecasts for 2021 in 20 of the 23 CESEE countries
- Main risks – new strong wave in Autumn and premature fiscal consolidation
- Inflation is back, but won't stay for long
- Still, some central banks have hiked rates, and few more may follow
- Labour market scarring is evident, but need more time to assess better
- FDI is pouring in
- Credit activity remains robust, and is shifting to households

Thank you for your attention!

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