Wiener Institut für Internationale Wirtschaftsvergleiche
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New wiiw forecast for the region of CENTRAL, EAST and SOUTHEAST EUROPE (CESEE), 2017-2019
Cautious upturn in CESEE: haunted by the spectre of uncertainty

- **Growth in the CESEE economies will strengthen gradually, surpassing on average 3% by 2019.**
- **This growth will be driven by consumption and increasing investment, amid a largely supportive international economic environment. Despite a rise in ULCs, competitiveness will not be endangered.**
- **Although the size of labour forces in CESEE is stagnating, data indicate an improvement in educational levels of workers. Meanwhile the tightness of labour markets will propel wage growth.**
- **The CESEE region as a whole is back on a convergence track, with an average positive growth differential of 1.2 pp vis-à-vis the euro area over the forecast horizon.**
- **Downside risks are significant, mostly stemming from political factors. The CESEE countries and Europe more broadly, together with the rest of the world, will be haunted by the spectre of political uncertainty; it is only to be hoped that, once fully roused, the 'animal spirits' of economic agents will shrug off the gloom.**

For the economies of CESEE, the international economic environment appears generally positive. In 2017-2018, GDP growth in the euro area is expected to hover around 1.7%. The international financial markets have stabilised and the current economic mood is improving. Because of the global recovery, the US Fed is expected to increase interest rates further in 2017, while oil prices are likely to rise. In the EU, disbursements from the payments cycle of the European Structural and Investment Funds are only just beginning, indicating higher co-financed investments in the EU-CEE countries from this year onwards.

Over recent quarters, GDP growth throughout almost the entire CESEE region has stabilised in positive territory. The only exception is Belarus, where growth is still in negative territory (albeit less so than was the case in 2015). The country is going through a painful adjustment process triggered by accumulated macroeconomic imbalances and its excessive dependence on Russia.

Current wiiw CESEE GDP growth forecasts for 2017-2019 point to growth of around 3% for most of the region, with a slightly upward trend. The EU-CEE sub-region and the Western Balkan economies in particular should manage to attain average GDP growth rates of up to 3% and in some countries, such as Hungary, Romania, Slovakia, Albania and Kosovo, the levels may be even higher. In Turkey, where growth slowed down markedly in 2016 to below 2% (down from around 6% in prior years) on account of the domestic political turmoil and

deterioration in foreign relations, we also expect growth to be closer to 3% by the end of the forecast horizon. The CIS-3 economies will record increasing GDP growth rates, rising from more than 1% in 2017 to over 2% in 2019, given the higher oil prices. Over the same forecast period, economic growth in Ukraine is projected to accelerate gradually to 3% by 2018-2019 – barring all-out warfare in Donbas and abortion of the IMF programme.

Private consumption and increasing investment will continue to be the main growth drivers over the forecast horizon. After the investment slump in 2016 attributable to the switch from the previous to the current EU (co-) financing period, investment in the EU-CEE economies will recover in the years ahead. Meanwhile the mood among consumers is improving and, due to changing spending patterns in the EU-CEE sub-region, this trend should prove durable. Tightening labour markets are conducive to major wage increases.

Despite the general rise in unit labour costs, competitiveness does not seem to be endangered. Most of the latest industrial production figures for the CESEE countries are encouraging; they point to an ongoing improvement in industry structure and, in several cases, to re-industrialisation. Longer-term FDI trends hold particular promise for the Western Balkans. In Romania and Slovakia the prospects for future FDI increases are also quite good, especially in the automotive sector. Although the size of the labour force in CESEE countries is more or less stagnating, a marked improvement in education levels is evident, as a younger and better educated generation enters the work force. This hints at a potential general increase in labour quality across the region's economies.

Nevertheless, heightened uncertainties following the UK referendum on Brexit in June 2016 and the US presidential elections in November have cast a cloud over the improved economic conditions noted above. A number of worrying scenarios are quite conceivable that could ultimately make our forecasts appear upbeat and overoptimistic. Thanks to US President Donald Trump, a rise in global protectionism is possible, which would harm industry in the region. Mr Trump has also questioned post-war European security arrangements, thus causing consternation in some EU-CEE countries. Meanwhile, the growing irritation with the EU-CEE sub-region among some older EU Member States and the fallout from Brexit could possibly pose a threat to west-east fiscal transfers and the free movement of labour in their current forms. In the Western Balkans, any confrontational interventions by Russia and uncertainties as to developments in Turkey could prove quite disruptive, were the influence of the EU and USA in the region to decline. Increasing uncertainties in the CIS and Ukraine are mostly related to future commodity price developments (most importantly oil prices) and heightened geopolitical tensions. Three special sections of the forecast report shed more light on the issue of heightened uncertainties in the EU-CEE, the Western Balkans and the CIS+UA regions.

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OVERVIEW 2015-2016 AND OUTLOOK 2017-2019

	GDP real change in % against prev. year					Consumer prices change in % against prev. year					Unemployment (LFS) rate in %, annual average					Current account in % of GDP				
			Forecast					Forecast					Forecast					Forecast		
	2015	2016	2017	2018	2019	2015	2016	2017	2018	2019	2015	2016	2017	2018	2019	2015	2016	2017	2018	2019
Bulgaria	3.6	3.4	2.9	3.1	3.3	-1.1	-1.3	0.5	1.0	1.5	9.2	7.6	7.0	6.5	6.0	0.4	3.8	3.5	3.2	2.8
Croatia	1.6	2.8	2.8	2.9	3.0	-0.3	-0.6	1.3	1.6	1.6	16.3	13.5	13.0	12.5	12.0	5.1	3.7	2.1	1.5	0.9
Czech Republic	4.5	2.3	2.4	2.6	2.3	0.3	0.6	2.0	1.8	1.8	5.1	4.0	3.9	3.8	3.6	0.9	1.6	1.2	0.9	0.8
Estonia	1.4	1.3	2.2	2.3	2.4	0.1	0.8	2.0	2.5	3.0	6.2	6.6	6.7	7.0	7.0	2.2	2.7	0.9	0.4	0.0
Hungary	3.1	2.0	3.3	3.4	3.1	0.1	0.4	2.0	2.5	2.8	6.8	5.2	4.8	4.5	4.5	3.4	4.3	4.2	3.4	2.5
Latvia	2.7	1.8	2.5	2.7	2.8	0.2	0.1	1.8	2.1	2.3	9.9	9.7	9.2	8.8	8.4	-0.8	1.6	0.0	-1.1	-1.7
Lithuania	1.8	2.2	2.7	2.8	3.1	-0.7	0.7	2.1	2.3	2.7	9.1	8.0	7.2	6.5	6.0	-2.3	0.3	-1.2	-1.4	-1.8
Poland	3.9	2.8	2.9	3.0	3.1	-0.7	-0.2	1.4	1.9	2.0	7.5	6.3	6.2	6.1	6.1	-0.6	-0.5	-0.7	-1.1	-1.4
Romania	3.9	4.8	4.0	4.0	4.0	-0.4	-1.1	1.5	2.5	2.5	6.8	6.0	5.8	5.6	5.5	-1.2	-2.4	-2.5	-2.6	-2.6
Slovakia	3.8	3.3	3.1	3.6	3.9	-0.3	-0.5	1.2	1.8	1.8	11.5	9.7	9.0	8.5	8.0	0.2	-0.6	0.4	0.9	1.5
Slovenia	2.3	2.6	2.9	2.9	3.0	-0.8	-0.2	1.3	1.4	1.4	9.0	8.2	7.8	7.0	6.5	5.2	6.9	5.8	5.0	4.5
EU-CEE [1)2)]	*3.7*	*3.0*	*3.0*	*3.2*	*3.2*	*-0.4*	*-0.2*	*1.5*	*2.0*	*2.1*	*7.8*	*6.6*	*6.3*	*6.1*	*6.0*	*0.4*	*0.7*	*0.4*	*0.0*	*-0.2*
EA-19	*2.0*	*1.7*	*1.6*	*1.8*	*.*	*0.0*	*0.2*	*1.7*	*1.4*	*.*	*10.9*	*10.0*	*9.6*	*9.1*	*.*	*3.7*	*3.6*	*3.2*	*3.1*	*.*
EU-28	*2.2*	*1.9*	*1.8*	*1.8*	*.*	*0.0*	*0.3*	*1.8*	*1.7*	*.*	*9.4*	*8.5*	*8.1*	*7.8*	*.*	*2.2*	*2.1*	*1.9*	*1.9*	*.*
Albania	2.6	3.2	3.5	3.9	4.0	1.9	1.3	2.3	2.8	3.0	17.1	15.2	14.8	14.5	14.0	-10.8	-11.5	-11.9	-11.3	-10.7
Bosnia and Herzegovina	3.1	2.3	2.8	3.0	3.1	-1.0	-1.1	1.0	1.4	1.9	27.7	25.4	25.3	25.1	25.0	-5.7	-6.0	-5.8	-5.7	-5.7
Kosovo	4.3	3.6	3.9	3.8	3.7	-0.5	0.3	0.9	1.6	2.3	32.9	26.5	25.8	25.5	25.2	-8.6	-9.9	-10.4	-11.2	-11.8
Macedonia	3.8	2.5	3.1	3.3	3.0	-0.3	-0.2	1.0	1.5	2.0	26.1	24.0	24.0	23.0	23.0	-2.1	-2.0	-4.0	-4.0	-4.0
Montenegro	3.4	2.7	3.1	2.9	3.3	1.4	0.1	1.5	2.0	2.0	17.6	17.5	17.0	16.5	16.5	-13.3	-17.0	-16.4	-20.7	-19.8
Serbia	0.8	2.7	2.8	3.0	3.3	1.9	1.2	2.0	2.0	2.0	17.7	16.1	15.0	14.0	14.0	-4.7	-5.0	-4.0	-4.0	-4.0
WB [1)2)]	*2.2*	*2.7*	*3.0*	*3.2*	*3.4*	*0.9*	*0.5*	*1.6*	*1.9*	*2.1*	*21.2*	*19.1*	*18.4*	*17.7*	*17.6*	*-6.1*	*-6.7*	*-6.6*	*-6.7*	*-6.7*
Turkey	6.1	1.9	2.1	2.6	3.1	7.7	7.8	8.7	7.5	6.8	10.3	10.8	11.0	10.6	10.4	-3.8	-3.8	-5.1	-5.4	-5.7
Belarus [3)]	-3.8	-2.6	0.5	1.6	2.2	13.5	11.8	10.0	9.0	8.0	1.0	0.8	1.0	1.0	1.0	-3.7	-3.0	-3.5	-4.4	-4.5
Kazakhstan	1.2	1.0	2.0	3.0	3.0	6.6	14.6	7.0	6.0	6.0	5.0	5.0	5.0	5.0	5.0	-3.0	-6.1	-2.4	-1.9	-2.2
Russia	-2.8	-0.2	1.7	1.7	2.0	15.5	7.1	5.0	5.0	5.0	5.6	5.3	5.6	5.6	5.5	5.1	1.7	1.7	1.3	0.9
Ukraine	-9.8	2.0	2.5	3.0	3.0	48.7	13.9	10.5	6.1	5.0	9.1	9.4	9.2	8.1	7.3	-0.2	-3.6	-4.5	-4.6	-4.8
CIS + Ukraine [1)2)]	*-3.0*	*0.0*	*1.7*	*1.9*	*2.2*	*17.1*	*8.6*	*5.8*	*5.3*	*5.2*	*5.9*	*5.9*	*6.0*	*5.8*	*5.6*	*3.6*	*0.6*	*0.8*	*0.5*	*0.2*
VIS-4 [1)2)]	*3.9*	*2.6*	*2.9*	*3.0*	*3.0*	*-0.4*	*0.0*	*1.6*	*2.0*	*2.1*	*7.3*	*6.0*	*5.8*	*5.7*	*5.6*	*0.3*	*0.6*	*0.5*	*0.2*	*0.0*
BALT-3 [1)2)]	*2.0*	*1.9*	*2.5*	*2.7*	*2.9*	*-0.3*	*0.5*	*2.0*	*2.3*	*2.7*	*8.7*	*8.2*	*7.7*	*7.3*	*7.0*	*-0.7*	*1.3*	*-0.3*	*-0.9*	*-1.3*
SEE-9 [1)2)]	*3.2*	*3.8*	*3.5*	*3.6*	*3.6*	*-0.2*	*-0.7*	*1.4*	*2.0*	*2.2*	*12.8*	*11.3*	*10.9*	*10.4*	*10.2*	*-1.3*	*-1.7*	*-2.0*	*-2.2*	*-2.3*
NON-EU-11 [1)2)]	*-0.2*	*0.6*	*1.9*	*2.2*	*2.5*	*13.8*	*8.1*	*6.5*	*5.8*	*5.6*	*7.6*	*7.6*	*7.7*	*7.4*	*7.2*	*0.9*	*-1.2*	*-1.2*	*-1.5*	*-1.9*
CESEE-22 [1)2)]	*0.9*	*1.3*	*2.2*	*2.5*	*2.7*	*9.7*	*5.6*	*5.0*	*4.7*	*4.6*	*7.6*	*7.3*	*7.3*	*7.1*	*6.9*	*0.9*	*-0.7*	*-0.8*	*-1.3*	*-1.7*

1) wiiw estimates. - 2) Current account data include transactions within the region (sum over individual countries). - 3) Unemployment rate by registration.

2) *Source*: wiiw, Eurostat. Forecasts by wiiw (Feb 2017) and European Commission for EU and Euro area (Winter Report, Feb 2017).