

PRESS RELEASE

Economic Outlook for Central, East and Southeast Europe: High Growth Continues, with Risks of Overheating on the Horizon

In its new forecast for Central, East and Southeast Europe, the Vienna Institute for International Economic Studies (wiiw) analyses the current economic situation in the region as well as development prospects for 2007 and 2008. Brief country surveys for Albania, Bosnia and Herzegovina, Bulgaria, Croatia, the Czech Republic, Hungary, Macedonia, Poland, the Slovak Republic, Slovenia, Serbia, Montenegro, Romania, Russia, Ukraine and Turkey (as well as China) are added. An annex contains indicators of competitiveness as well as revised projections of per capita GDP until 2015.

May 1st, 2007 marked the **third anniversary of the accession** of the eight former socialist **countries of Central and Eastern Europe** to the EU. The first three years of EU membership were a clear **economic success**. Over the period 2004-2006 GDP in the new member states (NMS) increased by 5.3% on annual average, 2.2 percentage points faster than in the previous three years. The NMS substantially increased their lead in terms of growth over the EU-15 and their catching-up process accelerated. The difference between pre- and post-accession periods was even more spectacular when looking at investments. Export growth rates nearly doubled after EU accession and NMS trade balances have improved. Stronger economic growth reduced unemployment and fostered employment. However, macroeconomic stability indicators – inflation, current account status and fiscal balances – reveal a less favourable picture than those related to developments of the real economy, possibly reflecting lesser enthusiasm regarding EMU accession.

In 2008 **high GDP growth** will continue in the NMS, except for Hungary. Nevertheless, in all but two countries (the Czech Republic and Hungary) growth rates are predicted to be somewhat lower than, or equal as, in the current year, because of constraints on further acceleration of the current rapid pace of growth. Supply-side constraints on further expansion will be felt especially because of a tight labour market. There are risks of overheating in Bulgaria, Romania and the Baltic States. Only in Slovakia does very high growth seem to be sustainable, at least over the next two years. Pressures arising from an increasingly tight labour market will be counterbalanced by further currency appreciation and the inflation will remain relatively low. Export growth will be high, reflecting a favourable international environment, growing import demand of the main trading partners and continuing competitiveness of the NMS.

Economic developments in **the future member states (FMS)** of the EU – the candidate and potential candidate countries **of the Balkans** – continue to surprise positively. All countries report respectable GDP growth, and the growth looks sustainable. Though external and internal imbalances, i.e. in the labour markets, are still quite large, price stability does not seem threatened. Even in Turkey and Serbia, where exchange rates and prices are more volatile, the risks of serious crises are rather low. In addition to macroeconomic stability, the underlying political stability seems to

have improved as well. Though no breakthrough has been achieved in longstanding political problems, the progress in democratization is bringing security and political risks down. The prospects of EU integration have improved during the German EU presidency and will add to the positive economic outlook. GDP growth should stay between 5% and 6% per year, investments and exports will grow even faster and macroeconomic stability should be sustained in the medium run.

Russian economic growth has accelerated in 2007, driven by booming private consumption and investment. Increased expenditures on state-sponsored programmes and industrial policy measures focusing on public-private partnership projects should foster restructuring and innovation. wiiw forecasts ongoing reliance on energy revenues and an average annual GDP growth of more than 5% in the coming years.

In **Ukraine**, strong consumer demand, vigorous investment activity and solid exports have all contributed to impressive GDP growth in 2007. Rising consumption and housing construction are increasingly driven by expanding consumer credit. Imports growing faster than exports will translate into a further current account deterioration. For the year 2008 we expect an economic growth of around 6%.

In **China**, the economy was driven by a rebound of investment, a ballooning trade surplus and an acceleration of consumer demand. The efforts to contain growth have so far not been successful. Recent data point to a continuation of rapid expansion, which may result in a growth rate for the year 2008 of about 10%.

‘High Growth Continues, with Risks of Overheating on the Horizon’

wiiw Research Report No. 341, by Vladimir Gligorov, Sándor Richter et al., July 2007

139 pages including 65 Tables and 25 Figures (in colour).

The Report comprises two regional overviews and seventeen brief Country Reports on the following transition countries: Albania, Bosnia and Herzegovina, Bulgaria, Croatia, the Czech Republic, Hungary, Macedonia, Poland, Romania, Russia, Serbia, Montenegro, Slovakia, Slovenia, Ukraine, Turkey and China.

Available in hard copy (EUR 70.--) or in PDF (EUR 65.--) from wiiw's website, www.wiiw.ac.at. (Individual Country Reports, only in PDF: EUR 10.-- each.) Orders can also be sent to fax (+43-1) 533 66 10-50 or to e-mail koehrl@wiiw.ac.at.

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Overview developments 2005-2006 and outlook 2007-2008

	GDP				Consumer prices				Unemployment, based on LFS ¹⁾				Current account			
	real change in % against previous year				change in % against previous year				rate in %, annual average				in % of GDP			
	2005	2006	2007 forecast	2008 forecast	2005	2006	2007 forecast	2008 forecast	2005	2006	2007 forecast	2008 forecast	2005	2006	2007 forecast	2008 forecast
Czech Republic	6,5	6,4	5	5,2	1,9	2,5	3	2,8	7,9	7,1	6,3	6	-1,6	-3,1	-4,3	-4,4
Hungary	4,1	3,9	2,7	3,1	3,6	3,9	7,0	3,5	7,2	7,5	7,7	7,7	-6,9	-5,8	-4,6	-3,8
Poland	3,6	6,1	6	5,5	2,1	1,0	2,3	2,5	17,8	13,9	11	10	-1,7	-2,3	-3,0	-3,5
Slovak Republic	6,0	8,3	8,5	8	2,7	4,5	3	2	16,2	13,3	11	10	-8,6	-8,3	-4,7	-4,1
Slovenia	4,0	5,2	5	5	2,5	2,5	2,6	2,3	6,6	6,0	5,8	5,5	-2,0	-2,5	-2,2	-1,5
NMS-5 ²⁾³⁾	4,5	5,9	5,4	5,2	2,4	2,1	3,3	2,7	14,1	11,5	9,7	9	-3,1	-3,5	-3,6	-3,7
Bulgaria	6,2	6,1	6	6	5,0	7,3	5	5	10,1	9,0	7,5	7	-12,0	-15,8	-16,5	-15,0
Romania	4,1	7,7	6,0	5,5	9,0	6,6	4,0	4,5	7,1	7,2	7	7	-8,7	-10,3	-13,0	-11,6
Estonia	10,5	11,4	9,5	8,4	4,1	4,4	5,5	5	7,9	5,9	5	4,5	-10,5	-14,8	-13,8	-11,5
Latvia	10,6	11,9	8,9	8	6,7	6,8	7,5	7	8,7	6,8	6	5,5	-12,6	-21,1	-19,5	-19,0
Lithuania	7,6	7,5	7	6,5	2,7	3,8	5	5	8,3	5,6	4,5	4	-7,2	-10,8	-11,1	-10,4
NMS-10 ²⁾³⁾	4,8	6,5	5,7	5,5	3,6	3,2	3,7	3,3	9,7	10,0	8,7	8,1	-4,6	-5,7	-6,2	-6,0
EU-15 ³⁾	1,6	2,8	2,7	2,5	2,1	2,2	.	.	7,9	7,4	6,9	6,5	0,01	-0,15	.	.
EU-25 ²⁾³⁾	1,9	3,1	3,0	2,8	2,1	2,2	2,0	1,9	8,8	8,0	.	.	-0,18	-0,40	.	.
EU-27 ²⁾³⁾	1,9	3,2	3,0	2,8	2,3	2,3	2,0	2,0	8,7	7,9	7,2	6,7	-0,27	-0,51	.	.
Croatia	4,3	4,8	5	5	3,3	3,2	2,8	2,3	12,7	11,1	10,8	10,3	-6,3	-7,6	-7,7	-7,1
Macedonia	3,8	3,1	4	4	0,5	3,2	3	3	37,3	36,0	35	35	-1,4	-0,4	-1,9	-1,8
Turkey	7,4	6,1	5,5	6,5	8,2	9,6	7,5	5	10,3	9,9	9,5	9	-6,4	-7,9	-6,9	-6,3
Albania ⁴⁾	5,6	4,9	5	5,5	2,4	2,4	2,5	3	14,2	13,9	14	13,5	-7,4	-7,6	-8,5	-6,6
Bosnia and Herzegovina ⁴⁾⁵⁾	5,5	6,2	6	6	3,0	7,2	3,7	2	44,2	31,1	30	30	-21,3	-11,4	-10,9	-9,2
Montenegro	4,0	6,5	5	5	2,3	3,0	3	3	30,3	30,0	30	30	-8,9	-29,4	-15,2	-15,2
Serbia	6,2	5,7	5	5	16,2	11,6	8	6	20,8	20,9	22	23	-8,5	-11,4	-12,5	-11,5
Russia	6,4	6,7	6,9	5,2	12,5	9,8	8	7	7,2	7,2	7	6,5	11,0	9,6	6,6	5,3
Ukraine	2,6	7,1	6,5	6	13,5	9,1	10	9	7,2	6,8	6,5	6,4	3,1	-1,5	-3,8	-4,9
China	10,4	10,7	10,5	10	1,8	1,5	2,8	2	7,2	9,5	8,5	6,6

Note: NMS: The New EU Member States.

1) LFS - Labour Force Survey. - 2) wiiw estimate. - 3) Current account data include flows within the region. - 4) Unemployment rate by registration, end of period. - 5) From 2006 data based on first LFS April 2006.

Source: wiiw (June 2007); Eurostat; forecasts for EU-15 and the Baltic States: European Commission (Spring 2007); wiiw.