

Developments in selected CESEE countries

Economic activity still in full swing, but headwinds are increasing^{1, 2, 3}

1 Regional overview

A weaker international environment and rising international uncertainty...

In the first half of 2018, global growth lost some of the strong momentum registered in the second half of 2017. This is especially true for the euro area, where slower export growth weighed on economic dynamics. In CESEE, the weakening of the external environment is exacerbated by a slowdown in global trade and industrial production as well as by a softening of export orders, which points toward an ongoing period of weaker trade.

More moderate growth numbers and the weaker incoming data that underpin them are due in part to a sharp rise in policy uncertainty since the beginning of the year. One important area where uncertainty has increased notably is international trade relations. U.S. actions (or threatened actions) on tariffs, the responses by its trading partners, and a general weakening of the commitment to the multi-lateral trade system have dented sentiment and could impact investment and trade in the future. In this respect, an especially important factor for the future economic development of the CESEE region is the evolution of global value chains. A process of de-fragmentation in international production would not only directly impact the position of CESEE in the international division of labor, but would also slow the diffusion of technological progress, thereby ultimately lowering productivity and welfare.

...have not yet impacted economic dynamics in CESEE EU Member States

Notwithstanding these international headwinds, CESEE EU Member States – despite mostly being small and open economies – have so far not experienced a noticeable slowdown in growth. On the contrary, growth remained very robust in the first half of 2018. Domestic demand continued to be boosted by good sentiment, higher wages, private sector leveraging and tightening labor markets. Firms are approaching the limits of their production capacity and were increasingly prepared to spend on capital formation. This was in part a reaction to the scarcity of available labor, and investments were directed toward labor-saving technologies in several countries. Public investment and construction continued to be supported by inflows of EU funds. Credit growth has recovered in recent years and currently seems to be broadly in line with economic fundamentals. Credit growth to certain sectors in some countries, however, experienced a boom. This is especially true for mortgage credit in several Central European countries, which among other things was fueled by strong increases in housing prices. These developments warrant close monitoring, and regulators have already taken steps to prevent excesses.

Developments in Turkey and Russia were less benign

Developments in Turkey and Russia were less benign than in the CESEE EU Member States. Financial conditions are tightening in many emerging markets

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² Cutoff date: October 5, 2018. This report focuses primarily on data releases and developments from April 2018 up to the cutoff date and covers Slovakia, Slovenia, Bulgaria, Croatia, the Czech Republic, Hungary, Poland, Romania, Turkey and Russia. The countries are ranked according to their level of EU integration (euro area countries, EU Member States, EU candidate countries and non-EU countries). For statistical information on selected economic indicators for CESEE countries not covered in this report (Albania, Bosnia and Herzegovina, Kosovo, FYR Macedonia, Montenegro, Serbia and Ukraine), see the statistical annex in this issue.

³ All growth rates in the text refer to year-on-year changes unless otherwise stated.

around the globe as they adjust to a tighter monetary policy by the Fed and an impending end of asset purchases by the ECB. In such an environment, rising domestic policy risk and/or geopolitical tensions can pose threats to financial and economic stability.

In Turkey, growth has already slowed noticeably due to a combination of various factors, including economic imbalances that have been building up in recent years, deteriorating international relations with the U.S. and worries about the future shape of economic policy, especially with respect to the independence of central economic policy institutions. Economic turbulence went hand in hand with deteriorating sentiment, sharply rising prices and a notable deceleration of credit growth.

Risks have also increased in Russia. The imposition of a new round of U.S. sanctions against the country, for example, has already contributed to a weakening of the ruble in international markets. The latter is even more remarkable as the weakening of the currency occurred in a period of rising oil prices, a factor that usually supports the ruble's external value. However, the high oil price did fuel a moderate economic expansion throughout the first half of 2018. Growth figures in Russia nevertheless remained well below the respective figures in other countries of the region, especially among the CESEE EU Member States.

Having averaged 3.9% annual GDP growth in 2017, aggregate economic activity in CESEE was at its strongest level for six years. This positive trend continued in the first half of 2018, with growth rates averaging 3.5% year on year. The moderate deceleration compared with last year's performance was mainly related to a slower economic expansion in Turkey. Quarterly growth profiles show that Turkey's economy lost steam especially in the second quarter of 2018, when political tensions and waning trust weighed on private consumption and investment (see table 1). In the other countries of the region, short-term growth dynamics are broadly similar to last year's readings with greater variation only in Romania, Russia and Slovenia.

Private consumption remained the single most important pillar of growth throughout most of the CESEE region, benefiting from good sentiment, rising stocks of household credit, swift wage growth and improving labor market conditions (see chart 1).

Strong economic momentum continues

Tightening labor market conditions fuel wage growth and private consumption

Table 1

Real GDP growth

	2016	2017	Q1 17	Q2 17	Q3 17	Q4 17	Q1 18	Q2 18
<i>Period-on-period change in %, seasonally and working-day adjusted</i>								
Slovakia	3.3	3.4	0.8	0.9	0.9	0.9	1.0	1.1
Slovenia	3.1	4.9	1.8	1.4	1.0	2.0	0.5	0.8
Bulgaria	3.9	3.6	0.9	1.0	0.9	0.7	0.9	0.8
Croatia	3.5	2.9	0.6	0.8	0.8	0.1	0.8	1.1
Czech Republic	2.5	4.3	1.3	2.3	0.5	0.7	0.5	0.7
Hungary	2.2	4.0	1.4	1.1	1.1	1.3	1.2	1.0
Poland	3.0	4.6	1.0	0.9	1.4	1.0	1.6	1.0
Romania	4.8	7.0	2.4	1.5	2.2	0.3	0.1	1.4
Turkey	3.2	7.4	1.4	2.1	1.2	1.8	2.0	0.9
Russia	-1.0	1.5	0.6	0.7	0.1	-0.3	0.9	..
Euro area	1.9	2.4	0.7	0.7	0.7	0.7	0.4	0.4

Source: Eurostat, national statistical offices.

In fact, labor markets are becoming increasingly tight in many countries, especially in the CESEE EU Member States. Unemployment rates have been falling consistently in recent years, from an average level of around 10% in early 2013 to just 4% in August 2018. This represents the lowest reading since the start of transition. Positive labor market developments are also substantiated by several other indicators: Unemployment declined among the most vulnerable age cohorts, namely young persons (under 25 years) and older persons (over 50 years). The trend in long-term unemployment was positive and broad based. Furthermore, employment kept expanding throughout the region, contributing to a convergence of employment rates to euro area levels. Although the highest increases in employment were reported for Turkey and Croatia, these were the countries in the region where employment rates still fell short of average euro area levels as of mid-2018. On the other side of the spectrum, the Czech Republic's employment rate increased to nearly 75%.

The flip side of these positive labor market trends were increasing labor market shortages. According to a survey by the European Commission, labor is increasingly perceived as a limiting factor for production in the CESEE EU Member States: In the third quarter of 2018, at least 43% of respondents struggled to find workers. The respective figures went up to as much as 83% in the case of Hungary. While the potential for immigration from the Western Balkans and Ukraine should be significant and is already alleviating some pressures on labor markets (e.g. in Poland), it is unlikely that immigration can fully offset the lack of workers given the overall restrictive immigration stance of most CESEE governments. Furthermore, geographic mobility in CESEE remains limited, with people's propensity to emigrate often being higher than their willingness to commute. In this context, regional labor market disparities have increased since 2013, with the dispersion of regional unemployment rates going up for nearly all countries where data are available.

Against this backdrop, nominal wages rose powerfully during the review period, increasing by more than 10% year on year, on average, in the first half of 2018. Romania led the ranking with annual increases of more than 30%. Slowly rising inflation rates cut somewhat into purchasing power throughout the region. Nevertheless, real wages also advanced swiftly in the first half of 2018.

In general, strong wage increases were not fully reflected in price developments during the review period. A certain increase in service price inflation could be observed in some CESEE EU Member States. Nominal effective currency appreciation and a certain reduction in corporate profit shares, however, kept core inflation largely in check.

Dynamic labor markets and higher wages positively impacted on sentiment. Consumer confidence as reflected by the Economic Sentiment Indicator of the European Commission reached a historic high in May 2018, some 25 points above the readings of early 2013. Despite some retreat in recent months, sentiment is still clearly above long-term averages. At the same time, demand for consumer credit rose noticeably, providing further impetus for private consumption.

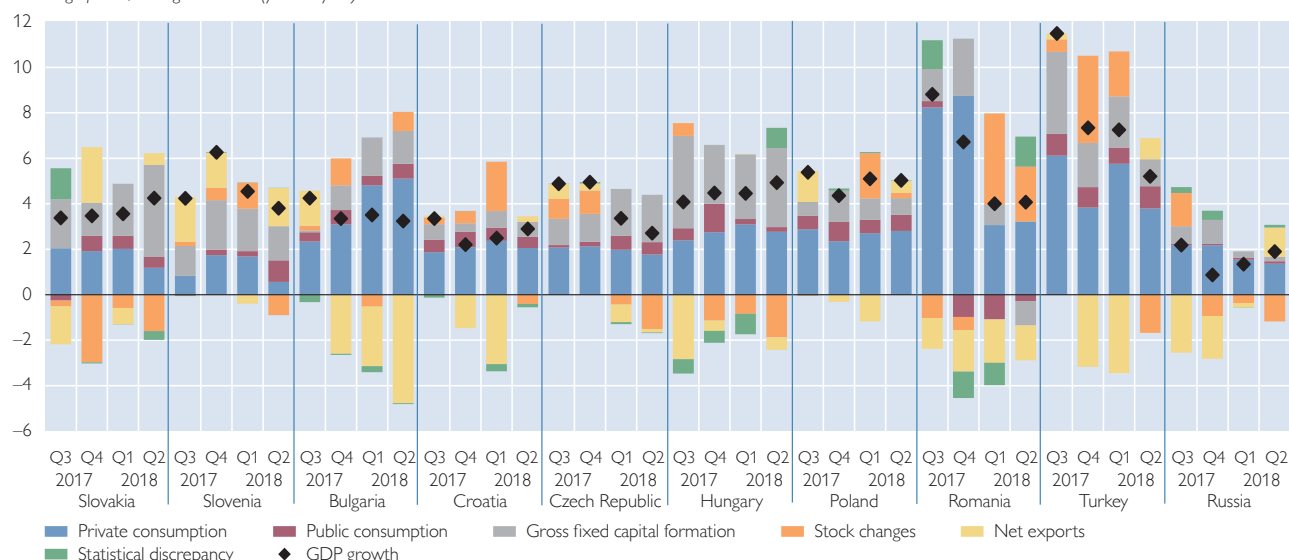
Gross fixed capital formation gained further momentum in most countries throughout the first half of 2018 (see chart 1), with private investment fueled by high capacity utilization rates, full order books, strong industrial confidence, efforts to save on increasingly scarce labor, and improved credit market conditions amid low interest rates. Investment in construction and public investment picked up as well, strongly supported by utilization of EU funds in many countries as the 2014–2020

Higher investment demand as capacities approach their limits

Chart 1

GDP growth and its main components

Percentage points, GDP growth in % (year on year)



Source: Eurostat, national statistical offices.

programming period unfolds. In the CESEE EU Member States, this lifted annual investment growth to an average of 7.6% year on year in the first half of 2018.

Capital formation, however, was less brisk in Russia and Turkey. In both countries, investment growth in the first half of 2018 was lower than in 2017. In Turkey, construction investment weakened and investment in new machinery and equipment practically came to a standstill. Financing costs for (often imported) capital goods increased strongly against the backdrop of the lira's slide and sharply higher interest rates since May 2018.

Moderating external demand put a damper on export growth. Given the region's strong integration into international production networks and a comparatively high import content of domestic export production, import growth moderated in tandem. Dynamic domestic demand, however, kept import growth rates (6.3% in the first half of 2018) above export growth rates (5.1% in the first half of 2018) for the region on average. This translated into an increasingly negative contribution of net exports to GDP growth. Only in Slovenia and Russia did the external sector lift growth somewhat in the first half of 2018.

Export dynamics might also have suffered from a deterioration of price competitiveness that has been observed for several quarters now. During the review period, unit labor cost (ULC) growth in manufacturing (measured in euro) outpaced the respective growth in the euro area in all countries but Russia, Slovenia and Turkey. In general, productivity figures were robust, reflecting increasingly tight labor markets that prevented labor input growth from keeping pace with manufacturing output growth. Some labor-saving investment might also have boosted productivity. At the same time, productivity advances fell notably short of labor cost increases: Labor cost growth in manufacturing was in the high single or even double digits in the first half of 2018 in most countries.

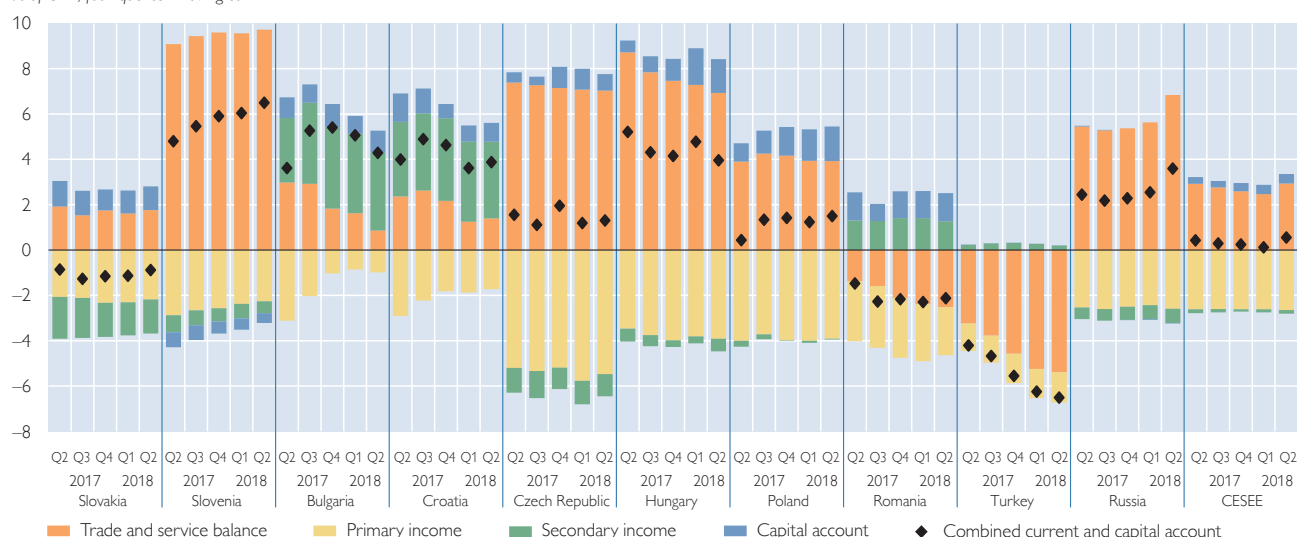
Lower international demand impinges on exports

Ongoing rise in ULCs strains price competitiveness

Chart 2

Combined current and capital account balance

% of GDP, four-quarter moving sum



Source: Eurostat, IMF, national central banks.

Compared with the rest of the region, cost increases were relatively moderate in Russia and Slovenia, which explains part of the good performance of those two countries in terms of price competitiveness. Furthermore, competitiveness in Russia and Turkey also benefited from a strong currency depreciation against the euro.

In addition to ULC trends, survey data also hint toward some weakening of international competitiveness. The European Commission regularly asks firms about their competitive positions in markets inside and outside the EU. While a majority of firms still reported improvements in competitiveness in the third quarter of 2018, the share of such responses decreased noticeably.

Rising headwinds from the international environment also impinged upon the region's external balances. Most countries reported some decline in their combined current and capital account surpluses or increases in their deficits during the review period. These developments were mostly related to weakening trade balances, while the other components of the current account remained broadly unchanged. Notable improvements in the current account were reported only for Slovenia (where the deficit in primary income decreased while the trade balance remained stable) and especially for Russia. The rising oil price and the weakening exchange rate boosted Russia's goods balance. Russia's strong performance was also responsible for the moderate increase in the region's combined current and capital account surplus from 0.2% of GDP in the fourth quarter of 2017 to 0.6% of GDP by mid-2018 (four-quarter moving sums; see chart 2).

The aggregate financial account balance (i.e. the difference between the net acquisition of assets and the net incurrence of liabilities, excluding reserves) of the ten CESEE countries as a whole increased from -5.1% of GDP in the fourth quarter of 2017 to 0.4% of GDP in the second quarter of 2018 (four-quarter moving sums; see chart 3). In other words, the CESEE countries experienced a capital outflow. This development was driven by a higher surplus in other investments which

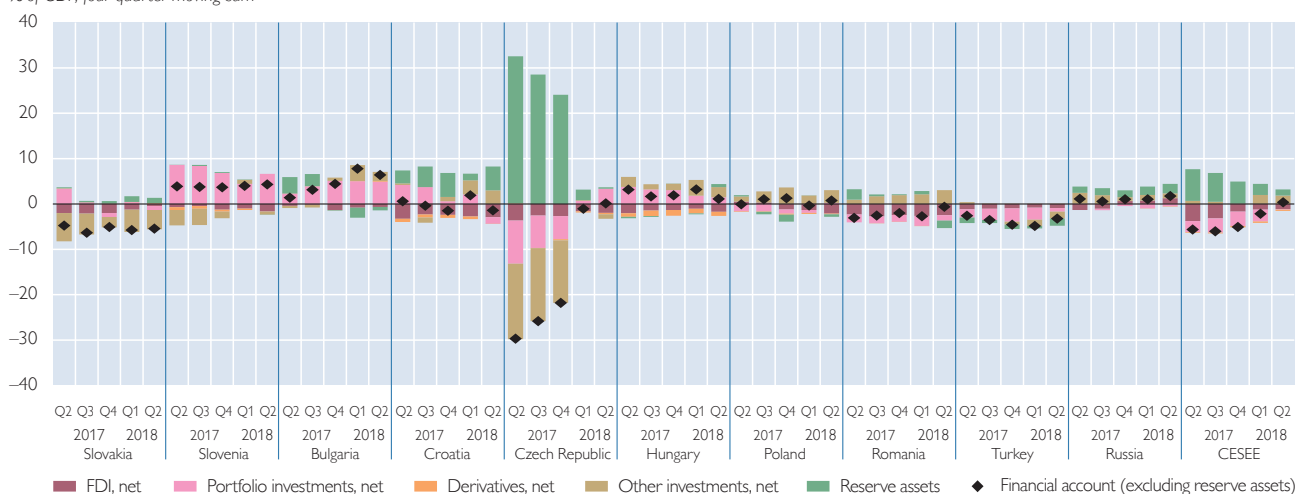
Trade balances weigh on current account positions in many countries

Moderate capital outflows from the CESEE region

Chart 3

Financial account balance

% of GDP, four-quarter moving sum



Source: National central banks.

reflect bank flows. At the same time, a deficit in portfolio investments of the magnitude of some 3% of GDP at the end of 2017 turned into a balanced position in mid-2018.

On a country level, the Czech Republic stands out with notable changes in both portfolio and other investments. A strong buildup of liabilities in those two categories was observed prior to the abolition of the exchange rate floor of the Czech koruna in April 2017, partly for speculative reasons.

Inflation gained some speed during the review period in all CESEE countries. The strongest increase was reported for Turkey, where exchange rate depreciation lifted the inflation rate to 17.9% in August and to 24.5% in September 2018. Price growth in Turkey was also fueled by still considerable demand pressures and the pass-through of strong producer price inflation. Producer prices increased by 46.2% in September 2018. A notable acceleration of inflation was also reported for Bulgaria, where service price growth outstripped HICP growth by a large margin.

In general, rising price pressures primarily reflected stronger inflation in energy goods not least related to rising oil prices in world markets (see chart 4). At the same time, service price growth also started to accelerate somewhat in many countries, putting moderate upward pressure on core inflation. In most CESEE countries, however, inflation as well as core inflation remained contained.

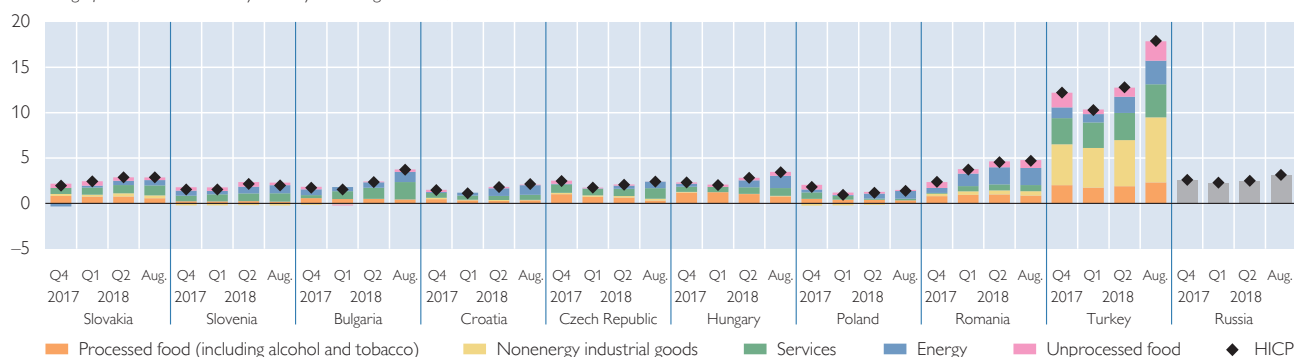
Domestic price pressures have been building up especially in the CESEE EU Member States over the past two years: Tight labor markets and strong wage growth pushed up aggregate ULC growth. Capacity utilization has been rising since late 2016 and is now above pre-crisis levels. According to the European Commission, the output gap turned positive in 2017 and is projected to widen further in 2018 and 2019. These factors have not yet had a stronger impact on inflation as nominal effective exchange rates in the countries of the region appreciated especially in 2017 and remained strong throughout 2018. Furthermore, there is evidence that corporate sector profit ratios have declined in recent quarters, absorbing some of the upward pressure of wages on prices.

Energy prices drive up headline inflation while core inflation continues to be surprisingly contained

Chart 4

HICP inflation and its main drivers

Percentage points, contribution to year-on-year change in HICP; HICP in %



Source: Eurostat.

Note: CPI data for Russia. No breakdown according to COICOP available.

Missed inflation targets and/or currency depreciation necessitate monetary tightening

The Czech Republic was the first country among the CESEE EU Member States to end the period of monetary accommodation that started in late 2012. The Czech central bank (CNB) adhered to a policy of gradual monetary tightening during the review period and hiked its policy rate in three steps from 0.75% in June to 1.5% in October 2018 (see chart 5). According to CNB projections, inflation will be above the target for the rest of the year 2018.

The Romanian central bank (NBR) increased its policy rate in May 2018, from 2.25% to 2.5%. At the same time, it raised the deposit facility rate to 1.5% and the lending facility rate to 3.5%. This step was motivated by accelerating inflation that consistently overshoot the inflation target. The NBR expects inflation to decline towards the upper bound of the variation band around its target by the end of 2018. Upward risks to inflation stem, among other things, from the fiscal policy stance and labor market conditions.

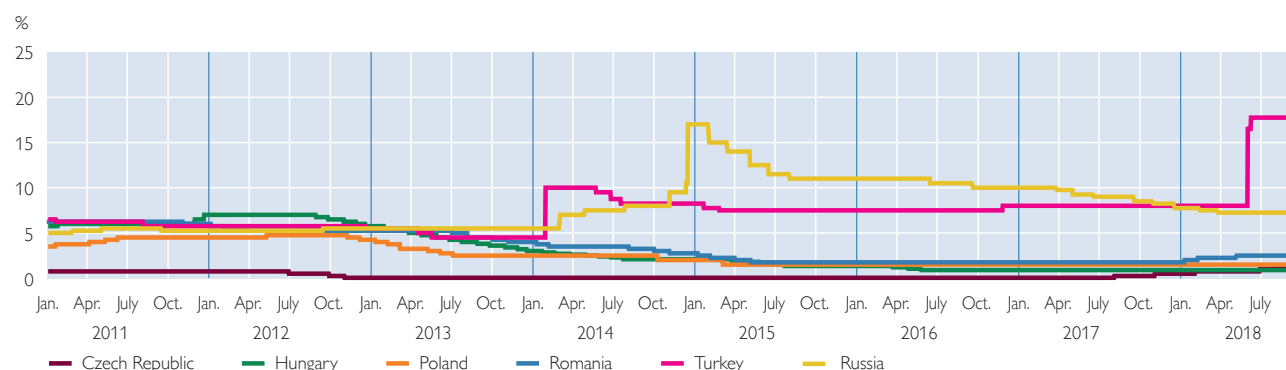
In Turkey, the central bank (CBRT) reacted to the depreciation of the Turkish lira and the increase in inflation by initially hiking its one-week repo auction rate from 8% to 17.75% in June 2018. On September 13, more than a month after financial market turbulence worsened, the CBRT increased its policy rate by a further 625 basis points to 24%. These measures were flanked by a row of liquidity and regulatory measures targeted at banks.

In September 2018, the Russian central bank (CBR) hiked its policy rate for the first time since January 2015, lifting it by 25 basis points to 7.5%. The ruble's depreciation, supply-side-related food inflation and increased inflation expectations were among the key drivers that motivated this step. The ruble depreciated notably throughout the year in reaction to the harsher-than-expected U.S. sanctions, the possibility of a new round of sanctions and the finance ministry's foreign-exchange purchases to replenish the reserve fund.

Stable and broadly solid credit developments throughout most of CESEE

Growth of domestic credit to the private sector (nominal lending to the non-bank private sector adjusted for exchange rate changes) was solid and broadly in line with fundamentals throughout most of CESEE. Credit growth accelerated moderately in most countries (see chart 6) reflecting favorable general economic conditions in an environment of low interest rates and heightened competition

Chart 5

Policy rate developments in CESEE

Source: National central banks.

among banks. Credit growth reflected to some extent a substantial increase in housing loans which went hand in hand with rising real estate prices. Housing prices rose by some 8% year on year in the first half of 2018, notably quicker than in the second half of 2017 (6.4%). Price increases of more than 10% were reported for Hungary, Slovenia and Turkey.

Notwithstanding the country's still modest economic growth and high NPL ratio (19.2% in mid-2018), lending growth in Russia accelerated throughout 2018 and was the highest in the CESEE region. The revival was largely driven by retail credit, which rose by 20.6% in August 2018, while credit to enterprises increased by only 11.6%. Mortgage loans and unsecured consumer credit have grown particularly briskly, which gives rise to concern. The CBR has responded by increasing its risk-weightings for high-interest mortgage and consumer loans.

Credit growth accelerated notably also in Croatia and Hungary. In Croatia, the availability of bank financing on the market and favorable liquidity led to lower interest rates and to an easing of credit standards for corporates. Among households, demand for housing loans increased in connection with a positive outlook for the real estate market and consumer confidence while the consumption of durable consumer goods spurred growth in the demand for other types of household loans. In Hungary, corporate lending benefited from the central bank's Market-based Lending Scheme, while lending to households was bolstered by expanded housing subsidies.

A certain moderation of credit growth over the past months was reported for the Czech Republic, Slovakia and Slovenia. In Slovenia, consumer credit largely sustained its momentum, while credit growth to corporations decelerated as increasing corporate profits enabled companies to satisfy their investment needs by means of retained earnings.

In the Czech Republic and Slovakia, credit growth declined against the backdrop of regulatory action (however, credit to Slovak households continued to grow, remaining in the double digits). Specifically, since 2016 banks in both countries are required to hold countercyclical capital buffers. Those buffers have repeatedly been raised to their current levels of 1% in the Czech Republic and 1.25% in Slovakia. Further increases of the buffer rates are in the pipeline, to

Tightening financial conditions lead to a marked deceleration of credit growth in Turkey

Lending surveys indicate easing supply conditions

1.25% in January 2019 and to 1.5% in July 2019 in the Czech Republic, and to 1.5% in August 2019 in Slovakia. Furthermore, both countries introduced measures to put a brake on the expansion of housing loans. The Slovak central bank (NBS) placed new limits on debt-to-income ratios for housing and consumer loans and tightened loan-to-value limits for housing loans in July 2018. The Czech central bank introduced stricter loan-to-value ratios for housing loans already in 2017.

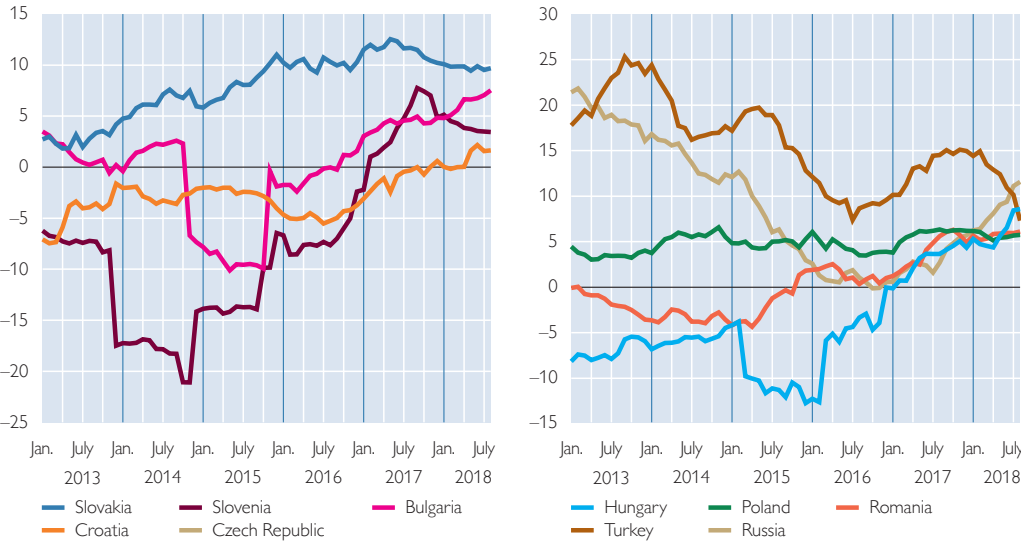
The largest deceleration of credit growth was observed in Turkey (from a peak of 15% in December 2017 to 7.3% in August 2018) as financial conditions tightened substantially. The weighted average cost of CBRT funding increased from 12.75% at the end of 2017 to 24% in October 2018. Apart from higher borrowing costs, the slowdown also reflected the moderating economic momentum and fading effects of the government’s subsidized loan schemes. As of mid-2018, the NPL ratio in the Turkish banking sector remained low at 3.2% but the quality of bank assets might actually be lower than this figure suggests (due to sales of NPLs and the rollover of potentially distressed loans under the government’s loan guarantee scheme). The banking system had an overall capital adequacy ratio of 15.9% at the end of June 2018 (13.1% when counting only tier-1 capital). The sharp depreciation of the Turkish lira, however, is weighing on the capital ratio, given that risk-weighted assets are partially denominated in foreign currency. The Turkish supervisor has temporarily allowed banks to calculate their capital ratios with the exchange rate of end-June 2018.

Lending surveys indicate a continued strength in demand for credit in the CESEE region. According to the most recent CESEE Bank Lending Survey by the European Investment Bank, demand for credit improved across the board in the first half of 2018. This marked the tenth semester of favorable developments. All factors affecting demand made positive contributions. Notably, investment accounted for a good part of the strengthening in demand, whilst debt and corporate

Chart 6

Growth of credit to the private sector

Year-on-year percentage change, adjusted for exchange rate changes



Source: National central banks.

restructuring were almost irrelevant. Access to funding also continued to improve in CESEE, supported by easy access to domestic sources (mainly retail and corporate deposits).

Increasing demand was paired with an easing of aggregate supply conditions in the first half of 2018 – the second significant easing over the past two years. At the same time, the gap between credit demand and credit supply that had been perceived for several quarters continued to persist. On balance, this would imply an improvement of the loan quality associated with most of the new lending compared with previous credit cycles. Across the client spectrum, credit standards eased especially for SME lending and consumer credit, while they tightened for mortgages. Changes in local regulations and groups' NPLs were perceived as key factors adversely affecting supply conditions.

Country-level bank lending surveys conducted by national central banks mostly corroborate these findings: More or less all countries reported rising demand for loans across sectors. With respect to lending conditions, several countries (e.g. Czech Republic, Croatia, Poland and Romania) reported some tightening, especially in the area of loans for housing purchases.

While remaining on generally very solid levels, leading indicators softened during the review period (see chart 7). With regard to activity indicators, industrial production growth declined from an average of 5.3% in February to 3.9% in July 2018. The decline was relatively broad based. The most substantial weakening, however, was reported for Turkey against the backdrop of increasing general economic tensions. Retail sale growth decelerated too: At 4.1% in July, it was 1.5 percentage points lower than in February 2018. On a country level, the largest decrease was again observed in Turkey, but sales moderated somewhat in most

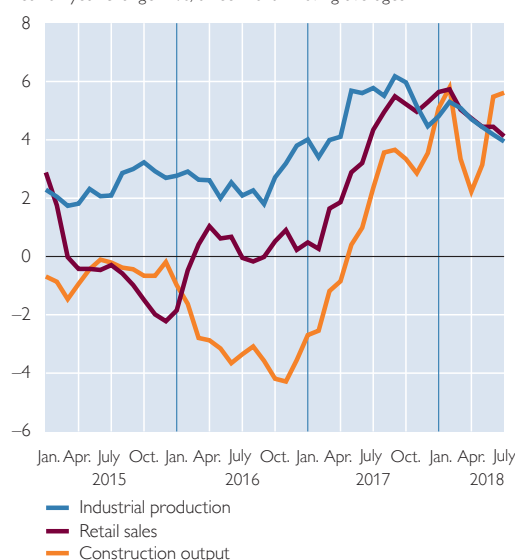
Softening high-frequency and sentiment indicators point toward decelerating growth

Chart 7

Leading indicators

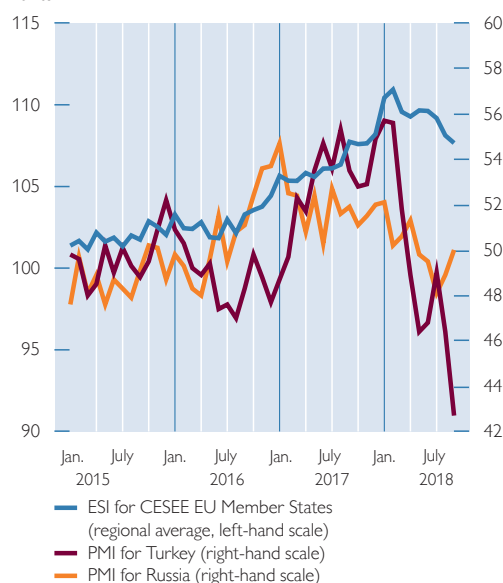
Activity indicators (CESEE regional average)

Year-on-year change in %, three-month moving averages



Sentiment indicators

Points



Source: Eurostat, wiw, European Commission, Markit.

other countries too. Construction output held up best among activity indicators, with broadly unchanged growth rates between early and mid-2018. The figures displayed a high degree of volatility, however.

Economic sentiment deteriorated throughout the region. The Economic Sentiment Indicator (ESI; average for the CESEE EU Member States) retreated from its peak in early 2018 to reach an average of 107.7 points in September 2018. This reading, however, still is notably above the long-term average. The decline in the index was most pronounced in services and industry, while sentiment in construction continued to brighten somewhat. The Purchasing Managers' Index (PMI) for Russia decreased to levels below 50 (the threshold indicating an expansion) over the summer months, before coming back to this level in September 2018. Reflecting the general economic situation, the PMI for Turkey plummeted from 55.7 points in January to only 42.7 points in September 2018.

The softening of leading indicators is already reflected in recent GDP growth forecasts for Turkey. The IMF, for example, cut its projection for 2019 from 4.4% in April to 0.4% in October 2018. Forecasts for the CESEE EU Member States and Russia remained broadly stable over time. However, at around 3.5% (for CESEE EU Member States) and 1.5% (for Russia), growth in 2019 is expected to turn out lower than in 2018. For a detailed outlook for the CESEE region, see "Outlook for selected CESEE countries" in this issue.

Box 1

Ukraine: new official financing crucial for building up FX reserves in view of debt repayment constraints and election-related uncertainties

In the first half of 2018, GDP growth accelerated to 3.5% on the year from 2.5% in 2017, with domestic demand remaining the key driver. Private consumption benefited from increasing real wages and pensions as well as from remittances, while gross fixed capital formation was on the rise inter alia due to road and transport infrastructure projects. Public consumption also increased somewhat. Export performance was rather weak, posting a contraction in the first quarter and only a small increase in the second quarter of 2018. Imports showed similar dynamics, but the negative contribution of net exports declined on balance. Moreover, it should be noted that agricultural output increased on the year because the grain crop harvest started earlier than usual. While GDP growth gained momentum, annual CPI inflation decelerated markedly, nearing the upper bound of the central bank's target range (6.5% \pm 2 percentage points as of the end of the third quarter of 2018) in August 2018 at 9%. Core inflation, which has also been declining this year, reached 8.7% in August 2018. These developments notwithstanding, the National Bank of Ukraine (NBU) decided to hike its key policy rate by 50 basis points, to 18%, in early September 2018, citing various risks to the disinflation trend.

The current account deficit stood at 2.2% of GDP in the four quarters up to mid-2018, thus remaining broadly unchanged compared with 2017. With the trade and services balances showing a considerable deficit (of almost 7% of GDP), the current account deficit was kept in check by surpluses in the income balances arising from income generated by Ukrainians abroad, particularly in Poland. Net FDI inflows (partly related to debt-to-equity transactions) covered almost 80% of the current account deficit in the four quarters up to mid-2018. Despite a noticeable reduction in recent years, Ukraine's gross external debt is still very high (EUR 97 billion or 95.4% of GDP in mid-2018). For comparison, official FX reserves amounted to EUR 14 billion (excluding gold) at end-August 2018. With sizeable public external debt repayments coming up, further IMF disbursements would be crucial for building up FX buffers. Doubts over a further IMF tranche together with other domestic and external factors fueled pressures on the hryvnia during the summer, as evidenced by some depreciation and foreign currency sales by the NBU. Moreover, presidential and parliamentary elections in 2019 might bring about heightened uncertainties.

The structural reform agenda has been moving forward this year with the parliamentary endorsement of a bill to create a specialized anti-corruption court (and amendments demanded by the IMF). This step raised the chances for concluding the pending review under the IMF Extended Fund Facility (EFF), on which discussions had started in May 2017. Yet, agreements on fiscal policy issues and on household gas and heating tariff increases were still outstanding until recently. Eventually, the Ukrainian authorities opted to negotiate a new arrangement that will replace the EFF (which would have expired in March 2019). Following an IMF mission to Kyiv in September, a staff-level agreement on a USD 3.9 billion 14-month stand-by arrangement (SBA) was made public in mid-October immediately after the government had announced an increase in household gas and heating tariffs. The IMF Executive Board will consider the new SBA following parliamentary adoption of a government budget for 2019 that is in line with IMF staff recommendations. Approval of the new SBA would also help to unlock external funding from other sources, inter alia from the EU under the fourth macro-financial assistance program (signed in September 2018), under which EUR 1 billion could be made available in two installments.

Western Balkans¹: keeping the growth momentum despite rising headwinds

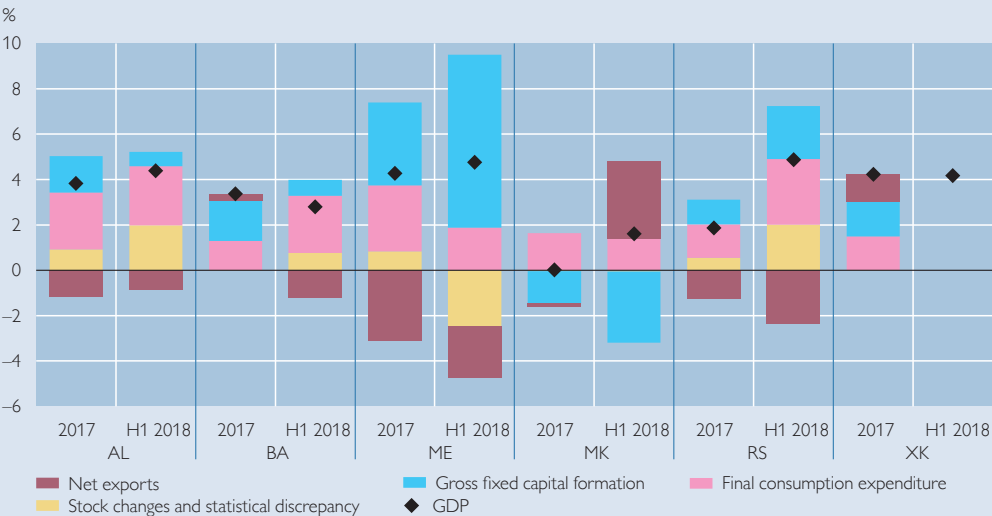
Economic growth kept pace in the first half of 2018 in all Western Balkan countries. On balance, (unweighted) output growth rose to 3.8% on average, from 2.9% in 2017, with year-on-year growth ranging from 1.6% (in the former Yugoslav Republic (FYR) of Macedonia) to 4.9% (in Serbia). FYR Macedonia and Serbia also happened to be the countries that experienced the strongest economic headwind. In Montenegro, Albania and Kosovo, GDP growth remained elevated but broadly flat compared with full-year 2017 figures (4.8%, 4.4% and 4.2 %, respectively), while GDP growth in Bosnia and Herzegovina decelerated to 2.8% in the first half of 2018.

In most of these economies, domestic demand remained the main driver of GDP growth in the first half of 2018 (see chart 1). Upbeat growth of employment and wages continued to fuel private consumption, while fiscal stimulus pushed up public investments especially in the infrastructure and energy sectors, thus compensating for lukewarm private (foreign direct) investments in some countries.

At the same time, net exports were less of a drag on, and even turned supportive for, GDP growth in some Western Balkan countries in the first half of 2018 as compared to 2017. In FYR Macedonia, the strong export performance of the automotive industry coupled with weaker imports added to growth while sizeably narrowing external imbalances. In Kosovo and Albania, exports benefited from rising commodity and basic metals prices, helping Albania to narrow its external imbalances (see chart 2). In Montenegro, the solid increase of exports was overshadowed by the high import content of investments mainly related to the Bor-Boljare highway, thus lifting the four-quarter moving average current plus capital account deficit to 21.4% of GDP by June. On the financing side, net FDI inflows increased in all countries but Montenegro and Kosovo. Overall, the current account deficit was fully covered by net FDI in Albania, Serbia and FYR Macedonia, while notable coverage gaps were reported for Montenegro and Kosovo.

Chart 1

Robust contribution of domestic demand in first half of 2018



Source: Eurostat, wiw, World Bank.

¹ The Western Balkans comprise the EU candidate countries Albania, FYR Macedonia, Montenegro and Serbia as well as the potential candidate countries Bosnia and Herzegovina, and Kosovo. The designation “Kosovo” is used without prejudice to positions on status and in line with UNSC 1244 and the opinion on the Kosovo Declaration of Independence.

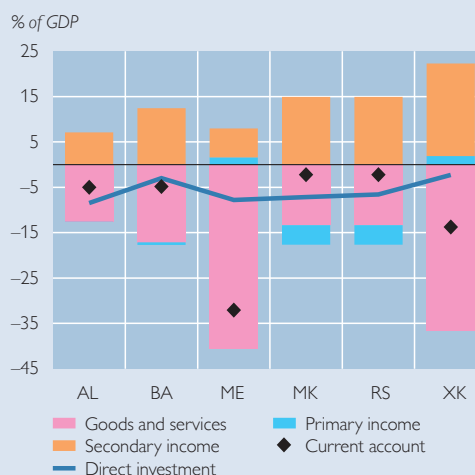
Despite the ongoing economic acceleration and recent reforms in some countries, the rapid employment creation experienced in 2017 slowed down in the first half of 2018 across the Western Balkan countries except for Albania. In Kosovo, employment even contracted by 2 percentage points. According to the Labour Force Survey, employment growth was strongest in Albania (+2.4 percentage points) and Serbia (+1.2 percentage points), with the services and manufacturing sectors apparently accounting for the largest increases according to the World Bank. In Montenegro and Kosovo, employment was also boosted by public sector hiring. Despite these increases, employment rates remained still well below EU-28 levels (i.e. 72.2% in 2017) in the first half of 2018, ranging from 29% (Kosovo) to 59% (Albania). Yet, unemployment continued to decline and hit historical lows in most of the countries in the region (see statistical annex). Compared to the same period of the previous year, Albania and FYR Macedonia reported the biggest unemployment declines, to 12.9% and 21.4%, respectively in the second quarter of 2018. The lower unemployment rates achieved by Bosnia and Herzegovina and Kosovo are somewhat distorted because they are mainly due to declining labor force participation rates by young cohorts given strong emigration and to some extent by lower female participation. Youth unemployment (among those aged 15–24) dropped somewhat in the first half of 2018 in Albania and Montenegro, but remained high in all Western Balkan countries, with levels ranging from 27% (Serbia) and 55% (Kosovo).

Mirroring higher energy prices, stronger domestic demand and tax hikes, consumer price inflation increased somewhat in several Western Balkan countries in the first half of 2018 compared to 2017. Core inflation remained relatively stable in this period, implying contained inflationary pressures. Inflation in Montenegro was the highest in the region (3.6% in the first half of 2018) due to VAT and excise hikes. While also having raised fuel excise duties, Bosnia and Herzegovina and FYR Macedonia managed to keep inflation at 1.1% and 1.6%, respectively, in the same period. In Serbia, inflation declined to 1.7% in the first half of 2018 on the back of subdued food prices and currency appreciation. Kosovo reported the lowest inflation rate in the region (0.3% in the first half of 2018) against the backdrop of declining energy and housing prices.

In contrast to 2017, none of the inflation-targeting countries undershot the lower bound of the inflation target in the first half of 2018. In Albania, lower-than-expected inflation coupled with currency appreciation prompted the central bank to lower its policy rate in June 2018 for the first time since May 2016, by 25 basis points to 1%. To preserve the inflation target and to keep exchange rate appreciation from accelerating further, it also decided to purchase excess currency in the forex market. In Serbia, the latest policy rate cut, to 3% in April 2018, has not been followed by further adjustments, despite mounting appreciation pressures and contained inflation. Moreover, frequent central bank interventions on the foreign exchange market served to reduce exchange rate volatility vis-à-vis the euro (both in nominal and real terms), thus limiting the appreciation of the dinar to close to 2% between April 2018 and September 2018. The central bank of FYR Macedonia, finally, lowered its key interest rate in August 2018, by 25 basis points to 2.75%, citing sluggish domestic demand and improved external position.

Chart 2

Current account and FDI



Source: IMF, national central banks, World Bank.

Note: Positive (negative) values for direct investment positions indicate that net acquisition of assets is higher (lower) than the net incurrence of liabilities.

On the back of resolution mechanisms put in place in some Western Balkan countries, bank asset quality gradually improved and overall supported credit growth (see statistical annex). Albania continued to record the highest nonperforming loan (NPL) ratio in the region (13.3% in mid-2018) despite the introduction of new insolvency legislation, while Serbia managed to cut back NPLs substantially, to a historical low of 9.7% in the first quarter of 2018, supported by ongoing sales of NPLs to asset management companies. In Montenegro, asset quality improved also due to the effective implementation of legislation on voluntary financial restructuring and despite the application of stricter financial reporting standards (IFRS 9), thus bringing the NPL share down to 7% by June 2018. Kosovo, while having failed to put in place a NPL resolution mechanism so far, has been making progress with the introduction of a new system to enforce collateral recovery. This contributed to the decline of the NPL share to 2.8% as of June 2018.

The ongoing process of bank balance sheet cleaning, more favorable lending conditions and elevated domestic demand fed through to credit dynamics in most countries. The first half of 2018 was marked by an acceleration of credit growth. Albania was the only country to buck the regional trend, with lending decelerating somewhat, to 3.2% year on year in the first half of 2018, but this decline also reflected the lek appreciation and loan write-offs. As a common feature among all Western Balkan countries, the growth of lending to households used to outpace the growth of corporate lending for years. In Kosovo and in Bosnia and Herzegovina, however, corporate lending growth has since become as high as the growth of lending to households. Overall, lending to the nonfinancial private sector was the strongest in the first half of 2018 in Kosovo (10.9%), FYR Macedonia (8.2%) and Serbia (8.1%). On a positive note, currency risks in the private sector portfolios declined somewhat on the back of the ongoing implementation of de-euroization measures. With the Albanian authorities having adopted a comprehensive de-euroization strategy in January 2018, de-euroization has also become more widespread. De-euroization will, however, be a protracted process, as foreign currency loans continue to account for high shares of overall lending, ranging from some 42% of total loans (FYR Macedonia) to nearly 67% (Serbia).

Fiscal imbalances remained broadly unchanged at best in most of the Western Balkan economies in the first half of 2018 despite robust revenue growth. Improved tax collection and higher revenues from indirect taxes coupled with lower interest payments are expected to have kept fiscal balances on the positive side only in Serbia. In addition, expenditure-led consolidation in Serbia and Montenegro is ongoing. Montenegro should be able to meet the 2018 annual budget target of 2.8% of GDP, not least because of a comprehensive tax reform, including a VAT hike. In contrast, fiscal imbalances widened in Kosovo due to rising public sector wages and pensions for war veterans. Similarly, the fiscal position of Bosnia and Herzegovina markedly deteriorated during 2018 due to increased pre-election expenditures prior to the general elections in October 2018. However, even the countries pursuing expenditure consolidation policies have been investing more during 2018, targeting mainly infrastructure and public utilities. Only in FYR Macedonia were increased fiscal expenditures largely directed to pensions, subsidies, and social assistance, with capital spending declining. Helped by accelerating GDP growth and despite rising fiscal deficits, the stock of public debt (including publicly guaranteed debt) was on a decline in most of the Western Balkan economies in the first half of 2018. In Serbia, public debt shrank only somewhat until June 2018, to 59.7% of GDP, yet following a decrease of almost 10 percentage points in 2017. Small debt increases were reported by Kosovo and by Bosnia and Herzegovina, but they have kept their public debt ratios at low levels (i.e. 16.3% and 36.3% of GDP, respectively as of June).

As of the third quarter of 2018, Bosnia and Herzegovina as well as Serbia are the only countries in the region to have programs with the IMF in place. In Bosnia and Herzegovina, slow progress with the implementation of structural reforms considerably delayed the completion of the second review under the Extended Fund Facility (initially approved in September 2016). The planned disbursement of a tranche of EUR 38 million was postponed by the IMF in July, with reference to the pre-election weakening of the fiscal position due to higher public sector wages and social transfers. Serbia reached a staff-level agreement with the IMF in June on a

30-month policy coordination instrument, without having drawn any funds under the IMF stand-by arrangement concluded in February. With respect to EU accession, Montenegro remains most advanced in the negotiation process. So far, 31 out of 35 chapters have been opened, most recently chapter 17 on economic and monetary policy on June 25. In FYR Macedonia, a consultative referendum was held on September 30 on the country's name. Voter participation was well below 50%, but the majority of those who exercised their voting right supported the agreement with Greece. The corresponding bill has since been approved by parliament, but parliamentary approval is still outstanding in Greece.

2 Slovakia: economic growth robust but constrained by tight labor market conditions

Investment becomes the dominant driver of economic growth

Slovakia's real GDP growth accelerated in the first half of 2018 to nearly 4% compared to 3.4% last year. In the second quarter of 2018, the economy grew at the fastest year-on-year rate observed since end-2015. Economic expansion continued to be driven by domestic demand on the back of ongoing household spending and particularly by a sustained swift increase in gross fixed capital formation. After having accelerated for more than a year, household consumption growth started to gradually peter out in the last quarter of 2017 and slowed down noticeably in the second quarter of 2018. The latter drop – mainly brought about by significantly lower food and beverage consumption – came rather as a surprise given the favorable labor market developments and the ensuing wage hikes. In contrast, public consumption speeded up in the first six months of 2018 compared to 2017 as a whole, not least owing to strong wage growth in the public sector. The weakened contribution of private consumption to growth was counteracted by a massive increase in fixed investment, especially in the automotive sector. However, also public investment strengthened, boosted by a revival in large infrastructure projects and an increased absorption of EU funds. The external sector made a broadly neutral contribution to growth in the first half of 2018, compared to a mildly positive influence in 2017 as a whole. On the one hand, the dent in the contribution of net exports was caused by somewhat weaker external demand. On the other hand, import growth outpaced export growth due to higher investment-driven demand for imports.

Exports supported by investments in the automotive sector

The goods and services trade balance remained positive also in the six months to June 2018. The foreign trade figures benefited from the higher production capacity in the automotive sector and the introduction of new car models, which spurred both the volume and value of exported cars. The current account deficit improved somewhat in the first half of 2018 in comparison to 2017 as a whole, mainly due to a lower deficit of the primary income balance.

Economic growth could be significantly higher if there were no labor shortages

The general government deficit is expected to fall marginally in 2018 compared to the 1% of GDP recorded in 2017. Faster fiscal consolidation is held back by some legislative measures of the government as well as the expected acceleration in healthcare expenditures. As a result, aided by an increasing primary budget surplus, falling debt servicing costs and vigorous GDP growth, the general government debt is projected to trend downward rather mildly to about 49% of GDP this year.

Robust economic growth and the resulting higher demand for skilled labor continue to be echoed in historically high employment levels, record-low unemployment rates and significant wage growth. As the latter increasingly outpaces productivity growth, unit labor costs are rising more quickly. Moreover, shortages of (skilled) labor increasingly put a drag on economic growth. Slovakia's central bank estimates that GDP would increase by an additional 1.3% if all the current job vacancies were filled.

After three years of falling prices, inflation turned positive in 2017 and accelerated further to average 2.7% between January and August 2018. This was mainly due to faster fuel and energy price increases as a result of the continuing rise in the oil price. However, also nonenergy industrial goods prices and services prices contributed to the inflation speedup. Credit to households kept growing at double-digit rates despite macroprudential measures introduced by the Slovak central bank to curb the too swift expansion. The growth of credit to households is driven mainly by mortgages amid interest rates below the euro area average.

Table 2

Main economic indicators: Slovakia

	2015	2016	2017	Q1 17	Q2 17	Q3 17	Q4 17	Q1 18	Q2 18
<i>Year-on-year change of the period total in %</i>									
GDP at constant prices	3.9	3.3	3.4	3.0	3.7	3.4	3.5	3.6	4.2
Private consumption	2.2	2.7	3.6	3.3	3.5	3.9	3.6	3.5	2.2
Public consumption	5.4	1.6	0.2	-1.1	-0.3	-1.4	3.1	3.1	2.5
Gross fixed capital formation	19.8	-8.3	3.2	0.8	-5.4	10.4	6.1	12.5	20.4
Exports of goods and services	6.4	6.2	4.3	8.2	-0.3	3.8	5.7	2.4	8.0
Imports of goods and services	8.4	3.7	3.9	7.7	-0.8	5.9	3.3	3.2	7.8
<i>Contribution to GDP growth in percentage points</i>									
Domestic demand	5.4	0.9	2.6	2.2	3.3	3.6	1.1	4.3	4.1
Net exports of goods and services	-1.5	2.4	0.5	0.8	0.4	-1.7	2.5	-0.7	0.5
Exports of goods and services	5.9	5.8	4.0	7.9	-0.3	3.3	5.6	2.4	7.6
Imports of goods and services	-7.4	-3.4	-3.5	-7.1	0.8	-4.9	-3.1	-3.1	-7.0
<i>Year-on-year change of the period average in %</i>									
Unit labor costs in the whole economy (nominal, per person)	1.6	1.4	2.8	2.2	2.4	4.0	2.7	5.1	4.2
Unit labor costs in manufacturing (nominal, per hour)	-0.4	3.6	6.5	3.4	10.1	7.1	5.6	9.5	7.9
Labor productivity in manufacturing (real, per hour)	4.4	0.4	0.5	2.3	-1.2	0.0	0.9	-0.4	1.7
Labor costs in manufacturing (nominal, per hour)	4.1	4.0	7.0	5.7	8.8	7.1	6.5	9.1	9.7
Producer price index (PPI) in industry	-2.9	-3.9	2.5	2.6	3.0	2.3	1.9	0.9	1.6
Consumer price index (here: HICP)	-0.3	-0.5	1.4	1.0	1.0	1.6	2.0	2.4	2.9
<i>Period average levels</i>									
Unemployment rate (ILO definition, %, 15–64 years)	11.5	9.7	8.2	8.8	8.2	8.0	7.8	7.2	6.7
Employment rate (%, 15–64 years)	62.7	64.9	66.2	65.8	66.1	66.4	66.4	67.1	67.1
Key interest rate per annum (%)	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<i>Nominal year-on-year change in the period-end stock in %</i>									
Loans to the domestic nonbank private sector ¹	11.0	10.3	10.2	11.5	12.3	11.5	10.2	9.9	9.9
of which: loans to households	12.4	13.4	11.8	13.9	13.4	12.3	11.8	12.4	12.3
loans to nonbank corporations	8.9	5.4	7.6	7.7	10.6	10.0	7.6	5.6	5.9
<i>%</i>									
Share of foreign currency loans in total loans to the nonbank private sector	0.5	0.4	0.2	0.4	0.4	0.4	0.2	0.2	0.2
Return on assets (banking sector)	0.9	1.1	0.8	0.9	1.0	0.9	0.8	0.9	0.9
Tier 1 capital ratio (banking sector)	16.5	16.2	16.6	16.6	16.6	16.5	16.6	16.4	16.3
NPL ratio (banking sector)	4.8	4.3	3.6	4.2	4.0	4.0	3.6	3.5	3.4
<i>% of GDP</i>									
General government revenues	42.5	39.3	39.4	..	..	..	..	..	..
General government expenditures	45.2	41.5	40.4	..	..	..	..	..	..
General government balance	-2.7	-2.2	-1.0	..	..	..	..	..	..
Primary balance	-1.0	-0.6	0.4	..	..	..	..	..	..
Gross public debt	52.3	51.8	50.9	..	..	..	..	..	..
<i>% of GDP</i>									
Debt of nonfinancial corporations (nonconsolidated)	51.7	55.0	29.8	..	..	..	..	..	..
Debt of households and NPISHs ² (nonconsolidated)	35.0	38.2	20.4	..	..	..	..	..	..
<i>% of GDP (based on EUR), period total</i>									
Trade balance	1.3	2.0	0.8	1.7	1.5	-0.9	0.8	1.2	2.0
Services balance	0.2	0.6	1.0	0.9	1.1	1.4	0.5	0.8	1.1
Primary income	-1.7	-2.3	-2.3	-1.4	-2.5	-2.5	-2.8	-1.3	-2.0
Secondary income	-1.6	-1.7	-1.5	-1.6	-2.3	-1.3	-0.8	-1.4	-2.4
Current account balance	-1.7	-1.5	-2.1	-0.4	-2.2	-3.3	-2.2	-0.8	-1.3
Capital account balance	3.5	2.0	0.9	0.0	1.8	0.4	1.5	0.4	1.9
Foreign direct investment (net) ³	-0.1	0.6	-2.0	-4.5	-0.7	-3.1	0.0	-1.2	2.4
<i>% of GDP (rolling four-quarter GDP, based on EUR), end of period</i>									
Gross external debt	85.4	90.9	110.8	95.1	95.2	97.3	110.8	111.7	114.2
Gross official reserves (excluding gold)	2.1	2.0	2.3	1.8	2.1	2.1	2.3	2.8	3.2
<i>Months of imports of goods and services</i>									
Gross official reserves (excluding gold)	0.3	0.3	0.3	0.2	0.3	0.3	0.3	0.4	0.4
<i>EUR million, period total</i>									
GDP at current prices	78,896	81,154	84,985	19,340	21,196	22,315	22,135	20,461	22,635

Source: Bloomberg, European Commission, Eurostat, national statistical offices, national central banks, wiw, OeNB.

¹ Foreign currency component at constant exchange rates.² Nonprofit institutions serving households.³ + = net accumulation of assets larger than net accumulation of liabilities (net outflow of capital).

- = net accumulation of assets smaller than net accumulation of liabilities (net inflow of capital).

3 Slovenia: new government takes over solid public finances

Minority government took office in September 2018

Following lengthy coalition talks, a new center-left minority government took office in Slovenia in mid-September 2018. It consists of five parties holding 43 out of 90 parliamentary seats and depends on the support of a left-leaning party. This introduces uncertainty, both regarding the stability of the government and the effectiveness of policy implementation, especially as the government faces politically sensitive issues such as the privatization of two major banks and the reform of the pension, healthcare and long-term care systems.

GDP growth moderates during first half of 2018, but remains healthy

GDP growth slowed to a still healthy 4.2% year on year during the first half of 2018. The growth structure was balanced, with consumption, investments and net real exports all contributing to growth. Private consumption growth benefited from healthy increases in real wages and employment, the continued expansion of consumption loans and a further strengthening in consumer confidence. Public consumption growth surged in the second quarter of 2018, possibly in connection with the parliamentary elections. Investment growth was particularly high in non-residential construction and, to a lesser extent, in machinery and equipment, mirroring historically high capacity utilization in industry and the improved financial position of the corporate sector. Both export and import growth held up well despite the moderation of import demand in major export markets, but net real exports contributed less to the overall GDP growth rate than in 2017.

Structural balance moving away from MTO despite headline budget surplus

According to the European Commission's 2018 Spring Forecast, Slovenia's budget is expected to post a surplus of 0.5% of GDP in 2018 and 0.4% in 2019. Government debt should continue to decline and reach 65% by end-2019. Fiscal developments are set to benefit from the strong economic background while the European Commission expects the structural balance to gradually deteriorate to a deficit of 1.5% of GDP in 2019 (from a deficit of 0.6% in 2017) and thus to move away from Slovenia's medium-term objective (MTO) of a surplus of 0.25% of GDP. In June 2018, the EU Council therefore found that Slovenia faced the risk of significantly deviating from the recommended adjustment path toward the MTO and recommended that measures be taken already in 2018 to comply with the Stability and Growth Pact.

European Commission approved new privatization plan for NLB

In mid-August 2018, the European Commission approved a new privatization plan for Nova Ljubljanska banka (NLB), according to which a first sale tranche of at least 50% plus one share must be sold by end-2018 and the state's stake in the bank will be reduced to 25% plus one share by end-2019. If Slovenia fails to comply with these deadlines, a divestiture trustee will be appointed to complete the privatization. In late July, parliament also passed legislation to shield the NLB from the enforcement of claims by Croatian courts in connection with Yugoslav-era deposits of Croatian citizens.

Inflation remains low despite strong economic and household credit growth

Inflation accelerated from 1.5% in the first quarter of 2018 to around 2% by mid-2018 mainly on the back of energy and unprocessed food prices. Core inflation remained almost unchanged at around 1% over the period. Despite continuing low interest rates, the growth of lending to the corporate sector remained weak during the reporting period as the sector continued to finance investments from internal resources, given good profitability. By contrast, lending to households remained fairly strong, reflecting robust growth in consumption loans. The Slovenian central bank has already called attention to risks in connection with this type of lending (i.e. unsecured loans with relatively long maturities and approved in simplified procedures), even if stable lending growth is seen as necessary to reduce banks' income risks and preserve their profitability amid low interest rates.

Table 3

Main economic indicators: Slovenia

	2015	2016	2017	Q1 17	Q2 17	Q3 17	Q4 17	Q1 18	Q2 18
<i>Year-on-year change of the period total in %</i>									
GDP at constant prices	2.3	3.1	4.9	4.8	4.2	4.2	6.3	4.5	3.8
Private consumption	2.3	3.9	1.9	1.9	0.9	1.6	3.1	3.4	1.1
Public consumption	2.4	2.7	0.5	0.7	0.1	-0.2	1.3	1.2	5.3
Gross fixed capital formation	-1.6	-3.7	10.7	13.8	10.0	7.4	12.0	10.1	8.2
Exports of goods and services	5.0	6.4	10.7	9.8	8.3	12.1	12.7	8.7	9.3
Imports of goods and services	4.7	6.6	10.3	10.2	8.1	10.9	11.8	10.5	8.3
<i>Contribution to GDP growth in percentage points</i>									
Domestic demand	1.7	2.6	3.6	4.0	3.3	2.3	4.7	4.9	2.1
Net exports of goods and services	0.6	0.5	1.3	0.8	0.9	2.0	1.5	-0.4	1.7
Exports of goods and services	3.8	5.0	8.4	7.8	6.4	9.3	9.9	7.3	7.6
Imports of goods and services	-3.2	-4.5	-7.0	-7.0	-5.5	-7.3	-8.4	-7.7	-5.9
<i>Year-on-year change of the period average in %</i>									
Unit labor costs in the whole economy (nominal, per person)	0.3	1.8	1.2	0.3	1.5	1.9	1.2	2.4	3.6
Unit labor costs in manufacturing (nominal, per hour)	-5.2	-5.2	-1.7	-2.8	2.0	-0.2	-5.2	-1.3	-4.1
Labor productivity in manufacturing (real, per hour)	6.0	9.0	8.7	5.9	7.5	10.0	11.5	9.1	7.3
Labor costs in manufacturing (nominal, per hour)	0.5	3.3	7.0	2.9	9.6	9.8	5.7	7.6	2.9
Producer price index (PPI) in industry	-0.2	-1.4	2.2	1.7	2.2	2.3	2.4	2.2	2.1
Consumer price index (here: HICP)	-0.8	-0.2	1.6	2.0	1.4	1.3	1.5	1.5	2.1
<i>Period average levels</i>									
Unemployment rate (ILO definition, %, 15–64 years)	9.1	8.1	6.7	7.9	6.5	6.4	5.9	6.0	5.3
Employment rate (%, 15–64 years)	65.2	65.9	69.3	67.3	69.1	70.4	70.3	69.7	71.1
Key interest rate per annum (%)	0.1	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<i>Nominal year-on-year change in the period-end stock in %</i>									
Loans to the domestic nonbank private sector ¹	-6.5	-2.4	4.8	1.3	3.8	7.8	4.8	4.3	3.5
of which: loans to households	0.1	3.3	6.8	5.2	5.9	7.3	6.8	6.5	6.5
loans to nonbank corporations	-11.2	-7.0	3.1	-2.0	2.0	8.2	3.1	2.3	0.8
<i>%</i>									
Share of foreign currency loans in total loans to the nonbank private sector	3.8	3.2	2.4	3.1	2.8	2.5	2.4	2.3	2.2
Return on assets (banking sector)	0.3	0.9	1.1	1.4	1.3	1.2	1.1	1.4	1.5
Tier 1 capital ratio (banking sector)	20.1	20.2	19.4	20.0	19.9	19.7	19.4	..	..
NPL ratio (banking sector)	9.9	5.5	3.6	5.2	5.0	4.7	3.6	3.2	2.9
<i>% of GDP</i>									
General government revenues	44.9	43.3	43.1	..	..	..	..	..	..
General government expenditures	47.7	45.3	43.1	..	..	..	..	..	..
General government balance	-2.9	-1.9	0.0	..	..	..	..	..	..
Primary balance	0.4	1.0	2.5	..	..	..	..	..	..
Gross public debt	82.6	78.6	73.6	..	..	..	..	..	..
<i>% of GDP</i>									
Debt of nonfinancial corporations (nonconsolidated)	67.8	60.9	27.6	..	..	..	..	..	..
Debt of households and NPISHs ² (nonconsolidated)	27.6	27.4	13.6	..	..	..	..	..	..
<i>% of GDP (based on EUR), period total</i>									
Trade balance	3.8	3.8	3.6	3.6	3.9	4.3	2.7	3.1	3.9
Services balance	4.8	5.4	6.0	5.4	6.1	6.9	5.3	5.8	6.7
Primary income	-3.2	-3.2	-2.6	-2.2	-2.2	-2.8	-3.0	-1.4	-1.8
Secondary income	-1.0	-0.8	-0.6	-0.9	-0.7	-0.5	-0.2	-1.1	-0.3
Current account balance	4.4	5.2	6.4	5.9	7.1	7.9	4.7	6.4	8.5
Capital account balance	1.1	-0.7	-0.5	-0.5	-0.6	-0.5	-0.5	-0.4	-0.3
Foreign direct investment (net) ³	-3.3	-2.2	-1.2	-2.1	1.2	-1.9	-2.1	-1.2	-1.4
<i>% of GDP (rolling four-quarter GDP, based on EUR), end of period</i>									
Gross external debt	120.0	111.0	101.1	109.7	107.3	103.2	101.1	99.6	98.0
Gross official reserves (excluding gold)	1.8	1.5	1.5	1.6	1.5	1.6	1.5	1.4	1.4
<i>Months of imports of goods and services</i>									
Gross official reserves (excluding gold)	0.3	0.3	0.2	0.3	0.3	0.3	0.2	0.2	0.2
<i>EUR million, period total</i>									
GDP at current prices	38,863	40,357	43,000	9,873	10,931	10,995	11,201	10,563	11,642

Source: Bloomberg, European Commission, Eurostat, national statistical offices, national central banks, wiw, OeNB.

¹ Foreign currency component at constant exchange rates.² Nonprofit institutions serving households.³ + = net accumulation of assets larger than net accumulation of liabilities (net outflow of capital).

- = net accumulation of assets smaller than net accumulation of liabilities (net inflow of capital).

4 Bulgaria: robust economic growth increasingly driven by domestic demand

Buoyant domestic demand counterbalanced by slowing exports

Domestic demand in Bulgaria gained further momentum in the first half of 2018. The increasingly positive contributions to economic growth from private consumption and fixed investment were, however, counterbalanced by a further slowdown in exports. As a result, in the first half of 2018 the Bulgarian economy did not grow as dynamically as in 2017. Post-2009 average growth rates are still significantly outpaced, though. A production-side view reveals that the real estate and financial sectors provided a major lift to the economy.

Compared to recent years, gross fixed capital formation grew surprisingly strongly in the first half of 2018 on the back of the government's public infrastructure priorities, a recovery in the use of EU investment funding programs and robust investor confidence indicators. Also, private consumption expanded very significantly, surging in the second quarter of 2018 in particular. The labor market is still improving as unemployment rates are approaching historical lows, but it is also becoming increasingly tight and potentially mismatched; in the first half of 2018, for example, the number of job vacancies grew far more strongly than the number of occupied jobs. On the other hand, annual real wage growth lost considerable steam in the first half of 2018, nearly halving to around 5% compared to the second half of 2017.

Relatively strong pickup in consumer prices compared to previous years

Driven mainly by services and energy price hikes, the annual HICP inflation rate in Bulgaria has climbed gradually from 1.3% in January to 3.7% in August 2018. Due to raised excise duties on tobacco products in place since early 2018 and higher prices of water supply services over the 2018 to 2019 period, administered prices have also contributed significantly to inflation.

Sound financial sector developments support domestic demand

Lending to the domestic nonbank private sector – especially to households – gained further momentum in the first half of 2018. However, credit dynamics still did not outpace buoyant deposit growth and the loan-to-deposit ratio thus continued to decline. Banking sector profitability increased considerably in the first half of 2018, with returns on assets and on equity reaching 1.6% and 13.1%, respectively, in June 2018. Banking sector capitalization, on the other hand, declined somewhat, reaching a still comfortable tier 1 capital ratio of 19.7% in mid-2018. Despite growing loans, the NPL ratio declined only moderately in the first half of 2018 compared to end-2017, but the coverage ratio improved considerably as provisions and reserves expanded.

Adopted roadmap toward simultaneously joining ERM II and the banking union

In the first half of 2018, Bulgaria for the first time held the semiannual presidency of the Council of the European Union. More clarity has been achieved on Bulgaria's path toward ERM II participation. On July 12, 2018, ERM II stakeholders established that a positive assessment on Bulgaria's ERM II entry will be linked to a positive ECB decision on Bulgaria entering into close cooperation with the SSM. Bulgaria applied for close cooperation with the SSM on July 18, 2018, with a view to entering into this cooperation when it starts participating in ERM II. The ECB has already made explicit which Bulgarian credit institutions will be subject to a comprehensive assessment, which can be expected to be concluded by July 2019, approximately, and would be followed by the implementation of the identified follow-up measures. Apart from close supervisory cooperation with the ECB, the Bulgarian authorities committed to implementing, before ERM II entry, additional policy measures related to other financial sector issues, institutional quality and governance.

Table 4

Main economic indicators: Bulgaria

	2015	2016	2017	Q1 17	Q2 17	Q3 17	Q4 17	Q1 18	Q2 18
<i>Year-on-year change of the period total in %</i>									
GDP at constant prices	3.6	3.9	3.6	3.6	3.9	3.8	3.0	3.5	3.2
Private consumption	4.5	3.6	4.8	3.8	5.7	4.6	5.2	3.6	7.3
Public consumption	1.4	2.2	3.2	5.8	1.2	2.5	3.5	1.6	2.8
Gross fixed capital formation	2.7	-6.6	3.8	2.4	4.0	4.2	4.1	10.2	6.3
Exports of goods and services	5.7	8.1	4.0	6.1	3.6	4.6	2.1	5.0	0.5
Imports of goods and services	5.4	4.5	7.2	9.1	6.2	5.4	8.2	4.6	5.8
<i>Contribution to GDP growth in percentage points</i>									
Domestic demand	3.5	1.6	5.3	5.3	5.2	4.0	6.5	3.8	6.7
Net exports of goods and services	0.1	2.3	-1.7	-2.2	-1.5	0.2	-3.4	0.0	-3.5
Exports of goods and services	3.7	5.2	2.6	4.0	2.3	3.2	1.2	3.5	0.3
Imports of goods and services	-3.6	-2.9	-4.3	-6.2	-3.8	-3.0	-4.6	-3.5	-3.8
<i>Year-on-year change of the period average in %</i>									
Unit labor costs in the whole economy (nominal, per person)	2.3	2.5	5.4	2.6	4.1	7.5	8.3	6.1	5.1
Unit labor costs in manufacturing (nominal, per hour)	6.8	6.5	1.0	1.0	-1.0	2.2	2.1	7.1	8.9
Labor productivity in manufacturing (real, per hour)	2.3	2.9	11.1	9.8	12.3	10.5	11.5	3.1	1.4
Labor costs in manufacturing (nominal, per hour)	9.3	9.5	12.2	10.8	11.2	12.9	13.8	10.4	10.5
Producer price index (PPI) in industry	-2.1	-3.1	4.9	5.2	4.3	5.2	5.1	3.1	5.1
Consumer price index (here: HICP)	-1.1	-1.3	1.2	0.8	1.4	0.9	1.7	1.6	2.4
EUR per 1 BGN, + = BGN appreciation	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
<i>Period average levels</i>									
Unemployment rate (ILO definition, %, 15–64 years)	9.3	7.7	6.3	7.0	6.4	5.9	5.7	5.8	5.5
Employment rate (%, 15–64 years)	62.9	63.4	66.9	64.3	67.2	68.5	67.5	66.5	67.9
Key interest rate per annum (%) ¹	..	..	..	..	..	..	..	..	..
BGN per 1 EUR	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0	2.0
<i>Nominal year-on-year change in the period-end stock in %</i>									
Loans to the domestic nonbank private sector ²	-1.9	1.6	4.9	3.7	4.3	5.0	4.9	5.6	6.7
of which: loans to households	-1.4	2.0	6.1	4.6	6.0	5.9	6.1	6.4	9.2
loans to nonbank corporations	-2.2	1.3	4.1	3.1	3.3	4.4	4.1	5.1	5.3
<i>%</i>									
Share of foreign currency loans in total loans to the nonbank private sector	49.9	44.4	37.9	42.5	41.0	39.7	37.9	37.0	36.3
Return on assets (banking sector)	1.0	1.4	1.2	1.2	1.4	1.2	1.2	1.1	1.6
Tier 1 capital ratio (banking sector)	20.5	20.9	20.9	21.3	21.3	21.0	20.9	19.8	19.7
NPL ratio (banking sector)	10.9	9.0	6.9	9.1	8.7	8.1	6.9	6.6	6.6
<i>% of GDP</i>									
General government revenues	39.1	35.2	36.1	..	..	..	..	..	..
General government expenditures	40.7	35.0	35.2	..	..	..	..	..	..
General government balance	-1.6	0.2	0.9	..	..	..	..	..	..
Primary balance	-0.7	1.1	1.7	..	..	..	..	..	..
Gross public debt	26.0	29.0	25.4	..	..	..	..	..	..
<i>% of GDP</i>									
Debt of nonfinancial corporations (nonconsolidated)	96.5	91.3	87.7	..	..	..	..	..	..
Debt of households and NPISHs ³ (nonconsolidated)	23.8	23.2	23.7	..	..	..	..	..	..
<i>% of GDP (based on EUR), period total</i>									
Trade balance	-5.8	-2.1	-4.1	-5.9	-3.2	-1.3	-6.3	-7.3	-6.4
Services balance	6.7	6.1	6.0	1.8	5.3	13.8	2.0	2.7	5.4
Primary income	-4.5	-5.1	-1.1	-2.2	-0.7	-0.6	-1.0	-1.3	-1.2
Secondary income	3.6	3.3	3.7	5.2	3.5	4.4	2.0	4.7	3.1
Current account balance	-0.1	2.3	4.5	-1.0	4.8	16.2	-3.3	-1.2	0.9
Capital account balance	3.1	2.2	1.0	1.1	0.7	1.0	1.3	0.0	1.5
Foreign direct investment (net) ⁴	-5.2	-1.5	-1.4	-2.2	-1.3	-0.7	-1.5	0.5	-0.8
<i>% of GDP (rolling four-quarter GDP, based on EUR), end of period</i>									
Gross external debt	81.6	79.3	74.2	78.8	77.5	74.9	74.2	75.7	72.1
Gross official reserves (excluding gold)	42.2	46.7	44.1	46.5	45.9	46.4	44.1	41.5	42.5
<i>Months of imports of goods and services</i>									
Gross official reserves (excluding gold)	8.0	9.4	8.2	9.0	8.8	8.8	8.2	7.7	7.9
<i>EUR million, period total</i>									
GDP at current prices	45,287	48,129	50,430	10,260	12,347	13,800	14,023	10,982	13,249

Source: Bloomberg, European Commission, Eurostat, national statistical offices, national central banks, wiw, OeNB.

¹ Not available in a currency board regime.² Foreign currency component at constant exchange rates.³ Nonprofit institutions serving households.⁴ + = net accumulation of assets larger than net accumulation of liabilities (net outflow of capital).

- = net accumulation of assets smaller than net accumulation of liabilities (net inflow of capital).

5 Croatia: solid growth, Agrokor settlement plan adopted

Strong private consumption growth, but investment and exports disappoint

GDP growth in Croatia re-accelerated to 2.7% in the first half of 2018, after a temporary slowdown in the last quarter of 2017. Private consumption remained the main growth driver, growing by 3.7% year on year in the first half of the year. It benefited from steadily falling unemployment, an increase in net real earnings and a slow acceleration of credit growth. Gross fixed capital formation advanced by 3.3% in the first half of 2018 against the backdrop of an improving investment climate (with the ESI near all-time highs) and a higher absorption of EU funds. The latter also fueled construction activity, which benefited from rising demand and real estate prices.

Net exports made a negative contribution to growth. Export growth was negative in the first quarter of 2018, partially due to strong base effects, but re-accelerated to 5.6% in the second quarter. Import growth remained strong at 5.1% in the first half of the year. The six-month trade deficit was reported at EUR 4.7 billion, 9% higher than in the same period of 2017. The services balance was supported by another strong tourist season.

On the output side, the main contribution to growth came from wholesale and retail trade, transport, accommodation and food service activities, which expanded by 4.6% in the first half of 2018. Industry and manufacturing output grew by only 0.5% in the first half of 2018.

Fiscal consolidation continues; room for limited fiscal easing

After a small budget surplus in 2017, the Croatian government expects budget deficits of 0.5% of GDP in 2018 and 0.4% of GDP in 2019. The debt-to-GDP ratio continued its decline and stood at 76.2% of GDP at the end of the first quarter. According to Croatia's public debt management strategy, the ratio will be reduced to 69% of GDP by 2020.

Despite ongoing consolidation, the Croatian government should have enough fiscal space to support EU fund absorption and deliver some limited fiscal easing to the private sector. The government just submitted a proposal to parliament that includes lower income and property tax rates from 2019 and a lower VAT rate from 2020.

Central bank continues expansionary stance

Monthly HICP inflation has accelerated over the course of the year and reached 2.1% year on year in August 2018, largely driven by energy price developments. Core inflation remained roughly unchanged at around 0.7%. The national reference rate (average interest rate paid by banks on deposits) continued its downward trend and Croatian kuna liquidity in the banking system increased to a record high of HRK 23.3 billion in July 2018 (+18% since end-2017). In 2018, the Croatian central bank has so far conducted two outright foreign exchange operations, purchasing EUR 726 million from the banking sector. Growth of lending to households accelerated over the first half of the year. Corporate lending growth remained negative.

Croatian outlook improves due to Agrokor settlement

The elevated risks surrounding the restructuring of the Agrokor company have decreased considerably. On July 4, 2018, Agrokor creditors representing 80% of outstanding claims voted in favor of the proposed settlement plan. The decision on the settlement became effective in October 2018, and restructuring could be completed around January 2019. Some risks associated with the orderly implementation of the settlement plan remain. In addition, Uljanik, a Croatian shipbuilding company that employs roughly 4,200 people, has been in severe financial distress. A restructuring solution has yet to be agreed.

Despite the Uljanik situation, the rating agency Standard & Poor's recently revised the outlook on Croatia's BB+ sovereign rating from neutral to positive. Fitch and Standard & Poor's upgraded Croatia's long-term sovereign rating from BB to BB+ earlier in 2018, citing strong GDP growth prospects and an improving fiscal position that will continue to reduce the government debt burden.

Table 5

Main economic indicators: Croatia

	2015	2016	2017	Q1 17	Q2 17	Q3 17	Q4 17	Q1 18	Q2 18
<i>Year-on-year change of the period total in %</i>									
GDP at constant prices	2.4	3.5	2.9	2.9	3.2	3.4	2.2	2.5	2.9
Private consumption	1.1	3.5	3.6	3.5	3.8	3.7	3.4	3.9	3.6
Public consumption	-1.0	0.7	2.7	2.0	2.3	3.1	3.4	2.8	2.5
Gross fixed capital formation	3.8	6.5	3.8	6.1	3.7	3.7	1.9	3.6	3.1
Exports of goods and services	9.4	5.6	6.4	10.6	7.0	5.6	3.8	-0.5	5.6
Imports of goods and services	9.2	6.2	8.1	11.7	6.1	8.3	6.8	5.5	4.7
<i>Contribution to GDP growth in percentage points</i>									
Domestic demand	2.1	3.7	3.5	4.2	3.0	3.4	3.7	5.9	2.8
Net exports of goods and services	0.3	-0.1	-0.6	-1.4	0.2	0.1	-1.5	-3.1	0.2
Exports of goods and services	4.2	2.7	3.1	4.1	3.1	3.7	1.7	-0.2	2.6
Imports of goods and services	-4.0	-2.8	-3.7	-5.5	-2.9	-3.6	-3.1	-2.9	-2.3
<i>Year-on-year change of the period average in %</i>									
Unit labor costs in the whole economy (nominal, per person)	..	..	..	..	..	..	..	..	..
Unit labor costs in manufacturing (nominal, per hour)	51.7	-3.0	2.1	9.1	-3.2	1.0	1.5	5.5	8.8
Labor productivity in manufacturing (real, per hour)	-32.3	7.0	3.5	-2.2	9.1	4.6	2.3	2.5	3.8
Labor costs in manufacturing (nominal, per hour)	2.4	4.2	5.4	6.7	5.6	5.6	3.8	8.1	13.0
Producer price index (PPI) in industry	-3.8	-4.3	2.0	2.1	1.7	1.8	2.2	1.1	2.5
Consumer price index (here: CPI)	-0.3	-0.6	1.3	1.1	1.1	1.4	1.5	1.1	1.8
EUR per 1 HRK, + = HRK appreciation	0.3	1.1	0.9	2.0	1.0	0.9	-0.1	0.4	0.4
<i>Period average levels</i>									
Unemployment rate (ILO definition, %, 15–64 years)	16.4	13.3	11.3	14.1	11.1	9.1	11.0	10.5	7.7
Employment rate (%, 15–64 years)	56.0	56.9	58.9	55.9	59.2	61.0	59.6	59.0	61.1
Key interest rate per annum (%)	..	..	..	..	..	..	..	..	..
HRK per 1 EUR	7.6	7.5	7.5	7.5	7.4	7.4	7.5	7.4	7.4
<i>Nominal year-on-year change in the period-end stock in %</i>									
Loans to the domestic nonbank private sector ¹	-4.0	-3.8	0.8	-1.7	-0.9	0.0	0.8	0.0	2.2
of which: loans to households	-3.2	-4.6	2.3	-0.2	0.1	0.7	2.3	2.3	4.0
loans to nonbank corporations	-5.2	-2.6	-1.1	-3.5	-2.1	-0.9	-1.1	-3.0	-0.3
<i>%</i>									
Share of foreign currency loans in total loans to the nonbank private sector	66.7	60.1	56.9	58.9	58.0	57.7	56.9	56.1	55.5
Return on assets (banking sector)	-1.1	1.3	0.9	0.4	0.5	0.7	0.9	1.4	1.5
Tier 1 capital ratio (banking sector)	19.1	21.3	22.3	21.6	21.7	21.3	22.3	21.6	21.4
NPL ratio (banking sector)	16.7	13.8	11.3	13.9	13.2	12.5	11.3	11.4	11.2
<i>% of GDP</i>									
General government revenues	44.9	46.3	46.0	..	..	..	..	..	..
General government expenditures	48.4	47.2	45.3	..	..	..	..	..	..
General government balance	-3.4	-0.9	0.8	..	..	..	..	..	..
Primary balance	0.0	2.2	3.4	..	..	..	..	..	..
Gross public debt	83.8	80.6	78.0	..	..	..	..	..	..
<i>% of GDP</i>									
Debt of nonfinancial corporations (nonconsolidated)	99.1	96.3	90.0	..	..	..	..	..	..
Debt of households and NPISHs ² (nonconsolidated)	38.3	35.0	34.2	..	..	..	..	..	..
<i>% of GDP (based on EUR), period total</i>									
Trade balance	-15.6	-15.8	-16.8	-18.5	-19.1	-15.8	-14.3	-20.9	-18.1
Services balance	17.9	18.7	19.0	3.5	19.1	43.2	5.3	2.6	18.8
Primary income	-0.7	-3.2	-1.8	-2.1	-3.2	-2.2	0.3	-2.4	-2.5
Secondary income	2.9	2.9	3.6	3.5	4.0	2.8	4.3	3.0	3.4
Current account balance	4.5	2.6	4.0	-13.6	1.0	28.1	-4.4	-17.7	1.6
Capital account balance	0.7	1.4	0.6	0.7	0.9	0.5	0.5	1.0	1.4
Foreign direct investment (net) ³	-0.5	-4.1	-2.4	-2.1	-1.3	-2.5	-3.6	-3.5	-2.0
<i>% of GDP (rolling four-quarter GDP, based on EUR), end of period</i>									
Gross external debt	101.7	89.3	81.8	92.9	84.2	81.8	81.8	82.0	80.0
Gross official reserves (excluding gold)	30.7	29.0	32.1	34.0	29.3	30.8	32.1	33.3	33.3
<i>Months of imports of goods and services</i>									
Gross official reserves (excluding gold)	8.0	7.6	7.8	8.7	7.4	7.6	7.8	8.1	8.1
<i>EUR million, period total</i>									
GDP at current prices	44,623	46,656	48,999	10,816	12,331	13,746	12,107	11,297	13,004

Source: Bloomberg, European Commission, Eurostat, national statistical offices, national central banks, wiw, OeNB.

¹ Foreign currency component at constant exchange rates.² Nonprofit institutions serving households.³ + = net accumulation of assets larger than net accumulation of liabilities (net outflow of capital).

- = net accumulation of assets smaller than net accumulation of liabilities (net inflow of capital).

Growth remains robust thanks to domestic demand

6 Czech Republic: economic boom has passed its peak

After the Czech economy expanded at the second highest pace in a decade in 2017 (4.3%), growth slowed down noticeably in the first half of 2018 (to just above 3%). Real GDP thus grew at rates broadly in line with Czech National Bank (CNB) estimates of potential output. In contrast to last year's positive contribution to the economic boom by both domestic demand and net exports, growth in the first half of 2018 was driven solely by domestic demand. Net exports, in contrast, put a slight drag on growth as a result of weaker external demand. Household consumption remained one of the key growth determinants. It was buoyed particularly by strong growth in disposable income on the back of rising wages, higher social benefits and stronger business income. In addition, consumer expectations remained optimistic despite some recent slight deterioration. The positive contribution of public consumption to economic growth increased in the first half of 2018, mainly owing to accelerated wage growth. Fixed investment continued to post major gains in the first half of 2018 so that its contribution to growth nearly tripled compared with 2017 as a whole. On the one hand, this is ascribable to intensified household housing investment despite tightening monetary policy and credit standards. On the other hand, fixed capital formation by the public and private nonfinancial sectors also strengthened. While the former was spurred mainly by higher drawdown of EU funds, the latter echoes firms' effort to automatize production in the face of labor shortages and rapidly growing wages.

The surplus of the trade and services balance improved on the back of positive terms-of-trade values. As a result, the current account balance turned positive again despite deficits in the primary and secondary income balances. The fiscal surplus recorded in 2017 is expected to remain broadly unchanged this year, rising public sector wages and strong government investment notwithstanding. This is because these higher expenditures will be counteracted by higher revenue stemming from strong economic growth and certain government measures⁴. As a result, gross public debt relative to GDP is projected to decline by about 2 percentage points by end-2018.

"Treat our staff nicely" – labor shortages increasingly dampen the economy

Robust economic growth is taking its toll in the form of a sustained tightening of the labor market. Employment has climbed to new historical highs while the unemployment rate stood at 2.2% in the second quarter of 2018. This is the lowest level since the beginning of transition and still the lowest rate in the EU. The shortage of labor and the resulting wage hikes (which somewhat outpace productivity growth) pose a growing challenge for firms and a barrier to growth. This is exemplified by a restaurant which is said to have put up a sign asking guests for an unusual favor: "Please treat our staff nicely as it is much more difficult to find a waiter than a guest."

Inflation eased somewhat in the first half of 2018 compared with 2017 as a whole, hovering on average around the CNB's target (2% \pm 1 percentage point). This deceleration was brought about mainly by lower food price growth and lower core inflation in the first quarter of 2018. Since the second quarter of 2018, however, food and fuel price growth started to quicken while core inflation accelerated, too. As a result, overall inflation has been picking up over the last couple of months and came in at 2.4% in August.

The CNB expects headline inflation to remain in the upper half of the tolerance band until mid-2019 before it returns to target. Therefore, the CNB has continued its monetary policy tightening; so far in 2018, it has lifted its two-week repo rate by a total of 100 basis points in four steps. The key policy rate was raised most recently to 1.5% on September 27, 2018.

⁴ E.g. the electronic sales registration introduced in the recent past, and VAT control statements.

Table 6

Main economic indicators: Czech Republic

	2015	2016	2017	Q1 17	Q2 17	Q3 17	Q4 17	Q1 18	Q2 18
<i>Year-on-year change of the period total in %</i>									
GDP at constant prices	5.3	2.5	4.3	3.6	3.6	4.9	4.9	3.4	2.7
Private consumption	3.7	3.6	4.3	4.0	4.2	4.4	4.5	4.1	3.8
Public consumption	1.9	2.7	1.3	2.1	1.5	0.6	1.0	3.0	2.7
Gross fixed capital formation	10.2	-3.1	3.3	0.0	3.6	4.6	4.6	8.9	8.8
Exports of goods and services	6.0	4.3	6.7	7.8	4.5	6.7	7.9	3.8	4.3
Imports of goods and services	6.8	2.8	6.0	5.8	3.5	6.4	8.2	5.3	5.0
<i>Contribution to GDP growth in percentage points</i>									
Domestic demand	5.5	1.0	3.2	1.3	2.6	4.2	4.6	4.3	2.9
Net exports of goods and services	-0.2	1.4	1.1	2.3	1.1	0.7	0.3	-0.8	-0.1
Exports of goods and services	5.0	3.5	5.4	6.6	3.7	5.0	6.2	3.2	3.5
Imports of goods and services	-5.2	-2.1	-4.3	-4.3	-2.6	-4.3	-5.9	-4.0	-3.6
<i>Year-on-year change of the period average in %</i>									
Unit labor costs in the whole economy (nominal, per person)	-0.8	3.1	3.6	3.1	4.7	3.1	3.4	6.4	6.6
Unit labor costs in manufacturing (nominal, per hour)	0.3	2.6	0.5	1.8	-1.7	1.8	0.1	4.3	7.2
Labor productivity in manufacturing (real, per hour)	3.7	2.0	6.7	4.9	10.1	5.6	6.2	4.1	2.6
Labor costs in manufacturing (nominal, per hour)	4.0	4.7	7.2	6.8	8.2	7.5	6.3	8.6	10.0
Producer price index (PPI) in industry	-2.4	-3.2	0.8	2.3	1.5	0.1	-0.9	-2.4	-0.2
Consumer price index (here: HICP)	0.3	0.6	2.4	2.5	2.3	2.4	2.5	1.7	2.1
EUR per 1 CZK, + = CZK appreciation	0.9	0.9	2.7	0.1	1.8	3.6	5.4	6.4	3.7
<i>Period average levels</i>									
Unemployment rate (ILO definition, %, 15–64 years)	5.1	4.0	2.9	3.5	3.0	2.8	2.4	2.4	2.2
Employment rate (%, 15–64 years)	70.2	72.0	73.6	72.8	73.3	74.1	74.3	74.2	74.7
Key interest rate per annum (%)	0.1	0.1	0.2	0.1	0.1	0.2	0.4	0.7	0.8
CZK per 1 EUR	27.3	27.0	26.3	27.0	26.6	26.1	25.6	25.4	25.6
<i>Nominal year-on-year change in the period-end stock in %</i>									
Loans to the domestic nonbank private sector ¹	6.7	7.8	6.9	9.2	9.2	8.8	6.9	6.7	6.3
of which: loans to households	7.6	7.2	7.5	8.0	8.1	7.7	7.5	7.6	7.5
loans to nonbank corporations	5.7	8.5	6.2	10.6	10.5	10.1	6.2	5.6	4.9
<i>%</i>									
Share of foreign currency loans in total loans to the nonbank private sector	10.8	13.0	13.3	15.5	14.8	15.2	13.3	14.5	14.8
Return on assets (banking sector)	1.2	1.3	1.1	1.1	1.3	1.2	1.1	1.0	1.2
Tier 1 capital ratio (banking sector)	17.9	17.9	18.7	17.6	18.3	18.0	18.7	18.1	18.3
NPL ratio (banking sector)	5.5	4.6	3.7	4.2	4.0	3.8	3.7	..	..
<i>% of GDP</i>									
General government revenues	41.1	40.2	40.4	..	..	..	..	..	..
General government expenditures	41.7	39.4	38.8	..	..	..	..	..	..
General government balance	-0.6	0.7	1.6	..	..	..	..	..	..
Primary balance	0.5	1.7	2.3	..	..	..	..	..	..
Gross public debt	40.0	36.8	34.6	..	..	..	..	..	..
<i>% of GDP</i>									
Debt of nonfinancial corporations (nonconsolidated)	59.7	58.5	59.8	..	..	..	..	..	..
Debt of households and NPISHs ² (nonconsolidated)	30.5	31.2	32.6	..	..	..	..	..	..
<i>% of GDP (based on EUR), period total</i>									
Trade balance	4.1	5.2	4.7	7.7	5.6	3.3	2.8	6.8	5.3
Services balance	1.7	2.3	2.4	2.5	2.6	2.4	2.2	2.7	2.7
Primary income	-5.6	-5.3	-5.2	-0.4	-7.7	-7.3	-4.8	-3.3	-6.4
Secondary income	0.0	-0.6	-0.9	-1.3	-1.2	-1.1	-0.2	-1.7	-1.0
Current account balance	0.2	1.6	1.0	8.4	-0.6	-2.7	-0.1	4.5	0.6
Capital account balance	2.2	1.1	0.9	0.1	0.6	0.6	2.2	0.1	-0.1
Foreign direct investment (net) ³	1.1	-3.9	-2.7	-5.4	-2.1	-0.9	-2.6	-0.8	-3.4
<i>% of GDP (rolling four-quarter GDP, based on EUR), end of period</i>									
Gross external debt	68.5	73.4	89.2	90.3	92.6	91.9	89.2	86.0	83.6
Gross official reserves (excluding gold)	35.0	45.9	64.1	68.8	68.7	66.7	64.1	61.4	61.2
<i>Months of imports of goods and services</i>									
Gross official reserves (excluding gold)	5.6	7.7	10.7	11.3	11.3	11.0	10.7	10.4	10.4
<i>EUR million, period total</i>									
GDP at current prices	168,522	176,368	191,921	42,814	47,707	49,406	51,994	48,311	51,983

Source: Bloomberg, European Commission, Eurostat, national statistical offices, national central banks, wiw, OeNB.

¹ Foreign currency component at constant exchange rates.² Nonprofit institutions serving households.³ + = net accumulation of assets larger than net accumulation of liabilities (net outflow of capital).

- = net accumulation of assets smaller than net accumulation of liabilities (net inflow of capital).

7 Hungary: approaching the end of loose policy conditions

GDP growth accelerated in the first half of 2018, driven by strong consumption and investment activity

Hungary called on to take corrective action to approach MTO

MNB has signaled intention to start tightening monetary conditions from mid-2019

GDP in Hungary grew by 4.6% year on year during the first half of 2018. Private consumption and gross fixed capital formation were the major pillars of growth, while net real exports made a slightly negative contribution. Private consumption benefited from the acceleration of employment growth, continued heavy wage increases and strong and improving consumer confidence. Vibrant investment activity was boosted by the utilization of EU funds, a notable pick-up in lending to corporates and in lending to households for house purchases amid low interest rates, increased capacity utilization, expanded housing subsidies and a further improvement in economic sentiment. Export growth slowed somewhat, mirroring weaker demand in major export markets and the wage-driven erosion of cost competitiveness. Import growth slowed along with decelerating exports and a substantial run-down of inventories, so that net real exports contributed substantially less negatively than in 2017.

According to the European Commission's spring forecast, Hungary's budget deficit will widen to 2.4% of GDP in 2018. The budgetary stance in 2018 is procyclical, with the structural deficit rising further beyond 3% of GDP and thus further away from the medium-term objective (MTO) of 1.5% of GDP. Having assessed the country's budgetary developments, the European Commission concluded in May 2018 that Hungary was in significant deviation from the adjustment path toward the MTO in 2017. Following up on this, the EU Council in June 2018 issued a recommendation that Hungary implement measures to achieve a structural adjustment of 1% of GDP already in 2018 and gave Hungary a deadline of mid-October 2018 to report on action taken.

Inflation rose to 3.4% by the third quarter of 2018, mainly due to higher energy prices. Core inflation remained stable at around 2.3%, as rising services price inflation was counterbalanced by decelerating processed food price increases.

The Hungarian central bank (MNB) continued to maintain a loose monetary policy stance. While it kept its main policy rates unchanged, it gradually increased the outstanding volume of its Hungarian forint liquidity-providing foreign exchange swaps (until May) and of its monetary policy interest rate swaps. The MNB also continued its mortgage bond purchase program. However, the increase in oil prices led to an upward revision in the MNB's medium-term inflation forecast in June 2018, which (along with heightened exchange rate volatility) prompted the MNB to scale back its easing bias. Finally, at its meeting in September 2018, the monetary council announced that it would start to gradually normalize monetary conditions. To this end, the three-month deposit facility, the monetary interest rate swaps and the mortgage bond purchase program will be phased out by end-2018. In the future, required reserves will be the main policy instrument, and monetary conditions will be adjusted through foreign exchange swaps and the interest rate corridor. At the same time, the MNB decided to introduce a new, liquidity-neutral "Funding for Growth Scheme Fix" to promote long-term lending to SMEs at fixed interest rates in 2019.

Lending grew during the first half of 2018. Lending to the corporate sector continued to be supported by strong investment growth, the loosening of lending conditions by banks and the MNB's Market-based Lending Scheme, which is set to terminate at end-2018, however. Lending to households benefited from ongoing strong wage growth, housing subsidies, the modest loosening of lending standards by banks and the expansion of fixed rate loans. To further promote lending to households at fixed interest rates, the MNB has prescribed tighter debt service-to-income ratios for loans with interest rate fixation periods of less than ten years, effective from October 1, 2018.

Table 7

Main economic indicators: Hungary

	2015	2016	2017	Q1 17	Q2 17	Q3 17	Q4 17	Q1 18	Q2 18
<i>Year-on-year change of the period total in %</i>									
GDP at constant prices	3.4	2.2	4.0	4.3	3.3	3.9	4.4	4.4	4.8
Private consumption	3.6	4.3	4.7	3.5	4.7	5.1	5.6	6.0	5.4
Public consumption	1.1	0.8	0.3	-5.8	-2.2	2.8	6.1	2.6	0.3
Gross fixed capital formation	1.9	-10.6	16.8	21.6	21.0	14.4	13.1	17.1	15.0
Exports of goods and services	8.5	3.4	7.1	10.2	5.4	4.7	8.3	3.5	6.2
Imports of goods and services	6.4	2.9	9.7	12.7	7.6	9.1	9.7	3.8	7.5
<i>Contribution to GDP growth in percentage points</i>									
Domestic demand	1.2	1.5	5.4	5.3	4.5	6.8	4.9	4.4	5.4
Net exports of goods and services	2.2	0.7	-1.4	-1.0	-1.2	-2.8	-0.5	0.0	-0.5
Exports of goods and services	7.5	3.1	6.3	9.6	5.0	4.2	7.0	3.4	5.7
Imports of goods and services	-5.2	-2.4	-7.7	-10.6	-6.2	-7.0	-7.4	-3.4	-6.2
<i>Year-on-year change of the period average in %</i>									
Unit labor costs in the whole economy (nominal, per person)	-2.4	4.4	5.9	6.1	7.8	5.1	4.4	7.8	5.4
Unit labor costs in manufacturing (nominal, per hour)	-0.1	8.5	5.9	4.1	6.3	7.6	5.6	7.9	6.7
Labor productivity in manufacturing (real, per hour)	4.1	-2.7	2.3	3.4	2.9	0.9	2.1	1.5	2.1
Labor costs in manufacturing (nominal, per hour)	4.0	5.6	8.4	7.6	9.4	8.6	7.9	9.5	8.8
Producer price index (PPI) in industry	-1.0	-1.7	3.3	3.5	2.9	2.6	4.3	3.6	5.3
Consumer price index (here: HICP)	0.1	0.4	2.4	2.6	2.1	2.5	2.3	2.0	2.8
EUR per 1 HUF, + = HUF appreciation	-0.4	-0.5	0.7	1.0	1.1	1.5	-0.7	-0.6	-2.3
<i>Period average levels</i>									
Unemployment rate (ILO definition, %, 15–64 years)	6.9	5.2	4.2	4.6	4.3	4.1	3.8	3.9	3.6
Employment rate (%, 15–64 years)	64.0	66.5	68.2	67.1	68.1	68.7	68.8	68.7	69.3
Key interest rate per annum (%)	1.6	1.0	0.9	0.9	0.9	0.9	0.9	0.9	0.9
HUF per 1 EUR	309.9	311.5	309.3	309.1	309.9	306.5	311.7	311.1	317.1
<i>Nominal year-on-year change in the period-end stock in %</i>									
Loans to the domestic nonbank private sector ¹	-12.7	0.0	4.3	0.7	3.7	4.1	4.3	4.6	6.5
of which: loans to households	-15.6	-2.7	1.3	-0.7	0.6	1.6	1.3	-0.1	2.1
loans to nonbank corporations	-10.0	2.3	6.8	1.8	6.3	6.3	6.8	8.4	10.1
<i>%</i>									
Share of foreign currency loans in total loans to the nonbank private sector	24.3	22.4	23.5	22.4	23.0	23.1	23.5	23.5	24.7
Return on assets (banking sector)	-0.1	1.3	1.8	2.1	2.1	1.8	1.8	1.7	1.6
Tier 1 capital ratio (banking sector)	16.9	19.2	21.1	19.3	19.7	19.6	21.1	20.2	19.3
NPL ratio (banking sector)	10.6	6.4	3.7	5.3	4.6	4.1	3.7	3.1	2.8
<i>% of GDP</i>									
General government revenues	48.2	44.9	44.5	..	..	..	..	..	..
General government expenditures	50.1	46.5	46.5	..	..	..	..	..	..
General government balance	-1.9	-1.7	-2.0	..	..	..	..	..	..
Primary balance	1.6	1.6	0.8	..	..	..	..	..	..
Gross public debt	76.7	76.0	73.6	..	..	..	..	..	..
<i>% of GDP</i>									
Debt of nonfinancial corporations (nonconsolidated)	77.0	73.2	66.0	..	..	..	..	..	..
Debt of households and NPISHs ² (nonconsolidated)	20.9	20.4	18.7	..	..	..	..	..	..
<i>% of GDP (based on EUR), period total</i>									
Trade balance	3.7	4.1	1.5	1.6	3.4	0.6	0.7	0.1	1.7
Services balance	4.5	6.0	6.0	5.5	6.1	7.0	5.3	6.2	6.2
Primary income	-4.5	-2.5	-4.0	-4.0	-4.6	-3.7	-3.7	-3.3	-4.9
Secondary income	-0.8	-1.3	-0.3	-0.2	0.4	-0.7	-0.6	-0.2	-0.6
Current account balance	2.8	6.2	3.2	2.9	5.3	3.2	1.6	2.9	2.4
Capital account balance	4.6	0.0	1.0	1.1	1.7	0.4	0.7	3.8	1.3
Foreign direct investment (net) ³	-1.1	-2.0	-1.3	-2.0	2.8	-2.8	-3.1	-0.9	0.0
<i>% of GDP (rolling four-quarter GDP, based on EUR), end of period</i>									
Gross external debt	107.8	97.3	85.0	96.9	94.1	89.3	85.0	82.9	82.4
Gross official reserves (excluding gold)	27.3	21.4	18.8	21.0	19.8	18.3	18.8	18.3	18.7
<i>Months of imports of goods and services</i>									
Gross official reserves (excluding gold)	4.0	3.2	2.8	3.1	2.9	2.7	2.8	2.7	2.8
<i>EUR million, period total</i>									
GDP at current prices	110,706	113,760	123,465	27,217	30,515	31,664	34,069	29,426	32,625

Source: Bloomberg, European Commission, Eurostat, national statistical offices, national central banks, wiw, OeNB.

¹ Foreign currency component at constant exchange rates.² Nonprofit institutions serving households.³ + = net accumulation of assets larger than net accumulation of liabilities (net outflow of capital).

- = net accumulation of assets smaller than net accumulation of liabilities (net inflow of capital).

8 Poland: no adjustment of structural budget deficit amidst strong growth

Persistent, albeit moderate unit labor cost increases

GDP growth in Poland remained at about 5% in the first half of 2018 (after 4.6% in 2017), with quarter-on-quarter growth declining to 1.0% after 1.6% in the first quarter. Total final demand growth was equally strong year on year in both quarters, with weak export growth (in line with German import growth) offset by stronger inventory build-up in the first quarter and both strong foreign and domestic demand growth in the second quarter. Hence, annual real import growth remained nearly unchanged, and the net export contribution turned positive. In the first half of 2018, the current account balance showed a small surplus of 0.5% of GDP, lower than the 0.9% of GDP recorded a year earlier due to the deterioration of the trade balance to –0.5% of GDP from 0.7% of GDP. The capital account surplus increased to 1.2% of GDP from 0.7% of GDP. Net FDI inflows rose to 2.2% of GDP from 0.2% of GDP. Both fixed investment growth and the contribution of inventory build-up slowed in the second quarter, possibly reflecting previously low foreign demand. Factors conducive to business fixed investment like strong demand, high capacity utilization rates, a stable liquidity position and low real lending rates remained in place, but industrial confidence and profitability showed slight signs of deterioration, possibly linked to moderate unit labor cost (ULC) increases. In view of the number of dwellings under construction, housing investment growth again appears to have accelerated moderately, benefiting from income and financing conditions. Private consumption growth was robust at about 4.5%, supported by ongoing real wage and employment growth, stronger real pensions growth and further improvements in consumer confidence.

Headline inflation moderately higher, but core inflation hardly changed

In the first half of 2018, manufacturing ULC in Poland accelerated and outpaced corresponding ULC growth figures recorded in the euro area by 3 percentage points. The Polish złoty's euro value was higher year on year by 2.5 percentage points, eroding price competitiveness further, while helping contain inflation. In August 2018, annual headline inflation stood at 1.4% (HICP) and 2.0% (national CPI), while core inflation stood at 0.6% (HICP excluding energy and unprocessed food) and 0.9% (CPI excluding energy and food). Headline and core figures were higher than in March 2018, by 0.7 and 0.2 percentage points, under both concepts. The Polish Monetary Policy Council (MPC), pursuing an inflation target of 2.5% (CPI), has held the policy rate at 1.5% since March 2015. On October 3, 2018, it assessed that inflation will remain close to target over the monetary policy horizon and that the current interest rate level is conducive to keeping the economy on a sustainable growth path.

Risk of significant deviation from the structural adjustment path

Both the government's Convergence Program and the European Commission staff forecast expect a higher general government revenue-to-GDP ratio (due to new VAT collection measures) and a higher expenditure-to-GDP ratio (due to higher public investment) in 2018 than in 2017. The European Commission forecasts a lower headline deficit of 1.4% of GDP (2017: 1.7% of GDP), but a higher structural deficit of 2.2% of GDP (2017: 2.0% of GDP), implying a structural primary deficit of 0.7% of GDP (2017: 0.5% of GDP) and a persistent deviation from the medium-term objective of a structural deficit of 1% of GDP. Thus, in June 2018, the EU Council saw the risk of a significant deviation from the structural adjustment of 0.5% of GDP in 2018, and it recommended that the Polish government take action to ensure a structural adjustment of 0.6% of GDP in 2019. General government gross debt is forecast by the European Commission to reach 49.6% of GDP at end-2018, after 50.6% of GDP at end-2017.

Table 8

Main economic indicators: Poland

	2015	2016	2017	Q1 17	Q2 17	Q3 17	Q4 17	Q1 18	Q2 18
<i>Year-on-year change of the period total in %</i>									
GDP at constant prices	3.8	3.0	4.6	4.7	4.2	5.4	4.4	5.1	5.0
Private consumption	3.0	3.9	4.7	4.6	4.7	4.7	4.7	4.2	4.7
Public consumption	2.4	1.8	3.4	2.2	3.1	3.4	4.5	3.4	4.1
Gross fixed capital formation	6.1	-8.2	3.4	1.0	1.1	3.5	5.7	8.1	4.5
Exports of goods and services	7.7	8.8	8.2	11.3	4.6	9.3	7.9	1.1	4.2
Imports of goods and services	6.6	7.6	8.7	10.7	7.7	7.0	9.4	3.4	3.6
<i>Contribution to GDP growth in percentage points</i>									
Domestic demand	3.2	2.1	4.6	3.9	5.5	4.0	4.7	6.3	4.5
Net exports of goods and services	0.6	0.8	0.1	0.8	-1.3	1.4	-0.3	-1.2	0.5
Exports of goods and services	3.7	4.4	4.3	6.1	2.5	4.8	3.8	0.6	3.9
Imports of goods and services	-3.0	-3.5	-4.2	-5.4	-3.8	-3.5	-4.1	-1.8	-3.3
<i>Year-on-year change of the period average in %</i>									
Unit labor costs in the whole economy (nominal, per person)	-0.6	2.6	1.3	0.7	1.0	1.1	2.4	2.3	4.5
Unit labor costs in manufacturing (nominal, per hour)	0.7	3.2	3.0	3.4	2.8	2.3	3.5	4.2	4.0
Labor productivity in manufacturing (real, per hour)	3.2	0.6	3.6	1.3	4.4	4.2	4.2	3.9	4.0
Labor costs in manufacturing (nominal, per hour)	3.9	3.8	6.6	4.7	7.3	6.6	7.9	8.2	8.2
Producer price index (PPI) in industry	-2.1	-0.3	2.7	4.1	2.7	2.6	1.6	0.1	2.4
Consumer price index (here: HICP)	-0.7	-0.2	1.6	1.7	1.5	1.5	1.8	1.0	1.1
EUR per 1 PLN, + = PLN appreciation	0.0	-4.1	2.5	1.0	3.7	1.9	3.5	3.4	-1.0
<i>Period average levels</i>									
Unemployment rate (ILO definition, %, 15–64 years)	7.6	6.3	5.0	5.5	5.0	4.8	4.5	4.2	3.6
Employment rate (%, 15–64 years)	62.9	64.5	66.1	65.4	66.2	66.5	66.4	66.6	67.7
Key interest rate per annum (%)	1.6	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5
PLN per 1 EUR	4.2	4.4	4.3	4.3	4.2	4.3	4.2	4.2	4.3
<i>Nominal year-on-year change in the period-end stock in %</i>									
Loans to the domestic nonbank private sector ¹	5.3	3.9	6.2	5.5	6.1	6.1	6.2	5.6	5.5
of which: loans to households	3.9	4.0	4.8	4.2	4.4	4.5	4.8	5.1	5.2
loans to nonbank corporations	7.8	3.8	8.7	7.8	9.3	9.1	8.7	6.3	6.0
<i>%</i>									
Share of foreign currency loans in total loans to the nonbank private sector	26.9	25.8	21.3	24.2	23.2	22.6	21.3	21.2	21.5
Return on assets (banking sector)	0.7	0.8	0.8	0.6	0.8	0.8	0.8	0.8	0.9
Tier 1 capital ratio (banking sector)	15.0	16.1	17.2	16.5	17.0	17.2	17.2	17.0	17.0
NPL ratio (banking sector)	7.5	7.1	6.8	6.9	6.9	6.9	6.8	7.7	7.3
<i>% of GDP</i>									
General government revenues	38.9	38.8	39.6	..	..	..	..	..	..
General government expenditures	41.6	41.1	41.2	..	..	..	..	..	..
General government balance	-2.6	-2.3	-1.7	..	..	..	..	..	..
Primary balance	-0.9	-0.6	0.0	..	..	..	..	..	..
Gross public debt	51.1	54.2	50.6	..	..	..	..	..	..
<i>% of GDP</i>									
Debt of nonfinancial corporations (nonconsolidated)	46.5	49.0	47.1	..	..	..	..	..	..
Debt of households and NPISHs ² (nonconsolidated)	35.4	36.3	35.7	..	..	..	..	..	..
<i>% of GDP (based on EUR), period total</i>									
Trade balance	0.5	0.7	0.3	0.7	0.7	0.5	-0.4	-1.0	0.0
Services balance	2.5	3.3	3.9	3.8	4.1	3.9	3.6	4.5	4.8
Primary income	-3.4	-4.2	-4.0	-2.6	-4.6	-4.3	-4.3	-2.8	-4.1
Secondary income	-0.2	-0.3	0.0	0.0	-0.3	-0.1	0.2	-0.2	-0.1
Current account balance	-0.6	-0.5	0.2	1.9	-0.1	0.0	-1.0	0.5	0.5
Capital account balance	2.4	1.1	1.3	0.6	0.8	0.9	2.5	1.2	1.3
Foreign direct investment (net) ³	-2.1	-0.9	-1.2	-2.4	1.8	-2.1	-2.0	-2.8	-1.6
<i>% of GDP (rolling four-quarter GDP, based on EUR), end of period</i>									
Gross external debt	70.5	75.4	68.4	74.8	72.6	69.4	68.4	67.2	64.7
Gross official reserves (excluding gold)	19.5	24.5	19.5	23.3	21.3	20.0	19.5	19.6	18.7
<i>Months of imports of goods and services</i>									
Gross official reserves (excluding gold)	5.0	6.1	4.7	5.7	5.1	4.8	4.7	4.7	4.4
<i>EUR million, period total</i>									
GDP at current prices	429,921	425,880	465,897	105,698	113,072	115,122	132,004	116,136	118,028

Source: Bloomberg, European Commission, Eurostat, national statistical offices, national central banks, wiw, OeNB.

¹ Foreign currency component at constant exchange rates.² Nonprofit institutions serving households.³ + = net accumulation of assets larger than net accumulation of liabilities (net outflow of capital).

- = net accumulation of assets smaller than net accumulation of liabilities (net inflow of capital).

9 Romania: heightened fiscal policy concerns

Strong inventory
buildup boosted
GDP growth

Economic activity decelerated noticeably in the first half of 2018 with year-on-year GDP growth slipping to 4%. Changes in inventories delivered a remarkably large growth contribution of 2.9 percentage points and became almost as important as private consumption. In early 2018, private consumption growth was negatively affected by uncertainties about how changes in the tax system would affect net wages. Yet annual net real wage growth still posted a robust increase of 8.4% in July amid tightening labor market conditions, while consumer confidence recovered somewhat over the summer. Meanwhile, consumer lending picked up and provided some support. The investment recovery that had started in mid-2017 came to a halt with gross fixed capital formation shrinking in the second quarter. The absorption of EU funds has remained low, while residential construction weakened. Despite the slowdown in domestic demand, the negative contribution from net exports remained close to the figures seen in the second half of 2017. Import growth did not start to fall until the second quarter of 2018, when export growth dipped as well.

Fiscal policy not in
line with EU policy
framework

In its spring forecast, the European Commission expected Romania's general government deficit to reach 3.4% of GDP in 2018 and 3.8% of GDP in 2019. It also projected that the structural deficit will widen by 0.4% of GDP in 2018 and by a further 0.4% in 2019 from an already elevated 3.3% of GDP in 2017. In June 2018 the EU Council recommended that, under the significant deviation procedure, Romania implement measures to achieve a structural adjustment of 0.8% of GDP in 2018 and 2019 and asked Romania to report on action taken by mid-October 2018. In deriving its recommendation, the EU Council took note of Romania's failure to act upon earlier recommendations to correct its significant deviation from the adjustment path toward the medium-term budgetary objective and the risk of exceeding the 3% of GDP reference value.

Current account
deficit remained
unchanged, while
foreign reserves
declined

In the first half of 2018, Romania's current account deficit as a percentage of GDP stood at the same level (4.2%) as in the first half of 2017. The deficit in the goods and services balance increased by about 1 percentage point, but this deterioration was counterbalanced by a declining deficit in the primary income balance. The surplus in the capital account balance was only slightly higher than in the first half of 2017, reflecting the still weak absorption of EU funds. Net FDI inflows remained below the net borrowing position from current and capital accounts. It is noteworthy that official foreign exchange reserves declined markedly in the second quarter of 2018, while both portfolio and other investments recorded net outflows. The decline of official foreign exchange reserves was partly related to repayments of public external debt. Yet market observers also pointed to possible foreign currency sales by the central bank to support the Romanian leu.

Inflation peaked
toward the end of
the second quarter
of 2018

Romanian CPI and HICP inflation rates continued to rise in the first half of 2018. The CPI inflation rate, on which Romania's inflation target is based, peaked at 5.4% year on year in May and June, before coming down somewhat to 4.6% in July and 5% in August. Core inflation rose to 3.1% in April before steadily declining to 2.8% in August. The Romanian central bank decided to raise its key policy rate by 25 basis points to 2.5% in May and has left it unchanged since then. It currently projects inflation to decline to the upper bound of its target band of 2.5% \pm 1 percentage point by the end of 2018 and to decline further in 2019. Monetary conditions have become tighter than the key policy rate suggests, with the three-month money market rate moving up to 3.5% in mid-summer before receding slightly to 3% at end-September.

Table 9

Main economic indicators: Romania

	2015	2016	2017	Q1 17	Q2 17	Q3 17	Q4 17	Q1 18	Q2 18
<i>Year-on-year change of the period total in %</i>									
GDP at constant prices	3.9	4.8	7.0	5.7	6.1	8.8	6.7	4.0	4.1
Private consumption	5.9	7.9	10.2	7.3	7.3	13.5	11.7	5.8	5.1
Public consumption	-0.4	3.8	0.2	3.8	-0.3	8.8	-6.9	-3.4	-1.0
Gross fixed capital formation	7.2	-1.9	4.5	-0.9	-0.4	6.2	10.1	6.3	-3.0
Exports of goods and services	4.9	8.3	9.1	10.6	8.7	8.7	8.3	8.1	5.3
Imports of goods and services	8.1	10.0	10.7	10.3	10.1	11.0	11.4	11.4	7.9
<i>Contribution to GDP growth in percentage points</i>									
Domestic demand	5.3	5.3	7.7	2.7	7.9	8.8	9.7	6.7	4.2
Net exports of goods and services	-1.4	-0.5	-0.7	1.1	-0.2	-1.4	-1.8	-1.9	-1.5
Exports of goods and services	1.9	3.6	4.0	5.8	3.9	3.6	3.3	3.8	1.9
Imports of goods and services	-3.3	-4.1	-4.7	-4.7	-4.1	-4.9	-5.1	-5.7	-3.5
<i>Year-on-year change of the period average in %</i>									
Unit labor costs in the whole economy (nominal, per person)	-3.0	6.3	9.3	7.8	12.0	6.3	10.7	15.6	11.0
Unit labor costs in manufacturing (nominal, per hour)	6.6	8.4	5.6	8.6	6.9	5.2	2.0	5.6	2.5
Labor productivity in manufacturing (real, per hour)	-0.1	1.2	8.3	6.2	8.7	7.8	10.4	5.3	7.8
Labor costs in manufacturing (nominal, per hour)	6.5	9.7	14.3	15.3	16.2	13.4	12.5	11.2	10.5
Producer price index (PPI) in industry	-2.2	-1.8	3.5	3.5	3.0	3.6	3.7	3.9	5.2
Consumer price index (here: HICP)	-0.4	-1.1	1.1	0.4	0.6	1.0	2.4	3.7	4.5
EUR per 1 RON, + = RON appreciation	0.0	-1.0	-1.7	-0.6	-1.2	-2.6	-2.4	-2.9	-2.2
<i>Period average levels</i>									
Unemployment rate (ILO definition, %, 15–64 years)	7.1	6.1	5.1	5.6	5.0	4.9	4.9	4.8	4.3
Employment rate (%, 15–64 years)	61.4	61.6	63.9	61.2	65.5	65.3	63.4	63.1	65.5
Key interest rate per annum (%)	1.9	1.8	1.8	1.8	1.8	1.8	1.8	2.1	2.4
RON per 1 EUR	4.4	4.5	4.6	4.5	4.6	4.6	4.6	4.7	4.7
<i>Nominal year-on-year change in the period-end stock in %</i>									
Loans to the domestic nonbank private sector ¹	1.8	1.0	4.8	2.3	4.0	5.9	4.8	5.3	6.1
of which: loans to households	4.1	4.5	7.1	4.8	5.3	6.5	7.1	8.8	9.3
loans to nonbank corporations	-0.3	-2.4	2.3	-0.3	2.6	5.4	2.3	1.7	2.7
<i>%</i>									
Share of foreign currency loans in total loans to the nonbank private sector	49.3	42.8	37.2	41.8	39.8	38.6	37.2	36.8	35.0
Return on assets (banking sector)	1.2	1.1	1.3	1.3	1.4	1.4	1.3	1.6	1.7
Tier 1 capital ratio (banking sector)	16.7	17.6	18.0	17.7	17.8	17.2	18.0	17.9	17.6
NPL ratio (banking sector)	13.5	9.6	6.4	9.4	8.3	8.0	6.4	6.2	5.7
<i>% of GDP</i>									
General government revenues	35.0	31.6	30.5	..	..	..	..	..	..
General government expenditures	35.8	34.6	33.4	..	..	..	..	..	..
General government balance	-0.8	-3.0	-2.9	..	..	..	..	..	..
Primary balance	0.8	-1.5	-1.6	..	..	..	..	..	..
Gross public debt	37.7	37.4	35.0	..	..	..	..	..	..
<i>% of GDP</i>									
Debt of nonfinancial corporations (nonconsolidated)	43.0	39.7	35.9	..	..	..	..	..	..
Debt of households and NPISHs ² (nonconsolidated)	17.2	16.5	15.8	..	..	..	..	..	..
<i>% of GDP (based on EUR), period total</i>									
Trade balance	-4.9	-5.4	-6.3	-5.9	-7.0	-5.7	-6.8	-6.7	-7.0
Services balance	4.2	4.5	4.2	5.2	4.6	4.1	3.4	4.7	4.1
Primary income	-2.4	-2.6	-2.6	-2.2	-5.9	-2.6	-0.5	-1.6	-4.0
Secondary income	1.7	1.5	1.4	0.7	1.9	1.5	1.4	0.8	1.3
Current account balance	-1.2	-2.1	-3.4	-2.1	-6.3	-2.6	-2.5	-2.9	-5.6
Capital account balance	2.4	2.5	1.2	0.6	0.7	0.6	2.4	0.7	1.0
Foreign direct investment (net) ³	-1.8	-2.6	-2.4	-3.1	-1.3	-4.0	-1.4	-3.9	-0.8
<i>% of GDP (rolling four-quarter GDP, based on EUR), end of period</i>									
Gross external debt	57.5	54.4	49.7	53.6	52.1	50.1	49.7	50.4	49.2
Gross official reserves (excluding gold)	20.1	20.1	17.8	19.9	19.8	18.2	17.8	18.3	16.4
<i>Months of imports of goods and services</i>									
Gross official reserves (excluding gold)	5.8	5.7	4.9	5.6	5.5	5.1	4.9	5.0	4.4
<i>EUR million, period total</i>									
GDP at current prices	160,312	170,881	187,703	36,293	43,380	51,894	56,136	38,775	47,013

Source: Bloomberg, European Commission, Eurostat, national statistical offices, national central banks, wiiw, OeNB.

¹ Foreign currency component at constant exchange rates.² Nonprofit institutions serving households.³ + = net accumulation of assets larger than net accumulation of liabilities (net outflow of capital).

- = net accumulation of assets smaller than net accumulation of liabilities (net inflow of capital).

10 Turkey: currency crisis, economic downturn and uncertain outlook

Recent financial
market turmoil and
policy actions

Turkey's financial and economic situation has deteriorated throughout 2018, culminating in severe financial market turbulence in early August. CPI inflation has accelerated sharply, reaching 24.5% in September 2018, compared to 11.9% at the end of 2017. The sharp acceleration was triggered by a combination of the Turkish lira's depreciation (by 39% to TRY 6.2 against the U.S. dollar from the start of the year until the end of September), still considerable demand pressures and the pass-through of strong producer price inflation (46.2% in September 2018). The melt-down was likely triggered by various factors: economic imbalances have been building up in recent years, including debt build-up in the corporate sector and an increasing current account deficit financed largely by portfolio and other investment flows. Moreover, international relations with the U.S.A. deteriorated and investors became increasingly worried about President Erdogan's influence on various Turkish institutions, particularly the central bank. Policy actions by the Turkish central bank (CBRT) did not keep pace with the Turkish lira's sharp depreciation and accelerating inflation. Between April and June 2018, the CBRT raised its policy rate by a total of 500 basis points and simplified its monetary policy framework in May. In reaction to the turbulence in August, Turkish authorities initially focused on liquidity and regulatory measures targeted at banks. In mid-September, more than one month after the start of the financial market turmoil, the CBRT raised its policy rate from 17.75% to 24%, and the government announced an economic reform program that aims to bring down inflation and promises fiscal restraint.

Economic slowdown
has started and is
expected to
accelerate

GDP grew by 6.2% in the first half of 2018, decelerating from its peak in the third quarter of 2017 (11.5%). The slowdown in growth was visible across all growth components. Private consumption growth decelerated from 9.3% in the first quarter to 6.3% in the second quarter. Investment growth decelerated from 7.9% to 3.9%.

The fiscal stance continued to be expansionary in the first half of the year, and gross public debt increased to 29.2% of GDP. The recent mid-term economic program envisages fiscal restraint, and the government plans to keep annual general budget deficits below 2% of GDP until 2021. This fading fiscal support – paired with the effects of the depreciating lira, rising borrowing costs and elevated inflation – is expected to cause economic growth to decelerate swiftly over the coming quarters.

External imbalances
are a key source of
risk for Turkey

Net exports contributed negatively to economic growth in the first half of 2018. Export growth was slow in the first half of the year, reaching 2.6% year on year. Import growth was still as high as 7.8% but has been slowing down rapidly. Imports shrank in June, July and August in annual terms. In mid-2018, Turkey's current account deficit stood at 7.7% of GDP (compared to 5.5% a year earlier).

Net FDI inflows amounted to only 0.7% of GDP in the first half of 2018. Net portfolio inflows hovered around 0% of GDP, thus being much lower than the 4.5% registered in the same period of 2017. The shortfall was partly offset by net other investment inflows of 2.9% of GDP. Gross international reserves declined from EUR 90 billion at end-2017 to EUR 84 billion in June 2018, net of banking sector minimum reserve requirements, reserves amounted to only EUR 50 billion (equivalent to roughly two months of imports). Gross external debt increased further to 53.6% of GDP at mid-2018, of which 80% can be attributed to the banking and nonfinancial corporate sector.

Table 10

Main economic indicators: Turkey

	2015	2016	2017	Q1 17	Q2 17	Q3 17	Q4 17	Q1 18	Q2 18
<i>Year-on-year change of the period total in %</i>									
GDP at constant prices	6.1	3.2	7.4	5.3	5.3	11.5	7.3	7.3	5.2
Private consumption	5.4	3.7	6.1	4.5	3.1	10.3	6.3	9.3	6.3
Public consumption	3.9	9.5	5.0	9.0	-1.8	7.6	5.9	4.9	7.2
Gross fixed capital formation	9.3	2.2	7.8	3.9	7.7	12.8	6.6	7.9	3.9
Exports of goods and services	4.3	-1.9	11.9	10.0	11.0	17.7	9.2	0.7	4.5
Imports of goods and services	1.7	3.7	10.3	0.9	2.2	15.0	22.8	15.4	0.3
<i>Contribution to GDP growth in percentage points</i>									
Domestic demand	6.5	4.1	6.7	5.2	3.9	10.7	6.7	8.7	6.0
Net exports of goods and services	0.5	-1.3	0.1	2.0	1.7	0.3	-3.2	-3.4	0.9
Exports of goods and services	0.9	-0.4	2.5	2.2	2.3	3.5	1.8	0.2	1.0
Imports of goods and services	-0.4	-0.9	-2.4	-0.2	-0.5	-3.2	-5.0	-3.6	-0.1
<i>Year-on-year change of the period average in %</i>									
Unit labor costs in the whole economy (nominal, per person)	..	..	..	..	..	..	..	..	..
Unit labor costs in manufacturing (nominal, per hour)	11.6	15.8	4.0	5.5	5.9	0.8	4.0	11.5	14.7
Labor productivity in manufacturing (real, per hour)	4.9	4.5	6.2	4.8	5.2	8.1	6.6	6.1	3.3
Labor costs in manufacturing (nominal, per hour)	16.8	21.0	10.4	10.5	11.5	8.9	10.9	18.2	18.5
Producer price index (PPI) in industry	5.3	4.3	15.8	15.0	15.5	16.0	16.7	13.4	20.1
Consumer price index (here: HICP)	7.7	7.7	11.1	10.0	11.6	10.6	12.2	10.3	12.8
EUR per 1 TRY, + = TRY appreciation	-3.8	-9.6	-18.9	-17.5	-17.0	-19.8	-20.9	-16.1	-24.5
<i>Period average levels</i>									
Unemployment rate (ILO definition, %, 15–64 years)	10.5	11.1	11.1	12.9	10.3	10.7	10.4	10.8	9.8
Employment rate (%, 15–64 years)	50.2	50.7	51.6	49.5	52.2	52.6	51.9	51.1	52.7
Key interest rate per annum (%)	7.6	7.5	8.0	8.0	8.0	8.0	8.0	8.0	11.2
TRY per 1 EUR	3.0	3.3	4.1	3.9	3.9	4.1	4.5	4.7	5.2
<i>Nominal year-on-year change in the period-end stock in %</i>									
Loans to the domestic nonbank private sector	19.4	15.8	20.8	20.3	21.5	23.2	20.8	19.3	21.3
of which: loans to households	8.5	9.6	16.3	12.3	13.4	17.6	16.3	14.8	14.1
loans to nonbank corporations	24.2	18.2	22.3	23.3	24.6	25.3	22.3	20.8	23.8
<i>%</i>									
Share of foreign currency loans in total loans to the nonbank private sector	33.6	35.8	32.9	34.6	32.8	32.4	32.9	33.4	35.1
Return on assets (banking sector)	1.2	1.5	1.6	1.9	1.8	1.7	1.6	1.7	1.7
Tier 1 capital ratio (banking sector)	12.7	12.7	13.6	13.1	13.7	13.9	13.6	13.5	13.1
NPL ratio (banking sector)	3.1	3.4	3.1	3.3	3.2	3.2	3.1	3.0	3.2
<i>% of GDP</i>									
General government revenues	32.4	..	..	..	..	..	..	..	..
General government expenditures	31.1	..	..	..	..	..	..	..	..
General government balance	1.3	-1.3	-2.0	..	..	..	..	..	..
Primary balance	3.3	1.1	0.5	..	..	..	..	..	..
Gross public debt	27.5	28.5	28.5	..	..	..	..	..	..
<i>% of GDP</i>									
Debt of nonfinancial corporations (nonconsolidated)	..	..	..	..	..	..	..	..	..
Debt of households and NPISHs ¹ (nonconsolidated)	..	..	..	..	..	..	..	..	..
<i>% of GDP (based on EUR), period total</i>									
Trade balance	-5.6	-4.7	-6.9	-4.8	-6.9	-7.8	-7.7	-8.3	-8.1
Services balance	2.8	1.8	2.3	1.0	1.9	4.2	1.9	1.4	2.6
Primary income	-1.1	-1.1	-1.3	-1.2	-1.6	-1.0	-1.4	-1.1	-1.8
Secondary income	0.2	0.2	0.3	0.3	0.3	0.3	0.4	0.1	0.0
Current account balance	-3.7	-3.8	-5.6	-4.8	-6.3	-4.3	-6.9	-8.0	-7.4
Capital account balance	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Foreign direct investment (net) ²	-1.5	-1.2	-1.0	-1.2	-0.6	-1.1	-1.0	-0.5	-0.9
<i>% of GDP (rolling four-quarter GDP, based on EUR), end of period</i>									
Gross external debt	48.9	50.6	51.5	51.4	51.6	50.8	51.5	51.2	53.6
Gross official reserves (excluding gold)	11.1	11.2	9.3	10.8	10.4	10.1	9.3	9.1	8.8
<i>Months of imports of goods and services</i>									
Gross official reserves (excluding gold)	5.1	5.4	3.8	5.0	4.7	4.4	3.8	3.7	3.5
<i>EUR million, period total</i>									
GDP at current prices	771,913	778,812	751,693	164,918	186,454	201,532	198,788	167,977	169,374

Source: Bloomberg, European Commission, Eurostat, national statistical offices, national central banks, wiw, OeNB.

¹ Nonprofit institutions serving households.² + = net accumulation of assets larger than net accumulation of liabilities (net outflow of capital).

- = net accumulation of assets smaller than net accumulation of liabilities (net inflow of capital).

11 Russia: coping with fresh waves of U.S. sanctions and benefiting from oil price rises

Modest economic recovery picks up slightly, driven by domestic demand

Russia's modest economic recovery picked up speed slightly during the first half of 2018. GDP growth (year on year) accelerated from the first to the second quarter, resulting in a 1.7% expansion in the first half of 2018. Economic activity continued to be driven by domestic demand as private consumption posted a 2.7% gain in the first half of 2018 (year on year) and fixed investment grew by 1.4%. The growth contribution of net exports turned positive in the second quarter of 2018 as import expansion was dampened by the relatively weak Russian ruble and by the authorities' import substitution policies. On the production side of GDP, manufacturing led the recovery, followed by retail sales. The unemployment rate (ILO definition, seasonally adjusted) declined to 4.8% in the second quarter, a post-Soviet record low.

New U.S. sanctions hit Russian ruble, but CBR's prudent stance contributes to low inflation

Notwithstanding a substantial rise in the price of Urals grade crude (by an average of 39% on the year during the first eight months of 2018), the Russian ruble's external value did not strengthen like it usually does in periods of oil price rises, but instead weakened (by 3% against the U.S. dollar and 11% against the euro). This was due to economic uncertainty triggered by the imposition of fresh U.S. sanctions in April 2018, which were directed against a number of Russian businessmen and companies; extraterritorial measures also allow for the punishment of non-U.S. firms doing business with Russia. Further trade-related punitive measures were adopted by the U.S.A. in August, and additional sanctions may follow in late 2018. A second reason for the Russian ruble's weakness was the finance ministry's foreign exchange purchase program carried out by the Russian central bank (CBR) in order to bolster the country's international reserve position. This program was temporarily halted in August. Despite the weak Russian ruble, inflation remained low, yet ticked up slightly from July (2.6%) to August (3.1%), compared to the annual target of 4%. The moderate level of inflation is attributable to continued restrained domestic demand and the CBR's prudent monetary policy. In reaction to the volatility of the exchange rate, the CBR raised its key interest rate slightly to 7.5% in mid-September.

Higher oil prices, the weak Russian ruble and conservative macroeconomic policies contribute to the re-emergence of twin surpluses

Swelling revenues from the further growth of oil prices combined with sustained restraint in spending pushed the federal budget surplus in the first eight months of 2018 to 3.1% of GDP (compared to a deficit of 0.6% of GDP for the same period in 2017). The fiscal rule providing for the transfer of "excess" oil revenues to the National Wealth Fund if the Urals oil price exceeds the threshold level of USD 40 per barrel led to the replenishment of this fund, which recovered to 5.2% of GDP in mid-2018. The oil price-triggered expansion of exports (valued in U.S. dollars) coupled with the weakening of the Russian ruble were the main factors driving up Russia's current account surplus, which increased to 6.3% of GDP in the first half of 2018.

Despite still elevated NPL ratio, bank lending regains some momentum

Net private capital outflows more than doubled to 2.5% of GDP during the same period. These outflows were mostly connected to enterprises building up foreign assets and banks paying down their debts. The country's total external debt declined further to 30.8%, largely on account of firms reducing their financial obligations. International reserves amounted to 23.7% of GDP in mid-2018. Notwithstanding the country's ongoing modest economic growth and high NPL ratio (19.2% in mid-2018), lending started to regain momentum; however, this revival is partly driven by unsecured consumer credit and thus gives rise to concern.

Table 11

Main economic indicators: Russia

	2015	2016	2017	Q1 17	Q2 17	Q3 17	Q4 17	Q1 18	Q2 18
<i>Year-on-year change of the period total in %</i>									
GDP at constant prices	-2.8	-1.0	1.5	0.6	2.5	2.2	0.9	1.3	1.9
Private consumption	-9.7	-3.7	3.3	1.7	3.0	4.2	4.3	2.8	2.6
Public consumption	-3.1	-0.7	0.4	0.3	0.4	0.4	0.4	0.5	0.6
Gross fixed capital formation	-9.9	2.3	4.3	3.1	7.0	4.0	3.4	1.8	1.0
Exports of goods and services	3.7	5.2	5.1	7.2	3.3	4.7	5.2	6.8	7.3
Imports of goods and services	-25.8	-1.0	17.4	15.0	22.0	17.1	15.4	9.6	2.8
<i>Contribution to GDP growth in percentage points</i>									
Domestic demand	-9.5	-1.6	3.5	1.2	5.9	4.5	2.4	1.5	0.5
Net exports of goods and services	7.8	1.5	-2.3	-0.9	-3.6	-2.5	-1.9	-0.2	1.3
Exports of goods and services	0.8	1.3	1.3	1.9	0.9	1.1	1.3	1.9	2.0
Imports of goods and services	6.9	0.2	-3.6	-2.8	-4.5	-3.7	-3.2	-2.1	-0.7
<i>Year-on-year change of the period average in %</i>									
Unit labor costs in the whole economy (nominal, per person)	..	..	..	..	..	..	..	..	..
Unit labor costs in manufacturing (nominal, per hour)	6.8	4.3	17.7	18.4	19.1	14.4	18.9	2.6	0.9
Labor productivity in manufacturing (real, per hour)	1.2	4.7	7.5	6.9	9.7	7.9	6.0	5.1	4.5
Labor costs in manufacturing (nominal, per hour)	8.0	9.1	26.7	26.5	30.7	23.4	26.3	7.9	5.4
Producer price index (PPI) in industry	13.5	4.3	7.8	13.1	5.5	4.5	8.0	5.0	12.0
Consumer price index (here: CPI)	15.6	7.1	3.6	4.5	4.0	3.3	2.6	2.3	2.5
EUR per 1 RUB, + = RUB appreciation	-25.0	-8.4	12.6	31.9	18.1	4.1	-1.2	-10.6	-14.9
<i>Period average levels</i>									
Unemployment rate (ILO definition, %, 15–64 years)	5.6	5.5	5.2	5.5	5.2	5.0	5.1	5.1	4.8
Employment rate (%, 15–64 years)	..	..	..	..	..	..	..	..	..
Key interest rate per annum (%)	12.6	10.6	9.1	10.0	9.4	8.9	8.2	7.6	7.3
RUB per 1 EUR	68.0	74.2	65.9	62.5	62.9	69.3	68.8	69.9	74.0
<i>Nominal year-on-year change in the period-end stock in %</i>									
Loans to the domestic nonbank private sector ¹	2.9	0.6	5.7	2.0	2.4	4.2	5.7	7.3	9.4
of which: loans to households	-6.1	1.6	12.7	3.4	5.9	8.8	12.7	15.5	18.8
loans to nonbank corporations	6.7	0.2	3.1	1.5	1.1	2.5	3.1	4.3	5.8
<i>%</i>									
Share of foreign currency loans in total loans to the nonbank private sector	24.5	18.9	14.7	17.7	18.2	16.5	14.7	14.5	14.7
Return on assets (banking sector)	0.2	1.2	1.0	1.7	1.9	1.1	1.0	1.7	1.5
Tier 1 capital ratio (banking sector)	8.5	9.2	8.5	9.9	9.4	8.6	8.5	9.9	9.0
NPL ratio (banking sector)	16.7	18.9	19.1	18.8	18.9	18.8	19.1	19.4	19.2
<i>% of GDP</i>									
General government revenues	32.3	32.7	33.7	..	..	..	..	..	..
General government expenditures	35.7	36.4	35.2	..	..	..	..	..	..
General government balance	-3.4	-3.6	-1.5	..	..	..	..	..	..
Primary balance	..	..	..	..	..	..	..	..	..
Gross public debt	13.1	12.9	13.0	..	..	..	..	..	..
<i>% of GDP</i>									
Debt of nonfinancial corporations (nonconsolidated)	..	..	..	..	..	..	..	..	..
Debt of households and NPISHs ² (nonconsolidated)	..	..	..	..	..	..	..	..	..
<i>% of GDP (based on EUR), period total</i>									
Trade balance	10.8	7.0	7.3	9.9	6.5	5.1	7.9	11.3	11.4
Services balance	-2.7	-1.9	-2.0	-1.5	-2.0	-2.4	-2.0	-1.7	-1.9
Primary income	-2.8	-2.7	-2.5	-1.5	-3.6	-2.7	-2.1	-1.2	-4.3
Secondary income	-0.4	-0.5	-0.6	-0.5	-0.4	-0.7	-0.6	-0.7	-0.4
Current account balance	4.9	1.9	2.3	6.4	0.6	-0.7	3.1	7.8	4.8
Capital account balance	0.0	-0.1	0.0	0.0	0.0	0.0	0.0	-0.1	-0.1
Foreign direct investment (net) ³	1.1	-0.8	0.7	1.0	-1.3	0.4	2.5	1.5	0.6
<i>% of GDP (rolling four-quarter GDP, based on EUR), end of period</i>									
Gross external debt	38.7	41.5	31.2	38.5	34.5	32.8	31.2	30.7	30.8
Gross official reserves (excluding gold)	23.8	25.7	21.3	24.3	22.4	21.6	21.3	22.1	23.7
<i>Months of imports of goods and services</i>									
Gross official reserves (excluding gold)	13.9	15.0	12.4	14.6	13.3	12.7	12.4	12.7	13.4
<i>EUR million, period total</i>									
GDP at current prices	1,232,463	1,173,009	1,395,089	328,692	350,042	345,815	370,540	317,949	335,701

Source: Bloomberg, European Commission, Eurostat, national statistical offices, national central banks, wiw, OeNB.

¹ Foreign currency component at constant exchange rates.² Nonprofit institutions serving households.³ + = net accumulation of assets larger than net accumulation of liabilities (net outflow of capital).

- = net accumulation of assets smaller than net accumulation of liabilities (net inflow of capital).