



OESTERREICHISCHE NATIONALBANK

EUROSYSTEM

Central, Eastern and Southeastern Europe Economic Perspectives

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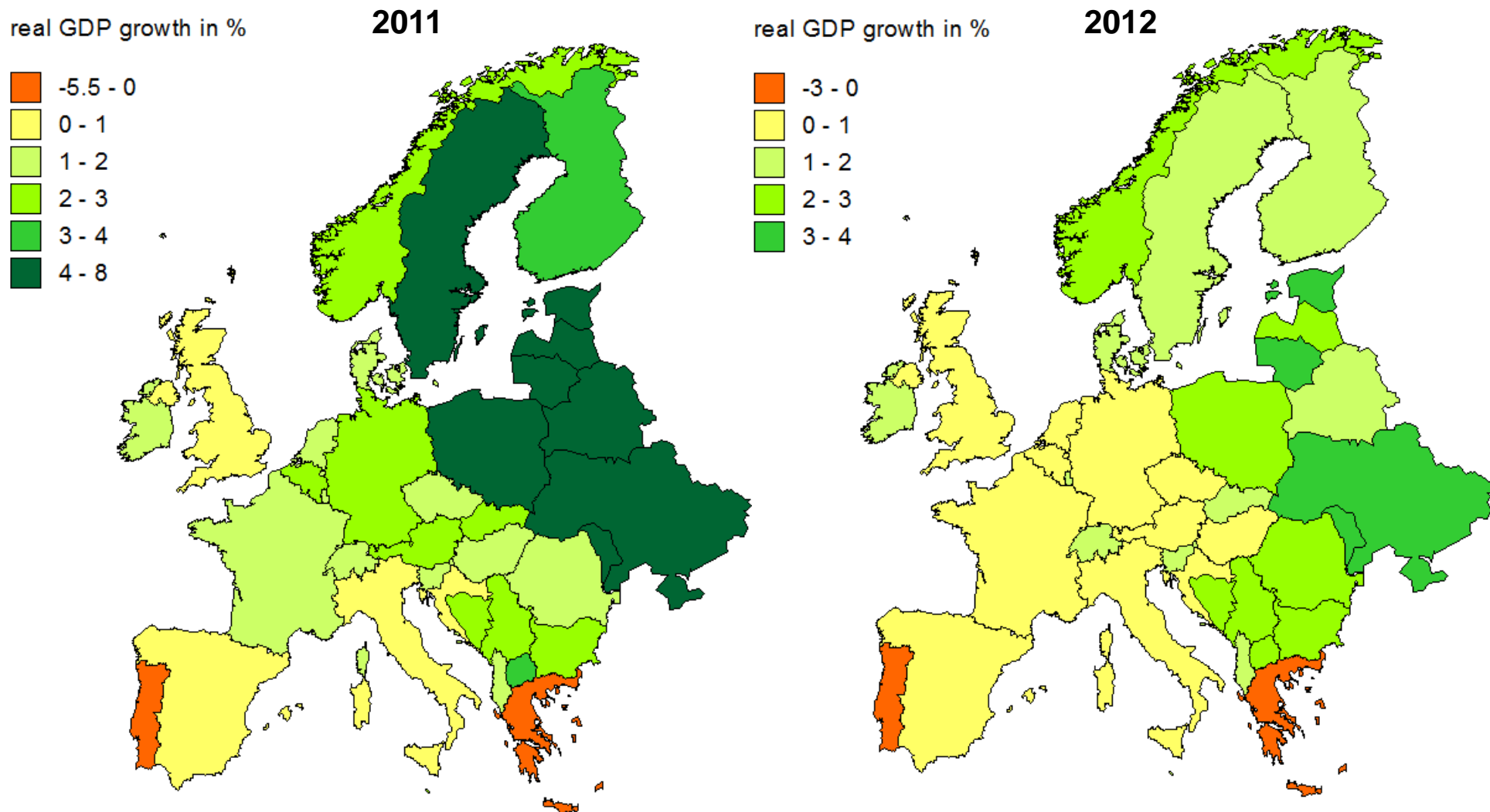
The Central and Eastern European Forum
Euromoney Conference

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Overview

- **Growth prospects for Central, Eastern and Southeastern Europe (CESEE)**
- **Short-term risks to the outlook:**
 - **Additional pro-cyclical fiscal tightening**
 - **Bottlenecks in credit supply**
- **Longer-term macrofinancial challenges in CESEE**
- **Strengthening Austrian banks' business models in the region**

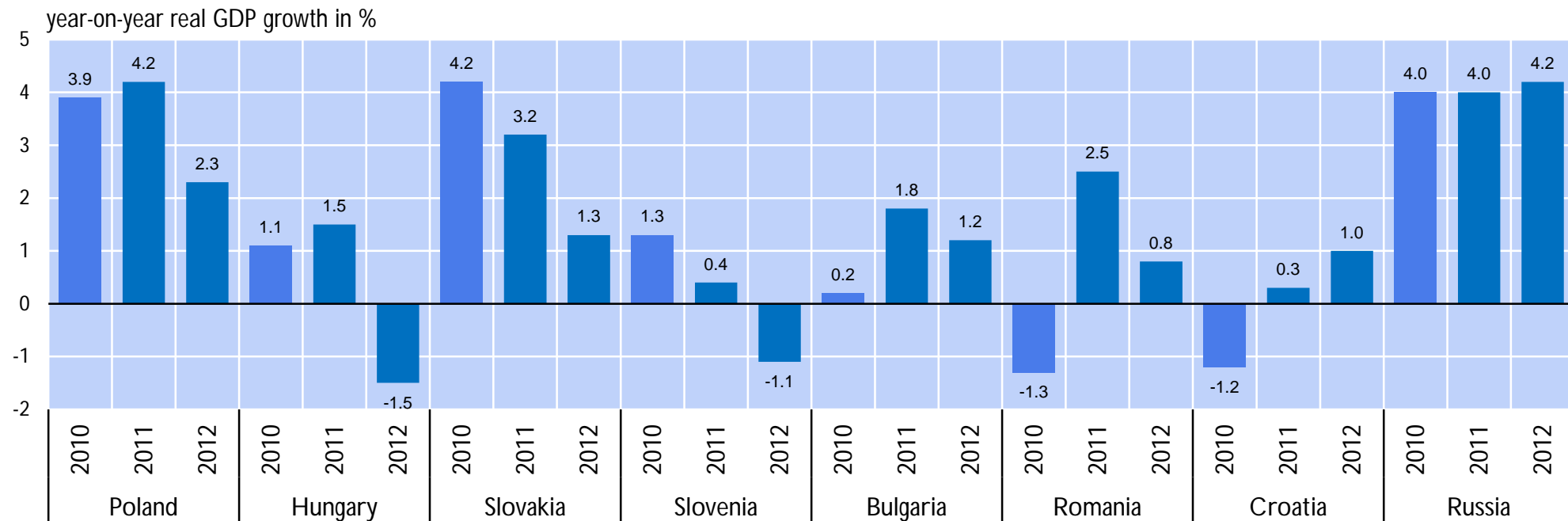
CESEE: Strong Dependence on Euro Area Developments



Sources: European Commission, EBRD.

EBRD CESEE Forecast – Growth Moderates Mainly Due to Worsening External Demand

EBRD CESEE GDP Projections 2011-2012

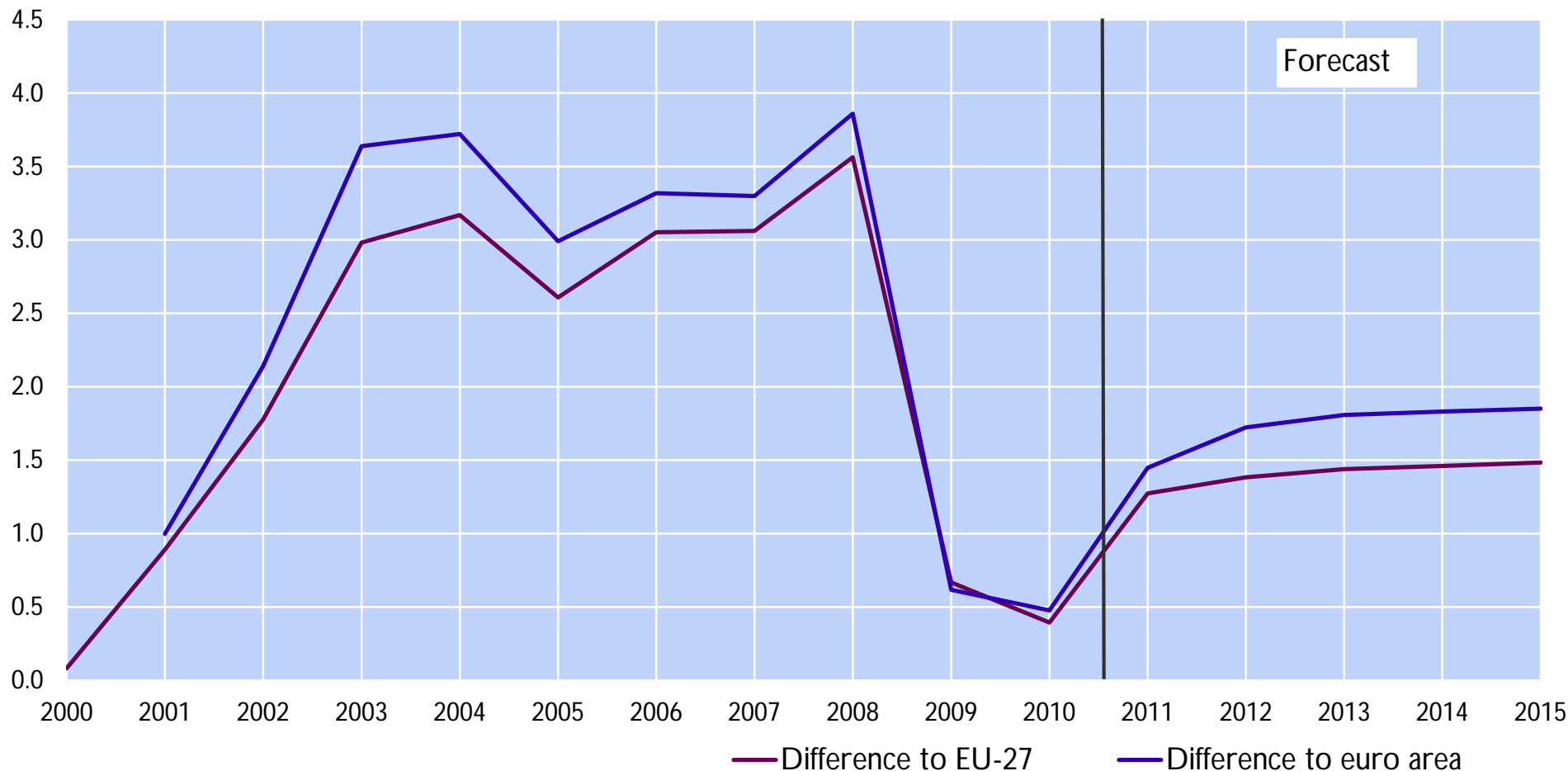


Source: EBRD, January 2012.

- **Regional slowdown in central and southeastern Europe largely due to exposure to euro area.**
- **Russia (and other CIS countries), much less integrated in Western Europe, continue to grow dynamically assuming commodity prices remain high.**

Growth Differential of CESEE EU Member States vis-à-vis the EU-27 and the Euro Area

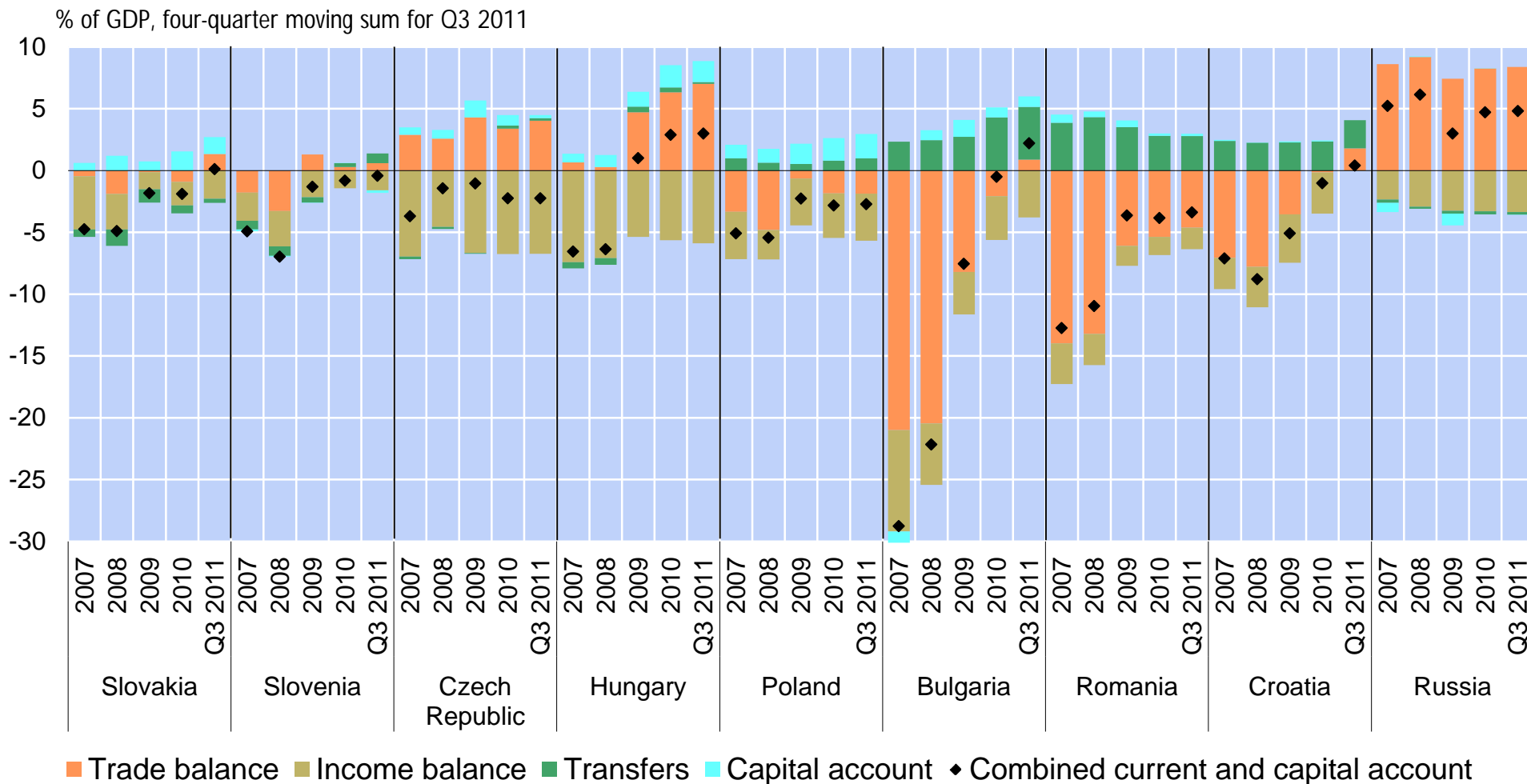
percentage points



Note: Based on the IMF's World Economic Outlook of fall 2011. Slovakia and Slovenia are included in the CESEE EU-member states aggregate.

Sources: OeNB, IMF.

External Re-Balancing Needs to Be Completed

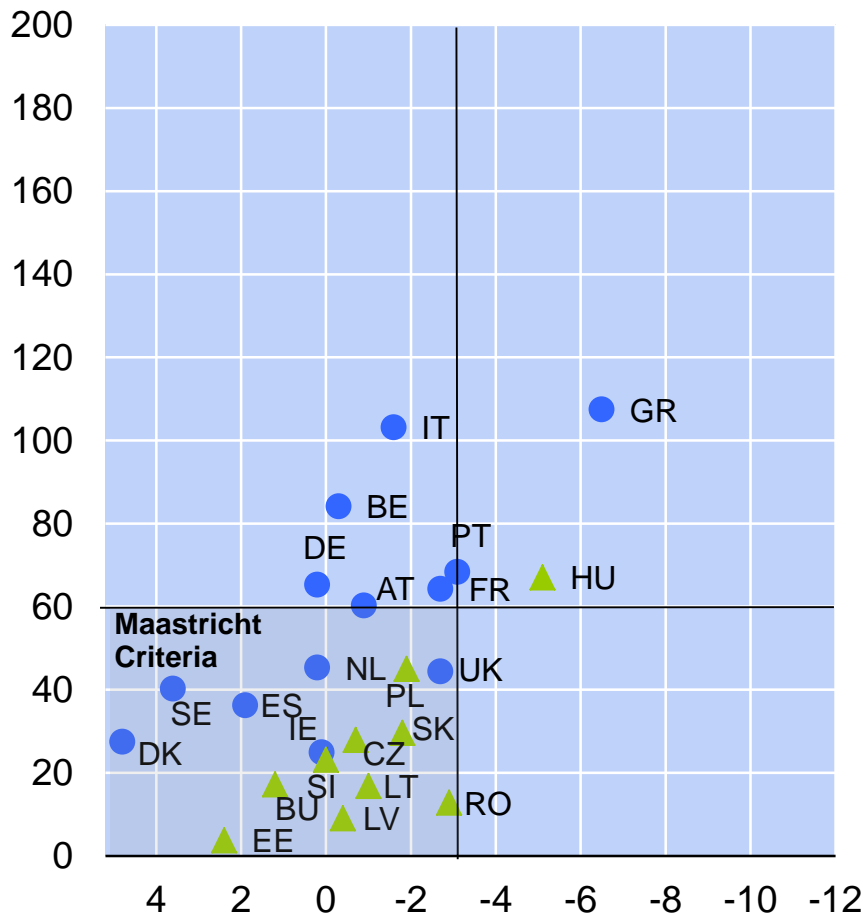


Source: Eurostat, IMF, NCBs.

Considerably Reduced Fiscal Space to Address Downturn

2007

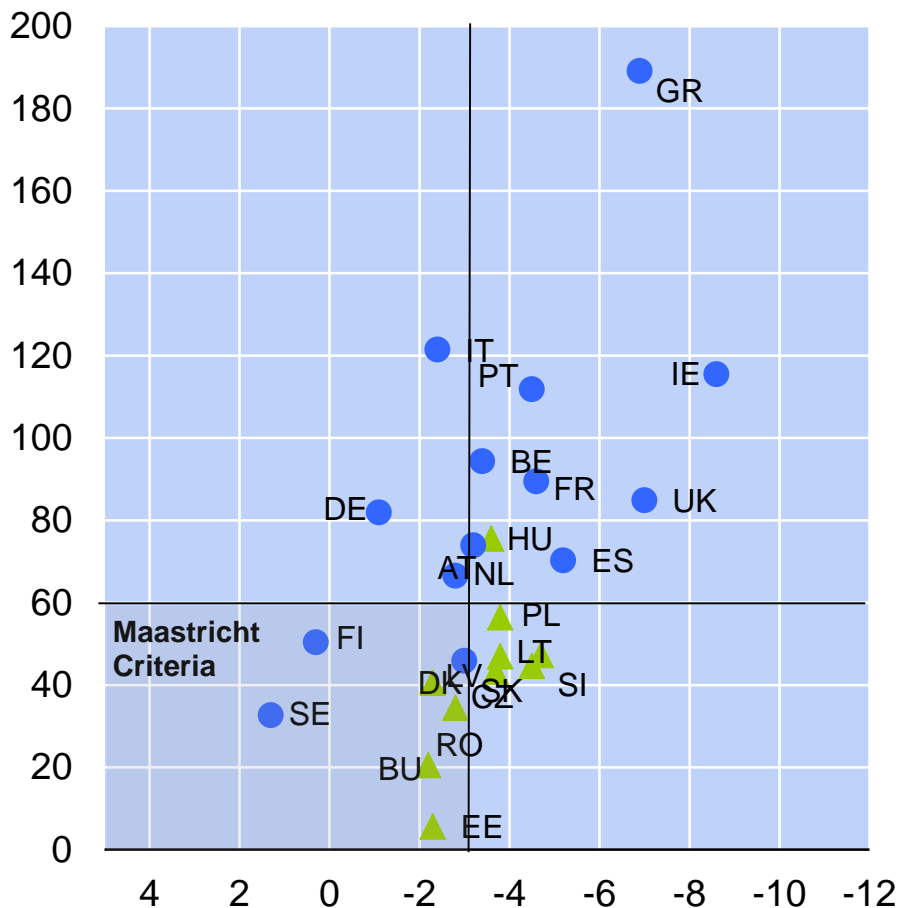
x-axis: budget deficit, y-axis: public debt, in % of GDP



Source: Eurostat, European Commission November 2011.

2012 (Projection)

x-axis: budget deficit, y-axis: public debt, in % of GDP



Risk of Restrained Supply of Bank Credit to the Real Economy

- **Negative feedback loop between sovereign debt problems and the banking sector in the euro area has emerged.**
- **Heightened funding pressures (due to significant refinancing needs) and EBA recapitalization exercise have increased banks' efforts to restructure their balance sheets.**
 - **Already, euro area banks have selectively reduced their sovereign exposure.**
 - **Both public and financial sector problems in the euro area increasingly threaten to adversely affect the real economy in- and outside the euro area (in particular in CESEE).**
 - **The risk of a sudden and simultaneous deleveraging as a result of these factors has to be addressed.**

Growth of Credit to the Private Sector

year-on-year growth of average stock of the periode in %, adjusted for exchange rate changes



Source: National central banks.

Policy Measures to Mitigate Banks' Funding Risks

- **The ECB's three-year LTRO of December 21, 2011, has alleviated the most acute funding problems of euro area banks.**
- **Individual banks will shortly submit their plans for proposed actions to fulfill the EBA regulatory requirements.**
- **Supervisory authorities will have to rigorously assess these plans to avoid that the envisaged actions have a restrictive impact on credit provision to the real economy.**

Avoiding the Re-Emergence of Macroeconomic Vulnerabilities as Convergence Resumes

- As the convergence process advances, the role of domestic saving should be enhanced through
 - domestic local currency deposit business
 - domestic bond issues
 - domestic equity issues
- The CESEE region will continue to be a catching-up region. Hence, foreign financing will continue to play an important role in the convergence process.

Yet, past mistakes must be avoided in the future!

Foreign financing should

- be geared toward export-oriented fixed investment
 - be more diversified
 - not crowd out / restrain domestic financing
- A bundle of measures is required in the fields of macroeconomic policy, institution building and macroprudential supervision to help realize these adjustments to (the financing of) the CESEE growth model.

To Sum Up: Key Challenges for the CESEE Region

- **Growth needs to become more broadly based, with both foreign and domestic sources playing an important role.**
- **Fiscal positions need to be stabilized gradually, without endangering domestic growth drivers.**
- **Banks actions to fulfill regulatory requirements must not have a restrictive impact on the provision of credit to the real economy.**
- **Policy toolkits (e.g. in the macroprudential area) have to be developed further to provide enough instruments to face current problems and any renewed increase in capital inflows.**
 - **Recent FMA/OeNB measures aim at strengthening Austrian banks' business models in the long run, given that they continue to have a long-term strategic commitment to the CESEE region.**

Strengthening the Sustainability of Large Austrian Banks' Business Models

Official supervisory guidance to be issued by FMA and OeNB to large internationally active Austrian banks (currently the top 3 Austrian banks)

1. Higher capitalization at the group level (increase risk-bearing capacity)

- Full implementation of **Basel III CET1-requirements*** without transition periods as of January 1, 2013
- Introduction of an **additional capital surcharge up to 3% CET1** as of January 1, 2016

2. Strengthening the local funding base of subsidiaries

(enhance the sustainability of future credit growth)

- Linking future net credit growth to the growth in stable refinancing (mostly deposits) at the subsidiary level by introducing a **maximum loan-to-stable funding ratio (LSFR) for net new lending of 110%** (only applicable to subsidiaries with high LSFRs)

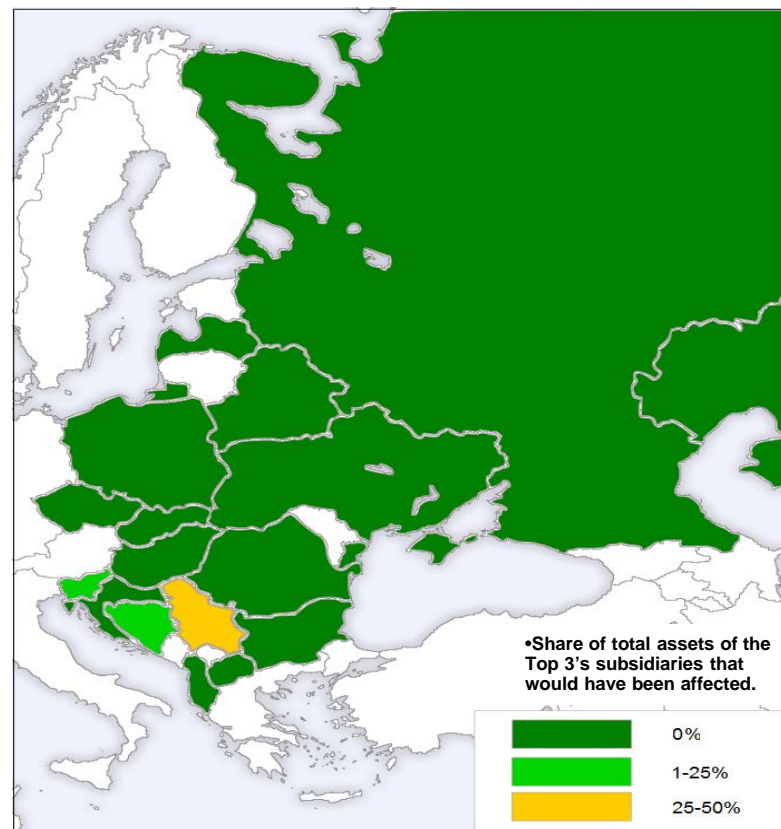
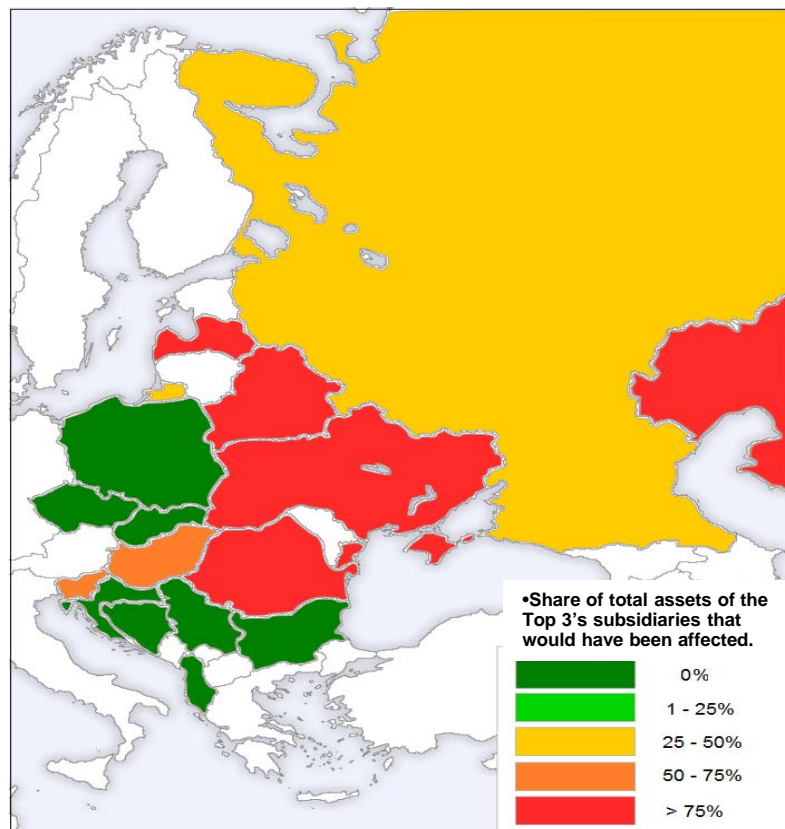
3. Submission of recovery and resolution plans on the group level in 2012

* An exception applies to private and public participation capital, which was issued in the course of the state's bank support package. This participation capital will be treated in line with the final CRR grandfathering / phasing-out provisions.

Anti-Cyclical: LSFR Measure Would Have Intervened in Boom Times, But No Credit Crunch in Times of Crisis

•Avoiding excessive credit growth (Q1 – Q4 2008)

•No credit crunch during the crisis (Q4 2008 – Q4 2009)



•Source: OeNB. Note: a) These representations use the stricter LDR, b) the proportionality clause (size of the subsidiaries) was not taken into account, c) Poland without Polbank data.