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CESEE Research Update

Foreign Research Division

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The CESEE Research Update is released quarterly by the Foreign Research Division of the Oesterreichische Nationalbank (OeNB). The aim of this newsletter is to inform readers about OeNB analysis and research output on Central, Eastern and Southeastern Europe (CESEE) as well as past and forthcoming CESEE-related events.

Foreign Research Division
OeNB

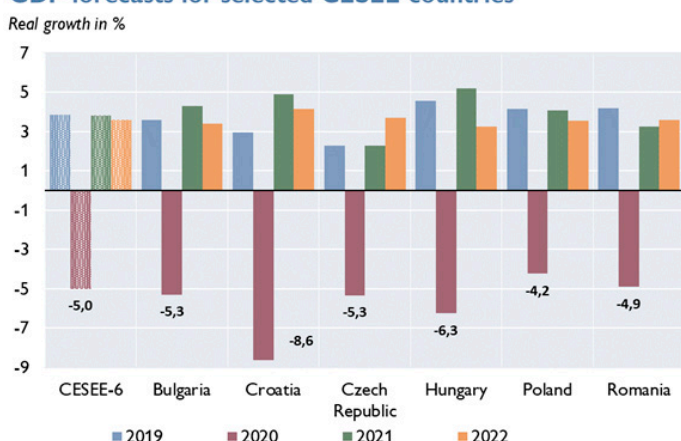
Highlight of this Issue

CESEE-6 with deepest downturn after transformational recession, uncertain recovery

Economic growth in the CESEE-6 countries (Bulgaria, Croatia, the Czech Republic, Hungary, Poland, Romania) will slump by 5.0% in 2020. We expect a moderate economic recovery of 3.8% in 2021 and of 3.6% in 2022. Croatia and Hungary are expected to be hit strongest by the COVID-19 crisis in 2020 but both economies will rebound somewhat more strongly in 2021. In 2020, private consumption will severely curb GDP growth in all CESEE-6 countries as a result of lockdown measures, income losses and great uncertainty among households. For 2021 and 2022, we expect a gradual recovery. The picture is similar for gross fixed capital formation. In line with our assumptions on euro area imports, exports will take a deep blow in 2020 in all CESEE-6 countries and the subsequent recovery will be somewhat muted. Import growth will turn negative in 2020 due to both lower domestic demand and lower intermediate demand for the production of export goods. In 2021, export and import growth will start to recover. In contrast to the global financial crisis, the contribution of net exports will be negative in all CESEE-6 countries in 2020 apart from Poland, and particularly so in Croatia and Hungary.

From 2021 onward, we expect the contribution of net exports to become slightly more favorable in most CESEE-6 countries. The catching-up process will also be affected by the COVID-19 crisis: In our baseline, GDP growth in the CESEE-6 region will surpass euro area growth by 3 percentage points in 2020. However, the growth differential will turn negative in 2021 (–1.2 percentage point) and be almost zero in 2022. Our forecast is surrounded by an exceptionally high degree of uncertainty related to the future development of the COVID-19 pandemic, connected economic developments in the euro area and the future EU budget (including the recovery fund). Overall, risks are mainly tilted to the downside.

GDP forecasts for selected CESEE countries



The COVID-19 crisis will weigh strongly on private consumption in 2020. As private consumption is an important growth contributor, this reduction will significantly burden CESEE-6 GDP growth. For 2021 and 2022, we expect private consumption growth to recover and to contribute positively to growth. Importantly, the base effect will help lift private consumption growth into positive territory in 2021, with growth being strongest in countries that experienced the strongest decline. However, there will be also negative carry-over effects of 2020 that weigh on private consumption, in addition to income losses and the uncertainty of households.

Public consumption growth is expected to contribute positively to GDP growth in all CESEE-6 countries in 2020. In 2021 and 2022, public consumption growth in the CESEE-6 countries will slow down further compared to 2020, possibly due to limited fiscal space.

Only in Hungary will growth gain speed because of carry-over effects from 2020 and the upcoming parliamentary elections.

Gross fixed capital formation will be negative in 2020 in all CESEE-6 countries with the notable exception of Romania. The drop will be strongest in Poland. The lockdown in spring 2020 meant a temporary standstill for many projects in the CESEE-6. Furthermore, an uncertain future, financial constraints or shortage of labor from abroad due to travel restrictions (particularly in the construction sector) will reduce investment activity visibly in 2020. For 2021, we foresee a recovery, which will also be based on EU funds. The recovery will be muted, though, by tightening financing conditions, a rising number of bankruptcies and idle capacities.

Our export growth projections are in line with the September 2020 ECB staff Macroeconomic Projection Exercise on euro area imports. Accordingly, export growth will collapse in 2020 in all CESEE-6 countries. For 2021 and 2022, we expect a rather modest recovery in line with assumptions on euro area imports. Import growth in the CESEE-6 will turn negative in 2020 due to both weaker domestic demand and lower export growth, given the high import content of traded goods. In 2021, both imports and exports will recover. The contribution of net exports in 2020 will be clearly negative in all CESEE-6 countries, particularly in Croatia and Hungary (reaching –3.2 and –3.3 percentage points, respectively). Only for Poland do we expect a positive contribution of net exports in the current year. From 2021 onward, we expect the contribution of net exports to become slightly more favorable in most CESEE-6 countries.

Currently, the most striking risk to our forecast – namely an increased spreading of the coronavirus in the CESEE-6, accompanied by renewed lockdown measures – is materializing in more and more instances. On the upside, a containment of the spreading of the coronavirus, new ways of reducing the dangers of COVID-19 infections, e.g. by some new treatment, or the availability of vaccination earlier than in mid-2021 (as assumed in our baseline) would improve our outlook for 2021 and 2022.

Economic growth in the CESEE-6 countries depends largely on economic growth in their trading partners. Therefore, higher (lower) growth of the world economy or of the euro area, in particular, than assumed in our baseline scenario would translate into higher (lower)

growth prospects for the CESEE-6. However, we see downside risks to external growth due to the negative impacts of an emerging second wave of COVID-19 infections in the CESEE-6 trading partners.

On the upside, the CESEE-6 countries would benefit particularly strongly, compared to other EU countries in relation to their GDP, from the July European Council proposal on the EU recovery instrument within the Next Generation EU (NGEU) fund for the period from 2021 to 2026 and the multiannual financial framework (MFF) for the period from 2021 to 2027.

However, some CESEE-6 countries' deficiencies in aligning with the EU's democratic standards are challenging these countries' relations with other EU members and

present a downside risk for the countries concerned if the EU were to condition the pay-out of EU funds on respecting the rule of law. This could also pose a more general downside risk to all CESEE-6 countries if potentially affected countries vetoed the NGEU.

Regarding Brexit, a hard Brexit cannot be ruled out and could likely impact our growth projections negatively, especially via trade disruptions.

In the context of international trade, disruptions in supply chains could last longer and leave deeper traces than assumed. On the other hand, a relocation of production to European countries in the process of shortening supply chains could also give a positive impetus to trade in the CESEE-6 region.

Summary: 86th East Jour Fixe: All about COVID-19? Geopolitical, economic and macrofinancial perspectives for the Western Balkans

The OeNB's 86th East Jour Fixe on September 28, 2020 was the first purely virtual event ever hosted by the OeNB. More than 80 registered participants followed the workshop online and gave the organizers credit for the good and innovative organization. In particular, the virtual coffee breaks, which enabled participants to have a personal online exchange in small groups with the speakers and panelists were met with a positive response.

In his welcome remarks, **OeNB Governor Robert Holzmann** reviewed the COVID-19 situation in the Western Balkans, virus-induced vulnerabilities as well as the potential macro- and microeconomic impact. He voiced expectations that the coronavirus crisis is likely to cause less macroeconomic damage in the Western Balkan region than in other CESEE countries, as the former is less integrated in global value chains. Nonetheless, countries highly reliant on tourism will be hit harshly, and this includes some Western Balkan countries. In addition, Governor Holzmann pointed to the expected sharp decline in remittances and its implications. He closed by calling for 1) providing (orchestrated) liquidity support for the region, 2) adjusting trade policies to facilitate cross-border commercial exchanges, 3) reducing transaction costs of remittances and, last but not least, 4) avoiding the

brain drain and population shrinkage. Most of these topics were picked up and deepened by the ensuing speakers.

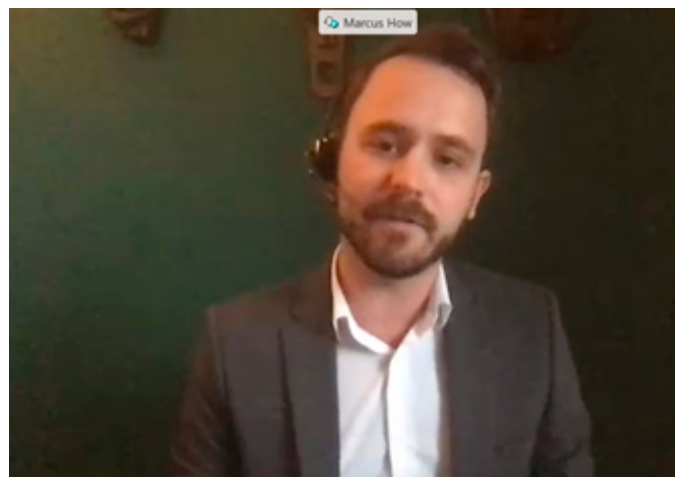


Session 1 – devoted to policy options and challenges ahead of the Western Balkan countries – was kicked off by a keynote speech delivered by **Wolfgang Petritsch, President of the Austrian Marshall Plan Foundation**. He addressed the populist tendencies and the authoritarian turn toward illiberal democracy which have been gaining momentum in the region, fueling legitimate concerns among EU enlargement skeptics such as France and The Netherlands. Add to this the widespread phenomenon of corruption and clientelism, long ignored or even tacitly accepted by the European Commission in the name of “stabilocracy”. Unfortunately, prospective EU membership has not produced a sustainable drive to embark on reforms. The EU is no longer the only major stakeholder in the region. Old and new players, particularly China, Russia and Turkey, have been expanding their role and pursuing their own objectives. Petritsch concluded by saying that the EU would need to shape a more strategic policy vis-à-vis the Western Balkans and double-down on its investments while engaging with China as a partner.



In the following panel discussion, **Marcus How, Head of Research and Analysis at ViennEast Consulting**, picked up on the enlargement skepticism in the region to which the EU has contributed. Yet, rather than subscribing to the general perception of EU candidates in the Western Balkans as victims of the enlargement standstill, How considers the region's state of limbo about EU accession to actually provide room for competition among other players. This may not be entirely negative for further development and may in fact be seen positively by foreign investors. Foreign investors value above all predictability, rejecting the usual narrative that pictures the rule of law and functioning democratic institutions as a prerequisite for a successful

economic development. That is, even if the rules of the game are rigged, investors can cope with the situation if some form of predictability exists, allowing risks to be navigated. Consequently, the revenue and expertise can be generated that may shape strong institutions.



Adding to these views, **Othon Anastasakis, Director of South-East European Studies at Oxford (SEESOX)**, argued that the geopolitical agenda in the region has grown beyond the strictly ethno-national, post-Yugoslav conflict issues and now includes other important global threats which make the region more vulnerable. Anastasakis stressed that despite the predominance of the transatlantic impact, the latter is not always uniform. There are some disagreements among EU countries and more so between the EU and the United States as far as the region's progress is concerned. Regarding external geopolitical actors that have become increasingly visible and seek to de-westernize the region, Anastasakis pointed out that these players have their own agendas, which are not necessarily compatible with each other, and that their influence is usually opportunistic and short-term. He cautioned against overestimating the influence exerted by non-European actors. Finally, Anastasakis urged participants not to overlook the biggest threat arising from internal vulnerabilities of the Western Balkan countries, namely rule-of-law issues, institutional weaknesses, illiberal elites and democratic backsliding.

The second session was designed to shed light on the threats to macrofinancial stability arising from the COVID-19 crisis. In the first of two kick-off presentations, **Antje Hildebrandt, Senior Economist at the OeNB's Foreign Research Division**, voiced concerns that financial



deepening and the process of de-euroization may be slowed down by the economic fallout from the pandemic. Additionally, but more in the short run, a high degree of euroization makes economies with a flexible exchange rate more vulnerable in case of sizeable currency depreciation. Regarding the impact of the crisis on nonperforming loans, Hildebrandt pointed out that this impact will depend on measures implemented (e.g. loan moratoria) to support households as well as on the economic recovery path.



Concerning the financial vulnerability of households in the Western Balkans due to the COVID-19 crisis, **Aleksandra Riedl, Senior Economist** at the **OeNB's Foreign Research Division**, shared research data collected with the OeNB Euro Survey. Specifically, she presented debt service-to-income ratios (DSTIs) of households in ten countries covered by the survey and found the median DSTI to be relatively high in the Western Balkan region. While the wealth position of households is rarely known, their income situation points to little room for maneuver. In a second step, Riedl assessed the impact of job losses due to the COVID-19 slump on DSTIs and found that a significant share of households in Bosnia and Herzegovina as well as in Serbia may run into trouble repaying their loans.



These two kick-off presentations were followed by a discussion among three high-ranking panellists. First, **Stephanie Eble, IMF's Regional Resident Representative for the Western Balkans**, gave an overview of economic developments and challenges of the Western Balkan region. Accordingly, all countries have been heavily hit by the crisis, particularly countries strongly dependent on tourism. Despite a high degree of uncertainty, risks

to economic growth are tilted to the downside. Inflation in the Western Balkan countries has remained rather subdued, and economic support packages have been smaller than in advanced countries with the notable exception of Serbia. Furthermore, foreign currency reserves have remained stable and deposits have increased due to precautionary savings. The decline in remittances has been partly mitigated by higher formal transfer payments. Eble pointed out that the Western Balkan countries are in a better situation regarding cross-border exposure than during the global financial crisis.

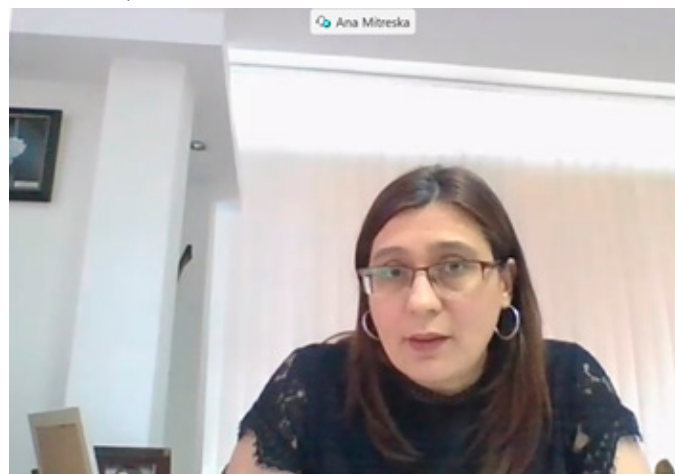


Second, **Sokol Havolli, Deputy Governor of the Central Bank of Kosovo**, gave a broad overview of how the pandemic has affected the Kosovar economy. Travel restrictions by European countries are one of the major drags on the country, as travel exports – an important source of income – have declined significantly. Havolli emphasized that quick and creative measures were implemented to overcome economic difficulties and to preserve liquidity in the economy. According to Havolli,



while the future is surrounded by many uncertainties, a worsening of the current situation would certainly imply a further deterioration of economic conditions, and additional measures would be needed.

Finally, **Ana Mitreska, Vice Governor of the National Bank of the Republic of North Macedonia**, pointed towards stronger fundamentals and smaller vulnerabilities in the current COVID-19 crisis compared to the global financial crisis of 2008. This is reflected in a more resilient banking sector, stronger external positions and a higher level of foreign reserves. According to Mitreska, the economy has been affected via several channels: private consumption and investment have been negatively affected by lower confidence and more pessimistic expectations, exports by lower foreign demand. However, the opening of the economy was immediately followed by a rebound. Mitreska also referred to monetary policy and regulatory changes adopted by the National Bank of the Republic of North Macedonia.



Issues addressed in the ensuing general discussion included the impact of the crisis on the de-euroization process. Overall, the pandemic has been observed to have changed the structure of the portfolio towards more liquid forms of assets in domestic currency and towards more savings in foreign currency in highly euroized countries. Yet, overall euroization remained stable. Last but not least, the debate touched upon global value chains, particularly in the automotive sector, in North Macedonia.

The presentation slides are posted on the OeNB website at <https://www.oenb.at/en/Calendar/2020/2020-09-28-east-jour-fixe-86.html>

OeNB Euro Survey

The OeNB Euro Survey of households has been conducted since 2007 in ten Central, Eastern and Southeastern European (CESEE) countries. With a strong focus on exploring different dimensions and drivers of currency holdings and households' saving and borrowing behavior, the OeNB Euro Survey additionally provides information on various aspects of financial literacy of CESEE households. The main results of the survey (recently updated with 2019 data) and information about possibilities of data sharing can be found at <https://oenb.at/en/Monetary-Policy/Surveys/OeNB-Euro-Survey.html>.

Focus on European Economic Integration Q3/20 – latest issue [\(full version\)](#)

Call for applications

Klaus Liebscher Economic Research Scholarship

Recent economic developments and outlook

A sleeping beauty or a dead duck? The state of capital market development in CESEE EU Member States
Thomas Reininger, Zoltan Walko

How financially literate is CESEE? Insights from the OeNB Euro Survey
Sarah Reiter, Elisabeth Beckmann

Typology of multinationals in Austria: CESEE focus and foreign control as distinct features
Thomas Cernohous, Tomáš Slačák

A CESEE conundrum: low trust in government but high hopes for government-led job creation
Markus Eller, Thomas Scheiber

CESEE-related abstracts from other OeNB publications



KLERS Klaus Liebscher Economic Research Scholarship

The Oesterreichische Nationalbank (OeNB) has established a new research scholarship: the “Klaus Liebscher Economic Research Scholarship.” This scholarship program gives outstanding researchers the opportunity to contribute their expertise to the research activities of the OeNB’s Economic Analysis and Research Department by providing remunerated consultancy services. The scholarship program targets Austrian and international experts with a proven research record in economics, finance or financial market stability who are interested in broadening their research experience and expanding their personal research networks. Given the OeNB’s strategic research focus on Central, Eastern and Southeastern Europe (CESEE), another key field of research might be the analysis of economic developments in the CESEE region. The program provides for an honorarium that depends on the length of the respective research project (max. EUR 10,000).

Please note that applicants need to be in active employment with their home institution. Eligible candidates must hold a PhD or equivalent degree and must have published work and conducted scientific research in the fields defined in the call for scholarship applications. Employees of the European Central Bank (ECB) or other central banks within the European System of Central Banks (ESCB) are not eligible for the Klaus Liebscher Economic Research Scholarship. ESCB employees may consider the options available under the ESCB’s External Work Experience (EWE) scheme or the Schuman Programme.

For more information, please visit the OeNB’s website at www.oenb.at/en/About-Us/Research-Promotion/scholarships_and_awards/klaus_liebscher_economic_research_scholarship.html or contact us by e-mail at scholarship@oenb.at.

Save the Date

OeNB-JVI webinar on „Monetary policy responses to the COVID-19 crisis”
with Barnabas VIRAG (NBH), Tomas HOLUB (CNB) and Piotr SZPUNAR (NBP).

Welcome: Herve JOLY (JVI)

Chair: Doris Ritzberger-Grünwald (OeNB)

Friday, December 11, 1:00 p.m.

More information concerning this webinar will be available at www.jvi.org shortly. For any administration-related questions concerning the webinar, please contact mpalahitskyy@jvi.org.

Announcement



The OeNB's conference volume “30 Years of Transition in Europe: Looking Back and Looking Beyond in CESEE Countries” will be published in the fall of 2020

Edited by Robert Holzmann, Governor; Doris Ritzberger-Grünwald, Director and Helene Schuberth, Head of Division, Oesterreichische Nationalbank, Austria

This thought-provoking book investigates the political and economic transformation that has taken place over the past three decades in Central, Eastern and Southeastern Europe (CESEE) since the fall of the Iron Curtain. Through an examination of both the successes and shortcomings of post-communist reform and the challenges ahead for the region, it explores the topical issues of economic transition and integration, highlighting important lessons to be learned.

Featuring contributions from both top academics and experienced policymakers, 30 Years of Transition in Europe first discusses the process of transition in CESEE from a historical perspective, analysing the impacts of differing approaches on economic and monetary policy, the role of central banks and the speed of reform in various countries of the region. Chapters also compare CESEE transformations to emerging economies in Asia, and examine contemporary concerns around financial and monetary stability, as well as exploring the long-term determinants of economic growth such as digitalization, climate change and demographic trends.

Economists, central bankers, and policymakers in the banking sector and other international financial organizations will find this book an enlightening read. It will also be useful for academics in economics and politics with a particular interest in emerging European economies and European integration.

More information: <https://www.e-elgar.com/shop/gbp/catalog/product/view/id/16704/>

Upcoming Events

The following events are organized by the OeNB and cover CESEE relevant topics.

Please note that attendance is by invitation only. If you are interested in participating in one or more of the events, please send an e-mail to event-management@oenb.at.

November 26, 2020	Global Economy Lecture in cooperation with the Vienna Institute for International Economic Studies (wiiw) on "Globalization and pandemics" (by invitation only)
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OeNB Courses at the Joint Vienna Institute (JVI) 2020 and 2021

In light of the ongoing COVID-19 global health emergency, the Joint Vienna Institute (JVI) has suspended its face-to-face training operations until the end of 2020. Many of the courses are now being delivered as virtual training events. In addition, the JVI is offering a series of webinars.

For the most up-to-date information on JVI training courses, please click the following link:

<https://www.jvi.org/training/course-schedules/course-schedule-2020.html>

Upcoming OeNB course

Title	Organization	Date
Monetary and Financial Statistics collected and Compiled by the ESCB	Oesterreichische Nationalbank	23 November – 1 December 2020
Financial Education	Oesterreichische Nationalbank	February 22 – 26, 2021
HR Issues and Compliance	Oesterreichische Nationalbank, in cooperation with the Deutsche Bundesbank	March 1 – March 5, 2021
Financial Stability and Supervisory Stress Testing for Banking Systems	Oesterreichische Nationalbank	April 12 – 16, 2021
Euro area integration and accession: institutional challenges and governance issues for central bankers	Oesterreichische Nationalbank	May 17 – 21, 2021
Climate Change and Green Finance	Oesterreichische Nationalbank and Austrian Federal Ministry of Finance	June 14 – 18, 2021
Diversity and Inclusion	Oesterreichische Nationalbank	September 6 – 8, 2021
Macrofinancial Stability in Central, Eastern and Southeastern Europe	Oesterreichische Nationalbank (OeNB), in cooperation with the JVI	October 11 – 20, 2021
Financial Translation and Editing: Trends and Tools for Future Challenges	Oesterreichische Nationalbank	October 13 – 15, 2021
Cash Circulation and Payment Systems in Austria	Oesterreichische Nationalbank	November 22 – 24, 2021

For more information please follow this link: <https://www.jvi.org/home.html>