Developments in selected CESEE countries

International headwinds take a toll on economic activity[1, 2, 3]

1 Regional overview

Further weakening of the international environment…

The pace of global economic activity remained weak in the review period. In mid-2019, global industrial production expanded at its lowest level since early 2016 and world trade growth came to a standstill. Rising trade and geopolitical tensions have furthermore increased uncertainty and negatively impacted on business confidence and investment. A more accommodative monetary policy in major regions of the world economy has cushioned some of the impact of these tensions on financial market sentiment and activity, however.

Euro area growth slowed notably in the second quarter of 2019, given a combination of risks (most prominently the threat of a "hard Brexit") and country-specific factors. The latter include political, fiscal and economic fragility in Italy and, which is more important from the perspective of Central, Eastern and Southeastern Europe (CESEE), the weakening economic momentum in Germany. German economic activity declined in the second quarter of 2019 and the country could easily slip into technical recession in the third quarter amid a slump in industrial activity.

… impacts CESEE EU Member States' GDP growth in the second quarter

After an unexpectedly strong first quarter of 2019, these external headwinds took their toll on the CESEE EU Member States. In this group of countries, average real GDP growth declined to the lowest level in three years by mid-2019. However, strong private consumption, easing real monetary conditions and a mostly expansionary fiscal stance kept economic growth at a rather robust level. We must also note that today, resilience to an adverse international environment is notably higher than ten years ago, given solid external and public balances and the associated policy space.

In the CESEE region, growth in the observation period was slowest in Russia. Lower investment and construction expenditures and the value added tax (VAT) hike at the beginning of the year weighed on domestic demand. At the same time, the weakening of the global economy and lower oil prices had exports declining notably especially in the second quarter of 2019. Industrial production continued to be supported by raw materials and low-value added goods but failed to accelerate due to weaknesses in the manufacturing sector.

Economic activity in Turkey stabilizes

More positive news came from Turkey. The Turkish economy exited recession in the first half of 2019 and reported quarterly growth rates that were notably above regional averages. This revival was based mainly on a sizable external adjustment (based on rising exports and declining imports) and several government measures (including adjusting tax rates and rising public sector wages). Private consumption and

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[2] *Cutoff date: October 4, 2019. This report focuses primarily on data releases and developments from April 2019 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, Montenegro, North Macedonia, 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.*

Table 1

Real GDP growth

	2017	2018	Q1 2018	Q2 2018	Q3 2018	Q4 2018	Q1 2019	Q2 2019
	Period-on-period change in %, seasonally and working day adjusted							
Slovakia	3.2	4.1	1.0	1.3	0.8	0.6	0.7	0.5
Slovenia	4.8	4.1	0.3	1.2	1.1	0.6	0.6	0.0
Bulgaria	3.8	3.1	0.9	0.8	0.7	0.8	1.2	0.8
Croatia	2.9	2.6	0.3	1.4	0.5	0.3	1.5	0.2
Czech Republic	4.4	3.0	0.6	0.6	0.6	0.9	0.6	0.7
Hungary	4.1	4.9	1.2	1.1	1.5	1.1	1.4	1.1
Poland	4.9	5.1	1.4	1.3	1.4	0.4	1.4	0.8
Romania	7.0	4.1	0.3	1.3	1.3	1.0	1.2	1.0
Turkey	7.5	2.8	2.0	0.9	–1.1	–2.4	1.3	1.2
Russia	1.6	2.3	2.2	0.3	0.3	0.2	0.2	0.2
CESEE (weighted average)	3.9	3.0	1.8	0.7	0.2	–0.3	0.8	0.6
Euro area	2.5	1.9	0.3	0.4	0.2	0.3	0.4	0.2

Source: Eurostat, national statistical offices.

investments continued to shrink, however, as the instability of the Turkish lira and the efforts to stabilize the currency have badly hurt domestic demand and confidence.

Our data show that average real GDP growth in CESEE amounted to 0.8% in the first and 0.6% in the second quarter of 2019 (quarter on quarter, respectively, see table 1). This represents an acceleration compared to the second half of 2018. Most of the acceleration, however, was due to the rebound of the Turkish economy, which reported growth rates of well above 1% both in the first and second quarters of 2019 (year-on-year growth, however, remained negative). Average growth in the CESEE EU Member States declined to 0.8% in the second quarter of 2019, 0.5 percentage points below the reading recorded in the first quarter of the year. At the level of individual countries, strong dynamics were observed for Hungary and Romania, while growth in Croatia and Slovenia came to a near standstill. The same is true for Russia, where quarter-on-quarter growth has hovered at around 0.2% since mid-2018.

Exports exert a drag on growth in most CESEE countries

A look at the development of individual GDP components reveals that net exports contributed negatively to growth in most CESEE EU Member States and Russia (see chart 1). This suggests that deteriorating international demand took a toll on export activity except in Turkey. In fact, export growth in the CESEE EU Member States declined considerably in the second quarter of 2019, reaching its lowest level since late 2012 (2.4% on average, year on year). Import growth declined, too, but continued to outpace export growth on the back of robust domestic demand (+3.4% on average, year on year).

At the country level, export growth declined most clearly in Slovakia (to negative levels) and the Czech Republic, the countries most strongly integrated into European production networks. However, a downward trend was observed in most other countries as well. Throughout the CESEE region, export expectations soured and the growth of (strongly export-oriented) industrial production declined markedly during the past months and has reached its weakest level in six years.

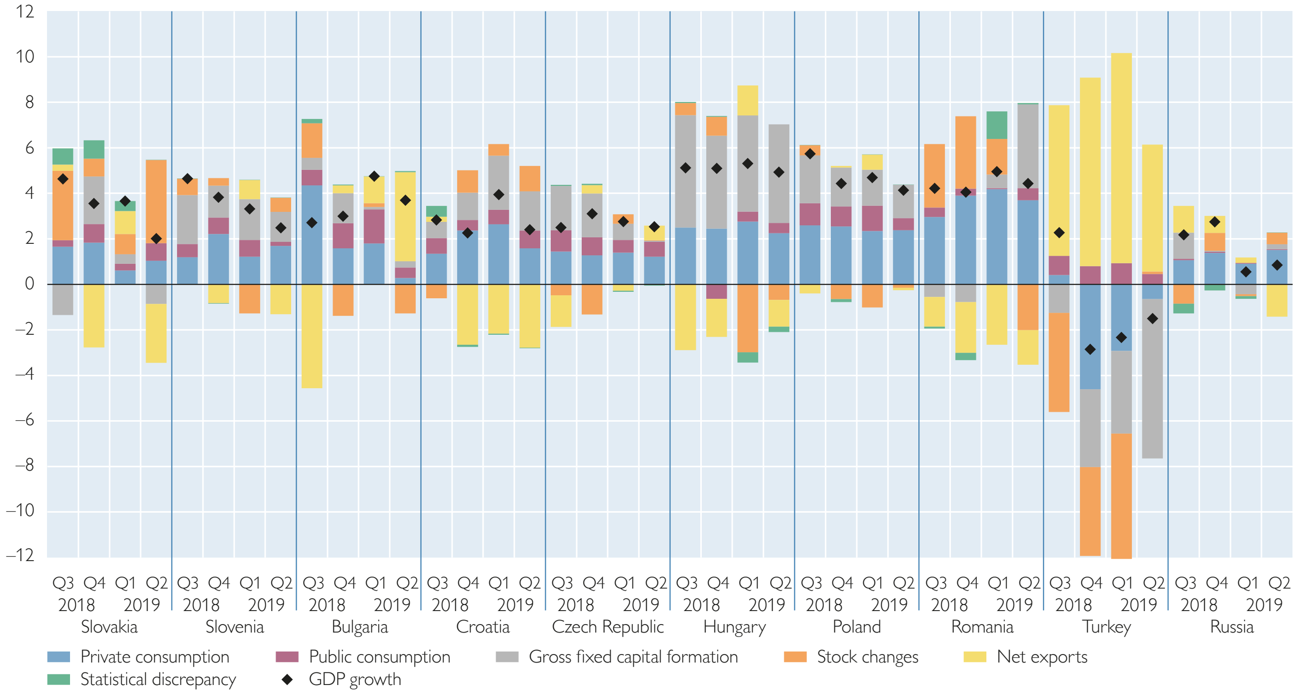
Diverging trends in competitiveness, but wage growth fuels ULC throughout the region

Elevated and prolonged increases in unit labor costs (ULC) in the CESEE EU Member States may help explain recent export weaknesses. For many quarters,

Chart 1

GDP growth and its main components

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



Source: Eurostat, national statistical offices.

strong wage advances have pushed up CESEE manufacturing ULC (measured in euro), and they continued to do so also in the review period. At the same time, largely robust productivity developments and a moderate depreciation of local currencies against the euro (by 1% to 2% in the first half of 2019) bolstered the CESEE EU Member States' competitive position somewhat in the past two quarters.

However, the situation is not homogenous throughout the region. Slovenia, Croatia and Poland, for example, managed to improve their competitiveness vis-à-vis the euro area mainly on the back of comparatively low wage growth rates in the first half of 2019. There are also differences when it comes to export markets. Surveys suggest that companies in the CESEE EU Member States assess their competitive position on markets outside the EU as largely solid, while it deteriorated on EU markets as of late.

Developments were more clear-cut in Russia and Turkey. Both countries gained competitiveness on the back of a depreciation of the respective local currencies while underlying ULC trends remained weak. In the first half of 2019, the Turkish lira lost more than 20% of its value against the euro when compared to the same period of the previous year. The Russian ruble depreciated by around 6% against the euro in the first quarter before regaining some value in the second quarter of 2019.

Poorer export prospects impact on investment…

Investment developed heterogeneously in the CESEE region. In some countries, poor export prospects led companies to postpone or scale down investment, with some of the largest projects in car manufacturing under threat from plummeting European demand. This was especially the case in the Czech Republic and Slovakia, where investment growth nosedived in the review period. However, investment growth also lost substantial steam in Bulgaria and Slovenia. Negative trends were substantiated further by weakening orders and especially a decline in export order books. This was mirrored in corporate sentiment, with both construction and industrial sentiment (as measured by the European Commission's Economic Sentiment Indicator) on a downward trend since 2018.

In Turkey, investment spending contracted markedly. Capital formation suffered from tight financing conditions, corporates' high repayment obligations (partly related to foreign currency-denominated debt) and poor investor sentiment. In Russia, capital formation hardly contributed to growth in the first half of 2019.

… but domestic factors keep capital formation running in several CESEE countries

The negative investment dynamics, however, did not extend to the whole CESEE region. Croatia, Hungary, Poland and Romania reported strong capital formation, despite external headwinds and weakening sentiment. Factors contributing to this development include, inter alia, high capacity utilization rates, accelerated growth of credit to the corporate sector, expanded housing subsidies, EU-funded projects and/or accommodative monetary policy.

Favorable labor market developments spur domestic demand

The generally still solid level of output growth is attributable mainly to the ongoing dynamism of private consumption. Private consumption – which was responsible for the largest contributions to GDP growth in 5 of the 8 CESEE EU Member States in the first half of 2019 – continued to benefit from benign labor market conditions, swift wage growth and supportive policy measures in some countries.

Despite some softening of general economic dynamics, labor markets remained in full swing, with important labor market indicators at, or close to, historical records 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 3.6% in August 2019 – 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 (aged under 25) and older persons (aged 50+). The downward trend in long-term unemployment continued and was broad based. Furthermore, employment kept expanding throughout most of the region, contributing to a convergence of employment rates toward euro area levels (68% in the second quarter of 2019). By the second quarter of 2019, the employment rates of six CESEE EU Member States had already exceeded the euro area average.

The reverse side of these positive labor market trends were labor market shortages. According to a survey by the European Commission, a lack of labor is perceived as a strongly limiting factor for production in the CESEE EU Member States: In the third quarter of 2019, at least 39% of respondents in industry, 24% in services and 43% in construction reported that they struggled to find workers. The respective figures were highest for Hungary, where they reached levels of up to 68%.

Labor market strains relax slightly

The European Commission survey reported slightly better outcomes for manufacturing and construction during the past three quarters, which might indicate that labor markets are finally starting to cool off somewhat. Labor shortages were possibly mitigated by immigration from the Western Balkans and Ukraine (e.g. in Poland), some re-migration of CESEE citizens from Western European countries, investment in labor-saving technologies as well as a higher geographic mobility within the CESEE EU Member States.

Wage statistics also hint toward some easing of labor market strains. After a long period of acceleration, nominal wage growth in the CESEE EU Member

States has softened, on average, since the beginning of 2019, declining from around 12% year on year to about 10.5% in the second quarter of 2019.

Dynamic labor markets and higher wages positively impacted on sentiment and prompted consumers to take out credit. Consumer confidence was the only component of the European Commission's Economic Sentiment Indicator that actually improved over the reporting period.

The unemployment rate remains at a record low also in Russia (4.3% in August 2019). However, low unemployment in Russia seems to be, at least in part, related to people dropping out of the labor force. Despite remaining relatively weak by regional comparison, private consumption contributed most strongly to growth in Russia.

Turkey was the only country in the region where private consumption contributed negatively to growth and unemployment increased to above 20% in August 2019. The drag on output moderated in the review period on the back of a package of expansionary economic policy measures. These include higher minimum wages, tax cuts and the extension of cheap credit by state-owned banks, among others.

Domestic price pressures push up inflation further in the CESEE EU Member States…

Dynamic wage growth contributed to a further increase of price pressures in the CESEE EU Member States. The average inflation rate rose from 2.2% in February to 2.9% in August 2019 (see chart 2). This has been the highest inflation reading since 2012. The increase of inflation was broad based and encompassed all HICP components but energy. Energy prices were held back by the lower average oil price in the review period. Against this background, core inflation also trended up notably (from 2.2% in February to 2.8% in August 2019), indicating a strengthening of domestic price pressures. The latter have been fueled by generally tight labor markets pushing up aggregate ULC growth, by capacity utilization rates far above historical averages and a positive output gap.

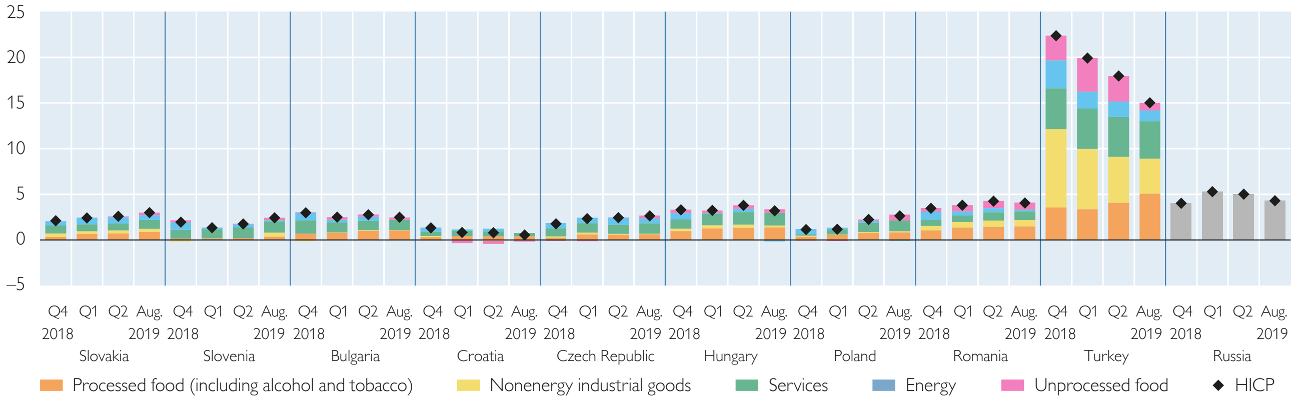
… while price dynamics moderate in Russia and Turkey

Unlike in the CESEE EU Member States, price growth moderated in Russia and Turkey. In Russia, inflation declined to 4.3% in August 2019 after it had risen to 5.3% in the first quarter of 2019 against the backdrop of a VAT increase. The pass-through effect of the VAT increase to consumer prices has been weaker than expected, in part because of low domestic demand.

Chart 2

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.

In Turkey, inflation declined from around 20% at the beginning of the year to 15% in August 2019, aided by a partial recovery of the Turkish lira and soft domestic demand conditions.

Interest rate cuts in Russia and Turkey against the background of lower inflation rates

Both the Turkish and the Russian central bank cut their policy rates as inflation rates were moderating.

In Russia, the key policy rate was cut in three steps of 25 basis points each from 7.75% in June to 7% in September 2019 (see chart 3). After these cuts, the key rate has reached the lowest level since early 2014, just before the oil price crash and Western sanctions triggered a financial turmoil and a sharp fall in the Russian ruble's external value. The Russian central bank (CBR) noted that inflation is continuing to slow and reduced its forecast for year-end inflation from 4.2%–4.7% to 4%–4.5%. With these inflation figures, compliance with the CBR's 4% inflation target is within reach.

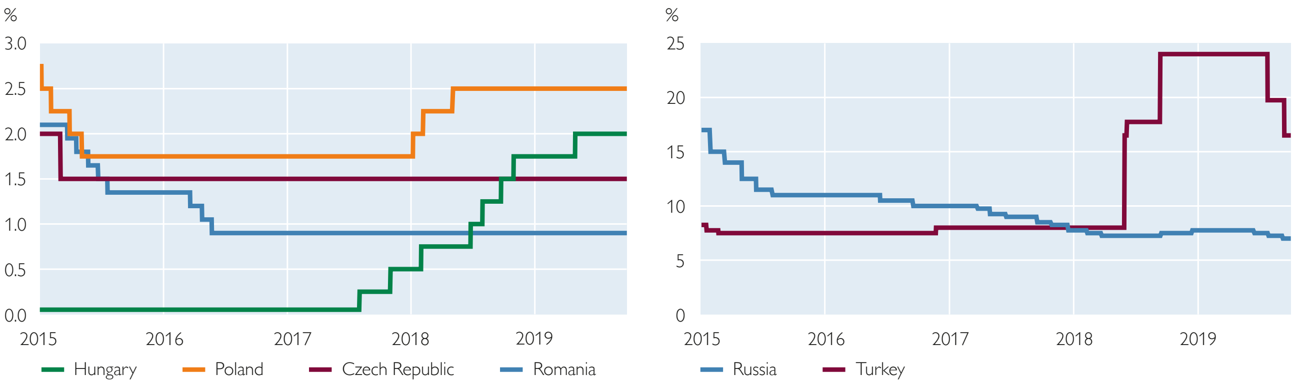
It remains to be seen, however, whether the rate cut will have a significant impact on business lending and consumption. Surveys indicate that the main constraint on investment is not the low availability of credit, but high uncertainty and the poor business environment. Moreover, although corporate profits were high across much of the business sector last year, this has not translated into a strong pickup of spending on investment. At the same time, lending conditions for households became tighter in October, as the CBR implemented new prudential rules to constrain unsecured household borrowing, which has grown too rapidly in the past two years.

The Turkish central bank (CBRT) cut its policy rate in two steps from 24% in July to 16.5% in September 2019. A change in the CBRT's top management in July preceded these two cuts. The CBRT stated that the year-end consumer price inflation rate was likely to be lower than projected. In addition to the stable course of the Turkish lira, it argued, improving inflation expectations and soft domestic demand conditions had supported the decline in core inflation. In early October, the Turkish lira came under renewed pressure because of concerns over Turkey's military incursion into Syria.

Among the CESEE EU Member States, the Czech Republic was the only country to adjust its policy rates in the review period. The Czech central bank (CNB)

Chart 3

Policy rate developments in CESEE



Source: Macrobond.

increased its rate by 50 basis points to 2% in May 2019. The CNB expects inflation to stay above the 2% target but still within the tolerance band for the rest of 2019. Comparatively strong price rises are related to persisting domestic inflation pressures, stronger administered price inflation and a renewed rise in food prices. According to the CNB, inflation will start to decrease in early 2020 and will approach the target over the monetary policy horizon, i.e. in the second half of 2020.

External adjustment in Turkey pushes up CESEE's current account balance

The combined current and capital account surplus in the CESEE region increased further in the review period, rising from 2.5% of GDP at the end of 2018 to 3.3% of GDP in mid-2019 (see chart 4). The external adjustment was especially remarkable in Turkey, where a current account deficit of 3.4% of GDP in 2018 turned into a broadly balanced position by mid-2019. A large-scale exchange rate depreciation and weak domestic demand boosted Turkey's goods and services balance. A notable improvement in the current account surplus was also reported for Bulgaria, where all individual components, especially the trade balance, posted better outcomes than a year ago.

Changes in the external accounts of the other countries under review where more moderate, ranging between +0.7 percentage points of GDP in Poland and –1.5 percentage points of GDP in Croatia. Among the components, the only somewhat more broad-based trend was a moderate decline in the primary income balance, related to lower outflows of dividends against the backdrop of generally lower economic dynamics.

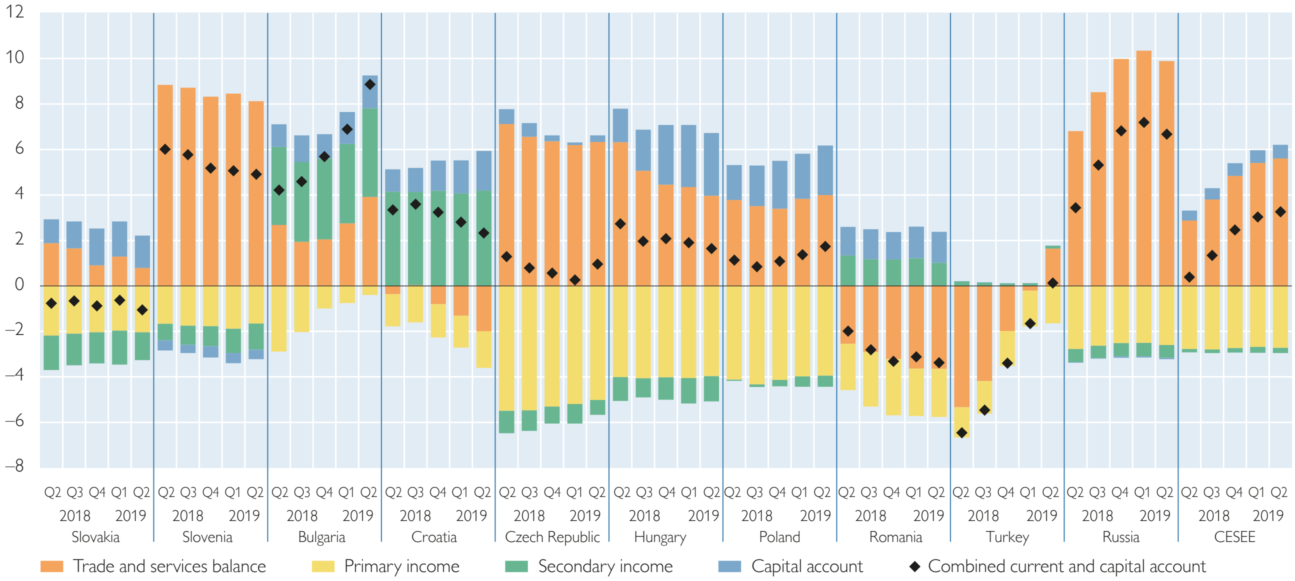
Capital outflows from CESEE broadly unchanged

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 remained broadly unchanged between end-2018 and mid-2019 (+4.2% of GDP, four-quarter moving sums, see chart 5). However, a notable reduction of the balance was to be observed between the first and second quarters

Chart 4

Combined current and capital account balance

% of GDP, four-quarter moving sum

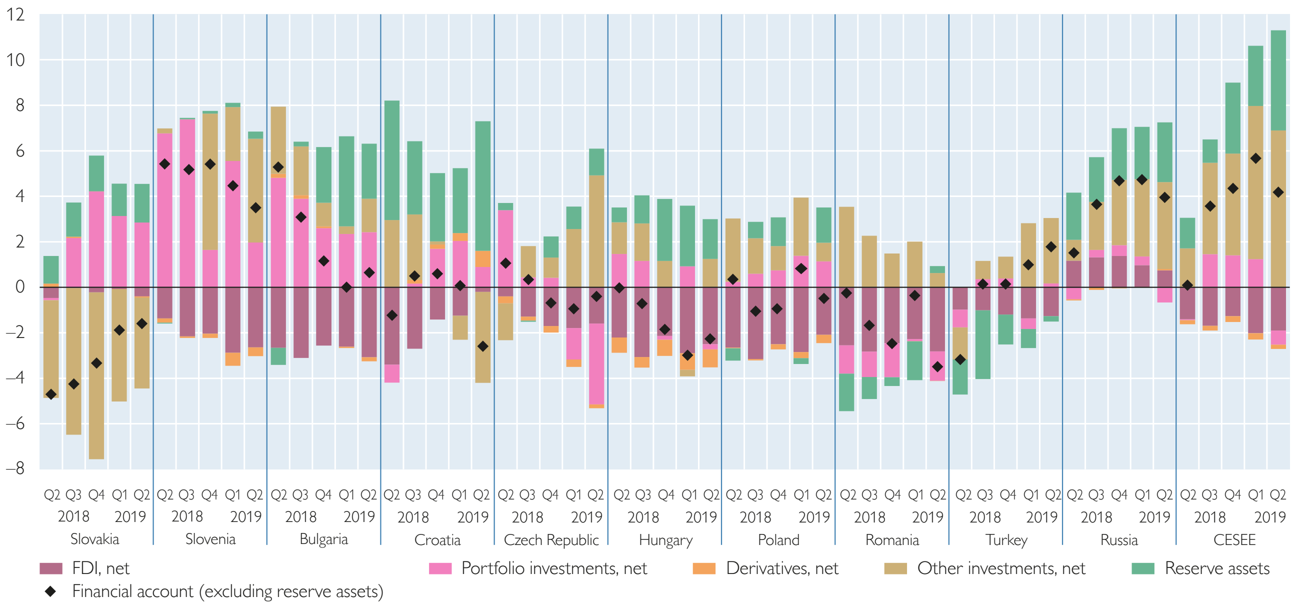


Source: Eurostat, IMF, national central banks.

Chart 5

Financial account balance

% of GDP, four-quarter moving sum



Source: National central banks.

Note: Positive values indicate a net outflow of capital, negative values indicate a net inflow of capital (vice versa for reserves).

of 2019. This implies that capital outflows have moderated. Russia contributed most to this development, as the country again reported net capital inflows into government bonds in the second quarter of 2019. However, the imposition of a new round of U.S. sanctions in August 2019 might put a brake on this development. Sanctions comprise a ban of U.S. banks from participating in initial sales of Russia's non-Russian ruble denominated sovereign debt and from providing foreign currency financing to the Russian sovereign. Furthermore, it must be noted that private sector net capital outflows from Russia continued in the first half of 2019.

Turkey was the only country in the region to report higher capital outflows in the review period. It was other investments (mostly reflecting bank flows) that weighed most strongly on capital flows, with the deterioration being driven by both a higher acquisition of assets abroad and a lower incurrence of liabilities from abroad.

Credit growth trending moderately downward in many CESEE countries

With currencies on a moderate downward trend and real interest rates falling due to higher inflation or rate cuts, real monetary conditions eased throughout CESEE in the first half of 2019 (see chart 6). Growth of domestic credit to the private sector (nominal lending to the nonbank private sector adjusted for exchange rate changes), however, declined somewhat in many countries.

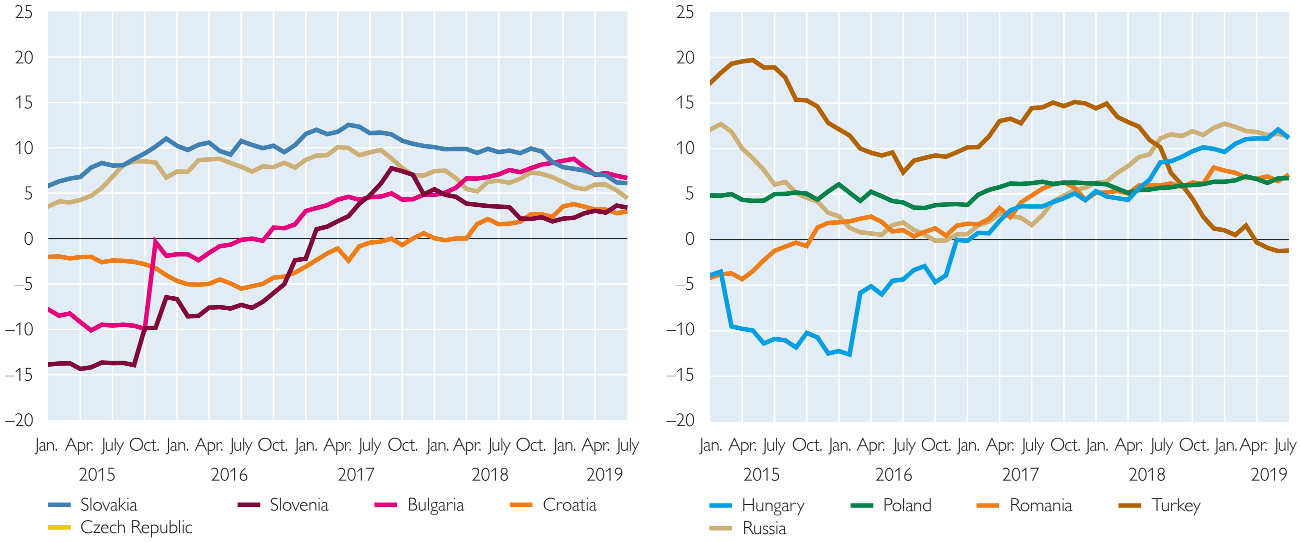
This is true for Turkey in particular. Turkish credit growth dipped into the reds in mid-2019 as tighter financial conditions, high risks and adverse exchange rate developments held back loan supply, while weakening domestic demand and high interest rates impinged on loan demand. A relaxation of lending standards for some segments and the key interest rate slash as of July 2019, however, recently contributed to an easing of lending conditions.

In fact, some moderation of credit dynamics was a welcome development especially in the CESEE EU Member States, as too rapid loan growth had caused

Chart 6

Growth of credit to the private sector

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



Source: National central banks.

risks to build up in certain segments of the loan market in several countries. This applies to housing loans in particular.

Regulators take action against rising housing loans and house prices

The past years have witnessed a notable increase in real estate prices in CESEE. In the first quarter of 2019, housing prices in the CESEE EU Member States rose by some 7% on average year on year (with growth rates ranging between 3.3% in Romania and 9.4% in the Czech Republic and Hungary). While this represents some moderation compared to 2018, housing prices continued to grow at a substantially stronger pace than in the EU on average. These dynamics were related to strong housing demand against the backdrop of favorable financing and general economic conditions as well as policies to improve the affordability of housing in several countries (e.g. in Croatia, Hungary and Poland). At the same time, a lack of skilled labor in the construction sector prevented supply from keeping track with demand.

Several CESEE central banks identified the combination of rapidly rising house prices and housing loans as a threat to financial stability (e.g. in the Czech Republic, Slovakia and Slovenia) and introduced macroprudential measures and/or issued recommendations to put a brake on this development. Instruments include debt service-to-income ratios (e.g. in the Czech Republic, Hungary, Romania, Slovakia and Slovenia), higher risk weights (e.g. in Poland and Slovenia), loan-to-value ratios (e.g. in the Czech Republic, Hungary and Slovakia) as well as loan-to-income ratios (e.g. in the Czech Republic and Slovakia).

Countercyclical capital buffer active in three countries

Bulgaria, the Czech Republic and Slovakia have also activated the countercyclical capital buffer. In Bulgaria, the buffer was implemented only in October 2019 (0.5%) and will be raised to 1% in April 2020. In the Czech Republic, the buffer currently stands at 1.5% and is to be raised to 1.75% in January 2020 and to 2% in July 2020. In Slovakia, the buffer will be raised to 2% in August 2020 from its current level of 1.5%. These measures seem to be successful in curbing credit dynamics as Bulgaria, the Czech Republic and Slovakia also were the countries that reported the most notable decline of credit growth in the review period.

Only Hungary and Slovenia reported a stronger rise in credit growth than in the previous observation period. In Hungary, lending was supported by various policy measures, including the expansion of housing subsidies to families and the central bank's Funding for Growth Scheme Fix, targeted at long-term lending to small and medium-sized enterprises (SMEs) at fixed interest rates. In Slovenia, the growth of loans to households far outstripped the growth of loans to corporates. The latter was held back by high corporate profitability and increasing internal resources but accelerated somewhat in recent months.

Prudent lending in the CESEE EU Member States

By and large, the CESEE EU Member States' credit markets are in a sound shape as regulators keep a close eye on the build-up of risks and banks have become more prudent when it comes to extending new credit. This also shows in the European Investment Bank's (EIB) latest CESEE Bank Lending Survey. Credit demand improved across the board in the first half of 2019, marking the 13th consecutive semester of favorable developments. All factors affecting credit demand made positive contributions, only debt and corporate restructuring had almost no effect.

Higher credit demand was paired with broadly unchanged credit supply conditions in the first half of 2019. With that, the positive gap between credit demand and credit supply that had been perceived for several quarters continued to persist. On balance, this would imply a better loan quality for most of new lending than in previous credit cycles. Across the client spectrum, credit standards eased again for lending to SMEs and consumer credit, while they tightened for mortgages. Changes in local regulations were perceived as key factors adversely affecting supply conditions.

Strong growth of unsecured consumer loans in Russia

In Russia, high credit growth rates of around 12% year on year since mid-2018 have given rise to concerns. Growth is relatively lopsided as it is largely driven by retail loans, while credit to enterprises has continued to be rather sluggish. Although household debt remains comparatively low on aggregate, unsecured consumer loans (which comprise over half of all consumer loans) have grown particularly briskly. The CBR has responded by raising risk-based capital buffers several times since early 2018 and introduced additional tightening measures in October 2019.

Box 1

Ukraine: economic recovery continues, talks on further IMF program initiated

GDP growth accelerated to 3.6% year on year in the first half of 2019. Private consumption grew briskly by 11.3% year on year, benefiting from increasing real wages and pensions as well as from remittances and consumer loan growth. The unemployment rate fell to 9.2% in the first quarter of 2019, down from 9.7% one year earlier. Growth of gross fixed capital formation decelerated somewhat but remained dynamic with an annual growth rate of 12%. After exports had contracted in 2018, they recovered in the first half of 2019, boosted by a bumper harvest. Yet, as import growth sped up, the growth contribution of net exports remained negative.

Since the beginning of the year, annual headline inflation has fluctuated around 9%, and it stood at 8.8% in August. Yet, core inflation fell to 7.2% in August from 8.7% at end-2018. The National Bank of Ukraine (NBU) cut its key policy rate three times (in April, July and September) by 150 basis points overall to 16.5%. Despite these interest rate cuts, the real interest rate level is still relatively high. The NBU expects inflation to meet the 5% target at the end of next year and signaled that it would continue the monetary policy easing cycle provided inflation is steadily declining toward this target.

In the four quarters up to mid-2019, the current account deficit stood at 3.1% of GDP, slightly down from 3.4% at end-2018. The current account continues to show a large trade deficit, which is partly compensated by surpluses in both income balances that largely reflect income from Ukrainians working abroad, particularly in Poland. Net FDI inflows remained subdued, amounting to 1.7% of GDP in the four quarters up to mid-2019 (almost unchanged compared to 2018). Despite a notable reform progress that has been going on since 2014, the main obstacles to foreign investment (widespread corruption, lack of trust in the judiciary, and the influence of oligarchs) still prevail. After international financial support lifted official foreign currency reserves to USD 20.8 billion at end-2018, these reserves increased further to USD 22 billion (3.5 months of imports) by August 2019. Favorable conditions on the foreign currency market allowed the NBU to replenish its foreign currency reserves while the Ukrainian hryvnia was on an appreciation trend.

Under the 14-month IMF Stand-By Arrangement (SBA) approved in December 2018, only one tranche amounting to USD 1.4 billion (out of a total volume of USD 3.9 billion) was disbursed. In May 2019, an IMF mission held discussions with the Ukrainian authorities (including the newly elected President Volodymyr Zelensky) on the first review of the SBA. Yet, the mission indicated that it would be necessary to wait for the outcome of early parliamentary elections and for clarity about the policy intentions of the new administration before the review could be concluded. Parliamentary elections took place in July and Zelensky's party secured an absolute majority. After a government was formed, an IMF team visited Kiev to initiate discussions on a new three-year program under the IMF's Extended Fund Facility (EFF) in September. The IMF mission statement highlighted productive discussions on economic policies (including further reforms) but also underlined the need to make every effort to minimize the fiscal costs of bank resolutions. While no final agreement could be reached, it was announced that discussions would continue. The IMF seems to be concerned about controversial court rulings (to which the NBU has filed appeals) on the nationalization of Privatbank, which was carried out in December 2016 under the auspices of the IMF.

Box 2

Western Balkans[4]: economic growth lost momentum in the first half of 2019

In the Western Balkan countries, annual economic growth decelerated to 2.9% (GDP-weighted average) in the first half of 2019 from 3.8% in 2018 (and from 4.1% in the first half of 2018). The slowdown was strongest in Albania, Montenegro and Serbia. Economic performance was blurred by country-specific one-off factors in Albania and Montenegro. Albania suffered mainly from adverse weather conditions (low rain falls) that negatively affected the generation of hydroelectricity; in Montenegro, the phasing out of a large infrastructure project related to highway construction was reflected in deteriorating investment growth. In Serbia, the reasons for slower growth were more broadly based. North Macedonia, by contrast, grew much more strongly in the first half of 2019, largely reflecting recovery after a phase of political uncertainty in 2017 and early 2018. Kosovo's growth profile changed strongly in the second quarter of 2019 compared to the first quarter, with net exports becoming the major growth contributor whereas private consumption growth almost stagnated.

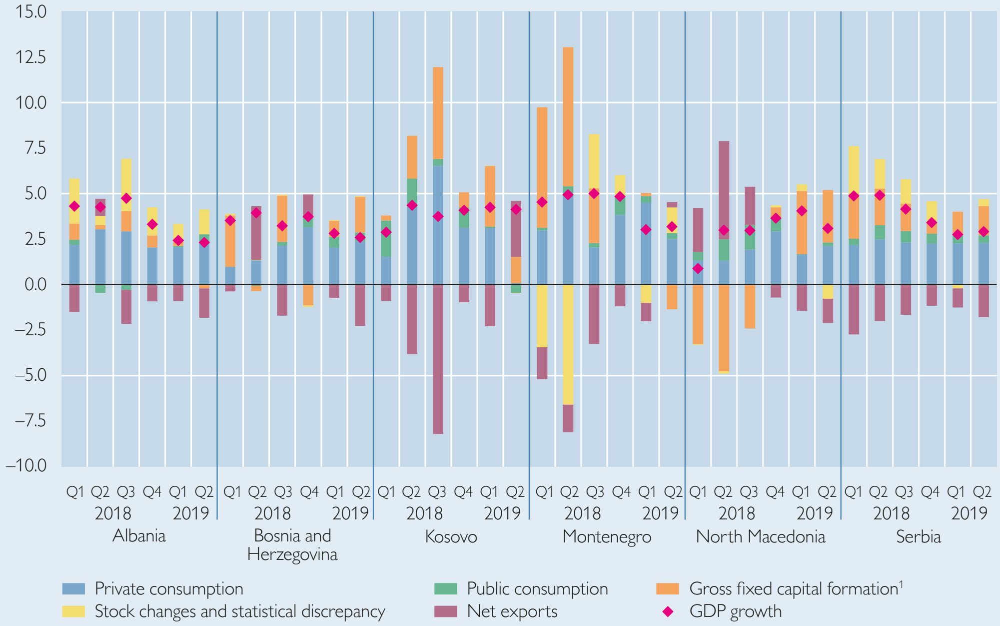
Overall, private consumption remained a dominant growth generator in the Western Balkans. It was supported by rising wages, perceptible labor market improvements, a stable inflow of remittances and a robust growth of credit to households. Remarkably, private consumption growth stagnated in Kosovo in the second quarter of 2019 after a more than 3% annual growth rate was recorded in the previous quarter. This slowdown was possibly due to higher food prices (see below) and elevated uncertainty before parliamentary snap elections in early October 2019.

[4] *The Western Balkans comprise the EU candidate countries Albania, Montenegro, North Macedonia and Serbia as well as the potential candidates 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.*

Chart 1

GDP growth slowed down in most Western Balkan countries in the first half of 2019

Percentage points, year-on-year GDP growth in %



Source: National statistical offices.

[1] Gross capital formation for Bosnia and Herzegovina, Kosovo, North Macedonia.

In the first half of 2019, public consumption growth was rather subdued in the Western Balkans. Kosovo even registered negative growth rates in the first half of 2019. In Albania, by contrast, public consumption accelerated quite strongly in the second quarter of 2019 (+4.4% annually), driven by higher public wages.

As to investment activity, the picture was more mixed. In Albania and Montenegro, gross fixed capital formation slumped in the first half of 2019 (in both countries, annual growth even turned negative in the second quarter of 2019) when compared to the previous year. The phasing out of large infrastructure projects (Trans Adriatic Pipeline in Albania, highway section in Montenegro) were the main factors behind the slowdown. In Serbia, the growth of gross fixed capital formation also weakened somewhat, but the momentum remained strong overall. In North Macedonia, gross capital formation continued to recover after investment activity was dragged down by a prolonged period of political uncertainty in 2017 and early 2018.

In the first half of 2019, export growth weakened in most Western Balkan countries compared to the full year of 2018 (and compared to the first half of 2018). Apart from an overall slowdown in global trade, Bosnia and Herzegovina was affected by the trade conflict[5] with Kosovo, which is an important trade destination for the country. In Albania, exports slumped due to low energy production. Despite some deceleration, Kosovo and North Macedonia still featured strong export growth rates in the first half of 2019. Import growth weakened considerably – due to falling infrastructure-related imports in Montenegro and, in Kosovo, possibly because of higher import prices (related to the imposed tariffs) and the overall weakening of private consumption growth. In Albania, lower imports for infrastructural purposes were largely compensated by a higher need to import energy as energy production was low in the first half of 2019. The growth contribution of net exports was negative in all Western Balkan countries

[5] *In November 2018, Kosovo imposed 100% tariffs on goods from Bosnia and Herzegovina, and from Serbia. These tariffs were introduced because the two countries do not recognize Kosovo's independence.*

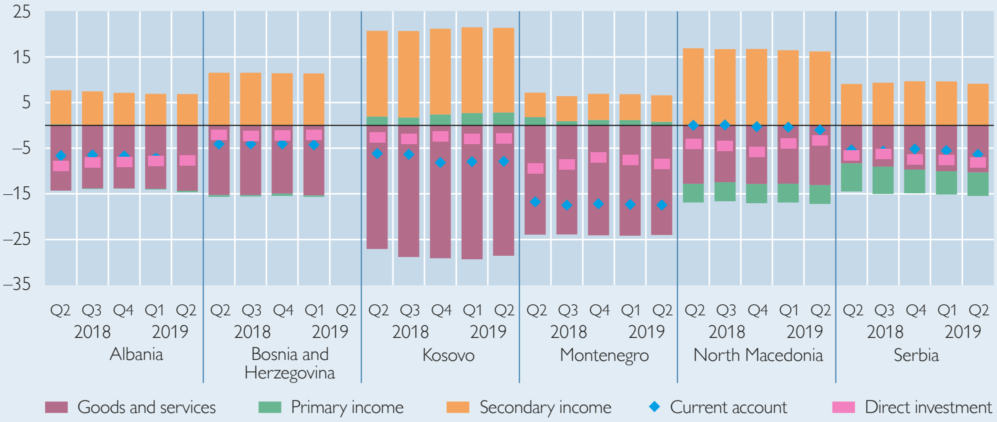
in the first quarter of 2019. In the second quarter of 2019, however, Kosovo and Montenegro registered a positive contribution of net exports.

Trade balances remained clearly negative, particularly in Kosovo and Montenegro, which recorded deficits of almost 30% and 24% of GDP, respectively, in the first half of 2019. External imbalances even widened in the Western Balkans in the first half of 2019 compared to the same period of 2018, largely on account of worsening merchandise trade balances. Remittances remained robust. In most Western Balkan countries, FDI inflows continued to finance a large part of the current account deficits.

Chart 2

Current account balances and FDI in the Western Balkans

% of GDP, four-quarter moving average



Source: National central banks, national statistical offices.

Note: A positive (negative) value in the category of direct investments indicates that the net acquisition of assets is higher (lower) than the net incurrence of liabilities.

Unemployment rates are strikingly high in most Western Balkan countries (particularly when compared to record-low unemployment rates in the CESEE EU Member States), ranging from around 10% in Serbia to 25% in Kosovo in the second quarter of 2019. It is worth noting that unemployment rates improved visibly across the region compared to the same period of 2018 – except in Montenegro, where it remained at 14.7%. Employment rates in the region increased as well, except in Kosovo, whose employment rate continues to hover around the low level of 29%. Wages (whole economy) increased robustly in most Western Balkan countries,[6] particularly in Serbia. Apart from overall robust economic growth, accelerating public wages or the raising of minimum wages supported overall wage growth. In Montenegro, by contrast, wages have stagnated more or less since early 2018, partly because government wages have remained unchanged. However, minimum wages in Montenegro were raised in spring, and wages grew marginally in the months thereafter.

Inflation has remained mostly low so far. Apart from country-specific factors, contained inflationary pressure was partly due to low imported inflation as a result of low inflation in the main trading partner countries. In Montenegro, for instance, inflation decelerated to 0.4% year on year in the first nine months of 2019 (with slightly negative inflation rates from June to September 2019), compared to 2.6% in 2018. In Bosnia and Herzegovina, inflation fell to 0.3% year on year in August 2019 (after 1.4% in 2018). In Albania, where inflation rates were below 2% in the first nine months of 2019, inflation remained below the target of 3% set by the Bank of Albania. In this case, low inflation was also related to the strong appreciation of the currency in nominal effective terms in 2018, which had a perceptible impact on inflation in the first half of 2019. The currency appreciation moderated in the first half of 2019 compared

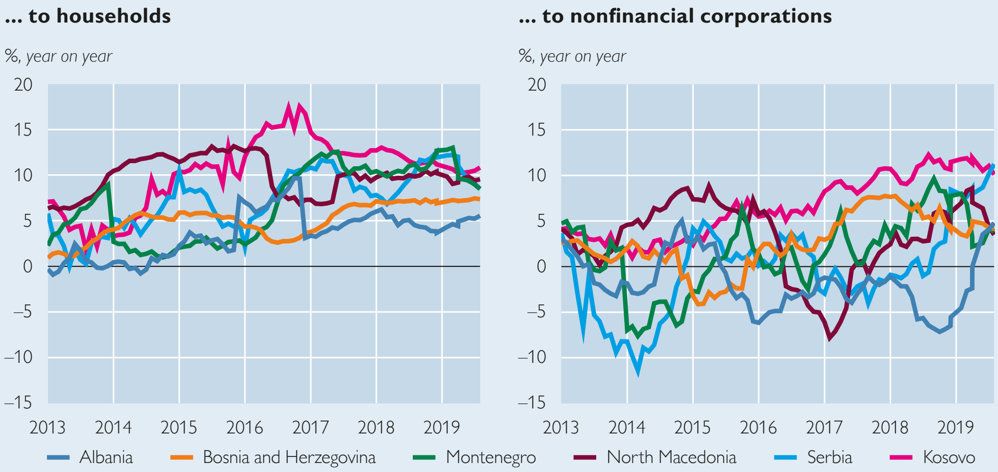
[6] *No comparable data are available for Kosovo.*

to developments recorded in 2018. In Serbia, the other inflation-targeting country in the region, inflation peaked in spring 2019 (April 2019: +3% year on year) but moved down to 1.1% year on year in September 2019. Against the background of limited inflationary pressure (the inflation target is set at 3% ±1.5 percentage point), the National Bank of Serbia (NBS) cut its key interest rate in two steps by 50 basis points to 2.5% over the summer of 2019. The Serbian dinar continued to be under appreciation pressure and the NBS intervened on the foreign exchange market to counteract the appreciation of the dinar against the euro. Kosovo, by contrast, featured rather elevated inflation rates (above 3% on average in the first seven months of 2019); this is related to the 100% tariffs imposed on goods from Bosnia and Herzegovina and from Serbia, which lifted food prices significantly.

Turning to credit developments, lending to the household sector generally remained strong in the present low interest rate environment. In Serbia, the growth of annual lending to households moderated visibly in June, July and August 2019. This might be connected to the write-offs related to the conversion of Swiss franc-denominated housing loans into euro loans. Additionally, the growth of cash loans slowed down, possibly due to regulatory changes that were already implemented at end-2018 with the aim to support sustainable lending for unsecured nonpurpose loans.[7,8] *Specifically, lending to the corporate sector accelerated strongly in Serbia in the first half of 2019 and grew by more than 10% year on year in July and August 2019. In Albania, lending to the corporate sector also recovered visibly. According to the Bank of Albania,*[9] *the lending activities of some banks have become more dynamic after some changes in bank ownership.*

Chart 3

Growth of credit



Source: IMF, national central banks.

The downward trend in nonperforming loans (NPLs) has continued since end-2018. Albania, the country with the highest NPL ratio in the Western Balkans, managed to bring its NPLs down to close to 11% of total loans in June 2019 from about 13% at the end of 2018. In June 2019, the other Western Balkan countries posted NPL ratios between 2.5% (Kosovo) and 7.2% (Bosnia and Herzegovina).

To bring down public debt and to ensure overall fiscal sustainability, the consolidation of public finances remains key in the Western Balkan countries. In 2018, public debt as a share of GDP was highest in Montenegro at 70.1%, followed by Albania with a rate of 67.9% and Serbia with 53.2%.

[7] *For more details on lending to the private sector for nonhousing purposes, see box 2 in Focus on European Economic Integration Q2/19.*

[8] *National Bank of Serbia. 2019. Trends in Lending. Second Quarter Report. September 2019.*

[9] *Bank of Albania. 2019. Monetary Policy Report. 2019/III.*

Moreover, reducing underspending for public investments remains a challenge to public finances in almost all Western Balkan countries. They also face risks related to contingent liabilities and have to address the large shadow economies. In October 2019, the Serbian authorities adopted an additional budget as government revenues were higher than expected. The extra budget mainly provides for additional spending for infrastructure projects (for roads in particular) and increasing public wages (on average, an annual increase by 9.6% is to become effective in November 2019) without changing the 2019 fiscal deficit target of 0.5% of GDP. Overall, better fiscal discipline and progress with regard to fiscal consolidation were an important motivation for Moody's to change Serbia's long-term foreign currency sovereign debt rating from stable to positive and for Fitch to revise its rating upward from BB to BB+ in September 2019.

Regarding the EU accession process, Albania and North Macedonia are still waiting to get the green light for opening accession negotiations with the European Commission. Albania has been an EU candidate country since 2014, North Macedonia since 2005. The European Commission would be ready to start accession negotiations as soon as possible. The decision, however, requires the unanimity of all EU Member States. Recently, at the European Council in mid-October 2019, the EU Member States failed to agree on opening accession talks with Albania and North Macedonia and postponed the decision on this issue to a later date. Turning to the relationship of this country group with the IMF, Bosnia and Herzegovina as well as Serbia have programs with the IMF. The IMF's EFF program with Bosnia and Herzegovina came to a standstill in 2018 due to the lacking reform process in the country. Serbia uses the IMF's Policy Coordination Instrument (PCI). In mid-October 2019, the IMF published its conclusions of the third review under the PCI. According to this review, Serbia's PCI program is broadly on track.

2 Slovakia: economic growth declines to lowest level in six years

Drivers of GDP growth rather volatile in the first half of 2019

Real economic growth in Slovakia hit the brakes and moderated from more than 4% in 2018 to 2.8% in the first half of 2019. The structure of growth was somewhat volatile. In the first quarter of 2019, the economy grew at a similar pace as at end-2018 and GDP growth was broadly balanced between domestic and foreign demand. In the second quarter of 2019, economic expansion slowed down significantly as the vigorous increase in the growth contribution of domestic demand was massively counteracted by net exports. While in the first quarter, exports benefited from the launch of new car production capacities and export growth outpaced import growth, exports contracted in the second quarter in the year-to-year comparison. Apart from base effects, this partly reflected weaker foreign demand and a significant drop of exports of petrochemical products as a result of a temporary closure of oil refinery facilities. By contrast, domestic demand maintained a relatively robust growth contribution primarily on the back of both public and private consumption. Both were boosted particularly by rising compensation of private and public employees. Yet, household consumption also profited from one-off factors such as the 2019 Ice Hockey World Championship, which was hosted by Slovakia in May. Nonetheless, despite continuously increasing disposable income, private consumption growth slowed down in the first semester of 2019 when compared to the previous year as households preferred to increase their saving rate. This possibly mirrors consumers' deteriorated confidence particularly with regard to the general economic situation and to unemployment. Fixed investment contracted in the second quarter of 2019, following a significant slowdown at the beginning of the year. Over the review period, gross fixed capital formation thus made a slightly negative contribution to growth due to moderated public investment and shrinking investment in the automotive sector. This echoed firms' reaction to discouraging signals about demand developments in trading partner countries. At the same time, it became more challenging for firms to sell their products, which brought about a significant build-up of stocks. As a result, additions to inventories became the single most important growth driver in Slovakia in the first half of 2019, adding 2.3 percentage points to GDP growth.

Due to the slowdown in economic growth, the downward trend the general government deficit showed during the last decade is expected to come to a halt in 2019. While the fiscal deficit should remain at broadly the same level as last year, public debt relative to GDP, however, is projected to go down by about 1 percentage point. This will be buttressed by a continued primary surplus and low interest payments relative to GDP growth.

Long-lasting positive labor market dynamics seem to moderate

While employment continued to rise in the first three months of 2019 mainly thanks to the service sector, employment growth came to a standstill in the second quarter in the wake of skilled labor shortages, slower economic growth and labor saving measures. The lower demand for labor in the first half of 2019 was mirrored also in a less dynamic downward trend in unemployment compared to the recent past. Nonetheless, wage growth remained robust both in the private and public sectors, reaching record levels. This was reflected again in a significant increase in ULC as wage dynamics outstripped increases in productivity by a wide margin. In the six months to June, inflation averaged 2.5% – the same price increase as in 2018. Inflation accelerated to about 3% in the third quarter, however, mainly reflecting price increases in housing, food and energy. Annual growth in loans to households moderated further in the period under review.

Table 2

Main economic indicators: Slovakia

	2016	2017	2018	Q1 18	Q2 18	Q3 18	Q4 18	Q1 19	Q2 19
	Year-on-year change of the period total in %								
GDP at constant prices	3.1	3.2	4.1	3.7	4.5	4.6	3.6	3.7	2.0
Private consumption	2.9	3.5	3.0	3.5	2.0	3.1	3.4	1.1	1.9
Public consumption	1.6	1.7	1.9	1.2	0.7	1.6	3.8	1.5	4.2
Gross fixed capital formation	–9.4	3.4	6.8	8.1	18.5	–5.7	9.0	2.1	–3.7
Exports of goods and services	5.5	5.9	4.8	1.3	7.6	5.6	4.7	7.2	–1.9
Imports of goods and services	3.4	5.3	5.3	1.1	6.6	5.4	7.8	6.4	0.8
	Contribution to GDP growth in percentage points								
Domestic demand	1.1	2.5	4.0	3.5	3.3	3.6	5.6	2.2	4.6
Net exports of goods and services	2.0	0.7	–0.3	0.2	1.2	0.3	–2.8	1.0	–2.6
Exports of goods and services	5.1	5.5	4.7	1.3	7.3	5.0	4.7	7.3	–1.9
Imports of goods and services	–3.1	–4.8	–5.0	–1.1	–6.1	–4.7	–7.5	–6.3	–0.7
	Year-on-year change of the period average in %								
Unit labor costs in the whole economy (nominal, per person)	1.3	4.2	3.4	3.9	3.2	2.6	3.7	4.4	7.8
Unit labor costs in manufacturing (nominal, per hour)	2.8	6.6	3.6	7.8	5.6	0.4	1.4	1.7	3.8
Labor productivity in manufacturing (real, per hour)	1.4	0.9	4.8	0.6	4.9	7.1	6.4	7.5	2.8
Labor costs in manufacturing (nominal, per hour)	4.2	7.5	8.6	8.4	10.7	7.6	7.9	9.3	6.7
Producer price index (PPI) in industry	–3.9	2.5	2.4	0.9	1.6	3.6	3.6	2.7	2.9
Consumer price index (here: HICP)	–0.5	1.4	2.5	2.4	2.9	2.7	2.1	2.4	2.6
	Period average levels								
Unemployment rate (ILO definition, %, 15–64 years)	9.7	8.2	6.6	7.2	6.7	6.4	6.1	5.9	5.8
Employment rate (%, 15–64 years)	64.9	66.2	67.6	67.1	67.1	67.9	68.2	68.6	68.1
Key interest rate per annum (%)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
	Nominal year-on-year change in the period-end stock in %								
Loans to the domestic nonbank private sector[1]	10.3	10.2	8.4	9.9	9.9	9.4	8.4	7.5	6.2
of which: loans to households	13.4	11.8	11.3	12.4	12.3	12.0	11.3	9.5	8.5
loans to nonbank corporations	5.4	7.6	3.4	5.6	5.9	5.0	3.4	3.9	2.1
	%								
Share of foreign currency loans in total loans to the nonbank private sector	0.4	0.2	0.1	0.2	0.2	0.2	0.1	0.2	0.1
Return on assets (banking sector)	1.1	0.8	0.8	0.9	0.9	0.9	0.8	0.8	0.9
Tier 1 capital ratio (banking sector)	16.2	16.6	16.6	16.4	16.3	16.7	16.6	16.7	16.8
NPL ratio (banking sector)	4.3	3.6	3.0	3.5	3.4	3.4	3.0	2.9	2.8
	% of GDP								
General government revenues	39.2	39.4	39.9	..	..	..	..	..	..
General government expenditures	41.5	40.2	40.6	..	..	..	..	..	..
General government balance	–2.2	–0.8	–0.7	..	..	..	..	..	..
Primary balance	–0.7	0.6	0.6	..	..	..	..	..	..
Gross public debt	51.8	50.9	48.9	..	..	..	..	..	..
	% of GDP								
Debt of nonfinancial corporations (nonconsolidated)	55.6	59.6	53.8	..	..	..	..	..	..
Debt of households and NPISHs[2] (nonconsolidated)	38.2	40.8	42.2	..	..	..	..	..	..
	% of GDP (based on EUR), period total								
Goods balance	2.0	0.8	0.1	1.2	2.0	–1.3	–1.5	2.7	–0.6
Services balance	0.6	1.0	0.9	0.8	1.1	1.3	0.2	0.8	1.6
Primary income	–3.1	–2.3	–2.0	–1.3	–2.0	–2.2	–2.5	–1.1	–2.3
Secondary income	–1.7	–1.5	–1.4	–1.4	–2.4	–0.9	–0.8	–1.9	–1.3
Current account balance	–2.2	–2.0	–2.5	–0.7	–1.4	–3.1	–4.6	0.5	–2.6
Capital account balance	2.0	0.9	1.6	0.4	1.9	0.9	3.2	0.2	1.3
Foreign direct investment (net)[3]	–0.8	–2.0	–0.2	–1.2	2.3	–1.3	–0.7	–0.5	1.0
	% of GDP (rolling four-quarter GDP, based on EUR), end of period								
Gross external debt	92.2	111.0	113.0	108.1	109.6	109.7	113.0	109.6	111.7
Gross official reserves (excluding gold)	2.0	2.3	3.8	2.8	3.2	3.5	3.8	4.3	4.8
	Months of imports of goods and services								
Gross official reserves (excluding gold)	0.3	0.3	0.5	0.4	0.4	0.4	0.5	0.5	0.6
	EUR million, period total								
GDP at current prices	81,226	84,851	90,202	20,425	22,653	23,799	23,325	21,794	23,719

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).

3 Slovenia: wage growth feeding through to inflation despite moderating output growth

GDP growth notably weaker in the first half of 2019

Output growth in Slovenia moderated notably during the first half of 2019, primarily as a result of slackening domestic demand, while the growth contribution of net real exports remained slightly negative. The dynamics of private consumption eased despite accelerating real wage growth, mirroring the slowing expansion of employment, some deterioration in consumer confidence, a modest increase in households' savings rate and a slight decline in household credit growth. Government consumption slowed from an outstandingly high base in 2018. Investment activity eased as well, driven by slowing investments in machinery and equipment along with declining capacity utilization, which was not counterbalanced by strengthening construction investments. Continued contraction in corporate credit and worsening economic sentiment along with a sharp deterioration in export expectations may have played a role here. So far, however, export growth accelerated during the first half of 2019, but as import growth strengthened similarly, the contribution of net real exports remained slightly negative like in 2018.

Budget on course toward MTO, but long-term sustainability issues still unresolved

According to the European Commission's 2019 Spring Economic Forecast, the general government surplus is expected to come to 0.7% of GDP in 2019 and to rise to 0.9% in 2020. However, as budgetary developments benefit strongly from economic strength, the structural balance is negative and is expected to deteriorate slightly in 2019, mainly on the back of higher wage costs and public investments. The European Commission expects the projected decrease in the output gap to bring about a decline in the structural deficit in 2020, close to the country's medium-term objective (MTO) (–0.25% of GDP). As a result, in its June 2019 assessment, the European Council saw Slovenia at risk of some deviation from its medium-term budgetary objective and called on the authorities to stand ready to take further measures. In addition, the European Council urged the adoption and implementation of pension, health and long-term care reforms as well as improvements in the employability of low-skilled and older workers and in the business environment.

Wage growth feeding through to inflation

HICP inflation increased from a temporary low of 1.2–1.3% at the beginning of 2019 to 2.4% by August. This acceleration was in stark contrast to average euro area developments, so that the inflation gap between Slovenia and the euro area rose from a negative 0.2 percentage points in January and February 2019 to a positive 1.4 percentage points by August. The rise in headline inflation during the reporting period mainly reflected an increase in core inflation. This increase, in turn, was attributable to both processed food and nonenergy industrial goods prices, but mostly to services prices. This may be the first indication that the rapid rise of ULC since early 2018 has finally begun to feed through to prices.

Living up to its obligations, the government sold a final 10% of the country's largest bank, Nova Ljubljanska banka (NLB), to institutional investors in June 2019. At the same time, it also privatized the third-largest bank, Abanka, by selling it to the second-largest bank, Nova Kreditna Banka Maribor (NKBM), giving them a combined market size of almost that of NLB (around 23%). In a pathbreaking ruling, a Slovene appellate court at end-August 2019 ordered Abanka to fully compensate former owners of subordinated bonds which had been scrapped during the bank restructuring of 2013/2014. According to the court, the Abanka had not fully informed its clients about possible adverse consequences of purchasing subordinated debt. The ruling could serve as a precedence for other holders of erased subordinated debt, which totals around EUR 600 million.

Table 3

Main economic indicators: Slovenia

	2016	2017	2018	Q1 18	Q2 18	Q3 18	Q4 18	Q1 19	Q2 19
	Year-on-year change of the period total in %								
GDP at constant prices	3.1	4.8	4.1	4.3	3.7	4.6	3.8	3.3	2.5
Private consumption	4.4	2.3	3.4	4.0	3.3	2.3	4.1	2.3	3.3
Public consumption	2.5	0.3	3.2	2.4	3.1	3.2	4.0	3.9	1.0
Gross fixed capital formation	–3.7	10.4	9.4	9.9	9.1	11.9	7.1	10.0	6.9
Exports of goods and services	6.5	10.8	6.6	7.7	8.2	4.2	6.5	7.9	9.4
Imports of goods and services	6.7	10.7	7.7	9.4	8.4	4.8	8.2	7.7	12.3
	Contribution to GDP growth in percentage points								
Domestic demand	2.7	3.8	4.3	4.9	3.1	4.6	4.7	2.5	3.8
Net exports of goods and services	0.4	1.0	–0.2	–0.6	0.6	0.0	–0.8	0.8	–1.3
Exports of goods and services	5.0	8.4	5.5	6.4	6.7	3.6	5.4	6.8	8.0
Imports of goods and services	–4.6	–7.4	–5.7	–6.9	–6.1	–3.6	–6.2	–6.0	–9.3
	Year-on-year change of the period average in %								
Unit labor costs in the whole economy (nominal, per person)	1.8	1.2	3.0	3.2	3.9	1.7	3.1	3.8	5.8
Unit labor costs in manufacturing (nominal, per hour)	–6.3	–2.7	–2.2	–2.5	–5.7	–3.1	2.4	1.5	0.2
Labor productivity in manufacturing (real, per hour)	9.4	9.6	6.0	9.4	8.2	4.6	2.3	5.3	4.3
Labor costs in manufacturing (nominal, per hour)	2.5	6.7	3.6	6.7	2.0	1.3	4.7	6.9	4.5
Producer price index (PPI) in industry	–1.4	2.2	2.1	2.2	2.1	2.4	1.6	1.1	0.8
Consumer price index (here: HICP)	–0.2	1.6	1.9	1.5	2.1	2.1	2.0	1.3	1.7
	Period average levels								
Unemployment rate (ILO definition, %, 15–64 years)	8.1	6.7	5.2	6.0	5.3	5.1	4.4	4.9	4.3
Employment rate (%, 15–64 years)	65.9	69.3	71.1	69.7	71.1	71.9	71.8	71.3	72.5
Key interest rate per annum (%)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
	Nominal year-on-year change in the period-end stock in %								
Loans to the domestic nonbank private sector[1]	–2.4	4.9	1.9	4.6	3.6	2.2	1.9	2.8	3.6
of which: loans to households	3.3	6.8	6.4	6.5	6.5	6.5	6.4	6.3	5.9
loans to nonbank corporations	–7.0	3.1	–2.2	2.9	0.9	–1.7	–2.2	–0.6	1.4
	%								
Share of foreign currency loans in total loans to the non-bank private sector	3.2	2.4	2.0	2.3	2.2	2.1	2.0	1.9	1.8
Return on assets (banking sector)	0.9	1.1	1.3	1.4	1.5	1.3	1.3	1.3	1.8
Tier 1 capital ratio (banking sector)	20.2	19.4	19.4	19.8	20.2	19.4	19.4	..	..
NPL ratio (banking sector)	5.5	3.7	2.3	3.2	2.9	2.7	2.3	2.0	1.5
	% of GDP								
General government revenues	43.4	43.2	43.1	..	..	..	..	..	..
General government expenditures	45.3	43.2	42.4	..	..	..	..	..	..
General government balance	–1.9	0.0	0.7	..	..	..	..	..	..
Primary balance	1.1	2.5	2.7	..	..	..	..	..	..
Gross public debt	78.7	74.1	70.1	..	..	..	..	..	..
	% of GDP								
Debt of nonfinancial corporations (nonconsolidated)	60.9	55.4	51.4	..	..	..	..	..	..
Debt of households and NPISHs[2] (nonconsolidated)	27.3	27.2	27.0	..	..	..	..	..	..
	% of GDP (based on EUR), period total								
Goods balance	3.8	3.7	2.5	3.1	3.7	3.1	0.0	3.4	1.5
Services balance	4.8	5.2	5.9	5.0	5.6	6.8	5.9	5.3	6.4
Primary income	–2.8	–2.1	–1.8	–0.3	–2.6	–2.2	–1.9	–0.8	–1.7
Secondary income	–0.9	–0.7	–0.9	–1.3	–0.6	–1.0	–0.6	–2.1	–0.9
Current account balance	4.8	6.1	5.7	6.6	6.1	6.8	3.4	5.8	5.3
Capital account balance	–0.8	–0.8	–0.5	–0.4	–0.3	–0.2	–1.0	–0.2	–0.2
Foreign direct investment (net)[3]	–2.1	–1.2	–2.0	–0.2	–2.0	–3.9	–1.8	–3.8	–1.1
	% of GDP (rolling four-quarter GDP, based on EUR), end of period								
Gross external debt	109.7	100.5	92.0	98.0	96.7	93.0	92.0	91.5	93.0
Gross official reserves (excluding gold)	1.5	1.5	1.5	1.4	1.4	1.5	1.5	1.6	1.7
	Months of imports of goods and services								
Gross official reserves (excluding gold)	0.3	0.2	0.2	0.2	0.2	0.2	0.2	0.2	0.3
	EUR million, period total								
GDP at current prices	40,367	42,987	45,755	10,564	11,509	11,812	11,871	11,169	12,124

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).

4 Bulgaria: strong exports counterbalance slowing domestic demand

Strong turnaround of growth engines, largely due to one-off factors

GDP growth in Bulgaria was unexpectedly strong in the review period (with the annual growth rate coming to 4.2% in the first half of 2019) as exports performed surprisingly well despite unfavorable economic conditions in important export destinations (recession in Turkey, slowdown in the euro area). A major contribution to overall export growth came from mineral products, fuels and metals and was largely due to a base effect as a key sector company significantly cut production in 2018 due to the refurbishment of production capacities.

Domestic demand, by contrast, slowed remarkably in the review period compared to previous years. The considerable deceleration of gross fixed capital formation went hand in hand with a decline in industrial production (excluding construction) in the second quarter of 2019, some deceleration of lending to enterprises as well as some deterioration in capacity utilization. On the other hand, the first half of the year also saw a notable revival in the construction sector, which had stagnated in 2018. The slowdown in private consumption was accompanied by worsened consumer sentiment indicators, a slowdown in retail sales, an increase in household deposits and some deceleration in lending to households. Employment and unemployment rates, though, are still at historical best levels and annual real wage growth returned from about 5% in 2018 to more than 9% in the first half of 2019.

Consumer price pressure alleviated somewhat, reaching an annual HICP inflation rate of 2.5% in August. Inflation can be nearly fully explained by rising prices of processed food and services, while lower energy prices have negatively contributed to inflation. It should be noted that the average HICP inflation rate over the period from September 2018 to August 2019 is considerably higher (by about 2 percentage points) in Bulgaria than in the three EU countries that recorded the lowest inflation rates over this period.

Government consumption remained strong, especially in the first quarter, on the back of the realized 10% increase in public sector wages as well as rising pension, social and healthcare expenditure. However, considerable extra defense spending for the acquisition of fighter aircraft could jeopardize the targets of the national fiscal rules this year. Compared to the originally planned general government budget deficit of 0.5% of GDP, under conservative revenue assumptions this extra spending could bring public expenditures and the budget deficit close to, or above, the respective ceilings of 40% and 2% of GDP according to the Bulgarian Fiscal Council.

ECB's comprehensive assessment revealed capital shortfalls at two larger banks

In July 2019, the ECB concluded the comprehensive assessment of the six largest Bulgarian banks, revealing for two of them capital shortfalls that must be tackled before the country's entry into ERM II and the banking union. As of end-June, First Investment Bank stressed that it had already secured half of the required additional capital through provisioning and Investbank referred to the reclassification of problematic exposures and the optimization of risk-weighted assets. Meanwhile, the Bulgarian authorities have implemented most of the policy measures listed in the Action Plan to Join the ERM II. As of end-September, besides the update of secondary legislation required for participating in the banking union (i.e. the periodic adoption of EBA guidelines), only the adoption of a law to modernize the governance of state-owned enterprises in line with OECD guidelines was still pending. Last but not least the European Commission's assessment of progress made under the Cooperation and Verification Mechanism, which is to be released in mid-November 2019, will be decisive for Bulgaria's ERM II accession path.

Table 4

Main economic indicators: Bulgaria

	2016	2017	2018	Q1 18	Q2 18	Q3 18	Q4 18	Q1 19	Q2 19
	Year-on-year change of the period total in %								
GDP at constant prices	3.9	3.8	3.1	3.5	3.2	2.7	3.0	4.8	3.7
Private consumption	3.6	4.5	6.4	7.1	8.6	8.1	2.5	2.6	0.5
Public consumption	2.2	3.7	4.7	2.4	4.0	5.2	6.8	8.3	2.7
Gross fixed capital formation	–6.6	3.2	6.5	10.9	7.0	3.0	6.7	0.6	1.3
Exports of goods and services	8.1	5.8	–0.8	1.1	–2.3	–3.2	2.2	6.9	2.1
Imports of goods and services	4.5	7.5	3.7	4.6	4.9	3.8	1.6	4.8	–4.0
	Contribution to GDP growth in percentage points								
Domestic demand	1.6	4.6	5.9	6.3	8.0	6.9	2.8	3.6	–0.2
Net exports of goods and services	2.3	–0.8	–2.8	–2.6	–4.8	–4.6	0.3	1.2	3.9
Exports of goods and services	5.2	3.7	–0.5	0.8	–1.6	–2.3	1.3	4.7	1.3
Imports of goods and services	–2.9	–4.5	–2.3	–3.4	–3.2	–2.2	–0.9	–3.5	2.6
	Year-on-year change of the period average in %								
Unit labor costs in the whole economy (nominal, per person)	2.5	8.1	2.4	3.3	2.3	1.4	2.4	6.3	7.7
Unit labor costs in manufacturing (nominal, per hour)	6.5	1.1	6.9	6.9	8.5	5.8	6.5	2.3	6.5
Labor productivity in manufacturing (real, per hour)	2.9	11.0	2.6	3.3	1.8	4.5	1.0	9.2	3.4
Labor costs in manufacturing (nominal, per hour)	9.6	12.2	9.7	10.4	10.5	10.6	7.6	11.7	10.0
Producer price index (PPI) in industry	–3.1	4.9	4.0	3.1	5.1	4.1	3.5	3.3	2.7
Consumer price index (here: HICP)	–1.3	1.2	2.6	1.6	2.4	3.6	3.0	2.5	2.8
EUR per 1 BGN, + = BGN appreciation	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
	Period average levels								
Unemployment rate (ILO definition, %, 15–64 years)	7.7	6.3	5.3	5.8	5.5	5.0	4.7	5.1	4.2
Employment rate (%, 15–64 years)	63.4	66.9	67.7	66.5	67.9	68.8	67.7	68.3	70.7
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
	Nominal year-on-year change in the period-end stock in %								
Loans to the domestic nonbank private sector[2]	1.6	4.8	8.3	5.6	6.8	7.3	8.3	7.9	6.9
of which: loans to households	2.0	6.1	11.2	6.4	9.2	9.7	11.2	11.0	8.1
loans to nonbank corporations	1.3	4.1	6.6	5.1	5.4	5.9	6.6	6.1	6.2
	%								
Share of foreign currency loans in total loans to the non-bank private sector	44.4	37.9	34.9	37.0	36.3	35.6	34.9	34.1	33.5
Return on assets (banking sector)	1.4	1.2	1.7	1.1	1.6	1.6	1.7	1.2	1.7
Tier 1 capital ratio (banking sector)	20.9	20.9	19.4	19.8	19.7	19.0	19.4	18.3	19.7
NPL ratio (banking sector)	9.0	6.9	5.1	6.6	6.6	6.1	5.1	4.9	4.8
	% of GDP								
General government revenues	35.2	36.2	36.8	..	..	..	..	..	..
General government expenditures	35.1	35.0	34.8	..	..	..	..	..	..
General government balance	0.1	1.2	2.0	..	..	..	..	..	..
Primary balance	1.0	2.0	2.7	..	..	..	..	..	..
Gross public debt	29.6	25.6	22.6	..	..	..	..	..	..
	% of GDP								
Debt of nonfinancial corporations (nonconsolidated)	91.4	86.3	81.7	..	..	..	..	..	..
Debt of households and NPISHs[3] (nonconsolidated)	23.2	22.9	23.4	..	..	..	..	..	..
	% of GDP (based on EUR), period total								
Goods balance	–2.1	–1.5	–4.1	–5.6	–5.2	–1.7	–4.4	–2.7	–1.1
Services balance	6.4	5.5	6.2	2.7	5.5	12.8	2.7	3.4	6.2
Primary income	–5.0	–4.6	–1.0	–1.7	–1.5	–0.8	–0.3	–0.5	–0.1
Secondary income	3.3	3.6	3.5	4.7	3.1	4.5	2.2	4.3	4.7
Current account balance	2.6	3.1	4.6	0.1	1.9	14.8	0.2	4.6	9.7
Capital account balance	2.2	1.0	1.1	0.0	1.4	1.6	1.0	1.5	1.6
Foreign direct investment (net)[4]	–1.3	–3.9	–2.6	0.6	–0.3	–3.3	–6.1	0.1	–2.3
	% of GDP (rolling four-quarter GDP, based on EUR), end of period								
Gross external debt	79.3	72.6	66.7	71.3	70.8	69.8	66.7	66.3	64.7
Gross official reserves (excluding gold)	46.7	43.1	42.8	40.5	41.6	42.7	42.8	41.6	40.7
	Months of imports of goods and services								
Gross official reserves (excluding gold)	9.4	8.2	8.2	7.7	7.9	8.1	8.2	8.0	8.1
	EUR million, period total								
GDP at current prices	48,129	51,663	55,182	11,240	13,451	15,248	15,243	12,607	14,883

Source: Bloomberg, European Commission, Eurostat, national statistical offices, national central banks, wiiw, 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: stronger economic growth as investment growth accelerates

Higher EU fund absorption supports investment growth

Croatian GDP growth was higher than expected in the first half of 2019 (3.1% year on year), largely as a result of higher investment growth. Investment growth accelerated almost to double digits and was most likely driven by EU funds. Investments contributed roughly as much to overall growth as private consumption. The latter was supported by various factors: From January 1, 2019, several changes to personal income tax legislation became effective, public sector salaries were increased and the scope of reduced VAT rates was extended. The growth of loans to households accelerated in the first half of 2019, supported by lower financing costs and strong demand. Labor market trends were favorable and the (seasonally adjusted) unemployment rate declined mildly to 6.9% in August 2019.

Industrial sector weak, construction sector booming

The negative contribution of net exports to growth, which was already substantial, increased further. Export growth was sluggish in the first half of 2019, while imports grew dynamically, driven by strong domestic demand. Global factors, such as headwinds to international trade and the resulting weakness of manufacturing across Europe, likely had a negative effect on exports as did the industrial sector and the manufacturing sector in particular. The latter contracted in the second quarter, leading to an overall weak performance in the first half. The construction sector, on the other hand, grew by double digits. Tourist arrivals and overnight stays continued to grow at a moderate pace in the first eight months of 2019, contributing to solid growth in the sectors of wholesale and retail trade, transportation, storage, accommodation and food service activities. Both the tourism and construction sectors reported labor shortages, leading to a rise in the number of work permits granted to foreigners in June 2019.

Debt reduction temporarily stalled, fiscal stance still prudent

For 2019, the Croatian government expects a budget deficit of 0.3% of GDP after a surplus of 0.2% of GDP in 2018. The projected deterioration in the budget balance stems from higher expected expenditures on investments, and, to a lesser extent, subsidies and intermediate consumption. In the first quarter of 2019, budget revenues and expenditures both grew by roughly 7.5% year on year. Uljanik Group, one of Croatia's largest shipbuilding companies, was declared bankrupt and further state guarantees were activated during 2019 but, overall, fiscal risks remain low. The general government debt-to-GDP ratio stood at 74.5% in March 2019, roughly unchanged compared to end-2018. In preparation for euro adoption, the government will sell its minority stakes (<15%) in at least 90 companies in three waves by mid-2020.

Five Croatian banks to be subject to ECB's comprehensive assessment

Headline HICP inflation was 0.6% year on year in Croatia in August 2019, while core inflation came to 0.8%. The Croatian central bank (HNB) intervened in the foreign exchange market to alleviate appreciation pressures, purchasing a total of EUR 1 billion from the Croatian banking sector in February and August. Although the HNB partially offset its foreign currency operations with the Ministry of Finance, its gross international reserves continued to increase and stood at EUR 19.9 billion at end-July 2019. Banking sector claims on the private sector increased only moderately in the first half of 2019, as corporate lending growth contracted due to NPL sales and the activation of shipbuilding guarantees. The profitability and capitalization of the Croatian banking sector increased mildly from already high levels in the first half of 2019. As part of the process of establishing close cooperation with the ECB, five Croatian banks are currently undergoing an ECB comprehensive assessment. Results are expected for mid-2020.

Table 5

Main economic indicators: Croatia

	2016	2017	2018	Q1 18	Q2 18	Q3 18	Q4 18	Q1 19	Q2 19
	Year-on-year change of the period total in %								
GDP at constant prices	3.5	2.9	2.6	2.5	2.9	2.8	2.3	3.9	2.4
Private consumption	3.5	3.6	3.5	3.9	3.6	2.7	3.9	4.3	2.7
Public consumption	0.7	2.7	2.9	2.8	2.5	3.9	2.3	3.1	3.9
Gross fixed capital formation	6.5	3.8	4.1	3.6	3.1	3.7	6.1	11.5	8.2
Exports of goods and services	5.6	6.4	2.8	–0.5	5.6	3.7	1.3	4.6	1.3
Imports of goods and services	6.2	8.1	5.5	5.5	4.7	5.1	6.6	7.7	6.7
	Contribution to GDP growth in percentage points								
Domestic demand	3.7	3.5	3.8	5.9	2.8	2.1	5.0	6.2	5.2
Net exports of goods and services	–0.1	–0.6	–1.2	–3.1	0.2	0.2	–2.7	–2.2	–2.8
Exports of goods and services	2.7	3.1	1.5	–0.2	2.6	2.5	0.6	1.9	0.6
Imports of goods and services	–2.8	–3.7	–2.7	–2.9	–2.3	–2.3	–3.2	–4.0	–3.4
	Year-on-year change of the period average in %								
Unit labor costs in the whole economy (nominal, per person)	..	..	..	..	..	..	..	..	..
Unit labor costs in manufacturing (nominal, per hour)	–15.1	1.6	6.7	3.7	8.4	6.8	8.1	–1.3	3.5
Labor productivity in manufacturing (real, per hour)	7.0	3.5	2.2	2.5	3.7	1.5	1.1	8.2	–1.5
Labor costs in manufacturing (nominal, per hour)	–8.7	5.1	9.1	6.2	12.4	8.4	9.2	6.8	2.0
Producer price index (PPI) in industry	–4.3	2.0	2.2	1.1	2.5	3.8	1.6	1.4	1.6
Consumer price index (here: HICP)	–0.6	1.3	1.6	1.1	1.8	2.0	1.3	0.8	0.8
EUR per 1 HRK, + = HRK appreciation	1.1	0.9	0.6	0.4	0.4	0.1	1.5	0.2	–0.3
	Period average levels								
Unemployment rate (ILO definition, %, 15–64 years)	13.3	11.3	8.6	10.5	7.7	7.4	8.7	7.6	6.2
Employment rate (%, 15–64 years)	56.9	58.9	60.7	59.0	61.1	61.9	60.6	61.2	61.8
Key interest rate per annum (%)	..	..	..	..	..	..	..	..	..
HRK per 1 EUR	7.5	7.5	7.4	7.4	7.4	7.4	7.4	7.4	7.4
	Nominal year-on-year change in the period-end stock in %								
Loans to the domestic nonbank private sector[1]	–3.8	0.6	2.4	0.0	2.2	1.8	2.4	3.5	2.8
of which: loans to households	–4.6	2.2	4.7	2.3	4.0	4.3	4.7	5.9	6.0
loans to nonbank corporations	–2.6	–1.6	–0.8	–3.0	–0.3	–1.4	–0.8	0.2	–1.6
	%								
Share of foreign currency loans in total loans to the nonbank private sector	60.1	56.9	54.7	56.1	55.5	55.5	54.7	54.4	53.0
Return on assets (banking sector)	1.3	0.9	1.2	1.4	1.5	1.5	1.2	1.3	1.5
Tier 1 capital ratio (banking sector)	21.3	22.3	22.1	21.6	21.4	21.1	22.1	21.6	22.0
NPL ratio (banking sector)	13.8	11.3	9.8	11.4	11.2	10.3	9.8	9.5	9.2
	% of GDP								
General government revenues	46.3	46.1	46.6	..	..	..	..	..	..
General government expenditures	47.3	45.3	46.4	..	..	..	..	..	..
General government balance	–1.0	0.8	0.2	..	..	..	..	..	..
Primary balance	2.1	3.5	2.5	..	..	..	..	..	..
Gross public debt	80.5	77.8	74.6	..	..	..	..	..	..
	% of GDP								
Debt of nonfinancial corporations (nonconsolidated)	96.3	94.9	93.1	..	..	..	..	..	..
Debt of households and NPISHs[2] (nonconsolidated)	35.0	34.2	34.1	..	..	..	..	..	..
	% of GDP (based on EUR), period total								
Goods balance	–16.3	–17.2	–18.7	–21.6	–19.0	–16.5	–18.4	–21.5	–22.0
Services balance	17.5	17.9	17.9	3.0	15.5	42.4	5.9	1.6	15.9
Primary income	–3.0	–1.5	–1.5	–1.6	–1.8	–2.6	0.3	–1.4	–2.6
Secondary income	3.9	4.2	4.2	4.1	4.4	3.1	5.3	3.6	4.9
Current account balance	2.1	3.4	1.9	–16.1	–0.9	26.4	–6.8	–17.6	–3.8
Capital account balance	1.3	1.0	1.3	0.9	1.4	1.0	2.0	1.5	2.5
Foreign direct investment (net)[3]	–4.3	–2.3	–1.4	–3.8	–3.3	0.3	0.6	–2.9	0.9
	% of GDP (rolling four-quarter GDP, based on EUR), end of period								
Gross external debt	95.8	89.2	83.0	89.6	87.9	84.4	83.0	83.8	84.7
Gross official reserves (excluding gold)	29.0	32.1	33.9	33.3	33.3	32.7	33.9	35.2	37.8
	Months of imports of goods and services								
Gross official reserves (excluding gold)	7.5	7.8	7.9	8.0	7.9	7.7	7.9	8.1	8.6
	EUR million, period total								
GDP at current prices	46,656	48,999	51,473	11,297	13,004	14,414	12,758	11,943	13,470

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).

6 Czech Republic: steady though slower economic growth, still driven by domestic demand

Declining investments, in particular, bring GDP growth down to potential

Real GDP growth in the Czech Republic has been gradually losing momentum since 2017, averaging some 2.5% in the first half of 2019. As a consequence, the positive output gap has been closed. Economic growth in the six months to June 2019 was again driven predominantly by domestic demand even though it lost some steam. Despite a slight deceleration, household consumption growth remained solid on the back of rising disposable income. The latter was spurred by an extraordinary hike in pensions far beyond the statutory indexation on the one hand and by rising wages on the other. Fast wage growth in the government sector also kept public consumption afloat. Growth in disposable income has been outpacing growth in private consumption since early 2018, thus lifting households' savings. This might reflect a downward trend in consumer confidence between mid-2018 and mid-2019 mainly on the back of households' rising concerns about the economic situation. However, as these worries have faded more recently, consumer confidence has begun to recover. The slowdown in GDP growth in the first half of 2019 is mostly ascribable to the significant cooling-down in fixed investment. This was partly due to base effects and partly reflected weakened foreign demand both owing to one-off factors (mainly in the automotive industry) and cyclical reasons. Weaker foreign demand is mirrored also in a significant deceleration in export growth. However, as import growth slowed down even faster, the contribution of net exports to GDP expansion turned slightly positive.

After the current account surplus had nearly vanished in 2018, it increased again in the first half of 2019 as a result of a higher surplus of the trade balance as well as a weaker outflow of dividends in the primary income balance. The fiscal surplus recorded in 2018 is projected to drop markedly. The revenue side will be negatively affected by slower economic growth and some one-off factors. At the same time, expenditures will be lifted by continued strong wage growth in the public sector, higher social transfers and government investment. Gross public debt is expected to go down by another 2 percentage points of GDP by the end of this year.

Administered prices and food prices push inflation temporarily above target

Labor markets seem to be cooling off somewhat as employment growth leveled off in the first two quarters of 2019. The unemployment rate continued to fall (to a historical low of 1.9% in the second quarter of 2019), but the decline appears to be coming to a halt. Nonetheless, labor market bottlenecks coupled with a minimum wage hike (by more than 9%) at the beginning of 2019 kept driving buoyant wage growth throughout the economy, particularly in nonmarket professions (e.g. teachers and other public employees). As a result of strong wage dynamics and consumer demand, inflation has accelerated beyond the Czech National Bank's (CNB) target (2% ±1 percentage point). Inflation thus averaged 2.4% in the first eight months of the year, driven by core components as well as faster growth in noncore administered and food prices. While the CNB assesses its monetary policy as "slightly easier than optimal," the monetary authorities expect headline inflation to gradually converge to the target by the second half of 2020. Against the background of slightly higher-than-projected inflation, the CNB proceeded with another hike of its key policy rate by 25 basis points to 2% in early May. While this policy decision was unanimous, a further monetary tightening currently does not seem likely as a vast majority of CNB board members have since been in favor of leaving rates unchanged.

Table 6

Main economic indicators: Czech Republic

	2016	2017	2018	Q1 18	Q2 18	Q3 18	Q4 18	Q1 19	Q2 19
	Year-on-year change of the period total in %								
GDP at constant prices	2.5	4.4	3.0	3.6	2.7	2.5	3.1	2.8	2.5
Private consumption	3.6	4.3	3.4	4.1	3.7	3.1	2.7	2.9	2.6
Public consumption	2.7	1.3	3.9	3.5	3.4	5.1	3.8	2.8	3.4
Gross fixed capital formation	–3.1	3.7	7.2	6.4	7.2	7.7	7.2	3.0	0.2
Exports of goods and services	4.3	6.7	4.4	3.6	4.2	4.2	5.6	1.3	1.5
Imports of goods and services	2.8	5.9	5.9	6.1	5.6	6.6	5.5	1.9	0.8
	Contribution to GDP growth in percentage points								
Domestic demand	1.0	3.3	3.7	5.1	3.4	3.8	2.7	3.1	1.9
Net exports of goods and services	1.4	1.1	–0.8	–1.5	–0.7	–1.4	0.4	–0.3	0.6
Exports of goods and services	3.5	5.3	3.5	3.1	3.3	3.1	4.4	1.1	1.2
Imports of goods and services	–2.1	–4.3	–4.3	–4.6	–4.0	–4.5	–4.1	–1.4	–0.5
	Year-on-year change of the period average in %								
Unit labor costs in the whole economy (nominal, per person)	3.1	3.5	6.3	6.6	7.1	7.0	4.8	4.9	4.7
Unit labor costs in manufacturing (nominal, per hour)	2.5	1.3	4.4	3.4	5.7	3.9	4.6	7.3	5.7
Labor productivity in manufacturing (real, per hour)	2.1	6.5	3.9	4.9	3.5	3.7	3.6	0.3	1.5
Labor costs in manufacturing (nominal, per hour)	4.8	7.8	8.5	8.4	9.4	7.7	8.4	7.6	7.3
Producer price index (PPI) in industry	–3.2	0.8	0.7	–2.4	–0.2	2.2	3.2	3.1	2.5
Consumer price index (here: HICP)	0.6	2.4	2.0	1.7	2.1	2.3	1.8	2.3	2.4
EUR per 1 CZK, + = CZK appreciation	0.9	2.7	2.7	6.4	3.7	1.4	–0.8	–1.1	–0.3
	Period average levels								
Unemployment rate (ILO definition, %, 15–64 years)	4.0	2.9	2.3	2.4	2.2	2.4	2.1	2.1	1.9
Employment rate (%, 15–64 years)	72.0	73.6	74.8	74.2	74.7	75.0	75.4	75.0	75.0
Key interest rate per annum (%)	0.1	0.2	1.1	0.7	0.8	1.2	1.7	1.8	1.9
CZK per 1 EUR	27.0	26.3	25.6	25.4	25.6	25.7	25.9	25.7	25.7
	Nominal year-on-year change in the period-end stock in %								
Loans to the domestic nonbank private sector[1]	7.8	6.9	6.8	6.7	6.3	6.6	6.8	5.4	5.3
of which: loans to households	7.2	7.5	7.5	7.6	7.5	7.6	7.5	7.0	6.6
loans to nonbank corporations	8.5	6.2	5.8	5.6	4.9	5.4	5.8	3.6	3.9
	%								
Share of foreign currency loans in total loans to the non-bank private sector	13.0	13.3	14.1	14.5	14.8	15.3	14.1	14.9	14.8
Return on assets (banking sector)	1.3	1.1	1.1	1.0	1.2	1.1	1.1	1.0	1.2
Tier 1 capital ratio (banking sector)	17.9	18.7	19.1	18.1	18.3	18.3	19.1	19.1	19.8
NPL ratio (banking sector)	4.6	3.7	3.1	3.4	3.3	3.2	3.1	3.0	2.7
	% of GDP								
General government revenues	40.2	40.5	41.5	..	..	..	..	..	..
General government expenditures	39.5	38.9	40.6	..	..	..	..	..	..
General government balance	0.7	1.6	0.9	..	..	..	..	..	..
Primary balance	1.6	2.3	1.7	..	..	..	..	..	..
Gross public debt	36.8	34.7	32.7	..	..	..	..	..	..
	% of GDP								
Debt of nonfinancial corporations (nonconsolidated)	58.5	58.1	56.7	..	..	..	..	..	..
Debt of households and NPISHs[2] (nonconsolidated)	31.2	32.6	32.0	..	..	..	..	..	..
	% of GDP (based on EUR), period total								
Goods balance	5.2	5.1	4.1	6.6	5.2	2.3	2.6	5.5	5.6
Services balance	2.3	2.5	2.3	2.5	2.7	1.7	2.1	2.8	2.7
Primary income	–5.3	–5.1	–5.3	–3.3	–6.5	–7.1	–4.2	–2.9	–5.8
Secondary income	–0.6	–0.9	–0.8	–1.7	–1.0	–0.8	0.3	–2.1	–0.2
Current account balance	1.6	1.6	0.3	4.2	0.4	–3.9	0.8	3.3	2.4
Capital account balance	1.1	0.8	0.3	0.1	–0.1	0.3	0.7	–0.5	0.6
Foreign direct investment (net)[3]	–3.9	–0.9	–1.7	0.6	–2.0	–2.7	–2.5	0.1	–1.2
	% of GDP (rolling four-quarter GDP, based on EUR), end of period								
Gross external debt	73.4	89.1	81.5	85.6	82.4	82.2	81.5	80.5	80.0
Gross official reserves (excluding gold)	45.9	64.1	59.8	61.4	61.1	59.9	59.8	60.4	60.3
	Months of imports of goods and services								
Gross official reserves (excluding gold)	7.7	10.6	10.0	10.3	10.3	10.0	10.0	10.1	10.2
	EUR million, period total								
GDP at current prices	176,368	191,999	207,725	48,429	52,127	52,578	54,591	50,875	55,161

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).

7 Hungary: government tightens budget amid slowing growth in 2020

GDP growth presumably peaked in the first quarter of 2019

Output growth in Hungary accelerated modestly during the first half of 2019 and presumably reached its cyclical peak in the first quarter. As in the past two years, growth was most pronounced in domestic demand, particularly in gross fixed capital formation, which accelerated even further from an already high base. High capacity utilization rates, accelerated credit growth, strong economic sentiment, expanded housing subsidies, EU-funded projects and loose monetary policy supported investment activity. Private consumption growth slowed but remained healthy, along with similar trends in consumer confidence, the ongoing expansion of employment and a stronger growth of loans to households. At the same time, real wage growth became somewhat weaker. Notwithstanding strong domestic demand (excluding stock changes), the contribution of net real exports improved compared to 2018, as export growth accelerated and sharp destocking reduced import demand. Looking forward, high-frequency indicators suggest a weakening of economic activity, but loose monetary policy and various government measures (Family Protection Plan, Economy Protection Action Plan) are expected to keep output growth well above the EU average.

Government tightens budgetary stance in 2020 compared to earlier plans

The deficit of the general government budget amounted to 2.2% of GDP in 2018. According to the European Commission's Spring 2019 Economic Forecast, the deficit should decline to 1.8% of GDP in 2019 and 1.6% of GDP in 2020. While the forecast for 2019 matches the Hungarian government's deficit target, the 2020 budget law envisages a substantially smaller deficit of 1% of GDP, which is also 0.5 percentage points lower than what was penciled in in the 2019 Convergence Programme Update. The tightening of the budgetary stance may be motivated by the ongoing significant deviation procedure against Hungary. In this framework, the EU Council in mid-2019 called on Hungary to adopt structural measures in the magnitude of a combined 0.8% of GDP in 2019 and 2020. Hungary must report to the EU Council on actions taken by mid-October 2019.

Central bank in data-driven wait-and-see mode

Headline inflation (HICP) peaked at 4% in May 2019 and fell back to 3.2% by August 2019. Magyar Nemzeti Bank's (MNB) preferred gage for less volatile underlying inflationary trends, i.e. core inflation[10] excluding indirect taxes, also peaked in May, at 3.7%, and declined to 3.2% by August. In its June and September 2019 inflation reports, the MNB again revised upward its inflation forecasts for the period from 2019 to 2021, expecting annual average inflation to climb from 3.3% in 2019 to 3.4% in 2020 before falling back to 3.3% in 2021. Overall, these developments have so far validated the monetary council's wait-and-see attitude as inflation is again back to near the midpoint of the MNB's medium-term target of 3% ± 1 percentage point. In addition, the monetary council has repeatedly suggested since late August 2019 that most recent trends indicated a strengthening of downside risks to the longer-term inflation outlook.

Credit to households continued to expand at a rate of 7.5% to 8% year on year during the reporting period. Housing loans were the most dynamic segment, bolstered by the expansion of housing subsidies to families, but other lending categories strengthened as well. Lending to the corporate sector continued to grow by close to 15% year on year in the second quarter of 2019, with demand focusing on longer-term credit, which was, in part, promoted by the MNB's Funding for Growth Scheme Fix (FGS-fix) scheme for SMEs and in line with strong corporate investment activity.

[10] *The national definition of core inflation excludes unprocessed food, energy and administered prices from the CPI.*

Table 7

Main economic indicators: Hungary

	2016	2017	2018	Q1 18	Q2 18	Q3 18	Q4 18	Q1 19	Q2 19
Year-on-year change of the period total in %									
GDP at constant prices	2.3	4.1	4.9	4.6	4.9	5.1	5.1	5.3	4.9
Private consumption	4.0	4.8	5.4	5.8	5.5	5.3	5.0	5.3	4.5
Public consumption	0.7	1.3	–0.5	1.6	–0.2	–0.1	–3.1	2.2	2.3
Gross fixed capital formation	–11.7	18.2	16.5	10.5	15.6	20.0	17.2	23.4	16.4
Exports of goods and services	5.1	4.7	4.7	4.0	7.1	2.3	5.6	7.7	2.7
Imports of goods and services	3.9	7.7	7.1	5.3	8.5	6.2	8.2	6.7	4.3
Contribution to GDP growth in percentage points									
Domestic demand	0.9	6.1	6.5	5.4	5.5	8.0	6.7	4.1	6.2
Net exports of goods and services	1.4	–1.9	–1.5	–0.8	–0.6	–2.9	–1.7	1.3	–1.2
Exports of goods and services	4.5	4.2	4.2	3.8	6.3	2.0	4.7	7.1	2.4
Imports of goods and services	–3.1	–6.2	–5.7	–4.6	–6.9	–4.9	–6.3	–5.8	–3.6
Year-on-year change of the period average in %									
Unit labor costs in the whole economy (nominal, per person)	4.0	4.5	3.5	5.8	2.4	2.5	3.2	4.8	6.7
Unit labor costs in manufacturing (nominal, per hour)	8.8	5.2	7.4	7.1	7.0	8.1	7.6	7.0	9.0
Labor productivity in manufacturing (real, per hour)	–2.9	2.7	1.5	2.0	1.5	0.9	1.4	5.0	2.3
Labor costs in manufacturing (nominal, per hour)	5.6	8.0	9.0	9.3	8.6	9.1	9.1	12.4	11.6
Producer price index (PPI) in industry	–1.7	3.3	5.6	3.6	5.3	7.9	5.5	3.2	2.3
Consumer price index (here: HICP)	0.4	2.4	2.9	2.0	2.8	3.5	3.3	3.2	3.8
EUR per 1 HUF, + = HUF appreciation	–0.5	0.7	–3.0	–0.6	–2.3	–5.4	–3.5	–2.1	–1.8
Period average levels									
Unemployment rate (ILO definition, %, 15–64 years)	5.2	4.2	3.8	3.9	3.6	3.9	3.6	3.6	3.4
Employment rate (%, 15–64 years)	66.5	68.2	69.3	68.7	69.3	69.5	69.5	69.9	70.0
Key interest rate per annum (%)	1.0	0.9	0.9	0.9	0.9	0.9	0.9	0.9	0.9
HUF per 1 EUR	311.5	309.3	318.8	311.1	317.1	324.1	323.0	317.9	322.9
Nominal year-on-year change in the period-end stock in %									
Loans to the domestic nonbank private sector[1]	0.0	4.3	10.0	4.5	6.6	9.1	10.0	11.0	12.1
of which: loans to households	–2.8	1.3	5.8	–0.1	2.1	3.2	5.8	7.7	7.6
loans to nonbank corporations	2.3	6.8	13.1	8.3	10.1	13.7	13.1	13.5	15.4
%									
Share of foreign currency loans in total loans to the non-bank private sector	22.4	23.5	24.0	23.5	24.7	24.1	24.0	23.8	24.1
Return on assets (banking sector)	1.3	1.8	1.4	1.7	1.6	1.5	1.4	1.4	1.3
Tier 1 capital ratio (banking sector)	19.2	21.1	17.8	20.2	19.3	19.2	17.8	16.3	16.8
NPL ratio (banking sector)	5.6	3.7	2.2	3.1	2.8	2.6	2.2	3.4	3.1
% of GDP									
General government revenues	45.1	44.7	44.2	..	..	..	..	..	..
General government expenditures	46.8	46.9	46.5	..	..	..	..	..	..
General government balance	–1.6	–2.2	–2.2	..	..	..	..	..	..
Primary balance	1.5	0.6	0.2	..	..	..	..	..	..
Gross public debt	76.0	73.4	70.8	..	..	..	..	..	..
% of GDP									
Debt of nonfinancial corporations (nonconsolidated)	71.8	67.3	66.5	..	..	..	..	..	..
Debt of households and NPISHs[2] (nonconsolidated)	20.4	18.7	17.8	..	..	..	..	..	..
% of GDP (based on EUR), period total									
Goods balance	3.5	1.5	–1.3	0.6	0.3	–4.0	–1.6	0.2	–1.1
Services balance	5.4	5.8	5.7	5.3	6.3	6.6	4.7	5.1	6.0
Primary income	–2.7	–4.1	–4.0	–3.3	–4.9	–4.0	–3.8	–3.5	–4.6
Secondary income	–1.5	–1.0	–1.0	–1.1	–0.7	–0.4	–1.7	–1.6	–0.7
Current account balance	4.6	2.3	–0.5	1.5	0.9	–1.8	–2.4	0.2	–0.3
Capital account balance	0.0	0.9	2.6	2.4	2.3	1.7	3.9	2.9	2.5
Foreign direct investment (net)[3]	–2.2	–1.7	–2.1	–1.6	–0.2	–6.6	–0.2	–4.9	1.1
% of GDP (rolling four-quarter GDP, based on EUR), end of period									
Gross external debt	97.4	85.1	81.3	83.1	82.8	81.5	81.3	81.9	81.1
Gross official reserves (excluding gold)	21.4	18.8	19.9	18.2	18.6	18.2	19.9	19.6	18.9
Months of imports of goods and services									
Gross official reserves (excluding gold)	3.2	2.8	2.9	2.7	2.8	2.7	2.9	2.9	2.8
EUR million, period total									
GDP at current prices	113,933	124,023	131,821	29,496	32,665	33,471	36,189	31,832	35,281

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).

8 Poland: no signs of taking heed of the EU Council's fiscal recommendation

Robust balanced growth coupled with moderate current account surplus

GDP growth in Poland stood at 4.4% in the first half of 2019 after 5.1% in 2018, with quarter-on-quarter growth declining to 0.8% after 1.4% in the first quarter. Like GDP growth, total final demand growth was lower in the first half of 2019 than in 2018, as both foreign and domestic demand growth declined and contributed substantially to total final demand growth. As a result, import growth shrank by more than export growth and the net export contribution to GDP growth turned positive. The slowdown in domestic demand stemmed mainly from the contribution of inventory build-up swinging into negative territory, having added ½ percentage point to growth in 2018. By contrast, fixed investment growth accelerated. While public investment growth (on the back of EU funds) declined, several factors like strong demand, high capacity utilization rates, a stable liquidity position and low real lending rates led to sharply higher business fixed investment, even though industrial confidence and profitability showed slight signs of deterioration. Measured by the number of dwellings under construction, housing investment growth continued but slowed down moderately. Private consumption growth also slowed moderately, as the real wage sum rose somewhat less due to an uptick in inflation. But the real growth of pensions continued unabated, and consumer confidence remained robust.

In the first half of 2019, the Polish current account balance showed a surplus of 1% of GDP after having recorded a balanced position one year earlier; this was attributable to a rise in the goods and services balance to 5% of GDP, given the parallel weakening of both export growth and domestic demand growth. The capital account surplus stood at 1.5% of GDP. Net FDI inflows stood at about 2% of GDP.

Higher ULC without eroding price competitiveness, while inflation returns to target

In the first half of 2019, nominal ULC in the whole economy continued to rise by about 4%. Manufacturing ULC grew somewhat less; their growth was also lower than in the euro area. The Polish złoty's euro value was lower year on year by about 2%, thus slightly improving price competitiveness and providing an inflation impulse. In August 2019, annual headline inflation stood at 2.6% (HICP) and 2.9% (national CPI), respectively, while core inflation stood at 2.5% (HICP excluding energy and unprocessed food) and 2.2% (CPI excluding energy and all food), respectively. Headline and core inflation figures were higher in August than in March, by roughly 0.5 percentage points, under both concepts. The Polish Monetary Policy Council, pursuing an inflation target of 2.5% (CPI), has kept the key policy rate at 1.5% since March 2015. On October 2, 2019, it concluded that inflation would remain close to the target over the monetary policy transmission horizon (after a temporary rise in early 2020) and that the current level of interest rates was conducive to keeping the economy on a sustainable growth path.

Social transfer hike ahead of elections enlarged deviation from fiscal MTO

The European Commission staff forecast expects an almost stable revenue-to-GDP ratio but an increase of the expenditure-to-GDP ratio by about 1 percentage point of GDP in 2019 compared to 2018. A significant increase of social transfers to pensioners and middle- and upper-income households with children is the main factor behind the rise in expenditures. As a result, the European Commission forecasts a headline deficit of 1.6% of GDP (2018: 0.4%) and a structural deficit of 2.8% of GDP (2018: 1.4%), implying a structural primary deficit of 1.4% of GDP (2018: 0.0%) and a persistent deviation from the MTO of a structural deficit of 1% of GDP. Thus, in July 2019, the EU Council recommended that the Polish government take action to ensure an annual structural adjustment by 0.6% of GDP in 2019, as it had already recommended in July 2018, and in 2020. The European Commission expects Polish general government gross debt to reach 48.2% of GDP at end-2019, after 48.9% at end-2018.

Table 8

Main economic indicators: Poland

	2016	2017	2018	Q1 18	Q2 18	Q3 18	Q4 18	Q1 19	Q2 19
	Year-on-year change of the period total in %								
GDP at constant prices	3.1	4.9	5.1	5.2	5.4	5.7	4.4	4.7	4.1
Private consumption	3.9	4.5	4.4	3.9	4.4	4.3	5.1	3.7	4.0
Public consumption	1.9	2.9	4.7	4.3	4.1	5.7	4.7	6.5	3.0
Gross fixed capital formation	–8.2	4.0	8.7	11.0	5.8	12.4	7.1	12.7	9.1
Exports of goods and services	8.8	9.5	6.3	3.8	8.6	5.9	6.9	6.0	3.9
Imports of goods and services	7.6	9.8	7.1	6.5	7.7	7.1	7.3	5.1	4.4
	Contribution to GDP growth in percentage points								
Domestic demand	2.2	4.7	5.3	6.4	4.5	6.1	4.4	4.0	4.2
Net exports of goods and services	0.8	0.3	–0.2	–1.2	0.8	–0.4	0.1	0.7	–0.1
Exports of goods and services	4.4	5.0	3.4	2.2	4.8	3.2	3.5	3.4	2.3
Imports of goods and services	–3.5	–4.7	–3.6	–3.4	–4.0	–3.6	–3.4	–2.7	–2.3
	Year-on-year change of the period average in %								
Unit labor costs in the whole economy (nominal, per person)	2.5	2.1	2.8	1.6	3.6	2.4	3.6	4.5	3.7
Unit labor costs in manufacturing (nominal, per hour)	3.6	2.7	4.7	4.7	3.6	4.3	6.3	2.4	5.0
Labor productivity in manufacturing (real, per hour)	0.5	3.6	3.1	3.3	4.4	2.7	2.0	3.9	2.4
Labor costs in manufacturing (nominal, per hour)	4.2	6.4	8.0	8.2	8.2	7.2	8.4	6.4	7.5
Producer price index (PPI) in industry	–0.3	2.7	2.1	0.1	2.4	3.1	2.7	2.6	1.6
Consumer price index (here: HICP)	–0.2	1.6	1.2	1.0	1.1	1.4	1.1	1.2	2.2
EUR per 1 PLN, + = PLN appreciation	–4.1	2.5	–0.1	3.4	–1.0	–1.1	–1.6	–2.9	–0.5
	Period average levels								
Unemployment rate (ILO definition, %, 15–64 years)	6.3	5.0	3.9	4.2	3.6	3.9	3.9	4.0	3.3
Employment rate (%, 15–64 years)	64.5	66.1	67.4	66.6	67.7	68.0	67.3	67.2	68.2
Key interest rate per annum (%)	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5	1.5
PLN per 1 EUR	4.4	4.3	4.3	4.2	4.3	4.3	4.3	4.3	4.3
	Nominal year-on-year change in the period-end stock in %								
Loans to the domestic nonbank private sector[1]	3.9	6.2	6.4	5.6	5.5	5.9	6.4	6.9	6.7
of which: loans to households	4.0	4.8	5.7	5.1	5.2	5.4	5.7	5.6	5.9
loans to nonbank corporations	3.7	8.7	7.6	6.3	6.0	6.9	7.6	9.2	8.2
	%								
Share of foreign currency loans in total loans to the non-bank private sector	25.8	21.3	20.8	21.2	21.5	20.9	20.8	20.6	19.8
Return on assets (banking sector)	0.8	0.8	0.7	0.7	0.8	0.8	0.7	0.6	0.8
Tier 1 capital ratio (banking sector)	16.1	17.2	17.1	17.0	17.0	17.3	17.1	17.0	16.9
NPL ratio (banking sector)	7.1	6.8	6.8	7.7	7.1	7.0	6.8	6.8	6.8
	% of GDP								
General government revenues	38.9	39.7	41.2	..	..	..	..	..	..
General government expenditures	41.1	41.2	41.5	..	..	..	..	..	..
General government balance	–2.2	–1.5	–0.4	..	..	..	..	..	..
Primary balance	–0.5	0.1	1.1	..	..	..	..	..	..
Gross public debt	54.2	50.6	48.9	..	..	..	..	..	..
	% of GDP								
Debt of nonfinancial corporations (nonconsolidated)	49.1	47.1	45.2	..	..	..	..	..	..
Debt of households and NPISHs[2] (nonconsolidated)	36.2	35.6	34.8	..	..	..	..	..	..
	% of GDP (based on EUR), period total								
Goods balance	0.7	0.3	–1.0	–1.3	–0.5	–0.9	–1.2	0.4	0.3
Services balance	3.3	3.8	4.4	4.6	4.8	4.1	4.0	4.7	4.7
Primary income	–4.2	–4.1	–4.1	–3.0	–4.5	–5.2	–3.8	–2.4	–4.3
Secondary income	–0.3	0.0	–0.3	–0.2	–0.1	–0.4	–0.4	–0.9	–0.3
Current account balance	–0.5	0.1	–1.0	0.1	–0.3	–2.4	–1.3	1.7	0.3
Capital account balance	1.0	1.3	2.1	1.2	1.4	2.0	3.6	0.7	2.2
Foreign direct investment (net)[3]	–0.9	–1.4	–2.5	–3.5	–2.2	–4.7	0.0	–4.8	0.8
	% of GDP (rolling four-quarter GDP, based on EUR), end of period								
Gross external debt	75.3	68.4	63.4	67.3	64.7	64.7	63.4	62.0	60.8
Gross official reserves (excluding gold)	24.5	19.5	19.7	19.5	18.6	19.0	19.7	19.2	18.5
	Months of imports of goods and services								
Gross official reserves (excluding gold)	6.1	4.7	4.5	4.7	4.4	4.4	4.5	4.4	4.3
	EUR million, period total								
GDP at current prices	426,485	467,598	496,267	116,560	119,092	122,044	138,571	120,931	127,398

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).

9 Romania: unbalanced growth amid mounting fiscal risks

Strong rebound of investments, export growth weakens further

GDP growth in Romania accelerated to 4.7% in the first half of 2019, mainly driven by buoyant domestic demand. Economic policy has remained supportive for private consumption, as minimum wages were hiked considerably again at the beginning of the year. Real wage growth also benefited from tight labor market conditions. It is interesting to note that a minimum wage of RON 3,000 was set in the construction sector together with further measures to attract workforce in this sector (exemption from paying personal income tax, lower social security contributions, easier conditions for granting work permits to non-EU citizens). As a matter of fact, the strong increase in construction activity fueled a substantial rebound of investments. The absorption of EU funds and continued domestic credit growth played an important role in this respect as well.

Current account deficit widens while inflationary pressures persist

Partly reflecting subdued external demand, export growth weakened further in the first half of 2019, with exports almost stagnating in the second quarter. After a strong increase in the first quarter, import growth decelerated somewhat in the second quarter. In total, the contribution of net exports to growth remained clearly negative. The mild nominal depreciation of the Romanian leu vis-à-vis the euro fell short of offsetting ULC increases both for the whole economy and the manufacturing sector.

Mainly driven by the expanding trade deficit, the Romanian current account deficit widened to 4.9% of GDP in the first half of 2019, compared to 4.4% in the first half of 2018. As net inflows in the capital account (including EU funds) rose, the deterioration in the net borrowing position from the combined current and capital account was less pronounced. This position reached 3.7% of GDP, of which about 80% were covered by net FDI inflows.

Monetary policy-relevant CPI inflation rose to 4.1% in July before falling slightly to 3.9% in August, thus staying above the upper bound of the Romanian central bank's target band of 2.5% ± 1 percentage point. Amid the build-up of demand-pull and cost-push pressures, core inflation continuously went up from 2.4% at end-2018 to 3.4% in August. The central bank left its key policy rate unchanged at 2.5% and repeatedly stated that it will maintain strict control over money market liquidity. It expects the inflation rate to remain above the upper bound of the target band for the remainder of the year.

Growing fiscal risks; significant deviation procedure has not triggered effective action

In 2018, the general government budget deficit reached 3% of GDP, i.e. the limit laid down in the EU Stability and Growth Pact. In the first eight months of 2019, the deficit increased by about 15% in nominal terms. A first budget revision was adopted in August, aiming to reach a deficit of 2.8% of GDP in 2019. Yet, Romania's fiscal council sees significant risks of exceeding the deficit target and the 3% limit in 2019 in the absence of additional measures. The breakup of the ruling coalition in late August 2019 may complicate the adoption of further corrective measures, however. In June, the Romanian parliament passed a new pension law that will have a considerable impact on the budget from 2020 onward and entails the doubling of pillar I pension benefits by 2022.

Under the significant deviation procedure, the EU Council established in June 2019 that Romania had not taken effective action in response to its recommendation issued in December 2018. It recommended that Romania take fiscal measures corresponding to an annual structural adjustment of 1% in 2019 and 0.75% in 2020.

Table 9

Main economic indicators: Romania

	2016	2017	2018	Q1 18	Q2 18	Q3 18	Q4 18	Q1 19	Q2 19
	Year-on-year change of the period total in %								
GDP at constant prices	4.8	7.0	4.1	4.0	4.1	4.2	4.1	5.0	4.4
Private consumption	8.2	10.0	5.2	5.9	5.0	4.4	5.8	7.0	5.3
Public consumption	3.9	2.8	1.9	2.7	–2.4	6.7	0.8	0.1	1.6
Gross fixed capital formation	0.0	3.3	–3.1	1.5	–4.9	–3.9	–3.2	3.9	18.0
Exports of goods and services	16.1	9.7	5.4	7.9	7.1	2.6	4.2	3.6	0.5
Imports of goods and services	16.5	11.3	9.1	11.7	9.4	6.8	9.0	10.2	3.6
	Contribution to GDP growth in percentage points								
Domestic demand	5.1	7.6	5.8	7.0	4.0	5.6	6.7	6.6	5.9
Net exports of goods and services	–0.3	–0.7	–1.7	–2.0	–1.3	–1.3	–2.2	–2.6	–1.5
Exports of goods and services	6.6	4.1	2.3	3.7	2.9	1.3	1.7	2.3	0.2
Imports of goods and services	–6.9	–4.8	–4.0	–5.7	–4.2	–2.6	–3.9	–5.0	–1.7
	Year-on-year change of the period average in %								
Unit labor costs in the whole economy (nominal, per person)	8.6	8.1	14.3	17.3	14.2	14.5	10.6	6.1	3.1
Unit labor costs in manufacturing (nominal, per hour)	8.3	5.6	4.9	5.6	2.5	4.9	6.6	8.0	14.0
Labor productivity in manufacturing (real, per hour)	1.2	8.3	5.5	5.3	7.8	5.4	3.5	4.1	–1.9
Labor costs in manufacturing (nominal, per hour)	9.6	14.3	10.6	11.2	10.5	10.5	10.3	12.5	11.8
Producer price index (PPI) in industry	–1.8	3.5	5.0	3.9	5.2	5.8	5.2	4.6	4.5
Consumer price index (here: HICP)	–1.1	1.1	4.1	3.7	4.5	4.6	3.5	3.8	4.3
EUR per 1 RON, + = RON appreciation	–1.0	–1.7	–1.8	–2.9	–2.2	–1.4	–0.9	–1.7	–2.0
	Period average levels								
Unemployment rate (ILO definition, %, 15–64 years)	6.1	5.1	4.3	4.8	4.3	4.0	4.2	4.2	3.9
Employment rate (%, 15–64 years)	61.6	63.9	64.8	63.1	65.5	66.2	64.5	64.2	66.4
Key interest rate per annum (%)	1.8	1.8	2.4	2.1	2.4	2.5	2.5	2.5	2.5
RON per 1 EUR	4.5	4.6	4.7	4.7	4.7	4.6	4.7	4.7	4.7
	Nominal year-on-year change in the period-end stock in %								
Loans to the domestic nonbank private sector[1]	1.5	4.4	7.9	5.4	6.0	5.8	7.9	6.8	6.4
of which: loans to households	4.5	7.1	9.1	8.8	9.3	9.0	9.1	7.3	6.3
loans to nonbank corporations	–2.4	2.5	6.6	1.7	2.5	2.4	6.6	6.3	6.5
	%								
Share of foreign currency loans in total loans to the non-bank private sector	43.3	37.2	34.0	36.4	35.0	34.6	34.0	34.2	33.4
Return on assets (banking sector)	1.1	1.3	1.6	1.6	1.7	1.8	1.6	1.6	1.2
Tier 1 capital ratio (banking sector)	17.6	18.0	18.6	17.9	17.6	17.8	18.6	17.9	17.7
NPL ratio (banking sector)	9.6	6.4	5.0	6.2	5.7	5.6	5.0	4.9	4.7
	% of GDP								
General government revenues	31.8	30.9	32.0	..	..	..	..	..	..
General government expenditures	34.5	33.6	35.0	..	..	..	..	..	..
General government balance	–2.7	–2.7	–3.0	..	..	..	..	..	..
Primary balance	–1.2	–1.4	–1.8	..	..	..	..	..	..
Gross public debt	37.3	35.2	35.0	..	..	..	..	..	..
	% of GDP								
Debt of nonfinancial corporations (nonconsolidated)	39.8	35.1	33.1	..	..	..	..	..	..
Debt of households and NPISHs[2] (nonconsolidated)	16.5	15.9	15.9	..	..	..	..	..	..
	% of GDP (based on EUR), period total								
Goods balance	–5.5	–6.5	–7.3	–7.0	–7.3	–6.6	–8.2	–8.8	–7.8
Services balance	4.5	4.4	4.1	5.0	4.3	3.6	3.8	4.6	4.8
Primary income	–2.6	–2.5	–2.5	–1.5	–4.3	–3.7	–0.6	0.3	–4.3
Secondary income	1.5	1.4	1.2	0.9	1.5	0.9	1.4	1.1	0.6
Current account balance	–2.1	–3.2	–4.5	–2.7	–5.8	–5.7	–3.6	–2.8	–6.7
Capital account balance	2.5	1.2	1.2	0.7	1.0	0.9	2.0	1.7	0.9
Foreign direct investment (net)[3]	–2.6	–2.6	–2.5	–3.9	–0.5	–4.9	–0.8	–2.9	–2.9
	% of GDP (rolling four-quarter GDP, based on EUR), end of period								
Gross external debt	54.6	51.9	49.0	51.3	50.1	50.0	49.0	48.3	49.2
Gross official reserves (excluding gold)	20.1	17.9	16.3	18.3	16.5	15.9	16.3	15.5	15.4
	Months of imports of goods and services								
Gross official reserves (excluding gold)	5.7	4.9	4.4	5.0	4.4	4.3	4.4	4.1	4.1
	EUR million, period total								
GDP at current prices	170,382	187,282	202,879	38,503	46,553	56,539	61,285	42,307	50,674

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: fragile stabilization amid high macrofinancial risks

Slower decline in GDP growth given pre-election policy stimulus

Following a technical recession in the second half of 2018, the annual contraction of GDP growth in Turkey moderated in the first half of 2019 (–1.9% year on year). All domestic demand components except public consumption have contributed to the decline in GDP since the beginning of 2019. Gross fixed capital formation edged down sizably by 17.6% as a number of public projects, inter alia, were discontinued, while the corporate sector held back investments. At the same time, despite supportive lending by state banks related to the policy stimulus ahead of the local elections in March 2019 and the increase of the minimum wage by 26% as of January 2019, private consumption declined by 3%, albeit at a diminishing rate throughout the first half of 2019. The unemployment rate, which peaked at a historical high of 14% in June, also weighed against a sustainable recovery of private consumption.

On the back of temporary tax reductions, continued minimum wage subsidies and employment incentive schemes that were partly related to an election-related stimulus, the budget deficit widened in the course of 2019 and is expected to reach 2.9% of GDP according to the New Economic Programme that was announced in September 2019. Gross public debt increased only slightly, however, with repayment pressures mounting until end-2019.

Remarkable adjustment of external imbalances

Net exports continued to contribute positively to economic growth in the first half of 2019. Export growth remained robust in line with a strong tourism season and sound economic activity in major trading partners. At the same time, imports nosedived due to stagnating private consumption and the continued depreciation of the Turkish lira. Accordingly, Turkey's current account posted a minor deficit of 0.9% of GDP in the second half of 2019, following a surplus of 1.1% of GDP in the second half of 2018. Net FDI inflows covered nearly 90% of the current account deficit. The traditionally strong portfolio inflows peaked at 5% of GDP in the first quarter of 2019 due to enhanced investor interest, before strongly reversing to an outflow of 4.1% of GDP in the second quarter of 2019. Gross external financing needs remain among the highest in the emerging markets and continued to stay above 20% of GDP.

Somewhat weaker inflation pressures give way to monetary easing cycle

The gradual slowdown in the depreciation of the Turkish lira between early January and end-September 2019 (7% against the U.S. dollar and 1.5% against the euro), coupled with lower domestic demand pressures, contributed to easing inflation. Following a peak of 25.2% in October 2018, consumer inflation (CPI) came down to 9.3% in September 2019 – still clearly above the monetary policy target of 5%. Despite enduring depreciation pressures, the Turkish central bank (CBRT) kept its one-week repo rate unchanged at 24% from mid-September 2018 until recently. Surpassing market expectations, the CBRT slashed its policy rate for the first time since 2017 by a total of 750 basis points to 16.5% in two steps in July and in September 2019 – the largest interest rate reduction in at least 17 years.

Mounting credit risk weighs on banking system

On the back of a pre-election fiscal stimulus and the relaxation of lending standards for some segments, and despite elevated inflationary pressures, financial conditions have eased somewhat since the beginning of 2019. Nevertheless, the growth of credit to the nonfinancial private sector slowed down in the first half of 2019. Credit risk has increased since August 2018, and the NPL ratio rose to 4.7% of total loans. In addition, the Turkish government's policy plans to clean up banks' NPLs – as announced in April 2019 – have stalled.

Table 10

Main economic indicators: Turkey

	2016	2017	2018	Q1 18	Q2 18	Q3 18	Q4 18	Q1 19	Q2 19
	Year-on-year change of the period total in %								
GDP at constant prices	3.2	7.5	2.8	7.5	5.6	2.3	–2.8	–2.3	–1.5
Private consumption	3.7	6.2	0.1	6.0	2.7	0.7	–7.7	–4.8	–1.1
Public consumption	9.5	5.0	6.6	4.9	9.6	6.9	5.3	6.6	3.3
Gross fixed capital formation	2.2	8.3	–0.6	10.4	6.2	–4.4	–11.6	–12.4	–22.8
Exports of goods and services	–1.9	12.0	7.8	0.9	4.5	14.2	10.7	9.2	8.1
Imports of goods and services	3.7	10.4	–7.8	15.3	0.2	–16.4	–24.3	–28.9	–16.9
	Contribution to GDP growth in percentage points								
Domestic demand	4.1	6.9	0.8	7.3	4.8	0.0	–7.2	–5.6	–7.2
Net exports of goods and services	–1.3	0.1	3.5	–3.4	0.9	6.6	8.3	9.2	5.6
Exports of goods and services	–0.4	2.5	1.7	0.2	1.0	3.0	2.2	2.0	1.7
Imports of goods and services	–0.9	–2.4	1.9	–3.6	0.0	3.7	6.1	7.3	3.8
	Year-on-year change of the period average in %								
Unit labor costs in the whole economy (nominal, per person)	..	..	..	..	..	..	..	..	..
Unit labor costs in manufacturing (nominal, per hour)	15.8	4.0	18.1	11.6	15.1	18.6	28.0	24.1	24.2
Labor productivity in manufacturing (real, per hour)	4.4	6.3	1.7	6.0	2.9	1.7	–3.0	–0.1	3.1
Labor costs in manufacturing (nominal, per hour)	21.0	10.5	20.4	18.2	18.5	20.7	24.2	24.0	28.1
Producer price index (PPI) in industry	4.3	15.8	27.0	13.4	20.1	34.5	39.0	30.7	27.9
Consumer price index (here: HICP)	7.7	11.1	16.3	10.3	12.8	19.4	22.4	19.9	18.0
EUR per 1 TRY, + = TRY appreciation	–9.6	–18.9	–27.7	–16.1	–24.5	–37.5	–28.6	–23.2	–20.9
	Period average levels								
Unemployment rate (ILO definition, %, 15–64 years)	11.1	11.1	11.1	10.8	9.8	11.3	12.5	15.0	13.1
Employment rate (%, 15–64 years)	50.7	51.6	52.0	51.1	52.7	53.0	51.1	49.3	50.7
Key interest rate per annum (%)	7.5	8.0	15.5	8.0	11.2	18.9	24.0	24.0	24.0
TRY per 1 EUR	3.3	4.1	5.7	4.7	5.2	6.6	6.3	6.1	6.6
	Nominal year-on-year change in the period-end stock in %								
Loans to the domestic nonbank private sector	15.8	20.8	12.4	19.7	21.7	27.6	12.4	12.9	6.7
of which: loans to households	9.6	16.3	3.2	14.8	14.1	9.2	3.2	1.5	–0.6
loans to nonbank corporations	18.2	22.3	15.5	21.4	24.3	33.9	15.5	16.6	8.9
	%								
Share of foreign currency loans in total loans to the nonbank private sector	35.8	32.9	38.5	33.4	35.2	41.0	38.5	38.6	38.2
Return on assets (banking sector)	1.5	1.6	1.5	1.7	1.7	1.5	1.5	1.2	1.2
Tier 1 capital ratio (banking sector)	12.7	13.6	13.4	13.5	13.1	13.9	13.4	12.6	13.1
NPL ratio (banking sector)	3.4	3.1	4.1	3.0	3.2	3.4	4.1	4.3	4.7
	% of GDP								
General government revenues	33.0	31.4	30.3	..	..	..	..	..	..
General government expenditures	34.1	34.2	32.9	..	..	..	..	..	..
General government balance	–1.1	–2.8	–2.6	..	..	..	..	..	..
Primary balance	0.9	–0.6	–0.2	..	..	..	..	..	..
Gross public debt	28.3	28.3	31.1	..	..	..	..	..	..
	% of GDP								
Debt of nonfinancial corporations (nonconsolidated)	..	..	..	..	..	..	..	..	..
Debt of households and NPISHs[1] (nonconsolidated)	..	..	..	..	..	..	..	..	..
	% of GDP (based on EUR), period total								
Goods balance	–4.7	–6.9	–5.3	–8.3	–8.1	–4.1	–0.4	–1.8	–2.9
Services balance	1.8	2.3	3.3	1.5	2.7	6.2	3.1	1.9	4.4
Primary income	–1.1	–1.3	–1.5	–1.1	–1.8	–1.3	–1.8	–1.3	–2.1
Secondary income	0.2	0.3	0.1	0.1	0.0	0.1	0.2	0.1	0.0
Current account balance	–3.8	–5.5	–3.4	–7.9	–7.3	0.9	1.2	–1.0	–0.7
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]	–1.3	–1.0	–1.2	–0.6	–1.0	–1.4	–1.8	–1.2	–0.6
	% of GDP (rolling four-quarter GDP, based on EUR), end of period								
Gross external debt	50.3	51.1	58.3	50.7	53.0	54.8	58.3	61.5	61.0
Gross official reserves (excluding gold)	11.2	9.3	9.7	9.1	8.8	8.4	9.7	10.5	10.4
	Months of imports of goods and services								
Gross official reserves (excluding gold)	5.4	3.8	3.8	3.7	3.5	3.2	3.8	4.1	4.1
	EUR million, period total								
GDP at current prices	778,742	752,677	656,467	168,433	170,607	155,493	161,934	150,799	155,171

Source: Bloomberg, European Commission, Eurostat, national statistical offices, national central banks, wiiw, 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: renewed slowdown of economic dynamics

External factors and stagnating investment dampen growth again

Economic activity in Russia decelerated to +0.7% in the first half of 2019 (year on year) owing to the weakening global economy, weaker oil prices and the end of the construction boom that was linked to a major resource extraction project in Siberia (Yamal LNG). Thus, in the first six months of 2019, net exports lost momentum again and fixed investment stagnated (year on year). Although by no means dynamic, the factor driving growth was private consumption, while public consumption stagnated and fiscal policy remained tight. On the production side of GDP, growth continued to be driven by resource extraction, manufacturing (including automobile production) and retail trade. The unemployment rate declined further to 4.6% in the second quarter of 2019, a new historical minimum.

CBR's tight monetary stance helps bring down VAT increase-triggered inflationary spike

Given the weakness of the oil price (down 4.5% in the first half of 2019 against the same period of 2018), continued foreign exchange purchases of the Russian central bank (CBR) under the fiscal rule and the absence of new U.S. sanctions until August 2019, the exchange rate of the Russian ruble slightly declined in nominal effective terms in the first half of 2019 compared to 2018. In early August 2019, new sanctions were adopted, including U.S. opposition to loans of international financial organizations to Russia and further restrictions on U.S. bank loans to Russia – which, however, do not promise to have a substantial impact on economic stability. The CBR's tight monetary stance (increase of the key rate to 7.75% in late 2018) helped cushion the temporary rise in inflation linked to housing and communal tariff adjustments as well as the VAT increase (from 18% to 20%) in January 2019. Thus, inflation eased from 5.3% in March to 4.0% in September 2019. This, in fact, already corresponds to the inflation target for 2020. Declining inflation and weaker-than-expected GDP growth in the first half of 2019 prompted the CBR to lower its key rate in three steps of ¼ percentage point each (in June, July and September) to 7.0%.

Solid twin surpluses continue, sizable international reserves expand further

The VAT increase, improved tax administration, pension reform (adjustment of the retirement age) and sustained restraint in spending pushed the federal budget surplus to 3.7% of GDP in the first eight months of 2019 (against 3.2% in the corresponding period of 2018). The weakened oil price combined with the slightly weakened Russian ruble held the current account surplus in the first six months of 2019 at 5.8% of GDP (first half of 2018: 6.0%). At the same time, net private capital outflows more than doubled to 3.5% of GDP, driven by banks' accelerated build-up of assets abroad and their continued paying-down of external liabilities. Largely on account of nonresidents purchasing Russian obligations, the country's foreign debt expanded to EUR 425 billion in the first six months of 2019 (+7% year on year), which, however, remains relatively modest in relation to GDP (29.7%). Moreover, Russia's foreign debt has been clearly outgrown by its international reserves (including gold, which the authorities stocked up substantially in recent months), which stood at EUR 482 billion in late September 2019 (+14% over six months).

Rapid retail lending growth adds to banking sector fragility

Notwithstanding Russia's sluggish economic growth and its NPL ratio stagnating at a relatively high level (18% at end-July 2019), retail lending (as opposed to corporate lending) continues to expand swiftly (+17% annually at end-June 2019 in real terms and exchange rate adjusted). Although overall household debt in Russia is comparatively low, this strong lending growth raises concern, given that it is partly driven by unsecured consumer credit (+21% annually). In response, the CBR has repeatedly raised risk weights for unsecured lending and announced additional tightening measures.

Table 11

Main economic indicators: Russia

	2016	2017	2018	Q1 18	Q2 18	Q3 18	Q4 18	Q1 19	Q2 19
	Year-on-year change of the period total in %								
GDP at constant prices	0.3	1.6	2.3	1.9	2.2	2.2	2.7	0.5	0.9
Private consumption	–1.9	3.3	2.3	2.7	1.9	2.0	2.6	1.6	2.8
Public consumption	1.5	2.5	0.3	0.3	0.3	0.3	0.3	0.2	0.2
Gross fixed capital formation	1.0	5.2	2.9	3.5	4.2	5.5	0.2	–2.6	1.0
Exports of goods and services	3.2	5.0	5.5	7.2	7.8	4.8	2.6	–0.4	–4.9
Imports of goods and services	–3.6	17.4	2.7	10.0	2.8	0.1	–0.3	–1.6	0.1
	Contribution to GDP growth in percentage points								
Domestic demand	–1.1	3.6	1.5	1.6	0.6	1.4	2.3	0.4	2.3
Net exports of goods and services	1.6	–2.3	0.8	–0.2	1.4	1.2	0.7	0.2	–1.4
Exports of goods and services	0.8	1.3	1.5	2.0	2.1	1.2	0.7	–0.1	–1.4
Imports of goods and services	0.8	–3.6	–0.6	–2.2	–0.7	0.0	0.1	0.4	0.0
	Year-on-year change of the period average in %								
Unit labor costs in the whole economy (nominal, per person)	..	..	..	..	..	..	..	..	..
Unit labor costs in manufacturing (nominal, per hour)	4.3	17.7	2.3	2.7	0.9	2.6	3.3	3.1	4.7
Labor productivity in manufacturing (real, per hour)	4.7	7.5	4.2	5.1	4.5	4.2	3.0	3.3	3.8
Labor costs in manufacturing (nominal, per hour)	9.1	26.7	6.6	7.9	5.4	7.0	6.3	6.5	8.7
Producer price index (PPI) in industry	4.3	7.8	12.0	5.0	12.0	15.9	15.1	9.2	6.6
Consumer price index (here: HICP)	7.1	3.6	3.0	2.3	2.5	3.1	4.0	5.3	5.0
EUR per 1 RUB, + = RUB appreciation	–8.4	12.6	–11.0	–10.6	–14.9	–9.3	–9.4	–6.6	2.0
	Period average levels								
Unemployment rate (ILO definition, %, 15–64 years)	5.5	5.2	4.8	5.1	4.8	4.6	4.8	4.8	4.5
Employment rate (%, 15–64 years)	..	..	..	..	..	..	..	..	..
Key interest rate per annum (%)	10.6	9.1	7.4	7.6	7.3	7.3	7.5	7.8	7.7
RUB per 1 EUR	74.2	65.9	74.1	69.9	74.0	76.3	75.9	74.9	72.6
	Nominal year-on-year change in the period-end stock in %								
Loans to the domestic nonbank private sector[1]	0.6	5.7	12.3	7.3	9.4	11.4	12.3	11.9	11.6
of which: loans to households	1.6	12.7	22.2	15.5	18.8	21.4	22.2	23.5	22.8
loans to nonbank corporations	0.2	3.1	8.3	4.3	5.8	7.5	8.3	7.2	6.9
	%								
Share of foreign currency loans in total loans to the non-bank private sector	18.9	14.7	13.6	14.5	14.7	14.4	13.6	12.2	11.6
Return on assets (banking sector)	1.2	1.0	1.5	1.7	1.5	1.7	1.5	2.5	2.2
Tier 1 capital ratio (banking sector)	9.2	8.5	8.9	9.9	9.0	9.5	8.9	9.6	9.2
NPL ratio (banking sector)	18.9	19.1	18.0	19.4	19.2	18.7	18.0	18.0	18.0
	% of GDP								
General government revenues	32.8	33.7	35.9	..	..	..	..	..	..
General government expenditures	36.4	35.2	33.0	..	..	..	..	..	..
General government balance	–3.7	–1.5	2.9	..	..	..	..	..	..
Primary balance	..	..	..	..	..	..	..	..	..
Gross public debt	12.9	12.6	12.1	..	..	..	..	..	..
	% of GDP								
Debt of nonfinancial corporations (nonconsolidated)	..	..	..	..	..	..	..	..	..
Debt of households and NPISHs[2] (nonconsolidated)	..	..	..	..	..	..	..	..	..
	% of GDP (based on EUR), period total								
Goods balance	7.0	7.3	11.8	11.2	11.4	11.6	12.9	12.6	9.7
Services balance	–1.8	–2.0	–1.8	–1.7	–1.9	–2.1	–1.6	–1.6	–2.1
Primary income	–2.7	–2.7	–2.5	–1.3	–4.6	–2.2	–2.0	–1.2	–4.8
Secondary income	–0.5	–0.6	–0.6	–0.7	–0.4	–0.6	–0.7	–0.7	–0.3
Current account balance	1.9	2.1	6.9	7.6	4.5	6.6	8.7	9.1	2.6
Capital account balance	–0.1	0.0	–0.1	–0.1	–0.1	0.0	–0.1	0.0	–0.1
Foreign direct investment (net)[3]	–0.8	0.5	1.4	1.4	0.6	1.0	2.3	–0.3	–0.2
	% of GDP (rolling four-quarter GDP, based on EUR), end of period								
Gross external debt	41.5	31.1	28.3	30.7	30.7	29.3	28.3	29.7	29.7
Gross official reserves (excluding gold)	25.7	21.3	23.8	22.1	23.7	23.8	23.8	25.2	25.7
	Months of imports of goods and services								
Gross official reserves (excluding gold)	15.0	12.3	13.7	12.7	13.4	13.6	13.7	14.4	14.8
	EUR million, period total								
GDP at current prices	1,171,677	1,396,089	1,399,910	320,790	335,393	355,474	388,253	326,999	360,921

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).