Regional Economic Prospects in

EBRD Countries of Operations: May 2013[1]

EBRD Office of the Chief Economist

Overview

No quick turnaround in sight

The effects of the Eurozone crisis on the transition region appear to be abating, with recovering exports and milder cross-border deleveraging. At the same time, the transition region is being hit by a significant economic slowdown in Russia, and downturns in Poland and Turkey. This has worsened the outlook for neighbouring countries, including Ukraine and in central Asia. Overall, economic growth in the transition region is expected to decelerate further from an already slow rate of 2.6 per cent last year to 2.2 per cent in 2013 – almost a full percentage point lower than our January forecast. A modest recovery to growth of 3.2 per cent is expected next year. A resumption of structural reforms is now urgently needed to pave the way for more robust growth in the future.

Regional overview

Growth across the transition region significantly decelerated last year in the weak external environment stemming from the Eurozone crisis. Notwithstanding recoveries in the three Baltic countries, which posted the strongest growth rates for 2012 in the European Union, **Central Europe and the Baltics** (CEB) as a whole barely grew in the last quarter, due to a further slowdown in Poland, where there is little room left for fiscal stimulus due to constitutional limits, while impetus from EU structural funds has abated. Recessions continued in Croatia, Hungary and Slovenia due in part to home-grown factors. Weak expansion in **South-eastern Europe** (SEE) in the fourth quarter was an improvement over an earlier sharp contraction. As growth has slowed unemployment rates have edged upwards in much of CEB and SEE, and countries that saw a recession in 2012, especially Croatia and Slovenia, also saw a significant increase in youth unemployment.

Recent improvements in exports from the CEB and SEE region suggest that the negative impact of the Eurozone debt crisis on trade may be abating. Exports in the second half of last year grew faster relative to the first half in most of the countries of the CEB and SEE regions, with the Baltic states recording the highest rises (Chart 1). While the increases often followed earlier declines in exports, they are consistent with the view that demand in the Euro area, CEB and SEE regions' main export market, is no longer deteriorating.

[1] This document is provided as a companion to the EBRD's growth forecasts for its countries of operations, which are released four times a year. For more comprehensive coverage of economic policies and structural changes, the reader is referred to the EBRD's Transition Report 2012 as well as country strategies and updates and statistical series on economic and structural reform variables, which are all available on the EBRD's website (www.ebrd.com).

In contrast, remittances, a reliable source of foreign exchange and household income in the past, dropped in many SEE countries, including in Albania and Serbia where they are important as a share of GDP. Recent evidence shows that remittances originating in the Eurozone started declining in the second half of last year. As SEE remittances partly emanate from the weaker peripheral economies of the Euro area, they are likely to continue to drop in 2013, further weakening income and domestic demand.

The Baltic economies are reaping the benefits of the drastic adjustment in their economies following the output collapse in 2009/10. While their economies are still smaller than they were at the peak of the cycle in late 2007 or early 2008, they are enjoying much higher growth than other CEB and SEE countries in which output also remains significantly below its pre-crisis level (for example, Bulgaria, Croatia, Hungary, Romania and Slovenia as well as Ukraine). Internal devaluations in the Baltic states resulted in substantially higher competitiveness. Along with the upgrading of the technology content of industrial production, this has enabled strong export-led growth despite faltering demand from the Eurozone, a key trading partner.

Russia's slowdown is becoming a new source of weakness in the region. The latest data suggest that what until recently may have seemed a temporary weakening has in fact been a trend slowdown in the economy since late 2011 culminating in a mild quarter-on-quarter contraction in the first quarter of this year (see Chart 2). Both weak demand and supply side constraints seem to be at play:

- Slower global demand and associated stagnation of commodity prices and export revenues have likely contributed to lower consumption growth and, with a lag, to the recent disappearance of investment growth. Other factors that may have weakened demand include the slowdown in public social spending growth following last year's elections, and possible dents to investor confidence following setbacks with business environment reforms and the treatment of foreign investors.
- Supply side bottlenecks also seem to have played a role, as employment and capacity utilisation in manufacturing remain at record high levels.

The slowdown in Russia has already started affecting the regions that depend on it. **Eastern Europe and Caucasus** (EEC) contracted sharply at the end of last year mainly due to further output decline in Ukraine, which has also been exposed to the troubles in the Eurozone. The contracting Ukrainian economy is running a substantial external deficit, which may require devaluation. Growth in **Central Asia** slowed down as well, even though it remained at strong levels, and Mongolia and Turkmenistan continued their natural resource-induced boom. At the same time remittances have held up well in these countries after a drop in the aftermath of the 2008/9 crisis and continue to provide vital sources of income and foreign exchange to countries particularly in the Caucasus and Central Asia (Chart 3). Armenia, Moldova, the Kyrgyz Republic and Tajikistan, all countries where remittances represent 15 per cent of output or more, have witnessed increases in remittance flows since the crisis year 2009.

Turkey decelerated more sharply than expected in the second half of last year despite positive contributions from next exports and public spending after a capital inflow-funded credit boom of 2010-11 came to an end. At the same time, Turkey appears to have avoided a hard landing. The external current account deficit remains sizeable, financed mainly by portfolio inflows.

Overall growth in the South-eastern Mediterranean (SEMED) region has also weakened. In Egypt and Tunisia, volatile political and security conditions have weighed on the economy, adversely affecting investor confidence. Morocco and Jordan have been particularly faced with weak external conditions and high commodity prices. Equally important, macro economic imbalances – high twin fiscal and external account deficits - are a particular problem. In Egypt, domestic instability has affected both government finances and sources of foreign financing such as tourism. The complex political situation has complicated reforms such as substantial cuts to fuel subsidies, which could help re-balance the government budget as well as the external accounts and improve price signals in the marketplace. Nevertheless, governments in the SEMED region have made some progress in subsidy reforms, and in all countries measures were taken to increase fuel prices.

Capital inflows

Private capital continued to flow into the region but may be weakening (Chart 4). Total flows into the CEB and SEE regions bottomed out in the second quarter of last year, after which they rose thanks to a return of non-FDI flows in the second half of the year. Nevertheless, the quarterly amounts remain modest at a mere 1 per cent of GDP, as compared to 4 per cent of GDP in pre-crisis 2007. Capital outflows from Russia slowed considerably in most of 2012, perhaps as investor uncertainty calmed down after the March presidential elections. However, recent evidence suggests that outflows from Russia rose again substantially early this year as the country's economic situation weakened. Inflows into Turkey remained elevated, though most of them are more volatile non-FDI portfolio investments. The SEMED region as a whole received modest capital inflows.

Cross-border deleveraging in the transition region as a whole abated towards the end of last year, although it remains significant in a few countries. Survey evidence on credit conditions shows that, for the first time in more than a year, lending conditions in general no longer tightened at the end of 2012. In particular, banks' funding conditions continued to improve throughout the second half of last year thanks to ample global liquidity, including from the ECB's monetary easing since late 2011. Within the region, most recent data suggests that foreign banks stopped withdrawing funding from the CEB region, but deleveraging from the weakly performing SEE region and countries with policy uncertainties seems to be continuing.

Credit growth

Milder cross-border deleveraging has not yet translated into a clear improvement of credit conditions in countries exposed to the Eurozone. Credit is constrained by balance sheet weaknesses related to the dual legacy of the pre-crisis lending boom of high loan to deposit ratios and weak asset quality, including high share of foreign exchange denominated loans and high non-performing loans (NPLs). NPLs increased in many economies, such as Hungary, Romania, Slovenia and

Ukraine as well as most SEE countries (Chart 5). But they continued to decrease in the fast-growing Baltic states, even though they still remain at relatively high levels in Latvia and Lithuania.

Real credit growth has shown significant variations. Credit contractions continued in a number of CEB and SEE countries albeit at a reduced rate, including in recession-stricken Hungary, but they accelerated in others. The already weak credit expansion in Poland has grounded to a virtual halt. Elsewhere, credit growth has slowed down in Turkey as the country's boom wound down and in Russia as its economy decelerated from a year earlier.

Outlook and risks

GDP growth in the transition region is projected to slow down to 2.2 per cent in 2013 before modestly recovering to 3.2 per cent in 2014 (Chart 6). The forecast for this year represents a slowdown relative to the already slow growth of 2.6 per cent in 2012, and also a substantial downward revision relative to our January forecast for 2013, which stood at 3.1 per cent. This is largely driven by the worsening outlook for Russia and its knock-on effects in the EEC region and elsewhere. The deeper-than-expected slowdown in Poland and Egypt's weak outlook are also playing a role.

The region will continue to operate in a weak external environment driven by the on-going Eurozone crisis and the resulting mild recession in the single currency area. The projection assumes a baseline scenario of continued slow and uneven progress towards containment of the Eurozone crisis:

- On the one hand, various earlier policy decisions have reduced the probability of a further substantial deterioration of the crisis, increasing the chances that the single currency area may see a very slow and gradual improvement of its economy in the baseline, notwithstanding the mild contraction for the whole of 2013.
- On the other hand, policy credibility needs to be re-affirmed in the aftermath of the Cyprus crisis with credible actions towards a common resolution framework and banking union. This can in turn ease Europe's current state of heightened financial fragmentation that impedes the optimal allocation of capital across Europe.

Under such a scenario, the Eurozone recession may have already bottomed out and the negative impact of the crisis on the transition region should continue to decrease in magnitude both through the export and the cross-border lending and remittance channels. Moreover, the more stable markets are already benefiting the transition region through lower sovereign borrowing spreads as well as increased corporate debt issuance.

In the baseline scenario, countries that are the most integrated with the Euro area will continue to see weak growth. While feeble demand in the Eurozone may not translate into further decreases in exports from CEB and SEE countries, neither will it spur export growth in 2013. Similarly, thanks to calmer financial markets, cross-country deleveraging may continue to abate. Yet transition countries whose banking systems are deeply integrated with that of the single currency area are unlikely to be able to replace lost funding in the near future with local sources, given limits to rapid deposit increases and still underdeveloped local capital markets.

Therefore credit growth will likely only very slowly return to the CEB and SEE regions.

Several countries have started experimenting with unconventional demand-boosting measures, either through off-budget funds (e.g. Poland) or unorthodox monetary schemes to support SME lending (e.g. Hungary). Their effectiveness will depend, among others, on good institutional setups as well as removing any other major policy obstacles in the way of recovery.

Overall, the CEB region will grow at 0.8 per cent this year before modestly recovering to 1.8 per cent next year. The worse-than-previously-forecast performance this year is a combination of slowing expansions in Poland and the Slovak Republic and deepening recessions in Croatia, Hungary and Slovenia. Growth in the SEE region will reach a modest 1.4 per cent this year and 2.2 per cent next year, up from a very low 0.4 per cent last year.

Economic growth in Russia will likely slow down substantially this year to 1.8 per cent, only partly recovering to 3 per cent in 2014. The recovery in growth performance this year and next assumes that the authorities will use some available policy space to help the economy. In particular, given that inflation has already started to slow, there may be space for some monetary loosening in the coming quarters. Room for fiscal stimulus is limited as oil prices are projected to remain below the budget-balancing break-even level and the government seems firmly committed to its fiscal rule. In any event, supply side constraints may put a limit to policy stimulus, with potential growth now estimated at around 3 per cent. Under these circumstances, growth can be sustainably increased only through pursuing consistent policies to substantially improve the business environment, which is crucial for attracting the necessary foreign and domestic investment that will help diversify the economy.

Regions that are vulnerable to swings in the performance of the Russian economy will also decelerate. In particular, the EEC region will witness a low growth of 1.2 per cent this year as the virtual standstill in Ukraine in 2012 gives way to a small contraction in 2013. Other EEC countries are likely to fare better even though Georgia's prospects have worsened relative to the January forecast. In Central Asia, Kazakhstan's growth forecast has also deteriorated as the impact of weaker growth in Russia will combine with delays in new oil and gas production.

Growth in Turkey is likely to increase to 3.7 per cent this year and further to 4 per cent in 2014 after the sharp slowdown from the country's capital inflow-fuelled boom, but the country's widening current account balance continues to present a risk. Moreover, Turkey depends on the more volatile portfolio flows rather than FDI to fund the deficit. Global funds in search for yield are likely to provide the necessary financing in the short run but may further exacerbate the external imbalance of the economy.

The SEMED region is likely to expand this year at the same rate as in 2012, but growth is projected to pick up in 2014. We have revised growth projections in 2013 since our January forecast as the complex political situation in Egypt and Tunisia affect growth. While all SEMED countries remain vulnerable to external shocks, Morocco is expected to grow at 5 per cent in 2013 thanks to a rebound in agricultural production. While the IMF programmes currently in place in Morocco, Tunisia, and Jordan will help investor confidence and buffer against external shocks, a loan agreement with Egypt is still under negotiation. Reaching an agreement could help cement necessary structural reforms and unlock needed external assistance. Overall, growth in the region would pick up to about 4 per cent in 2014, driven by Egypt's recovery.

A possible further deterioration of the Eurozone crisis still poses the largest downside risk to the outlook. The recent developments in Cyprus served as a reminder that, until the Eurozone policy makers agree on a substantive reform of the single currency area including the establishment of a banking union, a worsening of the crisis is always possible. Moreover, in the absence of more growth-friendly economic policies in advanced Europe, recovery may falter. In a downside external scenario – largely unchanged since October 2011, though at this point substantially less likely – the Eurozone troubles become much worse before they are ultimately resolved. In this scenario, the crisis would spread to larger single currency area members, which in turn renders several large European banks insolvent. Major parent banks would accelerate deleveraging in the region, triggering a credit crunch and recession in emerging Europe. This scenario implies prolonged market turmoil and a severe western European recession with swift negative spill-overs for the global economy, resulting in lower growth in advanced and emerging economies and lower commodity prices. A negative Eurozone crisis scenario would affect CEB and SEE countries via the same channels as in the baseline, including depressed exports and financing inflows, only more severely. Substantially lower commodity prices in the downside scenario would also cause a more severe slowdown in Russia and other CIS commodity exporters. The weaker Russian economy would in turn seriously impact the non-commodity exporting countries of the CIS.

Growth in real GDP

(In per cent; EBRD forecasts as of 26 April 2013)

	Current forecast			EBRD Forecast in January 2013			
	2012	2013	2014	2012	Change January-April	2013	Change January-April
Central Europe and the Baltic states							
Croatia	-2.0	-0.3	1.9	-1.9	-0.1	0.8	-1.1
Estonia	3.2	3.0	3.1	3.3	-0.1	3.1	-0.1
Hungary	-1.7	-0.8	0.9	-1.5	-0.2	-0.1	-0.7
Latvia	5.6	3.5	3.2	5.4	0.2	3.0	0.5
Lithuania	3.6	2.8	3.0	3.2	0.4	2.9	-0.1
Poland	1.9	1.2	2.0	2.0	-0.1	1.5	-0.3
Slovak Republic	2.0	1.0	2.0	2.2	-0.2	1.7	-0.7
Slovenia	-2.3	-2.5	-0.9	-2.1	-0.2	-2.0	-0.5
***Average*[1,2]**	***1.1***	***0.8***	***1.8***	***1.3***	***-0.2***	***1.2***	***-0.4***
South-eastern Europe							
Albania	1.6	1.5	1.9	1.8	-0.2	2.0	-0.5
Bosnia and Herzegovina	-0.5	0.1	1.8	-0.5	0.0	0.6	-0.5
Bulgaria	0.8	1.0	2.5	1.1	-0.3	1.9	-0.9
FYR Macedonia	-0.3	1.5	2.6	-0.5	0.2	1.8	-0.3
Kosovo	2.5	3.0	3.5	2.5	0.0	3.0	0.0
Montenegro	-0.5	1.0	2.0	0.3	-0.8	0.8	0.2
Romania	0.7	1.4	2.2	0.3	0.4	1.4	0.0
Serbia	-1.7	2.2	1.9	-1.9	0.2	2.1	0.1
***Average*[1]**	***0.3***	***1.4***	***2.2***	***0.1***	***0.2***	***1.5***	***-0.1***
Eastern Europe and the Caucasus							
Armenia	7.2	5.0	4.0	6.0	1.2	5.0	0.0
Azerbaijan	2.2	3.5	4.0	2.2	0.0	4.0	-0.5
Belarus	1.1	2.0	2.5	1.5	-0.4	1.5	0.5
Georgia	6.2	3.0	5.0	6.5	-0.3	5.0	-2.0
Moldova	-0.5	2.5	4.0	0.0	-0.5	3.0	-0.5
Ukraine	0.2	-0.5	2.5	0.0	0.2	1.0	-1.5
***Average*[1]**	***1.2***	***1.2***	***3.0***	***1.2***	***0.0***	***2.1***	***-0.9***
Turkey	2.2	3.7	4.0	2.6	-0.4	3.7	0.0
Russia	3.4	1.8	3.0	3.5	-0.1	3.5	-1.7
Central Asia							
Kazakhstan	5.0	4.9	5.5	5.0	0.0	6.0	-1.1
Kyrgyz Republic	-0.9	6.5	5.0	-0.9	0.0	7.0	-0.5
Mongolia	12.3	16.0	17.0	11.0	1.3	16.0	0.0
Tajikistan	7.5	5.0	5.0	7.5	0.0	5.0	0.0
Turkmenistan	11.1	10.0	10.0	11.1	0.0	10.0	0.0
Uzbekistan	8.2	7.5	7.0	8.2	0.0	7.0	0.5
***Average*[1]**	***6.3***	***6.2***	***6.6***	***6.2***	***0.1***	***6.9***	***-0.7***
Average EBRD region (excluding SEMED) [1]	***2.5***	***2.1***	***3.1***	***2.6***	***-0.1***	***3.0***	***-0.9***
Southern and Eastern Mediterranean							
Egypt	3.1	2.0	3.6	3.1	0.0	3.8	-1.8
Jordan	2.7	3.0	3.4	2.6	0.1	3.0	0.0
Morocco	2.4	5.0	5.2	2.6	-0.2	5.2	-0.2
Tunisia	3.7	3.8	4.3	2.4	1.3	3.0	0.8
***Average*[1]**	***3.0***	***3.0***	***4.1***	***2.9***	***0.1***	***4.0***	***-1.0***
Average EBRD region (including SEMED) [1]	***2.6***	***2.2***	***3.2***	***2.6***	***0.0***	***3.1***	***-0.9***

[1] Weighted averages. The weights used for the growth rates are WEO estimates of nominal dollar-GDP for 2011.
[2] Weighted averages do not include the Czech Republic, for which EBRD no longer produces a forecast.

Chart 1. Exports
(Last 6 months / previous 6 months, % diff. from 100%)

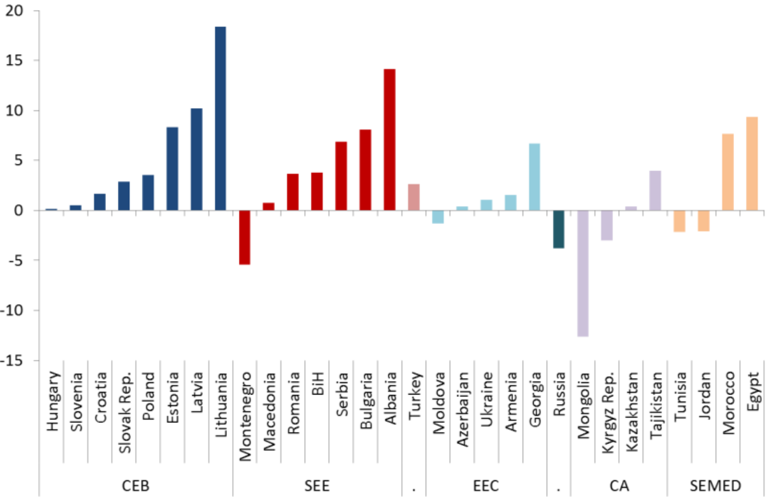


Chart 2: Real output growth in Russia and its components
(Quarter-on-quarter, seasonally adjusted, %)

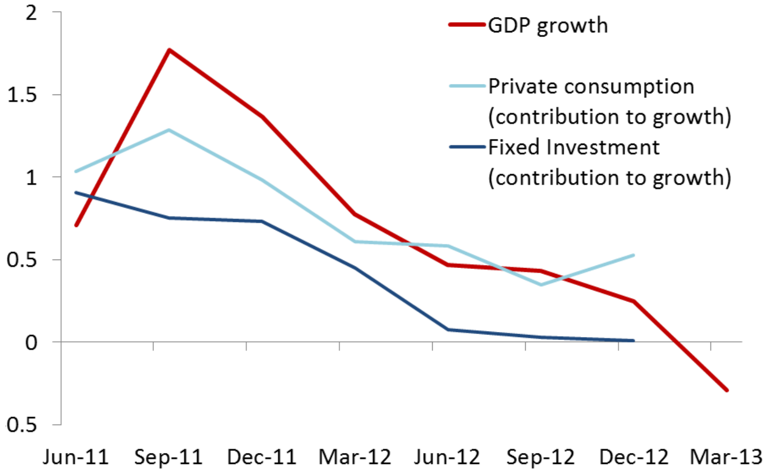


Chart 3. Remittances
(as % of GDP)

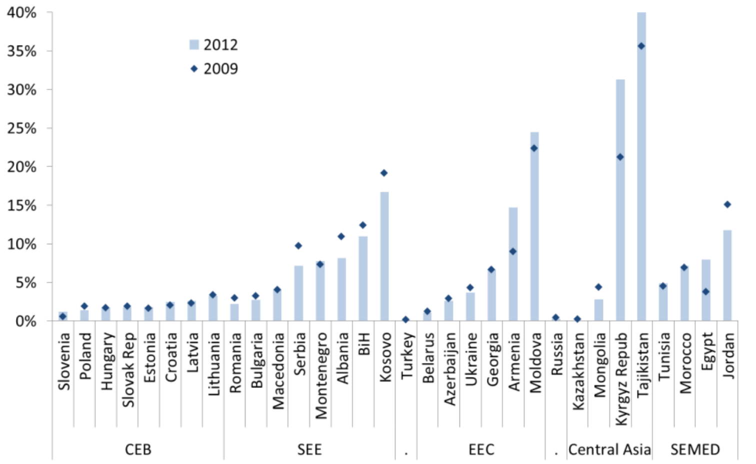


Chart 4. Private capital flows
(as % of 2011 GDP)

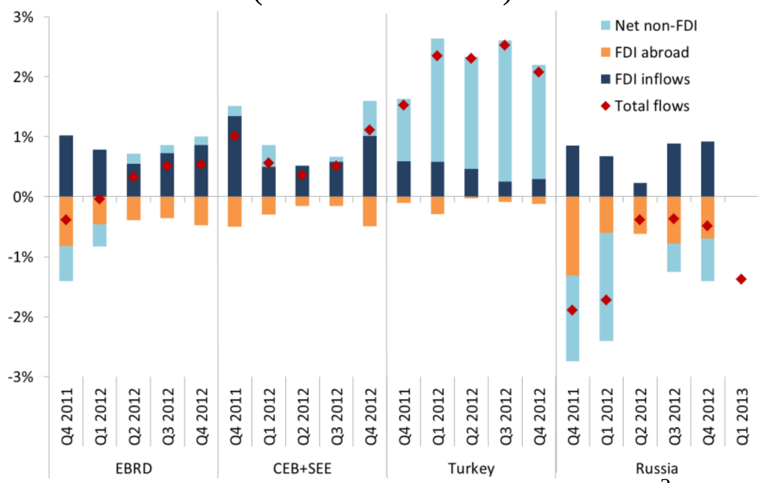


Chart 5. Non-performing loans
(% of all loans)

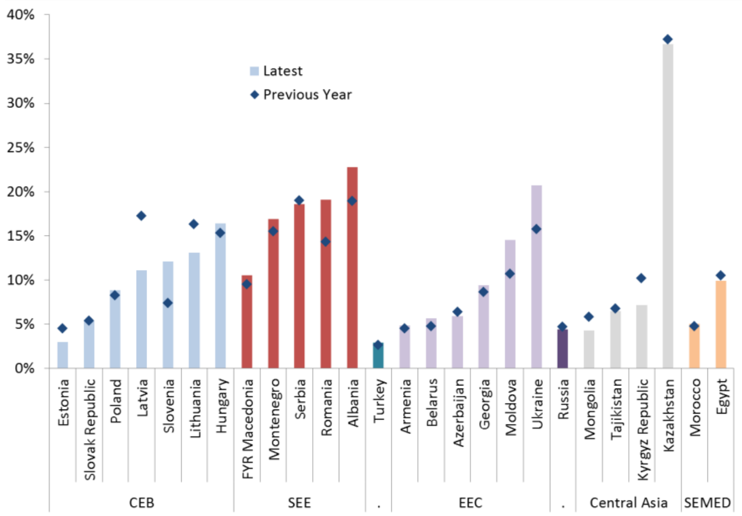
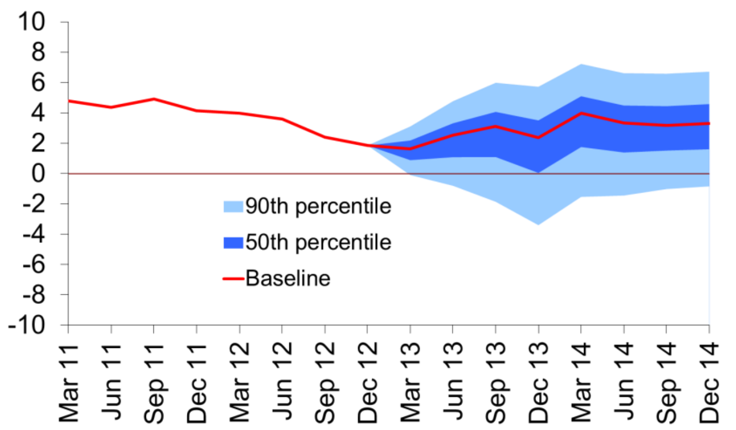


Chart 6. Transition region real GDP Growth[2]
(%, quarterly, year-on-year)



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[2] Y-o-y growth in aggregate real GDP of transition countries. The fan-chart is based on a Bayesian Vector Autoregression Model The baseline scenario assumes Eurozone real GDP growth of -0.3% in 2013, VIX around 17 in 2013, and an oil price of about US$100 per barrel. The downside scenario assumes a recession in the Eurozone, with growth of -2 per cent in 2013 and more volatile market, with VIX averaging 40 in the third quarter of 2013 and then slowly declining at the end of the year.

Central Europe and the Baltic States (CEB)

The eight countries in the central Europe and Baltic states region continue to show divergent growth patterns. While the Baltic states are all growing strongly, growth in Poland and the Slovak Republic has now sharply slowed and three countries (Hungary, Slovenia and Croatia) remain mired in recession. In the low growth environment and with no more fiscal policy room, several authorities are experimenting with novel ways to boost investment and lending (such as off-budget investments funds as in Poland or special lending schemes through the central bank as in Hungary).

- The **Baltic economies** have remained resilient throughout 2012, with Latvia registering the highest growth rate in the EU (at 5.6 per cent), and Lithuania and Estonia not too far behind (at 3.6 and 3.2 per cent respectively). Competitiveness gains with steady rises in market shares, along with the upgrading of the technology content of industrial production, have sustained this growth, in the face of a faltering Eurozone. This strategy is likely to be somewhat impacted from the slowdown in key export markets in Scandinavia, Russia and Poland. Projections for this year for Lithuania and Estonia remain roughly unchanged from January (at 2.8 and 3 per cent respectively), though they are slightly upgraded for Latvia (to 3.5 per cent). Bank and corporate balance sheets are being cleaned up and the share of non-performing loans is reducing (albeit still at elevated levels), but the resulting credit contraction masks healthy credit to the corporate sector for example in Latvia.

- Growth in **Poland** in 2012 fell to 1.9 per cent, the lowest since 2009. Indicators of industrial production in the first quarter (falling by 2 per cent over the previous year), and slight drops in retail sales and exports over the same period underline that this weakness extended into this year, and the EBRD has once again cut its growth projection for 2013 to now 1.2 per cent. It is increasingly evident that resilience to the European recession in 2009, and elevated growth rates of over 4 per cent in 2010-11, were due to a number of transient factors, including the rapid absorption of EU structural funds and the ensuing boom in public investment. Public investment has been contracting in annual terms since early 2012. Reversing an earlier tightening the National Bank started in November 2012 a rapid loosening in the monetary policy stance, with a cumulative reduction in the base rate of over 150 basis points since then. Also regulatory lending standards applied to consumer credit were made less onerous. However, given weaker than expected growth, missing of successive deficit targets and being close to legal debt limits, there is an on-going programme of fiscal consolidation. The government's attempt to counteract the weakness in public investment, the *Polish Investments* off-budget vehicle for infrastructure and energy investment, is not likely to become effective until next year.

- The **Slovak Republic** similarly experienced a slowdown in industrial production in late 2012 and early this year. Weakness in the very concentrated export sector belatedly became apparent. In addition, domestic firms had to adapt to changes in the labour code, and modifications to Slovakia's traditionally very low corporate tax rate. A relatively moderate tax on banks remains in effect. Growth this year is set to fall to about 1 per cent only before picking up next year as confidence returns to the export sector. As in Poland, the government is considering a number of initiatives to stimulate investment, though these are unlikely be effective in the near term.

- Last year’s contraction in **Hungary** was worse than anticipated, with a poor fourth quarter taking the growth average to minus 1.7 per cent. Despite the long-planned capacity expansion of two prominent foreign-owned car manufacturers industrial production dropped slightly for last year as a whole, and was again negative in annual terms in the first quarter of 2013. Domestic demand continued its slide, with fixed investment now back to levels last seen over 14 years ago. In real terms the capital stock is now declining. Measures announced by the new central bank governor in early April are to make interest free loans available to banks for on-lending to SMEs. This is unlikely to reverse investment trends unless business confidence and the investment environment improve. At the same time, the government pressed on with its fiscal consolidation and the general government deficit was reduced to under 2 per cent of GDP last year. This depresses domestic demand in the short run, though may enhance confidence in light of the country's public debt of just under 80 per cent of GDP, one of the highest in the transition region. The 2013 budget presented in April did not include additional revenue measures, and the budget is likely to miss the EU targets.. Hungary has had an unbroken history within the EU’s excessive deficit procedure since EU accession in 2004. Remaining within that mechanism would significantly constrain the scope for expenditure policies ahead of the 2014 elections.

- GDP figures in **Slovenia** in late 2012 – showing an aggregate contraction by about 3 per cent compared to a year earlier – underlined renewed weakness, in particular in domestic demand. Exports suffer from recessions in principal markets, such as Italy and the western Balkans. The contraction in investment levels shows no signs of abating – it is almost 9 per cent below a year earlier, and over 40 per cent below the levels three years ago. The government that took office in March this year is committed to pursuing key reform steps such as the bank asset management company and the state asset holding, though implementation risks remain high. The recession is set to continue throughout this year as the severe crisis of the banking and corporate sector persists.

- **Croatia** continues to be in recession with negative growth of around 2 per cent in 2012 (notwithstanding the uptick in Q3), and the prospect of another year of falling GDP in 2013. The economy remains weighed down by long-standing problems of uncompetitive industries, labour market inflexibility and a large and inefficient public sector. The country’s accession to the EU from July 01 2013 provides an opportunity to benefit from full access to the single market and to substantial EU funds, but an acceleration of reforms is needed to benefit fully from EU membership.

South-Eastern Europe (SEE)

South-eastern Europe continues to face serious economic difficulties and risks. Overall, the region recorded only minimal growth in 2012 and, although prospects for 2013 are slightly better, there are no major internal or external growth drivers at present. Remittances, a major source of income and foreign exchange in many West Balkan countries, have fallen due to the crisis in the euro zone, from where most of the remittance flows to the region originate, though still significant. It is increasingly recognised that the region will have to rely more on its own resources and an enhanced reform agenda if it is to move to a sustainable growth path. So far, however, reform efforts have been hesitant and constrained by the difficult economic environment. SEE remains vulnerable to weaknesses in the Eurozone, the main export market. Financial sector risks are also significant, given the high level of non-performing loans in several countries and the possibility of contagion from peripheral Eurozone economies.

- **Albania's** economy slowed down significantly in 2012, although growth was still higher than in other countries of the region except Kosovo. Fiscal and monetary buffers have been largely exhausted and the banking sector has a large proportion of non-performing loans and remains vulnerable to external contagion. These risks have been managed prudently so far, and good efforts have been made by the authorities to keep inflation and the fiscal deficit under control.

- **Bosnia and Herzegovina's** economy has shown few signs of vitality in the past year, with growth in 2012 estimated to have been slightly negative, and prospects for this year are little better. However, the authorities have shown a commitment to macroeconomic stability by adhering to commitments so far under the Stand-By Arrangement with the IMF, approved in September 2012.

- **Bulgaria** continues to perform well in terms of fiscal prudence, with an almost balanced budget in 2012 despite sluggish growth. Social discontent has been increasing, as evidenced by the massive street protests earlier this year that led to the resignation of the government. A modest increase in growth, possibly combined with some slight fiscal loosening, is likely in 2013 and 2014.

- **FYR Macedonia** was affected significantly by the Eurozone crisis in 2012, which weakened demand for exports and led to a drop in investment and remittances. As a result, GDP growth was marginally negative. However, the country has made strong efforts in recent years to improve the business environment and defy global trends by attracting much-needed FDI. These efforts should help growth to pick up this year and beyond.

- Economic growth in **Kosovo** in 2012 was the highest in the region, but the country also remains the poorest in SEE, with unemployment and poverty at elevated levels. The macroeconomic environment is stable, assisted by an IMF Stand-By Arrangement, and the business environment is improving, but Kosovo has major investment needs across the whole economy.

- **Montenegro's** economy suffered a downturn in 2012, after reasonable growth in the previous two years, as a result of both declining external demand and weak internal demand. The future of the large aluminium conglomerate, KAP, remains uncertain. On the positive side, FDI has held up well and the twin achievements in 2012 of WTO accession and the start of EU membership negotiations should bring longer term benefits to the country.

- The slowdown in the eurozone and a significant drop in agricultural output have had significant dampening effects on **Romania's** economy in 2012, resulting in growth of less than one per cent. However, the country maintained good macroeconomic discipline, despite it being an election year, and growth is likely to pick up this year on the back of a modest recovery in domestic demand and confidence.

- **Serbia's** economy is vulnerable on several fronts at present. Real GDP fell by 1.7 per cent in 2012, reflecting low domestic demand, fallout from the Eurozone crisis (which affected export demand), and a very poor harvest because of drought. Inflation is at double-digit levels, though it is likely to fall significantly in the second half of the year, and public debt has risen close to 60 per cent of GDP, well above the administrative limit of 45 per cent. The banking sector remains liquid and reasonably capitalized but non-performing loans are a major problem. Discussions are ongoing with the IMF on a possible new arrangement. Notwithstanding the present economic difficulties, growth is likely to return in 2013 on the back of a better agricultural season, a strong boost from car exports and a resumption of steel production at the country's main steel plant.

Turkey

After a strong performance in 2010 and 2011, the Turkish economy slowed down significantly last year as real GDP growth dropped to 2.2 per cent from 8.8 per cent a year earlier. The drop in growth was a result of weak domestic demand and manufacturing activity, coupled with a large drop in private sector capital investments. This slowdown occurred despite positive contributions to growth from public spending and net exports. More recent higher frequency data indicate a pick-up in domestic demand in Q1 2013, driven by higher credit growth and slowly expanding industrial production, while an accommodative monetary policy should support activity in the coming months. However, exports, which have been the major contributor to growth in the last five quarters, are showing signs of weakening. Over the past year, decelerating imports and strong export growth and tourist revenues had helped bring down the current account deficit to a more sustainable level around 6 per cent of GDP. Inflation is proving stubborn, having reached 7.3 per cent y-o-y in March 2013, significantly above the central bank's target of 5 per cent.

Growth in 2013 is likely to increase, but macroeconomic risks remain. Imports have visibly picked up in the first few months of this year, while exports have slowed down, and the current account deficit has widened again in the first two months of 2013. Most importantly, funding remains relatively short-term and dependent on portfolio flows, which are vulnerable to shifts in global market sentiments. FDI inflows fell by around a third over the past year and covers only 17 per cent of the current account deficit. While the global hunt for yield continues to help Turkey meet its external financing requirements, it could exacerbate the risk of high credit growth leading to an even wider current account deficit.

Eastern Europe and the Caucasus (EEC)

Regional vulnerabilities in this region remain significant due to the reliance on external demand (both from the EU and Russia) to support growth, terms of trade pressures (as all countries except for Azerbaijan are net energy importers, and the Caucasus countries depend on import of foodstuffs), and volatility of remittances (Armenia, Georgia and Moldova). Risks to the outlook are related to developments in external demand, commodity prices, and stability of the domestic and, in some cases, broader European financial sectors, as well as domestic policy slippages. The latter may in some cases threaten the delivery of needed international support and could re-ignite balance-of-payments pressures.

- **Ukraine**'s economy has been affected by the difficult external environment but also by domestic policy uncertainty in some critical areas. Lower external demand and subdued steel and other commodity prices led to a contraction of machine building, steel and chemicals sectors. The construction sector continued to decline following completion of significant public infrastructure investments related to the Euro-2012 football championship. Consumer demand, fuelled by rising real wages through 2012, is showing signs of a slowdown. Following a period of tight monetary conditions, the central bank allowed interest rates to decline, and lending has shown early signs of recovery. Agricultural output, which suffered from adverse weather conditions in 2012, has also started to recover. In 2012 the National Bank lost about a quarter of gross external reserves which now cover less than three months of projected imports. Ukraine's economy is very much exposed to developments in the Eurozone and Russia, and the slowdown in both will continue to negatively affect the country's growth and economic stability.
- **Armenia**'s output growth has accelerated, led by manufacturing and mining. The authorities are pursuing fiscal consolidation and structural reforms under an IMF-supported programme. The economy continues to benefit from large remittance inflows and substantial official financing. Immediate risks are related to the uncertain external environment, in light of the country's dependence on remittances and export concentration, and financial sector dollarization.
- After recovering from a deep, policy-induced crisis of 2011, the economy of **Belarus** has been unable to sustain momentum. Domestic investment and construction had to be curtailed as the government cut back on the direct investment programmes. Industrial production also slowed down, likely due to falling external demand. Domestic consumption grew fast in mid-2012 after the authorities implemented significant public wage increases, but slowed down more recently. As inflation pressures subsided, the central bank has been able to steadily reduce the policy rate. Soft loans from a CIS stabilization fund and bilateral loans as well as windfall hydrocarbon revenues from Russia have been used to increase critically low external reserves.
- After two years of fast paced recovery from the financial crisis, **Moldova**'s output growth came to a halt in 2012 in response to the weakening external demand and unfavourable weather conditions. Short-term growth prospects are uncertain and depend on the evolution of remittances, exports and investment sentiment.
- **Georgia**'s economic growth slowed down at the end of 2012, likely due to lower investment and uncertainty related to post-election political transition. As the external financing package mobilised by a range of donors during the twin crises of 2008 has largely been exhausted, the new authorities' challenge will be to mobilise private sources of financing for supporting investment in key sectors. Uncertainty about the external environment has been mitigated by

a precautionary arrangement with the IMF. Further normalisation of trade relations with Russia should help support export-led growth over time.

- After successfully weathering the financial crisis, **Azerbaijan**'s economy has slowed as the pace of oil extraction decelerated. The decline of oil output has been more than offset by the encouraging growth of the non-oil sector, led by construction and services. The lack of diversification of the economy remains important as risks associated with high oil dependence became apparent during the 2008-9 crisis, when oil prices declined. Some recovery of the oil sector and continued expansion of the non-oil economy should lead to an acceleration of output growth in 2013. Immediate macroeconomic risks continue to be mitigated by a very strong fiscal position including from oil reserves.

Russia

Economic growth in Russia ground to a halt in Q1 2013. GDP growth fell to an estimated 1.1 per cent year-on-year during the first quarter of 2013 (a quarterly contraction when correcting for seasonality), from around 5 per cent a year earlier. When looking at high frequency seasonally adjusted data, it becomes apparent that the slowdown started in fact already in Q4 2011, and appears to have been driven mostly by a fall in domestic demand, as indicated by slowing private consumption, investment, imports, and inflation. While the slowdown was initially driven by slowing consumption, it has now increasingly been driven by slowing investment as well.

Part of the slowdown can be attributed to the deteriorating external environment. First, the Eurozone crisis negatively affected consumer and investor confidence worldwide, with Russia not being an exception. Second, the fact that oil prices stopped growing naturally contributed to a slowdown in export and tax revenues, which in turn may have affected public and private spending on non-tradables and investment. Finally, the global slowdown has reduced returns on, and valuations of, foreign assets, again contributing to lower demand.

However, part of the slowdown appears to be the result of domestic supply and demand factors. Supply-side bottlenecks have likely started to constrain growth, given that capacity utilisation in manufacturing has remained high at around 80 per cent for the past two years, while official unemployment remains low at around 5½ per cent. On the fiscal side, there has been a slowdown in social expenditure following the pre-election surge, while public investments were cut at the expense of increased defence spending. On the monetary side, the CBR may have resisted policy rate cuts for too long, as inflationary risks now seem to have abated. In addition, wealth effects may have played a role, as Russian equity values have fallen by about 30 per cent on average since mid-2011, while housing price growth has slowed since early 2012. Finally, investor confidence has likely been dented following the TNK-BP buyout by Rosneft and other setbacks with business environment and civil society reforms. This could also help explain the pickup in net capital outflows to US$ 26 billion in the first quarter of 2013.

Looking forward, GDP growth is expected to recover slightly but remain subdued. Even when assuming a gradual recovery through 2013, GDP growth for the year is unlikely to exceed 2 per cent in 2013 but may increase to 3 per cent in 2014. Growth could be higher in case of substantial fiscal loosening, but prospects for such loosening are limited given the government's appropriate commitment to its fiscal rule, plus the fact that oil prices are projected to remain below the budget-balancing break-even level of US$ 115. With inflation slowing, there may be some space for monetary loosening even within the current inflation targeting framework. The most effective way to stimulate growth, however, is to speed up reforms to radically improve the business environment and the investment climate, particularly for foreign investors.

Central Asia

In most of Central Asia, economic growth continued decelerating in response to the global economic slowdown. The deepening slowdown in Russia may have a further negative impact on growth in this region, mainly through the impact on remittance flows, which have so far performed strongly. However, large natural resource exploration projects remain broadly on track throughout the region, despite certain delays, and are expected to make a sizable contribution to growth in 2013 and over the medium term.

- In **Kazakhstan,** GDP growth slowed from 7.5 per cent in 2011 to around 5 per cent in 2012 and 4.5 per cent in the first quarter of 2013 owing to more difficult external environment. It is expected to remain around this level in 2013, as production capacity at new oil and gas fields may come on stream slower than originally expected. In March 2013 Unicredit sold ATF Bank, its Kazakh Subsidiary, to local buyers. More broadly, the banking sector remains weak, suffering from overhang of non-performing loans. Inflation has accelerated somewhat, to around 7 per cent in March 2013, but remains broadly within the targeted range.

- In the **Kyrgyz Republic,** a strike and weather-related disruption at the Kumtor gold mine in early 2012 caused a significant temporary drop in gold production and resulted in an output contraction of around 1 per cent for the year as whole. Given the one-off nature of the disruption, output rebounded strongly in the first quarter of 2013 and growth is expected to reach 6.5 per cent for 2013 as a whole, reflecting the base effect, before subsequently moderating. Inflation picked up from around 2 per cent in August 2012 to 7.9 per cent in March 2013 owing to higher food prices but is expected to slow down.

- In **Tajikistan**, GDP growth remained strong at 7.5 per cent in 2012, broadly unchanged from 2011. However, growth is expected to slow down to 5 per cent in 2013 on account of slowing remittances, particularly from Russia. Moreover, the growth outlook in Tajikistan is particularly uncertain given fundamental weakness of the banking system and continued tensions with Uzbekistan that may lead to further interruptions in gas supplies and railway shipments. Inflation picked up somewhat from 5 per cent in August 2012 to around 6.4 per cent in March 2013 owing to higher food prices.

- **Turkmenistan** continues to experience a buoyant economic expansion with GDP growth of 11.1 per cent in 2012, driven by large public construction projects and increased gas exports to China and Iran. GDP growth is expected to reach 10 per in

2013 and remain strong over the medium term, supported by exploration of Turkmenistan's abundant gas reserves and further diversification of export routes.

- **Uzbekistan**'s GDP growth remained strong at 8.2 per cent in 2012 largely driven by public spending, diversification of gas export routes and accommodating monetary conditions. Growth is expected to slow down somewhat to around 7.5 per cent in 2013.
- **Mongolia** continued to benefit from a mining boom, with GDP growth of 12.3 per cent in 2012. Growth is projected to pick up again in 2013, to 16 per cent, as the first phase of Oyu Tolgoi, one of the world's largest copper mines, comes on stream. Substantial mining-related FDI inflows, which exceeded 35 per cent of GDP in 2012, are expected to continue for a number of years. Inflation remains high at around 10 per cent at end-March 2013 and may accelerate further given the highly procyclical fiscal policy.

Southern and Eastern Mediterranean (SEMED)

Economic growth momentum has slowed down across the SEMED countries, while unemployment, especially among the youth, remains a chronic problem in all four countries and has remained persistently high in 2012. Fiscal deficits have widened across all SEMED countries as governments continue to increase spending on wages social benefits, and subsidies, at the expense of much needed public investment,. However, governments across the SEMED countries have begun taking positive steps in subsidy reforms, undertaking various measures to raise the prices of fuel for consumers and businesses. Growth for the region as a whole is expected to remain muted in 2013, picking up only in 2014. In Egypt and Tunisia, protracted political transitions are expected to continue to weigh on growth and investor confidence in the near term. In Jordan and Morocco, the external environment will be a key factor in economic recovery.

- Economic recovery in **Egypt** continues to face significant headwinds. The renewal of political turmoil and widespread protests are likely to weigh on the Egyptian economy, disrupting normal business activity, and adversely affecting tourism and business confidence. Real GDP growth fell to 2.2 per cent in Fiscal Year (FY) 2011-12 (which runs from July to June), and has grown by a modest 2.1 per cent in the first half of FY 2012-13. This economic performance falls well below the estimated growth rate of 6-7 per cent required for Egypt to keep the unemployment rate unchanged. As a result unemployment continued rising, reaching 13 per cent in the last quarter of 2012. The fiscal deficit reached 11 per cent of GDP in FY 2011-12, and continued to widen in the first half of FY 2012-13 on the back of higher spending on wages, social benefits, and fuel subsidies. Egypt's balance of payments remains under significant pressure, mostly due to weak capital inflows, slow export growth, and a surge in imports partly reflecting high energy import costs and a depreciating currency. Foreign reserves are barely enough to cover three months of imports. The currency depreciation has also led to a spike in inflation, leading the central bank to institute an across-the-board interest rate hike for its key policy rates, despite weak economic performance. The continued deterioration of macroeconomic fundamentals has exhausted almost all available policy space, and the lack of political consensus has prevented the enacting of much needed economic reforms.

- The **Jordanian** economy continued to grow at a lacklustre pace in 2012, amid on-going regional and external shocks. Real GDP growth was 2.7 per cent in 2012, only slightly higher than 2.6 per cent in 2011. Jordan's vulnerability to its external environment has intensified balance of payments pressures, made worse mostly by the disruption of the flow of natural gas and higher oil prices and the regional turmoil in neighbouring Syria. As a result, the current account deficit has widened to 18.1 per cent of GDP in 2012, up from 12 per cent in 2011. The fiscal deficit (excluding grants) also worsened from 6.8 per cent of GDP in 2011 to 8.2 per cent in 2012. A three-year US$ 2 billion IMF loan is underpinned by a fiscal consolidation programme centred on energy subsidy reform to ease both fiscal and balance of payments pressures.

- In **Morocco,** economic activity slowed down during 2012 after robust growth in 2011. Growth remained below potential, falling from 5.0 per cent in 2011 to 2.4 per cent in 2012, and continues to be adversely affected by the weak economic performance in the Eurozone. Agricultural production (which accounts for 15 per cent of GDP) has suffered from drought and has been the leading cause of weaker household consumption, as the sector accounts for around 40 per cent of employment. However, non-agricultural production held up, underpinned by strong performance in the telecommunications and energy sectors, as well as in the services sector, which is the fastest-growing employment sector. The current account deficit widened from 8.1 per cent of GDP in 2011 to 9.9 per cent in 2012 due to high oil prices and a weak external demand for Moroccan exports. However, official reserves have stabilised at around four months of imports. The fiscal position has worsened markedly in 2012, with preliminary data indicating a fiscal deficit amounting to 7.4 per cent of GDP, well above the government's target of 5 per cent of GDP. The IMF's US$ 6.2 billion Precautionary Liquidity Line provides a safety net. A pickup in agricultural activity after the severe droughts of 2012 is expected to boost growth this year, but any prolonged weakness in the external environment will remain a downside risk.

- **Tunisia**'s volatile political and security conditions, along with weak external environment, have adversely affected the economy. After contracting in 2011, real GDP grew by 3.6 per cent in 2012, largely the result of favourable base effects, but remains below a historical average of 4.4 per cent over the last decade. The current account deficit widened from 7.4 per cent of GDP in 2011 to an estimated 8.1 per cent of GDP in 2012, driven by export growth slowdown due to weak demand from Europe while imports rose sharply, affected especially by high oil prices. Higher current spending on wages, subsidies and social benefits have increased the fiscal deficit as well. The government has, however, begun implementing some reforms to alleviate budget pressures. The authorities reached an agreement in April with the IMF on a two-year US$ 1.75 billion Stand-by Arrangement.

Table 1. Transition Region: Vulnerability Indicators 1/

	Public and External Debt /2 (% of GDP)				Gross reserves /2				Bank dep. (latest)	Loans/ dep. (latest)	Country risk			Domestic FX loan stocks (latest) (% GDP)				Nonperforming loans /3	Unem-ployment
	Government (end 2012)	External				in percent of					25-Apr-13	Latest			of which				
		Total (end 2012)	Private (end 2012)	Short term (remaining maturity)	billions US$ (latest)	GDP	Short term debt	month of prosp. Imports	% of GDP	Private sector, in %	(CDS spread, bps)	S&P sovereign country ratings	Fitch sovereign country ratings	Total pvt sector	Corp.	HH	% FX credit in total loan stock	latest	% (latest avail.)
Central Europe and Baltics																			
Croatia	56.3	105.9	84.0	31.1	14.6	25.8	83.0	7.0	64.2	108.4	298.8	BB+	BBB-	45.4	16.3	29.0	71.2	13.8	18.0
Estonia*	8.5	93.0	87.0	53.0	…	…	…	…	49.9	156.1	…	AA-	A+	1.9	1.9	0.0	2.2	3.0	9.9
Hungary	79.2	129.7	75.0	31.1	46.9	37.3	120.1	5.0	42.8	117.7	311.4	BB	BB+	27.0	13.1	14.0	56.0	16.4	11.2
Latvia	36.4	139.8	106.7	61.5	7.1	25.0	40.6	4.2	33.8	177.8	115.3	BBB	BBB	53.5	26.6	27.0	86.1	11.1	14.3
Lithuania	39.6	73.4	42.6	29.6	8.7	20.6	69.7	2.9	36.9	126.4	…	BBB	BBB+	34.1	17.6	16.5	72.1	13.1	13.1
Poland	55.2	68.4	42.4	19.2	101.8	20.8	107.9	5.3	44.6	110.0	81.1	A-	A-	15.6	3.7	11.9	31.5	8.9	10.6
Slovak Republic*	52.1	77.3	33.5	54.1	…	…	…	…	48.1	96.1	84.5	A	A+	0.3	0.3	0.0	0.6	5.3	14.6
Slovenia*	54.1	131.3	65.7	22.1	…	…	…	…	53.2	145.8	…	A-	A-	3.6	0.7	2.9	4.4	17.0	9.7
South-Eastern Europe																			
Albania	60.6	37.9	10.6	3.2	2.5	19.8	617.8	4.3	67.2	58.9	…	B+	…	24.7	19.0	5.8	62.4	22.8	12.8
Bosnia and Herzegovina	44.3	52.6	24.3	14.0	4.2	24.8	177.4	4.5	42.2	137.3	…	B	…	36.2	19.1	17.1	66.8	13.5	28.0
Bulgaria	18.5	102.7	94.0	38.7	16.2	31.9	82.4	5.3	63.5	108.4	102.6	BBB	BBB-	44.0	34.2	9.8	63.5	16.6	12.5
FYR Macedonia	33.3	67.1	45.1	27.6	2.6	26.8	97.1	3.7	51.0	93.8	…	BB	BB+	25.7	16.8	8.9	54.3	10.6	30.6
Kosovo	17.0	…	…	…	1.2	…	…	3.7	41.0	115.2	…	…	…	35.6	24.6	11.0	…	7.0	45.4
Montenegro	51.1	109.3	…	…	0.5	10.9	…	1.9	52.3	101.9	…	BB-	…	52.6	…	…	…	16.9	14.1
Romania	37.8	77.3	50.7	27.4	42.6	25.2	92.0	6.3	33.3	112.6	201.7	BB+	BBB-	24.4	12.2	12.2	62.3	19.1	6.7
Serbia	59.3	85.9	…	…	13.4	34.9	242.6	6.6	41.2	134.2	…	BB-	BB-	40.6	27.9	12.7	71.6	18.6	22.4
Eastern Europe and the Caucasus																			
Armenia	44.3	78.9	40.8	5.5	1.8	18.0	328.9	4.1	21.5	174.9	…	…	BB-	23.6	19.0	4.6	65.3	4.9	5.9
Azerbaijan	11.6	9.2	…	…	12.5	18.1	…	6.7	14.7	143.8	…	BBB-	BBB-	6.5	3.8	2.5	33.0	5.9	5.4
Belarus	40.9	55.4	31.6	27.4	5.8	9.2	33.5	1.4	24.2	155.7	…	B-	…	16.4	16.2	0.2	45.9	5.7	0.6
Georgia	32.6	60.5	32.5	16.7	3.0	18.7	111.8	3.8	32.5	98.1	…	BB-	BB-	21.4	17.3	5.4	67.7	9.4	15.1
Moldova	23.8	73.0	49.5	35.8	2.5	34.8	97.0	4.7	43.4	87.6	…	…	…	16.1	15.8	0.3	42.4	14.5	5.9
Ukraine	37.4	75.2	57.3	33.6	22.8	13.0	38.5	2.6	39.6	133.7	619.3	B	B	20.8	14.6	6.2	38.1	20.7	8.0
Turkey	36.4	46.1	31.8	20.0	104.0	13.2	65.6	4.6	39.5	137.6	121.4	BB+	BBB-	13.6	…	…	26.7	2.9	10.6
Russia	10.9	26.6	24.3	7.9	527.7	26.1	298.6	14.2	38.1	126.9	143.0	BBB	BBB	6.1	5.7	0.4	11.9	4.4	5.3
Central Asia																			
Kazakhstan	12.3	68.7	65.9	8.3	28.1	13.8	122.4	7.0	32.0	104.9	154.0	BBB+	BBB+	9.5	7.6	1.9	28.2	29.8	5.3
Kyrgyz Republic	48.9	76.7	30.9	7.6	2.1	31.8	386.5	4.6	17.0	79.1	…	…	…	7.3	…	…	54.5	7.2	2.4
Mongolia	56.7	126.0	96.4	…	3.7	36.2	…	4.9	33.2	138.2	…	BB-	B+	14.7	13.7	1.1	32.0	4.2	7.0
Tajikistan	32.5	43.5	19.1	1.3	0.3	3.4	258.7	0.6	13.4	116.3	…	…	…	9.3	…	…	60.0	6.5	2.4
Turkmenistan	15.8	15.8	0.0	2.4	…	…	…	…	…	…	…	…	…	2.4	…	…	…	...	…
Uzbekistan	8.6	13.0	4.8	0.8	20.2	39.5	…	14.6	…	…	…	…	…	…	…	…	…	...	…
Southern and Eastern Mediterranean																			
Egypt	80.4	13.8	4.5	2.4	13.4	5.4	251.3	2.5	60.1	49.3	584.8	B-	B	8.8	7.7	0.2	…	10.1	13.0
Jordan	80.2	60.7	38.2	31.3	8.2	26.5	1210.8	4.2	107.8	72.0	259.0	BB	…	9.7	…	…	…	8.4	12.5
Morocco	59.6	27.3	1.5	2.0	15.8	16.4	836.5	3.8	64.5	107.9	215.8	BBB-	BBB-	…	…	…	…	5.1	9.0
Tunisia	44.5	51.6	15.0	15.2	7.2	14.0	105.4	3.2	54.2	104.2	246.0	BB-	BB+	…	…	…	…	...	16.7

1/ National sources based on CEIC and IFS, unless stated otherwise.
2/ WEO April 2013 estimates. CEB figures from Eurostat. Data from WEO April 2013 may not fully reflect the latest revisions to GDP in 2012.
3/ Slovenia NPLs: EBRD estimate
* Euro area members

Table 2. Transition Region: Annual indicators and projections 1/

	GDP Growth (average) (year over year percent change)			GDP Growth (end year) (Q4 over Q4 percent change)			Inflation (average) (year over year percent change)		Fiscal Balance /4 (Gen. gov; % of GDP)	Primary fiscal balance to GDP /4	GG Debt/revenues (%)	Current Account (% of GDP)	Net FDI (% of GDI
		Forecast 2/				Forecast 2/		Forecast 2/	3/	3/	3/	3/	3/
	2012	2013	2014	2011	2012	2013	2012	2013	2012	2012	2012	2012	2012
Central Europe and Baltics													
Croatia	-2.0	-0.3	1.9	-0.3	-2.3	0.3	3.4	3.1	-4.1	-1.5	147.5	0.1	2.4
Estonia	3.2	3.0	3.1	5.9	3.7	2.5	4.2	3.5	-0.2	-0.1	18.9	-1.2	2.6
Hungary	-1.7	-0.8	0.9	1.3	-2.7	0.7	5.7	2.7	-1.9	2.3	170.3	1.6	2.3
Latvia	5.6	3.5	3.2	5.7	5.1	4.3	2.3	1.5	0.1	1.6	98.4	-1.7	2.8
Lithuania	3.6	2.8	3.0	5.7	4.1	1.3	3.2	2.0	-3.0	-1.1	117.0	-0.6	1.0
Poland	1.9	1.2	2.0	4.6	1.1	1.0	3.7	1.5	-3.5	-0.5	138.6	-3.5	0.8
Slovak Republic	2.0	1.0	2.0	3.8	0.7	1.3	3.7	2.3	-4.9	-3.2	162.3	2.3	3.4
Slovenia	-2.3	-2.5	-0.9	-2.4	-3.0	-1.1	2.8	2.0	-4.0	-1.9	120.2	2.3	0.5
South-Eastern Europe													
Albania	1.6	1.5	1.9	2.2	1.7	1.9	2.0	2.1	-3.1	0.0	250.6	-10.4	7.4
Bosnia and Herzegovina	-0.5	0.1	1.8	…	…	…	1.9	1.7	-2.8	-2.0	96.9	-9.4	3.5
Bulgaria	0.8	1.0	2.5	0.6	0.3	2.1	2.4	2.0	-0.8	0.1	53.1	-1.5	3.3
FYR Macedonia	-0.3	1.5	2.6	0.9	0.4	1.2	3.3	2.7	-3.8	-2.9	115.0	-4.0	1.4
Kosovo	2.5	3.0	3.5	…	…	…	3.3	2.5	-2.7	...	61.1	-20.3	46.3
Montenegro	-0.5	1.0	2.0	…	…	…	3.6	2.7	-4.0	-2.2	136.0	-18.3	13.8
Romania	0.7	1.4	2.2	1.6	1.1	1.7	3.4	4.0	-2.9	-1.1	112.9	-3.9	1.3
Serbia	-1.7	2.2	1.9	0.4	-2.4	4.3	7.3	8.5	-6.4	…	…	-10.6	0.8
Eastern Europe and the Caucasus													
Armenia	7.2	5.0	4.0	5.3	6.4	4.7	2.6	4.5	-1.5	-0.5	187.7	-10.7	4.8
Azerbaijan		3.5	4.0	-0.5	4.5	3.1	0.7	3.4	3.1	3.6	28.5	21.8	-2.8
Belarus	1.1	2.0	2.5	0.3	-1.9	3.5	59.2	19.2	0.7	2.1	90.5	-2.9	2.1
Georgia	6.2	3.0	5.0	8.5	2.8	5.5	-0.9	0.0	-2.3	0.2	112.5	-11.5	3.8
Moldova	-0.5	2.5	4.0	5.8	-2.5	4.0	3.4	4.1	-2.1	-1.3	62.5	-7.1	1.9
Ukraine	0.2	-0.5	2.5	5.0	-2.5	2.4	0.7	0.8	-4.6	-1.1	83.8	-8.4	3.8
Turkey	2.2	3.7	4.0	5.3	1.4	5.2	8.9	7.9	-1.5	2.0	105.0	-6.0	1.1
Russia	3.4	1.8	3.0	5.1	2.1	0.7	5.1	5.9	-0.2	1.0	29.4	3.7	0.0
Central Asia													
Kazakhstan	5.0	4.9	5.5	8.7	4.5	4.7	5.2	6.2	4.7	5.1	44.2	3.8	6.2
Kyrgyz Republic	-0.9	6.5	5.0	4.6	8.1	0.4	2.8	7.4	-5.8	-4.9	142.0	-21.9	6.6
Mongolia	12.3	16.0	17.0	19.3	17.3	11.0	14.9	11.0	-7.7	-6.8	159.2	-32.5	37.6
Tajikistan	7.5	5.0	5.0	7.2	7.5	3.8	5.8	6.9	0.6	1.2	129.2	-2.3	2.3
Turkmenistan	11.1	10.0	10.0	…	…	…	4.9	5.7	15.5	...	53.0	1.7	10.4
Uzbekistan	8.2	7.5	7.0	8.5	8.2	6.9	12.1	11.0	4.7	4.8	22.4	2.7	1.7
Southern and Eastern Mediterranean													
Egypt	3.1	2.0	3.6	0.4	1.6	2.7	7.1	12.0	-10.7	-4.7	356.0	-2.7	1.0
Jordan	2.7	3.0	3.4	3.1	2.2	3.4	4.8	5.8	-8.2	-5.6	251.0	-18.1	4.5
Morocco	2.4	5.0	5.2	4.8	2.0	4.7	1.3	2.5	-7.4	-5.2	215.1	-9.9	2.6
Tunisia	3.7	3.8	4.3	-1.6	4.0	4.0	5.6	6.0	-4.9	-3.1	145.8	-8.2	3.9

1/ EBRD data and projections unless otherwise stated.

2/ As of April 26, 2013.

3/ WEO April 2013. CEB figures from Eurostat.

4/ Ukraine: Augmented general government balance: overall government balance includes Naftogaz and other debt-creating flows.

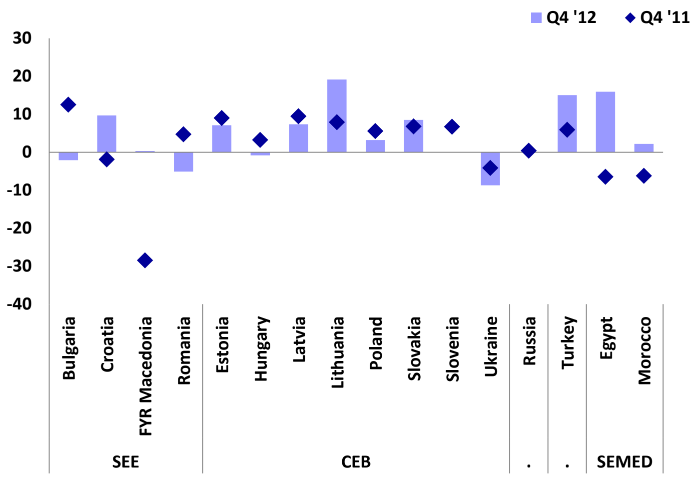
Table 3. Transition Region: Quarterly GDP actuals and projections, Q1 2011- Q1 2013 1/

	Quarterly GDP Growth (seasonally adjusted, quarter-on-quarter percent change)									Quarterly GDP Growth (year-on-year percent change)									GDP Growth (average) (year over year percent change)		
									Estimates 1/									Estimates 1/		Forecast 1/	
	2011				2012				2013	2011				2012				2013			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4	Q1	2012	2013	2014
Central Europe and Baltics																					
Croatia	-0.9	10	0.1	-0.8	-10	-0.5	0.0	-0.8	0.0	-14	0.6	0.8	-0.3	-11	-2.5	-19	-2.3	-0.2	-2.0	-0.3	19
Estonia	2.6	15	11	0.7	0.3	0.4	18	0.9	0.5	9.9	8.3	9.3	5.9	3.4	2.2	3.5	3.7	3.8	3.2	3.0	3.1
Hungary	14	-0.3	0.0	0.2	-10	-0.6	-0.4	-0.9	-0.2	2.6	13	14	13	-0.6	-17	-17	-2.7	-2.6	-17	-0.8	0.9
Latvia	15	2.0	13	10	13	14	17	14	0.7	3.6	5.7	6.6	5.7	7.0	5.2	5.2	5.1	4.3	5.6	3.5	3.2
Lithuania	16	17	0.9	11	0.5	0.5	12	0.7	0.7	5.5	5.6	6.6	5.7	3.9	2.1	4.4	4.1	3.6	3.6	2.8	3.0
Poland	11	13	0.8	0.9	0.4	0.1	0.3	0.2	0.2	4.1	4.4	4.1	4.6	3.7	2.0	16	11	10	19	12	2.0
Slovak Republic	0.8	0.8	0.7	0.9	0.3	0.4	0.3	0.2	0.2	3.2	3.4	2.6	3.8	2.9	2.6	2.1	0.7	10	2.0	10	2.0
Slovenia	-0.3	0.4	-0.1	-0.9	-0.2	-11	-0.6	-10	-0.5	2.5	16	0.8	-2.4	0.0	-3.2	-3.1	-3.0	-3.8	-2.3	-2.5	-0.9
South-Eastern Europe																					
Albania	19	-11	0.8	0.8	-0.6	13	12	-0.2	0.3	5.6	0.9	2.9	2.2	-0.4	2.1	2.9	17	2.5	16	15	19
Bosnia and Herzegovina	…	…	…	…	…	…	…	…	…	…	…	…	…	…	…	…	…	…	-0.5	0.1	18
Bulgaria	0.3	0.4	0.2	0.1	0.0	0.4	0.1	0.0	0.2	2.1	2.9	19	0.6	10	11	0.8	0.3	2.5	0.8	10	2.5
FYR Macedonia	0.9	0.2	-0.8	0.4	-0.8	0.2	0.5	0.3	0.3	5.1	5.3	2.3	0.9	-13	-0.8	0.3	0.4	15	-0.3	15	2.6
Kosovo	…	…	…	…	…	…	…	…	…	…	…	…	…	…	…	…			2.5	3.0	3.5
Montenegro	…	…	…	…	…	…	…	…	…	…	…	…	…	…	…	…	…	…	-0.5	10	2.0
Romania	12	-0.2	14	-0.2	-0.1	0.6	-0.2	0.4	0.0	15	12	4.1	16	0.4	19	-0.5	11	14	0.7	14	2.2
Serbia	14	-0.2	-0.3	-0.3	-0.5	0.4	-2.2	-0.2	10	3.0	2.5	0.7	0.4	-13	-0.6	-2.5	-2.4	-13	-17	2.2	19
Eastern Europe and the Caucasus																					
Armenia	19	0.8	-0.6	3.0	16	2.2	2.5	0.0	2.1	19	3.4	6.6	5.3	5.6	6.6	9.3	6.4	3.7	7.2	5.0	4.0
Azerbaijan	-17	2.5	-0.7	-0.9	0.3	11	18	10	0.1	16	0.3	-0.1	-0.5	0.5	-0.4	2.5	4.5	3.1	2.2	3.5	4.0
Belarus	0.3	12	-2.6	2.2	13	0.6	-11	-2.0	5.2	10.6	11.2	17	0.3	3.0	2.5	2.7	-19	3.5	11	2.0	2.5
Georgia	18	2.0	19	2.6	0.1	3.4	12	-18	0.0	5.8	6.0	7.9	8.5	6.7	8.2	7.5	2.8	2.8	6.2	3.0	5.0
Moldova	13	11	0.9	2.2	-2.8	0.7	0.2	-0.6	0.0	8.4	6.7	6.0	5.8	10	0.6	0.2	-2.5	0.7	-0.5	2.5	4.0
Ukraine	2.1	0.3	2.4	0.3	-0.6	0.6	-17	-0.8	-0.8	5.1	3.9	6.5	5.0	2.2	3.0	-13	-2.5	-2.4	0.2	-0.5	2.5
Turkey	2.8	0.4	0.8	11	0.5	0.3	-0.2	0.7	12	12.4	9.3	8.7	5.3	3.3	2.9	16	14	11	2.2	3.7	4.0
Russia	0.8	0.6	19	15	0.6	0.4	0.5	0.4	-0.2	3.5	3.4	5.0	5.1	4.8	4.3	3.0	2.1	11	3.4	18	3.0
Central Asia																					
Kazakhstan	15	2.6	19	17	-0.1	18	12	12	0.6	6.8	7.4	6.8	8.7	5.6	5.6	4.6	4.5	4.5	5.0	4.9	5.5
Kyrgyz Republic	5.7	-0.2	13	-4.0	-3.6	2.1	2.8	5.1	-15	-15	8.2	10.0	4.6	-7.1	-4.8	-3.9	8.1	7.6	-0.9	6.5	5.0
Mongolia	6.5	6.0	5.5	0.4	3.7	0.9	0.3	11.9	2.6	9.8	16.8	20.7	19.3	16.7	10.9	5.3	17.3	15.4	12.3	16.0	17.0
Tajikistan	14	2.3	17	13	18	2.4	19	12	17	6.5	7.2	8.1	7.2	7.2	7.5	7.6	7.5	7.3	7.5	5.0	5.0
Turkmenistan	…	…	…	…	…	…	…	…	…	…	…	…	…	…	…	…	…	…	11.1	10.0	10.0
Uzbekistan	13	2.7	2.1	19	0.8	3.5	2.0	16	18	7.6	8.3	8.4	8.5	7.5	8.5	8.3	8.2	9.8	8.2	7.5	7.0
Southern and Eastern Mediterranean																					
Egypt	-5.2	4.0	0.9	0.8	-0.1	15	0.3	0.0	0.7	-4.2	0.4	0.3	0.4	5.2	3.3	2.6	16	3.5	3.1	2.0	3.6
Jordan	0.2	0.8	11	0.9	0.3	0.6	0.6	0.6	0.8	2.3	2.4	2.6	3.1	3.0	2.9	2.6	2.2	3.1	2.7	3.0	3.4
Morocco	0.8	0.5	16	16	-0.8	0.0	18	16	16	4.1	4.5	5.0	4.8	2.8	2.2	2.7	2.0	4.5	2.4	5.0	5.2
Tunisia	-3.8	2.2	-0.3	10	0.5	10	18	0.4	0.9	-3.7	-0.9	-12	-16	4.9	2.2	3.7	4.0	3.5	3.7	3.8	4.3

1/ As of April 26, 2013.

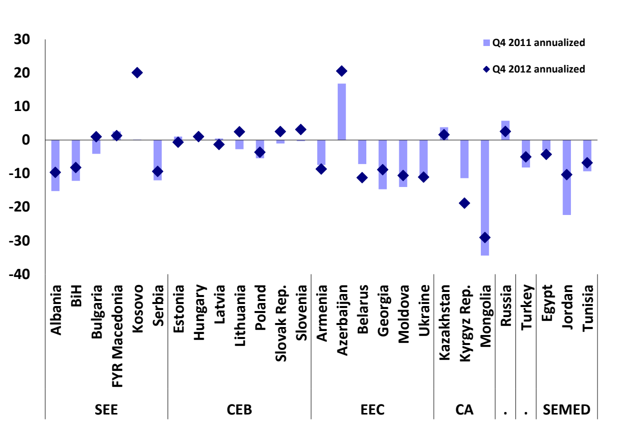
Figure 1. External environment

Export volumes, y-o-y, %



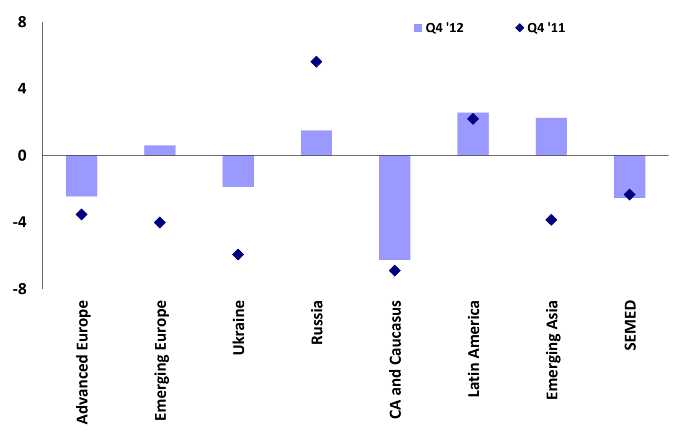
Source: National authorities via CEIC data service.

Current account, % of GDP



Source: National authorities via CEIC data service.

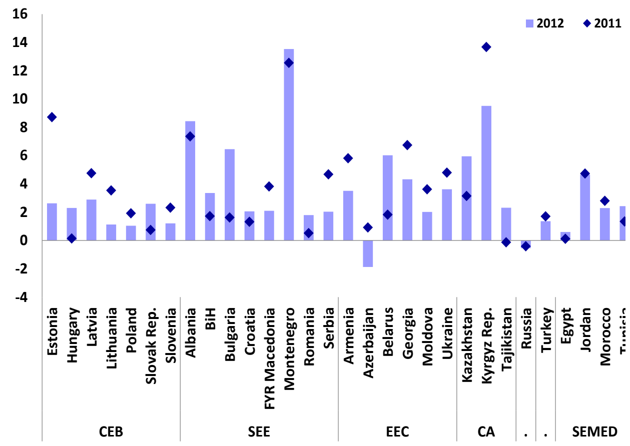
Net lending from BIS-reporting banks, exch. rate adjusted, q-o-q



1/ Emerging Europe excludes Russia and Ukraine.
2/ Emerging Asia excludes China, Central Asia and Caucasus.

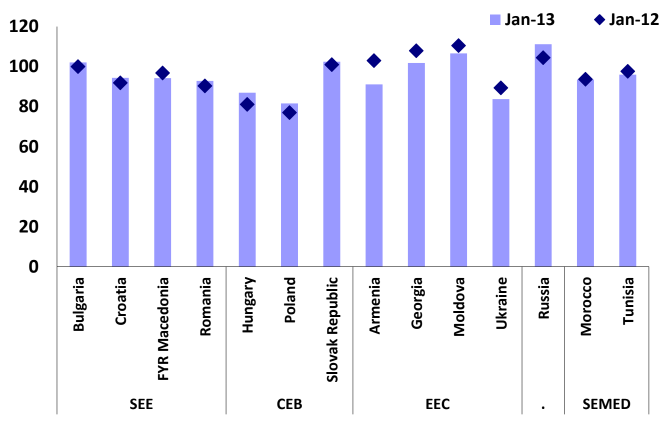
Source: BIS via CEIC data service.

FDI net inflows, % of GDP



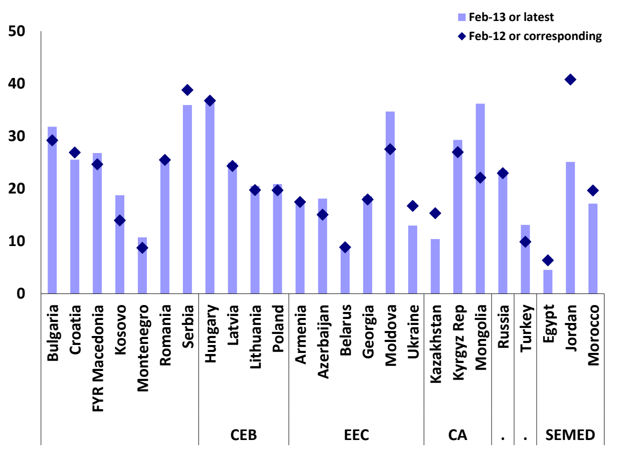
Source: National authorities via CEIC data service.

Real effective exchange rate, July 2008=100



Source: IMF International Financial Statistics.

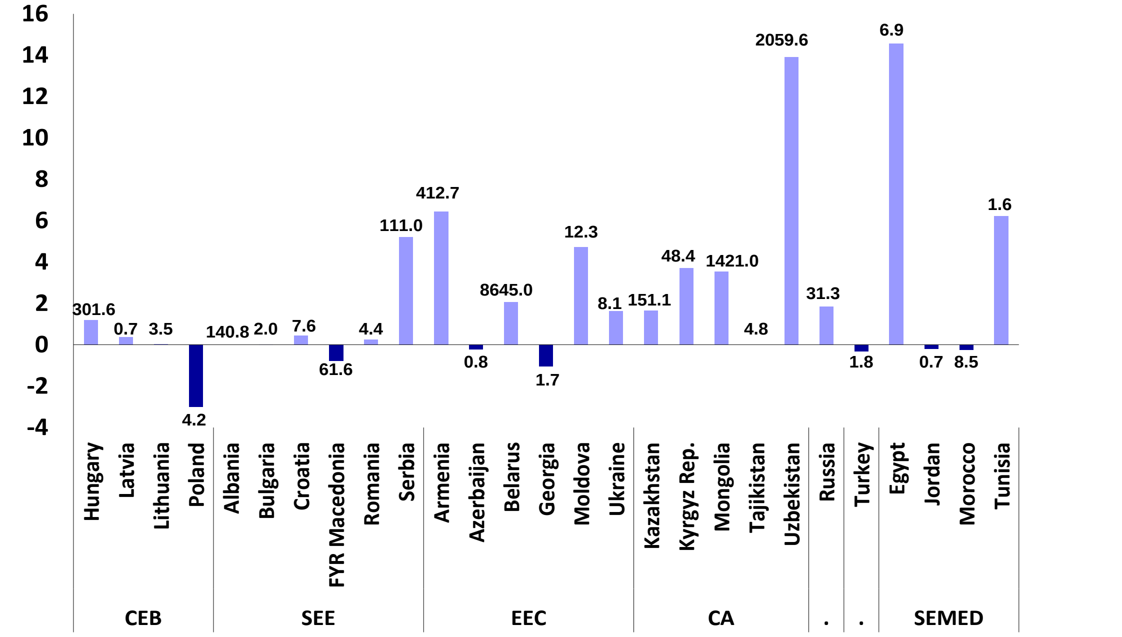
Reserves, end of period, % of GDP



Source: IMF International Financial Statistics.

Figure 2: Currencies and financial market indicators (daily frequency)

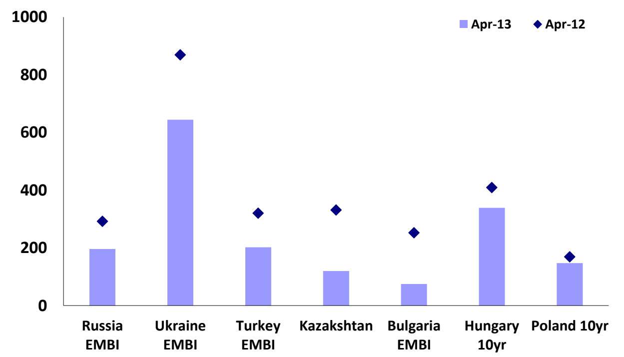
Currencies (change since 30/01/2012)



Source: Bloomberg.

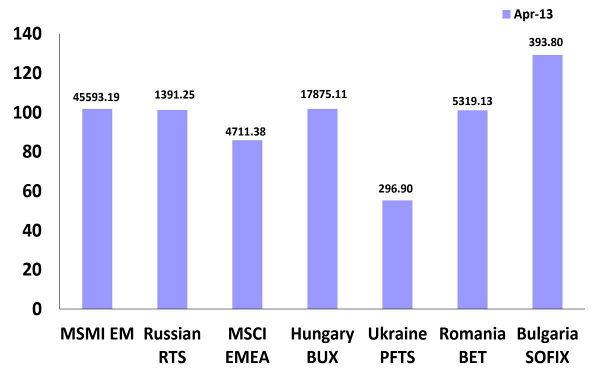
For EEC, CA, SEMED, Turkey and Russia the reference currency is U.S. dollar; For CEB and SEE the reference currency is Euro. A decrease represents an appreciation. Numbers on bars represent actual exchange rate values

Sovereign risk (bond spreads, bp)



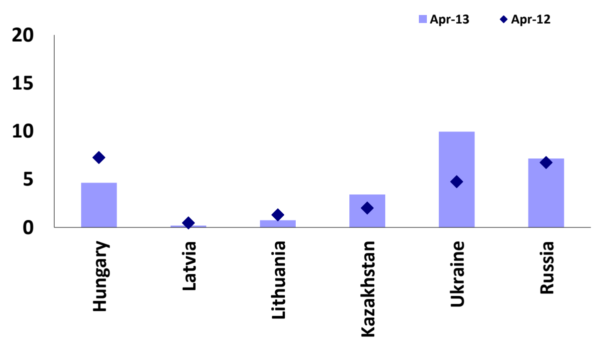
Source: Bloomberg.

Stock markets (January 2011=100)

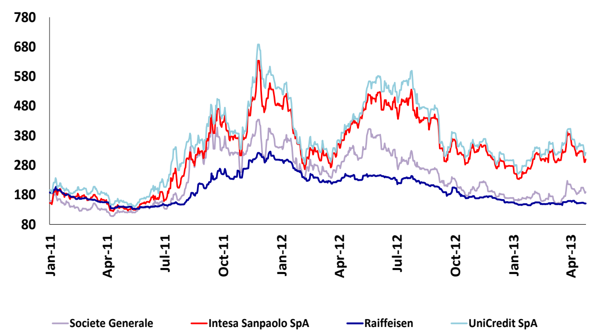


Numbers on bars represent actual values of stock indices.

Interbank rates (%)



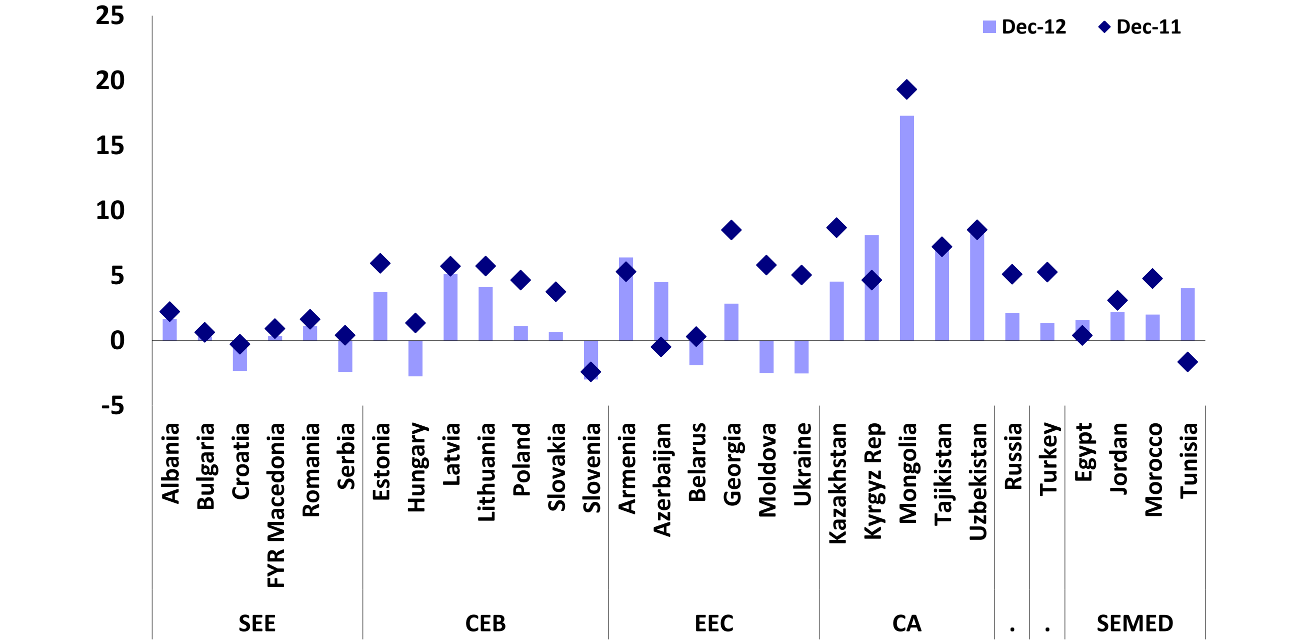
Parent banks CDS spreads (bp)



Source: Bloomberg.

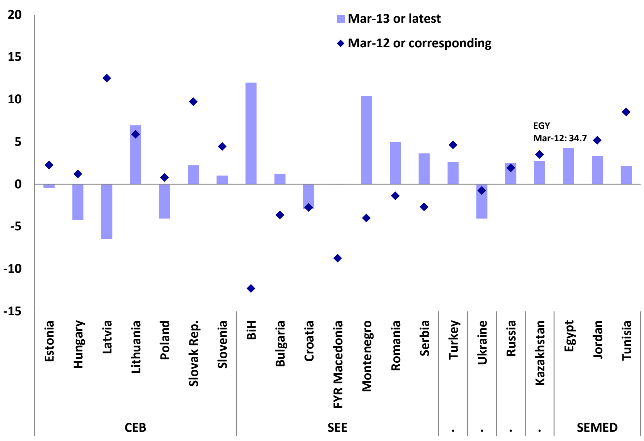
Figure 3. Indicators of real activity

Real GDP, y-o-y change, %

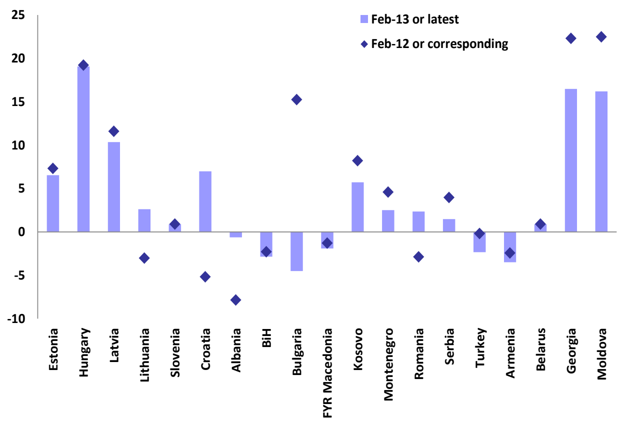


Source: National authorities via CEIC data service.

Industrial production, monthly y-o-y change, %

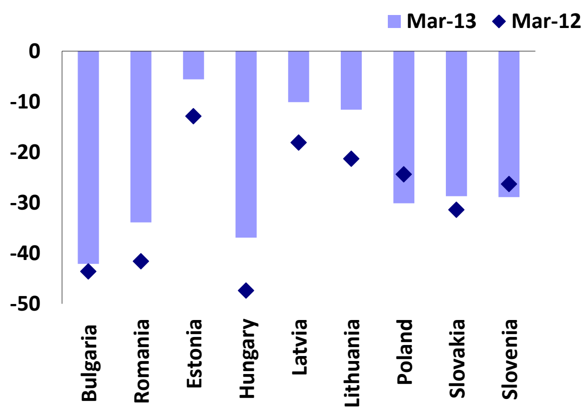


Retail sales, monthly y-o-y change, %



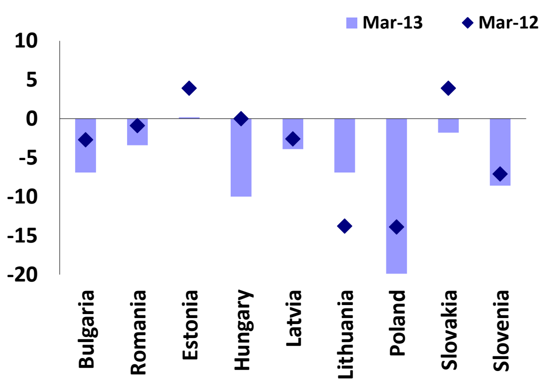
Source: National authorities via CEIC data service.

Consumer confidence



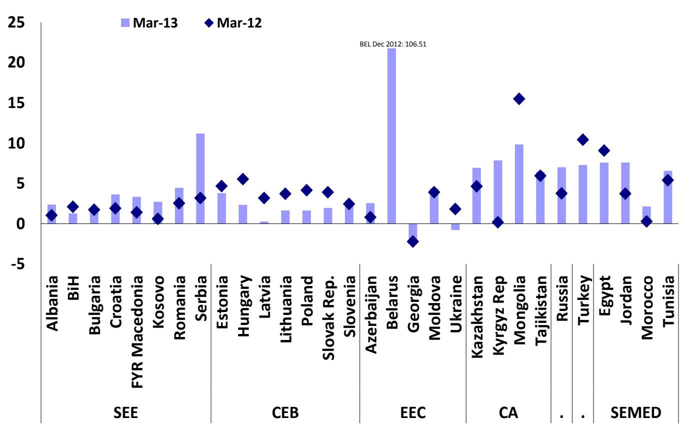
defined as the difference (in percentage points of total answers) between positive and negative answers
Source: Eurostat

Industrial confidence

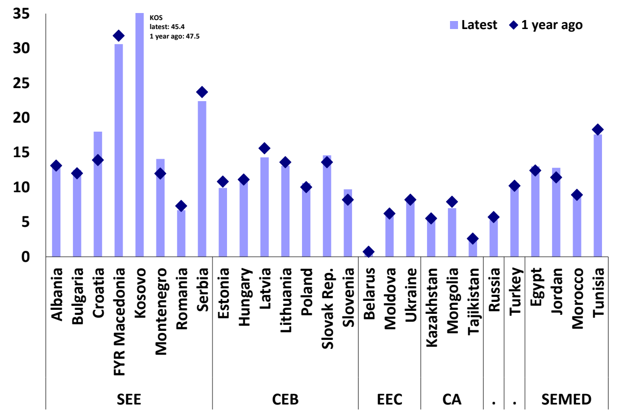


defined as the difference (in percentage points of total answers) between positive and negative answers

CPI, y-o-y change, %



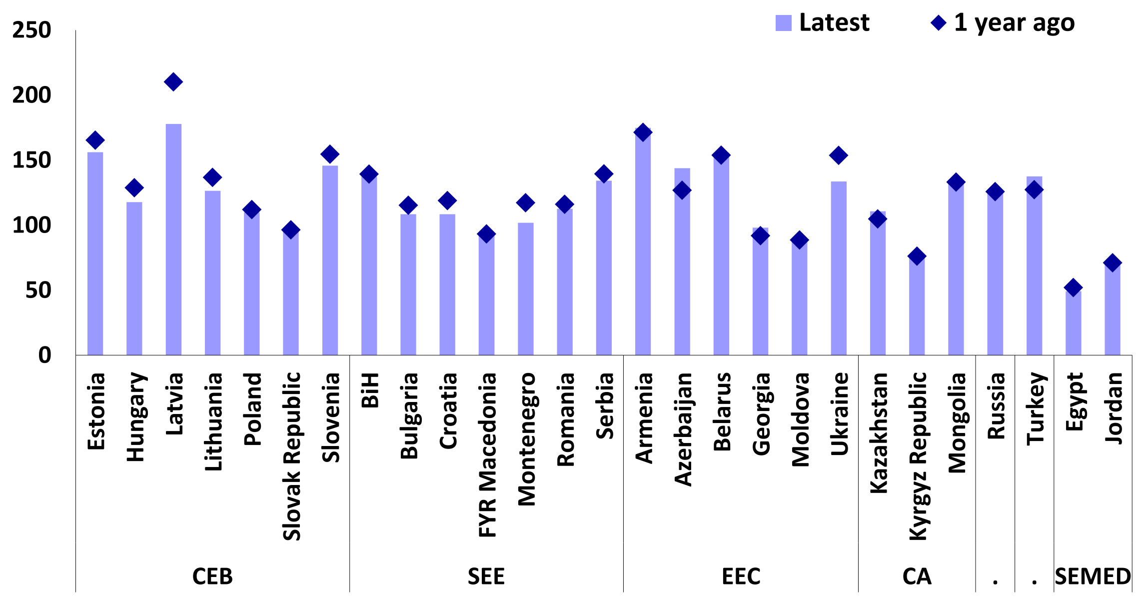
Unemployment rate, %



Source: National authorities via CEIC data service, Eurostat

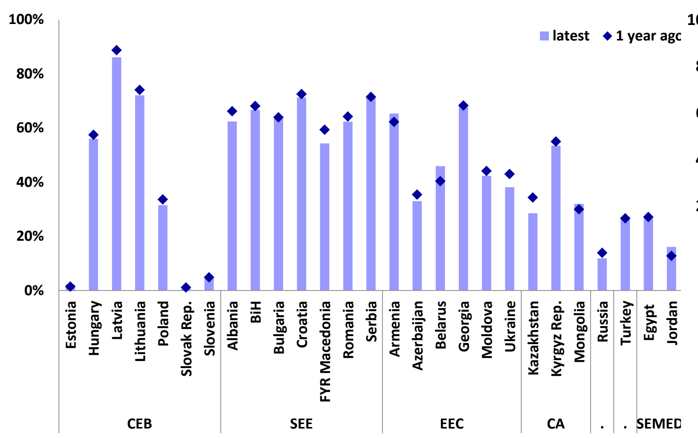
Figure 4: Financial sector indicators: loans and deposits

Loan to deposit ratio, (%)

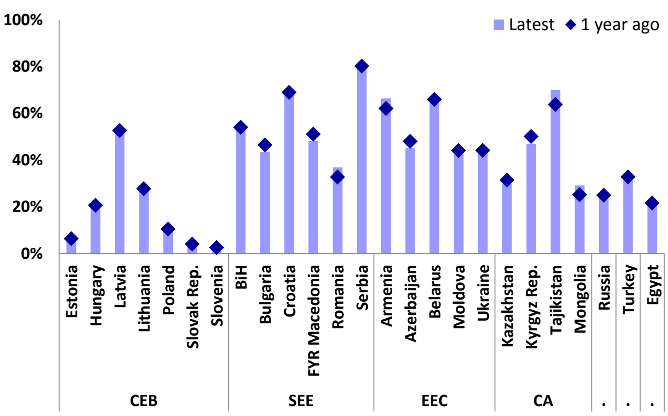


Source: National authorities via CEIC data service.

Foreign currency loans to total loans ratio, (%)



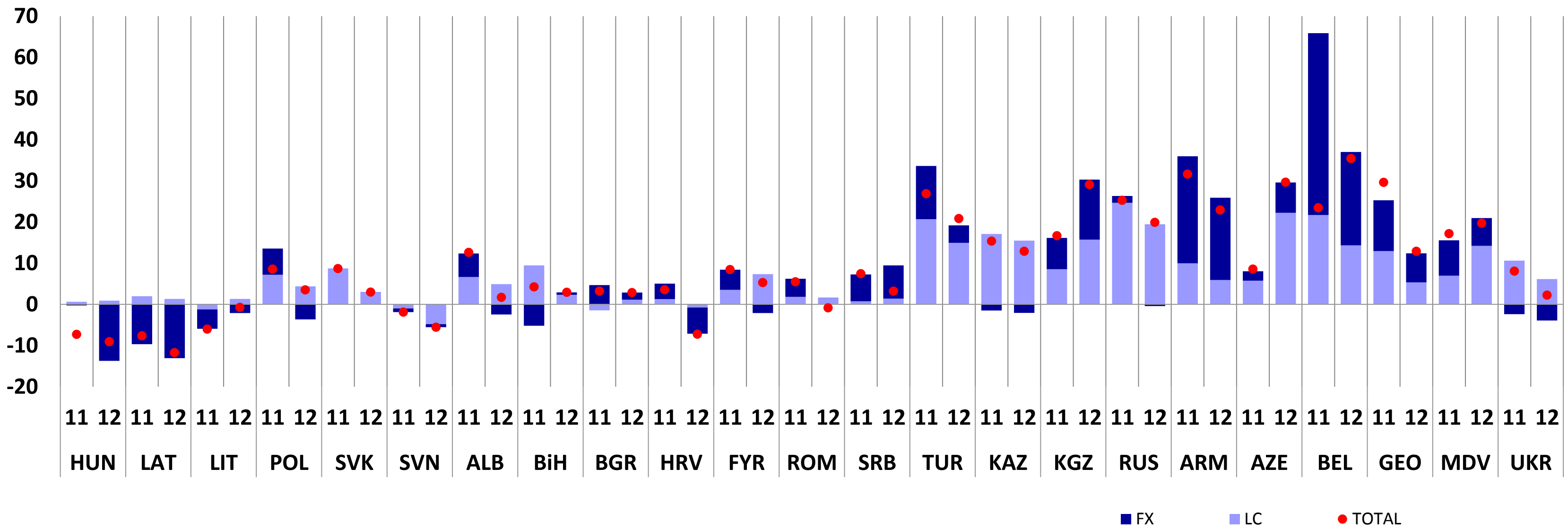
Foreign currency deposits to total deposits ratio, (%)



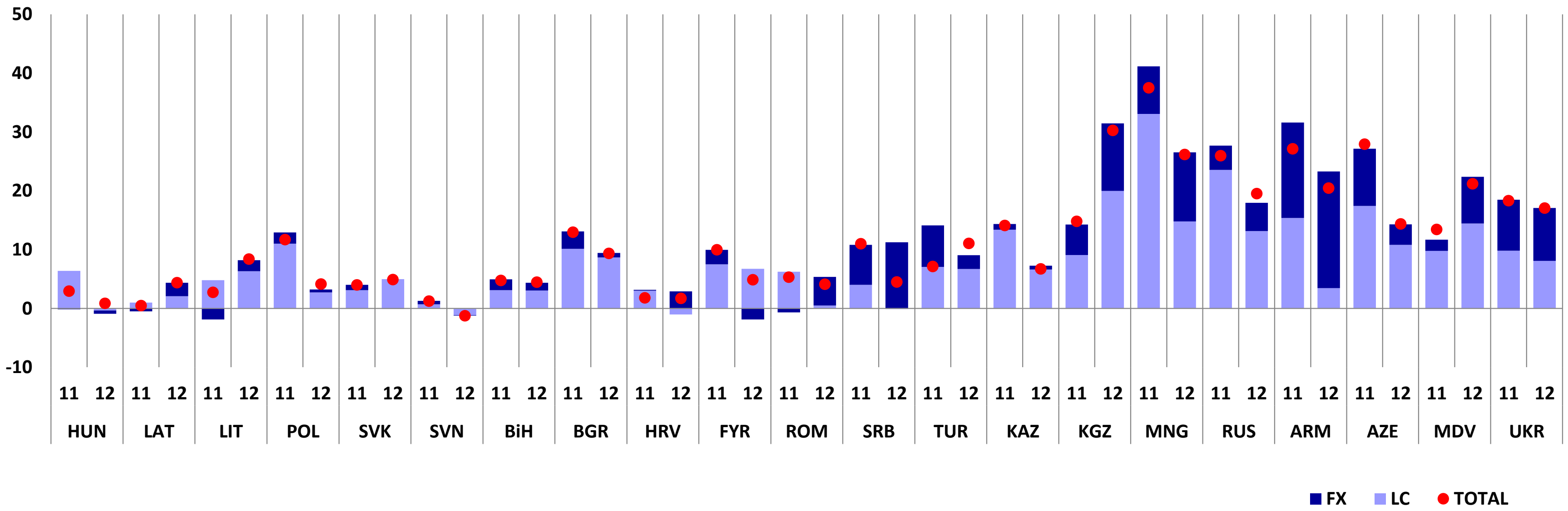
Source: National authorities via CEIC data service

Figure 5. Financial sector indicators: foreign and local currency lending and deposits

Contribution to private sector credit growth (year-on-year, in %)



Contribution to private sector deposits growth (year-on-year, in %)



Source: National authorities via CEIC data service