Eurozone banks and Growth in CESEE

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Western banks are very important in CESEE

Foreign bank participation
(percent of banking sector assets)

- Baltics
- SEE EU
- SEE non-EU
- CE5
- CIS

- 0-20 percent
- 50-60 percent
- 90-100 percent
This makes CESEE vulnerable to what happens with Western European banks

- In boom years, they funded a credit boom in CESEE
- After Lehman, pressure on Western European bank led to sudden stop in capital flows to CESEE
- Second deleveraging wave from mid-2011 onwards, triggered by eurozone sovereign debt crisis
The boom-bust in bank flows has been quite dramatic.
As has the boom-bust in growth—and current account deficits

Real GDP growth (y/y percent)

Current Accounts in Europe (percent of GDP)
Weak parent banks have contributed to weak credit and GDP growth.
Further exacerbated by high domestic NPLs

NPLs ratios (2014)
Overall, post-crisis growth has been very modest in SEE.
Reflecting a sharp drop in investment as well as TFP
SEE remains one of the poorest regions in Europe

GDP per capita
(percent of EU average)

2000

2007

2013
How to raise investment?

- Reduce constraints on bank lending to private sector
  - Address NPLs

- Raise domestic saving
Raise domestic saving: reduce public dissaving

**Fiscal balance, 2014 (percent of GDP)**

<table>
<thead>
<tr>
<th>Country</th>
<th>Fiscal Balance</th>
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<tbody>
<tr>
<td>Serbia</td>
<td>-7.0</td>
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<tr>
<td>Slovenia</td>
<td>-6.5</td>
</tr>
<tr>
<td>Croatia</td>
<td>-5.6</td>
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<tr>
<td>Albania</td>
<td>-4.5</td>
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<tr>
<td>Macedonia</td>
<td>-3.5</td>
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<tr>
<td>Bulgaria</td>
<td>-3.4</td>
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<tr>
<td>Poland</td>
<td>-2.6</td>
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<tr>
<td>BiH</td>
<td>-2.1</td>
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<tr>
<td>Slovakia</td>
<td>-1.4</td>
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<tr>
<td>Hungary</td>
<td>-0.9</td>
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<tr>
<td>Czech Rep.</td>
<td>0.0</td>
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<tr>
<td>Romania</td>
<td>0.2</td>
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<tr>
<td>Latvia</td>
<td>0.4</td>
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<tr>
<td>Lithuania</td>
<td>0.7</td>
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<tr>
<td>Estonia</td>
<td>0.9</td>
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Note: In green countries that improved fiscal balance vs. 2004-07 average.
Improve EU funds absorption

Unutilized 2007-13 EU funds
(percent of 2014 GDP)

- Hungary
- Slovakia
- Romania
- Czech Rep.
- Bulgaria
- Latvia
- Poland
- Slovenia
- Lithuania
- Estonia
This is particularly important given the amounts involved.

EU Cohesion Policy funds allocation (percent of initial year GDP)

- 2007-13 budget perspective
- 2014-20 budget perspective

Countries: Slovenia, Romania, Czech Rep., Latvia, Bulgaria, Slovakia, Estonia, Poland, Lithuania, Hungary

Graph shows allocation percentages for different countries and budget perspectives.
SEE is lagging in structural reforms

CESEE: Structural Reforms Relative to OECD Countries

<table>
<thead>
<tr>
<th>Category</th>
<th>Baltics</th>
<th>CEE</th>
<th>SEE</th>
<th>CIS</th>
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<tbody>
<tr>
<td>Institutions and contracts</td>
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<td>Infrastructure</td>
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<td>Human capital</td>
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<td>Labor market efficiency</td>
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<td>Business regulation</td>
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<td>Openness to trade and FDI</td>
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<td>Credit market rigidity</td>
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<td>Innovation</td>
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Note: Red - value below the 25th percentile; Yellow - value in the 50th and 75th percentile range. The sample includes all OECD and CESEE countries.

Source: IMF Spring 2015 Regional Economic Issues Report on CESEE, May 11, 2015:
Thank you