Economic and Financial Issues in CESEE

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Global growth has hovered around 3¼ percent. In recent years, well below pre-crisis levels.
Growth in EMCS has lost steam...
...with Brazil and Russia in recession and China slowing down.
Euro area has been recovering gradually, but growth in US has disappointed.
Large difference between CIS and non-CIS
- Non-CIS CESEE doing quite well
- CIS in recession in 2014-15
Non-CIS CESEE is growing at solid pace. Unemployment is falling rapidly...
...to pre-crisis lows.
While inflation is still low...
Real wage growth has accelerated

Real wage growth
(y/y, percent)

Q2'2015 → Q2'2016 →
Which has increased wage shares and reduced corporate profits and saving.

Change in wage share of income and corporate saving, 2014-16
Investment has weakened in 2016...

Annual growth of gross fixed capital formation (percent)

Note: Simple average of annual growth of GFCF in given countries.
...but this is partly a temporary problem, linked to timing of EU funds
CIS suffered from recession in 2014/15

- Collapse of commodity prices
- Sudden stop in capital flows to Russia, result of sanctions on Russia
- Conflict in Ukraine
- Spillovers from Russia to other CIS countries

Change in GDP (percent)

- Ukraine: Between 2013-16
- Belarus: Between 2013-15
- Russia
- Moldova
Exchange rate flexibility helped absorb much of the shock...
...although at cost of high inflation.
Russia is recovering, helped by rising oil prices.
Forecasts for 2017
Global growth for 2017 continues to be modest

GDP growth according to WEO Oct-16 (percent)
Country forecasts: Non-CIS similar as 2016; pick-up in CIS; Belarus still in recession

GDP growth (percent)

Note: CIS countries in red.
Downside risks continue to dominate the outlook

- Tighter and more volatile financial conditions
- Structurally weak growth in the euro area
- Slowdown in China or failure of recovery in major EMs
- What will be impact of US election?
- Non-economic shocks:
  - Political fragmentation
  - Refugee crisis
  - Terrorism
Crisis legacies in the banking sector
Post-crisis, there has been withdrawal of Western Bank funding from CESEE

Bank’s external claims on all sectors (billions of USD, exchange rate adjusted)

Note: for MNE and BGR data for 2012 and 2015.
There has also been selected withdrawal of ownership.
Renewed pressure on some parent banks may lead to further sales
NPLs have come down (although they are still high in SEE and Ukraine)...

Non-performing loans to total loans, 2016 (Percent)

Note: for MNE and BGR data for 2012 and 2015.
Large differences in return on equity.

Bank Return on Equity, 2016Q2
(percent)

Note: for BLR, HRV, BLR, TUR, MDA: data for 2016Q1; for BGR and RUS: data for 2015.
Syndicated loans
Syndicated loans issuance is very cyclical.

Gross issuance of syndicated loans to private sector
(USD billion, 4-quarter moving average)
Syndicated loans segment in CESEE is small relative to other EMCs

Issuance of syndicated loans to private sector
(Percent of GDP, 4-quarter average)
Challenges
1. Brexit and future of EU

- Impact of Brexit has been modest so far
- But large uncertainty remains
- Most important question: what will be impact on future EU?
In the past decade there has been a sharp decline in confidence in the EU.

Level of confidence in the European Union
(percent of population surveyed by Eurobarometer)
2. Pro-cyclical fiscal policy: unemployment is declining rapidly

Change in unemployment rate, 2013-2016
(Percentage points)
But a number of countries have procyclical loosening.
3. Longer-term challenge: potential output growth has slowed in many countries...
...as productivity growth has decelerated.

Average total factor productivity growth (percent)

2000-04

2010-14
Aging will provide further headwinds.

Working age (15-64) population growth (percent)
Thank you