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Monthly Report

## Summer Forecast Update

# Solid but Lopsided Recovery

## Economic Forecasts for Eastern Europe for 2024-26

The Vienna Institute for International Economic Studies
Wiener Institut für Internationale Wirtschaftsvergleiche

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## Economic Forecasts for Eastern Europe for 2024-26

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# Executive summary

**Economic recovery in most of the countries of Central, East and Southeast Europe (CESEE) gathered momentum in Q1 2024, with annual growth ranging from 5.7% in Turkey to -2.4% in Estonia.** However, the recovery continued to be lopsided: private consumption and services picked up, whereas industry and exports still struggled, due to industrial weakness in Germany – the main trading partner of most CESEE countries. By contrast, countries outside the German-led manufacturing cluster, such as the states of the CIS and Turkey, have shown much better industrial performance.

**The main drivers behind the recovery in household consumption have been the growth in real wages on the back of recent disinflation and a sharp rise in nominal wages.** For the first time in the past three years, real wage growth in Q1 turned positive everywhere in the region. However, only part of the extra money from rising wages is being spent; the rest is being used to replenish the savings that were dipped into to smooth consumption over the previous two years. Besides, the recent slowdown in inflation – to 2-3% in many countries – is likely to be nearing its end, as consumer demand strengthens further and production costs rise on the back of the major growth in wages – which is in part a consequence of resurgent labour shortages. In Russia and Belarus – to say nothing of Turkey – inflationary pressures remain high, arguably reflecting conditions of economic overheating.

**Despite some monetary easing in many CESEE countries recently, financial conditions remain generally tight,** with real policy interest rates hovering in positive territory nearly everywhere. **At the same time, economic recovery is being supported by lax fiscal policy.** Budget deficits are generally on the rise, in part due to the elections in many countries this year, as well as high levels of military spending. Although deficits can be comfortably financed in most cases, the forthcoming (re)launch of the EU Excessive Deficit Procedure (EDP) against Poland, Hungary, Slovakia and Romania – all of which will run public deficits in excess of 5% of GDP this year – may exert some consolidation pressure.

**Compared with our Spring 2024 Forecast, the growth prospects in CESEE for this year have generally improved.** The economy of the region as a whole is projected to grow by 3.1% – roughly the same pace as in 2023, with the acceleration in EU-CEE (and, to a lesser extent, Western Balkans) being offset by the slowdown in Turkey, CIS3 and particularly Ukraine, where the large-scale destruction of power generation capacity will weigh heavily on the economic performance. In 2025-2026, economic expansion in CESEE is projected to pick up pace only marginally, and the risks are mainly on the downside. The most important risk is related to the possible victory of Donald Trump in the US presidential elections in November: that could lead to another round in the trade war with China and to a weakening of the US security commitment to the CESEE region.

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**Cut-off date for historical data and forecasts: 13 June 2024. Most data are taken from the wiiw Databases. Direct access is available at: https://data.wiiw.ac.at/.**

## ABBREVIATIONS

| | |
|---|---|
| EUR | euro |
| USD | US dollar |
| | |
| CIS | Commonwealth of Independent States |
| CPI | consumer price index |
| DP | Domovinski pokret (Homeland Movement), far-right party in Croatia |
| ECB | European Central Bank |
| EDP | Excessive Deficit Procedure |
| EU | European Union |
| EXPO 2027 | specialised exposition to be held in 2027 in Belgrade |
| FDI | foreign direct investment |
| FX | foreign exchange |
| GERB | Bulgarian conservative party (Граждани за европейско развитие на България) |
| GDP | gross domestic product |
| HDZ | Hrvatska demokratska zajednica (Croatian Democratic Union), conservative party |
| HICP | harmonized index of consumer prices |
| ICT | information and communication technologies |
| LFS | labour force survey |
| NATO | North Atlantic Treaty Organisation |
| OPEC+ | Organisation of the Petroleum Exporting Countries (OPEC) plus 10 of the biggest non-OPEC oil-exporting countries |
| pp | percentage points |
| RN | Rassemblement National (far-right party in France) |
| SNS | Srpska napredna stranka (Serbian Progressive Party) |
| TISZA | Tisztelet és Szabadság Párt (Respect and Freedom Party), opposition party in Hungary |
| UAE | United Arab Emirates |
| VMRO-DPMNE | Internal Macedonian Revolutionary Organization – Democratic Party for Macedonian National Unity, conservative party in North Macedonia |
| wiiw | The Vienna Institute for International Economic Studies |
| | |
| . | not available (in tables) |
| bn | billion |
| eop | end of period |
| m | million |
| p.a. | per annum |
| Q1 2021 | first quarter of 2021 |
| y-o-y | year on year |

**Keywords:** CESEE, economic forecast, Central and Eastern Europe, Western Balkans, EU, euro area, CIS, economic growth, inflation, monetary policy, fiscal policy, GDP, wages, fiscal balance, policy rate, political risk

**JEL classification:** E20, E21, E23, E24, E31, E5, E62, H60, J20, J30, O47, O52, O57, P24, P27, P52

# wiiw COUNTRY GROUPS

## CESEE23 Central, East and Southeast Europe

| | | | |
|---|---|---|---|
| AL | Albania | ME | Montenegro |
| BA | Bosnia and Herzegovina | MK | North Macedonia |
| BG | Bulgaria | PL | Poland |
| BY | Belarus | RO | Romania |
| CZ | Czechia | RS | Serbia |
| EE | Estonia | RU | Russia |
| HR | Croatia | SI | Slovenia |
| HU | Hungary | SK | Slovakia |
| KZ | Kazakhstan | TR | Turkey |
| LT | Lithuania | UA | Ukraine |
| LV | Latvia | XK | Kosovo |
| MD | Moldova | | |

## EU-CEE11 Central and East European EU members

| | | | |
|---|---|---|---|
| BG | Bulgaria | LV | Latvia |
| CZ | Czechia | PL | Poland |
| EE | Estonia | RO | Romania |
| HR | Croatia | SI | Slovenia |
| HU | Hungary | SK | Slovakia |
| LT | Lithuania | | |

## V4 Visegrád countries

| | |
|---|---|
| CZ | Czechia |
| HU | Hungary |
| PL | Poland |
| SK | Slovakia |

## V4+SI Visegrád countries and Slovenia

| | |
|---|---|
| CZ | Czechia |
| HU | Hungary |
| PL | Poland |
| SI | Slovenia |
| SK | Slovakia |

## BALT3 Baltic countries

| | |
|---|---|
| EE | Estonia |
| LT | Lithuania |
| LV | Latvia |

## EU-SEE3 Southeast European EU members

| | |
|---|---|
| BG | Bulgaria |
| HR | Croatia |
| RO | Romania |

## non-EU12 Non-European Union CESEE countries

| | | | |
|---|---|---|---|
| AL | Albania | MK | North Macedonia |
| BA | Bosnia and Herzegovina | RS | Serbia |
| BY | Belarus | RU | Russia |
| KZ | Kazakhstan | TR | Turkey |
| MD | Moldova | UA | Ukraine |
| ME | Montenegro | XK | Kosovo |

## WB6+MD+UA EU accession 8

| | | | |
|---|---|---|---|
| AL | Albania | MK | North Macedonia |
| BA | Bosnia and Herzegovina | RS | Serbia |
| MD | Moldova | UA | Ukraine |
| ME | Montenegro | XK | Kosovo |

## MD+UA New EU accession 2

| | |
|---|---|
| MD | Moldova |
| UA | Ukraine |

## CIS3 Commonwealth of Independent States-3

| | |
|---|---|
| BY | Belarus |
| KZ | Kazakhstan |
| RU | Russia |

## EU27 European Union

| | | | |
|---|---|---|---|
| AT | Austria | IE | Ireland |
| BE | Belgium | IT | Italy |
| BG | Bulgaria | LT | Lithuania |
| CY | Cyprus | LU | Luxembourg |
| CZ | Czechia | LV | Latvia |
| DE | Germany | MT | Malta |
| DK | Denmark | NL | Netherlands |
| EE | Estonia | PL | Poland |
| EL | Greece | PT | Portugal |
| ES | Spain | RO | Romania |
| FI | Finland | SE | Sweden |
| FR | France | SI | Slovenia |
| HR | Croatia | SK | Slovakia |
| HU | Hungary | | |

## EA20 Euro area

| | | | |
|---|---|---|---|
| AT | Austria | IE | Ireland |
| BE | Belgium | IT | Italy |
| CY | Cyprus | LT | Lithuania |
| DE | Germany | LU | Luxembourg |
| EE | Estonia | LV | Latvia |
| EL | Greece | MT | Malta |
| ES | Spain | NL | Netherlands |
| FI | Finland | PT | Portugal |
| FR | France | SI | Slovenia |
| HR | Croatia | SK | Slovakia |

# Summer 2024 interim forecast update

**Table 1 / OVERVIEW 2022-2023 AND OUTLOOK 2024-2026**

| | | GDP real change in % against prev. year | | | | | Consumer prices average change in % against prev. year | | | | | Unemployment (LFS) rate in %, annual average | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | Forecast | | | | | Forecast | | | | | Forecast | | |
| | | 2022 | 2023 | 2024 | 2025 | 2026 | 2022 | 2023 | 2024 | 2025 | 2026 | 2022 | 2023 | 2024 | 2025 | 2026 |
| BG | Bulgaria | 3.9 | 1.8 | 2.0 | 2.5 | 3.0 | 13.0 | 8.6 | 4.0 | 3.0 | 3.0 | 4.3 | 4.3 | 4.2 | 4.1 | 4.0 |
| CZ | Czechia | 2.4 | -0.3 | 1.2 | 2.5 | 2.7 | 14.8 | 12.0 | 2.4 | 2.2 | 2.2 | 2.2 | 2.6 | 3.0 | 2.6 | 2.6 |
| EE | Estonia | -0.5 | -3.0 | 0.2 | 3.2 | 3.6 | 19.4 | 9.1 | 3.2 | 2.8 | 2.1 | 5.6 | 6.4 | 7.3 | 6.6 | 6.1 |
| HR | Croatia | 7.0 | 3.1 | 3.0 | 2.9 | 3.0 | 10.7 | 8.4 | 3.7 | 2.9 | 2.5 | 7.0 | 6.1 | 6.1 | 6.0 | 6.0 |
| HU | Hungary | 4.6 | -0.9 | 2.0 | 2.5 | 2.9 | 15.3 | 17.0 | 4.5 | 3.8 | 3.5 | 3.6 | 4.1 | 4.4 | 4.0 | 3.7 |
| LT | Lithuania | 2.4 | -0.3 | 1.7 | 2.2 | 2.6 | 18.9 | 8.7 | 1.5 | 2.3 | 2.5 | 6.0 | 6.9 | 7.2 | 6.7 | 6.4 |
| LV | Latvia | 3.0 | -0.3 | 1.6 | 2.5 | 2.7 | 17.2 | 9.1 | 1.4 | 2.2 | 2.7 | 6.9 | 6.5 | 7.0 | 6.7 | 6.4 |
| PL | Poland | 5.6 | 0.2 | 3.3 | 3.6 | 3.3 | 13.2 | 10.9 | 4.5 | 3.5 | 2.8 | 2.9 | 2.8 | 2.8 | 3.0 | 3.0 |
| RO | Romania | 4.1 | 2.1 | 3.0 | 3.1 | 3.6 | 12.0 | 9.7 | 5.6 | 4.0 | 3.5 | 5.6 | 5.6 | 5.5 | 5.4 | 5.2 |
| SI | Slovenia | 2.5 | 1.6 | 2.4 | 2.5 | 2.6 | 9.3 | 7.2 | 2.8 | 2.3 | 2.2 | 4.0 | 3.7 | 3.6 | 3.6 | 3.5 |
| SK | Slovakia | 1.9 | 1.6 | 2.0 | 2.2 | 2.6 | 12.1 | 11.0 | 2.8 | 3.4 | 3.4 | 6.1 | 5.8 | 5.8 | 5.6 | 5.4 |
| | *EU-CEE11 [1)2)]* | *4.3* | *0.6* | *2.6* | *3.0* | *3.1* | *13.5* | *10.9* | *4.1* | *3.3* | *2.9* | *4.0* | *4.1* | *4.1* | *4.1* | *4.0* |
| AL | Albania | 4.9 | 3.4 | 3.6 | 3.7 | 3.8 | 6.6 | 5.3 | 3.0 | 2.5 | 2.4 | 10.9 | 10.7 | 10.4 | 10.2 | 10.0 |
| BA | Bosnia and Herzegovina | 4.2 | 1.7 | 2.5 | 2.9 | 3.4 | 14.0 | 6.1 | 2.4 | 2.2 | 2.0 | 15.4 | 13.2 | 12.9 | 12.7 | 12.4 |
| ME | Montenegro | 6.4 | 6.0 | 4.2 | 3.7 | 3.5 | 11.9 | 8.7 | 4.5 | 3.0 | 2.5 | 14.7 | 13.1 | 11.0 | 10.0 | 9.0 |
| MK | North Macedonia | 2.2 | 1.0 | 2.0 | 2.5 | 2.8 | 14.0 | 9.0 | 3.5 | 3.0 | 2.5 | 14.4 | 13.1 | 12.5 | 11.8 | 11.0 |
| RS | Serbia | 2.5 | 2.5 | 3.5 | 3.6 | 3.7 | 11.7 | 12.1 | 4.5 | 3.5 | 2.8 | 9.4 | 9.5 | 9.0 | 8.5 | 8.0 |
| XK | Kosovo | 4.3 | 3.3 | 3.6 | 3.8 | 3.9 | 11.6 | 4.9 | 2.9 | 2.3 | 2.2 | 12.5 | 12.4 | 12.3 | 12.0 | 11.5 |
| | *WB6 [1)2)]* | *3.4* | *2.6* | *3.2* | *3.4* | *3.6* | *11.7* | *9.0* | *3.7* | *3.0* | *2.5* | *11.7* | *11.1* | *10.6* | *10.2* | *9.8* |
| MD | Moldova | -4.6 | 0.7 | 3.0 | 3.5 | 4.0 | 28.7 | 13.4 | 4.0 | 5.0 | 5.0 | 3.1 | 4.6 | 4.3 | 4.0 | 3.5 |
| UA | Ukraine | -28.8 | 5.3 | 2.7 | 4.0 | 4.5 | 20.2 | 12.9 | 6.5 | 7.5 | 6.0 | 25.0 | 20.0 | 15.0 | 10.0 | 9.0 |
| | *New EU accession 2 [1)2)]* | *-26.8* | *4.9* | *2.7* | *4.0* | *4.5* | *20.9* | *12.9* | *6.3* | *7.3* | *5.9* | *23.9* | *19.2* | *14.4* | *9.7* | *8.7* |
| TR | Turkey | 5.5 | 4.5 | 3.4 | 4.0 | 4.5 | 72.3 | 54.0 | 59.0 | 31.0 | 26.0 | 10.5 | 9.4 | 10.0 | 10.5 | 10.0 |
| BY | Belarus | -4.7 | 3.9 | 3.5 | 2.3 | 2.5 | 15.2 | 5.1 | 8.0 | 7.0 | 6.0 | 3.6 | 3.5 | 3.4 | 3.3 | 3.3 |
| KZ | Kazakhstan | 3.2 | 5.1 | 4.2 | 4.9 | 4.9 | 15.0 | 14.7 | 8.3 | 6.0 | 5.8 | 4.9 | 4.7 | 4.7 | 4.6 | 4.5 |
| RU | Russia | -1.2 | 3.6 | 3.2 | 2.5 | 2.5 | 13.8 | 5.9 | 7.2 | 4.6 | 3.7 | 3.9 | 3.2 | 2.7 | 2.5 | 2.4 |
| | *CIS3 [1)2)]* | *-0.9* | *3.8* | *3.3* | *2.7* | *2.7* | *13.9* | *6.8* | *7.3* | *4.8* | *4.0* | *4.0* | *3.3* | *2.9* | *2.8* | *2.7* |
| | *V4+SI [1)2)]* | *4.5* | *0.1* | *2.6* | *3.1* | *3.1* | *13.6* | *11.8* | *3.9* | *3.3* | *2.8* | *3.2* | *3.3* | *3.4* | *3.3* | *3.3* |
| | *BALT3 [1)2)]* | *1.9* | *-0.9* | *1.3* | *2.5* | *2.9* | *18.6* | *8.9* | *1.9* | *2.4* | *2.5* | *6.1* | *6.6* | *7.2* | *6.7* | *6.3* |
| | *EU-SEE3 [1)2)]* | *4.5* | *2.2* | *2.8* | *3.0* | *3.4* | *12.0* | *9.3* | *5.0* | *3.7* | *3.3* | *5.5* | *5.4* | *5.3* | *5.2* | *5.0* |
| | *EU accession 8 [1)2)]* | *-14.2* | *4.0* | *2.9* | *3.7* | *4.1* | *17.0* | *11.3* | *5.2* | *5.5* | *4.5* | *20.3* | *16.8* | *13.3* | *9.8* | *9.0* |
| | *non-EU12 [1)2)]* | *-0.1* | *4.0* | *3.3* | *3.2* | *3.4* | *32.3* | *21.8* | *23.2* | *13.0* | *10.9* | *8.3* | *7.0* | *6.3* | *5.8* | *5.5* |
| | *CESEE23 [1)2)]* | *1.3* | *3.0* | *3.1* | *3.2* | *3.3* | *26.6* | *18.5* | *17.4* | *10.1* | *8.5* | *7.3* | *6.3* | *5.8* | *5.4* | *5.1* |
| | *EA20 [3)]* | *3.4* | *0.5* | *0.6* | *1.6* | *1.6* | *8.4* | *5.4* | *2.5* | *2.2* | *2.0* | *6.8* | *6.6* | *6.7* | *6.6* | *6.6* |
| | *EU27 [3)]* | *3.4* | *0.5* | *0.8* | *1.8* | *1.8* | *9.2* | *6.4* | *2.7* | *2.4* | *2.2* | *6.2* | *6.1* | *5.9* | *5.8* | *5.8* |

## Table 1 / OVERVIEW 2022-2023 AND OUTLOOK 2024-2026 (contd.)

| | | Current account in % of GDP | | | | | Fiscal balance in % of GDP | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | Forecast | | | | | Forecast | | |
| | | 2022 | 2023 | 2024 | 2025 | 2026 | 2022 | 2023 | 2024 | 2025 | 2026 |
| BG | Bulgaria | -1.4 | -0.3 | -1.2 | -1.5 | -1.8 | -2.9 | -1.9 | -4.0 | -3.0 | -3.0 |
| CZ | Czechia | -4.9 | 0.4 | 0.4 | 0.8 | 1.4 | -3.2 | -3.7 | -2.5 | -2.0 | -1.5 |
| EE | Estonia | -3.2 | -2.1 | -2.0 | -2.2 | -1.9 | -1.0 | -3.4 | -3.4 | -4.5 | -3.6 |
| HR | Croatia | -2.8 | 1.1 | 0.2 | 1.0 | 1.3 | 0.1 | -0.7 | -2.0 | -1.4 | -1.2 |
| HU | Hungary | -8.4 | 0.2 | 0.2 | 0.3 | 0.4 | -6.2 | -6.7 | -5.5 | -4.0 | -3.5 |
| LT | Lithuania | -5.5 | 1.9 | 2.2 | 2.8 | 2.5 | -0.6 | -0.8 | -2.5 | -2.5 | -2.3 |
| LV | Latvia | -4.8 | -4.0 | -3.1 | -4.6 | -5.7 | -4.6 | -2.2 | -2.8 | -2.3 | -2.0 |
| PL | Poland | -2.4 | 1.6 | 1.0 | -0.3 | 0.0 | -3.4 | -5.1 | -5.9 | -5.4 | -5.3 |
| RO | Romania | -9.2 | -7.0 | -6.8 | -6.0 | -6.0 | -6.3 | -6.6 | -6.8 | -4.8 | -3.8 |
| SI | Slovenia | -1.0 | 4.5 | 3.0 | 2.4 | 2.5 | -3.0 | -2.5 | -3.1 | -2.3 | -0.6 |
| SK | Slovakia | -7.3 | -1.6 | -1.3 | -0.9 | -1.0 | -1.7 | -4.9 | -6.0 | -5.0 | -4.0 |
| | *EU-CEE11 1)2)* | *-4.8* | *-0.4* | *-0.7* | *-1.0* | *-0.8* | *-3.7* | *-4.6* | *-5.0* | *-4.2* | *-3.7* |
| AL | Albania | -5.9 | -0.9 | -1.4 | -1.3 | -1.4 | -3.7 | -1.3 | -1.5 | -1.5 | -2.0 |
| BA | Bosnia and Herzegovina | -4.3 | -2.8 | -3.6 | -3.4 | -3.2 | -0.4 | 1.0 | -0.5 | -0.7 | -1.0 |
| ME | Montenegro | -12.9 | -11.4 | -10.7 | -10.6 | -10.4 | -4.2 | 0.6 | -4.0 | -4.0 | -4.0 |
| MK | North Macedonia | -6.1 | 0.7 | -0.8 | -1.9 | -2.4 | -4.4 | -4.9 | -4.0 | -3.0 | -2.5 |
| RS | Serbia | -6.9 | -2.6 | -2.7 | -2.9 | -2.9 | -3.2 | -2.2 | -2.0 | -1.5 | -1.0 |
| XK | Kosovo | -10.3 | -7.6 | -8.6 | -8.7 | -8.5 | -0.5 | -0.3 | -1.0 | -1.0 | -1.5 |
| | *WB6 1)2)* | *-6.7* | *-2.8* | *-3.2* | *-3.4* | *-3.4* | *-2.7* | *-1.5* | *-1.9* | *-1.6* | *-1.5* |
| MD | Moldova | -17.1 | -11.9 | -9.7 | -8.9 | -8.1 | -3.2 | -5.2 | -4.8 | -3.8 | -3.5 |
| UA | Ukraine | 4.9 | -5.2 | -8.0 | -10.0 | -10.0 | -16.1 | -20.3 | -18.0 | -15.0 | -12.0 |
| | *New EU accession 2 1)2)* | *3.1* | *-5.7* | *-8.2* | *-9.9* | *-9.8* | *-15.1* | *-19.0* | *-16.8* | *-14.0* | *-11.3* |
| TR | Turkey | -5.4 | -4.1 | -3.1 | -2.7 | -2.3 | -1.1 | -5.2 | -4.0 | -3.0 | -3.0 |
| BY | Belarus | 3.5 | -1.4 | -2.0 | -1.3 | -0.9 | -1.5 | -1.0 | -1.5 | -1.0 | -1.0 |
| KZ | Kazakhstan | 3.1 | -3.3 | -2.0 | -1.5 | -0.5 | -2.1 | -2.3 | -2.3 | -2.0 | -2.0 |
| RU | Russia | 10.5 | 2.5 | 3.8 | 3.3 | 3.0 | -1.4 | -2.3 | -1.2 | -1.5 | -1.0 |
| | *CIS3 1)2)* | *9.6* | *1.7* | *2.9* | *2.5* | *2.4* | *-1.4* | *-2.2* | *-1.3* | *-1.5* | *-1.1* |
| | *V4+SI 1)2)* | *-4.1* | *1.0* | *0.7* | *0.1* | *0.4* | *-3.6* | *-4.9* | *-5.1* | *-4.4* | *-4.0* |
| | *BALT3 1)2)* | *-4.7* | *-0.7* | *-0.3* | *-0.5* | *-0.8* | *-1.8* | *-1.8* | *-2.8* | *-3.0* | *-2.6* |
| | *EU-SEE3 1)2)* | *-6.6* | *-4.5* | *-4.7* | *-4.1* | *-4.1* | *-4.6* | *-4.8* | *-5.5* | *-3.9* | *-3.3* |
| | *EU accession 8 1)2)* | *-1.2* | *-4.4* | *-5.9* | *-6.9* | *-6.9* | *-9.7* | *-11.2* | *-10.0* | *-8.3* | *-6.8* |
| | *non-EU12 1)2)* | *5.1* | *-0.5* | *0.2* | *-0.1* | *-0.1* | *-2.0* | *-3.9* | *-3.0* | *-2.7* | *-2.3* |
| | *CESEE23 1)2)* | *1.8* | *-0.5* | *-0.1* | *-0.4* | *-0.4* | *-2.6* | *-4.2* | *-3.8* | *-3.2* | *-2.8* |
| | *EA20 3)* | *1.3* | *2.9* | *2.5* | *2.5* | *2.5* | *-3.7* | *-3.6* | *-2.6* | *-2.6* | *-2.5* |
| | *EU27 3)* | *1.2* | *2.9* | *2.5* | *2.5* | *2.5* | *-3.4* | *-3.5* | *-2.2* | *-2.2* | *-2.1* |

1) wiiw estimates. - 2) Current account data include transactions within the region (sum over individual countries). -
3) Forecasts estimated by wiiw.
Source: wiiw, Eurostat. Forecasts by wiiw. Cut-off date for historical data and forecasts: 13 June 2024.

**Table 2 / Policy rate and exchange rate for selected CESEE countries: overview 2022-2023 and outlook 2024-2026**

| | | Policy rate eop, p.a. | | | | | Exchange rate NCU/EUR average | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | | | Forecast | | | | | Forecast | | |
| | | 2022 | 2023 | 2024 | 2025 | 2026 | 2022 | 2023 | 2024 | 2025 | 2026 |
| AL | Albania | 2.75 | 3.25 | 3.25 | 3.00 | 3.00 | 118.98 | 108.80 | 103.00 | 102.00 | 102.00 |
| BY | Belarus | 12.00 | 9.50 | 10.00 | 10.00 | 9.00 | 2.78 | 3.25 | 3.50 | 3.70 | 3.80 |
| CZ | Czechia | 7.00 | 6.75 | 4.50 | 3.25 | 3.00 | 24.57 | 24.00 | 24.90 | 24.80 | 24.80 |
| HU | Hungary | 13.00 | 10.75 | 6.50 | 4.60 | 4.00 | 391.29 | 381.85 | 398.00 | 410.00 | 415.00 |
| KZ | Kazakhstan | 16.75 | 15.75 | 13.50 | 10.00 | 9.00 | 484.22 | 493.33 | 495.00 | 500.00 | 510.00 |
| MD | Moldova | 20.00 | 4.75 | 3.60 | 4.00 | 4.00 | 19.90 | 19.64 | 19.80 | 20.00 | 20.00 |
| MK | North Macedonia | 4.75 | 6.30 | 5.75 | 5.00 | 4.50 | 61.62 | 61.56 | 61.60 | 61.60 | 61.60 |
| PL | Poland | 6.75 | 5.75 | 5.50 | 5.00 | 4.00 | 4.69 | 4.54 | 4.30 | 4.35 | 4.40 |
| RO | Romania | 6.75 | 7.00 | 6.50 | 4.00 | 3.00 | 4.93 | 4.95 | 5.00 | 5.05 | 5.12 |
| RS | Serbia | 5.00 | 6.50 | 5.50 | 5.00 | 4.50 | 117.46 | 117.25 | 117.00 | 116.50 | 116.00 |
| RU | Russia | 7.50 | 16.00 | 16.00 | 13.00 | 10.00 | 72.48 | 92.14 | 102.00 | 105.00 | 110.00 |
| TR | Turkey | 9.00 | 42.50 | 40.00 | 30.00 | 20.00 | 17.41 | 25.76 | 39.00 | 48.00 | 53.00 |
| UA | Ukraine | 25.00 | 15.00 | 13.00 | 11.00 | 9.00 | 33.98 | 39.56 | 43.00 | 45.00 | 46.00 |

Source: wiiw, forecasts by wiiw. Cut-off date for historical data and forecasts: 13 June 2024.

# 1. Global assumptions: Getting better, slowly

BY RICHARD GRIEVESON

**In recent months, the global economy has continued its steady, if unspectacular, recovery from the 2022-2023 inflation shock.** High-frequency indicators for the world's most important economies – the US, China and the euro area – all point generally in the direction of either robust growth (the US and China) or an improvement from weaker levels (the euro area). This is good news for CESEE's mostly very open and internationally integrated economies.

**While signs of improvement are visible, 2024 overall will not be a great year for the euro area, and more sustained momentum is only likely to be fully visible in the data from 2025.** Despite improvements, according to the most recent purchasing managers' indices the industrial sector is still contracting – especially in Germany – and real financial conditions are tight. Private consumption is doing slightly better as real wages rise; but a lot of this extra money is being saved, rather than spent. The continued weakness of the German industrial sector, in particular, is a major barrier to improved growth in CESEE, given the region's high level of export dependence on Europe's biggest economy.

**Table 3 / wiiw summer 2024 global assumptions**

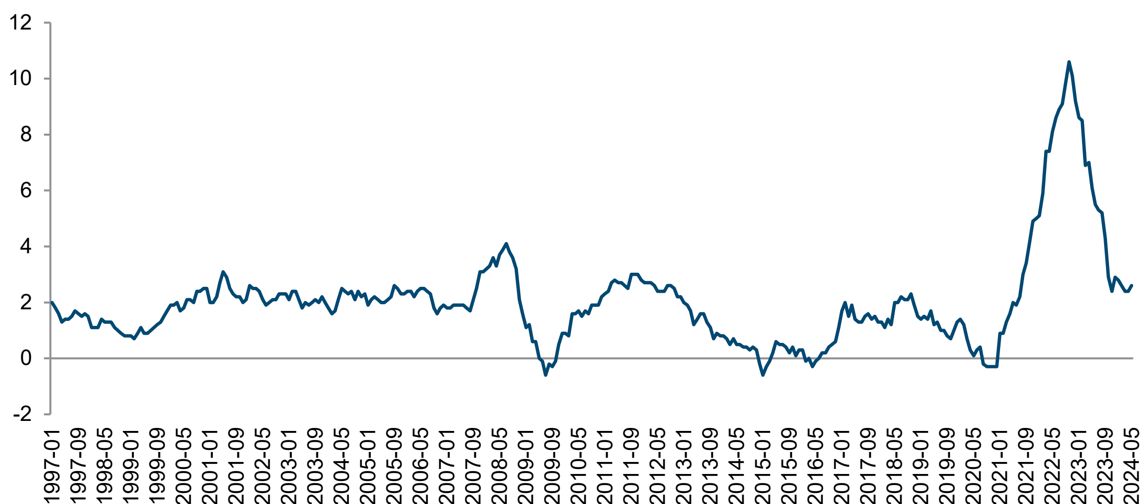
| | Summer 2024 | | | Changes since spring | | |
|---|---|---|---|---|---|---|
| | 2024 | 2025 | 2026 | 2024 | 2025 | 2026 |
| Euro area real GDP growth, % | 0.6 | 1.6 | 1.6 | 0.0 | 0.0 | 0.0 |
| Euro area HICP, % | 2.5 | 2.2 | 2.0 | 0.0 | 0.0 | 0.0 |
| Euro area unemployment rate, % | 6.7 | 6.6 | 6.6 | 0.0 | 0.0 | 0.0 |
| Euro area current account, % of GDP | 2.5 | 2.5 | 2.5 | -0.7 | -0.7 | -0.6 |
| USD/EUR exchange rate, average | 1.08 | 1.08 | 1.08 | 0.0 | 0.0 | 0.0 |
| ECB refinancing rate, %, eop | 3.50 | 2.50 | 2.00 | 0.0 | 0.0 | 0.0 |
| Brent crude oil, USD per barrel, average | 83.0 | 80.0 | 77.0 | 3.0 | 3.0 | 3.0 |

Source: wiiw forecasts. Cut-off date: 13 June 2024.

**From the end of this year and into 2025, the outlook for the euro area is brighter.** The industrial sector should recover; private consumption will pick up pace on the back of real wage growth, greater consumer confidence and lower inflation; and investment should rise on account of drawdowns from EU funds and the pass-through from loose monetary policy. The European Central Bank (ECB) trimmed its interest rates in June and is likely to make further cuts in the coming quarters. As the euro area economy strengthens, there will be positive and fairly immediate spillovers for CESEE.

**The inflation outlook for the euro area is also basically unchanged from our Spring Forecast, meaning that the inflation shock has mostly passed.** However, we do not see inflation in the euro area returning to 2% on average until 2026, as some lingering effects of the price shocks of the past two years remain. Inflation in the euro area accelerated to 2.6% in May.

**Figure 1 / Euro area harmonised index of consumer prices (HICP), % change, year on year**




Source: Eurostat.

**We maintain our forecast that the euro will average 1.08 per dollar this year, although we see downside risks to this projection, given that the ECB is likely to prune interest rates more than the Fed in 2024.** Nevertheless, the initial rate cut by the ECB in June does not seem to have exerted any significant downside pressure on the euro, indicating that the market does not expect substantial and persistent divergence in the trajectory of monetary policy between the Fed and the ECB.

**For the summer, we have made a small upward adjustment to the oil price forecast, with a consequent deterioration in the current account balance.** Although the adjustment is not big, and will therefore have limited impact on overall inflation and economic growth, the risks to the oil price are currently skewed to the upside, due to the conflict in the Middle East. A sharp spike in oil prices would quickly reverse the positive trends in the global economy and CESEE, given the extent to which the current recovery is reliant on rising real wages and greater household spending in the wake of lower price growth.

**The main risk to the forecast is that Donald Trump wins the upcoming US election.** The main implication of a Trump victory would naturally be uncertainty: we simply do not know what he would do, as many of his statements are contradictory. Yet three things seem quite likely if he does win. First, there will be some kind of US protectionism directed towards Europe. That would hurt CESEE economies in particular, given their high level of openness and trade dependence. Second, there would be potentially very significant US protectionism directed towards China, which would weaken overall economic growth and lead to the re-routing of extra Chinese exports towards Europe. That could bring lower prices for some consumers in Europe, but it would also present a grave challenge to European firms, many of which are already struggling to compete with Chinese products. Third, a Trump victory would cast doubt on the US security commitment to Europe. This would have the greatest repercussions for Ukraine, but it could also have potentially serious security implications – and therefore also an adverse economic impact – in the Baltic states and the Balkans.

**A second risk for the euro area and CESEE economies emanating from political uncertainty stems from recent events in France.** The recent European Parliament elections did result in gains for the far right; however, at the time of writing it still looks as if centrist parties will have enough votes to maintain control over the key positions. This should mean consistency on EU support to Ukraine, and also the continuation of a gradual increase in measures to support the EU economy amid the US-China trade war. However, if the snap French election produces a government led by the far right, that would create huge uncertainty about future EU economic policy making and support for Ukraine. Following the announcement of the snap election, the cost of French borrowing relative to that of Germany rose sharply, underlining the uncertainty and worries about the economic impact of a far-right government in France.

**Beyond these two factors, we continue to see a range of potential risks on the horizon that could yet knock the euro area recovery off course, and lead to negative fallout for CESEE as well.** These include the potential for any escalation of the tension in the Middle East to bring higher oil prices and further disruption to global shipping, which in turn would push up inflation. In addition, growing trade tensions between the EU and China would have adverse economic effects if the situation were to escalate.

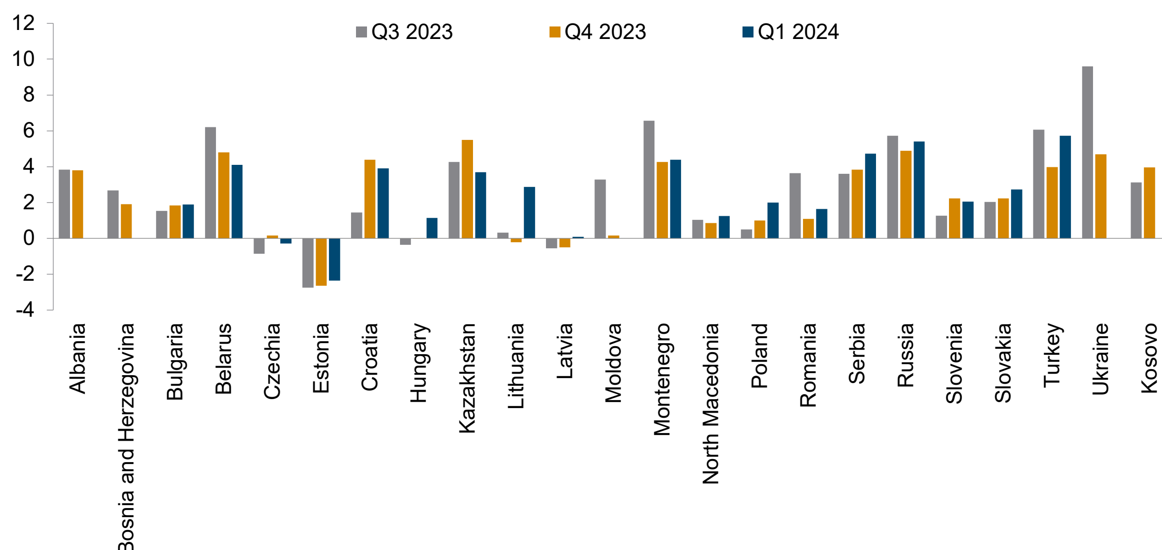
# 2. CESEE Overview: Solid but lopsided recovery

BY VASILY ASTROV[1]

## 2.1 ECONOMIC RECOVERY GATHERS MOMENTUM

**Recent data demonstrate that economic recovery in most countries of Central, East and Southeast Europe (CESEE) has gathered momentum.** Of the 18 CESEE countries for which data for Q1 2024 were available at the time of writing, in only five – Belarus, Czechia, Croatia, Kazakhstan and Slovenia – did economic growth slow on an annual basis, compared to Q4 2023 (Figure 2). The most notable positive turnaround was recorded in Lithuania, where GDP shot up by 2.9% in Q1, following near-stagnation in H2 2023. In Turkey, growth picked up by 1.7 percentage points (pp) compared to the previous quarter, to 5.7%, making it the regional frontrunner, while growth also exceeded the 5% mark in Russia. At the opposite end of the spectrum, Estonia was the only country that was still mired in recession in Q1 – at -2.4%, a figure virtually unchanged from H2 2023. In Czechia and Latvia, the economy continued to stagnate.

**Figure 2 / Real GDP growth, in %, year on year**



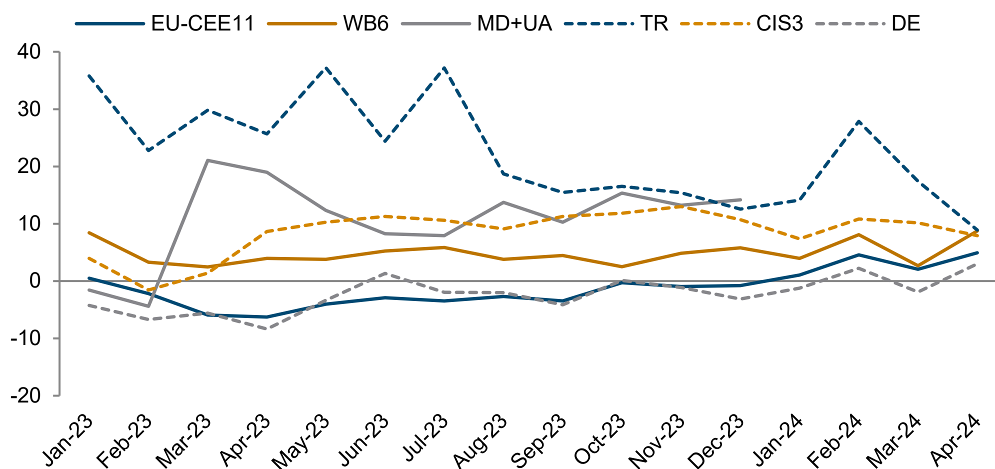

Note: no data for Q1 2024 for Albania, Bosnia and Herzegovina, Moldova, Ukraine and Kosovo.
Source: wiiw Monthly Database and Eurostat.

[1] The author thanks Richard Grieveson, Doris Hanzl-Weiss and Branimir Jovanović for the valuable comments and suggestions on the first draft.

## 2.2 PRIVATE CONSUMPTION IMPROVING, INDUSTRY STILL STRUGGLING

**The main factor underpinning the acceleration in growth has been improving private consumption.** This represents a continuation of the trend that was already emphasised in our Spring Forecast.[2] In January-April 2024, the annual dynamics of retail trade turnover – a proxy for private consumption – switched to positive in EU-CEE (after a decline over the previous four months) and accelerated in the Western Balkans and Turkey (Figure 3). Only in CIS3 did it lose steam somewhat – from 11.7% to 9.1% (mostly on account of Kazakhstan) – though it remained strong nonetheless. Positive trends in retail trade have gone hand in hand with rising consumer confidence – although in many EU-CEE countries (especially Estonia), as well as in Turkey, that is still at below the long-term average (Figure 4).

**Figure 3 / Retail trade turnover, real growth in %, year on year**




Notes: simple average over available countries; WB6 – excluding Kosovo; missing data for Albania, Bosnia and Herzegovina, and Ukraine for 2024.
Source: national statistical offices and Eurostat.

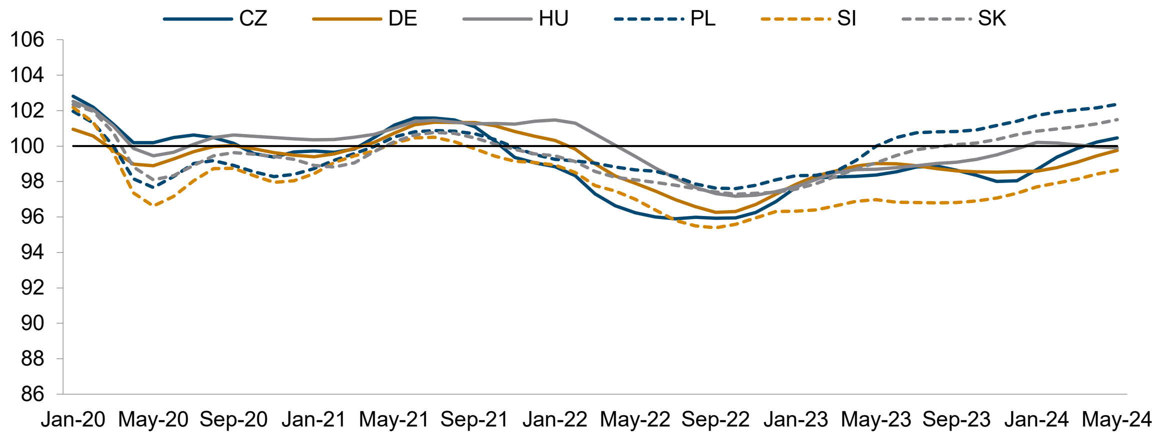
**By contrast – and as was already emphasised in our Spring Forecast – the industry and exports of most CESEE countries continued to struggle, dragged down by the ongoing industrial weakness in Germany.** Figure 5 shows that those sub-regions that recorded the worst performance on industrial production in Q1 were, once again, EU-CEE and the Western Balkans. Both groups are heavily dependent on demand from Germany: (gross) merchandise exports to it account for as much as 27% of GDP in North Macedonia, 25% in Czechia, 20% in Hungary and 19% in Slovakia.[3] It therefore comes as no surprise that industrial production in EU-CEE has now been sliding – or in the Western Balkans stagnating – for six quarters in a row. Business confidence, too, remains generally depressed: among the countries of EU-CEE, only Latvia and Lithuania saw the business confidence index in May marginally exceed the long-term average (Figure 6). By contrast, countries outside the German-led manufacturing cluster, such as the CIS and Turkey, have shown much better industrial performance recently (Figure 5). In Russia, this reflects a combination of booming military production, import substitution in some sectors, and the partial recovery of industries that were initially badly hit by sanctions.

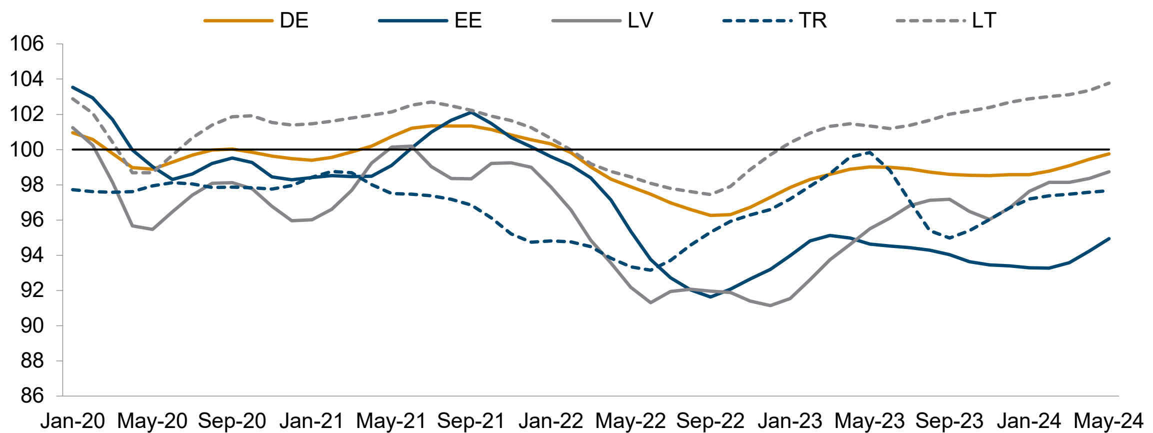
[2] Pindyuk et al. (2024).

[3] As of 2023.

**Figure 4 / Consumer confidence index**

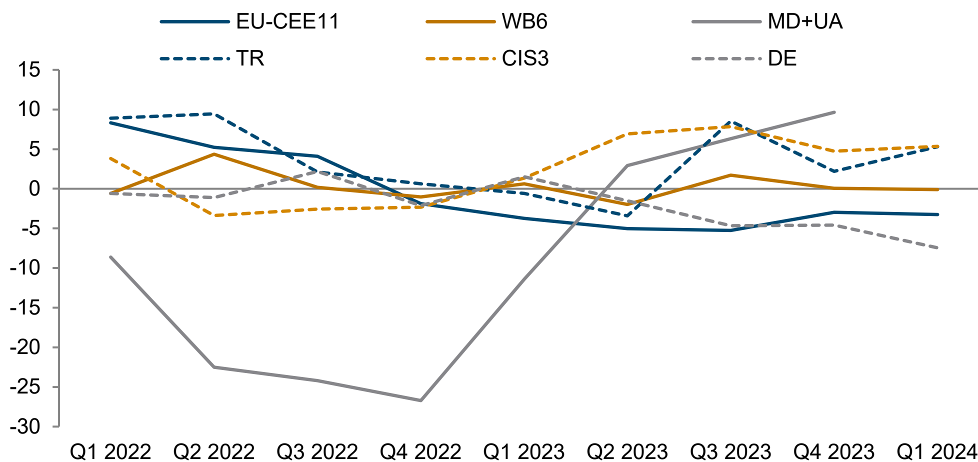
Long-term average=100



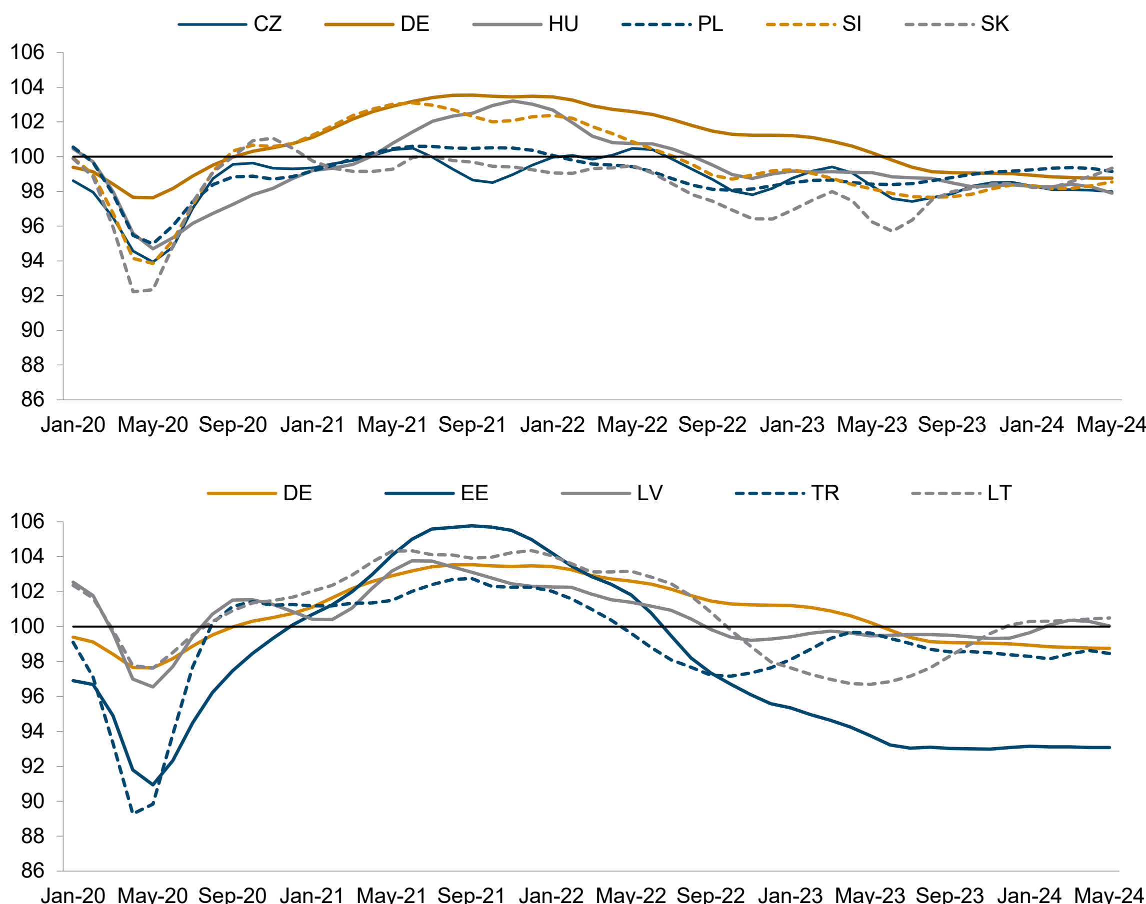

Sources: OECD, own calculations.

**Figure 5 / Gross industrial production, real growth in %, year on year**




Note: simple average over available countries, no data for Q1 2024 for Albania, Kosovo and Ukraine.
Sources: wiiw Monthly Database and Eurostat, own calculations.

**Figure 6 / Business confidence index**

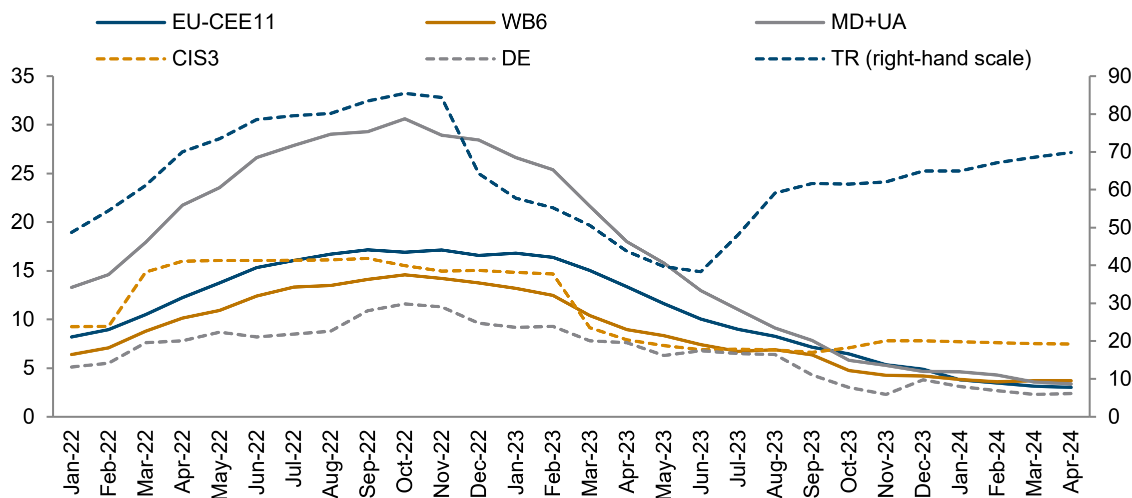



Sources: OECD, own calculations.

## 2.3 IS DISINFLATION NEARING ITS END?

**In the vast majority of CESEE countries, inflation has continued on its downward trend** (Figure 7), **prompting downward forecast revisions in many cases.** In most EU-CEE and Western Balkan countries, inflation has slowed to 2-3% on an annual basis, thus approaching (or even undershooting) the target in countries with inflation-targeting regimes. In Latvia and Lithuania, it has been hovering at a particularly low level, attesting to the recent weakness in consumer demand in those countries. As a consequence, for nine CESEE countries the inflation forecast for 2024 as a whole has been revised downwards, compared to our Spring Forecast; in only four countries – all of them in EU-CEE – will inflation be higher than expected in spring (Table 4). Weakening price pressures have allowed a further relaxation of monetary policy in a number of countries, with Czechia, Hungary, Serbia, Moldova, Ukraine and Kazakhstan having cut policy interest rates over the past few months. Still, in real terms policy interest rates are nearly everywhere in positive territory.

**Figure 7 / Consumer price index, year-on-year growth in %**




Note: simple average over available countries.
Sources: wiiw Monthly Database and Eurostat.

**However, in many CESEE countries inflationary pressures are likely to pick up in the coming months.** The main reasons for this are a further recovery in consumer demand and the strong growth of nominal wages, translating into rising production costs. In many countries, wage settlements for 2024 were based on still relatively high inflationary expectations. Besides, with economic recovery under way, labour shortages are resurfacing, to exert upward pressure on wages. Pro-inflationary country-specific factors are playing a role as well (the recent removal of price controls in North Macedonia and hikes in regulated tariffs in Romania), or will do so in the near future (forthcoming deregulation of energy utilities in Poland). Partly because of all this, in many CESEE countries the monetary easing cycle is likely either to proceed only slowly (Czechia, Romania, North Macedonia, Kazakhstan) or to be put on the back burner, at least until the end of the year (Albania, Moldova). In Poland, it was already interrupted back in October 2023.

**Inflationary pressures remain stubbornly high in Belarus, Russia and Turkey, arguably reflecting conditions of economic overheating.** On current trends, monetary policy in Russia is set to remain tight, while in Belarus the policy interest rate looks likely to be hiked in the coming months. In Turkey, where the extremely high inflation – a long-standing feature of its economic model – has picked up further to reach 75.4% in May, financial conditions have been tightened via stricter macro-prudential regulations and increased reserve requirements. This will likely lead to a gradual downward trend in inflation in Turkey over the remainder of the year. However, given the overall pro-growth policy mix in all three countries (and the massive labour shortages in Russia and Belarus, partly on account of military mobilisation and/or emigration), rapid disinflation is hardly to be expected.

**Table 4 / CPI growth forecasts and direction of revisions since wiiw Spring 2024 Forecast Report**

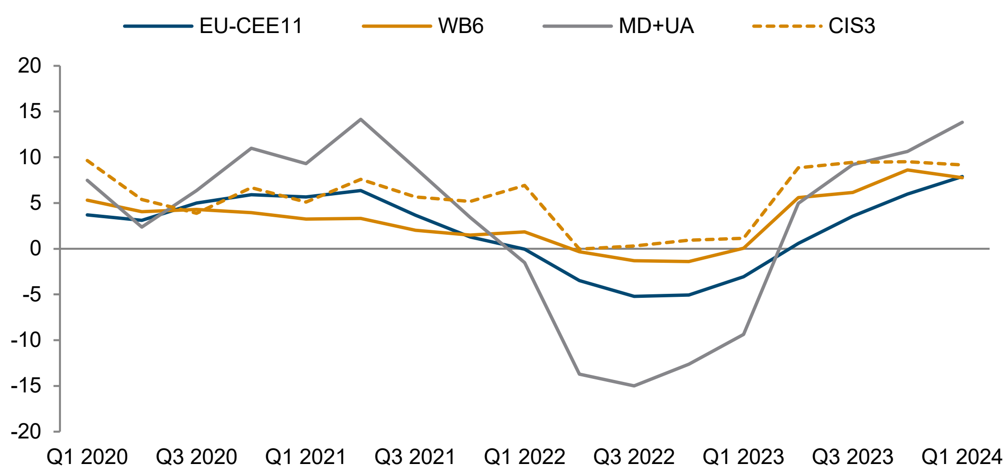
| Region | | 2024 | | 2025 | | 2026 | |
|---|---|---|---|---|---|---|---|
| **EU-CEE** | | | | | | | |
| BG | Bulgaria | 4.0 | ▲ | 3.0 | | 3.0 | |
| CZ | Czechia | 2.4 | ▲ | 2.2 | | 2.2 | |
| EE | Estonia | 3.2 | ▼ | 2.8 | | 2.1 | ▼ |
| HR | Croatia | 3.7 | ▲ | 2.9 | | 2.5 | |
| HU | Hungary | 4.5 | ▼ | 3.8 | ▼ | 3.5 | |
| LT | Lithuania | 1.5 | | 2.3 | | 2.5 | |
| LV | Latvia | 1.4 | | 2.2 | | 2.7 | |
| PL | Poland | 4.5 | | 3.5 | | 2.8 | |
| RO | Romania | 5.6 | ▼ | 4.0 | | 3.5 | |
| SI | Slovenia | 2.8 | ▼ | 2.3 | ▼ | 2.2 | |
| SK | Slovakia | 2.8 | ▲ | 3.4 | | 3.4 | |
| **Western Balkans** | | | | | | | |
| AL | Albania | 3.0 | | 2.5 | | 2.4 | |
| BA | Bosnia and Herzegovina | 2.4 | ▼ | 2.2 | ▼ | 2.0 | |
| ME | Montenegro | 4.5 | | 3.0 | | 2.5 | |
| MK | North Macedonia | 3.5 | | 3.0 | | 2.5 | |
| RS | Serbia | 4.5 | | 3.5 | | 2.8 | |
| XK | Kosovo | 2.9 | ▼ | 2.3 | ▼ | 2.2 | |
| **New EU accession 2** | | | | | | | |
| MD | Moldova | 4.0 | ▼ | 5.0 | | 5.0 | ▲ |
| UA | Ukraine | 6.5 | ▼ | 7.5 | ▲ | 6.0 | |
| **Turkey** | | | | | | | |
| TR | Turkey | 59.0 | | 31.0 | | 26.0 | |
| **CIS3** | | | | | | | |
| BY | Belarus | 8.0 | | 7.0 | | 6.0 | |
| KZ | Kazakhstan | 8.3 | ▼ | 6.0 | ▼ | 5.8 | ▼ |
| RU | Russia | 7.2 | | 4.6 | ▲ | 3.7 | |

Source: wiiw forecasts as of 13 June 2024.

## 2.4 RISING WAGES BENEFIT PRIVATE CONSUMPTION – BUT ONLY TO AN EXTENT

**High nominal wage growth and recent disinflation have contributed to a recovery in real wages** (Figure 8)**.** In Q1, in nearly half of CESEE countries the annual growth in real wages picked up pace, and for the first time since Q1 2021 it turned positive everywhere in the region. It reached nearly 18% in Ukraine and was in double digits in Bulgaria, Belarus, Hungary, Latvia, Moldova, North Macedonia and Russia. In Czechia, real wages grew for the first time since Q3 2021. Given that many of the countries saw a pronounced decline in real wages in 2022-2023, there is generally ample scope for them to grow further in the coming years.

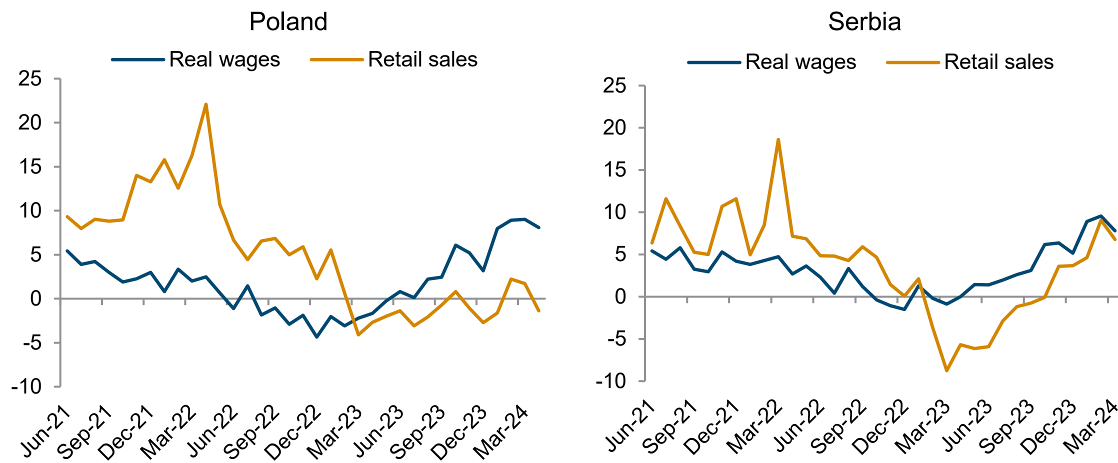
**Figure 8 / Real average gross monthly wages, growth in %, year on year**




Note: simple average over available countries; WB6 - excluding Kosovo; data for Turkey unavailable.
Sources: wiiw Monthly Database, national statistics, own calculations.

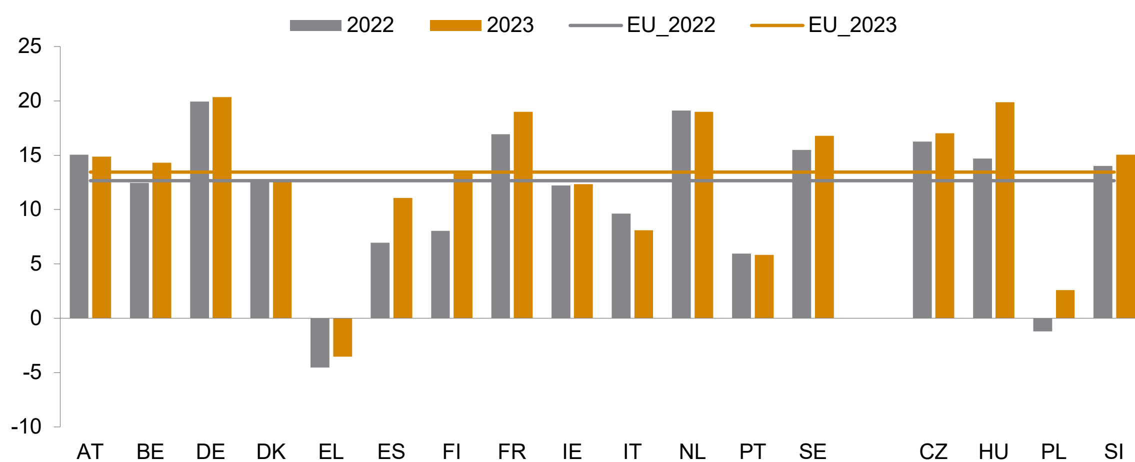
**However, rising wage incomes have only partly been channelled into consumer spending.** In most CESEE countries, developments in retail trade in Q1 lagged behind those in wages (Figure 9 demonstrates this divergence for Poland and Serbia). This may reflect the cautious attitude of many households in the face of great uncertainty; but it also has to do with the high – and in real terms positive – interest rates, which provide an incentive to save, rather than spend. This pattern is generally consistent with Figure 10, which shows the household saving rate for selected EU countries in 2022 and 2023. As may be seen, last year the household saving rate went up almost everywhere in the EU, including in EU-CEE, as, in part, households took advantage of the improved income situation to replenish savings (which were used in some countries to smooth consumption over the past two years, when real incomes were declining). This pattern has likely continued this year.

**Figure 9 / Retail trade turnover versus average gross monthly wages in Poland and Serbia, real growth in %, year on year**




Source: wiiw Monthly Database.

**Figure 10 / Household saving rate, in %**




Note: The household saving rate is defined as gross household saving divided by gross disposable income.
Source: Eurostat.

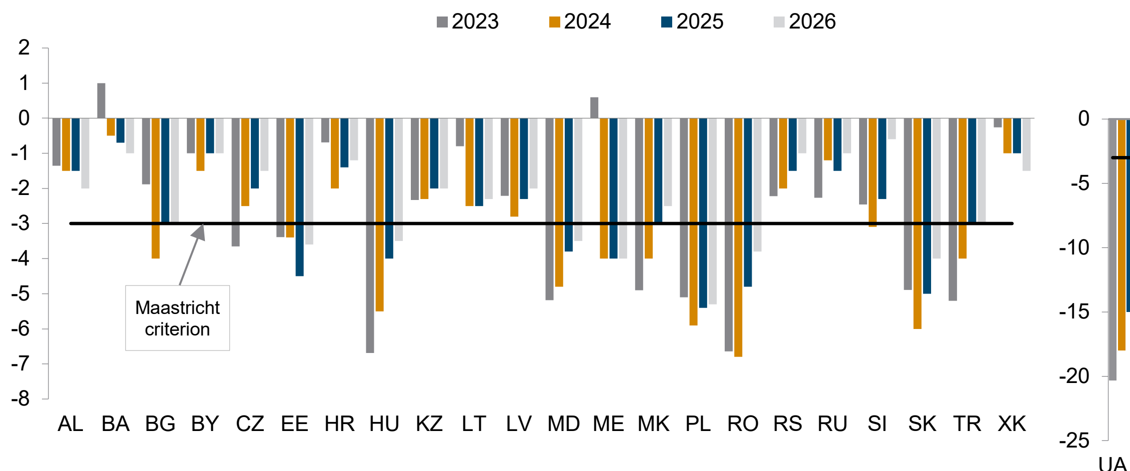
## 2.5 FISCAL CONSOLIDATION DELAYED

**Contrary to our earlier expectations,[4] the budget deficit is projected to rise this year in more than half of the CESEE countries** (Figure 11). The most marked deterioration in the budget balance – of 4.6 pp of GDP – is expected for Montenegro, followed by Bulgaria and Lithuania (around 2 pp each). Even in some countries that already recorded a very high deficit last year (such as Romania, Slovakia and Poland), it is projected to increase further. In war-torn Ukraine, the huge budget deficit is forecast to

[4] See e.g. Jovanović et al. (2023).

improve only moderately, to 18% of GDP; it will once again be mostly financed by EU and other Western assistance, as the country has no access to international financial markets under the current conditions.

**Figure 11 / General government budget balance as % of GDP**



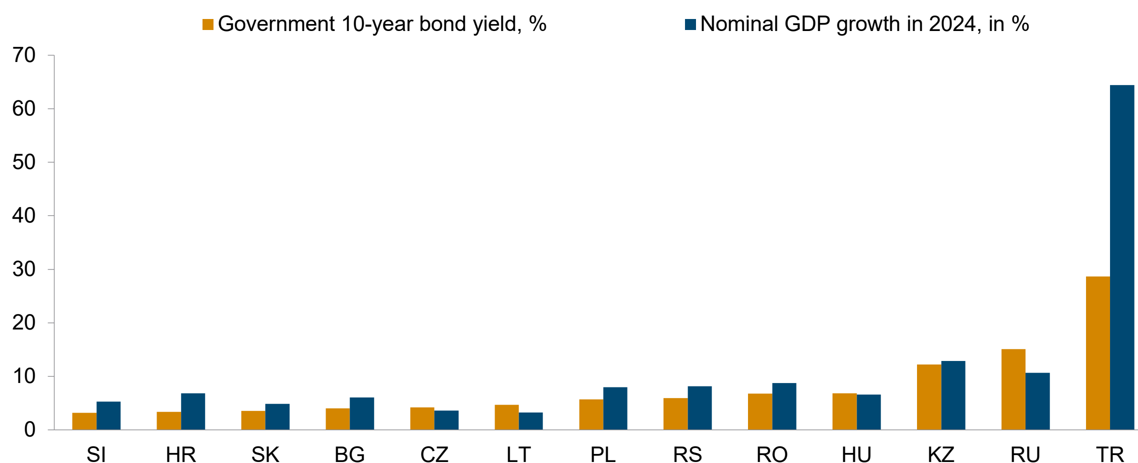

Note: 2023 - wiiw estimates for Bosnia and Herzegovina and Belarus; 2024-2026 - wiiw forecasts as of 13 June 2024.
Sources: wiiw Annual Database and Eurostat.

**In many countries, the budget deficit remains high, despite economic recovery being under way and the almost complete removal of support measures, which were introduced back in 2022 to cope with the cost-of-living crisis.** This is due to a number of factors. On the one hand, the lower-than-expected inflation in some countries has led to lower government revenue, compared to the original targets. On the other hand, military spending – which has already increased markedly since the start of the Russian invasion of Ukraine (especially in Poland and the Baltic states, where perceptions of the Russian threat are high)[5] – will remain at an elevated level, or may even rise further, effectively implying an end to the famous 'peace dividend' enjoyed by European countries over the past 30 years. For instance, Poland is planning to spend more than 4% of its GDP on defence this year,[6] making the country the frontrunner among Central and Eastern European NATO members. This is not far behind the 6% of GDP spent by Russia, which is embroiled in a full-fledged war. Besides, many CESEE countries are holding elections this year, which explains in part the generous fiscal policy of the incumbent governments (e.g. the hikes in public-sector wages in Albania, Croatia and Poland). Finally, and probably most importantly, there has been little pressure from the financial markets to consolidate, at least so far. In most countries, the yields on government bonds do not exceed the projected growth in nominal GDP (Figure 12). So long as this remains the case, public debt can generally be serviced from future revenue, without the debt ratio relative to GDP necessarily rising.

[5] For more on that, see Pindyuk et al. (2024), Figure 2.17.

[6] https://www.reuters.com/world/europe/polands-2024-budget-see-big-spending-defence-social-benefits-2023-08-24/

**Figure 12 / Government 10-year bond yields versus forecast of nominal GDP growth in 2024, in %**




Note: bond yields as of 13 June 2024. Nominal GDP growth calculated as real GDP growth forecast multiplied by inflation forecast in 2024.
Source: www.investing.com, wiiw forecasts as of 13 June 2024.

**The lax fiscal policy in many CESEE countries is conducive to growth, but is fraught with risks of its own.** In the EU, the reinstatement from July 2024 of the Maastricht fiscal criteria – budget deficit below 3% of GDP and public debt below 60% of GDP – means that any EU-CEE country in systematic breach of them will be subject to EU Excessive Deficit Procedure (EDP), potentially resulting in financial penalties. In its most recent report, from 19 June 2024, the European Commission recommended that EDP be initiated as early as July against three EU-CEE countries: Hungary, Poland and Slovakia (along with Belgium, France, Italy and Malta).[7] Against Romania, EDP has been formally running since 2020.[8]

## 2.6 OUTLOOK

**Compared with our Spring 2024 Forecast, the growth prospects for this year have generally improved.** For nine CESEE countries, the growth forecast has been revised upwards; for eight countries it has been left unchanged; and for only six countries has it been revised downwards (Table 5). The biggest upward revision – of 1.5 pp – is for Belarus, which is now economically closely integrated with Russia and is benefiting from the military fiscal stimulus in that country. The biggest downward revisions – of 0.5 pp apiece – are for Ukraine, Kazakhstan and Moldova. In Ukraine, Russia's recent destruction of around half of its power generation capacity will weigh on the economy, since it will take many months to repair the damage. In Kazakhstan, growth will suffer somewhat, mainly on account of OPEC+ production cuts, which will stay in place until at least September 2024.

[7] European Commission (2024).

[8] https://economy-finance.ec.europa.eu/economic-and-fiscal-governance/stability-and-growth-pact/corrective-arm-excessive-deficit-procedure/excessive-deficit-procedures-overview/romania_en

**Table 5 / Real GDP growth forecasts and direction of revisions since wiiw Spring 2024 Forecast Report**

| Region | | 2024 | | 2025 | | 2026 | |
|---|---|---|---|---|---|---|---|
| **EU-CEE** | | | | | | | |
| BG | Bulgaria | 2.0 | | 2.5 | | 3.0 | |
| CZ | Czechia | 1.2 | | 2.5 | | 2.7 | |
| EE | Estonia | 0.2 | ▼ | 3.2 | ▲ | 3.6 | |
| HR | Croatia | 3.0 | ▲ | 2.9 | ▲ | 3.0 | |
| HU | Hungary | 2.0 | ▲ | 2.5 | ▲ | 2.9 | |
| LT | Lithuania | 1.7 | ▲ | 2.2 | | 2.6 | |
| LV | Latvia | 1.6 | | 2.5 | | 2.7 | |
| PL | Poland | 3.3 | ▲ | 3.6 | ▲ | 3.3 | |
| RO | Romania | 3.0 | | 3.1 | ▼ | 3.6 | ▼ |
| SI | Slovenia | 2.4 | ▼ | 2.5 | ▼ | 2.6 | |
| SK | Slovakia | 2.0 | ▲ | 2.2 | | 2.6 | |
| **Western Balkans** | | | | | | | |
| AL | Albania | 3.6 | | 3.7 | | 3.8 | ▲ |
| BA | Bosnia and Herzegovina | 2.5 | | 2.9 | | 3.4 | |
| ME | Montenegro | 4.2 | | 3.7 | | 3.5 | |
| MK | North Macedonia | 2.0 | ▼ | 2.5 | ▼ | 2.8 | ▼ |
| RS | Serbia | 3.5 | ▲ | 3.6 | ▲ | 3.7 | ▲ |
| XK | Kosovo | 3.6 | ▲ | 3.8 | ▲ | 3.9 | ▲ |
| **New EU accession 2** | | | | | | | |
| MD | Moldova | 3.0 | ▼ | 3.5 | | 4.0 | |
| UA | Ukraine | 2.7 | ▼ | 4.0 | ▼ | 4.5 | ▼ |
| **Turkey** | | | | | | | |
| TR | Turkey | 3.4 | | 4.0 | | 4.5 | |
| **CIS3** | | | | | | | |
| BY | Belarus | 3.5 | ▲ | 2.3 | | 2.5 | |
| KZ | Kazakhstan | 4.2 | ▼ | 4.9 | | 4.9 | |
| RU | Russia | 3.2 | ▲ | 2.5 | | 2.5 | ▲ |

Source: wiiw forecasts as of 13 June 2024.

**The economy of CESEE as a whole is projected to grow by 3.1% this year[9] – roughly the same pace as in 2023** (Overview Table 1). The crucial assumption underlying this forecast is that the war in Ukraine will not spill over to other parts of CESEE. This applies even to Moldova, which is not a NATO member, but where security should be boosted by the Security and Defence Partnership agreement with the EU, signed in May 2024.[10]

The aggregate growth projection for CESEE as a whole masks huge differences across the individual sub-regions.

- In EU-CEE, growth should pick up by, on average, 2 pp compared to 2023 (to 2.6%), mostly thanks to more buoyant consumer spending, as well as public-sector investments, partly financed from the NextGenerationEU programme. This means that the convergence of EU-CEE countries with the EU average, which nearly stalled last year, will resume: the growth differential is likely to reach, on average, nearly 2 pp this year, which is roughly in line with the long-term average. With GDP growth of around 3%, Poland, Romania and Croatia will be the regional frontrunners, reflecting in part fiscal expansion in the former two countries and the strong performance of tourism in the latter. In Estonia, the economic dynamics is expected to switch to positive for the remainder of the year, translating into stagnation for 2024 as a whole.
- In the Western Balkans, growth should pick up by 0.6 pp this year, to reach 3.2% on average, with all countries apart from Montenegro growing faster than in 2023. The region continues to benefit from high inflows of remittances and foreign direct investment (partly reflecting near-shoring), large-scale public investment ahead of Expo 2027 in Serbia, and the good performance of tourism in Albania and Montenegro.
- In Turkey, growth is expected to decelerate by 1.1 pp, to 3.4%, on the back of tighter financial conditions and subdued wage growth.
- In the new EU candidate countries of Moldova and Ukraine, growth will slow by 2 pp on average, to 2.7%. This is entirely due to the slowdown in Ukraine, where last year's partial recovery from the huge war-related slump in the economy in 2022 will lose steam on the back of the less favourable basis effect. In Moldova, by contrast, growth is set to accelerate sharply from last year's near-stagnation.
- In CIS3, growth will slow by 0.5 pp, to 3.3% on average. This is mainly due to the expected moderate cooling in Russia over the remainder of the year, with tight monetary conditions and rising labour shortages increasingly coming to the fore.

**In 2025-2026, economic expansion in CESEE as a whole is projected to pick up pace marginally**, with the acceleration of growth in EU-CEE and Turkey being almost totally offset by the slowdown in CIS3 (Overview Table 1). The risks to this forecast are mainly on the downside and are related, above all, to the possible victory of Mr Trump in the US presidential elections in November 2024. First, the possibility of a US 'trade war' with China and potentially with the EU under Mr Trump's presidency would have a severe impact on CESEE countries. Most of them are small, open economies, which – via extensive trade links with Germany – are ultimately heavily dependent on Chinese demand. Second, under Mr Trump the US security commitment to NATO and to Europe in general may not be as certain as it has been for most of the last 80 years. This may, in turn, have some adverse economic and

[9] Here and below: on a weighted average basis.

[10] https://www.eeas.europa.eu/delegations/moldova/security-and-defence-partnership_en?s=223

confidence implications in, for example, the Baltic states. Finally, the possibility of the far-right Rassemblement National (RN) leading the next French government following the snap elections also creates uncertainty, including for many CESEE countries, although the economic impact of such a scenario is far from clear at the time of writing.

## 2.7 REFERENCES

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# 3. Country updates

## ALBANIA: SOLID ECONOMIC GROWTH

***by Isilda Mara***

The economy is expected to grow at 3.6% in 2024, driven by robust domestic and external demand. Domestic demand is benefiting from strong household consumption, government spending and investment. Consumer confidence has been improving, thanks to rising wages and falling inflation in the first half of the year. Public-sector wages are set to rise by 14% in June 2024, with the private sector expected to follow suit. This is driven by the ongoing tourist boom and a tighter labour market resulting from a high rate of emigration. The rate of increase in consumer prices has slowed in the first half of this year, averaging 2.8% annually for January to April 2024; that said, the rising wages are likely to generate inflationary pressures in the second half of the year, preventing inflation from falling below 3% in 2024. Robust external demand means that the domestic currency is appreciating against the euro. This appreciation is causing negative spillovers for export-oriented companies and is leading to layoffs. Although goods exports have accelerated in real terms, nominal exports have contracted significantly. Meanwhile, imports remain on a positive trajectory, which could lead to a deterioration in the current account. On the positive side, particularly in the medium term, we anticipate a surge in public and private investment – not least owing to rising FDI inflows – which will propel economic growth to 3.8% in 2025-2026.

## BELARUS: RECOVERY CONTINUES, DEFYING EXPECTATIONS

***by Rumen Dobrinsky***

Recent short-term indicators suggest that after slowing down towards the end of 2023, economic performance in Belarus strengthened at the beginning of 2024: in Q1, GDP grew by 4.1% year on year and industrial output surged by 6.5%. The available monthly statistics for April suggest a further invigoration of economic activity. Moreover, all indicators point to a broad-based recovery that is also to be observed in agriculture, construction and the services sectors – including, for the first time since 2022, the ICT sector. Because of the very tight labour market and the reported labour shortages in many industries, real wages and disposable incomes have kept on rising. Consumer prices have also been increasing, reversing the prevailing trend of 2023. The embargo imposed back in 2022 on the publication of certain important statistics (especially regarding the composition and direction of foreign trade) precludes any more detailed assessment of the drivers of the current upswing but most likely, local manufacturers and exporters benefited from the strong upturn in Russia at the start of 2024. In addition, domestic policies remained accommodative and various forms of additional support from Russia were still in place. Taking account of these recent developments, we have revised upwards our forecast for GDP growth in 2024 – to 3.5% (up 1.5 percentage points from spring). The forecasts for 2025 and 2026 remain unchanged, reflecting the long-term structural challenges faced by the Belarusian economy.

## BOSNIA AND HERZEGOVINA: INFLATION SLOWING, BUT ECONOMY REMAINS WEAK

***by Selena Duraković***

Inflation remained stable at 2% in Q1 2024, with no new inflationary pressures on the horizon. We are therefore reducing our inflation forecast for 2024 by 0.4 percentage points, to 2.4%. Economic activity is presenting mixed signals: industrial production and the export of goods declined in the first three months of 2024 compared to the same period last year, while imports rose. On a positive note, retail sales increased in Q1 2024, as did tourist overnight stays. Credit activity grew slowly in the first quarter of the year despite rising interest rates, and we expect private consumption to increase on the back of higher real wages. Considering all this, we are maintaining our GDP growth forecast for 2024 at 2.5%. On the political front, the resolution on the Srebrenica genocide that was adopted by United Nations General Assembly in May has heightened tensions both within the country and with Serbia over the past two months. This could further destabilise the country, hindering its economic development and delaying its efforts to join the European Union.

## BULGARIA: ECONOMY LACKS DIRECTION AMIDST A MESSY POLITICAL SITUATION

***by Rumen Dobrinsky***

The snap parliamentary elections held at the same time as the European vote did not result in any major change on the political scene: the GERB party came first in the vote but far from a majority to rule on its own. Consequently, the political impasse is likely to linger on. Economic performance remained sluggish in the first quarter, with GDP growing by 1.9% year on year – a pace similar to that recorded in the previous three quarters. The prolonged recession in manufacturing continued, with gross output down 6.5% year on year in Q1 2024. This mirrored the situation in the export sector: exports of goods remained in negative territory for a fifth consecutive quarter. The picture on the domestic demand side was quite different, as both private consumption and fixed investment recorded visible growth. Private consumption continued to be driven by rising real disposable income and an ongoing credit boom. The volume of new consumer loans in April was 44% higher than a year earlier, and the volume of new mortgage loans was up 60% year on year. On several occasions, the central bank has signalled that this expansion is unsustainable; however, it does not have effective instruments to hand to cool the surge in credit. One of the implications of this macroeconomic pattern is a widening current account deficit. There are no signs that the economic situation will change significantly in the coming months, and our forecast for GDP growth in 2024 as a whole remains unchanged from spring, at 2.0%.

## CROATIA: OUTLOOK REMAINS POSITIVE

***by Bernd Christoph Ströhm***

Croatia's GDP expanded by 3.9% year on year in Q1 2024. The country's accession to the EU's border-free Schengen Area and the euro area is providing a boost to tourism, with EU-related funds further supporting investment activity. In Q1 2024, Croatia already recorded over 15% more tourist arrivals and overnight stays than in the same period last year. We are thus upgrading our GDP growth for 2024 to 3%. Thanks to softer pressures from energy and commodity prices, inflation will continue to decline gradually; but upward pressure from rising wages will mean it remains above the euro area target, averaging 3.7% in 2024. We expect nominal and real gross wages in Croatia to continue to grow in 2024, albeit more slowly than in 2023. The public-sector unions signed a collective-bargaining agreement in March 2024, which will also result in pay increases for public employees. The lack of skilled workers remains an issue for the economy and an obstacle to higher GDP growth over the medium term. On a political note: the ruling Croatian Democratic Union (HDZ) party, led by Prime Minister Plenković, won the parliamentary election in April 2024 and has managed to form a new governing coalition with the right-wing Homeland Movement (DP). This will ensure that there are no major changes in terms of economic policies in the forthcoming period.

## CZECHIA: ON TRACK FOR MODERATE RECOVERY

***by Zuzana Zavarská***

The Czech economy grew by 0.2% year on year in Q1 2024[1], with household consumption and external demand contributing most significantly. Real wages finally grew for the first time since Q3 2021, providing a much-needed boost to consumer spending for the period ahead. The recovering purchasing power is visible in the dynamic growth of retail sales (5.3% year on year in April), along with improvements in consumer confidence indicators. While inflation fell sharply in the first months of the year and remains reasonably low, the Harmonised Index of Consumer Prices (HICP) again jumped in April, pointing to a likely moderation of disinflationary trends in the future. At the same time, due to the ripple effect of the struggling German economy, Czech industrial production remains stagnant, with no sign of any major improvement on the horizon. Nonetheless, trade in goods has been buoyant, with the growth of exports outpacing that of imports. The strong export performance, especially in motor vehicles, is likely a lagged reflection of last year's robust industrial production in the sector; but given the current slowdown in production, a partial loss of this momentum is to be expected. All in all, recent developments mostly confirm our previous expectations from the spring forecast – the Czech economy is on track for modest growth this year (1.2%), supported primarily by private consumption; this will be followed by a more extensive revival in subsequent years. On the monetary side, persistent pro-inflationary pressures justify an upward revision of the HICP for 2024 (2.4%; +0.4 percentage points), and a somewhat more conservative progression of the monetary easing cycle by the Czech National Bank, possibly landing at 4.5% at the year-end.

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[1] Adjusted for price, seasonal, and calendar effects.

## ESTONIA: ON THE VERGE OF GROWTH

*by Maryna Tverdostup*

After two years of continuous recession, the Estonian economy is finally perking up. In Q1 2024, the economy experienced a 2.4% decline year on year, yet this was less than in previous quarters. The downturn was still driven by the lengthy slump in the energy and manufacturing sectors. Recent months have been marked by a stabilisation of business sentiment, prices and private consumption, as well as by notable improvements in both foreign and domestic corporate investment. Thus, growth prospects for the second half of the year appear more positive, as demand in the main export markets, including Scandinavia, gradually picks up and the distorting effects of the energy crisis wear off. Thus, we expect the economy to stagnate this year, but then to see a rapid improvement – to 3.2% in 2025 and 3.6% in 2026. Despite a sizeable plunge in energy prices, inflation is forecast to stay at around 3.2% this year, with subsequent declines to 2.8% in 2025 and 2.1% in 2026. The labour market remains resilient, as the upsurge in unemployment during the first quarter was mainly fuelled by an increase in the workforce. Unemployment is expected to reach 7.3% overall in 2024, as companies remain reluctant to hire new workers. However, it will decline steadily in coming years, in response to strengthening demand and expanding production. The budget deficit will remain at above 3% throughout the forecast period, driven by steadily high government spending on defence and a reduction in personal income tax planned for next year.

## HUNGARY: MOUNTING FISCAL PROBLEMS PREVAIL

*by Sándor Richter*

GDP increased by 1.1% in the first quarter of the year. Services performed at above the average growth rate, while industry has witnessed considerable shrinkage for over a year now, explained mainly by the weak performance of its largest sector, the automotive industry. Growth in Q1 2024 was driven by a moderate recovery in private consumption and positive net exports. Gross fixed investments booked a strong decline. Looking ahead, private consumption is expected to continue as the main engine of growth this year. Wages increased by 14.2% in Q1, while inflation amounted to 3.6% in the same period, meaning a substantial increase in real wages. Nevertheless, consumer price inflation is expected to rise slightly over the year. More importantly, the inflation shock of 2023 has obviously continued to affect consumer behaviour, as demonstrated by the modest (2.4%) increase in retail sales in real terms in the first trimester of the year (year on year). Part of the increase in household income has been channelled into various forms of savings – the combined outcome of consumer cautiousness and enticing yields on government securities. A crucial issue is how the expected start of an unavoidable fiscal consolidation after the European Parliament and municipal elections in June will impact private consumption. Even moderate fiscal measures will slow the pace of economic recovery. Lasting conflicts with the EU are not helpful in this respect, either. This year GDP may grow by around 2%, a minimal improvement on our previous forecast. Then 2025 and 2026 could see a somewhat better growth performance. The European Parliament elections in June brought a political earthquake in the shape of a new opposition party. Set up by a disaffected former Orbán loyalist, TISZA – with its trenchant anti-corruption programme and its commitment to restore the rule of law – managed to collect close to a third of the votes, just a few weeks after being established. Stay tuned for further political developments.

## KAZAKHSTAN: OIL PRODUCTION CUTS UNDERMINE ECONOMIC GROWTH

***by Alexandra Bykova***

Economic performance in Q1 2024 was weaker than expected, with real GDP growth of 3.7% year on year, down from 5.5% in Q4 2023. A 0.6% decline in oil production due to OPEC+ production restrictions, as well as weak performance in agriculture and wholesale trade in the first four months, held back overall economic growth. By contrast, construction, communication services, transport and logistics remain key drivers of growth, fuelled by investment. The performance of the manufacturing sector remains robust, driven primarily by the machinery, metallurgy and chemical industries; this is likely to persist, given the prevailing positive sentiment. Consumption should also continue to pick up, thanks to the minimum wage hike in January, strong consumer lending and the gradual return of the monthly inflation rate to its long-term average. From the monetary policy side, the latest policy rate cut of 25 basis points (to 14.5%) is in line with the course of easing. In view of the pro-inflationary risks – such as loose fiscal policy, rising global food prices and higher utility tariffs – the pace is likely to remain moderate. Given the weak oil sector, characterised by poor four-month results, a slump in investment and the recent extension of OPEC+ oil production restrictions until the end of September 2024, we have revised our 2024 GDP growth forecast downwards by 0.5 percentage points, to 4.2%. We expect the economy to accelerate back to almost 5% in 2025, driven by stronger consumption amid lower inflation and a significant impetus to the country's oil production, once the Tengiz oil field expansion is completed.

## KOSOVO: GOOD GROWTH MOMENTUM

***by Isilda Mara***

In 2024, economic growth will remain consumption led, with investment also contributing positively. A lower rate of increase in consumer prices, rising remittances and higher public-sector wages will sustain consumption. Consumer price inflation declined to 2.2% in the first four months of 2024, but headline inflation – and especially energy price inflation – was still elevated, standing at three times the rate for the same period last year. Given the heavy dependence of the Kosovo economy on imports, we expect inflation to hover at around 2.9% for the year. Remittances will continue to play a vital role for households, bolstering consumption. Public finances have improved steadily, allowing the government to further support reforms in public-sector wages and to increase public investment. Military spending has increased substantially, but this will not affect improvements in the public finances. Despite external turbulence, the economy and foreign direct investment have demonstrated resilience. The banking sector remains supportive, with demand for credit rising and non-performing loans remaining low. In Q1 2024, goods exports lost momentum, while services exports picked up. However, the strong showing by service exports will not prevent the current account from deteriorating, on account of the continued surge in imports. Anticipating strong domestic demand, we expect a growth rate of 3.6% in 2024. Over the medium term, growth momentum is projected to hover at around 3.9%.

## LATVIA: UPSWING APPROACHING, BUT ONLY SLOWLY

***by Sebastian Leitner***

A contraction in external demand and investment resulted in GDP stagnating in Q1 2024. Looking ahead over the year as a whole, the economy will recover, though by just 1.6%. The main growth driver will be planned investment, financed from the NextGenerationEU programme; meanwhile exports will revive only gradually, since EU – and particularly German – industrial activity will remain subdued. Consumer price inflation is about to decline further and will be 1.5% on average this year, while a gradual rise is to be expected in the coming years. Real incomes are increasing quite swiftly again; thus, we will see private household demand revive somewhat more rapidly in the second half of 2024. Given the fairly low growth, the public deficit will amount to 3% of GDP this year. The labour market remained quite tight last year; the unemployment rate is expected to increase slightly to 7% in 2024 and thereafter to decline again. In the coming years, growth is projected to pick up to 2.5% in 2025 and 2.7% in 2026.

## LITHUANIA: HOUSEHOLD CONSUMPTION PUTS AN END TO STAGNATION

***by Sebastian Leitner***

In Q1 2024, the Lithuanian economy returned to growth mode, increasing by 2.9% in real terms year on year. Household consumption resumed its position as the strongest driver of growth, and further signs of an upswing came in the form of the retail trade data for April 2024. As expected, external demand from Lithuania's main trading partners continues to stagnate, leading enterprises to deplete their stocks and resulting in a sharp decline in gross capital formation. Despite that, gross fixed capital formation is growing, driven mainly by public investment. In May 2024, consumer price inflation was down to 0.8%, but for the year as a whole it is likely to be somewhat above that level (1.5%) due to wages, which are continuing to rise swiftly. Following a budget deficit of only 0.8% of GDP in 2023, we are likely to see an increase to 2.5% this year, largely on account of the hike in defence spending to 3% of GDP. Although GDP stagnated in 2023, the unemployment rate increased only slightly last year; this year, too, it is likely to rise to only 7.2%. We expect real GDP to grow again by 1.7% in 2024, followed by an upswing of 2.2% in 2025 and 2.6% in 2026.

## MOLDOVA: SLOW RECOVERY DESPITE SUBDUED INFLATION

***by Gábor Hunya***

The economy emerged from recession in mid-2023, but has not yet achieved sustained take-off. Early 2024 data indicate sluggish growth, based on a modest recovery in household consumption on the back of robust real wage growth (10% in Q1 year on year). However, manufacturing production, investments and the performance of the construction sector were all below the level of Q1 2023. Agricultural production has recovered and could have a positive effect on growth, assuming a good harvest. Exports and imports both contracted in nominal terms, mainly the effect of lower prices. Dependence on the supply of gas from Russia could be replaced by imports from the EU. Due to the low energy prices and still subdued consumption, inflation fell to below the 5% target of the National Bank of Moldova, hovering in the range 3.5-4% in March through May. The base rate was relaxed to 3.6% at the same time, but with a fairly wide ±2 percentage point deposit/credit corridor. Further rate cuts will be constrained by the acceleration of inflation, as consumption recovers. Narrowing the corridor or cutting the deposit requirements could result in some monetary easing to support investment, however. Fiscal and current account deficits are high, but the necessary financing is being provided by international donors and creditors – mainly the International Monetary Fund and the EU. Support is underpinned by the political efforts on the part of Moldova to commence accession negotiations with the EU. Challenges come not only from the domestic anti-EU forces, but also from Russian subversion. In May this year, the EU signed a comprehensive security and defence partnership with Moldova to help combat security challenges. As the situation appears now, the pro-EU forces will win the referendum on EU membership to be held in October. But a favourable outcome to the simultaneous presidential election is less certain. This poses a downside risk to the current forecast, which sees economic growth accelerating from 3% this year to 4% in 2026.

## MONTENEGRO: SOME QUESTION MARKS, BUT OVERALL POSITIVE

***by Branimir Jovanović***

The economy is continuing to grow robustly, with GDP expanding by 4.4% year on year in Q1. The main driver of growth was investment, with inflows of foreign direct investment remaining strong, at 10% of GDP in Q1. Nearly half of those inflows went into real estate, and about a third originated in Serbia or Russia. The labour market continues to improve, with registered employment increasing and registered unemployment declining. Real wages, which have seen robust growth over the past two years, have plateaued, with growth at the beginning of 2024 close to zero. Meanwhile, inflation has recently accelerated, reaching 5.4% in April. Both these developments may herald a slowdown in consumption in the coming period. The fiscal situation remains stable, with the budget in surplus for the first four months of the year. Nonetheless, significant uncertainties arise from the government's Europe Now 2 package, which aims to increase pensions and salaries, while reducing certain taxes. Details of the reform – including its implementation timeline and the specific measures involved – are still under wraps. A good tourist season in 2024 will be crucial for the economy, and early booking figures suggest that it will indeed be better than last year. Consequently, we are maintaining our forecasts for GDP growth and inflation in 2024 at 4.2% and 4.5%, respectively.

## NORTH MACEDONIA: CHANGE, BUT POSSIBLY NOT IN THE RIGHT DIRECTION

***by Branimir Jovanović***

Economic growth in the first quarter was weaker than anticipated. Despite robust fiscal support ahead of the elections and an increase in real wages, GDP grew by only 1.2% year on year. While there were improvements in household consumption, government consumption and gross investment, the overall economic performance was dragged down by a significant decline in exports, which was linked to a sharp drop in agricultural production. Inflation accelerated to 4.5% in May, following the government's removal of price controls. Consequently – and contrary to our previous expectations – the central bank decided not to cut its interest rate in June, thus placing additional pressure on the economy. For all these reasons, we have revised our GDP forecast for 2024 down to 2% (-0.2 percentage points). Despite a decisive victory in the May elections, the new ruling party, VMRO-DPMNE, has been slow to form a government – possibly in order to avoid taking difficult decisions immediately. It is clear that the government coalition will enjoy a comfortable parliamentary majority; and while there are high hopes of change, no significant alteration in economic policies is to be expected, since the two major parties in the country adhere to similar economic ideologies. Optimism is being further dampened by the new ruling majority's first move: a reorganisation of ministries that will see their number rise from 16 to 20. The new leadership of the country is also making waves internationally: both the newly elected president and the incoming prime minister have repeatedly refused to use the country's constitutional name, sparking criticism from Greece and EU officials.

## POLAND: STRONG CURRENCY, LOW INFLATION

***by Adam Żurawski***

GDP rose by 2% year on year in Q1 2024, driven by strong consumption. External balances remain positive. Rising real wages and investment will speed up growth in the coming quarters. Investment will be positively affected by rising public spending, also on account of higher transfers from the EU sources. Inflation is low (2.4% in April) but the wage dynamics and price effects of the coming energy market's deregulation will push it up in the second half of 2024. Most probably the official interest rate (5.75%) will not change in 2024 and the PLN will remain strong. We stick by our previous forecast for inflation in 2024 and raise the forecast for GDP growth to 3.3%, from 3.1% in spring.

## ROMANIA: GROWING FISCAL TENSION

*by Gábor Hunya*

Economic growth will be faster in 2024 than in the previous year, despite a modest start. In spite of recovering household consumption and a rapid expansion in public consumption, GDP was up by only 1.6% in Q1, due to subdued investments and exports. Manufacturing production also declined in Q1, hit by reduced demand on Romania's main export markets. Economic growth is set to accelerate in Q2 and beyond, as indicated by improving sentiment on the part of managers and an increase in new orders in manufacturing. Household demand will expand further as wages and pensions increase significantly faster than prices: in such circumstances, Romanians have a habit of spending rather than saving. Inflation was stubborn in Q1, due to a change in regulated prices, but it has moderated more recently. Disinflation will continue (albeit slowly) for the rest of the year, with some possibility of more rapid movement in the event of a bumper harvest. Labour shortages are again on the up, as indicated by the declining unemployment rate and increasing vacancies. The twin deficits of the general budget and the current account will barely shrink at all this year. Foreign financing is available, albeit at a higher cost than in other EU-CEE countries (due to Romania's relatively poor, though stable, credit ratings). A real positive central bank base rate and a roughly constant exchange rate will stimulate the appetite of financial investors. Fiscal adjustments have been mild up to now, while deficits are growing faster than planned by the government. Stabilisation measures can only be expected after the parliamentary and presidential elections scheduled for later 2024. Monetary policy will continue to somewhat offset the loose fiscal policy by keeping the base rate above inflation. We have revised our 2025 growth forecast down from 3.3% to 3.1% in the expectation of stricter fiscal austerity than was earlier assumed. Household consumption will decelerate, while investment may pick up and the external balance may improve.

## RUSSIA: ECONOMY RESILIENT TO TIGHT MONETARY CONDITIONS

*by Vasily Astrov*

In Q1 2024, real GDP grew by 5.4% year on year, following 4.9% in Q4 2023. The high growth rate in Q1 should partly be viewed against the low basis from Q1 2023, when the economy declined by 1.6%, which means that growth will probably slow somewhat in annual terms as the year progresses. Nevertheless, the underlying growth momentum remains strong, prompting us to raise our growth forecast for 2024 once again – to 3.2% (from 2.8% in spring). Since December 2023, the policy interest rate has been kept at a very high 16%; but this has still not been enough to cool the economy, which remains clearly overheated. Inflation has been hovering at around 8% in annual terms, driven primarily by ongoing high real wage growth amidst further labour-market tightening: in April, the unemployment rate (LFS) dropped to another all-time low of 2.6%. On the external front, increased US pressure on banks from third countries (such as China, Turkey and the UAE) to discourage them from receiving payments from Russia has resulted in a marked decline in imports from these countries. For instance, merchandise imports from China – which accounts for nearly half of total Russian imports – fell sharply in both March and April (year on year), with dual-use products hit particularly hard. Although alternative payment channels will likely be found eventually, these will entail extra costs, which will serve to fuel inflation still further. In 2025-2026, growth is projected to slow to around 2.5%, with tight monetary conditions and further rising labour shortages ultimately weighing on economic dynamics.

## SERBIA: ECONOMY GROWING, BUT CHALLENGES REMAIN

***by Branimir Jovanović***

The overall economic situation in the country is continuing to improve, with GDP growth of 4.7% year on year in Q1. All sectors and GDP components experienced gains, but the primary drivers were robust household consumption (driven by real wage growth) and strong investment, supported by significant FDI inflows and ambitious public investment ahead of the upcoming EXPO 2027. On the downside, inflation remains rather high, at 4.5% in May; that said, it has been on a clear downward trend for over a year and does not appear to be visibly constraining the performance of the economy. As inflation fell on the upper bound of the inflationary target (3%±1.5%), the central bank cut its base interest rate to 6.25% in June, and we expect it to come down to 5.5% by the end of the year. On the political front, the ruling SNS party secured a convincing victory in the June local elections, including in the capital city of Belgrade. This will reinforce its hold on power and ensure that the status quo in the country remains largely unchanged. This includes numerous structural issues related to the rule of law, control of corruption, freedom of the media and lack of an industrial policy: these are likely to prevent the economy from achieving high growth rates over an extended period. Thus, we are revising upwards our GDP forecasts for this year and the next two – but only slightly, to 3.5%, 3.6% and 3.7%.

## SLOVAKIA: MOUNTING POLITICAL RISKS

***by Doris Hanzl-Weiss***

After a figure of 1.6% in 2023, in Q1 2024 Slovakia experienced unexpectedly rapid GDP growth of 2.7% year on year, making it one of the fastest-growing countries in the EU. This robust performance was driven by domestic demand. Household consumption recovered from last year's high inflation, bolstered by a 5.6% rise in real wages in Q1, as inflation subsided to 2.4% in April 2024. Government consumption and investment also expanded. On the other hand, net exports dragged growth down, with imports of goods and services rising faster than exports in real terms. The labour market is in reasonable shape: employment continued to increase in Q1, while unemployment dropped to a historically low level. The labour shortages have led to more visas being offered to attract foreign workers. However, industry in general – and the automotive industry in particular – were not doing well at the beginning of the year. Production had dropped markedly and new orders were significantly down. Nevertheless, the forecast for this year has been revised slightly upward, given the unexpectedly positive developments observed in Q1. We now expect growth to reach 2% in 2024, 2.2% in 2025 and 2.6% in 2026. This improvement will be driven by increased household confidence, growing income and a strong labour market, all of which will boost household demand. However, poor growth in external markets – particularly in Slovakia's main export markets of Germany and Czechia – will hamper a stronger performance. In addition, growth prospects are being overshadowed by domestic political changes and a harsher political climate following the attempted assassination of Prime Minister Robert Fico. The budget deficit is expected to be very high this year, and will decline only slowly in the coming years, thus postponing fiscal consolidation.

## SLOVENIA: SOLID GROWTH EXPECTED IN YEAR OF INFRASTRUCTURE REBUILDING AND DISINFLATION

***by Niko Korpar***

In 2024, Slovenia's GDP is expected to grow by 2.4% – well above the EU average. Growth will be driven by government spending (primarily on rebuilding infrastructure after last year's severe floods), as well as by private consumption and investment, which will benefit from receding inflation. Exports will improve somewhat from 2023 and will see a current account surplus of 3% of GDP, despite imports growing more than exports. In April, annual inflation stood at 3% – lower than expected – and we have downgraded our forecast for the whole year from 3.3% to 2.7%, in anticipation of further disinflation as the year progresses. The labour market remains tight, and unemployment will continue to hover at around 3.6% in 2024 and beyond. The government has introduced limited tax reform, offering tax breaks for the employment of skilled workers from abroad and encouraging equity-based corporate incentives. A (non-binding) public referendum on expanding the nuclear power plant is planned for the second half of the year, as the country deliberates on one of the most far-reaching issues for several decades. Despite losing ground to the right-wing opposition in the 2024 European elections, the government of Dr Robert Golob is secure, and most political parties are in agreement as regards the nuclear expansion project.

## TURKEY: DESPITE MARKET CONFIDENCE, THE DATA PAINT AN UNCERTAIN OUTLOOK

***by Meryem Gökten***

As expected, GDP growth in Q1 2024 was strong, but high-frequency economic indicators suggest a modest deceleration in domestic demand from Q2 2024. Household consumption grew sluggishly in Q1 compared to the previous quarter, with growth driven primarily by investment, government spending and positive net exports. The tightening of financial conditions and subdued real wage growth are likely to contribute to a further slowdown in domestic demand. In May, annual inflation likely peaked at 75.5%. In response, the central bank maintained the policy rate at 50% for a second consecutive month and introduced further macroprudential measures to control FX loan growth, while increasing reserve ratios for Turkish lira deposits. Despite market optimism about disinflation, substantial structural and institutional challenges remain. Given the current high inflation and interest rates, it is very unlikely that disinflation can be achieved without sacrificing short-term growth. The optimism may be premature, given the historical volatility in President Erdoğan's policy direction and his government's reluctance to shift from growth-oriented policies; this suggests that economic rebalancing will take time and patience. Therefore, the decline in inflation is projected to be more modest than initially anticipated by the central bank, and to have only a limited impact on growth. Our forecast for 2024 remains unchanged: 3.4% growth and 59% average annual inflation.

## UKRAINE: ECONOMY UNDERMINED BY RUSSIA'S MISSILE ATTACK ON THE ENERGY INFRASTRUCTURE

***by Olga Pindyuk***

The economy showed strong growth in Q1 2024 of about 4.5% year on year (according to estimates by the Ministry of Economy), as the functioning Black Sea Corridor supported growth in metallurgy, the extraction industries and transport. Consumer inflation in April 2024 slowed more rapidly than expected – mainly on the back of falling raw food prices (the result of temporary excess supply). Also, the approval by the US of over USD 60bn in military aid for Ukraine in April provided much-needed funding for military expenditure and, together with loans from the EU under its Ukraine Facility, allowed macro-financial stability to be further maintained. Encouraged by the recent trends in inflation and external funding, in April the central bank cut its policy rate by 1 percentage point (pp) – to 13.5%. However, Russia's recent missile and drone attacks on the energy infrastructure are putting a brake on the economic recovery. About half of the country's power-generation capacity has been destroyed, which has forced energy providers to introduce nationwide rolling power outages that are expected to continue for at least another year. In light of these developments, we have downgraded our GDP forecast for 2024 by 0.5 pp – to 2.7%. In 2025-2026, annual GDP growth will accelerate to about 4%, assuming the country receives sufficient external funding and military aid. The results of the June G7 summit – at which the leaders agreed to provide Ukraine with USD 50bn in new financing, funded by interest earned on frozen Russian sovereign assets – are reassuring. However, the downside risks to the forecast remain high, as the government's need for external funding for the coming years is not yet fully covered, and Ukraine's military continues to experience a shortage of weapons, ammunition and anti-missile defence systems – all critical to defending the country from further destruction by Russia.

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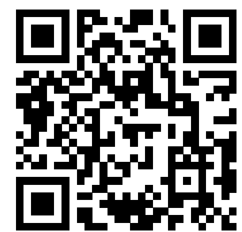

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