

The Impact of the Crisis on the „Real Economy”

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Topics and sources

Macro-Economic Performance

Foreign Direct Investment

Export

Rebound of the global growth, and hence of the external (Euro-zone) demand for SEE goods and services, happens sooner than expected. The last few years must be seen in a perspective.

The sources used are the forecasts of *UniCreditGroup, Citigroup, IMF, EBRD, WIIW.*

EU Members and Croatia

Country/indicators	2007	2008	2009e	2010f	2011f
BULGARIA					
GDP/Growth (%)	6,2	6	-6,3	-2,4	2
Inflation (yoy, %)	8,4	12,4	2,6	-0,6	1,5
FDI/GDP (%)	28,7	16,7	8,3	6,5	6,5
Budget balance/GDP (%)	3,5	3	0,3	-1,8	-1,8
Unemployment	6,9	6,3	9,5	12,9	13,5
CA Blance/GDP (%)	-25,1	-25,3	-12,4	-9,1	-6,9
ROMANIA					
GDP/Growth (%)	6,2	7,1	-7,5	0,4	3,5
Inflation (yoy, %)	4,3	7,9	5,7	3,9	3,8
FDI/GDP (%)	5,8	6,6	3,9	3,9	4
Budget balance/GDP (%)	-2,3	-4,8	-7,3	-6	-5
Unemployment	4,3	4,0	7	7,6	7
CA Blance/GDP (%)	-13,5	-12,3	-6	-6,3	-6,7
CROATIA					
GDP/Growth (%)	5,5	2,4	-6,2	-1,5	1,2
Inflation (yoy, %)	2,9	6,1	3	3,3	3,1
FDI/GDP (%)	8,1	6,8	3,3	3,7	4,2
Budget balance/GDP (%)	-2,0	-0,8	-3,9	-3,5	-3
Unemployment	9,6	8,4	10	11	9,8
CA Blance/GDP (%)	-7,6	-9,3	-4,5	-3,6	-2,8

Source: UniCredit

Other SEE: Bosnia and Herzegovina and Serbia

Country/indicators	2007	2008	2009e	2010f	2011f
BiH					
GDP/Growth (%)	6,8	5,4	-3	-1	0,8
Inflation (yoy, %)	1,5	7,4	0,2	2,6	2,2
FDI/GDP (%)	13,8	5,5	1,7	3,3	4
Budget balance/GDP (%)	3,5	3	0,3	-1,8	-1,8
Unemployment	44	40,3	42	44,0	43,5
CA Blance/GDP (%)	-10,4	-14,9	-8,3	7,0	-7,5
SERBIA					
GDP/Growth (%)	7,1	5,4	-4,8	-0,7	1,3
Inflation (yoy, %)	6,5	11,7	8,6	7,0	6,1
FDI/GDP (%)	6,2	5,4	3,5	3,7	4,3
Budget balance/GDP (%)	-1,5	-2,0	-4,5	-4	-3,5
Unemployment	18,1	18,0	18,5	19	18,2
CA Blance/GDP (%)	15,6	13,9	-7,5	-6,2	-7,2
<i>Source: UniCredit</i>					

Other SEE: Albania, Macedonia and Montenegro

Country/indicators	2007	2008	2009e	2010f	2011f
ALBANIA					
GDP/Growth (%)	6,2	6,7	0,7	2,2	6,3
Inflation (yoy, %)	2,9	3,3	1,6	2,0	2,8
FDI/GDP (%)	6,6	6,0	n.a.	n.a.	n.a.
Budget balance/GDP (%)	3,8	5,9	6,1	n.a.	n.a.
Unemployment	13,5	12,8	13,0	12,0	11,0
CA Blance/GDP (%)	-9,1	-14,0	-11,5	7,9	6,9
MACEDONIA					
GDP/Growth (%)	5,9	4,9	-2,5	2,0	5,0
Inflation (yoy, %)	2,3	8,3	-0,5	2,0	3,0
FDI/GDP (%)	8,8	6,4	n.a.	n.a.	n.a.
Budget balance/GDP (%)	0,6	-1,0	-2,8	n.a.	n.a.
Unemployment	34,9	33,8	34,0	33,0	33,0
CA Blance/GDP (%)	-7,2	-13,1	-10,6	-9,7	-8,1
MONTENEGRO					
GDP/Growth (%)	10,7	7,5	-4,0	-2,0	3,7
Inflation (yoy, %)	3,5	9,0	3,4	2,1	2,6
FDI/GDP (%)	18,7	16,7	n.a.	n.a.	n.a.
Budget balance/GDP (%)	6,4	1,5	-3,0	n.a.	n.a.
Unemployment	16,8	17,5	n.a.	n.a.	n.a.
CA Blance/GDP (%)	-29,4	-29,6	-16,0	-11,0	-9,0

Sources: WEO, EBRD, WIIW

Legend: Production factors, Demand characteristics, Industry, strategy, rivalry, Clustering characteristics, Government policies/regulations

Recent Winners

Clothing, footwear	Tourism	Telecoms	Trade
<p>Skilled labor at low cost</p> <p>Improving domestic demand</p> <p>Close to EU markets</p> <p>China threat relatively small</p> <p>International integration</p> <p><i>Fragmented</i></p>	<p>Nature and history</p> <p>Skilled labor at low cost</p> <p>EU customer penetration</p> <p>Large investments</p> <p>Improving industry strategy</p> <p><i>Fragmented</i></p>	<p>High profits</p> <p>Very strong demand growth</p> <p>High investments</p> <p>IT clustering</p> <p>Sound regulation on paper</p> <p>But little competition</p>	<p>Improving networks, infrastructure</p> <p>Better leasing, payment mechanisms</p> <p>Rising real incomes</p> <p>Significant investments</p> <p>Improved management, turnover speed</p> <p><i>Retail sector remained protected in some countries</i></p>

Recent Winners

Machines, equipment	Food, beverages, tobacco	Financial
<p>Skilled labor at low cost</p> <p>Technology transfers</p> <p>Improving infrastructure</p> <p>Rising demand</p> <p>Ability to find markets</p> <p><i>Fragmented, global integration worked both ways</i></p>	<p>Good supply base</p> <p>Expertise, experience</p> <p>Growing demand</p> <p>Competitive pricing at better quality</p> <p>Investments coming/expected</p> <p><i>Somewhat integrated with global leaders in tobacco but well integrated in beer, soft drinks, confectionary</i></p>	<p>Rising demand</p> <p>Very high growth, good indicators</p> <p>High productivity</p> <p>Ownership</p> <p>Sound regulation</p>

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Legend: **Production factors**, Demand characteristics, **Industry**, strategy, rivalry,
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Prospective Winners

Transport	Energy (generation and transit)	Pharma	Chemicals	Infra structure
<p>Experience</p> <p>Infrastructure to improve</p> <p>EU – Turkey</p> <p>PPP (concessions)</p> <p>Regulations to improve</p> <p><i>Operators of transport concessions emerge</i></p>	<p>Skills and experience missing</p> <p>Regional positions under-utilized</p> <p>Privatization</p> <p>High recent, expected investment</p> <p>Regulatory framework</p> <p><i>FDI's in pipeline</i></p>	<p>Skilled low cost labor</p> <p>Access to regional / CIS markets</p> <p>Private ownership</p> <p>High investments</p> <p>International clustering</p> <p><i>In some countries remained untouched by the crisis</i></p>	<p>Good material, resource base</p> <p>Good international demand</p> <p>Sectors completing restructuring</p> <p>Strategic owners</p> <p>Investments, new technologies</p> <p><i>Stretched b/n Russia energy supply and EU demand</i></p>	<p>EU money</p> <p>Basic grids in place</p> <p>High demand (high time)</p> <p>PPP</p> <p>Regulations in place</p> <p><i>Utilities, remained to be better integrated</i></p>

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Expected Losers

Agro	Auto	Ferrous Metals	Health/Pension
<p>No land market yet</p> <p>Highly fragmented property</p> <p>Undercapitalised</p> <p>Low cost competition in region</p> <p>EU subsidy absorption still low and difficult to compete with</p>	<p>No tradition or skills</p> <p>Negligible internal market</p> <p>Several failed attempts</p> <p>Romania, Serbia, Turkey</p> <p>No domestic clusters</p>	<p>Inherited unproductive assets</p> <p>Old technology</p> <p>Poor financials</p> <p>Long term restructuring needed</p> <p>EU competition to cut margins</p>	<p>Unfavorable contellation</p> <p>State ownership</p> <p>Falling quality of service</p> <p>Inadequate regulations / incentives</p> <p>Vested anti-reform interests</p>

Sectoral Impacts (1)

Housing: in Bulgaria – prices went 24% down; in Bosnia and Herzegovina – 30%; construction contracted everywhere by 10-15%. However, unlike US and some other countries, policies were sound.

Banks faced challenges related to reduce external borrowing and refrained from lending but remain liquid – in different countries for different reasons.

Falling imports indicate weakness of a) private consumption; b) FDI's and c) exports – scaled-down consumer credit and remittances contributed to the picture.

Exports of raw materials and manufacturing have contracted sharply in response to weaker external demand in all countries.

Sectoral Impacts (2)

Countries that in the past followed sort of industrial policy, e.g. Romania, were hit hardest but manufacturing declined across the region.

Price levels and labor costs remain a comparative advantage but lost markets cause downsizing and closures.

Sectors that remained untouched are relatively few: medium-to-long term investment projects in utilities and infrastructure; such projects explain relatively positive outlook for Albania (plus other factors) and seem to prevent sharper GDP slowdown in Romania and Bulgaria.

Deterioration/Improvement of political climate

Deterioration

Bosnia and Herzegovina
Romania

Improvement

Albania
Bulgaria
Croatia



discipline, pro-liberalization, competition based spending

Neutral

Serbia
Montenegro
Macedonia



Conclusions (1)

The actual slowdown resembles **use of brakes amidst high speed driving**, GDP performance turned from average 4-5% in 2008 to -5% in 2009.

These developments had little to do with domestic economic policies, but exacerbated existing deficiencies.

For most countries **challenges** are no longer with the external imbalances: they **moved to area of fiscal balances**.

IMF (and EU) supported programs are in *status nascendi*, subject to uncertainties.

Tax reform growth (and revenue) triggers have been used, exhausted: **new sources of savings and investment are needed (perhaps linked to pensions, healthcare and education)**.

Conclusions (2)

The consensus forecast of 1.2-1.5 **2010 growth in CEE (including Russia and Turkey) is not quite applicable for SEE**, but could serve as positive factor, if intra-regional investment rebounds.

For most SEE countries cutting government expenditures (and administration – in Bulgaria and Romania, esp.), job losses, falling housing prices and anemic credit growth will keep GDP growth negative in 2010.

Domestic demand will remain weak over mid-term, consumption is being hampered by accelerating unemployment, and frozen wages and government expenditures. (None of SEE countries is a an example of good public governance; relying on public sectors, projects to compensate for the decline is not a good option.)

Time is needed to reallocate resources from previously overheated domestic-demand-oriented sectors to higher-value-added export driven activities, to resume lending and stabilize housing market.

Conclusions (3)

Issues of privatization are still on the agenda, both as unfinished business and a room to maneuver, given fiscal challenges and decline in FDIs. (Croatia and Montenegro ports and shipyards; BiH communications)

Another room to maneuver is quasi-taxes, the so called business environment and the rule of law. (Hitrorez in Croatia, business registration in RS)

EU is costly but accession brings in capital and increases individual freedom; current programs make little economic sense; ideally, EU may promote via its programs market reforms and prosperity but the incumbent designs do not fit this goal.

Lastly, I think there is **no new growth “model”, and there is no need for such**: reforms that would boost saving require time are difficult amidst fiscal challenges and low employment rates; infrastructure investment is no immediate remedy.