NBP

National Bank of Poland

Economic Institute
Bureau of World Economy and European Economic Integration

Analysis of economic situation in the countries of Central and Eastern Europe

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This report has been prepared for information purposes on the basis of various research sources independent from the National Bank of Poland.

EXECUTIVE SUMMARY

The deepening recession in the old EU countries (EU-15) and intensifying financial crisis strongly affected a decline in economic activity in the countries of Central and Eastern Europe. In Q4 2008 the GDP in nine CEE countries considered collectively dropped by 0.3% y/y. The dynamics of recession processes in the region was thus much more pronounced than in the countries of Western Europe. Preliminary estimates of GDP changes in Q1 2009 point to a further fast proceeding slowdown in the CEE economies.

The intensification and spreading of recession in the global economy resulted in a significant decline in exports in Q4 2008 which earlier had a strong pro-growth impact on the economies of the region. A drop in external demand increased the reduction of the exports sector's output, which in consequence contributed to the decline in employment in the manufacturing sector and the drop in a relatively high wage growth. In combination with a strong reduction of lending, it resulted in contracted household consumption. The reduced activity in the manufacturing sector contributed to the decrease in fixed capital formation. The economic growth rate varied widely among the countries of the region (definitely more than in the EU-15). As many as five countries of the region recorded a decline in the annual gross domestic product. In four countries affected by the global crisis in the period when they struggled with internal economic crisis, the GDP decline q/q happened for at least second consecutive time. It means that the economies of the Baltic states and Hungary are at the stage of technical recession.

The decline in economic growth in other CEE countries considered collectively was stronger than in Poland in Q4 2008, as a result of a relatively large drop in consumption expenditure in the region. Such diversified tendencies stemmed from a higher impact of the exports sector on the changes in domestic demand in the remaining CEE countries (i.e. greater openness of the CEE economies as compared to Poland) and a slightly larger role of loans.

Recession intensified in the region at the beginning of 2009, due to the further strong decline in external demand. This is evidenced both by strong decreases in retail sales and industrial output (in particular in the strongly export-oriented sectors), and by deteriorating consumer and business sentiment (often to the historically lowest levels).

The worsening economic situation in the second half of 2008 led to the deterioration of the situation on the labour market. After several years of decline, the unemployment rate rose significantly in the entire region.

The second half of 2009 was characterised by a marked disinflation trend in all economies of the region. The core inflation in the CEE countries also started to moderate as from Q4 2008. Apart from a direct impact of the decrease in food and energy prices, it was also affected by a decline in consumption demand. In 2009 the downward inflation trend continued in the countries with a fixed exchange rate regime and in the euro area countries. Strong depreciation of national currencies in Poland, Czech Republic, Hungary and Romania led to the growth of inflation in those countries in Q1 2009.

After two consecutive years (2006-2007) of the deepening current account deficit in the CEE countries, the deficit declined from 9.3% in 2007 to 8.9% in 2008. The improvement was primarily attributed to the reduction of the deficit in Q4 2008. In Q4 2008 large outflows of portfolio investments were recorded mainly in the countries with a floating exchange rate regime. In addition, intensifying liquidity crisis and declining foreign trade volume resulted in the reduced inflow of trade loans and loans for the banking sector, which caused the decreased inflow of other investments (particularly in the Baltic states). This trend continued in Q1 2009, but on a significantly smaller scale.

The situation of public finances deteriorated in the majority of countries of Central and Eastern Europe in 2008 (except for Bulgaria and Hungary). Fiscal prospects for 2009 in many cases point to a further increase in public finance imbalance in the countries of the region. The risk for financial prospects is high due to the uncertain economic environment and the impact of global crisis and introduction of fiscal stimuli packages.

The deepening recession in Western Europe and the consequences of the financial crisis resulted in a significant lowering of economic growth forecasts for Central and Eastern Europe in recent months. In addition, the correction was stronger than for forecasts for the EU-15 (due to a greater importance of external demand). Moreover, the downward trend in GDP may maintain also in 2010. Inflation forecasts for the coming years vary depending on exchange rate regime. Inflation is predicted to decline further in the countries with fixed exchange rate regimes, while the countries with floating exchange rate regimes are to see inflation fluctuating around the currently observed levels in the coming years.

COUNTRIES OF CENTRAL AND EASTERN EUROPE

Economic growth

Deepening recession in the old EU countries (EU-15) and intensifying financial crisis strongly affected the decline in economic activity in the countries of Central and Eastern Europe. In Q4 2008 the GDP in nine CEE countries considered collectively dropped by 0.3% y/y. The dynamics of recession processes in the region was thus much more pronounced than in the countries of Western Europe. Preliminary estimates of GDP changes in Q1 2009 point to a further fast proceeding slowdown in the CEE economies[1].

Such a sudden reaction of the economies of the countries of Central and Eastern Europe was somewhat surprising, in particular in view of the fact that the majority of them did unexpectedly well in the first three quarters of 2008[2] (as evidenced by the upward adjustment of forecasts of international institutions in autumn 2008), while Western Europe recorded a strong decline in economic activity. Despite strong trade, capital and financial links with the EU-15 countries, the economic growth in the region between Q1 and Q3 2009 amounted to 4.7% (as compared to only 1.5% in the EU-15 countries). Exports, mainly within corporations, remained the main determinant of economic growth in the region. The exports grew mainly due to a maintaining relatively high demand in the countries from outside the European Union[3]. The exports increased by 10.8% within that period (i.e. only slightly less than in 2007 when it grew by 12.7%). The exports sector growth rate remaining on a relatively high level was conducive to the growth of both consumption expenditure and fixed capital formation.

Figure 1.1

Contribution to GDP growth (in pp, y/y)

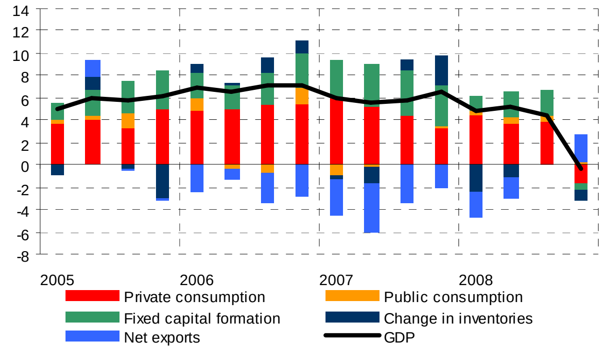


Table 1.1

GDP and its components growth rate (in %, y/y)

	2007	2008	Q2 2008	Q3 2008	Q4 2008
GDP	**5,9**	**3,3**	**4,9**	**4,1**	**-0,3**
Private consumption	7,1	3,4	5,3	5,3	-2,5
Public consumption	-0,8	2,0	2,8	3,3	0,6
Fixed capital formation	12,1	5,1	9,2	7,6	-1,5
Exports	12,7	6,4	12,1	7,1	-6,3
Imports	14,6	5,6	12,0	5,9	-7,8

source: Ecowin Economic

The intensification and spreading of recession in the global economy resulted in a significant decline in exports in Q4 2008 which earlier had a strong pro-growth impact on the economies of the region. A decrease in external demand influenced the reduction of the exports sector's output, which in consequence contributed to a decline in employment in the manufacturing sector and fall wages growth rate. In combination with a strong reduction of lending, it resulted in a drop in the consumption of households. A reduction of the activity of the manufacturing sector also contributed to the decrease in fixed capital formation. As a result, in Q4 2008 domestic demand in the region fell by 2.3% (as compared to the growth of 3.4% in Q1-Q3 2008)[4].

The economic growth rate varied widely among the countries of the region (significantly more than in the EU-15 countries). The highest economic growth was recorded in Bulgaria[5] (due to maintaining high investment growth rate). On the other hand, as many as five countries recorded a drop in the GDP y/y with the decline in Latvia and Estonia amounting to around 10%

[1] According to the Eurostat's estimates (15 May 2009), GDP in the Czech Republic declined by 3.4% (as compared to the growth of 0.7 in Q4 2008), in Bulgaria by 3.5% (+3.5%), in Slovakia by 5.4% (+2.5%), in Romania by 6.4% (+2.9%), in Hungary by 4.7% (as compared to a drop of 1.7% in Q4 2008), in Lithuania by 10.9% (-1.3%), in Estonia by 15.6% (-9.7%) and in Latvia by 18.6% (-10.4%) in 2009 Q1.

[2] A large decline in the GDP growth in that period took place only in the Baltic states, where it resulted from a decrease in domestic demand as a result of a dramatic reduction in lending. In other countries the decline in domestic demand growth rate, in particular in consumption growth rate, was relatively small as compared to 2007.

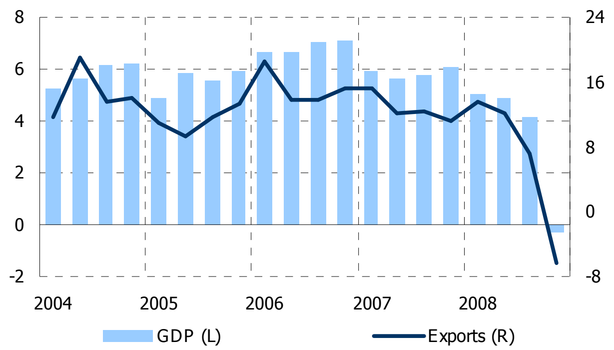
[3] The exports of the EU-15 countries to the non-EU countries rose by 7.1% in first three quarters of 2008 (as compared to 6.5% in 2007), while trade between the EU-15 countries demonstrated a stagnation trend.

[4] The impact of the domestic demand decline on the GDP growth rate was moderated by a positive contribution of net exports. The reduction in the trade imbalance resulted from a stronger decrease in imports than exports.

[5] The growth of GDP in Bulgaria in Q4 2008 was the highest not only among the new EU countries, but also in the entire European Union.

(the highest GDP decline in the European Union). In four countries affected by the global crisis in the period when they struggled with internal economic slowdown, the GDP decline q/q happened for at least second consecutive time. This means that the economies of the Baltic states and Hungary were at the stage of technical recession.

Figure 1.2
Exports and GDP growth rates in CEE countries (in %, y/y)

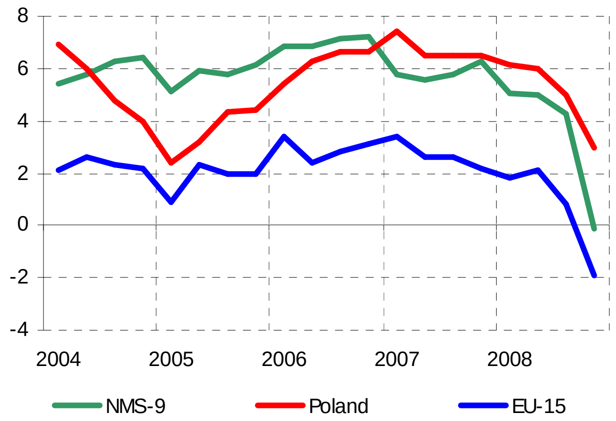


source: Ecowin Economic

The economic growth slowdown in other CEE countries considered collectively was stronger than in Poland in Q4 2008. It resulted from a relatively large decline in consumption expenditure in the region (by 2.5% y/y), while in Poland the expenditure grew by 5.3%. Such diversified tendencies stemmed from a higher impact of the exports sector on the changes in domestic demand in the remaining CEE countries (i.e. greater openness of the CEE economies as compared to Poland) and a slightly larger role of loans.

Although the scale of the GDP decline in the CEE countries in Q4 2008 was lower than in the EU-15 countries, the factors influencing the decline were slightly different. As compared to the old EU countries, the CEE countries experienced a significantly higher (over two times) drop in domestic demand (mainly as a result of a stronger decline in consumption expenditure). At the same time, the decline in consumption largely determined the strong decrease in imports, resulting in the positive contribution of net exports in the CEE countries (while in the EU-15 the scale of the imports decline proved to be lower than that of exports).

Figure 1.3
GDP growth rate (in %, y/y)



source: Ecowin Economic

Recession tendencies intensified in the region at the beginning of 2009, in relation to the further strong decline in external demand. This is evidenced both by strong decreases in retail sales and industrial output (in particular in the strongly export-oriented sectors) and by deteriorating consumer and business sentiment (often to the historically lowest levels).

In the majority of the CEE countries, industrial output fell by more than 20% y/y in the first two months of 2009. A strong decline (by around 40%) in the production of automotive industry, related to a global decrease in demand for cars, has a large impact on the reduction of production in the region. Such dramatic lowering of the production level is partly attributed to the policy pursued by automotive concerns, as a result of which the reduction of production was higher in the CEE countries than in countries of Western Europe. The introduction of government subsidies for car scrappage (in particular in Germany and France) contributed to the reduction of the scale of production decreases in the sector at the end of Q1 2009 and at the beginning of Q2 2009. Strong production declines were also recorded in the metallurgy industry at the beginning of 2009. In addition, in some countries the decline in industrial output was related to the interruptions in the gas deliveries from Russia. The decrease in output was followed by the deterioration in business confidence indexes, with particularly negative assessments concerning the inflow of export orders.

Further decline in consumption expenditure may point to the further downward trend in retail sales. As regards the deterioration in consumer confidence, the greatest role was played by the assessment of the deteriorating general economic situation which leads to the worsening of the situation on the labour market.

Labour market

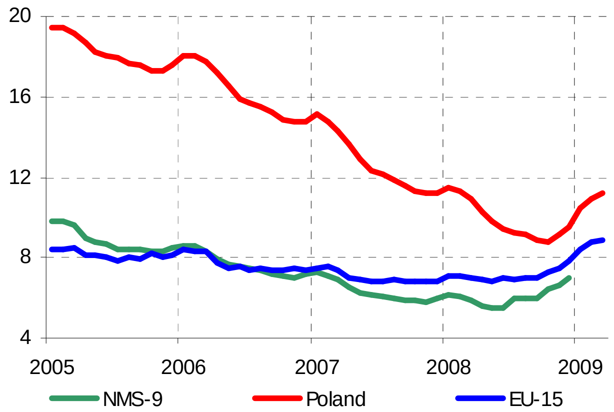
The worsening economic situation in the second half of 2008 led to the deterioration of the situation on the labour market. After several years of decline, the unemployment rate significantly grew in the entire region (on average from 5.5% in mid-2008 to 7% in December 2008), with the growth being the highest in the Baltic states and the lowest in Bulgaria and Romania. At the beginning of 2009, the unemployment rate continued to increase in the majority of the countries.

The rise in unemployment rate was accompanied by a decline in employment growth rate. At the beginning of 2008, it amounted to slightly over 2% y/y on average in the region and fell to zero in Q4. The number of employed decreased in Hungary and the Baltic states (it amounted to as much as 5.5% y/y in Latvia).

The unemployment growth rate in Central and Eastern Europe was slightly higher than in the EU-15 but lower than in Poland.

Figure 1.4

Unemployment rate (in %) and employment growth rate (in %, y/y)



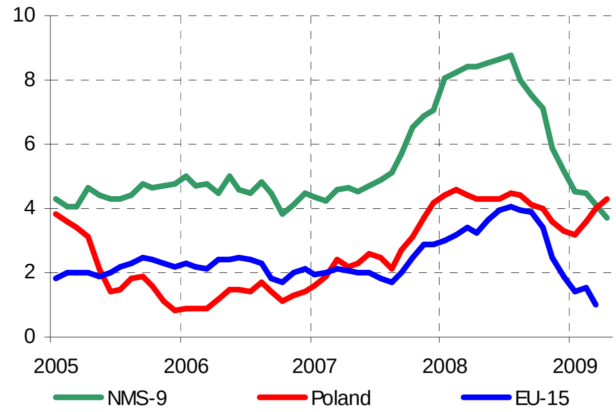
source: Ecowin Economic

Inflation and labour costs

After a period of strong price increase in the second half of 2007 and first half of 2008, the second half of 2008 was characterised by a marked disinflation trend in all economies of the region. This was mainly due to the situation on global market of energy and food. The fall in their prices caused the decrease in inflation all over the world, not only in the CEE region. The inflation decline was the most pronounced in the Baltic states, where within several months the consumption price growth rate fell by as much as 9 percentage points in Estonia. In 2009 the downward inflation trend continued in the countries with a fixed exchange rate regime and in the euro area countries. Strong depreciation of national currencies of Poland, Czech Republic, Hungary and Romania led to the growth of inflation in those countries in Q1 2009.

Figure 1.5

HICP (in %, y/y)



source: Ecowin Economic

The core inflation in the CEE countries also started to moderate as from Q4 2008. Apart from a direct impact of the decrease in food and energy prices, it was also affected by a decline in consumption demand.

Easing tensions on the labour market led to a drop in nominal wage growth rate in all countries of the region in the second half of 2008. In the case of Hungary and Slovakia, annual growth rate in Q4 was already negative. The highest drop in wage growth rate was recorded in the Baltic states. While in previous years the rate totalled almost 30% y/y, it declined by around 10-15 percentage points in Q4 2008 as compared to the beginning of 2008. A very high annual growth rate of nominal wages (20% y/y) continued to maintain in Bulgaria and Romania.

Despite a significant drop in nominal wage growth rate and the declining employment growth rate, the unit labour costs (ULC) growth rate fell insignificantly in 2008, due to economic slowdown in the CEE countries.

External imbalances

After two consecutive years (2006-2007) of the deepening current account deficit in the CEE countries, the deficit declined from 9.3% in 2007 to 8.9% in 2008. The improvement resulted mainly from the reduction of the deficit in Q4 2008. However, the tendencies inside the region varied. A very fast decline in deficits was recorded in the Baltic states and Romania in 2008 (but the deficits were still among the highest in the region)[6]. The reduction of the current account deficit was almost entirely due to the lowered negative balance of trade in goods, which remained its largest component. The decline in foreign trade deficit resulted mainly from the deterioration of domestic demand and thus the decrease in imports. Exports growth rate also dropped but to a smaller extent.

The current account deficit in Czech Republic and Bulgaria (the highest deficit in the region – 25.3% of GDP) remained virtually unchanged as compared to the previous year. In other countries of the region external imbalance increased (most markedly in Hungary)[7]. The structure of the deficit was not altered significantly with the largest items being the negative balance of trade in goods (5.6% of GDP in 2008 against 6.4% in 2007) and income deficit (5.4% in 2008 – practically without changes as compared to the previous year), which has the highest share in current account deficit in Czech Republic, Slovakia and Hungary.

Figure 1.6
Current account balance and its components (in % of GDP, 4Q moving average)

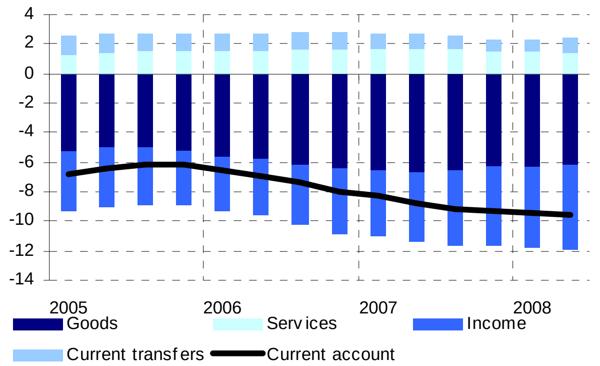
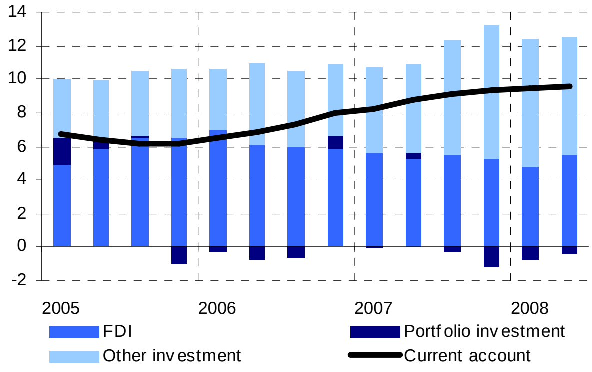


Figure 1.7
Financial account balance and its components (in % of GDP, 4Q moving average)



In Q4 2008 large outflows of portfolio investments were recorded mainly the countries with floating exchange rate regimes (Czech Republic, Hungary, Romania). In addition, intensifying liquidity crisis and declining foreign trade volume resulted in a decreased inflow of trade loans and loans for the banking sector, which caused the smaller inflow of other investment (particularly in the Baltic states). It continued in Q1 2009, but on a significantly smaller scale.

Exchange rates and interest rates

In the second half of 2008 and at the beginning of 2009 countries following a floating exchange rate regime (Czech Republic, Hungary and Romania) saw a very strong depreciation of national currencies as a result of an increase in global risk aversion, deteriorating sentiment for developing countries, including the CEE countries, and in consequence an outflow of foreign capital from those countries. Between August 2008 and February 2009 CZK depreciated by 27% against EUR, HUF by 33% and RON by 21% (in that period PLN depreciated by 50% against EUR). Exchange rates stabilized from mid-February 2009.

Following a period of the tightening of monetary policy, which lasted till mid-2008, central banks of Czech Republic, Hungary and Romania began to cut interest rates in order to cushion the crisis effects[8]. Between October 2008 and April 2009 the main interest rate in Czech Republic (to 1.5%) and Hungary (to 0.9%) was reduced by 200 basis points and by 250 basis points in Romania (to 10%). At the same time the NBP cut

[6] In Latvia current account deficit in relation to GDP fell from 22.5% in 2007 to 12.6% in 2008, while in Lithuania it declined from 18.1% to 9.2%, respectively.

[7] The current account deficit grew also in Poland from 4.7% in 2007 to 5.4% in 2008. However, it was still among the lowest in the CEE region, set aside Czech Republic.

[8] Although the Magyar Nemzeti Bank increased interest rates by 300 bps, it was a one-off action aimed at stopping the outflow of foreign capital.

the rates by 225 basis points to 3.75% and the ECB by 250 basis points to 1.25%.

Fiscal policy

The situation of public finances deteriorated in the majority of countries of Central and Eastern Europe in 2008 (except for Bulgaria and Hungary), but the degree of deterioration measured by the relation of public finance balance to GDP was diversified. Fiscal prospects for 2009 in many cases point to a further increase in public finance imbalance in the countries of the region. The risk for financial prospects is high due to uncertain economic environment and the impact of global crisis and introduction of fiscal stimuli packages.

The spring forecast of the European Commission (from May 2009) shows that in 2009 the marginal value of public finance sector deficit in relation to GDP established at 3% will be exceeded in Czech Republic, Poland, Latvia, Romania, Lithuania and Hungary, as well as in Slovenia and Slovakia which belong to the euro area. The highest rise in the deficit in 2009 is expected in Latvia (from 0.4% of GDP to 11.1% of GDP), which recorded surpluses in its budget until 2007, and in Slovenia (0.9% of GDP in 2008 to 5.5% of GDP in 2009). In view of major economic problems affecting public finances, Lithuania, Latvia and Romania use financial aid of the IMF, World Bank and other international institutions in order to alleviate the negative consequences of the crisis. Bulgaria is the only country in the region which will record a positive situation in public finances. According to the forecasts of the Bulgarian government, a fiscal surplus amounting to 1.5% of GDP will be maintained in 2009, as in 2008 (European Commission forecasts a deficit of 0.5% of GDP in 2009). Public finances in Hungary perform quite well against this background. After a very restrictive fiscal policy in recent years, due to a deep crisis in the public finance sector (in 2006 the deficit amounted to 9.2% of GDP), the situation begins to improve. The European Commission projects that the public finance sector deficit in Hungary will amount to 3.4% of GDP in 2009. The strategy of reducing the public finance sector deficit adopted by Hungary was supported by international financial aid from the EU, IMF and World Bank.

Forecasts

The deepening recession in Western Europe and the consequences of the financial crisis resulted in a significant moderation of the economic growth forecasts for Central and Eastern Europe in recent months. In addition, the correction was stronger than for forecasts for the EU-15 (due to a greater importance of external demand).

According to the spring forecast of the European Commission, in 2009 GDP in nine CEE countries will decline by 4.8%[9] (i.e. it will be stronger than in the EU-15 where a 4.0% decrease in economic growth is projected) and domestic demand will fall by 6.3% (and by 3.2% in the EU-15). High wage growth rate maintaining in some countries by the end of 2008 may support an increase in consumption expenditure also in 2009. A decline in exports (European Commission expects it will amount to 12.4%) will be of key importance for the degree of economic activity reduction in the region[10]. The decline in domestic demand coupled with the decline in demand of exports sector will have an impact on even stronger decrease in imports which will in consequence lead to an increase in a positive impact of net exports on GDP growth rate in the region to 2.2 percentage points.

The downward trend in GDP may hold also in 2010 (according to the European Commission, the GDP will drop by 0.3%), mainly as a result of a decline in consumption and investment with simultaneous reduction of the positive contribution of net exports. The GDP will continue to decrease in five countries (with largest decreases in Lithuania and Latvia).

Inflation forecasts for the coming years vary depending on exchange rate regime. Inflation is predicted to decline further in the countries with fixed exchange rate regimes in 2009, while the countries with floating exchange rate regimes are to see inflation fluctuating around the currently observed levels in the coming years.

Current account deficits are also to decline, with the greatest decreases observed in the countries which are currently characterised by the highest external imbalances (Baltic states, Bulgaria and Romania).

[9] The economic decline rate will vary. The largest decline by over 10% is expected in the Baltic states. A significant decline in GDP is expected in Hungary 6.3%, while the lowest is to be in Bulgaria (1.6%). Therefore, the decline in GDP will be larger in all CEE countries than in Poland (European Commission expects that the GDP will fall by 1.4% in our country).

[10] It seems justified to claim that changes in the exports structure of CEE countries, which took place in recent years, made the exports more sensitive to changes in external economic situation, in particular to changes in demand in the old EU countries. Due to a greaer role of corporate trade, exports, which managed to avoid the slowdown in the EU-15 countries in 2001 and 2002, are already severely affected by the recession in Western Europe.

BULGARIA

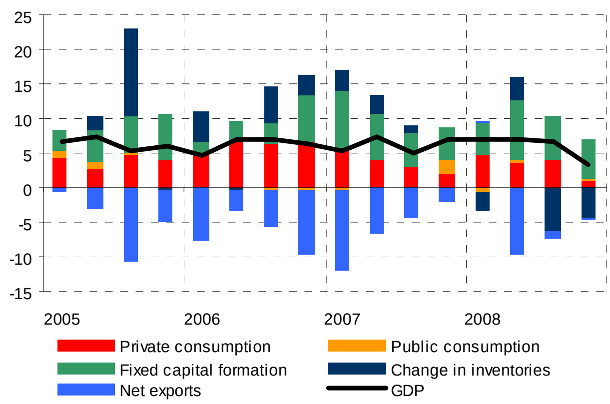
Economic growth

Similarly to other countries of the region, Bulgaria saw a marked reduction in economic growth rate in Q4 2008. While in the first three quarters of 2009 the GDP grew 7.0% y/y (i.e. significantly faster than the average for 2007), it increased only by 3.5% in the last quarter of 2008 (i.e. the increase was the slowest since 1999). As in the majority of the countries of the region, the reduction of economic growth rate was due to the reduction in availability of loans, lower foreign financing and the deterioration of the economic situation in main trade partners of Bulgaria.

The reduction of economic growth rate was mainly attributable to a decline in consumption growth rate (from 7.0% in the first three quarters to 1.8% in Q4) and a decrease in inventories. The growth rate of fixed capital formation remained relatively high (15.8% y/y in Q4, as compared to 22.1% y/y in Q1-Q3 2008), which is why investments remained the most important growth factor for the Bulgarian economy also at the end of 2008.

Figure 2.1

Contribution to GDP growth (in pp, y/y)



source: Ecowin Economic

Both exports and imports exhibited negative growth rate in Q4 2008, which caused a near zero share of net exports in the growth. Exports fell by 6.0% y/y (as compared to a growth of 6.0% in Q1-Q3 2008), while imports dropped by 3.8% (as compared to a growth of 7.9% in Q1-Q3 2008). In both cases the decreases resulted mainly from lower volume of trade in metals, oil and oil derivatives (due to simultaneous weakening of demand and decrease in prices on world markets).

Table 2.1

GDP and its components growth rate (in %, y/y)

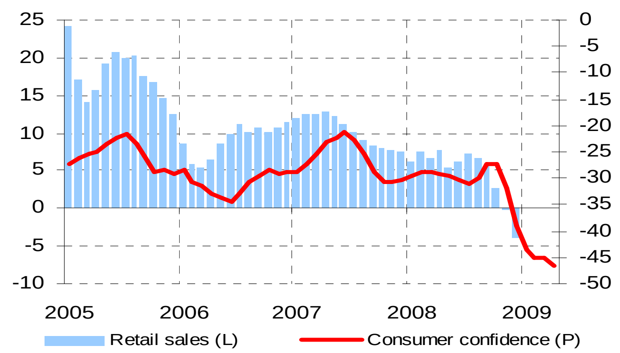
	2007	2008	Q3 2008	Q4 2008	Q1 2009
GDP	**6,2**	**5,8**	**6,8**	**3,5**	**-3,5**
Private consumption	5,3	5,0	6,5	1,8	
Public consumption	3,1	-0,9	0,4	-1,5	
Fixed capital formation	21,7	20,4	22,3	15,8	
Exports	5,2	2,9	3,8	-6,0	
Imports	9,9	4,7	4,2	-3,8	

source: Ecowin Economic

In 2008 the Bulgarian economy grew on average by 6.0%, i.e. similarly as in the previous year, but already in Q1 2009 the estimates show a decline in annual growth rate to -3.5%.

Figure 2.2

Retail sales (in %, y/y) and consumer confidence index

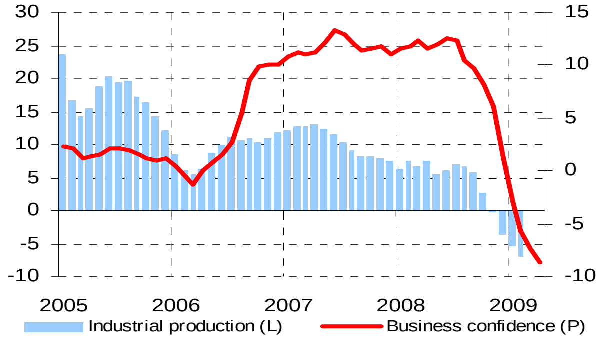


source: Ecowin Economic

The beginning of 2009 saw deepening retail sales declines. In February 2009, retail sales decreased by 6.4% y/y (as compared to a decline of 1.0% in Q4 2008) mainly as a result of a significant drop in sales of consumer durable goods. The deteriorating consumer sentiment was also reflected in further decline in confidence index, which fell to its all-time low in April 2009 (the index has been published since 2001). The deteriorating assessments of both current and future economic situation of the country had the greatest impact on consumer sentiment changes. Bulgarians fear that a decline in economic activity will contribute to a significant rise in unemployment. This is also a likely reason for concerns regarding the deterioration of future financial standing of households which have been growing fast since the beginning of 2009.

Figure 2.3

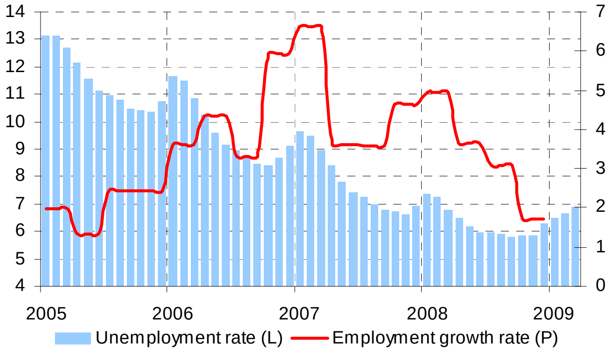
Industrial production (in %, y/y) and business confidence index



source: Ecowin Economic

Figure 2.4

Unemployment rate (in %) and employment growth rate (in %, y/y)



source: Ecowin Economic

The beginning of 2009 saw deepening industrial output declines. Between January and February 2009, it dropped by 18.0% y/y (as compared to a decrease of 6.6% in Q4 2008). The decline in output at the beginning of 2009 resulted, on the one hand, from the reduction of activities of some Bulgarian enterprises in relation to a temporary suspension of natural gas deliveries (as a result of a dispute on the transit of gas between Russia and Ukraine). On the other hand, foreign demand for the most important Bulgarian products, i.e. products of metallurgical industry and oil refinery products, suffered a significant decline. Decreases in current output were also one of the major reasons for deteriorating business sentiment. In March and April, business confidence index in manufacturing fell to its lowest level since 2001, which was attributable mainly to a decline in export orders. Business indexes in services and retail trade dropped to their all-time lows (the lowest values since 1991).

Labour market

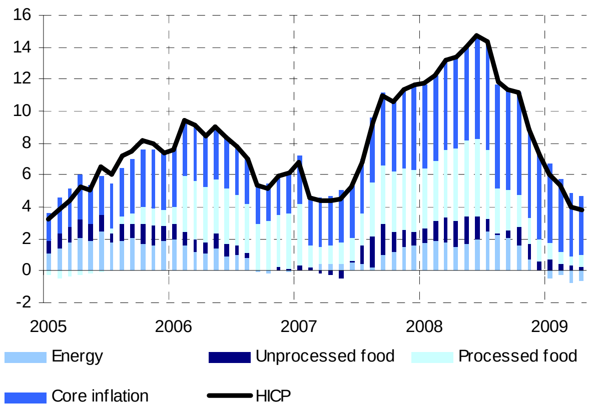
Despite a considerable decline in its growth rate, employment in the Bulgarian economy continued to grow in Q4 2008 (1.7% y/y as compared to 3.9% y/y in Q1-Q3 2008). A relatively small growth in unemployment rate, which amounted to 6.7% in February 2009, was attributable mainly to seasonal factors.

Inflation and labour costs

At the beginning of 2009, inflation in Bulgaria continued a downward trend. In April 2009 it fell to 3.8% (while in December 2008 it amounted to 7.2%). The decline in inflation was attributable to global factors, such as a price decrease on the energy raw materials market and to domestic factors, such as a decrease in food prices. The core inflation contracted much more slowly, as a result of increases in administrative prices (mainly electricity and public transport), tobacco products (increase in excise tax) and services. In addition, still high growth of unit labour costs (18.4% y/y in Q4 2008 as compared to 20.6% in Q1-Q3 2008) contributed to the maintenance core inflation at a relatively high level.

Figure 2.5

HICP and its components (in pp, y/y)



source: Ecowin Economic

Table 2.2

HICP and its components (in pp, y/y)

	Q2 2008	Q3 2008	Q4 2008	Q1 2009	04 2009
HICP	**14,0**	**12,5**	**9,1**	**5,1**	**3,8**
Categories with largest contribution					
Housing	0,8	1,3	1,4	1,5	1,4
Restaurants and hotels	2,4	2,3	1,8	1,6	1,4
Alcohol beverages and tobacco products	0,5	0,7	0,7	0,7	1,1
Miscellaneous	0,4	0,4	0,5	0,5	0,4
Recreation and culture	0,1	0,2	0,3	0,4	0,3

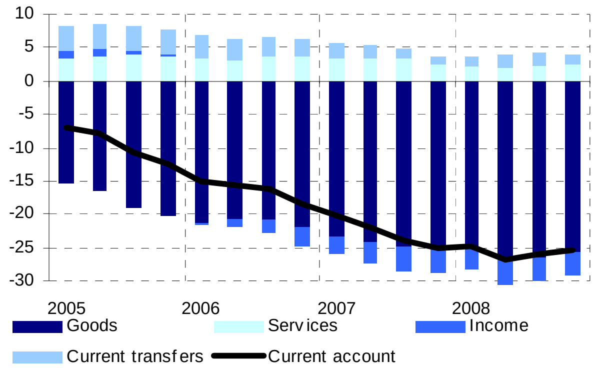
source: Ecowin Economic

External imbalances

In Q3 2008, the trend of deepening current account deficit was halted. After the third quarter the deficit in relation to GDP amounted to 25.3% as compared to 26.8% after Q2 2008. The reduction in a negative balance of trade in goods was the main factor behind the decrease in current account deficit. The improvement in the balance of trade in goods was limited due to the fixed exchange rate regime (currency board) and the fact that funds flowing into Bulgaria in recent years were mainly directed to the non-tradable sector, thus decreasing the relative competitiveness of the tradable sector. The positive balances of current transfers and trade in services, as well as income account deficit, were relatively stable.

Figure 2.6

Current account balance and its components (in % of GDP, 4Q moving average)



source: Ecowin Economic

Following a period of strong growth by the end of 2007, the surplus on financial account stabilised at 41.1% of GDP in the first half of 2008 and then began to contract to 25.6% of GDP in the second half of 2008. The inflow of both direct investments and other investments decreased, as did the portfolio investment account deficit.

Figure 2.7

Financial account balance and its components (in % of GDP, 4Q moving average)

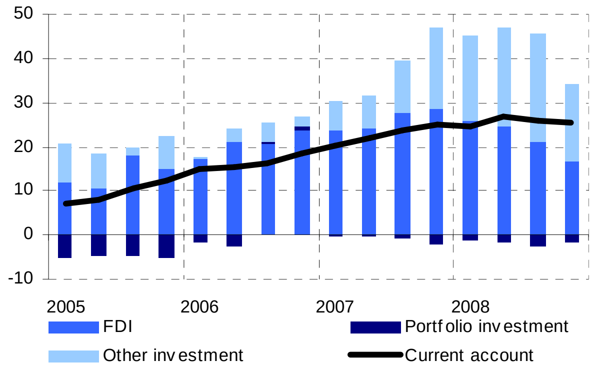


Table 2.3

Balance of payments (EUR mn)

	Q4 2007	Q1 2008	Q2 2008	Q3 2008	Q4 2008
Current account	-2674	-1980	-2485	-1381	-2788
Goods	-2305	-1779	-2488	-2122	-2370
Services	-208	-243	224	957	-108
Income	-270	-93	-568	-270	-276
Current transfers	109	135	347	54	-34
Capital account	77	174	0	8	23
Financial account	4033	2231	2768	2213	3264
Direct investments	2445	792	2017	1750	1126
Portfolio investments	-296	29	-264	-298	20
Other investments	2061	1552	2144	2209	73

source: Ecowin Economic

Interest rates

Following a growth to around 8.0% in the second half of 2008, interbank interest rates dropped to the levels comparable to the figures from the preceding year (average 3m Sofibor in February 2009 amounted to 6.61% as compared to 6.65% in February 2008). This temporary distortion on the financial market was mainly due to the reduced foreign financing of banks which led to the lack of confidence on the market and aggressive acquisition of deposits. The stabilisation of financial markets seems to reflect the stability of the currency board which pegs the Bulgarian lev to the euro.

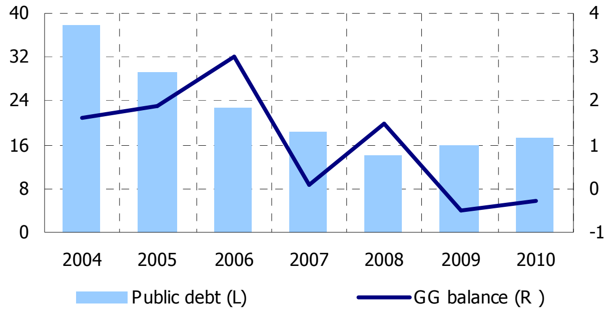
Fiscal policy

In 2008 the public finance sector in Bulgaria attained a positive balance of 1.5% of GDP (as compared to 0.1% of GDP in 2007). The result would have been even better, if the government had not made a decision on additional spending, mainly capital expenditure, in December 2008.

A very high economic growth prevailing in the first three quarters of 2008 has a positive impact on income situation of the public finance sector. As a result, despite the economic growth slowdown in Q4 2008 translating into the lower tax revenues within that period, total revenues of the finance sector proved to be higher than planned in 2008 (by 0.5 percentage point).

Fiscal forecasts for 2009 are subject to high uncertainty related to the impact of the global financial crisis on the Bulgarian economy. The 2009 budget was based on an optimistic assumption of a positive economic situation in 2009 and the resulting dynamic growth of budget revenues. The Bulgarian government assumed a fiscal surplus of 3% of GDP in 2009. According to the spring forecast of the European Commission (of May 2008), the public finance sector may in 2009 attain a negative balance of 0.5% of GDP. The government anticipated a surplus of 1.5% of GDP in 2009 in the spring fiscal notification.

Figure 2.8
General government balance and debt (in % of GDP)



source: Eurostat

The Bulgarian government declares to pursue prudent fiscal policy to maintain macroeconomic equilibrium and does not project any specific fiscal measures aimed at stimulating the economy in 2009. An increase in investment public expenditure is to be the main factor to improve domestic demand and reduce unemployment. To attain the fiscal target for 2008, the budget act for 2009 includes a rule allowing to reduce the central budget current expenditure by 10% (excluding social transfers and debt servicing costs) if the budget revenues are lower than assumed in the budget act.

Forecasts

Although Bulgaria was the fastest developing economy of the CEE region in Q4 2008, international forecast institutions agree that 2009 will see a decline in GDP. The Bulgarian National Bank also anticipates that in 2009 the Bulgarian economy may contract by as much as 2.0% y/y. A relatively small decline in GDP in 2009 will probably be the result of an improvement in trade balance. The fall in imports is expected to exceed the decline in exports, which is due to a marked weakening of domestic demand, mainly fixed capital formation which were growing two-fold in recent years. Despite the reduced loan availability and increasing unemployment, the decline in consumption of households will be relatively low due to maintaining positive wage growth rate. According to the European Commission, GDP will continue to contract in Bulgaria also in 2010.

Global trends on the markets of energy raw materials, weakening domestic demand, decreasing unit labour costs and a favourable base effect in the majority of categories will contribute to further gradual decline in inflation in 2009. Disinflation trends are set to continue also in 2010. The decline in domestic demand will also lead to the contraction of current account deficit which according to the expectations of the International Monetary Fund may drop to 3.6% in 2010 (from 25% in 2008).

Table 2.4
Forecasts of main indicators

	EC	IMF	Consensus Economics
	05.2009 (11.2008)	04.2009 (10.2008)	04.2009 (11.2008)
GDP, in %, y/y			
2008	6,0 (6,5)	6,0 (6,3)	6,0 (5,9)
2009	-1,6 (4,5)	-2,0 (4,3)	-1,0 (3,6)
2010	-0,1 (4,7)	-1,0 (5,5)	1,2
Inflation, in %, y/y			
2008	12,0 (12,4)	12,0 (12,2)	12,4 (12,5)
2009	3,9 (7,9)	3,7 (7,0)	4,7 (7,6)
2010	3,6 (6,8)	1,3 (4,7)	4,0
Current account balance, in % of GDP			
2008	-24,8 (-23,8)	-24,4 (-24,4)	
2009	-18,8 (-22,3)	-12,3 (-21,5)	
2010	-17,2 (-21,5)	-3,6 (-19,9)	

CZECH REPUBLIC

Economic growth

The economic growth rate in the Czech Republic slowed down already in the first three quarters of 2008 (to slightly more than 4%). It was mainly attributable to the contraction in inventories, although it was accompanied by the weakening domestic demand, both consumption and investments. Meanwhile, as a result of the decline in imports due to the weakening domestic demand (while exports recorded a strong growth of almost 13% in Q1-Q3 2008), the contribution of net exports to the GDP growth showed an increase.

Figure 3.1
Contribution to GDP growth (in pp, y/y)

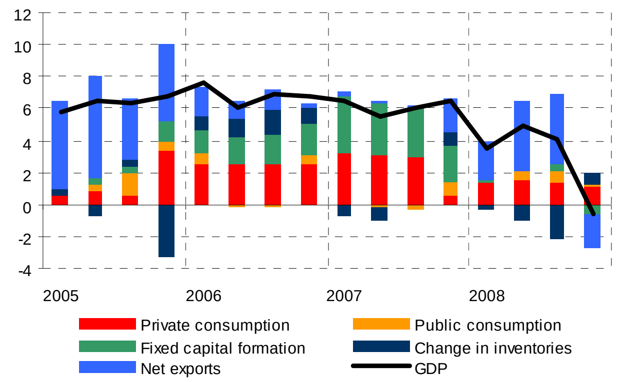


Figure 3.1
GDP and its components growth rate (in %, y/y)

	2007	2008	Q3 2008	Q4 2008	Q1 2009
GDP	**6,0**	**3,2**	**4,0**	**0,2**	**-3,4**
Private consumption	5,2	2,9	3,0	2,6	
Public consumption	0,4	0,9	2,6	-0,2	
Fixed capital formation	6,7	3,1	3,4	0,3	
Exports	14,9	6,9	9,0	-8,7	
Imports	14,2	4,6	4,3	-6,9	

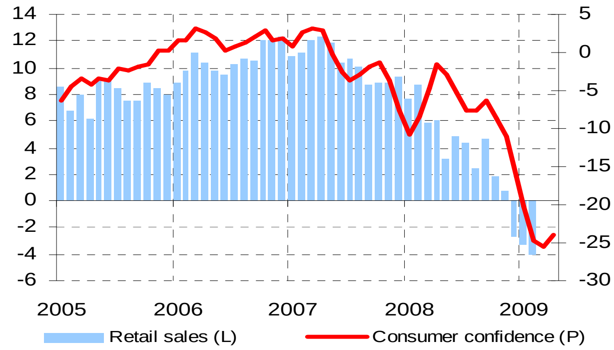
source: Ecowin Economic

In the context of weakening domestic demand, the decline in exports which took place in Q4 2008 (by 8.7%) also contributed to a pronounced decrease in the GDP growth rate. The result was a marked decline in the contribution of net exports which were responsible for maintaining the economic growth rate in the previous quarters (to -2 percentage points as compared to 4 percentage points in the three preceding quarters of 2008). The reason for the decline was a considerable weakening of external demand, particularly in the EU-15 countries which are the main recipients of Czech goods and services. The decline in exports and fixed capital formation was related to a contraction in industrial output and services (except for trade). Trade and agriculture were the only sectors to record an increase in added value in Q4 2008.

Preliminary estimates of the GDP for Q1 2009 point to its marked decline y/y (by 3.5%).

Constantly deteriorating indicators of business sentiment (all-time low), as well as the decline in industrial output growth rate observed since the beginning of 2008, in particular in the manufacturing of non-metal products, machines and equipment and motor vehicles, which deepened in 2009 (23.4%, 35.8% and 27.9% y/y in February, respectively) indicate the intensifying recession in the Czech economy. The main reason behind the deterioration of business sentiment was a pronounced drop in orders, in particular export orders. The slight improvement of sentiment in April 2009 stemmed from a better assessment of future output prospects.

Figure 3.2
Retail sales (in %, y/y) and consumer confidence index



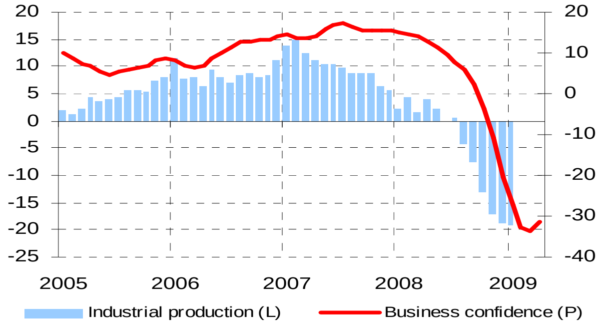
source: Ecowin Economic

The consumer sentiment also deteriorated significantly (to the lowest level in 10 years), mainly due to unfavourable economic growth prospects and expectations of maintaining high inflation[11]. The consumer sentiment improved somewhat in April 2009 as a result of a better assessment of the prospects of the Czech economy. The deteriorating consumer sentiment was accompanied by a decline in retail sales growth rate (it fell by 7.9% y/y in April 2009).

[11] Inflation dropped significantly in 2009. Therefore, the resulting increase in pessimisn may be expected to maintain.

Figure 3.3

Industrial production (in %, y/y) and business confidence index



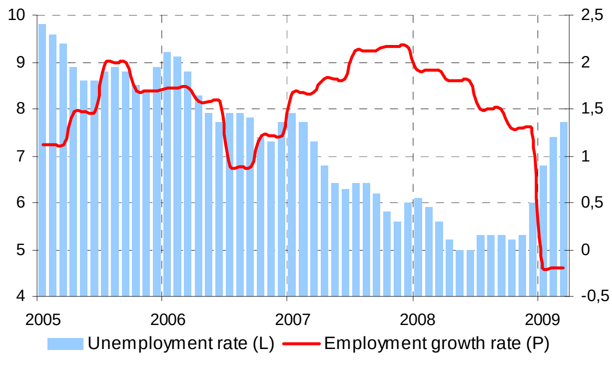
source: Ecowin Economic

Labour market

The deepening recession in manufacturing and services resulted in the deterioration of the situation on the Czech labour market. The unemployment rate, which fell by almost 6 percentage points between 2004 and the first half of 2008, recorded a pronounced increase in the second half of 2008 (to 7.7% in March 2009). The employment growth rate in the Czech Republic, which exceeded 2% at the end of 2007, also followed a downward trend in 2008 and became negative in Q1 2009 (-0.2% y/y). The number of jobs in agriculture and industry, mainly in manufacturing, decreased, while the number of the employed in services grew.

Figure 3.4

Unemployment rate (in %) and employment growth rate (in %, y/y)



source: Ecowin Economic

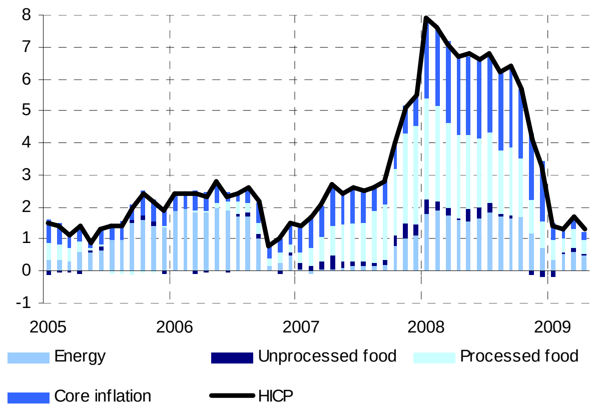
Immigrants account for a large part of the Czech labour market (around 360 000 legally employed immigrants, i.e. around 7.5% of all workforce), many of them from outside the EU (Ukrainians, Vietnamese, Mongolians). The fast unemployment growth (expected to reach 10% by the end of 2009) and increased social unrest led to the establishment of a USD 3 million worth programme of financing the return of immigrants to their countries of origin (EUR 500 for an adult, EUR 250 for a child and the cost of plane tickets). The programme covered around 1400 people within three months (February – April 2009). At the beginning of May 2009 the budget of the programme was increased to USD 4.5 million. Similar programmes of fight against unemployment were introduced by Spain and Japan.

Inflation and labour costs

In 2008 the HICP growth rate remained elevated[12], but exhibited a marked downward trend which intensified in the second half of the year. It resulted mainly from global factors, i.e. falling prices of food and energy raw materials. In December 2008 inflation in the Czech Republic amounted to 3.3%. At the beginning of 2009 the annual inflation dropped abruptly below the inflation target (2%), due to the receding base effect observed in 2008, to 1.3% in April 2009. The decline in inflation in 2009 was lower than the average for the region as a result of the depreciation of the koruna and the increases in administrative prices. The prices of energy, utilities and excise tax for alcohol and tobacco products are the main contributors to inflation due to their increase at the beginning of 2009. Other prices, including food prices, in majority decreased in Q1 2009. The depreciation of the Czech koruna contributed to the growth of inflation in recent months, as it led to the increased price growth of energy and fuels.

Figure 3.5

HICP and its components (in pp, y/y)



[12] At the beginning of 2008 inflation in the Czech Republic grew as a result of an increase in administrative prices and indirect taxes (i.a. medical services, energy resources, alcohol and tobacco products). As a result, the consumption price growth rate increased by around 2 percentage points to 7.9% in Jnauary 2008.

Table 3.2

HIC P and its components (in pp, y/y)

	Q2 2008	Q3 2008	Q4 2008	Q1 2009	04 2009
HICP	**6,7**	**6,5**	**4,4**	**1,7**	**1,3**
Categories with largest contribution					
Housing	1,9	2,1	2,4	2,2	2,0
Alcohol beverages and tobacco products	0,9	0,8	0,9	0,8	0,8
Restaurants and hotels	0,5	0,5	0,4	0,2	0,1
Miscellaneous	0,3	0,3	0,3	0,1	0,1
Edukacja	0,0	0,0	0,0	0,0	0,0

source: Ecowin Economic

Despite the economic slowdown and deteriorating situation on the labour market, the growth of wages in 2008 accelerated considerably as compared to the previous year (8.6% in 2008 vis-à-vis 7.3% in 2007). In Q4 2008 the annual wage growth rate increased as compared to Q3 (8.3% vis-à-vis 7.8%). The wages increased the most in mining industry, construction and financial services.

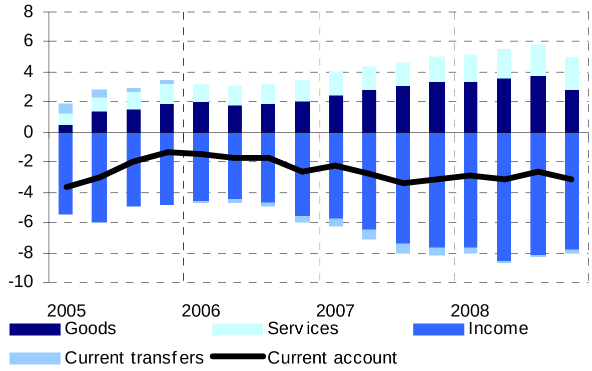
The high growth of wages coupled with a positive employment growth rate contributed to the increased unit labour costs growth rate. Along with the economic slowdown in 2008, unit labour costs grew considerably as compared to 2007 (7.0% in 2008 as compared to 3.3% in 2007), particularly in Q4 2008 (9.4%).

External imbalances

The current account deficit in 2008 remained at the similar level as in the previous year (3.1 and 3.2% of the GDP, respectively). The structure of the current account deficit remained broadly unchanged with the greatest impact exercised by a negative income balance (almost 8% of the GDP, which marks a slight increase as compared to 2007). A surplus in the trade in goods and services contributed to the reduction of the current account deficit (contrary to other CEE countries), although it gradually decreased in 2008. As a result, in Q4 2008 the Czech Republic recorded a negative balance of trade in goods for the first time since 2004.

Figure 3.6

Current account balance and its components (in % of GDP, 4Q moving average)



source: Ecowin Economic

The deterioration of the foreign trade balance was mainly attributable to the decrease in exports resulting from the economic slowdown in the world, and in particular in the EU-15 countries (mainly in Germany), which are the main trade partners of the Czech Republic. In Q4 2008 the value of exports (in EUR, y/y) fell by almost 14%, and by over 20% in January and February 2009, due to a massive decrease in exports of cars (by 30% and 35%, respectively). In March 2009, the decline in exports considerably contracted, due to a larger than in the previous months exports of motor vehicles, to Germany and Slovakia (supported by government subsidies to the purchase of new cars in those countries).

Table 3.3

Balance of payments (EUR mn)

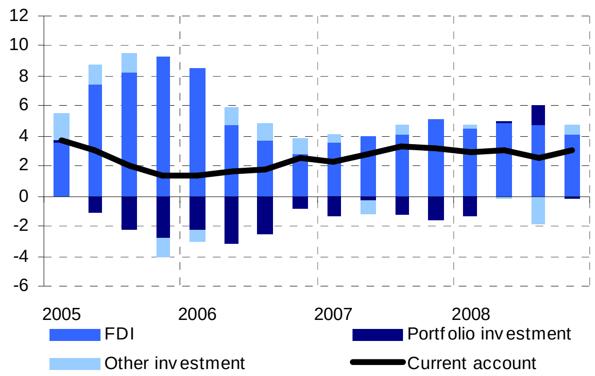
	Q4 2007	Q1 2008	Q2 2008	Q3 2008	Q4 2008
Current account	-1457	1185	-2251	-1249	-2296
Goods	1005	1679	1597	1140	-268
Services	404	872	891	810	714
Income	-2778	-1410	-4823	-2899	-2494
Current transfers	-89	45	85	-300	-247
Capital account	502	272	515	77	372
Financial account	1690	-623	2704	1941	2100
Direct investments	2301	842	2141	1720	1354
Portfolio investments	472	-510	1583	351	-1732
Other investments	-1008	-801	-947	-11	2689

source: Ecowin Economic

The structure of the financial account also remained broadly unchanged in 2008. Direct investments continued to be the largest item (4% of GDP) but their inflow decreased as compared to 2007 (5% of GDP). Contrary to other countries of the region, the net inflow of other investments (loans) increased in 2008, but failed to exceed 1% of GDP.

The Q4 2008 saw a relatively large outflow of portfolio investment (4% of GDP), but their inflow in the previous three quarters resulted in the annual portfolio investment balance being close to zero.

Figure 3.7
Financial account balance and its components (in % of GDP, 4Q moving average)



source: Ecowin Economic

Interest rates and foreign exchange rate

In the second half of 2008, the National Bank of Czech Republic (CNB) started the process of easing the monetary policy. Between July 2008 and May 2009, it reduced interest rates on 5 occasions, in total by 225 b.p. to 1.50%.

3-month interest rates on the inter-banking market increased considerably in October 2008 which was caused by turmoil on international financial markets. However, this increase was short-term, and in addition to further reductions in interest rates by the CNB, interest rates on the Czech inter-banking market gradually decreased and reached approx. 2.5% in May 2009.

In the second half of 2008 and at the beginning of 2009, Czech koruna (CZK) depreciated considerably, similar to other currencies in the region. Between July 2008 and February 2009, EUR/CZK exchange rate fell by 29% and NEER by 13%. In the middle of the first quarter of 2009, Czech koruna started to appreciate (by 10% between the mid-February and the beginning of May 2009).

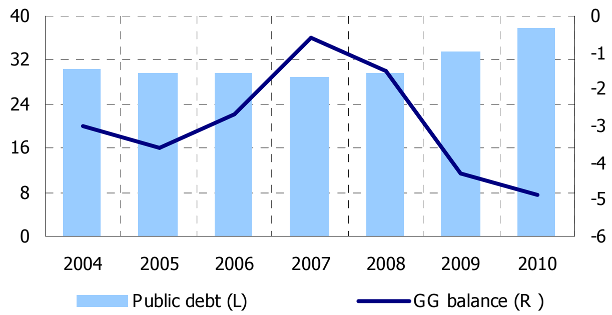
Fiscal policy

In 2008, deficit of the public finance sector amounted to approx. 1.5% GDP, i.e. slightly exceeded the plan figure set in the Convergence Programme (1.2% GDP). Increasing imbalance of public finance last year (2007 deficit amounting to 0.6% GDP) was related, inter alia, to deterioration of the economic situation, higher use of funds rolled forward from previous years and necessity of an additional valorisation of pension and disability benefits. Despite lower indirect tax revenues than assumed in the budget act - due to deterioration of economic prosperity in Czech Republic - high non-tax revenues made it possible to exceed planned state budget revenues in 2008 (by 1.4 p.p.).

Fiscal forecasts for 2009 were verified due to a considerable decline in the expected growth of Czech economy (from 4.8% to 1.4%) as a result of the global financial crisis.

The Convergence Programme, submitted to the European Commission in November 2008, assumed deficit of the public finance sector in 2009 at 1.6% GDP, however, at present it is estimated at 3.9% GDP. The European Commission estimates that a negative balance will grow in 2009 as a result of the deterioration of the economic situation, automatic stabilisers and discretional actions (fiscal package), and will amount to 4.3% GDP.

Figure 3.8
General government balance and debt (in % of GDP)



source: Eurostat, 2009-2010: wiosenna prognoza KE (z maja br.)

In February this year, Czech government presented the National Anti-crisis Plan comprising changes implemented since the beginning of 2009 as well as new proposals (which were largely adopted by the Parliament). The Anti-crisis Plan, aimed at stimulating Czech economy, comprises the following actions:

- reducing social insurance contributions for an employee (by 1.5 p.p.) and by an employer (by 1 p.p.),
- reducing CIT rate (by 1 p.p.),
- blocking 5% of current expenditures in some ministries,
- increasing expenditures on transport infrastructure as well as on research and development,

– improving the use of EU funds,
– reducing bureaucratic burden.

Financial results of the above actions are estimated at approx. 2% GDP and their implementation would provide a relief to public finance. In May this year was adopted a project which implements a subsidy to the purchase of a new car, if another car - at least 10 years old - has been scrapped (approx. 0.1% GDP).

Forecasts

GDP growth forecasts for 2009 and 2010 are much worse than in the recent months. In April and May this year, GDP was forecast to fall significantly (as much as 3.5%), whereas an increase by 3% was estimated at the end of 2008. A decline in GDP may be influenced mainly by a considerable decline in exports and investment expenditures (additional forecasts for these categories were revised down most considerably).

Inflation forecasts also decreased as compared to the end of 2008, however, depreciation of Czech koruna led to the fact that inflation forecasts fell more significantly than in other countries in the region.

Forecasts for the balance on the current account indicate that it will not change much in 2009 and 2010 as compared to the balance observed last year.

Table 3.4

Forecasts of main indicators

	European Commission	IMF	Consensus Economics	ČNB
	05.2009 (11.2008)	04.2009 (10.2008)	04.2009 (11.2008)	05.2008 (11.2008)
GDP, in %, y/y				
2008	3,2 (4,4)	3,2 (4,0)	3,1 (4,2)	0,2 (4,5)
2009	-2,7 (3,6)	-3,5 (3,4)	-2,5 (2,6)	-2,4 (2,9)
2010	0,3 (3,9)	0,1 (4,2)	1,1	1,4
Inflation, in %, y/y				
2008	6,3 (6,6)	6,3 (6,7)	6,3 (6,5)	6,4 (6,6)
2009	1,1 (3,1)	1,0 (3,4)	1,5 (2,7)	0,9 (2,5)
2010	1,6 (2,0)	1,6 (2,0)	2,2	2,0
Current account balance, in % of GDP				
2008	-3,1 (-1,9)	-3,1 (-2,2)		-1,4 (-1,4)
2009	-3,2 (-2,2)	-2,7 (-2,5)		0,0 (0,0)
2010	-3,3 (-1,2)	-3,0 (-2,7)		

ČNB - Česká národní banka

ESTONIA

Economic growth

In 2008, Estonian and Latvian GDP fell most considerably in the region. Last year, Estonian economy shrank by 3.6% as compared to 2007, and in the fourth quarter real GDP decreased by 9.7% y/y. The crisis in Estonia started already in mid-2007, and turbulences on world financial markets made it even sharper. The crisis deepened in the first quarter of 2009 and preliminary estimates show an annual GDP fall by as much as 15.6%.

In 2008, an economic growth structure changed. In the recent years, when economic growth in Estonia amounted to 10% y/y, it was based mainly on a strong domestic demand, both of consumption and investment character, whereas net exports negatively influenced GDP growth. A decline in economic activity in 2008 resulted first of all from a weakening domestic demand (consumption and investments) which caused a significant decline in imports growth, and as a result, a contribution of net exports to GDP growth increased considerably (it was positive for the first time since the beginning of 2004). Exports growth in Estonia also decreased as in other countries in the region, but much less than imports growth.

Figure 4.1

Contribution to GDP growth (in pp, y/y)

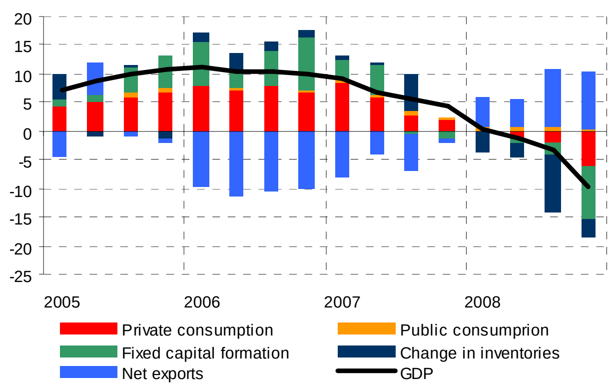


Table 4.1

GDP and its components growth rate (in %, y/y)

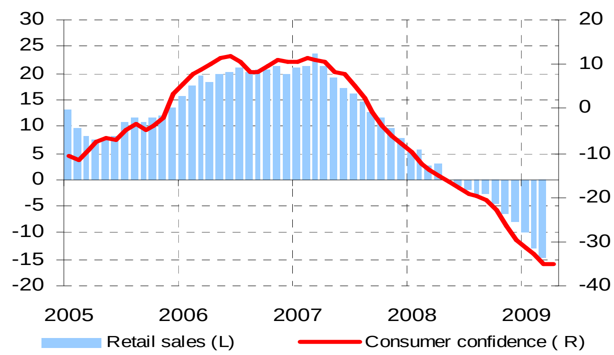
	2007	2008	Q3 2008	Q4 2008	Q1 2009
GDP	**6,3**	**-3,6**	**-3,5**	**-9,7**	**-15,6**
Private consumption	7,8	-4,0	-3,5	-10,4	
Public consumption	3,9	4,4	5,7	3,3	
Fixed capital formation	4,8	-7,6	-6,0	-20,4	
Exports	0,0	-1,1	6,3	-3,2	
Imports	4,2	-7,9	-4,9	-11,9	

source: Ecowin Economic

Consumer confidence and entrepreneur confidence indices in Estonia have been gradually decreasing since the beginning of 2007. As regards consumer prosperity, the most considerable deterioration affected the perception of current and future financial situation of households and the country's general economic situation. With respect to companies, deterioration was observed in sub-indicators measuring the number of orders, in particular export orders, as well as employment indices.

Figure 4.2

Retail sales (in %, y/y) and consumer confidence index

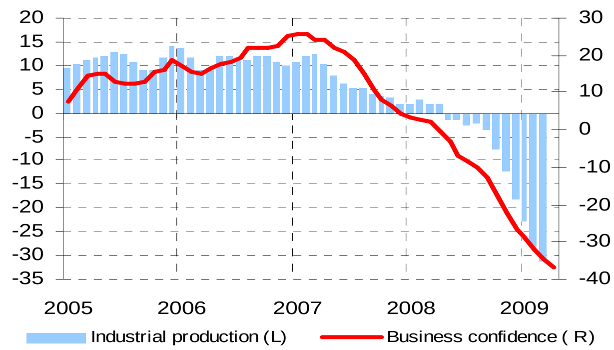


source: Ecowin Economic

Deteriorating consumer and business confidence indices were accompanied by a decline in retail sales and industrial production growth rates which were negative since mid-2008. A decline in retail sales slowed down slightly in March 2009, but still amounted to as much as -15% y/y. In March 2009, industrial production fell by 32% y/y (the biggest fall in the region), including a decline in production of construction materials by 55% and of machinery and equipment by 41%.

Figure 4.3

Industrial production (in %, y/y) and business confidence index

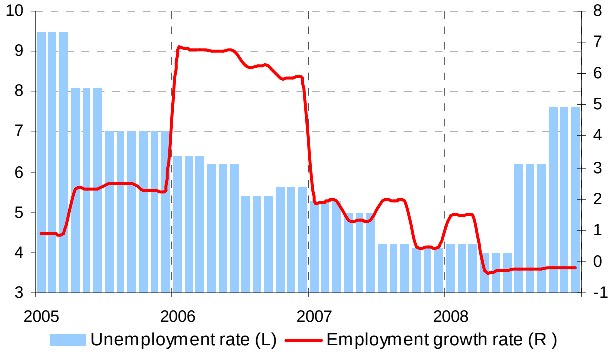


source: Ecowin Economic

Labour market

The deepening economic crisis had a significant impact on the deterioration of the situation on the labour market. After a long-term decline (since the beginning of 2004 – from over 10% to 4% in the second quarter of 2008) unemployment rate almost doubled in the second half of 2008. Employment in economy, which slightly increased even in the first quarter of 2008, fell in the following quarters. 2008 was also marked by a change in the employment structure. The number of employees decreased in agriculture and industry, and increased in services.

Figure 4.4
Unemployment rate (in %) and employment growth rate (in %, y/y)



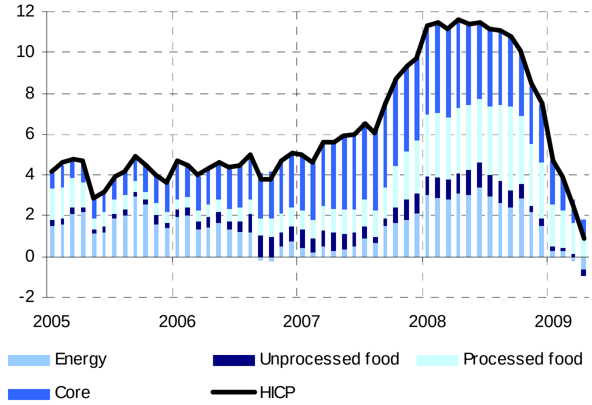
source: Ecowin Economic

Inflation and labour costs

In mid-2008, inflation in Estonia reached its peak in the last 10 years (11.6% y/y in April). Since the second half of 2008, HICP growth clearly slowed down and fell to 7.5% y/y in December 2008. A decline in inflation resulted mainly from falling food and energy prices, though also core inflation demonstrated downward tendencies due to a decreasing domestic demand and deteriorating situation on the labour market.

Furthermore, at the beginning of 2009, it was possible to observe in Estonia the expiry of the base effect related to increases in regulated prices which took place at the beginning of 2008 (first of all in energy prices). As a result of this fact a downward trend in inflation accelerated in 2009. In April this year, annual HICP growth rate slowed down to 0.9% which means the lowest inflation level in the region.

Figure 4.5
HICP and its components (in pp, y/y)



A growth in nominal salaries in Estonia remained at a high level for the most part of 2008 (on average 16.5% y/y in the first three quarters of 2008). It was only in the fourth quarter of the previous year that salaries growth fell considerably to 6.8% y/y. Actions taken by Estonian government, aimed at reducing salaries in the public sector by 10% and allowing to reduce salaries in enterprises by 7%, will lead to a further decline in salaries growth in further quarters.

A considerable decline in salaries growth in the fourth quarter of 2008, combined with a decline in employment, caused a downward trend in the growth of labour unit costs. The scale of this decline was, however, limited by deepening recession in economy.

Table 4.2
HICP and its components (in pp, y/y)

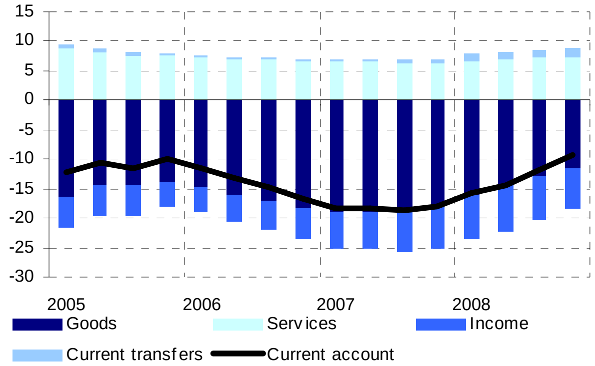
	Q2 2008	Q3 2008	Q4 2008	Q1 2009	kwi-09
HICP	**11,5**	**11,0**	**8,7**	**3,7**	**0,9**
Categories with largest contribution					
Alcohol beverages and tobacco products	0,7	1,6	2,1	1,7	1,6
Housing	2,3	1,7	2,4	1,6	0,4
Miscellaneous	0,6	0,5	0,4	0,5	0,4
Clothing and footwear	0,4	0,3	0,3	0,1	0,2
Health	0,3	0,3	0,2	0,2	0,2

source: Ecowin Economic

External imbalances

In 2008, deficit on the current account in Estonia gradually decreased. In 2007, it exceeded 18% GDP and in 2008 fell to 9.2% GDP. A decline in deficit was caused most considerably by decreasing deficit in trade with goods, and to a lesser extent by increasing positive balance on the services account and current transfers account.

Figure 4.6
Current account balance and its components (in % of GDP, 4Q moving average)



source: Ecowin Economic

Tendencies in foreign trade of Estonia were similar to those observed also in other Baltic countries. In 2008, imports decreased which strengthened further in the second half of the year. The most considerable decline affected a demand for imported machinery and equipment as well as for mechanical vehicles which results from a collapse of domestic demand in Estonia. At the same time, exports growth slowed down considerably not earlier than in the fourth quarter. Exports decreased in almost all categories of goods (except for chemicals and machinery). The most significant decline in exports affected Latvia and Lithuania which belong to Estonia's main trade partners (approx. 17% of foreign trade).

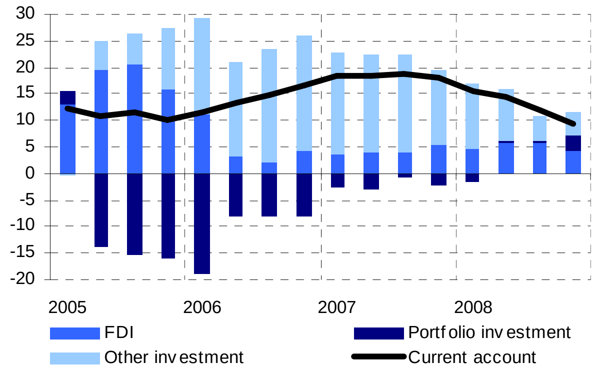
Table 4.3
Balance of payments (EUR mn)

	Q4 2007	Q1 2008	Q2 2008	Q3 2008	Q4 2008
Current account	-669	-502	-454	-301	-199
Goods	-639	-495	-479	-475	-393
Services	219	237	329	344	235
Income	-289	-324	-354	-212	-167
Current transfers	40	80	51	42	127
Capital account	31	53	27	11	45
Financial account	342	569	593	205	372
FDI	343	270	193	79	17
Portfolio investment	-8	30	155	-100	305
Other investment	30	218	246	264	20

source: Ecowin Economic

In 2008, an inflow of direct investments decreased (3.5% GDP as compared to 5.3% GDP in 2007) which was a result of a smaller inflow of reinvested gains (lower profits of companies). Tightening credit policy of banks in Estonia, financial turmoil on world markets and deteriorating outlook for the Estonian economy led also to a considerable decline in the inflow of other investments (mainly trade credits and credits for the banking sector). In 2007, this was the main source of financing for deficit on the current account. At the same time, their inflow decreased significantly in 2008 (in particular in the fourth quarter of the previous year) which limited considerably their role in financing external imbalances.

Figure 4.7
Financial account balance and its components (in % of GDP, 4Q moving average)



source: Ecowin Economic

Interest rates

In the first three quarters of 2008, 3-month interest rates on the inter-banking market in Estonia were relatively stable (6.4-6.6%). Turmoil on financial markets in October and increasing aversion to risk as well as worsening outlook for Central and Eastern European countries led to their increase to almost 8% at the end of 2008. In 2009, interest rates in Estonia slightly decreased to 6.2% in May. A considerable decrease in inflation in the second half of 2008, and first of all in 2009, led to the situation when in 2009, for the first time since 2009, real 3-month interest rates in Estonia were positive.

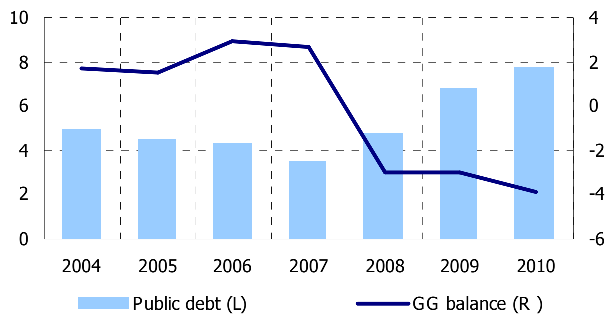
Fixed exchange rate regime saved Estonian currency (as well as currencies of other Baltic countries) from depreciation which took place in other countries of the region applying a floating exchange rate policy. A nominal effective exchange rate of Estonian koruna strengthened in March 2009 by 3.1% y/y, and a real rate (REER) by 3.5% y/y. Appreciation of the currency, in particular during the world crisis, may be, however, a factor decreasing competitiveness of the economy, and may additionally extend the recession period in Estonia.

Fiscal policy

In 2008, public finance of Estonia generated deficit for the first time since 2002 (3.0% GDP as compared to 1.9% GDP assumed in the recent Convergence Programme).

A negative general government balance was a result of a strong economic slowdown started in 2007 and negatively influenced the income situation of public finance despite reductions in administrative expenditures made last year (by approx. 7%).

Figure 4.8
General government balance and debt (in % of GDP)



source: Eurostat, 2009-2010: EC spring forecast 2009

A strong decline in economic activity forecast for 2009 and continuation of negative tendencies on the labour market will probably lead to a further increase in the general government deficit this year to approx. 2.9% GDP (governmental forecast included in the spring fiscal notification). The European Commission estimates that a negative balance of the government sector will amount this year to 3.0% GDP. In order to limit the increase in deficit of this sector, Estonian government prepared savings in public expenditures, inter alia, by reducing salaries of the public sector employees by 10%, paying illness benefits from the 9th and not from the 1st day of illness leave, changing the financing method of investments in roads (larger use of EU funds instead of revenues from excise tax on engine fuels) and reducing expenditures on environmental programmes.

The situation of Estonian public finance is protected by financial reserves estimated at approx. 8-9% GDP, generated in the years 2002 – 2007, when the public finance sector generated high surpluses.

Forecasts

Deteriorating current situation of the Estonian economy and a global economic slowdown caused a profound decline in economic growth rate expectations for Estonia in 2009 and 2010. April and May forecasts indicate that GDP in Estonia may shrink in 2009 by as much as 10%. It is estimated that GDP growth will be negative also in 2010, and recovery is possible not earlier than after 2 years. A decline in real GDP in Estonia in the coming years is estimated to be mainly a result of a decline in domestic demand – both as regards consumption and investments.

Weakening domestic demand is named the main reason for a decline in inflation in 2009 and 2010 to below 1% y/y (for 2010, the IMF even forecasts deflation). Therefore, Estonia – a country with one of the highest inflation rates in the region – may become the country of the lowest price growth rate.

Forecasts also show that the situation regarding the balance on the current account improved significantly, leading to one of the lowest level in the region also for this indicator.

Table 4.4
Forecasts of main indicators

	KE	IMF	Consensus Economics	EP
	05.2009 (11.2008)	04.2009 (10.2008)	04.2009 (11.2008)	04.2009 (10.2008)
GDP, in %, y/y				
2008	-3,6 (-1,3)	-3,6 (-1,5)	-3,6 (-1,8)	-3,6 (-1,8)
2009	-10,3 (-1,2)	-10,0 (0,5)	-9,2 (-1,2)	-12,3 (-2,1)
2010	-0,8 (2,0)	-1,0 (5,4)	-1,4	0,2
Inflation, in %, y/y				
2008	10,6 (10,6)	10,4 (10,2)	10,4 (10,7)	10,4 (10,7)
2009	0,6 (4,9)	0,8 (5,1)	0,6 (5,4)	-0,5 (4,8)
2010	0,5 (3,3)	-1,3 (3,0)	0,9	-2,9
Current account balance, in % of GDP				
2008	-9,1 (-12,1)	-9,2 (-10,8)		-9,2 (-9,1)
2009	-1,1 (-8,1)	-6,5 (-8,7)		2,7 (-4,8)
2010	-3,1 (-6,5)	-5,4 (-9,7)		-1,7

EP - Eesti Pank

LITHUANIA

Economic growth

For the major part of 2008, Lithuanian economy successfully resisted strong economic slowdown observed in other Baltic countries. Although GDP growth rate in 2008 slowed down significantly as compared to the previous year (3.1% vs. 8.9%), GDP growth rate in Lithuania was still positive, opposite to the situation in Estonia and Latvia. A decline in economic activity occurred not earlier than in the fourth quarter of 2008 when Lithuanian GDP fell by 2% y/y. However, preliminary estimates for the first quarter of 2009 indicate an acceleration of recession tendencies (according to preliminary data of the Lithuanian Statistical Office, GDP decreased in the first quarter of 2009 by as much as 10.9% y/y).

A decline in GDP growth in the first three quarters of 2008 resulted mainly form decreasing investment. At the same time, the share of individual consumption in economic growth, though slowing down, was still at a relatively high level[13].

In the fourth quarter of 2008, investment expenditures continued to fall considerably (-18.9% y/y), which combined with weakening consumption, led to a negative GDP growth. As in the case of other Baltic countries, a weakening domestic demand caused a decline in imports growth, and consequently, the share of net exports in economic growth increased significantly (in the fourth quarter of 2008, it was positive for the first time since 2004). Lithuanian economy is characterised by the fact that exports growth did not slow down even in the fourth quarter of 2008, opposite to other countries of the region.

Figure 5.1

Contribution to GDP growth (in pp, y/y)

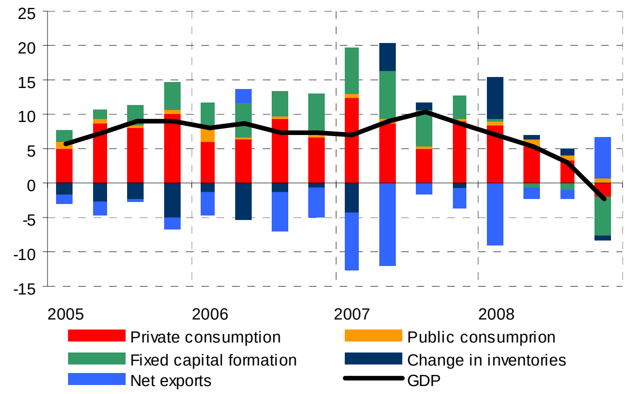


Table 5.1

GDP and its components growth rate (in %, y/y)

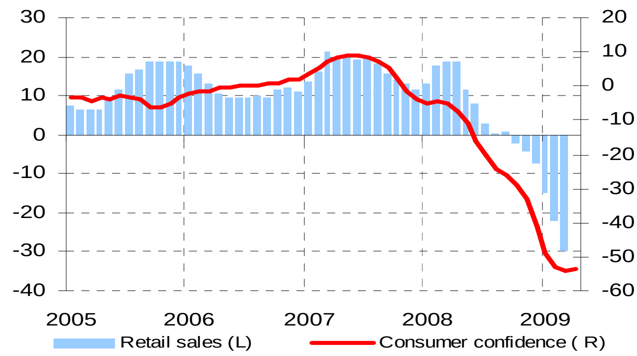
	2007	2008	Q3 2008	Q4 2008	Q1 2009
GDP	**8,9**	**3,0**	**2,9**	**-2,2**	**-10,9**
Private consumption	12,3	5,9	4,7	-2,9	
Public consumption	3,3	4,1	4,9	2,9	
Fixed capital formation	20,8	-6,4	-3,3	-18,9	
Exports	4,3	11,5	11,3	11,0	
Imports	11,6	10,3	10,9	0,3	

source: Ecowin Economic

Deterioration of indices describing consumer and business sentiment in Lithuania was visible already in 2008, and in 2009 these indices fell to their lowest levels since 1998. Deterioration of consumer sentiment was influenced mainly by the worsening country's general economic situation. With respect to business representatives, the most significant influence was exerted by the current and expected volume of orders, including export orders, and a decline in production in the coming months.

Figure 5.2

Retail sales (in %, y/y) and consumer confidence index



source: Ecowin Economic

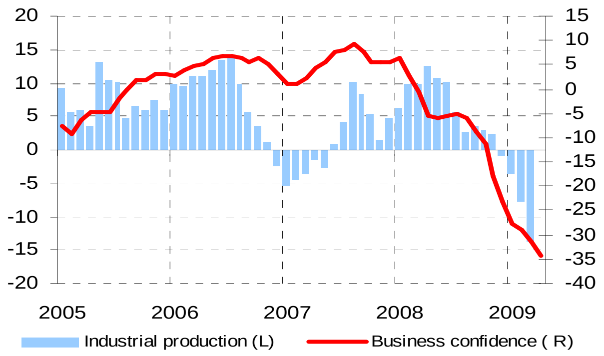
Data on retail sales and industrial production confirms these tendencies. A strengthening downward trend in both these categories has

[13] A relatively lower decline in individual consumption growth in Lithuania as compared to neighbouring Baltic countries may be explained by a more balanced increase in previous years which was not based to such extent on credits.

been observed since the second quarter of the previous year. A decline in industrial production at the end of 2008 was not as deep as in other Baltic countries (5% y/y in the fourth quarter of 2008), but a decline in retail sales (the first one since 1998), which amounted to almost 10% y/y in December, was the highest decline in history. At the beginning of 2009, a decline in these categories accelerated considerably. In March this year, retail sales fell by over 30% y/y (the highest fall in the region) and a decline in industrial production – by 18%.

Figure 5.3

Industrial production (in %, y/y) and business confidence index



source: Ecowin Economic

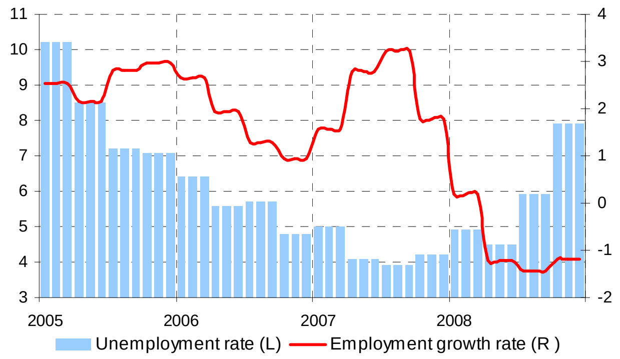
Labour market

Despite the fact that the condition of the Lithuanian economy in 2008 was the best one in the Baltic region, the situation on the labour market was very similar to what was observed in Estonia and Latvia. Unemployment rate increased already at the beginning of 2008, and reached almost 8% in the fourth quarter of 2008 (as compared to 4% in mid-2007).

Employment growth was also gradually decreasing since mid-2007 when it exceeded 3% y/y, reaching a negative amount already in the second quarter of 2008 (-1.2% y/y in the second quarter of 2008). In 2008, employment fell most considerably in agriculture and construction, whereas in services it slightly increased and in industry remained unchanged.

Figure 5.4

Unemployment rate (in %) and employment growth rate (in %, y/y)



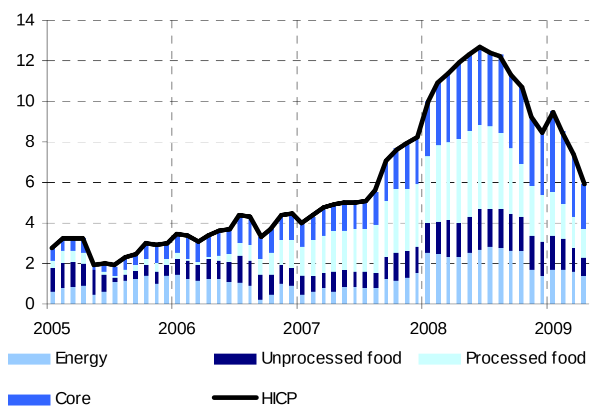
source: Ecowin Economic

Inflation and labour costs

Inflation in Lithuania reached its peak in June 2008 (12.6% y/y) and started to decrease since afterwards (to 5.9% y/y in April 2009). Similar to other countries in the region, a decrease in inflation was explained mainly by a falling growth in prices on global markets, i.e. food and energy markets. Core inflation in Lithuania decreased not earlier than in the fourth quarter of 2008 and to a lesser extent than in other Baltic countries which may be explained by still continuing positive growth in consumption expenditures.

Figure 5.5

HICP and its components (in pp, y/y)



source: Ecowin Economic

Table 5.2

HICP and its components (in pp, y/y)

	Q2 2008	Q3 2008	Q4 2008	Q1 2009	04 2009
HICP	**12,3**	**12,0**	**9,5**	**8,5**	**5,9**
Categories with largest contribution					
Housing	2,2	2,2	2,7	2,7	2,4
Food and non-alcoholic beverages	4,5	4,3	2,9	2,2	2,3
Health	0,6	0,5	0,6	1,2	1,3
Alcohol beverages and tobacco products	1,3	1,2	1,1	1,0	1,2
Restaurants and hotels	1,2	1,2	1,2	0,9	1,1

source: Ecowin Economic

In January 2009, inflation rose due to an increase in VAT rate (unified rate of 19% as compared to two previous rates of 15% and 18%) by 1 p.p.. However, already in the following months HICP growth slowed down (to 7.4% in March 2009), in the first instance due to a decline in food prices.

Despite a deterioration in the situation on the labour market observed already at the beginning of 2008, nominal salaries in the first half of the previous year still grew fast (growth rate was even higher than in 2007). This was mainly due to a high increase in salaries in the public sector which in 2008 amounted to over 20% y/y (as compared to 13% for the whole economy on average). Salaries growth decreased not earlier than in the fourth quarter of 2008.

An increase in salaries growth in the first three quarters of 2008 led to higher growth rate in labour unit costs. In the fourth quarter of 2008, its decline led to a decrease in ULC growth rate, however, it was still over the respective amount for 2007.

External imbalances

Current account deficit in Lithuania decreased not earlier than in the second half of 2008 from a record level observed in the first half of the year. After the first quarter of 2008, deficit on the current account reached 15.6% GDP (4Q moving average), and after the fourth quarter of 2008, it fell to 11.6% GDP[14]. It was almost completely due to reduced deficit in trade of goods.

Foreign trade turnover in Lithuania, opposite to the majority of the countries in the region, increased in 2008 as compared to the previous year, whereas exports growth significantly exceeded imports growth – a tendency opposite to the situation observed in previous years. The amount of Lithuanian imports decreased only in the fourth quarter of 2008 which resulted mainly from lower imports of fuels (due to a decline in prices on world markets). In geographical terms, a considerable decline was observed in growth of trade with EU-15 countries, and was negative for imports in the whole 2008. In January and February 2009, turnover in foreign trade fell considerably. Exports decreased by 20% and imports by as much as 40% which led to a strong reduction in foreign trade deficit.

A decline in a negative balance of trade with goods was accompanied by a decrease in deficit on the income account. At the same time, a positive balance on the services account decreased.

Figure 5.6

Current account balance and its components (in % of GDP, 4Q moving average)

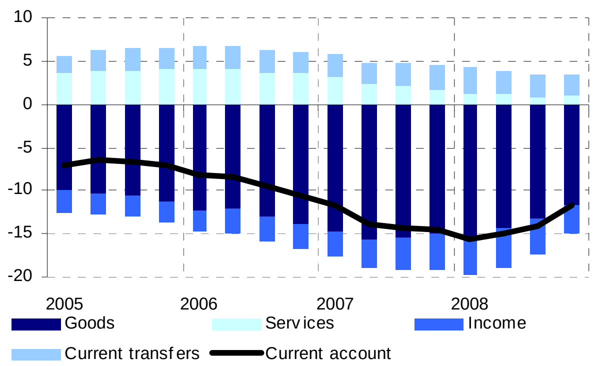


Table 5.3

Balance of payments (EUR mn)

	Q4 2007	Q1 2008	Q2 2008	Q3 2008	Q4 2008
Current account	-1067	-1333	-1389	-834	-643
Goods	-1167	-1308	-1082	-782	-668
Services	105	36	18	42	76
Income	-234	-280	-479	-316	-158
Current transfers	228	219	154	221	108
Capital account	19	132	62	25	35
Financial account	1070	1000	1319	804	645
FDI	134	90	277	310	88
Portfolio investment	520	-153	-96	-50	434
Other investment	985	324	1360	258	132

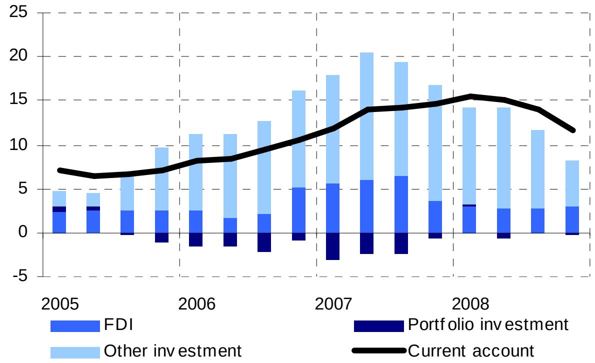
source: Eurostat

In 2008, surplus on the financial account increased. First of all, an inflow of other investments, mainly credits, was lower (decrease from 13.1% GDP in 2007 to 5.4% GDP in 2008) due to a fall in foreign trade credit volume and reduction of the credit action. An inflow of direct investments also decreased, however, to a lesser extent (from 3.6% to 3.1% GDP respectively). Despite a decline in deficit on the current account

[14] Deficit in individual quarters decreased from 18.7% GDP in Q1 to 3.8% GDP in Q4 2008.

an inflow of foreign capital in 2008 was not able to finance it.

Figure 3.7
Financial account balance and its components (in % of GDP, 4Q moving average)



source: Eurostat

Interest rates

In October 2008, market interest rates in Lithuania - as in other Central and Eastern European countries - increased rapidly reaching 9%. The upward trend in interest rates continued in the following months. In January 2009, 3-month VILIBOR reached almost 10%, however, it started to drop continuously in the following months due to stabilisation on world markets and a decline in interest rates, reaching 6.8 - 6.9% in April and May respectively.

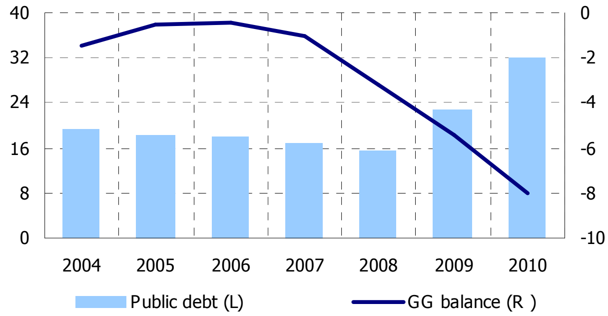
Similar to other Baltic countries, a strong appreciation of nominal and real exchange rate of the Lithuanian litas took place in 2008 and at the beginning of 2009. In March this year, NEER increased by 4.6% y/y and REER by 9.5% y/y.

Fiscal policy

Due to economic slowdown, caused by the economic crisis at Lithuania's largest business partners, the general government deficit in Lithuania increased in 2008 to 3.2% GDP from 1.0% GDP in 2007.

According to the Convergence Programme, the Lithuanian government forecasts a reduction in deficit in 2009 to 2.1% GDP, assuming a negative economic growth rate of 4.8% The spring fiscal notification contains a governmental forecast for deficit in this year amounting to 2.9% GDP, whereas the European Commission estimates deficit at 5.4% GDP.

Figure 5.8
General government balance and debt (in % of GDP)



source: Eurostat

The fiscal objective will be achieved by implementing a drastic anti-crisis package, i.e. the stabilisation plan for public finance comprising, inter alia: increase in basic VAT rate from 18% to 19% (including abolition of preferential rates), liquidation of all tax relieves and reducing salaries in the budget sector by 15%. These solutions was serious criticised by the Lithuanian society and, in turn, led to social dissatisfaction.

In February this year, the government presented a programme to support business which value is estimated at approx. 4% of GDP forecast. This programme is designed to assist entrepreneurs in solving their liquidity problems related to the repayment of credits, support the construction industry, facilitate legal labour conditions and accelerate the use of EU structural funds.

Funds to support the economy shall originate from the European Union budget, European Investment Bank loans and national budget.

In May this year, a novelisation of the budget act was adopted. The forecast for revenues was lowered by approx. 3.9% GDP and expenses by approx. 3% GDP (including salaries). After modifications, a budget deficit is planned at approx. 5% GDP.

Forecasts

A better situation of the Lithuanian economy in 2008 as compared to Latvia and Estonia led to some opinions suggesting a possible separation of this economy from tendencies observed in other Baltic countries. However, the crisis deterioration in the fourth quarter of 2008 as well as preliminary data for the first quarter of 2009 indicate that such scenario seems unlikely. GDP growth decreased significantly already in the first quarter this year, and forecasts for 2009 and 2010 indicate a long-term recession. According to forecasts, a decline in GDP in 2009 and 2010 may be as high as -11% and -5% respectively (as indicated by the spring European Commission forecast).

A falling domestic demand, which is the main reason for a decline in GDP, will also result in decreasing inflation, expected to continue a downward trend in the coming years.

According to forecasts, the current account deficit will also decrease, influenced mainly by improving foreign trade balance and income balance (reinvested profits are expected to fall in the coming quarters).

Table 5.4

Forecasts of main indicators

	EC	IMF	Consensus Economics	LB
	05.2009 (11.2008)	04.2009 (10.2008)	04.2009 (11.2008)	02.2009 (11.2008)
GDP, in %, y/y				
2008	3,0 (3,8)	3,0 (3,9)	3,0 (4,0)	3,0 (4,2)
2009	-11,0 (0,0)	-10,0 (0,7)	-8,9 (0,5)	-4,9 (1,2)
2010	-4,7 (-1,1)	-3,0 (2,6)	-2,8	-3,9
Inflation, in %, y/y				
2008	11,1 (11,9)	11,1 (11,3)	11,1 (11,2)	11,0 (11,6)
2009	3,6 (7,1)	5,1 (6,2)	4,8 (6,8)	5,8 (6,9)
2010	-0,4 (7,5)	0,6 (8,5)	2,0	4,8
Current account balance, in % of GDP				
2008	-12,2 (-13,8)	-11,6 (-14,9)		-13,0 (-13,0)
2009	-1,9 (-8,7)	-4,0 (-8,7)		-4,8 (-6,2)
2010	0,7 (-8,9)	-5,3 (-7,6)		-2,0

LB - Lietuvos bankas

LATVIA

Economic growth

GDP growth in Latvia in 2008 was at the lowest level of all Central and Eastern European countries. In 2008, Latvian economy shrank by 4.6%, mainly as a result of a deep fall in the fourth quarter by 10.3% y/y. Thus, a strong upward trend in the Latvian economy since 1997 ended. GDP forecasts for the first quarter of 2009 show that a decline in GDP is still most considerable in the whole region (-18.6% y/y).

A drop in economic growth resulted mainly from an increasing decline in consumption expenditures (started in the first quarter of 2007). Private consumption, which in 2006 grew by over 20% y/y, decreased at the end of 2008 by 20%. A significant decline was also observed in investment expenditures. A decline in domestic demand may be explained to a great extent by a decreasing credit action which fell from over 70% y/y in 2007 to approx. 5% y/y in February 2009.

At the same time, net exports, which had a negative impact on the economic growth rate in the recent years, increased significantly its contribution to GDP growth. However, this did not compensate for a decline in domestic demand, as a result of a relatively low openness of the Latvian economy. An increase in the contribution of net exports, related to a decline in domestic demand, resulted from a considerable decline in imports, whereas exports growth rate decreased more slowly.

Figure 6.1

Contribution to GDP growth (in pp, y/y)

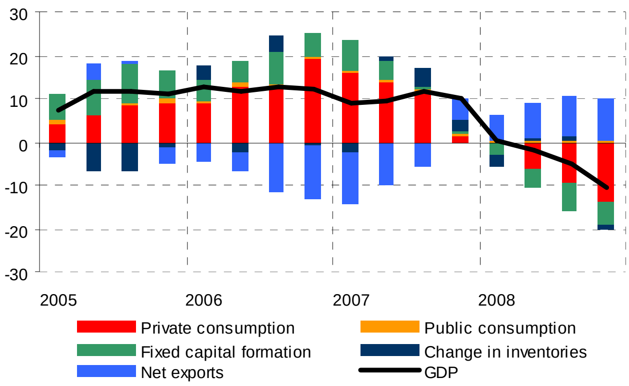


Table 6.1

GDP and its components growth rate (in %, y/y)

	2007	2008	Q2 2008	Q3 2008	Q4 2008
GDP	**10,0**	**-4,6**	**-5,2**	**-10,3**	**-18,6**
Private consumption	14,8	-11,1	-13,4	-20,1	
Public consumption	3,7	1,5	0,1	0,9	
Fixed capital formation	7,5	-13,2	-16,9	-15,0	
Exports	10,0	-1,3	-2,1	-6,1	
Imports	14,7	-13,6	-15,1	-20,7	

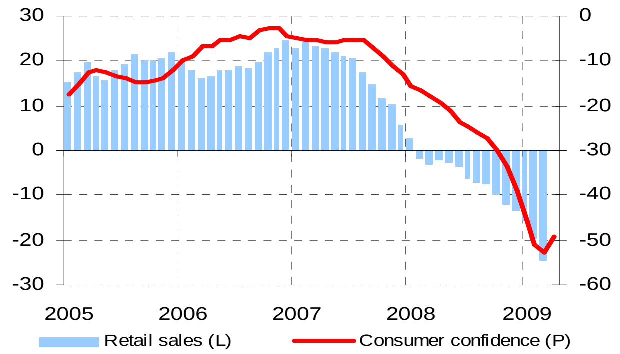
source: Ecowin Economic

A decline in industrial production, observed as early as in 2008, deepened during the year, and reached almost 24% y/y in March 2009. The most significant decrease was found in production of textiles (by 59% y/y) and vehicles (by 53% y/y). This was accompanied by a permanent decline in business confidence indices which were at their historical lowest levels in 2008. Production, orders and employment sub-indices decreased considerably.

Consumer confidence indices decreased even more significantly (though a slight improvement was observed in March this year). First of all, consumers have a very unfavourable opinion on their current and future financial situation which is probably related to a limitation of the credit action, negative signals on the labour market and a deterioration of the country's economic situation. This was reflected in record declines in retail sales in 2008/2009. In February 2009, it decreased by almost one fourth as compared to the previous year.

Figure 6.2

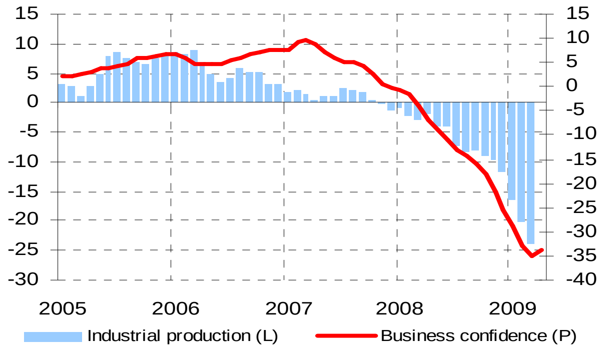
Retail sales (in %, y/y) and consumer confidence index



source: Ecowin Economic

Figure 6.3

Industrial production (in %, y/y) and business confidence index



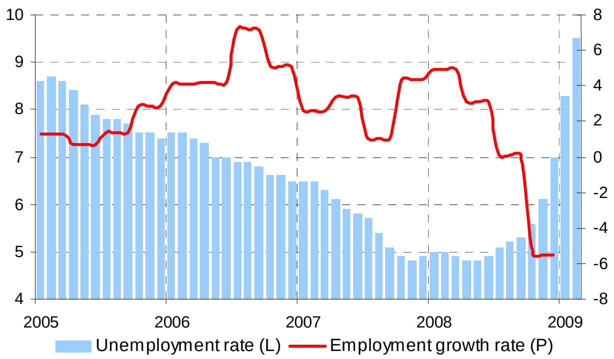
source: Ecowin Economic

Labour market

The situation on the Latvian labour market worsened dramatically since the second half of 2008. In this period, unemployment rate increased from 4.8% in May 2008 to 9.5% in February 2009. In the fourth quarter of 2008, the number of employees decreased as well. Employment, which was on the increase since 2001, fell to 5.5% y/y (4.1% q/q). in the fourth quarter of 2008. The largest decline in employment was found in financial intermediation sector (-21% y/y), gas, water and electricity supplies (-19%) and construction (-13%).

Figure 6.4

Unemployment rate (in %) and employment growth rate (in %, y/y)



source: Ecowin Economic

Inflation and labour costs

Due to a significant decline in inflation in the second half of 2008 and in the first months of 2009, Latvia ceased to be a country with the highest inflation rate in the region. Annual HICP growth amounted to 5.9% in April 2009 (6.5% in Romania).

As compared to May 2008, when inflation reached its peak (17.7%), growth rate in almost all price categories slowed down. A decline in growth of food prices, in particular of processed food, as well as of energy prices, were main factors behind a decline in inflation. In mid-2008, annual growth rate of these price categories still exceeded 30%, but already in February this year, they fell by over 50%, which was related mainly to worldwide tendencies on the food and energy raw materials markets. A decline in consumption demand also led to a decrease in core inflation, which fell from 10% y/y to 5.8% y/y between the mid-2008 and March 2009.

Figure 6.5

HICP and its components (in pp, y/y)

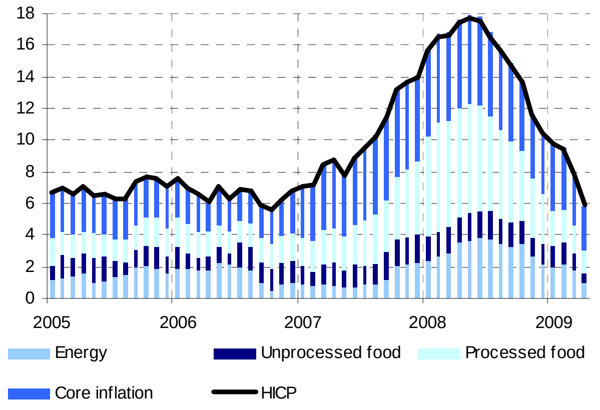


Table 6.2

HICP and its components (in pp, y/y)

	Q2 2008	Q3 2008	Q4 2008	Q1 2009	04 2009
HICP	**17,5**	**15,6**	**11,9**	**9,0**	**5,9**
Categories with largest contribution					
Housing	3,8	3,4	3,7	3,9	2,1
Alcohol beverages and tobacco products	5,0	4,6	2,9	2,0	1,6
Health	3,2	2,2	2,0	1,3	1,1
Food and non-alcoholic beverages	0,6	0,6	0,5	0,7	0,7
Recreation and culture	0,5	0,5	0,5	0,5	0,4

source: Ecowin Economic

A growth in nominal wages also slowed down in the second half of 2008. In the fourth quarter of 2008, it amounted to 12.1% as compared to over 30% a year ago.[15] However, it was still one of the highest in the region (except for Bulgaria and Romania).

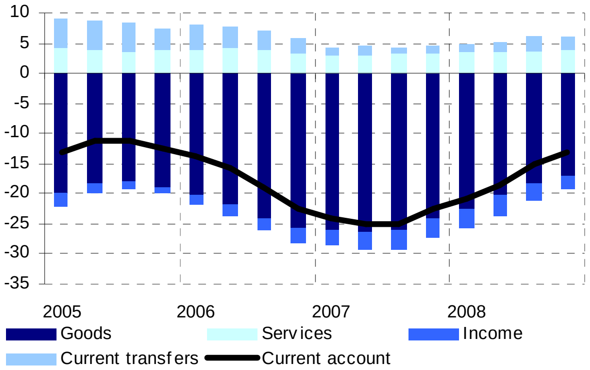
A slower growth in wages and in employment in 2008 led to a slower growth in unit labour costs.

[15] Growth in salaries in 2009 is expected to slow down further, in particular if the saving package, assuming reductions in salaries in the public sector by as much as 20%, is implemented.

External imbalances

Current account deficit, which reached as much as 25% GDP in mid-2007, decreased to 13% GDP in 2008. A decline in imports of goods, resulting from a weak domestic demand, was the main factor leading to a decrease in deficit on the current account. In 2008, income deficit also decreased, whereas surplus in trade of services increased.

Figure 6.6
Current account balance and its components (in % of GDP, 4Q moving average)



The value of Latvian foreign trade in 2008 and at the beginning of 2009 decreased significantly. This was related both to exports (-30% y/y in February 2009), and in particular to imports (-40%). The biggest fall in exports was observed in the following categories of products: wooden products and motor vehicles. At the same time, a weakening domestic demand contributed to a decline in imports, in particular of cars (by 68% y/y) and machines (by 55% y/y).

In 2008, surplus on the financial account decreased. Net inflow of direct investments decreased from 6.7% GDP in 2007 to 4.2% GDP in 2008 as a result of a smaller inflow of reinvested profits. An inflow of other investments, which were the basic source of financing for deficit on the current account in Latvia since 2005, decreased significantly. In 2007, it amounted to almost 20% GDP, and decreased to 7.5% in 2008. A decline in the inflow of other investments was mainly due to: a decrease in foreign trade volume (smaller inflow of trade credits) and reduction in the credit action (smaller inflow of credits to the banking sector).

Figure 6.7
Financial account balance and its components (in % of GDP, 4Q moving average)

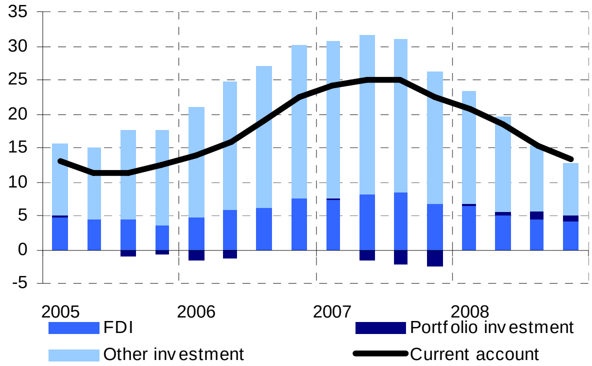


Table 6.3
Balance of payments (EUR mn)

	Q4 2007	Q1 2008	Q2 2008	Q3 2008	Q4 2008
Current account	-1102	-901	-840	-695	-618
Goods	-1238	-999	-989	-1015	-916
Services	182	170	248	248	246
Income	-151	-162	-287	-97	-13
Current transfers	105	90	188	169	66
Capital account	130	31	21	28	66
Financial account	694	1067	719	754	777
Direct investments	138	370	281	226	106
Portfolio investments	0	0	0	0	0
Other investments	602	483	638	539	100

source: Ecowin Economic

Insufficient inflow of foreign capital led to destabilisation of the financial sector in Latvia. This made it necessary to apply for aid to the International Monetary Fund, which decided in December 2008 to grant a credit amounting to EUR billion 1.7 to Latvia. The programme was also supported by the European Union (EUR 3.1 billion), World Bank (EUR 0.4 billion) as well as Scandinavian countries, Poland, Czech Republic and Estonia (in total EUR 2.3 billion). In the coming three years, Latvia shall receive EUR 7.5 billion as aid to stabilise its economy.

Interest rates

Latvian inter-banking market was affected in the fourth quarter of 2008 by a significant increase in interest rates due to turmoil on world financial markets. 3-month RIGIBOR rate, which amounted to approx. 7% in mid-2008, increased to over 13% in December. In 2009, due to lower aversion to risk and a decline in interest rates worldwide, including Latvia, it was also possible to notice a decline in interest rates on the inter-banking market to 10% in February and March, but the refusal to pay out the first tranche of the credit by the IMF caused their further increase by approx. 200 b.p. in April and May.

Real interest rates in Latvia are still very low, however, due to a decline in inflation, they are no longer negative which was the case in the years 2004 -2008.

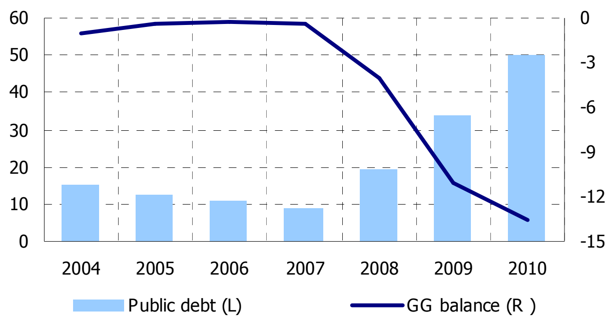
Both a nominal (NEER) and in particular real (REER) effective exchange rate of Latvian lat increased in 2008 and at the beginning of 2009, which further reduced competitiveness of Latvian economy on external markets. In March 2009, NEER strengthened by 2.5% y/y, and REER by 9.1% y/y.

Fiscal policy

After three years of balanced public finance, Latvia was affected by high deficit (4.0% GDP) in 2008 due to economic collapse. On one hand, it was a result of a decline in tax revenues, and on the other hand – a consequence of a rapid increase in public expenditures, mainly for social benefits.

This year, the financial situation in Latvia will further deteriorate, which is confirmed by deficit of the public finance sector of 11.1% GDP as per forecast by the European Commission.

Figure 6.8
General government balance and debt (in % of GDP)



source: Eurostat

In order to stabilise the Latvian economy, an agreement between the Latvian government, European Commission, IMF and Scandinavian countries, providing Latvia with financial support amounting to EUR 7.5 billion, was signed in December 2008. Creditors indicated that the Latvian government has to prepare a revised budget for 2009, including additional actions to limit public expenditures.

A novelised budget shall be adopted in April this year. The European Commission expects from Latvia to keep deficit in 2009 below 5% GDP and to reduce it further to 3% GDP in 2010.

Forecasts

Forecasts show that in 2009 and 2010 Latvia will be the country most seriously affected by the world crisis. GDP is expected to fall by as much as 14% in 2009 and further 2-4% in 2010. A decline in domestic demand, in particular individual consumption, will remain the main reason for recession. In the recent couple of months, forecasts for real GDP growth in Latvia worsened significantly.

Similar to Estonia, a further strong decline in inflation is also expected to take place in 2009 and 2010 to such an extent that deflation is expected in 2010.

An improving balance of trade with goods is expected to be the main reason behind a fall in the current account deficit in the following quarters.

Table 6.4
Forecasts of main indicators

	KE	IMF	Consensus Economics	LB
	05.2009 (11.2008)	04.2009 (10.2008)	04.2009 (11.2008)	02.2009 (10.2008)
GDP, in %, y/y				
2008	-4,6 (-0,8)	-4,6 (-0,9)	-4,6 (-1,0)	-4,6 (-0,5)
2009	-13,1 (-2,7)	-12,0 (-2,2)	-13,6 (-3,0)	-12,0 (-1,0)
2010	-3,2 (1,0)	-2,0 (1,1)	-3,8	
Inflation, in %, y/y				
2008	15,3 (15,7)	15,3 (15,9)	15,3 (15,6)	15,5 (15,9)
2009	4,6 (8,2)	3,3 (10,6)	3,7 (6,5)	2,5-3,5 (8,6)
2010	-0,7 (4,7)	-3,5 (6,7)	-0,1	
Current account balance, in % of GDP				
2008	-13,6 (-14,5)	-13,2 (-15,1)		-13,2 (-15,6)
2009	-1,5 (-8,7)	-6,7 (-8,3)		-6,1 (-9,6)
2010	-1,9 (-6,2)	-5,5 (-5,9)		-3,2

LB - Latvijas Banka

Box 1

Aid packages of the International Monetary Fund for Central and Eastern European countries

The world financial crisis hit the economies of Central and Eastern Europe to a different degree. Economies with weak foundations (struggling with internal problems already before the crisis appeared) were hit more severely than others, and even faced economic collapse which made them apply for aid to the International Monetary Fund and other international organisations.

The first country in Central and Eastern Europe which applied for the IMF loan was **Hungary**. Following the bankruptcy of an investment bank Lehman Brothers aversion to risk increased worldwide, in particular in Central and Eastern European countries, which caused an outflow of foreign capital from the equity and bonds market. In the case of Hungary, this led to an increase in yield on bonds and a significant depreciation of Hungarian forint.

At the beginning of November 2008, the IMF, EU and World Bank decided to provide Hungary with a loan amounting to EUR 20 billion. This aid had two objectives: to improve stability of the public finance sector and liquidity of the financial sector. At the same time, the IMF persuaded Hungarian authorities to prepare the recovery plan for the public finance system (reductions of expenditures). It comprised freezing salaries in the public sector, delayed indexation of benefits and pensions as well as reduction of expenditures of individual ministries.

The information on granting aid to Hungary and the payment of the first credit tranche in November (EUR 4.9 billion from the IMF) and December (EUR 2 billion) in 2008 led to a temporary improvement of the situation on financial markets (Hungarian forint appreciated against October minimum levels, yield on bonds decreased and main indices on equity markets increased). Aid granted to Hungary eased financial crisis effects in November and at the beginning of December, however it did not eliminate itscauses. At the end of 2008 and at the beginning of 2009, effects of the global financial crisis strengthened again. At the end of March 2009, the IMF decided to pay out the second credit tranche in the amount of EUR 2.5 billion.

On 19 December 2008, the IMF decided to provide **Latvia,** facing the most severe economic crisis in the region, with a loan of EUR 1.7 billion (together with other funds provided by other creditors, total aid amount reached EUR 7.5 billion). The main objective of the programme was to stabilise the Latvian economy by supporting the financial sector and regaining confidence of depositaries. At the same time, the IMF obliged to Latvia to recover the public finance system, an in particular deficit of the public finance sector should not exceed 5% GDP in 2009 (as compared to 12% forecast in the case of no actions undertaken). The saving package comprised, inter alia, a reduction in salaries in the public sector and an increase in basic VAT rate from 18% to 21%.

Announcements on savings in the public finance sector and a deteriorating economic situation in Latvia led to growing concerns within the country, and consequently, to the collapse of the government in February 2009.

According to preliminary arrangements, the first credit tranche (EUR 200 million) was decided to be paid out until the end of March 2009. The IMF decided to freeze it because Latvian authorities did not take adjusting actions under previously agreed reforms of public finance. The decision to withdraw from granting the first credit tranche resulted in growing anxiety on financial markets (CDS amounts on Latvian bonds increased on 1 April by over 60 bps). This decision as well as worsening economic outlook for Latvia also influenced a decline in rating of governmental bonds by Moody's i Fitch agencies in April 2009.[16] Another credit tranche (EUR 1.7 billion from the EU) is expected to be paid in June this year, and it seems that the European Commission will not be so restrictive as the IMF.

[16] Earlier, in February 2009, Latvian bonds were also downgraded in the S&P rating.

A constantly deteriorating situation in Latvia and a withdrawal from the payment of the first loan tranche made the government renew negotiations on the conditions of aid to be granted by the IMF. It seems that reaching budget deficit of 5% GDP is not realistic and therefore the Latvian government attempts to persuade the IMF to increase this limit to 8% GDP[17], which would be more realistic and would make it possible to fully use the stabilising package.

Another new EU member state applying for the IMF aid was **Romania**. The IMF, European Union, World Bank and European Bank for Reconstruction and Development decided to provide Romania with a loan of total EUR 20 billion. The main objective of this plan was to provide additional capital to domestic banks and to increase liquidity on the financial market. In addition, these funds should help reach the inflation target, and thus help Romania join the Eurozone. The first credit tranche shall be paid out at the beginning of July 2009.

The IMF aid was also applied for other Central and Eastern European countries which are not EU member states such as Ukraine, Belarus and Serbia (initially USD 520 million in January 2009, later changed to EUR 3 billion in March this year).

The value of aid packages provided by the IMF and other institutions to Central and Eastern European countries.

	Total	IMF	EU	World Bank	Other
Hungary	20.0	12.5	6.5	1.0	
Latvia	7.5	1.7	3.1	0.4	1.8*
Romania	20.0	13.0	5.0	1.0	1.0**
Other Central and Eastern European countries which are not EU member states					
Ukraine	10.4	10.4			
Belarus	1.8	1.8			
Serbia	3.0	3.0			

* Scandinavian countries, Poland, Czech Republic, Estonia
** EBRD

[17] Previous assumptions were adopted in December 2008, when GDP growth was estimated at approx. -5%. In April, outlook significantly deteriorated and forecasts now estimate a decline in GDP by 12-14%.

ROMANIA

Economic growth

During the first three quarters of 2008, Romania was the most rapidly developing country in the region (GDP rose by 9.0% y/y in this period). However, in the fourth quarter of the previous year, GDP growth decreased significantly (to 2.9%). Such considerable decline in GDP growth was influenced mainly by consumption expenditures which previously contributed to the acceleration of economic growth. A decline in household consumption for the first time since 2000 resulted from a strong reduction of the credit action (related to a high share of Western European banks in the Romanian financial sector which were no longer able to provide their Romanian daughter-companies with funds at a previous level). Furthermore, a strong depreciation of the Romanian currency led to an increase in household debt denominated in foreign currencies. Under such circumstances, the main factor supporting GDP growth in the fourth quarter of 2008 was an increase in net exports. This was caused by a strong decline in imports (by 10.2% as compared to an increase by 27.7% in the first three quarters this year), related to a decline in consumption demand, whereas exports showed a slight downward tendency (by 1.6% as compared to an increase by 25.8% in the Q1-Q3 2008). At the end of 2008, investment activity also decreased significantly. In the fourth quarter of this year, investment expenditures increased by mere 2.8% (as compared to 27.7% in the first three quarters of 2008).

GDP estimates for the first quarter indicate increasingly severe recession. Its growth fell by as much as -6.4% y/y (lowest level except for Baltic countries).

Figure 7.1

Contribution to GDP growth (in pp, y/y)

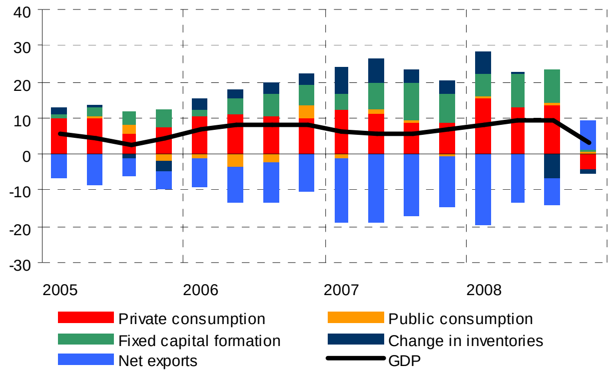


Table 7.1

GDP and its components growth rate (in %, y/y)

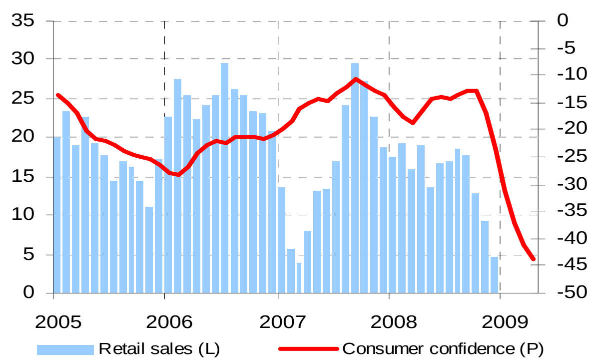
	2007	2008	Q3 2008	Q4 2008	Q1 2009
GDP	**6,2**	**7,1**	**9,2**	**2,9**	**-6,4**
Private consumption	11,7	9,2	16,1	-4,7	
Public consumption	1,2	3,1	4,2	3,9	
Fixed capital formation	29,0	19,3	24,3	2,8	
Exports	7,9	19,4	22,0	1,6	
Imports	27,2	17,5	20,7	-10,2	

source: Ecowin Economic

At the beginning of 2009, a downward trend in retail sales, initiated at the end of the previous year, strengthened. Between January and February 2009, retail sales fell by 6.1% (including February decline by 7.9%), as a result of not only more restrictive credit conditions and a reduction in salaries growth, but also due to an increase in prices of imported goods – in particular of durable goods (sales in the first two months of this year decreased by 24.1% y/y). A decrease in retail sales is accompanied by a strong fall in consumer confidence. The European Commission consumer confidence indicator declined in April this year to its historical lowest level (i.e. since 2001). Romanian customers have a particularly unfavourable perception of the current situation of the national economy and its outlook for the following 12 months. Estimates of future household situation fell to their low levels, mainly as a result of an expected increase in unemployment (this sub-indicator is almost four times higher than six months ago).

Figure 7.2

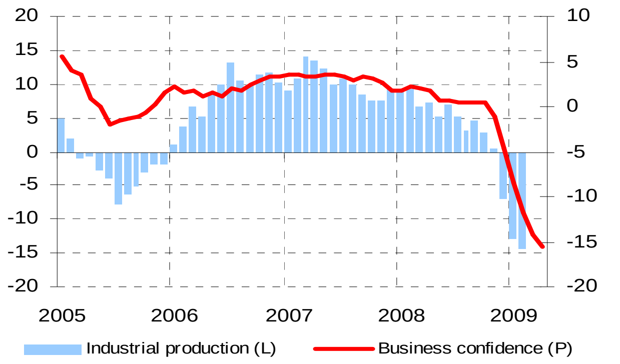
Retail sales (in %, y/y) and consumer confidence index



source: Ecowin Economic

A deepening decline in external demand at the beginning of 2009 led to acceleration of the downward trend in industrial production observed since November of the previous year. Between January and February 2009, it decreased by 15.4% y/y. The factor which had the strongest impact on this was a decrease in production of metallurgic industry (by over 50% as compared to a relevant period of the previous year) and of automotive sector (decline by almost 40%). At the same time, a decline in orders for the industry (by 26.1% y/y between January and February 2009) may indicate a continuation of the falling trend in production in the following months. It also takes into account a drop in business confidence, influenced by both a decreasing production level and anxiety related to future sales prices.

Figure 7.3
Industrial production (in %, y/y) and business confidence index

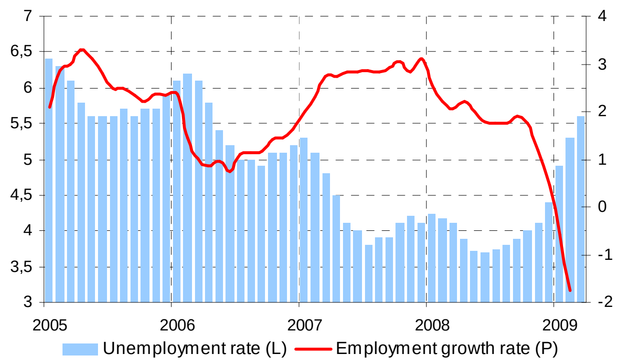


source: Ecowin Economic

Labour market

High growth in economic activity in Romania resulted in the fact that the country's unemployment rate in mid-2008 fell to its lowest level since 1992 (3.8%). However, a deteriorating situation in external environment caused a gradual increase in unemployment in the following months up to 5.6% in March 2009 (highest level in the last three years), additionally influenced by return of work emigrants from other European Union countries.

Figure 7.4
Unemployment rate (in %) and employment growth rate (in %, y/y)



source: Ecowin Economic

Inflation and labour costs

Inflation in Romania was on the decrease in the whole second half of 2008, falling from 9.1% in July 2008 to 6.4% in December 2008. However, in January this year, an increase in regulated prices (raising excise tax on fuels and tobacco products and an increase in prices of phone services and refunded medicaments) resulted in stopping the downward trend, and in April 2009 HICP growth remained at a similar level (6.5%). Similar to the second half of the previous year, growth in food prices decreased also at the beginning of 2009, as a result of high crops in 2008 and a favourable base effect.

Despite a decline in general inflation indicator at the end of 2008 and at the beginning of 2009, an increase in core inflation was observed. In addition to salaries growth, it also takes into account an influence of depreciation of Romanian currency on both imported goods and prices of services – frequently valued in euro.

Figure 7.5
HICP and its components (in pp, y/y)

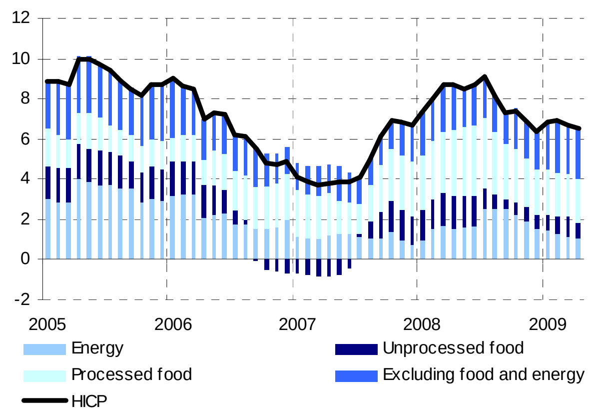


Table 7.2
HICP and its components (in pp, y/y)

	Q2 2008	Q3 2008	Q4 2008	Q1 2009	04 2009
HICP	**8,6**	**8,2**	**6,9**	**6,8**	**6,5**
Categories with largest contribution					
Food and non-alcoholic beverages	4,4	3,3	2,4	2,2	1,8
Housing	1,5	2,2	2,2	2,0	1,7
Alcohol beverages and tobacco products	0,6	0,6	0,7	0,9	1,3
Communication	0,6	0,5	0,3	0,6	0,6
Recreation and culture	0,1	0,1	0,1	0,2	0,2

source: Ecowin Economic

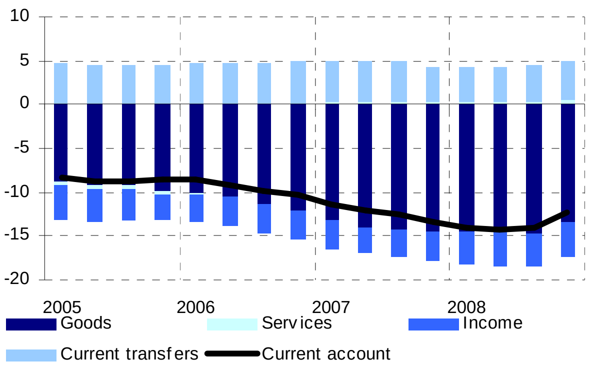
High core inflation is also influenced by a considerable increase in wages. In March 2009, salaries in the Romanian economy increased by 17.6% y/y. In the following months, salaries growth should slow down significantly which will be influenced by freezing wages in the public sector.

External imbalances

Due to high growth in consumption expenditures, stimulated by considerable availability of credits, a high growth in employment and an expansive fiscal policy, Romanian economy was characterised in the recent years by high deficit on the current account. This was caused mainly by deficit in trade of goods and a negative income balance, resulting inter alia from a large inflow of direct investments. In the fourth quarter this year, deficit in trade fell to 10.3% GDP from 13.0% in the third quarter 2008), caused by weakening of domestic demand and a strong appreciation of the Romanian currency. A factor which influenced a reduction in deficit on the current account was a positive balance of transfers, though it was marked by a downward trend in the recent time.

Figure 7.6

Current account balance and its components (in % of GDP, 4Q moving average)



source: Ecowin Economic

The main sources of financing for deficit on the current account in the second half of the previous year were direct investments, which stabilised in 2008 at 6.8% GDP, and other investments, including mainly reinvested profits, which demonstrated a downward trend in the second half of the previous year (from 7.2% GDP in the first quarter to 5.5% GDP in the fourth quarter of 2008). A fall in other investments net inflow resulted from a relatively high involvement of foreign companies in the Romanian banking sector which belonged to the first companies endangered by the crisis, and consequently limited availability of funds for their subsidiaries in Romania. Furthermore, the fourth quarter of 2008 was marked by an outflow of portfolio investments amounting to 2.2% of GDP.

Figure 7.7

Financial account balance and its components (in % of GDP, 4Q moving average)

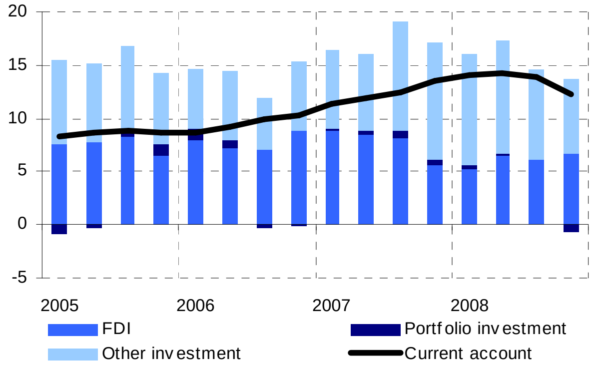


Table 7.3

Balance of payments (EUR mn)

	Q4 2007	Q1 2008	Q2 2008	Q3 2008	Q4 2008
Current account	-5606	-3763	-4902	-4307	-3906
Goods	-5595	-4058	-4916	-4989	-4237
Services	-51	168	222	-2	448
Income	-1048	-1262	-1552	-1365	-1352
Current transfers	369	141	167	51	252
Capital account	1087	1388	1345	2050	1235
Financial account	4777	3632	6473	4304	3184
Direct investments	1314	1952	3231	2117	1936
Portfolio investments	-104	210	-93	-171	-877
Other investments	3918	1777	3259	2459	2040

source: Ecowin Economic

Interest rates and foreign exchange rate

High inflation and symptoms of economic overheating were main reasons for an increase in interest rates by the National Bank of Romania (NBR) in the period from the beginning of 2008 to August 2008 by 225 bps in total. At the same time, since the beginning of this year Romanian monetary policy has been determined by two factors. The first one is the fact that any further depreciation of the Romanian leu may even strengthen inflation which speaks in favour of maintaining restrictive monetary policy. The second factor is an increasing risk of recession which favours easing of the monetary policy. Therefore, since the beginning of this year, the NBR has decided on two occasions (in February and May this year) to reduce interest rates (in total by 75 bps to 9.5% which indicates that the NBR identified recession as the main threat to the Romanian economy. It is expected that NBR will further reduce interest rates at its further meetings (which is indicated by an observed downward trend in market interest rates).

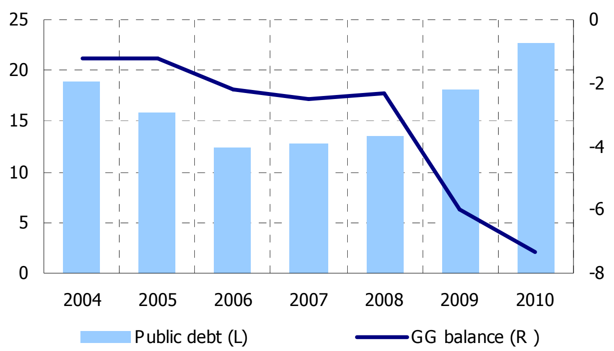
In the second half of 2008, the leu demonstrated a tendency for a gradual depreciation against the euro (by 6.8%) and the U.S. dollar (by 23.4%). This depreciation even accelerated in the first quarter of this year (16.9% against the euro and 39.6% against the U.S. dollar). At the same time, in April, average monthly exchange rate of the leu remained stable at below 4.2 EUR/RON and 3.2 USD/RON.

Fiscal policy

In 2008, Romania had the highest deficit of the public finance sector among all Central and Eastern European countries. It amounted to 5.4% GDP, i.e. twice as much as in 2007 and much higher than in the plan for 2008 (3.3% GDP). This resulted from lower revenues and higher public expenditures (inter alia due to additional expenditures on parliamentary elections).

Figure 7.8

General government balance and debt (in % of GDP)



source: Eurostat

According to the European Commission forecasts (from May 2009), Romanian public finance deficit shall amount this year to approx. 5.1% GDP. This data is in contrast with preliminary estimates of the Romanian government, which assumed a deficit of 2.9% GDP. At present, this assumption changed to 5.1% GDP in 2009. Due to an estimated strong slowdown in a growth rate of investments, leading to the weakening of economic growth in 2009, a reduction in deficit to the level forecast by the government seems very unlikely. Newly appointed Romanian government assumes namely a significant increase in budget revenues, which even taking into account a declared reduction in budget expenditures, may turn out to be insufficient. Most significant tasks related to public expenditures, which shall help meet the fiscal objective assumed by the government, comprise inter alia:

- reducing current expenditures for the purchase of goods and services by 15%,
- limiting subsidies by 21%,
- reducing expenditures on wages by decreasing bonuses and overtime premium.

Due to high uncertainty of the economic situation development in Romania, the government provide, in March this year, the Chamber of Deputies of the Romanian parliament with a package of anti-crisis activities consisting inter alia in:

- increasing budget expenditures on infrastructural investments in order to maintain and create new jobs,
- broadening the program of car park modernisation by increasing premium amount for scrapping an old car and increasing the number of cars covered by this programme
- facilitating procedures for absorption of European funds (in 2007 and 2008, Romania used mere 6% of provided EU funds) and acceleration of public procurement procedures,
- implementing a minimum pension,
- covering 90% of reference price of medicaments covered by a refund for pensioners, if their amount does not exceed double amount of a minimum pension,
- exempting an employer from the obligation to pay insurance contributions and employees from paying income tax during the so-called technical unemployment (lasting for no longer than 3 months),
- extending the period of unemployment benefit eligibility by 3 months.
- abolishing a tax on reinvested profits,
- stimulating investments by providing state aid, in particular for companies operating in strategic branches of the Romanian economy,
- keeping a flat PIT and CIT rate at 16%.

According to Romanian governmental sources, Romania used an external aid to fight with the crisis effects. The loan by the IMF, World Bank and EBRD will probably amount to approx. EUR 20 billion. An agreement with the IMF, which will provide as much as EUR 13 billion, would improve the fiscal situation and assure relative macroeconomic stability in Romania..

Forecasts

A slowdown in GDP in the fourth quarter 2008 indicates the end of the period of a rapid economic growth in Romania. An increase in unemployment, lower credit availability as well as consumer and entrepreneur pessimism will surely influence consumption and investments which were so far main factors supporting economic growth. At the same time, due to high fiscal deficit, the government has limited possibilities for fiscal stimulation of domestic demand. However, it should be noticed that weak consumption and depreciation of the Romanian currency may positively influence the share of net exports in this growth. This potential impact is, however, limited due to recession in the euro zone and in other business partners of Romania. Taking into account all above factors, the majority of forecasts assume a negative economic growth.

At the same time, Romanian government expects that the aid provided by the International Monetary Fund will weaken recession tendencies in Romania.

A deteriorating situation on the labour market and deepening recession will lead to a considerable decline in inflation in 2009. However, it should be borne in mind that a possible further depreciation of the Romanian currency and higher than expected fiscal deficit may partially eliminate the effect of economic slowdown.

Table 7.4

Forecasts of main indicators

	KE	IMF	Consensus Economics	BNR
	05.2009 (11.2008)	04.2009 (10.2008)	04.2009 (11.2008)	05.2009 (11.2008)
GDP, in %, y/y				
2008	7,1 (8,5)	7,1 (8,6)	7,1 (8,1)	
2009	-4,0 (4,7)	-4,1 (4,8)	-2,3 (3,4)	
2010	0,0 (5,0)	0,0 (5,3)	1,1	
Inflation, in %, y/y				
2008	7,9 (7,8)	7,8 (8,2)	7,9 (7,8)	6,7 (6,6)[1]
2009	5,8 (5,7)	5,9 (6,6)	5,9 (5,5)	4,4 (4,5)[1]
2010	3,5 (4,0)	3,9 (5,5)	4,7	2,8
Current account balance, in % of GDP				
2008	-12,3 (-13,5)	-12,6 (-13,8)		
2009	-7,4 (-13,0)	-7,5 (-13,3)		
2010	-6,1 (-12,6)	-6,5 (-12,7)		

BNR – Banca Naţională a României

SLOVAKIA

Economic growth

In the fourth quarter of 2008, a significant slowdown of economic growth took place in Slovakia, which in the previous three quarters belonged to the most rapidly developing Central and Eastern European countries. Whereas between January and September 2008 Slovak economy increased by 7.8% y/y, in the fourth quarter economic growth rate slowed down to 2.5%[18]. Thus, this was the lowest GDP growth rate since the first quarter of 2001. However, Slovak economy still developed on average faster than other Central and Eastern European countries. In the first quarter of 2009, GDP in Slovakia fell considerably on a yearly basis (according to preliminary estimates by as much as 5.4%).

The most significant influence on a slower economic growth was exerted by a lower demand in the countries being Slovakia's most important trade partners. Taking into account the share of exports in GDP (amounting to 86% in 2007), it has to be stated that Slovak economy depends more than other countries in the region on prosperity of main export markets. Exports growth declined continuously from the beginning of 2008 and fell to 7.8% in the last quarter of the previous year (which was the most significant decline in the last ten years), as compared to an increase by 7.3% in the first three quarters of 2008. Due to high import dependency of Slovak exports, at the same time imports fell considerably – however the scale of this decline was lower (6.7%) as a result of a relatively high increase in consumption demand. Consequently, a negative impact of net exports on GDP growth increased (as compared to the third quarter of 2008).

GDP growth significantly slowed down in the fourth quarter also due to a considerable slowdown of investment expenditures (from 8.9% in the first three quarters of 2008 to 1.4% in the fourth quarter of 2008), which in the last three years belonged to the most important economic growth factors. On the other hand, GDP growth in the fourth quarter was determined mainly by the continuation of an upward trend in household consumption expenditures. A slowdown in growth rate of this category was relatively small (from 6.7% to 4.7%), which was related to a relatively high growth in salaries even in 2008.

In the whole 2008, Slovak economy grew by 6.4% (as compared to 10.4% in 2007). This was the lowest increase since 2004.

Figure 8.1

Contribution to GDP growth (in pp, y/y)

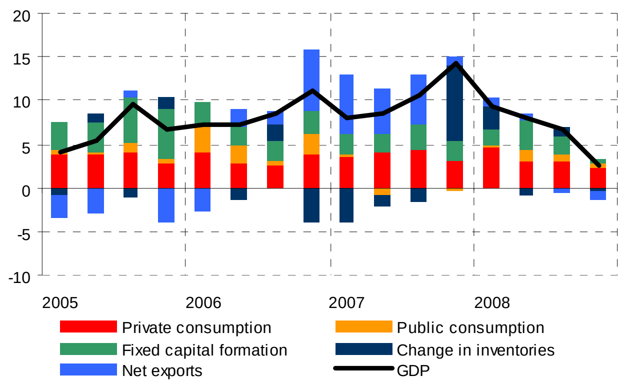


Table 8.1

GDP and its components growth rate (in %, y/y)

	2007	2008	Q3 2008	Q4 2008	Q1 2009
GDP	**10,4**	**6,4**	**6,6**	**2,5**	**-5,4**
Private consumption	7,1	6,1	6,0	4,7	
Public consumption	-1,3	4,3	5,3	2,3	
Fixed capital formation	8,7	6,8	7,3	1,4	
Exports	13,8	3,2	2,7	-7,8	
Imports	8,9	3,3	3,6	-6,7	

source: Ecowin Economic

Data describing the situation of the Slovak economy at the beginning of 2009 indicates fast acceleration of recession tendencies. A significant decline in growth of consumption expenditures is indicated on one hand by a significant fall in retail sales, and on the other hand by a strong deterioration of consumer prosperity. In February, retail sales decreased by 10.3% as compared to the previous year (this was the strongest fall in the last six years), after a decline by 3.3% in January. The largest decline in sales affected durable goods. Car sales also suffered a considerable decline (by almost 40%). In March this year, the scale of a decline in retail sales slowed down (sales declined by 7.5% y/y, including passenger cars by 2.0%).

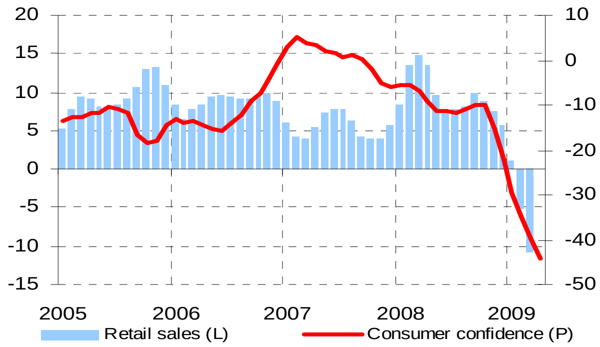
Owing to the premium for the sale of a new car and for scrapping of an old car (amounting to EUR 2 thousand), implemented by the Slovak government in March this year, the number of registered new cars in Slovakia increased by 18.2% (the second biggest growth in Europe

[18] A low increase in the fourth quarter of 2008 results partially also from the base effect. In the fourth quarter of 2007, Slovak economy grew by 14.3%.

behind Germany)[19]; whereas in the period January – February 2009 it declined by 38.5%. The impact of these premiums on the growth in consumption expenditures will be probable short-term (furthermore, the impact on retail sales growth was additionally weakened by the purchase of a part of cars in neighbouring countries).

Since the end of 2008, pessimism among Slovak consumers has been growing. In April this year, consumer sentiment indicator reached the lowest level since 1999. Slovaks mainly fear an increase in unemployment and deterioration of the outlook for the national economy.

Figure 8.2
Retail sales (in %, y/y) and consumer confidence index



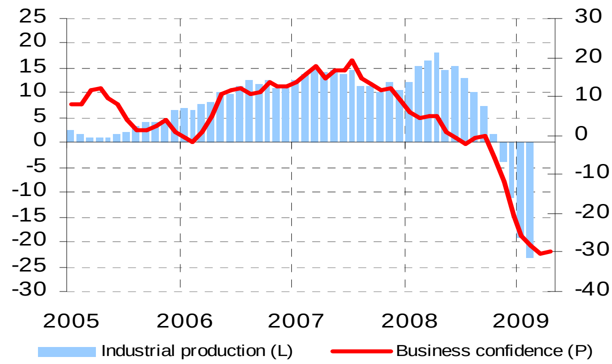
source: Ecowin Economic

An increasing decline in demand in Western European countries causes a strong decrease in production in the most significant sectors of economy – largely export-oriented. Between January and February 2009, industrial production fell by 29.5% y/y[20], most considerably in automotive industry[21] (approx. 98-99% of cars manufactured in Slovakia are designed for export) and electronic industry. In both branches production fell by almost 50% as compared to a relevant period of the previous year. All three car plants (Volkswagen, Kia and PSA Peugeot Citroen) reduced production and working time in 2008. Slovak Ministry of Finance estimates a decline in the number of manufactured cars this year by over 20%. It is expected that implementing a premium for scrapping cars in Germany and France will make it possible to ease deep drops in car production. This may be confirmed by recent decisions of Kia and PSA to increase production level in response to a rising demand for small and medium-sized car brands. On the other hand, Volkswagen which manufactures mainly big cars, temporarily ceased production at the beginning of April.

In January this year, a decline in production was additionally strengthened by disturbances in natural gas supplies. Slovakia was one of the countries most significantly affected by the gas conflict between Russia and Ukraine.

A drop in orders for the industry causes a severe deterioration of business sentiment. Business confidence indicator reached its lowest level in January this year. Despite a certain improvement in further months (influenced mainly by better outlook for production), it is still close to its historical lowest level. Particularly unfavourable is employment sub-indicator suggesting possible further deterioration of the situation on the labour market.

Figure 8.3
Industrial production (in %, y/y) and business confidence index



source: Ecowin Economic

Labour market

Unemployment rate was falling until August last year. In August 2008, it decreased to 7.4% - reaching its lowest level since gaining independency by Slovakia. However, weaker employment growth since the end of the previous year (in particular in processing industry) contributed to an increase in unemployment rate. In March 2009, after 2.5 years, it exceeded 10% again. The number of jobs has been clearly on the decrease since December 2008. Whereas in 2008 employment in Slovakia rose by 2.8% on average – the biggest increase since Slovakia gained independence, in the first two months of

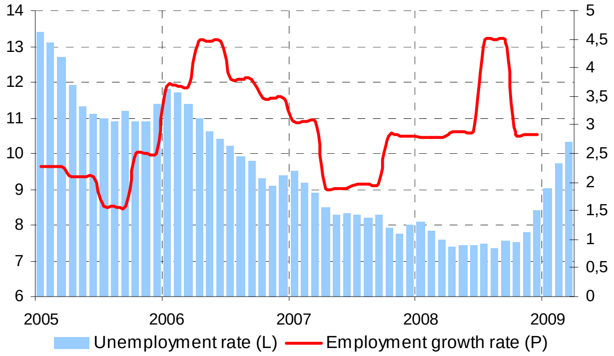
[19] According to the Association of European Automobile Constructors (ACEA).

[20] Industrial production growth started to decline already in the third quarter this year, and fell afterwards in the fourth quarter.

[21] The share of automotive sector in industrial production amounted to 35.2% in 2007 (2008: decrease to 32.8%). Automotive sector employs 74 thousand people, including 14 thousand dealing directly with car production .

this year the number of jobs declined by 4.5% (including a 10.0% decline in industry).

Figure 8.4
Unemployment rate (in %) and employment growth rate (in %, y/y).

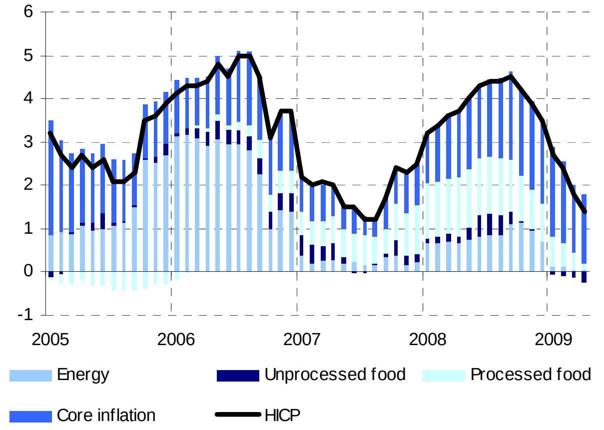


source: Ecowin Economic

Inflation and labour costs

Despite concerns, implementing euro did not reverse a downward trend in inflation in Slovakia (see box). Inflation measured by a harmonised consumer price indicator decreased in April 2009 to 1.4% y/y, i.e. to its lowest level in 1.5 years. In the last 6 months, HICP indicator fell by 2.7 p.p. Such considerable decline in inflation was caused by both a lower growth in food prices (despite an increase in excise tax on tobacco products), energy and in other goods and services – in particular durable goods (cars, household goods and electronic equipment).

Figure 8.5
HICP and its components (in pp, y/y)



source: Ecowin Economic

Despite a considerable decrease in the recent months, core inflation in Slovakia is still higher than in neighbouring countries. This is mainly due to a higher growth in salaries in 2008 as compared to other Central European countries. However, at the beginning of 2009, a growth in salaries slowed down considerably. Although in January this year nominal wages were still higher by 3.6% on average as compared to January of the previous year, in February they increased only by 1.1%. It may be therefore expected that a downward trend in core inflation will accelerate in the coming months.

Table 8.2
HICP and its components (in pp, y/y)

	Q2 2008	Q3 2008	Q4 2008	Q1 2009	04 2009
HICP	**4,0**	**4,4**	**3,9**	**2,3**	**1,4**
Categories with largest contribution					
Housing	0,7	0,9	1,4	1,1	1,0
Restaurants and hotels	0,4	0,6	0,6	0,6	0,6
Alcohol beverages and tobacco products	0,2	0,2	0,4	0,5	0,5
Health	0,4	0,4	0,4	0,4	0,4
Miscellaneous	0,2	0,3	0,2	0,3	0,3

source: Ecowin Economic

External imbalances

In 2008, a negative current account balance showed a further decrease. In the previous year, deficit on the current account amounted to 6.5% GDP (as compared to 5.3% in 2007). Its increase was caused mainly by much faster increase in imports of services than in their exports. As a result, Slovakia became a net importer of services (though it had a relatively high surplus of exports over imports even in 2007). Consequently, all items of current account balance are negative. In 2008, a negative balance of transfers further increased for the third time in a row. In the first three quarters of this year, income deficit also increased, though it decreased considerably in the fourth quarter of 2008.

As compared to 2007, a negative balance of trade in goods almost did not change due to a similar growth in exports and imports. In 2008, Slovak exports rose by 5.1% and imports by 5.0% (as compared to 15.2% and 10.2% in 2007 respectively). A decrease to the lowest level of trade growth in the recent years was influenced by a strong fall in turnover in the fourth quarter this year. Although in the first three quarters both exports and imports rose by 11.2% per year, the fourth quarter was marked by their decline by 11.0% - slightly more than in other countries in the region, which is closely related to domination of automotive industry in Slovak exports. At the same time, a strong decrease in imports was influenced by a decline in demand of the Slovak export sector for import of intermediate goods.

At the beginning of 2009, a decline in foreign trade accelerated. Between January and February this year, exports fell by 32.1% and imports by 30.7%. The goods structure of Slovak exports (with a dominant share of products classified as machines and transport vehicles whose replacement is mainly carried out under corporate trade) is the reason for the fact that the scale of a decline in Slovak exports at the end of 2008 and at the beginning of 2009 was slightly larger as compared to other Central European countries. At the same time, it seems that the appreciation of euro against other currencies of Central and Eastern European countries had no significance for the result of Slovak trade. Exports to Poland, the Czech Republic and Hungary altogether decreased in January 2009 by over 32.4% y/y, whereas exports to the euro zone fell by 30.7%. A decline in imports from the countries in the region was slightly lower. Imports from three neighboring countries in the region fell namely by 26.3%, and from the euro zone by 30.9%.

Figure 8.6
Current account balance and its components (in % of GDP, 4Q moving average)

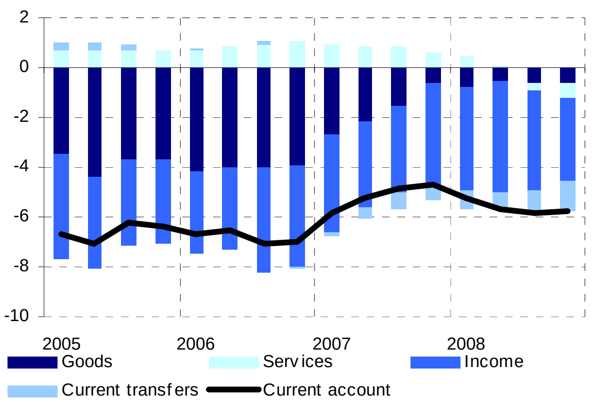


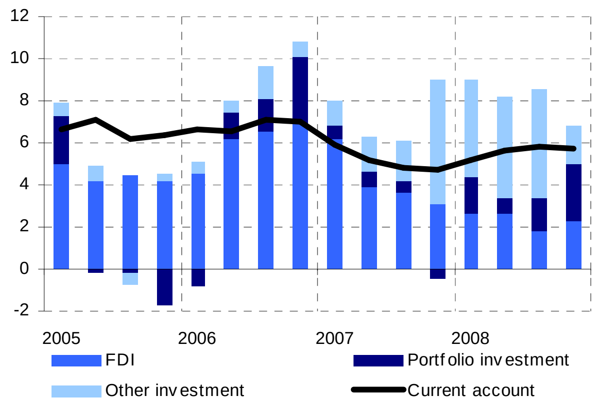
Table 8.3
Balance of payments (EUR mn)

	Q4 2007	Q1 2008	Q2 2008	Q3 2008	Q4 2008
Current account	-1048	-50	-1257	-1501	-975
Goods	-138	277	-352	-154	230
Services	30	-70	-101	-35	206
Income	-902	-52	-668	-1105	1825
Current transfers	-38	-204	-136	-206	546
Capital account	228	139	402	222	-222
Financial account	726	203	958	2088	-3248
Direct investments	346	-197	329	643	-775
Portfolio investments	-286	550	266	679	-1495
Other investments	135	-301	-146	-675	1122

source: Ecowin Economic

An increase in the current account deficit was accompanied by a certain decrease in a positive balance on the financial account. As compared to previous years, deficit financing structure changed slightly. In 2008 (in particular in the fourth quarter of 2008), the inflow of foreign direct investments, which in the previous year was a bit lower than in 2007, was most important. An inflow of portfolio investments increased considerably. At the same time, a considerable decline was observed in the inflow of other investments. An improvement in deficit on the current account results, inter alia, from the accession to the economic and monetary union which stopped the outflow of foreign investors taking place in other Central and Eastern European countries.

Figure 8.7
Financial account balance and its components (in % of GDP, 4Q moving average)



source: Ecowin Economic

Despite the crisis, Slovakia still belongs to the most attractive locations for direct foreign investments. In April this year, Volkswagen confirmed its intention to manufacture a new model of a small, economical car in Slovakia (previously, the Czech Republic was taken into account as a possible location for this investment). A German group intends to invest over EUR 300 million in production of this car. The sale of a new car will start in 2011. It is estimated that the investment in the plant located in Bratislava will create 1.5 thousand new jobs.

Foreign exchange rate

Implementing a fixed exchange rate of the Slovak koruna to the euro in July 2008 contributed to stabilisation of the financial situation in Slovakia and weakened short-term impact of the world financial crisis on the Slovak economy at the end of the previous year. The koruna exchange rate remained stable against the euro, whereas currencies of neighbouring countries suffered from a strong depreciation. In the medium term, a high conversion rate of the Slovak koruna and simultaneous depreciation of currencies in neighbouring countries may presumably weaken competitiveness of the Slovak economy. On the other hand, the adoption of euro may be an additional advantage of Slovakia as a location for foreign investments[22].

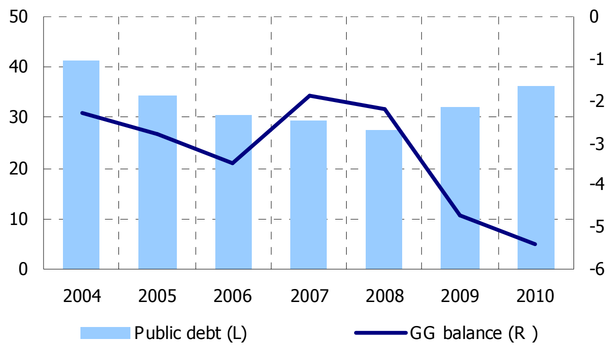
Fiscal policy

In 2008, general government deficit amounted to approx. 2.2% GDP and as such was at the level forecast by the European Commission in autumn last year. At the same time, a negative sector balance turned out slightly higher than the planned figure for 2008 (1.7% GDP) and deficit in 2007 (1.9% GDP).

Slovak government adopted a budget act for 2009 with deficit of the public finance sector at the previous year's level (2.1% GDP), assuming that economic growth will remain at 4.6%. Current economic forecasts indicate a possibility of a significantly lower economic growth rate (2.7%) than assumed in the budget act for 2009, and even a decline in GDP (European Commission and the National Bank of Slovakia) which will have a negative impact on the income side of the public finance sector. Slovak monetary authorities declare that deficit of the public finance sector may amount to 2.6-2.8% GDP taking into account worse macroeconomic circumstances than expected for 2009. At the same time, the European Commission estimates it at 4.7% GDP.

Figure 8.8

General government balance and debt (in % of GDP)



source: Eurostat

In January this year, Slovak government started its work on preparing the anti-crisis package, and the Council for the Economic Crisis was set up for this purpose. This Council consists of representatives of the government, central banks, employers and trade unions. The anti-crisis package prepared by the Slovak government is mainly aimed at protecting the labour market (protecting jobs, supporting employers) and stimulating economic growth by an increasing domestic demand. The most important actions specified in the package are as follows:

- budget funds providing partial financing for salaries of employees whose working week was reduced to 4 days,
- allowance to every newly created workplace provided to companies which did not carry out staff reductions in the last 12 months and were not in delay with public law payments,
- aid to people coming back from abroad who will undertake economic activity or a possibility of a 2-year exemption from the payment of social and health insurance contributions,
- allowances for employees working outside their residence,
- allowance to the purchase of a new car, if an old car manufactured before 2000 was scrapped, having been registered in Slovakia before 2009,
- increasing the number of so-called social companies, established with state funds, employing employees with low qualifications,
- increasing a non-taxable amount for personal income tax,
- decreasing the period for return of VAT advances paid by entrepreneurs (from 60 to 30 days),
- increasing investment programmes under public-private partnership.

Slovak government estimates to spend EUR 0.3 billion (0.5% GDP) on the above actions using savings planned in public administration for this year. Slovak government declares further work to find solutions easing the crisis effects, however, its priority is to maintain deficit of the public finance sector below 3% GDP this year.

Forecasts

Even in January this year, in its review of the Slovak economy, OECD[23] expressed an opinion that implementing euro may save this country from a growing crisis in real economy. However, in the following months economic growth forecasts were revised down as in the case of other countries in the region. At present, Slovak

[22] According to the report prepared every year by Pricewaterhouse Coopers, Slovakia was chosen the most attractive location for investments in the services sector due to the implementation of euro.

[23] Economic Survey of the Slovak Republic 2009, OECD 2009.

and foreign research centres believe that Slovak GDP will decline in 2009. Due to an expanding crisis in Western Europe, the National Bank of Slovakia estimates that GDP will decrease by 2.4% - this would be the first decline in GDP since Slovakia gained independence in 1993.[24], which would - to a great extent - reflect growing deficit in trade (exports are estimated to fall by 8.3%, whereas imports – by 4.8%[25]). Lower decline in imports than in exports was due to the continuation of an upward trend in consumption expenditures. The Bank of Slovakia expects that household consumptions will grow by 1.0% this year (whereas a previous forecast assumed an increase by 5.9%). A moderate increase in consumption will be favoured by a positive growth in disposable income. Investment expenditures are expected to fall (by 0.4%), though infrastructural investments carried out under public-private partnership should ease this decline. It is expected that Slovak economy will return to the economic growth path in 2010. This will be caused by stopping a downward tendency in exports (which shall lead to neutral impact of net exports on GDP growth) and a simultaneous increase in consumption expenditures.

In addition to worse economic activity growth, inflation (HICP) will decrease as well – in 2009 it shall amount to 1.7%, and in 2010 it is estimated by the Bank of Slovakia at 2.9%.

The highest risk to the forecast may be a decline in household expenditures, as indicated by figures on retail sales at the beginning of this year.

Table 8.4

Forecasts of main indicators

	KE	IMF	Consensus Economics	NBS
	05.2009 (11.2008)	04.2009 (10.2008)	04.2009 (11.2008)	04.2009 (11.2008)
GDP, in %, y/y				
2008	6,4 (7,0)	6,4 (7,4)	6,4 (7,0)	6,4 (7,5)
2009	-2,6 (4,9)	-2,1 (5,6)	-1,1 (4,9)	-2,4 (4,7)
2010	0,7 (5,5)	1,9 (5,9)	1,8	2,0 (5,8)
Inflation, in %, y/y				
2008	3,9 (4,0)	3,9 (3,9)	4,6 (4,6)	1,7 (3,9)
2009	2,0 (3,5)	1,7 (3,6)	2,4 (3,8)	2,0 (2,7)
2010	2,4 (3,3)	2,3 (3,2)	2,8	2,9 (3,2)
Current account balance, in % of GDP				
2008	-6,8 (-5,6)	-6,3 (-5,1)		-6,5 (-5,8)
2009	-7,5 (-4,7)	-5,7 (-4,7)		-7,3 (-4,6)
2010	-7,1 (-3,5)	-5,0 (-4,5)		-6,4 (-3,5)

NBS - Národná banka Slovenska

[24] In December 2008, the National Bank of Slovakia expected that economic growth rate would amount in 2009 to 4.7%, whereas the forecast of the Ministry of Finance from February this year indicated a GDP increase ny 2.4%.

[25] This will influence constant deficit on the current account. It is expected that it will increase to 7.3% GDP in 2009 (as compared to 6.5% in 2008).

Box 2

Impact of the implementation of the euro on inflation in Slovakia

On 1 January 2009, Slovakia joined the economic and monetary union as 16th country, and thus the Slovak koruna was replaced by the euro. Adoption of a new currency was related to numerous concerns expressed by society that it may cause a significant increase in prices in Slovakia. These concerns resulted form the fact that vendors could increase prices of certain goods and services when converting prices expressed in the koruna to the euro, which did not necessarily have to be related to price rounding. In order to prevent such practices, Slovak government adopted already in mid-2008 the *Ethical code* obliging sellers to quote prices of goods in both currencies (*dual-pricing*) within 5 months prior and 12 months after the currency exchange. Moreover, since August 2008 prices of selected and popular products were regularly monitored by the Slovak statistical office in order to avoid price increases.

An increase in prices due to the so-called *changeover effect* occurred earlier in other Eurozone countries, however, in all cases it was lower than previous social expectations. 2003 Eurostat estimates indicated that the implementation of the euro to cash circulation in 2002 led to an increase in inflation in the euro zone by approx. 0.09-0.28 p.p.[26]. Similar research was made during further Eurozone extension. In the case of Slovenia, the impact of changeover effect on inflation amounted to 0.3 p.p.[27], and in the case of Cyprus and Malta – to approx 0.2-0.3 p.p.[28].

In March 2009, the National Bank of Slovakia (NBS) prepared a report, in which it evaluated the impact of the implementation of the euro in Slovakia on inflation[29]. According to these estimates, the impact of the implementation of the euro on HICP growth amounted to approx. 0.12-0.19 p.p., i.e. was comparable to the one observed in other countries. NBS calculations were based on a few simultaneous methods:

- 3 sigma approach – studying monthly changes in prices of over 700 products composing the CPI basket in the years 2005-2008 and calculating a standard deviation, with which price changes would be compared in the period from December 2008 to January 2009 (prices changes of only 49 products did not fall in an interval of 3 standard deviations);
- International comparison approach – comparing changes in prices of goods and services composing the CPI basket with those in neighbouring countries (Czech Republic, Poland, Hungary, Austria);
- Means and medians approach – comparing means and medians of prices in December 2008 and January 2009 (if an increase in average prices exceeds an increase in their medians, this could indicate that prices of certain goods and services increased in an disproportionate manner);
- Approach comparing monthly price changes in January – price changes in January 2009 were compared with those at the beginning of previous years;
- ARMA based approach – comparing changes in individual price groups with forecasts based on the ARMA model.

When calculating the scale of the changeover effect roundings up and down, which occurred many times, were not taken into account. Such practices took place in particular in food prices. A part of trade chains decided to decrease prices a bit due to a currency change under marketing actions carried out by them. An influence on rounding prices down could also be exerted by restrictions imposed by authorities due to unjustified increase in prices of products during the currency change. Taking into consideration also those groups of products whose price decreased due to price roundings, the changeover effect would be between -0.12 and 0.12 p.p., which means that

[26] News Release 69/2003, Eurostat, June 2003
[27] Euro changeover and inflation in Slovenia, Eurostat, March 2007
[28] Euro changeover and inflation in Cyprus and Malta, Eurostat, April 2008
[29] The Impact of Euro Adoption on Inflation in the Slovak Republic in January 2009, NBS, March 2009

the changeover effect related to a change from the Slovak koruna to the euro would be insignificant.

The changeover effect on inflation in Slovakia was also estimated by Eurostat. Eurostat estimates were close to those presented by the NBS. According to Eurostat, the impact of the implementation of euro on the increase in inflation in Slovakia amounted to approx. 0.2 p.p.[30].

Observing the main HICP indicator, whose growth slowed down further in 2009 and a change m/m in January 2009 of only 0.3% (the lowest monthly increase in inflation ever), it may seem that the implementation of euro in Slovakia had no impact on an increase in consumer prices. However, prices of certain goods and services contributed more considerably to inflation than in the previous years. These were, inter alia: prices of transport services, household keeping services, veterinary services or some hotel and restaurant services.

It seems that the implementation of euro in Slovakia has an additional positive impact on inflation by stabilising exchange rate. In the second half of 2008 and at the beginning of 2009, a very strong depreciation of domestic currencies took place in neighbouring countries (Poland, Czech Republic, Hungary), which led to an increase in import prices, and thus contributed to an increase in inflation in these countries in the first quarter of 2009. At the same time, a decline in consumer price growth in Slovakia, which started in mid-2008, continued through 2009 (as in other countries in the region using a fixed exchange rate system). In March 2009, HICP growth in Slovakia amounted to 1.8% y/y, and apart from Slovenia and Czech Republic (where in March 2009 inflation increased from 1.4% in January to 1.7%), it belonged to the lowest in the region.

The report of the European Commission after the adoption of euro in Slovakia[31] shows that the majority of Slovaks (91%) did not have any problems with getting familiar with a new currency. Slovaks more critically evaluated price changes after a conversion from the Slovak koruna to the euro - approx. 1/3 respondents were of the opinion that vendors often increased prices of their goods in an unjustified manner. A similar percentage of surveyed respondents stated that price roundings influenced prices. However, this was a less critical result than the one observed in the previous years in Cyprus and Slovenia. At the same time, Slovaks gave a very favourable opinion on the activities of authorities preventing price increases. As much as 80% of respondents positively evaluated functioning and utility of the double-price system.

[30] Euro changeover and inflation in Slovakia, Eurostat, March 2009

[31] Euro Introduction in Slovakia; Ex-post Citizen Survey, Flash Eurobarometer 259, The Gallup Organization, March 2009

SLOVENIA

Economic growth

In the fourth quarter of 2008, Slovenian GDP growth was negative for the first time since 1993. GDP decreased by 0.8% on an annual basis and by 4.1% on a quarterly basis. Such strong deterioration of economic activity at the end of 2008 (in the first three quarters of 2008, Slovenian economy grew by 5.0% y/y) probably resulted mainly from a strong decline in external demand as in other economies. Slovenian exports in the fourth quarter of the last decreased by 6.2% (including a decrease in exports of goods by 9.4%), whereas in the first three quarters exports rose by 4.6%. A decline in imports was slightly bigger (by 7.3% in the fourth quarter of 2008 as compared to an increase by 7.2 in the first three quarters of the previous year). At the same time, investment expenditures, which were so far the most important source of economic growth apart from exports, decreased significantly. In the fourth quarter, investments decreased by 5.3% (as compared to an increase by 10.2% in the period January-September 2008). Although in the first three quarters of 2008, investment expenditures were largely influenced by infrastructural projects, this kind of investments as well as investments in machinery decreased significantly in the fourth quarter of the previous year. A growth in household consumption was gradually diminishing since the beginning of 2008. In the fourth quarter of the previous year, consumption expenditures grew by mere 1.1%, which was influenced on one hand by a decline in demand for durable goods, and on the other hand by an increasing difference between expenditures of residents abroad and domestic expenditures by non-residents– related to an increasing inflow of immigrants to Slovenia.

Figure 9.1
Contribution to GDP growth (in pp, y/y)

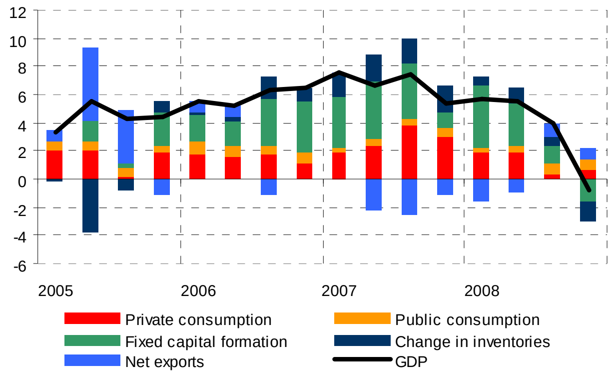


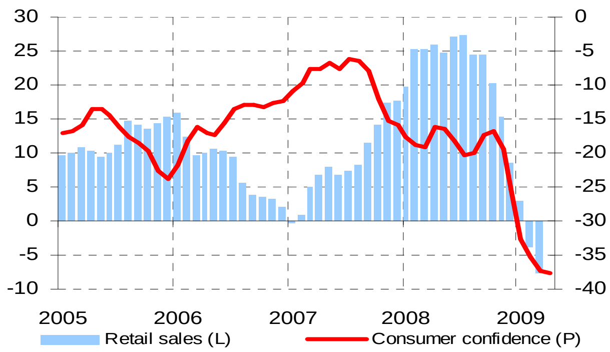
Table 9.1
GDP and its components growth rate (in %, y/y)

	2007	2008	Q2 2008	Q3 2008	Q4 2008
GDP	6,8	3,5	5,5	3,9	-0,8
Private consumption	5,3	2,2	3,5	0,6	1,1
Public consumption	2,5	3,7	3,3	4,6	5,0
Fixed capital formation	11,9	6,2	10,3	4,5	-5,3
Exports	13,8	3,3	8,0	4,2	-6,2
Imports	15,7	3,5	9,2	3,0	-6,6

source: Ecowin Economic

An increasing downward trend in consumption expenditures at the beginning of 2009 is confirmed by a decline in retail sales. In the first quarter this year, retail sales decreased by 5.0% y/y (as compared to an increase by 7.2% in the fourth quarter of 2008 and 14.1% in the period January-September 2008) and by 8.5% q/q. Food sales remained at a similar level to the previous year, but household, electronic equipment and car sales decreased considerably. It seems that a decline in sales was much more influenced by growing concerns of consumers about the world crisis for Slovenian households than by current deterioration of the financial situation of consumers (as indicated by the continuation of an upward trend in salaries). This is confirmed by the results of consumer sentiment research. The financial situation of households is evaluated by Slovenian consumers at a similar level to the long-term average, but the outlook for the coming 12 months is evaluated very negatively. Furthermore, a future economic situation of the country is evaluated worse than the situation of households. The situation on the labour market is evaluated as particularly negative.

Figure 9.2
Retail sales (in %, y/y) and consumer confidence index



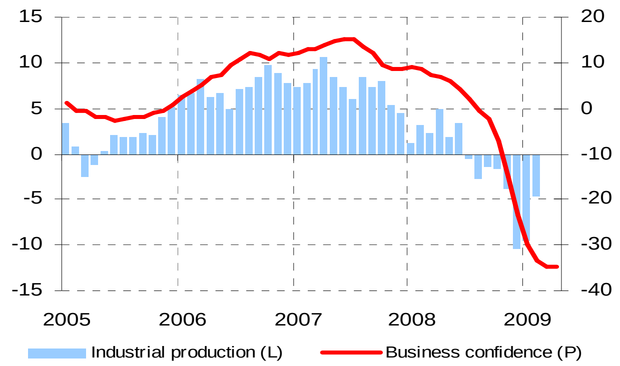
source: Ecowin Economic

At the beginning of this year, a decline in industrial production even accelerated. In the first two months of 2009, industrial production fell by almost 20% y/y. A decline in production deepened in all main categories of economic activity – affecting most considerably industrial manufacturing. At the same time, a decline in external and domestic demand causes a significant increase in inventories which increased by over 7% in the period January-February 2009 as compared to the previous year. Furthermore, domestic orders fell in the first two weeks of this year by 20.4%, and foreign orders by 23.2%, affecting most considerably intermediate goods.

A particularly high decline in production took place in companies operating in automotive industry (approx. 30% y/y). In November last year, Slovenian subsidiary of Renault limited the work process to two shifts, and in March this year it stopped it temporarily. Due to an increase in demand for small types of cars (related to implementing a premium for scrapped cars in some EU countries), work in a three-shift system restarted at the end of April 2009. However, Renault decided to move the production line of Clio2 to Flins, France. Therefore, in Slovenia Renault will manufacture only Twingo model. Even more unfavourable situation takes place in plants manufacturing spare parts for cars. For example, Slovenian subsidiary of Goodyear manufacturing car tyres sent its employees to obligatory vacation at the beginning this year, and afterwards a work week was reduced to four days.

A decline in orders, in particular for export, has a negative impact on the economic situation of companies. In April this year, a confidence indicator in manufacturing decreased to its lowest level in history (i.e. since 1995). According to studies, an increasing number of entrepreneurs takes into account a possible reduction in employment in the foreseeable future. However, an evaluation of the future situation of Slovenian companies has been constantly improving since the beginning of this year.

Figure 9.3
Industrial production (in %, y/y) and business confidence index



source: Ecowin Economic

Labour market

A high growth in employment – over 3% per year – continued almost to the end of 2008, mainly due to a strong increase in employment in construction and an increasing number of jobs in some categories of services (whereas the number of jobs in manufacturing fell already in the second quarter of the previous year)[32]. As a result, unemployment rate decreased to its historical lowest level of 6.3% in September last year.

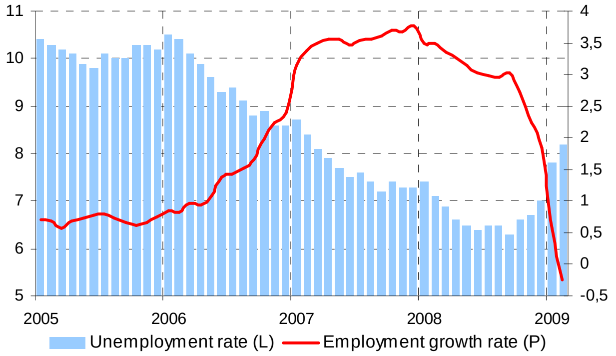
A decline in the number of jobs in the Slovenian economy has been observed since November last year (a decrease by almost 20 thousand jobs within four months), which was reflected by an increase in unemployment rate 8.2% in February 2009.

A governmental programme valued at over EUR 800 million was designed to limit a negative impact of the world crisis on the Slovenian labour market. In the period February-August, state budget will finance social insurance for employees of companies which will not reduce employment and will not pay additional remuneration to management in exchange for reducing a work week. The programme covered over 400 companies. Furthermore, in April this year, Slovenian government proposed to offer subsidies to the remuneration fund amounting to 50% of employee base salary to companies which will not reduce work time and employment. At the same time, 35% of salaries will be financed by companies which shall guarantee 85% of remuneration.

[32] It is estimated that approx. 80% of 2008 increase in employment in Slovenia relates to immigrants.

Figure 9.4

Unemployment rate (in %) and employment growth rate (in %, y/y)



source: Ecowin Economic

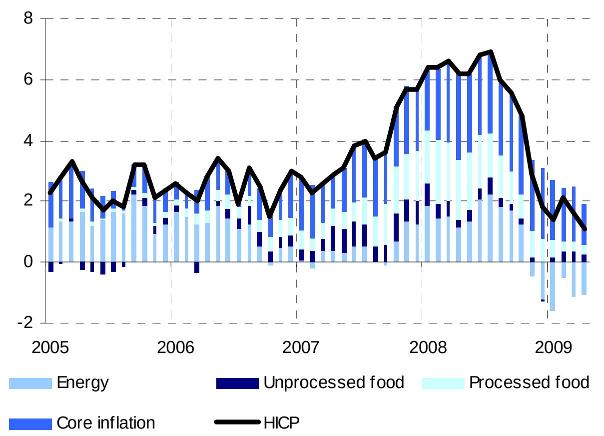
Inflation and labour costs

In April 2009, HICP in Slovenia fell to 1.1% - i.e. to the second lowest level in the region, just behind Estonia. Since the beginning of the second half of 2008, inflation gradually decreased, and afterwards rose slightly in February due to an increase in excise tax on some energy. As a result, fuel and electricity prices contributed to a decline in HICP inflation to a relatively smaller extent than in other euro zone countries.

However, in the next two months, i.e. in March and April 2009, inflation in Slovenia further decreased. In April this year, it decreased to 1.1% - historical lowest level as a result of a considerable slowdown in the growth of foods prices (also influenced by appreciation of euro to other currencies of neighbouring countries). On the other hand, HICP-core indicator became relatively stable at the beginning of this year.

Figure 9.5

HICP and its components (in pp, y/y)



source: Ecowin Economic

Relatively small changes in prices of consumption goods and services after their inclusion in food and energy prices may explain an upward trend in salaries observed still at the beginning of the year. In the period January-February 2009, average salary increased by 5.5% y/y (whereas an average increase in 2008 amounted to 8.3 y/y). A positive impact of an increase in salaries on inflation in the coming months will gradually diminish, which is indicated by a decrease in salaries in January and February this year as compared to December 2008 (by 2.8% and 5.2% respectively).

Table 9.2

HICP and its components (in pp, y/y)

	Q2 2008	Q3 2008	Q4 2008	Q1 2009	04 2009
HICP	**6,4**	**6,2**	**3,2**	**1,7**	**1,1**
Categories with largest contribution					
Restaurants and hotels	0,8	0,9	0,8	0,7	0,6
Food and non-alcoholic beverages	2,0	1,7	0,8	0,5	0,3
Wyposażenie mieszkania	0,4	0,4	0,4	0,4	0,3
Recreation and culture	0,4	0,4	0,3	0,2	0,3
Miscellaneous	0,4	0,3	0,3	0,3	0,3

source: Ecowin Economic

External imbalances

In 2008, current account deficit increased for the third year in a row, and amounted to 5.5% GDP at the end of 2008 (as compared to 4.2% in 2007) – thus reaching its highest level in Slovenia since gaining independence. The largest influence on an increase in deficit on the current account was exerted by an increasing negative balance in trade with goods – in particular in the first half of 2008, when on one hand a decreasing external demand contributed to a falling exports growth, and on the other hand - a relatively high growth in economic activity in Slovenia supported a relatively high growth in imports. In the period January-September 2008, exports grew by 4.9%, i.e. much more slowly than in 2007 when it went up by 16.3%. At the same time, imports grew faster – by 10.2%, though due to a decline in a demand by branches focused mainly on exports, imports in this area also slowed down as compared to 2007 (when it rose by 18.1%).

However, in the fourth quarter of 2008, both exports and imports grew (by 9.8% and 7.4% respectively), which helped stabilise deficit in trade in goods. A decline in trade in goods was even bigger at the beginning of 2009. Similarly to other countries in the region, a decline in imports turned out to be stronger than in the case of exports (due to a decline in an investment and consumption demand). In the period January-February 2009, imports fell by 30.4% and exports by 25.3% on a yearly basis. This led to a decrease in deficit in trade.

Increasing deficit in trade in goods in 2008 was accompanied by an increase in a negative income balance. At the same time, deficit on the current account was positively influenced by decreasing deficit in transfers and an increasing positive balance on the services account.

Figure 9.6
Current account balance and its components (in % of GDP, 4Q moving average)

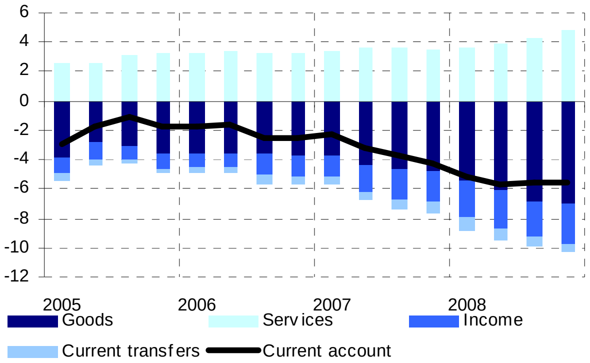


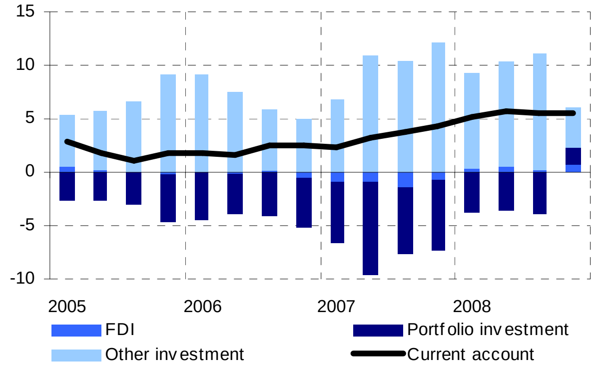
Table 9.3
Balance of payments (EUR mn)

	Q4 2007	Q1 2008	Q2 2008	Q3 2008	Q4 2008
Current account	-663	-512	-480	-456	-731
Goods	-664	-494	-678	-746	-743
Services	198	355	469	545	333
Income	-112	-221	-235	-293	-259
Current transfers	-86	-152	-37	39	-62
Capital account	-8	-2	-21	-42	-27
Financial account	924	423	849	501	592
Direct investments	47	148	-27	-86	223
Portfolio investments	-814	301	-1127	180	1253
Other investments	1636	53	1922	403	-905

source: Ecowin Economic

In 2008, after a 3-year pause, Slovenia became again a net importer of direct foreign investments. The inflow of direct foreign investments slightly exceeded the amount of Slovenian investments abroad which was due to a decline in Slovenian investments abroad (related to decreasing financing for Slovenian subsidiaries abroad, whereas investments in equity remained at the 2007 level) and to the continuation – for the third year in a row – of an increasing inflow of foreign investments to Slovenia. The inflow of portfolio investments also turned out to be at a record level – in particular in the fourth quarter of this year due to the issue of euro-bonds for total amount of EUR 2.5 billion.

Figure 9.7
Financial account balance and its components (in % of GDP, 4Q moving average)



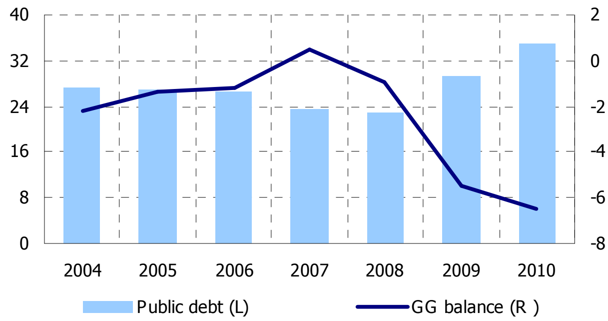
source: Ecowin Economic

Fiscal policy

In 2008, the situation of public finance in Slovenia deteriorated. Due to an economic slowdown, the public finance sector closed last year with deficit of approx. 0.9% GDP, whereas in 2007 the balance was positive and amounted to 0.5% GDP.

A deteriorating financial situation in Slovenia in 2008/2009 and actions taken by Slovenian government to reduce the crisis effects led to a decision on budget novelisation for 2009. As a result of a considerable increase in budget expenditures as compared to the previous budget version and due to a decline in revenues it was planned that the budget would generate deficit of 2.9% GDP instead of a surplus. Keeping deficit below a reference amount of 3% GDP was possible owing to the consent of social partners to postpone salary increases in the public sector. Nevertheless, a fiscal notification from April estimates deficit for 2009 at 3.7% GDP (European Commission forecasts deficit of 5.5% GDP).

Figure 9.8
General government balance and debt (in % of GDP)



source: Eurostat

The cost related to anti-crisis actions adopted by Slovenia is expected to reach almost EUR 1.1 billion (approx. 2.8% GDP). The most important actions aimed at improving the situation on the labour market are as follows: partial financing of salaries up to the full-time equivalent, co-financing trainings and requalification of employees, financial support to development projects, e.g. social entrepreneurship. Furthermore, the government adopted a package of anti-crisis actions aimed at improving the access of companies to external financing and liquidity of the whole economy. These activities comply with the EC recommendations and comprise inter alia:

– establishing a system of credit guarantees for entrepreneurs having difficulties in maintaining financial liquidity,
– elaborating the subsidy programme for companies, mainly to support investments in research and development,
– increasing capital of the Slovenian Export Bank to assure that export-supporting policies are carried out.

Forecasts

All forecasting centres estimate a decline in Slovenian GDP in 2009 and its slight increase in 2010. Domestic forecasts are more pessimistic than those presented by foreign centres (IMF and European Commission). The Institute of Macroeconomic Analysis and Development (IMAD) estimates in its forecast published at the beginning of April 2009 that Slovenian GDP will fall by 4.0% (as compared to an increase by 1.1% in the December forecast). Thus, this will be the first annual decline in GDP of Slovenia since its independence. Such profound decline in economic activity is related to a strong drop in a foreign demand for Slovenian goods and services. Slovenian exports may decrease this year by as much as 8.6% (as compared to an increase by 3.3% in 2008, whereas December forecast assumed its increase in 2009 by 1.5%). A decline in imports will be probably even higher, mainly as a result of not only a strong decline in the demand by the export sector, but also a fall in a domestic demand, in particular as regards investments. A decline in economic activity of the export sector will contribute to a strong decline in investments, which according to forecasts presented by the institute may reach 12.0% in 2009 (as compared to an increase by 6.2% in 2008 and assumed a decline by 2.0% assumed in the previous forecast). Relatively lowest decline will affect household consumption expenditures, though they will be negatively influenced by rising unemployment and likely decline in wages.

At the same time, inflation will slow down considerably, influenced by a decreasing growth in unit labour costs. In 2009, average annual HICP will decrease to 0.4%, and in 2010, it will grow to 1.6%.

Table 9.4

Forecasts of main indicators

	KE	IMF	Consensus Economics	IMAD
	05.2009 (11.2008)	04.2009 (10.2008)	04.2009 (11.2008)	04.2009 (10.2008)
GDP, in %, y/y				
2008	3,5 (4,4)	3,5 (4,3)	3,5 (4,6)	3,5 (4,8)
2009	-3,4 (2,9)	-2,7 (3,7)	-2,3 (3,0)	-4,0 (3,1)
2010	0,7 (3,7)	1,4 (3,8)	0,8	1,0 (4,0)
Inflation, in %, y/y				
2008	4,0 (6,2)	5,7 (5,9)	5,7 (6,0)	5,7 (6,2)
2009	1,9 (3,7)	0,5 (3,3)	1,7 (3,8)	0,4 (3,9)
2010	2,0 (3,1)	2,3 (3,3)	2,6	1,6 (3,3)
Current account balance, in % of GDP				
2008	-6,1 (-6,3)	-5,9 (-4,7)		-5,9 (-5,8)
2009	-4,6 (-6,3)	-4,0 (-4,7)		-2,2 (-4,7)
2010	-4,4 (-6,0)	-5,0 (-4,5)		-3,5 (-4,1)

IMAD - Institute of Macroeconomic Analysis and Development

HUNGARY

Economic growth

Hungarian economy was affected by a global crisis at the time when it already coped with a domestic slowdown. As a result of deterioration in external and internal circumstances in the fourth quarter of 2008, Hungarian GDP decreased by 2.3% y/y[33]. In the whole year 2008, Hungarian economy grew by 0.5% y/y (as compared to 1.1% in 2007). Preliminary GDP estimates forecast a growing GDP decline in the first quarter of 2009 (6.4% y/y).

Although in the first three quarters of the previous year, the majority of economic growth categories, except for investments, grew, only one category, namely change in inventories, increased in Q4 2008. A positive impact on GDP growth in Q4 2008 was also observed for net exports which resulted from the fact that imports decreased more than exports.

Figure 10.1

Contribution to GDP growth (in pp, y/y)

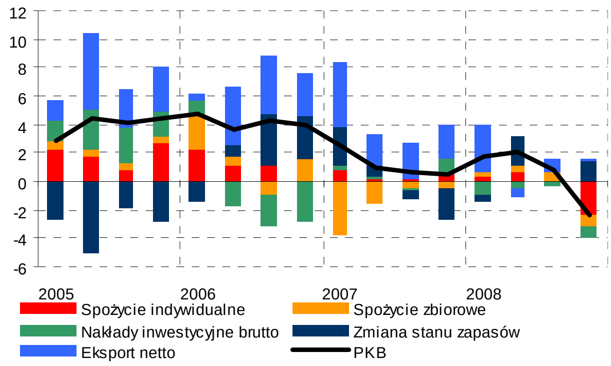


Table 10.1

GDP and its components growth rate (in %, y/y)

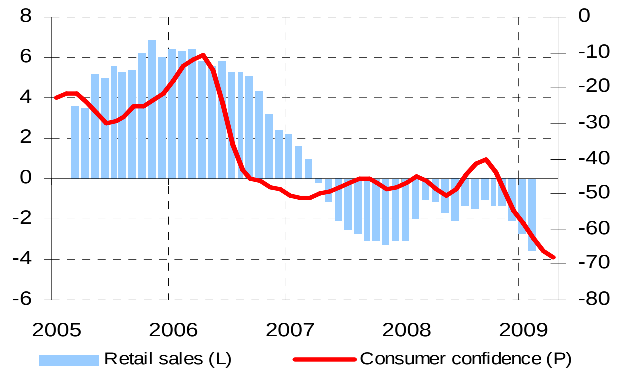
	2007	2008	Q3 2008	Q4 2008	Q1 2009
GDP	1,1	0,5	0,8	-2,3	-4,7
Private consumption	0,7	-0,7	0,1	-4,4	
Public consumption	-7,4	0,5	3,0	-4,3	
Fixed capital formation	1,5	-2,6	-1,5	-2,7	
Exports	15,9	4,6	3,5	-7,8	
Imports	13,1	4,0	2,8	-8,2	

source: Ecowin Economic

Whereas in the period January-September 2008 private consumption remained almost unchanged (increase by 0.6% y/y), it fell considerably in the fourth quarter of 2008. A similar tendency was observed in retail sales which has been gradually decreasing since the beginning of the second quarter of 2008, and a downward trend is clearly visible for all product categories. In February 2009, retail sales were below their 2005 level. Consumer confidence indices of the European Commission and GKI indicate further deterioration of sentiment among Hungarian consumers (in April the EC indicator fell to its lowest level in history, i.e. since 1993).

Figure 10.2

Retail sales (in %, y/y) and consumer confidence index



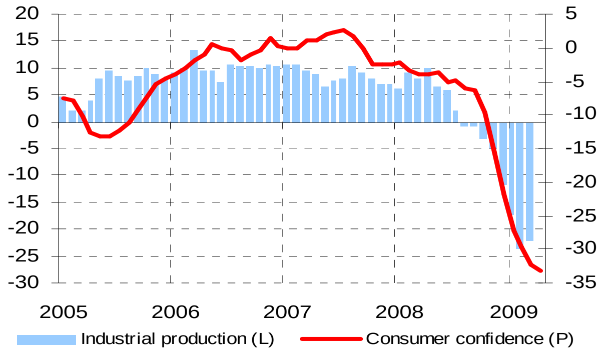
source: Ecowin Economic

In the fourth quarter of 2008 and at the beginning of 2009, a considerable acceleration of a decline in industrial production took place. In the first two months of 2009, industrial production fell by 26.1%. A strong decline in production resulted mainly from a growing decline in export production. Export production decreased in the first two months of 2009 by 30% as compared to the same period of the previous year (whereas in Q4 2008, it decreased by 15% y/y), which was due to a strong decline in production of automotive industry (decrease by as much as 52% y/y in February this year as compared to 19.7% y/y on average in Q4 2008) and in production of electronic equipment (decline by 22.8% y/y and on average by 18% y/y in Q4 2008). A decline in industrial production for domestic market deepened in the first two months to 18% y/y from 9% y/y/ in Q4 2008.

[33] As compared to the previous quarter, GDP decreased in the fourth quarter by 1.2%. This was the third quarterly GDP decline in a row (in the second quarter of 2008 by 0.1% and in the third quarter of 2008 by 0.6%).

Figure 10.3

Industrial production (in %, y/y) and business confidence index



source: Ecowin Economic

Following a period of a strong decline in export orders observed since mid-2008, a downward trend in domestic orders accelerated at the beginning of this year. This was a consequence of a lower demand of the export sector. Indices of new export and domestic orders fell in February this year by 37% and 28% y/y respectively.

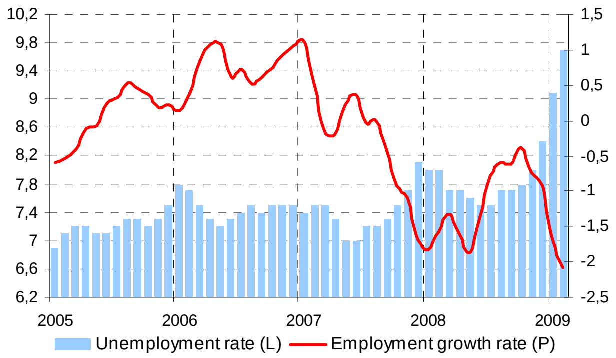
Leading indicators, i.e. business confidence indicator of the European Commission and PMI in manufacturing, despite some improvement observed in April this year, still indicate a low probability of any increases in investment in forthcoming months.

Labour market

Unemployment rate in Hungary has been gradually increasing since mid-2008, accelerating at the beginning of 2009. In March this year, it rose to 9.7%, which is the highest level in unemployment since the implementation of new methodology for measuring employment in 1998. The number of employees has been on the decrease since the end of 2007. At the same time, a labour activity indicator has been falling. In mid-2008, it amounted to 55.2%, and now it is at 54.1%

Figure 10.7

Unemployment rate (in %) and employment growth rate (in % y/y)



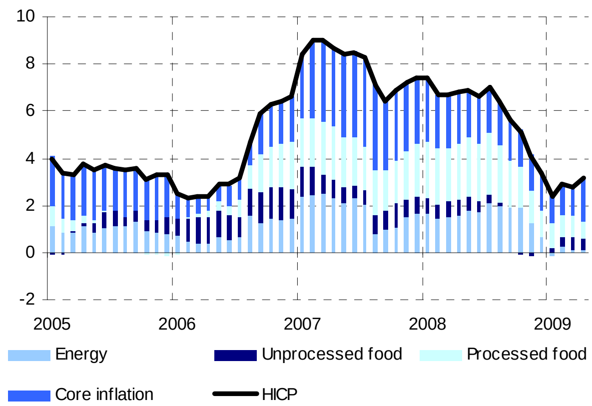
source: Ecowin Economic

Inflation and labour costs

In the second half of 2008, disinflation processes returned. In the fourth quarter of 2008, HICP indicator decreased by 0.3% as compared to the third quarter and was higher by 4.2% than in the same quarter of the previous year (as compared to average HICP increase by 6.7% y/y in the first three quarters of 2008).

Figure 10.8

HICP and its components (in pp, y/y)



source: Ecowin Economic

In 2009, inflation rose again (to 3.2% in April 2009), mainly due to a strong depreciation of the Hungarian forint. After a considerable fall in the growth in food and energy prices in the third quarter of 2008, it stabilised in the fourth quarter. This tendency continued also at the beginning of this year. A considerable appreciation of the Hungarian forint in the time of large openness of the Hungarian economy may create a significant inflation pressure, but base effects related to a considerable increase in food and fuel prices in the first half of 2008 played a big role in determining the inflation level.

Table 10.2
HICP and its components (in pp, y/y)

	Q2 2008	Q3 2008	Q4 2008	Q1 2009	04 2009
HICP	**6,8**	**6,3**	**4,2**	**2,7**	**3,2**
Categories with largest contribution					
Housing	1,4	1,8	2,0	1,4	1,2
Food and non-alcoholic beverages	2,7	2,1	0,9	0,9	0,7
Alcohol beverages and tobacco products	0,4	0,5	0,4	0,4	0,4
Restaurants and hotels	0,6	0,6	0,5	0,4	0,4
Recreation and culture	0,2	0,2	0,2	0,2	0,2

source: Ecowin Economic

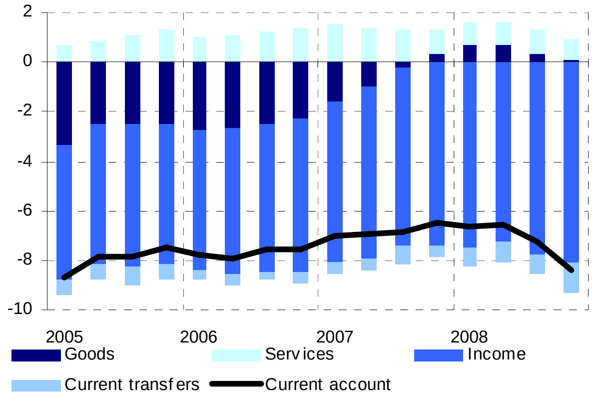
In the fourth quarter of 2008 and at the beginning of this year, PPI inflation gradually decreased (from 7.6% y/y in October 2008 to 4.6% y/y in January this year), which resulted from a decrease in raw material prices. In February this year, PPI inflation rose temporarily to 8.0% y/y, due to a delayed increase in prices of imported goods as a result of depreciation of the Hungarian forint.

In the third and fourth quarter 2008, salaries decreased as compared to the same quarters of the previous year by 1.4% and 0.5% respectively. As recession deepens, inflation-based pressure on wages is expected to become weaker.

External imbalances

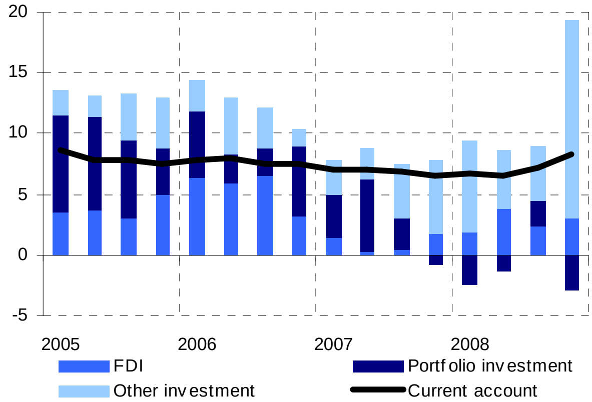
In 2008, and in particular in its second half, current account deficit increased significantly. At the end of 2008, it amounted to 8.4% GDP as compared to 6.4% at the end of 2007, 6.7% in the second half of the year and 7.4% in the third quarter. Deterioration of the current account balance in 2008 was caused mainly by much worse income balance, arising from an increase in foreign debt servicing cost. At the same time, some adjustment took place in the fourth quarter of 2008 to decrease deficit on the current account. Deficit on the current account slightly narrowed due to a fall in dividends paid out by foreign companies.

Figure 10.5
Current account balance and its components (in % of GDP, 4Q moving average)



source: Ecowin Economic

Figure 10.6
Financial account balance and its components (in % of GDP, 4Q moving average)



source: Ecowin Economic

In the fourth quarter of 2008, a surplus on the financial account grew considerably. However, this results mainly from the fact that the consortium consisting of the IMF, EU and World Bank granted a loan in October 2008 (a significant increase in a surplus for the category of other investments, in particular for the governmental sector). However, at the same time, there was an outflow of portfolio investments, in particular from the treasury bonds market, and - to a lesser extent – from the equity market. Deficit on the current account in the third quarter of 2008 was financed to a lesser extent by transactions which did not increase debt (a considerable outflow of direct investments and investments on the equity market was observed). As a result, Hungarian foreign debt increased, and amounted to 113.2% GDP at the end of 2008 (as compared to 97% at the end of 2007)[34]. Furthermore, significant risk aversion on international financial markets resulted in reducing maturity of rolled debt, which led to an increase in the share of short-term debt in total foreign debt. The ratio of foreign short-term debt to GDP in 2008 amounted to 18% as compared to 15% at the beginning of 2008.

Table 10.3

Balance of payments (EUR mn)

	Q4 2007	Q1 2008	Q2 2008	Q3 2008	Q4 2008
Current account	-1420	-1636	-1946	-2492	-2584
Goods	194	377	169	-206	-931
Services	144	73	301	582	40
Income	-1846	-1832	-2121	-2510	-2109
Current transfers	87	-255	-296	-357	-422
Capital account	348	791	128	145	
Financial account	1442	2511	3024	2723	9483
Direct investments	782	546	1569	-373	149
Portfolio investments	-339	185	1043	1560	-5566
Other investments	998	1780	411	1537	13566

source: Ecowin Economic

Interest rates and foreign exchange rate

In the period August 2008 – April 2009, the Hungarian forint depreciated against the euro by 19.2%. This depreciation was particularly strong at the beginning of March this year when EUR/HUF exchange rate was at a historical record level of 314.47. However, a decreasing aversion to risk on international financial markets as compared to emerging markets enabled appreciation of the forint against the euro (to 280 HUF at the end of May this year).

After a surprising increase in reference interest rate by 300 bps in October 2008, the MNB started a series of reductions in interest rates. Until the end of January this year, reference rate was decreased by 200 bps in total to 9.5%, but afterwards, due to an increasing risk of high inflation resulting from a sudden depreciation of the forint, the MNB decided to abstain from further reductions in interest rates.

Following a period of increasing investor confidence and decreasing yield of the Hungarian bonds, which occurred after Hungary was granted aid by the consortium of the IMF, World Bank and European Union in autumn 2008, yield on bonds increased again in March this year reaching the level higher than the one observed at the beginning of the financial crisis. At the end of March this year, yield on 10-year Hungarian treasury bonds exceeded 12% p.a., while just after an increase in interest rates in October, an increase in yield stopped at 10.9% p.a. This was related to a radical decrease in demand for Hungarian debt securities in the light of high aversion to Central and Eastern European economies by investors and unstable financial situation of Hungary. However, as risk appetite increased again, yield on 10-year bonds fell and reached 10.5% at the end of April this year.

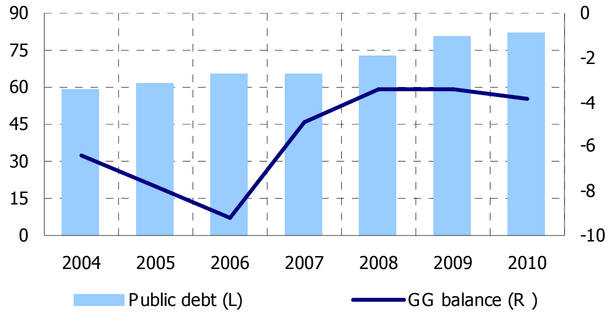
Fiscal policy

In 2008, general government deficit in Hungary amounted to 3.4% GDP as compared to 4.9% GDP in 2007 and 9.2% GDP in 2006. A decline in deficit last year was possible owing to a fiscal consolidation made in 2007, as a result of which public expenditures grew in 2008 in nominal terms by mere 4.4% y/y, whereas public revenues increased considerably by 7.9% y/y.

Despite a significant decline in general government deficitr in the recent years, Hungary is still exposed to threats related to a high level of foreign public debt. Therefore, the crisis hit Hungary particularly hard, causing a rapid depreciation of Hungarian currency and turmoil on the financial market in Hungary. In the economic programme adopted for 2009, the government sets more ambitious fiscal objectives as well as a rescue package for banks and improvement of the financial sector regulations. To support these activities, Hungary was granted a considerable international financial aid from the EU, IMF and World Bank (EUR 20 billion), depending on the progress in budget consolidation, implementation of the budget management reform, reform of regulations and supervision over financial sector as well as structural reforms. The economic programme related to the loan was reflected in the budget for 2009. The updated Convergence Report assumes that general government deficit will decrease in 2009 to 2.6% GDP. Given the financial crisis as well as considerable deficit and public debt, the government did not adopt any budgetary stimulating measures.

[34] Gross debt, including inter-corporate loans, data does not include SPE (*special purpose entities*).

Figure 10.8
General government balance and debt (in % of GDP)



source: Eurostat

However, in the light of more considerable economic slowdown than previously expected, which means that public finance revenues will be lower by approx. 1% GDP, the government adopted in February this year an additional recovery package amounting to 0.7% GDP and revised deficit for 2009 to 2.9% GDP (as per fiscal notification in spring). According to the European Commission, deficit of the public finance sector will probably amount to 3.4% GDP (forecast from May 2009).

The governmental package of actions comprised changes in the country's tax system, pension system as well as administrative and social expenses. Governmental proposals comprised inter alia:

- reducing income tax rates and social insurance contributions, while raising indirect tax rates, extending tax base and eliminating tax relieves,
- reducing social expenditures (inter alia scholarships for students, price subsidies for households) and better use of social aid,
- changing principles for valorisation of pension and disability benefits and eliminating 13th pension for new beneficiaries from 2010,
- reducing current expenditures of the public finance sector by limiting the number of members of the Parliament, conducting a reform of local governments.

In order to support a global demand and employment in the years 2009-2010, measures adopted by Hungarian government comprised, in particular, acceleration of absorption of EU structural funds and their reorientation as well as improving access to financing sources for new and medium-sized enterprises.

The IMF and EC accepted an increase in deficit of the public finance sector this year from 2.9% GDP to 3.9% GDP due to an estimated deeper fall in GDP in Hungary this year (7% as compared to 1%).

Forecasts

External centres and the Bank of Hungary expect a further decline in GDP in 2009 and a slow recovery from recession in 2010, whereas forecasts are gradually being revised down. In particular in 2009 it is expected that household consumption expenditures and investment expenditures will fall considerably.

Disinflation processes observed on the turn of 2008 and 2009 may be stopped in the second half of this year due to planned increases in indirect tax rates. An increase in inflation may be also stimulated by a base effect related to a significant decline in food and energy prices in the second half of 2008.

In the foreseeable future it may be expected that deficit on the current account will decrease due to a decline in deficit in foreign trade (a fall in imports as a result of a decrease in consumption and investment expenditures) and probably a lower extent of profit repatriation by foreign investors due to a lower profitability of Hungarian companies.

Table 10.4
Forecasts of main indicators

	EC	IMF	Consensus Economics	MNB
	05.2009 (11.2008)	04.2009 (10.2008)	04.2009 (11.2008)	02.2009 (11.2008)
GDP, in %, y/y				
2008	0,5 (1,7)	0,6 (1,9)	0,5 (1,4)	0,6 (1,0-1,1)
2009	-6,3 (0,7)	-3,3 (2,3)	-5,2 (-0,6)	-3,5 (-1,7--1,2)
2010	-0,3 (1,8)	-0,4 (3,0)	-0,4	-0,5 (0,5-2,0)
Inflation, in %, y/y				
2008	6,0 (6,3)	6,1 (6,3)	6,1 (6,3)	6,1 (6,2)
2009	4,4 (3,9)	3,8 (4,1)	3,4 (3,7)	3,7 (3,1-3,4)
2010	4,1 (2,9)	2,8 (3,0)	3,2	2,8 (1,5-1,9)
Current account balance, in % of GDP				
2008	-8,4 (-6,3)	-7,8 (-5,5)		-7,9 (-7,2--7,0)
2009	-5,0 (-5,1)	-3,9 (-6,1)		-3,9 (-4,9—4,0)
2010	-4,8 (-5,5)	-3,4 (-6,2)		-4,5 (-4,4--4,3)

MNB - Magyar Nemzeti Bank

Statistical annex

1. National accounts

Table 1. Gross domestic product (in %, y/y)

	2006	2007	I 2008	II 2008	III 2008	IV 2008	I 2009
Poland	6,2	6,6	6,0	5,8	4,8	2,9	
Czech Rep.	6,4	6,5	4,4	4,4	4,0	1,0	-3,4
Slovakia	8,5	10,4	8,7	7,6	7,1	2,5	-5,4
Slovenia	5,7	6,1	5,7	5,5	3,9	-0,8	
Hungary	3,9	1,3	1,7	2,0	0,8	-2,3	-4,7
Estonia	11,2	7,1	0,2	-1,1	-3,5	-9,4	-15,6
Lithuania	7,7	8,8	7,0	5,2	2,9	-2,2	-10,9
Latvia	12,2	10,3	0,5	-1,9	-5,2	-10,5	-18,6
Bulgaria	6,3	6,2	7,0	7,1	6,8	3,5	-3,5
Romania	7,9	6,0	8,2	9,3	9,2	2,9	-6,4
EU-15	2,9	2,9	1,8	2,1	0,8	-1,9	

Source: National statistical offices

Table 2. Private consumption (in %, y/y)

	2006	2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Poland	4,9	5,2	3,5	5,6	5,5	5,1	5,2
Czech Rep.	5,4	5,7	3,7	2,7	3,4	3,0	2,6
Slovakia	5,9	7,1	5,8	8,4	5,7	6,0	4,7
Slovenia	4,0	3,1	5,6	3,7	3,5	0,6	1,1
Hungary	1,9	-0,3	0,8	0,5	1,3	0,1	-4,4
Estonia	15,1	8,9	3,2	0,1	-2,0	-3,5	-10,4
Lithuania	11,8	11,5	12,5	11,1	7,3	4,7	1,5
Latvia	21,4	14,0	1,6	-0,5	-8,4	-13,3	-20,1
Bulgaria	9,5	5,3	3,4	5,7	5,3	5,9	1,8
Romania	12,6	10,4	7,6	14,3	11,8	14,6	-3,7
EU-15	2,0	1,9	2,0	1,7	1,1	0,5	-0,7

Source: National statistical offices

Table 3. Gross fixed capital formation(in %, y/y)

	2006	2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Poland	15,6	19,3	15,2	15,7	15,2	3,5	3,5
Czech Rep.	5,5	6,1	6,5	4,5	4,5	3,4	0,3
Slovakia	8,1	8,2	7,0	7,5	11,8	7,3	1,4
Slovenia	8,2	17,6	4,2	16,9	10,3	4,5	-5,3
Hungary	-2,5	0,7	4,0	-5,1	-1,9	-1,5	-2,7
Estonia	22,4	7,8	-3,0	0,6	-2,5	-6,0	-24,0
Lithuania	17,4	15,8	10,9	1,6	-2,3	-3,3	-18,9
Latvia	16,4	8,4	0,9	-7,2	-11,8	-16,9	-15,0
Bulgaria	14,7	21,7	14,0	15,5	28,6	22,3	15,8
Romania	19,3	28,9	28,0	33,2	30,0	24,3	2,8
EU-15	5,9	4,9	3,5	2,2	1,9	-0,8	-5,8

Source: National statistical offices

Table 4. Exports of goods and services (in %, y/y)

	2006	2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Poland	14,6	8,4	8,4	11,1	8,5	7,1	-2,6
Czech Rep.	14,4	14,5	13,6	13,9	14,9	8,9	-9,1
Slovakia	21,0	16,0	11,6	11,2	8,1	2,7	-7,8
Slovenia	12,5	13,1	10,1	7,6	8,0	4,2	-6,2
Hungary	19,0	14,2	12,2	15,1	9,3	3,5	-7,8
Estonia	8,3	1,5	-1,3	-2,1	-4,9	6,3	-3,2
Lithuania	12,2	4,7	0,6	9,8	13,7	11,3	11,0
Latvia	6,5	11,1	13,1	2,9	0,5	-2,1	-6,1
Bulgaria	8,7	5,2	6,0	9,2	5,1	3,8	-6,0
Romania	10,6	8,8	13,7	25,3	30,4	22,0	1,6
EU-15	8,8	4,4	3,9	4,0	4,6	2,0	-5,6

Source: National statistical offices

Table 5. Imports of goods and services (in %, y/y)

	2006	2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Poland	17,4	12,4	11,5	11,5	8,7	5,9	-0,3
Czech Rep.	13,8	13,7	11,4	12,3	10,5	4,3	-7,0
Slovakia	17,7	10,4	10,2	10,6	7,7	3,6	-6,7
Slovenia	12,3	14,3	11,0	9,7	9,2	3,0	-6,6
Hungary	14,7	12,1	10,0	12,6	10,2	2,8	-8,2
Estonia	17,1	2,8	-0,3	-6,3	-8,2	-5,1	-11,9
Lithuania	13,8	9,1	4,6	18,5	12,1	10,9	0,3
Latvia	19,3	15,0	-0,2	-6,4	-11,7	-15,1	-20,7
Bulgaria	14,0	9,9	5,7	5,8	13,7	4,2	-3,2
Romania	22,4	26,1	30,2	35,1	29,1	20,7	-10,2
EU-15	8,6	4,3	4,1	3,3	3,6	1,8	-3,8

Source: National statistical offices

2. Indices of business cycle and economic activity

Table 6. Industrial production (in %, y/y)

	2006	2007	10.2008	11.2008	12.2008	01.2009	02.2009	03.2009
Poland	12,0	9,7	-2,0	-10,7	-5,6	-15,3	-14,6	-2,0
Czech Rep.	11,2	8,3	-9,8	-18,0	-12,8	-22,8	-23,4	-17,5
Slovakia	9,8	13,1	-1,2	-15,5	-19,1	-26,9	-26,4	-15,9
Slovenia	7,3	7,1	-3,1	-14,0	-15,8	-20,0	-21,2	
Hungary	10,3	8,3	-7,2	-12,1	-20,8	-22,9	-28,9	
Estonia	7,4	6,8	-13,7	-21,3	-17,7	-29,0	-33,0	-25,7
Lithuania	7,4	4,1	1,0	-2,6	-0,8	-7,0	-15,5	-17,9
Latvia	7,8	0,4	-9,4	-13,9	-13,7	-23,9	-24,2	
Bulgaria	6,1	9,2	-2,3	-9,3	-8,3	-16,7	-17,1	-20,7
Romania	7,2	5,4	1,3	-9,5	-12,5	-16,4	-14,5	-8,5
EU-15	3,4	3,1	-6,9	-9,2	-11,3	-14,6	-17,1	

Source: National statistical offices

Table 7. Retail sales (in %, y/y)

	2006	2007	10.2008	11.2008	12.2008	01.2009	02.2009	03.2009
Poland	11,9	14,6	5,0	1,1	6,2	1,4	-2,3	-1,8
Czech Rep.	6,5	7,8	-0,4	-4,7	0,1	-3,4	-7,9	
Slovakia	6,5	5,4	7,2	4,4	5,3	-3,3	-10,3	-7,5
Slovenia	6,5	9,6	2,8	1,0	3,1	-1,3	-13,9	-8,4
Hungary	4,4	-2,8	-1,3	-1,8	-3,2	-2,8	-3,2	
Estonia	19,0	15,2	-5,7	-8,9	-9,0	-11,3	-18,4	-14,3
Lithuania	14,5	17,7	-5,2	-11,4	-8,8	-27,7	-31,5	-30,8
Latvia	19,8	19,9	-14,5	-15,3	-16,9	-20,0	-26,0	-27,3
Bulgaria	6,6	4,9	1,4	-5,5	-7,5			
Romania	24,3	16,4	8,4	2,4	3,0			
EU-15	0,5	0,6	-1,5	-1,9	-0,1			

Source: National statistical offices

Table 8. Consumer confidence index

	2006	2007	11.2008	12.2008	01.2009	02.2009	03.2009	04.2009
Poland	-12,7	-5,0	-16,1	-17,7	-21,0	-34,2	-34,3	-30,0
Czech Rep.	1,9	-2,2	-13,8	-20,9	-25,7	-27,6	-23,3	-20,6
Slovakia	-9,8	-0,2	-26,9	-29,2	-31,9	-43,1	-44,1	-44,9
Slovenia	-14,2	-9,8	-27,7	-30,4	-39,7	-35,7	-36,5	-41,0
Hungary	-32,9	-48,3	-54,3	-58,0	-63,6	-66,5	-67,6	-70,0
Estonia	10,1	2,8	-30,9	-30,7	-32,9	-34,5	-38,6	-32,8
Lithuania	0,4	4,6	-38,9	-48,5	-56,1	-53,7	-54,1	-54,6
Latvia	-5,0	-7,8	-36,5	-47,5	-52,7	-53,6	-51,7	-41,8
Bulgaria	-31,1	-26,4	-40,2	-45,1	-45,2	-45,2	-45,2	-49,9
Romania	-22,9	-14,3	-23,8	-31,3	-38,9	-41,5	-43,6	-45,6

Source: European Commission

Table 9. Business confidence index

	2006	2007	11.2008	12.2008	01.2009	02.2009	03.2009	04.2009
Poland	-8,0	-0,7	-16,5	-20,8	-25,0	-27,9	-28,4	-26,4
Czech Rep.	10,8	15,4	-17,7	-30,7	-33,0	-35,1	-32,5	-26,0
Slovakia	9,0	14,2	-18,9	-25,6	-32,3	-27,1	-31,0	-30,9
Slovenia	9,5	12,3	-24,9	-30,3	-35,2	-34,3	-35,0	-35,0
Hungary	-0,7	0,3	-23,8	-27,1	-30,7	-30,7	-35,1	-33,5
Estonia	20,1	15,1	-26,3	-31,1	-28,3	-36,0	-39,1	-35,5
Lithuania	5,1	5,7	-25,9	-27,6	-29,0	-30,7	-34,4	-37,5
Latvia	6,0	4,8	-25,2	-29,4	-32,3	-36,7	-36,1	-28,8
Bulgaria	4,8	11,7	1,4	-4,4	-6,0	-6,4	-9,6	-9,8
Romania	2,1	3,0	-6,1	-9,0	-10,4	-15,7	-16,7	-14,2

Source: European Commission

Table 10. PMI manufacturing

	2006	2007	11.2008	12.2008	01.2009	02.2009	03.2009	04.2009
Poland	53,9	52,9	40,5		40,3	40,8	42,2	42,1
Czech Rep.	55,7	56,8	37,8		31,5	32,6	34,0	38,6
Hungary	54,0	53,6	39,9	41,0	38,6	39,7	39,5	40,4

Source: EcoWin Economic

3. Prices

Table 11. CPI (in %, y/y)

	09.2008	10.2008	11.2008	12.2008	01.2009	02.2009	03.2009	04.2009
Poland	4,5	4,2	3,7	3,3	2,8	3,3	3,6	4,0
Czech Rep.	6,6	6,0	4,4	3,6	2,2	2,0	2,3	1,8
Slovakia	5,4	5,1	4,9	4,4	3,4	3,1	2,6	2,3
Slovenia	5,5	4,9	3,1	2,1	1,6	2,1	1,8	1,1
Hungary	5,7	5,1	4,2	3,5	3,1	3,0	2,9	3,4
Estonia	10,5	9,8	8,0	7,0	4,1	3,4	2,0	0,3
Lithuania	11,0	10,5	9,1	8,5	9,6	8,7	7,7	6,3
Latvia	14,9	13,8	11,8	10,6	9,9	9,6	8,3	6,2
Bulgaria	11,0	10,9	9,1	7,8	7,1	6,0	4,9	4,8
Romania	7,3	7,4	6,7	6,3	6,7	6,9	6,7	6,5

Source: National statistical offices

Table 12. PPI (in %, y/y)

	08.2008	09.2008	10.2008	11.2008	12.2008	01.2009	02.2009	03.2009
Poland	5,8	5,7	4,7	3,8	3,5	4,2	4,8	
Czech Rep.	5,7	5,6	4,0	1,3	-0,1	-0,8	-0,6	-2,0
Slovakia	6,8	6,8	7,5	6,7	6,1	3,7	1,8	0,5
Slovenia	6,7	5,7	5,0	4,0	3,5	2,4	1,2	0,8
Hungary	13,1	12,9	13,2	10,8	8,3	4,0	6,2	4,6
Estonia	10,5	9,0	10,0	9,1	8,0	5,8	4,4	
Lithuania	20,7	18,4	15,0	9,5	4,8	1,9	-0,1	-2,7
Latvia	15,3	14,7	16,5	15,7	14,6	12,7	9,4	
Bulgaria	16,5	14,4	13,0	7,5	4,7	2,2	0,5	-1,1
Romania	16,6	14,7	13,2	10,1	6,9	6,4	5,8	3,8
EU-15	-0,8	-0,3	-1,2	-2,1	-1,6	-0,8	-0,4	-0,6

Source: National statistical offices

Table 13. HICP (in %, y/y)

	09.2008	10.2008	11.2008	12.2008	01.2009	02.2009	03.2009	04.2009
Poland	4,1	4,0	3,6	3,3	3,2	3,6	4,0	4,3
Czech Rep.	6,4	5,7	4,1	3,3	1,4	1,3	1,7	1,3
Slovakia	4,5	4,2	3,9	3,5	2,7	2,4	1,8	1,4
Slovenia	5,6	4,8	2,9	1,8	1,4	2,1	1,6	1,1
Hungary	5,6	5,1	4,1	3,4	2,4	2,9	2,8	3,2
Estonia	10,8	10,1	8,5	7,5	4,7	3,9	2,5	0,9
Lithuania	11,3	10,7	9,2	8,5	9,5	8,5	7,4	5,9
Latvia	14,7	13,7	11,6	10,4	9,7	9,4	7,9	5,9
Bulgaria	11,4	11,2	8,8	7,2	6,0	5,4	4,0	3,8
Romania	7,3	7,4	6,8	6,4	6,8	6,9	6,7	6,5
EU-15	3,9	3,4	2,4	1,9	1,4	1,6	1,0	

Source: Eurostat

Table 14. HICP – unprocessed food (in %, y/y)

	09.2008	10.2008	11.2008	12.2008	01.2009	02.2009	03.2009	04.2009
Poland	1,3	1,7	1,5	3,4	4,0	5,2	7,9	9,9
Czech Rep.	0,9	0,2	-2,0	-2,2	-2,5	0,6	1,6	0,7
Slovakia	3,8	0,7	0,4	0,0	-0,8	-1,1	-1,7	-3,6
Slovenia	3,1	2,8	2,0	-0,3	2,4	5,3	4,8	3,3
Hungary	-0,3	-1,5	-2,0	-0,6	2,2	5,2	6,5	6,0
Estonia	9,6	6,9	3,2	4,1	2,1	1,7	1,7	-2,7
Lithuania	16,3	14,9	15,3	14,9	14,8	12,9	10,1	7,5
Latvia	13,5	13,2	10,9	11,2	13,5	12,6	9,7	5,4
Bulgaria	5,3	11,9	9,8	6,8	7,8	4,6	3,8	2,0
Romania	3,3	4,1	4,3	4,6	4,8	5,4	5,7	4,8

Source: Eurostat

Table 15. HICP – processed food (including alcohol beverages and tobacco products) (in %, y/y)

	09.2008	10.2008	11.2008	12.2008	01.2009	02.2009	03.2009	04.2009
Poland	7,6	6,5	5,9	5,5	5,2	5,3	5,9	6,2
Czech Rep.	10,9	9,4	5,6	4,2	3,4	2,3	3,1	2,3
Slovakia	8,1	6,8	6,2	5,8	4,6	3,7	2,5	0,8
Slovenia	7,3	5,3	5,9	5,2	3,5	1,6	2,1	1,9
Hungary	10,3	8,7	7,1	5,8	5,1	4,6	4,6	3,4
Estonia	21,3	17,6	15,8	14,5	10,6	9,0	7,5	5,4
Lithuania	14,7	11,9	11,0	10,3	10,0	8,0	7,3	6,5
Latvia	25,1	21,6	18,0	15,5	10,8	10,8	9,1	7,6
Bulgaria	13,0	10,6	8,7	7,0	5,9	4,3	3,1	4,7
Romania	10,0	9,6	8,9	8,3	8,4	8,0	8,0	8,2

Source: Eurostat

Table 16. HICP - energy (in %, y/y)

	09.2008	10.2008	11.2008	12.2008	01.2009	02.2009	03.2009	04.2009
Poland	9,3	9,9	8,2	5,5	5,1	7,2	6,6	7,0
Czech Rep.	11,6	11,8	8,0	5,2	2,5	4,0	4,5	3,7
Slovakia	6,0	6,2	5,2	3,8	1,1	1,1	0,5	0,6
Slovenia	13,3	9,8	-3,5	-9,6	-9,8	-3,1	-6,9	-6,5
Hungary	14,4	14,3	9,3	4,8	-1,0	1,8	1,0	1,1
Estonia	20,9	25,5	19,4	13,1	2,3	2,3	-2,0	-5,2
Lithuania	19,4	19,6	12,5	10,5	13,4	13,5	12,6	11,3
Latvia	28,8	29,7	23,0	18,7	16,7	18,6	15,3	8,5
Bulgaria	16,1	12,5	5,3	-0,1	-3,7	-1,9	-5,3	-4,9
Romania	13,3	11,9	10,2	8,0	8,5	7,7	7,0	6,1

Source: Eurostat

Table 17. HICP – core (in %, y/y)

	09.2008	10.2008	11.2008	12.2008	01.2009	02.2009	03.2009	04.2009
Poland	2,2	2,2	2,1	2,0	1,8	1,8	2,0	2,1
Czech Rep.	4,2	3,7	3,5	3,2	0,9	0,6	0,6	0,4
Slovakia	3,4	3,4	3,4	3,3	3,1	2,8	2,4	2,4
Slovenia	3,8	3,9	3,6	3,6	3,2	3,0	3,0	2,3
Hungary	2,8	2,7	2,6	2,7	2,3	2,3	2,1	3,1
Estonia	5,7	5,1	4,7	4,6	3,6	2,8	2,0	1,3
Lithuania	6,8	7,1	6,3	5,9	7,3	6,6	5,6	4,1
Latvia	8,6	7,9	7,2	6,9	7,3	6,7	5,8	4,8
Bulgaria	10,7	11,0	9,5	9,1	8,2	7,6	6,7	6,1
Romania	4,4	5,3	4,8	5,0	5,7	6,4	6,1	6,1

Source: Eurostat

4. Balance of payments

Table 18. Current account balance (in % of GDP, 4Q moving average)

	I 2007	II 2007	III 2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Poland	-3,1	-3,9	-4,4	-4,7	-4,9	-5,1	-5,1	-5,4
Czech Rep.	-2,3	-2,8	-3,4	-3,2	-2,9	-3,1	-2,6	-3,1
Slovakia	-5,9	-5,2	-4,8	-4,7	-4,8	-5,5	-5,8	-5,7
Slovenia	-2,3	-3,2	-3,7	-4,2	-5,2	-5,6	-5,5	-5,5
Hungary	-7,0	-6,9	-6,8	-6,4	-6,6	-6,5	-7,3	-8,4
Estonia	-18,4	-18,3	-18,7	-18,1	-15,6	-14,3	-12,0	-9,2
Lithuania	-11,7	-14,0	-14,3	-14,6	-15,6	-15,5	-14,5	-13,0
Latvia	-24,2	-24,9	-24,9	-22,5	-20,7	-18,5	-15,2	-13,2
Bulgaria	-20,3	-22,0	-23,9	-25,1	-24,8	-26,8	-25,9	-25,3
Romania	-11,3	-12,0	-12,4	-13,5	-13,9	-14,1	-13,8	-12,3
EU-15	-0,3	-0,2	-0,2	-0,2	-0,2	-0,3	-0,5	-0,8

Source: Eurostat, central banks, own calculations

Table 19. Poland: balance of payments (in % of GDP, 4Q moving average)

	I 2007	II 2007	III 2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Current account	-3,1	-3,9	-4,4	-4,7	-4,9	-5,1	-5,1	-5,4
Goods	-2,5	-3,1	-3,4	-4,0	-4,0	-4,1	-4,3	-4,5
Services	0,4	0,6	0,8	1,1	1,0	1,0	1,0	0,9
Income	-3,2	-3,5	-3,7	-3,8	-3,7	-3,7	-3,5	-3,2
Current transfers	2,2	2,1	2,0	2,0	1,7	1,7	1,7	1,4
Capital account	0,3	0,3	0,3	0,4	0,6	0,6	0,5	0,3
Financial account	4,4	6,1	7,3	9,2	10,4	10,7	9,9	7,2
Direct investments	3,3	3,4	4,4	4,2	3,5	3,4	2,8	2,3
Portfolio investments	-1,9	-1,7	-2,0	-1,2	-1,4	-0,5	0,7	-0,7
Other investments	3,2	4,6	5,2	6,7	8,6	8,0	6,7	5,7

Source: Eurostat, central banks, own calculations

Table 20. Czech Rep.: balance of payments(in % of GDP, 4Q moving average)

	I 2007	II 2007	III 2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Current account	-2,3	-2,8	-3,4	-3,2	-2,9	-3,1	-2,6	-3,1
Goods	2,5	2,8	3,1	3,4	3,3	3,6	3,7	2,8
Services	1,5	1,6	1,6	1,6	1,9	2,0	2,0	2,2
Income	-5,8	-6,5	-7,4	-7,6	-7,7	-8,6	-8,2	-7,8
Current transfers	-0,5	-0,6	-0,6	-0,5	-0,4	-0,1	-0,2	-0,3
Capital account	0,3	0,3	0,3	0,6	0,7	1,0	0,9	0,8
Financial account	2,8	2,9	3,5	3,6	3,2	4,2	3,9	4,1
Direct investments	3,6	3,9	4,1	5,1	4,5	4,9	4,8	4,1
Portfolio investments	-1,3	-0,4	-1,2	-1,6	-1,3	0,1	1,3	-0,2
Other investments	0,4	-0,9	0,6	0,1	0,2	-0,2	-1,9	0,6

Source: Eurostat, central banks, own calculations

Table 21. Slovakia: balance of payments (in % of GDP, 4Q moving average)

	I 2007	II 2007	III 2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Current account	-5,9	-5,2	-4,8	-4,7	-4,8	-5,5	-5,8	-5,7
Goods	-2,7	-2,2	-1,6	-0,6	-0,4	-0,4	-0,6	-0,6
Services	0,9	0,8	0,9	0,6	0,5	0,1	-0,3	-0,6
Income	-3,9	-3,5	-3,4	-4,1	-4,1	-4,4	-4,1	-3,3
Current transfers	-0,2	-0,5	-0,7	-0,6	-0,8	-0,8	-0,9	-1,2
Capital account	0,2	0,2	0,5	0,9	0,9	1,4	1,5	2,0
Financial account	1,6	3,3	9,6	8,6	7,9	5,3	6,0	6,8
Direct investments	6,2	3,9	3,7	3,0	2,5	2,5	1,7	2,3
Portfolio investments	0,7	0,7	0,5	-0,3	1,8	1,0	1,8	2,6
Other investments	1,1	1,6	0,5	0,8	-0,5	-1,1	-1,5	0,6

Source: Eurostat, central banks, own calculations

Table 22. Slovenia: balance of payments (in % of GDP, 4Q moving average)

	I 2007	II 2007	III 2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Current account	-2,3	-3,2	-3,7	-4,2	-5,2	-5,6	-5,5	-5,5
Goods	-3,7	-4,4	-4,7	-4,8	-5,4	-6,1	-6,9	-7,1
Services	3,4	3,6	3,6	3,5	3,6	3,9	4,3	4,8
Income	-1,5	-1,8	-2,1	-2,1	-2,5	-2,6	-2,4	-2,8
Current transfers	-0,5	-0,6	-0,6	-0,8	-0,9	-0,8	-0,6	-0,5
Capital account	-0,4	-0,5	-0,4	-0,2	-0,2	-0,2	-0,2	-0,2
Financial account	4,6	4,8	4,1	5,1	5,4	7,1	7,2	6,2
Direct investments	-1,0	-1,0	-1,4	-0,8	0,4	0,5	0,2	0,7
Portfolio investments	-5,7	-8,7	-6,3	-6,6	-3,8	-3,5	-4,0	1,6
Other investments	6,8	11,0	10,4	12,1	8,9	9,9	10,8	3,8

Source: Eurostat, central banks, own calculations

Table 23. Hungary: balance of payments (in % of GDP, 4Q moving average)

	I 2007	II 2007	III 2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Current account	-7,0	-7,0	-6,9	-6,5	-6,7	-6,6	-7,3	-8,4
Goods	-1,6	-1,0	-0,3	0,3	0,7	0,7	0,4	0,1
Services	1,5	1,4	1,3	1,0	0,9	0,9	1,0	0,9
Income	-6,5	-6,9	-7,1	-7,4	-7,5	-7,3	-7,8	-8,1
Current transfers	-0,5	-0,5	-0,8	-0,5	-0,8	-0,8	-0,8	-1,2
Capital account	0,6	0,8	1,1	1,1	1,8	1,8	1,3	1,1
Financial account	7,8	8,8	7,5	7,1	7,1	7,3	9,0	16,6
Direct investments	1,4	0,3	0,4	1,7	1,9	3,8	2,4	3,1
Portfolio investments	3,6	6,0	2,7	-0,8	-2,5	-1,3	2,0	-2,9
Other investments	2,8	2,6	4,4	6,2	7,6	4,8	4,5	16,5

Source: Eurostat, central banks, own calculations

Table 24. Estonia: balance of payments (in % of GDP, 4Q moving average)

	I 2007	II 2007	III 2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Current account	-18,4	-18,3	-18,7	-18,1	-15,6	-14,3	-12,0	-9,2
Goods	-19,0	-18,9	-18,5	-17,6	-16,2	-14,5	-13,0	-11,6
Services	6,4	6,6	6,4	6,3	6,7	6,8	7,0	7,2
Income	-6,2	-6,4	-7,1	-7,5	-7,4	-7,9	-7,3	-6,7
Current transfers	0,3	0,5	0,6	0,7	1,3	1,3	1,3	1,9
Capital account	0,6	0,5	0,4	0,4	0,7	0,8	0,8	0,9
Financial account	20,2	19,4	21,4	16,8	15,5	15,8	10,7	11,0
Direct investments	3,7	3,9	4,0	5,3	4,7	5,7	5,5	3,5
Portfolio investments	-2,5	-3,0	-0,8	-2,4	-1,7	0,3	0,5	2,5
Other investments	19,1	18,5	18,4	14,2	12,4	9,8	4,7	4,7

Source: Eurostat, central banks, own calculations

Table 25. Lithuania: balance of payments (in % of GDP, 4Q moving average)

	I 2007	II 2007	III 2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Current account	-11,7	-14,0	-14,3	-14,6	-15,6	-15,0	-14,1	-11,6
Goods	-14,8	-15,7	-15,3	-15,1	-15,4	-14,3	-13,3	-11,6
Services	3,2	2,4	2,2	1,6	1,3	1,2	0,8	1,1
Income	-2,9	-3,1	-3,8	-4,1	-4,3	-4,6	-4,1	-3,3
Current transfers	2,7	2,5	2,7	3,0	2,9	2,7	2,6	2,3
Capital account	0,4	0,4	0,4	0,3	0,8	0,8	0,8	0,8
Financial account	11,2	13,4	12,5	12,9	13,3	12,9	12,4	10,3
Direct investments	5,5	5,9	6,3	3,6	3,1	2,7	2,8	3,1
Portfolio investments	-3,1	-2,5	-2,5	-0,8	0,1	-0,7	0,1	-0,2
Other investments	12,4	14,6	13,0	13,1	11,1	11,5	8,8	5,0

Source: Eurostat, central banks, own calculations

Table 26. Latvia: balance of payments(in % of GDP, 4Q moving average)

	I 2007	II 2007	III 2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Current account	-24,2	-24,9	-24,9	-22,5	-20,7	-18,5	-15,2	-13,2
Goods	-26,0	-26,2	-25,9	-23,9	-22,3	-20,3	-18,3	-16,9
Services	2,9	2,9	3,1	3,4	3,4	3,5	3,6	3,9
Income	-2,5	-3,1	-3,3	-3,3	-3,3	-3,4	-3,0	-2,4
Current transfers	1,4	1,6	1,1	1,3	1,6	1,7	2,4	2,2
Capital account	0,3	0,3	0,2	0,8	0,8	0,8	0,9	0,6
Financial account	23,2	24,2	24,9	21,2	19,7	17,0	13,9	14,3
Direct investments	7,3	8,1	8,3	6,7	6,4	4,9	4,4	4,2
Portfolio investments	0,4	-1,7	-2,0	-2,3	0,4	0,8	1,2	0,9
Other investments	23,1	23,4	22,7	19,5	16,4	13,8	9,7	7,6

Source: Eurostat, central banks, own calculations

Table 27. Bulgaria: balance of payments(in % of GDP, 4Q moving average)

	I 2007	II 2007	III 2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Current account	-20,3	-22,0	-23,9	-25,1	-24,8	-26,8	-25,9	-25,3
Goods	-23,3	-24,3	-24,8	-25,1	-24,9	-26,5	-26,4	-25,7
Services	3,3	3,3	3,3	2,6	2,2	2,0	2,2	2,4
Income	-2,7	-3,1	-3,8	-3,8	-3,4	-4,3	-3,6	-3,5
Current transfers	2,4	2,0	1,4	1,2	1,3	2,1	2,0	1,5
Capital account	0,2	0,3	0,2	0,3	0,8	0,8	0,8	0,6
Financial account	22,2	24,9	27,0	34,7	33,9	34,1	34,2	30,7
Direct investments	23,7	24,4	27,5	28,7	25,8	24,4	21,3	16,7
Portfolio investments	-0,5	-0,4	-0,9	-2,0	-1,1	-1,8	-2,5	-1,5
Other investments	6,6	7,3	12,0	18,1	19,4	22,7	24,2	17,5

Source: Eurostat, central banks, own calculations

Table 28. Romania: balance of payments(in % of GDP, 4Q moving average)

	I 2007	II 2007	III 2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Current account	-11,3	-12,0	-12,4	-13,5	-13,9	-14,1	-13,8	-12,3
Goods	-13,3	-14,0	-14,2	-14,4	-14,5	-14,5	-14,5	-13,3
Services	0,2	0,3	0,3	0,4	0,3	0,3	0,3	0,6
Income	-3,1	-2,9	-3,2	-3,4	-3,8	-3,9	-3,9	-4,0
Current transfers	4,8	4,7	4,6	3,9	4,1	4,1	4,4	4,4
Capital account	-0,1	0,6	0,6	0,7	0,7	0,7	0,5	0,4
Financial account	12,4	12,3	12,6	13,3	12,2	14,2	14,6	12,9
Direct investments	8,9	8,5	8,2	5,7	5,3	6,7	6,4	6,8
Portfolio investments	0,2	0,3	0,6	0,4	0,2	0,1	-0,1	-0,7
Other investments	7,3	7,5	10,0	11,1	10,5	10,6	8,8	7,0

Source: Eurostat, central banks, own calculations

Table 29. Official reserve assets to external debt ratio (in %, end of quarter)

	I 2007	II 2007	III 2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Poland	28,0	28,5	27,2	27,8	27,2	28,3	29,1	24,0
Czech Rep.	55,0	51,1	48,7	45,9	44,2	38,9	40,5	46,0
Slovakia	52,1	53,5	51,9	48,7	46,8	42,1	40,6	43,7
Slovenia	3,0	2,9	2,5	2,1	2,1	1,8	1,8	1,8
Hungary	19,4	18,0	17,2	16,4	16,0	15,7		
Estonia	14,5	12,9	13,8	12,6	12,9	14,0	13,1	14,8
Lithuania	27,5	27,1	26,1	25,8	21,8	21,1	19,5	20,7
Latvia	17,0	16,5	15,6	14,8	15,6	14,7	14,8	13,2
Bulgaria	41,9	41,9	44,9	41,2	40,1	39,4	40,6	34,6
Romania	52,2	48,1	49,8	46,4	44,5	40,3	39,8	38,7

Source: Eurostat, central banks, own calculations

Table 30. Fitch – long-term foreign currency debt rating

	2004	2005	2006	2007	2008	05.2009
Poland	BBB+	BBB+	BBB+	A-	A-	A-
Czech Rep.	A-	A	A	A	A+	A+
Slovakia	A-	A	A	A	A+	A+
Slovenia	AA-	AA-	AA	AA	AA	AA
Hungary	A-	BBB+	BBB+	BBB+	BBB	BBB
Estonia	A	A	A	A	A-	BBB+
Lithuania	A-	A-	A	A	BBB+	BBB
Latvia	A-	A-	A-	BBB+	BBB-	BB+
Bulgaria	BBB-	BBB	BBB	BBB	BBB-	BBB-
Romania	BBB-	BBB-	BBB	BBB	BB+	BB+

Source: FitchRatings

Table 31. Fitch – long-term domestic currency debt rating

	2004	2005	2006	2007	2008	05.2009
Poland	A	A	A	A	A	A
Czech Rep.	A	A+	A+	A+	AA-	AA-
Slovakia	A+	A+	A+	A+	A+	A+
Slovenia	AA	AA	AA	AA	AA	AA
Hungary	A+	A-	A-	A-	BBB+	BBB+
Estonia	A+	A+	A+	A+	A	A-
Lithuania	A	A	A+	A+	A-	BBB+
Latvia	A	A	A	A-	BBB	BBB-
Bulgaria	BBB	BBB+	BBB+	BBB+	BBB	BBB
Romania	BBB	BBB	BBB+	BBB+	BBB-	BBB-

Source: FitchRatings

5. Interest rates and exchange rates

Table 32. Main policy rates (end of month)

	09.2008	10.2008	11.2008	12.2008	01.2009	02.2009	03.2009	04.2009
Poland	6,00	6,00	5,75	5,00	4,25	4,00	3,75	3,75
Czech Rep.	3,50	3,50	2,75	2,25	2,25	1,75	1,75	1,75
Hungary	8,50	11,50	11,00	10,00	9,50	9,50	9,50	9,50
Romania	10,25	10,25	10,25	10,25	10,25	10,00	10,00	10,00
Strefa euro	4,25	3,75	3,25	2,50	2,00	2,00	1,50	1,25

Source: Banki Centralne, EcoWin Financial

Table 33. 3m interbank rates (monthly average)

	09.2008	10.2008	11.2008	12.2008	01.2009	02.2009	03.2009	04.2009
Poland	6,6	6,8	6,7	6,4	5,5	4,7	4,3	4,2
Czech Rep.	3,8	4,2	4,2	3,9	3,1	2,5	2,5	2,5
Slovakia	4,3	4,0	3,5	3,0	2,1	1,8	1,5	1,4
Slovenia	5,0	5,1	4,2	3,3	2,5	1,9	1,6	1,4
Hungary	8,6	9,6	11,6	10,6	9,7	9,5	9,6	9,7
Estonia	6,3	6,7	7,2	7,8	7,3	6,9	7,1	6,5
Lithuania	5,8	7,0	7,9	9,1	8,7	7,2	7,1	6,9
Latvia	6,4	10,0	12,1	13,9	11,9	10,7	12,1	12,4
Bulgaria	7,3	7,7	7,9	7,7	7,0	6,6	6,6	6,0
Romania	13,3	22,2	16,6	15,6	15,2	15,4	15,3	14,2

Source: EcoWin Financial

Table 34. Exchange rates against the euro (monthly average)

	09.2008	10.2008	11.2008	12.2008	01.2009	02.2009	03.2009	04.2009
Poland	3,37	3,58	3,73	4,01	4,23	4,65	4,61	4,40
Czech Rep.	24,42	24,77	25,19	26,12	27,14	28,50	27,14	26,68
Slovakia	30,31	30,27	30,45	30,18	1,00	1,00	1,00	1,00
Slovenia	1,00	1,00	1,00	1,00	1,00	1,00	1,00	1,00
Hungary	240,49	260,74	264,80	264,47	279,61	298,40	303,61	293,67
Estonia	15,64	15,64	15,64	15,64	15,64	15,64	15,64	15,64
Lithuania	3,45	3,45	3,45	3,45	3,45	3,45	3,45	3,45
Latvia	0,70	0,70	0,70	0,71	0,71	0,71	0,71	0,71
Bulgaria	1,96	1,96	1,96	1,96	1,96	1,96	1,96	1,96
Romania	3,62	3,74	3,77	3,92	4,22	4,28	4,28	4,19

Source: Eurostat

Table 35. Exchange rates against the euro (in %, y/y)

	09.2008	10.2008	11.2008	12.2008	01.2009	02.2009	03.2009	04.2009
Poland	-11,0	-3,2	2,1	11,3	17,3	30,3	43,0	28,0
Czech Rep.	-11,4	-9,3	-5,6	-0,7	4,2	12,4	21,2	6,6
Hungary	-4,9	4,0	4,1	4,5	9,4	13,8	28,8	16,0
Romania	8,2	11,7	8,7	11,3	14,6	17,2	19,9	15,3

Source: Eurostat, own calculations

Table 36. NEER (in %, y/y)

	09.2008	10.2008	11.2008	12.2008	01.2009	02.2009	03.2009	04.2009
Poland	10,2	1,1	-4,7	-9,3	-13,9	-22,3	-23,0	-22,5
Czech Rep.	11,5	6,2	2,5	-0,4	-3,6	-10,2	-6,8	-6,5
Slovakia	10,2	7,2	8,3	11,5	13,4	13,1	10,4	9,0
Slovenia	-0,1	-1,1	-1,2	0,4	1,1	1,5	1,4	0,7
Hungary	4,4	-4,0	-6,6	-3,6	-7,9	-11,3	-14,0	-14,3
Estonia	0,5	-1,1	-1,4	1,1	2,4	3,1	3,1	2,1
Lithuania	0,2	-0,5	-0,1	2,3	3,6	4,9	4,6	3,6
Latvia	-0,1	-1,5	-1,6	0,7	2,4	3,1	2,5	1,6
Bulgaria	0,5	-0,4	-0,3	1,3	2,5	2,7	2,2	0,7
Romania	-6,9	-7,6	-7,0	-4,8	-11,0	-12,7	-11,5	-12,9

Source: BIS, own calculations

Table 37. REER (in %, y/y)

	09.2008	10.2008	11.2008	12.2008	01.2009	02.2009	03.2009	04.2009
Poland	10,0	1,1	-3,8	-9,0	-12,8	-20,8	-21,0	-20,2
Czech Rep.	13,4	7,5	4,2	-1,7	-3,2	-9,9	-5,8	-5,8
Slovakia	10,9	8,5	10,4	12,4	15,0	14,6	11,7	10,0
Slovenia	0,6	-0,7	-1,1	0,0	0,8	1,8	1,7	0,5
Hungary	5,1	-2,8	-5,4	-3,4	-6,8	-10,2	-12,6	-12,5
Estonia	6,1	4,1	3,6	3,1	3,9	4,0	2,9	0,3
Lithuania	7,0	6,0	5,5	5,0	10,3	10,9	9,9	7,5
Latvia	4,5	4,5	4,8	6,0	8,9	9,5	9,5	8,8
Bulgaria	6,4	4,8	4,5	4,8	7,2	6,4	5,3	3,8
Romania	-4,9	-5,0	-3,8	-2,0	-7,0	-8,4	-6,9	-8,5

Source: BIS, own calculations

6. Labour market

Table 38. Employment (in %, y/y)

	I 2007	II 2007	III 2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Poland	4,6	4,8	3,5	4,2	4,6	3,5	3,6	3,0
Czech Rep.	1,7	1,8	2,1	2,2	1,9	1,8	1,5	1,3
Slovakia	3,1	1,9	2,0	2,8	2,8	2,9	4,5	2,8
Slovenia	3,3	3,5	3,6	3,7	3,5	3,1	3,0	2,3
Hungary	0,5	0,2	0,0	-1,1	-1,6	-1,9	-0,6	-0,7
Estonia	1,9	1,3	1,9	0,5	1,5	-0,3	-0,2	-0,2
Lithuania	1,6	2,8	3,2	1,8	0,2	-1,2	-1,4	-1,2
Latvia	2,6	3,4	1,1	4,3	4,9	3,1	0,2	-5,5
Bulgaria	2,3	2,8	2,9	3,0	2,3	2,0	1,8	1,1
Romania	6,6	3,6	3,6	4,6	4,9	3,7	3,1	1,7

Source: National statistical offices, own calculations

Table 39. Unemployment rate (in % of labour force)

	09.2008	10.2008	11.2008	12.2008	01.2009	02.2009	03.2009	04.2009
Poland	8,9	8,8	9,1	9,5	10,5	10,9	11,2	11,0
Czech Rep.	5,3	5,2	5,3	6,0	6,8	7,4	7,7	7,9
Slovakia	7,5	7,5	7,8	8,4	9,0	9,7	10,3	
Slovenia	6,3	6,6	6,7	7,0	7,8	8,2		
Hungary	7,7	7,8	8,0	8,4	9,1	9,7		
Estonia	6,2	7,6	7,6	7,6	11,4	11,4	11,4	
Lithuania	5,9	7,9	7,9	7,9				
Latvia	5,3	5,6	6,1	7,0	8,3	9,5	10,7	
Bulgaria	5,8	5,9	5,9	6,3	6,5	6,7	6,9	
Romania	3,9	4,0	4,1	4,4	4,9	5,3	5,6	5,7
EU-15	7,0	7,3	7,5	7,8	8,4	8,7	8,8	

Source: National statistical offices

Table 40. Nominal wages (in %, y/y)

	I 2007	II 2007	III 2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Poland	7,1	8,9	9,7	8,9	10,1	11,6	9,8	6,8
Czech Rep.	7,8	7,4	7,5	6,6	10,2	8,0	7,8	8,3
Slovakia	4,2	4,1	4,2	4,5	5,8	4,8	3,5	-0,2
Slovenia	5,4	5,6	5,8	6,7	7,8	8,6	9,9	7,1
Hungary	-0,3	1,4	-0,1	-1,7	-0,9	0,9	-1,4	-0,5
Estonia	20,1	21,2	20,2	20,2	19,5	15,2	14,8	6,9
Lithuania	20,9	20,2	17,9	18,5	23,8	22,5	19,0	13,0
Latvia	31,6	32,2	32,9	29,7	28,3	23,9	21,0	12,1
Bulgaria	17,6	19,6	21,7	23,2	24,4	24,2	22,6	20,1
Romania	16,8	23,6	24,1	22,7	27,7	25,8	24,7	19,9

Source: National statistical offices, own calculations

Table 41. ULC (in %, y/y)

	I 2007	II 2007	III 2007	IV 2007	I 2008	II 2008	III 2008	IV 2008
Poland	4,3	7,2	6,7	6,6	8,7	9,4	8,6	6,8
Czech Rep.	3,3	3,3	3,8	2,9	7,7	5,4	5,4	9,4
Slovakia	-0,7	-2,5	-4,3	-7,0	-0,7	-0,2	1,4	0,1
Slovenia	1,1	2,6	1,9	5,0	5,5	6,3	8,9	10,2
Hungary	-2,3	0,7	-0,7	-3,3	-4,2	-3,0	-2,8	1,1
Estonia	13,0	15,8	16,6	16,2	20,8	16,0	17,9	16,4
Lithuania	15,5	13,9	10,6	11,5	16,9	16,1	14,4	13,8
Latvia	25,2	26,3	22,6	24,0	32,8	28,9	25,3	16,9
Bulgaria	18,8	15,9	20,4	20,9	22,3	20,7	18,9	18,4
Romania	13,1	20,4	21,1	18,9	21,8	18,5	17,3	18,1

Source: Eurostat, National statistical offices, own calculations

7. Public finance

Table 42. General government balance (in % of GDP)

	2001	2002	2003	2004	2005	2006	2007	2008
Poland	-5,1	-5,0	-6,3	-5,7	-4,3	-3,9	-1,9	-3,9
Czech Rep.	-5,7	-6,8	-6,6	-3,0	-3,6	-2,6	-0,6	-1,5
Slovakia	-6,5	-8,2	-2,7	-2,3	-2,8	-3,5	-1,9	-2,2
Slovenia	-4,0	-2,5	-2,7	-2,2	-1,4	-1,3	0,5	-0,9
Hungary	-4,0	-8,9	-7,2	-6,4	-7,8	-9,2	-4,9	-3,4
Estonia	-0,1	0,3	1,7	1,7	1,5	2,9	2,7	-3,0
Lithuania	-3,6	-1,9	-1,3	-1,5	-0,5	-0,4	-1,0	-3,2
Latvia	-2,1	-2,3	-1,6	-1,0	-0,4	-0,5	-0,4	-4,0
Bulgaria		-0,8	-0,3	1,6	1,9	3,0	0,1	1,5
Romania	-3,5	-2,0	-1,5	-1,2	-1,2	-2,2	-2,5	-5,4
EU-15	-1,2	-2,3	-3,0	-2,8	-2,4	-1,3	-0,8	-1,8

Source: Eurostat

Table 43. Public debt (in % of GDP)

	2001	2002	2003	2004	2005	2006	2007	2008
Poland	37,6	42,2	47,1	45,7	47,1	47,7	44,9	47,1
Czech Rep.	25,1	28,5	30,1	30,4	29,8	29,6	28,9	29,8
Slovakia	48,9	43,4	42,4	41,4	34,2	30,4	29,4	27,6
Slovenia	26,8	28,0	27,5	27,2	27,0	26,7	23,4	22,8
Hungary	52,1	55,7	58,0	59,4	61,7	65,6	65,8	73,0
Estonia	4,8	5,7	5,6	5,0	4,5	4,3	3,5	4,8
Lithuania	23,1	22,3	21,1	19,4	18,4	18,0	17,0	15,6
Latvia	14,0	13,5	14,6	14,9	12,4	10,7	9,0	19,5
Bulgaria	67,3	53,6	45,9	37,9	29,2	22,7	18,2	14,1
Romania	26,0	25,0	21,5	18,8	15,8	12,4	12,7	13,6
EU-15	62,2	61,6	63,0	63,2	64,1	62,8	60,4	62,5

Source: Eurostat