



**World Bank**  
**EU10 Regular Economic**  
**Report**

***Securing***  
***Recovery Amid***  
***Headwinds***

**Warsaw, 18 November 2011**



The World Bank

**EU10**  
**Regular Economic Report**

**Main Report**  
**Securing Recovery Amid Headwinds**

November 2011

**Focus Note:**  
**Skills, Not Just Diplomas**

This report is prepared by a team including Simon Davies, Stella Ilieva, Ewa Korczyk, Matija Laco, Sanja Madzarevic-Sujster, Catalin Pauna, Kaspár Richter (task manager, [krichter@worldbank.org](mailto:krichter@worldbank.org)) and Emilia Strok.

The team is very grateful to Lars Sondergaard for the focus note, and to Marcin Piatkowski, Lucio Vinhas de Souza and the World Bank Global Prospect Group, coordinated by Annette De Kleine, for excellent inputs.

EU10 refers to Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, the Slovak Republic and Slovenia. EU10+1 includes Croatia.



## MESSAGES

- **External headwinds are weighing down on growth in late 2011 and 2012.**
- **Slowing export growth, weakening credit growth, low investment, and persistent unemployment make for a sluggish recovery.**
- **Securing recovery and job creation require shoring up confidence of financial markets, getting the fiscal house in order and pursuing structural reforms**

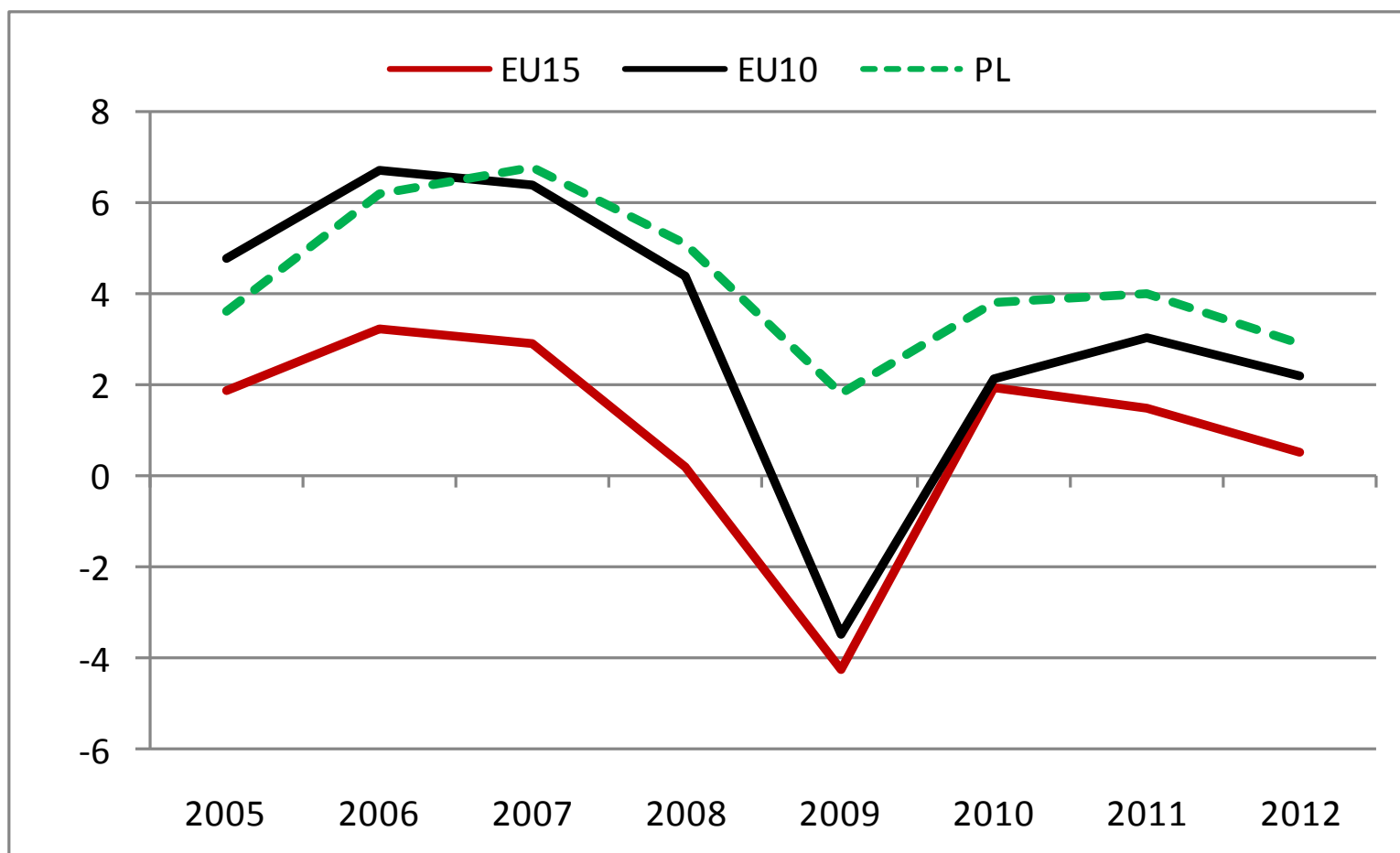


# Recovery Weakening



# Growth in EU10 weakening as growth in EU15 slows down

EU10, EU15 and Poland's projected growth, percent, year-over-year

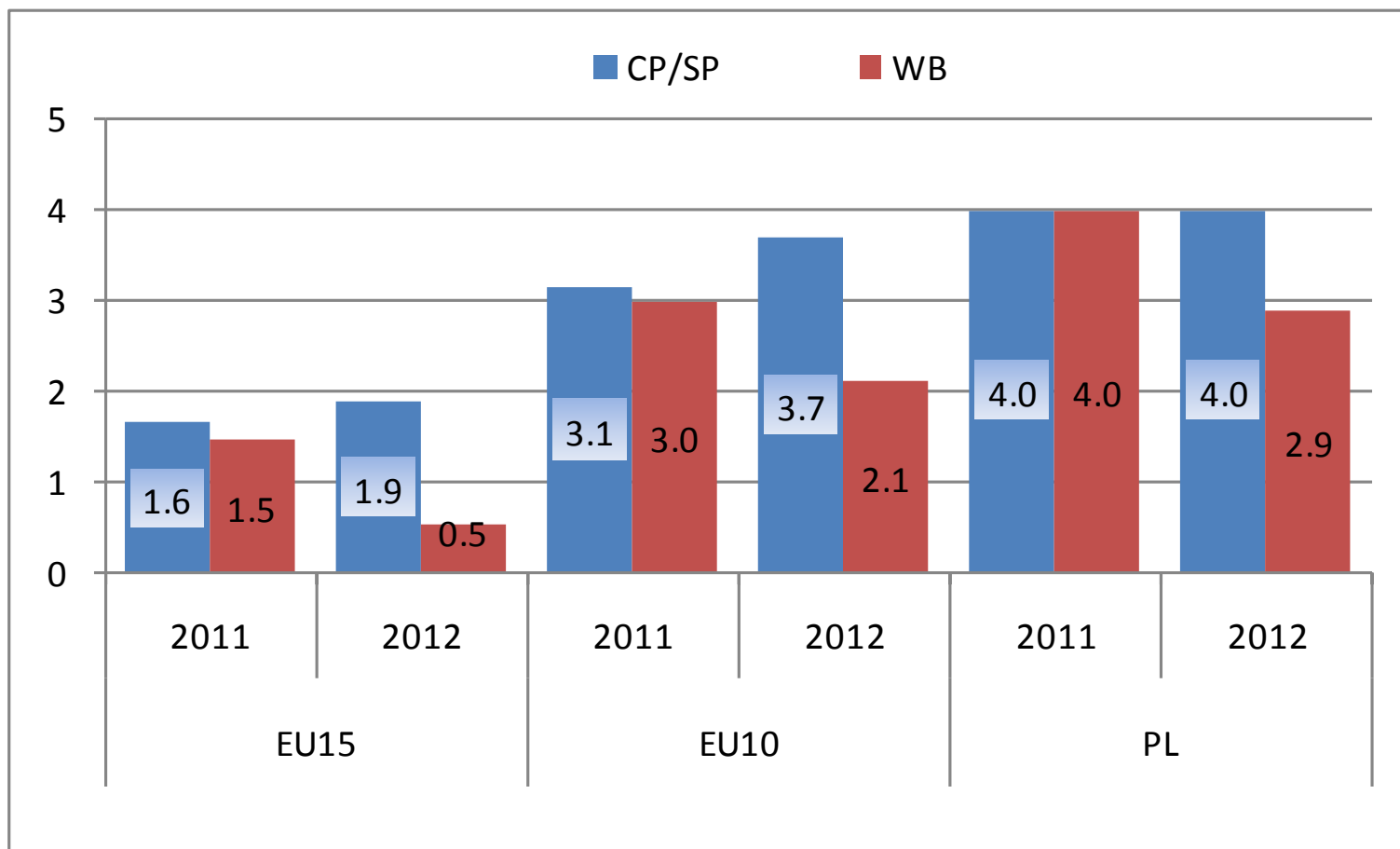


Source: Eurostat, World Bank forecasts from November 2011



# Growth set to be worse than expected

EU10, EU15 and Poland projected growth, percent, year-over-year



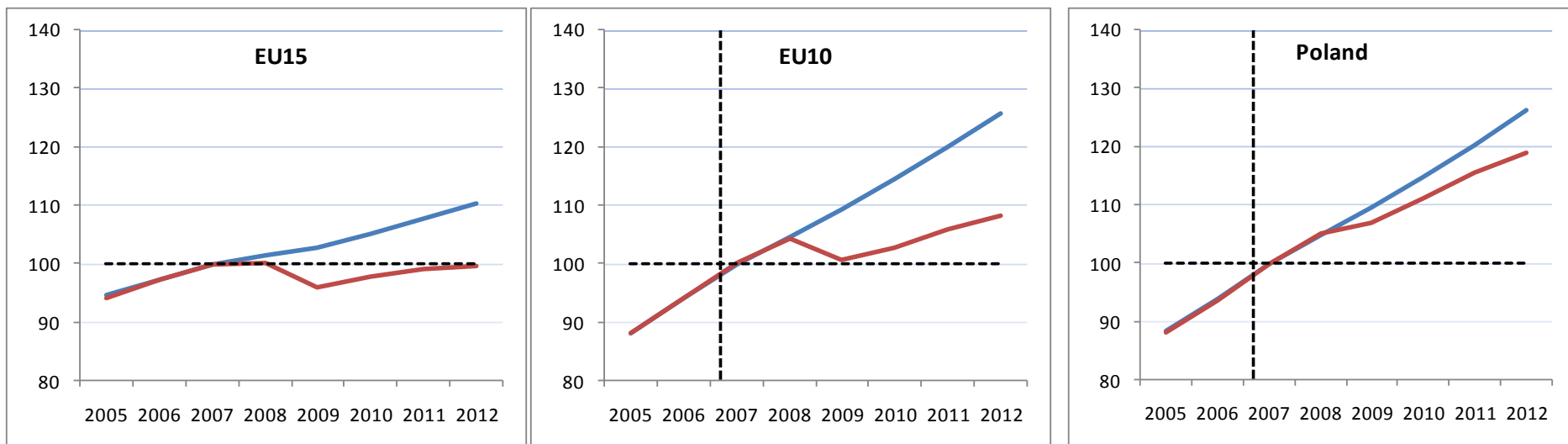
Source: Convergence/Stability Programs from Summer 2011, EC November 2011 Forecast for EU15, for EU10 and Poland World Bank Forecasts from November 2011



# Growth trajectories flatter than pre-crisis

Comparison of growth projections from April 2008 and November 2011 – EU10 and EU15 to 2012

— April 2008 forecasts      — November 2011 forecasts

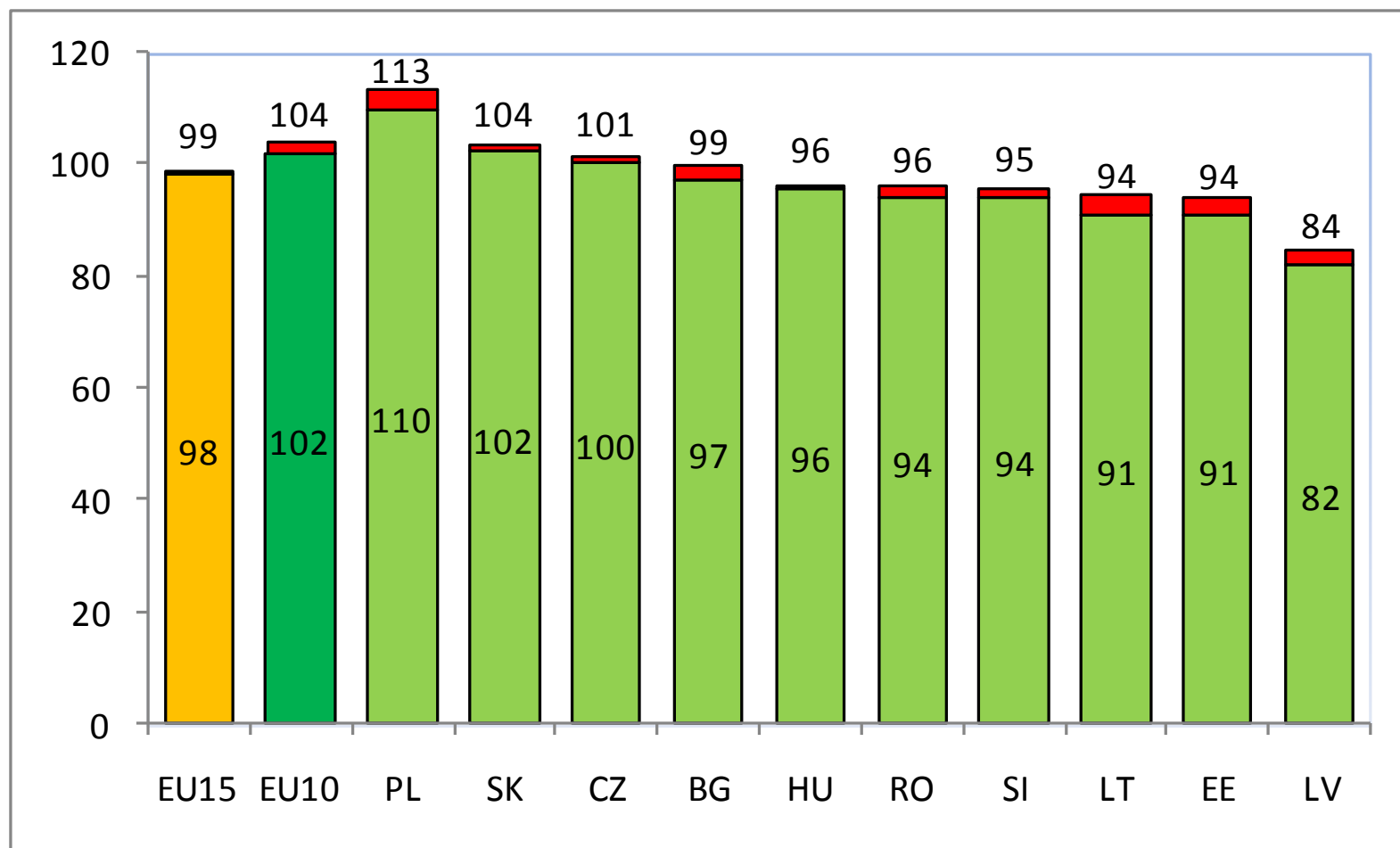


Source: IMF April 2008 WEO, World Bank forecasts from November 2011



# Only 3 EU10 countries above pre-crisis output levels

Level output in 2011 and 2012 as percent of the pre-crisis peak output

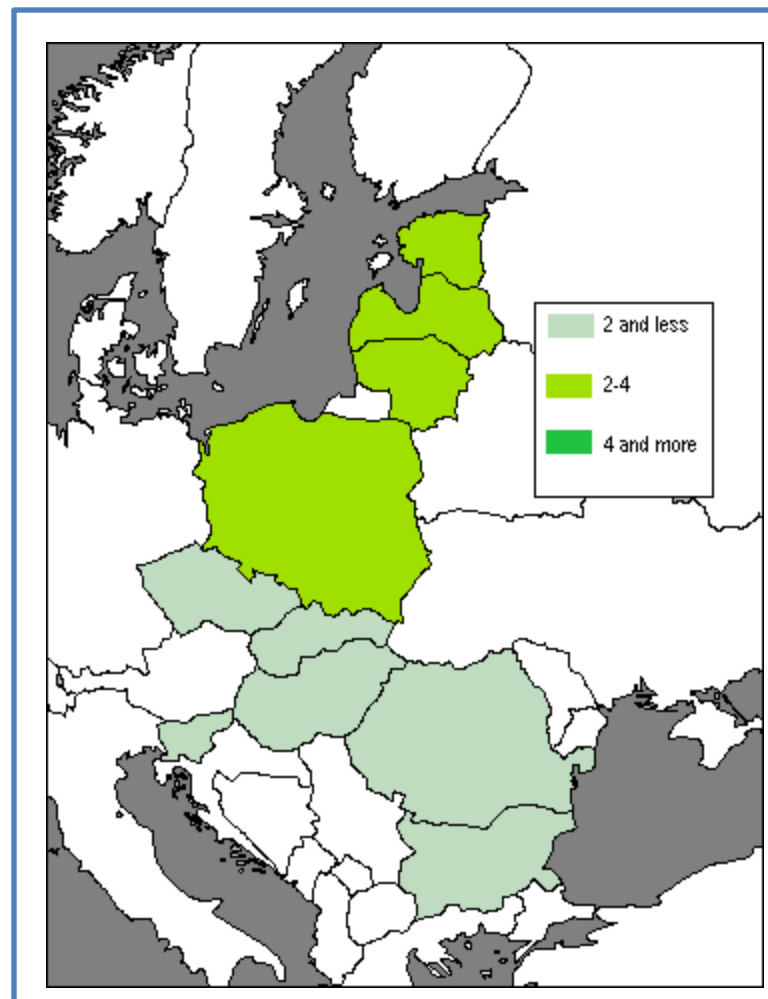
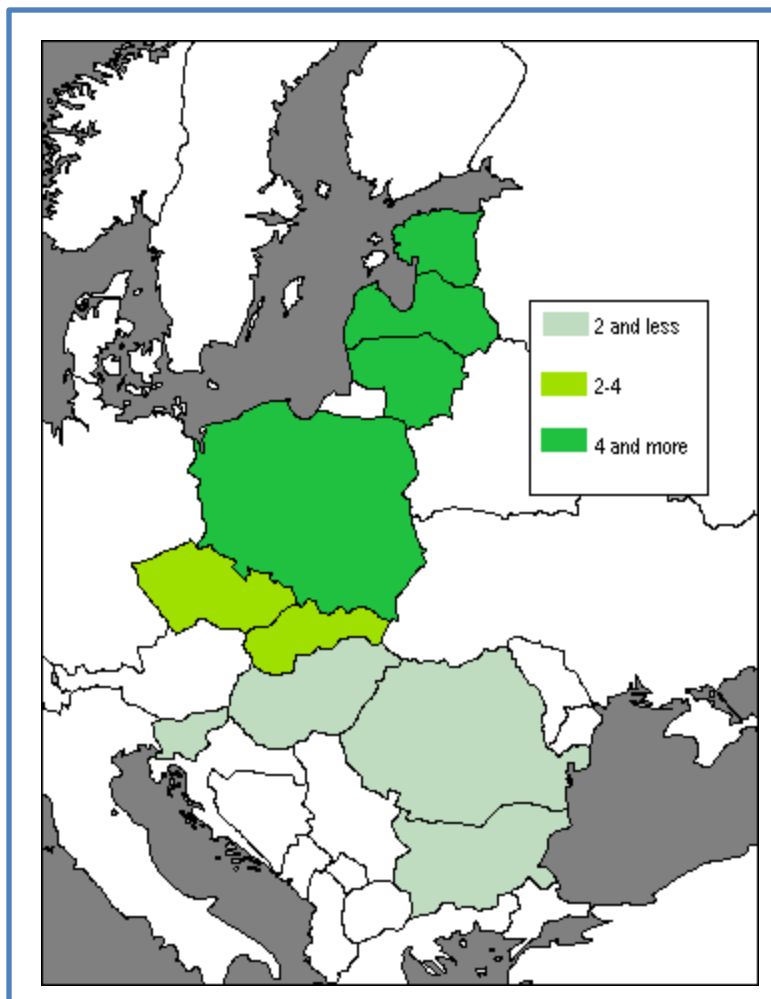


Source: Eurostat, World Bank staff calculations



# From dark green to light green

Projected 2011 and 2012 GDP growth rates, percent



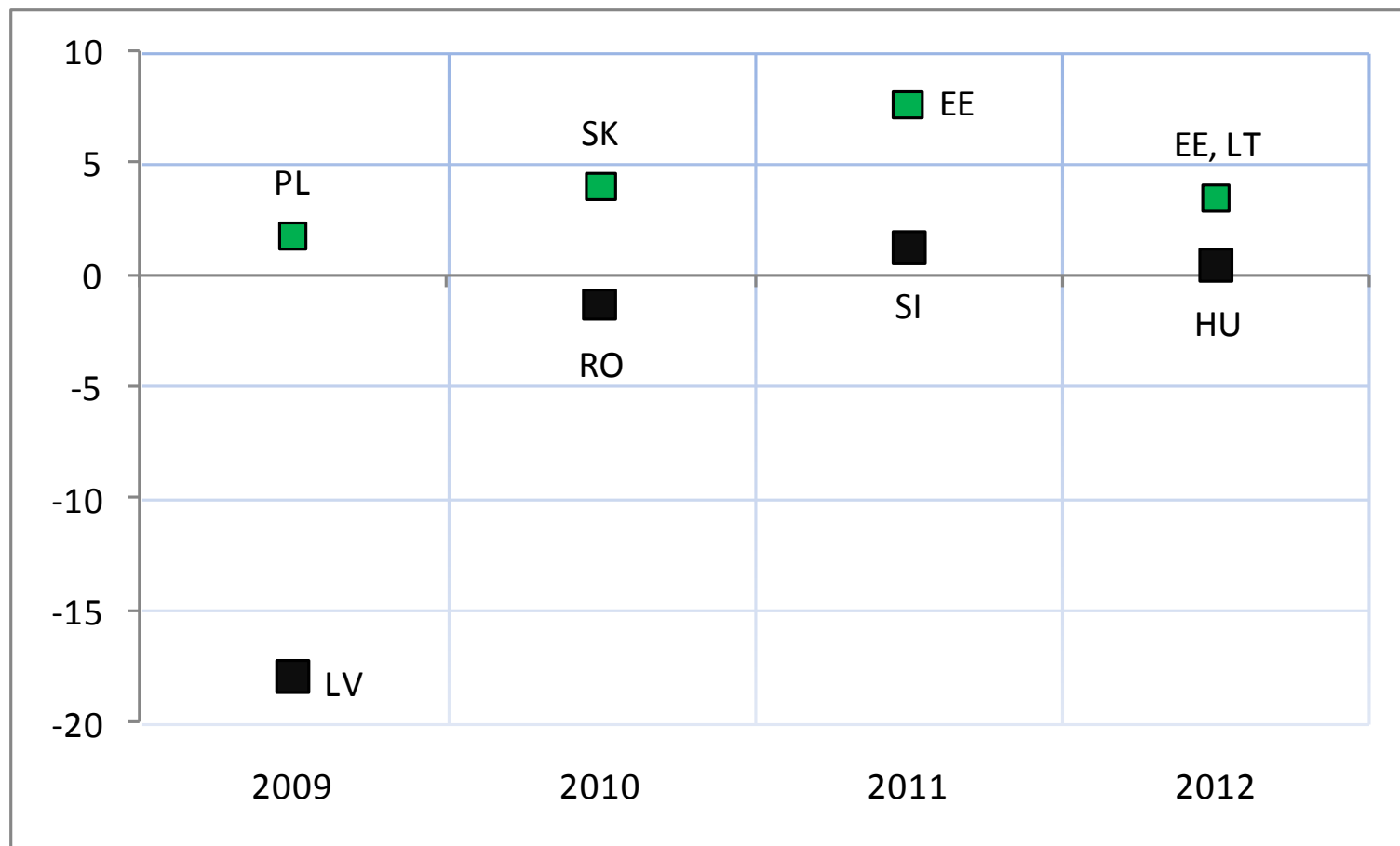
Source: World Bank forecasts from November 2011





# Growth differentials declining

Growth rates of worst and best performers in 2009-2012



Source: Eurostat, World Bank forecasts from November 2011



# Features of Sluggish Recovery

**Trade**

**Credit**

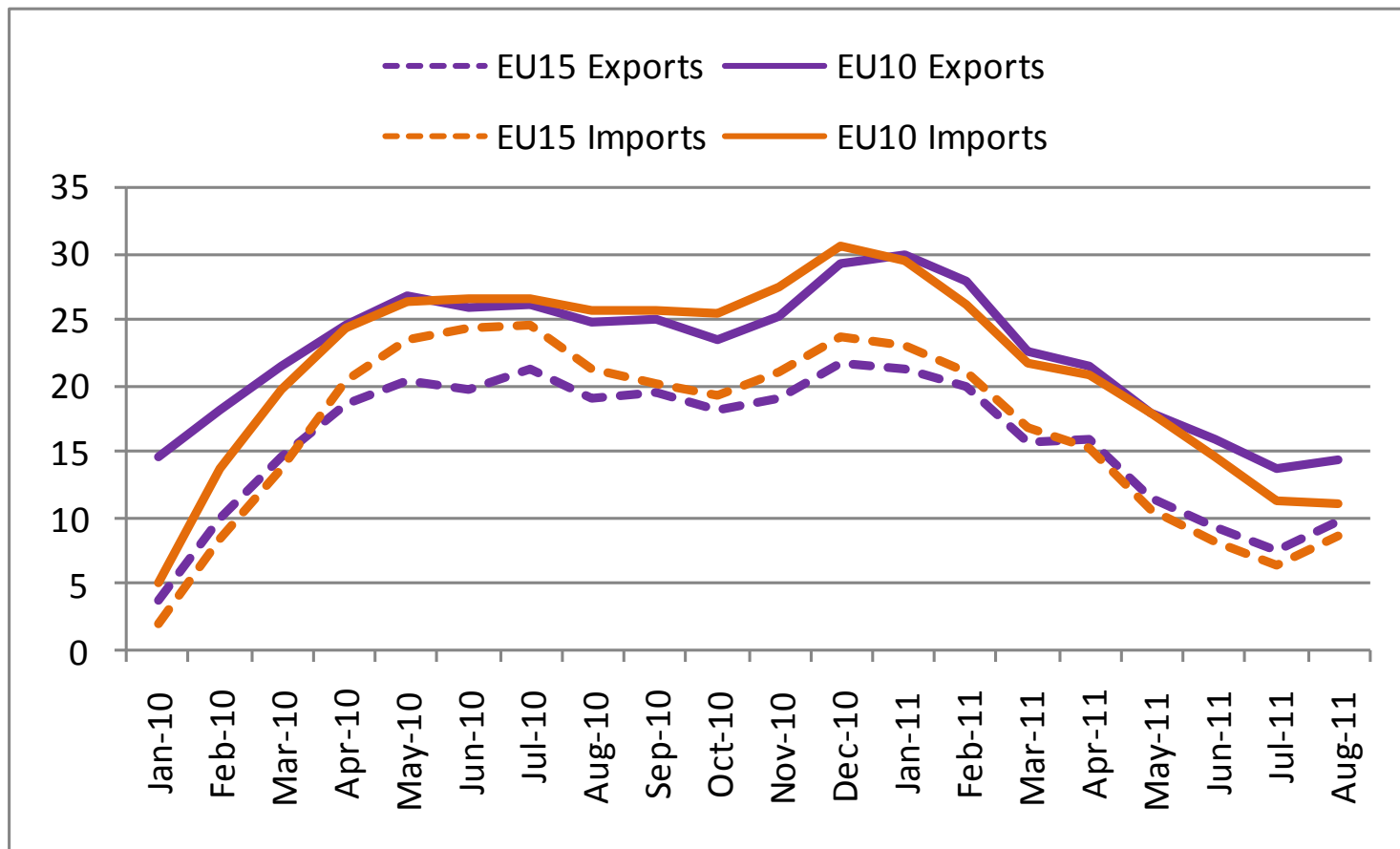
**Investment**

**Unemployment**



# Trade growth weakening in recent months

Exports and imports growth, year-on-year, percent

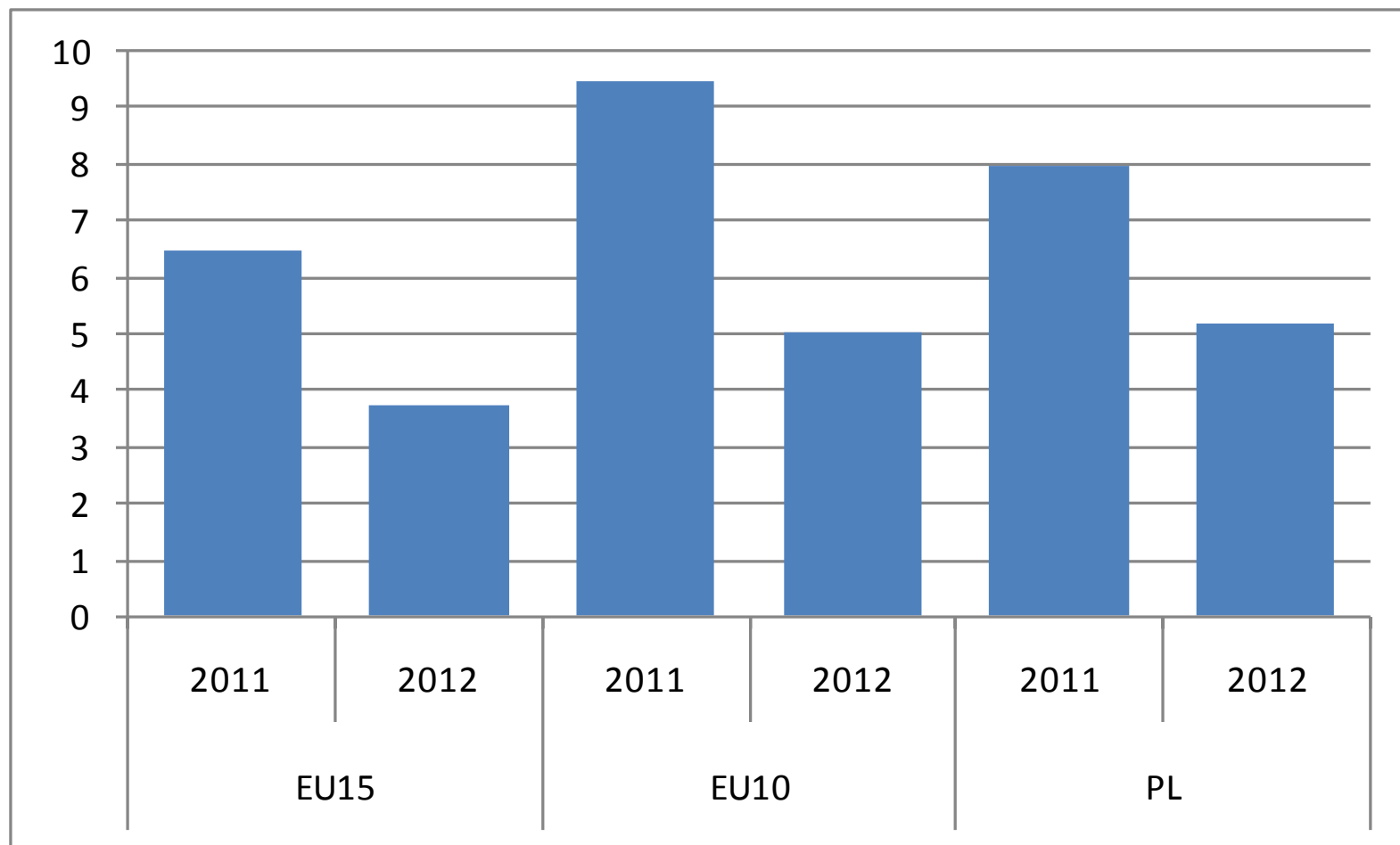


Source: Eurostat, World Bank staff calculations



# Trade growth declining further next year

Exports of goods growth, year-on-year, percent

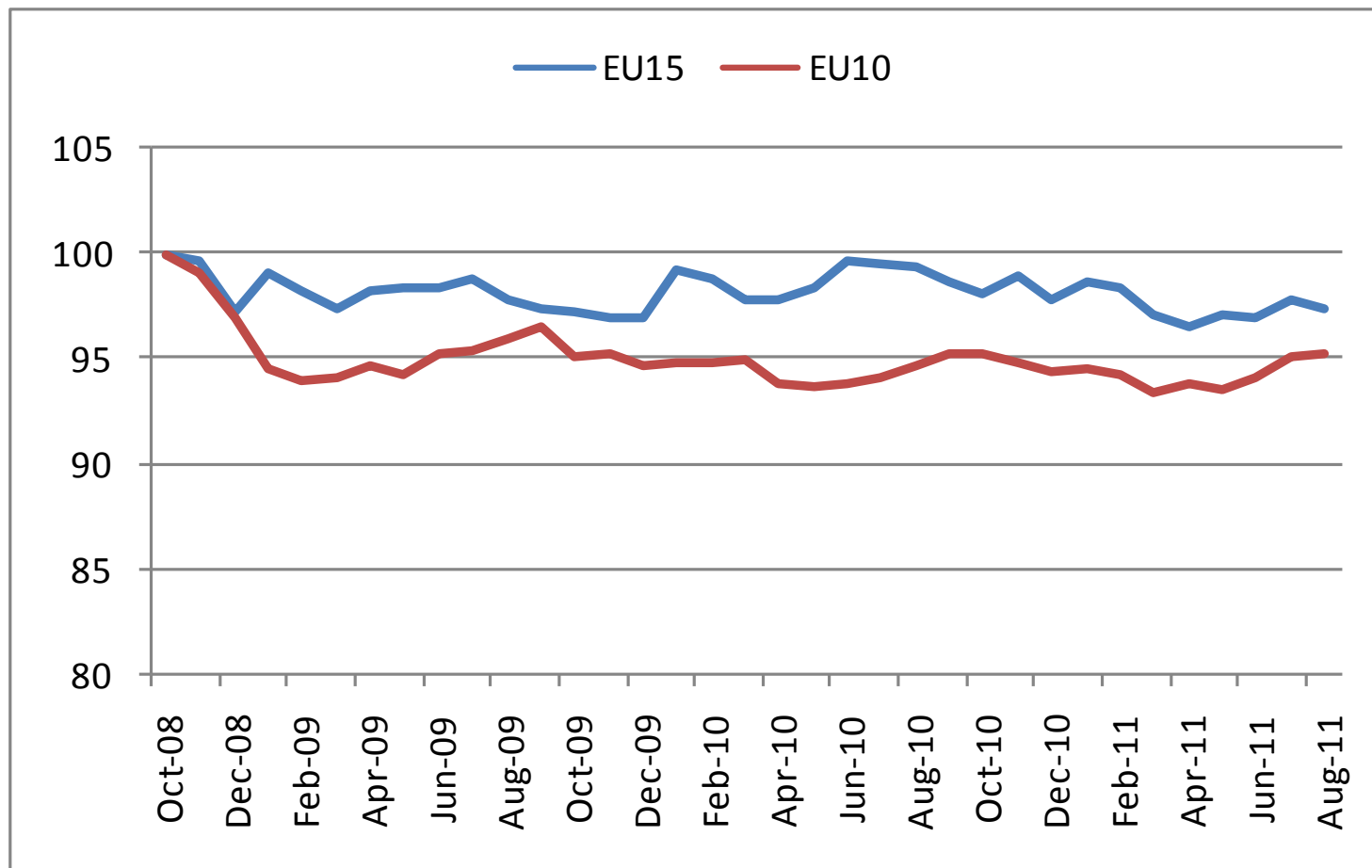


Source: World Bank staff based on EC Autumn Forecast November 2011



# Credit growth weakening

Real credit, index, Oct 2008 = 100

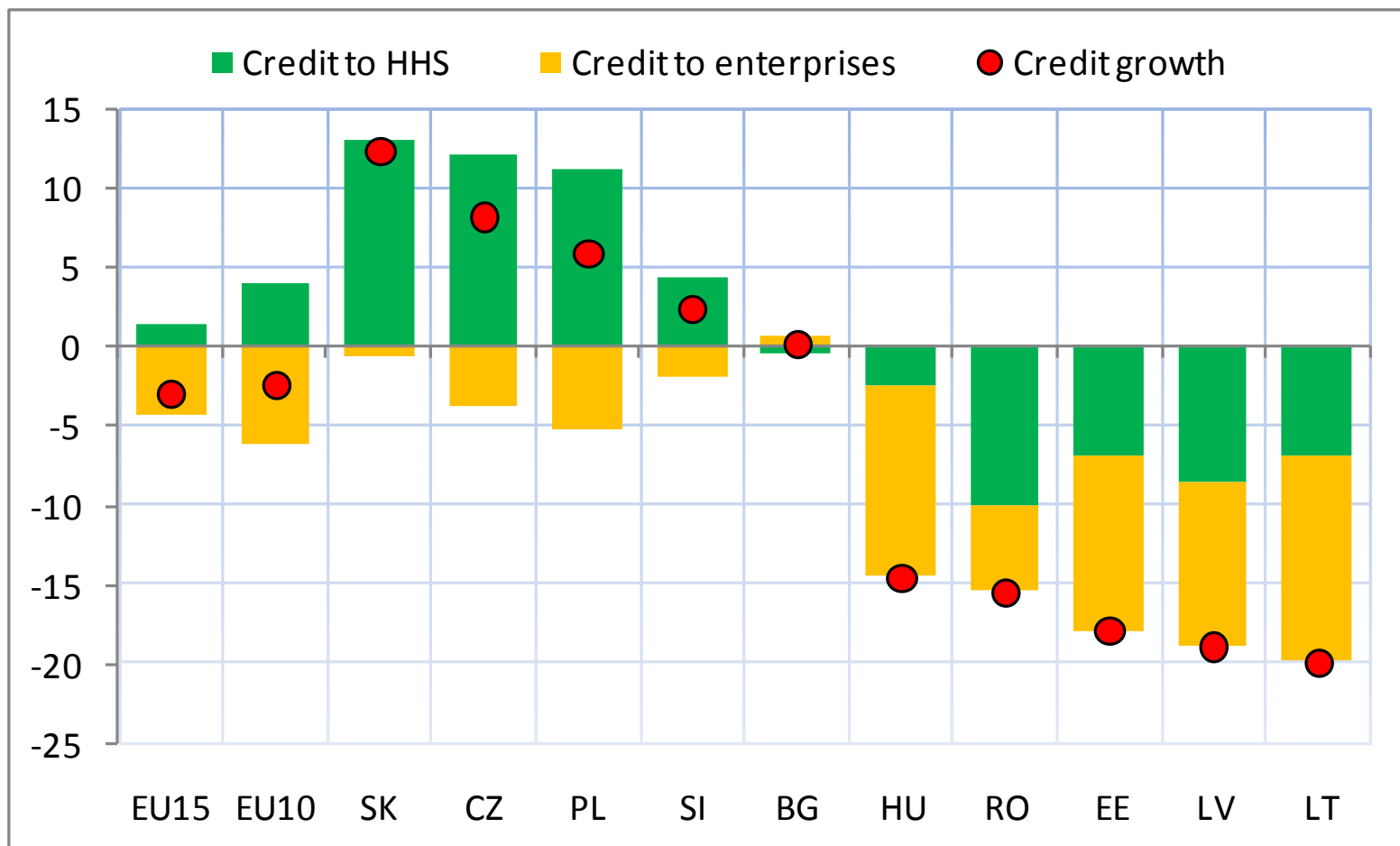


Source: ECB, World Bank staff calculations



# Credit to enterprises below pre-crisis levels

Contribution to real credit growth from Oct 2008 to August 2011

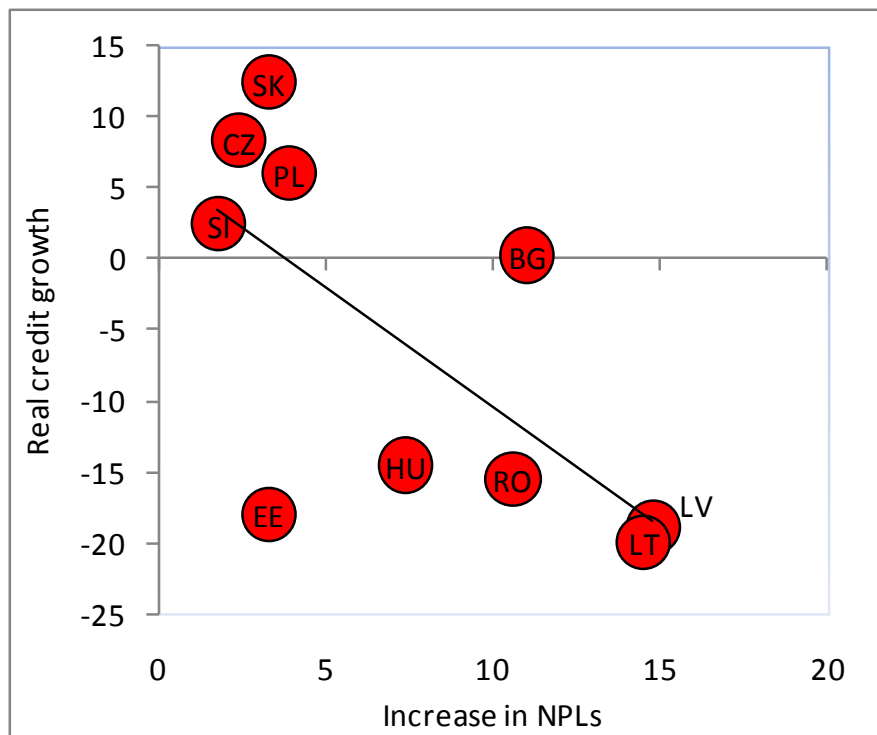


Source: ECB, World Bank staff calculations

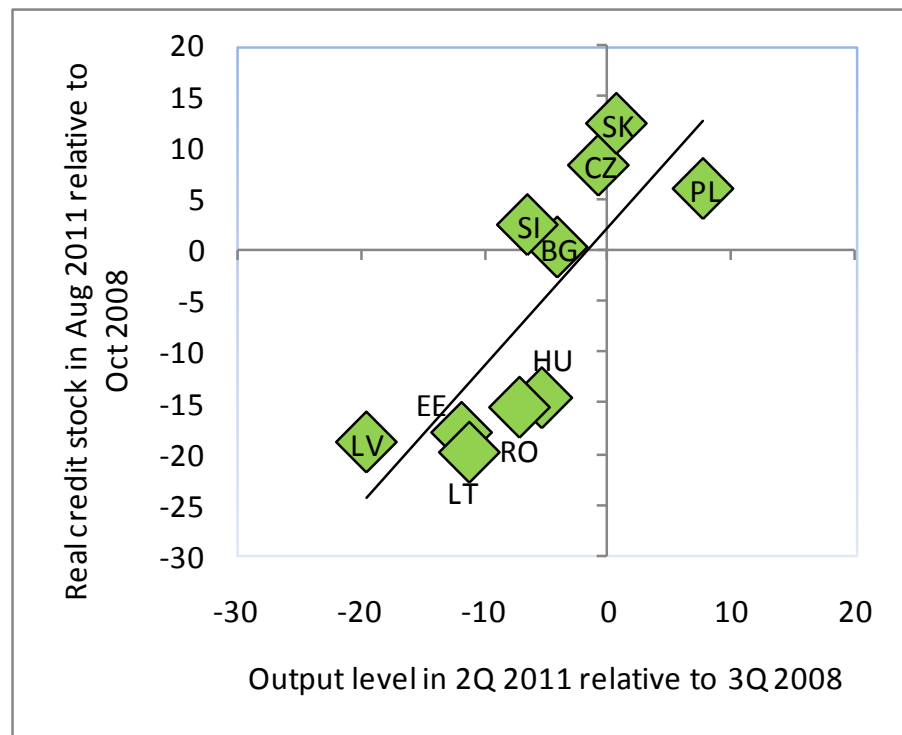


# Weak credit growth held back by supply and demand

Credit growth Oct 2008 - Aug 2011 vs. increase in non-performing loans (2008-2011), percent



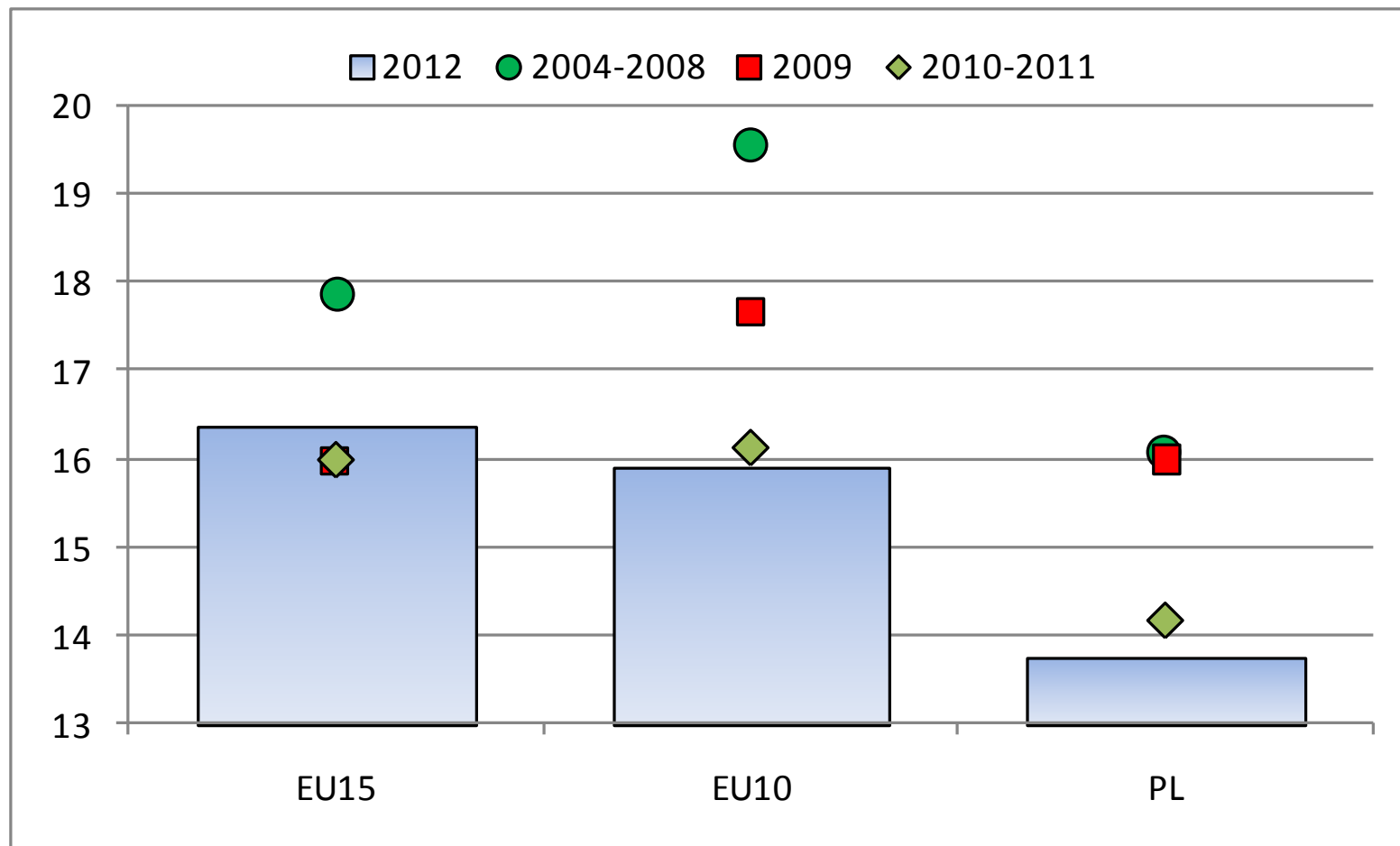
Real credit growth Oct 2008 – Aug 2011 vs. output level in 2Q 11 relative to 3Q 08, percent





# Private investment low and declining

Private investment as percent of GDP



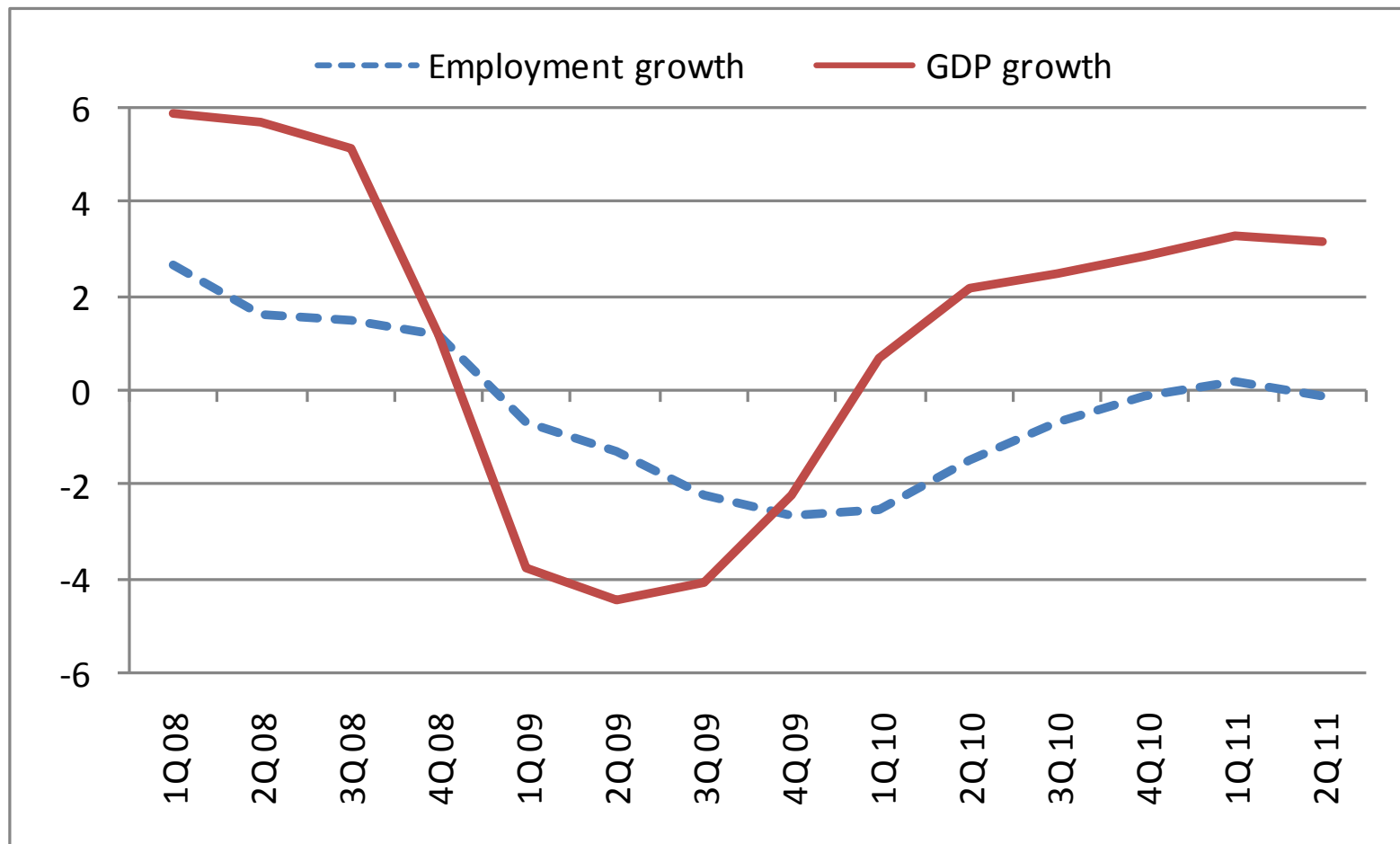
Source: World Bank staff based on EC Autumn Forecast November 2011





# Employment growth lags behind output growth

Employment and GDP growth, year-on-year, percent

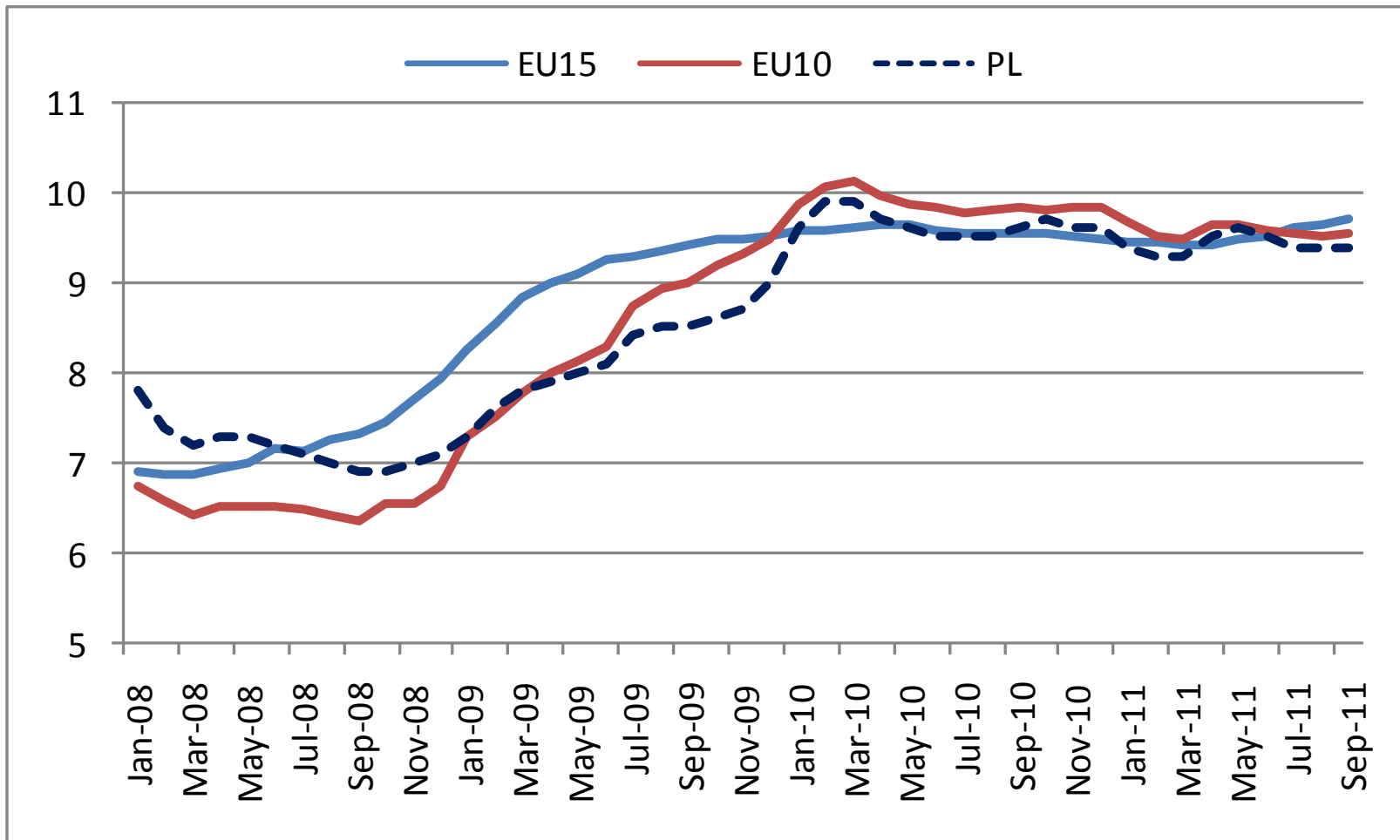


Source: Eurostat, World Bank staff calculations



# Unemployment persists at elevated levels

Unemployment rates in EU10, EU15 and Poland

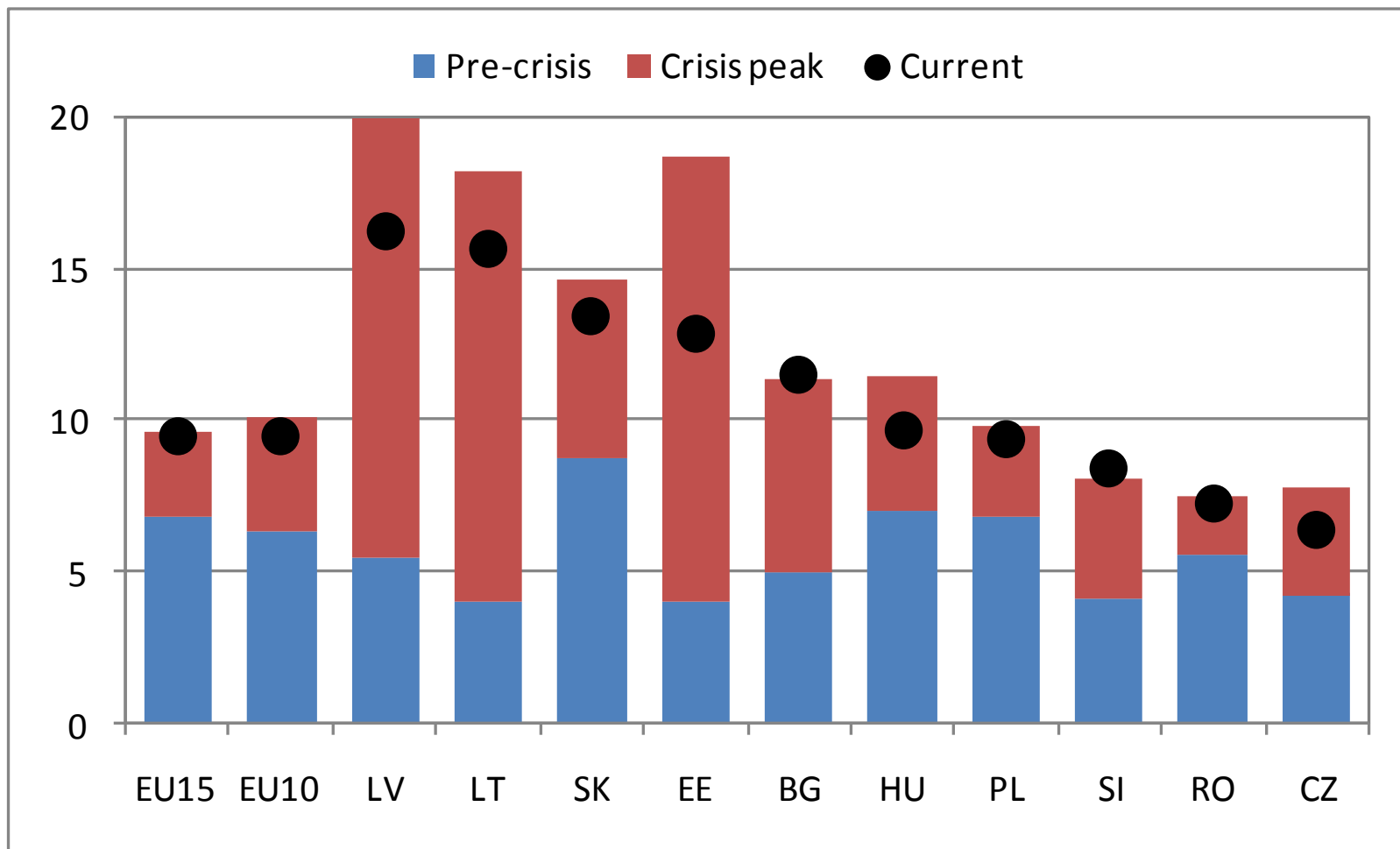


Source: Eurostat, World Bank staff calculations



# Outside of Estonia, Lithuania and Latvia, little progress in lowering unemployment

Harmonized unemployment rates, percent

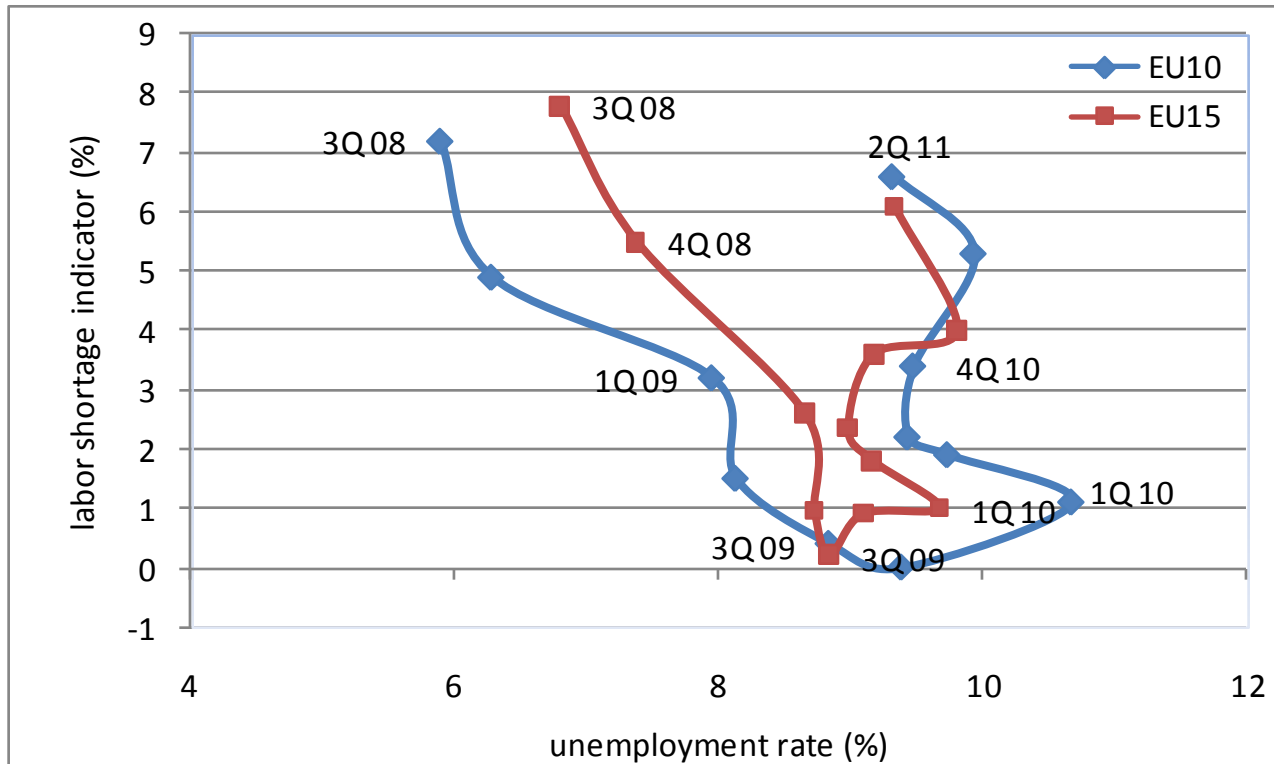


Source: Eurostat, World Bank staff calculations



# Businesses report more labor shortages but unemployment stays high

Labor shortages and unemployment in EU10, 3Q 08 – 2Q 11



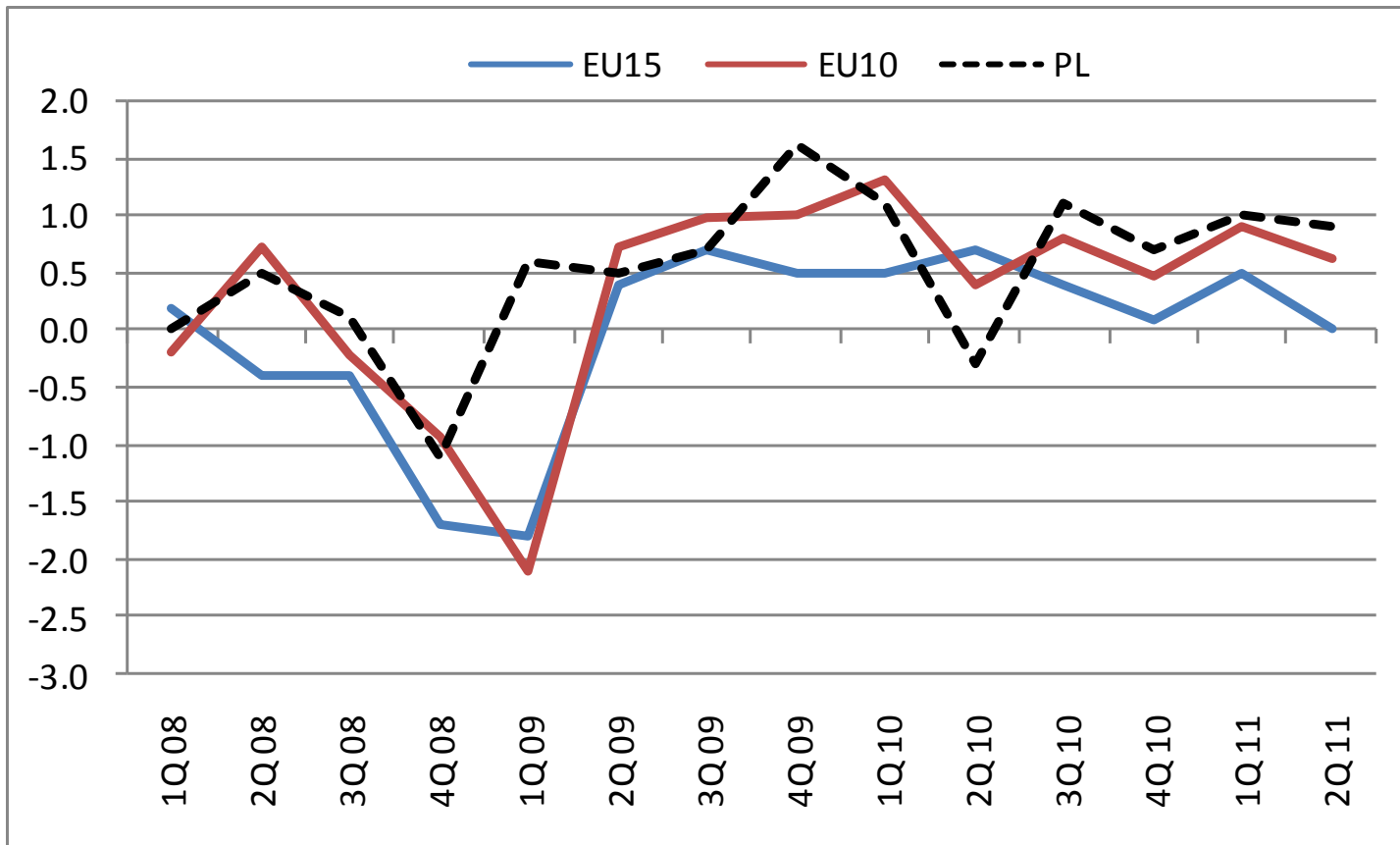
Source: Eurostat, World Bank staff calculations

Notes: Labor shortage = % of manufacturing firms indicating labor as a factor limiting the production



# Businesses rely on more output per worker rather than more hiring to increase their output

Change in real labor productivity per person employed in EU10 and EU15, quarter-to-quarter, seasonally adjusted



Source: Eurostat, World Bank staff calculations

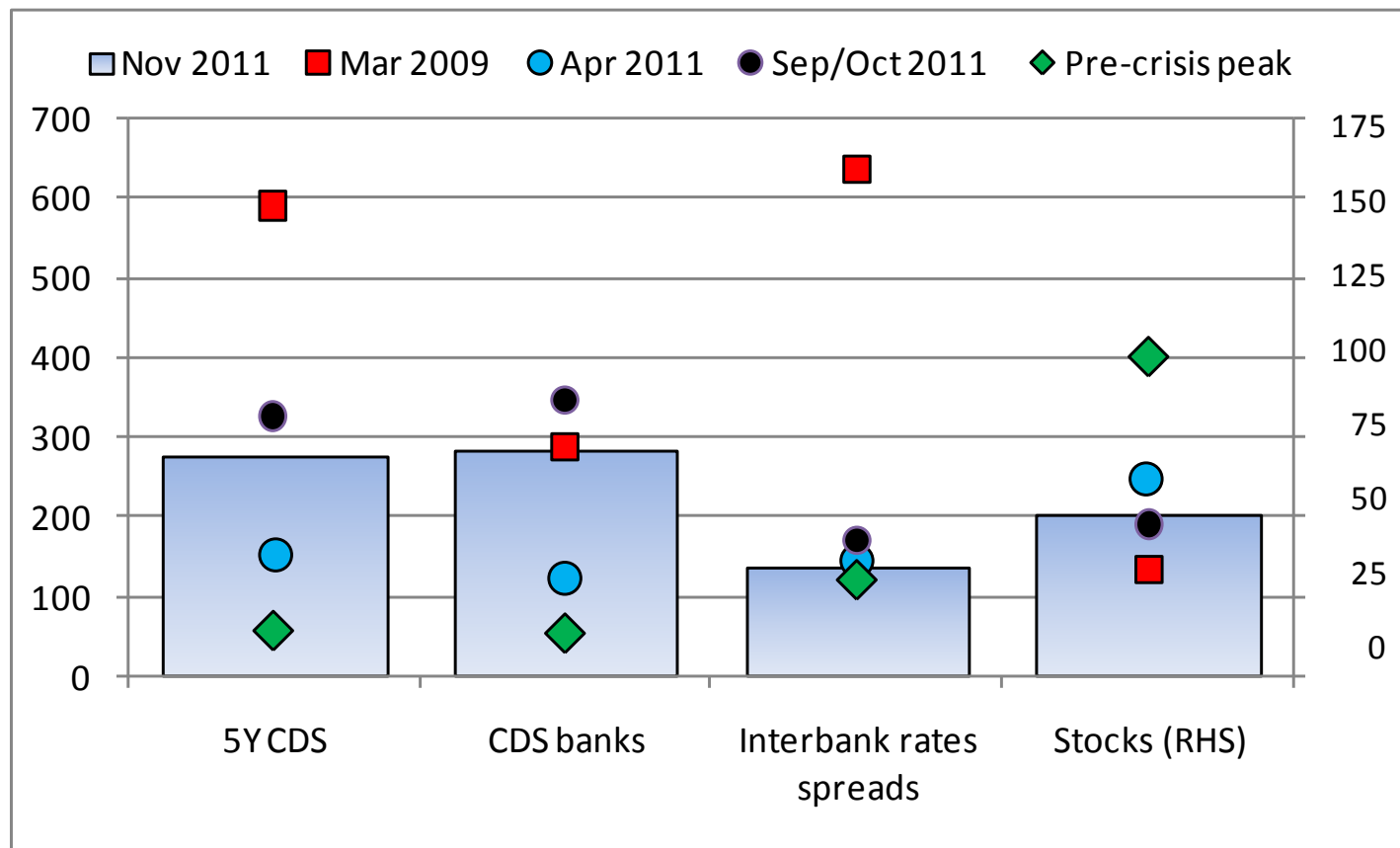


# **Policies: Stable Financial Markets**



# Risk aversion returned to the region

Asset class performance, percent change

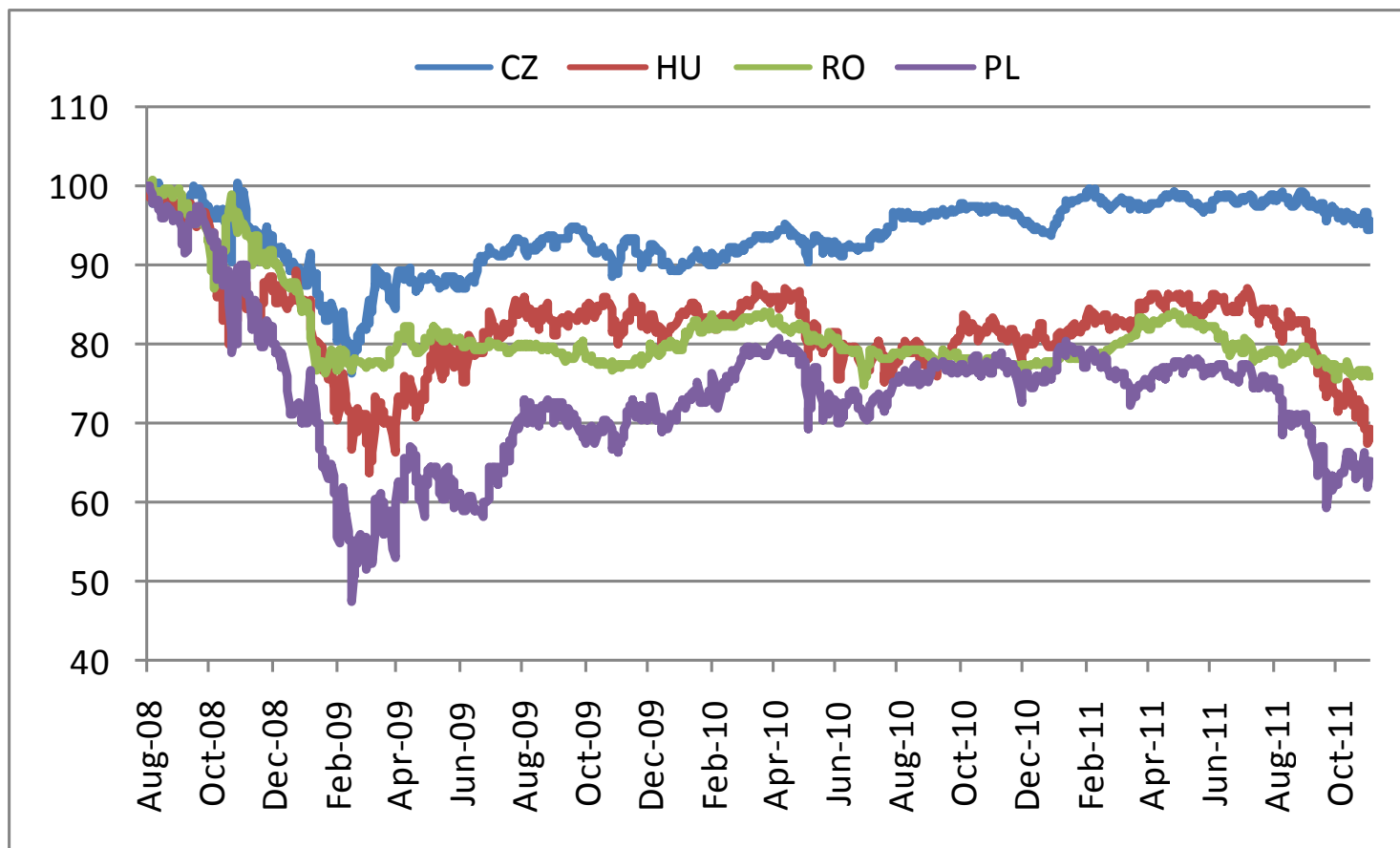


Source: Bloomberg, Reuters, World Bank staff calculations



# Currencies depreciating

Exchange rate to EUR



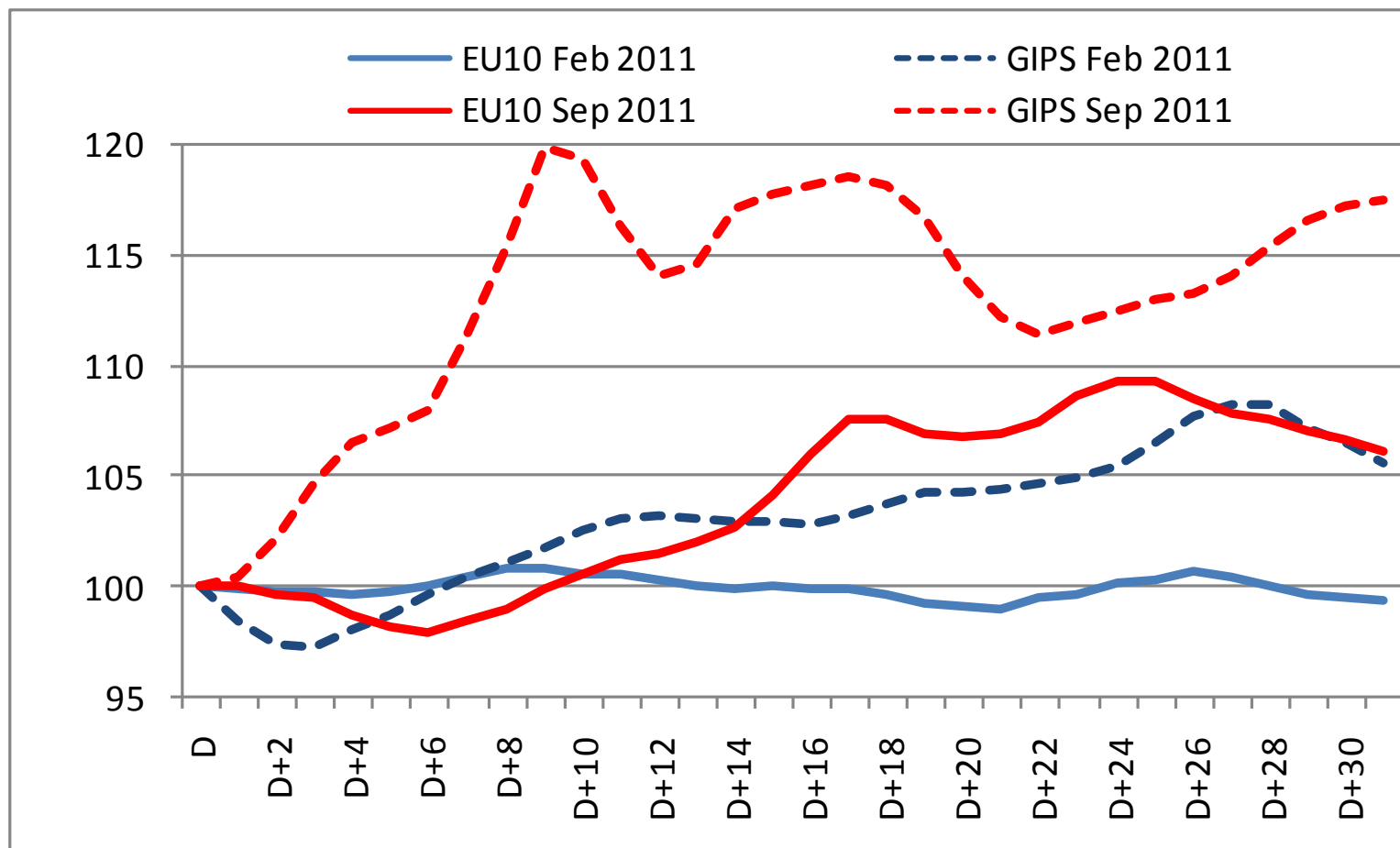
Source: DECPG, World Bank staff calculations





# Worries on sovereign debt spilled over from GIPS to EU10 in September, unlike in February

Median government bond yields EU10 and GIPS countries (basis points)



Source: Bloomberg, Reuters, World Bank staff calculations



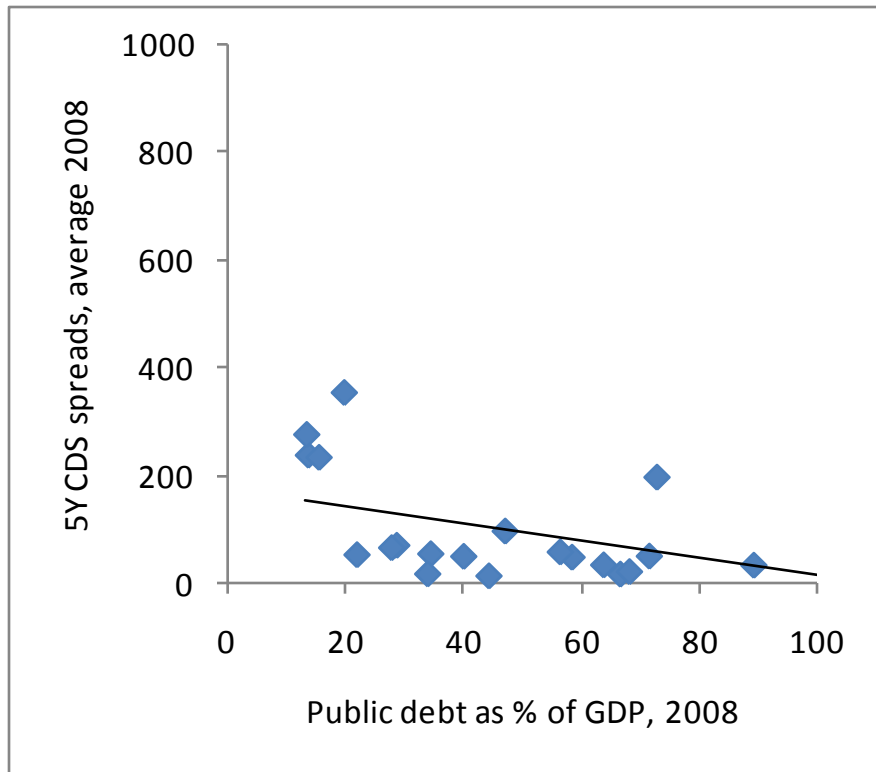
# **Policies: Getting the Fiscal House in Order**



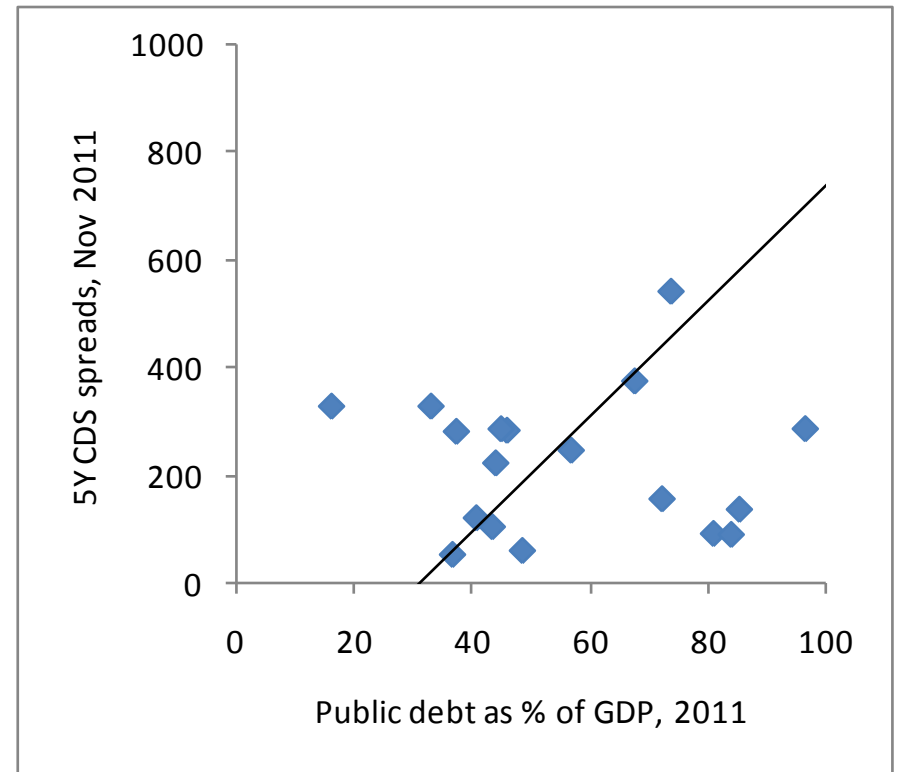
# Financial markets look closely at fiscal vulnerabilities

5Y CDS spreads vs. public debt

Pre-crisis



Post-crisis

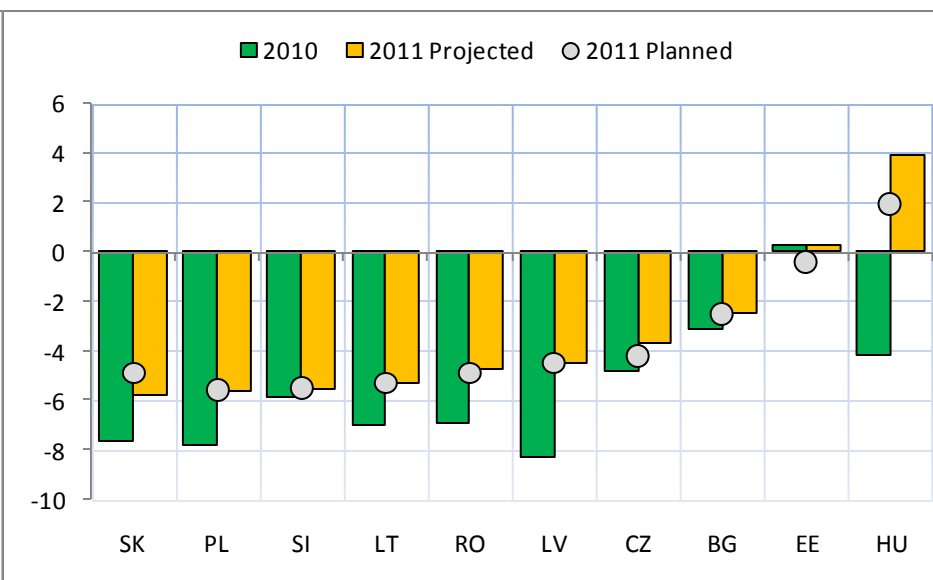
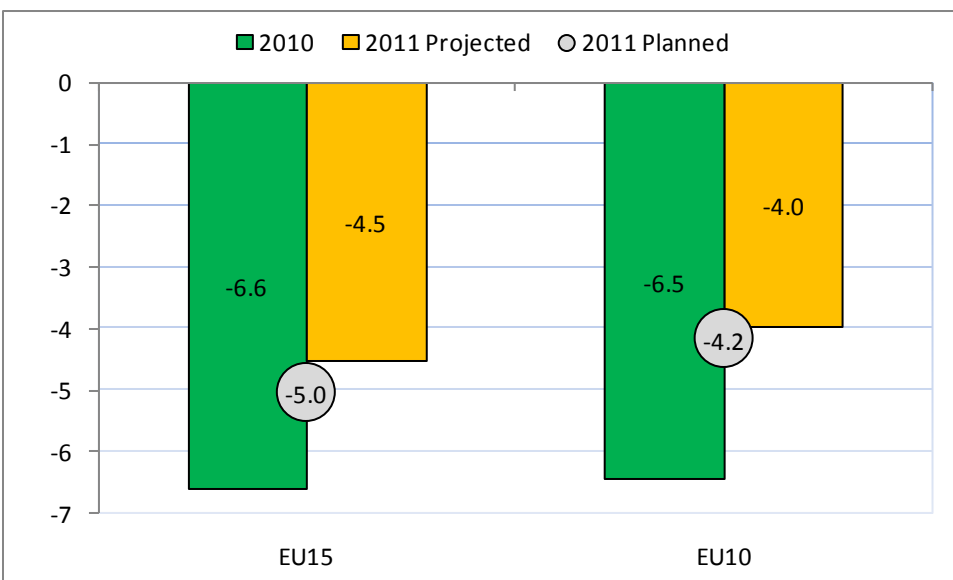


Source: EU10 World Bank staff forecasts for 2011 and 2012, EDP notifications from Oct 2011



# Countries proceeded with fiscal consolidation according to plan

## General government fiscal deficit in 2010-11, percent of GDP



Source: World Bank staff calculations based on EDP notifications from October 2011 and CP/SP from Summer 2011



# Countries get ready for further adjustments in 2012

## Fiscal measures in Budget drafts for 2012

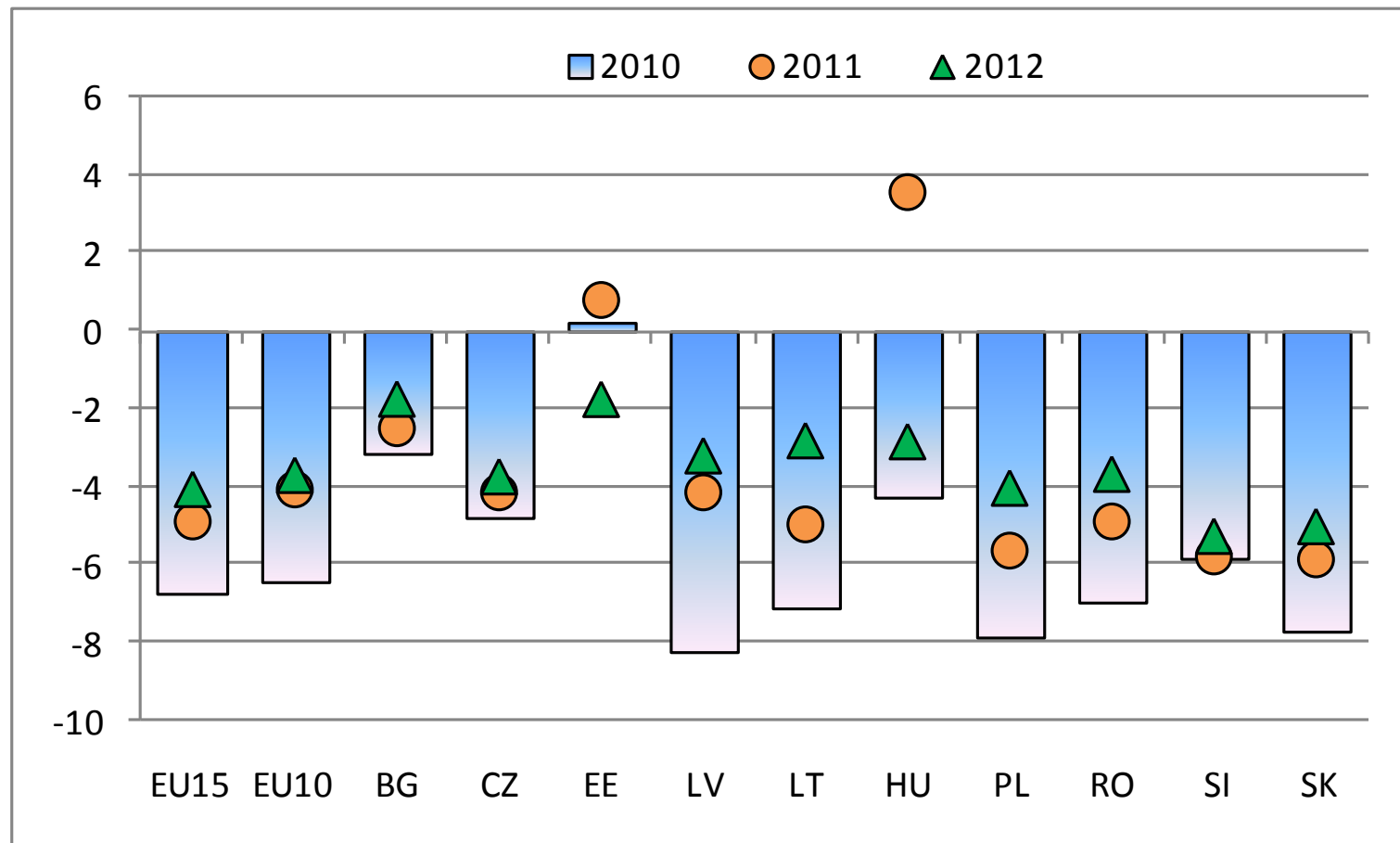
	Pensions	Public wages	New revenue measures		
	Freeze	Freeze (or cut)	VAT	Direct Tax	Others
BG	✓	✓			✓
CZ		✓	✓		✓
EE		✓			✓
HU		✓	✓	✓	✓
LV	✓	✓			✓
LT		✓			✓
PL		✓			✓
RO	✓*	✓*			✓
SK		✓			✓
SI	✓	✓			

Source: World Bank staff staff



# Fiscal deficits to decline further in 2012

General government fiscal deficit in 2010 to 2012, percent of GDP

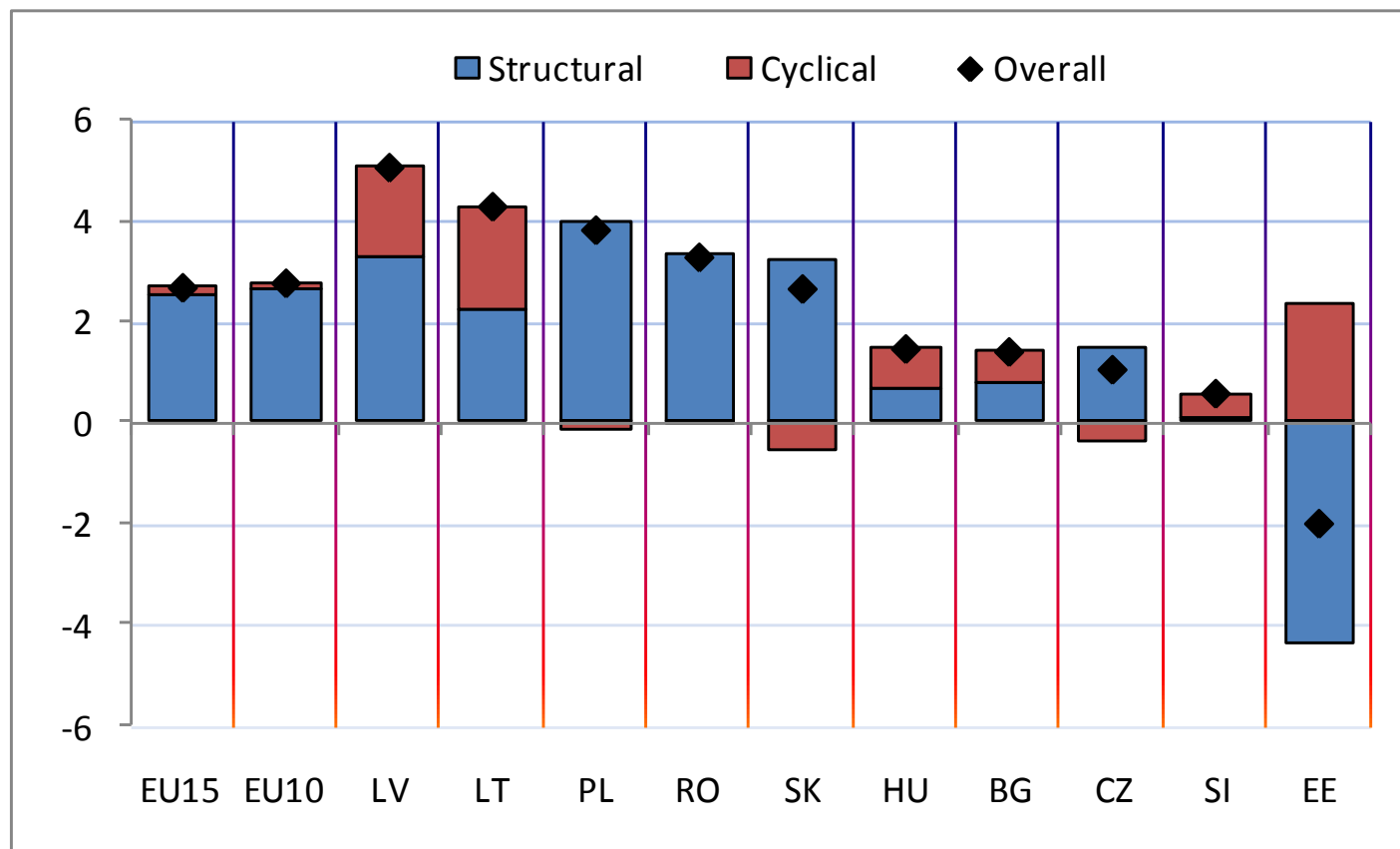


Source: World Bank staff calculations based on Fiscal Notifications from October 2011 and EC Autumn Forecast from November 2011



# Fiscal adjustments mainly structural in nature

General government fiscal deficit in 2010 to 2012, percent of GDP

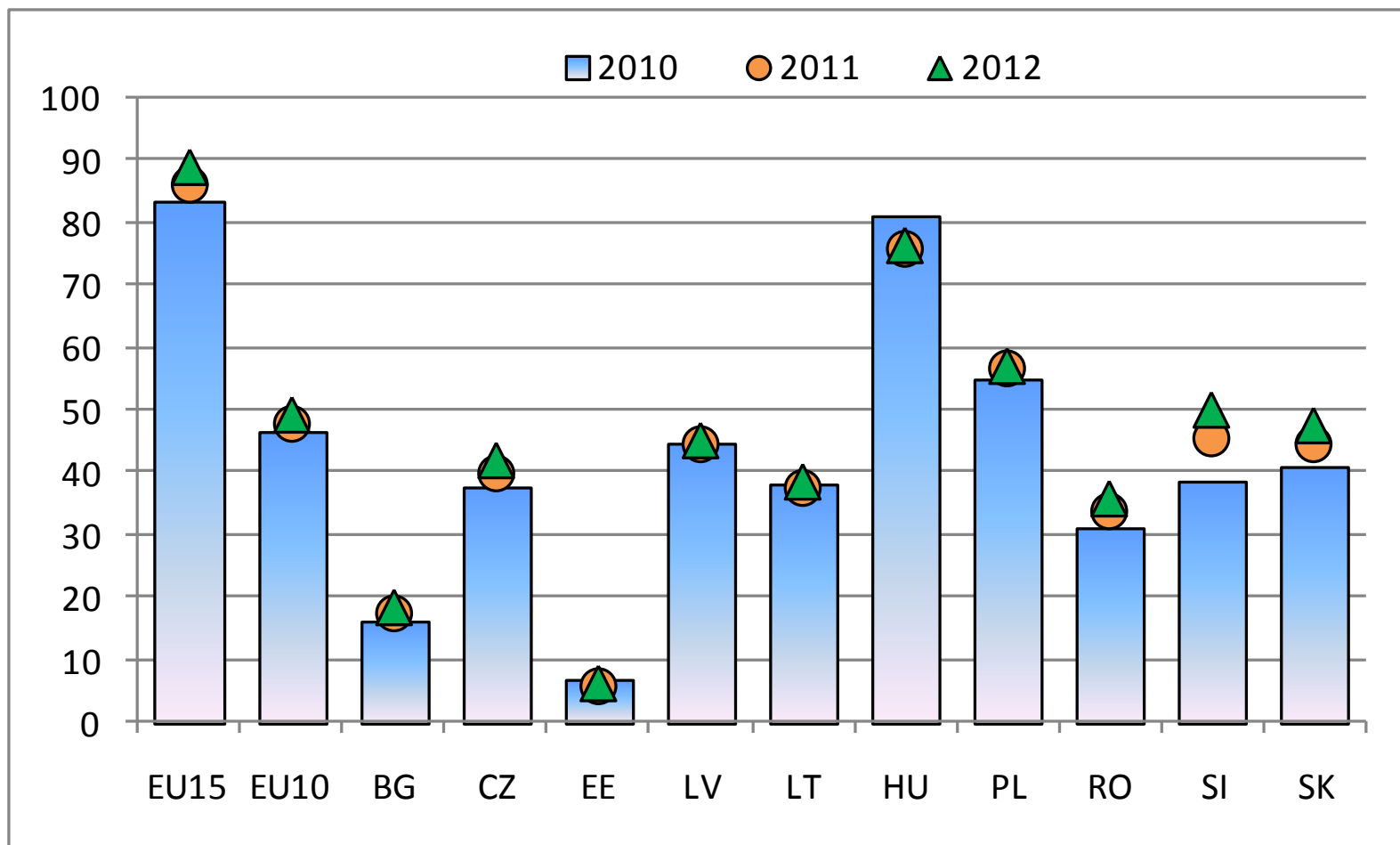


Source: World Bank staff calculations based on CP/SP from Summer 2011 and EC Autumn Forecast from November 2011



# Public debt stabilizing

General government public debt from 2010 to 2012, percent of GDP



Source: World Bank staff calculations based on Fiscal Notifications from October 2011 and EC Autumn Forecast from November 2011



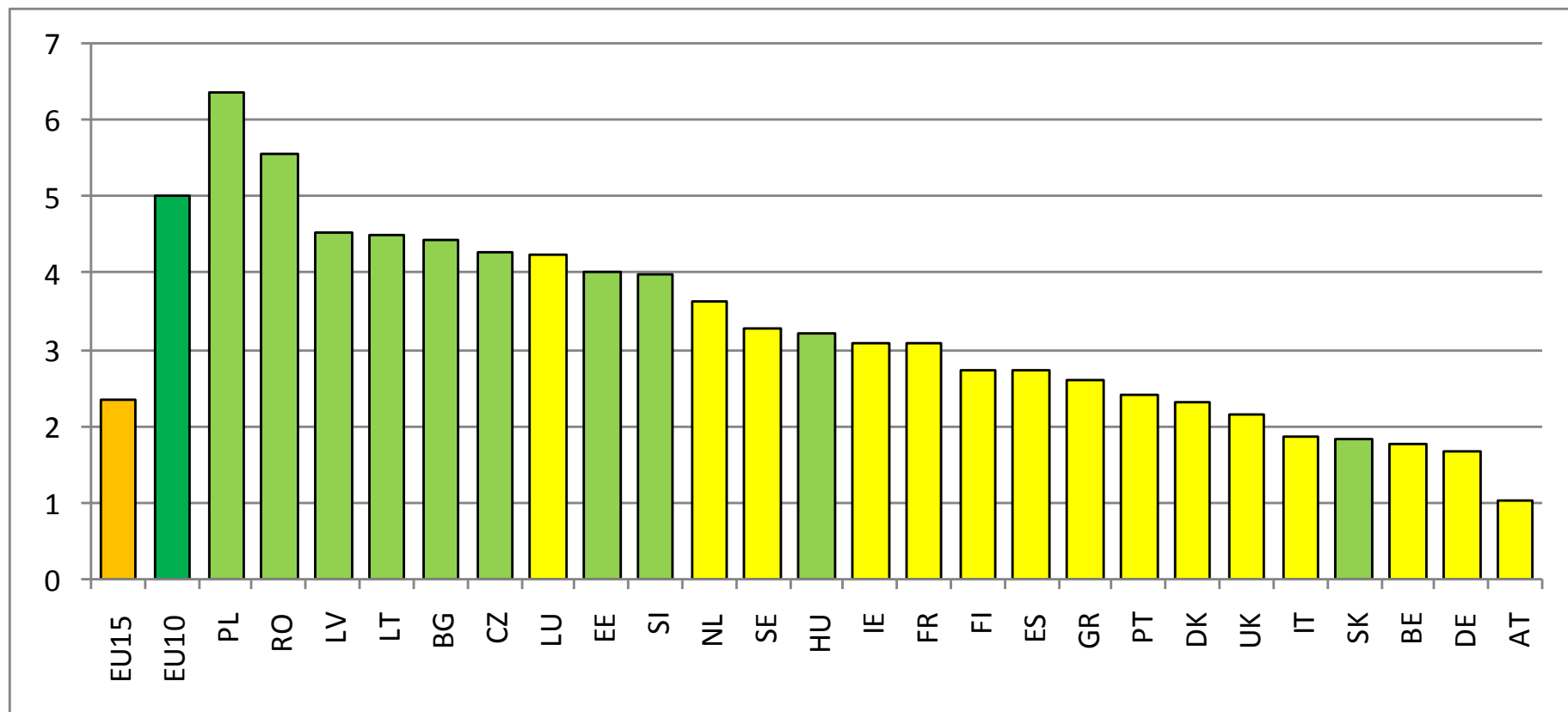


# **Policies: Structural Reforms**



# Public investment helping Poland to bolster growth

Public investment as percent of GDP in 2011

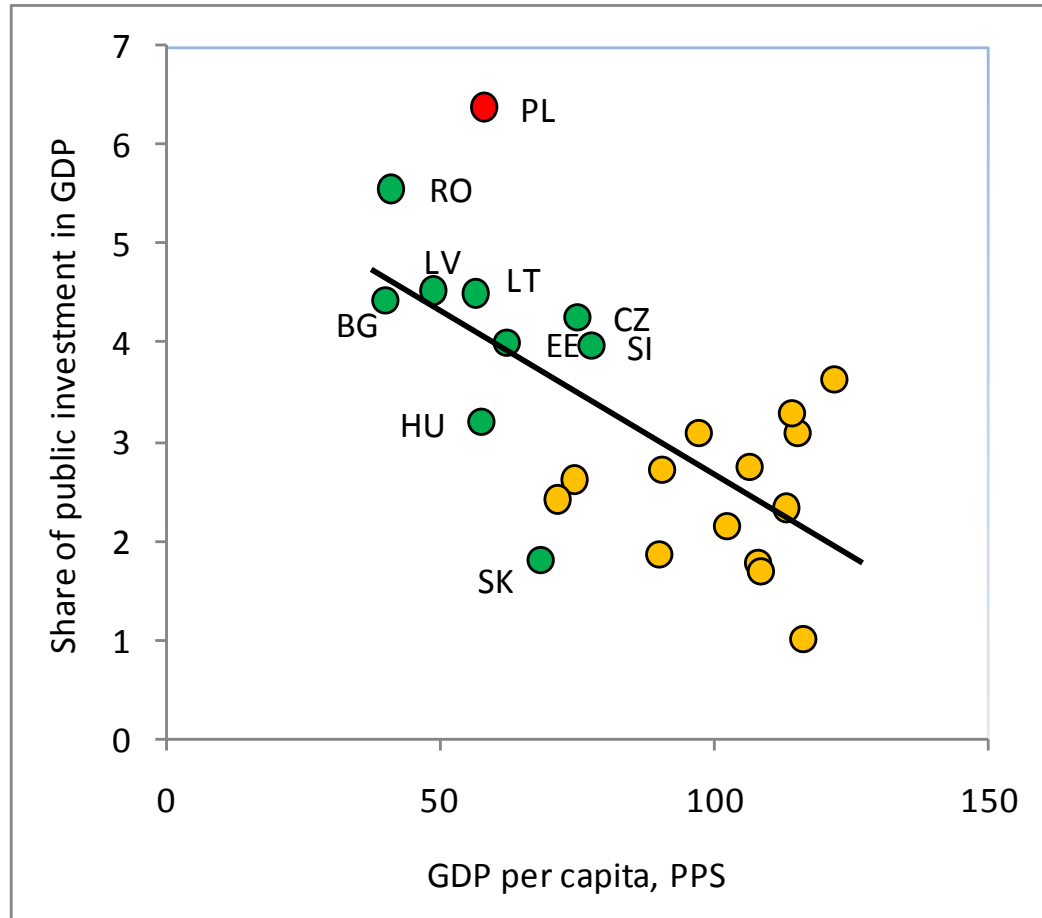


Source: World Bank staff based on EC Autumn Forecast November 2011



# Poland is over the trend line for public investment

GDP per capita PPS (EU15=100) vs. share of public investment in GDP, 2011

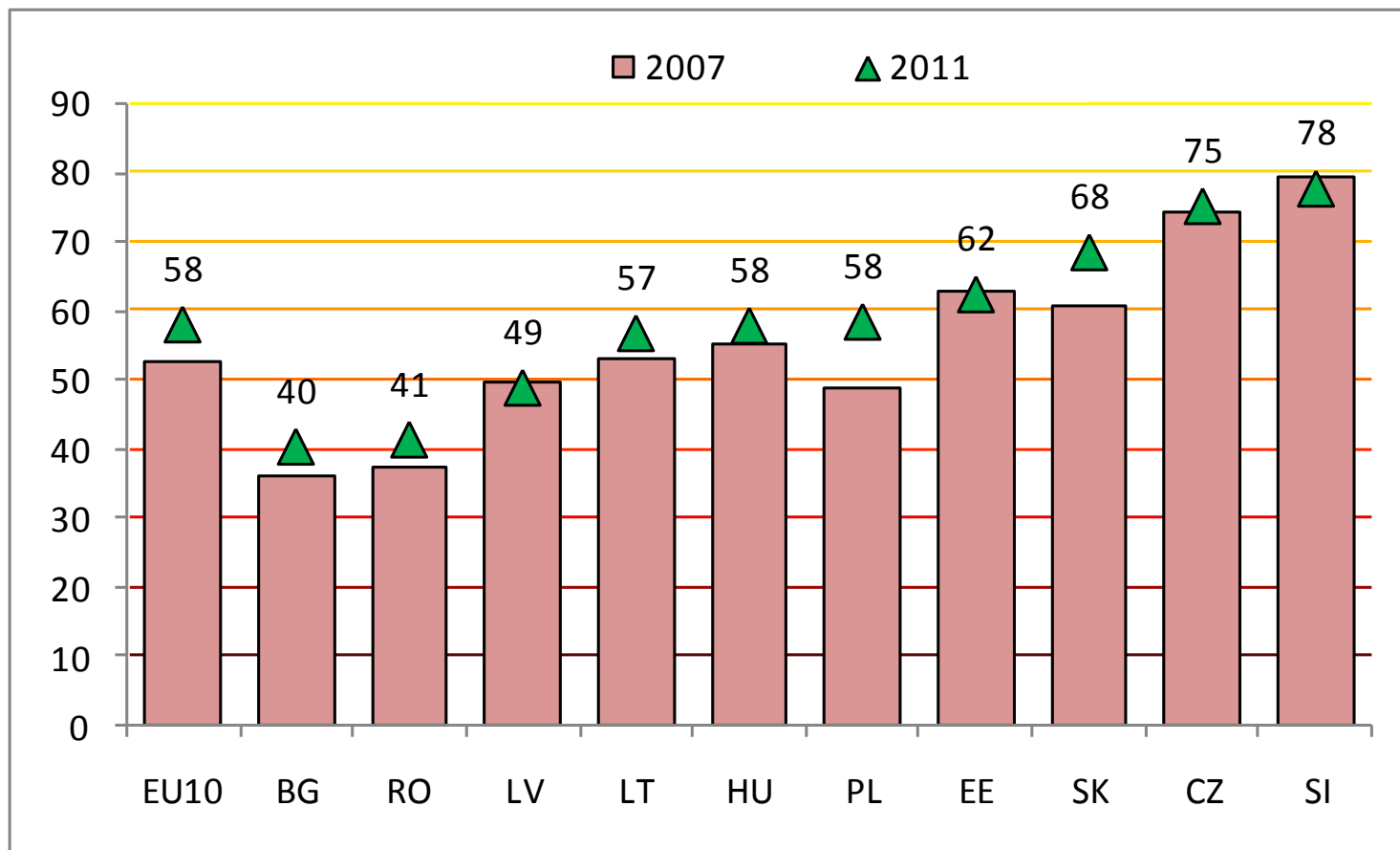


Source: World Bank staff calculations based on EC Autumn Forecasts November 2011



# Poland closing the gap to EU15 living standards by 10 percent in 4 years

Comparison of GDP per capita 2007 and 2011 adjusted for purchasing power parities – EU10 Countries, EU15 = 100



Source: World Bank staff calculations based on EC Autumn Forecasts November 2011



# THANK YOU

For more information visit:

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