



World Bank
EU10 Regular Economic
Report

Recovery

and

Beyond

Bucharest, 19 April 2011



The World Bank

EU10
Regular Economic Report

Main Report

Recovery and Beyond

April 2011

Focus Notes:

**Fueling Growth and Competitiveness through Employment,
Skills, and Innovation**

**Household and Government Responses to the Global Financial
Crisis**

This report is prepared by a team led by Kaspar Richter (krichter@worldbank.org) and including Stella Ilieva, Ewa Korczyk, Matija Laco, Sanja Madzarevic-Sujster, Catalin Pauna, Marcin Piatkowski, Lazar Sestovic, and Emilia Skrok.

The team is very grateful for the excellent inputs from the World Bank Global Prospect Group, coordinated by Lucio Vinhas de Souza, and from Olga Vybornaya.

EU10 refers to Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, the Slovak Republic and Slovenia



MESSAGES

- **With the recovery strengthening, output has reached pre-crisis levels in early 2011 and growth is set to get close to its potential in 2012**
- **Yet, weak demand and high unemployment could undermine the recovery**
- **Sustained growth and job creation require stable financial markets, sustainable fiscal balances and structural reforms**

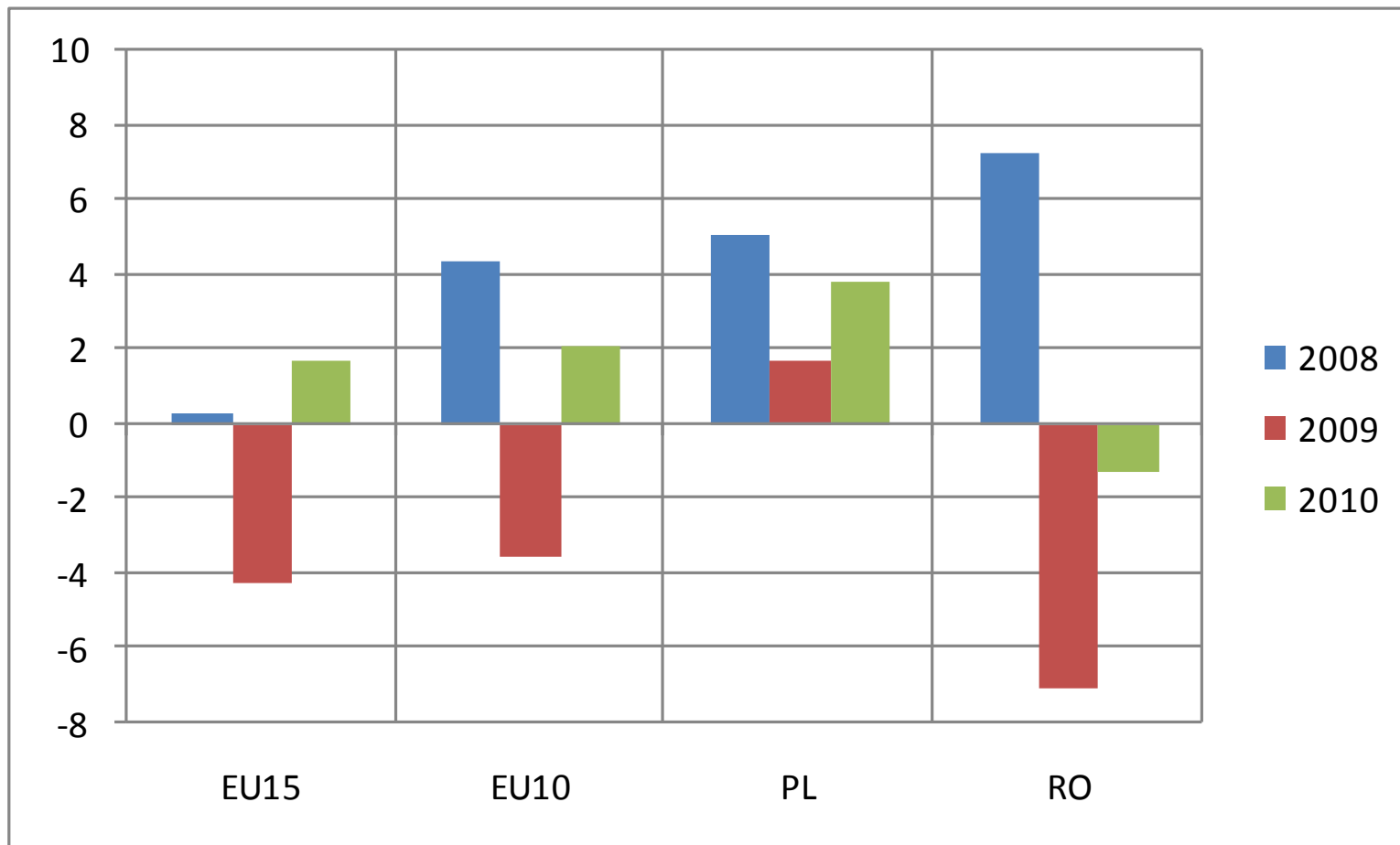


Recovery Strengthening



Growth is improving ...

Year-on-year GDP growth in EU10, EU15, Poland and Romania

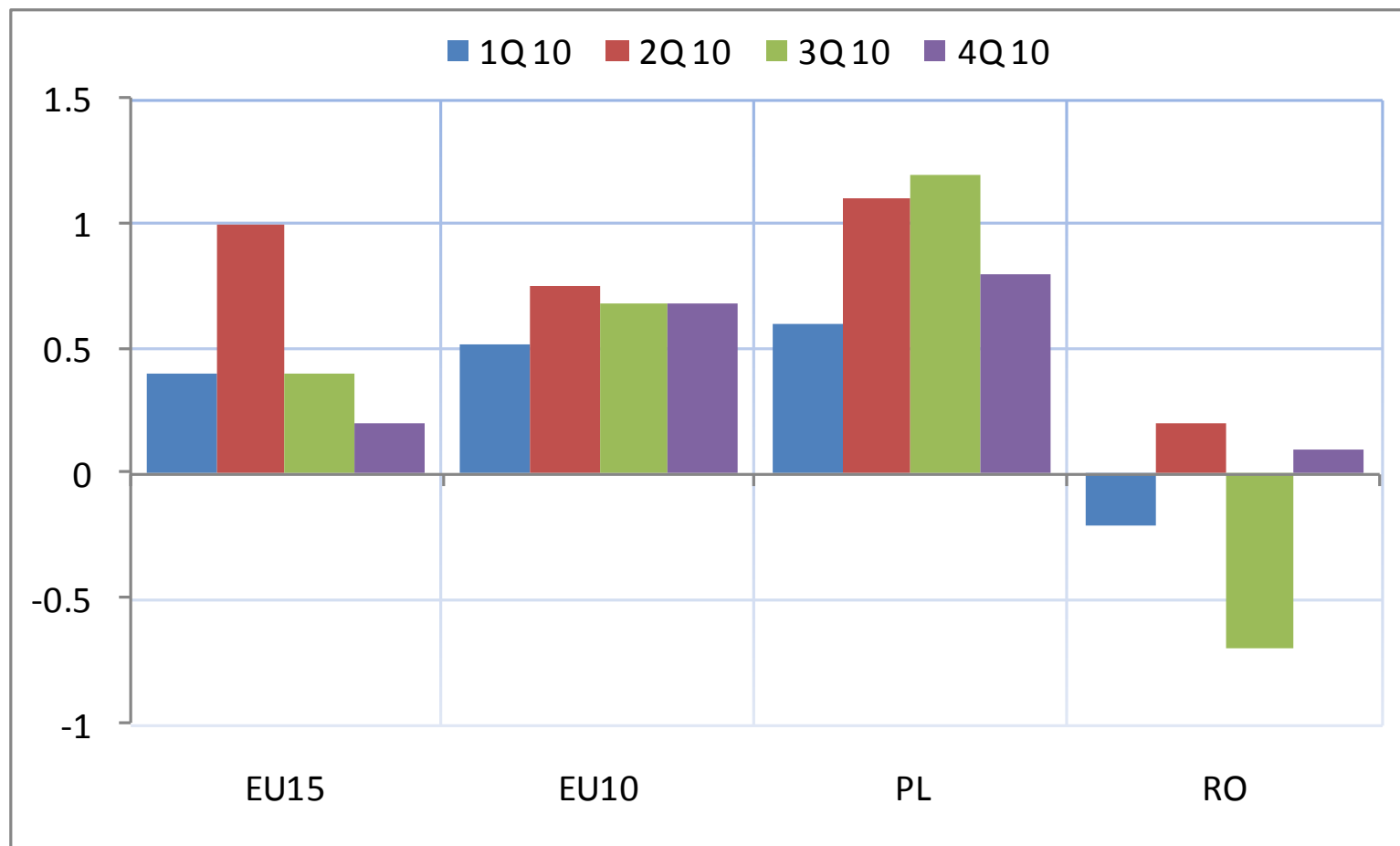


Source: Eurostat, Central Statistical Offices, World Bank staff calculations



... with rising momentum ...

Quarter-on-quarter GDP growth in EU10, EU15, Poland and Romania

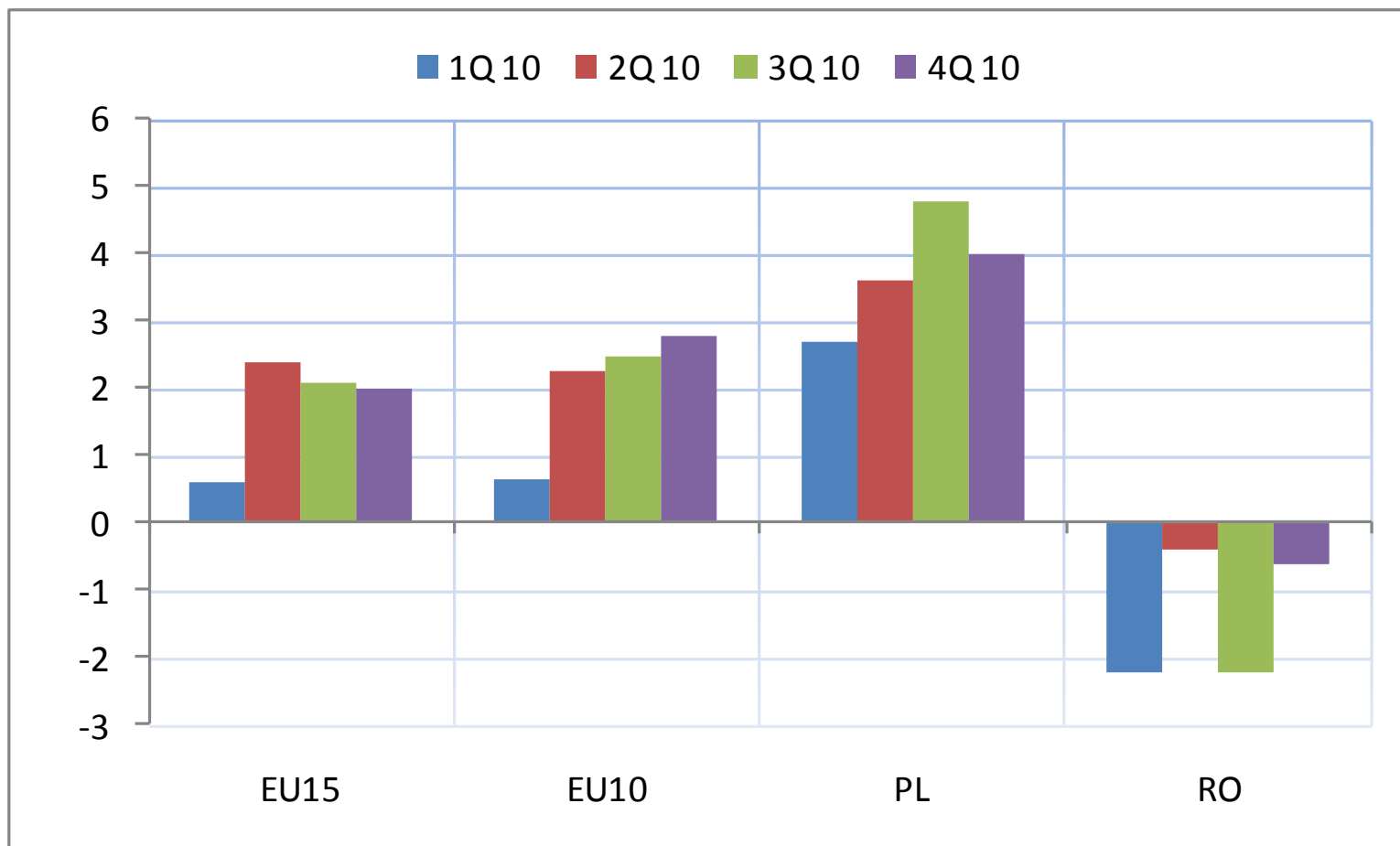


Source: Eurostat, Central Statistical Offices, World Bank staff calculations



... also year-over-year ...

Year-on-year GDP growth in EU10, EU15, Poland and Romania

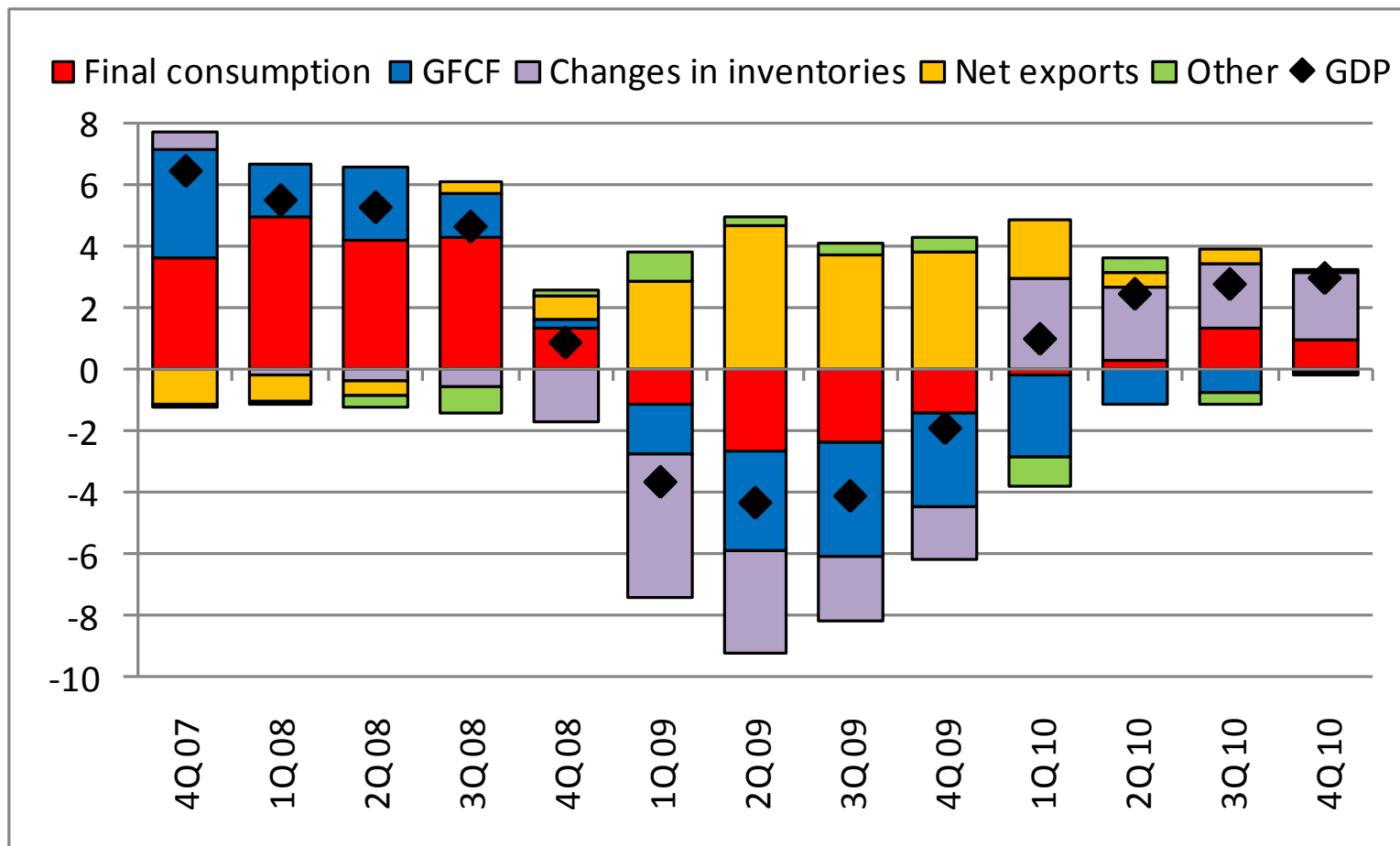


Source: Eurostat, Central Statistical Offices, World Bank staff calculations



... aided by restocking ...

Contribution to GDP growth in the EU10, percent, year-on-year, not seasonally adjusted

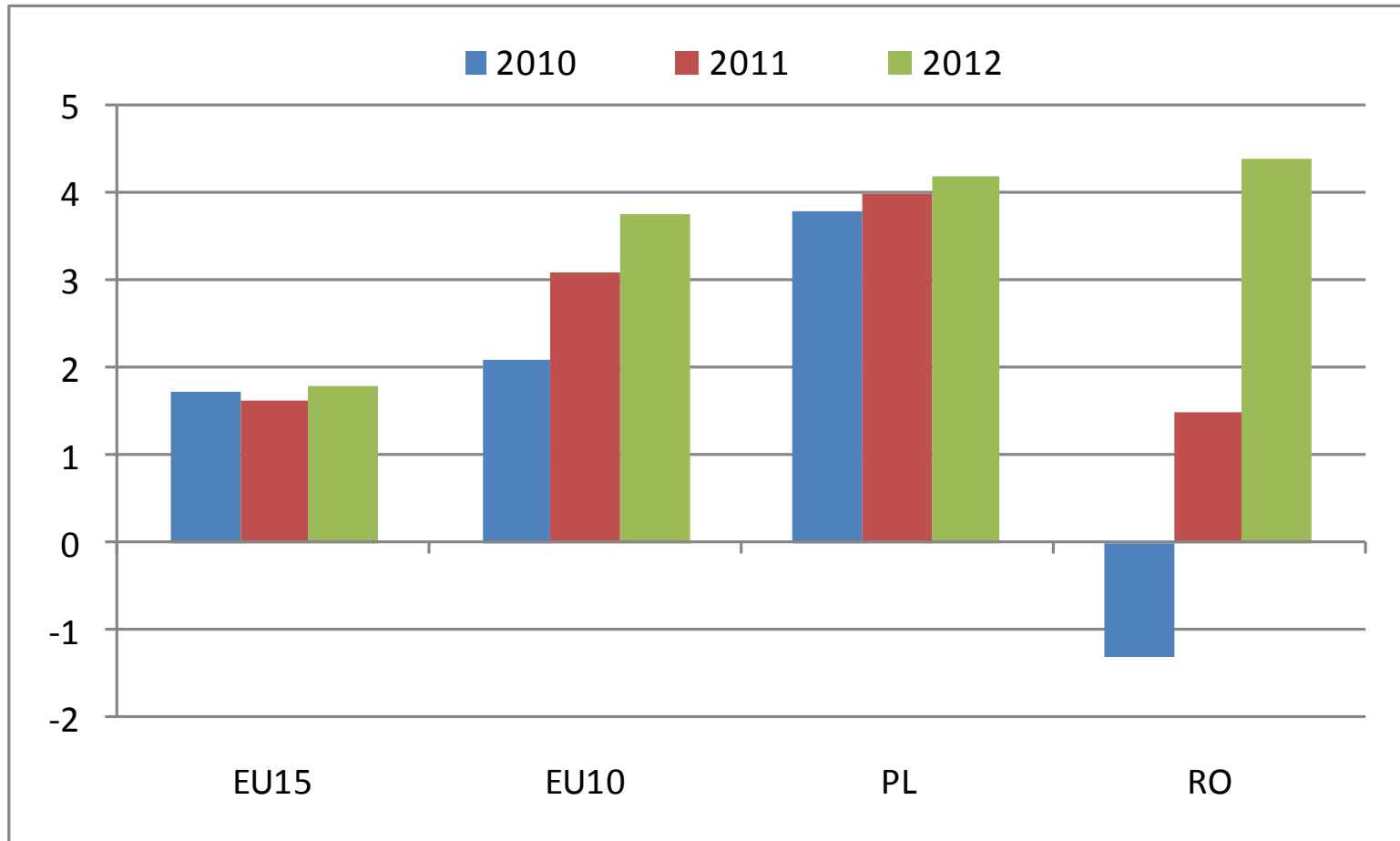


Source: Eurostat, World Bank staff calculations



... across the region ...

Forecasted GDP growth rates, percent

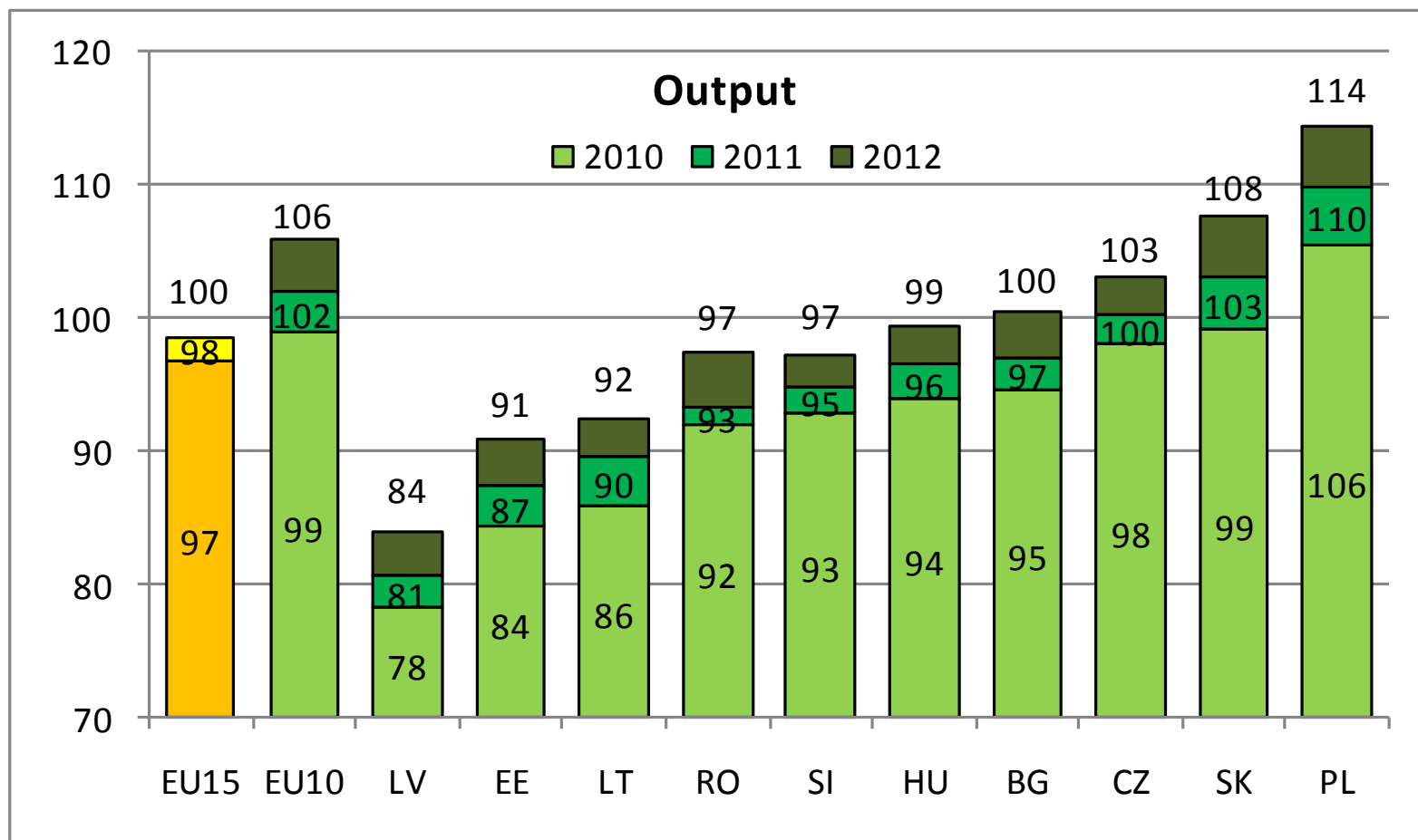


Source: World Bank



... and catch-up to pre-crisis levels ...

Level output in 2010, 2011 and 2012 as percent of the pre-crisis peak output

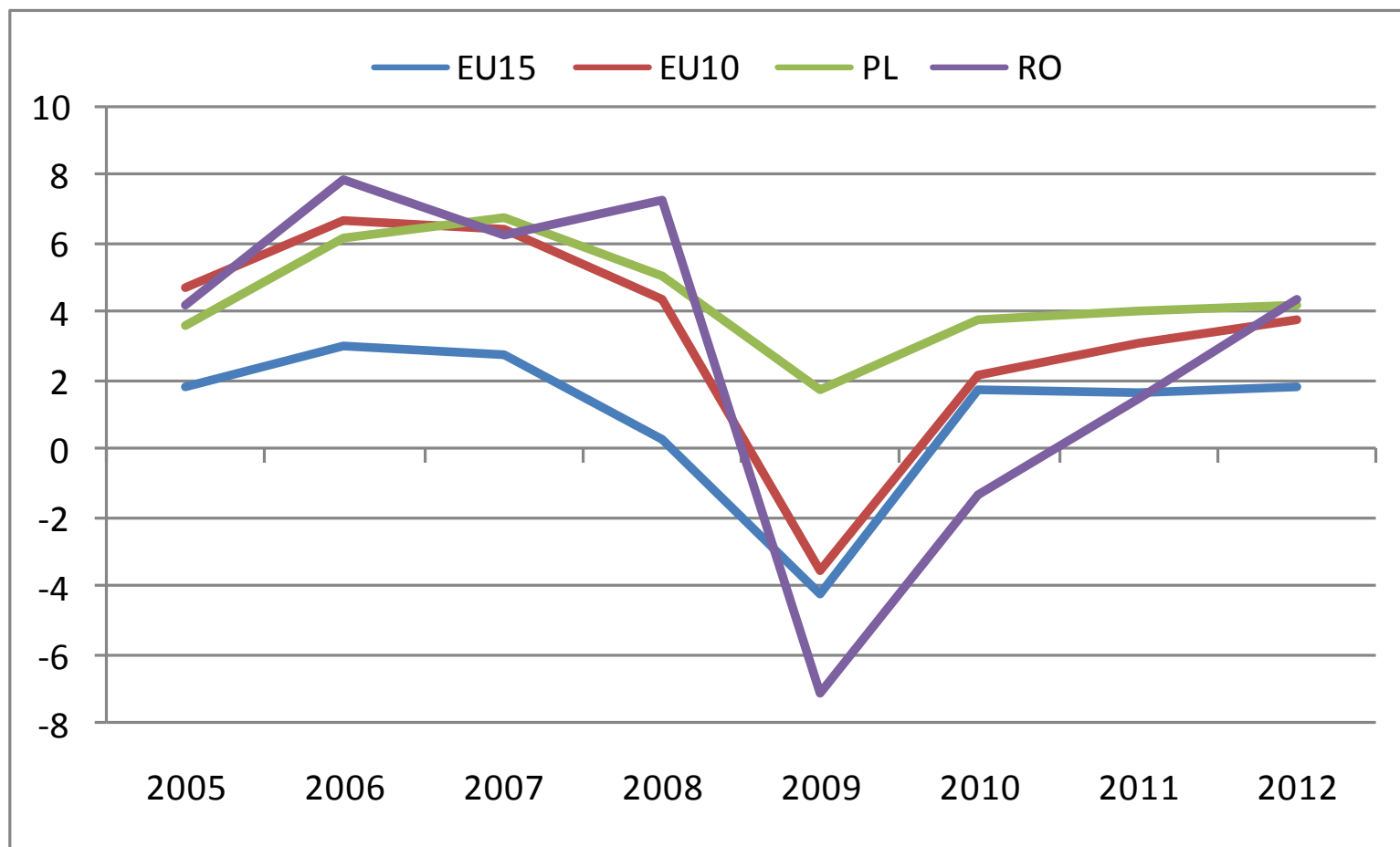


Source: World Bank staff calculations



... as growth advantage over EU10 has returned

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



Source: Eurostat, World Bank

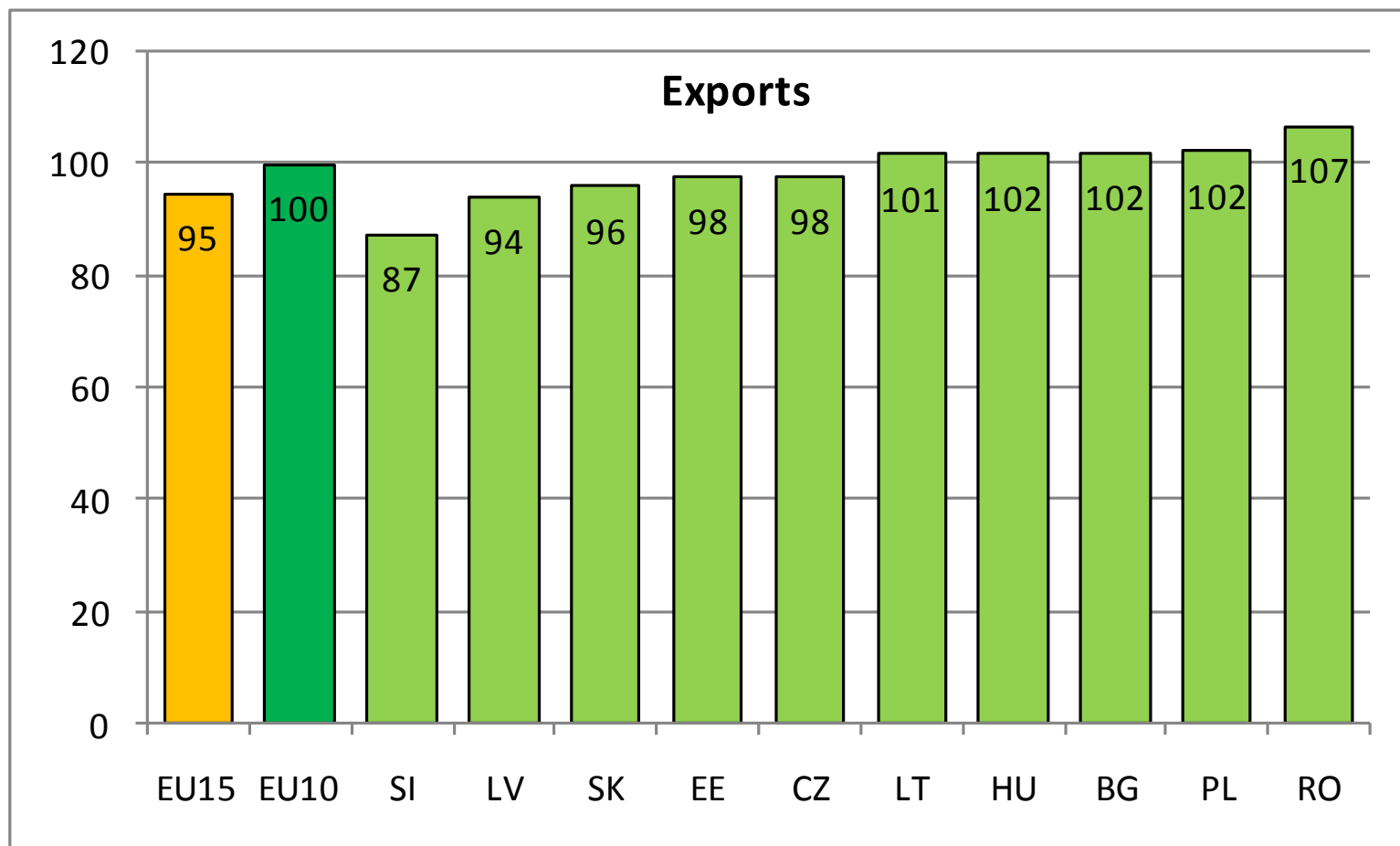


Weak Demand



Exports have rebounded ...

Recovery in exports from pre-crisis peak to 2010, index, peak = 100, seasonally adjusted

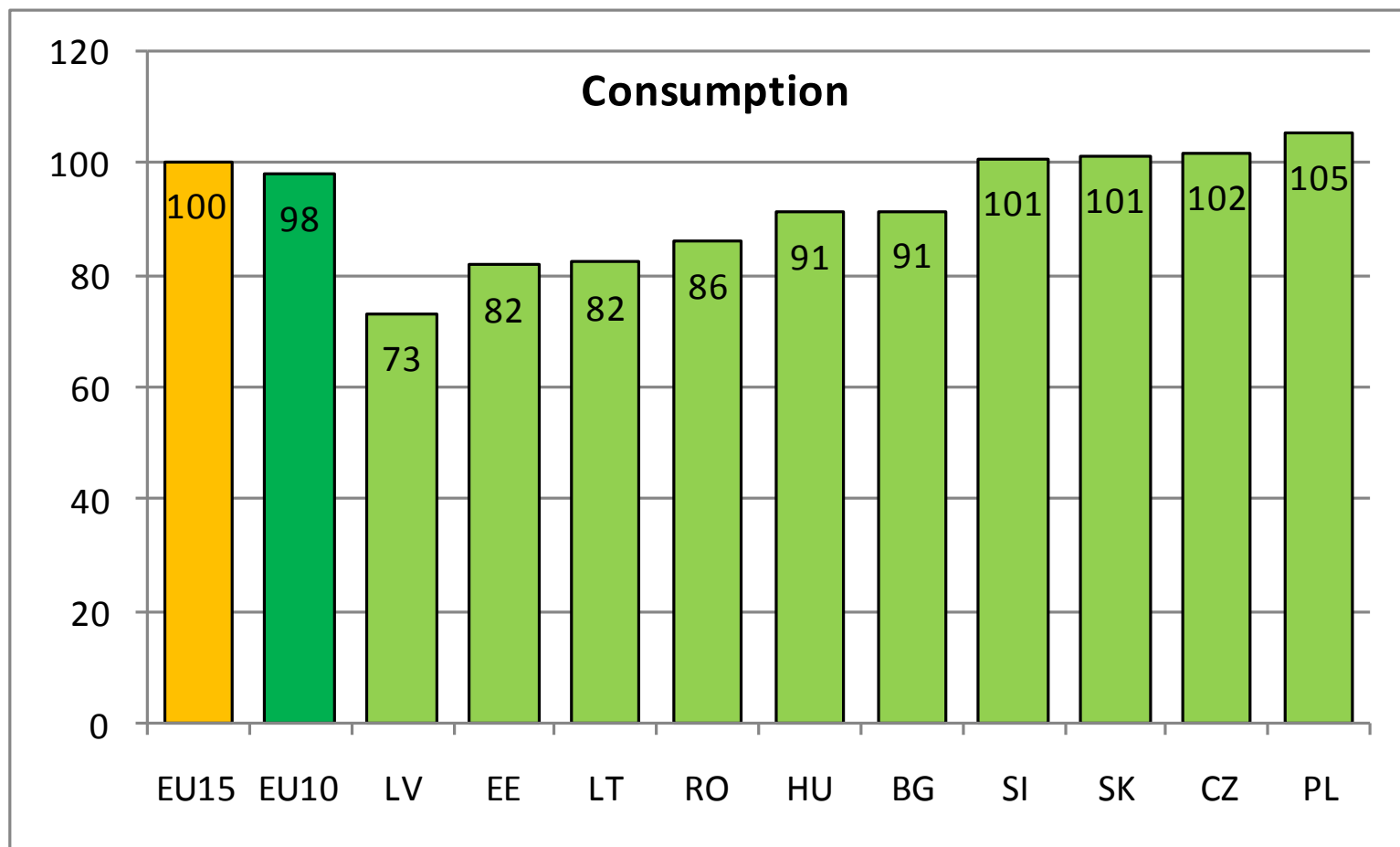


Source: Eurostat, World Bank staff calculations



... but consumption remains weak in some countries ...

Recovery in final consumption from pre-crisis peak to 2010, index, peak = 100, seasonally adjusted

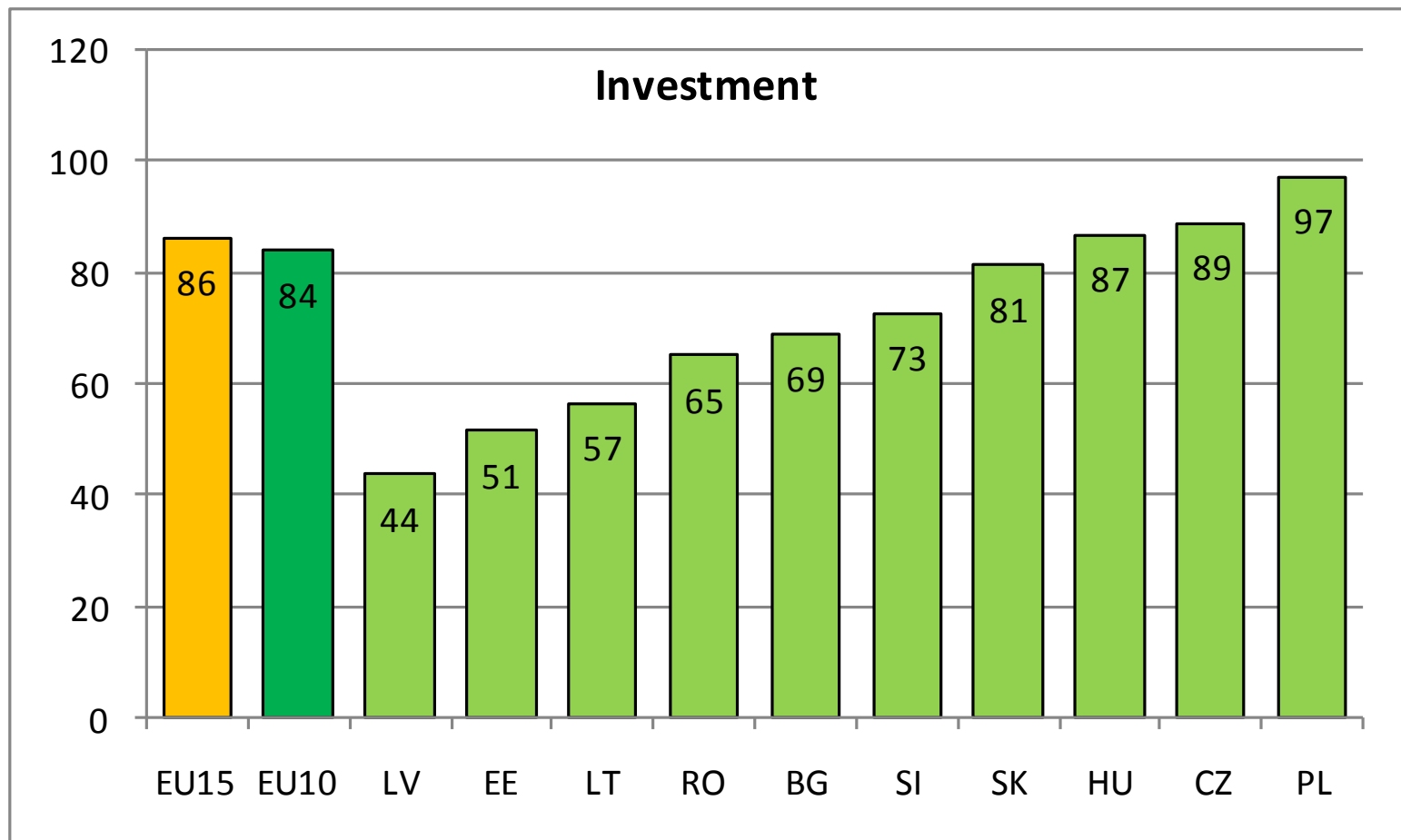


Source: Eurostat, World Bank staff calculations



... and investment weak across the region ...

Recovery in gross fixed investment from pre-crisis peak to 2010, index, peak = 100, seasonally adjusted

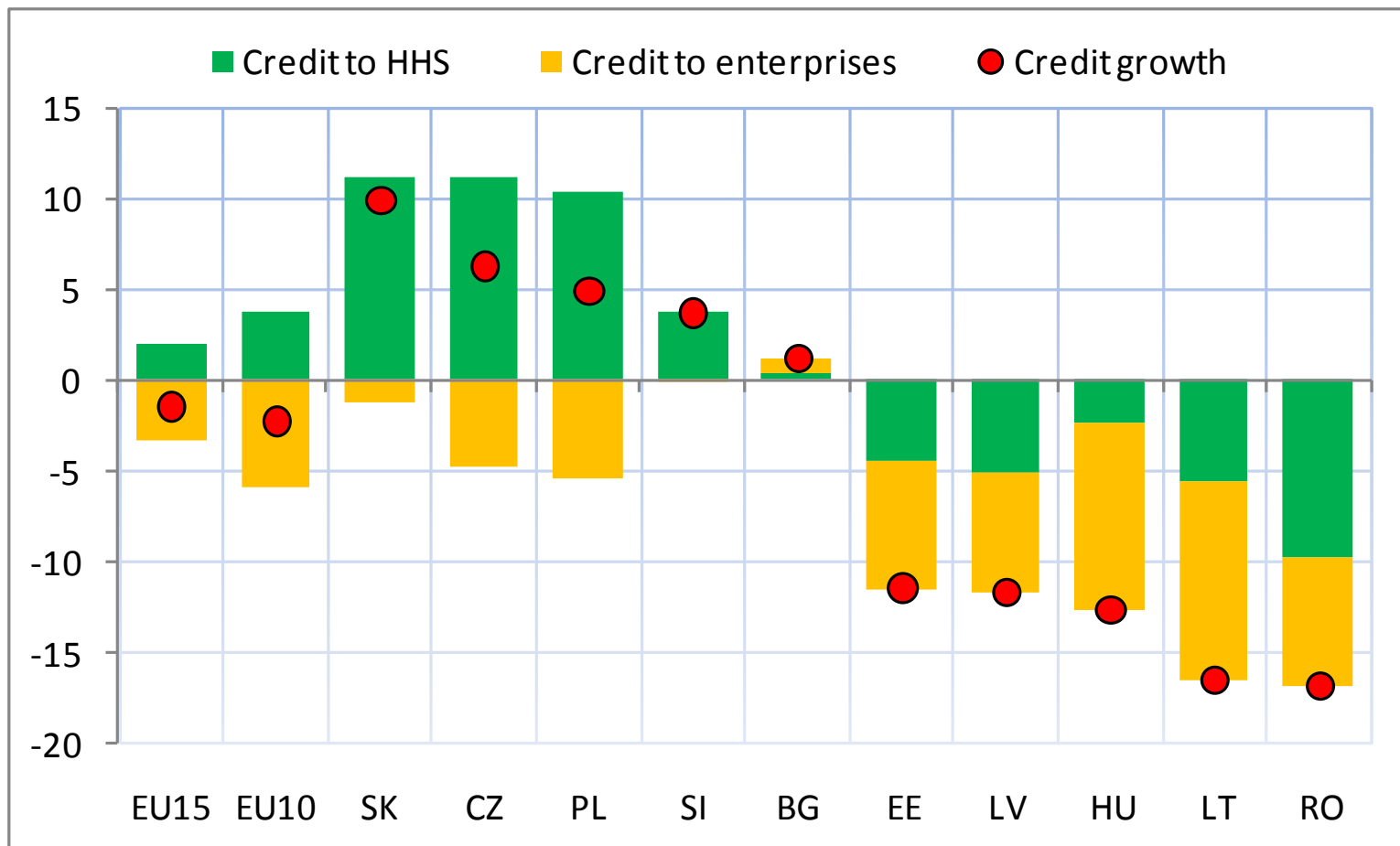


Source: Eurostat, World Bank staff calculations



... as credit growth to enterprises remains weak

Contribution to real credit growth from Oct 2008 to January 2011



Source: ECB, World Bank staff calculations

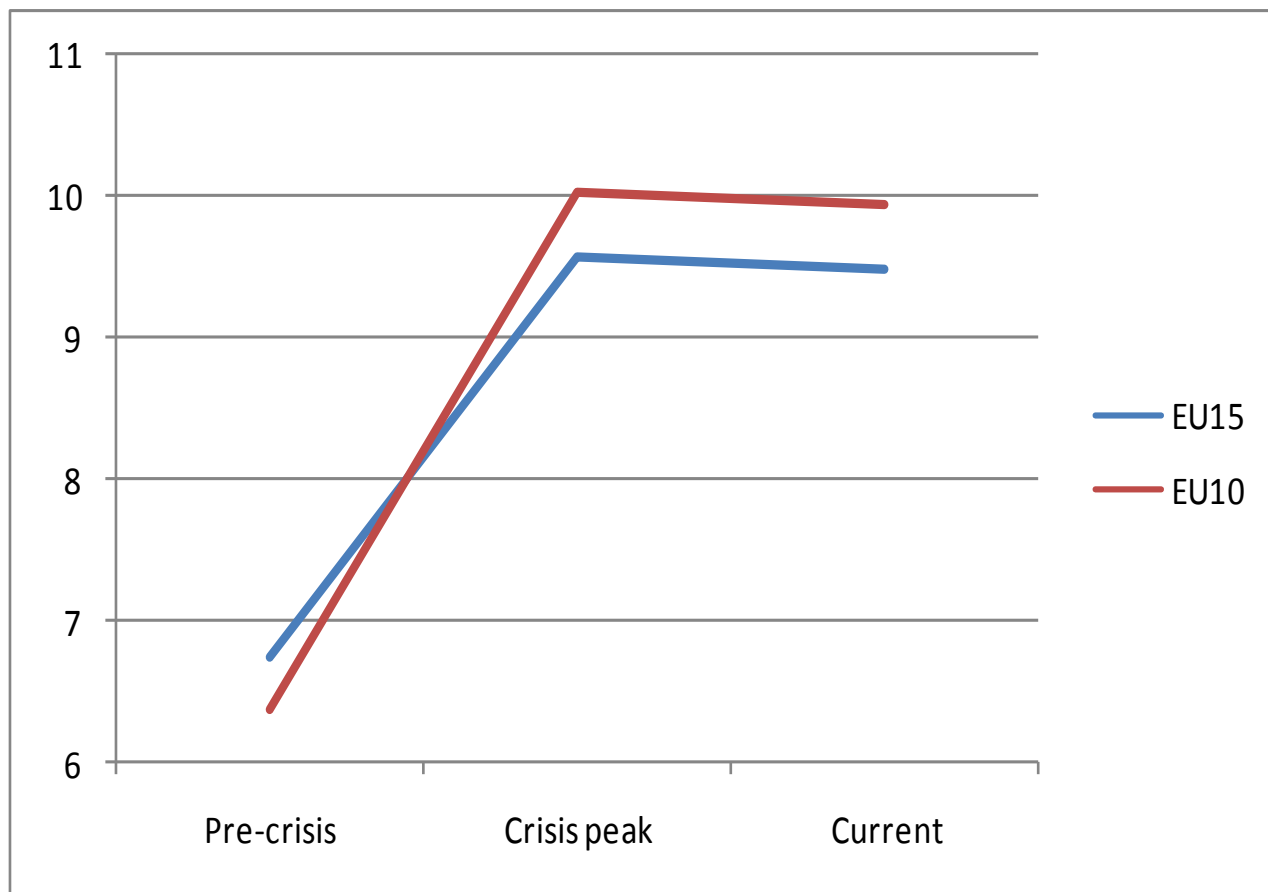


High Unemployment



Recovery is still jobless ...

Unemployment rates in EU10 and EU15, pre-crisis, crisis peak and latest, percent



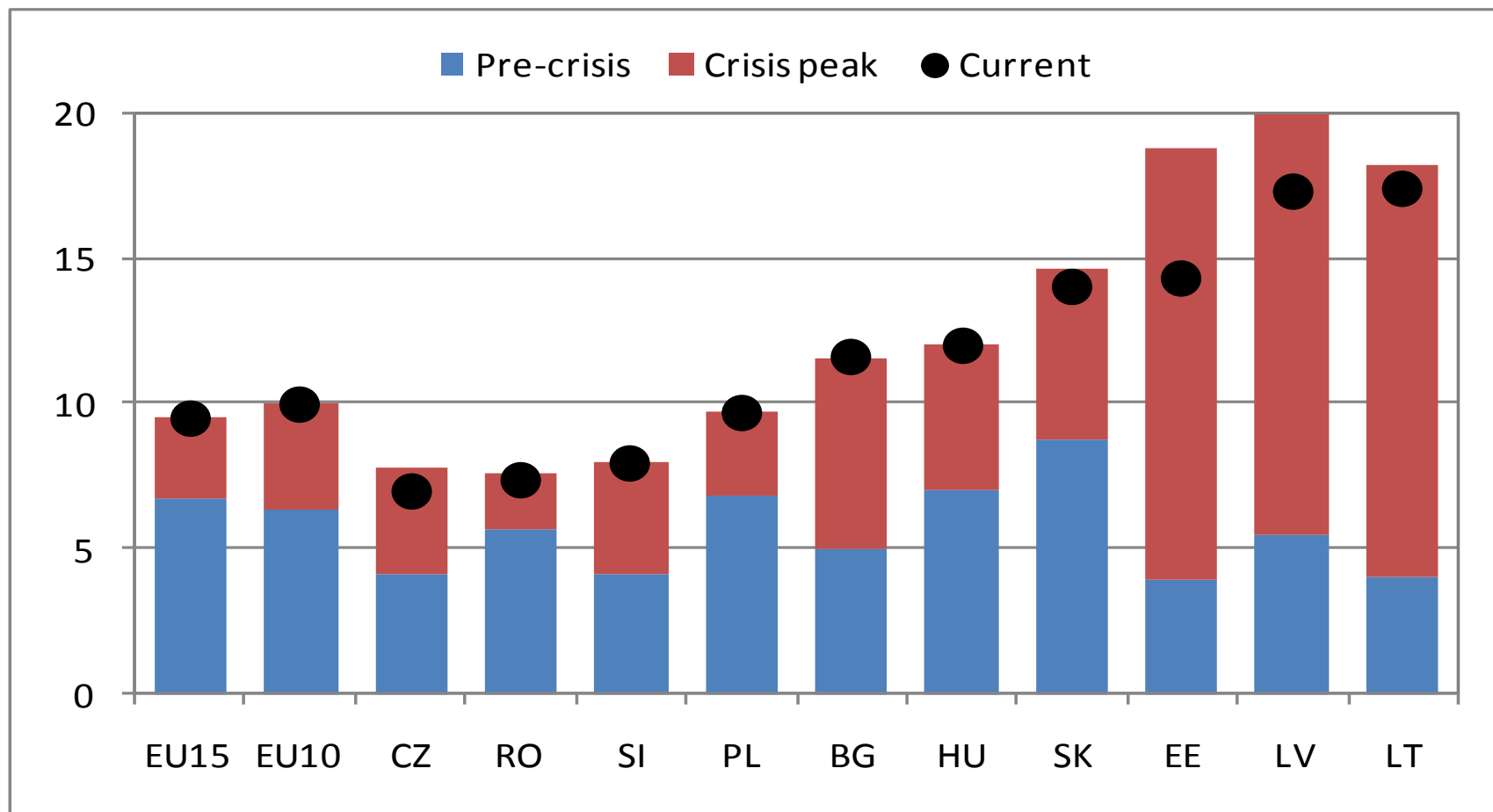
Source: Eurostat, World Bank staff calculation

Notes: Pre-crisis refers to lowest unemployment rate in period 2007-2008, crisis peak refers to highest unemployment rate in period January 2008 to current, current is February 2011.



... as unemployment declined only in few countries ...

Unemployment rates in EU10 and EU15, pre-crisis, crisis peak and latest, percent



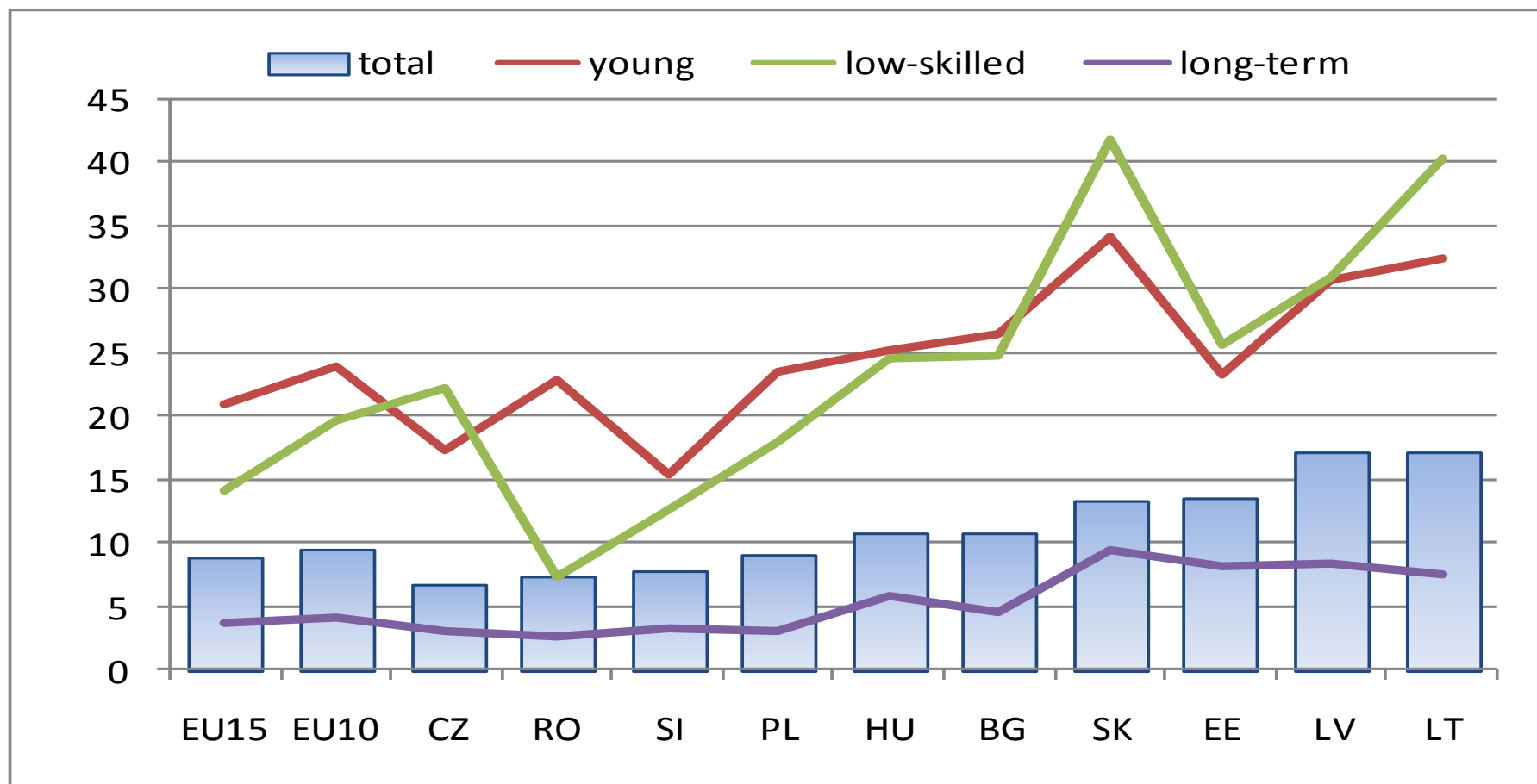
Source: Eurostat, World Bank staff calculation

Notes: Pre-crisis refers to lowest unemployment rate in period 2007-2008, crisis peak refers to highest unemployment rate in period January 2008 to current, current is February 2011.



... and remains high for the young & low-skilled and often of long duration ...

Unemployment rates in EU10 countries in 4Q 2010, percent



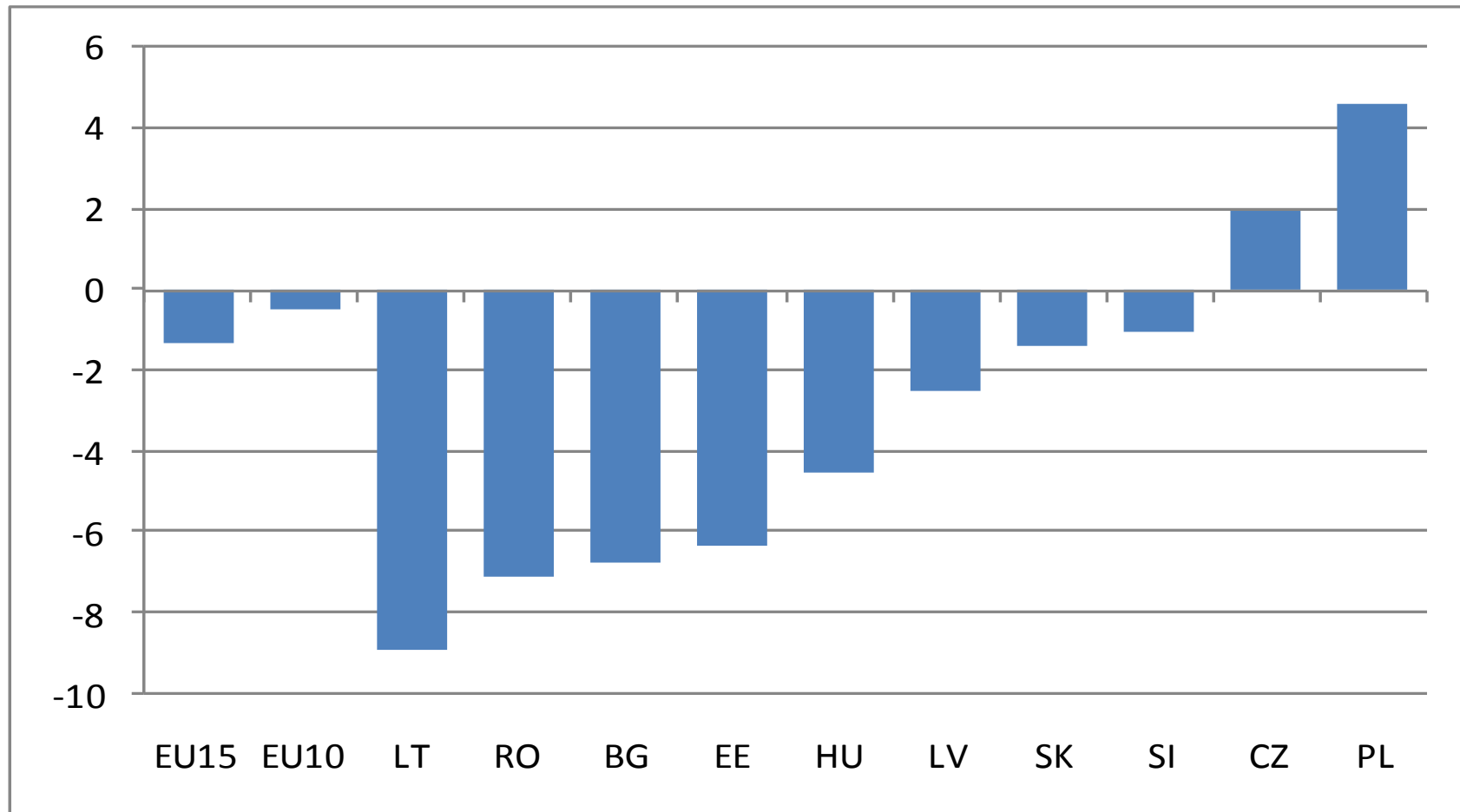
Source: Eurostat, World Bank staff calculation

Notes: LTU refers to 3Q 2010.



... even though labor costs are declining in most countries ...

Real unit labor cost in selected EU10 countries in 4Q 2010, total economy, annual rate of change, not seasonally adjusted, percent



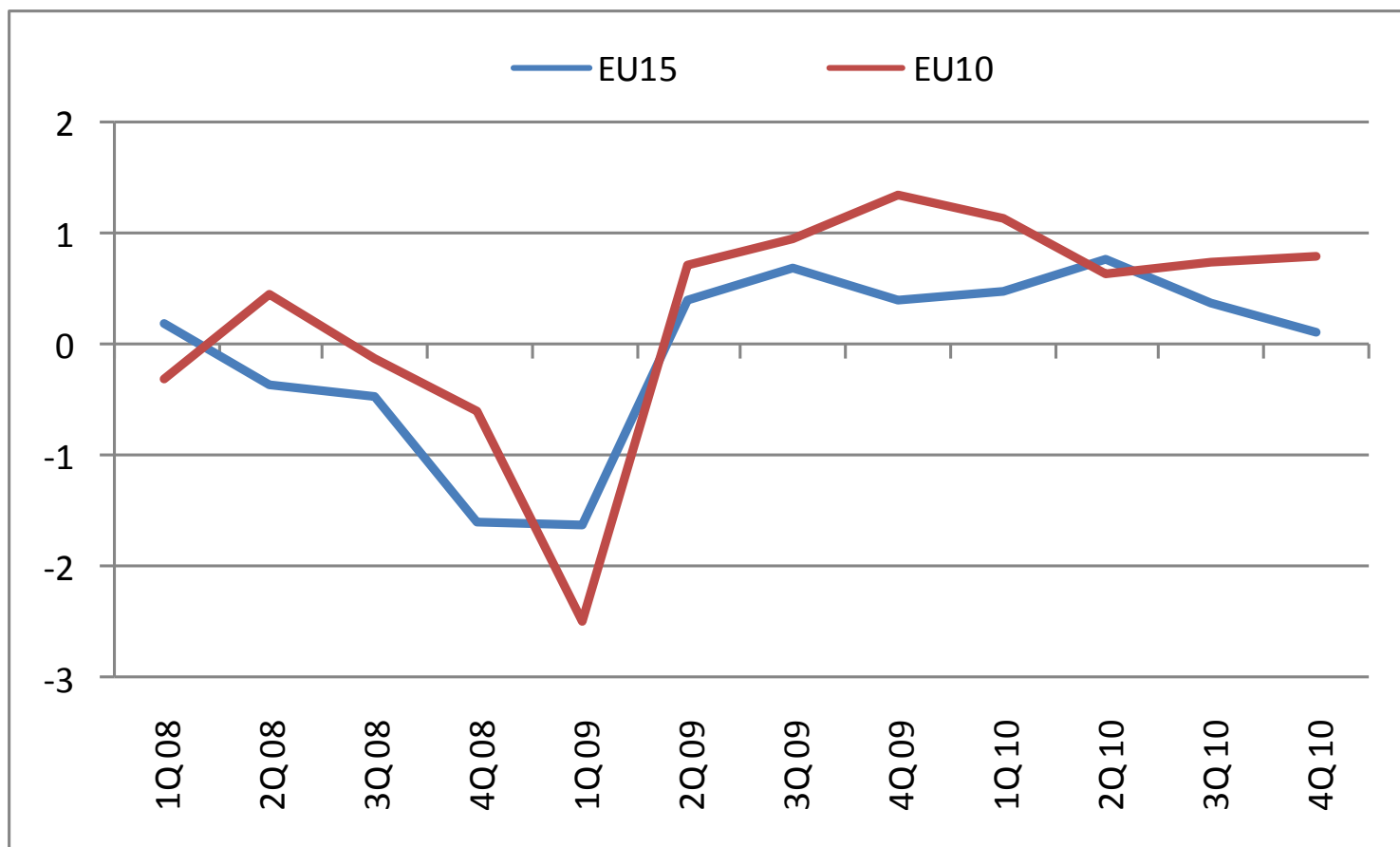
Source: Eurostat, World Bank staff calculations.

Notes: Data for Poland refer to 3Q 2010.



... as higher demand leads to increases in productivity per worker

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



Source: Eurostat, World Bank staff calculations.

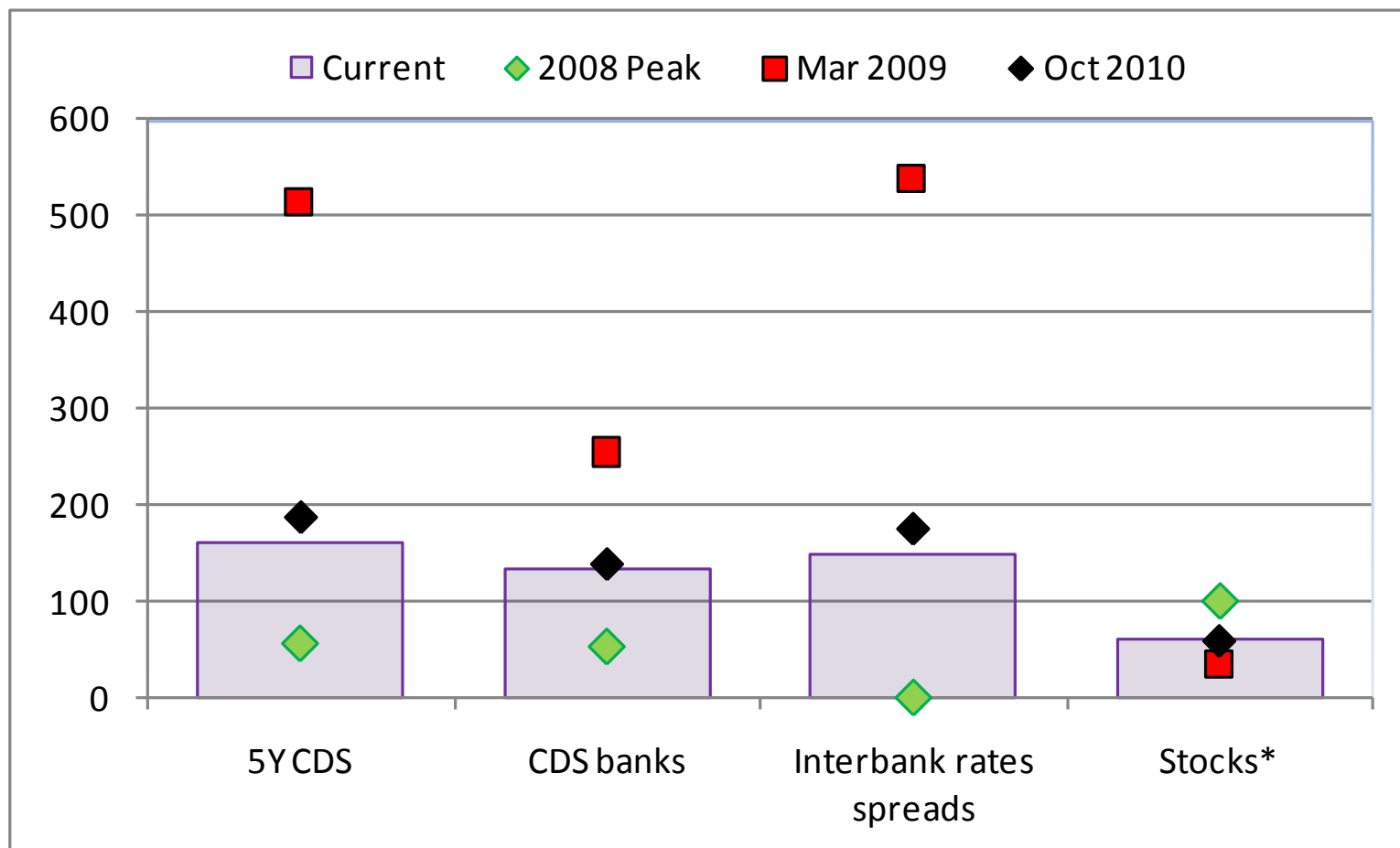


Policies: Stable Financial Markets



Risk appetite has returned ...

Asset class performance, percent change

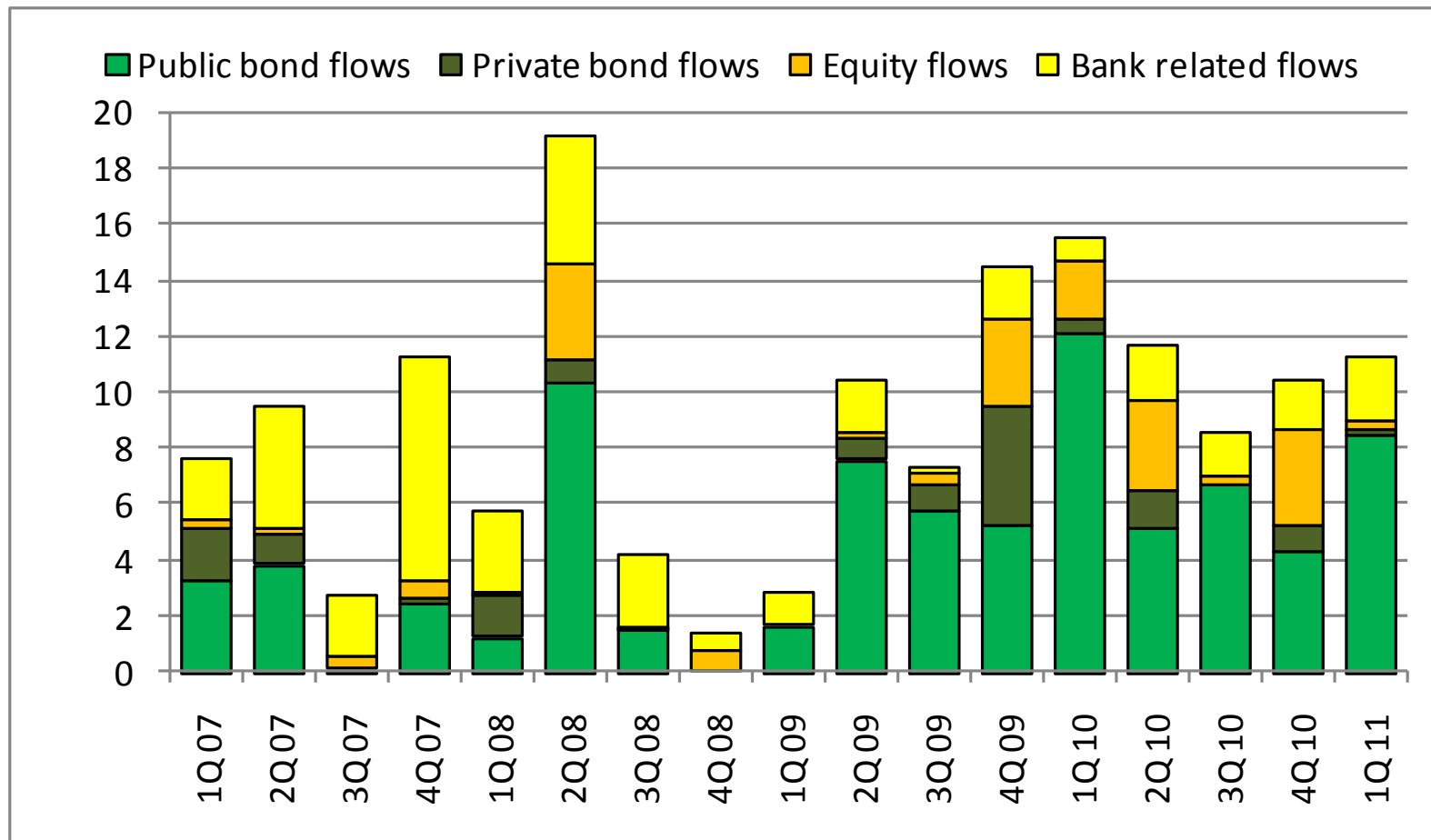


Source: Bloomberg, Reuters, World Bank staff calculations



... and capital flows continued ...

Gross capital inflows to EU10 markets, USD billions

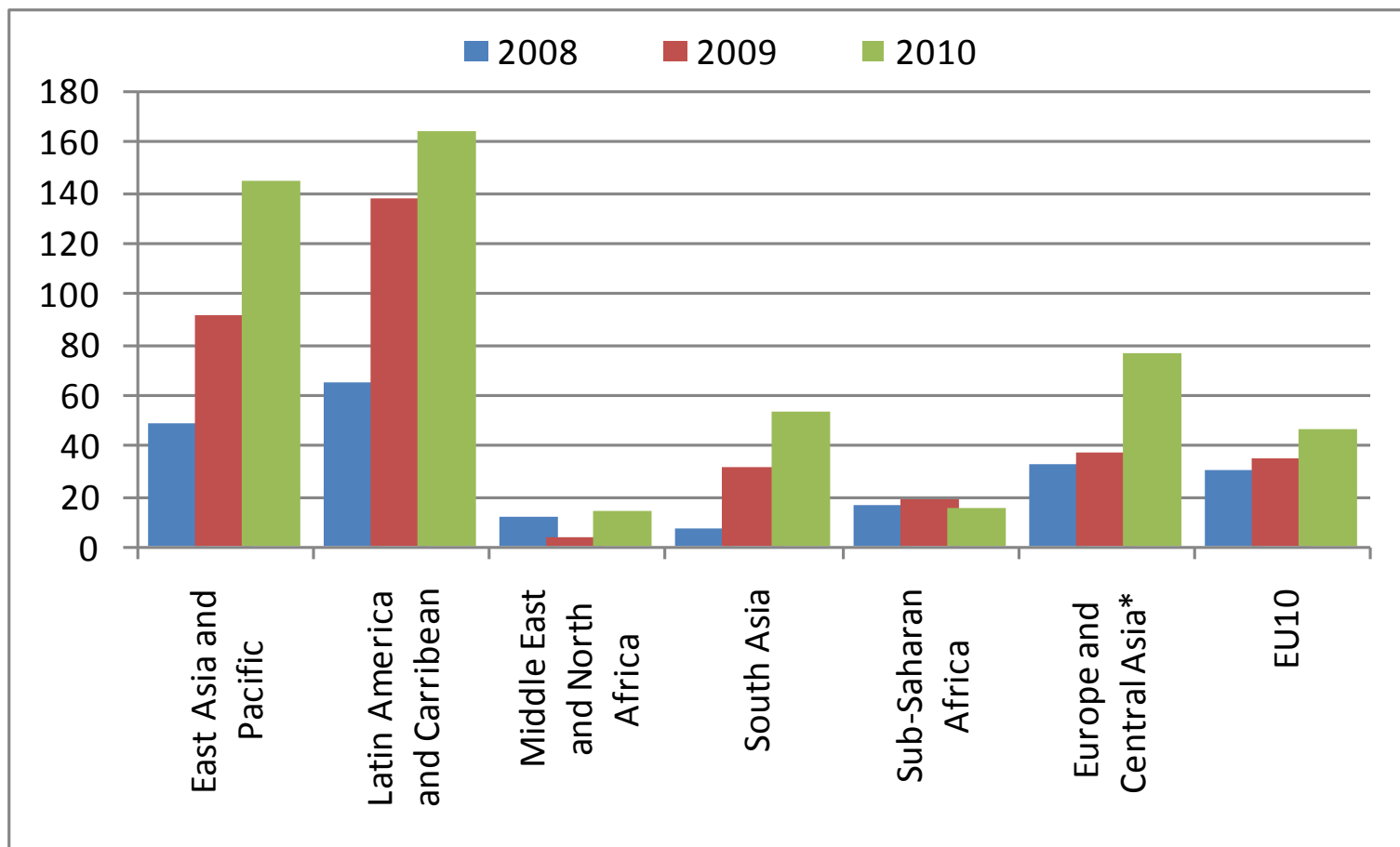


Source: DECPG, World Bank staff calculations



... at moderate rate ...

Gross capital flows EU10 versus other external markets

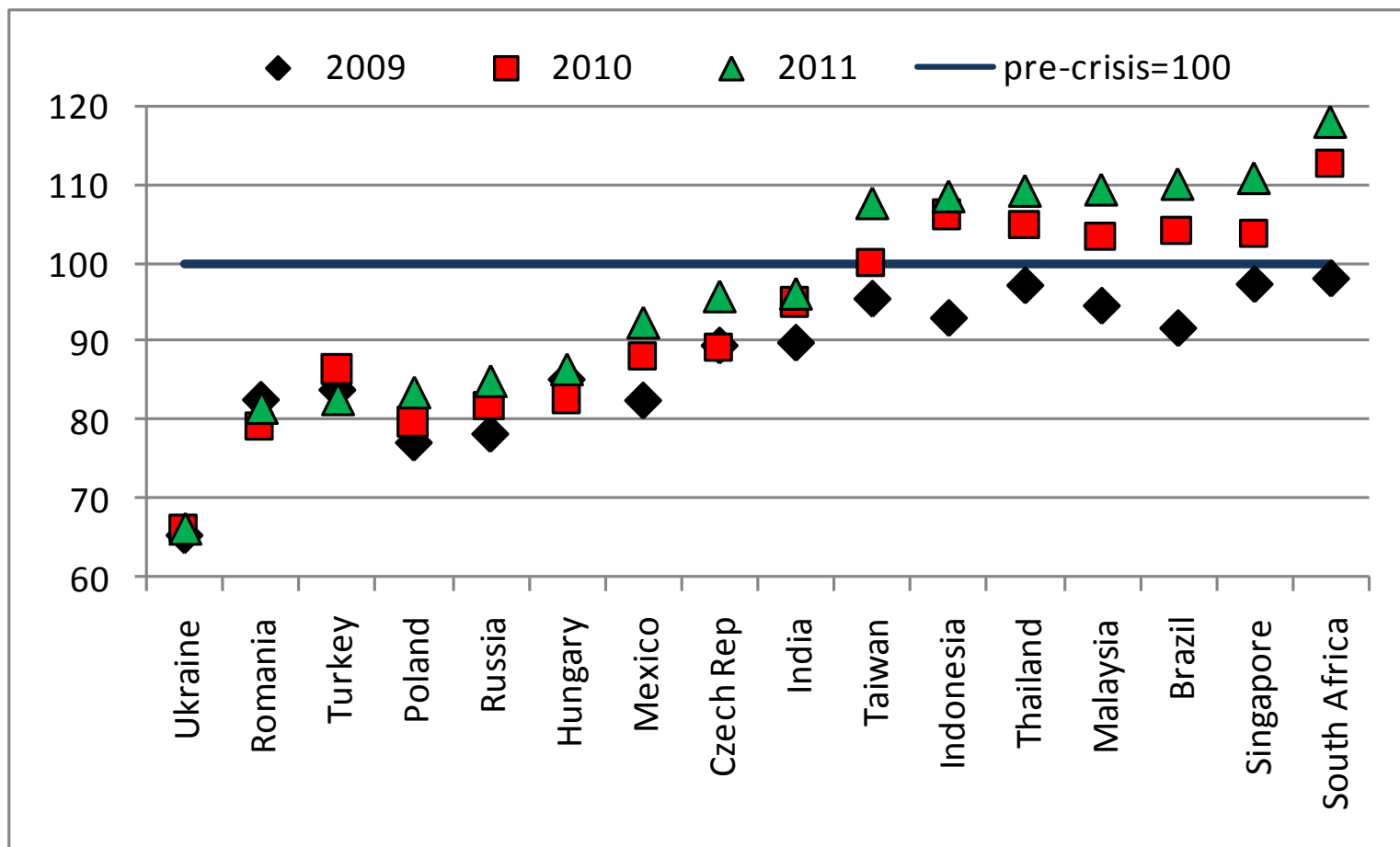


Source: GEM database, World Bank staff calculations



... leaving exchange rates competitive ...

US Dollar exchange rates EU10 versus other external markets, index, 2008=100

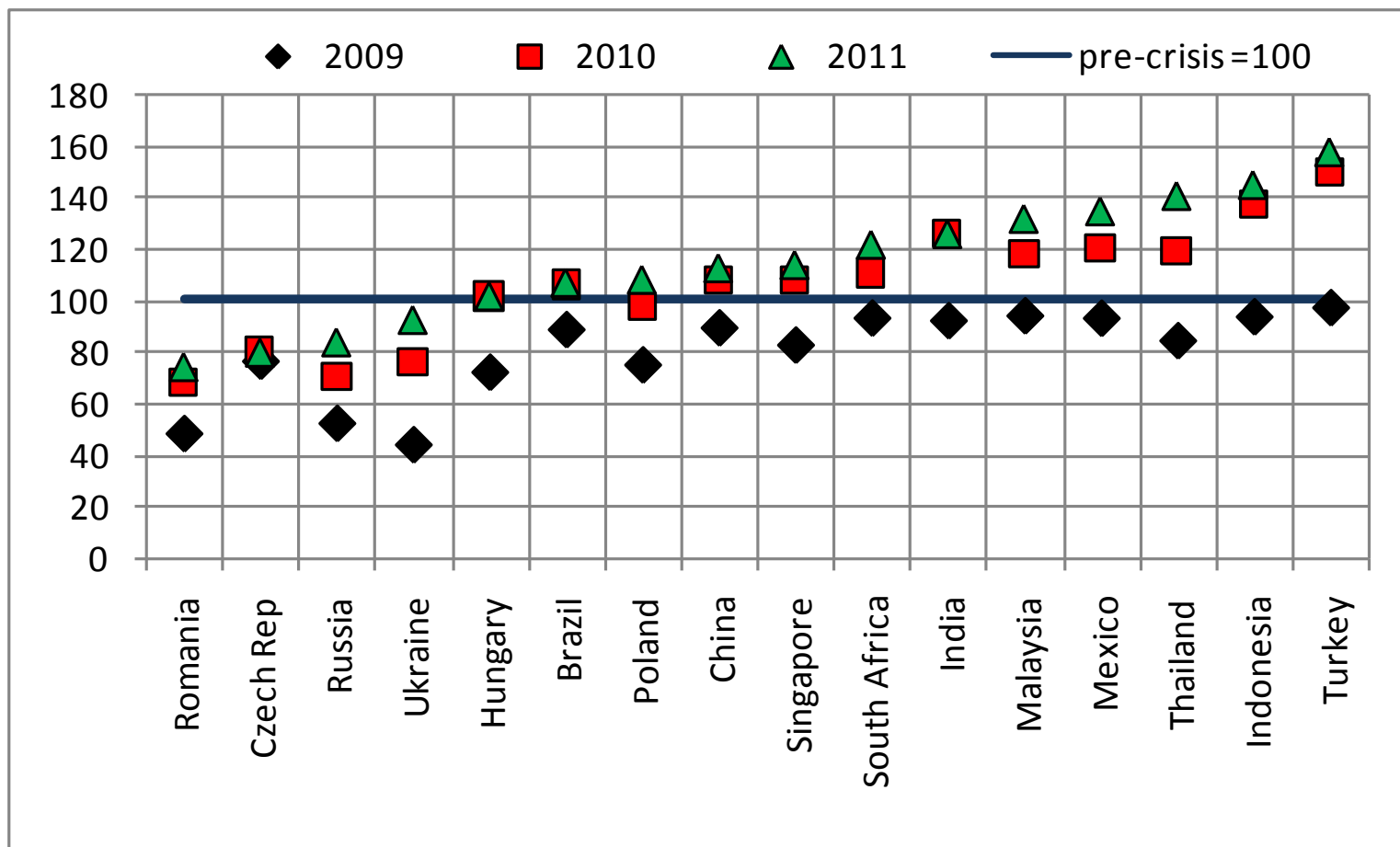


Source: GEM database, World Bank staff calculations



... and stock markets below or close to pre-crisis peaks ...

Stock markets in EU10 versus other emerging markets, index, 2008=100

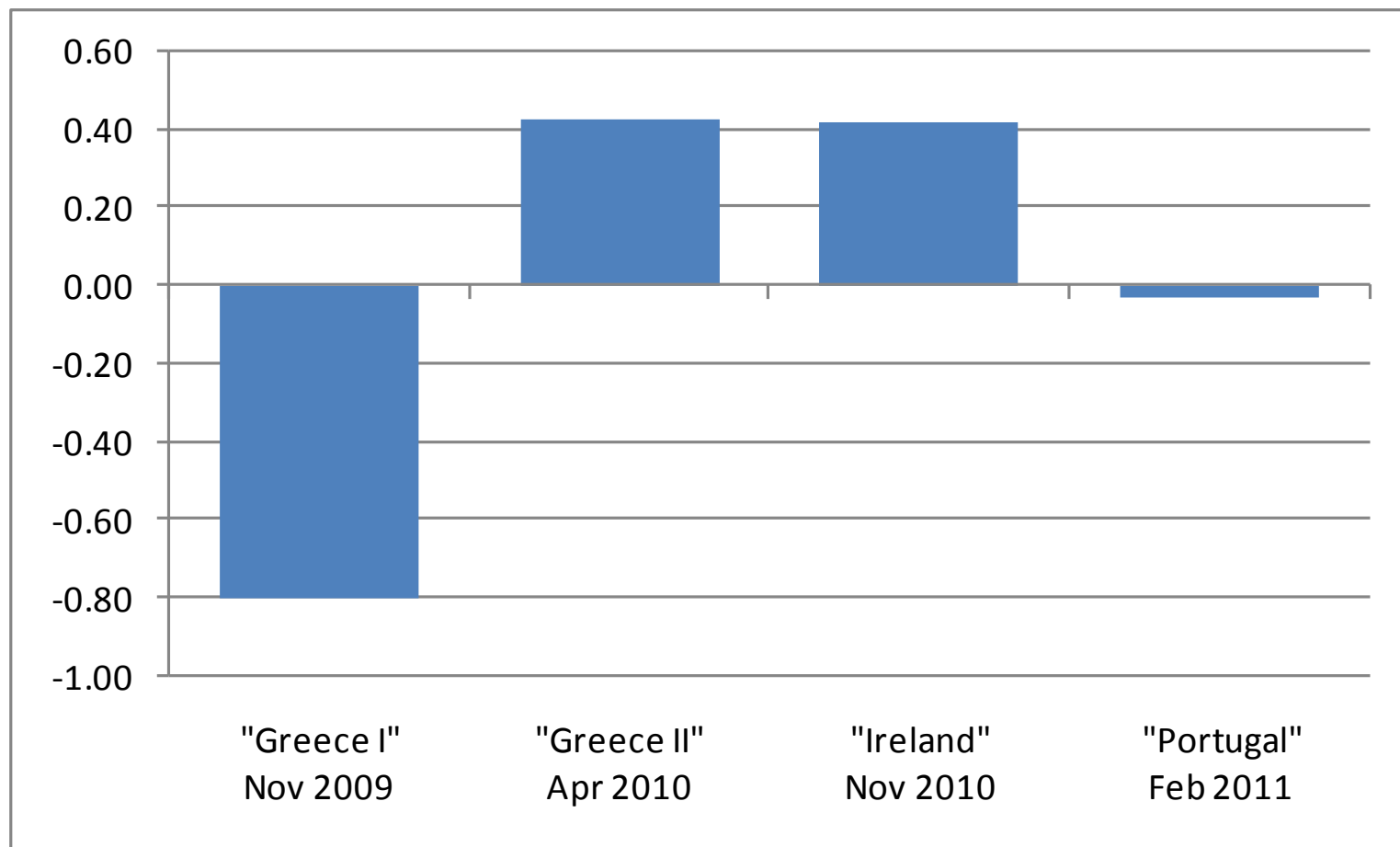


Source: GEM database, World Bank staff calculations



... but spillovers from sovereign debt issues in parts of the euro area are a concern ...

EU10 government bonds' yields correlations with Greek, Irish and Portuguese yields



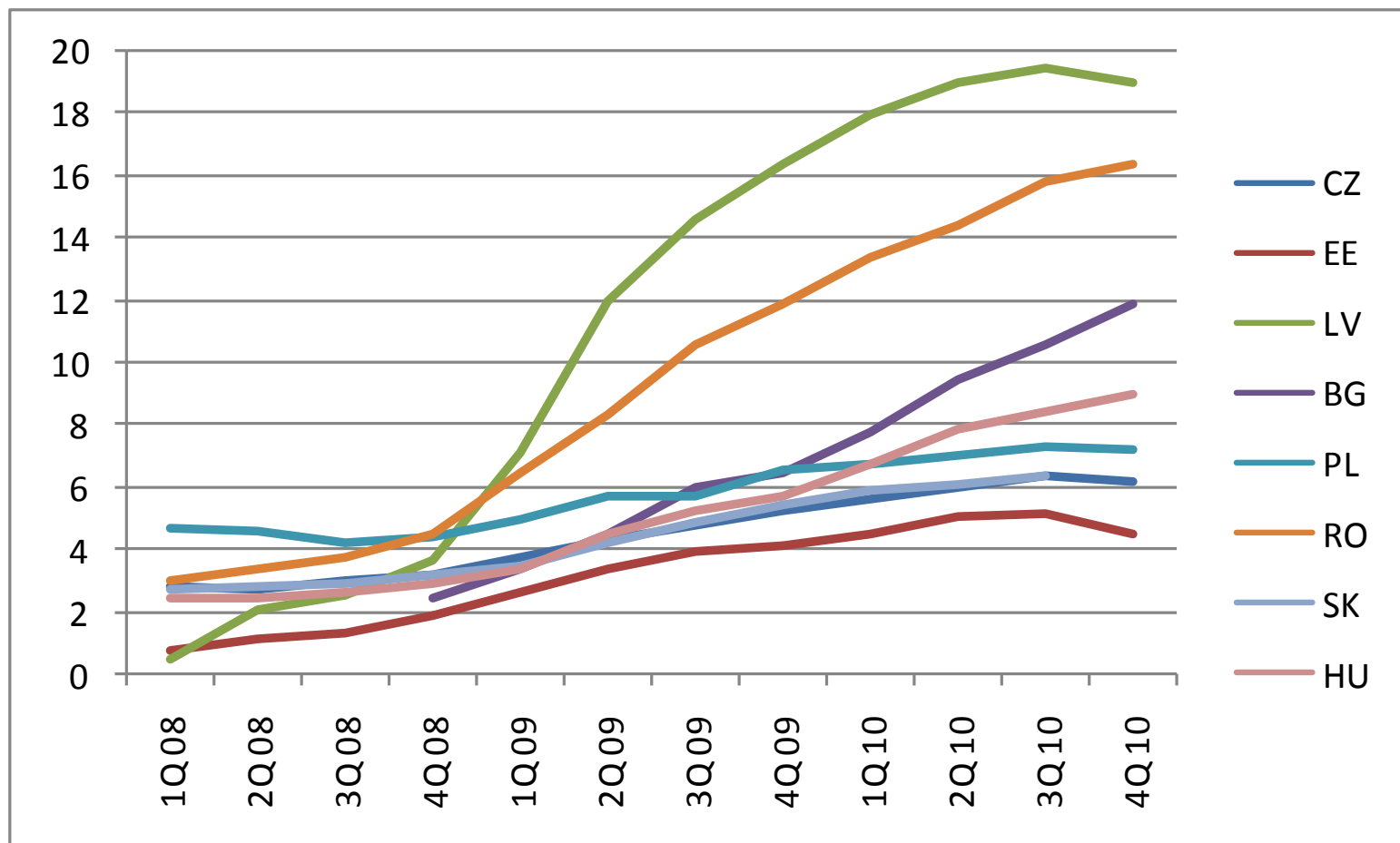
Source: Reuters, Bloomberg, World Bank staff calculations

Notes: 3-month correlations



... as are funding pressures of banks

Non-performing loans of banks in EU10 countries, percent of loan portfolio



Source: Central Banks, World Bank staff calculations.

Notes: Definition of non-performing loans may differ from one country to the next.

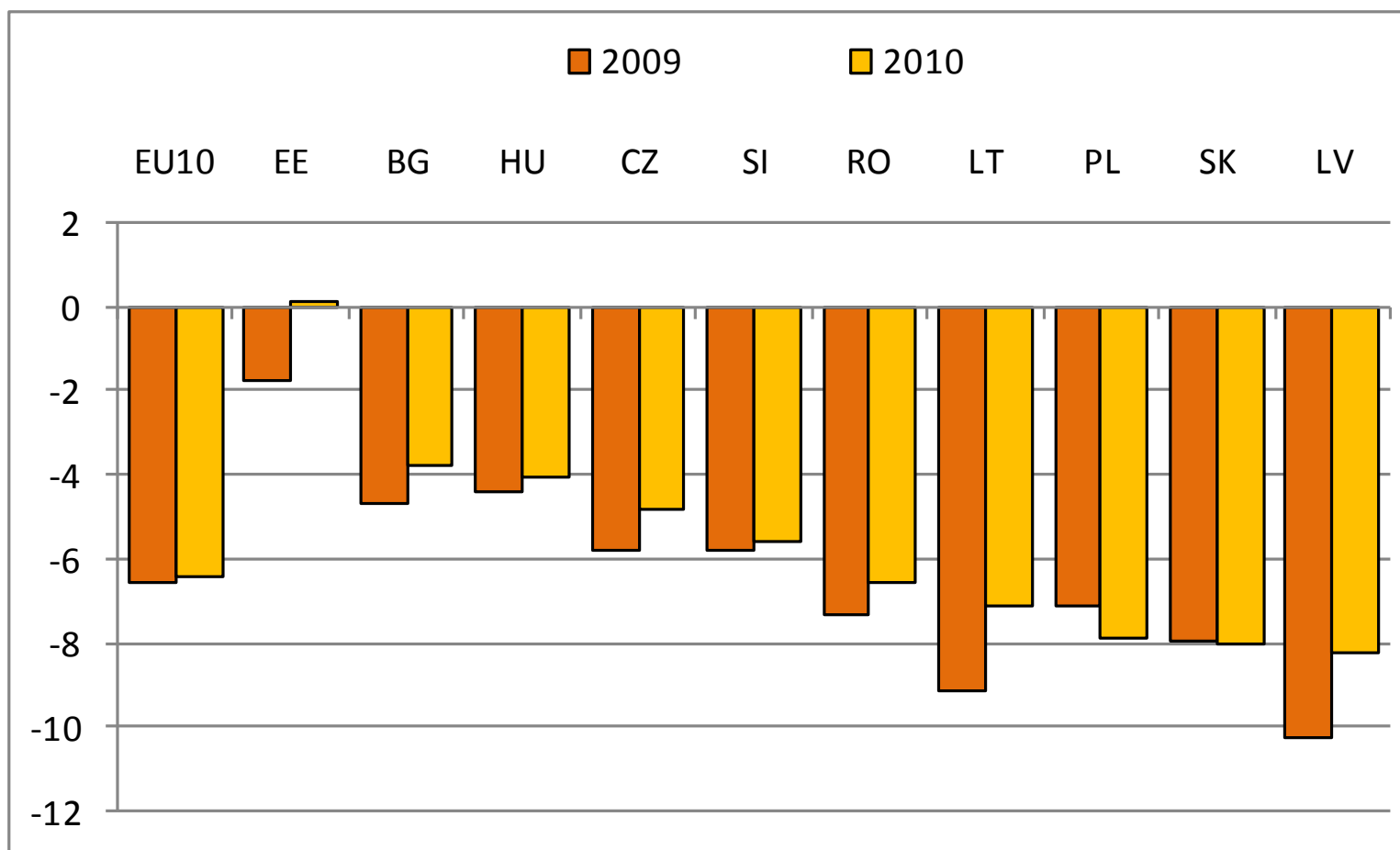


Policies: Sustainable Fiscal Balances



Most countries started fiscal consolidation last year ...

General government fiscal deficit in 2009 and 2010, percent of GDP

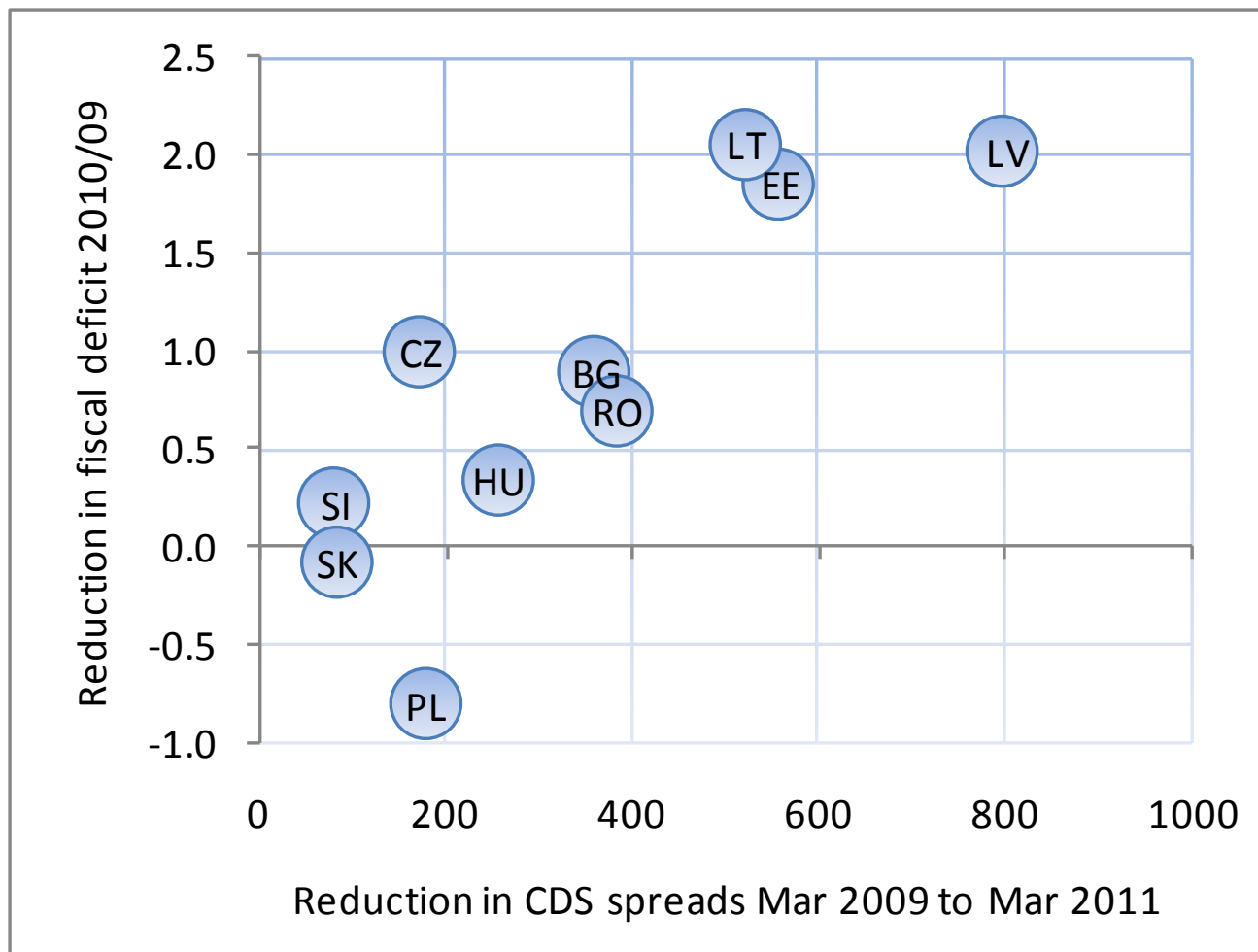


Source: World Bank staff calculations



... helping to improve market risk perception ...

Reduction in CDS spreads vs. reduction in general government fiscal deficit in 2009/10

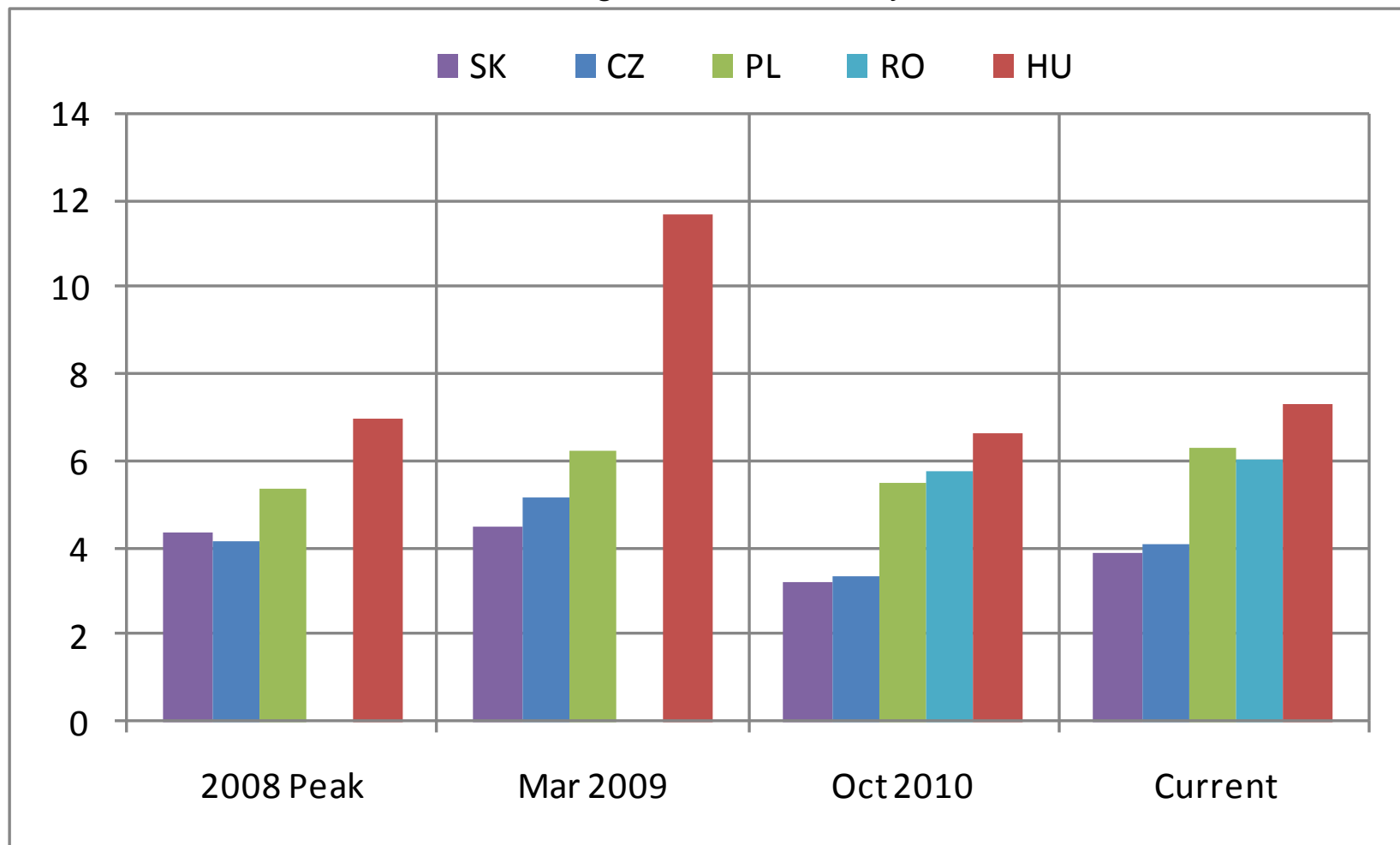


Source: Bloomberg, Eurostat, World Bank staff calculations



... and to moderate increases in government bond yields ...

EU10 government bond yields

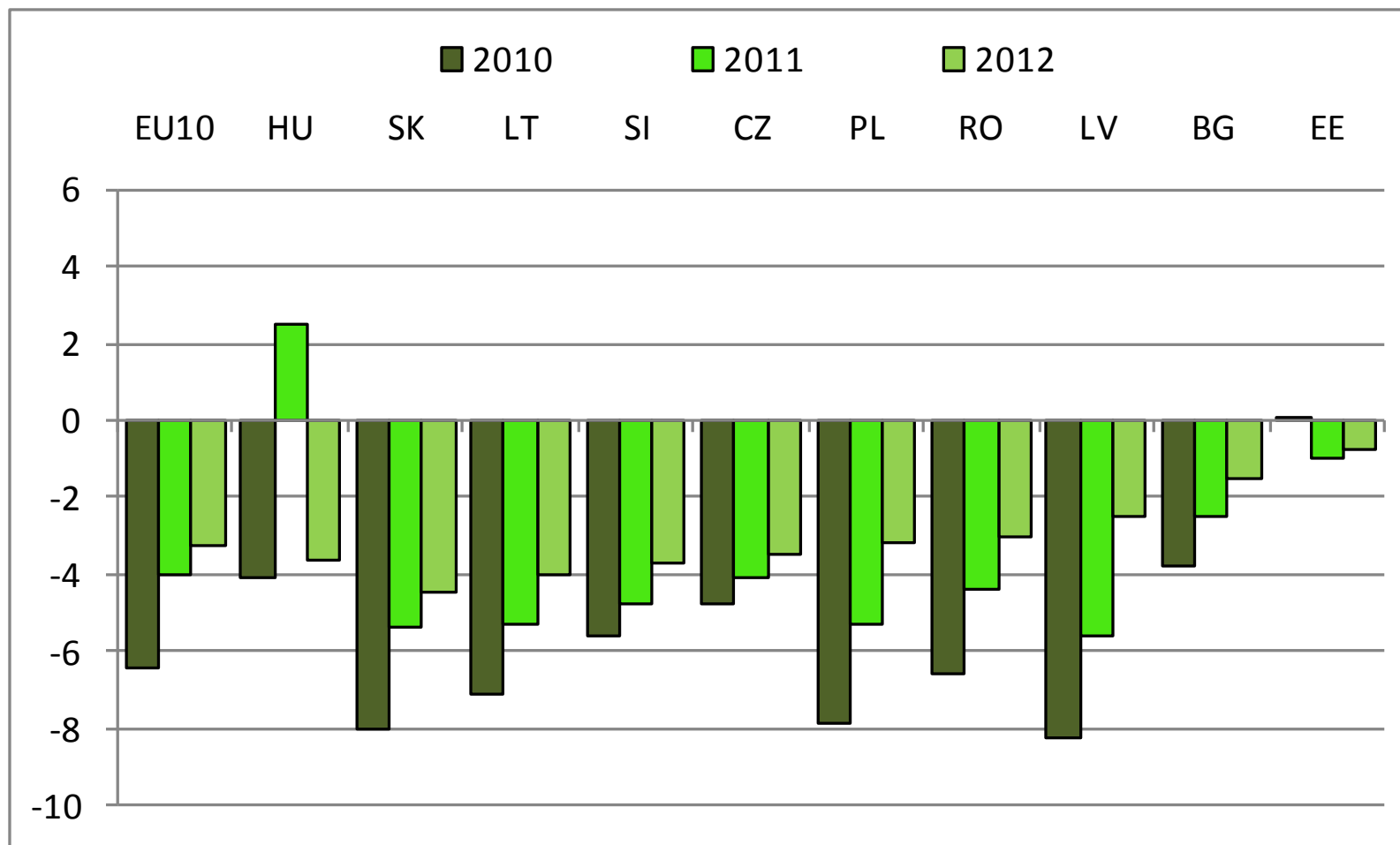


Source: Bloomberg, Eurostat, World Bank staff calculations



... and envision continued adjustments in the next years ...

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

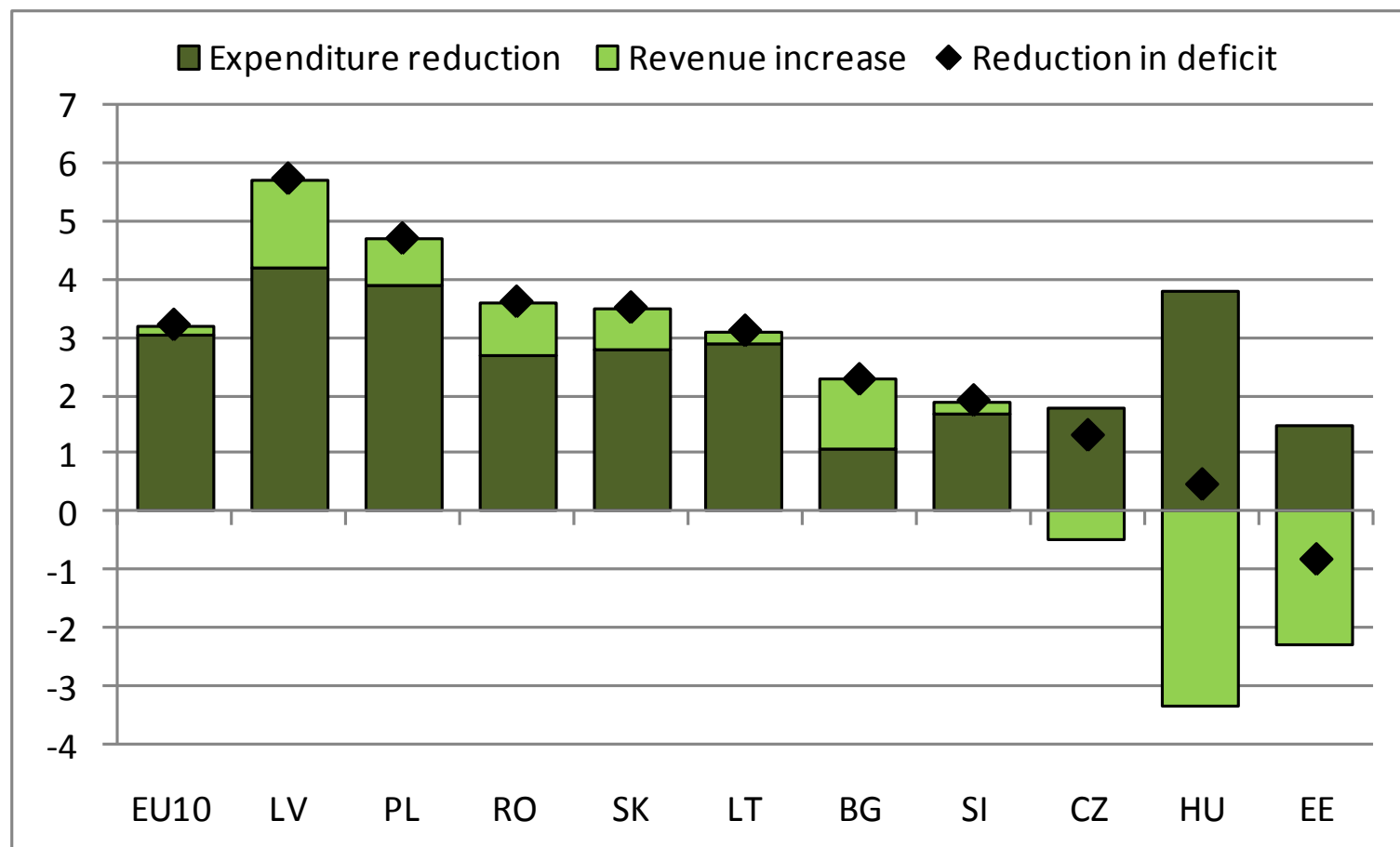


Source: World Bank staff calculations



... mostly on the expenditure side ...

Decomposition of general government fiscal deficit reduction from 2010 to 2012, percent of GDP

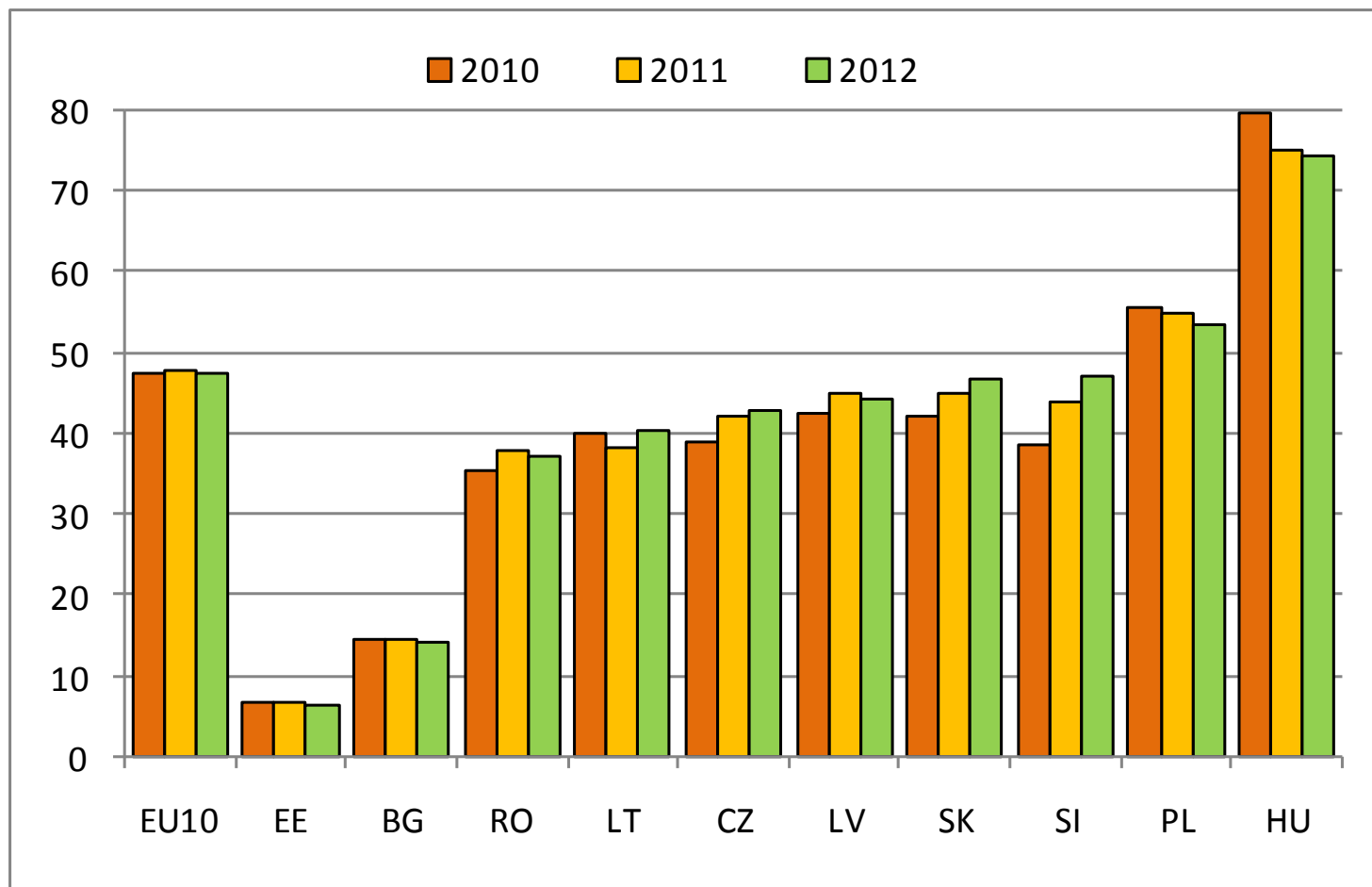


Source: World Bank staff calculations



... also to limit further increases in public debt

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



Source: World Bank staff calculations

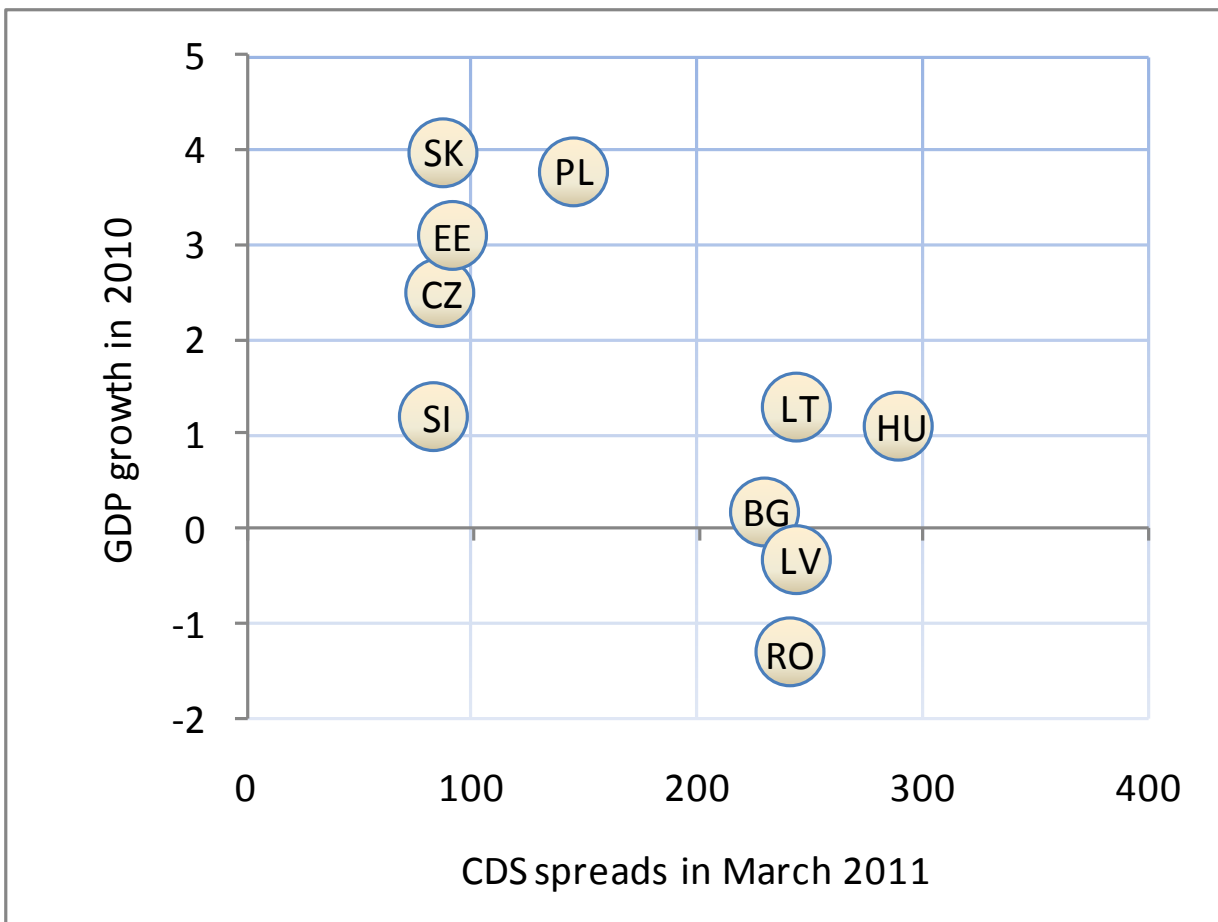


Policies: Structural Reforms



Growth helps to bolster financial markets ...

CDS spreads vs. GDP growth in 2010

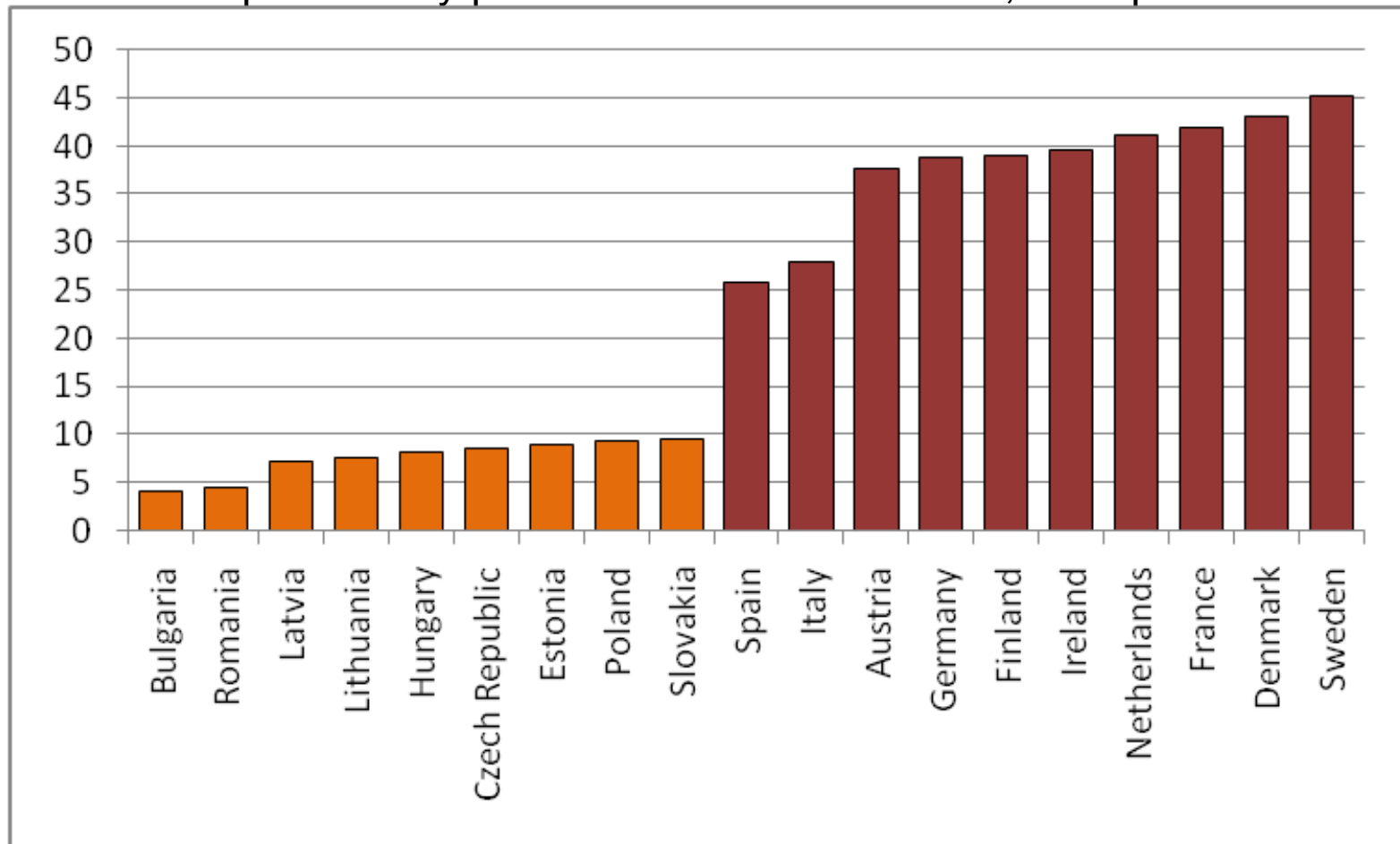


Source: Bloomberg, Eurostat, World Bank staff calculations



... but will require productivity improvements

Real labor productivity per hour worked in 4Q 2010, Euro per hour worked



Source: Eurostat, World Bank staff calculations



THANK YOU

For more information visit:

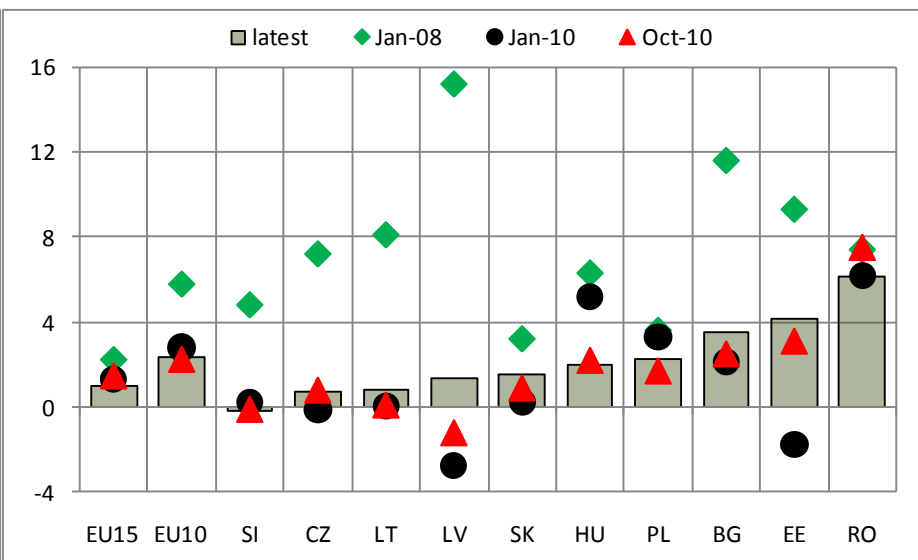
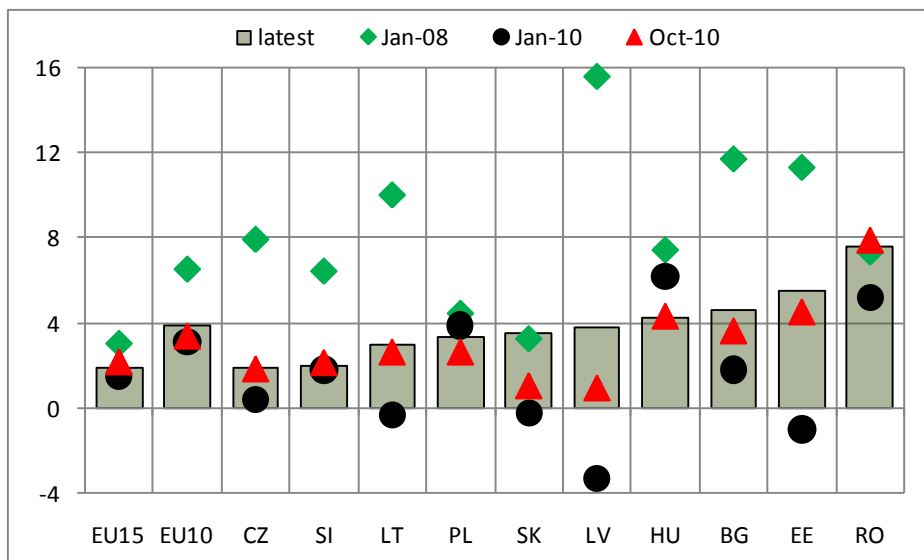
www.worldbank.org/eca/eu10rer

krichter@worldbank.org



Inflation pressures

HICP overall and core inflation in EU10 countries and EU15, year-over-year



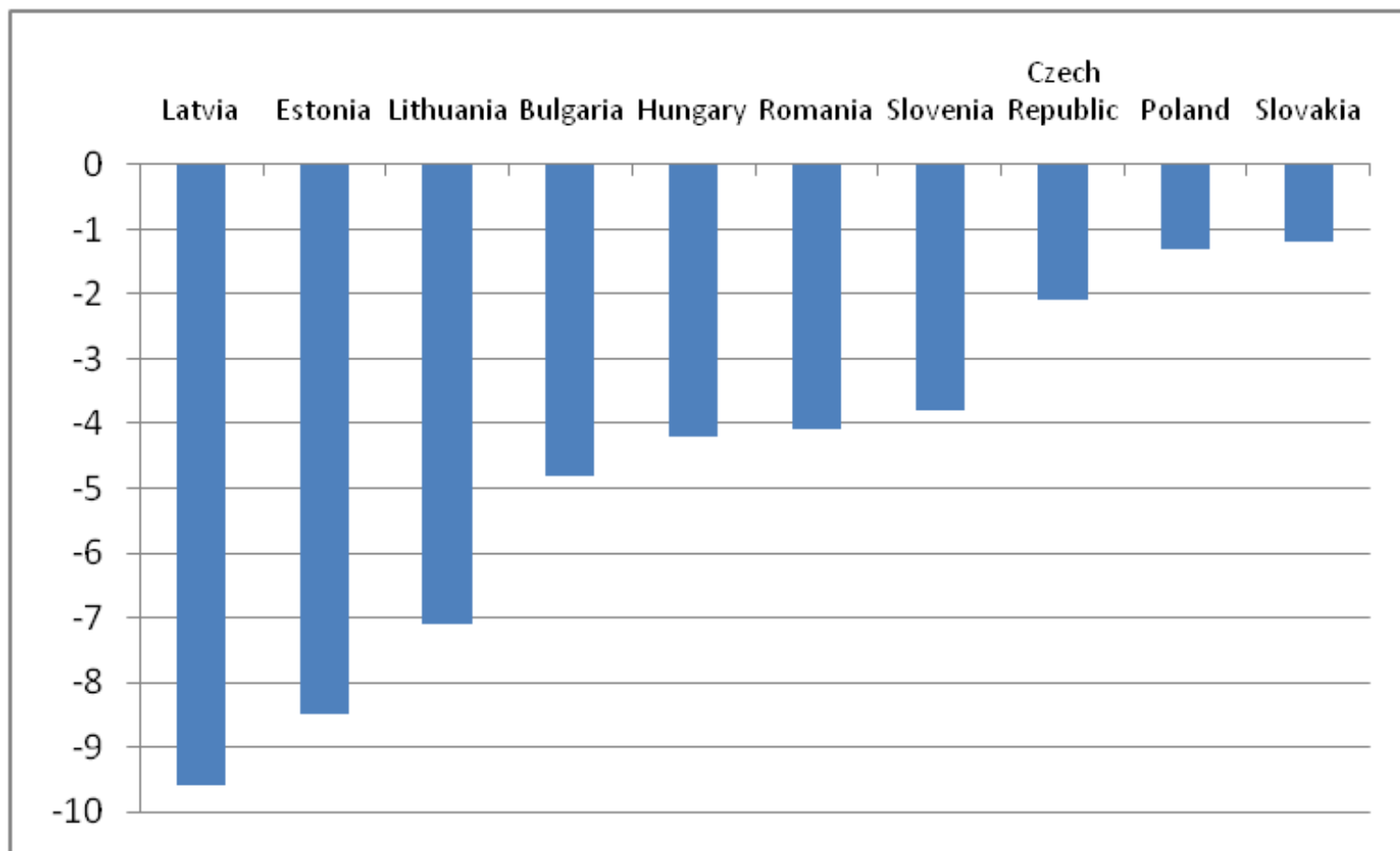
Source: Eurostat, World Bank staff calculations

Notes: Core inflation is overall index excluding energy and unprocessed food



Actual output getting close to potential output in some countries

Gap between actual and potential output in 2010

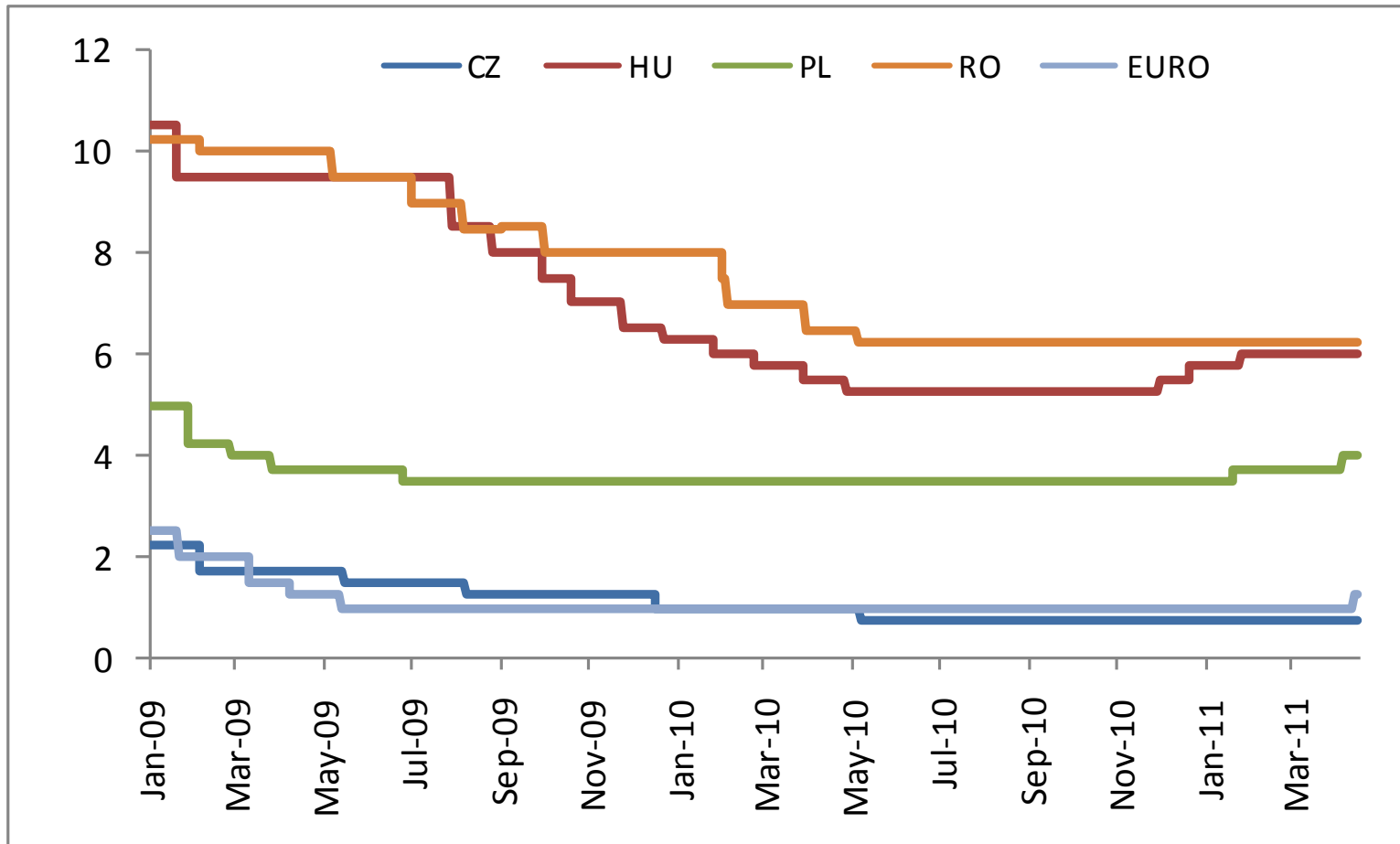


Source: EC Ameco database



Monetary policy has started to tighten in some countries

Key monetary policy interest rates



Source: Central Banks