



World Bank EU8 Quarterly Economic Report September 2006¹

EU8

HIGHLIGHTS OF THE REPORT

Main Report

- The external environment for the EU8 countries has remained broadly favorable so far in 2006 despite higher oil prices and global interest rates. In particular, growth gained further strength in the eurozone in the second quarter of the year. The turbulence in international financial markets in May-June, that saw a sharp correction in emerging markets, was short-lived and most markets had fully recovered by the end of August. Global growth is expected to remain strong through 2007, although there are significant downside risks.
- Recent elections in the Visegrad countries have revealed a high degree of fragmentation which has forced parties to make fragile alliances and allowed populist forces to gain influence. This is hampering progress on the outstanding reform agenda, complicating the required fiscal and macroeconomic stabilization, and delaying euro adoption in all EU8 countries except Slovenia and possibly Slovakia.
- The strong growth momentum and broadening recovery in domestic demand have allowed the EU8 economies to weather the negative effects of high oil prices and recent turbulence in global financial markets. Growth in the region should continue to be robust albeit with some cooling in the Baltic countries and adjustment related slowdown in Hungary. Unemployment continues to decline in most countries in the region, and labor market bottlenecks—exacerbated by sizeable outflows of workers since EU accession—are becoming increasingly evident in the Baltic countries and even Poland.
- Inflation pressures appear to be mounting across the region. Wage growth is accelerating rapidly in the Baltic countries, credit is growing rapidly in most countries, and several of the new EU member states have not yet seen the full impact of rising commodity and producer prices—in part reflecting freezing in some countries of excise taxes on fuels. Inflation problems have already delayed euro adoption plans in the Baltic countries and may add to the fiscal challenges of securing euro adoption in 2009 in Slovakia.
- The EU8 countries have not taken adequate advantage of the benign growth conditions to tighten the fiscal stance and advance major structural reforms. Fiscal balances are worsening in several of the countries in 2006 and budget plans for 2007 point to further laxity (except notably in Hungary where there is no alternative to strong consolidation efforts). Hungary needs to follow through fully on its ambitious fiscal adjustment program and move quickly to prepare the critical spending reforms. Poland needs at a minimum to stick firmly to its informal deficit ceiling and Slovakia needs to put in place

¹ This report is generally based on information available through end-August, 2006. The report was prepared by a team of World Bank economists in the region led by Thomas Laursen and including Paulina Bucun, Leszek Kasek, Ewa Korczyc, Anton Marcincin, and Emilia Skrok.

a well-specified and credible medium-term fiscal framework consistent with its deficit targets. The Czech Republic should avoid drifting away from its hard-won fiscal consolidation.

- Progress on advancing the outstanding reform agenda has been mixed following EU accession. While some further progress has been made in the region on broad indicators of transition, economic freedom and corruption, other indicators relating to competitiveness, ease of doing business, and governance reveal a more nuanced and less positive picture. Among other areas, privatization and liberalization in “strategic sectors” has seen little momentum in most of the EU8 countries. Furthermore, critical public finance and administration reforms, which are not well captured in the broader indices above, have largely stalled. These areas should be given urgent attention, including to enhance needed infrastructure investments and make the most of the large amounts of EU structural funds soon becoming available.

Special Topic: Labor Migration from the New EU Member States

- Labor mobility from the EU8 following accession has intensified, including because of the opening of selected EU15 labor markets for EU8 nationals (initially the U.K., Ireland, and Sweden, but now joined by Italy, Spain, Portugal, Greece, and Finland).² These developments were fueled both by existing labor market disequilibria in the sending countries and demand for relatively cheap foreign labor in the receiving economies. These trends are a natural and desirable part of the integration process where capital moves east and labor west in search of higher returns.
- Evidence from receiving countries suggests that they have little to fear from lifting remaining restrictions on labor migration from the New Member States. Fears of massive inflows of workers and devastating impacts on receiving labor markets have not materialized. Post-accession migration from the EU8 has so far been dominated by short-term labor flows, with migrants attracted by labor market opportunities abroad, rather than “welfare tourism.” True, migrants have not been immediately eligible for social benefits, but even in Sweden, where they are eligible, inflows have been modest. Although they were funneled to the only three countries without entry restrictions (U.K., Ireland, and Sweden), the more permanent inflows of foreign workers have proven quite manageable. Entering as they did some of the most dynamic labor markets in the EU, they generally supplemented domestic labor, rather than displacing it or depressing local wages, and helped sustain solid economic growth. A general lifting of the remaining entry restrictions would spread the flows more evenly, and make them manageable even for the less flexible labor markets.
- From the sending countries’ perspective, outflows of labor are more of a mixed blessing. Recent migrants tend to be younger and relatively well-educated people, already working in their home countries or with good employment prospects. This has led to skills shortages and bottlenecks in several sectors in the main sending countries, especially the smaller Baltic States where labor outflows have been relatively large. This is, in turn, is leading to increasing wage pressures and reinforcing already strong inflationary pressures thus complicating euro adoption plans. It may also gradually slow output growth and will place a greater burden on domestic workers in caring for their nations’ rapidly aging populations. At the same time, sending countries are benefiting from increased remittances from workers abroad who may also return with additional human capital.

² Part of the newly registered flows reflect formalization of already residing workers.

- Governments need to manage this process more proactively. Further efforts are needed to stimulate labor force participation and employment, including reducing high labor taxes and in some cases social benefits. EU8 countries should also phase in—in tandem with development of capacity for screening needed labor—a more liberal regime for importing labor from countries further east. In the fiscal sphere, governments need to make room for additional spending on wages in sectors where public workers are becoming in short supply (notably the health sector) and investment where private labor is becoming more expensive (notably construction). Governments may also need to rely more on user fees, and in the education sector, greater reliance should be placed on private financing where returns are mostly private, including tertiary education but potentially also vocational education to the extent workers tend to seek employment abroad.



PREVIOUS SPECIAL TOPICS:

- Apr 2004: Public Expenditure Management Reform in EU8 Countries
- Jul 2004: Regional Policy in the EU8
- Oct 2004: Corporate Income Taxation and FDI in the EU8
- Jan 2005: The Baltic Growth Acceleration—Is It Sustainable?
- Apr 2005: Labor Taxes and Employment in the EU8
- Jul 2005: PPPs—Fiscal Risks and Institutions
- Jul 2005: Addendum: Lessons from EU Accession—One Year After
- Oct 2005: Sustainability of Pension Systems in the EU8
- Feb 2006: Growth in Central Europe and the Baltic States
- May 2006: Public Finances, Employment and Growth in the EU8

EXTERNAL ENVIRONMENT

The external environment for the EU8 countries has remained broadly favorable so far in 2006, despite higher oil prices and global interest rates. Growth gained further strength in the eurozone in the second quarter of the year, remained strong in Russia and Ukraine, but appeared to slow somewhat in the U.S. The turbulence in international financial markets in May-June, that saw a sharp correction in emerging markets, was short-lived and most markets had fully recovered by the end of August.

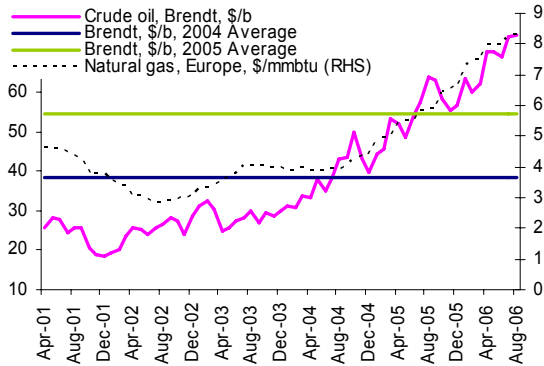
Oil prices have continued their strong upward trend in 2006, but remain highly volatile and the outlook subject to considerable uncertainty. Oil prices reached a peak of 78 US\$/barrel in early August, but have since then fallen back to around US\$65 (Chart 1). Current futures prices suggest that oil prices are expected to be around 73 US\$/barrel in the second half of 2006. Some market analysts have recently predicted that prices could reach 100 US\$/barrel in the near term, while others have suggested that they were more likely to gradually ease to 30-40 US\$/barrel.

The global economy has so far weathered the surge in oil prices well. In the eurozone, growth accelerated to a robust pace of 0.9 percent (qoq) in the second quarter of 2006, including not least because of a continued recovery in domestic demand in Germany, despite a series of interest rate hikes by the ECB (Chart 2, Chart 3). Meanwhile, growth remained strong in Russia and Ukraine. On the other hand, growth appeared to slow markedly in the U.S. during the course of the first half of 2006, on the background of continued monetary tightening and a weakening housing market.

However, growth in the major industrial markets looks set to slow in the period ahead. Interest rates are expected to continue moving higher in the eurozone, and leading indicators point to some slow down in the coming 6-18 months (Chart 4). There is more uncertainty about prospects in the U.S., including whether the Fed's decision to keep interest rates unchanged in August marked the ending of the tightening cycle and whether the housing market is heading for a soft landing or a crash. Markets and leading indicators suggest that growth is likely to remain sluggish in the coming quarters. The latest forecasts from international institutions point to a slight slowdown in the key markets and global economy in 2007, but there are significant downside risks related in particular to oil prices, the U.S. housing market, and the persistent large global macroeconomic imbalances.

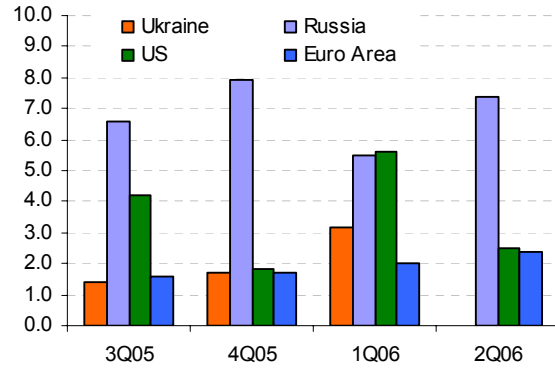
The turbulence in international financial markets in May-June was short-lived but revealed significant vulnerabilities in emerging markets with weak fundamentals. Fears that inflationary pressures had been underestimated and that global interest rates would need to rise significantly led to a sharp correction in global and not least emerging markets in May-June, with emerging market bond spreads widening by more than 50 basis-points, stock market indices falling sharply, and several currencies coming under significant pressure (Chart 5, Chart 6). However, most markets recovered fully during July-August, although assets in emerging market economies with weaker fundamentals such as Turkey and Hungary remained lower priced than in April.

Chart 1. Commodity prices



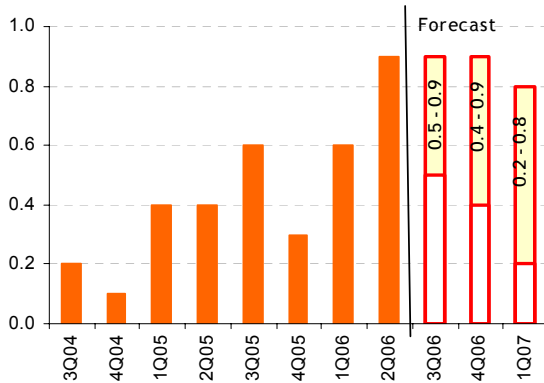
Source: GEM World Bank; Reuters.

Chart 2. Real GDP growth in key markets, % yoy



Source: CSOs, ISI.

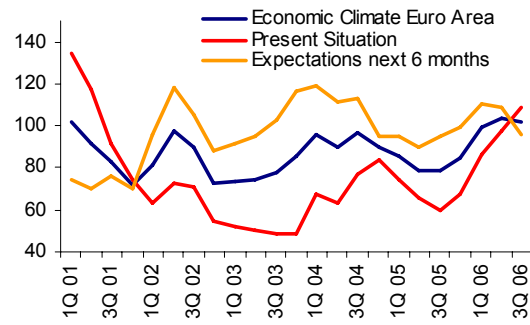
Chart 3. Euro area GDP growth, % qoq



Source: Eurostat; EC DG EFA.

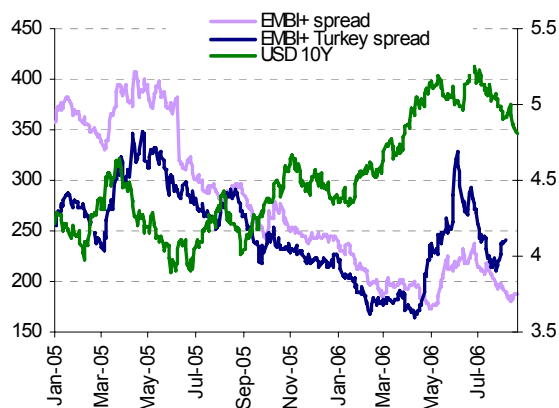
Note: Confidence level for forecast: 68 percent.

Chart 4. IFO economic climate of the euro area indicator



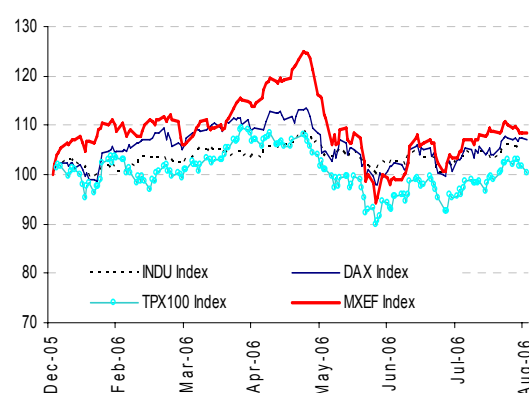
Source: IFO Institute.

Chart 5. Emerging market bond spreads and 10-year bond yield in the U.S.



Source: GEM World Bank; Bloomberg.

Chart 6. Global equity markets



Source: Bloomberg.

MSCI Emerging Markets Index, TPX- Tokyo Stock Price Index, INDU- Dow Jones Equity Markets, DAX- Germany Stock Price Index

POLITICAL BACKGROUND

Recent elections in the Visegrad countries have revealed a high degree of fragmentation which has forced parties to make fragile alliances and allowed populist forces to gain influence. This is hampering progress on the outstanding reform agenda, complicating the required fiscal and macroeconomic stabilization, and delaying euro adoption.

Recent months have seen several important changes in the regional political landscape (Table 1). In July, work was started under the new government of Robert Fico in Slovakia, a new minority coalition government led by Gediminas Kirkilas took office in Lithuania, Jaroslaw Kaczynski took over as Prime Minister in Poland, and in the Czech Republic Parliamentary elections in June resulted in a three months political stalemate.

Table 1. Political timetable

	Changes in last 12 months		Forthcoming elections	
CZECH REPUBLIC	parliamentary elections	Jun 2006	Senate and local elections	Oct 2006
ESTONIA	local elections	Oct 2005	presidential election	Sep 2006
HUNGARY	parliamentary elections	Apr 2006	local elections	Oct 2006
LATVIA	changes within government	Apr 2006	parliamentary	Oct 2006
LITHUANIA	changes within government	Jul 2006	local elections	Feb 2007
POLAND	changes within government	Jul 2006	local elections	Nov 2006
SLOVAKIA	parliamentary elections	Jun 2006	local elections	Sep 2007
SLOVENIA			local elections	Oct 2006

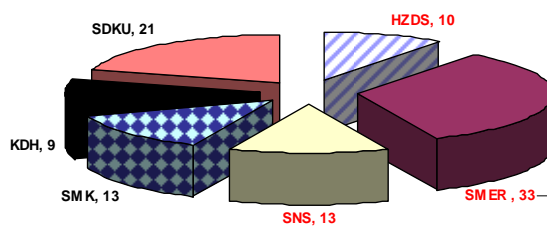
Source: ISI; EIU.

- In Slovakia, Parliamentary elections in June led to the formation of a new majority government headed by Fico's SMER and including the Slovak National Party (SNS) and HZDS (Chart 7). The new government's program was approved by Parliament in early August. The program aims to reduce the VAT rate in 2007 on drugs, increase social benefits while raising taxes on "above-standard" incomes (€15,000/year), make the second pension pillar voluntary, reform the Labor Code to make it more employee-friendly, increase subsidies to farmers, partially compensate 300,000 people who in the

past lost money in pyramid saving schemes, and subsidize mortgage interest rates. To accommodate new expenditures, the new government wants to cut existing budgets (including Ministry of Education) by 5-10 percent. The government has confirmed its commitment to the inherited 2009 euro adoption target.

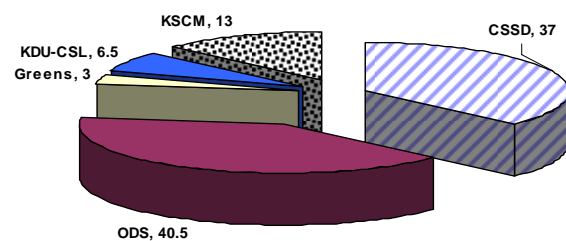
- Czech politics has been locked in stalemate for more than three months after the elections in June, with the left-wing and right-wing political forces each having control of 100 seats in the 200-seat Chamber of Deputies (Chart 8). On September 4, after three unsuccessful attempts to establish a new government, the winning Civic Democratic Party (ODS) formed a single-party minority government, with its Chairman Mirek Topolánek as Prime minister. A vote of confidence is scheduled for early October, but with the CSSD categorically ruling out support, this will hinge on the smaller parties, including the Communists. The ODS has rejected earlier CSSD plans to join the ERM-2 in 2007 with a view to adopting the euro in 2010, and the fiscal deficit looks set to widen further next year.

Chart 7. Parliamentary election results in Slovakia (share of seats in parliament, %)



Source: EIU; ISI; staff calculations.

Chart 8. Parliamentary election results in the Czech Republic (share of seats in parliament, %)



Source: EIU; ISI; staff calculations.

- In Hungary, the alliance between the ruling Hungarian Socialist Party (MSZP) and the Hungarian Liberal Party (SZDSZ) was renewed on June 1, following the April 2006 parliamentary election. Now, the coalition has a much more stable majority in parliament (54 percent of the votes) than it did in 2002-06. On June 10, Prime Minister Ferenc Gyurcsány announced a package of fiscal austerity measures aimed at a sustainable reduction of Hungary's runaway fiscal deficit. The "New Equilibrium" program calls for a series of tax increases and limited spending cuts in the short term, to be followed by more comprehensive reform of the public sector over the next few years. However, the spending reforms remain vague, and there are serious doubts about the government's ability to reduce the fiscal deficit to 3 percent of GDP by 2009-10 as planned. The government has dropped any euro adoption target date. The MSZP's popularity has fallen sharply following the announcement of austerity measures, and, most recently, following the leakage of a party speech by Mr. Gyurcsány in which he admitted to having lied and misled people in order to get re-elected.
- In Poland, Jarosław Kaczyński (chairman of PiS) replaced Kazimierz Marcinkiewicz as Prime Minister on July 10. Deputy Prime Minister and Finance Minister Zyta Gilowska was forced to resign in mid-June as an investigation of her alleged collaboration with the Communist Intelligence Service was initiated. After being acquitted, she resumed her duties on September 22 (following two interim Finance Ministers: first Paweł Wojciechowski and later Stanisław Kluza). Tensions between the three coalition parties mounted during the preparation of the 2007 budget, with coalition partners demanding

higher social payments and higher public sector salaries. This culminated with the dismissal of the Deputy PM and Self-Defence leader Andrzej Lepper on September 22. The possible scenarios, starting from the most probable, include a new coalition formed by PiS, LPR and the Polish Peasants Party (PSL) as well as potential defects from Self-Defense (needed to establish a majority); early elections - possibly already in November; or a minority government.

- In Lithuania, a three-month political crisis was ended in July with the formation of a four-party coalition minority government consisting of the Social Democratic Party (LSP), the Peasant Nationalists (LVL), the Liberal and Centre Union (LCS) and Civic Democracy. The government, led by Gediminas Kirkilas of the LSP, commands only 53 of the 141 seats in the Seimas (parliament), but is supported by the conservative opposition Homeland Union (TS) with 26 seats. The political situation remains fragile given the long-standing tensions between the TS and the LSP.
- In Latvia, parliamentary elections will take place on October 7. Following New Era's withdrawal from the government in April, the minority centre-right coalition has relied on support from either the nationalist For Fatherland and Freedom-Latvian National Independence Movement (TB-LNNK) or the left-wing Harmony Centre. The appointment in July of the popular mayor of Ventspils, Aivars Lembergs, as Prime Minister candidate for the Greens and Farmers (ZZS) has thrown the political battle wide open.
- In Estonia, the three-party coalition government (consisting of the liberal Reform Party, the left-leaning Centre Party and the centre-left Estonian People's Union) has a limited agenda so that policy differences between the three parties are unlikely to threaten the government's unity ahead of the March 2007 parliamentary election. However, there have been some tensions between the Reform Party and the Centre Party ahead of the two-step presidential election in August-September 2006. Meanwhile, the Centre Party and the People's Union are standing together.
- In Slovenia, the centre-right Slovenian Democratic Party (SDS) led majority coalition has faced widespread opposition to its economic and social reform proposals, and should the main opposition party, the centre-left Liberal Democracy of Slovenia (LDS), do well in the local elections in late 2006, this could open up the field ahead of general elections in late 2008.

MACROECONOMIC DEVELOPMENTS AND PROSPECTS

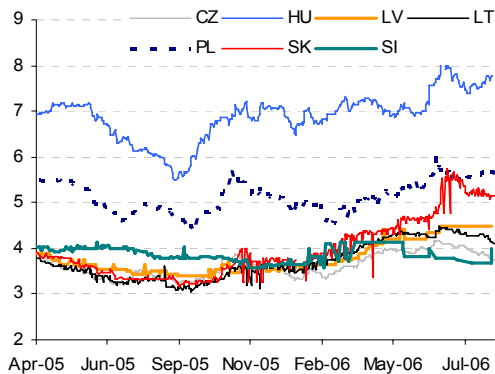
The strong growth momentum and broadening recovery in domestic demand have allowed the EU8 economies to weather the negative effects of high oil prices and recent turbulence in global financial markets. While unemployment continues to decline, wage pressures are mounting and with volatile financial markets and risks of further increases in oil and other commodity prices (including food) monetary authorities need to remain vigilant. The New Member States have not taken adequate advantage of the benign growth conditions to tighten the fiscal stance and advance major structural reforms. Fiscal balances are worsening in several of the countries in 2006 and budget plans for 2007 point to further laxity (except notably in Hungary where there is no alternative to strong consolidation efforts).

Market developments

The emerging market sell-off in May-June affected mostly Hungary, but Slovakia also felt the pain. The sell-off affected mainly equity markets in the region, which declined by about 20 percent in May-June (Chart 9). In Hungary, markets reacted with disappointment to the announcement on June 10 of the government's "New Equilibrium" fiscal adjustment package, with the forint weakening by 8.5 percent against the euro and yields on 10-year government bonds increasing by 110 bps in June (Chart 9). In Slovakia, the koruna weakened slightly ahead of elections in June but downward pressures increased following the announcement of the new

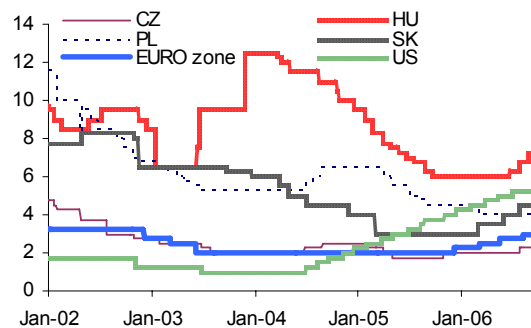
coalition SMER-SNS-HZDS and the koruna fell below its central parity of 38.455 SKK/€ and provoked significant foreign exchange intervention by the NBS - the first time since accession to the ERM-2 (ANNEX1: Chart 45). Subsequently, the declaration by PM Fico that the new government was committed to the 2009 euro adoption target helped to calm markets, and Hungary's new Convergence Program announced in August has so far been given the benefit of doubt. By the end of August, regional equity markets had recovered most of their losses, in yet another episode of asset market overshooting.

Chart 9. Government bond yields (10Y)



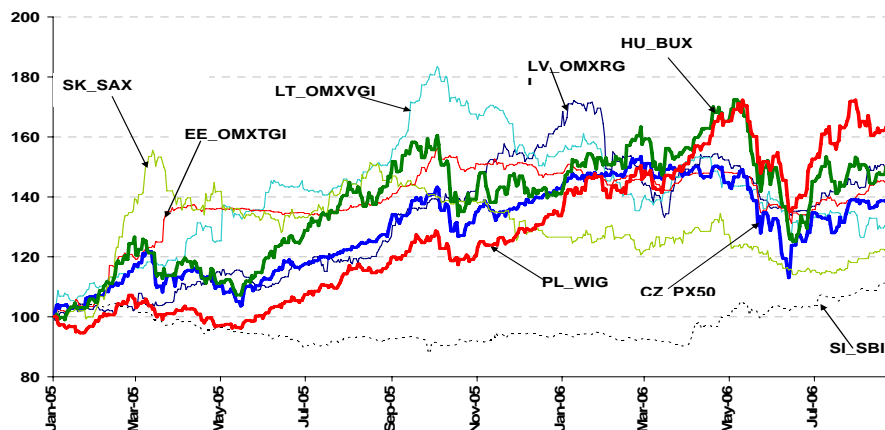
Source: Reuters.

Chart 10. Policy rates in the U.S., Eurozone and Visegrad countries



Source: CBs.

Chart 11. Stock exchange indices, January 2005=100



Source: Reuters.

Hungary remains the most vulnerable among the EU8 countries to external shocks. This reflects the persistently large macroeconomic imbalances and rising public and external debt ratios. The current account deficit remains above 7 percent of GDP, while the general government deficit is likely to exceed 10 percent of GDP this year. Non-debt financing of the current account deficit has declined in 2006 due to a sharp fall of both equity capital inflows and reinvested earnings. As a result, gross foreign debt increased 87 percent of GDP in the first quarter of the year, compared to 78 percent of GDP by end-2005 (Table 2). Public debt is projected to reach about 67 percent of GDP by end-2006.

Table 2 Selected vulnerability indicators in the EU8, Q1-2006

	CZ	EE	HU	LT	LV	PL	SK	SI
GDP growth, SNA (real, %, yoy)	7.1	11.6	4.6	8.8	13.1	5.2	6.3	5.1
Current account balance, (4Q cumulative, % of GDP)	-2.6	-12.0	-7.4	-8.1	-13.3	-1.5	-9.8	-1.1
FDI (4Q cumulative, % of GDP)	6.9	12.4	6.0	2.4	4.0	2.5	4.6	0.2
Total gross external debt (eop, % of GDP)	35.7	95.3	86.9	53.2	101.3	43.2	59.1	73.6
Change of international reserves in euro (eop, relative to previous period, %)	-1.9	-5.3	13.4	2.8	11.1	1.6	14.4	0.4
Reserves-to-short-term debt ratio (eop, %)	242.4	38.6	193.0	76.4	34.7	175.8	159.5	180.0
Money Supply-to-Reserves ratio (eop, %)	264.7	352.9	251.2	262.2	268.1	290.3	151.4	260.9
Overall balance of state budget (4Q cumulative, % of GDP)	-1.6	-1.7	-3.9	-0.2	1.2	-2.5	-2.4	-1.3
Credit to private sector (eop, % of GDP)	37.0	76.8	52.3	44.0	71.6	29.2	36.3	58.2
Growth rate of credit to the private sector (avg, %)	18.2	40.5	18.1	68.6	64.7	9.7	22.1	30.2
Foreign currency loans to the private sector (eop, % of loans to priv. sect.)	9.9	80.3	48.5	64.2	70.7	27.0	21.0	47.3
Non-performing loans at the end of 2004 (eop, % of total loans)	4.1	0.3	3.7	2.4	1.1	14.2	7.2	7.5
Short-term (3M) interest rates spreads to euro area (avg, basis points)	-53.0	9.0	341.0	3.0	140.0	168.0	81.0	118.0
Change of stock exchange index (avg, relative to previous period, %)	8.7	-2.9	6.8	-10.6	3.2	15.0	-6.1	0.1
Long term foreign currency sovereign credit rating according to S&P's	A- (↔) (P)	A (↔) (P)	A- (↔) (N↓)	A (↔) (P)	A- (↔) (S)	BBB+ (↔) (P)	A (↔) (S)	A+ (↔) (P↑)

Notes: The symbols in the line with S&P ratings denote the outlook, while S=stable, P=positive, N=negative.

Pressures on the Baltic countries in May-June were limited despite significant vulnerability related to their weak external positions. Financial market pressures in a currency board would show up in lower reserves and monetary base and higher money market interest rates, but no such tendencies were visible during the emerging market pressures in May-June (Box 1).

Box 1. Financial market pressure under currency board regimes

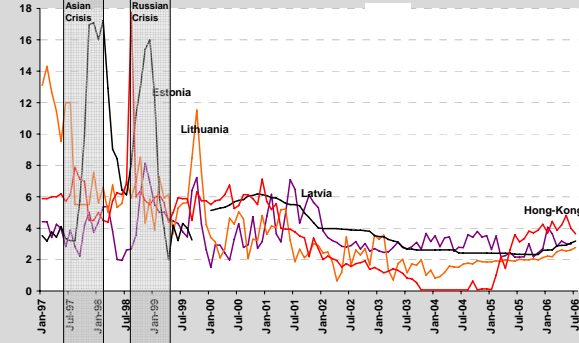
Under currency board system, the exchange rate is fixed and the monetary base fully covered by international reserves (with changes exclusively reflecting changes in the central bank's net foreign assets, which in turn is determined by the overall balance of payments). In case of an abrupt capital outflow, liquidity will be squeezed and money market rates rise (the central bank cannot act as a lender of last resort).¹

There are several cases of financial market pressure on currency boards (Chart 12, Chart 13, Chart 14). In some episodes, countries managed without major problems (Argentina during the tequila crisis in 1995, Hong-Kong during the Asian Crisis in 1997-98 and the Baltic States during the *Russian Crisis* in 1998), while there is also a case of the currency board system collapse (Argentina in 2001-2002).

In contrast to the Russian crisis in the late 1990s, there were no spillovers to the Baltic countries from the weakening sentiment in emerging markets in May-June this year. International reserves and monetary bases continued rising, while slightly higher money market rates resulted from interest rate hikes by the ECB. Hence, the equity market was the only financial market segment where the bearish global attitude was visible.

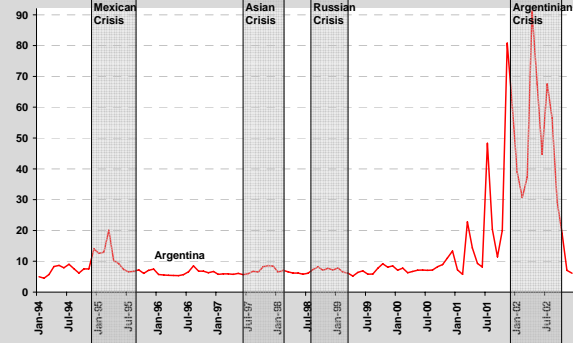
¹ Commercial banks operating in the Baltic States are mostly owned by foreigners, and in the event of liquidity problems can seek recourse to their owners. In the Baltic countries, which have very small stocks of public debt, monitoring of bond yields does not convey much information.

Chart 12 Money market interest rates, %
Baltic States and Hong-Kong (Jan 1997 - Jul 2006)



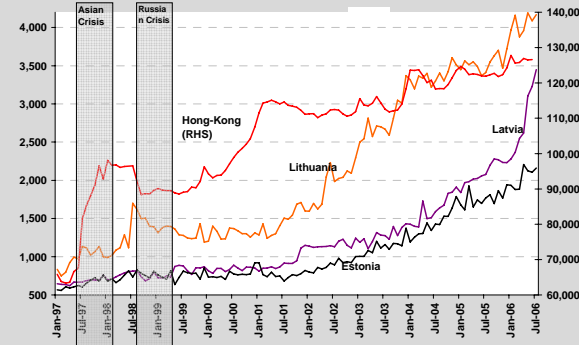
Source: IFS online.

Argentina (Jan 1994 - Dec 2002)



Source: IFS online

Chart 13. Foreign currency reserves, US\$ million
Baltic States and Hong-Kong (Jan 1997 - Jul 2006)



Source: IFS online.

Argentina (Jan 1994 - Dec 2002)

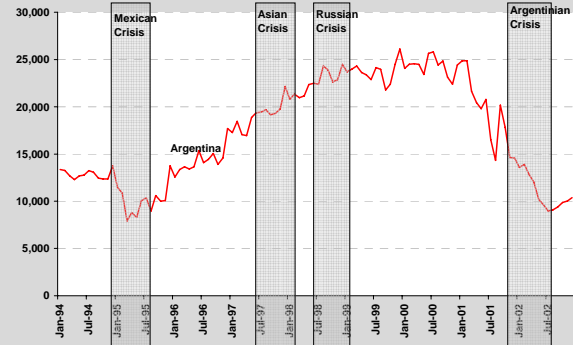
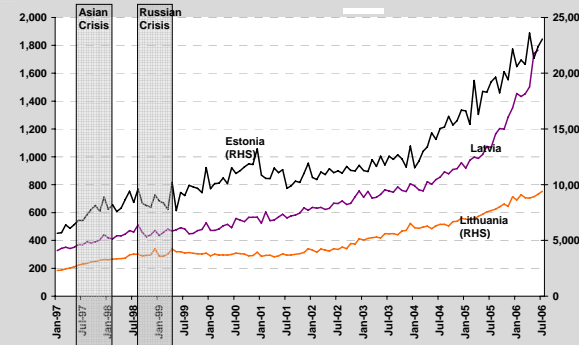
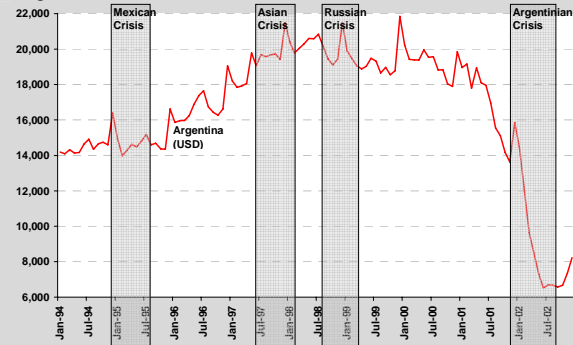


Chart 14. Monetary base (M0), national currency (million)
Baltic States (Jan 1997 - Jul 2006)



Source: IFS online.

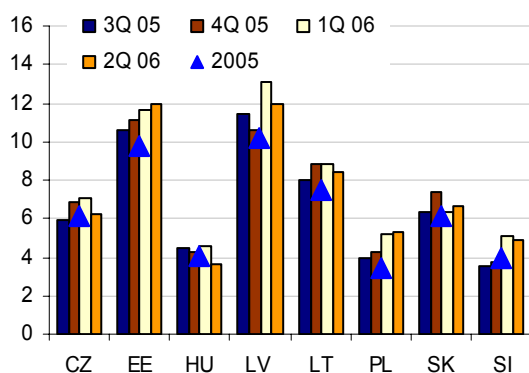
Argentina (Jan 1994 - Dec 2002), in US\$ millions



Output developments

Output growth in the region continues to be buoyant. Growth continues to surprise on the up-side in the Baltic countries, although with clear signs of overheating. Output growth gained further strength in the Czech Republic, Poland, Slovakia and Slovenia, but eased somewhat in Hungary (Chart 15).

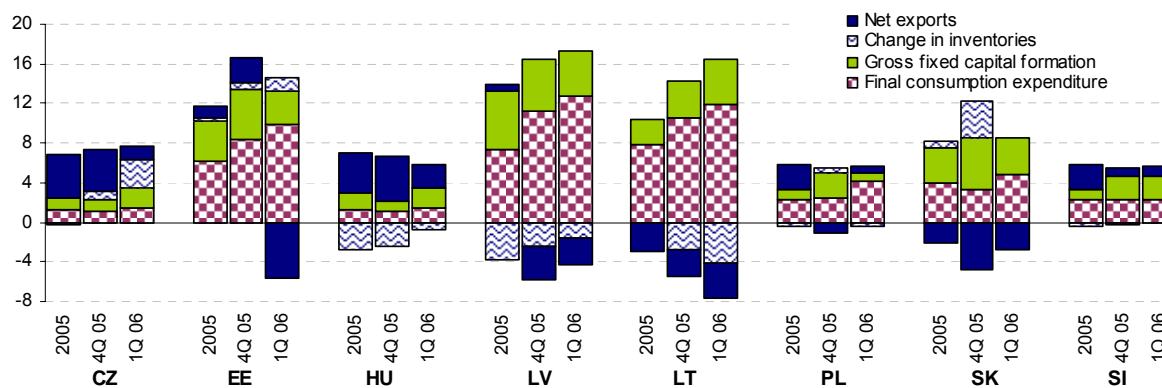
Chart 15. Real GDP growth rate, % yoy



Source: CSOs.

Output growth is increasingly led by domestic demand. In the Visegrad countries and Slovenia, domestic demand started to lead growth in the first quarter of 2006 while the contribution of foreign trade to overall growth declined (Chart 16). As a result, growth has become more balanced in these countries. Meanwhile, domestic demand—especially private consumption—continued to drive growth in the Baltic countries. In 2006, both consumption (supported by rising wages, employment and credit) and gross fixed capital formation have accelerated sharply. In particular, consumption spending rebounded strongly in the Baltic countries and Slovakia, but also in Poland. The recovery in investment, which was particularly noteworthy and welcome in Poland,³ reflected a combination of good demand prospects, high profits in the corporate sector and stepped-up infrastructure investment (Hungary and Slovakia) and housing construction (Baltic countries).

Chart 16. Contributions to GDP growth, % points of GDP

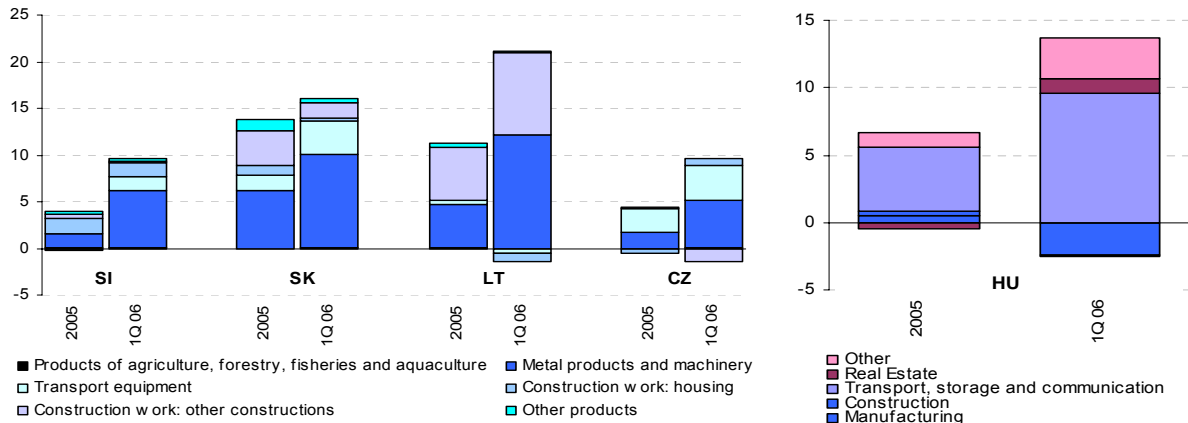


Source: CSOs; staff calculations.

Investment in equipment was particularly dynamic (Chart 17). In contrast, capital formation in construction was weaker, although likely in part a seasonal phenomenon.

³ In Poland, investment growth accelerated to 14.4 percent yoy in Q2-2006 (a multi-year high).

Chart 17. Contributions to gross fixed capital formation, %

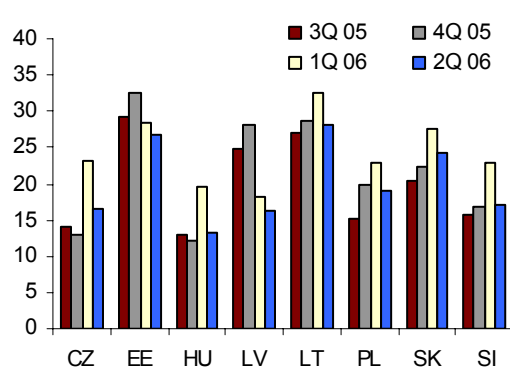


Source: Eurostat.

Source: CSOs.

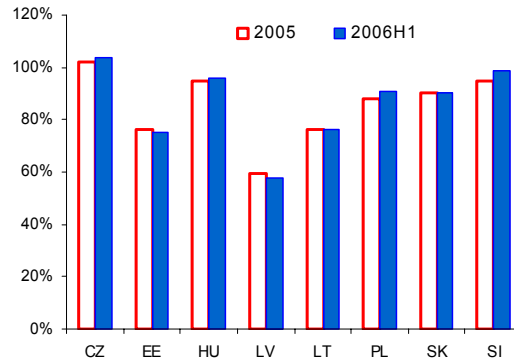
At the same time, export performance continues to impress (Chart 18, Chart 19). Exports from most of the EU8 countries are continuing to expand at 15-20 percent yoy on the background of stronger growth in major export markets and sustained cost competitiveness (Chart 33).

Chart 18. Export of goods (€), % yoy



Source: Eurostat.

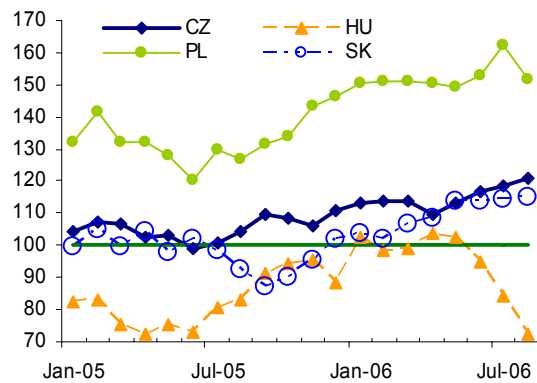
Chart 19. Export/import, %



Source: Eurostat; staff calculations.

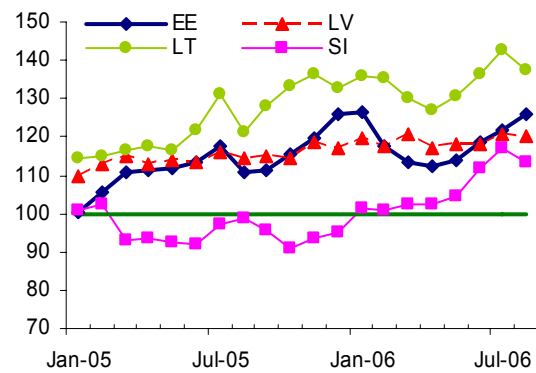
Growth is likely to remain brisk in the remainder of 2006, but may slow moderately next year. The Economic Sentiment Indicators paint an upbeat picture, with the exception of Hungary (Chart 20). The increase in the sentiment indicators for the EU8 can be explained mainly by improved confidence in the industry and construction sectors (ANNEX1: Table 9) while consumer sentiment is broadly stable.

Chart 20. Economic Sentiment Indicator



Source: EC.

Chart 21. Economic Sentiment Indicator



Source: EC.

The expected moderation of growth in 2007 reflects some slowdown in the eurozone, while some likely cooling of demand in the Baltic states and the impact of fiscal tightening in Hungary would slow growth in these countries. The most pronounced slowdown is expected in Hungary, where domestic demand is likely to decelerate in the second half of 2006 and in 2007 on the back of tax increases, higher interest rates, and a rise in inflation (Table 3). Growth is likely to slow to 2-3 percent in 2007 as the fiscal measures take full effect. Growth in the Czech economy is expected to slow slightly to around 6 percent next year, mainly as a result of de-stocking and a moderation in export growth from the current rapid pace. Meanwhile, growth should remain broadly stable in Poland and Slovenia, but gain further speed in Slovakia with the coming on stream of new exports from the automotive industry.

Table 3. Macroeconomic outlook

	Output growth (real GDP), % yoy			Inflation (CPI average)			Current account, % GDP			Fiscal balance (GG), % GDP*		
	2005	2006E	2007F	2005	2006E	2007F	2005	2006E	2007F	2005	2006E	2007F
Czech Republic	6.1	6.8	6.0	1.9	2.8	3.0	-2.1	-3.0	-3.1	-2.6	-3.3	-3.8
Estonia	9.8	9.2	8.0	4.1	4.5	3.8	-11	-11.8	-11.2	1.6	1.4	0.7
Hungary	4.1	3.8	2.5	3.6	3.7	6.5	-7.4	-8.0	-6.7	-6.1	-8.6	-5.1
Latvia	10.2	9.8	7.5	6.7	6.5	5.2	-12.4	-13.5	-12.0	0.2	-1.5	-1.2
Lithuania	7.5	7.0	6.5	2.7	3.4	3.1	-7	-8.5	-8.4	0	-0.5	-0.3
Poland	3.4	5.0	5.1	2.1	1.1	1.9	-1.4	-1.7	-2.4	-2.5	-2.4	-2.3
Slovakia	6.1	6.7	7.1	2.7	4.5	2.8	-8.6	-7.2	-4.2	-2.9	-2.2	-1.9
Slovenia	3.9	4.2	4.0	2.5	2.5	2.3	-1.1	-2	-2.1	-1.8	-1.8	-1.8

*) excluding pension reform costs.

Source: CSOs; WB estimates. Differences between WB estimates and official forecasts marked as follows:

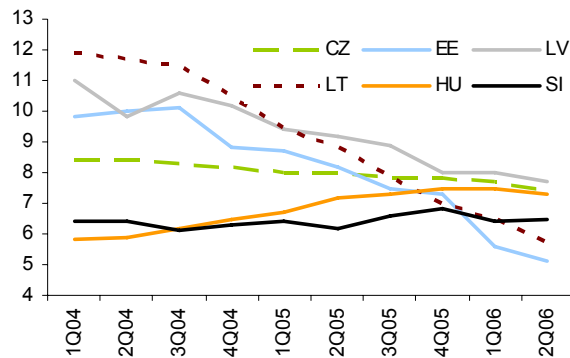
positive
negative

CZ: MOF (July); HU: Convergence Program (August); EE: MoF (Aug); PL: MOF (Sept.); SK: WB (fiscal in line with MOF); SI: WB, IMF, CB.; LV, LT: WB projections

Labor markets

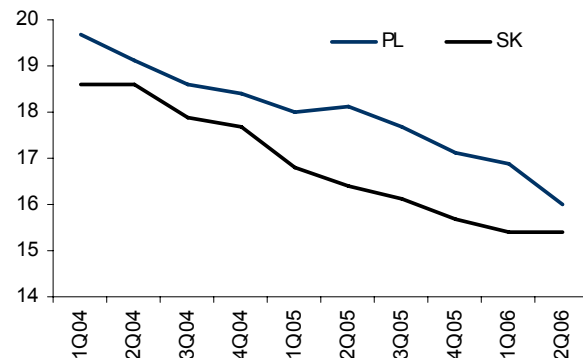
Most EU8 labor markets are responding to recent rapid growth rates with lower unemployment and strong or emerging wage pressures. In the Baltic States, labor markets are tightening with labor shortages emerging in several sectors. Since end-2005, the unemployment rate has fallen significantly in Estonia and Lithuania, to around 5 percent in Q2-2006, while it is falling at a more measured pace in Latvia (Chart 22). In Poland and Slovakia, high unemployment rates are coming down steadily, reaching around 16 percent and 15 percent, respectively (Chart 23). On the other hand, unemployment rates are stuck at moderately high levels in Slovenia, the Czech Republic and Hungary.

Chart 22. Harmonized unemployment rates in EU6, SA



Source: Eurostat

Chart 23 Harmonized unemployment rates in Poland and Slovakia, SA



Source: Eurostat

Recent improvements in labor market performance appear to be mainly cyclical in some countries but more of a structural nature in others. In Poland and in Slovakia, the decline in unemployment seems to be largely cyclical. Since 2004, Poland has been experiencing rapid growth and the employment rate has increased from 50.5 percent in Q1-04 to 53.4 percent in Q1-06. At the same time, the long-term unemployment rate (largely of a structural nature) increased (Box 2). On the other hand, long-term unemployment has trended down in the Baltic countries.

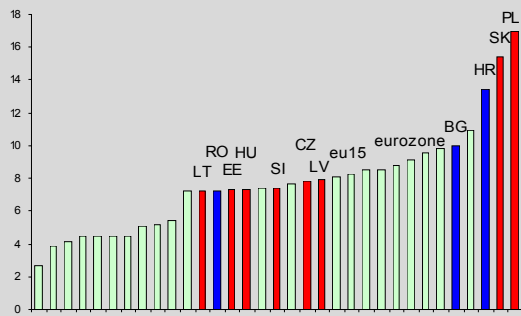
Box 2. Long term unemployment in the EU8

EU8 countries have a relatively high share of long-term unemployed (those being unemployed more than 12 months) among the unemployed (LTU). While the total unemployment rate in the EU8 is similar to the EU15 (9.3 percent and 8.3 percent, respectively, in Q1-2006 (Chart 24), LTU in the first group is as high as 53 percent while in the EU15 the rate is “only” 42 percent (Chart 25). LTU is especially high in Slovakia (87 percent), Poland (74 percent) and the Czech Republic (71 percent).

While a decline in LTU played a major role in the decline in average EU8 unemployment in 2002-2003 and also contributed positively to the decline since 2004 (Chart 26), only three countries managed to reduce LTU between 2001 and 2005: Latvia by 22 percent, Hungary by 6 percent and Slovenia by 23 percent (all to about one-half of total unemployment). In Lithuania, the Czech Republic and Estonia, LTU increased to the EU8 average. LTU increased the most in Poland and Slovakia - by 25 and 32 percent, respectively. The very high and steadily increasing long-term unemployment rate in Slovakia is worrisome.

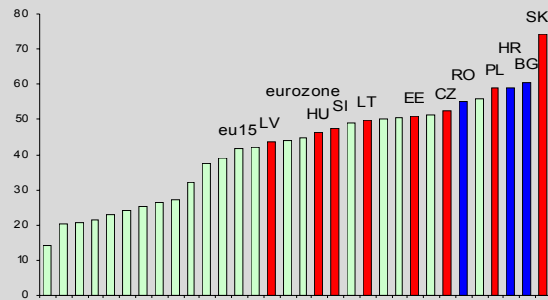
LTU seems to be associated more with low-skills, distant regions and poverty traps than labor market flexibility. Poland has one of the highest degree of labor market flexibility in the EU8 (see Table 8) and a relatively high ratio of part-time employment as well as one of the highest ratios of self-employment in Europe, but still has a high unemployment rate and share of LTU. On the other hand, Latvia has about average labor market flexibility and part-time employment in the region and one of the lowest rates of self-employment in the EU, but a relatively moderate share of long-term unemployed among the unemployed.

Chart 24. Unemployment rate in EU and CC, 15-64



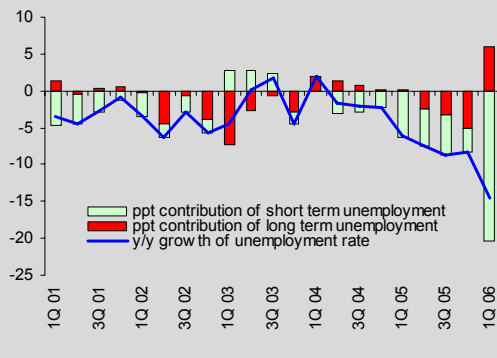
LFS data for EU and three candidate countries, 4q2005; EU15, Eurozone, CH and HR, 2q2005. Source: EUROSTAT.

Chart 25. Long-term unemployment in EU and CC, 25-64 (in percent of unemployment)



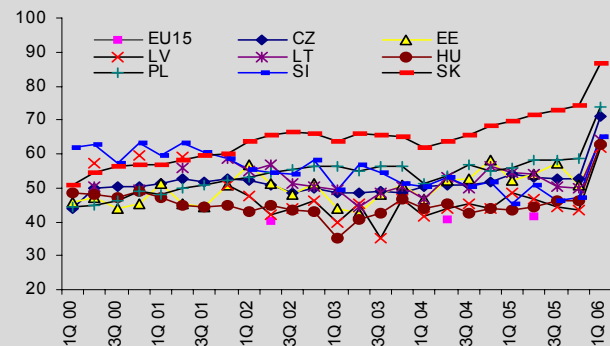
LFS data for EU and three candidate countries, 4q2005; EU15, Eurozone, SE, CH and HR, 2q2005. Duration of unemployment longer than 12 months. Source: EUROSTAT.

Chart 26. Unemployment rate in EU8 decomposed (yoy change)



LFS 1q2001-1q2006, age 15-64. Source: EUROSTAT and staff calculations.

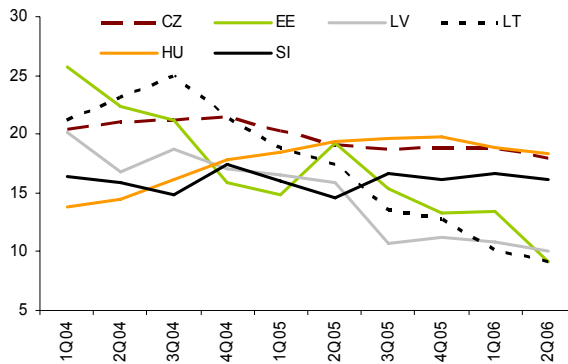
Chart 27. Long-term unemployment (in percent of unemployment)



LFS, 1q2001-1q2006, age 15-64. Source: EUROSTAT.

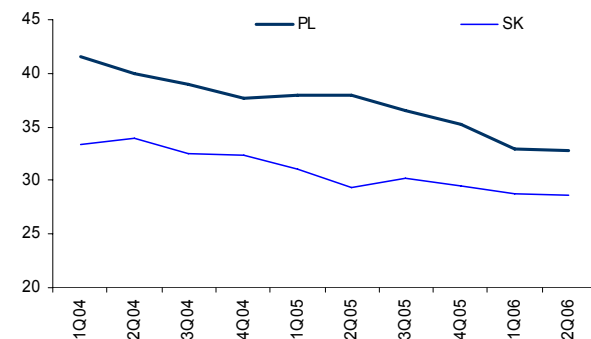
A large number of unemployed young people appear to have left the Baltic countries after EU accession. Youth unemployment (age 15-24) has declined significantly since 2004, matched by a corresponding decline in the activity rate of this age group (and thus unchanged employment rate) (Chart 28). This points to a sizeable outflow of young, unemployed people, as there is no reason to believe that they would otherwise have withdrawn from the labor force.

Chart 28. Harmonized unemployment rates in EU6, 15-24, SA



Source: Eurostat

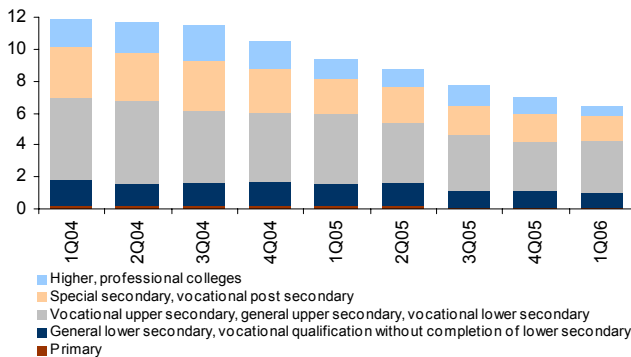
Chart 29. Harmonized unemployment rates in Poland and Slovakia, 15-24, SA



Source: Eurostat

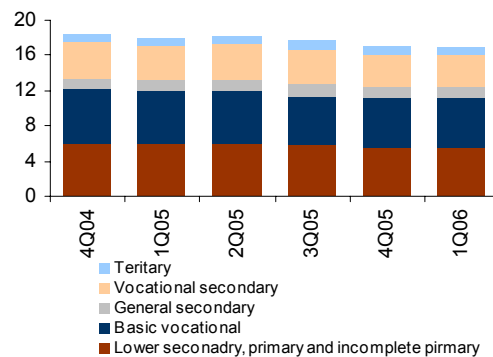
Meanwhile, bottlenecks (notably shortages of highly-skilled labor) are developing in several labor markets, mainly in the Baltic countries. In Lithuania and Estonia, unemployment declined most rapidly for people with special and vocational secondary education as well as tertiary education (Chart 30). In Poland, employment growth was divided more or less evenly across the various educational groups (Chart 31), but anecdotal evidence suggests the emergence of high-skill labor shortages in certain sectors like construction, medical care, transport services and IT services in Poland and the other Visegrad countries.

Chart 30. Unemployment rate by education in Lithuania



Source: Eurostat.

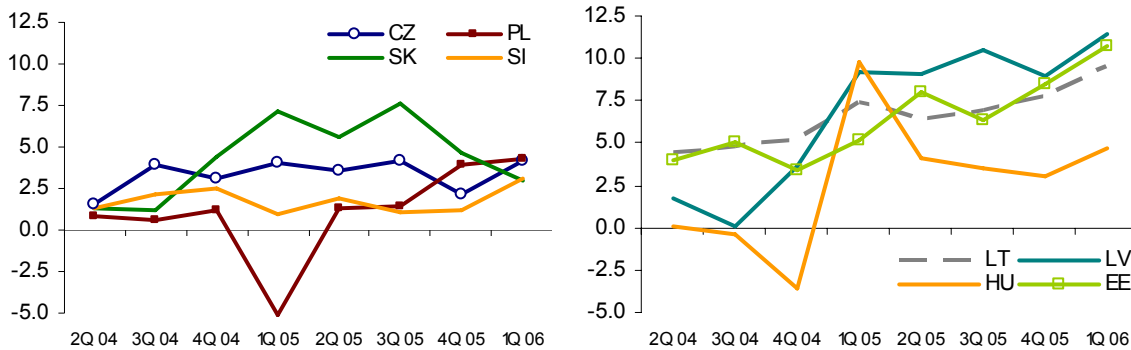
Chart 31. Unemployment rate by education in Poland



Source: Eurostat.

The decline in unemployment and emerging bottlenecks in several sectors has translated into accelerating wage growth in the Baltic countries. Employment gains, emigration flows, and excess labor demand in several sectors in the Baltic countries has led to accelerating wage growth in the economies (Chart 32). Meanwhile, in Poland, the Czech Republic, Hungary and Slovenia, wage growth has remained remarkably modest, and in Slovakia - where real wages rose strongly in 2004-2005 - wage growth has moderated. However, even in those countries where unemployment remains high, wages pressures have started to build-up in some sectors (e.g. construction, agriculture, and financial intermediation) reflecting rising demand for skilled labor, and may spill-over to the new wage settlements for 2007 (notably public-sector wages and pensions).

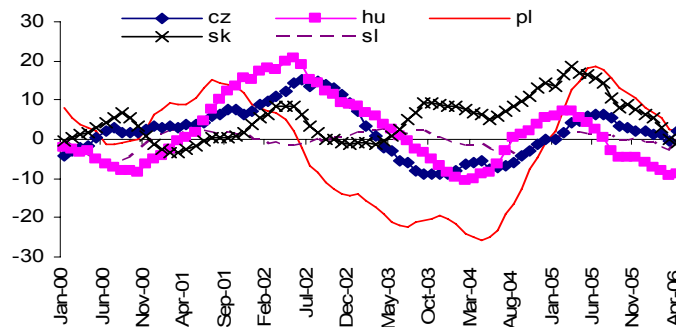
Chart 32. Real wage growth, % yoy



Source: CSOs; and staff calculations.

Moderate wage growth combined with strong productivity growth has offset appreciation of currencies in the Visegrad countries and Slovenia to preserve unit labor costs at highly competitive levels. The change in unit labor costs measured in euro in these countries have fluctuated around zero since 2000, and generally remain below one-half of the average level in Western Europe (Chart 33).⁴ Poland appears to have gained a considerable additional competitive advantage in the period 2002-04.

Chart 33. ULC in industry, €-adjusted, % yoy



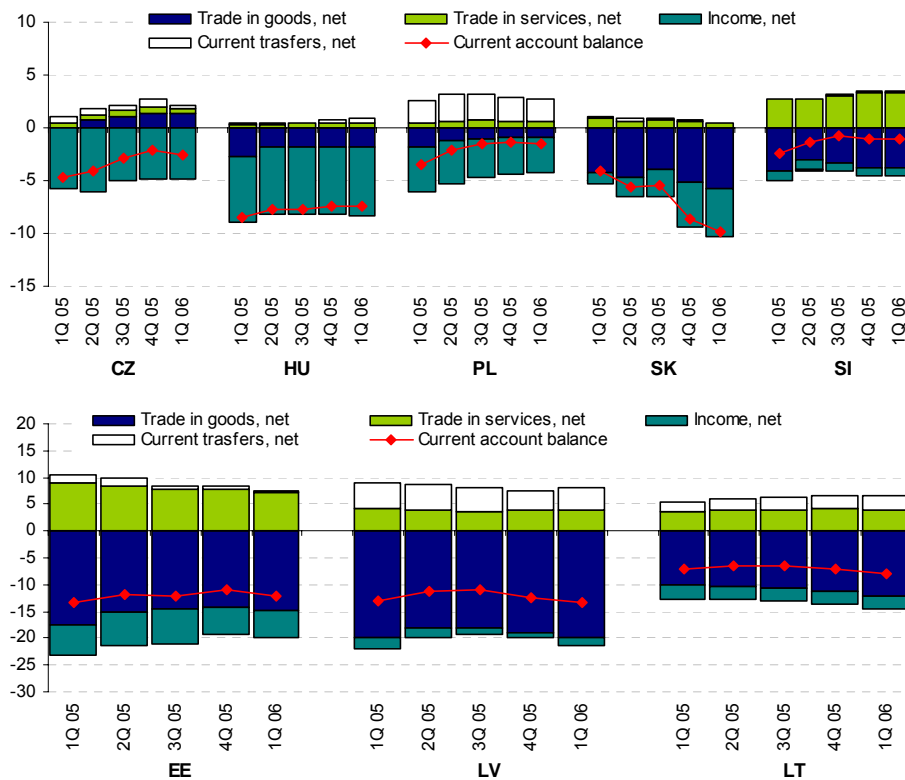
Source: WIIW; CSOs; staff calculations. 6-month rolling average.

Balance of payments and foreign trade

Current account positions have deteriorated further in the Baltic countries as well as in Slovakia. In the Baltic countries, current account deficits increased further in the first quarter of 2006, in Estonia and Latvia reaching 12-13 percent of GDP. In Slovakia, the deficit jumped to almost 10 percent of GDP. The deficits in these countries are mainly driven by trade in goods (Chart 34), with soaring imports related to strong domestic demand - in Slovakia in part related to large FDI projects. The deficit also remains high in Hungary at 7.4 percent of GDP, reflecting a large income deficit (which is also the largest drag on the current account in the Czech Republic, Poland and increasingly Slovakia). The largest factor is the repatriation of profits from direct investments and dividend payments. Meanwhile, external imbalances remain low in Poland, the Czech Republic, and Slovenia.

⁴ According to WIIW Research Report No. 328, July 2006.

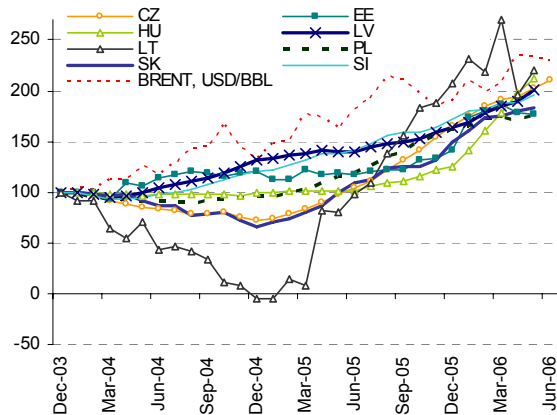
Chart 34. Current account balance and components, % of GDP



Source: NCBS; and staff calculations

Weaker current accounts also reflect the rise in oil prices. Given the large dependence of EU8 countries on imported energy, trade deficits in fuels have more or less doubled since early 2005 in tandem with rising oil prices (Chart 35). The deterioration in the fuel balance is particularly stark in Lithuania, which had eliminated its deficit by the end of 2004 but where this surged subsequently possibly reflecting supply problems to the domestic refinery.

Chart 35. Trade deficit in fuels (SITC 3) and Brent crude oil price, Dec2003=100



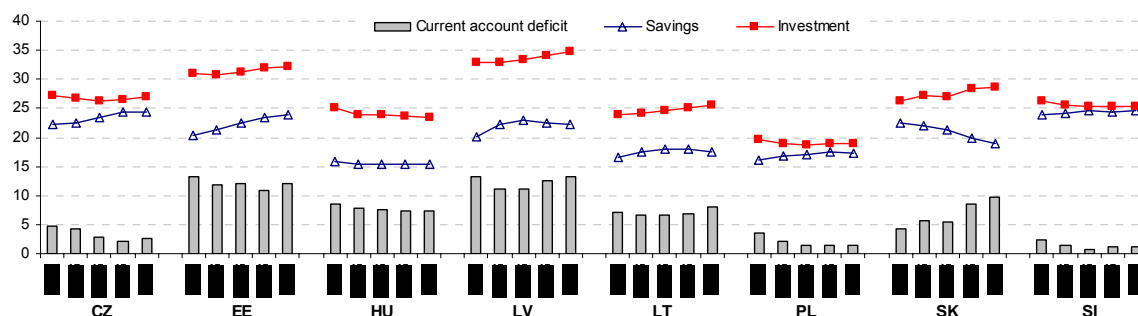
12M cumulative.

Source: Eurostat.

The largest external imbalances in the region - in the Baltic States and Slovakia - reflect increased investment rather than lower savings. Increased investment in Slovakia and the

Baltic States has not been accompanied by higher domestic savings (except in Estonia) which even declined markedly in Slovakia as a result of higher income outflows (Chart 36).

Chart 36. Savings-investment gap, % of GDP



4 quarters cumulative.

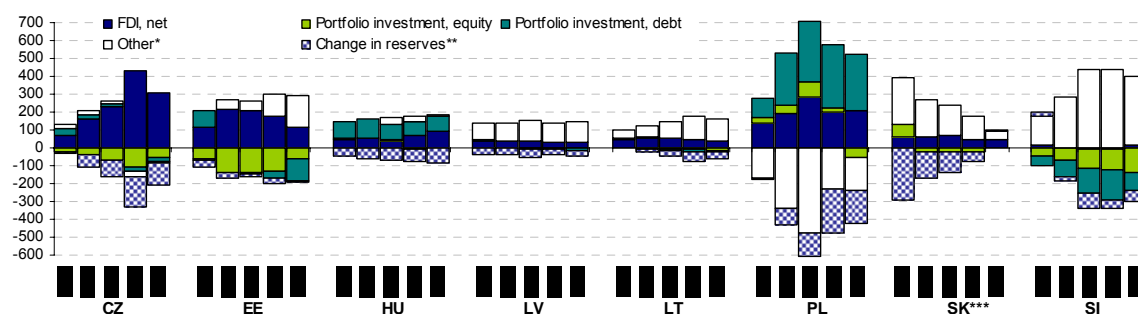
Savings are calculated as gross national domestic income less consumption.

Current account deficit reflects the gap between investment and saving in the economy ($S-I=CAB$). However, in some countries—notably Estonia—there were significant statistical discrepancies in this equation.

Source: NCBs; and staff calculations.

On the financing side, strong FDI flows covered the combined current and capital deficits in the Czech Republic, Estonia, Poland and to a large degree Hungary (Chart 37). In the other countries in the region, net FDI covered less than 50 percent of deficit - in Slovenia even as low as 14 percent. Debt portfolio investment was buoyant in Hungary and Poland, reflecting existing bond yield differentials, although these flows are likely to have weakened significantly in the second quarter in line with the deterioration in investor sentiment towards emerging markets and - in Hungary - an even worse than expected fiscal situation. In the Baltic States, foreign borrowing by banks plays an increasingly important role in financing the deficits. All EU8 countries, except Slovakia, increased reserves thus partly mitigating upward pressures on exchange rates but complicating liquidity control in the Baltic States. In Slovakia, reserves declined significantly in the second quarter as the central bank intervened heavily to defend the koruna.

Chart 37. Financing of current account and capital deficit, % of deficit



4 quarters cumulative.

*financial derivatives, other investment and net errors and omissions.

**negative values denote increase of reserves.

***portfolio investment includes equity and debt.

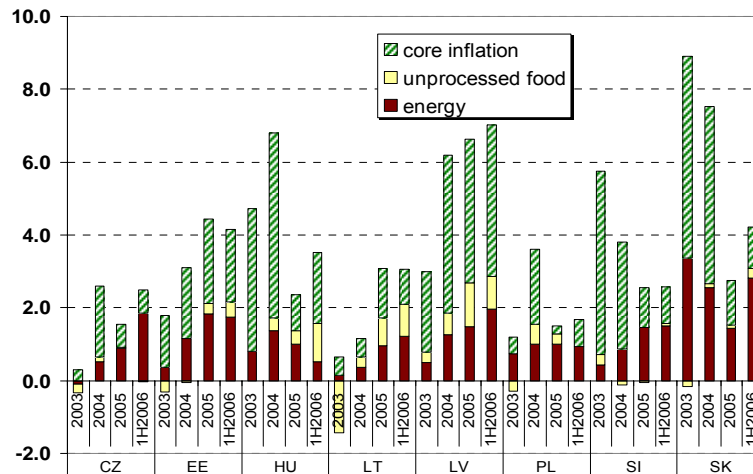
Source: NCBs; and staff calculations.

Inflation and monetary policy

Inflationary pressures are rising across the region. Consumer price inflation is rising in most EU8 countries, with supply-side factors—notably food and energy—playing an increasing role

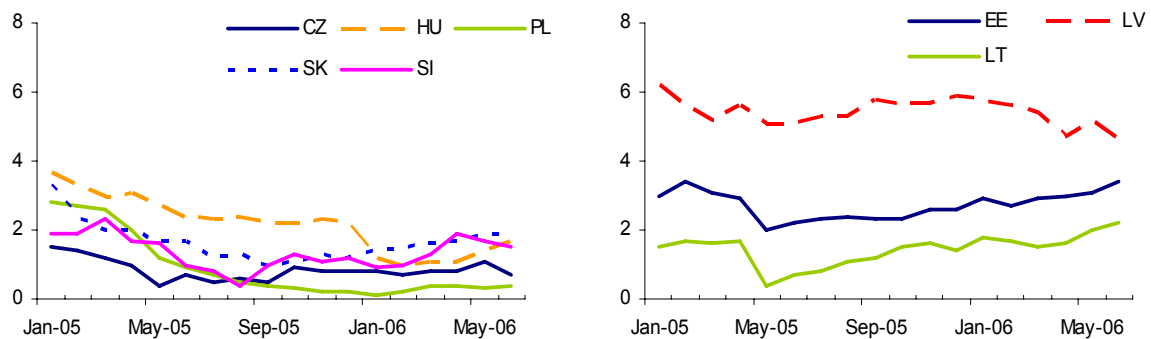
(Chart 38).⁵ A few countries—notably Hungary but also Estonia, Poland, and Slovenia, appear to be attempting to delay the impact of higher oil prices through freezing of excise taxes on fuels, but such a policy is not sustainable for long. Core inflation is picking up rapidly in Hungary, but also edging higher in Poland although from a very low level (Chart 39). PPI inflation is running well-ahead of CPI inflation in Hungary, Poland, Slovakia, Latvia, and Lithuania, and while there was undoubtedly some scope for squeezing high profit margins, it is likely that higher producer prices will eventually find their way through to consumers (ANNEX1: Chart 50). In Hungary and Poland, monetary conditions have eased recently—in the former, to a significant degree reflecting currency depreciation (ANNEX1: Chart 47, Chart 46).

Chart 38. Decomposition of average HICP changes in 2003-2006, % yoy



Source: Eurostat; and staff calculations.

Chart 39. Core inflation, overall HICP index excluding energy and unprocessed food, % y/y



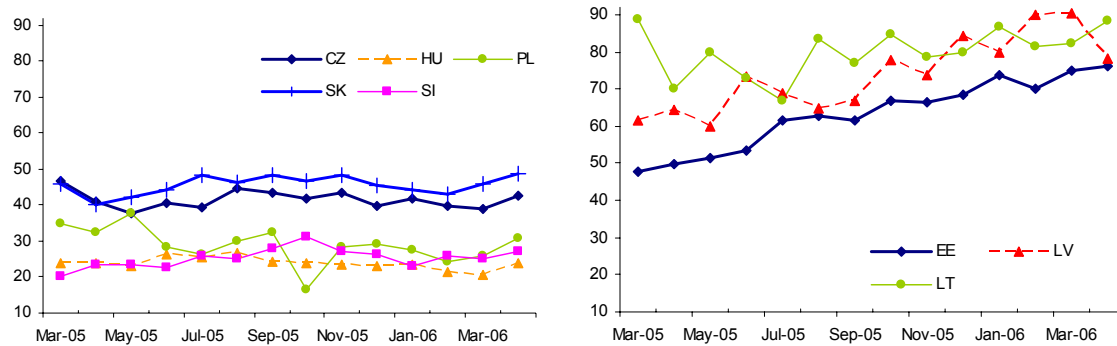
Source: Eurostat.

Rapid credit and—in the Baltic countries—wage growth are further fueling inflationary pressures. With the tightening of labor markets in the Baltic countries, real wage growth has accelerated and is now running at around 10 percent - likely well-ahead of productivity growth.

⁵ Supply factors (energy and food prices) explain around one half (or more) of average consumer price increases in 2006 (except in Latvia). Their share in the price baskets ranges from 20 percent in Slovenia to 25 percent in Slovakia.

Loans to households are growing at 20-30 percent in Slovenia, Hungary and Poland,⁶ 40-50 percent in Slovakia and the Czech Republic, and 70-90 percent in the Baltic States despite automatic interest rates hikes following the tightening stance of the ECB (Chart 40).

Chart 40. Bank credit to households, % yoy



Source: ECB; and staff calculations.

Consumer sentiment surveys and prices of financial market instruments also point to rising inflationary expectations. Consumers' inflation expectations (revealed in the monthly survey of business and consumer sentiment conducted by DG ECFIN) have risen recently even in countries with low inflation (Poland, the Czech Republic, and Slovenia). Rising inflation expectations are also present in generally steeper yield curves across the Visegrad countries.

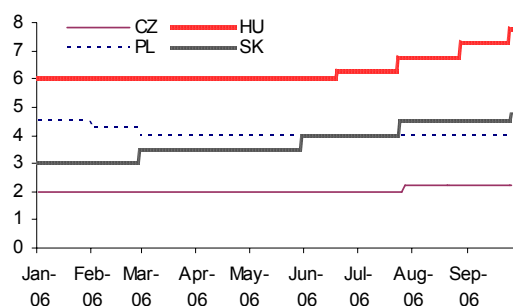
Inflationary pressures have delayed euro adoption plans in the Baltic countries, and could complicate the process in Slovakia. Lithuania's bid to join the eurozone from January 2007 was rejected in the spring, and Estonia unilaterally pushed back its target date to January 2008 (corresponding to Latvia's original target). While none of the Baltic countries have announced new formal targets, Latvia has indicated that 2010 was realistic and the other two Baltic countries are likely to follow suit.⁷ Slovakia remains committed to the 2009 target date, but problems in bringing inflation under control may add to the fiscal challenges in this regard. Poland, Hungary, and the Czech Republic have no firm target date.

In response to financial market pressures and/or rising inflation risks, central banks in the Visegrad countries (except Poland) have raised interest rates. Since June, the Hungarian, Slovak and Czech central banks have raised interest rates by 175, 75 and 25 basis points, respectively. (Chart 41). Further, as discussed above, the National Bank of Slovakia (NBS) intervened heavily between late May and mid-August to support the koruna (international reserves of the NBS declined by over US\$ 4 billions (from US\$ 17.3 billion to US\$ 13.1 billion) during this period). The Czech central bank (CNB) followed the ECB rate increase but maintained a negative spread. The Bank of Slovenia cut its interest rates by 25 basis points in early June but reversed this move in early August.

⁶ In Poland, bank loan dynamics was accelerated after the Banking Supervision watchdog announced restrictions on FX mortgage lending effective from July 2006. The Bank of Estonia announced it would raise banks' reserve requirement from 13 percent to 15 percent as of September.

⁷ The IMF has advised Estonia and Lithuania to implement required excise tax increases as soon as possible since the inflation target is not likely to be met in the near term in any case.

Chart 41. Policy Rates in Visegrad countries in 2006



Source: CBs.

Public finances

EU8 countries have generally not taken advantage of the ongoing economic boom to further consolidate public finances. With elections in several countries in the region in 2006, taxes have generally been cut and social spending increased, leading to expansionary and pro-cyclical fiscal policies in most of the EU8 countries in 2006 (with Slovakia the main exception) and similar tendencies envisaged for 2007 (with Hungary the main exception). This has further pushed back euro adoption plans in the region.

Table 4. GG budget (ESA95)

	CZ	EE	HU	LV	LT	PL	SK	SI
2005 outcome								
Balance (w/ CPR)	-2.6	1.6	-7.5	0.2	-0.5	-4.3	-3.5	-1.8
Cost of pension reform	..	..	1.4	..	0.5	1.8	0.6	..
Balance (w/o CPR)	-2.6	1.6	-6.1	0.2	0.0	-2.5	-2.9	-1.8
2006 estimate								
Balance (w/ CPR)	-3.3	1.5	-10.1	-1.5	-1.2	-4.4	-3.4	-1.8
Cost of pension reform	..	..	1.5	..	0.7	2.0	1.2	..
Balance (w/o CPR)	-3.3	1.5	-8.6	-1.5	-0.5	-2.4	-2.2	-1.8
2007 estimate								
Balance (w/ CPR)	-3.8	0.7	-6.8	-1.2	-1.1	-4.2	-3.0	-1.7
Cost of pension reform	..	..	1.7	..	0.8	1.9	1.1	..
Balance (w/o CPR)	-3.8	0.7	-5.1	-1.2	-0.3	-2.3	-1.9	-1.7

Note: CPR denotes "cost of pension reform." Source: Eurostat, Government forecasts and staff estimates (italics).

Table 5. Planned EMU membership dates

	August 2004		August 2006		
	ERM II	Planned time for EURO adoption	ERM II	Planned time for EURO adoption	Risk "+" / "-" Reasons of delay
Czech Republic	No concrete timetable	2009-2010	after 2006*	2010	"+" deficit
Estonia	June 2004	2007	June 2004	2008	"+" inflation
Hungary	No concrete timetable	2010 (if possible 2009)	2009*	No concrete date	"+" deficit/debt
Latvia	April 2005	2008	May 2005	No concrete date	"+" inflation
Lithuania	June 2004	2007	June 2004	No concrete date	"+" inflation
Poland	No concrete timetable	No explicit date	No concrete timetable	No explicit date	
Slovak Republic	Before June 2006	Beginning of 2009	November 2005	Beginning of 2009	"-" lack of coordination
Slovenia	June 2004	2007	June 2004	January 2007	

Source: CPs, MOFs, CBs.

*) CZ - Nov 2005; HU - According to Finance Minister Veres, Hungary may adopt the euro between 2011 and 2013 but the new CP contains no official target date. The government of Latvia indicated 2010 as realistic for euro adoption.

"No explicit date" means that no target date for euro adoption has been announced so far. "No concrete date" means that earlier targets have been abandoned and no new targets officially announced.

- ▲ In Slovakia, the general government deficit could decline to around 2.2 percent of GDP this year from 2.9 percent of GDP in 2005 (figures excluding cost of pension reform), mainly due to higher revenues but also lower capital spending interest costs on public debt (Table 4). However, the new government wants to introduce several new spending programs already this year, and all budgetary chapters have been asked to save 10 percent of their annual budget by cutting non-wage spending in order to accommodate this additional spending. This would likely mean further, undesirable cuts in capital spending. The outcome of these plans is difficult to judge, but they amount to less than the rhetoric suggests.

The draft budget for 2007-09 submitted to the government on August 16 assumes a further reduction in the deficit to 1.9 percent of GDP in 2007 and 1.3 percent of GDP in 2008 (consistent with a deficit in 2007 of 3.0 percent of GDP including cost of pension reform). However, the budget plans lack clarity, both about the central government budget and the general budgetary sector. The final budget proposal should be ready by the end of September, and will likely reflect several new initiatives in line with the new government's program manifesto. On the revenue side, this includes introduction of a lower 10 percent VAT rate on medicinal drugs and selected medical goods and a "millionaire tax" on high income earners. There may also be a new special tax on regulated monopolies. On the expenditure side, plans call for increasing the allowance for the first child to SK 15,460 (from current SK 4,460), payment of a Christmas allowance to pensioners, increased subsidies to farmers and for public transport, and compensation of 300,000 participants that lost their money in past pyramid schemes. To finance these initiatives and maintain the target fiscal balance in 2007, the government aims to reduce public administration employment and improve procurement.

The new government has announced its commitment to the 2009 euro adoption target introduced by the previous government (Table 5), but the current lack of clarity regarding fiscal plans for 2007 and beyond makes it difficult to assess the extent to which this goal is substantiated.

- ⤴ In Poland, the PIS-led government has committed to the PLN 30 billion state budget deficit ceiling introduced by the previous government. The fiscal deficit is set to remain broadly unchanged in 2006 (at about 2.4 percent of GDP excluding cost of pension reform) compared to the year before on the back of strong revenues which accommodate increased social spending (child bonuses, family allowances for farmers, longer paid maternity leave and a 30 percent increase in healthcare wages from October 1) and support to farmers.⁸

The draft budget for 2007 is consistent with the prevailing deficit ceiling, although there are strong pressures from coalition parties to raise this ceiling. Expenditures will be boosted by higher social spending (including a shift back to annual indexation for pensions, public wages, and social benefits as well as increases in family benefits) and higher spending on defense. The government has withdrawn from the plans announced in the spring by then Finance Minister Gilowska to cut social security contributions from 2007 (aimed at stimulating job creation) as it prioritized additional spending over financing the reform (costing around 1 percent of GDP).

PM Kaczynski has declared that euro adoption is not among his priorities, and the setting of any target for euro adoption is therefore likely to be postponed until after the next parliamentary elections (due in 2009). The latest convergence program envisaged that the fiscal deficit would rise to above the 3 percent of GDP threshold in 2008 (given the required phasing in of pension reform costs), and although the government maintains that it would meet all the Maastricht criteria in 2009 it is seeking a longer period over which to phase in pension reform costs.

- ⤴ In Hungary, the deficit is expected to widen further to over 10 percent of GDP (including cost of the pension reform) in 2006 (compared to 6 percent of GDP in the budget and 7.4 percent of GDP in 2005) despite measures announced in June of almost 2 percent of GDP in 2006. This marks the fourth consecutive year of significant deficit overshoot caused mainly by spending overruns, notably on subsidies for pharmaceuticals, electricity and natural gas used by households, health, pensions and interest payments. The wider gap is also the result of additional spending to cover deficits among local governments, the railways and the Budapest municipal transport system as well as partial cancellation of Iraqi debt and flood recovery costs. Moreover, methodological and accounting changes have increased this year's deficit by 1.4 percent of GDP (Gripen fighter jet purchases costing 0.3 percent of GDP and motorway construction under PPP-schemes costing 1.1 percent of GDP).

The revised convergence program, submitted to the EC on 1 September 1, aims to reduce the general government deficit to 6.8 percent of GDP in 2007 and further to 3.2 percent of GDP by 2009. The fiscal austerity package announced over the summer relies heavily on tax hikes (VAT, corporate income taxes, tax on capital gains and interest income, a special bank tax, higher personal income taxes for high income earners, higher social security contributions and higher excise taxes) in 2006-2007, while expenditure cuts are clearly back-loaded (Table 6). The specific measures underlying the envisaged reduction expenditures (by about 4 percent of GDP between 2006 and 2009) include cuts in consumer subsidies, reduction in the operational expenditures of the public sector (cuts in central government employment,⁹ more flexible wage regulations, cuts in spending on purchase of goods and services) as well as savings from

⁸ Despite these fiscal prospects and plans, the public debt-to-GDP ratio is likely to breach the first preventive threshold (50 percent of GDP) in 2006, and in 2007 the ratio would increase further as the stalled privatization process limits non-debt financing of the deficit.

⁹ The number of ministries will be reduced from 14 to 11 and the number of employees by 20 percent from January 1, 2007.

comprehensive reform of local governments, education, health care and pensions.¹⁰ The feasibility of many of these reforms is uncertain, including because some would require approval by a qualified majority in parliament. Further, the government plans stricter control over spending through quarterly reporting and introduction of reserves.

Table 6. Hungary's fiscal austerity program, % of GDP

	2006	2007	2008	2009	2006-09
Revenues	-0.7	1.8	0.6	0.6	3.0
Expenditures	1.9	-1.5	-1.9	-0.5	-3.9
<i>in which:</i>					
<i>Compensation of employees</i>		-0.73	-0.90	-0.22	-1.85
<i>Intermediate consumption</i>		-0.64	-0.47	-0.18	-1.29
<i>Social transfers other than in kind</i>		0.13	0.02	-0.3	-0.15
<i>Social transfers in kind supplied via market producers</i>		-0.25	-0.14	-0.10	-0.49
<i>Investments and other spending programmes implemented from domestic sources</i>		-0.74	-0.75	-0.40	-1.89

Note: Spending measures exceed total savings as spending is increased in other areas.

Source: Convergence Program of September 1, 2006.

Hungary has dropped any specific euro adoption target, and official indications that Hungary might be able to join the ERM-2 sometime during 2007-09 (allowing for euro adoption by 2010-12) are hardly credible given that the fiscal deficit would remain above 3 percent of GDP through 2009 and debt well-above 60 percent of GDP beyond that year, even with full implementation of the program.

- ✧ In the Czech Republic, the fiscal deficit is likely to increase to about 3.7 percent of GDP in 2006 (compared to 2.6 percent of GDP last year) owing to tax cuts and increased social spending, including on pensions and healthcare, which results in a breach of the total spending ceiling in the Medium Term Expenditure Framework.¹¹ Outcomes could be even worse to the extent carried-over reserves are spent.¹²

Although the 2007 budget process has been delayed owing to the political stalemate, the fiscal deficit is set to widen further to at least 4 percent of GDP next year reflecting increases in social spending (approved by the former government ahead of the June elections with the support of the opposition). This exceeds the 3.3 percent of GDP deficit pledged in the November 2005 Convergence Program.

The fiscal outlook, lack of any consensus on public finance reform (with the ODS preferring tax cuts and the CSSD increased social spending), and ODS's skepticism about the near-term benefits of euro adoption will almost inevitably delay earlier plans to enter the ERM-2 in 2007 and join the eurozone in 2010.

¹⁰ Key measures would include closure of underutilized hospitals and schools, introduction of co-payments in health care, linking some healthcare services to timely payment of social contributions, increase in the retirement age and tightened eligibility for early retirement and disability pensions, introduction of tuition fees for students in state-financed higher education institutions, and reform of public transport and local government financing.

¹¹ In 2006, the last of a scheduled series of corporate income tax-rate cuts reduced the rate from 26 percent to 24 percent. This still leaves the corporate tax rate relatively high compared with some neighboring countries, although the effective tax rate has been reduced by a number of measures, in particular higher depreciation rates on assets.

¹² The 2006 budget assumed that unspent authorized spending carried over from 2005 would remain unchanged at 1¾ percent of GDP.

- ⤴ In the Baltic countries, fiscal outcomes in 2006 are likely to be worse than last year, at least in Latvia and Lithuania. Higher than expected revenues have led to supplementary budgets in Estonia (spending raised by 1.2 percent of GDP) and Lithuania (spending raised by 0.7 percent of GDP), and the same is planned for Latvia immediately after elections in October. While Estonia should maintain a fiscal surplus of about 1½ of GDP, both Lithuania and Latvia would move from broadly balanced outcomes last year to deficits of about ½ and 1½ percent of GDP, respectively.

In Estonia, budget plans for next year prudently envisage a surplus of 0.7 percent of GDP (although this is lower than the projected outcome in 2006, the budget for 2006 was balanced), with a strong expansion of both revenues and expenditures. All ministries will receive additional funds, but Social Affairs the most. Minimum monthly wages of policemen, fire fighters and prison guards will be increased by 30 percent next year while teachers will see a 15 percent increase in their salaries. No information is available yet on budget plans for next year in Lithuania and Latvia.

STRUCTURAL REFORMS

Progress on advancing the outstanding reform agenda has been mixed following EU accession. While some further progress has been made in the region on broad indicators of transition, economic freedom and corruption, other indicators relating to competitiveness, ease of doing business, and governance reveal a more nuanced and less positive picture. Among other areas, privatization and liberalization in “strategic sectors” has seen little momentum in most of the EU8 countries. Furthermore, critical public finance and administration reforms, which are not well captured in the broader indices above, have largely stalled. This may reflect a combination of “reform fatigue” in the aftermath of EU accession and uncertain political trends in the region.

Since 2004, the EU8 countries have made a progress in a wide range of areas, including liberalization, privatization, the business environment, competition, infrastructure, and the financial sector (as indicated by EBRD transition indicators) as well as reduced the level of government interference in the economy (as indicated by the Index of Economic Freedom) (Box 3, Table 7). Moreover, EU8 countries (with the exception of Poland) have managed to scale back corruption, although it remains an issue of concern in most countries in the region. However, business regulations, broader governance and competitiveness have deteriorated in recent years in several of the EU8 countries (Box 3, Table 7 and Table 8). These various indicators do not paint an entirely consistent picture as methodologies vary and should thus be treated with some caution.

Box 3. Structural reforms and Doing Business 2007 in the EU8

After joining the EU, the NMS have further improved on the Index of Economic Freedom - all countries apart from Latvia managed to improve their scores, due mainly to progress in the area of Trade and Fiscal Burden. Better scores in the fiscal area result mainly from the introduction of more business-friendly and transparent corporate taxes (Czech Republic, Hungary, Poland and Slovakia).

According to World Bank BEEPS indicators there has also been further progress on reducing corruption, which nevertheless remains a serious issue across the region. Lithuania is of particular concern having the highest bribe frequency in 2005 (and higher than in 2002), while the Czech Republic, Estonia and Hungary saw a deterioration in corruption as it related to doing business. Meanwhile, Slovakia made impressive progress by reducing bribe frequency by more than 10 pp. and corruption while doing business by 24 pp. within the last 3 years.

While a few countries (notably the Czech Republic and Estonia) have further strengthened competitiveness (in a broad sense), others (notably Poland and Slovenia) has gone backwards from

already low levels. According to the IMD Competitiveness Index, Poland and Slovakia showed the poorest performance on Government and Business Efficiency while Slovenia ranked lowest on Economic Performance.

Table 7. Selected reform indicators, 2002-2006

		CZ	EE	HU	LV	LT	PL	SK	SI
World Bank BEEPS- Bribe Frequency (%)	2002	13.33	12.14	22.55	17.90	20.62	18.57	36.02	7.14
	2005	9.93	6.47	9.93	7.49	24.08	14.78	10.64	4.65
World Bank BEEPS- Corruption as a problem while doing business (%)	2002	28.23	16.87	23.53	29.45	38.54	49.89	50.00	18.23
	2005	49.55	22.60	27.91	25.53	36.79	38.07	25.48	14.49
EBRD Transition Indicators ^a	2002	3.48	3.64	3.81	3.28	3.26	3.64	3.31	3.26
	2004	3.59	3.67	3.81	3.38	3.31	3.62	3.40	3.26
	2005*	3.67	3.69	3.86	3.38	3.36	3.67	3.45	3.26
Index of Economic Freedom- Heritage Foundation ^b	2002	2.29	1.73	2.23	2.49	2.35	2.65	2.81	3.25
	2004	2.39	1.76	2.55	2.41	2.19	2.81	2.44	2.70
	2006	2.10	1.75	2.44	2.43	2.14	2.49	2.35	2.41
IMD Competitiveness Index ^c	2002	55.29	63.41	56.65	NA	NA	30.18	45.65	45.44
	2004	56.44	68.43	57.21	NA	NA	41.95	57.46	55.50
	2006	63.00	71.42	57.32	NA	NA	39.96	57.44	51.64
Starting a business	2005/2006	85/74	50/51	80/87	26/25	44/48	99/114	54/63	89/98
Dealing with Licences	2005/2006	111/110	13/13	141/143	65/65	22/23	142/146	44/47	60/63
Employing Workers	2005/2006	44/45	151/151	89/90	125/123	119/119	61/49	73/72	149/146
Registering Property	2005/2006	55/58	23/23	100/103	102/82	2/3	80/86	4/5	93/97
Getting Credit	2005/2006	19/21	41/48	19/21	19/13	33/33	59/65	13/13	41/48
Protecting Investors	2005/2006	81/83	33/33	114/118	43/46	58/60	43/33	114/118	43/46
Paying Taxes	2005/2006	104/110	25/29	115/118	106/52	42/40	68/71	109/114	82/84
Trading Across Borders	2005/2006	39/41	5/6	67/76	27/28	31/32	96/102	79/88	101/108
Enforcing Contracts	2005/2006	55/57	20/20	11/12	11/11	5/4	111/112	58/59	85/84
Closing a Business	2005/2006	110/113	46/47	57/48	63/62	28/30	84/85	48/41	35/35
worsening		<							
no change		=							
improvement		>							

^a EBRD Transition Indicators- scores range from 1 (central planning) to 4 (fully functioning market economy)

^b Index of Economic Freedom- overall score is an average of 10 broad categories: Trade Policy, Fiscal Burden, Government Intervention, Monetary Policy, Foreign Investment, Banking, Wages&Prices, Property Rights, Regulation, Informal Market. Scores range from 1 (Free Economy) to 5 (Repressed Economy)

^c IMD's competitiveness index is made of four components: Economic Performance, Government Efficiency, Business Efficiency, and Infrastructure. Value of the index shows competitiveness against highest ranked country (100)

Changes in the ease of Doing Business also show a mixed picture since EU accession. Most EU8 countries fell in the global ranks between 2005 and 2006. Only one country in the region (Latvia) is ranked higher than a year ago. The Baltic States remain the most “business friendly” countries in the region, with Lithuania ranking highest in 16th place among the 175 countries reviewed. The worst regional performer is Poland, followed by Hungary and Slovakia (with the latter two countries slipping significantly compared to the last year’s rankings). In contrast to previous years, no country in the region is currently found among the top global reformers (this list is led by Georgia, Romania, Mexico, China, and Peru). On average, the EU8 ranks 43 while the EU14 (EU15 excluding Luxemburg) ranks 32. Five countries from the EU15 (UK, Denmark, Ireland, Sweden, and Finland) were placed higher than Lithuania, and two countries from the EU15 (Italy and Greece) were placed lower than Poland. The top-three global rankings are taken by Singapore, New Zealand and the United States.

Country	DB 2006	DB 2007	Starting a Business				Dealing with Licenses			Hiring and Firing Workers 2/					
	Ease of doing business		Procedures	Time	Cost	Minimum capital	Cost	Procedures	Time	Difficulty of Hiring	Rigidity of Hours	Difficulty of Firing	Rigidity of Employment 3/	Nonwage labor cost	Firing costs
Unit	Rank		number	days	% of income per capita		number	days	Index					% of salary	weeks of wages
Lithuania	15	16	7	26	2.8	48.8	18.2	14	151	33	80	30	48	31.2	30.3
Estonia	17	17	6	35	5.1	34.3	34.3	13	117	33	80	60	58	33.5	34.7
Latvia	31	24	5	16	3.5	26.1	36.3	22	152	67	40	70	59	24.1	17.3
Slovakia	34	36	9	25	4.8	39.1	17.1	13	272	17	60	40	39	35.2	13.0
Czech R.	50	52	10	24	8.9	36.8	14.5	31	271	33	20	30	28	35.0	21.7
Slovenia	56	61	9	60	9.4	16.1	122.2	14	207	61	60	50	57	16.6	39.6
Hungary	60	66	6	38	20.9	74.2	260.0	25	212	11	80	10	34	35.2	34.5
Poland	74	75	10	31	21.4	204.4	85.6	25	322	0	60	40	33	21.4	13.0
EU8	42	43	7.8	31.9	9.6	60.0	73.5	19.6	213.0	31.9	60.0	41.3	44.5	29.0	25.5
EU14 1/	32	32	6.9	19.7	6.3	33.9	83.0	13.9	175.2	33.3	52.9	37.9	41.4	27.0	39.3
USA	3	3	5.0	5.0	0.7	0.0	16.0	18.0	69.0	0.0	0.0	0.0	0.0	8.5	0.0
Country	Registering Property			Closing a Business			Getting Credit				Protecting Investors				
	Procedures	Time	Cost	Time	Cost	Recovery rate	Legal Rights 4/	Credit Information 4/	Public registry coverage	Private bureau coverage	Disclosure 5/	Director Liability 6/	Ease of shareholder suits 7/	Strength of investor protection 8/	
Unit	number	days	% of property value	years	% of estate	cents on the dollar	Index		% of adults		Index				
Lithuania	3	3	0.7	1.7	7.0	50.5	4	6	4.2	7.2	6	4	6	5.3	
Estonia	3	51	0.7	3.0	9.0	39.9	4	5	0.0	18.2	8	4	6	6.0	
Latvia	8	54	2.0	3.0	13.0	34.8	8	4	1.9	0.0	5	4	8	5.7	
Slovakia	3	17	0.1	4.0	18.0	48.1	9	3	1.0	45.3	2	4	7	4.3	
Czech R.	4	123	3.0	9.2	14.5	18.5	6	5	3.5	51.0	2	5	8	5.0	
Slovenia	6	391	2.0	2.0	8.0	44.9	6	3	2.9	0.0	3	8	6	5.7	
Hungary	4	78	11.0	2.0	14.5	39.7	6	5	0.0	5.9	2	4	7	4.3	
Poland	6	197	2.0	3.0	22.0	27.9	4	4	0.0	38.1	7	2	9	6.0	
EU8	4.6	114.3	2.7	3.5	13.3	38.0	5.9	4.4	1.7	20.7	4.4	4.4	7.1	5.3	
EU14	5.0	46.9	5.4	1.5	9.0	71.0	5.9	4.9	13.9	45.5	6.2	4.5	6.1	5.6	
USA	4.0	12.0	0.5	1.5	7.0	77.0	7.0	6.0	0.0	100.0	7.0	9.0	9.0	8.3	
Country	Paying Taxes			Trading Across Borders					Enforcing Contracts			Economy Character.			
	Payments	Time	Total tax rate	Documents for export	Cost to export	Time for export	Documents for import	Cost to import	Time for import	Procedures	Time	Cost	Informal economy	Population	
Unit	number	hours	% of gross profit	number	US\$ per container	days	number	US\$ per container	days	number	days	% of claim	% of GNP	millions	
Lithuania	13	162	48.4	5	704	6	12	782	17	24	166	8.6	30.3	3.4	
Estonia	11	104	50.2	5	640	3	6	640	5	25	275	11.5	..	1.3	
Latvia	8	320	42.6	6	965	11	5	965	12	21	240	11.8	39.9	2.3	
Slovakia	30	344	48.9	9	1015	20	8	1050	21	27	565	15.7	18.9	5.4	
Czech R.	14	930	49.0	5	713	20	8	833	22	21	820	14.1	19.1	10.2	
Slovenia	34	272	39.4	9	1070	20	11	1107	24	25	1350	15.2	27.1	2.0	
Hungary	24	304	59.3	6	922	23	10	1137	24	21	335	9.6	25.1	10.1	
Poland	43	175	38.4	6	2260	19	7	2260	26	41	980	10.0	27.6	38.2	
EU8	22.1	326.4	47.0	6.4	1036.1	15.3	8.4	1096.8	18.9	25.6	591.4	12.1	26.9	9.1	
EU14	16.9	222.2	52.8	4.7	884.6	10.5	5.9	942.4	12.4	23.6	416.1	12.4	18.8	27.5	
USA	10.0	325.0	46.0	6.0	625.0	9.0	5.0	625.0	9.0	17.0	300.0	7.7	8.8	296.5	

1/ Information not available for Luxembourg

Source and for methodology see www.doingbusiness.org; in 2006 175 countries were reviewed.

2/ indexes take value of 0 to 100, with higher values indicating more rigid regulation

3/ Rigidity of employment is an average of previous three sub-indices

4/ The index ranges between 0 and 10, with higher scores indicating that collateral and bankruptcy laws are better designed to expand access to credit

5/ The index ranges between 0 and 10, with higher values indicating greater disclosure

6/ The index ranges between 0 and 10, with higher values indicating greater liability of directors

7/ The index ranges between 0 and 10, with higher values indicating greater powers of shareholders to challenge the transactions

8/ The protecting-investors index is the average of the previous three indices. The index ranges between 0 and 10, with higher values indicating better investor protection

Table 8. Doing Business 2007

There are two areas in which the business environment in the EU8 is not worse than that of the EU14:

Hiring and firing conditions are almost the same in the EU8 and the EU14. While hiring costs are almost equal, firing costs are lower in the EU8. However, both groups of countries are outperformed by the US.

Protecting investors is equally successful in the EU8 and the EU14, although the disclosure index in the former group is slightly worse. Again, the US performs much better.

The critical issues differ significantly among EU8 countries, but there are some commonalities. Attention should be focused on credit bureau activities and closing a business, and some other areas. Limiting the informal economy remains a challenge in Latvia.

Starting business. The number of procedures, cost and time is higher in the EU8 than in the EU14 and minimum capital is almost twice as high as in the EU14.

Dealing with licenses is cheaper in the EU8, but requires more procedures and time than in the EU14.

Registering property is cheaper in the EU8 and requires the same number of procedures as in the EU14, but takes much longer in the EU8 (114 days) compared to 47 days in EU14 and only 12 days in the US.

Closing a business takes more than twice as long in the EU8 and is characterized by higher costs of estate and much lower recovery rates than in the EU14 and the US.

Getting credit. Legal rights and credit information is almost equal to the EU14, but the EU8 suffer from very low coverage of public registry and private bureaus.

Paying taxes. While on average taxation is lower in the EU8 and comparable with the US, the payments are more frequent and more time than in the EU14.

Trading across borders. There are more bureaucratic burdens and higher costs of trade turnover in the EU8 than in the EU14 and the US.

Enforcing contracts. Costs are comparable with the EU14, but it takes a half of year longer in the EU8 than in the EU14 and nearly 300 days longer than in the US.

Recent reform initiatives in the region do not suggest much forward momentum. While there have been sporadic steps in the right direction, there have also been steps backwards, and critical outstanding reforms of strategic enterprise sectors and public finance and administration are either still on the table or have been taken off altogether. Efforts to promote public finance reforms were discussed above - the following looks at other reform initiatives.

In Poland, the government has focused on administrative reforms as a means to reduce government spending and reassertion of state control over strategic enterprises. Deeper reforms of social spending are not under consideration.

- ✦ Privatization has stalled completely - in the first half of this year, privatization proceeds amounted to only 7.2 percent of the annual target.
- ✦ Amendments to the Act on Public Procurement, aimed at facilitating and shortening procedures connected with public procurement and giving more flexibility for the selection of providers, were passed by Parliament in the spring. This may help speed up the absorption of EU structural funds, which has been very slow although improving recently.
- ✦ A Central Anti-Corruption Office was established by Parliament in mid-2006. While this should help combat corruption and lower overall costs of business activity in Poland, the new regulations were criticized by representatives of employers as the new office was entitled with broad competences that could interfere in business activity through the creation of various reporting and bureaucratic burdens.

In Hungary, the new government program ("New Equilibrium") aims at carrying out a series of structural reforms, including in education, healthcare and local government administration (see above). Further privatizations have been put off for the time being.

- ✦ Parliament approved changes to the Public Education Act on July 25. The most important change relates to the introduction of tuition fees in state institutions for higher education. Further, the new amendments stipulate integration of small schools and obligation for teachers to take on extra classes. Both changes aim at reducing education spending. However, President Solyom has declined to sign the new education bill into law and instead sent it to the Constitutional Court for consideration.
- ✦ Parliament rejected bills to reform local government and downsize the Parliament. The government had proposed to consolidate sub-national governments into seven regional governments and micro regions instead of the current municipal structure, aiming to reduce bureaucracy and provide for more efficient use of EU funds. It had also proposed to reduce the size of Parliament from the current 386 deputies to 298. Both measures required qualified majority, but only the government coalition voted for it.

In the Czech Republic, the previous government focused on improving the business environment, while pension and healthcare reforms as well as privatization of strategic enterprises (notably the sale of the state's 68 percent stake in electricity conglomerate CEZ) had been put off. Differing political views between the ODS and the ČSSD on the reform of pension and healthcare systems look likely to continue to hamper efforts to reduce government spending and enhance medium-term fiscal sustainability.

- ✦ New bankruptcy legislation was passed in early 2006. This aims to strengthen the position of creditors in various ways, including the introduction of a "reorganization" option. Legal changes aimed at reducing the administrative tasks of judges, lightening checking procedures in legal processes and shortening the maximum time allowed for registration of a file with the courts were also introduced, while business registration forms were standardized.

In Slovakia, structural reforms implemented in 2004-05 by the previous center-right government helped to strengthen public finances, while the new government proposes to roll back numerous reform measures. Key elements of its program include (in addition to what was already mentioned above):

- ✦ Canceling the system of healthcare co-payments and fees and protecting hospitals from bankruptcy (from October 2006).

- ✧ Abolishing the Special Court and Special Prosecutor's Office from 2007.
- ✧ Retaining remaining state shares in "strategic companies." The Austria-Slovak company that won the tender (organized by previous government) for the sale of three Slovak airports did not obtain any decision from the anti-monopoly authority on the purchase of 66 percent of the Bratislava airport before a set deadline, which allowed the new government to withdraw from the contract. The government also decided that Railway Cargo will not be privatized.

In Estonia, the government in September decided to renationalize Estonian Railways (claiming that the privatization contract had been violated), although it remains unclear how this will be accomplished. Baltic Rail Services, a mixed U.S., British and Estonian consortium, owns 66 percent of the shares. The government's decision came after it received another offer for the BRS stake in the company.

In Latvia, the state privatization agency in August approved a long-awaited plan for the sale of the state's 39 percent stake in Ventspils Nafta, an oil transit company. Under the plan, which was also approved by Latvijas Naftas Tranzits, the largest shareholder of Ventspils Nafta, the state's stake will be sold via an auction in various lots with the minimum price guaranteed. Poland's PKN Orlen, Kazakhstan's state oil and gas company KazMunaiGaz and Russian state-controlled Rosneft have all shown an interest in the sale. However, Ventspils Nafta has struggled operationally since 2003, when Russia turned off the pipe that feeds the company crude oil thus forcing it to accept crude deliveries via more expensive rail.

In Lithuania, the government agreed in May 2006 to sell its 31 percent stake in Lithuania's oil refinery, Mazeikiu Nafta (Maizeikiai Oil), to Poland's PKN Orlen for US\$852m. PKN also purchased the 54 percent stake held by the Russian oil company Yukos, for a reported US\$1.43bn. The acquisition should be finalized by early 2007. The refinery went through a modernization program that enabled it to meet EU standards and expand sales into Western Europe, but questions remain about the new owner's ability to guarantee stable supplies of oil for the refinery.

WORLD BANK ACTIVITIES

ESTONIA AND LITHUANIA

Estonia and Lithuania graduated from IBRD borrower status to become development cooperation partners on September 17 at an official signing ceremony held during the World Bank and International Monetary Fund Annual Meetings in Singapore.

POLAND

- The Third Road Maintenance and Rehabilitation project for € 150 million was approved by the World Bank on June 6, 2006. Implementation has started and so far 35 percent of the loan proceeds have been disbursed with a further 35 percent expected before the end of the year to support implementation of the national road agency (GDDKiA) maintenance program for 2006 with the balance of the proceeds to be disbursed over a five-year period to support implementation of performance-based maintenance and rehabilitation contracts on a pilot basis and continued modernization of GDDKiA.
- Discussion of the World Bank's Annual Business Plan for 2007 with the Government started in June and should be completed by the end of September following the Council of Ministers approval of the 2007 budget. The level of activities for 2007 is expected to be comparable to levels in 2005 and 2006.

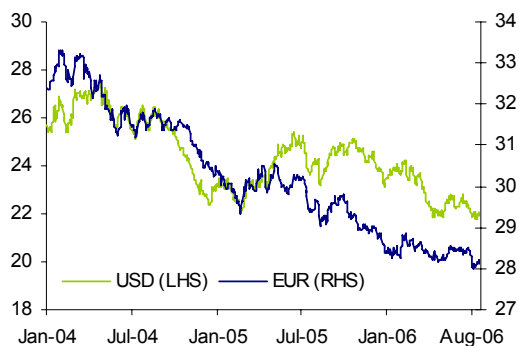
SLOVAKIA

- A "Transition Policy Note," providing the World Bank's view on the issues and challenges facing the new Government in Slovakia, was discussed with key Government members in August.

The note focuses on four priority areas: economic growth and euro adoption; jobs and competitiveness; social cohesion; and better Government and greater impact of EU funds.

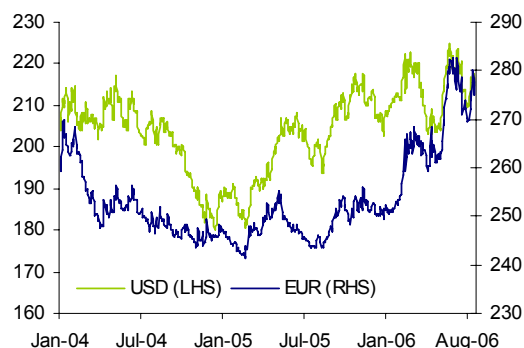
- A workshop on “Statistical Master Plan for Slovakia” was organized in September by the World Bank in cooperation with the Statistical Office of the Slovak Republic. The aim of the workshop was to discuss main recommendations of the master plan prepared by an independent consultant, with a particular focus on proposed measures focused at increasing the capacity of the statistical system to provide relevant and up to date information for policy making.
- The World Bank also sponsored a regional workshop in September on Administrative Capacity Development in the EU8 countries, as part of its broader, multi-year work program on public sector and finance reforms in the region. The workshop discussed a set of draft papers analyzing critical aspects of public management in the region, including strategic planning and performance management, civil service development and e-governance.
- A study on integration of the Slovak Republic into the CAP Single Farm Payment Mechanism has been finalized and will be discussed with the Ministry of Agriculture of the Slovak Republic in the near future. The study provides an assessment of the current status of implementation of the Common Agricultural Policy (CAP) and explores options and impacts of shifting from the current CAP implementation scheme to the future Single Farm Payment Mechanism to be introduced in 2009.

Chart 42. Czech Republic- US\$, € exchange rates



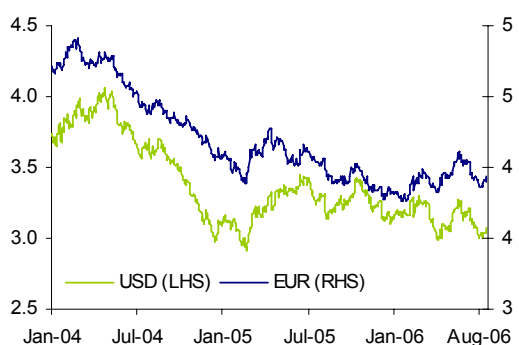
Source: Reuters

Chart 43. Hungary- US\$, € exchange rates



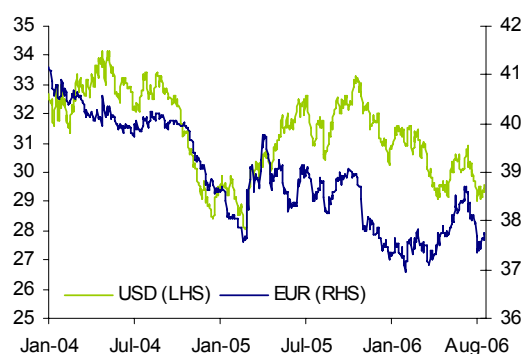
Source: Reuters

Chart 44. Poland- US\$, € exchange rates



Source: Reuters

Chart 45. Slovakia- US\$, € exchange rates



Source: Reuters

Table 9. Indicators of confidence and economic sentiment, changes in Q3 compared to H1-06, SA

	CZ	EE	HU	LV	LT	PL	SK	SI
Industry	↑	↑	↓	↑	↔	↑	↑	↑
Services	↑	↑	↓	↔	↑	↑	↑	↑
Consumer	↑	↓	↓	↑	↔	↑	↑	↑
Retail trade	↑	↑	↓	↓	↑	↑	↑	↑
Construction	↑	↓	↑	↑	↑	↑	↑	↑
=ESI	↑	↑	↓	↑	↑	↑	↑	↑

Source: EC.

Chart 46. MCI in Poland, % (reer weight 30.6%)

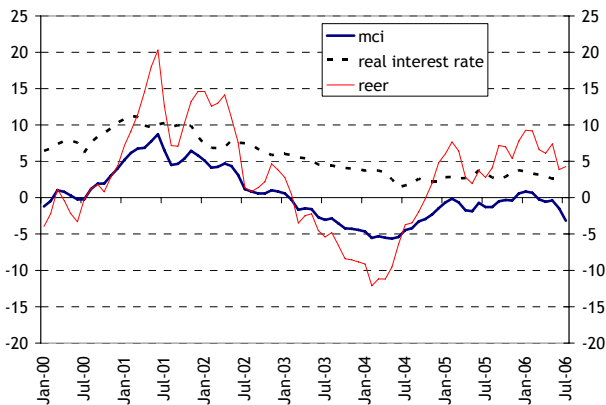


Chart 47. MCI in Hungary, % (reer weight 61.4%)

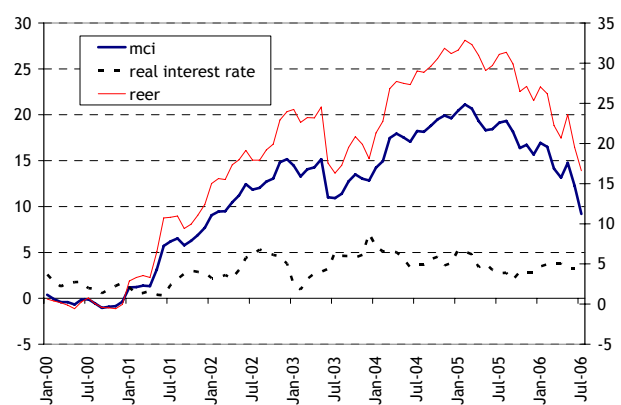


Chart 48. MCI in the Czech Republic, % (reer weight 59.2%)

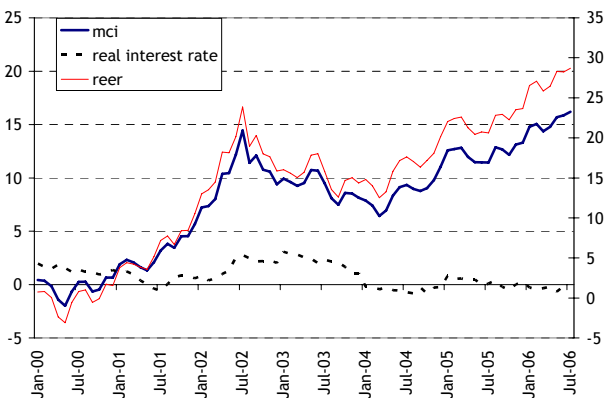
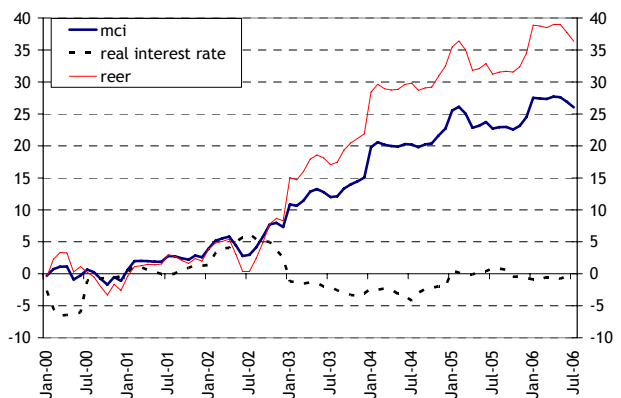


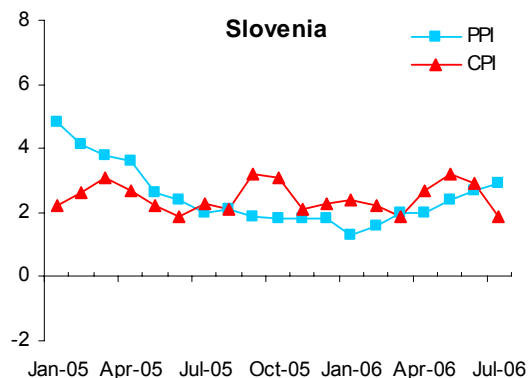
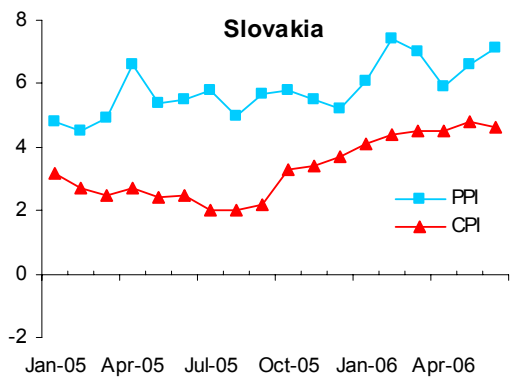
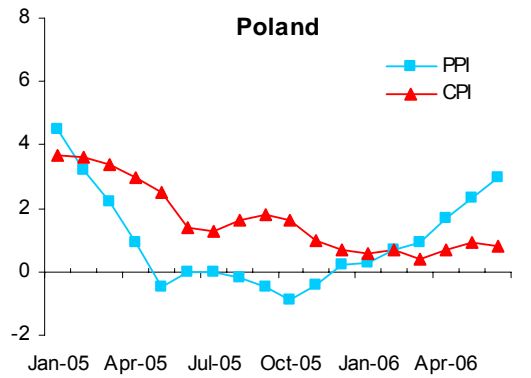
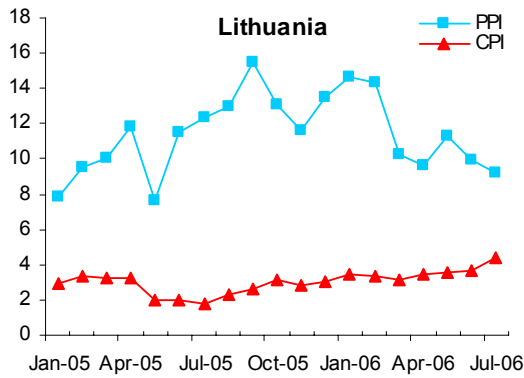
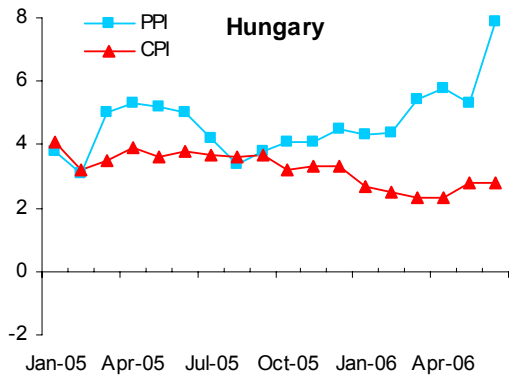
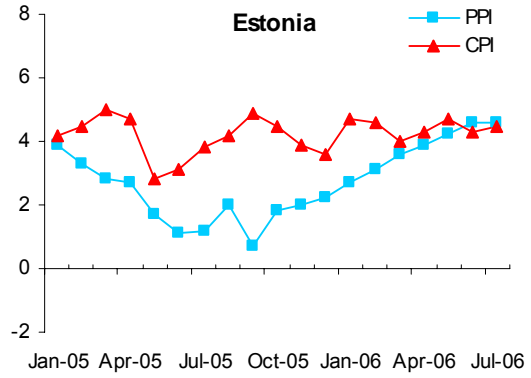
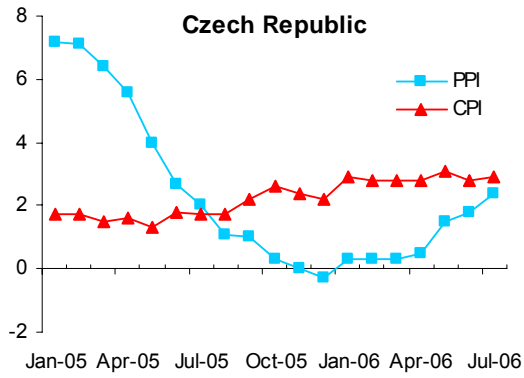
Chart 49. MCI in Slovakia, % (reer weight 69.4%)



The monetary conditions index is defined as: $MCI = (1-w)*(r - r_{base}) + w*[(e/e_{base}) * 100 - 100]$, where r = 3-month real interest rate, CPI deflated; e = single-based index of real effective exchange rate (REER), CPI deflated and calculated by Eurostat for 12 trading partners (REER increase = LCU appreciation); w = weight (import-to-GDP ratio, average in 2000-2005). A higher value of the MCI indicates tighter monetary conditions.

Source: Eurostat; CSOs; and staff calculations.

Chart 50. CPI vs. PPI



Source: CSOs.

STATISTICAL ANNEX

	2002	2003	2004	2005	2Q 05	3Q 05	4Q 05	1Q 06	Mar-06	Apr-06	May-06	Jun-06
GDP, SNA (real, %, y/y)												
Czech Republic	1.9	3.6	4.2	6.1	6.1	5.9	6.9	7.1				
Estonia	7.2	6.7	7.8	9.8	9.9	10.6	11.1	11.6				
Hungary	3.8	3.4	5.2	4.1	4.5	4.5	4.3	4.6				
Latvia	6.5	7.2	8.5	10.2	11.2	11.4	10.6	13.1				
Lithuania	6.8	10.5	7.0	7.5	8.4	8.0	8.8	8.8				
Poland	1.4	3.8	5.3	3.4	2.9	3.9	4.3	5.2				
Slovakia	4.1	4.2	5.4	6.1	5.4	6.3	7.4	6.3				
Slovenia	3.5	2.7	4.2	3.9	5.4	3.6	3.7	5.1				
Consumption, SNA (real, %, y/y)												
Czech Republic	3.5	6.3	0.8	1.8	1.9	3.1	1.4	2.8				
Estonia	9.5	7.2	5.0	8.1	6.6	8.3	10.7	12.9				
Hungary	9.3	7.8	2.8	1.7	2.0	1.9	1.4	2.0				
Latvia	6.1	6.7	7.7	9.1	6.5	10.9	13.5	16.8				
Lithuania	4.9	10.5	9.2	9.4	8.9	11.0	12.3	14.1				
Poland	2.9	2.5	4.0	2.7	2.6	2.4	3.3	4.7				
Slovakia	5.2	1.2	3.6	5.3	5.0	6.4	4.1	6.6				
Slovenia	1.8	3.0	3.1	3.2	3.6	3.4	3.1	3.3				
Gross capital formation, SNA (real, %, y/y)												
Czech Republic	4.6	-1.4	8.2	2.9	0.6	1.9	7.3	12.4				
Estonia	20.0	8.7	5.2	13.2	8.3	18.7	18.6	14.6				
Hungary	-3.3	1.1	2.8	-4.7	-12.5	0.3	-5.1	-0.8				
Latvia	5.8	22.0	23.0	6.1	1.5	3.7	7.1	8.7				
Lithuania	12.3	18.7	25.5	8.6	18.4	3.5	3.1	1.6				
Poland	-7.2	3.3	14.7	-0.3	-12.0	-0.3	11.4	3.0				
Slovakia	1.3	-8.0	14.3	15.3	17.8	0.4	38.6	13.4				
Slovenia	4.0	10.1	9.2	-3.0	-8.0	-4.4	2.0	6.0				
Gross fixed capital formation, SNA (real, %, y/y)												
Czech Republic	5.1	0.4	4.7	3.6	3.8	3.8	4.4	6.8				
Estonia	17.2	8.5	6.0	13.9	13.3	14.5	16.5	12.8				
Hungary	9.3	2.5	8.4	6.6	9.4	8.7	3.1	9.7				
Latvia	13.0	12.3	23.8	18.6	21.2	22.2	12.9	18.1				
Lithuania	11.1	14.0	12.3	11.2	4.9	14.3	15.2	24.5				
Poland	-6.3	-0.1	6.4	6.5	4.0	6.5	10.1	7.4				
Slovakia	0.3	-2.3	5.0	13.8	12.1	16.9	19.5	16.1				
Slovenia	0.9	7.1	5.9	3.7	3.9	1.6	8.2	8.9				
Exports, SNA (real, %, y/y)												
Czech Republic	2.1	7.2	21.1	10.6	5.9	10.9	10.1	17.6				
Estonia	0.8	5.8	16.0	21.3	18.0	20.9	28.9	17.3				
Hungary	3.9	7.8	16.4	10.6	11.3	11.5	12.7	18.2				
Latvia	5.4	5.2	9.4	20.7	21.6	20.9	20.2	13.6				
Lithuania	19.5	6.9	4.2	14.3	55.9	12.3	16.5	20.1				
Poland	4.8	14.2	14.0	8.1	10.2	6.1	11.8	20.8				
Slovakia	4.7	15.9	7.9	13.5	8.5	19.2	16.3	18.0				
Slovenia	6.7	3.1	12.5	9.2	9.6	9.5	8.8	13.7				
Imports, SNA (real, %, y/y)												
Czech Republic	5.0	8.0	18.2	4.9	-0.3	6.3	4.8	15.5				
Estonia	3.8	10.6	14.6	17.4	9.5	22.2	22.0	21.6				
Hungary	6.6	11.1	13.2	5.8	3.8	7.7	7.3	14.2				
Latvia	4.7	13.1	16.6	13.5	6.2	12.8	18.8	15.7				
Lithuania	17.7	10.3	14.8	15.9	19.2	13.0	16.8	21.8				
Poland	2.7	9.3	15.2	4.9	2.3	1.2	14.7	18.9				
Slovakia	4.6	7.6	8.8	15.5	12.3	16.5	20.5	20.8				
Slovenia	4.8	6.7	13.2	5.3	1.6	5.9	7.2	12.1				

	2002	2003	2004	2005	2Q 05	3Q 05	4Q 05	1Q 06	Mar-06	Apr-06	May-06	Jun-06
Industrial production (% y/y)												
Czech Republic	1.9	5.5	9.6	6.7	6.6	7.5	8.4	15.1	17.4	3.8	12.4	10.5
Estonia	8.3	11.1	10.5	9.1	11.1	9.8	8.3	8.4	8.1	0.8	11.4	8.9
Hungary	2.8	6.4	7.4	7.3	9.7	9.0	8.4	13.3	14.8	2.1	10.0	8.8
Latvia	5.8	6.5	6.0	5.6	7.8	7.5	7.4	8.4	8.9	5.1	2.2	5.7
Lithuania	3.1	16.1	10.8	7.3	8.8	7.7	8.1	12.5	13.4	9.7	15.2	13.6
Poland	1.1	8.3	12.3	4.1	1.5	2.5	4.1	12.4	16.4	5.8	19.1	12.2
Slovakia	6.4	5.1	4.2	3.6	3.1	4.9	6.2	9.6	16.5	3.5	10.9	12.0
Slovenia	2.4	1.4	4.8	3.1	5.2	2.3	5.5	7.7	7.3	1.1	9.8	4.3
Retail sales (excl. motor vehicles, automotive fuel, % y/y)												
Czech Republic	3.2	4.0	3.0	3.7	3.1	4.0	4.2	7.1	6.9	6.0	7.2	8.3
Estonia	14.4	9.9	13.1	12.0	11.0	13.0	15.0	21.3	21.0	18.0	22.0	23.0
Hungary	8.7	8.9	5.7	5.6	5.5	6.2	5.6	5.3	3.4	6.1	5.4	3.6
Latvia	12.1	13.4	12.5	21.2	18.2	21.6	22.3	15.8	18.5	14.0	20.8	20.9
Lithuania	7.9	11.1	10.7	12.9	10.3	15.6	17.1	9.3	9.1	6.6	5.6	5.9
Poland	1.9	3.6	7.1	2.1	-3.2	4.1	5.4	9.5	10.1	13.3	13.4	10.5
Slovakia	5.8	-5.2	6.2	9.7	8.1	10.6	11.0	7.7	10.0	8.6	9.3	10.7
Slovenia			3.8	6.8	6.4	8.0	7.3	3.3	1.9	2.3	4.7	2.7
Unemployment (% NSA, LFS data)												
Czech Republic	7.3	7.8	8.3	8.2	7.8	7.8	7.8	8.0				
Estonia	10.3	10.0	9.7	7.9	8.1	7.0	7.0	6.4				
Hungary	5.7	5.9	6.1	7.2	7.1	7.3	7.7	7.3				
Latvia	12.0	10.6	10.4	10.0	9.2	8.7	7.8	7.8				
Lithuania	13.8	12.4	11.4	8.3	8.5	7.2	7.1	6.4				
Poland	19.6	19.7	19.0	18.6	18.1	17.4	16.7	16.0				
Slovakia	18.5	17.4	18.1	16.2	16.2	15.6	15.3	14.9				
Slovenia	6.7	6.7	6.3	6.4	5.8	6.3	7.2	6.9				
CPI inflation (% average y/y)												
Czech Republic	1.8	0.1	2.8	1.9	1.6	1.9	2.4	2.8	2.8	2.8	3.1	2.8
Estonia	3.6	1.3	3.0	4.1	3.5	4.3	4.0	4.4	4.0	4.3	4.7	4.3
Hungary	5.3	4.7	6.8	3.6	3.8	3.7	3.3	2.5	2.3	2.3	2.8	2.8
Latvia	1.9	2.9	6.2	6.7	6.5	6.5	7.3	7.0	6.5	6.1	6.6	6.3
Lithuania	0.3	-1.2	1.2	2.7	2.4	2.3	2.9	3.3	3.1	3.5	3.6	3.7
Poland	1.9	0.8	3.5	2.1	2.3	1.6	1.1	0.6	0.4	0.7	0.9	0.8
Slovakia	3.3	8.5	7.5	2.7	2.5	2.1	3.5	4.3	4.5	4.5	4.8	4.6
Slovenia	7.5	5.6	3.6	2.5	2.3	2.5	2.5	2.2	1.9	2.7	3.2	2.9
PPI (% average y/y)												
Czech Republic	-0.5	-0.3	5.7	3.0	4.1	1.4	0.0	0.3	0.3	0.5	1.5	1.8
Estonia	0.4	0.2	2.9	2.1	1.8	1.3	2.0	3.2	3.6	3.9	4.3	4.6
Hungary	-1.8	2.4	3.5	4.3	5.2	3.8	4.2	4.7	5.4	5.8	5.3	7.9
Latvia	1.0	3.2	8.6	7.8	7.9	6.1	6.8	7.5	8.3	8.8	10.0	9.7
Lithuania	-2.8	-0.5	6.0	11.5	10.3	13.6	12.7	13.1	10.3	9.6	11.3	9.9
Poland	1.0	2.6	7.0	0.7	0.1	-0.2	-0.4	0.6	0.9	1.7	2.3	3.0
Slovakia	2.1	8.3	2.6	5.3	5.8	5.5	5.5	6.8	7.0	5.9	6.6	7.1
Slovenia	5.1	2.5	4.3	2.7	2.9	2.0	1.8	1.6	2.0	2.0	2.4	2.7
Exchange rate (nominal, LCU/€, period average)												
Czech Republic	30.81	31.84	31.90	29.78	30.13	29.69	29.30	28.60	28.65	28.50	28.27	28.39
Estonia	15.65	15.65	15.65	15.65	15.65	15.65	15.65	15.65	15.65	15.65	15.65	15.65
Hungary	243.0	253.5	251.7	248.1	249.8	245.6	251.8	254.6	260.9	265.5	262.4	272.4
Latvia	0.581	0.641	0.665	0.703	0.703	0.703	0.703	0.703	0.696	0.696	0.696	0.696
Lithuania	3.459	3.453	3.453	3.453	3.453	3.453	3.453	3.453	3.453	3.453	3.453	3.453
Poland	3.856	4.398	4.534	4.023	4.130	4.019	3.915	3.835	3.875	3.919	3.894	4.016
Slovakia	42.68	41.48	40.03	38.60	38.92	38.67	38.49	37.46	37.48	37.37	37.58	38.06
Slovenia	226.2	233.7	238.9	239.6	239.5	239.5	239.5	239.5	239.6	239.6	239.6	239.7

	2002	2003	2004	2005	2Q 05	3Q 05	4Q 05	1Q 06	Mar-06	Apr-06	May-06	Jun-06
Exchange rate (nominal, LCU/US\$, period average)												
Czech Republic	32.74	28.23	25.70	23.95	23.94	24.31	24.66	23.79	23.83	23.25	22.14	22.44
Estonia	16.61	13.86	12.60	12.59	12.42	12.82	13.16	12.92	12.97	12.46	12.21	12.45
Hungary	258.0	224.4	202.6	199.7	198.2	201.2	211.7	211.6	216.9	216.3	205.5	214.9
Latvia	0.618	0.571	0.540	0.565	0.557	0.576	0.591	0.584	0.585	0.574	0.551	0.554
Lithuania	3.677	3.062	2.779	2.775	2.737	2.830	2.902	2.871	2.875	2.825	2.712	2.723
Poland	4.080	3.889	3.654	3.235	3.278	3.296	3.290	3.187	3.223	3.198	3.049	3.171
Slovakia	45.33	36.77	32.25	31.02	30.85	31.69	32.36	31.20	31.19	30.54	29.46	30.05
Slovenia	240.2	207.1	192.4	192.7	190.2	196.4	201.5	199.2	199.5	195.9	187.6	189.2
Real effective exchange rate, CPI based (% , period average, y/y), (negative value= depreciation)												
Czech Republic	9.0	-2.7	3.0	2.2	4.7	4.3	3.8	3.7				
Estonia	3.4	2.4	1.7	0.5	1.1	0.9	-0.4	0.2				
Hungary	8.7	0.2	7.8	0.8	1.9	1.2	-3.8	-5.2				
Latvia	-4.6	-3.3	1.1	-1.3	-2.4	-2.6	-0.4	2.2				
Lithuania	2.8	1.3	-0.5	-0.9	-1.0	-2.4	-3.3	-2.0				
Poland	-8.2	-10.4	7.0	5.2	13.1	7.9	4.3	1.8				
Slovakia	4.4	13.5	8.0	1.0	2.5	1.7	1.4	2.3				
Slovenia	3.0	2.5	-1.0	-0.8	-1.3	-1.7	-2.7	-2.3				
Exports of goods (€, %, y/y)												
Czech Republic	9.3	5.8	28.8	13.5	7.2	14.0	12.9	23.3	25.4	9.5	24.2	15.9
Estonia	-1.6	9.9	19.4	29.2	30.8	29.3	32.4	28.4	32.9	28.5	26.2	25.6
Hungary	7.4	4.4	17.3	12.5	13.8	12.9	12.0	19.7	21.3	8.7	23.9	7.9
Latvia	8.2	5.8	26.0	28.7	30.1	24.8	28.0	18.2	16.7	6.8	14.5	28.9
Lithuania	15.8	11.2	21.4	27.1	28.5	27.1	28.6	32.7	37.4	16.7	33.8	34.2
Poland	8.2	9.3	26.8	19.3	20.1	15.2	19.8	22.8	26.2	11.4	31.7	15.5
Slovakia	8.3	26.7	14.7	16.3	9.1	20.5	22.5	27.6	33.8	16.2	32.8	23.4
Slovenia	5.9	2.9	16.6	17.6	19.5	15.6	16.9	22.8	23.4	11.7	25.0	14.6
Imports of goods (€, %, y/y)												
Czech Republic	6.1	6.3	23.0	9.6	2.8	9.7	9.4	24.3	26.1	9.4	26.7	16.4
Estonia	5.9	12.9	16.9	20.4	12.3	25.8	26.3	36.5	32.2	30.1	23.2	22.2
Hungary	6.4	5.9	15.2	9.2	4.4	12.5	11.5	20.2	23.2	2.6	22.7	9.0
Latvia	9.3	8.1	23.3	22.6	16.7	19.7	31.0	29.5	25.6	18.9	28.6	26.0
Lithuania	18.9	7.1	16.8	25.0	25.1	26.1	30.9	39.8	51.8	-4.1	40.9	40.8
Poland	4.4	3.2	19.5	13.3	5.6	11.9	18.3	22.0	21.6	5.9	25.9	10.4
Slovakia	6.3	13.7	19.0	20.1	12.8	16.2	29.0	31.0	28.5	17.2	31.0	23.7
Slovenia	2.0	5.7	16.6	14.5	8.5	15.0	18.0	20.4	22.9	5.1	23.6	16.0
Trade balance (% GDP)												
Czech Republic	-3.0	-2.7	-1.0	1.4	0.7	1.0	1.4	1.3				
Estonia	-15.8	-17.0	-18.0	-14.1	-15.0	-14.5	-14.1	-14.9				
Hungary	-3.2	-3.9	-3.0	-1.8	-1.8	-1.9	-1.8	-1.8				
Latvia	-15.8	-17.8	-20.3	-18.9	-18.2	-18.0	-18.9	-19.9				
Lithuania	-9.4	-9.1	-10.6	-11.2	-10.3	-10.5	-11.2	-12.1				
Poland	-3.7	-2.6	-2.3	-0.9	-1.3	-1.0	-0.9	-0.9				
Slovakia	-8.6	-1.9	-3.5	-5.2	-4.7	-4.0	-5.2	-5.8				
Slovenia	-1.1	-2.2	-3.9	-3.8	-3.0	-3.3	-3.8	-3.7				
Current account (% GDP)												
Czech Republic	-5.6	-6.2	-6.0	-2.1	-4.2	-2.8	-2.1	-2.6				
Estonia	-11.0	-12.1	-13.0	-11.0	-11.7	-12.1	-11.0	-12.0				
Hungary	-7.0	-8.7	-8.6	-7.4	-7.7	-7.7	-7.4	-7.4				
Latvia	-6.6	-8.1	-12.9	-12.4	-11.2	-11.1	-12.4	-13.3				
Lithuania	-5.1	-6.8	-7.7	-7.0	-6.5	-6.6	-7.0	-8.1				
Poland	-2.5	-2.1	-4.2	-1.4	-2.2	-1.5	-1.4	-1.5				
Slovakia	-7.8	-0.8	-3.4	-8.6	-5.6	-5.5	-8.6	-9.8				
Slovenia	1.5	-0.3	-2.1	-1.1	-1.4	-0.8	-1.1	-1.1				

	2002	2003	2004	2005	2Q 05	3Q 05	4Q 05	1Q 06	Mar-06	Apr-06	May-06	Jun-06
FDI net (% GDP)												
Czech Republic	11.2	2.1	3.7	8.1	7.5	7.8	8.1	7.6				
Estonia	2.2	8.4	6.2	17.6	22.6	22.7	17.6	12.4				
Hungary	4.1	0.6	3.5	4.8	3.7	2.7	4.8	6.0				
Latvia	2.7	2.3	4.3	3.1	3.9	4.0	3.1	4.0				
Lithuania	5.0	0.8	2.3	2.6	2.6	2.6	2.6	2.4				
Poland	2.0	2.0	4.7	2.2	3.1	3.5	2.2	2.5				
Slovakia	16.8	2.2	3.3	3.7	3.3	3.7	3.7	4.6				
Slovenia	6.5	-0.5	0.8	-0.1	0.0	-0.1	-0.1	0.2				
Net portfolio investment (% GDP)												
Czech Republic	-1.9	-1.4	2.1	-2.4	-0.9	-1.9	-2.4	-1.9				
Estonia	2.1	1.9	6.4	-16.6	-14.8	-16.1	-16.6	-19.7				
Hungary	2.6	3.6	6.8	4.1	7.6	6.5	4.1	5.6				
Latvia	-2.2	-2.0	1.7	-0.8	-0.2	-1.0	-0.8	-1.8				
Lithuania	0.1	1.5	0.9	-1.5	0.1	-0.8	-1.5	-1.8				
Poland	1.0	1.1	3.7	4.1	5.5	5.0	4.1	3.2				
Slovakia	2.3	-1.7	2.1	-2.1	-1.3	-1.2	-2.1	0.1				
Slovenia	-0.3	-0.9	-2.2	-4.5	-2.9	-3.0	-4.5	-3.8				
General government balance (ESA95, % GDP)												
Czech Republic	-6.8	-6.6	-2.9	-2.6								
Estonia	1.0	2.4	1.5	1.6								
Hungary	-8.4	-6.4	-5.4	-6.1								
Latvia	-2.3	-1.2	-0.9	0.2								
Lithuania	-1.4	-1.2	-1.5	-0.5								
Poland	-3.2	-4.7	-3.9	-2.5								
Slovakia	-7.7	-3.7	-3.0	-2.9								
Slovenia	-2.7	-2.8	-2.3	-1.8								
General government revenue (ESA95, % GDP)												
Czech Republic	40.4	41.1	41.7	41.5								
Estonia	37.8	39.1	37.9	37.5								
Hungary	43.7	43.4	44.1	44.5								
Latvia	33.4	33.5	34.9	36.4								
Lithuania	32.9	31.9	31.9	33.1								
Poland	41.0	39.9	38.6	40.8								
Slovakia	35.7	35.6	35.9	33.9								
Slovenia	45.4	45.2	45.3	45.5								
General government expenditure (ESA95, % GDP)												
Czech Republic	47.3	47.7	44.6	44.1								
Estonia	36.8	36.7	36.4	35.9								
Hungary	52.0	49.8	49.5	50.7								
Latvia	35.6	34.6	35.9	36.2								
Lithuania	34.3	33.2	33.4	33.7								
Poland	44.2	44.6	42.5	43.3								
Slovakia	43.3	39.4	38.9	36.8								
Slovenia	48.0	48.1	47.6	47.3								
Public debt (ESA95, % GDP)												
Czech Republic	28.5	30.1	30.7	30.3								
Estonia	5.5	6.0	5.4	4.8								
Hungary	55.0	56.7	57.1	58.4								
Latvia	13.5	14.4	14.6	11.9								
Lithuania	22.3	21.2	19.5	18.7								
Poland	39.8	43.9	41.9	42.5								
Slovakia	43.3	42.7	41.6	34.5								
Slovenia	29.7	29.1	29.5	29.1								
Oil (Brent) US\$/BBL	25.1	28.8	38.4	54.7	47.9	51.6	61.7	57.1	57.1	63.0	59.9	62.3
Exch. Rate (US\$/€)	0.946	1.131	1.244	1.244	1.259	1.259	1.220	1.188	1.186	1.210	1.194	1.202

Sources: Eurostat; WIIW; CSOs; NCBs; IMF; and World Bank.

VULNERABILITY INDICATORS*

Czech Republic	2002	2003	2004	2005	2Q 05	3Q 05	4Q 05	1Q 06
GDP growth, SNA (real, %, yoy)	1.5	3.2	4.2	6.1	6.1	5.9	6.9	7.1
Current account balance, (4Q cumulative, % of GDP)	-5.6	-6.2	-6.0	-2.1	-4.2	-2.8	-2.1	-2.6
FDI (4Q cumulative, % of GDP)	11.2	2.1	3.7	8.1	7.5	7.8	8.1	6.9
Total gross external debt (eop, % of GDP)	33.7	34.7	36.4	37.8	37.3	38.1	37.8	35.7
Change of international reserves in euro (eop, relative to previous period, %)	37.9	-5.6	-2.1	20.0	17.0	-0.1	0.9	-1.9
Reserves-to-short-term debt ratio (eop, %)	271.1	229.1	201.3	217.1	260.4	236.7	217.1	242.4
Money Supply-to-Reserves ratio (eop, %)	200.0	220.2	257.0	249.7	230.4	237.3	249.7	264.7
Overall balance of state budget (4Q cumulative, % of GDP)	-1.9	-4.2	-3.4	-1.9	-1.4	-0.9	-1.9	-1.6
Credit to private sector (eop, % of GDP)	30.8	31.4	32.7	36.3	34.7	35.8	36.3	37.0
Growth rate of credit to the private sector (avg, %)	-14.4	2.1	11.3	15.6	15.1	17.5	17.2	18.2
Foreign currency loans to the private sector (eop, % of loans to priv. sect.)	14.0	12.2	10.7	9.7	10.3	10.3	9.7	9.9
Non-performing loans (eop, % of total loans)	8.1	4.9	4.1	na	4.8	4.6	4.4	na
Short-term (3M) interest rates spreads to euro area (avg, basis points)	22.0	-6.0	25.0	-18.0	-27.0	-34.0	-23.0	-53.0
Change of stock exchange index (avg, relative to previous period, %)	6.5	27.4	48.3	51.6	2.5	12.9	7.1	8.7
Long term foreign currency sovereign credit rating according to S&P's	A- (↔) (S)	A- (↔) (S)	A- (↔) (S)	A- (↔) (S)	A- (↔) (S)	A- (↔) (S)	A- (↔) (P†)	A- (↔) (P)
Maastricht indicators								
HICP 12M rolling average inflation relative to reference value (perc. points)	25.5	-226.7	-86.2	-32.1	-10.6	-59.7	-84.9	-82.2
Convergence criterion bond yield relative to reference value (basis points)	-235.2	-249.4	-172.4	-186.8	-190.1	-180.4	-170.8	-199.1
Change of LCU/EUR rate, minus denotes euro depreciation (avg, %)	-9.6	3.3	0.2	-6.7	0.4	-1.5	-1.3	-2.4
Fiscal balance, ESA'95 (% of GDP)	-6.8	-6.6	-2.9	-2.6	na	na	na	na
Public debt, ESA'95 (% of GDP)	28.8	30.0	30.6	30.5	na	na	na	30.5

Notes: Czech Republic has adopted free floating as exchange rate regime in 1997.

Estonia	2002	2003	2004	2005	2Q 05	3Q 05	4Q 05	1Q 06
GDP growth, SNA (real, %, yoy)	7.2	6.7	7.8	9.8	9.9	10.6	11.1	11.6
Current account balance, (4Q cumulative, % of GDP)	-11.0	-12.1	-13.0	-11.0	-11.7	-12.1	-11.0	-12.0
FDI (4Q cumulative, % of GDP)	2.2	8.4	6.2	17.6	22.6	22.7	17.6	12.4
Total gross external debt (eop, % of GDP)	60.1	68.9	81.2	90.2	86.7	88.8	90.2	95.3
Change of international reserves in euro (eop, relative to previous period, %)	3.0	14.7	19.9	25.1	-5.4	0.3	16.6	-5.3
Reserves-to-short-term debt ratio (eop, %)	68.6	58.3	62.4	50.0	47.1	45.2	50.0	38.6
Money Supply-to-Reserves ratio (eop, %)	302.5	292.4	282.4	320.5	317.1	324.7	320.5	352.9
Overall balance of state budget (4Q cumulative, % of GDP)	2.0	0.3	-1.0	-1.4	-1.9	-1.2	-1.4	-1.7
Credit to private sector (eop, % of GDP)	46.3	54.1	63.6	72.9	68.2	72.1	72.9	76.8
Growth rate of credit to the private sector (avg, %)	23.2	26.1	27.4	34.9	32.2	35.6	39.2	40.5
Foreign currency loans to the private sector (eop, % of loans to priv. sect.)	82.8	81.6	81.1	80.4	81.5	81.8	80.4	80.3
Non-performing loans (eop, % of total loans)	0.8	0.4	0.3	na	0.3	0.2	0.3	na
Short-term (3M) interest rates spreads to euro area (avg, basis points)	56.0	59.0	39.0	19.0	26.0	20.0	7.0	9.0
Change of stock exchange index (avg, relative to previous period, %)	33.6	32.8	53.4	67.5	18.2	2.7	8.1	-2.9
Long term foreign currency sovereign credit rating according to S&P's	A- (↔) (S)	A- (↔) (P†)	A (†) (S↓)	A (↔) (P)	A (↔) (S)	A (↔) (P†)	A (↔) (P)	A (↔) (P)
Maastricht indicators								
HICP 12M rolling average inflation relative to reference value (perc. points)	159.5	-17.0	-49.7	170.1	188.8	173.4	170.7	154.4
Convergence criterion bond yield relative to reference value (basis points)	119.0	-136.4	-209.0	-142.4	-126.1	-115.8	-167.1	-153.1
Change of LCU/EUR rate, minus denotes euro depreciation (avg, %)	0.0	0.0	0.0	0.0	0.0	0.0	0.0	0.0
Fiscal balance, ESA'95 (% of GDP)	1.0	2.4	1.5	1.6	na	na	na	na
Public debt, ESA'95 (% of GDP)	5.5	6.0	5.4	4.8	5.2	5.0	4.8	na

Notes: Estonia has adopted currency board as exchange rate regime in 1992 and participates in ERM2 since 28 June 2004.

* The symbols in the line with S&P ratings denote the outlook, where S=stable, P=positive, N=negative.

Source: Eurostat, CSOs, CNBs, MoFs, ISI, Standard and Poor's.

Hungary	2002	2003	2004	2005	2Q 05	3Q 05	4Q 05	1Q 06
GDP growth, SNA (real, %, yoy)	3.8	3.4	5.2	4.1	4.5	4.5	4.3	4.6
Current account balance, (4Q cumulative, % of GDP)	-7.0	-8.7	-8.6	-7.4	-7.7	-7.7	-7.4	-7.4
FDI (4Q cumulative, % of GDP)	4.1	0.6	3.5	4.8	3.7	2.7	4.8	6.0
Total gross external debt (eop, % of GDP)	53.8	64.7	66.3	76.8	74.3	75.1	76.8	86.9
Change of international reserves in euro (eop, relative to previous period, %)	-18.7	2.2	15.4	34.3	6.2	2.7	7.9	13.4
Reserves-to-short-term debt ratio (eop, %)	218.5	152.5	159.3	157.5	162.1	164.1	157.5	193.0
Money Supply-to-Reserves ratio (eop, %)	334.8	330.1	340.5	282.5	292.5	292.1	282.5	251.2
Overall balance of state budget (4Q cumulative, % of GDP)	-8.7	-3.9	-4.4	-2.5	-4.0	-3.0	-2.5	-3.9
Credit to private sector (eop, % of GDP)	34.2	41.7	45.3	50.5	46.7	48.2	50.5	52.3
Growth rate of credit to the private sector (avg, %)	21.4	24.0	25.2	17.0	16.9	15.6	18.0	18.1
Foreign currency loans to the private sector (eop, % of loans to priv. sect.)	29.4	33.7	39.0	45.9	42.2	44.1	45.9	48.5
Non-performing loans (eop, % of total loans)	4.9	3.8	3.7	na	na	na	na	na
Short-term (3M) interest rates spreads to euro area (avg, basis points)	589.0	618.0	942.0	451.0	535.0	404.0	385.0	341.0
Change of stock exchange index (avg, relative to previous period, %)	12.5	8.1	39.8	61.9	4.7	22.6	-0.1	6.8
Long term foreign currency sovereign credit rating according to S&P's	A- (↔) (S)	A- (↔) (S)	A- (↔) (S)	A- (↔) (S)	A- (↔) (S)	A- (↔) (S)	A- (↔) (S)	A- (↔) (N?)
Maastricht indicators								
HICP 12M rolling average inflation relative to reference value (perc. points)	384.6	220.3	373.2	256.8	302.0	200.3	119.9	67.8
Convergence criterion bond yield relative to reference value (basis points)	-14.3	21.3	171.1	121.7	148.2	74.2	141.2	133.9
Change of LCU/EUR rate, minus denotes euro depreciation (avg, %)	-5.3	4.3	-0.7	-1.4	1.9	-1.7	2.6	1.1
Fiscal balance, ESA'95 (% of GDP)	na	na	na	na	na	na	na	na
Public debt, ESA'95 (% of GDP)	55.0	56.7	57.1	58.3	61.2	60.7	58.3	64.0

Notes: Hungary adopted peg to euro with +/-1% fluctuation band in May 2001.

Latvia	2002	2003	2004	2005	2Q 05	3Q 05	4Q 05	1Q 06
GDP growth, SNA (real, %, yoy)	6.5	7.2	8.5	10.2	11.2	11.4	10.6	13.1
Current account balance, (4Q cumulative, % of GDP)	-6.9	-8.1	-12.9	-12.4	-11.2	-11.1	-12.4	-13.3
FDI (4Q cumulative, % of GDP)	4.0	2.4	4.3	3.1	3.9	4.0	3.1	4.0
Total gross external debt (eop, % of GDP)	72.7	79.1	92.7	100.7	95.7	97.7	100.7	101.3
Change of international reserves in euro (eop, relative to previous period, %)	-8.5	-4.0	22.1	34.8	11.3	11.1	0.5	11.1
Reserves-to-short-term debt ratio (eop, %)	31.4	26.6	26.2	31.4	30.5	33.2	31.4	34.7
Money Supply-to-Reserves ratio (eop, %)	0.0	267.7	270.0	280.4	256.4	250.7	280.4	268.1
Overall balance of state budget (4Q cumulative, % of GDP)	-1.8	-1.6	-1.4	0.6	-0.1	-0.1	0.6	1.2
Credit to private sector (eop, % of GDP)	30.2	38.9	49.7	67.9	57.5	62.3	67.9	71.6
Growth rate of credit to the private sector (avg, %)	43.8	39.3	42.9	52.3	50.3	55.9	62.1	64.7
Foreign currency loans to the private sector (eop, % of loans to priv. sect.)	54.4	55.2	60.7	69.7	68.1	68.8	69.7	70.7
Non-performing loans (eop, % of total loans)	2.1	1.4	1.1	na	na	na	na	na
Short-term (3M) interest rates spreads to euro area (avg, basis points)	103.0	151.0	212.0	88.0	74.0	63.0	59.0	140.0
Change of stock exchange index (avg, relative to previous period, %)	13.3	22.4	36.0	50.3	8.9	11.0	19.6	3.2
Long term foreign currency sovereign credit rating according to S&P's	BBB (↔) (P?)	BBB+ (↑) (S↓)	BB+ (↔) (P?)	A- (↑) (S↓)	A- (↔) (S)	A- (↔) (S)	A- (↔) (S)	A- (↔) (S)
Maastricht indicators								
HICP 12M rolling average inflation relative to reference value (perc. points)	-30.4	-36.5	225.8	450.4	468.2	449.0	442.0	437.8
Convergence criterion bond yield relative to reference value (basis points)	-182.0	-170.9	-162.1	-150.7	-148.1	-126.1	-164.4	-185.1
Change of LCU/EUR rate, minus denotes euro depreciation (avg, %)	3.7	10.3	3.8	5.7	0.0	0.0	0.0	0.0
Fiscal balance, ESA'95 (% of GDP)	-2.3	-1.2	-0.9	0.2	na	na	na	na
Public debt, ESA'95 (% of GDP)	13.5	14.4	14.5	11.9	12.8	12.0	11.9	na

Notes: Latvia has *de facto* adopted currency board as exchange rate regime in 1994 (officially formalized in 1997) and participates in ERM2 since 29 April 2005.

Lithuania	2002	2003	2004	2005	2Q 05	3Q 05	4Q 05	1Q 06
GDP growth, SNA (real, %, yoy)	6.8	10.5	7.0	7.5	8.4	8.0	8.8	8.8
Current account balance, (4Q cumulative, % of GDP)	-5.1	-6.8	-7.7	-7.0	-6.5	-6.6	-7.0	-8.1
FDI (4Q cumulative, % of GDP)	5.0	0.8	2.3	2.6	2.6	2.6	2.6	2.4
Total gross external debt (eop, % of GDP)	39.5	40.6	42.5	50.8	46.5	49.1	50.8	53.2
Change of international reserves in euro (eop, relative to previous period, %)	22.2	19.3	-4.4	21.9	3.3	7.5	4.4	2.8
Reserves-to-short-term debt ratio (eop, %)	113.7	105.3	95.4	69.9	96.3	85.9	69.9	76.4
Money Supply-to-Reserves ratio (eop, %)	193.2	193.4	247.5	268.8	255.4	248.1	268.8	262.2
Overall balance of state budget (4Q cumulative, % of GDP)	-1.3	-1.2	-1.6	-1.0	-1.3	-0.7	-1.0	-0.2
Credit to private sector (eop, % of GDP)	15.8	22.4	28.4	41.1	32.0	35.0	41.1	44.0
Growth rate of credit to the private sector (avg, %)	27.4	42.4	52.1	40.4	37.6	44.3	54.4	68.6
Foreign currency loans to the private sector (eop, % of loans to priv. sect.)	49.7	53.6	57.2	64.9	60.4	62.0	64.9	64.2
Non-performing loans (eop, % of total loans)	5.8	2.6	2.4	na	na	na	na	na
Short-term (3M) interest rates spreads to euro area (avg, basis points)	42.0	51.0	57.0	24.0	29.0	19.0	8.0	3.0
Change of stock exchange index (avg, relative to previous period, %)	5.8	58.0	62.6	86.8	19.5	13.8	7.7	-10.6
Long term foreign currency sovereign credit rating according to S&P's	BBB (↑) (S)	BBB+ (↑) (P?)	A- (↑) (S↓)	A- (↔) (P?)	A- (↔) (P)	A- (↔) (P)	A- (↔) (P)	A- (↔) (P)
Maastricht indicators								
HICP 12M rolling average inflation relative to reference value (perc. points)	-148.0	-246.9	-207.1	11.4	31.3	29.0	19.4	7.8
Convergence criterion bond yield relative to reference value (basis points)	-116.6	-128.8	-197.6	-168.4	-152.8	-159.4	-168.1	-181.8
Change of LCU/EUR rate, minus denotes euro depreciation (avg, %)	-3.4	-0.2	0.0	0.0	0.0	0.0	0.0	0.0
Fiscal balance, ESA'95 (% of GDP)	-1.4	-1.2	-1.5	-0.5	na	na	na	na
Public debt, ESA'95 (% of GDP)	22.3	21.2	19.5	18.7	19.0	18.0	18.7	na

Notes: Lithuania has adopted currency board as exchange rate regime in 1994 and participates in ERM2 since 28 June 2004.

Poland	2002	2003	2004	2005	2Q 05	3Q 05	4Q 05	1Q 06
GDP growth, SNA (real, %, yoy)	1.4	3.8	5.3	3.4	2.9	3.9	4.3	5.2
Current account balance, (4Q cumulative, % of GDP)	-2.5	-2.1	-4.2	-1.4	-2.2	-1.5	-1.4	-1.5
FDI (4Q cumulative, % of GDP)	2.0	2.0	4.7	2.2	3.1	3.5	2.2	2.5
Total gross external debt (eop, % of GDP)	40.3	47.5	41.7	43.0	43.8	43.4	43.0	43.2
Change of international reserves in euro (eop, relative to previous period, %)	-5.4	-4.8	-0.5	33.4	15.8	0.0	5.3	1.6
Reserves-to-short-term debt ratio (eop, %)	214.7	174.1	151.5	166.8	180.2	168.8	166.8	175.8
Money Supply-to-Reserves ratio (eop, %)	281.5	266.1	335.9	297.0	283.7	299.8	297.0	290.3
Overall balance of state budget (4Q cumulative, % of GDP)	-4.9	-4.4	-4.5	-2.9	-4.2	-3.1	-2.9	-2.5
Credit to private sector (eop, % of GDP)	28.1	28.9	27.2	28.3	27.8	28.2	28.3	29.2
Growth rate of credit to the private sector (avg, %)	4.7	5.4	5.2	5.0	6.0	6.4	2.0	9.7
Foreign currency loans to the private sector (eop, % of loans to priv. sect.)	27.7	31.6	24.3	26.0	25.5	25.2	26.0	27.0
Non-performing loans (eop, % of total loans)	20.4	20.4	14.2	na	13.7	12.6	11.6	na
Short-term (3M) interest rates spreads to euro area (avg, basis points)	566.0	335.0	409.0	309.0	337.0	249.0	226.0	168.0
Change of stock exchange index (avg, relative to previous period, %)	0.4	18.2	41.1	22.6	0.3	15.5	8.1	15.0
Long term foreign currency sovereign credit rating according to S&P's	BBB+ (↔) (S)	BBB+ (↔) (N↓)	BBB+ (↔) (S↑)	BBB+ (↔) (S↑)	BBB+ (↔) (P)	BBB+ (↔) (P)	BBB+ (↔) (P)	BBB+ (↔) (P)
Maastricht indicators								
HICP 12M rolling average inflation relative to reference value (perc. points)	42.2	-158.3	-20.7	105.6	166.3	83.8	-1.0	-92.2
Convergence criterion bond yield relative to reference value (basis points)	12.8	-83.3	41.8	-16.4	-10.1	-40.8	-16.8	-60.8
Change of LCU/EUR rate, minus denotes euro depreciation (avg, %)	5.1	14.1	3.1	-11.3	2.6	-2.7	-2.6	-2.1
Fiscal balance, ESA'95 (% of GDP)	-3.2	-4.7	-3.9	-2.4	na	na	na	na
Public debt, ESA'95 (% of GDP)	39.8	43.9	41.8	41.9	43.3	41.9	41.9	0.0

Notes: Poland has adopted "pure" free floating as exchange rate regime in April 2000.

Slovakia	2002	2003	2004	2005	2Q 05	3Q 05	4Q 05	1Q 06
GDP growth, SNA (real, %, yoy)	4.1	4.2	5.4	6.1	5.4	6.3	7.4	6.3
Current account balance, (4Q cumulative, % of GDP)	-7.8	-0.8	-3.4	-8.6	-5.6	-5.5	-8.6	-9.8
FDI (4Q cumulative, % of GDP)	16.8	2.2	3.3	3.7	3.3	3.7	3.7	4.6
Total gross external debt (eop, % of GDP)	47.5	49.1	50.0	58.7	81.7	59.5	58.7	59.1
Change of international reserves in euro (eop, relative to previous period, %)	61.5	9.7	13.8	24.6	-7.5	2.0	3.7	14.4
Reserves-to-short-term debt ratio (eop, %)	264.8	186.3	171.3	125.1	134.6	132.8	125.1	159.5
Money Supply-to-Reserves ratio (eop, %)	188.7	185.7	177.6	168.1	156.1	155.2	168.1	151.4
Overall balance of state budget (4Q cumulative, % of GDP)	-4.6	-4.6	-5.2	-2.3	-4.2	-3.4	-2.3	-2.4
Credit to private sector (eop, % of GDP)	32.0	31.0	29.7	35.0	32.0	33.5	35.0	36.3
Growth rate of credit to the private sector (avg, %)	-1.6	8.3	9.7	15.7	14.9	19.7	21.5	22.1
Foreign currency loans to the private sector (eop, % of loans to priv. sect.)	17.1	18.8	21.5	22.3	22.7	22.3	22.3	21.0
Non-performing loans (eop, % of total loans)	11.2	9.1	7.2	na	na	7.7	na	na
Short-term (3M) interest rates spreads to euro area (avg, basis points)	445.0	385.0	257.0	74.0	61.0	79.0	77.0	81.0
Change of stock exchange index (avg, relative to previous period, %)	14.1	40.7	29.8	104.9	11.2	5.4	-6.2	-6.1
Long term foreign currency sovereign credit rating according to S&P's	BBB (↑) (P)	3BB (↔) (P)	BB+ (↑) (P)	A- (↔) (P)	A- (↔) (P)	A- (↔) (P)	A (↔) (S)	A (↔) (S)
Maastricht indicators								
HICP 12M rolling average inflation relative to reference value (perc. points)	238.4	330.9	607.0	226.0	283.8	136.1	48.8	41.1
Convergence criterion bond yield relative to reference value (basis points)	-29.3	-162.4	-145.3	-186.0	-179.8	-193.4	-179.4	-166.8
Change of LCU/EUR rate, minus denotes euro depreciation (avg, %)	-1.4	-2.8	-3.5	-3.6	1.6	-0.6	-0.5	-2.7
Fiscal balance, ESA'95 (% of GDP)	-7.7	-3.7	-3.0	-2.9	na	na	na	na
Public debt, ESA'95 (% of GDP)	43.3	42.7	41.6	34.5	35.2	34.7	34.5	0.0

Notes: Slovakia adopted managed float regime with the euro as the main reference currency in October 1998 and participates in ERM2 since 28 November 2005.

Slovenia	2002	2003	2004	2005	2Q 05	3Q 05	4Q 05	1Q 06
GDP growth, SNA (real, %, yoy)	3.5	2.7	4.2	3.9	5.4	3.6	3.7	5.1
Current account balance, (4Q cumulative, % of GDP)	1.5	-0.3	-2.1	-1.1	-1.4	-0.8	-1.1	-1.1
FDI (4Q cumulative, % of GDP)	6.5	-0.5	0.8	-0.1	0.0	-0.1	-0.1	0.2
Total gross external debt (eop, % of GDP)	49.4	54.0	58.6	71.5	63.4	68.0	71.5	73.6
Change of international reserves in euro (eop, relative to previous period, %)	36.1	1.4	-4.9	5.4	2.6	1.9	0.0	0.4
Reserves-to-short-term debt ratio (eop, %)	295.3	281.0	248.6	179.6	215.6	198.7	179.6	180.0
Money Supply-to-Reserves ratio (eop, %)	230.7	232.2	257.3	257.9	248.9	251.6	257.9	260.9
Overall balance of state budget (4Q cumulative, % of GDP)	-2.6	-1.2	-1.3	-1.4	-1.9	-1.0	-1.4	-1.3
Credit to private sector (eop, % of GDP)	40.0	42.8	47.8	56.9	51.7	53.8	56.9	58.2
Growth rate of credit to the private sector (avg, %)	13.5	13.2	18.8	23.7	24.3	23.5	24.2	30.2
Foreign currency loans to the private sector (eop, % of loans to priv. sect.)	22.6	27.1	33.1	44.5	38.4	40.9	44.5	47.3
Non-performing loans (eop, % of total loans)	10.0	9.4	7.5	na	na	na	na	na
Short-term (3M) interest rates spreads to euro area (avg, basis points)	471.0	445.0	255.0	184.0	193.0	190.0	167.0	118.0
Change of stock exchange index (avg, relative to previous period, %)	50.5	18.7	35.0	2.6	-6.9	-3.0	0.8	0.1
Long term foreign currency sovereign credit rating according to S&P's	A (↔) (P↑)	A+ (↑) (P)	AA- (↑) (S↓)	AA- (↔) (S)	AA- (↔) (S)	AA- (↔) (S)	AA- (↔) (S)	A+ (↔) (P↑)
Maastricht indicators								
HICP 12M rolling average inflation relative to reference value (perc. points)	497.2	406.3	217.3	65.5	89.1	35.9	9.4	-22.2
Convergence criterion bond yield relative to reference value (basis points)	3.2	-20.8	-179.5	-157.5	-142.8	-136.1	-167.4	-170.1
Change of LCU/EUR rate, minus denotes euro depreciation (avg, %)	4.2	3.3	2.2	0.3	-0.1	0.0	0.0	0.0
Fiscal balance, ESA'95 (% of GDP)	-2.7	-2.8	-2.3	-1.8	na	na	na	na
Public debt, ESA'95 (% of GDP)	29.7	29.1	29.5	29.1	28.9	28.2	29.1	0.0

Notes: Slovenia has *de facto* adopted crawling band as exchange rate regime in 1992 (*de jure* - managed float) and participates in ERM2 since 28 June 2004.