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Transition Countries Resist Global Slowdown: Productivity Gains Offset Effects of Appreciation

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Leon Podkaminer, Vasily Astrov, Helen Boss Heslop, Vladimir Gligorov, Gábor Hunya, Zdenek Lukas, Josef Pöschl, Sándor Richter and Hermine Vidovic are wiiw research economists. Peter Havlik is wiiw Deputy Director.

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Executive summary

After satisfactory performance of the transition countries in 2000, their growth slowed down in 2001 as the external conditions deteriorated. This tendency was checked in the second half of 2002. Industrial production and exports have generally strengthened since then – though in some countries apparently only temporarily. Expanding consumption was the major factor supporting growth in the year 2002 as the capital formation was generally weak in the more advanced countries and only moderately strong in the less advanced ones.

The contribution of foreign trade to GDP growth in 2002 seems on the whole positive, excepting Russia and most post-Yugoslav countries. Despite weak growth in the EU, exports of the accession countries (and of Ukraine) performed quite well. This must be attributed to the ongoing growth in labour productivity and related cost improvements in industry which kept exports competitive. Gains in labour productivity are generally associated with some cuts in employment, adding to unemployment which is generally high, or very high, and unlikely to go down significantly even in the medium run.

There has been a continuous decline in inflation. In most cases the disinflation is gradual and appears to be little affected by the monetary and fiscal policies. Inertial cost–price adjustments are likely to continue in the foreseeable future. The remarkable strength of the national currencies appears to have had a fairly limited impact on the performance of trade and production so far. The recent years' exchange rate trends may have reflected financial (or even speculative) developments so that a potential for adjustments, involving devaluation, may be there. But the likelihood of major adjustments seems rather small because the solid capital inflows will continue even in the medium term, especially in view of the prospective EU membership of the candidate countries. The general concern over potential loss of competitiveness due to overvaluation remains still valid. However, the productivity and efficiency gains may offset the negative consequences of real appreciation and the process has been associated with quality and price gains in export activities. It is not clear yet how sustainable the process of productivity improvements will be. Most probably high levels of investment (including green-field FDI) are needed to maintain its momentum.

Growth acceleration in 2003-04 is possible provided the business climate in the EU improves. Otherwise growth rates will be roughly the same as in 2002. In any case the average rate of catching-up vis-à-vis the EU will stay at about 2 percentage points per year.

Keywords: *Central and East European transition countries, Bulgaria, Croatia, Czech Republic, Hungary, Macedonia, Poland, Romania, Russia, Slovakia, Slovenia, Ukraine, Yugoslavia (Serbia and Montenegro), forecast, East-West trade, European Union, EU enlargement, exchange rates*

JEL classification: *O52, O57, P24, P27, P33, P52*

Figure I: Gross domestic product

real change in % against preceding year

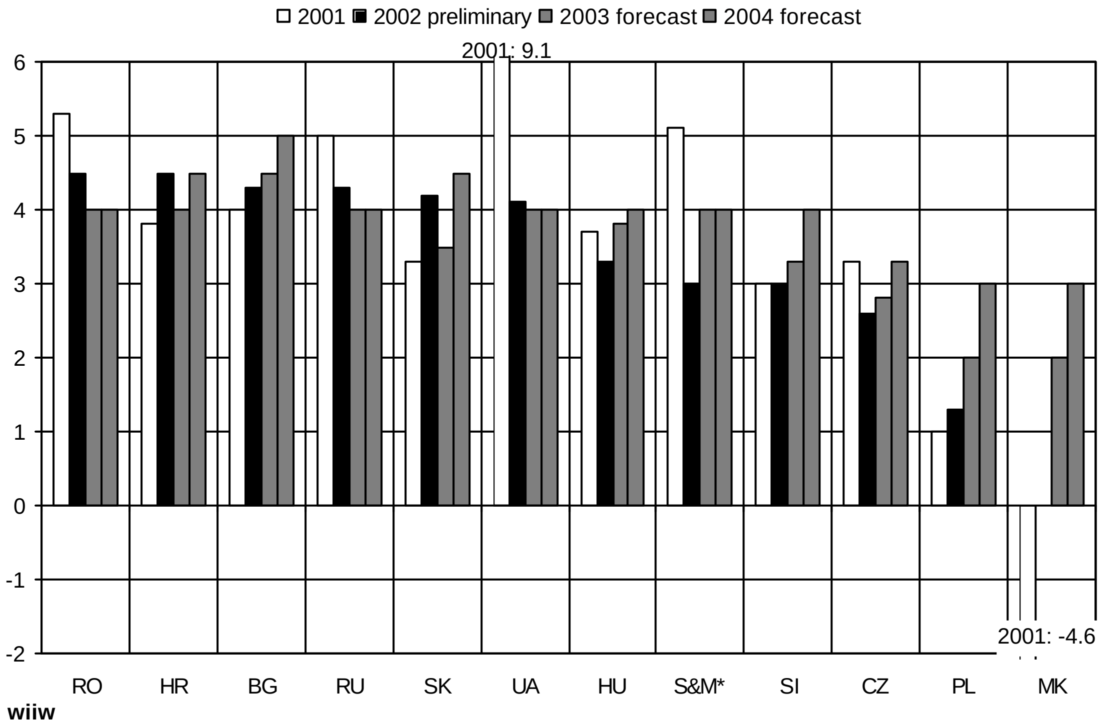
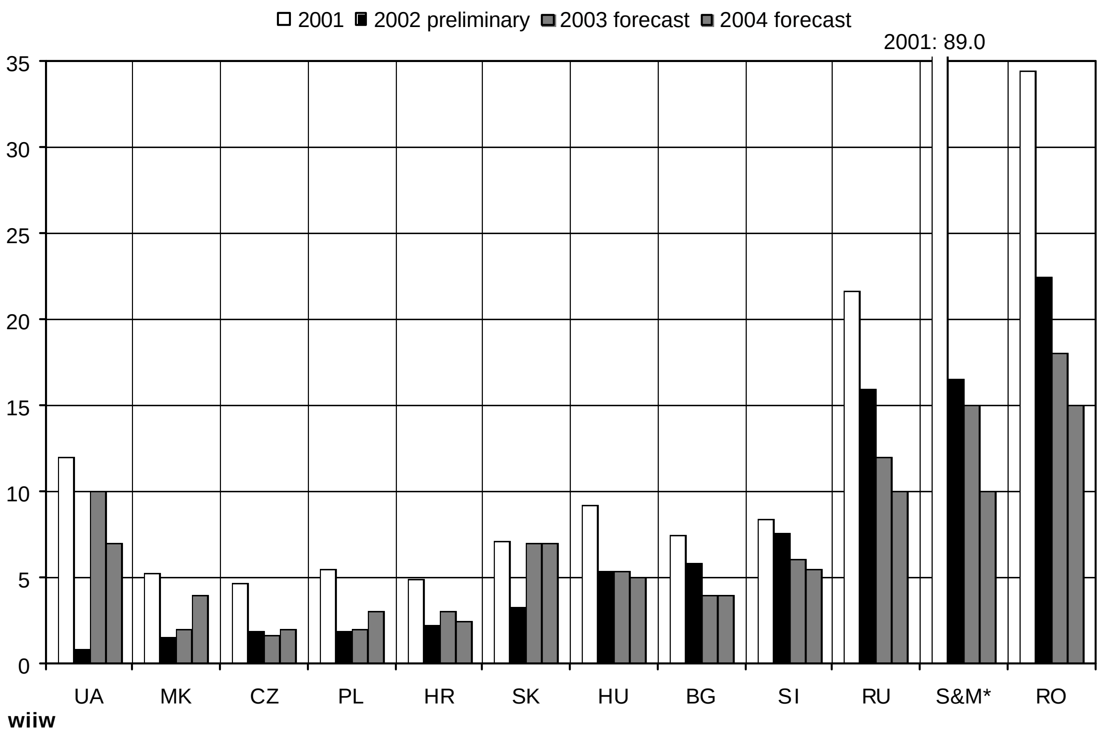


Figure II: Consumer price inflation

annual change in % against preceding year



*) S&M: Serbia & Montenegro

OVERVIEW

Leon Podkaminer *

Transition Countries Resist Global Slowdown: Productivity Gains Offset the Effects of Appreciation

Limited impacts of the EU growth slowdown

The marked slowdown of GDP growth, which generally set in around the second quarter of 2001, continued well into 2002 in most transition countries. This was commonly considered quite consistent with the growth slowdown in the EU and the resultant weakening of the EU import demand, and also consistent with the ongoing real appreciation of the CEE countries' currencies vs. the euro. In the second half of 2002 the EU economy remained depressed, with Germany, by far the largest single trading partner of the transition countries, heading towards recession. Rather unexpectedly, and despite the effects of continuing real appreciation, the transition countries most dependent on trade with the EU managed to maintain (and in some cases even to accelerate) their GDP growth in 2002 (Table 1, Figures 1a-1b). Moreover, foreign trade in goods and services does not seem to have had adverse effects on the overall growth in all accession countries (Bulgaria, the Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania, Slovakia and Slovenia). In contrast, in Russia, Yugoslavia and Macedonia, all of which are less dependent on trade with the EU, the contribution of foreign trade to GDP growth appears definitely negative. Although no precise estimates are currently available to evaluate the effects of the balance of foreign trade in goods and services on GDP growth in 2002, there are good reasons to believe that these impacts were generally positive in the accession countries. In particular, exports of goods performed quite well, with imports of goods rising at lower rates, at least in current euro terms. Apparently, the close dependence of the accession countries on trade with the EU does not automatically condemn them to stagnation even when growth in the EU is very weak. The poor business climate in the EU does not have to worsen the accession countries' trade deficits. Of course, this does not imply than those transition countries which are not yet integrating with the EU are somehow more vulnerable to the shocks hitting the EU. The experiences of Russia, Yugoslavia (Serbia and Montenegro) and Macedonia are different, for quite specific reasons which have relatively little to do with what goes on in the EU. In Yugoslavia (Serbia and Montenegro) and Macedonia the rising trade deficits reflect the ongoing reconstruction efforts, obsolescence of industrial equipment and acute supply-side

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bottlenecks. In Russia the contribution of foreign trade to the GDP growth was probably negative primarily because of continuing real appreciation and the resulting rise in imports.

Table 1

Gross domestic product

real change in % against preceding year

	1995	1996	1997	1998	1999	2000	2001	2002 [1]	2003 forecast	2004 forecast	Index 1990=100 2002	Index 1995=100 2002
Czech Republic	5.9	4.3	-0.8	-1.0	0.5	3.3	3.3	2.6	2.8	3.3	107.2	112.6
Hungary	1.5	1.3	4.6	4.9	4.2	5.2	3.7	3.3	3.8	4	115.6	130.4
Poland	7.0	6.0	6.8	4.8	4.1	4.0	1.0	1.3	2	3	146.4	131.4
Slovak Republic	6.5	5.8	5.6	4.0	1.3	2.2	3.3	4.2	3.5	4.5	111.6	129.5
Slovenia	4.1	3.5	4.6	3.8	5.2	4.6	3.0	3	3.3	4	127.4	131.1
CEEC-5 [2]	5.7	4.7	4.7	3.5	3.2	3.9	2.2	2.2	2.7	3.4	128.3	127.2
Bulgaria	2.9	-9.4	-5.6	4.0	2.3	5.4	4.0	4.3	4.5	5	87.9	104.0
Romania	7.1	3.9	-6.1	-4.8	-1.2	1.8	5.3	4.5	4	4	92.3	102.8
CEEC-7 [2]	5.8	3.8	2.5	2.4	2.5	3.7	2.7	2.7	3.0	3.6	119.6	122.2
Croatia	6.8	5.9	6.8	2.5	-0.9	2.9	3.8	4.5	4	4.5	92.9	128.2
Macedonia	-1.1	1.2	1.4	3.4	4.3	4.5	-4.6	0	2	3	87.0	110.4
Serbia & Montenegro [3]	6.1	5.9	7.4	2.5	-17.7	6.4	5.1	3	4	4	53.0	110.4
Russia	-4.1	-3.4	0.9	-4.9	5.4	9.0	5.0	4.3	4	4	72.4	116.6
Ukraine	-12.2	-10.0	-3.0	-1.9	-0.2	5.9	9.1	4	4	4	49.1	102.7
Estonia	4.3	3.9	9.8	4.6	-0.6	7.1	5.0	5.3	5.5	5.5	97.4	140.5
Latvia	-0.8	3.3	8.6	3.9	1.1	6.8	7.6	5.3	6	6	70.7	142.6
Lithuania	3.3	4.7	7.3	5.1	-3.9	3.8	5.9	5.8	5.5	5.7	76.5	131.9
Armenia	6.9	5.9	3.3	7.3	3.3	6	9.6	12.5	.	.	83.7	158.5
Azerbaijan	-11.8	1.3	5.8	10	7.4	11.1	9.9	10.4	.	.	71.4	170.7
Belarus	-10.4	2.8	11.4	8.4	3.4	5.8	4.1	4.3	.	.	95.3	147.5
Georgia	2.6	11.2	10.6	2.9	3	2	4.5	4.1	.	.	40.9	144.6
Kazakhstan	-8.2	0.5	1.7	-1.9	2.7	9.8	13.2	9.4	.	.	86.0	140.0
Kyrgyzstan	-5.4	7.1	9.9	2.1	3.7	5.4	5.3	-1.7	.	.	68.9	136.0
Moldova	-1.9	-5.9	1.6	-6.5	-3.4	2.1	6.1	5.9	.	.	38.9	99.1
Tajikistan	-12.4	-16.7	1.7	5.3	3.7	8.3	10.2	8.5	.	.	69.1 [4]	119.8
Turkmenistan	-7.7	0.1	.	.	.	.	.	.	.	.	.	.
Uzbekistan	-0.9	1.7	5.2	4.4	4.4	4.0	4.5	3	.	.	106.0	130.5
CIS	-5.3	-3.2	1.0	-3.6	4.6	8.3	6.0	4.5	.	.	70.2	118.3

Notes: 1) Preliminary. - 2) **wiiw** estimate. - 3) Gross Material Product. - 4) 1992 = 100.

Source: **wiiw** Database incorporating national statistics, forecast: **wiiw**.

Figure 1a: Quarterly GDP growth rates

in %, year-on-year

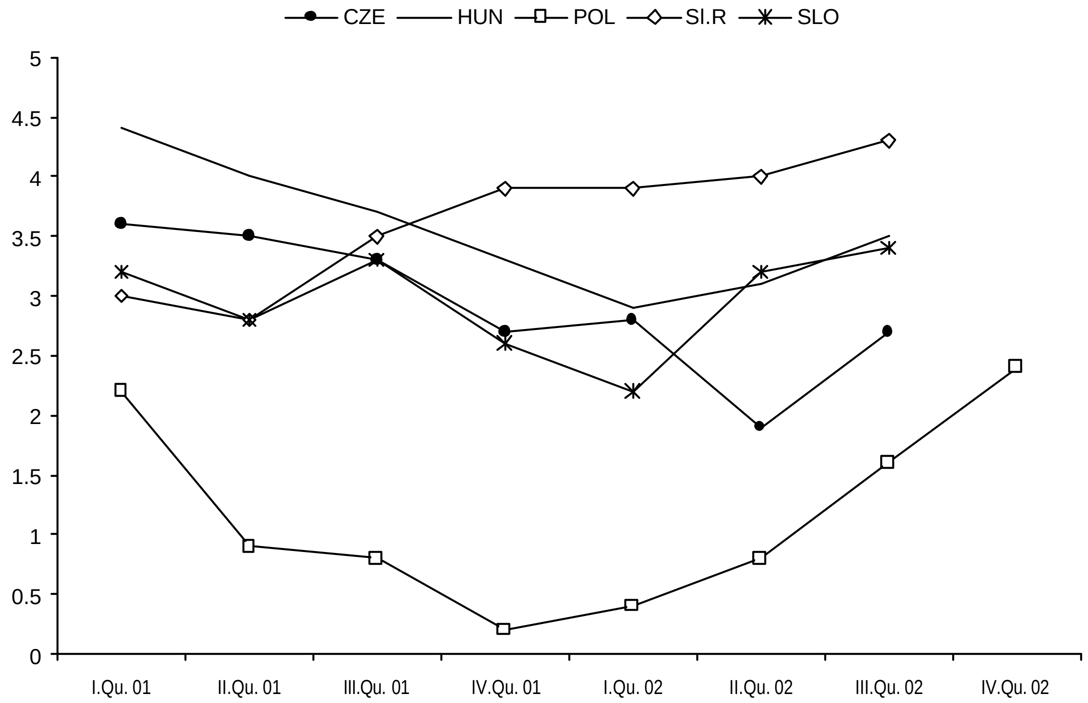
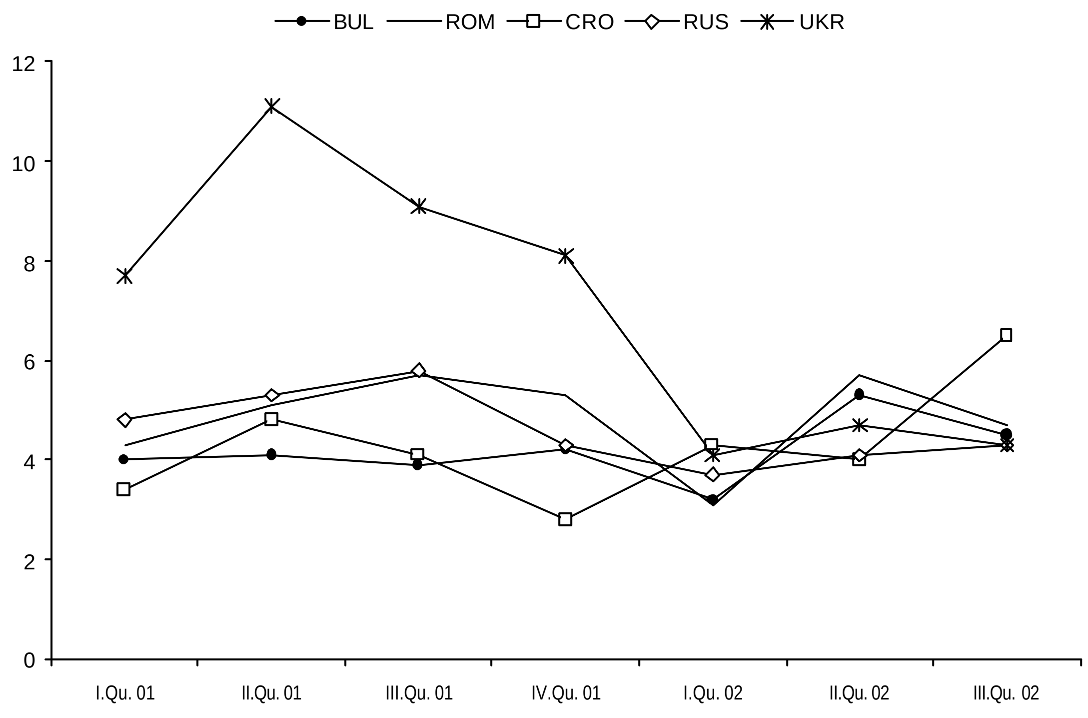


Figure 1b: Quarterly GDP growth rates

in %, year-on-year



Source: **wiiw** Monthly Database incorporating national statistics.

Rising private consumption supported the GDP growth everywhere. In Poland it was the rising consumption expenditure out of stagnating household income which turned out to be the major factor preventing recession in 2002. In Russia, rapidly growing incomes of the population and strongly expanding private consumption were the main factors behind the GDP growth.

Changes in fiscal stances of the public sector were, in most cases, rather insignificant and their overall impacts on GDP growth seem generally neutral, if not negative – and in any case negligible. Although the ratios of fiscal deficits to GDP became larger (and the fiscal surplus in Russia smaller), fiscal policies were not expansionary because rising deficits primarily reflected rising expenditure on public debt servicing or the consolidation of debts of the troubled public sector and could not stimulate aggregate demand perceptibly. There are two exceptions though: Slovakia and Hungary. Both countries held parliamentary elections in 2002. These occasioned shows of 'generosity' in the form of higher wages to the employees of the public service sectors or higher subsidies (e.g. delayed adjustments in regulated prices of energy, rents etc.). Only in these two countries did the fiscal policy have some positive, even if temporary, impact on GDP growth in 2002.

Gross fixed capital formation higher among the erstwhile 'laggards'

The contribution of gross capital formation to GDP growth varied from country to country. Generally, however, that contribution was of secondary importance in most countries in 2002 as investment growth was low at best.

Investment in fixed assets continued to fall precipitously in Poland, and its rise in Russia and Slovakia was very weak (Table 2). After two years of virtual stagnation there was a modest revival of investment in Slovenia. The quite strong rise in investment in Hungary did not represent a change of private investors' moods but the expansion of public investment in infrastructure. (Rising public investment was here also a part of the pre-election 'economics'). Investment rose fairly strongly in the erstwhile 'laggards' among the transition countries: Romania, Bulgaria, Croatia and Ukraine.

The current levels of gross fixed capital formation are still very low, compared to 1990, in Russia, Ukraine, Croatia, Yugoslavia (Serbia and Montenegro) and Macedonia. This suggests that the GDP growth in these countries may be thwarted by shortages of production capacities capable of supplying goods and services competitively. Sustained high investments are badly needed, especially in Ukraine and Russia. A continuing fall in real interest rates is only one condition for a revival of private sector investment on a meaningful scale. But much more is still needed. In the first place there is a need to consolidate old bad debts accumulated in firms and banks during the protracted period of disinflation. The recovery of private investment in Bulgaria and Romania may at least in part be attributed to the ongoing attempts to sort out the problems over bad debts. Besides, the overall institutional and legal framework must be overhauled. Investment is likely to remain depressed as long as property rights and administrative rules remain unclear, laws are applied selectively and regulations are relatively easy to manipulate. In this respect much remains to be done especially in Russia and Ukraine. Finally, the expansion of private investment (and the attraction of FDI in particular) usually requires rather substantial state-financed investment in infrastructure. This truth is quite well understood in the Czech Republic, Slovakia and Slovenia (which have attracted many green-field FDI projects recently) – but not yet fully elsewhere.

Table 2

Gross fixed capital formation

real change in % against preceding year

	1995	1996	1997	1998	1999	2000	2001	2002 1)	2003 forecast	2004 forecast	Index 1990=100 2002	Index 1995=100 2002
Czech Republic	19.8	8.2	-2.9	0.7	-1.0	5.4	7.2	0.9	2	5	132.3	119.3
Hungary	-4.3	6.7	9.2	13.3	5.9	7.7	3.1	6	7.5	8	157.6	164.4
Poland	16.5	19.7	21.7	14.2	6.8	2.7	-8.8	-7.2	.	.	197.6	154.4
Slovak Republic	1.8	30.9	14.3	11.0	-18.5	1.2	9.6	1	5	7	101.9	151.7
Slovenia	16.8	8.9	11.6	11.3	19.1	0.2	-1.9	3.5	4	5	186.6	163.9
Bulgaria	16.1	-21.2	-20.9	35.2	20.8	15.4	19.9	7.4	.	.	108.9	151.3
Romania	7.0	5.7	1.7	-5.7	-4.8	4.6	6.6	8	5	5	123.2	116.1
Croatia	.	37.6	26.4	2.5	-3.9	-3.8	9.7	10	7	6	28.6	198.9
Macedonia	10.2	6.5	-4.3	-2.6	-1.4	-3.2	.	.	.	.	70.3 3)	94.8 3)
Serbia & Montenegro 2)	-3.7	-5.7	0.8	-2.2	-29.7	13.3	.	.	.	.	23.4 3)	74.1 3)
Russia 2)	-10.0	-18.0	-5.0	-12.0	5.3	17.7	8.7	2.6	5	7	29.2	94.8
Ukraine 2)	-35.1	-22.0	-8.8	6.1	0.4	14.4	20.8	6.2	10	15	29.3	111.1

Notes: 1) Preliminary. - 2) Gross fixed investment. - 3) Year 2000.

Source: **wiiw** Database incorporating national statistics, forecast: **wiiw**.

High FDI inflows to the Czech Republic and Slovakia

FDI inflows to most transition countries were much lower in 2002 than in earlier years. This may be attributed to several factors. Generally, the FDI flows were lower world-wide, reflecting the overall deterioration of the business climate and mounting uncertainties. In some transition countries (notably Poland and Hungary) the supply of privatization deals which would be potentially attractive to foreign investors was definitely lower, for various reasons. Both countries have seen some revival of populist-nationalistic opposition to sales of 'family silver' to foreigners. Besides, despite urgent budgetary needs, it made sense to delay some privatization deals until prices become stronger.

Table 3

Foreign direct investment inflow

based on the balance of payments, USD million

	1994	1995	1996	1997	1998	1999	2000	2001	2002 I-IX	2002 estimate	2003 estimate
Czech Republic	869	2562	1428	1300	3718	6324	4986	4916	7068	8000	4000
Hungary	1147	4453	2275	2173	2036	1970	1649	2443	835	1600	1600
Poland	1875	3659	4498	4908	6365	7270	9341	5713	.	4000	4000
Slovak Republic	273	258	358	220	684	390	1925	1475	3391	4000	2000
Slovenia	117	151	174	334	216	107	136	503	1110	2000	2000
Total (5)	4280	11083	8732	8936	13018	16061	18038	15051	.	19600	13600
Bulgaria	105	90	109	505	537	819	1002	694	289	400	600
Romania	341	419	263	1215	2031	1041	1037	1157	741	900	1000
Total (7)	4727	11593	9104	10656	15587	17921	20076	16902	.	20900	15200
Estonia	215	202	151	267	581	305	387	542	223	300	400
Latvia	213	178	382	521	357	348	410	155	349	400	400
Lithuania	31	73	152	355	926	486	379	446	577	600	400
Total (10)	5185	12045	9789	11798	17450	19060	21252	18045	.	22200	16400
Croatia	117	121	516	568	1018	1641	1140	1499	742	1000	1000
Macedonia	24	9	11	16	118	32	175	443	67	100	500
Bosnia & Herzegovina	.	.	.	.	100	90	150	130	.	200	200
Serbia & Montenegro	.	.	.	740	113	112	50	165	310	400	500
Russia	690	2065	2579	4865	2761	3309	2714	2469	1829	2500	2500
Ukraine	159	267	521	623	743	496	595	792	392	500	500

Source: National Banks of the respective countries according to balance of payments statistics.

Table 4

Foreign direct investment stock

USD million

	1994	1995	1996	1997	1998	1999	2000	2001	2002 Sept	2002 estimate
Czech Republic	4547	7350	8572	9234	14375	17552	21644	26764	35992	37000
Hungary	7095	11926	14961	16086	18517	19299	19804	23562	27837	27000
Poland	3789	7843	11463	14587	22479	26075	34227	41031	.	46000
Slovak Republic	897	1297	2046	2083	2890	3188	4746	5582	.	10000
Slovenia	1326	1763	1998	2207	2777	2682	2893	3209	.	5500
Total (5)	17654	30180	39040	44197	61038	68797	83314	100148	.	125500
Bulgaria	247	337	446	951	1488	2307	3309	4003	4292	4400
Romania	552	971	1234	2449	4480	5521	6558	7715	8456	8600
Total (7)	18453	31488	40720	47597	67007	76625	93180	111866	.	138500
Estonia	495	737	838	1148	1822	2467	2645	3160	3889	3600
Latvia	309	616	936	1272	1558	1795	2084	2332	2746	3000
Lithuania	310	352	700	1041	1625	2063	2334	2666	3564	3600
Total (10)	19566	33191	43195	51057	72011	82950	100243	120023	.	148700
Croatia	238	359	874	1443	2460	4102	5241	6741	7482	7700
Macedonia	24	33	45	60	178	210	386	829	896	900
Bosnia & Herzegovina	.	.	.	.	100	190	340	470	.	700
Serbia & Montenegro	.	.	.	740	853	965	1015	1180	1490	1600
Russia	1901	3966	6545	11410	14171	17480	20194	22663	24492	25000
Ukraine	529	796	1317	1940	2683	3179	3774	4566	4958	5000

Source: For Czech Republic, Hungary, Poland, Slovak Republic, Slovenia, Croatia, Estonia, Latvia, Lithuania: National Banks of the respective countries according to international investment position. For Bulgaria, Romania, Macedonia, Bosnia & Herzegovina, Serbia & Montenegro, Russia, Ukraine: cumulated US dollar inflows based on Table 3.

FDI inflows to Slovenia, Slovakia and the Czech Republic increased strongly in 2002. The privatization deals completed in Slovenia had been carefully planned for a long time. Thus the rise in FDI in Slovenia does not represent any break with the past policy of a rather discriminate approach to foreign capital inflows. The very high FDI inflows to Slovakia and the Czech Republic materialize not only on account of huge privatization deals (involving primarily the utilities) but also because of a number of large green-field investment projects (e.g. in the automotive and electronics industries). Both countries appear attractive for several reasons such as long industrial traditions and the abundance of skilled and disciplined labour force. Perhaps most important is their geographical location (closest to the core EU markets), and excellent (compared to e.g. Poland's) transportation networks.

Table 5

Branch-specific effects of FDI Penetration (year 1999) **on output and productivity growth and Unit Labour Costs improvements in CEECs' manufacturing** (1993-1999)

Model 1: Ln(output growth) = constant + b * Ln(FDI)						
Regression with robust standard errors				Number of obs = 96		
				F(7, 88) = 8.82		
				Prob > F = 0.0000		
				R-squared = 0.2444		
				Root MSE = .56793		
Ln(output growth)	Coefficient	Robust std. error	t	P > |t|	(95% confidence interval)	
Ln(FDI)	.0960262	.047664	2.01	0.047	.0013041	.1907484
constant	4.417662	.394494	11.20	0.000	3.633687	5.201637
Model 2: Ln(productivity) = constant + b * ln(FDI)						
Regression with robust standard errors				Number of obs. = 96		
				F (7, 88) = 4.34		
				Prob > F = 0.0004		
				R-squared = 0.2540		
				Root MSE = .39053		
Ln(productivity)	Coefficient	Robust std. error	t	P > |t|	(95% confidence interval)	
Ln(FDI)	.0810696	.0334910	2.42	0.018	.0145132	.1476259
constant	4.488041	.2753069	16.30	0.000	3.940926	5.035155
Model 3: Ln(ULC) = constant + b * ln(FDI)						
Regression with robust standard errors				Number of obs. = 96		
				F (7, 88) = 36.45		
				Prob > F = 0.0000		
				R-squared = 0.7447		
				Root MSE = .35844		
Ln(ULC)	Coefficient	Robust std. error	t	P > |t|	(95% confidence interval)	
Ln(FDI)	-.0476279	.0271675	-1.75	0.083	-.1016175	-.0063617
constant	5.013555	.2238641	22.40	0.000	4.568674	5.458436

Note: Huber-White robust estimators were used. Results for country-specific dummies are not reported. Industry-specific dummies were not statistically significant. (For more details see P. Havlik, 'Restructuring of manufacturing industry in the Central and East European countries', *Prague Economic Papers,* forthcoming.)

The relatively high FDI stocks accumulating in individual accession countries certainly improve their overall production efficiency. Manufacturing branches with high FDI penetration levels are rightly expected to contribute to quality and productivity upgrading and hence to competitive gains on international as well as domestic markets (Table 5). Some of the recent foreign trade improvements (and in particularly export gains in the transport, optical and electrical equipment industries) are definitely due to new FDI factories starting production and exports on a large scale.[1]

Industrial production: strong gains in labour productivity

Growth of industrial production weakened quite dramatically in the first quarter of 2002 in all transition countries, except the Czech Republic. In Poland, Bulgaria, Macedonia, Ukraine and Yugoslavia (Serbia and Montenegro) industrial production even contracted and in Hungary it came to a standstill. Later in the year growth resumed and in some cases strengthened considerably. Nonetheless, generally growth remained less stable and much weaker than in 'good' years such as 2000, for most countries (Tables 6 and 7).

Table 6

Industrial output – growth rate year-on-year[1)], 2001-2002

	Q1 01	Q2 01	Q3 01	Q4 01	Q1 02	Q2 02	Q3 02	Q4 02	Oct-02	Nov-02	Dec-02
Czech Republic	10.0	7.3	4.5	4.8	4.2	4.8	5.7	4.0	3.5	4.4	.
Hungary	10.6	6.2	-1.3	0.7	-0.3	1.3	5.5	1.6	-0.8	4.0	.
Poland	4.6	-0.5	-0.5	-1.4	-1.4	-0.6	3.7	3.9	3.3	3.1	5.1
Slovakia	8.0	8.0	7.4	4.7	1.1	5.9	9.4	8.9	8.7	9.1	.
Slovenia	4.9	2.2	2.7	2.5	1.9	2.6	3.8	1.1	1.5	0.6	.
Bulgaria	7.9	1.9	6.6	-1.5	-1.8	7.9	7.1	4.1	0.6	11.0	0.8
Romania	11.1	10.1	4.3	7.7	3.3	4.1	8.2	8.3	9.6	7.0	.
Croatia	6.0	6.4	6.1	6.0	2.1	2.6	8.2	9.2	9.4	9.9	8.3
Russia	5.2	5.9	4.5	4.1	2.6	3.8	5.6	2.6	3.9	0.8	3.2
Ukraine	15.5	18.4	11.5	-2.5	-0.2	.	.	.	.	.	.

Notes: 1) Quarterly data are averages of monthly rates. The Q4 average covers as many months as available.
Source: **wiiw** Monthly Database incorporating national statistics.

The course of industrial production seems to reflect the foreign trade performance (primarily of exports) and the investment activities. A slight deflationary tendency (with respect to industrial producer prices) was present in several countries (the Czech Republic,

[1] The impacts of FDI on productivity and costs are researched extensively by wiiw – see *wiiw Research Reports* Nos. 273, 278 and especially No. 279

Table 7

Gross industrial production

real change in % against preceding year

	1995	1996	1997	1998	1999	2000	2001	2002 1)	2003 forecast	2004 forecast	Index 1990=100 2002	Index 1995=100 2002
Czech Republic	8.7	2.0	4.5	1.6	-3.1	5.4	6.5	4.6	4.7	6	94.0	123.2
Hungary	4.6	3.4	11.1	12.5	10.4	18.1	3.6	2.6	7	9	160.9	179.2
Poland 2)	9.7	8.3	11.5	3.5	3.6	6.7	0.3	1.5	2	2	174.0	140.7
Slovak Republic	8.3	2.5	2.7	5.0	-2.7	8.6	6.9	6.3	5.5	6	105.8	132.7
Slovenia	2.0	1.0	1.0	3.7	-0.5	6.2	2.9	2.4	3	3	94.5	117.8
CEEC-5 3)	8.2	5.1	8.5	4.6	2.3	8.4	3.0	2.9	3.8	4.5	137.9	140.1
Bulgaria	4.5	5.1	-5.4	-7.9	-9.3	10.3	-2.4	2.6	4	5	62.2	91.7
Romania	9.4	6.3	-7.2	-13.8	-2.4	7.1	8.2	6	4	4	70.3	101.9
CEEC-7 3)	8.3	5.3	5.6	1.4	1.1	8.3	3.5	3.3	3.8	4.4	118.5	131.9
Croatia	0.3	3.1	6.8	3.7	-1.4	1.7	6.0	5.4	4	5	71.7	127.9
Macedonia	-10.7	3.2	1.6	4.5	-2.6	3.5	-3.1	-6.5	-3	3	48.1	100.1
Serbia & Montenegro	3.8	7.6	9.5	3.6	-23.1	11.2	0.0	1.7	3	5	44.8	106.1
Russia	-3.3	-4.0	1.9	-5.2	11.0	11.9	4.9	3.7	4	4.5	62.2	125.3
Ukraine	-12.0	-5.2	-0.3	-1.0	4.0	12.4	14.2	7.0	6	7	70.1	133.6

Notes: 1) Preliminary. - 2) Sales. - 3) **wiiw** estimate.

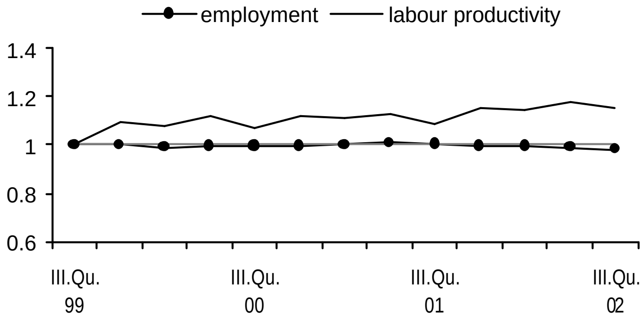
Source: **wiiw** Database incorporating national statistics, forecast: **wiiw**.

Hungary, Poland, Croatia, Macedonia, and even Ukraine). This indicates that the demand constraints on industrial sales remained in place. In the Czech Republic the weakness of producer prices may also follow from nominal appreciation. Of course the weakness of producer prices is having a moderating impact on the overall consumer price inflation – and therefore also on the impetus of the wage push. Potentially unwelcome consequences of weakening producer prices include the deterioration of profitability and a rise in the real burden of servicing firms' debts. Besides, weakening prices under high interest rates make credit too expensive and therefore restrict both investment and current activities. The consequences of deflation remain a valid concern in the case of Poland where the interest rates on commercial credit have remained quite high in both nominal and real terms. The recent changes in the monetary policy in Hungary may have similarly affected part of the (domestically owned) industrial sector, with the consequences yet to be registered. In the Czech Republic, where interest rates are much lower, the disruptive effects of deflation may have been more limited. The potentially negative consequences of weakening (or declining) producer prices have been counteracted by the renewed acceleration of growth in labour productivity.

Panel 1: Indices of labour productivity in industry and industrial employment in selected countries

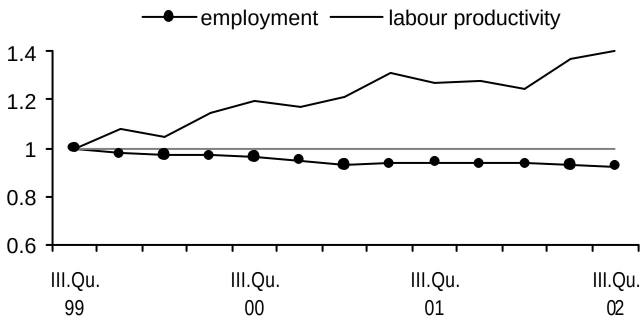
3rd quarter 1999 = 1

Slovenia

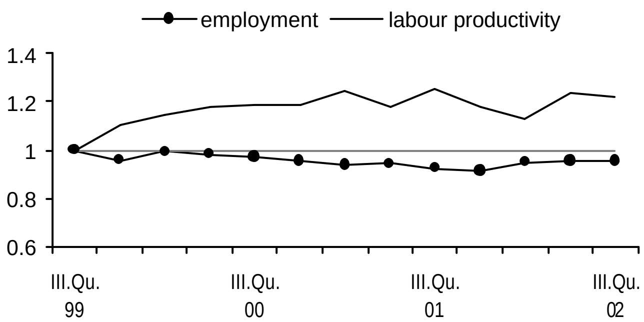


Croatia

Romania



Bulgaria



Source: **wiiw** Monthly Database incorporating national statistics, **wiiw** calculation.

In most accession countries the labour productivity improvements have involved fairly moderate cuts in employment. Only in Poland (and Croatia, which is not yet an accession country) has there been a tendency to reduce employment very strongly. Cuts in Croatian industrial employment have been associated with strongly rising production, which is indicative of the ongoing active restructuring. The huge productivity gains in the erstwhile 'laggards' (Bulgaria and especially Romania), which are primarily due to production expansion, indicate that currently these two countries are also undergoing industrial consolidation which the more advanced transition countries (including Poland) experienced much earlier. Cuts in Polish employment continue to be rather 'defensive' as they are coupled with very weak production growth.

Table 8

Labour productivity in industry

change in % against preceding year

	1995	1996	1997	1998	1999	2000	2001	2002 [1]	Index 1990=100 2002	Index 1995=100 2002
Czech Republic [2]	10.6	8.6	9.2	3.7	1.7	9.5	5.5	6.2	146.8	152.8
Hungary [3]	10.2	9.4	13.7	11.9	10.5	18.3	4.8	4.5	255.3	197.7
Poland [4]	6.3	9.1	11.2	4.7	11.8	13.6	4.2	7.3	263.6	180.4
Slovak Republic	4.0	2.5	4.8	9.1	0.2	12.1	5.9	5.8	139.3	147.5
Slovenia	6.3	9.2	4.4	5.4	3.1	8.4	3.5	5.6	178.5	146.8
Bulgaria [5]	7.4	7.0	-2.8	-3.8	0.8	20.4	1.9	.	142.6 [8]	123.7 [8]
Romania [6]	13.7	7.5	-1.8	-7.4	11.3	13.8	11.5	6.5	154.0	147.2
Croatia [6]	6.6	11.3	11.9	8.7	3.9	4.3	9.6	9.5	168.8	176.0
Macedonia [7]	1.2	29.8	8.3	14.8	6.4	6.0	-7.2	.	111.1 [8]	168.9 [8]
Serbia & Montenegro [7]	8.3	9.6	12.3	6.3	-19.1	16.4	3.4	.	66.2 [8]	127.3 [8]
Russia	5.4	2.9	8.6	0.8	11.8	10.1	4.6	.	94.2 [8]	145.0 [8]
Ukraine	-4.2	3.0	8.2	2.2	9.6	28.3	12.5	.	124.2 [8]	180.2 [8]

Notes: 1) Preliminary. - 2) Enterprises with 100 and more, from 1997 with 20 and more employees. From 2001 calculated with sales. - 3) From 1995 with more than 10, from 1999 more than 5 employees. - 4) For 2002 enterprises with more than 9 employees. - 5) Up to 1996 public sector only. - 6) Enterprises with more than 20 employees (for Romania from 1999). - 7) Excluding small enterprises. - 8) Year 2001.

Source: **wiiw** Database incorporating national statistics.

In all countries nominal gross wages in industry have been rising (wages were generally rising, also outside industry – see Appendix C). But even in countries with weakening (stabilizing, or falling) producer prices, the share of wages in industrial sales was generally lower than in earlier years. In Poland and Romania (and to a lesser extent in Croatia) that share was falling in 2002 consistently and strongly. Only in Hungary there was a marked rise in the share of wages in 2002 – no doubt an unintended 'demonstration' effect of the huge wage rises granted to the employees of the public service sectors in 2002. The index of the share of wages, which is equivalent to the index of unit labour costs in real terms, unequivocally points to a rise in potential profitability (per unit of real output) of

Table 9

Relative productivity gains, winner and loser manufacturing branches, 1995-2001

average annual change in % for total manufacturing (D) and relative gains DA to DN, in percentage points [1)]

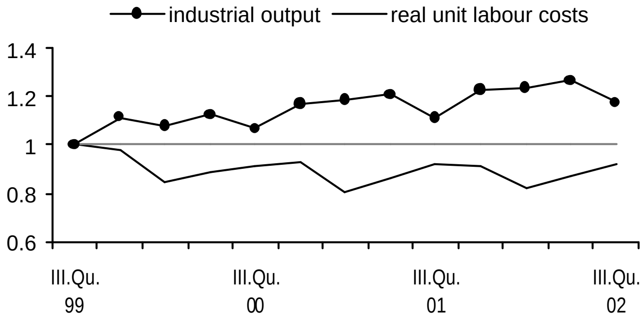
		Bulgaria	Czech Republic	Hungary	Poland	Romania	Slovak Republic	Slovenia	Estonia [2)]	Latvia	Lithuania [2)]
D	**Manufacturing total**	**3.5**	**7.7**	**14.3**	**9.4**	**7.5**	**8.2**	**4.2**	**10.0**	**6.6**	**6.7**
DA	Food products; beverages and tobacco	-1.3	-4.4	-9.0	-3.7	3.9	-4.7	-1.7	-6.6	-3.6	-7.2
DB	Textiles and textile products	-3.1	-4.9	-7.7	-3.6	-4.5	-10.1	0.7	6.1	-0.4	-0.1
DC	Leather and leather products	-4.5	-16.2	-12.0	-2.4	-1.8	0.0	-6.4	4.3	-3.5	11.2
DD	Wood and wood products	4.4	-2.5	-10.4	-3.5	-5.7	-1.8	-7.5	12.4	-1.5	0.6
DE	Pulp, paper & paper products; publishing & printing	-6.0	-2.4	-1.2	-0.3	-4.8	2.6	-7.8	-0.7	-1.1	-7.0
DF	Coke, refined petroleum products & nuclear fuel	-0.9	-1.7	-10.2	-2.7	-2.5	-2.6	.	.	.	-13.1
DG	Chemicals, chemical products and man-made fibres	1.6	-1.4	-10.9	-0.6	-2.8	-1.2	1.3	3.4	-2.3	16.1
DH	Rubber and plastic products	-0.8	1.2	-10.3	0.5	-7.2	-2.3	-1.7	0.0	11.7	-7.8
DI	Other non-metallic mineral products	4.6	-0.5	-7.2	0.0	1.1	-2.8	-0.1	2.4	8.4	2.1
DJ	Basic metals and fabricated metal products	4.1	-5.5	-5.9	-0.4	0.4	-6.3	0.5	1.9	0.9	2.5
DK	Machinery and equipment n.e.c.	0.5	5.2	-6.2	2.0	6.0	1.0	-2.6	8.8	-4.5	-2.7
DL	Electrical and optical equipment	5.7	12.7	19.5	5.2	1.1	1.7	4.7	5.1	14.6	16.4
DM	Transport equipment	-3.5	4.7	15.8	6.4	4.1	21.9	6.3	0.2	-1.8	22.4
DN	Manufacturing n.e.c.	7.7	1.0	-7.5	-0.2	6.9	2.2	0.3	2.1	1.8	-5.3

Notes: 1) Calculations of relative gains DA (1995-2001) – D (1995-2001) = relative gain DA. - 2) 1995-2000.
Source: **wiiw** estimates based on national statistics; own calculations.

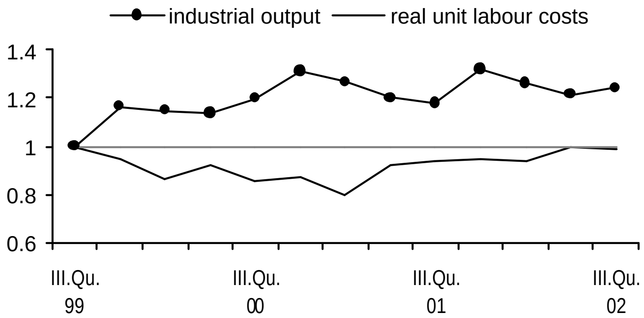
Panel 2: Indices of industrial output and real unit labour costs in selected countries

3rd quarter 1999 = 1

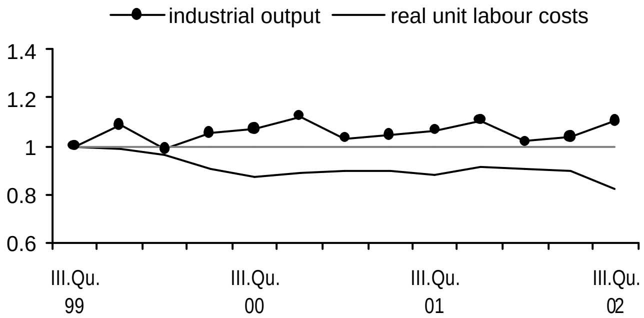
Czech Republic



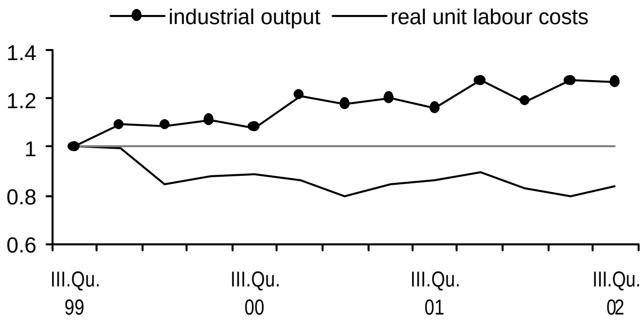
Hungary



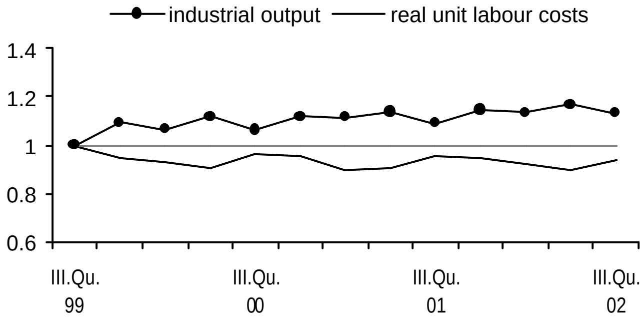
Poland



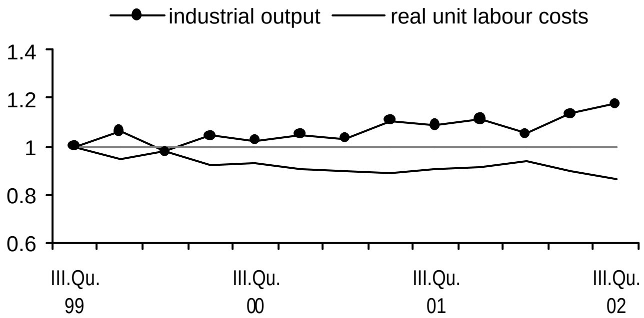
Slovak Republic



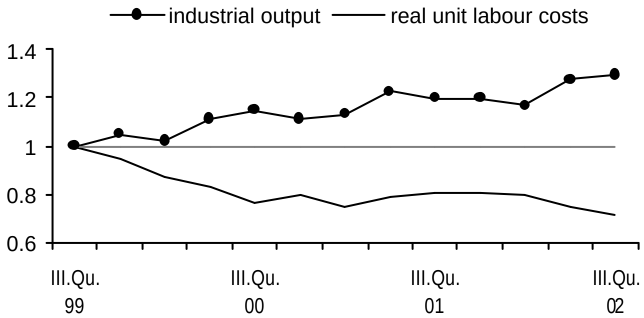
Slovenia



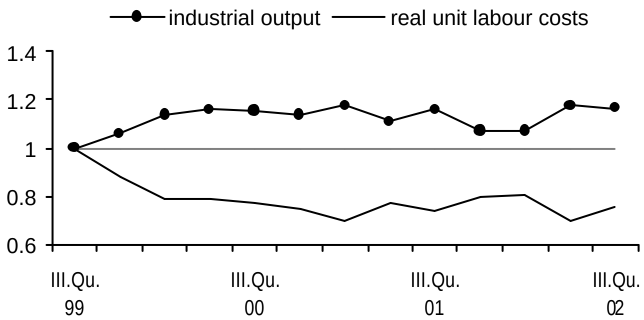
Croatia



Romania



Bulgaria



Source: **wiiw** Monthly Database incorporating national statistics, **wiiw** calculation.

industrial production. Of course, some qualifications have to be made here. First, actual profitability depends also on prices of intermediate inputs (including imported raw materials and components). Second, it also depends on fixed or quasi-fixed costs including depreciation and interest on external financing. But in countries whose currencies were on the whole rather strengthening in nominal terms recently (the Czech Republic, Hungary, Croatia, Poland and Slovakia), the actual profitability should have been even higher on account of the use of cheaper imported intermediate inputs. Rather weak (compared with 2001) world-market prices of imported oil must have added to profitability generally – certainly except in Russia where the profitability of industry, which is dominated by the energy and raw-materials producing branches, has been adversely affected by the weaker world-market prices.

All in all, because of the important role of wage costs in determining aggregate industrial profitability, falling real unit labour costs seem quite certain to have helped raise industry's profitability in a number of countries. Hungary may be the only exception to this rule in 2002. From a longer-term perspective, the movements in real unit labour costs appear to be reflected by the movements in industrial output (see Panel 2).

As can be seen, the diagrams for output and real unit labour costs in individual countries are roughly symmetrical. No doubt that visual impression is reinforced by the seasonal variations in both variables. Nonetheless there seems to be a more fundamental dynamic link between the two. Losses due to rising real unit labour costs (as recently in Hungary) may well augur a stagnation in output (and other adjustments such as stronger cuts in employment). By the same token, the improvements in profitability (Poland, Romania and Croatia) should be considered conducive to production growth.

Of course the rule 'the lower the real unit labour costs the higher the production' is far from being universally valid. It is valid only in quite specific circumstances. In Slovenia and the Czech Republic the real unit costs went up similarly through the consecutive years – but production has been generally rising, though not spectacularly. In Poland the strong labour cost gains in 2001 did not preclude production stagnation. Generally, the improvements in profitability (or fall in real unit costs) are quite certain to accelerate output growth only when there is strong demand for industrial output, reflecting robust investment or foreign demand growth. Otherwise, rising profitability may only imply a contraction in the share of labour household income in GDP – and consequently a weakening of private demand and then of production. In this case rising unit profitability may be coupled with rising unemployment and possibly even with a decline in the absolute level of firms' profits. A drive for lower unit labour costs may therefore be eventually counterproductive. In particular it may be counterproductive if the resultant gains in external competitiveness (falling trade deficits) are associated with falling domestic sales (caused by stagnating or falling household labour income).

Foreign trade in accession countries unaffected by real appreciation

Compared to 2001, both exports and imports in most of the accession countries (and Ukraine) grew quite anaemically in current euro terms in 2002 (Tables 10, 11). But exports in all of those countries rose faster than imports (which in 2001 was not the case in Slovakia, Bulgaria and Romania). The differences between the rates of growth of exports and imports were large enough to yield lower trade deficits in all CEE accession countries (except Hungary where the trade deficit rose). In view of the real appreciation (in PPI terms) present, to various degrees, in all countries, the trade deficits calculated at constant domestic prices may have contracted even more substantially everywhere, including even Hungary.

Out of the remaining (non-accession) countries, only Ukraine followed the pattern of the accession countries and managed to improve its trade balance (actually a surplus). In Croatia, Macedonia and Yugoslavia (Serbia and Montenegro) the trade deficits grew substantially and in Russia the trade surplus contracted. The trade balances in Croatia, Yugoslavia (Serbia and Montenegro) and Russia were deteriorating quite strongly for the third year running (though it must be remembered that the Russian trade surplus still amounted to nearly 13% of GDP).

Provisional estimates suggest that the accession countries' trade with the EU performed relatively well in 2002 (Table 12). Of course both exports to and imports from the EU grew at lower rates than in 2001. Nonetheless, exports rose quite respectably (by about 7%), especially if one considers the fact that all EU imports declined by about 5% (in current euro terms) in 2002. Only Slovenian exports to the EU may actually have declined, if only slightly. The Czech Republic, Hungary and Slovakia have increased their trade surpluses with the EU, and that rather strongly. Their exports have gained market shares in the EU again. The remaining accession countries (except Slovenia) may have reduced their deficits vs. the EU. The first-wave accession countries reduced their combined trade deficit with the EU by about EUR 13 billion (compared with the year 1997, when their trade deficit was the highest). Interestingly, some countries (Poland, the Czech Republic) have managed to reorient part of their exports from the German to other EU markets (the Netherlands, UK, Sweden and France).

The foreign trade developments of the accession countries (expansion of exports, which predominantly consist of manufactured goods, coupled with moderate growth in imports) square quite well with the performance of industrial production. Also, this fact is consistent with the improvements in profitability (falling unit real costs) in industry: Rising exports allowed the realization of gains in productivity and profitability. Without export sales strengthening in the second half of 2002 (in all accession countries except Hungary) industrial production would have recorded less growth (or would have fallen further in Poland).

Table 10

Foreign trade of Central and Eastern Europe and the main CIS States, in EUR million

based on customs statistics

		1995	1998	1999	2000	2001	2002 1)	2001	2002	2003	2004
										forecast	
								change in %			
Czech Republic	Exports	16502	23070	24641	31483	37251	40630	18.3	9.1	4	11
	Imports	19404	25289	26387	34876	40675	43046	16.6	5.8	7	12
	Balance	-2902	-2219	-1747	-3393	-3424	-2416	.	.	.	.
Hungary 2)	Exports	9972	20477	23491	30545	34082	36100	11.6	6	8	10
	Imports	11905	22871	26288	34856	37654	39700	8.0	5	8	9
	Balance	-1933	-2394	-2797	-4312	-3572	-3600	.	.	.	.
Poland	Exports	17710	25145	25729	34383	40375	43200	17.4	7	6	7
	Imports	22491	41539	43151	53122	56223	58300	5.8	4	4	7
	Balance	-4781	-16394	-17422	-18739	-15848	-15100	.	.	.	.
Slovakia 3)	Exports	6634	9541	9602	12880	14115	15256	9.6	8.1	10	11
	Imports	6783	11635	10628	13860	16488	17519	19.0	6.3	5	8
	Balance	-148	-2094	-1025	-980	-2372	-2263	.		.	.
Slovenia	Exports	6426	8052	8037	9505	10349	10920	8.9	6	5	6
	Imports	7327	8999	9482	10996	11345	11460	3.2	1	3	3
	Balance	-901	-947	-1445	-1491	-997	-540	.	.	.	.
CEEC-5	Exports	57245	86285	91500	118795	136172	146106	14.6	7	6	9
	Imports	67909	110334	115936	147709	162385	170025	9.9	5	6	8
	Balance	-10665	-24049	-24436	-28915	-26213	-23919	.	.	.	.
Bulgaria 4)	Exports	4142	3841	3734	5253	5714	5900	8.8	3	5	6
	Imports	4377	4476	5140	7085	8128	8100	14.7	0	2	3
	Balance	-234	-635	-1406	-1832	-2414	-2200	.	.	.	.
Romania	Exports	6047	7412	7956	11219	12711	14500	13.3	14	6	6
	Imports	7857	10569	9896	14128	17363	19100	22.9	10	7	7
	Balance	-1810	-3157	-1940	-2909	-4652	-4600	.	.	.	.
CEEC-7	Exports	67434	97539	103190	135267	154597	166506	14.3	8	23	9
	Imports	80143	125379	130972	168922	187875	197225	11.2	5	21	8
	Balance	-12709	-27841	-27782	-33656	-33278	-30719	.	.	.	.
Croatia 5)	Exports	3595	4046	4027	4818	5210	5183	8.1	-0.5	1	3
	Imports	5810	7477	7324	8588	10232	11316	19.1	10.6	5	5
	Balance	-2215	-3431	-3297	-3770	-5022	-6134	.	.	.	.
Macedonia	Exports	920	1170	1117	1431	1290	1200	-9.9	-7	8	0
	Imports	1314	1709	1665	2266	1884	2000	-16.9	6	5	5
	Balance	-394	-539	-548	-835	-595	-800	.	.	.	.
Serbia & Montenegro 6)	Exports	.	2518	1391	1808	2095	2274	15.9	8.5	9	6
	Imports	.	4283	3081	3892	5386	6003	38.4	11.5	2	2
	Balance	.	-1766	-1690	-2084	-3291	-3729	.	.	.	.
Russia 7)	Exports	63005	66467	70820	113672	113448	113172	-0.2	-0.2	2	3
	Imports	47856	51798	37061	48552	60025	64049	23.6	6.7	9	9
	Balance	15148	14668	33759	65120	53423	49123	.	.	.	.
Ukraine	Exports	10036	11283	10856	15771	18159	18700	15.1	3	5	7
	Imports	11837	13103	11104	15104	17612	17800	16.6	1	4	6
	Balance	-1801	-1820	-248	667	547	900	.	.	.	.

Notes: 1) Preliminary. - 2) Including trade of firms with customs free legal status. - 3) From 1998 according to new methodology. - 4) From 1999 according to new methodology. - 5) From 2000 according to new methodology. - 6) From 1999 excluding Kosovo and Metohia. - 7) Including estimate of non-registered trade.

Source: **wiiw** Database incorporating national statistics, forecast: **wiiw**.

Table 11

Exports and imports, at current prices[1], converted into EUR million, 2001 and 2002

Exports, growth rates, year-on-year, in %[2]

	Q1 01	Q2 01	Q3 01	Q4 01	Q1 02	Q2 02	Q3 02	Q4 02	Oct-02	Nov-02	Dec-02
Czech Republic	27.8	21.1	15.1	10.9	7.7	11.1	11.7	6.1	6.8	6.1	5.1
Hungary	24.1	19.3	7.9	0.1	8.6	7.9	4.0	.	3.2	-0.4	.
Poland	29.1	23.3	14.3	5.3	3.3	7.5	5.5	.	-2.8	21.7	.
Slovakia	18.0	13.6	9.2	-0.3	-0.3	3.5	11.7	17.4	13.3	16.1	24.2
Slovenia	17.9	10.3	8.8	0.3	1.6	5.8	7.6	.	8.7	5.2	.
Bulgaria	25.5	11.7	9.2	-6.4	-3.0	4.5	12.3	.	7.4	-30.3	.
Romania	27.6	20.8	11.6	-4.2	6.2	11.2	14.6	.	31.2	23.4	.
Croatia	9.0	11.3	4.7	8.0	-0.2	2.8	-2.1	-2.6	-12.1	2.0	5.2
Russia	14.0	9.9	-2.9	-18.3	-11.0	-4.9	2.4	11.3	17.0	-0.3	17.9

Imports, growth rates, year-on-year, in %[2]

	Q1 01	Q2 01	Q3 01	Q4 01	Q1 02	Q2 02	Q3 02	Q4 02	Oct-02	Nov-02	Dec-02
Czech Republic	29.6	20.0	12.9	7.2	2.3	7.0	8.7	5.2	4.6	8.2	2.7
Hungary	22.8	18.1	2.1	-4.8	5.0	3.3	5.5	.	6.6	2.7	.
Poland	12.2	8.6	5.0	-1.3	0.4	4.5	2.6	.	-2.6	12.0	.
Slovakia	25.8	26.8	20.2	7.2	0.5	2.8	7.5	13.6	18.2	8.6	14.3
Slovenia	7.8	7.4	0.7	-2.3	0.1	-0.7	2.8	.	3.0	3.6	.
Bulgaria	15.8	27.1	19.9	0.3	-0.3	0.2	-1.8	.	4.1	-5.1	.
Romania	45.9	32.2	11.7	7.6	4.2	1.3	19.0	.	13.6	11.0	.
Croatia	29.3	33.3	14.8	4.2	12.2	4.4	12.2	14.0	14.2	7.0	22.0
Russia	20.9	40.4	20.8	13.6	15.0	3.1	6.6	2.0	10.4	-2.5	-1.0

Trade balance cumulated, EUR million

	Q1 01	Q2 01	Q3 01	Q4 01	Q1 02	Q2 02	Q3 02	Q4 02	Oct-02	Nov-02	Dec-02
Czech Republic	-752	-719	-848	-1125	-283	-381	-656	-1100	-244	-255	-601
Hungary	-981	-958	-738	-891	-739	-591	-905	.	-461	-249	.
Poland	-3527	-4329	-3778	-4280	-3259	-4221	-3582	.	-1373	-1224	.
Slovakia	-428	-527	-541	-880	-459	-517	-434	-864	-315	-228	-322
Slovenia	-203	-316	-166	-309	-165	-140	-51	.	-3	-86	.
Bulgaria	-382	-680	-610	-742	-419	-619	-388	.	-245	-358	.
Romania	-889	-1396	-692	-1687	-861	-1093	-970	.	-457	-381	.
Croatia	-999	-1564	-1226	-1244	-1267	-1653	-1569	-1648	-620	-563	-465
Russia	15431	14367	13744	9839	10542	12418	13456	12577	4399	3822	4356

Notes: 1) Exports fob, imports cif, except for Czech Republic and Slovakia (fob). - 2) Quarterly data for exports and imports are averages of monthly data. The Q4 average covers as many months as are available.

Source: **wiiw** Monthly Database incorporating national statistics.

Table 12

EU(15) trade of Central and Eastern European Countries, EUR million

based on customs statistics

		1995	1996	1997	1998	1999	2000	2001	2002 [1)]	2001 change in %	2002 change in %
Czech Republic	Exports	9987	10364	11842	14762	17053	21588	25682	27793	19.0	8.2
	Imports	11831	13851	14846	16055	16946	21637	25139	25907	16.2	3.1
	Balance	-1844	-3487	-3004	-1293	107	-49	543	1886	.	.
Hungary [2)]	Exports	6249	6564	12037	14940	17906	22939	25315	26910	10.4	6
	Imports	7322	7715	11788	14664	16929	20354	21761	22175	6.9	2
	Balance	-1073	-1151	249	276	977	2586	3554	4735	.	.
Poland	Exports	12398	12908	14600	17173	18127	24037	27942	29646	16.2	6
	Imports	14540	18970	23911	27268	28016	32494	34512	35961	6.2	4
	Balance	-2142	-6061	-9312	-10096	-9889	-8457	-6570	-6315	.	.
Slovakia [3)]	Exports	2481	2909	3045	5309	5701	7602	8450	9234	11.1	9.3
	Imports	2358	3310	3597	5833	5493	6775	8207	8815	21.1	7.4
	Balance	123	-401	-553	-524	208	827	243	418	.	.
Slovenia	Exports	4306	4286	4705	5271	5304	6060	6434	6492	6.2	1
	Imports	5041	5088	5588	6242	6530	7451	7675	7828	3.0	2
	Balance	-734	-801	-884	-972	-1226	-1391	-1240	-1336	.	.
CEEC-5	Exports	35421	37032	46228	57455	64091	82227	93823	100075	14.1	7
	Imports	41092	48933	59731	70063	73914	88712	97293	100687	9.7	4
	Balance	-5671	-11902	-13503	-12608	-9823	-6485	-3470	-611	.	.
Bulgaria [4)]	Exports	1560	1526	1889	1905	1942	2684	3126	3220	16.5	3
	Imports	1628	1420	1645	2010	2486	3119	4005	4130	28.4	3
	Balance	-68	105	243	-105	-544	-435	-879	-909	.	.
Romania	Exports	3274	3603	4204	4783	5214	7163	8619	9826	20.3	14
	Imports	3964	4721	5222	6097	6004	7996	9957	11032	24.5	11
	Balance	-690	-1118	-1018	-1314	-790	-833	-1338	-1207	.	.
CEEC-7	Exports	40255	42160	52321	64143	71246	92074	105569	113121	14.7	7
	Imports	46684	55074	66599	78170	82403	99827	111256	115848	11.4	4
	Balance	-6429	-12914	-14278	-14027	-11157	-7753	-5687	-2727	.	.
Croatia [5)]	Exports	2072	1838	1823	1927	1960	2619	2821	2742	7.7	-2.8
	Imports	3609	3693	4793	4440	4136	4756	5844	6316	22.9	8.1
	Balance	-1537	-1855	-2970	-2513	-2175	-2137	-3023	-3574	.	.
Macedonia	Exports	312	387	407	516	506	612	628	.	2.6	.
	Imports	527	497	581	620	677	866	800	.	-7.7	.
	Balance	-215	-110	-173	-104	-172	-254	-172	.	.	.
Serbia & Montenegro [6)]	Exports	.	551	939	965	504	700	896	.	28.1	.
	Imports	.	1366	1758	1847	1276	1610	2212	.	37.4	.
	Balance	.	-815	-820	-882	-772	-910	-1316	.	.	.
Russia [7)]	Exports	20104	21570	24691	20721	23290	39927	40866	.	2.4	.
	Imports	13718	12508	17258	14047	10479	12061	17068	.	41.5	.
	Balance	6386	9062	7432	6674	12810	27867	23798	.	.	.
Ukraine	Exports	1074	1259	1549	1892	1986	2813	3323	3692	18.1	11
	Imports	1768	2184	2980	2831	2249	3118	3820	4241	22.5	11
	Balance	-694	-925	-1430	-939	-263	-305	-497	-549	.	.

Notes: 1) Preliminary. - 2) Including trade of firms with customs free legal status. - 3) From 1998 according to new methodology. - 4) From 1999 according to new methodology. - 5) From 2000 according to new methodology. - 6) From 1999 excluding Kosovo and Metohia. - 7) Registered trade only.

Source: **wiiw** Database incorporating national statistics.

The foreign trade performance of the transition countries is rather inconsistent with the conventional logic which suggests that exports should have rather declined. First, there is no denying that the business climate in the EU has been pretty bad. Second, the currencies of all accession countries appreciated in real terms at least vs. the euro in 2002, some of them very strongly (Figures 3a-3b). In such circumstances one often expects falling exports and rising imports – with the requisite adverse effects on production and GDP growth.

The alternative indicator of real appreciation, which is the exchange rate corrected for nominal unit labour costs in industry, supports a different judgement on the pace of appreciation in the individual countries. The ULC-based real appreciation appears substantially lower than the PPI-based real appreciation. This reflects the tendency for the nominal unit labour costs to fall whereas the PPI continues to rise. Actually, all countries (except the Czech Republic and Hungary) have had real depreciation (in ULC terms) in 2002. Thus, falling ULCs – primarily the effect of expanding labour productivity – seem to have compensated for the nominal appreciation of the domestic currencies.

Moreover, the PPI-based real exchange rate index may be an inadequate indicator of actual competitiveness because rising producer prices may well reflect quality improvements, and in particular better prices received by domestic producers on their exports. There is more than anecdotal evidence that the processes of qualitative upgrading of exports (and, by implication, of production) goes on in the accession countries fairly vigorously. In actual fact several accession countries improve prices and quality of their exports not only in absolute terms, but in relation to their foreign competitors. In selected branches of manufacturing the quality/price improvements have been enormous (see Appendix A).

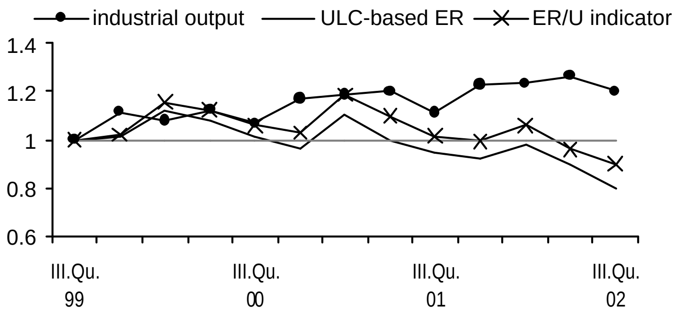
In so far as rising competitiveness is reflected in 'better' export prices received, the ULC-based real exchange rate indicators, which ignore price developments, may be insufficient for the evaluation of the prospects of withstanding foreign competition. Therefore it makes sense to complement the examination of trends in ULC-based real exchange rates with the examination of trends in alternative indicators, which allow for the competitiveness-linked increases in producer prices. One such indicator can be defined as the ratio of the index of nominal appreciation (ER) and the index of real unit costs (U).

Recent trends in industrial output, ER/ULC and ER/U are shown in Panel 3.

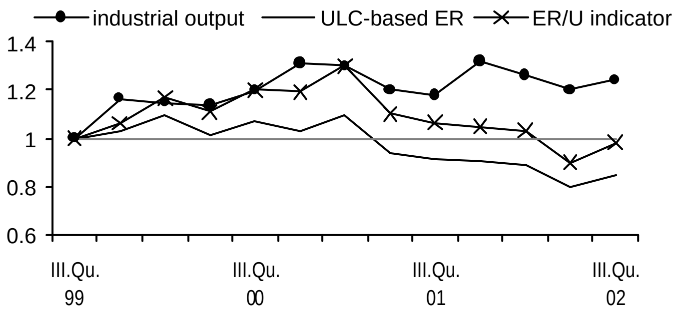
Panel 3: Indices of industrial output, ULC-based exchange rate and the ER/U indicator in selected countries

3rd quarter 1999 = 1

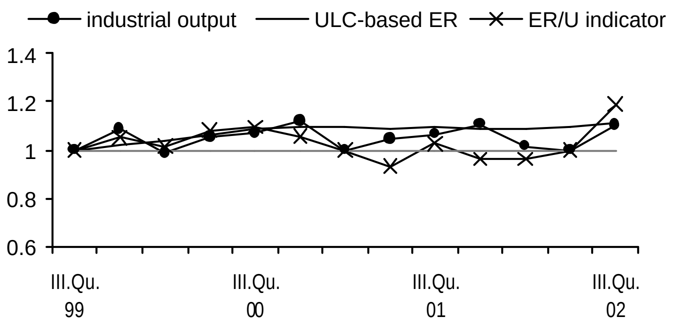
Czech Republic



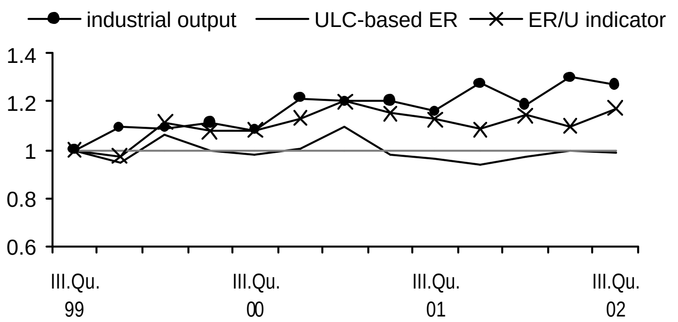
Hungary



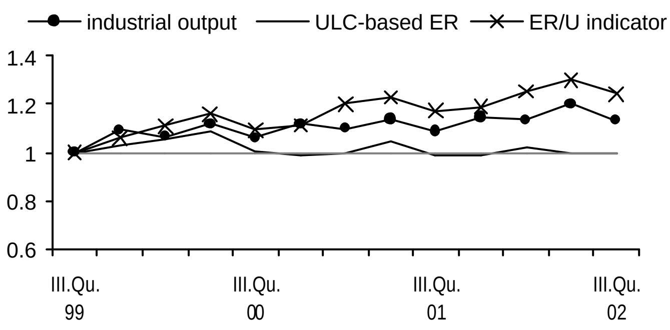
Poland



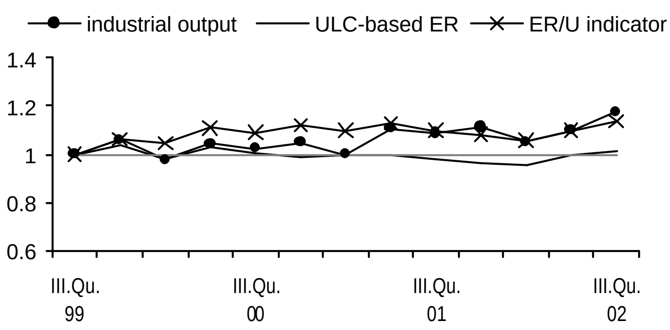
Slovak Republic



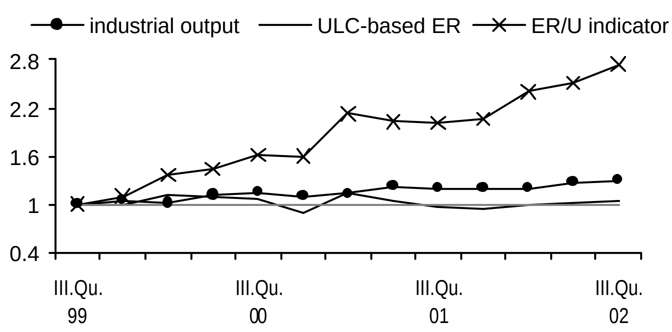
Slovenia



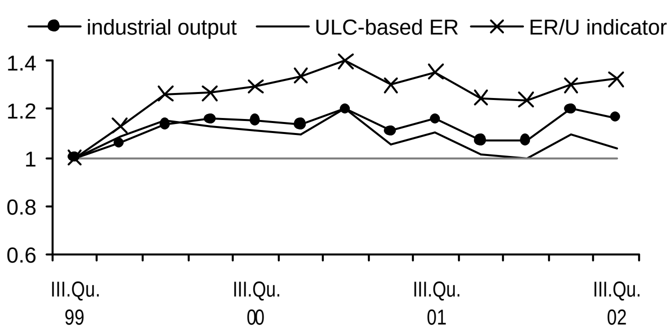
Croatia



Romania



Bulgaria



Source: **wiiw** Monthly Database incorporating national statistics, **wiiw** calculation.

As can be seen from Panel 3, recently ER/U and ER/ULC have been improving (rising) in most accession countries, with the strongest gains made in Romania and Poland. ERU gains were on the whole moderate in Bulgaria and Croatia, while in Hungary and the Czech Republic the ERU have generally been falling. This suggests that the latter two countries may be heading for a period of slowdown in industrial growth, which could be attributed to excessive nominal appreciation, not paralleled by improvements in productivity and unit labour costs. In so far as trends in industrial production mirror the foreign trade developments, one can expect also a certain weakening of the trade performance (e.g. a rise in trade deficits) in both countries.

Inflation: no longer an issue ?

Inflation has been subsiding consistently everywhere, including countries with a quite recent history of hyperinflation. In the Czech Republic and Poland the CPI index is currently lower than in the EU. In some countries (notably Slovakia) inflation in consumer prices was suppressed 'artificially', through the politically motivated postponement of hikes in regulated prices (of the services of public utilities). Adjustments in regulated prices will continue everywhere for a long time and hence will be adding to CPI inflation. In some cases further deregulation of prices, if coupled with an active antitrust policy, should however lower inflation. This may be the case in Poland and the Czech Republic where the foreign-owned national telecom companies charge e.g. internet fees several times the

Table 13

Consumer price inflation

change in % against preceding year

	1995	1996	1997	1998	1999	2000	2001	2002 1)	2003 forecast	2004 forecast
Czech Republic	9.1	8.8	8.5	10.7	2.1	3.9	4.7	1.8	1.6	2
Hungary	28.2	23.6	18.3	14.3	10.0	9.8	9.2	5.3	5.3	5
Poland	27.8	19.9	14.9	11.8	7.3	10.1	5.5	1.9	2	3
Slovak Republic	9.9	5.8	6.1	6.7	10.6	12.0	7.1	3.3	7	7
Slovenia	13.5	9.9	8.4	7.9	6.1	8.9	8.4	7.5	6	5.5
Bulgaria	62.1	121.6	1058.4	18.7	2.6	10.3	7.4	5.8	4	4
Romania	32.3	38.8	154.8	59.1	45.8	45.7	34.5	22.5	18	15
Croatia 2)	2.0	3.5	3.6	5.7	4.2	6.2	4.9	2.2	3	2.5
Macedonia 2)	15.9	3.0	4.4	0.8	-1.1	10.6	5.2	1.5	2	4
Serbia & Montenegro	78.6	91.5	21.6	29.9	44.9	85.6	89.0	16.5	15	10
Russia	197.5	47.8	14.8	27.6	85.7	20.8	21.6	16.0	12	10
Ukraine	376.8	80.2	15.9	10.6	22.7	28.2	12.0	0.8	10	7

Notes: 1) Preliminary. - 2) Retail prices.

Source: **wiiw** Database incorporating national statistics, forecast: **wiiw**.

Figure 2a: Minimum interest rates

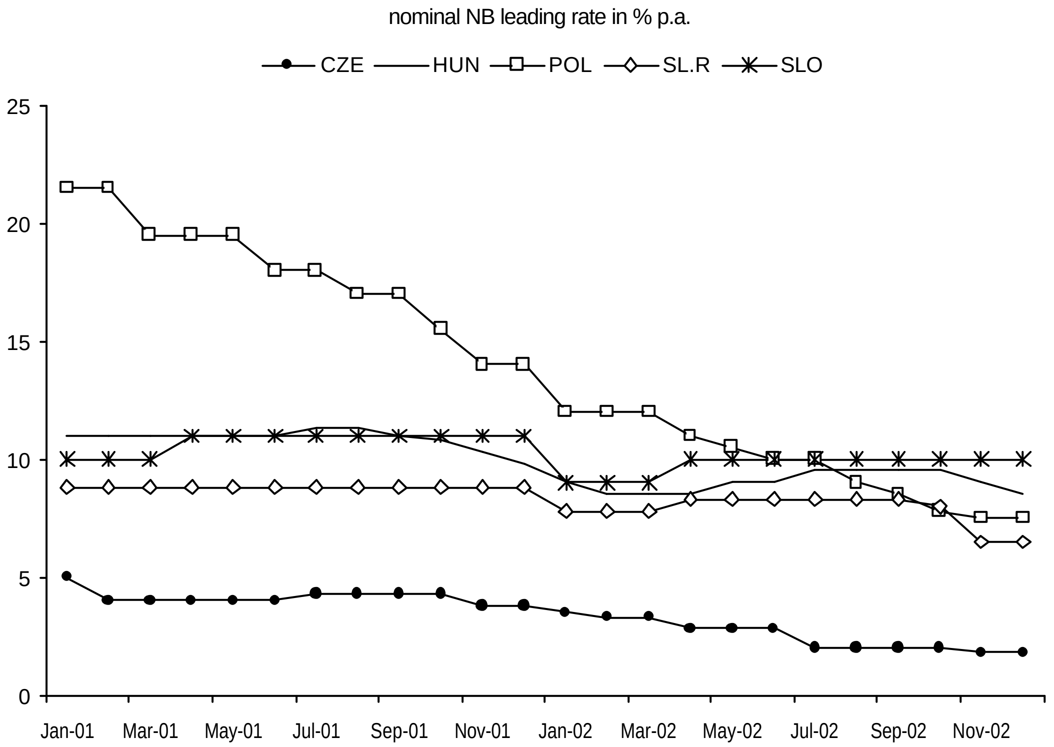
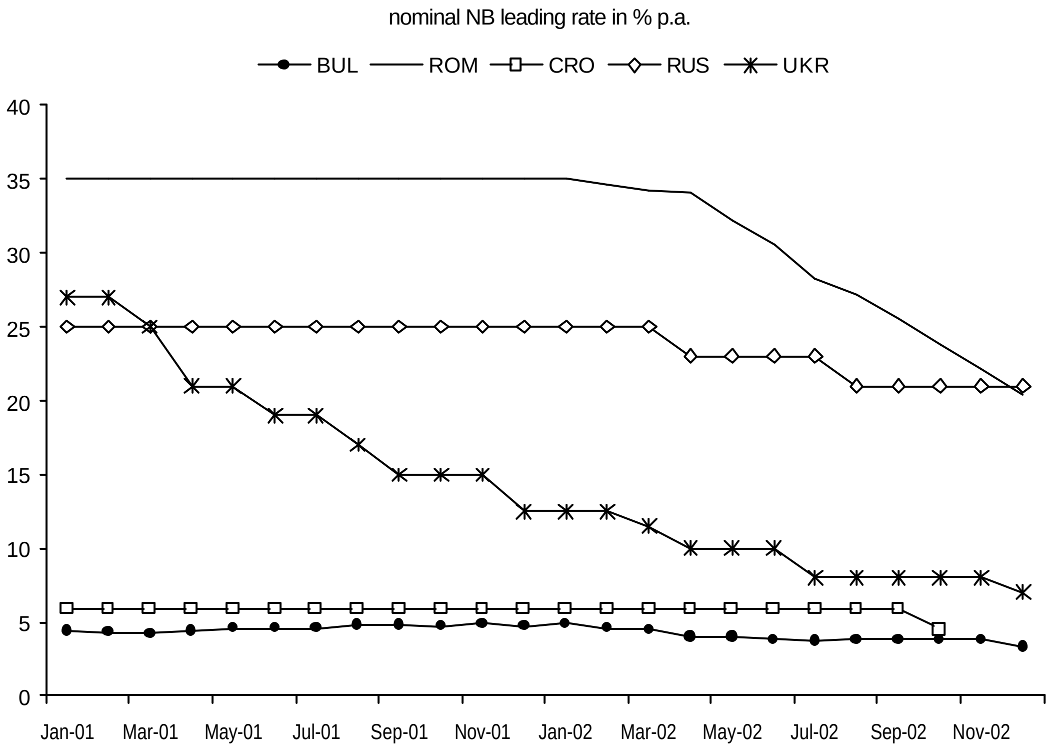


Figure 2b: Minimum interest rates



Source: **wiiw** Monthly Database incorporating national statistics.

average EU level. Also, some 'structural' inflation will continue for quite some time. Rising incomes will be strengthening the demand for consumer services (housing, recreation etc.). Prices of services, which are currently relatively much lower than in the EU, will therefore be rising generally faster than the prices of consumer goods.

The past experience suggests that further disinflation will continue consistently, even if in most cases rather gradually. Certainly, a rapid halt in inflation can in principle be always possible through a draconian monetary policy. Poland's disinflation 'success' in 2001-02 illustrates this point vividly. There is little doubt that the enormous real costs of this policy (output stagnation, massive unemployment) will discourage other transition countries from implementing it. The recent (long overdue) relaxation of the monetary policy in Poland would indicate that the monetary authorities are learning from their past mistakes. A much better example to follow is provided by the Czech monetary authorities, which have administered consistently low interest rates, without this having any perceptible impact on inflation (Figures 2a and 2b)

Also the fact that most transition countries run quite high (and in many cases even rising) fiscal deficits appears to have little or nothing to do with current inflation. Rising deficits need not produce higher inflation – just as falling deficits may coincide with higher inflation. Thus, even if the transition countries appear unable, or unwilling, to cut their budget deficits, disinflation may continue along its longer-term downward trend.

Table 14

Central government budget balance in % of GDP

	1995	1996	1997	1998	1999	2000	2001	2002 1)
Czech Republic	0.5	-0.1	-0.9	-1.6	-1.6	-2.3	-3.1	-2.0
Hungary	-5.5	-1.9	-4.0	-5.5	-3.0	-2.8	-2.7	-9.1
Poland	-2.4	-2.4	-1.2	-2.4	-2.0	-2.2	-4.3	-5.1
Slovak Republic	-1.5	-4.1	-5.2	-2.5	-1.8	-3.0	-4.5	-4.9
Slovenia	0.9	0.7	-1.1	-1.1	-0.5	-0.9	-1.1	.
Bulgaria	-6.6	-10.8	-3.8	1.4	1.7	-0.9	-2.0	-0.7 2)
Romania	-4.1	-4.9	-3.6	-2.8	-2.5	-3.6	-3.1	-2.9
Croatia	-0.7	-0.1	-0.9	0.9	-1.8	-4.0	-2.3	-2
Macedonia	.	.	0.0	0.0	0.3	2.3	-2.5	-1
Russia	-2.8	-3.5	-3.8	-5.3	-1.1	1.4	2.9	2.1
Ukraine 2)	-6.6	-4.9	-6.6	-2.2	-1.5	0.6	-0.6	2

Remark: – = deficit.

Notes: 1) Preliminary. - 2) General government.

Source: **wiiw** Database incorporating national statistics.

The longer-term inflationary trends in the accession countries (and possibly also in the remaining transition countries) seem to be reflecting primarily an inflationary inertia. Rising producer prices affect the consumer prices and the latter affect wages. These in turn are reflected in labour costs, and have a bearing on producer prices. Of course this 'circular' process is affected by many other developments (e.g. costs of capital, costs of imported inputs, degree of competition, strength of demand, etc.). Besides the process is crucially affected by productivity and efficiency developments, in the first place developments in labour productivity. Rising labour productivity can offset the effects of rising nominal wages, and hence contribute to price stability.

Table 15

Producer prices in industry

change in % against preceding year

	1995	**1996**	**1997**	**1998**	**1999**	**2000**	**2001**	**2002** [1)]	**2003 forecast**	**2004 forecast**
Czech Republic	7.6	4.7	4.9	4.9	1.0	4.9	2.9	-0.5	0.5	1
Hungary	28.9	21.8	20.4	11.3	5.1	11.6	5.2	-1.8	.	.
Poland	25.4	12.4	12.2	7.3	5.7	7.8	1.6	1.0	.	.
Slovak Republic	9.0	4.2	4.5	3.3	4.3	10.8	6.5	2.1	.	.
Slovenia	12.8	6.8	6.1	6.0	2.1	7.6	8.9	5.1	.	.
Bulgaria	53.4	130.0	971.1	16.5	3.2	17.1	7.3	3.0	.	.
Romania	35.1	49.9	152.7	33.2	44.5	53.4	41.0	24.9	.	.
Croatia	0.7	1.4	2.3	-1.2	2.6	9.7	3.6	-0.4	.	.
Macedonia	4.7	-0.3	4.2	4.0	-0.1	10.7	2.0	1.1	2	4
Serbia & Montenegro	57.7	90.2	19.5	25.5	43.3	106.9	85.1	8.7	10	10
Russia	236.5	50.8	15.0	7.1	58.9	46.6	19.1	11.6	15	8
Ukraine	488.8	52.1	7.7	13.2	31.1	20.9	8.6	3.1	0	.

Note: 1) Preliminary.

Source: **wiiw** Database incorporating national statistics, forecast: **wiiw**.

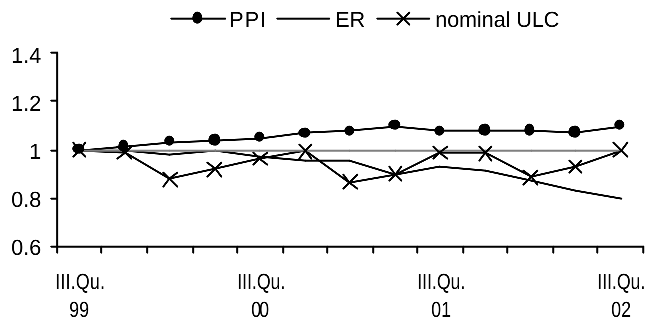
At the aggregate level the evolution of producer prices in industry turns out to be broadly consistent with the developments in nominal unit labour costs (ULCs) and/or the movements in the nominal exchange rates, which to some degree represent the costs of imported production inputs (see Panel 4).

Producer price inflation (PPI) in the individual accession countries is variously affected by the developments in ULCs and exchange rates. In Bulgaria (which is on a currency board regime with a fixed exchange rate) inflation and unit labour costs move roughly together. In Slovenia, all three items follow similar trends, each feeding on the other two. A similar

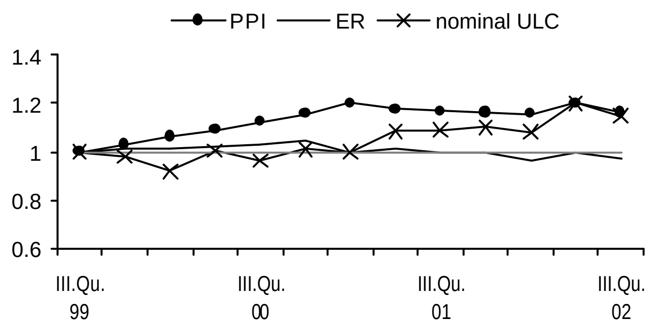
Panel 4: Indices of producer prices in industry, nominal exchange rate (ER) and nominal unit labour costs (ULC) in selected countries

3rd quarter 1999 = 1

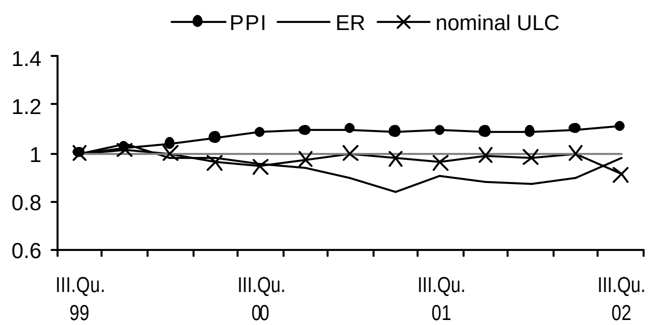
Czech Republic



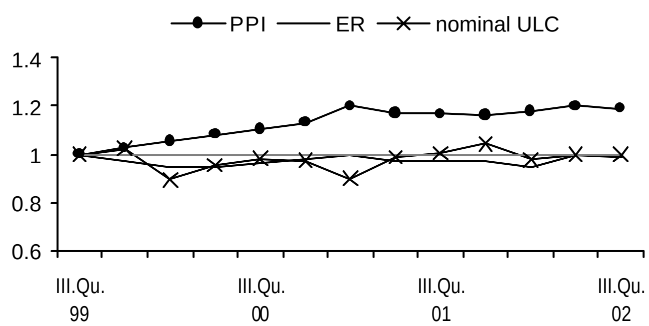
Hungary

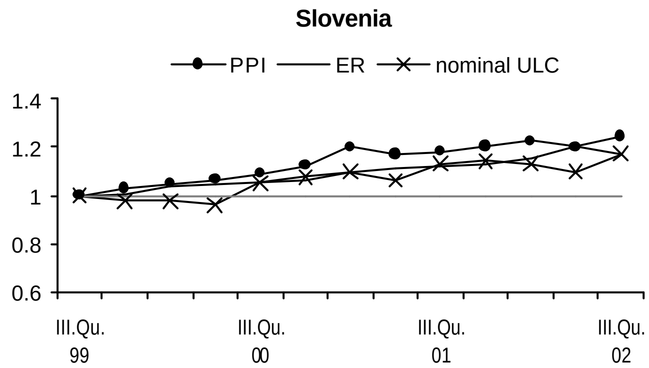


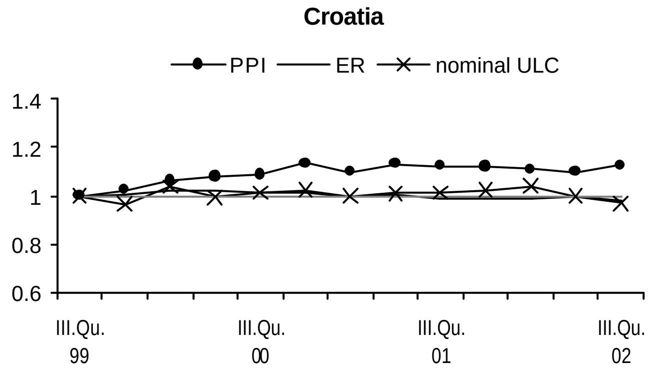
Poland

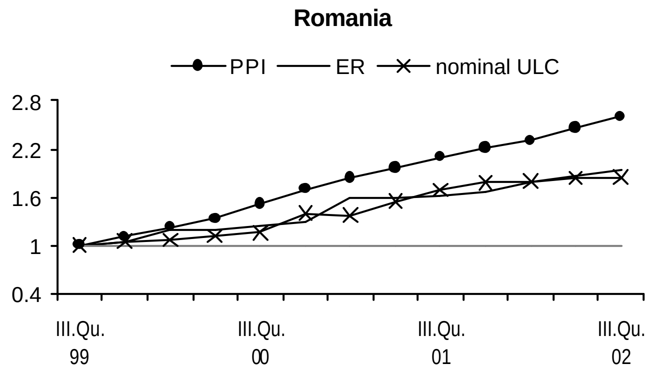


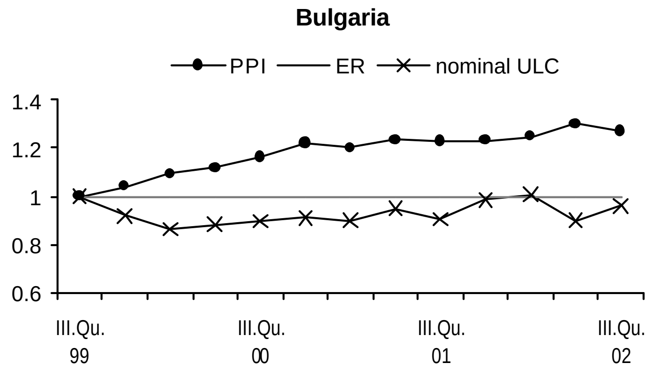
Slovak Republic











Source: **wiiw** Monthly Database incorporating national statistics, **wiiw** calculation.

pattern was observed in Romania, but recently both devaluation and the rise in ULCs have fallen behind PPI. This suggests the Romanian PPI should be stabilizing too. In Poland, Croatia and the Czech Republic the three items move at different speeds, with prices gradually stabilizing under the impact of stabilizing ULCs and nominal appreciation (particularly strong in the Czech Republic). In Hungary and Slovakia, PPI appears to have been largely a function of the exchange rate.

The graphs from Panel 4 suggest that sustained labour productivity improvements (or, more precisely, sustained decline in unit labour costs) and/or sustained nominal appreciation is needed for a stabilization of producer prices. Moreover, even when these conditions are satisfied, approaching the price stability may take substantial time. Thus, although in most accession countries the prospects of improvements in labour productivity are good and the exchange rates need not devalue significantly, inflation will continue. On the whole, as long as rising prices reflect qualitative improvements and better export performance, there seems to be little reason to be concerned about inflation – which in most cases is already low, and in others is likely to be quite low in a not too distant future.

Volatility of nominal exchange rates

Under relatively free capital movements the exchange rates in the advanced transition countries tend to appreciate, even in nominal terms, over substantial periods of time (Figures 4a, 4b). Periods of appreciation are often followed by periods of depreciation (usually much shorter). The nominal exchange rate movements generally reflect the movements of capital, including the short-term (or speculative) flows. This description still does not apply to Slovenia, whose currency is managed, and apparently devalued more or less in line with inflation. Of course, there is no nominal appreciation (nor depreciation) in Bulgaria or in Romania (where the exchange rate market is still too shallow to attract speculation).

In the case of the Czech Republic and Slovakia, the recent appreciation has been primarily due to high inflows of 'solid' capital (FDI). The very low interest rates and the on the whole competent management of the exchange rates by the Czech monetary authorities suggest that the role played by short-term capital in the recent appreciation of the Czech currency is probably minimal. Hence also the risk of a sudden outflow (and therefore large depreciation) seems rather low. Additionally, that risk may have been reduced by the recent improvements in the foreign financial position of individual countries (primarily due to the containment of current account deficits).

Figure 3a: Real appreciation*, 2000-2002 (base month January 2000)

national currency vis-à-vis EUR, PPI-deflated

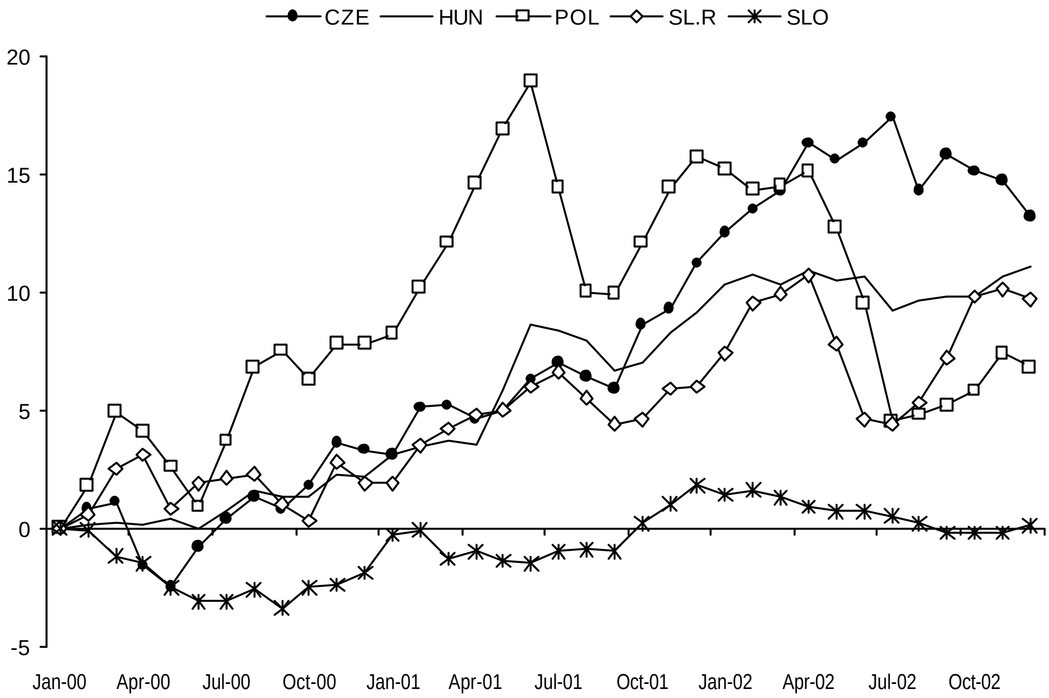
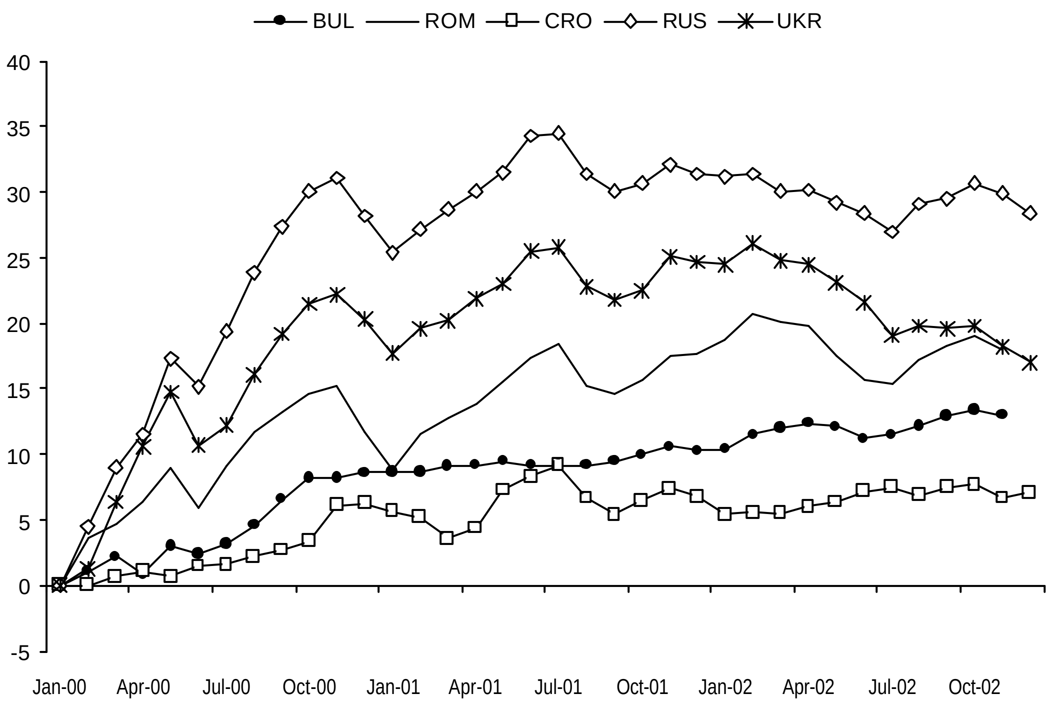


Figure 3b: Real appreciation*, 2000-2002 (base month January 2000)

national currency vis-à-vis EUR, PPI-deflated



Note: * An increasing line means real appreciation.

Source: **wiiw** Monthly Database incorporating national statistics.

Table 16

Foreign financial position

USD billion, end of period

	Gross external debt			Reserves of National Bank (excluding gold) [1]			Current account USD billion				Current account in % of GDP			
	2000	2001	2002	2000	2001	2002	2001	2002	2003 forecast	2004 forecast	2001	2002	2003 forecast	2004 forecast
Czech Republic	21.6	21.7	23.8 [2]	13.1	14.5	23.7	-2.6	-3.2	-3.5	-4.0	-4.6	-4.7	-4.3	-4.7
Hungary	30.7	33.4	38.2 [3]	11.2	10.7	9.7 [3]	-1.1	-3.4	-3.9	-3.7	-2.1	-5.4	-5.1	-4.6
Poland	69.5	71.8	78.7 [2]	26.6	25.6	28.7	-7.2	-6.7	-7.6	-8.5	-3.9	-3.6	-3.7	-4.3
Slovak Republic	10.8	11.0	12.2 [4]	4.1	4.2	9.2	-1.8	-1.9	-1.3	-1.0	-8.6	-8.2	-4.5	-3.3
Slovenia	6.2	6.7	8.2 [3]	3.2	4.3	7.0	0.0	0.4	0.1	0.1	0.2	1.7	0.4	0.4
Bulgaria	11.2	10.6	10.6 [3]	3.2	3.3	4.4	-0.8	-0.7	-0.6	-0.5	-6.2	-4.1	-3.1	-2.3
Romania	10.3	12.0	14.3 [3]	2.5	3.9	6.1	-2.3	-1.8	-2.5	-2.5	-5.8	-4.0	-4.7	-4.6
Croatia	11.0	11.2	14.1 [3]	3.5	4.7	5.9	-0.6	-1.1	-0.9	-0.9	-3.2	-5.0	-3.4	-3.4
Macedonia	1.4	1.4	1.7 [3]	0.4	0.7	.	-0.2	-0.3	-0.3	-0.3	-6.9	-6.9	-5.9	-5.7
Serbia & Montenegro	11.4	11.7	11.5 [2]	0.5	1.2	2.3	-0.6	-2.0	-2.0	-2.0	-5.9	-15.2	-11.8	-10.4
Russia	161.4	151.1	149.7 [2]	28.0	36.6	47.8	34.8	31.7	27.0	25.0	11.2	9.1	7.0	6.0
Ukraine	10.4	12.1	10.8	1.4	3.0	4.4	1.4	2.3	1.0	.	3.7	5.7	2.3	.

Notes: 1) Forex reserves, SDR and reserve position with the IMF. Including gold for the Czech Republic, Russia, Slovakia. Figures for Hungary correspond to total reserves of the country. - 2) September. - 3) November. – 4) October.

Source: **wiiw** Database incorporating national statistics, forecast: **wiiw**.

The relatively low FDI inflows to Poland and recently also to Hungary suggest that the spells of real appreciation happening in these two countries in 2002 may have been caused by inflows of speculative capital. In Poland the monetary policy (high albeit falling interest rates) certainly created incentives for short-term capital movements. Only in mid-2002 (and in January 2003) the Polish currency weakened, most probably under the impact of falling interest rates. A similar development took place in Hungary where the initially strong inflows, induced by high interest rates, forced the NBH into chaotic actions (first an unsuccessful market intervention, followed by cuts in interest rates and an ensuing depreciation).

Overall, the recent exchange rate volatility, which is certainly a function of many variables (economic, psychological and institutional), appears to be linked to the interest rate policies of the National Banks. A practical lesson seems to be that over-ambitious inflation targets (and too high interest rates administered to achieve those targets) are likely to provoke possibly harmful exchange rate volatility.

Figure 4a: Nominal exchange rate movements, 2000-2002 (base month January 2000)

national currency vis-à-vis EUR

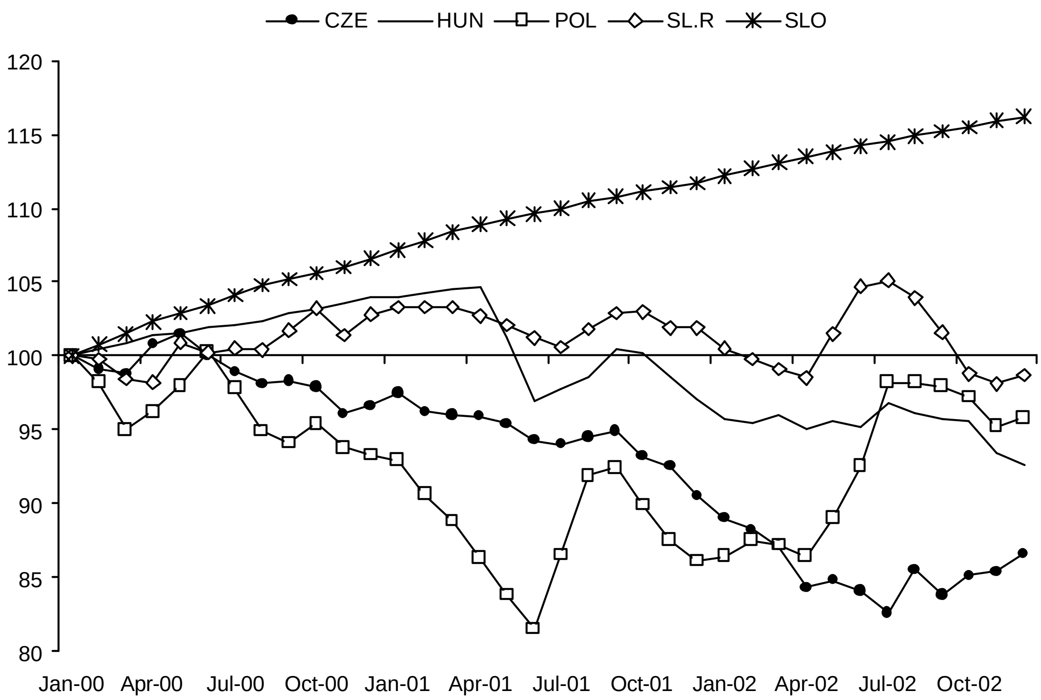
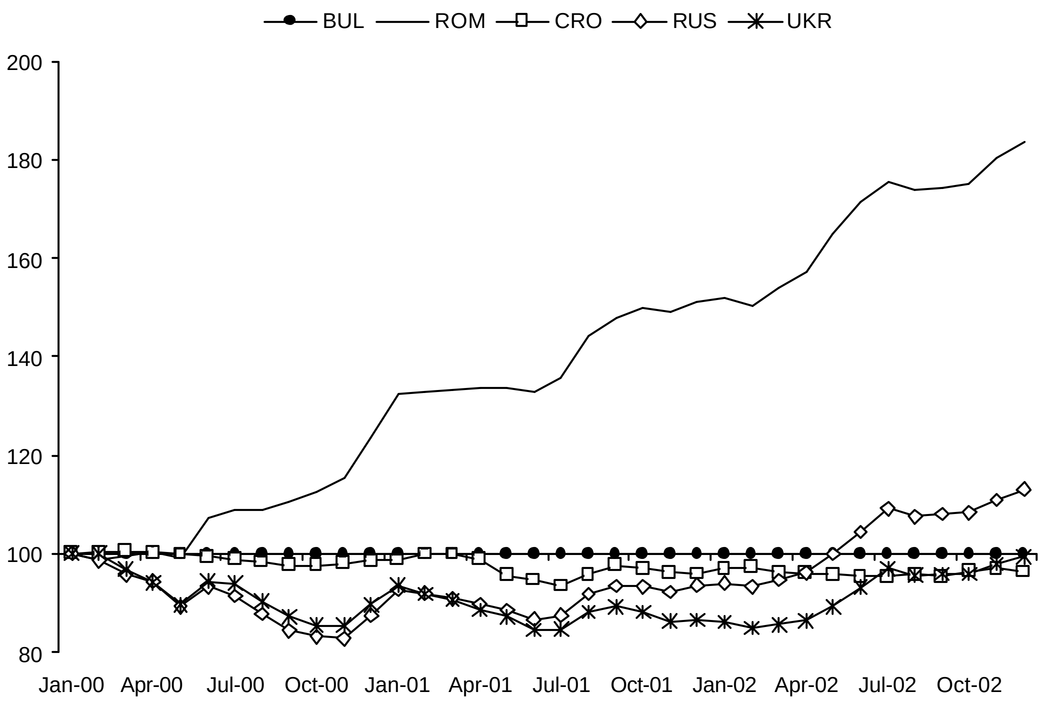


Figure 4b: Nominal exchange rate movements, 2000-2002 (base month January 2000)

national currency vis-à-vis EUR



Source: **wiiw** Monthly Database incorporating national statistics, **wiiw** calculation.

Little progress on unemployment

With labour productivity rising strongly and output growing just moderately there has been very little progress on reducing unemployment. Essentially, no great changes are expected in the near future because GDP growth will remain moderate. Some minor changes in unemployment recorded in the individual countries may reflect demographic developments (and changes in the methods of counting the unemployed) rather than a genuine decline in the number of jobless. The very high unemployment rates in Poland, Slovakia and the post-Yugoslav countries (except Slovenia) will continue to be a major problem. It should be added that high unemployment in most countries is very unevenly distributed among the regions. The unemployment rates in some depressed regions approach 40% or more. Also, the incidence of youth unemployment is very high. Worse still, in countries with high shares of agricultural population (Romania, Bulgaria, Poland, Russia and Ukraine) the potential for further high increases in unemployment is still far from exhausted.

Table 17

Unemployment, LFS definition, annual averages

	in 1000 persons				rate in %					
	1999	**2000**	**2001**	**2002** [1]	**1999**	**2000**	**2001**	**2002**	**2003**	**2004**
									forecast	
Czech Republic	454	455	421	377	8.7	8.8	8.1	7.3	7.5	7.4
Hungary	285	263	233	239	7.0	6.4	5.7	5.8	5.8	5.8
Poland	2391	2785	3170	3449	13.9	16.1	18.2	20.0	20	20
Slovak Republic	417	485	508	498	16.2	18.6	19.2	19.0	18	17
Slovenia	73	68	63	63	7.6	7.0	6.4	6.4	5.5	5.5
CEEC-5 [2]	3620	4055	4395	4626	12.1	13.5	14.5	15.4	15.3	15.1
Bulgaria	534	567	664	592	15.7	16.9	19.7	17.8	18	17
Romania [3]	790	821	750	946	6.8	7.1	6.6	9.0	9	9
CEEC-7 [2]	4944	5443	5809	6164	11.0	12.1	12.9	14.0	14.0	13.8
Croatia	234	298	277	273	13.6	16.1	15.9	15.2	15	15
Macedonia	261	262	263	260	32.4	32.2	30.5	31.9	30	30
Serbia & Montenegro	528	481	490	490	13.7	12.6	12.9	13.0	15	15
Russia	9323	7515	6416	5565	13.0	10.5	9.1	7.8	7.5	8.0
Ukraine	2699	2708	2517	2232	11.9	11.7	11.1	9.8	10	11

Note: 1) Preliminary. - 2) WIIW estimate. - 3) From 2002 new methodology in accordance with EU definitions.

Source: **wiiw** Database incorporating national statistics, forecast: **wiiw**.

Outlook for 2003 and 2004

External conditions, less favourable than in 1999-2001, have been largely responsible for the current growth slowdown. Despite this, the majority of the transition countries managed to grow at respectable rates in 2002. Foreign trade performed surprisingly well, despite the weak EU economy and real appreciation everywhere in the region. This achievement is attributed to the ongoing strong improvements in labour productivity and unit costs. The moderate acceleration of GDP growth expected for 2003 and 2004 primarily reflects the generally shared belief in global economic recovery.

Current account deficits are becoming less of a problem. This is due not only to weaker GDP growth rates than in the late 1990s, but also to the ongoing consolidation of the export sectors. It is expected that the current slowdown in investment activity will be temporary and will not interfere with an expansion of production and export capacities in the near future. In effect the current account deficits should remain relatively low also in 2003 and 2004. We do not expect major problems over financing these deficits. The approaching accession to the EU is likely to bring more FDI while the net transfers from the EU will be rising. However, Russia's current account surpluses will be falling not only on account of lower export revenue, but also due to a steady expansion of imports. One hopes that rising Russian imports will be linked to expanding investment rather than consumption.

Unemployment will remain very high in most countries. It is unlikely to go down significantly even in the medium run. Rather, the expected improvements in labour productivity and profitability may translate into higher and lasting unemployment.

For the accession countries invited to join the EU in 2004, the year 2003 marks the end of 'economic independence'. More than ever before they will have to consult their domestic policies with the EU bureaucracy. This will involve not only benefits but also additional costs and efforts. In particular, the accession countries will be requested to 'reform' their fiscal policies. This is unlikely to support growth and further restructuring, at least in the short run. Besides, the removal of the remaining barriers to trade with the EU and the adoption of the (lower) EU tariffs on imports from third countries will probably increase overall imports and trade deficits of the accession countries. Some industries (especially textiles) will be exposed to rising competition on the domestic markets. On the other hand, one should expect some positive effects (e.g. in the form of higher FDI) already in 2003. However, some marginal doubts persist whether the enlargements will indeed take place in May 2004. This will be decided by referendums to be held in the individual accession countries in the course of 2003. And it is not clear whether the actual accession conditions will turn out to be generous enough to compensate the accession-related costs borne by the accession countries so far. Nevertheless, any delay of membership would be a major setback with gravely negative impacts on economic growth in the coming years. The WIIW forecasts assume no crisis over delayed accession. And, on balance, we reckon that EU membership will have some positive, if only slight, effects on growth already in 2004.

There is much uncertainty over the developments on the Iraqi front. No doubt the global consequences of those developments (and in particular the consequences on the EU economy) will bear on the situation of the transition countries. As long as the course of events has not been determined, the range of possible global outcomes is very broad. Correspondingly, there is much uncertainty about their impacts on the transition countries as well. The impacts of rising oil prices would generally be negative for all transition countries, except Russia. (For quantitative estimates of these impacts see Appendix B.)

Résumés for individual countries

Bulgaria

According to preliminary estimates for 2002 as a whole, GDP increased by more than 4% which was above the official target for the year. This positive outcome was underpinned by the strong performance of the tourist industry and of some manufacturing branches where export-led growth resumed in the third quarter. The banking system seems to be finally recovering from the deep crisis it experienced in 1996-1997 and financial intermediation was gathering speed in 2002. Both the external and internal macroeconomic balances improved and there was some reduction in the level of unemployment. Overall, Bulgaria's economy appears to be in a good shape and, in the absence of major external shocks, moderate to strong growth can be expected to continue.

Czech Republic

The Czech GDP growth rates of 2002 and probably also 2003 will turn out as falling short of the 3.3% level achieved in the years 2000 and 2001. The weak international business climate led to a growth slowdown of exports and imports in euro terms, but did not provoke a major worsening of the current account deficit. The National Bank was able to stop nominal appreciation at least for the time being. In spite of its low lead rates and a relatively high government deficit, inflation was practically non-existent in 2002, and a dramatic rise is not very likely to occur in the next few years. Unemployment is slowly approaching unpleasant west European standards.

Hungary

Despite the relatively good growth performance compared to the EU(15) or the other central European countries, the Hungarian economy in 2002 continued departing from its successful growth path of the period 1997-2000 and was heading towards uncertain waters. Runaway wage increases, huge fiscal imbalance, deteriorating competitiveness and a growing current account deficit call for urgent corrections in 2003. These problems notwithstanding, we expect a modest acceleration of GDP growth.

Poland

Continuing strong contraction of gross fixed investment was compensated in 2002 by rising private consumption out of stagnating household income. Due to strong productivity and cost gains, foreign trade performed quite well. The long-overdue monetary policy relaxation is improving the financial situation of the non-financial sector. The situation remains fragile though because a revival of investment activities need not follow anytime soon.

Romania

With the invitation to join NATO in 2004 and the EU in 2007, the government has achieved its main political targets. While the economic upswing has continued for more than two years now, the question is how lasting it can be if the solving of pressing structural problems is delayed.

Slovakia

The acceleration of GDP growth was mostly driven by private consumption. Despite real appreciation of the currency and depressed demand in the EU, the foreign trade deficit diminished. That supported the economic expansion and reflects increasing competitiveness especially in high-value-added industrial branches. Acquisition dominated the strong FDI inflow which, however, hardly mitigated the persisting unemployment problem. Economic growth will probably continue to be robust in the coming years. But additional currency appreciation may undermine gains in export competitiveness in the long run.

Slovenia

Accelerating exports from the second quarter of the year and the revival of investment growth kept Slovenia on its path of moderate but steady economic growth in 2002. Thanks to a reduction of the trade deficit and higher earnings from services, the current account closed with a remarkable surplus. FDI inflows were the highest in Slovenia's history as an independent state. Combating the persistently high inflation remains one of the main challenges for the country's authorities in the years to come. Based on these generally favourable developments, economic growth can be expected to continue at rates of 3% to 4% in both 2003 and 2004.

Croatia

High GDP growth was driven both by expanding household consumption and rising investment activities. The external sector, in contrast, experienced another disappointing year, reporting the highest trade deficit since the country's gaining independence. The current account deficit nearly doubled compared to 2001 and the foreign debt to GDP ratio exceeded the 60% mark. In 2003 the general economic trends will continue but GDP growth will be somewhat lower due to a contraction of household consumption, following the credit restrictions imposed by the National Bank.

Russian Federation

The GDP growth slowdown continued in 2002 as the trade surplus was falling and investors remained extremely cautious. Structural distortions in the economy are increasing and sound foundations for a sustainable development are still missing. The country continues to be highly dependent on volatile commodity prices. GDP growth is expected to hover around 4% in the coming two years; inflation will gradually decline. This forecast rests on the assumption that no major shift in energy prices will occur; any larger drop in the oil price would substantially alter the GDP and budgetary outlook. In view of the forthcoming parliamentary (December 2003) and presidential elections (Spring 2004) no major reform steps can be expected. The re-election of President Putin – and with it also some degree of political stability – is almost certain.

Ukraine

The Ukrainian economy grew 4.1% in 2002, down from 9.1% in 2001. Growth is forecast to remain at around 4% in 2003 and 2004. Domestic demand remained strong in 2002, but foreign demand was weak, especially in the first half, and exports to Russia fell. Growth rates in industry recovered slightly in the second half. The 2000-01 investment boom faltered, mainly because of the poor business climate. Inflation is forecast to pick up in 2003, increasing pressure on the exchange rate. Some USD 1.53 billion worth of foreign-currency sovereign debt falls due in 2003, as does some USD 500 million of domestic debt; barring new loans, these will take up 22% of government expenditures.

Macedonia

The country has come out of the political crisis with the election of a new government. Modest recovery can be expected in the next couple of years due partly to the fact that significant restructuring of industry and the public sector is necessary. The new government has a chance to turn the country around if it moves energetically.

Serbia & Montenegro

Reforms have slowed down because of the constitutional rearrangement, which does not guarantee that they will be speeded up in the future. Macroeconomic stability has been maintained, though the trade deficit is rising sharply and fiscal pressures are increasing too. There is uncertainty about the supply response in the next couple of years because of the slow institutional change and uncertain prospects for investments.

Table 18

Overview developments 2001-2002 and outlook 2003-2004

	GDP real change in % against previous year				Consumer prices change in % against previous year				Unemployment, based on LFS 1) rate in %, annual average				Current account in % of GDP			
	2001	2002	2003 forecast	2004 forecast	2001	2002	2003 forecast	2004 forecast	2001	2002	2003 forecast	2004 forecast	2001	2002	2003 forecast	2004 forecast
Czech Republic	3.3	2.6	2.8	3.3	4.7	1.8	1.6	2	8.1	7.3	7.5	7.4	-4.6	-4.7	-4.3	-4.7
Hungary	3.7	3.3	3.8	4	9.2	5.3	5.3	5	5.7	5.8	5.8	5.8	-2.1	-5.4	-5.1	-4.6
Poland	1.0	1.3	2	3	5.5	1.9	2	3	18.2	20	20	20	-3.9	-3.6	-3.7	-4.3
Slovak Republic	3.3	4.2	3.5	4.5	7.1	3.3	7	7	19.2	19	18	17	-8.6	-8.2	-4.5	-3.3
Slovenia	3.0	3	3.3	4	8.4	7.5	6	5.5	6.4	6.4	5.5	5.5	0.2	1.7	0.4	0.4
CEEC-5	2.2	2.2	2.7	3.4	7.0	4.0	4.4	4.5	14.5	15.4	15.3	15.2	-3.8	-4.1	-3.9	-4.1
Bulgaria	4.0	4.3	4.5	5	7.4	5.8	4	4	19.7	17.8	18	17	-6.2	-4.1	-3.1	-2.3
Romania	5.3	4.5	4	4	34.5	22.5	18	15	6.6	9	9	9	-5.8	-4.0	-4.7	-4.6
CEEC-7	2.7	2.7	3.0	3.6	11.0	6.9	6.3	5.9	12.9	14.0	14.0	13.9	-4.1	-4.1	-4.0	-4.0
Croatia 2)	3.8	4.5	4	4.5	4.9	2.2	3	2.5	15.9	15.2	15	15	-3.2	-5.0	-3.4	-3.4
Macedonia 2)	-4.6	0	2	3	5.2	1.5	2	4	30.5	31.9	30	30	-6.9	-6.9	-5.9	-5.7
Serbia & Montenegro 3)	5.1	3.0	4	4	89.0	16.5	15	10	12.9	13	15	15	-5.9	-15.2	-11.8	-10.4
Russia	5.0	4.3	4	4	21.6	16.0	12	10	9.1	7.8	7.5	8	11.2	9.1	7.0	6.0
Ukraine	9.1	4.1	4	4	12.0	0.8	10	7	11.1	9.8	10	11	3.7	5.7	2.3	.

Notes: 1) LFS - Labour Force Survey, refers to ILO definition. - 2) Consumer prices correspond to retail prices. - 3) Excluding Kosovo and Metohia.

Source: **wiiw** (February 2003).

Appendix A

Price/quality gap indicators for EU exports of the accession countries

The price/quality gap indicator compares the price level of CEECs' exports to the EU with the price level of overall EU imports in the same product category. The price levels are measured as unit values (value per kilo of exports) and the indicators in the standardized form presented here show the percentage deviation of CEECs' export unit values from the average EU import unit values in the respective product category.[2] Under certain conditions ('law of one price') these indicators can be interpreted as differences in product quality. A positive value of the price/quality gap indicator (PQ indicator) in Table A/1 thus points to a relatively higher price and probably higher quality of CEECs' exports compared to other competitors on the EU market in the product group under consideration. A negative value indicates below-average price/quality.

In 2000/2001 the price/quality gap indicators were negative for manufacturing exports as a whole and for most individual product groups as well, pointing towards lower than average quality of CEECs' exports to the EU in most fields. The only important exception is Hungary, where positive PQ indicators suggest relatively high quality for manufacturing exports as a whole and for certain industries in particular – textiles (DB), leather & leather products (DC), electrical & optical equipment (DL), transport equipment (DM) and manufacturing n.e.c. (DN).

The quality level of CEECs' exports to the EU seems to be especially low in machinery & equipment (DK) and rubber & plastic products (DH). On the other hand, if compared to the level of total manufacturing, the quality level is relatively high in many countries for textiles & textile products (DB) and leather & leather products (DC; with the exception of Romania). Broadly speaking, in the technology-intensive sectors the CEECs seem to concentrate on the low price/quality segment mainly while in the labour-intensive industries they have specialized in the high quality segment rather.

From a dynamic perspective, PQ indicators increased significantly for all CEECs over the period 1995-2001, indicating substantial catching-up in export prices and upgrading the quality of exports to the EU, respectively. The rise of PQ indicators was very pronounced in textiles, leather and leather product, rubber & plastic products, machinery & equipment,

2 For each country and industry, we start with calculating unit values ratios at the most detailed (8-digit) level of the Eurostat COMEXT trade database. We then aggregate the unit value ratios to the level of (3-digit NACE) industries and further to the 14 NACE industries. This is done (for each country) by constructing a weighed sum of the unit value ratios across the products belonging to a particular industry. The weight used for a particular commodity in such an aggregation is the share of its export value in the industry's exports. See P. Havlik, M. Landesmann and R. Stehrer, 'Competitiveness of CEE Industries: Evidence from Trade Specialization and Quality Indicators', *wiiw Resarch Reports*, No. 278, July 2001, for a more detailed presentation of the methodology.

electrical & optical equipment and manufacturing n.e.c. Notably, in most countries the increase of PQ indicators was accompanied by rising EU market shares[3] in the respective field, pointing to improved quality rather than rising relative prices impairing (cost) competitiveness. However, the picture is different in the case of textiles and leather & leather products where EU market shares declined for many CEECs, indicating declining (price) competitiveness, probably because rising prices were not equally matched by quality or rising quality was priced too high. For textiles & textile products this was the case, for instance, in Hungary, Poland and Slovenia, and for leather & leather products in the Czech Republic, in Hungary, Poland, Slovenia[4], Latvia and Lithuania. From this we may conclude that the high PQ indicators for textiles and leather & leather products probably represent a problem for some countries rather than an advantage.

3 Share of CEECs' exports in total (extra) EU imports of a certain product group.

4 Notably, Slovenia shows a decline of EU market shares in most industries independent of the development of PQ indicators.

Table A/1

Price/Quality gap indicators for individual industries, average 2000/2001[1)]

in %

		Bulgaria	Czech Republic	Hungary	Poland	Romania	Slovak Republic	Slovenia	Estonia	Latvia	Lithuania
D	**Manufacturing total**	**-16.5**	**-16.4**	**7.3**	**-14.9**	**-12.8**	**-10.3**	**-3.8**	**-4.0**	**-11.9**	**-10.0**
DA	Food products; beverages and tobacco	-5.6	-20.1	4.5	-3.3	6.9	-18.5	4.4	-4.8	-8.6	9.4
DB	Textiles and textile products	-16.5	2.0	25.3	11.2	-2.9	15.7	46.5	5.1	0.6	-2.7
DC	Leather and leather products	-7.3	-5.0	22.9	8.2	-19.6	17.1	13.8	-0.5	15.6	1.4
DD	Wood and wood products	-21.0	-24.3	-29.1	-32.4	-15.2	-19.3	8.9	-15.2	-22.2	-36.0
DE	Pulp, paper & paper products; publishing & printing	-13.1	-13.4	-15.9	-9.9	-13.1	-23.1	-16.8	-0.4	14.8	-23.2
DF	Coke, refined petroleum products & nuclear fuel	-2.8	2.3	2.9	0.4	2.8	-0.9	47.6	-5.1	-1.8	-4.6
DG	Chemicals, chemical products and man-made fibres	-8.7	-13.9	-5.5	-11.2	-8.5	-16.0	-12.2	-8.5	-8.8	-1.0
DH	Rubber and plastic products	-44.3	-18.6	-3.2	-28.2	-27.4	-23.8	-9.6	1.1	0.1	-38.8
DI	Other non-metallic mineral products	-34.5	-13.5	1.1	-20.8	-25.5	-11.9	-11.6	-9.4	-30.2	-22.8
DJ	Basic metals and fabricated metal products	-7.6	-16.2	-4.6	-14.7	-14.0	-11.3	-6.0	9.8	3.9	-7.7 [2)]
DK	Machinery and equipment n.e.c.	-47.7	-38.9	-27.2	-44.7	-42.4	-35.5	-22.0	-44.7	-36.4	-31.2
DL	Electrical and optical equipment	-30.3	-14.0	13.1	-13.9	-13.0	-15.1	-12.8	7.8	-5.8	-22.7
DM	Transport equipment	-34.5	-9.8	14.9	-6.0	18.8	2.3	-12.2	9.9	13.9	-14.3
DN	Manufacturing n.e.c.	-33.3	-8.2	12.8	-31.3	-33.2	-29.7	39.6	-16.3	-24.6	-32.2

Notes: 1) Defined as the unit value ratio uvr_j^c of industry j in country c, which shows the percentage deviation from the average EU import unit value in industry j. - 2) Adjusted for waste and scrap of platinum and waste and scrap of precious metals.

Source: Calculations by R. Stehrer, **wiiw**.

Table A/2

Price/quality gap indicators for individual industries, change 1995-2001[1)]

in percentage points

		Bulgaria	Czech Republic	Hungary	Poland	Romania	Slovak Republic	Slovenia	Estonia	Latvia	Lithuania
D	**Manufacturing total**	**8.6**	**7.6**	**13.5**	**7.4**	**15.4**	**9.4**	**1.9**	**13.9**	**4.0**	**11.5**
DA	Food products; beverages and tobacco	-3.5	-1.8	2.0	2.4	15.6	-17.4	8.0	-1.2	-2.8	17.9
DB	Textiles and textile products	10.9	10.6	17.9	14.3	19.6	27.0	11.3	14.2	22.9	26.7
DC	Leather and leather products	29.0	3.4	19.8	13.9	7.7	13.1	-5.6	8.9	14.1	8.5
DD	Wood and wood products	17.2	5.3	-6.0	2.5	12.5	6.9	2.7	-3.1	12.0	8.2
DE	Pulp, paper & paper products; publishing & printing	5.6	5.3	14.3	12.6	2.6	0.0	2.2	21.0	33.0	6.5
DF	Coke, refined petroleum products & nuclear fuel	1.7	2.7	1.1	7.7	0.3	-4.1	69.2	0.6	1.0	-2.2
DG	Chemicals, chemical products and man-made fibres	4.9	-8.1	4.0	1.4	4.2	1.0	4.6	0.6	8.6	4.4
DH	Rubber and plastic products	6.1	14.9	14.7	10.4	18.5	7.3	10.7	16.8	47.7	16.7
DI	Other non-metallic mineral products	12.2	1.9	-0.5	4.2	5.3	3.8	9.3	5.4	-2.1	-7.7
DJ	Basic metals and fabricated metal products	7.4	1.8	4.0	-3.4	7.9	3.8	2.3	8.6	3.4	4.1 [2)]
DK	Machinery and equipment n.e.c.	9.9	9.2	12.4	13.3	16.9	14.5	8.7	-4.5	10.1	15.9
DL	Electrical and optical equipment	13.7	12.6	20.7	13.1	31.6	17.7	11.0	50.7	17.5	-7.2
DM	Transport equipment	7.4	25.5	8.0	21.8	-0.1	8.0	-18.1	34.8	45.0	21.4
DN	Manufacturing n.e.c.	8.8	0.9	24.4	10.5	18.3	14.8	32.8	23.6	16.7	23.1

Notes: 1) Average PQ gap indicator 2000/2001 minus average PQ indicator 1995/1996. - 2) Adjusted for waste and scrap of platinum and waste and scrap of precious metals.

Source: Calculations by R. Stehrer, **wiiw**.

Appendix B

by Vasily Astrov

The looming war with Iraq and possible economic consequences for transition countries

The short-term forecasting of economic developments in transition countries is complicated by the uncertainty regarding the oil prices in the coming months. The plans of the US government to launch a war against Iraq have already brought about an increase in the world price of oil, which now trades at above USD 30 per barrel. None of the countries of the region (with the major exception of Russia) has sufficient own oil production to cover domestic needs, and crude oil and oil products account for an important part of their imports. True, as can be seen from Table B/1, the role of oil in primary energy consumption of most CEECs is fairly modest as compared e.g. to the more advanced countries such as Germany or the USA.[5] Nor is the PPP-adjusted oil intensity of production particularly high – with the exception of Russia (column 2 of Table B/1). However, when measured at market exchange rates (column 3), the oil intensity of transition economies appears much higher, and it is this parameter which makes them vulnerable to the oil price volatility. An oil price shock, if it happens, will be a fairly heavy burden on their relatively small economies.

Obviously, the impact of rising world oil prices on oil-importing (most countries of the region) and oil-exporting countries (in the first place Russia, but also Kazakhstan and Azerbaidzhan) will be the opposite. In the case of most CEE countries, the rising price of imported oil will affect the costs of production and thus translate into higher prices. In turn, higher prices will bring about a decline in the level of aggregate demand. Therefore, the likely outcome in these countries will be a combination of a slowdown in the growth of GDP and higher inflation. In the case of Russia, where crude oil accounts for a quarter and all energy carriers for half of exports, the 'windfall profits' of oil companies will, via the multiplier effect, further stimulate demand and thus accelerate economic growth, at least in the short run. At the same time, inflation may follow as well, especially because higher world prices will put an upward pressure on already very low domestic prices for oil.

Table B/2 presents some back-of-the-envelope estimates of the impact the looming war with Iraq might have on the GDP and external balances of the countries of the region due to a spike in world oil prices. We base our calculations on the assumption that the average world oil price in 2003 will stand at USD 30 per barrel, which represents a growth of USD 6.5 per barrel against 2002.[6] In fact, this is a rather conservative assumption, given

5 Primary energy consumption includes energy consumption in refineries, heating plants, and electric power stations.

6 The average world price of crude oil (spot price, weighted by estimated export volumes, f.o.b.) in the year 2002 stood at USD 23.5 per barrel. Therefore, our assumption of a USD 30 price for the year 2003 implies a price increase of 27.7% against the previous year. In fact, the major oil blend being imported by the countries in question – the Urals blend coming from Russia – traded in 2002 somewhat above the world average price (albeit e.g. below the Brent oil of the UK). However, it seems reasonable to assume that the price for Urals in relative terms will increase at the same pace as the world average price, and we base our calculations on this assumption.

that oil already now trades at above USD 30 per barrel, and is based on the 'benign' scenario of war. Although the war itself will be most probably accompanied by a sharp rise in oil price – e.g. to USD 40 per barrel, a fairly brief military campaign followed by a victory of the US-led coalition, quick removal of the present Iraqi leadership and the absence of hostile measures on the part of other Middle Eastern countries vis-à-vis the US, will prove an important stabilizing effect and will exert a considerable downward pressure on oil prices subsequently. Most importantly, the 'benign' scenario assumes no major damage to Iraqi oil facilities (be it due to the war itself, or to a possible 'revenge'-related deliberate destruction of facilities by the regime of Saddam Hussein) and hence no substantial disruptions to oil deliveries from Iraq and the adjacent countries. If the war is brief and victorious and Iraqi oil capacity remains intact, the production of oil in Iraq will almost certainly rise from the current level of some 2.5 million barrels per day – either to 2.8 million barrels per day, which corresponds to the old share allotted to Iraq in OPEC, or even more than that, which is realistic in case the country is fully controlled by the occupier, who may want to push Iraq out of OPEC. Therefore, it is not impossible that the world oil price may decline substantially by the end of the year, say, to levels between USD 20 and 25 per barrel, so that the assumption of an average annual price of USD 30 can be justified.

In the short run (which we are primarily interested in), the demand for oil of the oil-importing countries of the region is price-inelastic so that the 'oil bill' these countries have to pay rises along with the world price. Similarly, Russia, which will benefit from the new oil price spike, will be unable to raise its production (and export) volumes in the short run – mainly due to bottlenecks in its exporting capacity.

According to our calculations, higher oil prices and the related deterioration in the current account will bring about a decline in real GDP[7] in all countries of the region, except Russia. The current account deficit of oil-importing countries will deteriorate, in some cases (such as in that of Slovakia and Serbia and Montenegro) by more than 1 percentage point, accounting for a decline in real GDP of a similar magnitude. The impact on Romania (which covers half of its oil consumption through domestic production) and the more advanced CEE countries, which are relatively less dependent on oil, will be more limited. Ukraine will be hit the hardest (–1.3% drop in real GDP), though it will still be able to maintain its current account surplus. In turn, Russian GDP would rise by nearly 2 percentage points.

7 We assume constant real exchange rates of respective currencies against the US dollar.

Table B/1

Selected indicators of oil dependence, year 2000

	Share of oil in primary energy consumption, %	Oil intensity of GDP (barrels per 1 mn dollar of GDP at PPP)	Oil intensity of GDP (barrels per 1 mn dollar of GDP at ER)
	2000	**2000**	**2000**
Czech Republic	23.1	423	1166
Hungary	28.3	425	1136
Poland	24.4	438	1024
Slovak Republic	17.4	391	1209
Slovenia	39.9	599	1111
Bulgaria	20.6	582	2673
Romania	25.8	554	1935
Croatia	46.2	821	1748
Macedonia	31.7	520	1938
Russia	18.6	954	3524
Ukraine	11.5	657	4215
Austria	38.9	438	508
Germany	41.0	476	543
Japan	51.5	614	425
USA	38.9	730	730

Source: **wiiw** calculations based on data taken from EIA and the **wiiw** Database.

Table B/2

The implications of an oil price surge on transition economies

	Net imports of oil and oil products mn USD per day[1)]	Additional annual oil bill in 2003 based on assump. of USD 30 per barrel, USD mn	% change in real GDP[5)] due to oil price shock, proj.	Current account as % of GDP, with oil price shock, proj.	Change in CA, due to oil price shock, proj. perc. points of GDP
	2002	**2003**	**2003**	**2003**	**2003**
Czech Republic	3.8	389	-0.5	-4.8	-0.5
Hungary	1.9	191	-0.2	-5.4	-0.3
Poland	8.0	805	-0.4	-4.1	-0.4
Slovak Republic[2)]	3.2	319	-1.1	-5.7	-1.2
Slovenia	1.4	145	-0.6	-0.2	-0.6
Romania	1.1	112	-0.2	-4.9	-0.2
Croatia	1.8	178	-0.7	-4.1	-0.7
Macedonia[3)]	0.2	20	-0.5	-6.4	-0.5
Serbia & Montenegro[3)]	1.8	182	-1.1	-13.0	-1.2
Russia[4)]	-73.2	-7403	1.9	8.8	1.8
Ukraine[4)]	5.6	571	-1.3	1.0	-1.3

Notes: 1) Based on the latest available statistics for the largest available number of months of the year 2002. - 2) Including natural gas. - 3) Gross imports. - 4) Crude oil only. - 5) Based on the assumption of constant real exchange rate of respective currency against the USD.

Source: **wiiw** calculations and forecasts based on national statistics.

Appendix C

Selected Indicators of Competitiveness

Table C/1 GDP per capita at current PPPs (EUR/ECU), from 2003 at constant PPPs

	1990	1995	1998	1999	2000	2001	2002	2003	2004	2005	2010	2015
											projection assuming 4% p.a. GDP growth and zero population growth p.a.	
Czech Republic	10088	11281	12218	12542	13321	14138	14836	15251	15755	16385	19935	24254
Hungary	7229	8236	9743	10385	11247	11947	12615	13095	13618	14163	17232	20965
Poland	4593	6302	7785	8269	8834	9484	9805	10001	10301	10713	13034	15858
Slovak Republic	7507	8235	10156	10487	10996	11654	12382	12816	13392	13928	16946	20617
Slovenia	10152	11607	13546	14516	15558	16363	17159	17725	18434	19172	23325	28379
Bulgaria	4879	5004	5722	6005	6532	7076	7645	7989	8388	8724	10614	12913
Romania	5357	5768	4970	5054	5289	5699	5980	6219	6468	6726	8184	9957
Estonia	.	5927	8032	8203	9065	9771	10380	10951	11553	12016	14619	17786
Latvia	7148	4407	5850	6070	6741	7467	7987	8467	8975	9334	11356	13816
Lithuania	7401	5091	7412	7318	7855	8543	9121	9622	10171	10578	12869	15657
Croatia	6003	5214	7518	7511	8147	8643	9228	9597	10029	10430	12689	15439
Macedonia	3958	3769	5380	5696	6085	5905	6012	6132	6316	6569	7992	9723
Russia	8468	6157	5001	5399	6075	6555	7000	7295	7608	7912	9627	11712
Ukraine	5899	3324	3316	3403	3732	4216	4528	4709	4897	5093	6197	7539
											projection assuming 2% p.a. GDP growth and zero population growth p.a.	
Austria	16007	19937	22466	23589	24867	25363	26355	26882	27420	27968	30879	34093
Germany	14243	19890	21689	22585	23836	24169	24864	25362	25869	26386	29133	32165
Greece	8846	11924	13732	14546	15500	15646	16555	16886	17224	17569	19397	21416
Portugal	9399	12840	14843	15668	16551	16912	17508	17858	18215	18580	20513	22648
Spain	11543	14141	16516	17574	18750	19438	20412	20821	21237	21662	23916	26405
Turkey	4433	5239	5739	5477	5857	5332	5708	5822	5939	6057	6688	7384
Japan	17297	21675	22394	22889	23915	24067	24349	24836	25333	25840	28529	31498
USA	21936	26141	29704	31173	33021	33506	35277	35983	36702	37437	41333	45635
EU(15) average	14647	18182	20422	21391	22622	23119	23582	24053	24534	25025	27630	30505

European Union (15) average = 100

	1990	1995	1998	1999	2000	2001	2002	2003	2004	2005	2010	2015
Czech Republic	69	62	60	59	59	61	63	63	64	65	72	80
Hungary	49	45	48	49	50	52	53	54	56	57	62	69
Poland	31	35	38	39	39	41	42	42	42	43	47	52
Slovak Republic	51	45	50	49	49	50	53	53	55	56	61	68
Slovenia	69	64	66	68	69	71	73	74	75	77	84	93
Bulgaria	33	28	28	28	29	31	32	33	34	35	38	42
Romania	37	32	24	24	23	25	25	26	26	27	30	33
Estonia	.	33	39	38	40	42	44	46	47	48	53	58
Latvia	.	24	29	28	30	32	34	35	37	37	41	45
Lithuania	.	28	36	34	35	37	39	40	41	42	47	51
Croatia	41	29	37	35	36	37	39	40	41	42	46	51
Macedonia	27	21	26	27	27	26	25	25	26	26	29	32
Russia	58	34	24	25	27	28	30	30	31	32	35	38
Ukraine	40	18	16	16	16	18	19	20	20	20	22	25
Austria	109	110	110	110	110	110	112	112	112	112	112	112
Germany	97	109	106	106	105	105	105	105	105	105	105	105
Greece	60	66	67	68	69	68	70	70	70	70	70	70
Portugal	64	71	73	73	73	73	74	74	74	74	74	74
Spain	79	78	81	82	83	84	87	87	87	87	87	87
Turkey	30	29	28	26	26	23	24	24	24	24	24	24
Japan	118	119	110	107	106	104	103	103	103	103	103	103
USA	150	144	145	146	146	145	150	150	150	150	150	150
EU(15) average	100	100	100	100	100	100	100	100	100	100	100	100

Sources: Benchmark Results of the 1996 Eurostat-OECD Comparison by Analytical Categories, OECD, 1999; Purchasing Power Parities and Real Expenditures, 1999 Benchmark Year, OECD, 2002; National statistics; WIFO; **wiiw** estimates.

Benchmark PPPs for 1996 and 1999 extrapolated with GDP price deflators. GDP per capita for OECD countries according to OECD Economic Outlook statistics converted into EUR.

Table C/2

Indicators of macro-competitiveness, 1995-2002

EUR-based (ECU until1998), annual averages

	1995	1996	1997	1998	1999	2000	2001	2002 prelim.
Czech Republic								
Producer price index, 1989=100	241.6	253.0	265.4	278.4	281.2	295.0	303.6	302.0
Consumer price index, 1989=100	276.7	301.0	326.6	361.6	369.2	383.6	401.6	408.8
GDP deflator, 1989=100	253.5	275.8	297.8	329.5	339.1	342.5	360.2	366.3
Exchange rate (ER), CZK/EUR	34.31	34.01	35.80	36.16	36.88	35.61	34.08	30.81
ER nominal, 1989=100	206.7	204.9	215.7	217.9	222.2	214.5	205.3	185.6
Real ER (CPI-based), 1989=100	95.8	89.5	88.6	82.2	83.2	79.3	74.3	67.4
Real ER (PPI-based), 1989=100	98.4	93.8	95.0	91.2	92.1	88.7	83.6	75.9
PPP, CZK/EUR	11.85	12.68	13.39	14.62	14.75	14.51	14.93	14.88
ERDI (EUR based)	2.90	2.68	2.67	2.47	2.50	2.46	2.28	2.07
Average monthly gross wages, CZK	8172	9676	10691	11693	12666	13499	14640	15740
Average monthly gross wages, EUR (ER)	238	285	299	323	343	379	430	511
Average monthly gross wages, EUR (PPP)	690	763	799	800	859	931	981	1057
GDP nominal, bn CZK	1381.0	1567.0	1679.9	1839.1	1902.3	1984.8	2157.8	2250
Employment total, 1000 persons	4962.6	4972.0	4936.5	4865.7	4764.1	4731.6	4750.2	4796
GDP per employed person, CZK	278291	315158	340306	377970	399297	419485	454260	469141
GDP per empl. person, CZK at 1999 pr.	372270	387489	387428	388931	399297	415355	427631	434257
Unit labour costs, 1989=100	227.9	259.3	286.5	312.2	329.4	337.5	355.5	376.4
Unit labour costs, ER adj., 1989=100	110.3	126.5	132.9	143.3	148.2	157.3	173.1	202.7
Unit labour costs, PPP adj., Austria=100	20.99	24.97	27.32	29.78	30.40	32.27	34.99	40.88
Hungary								
Producer price index, 1989=100	286.7	349.2	420.4	467.9	491.8	548.8	577.3	567.0
Consumer price index, 1989=100	399.3	493.5	583.8	667.3	734.0	805.9	880.1	926.7
GDP deflator, 1989=100	348.8	422.7	500.9	564.1	611.4	670.9	729.3	771.6
Exchange rate (ER), HUF/EUR	162.65	191.15	210.93	240.98	252.80	260.04	256.68	242.97
ER, nominal 1989=100	250.0	293.8	324.2	370.3	388.5	399.6	394.5	373.4
Real ER (CPI-based), 1989=100	80.3	78.2	74.5	75.8	73.2	70.3	65.1	59.8
Real ER (PPI-based), 1989=100	100.3	97.4	90.1	92.2	92.0	88.8	84.4	81.3
PPP, HUF/EUR	65.99	78.67	90.73	100.85	107.17	114.51	121.79	126.33
ERDI (EUR based)	2.46	2.43	2.32	2.39	2.36	2.27	2.11	1.92
Average monthly gross wages, HUF	38900	46837	57270	67764	77187	87645	103553	121990
Average monthly gross wages, EUR (ER)	239	245	272	281	305	337	403	502
Average monthly gross wages, EUR (PPP)	589	595	631	672	720	765	850	966
GDP nominal, bn HUF	5614.0	6893.9	8540.7	10087.4	11393.5	13150.8	14823.9	16200
Employment total, 1000 persons	3678.8	3648.1	3646.3	3697.7	3811.5	3849.1	3859.5	3862
GDP per employed person, HUF	1526041	1889723	2342292	2728020	2989243	3416583	3840886	4194718
GDP per empl. person, HUF at 1999 pr.	2675150	2733209	2858722	2956947	2989243	3113412	3220026	3323877
Unit labour costs, 1989=100	277.2	326.6	381.9	436.8	492.2	536.6	613.0	699.6
Unit labour costs, ER adj., 1989=100	110.9	111.2	117.8	118.0	126.7	134.3	155.4	187.4
Unit labour costs, PPP adj., Austria=100	21.31	22.16	24.46	24.75	26.23	27.81	31.71	38.14
Poland								
Producer price index, 1989=100	2837.2	3189.0	3578.0	3839.6	4058.4	4375.0	4445.0	4489.4
Consumer price index, 1989=100	3818.1	4577.9	5260.0	5880.7	6309.9	6947.2	7329.3	7468.5
GDP deflator, 1989=100	2690.0	3194.4	3642.9	4073.4	4348.3	4655.9	4849.1	4914.3
Exchange rate (ER), PLN/EUR	3.135	3.377	3.706	3.923	4.227	4.011	3.669	3.856
ER, nominal, 1989=100	1966.1	2118.3	2324.1	2460.5	2651.1	2515.7	2300.9	2418.3
Real ER (CPI-based), 1989=100	66.0	60.8	59.3	57.1	58.1	51.3	45.6	48.0
Real ER (PPI-based), 1989=100	79.7	76.9	75.9	74.7	76.1	70.2	64.0	66.5
PPP, PLN/EUR	1.2669	1.4797	1.6659	1.8389	1.9245	2.0065	2.0447	2.0316
ERDI (EUR based)	2.47	2.28	2.22	2.13	2.20	2.00	1.79	1.90
Average monthly gross wages, PLN *)	691	874	1066	1233	1697	1894	2045	2277
Average monthly gross wages, EUR (ER)	220	259	288	314	401	472	557	591
Average monthly gross wages, EUR (PPP)	545	591	640	670	882	944	1000	1121
GDP nominal, bn PLN	308.1	387.8	472.4	553.6	615.1	685.0	749.3	769.4
Employment total, 1000 persons	14735.2	15020.6	15438.7	15800.4	15373.5	15017.5	14923.6	14900
GDP per employed person, PLN	20909	25820	30595	35035	40011	45612	50210	51638
GDP per empl. person, PLN at 1999 pr.	33799	35146	36520	37398	40011	42599	45024	45690
Unit labour costs, 1989=100	2991.2	3640.0	4270.3	4823.1	6206.6	6505.0	6646.5	7292.3
Unit labour costs, ER adj., 1989=100	152.1	171.8	183.7	196.0	234.1	258.6	288.9	301.6
Unit labour costs, PPP adj., Austria=100	27.91	32.69	36.42	39.26	46.27	51.13	56.27	58.61

*) Methodological change in 1999 (broader wage coverage).

(Table C/2 ctd.)

(Table C/2 ctd.)

	1995	1996	1997	1998	1999	2000	2001	2002 prelim.
Slovak Republic								
Producer price index, 1989=100	262.6	273.5	285.8	295.3	307.9	341.2	363.4	371.1
Consumer price index, 1989=100	300.5	317.8	337.2	359.8	397.9	445.6	477.2	493.0
GDP deflator, 1989=100	230.0	240.1	256.2	269.5	286.8	305.2	321.6	329.4
Exchange rate (ER), SKK/EUR	38.45	38.40	38.01	39.60	44.12	42.59	43.31	42.69
ER, nominal, 1989=100	231.7	231.4	229.0	238.6	265.8	256.6	260.9	257.2
Real ER (CPI-based), 1989=100	98.8	95.7	91.1	90.5	92.3	81.6	79.4	77.4
Real ER (PPI-based), 1989=100	101.5	97.9	93.7	94.1	100.6	91.7	88.7	85.6
PPP, SKK/EUR	12.88	13.22	13.63	14.16	14.77	15.30	15.78	15.84
ERDI (EUR based)	2.99	2.90	2.79	2.80	2.99	2.78	2.74	2.69
Average monthly gross wages, SKK	7195	8154	9226	10003	10728	11430	12365	13520
Average monthly gross wages, EUR (ER)	187	212	243	253	243	268	286	317
Average monthly gross wages, EUR (PPP)	559	617	677	707	726	747	784	853
GDP nominal, bn SKK	568.9	628.6	708.6	775.0	835.7	908.8	989.3	1055.0
Employment total, 1000 persons	2146.8	2224.9	2205.9	2198.6	2132.1	2101.7	2123.7	2125
GDP per employed person, SKK	265010	282524	321237	352498	391971	432412	465837	496471
GDP per empl. person, SKK at 1999 pr.	330547	337573	359676	375146	391971	406380	415443	432385
Unit labour costs, 1989=100	215.7	239.4	254.2	264.2	271.2	278.7	294.9	309.8
Unit labour costs, ER adj., 1989=100	93.1	103.5	111.0	110.7	102.0	108.6	113.0	120.5
Unit labour costs, PPP adj., Austria=100	18.60	21.42	23.95	24.15	21.95	23.38	23.97	25.49
Slovenia								
Producer price index, 1989=100	5601.3	5982.4	6347.2	6727.8	6869.0	7391.3	8048.9	8459.4
Consumer price index, 1989=100	7857.9	8635.7	9360.9	10100.5	10716.2	11670.2	12650.2	13598.9
GDP deflator, 1989=100	6868.3	7633.5	8303.1	8953.7	9542.1	10089.7	11084.3	11915.6
Exchange rate (ER), SIT/EUR	153.12	169.51	180.40	186.27	193.63	205.03	217.19	226.22
ER, nominal, 1989=100	4745.5	5253.6	5591.0	5772.9	6001.0	6354.5	6731.1	7011.3
Real ER (CPI-based), 1989=100	77.4	79.9	80.1	78.0	77.4	77.2	77.3	76.5
Real ER (PPI-based), 1989=100	97.4	101.7	103.0	100.0	101.8	104.9	103.4	102.3
PPP, SIT/EUR	96.30	105.26	113.81	121.15	126.58	130.33	140.09	147.64
ERDI (EUR based)	1.59	1.61	1.59	1.54	1.53	1.57	1.55	1.53
Average monthly gross wages, SIT	111996	129125	144251	158069	173245	191669	214561	234940
Average monthly gross wages, EUR (ER)	731	762	800	849	895	935	988	1039
Average monthly gross wages, EUR (PPP)	1163	1227	1268	1305	1369	1471	1532	1591
GDP nominal, bn SIT	2221.5	2555.4	2907.3	3253.8	3648.4	4035.5	4566.2	5056
Employment total, 1000 persons	745.2	741.7	743.4	745.2	758.5	768.2	779.0	784
GDP per employed person, SIT	2980876	3445175	3910621	4366460	4810186	5253404	5861297	6451323
GDP per empl. person, SIT at 1999 pr.	4141304	4306585	4494177	4653422	4810186	4968295	5045826	5166290
Unit labour costs, 1989=100	4492.9	4981.2	5332.5	5643.3	5983.5	6409.2	7064.4	7555.0
Unit labour costs, ER adj., 1989=100	94.7	94.8	95.4	97.8	99.7	100.9	105.0	107.8
Unit labour costs, PPP adj., Austria=100	49.72	51.63	54.12	56.05	56.42	57.09	58.53	59.96
Bulgaria								
Producer price index, 1989=100	2454.4	5645.0	60462.0	70468.5	72723.6	85159.3	91376.0	94025.9
Consumer price index, 1989=100	5702.9	12637.6	146392.9	173732.5	178203.6	196584.0	211132.0	223377.8
GDP deflator, 1989=100	2897.2	6399.9	67110.2	83015.2	86086.7	91854.7	97733.7	103109.0
Exchange rate (ER), BGN/EUR	0.087	0.220	1.896	1.972	1.956	1.956	1.956	1.956
ER, nominal, 1989=100	9338.4	23704.0	203894.4	212116.3	210349.5	210349.5	210349.5	210349.5
Real ER (CPI-based), 1989=100	209.9	246.5	186.8	166.7	163.1	151.6	144.8	139.7
Real ER (PPI-based), 1989=100	437.6	486.3	394.2	350.7	337.0	301.3	284.5	276.2
PPP, BGN/EUR	0.02093	0.04546	0.3887	0.4746	0.4825	0.5013	0.5219	0.5398
ERDI (EUR based)	4.15	4.85	4.88	4.16	4.05	3.90	3.75	3.62
Average monthly gross wages, BGN	8	13	128	183	201	225	248	270
Average monthly gross wages, EUR (ER)	87	60	67	93	103	115	127	138
Average monthly gross wages, EUR (PPP)	363	291	329	386	417	448	476	500
GDP nominal, bn BGN	0.9	1.8	17.4	22.4	23.8	26.8	29.6	32.6
Employment total, 1000 persons	3282.2	3285.9	3157.4	3152.6	3087.8	2980.1	2940.3	2970
GDP per employed person, BGN	268	536	5521	7112	7705	8977	10073	10976
GDP per empl. person, BGN at 1999 pr.	7970	7210	7082	7375	7705	8413	8873	9164
Unit labour costs, 1989=100	2712.7	5228.7	51394.5	70706.6	74239.8	75933.5	79635.7	83840.3
Unit labour costs, ER adj., 1989=100	29.0	22.1	25.2	33.3	35.3	36.1	37.9	39.9
Unit labour costs, PPP adj., Austria=100	11.78	9.28	11.04	14.76	15.42	15.78	16.30	17.13

(Table C/2 ctd.)

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	1995	1996	1997	1998	1999	2000	2001	2002 prelim.
Romania								
Producer price index, 1989=100	9961.1	14928.8	37725.0	50235.3	72589.7	111353.7	157008.9	196104.1
Consumer price index, 1989=100	9829.0	13643.6	34758.8	55300.0	80629.4	117450.2	157970.5	193513.9
GDP deflator, 1989=100	10633.6	15453.6	38220.3	58917.0	87060.2	125420.3	171756.9	214696.2
Exchange rate (ER), ROL/EUR	2629.51	3862.90	8090.92	9989.25	16295.57	19955.75	26026.89	31255.25
ER, nominal, 1989=100	15984.9	23482.7	49184.9	60724.9	99061.2	121311.6	158218.2	190001.5
Real ER (CPI-based), 1989=100	208.5	226.2	189.8	149.9	169.8	146.4	145.5	145.7
Real ER (PPI-based), 1989=100	184.5	182.2	152.4	140.8	159.0	132.9	124.6	119.6
PPP, ROL/EUR	551.44	788.18	2181.1	3319.0	4808.2	6744.7	9037.7	11075.6
ERDI (EUR based)	4.77	4.90	3.71	3.01	3.39	2.96	2.88	2.82
Average monthly grross wages, ROL	281287	426610	846450	1357132	1957731	2876645	4282622	5473191
Average monthly gross wages, EUR (ER)	107	110	105	136	120	144	165	175
Average monthly gross wages, EUR (PPP)	510	541	388	409	407	427	474	494
GDP nominal, bn ROL	72135.5	108919.6	252925.7	371193.8	545730.2	800308.1	1154126.4	1483500
Employment total, 1000 persons	9752.0	9436.0	9200.9	8917.7	8616.3	8524.5	9000	9000
GDP per employed person, ROL	7396995	11542984	27489384	41624621	63336954	93883289	128236267	164833333
GDP per empl. person, ROL at 1999 pr.	60561542	65029137	62616737	61507755	63336954	65168884	65000468	66840647
Unit labour costs, 1989=100	9711.4	13716.8	28264.5	46134.1	64628.8	92294.6	137760.1	171210.4
Unit labour costs, ER adj., 1989=100	60.8	58.4	57.5	76.0	65.2	76.1	87.1	90.1
Unit labour costs, PPP adj., Austria=100	18.89	18.83	19.30	25.79	21.85	25.49	28.74	29.68
Estonia								
Producer price index, 1992=100	299.9	344.3	374.6	390.4	385.7	404.6	422.4	424.1
Consumer price index, 1992=100	361.7	445.2	495.1	535.7	553.3	575.5	608.9	630.8
GDP deflator, 1992=100	332.4	410.0	456.2	500.8	523.1	558.0	588.1	624.6
Exchange rate (ER), EEK/EUR	14.819	15.074	15.670	15.783	15.647	15.647	15.647	15.647
ER, nominal, 1992=100	93.2	94.8	98.5	99.2	98.4	98.4	98.4	98.4
Real ER (CPI-based), 1992=100	28.4	24.0	22.9	21.7	21.1	20.8	20.2	19.9
Real ER (PPI-based), 1992=100	33.6	30.0	28.9	27.9	28.0	27.9	27.1	26.9
PPP, EEK/EUR	4.803	5.8255	6.095	6.605	6.764	7.027	7.246	7.544
ERDI (EUR based)	3.09	2.59	2.57	2.39	2.31	2.23	2.16	2.07
Average monthly gross wages, EEK	2375	2985	3573	4125	4440	4907	5510	5840
Average monthly gross wages, EUR (ER)	160	198	228	261	284	314	352	373
Average monthly gross wages, EUR (PPP)	494	512	586	625	656	698	760	774
GDP nominal, bn EEK	40.9	52.4	64.0	73.5	76.3	87.2	96.6	106.5
Employment total, 1000 persons	633.4	619.3	617.2	606.5	579.3	572.5	577.7	580
GDP per employed person, EEK	64567	84648	103767	121250	131757	152376	167164	183621
GDP per empl. person, EEK at 1999 pr.	101610	108002	118978	126650	131757	142827	148677	153780
Unit labour costs, 1992=100	384.8	455.1	494.4	536.2	554.8	565.7	610.2	625.3
Unit labour costs, ER adj., 1992=100	413.1	480.2	501.9	540.5	564.1	575.1	620.3	635.7
Unit labour costs, PPP adj., Austria=100	23.73	28.60	31.15	33.89	34.91	35.60	37.83	38.68
Latvia								
Producer price index, 1992=100	284.0	322.9	336.1	342.5	328.8	330.8	336.4	339.8
Consumer price index, 1992=100	355.4	417.9	453.0	474.3	485.7	498.3	510.8	520.5
GDP deflator, 1992=100	275.2	320.7	341.8	360.6	387.3	403.4	410.1	411.7
Exchange rate (ER), LVL/EUR	0.6818	0.6900	0.6574	0.6614	0.6237	0.5600	0.5627	0.5826
ER, nominal, 1992=100	78.5	79.5	75.7	76.2	71.9	64.5	64.8	67.1
Real ER (CPI-based), 1992=100	24.3	21.5	19.3	18.8	17.6	15.8	15.8	16.4
Real ER (PPI-based), 1992=100	29.9	26.8	24.8	24.4	23.9	22.4	22.4	22.9
PPP, LVL/EUR	0.2127	0.2438	0.2446	0.2548	0.2683	0.2721	0.2706	0.2664
ERDI (EUR based)	3.21	2.83	2.69	2.60	2.32	2.06	2.08	2.19
Average monthly gross wages, LVL	90	99	120	133	141	150	159	170
Average monthly gross wages, EUR (ER)	131	143	183	202	226	267	283	292
Average monthly gross wages, EUR (PPP)	421	405	491	523	525	550	588	638
GDP nominal, bn LVL	2.33	2.81	3.27	3.59	3.89	4.35	4.76	5.00
Employment total, 1000 persons	973.0	949.0	990.0	986.0	968.0	941.0	962.0	982
GDP per employed person, LVL	2394	2958	3303	3643	4018	4621	4947	5092
GDP per empl. person, LVL at 1999 pr.	3370	3573	3742	3913	4018	4437	4672	4790
Unit labour costs, 1992=100	399.2	415.3	482.1	511.9	527.3	506.5	511.4	533.4
Unit labour costs, ER adj., 1992=100	508.2	522.4	636.5	671.9	733.9	785.1	788.9	794.7
Unit labour costs, PPP adj., Austria=100	23.24	24.78	31.45	33.55	36.17	38.70	38.32	38.51

(Table C/2 ctd.)

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	1995	1996	1997	1998	1999	2000	2001	2002 prelim.
Lithuania								
Producer price index, 1992=100	914.0	1064.8	1128.7	1084.6	1117.2	1318.3	1301.2	1293.4
Consumer price index, 1992=100	1227.0	1528.8	1664.9	1749.8	1763.8	1781.4	1804.6	1810.0
GDP deflator, 1992=100	906.4	1133.7	1283.5	1369.1	1413.6	1441.5	1446.8	1446.8
Exchange rate (ER), LTL/EUR	5.1717	5.0118	4.5272	4.4924	4.2712	3.6990	3.5849	3.4605
ER, nominal, 1992=100	225.0	218.0	196.9	195.4	185.8	160.9	155.9	150.5
Real ER (CPI-based), 1992=100	20.2	16.1	13.6	13.1	12.5	11.0	10.8	10.6
Real ER (PPI-based), 1992=100	26.6	22.3	19.2	19.7	18.2	14.0	13.9	13.5
PPP, LTL/EUR	1.3045	1.6054	1.552	1.634	1.654	1.642	1.613	1.581
ERDI (EUR based)	3.96	3.12	2.92	2.75	2.58	2.25	2.22	2.19
Average monthly gross wages, LTL	481	618	778	930	987	971	982	1030
Average monthly gross wages, EUR (ER)	93	123	172	207	231	262	274	298
Average monthly gross wages, EUR (PPP)	369	385	501	569	597	591	609	651
GDP nominal, bn LTL	24.1	31.6	38.3	43.0	42.7	45.1	48.0	49.9
Employment total, 1000 persons	1643.6	1659.0	1669.2	1656.1	1647.5	1586.0	1521.8	1405
GDP per employed person, LTL	14665	19029	22969	25959	25891	28466	31520	35526
GDP per empl. person, LTL at 1999 pr.	22871	23726	25297	26800	25891	27914	30797	34710
Unit labour costs, 1992=100	1063.4	1317.8	1555.6	1754.6	1928.8	1758.9	1613.2	1500.8
Unit labour costs, ER adj., 1992=100	472.7	604.5	789.9	897.9	1038.2	1093.1	1034.5	997.0
Unit labour costs, PPP adj., Austria=100	14.96	19.83	27.00	31.01	35.39	37.27	34.75	33.42
Croatia								
Producer price index, 1989=100	365072.8	370183.9	378698.3	374153.9	383881.7	421118.3	436278.3	434533.3
Consumer price index, 1989=100	394858.7	408679.1	423391.3	447530.6	466326.7	495238.8	519505.8	530935.2
GDP deflator, 1989=100	309216.7	320477.1	344066.9	373062.5	387324.9	405475.9	417257.0	426436.7
Exchange rate (ER), HRK/EUR	6.76	6.80	6.96	7.14	7.58	7.63	7.47	7.41
ER, nominal, 1989=100	209442.2	210895.8	215699.6	221182.2	234912.7	236628.2	231483.2	229555.6
Real ER (CPI-based), 1989=100	68.0	67.8	68.3	67.5	69.6	67.7	64.7	64.1
Real ER (PPI-based), 1989=100	66.0	66.0	66.6	68.9	71.3	68.6	65.6	65.2
PPP, HRK/EUR	4.041	4.119	3.799	4.066	4.139	4.219	4.248	4.257
ERDI (EUR based)	1.67	1.65	1.83	1.76	1.83	1.81	1.76	1.74
Average monthly gross wages, HRK	2887	3243	3668	4131	4551	4869	5061	5355
Average monthly gross wages, EUR (ER)	427	477	527	579	600	638	678	723
Average monthly gross wages, EUR (PPP)	714	787	966	1016	1100	1154	1191	1258
GDP nominal, bn HRK	98.4	108.0	123.8	137.6	141.6	152.5	162.9	174
Employment total, 1000 persons	1417.4	1329.5	1310.9	1384.8	1364.5	1341.0	1348.3	1340.8
GDP per employed person, HRK	69410	81219	94447	99364	103759	113739	120825	129770
GDP per empl. person, HRK at 1999 pr.	86943	98160	106322	103163	103759	108647	112157	117868
Unit labour costs, 1989=100	253947.6	252664.5	263840.3	306241.5	335438.2	342731.6	345097.3	347422.9
Unit labour costs, ER adj., 1989=100	121.2	119.8	122.3	138.5	142.8	144.8	149.1	151.3
Unit labour costs, PPP adj., Austria=100	45.23	46.34	49.30	56.39	57.39	58.23	59.05	59.82
Macedonia	**1995**	**1996**	**1997**	**1998**	**1999**	**2000**		
Producer price index, 1989=100	170868.8	170357.8	177512.8	184616.7	184429.3	204156.7	208245.3	210536.0
Consumer price index, 1989=100	288886.7	295385.2	303065.2	302769.8	300643.1	318070.8	333667.1	338672.1
GDP deflator, 1990=100	42493.5	43708.8	45429.8	46050.2	47329.3	51225.9	52946.9	53741.1
Exchange rate (ER), MKD/EUR	49.15	50.08	56.20	61.07	60.62	60.73	60.91	61
ER, nominal, 1989=100	152643.3	155515.9	174525.6	189641.9	188247.5	188584.8	189169.5	189438.8
Real ER (CPI-based), 1989=100	67.7	69.2	77.2	85.5	86.5	84.0	82.4	83.0
Real ER (PPI-based), 1989=100	102.7	105.7	114.9	119.7	118.9	112.7	112.3	111.1
PPP, MKD/EUR	22.88	23.14	18.04	18.05	18.19	19.17	19.39	19.29
ERDI (EUR based)	2.15	2.16	3.12	3.38	3.33	3.17	3.14	3.16
Average monthly net wages, MKD	8581	8817	9063	9394	9664	10193	10552	11260
Average monthly net wages, EUR (ER)	175	176	161	154	159	168	173	185
Average monthly net wages, EUR (PPP)	375	381	502	520	531	532	544	584
GDP nominal, bn MKD	169.5	176.4	186.0	195.0	209.0	236.4	233.1	236.6
Employment total, 1000 persons	.	537.6	512.3	539.8	545.2	549.8	599.3	600
GDP per employed person, MKD	.	328212	363103	361231	383348	429919	388932	394333
GDP per empl. person, MKD at 1999 pr.	.	355399	378285	371265	383348	397216	347666	347285
Unit labour costs, 1990=100	.	.	.	.	.	.	.	.
Unit labour costs, ER adj., 1990=100	.	.	.	.	.	.	.	.
Unit labour costs, PPP adj., Austria=100	.	20.78	18.63	18.30	18.13	18.42	21.40	22.78

(Table C/2 ctd.)

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	1995	1996	1997	1998	1999	2000	2001	2002 prelim.
Russia								
Producer price index, 1989=100	899321	1356086	1559505	1670224	2653986	3890743	4635820	5171258
Consumer price index, 1989=100	388817	574672	659723	841807	1563235	1888388	2296280	2663684
GDP deflator, 1989=100	446728	644091	737391	857437	1414632	1988125	2344270	2700599
Exchange rate (ER), RUB/EUR	5.89	6.63	6.54	11.06	26.24	26.03	26.13	29.65
ER, nominal, 1989=100	848366	954960	941800	1592973	3778114	3747905	3762448	4268826
Real ER (CPI-based), 1989=100	279.7	218.4	191.4	258.3	334.0	281.2	238.1	237.7
Real ER (PPI-based), 1989=100	108.5	81.5	70.6	111.1	165.8	117.5	100.3	101.9
PPP, RUB/EUR	1.6890	2.395	3.250	3.731	6.035	8.259	9.528	10.761
ERDI (EUR based)	3.49	2.77	2.01	2.97	4.35	3.15	2.74	2.75
Average monthly gross wages, RUB	532.6	790.2	950.2	1051.5	1522.6	2223.4	3240.4	4426.0
Average monthly gross wages, EUR (ER)	90	119	145	95	58	85	124	149
Average monthly gross wages, EUR (PPP)	315	330	292	282	252	269	340	411
GDP nominal, bn RUB	1540.5	2145.7	2478.6	2741.1	4766.8	7302.2	9040.8	10950
Employment total, 1000 persons	66409	65950	64693	63812	63963	64327	64710	66650
GDP per employed person, RUB	23197	32535	38313	42955	74524	113517	139713	164291
GDP per empl. person, RUB at 1999 pr.	73457	71456	73501	70869	74524	80772	84309	86059
Unit labour costs, 1989=100	302358	461145	539088	618714	851969	1147868	1602739	2144621
Unit labour costs, ER adj., 1989=100	35.6	48.3	57.2	38.8	22.6	30.6	42.6	50.2
Unit labour costs, PPP adj., Austria=100	16.52	23.21	28.66	19.65	11.26	15.30	20.96	24.67
Ukraine								
Producer price index, 1989=100	19914767	30290361	32622718	36928917	48413810	58532296	63566073	65536621
Consumer price index, 1989=100	6786409	12229109	14172537	15674826	19233012	24656721	27615528	27836452
GDP deflator, 1989=100	7715454	12819488	15140086	16950568	21587839	26575880	28925236	29792993
Exchange rate (ER), UAH/EUR	1.928	2.322	2.113	2.768	4.393	5.029	4.814	5.030
ER, nominal, 1989=100	27739568	33408633	30401439	39821583	63212950	72357554	69260000	72370360
Real ER (CPI-based), 1989=100	524.0	359.0	287.7	346.8	454.2	415.8	364.4	385.7
Real ER (PPI-based), 1989=100	160.2	127.7	108.9	125.6	152.1	150.8	134.7	136.4
PPP, UAH/EUR	0.3183	0.5201	0.5565	0.6151	0.7680	0.9206	0.9804	0.9900
ERDI (EUR based)	6.06	4.46	3.80	4.50	5.72	5.46	4.91	5.08
Average monthly gross wages, UAH	73.0	126.0	143.0	153.0	177.5	230.1	311.1	376.0
Average monthly gross wages, EUR (ER)	38	54	68	55	40	46	65	75
Average monthly gross wages, EUR (PPP)	229	242	257	249	231	250	317	380
GDP nominal, bn UAH	54.5	81.5	93.4	102.6	130.4	170.1	201.9	216.51
Employment total, 1000 persons	23725.5	23231.8	22597.6	22348.7	21823.7	21268.5	20941.9	20500
GDP per employed person, UAH	2298	3509	4132	4591	5977	7996	9642	10561
GDP per empl. person, UAH at 1999 pr.	6429	5909	5891	5846	5977	6495	7196	7653
Unit labour costs, 1989=100	6821887	12811424	14583936	15723252	17844302	21286399	25971847	29519571
Unit labour costs, ER adj., 1989=100	24.6	38.3	48.0	39.5	28.2	29.4	37.5	40.8
Unit labour costs, PPP adj., Austria=100	10.06	16.26	21.20	17.63	12.44	12.97	16.29	17.68
Austria								
Producer price index, 1989=100	104.8	104.8	105.2	104.7	103.7	107.9	109.6	109.2
Consumer price index, 1989=100	121.1	123.3	125.0	126.1	126.8	129.8	133.3	135.7
GDP deflator, 1989=100	120.4	122.0	123.1	123.7	124.5	126.3	128.4	129.7
Exchange rate (ER), ATS-EUR/EUR	0.9471	0.9636	1.0017	1.0089	1.0000	1.0000	1.0000	1.0000
ER, nominal, 1989=100	89.5	91.0	94.6	95.3	94.5	94.5	94.5	94.5
Real ER (CPI-based), 1989=100	94.8	97.0	101.6	103.2	102.9	103.1	103.0	103.3
Real ER (PPI-based), 1989=100	98.2	100.6	105.2	106.1	106.1	106.8	106.5	106.8
PPP, ATS-EUR/EUR	1.0740	1.0697	1.0487	1.0581	1.0305	1.0175	1.0115	1.0015
ERDI (EUR based)	0.88	0.90	0.96	0.95	0.97	0.98	0.99	1.00
Average monthly gross wages, EUR-ATS	2140	2157	2180	2245	2295	2356	2396	2432
Average monthly gross wages, EUR (ER)	2260	2239	2177	2225	2295	2356	2396	2432
Average monthly gross wages, EUR (PPP)	1993	2016	2079	2121	2227	2316	2369	2429
GDP nominal, bn EUR-ATS	172.3	178.0	182.5	190.6	197.2	207.0	211.9	215.9
Employment total, 1000 persons	3439.5	3415.4	3424.5	3446.6	3478.8	3506.5	3522.5	3509.4
GDP per employed person, EUR-ATS	50090	52131	53289	55309	56673	59044	60144	61515
GDP per empl. person, EUR-ATS at 1999 pr.	51796	53199	53895	55667	56673	58202	58317	59062
Unit labour costs, 1989=100	120.8	118.5	118.2	117.9	118.4	118.3	120.1	120.4
Unit labour costs, ER adj., 1989=100	135.0	130.2	124.9	123.7	125.3	125.3	127.1	127.4
Unit labour costs, PPP adjusted	0.54	0.52	0.50	0.49	0.50	0.50	0.51	0.51

Employment: Employees + self-employed + farmers.

ER = Exchange Rate, PPP = Purchasing Power Parity, ERDI = Exchange Rate Deviation Index (all in terms of national currency per EUR). Till 1996 PPPs have been calculated using the benchmark PPPs for 1996 and extrapolated with GDP deflators, from 1997 using benchmark PPPs for 1999 and extrapolated with GDP deflators.

Sources: BENCHMARK RESULTS OF THE 1996 EUROSTAT-OECD COMPARISON BY ANALYTICAL CATEGORIES, OECD, 1999; PURCHASING POWER PARITIES AND REAL EXPENDITRUES, 1999 BENCHMARK YEAR, OECD, 2002; National statistics; WIFO; **wiiw** estimates.

Table C/3

Indicators of macro-competitiveness, 1995-2002

annual changes in %

	1995	1996	1997	1998	1999	2000	2001	2002 prelim.	1996-01 average
Czech Republic									
GDP deflator	10.2	8.8	8.0	10.6	2.9	1.0	5.2	1.7	6.0
Exchange rate (ER), CZK/EUR	0.7	-0.9	5.3	1.0	2.0	-3.4	-4.3	-9.6	-0.1
Real ER (CPI-based)	-4.9	-6.6	-1.0	-7.1	1.1	-4.7	-6.3	-9.3	-4.1
Real ER (PPI-based)	-2.2	-4.7	1.3	-4.1	1.0	-3.6	-5.8	-9.2	-2.7
Average gross wages, CZK	18.5	18.4	10.5	9.4	8.3	6.6	8.5	7.5	10.2
Average gross wages, real (PPI based)	10.2	13.1	5.3	4.3	7.2	1.6	5.4	8.1	6.1
Average gross wages, real (CPI based)	8.6	8.8	1.8	-1.2	6.1	2.6	3.6	5.6	3.6
Average gross wages, EUR (ER)	17.7	19.4	5.0	8.3	6.2	10.4	13.3	18.9	10.3
Employment total	0.7	0.2	-0.7	-1.4	-2.1	-0.7	0.4	1.0	-0.7
GDP per empl. person, CZK at 1999 pr.	5.2	4.1	0.0	0.4	2.7	4.0	3.0	1.5	2.3
Unit labour costs, CZK at 1999 prices	12.7	13.8	10.5	8.9	5.5	2.5	5.3	5.9	7.7
Unit labour costs, ER (EUR) adjusted	11.9	14.8	5.0	7.9	3.4	6.1	10.1	17.1	7.8
Hungary									
GDP deflator	25.5	21.2	18.5	12.6	8.4	9.7	8.7	5.8	13.1
Exchange rate (ER), HUF/EUR	30.3	17.5	10.3	14.2	4.9	2.9	-1.3	-5.3	7.9
Real ER (CPI-based)	4.8	-2.5	-4.8	1.7	-3.4	-3.9	-7.3	-8.2	-3.4
Real ER (PPI-based)	5.6	-2.8	-7.5	2.3	-0.2	-3.5	-4.9	-3.7	-2.8
Average gross wages, HUF	16.8	20.4	22.3	18.3	13.9	13.5	18.2	17.8	17.7
Average gross wages, real (PPI based)	-9.4	-1.1	1.6	6.3	8.4	1.7	12.3	20.0	4.8
Average gross wages, real (CPI based)	-8.9	-2.6	3.4	3.5	3.6	3.4	8.2	11.9	3.2
Average gross wages, EUR (ER)	-10.4	2.5	10.8	3.6	8.6	10.4	19.7	24.5	9.1
Employment total	-1.9	-0.8	0.0	1.4	3.1	1.0	0.3	0.1	0.8
GDP per empl. person, HUF at 1999 pr.	4.5	2.2	4.6	3.4	1.1	4.2	3.4	3.2	3.1
Unit labour costs, HUF at 1999 prices	11.7	17.8	16.9	14.4	12.7	9.0	14.2	14.1	14.1
Unit labour costs, ER (EUR) adjusted	-14.3	0.3	5.9	0.1	7.4	6.0	15.7	20.6	5.8
Poland									
GDP deflator	28.6	18.8	14.0	11.8	6.7	7.1	4.1	1.3	10.3
Exchange rate (ER), PLN/EUR	16.3	7.7	9.7	5.9	7.7	-5.1	-8.5	5.1	2.7
Real ER (CPI-based)	-6.2	-7.9	-2.6	-3.6	1.7	-11.6	-11.1	5.3	-6.0
Real ER (PPI-based)	-3.1	-3.5	-1.3	-1.7	1.9	-7.8	-8.8	4.0	-3.6
Average gross wages, PLN *)	31.6	26.5	21.9	15.7	10.6	11.6	8.0	11.3	15.5
Average gross wages, real (PPI based)	4.9	12.6	8.6	7.8	30.3	3.5	6.3	10.2	11.2
Average gross wages, real (CPI based)	3.0	5.5	6.1	3.5	28.3	1.3	2.4	9.3	7.5
Average gross wages, EUR (ER)	13.2	17.4	11.1	9.2	27.8	17.6	18.1	5.9	16.7
Employment total	1.8	1.9	2.8	2.3	-2.7	-2.3	-0.6	-0.2	0.2
GDP per empl. person, PLN at 1999 pr.	11.8	4.0	3.9	2.4	7.0	6.5	5.7	1.5	4.9
Unit labour costs, PLN at 1999 prices	17.7	21.7	17.3	12.9	28.7	4.8	2.2	9.7	14.2
Unit labour costs, ER (EUR) adjusted	1.2	12.9	6.9	6.7	19.4	10.5	11.7	4.4	11.3
Slovak Republic									
GDP deflator	9.9	4.4	6.7	5.2	6.4	6.4	5.4	2.4	5.8
Exchange rate (ER), SKK/EUR	1.4	-0.1	-1.0	4.2	11.4	-3.5	1.7	-1.4	2.0
Real ER (CPI-based)	-4.9	-3.2	-4.8	-0.6	2.0	-11.6	-2.6	-2.6	-3.6
Real ER (PPI-based)	-2.8	-3.5	-4.4	0.5	6.8	-8.8	-3.3	-3.6	-2.2
Average gross wages, SKK	14.3	13.3	13.1	8.4	7.2	6.5	8.2	9.3	9.4
Average gross wages, real (PPI based)	4.9	8.8	8.3	5.0	2.8	-3.8	1.6	7.1	3.7
Average gross wages, real (CPI based)	4.0	7.1	6.6	1.6	-3.0	-4.9	1.0	5.8	1.3
Average gross wages, EUR (ER)	12.8	13.5	14.3	4.1	-3.7	10.4	6.4	10.9	7.3
Employment total	1.7	3.6	-0.9	-0.3	-3.0	-1.4	1.0	0.1	-0.2
GDP per empl. person, SKK at 1999 pr.	4.7	2.1	6.5	4.3	4.5	3.7	2.2	4.1	3.9
Unit labour costs, SKK at 1999 prices	9.2	11.0	6.2	4.0	2.6	2.8	5.8	5.1	5.4
Unit labour costs, ER (EUR) adjusted	7.7	11.1	7.3	-0.2	-7.9	6.5	4.1	6.6	3.3
Slovenia									
GDP deflator	15.2	11.1	8.8	7.8	6.6	5.7	9.9	7.5	8.3
Exchange rate (ER), SIT/EUR	0.5	10.7	6.4	3.3	4.0	5.9	5.9	4.2	6.0
Real ER (CPI-based)	-8.8	3.2	0.2	-2.6	-0.8	-0.3	0.2	-1.1	0.0
Real ER (PPI-based)	-6.9	4.4	1.3	-2.9	1.8	3.1	-1.5	-1.0	1.0
Average gross wages, SIT	18.4	15.3	11.7	9.6	9.6	10.6	11.9	9.5	11.4
Average gross wages, real (PPI based)	4.9	8.0	5.3	3.4	7.3	2.8	2.8	4.2	4.9
Average gross wages, real (CPI based)	4.3	4.9	3.1	1.6	3.3	1.6	3.3	1.9	2.9
Average gross wages, EUR (ER)	17.8	4.1	5.0	6.1	5.4	4.5	5.7	5.1	5.1
Employment total	-0.1	-0.5	0.2	0.2	1.8	1.3	1.4	0.6	0.7
GDP per empl. person, SIT at 1999 pr.	4.2	4.0	4.4	3.5	3.4	3.3	1.6	2.4	3.3
Unit labour costs, SIT at 1999 prices	13.5	10.9	7.1	5.8	6.0	7.1	10.2	6.9	7.8
Unit labour costs, ER (EUR) adjusted	13.0	0.1	0.6	2.5	2.0	1.2	4.1	2.7	1.7

(Table C/3 ctd.)

Table C/3 (ctd.)

	1994	1995	1996	1997	1998	1999	2000	2001	2002 prelim.	1996-01 average
Bulgaria										
GDP deflator	72.8	62.7	120.9	948.6	23.7	3.7	6.7	6.4	5.5	79.8
Exchange rate (ER), BGN/EUR	99.3	34.4	153.8	760.2	4.0	-0.8	0.0	0.0	0.0	68.1
Real ER (CPI-based)	4.9	-14.5	17.4	-24.2	-10.8	-2.1	-7.1	-4.5	-3.5	-6.0
Real ER (PPI-based)	15.8	-8.5	11.1	-18.9	-11.0	-3.9	-10.6	-5.6	-2.9	-6.9
Average gross wages, BGN	53.5	53.2	74.4	865.6	43.3	9.7	11.7	10.6	8.7	78.8
Average gross wages, real (PPI based)	-12.6	-0.2	-24.2	-9.9	22.9	6.3	-4.6	3.1	5.7	-2.1
Average gross wages, real (CPI based)	-21.7	-5.5	-21.3	-16.6	20.7	6.9	1.2	3.0	2.8	-2.1
Average gross wages, EUR (ER)	-23.0	13.9	-31.3	12.3	37.7	10.6	11.7	10.6	8.7	6.4
Employment total	0.6	1.3	0.1	-3.9	-0.2	-2.1	-3.5	-1.3	1.0	-1.8
GDP per empl. person, BGN at 1999 pr.	1.1	1.6	-9.5	-1.8	4.1	4.5	9.2	5.5	3.3	1.8
Unit labour costs, BGN at 1999 prices	51.8	50.7	92.8	882.9	37.6	5.0	2.3	4.9	5.3	75.6
Unit labour costs, ER (EUR) adjusted	-23.8	12.1	-24.1	14.3	32.2	5.9	2.3	4.9	5.3	4.5
Romania										
GDP deflator	139.0	35.3	45.3	147.3	54.2	47.8	44.1	36.9	25.0	59.0
Exchange rate (ER), ROL/EUR	122.4	33.6	46.9	109.5	23.5	63.1	22.5	30.4	20.1	46.5
Real ER (CPI-based)	-3.1	4.1	8.5	-16.1	-21.0	13.3	-13.8	-0.6	0.1	-5.8
Real ER (PPI-based)	-5.5	3.3	-1.3	-16.3	-7.6	12.9	-16.4	-6.3	-3.9	-6.3
Average gross wages, ROL	131.9	54.8	51.7	98.4	60.3	44.3	46.9	48.9	27.8	57.4
Average gross wages, real (PPI based)	-3.6	14.6	1.2	-21.5	20.4	-0.2	-4.2	5.6	2.3	-0.6
Average gross wages, real (CPI based)	-2.0	17.1	9.3	-22.1	0.8	-1.1	0.9	10.7	4.3	-0.9
Average gross wages, EUR (ER)	4.3	15.8	3.2	-5.3	29.9	-11.6	20.0	14.1	6.4	7.4
Employment total	-2.2	-2.8	-3.2	-2.5	-3.1	-3.4	-1.1	5.6	0.0	-1.3
GDP per empl. person, ROL at 1999 pr.	6.3	10.3	7.4	-3.7	-1.8	3.0	2.9	-0.3	2.8	1.2
Unit labour costs, ROL at 1999 prices	118.3	40.4	41.2	106.1	63.2	40.1	42.8	49.3	24.3	55.6
Unit labour costs, ER (EUR) adjusted	-1.9	5.1	-3.9	-1.6	32.2	-14.1	16.6	14.4	3.5	6.2
Estonia										
GDP deflator	39.6	31.3	23.3	11.3	9.8	4.5	6.7	5.4	6.2	10.0
Exchange rate (ER), EEK/EUR	-0.7	-3.4	1.7	4.0	0.7	-0.9	0.0	0.0	0.0	0.9
Real ER (CPI-based)	-30.7	-22.9	-15.3	-4.6	-5.2	-2.8	-1.4	-3.1	-1.4	-5.5
Real ER (PPI-based)	-25.6	-19.7	-10.8	-3.5	-3.7	0.3	-0.2	-3.0	-0.5	-3.5
Average gross wages, EEK	62.7	37.0	25.7	19.7	15.4	7.6	10.5	12.3	6.0	15.1
Average gross wages, real (PPI based)	19.3	9.1	9.5	10.0	10.8	8.9	5.4	7.6	5.6	8.7
Average gross wages, real (CPI based)	10.1	6.2	2.1	7.6	6.7	4.2	6.3	6.1	2.3	5.5
Average gross wages, EUR (ER)	63.9	41.9	23.6	15.1	14.6	8.6	10.5	12.3	6.0	14.0
Employment total	-3.4	-6.2	-2.2	-0.3	-1.7	-4.5	-1.2	0.9	0.4	-1.5
GDP per empl. person, EEK at 1999 pr.	1.4	11.2	6.3	10.2	6.4	4.0	8.4	4.1	3.4	6.5
Unit labour costs, EEK at 1999 prices	60.4	23.2	18.2	8.7	8.5	3.5	2.0	7.9	2.5	8.0
Unit labour costs, ER (EUR) adjusted	61.6	27.6	16.2	4.5	7.7	4.4	2.0	7.9	2.5	7.0
Latvia										
GDP deflator	38.3	16.0	16.5	6.6	5.5	7.4	4.1	1.7	0.4	6.9
Exchange rate (ER), LVL/EUR	-16.4	2.9	1.2	-4.7	0.6	-5.7	-10.2	0.5	3.5	-3.1
Real ER (CPI-based)	-36.6	-15.1	-11.8	-10.3	-2.2	-6.8	-10.3	0.5	3.7	-6.9
Real ER (PPI-based)	-27.0	-3.9	-10.4	-7.6	-1.6	-1.8	-6.5	0.1	2.4	-4.7
Average gross wages, LVL	52.2	24.5	10.3	21.6	11.1	5.8	6.1	6.3	6.9	10.1
Average gross wages, real (PPI based)	30.2	11.3	-3.0	16.8	9.0	10.2	5.4	4.6	5.9	7.0
Average gross wages, real (CPI based)	12.0	-0.4	-6.2	12.2	6.1	3.3	3.4	3.7	4.9	3.6
Average gross wages, EUR (ER)	82.1	21.0	9.0	27.6	10.4	12.2	18.1	5.8	3.3	13.6
Employment total	-10.1	-3.5	-2.5	4.3	-0.4	-1.8	-2.8	2.2	2.1	-0.2
GDP per empl. person, LVL at 1999 pr.	12.0	1.9	6.0	4.7	4.6	2.7	10.4	5.3	2.5	5.6
Unit labour costs, LVL at 1999 prices	35.9	22.2	4.0	16.1	6.2	3.0	-4.0	1.0	4.3	4.2
Unit labour costs, ER (EUR) adjusted	62.6	18.8	2.8	21.8	5.6	9.2	7.0	0.5	0.7	7.6
Lithuania										
GDP deflator	61.6	38.0	25.1	13.2	6.7	3.2	2.0	0.4	0.0	8.1
Exchange rate (ER), LTL/EUR	-7.9	9.7	-3.1	-9.7	-0.8	-4.9	-13.4	-3.1	-3.5	-5.9
Real ER (CPI-based)	-44.8	-19.0	-20.3	-15.3	-3.9	-4.5	-12.1	-1.9	-1.7	-9.9
Real ER (PPI-based)	-35.0	-10.7	-16.2	-14.0	2.9	-7.7	-23.1	-0.5	-3.0	-10.2
Average gross wages, LTL	95.9	47.8	28.6	25.9	19.5	6.2	-1.7	1.2	4.9	12.6
Average gross wages, real (PPI based)	35.3	15.2	10.3	18.7	24.3	3.1	-16.7	2.5	5.5	6.2
Average gross wages, real (CPI based)	13.8	5.9	3.2	15.6	13.7	5.4	-2.7	-0.1	4.5	5.6
Average gross wages, EUR (ER)	112.7	34.7	32.7	39.3	20.4	11.7	13.5	4.4	8.6	19.7
Employment total	-5.8	-1.9	0.9	0.6	-0.8	-0.5	-3.7	-4.0	-7.7	-1.3
GDP per empl. person, LTL at 1999 pr.	-4.2	5.3	3.7	6.6	5.9	-3.4	7.8	10.3	12.7	5.1
Unit labour costs, LTL at 1999 prices	104.5	40.4	23.9	18.0	12.8	9.9	-8.8	-8.3	-7.0	7.2
Unit labour costs, ER (EUR) adjusted	122.0	28.0	27.9	30.7	13.7	15.6	5.3	-5.4	-3.6	13.9

(Table C/3 ctd.)

Table C/3 (ctd.)

	1994	1995	1996	1997	1998	1999	2000	2001	2002 prelim.	1996-01 average
Croatia										
GDP deflator	111.8	5.3	3.6	7.4	8.4	3.8	4.7	2.9	2.2	5.1
Exchange rate (ER), HRK/EUR	71.5	-4.7	0.7	2.3	2.5	6.2	0.7	-2.2	-0.8	1.7
Real ER (CPI-based)	-10.5	-3.7	-0.3	0.8	-1.3	3.2	-2.7	-4.4	-0.9	-0.8
Real ER (PPI-based)	-1.4	-1.1	0.0	0.9	3.4	3.5	-3.8	-4.3	-0.5	-0.1
Average gross wages, HRK	154.1	34.0	12.3	13.1	12.6	10.2	7.0	3.9	5.8	9.8
Average gross wages, real (PPI based)	43.1	33.0	10.8	10.6	14.0	7.4	-2.5	0.3	6.2	6.6
Average gross wages, real (CPI based)	28.6	31.3	8.5	9.2	6.5	5.7	0.7	-0.9	3.5	4.9
Average gross wages, EUR (ER)	48.2	40.5	11.6	10.6	9.8	3.7	6.2	6.3	6.7	8.0
Employment total	-0.7	-1.4	-6.2	-1.4	5.6	-1.5	-1.7	0.5	-0.6	-0.8
GDP per empl. person, HRK at 1999 pr.	6.6	8.3	12.9	8.3	-3.0	0.6	4.7	3.2	5.1	4.3
Unit labour costs, HRK at 1999 prices	138.5	23.7	-0.5	4.4	16.1	9.5	2.2	0.7	0.7	5.2
Unit labour costs, ER (EUR) adjusted	39.1	29.7	-1.2	2.1	13.2	3.1	1.4	2.9	1.5	3.5
Macedonia										
GDP deflator	151.9	17.1	2.9	3.9	1.4	2.8	8.2	3.4	1.5	3.7
Exchange rate (ER), MKD/EUR	87.1	-3.8	1.9	12.2	8.7	-0.7	0.2	0.3	0.1	3.6
Real ER (CPI-based)	-15.5	-14.3	2.1	11.6	10.7	1.2	-2.9	-1.9	0.7	3.3
Real ER (PPI-based)	1.0	-4.0	2.9	8.7	4.1	-0.6	-5.2	-0.4	-1.0	1.5
Average net wages, MKD	105.0	10.7	2.8	2.8	3.7	2.9	5.5	3.5	6.7	3.5
Average net wages, real (PPI based)	8.3	5.7	3.1	-1.4	-0.3	3.0	-4.7	1.5	5.5	0.1
Average net wages, real (CPI based)	-10.2	-4.4	0.5	0.2	3.8	3.6	-0.3	-1.3	5.1	1.0
Average net wages, EUR (ER)	9.6	15.0	0.9	-8.4	-4.6	3.6	5.3	3.2	6.6	-0.1
Employment total	.	.	.	-4.7	5.4	1.0	0.8	9.0	0.1	0.1
GDP per empl. person, MKD at 1999 pr.	.	.	.	6.4	-1.9	3.3	3.6	-12.5	-0.1	-0.1
Unit labour costs, MKD at 1999 prices	.	.	.	-3.4	5.6	-0.4	1.8	18.3	6.8	6.8
Unit labour costs, ER (EUR) adjusted	.	.	.	-13.9	-2.8	0.4	1.6	17.9	6.7	6.7
Russia										
GDP deflator	307.8	163.0	44.2	14.5	16.3	65.0	40.5	17.9	15.2	31.8
Exchange rate (ER), RUB/EUR	114.8	126.2	12.6	-1.4	69.1	137.2	-0.8	0.4	13.5	28.2
Real ER (CPI-based)	-45.6	-21.6	-21.9	-12.3	34.9	29.3	-15.8	-15.3	-0.1	-2.7
Real ER (PPI-based)	-49.8	-29.8	-24.8	-13.4	57.4	49.3	-29.1	-14.6	1.6	-1.3
Average gross wages, RUB	277.5	119.6	48.4	20.2	10.7	44.8	46.0	45.7	36.6	35.1
Average gross wages, real (PPI based)	-13.6	-34.7	-1.6	4.6	3.3	-8.9	-0.4	22.3	22.4	2.8
Average gross wages, real (CPI based)	-7.2	-26.2	0.4	4.7	-13.3	-22.0	20.9	19.9	17.7	0.5
Average gross wages, EUR (ER)	75.7	-2.9	31.8	21.9	-34.6	-38.9	47.2	45.2	20.4	5.4
Employment total	-3.3	-3.0	-0.7	-1.9	-1.4	0.2	0.6	0.6	3.0	-0.4
GDP per empl. person, RUB at 1999 pr.	-9.7	-1.1	-2.7	2.9	-3.6	5.2	8.4	4.4	2.1	2.3
Unit labour costs, RUB at 1999 prices	317.9	122.0	52.5	16.9	14.8	37.7	34.7	39.6	33.8	32.0
Unit labour costs, ER (EUR) adjusted	94.6	-1.9	35.5	18.5	-32.1	-41.9	35.8	39.1	17.9	3.0
Ukraine										
GDP deflator	952.9	415.8	66.2	18.1	12.0	27.4	23.1	8.8	3.0	24.6
Exchange rate (ER), UAH/EUR	630.3	400.9	20.4	-9.0	31.0	58.7	14.5	-4.3	4.5	16.5
Real ER (CPI-based)	-24.0	8.3	-31.5	-19.9	20.6	31.0	-8.5	-12.4	5.8	-5.9
Real ER (PPI-based)	-39.6	-11.1	-20.3	-14.7	15.3	21.1	-0.9	-10.7	1.2	-2.9
Average gross wages, UAH	786.6	430.7	72.6	13.5	7.0	16.0	29.6	35.2	20.9	27.3
Average gross wages, real (PPI based)	-28.2	-9.9	13.5	5.4	-5.5	-11.5	7.2	24.5	17.2	4.9
Average gross wages, real (CPI based)	-10.5	11.3	-4.2	-2.1	-3.3	-5.4	1.1	20.7	19.9	0.8
Average gross wages, EUR (ER)	21.4	6.0	43.3	24.7	-18.3	-26.9	13.3	41.2	15.7	9.3
Employment total	-3.8	3.0	-2.1	-2.7	-1.1	-2.3	-2.5	-1.5	-2.1	-2.1
GDP per empl. person, UAH at 1999 pr.	-19.9	-14.8	-8.1	-0.3	-0.8	2.2	8.7	10.8	6.3	1.9
Unit labour costs, UAH at 1999 prices	1006.6	522.9	87.8	13.8	7.8	13.5	19.3	22.0	13.7	25.0
Unit labour costs, ER (EUR) adjusted	51.5	24.3	55.9	25.1	-17.7	-28.5	4.2	27.5	8.8	7.3

COUNTRY REPORTS

Anton Mihailov

Bulgaria: economic consolidation making headway

Economic activity in Bulgaria remained relatively strong in the second half of 2002, defying the fears of a notable slowdown. According to preliminary estimates announced by the government, real GDP grew by 4.3% in 2002 as a whole which was above the 4% official growth target incorporated in the budgetary framework for the year. If these estimates are confirmed they would imply that the rate of GDP growth in the second half of the year was between 4.1% and 4.7% year on year, about the same as reported in the first half.

According to the quarterly national accounts data, the fastest expansion was recorded in the services sector whose output in the first three quarters rose by 6.1% over the same period of 2001. The tourist industry contributed the most to this outcome, reporting its best results in more than a decade: in January-October tourist receipts (BOP basis) grew 10% year on year (and in absolute terms were larger than the annual figures for 2001) while in January-November the number of foreign tourists was 8% larger than it was a year earlier. On the demand side, fixed investment was the fastest growing aggregate demand item although its rate of growth was lower than in previous years (7.4% year on year in January-September, compared to almost 20% in 2001 as a whole). Private consumption increased less than GDP, by 2.5% year on year in the first three quarters.

In some manufacturing sectors such as the textiles and leather industry, wood products, metal processing and the pulp and paper industry there was an upturn of economic activity in the second half of the year. Notably, after more than a decade of decline, there was a strong output recovery also in some electrical engineering branches such as appliances, IT and communications equipment. Manufacturing sales as a whole were gradually picking up in the course of the year. The significant gap between output and sales growth figures – in the order of some 7-8 percentage points in the first quarter, indicating large stock-building – dropped to some 3-4 percentage points in the fourth quarter. While the discrepancy still remains, its decline suggests that a considerable part of the previously accumulated stocks were cleared.

The revival in manufacturing sales was largely driven by the notable recovery in exports, especially in the third quarter, when they rose in current euro terms by more than 12% year on year. The upturn in shipments can also be traced in the rise of their physical volume: in January-September the volume of Bulgaria's total merchandise exports reportedly increased by some 8.1% from the same period of 2001, while in the first half of the year the rate of growth had been only 3.0%. As to the direction of trade, the EU continued to gain market shares and contributed the most to the recovery of exports. By contrast, Russia and other CIS countries kept on losing market shares (Russia is now not even among Bulgaria's top 10 export destinations). There was also a revival of exports to other CEE economies which can be partly attributed to the liberalization of trade with some of these countries after Bulgaria and Romania joined CEFTA.

Another positive development that started in 2001 and strengthened considerably in 2002 was the revitalization of financial intermediation. The introduction of the currency board in 1997 was followed by several years of a severe credit crunch: banks were reducing their exposure to the corporate sector and were investing abroad a large share of their assets. 2002 marked a notable reversal in this trend: a significant amount of bank assets (USD 354 million in the first ten months of the year) were transferred back to the country and banks' credit activity intensified considerably. At the end of November the stock of outstanding credit to the corporate sector was 23% larger than it had been a year earlier. But the fastest growing segment of the credit market both in 2001 and in 2002 was that of household credit: after growing 45% over the course of 2001, the stock of outstanding household credit increased by a further 40% in the 11 months to November 2002.

The macroeconomic balance remains in a good shape. Annual inflation turned out to be below the official targets (which were revised upwards at the beginning of the year): in December the CPI was 3.8% higher than a year earlier while the average annual CPI inflation amounted to 5.8%. The final months of the year brought about a substantial reduction in registered unemployment, which fell between October and December by 1.1 percentage points to 16.3%, the lowest level in three years. However, it remains to be seen whether this reflects a genuine decline in joblessness or is related to the envisaged reform in registration schemes in 2003 (which involves an attempt to substitute part of the unemployment assistance with different forms of public works). The fiscal stance remained relatively tight: according to preliminary estimates, the consolidated general government deficit for the year was 0.7%, which was within the 0.8% target and below the 2001 level (0.9%). The two foreign debt restructuring deals undertaken in 2002 and the weakening of the US dollar helped to substantially reduce the level of public debt, which at the end of September fell to 59% of GDP (from 70% at the end of 2001).

The current account deficit declined sharply in 2002: by the end of October it was just USD 216 million, down from USD 585 million a year earlier (also in October, the 12-month rolling current account deficit was USD 515 million, down from USD 885 million in December 2001). Three main factors contributed to this development. First, the worsening of the merchandise trade balance was arrested and the trade deficit even started to decline, largely due to the low oil prices during most of 2002 (this reversed, however, later in the year). In the second place, there was an improvement in the balance of trade in services thanks to the booming tourist industry. And thirdly, the shrinking of the current account deficit reflects a weakening in the inflow of FDI, as the two largest privatization deals (the Bulgarian Telecom and Bulgartabac, the tobacco monopoly) failed to materialize in 2002.

The policy debate on the 2003 budget brought about the first serious row with the IMF since 1997. The main point of contention was the budget of the National Social Security Institute (NSSI, the first pillar of the new three-pillar pension system) for 2003. As part of the ongoing pension reform, the government introduced as of the beginning of 2003 lower limits ('insurance thresholds') for the minimum payroll contributions to the NSSI, because of massive tax evasion. Due to the perceived high level of taxation of labour costs, a large number of firms (mostly small private ones) seem to be formally paying to their employees the minimum wage only; accordingly, they use this low basis also to make their contributions to the NSSI. Another portion of the actual remuneration apparently is being paid in the shadow economy, thus avoiding taxation (both income and payroll taxes). By introducing the insurance thresholds the government is hoping to be able to reduce the level of tax evasion at least with respect to the payroll taxes.

However, the IMF considered the 2003 revenue targets of the NSSI as rather optimistic and expressed doubts whether the new measures would allow the government to increase the level of aggregate social security contributions to 8.8% of GDP in 2003 (as envisaged in the budget) from their current level of 7.2% of GDP. Similarly, it was considered that the expected VAT revenues in 2003 were overestimated. According to the IMF's more conservative estimates, the consolidated budget deficit in 2003 would not be 0.7% (as envisaged in the government target) but could reach some 2% of GDP, and so it insisted on further expenditure cuts. During two rounds of consultations with the government, the sides could not narrow their positions, raising serious policy concerns: the lack of the IMF stamp on the budget would mean that funding under the current two-year stand-by agreement might be suspended, which could be an extremely negative signal for the markets.

Only during a third round of negotiations in December was the deadlock broken, thus averting the worst-case scenario. While the final agreement did not imply formal changes in the parameters of the 2003 budget, some important contingency measures were introduced. Thus, as part of the funding conditionality, public revenues will be monitored by the IMF on a monthly basis; in case they fall below the target levels in the absence of external shocks, the government undertook a commitment to reduce public spending. On the other hand, the postponement of the large privatization deals allowed the government to carry forward this expected revenue as a possible funding source of future fiscal deficits.

The Bulgarian authorities achieved their main foreign policy objectives in 2002: at the Prague NATO summit in November Bulgaria received an invitation to join NATO, and at the Copenhagen EU summit in December, Bulgaria and Romania managed to push through 2007 as the target date for their EU accession in the final summit documents. Although there is still a long and difficult way to go before these targets materialize, both these events are likely to have a positive impact on investor confidence.

The outlook for 2003 is moderately positive. The favourable outcomes for 2002 raise hopes that the government's target of 4.8% of GDP growth in 2003 could be achieved. If output strengthens, this may bring about a further fall in the level of unemployment. Provided the government continues to pursue a prudent fiscal stance, no immediate threats to macroeconomic stability can be foreseen in 2003. The financing of the current account deficit does not seem to be a source of serious concern either. However, these favourable forecasts will be – probably to a considerable extent – conditional on the strength of the recovery in western Europe and on the absence of major external shocks.

Table BG

Bulgaria: Selected economic indicators

	1996	1997	1998	1999	2000	2001	2002 [1]	2003 forecast	2004 forecast
Population, th pers., end of period	8340.9	8283.2	8230.4	8190.9	8149.5	7891.1	.	.	.
Gross domestic product, BGN mn, nom.	1761.2	17432.6	22421.1	23790.4	26752.8	29618.1	32600	35300	38500
annual change in % (real)	-9.4	-5.6	4.0	2.3	5.4	4.0	4.3	4.5	5
GDP/capita (USD at exchange rate)	1198	1251	1543	1577	1542	1690	1990	.	.
GDP/capita (USD at PPP - wiiw)	5020	5920	6270	6540	7090	7680	8250	.	.
Gross industrial production									
annual change in % (real)	5.1	-5.4	-7.9	-9.3	10.3	-2.4	2.6	4	5
Gross agricultural production									
annual change in % (real)	-11.5	13.7	-1.5	2.7	-9.1	-0.3	.	.	.
Goods transport, public, mn t-kms [2]	79850	86543	82122	85568	84878	78624	.	.	.
annual change in % [2]	-8.4	8.4	-5.1	4.2	.	-7.4	.	.	.
Gross fixed capital form., BGN mn, nom.	238.5	1913.5	2919.8	3600.5	4206.0	5260.0	.	.	.
annual change in % (real)	-21.2	-20.9	35.2	20.8	15.4	19.9	7.4 I-IX	.	.
Construction output total									
annual change in % (real)	-14.0	-4.4	-0.2	8.0	8.1	-6.5	.	.	.
Dwellings completed, units	8099.0	7452.0	4942.0	9824.0	8795.0	5937.0	.	.	.
annual change in %	18.8	-8.0	-33.7	98.8	-10.5	-32.5	.	.	.
Employment total, th pers., average	3285.9	3157.4	3152.6	3087.8	2980.1	2940.3	.	.	.
annual change in %	0.1	-3.9	-0.2	-2.1	-3.5	-1.3	.	.	.
Employees in industry, th pers., average [3]	728.1	838.7	802.5	722.5	662.0	632.2	.	.	.
annual change in % [3]	-5.5	-2.7	-4.3	-10.0	-8.4	-4.5	.	.	.
Reg. unemployed, th pers, end of period	478.5	523.5	465.2	610.6	682.8	662.3	602.0	550	520
Reg. unemployment rate in %, end of period	12.5	13.7	12.2	16.0	17.9	17.3	16.3	15	14
LFS - unemployment rate in %, average	14.1	14.4	14.1	15.7	16.9	19.7	17.8	18	17
Average gross monthly wages, BGN [3]	14.0	127.9	183.3	201.0	224.5	248.3	262.9 I-IX	.	.
annual change in % (real, gross) [3]	-17.1	-16.6	20.7	6.9	1.3	3.0	1.9 I-IX	.	.
Retail trade turnover, BGN mn [4]	723.7	5469.3	7214.2	8023.3	9725.9	10593.0	.	.	.
annual change in % (real) [4]	-7.6	-36.4	18.5	12.3	12.7	2.1	2.2 I-IX	.	.
Consumer prices, % p.a.	121.6	1058.4	18.7	2.6	10.3	7.4	5.8	4	4
Producer prices in industry, % p.a.	130.0	971.1	16.5	3.2	17.1	7.3	3.0 I-XI	.	.
Central government budget, BGN mn									
Revenues	350.0	2983.3	4245.6	4543.5	5136.7	5429.6	12510 [5]	.	.
Expenditures	540.8	3650.0	3930.8	4132.0	5377.4	6012.7	12742 [5]	.	.
Deficit (-) / surplus (+)	-190.9	-666.7	314.7	411.6	-240.7	-583.1	-232 [5]	.	.
Deficit (-) / surplus (+), % of GDP	-10.8	-3.8	1.4	1.7	-0.9	-2.0	-0.7 [5]	.	.
Money supply, BGN mn, end of period [6]									
M1, Money	241.3	2433.9	2960.8	3302.1	3976.3	4883.8	5542.7	.	.
Broad money	1329.0	6163.3	6814.2	7662.1	10061.3	12600.1	14146.5	.	.
Base rate of NB % p.a., end of period	342.1	6.8	5.2	4.5	4.7	4.7	3.4	.	.
Current account, USD mn	163.7	1046.3	-61.4	-651.7	-701.6	-842.2	-650	-600	-500
Current account in % of GDP	1.6	10.1	-0.5	-5.0	-5.6	-6.2	-4.1	-3.1	-2.3
Gross reserves of NB excl. gold, USD mn	483.4	2121.0	2679.4	2892.0	3154.9	3289.6	4406.8	.	.
Gross external debt, USD mn [7]	9601.6	10408.5	10891.9	10913.9	11201.8	10618.7	10550.0 Nov	.	.
Exports total, fob, EUR mn [8]	3901.1	4368.3	3841.2	3733.8	5253.1	5714.2	5900	6200	6600
annual change in %	-5.8	12.0	-12.1	-0.4	40.7	8.8	3	5	6
Imports total, cif, EUR mn [8]	4047.6	4361.4	4475.8	5139.9	7084.9	8127.8	8100	8250	8500
annual change in %	-7.5	7.8	2.6	16.4	37.8	14.7	0	2	3
Average exchange rate BGN/USD	0.176	1.677	1.760	1.838	2.124	2.185	2.077	.	.
Average exchange rate BGN/EUR (ECU)	0.220	1.896	1.972	1.956	1.956	1.956	1.956	1.956	1.956
Purchasing power parity BGN/USD, wiiw	0.042	0.354	0.433	0.443	0.462	0.481	0.500	.	.
Purchasing power parity BGN/EUR, wiiw	0.045	0.389	0.475	0.483	0.501	0.522	0.540	.	.

Notes: 1) Preliminary. - 2) From 2000 new methodology. - 3) In 1996 public sector only. - 4) From 1996 according to NACE classification. - 5) General government bugdet. - 6) According to International Accounting Standards. - 7) From 1997 including trade credits to companies. - 8) From 1999 new methodology. Converted from the national currency to EUR at the official exchange rate.

Source: **wiiw** Database incorporating national statistics; **wiiw** forecasts.

Josef Pöschl

The Czech economy dragging its feet

The Czech economy has inherited a large industrial base; over the past few years, a sizeable segment of the industrial sector has been upgraded thanks to the massive involvement of foreign direct investors – and the process continues on. Seen from that angle, the economy is in good shape. It has the potential to expand rapidly in terms of both capacity and output. At present, however, capacity is not expanding; gross fixed investment has almost stagnated in 2002; and output expansion has switched to low speed. The restraining factor is sluggish foreign demand for want of dynamics in the EU and the western economies in general. In 2002, export revenues grew 9.1% in euro terms – much less than in the previous two years – but shrank by 1.4% in Czech koruna terms. Import growth followed roughly the same pattern, given the very high import content of Czech exports. The difference between the euro and CZK growth rates is the outcome of the nominal appreciation of the koruna vis-à-vis the euro: 3% in 2000, 4% in 2001 and 10% in 2002.

The country's accession negotiations with the EU came to a positive end in December 2002. The Czech Republic is scheduled to join the Union in May 2004, if its citizens give the go-ahead in a referendum to be held later this year (most probably mid-June). The economic ties between the Czech Republic and its EU neighbours are already very intense; direct investors from the EU are already massively involved; the larger part of the business community is enthusiastic about accession. On the political plane, the government with its clearly positive attitude towards the EU has yet to dispel some scepticism among the electorate.

The prospect of EU accession does not make the government's task any easier. It will be under strong pressure to bring the budget deficit into line with one of the Maastricht objectives. Major deficits in the public sector could well prevent the Czech Republic from joining the Economic and Monetary Union in the near future. To make matters worse, both EU pre-accession aid (viz. SAPARD) and several EU post-accession support funds currently available, such as the rural development fund within the EU agricultural budget and the EU structural fund, require some degree of co-financing from the national budget. At the same time, farmers are sure to insist on EU direct payments being topped up from national sources. Together with the government's annual transfers to Brussels, all these mandatory outlays will make for an extremely tight budgetary situation in the years to come.

Many business people, journalists and economists believe that a budget deficit always boosts inflation. Were this true, the Czechs should be grateful to their government for having built up a tidy budget deficit in 2002 which, solely on account of privatization revenues, remained restricted to 2.4% of GDP. Even given this deficit, the price indices fell rather than rose. In 2002 the consumer price index fell in all months except for three, and in January 2003 the index was 0.4% lower than the year before. We can thus speculate whether had there been a balanced budget, deflation might have been significant. Did the restrictive monetary policy actually offset the presumed inflationary impact of the budget deficit? Was it a heroic deed on the part of the National Bank that forced inflation down close to zero? No, quite the contrary! The interest rates under direct control of the National Bank were lower in the Czech Republic than anywhere else in Central Eastern Europe; for example, at the end of 2002 the discount rate was as low as 1.75%. The aim of this policy is to guard against nominal appreciation. As we can see, low interest rates, even if coupled to a significant public deficit, do not necessarily boost inflation.

As for the future of the public sector budget, in January 2003 the Czech finance minister Sobotka presented findings of a group of experts: Were the current budgetary rules to remain in force, so the experts, the overall public sector deficit, calculated according to the EU methodology, would peak in 2005 at close to 7% of GDP, whereas comparatively tough reforms could well bring the deficit down to slightly over 4% in 2005 and less than 4% in 2006.

One of the remarkable features of the Czech public sector hitherto has been that the social security system budget, based on the pay-as-you-go principle, has remained almost balanced. The deficit amounted to 0.2% of GDP in both 2001 and 2002. Within the system's budget, the funds collected for the financing of unemployment benefits displayed a surplus of around 1% of GDP; this more or less offset the pension system deficit. The health insurance budget was balanced. Overall the system's revenues amounted to less than 12% of GDP. Despite the system being in relatively good shape financially, we can already observe the all too familiar pressure building up in favour of a systemic change on the grounds that the public finances need to be consolidated. Admittedly, the increasing proportion of retired people will cause some headaches in future years, irrespective of the system applied. An ever smaller number of economically active people will have to generate income for the economically inactive. The debt-ridden hospitals also pose a pressing problem. That notwithstanding, for the time being the major problems besetting the public sector budget lie elsewhere, such as the deficit run up by the consolidation agency, an institution that in the past took over the bad loans accumulated by badly managed financial and non-financial corporations. Another problem is the low rate of efficiency in collecting taxes: a failing that at least in part is linked to corruption.

The Czech economy is doing relatively well in a difficult international environment. The GDP is likely to continue growing by about 3% throughout 2003 and 2004. Inflation will remain low; pressure will continue to build up in favour of nominal appreciation of the currency. The National Bank will continue to back a comparatively constant exchange rate – the degree to which it will manage to do so is difficult to say. It also depends on the future volume of foreign direct investment inflows.

The rate of unemployment measured as the share of those registered jobless in the total labour force is likely to exceed the 10% mark during the first half of 2003. It is the price to be paid for slow GDP growth. As soon as the most important trading partners and their economies re-enter the bullish mode, unemployment in the Czech Republic should decline somewhat.

Table CZ

Czech Republic: Selected economic indicators

	1996	1997	1998	1999	2000	2001	2002 [1]	2003 forecast	2004 forecast
Population, th pers., mid-year [2]	10315.4	10303.6	10294.9	10282.8	10272.5	10224.2	10189.1	.	.
Gross domestic product, CZK bn, nom.	1567.0	1679.9	1839.1	1902.3	1984.8	2157.8	2250	2350	2475
annual change in % (real)	4.3	-0.8	-1.0	0.5	3.3	3.3	2.6	2.8	3.3
GDP/capita (USD at exchange rate)	5596	5142	5536	5347	5007	5548	5750	.	.
GDP/capita (USD at PPP - wiiw)	12990	13160	13320	13660	13800	15090	15560	.	.
Gross industrial production									
annual change in % (real)	2.0	4.5	1.6	-3.1	5.4	6.5	4.6	4.7	6
Gross agricultural production									
annual change in % (real)	-1.4	-5.1	0.7	0.6	-4.5	2.5	.	.	.
Goods transport, mn t-kms [3]	32581	62460	53591	54620	57343	57777	45900 I-IX	.	.
annual change in %	-0.4	.	-14.2	1.9	5.0	0.8	7.0 I-IX	.	.
Gross fixed capital form., CZK bn, nom.	500.6	514.5	535.5	528.3	561.5	610.9	.	.	.
annual change in % (real)	8.2	-2.9	0.7	-1.0	5.4	7.2	0.9	2	5
Construction industry									
annual change in % (real)	5.3	-3.9	-7.0	-6.5	5.3	9.6	2.5	.	.
Dwellings completed, units	14482	16757	22183	23734	25207	24759	17376 I-IX	.	.
annual change in %	11.4	15.7	32.4	7.0	6.2	-1.8	12.1 I-IX	.	.
Employment total, th pers., average [4]	4972.0	4936.5	4865.7	4764.1	4731.6	4750.2	4796.0	.	.
annual change in %	0.2	-0.7	-1.4	-2.1	-0.7	0.4	1.0	.	.
Employment in industry, th pers., average [4]	1597.7	1550.4	1519.9	1468.7	1429.4	1470.6	1476.1 I-IX	.	.
annual change in %	-1.4	-3.0	-2.0	-3.4	-2.7	2.9	0.7 I-IX	.	.
Reg. unemployed, th pers, end of period	186.3	268.9	386.9	487.6	457.4	461.9	514.4	.	.
Reg. unemployment rate in %, end of period	3.5	5.2	7.5	9.4	8.8	8.9	9.8	10.3	9.8
LFS - unemployment rate in %, average	3.9	4.8	6.5	8.7	8.8	8.1	7.3	7.5	7.4
Average gross monthly wages, CZK [5]	9676	10691	11693	12666	13499	14640	15172 I-IX	.	.
annual change in % (real, gross)	8.8	1.8	-1.2	6.1	2.6	3.6	5.2 I-IX	.	.
Retail trade turnover, CZK bn	.	.	.	.	.	.	.	.	.
annual change in % (real)	12.1	-0.4	-6.8	3.0	4.3	4.5	2.9 I-X	.	.
Consumer prices, % p.a.	8.8	8.5	10.7	2.1	3.9	4.7	1.8	1.6	2.0
Producer prices in industry, % p.a.	4.7	4.9	4.9	1.0	4.9	2.9	-0.5	0.5	1.0
Central government budget, CZK bn									
Revenues	482.8	509.0	537.4	567.3	586.2	626.2	705.0	.	.
Expenditures	484.4	524.7	566.7	596.9	632.3	693.9	750.8	.	.
Deficit (-) / surplus (+)	-1.6	-15.7	-29.3	-29.6	-46.1	-67.7	-45.7	.	.
Deficit (-) / surplus (+), % GDP	-0.1	-0.9	-1.6	-1.6	-2.3	-3.1	-2.0	.	.
Money supply, CZK bn, end of period									
M1, Money	447.1	418.9	404.0	447.8	497.7	583.6	669.8 Nov	.	.
M2, Money + quasi money	1078.1	1177.8	1241.4	1337.5	1412.3	1596.0	1646.6 Nov	.	.
Discount rate, % p.a., end of period	10.5	13.0	7.5	5.0	5.0	3.75	1.75	.	.
Current account, USD mn	-4121	-3564	-1255	-1462	-2718	-2625	-3200	-3500	-4000
Current account in % of GDP	-7.1	-6.7	-2.2	-2.7	-5.3	-4.6	-4.7	-4.3	-4.7
Gross reserves of NB incl. gold, USD mn	12435	9774	12617	12825	13139	14464	23717	.	.
Gross external debt, USD mn	21181	21617	24348	22861	21608	21696	23824 Sep	.	.
Exports total, fob, EUR mn [6]	17691.3	19811.8	23070.4	24640.9	31482.7	37251.2	40629.8	42300	46800
annual change in %	7.2	12.0	16.4	6.8	27.8	18.3	9.1	4	11
Imports total, cif, EUR mn [6]	22189.7	24014.3	25289.4	26387.4	34875.7	40674.8	43046.2	46000	51500
annual change in %	14.4	8.2	5.3	4.3	32.2	16.6	5.8	7	12
Average exchange rate CZK/USD	27.15	31.71	32.27	34.60	38.59	38.04	32.74	.	.
Average exchange rate CZK/EUR (ECU)	34.01	35.80	36.16	36.88	35.61	34.08	30.81	30.5	29
Purchasing power parity CZK/USD, wiiw	11.69	12.39	13.42	13.54	14.00	13.99	14.19	.	.
Purchasing power parity CZK/EUR, wiiw	12.68	13.39	14.62	14.75	14.51	14.93	14.88	.	.

Notes: 1) Preliminary. - 2) From 2001 based on census March 2001. - 3) In 1996 public transport only. - 4) Based on Labour Force Survey data. - 5) Enterprises with more than 100, from 1997 with 20 and more employees. - 6) Converted from the national currency to EUR at the official exchange rate.

Source: **wiiw** Database incorporating national statistics; **wiiw** forecasts.

Sándor Richter

Hungary: the election year is over, repair of damages may begin

Despite the relatively good growth performance compared to the EU 15 or the CEECs, Hungarian economy in 2002 was further departing from the successful growth path of the period 1997-2000 and was heading towards uncertain waters. Runaway wage increases, huge fiscal imbalance, deteriorating competitiveness and a growing current account deficit call for urgent corrections in 2003.

The hysterical political atmosphere related to the general elections in April and the municipal elections in October last year determined the developments in 2002. The irresponsible 'who promises more' contest run by both big parties (the conservative FIDESZ and the socialist MSZP) led to a chain of events that began with the raising of the minimum wages in 2001 and 2002, altogether by nearly to the double by the Orban government. That was topped by the 50% wage raises for public servants by the new Medgyessy administration. Business sector wages increased about 10% in real terms, pushed partly by the distortion in the wage structure due to the disproportionately high new minimum wages, lower than originally expected inflation and partly by the demonstration effect of public sector wage increases. Government transfers to households rose by about 13% in real terms. All that resulted in 8-8.5% growth of household consumption, which is two and a half times the growth rate of the GDP.

GDP growth in 2002 may have attained 3.3%, while growth of domestic use amounted to about 5%. Nevertheless growth was not completely consumption-driven. Gross fixed investment increased by about 6%. That expansion derives from rocketing housing investment of households pushed by state-supported preferential credits and government-initiated infrastructure projects. A warning sign, manufacturing investments declined by about 15% in 2002.

On the production side of the GDP, the performance of industry was weak with 2.6% output growth. Industry’s export sales increased by about 4%, while domestic sales, despite the household consumption bonanza, stagnated. Agricultural output dropped. Due to booming infrastructure investments construction recorded a double-digit growth rate.

In the wake of the appreciating forint and the rapid increase in household consumption the current account deteriorated significantly as compared to the preceding year. An increasing deficit in commodity trade and shrinking surplus in tourism were the two main components of the deterioration, with comparatively equal weight. The current account deficit amounted to an estimated EUR 3.6 billion or more in 2002, that is over EUR 2 billion worse than in 2001, exceeding 5% of GDP. Non debt creating financing was much below the 2001 level;

not even 20% of the current account deficit was counterbalanced by respective inflows in November. Compared to the huge expansion of household consumption the deficit on the current account is relatively moderate. That can be explained by the compensating effect of the decline in manufacturing investment and its impact on imports of investment goods. Commodity exports (BoP) may have increased by about 9%, a remarkable performance considering the declining import demand on Hungary's main export markets and the strong appreciation of the national currency. The growth rate of imports was about 2 percentage points higher than that of exports.

There was an explosive increase in the general government deficit, which amounted to 9.6% of the GDP. Part of this was, however, not having any effect on demand. Certain items that were booked in 2002 had actually been spent in 2000 and 2001 already (highway construction, Hungarian Development Bank, a subsidized credit line for students, etc.) but were treated by the previous government as off-budgetary outlays. Also, some expenditures creating demand only this year were booked in the last days of December 2002 (such as the consolidation of the Budapest public transport company). Without these items, the general government deficit would have amounted to about 5.5-6% of GDP. According to the central bank's estimation, the contribution of government spending to the increase of aggregate demand in 2002 corresponded to 4.3% of GDP.

A spectacular achievement of the year 2002 was the reduction of consumer price inflation from a level of 9-10% (annual average) in the previous three years to 5.3% in 2002. The drop in December-to-December inflation was smaller, from 6.8% to 4.8%. That means that the National Bank of Hungary (NBH) attained its year-end inflation target for 2002 (4.5% ±1%). Part of that success is explained by the repeated postponement of long due price rises of certain important commodities and services (household gas, public transport and medicaments).

The NBH, headed by Mr. Járai, minister of finance in the former government before switching over to the central bank, has been deeply concerned about the wage rises and rapidly growing public finance deficit, especially since the inauguration of the new government in summer last year. Referring to the maximum 4.5% CPI inflation to be attained in December 2003 the central bank kept the interest rates high. By the end of 2002 real interest rates were twice, the interest premium three times as high as in May 2001 when the intervention bend was broadened to ±15% from ±2.25%.

The prospect of high yields on government securities coupled with the declining risk perceived due to the progress achieved in the process of accession to the EU, made Hungary a target for foreign financial investors. The increasing inflow of capital pushed the exchange rate to the strong edge of the intervention band. Reaching that edge at 234.69 HUF/EUR in January 2003, the forint became 13.8% more expensive in euro terms than before the broadening of the intervention band. That implies about 20% real appreciation of the national currency in one and a half years.

In November and December 2002 the monetary policy got into the crossfire of criticism of experts and business circles. The policy of high interest rates was criticized because of its devastating effect on the competitive position of exporters and import-competing firms. It was argued that the inflation target could be achieved with lower interest rates as well. But the central bank stuck to its principle that due to the huge budget deficit and excessive wage raises there was no way to decrease the prime rate because that would endanger the observation of the inflation target. Nevertheless, the central bank cut the prime rate by 0.5 percentage points in November, and to the same extent in December.

In mid-January 2003 a speculative attack was launched against the intervention band of the forint by foreign investors who expected that the central bank and the government could be forced to move the intervention band upwards, allowing for a further appreciation of the forint. The central bank intervened, and allegedly EUR 5 billion or more was bought up in the course of the intervention. To stop further speculative actions the central bank decreased the prime rate within two days, and in two steps, from 8.5% to 6.5%; further the overnight interest rate corridor around the two-week central bank deposit rate was widened the to ±3 percentage points and a quantity limit was set on the availability on two-week deposits. With these steps the effective key policy rate dropped to 3.5%. After the intervention the forint/euro exchange rate declined to 243.72.

That speculative attack showed the limits of using the interest rate policy solely for keeping inflation in the targeted range. The central bank was forced to defend the exchange rate, and while the credibility of the inflation targeting monetary policy may have weakened with the interest rate cuts, the positive side effects of that step are obvious, as a weaker forint is badly needed by the business sector and the new volatility of the interest rates and exchange rate diminishes the chances of speculative attacks in the future.

As the consumption- and non-productive investment-driven economic growth came to its limits by the beginning of 2003 it would be important to stabilize the exchange rate at its new, lower level to support a switch back to an export-based expansion of the economy. That would make even the attainment of the high edge of the targeted inflation range by December 2003 very difficult if not impossible. The market has been reckoning with higher than targeted inflation since November last year. The question is now whether the central bank will try to move the exchange rate closer to the strong edge of the intervention band again in order to force inflation down or whether it accepts the new situation and sets a new inflationary target. A recent interview with central bank governor Járai hints at the realization of the latter option.

In 2003 two issues, the budget and the wages, will play a crucial role. The 2003 budget is restrictive compared to the previous year. The government's target is to reduce the general government deficit to 4.5% of the GDP. Public spending on wages will still grow dynamically, due to pervading effects from the previous year, and the main post for savings will be public investment. The wage rise in the business sector proposed by the tripartite council amounts to 4.5%, in real terms. That means that the rise of incomes and consumption will again be higher than the growth of GDP.

In its optimistic scenario for 2003, the WIIW assumes that Hungary will be returning to the growth path of the earlier years, helped by increasing import demand from its main export markets. That process will certainly not be completed within one year. At an average exchange rate of around 245 HUF/EUR exports will pick up. Productive investment will also start to grow, resulting in higher imports and a deteriorating current account. The fiscal deficit will decrease but will be 0.5 to 1 percentage points higher than targeted. Inflation will remain at the previous year's level, slightly above 5% (annual average). GDP growth will be higher than in 2002 but remains below 4%, falling short of the governments target of 4-4.5%. The pessimistic scenario for 2003 assumes that the central bank returns to its policy mix of a strong forint and a high interest rate, putting inflation reduction above any other target. That would provoke a permanent conflict between the central bank and the government, and would lower the GDP growth rate but not necessarily inflation.

Table HU

Hungary: Selected economic indicators

	1996	1997	1998	1999	2000	2001	2002 [1]		2003 forecast	2004 forecast
Population, th pers., end of period [2]	10301.0	10280.0	10253.0	10222.0	10200.0	10175.0	10155	Nov	.	.
Gross domestic product, HUF bn, nom.	6893.9	8540.7	10087.4	11393.5	13150.8	14823.9	16200		17600	19200
annual change in % (real)	1.3	4.6	4.9	4.2	5.2	3.7	3.3		3.8	4
GDP/capita (USD at exchange rate)	4382	4444	4582	4690	4563	5078	6180		.	.
GDP/capita (USD at PPP - wiiw)	9220	9850	10620	11310	12200	13430	13720		.	.
Gross industrial production										
annual change in % (real)	3.4	11.1	12.5	10.4	18.1	3.6	2.6		7	9
Gross agricultural production										
annual change in % (real)	6.3	-3.3	0.7	0.4	-6.5	15.8	-4		2	.
Goods transport, mn t-kms	24874	24789	27144	26339	26399	26240	18931	I-IX	.	.
annual change in %	5.1	-0.3	9.5	-3.0	0.2	-0.6	-0.5		.	.
Gross fixed capital form., HUF bn, nom.	1475.5	1898.9	2384.6	2724.5	3179.8	3484.7	.		.	.
annual change in % (real)	6.7	9.2	13.3	5.9	7.7	3.1	6		7.5	8
Construction industry										
annual change in % (real)	2.7	8.1	15.3	9.0	7.9	7.7	20.1	I-XI	10	.
Dwellings completed, units	28257	28130	20323	19287	21583	28054	15742	I-IX	.	.
annual change in %	14.3	-0.4	-27.8	-5.1	11.9	30.0	15.1		.	.
Employment total, th pers., average [3)4)]	3648.1	3646.3	3697.7	3811.5	3849.1	3859.5	3861.5	I-XI	.	.
annual change in % [3)4)]	-0.8	0.0	0.7	3.1	1.0	0.3	0		0	0
Employees in industry, th pers., average [5]	789.0	783.5	795.9	834.0	844.8	833.9	819.9	I-XI	.	.
annual change in %	-5.3	-0.7	1.6	0.8	1.3	-1.3	-2.0		.	.
Reg. unemployed, th pers, end of period	477.5	464.0	404.1	404.5	372.4	342.8	.			
Reg. unemployment rate in %, end of period	11.4	11.0	9.6	9.6	8.7	8.0	8.2			
LFS - unemployment rate in %, average	9.9	8.7	7.8	7.0	6.4	5.7	5.8	I-XI	5.8	5.8
Average gross monthly wages, HUF [5]	46837	57270	67764	77187	87645	103553	118643	I-XI	.	.
annual change in % (real, net)	-5.0	4.9	3.6	2.5	1.5	6.4	13.1		4	.
Retail trade turnover, HUF bn	2594.5	2949.1	3682.8	4329.7	4822.0	5394.0	5434.8	I-XI	.	.
annual change in % (real)	-4.9	-1.6	12.3	7.9	2.0	5.4	11.0		.	.
Consumer prices, % p.a.	23.6	18.3	14.3	10.0	9.8	9.2	5.3		5.3	5
Producer prices in industry, % p.a.	21.8	20.4	11.3	5.1	11.6	5.2	-1.8		.	.
Central government budget, HUF bn [6]										
Revenues	2079.3	2364.6	2624.4	3227.6	3681.0	4068.0	4365.8		.	.
Expenditures	2209.1	2703.1	3176.6	3565.8	4049.7	4470.9	5840.5		.	.
Deficit (-) / surplus (+)	-129.8	-338.5	-552.2	-338.1	-368.7	-402.9	-1474.7		.	.
Deficit (-) / surplus (+), % GDP	-1.9	-4.0	-5.5	-3.0	-2.8	-2.7	-9.1		.	.
Money supply, HUF bn, end of period										
M1, Money	1237.2	1528.4	1791.1	2135.6	2378.3	2775.9	3306.1		.	.
Broad money	3352.8	4036.3	4635.8	5399.5	6052.0	7089.8	8409.8		.	.
Refinancing rate, % p.a., end of period	23.0	20.5	17.0	14.5	11.0	9.8	8.5		.	.
Current account, USD mn	-1678	-981	-2298	-2081	-1328	-1105	-3400		-3900	-3700
Current account in % of GDP	-3.7	-2.1	-4.9	-4.3	-2.9	-2.1	-5.4		-5.1	-4.6
Reserves total, excl. gold, USD mn	9714	8400	9312	10824	11202	10738	9706	Nov	.	.
Gross external debt, USD mn	27956	24395	27280	29336	30742	33386	38222	Nov	.	.
Exports total, fob, EUR mn [7]	10471.6	16910.1	20476.8	23491.0	30544.5	34082.0	36100		39000	42900
annual growth rate in %	5.0	35.1	21.1	14.7	30.0	11.6	6		8	10
Imports total, cif, EUR mn [7]	12911.6	18779.5	22871.2	26287.8	34856.3	37654.1	39700		42900	46800
annual growth rate in %	8.5	29.9	21.8	14.9	32.6	8.0	5.5		8	9
Average exchange rate HUF/USD	152.57	186.75	214.45	237.31	282.27	286.54	258.00		.	.
Average exchange rate HUF/EUR (ECU)	191.15	210.93	240.98	252.80	260.04	256.68	242.97		244	240
Purchasing power parity HUF/USD, wiiw	72.55	84.30	92.53	98.38	105.53	108.34	116.16		.	.
Purchasing power parity HUF/EUR, wiiw	78.67	90.73	100.85	107.17	114.51	121.79	126.33		.	.

Notes: 1) Preliminary. - 2) Revised data according to census Feb 2001. - 3) Based on Labour Force Survey. - 4) From 1998 new sample. - 5) Enterprises with more than 10, from 1999 more than 5 employees. - 6) Excluding privatization revenues. - 7) Converted from the national currency to EUR at the official exchange rate. From 1997 including trade of firms with customs free legal status.

Source: **wiiw** Database incorporating national statistics; **wiiw** forecasts.

Leon Podkaminer

Poland: muddling through

Despite the continuing strong decline in gross fixed investment, GDP increased by an estimated 1.3% in 2002. Growth was driven by private consumption (3.3% rise) and the falling deficit on foreign trade in goods and services.

Provisional calculations indicate that private consumption contributed 2.1 percentage points to the GDP growth rate, investment –1.5 and foreign trade 0.7 percentage points.

As the entire national wage bill declined by about 2% in real terms (on account of falling employment) the rise in private consumption must be primarily attributed to the falling propensity of households to save, and also to rising non-wage household income (pensions and personal income of the employers and the self-employed). GDP growth accelerated in consecutive quarters, paralleling faster growth of industrial production and improvements in foreign trade.

The good performance of foreign trade cannot be solely attributed to weak domestic demand forcing firms' exports even at loss. The current business climate analysis[8] suggests a clear improvement in profitability of exports and a marked decline in the share of unprofitable exports. Overall, the total net (post-tax) profits of the non-financial corporate sector have been improving as well. The corporate sector closed the year 2001 with a net loss of PLN 2.5 billion. In January-September 2002 the sector recorded a net profit of PLN 3.1 billion. Net profitability (ratio of net profit to all revenue) rose from –0.3% to 0.4%. (By way of comparison, net profitability was higher than 1.5% in the mid-1990s.) The rising profits follow strong gains in labour productivity coupled with declining unit labour costs.

Despite stronger sales, the vast majority of firms continue to perceive weak demand, the bad financial position of customers and arrears in payments for deliveries as the chief obstacles to expansion. Other factors have been declining in importance. Within a few quarters the percentage of firms naming the exchange rates as an obstacle fell from 24% to 13.9% and the percentage of firms naming high interest rates from 18.6 to 7%. Nonetheless, the demand for credit remains weak, with most firms planning to reduce rather than expand their credit exposure. This reflects falling investment, expectations of further declines in interest rates and also a continuing worsening of firms' credit standing. Currently 24% of firms have 'problems' serving their bank debts (compared with about 15%

8 See the website of the National Bank of Poland, www.nbp.pl/koniunktura.

in 1998-2000). This is of course mirrored by the deterioration of profits recorded by commercial banks which are saddled with non-performing debts whose share is expanding rapidly.

Very low inflation throughout 2002 (and much of 2001), correspondingly anaemic output growth and extremely high unemployment finally induced the National Bank of Poland (NBP) to take positive action. The NBP interest rates were gradually reduced throughout 2002 (e.g. its Lombard rate from 15.5% to 8.75%). In real terms the interest rates have been high anyway and, as such, depressed the money supply. (The M2 aggregate actually fell in 2002, even in nominal terms.) The exchange rates seem to have been discounting the NBP interest rate policy through a series of adjustments in mid-2002 which weakened the zloty, albeit moderately. The further weakening of the zloty which occurred in January 2003, apparently a 'contagion effect' of the turbulence hitting the Hungarian exchange rate market, may in fact represent a further exchange rate adjustment to falling domestic interest rates.

The budget for 2003 assumes 3.5% GDP growth. In all probability growth will be much lower. Although foreign trade is likely to perform well (as there may be further productivity and efficiency gains while a strong nominal appreciation is not expected), it is much less obvious what will happen to private consumption and gross fixed investment. Because employment is likely to fall further and wage incomes are likely to decline, or perhaps at best stagnate, a stabilization of private consumption would not be very surprising. And, given the burden of debts and pervasive uncertainties, the corporate sector need not initiate a strong investment recovery. Under such a pessimistic (but not unrealistic) scenario the GDP growth in 2003 would hinge on improvements in foreign trade – and may be much lower than assumed.

In mid-2002 there was a change at the helm of the finance ministry. However, the hopes (or fears) that this would bring definite changes in the fiscal policy have been largely disappointed. Some of the conceptually sound initiatives of the ministry proved badly prepared and were blocked in the parliament (together with the properly prepared ones). Worse still, the ministry seems to be seriously contemplating cuts in spending and social security transfers which are certain to interfere with the recovery. These cuts seem to have good chances of passing through the parliament uncontested.

The general orientation of the fiscal policy in 2003 and 2004 has much to do with the upcoming EU accession. The government will attempt to 'clean' the public finances. This is considered necessary for the adoption of the euro 'as soon as possible', which is the officially declared joint intention of the NBP and the government. Of course a lean budget is also considered necessary because of the intention of making maximum use of the EU transfers, which require national co-financing. Whether or not the GDP losses due to the upcoming fiscal changes will be eventually compensated by the effects of the EU transfers is an open question. In the long run they will probably be. But in the short run these changes are quite certain to depress popular moods further. Under such conditions the outcome of the accession referendum (to be held in April) is not yet certain.

Table PL

Poland: Selected economic indicators

	1996	1997	1998	1999	2000	2001	2002 [1)]	2003 forecast	2004 forecast
Population, th pers., end of period	38639	38660	38667	38654	38644	38632	38618 [Nov]	.	.
Gross domestic product, PLN mn, nom.	387827	472350	553560	615115	684982	749311	769400	800500	849200
annual change in % (real)	6.0	6.8	4.8	4.1	4.0	1.0	1.3	2	3
GDP/capita (USD at exchange rate)	3724	3725	4098	4011	4078	4737	4880	.	.
GDP/capita (USD at PPP - wiiw)	7360	8040	8490	9010	9550	10320	10510	.	.
Gross industrial production (sales)									
annual change in % (real)	8.3	11.5	3.5	3.6	6.7	0.3	1.5 [2)]	2	2
Gross agricultural production									
annual change in % (real)	0.7	-0.2	5.9	-5.2	-5.6	5.8	.	.	.
Goods transport, mn t-kms	309272	329737	317052	310698	282559	253269	.	.	.
annual change in %	2.8	6.6	-3.8	-2.0	-9.1	-10.4	.	.	.
Gross fixed capital form., PLN mn, nom.	80390	110853	139205	156690	170430	157209	.	.	.
annual change in % (real)	19.7	21.7	14.2	6.8	2.7	-8.8	-7.2	.	.
Construction output total									
annual change in % (real)	3.0	16.5	12.4	6.2	1.0	-6.4	-10.5 [2)]		
Dwellings completed, units	62130	73706	80594	81979	87789	105967	99089	.	.
annual change in %	-7.4	18.6	9.3	1.7	7.1	20.7	-6.5	.	.
Employment total, th pers., average	15020.6	15438.7	15800.4	15373.5	15017.5	14923.6	14900	.	.
annual change in %	1.9	2.8	2.3	-2.7	-2.3	-0.6	-0.2	.	.
Employees in industry, th pers., average	3436.0	3433.4	3378.7	3138.4	2955.0	2820.6	2469.0 [2)]	.	.
annual change in %	-0.7	-0.1	-1.6	-7.1	-5.8	-4.5	-5.6 [2)]	.	.
Reg. unemployed, th pers, end of period	2359.5	1826.4	1831.4	2349.8	2702.6	3115.1	3217.0	.	.
Reg. unemployment rate in %, end of period	13.2	10.3	10.4	13.1	15.1	17.5	18.1	18	18
LFS - unemployment rate in %, average	12.3	11.2	10.6	13.9	16.1	18.2	20.0 [I-IX]	20	20
Average gross monthly wages, PLN [3)]	874.3	1065.8	1232.7	1697.1	1893.7	2045.1	2277 [2)]	.	.
annual change in % (real, net) [4)]	5.7	7.3	4.5	4.7	1.0	2.5	0.5 [2)]	.	.
Retail trade turnover, PLN mn	213241	258166	291197	323687	360318	375438	.	.	.
annual change in % (real)	4.5	6.8	2.6	4.0	1.0	0.2	1.7 [2)]		.
Consumer prices, % p.a.	19.9	14.9	11.8	7.3	10.1	5.5	1.9	2	3
Producer prices in industry, % p.a.	12.4	12.2	7.3	5.7	7.8	1.6	1.0	.	.
Central government budget, PLN mn									
Revenues	99675	119772	126560	125922	135664	140527	143538	.	.
Expenditures	108842	125675	139752	138401	151055	172885	182950	.	.
Deficit (-) / surplus (+)	-9167	-5903	-13192	-12479	-15391	-32358	-39412	.	.
Deficit (-) / surplus (+), % GDP	-2.4	-1.2	-2.4	-2.0	-2.2	-4.3	-5.1	.	.
Money supply, PLN mn, end of period									
M1, Money	67866	79240	89920	111384	106456	118297	136267	.	.
M2, Money + quasi money	140039	179378	223678	268701	300424	328198	319777	.	.
Discount rate of NB % p.a., end of period	22.0	24.5	18.2	19.0	21.5	14.0	7.5	8	.
Current account, USD mn	-1371	-4309	-6841	-11553	-9952	-7166	-6734	-7600	-8500
Current account in % of GDP	-1.0	-3.0	-4.3	-7.5	-6.3	-3.9	-3.6	-3.7	-4.3
Gross reserves of NB incl. gold, USD mn	18220	21403	28275	27314	27466	26564	29794	.	.
Gross external debt, USD mn	47541	49647	59135	65365	69465	71754	78735 [Sep]	.	.
Exports total, fob, EUR mn [5)]	19488.2	22798.4	25145.4	25729.3	34382.6	40374.7	43200	45800	49000
annual growth rate in %	10.0	17.0	10.3	2.3	33.6	17.4	7	6	7
Imports total, cif, EUR mn [5)]	29677.1	37484.2	41539.3	43151.2	53121.9	56222.7	58300	60600	64900
annual growth rate in %	32.0	26.3	10.8	3.9	23.1	5.8	4	4	7
Average exchange rate PLN/USD	2.70	3.28	3.49	3.97	4.35	4.09	4.08	.	.
Average exchange rate PLN/EUR (ECU)	3.38	3.71	3.92	4.23	4.01	3.67	3.86	4.15	4.25
Purchasing power parity PLN/USD, wiiw	1.36	1.52	1.69	1.77	1.86	1.88	1.90	.	.
Purchasing power parity PLN/EUR, wiiw	1.48	1.67	1.84	1.92	2.01	2.05	2.03	.	.

Notes: 1) Preliminary. - 2) Enterprises sector with more than 9 employees. - 3) From 1999 including mandatory premium for social security. - 4) From 1999 real gross wages. - 5) Converted from the national currency to EUR at the official exchange rate.

Source: **wiiw** Database incorporating national statistics; **wiiw** forecasts.

Gábor Hunya

Romania: robust growth

With the invitation to join NATO in 2004 and the EU in 2007, the government has achieved its main political targets. These news together with the expected robust economic growth, improving external financial stability and decreasing inflation prompted all international rating agencies to upgrade Romania's rating. Despite all improvements, Romania has still the highest rate of inflation among the accession countries, and per capita GDP has not yet reached its pre-transition level. The EU still does not consider Romania a functioning market economy, privatization is behind schedule and financial indiscipline is acute. The question is how lasting and how high the rate of economic growth can be if the solving of the pressing structural problems is further delayed.

The 4.5% GDP growth recorded for the first nine months of 2002 can be regarded as the likely result for the year as a whole. That represents a deceleration compared to the (still provisional) 5.3% of the previous year and also to the expectation of the government.

Growth in 2002 was fed by a close to 7% increase in industry and construction value added, somewhat moderated by a 5% decline in agriculture. Industry is still growing in the traditional structure, with metallurgy, clothing and petroleum processing featuring the highest growth rates. On the demand side, household consumption, up by about 4%, sets the trend. A piece of very good news is that gross fixed capital formation grew by about 8%, increasing its share in value added to 22%. Private sector investments demonstrate the general confidence in the Romanian economy.

Budgetary policy underwent some tightening in the second half of the year, thus the annual consolidated deficit could be reduced to below 3% of GDP. Subsidies to the energy companies shrank after prices for electricity and gas had been raised. A further decrease of the consolidated budget deficit to 2.7% of GDP is envisaged for 2003. This should be achieved mainly by not increasing outlays at the rate of inflation. Substantial relief to the budget will come from falling interest payments for the public debt, while tax policy will mainly aim at harmonizing tax rates and lowering the tax burden. Corporate income tax on export earnings will be raised from 6% to 12.5%, half of the normal rate which would be reached next year, while there are plans to reduce the overall corporate income tax to 20%. Wage-related taxes were cut by 3 percentage points last year and by another 5% this year. With an overall wage-related tax burden of 50% Romania is still among the high-tax, but low-wage countries.

The external sector improved its contribution to GDP as the deficit on goods and services decreased. Merchandise exports grew by 19.7% in current USD terms and imports by 14.5% during the first 11 months. The trade deficit remained flat at USD 4.3 billion. Neither rising private consumption nor machinery investments generated an extraordinary import surge as in previous years. Romania could increase its market shares in its main market, the EU, for the most important export items: clothing, footwear, machinery and mineral products. Relying on low wages and improving product quality, Romanian companies, primarily foreign subsidiaries, attracted orders from higher-wage accession countries and EU incumbents not only in clothing and footwear but to a growing extent in machinery and electronics.[9]

The current account deficit in 2002 was about USD 1.8 billion, well below that of the previous year. The main factor in the improvement was the increase in transfers of Romanians working abroad (USD 1.3 billion in the first ten months). The balance of services improved as well. The inflow of capital more than balanced the current account deficit. International bond issues as well as multilateral credits contributed to a wider availability of external funds. Both foreign debts and reserves increased by some USD 2 billion. The only item below expectation was the inflow of FDI, USD 823 million in the first ten months, less than the previous year. The unsuccessful privatization attempt of the largest commercial bank, BCR, can be blamed for this.

Both the government and the central bank have done their job to reduce inflation. The achieved 22.5% on annual average is a good deal lower than in previous years but still higher than in most other transition countries. The gradualistic approach to dsinflation helped to maintain international competitiveness. The central bank did not allow much appreciation of the Romanian leu (ROL) against the euro and decreased the local currency interest rates all through the year. The reference rate was brought down from 35% to 20%. The easing of the interest burden stimulated non-government borrowing, which increased by 40% in the first ten months and even more lately. More than 62% of it was taken in foreign currency, thus dollarization remained a characteristic feature. The central bank started to counteract by decreasing the compulsory reserve rate for ROL deposits and increasing it for USD loans. Monetary expansion and wage rises also fuelled inflation in the last quarter of 2002. Increasing liquidity in the economy in 2003 will support growth but may slow down disinflation.

9 For details see G. Hunya, 'Restructuring Through FDI in Romanian Manufacturing', *wiiw Research Reports*, no. 287, August 2002.

Privatization proceeded at the usual sluggish pace. Law amendments in 2002 allowed for the rescheduling of tax and payment arrears for companies undergoing privatization. In January 2003 the generosity was further extended to unpaid utility bills. Utility companies, in turn, are exempted from various tax payments to balance their losses. This indicates that there is no fair competition between the private and the public sector, and the government aims to support the functioning of public sector companies with discretionary measures. Another privatization-related problem is the set of obligations the new owners have to pledge. These concern the number of workforce kept and future investment outlays. Checking commitments and suing non-performing firms has become one of the main activities of the privatization agency, while this attitude discourages potential investors.

The IMF considers that there will be no problem closing the current stand-by agreement by the extended deadline, August 2003. This would be the first of six such credit lines totally disbursed. It is likely that no new agreement will be put in place, which would relieve the Romanian authorities of the IMF straightjacket. More autonomy on the one hand, more freedom to stall reforms, on the other.

While the Romanian government maintains 5-5.5% as the feasible medium-term growth target, we consider 4% to be more in line with the international environment and the pace of structural reforms. This forecast is in fact higher than expected earlier and takes into account that catching-up to pre-transformation GDP can be faster than the normal growth rate and that EU pre-accession aid provides for more external financing than earlier assumed. We also think that disinflation will be slower than expected and year-end inflation will not come down to single digit by the end of 2004.

Table RO

Romania: Selected economic indicators

	1996	1997	1998	1999	2000	2001	2002 [1]	2003 forecast	2004 forecast
Population, th pers., mid-year	22607.6	22545.9	22502.8	22458.0	22435.2	22409.0	.	.	.
Gross domestic product, ROL bn, nom.	108920	252926	371194	545730	800308	1154126	1483500	1820000	2180000
annual change in % (real)	3.9	-6.1	-4.8	-1.2	1.8	5.3	4.5	4	4
GDP/capita (USD at exchange rate)	1563	1565	1872	1585	1644	1772	2000	.	.
GDP/capita (USD at PPP - wiiw)	6630	5640	5450	5510	5740	6180	6460	.	.
Gross industrial production									
annual change in % (real)	6.3	-7.2	-13.8	-2.4	7.1	8.2	6.0	4	4
Gross agricultural production									
annual change in % (real)	1.3	3.4	-7.5	5.2	-14.2	21.7	.	.	.
Goods transport, mn t-kms [2]	106758	87590	62364	45988	42131	40648	.	.	.
annual change in %	-15.8	-18.0	.	-26.3	-8.4	-3.5	.	.	.
Gross fixed capital formation, ROL bn, nom.	24998.5	53540.1	68111.6	96630.4	151486.2	219289.3	.	.	.
annual change in % (real)	5.7	1.7	-5.7	-4.8	4.6	6.6	8	5	5
Construction output total									
annual change in % (real)	3.7	-24.4	-0.5	-0.2	2.8	4.1	4.9 I-IX	.	.
Dwellings completed, units	29460	29921	29692	29517	26376	27041	15610 I-IX	.	.
annual change in %	-17.8	1.6	-0.8	-0.6	-10.6	2.5	7.4	.	.
Employment total, th pers., end of period	9379.0	9022.7	8812.6	8420.0	8629.0	.	.	.	.
annual change in %	-1.2	-3.8	-2.3	-4.5	2.5	.	.	.	.
Employees in industry, th pers., average	2586.0	2443.0	2272.0	1991.0	1873.0	1817.0	1817.8 I-X	.	.
annual change in %	-1.1	-5.5	-7.0	-12.4	-5.9	-3.0	-0.8	.	.
Reg. unemployed, th pers, end of period	657.6	881.4	1025.1	1130.3	1007.1	826.9	760.6	.	.
Reg. unemployment rate in %, end of period	6.6	8.9	10.4	11.8	10.5	8.4	8.1	8	8
LFS - unemployment rate in %, average [3]	6.7	6.0	6.3	6.8	7.1	6.6	9.0 I-VI	9	9
Average gross monthly wages, ROL	426610	846450	1357132	1957731	2876645	4282622	5354872 I-XI	.	.
annual change in % (real, net)	9.3	-22.6	3.4	-3.8	4.6	4.5	3.7	.	.
Retail trade turnover, ROL bn [4]	35316	83035	125513	160137	213569	.	.	.	.
annual change in % (real) [4]	15.3	-12.1	20.6	-6.4	-7.0	0.4	0.5 I-XI	.	.
Consumer prices, % p.a.	38.8	154.8	59.1	45.8	45.7	34.5	22.5	18	15
Producer prices in industry, % p.a.	49.9	152.7	33.2	44.5	53.4	41.0	24.9 I-XI	.	.
Central government budget, ROL bn									
Revenues	18373	43835	67216	93240	120342	148203	163194 I-XI	.	.
Expenditures	23732	52897	77617	106887	149168	184012	202620 I-XI	.	.
Deficit (-) / surplus (+)	-5359	-9062	-10401	-13647	-28826	-35809	-39426 I-XI	.	.
Deficit (-) / surplus (+), % GDP	-4.9	-3.6	-2.8	-2.5	-3.6	-3.1	.	.	.
Money supply, ROL bn, end of period									
M1, Money	11173	18731	22110	29669	46331	64309	72822 Nov	.	.
M2, money + quasi money	30335	62150	92530	134123	185060	270512	334584 Nov	.	.
Discount rate, % p.a., end of period [5]	35.0	40.0	35.0	35.0	35.0	35.0	20.4	.	.
Current account, USD mn	-2571	-2137	-2968	-1469	-1363	-2317	-1800	-2500	-2500
Current account in % of GDP	-7.3	-6.1	-7.1	-4.1	-3.7	-5.8	-4.0	-4.7	-4.6
Gross reserves of NB excl. gold, USD mn	550.7	2193.5	1374.8	1526.3	2469.7	3922.5	6145	.	.
Gross external debt, USD mn [6]	7208.9	8584.3	9322.6	8770.7	10273.4	11950.0	14292 Nov	.	.
Exports total, fob, EUR mn [7]	6375.9	7434.4	7412.4	7955.6	11219.2	12710.7	14500	15400	16300
annual growth rate in %	5.4	16.6	-0.3	7.3	41.0	13.3	14	6	6
Imports total, cif, EUR mn [7]	9018.6	9946.3	10569.3	9896.0	14128.2	17362.5	19100	20400	21800
annual growth rate in %	14.8	10.3	6.3	-6.4	42.8	22.9	10	7	7
Average exchange rate ROL/USD	3082.6	7167.9	8875.6	15332.9	21692.7	29060.9	33055.5	.	.
Average exchange rate ROL/EUR (ECU)	3862.9	8090.9	9989.3	16295.6	19955.8	26026.9	31255.3	36000	40000
Purchasing power parity ROL/USD, wiiw	726.9	1988.5	3028.9	4414.0	6215.9	8329.1	10257.6	.	.
Purchasing power parity ROL/EUR, wiiw	788.2	2181.1	3319.0	4808.2	6744.7	9037.7	11075.6	.	.

Notes: 1) Preliminary. - 2) From 1998 new methodology in road transport. - 3) From 2002 new methotology in accordance to EU definitions. - 4) From 1998 new methodology. - 5) Reference rate of NB from February 2002. - 6) Medium- and long-term. - 7) Converted from USD to EUR using the ECB EUR/USD foreign exchange reference rate.

Source: **wiiw** Database incorporating national statistics; **wiiw** forecasts.

Zdenek Lukas

Slovakia: growth backed by domestic demand

The Slovak GDP expanded by more than 4% in 2002 compared to 3.3% growth in 2001. Growth was driven mainly by private consumption, which rose by over 5%. At a historically low inflation rate and strongly rising wages real household income expanded considerably. The volume of private credits (mainly mortgages and consumer loans) increased as well. Gross fixed capital formation stagnated. The contribution of foreign trade (goods and services) to GDP growth remained negative. The foreign trade deficit was yet diminishing, particularly so in the last quarter of 2002, despite the real appreciation of the Slovak koruna (SKK). Supported by FDI, exports are gradually shifting to high-value-added branches such as manufacturing of transport equipment and electrical and optical equipment, which together account already for about 40% of merchandise exports.

Gross industrial production increased by more than 6% in 2002; labour productivity rose by more than 3%. In manufacturing, growth rates were highest in electrical and optical equipment, leather & leather products, and rubber & plastic products (about 24%, 14% and 12%, respectively). However, with more than 10% growth transport equipment, the largest manufacturing sub-sector, contributed most to the expansion of manufacturing. Car production (VW Bratislava) increased by nearly 30% and has again become the main driving force of manufacturing growth. Output of the construction sector rose by more than 3% in 2002, following stagnation in 2001 and three years of decline before.

The historically low inflation rate of 3.3% year on year was mainly the result of the postponement of price deregulation due to the parliamentary elections in September 2002. In addition, lower oil prices, low EU inflation, appreciation of the currency as well as weak food prices push consumer prices down. With tax collection improving, Russia's debt being repaid and expenditures being cut in the last two months of the year, the central government's deficit fell slightly to some 4% of GDP in 2002, compared to 4.5% in 2001.

In the course of 2002 the unemployment rate dropped by about 1 percentage point to 17.4% at year-end. Nevertheless, there is hardly any sign that the accelerated GDP expansion is essentially easing the unemployment problem. Rationalization measures adopted by new owners after acquisition of over-staffed companies and lack of labour market reform often impede any further drop in unemployment. Furthermore, the employment effects expected by green-field investments have been so far moderate. Long-term unemployed, less adaptable to new jobs, are taking an increasingly larger share in total unemployed. Regional disparities are becoming ever more pronounced. Economic activity is focusing on the already flourishing western region where both domestic and foreign investors find highly skilled labour, a well-developed infrastructure and, in retail trade, also outlets for consumers with strong purchasing power. As a result, with unemployment rates of about 30% in the country's eastern regions, the Slovak labour market features the largest disparities of all CEE candidate countries.

Those regional disparities are likely to even increase in the near future as the French car maker PSA Peugeot Citroen will build an auto factory in the Trnava industrial park, some 40 kilometres northeast of Bratislava. Total FDI into the project is to amount to close to EUR 0.7 billion by 2006 when the annual output capacity will reach 300,000 cars and more than 3000 workers will find jobs there. This is certainly good news for the Slovak economy as a whole. But experience from other big FDI projects allocated in western Slovakia indicate that spillover effects, if there are any, have again been confined mostly to the western, better developed part of the country. Total FDI inflows in 2002 probably exceeded USD 4 billion, of which however more than 98% went into the Bratislava region; the lion's share, nearly EUR 3 billion, was invested in a 49% stake in the Slovak gas utilities. By concluding the latter deal the largest part of the Slovak privatization programme has been implemented.

In the wake of strong FDI and portfolio inflows, the Slovak koruna has appreciated by about 7% in nominal terms since August 2002. Nevertheless, due to expanding high value-added exports (mainly cars), the foreign trade deficit dropped slightly to less than EUR 2.3 billion in 2002. As a result the current account deficit fell slightly as well, to some 8% of GDP in 2002 as compared to 8.6% in 2001.

The new coalition government, in power since October 2002, will probably push through an economic programme that is first of all targeted at the stabilization of public sector expenditures such as healthcare, education and public administration. Thus greater fiscal prudence is expected for 2003 and 2004. Domestic demand will probably lose momentum in its role as the main driving force behind the country’s economic growth. However, as exports will further expand, GDP growth in 2003 will decelerate only modestly to some 3.5%. For 2004 we expect higher GDP growth, thanks to expanding exports and slight recovery in domestic demand. The inflation rate will rise to about 7%, as the government restarted, at the beginning of 2003, to deregulate controlled prices for utilities, rents and public services. The current account deficit will decrease substantially, to 4% of GDP in 2003, again thanks to the export expansion but also benefiting from the weak US dollar that counteracts the current high oil prices. In 2004 the current account deficit may decrease even further because of strong exports. At the same time, the expected high FDI and portfolio inflows on the eve of EU accession will trigger an appreciation of the domestic currency, which however may undermine long-term gains in export competitiveness.

Table SK

Slovak Republic: Selected economic indicators

	1996	1997	1998	1999	2000	2001	2002 [1)]		2003	2004
									forecast	
Population, th pers., mid-year	5373.8	5383.2	5390.7	5395.3	5400.7	5379.8	5378.6		.	.
Gross domestic product, SKK bn, nom.	628.6	708.6	775.0	835.7	908.8	989.3	1055		1140	1245
annual change in % (real)	5.8	5.6	4.0	1.3	2.2	3.3	4.2		3.5	4.5
GDP/capita (USD at exchange rate)	3816	3915	4080	3740	3642	3804	4330		.	.
GDP/capita (USD at PPP - wiiw)	9590	10320	11070	11430	11280	12040	12600		.	.
Gross industrial production										
annual change in % (real)	2.5	2.7	5.0	-2.7	8.6	6.9	6.3		5.5	6
Gross agricultural production										
annual change in % (real)	2.0	-1.0	-5.9	-2.5	-12.3	7.8	.		.	.
Goods transport, mn t-kms	18785	17672	17808	19996	19829	17486	.		.	.
annual change in %	-7.9	-5.9	0.8	12.3	-0.8	-11.8	.		.	.
Gross fixed capital form., SKK bn, nom.	203.4	242.9	280.9	252.9	267.9	309.6	.		.	.
annual change in % (real)	30.9	14.3	11.0	-18.5	1.2	9.6	1		5	7
Construction industry										
annual change in % (real)	4.4	9.2	-3.5	-25.8	-0.4	0.8	3.4	I-XI	.	.
Dwellings completed, units	6257	7172	8234	10745	12931	10321	8513	I-IX	.	.
annual change in %	1.6	14.6	14.8	30.5	20.3	-20.2	25.2	I-IX	.	.
Employment total, th pers., average [2)]	2224.9	2205.9	2198.6	2132.1	2101.7	2123.7	2119.1	I-IX	.	.
annual change in %	3.6	-0.9	-0.3	-3.0	-1.4	1.0	0.0	I-IX	.	.
Employment in industry, th pers., average [2)]	690.0	665.8	662.5	630.3	615.3	629.1	639.8	I-IX	.	.
annual change in %	6.1	-3.5	-0.5	-4.9	-2.4	2.2	2.3	I-IX	.	.
Reg. unemployed, th pers, end of period	329.7	347.8	428.2	535.2	506.5	533.7	504.1		.	.
Reg. unemployment rate in %, end of period	12.8	12.5	15.6	19.2	17.9	18.6	17.5		17	16
LFS - unemployment rate in %, average	11.3	11.8	12.5	16.2	18.6	19.2	19.0		18	17
Average gross monthly wages, SKK	8154	9226	10003	10728	11430	12365	12924	I-IX	.	.
annual change in % (real, gross)	7.1	6.5	1.7	-2.8	-4.5	0.8	5.7	I-IX	.	.
Retail trade turnover, SKK bn [3)]	296.5	328.8	379.4	442.1	481.1	301.1	287.7	I-XI	.	.
annual change in % (real)	6.9	4.8	8.6	9.8	2.3	4.5	3.8	I-XI	.	.
Consumer prices, % p.a.	5.8	6.1	6.7	10.6	12.0	7.1	3.3		7	7
Producer prices in industry, % p.a.	4.2	4.5	3.3	4.3	10.8	6.5	2.1		.	
Central government budget, SKK bn										
Revenues	166.3	180.8	177.8	216.7	213.5	205.4	220.4		.	.
Expenditures	191.9	217.8	197.0	231.5	241.1	249.7	272.0		.	.
Deficit (-) / surplus (+)	-25.6	-37.0	-19.2	-14.8	-27.6	-44.4	-51.6		.	.
Deficit (-) / surplus (+), % GDP	-4.1	-5.2	-2.5	-1.8	-3.0	-4.5	-4.9		.	.
Money supply, SKK bn, end of period										
M1, Money	173.9	166.1	147.2	153.9	187.2	228.5	228.6	Nov	.	.
M2, Money + quasi money	416.9	453.5	466.1	523.6	601.5	680.3	703.9	Nov	.	.
Discount rate, % p.a., end of period	8.8	8.8	8.8	8.8	8.8	8.8	6.5		.	.
Current account, USD mn	-1960	-1804	-1982	-980	-701	-1756	-1900		-1300	-1000
Current account in % of GDP	-9.6	-8.6	-9.0	-4.9	-3.6	-8.6	-8.2		-4.5	-3.3
Gross reserves of NB incl. gold, USD mn	3473	3285	2923	3425	4077	4189	9195		.	.
Gross external debt, USD mn	7810	10700	11900	10518	10804	11043	12200	Oct	.	.
Exports total, fob, EUR mn [4)]	7048.0	7299.0	9540.6	9602.2	12879.5	14115.4	15255.7		16800	18600
annual growth rate in %	6.2	3.6	11.9	0.6	34.1	9.6	8.1		10	11
Imports total, fob, EUR mn [4)]	8877.7	9119.0	11634.7	10627.7	13859.8	16487.8	17519.2		18400	19900
annual growth rate in %	30.9	2.7	12.3	-8.7	30.4	19.0	6.3		5	8
Average exchange rate SKK/USD	30.65	33.62	35.24	41.42	46.20	48.35	45.33		.	.
Average exchange rate SKK/EUR (ECU)	38.40	38.01	39.60	44.12	42.59	43.31	42.69		41.5	41
Purchasing power parity SKK/USD, wiiw	12.20	12.75	12.99	13.55	14.92	15.28	15.57		.	.
Purchasing power parity SKK/EUR, wiiw	13.22	13.63	14.16	14.77	15.30	15.78	15.84		.	.

Notes: 1) Preliminary. - 2) Based on Labour Force Survey. - 3) From 2001 according to NACE, excluding VAT. - 4) Converted from the national currency to EUR at the official exchange rate; from 1998 new methodology.

Source: **wiiw** Database incorporating national statistics; **wiiw** forecasts.

Hermine Vidovic

Slovenia: sizeable current account surplus

Real GDP is estimated to have grown by 3% in 2002. Growth was mainly supported by foreign demand, especially by expanding exports of goods and services that gained momentum from the second quarter of the year. Having dropped by 2% in 2001, investment growth accelerated from quarter to quarter in 2002 and rose by about 3% in the year as a whole. The rise in investment growth had a positive impact on construction activities, which resumed growth in the second quarter, after several quarters of contraction.

The annual growth of industrial output decelerated to 2.4% in 2002, while an increase of 2% was reported for manufacturing. Within the latter, the fastest growth rates were recorded for strongly export-oriented branches (industries that realize more than 70% of their revenues abroad) such as machinery and equipment, chemicals, and transport equipment. In contrast, export-oriented labour-intensive industries (net revenues from sales abroad 50-70%) such as textiles, leather and leather products suffered from the strongest declines.

Consumer price inflation remained stubbornly high, at 7.5% year on year. Several factors can be pointed at for this development: at the beginning of the year inflation was pushed upwards by raising the VAT rate from 19% to 20% and by the increase of excise duties on tobacco and alcohol as well by surges in administered prices, e.g. telecom and public utilities. Later in the year prices were affected by the jump in oil prices, which translated into higher prices of petrol. In order to bring inflation down the Bank of Slovenia and the government agreed upon joint efforts: consequently 'rises in administered prices – considered as one of the major sources of inflation – should not exceed the targeted level of inflation' and changes on the fiscal side are to be examined for their impact on inflation. According to the monetary guidelines the M3 growth target will remain the main instrument, and apart from other indicators a medium-term inflation target of 3-4% has been set. As far as the exchange rate is concerned, the Bank of Slovenia will pursue a policy of continuous gradual depreciation, keeping the real exchange rate more or less stable.

Employment creation continued, albeit at a weak pace, while the number of registered unemployed remained almost stagnant; the unemployment rate was 11.7% in December 2002. The Active Employment Policy Programme for 2003, adopted in November 2002, should help to improve the employability of disadvantaged groups on the labour market such as long-term unemployed over 45 years with a low educational level. The programme is also envisaged to counteract the announced layoffs in the textiles, clothing and footwear industries. Real net wage growth slowed down to 1.9% during the first eleven months of 2002.

In late December the Slovenian parliament adopted the central budgets for 2003 and 2004, with the deficits for both years expected to remain below 1% each of the projected GDP (as for the general government the respective ratios are 1.2% and 0.9%). At the same time the programme for the sale of state-owned property was adopted, offering a comprehensive list of enterprises in the manufacturing, banking and infrastructure sectors: e.g., 80% of the Slovenian steelworks group, the footwear makers Peko and Planika, the oil company Nafta Lendava, the aluminium producer Talum and the leather manufacturer IUV; within the banking sector stakes are offered in Slovenia's second largest bank Nova Kreditna Banka Maribor (NKBM) and Poštna Banka; other companies to be sold are the Port of Koper, the Aerodrom Ljubljana and Telekom Slovenija.

Export activities gained momentum in the second quarter of the year. Measured in current euro terms, exports expanded by 5.5% and imports by 1% in 2002. The poor export performance to the European Union was largely compensated by a further increase in sales to the Yugoslav successor states, to CEFTA and Russia. As a result the foreign trade deficit was substantially lower than in 2001, which translated into a remarkable current account surplus in 2002, at close to 2% of the GDP.

The high level of FDI inflows witnessed in 2001 continued during 2002 and reached USD 1.9 billion in the first eleven months of the year. These investments were mainly due to takeovers in the trade, manufacturing and banking sectors (for instance, the pharmaceutical company Lek was sold to Novartis, a stake of Nova Ljubljanska Banka to the Belgian KBC and EBRD). Following these large foreign investments, monetary and exchange rate policies were conducted towards sterilizing foreign exchange inflows, with currency swap operations being the most important instruments. In parallel the Bank of Slovenia withdrew money through tolar transactions, using bills which were introduced in November and offered to the banks by the end of 2002.[10]

In December prime minister Janez Drnovšek was elected Slovenian president, following Milan Kucan, who had held this office since 1991. The hitherto minister of finance, Anton Rop, was appointed prime minister and his post was taken over by Dušan Mramor, a university professor of economics.

[10] Part of the inflow of the partial sale of NLB was deposited by the government with the Bank of Slovenia as a time deposit, while the earnings from Lek were dispersed between legal and natural persons and paid in both tolars and foreign currency. See *Slovenian Economic Mirror*, 12/2002.

Assuming that the European economy will not lift off any time soon, expectations for the Slovenian economy are moderate for 2003. Real GDP might grow by about 3-3.5%, while a more pronounced upswing may occur only in 2004. Investment activities may lend impetus to economic growth in 2003, coupled with a moderate increase in exports. The rate of inflation will continue its downward path provided there is no major change in oil prices.

Table SI

Slovenia: Selected economic indicators

	1996	1997	1998	1999	2000	2001	2002 [1]	2003	2004
								forecast	
Population, th pers., mid-year	1991.2	1986.8	1982.6	1985.6	1990.3	1992.0	1995.7	.	.
Gross domestic product, SIT bn, nom.	2555.4	2907.3	3253.8	3648.4	4035.5	4566.2	5056	5540	6080
annual change in % (real)	3.5	4.6	3.8	5.2	4.6	3.0	3	3.3	4
GDP/capita (USD at exchange rate)	9481	9163	9878	10109	9105	9443	10550	.	.
GDP/capita (USD at PPP - wiiw)	13220	14100	14840	15810	16880	17760	18530	.	.
Gross industrial production									
annual change in % (real)	1.0	1.0	3.7	-0.5	6.2	2.9	2.4	3	3
Gross agricultural production									
annual change in % (real)	1.0	0.0	2.2	-1.3	2.4	.	.	.	.
Goods transport, mn t-kms [2]	37820	37859	36733	40041	37003	41505	33302 I-XI	.	.
annual change in %	0.2	0.1	-3.0	9.0	-7.6	5.6	-12.5 I-XI	.	.
Gross fixed capital form., SIT bn, nom.	574.6	679.5	800.6	999.2	1076.8	1138.7	.	.	.
annual change in % (real)	8.9	11.6	11.3	19.1	0.2	-1.9	3.5	4	5
Construction output, in effect. working time									
annual change in % (real)	-2.5	-5.2	1.7	10.2	-1.2	-2.1	-3.4 I-XI	.	.
Dwellings completed, units [3]	6228	6085	6518	5142	6460	5475	3796 I-IX	.	.
annual change in %	9.0	-2.3	7.1	-21.1	25.6	-5.8	-14.5 I-IX	.	.
Employment total, th pers., average	741.7	743.4	745.2	758.5	768.2	779.0	783.6 I-XI	.	.
annual change in %	-0.5	0.2	0.2	1.8	1.3	1.4	0.6 I-XI	.	.
Employees in industry, th pers., average [4]	239.2	248.5	246.2	242.8	241.6	243.5	246.3 I-X	.	.
annual change in %	-5.2	-2.1	-0.9	-1.4	-0.5	0.8	1.0 I-X	.	.
Reg. unemployed, th pers, end of period	124.5	128.6	126.6	114.3	104.6	104.3	103.0	.	.
Reg. unemployment rate in %, end of period	14.4	14.8	14.6	13.0	12.0	11.8	11.7	10	10
LFS - unemployment rate in %, average	7.3	7.4	7.9	7.6	7.0	6.4	6.4	5.5	5.5
Average gross monthly wages, SIT	129125	144251	158069	173245	191669	214561	233004 I-XI	.	.
annual change in % (real, net)	4.4	2.9	1.5	3.0	1.4	3.1	1.9 I-XI	.	.
Retail trade turnover, SIT bn [5]	871.3	1290.0	1346.7	1555.0	1557.4	1684.8	.	.	.
annual change in % (real) [6]	2.9	1.0	2.1	2.9	7.4	7.8	4.5 I-XI	.	.
Consumer prices, % p.a.	9.9	8.4	7.9	6.1	8.9	8.4	7.5	6	5.5
Producer prices in industry, % p.a.	6.8	6.1	6.0	2.1	7.6	8.9	5.1	.	
General government budget, SIT bn									
Revenues	1091.8	1222.6	1397.9	1590.0	1726.7	1967.8	1653.2 I-X	.	.
Expenditures	1083.6	1256.7	1423.5	1613.3	1781.4	2031.0	1812.6 I-X	.	.
Deficit (-) / surplus (+)	8.2	-34.1	-25.6	-23.3	-54.7	-63.2	-159.4 I-X	.	.
Deficit (-) / surplus (+), % GDP	0.3	-1.2	-0.8	-0.6	-1.4	-1.4	.	.	.
Money supply, SIT bn, end of period									
M1, Money	235.1	270.5	332.7	399.8	424.0	502.2	565.8	.	.
Broad money	1135.3	1411.3	1690.3	1912.9	2206.4	2877.4	3374.3	.	.
Discount rate % p.a., end of period	10.0	10.0	10.0	8.0	10.0	11.0	10.0	.	.
Current account, USD mn	55.5	50.5	-118.0	-698.4	-547.6	30.9	350	100	100
Current account in % of GDP	0.3	0.3	-0.6	-3.5	-3.0	0.2	1.7	0.4	0.4
Gross reserves of NB excl. gold, USD mn	2297.4	3314.7	3638.5	3168.0	3196.0	4329.9	6980.2	.	.
Gross external debt, USD mn	3981	4123	4915	5400	6217	6717	8231 Nov	.	.
Exports total, fob, EUR mn [7]	6640.8	7413.4	8051.9	8037.0	9505.1	10348.7	10920	11470	12160
annual growth rate in %	3.3	11.6	8.6	-0.2	18.3	8.9	5.5	5	6
Imports total, cif, EUR mn [7]	7536.3	8289.7	8999.4	9482.0	10995.7	11345.4	11460	11800	12150
annual growth rate in %	2.9	10.0	8.6	5.4	16.0	3.2	1	3	3
Average exchange rate SIT/USD	135.37	159.69	166.13	181.77	222.68	242.75	240.24	.	.
Average exchange rate SIT/EUR (ECU)	169.51	180.40	186.27	193.63	205.03	217.19	226.22	234	240
Purchasing power parity SIT/USD, wiiw	97.08	103.76	110.56	116.20	120.11	129.10	136.74	.	.
Purchasing power parity SIT/EUR, wiiw	105.26	113.81	121.15	126.58	130.33	140.09	147.64	.	.

Notes: 1) Preliminary. - 2) From 2001 new methodology in road transport. - 3) From 2001 dwellings for which building permits were issued. - 4) In 1996 enterprises with 3 and more employees and excluding persons employed by self-employed. - 5) Including turnover tax; goods transport services, maintenance and repair of motor vehicles are not covered. - 6) Excluding turnover tax; maintenance and repair of motor vehicles are included. - 7) Converted from the national currency to EUR at the official exchange rate.

Source: **wiiw** Database incorporating national statistics; **wiiw** forecasts.

Hermine Vidovic

Croatia: private consumption boosted by bank loans

The high growth of Croatia's GDP in the third quarter of 2002 – 6.5% against the same quarter a year earlier – came rather unexpectedly; the average rate for the first nine months was 5%. Thus, for the year as a whole WIIW will revise up its GDP forecast to 4.5% (against 3.5% earlier). The main driver behind that growth was domestic demand – private consumption and strong (public) investment activities, while government consumption continued to shrink. Household consumption, accounting for about one half of the overall GDP, was spurred by intense lending from the banking sector (following the euro conversion, the liquidity of the banking sector is very high). In November 2002 the stock of household loans exceeded the November 2001 level by 40%, that of corporate loans by 21%. The favourable GDP data must be seen against the background of a further worsening of the trade balance, an expanding current account deficit and growing foreign indebtedness. In response to these developments the Croatian National Bank decided to limit the increase of loans both to the household and corporate sectors to a target growth rate of 16% as of February 2003.

High investment translated into booming construction activities (up 13%) mainly related to the construction of the Zagreb–Split motorway and to housing construction. Real retail turnover expanded by about 13%, of which the sale, maintenance and repair of motor vehicles was almost one quarter higher than a year earlier (Croatian citizens had bought about 70 thousand new cars in 2002). Inflation continued its downward trend, with average retail price inflation at 2.2% year on year.

Industrial production growth gained momentum from the second half of 2002 and was up 5.4% in the year as a whole. Within manufacturing, in line with overall industrial output growth, the best performing branches were publishing and printing, machinery and equipment, and other non-metallic mineral products. The worst results were recorded for wearing apparel, leather products and basic metals. Productivity increases were achieved exclusively through further shedding of labour.

Employment, showing some signs of improvement in 2001, fell again in 2002. Mainly thanks to a change in methodology, registered unemployment dropped, but the rate of unemployment remained high, at 21.5%. The international comparable Labour Force Survey (LFS) unemployment rate – traditionally lower than the registered one – fell from 16.3% in the second half of 2001 to 15.2% in the fist half of 2002.

The performance of foreign trade was extraordinarily poor. In 2002 the trade deficit reached the highest level (EUR 6.1 billion) since Croatia's gaining independence in 1991. Assuming that net earnings from tourism have reached USD 3.3 billion (based on the optimistic scenario of the National Bank) and the values of other current account items have not changed significantly from those in 2001, the current account deteriorated significantly and closed with a deficit of about 5% of the expected GDP in 2002, up from 3.3% a year earlier. Foreign debt totalled USD 14.1 billion by the end of November and was nearly one quarter higher than in December 2001. FDI inflows totalled USD 763.5 million during the first three quarters of 2002, significantly less than in the same period a year earlier (USD 1.2 billion). The banking sector was the main beneficiary of capital inflows, accounting for two thirds of the total, e.g. with Austria’s Erste Bank and Steiermärkische purchasing Rijecka Banka and the Charlemagne Capital Fund taking over Dubrovacka Banka. Another 11% was invested into tourist accommodations. The repeatedly announced (partial) sale of the INA oil company is expected to materialise only in 2003.

At the beginning of February 2003 the IMF approved a new standby credit worth USD 146 million. The economic programme agreed upon with the Fund aims at further fiscal consolidation focussing on the stabilization of the public debt ratio (which is rather questionable considering that public investments will at least in the short run translate into an increase in public debt), no further increases in government guarantees and a tight wage policy in the government sector, comprising among others wage freezes and employment cuts in the defence sector. Accordingly the 2003 budget adopted by the Croatian parliament in December 2002 anticipates a reduction of the general government deficit from an estimated 6.2% in 2002 to 5% in 2003. Deficit financing should rely on the domestic capital market rather than on foreign borrowing and privatization receipts as was the case in the past. Priorities of the budget are science and education, the reform of the judicial system, further reforms and the consolidation of the health system. Subsidies for agriculture and the shipbuilding industry are envisaged to increase as well as the funds for infrastructure investments, e.g. the construction of the Zagreb–Split motorway (mainly financed through domestic and foreign loans), the modernization of the Croatian Railways, for water supply infrastructure and the infrastructure on islands. In contrast, spending for the defence and interior ministries will be cut.

In late 2002 Croatia became the eighth member of CEFTA. The expected impact on the country’s foreign trade seems to be limited, as most of the countries under this agreement will join the European Union in 2004. An important step towards integration will be Croatia’s application for EU membership in February this year. The Croatian authorities hope that the country may enter the Union together with Bulgaria and Romania, reportedly to take place in 2007 – a quite ambitious target considering the time-consuming negotiations of the earlier joining transition countries. Support for this step has been announced by Germany, Austria and Greece and recently also by the EBRD.

The economic outlook for 2003 is moderately positive. Generally, the current trends will continue but GDP growth will be somewhat lower than in 2002 owing to a slowdown of private consumption, as the credit expansion will come to a halt. Consequently import growth is expected to abate and both the trade and current account deficits will be reduced. Substantial improvements on the labour market can hardly be expected. A continuation of the current policy of the National Bank will allow to maintain the stability of the exchange rate and the inflation rate.

Table HR

Croatia: Selected economic indicators

	1996	1997	1998	1999	2000	2001	2002 [1]	2003	2004
								forecast	
Population, th pers., mid-year [2]	4494	4573	4501	4554	4437	4437	.	.	.
Gross domestic product, HRK mn, nom.	107981	123811	137604	141579	152519	162909	174000	186400	199700
annual change in % (real)	5.9	6.8	2.5	-0.9	2.9	3.8	4.5	4	4.5
GDP/capita (USD at exchange rate)	4422	4398	4805	4371	4153	4403	5000	.	.
GDP/capita (USD at PPP - wiiw)	6330	7820	8240	8180	8840	9380	9960	.	.
Gross industrial production [3]									
annual change in % (real)	3.1	6.8	3.7	-1.4	1.7	6.0	5.4	4	5
Gross agricultural production									
annual change in % (real)	1.3	4.0	10.2	-3.5	-10.0	8.4	.	.	.
Goods transport, public, mn t-kms [4]	213172	203428	170107	146302	146852	142338	101827 I-IX	.	.
annual change in %	6.7	-4.6	-16.4	-14.0	.	-1.0	2.6 I-IX	.	.
Gross fixed capital form., HRK mn, nom.	22089.4	29935.6	32065.6	33025.0	33281.0	37252.0	.	.	.
annual change in % (real)	37.6	26.4	2.5	-3.9	-3.8	9.7	10	7	6
Construction industry, hours worked [5]									
annual change in % (real)	9.0	16.7	0.7	-7.7	-9.1	3.6	12.8 I-IX	.	.
Dwellings completed, units	12624	12516	12557	12175	12187	18088	.	.	.
annual change in %	71.5	-0.9	0.3	-3.0	0.1	48.4	.	.	.
Employment total, th pers., average [6]	1329.5	1310.9	1384.8	1364.5	1341.0	1348.3	1340.8	.	.
annual change in % [6]	-6.2	-1.4	0.4	-1.5	-1.7	0.5	-0.6	.	.
Employees in industry, th pers., average [7]	315.1	319.7	308.9	299.5	291.9	287.2	277.2	.	.
annual change in % [7]	-9.8	-6.4	-3.4	-3.0	-2.5	-1.6	-3.5	.	.
Reg. unemployed, th pers, end of period	269.3	287.1	302.7	341.7	378.5	395.1	366.2	.	.
Reg. unemployment rate in %, end of period	15.9	17.6	18.1	20.4	22.3	23.1	21.5	21	21
LFS - unemployment rate in %, average	9.9	9.9	11.4	13.6	16.1	15.9	15.2	15	15
Average gross monthly wages, HRK	3243	3668	4131	4551	4869	5061	5355 I-XI	.	.
annual change in % (real, net)	7.2	12.3	6.0	10.1	3.4	1.6	2.9 I-XI	.	.
Retail trade turnover, HRK mn	29412.4	34736.1	.	.	.	.		.	.
annual change in % (real)	3.4	14.9	0.1	-3.5	10.0	10.0	12.7 I-XI	.	.
Retail prices, % p.a.	3.5	3.6	5.7	4.2	6.2	4.9	2.2	3	2.5
Producer prices in industry, % p.a.	1.4	2.3	-1.2	2.6	9.7	3.6	-0.4	.	.
Central government budget, HRK mn [8]									
Revenues	31368	33846	43809	46356	44636	53444	63657 I-XI	.	.
Expenditures	31502	35006	42552	48879	50744	57202	66913 I-XI	.	.
Deficit (-) / surplus (+)	-134	-1160	1257	-2523	-6108	-3759	-3256 I-XI	.	.
Deficit (-) / surplus (+), % GDP	-0.1	-0.9	0.9	-1.8	-4.0	-2.3	.	.	.
Money supply, HRK mn, end of period									
M1, Money	11369	13731	13531	13859	18030	23704	30866	.	.
Broad money	36701	50742	57340	56659	73061	106071	116138	.	.
Discount rate % p.a., end of period	6.5	5.9	5.9	7.9	5.9	5.9	4.5	.	.
Current account, USD mn	-955.9	-2512.2	-1452.8	-1397.8	-438.9	-616.8	-1100.0	-900	-900
Current account in % of GDP	-4.8	-12.5	-6.7	-7.0	-2.4	-3.2	-5.0	-3.4	-3.4
Gross reserves of NB excl. gold, USD mn	2314.0	2539.1	2815.7	3025.0	3524.8	4704.2	5885.8	.	.
Gross external debt, USD mn	5307.6	7451.6	9586.2	9872.3	11002.2	11209.3	14070.5 Nov	.	.
Exports total, fob, EUR mn [9]	3602.1	3665.8	4046.2	4027.3	4818.0	5210.4	5182.5	5230	5390
annual growth rate in %	0.2	1.8	10.4	-0.5	18.9	8.1	-0.5	1	3
Imports total, cif, EUR mn [9]	6220.3	8059.7	7476.9	7324.1	8588.5	10232.4	11316.3	11880	12470
annual growth rate in %	7.1	29.6	-7.2	-2.0	16.8	19.1	10.6	5	5
Average exchange rate HRK/USD	5.43	6.16	6.36	7.11	8.28	8.34	7.86	.	.
Average exchange rate HRK/EUR (ECU)	6.80	6.96	7.14	7.58	7.63	7.47	7.41	7.5	7.5
Purchasing power parity HRK/USD, wiiw	3.80	3.46	3.71	3.80	3.89	3.92	3.94	.	.
Purchasing power parity HRK/EUR, wiiw	4.12	3.80	4.07	4.14	4.22	4.25	4.26	.	.

Notes: 1) Preliminary. - 2) From 2000 according to census March 2001. - 3) Enterprises with more than 19 employees. - 4) From 2000 new methodology. - 5) In 1996 enterprises with more than 10 employees, from 1997 more than 19 employees. - 6) From 1998 including persons employed at the Ministry of Defence and Ministry of Internal Affairs. - 7) In 1996 enterprises with more than 10 employees; from 1997 according to NACE classification. - 8) Methodological changes in June 2001 and January 2002 with respect to the stepwise inclusion of extrabudgetary funds. - 9) From 2000 new method of statistical processing. Converted from the national currency to EUR at the official exchange rate.

Source: **wiiw** Database incorporating national statistics; **wiiw** forecasts.

Peter Havlik

Russian Federation: GDP growth weakens, investments disappoint

The Russian economy grew by just slightly over 4% in 2002 – the lowest rate since the August 1998 crisis – as devaluation effects and high world market energy prices have been gradually fading. Neither the already implemented reforms nor greater political stability of Putin's presidency are bearing fruit sufficiently; investors remain extremely cautious. Moreover, the external surplus has been falling as imports rose faster than exports (though growing in volume, in euro terms the latter even fell last year owing to changes in the EUR/USD exchange rate). Investments were disappointingly weak and the main growth stimulus in 2002 came again from the expanding services sector. Annual inflation dropped to 16% (producer prices increased by less than 12%) and the federal budget again recorded a surplus – even after deducting debt service expenditures.

This positive news (which includes some improvements in the living standards as private disposable income grew by almost 9% and unemployment fell) are clouded by the recent reform stalemate and growing structural distortions in the economy. Despite some progress in the former, sound institutional foundations for a sustainable development are still largely missing. The impressive GDP growth during the last four years (almost 6% per year on average) has been just a windfall of the rouble devaluation and high world market energy prices; the larger part of manufacturing industry remains decimated. The main concern is about investments, which picked up temporarily during 1999-2001 but remained nearly flat last year. Apart from the oil sector (and booming housing construction in Moscow) investments actually declined and the drop in machinery and equipment investments is especially worrying. Moreover, FDI inflows have been disappointingly low; net inflows have even declined in 2002, and there is little FDI outside the fuels and metallurgy industries. In sum, the outlook for sustainable growth remains problematic as the country continues to be highly dependent on volatile commodity prices and investors' confidence remains weak. As a result, economic growth is expected to hover around 4%, and it may accelerate only slightly after reforms have gradually borne fruit. Needless to say, this forecast rests on the assumption that no major shift in energy prices will occur. With 50% of export revenues coming from energy carriers, any larger drop in the oil price would substantially alter the GDP and budgetary outlook.

Industry in particular has been losing steam gradually: it grew by just 3.7% last year (after nearly 5% in 2001 and more than 10% in 1999-2000). Agricultural production almost stagnated (despite another good grain harvest). Also construction output was weak, whereas the retail trade turnover (the latter increased by 9% last year) continues to record robust growth. As in the previous two years, the main growth impetus came from the expansion of domestic demand, last year with a clear shift towards more private consumption. The direct contribution of net exports to real GDP growth has become negligible. The trade surplus remains very high – it amounted to more than USD 46 billion in 2002. The current account surplus was USD 32 billion (9% of GDP). According to the Central Bank of Russia (CBR), total external debt decreased slightly in the course of 2002. Within total external indebtedness (USD 150 billion), the share of state debt is declining whereas debts of the banking system and non-financial enterprises are rising. The so-called '2003 debt service problem' is definitely no longer acute. Last but not least, budget revenues are increasing (to about 20% of GDP in 2002) and despite some growth in expenditures the federal budget recorded a primary surplus of 3.5% of GDP in 2002.

Several key pieces of reform legislation were adopted and implemented during 2001, but in 2002 – apart from the adoption of the Land Code, which legalized sales of agricultural land to Russian citizens – not much has happened. After the introduction of a flat income tax of 13% and new corporate taxation rules (since the beginning of 2002 a profit tax of 24% instead of previously 35% is being levied while numerous exemptions were simultaneously abolished), discussion regarding further tax reforms continue. Especially the unified social tax and VAT rates are likely to be modified. Import tariffs have been lowered and streamlined in the course of the preparations for WTO accession. As of 1 April 2002, Russia has been recognized as a market economy by the USA, and the EU followed suit in May. Apart from the political symbolism, the market economy status will make future anti-dumping claims against Russian exports more difficult. Unfortunately, virtually no progress has been achieved so far in the envisaged restructuring and improved transparency of natural monopolies (including UES Electricity System, RAO Gazprom and Railways), nor in the banking system reform.

The state budget plan for 2003 reckons with a smaller surplus (0.6% of GDP, about 2 percentage points less than in 2002). This implies that real budget expenditures will actually stagnate and revenues will fall. Annual inflation is projected at 10% to 12%, the average exchange rate at RUR 33 per USD. Official GDP growth projections range between 3.5% and 4.4% in 2003. On the whole, the official growth projections seem to be realistic, but WIIW does not expect GDP growth to significantly exceed 4% in the coming two years. In view of the forthcoming parliamentary (December 2003) and presidential elections (Spring 2004) no major reform steps can be expected. The re-election of President Putin – and with it some degree of political stability – is almost certain.

Table RU

Russia: Selected economic indicators

	1996	1997	1998	1999	2000	2001	2002 [1)]	2003	2004
								forecast	
Population, th pers., end of period	147502	147105	146693	145925	145185	144321	.	143500	143200
Gross domestic product, RUB bn, nom.	2145.7	2478.6	2741.1	4766.8	7302.2	9040.8	10863.4	12800	14600
annual change in % (real)	-3.4	0.9	-4.9	5.4	9.0	5.0	4.3	4.0	4.0
GDP/capita (USD at exchange rate)	2835	2909	1922	1323	1784	2141	2400	.	.
GDP/capita (USD at PPP - wiiw)	6580	5680	5480	5880	6590	7110	7560	.	.
Gross industrial production									
annual change in % (real)	-4.0	1.9	-5.2	11.0	11.9	4.9	3.7	4	4.5
Gross agricultural production									
annual change in % (real)	-5.1	1.5	-13.2	4.1	7.7	6.8	1.7	.	.
Goods transport, bn t-kms	3370	3256	3147	3315	3480	3592	.	.	.
annual change in %	-4.6	-3.4	-3.3	5.3	5.0	3.2	5.6	.	.
Gross fixed investment, RUB bn, nom.	376.0	408.8	407.1	670.4	1165.2	1599.5	1660.5	.	.
annual change in % (real)	-18.0	-5.0	-12.0	5.3	17.7	8.7	2.6	5	7
Construction output total									
annual change in % (real)	-16.0	-6.0	-5.0	6.0	11.0	9.9	2.7	.	.
Dwellings completed, th units	481.5	430.3	387.7	389.8	373.4	381.6	395.8	.	.
annual change in %	-20.0	-10.6	-9.9	0.5	-4.2	2.2	3.7	.	.
Employment total, th pers., average	65950	64693	63812	63963	64327	64710	66600	.	.
annual change in %	-0.7	-1.9	-1.4	0.2	0.6	0.6	3	.	.
Employment in industry, th pers., average	16366	14905	14162	14297	14543	14692	.	.	.
annual change in %	-4.6	-8.9	-5.0	1.0	1.7	1.0	.	.	.
Reg. unemployed, th pers, end of period	2506.0	1998.7	1929.0	1263.4	1037.0	1122.7	1309.0	.	.
Reg. unemployment rate in %, end of period	3.4	2.7	2.7	1.7	1.4	1.6	1.8	.	.
LFS - unemployment rate in %, average [2)]	9.8	12.0	13.5	13.0	10.5	9.1	7.8	7.5	8
Average gross monthly wages, RUB	790.2	950.2	1051.5	1522.6	2223.4	3240.4	4426.0	.	.
annual change in % (real, gross)	6.4	4.7	-13.3	-22.0	20.9	19.9	16.6	.	.
Retail trade turnover, RUB bn	756.3	883.3	1077.0	1848.2	2416.2	3151.5	3600	.	.
annual change in % (real)	0.4	4.7	-3.5	-6.3	8.8	10.6	9.1	.	.
Consumer prices, % p.a.	47.8	14.8	27.6	85.7	20.8	21.6	16.0	12	10
Producer prices in industry, % p.a.	50.8	15.0	7.1	58.9	46.6	19.1	11.6	15	8
Central government budget, RUB bn									
Revenues	281.9	343.4	325.9	615.5	1132.1	1590.7	2200.0	.	.
Expenditures	356.2	436.6	472.2	666.9	1029.2	1325.7	1970.0	.	.
Deficit (-) / surplus (+)	-74.3	-93.2	-146.3	-51.4	102.9	265.0	230.0	.	.
Deficit (-) / surplus (+), % GDP	-3.5	-3.8	-5.3	-1.1	1.4	2.9	2.1	.	.
Money supply, RUB bn, end of period									
M1, Money	192.4	298.3	342.8	526.8	879.3	1192.6	1337.4 Nov	.	.
M2, Money + quasi money	357.3	457.2	628.6	984.9	1560.0	2122.7	2602.7 Nov	.	.
Refinancing rate of NB % p.a., end of per.	48	28	60	55	25	25	21 Nov	.	.
Current account, USD mn	10847	-80	219	24616	46839	34842	31700	27000	25000
Current account in % of GDP	2.6	0.0	0.1	12.7	18.0	11.2	9.1	7.0	6.0
Gross reserves of NB, incl. gold, USD mn	15324	17784	12223	12456	27972	36622	47792	.	.
Gross external debt, USD mn	125000	130800	145000	158800	161400	151100	149700 Sep	.	.
Exports total, fob, EUR mn [3)]	70731	76623	66467	70820	113672	113448	113172	115000	118000
annual change in %	12.3	8.3	-13.3	6.5	60.5	-0.2	-0.2	2	3
Imports total, fob, EUR mn [3)]	53702	63474	51798	37061	48552	60025	64049	70000	76000
annual change in %	12.2	18.2	-18.4	-28.5	31.0	23.6	6.7	9	9
Average exchange rate RUB/USD	5.12	5.79	9.71	24.62	28.12	29.17	31.35	33	35
Average exchange rate RUB/EUR (ECU)	6.63	6.54	11.06	26.24	26.03	26.13	29.65	35	35
Purchasing power parity RUB/USD, wiiw	2.21	2.96	3.41	5.54	7.61	8.78	9.97	11	.
Purchasing power parity RUB/EUR, wiiw	2.40	3.25	3.73	6.04	8.26	9.53	10.76	.	.

Notes: 1) Preliminary. - 2) Up to 1998 data refer to October. - 3) Based on balance of payments statistics, including estimate of non-registered trade. Converted from USD to EUR using the ECB EUR/USD foreign exchange reference rate.

Source: **wiiw** Database incorporating national statistics; **wiiw** forecasts.

Helen Boss Heslop

Ukraine: boom over, debts due

The Ukrainian economy grew by some 4% in 2002, well below the torrid 9.1% GDP growth achieved in 2001. Domestic demand remained strong, but foreign demand was weak, especially in the first half. Above-average output growth occurred in petroleum products, food processing, wholesale and retail trade, forest products, machine-building, and transport equipment. Agriculture grew by only 1.9%, below expectations, owing to the high base of 2001 and a slowdown in non-grains. The 2000-01 investment boom faltered in 2002: construction fell 5.8% for the year; real interest rates remained high despite further cuts in the refinancing rate. There are no annual investment figures to date, but gross fixed investment as of September had slowed its rise to 6.2% year-on-year, cf. over 20% in 2001. FDI and privatization revenues were disappointing.

Industrial output rose 7% in 2002; within it, manufacturing was up 8.9%, cf. 14.2% and 17.2% respectively in 2001. Though there was a growth slowdown, it was worse in the first half than the second, and industry managed 9.3% growth in the last quarter year-on-year, as Russian oil revenues continued to be high, and the world economy began to come out of the doldrums. Steel and other metals, after contracting during September 2001-May 2002, picked up in the second half, managing 3.9% growth for the year. Output of the steel industry was a quarter above its 1999 level, though still 35% below the late Soviet peak. Judging by January-October data, metals exports rose over 2%, though this was mainly accounted for by raw steel; steel products, which make up nearly 30% of goods exports, saw sales down over a fifth. The machinery sector increased production by 11.3%, led by machine tools and transportation equipment. Basic oil refining continued its strong rebound, with petrol, diesel and heating oil output up 17-34%.

In agriculture, the bumper harvest of 2001 was nearly equalled in 2002, at 38.8 million t of cereals (after processing), of which grains made 22.5 mn t; yields were the best in eight years. Sunflower output soared 45%. However prices reflected the abundance, with e.g. potato prices falling 42%, and the sector has greatly shrunk in the past decade, so the impact on GDP growth was modest. The Land Code that took effect in early 2002 is bearing fruit, however, even if the long-awaited boom in FDI into e.g. organic farming on Ukraine's world-class *chernozem* has yet to occur on any scale, on account of the business climate in general and, in particular, the very slow planned liberalization of limits on agricultural activity by non-traditional users, such as foreigners.

Total goods exports in dollars grew by 8%, but sales to Russia and the rest of the CIS were down, by 8%, reflecting weaker Russian demand for industrial commodities and grains, and Russian trade restrictions. In euro terms, goods exports to all destinations managed only a tepid 3.1% rise. Merchandise imports in dollars rose 6%, in euros, 1%. The trade surplus rose substantially and the current account surplus stood at nearly 6% of GDP at yearend according to the IMF, thanks to a stronger services balance, higher remittances, and e.g. WWII compensation payments from Germany and Austria. More than 40% of merchandise exports consisted of steel and steel products, which count as sensitive in the EU, so that despite its proximity, Ukraine trades relatively little with Europe, in a sort of reverse gravity model. WTO accession, hoped-for by end 2004, may help Ukraine sell more to its richest neighbour.

Inflation turned out much tamer in 2002 than expected, and President Kuchma complained of this in firing the head of the National Bank in November. The CPI actually fell between January and December 2002, in part on account of lower food prices; the PPI rose 5.7% on the same basis (3.1% on annual average). The real exchange rate depreciated slightly, so Ukraine's competitiveness improved, especially vis-à-vis Europe; labour costs remain very low compared to neighbours'. With the euro's winter surge, this effect has strengthened, though trade restrictions and anti-dumping actions will likely dampen the impact. The hryvnia may be allowed to depreciate more than the budget assumption of 5.6 UAH to the USD. Though prices were stable in 2002, wages and money incomes grew nearly 20% in real terms for the second year running, and retail trade turnover rose almost 15%. State debt payments of some USD 1.5 billion weigh on the budget. The fiscal system remains a mess, with a doubling of VAT arrears in 2002, government arrears on VAT refunds, myriad exemptions, and fears that either the proposed tax code, the new customs code, or *ad hoc* profits taxes may push business back into the shadows.

Cumulative FDI as of end September 2002 was reported at USD 4.923 billion, about USD 100 per capita. Owing to the low attractiveness of debt-laden privatization objects, the government's revenues from selloffs came in at a tenth of the budget's original projection of them.

In 2003, and indeed 2004-05, the state will have to scramble to meet principal and interest payments on foreign- and domestic-currency debt. Some USD 1.53 billion worth of foreign-currency state borrowing falls due this year (USD 1.02 billion in principal and USD 510 million in interest); that does not include Ukraine's debt to the IMF. Peak months are March and September, in each of which USD 256 million in principal and interest on eurobonds falls due, hopefully to be more than covered by new euroloans in the works, worth up to USD 700 million. Some USD 500 million worth of domestic borrowing also falls due in 2003. The government has many more reserves than in past years, with over USD 4 billion in NBU coffers by yearend. The current account surplus may narrow but remain adequate. Concerns about raising the foreign exchange to meet the higher debt payments are thus mainly fiscal, as opposed to trade-related.

Ukraine's relations with Europe, the US and NATO have been at least temporarily put in the freezer by the scandals around President Kuchma. Even if Kuchma does not step down early, à la Yeltsin, for instance in favour of newly-appointed Prime Minister Yanukovych, the year 2003 marks the beginning of the 'lame-duck' phase of the long Kuchma presidency. By the time a new president takes office in late 2004, Ukraine will have three new EU-member neighbours.

Table UA

Ukraine: Selected economic indicators

	1996	1997	1998	1999	2000	2001	2002 [1)]	2003	2004
								forecast	
Population, th pers., end of period [2)]	50894.0	50499.9	50105.6	49710.8	49291.2	48415.5	48036.6 Oct	47650	47350
Gross domestic product, UAH mn, nom.	81519	93365	102593	130442	170070	201927	216510	246000	275000
annual change in % (real)	-10.0	-3.0	-1.9	-0.2	5.9	9.1	4.1	4	4
GDP/capita (USD at exchange rate)	872	989	833	633	632	769	842	920	968
GDP/capita (USD at PPP - wiiw)	3330	3630	3630	3710	4050	4580	4890	.	.
Gross industrial production									
annual change in % (real)	-5.2	-0.3	-1.0	4.0	12.4	14.2	7.0	6	7
Gross agricultural production									
annual change in % (real)	-9.5	-1.8	-9.6	-6.9	9.8	10.2	1.9	5	5
Goods transport, bn t-kms	450.3	402.3	391.7	388.0	394.1	393.8	.	.	.
annual change in %	-17.2	-10.7	-2.6	-0.9	1.6	-0.1	3.3	.	.
Gross fixed investment, UAH mn, nom.	12557.0	12437.0	13958.0	17552.0	23629.0	32573.0	19839.0 I-IX	.	.
annual change in % (real)	-22.0	-8.8	6.1	0.4	14.4	20.8	6.2 I-IX	10	15
Construction output total									
annual change in % (real)	-31.0	-9.9	2.7	-8.0	9.1	16.7	-0.7	.	.
Dwellings completed, units	88100	80000	70000	73000	62600	65000	.	.	.
annual change in %	-25.5	-9.2	-12.5	4.3	-14.2	3.8	3.2	.	.
Employment total, th pers., average	23231.8	22597.6	22348.7	21823.7	21268.5	20941.9	20100	20000	.
annual change in %	-2.1	-2.7	-1.1	-2.3	-2.5	-1.5	-4	.	.
Employees in industry, th pers., average [3)]	4642.0	4273.0	4142.0	3932.0	3445.0	3497.5	.	.	.
annual change in %	-7.8	-7.9	-3.1	-5.1	-12.4	1.5	.	.	.
Reg. unemployed, th pers, end of period	351.1	637.1	1003.2	1174.5	1155.2	1008.1	1034.2	.	.
Reg. unemployment rate in %, end of period	1.3	2.3	3.7	4.3	4.2	3.7	3.8	4	4
LFS - unemployment rate in %, average	7.6	8.9	11.3	11.9	11.7	11.1	9.8 I-IX	10	11
Average gross monthly wages, UAH [3)]	126.0	143.0	153.0	177.5	230.1	311.1	376.0	.	.
annual change in % (real, gross)	-4.2	-2.1	-3.2	-5.4	1.1	20.7	21.8	.	.
Retail trade turnover, UAH mn	17344	18933	19317	22151	28757	34417	39192	.	.
annual change in % (real)	-5.1	0.2	-6.6	-7.1	8.1	13.7	14.8	.	.
Consumer prices, % p.a.	80.2	15.9	10.6	22.7	28.2	12.0	0.8	10	7
Producer prices in industry, % p.a.	52.1	7.7	13.2	31.1	20.9	8.6	3.1	0	.
General government budget, UAH mn									
Revenues	30218.7	28112.0	28915.8	32876.4	49117.9	53993.0	54371.2 I-XI	50021 [4)]	.
Expenditures	34182.8	34313.0	31195.7	34820.9	48148.6	55256.6	50542.9 I-XI	52056 [4)]	.
Deficit (-) / surplus (+)	-3964.1	-6201.0	-2279.9	-1944.5	969.3	-1263.6	3828.3 I-XI	-2035 [4)]	.
Deficit (-) / surplus (+), % GDP	-4.9	-6.6	-2.2	-1.5	0.6	-0.6	1.8 I-XI	-0.8 [4)]	.
Money supply, UAH mn, end of period									
M0, Currency outside banks	4041	6132	7158	9583	12799	19465	24064 Nov	.	.
Broad money	9364	12541	15718	22070	32084	45555	59575 Nov	.	.
Refinancing rate of NB % p.a., end of period	39.6	34.8	74.2	45.0	27.0	12.5	7.0	.	.
Current account, USD mn	-1185	-1335	-1296	1658	1481	1402	2300	1000	.
Current account in % of GDP	-2.7	-2.7	-3.1	5.2	4.7	3.7	5.7	2.3	.
Gross reserves of NB excl. gold, USD mn [5)]	1960	2341	761	1046	1353	2955	4400	3700	.
Gross external debt, USD mn	8840	9555	11483	12438	10350	12100	10843	10563	.
Exports total, fob, EUR mn [6)]	11357	12550	11283	10856	15771	18159	18700	19600	21000
annual change in %	13.2	10.5	-10.1	-3.8	45.3	15.1	3	5	7
Imports total, cif, EUR mn [6)]	13883	15103	13103	11104	15104	17612	17800	18500	19600
annual change in %	17.3	8.8	-13.2	-15.3	36.0	16.6	1	4	6
Average exchange rate UAH/USD	1.830	1.862	2.450	4.130	5.440	5.372	5.327	5.6	6.0
Average exchange rate UAH/EUR (ECU)	2.322	2.113	2.768	4.393	5.029	4.814	5.030	6.0	6.3
Purchasing power parity UAH/USD, wiiw	0.480	0.507	0.561	0.705	0.848	0.904	0.917	.	.
Purchasing power parity UAH/EUR, wiiw	0.520	0.557	0.615	0.768	0.921	0.980	0.990	.	.

Notes: 1) Preliminary. - 2) In 2001 according to census 5, Dec 2001. - 3) Excluding small enterprises. - 4) Budget passed by Parliament end December 2002. - 5) Useable. - 6) Exports and imports of goods according to customs statistics, adjusted for oil, gas and non-declarable goods. Converted from USD to EUR using the ECB EUR/USD foreign exchange reference rate.

Source: **wiiw** Database incorporating national statistics; **wiiw** forecasts.

Vladimir Gligorov

Macedonia: stabilization and, hopefully, growth

The key event in 2002 was the successful completion of the parliamentary elections and the formation of the new government. This was the first step necessary on the path of political stabilization, which will in any case be a longer-term process. Still, the overall stability is much improved compared to the pre-election period not to mention the turbulent year 2001 that brought the country on the verge of civil war. There are remaining tensions and even isolated violent acts, but there is no strong political drive on any part of the society to destabilize the state again.

Though the new government took over in mid-autumn last year, it is yet to start energetically to act. The political instability took a high toll on both institutional development and on economic activity. It is therefore all the more important that the government comes up with a strong reform programme and, even more importantly, with the determination to implement it.

In 2002, the economy was still recovering from the shock it had suffered the year before. The one success throughout the political and economic crisis was the preservation of price stability. This was achieved mainly through a tough monetary policy stance. The National Bank decided early on that it would defend the exchange rate peg and thus raised interest rates, at times dramatically, in order to make its determination clear. Once the crisis was put under control, monetary policy was eased as much as the continuing defence of the exchange rate allowed. This policy kept the inflation low, at less than 4% in 2001 and at about 2% in 2002.

The cost in terms of economic activity was, however, large. GDP dropped by over 5% in 2001 and will most probably stagnate in 2002 (it was estimated to have grown by 0.3% in the first six months). Industrial production fell significantly in 2001 and will post another decline of 6% or so in 2002. This has kept the labour survey unemployment rate at more than 30%. Employment was falling throughout 2002 and will continue to fall as the state-owned loss making companies are being restructured. Any change in the labour market can be expected only in the medium term.

With the increased stability, imports have recovered, while exports are still lagging behind. As a consequence, the trade deficit has widened and has reached a record level. The current account deficit is smaller, due to the positive balance in services and due to the constant stream of remittances. Macedonia's exports were growing somewhat until 2001 and have fallen thereafter. Because of the structure of exports, which has not been changing very much for a rather long time, it can be expected that in the next few years exports will recover to reach their previous levels. Further increases in the export performance will depend on the restructuring of industry and on new investments.

Foreign direct investments have not dried out completely, despite the crisis. They can be excepted to grow in the future, with greenfield investments taking over from those connected primarily with privatizations. Still, privatization, particularly of state-owned companies in utilities, can be expected to accelerate. The driving force for privatization is efficiency, which means that both the budget expenditures, on subsidies for instance, and budget revenues, from sales, will benefit. That is so much more important because the fiscal deficit has been large in the last two years. Previously, Macedonia was able to keep its budgets in near balance. The civil strife, of course, had a ruinous effect on the budget. One of the most challenging tasks of the new government will be to cut public expenditures and that will have to be done at a time when the economy is still not growing.

Given the difficult situation in which the economy finds itself, it has the potential to return to growth if political stability is preserved. GDP should grow by 2% in 2003 and even faster in 2004. It will be driven by recovering exports and by an increase in investments together with rising private consumption, which should be supported by an increase in bank lending to households. The latter in turn will be supported by the continuing easing of the monetary policy. Though exchange rate stability is extremely important, the government may rethink its whole economic policy stance especially in view of the need to rebalance the budget. Macedonia is a small economy and it is hard to see sustainable and fast growth there unless it is led by rising exports.

Table MK

Macedonia: Selected economic indicators

	1996	1997	1998	1999	2000	2001	2002 [1]	2003	2004
								forecast	
Population, th pers., mid-year	1983.1	1996.9	2007.5	2017.1	2026.4	2036.0	.	.	.
Gross domestic product, MKD mn, nom.	176444	186018	194979	209010	236389	233090	236600	246200	263700
annual change in % (real)	1.2	1.4	3.4	4.3	4.5	-4.6	0	2	3
GDP/capita (USD at exchange rate)	2225	1869	1784	1821	1771	1683	1780	.	.
GDP/capita (USD at PPP - wiiw)	4170	5660	5900	6210	6600	6410	6490	.	.
Gross industrial production									
annual change in % (real) [2]	3.2	1.6	4.5	-2.6	3.5	-3.1	-6.5	-3	3
Gross agricultural production									
annual change in % (real)	-2.2	1.1	4.3	1.0	1.0	-13.3	.	.	.
Goods transport, mn t-kms [3]	1067	1175	1302	1219	1303	2773	.	.	.
annual change in % [3]	-20.6	10.1	10.8	-6.4	6.9	112.8	.	.	.
Gross fixed capital form., MKD mn, nom.	30654	32236	33982	34710	38332	.	.	.	.
annual change in % (real)	6.5	-4.3	-2.6	-1.4	-3.2	.	.	.	.
Construction output, value added									
annual change in % (real)	-0.6	0.2	7.7	10.4	-1.1	-3.9	.	.	.
Dwellings completed, units	5342	4300	3253	4479	5316	.	.	.	.
annual change in %	15.1	-19.5	-24.3	37.7	18.7	.	.	.	.
Employment total, th pers., average [4]	537.6	512.3	539.8	545.2	549.8	599.3	.	.	.
annual change in % [4]	.	-4.7	5.4	1.0	0.8	9.0	.	.	.
Employees in industry, th pers., average [2]	127.6	117.6	113.6	119.8	114.4	122.5	112.0 I-X	.	.
annual change in % [2]	-6.6	-7.9	-3.4	5.5	-4.5	-4.8	-8.5 I-X	.	.
LFS - unemployed persons, average	251.5	288.2	284.1	261.5	261.7	263.2	260	.	.
LFS - unemployment rate in %, average	31.9	36.0	34.5	32.4	32.2	30.5	31.9 Apr	30	30
Average net monthly wages, MKD	8817	9063	9394	9664	10193	10552	11257 I-XI	.	.
annual change in % (real, net)	0.5	0.2	3.8	3.6	-0.3	-1.9	4.7 I-XI	.	.
Retail trade turnover, MKD mn [4]	29893.0	32482.8	33215.6	38247.9	50208.6	45975.8	40535.2 I-X	.	.
annual change in % (real, calc.)	-8.4	4.1	1.5	16.4	18.7	-13.0	5.9 I-X	.	.
Retail prices, % p.a.	3.0	4.4	0.8	-1.1	10.6	5.2	1.5	2	4
Producer prices in industry, % p.a.	-0.3	4.2	4.0	-0.1	10.7	2.0	1.1	2	4
Central government budget, MKD mn									
Revenues	42722	41398	42655	50478	63097	63109	61455 I-XI	.	.
Expenditures	.	41393	42623	49761	57689	68885	63055 I-XI	.	.
Deficit (-) / surplus (+)	.	4	32	717	5408	-5776	-1600 I-XI	.	.
Deficit (-) / surplus (+), % GDP	.	0.0	0.0	0.3	2.3	-2.5	.	.	.
Money supply, MKD mn, end of period									
M1, Money	12143	13983	15178	19694	22388	25324	25792 Nov	.	.
M2, Money + quasi money	18490	22724	26003	33720	41957	69785	62900 Nov	.	.
Discount rate, % p.a., end of period	9.2	8.9	8.9	8.9	7.9	10.7	10.7 Sep	.	.
Current account, USD mn [5]	-339.9	-286.1	-269.3	-32.5	-75.3	-235.4	-250	-250	-250
Current account in % of GDP	-7.7	-7.7	-7.5	-0.9	-2.1	-6.9	-6.9	-5.9	-5.7
Gross reserves of NB, excl. gold, USD mn	239.5	257.0	306.1	429.9	429.4	745.2	.	.	.
Gross external debt, USD mn [6]	1172.4	1131.1	1398.6	1438.5	1437.7	1418.6	1749.8 Nov	.	.
Exports total, fob, EUR mn [7]	904.9	1090.6	1170.2	1116.7	1431.4	1289.6	1200	1300	1300
annual change in %	-1.7	20.5	7.3	-4.6	28.2	-9.9	-7	8	0
Imports total, cif, EUR mn [7]	1283.1	1568.3	1709.5	1664.9	2266.1	1884.1	2000	2100	2200
annual change in %	-2.4	22.2	9.0	-2.6	36.1	-16.9	6	5	5
Average exchange rate MKD/USD	39.99	49.83	54.45	56.90	65.89	68.04	65	58	60
Average exchange rate MKD/EUR (ECU)	50.08	56.20	61.07	60.62	60.73	60.91	61	61	61
Purchasing power parity MKD/USD, wiiw	21.35	16.45	16.48	16.70	17.67	17.87	17.87	.	.
Purchasing power parity MKD/EUR, wiiw	23.14	18.04	18.05	18.19	19.17	19.39	19.29	.	.

Notes: 1) Preliminary. - 2) From 2001 according to NACE. - 3) Road and rail. - 4) From 2000 according to NACE. - 5) Including grants. - 6) Medium- and long-term. - 7) Converted from USD to EUR using the ECB EUR/USD foreign exchange reference rate.

Source: **wiiw** Database incorporating national statistics; **wiiw** forecasts.

Vladimir Gligorov

Yugoslavia becomes Serbia and Montenegro

After one year of negotiations a new Constitutional Charter has been adopted by the parliaments of Serbia and Montenegro and by the federal parliament of Yugoslavia. The Charter dismantles the Federation and establishes the Union of Serbia and Montenegro. The Union will have a parliament and a president, who will also preside over the cabinet with five ministers, for foreign policy, defence, foreign economic relations, internal economic relations and for human and minority rights. There is no finance ministry because the Union will not have its own budget nor will it have any assets. The National Bank of Yugoslavia will become the National Bank of Serbia. Montenegro has its own central bank and uses the euro as its legal tender.

Serbia and Montenegro will practically become independent states. Only in external representation and relations will they have joint sovereignty. This incoherence between the internal and external sovereignty has already caused the emergence of problems. Thus, in order to negotiate an association agreement with the European Union and to accede to the World Trade Organization, Serbia and Montenegro need to harmonize their trade regimes and policies. This may prove to be difficult and time consuming. In general, the efficiency of the functioning of the Union will depend on the ability of the governments of Serbia and Montenegro to work together.

The new Union devolves the responsibility for economic and every other policy to the member states. They will now have to concentrate on the necessary reforms of institutions and policies. This will be even more urgent because the economic developments have not been all that favourable. For most of the year 2002, the economies of both Serbia and Montenegro have been in recession with industrial production falling in the first half and recovering somewhat in the second half. In the end, a growth of less than 2% has been registered for the year as a whole. Preliminary data indicate GDP growth of around 4% in Serbia and somewhat less for Montenegro. As agriculture has posted a decline of about 3% and construction is also declining, the growth of GDP has to be attributed to the services sector. That growth has been driven mainly by consumption, in which the rise of wages has played the major role in Serbia. A significant part of it comes from the budget, which is being supported by foreign grants and soft loans. In addition, banks are increasingly lending to households, who also hold most of the foreign currency deposits in the banks.

The sluggish supply response to the sharply rising consumption is balanced by the fast growth of imports – and thus of the trade deficit. There are some doubts about the quality of the foreign trade data, but the notably widening trade deficit is unmistakable. Exports have been growing too, at least in Serbia. In Montenegro, income from tourism has increased by about on third (ten months 2002 on ten months 2001). The current account deficit has been much smaller, because both countries cannot borrow very much, so the trade deficit has to be financed from remittances and other transfers and from foreign investments. Assuming that remittances will not grow very much in the next years and assuming that grants and other transfers will also stabilize and possibly decline, further growth of imports will depend mostly on foreign investments. However, they will be increasingly competing with the debt service, which will rise slowly in the next two to three years and then quite sharply once the grace period for the repayment of the principal is over. Thus, the growth of imports will have to be much more moderate.

Both states hope to increase the amount of foreign direct investments significantly in the next couple of years. Montenegro has been able to sell the gasoline distributor in 2002 and that sale has probably saved the budget, which is chronically running large deficits. Serbia hopes to sell companies in the oil and gasoline industries and in the tobacco industry, and it plans to sell the mobile telephone provider. With numerous sales of medium- and small-size companies, Serbia expects to cash in about one billion dollars of foreign direct investments in 2003. Similar or larger inflows are expected for the following few years. These financial inflows should help preserve macroeconomic stability.

Inflation has been falling in Serbia and Montenegro throughout 2002 – for different reasons, however. In Serbia, this was the consequence of the increase in imports and of weak demand for domestic goods. Still, because of adjustments in administered prices and of the prices of services, inflation was around 20%, year on year. In Montenegro inflation was slightly lower, somewhat above 15%, year on year. Further deceleration of inflation is expected this year and the next. This is presumed on growth accelerating and on wage increases moderating.

In Serbia, inflationary expectations depend on the stability of the exchange rate. In the last two years, the dinar has been pegged to the euro. Some nominal depreciation has occurred, mainly as a by-product of the euro conversion (basically, the German mark was exchanged for 30 dinars before the conversion while the euro was exchanged for 60 dinars after the conversion, i.e., two German marks for one euro, which is a few percentages more than the true conversion rate). By contrast, strong real appreciation has occurred; certainly in excess of 50%. This has supported imports, but has increasingly raised questions about the competitiveness of Serbian exports. With the exchange rate all but fixed and with wages rising, competitiveness has been eroding fast. This has led to the growing expectation that the exchange rate will start to depreciate.

Growth projections for 2003 and 2004 are not very ambitious. The accent is rather going to be on privatization and restructuring, at least officially. That of course implies further growth of unemployment, which is already much too high. However, there will be elections in both years in Serbia, where the government is not very popular. In Montenegro there is no pressure from elections, but the government does have to be sensitive to its popularity if it wants to push reforms and to also gain support for the vote for independence as it still plans to hold a referendum on that issue in the next couple of years.

In conclusion, the new union of Serbia and Montenegro leaves the impression of a temporary constitutional arrangement that will be tested and adjusted continuously. Reforms may suffer as a consequence, but they will also have to face squarely the growing dissatisfaction with their speed and performance.

Table YU

Serbia & Montenegro: Selected economic indicators *)

	1996	1997	1998	1999	2000	2001	2002 [1)]	2003 forecast	2004 forecast
Population, th pers., mid-year	10577.2	10600.1	10616.9	8372.7	8342.5	8325.7	8338.4	.	.
Gross domestic product, USD mn, nom. [2)]	16477	18146	18212	10376	8100	10500	13200	16900	19300
annual change in % (real) [3)]	5.9	7.4	2.5	-17.7	6.4	5.1	3	4	4
GDP/capita (USD at exchange rate) [2)]	1558	1712	1715	976	970	1260	1580	.	.
Gross industrial production [4)]									
annual change in % (real)	7.6	9.5	3.6	-23.1	11.2	0.0	1.7	3	5
Gross agricultural production									
annual change in % (real)	1.5	7.3	-3.2	-1.0	-12.9	17.2	-2.1	.	.
Goods transport, mn t-kms	28957	38164	45601	30026	32865	17456	5371	.	.
annual change in %	.	31.8	19.5	.	9.5	-46.9	-69.2	.	.
Gross fixed investment, YUM mn, nom.	9702.5	13525.3	17893.2	24867.8	59315.5	.	.	.	.
annual change in % (real)	-5.7	0.8	-2.2	-26.3	13.3	.	.	.	.
Construction output, value of work done									
annual change in % (real)	2.7	6.9	-0.8	.	.	.	.	.	.
Dwellings completed, units	15160	14768	13096	13123	12732	12156	12776	.	.
annual change in %	5.7	-2.6	-11.3	0.2	-3.0	-4.5	5.1	.	.
Employment total, th pers., average [5)]	2367	2332	2504	2298	2238	2241	2201	.	.
annual change in %	-0.5	-1.5	-0.1	.	-2.6	0.1	-1.8	.	.
Employees in industry, th pers., average [6)]	894.4	864.1	884.4	804.5	764.7	739.0	684.0	.	.
annual change in % [6)]	-1.7	-3.4	2.4	.	-5.0	-3.4	-7.4	.	.
Reg. unemployed, th pers, end of period	826.8	793.8	849.4	774.3	812.4	860.5	988.7	.	.
Reg. unemployment rate in %, end of period [7)]	26.1	25.5	25.4	25.5	26.7	27.9	31.2	30	30
LFS - unemployment rate in %, average	13.2	13.8	13.7	13.7	12.6	12.9	13.0	15	15
Average net monthly wages, YUM	658	803	1063	1309	2588	5545	9113	.	.
annual change in % (real, net)	1.0	21.2	2.0	-15.0	6.5	13.3	24.6	.	.
Retail trade turnover, YUM mn	27896	35433	48748	57697	119522	250312	322902	.	.
annual change in % (real, calc.)	7.4	11.8	3.9	-13.5	11.6	10.2	8.2	.	.
Consumer prices, % p.a.	91.5	21.6	29.9	44.9	85.6	89.0	16.5	15	10
Producer prices in industry, % p.a.	90.2	19.5	25.5	43.4	106.9	85.1	8.7	10	10
General government budget, YUM mn									
Revenues	35941	47455	61360	79321	138749	320475	507008	.	.
Expenditures	39044	55315	70739	.	.	.	.	.	.
Deficit (-) / surplus (+)	-3103	-7860	-9379	.	.	.	.	.	.
Deficit (-) / surplus (+), % GDP	.	-7.0	-6.1	.	.	.	.	.	.
Money supply, YUM mn, end of period	.								
M1, Money	5495.3	9148.0	10807.3	16332.0	26954.0	52686.0	94573.0	.	.
Broad money [8)]	31434.7	38948.4	62352.0	75393.7	65522.0	107825.0	190284.0	.	.
Discount rate, % p.a., end of period	68.2	33.7	33.7	26.3	26.3	16.4	9.5	.	.
Current account, USD mn [9)]	-1317	-1837	-1180	-1341	-339	-624	-2000	-2000	-2000
Current account in % of GDP	-8.0	-10.1	-6.5	-12.9	-4.2	-5.9	-15.2	-11.8	-10.4
Forex reserves of NBY, USD mn	300	300	300	297	524	1169	2280	.	.
Gross external debt, USD mn	9000	10500	11500	12500	11418	11740	11472 Sep	.	.
Exports total, fob, EUR mn [10)]	1592.8	2360.0	2517.7	1391.1	1808.2	2095.1	2273.7	2480	2630
annual growth rate in %	.	48.2	6.7	-44.0	30.0	15.9	8.5	9	6
Imports total, cif, EUR mn [10)]	3250.6	4245.2	4283.5	3080.8	3892.1	5385.7	6002.9	6120	6240
annual growth rate in %	.	30.6	0.9	-26.4	26.3	38.4	11.5	2	2
Average exchange rate YUM/USD	4.97	5.72	9.34	11.01	16.69	66.84	64.19	60	60
Average exchange rate YUM/EUR (ECU)	6.30	6.48	10.46	11.74	15.30	59.50	60.73	65	65

*) *Note*: From 1999 (GDP from 2000) excluding Kosovo and Metohia.

Notes: 1) Preliminary. - 2) Estimates based on World Bank method. From 1999 based on market exchange rate. - 3) Based on GMP in Dinar. - 4) Excluding private enterprises. - 5) Employees plus own account workers, excluding individual farmers; from 1998 including small enterprises. - 6) From 1998 including small enterprises. - 7) In % of unemployed plus employment. - 8) From 2000: at official exchange rate, excluding Montenegro, government deposits, household frozen foreign currency saving deposits. - 9) From 2000 including official grants. - 10) Converted from the national currency to EUR at the official exchange rate.

Source: **wiiw** Database incorporating national statistics; **wiiw** forecasts.

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