REGIONAL ECONOMIC PROSPECTS

European Bank for Reconstruction and Development

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Regional Economic Prospects in the EBRD Regions

European Bank
for Reconstruction and Development

Along the adjustment path

September 2024

After slowing from 3.4 per cent in 2022 to 2.6 per cent in 2023, average growth in the EBRD regions is estimated to have picked up to 2.9 per cent year on year in the first half of 2024 as energy prices moderated and economic activity in Emerging Europe adjusted to lower gas imports from Russia.

Growth in the EBRD regions is expected at 2.8 per cent in 2024, picking up to 3.5 per cent in 2025. This represents downward revisions relative to the May 2024 forecast (of 0.2 of a percentage point (pp) in 2024 and 0.1 pp in 2025) reflecting a weaker outlook for advanced Europe, stagnating mining output in Kazakhstan and Uzbekistan, the ongoing conflict in Gaza and Lebanon and severe droughts in Morocco and Tunisia.

Gas prices in Europe have stabilised around their 2017-21 averages, though are still almost five times the US price and some economies in the EBRD regions pay significantly higher average import prices for gas than Germany. As pipeline gas imports from Russia declined, pipeline gas imports from Norway and LNG imports from the United States and Norway increased through new and expanded terminals. Oil prices have also been relatively stable at around their 2017-21 averages. While here too, the composition of imports shifted away from Russia, a number of economies in Emerging Europe remain dependent on imports of gas and oil from Russia.

Disinflation proceeded largely as expected. Average inflation in the EBRD regions declined from 17.5 per cent at its peak in October 2022 to 5.8 per cent in July 2024 but remained 1.6 percentage points above the pre-pandemic average. This pattern is broadly similar to the one observed in advanced economies.

As inflation declined, real wages resumed growth after several quarters of declines, boosting household consumption. At the low point at the end of 2022, real wages in the EBRD regions were, on average, more than 10 per cent below their pre-Covid trend. After several months of rapid catch-up in 2024, they remain perhaps 3 per cent or so below the levels that could be expected if pre-Covid trends continued. The remaining catch-up potential thus appears to be limited and real wage growth can be expected to moderate going forward.

For a while, governments (as well as firms) benefited from higher inflation, which helped to reduce the effective burden of servicing previously issued debt. As a result, increases in corporate bankruptcies to date have been modest. Going forward, the effective burden of interest payments for corporates and governments may increase even as central banks reduce policy interest rates. Fiscal deficits in the EBRD regions, on average, remain above the pre-Covid levels and interest payments and debt levels as a share of GDP are significant in Greece, Hungary, Egypt, Jordan, Lebanon, Tunisia and Ukraine.

In a typical non-EU economy in the EBRD regions the spread on medium-term government debt versus Germany has started increasing again, to around 4.5 pp while in a typical EU economy in the EBRD regions the spread that opened in March 2022 has been maintained at around 1 pp.

In ***central Europe and the Baltic states*** *growth is expected to accelerate from 0.2 per cent in 2023 and 2 per cent year on year in the first half of 2024 to 2.3 per cent in 2024 and 3.2 per cent in 2025. The recovery in the region is uneven, with both upward and downward revisions since the May 2024 forecast, reflecting a combination of weak external demand from advanced Europe and fiscal pressures amidst continued resilience in labour markets.*

Growth in the ***south-eastern EU*** *is expected at 1.9 per cent in 2024, broadly in line with the outcomes in 2023 and the first half of 2024, picking up to 2.6 per cent in 2025. Forecasts for both years have been revised down relative to the May 2024 forecasts on weak industrial production and, in the case of Romania, lower demand for outsourcing weighing on the IT sector.*

Growth in the ***Western Balkans*** *picked up from 2.5 per cent in 2023 to an estimated 3.7 per cent in the first half of 2024. It is expected at 3.4 per cent in 2024 and 3.7 per cent in 2025. The 2024 growth forecasts have been revised up in Albania on a strong tourism season, in Serbia reflecting strong investment and an accommodative fiscal and monetary stance and in Montenegro on sustained consumption growth.*

Growth in ***Central Asia*** *is moderated from 5.7 per cent in 2023 to 4.7 per cent year on year in the first half of 2024 as mining output in Kazakhstan and Uzbekistan stagnated. It is expected to average 5.1 per cent in 2024 picking up to 5.9 per cent in 2025.*

In ***eastern Europe and the Caucasus****, growth picked up from 4.4 per cent in 2023 to an estimated 6 per cent year on year in the first half of 2024. It is expected to moderate to 3.7 per cent in 2024 as a whole before picking up to 4.1 per cent in 2025. The growth forecast for* ***Ukraine*** *is unchanged for 2024 but revised down for 2025 as the destruction of electricity infrastructure caused by Russia's war on Ukraine is expected to continue weighing on production.*

In ***Türkiye****, growth moderated from 5.1 per cent in 2023 to 3.8 per cent year on year in the first half of 2024. It is expected to moderate further to 2.7 per cent in 2024 and 3 per cent in 2025 (both unchanged relative to the May 2024 forecasts) reflecting the impact of tighter monetary policy. Real wages have been increasing rapidly. As inflation outran lira depreciation, the real effective exchange rate strengthened recently.*

Growth in the ***southern and eastern Mediterranean*** *moderated from 2.7 per cent in 2023 to an estimated 2.1 per cent year on year in the first half of 2024. It is expected to pick up to 2.8 per cent in 2024 as a whole and 3.9 per cent in 2025. This represents a downward revision on the previous forecast for 2024 owing to disruptions in the energy sector in Egypt, a slower-than-expected recovery in private and public investment, severe droughts in Morocco and Tunisia and the impact of the conflict in Gaza and Lebanon on Jordan and Lebanon.*

In ***Russia****, growth accelerated from 3.6 per cent in 2023 to 4.7 per cent year on year in the first half of 2024, with strong activity in the manufacturing sector, as the price of Russia's oil exports is estimated to have increased by more than 10 per cent year on year; trade with non-sanctioning economies has been strong and military spending has been high in the context of the ongoing full-scale invasion of Ukraine. Growth is expected to slow to 3.6 per cent in 2024 as a whole and 1.5 per cent in 2025 in line with the medium-term potential reflecting labour constraints.*

Table 1. GDP growth in real terms

	Actual			Forecast (Sep'24)		Revision since May'24	
	2022	**2023**	**2024H1**	**2024**	**2025**	**2024**	**2025**
EBRD Regions	**3.4**	**2.6**	**2.9**	**2.8**	**3.5**	**-0.2**	**-0.1**
Central Asia	**4.6**	**5.7**	**4.7**	**5.1**	**5.9**	**-0.3**	**0.0**
Kazakhstan	3.2	5.1	3.2	4.0	5.5	-0.5	0.0
Kyrgyz Republic	9.0	6.2	8.7	9.0	7.0	0.5	0.0
Mongolia	5.0	7.2	5.6	5.0	8.0	0.0	0.0
Tajikistan	8.0	8.3	8.2	8.0	7.0	0.5	0.0
Turkmenistan	6.2	6.3	6.3	6.3	6.3	0.0	0.0
Uzbekistan	6.0	6.3	6.4	6.0	6.0	-0.5	0.0
Central Europe and the Baltic states	**4.3**	**0.2**	**2.0**	**2.3**	**3.2**	**0.1**	**0.1**
Croatia	7.0	3.1	3.6	3.6	3.0	0.7	0.2
Czechia	2.8	-0.1	0.4	1.1	2.4	0.2	-0.1
Estonia	0.1	-3.0	-1.6	-0.8	2.5	-1.6	-1.0
Hungary	4.6	-0.9	1.3	1.8	3.3	-0.4	-0.2
Latvia	3.0	-0.3	0.3	0.9	2.4	-0.9	-0.2
Lithuania	2.4	-0.3	2.4	2.3	2.5	0.8	0.2
Poland	5.6	0.2	2.9	3.2	3.8	0.3	0.3
Slovak Republic	1.9	1.6	2.3	2.3	2.6	0.5	-0.1
Slovenia	2.5	2.1	1.4	1.5	2.6	-0.8	0.0
Eastern Europe and the Caucasus	**-12.8**	**4.4**	**6.0**	**3.7**	**4.1**	**0.2**	**-0.8**
Armenia	12.6	8.3	6.5	6.2	4.8	0.0	0.0
Azerbaijan	4.7	1.1	4.3	3.8	2.7	0.7	0.0
Georgia	11.0	7.5	9.1	6.5	4.6	1.3	0.0
Moldova	-4.6	0.7	2.2	3.2	3.5	-0.3	-0.2
Ukraine	-28.8	5.3	6.5 e	3.0	4.7	0.0	-1.3
South Eastern EU	**4.6**	**2.0**	**1.7**	**1.9**	**2.6**	**-0.9**	**-0.5**
Bulgaria	3.9	1.8	2.1	2.2	2.9	-0.4	-0.1
Greece	5.6	2.0	2.1	2.4	2.6	0.1	0.0
Romania	4.1	2.1	1.3	1.4	2.6	-1.8	-0.8
Southern and Eastern Mediterranean	**3.4**	**2.7**	**2.1**	**2.8**	**3.9**	**-0.6**	**0.0**
Egypt	4.2	2.9	2.2 e	3.2	4.5	-0.7	0.1
Jordan	2.6	2.7	2.0 e	2.2	2.6	-0.2	0.0
Lebanon	0.0	-0.2	-1.0 e	-1.0	2.0	-1.2	-1.0
Morocco	1.5	3.4	2.7	2.9	3.6	-0.1	0.0
Tunisia	2.7	0.0	0.6	1.2	1.8	-0.7	-0.2
Turkiye	**5.5**	**5.1**	**3.8**	**2.7**	**3.0**	**0.0**	**0.0**
Western Balkans	**3.4**	**2.5**	**3.7**	**3.4**	**3.7**	**0.1**	**0.0**
Albania	5.0	3.4	3.6 e	3.5	3.7	0.2	0.2
Bosnia and Herzegovina	4.1	1.7	2.7 e	2.8	3.0	0.0	0.0
Kosovo	4.3	3.3	5.6 e	4.0	4.0	0.0	0.0
Montenegro	6.4	6.0	4.4 e	3.8	2.9	0.3	0.0
North Macedonia	2.2	1.0	1.2 e	2.2	3.5	-0.3	0.0
Serbia	2.5	2.5	4.3	3.8	4.0	0.3	0.0
Memo: Egypt (fiscal year to June)	6.7	3.8	2.9	2.7	4.0	-0.3	0.0
EEC excl. Ukraine	6.6	3.4	5.3	4.6	3.5	0.6	0.0
Belarus	-4.7	3.9	5.0	4.2	2.5	1.4	0.3
Russia	-1.2	3.6	4.7	3.6	1.5	1.1	0.0

Source: National authorities and EBRD. Note: Weights are based on the values of gross domestic product in 2022 at market exchange rates. Where H1 is not yet available 'e' refers to Q1 numbers (and the 2024 forecast for Lebanon).

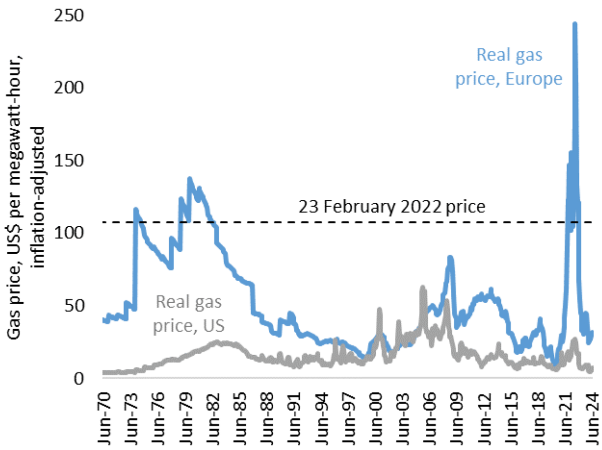
Growth in the EBRD regions picked up to an estimated 2.9 per cent year on year in the first half of 2024

Growth in the EBRD regions slowed from 3.4 per cent in 2022 to 2.6 per cent in 2023 as the war on Ukraine took its toll, energy prices in Europe remained relatively high and the post-Covid recovery in the services sector ran out of steam (see Table 1). As economies in Emerging Europe adjusted to lower gas imports from Russia following Russia's full-scale invasion of Ukraine, growth in the EBRD regions picked up to an estimated 2.9 per cent year on year in the first half of 2024.

Oil and gas prices around their 2017-21 levels

The price of gas in Europe increased sharply in late 2022. It has eased since, and as of early September 2024 was back to around its 2017-21 average (see Chart 1). At the same time, gas in Europe remains relatively expensive, trading at almost five times the US price.

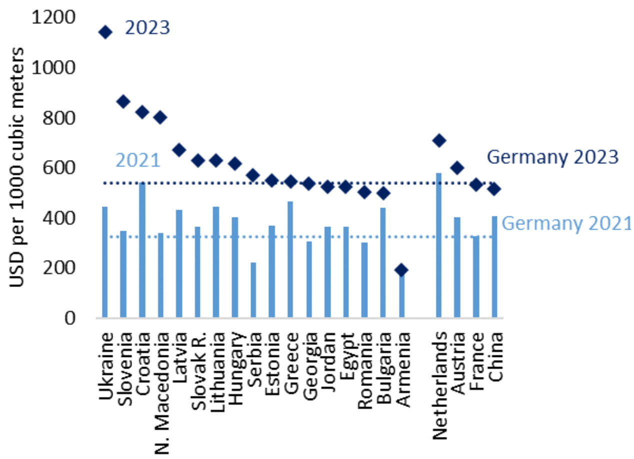
Chart 1. Gas prices in Europe are around their 2017-21 averages, but almost five times the US price



Source: Bloomberg, CEIC, IMF and authors' calculations.
Note: Prices adjusted for US inflation.

However, there is significant variation in the prices economies in the EBRD regions pay for imported gas. 'Effective' import prices can be calculated based on import statistics, as reported by UN Comtrade. These calculations suggest that while most average import price values align around the prevailing European import price levels, some economies, such as Ukraine, Slovenia, Croatia and North Macedonia appear to pay higher average import prices than Germany (see Chart 2). In contrast, Armenia benefits from a long-term gas contract with a lower price.

Chart 2. Some economies in the EBRD regions pay higher average import prices for gas than Germany

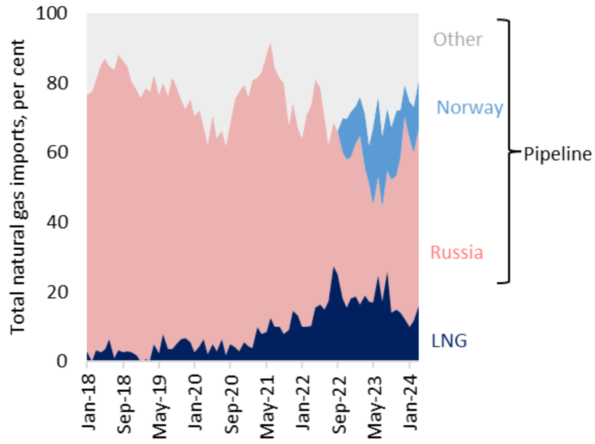


Source: UN Comtrade and authors' calculations.
Note: Implied price per 1000 cubic meters based on Comtrade reporting of trade values and quantities in kilograms. HS 271111 and 271121 used. Import prices can deviate substantially from overall prices in economies with significant domestic markets, such as the United States or Canada.

The composition of gas imports has shifted significantly since 2021. As pipeline gas imports from Russia declined, pipeline gas imports from Norway and liquified natural gas (LNG) imports from the United States and Norway increased (see Chart 3). As documented in earlier *Regional Economic Prospects*, there was also substantial adjustment through lower gas consumption.[1]

[1] See also Plekhanov and Sassoon (2023).

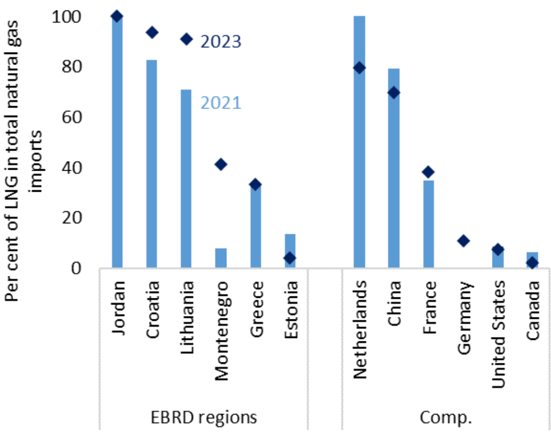
Chart 3. As pipeline gas imports from Russia declined, pipeline gas imports from Norway and LNG imports increased in central Europe, the Baltic states and the Western Balkans



Source: UN Comtrade and authors' calculations. Note: Implied price per 1000 cubic meters based on Comtrade reporting of trade values and quantities in kilograms. The sample includes Bosnia and Herzegovina, Bulgaria, Croatia, Czechia, Estonia, Hungary, Latvia, Lithuania, North Macedonia, Romania, Serbia, the Slovak Republic and Slovenia. HS 271111 used for LNG and 271121 for pipeline.

LNG imports increased through new and expanded terminals in Croatia, Greece, Jordan and Lithuania (see Chart 4). The share of LNG in natural gas imports of the EU economies in the EBRD regions and Western Balkans economies increased from around 4 per cent in 2019 to 18 per cent in 2023.

Chart 4. LNG imports increased

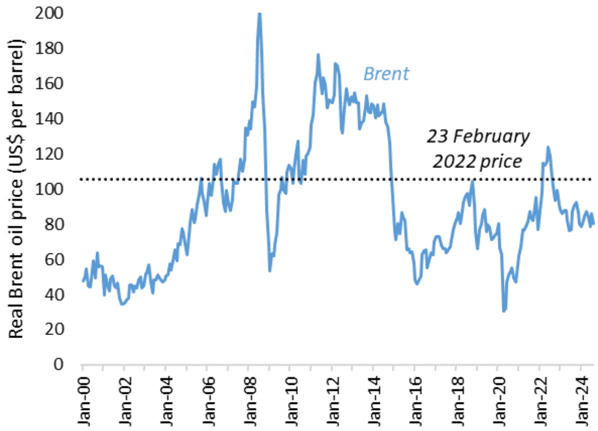


Source: UN Comtrade and authors' calculations.

Note: Implied price per 1000 cubic meters based on Comtrade reporting of trade values and quantities in kilograms. HS 271111 used for LNG and 271121 for pipeline. Economies with the highest shares in the EBRD regions shown.

Oil prices moderated on subdued economic activity and have also been relatively stable around their 2017-21 averages (adjusted for US inflation; see Chart 5).

Chart 5. Oil prices have been relatively stable at around their 2017-21 averages

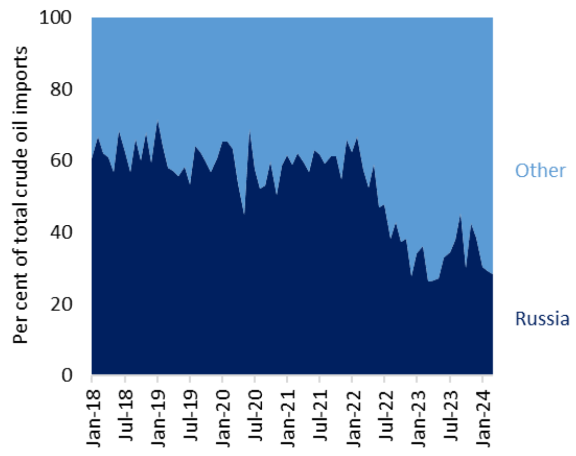


Source: Bloomberg, CEIC and authors' calculations. Note: Prices adjusted for US inflation.

Here too, the composition of imports shifted. On average, the EU economies in the EBRD regions and Western Balkans economies reduced Russia's share of oil from around 60 per cent to around 30 per cent (see Chart 6).

Reliance on oil imports from Russia remains particularly high in the Slovak Republic, Bulgaria and Hungary, where imports from Russia account for over 60 per cent of total crude oil imports (based on UN Comtrade, the analysis covers economies that reported at least US$ 10 million of crude oil in 2023 and does not cover refined oil products).

Chart 6. Dependence on oil imports from Russia has halved in central Europe, the Baltic states and Western Balkans

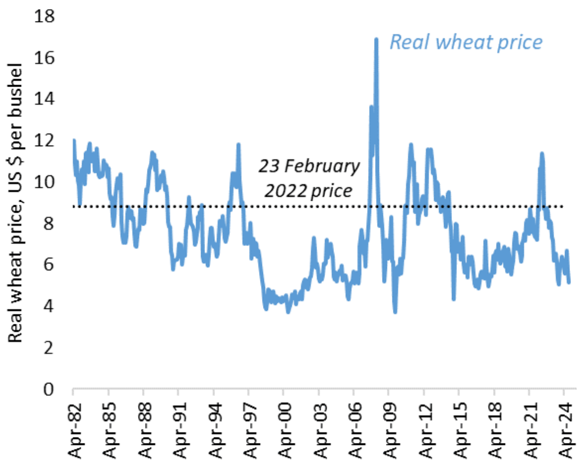


Source: UN Comtrade and authors' calculations.
Note: Implied price per 1000 cubic meters based on Comtrade reporting of trade values and quantities in kilograms. The sample includes Bosnia and Herzegovina, Bulgaria, Croatia, Czechia, Estonia, Hungary, Latvia, Lithuania, North Macedonia, Romania, Serbia, the Slovak Republic and Slovenia. HS 270900 used for crude oil.

Prices in global food markets normalised

Wheat prices have fallen to levels that are low by historical standards (adjusted for inflation), reflecting strong harvests (see Chart 7).

Chart 7. Wheat prices declined to levels that are low by historical standards

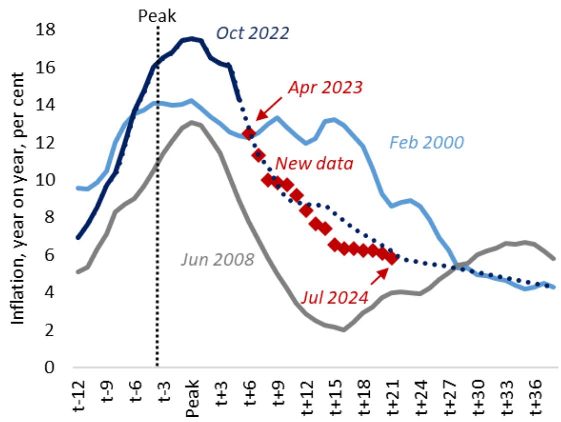


Source: Refinitiv and authors' calculations.
Note: Prices adjusted for US inflation.

Disinflation proceeded as expected

Average inflation is broadly in line with the levels expected as of early 2023 (see Chart 8).

Chart 8. Average inflation is in line with expectations as of early 2023

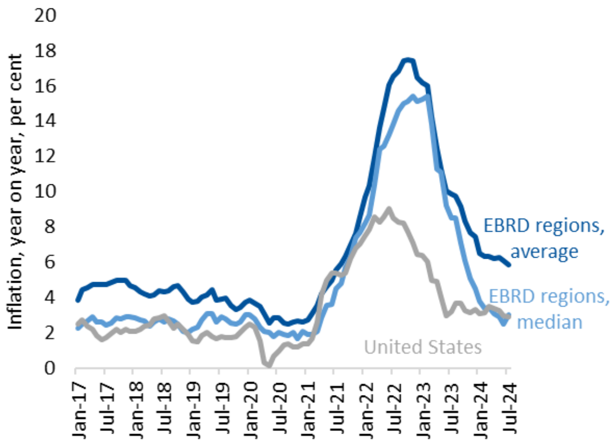


Source: May 2023 Regional Economic Prospects based on IMF, national authorities via CEIC, World Bank Global Inflation database and authors' calculations.
Note: Simple average across 29 economies in the EBRD regions for Feb 2000, 32 for June 2008, 33 for Oct 2022 (excluding Ukraine 2024 onwards). Dashed line denotes a month-to-month curve fitted based on end of-year and annual average April 2023 IMF inflation forecasts. Curves corresponding to previous disinflation episodes are superimposed in a way that peak inflation (Feb 2020 and June 2008) coincides with the recent inflation peak observed in Oct 2022. For example, Nov 2022 corresponds to July 2008 for the 2008 episode, and so on. Diamonds denote data releases after the May 2023 Regional Economic Prospects.

Average inflation in the EBRD regions declined from 17.5 per cent at its peak in October 2022 to 5.8 per cent in July 2024 but remained 1.6 percentage points above the pre-pandemic average (see Chart 9). This pattern is broadly similar to the one observed in advanced economies. In a typical (median) economy inflation has been broadly at par with the United States since February 2024.

Yet, in some cases, disinflation proved difficult, with a substantial average-median difference.

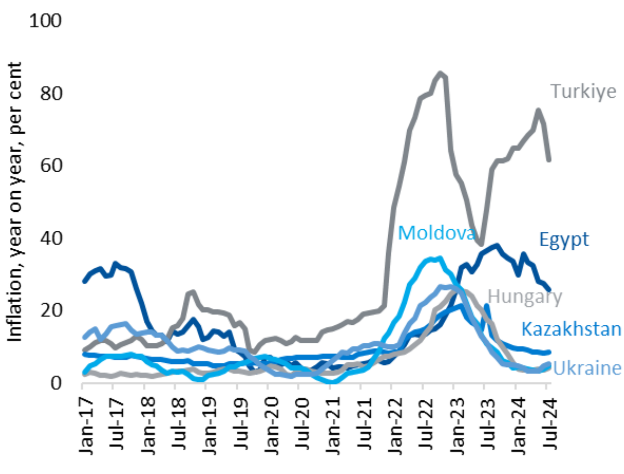
Chart 9. In a typical (median) economy inflation was at par with the United States by February 2024



Source: National authorities via Refinitiv and authors' calculations.

Disinflation has been slow in several economies, with cumulative price increases since February 2022 in excess of 30 per cent (see Chart 10).

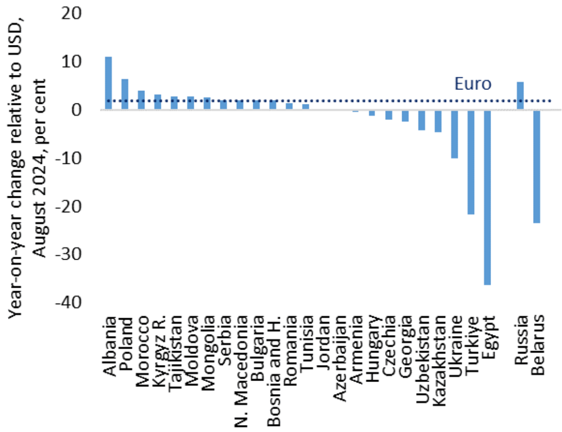
Chart 10. In some economies disinflation has been slow



Source: National authorities via Refinitiv and authors' calculations.

In some of these economies, such as Egypt and Türkiye, inflation remains high as substantial depreciations against the euro and US dollar have added to inflationary pressures (see Chart 11).

Chart 11. Depreciations contributed to inflationary pressures in some economies

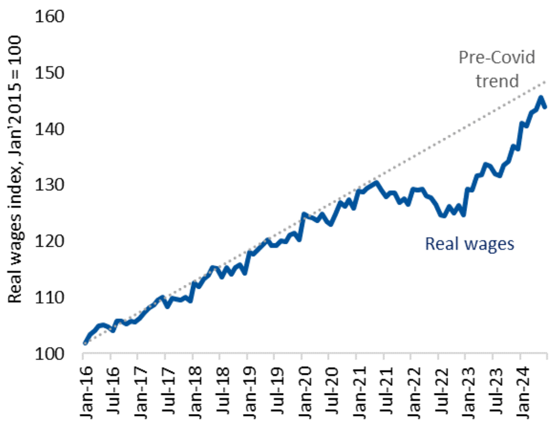


Source: Bloomberg and authors' calculations.

Real wage growth resumed, with real wages returning to just below their pre-Covid-trend levels

As inflation moderated, real wages resumed rapid growth after several quarters of declines (see Chart 12). At the low point at the end of 2022, real wages in the EBRD regions were, on average, more than 10 per cent below their pre-Covid trend. After several months of rapid catch-up in 2024, they remain perhaps 3 per cent or so below the levels that could be expected if pre-Covid trends continued. The remaining catch-up potential thus appears to be limited and real wage growth can be expected to moderate going forward.

Chart 12. Real wages started growing

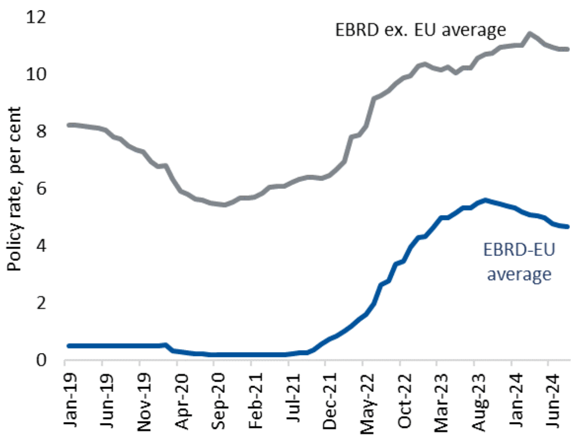


Source: Refinitiv Eikon and authors' calculations.
Note: Simple average across 15 economies in the EBRD regions.

Monetary policy started easing as inflation declined

Monetary policy started easing as inflation declined. Monetary easing started somewhat earlier in the EU economies in the EBRD regions than in EBRD economies outside the EU (see Chart 13).

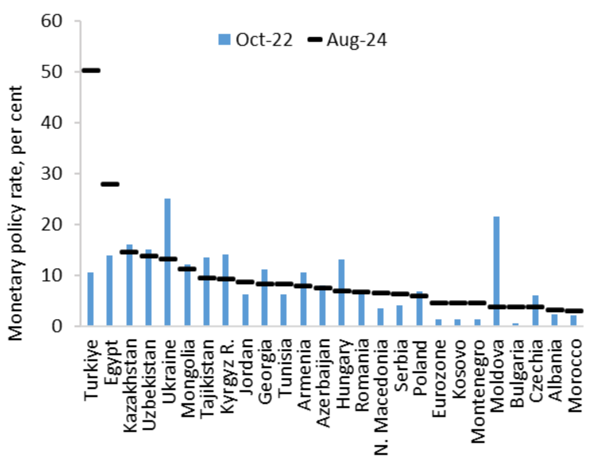
Chart 13. Policy interest rates started declining in the EBRD regions



Source: Bloomberg, national authorities via CEIC and authors' calculations.

Monetary policy rates typically remain higher than they were when inflation peaked in October 2022. Notable exceptions include Hungary, Moldova, Ukraine and some economies in the Caucasus and Central Asia (see Chart 14).

Chart 14. Monetary policy rates typically remain higher than they were when inflation peaked

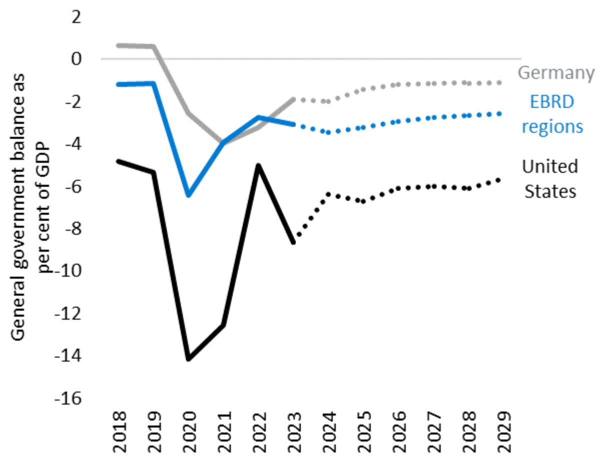


Source: Bloomberg, national authorities via CEIC and authors' calculations.

Fiscal and external vulnerabilities

Following the large fiscal stimulus packages that governments implemented during the Covid-19 crisis, fiscal deficits stabilised, on average, at above their pre-Covid levels. These trends are similar in the EBRD regions and in advanced economies (see Chart 15).

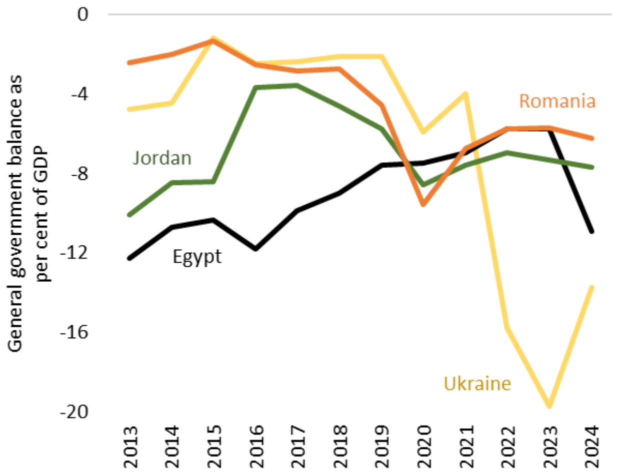
Chart 15. Fiscal deficits stabilised at or above pre-Covid levels



Source. IMF WEO April 2024 and authors' calculations. Note: Simple average based on 34 economies in the EBRD regions. Dashed lines denote IMF forecasts.

General government deficits remain largest in Ukraine, Egypt, Jordan and Romania (see Chart 16), though Romania faces relatively lower interest payments and so far more moderate levels of debt (see Chart 16). Most economies in the EBRD regions run twin (fiscal and external) deficits.

Chart 16. General government deficits remain largest in Ukraine, Egypt and Jordan and Romania

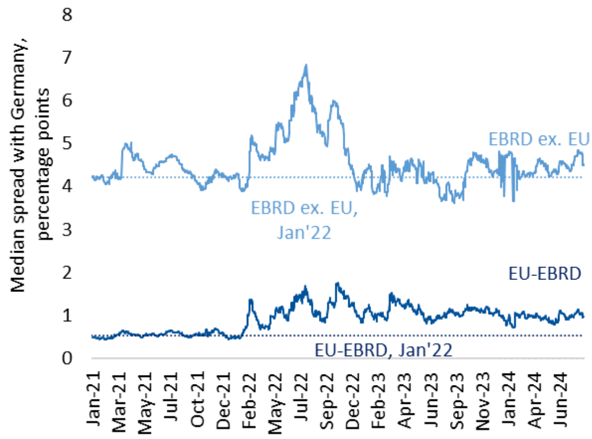


Source. IMF WEO April 2024 and authors' calculations.

In the EBRD regions as a whole, the median yield on 5-year government bonds increased by three percentage points between early February 2022 and August 2024. Most of this increase reflects monetary tightening in advanced economies. In the US and Germany interest rates increased by an average of 2.25 percentage points over this period. The remaining 0.75 percentage points are due to a widening of the spread between the EBRD regions and Germany / the United States because of a reassessment of economic and geopolitical risks faced by individual borrowers.

In a typical economy outside the EU in the EBRD regions the spread relative to Germany that had been narrowing gradually since peaking in August 2022 has resumed widening recently, reaching around 4.5 pp (see Chart 17). In the EU economies in the EBRD regions the spread that had opened sharply in March 2022 has been maintained and remains around 1 percentage point.

Chart 17. In a typical EU-EBRD economy the spread that opened in March 2022 remains

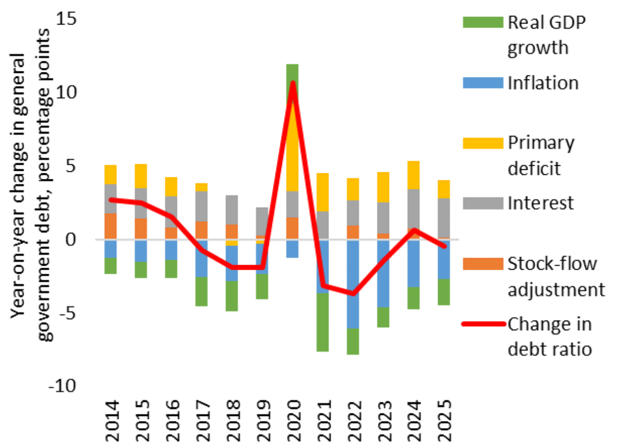


Source: Bloomberg and authors' calculations.
Note: Spread between the German 5-year bond and median government bond in EUR or USD of maturity between 4-7 years. EU-EBRD includes Bulgaria, Croatia, Czechia, Estonia, Hungary, Latvia, Lithuania, Poland, Slovak Republic and Slovenia.

Despite still-significant fiscal deficits and high interest rates, the post-pandemic inflation surge allowed policymakers to keep debt ratios relatively stable (estimated at around 51 per cent for the EBRD regions as a whole in 2024).

The average debt-to-GDP ratio in the EBRD regions peaked in 2020 at 60 per cent but started declining in 2021 as growth rebounded—this contributed about 4 percentage points to the debt reduction (see Chart 18, showing a decomposition of the impacts of growth, inflation, deficits and borrowing costs on debt dynamics). While by 2022-23, the growth effect had faded, inflation helped to bring debt ratios down further: by 6 percentage points in 2022, 4.6 percentage points in 2023 and 3.3 percentage points in 2024, as the inflation surprise eroded the real value of previously issued debt.

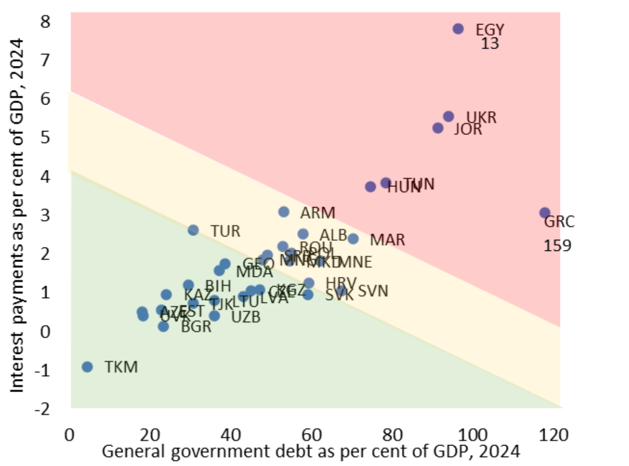
Chart 18. Inflation helped stabilise debt ratios despite large fiscal deficits and higher policy interest rates



Source. IMF WEO April 2024 and authors' calculations.

Early estimates for 2024 suggest that fiscal vulnerabilities, proxied here as a combination of relatively high interest payments as a share of GDP and elevated levels of general government debt, are highest in Egypt, Ukraine, Jordan, Greece, Tunisia and Hungary (see Chart 19). Some economies also have substantial external debt to GDP. These include some economies in the EU (such as Estonia, Greece, Latvia and the Slovak Republic), reflecting their high integration (and external debt mostly in euros), as well as Jordan, North Macedonia, Mongolia and Ukraine.

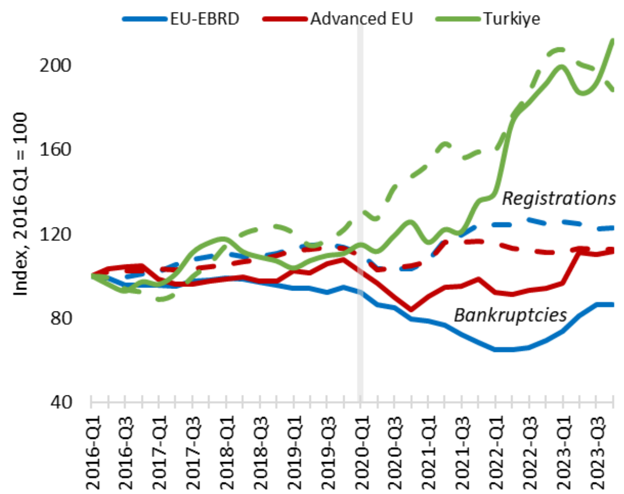
Chart 19. Fiscal vulnerabilities are significant in parts of the southern and eastern Mediterranean, Greece and Hungary



Source. IMF WEO April 2024 and authors' calculations.

Like governments, many corporates have benefited from higher inflation, which helped to reduce the effective burden of servicing previously issued debt. As a result, increases in corporate bankruptcies to date have been modest (see Chart 20). Going forward, the effective burden of interest payments for corporates and governments may increase even as central banks reduce policy interest rates.

Chart 20. Increases in corporate bankruptcies to date have been modest as higher inflation helped to reduce the effective burden of servicing previously issued debt



Source: Eurostat, The Union of Chambers and Commodity Exchanges of Türkiye and authors' calculations.
Note: EBRD regions is a simple average of 8 EU-EBRD economies. Advanced EU is a simple average of 13 economies. Liquidations shown for Türkiye. 4-quarter moving averages.

Shifting patterns of trade and investment

Recent geopolitical shifts have resulted in significant decoupling between China and the United States (see, for instance, Gopinath et al., 2024; Alfaro and Chor, 2024). However, while China-US trade contracted, China's importance as a trading partner for the EBRD regions has remained unchanged or, in some cases, has grown.

To illustrate shifts in trade patterns, Chart 21 decomposes the exports and imports of Armenia, the Kyrgyz Republic and Kazakhstan (CCA3;

economies which have benefited significantly from intermediating trade into and out of Russia, as documented in recent *Regional Economic Prospects*[2]) and the EU economies in the EBRD regions by trading partner. Focus here is on real gross exports and imports rather than value added.

China has become a more important trading partner for CCA3. China's share in the CCA3 economies' imports increased from 14 per cent in 2021 to 25 per cent in 2023, mostly replacing the declining share of imports from Russia. The shift was less pronounced for CCA3's exports: here China's share rose from 10 to 12 per cent. These shifts occurred in a context of rising CCA3 trade overall: exports reported by CCA3 increased by 37 per cent in 2023 relative to 2021, while imports reported by CCA3 increased by 64 per cent in real terms (these figures may not fully account for intermediated trade as discussed in Chupilkin et al., 2023).

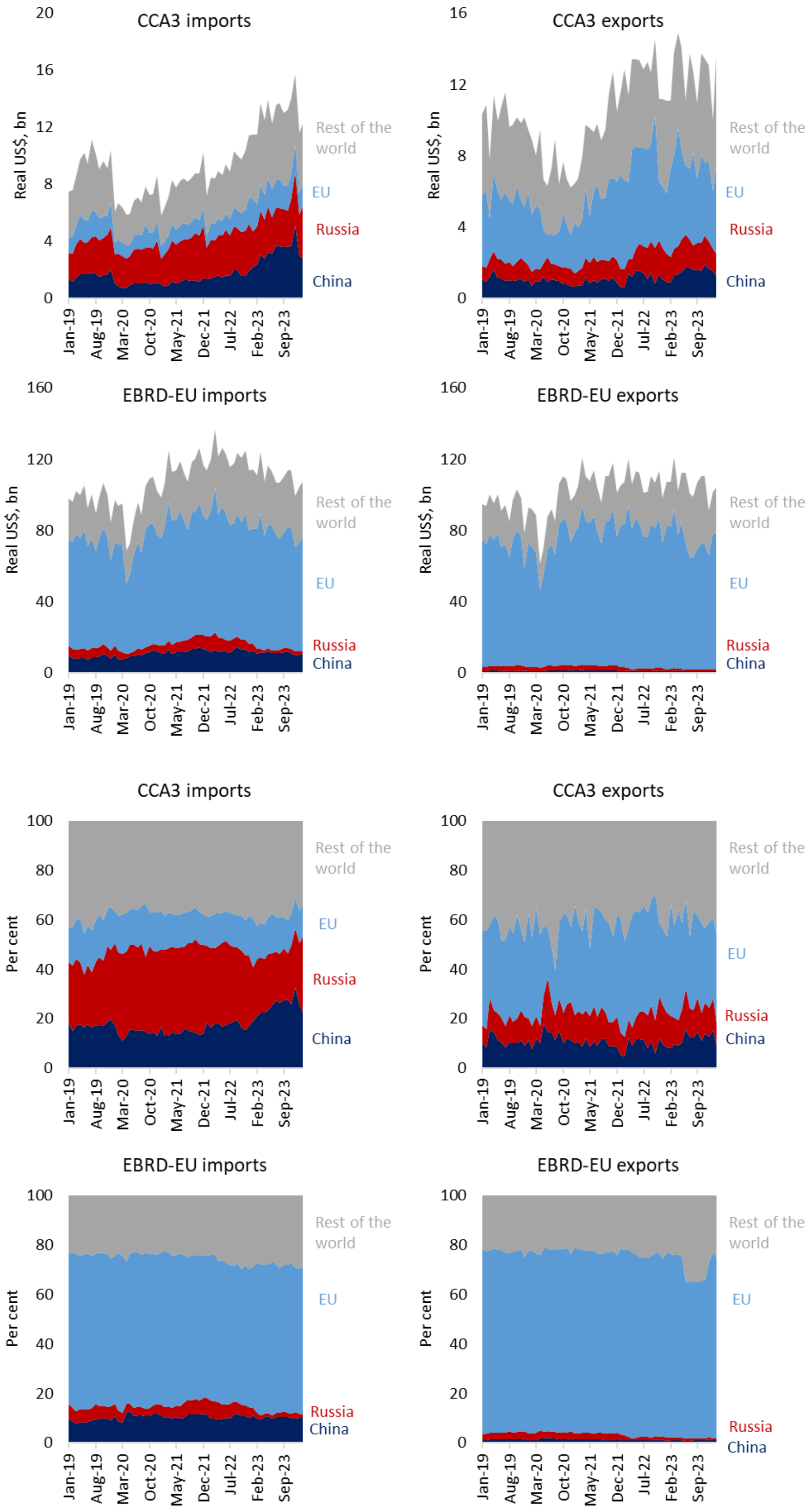
China's share of imports of the EU economies in the EBRD regions has been broadly stable at around 10 per cent. China also remains an important source of imports in a number of sectors related to the green transition. For instance, China accounts for 69 per cent of imports of solar batteries in central and south-eastern Europe, 46 per cent of imports of wind turbines, 46 per cent of lithium-ion batteries and 5 per cent of imports of electric cars (based on data from UN Comtrade).

Reliance on green technologies from China is, in part, driven by lower prices. In 2023, the average electric vehicle imported by the EU from China was 33 per cent cheaper than the average electric vehicle imported from the rest of the world. Specifically, electric vehicles from China cost, on average, US$ 23,900, compared with US$ 35,600 for those from other regions. In Slovenia, the differential was around 42 per cent less. Electric vehicles exported by the EU cost, on average, more than double those imported from China, suggesting that domestic production targets primarily the higher end of the market.[3]

[2] See also Chupilkin, Javorcik and Plekhanov (2023).

[3] See Kirkegaard (2024).

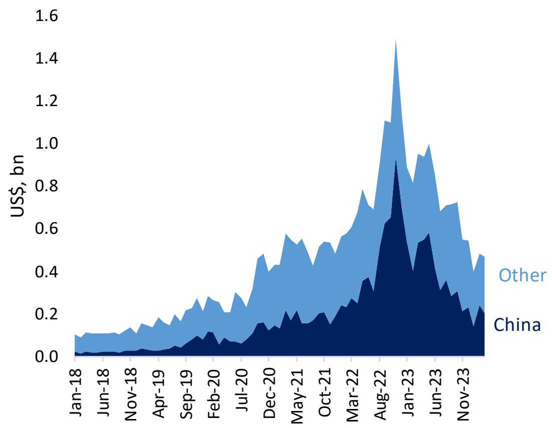
Chart 21. China's share in CCA3 imports increased, while its share in imports of EU economies in the EBRD regions has remained broadly stable



Source: UN Comtrade and authors' calculations.

Since 2023, the EBRD regions' imports of batteries from China have, however, declined in both value and quantity – as domestic battery industries emerged supported by foreign direct investment (FDI) (see Chart 22). For instance, in 2022 FDI from China into the battery sector in Hungary was estimated at around US$ 7.5 billion, with a large new factory in Debrecen. In 2023, Chinese FDI in batteries in Morocco was estimated at around US$ 6.4 billion (based on estimated announced capital expenditures in the fDi Markets database).

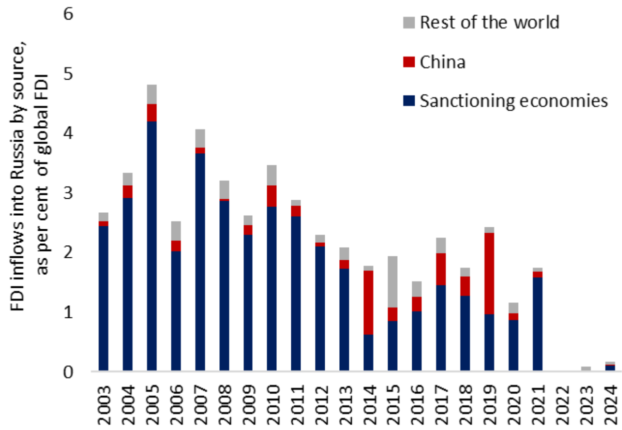
Chart 22. EU-EBRD economies' battery imports from China have declined



Source: UN COMTRADE and authors' calculations.
Note: HS 850760 used for lithium-ion batteries.

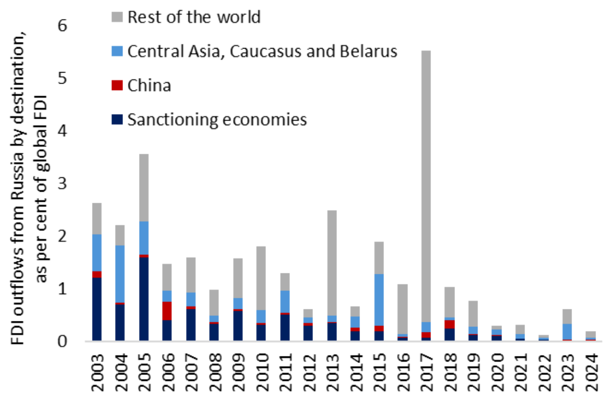
While in some instances geopolitical tensions may give rise to FDI seeking to bypass barriers to trade, in other cases such tensions have clearly negative impacts on investment linkages. Greenfield FDI inflows into Russia have collapsed since the start of the war on Ukraine (see Chart 23 and analysis in Cheng and Plekhanov, 2024). This collapse in FDI contrasts with the picture for trade where China, Türkiye and other economies that did not impose sanctions on Russia filled the gap left by withdrawing firms from sanctioning economies (see, for instance, Chupilkin et al., 2024b). FDI outflows from Russia have also dropped to low levels since the start of the war on Ukraine (see Chart 24).

Chart 23. Greenfield FDI inflows into Russia have collapsed since the start of the war on Ukraine



Source: fDi Markets database and authors' calculations.
Note: Based on estimated announced capital expenditures. Shown as a share of global FDI to take into account the effect of global shocks, such as the Covid-19 crisis. Sanctioning economies are those that have imposed sanctions on Russia (see Chupilkin et al., 2024a).

Chart 24. Greenfield FDI outflows from Russia have been low in recent years

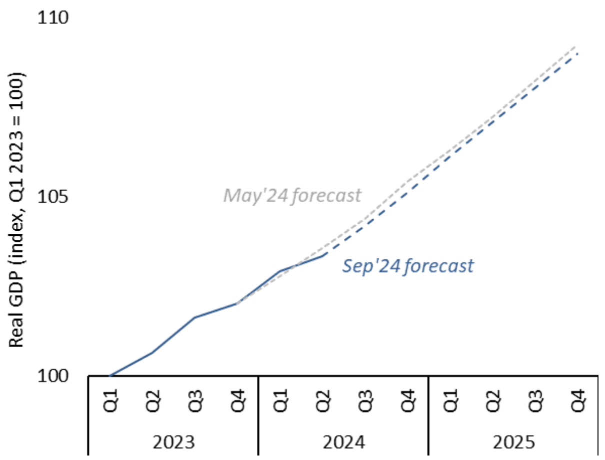


Source: fDi Markets database and authors' calculations.
Note: Based on estimated announced capital expenditures.

Output in the EBRD regions is expected to grow by 2.8 per cent in 2024 and 3.5 per cent in 2025

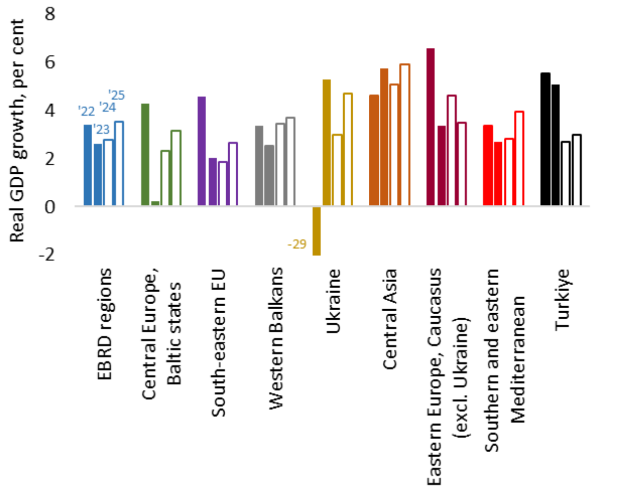
Growth in the EBRD regions is expected at 2.8 per cent in 2024, picking up to 3.5 per cent in 2025 (see Table 1 and Chart 25). This represents downward revision relative to the May 2024 forecast (of 0.2 of a percentage point (pp) in 2024 and 0.1 pp in 2025) reflecting weaker outlook for advanced Europe, stagnating mining output in Kazakhstan and Uzbekistan, the ongoing conflict in Gaza and severe droughts in Morocco and Tunisia (see Chart 26).

Chart 25. Forecasts of growth in the EBRD regions in 2024-25 have been revised down by 0.1 – 0.2pp since May 2024



Source: National authorities via CEIC and EBRD forecasts.
Note: EBRD average based on the values of gross domestic product in 2022 in current US dollars from the IMF.

Chart 26. Growth in the EBRD regions is expected at 2.8 per cent in 2024 and 3.5 per cent in 2025



Source: National authorities via CEIC and EBRD forecasts.
Note: EBRD average based on the values of gross domestic product in 2022 in current US dollars from the IMF.

The recent slowdown and the expected rebound in the EBRD regions are more pronounced than for the global economy as a whole. Global growth (measured at market exchange rates) slowed from 3 per cent in 2022 to 2.7 per cent in 2023. The International Monetary Fund (IMF) expected it to remain at 2.7 per cent in 2024 picking up slightly to 2.8 per cent in 2025 in its July 2024 *World Economic Outlook Update.* This was in line with the forecasts made in April 2024, though with an upward revision to growth in China, reflecting a pick-up in domestic consumption as well as a surge in exports.

Regional outlooks

In **central Europe and the Baltic states** growth is expected to accelerate from 0.2 per cent in 2023 and 2 per cent year on year in the first half of 2024 to 2.3 per cent in 2024 and 3.2 per cent in 2025. The recovery in the region is uneven, with both upward and downward revisions since the May 2024 forecast, reflecting a combination of weak external demand from advanced Europe and fiscal pressures amidst continued resilience in labour markets. Growth has been revised up in Croatia, Czechia, Lithuania, Poland and the Slovak Republic, in large part reflecting rapid real wage growth supporting household consumption as inflation slowed. It has been revised down in Estonia and Latvia (including on spillovers from slow growth in the Nordic economies), Hungary (where inflation peaked later than elsewhere in the region) and Slovenia (on weak external demand).

Growth in the **south-eastern EU** is expected at 1.9 per cent in 2024, broadly in line with the outcomes in 2023 and the first half of 2024, picking up to 2.6 per cent in 2025. Forecasts for both years have been revised down relative to the May 2024 forecasts on weak industrial production and, in the case of Romania, lower demand for outsourcing weighing on the IT sector.

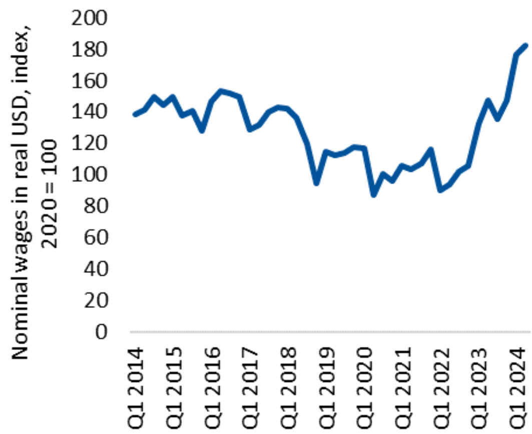
Growth in the **Western Balkans** picked up from 2.5 per cent in 2023 to an estimated 3.7 per cent in the first half of 2024. It is expected at 3.4 per cent in 2024 and 3.7 per cent in 2025. The 2024 growth forecasts have been revised up in Albania on a strong tourism season, in Serbia reflecting strong investment and an accommodative fiscal and monetary stance and in Montenegro on sustained consumption growth.

Growth in **Central Asia** is moderated from 5.7 per cent in 2023 to 4.7 per cent year on year in the first half of 2024 as mining output in Kazakhstan and Uzbekistan stagnated. It is expected to average 5.1 per cent in 2024 picking up to 5.9 per cent in 2025.

In **eastern Europe and the Caucasus**, growth picked up from 4.4 per cent in 2023 to an estimated 6 per cent year on year in the first half of 2024. It is expected to moderate to 3.7 per cent in 2024 as a whole before picking up to 4.1 per cent in 2025. The growth forecast for **Ukraine** is unchanged for 2024 but revised down for 2025 as the destruction of electricity infrastructure in the context of Russia's full-scale invasion of Ukraine is expected to continue weighing on production. The upward revision to the 2024 forecast in Georgia reflects strong growth in manufacturing output.

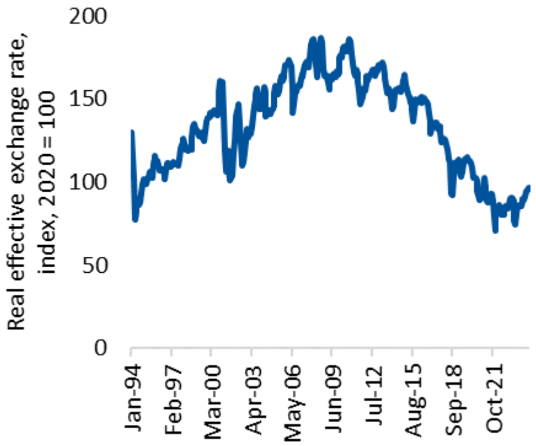
In **Türkiye**, growth moderated from 5.1 per cent in 2023 to 3.8 per cent year on year in the first half of 2024. It is expected to moderate further to 2.7 per cent in 2024 and 3 per cent in 2025 (both unchanged relative to the May 2024 forecasts) reflecting the impact of tighter monetary policy. Real wages have been increasing rapidly, both in local-currency terms and expressed in US dollars (see Chart 27). As inflation outran lira depreciation, the real effective exchange rate strengthened rapidly (see Chart 28).

Chart 27. Real wages have been increasing in Türkiye, in local-currency and in US-dollar terms



Source: Refinitiv and authors' calculations
Note: Nominal wages converted into USD and controlling for US inflation.

Chart 28. In Türkiye, the real effective exchange rate strengthened recently after years of trending downward



Source: Bank for International Settlements and authors' calculations.

Growth in the **southern and eastern Mediterranean** moderated from 2.7 per cent in 2023 to an estimated 2.1 per cent year on year in the first half of 2024. It is expected to pick up to 2.8 per cent in 2024 as a whole and 3.9 per cent in 2025. This represents a downward revision on the previous forecast for 2024 owing to disruptions in the energy sector in Egypt, a slower-than-expected recovery in private and public investment, severe droughts in Morocco and Tunisia and the impact of the conflict in Gaza and Lebanon on Jordan and Lebanon.

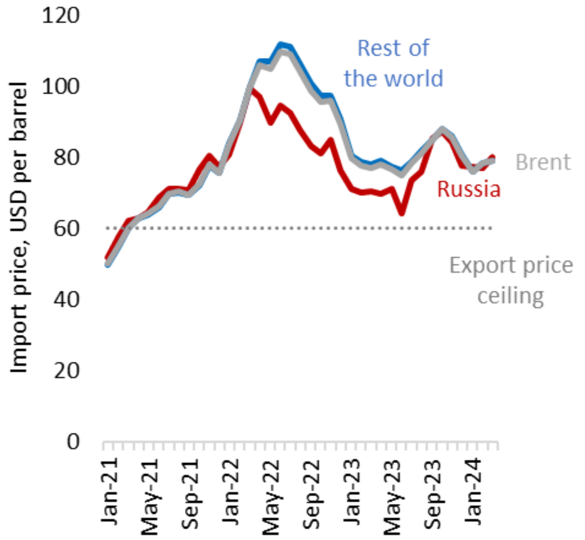
In **Russia**, growth accelerated from 3.6 per cent in 2023 to 4.7 per cent year on year in the first half of 2024, with strong activity in the manufacturing sector, as the price of Russia's oil exports is estimated to have increased by more than 10 per cent year on year, trade with non-sanctioning economies has been strong and military spending has been high in the context of the ongoing full-scale invasion of Ukraine. Growth is expected to slow to 3.6 per cent in 2024 as a whole and 1.5 per cent in 2025 in line with the medium-term potential reflecting labour constraints.

Following the start of the war on Ukraine, a significant spread emerged between Russian oil prices and those of other global producers, peaking at nearly 20 US dollars per barrel in the summer of 2022 based on import price data reported by the purchasing economies to UN Comtrade (see Chart 29). However, this spread has gradually declined, closing by the end of 2023 as new trading arrangements have been put in place.

It should be noted that import prices reported by destination economies are higher than the price paid at the point of export on account of cost of insurance and transportation and the difference between the two in the case of Russian oil can be large as discussed in Kilian et al. (2024). Import prices are nonetheless indicative of trends over time.

These trends suggest that the price of Russian oil increased by around 11 per cent year on year in the first months of 2024. Given the average estimate of the marginal cost of production of 32 US dollars per barrel, the rent Russia earns per barrel of exported oil (price net of cost) increased by 23 per cent year on year in the first quarter of 2024. The estimates of marginal cost of production used in the above calculation average data from Rosstat (see Chart 31), as well as a number of other sources. If higher cost estimates are used the year-on-year increase in oil rent will in fact be larger.

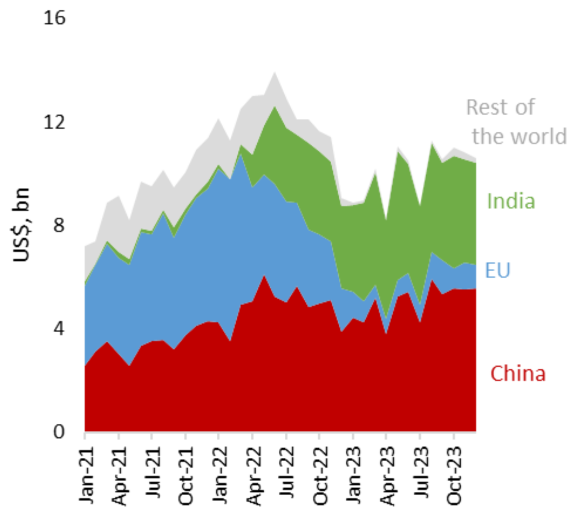
Chart 29. The spread between import prices reported for Russian crude oil and oil from other sources has disappeared by end-2023



Source: UN COMTRADE, Refinitiv and authors' calculations.
Note: The import price per barrel is derived from weight, based on 136 kg per barrel of oil. Price ceiling refers to the G7 agreed ceiling for the export price of Russian oil.

The price dynamics in part reflects reorientation of exports towards new markets (see Chart 30). The EU's share in Russian oil exports fell sharply, from 45 per cent in 2021 to 8 per cent in 2023. Meanwhile, China's share increased from 36 to 50 per cent, and India's rose from 2 to 40 per cent. Although all importers of Russian oil paid less for it in 2023 compared to oil from other sources, EU buyers paid around 15 per cent less than their counterparts in China and India, according to UN Comtrade data.

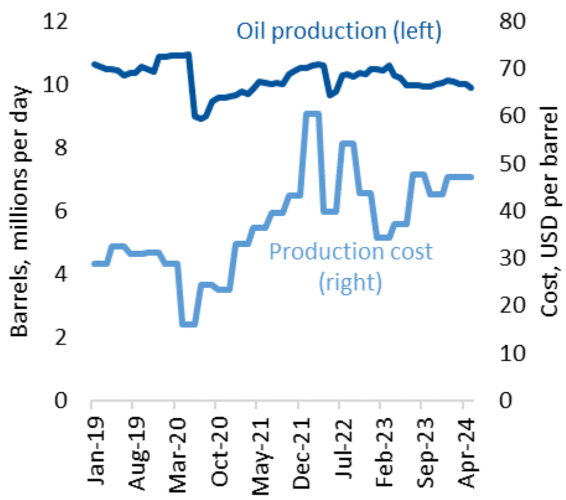
Chart 30. Exports of Russian crude oil have shifted from the EU to China and India



Source: UN COMTRADE and authors' calculations.

In 2023, Russia produced approximately 10.2 million barrels per day, representing a decline of 3.2 per cent compared to 2019 levels (see Chart 31).

Chart 31. Oil production has become more costly in Russia, constraining supply



Source: Refinitiv, Rosstat and authors' calculations.

The outlook for growth in the EBRD regions is subject to numerous risks. They relate to further rapid escalation of geopolitical tensions; renewed inflationary pressures on the back of high nominal wage growth in the EBRD regions as well as selected advanced economies; and increased frequency of extreme weather events such as droughts or floods against the background of sustained increased in average temperatures globally and in the EBRD regions. A sharper than expected slowdown in China would also weigh on external demand.

Box 1. Declining intergenerational mobility

This box examines changes in intergenerational mobility in the EBRD regions and advanced economies.

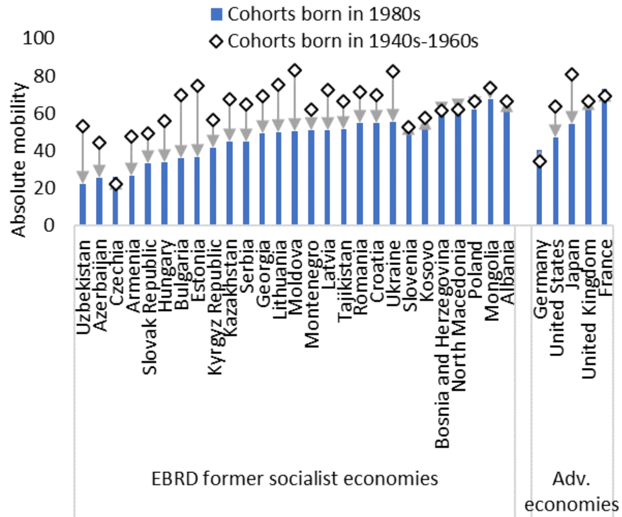
Intergenerational mobility—the extent to which children do better in life than their parents—is often measured as 'absolute mobility': the percentage of individuals who have a higher level of education than their parents (conditional on the parents not having completed tertiary education).

In general, absolute mobility has an inverted U-shaped relationship with GDP per capita. The lowest rates of absolute mobility are observed in the very poorest countries where the threshold for surpassing parents' level of education is low, but so is the capacity to educate children. It then rises with income per capita before declining again in richer countries where the capacity to educate children is high, but so is the threshold for surpassing parents' level of education.

High levels of intergenerational mobility tend to be associated with greater equality of opportunity in a society, which, in turn, is associated with greater economic efficiency and social cohesion (see, for instance, EBRD, 2024, for a discussion).

In the former socialist economies in the EBRD regions, absolute mobility has declined sharply for cohorts born in the 1980s relative to cohorts born in the 1940s-60s (see Chart 1.1). Those born in the 1940s-60s were very likely to achieve a higher level of education than their parents, reflecting substantial investments in education and overall promotion of social mobility in the decades following the Second World War. In contrast, this likelihood has fallen for those born in the 1980s and thus reaching adulthood after the start of transition.

Chart 1.1 Absolute mobility has declined sharply for cohorts born in the 1980s relative to cohorts born in the 1940s-60s



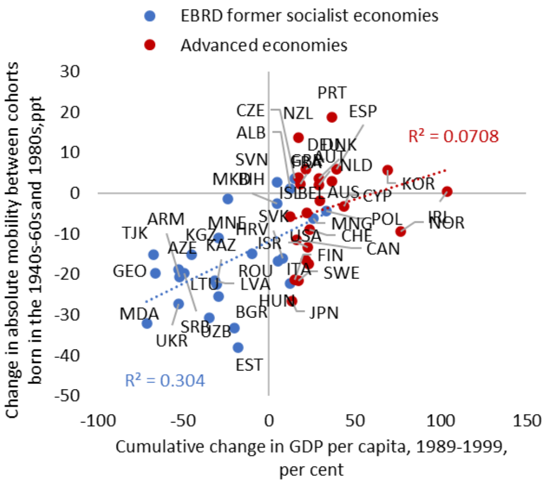
Source: GDIM and authors' calculations.

This pattern holds in advanced economies, for instance, absolute mobility has declined sharply in the United States and Japan. However, it is much more pronounced on average in the former socialist economies. This could reflect the increase in inequality and reductions in education spending during the 1990s, as well as the impact of the transition recessions, which may have forced lower-income individuals to prioritise income at hand over investment in human capital.

Indeed, the decline in absolute mobility tended to be larger in economies with larger cumulative GDP per capita drops in the 1990s (see Chart 1.2). While this relationship between intergenerational mobility and long-term growth also holds in advanced economies, it is not statistically significant in that subsample and the cumulative change in GDP per capita explains much less of the variation in the change in absolute mobility.

The observed drop in intergenerational mobility, in turn, has important implications for support for democracy, market economy and reforms in general—as discussed in detail in the forthcoming *Life in Transition Survey IV* report.[4]

Chart 1.2 Declines in absolute mobility were larger where transition recessions were deeper



Source: Maddison Project, World Bank's WDI and authors' calculations.
Note: Advanced economies based on the classification in the IMF's World Economic Outlook.

[4] See EBRD (2024).

Regional updates

Central Asia

Extreme weather events in Kazakhstan and Mongolia weakened the countries' growth momentum in the first half of 2024. In contrast, the Kyrgyz Republic and Tajikistan demonstrated strong economic performance, with GDP rising by 8.7 and 8.2 per cent year on year, respectively. Overall, sustained remittance inflows, increased wages and favourable tourist seasons supported demand, boding well for the services sector. Investment activity continued booming, reflecting efforts to develop transport, logistics and energy infrastructure. In line with global trends, inflation in the region eased to single digits (except in Uzbekistan), allowing central banks to start loosening their monetary policy rates gradually. Nevertheless, inflationary risks persist, related to utility tariff adjustments and elevated government spending. The short-term regional outlook remains positive. Regional growth is expected to reach 5.1 per cent in 2024 (somewhat below the 2023 reading of 5.7 per cent) and accelerate to 5.9 per cent in 2025 on stronger commodity revenues, infrastructure investment and market-oriented reforms.

Kazakhstan

In the first half of 2024, the economy expanded by 3.2 per cent year on year in real terms. Industry and trade were the main growth drivers, contributing 0.8 and 0.6 percentage points, respectively. Reflecting the authorities' diversification efforts, growing manufacturing output (up 5.1 per cent year on year) supported industrial production despite sluggish growth in the mining and quarrying sector (up 0.3 per cent year on year). Services expanded at the rate of 3.1 per cent year on year, led by trade, transport and warehousing and ICT. Export growth was modest, but a notable import decline resulted in a trade surplus, which expanded by 36 per cent year on year. Since February 2023, inflation has been trending downward, before rising slightly to 8.6 per cent in July 2024 on higher utility costs.

While gradually loosening its policy rate (with cumulative rate cuts of 150 basis points year-to-date), the National Bank of Kazakhstan maintains a cautious monetary policy stance as inflationary risks persist. The tenge strengthened vis-à-vis the US dollar in the first five months of 2024, supported by elevated foreign exchange sales from the National Fund. With National Fund transfers gradually decreasing, the tenge experienced a downward correction depreciating by 5 per cent in January-August. Economic growth is forecast to pick up from 3.2 per cent year on year in the first half of the year to 4 per cent in 2024 as a whole and public spending to restore flood-affected infrastructure and housing could provide an upside. In 2025, real GDP is projected to grow by 5.5 per cent amid the planned expansion of the Tengiz oil field.

Kyrgyz Republic

Real GDP expanded by 8.7 per cent in January-July 2024. The Kyrgyz Republic's growing attractiveness as a tourist destination resulted in an increased restaurant and bars turnover (up 24 per cent year on year in the first half of 2024) and tourist transportation revenues (up 53 per cent), bringing the tourism sector's gross value added up to 2.7 per cent of GDP. Additionally, net remittances increased by 12 per cent and real wages were up 5.2 per cent, helping retail and wholesale trade. Sophisticated manufacturing activities are gathering steam as domestic production of computers and electronics (up almost five times) and vehicles and equipment (up 1.6 times) expanded in January-July 2024. Nevertheless, overall industrial production stagnated (up just 0.8 per cent) amid a decline in mining output. In May 2024, as inflation stabilised, the National Bank of the Kyrgyz Republic opted for the first policy rate cut since November 2022, lowering the rate to 9 per cent. At 4.1 per cent as of July 2024, inflation was below the target range. GDP growth is forecast to reach 9 per cent in 2024 before moderating to 7 per cent in 2025. There is upside potential related to tourism expansion, infrastructure investment, and silver and gold exports picking up in the second half of 2024. At the same time, secondary sanctions in the context of trade with Russia remain a threat.

Mongolia

Economic growth moderated to 5.6 per cent year on year in the first half of 2024. Due to extreme weather, livestock losses reached 8.1 million heads (2.1 times higher than in the first half of 2023), driving a deep contraction in agriculture (-26.7 per cent year on year). On the positive side, services emerged as the main growth driver, contributing 4.4 percentage points to growth. The number of inbound foreign passengers increased by 32.6 per cent, supporting revenues of hotels (up 11.7 per cent), food and beverages service activities (up 20.1 per cent) and transportation (up 24.8 per cent). Gross industrial output expanded at the rate of 16.4 per cent year on year, supported by expansion in mining and quarrying (up 21.1 per cent) and manufacturing production (up 4.5 per cent). In January-July 2024, exports recorded a modest growth of 6.5 per cent year on year on rising coal and copper concentrate exports. Imports increased by 27.6 per cent, driven by a 44.6 per cent increase in machinery, equipment and electric appliances imports. Amid receding inflation, the Bank of Mongolia cut the policy rate to 10 per cent in September 2024. Inflation remains within the central bank's target range, at 6.5 per cent as of August 2024. Growth in 2024 is expected to moderate to 5 per cent, as lower agricultural output and economic slowdown in China cloud the outlook. In 2025, the economy is projected to expand by 8 per cent, supported by a rebound in agriculture and further expansion in mining. Upside risks to the outlook are related to stronger-than-expected growth in China, driving external demand. On the downside, growth prospects remain highly vulnerable to fluctuations in commodity prices and energy supply.

Tajikistan

Output expanded at the rate of 8.2 per cent year on year in the first half of 2024 with real wages posting 9.1 per cent growth, thanks to a hike in public sector salaries, pensions and minimum wage. Supported by higher incomes, domestic demand remained robust. Retail and wholesale trade was up 11.6 per cent year on year in January-July 2024 and the hospitality, restaurants and catering sector was up 13.8 per cent. Led by public infrastructure spending, fixed capital investment was another important growth driver (up 11.5 per cent). Resumption of gold exports resulted in a 46 per cent export growth. However, the trade balance recorded a deficit of US$ 2.8 billion on higher imports of mineral products, food and chemicals. A stronger somoni (up 2.5 per cent year-to-date against the US dollar) helped contain inflationary pressures, with inflation coming down to 3.4 per cent year on year in July 2024. As a result, the central bank lowered its policy rate to 9 per cent in August, reflecting a shift towards a more accommodative monetary stance. On the fiscal side, revenues were up 6.8 per cent, while expenditures increased by 7.4 per cent and the budget remained in surplus. GDP growth is projected to reach 8 per cent in 2024 and 7 per cent in 2025, supported by large-scale investment in infrastructure. Fluctuations in remittances from Russia represent a major downside risk.

Turkmenistan

According to official estimates, Turkmenistan's economy has demonstrated remarkable stability in recent years, growing by 6.3 per cent year on year in the first half of 2024. Investment was one of the major growth drivers, as fixed capital investment was up 20.8 per cent year on year, reaching 17.5 per cent of GDP. Supported by state-funded infrastructure projects, the construction sector expanded by 9.3 per cent. Services grew at the rate of 7.9 per cent, as higher wages and pensions helped sustain strong purchasing power. The launch of a new single window for export-import operations has improved customs efficiency and simplified transit procedures, enabling higher freight turnover. As a result, the transportation sector expanded (up 7.3 per cent), with sea freight growing by 8.2 per cent. In August 2024, Fitch upgraded Turkmenistan's rating to “BB-” with a “stable” outlook, reflecting the country's ample external reserves, low public debt and consistent fiscal discipline. Growth is expected to remain stable, at 6.3 per cent in 2024 and 2025. Weaker growth in China, Turkmenistan’s key trade partner, would negatively impact demand for Turkmen gas, thus weighing down on the country’s growth opportunities. On the upside, diversification efforts and investment in transport infrastructure could strengthen the outlook.

Uzbekistan

Economic growth accelerated slightly, to 6.4 per cent year on year in the first half of 2024. The services sector contributed 2.8 percentage points to GDP growth, supported by increased remittances and tourist arrivals. Industrial production expanded by 7.8 per cent, with 9.4 per cent growth in manufacturing. Energy shortages amid lower gas extraction led to a 78 per cent increase in mineral fuel imports in January-July 2024 (including an almost five-fold increase in gas imports), resulting in a trade deficit of US$ 7.3 billion. The consolidated budget deficit reached 2.6 per cent of GDP as of the first quarter of 2024. Budget subsidies to the energy sector accounted for more than 70 per cent of total subsidies in the first half of 2024, with subsidies allocated for covering the losses owing to the difference between import price of natural gas and the price in the domestic market almost fully used up. At 10.5 per cent year on year as of July 2024, inflation remained more persistent than that of regional peers amid expansionary fiscal policy, currency depreciation and energy tariff adjustments. Nevertheless, the Central Bank opted for a small rate cut in July, bringing its policy rate down from 14 to 13.5 per cent. The economy is projected to expand by 6 per cent in 2024 and 2025 on continued market-oriented reforms and infrastructure investments. However, energy deficits could pose challenges and limit growth opportunities.

Central Europe and the Baltic states

Average growth in central Europe and the Baltic states (CEB) recovered from 0.2 per cent in 2023 to 2 per cent year on year in the first half of 2024. Czechia, Estonia and Latvia have experienced weak export performance, while Croatia, Lithuania, Poland, and the Slovak Republic have rebounded strongly on robust household consumption and public investment. Hungary saw robust consumption growth on the back of rising real wages, while corporate investment, especially in manufacturing, was at its lowest level since the pandemic. Rising government deficits are a source of concern, with Hungary, Poland, and the Slovak Republic being under European Commission scrutiny, calling for tax hikes and fiscal consolidations. The war on Ukraine, energy price fluctuations and declining trade with Russia and Belarus are all exacerbating external vulnerabilities, particularly in Estonia and Latvia. Weaknesses in Germany’s industry, along with slow growth in Italy and France, are leading to weaker exports across the CEB region, with Poland, Slovenia, and Hungary experiencing large drops in exports to Germany in early 2024. Recent floods disrupted economic activity in parts of the CEB region, in particular in Czechia and Poland. However, post-flood reconstruction should boost GDP growth later this year and next year. Labour markets in Czechia, Poland, Hungary, and Slovenia remain tight, with low unemployment and significant participation of foreign workers, particularly in Poland. Skill mismatches and rising labour costs raise concerns, as large minimum wage hikes in Poland, Croatia, Hungary, and the Baltic states have contributed to rapid real wage growth.

Croatia

The Croatian economy continued its expansion in 2024, with GDP growing by 3.6 per cent in the first half of 2024. The highest rate of growth in the region reflected acceleration in both private consumption and investment. The minimum wage hike, together with a public pay reform that resulted in significant salary increases in the public sector, translated into a real wage growth of 12 per cent in the first half of 2024. Reflecting this, retail sales growth has accelerated to 8 per cent year on year since October 2023. Unemployment has further declined in 2024 while industrial production has not yet returned to a stable growth path. On the upside, the tourism season recorded another increase in arrivals and nights, with significant growth recorded outside the peak summer months. Improved absorption of EU funds and acceleration of post-earthquake reconstruction have supported investment. However, significant increases in public sector salaries will lead to a fiscal deterioration in 2024. Public debt is nonetheless expected to decline slowly as a per cent of GDP in the medium term. GDP growth forecast for 2024 is revised up to 3.6 per cent. In 2025, GDP could expand by 3 per cent, driven by EU-funded investments and reflecting a weaker momentum in consumption as the wage growth effect wanes.

Czechia

After contracting by 0.1 per cent in 2023, the Czech economy showed timid signs of recovery in the first half of 2024. After a 2.8 per cent drop in 2023, private consumption expanded by 1.4 per cent year on year in the first half of 2024 while retail sales were growing by 3.9 per cent year on year by July 2024, reflecting improved consumer confidence. After recording the steepest fall among peers in 2023, real wages recovered somewhat, with real wage growth subsequently easing to 3.9 per cent year on year in the second quarter of 2024. After a strong recovery after the pandemic, investment declined by almost 2 per cent in the first half of 2024, while the destocking cycle continued. Reflecting this, imports were lower than in the same period of last year, counterbalancing weak exports. As inflation averaged 2.5 per cent in the seven months to July 2024, the Czech National Bank cut the key interest rate five times in January-August 2024, to 4.5 per cent. The September 2024 floods resulted in a 10 per cent increase in the fiscal deficit planned for the year (around €1.2 billion), despite the EU being expected to offer grants worth €2 billion to limit the impact on the budget. The economy is forecast to grow by 1.1 per cent in 2024 on the back of the modest rebound of consumption, while stagnating foreign demand remains a key risk to the outlook. In 2025, more favourable financing conditions and further strengthening of foreign demand should support an increase in the growth rate to 2.4 per cent.

Estonia

Estonia’s economy has been grappling with a severe recession, the worst since 2009. Following a 3 per cent contraction in 2023, GDP fell further by 1.6 per cent year on year in the first half of 2024. The war on Ukraine has disrupted supply chains, prompting a shift from cheaper Russian and Belarusian imports to costlier alternatives. Combined with a stronger euro, this contributed to a nearly 10 per cent drop in exports over the past year. Inflation eased to 3.5 per cent in July 2024 but remains high compared with regional peers reflecting steep services inflation and a recent value added tax (VAT) increase. As a result, household consumption remains weak, constrained by low consumer confidence. Investment and hiring have also declined as businesses face rising production costs and subdued external demand. Investment dropped by 3 per cent in 2023, and the employment rate fell from 82.4 per cent in the first quarter of 2023 to 81.5 per cent in the first quarter of 2024, with unemployment rising to 7.8 per cent. Despite these challenges, Estonia is expected to remain compliant with EU deficit criteria, with the general government deficit projected to hold at 3.4 per cent of GDP in 2024. The government plans tax hikes starting in mid-2025 and a temporary corporate defence tax to support increased military spending. While the economy is forecast to contract by 0.8 per cent in 2024, growth is anticipated to return to 2.5 per cent in 2025, driven by improved external demand and domestic investment.

Hungary

After a contraction of 0.9 per cent in 2023, Hungary's economy grew at the rate of 1.3 per cent year on year in the first half of 2024. This rebound was driven by rising real wages, which surged by nearly 10 per cent in mid-2024, as inflation eased to 4.1 per cent in July 2024 and labour market remained tight, with unemployment at 4.3 per cent and the employment rate above 81 per cent. At the same time, corporate investment remained subdued due to high economic uncertainty, elevated labour costs, and weak external demand. Hungary has become a key destination for Chinese foreign direct investment (FDI); in 2023, Hungary surpassed traditional leaders like Germany and France, capturing 44 per cent of all Chinese FDI flows in Europe, largely directed towards the electric vehicle (EV) sector. This influx, with FDI inflow estimated at nearly €5 billion or 2.5 per cent of 2023 GDP in 2023 and the first half of 2024, has created around 9,000 jobs. Meanwhile, FDI from the EU, the United Kingdom, and the United States made up just a quarter of Hungary's total inflows in 2023, far below the 80 per cent typical in other CEB economies. With the fiscal deficit hitting 6.7 per cent of GDP in 2023, the European Commission has proposed an excessive deficit procedure for Hungary. New taxes introduced in August 2024 aim to reduce the deficit to 4.5 per cent this year. Investment and export recovery will be crucial for sustained economic growth. GDP growth is forecast at 1.8 per cent for 2024 and 3.3 per cent for 2025.

Latvia

Latvia's economy is making a slow recovery in 2024 after last year's downturn. In 2023, GDP contracted by 0.3 per cent, but the first half of 2024 saw a modest rebound with growth of 0.3 per cent year on year. Robust nominal wage growth of over 11 per cent and a sharp drop in inflation to 0.8 per cent by July 2024, have boosted consumer confidence. At the same time, exports remain weak, particularly in wood and metal products, due to subdued demand from the Nordic markets. A Luminor Bank survey reveals persistent concerns about inflation and rising costs, shared among 40 per cent of small and medium-sized enterprises. Investment activity has stalled after a strong rebound in 2023, which was driven by accelerated public-sector projects funded by the previous EU budget cycle. In 2024, both public and private investments have stagnated, as businesses await lower interest rates and a robust recovery in demand. Foreign direct investment flows have also moderated, from 3.4 per cent of GDP in 2023 to 1.5 per cent (annualized) in early 2024. The general government deficit is set to widen to 3 per cent of GDP in 2024, reflecting increased spending on public wages and defence. Looking ahead, Latvia's economy should gradually recover, with GDP growth projected at 0.9 per cent in 2024 and accelerating to 2.4 per cent in 2025, supported by improving export conditions.

Lithuania

Lithuania's economy is regaining momentum, buoyed by solid household consumption, rising investment, and a recovery in services exports. After a downturn last year, GDP grew by 2.4 per cent year on year in the first half of 2024, supported by a 9.3 per cent year-on-year increase in real gross wages in the second quarter of 2024. Public investments, especially in green energy and defence, are boosting growth, while service exports, particularly transport services, are rebounding from previous global disruptions. While headline inflation stood at 1.1 per cent, services inflation reached 6.1 per cent, driven by rising labour costs. The ECB's Harmonised Competitiveness Indicator shows a nearly 12 per cent drop in international competitiveness compared with pre-pandemic levels. Exports to Russia fell from nearly 20 per cent before 2014 to around 5 per cent of total exports in 2023, marking the steepest decline in Russia's market share of exports among the Baltic states. Despite most exports having been redirected to the EU, Lithuania's share of global exports fell.

Unemployment stood at 8.2 per cent in mid-2024, and significant skill mismatches persist. The general government deficit is expected to widen to 1.6 per cent of GDP in 2024, driven by increased social spending and defence outlays. As financing conditions ease, GDP growth is projected to reach 2.3 per cent in 2024 and 2.5 per cent in 2025.

Poland

Household spending is propelling a strong rebound in Poland's economy. The economy grew at the rate of 0.2 per cent in 2023, amidst high inflation and reduced consumer purchasing power. Growth picked up to 2.9 per cent year on year in the first half of 2024 as inflation declined and real wages increased by 12 per cent. Corporate investment remains weak, constrained by weak export conditions and high debt financing costs, but public investment is buoyant, supported by a significant rise in defence spending, which is expected to reach 4.7 per cent of GDP by 2025 and become the highest among NATO members relative to GDP. The labour market remains robust, with foreign workers playing a significant role in alleviating labour shortages. Unemployment stood at 2.9 per cent in July 2024, the second lowest in the EU after Czechia. Foreign workers, primarily from Ukraine, now make up 6.5 per cent of the total workforce. Their increased numbers contributed 2.3 percentage points to Poland's cumulative GDP growth between 2015 and 2023, according to a study by CASE, a think-tank. The September 2024 floods resulted in significant disruption to economic activity. While their exact extent remains difficult to estimate at this point, the significant floods in Poland in 1997 and 2010 resulted in an estimated damage of 2.3 and 0.9 per cent of GDP, respectively. This time, the damage is expected to be more limited, reflecting better infrastructure and crisis management by local authorities. Poland's general government deficit is projected to hit 5.7 per cent of GDP in 2024 due mainly to increased defence spending, along with rising healthcare costs and the repayment of Covid-19 bonds by the Polish Development Fund. The EU launched an excessive deficit procedure, requiring Poland to reduce its deficit to 3 per cent of GDP within the next few years. Poland is expected to receive €5 billion in grants from pre-allocated cohesion funds to finance post-flood recovery investments. Nonetheless, already stretched public finances will be further impacted. GDP growth is expected to reach 3.2 per cent in 2024 accelerating to 3.8 per cent in 2025.

Slovak Republic

After expanding by 1.6 per cent in 2023, largely due to a surge in EU-co-financed public investments, the Slovak economy grew at the rate of 2.3 per cent year on year in the first half of 2024. A strong recovery in household spending was supported by real wage increases (5.6 per cent year on year in the first quarter of 2024) amid decelerating inflation. Despite a decline in external demand for manufacturing products, the unemployment rate fell to 5.5 per cent and the employment rate reached 78.1 per cent by early 2024. The European Council has initiated an excessive deficit procedure against the Slovak Republic due to fiscal deficit reaching 4.9 per cent of GDP in 2023. Projections indicate that the deficit will remain high, reaching 5.9 per cent in 2024 and 5.4 per cent in 2025. In response, the government will need to implement fiscal consolidations, with the specifics of the adjustment plan yet to be fully detailed. While household consumption continues to drive growth, investments — especially in the automotive sector — and exports are expected to strengthen, with GDP growth forecast to reach 2.3 per cent in 2024 and 2.6 per cent in 2025.

Slovenia

Growth slowed from 2.1 per cent in 2023 to 1.4 per cent year on year in the first half of 2024 reflecting falls in investment, including inventories, and exports of services, while government spending growth accelerated to 10 per cent year on year over the same period. Sector-wise, the most notable decelerations were recorded in construction, services and industry.

After a deep fall in 2023, industrial production declined further by 3.6 per cent in the first half of 2024, reflecting weaker foreign demand, while trade in pharmaceuticals with Switzerland increased further in 2024, reaching 28 per cent of all exports and offsetting the weaknesses in trade with Germany and Italy. While inflation moderated to 0.9 per cent by August 2024, real wage growth was muted compared with most regional peers. The tight labour market poses upside risks to wage growth in the medium-term. Despite significant planned spending on post-flood reconstruction, increased taxes and lower-than-planned budget execution led to a 50 per cent decrease in the deficit in early 2024 compared with the same period of last year. The GDP growth forecast of 1.5 per cent in 2024 assumes recovery in investment. In 2025, easing conditions in the eurozone, stronger investment and rising real wages should support a pickup in growth to 2.6 per cent.

Eastern Europe and the Caucasus

Growth rates have been generally strong in the Caucasus economies, while Moldova's economic performance has remained sluggish and Ukraine continued to face severe disruption from the effects of the war. After successful disinflation efforts in the past year, inflation has ticked upwards again in some countries but remained within the central banks' target intervals. Monetary policy remained tight across the region. With the exception of Ukraine, and to some extent Moldova, fiscal deficits and public debt levels are moderate. While risks arising from the war on Ukraine remain high, regional geopolitical tensions in the Caucasus appear to be easing.

Armenia

The economy expanded at the rate of 6.5 per cent year on year in the first half of 2024, showing signs of moderation after very rapid growth in previous years. The manufacturing and construction sectors maintained their growth momentum. However, growth in the service sector subsided markedly as migration of high-skilled Russian ICT professionals waned and capital inflows significantly moderated. As a result, remittances and net export of services declined. Nonetheless, the current account deficit remained broadly stable due to the exceptional increase in exports and imports of precious stones and robust inflows of secondary income related to refugees. Despite the temporary pressure on government expenditure for accommodating refugees and strengthening national defence, the fiscal position remains stable with a moderate deficit. Meanwhile, falling food prices and a relatively higher central bank policy rate caused the inflation rate to hover around zero. Operations of the new gold mine from early 2025 give an additional boost to the medium-term economic outlook. GDP growth is expected to ease to 6.2 per cent in 2024 and 4.8 per cent in 2025. Geopolitical developments in the region continue to pose a risk to economic growth, but a possible positive outcome of the advanced peace negotiations might open a range of new growth opportunities.

Azerbaijan

Economic growth accelerated to 4.3 per cent year on year in the first half of 2024. Strong public investments and solid growth of real income supported robust growth of non-oil GDP, while the oil and gas sector benefited from increased demand in the European market. Credit growth accelerated further, to above 20 per cent, with both corporate and retail credit performing well. Inflation dropped to zero in April 2024, below the targeted interval of 4+/-2 per cent but has since rebounded to 2.7 per cent in July. The Central Bank of Azerbaijan reduced the policy rate to 7.25 per cent in May but has kept it at that level since then due to strong domestic demand. Short-term growth prospects remain positive. The production and exports of gas are projected to rise significantly in the following years, yielding stable revenue flows. At the same time, ample foreign reserves will continue to support public infrastructure investments. GDP is forecast to increase by 3.8 per cent in 2024 and 2.7 per cent in 2025. Fluctuating oil and gas prices and regional geopolitical developments remain the main risks that can affect the forecast in both directions.

Georgia

Robust economic growth continued, at 9.1 per cent year on year, in the first half of 2024, mainly driven by ICT, financial services, construction and transport sectors. However, growth in these sectors has decelerated as financial inflows linked to the war on Ukraine have diminished alongside reduced migration from Russia. Meanwhile, the contribution of domestic consumption to GDP growth increased. Net exports of services growth moderated and net inflows of money transfers fell. However, the exchange rate of the lari against the US dollar remained stable due to foreign exchange intervention of the National Bank of Georgia (NBG) during recent domestic political tensions, albeit at the expense of a reduction in the level of foreign reserves. Tourist inflows from Russia fell, but an increasing number of tourists from EU countries and Türkiye sustained revenues in this important sector. Annual inflation dropped sharply in 2023 and eased further to 1.0 per cent in August 2024. The NBG responded to falling inflation with policy rate cuts, to 8 per cent in May 2024. Monetary easing has been cautious amidst increasing mortgage and corporate lending and strong domestic demand. GDP growth is forecast to reach 6.5 per cent in 2024 and moderate to 4.6 per cent in 2025. However, possible political tensions around the time of the October 2024 elections and uncertain regional geopolitical developments remain major risk factors.

Moldova

Against the backdrop of the launch of the EU accession negotiations in June 2024, the economic recovery continued at a moderate pace. GDP growth stood at 2.2 per cent year on year in the first half of 2024, supported mainly by agriculture, manufacturing and ICT services. Falling inflation and rising real wages boosted private consumption while investment grew due to improving economic prospects. Annual inflation dropped to 4.8 per cent in July 2024 due to falling energy prices, prompting the National Bank of Moldova to cut the policy rate to 3.6 per cent in May 2024. Foreign financing remained robust, covering the balance of payments gap and supporting the exchange rate. Energy security has been strengthened by newly built interconnectors that enable gas and electricity supply from Romania. Emigration of young people to EU countries continued, raising concerns over a shortage of high-skilled labour. GDP growth is projected at 3.2 per cent in 2024 and 3.5 per cent in 2025. The expiration of the gas transit agreement through Ukraine at the end of 2024 poses significant risks to energy supply and growth. Progress with EU accession, on the other hand, has the potential to improve the business environment and attract investments.

Ukraine

A new wave of heavy destruction of electricity generation and transmission capacities in the context of the war on Ukraine has interrupted four quarters of solid GDP growth. The economy grew by an estimated 6.5 per cent year on year in the first quarter of 2024 but slowed down afterwards because of electricity shortages and higher costs of imported electricity. After a few months of delay, sufficient external financing was eventually secured for the whole of 2024. However, the underlying uncertainty associated with the delay negatively affected the exchange rate, and the hryvna has lost around 10 per cent against the US dollar since the move from a fixed exchange rate to a managed float at the beginning of October 2023. Inflation had stabilised below the 5 +/- 1 per cent target in the first half of the year, before reaching 5.8 per cent in July 2024. Therefore, monetary policy relaxation was paused by the central bank after seven policy rate cuts in the period from July 2023 to June 2024, when the rate was reduced from 25 to 13 per cent. Short-term growth prospects remain highly uncertain. Improved export prospects, boosted by the Black Sea corridor along the coastline, could be outweighed by electricity shortages. While external financing is fully provided for this year it remains uncertain for 2025. Labour shortages remain acute and the risk of additional destruction of infrastructure and productive capacity is ever-present. Amidst all these risks, GDP is forecast to grow by 3 per cent in 2024 and 4.7 per cent in 2025.

South-eastern EU

The south-eastern EU region is facing weak external demand while domestic consumption has been resilient on the back of strong real wage growth. In Bulgaria and Romania, rising minimum wages have stimulated demand but also resulted in a wider trade deficit and added to inflationary pressures. Tourist receipts growth accelerated in Greece. Fiscal positions continued to deteriorate amid significant spending increases, including capital spending. At the same time, utilisation of EU funding in both countries has stagnated amid slow implementation of the Recovery and Resilience Facility (RRF), while Greece remains among the frontrunners in this regard.

Bulgaria

After slowing to 1.8 per cent in 2023, GDP growth reached 2.1 per cent in year on year in the first half of 2024, driven by domestic demand. Real wage growth averaged 14 per cent in the first semester, driven by a 20 per cent minimum wage increase, which translated into resilient private consumption. Growing incomes, lack of investment opportunities and low interest costs led to strong investment in construction, especially in the capital, Sofia. This is reflected in the structure of loans, as households increasingly take on mortgage loans motivated by low interest rates and euro adoption expectations. Meanwhile, inflation has stabilised at around 2.8 per cent. On the downside, weak foreign demand translated into sluggish industrial output growth. The fiscal policy stance has been slightly expansionary, with a targeted deficit of 3 per cent of GDP in 2024. GDP is expected to expand by 2.2 per cent in 2024 as export demand will likely remain weak. Heading into 2025, the economy is forecast to grow by 2.9 per cent, albeit with downside risks related to the political situation and delays in EU funds absorption.

Greece

The economic performance of Greece has remained robust in 2024 as GDP rose by 2.1 per cent year on year in the first quarter and 2.3 per cent in the second quarter, boosted by private consumption and gross fixed capital formation. The country is also on track for another strong tourist season in 2024, possibly exceeding the record numbers of last year. Tourist arrivals rose by 15.5 per cent in the first half of 2024, compared with the corresponding period in 2023. Labour market conditions also continued improving in the first half of 2024 as the unemployment rate reached a 15-year low of 9.6 per cent in June 2024 (seasonally adjusted estimate). The budget, which returned to primary surpluses in 2023, recorded a surplus of 0.9 per cent of GDP in the first five months of 2024, slightly higher than the 0.6 per cent in the same period last year, due to higher tax revenues. At 161.9 per cent of GDP at end-2023, public debt remains the highest in Europe (as a per cent of GDP), but the ratio fell further in 2023 due to high nominal GDP growth and primary fiscal surplus. Inflation dropped further in the first six months of 2024 (to 3 per cent year on year on average, using the HCIP measure), but core inflation remained relatively high and persistent (3.3 per cent in June 2024). Good progress has been made in implementing projects funded by the Recovery and Resilience Facility (RRF), mitigating the downside risks coming from global and regional turbulence, weaknesses in key export markets, as well as climate-related disasters. By July 2024, Greece had received €14.9 billion from the RRF (41 per cent out of the total allocated amount of €36 billion), being above the EU average in terms of absorption. Hence, the overall short-term macroeconomic outlook remains positive, with growth forecast to pick up to 2.4 per cent in in 2024 and 2.6 per cent in 2025.

Romania

In the context of weaker foreign demand, growth slowed down to 2.1 per cent in 2023 and further to 1.3 per cent year on year in the first half of 2024. The ICT sector also slowed down significantly, in line with global trends, while industrial production stagnated. Infrastructure investment, on the other hand, continued to support growth. Inflation has proved sticky amid strong real wage growth (averaging 7.4 per cent, the highest since 2019) and pension increases. The (harmonised) inflation of 5.8 per cent was the highest in the EU in July 2024. On balance, the central bank cut the policy rate twice in summer 2024, to 6.5 per cent, while ample interbank liquidity kept market borrowing rates below the policy rate. Fiscal policy continues to be expansionary, with the half-year deficit at around 3.6 per cent of GDP, higher than in the three previous years. While revenues performed well in the first six months following the tax package announced towards the end of 2023, spending has surged, as capital expenses, salaries and spending on goods and services all increased by over 20 per cent year on year. The most recent estimates by the Fiscal Council see the deficit soaring towards 8 per cent of GDP in 2024. The Romanian economy is expected to grow by 1.4 per cent in 2024 and 2.6 per cent in 2025, on the assumption that some rebound will take place already in the second half of 2024 notwithstanding the need for fiscal consolidation. Delayed EU funds absorption is a risk to the outlook.

Southern and eastern Mediterranean

The southern and eastern Mediterranean region has shown mixed economic performance amid ongoing regional droughts and geopolitical tensions. Inflation has moderated across the region, most notably in Egypt as foreign exchange issues were gradually resolved. Egypt, Jordan and Morocco continue to pursue fiscal consolidation and structural reforms, supported by IMF programmes. Egypt's growth decelerated in 2023 and early 2024, despite a notable improvement in its external accounts following significant support from international partners and the IMF. Growth in Jordan and Morocco has dipped in 2024 following a robust performance in 2023 while Tunisia saw a modest uptick in the first months of 2024 following near-zero growth in the preceding year. Lebanon continued to struggle with severe external and domestic political and macroeconomic challenges. The region's average growth is forecast to reach 2.8 per cent in 2024 and 3.9 per cent in 2025 as regional stability improves. Significant downside risks remain, including potential escalation of regional tensions, policy regression and climate shocks.

Egypt

Economic growth slowed to 2.9 per cent in 2023, from 4.2 per cent the year before, and 2.2 per cent year on year in the first quarter of 2024, driven by an acute foreign exchange shortage and weak investor confidence. Growth in the retail and wholesale trade, agriculture, communications and real estate sectors counterbalanced sharp contractions in the gas and non-oil manufacturing industries. Inflation remains high but is moderating, having fallen to 25.7 per cent in July 2024 from a peak of 38 per cent in September 2023. The budget deficit stood at 3.6 per cent of GDP in FY24 (fiscal year ending June) and the debt-to-GDP ratio is expected to fall to 83 per cent in FY25. External accounts have recovered since the devaluation of the exchange rate in March 2024, supported by FDI inflows related to the Ras al Hekma deal (US$ 24 billion) and portfolio flows of over US$ 23 billion. Reserves rose to US$ 46.6 billion in August 2024, their highest level in five years covering around 7.4 months of imports. To rein in public investment, the government announced a budgetary limit of EGP 1 trillion (US$ 21 billion) in the FY25 budget. Private investment has been sluggish but recent indicators suggest a pickup in activity. Growth is forecast to rise slightly to 3.2 per cent in 2024 as the economy adjusts from the crisis period, rising to 4.5 per cent in 2025 (and corresponding to 4 per cent in FY25). Downside risks relate to continued disruptions in the energy and electricity sectors and delays in implementing structural reforms under the IMF programme.

Jordan

In 2023, economic growth remained robust at 2.7 per cent despite difficulties caused by regional instability, but these headwinds weighed on growth in the first quarter of 2024 as private consumption became muted and tourism and foreign investment inflows decreased. In parallel, unemployment remained high at 21.4 per cent in the second quarter of 2024, and significantly higher for women (34.7 per cent) and youth (43.7 per cent). Inflation remained moderate despite a slight pick up during the year to 1.9 per cent in July 2024. The Central Bank of Jordan maintained a stable policy interest rate between July 2023 and August 2024, mirroring the decisions of the Federal Reserve as part of its effort to preserve the currency peg. Spillovers from a prolonged war in Gaza are weighing on performance in 2024, slowing down growth for the year as a whole to a forecast 2.2 per cent, particularly through suppressed tourism and investment flows and with consumers holding back on large expenditures in times of increased uncertainty. A slight uptick in growth to 2.6 per cent is projected for 2025, provided geopolitical conditions improve. However, Jordan's heavy reliance on imports makes it vulnerable to geopolitical instability in the region, as well as to shocks in energy and food prices and disruptions in global supply chains. Leveraging the country's medium-term growth potential will depend on the successful implementation of announced reforms under the government's "Economic modernisation vision" aimed to attract foreign direct investment and promote new growth drivers.

Lebanon

Economic growth remained out of reach in Lebanon during 2023 as tensions in the south of the country weighed down considerably on the economy, while the political impasse and stagnant progress on critical reforms continued to hold back recovery. GDP is estimated to have contracted by -0.2 per cent during 2023, adding to a more than 40 per cent cumulative loss in GDP since 2018. Lower commodity prices and growing remittances and tourism flows in the first nine months of 2023 helped reduce pressure on the current account, but foreign exchange reserves decreased slightly as of December 2023 to US$ 14.5 billion. Exchange rate volatility eased as Lebanon's Central Bank (BDL) introduced several measures to unify the multiple exchange rates in the economy. This was further helped by the adoption of the 2024 budget law which aligns the exchange rate closer to the prevailing market rate and stabilises it at around 89,700 pounds per US dollar since August 2023. As a result, inflation dropped significantly to 35.4 per cent in July 2024, helped in part by easing energy and food prices. Meanwhile, dire economic conditions and years of very high inflation drove large segments of the population into poverty, with over a third of the labour force being unemployed, and over 80 per cent of the population estimated to live in poverty. GDP is expected to contract again by 1 per cent in 2024, amid rising geopolitical risks, political inaction, and stalled reforms. Growth could return to a forecast 2 per cent in 2025, provided regional tensions subside with some progress on reforms and an IMF programme in place.

Morocco

GDP growth recovered to 3.4 per cent in 2023, before decelerating to 2.7 per cent year on year in the first half of 2024. Despite robust tourism and manufacturing activities, the severe drought and consequent agricultural contraction weighed on growth. Meanwhile, inflation continued to ease, reaching 1.3 per cent in July 2024, supported by lower food and energy prices. The government is pursuing a path of gradual fiscal consolidation, which narrowed the deficit to 4.3 per cent of GDP and stabilised public debt at around 70 per cent of GDP in 2023, thanks to higher tax revenues and lower subsidies, despite the rise in external debt servicing costs. The current account deficit narrowed on the back of lower imports and the stronger performance of tourism, remittances, and automotive and electric exports. Growth is projected at 2.9 per cent in 2024, rising to 3.6 per cent in 2025. While unfavourable weather conditions are expected to weigh on economic activity this year, the recovery in the manufacturing and tourism sectors, supported by a pick-up in exports and domestic demand, should provide some breathing space. Downside risks relate to Morocco's high dependence on energy imports and seasonal agricultural production, which make the economy vulnerable to climate and external shocks.

Tunisia

Following a slowdown to almost zero per cent growth in 2023, GDP grew by 0.6 per cent year on year in the first half of 2024. Although there was a contraction in agriculture (due to severe drought) and mining, expansion occurred in the tourism, financial services and some industrial sectors. Growth was supported by recovering exports (including of olive oil, mechanical and electrical goods) and domestic demand amid easing inflation (which dropped to a 30-month low of 7 per cent in July 2024). The budget deficit in 2023 narrowed to 7.1 per cent of GDP, as tax revenues increased and basic goods subsidies decreased (due to lower food prices), despite an increase in interest payments and wages. Nevertheless, public finances remained constrained, with public debt standing at 80 per cent of GDP. On the external side, the current account deficit narrowed, supported by stronger remittances, tourism receipts and lower imports. Moody's upgraded Tunisia's outlook to stable from negative in March 2024 as the country was able to maintain access to some bilateral and multilateral external funding, despite the slow progress on the IMF-supported programme. Growth is forecast to remain modest in the short term at 1.2 per cent in 2024 and 1.8 per cent in 2025, supported by lower inflation, a strong current account, and continued reform efforts. Significant downside risks include the limited fiscal space, large external debt and the economy's vulnerability to external and climate shocks.

Türkiye

2023 marked the return to more orthodox economic policy. Since June 2023 monetary and fiscal policies have been tightened with the objective of bringing inflation down. The authorities have persevered with further tightening this year, despite the local elections of March 2024, a move welcomed by investors. After hiking the policy rate by a cumulative 4,150 basis points between June 2023 and March 2024, the Central Bank of the Republic of Türkiye held the rate at 50 per cent, used sterilisation tools to tighten the monetary stance further and enhanced the monetary policy transmission by implementing macroprudential measures. Through the public savings and efficiency package announced in May 2024, the Ministry of Treasury and Finance tightened the fiscal stance, except for earthquake-related expenditures, to support disinflation and reduce the fiscal deficit, which widened in 2023 and the first half of 2024. In addition, the authorities refrained from implementing an interim hike in the minimum wage in July 2024, after two years of semi-annual hikes, to help anchor inflation expectations.

The return to orthodoxy, coupled with Türkiye's removal from the Financial Action Task Force (FATF) grey list in June 2024, helped improve investor confidence. Türkiye's CDS premium declined significantly from its peak of more than 700 basis points in May 2023 to below 300 basis points, sovereign eurobonds were issued at favourable terms, and more major rating agencies upgraded Türkiye's sovereign ratings. At the same time, the FX-protected deposits (KKM) continued to decline, from a peak of TRY 3,408 billion (US$ 120 billion) in August 2023 (45 per cent of the total Turkish lira deposits at banks and 26 per cent of total bank deposits) to TRY 1,575 billion (US$ 46.4 billion) in September 2024 (less than 15 per cent of Turkish lira deposits and 10 per cent of total deposits).

The external position has also improved. The 12-month cumulative current account deficit declined steadily to US$ 19.1 billion in July 2024, from the peak of US$ 57 billion in May 2023, driven by lower imports of goods due to weaker domestic demand and constrained consumer lending, and stronger exports of services, particularly record tourism receipts. Meanwhile, capital flows accelerated, with the 12-month cumulative net portfolio flow reaching US$ 24 billion in July 2024, but foreign direct investment remains low, at US$ 10.7 billion in July 2024 (12-month cumulative inflows), equivalent to less than 1 per cent of GDP. On balance, the level of foreign exchange reserves improved substantially, from US$ 97.1 billion in May 2023 to US$ 147.9 billion in July 2024. Notably, net reserves (excluding currency swaps) turned positive for the first time since March 2020. Simultaneously, short-term external debt, categorised by remaining maturities of one year or less, increased to US$ 236.6 billion in June 2024, equivalent to 20 per cent of GDP.

Meanwhile, the tighter policies caused a deceleration in growth and a rebalancing in its drivers. The economy grew by 3.8 per cent year on year in the first half of 2024, down from 4.6 per cent in the same period of 2023, and the growth rate in the second quarter (2.5 per cent year on year) was the lowest since the pandemic. The services sector (trade, logistics, and tourism) remained strong and post-earthquake rebuilding continued to sustain the construction sector. Meanwhile, the manufacturing sector started recovering in the first quarter, reflecting renewed confidence from investors, but contracted in the second quarter, while growth in the financial services sector slowed. On the demand side, private consumption decelerated but remained the main driver of growth. At the same time, investment picked up, and the contribution of net exports turned positive, with exports increasing to a recovering Europe (Türkiye’s main trading partner).

After peaking at 75.4 per cent in May 2024, annual inflation decelerated to 52 per cent in August. It averaged 65.9 per cent in the first eight months of 2024. Still-high inflation reinforces the need to keep the monetary stance tight, or tighten it further, to anchor inflation expectations, meet the revised end-2024 inflation target of 41.5 per cent and maintain a positive real interest rate.

Economic growth is forecast to decline to 2.7 per cent in 2024 before picking up to 3 per cent in 2025, as the tighter policy stance cools down the economy and weakens private consumption growth. Key downside risks include persistently high inflation, the impact of the real appreciation of the Turkish lira on exports and tourism, high geopolitical tensions in the region, and tight global financing conditions given the high short-term external financing needs.

Western Balkans

Growth accelerated markedly in all Western Balkans countries at the beginning of 2024, from 2.5 per cent in 2023 on average to around 4 per cent year on year in the first quarter of 2024. This surge was mainly driven by private consumption boosted by easing inflation and rising wages, as well as a rise in capital investments throughout the region. On the other hand, external demand and goods exports have remained weak. Tourism has stayed strong, especially in Albania and Kosovo (mainly related to diaspora tourism from Western Europe), and to a lesser extent in Montenegro. Average inflation fell from double-digit levels in 2023 to within the target band in most countries, allowing the gradual easing of monetary conditions, although the policy rates have remained elevated. Overall, growth in 2024 is expected to be higher than in 2023, but somewhat lower than in the first quarter of 2024, as the low base and one-off effects fade. Further acceleration is expected in the medium term, close to the potential growth of around 4 per cent, but risks are slightly to the downside, arising from geopolitical uncertainty, and adverse climate change effects to which the region is highly susceptible. With surging public investments and much-needed reforms across the region, Western Balkans countries had to tap more external (IFI and financial market) financing, with three economies (Serbia, North Macedonia and Kosovo) still having IMF arrangements.

Albania

Growth accelerated to 3.6 per cent year on year in the first quarter of 2024 (from 3.4 per cent in 2023). Growth in the first quarter was driven by services and construction, while industrial and agricultural production declined. This is reflected on the expenditure side, where private consumption and public investment recorded strong growth, but net exports contracted due to a 30 per cent fall in goods exports, hampered by appreciation of the Albanian lek and weak external demand. As a result, the current account deficit expanded, reaching 7 per cent of GDP, despite the increase in remittance inflows. Inflation is on a declining trend and within the central bank's target band, at 2.1 per cent in July 2024, helped by the high base in the first half of 2023 and the currency appreciation. The Bank of Albania loosened its monetary policy slightly, cutting the policy rate by 25 basis points (to 3 per cent) in July 2024, after two years of rate hikes. The Albanian lek has been stable in the past few months, after an appreciation of 12.5 per cent in 2022-2023, partially due to central bank interventions in the market. The financial sector remained stable in the first half of 2024, with sufficient liquidity, stable profitability, and accelerating credit activity. Growth is forecast at 3.5 per cent in 2024 and 3.7 per cent in 2025, but with downward risks from droughts hampering electricity and agricultural production. On the positive side, faster implementation of structural reforms, supported by the European Union's Growth Plan for the Western Balkans, could boost growth.

Bosnia and Herzegovina

Following a slowdown to 1.7 per cent in 2023, growth picked up to 2.7 per cent year on year in the first quarter of 2024 on the back of a strong rise in fixed investments (close to 50 per cent) as well as a robust increase in private consumption due to easing inflation and growing remittance inflows. The contribution of net exports was negative due to a sharp rise in goods imports, and a simultaneous double-digit decline in exports, which were hampered by subdued external demand. On the production side, growth was underpinned by services and construction, with a decline in industrial production. The current account deficit expanded significantly compared with the first quarter of the previous year, reaching €460 million (7.5 per cent of GDP), but, on a positive note, FDI inflows continued to grow, reaching €260 million in the first quarter. Inflation declined to 2 per cent in the first half of 2024, driven by global disinflation. Fiscal policy was expansionary in 2023, yielding a general government deficit of around 1.7 per cent of GDP, after several years of surpluses. It is expected to stay on a similar course in 2024, with the deficit increasing further due to the accumulated impact of several permanent increases of public wages and social benefits. Public debt is still relatively low, and considered sustainable by the IMF, though it is significantly higher in the Republika Srpska entity, reflecting continued growth in current expenditures and capital spending. Growth is forecast at 2.8 per cent in 2024, accelerating to 3 per cent in 2025. Downside risks arise from the lack of coordination between the entities impeding structural reforms and implementation of major capital investments. On the positive side, the country's EU candidacy status might accelerate reforms.

Kosovo

After reaching 3.3 per cent in 2023, economic growth accelerated further to 5.6 per cent year on year in the first quarter of 2024 on the back of strong private consumption and investment, while the contribution of net exports remained negative due to higher imports. The current account deficit narrowed slightly compared with the first quarter of 2023 due to high services exports. FDI inflows continued in the first quarter of 2024 at around 9 per cent of GDP. Inflation peaked at 14.2 per cent year on year in July 2022 but has gradually decelerated since then, reaching 2.2 per cent in July 2024. Despite an increase in capital expenditures and wages as well as other fiscal measures introduced in 2023 to tackle inflation, the general government deficit reached only 0.25

per cent of GDP (far below expected), due to a sharp rise in revenues. This allows for a moderate fiscal expansion in 2024, while the low public debt level (at 17 per cent of GDP) provides ample room for much-needed public investments. The second review under the Stand-by Agreement and the Resilience and Sustainability Facility arrangements with the IMF was completed in June 2024, unlocking access to another €25 million for precautionary purposes and climate change adjustment projects. Growth is forecast to accelerate to 4 per cent in 2024, in line with the strong start of the year, and stay at that rate in 2025. However, the near-term outlook is subject to downside risks arising from prevailing geopolitical uncertainties which may affect trade flows and the availability of international (including EU) funding. Upside risks, on the other hand, arise from the potential acceleration of structural reforms and additional financing under the Growth Plan, if the necessary pre-conditions are met.

Montenegro

After reaching 6.4 per cent in 2022 and 6 per cent in 2023, growth moderated to 4.4 per cent year on year in the first quarter of 2024, driven by services and industrial production. This was reflected on the expenditure side by private consumption and fixed investments providing the highest contributions. Net exports contracted due to the decline in tourism exports, after a record 2023, as the surge of tourists and immigrants from Russia and Ukraine ended, though a recovery in tourism was evident in the second quarter. Consumption has stayed strong, with retail trade growing at 6.5 per cent year on year in the first half of the year, boosted by easing inflation and rising real wages and pensions. The current account deficit expanded by €170 million compared with the first quarter of 2023, reaching €435 million or 32.1 per cent of GDP. Net FDI inflows in the first five months increased by 9.1 per cent compared with the same period of 2023. Inflation declined significantly from its peak of 17.5 per cent in November 2022, to 3.5 per cent in July 2024. Nevertheless, the government introduced a new set of margin caps on essential products to moderate price rises further. Another set of wage increases for this year, and further pension rise for the start of 2025 were announced as part of the Europe Now 2.0 programme. Growth is projected to reach 3.8 per cent in 2024 as the growth of tourist inflow moderates. A further slowdown to 2.9 per cent is forecast for 2025 as the long rehabilitation of the Pljevlja thermal power plant, which currently supplies around 40 per cent of the country's electricity, is expected to lead to a decline in electricity production and an increase in energy imports.

North Macedonia

Economic growth was low in the past two years, with only 1 per cent recorded in 2023, and a modest acceleration is expected for 2024. Growth in the first quarter picked up slightly to 1.2 per cent year on year, driven by services and private consumption, supported by easing inflation and rising credit activity. On the other hand, the output/value added of industrial sectors and exports of goods declined, in line with sluggish demand from major trading partners. This resulted in the current account switching from a surplus in 2023 to a deficit of 1.3 per cent of GDP (€185 million) in the first quarter of 2024. On a positive note, FDI inflows remained strong at 1.6 per cent of GDP in the first quarter of 2024, sufficient to cover the current account deficit. After reaching the highest level in the region, inflation dipped below 3 per cent in July 2024, but monetary policy remains tight, with the policy rate held at 6.3 per cent since September 2023. Despite the high policy rate, credit activity continued to grow at a similar pace as in 2023, and the financial sector has stayed stable and profitable. Fiscal policy has remained expansionary, with an increased deficit target of 4.9 per cent of GDP for this year, due to elevated current and capital expenditures. Public debt is also expected to increase. The government has already issued domestic debt of around €800 million since the beginning of the year and reached a bilateral agreement with Hungary for a loan of €1 billion, half of which is to be used this year. Growth is expected to accelerate to 2.2 per cent this year and to 3.5 per cent in 2025, on the back of recovering external demand and ambitious investment projects. Downside risks arise from the tight fiscal space and weaker demand from the main export partners.

Serbia

GDP growth picked up significantly to 4.3 per cent year on year in the first half of 2024 from 2.5 per cent in 2022 and 2023. The acceleration was driven by services, predominantly trade, tourism and catering, and construction. On the expenditure side, household consumption and fixed investments provided the strongest impetus, while net exports had a negative contribution due to higher services imports, particularly related to tourism and transport, in line with easing inflation and the recovery of domestic demand. The current account deficit doubled compared with the first half of 2023, reaching over €1.2 billion (3.3 per cent of GDP), driven by high imports, dividend outflows and lower incoming government transfers from abroad. Net FDI inflows remained at the same level as in the first half of 2023 (at €2 billion). Inflation has stayed elevated compared with the rest of the region, at 4.3 per cent in July 2024, driven by core inflationary pressures. However, the policy rate was cut twice in recent months from its peak of 6.5 per cent to 6 per cent in July 2024. The fiscal stance remained expansionary, with a further rise in public wages and pensions announced for this year. Credit growth was modest, at 2 per cent year on year in the first half of the year but accelerated in the last two months. Growth is expected to reach 3.8 per cent in 2024 on the back of strong performance in the first half of 2024 as well as expansionary fiscal and monetary policy boosting consumption and capital investment. In 2025, growth is forecast to accelerate to 4 per cent but tight labour markets, geopolitical instability and adverse weather conditions constitute downside risks. On the other hand, successful implementation of reforms in the area of governance of state-owned enterprises as well as carefully planned and executed public investments may boost growth.

Belarus

GDP growth accelerated to 5 per cent in the first half of 2024 amid the growing dependency on the Russian economy. Adapting to the heavy sanctions, manufacturing, construction and trade recorded strong recoveries while agriculture saw robust growth after an underwhelming performance in the previous year. In contrast, performance in the information and telecommunication services, once a fast-growing flagship sector, remains lacklustre in the new environment after a large drop in the last two years. Exports and imports are also struggling owing to lost markets and logistical disruptions. Inflation rose again at the end of 2023 and is currently around 6 per cent. The central bank’s policy rate has remained at 9.5 per cent since the last reduction in June 2023. The exchange rate and foreign reserves have been broadly stable. The authorities continue with import substitution policies and investments in alternative export routes through Russian ports. However, these routes are costlier, and their full development will take several years. GDP is forecast to grow by 4.2 per cent in 2024 and 2.5 per cent in 2025, with high downside risks to the outlook.

Russia

Economic activity in Russia in the first half of 2024 grew at the rate of 4.7 per cent year on year, exceeding expectations, up from 1.8 per cent year on year in the same period of 2023, according to Rosstat. Growth was stronger in the first quarter (5.4 per cent year on year) but slowed down somewhat in the second quarter (4.1 per cent year on year), suggesting the economy may be cooling down. Growth was mostly driven by trade with China and a number of other economies, financial and ICT services and a manufacturing boom on the back of increased military spending. On the demand side, growth was driven by private consumption, investment and a rebound in net exports. Private consumption was supported by increased consumer confidence, subsidised lending, and gains in real wages, as higher military-related public expenditures resulted in higher wages in both the defence and non-defence sectors, while also exacerbating labour shortages. Investment has been further sustained by import substitution and local companies replacing western firms which exited Russia. Meanwhile, the contribution of net exports turned positive for the first time since the second quarter of 2022, primarily driven by a decline in imports of goods because of sanctions and difficulties in settling payments with foreign banks. At the same time, this led to a rise in the current account surplus, which increased from US$ 29 billion in the first 8 months of 2023 to US$ 40.5 billion in the same period of 2024. This was also the result of the decline in the deficit of the primary and secondary income balance, because of lower participation by non-residents in Russian companies' equity, lower dividends accrued to non-residents and lower outward remittances. Meanwhile, the rouble appreciated by 16 per cent against the U.S. dollar since October 2023, despite sanctions on the Moscow Exchange (MOEX), which disrupted the foreign exchange markets and led to the emergence of multiple exchange rates.

Labour shortages and the fiscal stimulus deployed ahead of the March 2024 elections resulted in an increase in inflation, which averaged 8.2 per cent year on year in the first 8 months of 2024, rising to 9.1 per cent year on year in July and August, and is likely yet to peak. Moreover, inflation was fuelled by both demand-side pressures and supply-side shortages, as the economy is operating close to full capacity and imports are constrained. To tame inflation, the Central Bank of Russia (CBR) hiked the policy rate by a total of 300 basis points in July-August 2024, to 19 per cent, following five earlier hikes between July 2023 and June 2024, totalling 850 basis points. Monetary policy is expected to remain tight, and inflation is expected to exceed the CBR's end-year target of 4 per cent.

The outlook remains uncertain, with growth forecast at 3.6 per cent in 2024, before slowing down to 1.5 per cent in 2025, given the tighter monetary stance and lower fiscal stimulus. Risks are tilted to the downside, including from labour shortages experienced by several non-military sectors, the adverse impact of high inflation on gains in real income and disruptions to international payment mechanisms. Sanctions could hold back productivity and growth in the medium- to-long term, including through limiting the ability to replace lost and amortised equipment and complicating any new large-scale FDI. On the upside, military spending and production, coupled with import substitution and mechanisation in sectors suffering from labour shortages, could continue to boost growth above expectations.

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About this report

The Regional Economic Prospects report is published twice a year. The report is prepared by the Office of the Chief Economist and the Department for Policy Strategy and Delivery and contains a summary of regional economic developments and outlook, alongside the EBRD's growth forecasts for the economies where it invests. The report also touches on the economic developments in Belarus and Russia notwithstanding the fact Russia's and Belarus's access to Bank resources is suspended under Article 8.3 of the EBRD's constitution. The estimates and projections are based on statistical information available through September 18, 2024.

For more comprehensive coverage of economic policies and structural changes, see the EBRD's country strategies and updates, as well as the Transition Report 2023-24, which are all available on the Bank's website at www.ebrd.com.

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