

2. CESEE Overview: The crisis is over, but its scarring effects are hindering recovery

BY OLGA PINDYUK

- › Most CESEE economies saw lower growth in 2023 than in 2022, with consumers and industry maintaining a pessimistic outlook. Rising bankruptcy rates in industry in many countries point to structural issues exacerbated by the recent economic crisis. Only in the services sector does sentiment appear largely positive, supported by rising demand.
- › CIS and Ukraine were the only sub-regions where economic growth accelerated in 2023. The Ukrainian economy managed to grow by more than 5% year on year, owing to a significant influx of foreign aid and a remarkable degree of economic resilience; meanwhile Russia's strong result of 3.6% annual GDP growth is credited to its ability to switch the economy to war mode and circumvent Western sanctions.
- › Inflation slowed significantly in all CESEE countries, but core inflation is proving more persistent, backed by rising real wages and tight labour markets. In 2024-2026, consumer prices will decline further, as wage growth moderates and global prices remain low.
- › The use of renewables in electricity generation increased in all CESEE countries in 2023, although it remains at below the levels of Austria or Germany. Financing of the necessary investment in renewable energy in the coming years will be hampered by the narrowing fiscal space and the need to prioritise defence spending.
- › In the next three years, annual GDP growth in CESEE will be about 3%; that will allow economic convergence with the euro area, but at a relatively low speed. Growth will be driven mainly by household consumption, whereas investment will be constrained by limited access to the sources of financing and will be insufficiently high to promote a faster green and digital transition and to ensure the structural changes needed to boost the region's competitiveness.
- › Risks to the outlook remain mostly on the downside, with the most significant of these related to geopolitics. Inadequate support from the West could lead to Ukraine losing the war, which would increase the security risks for the whole of Europe. Tensions in the Middle East could cause a significant increase in global energy prices, as well as supply-chain disruptions.

2.1. CESEE COUNTRIES SAW LITTLE IMPROVEMENT IN THEIR ECONOMIC PERFORMANCE IN Q4 2023

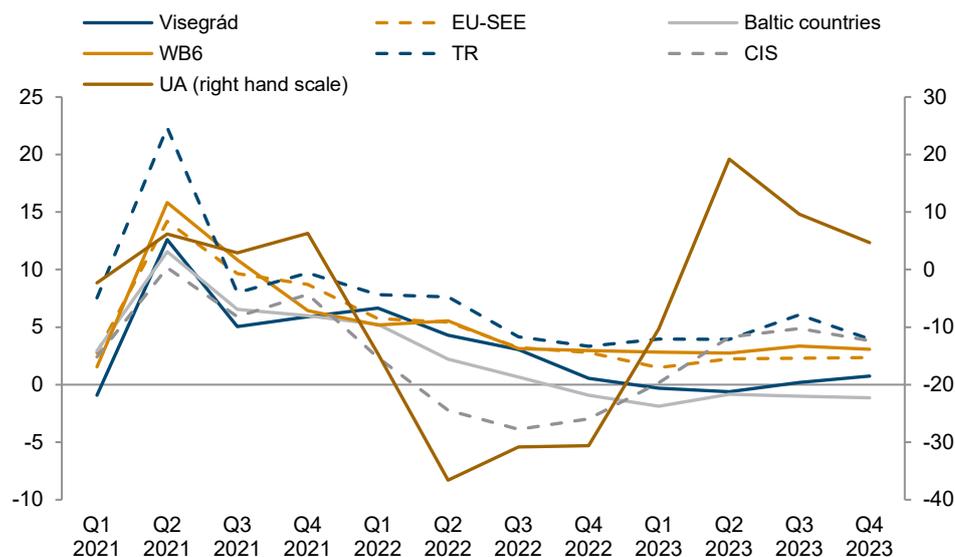
Last year was a challenging one for the CESEE region, with many economies struggling to build up a head of steam. The Baltic countries performed especially poorly (see Figure 2.1): their economies contracted throughout the year, as they continued to be those worst affected by the repercussions of Russia's war in Ukraine. The Visegrád countries, dragged down by the recession in their main export market of Germany (see Global overview), struggled to achieve a growth rate in excess of zero. Both sub-regions were also hit disproportionately hard last year by inflation, which contributed to the

weakening of their economies. Economic growth both in the Western Balkans and EU-SEE was mostly stable throughout 2023, at around 3% and 2% annual real GDP growth, respectively – a marked deceleration for these sub-regions.

Only the CIS countries and Ukraine saw a significant acceleration of economic growth in 2023 compared to the previous year. Ukraine, which lost almost a third of its economy in 2022 (partly on account of the de facto loss of some of its territory and population to Russia), was able to achieve positive economic growth during the second year of the war, thanks to a significant influx of foreign aid and a remarkable degree of economic resilience (see Ukraine report). Although there was a significant slowdown of economic growth in the second half of the year, the 4.7% growth year on year recorded in Q4 2023 was still one of the highest in the region. In the case of CIS, such growth was possible largely on account of Russia's ability to switch its economy to war mode and to circumvent most of the Western sanctions (see Russia report), but it was also helped by a steep rise in investment in Kazakhstan (see Kazakhstan report).

Figure 2.1 / Quarterly real GDP

change against preceding year, %



Note: simple average.

Source: wiiw Monthly Database incorporating national and Eurostat statistics.

In Q4 2023, GDP growth accelerated only in the Visegrád and EU-SEE countries, but then only marginally – by 0.4 and 0.1 percentage points (pp), respectively, year on year. In all other sub-regions, economic growth decelerated, with the Baltic countries being the worst performers: Latvia recorded a year-on-year decline in GDP in Q4 2023. The Western Balkan region, which succeeded in markedly speeding up economic growth in Q3 2023, experienced a deceleration of GDP growth in annual terms of 0.3 pp in the last quarter. In CIS, Moldova, which had been struggling to recover from the effects of Russia's war in Ukraine (see Moldova report), was the laggard in terms of economic growth, achieving only 0.2% year on year in Q4 2023 – a striking 3.1 pp lower than in the previous quarter.

Economic performance in the Western Balkan and EU-SEE sub-regions varied quite substantially from country to country. For EU-SEE, Croatia was something of a sub-regional champion, having seen its GDP growth boosted to 4.3% year on year in Q4 2023; its economy has benefited from a surge in tourism (helped by the country's accession to the EU's border-free Schengen zone) and the increased inflow of EU funds, which supported investment activity (see Croatia report). At the same time, GDP growth in Bulgaria, Romania and Slovenia was noticeably slower in Q4 2023 – between 1% and 2% year on year, as those countries' industries were hit by sluggish demand on their main export markets, and as inventories contracted after the completion of infrastructure projects, signalling a lack of confidence in future demand (see Bulgaria and Romania reports). In the Western Balkans, both Bosnia and Herzegovina and North Macedonia underperformed compared to their peers, achieving only 1.7% and 0.9% year-on-year economic growth in Q4 2023, respectively – versus 4% on average in the rest of the sub-region. Here again, a decline in inventories was among the main reasons for this – likely a result of the stockpiling of gas and oil in 2022 amid the energy crisis (see North Macedonia report).

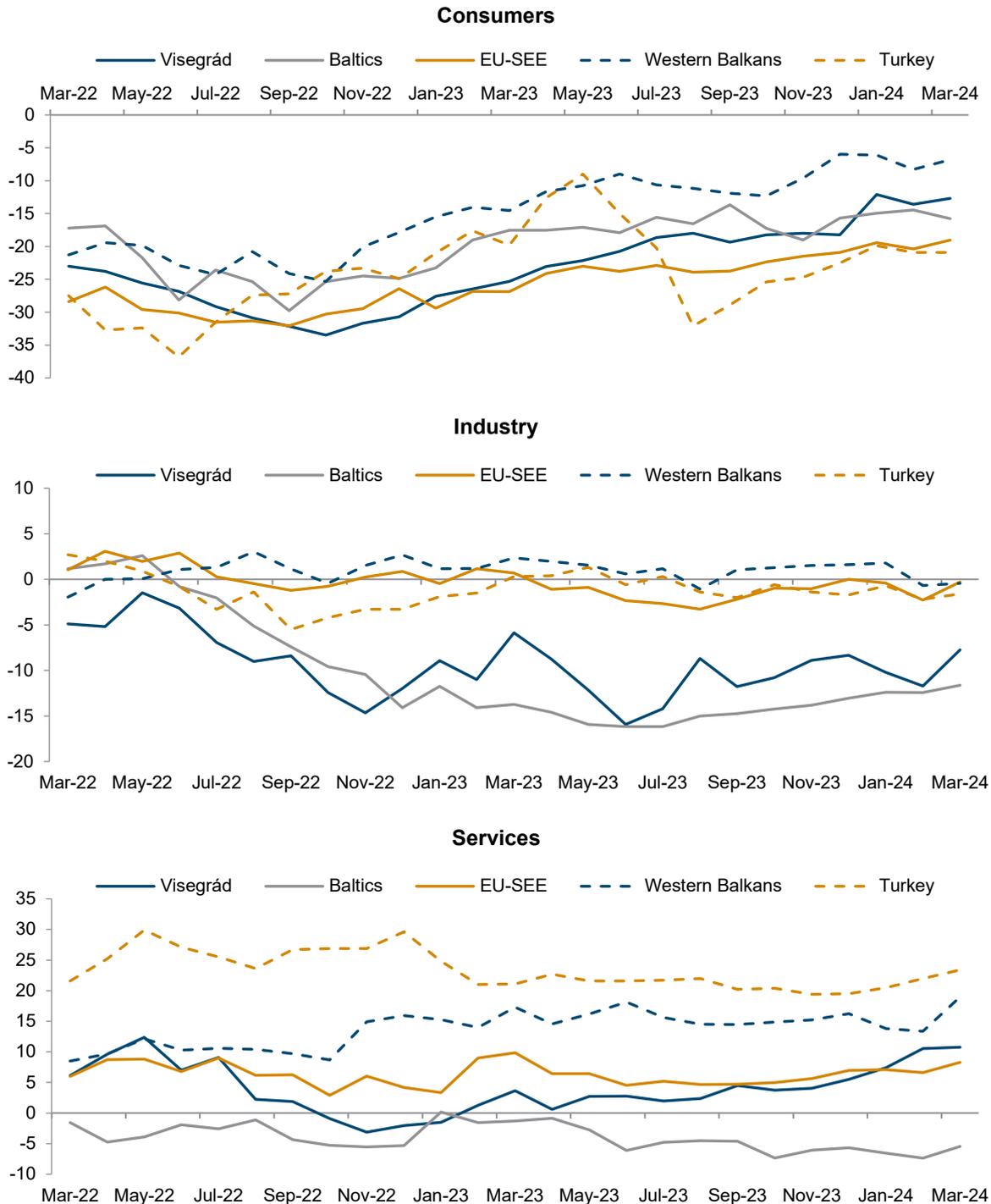
Industry and consumers both remain generally pessimistic, though consumer sentiment has been improving (Figure 2.2). In 2023, the mood of consumers remained subdued in all sub-regions, with the sentiment indicator values staying below zero. Turkey recorded the lowest values – quite likely reflecting the skyrocketing and persistent inflation, which affected the welfare of households (see Turkey report). There appears to have been some improvement in consumer sentiment in Q4 2023 to Q1 2024, most visibly in the Western Balkans and the Visegrád countries. Sentiment in industry, on the contrary, has shown no sign of recovery, with industry in the Visegrád and Baltic countries having on average far worse expectations than in EU-SEE, the Western Balkans and Turkey, where sentiment values have tended to hover around zero. Still, in all sub-regions, the sentiment expressed by industry remains less negative than that voiced by consumers: that dipped significantly deeper in 2022, as households struggled with the cost-of-living crisis, and has not recovered yet.

A striking divergence in economic sentiment developed after the start of the full-scale invasion of Ukraine by Russia, with the Western Balkans having a far more positive (or less negative) sentiment than the Visegrád and Baltic countries in all sectors of the economy. This likely reflects, on the one hand, the greater dependence of the Visegrád countries on the German economy (which was hit particularly hard by the increased energy prices) and, on the other, the greater security risks to the Baltic countries, as perceived by investors. Industry in the countries of EU-SEE maintained a better level of sentiment than the Visegrád countries on the back of robust investment, and to some extent as part of the re-shoring process.

The services sector, by contrast, exhibited overall positive sentiment in all CESEE sub-regions, apart from the Baltic countries (see Figure 2.2). Sentiment indicator values were highest in Turkey and Western Balkan countries, which tend to specialise in tourism services, which have experienced rapidly rising demand since the end of the COVID-19 pandemic. The Visegrád countries experienced a marked improvement in sentiment in the services sector in Q4 2023 to Q1 2024, pointing to a better performance in that part of the economy than in the manufacturing sector. Rising real wages in the region are likely to boost the confidence of service providers in the robustness of domestic demand – in contrast to industry, which remains much more dependent on developments on external markets.

Figure 2.2 / European Commission economic sentiment indicator, seasonally adjusted

Balance of positive over negative survey results²



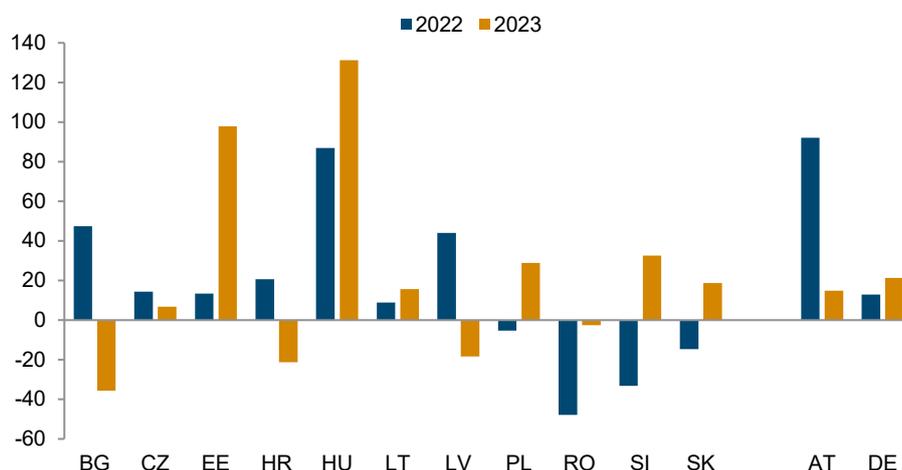
Note: Simple average of each country group. Here Western Balkans refers to just Albania, Montenegro, North Macedonia and Serbia; EU-SEE: Bulgaria, Croatia, Romania, Slovenia.
 Source: Eurostat and national statistics, own calculations.

² Numbers above 0 suggest optimism about future economic performance.

The rising bankruptcy rates in industry in many countries point to structural issues exacerbated by the recent economic crisis. Bankruptcies have been on the rise in all four Visegrád countries – together with Austria and Germany (see Figure 2.3) – driven by tightening of the financing and liquidity conditions amid rising interest rates and supply-chain disruptions. An especially high growth in bankruptcies has been observed in Hungary and Estonia – 131% and 98%, respectively, year on year in 2023. Only Bulgaria, Croatia and Romania saw bankruptcies in industry decline in 2023, which is yet further evidence that their economies are in better shape than the rest of EU-CEE. So far these trends have not caused any deterioration in the non-performing loans (NPL) situation; but in many countries, NPL ratios for corporate loans are noticeably higher than for household loans – by as much as 6.6 pp in Montenegro (where the NPL ratio for corporate loans reached 10% at the end of 2023).

Figure 2.3 / Bankruptcy declarations in industry

Average change against preceding year, %



Source: Eurostat, own calculations.

2.2. INFLATION HAS SLOWED SIGNIFICANTLY, BUT CORE INFLATION IS PROVING MORE PERSISTENT

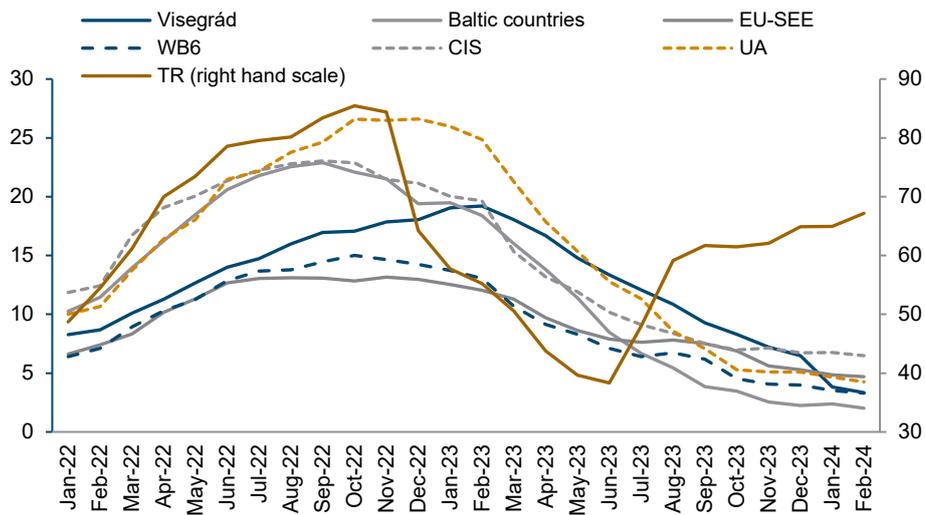
Inflation in CESEE has slowed further over the past few months everywhere, apart from Turkey and CIS (Figure 2.4). Turkey remains an outlier, with consumer prices having been trending upward since mid-2023 to reach 68.5% year on year in March 2024, driven by negative real interest rates, national currency depreciation and high import demand (see Turkey report). In CIS, inflation is highest in Kazakhstan and Russia (9.6% and 7.7%, respectively, year on year in February 2024). Yet in only a handful of countries – namely, Bosnia and Herzegovina, Czechia, Kosovo, Lithuania and Latvia – was inflation at or lower than about 2% in February 2024.

The rise in food and transport prices have decelerated significantly in line with global food and energy price trends (Figure 2.5). In Czechia, Hungary and Latvia, there was even deflation in food prices in February 2024 (partly explicable by the high comparison basis, since in February 2023 food prices in those three countries grew in the range of 18-26%), while transport prices fell in Hungary, Latvia, Poland,

Albania and Bosnia and Herzegovina. Turkey remains the only country in the region incapable of overcoming its problem of high inflation: even war-torn Ukraine has managed to curb its inflation.

Figure 2.4 / Consumer price index

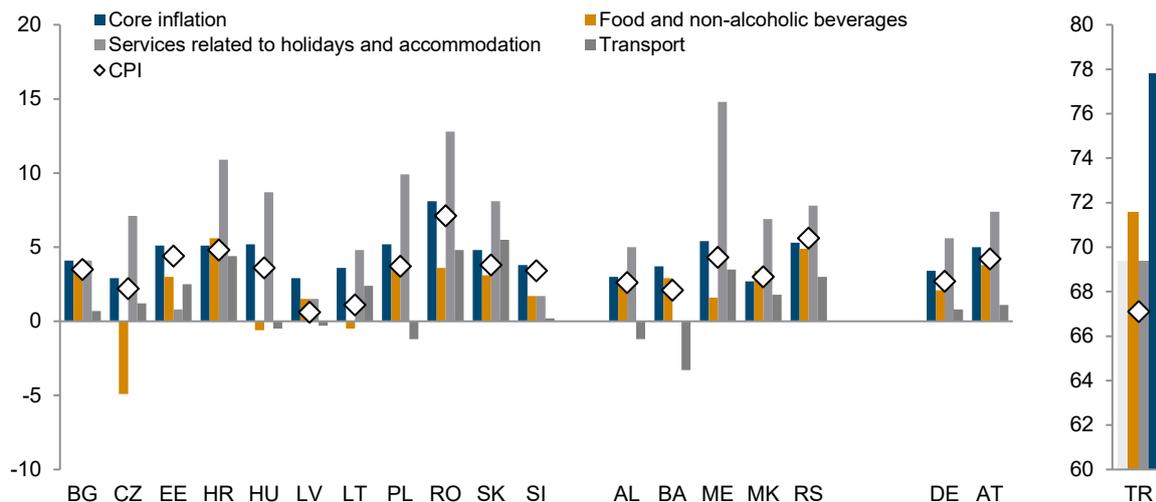
% change year on year, monthly



Note: simple average. Harmonised index of consumer prices (HICP) for EU-CEE.
Source: wiiw Monthly Database incorporating national and Eurostat statistics.

Figure 2.5 / Consumer price inflation sub-components in February 2024

percentage change year on year



Source: National sources, Eurostat, wiiw.

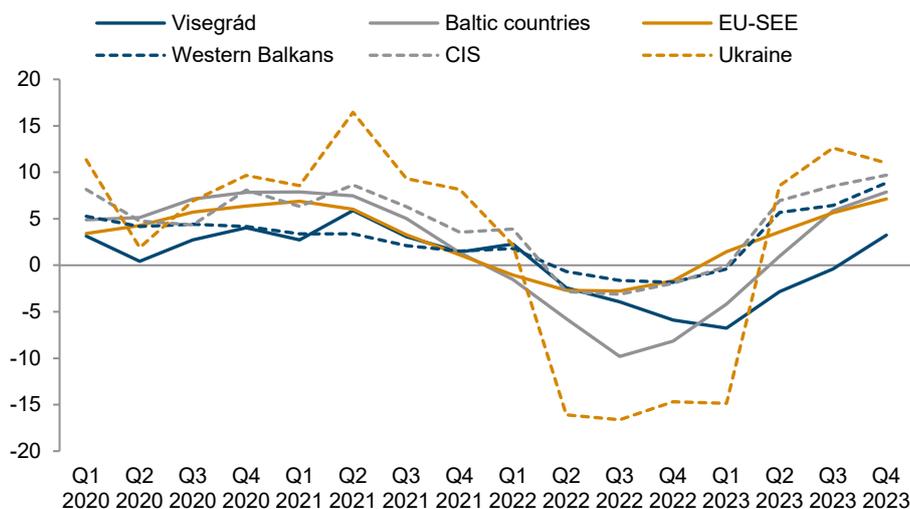
Core inflation is higher than headline inflation everywhere except for Croatia, indicating the continuing pass-through of higher production costs to prices. This is driven primarily by the cost of services, which appear to appear to be slower to respond than food or transport (see Figure 2.5).

Disregarding Turkey as an outlier, the cost of holidays and accommodation services – the fourth biggest component of the harmonised index of consumer prices – have grown fastest in Montenegro, Romania and Croatia: by 14.8%, 12.8% and 10.9%, respectively, year on year in February 2024. This is likely driven both by the rising demand for such services and by strong wage dynamics in the sector amid labour-supply constraints.

The accelerating growth of real wages appears to be one factor behind the steeply rising cost of services. Real wages picked up towards the end of 2023 in all CESEE countries (Figure 2.6) apart from Czechia, where they were still declining in Q4 2023 by 1.9% year on year. The fastest growth has been taking place in Ukraine and CIS, while the Visegrád countries had only a relatively modest increase in real wages of 3.3% year on year in Q4 2023, after six consecutive quarters of decline – likely due to high inflation eating into nominal wage growth, as well as because of the poor performance of their manufacturing sectors. In several countries – Belarus, Latvia, Moldova, North Macedonia and Ukraine – the rate of real wage growth was in double digits, which could indicate that it might take longer for core inflation there to subside.

Figure 2.6 / Real gross wages in 2020-2023, quarterly

percentage change year on year



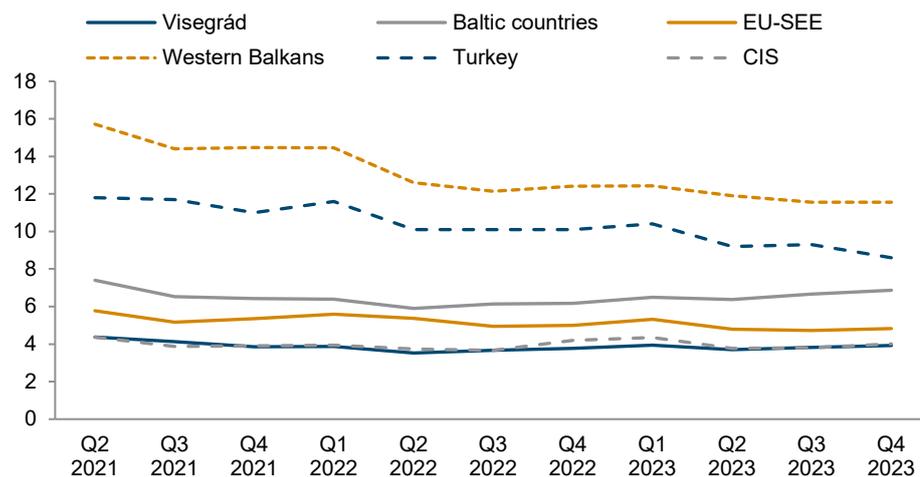
Source: wiiw Monthly Database incorporating national and Eurostat statistics.

Still, for many EU-CEE countries, real wages are much lower than at the end of 2021, and so their growth is quite welcome news for the economy. In Czechia, the decline in real wages has been the most dramatic – in Q4 2023, Czech employees were receiving wages that on average were 40% lower (in real terms) than in Q4 2021. The rate of decline in real wages was cumulatively in double digits during 2022-2023 in Estonia, Latvia, Slovakia and Slovenia, as well as in Moldova and Ukraine.

Wage growth is supported by tight labour markets, which are suffering from chronic labour shortages. The Visegrád and CIS countries appear to have the most acute labour shortages, as reflected in their unemployment data (see Figure 2.7) – for several years now, unemployment rates in those sub-regions have remained at around 4%. Given the difficulty they face in finding employees,

companies tend to ‘hoard labour’ – i.e. to be reluctant to lay off workers even during periods of poor economic performance. In Russia, the unemployment rate has recently declined further to reach 2.9% in Q4 2023 – partly due to war-related demographic shifts: military conscription has been taking men out of the labour force and has caused a lasting decline in the economically active population, since many are killed or rendered disabled in Ukraine. Besides, the threat of conscription has impelled many people, especially young men, to emigrate. On top of everything else, the demand for labour is relatively high, due to the reasonable economic growth. In the Western Balkans, pre-election wage rises in the public sector have played an important role as well. Although unemployment rates remain above 10% in all countries of the sub-region, apart from Serbia, they have been declining steadily, while skill mismatches have become more evident and have led to labour shortages in certain sectors. Only in the Baltic countries has there recently been a gradual uptick in unemployment, due to poor industrial performance; but the average unemployment rate remains relatively low (at just below 7%) and is expected to decline as economic growth is restored.

Figure 2.7 / Unemployment rate, %, quarterly (LFS)



Note: Simple average of each country group.

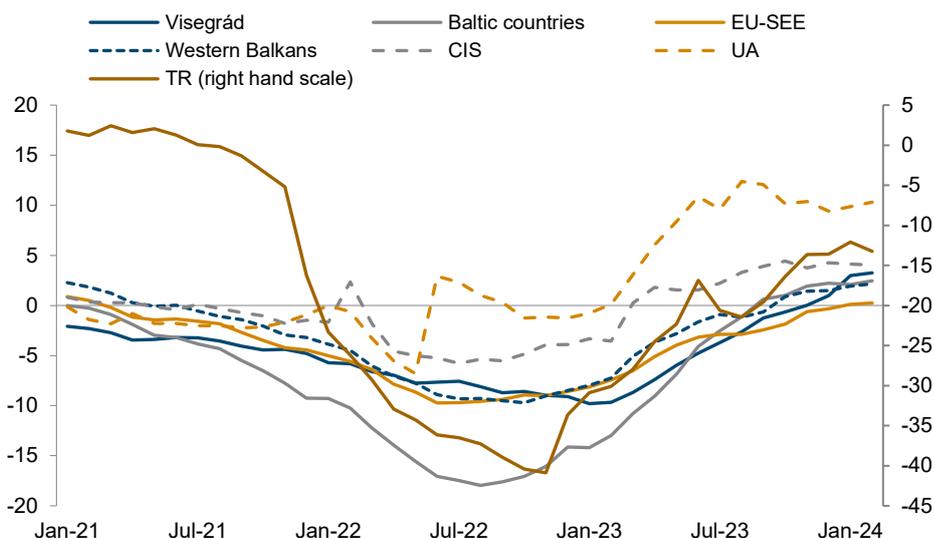
Source: wiiw Monthly Database incorporating national and Eurostat statistics.

2.3. REAL INTEREST RATES HAVE MOVED INTO POSITIVE TERRITORY, BUT SO FAR APPEAR TO HAVE HAD LIMITED EFFECT ON HOUSING PRICES AND CONSUMER LENDING

Thanks to a strong decline in inflation, real interest rates have moved above zero (see Figure 2.8). Many countries have started to loosen their monetary policy, but national banks have been cutting interest rates more slowly than inflation has been falling, resulting in a tightening of real financing conditions. Turkey, by contrast, has been trying to tighten its monetary policy, but the interest rate hikes in H2 2023 were too small to offset the accelerating inflation; thus that country still has a double-digit negative real interest rate. Among EU-CEE countries, real interest rates have increased most in the Visegrád countries, with the average real interest rate in the sub-region exceeding 3% in February 2024. Monetary authorities in the sub-region still appear to be cautious in their approach to monetary loosening: this is due to the sticky core inflation and fast nominal wage growth, as well as to a reluctance to risk any major weakening of the national currency, which could further increase imported inflation. The

countries of EU-SEE have been relatively lax in their monetary policy, with average real interest rates just slightly above zero. Croatia and Romania had real interest rates that were negative in February 2024 – albeit only slightly (-0.3% and -0.1%, respectively). Real interest rates are higher for all EU-CEE countries (bar Latvia and Lithuania) if one deflates nominal interest rates by the annual consumer price inflation (CPI) forecast for 2025 – the difference is greatest for Romania and Croatia. This may be seen as an argument for national banks to be less cautious when deciding on future interest rate cuts.

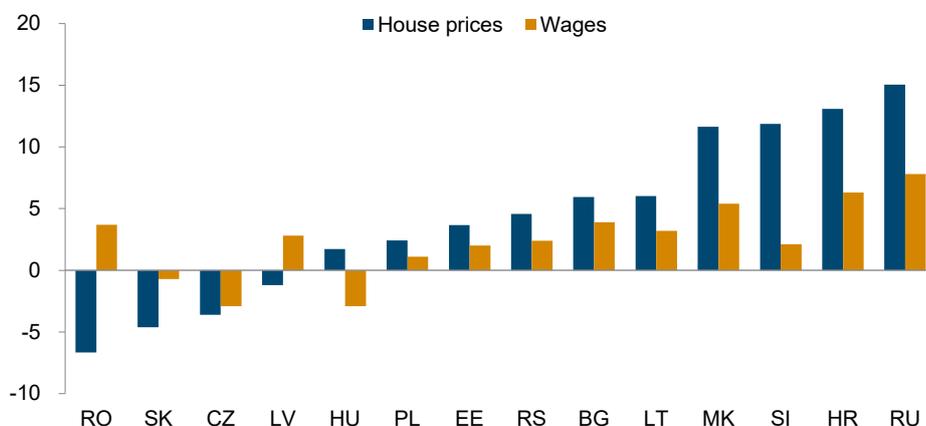
Figure 2.8 / Real interest rate (RIR), CPI deflated, %



Note: Simple averages for country aggregates.
 Source: wiiw Monthly Database incorporating national and Eurostat statistics and Eurostat, Bank for International Settlements.

Figure 2.9 / House prices, deflated by CPI, and real wages in 2023

percentage change year on year



Source: wiiw Monthly Database incorporating national and Eurostat statistics and Eurostat, Bank for International Settlements.

The high demand for housing continued even as interest rates were raised, and house prices in many CESEE countries rose rapidly in real terms in 2023, outpacing real wage growth (see Figure 2.9). An inadequate supply of housing also continues to support the property price growth in many countries. Russia, Croatia, Slovenia and North Macedonia stand out as those countries with double-digit annual growth in real house prices in 2023, while real wages grew much slower. Such developments might point to a possible overheating on the national housing markets.

Lower housing affordability is yet another indicator of the adverse social consequences of inflation. As buying a house becomes increasingly expensive, rapidly rising rents add to the economic hardships faced by households: rent absorbed more than 30% of household income among the poorer households of many CESEE countries (see Figure 2.10); Serbian and Romanian households were particularly badly affected (rents absorbed more than half of household income in those households that fell below 60% of median equalised income).

Figure 2.10 / Rent related to occupied dwelling as a share of disposable household income in 2023, %

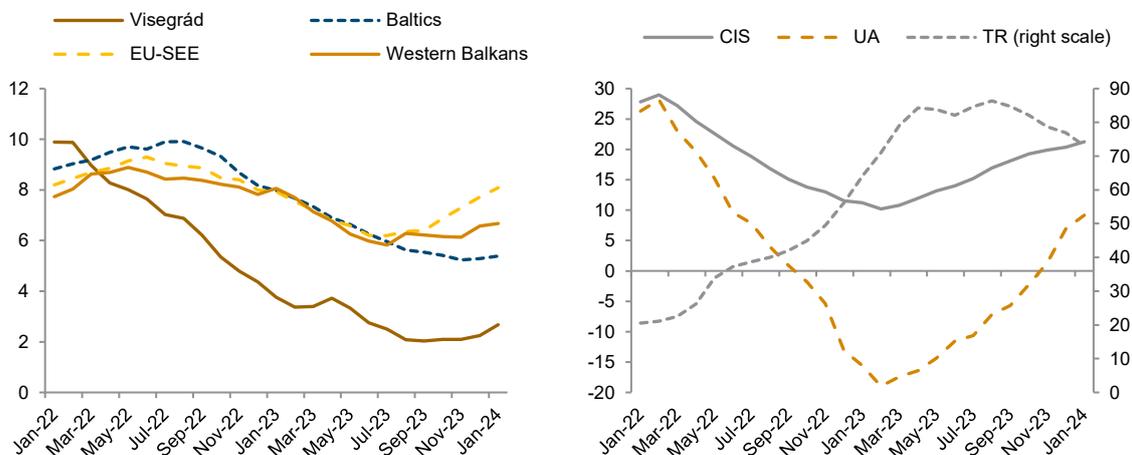
Households below 60% of median equalised income



Note: * the data are for 2022.

Source: Eurostat.

Regardless of rising real interest rates, the growth in loans to households has been accelerating over the past three months in many CESEE countries, though it mostly remains lower than two years ago. CIS countries have recorded double-digit growth in the stock of such loans over the past few years, and this trend shows no sign of abating (see Figure 2.11). As most lending to households in the sub-region is in the form of consumer (short-term) loans, this trend likely points to households financing part of their consumption through borrowing. Within EU-CEE, the countries of Southeast Europe have witnessed the fastest growth in loans to households – 8.1% year on year in January 2024. The four countries concerned vary quite considerably in this respect, though: banks in Bulgaria and Croatia have been rapidly building up their stock of loans to households (at respectively 16.3% and 10.2% year on year in January 2024), whereas in Romania and Slovenia the growth in such loans has been anaemic (1.9% and 3.8%, respectively). Compared to January 2022, the Visegrád countries have seen the greatest slowdown in the growth of household loans, likely as a result of the very high real interest rates in the region.

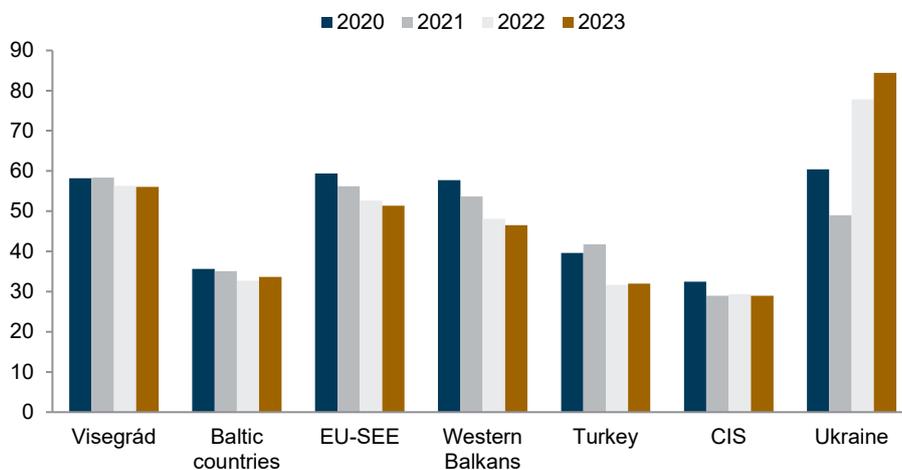
Figure 2.11 / Stock of loans to households, change year on year, %

Note: Simple averages for country aggregates.

Source: wiiw Monthly Database incorporating national and Eurostat statistics and Eurostat.

2.4. TIGHTER FINANCING CONDITIONS STARTING TO LIMIT PUBLIC AND PRIVATE INVESTMENT IN THE REGION

Public debt has been shrinking for several years now across most of the region, primarily due to the effects of high inflation. In 2023, the ratio of public debt to GDP decreased further in all the sub-regions – apart from Ukraine, which received a significant amount of financial support from abroad (see Figure 2.12). As the levels of public debt are relatively low in most countries and as the economic prospects appear positive, investors in sovereign debt will likely show increased interest in the region in the near future. However, the higher cost of borrowing and the need to pursue fiscal consolidation will limit governments' appetite for debt.

Figure 2.12 / Public debt, % of GDP

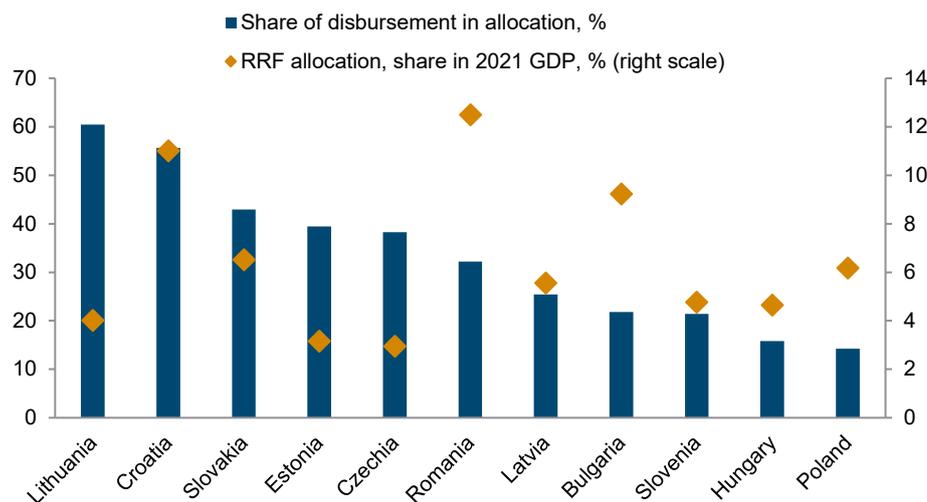
Note: Simple averages for country aggregates.

Source: wiiw Annual Database incorporating national and Eurostat statistics.

Resources from the EU Recovery and Resilience Facility (RRF) have provided relief to the EU-CEE, but disbursement is often too slow (see Figure 2.13). The fund's implementation has been delayed due to disagreements with Brussels over required reforms (primarily in the cases of Hungary, Poland and Slovakia) and over the design of the investment projects to be funded; and internal political bottlenecks have also prevented the agreed milestones being reached. Additionally, disbursements have often been delayed and the size of them effectively eroded by high inflation. By the end of March 2024, only Lithuania and Croatia had managed to secure disbursements of more than 50% of the RRF funds allocated to them in 2021. In March 2024, the European Commission unfroze Poland's funds, which had been blocked due to disagreements about the rule of law; however, it could prove difficult for the country to catch up in terms of the funds' absorption in the time remaining (until the end of 2026). Things look even bleaker for Hungary, where a substantial part of the EU funds continue to be frozen and their disbursement is conditional on the implementation of judicial reforms.

Figure 2.13 / RRF funds allocation and disbursement in 2021-2023

In descending order, by share of disbursement



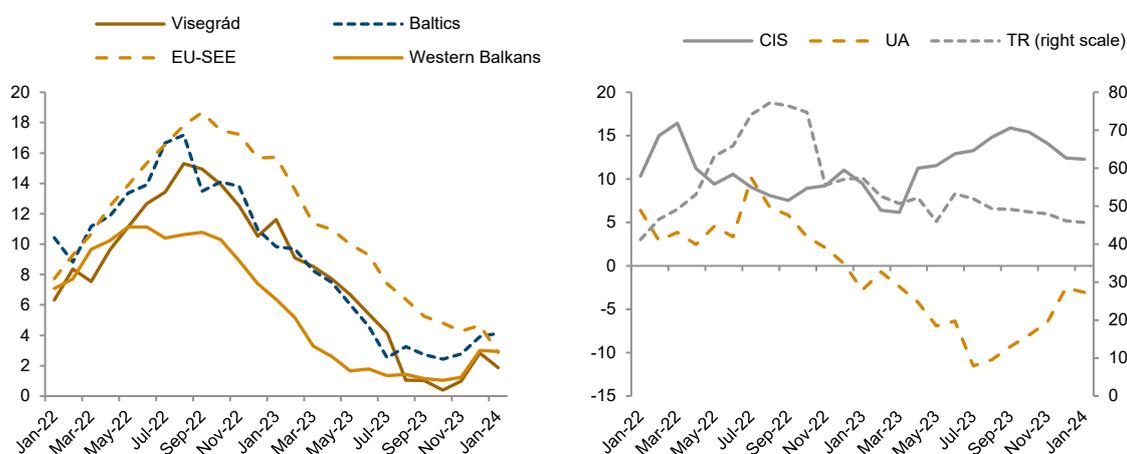
Note: Simple averages for country aggregates. Allocation is for the whole period of RRF operation (2021-2026).
Source: European Commission.

If EU-CEE countries improve their compliance with RRF conditions, they could receive a significant boost to their economies in 2024-2026. So far Croatia and Romania have benefited the most from RRF funds, having received the equivalent of 6.1% and 4.0% of their 2021 GDP. The funds have been crucial to the financing of their digital and renewable energy infrastructure projects. If they are successful in their application for the rest of the available funds, they could generate funds equivalent to as much as 4.9% of 2021 GDP in the case of Croatia, and 8.5% of 2021 GDP in the case of Romania. Bulgaria, Poland and Latvia also have large untapped resources allocated to them, amounting to 4-7% of 2021 GDP.

Private investment is being hampered by higher interest rates, which negatively affect bank lending to companies. Although the banking sector of the CESEE countries remains fairly healthy, with low rates of NPLs and high accumulated profits due to the big differential between deposit rates and loan interest rates, rising interest rates have curbed the growth of credit to non-financial corporations, which has lagged significantly behind the growth of household loans. The euro area bank lending survey

in Q1 2024 showed that net demand for loans by enterprises continued to decline substantially; also rejection rates for loan applications have increased. Signs of a tightened loan supply to companies are visible across most of the region (except for CIS), with the growth rates for loans far below their 2022 levels (see Figure 2.14). Of the EU-CEE countries, the picture regarding loans is poorest in the Visegrád countries, where the stock of loans to non-financial corporations increased by only 1.9% year on year in January 2024. There was even a contraction in the stock of loans in Slovenia, Poland and Latvia – by 7.0%, 4.1% and 0.3% year on year, respectively.

Figure 2.14 / Stock of loans to non-financial corporations, change year on year, %



Note: Simple averages for country aggregates.

Source: wiiw Monthly Database incorporating national and Eurostat statistics and Eurostat.

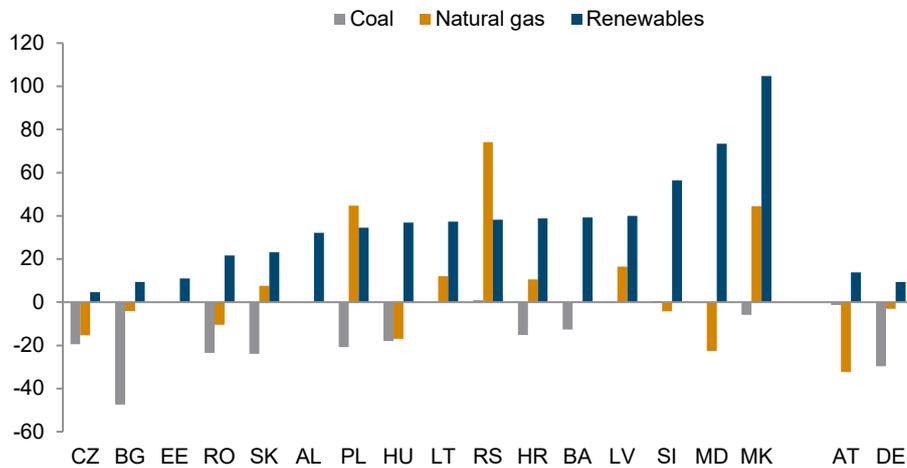
2.5. THE TRANSITION TO RENEWABLE ENERGY HAS BEEN ADVANCING, BUT THE FINANCING OF THE NECESSARY INVESTMENT WILL LIKELY PROVE MORE DIFFICULT IN FUTURE

Many CESEE countries have been investing in various energy infrastructure projects as part of the green transition agenda (and simultaneously with an eye to reducing dependence on Russia as an energy supplier). EU-CEE countries used RRF transfers to finance investment in energy transport networks (setting up connections to liquefied natural gas terminals), energy storage facilities and nuclear projects, as well as solar and wind parks. Outside the EU, the Western Balkans have been investing in solar and wind energy plants. Serbia and Turkey are investing in natural gas connections, in an effort to diversify away from Russian natural gas supplies.

As a result, the use of renewables in electricity generation increased in all CESEE countries in 2023, with Southeast Europe leading the way. All the countries apart from Czechia, Bulgaria and Estonia managed to increase their use of renewables faster than Austria (see Figure 2.15), with the fastest growth achieved in North Macedonia and Moldova; in the case of Moldova, this was motivated by the need to replace gas previously imported from Gazprom with alternative energy sources. Natural gas use increased most in Serbia, Poland and North Macedonia. These developments allowed a reduction in the use of coal everywhere; only in Serbia and Slovenia was there a marginal (below 1%) increase in the use of coal in electricity generation.

Figure 2.15 / Net electricity generation by type of fuel in 2023

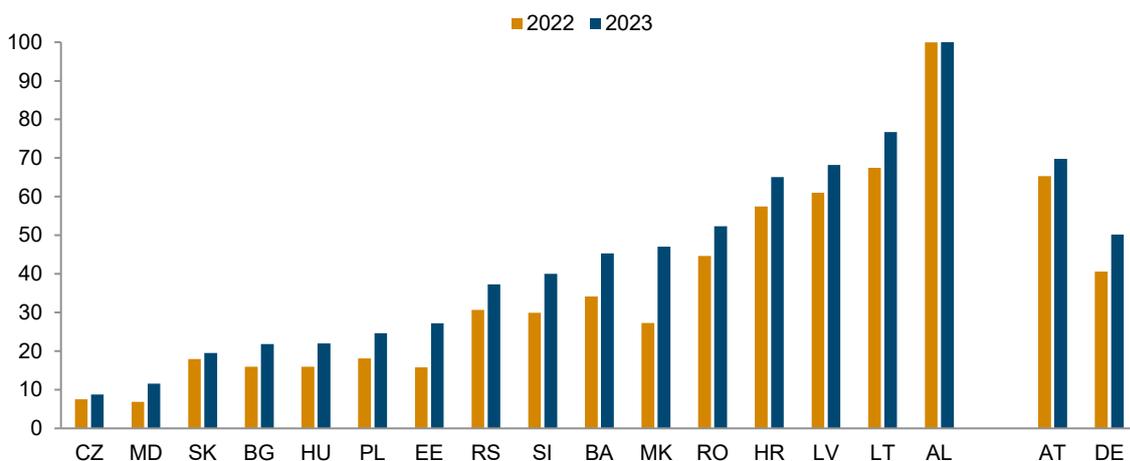
percentage change year on year



Note: Renewables consist of solar, wind, hydropower and geothermal energy.
Source: Eurostat, own calculations.

As a result of these developments, the share of renewable energy in electricity generation increased further in CESEE, although the majority of the countries have not yet reached the level of Austria or Germany (Figure 2.16). The biggest increases in the share of renewables in the energy mix in 2023 were achieved in North Macedonia, Estonia, Bosnia and Herzegovina and Slovenia – increases of 19.8 pp, 11.4 pp, 11.1 pp and 10.1 pp, respectively. Now Latvia, Lithuania, Croatia and Romania have more than half of their energy mix generated from renewables.

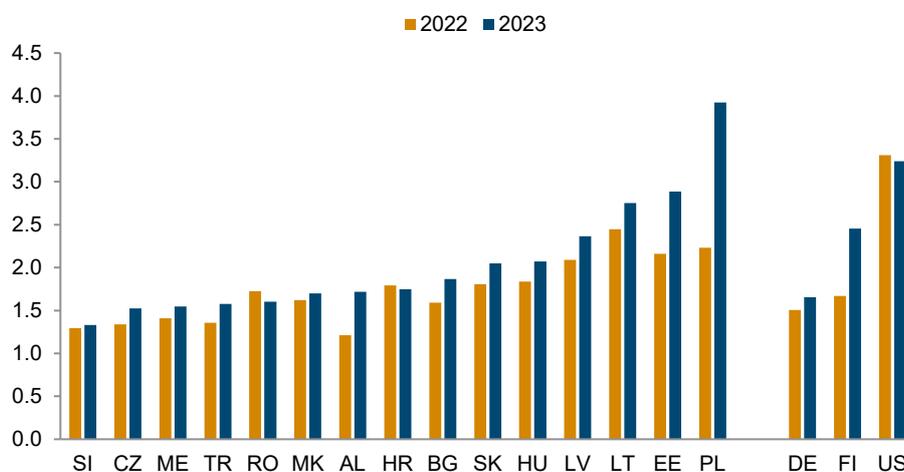
Figure 2.16 / Shares of renewable energy in net electricity generation in 2022 and 2023, %



Note: Renewables consist of solar, wind, hydropower and geothermal energy.
Source: Eurostat, own calculations.

The narrowing fiscal space and the need to prioritise defence spending due to the rising security risks will hinder investment in the green transition over the coming years. As the risk of instability has been increasing in many CESEE countries where a NATO presence is crucial for security (see Global assumptions), they have been raising their defence spending to improve their defence capabilities. Already in 2023, all the NATO members of CESEE (apart from Croatia and Romania) increased the share of defence expenditure in GDP (see Figure 17). Poland and the Baltic states (which feel most threatened by Russia) have been the most resolute in bolstering their military defence – in Poland the share of defence expenditure in GDP reached 4% of GDP in 2023.

Figure 2.17 / Defence expenditure as a share of GDP, %



Note: 2023 values are estimates.

Source: NATO.

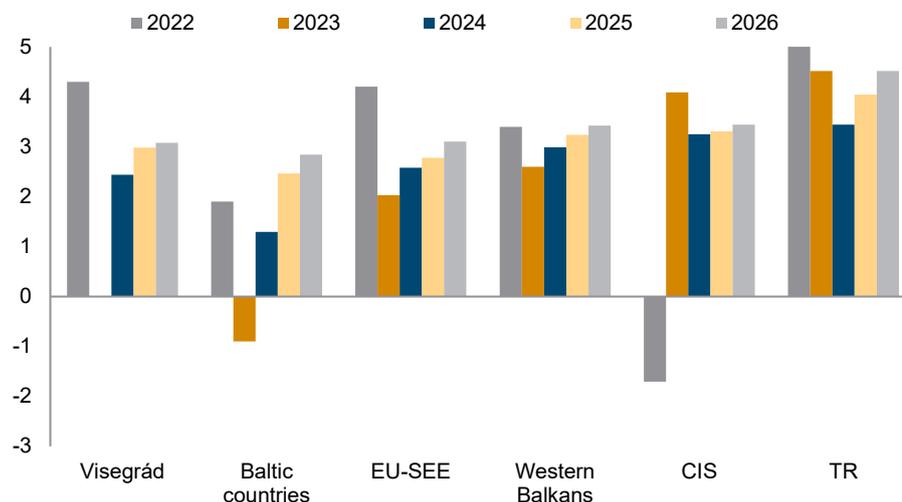
2.6. FORECAST FOR 2024-2026: CAUTIOUS ECONOMIC RECOVERY, WITH CONVERGENCE GRADUALLY SLOWING DOWN

This year, 2024, will bring an acceleration of economic growth for most of the region, apart from CIS, Ukraine and Turkey. The Visegrád sub-region, whose economy stagnated in 2023, will achieve the most rapid acceleration of annual GDP growth in 2024 – by 2.4 pp, after the previous year of economic stagnation (Figure 2.18). The Baltic countries, which went through a recession in 2023, will achieve economic growth of 1.3% this year – a growth differential of 2.2 p.p. Still, regardless of this rapid acceleration, growth in the Baltic and Visegrád countries will be the lowest of all the sub-regions in 2024. EU-SEE will outperform the Visegrád countries again this year, though this time only marginally – by 0.2 pp. In CIS, economic growth will moderate in 2024, as the statistical effect of a lower base of comparison in 2022 vanishes. Turkey's economic growth will slow down in 2024, due primarily to monetary tightening.

In 2025-2026, economic growth will become more uniform at about 3% year on year, as the economies of the Visegrád and Baltic countries accelerate to grow on a par with other sub-regions. Moderation of the growth in wages and a tightening of fiscal policy will prevent more dynamic economic performance. Looking at individual countries (see Tables 6.9, 6.22 and 6.23), Kazakhstan, Turkey and Ukraine will be the leaders in terms of economic growth in the region over the forecast

period. In the case of Ukraine, growth will be driven by both private and government consumption (assuming adequate foreign aid continues to be forthcoming); however, the forecast is subject to large downside risks related primarily to the intensity and duration of Russia's war in Ukraine and the continued willingness on the part of Ukraine's international partners to support it (see Ukraine report). In the Western Balkans, both Bosnia and Herzegovina and North Macedonia will manage to catch up with the other four countries of the sub-region in terms of the speed of growth, with annual GDP growth accelerating in 2026 to 3.4% and 3%, respectively. In the Visegrád region, only Poland will post annual GDP growth of above 3% in 2026; the other three economies will struggle to find stronger drivers of economic growth amidst a weaker global economy. With the exception of Slovenia, members of EU-SEE will perform more strongly than the Visegrád countries; Romania will grow fastest – at 3.8% year on year in 2026, on the back of increased RRF disbursement and mild fiscal stabilisation the previous year.

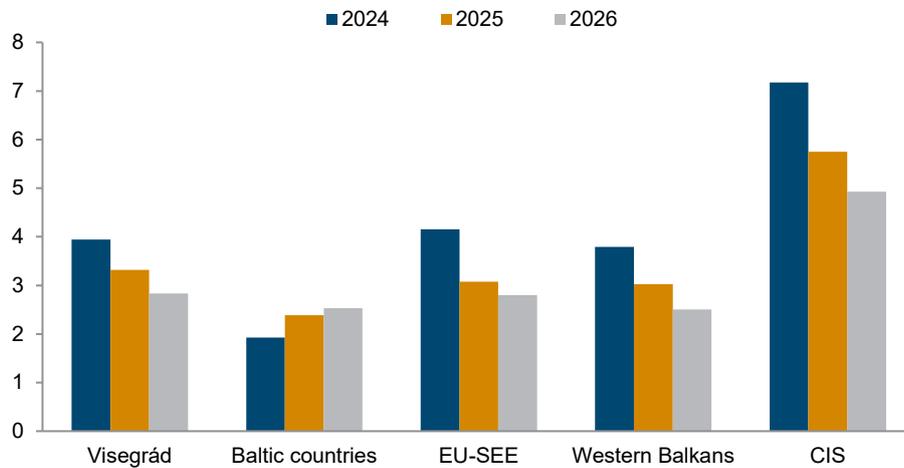
Figure 2.18 / Real GDP, annual change, %



Note: wiiw forecast for 2024-2026.

Source: wiiw annual dataset, wiiw forecast.

Inflation is expected to subside further across the region in 2024-2026, as wage growth moderates and global prices remain low (see Figure 2.19). The Baltic countries present an exception, as their inflation is expected to accelerate somewhat in 2025-2026; but even then it will remain the lowest in the region, at about 2.5% on average in 2026. Falling global food and energy prices will allow the relatively painless removal of price controls in many countries, although robust wage growth will stimulate private demand and push prices upwards. Along with Turkey, CIS will continue to have the highest CPI growth in CESEE, with prices growing fastest in Belarus and Kazakhstan (by 6% year on year in 2026 in both countries) – here inflation will be driven by high consumer demand, in particular for imports. Russia, by contrast, is expected to have a soft landing, with inflation decelerating rapidly to 3.7% year on year in 2026 (see Russia report). Turkey will still have uncomfortably high inflation of above 20% even in 2026, as monetary tightening will remain on the cautious side. In EU-CEE, Hungary, Romania and Slovakia will be the least successful in bringing down inflation, as their central banks tend to be less hawkish, and / or fiscal deficits will remain relatively high over the forecast period.

Figure 2.19 / CPI forecast for 2024-2026, average annual change, %

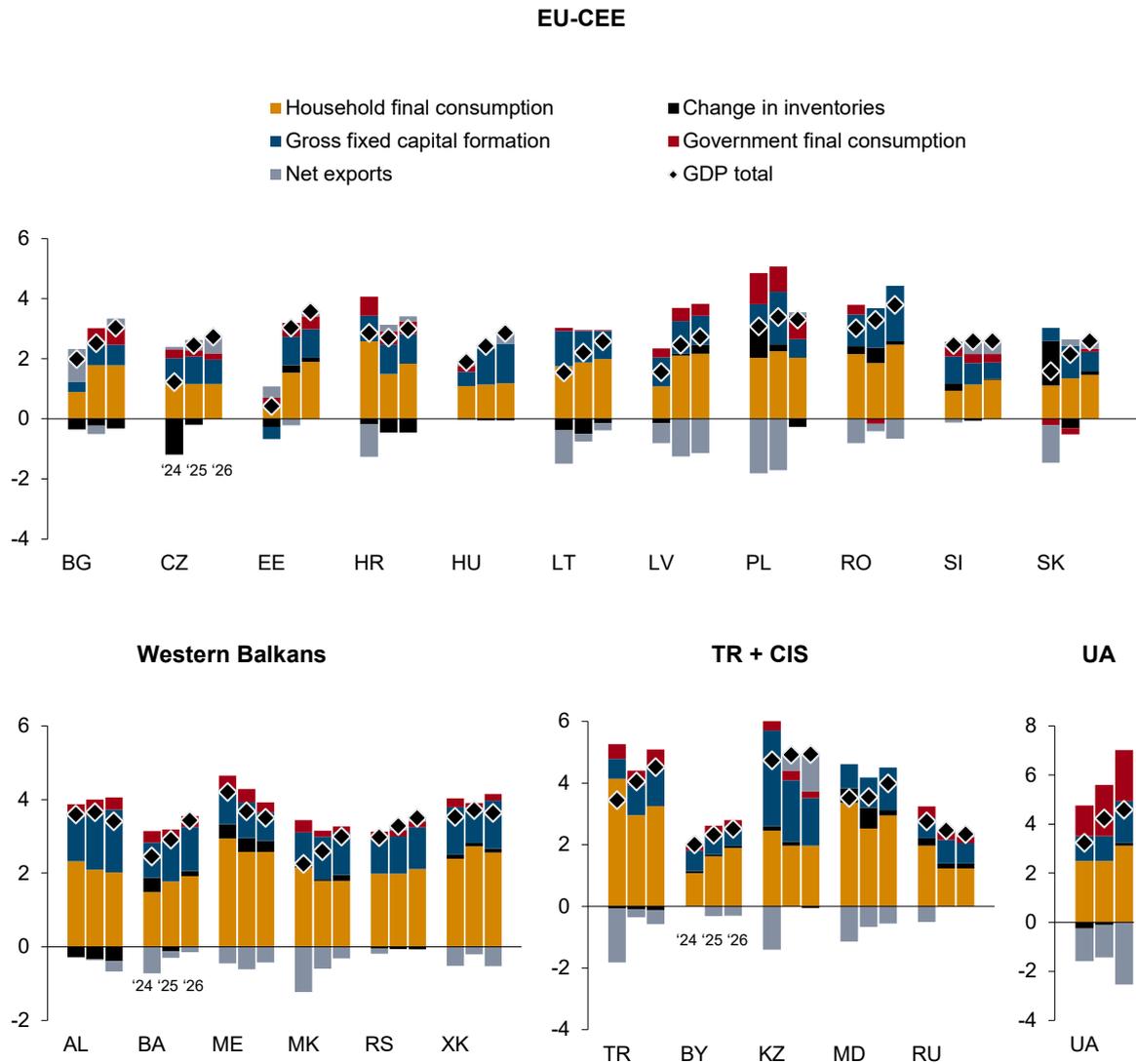
Note: Simple averages for country aggregates.

Source: wiiw forecast.

Economic convergence with the eurozone will speed up in 2024, but then slow down again. In 2024, the euro area's economy is expected to grow by only 0.6% year on year, which will increase the growth differential with CESEE region to 2.3 pp. In 2025-2026, however, it will narrow to 1.5 pp and 1.7 pp, respectively, against the backdrop of accelerated economic growth in the key euro area economies.

Private consumption will continue as the main growth driver during the forecast period, owing to the continued growth of wages and slowdown in inflation (see Figure 2.20). In 2026, it will account for more than 70% of GDP growth in Latvia, Lithuania, Kosovo, Montenegro, Turkey, Belarus and Moldova. Hungary is an outlier in the region, in that its private consumption is expected to contribute less to GDP growth in 2025-2026 than investment – assuming there is some progress in the disbursement of EU RRF and cohesion funds. In Kazakhstan, household consumption is expected to generate the least contribution to GDP growth in 2025-2026 (about 40% each year) in the region – primarily on account of the expanding energy exports.

Figure 2.20 / GDP growth forecast for 2024-2026 and contribution of individual demand components, in percentage points



Source: wiiw Annual Database incorporating national and Eurostat statistics, own calculations. Forecasts by wiiw.

Table 2.1 / OVERVIEW 2022-2023 AND OUTLOOK 2024-2026

	GDP					Consumer prices					Unemployment (LFS)				
	real change in % against prev. year					average change in % against prev. year					rate in %, annual average				
	2022	2023	Forecast			2022	2023	Forecast			2022	2023	Forecast		
BG Bulgaria	3.9	1.8	2.0	2.5	3.0	13.0	8.6	4.0	3.0	3.0	4.3	4.3	4.2	4.1	4.0
CZ Czechia	2.4	-0.3	1.2	2.5	2.7	14.8	12.0	2.0	2.2	2.2	2.2	2.6	3.0	2.6	2.6
EE Estonia	-0.5	-3.0	0.4	3.0	3.6	19.4	9.1	3.5	2.8	2.4	5.6	6.4	7.5	6.2	5.6
HR Croatia	6.3	2.8	2.9	2.7	3.0	10.7	8.4	3.5	2.9	2.5	7.0	6.1	6.1	6.0	6.0
HU Hungary	4.6	-0.9	1.9	2.4	2.9	15.3	17.0	5.2	4.0	3.5	3.6	4.1	4.0	3.8	3.5
LT Lithuania	2.4	-0.3	1.5	2.2	2.6	18.9	8.7	1.5	2.3	2.5	6.0	6.8	6.5	6.3	6.0
LV Latvia	3.0	-0.3	1.6	2.5	2.7	17.2	9.1	1.4	2.2	2.7	6.9	6.5	6.3	6.0	5.8
PL Poland	5.3	0.2	3.1	3.4	3.3	13.2	10.9	4.5	3.5	2.8	2.9	2.8	2.8	3.0	3.1
RO Romania	4.1	2.1	3.0	3.3	3.8	12.0	9.7	5.8	4.0	3.5	5.6	5.6	5.5	5.4	5.2
SI Slovenia	2.5	1.6	2.5	2.6	2.6	9.3	7.2	3.3	2.4	2.2	4.0	3.7	3.7	3.6	3.6
SK Slovakia	1.8	1.1	1.6	2.2	2.6	12.1	11.0	2.2	3.4	3.4	6.1	5.8	5.8	5.6	5.4
<i>EU-CEE11¹⁾²⁾</i>	<i>4.2</i>	<i>0.6</i>	<i>2.5</i>	<i>3.0</i>	<i>3.2</i>	<i>13.5</i>	<i>11.0</i>	<i>4.1</i>	<i>3.3</i>	<i>2.9</i>	<i>4.0</i>	<i>4.1</i>	<i>4.1</i>	<i>4.0</i>	<i>4.0</i>
<i>EA20³⁾</i>	<i>3.4</i>	<i>0.4</i>	<i>0.6</i>	<i>1.6</i>	<i>1.6</i>	<i>8.4</i>	<i>5.4</i>	<i>2.5</i>	<i>2.2</i>	<i>2.0</i>	<i>6.8</i>	<i>6.5</i>	<i>6.7</i>	<i>6.6</i>	<i>6.6</i>
<i>EU27³⁾</i>	<i>3.4</i>	<i>0.4</i>	<i>0.8</i>	<i>1.8</i>	<i>1.8</i>	<i>9.2</i>	<i>6.4</i>	<i>2.7</i>	<i>2.4</i>	<i>2.2</i>	<i>6.2</i>	<i>5.7</i>	<i>5.9</i>	<i>5.8</i>	<i>5.8</i>
AL Albania	4.9	3.4	3.6	3.7	3.4	6.7	4.8	3.0	2.5	2.4	10.9	10.7	10.4	10.0	9.7
BA Bosnia and Herzegovina	4.2	1.7	2.5	2.9	3.4	14.0	6.1	2.8	2.5	2.0	15.4	13.2	12.9	12.7	12.4
ME Montenegro	6.4	6.0	4.2	3.7	3.5	13.0	8.6	4.5	3.0	2.5	14.7	13.1	11.0	10.0	9.0
MK North Macedonia	2.2	1.0	2.2	2.6	3.0	14.2	9.4	3.5	3.0	2.5	14.4	13.1	12.5	11.8	11.0
RS Serbia	2.5	2.5	3.0	3.3	3.5	11.9	12.1	4.5	3.5	2.8	9.4	9.5	9.0	8.5	8.0
XK Kosovo	4.3	3.3	3.5	3.7	3.6	11.6	4.9	3.5	2.5	2.2	12.5	12.4	12.3	12.0	11.5
<i>WB6¹⁾²⁾</i>	<i>3.4</i>	<i>2.6</i>	<i>3.0</i>	<i>3.2</i>	<i>3.4</i>	<i>11.8</i>	<i>9.0</i>	<i>3.8</i>	<i>3.0</i>	<i>2.5</i>	<i>11.7</i>	<i>11.1</i>	<i>10.8</i>	<i>10.0</i>	<i>9.8</i>
TR Turkey	5.5	4.5	3.4	4.0	4.5	72.3	54.0	59.0	31.0	26.0	10.5	9.4	10.0	10.5	10.0
BY Belarus	-4.7	3.9	2.0	2.3	2.5	15.2	5.1	8.0	7.0	6.0	3.6	3.5	3.5	3.4	3.4
KZ Kazakhstan	3.2	5.1	4.7	4.9	4.9	15.0	14.7	8.5	6.5	6.0	4.9	4.7	4.6	4.5	4.4
MD Moldova	-4.6	0.7	3.5	3.5	4.0	28.7	13.4	5.0	5.0	4.0	3.1	4.6	4.0	3.8	3.5
RU Russia	-1.2	3.6	2.8	2.5	2.3	13.8	5.9	7.2	4.5	3.7	4.0	3.2	2.9	2.9	2.9
UA Ukraine	-28.8	5.3	3.2	4.2	4.6	20.2	12.9	8.0	6.0	6.0	25.0	20.0	15.0	10.0	9.0
<i>CIS4+UA¹⁾²⁾</i>	<i>-2.9</i>	<i>3.9</i>	<i>3.0</i>	<i>2.8</i>	<i>2.8</i>	<i>14.5</i>	<i>7.2</i>	<i>7.4</i>	<i>4.9</i>	<i>4.2</i>	<i>7.4</i>	<i>5.9</i>	<i>4.9</i>	<i>4.1</i>	<i>3.9</i>
<i>V4¹⁾²⁾</i>	<i>4.3</i>	<i>0.0</i>	<i>2.4</i>	<i>3.0</i>	<i>3.1</i>	<i>13.7</i>	<i>12.0</i>	<i>3.9</i>	<i>3.3</i>	<i>2.8</i>	<i>3.2</i>	<i>3.3</i>	<i>3.3</i>	<i>3.3</i>	<i>3.3</i>
<i>BALT3¹⁾²⁾</i>	<i>1.9</i>	<i>-0.9</i>	<i>1.3</i>	<i>2.5</i>	<i>2.8</i>	<i>18.6</i>	<i>8.9</i>	<i>1.9</i>	<i>2.4</i>	<i>2.5</i>	<i>6.1</i>	<i>6.6</i>	<i>6.7</i>	<i>6.2</i>	<i>5.8</i>
<i>SEE9¹⁾²⁾</i>	<i>4.2</i>	<i>2.3</i>	<i>2.8</i>	<i>3.1</i>	<i>3.5</i>	<i>12.0</i>	<i>9.2</i>	<i>4.8</i>	<i>3.5</i>	<i>3.1</i>	<i>7.7</i>	<i>7.5</i>	<i>7.3</i>	<i>7.0</i>	<i>6.8</i>
<i>CIS3+UA¹⁾²⁾</i>	<i>-9.4</i>	<i>4.8</i>	<i>3.7</i>	<i>4.2</i>	<i>4.4</i>	<i>17.3</i>	<i>12.5</i>	<i>8.1</i>	<i>6.4</i>	<i>5.9</i>	<i>15.3</i>	<i>12.5</i>	<i>9.8</i>	<i>7.1</i>	<i>6.5</i>
<i>non-EU12¹⁾²⁾</i>	<i>-0.1</i>	<i>4.0</i>	<i>3.1</i>	<i>3.2</i>	<i>3.3</i>	<i>32.3</i>	<i>21.8</i>	<i>23.3</i>	<i>12.9</i>	<i>10.9</i>	<i>8.3</i>	<i>7.0</i>	<i>6.4</i>	<i>5.9</i>	<i>5.7</i>
<i>CESEE23¹⁾²⁾</i>	<i>1.2</i>	<i>3.0</i>	<i>2.9</i>	<i>3.1</i>	<i>3.3</i>	<i>26.6</i>	<i>18.5</i>	<i>17.5</i>	<i>10.0</i>	<i>8.5</i>	<i>7.3</i>	<i>6.3</i>	<i>5.8</i>	<i>5.5</i>	<i>5.3</i>

Contd.

Table 2.1 / Continued

	Current account					Fiscal balance				
	in % of GDP					in % of GDP				
	2022	2023	Forecast			2022	2023	Forecast		
		2024	2025	2026	2022	2023	2024	2025	2026	
BG Bulgaria	-1.4	-0.3	-0.2	-0.6	-0.9	-2.9	-3.0	-4.0	-3.0	-3.0
CZ Czechia	-4.9	0.4	0.4	0.8	1.4	-3.2	-3.3	-2.5	-2.0	-1.5
EE Estonia	-3.2	-2.1	-2.0	-1.7	-1.8	-1.0	-3.3	-3.6	-4.5	-3.7
HR Croatia	-2.8	1.1	0.2	1.0	1.3	0.1	-1.0	-2.0	-1.4	-1.2
HU Hungary	-8.4	0.2	0.0	0.2	0.4	-6.3	-6.7	-5.0	-4.0	-3.5
LT Lithuania	-5.5	1.9	2.2	2.8	2.5	-0.7	-1.0	-2.5	-2.5	-2.3
LV Latvia	-4.8	-4.0	-3.1	-4.6	-5.7	-4.7	-3.0	-2.8	-2.3	-2.0
PL Poland	-2.4	1.6	0.5	-1.2	-1.0	-3.7	-5.6	-5.4	-5.3	-5.3
RO Romania	-9.2	-7.0	-6.5	-6.0	-6.0	-6.3	-6.2	-5.7	-4.3	-3.5
SI Slovenia	-1.0	4.5	5.1	4.5	3.8	-3.0	-3.3	-3.5	-2.0	-0.6
SK Slovakia	-7.3	-1.6	-1.3	-0.9	-1.1	-2.0	-6.0	-6.0	-5.0	-4.0
<i>EU-CEE11</i> ¹⁾²⁾	<i>-4.8</i>	<i>-0.4</i>	<i>-0.7</i>	<i>-1.2</i>	<i>-1.1</i>	<i>-3.8</i>	<i>-4.9</i>	<i>-4.6</i>	<i>-4.1</i>	<i>-3.7</i>
<i>EA20</i> ³⁾	<i>1.3</i>	<i>1.8</i>	<i>3.2</i>	<i>3.2</i>	<i>3.1</i>	<i>-3.6</i>	<i>-3.2</i>	<i>-2.6</i>	<i>-2.6</i>	<i>-2.5</i>
<i>EU27</i> ³⁾	<i>1.2</i>	<i>1.8</i>	<i>3.2</i>	<i>3.2</i>	<i>3.1</i>	<i>-3.3</i>	<i>-2.8</i>	<i>-2.2</i>	<i>-2.2</i>	<i>-2.1</i>
AL Albania	-5.9	-0.9	-1.4	-1.3	-1.4	-3.7	-1.4	-1.5	-1.5	-1.0
BA Bosnia and Herzegovina	-4.3	-2.8	-3.6	-3.1	-3.0	-0.4	1.0	-0.5	-0.7	-1.0
ME Montenegro	-12.9	-11.4	-10.7	-10.6	-10.4	-5.1	-5.0	-6.0	-6.0	-6.0
MK North Macedonia	-6.1	0.7	-0.8	-1.9	-2.4	-4.4	-4.9	-4.0	-3.0	-2.5
RS Serbia	-6.9	-2.6	-2.7	-2.9	-2.9	-3.2	-2.2	-2.0	-1.5	-1.0
XK Kosovo	-10.3	-7.6	-8.6	-8.7	-8.5	-0.5	-0.3	-1.0	-1.0	-2.0
<i>WB6</i> ¹⁾²⁾	<i>-6.7</i>	<i>-2.8</i>	<i>-3.2</i>	<i>-3.3</i>	<i>-3.3</i>	<i>-2.8</i>	<i>-1.8</i>	<i>-2.0</i>	<i>-1.7</i>	<i>-1.4</i>
TR Turkey	-5.4	-4.1	-3.1	-2.7	-2.3	-1.1	-5.3	-3.5	-3.0	-3.0
BY Belarus	3.5	-1.4	-2.1	-1.3	-0.9	-1.5	-1.0	-1.5	-1.0	-1.0
KZ Kazakhstan	3.1	-3.3	-2.3	-1.5	-0.5	-2.1	-2.4	-2.3	-2.0	-2.0
MD Moldova	-17.1	-11.9	-9.7	-8.9	-8.1	-3.2	-5.2	-4.0	-3.5	-3.0
RU Russia	10.5	2.5	3.3	3.2	3.0	-1.4	-2.3	-1.7	-1.5	-1.0
UA Ukraine	4.9	-5.2	-4.3	-4.7	-6.4	-16.1	-20.3	-17.0	-15.0	-12.0
<i>CIS4+UA</i> ¹⁾²⁾	<i>9.2</i>	<i>1.2</i>	<i>1.8</i>	<i>1.8</i>	<i>1.7</i>	<i>-2.3</i>	<i>-3.5</i>	<i>-2.9</i>	<i>-2.6</i>	<i>-2.0</i>
<i>V4</i> ¹⁾²⁾	<i>-4.3</i>	<i>0.8</i>	<i>0.3</i>	<i>-0.6</i>	<i>-0.3</i>	<i>-3.8</i>	<i>-5.3</i>	<i>-4.8</i>	<i>-4.4</i>	<i>-4.2</i>
<i>BALT3</i> ¹⁾²⁾	<i>-4.7</i>	<i>-0.7</i>	<i>-0.3</i>	<i>-0.3</i>	<i>-0.8</i>	<i>-1.8</i>	<i>-2.1</i>	<i>-2.9</i>	<i>-3.0</i>	<i>-2.6</i>
<i>SEE9</i> ¹⁾²⁾	<i>-6.7</i>	<i>-4.1</i>	<i>-4.0</i>	<i>-3.8</i>	<i>-3.8</i>	<i>-4.2</i>	<i>-4.1</i>	<i>-4.2</i>	<i>-3.2</i>	<i>-2.7</i>
<i>CIS3+UA</i> ¹⁾²⁾	<i>3.2</i>	<i>-3.9</i>	<i>-3.2</i>	<i>-2.7</i>	<i>-2.7</i>	<i>-6.8</i>	<i>-8.3</i>	<i>-7.1</i>	<i>-6.2</i>	<i>-5.2</i>
<i>non-EU12</i> ¹⁾²⁾	<i>5.1</i>	<i>-0.5</i>	<i>0.1</i>	<i>0.1</i>	<i>0.1</i>	<i>-2.0</i>	<i>-4.0</i>	<i>-3.0</i>	<i>-2.7</i>	<i>-2.3</i>
<i>CESEE23</i> ¹⁾²⁾	<i>1.8</i>	<i>-0.5</i>	<i>-0.2</i>	<i>-0.4</i>	<i>-0.4</i>	<i>-2.6</i>	<i>-4.3</i>	<i>-3.7</i>	<i>-3.2</i>	<i>-2.8</i>

1) wiiw estimates. - 2) Current account data include transactions within the region (sum over individual countries). -

3) Forecasts estimated by wiiw.

Source: wiiw, Eurostat. Forecasts by wiiw. Cut-off date for historical data and forecasts: 10 April 2024.

Table 2.2 / Real GDP growth forecasts and direction of revisions since wiiw winter forecast 2024

Region	2024	2025	2026
EU-CEE			
BG Bulgaria	2.0 ▲	2.5	3.0
CZ Czechia	1.2 ▼	2.5 ▼	2.7
EE Estonia	0.4 ▲	3.0 ▲	3.6 ▲
HR Croatia	2.9 ▲	2.7	3.0
HU Hungary	1.9 ▼	2.4 ▼	2.9 ▼
LT Lithuania	1.5	2.2 ▲	2.6 ▲
LV Latvia	1.6	2.5 ▲	2.7
PL Poland	3.1 ▲	3.4 ▼	3.3 ▲
RO Romania	3.0	3.3 ▼	3.8 ▲
SI Slovenia	2.5 ▼	2.6 ▲	2.6 ▼
SK Slovakia	1.6	2.2	2.6
Western Balkans			
AL Albania	3.6	3.7	3.4
BA Bosnia and Herzegovina	2.5 ▲	2.9 ▲	3.4 ▲
ME Montenegro	4.2 ▲	3.7 ▲	3.5 ▲
MK North Macedonia	2.2	2.6	3.0
RS Serbia	3.0 ▲	3.3 ▲	3.5 ▲
XK Kosovo	3.5	3.7	3.6
Turkey			
TR Turkey	3.4 ▲	4.0 ▲	4.5 ▲
CIS+UA			
BY Belarus	2.0	2.3 ▼	2.5 ▼
KZ Kazakhstan	4.7 ▲	4.9 ▲	4.9 ▲
MD Moldova	3.5 ▼	3.5 ▲	4.0 ▲
RU Russia	2.8 ▲	2.5 ▲	2.3 ▲
UA Ukraine	3.2 ▲	4.2 ▲	4.6 ▼

Note: Colour scale variation from the minimum (dark grey) to the maximum (dark orange).

Source: wiiw.

Table 2.3 / CPI growth forecasts and direction of revisions since wiiw winter 2024 Forecast Report

Region	2024	2025	2026
EU-CEE			
BG Bulgaria	4.0 ▲	3.0 ▼	3.0 ▼
CZ Czechia	2.0 ▼	2.2	2.2 ▲
EE Estonia	3.5	2.8 ▲	2.4 ▲
HR Croatia	3.5 ▼	2.9 ▼	2.5 ▲
HU Hungary	5.2 ▼	4.0	3.5
LT Lithuania	1.5 ▼	2.3	2.5
LV Latvia	1.4 ▼	2.2 ▼	2.7 ▲
PL Poland	4.5 ▼	3.5 ▼	2.8 ▲
RO Romania	5.8 ▼	4.0	3.5
SI Slovenia	3.3 ▼	2.4 ▼	2.2 ▼
SK Slovakia	2.2 ▼	3.4 ▼	3.4 ▲
Western Balkans			
AL Albania	3.0	2.5	2.4
BA Bosnia and Herzegovina	2.8	2.5	2.0
ME Montenegro	4.5 ▼	3.0	2.5
MK North Macedonia	3.5	3.0	2.5
RS Serbia	4.5	3.5	2.8
XK Kosovo	3.5 ▼	2.5	2.2 ▼
Turkey			
TR Turkey	59.0 ▲	31.0	26.0 ▼
CIS+UA			
BY Belarus	8.0	7.0 ▼	6.0 ▼
KZ Kazakhstan	8.5 ▼	6.5 ▼	6.0
MD Moldova	5.0 ▼	5.0	4.0
RU Russia	7.2 ▲	4.5 ▲	3.7 ▲
UA Ukraine	8.0	6.0 ▼	6.0 ▲

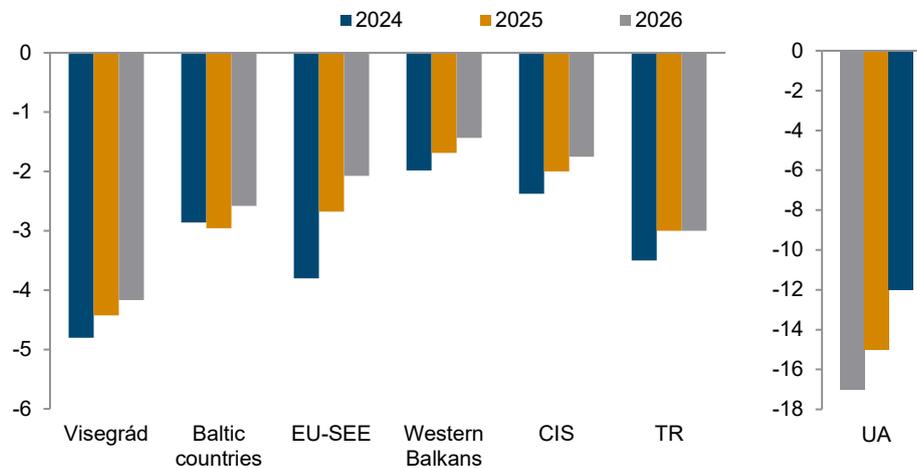
Note: Colour scale variation from the minimum (dark grey) to the maximum (dark orange).

Source: wiiw.

Investment is also expected to recover, but its contribution to economic growth will be too modest to generate the necessary structural changes. On average, investment will play a more important role for economic growth in the Western Balkans than in EU-CEE, even though the latter has access to EU funds. Given that the share in GDP of gross fixed capital formation remains fairly low in most CESEE countries (with the share in Poland as low as 17.5% in 2023), such growth rates will likely be too low to successfully promote the green and digital transition and to ensure the structural changes needed to boost the region's competitiveness.

High fiscal spending, including higher debts costs, will slow the pace of fiscal consolidation in the region (see Figure 2.21). EU-CEE will benefit from EU funds as an additional source of funding; these are expected to pick up in 2025-2026. The Visegrád countries are forecast to have the highest budget deficits in 2024-2026, at more than 4% of GDP on average. Within EU-CEE, the countries of Southeast Europe will reduce their fiscal balances the fastest, to achieve budget deficits of about 2% of GDP in 2026. Romania – which is facing pressure from Brussels to reduce its fiscal deficit – will go through rapid consolidation, with the deficit falling from 6.2% of GDP in 2023 to 3.5% of GDP in 2026. The countries of the Western Balkans (with the exception of Montenegro) will have to consolidate their public finances much faster than the rest of the region, due to the apparent fiscal space constraints: Albania, Bosnia and Herzegovina and Serbia are expected to reduce their fiscal deficits to a mere 1% of GDP in 2026.

Figure 2.21 / Fiscal balance as % of GDP



Note: simple averages for country aggregates.
Source: wiiw forecasts.

2.7. RISKS TO THE OUTLOOK REMAIN MOSTLY ON THE DOWNSIDE

The most significant downside risk to our forecast is related to a possible deterioration in the security situation of the region. Inadequate support from the West could lead to Ukraine losing the war (see Ukraine report). Mr Trump's (re)election as president in 2024 and the EU's inability to expand its defence sector and provide greater military and financial support to Ukraine could have that very outcome. This could result in an increase in the security risks for the whole of Europe, which would dampen consumer and investor confidence. Former Socialist-bloc countries will be particularly at risk of rising geopolitical instability.

The risk of rising energy prices, increased shipping costs and greater supply-chain disruption due to the tensions in the Middle East remains quite high. As the experience of the COVID-19 pandemic showed, many open economies of the region are highly susceptible to disruption to global trade. This could push inflation up again and reverse the course of the incipient economic recovery in the region.

A delayed German (and Austrian) recovery could have significant repercussions for the region. This risk is especially relevant for the Visegrád countries, for which Germany and Austria offer the most important sources of export demand and foreign direct investment.

Harder lending conditions could cause painful structural adjustments in the economy. As the rising bankruptcy rates in several countries indicate, many sectors are still adjusting to the reality of the new monetary regime, and that adjustment may turn out to be quite painful.

2.8. CONCLUSIONS

After a disappointing economic performance in 2023, things are finally looking up for the CESEE region. Economic growth will accelerate in 2024 in most of the countries, on the back of slower inflation and a recovery in real wages. In 2025-2026, economic growth will become more uniform, at about 3% year on year, as the economies of the Visegrád and Baltic countries speed up to grow on a par with other sub-regions. Private consumption will be the main growth driver, while investment growth will be constrained by higher interest rates.

Risks to the forecast are mainly on the downside. The security situation in the region could deteriorate significantly if Ukraine loses the war due to inadequate support on the part of the West. This could result in an increase in the security risks for the whole of Europe, which would dampen consumer and investor confidence in the region. Rising tensions in the Middle East could lead to increased energy prices and supply-chain disruptions, and could cause inflation to increase once again.