

Europe and Central Asia Economic Update  
Spring 2024

# Unleashing the Power of the Private Sector

Office of the Chief Economist  
Europe and Central Asia



# Recent Developments, Policies, and Outlook

## **Growth for 2023 picked up to 3.3% from 1.5% in 2022**

- A shift from contraction to expansion in Russia and Ukraine and robust recoveries in Central Asia
- Excluding Russia, growth broadly unchanged
- In two-thirds of the ECA countries, growth was slower in 2023 than in 2022

## **Inflation fell sharply due to lower global commodity prices and tighter monetary policies**

- Median year-on-year inflation down to 4.0% by March from almost 15% at the start of 2023
- Faster declines in inflation for goods, more persistence in price increases for services

## **Fiscal consolidation still deferred in most countries**

- Average fiscal deficit for 2023 amounted to 2% of GDP, little changed from 2022
- Higher social and capital spending to raise the average deficit in 2024

## **Subdued growth projected for 2024-25 with 2.8% on average vs 4.1% during 2000-2019**

- Slow euro area and global growth, geopolitical tensions, weak investment
- The key challenge is how to strengthen productivity growth and accelerate income convergence

# Moderate growth across most ECA countries

	2020	2021	2022	2023e	2024f	2025f	Percentage point differences from January 2024 projections		
				2023e	2024f	2025f	2023e	2024f	2025f
<b>ECA</b>	-1.7	7.3	1.5	3.3	2.8	2.7	0.5	0.4	0.0
<b>ECA excl. the Russian Federation</b>	-1.1	8.3	3.3	3.2	3.1	3.7	0.2	0.0	-0.1
<b>Central Europe<sup>a</sup></b>	-3.0	7.1	5.0	0.9	3.0	3.5	-0.1	0.2	0.0
<b>Western Balkans<sup>b</sup></b>	-3.0	7.9	3.4	2.6	3.2	3.5	0.1	0.2	0.0
<b>Eastern Europe excl. Ukraine<sup>c</sup></b>	-1.8	4.0	-4.7	3.4	1.3	1.2	0.6	0.0	-0.1
<b>South Caucasus<sup>d</sup></b>	-5.2	6.7	7.2	3.8	3.5	3.4	0.3	0.2	0.1
<b>Central Asia<sup>e</sup></b>	-1.3	5.3	4.2	5.5	4.1	4.9	0.6	-0.6	0.1
<b>Russian Federation</b>	-2.7	5.9	-1.2	3.6	2.2	1.1	1.0	0.9	0.2
<b>Türkiye</b>	1.9	11.4	5.5	4.5	3.0	3.6	0.3	-0.1	-0.3
<b>Poland</b>	-2.0	6.9	5.3	0.2	3.0	3.4	-0.3	0.4	0.0
<b>Ukraine</b>	-3.8	3.4	-28.8	4.8	3.2	6.5	0.0	0.0	0.0

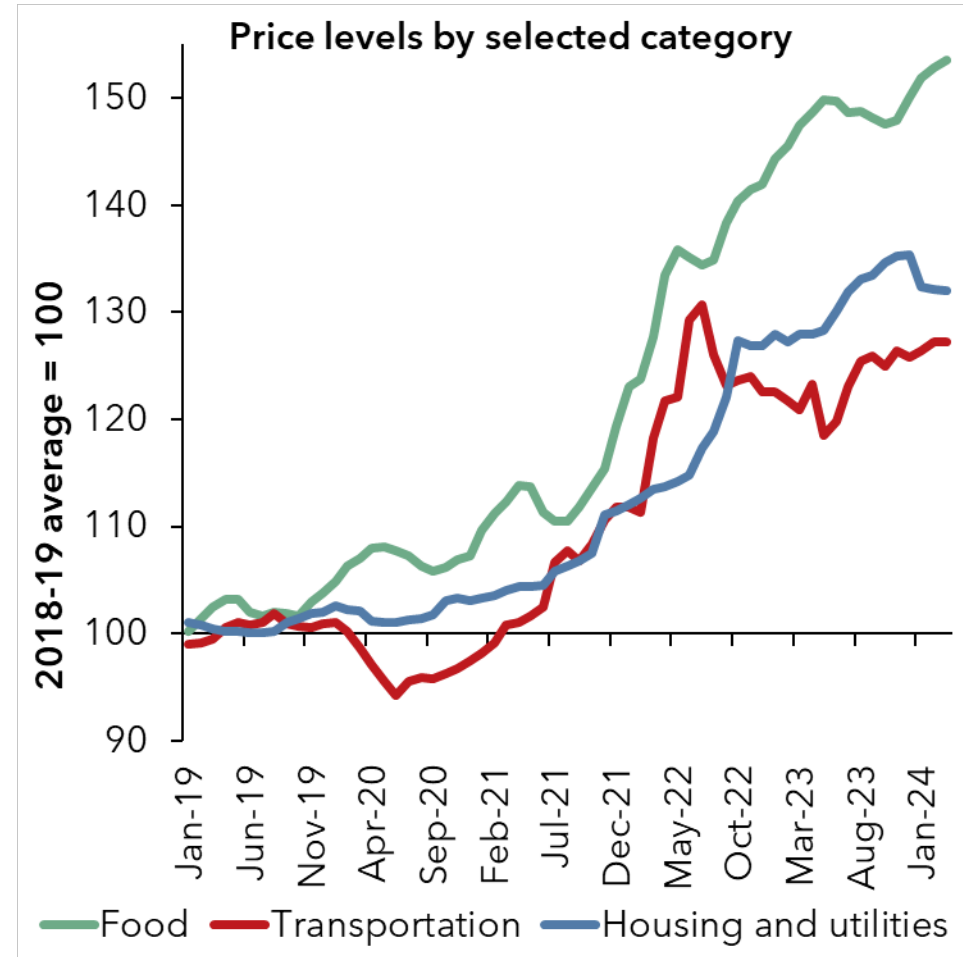
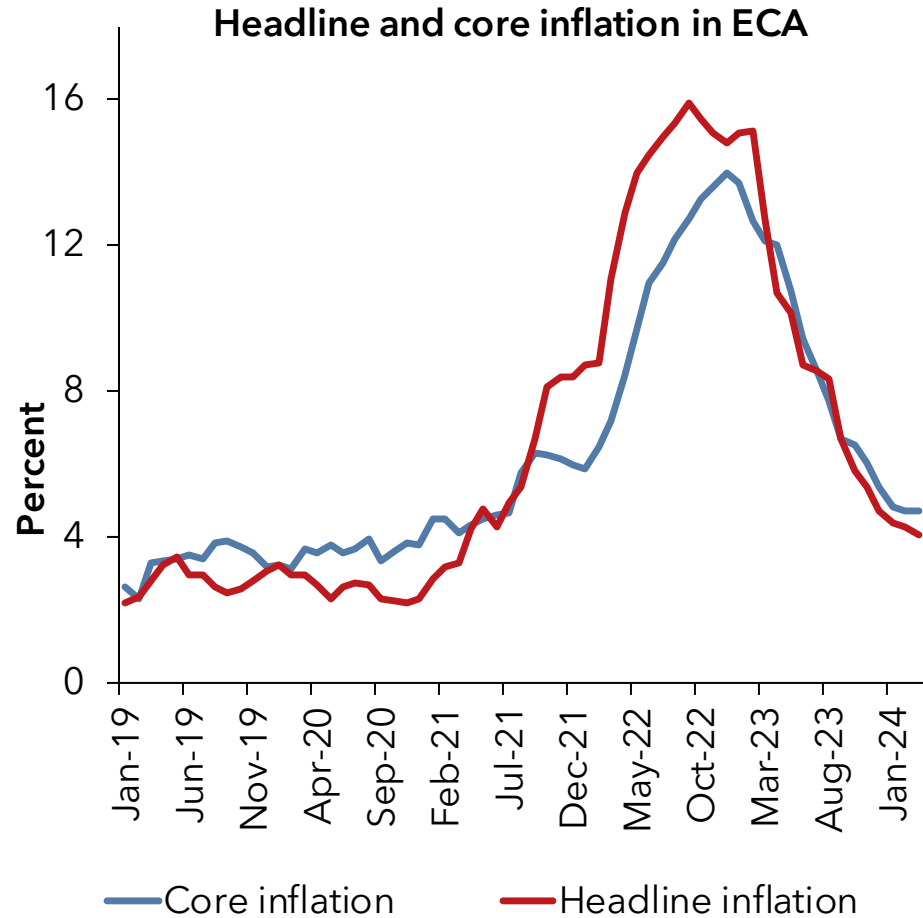
Source: World Bank.

Note: GDP is measured in average 2010–19 prices and market exchange rates.

e = estimates; f = forecast; GDP = gross domestic product.

a. Includes Bulgaria, Croatia, Poland, and Romania. b. Includes Albania, Bosnia and Herzegovina, Kosovo, Montenegro, North Macedonia, and Serbia. c. Includes Belarus and Moldova. d. Includes Armenia, Azerbaijan, and Georgia. e. Includes Kazakhstan, the Kyrgyz Republic, Tajikistan, and Uzbekistan.

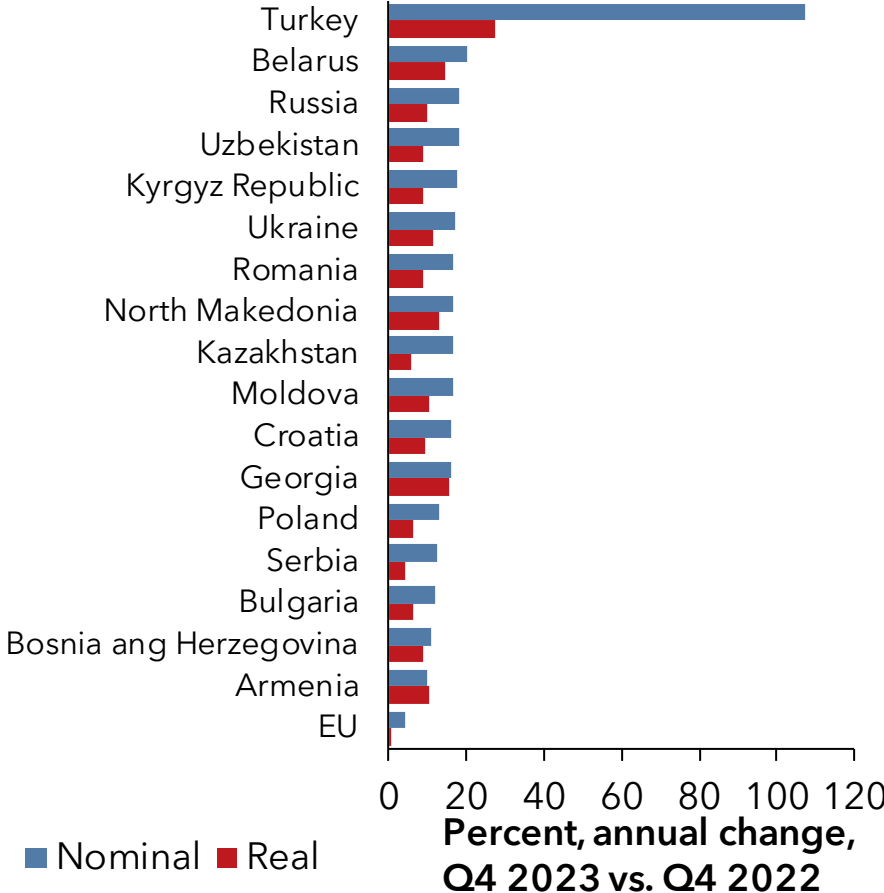
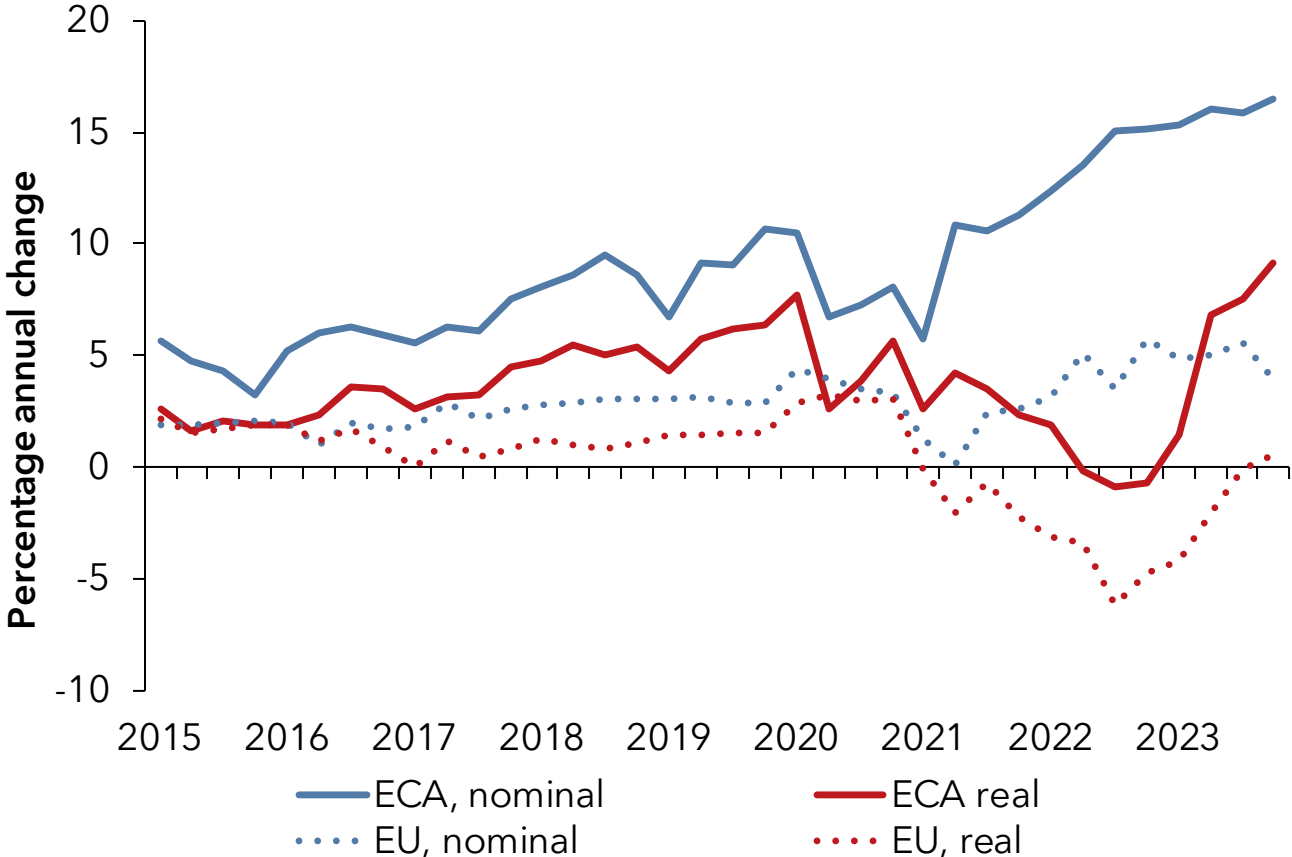
# Inflation is sharply lower, but price levels remain high



Source: Haver Analytics; World Bank.  
Note: Medians, last observation in March 2024

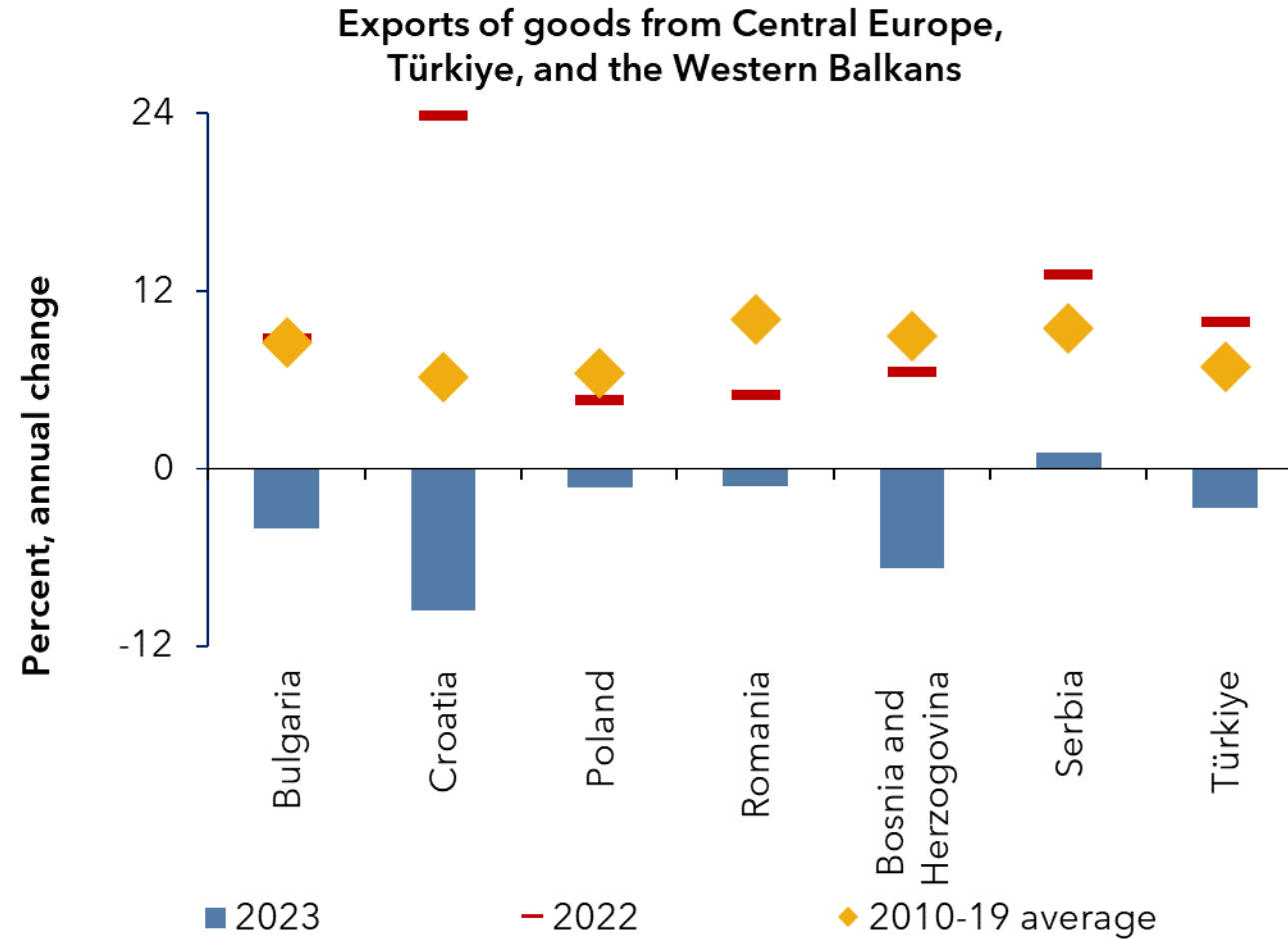
# Rising real wages amid tight labor markets support consumption

Growth of nominal and real wages



Source: Eurostat; Haver Analytics; National Statistical offices; World Bank  
 Note: Seasonally adjusted data. Real wages are nominal wages adjusted with consumer price index. EU = European Union.

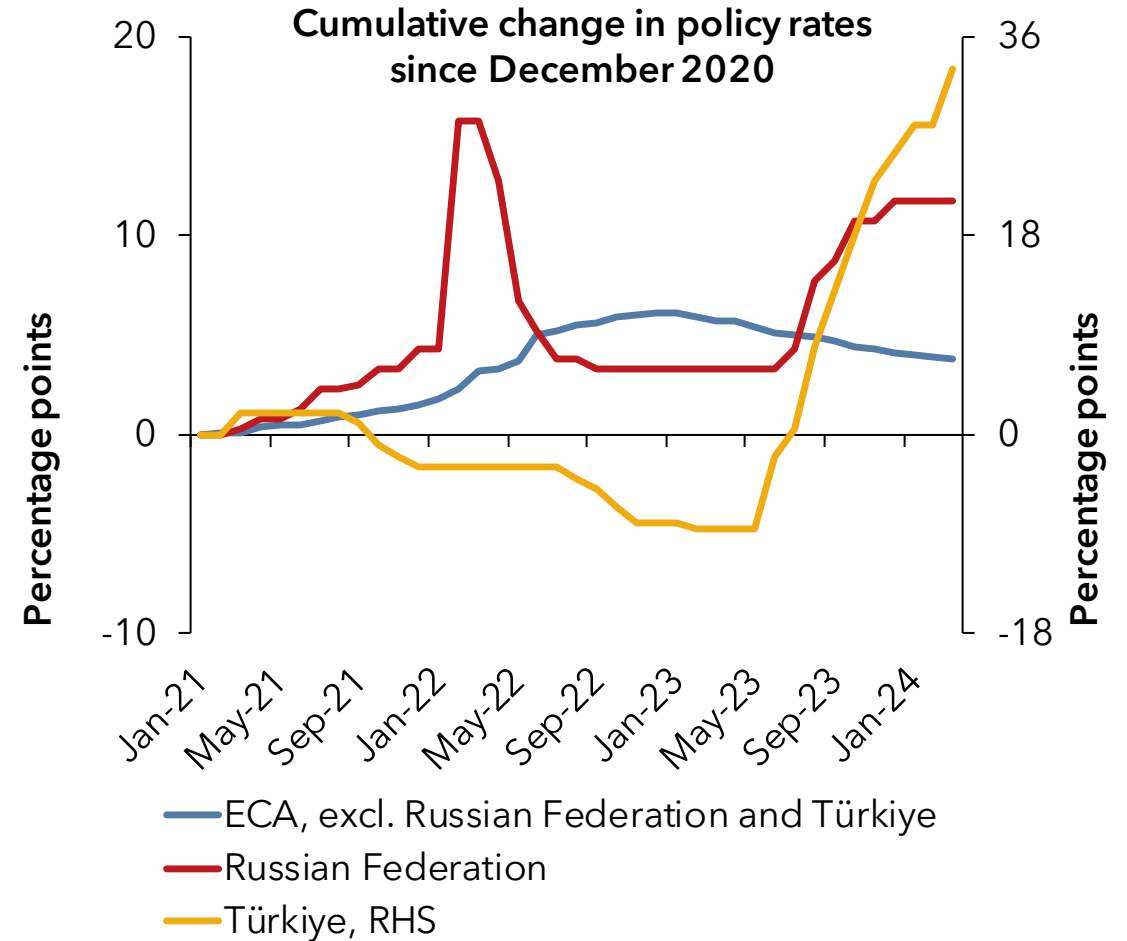
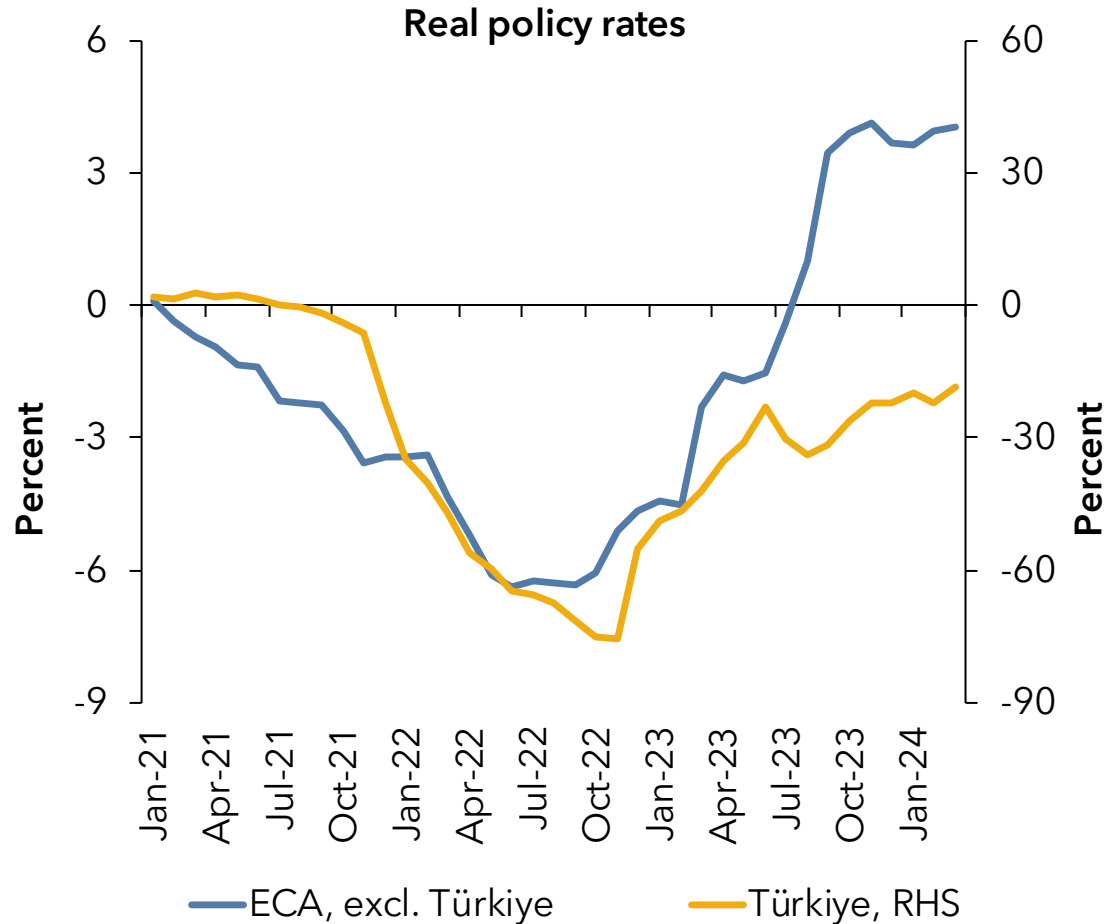
# Weaker exports because of slower growth in trading partners



Source: Eurostat; World Bank.

Note: Volume of exports of goods. For Türkiye, the data show exports of goods and services.

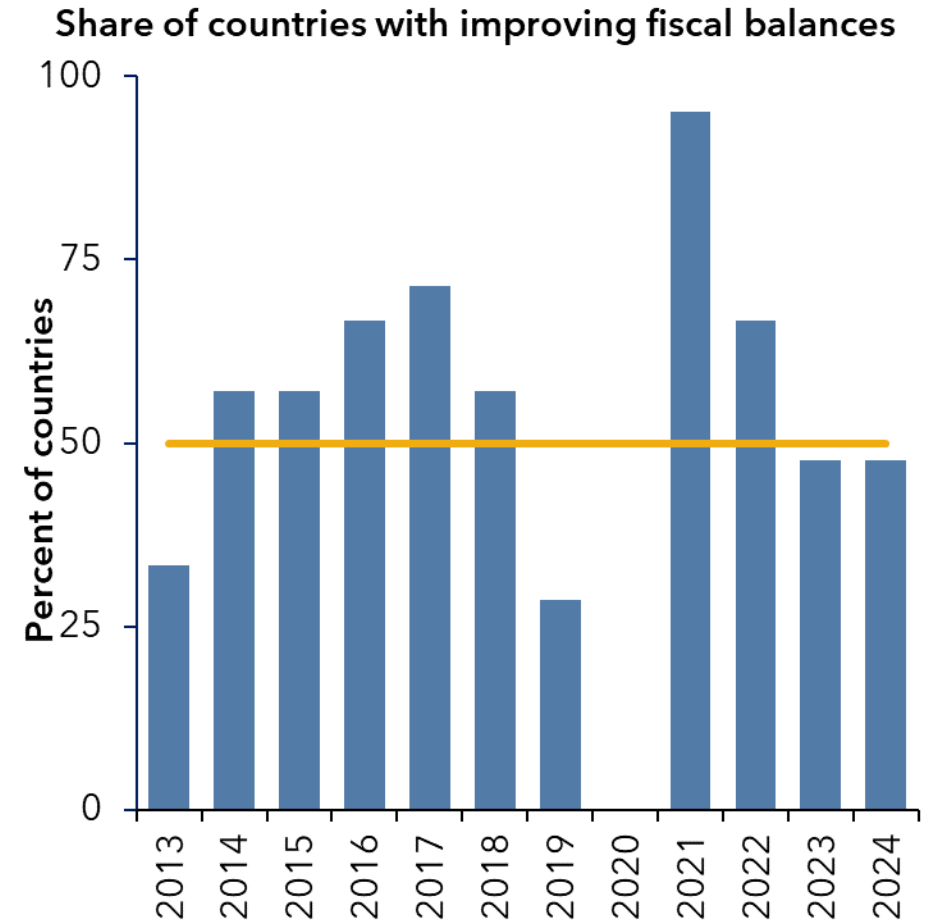
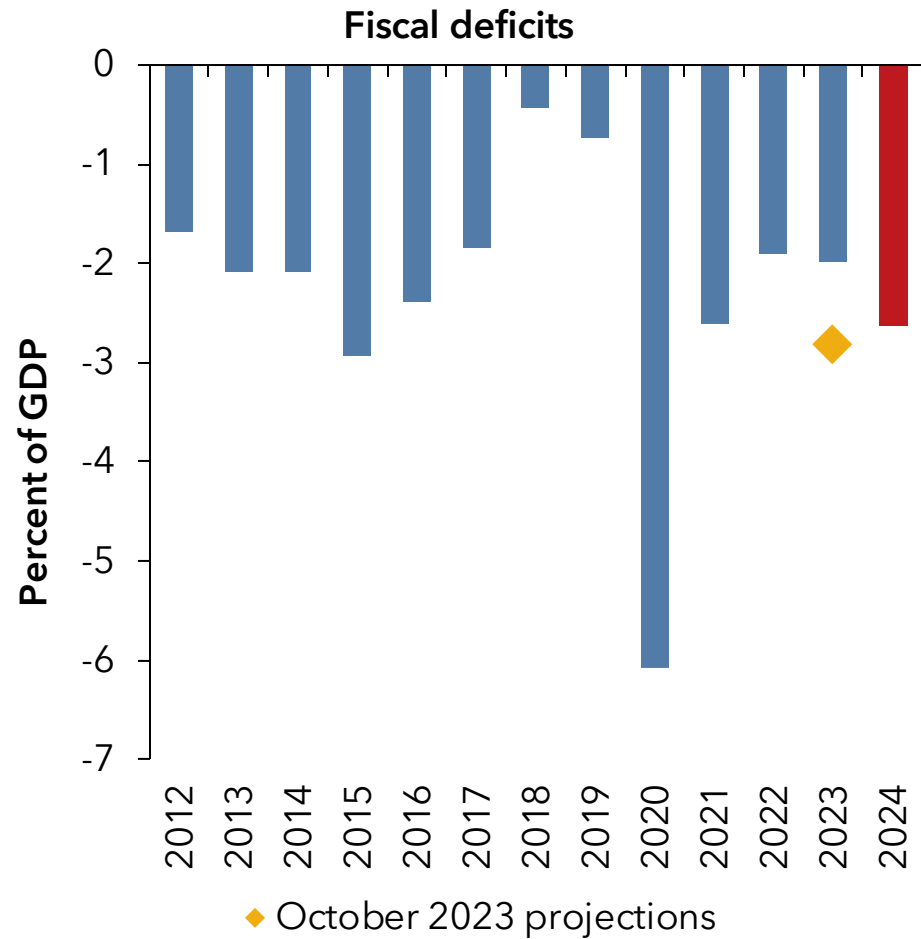
# Monetary policies have diverged across the region



Source: Haver Analytics; World Bank

Note: Left panel: Inflation adjusted nominal policy rates, ECA shows median. Right panel: ECA excluding the Russian Federation and Türkiye denotes the average for 15 economies.

# Better fiscal outcomes in 2023, but consolidation mostly deferred

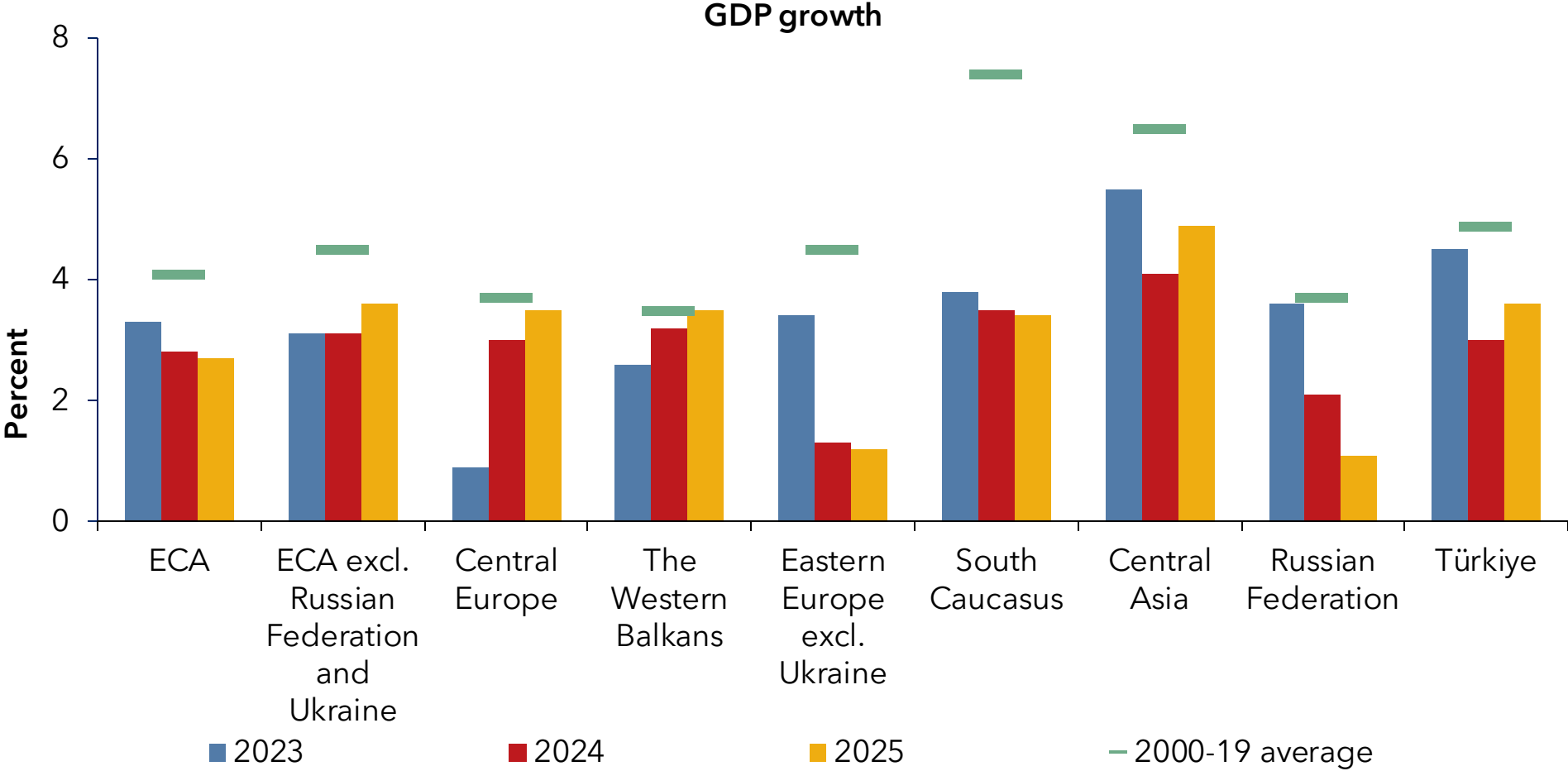


Source: World Bank

Note: Left panel: October 2023 projections are from the October 2023 edition of the Macro Poverty Outlooks. Unweighted averages, sample excludes Ukraine. Right panel: share of countries with lower fiscal deficits (or higher fiscal surpluses) compared to the previous year, sample excludes Ukraine.



# Growth in 2024-25: better than earlier feared but below ambitions



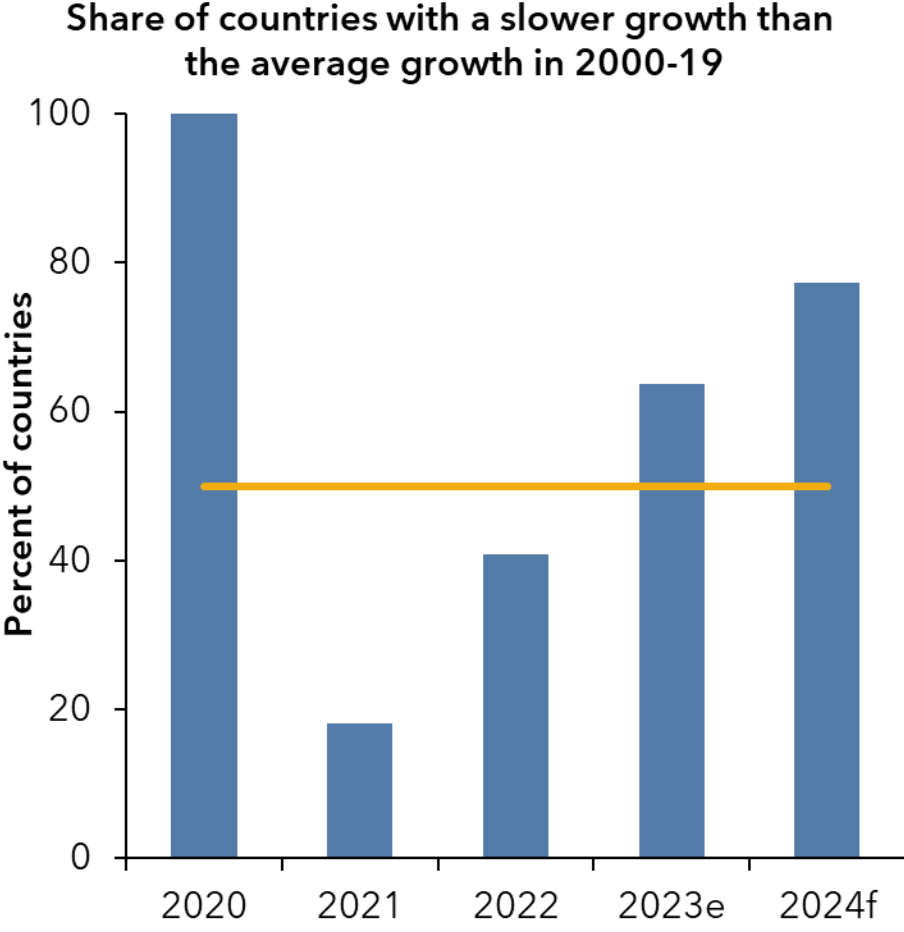
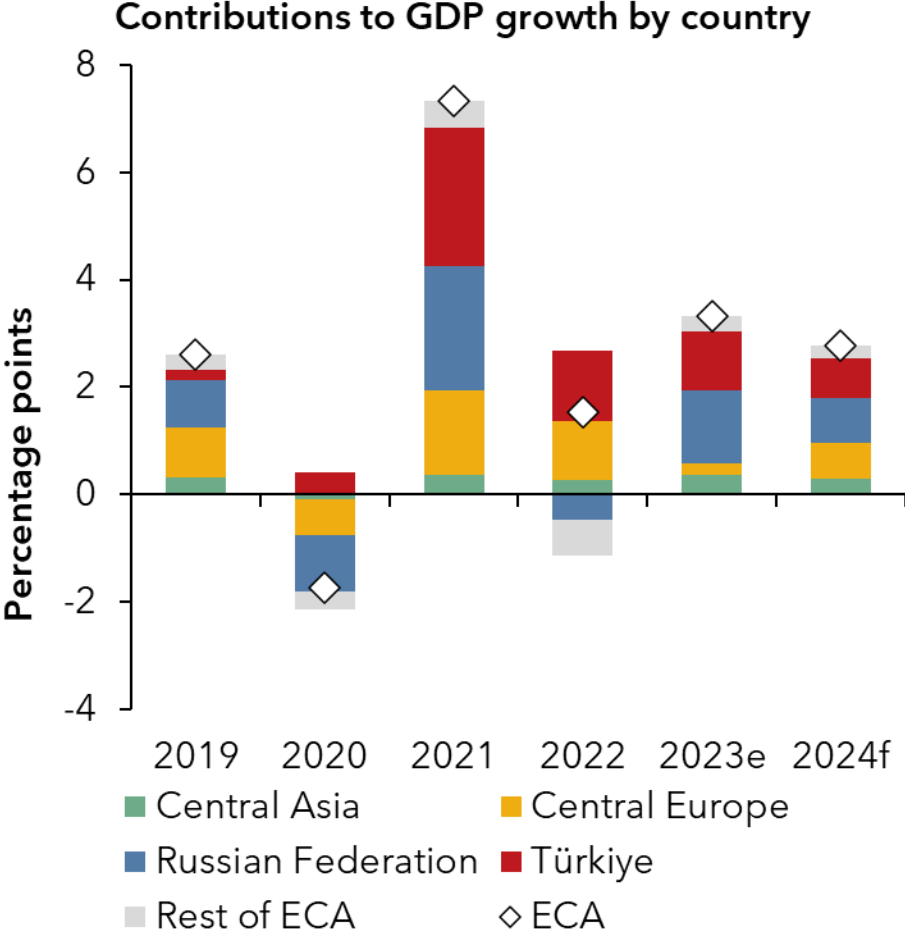
Source: World

Note: GDP is measured in average 2010–19 prices and market exchange rates.

Central Europe includes Bulgaria, Croatia, Poland, and Romania; The Western Balkans includes Albania, Bosnia and Herzegovina, Kosovo, Montenegro, North Macedonia, and Serbia; Eastern Europe includes Belarus and Moldova; South Caucasus includes Armenia, Azerbaijan, and Georgia; Central Asia includes Kazakhstan, the Kyrgyz Republic, Tajikistan, and Uzbekistan.

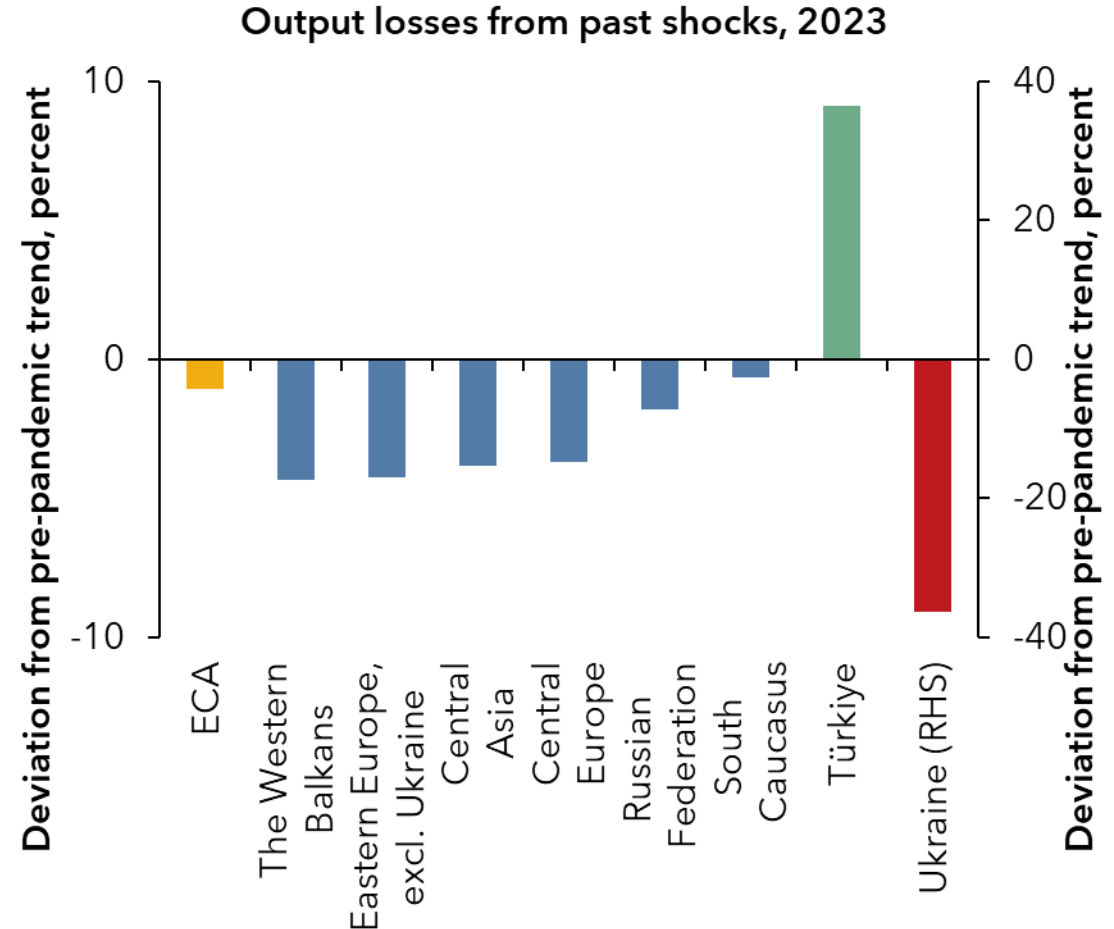
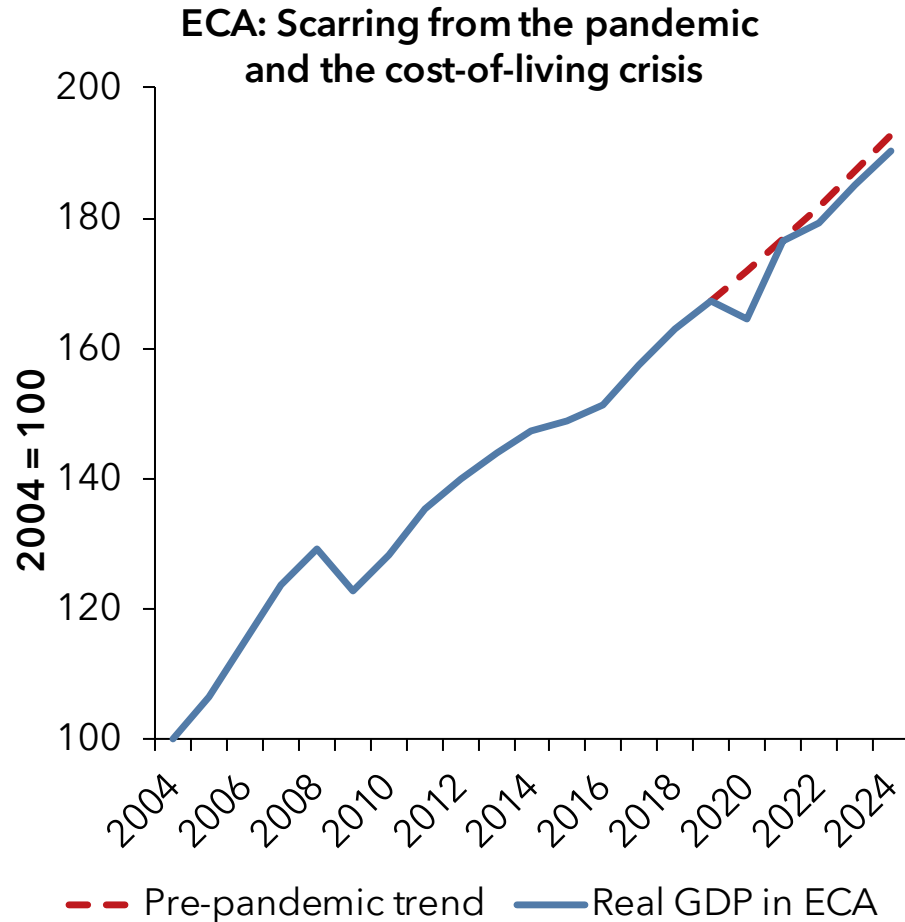


# Growth in 2024 supported by stronger recovery in Central Europe



Source: World  
 Note: GDP is measured in average 2010–19 prices and market exchange rates. Left panel: Central Europe includes Bulgaria, Croatia, Poland, and Romania; Central Asia includes Kazakhstan, the Kyrgyz Republic, Tajikistan, and Uzbekistan.

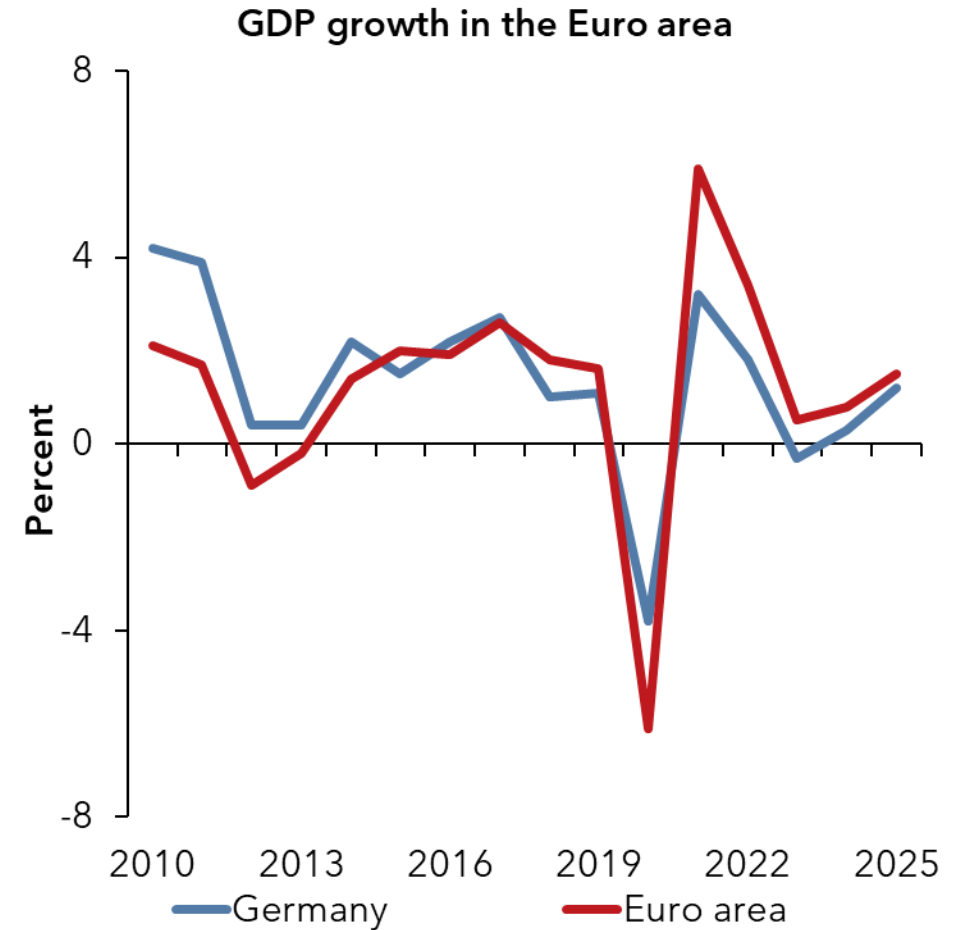
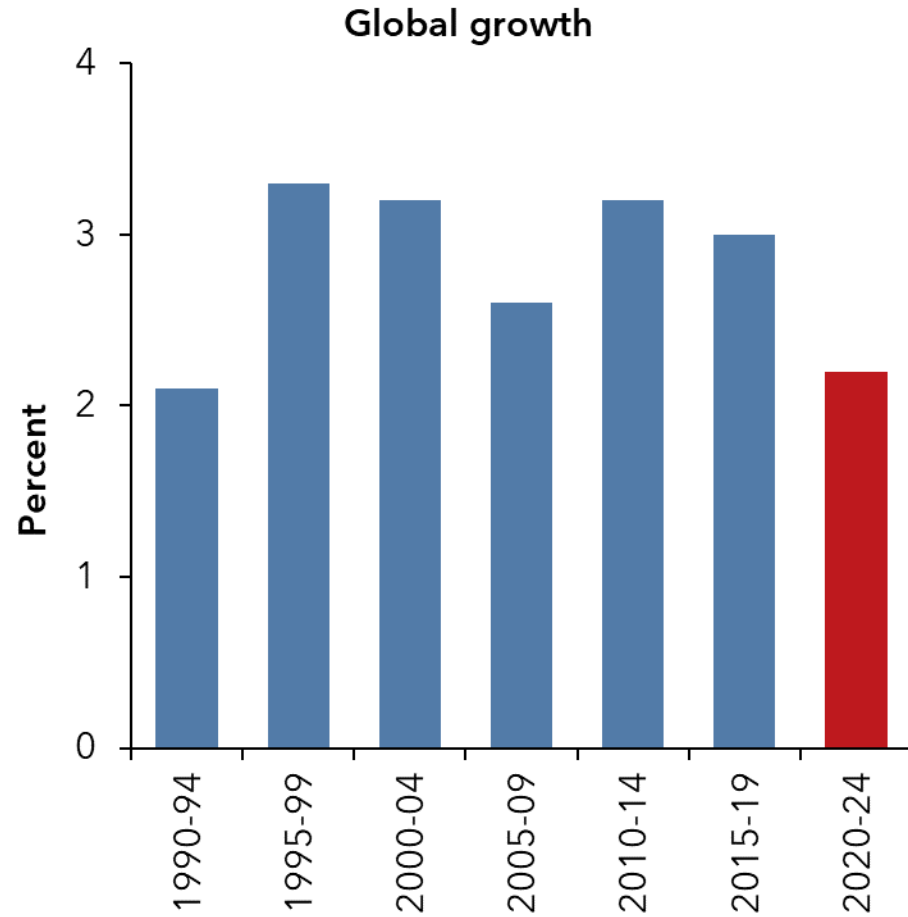
# The gap with the pre-pandemic GDP trend has yet to be closed



Source: World Bank.

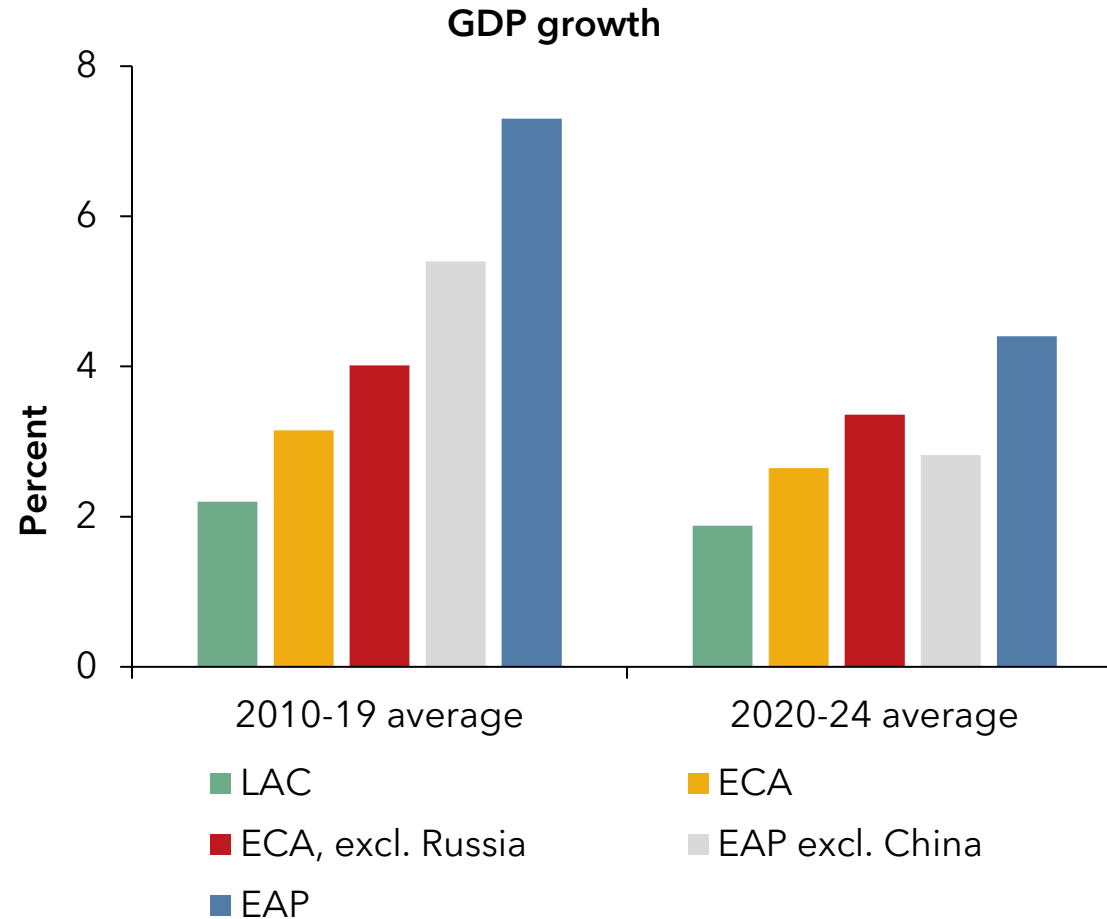
Note: GDP is measured in average 2010–19 prices and market exchange rates. The pre-pandemic GDP trend is calculated using GDP growth forecasts from the January 2020 Global Economic Prospects reports. Values for 2023 are estimates and those for 2024 are forecasts from the Spring 2024 Macro Poverty Outlooks.

# Prospects for global growth are at the lowest level in decades



Source: European Commission; World Bank..

# ECA's growth: higher than in LAC, moderate vs. EAP with China



# Conclusions: Recent Developments, Policies, and Outlook

## **Moderate growth is the greatest challenge for ECA**

- Growth of 2.8% in 2024-25 vs 4.1% on average for 2000-19
- Weak expansion in the Euro area, sluggish in China
- Global tensions, geo-economic fragmentation
- Convergence has slowed for many of the ECA countries

## **Inflation still not vanquished**

- Higher wages amid tight labor markets and migration supporting consumption and inflation.
- Risks to competitiveness from higher wages without productivity growth

## **Countries need to rebuild fiscal space**

- Unanticipated inflation helped reduce debt levels in many countries
- But spending pressures are not easing: aging, healthcare, education
- Investment needs are huge, especially with the climate transition

# Part 2. Unleashing the Power of the Private Sector

## **ECA's transition from plan to market**

- Broad and deep structural reforms and the emergence of private initiative
- Since 1990, 12 ECA countries joined the EU and almost all are high income economies by now

## **Among the middle-income economies of ECA, productivity growth has slowed**

- Reform progress, technology adoption, and innovation have weakened in ECA
- Income convergence has slowed

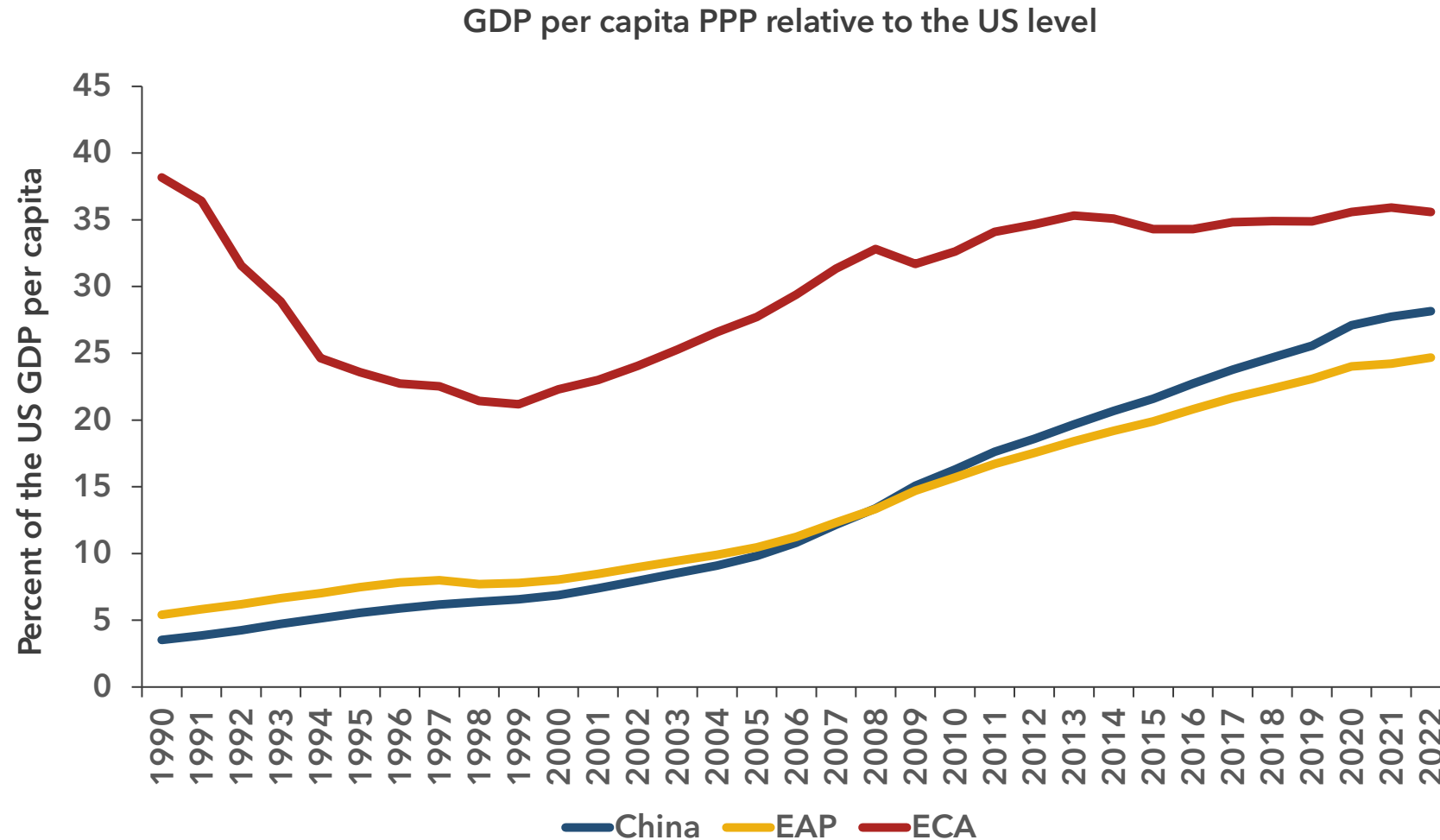
## **ECA has plenty of room to make up on business dynamism and innovation**

- Rates of firm entry and exit lag those in the AE in Europe. Firms do not grow much.

## **Boosting business dynamism in ECA will require addressing several challenges, including:**

- Upgrading the competition environment
- Reducing state involvement in the economy
- Boosting dramatically the quality of education
- Strengthening the availability of finance

# ECA's income convergence has largely stopped



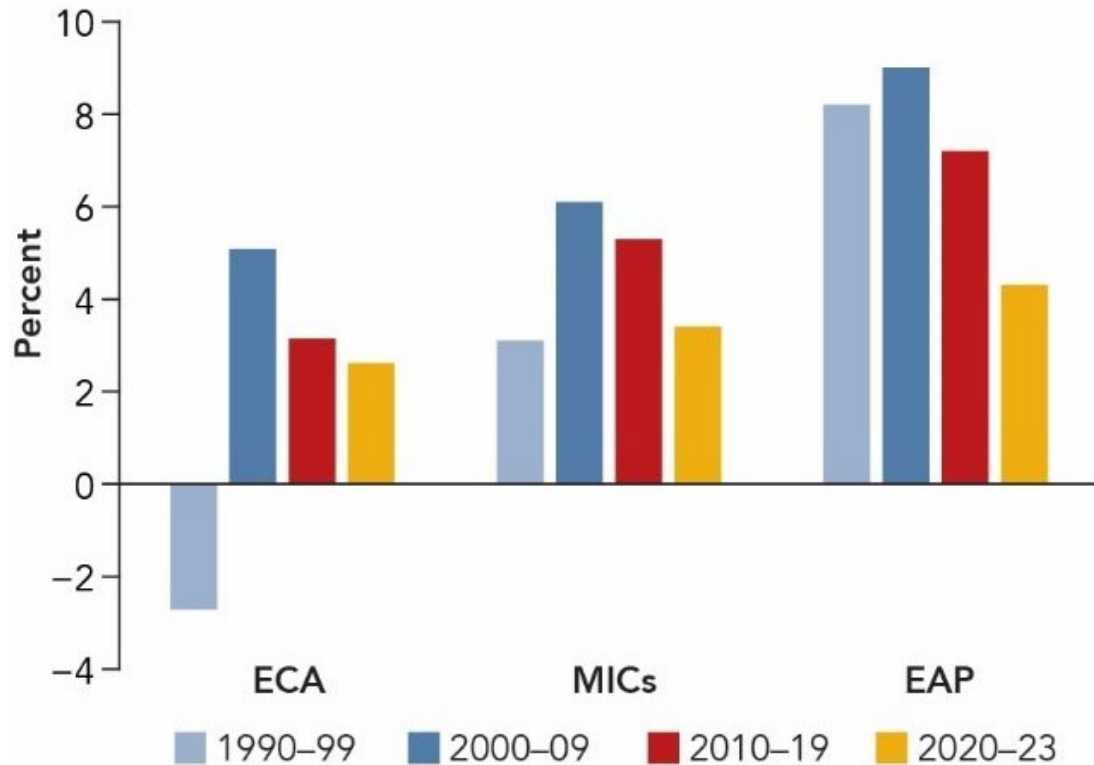
Source: World Bank WDI.

Note: GDP per capita is measured at PPP in constant 2017 international \$. ECA = Europe and Central Asia; EAP = East Asia and Pacific.

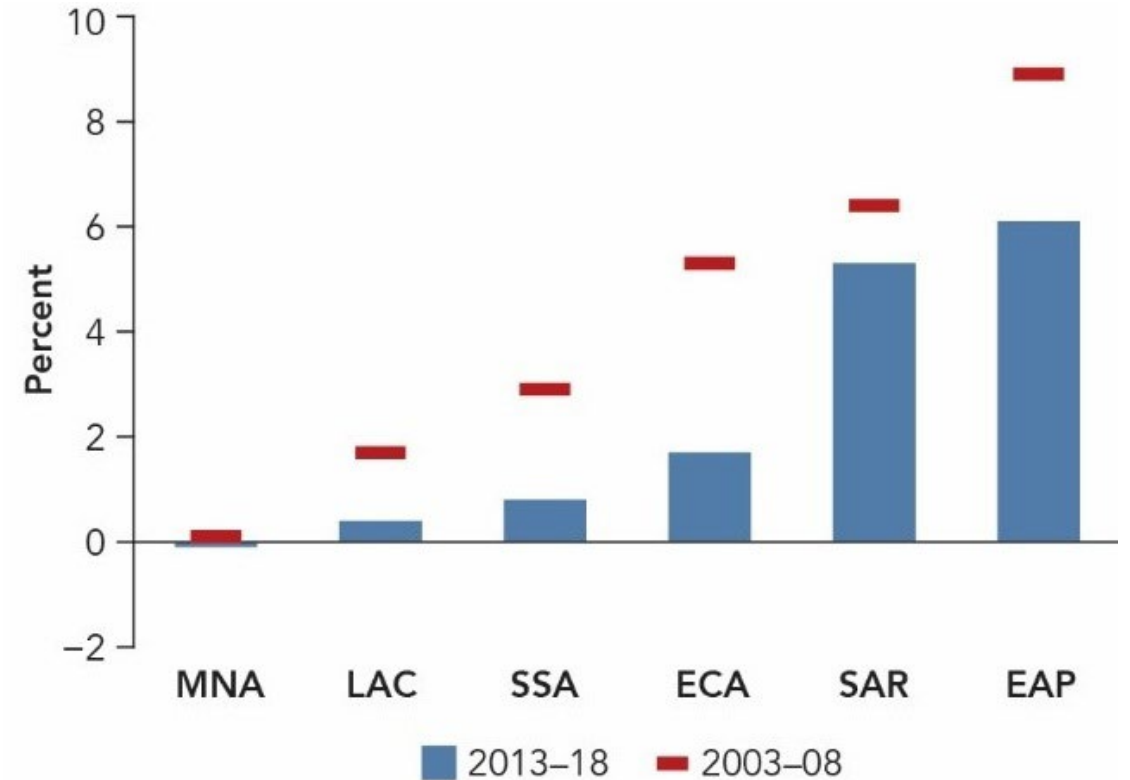


# Slowing growth and income convergence

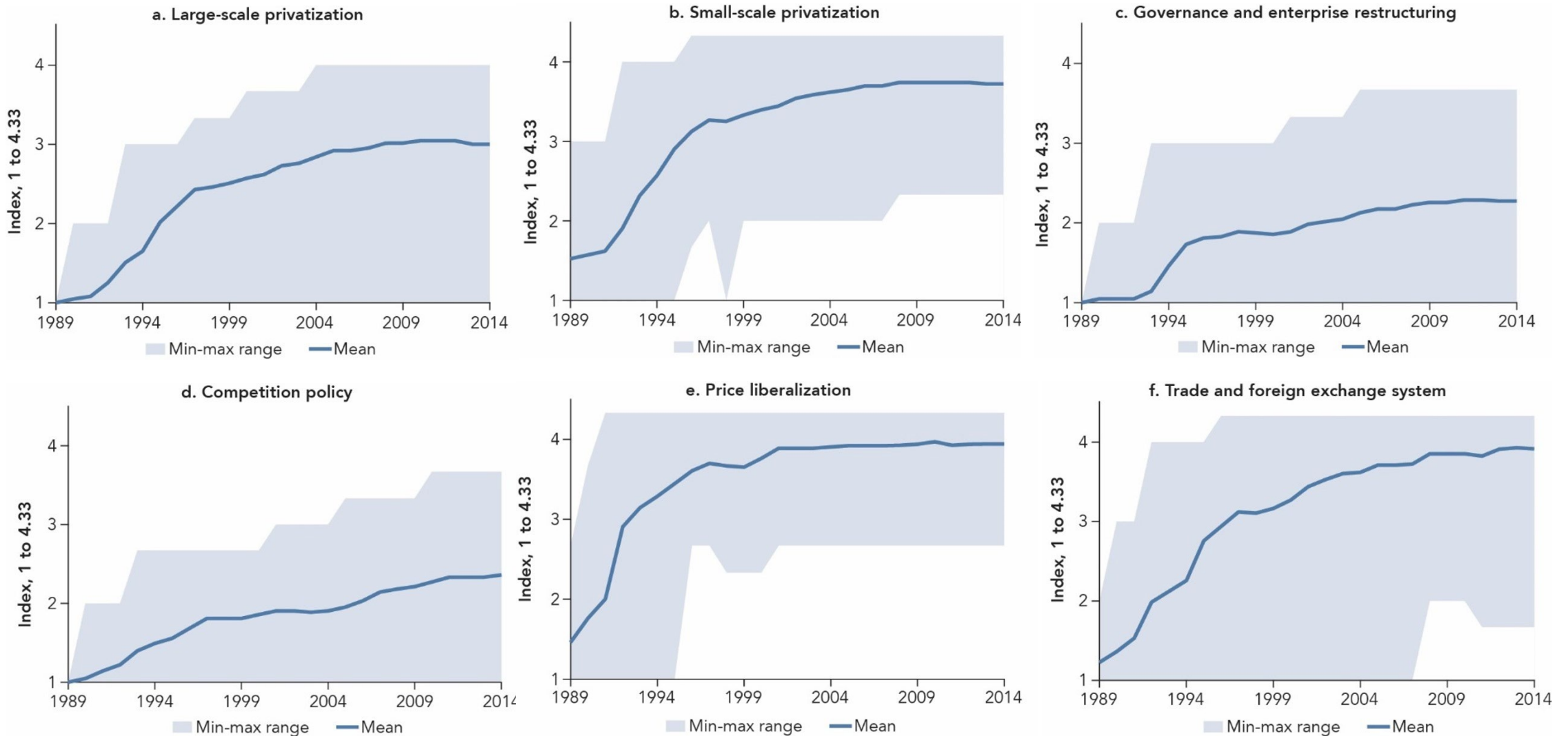
## Average growth since 1990



## Productivity growth

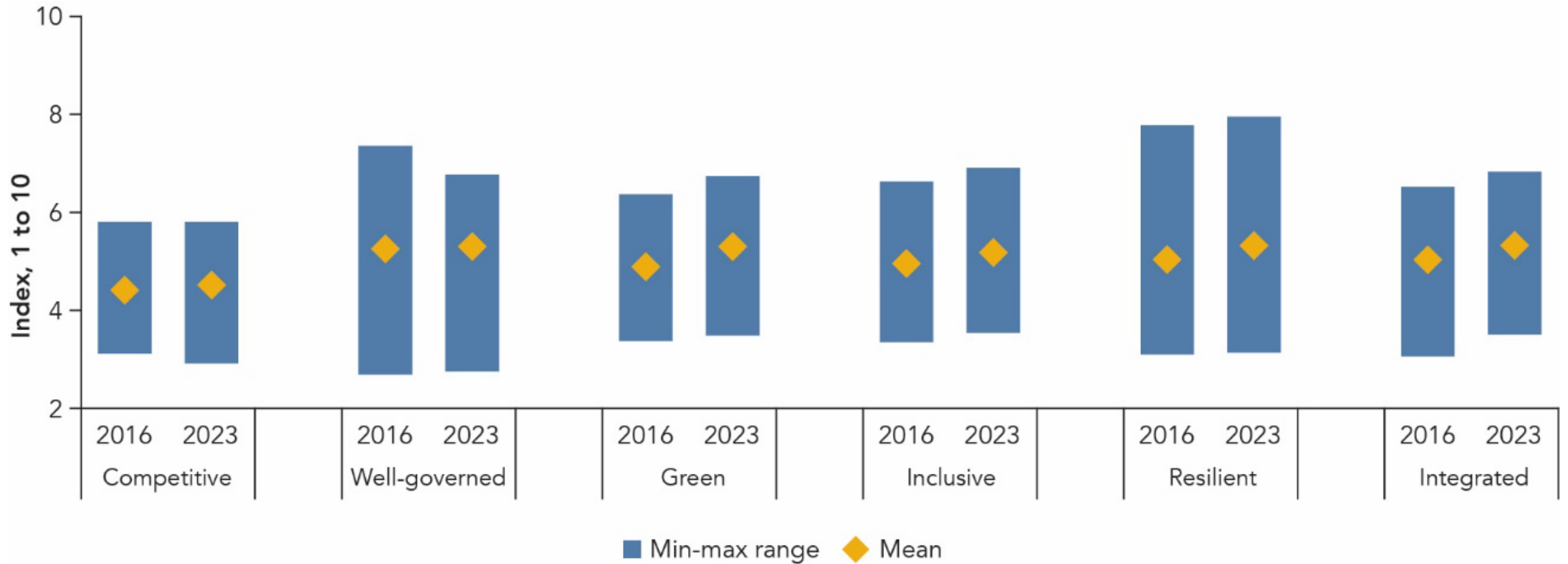


# Progress on transition indicators moderated over time, 1989–2014



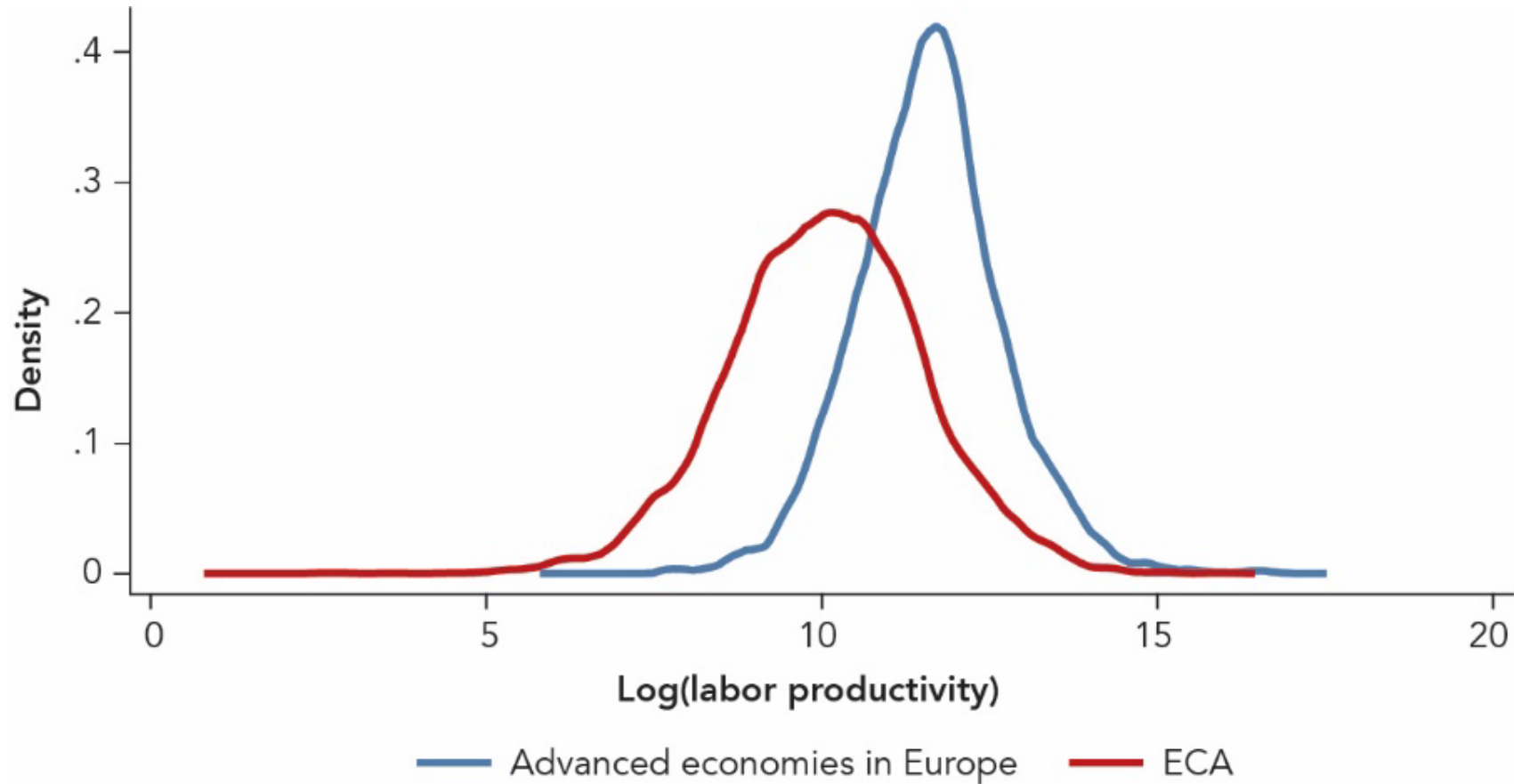
Source: EBRD transition indicators, 1989–2014 (latest year available).

# Progress on the transition qualities has been modest since 2016



Source: EBRD, 2016 (first year available) to 2023.

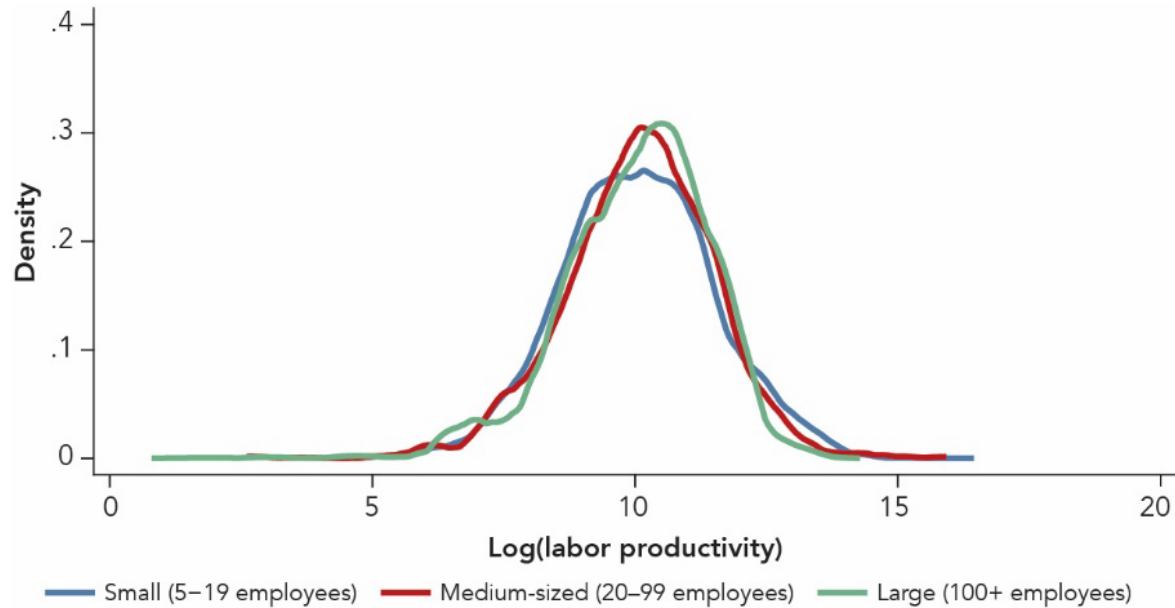
# Firm productivity in ECA lags that in AE in Europe



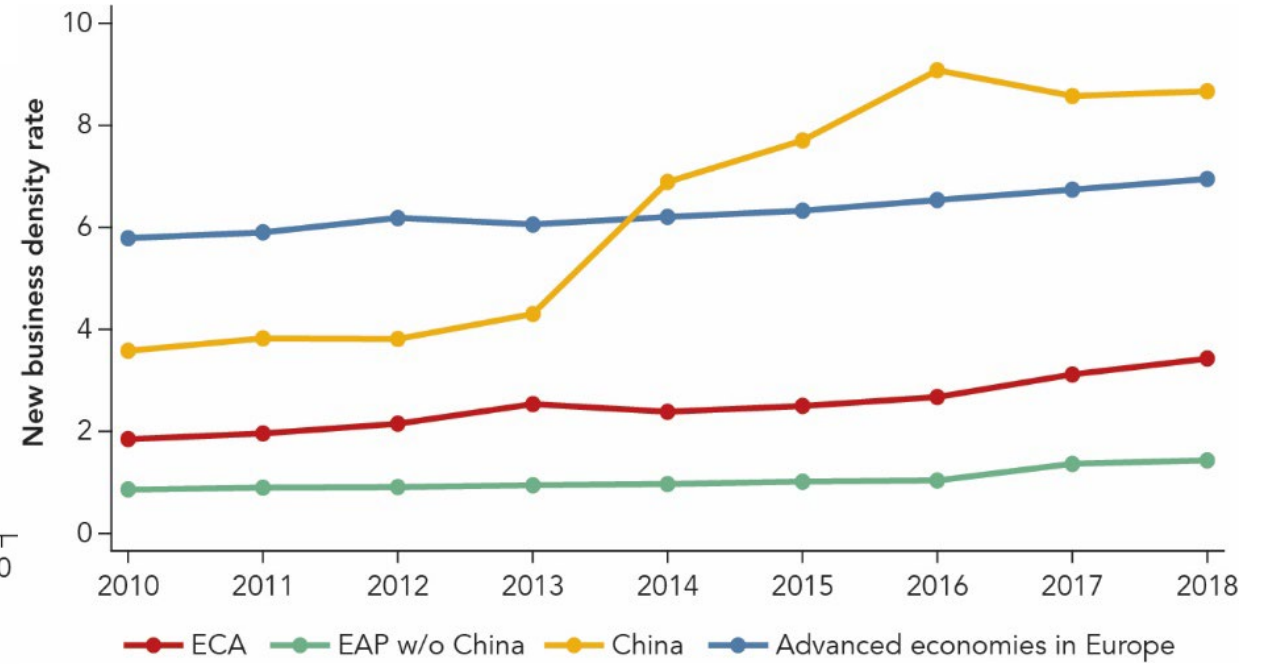
Source: Calculations based on data from the latest World Bank Enterprise Surveys (for most countries, 2019).

# Business dynamism in ECA lags

Firm productivity in ECA does not vary by firm size

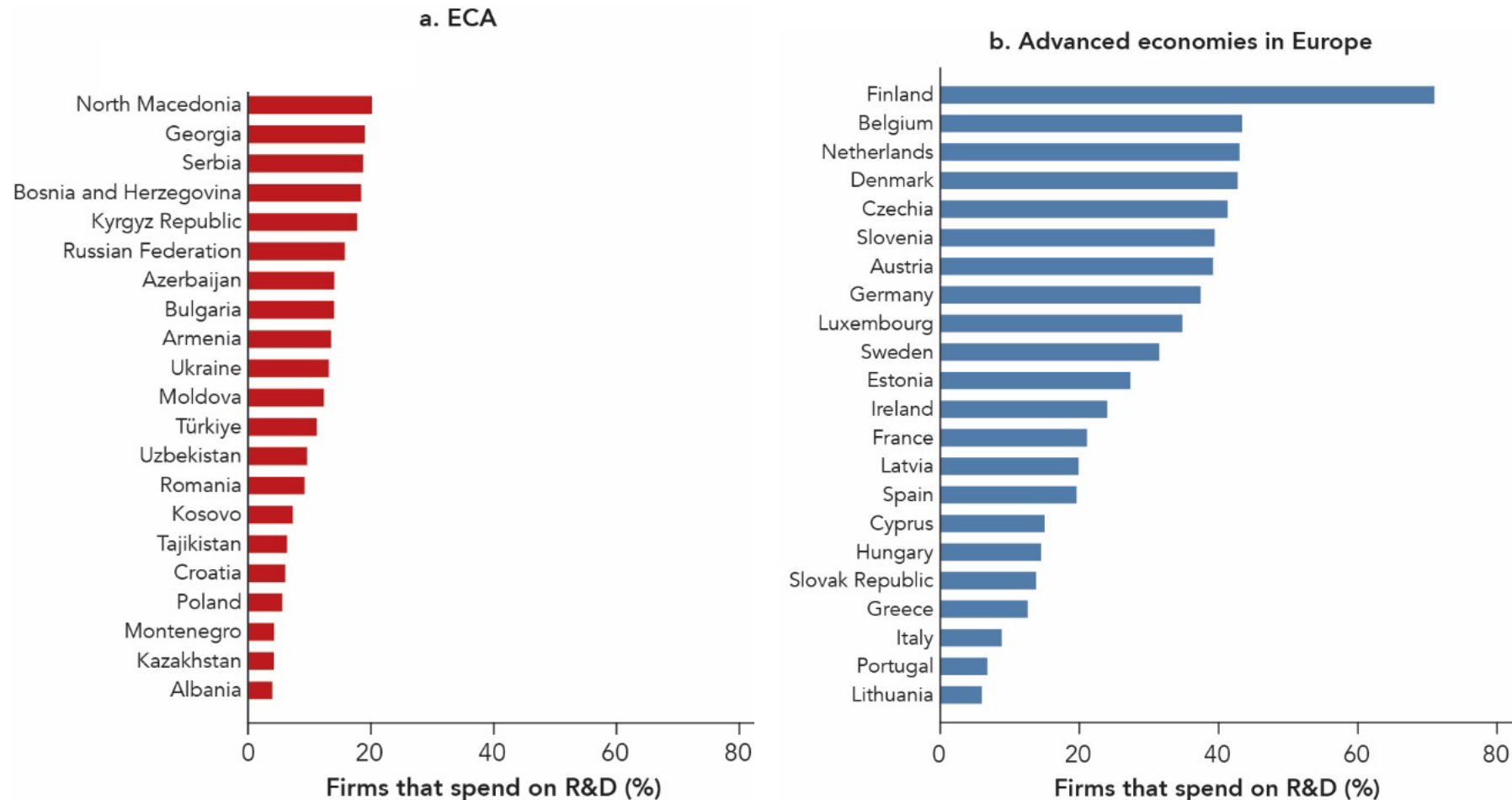


The new business density rate was little changed in ECA



# Innovation in ECA lags (I)

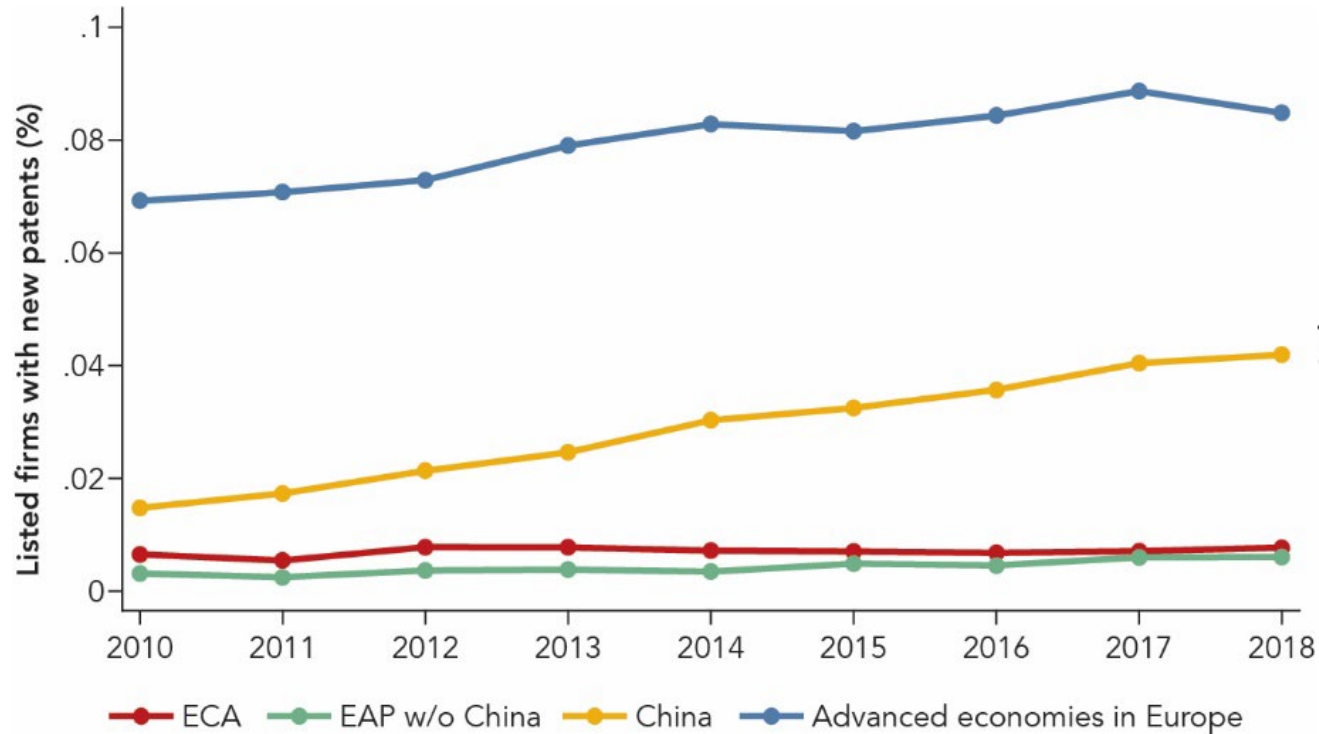
A lower share of firms spend on R&D in ECA compared to the advanced economies in Europe



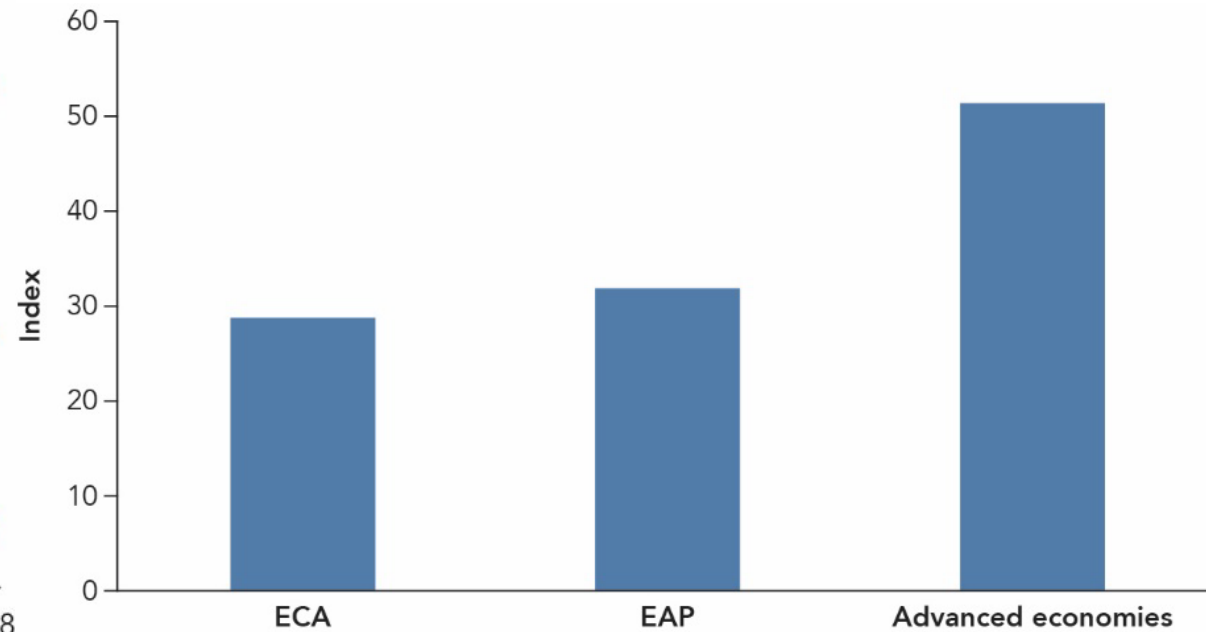
Source: Calculations based on data from the latest World Bank Enterprise Surveys (for most countries, 2019).

# Innovation in ECA lags (II)

## A widening gap in the share of listed firms with new patents



## ECA lags on the Global Innovation Index



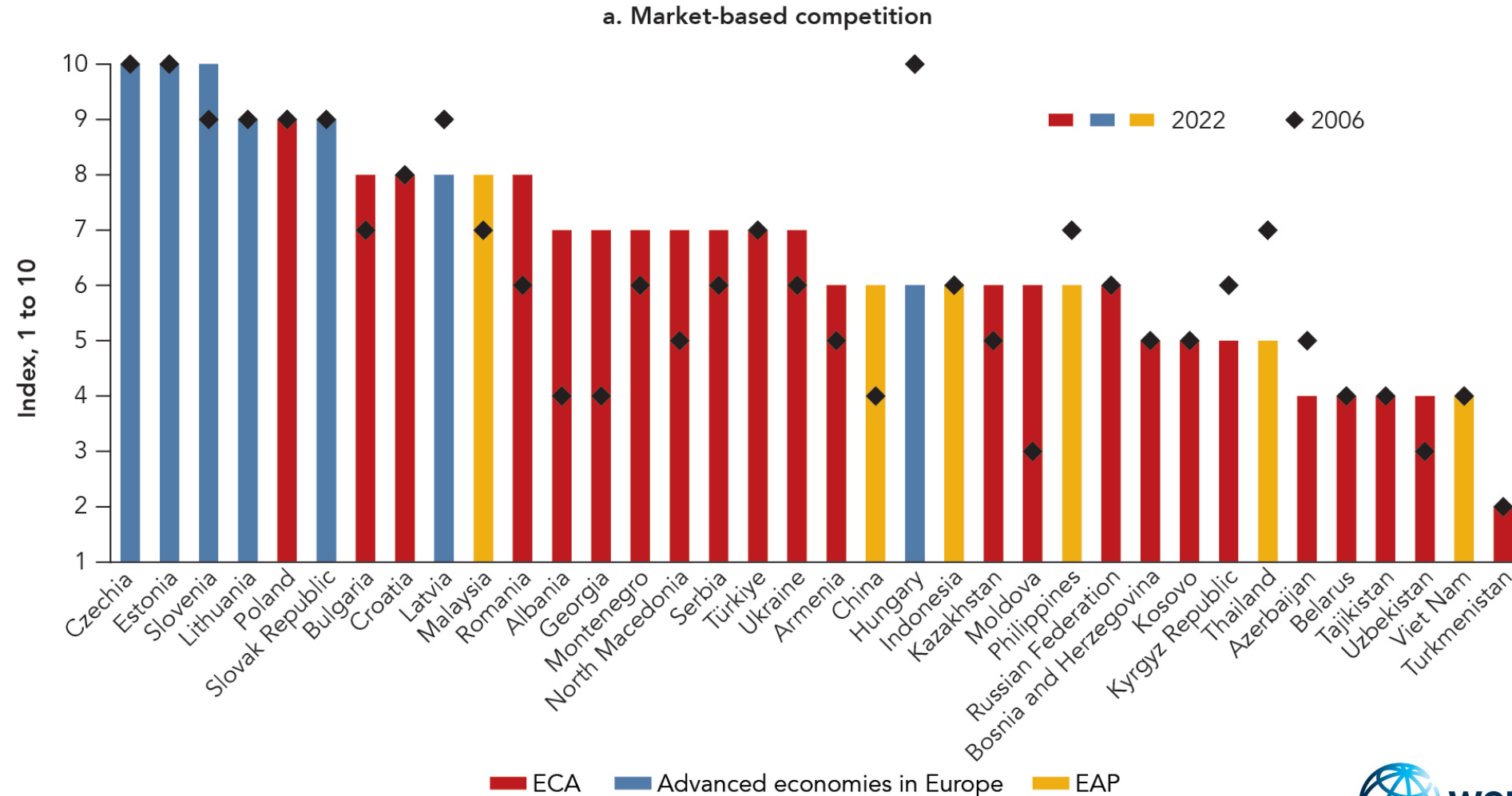
Source: Ayyagari, Demirgüç-Kunt, and Maksimovic 2022; Cheng 2019. Global Innovation Index, World Intellectual Property Organization (2023).

# Boosting Business Dynamism and Innovation in ECA



# I. Competition

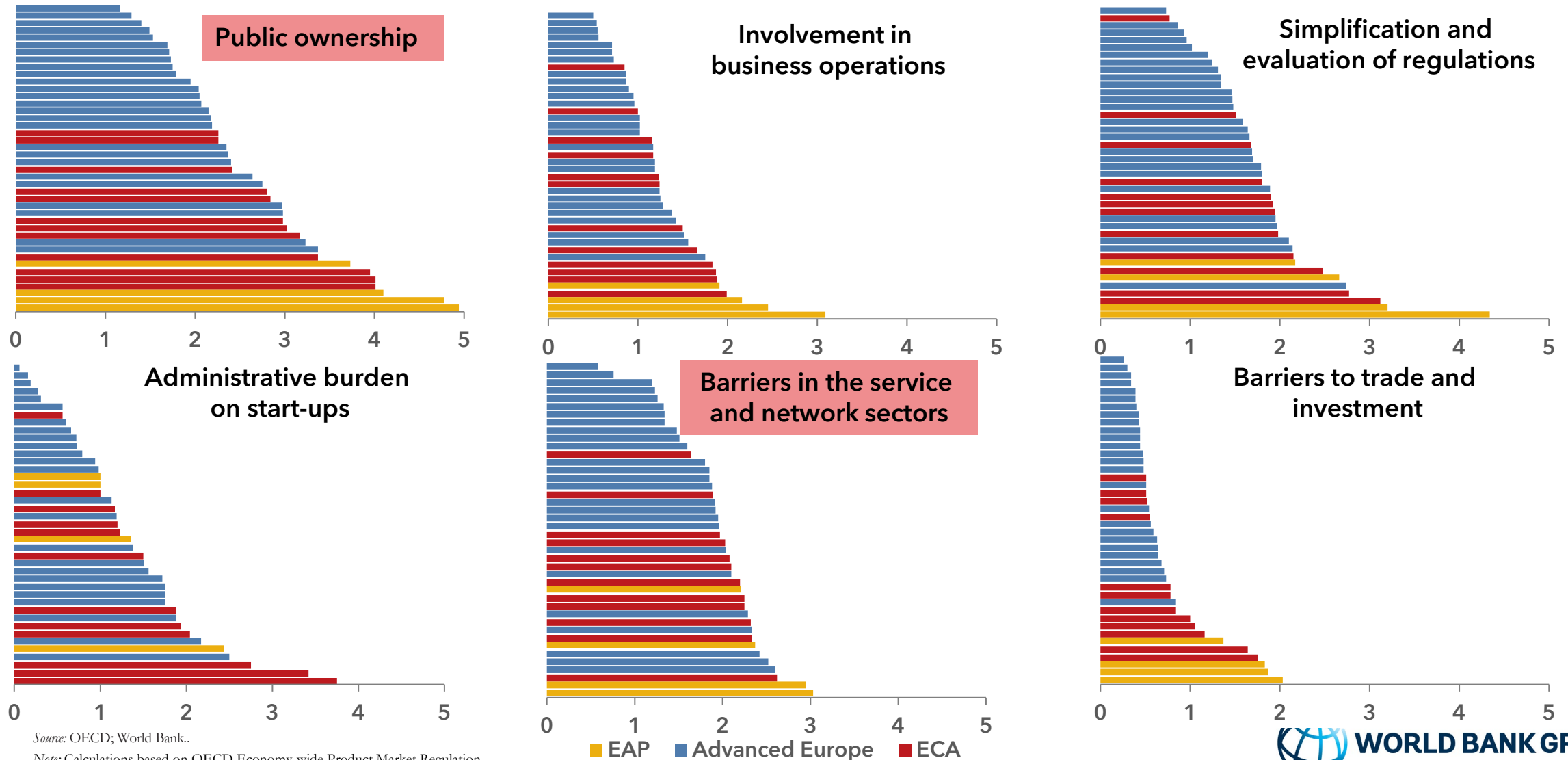
Most countries in ECA saw little change in the competition environment between 2006 and 2022



Source: Bertelsmann Stiftung Transformation Index (2022).

# I. Competition

Product market regulation in ECA needs to improve, especially in ...

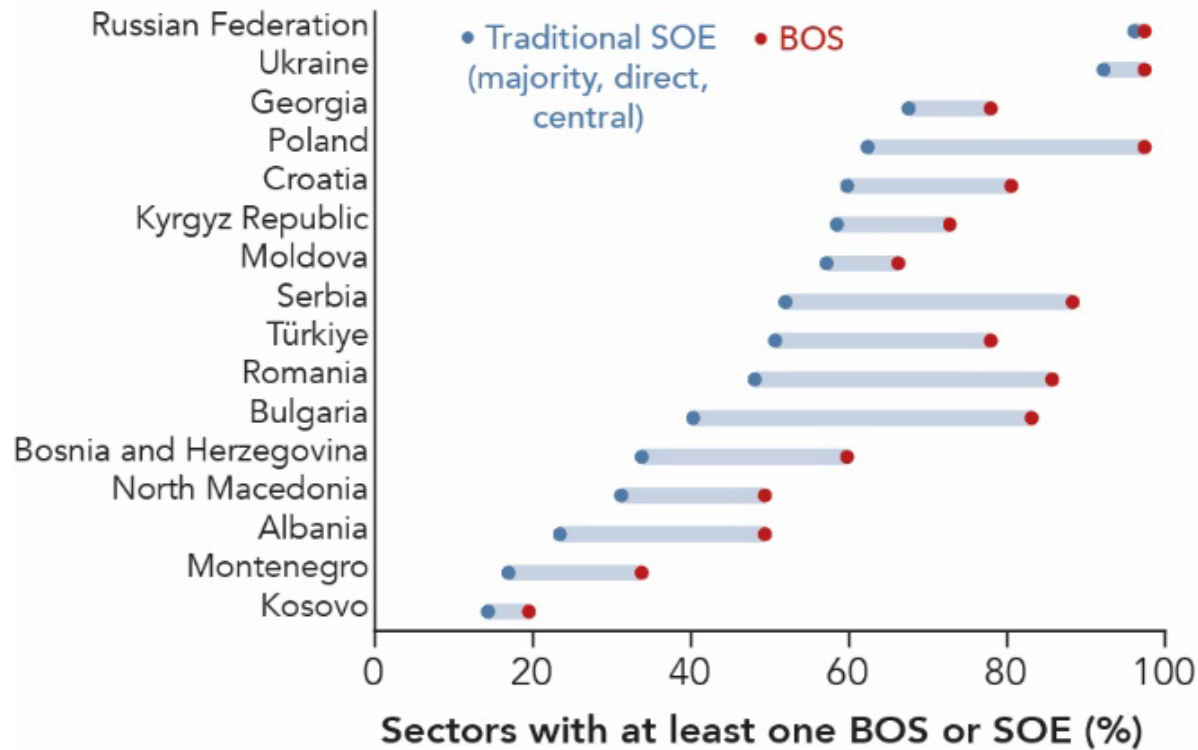


Source: OECD; World Bank.

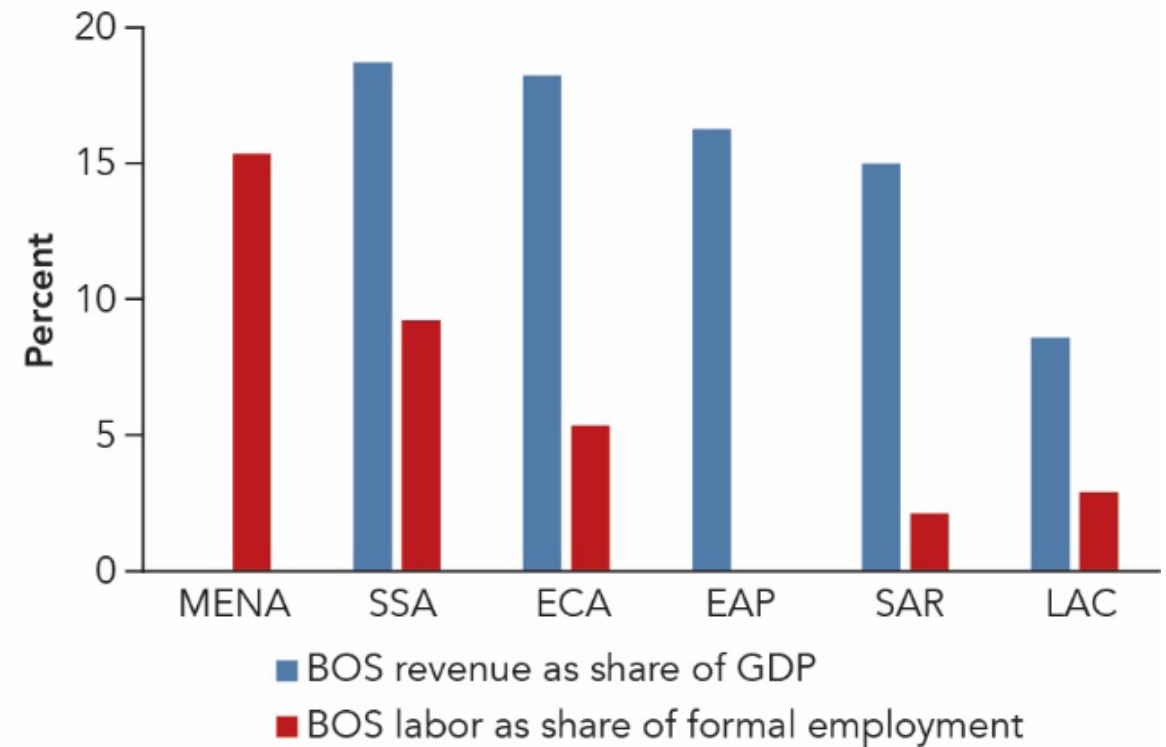
Note: Calculations based on OECD Economy-wide Product Market Regulation Indicators (2018).

# II. The role of the state in the economy is still substantial in ECA

a. The presence of BOS affects a significant proportion of economic sectors across ECA countries



b. ECA's BOS revenue as share of GDP and BOS labor as share of formal employment compared to other regions



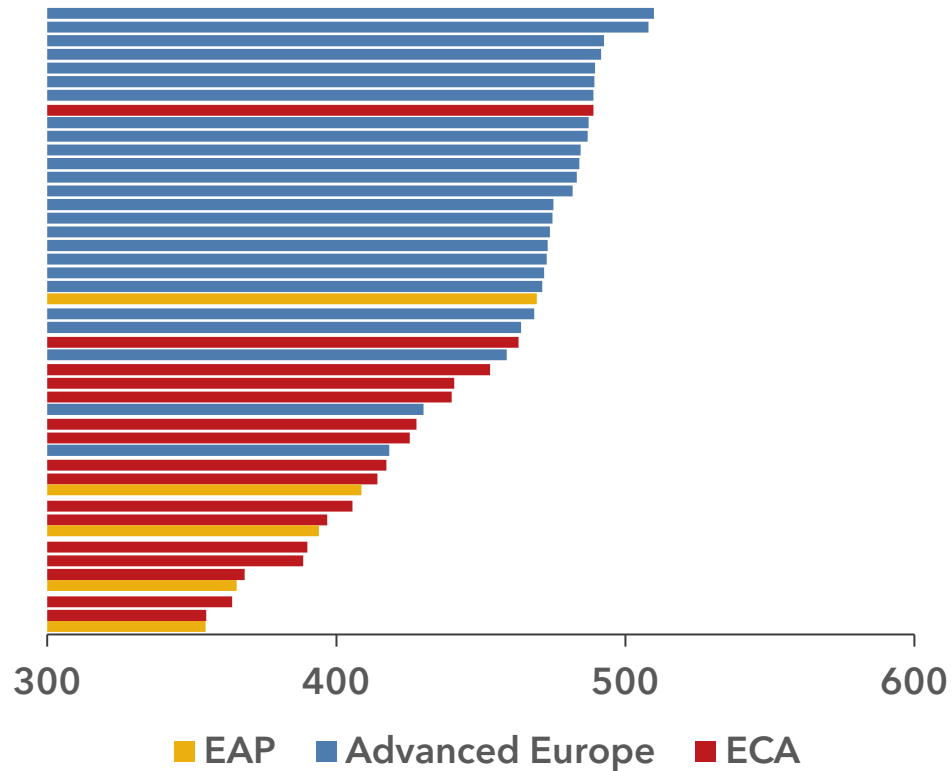
BOS: Business of the state

Source: World Bank.

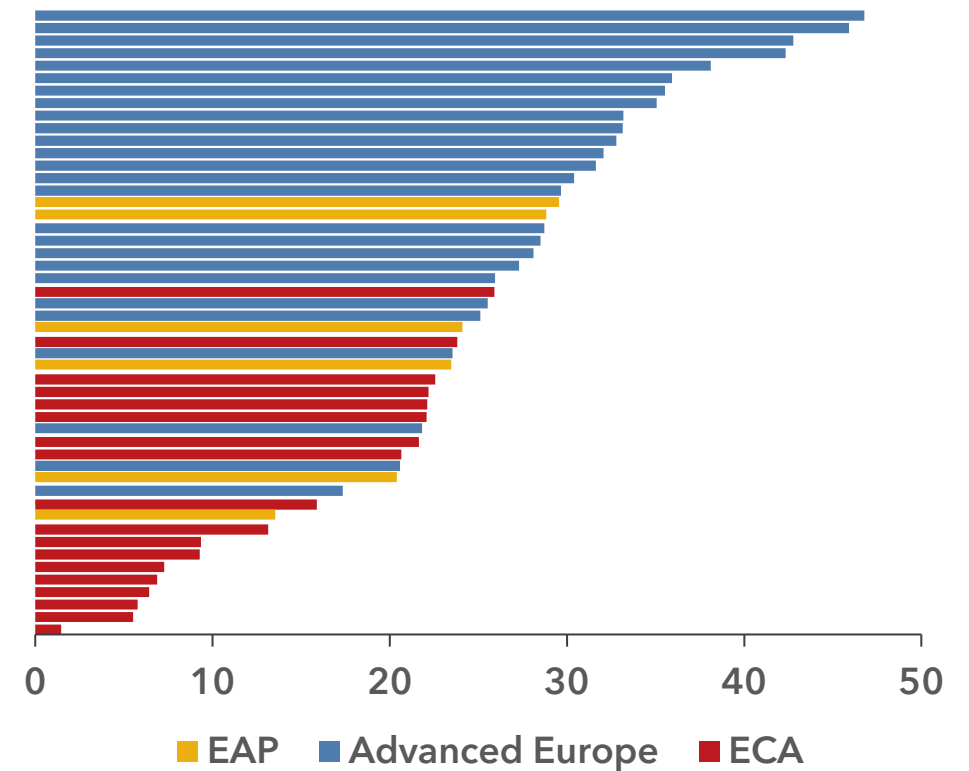
# III. Education and the skills gap

## Low quality of education contributes to sluggish innovation in ECA

Quality of basic education (Pisa scale math average)



Quality of higher education

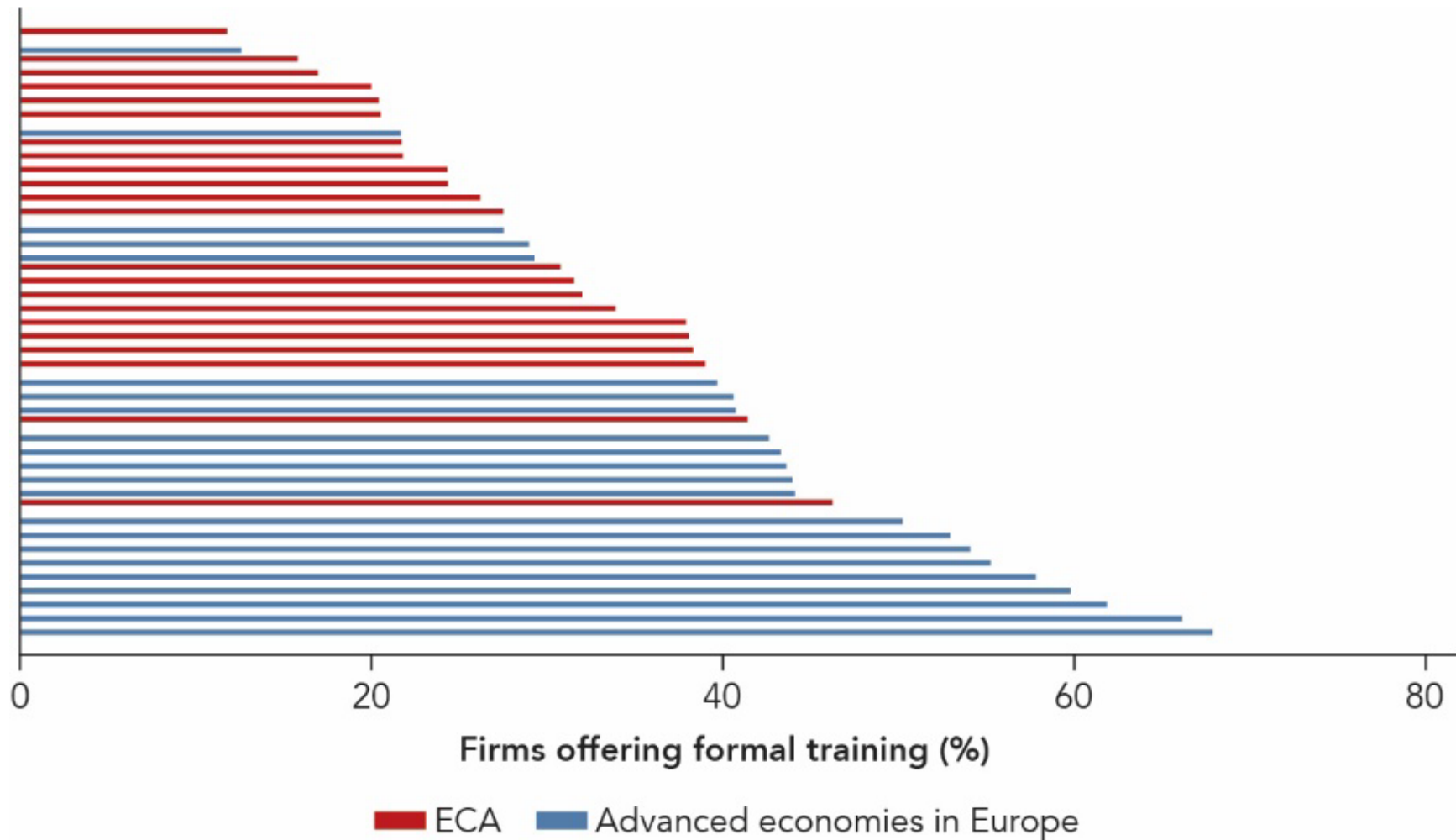


Source: OECD; World Bank.

Note: Calculations based on the Organisation for Economic Co-operation and Development's Program for International Student Assessment (2022). Demircuc-Kunt and Torre (2022).

# III. Education and the skills gap

## Fewer firms with worker training in ECA

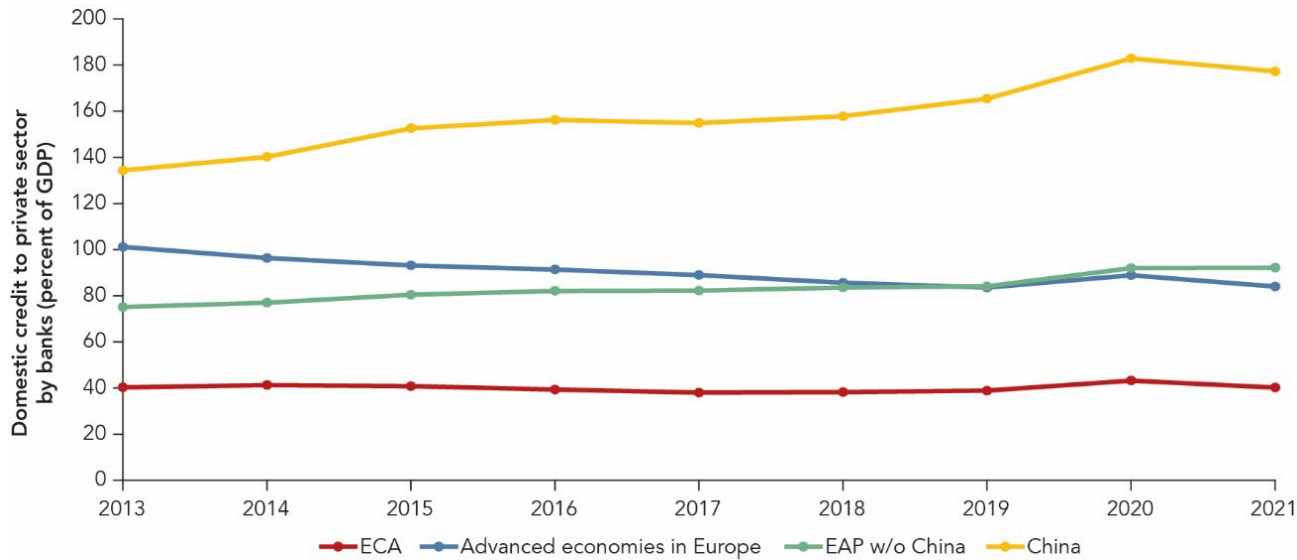


Source: World Bank Enterprise Surveys (for most countries, 2019).

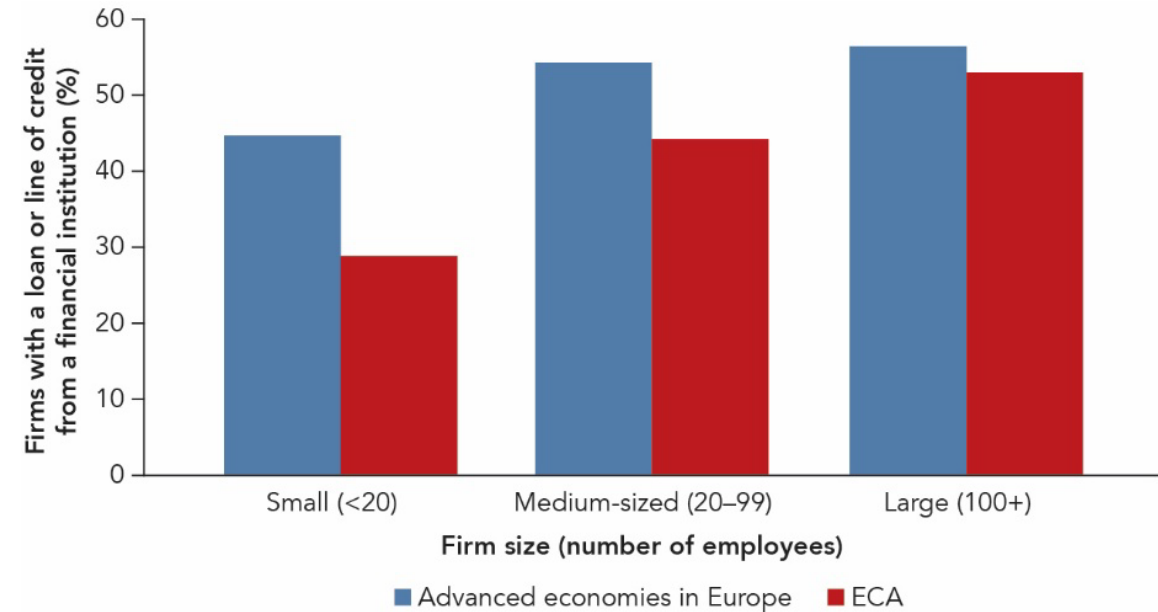


# IV. Access to finance

## Domestic credit to the private sector is relatively low in ECA



## Smaller firms have more difficult access to finance



Source: International Monetary Fund; OECD; World Bank.

Note: Calculations based on data from the World Development Indicators. The original sources are the International Monetary Fund, International Financial Statistics and data files, and World Bank and Organisation for Economic Co-operation and Development GDP estimates. World Bank Enterprise Surveys (for most countries, 2019).

# Conclusions: Unleashing the Power of the Private Sector

**ECA has plenty of room to make up on business dynamism and innovation**

- Firms are generally less productive. They grow less. Firm creation and exit are lower.
- The pace of innovation has not moved much.

**To boost business dynamism in ECA, focus on:**

- Upgrading the competition environment
- Reducing state involvement in the economy
- Boosting dramatically the quality of education
- Strengthening the availability of finance

**Deeper integration into the EU and global markets is needed:**

- Especially given the small size of most economies and enterprises

**Adverse demographics** are also a profound challenge





# Thank you



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