BOSNIA AND HERZEGOVINA | CROATIA | MACEDONIA | MONTENEGRO | SERBIA | SLOVENIA

SEE-6
Economic Outlook

SEEA is an international organization with the aim to: promote economic research in Southeastern Europe; foster networking and regional cooperation among the member institutes; develop joint research programs; organize joint scientific conferences, round tables and meetings on a national level.

CONTENT

2 BOSNIA AND HERZEGOVINA — Strong economic growth despite stagnation in the EU accession process

8 CROATIA — Positive economic trends continued in 2017 and expected to prevail in 2018

14 MACEDONIA — On the road to economic recovery

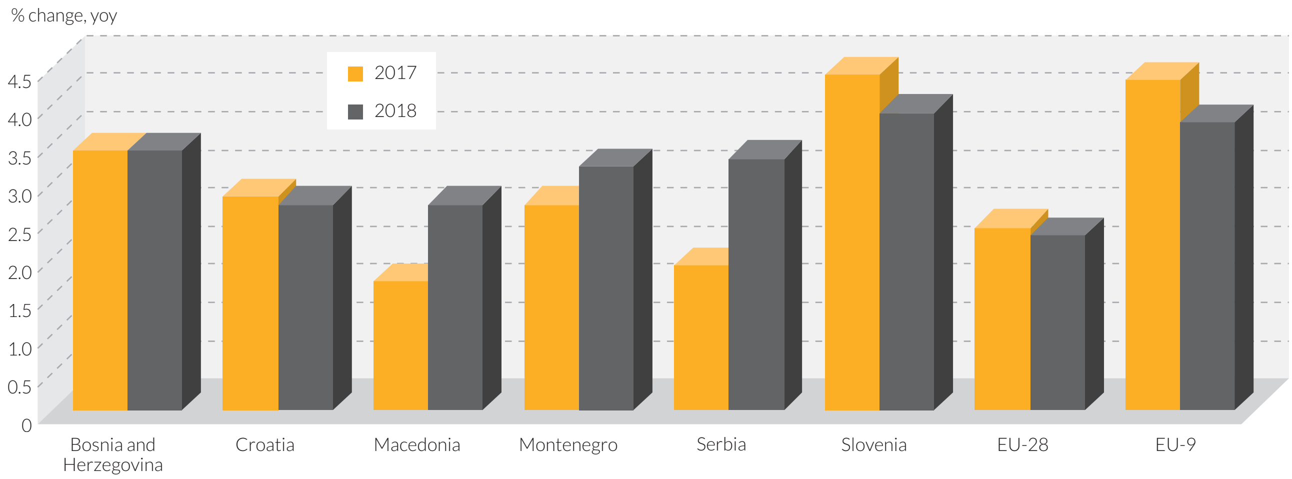
20 MONTENEGRO — Became the 29th Member State of the NATO

26 SERBIA — Competitive position improved as a result of a more favorable macroeconomic and business environment

32 SLOVENIA — Continuing the economic growth, waiting for sustainability

38 ANALYSIS — The national competitiveness and labor market efficiency in SEE-6 countries

REAL GDP GROWTH PROJECTIONS FOR SEE-6, EU-9* AND EU-28



Source: European Economic Forecast, European Commission, Winter 2018 and authors for SEE-6.
Note: * EU-9 include Bulgaria, Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Romania and Slovakia.

seea | Vol. **4** | No. **1** | **March** 2018 | e-ISSN **1849-8884** | ISSN **1849-8817**

BOSNIA AND HERZEGOVINA

Strong economic growth despite stagnation in the EU accession process

Recent economic developments

Slowing down of the EU accession process

At the end of 2016, BiH received a European Commission Questionnaire, and thus the process of preparing an opinion on Bosnia and Herzegovina's EU membership application (which was submitted to the Council of the European Union in February 2016) was officially started. However, in the first half of 2017, representatives of the authorities in BiH did not answer questions from the Questionnaire. In this way, the deadline set by the European Commission to answer questions from the Questionnaire was exceeded. Fulfilling the Questionnaire is a basic condition for applying for candidate status in the European Union, so delay in answering questions from the questionnaire means slowing down of the EU accession process.

BiH could also face the slowdown in socio-economic reforms, as the parliament did not adopt the amendments to the law on excise tax and the new law on deposit insurance in the first half of 2017. Both are key requirements of the authorities' program, supported by the IMF under the Extended Fund Facility (EFF) signed on September 7, 2016, when the IMF's Executive Board approved

a three-year extended arrangement under the EFF with BiH for an amount of about €563.3 million to support the country's economic reform agenda.

Strong economic growth driven by final consumption and exports

The end of 2016 and the beginning of 2017 were marked by strong economic growth in BiH. The growth rate in 2016 was 3.1%, which represents a significant improvement compared to the average for 2011-2015 when growth rate was only 1.5%. A similar trend of growth, with a rate of 3.0%, is continued in the first half of 2017. The main drivers of this growth were domestic consumption and exports, while at the same time the investments had a negative trend. In the first six months of 2017, total domestic consumption grew by 1.7%, while exports increased by as much as 9.4%. At the same time, investments fell by 9.4%. Positive economic trends in the surrounding countries are the main causes of a high growth in exports and hence of economic growth.

Employment growth and a slight decline in unemployment

Downward trend of unemployment rates in 2016 and early 2017 is characteristic for all EU and SEE countries. Decline of the unemployment rate was recorded in BiH in 2016, by 2.3 percentage points compared to 2015. Unfortunately, the Agency for Statistics of Bosnia and Herzegovina does not provide quarterly unemployment reports. Therefore, there are no official data on unemployment trends in 2017. However, according to data for 2016, BiH had the highest unemployment rate in the region. At the same time, in the first quarter of 2017, employment increased by 2.5%. This growth is largely due to growth of employment in three sectors: manufacturing (4.5%), provision of food and catering (5.2%), and arts, entertainment and recreation (7.4%).

Budget surplus and unchanged government public debt

In the first two quarters of 2017, a budget surplus was achieved implying a continued trend of balanced public finances from 2016. In the first 6 months of 2017, revenues grew at a rate of 6.7%, while expenditures increased by just 0.8% compared to the same period in 2016. Revenue growth is largely the result of an increase in revenues from direct and indirect taxes. Indirect taxes increased by 3.2% compared to the same period in 2016, within which the highest growth rates were in customs duties (12.2%) and excises (8.6%), while direct taxes increased by as much as 9.4%. In the same period, public government debt remained virtually unchanged and amounted to about 6 billion euros (0.9% yoy). The increase in indebtedness was influenced by an increase in external debt by 1.8%, while the internal debt was reduced by 0.9%.

Low inflation and a significant increase in credit activity

After several years of deflation, in the first six months of 2017, the general price level in BiH increased slightly by 1.2%. Mild inflation is the result of an increase in energy prices on the world market, primarily prices of oil and natural gas. As a consequence, there was a rise in prices in the transport sector (7.5%). In addition, an increase in the prices of alcoholic beverages and tobacco was also a significant contribution to the general price increase (4.2%). As a result of positive economic trends, the first half of 2017 marked a significant increase in lending activity. Total loans increased by 4.8% compared to the same period in 2016. Corporate loans grew at a slightly higher rate (6% yoy) than loans for households (5.3% yoy). At the same time, loans to the government had a negative growth rate (-0.6% yoy).

High growth of foreign trade and increase in foreign direct investment

The dynamics of foreign trade growth continued in the first half of 2017. A favorable external environment and increase in domestic demand are the main factors contributing to the rise in foreign trade. Thus, in the first half of 2017 exports increased by 15.3% and imports by 11.2% compared to the same period in 2016. The increase in exports was contributed by the growth of the manufacturing industry, which is mainly export oriented. However, due to the base effect, there was no significant change in the foreign trade deficit compared to the same period in 2016. At the same time, the current account deficit also did not change significantly in the first six months of 2017. Foreign direct investment in the first half of 2017 amounted to about 187 million euros, which represents a significant increase (68.5%) compared to the first half of 2016, when these investments amounted to about 111 million euros.

Table BH1 Main economic indicators

	2015	2016	2017		
		Q4	Q1	Q2	Q3
ECONOMIC ACTIVITY					
Real GDP (% change, yoy)	2.8	3.5	3.2	2.9	2.9
Real private consumption (% change, yoy)	1.9	2.8	1.5	1.5	2.0
Real government consumption (% change, yoy)	1.0	1.4	1.9	1.8	1.3
Industrial output (% change, yoy)	2.6	5.7	2.3	2.1	5.8
Unemployment rate (registered, %, pa)	27.7	25.4	-	-	-
Nominal GDP (EUR million)	14,361	3,782	3,527	4,047	4,465
GDP per capita (EUR)	3,752	990	923	1,057	1,168
PRICES, WAGES, AND EXCHANGE RATES					
Implicit GDP deflator (% change, yoy)	1.1	2.4	1.3	3.1	2.6
Consumer prices (% change, yoy, pa)	-1.0	-0.4	1.1	1.2	1.1
Producer prices (% change, yoy, pa)	0.6	-0.8	2.8	2.4	2.4
Average gross wage (% change, yoy, pa)	1.0	1.7	1.5	1.9	1.5
Exchange rate, BAM/EUR (pa)	1.96	1.96	1.96	1.96	1.96
Exchange rate, BAM/USD (pa)	1.76	1.81	1.83	1.78	1.66
FOREIGN TRADE AND CAPITAL FLOWS					
Exports of goods (EUR million)	5,070	1,411	1,316	1,548	1,744
Exports of goods (EUR, % change, yoy)	3.2	13.2	16.9	13.8	17.1
Imports of goods (EUR million)	7.823	2.128	1.933	2.267	2.383
Imports of goods (EUR, % change, yoy)	-2.3	7.9	12.3	10.2	13.0
Current account balance (EUR million)	-828	-210	-165	-242	-129
Current account balance (% of GDP)	-5.7	-5.5	-4.6	-5.9	-2.9
Gross foreign direct investment (EUR million)	221	69	145	42	83
Foreign exchange reserves (EUR million, eop)	4,413	4,887	4,739	4,854	5,230
Foreign debt (EUR million, eop)	8,238	7,911	-	-	-
GOVERNMENT FINANCE*					
Revenue (national currency)**	10,744	11,084	2,646	5,567	8,729
Expense (national currency)**	10,364	10,382	2,376	4,921	7,544
Net = Gross operating balance (BAM million)**	380	702	270	646	1,185
Net acquisition of non-financial assets (BAM million)**	239	364	30	100	131
Net lending/borrowing (national currency)**	-399	354	240	546	1,053
Domestic government debt (EUR million, eop)	1,664	958	992	960	838
Foreign government debt (EUR million, eop)	4,438	5,257	5,214	5,100	5,084
Total government debt (% of GDP)	30.9	34.9	-	-	-
MONETARY INDICATORS					
Narrow money, M1 (% change, yoy, eop)	11.2	13.6	13.9	14.8	13.9
Broad money, M2 (% change, yoy, eop)	8.0	8.3	9.3	10.2	9.8
Total domestic credit (% change, yoy, eop)	2.4	1.9	3.8	5.8	6.4
DMBs credit to households (% change, yoy, eop)	4.8	3.7	4.6	6.0	6.7
DMBs credit to enterprises (% change, yoy, eop)	-0.2	3.8	5.2	6.8	7.8
DMBs credit rate for enterprises, short-term, (%, pa)	6.3	6.0	5.6	5.4	5.3
DMBs credit rate for households, short-term (%, pa)	7.4	8.1	7.0	7.4	5.9

Notes: * Data refer to consolidated general government. ** On the cash principle, cumulative from the beginning of the year.

Conventional abbreviations: pa – period average; eop – end of period; yoy – year on year; EUR – euro, USD – U.S. dollar; BAM – Bosnia-Herzegovina convertible mark; DMB – deposit money bank.

Sources: Agency for Statistics of Bosnia and Herzegovina, Bosnia and Herzegovina Directorate for Economic Planning, Bosnia and Herzegovina Indirect Taxation Authority, Central Bank of Bosnia and Herzegovina.

Table BH2 Summary of projections

	2017	2018	2019
Real GDP (% change)	**3.4**	**3.4**	**3.8**
Real private consumption (% change)	1.6	2.1	2.0
Real investment (% change)	5.8	6.9	10.3
Exports of goods and services (constant prices, % change)	9.1	7.1	4.3
Imports of goods and services (constant prices, % change)	4.7	4.8	4.3
Current account balance (% of GDP)	4.6	4.3	4.3
Consumer prices (% change, pa)	1.1	1.2	1.4
Exchange rate, national currency/EUR (pa)	1.9	1.9	1.9
Unemployment rate (registered, %, pa)	20.5	-	-
General government balance (ESA95 definition, % of GDP)	-	-	-
Broad money, M4 (% change, eop)	-	-	-
Total domestic credit (% change, eop)	6.0	6.0	6.8

Note: Cut-off date for information used in the compilation of projections was December 20, 2017.
Conventional abbreviations: pa – period average, eop – end of period, EUR – euro.
Sources: BiH Directorate for Economic Planning, World Bank, IMF and author's projections.

Policy assumptions and projections summary

Strengthening economic growth in 2018 and 2019, mainly due to higher exports and private sector investments

The external environment over the previous years was the main structural determinant of economic trends in BiH. In line with this, the assumptions for 2018 are based on projections of favorable economic opportunities in the region, and the intensification of reform activities in the country that will allow the continued implementation of the arrangement with the IMF. In the second half of 2017, a high level of business activity is expected to continue in BiH, which according to projections at the end of the year should result in real GDP growth of 3.4%. The key generators of this economic growth should be real exports growth of 9.1% and growth in domestic demand of 2.3%. Expected export growth with a better business environment and generally higher optimism related to the implementation of the arrangement with the IMF could lead to a slight growth in private investment at a real rate of 6.9% in 2018. The above mentioned accompanied by the strong growth of public investments should lead to a real growth of investments in fixed assets of 10.6%. Hence, investments together with final consumption would be the main bearers of the projected economic growth of 3.4% in 2018 and 3.8% in 2019.

Positive developments in EU countries that are the main BiH trading partner with additional contribution from countries in the region, where economic growth is also expected to continue, should result in a continuing trend of growth in foreign trade in BiH. In the period from 2018 to 2019, annual real growth rates of total exports of 7.1% and 5.5%, respectively, can be expected. On the other hand, the growth in domestic demand accompanied by an increase in number of employees and their earnings, and a higher level of total investment in infrastructure and energy would lead to an increase in imports. However, import rates are expected to be slightly lower than export rates, so that the real growth rate of total imports would range from 4.8% in 2018 to 4.3% in 2019. In 2018 and 2019, BiH is expected to have approximately the same level of inflation as in 2017 (1.2% and 1.4%, respectively). The main reason for this low inflation is the stabilization of oil and food prices on the world market.

CROATIA

Positive economic trends continued in 2017 and are expected to prevail in 2018

Recent economic developments

Solid economic activity in spite of political instability and Agrokor's corporate crisis

In 2017, economic developments in Croatia were dominated by two phenomena: solid economic activity underpinned by the favorable global economic environment and the crisis in Agrokor, the biggest Croatian private company. Political situation was more stable than in 2016, but still not without glitches. The HDZ-MOST Government that came into power in October 2016 underwent a reconstruction in April 2017 when the central-right HDZ replaced its thus-far coalition partner MOST with a central-left HNS (Croatian People's Party). This reshuffling was provoked by MOST's decision to support a no-confidence vote against HDZ's Minister of Finance, Zdravko Marić. Prime Minister Plenković dismissed the three ministers that were members of MOST, changed the positions of some previous ministers, and got the Parliament's support to appoint two ministers and a Deputy Prime Minister from the HNS's quota. Leader of MOST, Božo Petrov resigned as the Speaker of the Parliament, and MOST became an opposition party. Plenković retained a slim and fragmented majority in the Parliament with 78 out of 151 seats. The Government crisis coincided with the crisis in Agrokor.

MOST accused Minister Marić for being partly responsible for (or at least well informed about) Agrokor's crisis, since he was holding a top management position in Agrokor prior to becoming the Minister of Finance.

In early spring 2017, Agrokor, a corporation whose annual revenues equal 15 percent of Croatia's GDP, became insolvent. In order to prevent immediate activation of the bankruptcy procedure provoking thereby huge supplier's losses, the Government prepared and passed the new law on "systematically important companies". The main intention of the Law was to give the troubled company some time to restructure before starting a regular bankruptcy procedure. Agrokor has activated the Law in April, and since then it has been managed by the extraordinary administration whose main obligation is to restructure the company and negotiate the partial write-off of obligations toward its suppliers. The Government claims that there will be no bail-out of Agrokor at taxpayers' expenses, but negative effects of the Agrokor crisis on the economy are inevitable.

Strong growth of private consumption and investment; yet another successful tourist season

The year 2017 will be the third consecutive year with growth rates close to 3 percent. In the last quarter of 2016, growth has accelerated, and in the first three quarters of 2017 there was a continuation of such strong growth, with y-o-y growth rates ranging from 2.6 percent in the first quarter to 3.3 percent in the third quarter. Growth was driven by the rising private consumption whose y-o-y growth rates were 3.5 percent in the first quarter, and 3.7 percent in second and third quarters. Retail trade has recorded even higher rates of growth, from 3.3 percent in the first quarter, to 5.2 and 5.5 percent in the second and third quarters. Investments grew as well, albeit less vigorously than private consumption. The overall contribution of net exports to growth in the first three quarters was positive thanks to exceptionally high exports of services in the third quarter. This can be attributed to yet another successful tourist season. Until the end of November 2017, the number of tourist arrivals was 12.8 percent higher than in same period last year, and the number of overnight stays went up by 8 percent.

Data on the industrial output indicate that growth is more reliant on the production of services than on the production of goods. In first eleven months of 2017 the industrial production was 2.3 percent higher than in the same period last year, and the output in manufacturing was 3.1 percent higher. Although there is still room for growth in tourism, especially in the continental part of the country, there are more and more voices warning that Croatia should not base its economic activity solely on tourism.

Rise in employment and strong decrease in unemployment

According to the Pension Insurance Institute, at the end of November 2017 the number of employed individuals was 29 thousand higher than in the same period last year. The number of job-seekers declined, however, much more in the same period. In November 2017, there were 48.6 thousand less jobless individuals than in the same month last year. As a consequence, the average unemployment rate in the first eleven months of 2017 stood at 12.5 percent, down from 15.0 percent in the same period last year. The Online Vacancy Index (OVI), a monthly index of online job advertisements developed by the Institute of Economics, Zagreb, indicates a strong recovery of labor demand in 2017, with a rise in the number of job advertisements by 33.0 percent when compared with 2016. The demand for workers with a university degree rose only by 4.0 percent, while there is a buoyant demand for lower qualified workers, such as sales assistants, cooks, waiters, and drivers. A part of this demand remains unsatisfied, implying that the labor supply does not match the requirements of the market.

The Government remains committed to fiscal consolidation

In 2016 Croatia had a sizeable fiscal consolidation. The deficit of the consolidated central Government that stood at 3.3 percent of GDP in 2015 went down to only 0.9 percent. Public debt ratio decreased to 82.9 percent at the end of 2016, i.e. 2.5 percentage points less than at the end of 2015. As a consequence, the Council of the European Union closed the Excessive Deficit Procedure for Croatia in June 2017. The fiscal outturn for the first three quarters of 2017 confirms the commitment to fiscal consolidation, which is in line with the "Strategy for the Adoption of the Euro in Croatia" presented in October 2017, in which the Government and the Croatian National Bank expressed their readiness to meet all the convergence criteria necessary to adopt the euro.

In the first three quarters of 2017, consolidated general Government ran a surplus of more than 4.1 billion kuna, up from 1.3 billion kuna in the same period last year. In spite of the lower tax burden, total revenues went up by 2 billion kuna in the first three quarters, compared by the first three quarters of 2016. There was some increase in expenditures as well, but it totaled only 0.4 billion kuna in the January–September period. In general, the tax reform implemented at the beginning of 2017 proved to be a step in the right direction, contributing to the rise in employment, increasing consumer optimism, and improving the business climate. However, the Government failed to complete the tax reform according to the plan. Part of the tax reform package was the introduction of property tax, which was supposed to replace the three existing recurrent taxes on immovable property levies—communal charge, tax on holiday houses, and monument annuity. Property tax should have been implemented at the beginning of 2018, but after a loud public disapproval the Government decided to postpone it indefinitely. The Government thus lost the opportunity to create the instrument which would allow it to shift the tax burden from income to capital in the future.

In September 2018, the Parliament adopted the Budget for 2018. It is based on the expectation of a 2.9 percent growth in real GDP, and foresees an increase in revenues by 6.1 percent and an increase in expenditures by 3.9 percent. On the level of consolidated general Government, 2018 is expected to end with a deficit of 0.8 percent of GDP. The Government foresaw the continuation of a rather tight fiscal policy in 2019 and 2020, which would push the Government balance in surplus, and the public debt ratio below 70 percent by 2020. Such ambition seems realistic, considering that a Budget outturn resulted in balance close to surplus already by the end of 2017.

Decreasing trend in price movements reversed in 2017

After three consecutive years of decreasing consumer prices, the price movements reversed in 2017. Overall, in 2017, the consumer prices grew on average by 1.1 percent in comparison with the previous year. Rise in prices was mainly fueled by the prices of food, which rose by 2.9 percent on average, while the contribution of housing, water, electricity, gas, and other fuels was negative (2.7 percentage points).

Policy assumptions and projections summary

Growth expected to decelerate, but still close to 3 percent in 2018 and 2019

Macroeconomic forecasts for Croatia are prepared by the Institute of Economics, Zagreb and were previously published in the publication *Croatian Economic Outlook* in March 2018. The Institute maintains optimistic projections with growth rates of 2.7 in 2018 and 2.6 percent in 2019. However, the Institute has recently revised the projections for 2018 downwards, since the high-frequency data for the last quarter of 2017 indicated that the growth is losing momentum. The underperformance of the economy at the end of 2017 resulted from a modest investment activity, a decrease in industrial production, and a restrained increase in exports. Gradual deceleration is projected for 2019 as well.

Private consumption was one of the main drivers of GDP growth in 2017, which can be attributed to a rise in disposable income after changes in personal income tax, strong consumer optimism, and an increase in pensions and wages of the public sector employees. Solid growth in private consumption is foreseen for 2018 as well, underpinned by the rise in legally defined minimum wage. Although the Government announced that 2018 will be the year that will finally bring the necessary structural reforms, we remain quite skeptical about it.

Investment activity was weak in 2017, which was not only a consequence of disrupted business activities in companies related to Agrokor, but also a result of an overall hesitancy to invest in an unfavorable investment climate. EU-funded infrastructural investment that might compensate for the slump

Table HR1 Main economic indicators

	2015	2016	2017		
		Q4	Q1	Q2	Q3
ECONOMIC ACTIVITY					
Real GDP (% change, yoy)	2.3	3.5	2.6	3.0	3.3
Real private consumption (% change, yoy)	1.1	3.7	3.5	3.7	3.7
Real government consumption (% change, yoy)	-0.9	2.2	1.5	1.7	2.3
Real investment (% change, yoy)	3.8	5.0	5.4	3.3	3.4
Industrial output (% change, yoy)	2.7	7.1	2.3	1.2	2.9
Unemployment rate (registered, %, pa)	17.4	14.3	15.0	11.9	10.8
Nominal GDP (EUR million)	44,546	11,634	10,676	12,231	13,755
GDP per capita (EUR)	10,596	-	-	-	-
PRICES, WAGES, AND EXCHANGE RATES					
Implicit GDP deflator (% change, yoy)	0.0	0.0	0.0	1.1	1.9
Consumer prices (% change, yoy, pa)	-0,5	-0.2	1.1	1.1	1.0
Producer prices (% change, yoy, pa)	-3.8	-1.8	2.1	1.8	1.9
Average gross wage (% change, yoy, pa)*	1.3	1.7	2.9	3.8	4.4
Exchange rate, HRK/EUR (pa)	7.61	7.52	7.47	7.43	7.42
Exchange rate, HRK/USD (pa)	6.86	6.96	7.02	6.76	6.32
FOREIGN TRADE AND CAPITAL FLOWS					
Exports of goods (EUR million)	11,528	3,425	3,274	3,460	3,415
Exports of goods (EUR, % change, yoy)	11.2	14.1	25.4	8.8	12.9
Imports of goods (EUR million)	18,483	5,151	5,226	5,651	5,595
Imports of goods (EUR, % change, yoy)	7.9	11.5	17.0	10.4	12.4
Current account balance (EUR million)	2,019	-682	-1,529	154	3,868
Current account balance (% of GDP)	4.5	-5.9	-14.3	1.3	28.1
Gross foreign direct investment (EUR million)	189	321	470	206	610
Foreign exchange reserves (EUR million, eop)	13,707	13,514	16,072	14,028	14,954
Foreign debt (EUR million, eop)	45,384	41,668	43,865	40,240	39,382
GOVERNMENT FINANCE**					
Revenue (HRK million)***	150,089	40,083	35,755	42,266	42,577
Expense (HRK million)***	150,559	40,893	36,862	38,387	36,947
Net = Gross operating balance (HRK million)***	-470	-810	-1,107	3,880	5,630
Net acquisition of non-financial assets (HRK million)***	7,849	3,268	1,091	1,618	1,572
Net lending/borrowing (HRK million)***	-8,320	-4,077	-2,198	2,262	4,058
Domestic government debt (EUR million, eop)	23,281	2,894	25,054	24,443	24,869
Foreign government debt (EUR million, eop)	16,037	14,354	15,297	13,873	14,026
Total government debt (eop, % of GDP)	85.4	-	-	-	-
MONETARY INDICATORS					
Narrow money, M1 (% change, yoy, eop)	11.4	18.1	21.1	18.1	20.1
Broad money, M4 (% change, yoy, eop)	5.2	4.7	3.8	2.9	3.3
Total domestic credit (% change, yoy, eop)	-2.0	-6.0	-3.4	-3.2	-1.9
DMBs credit to households (% change, yoy, eop)	-1.5	-5.5	-0.9	-0.8	0.4
DMBs credit to enterprises (% change, yoy, eop)	-5.2	-2.5	-4.1	-2.0	0.3
Money market interest rate (%, pa)	0.8	0.6	0.4	0.5	0.4
DMBs credit rate for enterprises, short-term, (%, pa)****	8.9	7.9	7.8	7.7	7.4
DMBs credit rate for households, short-term (%, pa)****	5.4	4.5	4.6	4.5	4.4

Notes: * Break in time series; data for 2016 and 2017 are gathered by processing data submitted in the reports on income, income taxes, and social security contributions; ** data refer to consolidated general Government; *** on the cash principle; **** the weighted average interest rate on new loan agreements, revised data.

Conventional abbreviations: pa – period average, eop – end of period, yoy – year on year, HRK – Croatian kuna, EUR – euro, USD – U.S. dollar, DMB – deposit money bank.

Sources: Croatian Bureau of Statistics, Croatian National Bank, and Ministry of Finance.

Table HR2 Summary of projections

	2017	2018	2019
Real GDP (% change)	**2.8**	**2.7**	**2.6**
Real private consumption (% change)	3.6	3.1	2.7
Real government consumption (% change)	2.0	2.2	0.9
Real investment (% change)	3.4	3.9	4.3
Exports of goods and services (constant prices, % change)	-	5.6	5.3
Imports of goods and services (constant prices, % change)	-	7.4	7.5
Current account balance (% of GDP)	-	1.4	0.6
Consumer prices (% change, pa)	1.2	1.6	1.8
Exchange rate, national currency/EUR (pa)	7.46	7.42	7.40
Unemployment rate (registered, %, pa)	12.4	10.5	9.7
General government balance (ESA 2010 definition, % of GDP)	-	0.2	0.5
Total domestic credit (% change, eop)	-4.7	-0.3	0.9

Note: Cut-off date for information used in the compilation of projections for 2018 and 2019 was March 5, 2018.
Conventional abbreviations: o – outturn, p – projection, pa – period average, eop – end of period, EUR – euro.
Source: The Institute of Economics, Zagreb.

in private investment activity materialized to a less-than-expected extent, revealing different structural weaknesses and a lack of capacity in the public sector. Still, since the Government recently cut some of the red tape and parafiscal burden, the Institute expects that the investment growth will resume at rates of 3.9 percent in 2018, and 4.3 percent in 2019.

Next two years are expected to be the years of lively international activity. Exports are supposed to grow by 5.6 and 5.3 percent, respectively, thanks to good tourist seasons and a favorable economic situation with our main trading partners. Due to the rise in private consumption, the imports might grow at even higher rates, i.e., 7.4 percent in 2018 and 7.5 percent in 2019. Current account balance is expected to decrease in comparison with previous years, and reach 1.4 percent in 2018 and 0.6 percent in 2019.

The Institute assumes that the Government will stick to its plan to balance the Budget in 2017 and enter the surplus in 2018. Although it forecasts the general Government deficit to amount up to 0.4 percent of GDP, the actual outturn might even be better. A surplus is projected for both 2018 and 2019, reaching 0.2 and 0.5 percent, respectively.

As for the labor market, a further decline in the number of unemployed and a moderate rise in the number of the employed are expected. The registered unemployment rate is projected to go down to 10.5 percent in 2018 and 9.7 percent in 2018. Although the credit activity will remain weak in 2018, credit growth might eventually resume in 2019, with a growth rate of 0.3 percent. As for the exchange rate, it is expected to remain stable in years to come, just as the prices. A slight acceleration of price dynamics is foreseen, owing to increase in energy prices, strong domestic demand, and higher wages. The consumer price inflation could thus reach 1.6 percent in 2018 and 1.8 percent in 2019. ■

MACEDONIA

On the road to economic recovery

Recent economic developments

The political crisis is stagnating, but the political climate is not improving

Changing the catalysts for economic growth

Since mid–2017 Macedonia has a new Government, which was formed long six months after the parliamentary elections. Although a political turmoil has thus been calmed, political scene is still far from being stable.

Rise in GDP that was mostly fueled by Government borrowing and driven by construction in both public and private sectors, stopped in the last quarter of 2017. The process of the parliamentary elections that was held in December 2016 froze the government expenditures. As the result of the long process of establishing the new Government, public expenditures even in the second quarter of the 2017 decreased by around 20%. Government investments as a main driver of economic growth trend were stopped.

The fall of the real investment was ended in the second quarter of 2017 and it is expected to continue with positive trend and to be the driving force of the growth. The private consumption is expected to rise at the same period, but not enough to fill in the gap made by the absence of government expenditures.

The NEET rate shows that great part of the younger population (20-34) in the Republic of Macedonia are neither employed nor receive education

and training. Despite its decline (from 50.1% in 2006 to 37.7% in 2016), it is still significantly higher than the one in the EU-28 and in the countries of the region. In 2016, 21.6% of the younger population classified as NEET are unemployed, while 16.1% are inactive.

Unfavorable position of the younger labor force

Despite the manifested positive changes on the labor market in the country, the unemployment and inactivity of the younger population (20-34) in the last decade remains high. The number of the unemployed decreased from over 148 thousand to almost 108 thousand persons. This change was accompanied with an increase of the share of the unemployed with high level of education (from 9.2% in 2006 to 20.3% in 2016). Also, the participation of the long term unemployed, particularly of those unemployed for more than 4 years, remains dominant (52.3% in 2016). As for the inactivity, it decreased for about 4%, but in 2016 there were about 142.7 thousand inactive persons aged 20-34 (out of them almost 70% are women). So, Macedonia is today faced with a relatively great scope of unemployed and inactive young population.

As for the unfavorable position of the young labor force, the problem of unemployment and inactivity of the highly educated population proved to be especially difficult (in 2016 it amounted to about 45 thousand persons). Increased number of the highly educated population in the last decade resulted in a huge increase of those who are outside the economic activity and with intensified intellectual emigration abroad.

Ensuring fiscal sustainability remains a priority

Ensuring fiscal sustainability remains a priority for the Republic of Macedonia. With the formation of the new government, policies should now focus on rebuilding fiscal buffers and implementing critical reforms to rekindle growth and give EU accession prospects a new push. In July the new government adopted a supplementary budget that adjusted revenues and expenditures based on more conservative growth projections but retained the deficit target in nominal terms.

Fiscal expansion in recent years has been accompanied by higher pensions and subsidies. Consolidation should start without delay to create policy space through more efficient collection of VAT, rationalization of subsidies, pension reforms and higher fuel taxation. These measures will ensure fiscal sustainability and help meet large investment needs in infrastructure and human capital.

Efficient monetary policy and banking sector mainly focused on household sector

For 2017, the slightly higher deficit relative to 2016 is driven by lower-than-budgeted revenue collection (about 87% of total years planed revenues are realized for 11 months) reflecting growth slowdown although overall expenditure is also projected to be below the budgeted amount (for the same period, 85.5% of years planned expenditures are realized). The under-execution of goods and services and capital spending (74.1% and 58.4% respectively, of years planned expenditures are realized for 11 months), which is expected to keep overall fiscal deficit below 3% of GDP in 2017. Public debt is projected to rise to 47% of GDP in 2017.

Decreased rate on CB bills to 3.25% in February 2017, provided strong signals for lessening the monetary policy, which during the previous period had triple adjustment such as 4% in May 2016, 3.75% in December 2016 and 3.50% in January 2017. After extensive utilization of the official foreign reserves in mid-2016 due to the political crises, their level was stabilized at the optimal balance during the year of 2017 reaching 2,534.4 and 2,399.9 million Euros in first and second quarter of 2017.

Banking sector was stable with capital adequacy of 15.4% and 15.8% for the first two quarters of 2017. Earnings were quite solid measured by ROA of 1.5% and 1.4% and ROE of 13.8% and 12.7%. NPLs to gross loans demonstrated further decrease such as 6.1 and 6.5% respectively, validating increased bank assets quality and enhanced risk assessment and management in the banks. Credit growth registered minor increase in terms of credit to enterprises, whilst credits to households indicated increase of 6.5% and 9.2%, respectively. Data demonstrate that bank deposits continue to grow clearly signifying the increased level of trust and decreased pressure of the political crises.

Increases in prices

The trend of decreasing consumer and production price was held to a stop in the second half of 2016. In the last quarter of 2016 and the first two quarters of 2017, we can see the rise in consumer and production prices for 0.5 and 1.2% percentage points respectively. The rise in the consumer price of transportation is the most relevant for the overall rise of prices. In the specified period, the rise of the consumer prices was mainly triggered by the rise of electricity and fuel prices for the industry and households. The expansion of the political crisis also had an effect on increasing the consumer prices due to the high level of uncertainty of the effects and the final epilogue to the crisis.

Stable state in foreign trade and capital flows

In the analyzed period, the deficit on the balance of payments' current account registered the lowest level in 2014, and in the upcoming period it is kept at a moderate level without indicating major imbalances in the external sector. The biggest contribution to this is the improvement of the exchange of goods as a result of the growing export of new industrial capacities, i.e. the more intensive growth of exports than imports. An exception to this is the first quarter of 2017, when despite the intensified export activity, the high import growth, driven primarily by the raw material imports (of some of the foreign capacities) and energy imports, led to the expansion of the negative foreign trade balance.

The financial account recorded inflows that are largely the result of government borrowing and inflows of FDI that were solid and stable. With the exception of 2014, in the rest of the period, given the changes in the current and financial account, part of the needs for external funding were covered by foreign exchange reserves, which declined on an annual basis, but remain adequate. Gross external debt has seen a continuous increase, which is due either to public debt or private sector debt, depending on the analyzed period.

Table MK1 Main economic indicators

	2015	2016	2017		
		Q4	Q1	Q2	Q3
ECONOMIC ACTIVITY					
Real GDP (% change, yoy)	3.9	2.4	0	-1.8	0.2
Real private consumption (% change, yoy)	3.7	5.1	2.7	4.1	2.9
Real government consumption (% change, yoy)	2.1	3.4	0.7	2.0	-3.6
Real investment (% change, yoy)	3.6	-10.4	0.6	-19.9	-9.4
Industrial output (% change, yoy)	4.9	-1.7	-1.6	3.8	-2.4
Unemployment rate (registered, %, pa)	26.1	23.1	22.9	22.6	22.1
Nominal GDP (EUR million)	9,061	2,607	2,373	2,488	2,594
GDP per capita (EUR)	4,392	-	-	-	-
PRICES, WAGES, AND EXCHANGE RATES					
Implicit GDP deflator (% change, yoy)	1.9	-	-	-	-
Consumer prices (% change, yoy, pa)	-0.3	-0.1	0.5	1.2	1.6
Producer prices (% change, yoy, pa)	-4.1	-0.5	0.1	0	0.5
Average gross wage (% change, yoy, pa)	3.0	2.2	1.8	1.0	1.3
Exchange rate, MKD/EUR (pa)	61.61	61.49	61.48	61.69	61.58
Exchange rate, MKD/USD (pa)	55.5	55.1	58.33	57.71	52.48
FOREIGN TRADE AND CAPITAL FLOWS					
Exports of goods (EUR million)	3,046.9	934.4	922.6	1,034.7	1,018.1
Exports of goods (EUR, % change, yoy)	9.4	12.9	19.6	22.4	10.7
Imports of goods (EUR million)	4,869.8	1,416.4	1,385.2	1,453.1	1,430.1
Imports of goods (EUR, % change, yoy)	5.1	3.9	17.8	7.4	7.2
Current account balance (EUR million)	-177.1	-115.5	-140.1	-95.5	174.9
Current account balance (% of GDP)	-2.0	-4.8	-5.9	-3.8	6.8
Gross foreign direct investment (EUR million)	262.3	83.4	219.2	54.1	-1.7
Foreign exchange reserves (EUR million, eop)	2,261.8	2,613.4	2,534.4	2,399.9	2,271.4
Foreign debt (EUR million, eop)	6,290.5	7,216.6	7,791.4	7,781.3	7,710.2
GOVERNMENT FINANCE*					
Revenue (million Denars)**	161,207	43,543	42,735	43,634	44,604
Expense (million Denars)**	180,632	50,507	46,301	48,373	47,349
Net = Gross operating balance (million Denars)**	-19,425	-6,964	-3,566	-4,739	-2,745
Net acquisition of non-financial assets (million Denars)**	-16,402	-5,821	-4,935	-3,390	-2,101
Net lending/borrowing (million Denars)**	-3,023	-1,143	1,369	-1,349	-644
Domestic government debt (EUR million, eop)	,1356.6	1,404.9	1,441.8	1,434.6	1499.1
Foreign government debt (EUR million, eop)	2,096.7	2,446.6	2,446.9	2,450.8	2376.7
Total government debt (% of GDP)	38.1	39.1	37.8	38	37.8
MONETARY INDICATORS					
Narrow money, M1 (% change, yoy, eop)	18.4	9.9	5.5	14.9	13.2
Broad money, M4 (% change, yoy, eop)	6.8	6.1	4.2	7.8	6.4
Total domestic credit (% change, yoy, eop)	9.5	0.9	0	4.4	4.3
DMBs credit to households (% change, yoy, eop)	13.2	6.9	6.5	9.2	10.0
DMBs credit to enterprises (% change, yoy, eop)	7.3	2.1	1.3	1.2	0.5
Money market interest rate (%, pa)	1.0	1.0	1.0	1.0	1.0
DMBs credit rate for enterprises, short-term, (%, pa)	6.8	5.7	5.5	5.4	5.3
DMBs credit rate for households, short-term (%, pa)	4.9	4.3	4.5	4.6	4.6

Notes: * Data refer to consolidated general government, unless stated otherwise. ** On the cash principle, cumulative from the beginning of the year.

Conventional abbreviations: pa – period average, eop – end of period, yoy – year on year, EUR – euro, USD – U.S. dollar, MKD – Macedonian denar, DMB – deposit money bank.

Sources: Ministry of Finance of the Republic of Macedonia, National Bank of the Republic of Macedonia, State Statistical Office of the Republic of Macedonia.

Table MK2 Summary of projections

	2017	2018	2019
Real GDP (% change)	**1.7**	**2.7**	**3.2**
Exports of goods and services (constant prices, % change)	8.8	8.8	8.4
Imports of goods and services (constant prices, % change)	5.5	6.8	7.0
Current account balance (% of GDP)	-2.5	-2.4	-2.3
Consumer prices (% change, pa)	1.2	2.0	2.4
Exchange rate, national currency/EUR (pa)	61.6	61.6	61.6
Unemployment rate (registered, %, pa)	22.2	21.4	21.0
General government balance (ESA 2010 definition, % of GDP)	-2.9	-3.0	-3.0
Broad money, M4* (% change, eop)			
Total domestic credit (% change, eop)	5.6	6.7	

Note: Cut-off date for information used in the compilation of projections was December 20, 2016.

Conventional abbreviations: pa – period average, eop – end of period, EUR – euro.

Sources: Ministry of Finance of the Republic of Macedonia, National Bank of the Republic of Macedonia, and the European Economic Forecast, Autumn 2016, European Commission Directorate - General for Economic and Financial Affairs, Institutional Paper 038, November 2016.

Policy assumptions and projections summary

Positive economic growth in 2018

The stabilization of the GDP growth is expected and the positive economic growth is predicted in 2018 (2.7%) and in 2019 (3.2%). In the coming period, the prices are expected to grow and stabilize. Over the medium-term, the fiscal deficit is projected to stay above 3½ percent of GDP with public debt rising to 53½ percent of GDP by end-2022 and gross fiscal financing needs peaking above 15% of GDP in 2020–21. The medium-term deterioration of the fiscal balance is primarily due to the measures included in the economic program: subsidies for proposed wage increases, the roll-out of additional employment and business incentives, and an increase in public sector wage bill from the pass-through of economy-wide minimum wage increase, as well as clearance of some unpaid claims.

In 2018 the positive trends are expected in terms of sustaining price stability and deposit and credit growths, particularly credits fostering company development and further economic development. However, these expectations can be significantly burdened by persistent threats from external and domestic environment. The NBRM plans future harmonization with the Basel principles, aiming to secure implementation of the Basel III principles in the following three years.

Considering the new economic policies, in the next two years, further reduction of the unemployment rate and inactivity can be expected. All projections confirm the decrease of the unemployment rate, but it will remain above 20%. In spite of the shortage of new jobs, a more significant decline in the unemployment and inactivity of the youth population cannot be expected. With the gradual resolution of the domestic political crisis, the maintenance of a robust external position and an adequate level of foreign exchange reserves is expected in the future. ■

MONTENEGRO

Became the 29th Member State of the NATO

Recent economic developments

The capital inflow was the main driver of the economy

The capital inflow was the main driver of the Montenegrin economy in the past few years. The most important variables that are expected to determine the high inflow of foreign capital are: continuation of works on a large number of started investment projects in tourism, energy sector (construction of small hydropower plants and wind farms) and the public sector (construction of highway), as well as the dynamics of realization of announced new investment projects in 2017.

The construction of highway in Montenegro, as a capital and one-time investment, will affect the growth of economic activity, while on the other hand it will cause public debt growth and increase of pressure in the fiscal sector.

Elected a new government

On 28 November 2016, the Parliament elected a new government headed by PM Duško Marković, vice-president of the Democratic Party of Socialists (DPS), which won a relative majority of 36 out of 81 seats at the parliamentary elections on 16 October 2016.

In 2017, Montenegro remains the frontrunner in the process of European integration, among the Western Balkans countries. Important update is that

Montenegro closed its third chapter in the negotiation process – Chapter 30- External relations, in June 2017. Montenegro now has 30 chapters opened (out of 33 chapters) and 3 chapters temporarily closed. On the path of European integration, focus will remain on strengthening rule of law and further strengthening of democratic capacities of the state and society as a whole.

The biggest achievement of Montenegro in the foreign policy area in 2017 is that it became 29th Member State of the North Atlantic Treaty Organization (NATO). Becoming a NATO member, Montenegro ensured the security of the country, but also created the preconditions for accelerated economic growth and development.

Highest contribution to growth comes from investments and household consumption

According to the data of the Statistical office of Montenegro (Monstat), GDP in current prices in 2016 amounted to 3.954 million euros, with real growth rate of 2.9%, compared to the same period of the previous year. Highest contribution to growth comes from investments and household consumption, whereby high import dependency of investments has reduced their expected effects which has also affected the GDP growth rate.

According to preliminary data from MONSTAT, real GDP growth in the first half of the year amounted to 4.2%,while according to the estimates of the Central Bank of Montenegro (CBM), similar growth is expected (about 4%) for the whole year.

Increased number of employees

The number of employees in 2016 was on average 177,908 and was higher by 1.3% compared to the previous year. The number of employees in June 2017 was 6% higher than in December of the previous year. The largest increase in the number of employees was recorded in the administrative sector and auxiliary service activities, and the largest decline was in the real estate business sector.

The total number of unemployed persons in June 2017 was 46,781, which is 5.5%[1] less compared to December 2016. According to the data of the Employment Agency of Montenegro, the unemployment rate in June 2017 amounted to 20.16% and it is higher by 2.93 p.p. than the rate recorded in June 2016.

New packages of fiscal consolidation measures

In order to stop the negative fiscal risks that characterized the previous period and make public finances sustainable, two packages of fiscal consolidation measures have been adopted. The plan for remedying the budget deficit and public debt for the period 2017-2021, which was adopted together with the Budget for 2017, defined the measures on the budget's revenue and expenditure side, has a total value of €126.9 mil. or 3.2% of GDP. In order to make the effects of consolidation more significant and achieved in a shorter period, an additional package of measures was defined, which was elaborated within the framework of the Fiscal Strategy for the period 2017-2020, which provides additional fiscal adjustment in the amount of €117.0 mil. or 2.8% of GDP.

According to the Ministry of Finance, at the end of June 2017, the government debt (gross) amounted to 2,483.1 million euros or 62.7% of GDP. Out of the above amount, EUR 474.1 million or 12% of GDP was on the domestic debt, while external debt amounted to EUR 2,008.9 million or 50.8% of GDP.

High level of solvency and liquidity in the banking sector

The banking market in 2016 is characterized by a high level of liquidity with the growth of liquid assets of 8.1% on annual level. Total loans of banks registered modest growth in 2016. Nevertheless, considering new loans, it can be said that credit activity has intensified.

The amount of non-performing loans (NPLs) at the end of 2016 amounted to EUR 248.6 million (10.3% of total loans) and were 17.1% lower than at the end of 2015. The trend of improving the quality of the loan portfolio continued, so that the NPLs at the end of June 2017 amounted to EUR 228.1 million and accounted for 8.8% of total loans.

In order to increase banks' liquidity and stimulate lending, the Council of the Central Bank of Montenegro (CBM),on 6 March 2017, cut the mandatory reserve requirement ratios by 2 percentage points (from 9.5% to 7.5% and from 8.5% to 6.5% for deposits with maturity up to or more than one year, respectively). The long-term tendency of reducing active and passive interest rates was continued in 2016.

1 The decline in the number of unemployed persons is largely the result of the Employment Agency of Montenegro's decision that university students, who are included in the program of vocational training, are deleted from the records of the institution during the duration of the program (15th January- 15th October every year).

After the positive annual inflation rates were recorded in Montenegro in 2015, inflation rates in 2016, observed over annual rates per month, were low or negative.

Inflation was low and stable

Consumer prices recorded an increase of 0.5% in June 2017 compared to the end of the previous year. Annual inflation in June amounted to 2.1% and was higher by 1.1 percentage points, compared to December of the previous year, when it was 1%, while annual inflation measured by the harmonized index of consumer prices was 2.4%.

Reduction in the current account deficit

The current account deficit in 2016 amounted to 715 million euros or was 48.1% higher compared to 2015. According to preliminary data, in the first six months of 2017, the current account deficit amounted to EUR 631.3 million or 5.1% less compared to the same period in 2016.

In the first half of 2017, total exports of goods amounted to EUR 163.5 million, an increase of 7% compared to the previous year, while the imports of goods increased by 8.4% and amounted to EUR 1 billion.

In 2016, net inflow of foreign direct investment (FDI) amounted to EUR 371.6 million, which is by 40% less compared to 2015. FDI registered a decline in 2016, but there was still a significant net inflow of around 9.8% of GDP. According to preliminary data, the net inflow of FDI in the period January - June 2017 amounted to 220 million euros, an increase of 41.7% compared to the same period of the previous year.

Table MN1 Main economic indicators

	2015	2016	2017		
		Q4	Q1	Q2	Q3
ECONOMIC ACTIVITY					
Real GDP (% change, yoy)	3.4	3.4	3.2	5.1	4.7
Real private consumption (% change, yoy)	2.2	1.0	1.1	-0.2	-2.7
Real government consumption (% change, yoy)	1.9	0.7	0.3	1.0	-0.4
Industrial output (% change, yoy)	7.9	0.6	-6.6	0.9	3.6
Unemployment rate (LFS, %)	17.6	17.5	17.4	15.1	14.8
Nominal GDP (EUR million)	3,625	946	747	946	1,392
GDP per capita (EUR)*	5,826	1,520	1,201	1,521	2,236
PRICES, WAGES, AND EXCHANGE RATES					
Implicit GDP deflator (% change, yoy)	1.4	-0.19	0.9	2.17	-2.36
Consumer prices (% change, annual change: end month/end month-12)	1.4	0.4	0.5	-0.13	0.23
Producer prices (% change, annual change: end month/end month-12)	0.0	0.03	0.3	-0.2	-0.1
Average gross wage (% change, yoy, average of monthly data)**	0.3	4.0	3.8	1.8	1.10
FOREIGN TRADE AND CAPITAL FLOWS					
Exports of goods (EUR million)***	325.0	105.5	81.2	82.3	111.9
Exports of goods (EUR, % change, yoy)	-9.0	5.3	36.3	-11.6	28.7
Imports of goods (EUR million)***	1,789.0	493.1	443.3	591.9	597.1
Imports of goods (EUR, % change, yoy)	3.2	10.9	20.9	1.4	6.8
Current account balance (EUR million)	-483	-290	-322	-313	250
Current account balance (% of GDP)	-13.3	3.9	11.9	-16.8	-18.1
Gross foreign direct investment (EUR million)	757.0	135.2	128.3	145.8	135.6
Foreign exchange reserves (EUR million, eop)***	674	792	780	723	740
GOVERNMENT FINANCE**					
Revenue (EUR million)	1,327.0	403.2	297.7	384.2	434.0
Expense (EUR million)*****	1,380.0	504.5	368.2	419.0	431.6
Net operating balance (EUR million)******	-53.0	-101.3	-70.5	-34.8	2.4
Capital expenses (EUR million)	238.0	39.5	9.0	32.1	60.0
Net lending/borrowing (EUR million) *******	-276.0	-140.8	-79.5	-66.9	-57.6
Domestic government debt (EUR million, eop), national methodology	320.0	400.2	431.3	474.1	431.3
Foreign government debt (EUR million, eop), national methodology	1,956.0	2,002.7	2,001.6	2,008.9	2,058.9
Total government debt (% of GDP), national methodology	62.8	63.7	59.1*	59.3	61.9
MONETARY INDICATORS					
Total domestic credit (% change, yoy, eop)	0.8	-1.0	3.1	9.6	7.6
DMBs credit to households (% change, yoy, eop)	3.1	19.7	29.1	-7.5	-8.2
DMBs credit to enterprises (% change, yoy, eop)	2.7	6.5	-4.5	0.7	-16.3
DMBs credit rate for enterprises, short-term, (%, pa)	8.0	6.0	5.9	5.8	5.6
DMBs credit rate for households, short-term (%, pa)	9.6	9.2	8.7	9.1	8.7

Notes: *Population data (denominator) used are Monstat estimates.
** Quarterly gross wage data are year to date.
***Data are in thousands for 4th quarter of 2016, and 1st and 2nd quarter of 2017.
****Quarterly budget data are year to date. Debt data exclude local governments.
*****Data refer to current expenses only, and exclude capital expenses.
******Calculated as a difference between revenues and current expenses.
*******Calculated as a difference between net operating balance and capital expenses
.

Conventional abbreviations: pa – period average, eop – end of period, yoy – year on year, EUR – euro, DMB – deposit money bank.
Sources: Central bank of Montenegro, Statistical Office of Montenegro, Ministry of Finance.

Table MN2 Summary of projections

	2017	2018	2019
Real GDP (% change)	**2.7**	**3.2**	**2.3**
Real private consumption (% change, yoy)	-0.9	-0.3	1.1
Real government consumption (% change, yoy)	-1.7	-1.5	-0.6
Nominal GDP, EUR million	3,957.2	4,192.4	4,372.2
Exports of goods and services (constant prices, % change)	2.5	1.8	2.0
Imports of goods and services (constant prices, % change)	2.7	1.6	-1.2
Current account balance (% of GDP)	-19.1	-18.6	-16.8
Consumer prices (% change, pa)	2.3	3.1	2.1
GDP deflator	2.1	2.7	1.9
Unemployment rate (LFS, %)	17.8	17.0	16.6

Conventional abbreviations: pa – period average, eop – end of period, EUR – euro.
Source: Ministry of Finance of the Government of Montenegro.

Projections summary

Strengthening of fiscal stability

In the period 2017–2019, the priority of the economic policy is the strengthening of fiscal stability, and within such framework, generating the budget surplus and setting a downward trend of the public debt from 2019, while strengthening the economic activity and competitiveness of the Montenegrin economy. Projections in table MN2 reflect the official projections of the Government of Montenegro presented in the "Montenegrin Fiscal Strategy 2017–2020".

S E R B I A

Competitive position improved as a result of a more favorable macroeconomic and business environment

Recent economic developments

Serbia opened Chapter 30-Economic relations with foreign countries

The strategic goal of the Serbian's Government is to become part of the European Union (EU). In this regard, Serbia opened Chapter 30 (Economic relations with foreign countries) in negotiations with the EU. Consequently, The Republic of Serbia has committed to break up all free trade agreements that it had concluded with Kazakhstan, Turkey, Belarus and the Russian Federation. The trade volume between Serbia and the Russian Federation is the largest, compared with the remaining three countries. For example, trade in 2017 has significantly increased compared to 2015 and 2016, especially Serbian's export. Therefore, abolition of a free trade agreement with Russia can indeed be a huge problem. Chapter 30 is of great importance for the Serbian economy, because Serbia would become part of a single customs union and the common EU market.

Economic activity continues to follow a stable growth path

According to the final data published by the Statistical Office of the Republic of Serbia, Serbian GDP recorded annual growth rate amounting to 2.8% in 2016. Given the fact that economic activity has been performed under negative impact of the fiscal consolidation measures, the recorded growth in 2016 could be considered as success of the economic policy. Although GDP continued to follow stable growth tendencies throughout 2017, initial projections of around 3% of GDP have not been fulfilled mainly due to lower agricultural production.

In the third quarter of 2017, GDP recorded a growth of 2.1% when compared to the same period in 2016, while annual growth for 2017 has been estimated to 1.9%. When considering expenditure approach of measuring GDP, the main positive impact on recorded growth came from the private consumption rising by 2.0%, 1.6% and 1.7%, respectively (by quarters). Gross investments and state consumption both recorded respectable rise in the third quarter 2017 amounting to 6.2% and 1.0%, respectively. Private consumption should be the most important GDP component to fuel growth in 2018 as well, given the slight rise of the wages in the public sector.

If production structure is analysed, both industrial production and sector of services have had positive impact on the economic activity in 2017. Highest growth rates were recorded in trade, tourism and transport. After negative weather conditions in the first half of 2017, a solid recovery of the construction industry could be noticed with annual growth of 2.8%. Agriculture had an extremely negative impact on the economic activity in 2017 since total output of this sector dropped by around 10% on annual basis influencing 0.8 p.p. lower GDP.

Labour market recovery continues

Labour market performance has been mildly improving during 2017. Activity of the workforce has significantly increased followed by the decline of the unemployed and the rise of the employed as depicted by the Labour Force Survey (LFS) data. After the decline in the employment rate by 1.3 p.p. and the increase in the unemployment rate by 1.6 p.p. in the first quarter of 2017 compared with the fourth quarter of 2016, both the employment and unemployment rates show further improvements during the second and third quarters of 2017. This development in the labour market is not surprising given a deceleration in economic activity in the first months of 2017. In the third quarter of 2017, the LFS-based employment rate was 48.2% up from 44.2% in the first quarter of 2017, while the unemployment rate fell to 12.9% showing an improvement of 1.7 p.p.

The registered number of employees has been growing on average by more than two and a half p.p. per quarter in 2017, while the number of registered jobseekers went down by 8.8% on average in 2017 compared with the previous year. Our forecast shows that the registered unemployment rate will continue to follow a decreasing trend. It will stand at less than one quarter in 2018 approaching the lower boundary of forecast in the fourth quarter of the year.

The real gross and net wages will continue to increase in 2018. This rise will be based on at least three reasons —rise in economic activity, stable inflation and the increase in the compulsory minimum wage. The higher minimum wage and the administrative correction of the public sector wages as of January 2018 will raise wages of all employees.

Restrictive fiscal policy is coming to the end

After three years of the very restrictive fiscal policy, the fiscal deficit is under control. During the period of fiscal consolidation, Serbian Government undertook several restrictive measures, including cut in pensions and public sector wages, and also restriction to new employments in public sector. Eventually, fiscal deficit in 2017 is expected to be in surplus, for the first time since 2005, which is far above projected deficit around 1.7% of GDP (according to the Fiscal Strategy in 2016). Beside fiscal balance improvement, share of public debt in GDP considerably dropped in 2017 (almost 8 p.p. in first three quarters), following the strong appreciation of RSD against USD, low interest rates and continuous primary surplus.

Yet, restrictive measures in 2017 on the expenditure side have been moderately successful, so that the deficit stabilization has been achieved mostly by the unanticipated surplus on the revenue side. The Government made an agreement with the IMF to nominally increase wages in public sector (up to 10%) and pensions (5%) in 2018.

NPL write-off in progress

Following the NPL Resolution Strategy of the Government, the National Bank adopted the Decision on the Accounting Write-off of Bank Balance Sheet Assets in August 2017. This resulted in accelerated decline of NPL at the end of the third quarter in 2017, reaching record high amount of written-off NPL (around RSD 54 billion) and the lowest share of NPL in total loans (around

12%) since global crisis outbreak. The high amounts of NPL write-offs to both non-financial corporations and households, and appreciation of RSD in 2017 explain moderate nominal increase in recorded credit activity, being arguably of a temporary nature. Increase in total domestic loans in September 2017 was almost 10%. The upward trend in credit activity was especially visible when only new corporate loans are considered – amount of new loans in the third quarter of 2017 was 25% higher than in Q2. Dinarisation of loans was achieved to a lesser extent: tangible increase in share of RSD households' loans (compared to the end of 2016) was partially offset by decline in share of RSD corporate loans.

The interest rates on corporate and households' loans have remained stable and low, despite higher inflation in 2017. The National Bank of Serbia continues policy of monetary easing in second half of 2017, by cutting policy rate two times by 0.25 p.p.

Inflation is stable and moves within the target band

Year-on-year inflation since the start of the year has moved within the target band (3.0±1.5%), standing in September 2017 at 3.2%. Due to low inflationary pressures that are present for a long period of time as well as improving macroeconomic indicators, the Executive Board of the National Bank of Serbia has decided to reduce key interest rate by 0.5 p.p. Inflationary pressures stay low, as confirmed by the trend of core inflation after excluding energy, food, alcohol and cigarettes, which decreased in September to 1.5%, at the same level as at the end of 2016. The average rate of the dinar appreciation against the euro in the first three quarters of 2017 was 3.5%, while in relation to the US dollar, dinar appreciation amounted to 4.4%, mainly to the considerable appreciation of the euro to the dollar. The appreciation of the dinar was influenced by the high inflow of foreign direct investments, increased exports, greater interest of foreign investors in government securities and growth in FX-indexed bank assets. In the following period the exchange rate of the dinar will depreciate. The intensity of depreciation will largely depend on the implemented monetary policy of major central banks worldwide but also of the movement of key domestic macroeconomic indicators.

Both exports and imports recorded high growth rates

Serbia's current account deficit during the first three quarters of 2017 deteriorated in relation to 2016. This was attributable to the worsening of the trade balance and the higher outflow of investment income – most notably of reinvested earnings related to FDIs. These tendencies were partly offset by higher inflow of transfers, referring mostly to remittances, but also to transfers received by the general government.

As regards the commodity trade, both exports and imports recorded high growth rates, but increase in imports was more substantial in absolute terms. The composition of commodity trade did not change substantially compared to the previous year: most important export products include cars, electrical appliances, metals and agricultural products, whereas imports are dominated by machinery and fuels. The growth in exports was mainly

Table SRB1 Main economic indicators

	2015	2016	2017		
		Q4	Q1	Q2	Q3
ECONOMIC ACTIVITY					
Real GDP (% change, yoy)	0.8	2.5	1.1	1.4	2.1
Real private consumption (% change, yoy)	0.2	0.9	2.0	1.6	1.7
Real government consumption (% change, yoy)	-	2.3	0.4	1.5	1.0
Industrial output (% change, yoy)	8.3		1,4	2,8	6,9
Unemployment rate (registered, %, pa)	27.1	25.5	25.5	24.3	23.3
Nominal GDP (EUR million)	33,491	34,617	7,985	8,908	9,693
GDP per capita (EUR)	4,720	4,904	-	-	-
PRICES, WAGES, AND EXCHANGE RATES					
Implicit GDP deflator (% change, yoy)					
Consumer prices (% change, yoy, pa)	1.5	0.5	2.4	0.5	-0.2
Producer prices (% change, yoy, pa)	0.7	1.3	1.5	-0.6	0.3
Average gross wage (% change, yoy, pa)	-2.4	1.9	1.2	0.9	0.9
Exchange rate, RSD/EUR (pa)	121.6	117.1	124.0	120.9	119.4
Exchange rate, RSD/USD (pa)	111.2	99.2	116.1	105.7	101.3
FOREIGN TRADE AND CAPITAL FLOWS					
Exports of goods (EUR million)	12,041	3,511	3,504	3,933	3,778
Exports of goods (EUR, % change, yoy)	7.9	15.9	13.4	13.2	12.7
Imports of goods (EUR million)	16.388	4.561	4.587	5.004	4.730
Imports of goods (EUR. % change, yoy)	5.8	5.5	15.4	10.2	13.3
Current account balance (EUR million)	-1.577	-247	-694	-336	-384
Current account balance (% of GDP)	-4.7	-	-	-	-
Gross foreign direct investment (EUR million)	2,114	492	582	632	747
Foreign exchange reserves (EUR million, eop)	11,813	11,761	11,213	11,029	11,816
Foreign debt (EUR million, eop)	26,234	26,488	26,135	25,435	26,033
GOVERNMENT FINANCE*					
Revenue (RSD billion)**	1,695	490	450	504	497
Expense (RSD billion)**	1,844	540	438	471	459
Net = Gross operating balance (RSD billion)**	-	-50	12	32	38
Net acquisition of non-financial assets (RSD billion)**	-	53	12	36	30
Net lending/borrowing (RSD billion)**	-149	-103	0	-3	8
Domestic government debt (EUR million, eop), national methodology***	9,420	9,149	9,034	9,271	9,371
Foreign government debt (EUR million, eop), national methodology***	14,773	15,671	15,514	14,624	14,737
Total government debt (% of GDP), national methodology	74.5	73.0	69.1	65.6	65.3
MONETARY INDICATORS					
Narrow money, M1 (% change, yoy, eop)	17.1	20.5	18.2	13.3	8.3
Broad money, M2)5 (% change, yoy, eop)	14.4	11.6	12.1	7.4	5.6
Total domestic credit (% change, yoy, eop)	5.7	7.8	9.5	7.9	9.8
DMBs credit to households (% change, yoy, eop)	4.7	13.1	15.1	13.0	12.3
DMBs credit to enterprises (% change, yoy, eop)	2.2	3.8	5.0	3.6	7.7
DMBs credit rate for enterprises, short-term, (%, pa)****	6.4	5.3	4.0	4.1	4.1
DMBs credit rate for households, short-term (%, pa)*****	13.3	9.4	8.3	8.1	8.2

Notes: The registered unemployment rate is calculated based on the registered number of the unemployed and the registered employment; The data about registered unemployment and employment are taken from the periodicals of the National Employment Service and the Statistical Office of the Republic of Serbia, * Data refer to consolidated general government, unless stated otherwise ** On the cash principle, cumulative from the beginning of the year,*** Central government debt only, **** New loans, ***** New loans, weighted average interest rates on consumer, cash and other loans.

Conventional abbreviations: pa – period average, eop – end of period, yoy – year on year, EUR – euro, USD – U.S. dollar, RSD – dinar, DMB – deposit money bank.

Sources: National Bank of Serbia, Statistical Office of the Republic of Serbia, Ministry of Finance.

Table SRB2 Summary of projections

	2017	2018	2019
Real GDP (% change)	**1.9**	**3.3**	**3.5**
Exports of goods and services (constant prices, % change)	9.7	7.3	6.5
Imports of goods and services (constant prices, % change)	10.7	8.5	7.0
Current account balance (% of GDP)	-4.6	-4.2	-4.1
Consumer prices (% change, pa)	3.0	2.9	2.8
Exchange rate, national currency/EUR (pa)	118.5	122.3	123.9
Unemployment rate (registered, %, pa)	24.0	23.2	21.9
General government balance (ESA 2010 definition, % of GDP)	0.8	0.5	0.5
Broad money, M4* (% change, eop)	-	-	-
Total domestic credit (% change, eop)	4.0	8.0	8.0

Notes: Cut-off date for information used in the compilation of projections was May13, 2016, * Data on M3, the broadest category of money for which statistic is compiled by the NBS.

Conventional abbreviations: pa – period average, eop – end of period, EUR – euro.

Sources: Authors' projections, Fiscal strategy of the Republic of Serbia for 2018 with projections for 2019 and 2020, the IMF WEO.

driven by electrical appliances, metals and tires, while cars (due to reduced production), cereals (due to unfavourable weather conditions) and tobacco products had a negative contribution. As regards growth in imports, it was mainly attributable to petroleum, metals and electrical machinery, whereas decline in imports of transport vehicles negatively affected total commodity imports growth.

Policy assumptions and projections summary

Projections in table SRB reflect the optimistic policy assumptions stemming from the recent success in macroeconomic stabilization and fiscal consolidation. Real GDP will most likely continue to grow at slightly higher pace than in 2016, probably exceeding 3% in 2018, while general government balance will continue to decrease. External sector variables will remain on the stable path, but high rate of export growth is expected to slow down. Due to policy of monetary easing and low interest rates it is reasonable to expect continuation of credit market recovery at similar pace observed in 2016, while inflation will probably moderately accelerate. However, it will need some time of steady growth and more sound structural reforms for the registered unemployment to substantially decrease. ■

SLOVENIA

Continuing the economic growth, waiting for sustainability

Recent economic developments

Slovenia – "growth with few structural developments"

Following years of discussions to ensure sufficient long-term care funding and develop home care by creating a level playing field and allowing patients to organize their own care, the Long-Term Care Act was submitted to public consultation by July 2017. Also, the amended Health Services Act is being discussed in Parliament and includes new criteria for granting concessions for public healthcare services to improve transparency and accessibility. The 2017 Health Care and Health Insurance Act focuses health-sector reforms on improving financing of hospitals, cost containment and revenue stabilization (also by broadening the contribution base).

The proposals followed more than a decade of discussions on structural reforms, in particular in the areas like labor market, pensions, healthcare, long-term care, education, science and culture. Nevertheless, the proposals were followed with a lot of critiques. Based on the recommendations of international organizations (pointing, e.g., to problems of demographic change, particularly noticeable for Slovenia), it would be expected that the

sectors, in particular healthcare and long-term care, finally adopt the needed reforms, improving the structural position of Slovenia and helping it to grow in a sustainable and long-term way.

Stable and solid economic growth continues

In 2017, economic activity continued to improve. In the first, second and third quarter of the year, gross domestic product increased by 5.1%, 4.6% and 4.5% on a year-on-year basis respectively. Real GDP growth is forecast to reach 4% in 2018 and 3.3% in 2019, and should be driven mainly by domestic demand. Domestic demand and private consumption continued to expand. Spurred by strong exports, the rise in industrial output was strong. Risks to the growth outlook are, on the upside, primarily domestic in nature, while downside risks are mainly external and relate to the future development of energy and raw material prices, resulting from the macroeconomic and political situation in Europe and world countries. Investment was significantly higher than in 2016, in particular in the first quarter of the year, related to the higher private investment due to continuing deleveraging of the Slovenian companies, as favorable economic conditions are reflected in higher demand for loans, and the creditworthiness of borrowers is improving.

Labor market conditions improve further

Labor market conditions continued to improve in 2017, in particular in the second quarter of the year. Employment growth remained high in most sectors as increasing exports, consumption and investment boosted labor demand in Slovenia. Employment is expected to continue to grow by 1-2% in the following years, but decelerate as labor shortages will likely increase in the tightening labor market. The unemployment rate is expected to decline to 5.2% in 2019. As the forecasted unemployment rate approaches its natural rate, wage pressures are set to rise. The level of employment will be on the rise in practically all sectors, but will be increasingly affected by demographic changes. Unemployment will drop further to below 90,000 persons for the year as a whole.

The government deficit reduces, public investment rises

In 2017, the government deficit declined further reflecting favorable economic conditions, the retention of the remaining measures that contain expenditure growth, and low expenditure on investment. Public investment increased after a plunge of nearly 30% in 2016. Both the compensation of public employees and pensions continued rising. In 2018, the general government balance is expected to be close to zero as tax revenues and social contributions should continue to grow strongly with interest expenditure decreasing significantly. Further improvement of the general government balance is expected in the coming years mainly due to cyclical factors. Both the general government revenue as well as expenditure were raised throughout this period, with revenue surpassing the expenditure in the second quarter of 2017.

First signs of improvement in lending activity

Banks' lending activity showed signs of improvement. Credits to households significantly expanded, for both housing and consumer loans, reaching 7.0% growth on year-to-year basis in the third quarter of 2017. Also, credits to enterprises continued to shrink, but on a lower rate than in 2016. Probably, this is a sign of improvement in macroeconomic environment, as well as activities for the deleveraging of private companies. The enterprises started to take out more investment loans and loans for financing current operations and fewer loans for refinancing existing liabilities than in previous years. In further years, the volume of bank loans is expected to expand further, but enterprises will be financing their operations using internal resources and by issuing debt securities, to a greater extent than before the financial crisis.

Deflation beaten, price changes stay moderate

After a period of fighting with deflation, Slovenia recorded consumer and producer price growth in the first three quarters of 2017. In the following years, inflation will hover around 2% on a yearly level. The growth of domestic and foreign demand boosts particularly the growth of service prices. Price rises in energy and non-energy goods will in future remain moderate in the absence of commodity shocks from abroad. Deflationary pressures have eased mainly as a result of smaller energy price declines and stronger food price growth. Core inflation is rising slightly due to higher prices for services. Also, the euro is expected to continue to appreciate against the currencies of some of Slovenia's main trading partners in 2018 and 2019, but the price competitiveness of Slovenia's economy remains relatively favorable.

Strong goods exports and imports enhanced

After a strong increase in 2016, both goods exports and imports remained very high in the first three quarters of 2017 (both with more than 10% nominal increase in the first and third quarter of the year). Export growth will strengthen in 2018 and 2019 thanks to the higher growth in foreign demand and the improving competitiveness of exporters. Over the entire period, we expect a continuation of export growth across all main groups of manufactured goods. The growth of imports will remain high in 2017–2019 amid further strong growth of exports and domestic consumption. The current account surplus widened further in 2017 and will remain high also in 2018 and 2019 (at around 5% of GDP). The high surplus reflects several years of private sector deleveraging and the still low level of domestic consumption, particularly investment.

FDI inflow slowly increasing in 2017

For the fourth consecutive year, the inflow of foreign direct investment increased in 2017. In the first three quarters of the year the net inflow amounted to EUR 707 million. Its Foreign Portfolio Investment fell by EUR 138.3 million in September 2017. Among concrete investments, in Maribor, TAM (a motor vehicle producer) and Maribor Airport are announced to be taken over by Chinese investors. Among the announced investments in 2016, in 2017 Austrian automotive giant Magna Steyr, indeed, started with opening up first employment vacancies for a projected newly built factory.

Policy assumptions and summary of projections

Broad-based economic growth will continue

The projected values of the main macroeconomic aggregates for Slovenia are those presented in the Autumn Forecast 2017 of the national Institute for Macroeconomic Analysis and Development (IMAD). The projected value of the general government deficit is based on the Autumn 2017 Economic Forecast of the European Commission.

The macroeconomic projections for Slovenia forecast continuing the broad-based economic growth, hovering between 3 and 4% in the growth of the gross domestic product in 2018-2019. The strong growth of exports will reflect the strengthening of foreign demand and the continued favorable competitive position of the tradable sector. The rising demand will contribute to a further increase in investment in machinery and equipment, while favorable borrowing conditions and rising disposable income will boost housing investment. Other construction investment will also continue to increase, including the planned absorption of EU funds. Favorable labor market conditions will remain the main factor of growth in disposable income

Table SI1 Main economic indicators

	2015	2016		2017	
		Q4	Q1	Q2	Q3
ECONOMIC ACTIVITY					
Real GDP (% change, yoy)	2.3	3.5	5.1	4.6	4.5
Real private consumption (%change, yoy)	2.1	6.5	3.8	2.8	2.7
Real government consumption (% change, yoy)	2.7	1.1	0.9	1.3	1.8
Real investment (% change, yoy)	0.2	3.8	14	7.5	1.9
Gross-fixed capital formation (%change, yoy)	-1.6	0.7	13	8.7	6.1
Industrial output (% change, yoy)	5.6	6.6	7.3	5.0	6.9
Unemployment rate (registered, %, pa)	12.3	10.6	11.1	9.4	8.9
Nominal GDP (EUR million)	38,837	10,396	9,909	11,018	11,107
GDP per capita (EUR)	18,823	5,032	4,797	5,336	5,760
PRICES AND WAGES					
Implicit GDP deflator (% change, yoy)	1.0	1.0	1.1	2.2	2.3
Consumer prices (% change, yoy, pa)	-0.5	0.6	1.8	1.4	1.2
Producer prices (% change, yoy, pa)	-0.2	-0.1	1.7	2.3	2.3
Average gross wage (% change, yoy, pa)	0.7	1.9	1.5	2.3	2.8
FOREIGN TRADE AND CAPITAL FLOWS					
Exports of goods (EUR million)	24,039	6,407	6,876	7,157	7,041
Exports of goods (EUR, % change, yoy)	5.3	4.5	10.1	8.2	12.6
Imports of goods (EUR million)	22,563	6,180	6,508	6,691	6,510
Imports of goods (EUR, % change, yoy)	5.1	6.7	11.3	8.3	10.7
Current account balance (EUR million)	1,698	343	583	785	872
Current account balance (% of GDP)	4.4	3.3	5.9	7.1	7.8
Gross foreign direct investment (EUR million)	1,465	41	364	86	257
Foreign exchange reserves (EUR million, eop)	787	705	754	751	766
Foreign debt (EUR million, eop)	46,627	44,805	44,852	44,543	43,503
GOVERNMENT FINANCE*					
Revenue (EUR million)**	17,419	4,544	4,314	4,778	4,643
Expense (EUR million)**	18,541	4,749	4,461	4,747	4,662
Net = Gross operating balance (EUR million)**					
Net acquisition of non-financial assets (EUR million)**					
Net lending/borrowing (EUR million)**	-1,122	-205	-147	31,1	-18,8
Domestic government debt (EUR million, eop)	17,256	20,500	22,535	24,259	24,951
Foreign government debt (EUR million, eop)	10,023	6,629	6,169	5,348	5,129
Total government debt (percent of GDP)	82.6	-	-	-	-
MONETARY INDICATORS					
Total domestic credit (% change, yoy, eop)	-12.6	-1.4	-1.4	1.7	5.6
DMBs credit to households (% change, yoy, eop)	-1.7	3.4	3.4	5.4	7.0
DMBs credit to enterprises (% change, yoy, eop)	-21.1	-7.0	-7.0	-2.0	8.1
3 months EURIBOR (%, pa)	0.21	-0.26	-0.31	-0.33	-0.33
6 months EURIBOR (%, pa)	0.31	-0.17	-0.21	-0.24	-0.27
DMBs credit rate for enterprises, short-term, (%, pa)	4.3	2.4	2.4	2.3	2.5
DMBs credit rate for households, short-term (%, pa)	4.3	3.1	3.2	3.2	3.3

Notes: * Data refer to consolidated general government, ** ESA 2010.

Conventional abbreviations: pa – period average; eop – end of period; yoy – year on year; EUR – euro; DMB – deposit money bank.

Sources: Statistical Office of the Republic of Slovenia, Bank of Slovenia, Ministry of Finance, Institute for Macroeconomic Analysis and Development – IMAD and calculations by IER.

Table SI2 Summary of projections

	2017	2018	2019
Real GDP (% change)	**4.4**	**3.9**	**3.2**
Real private consumption (% change)	3.3	3.0	2.3
Real government consumption (% change)	1.1	0.9	0.9
Gross fixed capital formation (% change)	9.0	8.0	7.0
Exports of goods and services (constant prices, % change)	8.8	7.5	6.1
Imports of goods and services (constant prices, % change)	8.9	7.7	6.3
Current account balance (% of GDP)	4.7	5.1	5.3
Consumer prices (% change, pa)	1.5	1.6	2.1
Exchange rate, national currency/USD (pa)	1.13	1.18	1.18
Unemployment rate (registered, %, pa)	9.5	8.7	8.4
General government balance (ESA95 definition, % of GDP)	-0.8	0.0	0.4

Note: Cut-off date for information used in the IMAD's compilation of projections was September 6, 2017.

Conventional abbreviations: pa – period average; eop – end of period; USD – U.S. dollar.

Sources: Institute for Macroeconomic Analysis and Development - IMAD (Autumn Forecast of Economic Trends 2017) and European Commission (Autumn 2017 Economic Forecast).

and household consumption. In both years a continuation of modest growth in government consumption is also expected.

With growth in employment and economic activity, registered unemployment will decline further in 2017–2019. Under the impact of employment growth and demographic change (larger outflows from unemployment into retirement and hiring to replace retirees), unemployment will continue to fall in 2018 and 2019. The registered unemployment rate is forecast to drop to 10.2% in 2017 and 9.5% in 2018. Inflation will hover around 2% in the next few years. Price rises in energy and non-energy goods will remain moderate in the absence of commodity shocks from abroad.

In 2018, the general government balance is expected to be close to zero as tax revenues and social contributions continue to grow strongly and interest expenditure is expected to decrease significantly. At the same time, the compensation of public employees and expenditure on social benefits are projected to increase further. Under a no-policy-change assumption, the general government balance is expected to record a surplus of 0.4% of GDP in 2019 mainly due to economic growth and improved labor market conditions. ■

ANALYSIS

The national competitiveness and labor market efficiency in SEE-6 countries

Launched in 1979, the World Economic Forum's Global Competitiveness Index (GCI) measures the factors that drive long-term growth and prosperity. GCI defines competitiveness as *the set of institutions, policies, and factors that determine the level of productivity of an economy*, which in turn is the main determinant of long-term growth and prosperity. It helps policymakers identify challenges to be addressed and strengths to build on when designing the economic growth strategies for their countries.

The World Economic Forum bases its competitiveness analysis on a comprehensive framework measuring microeconomic and macroeconomic foundations of national competitiveness, grouped into 12 pillars: institutions, infrastructure, macroeconomic environment, health and primary education, higher education and training, goods market efficiency, labor market efficiency, financial market development, technological readiness, market size, business sophistication, and innovation. These pillars are in turn organized into three subindexes: basic requirements, efficiency enhancers, and innovation and sophistication factors. The three subindexes are given different weights in the calculation of the overall Index, depending on each economy's stage of development.

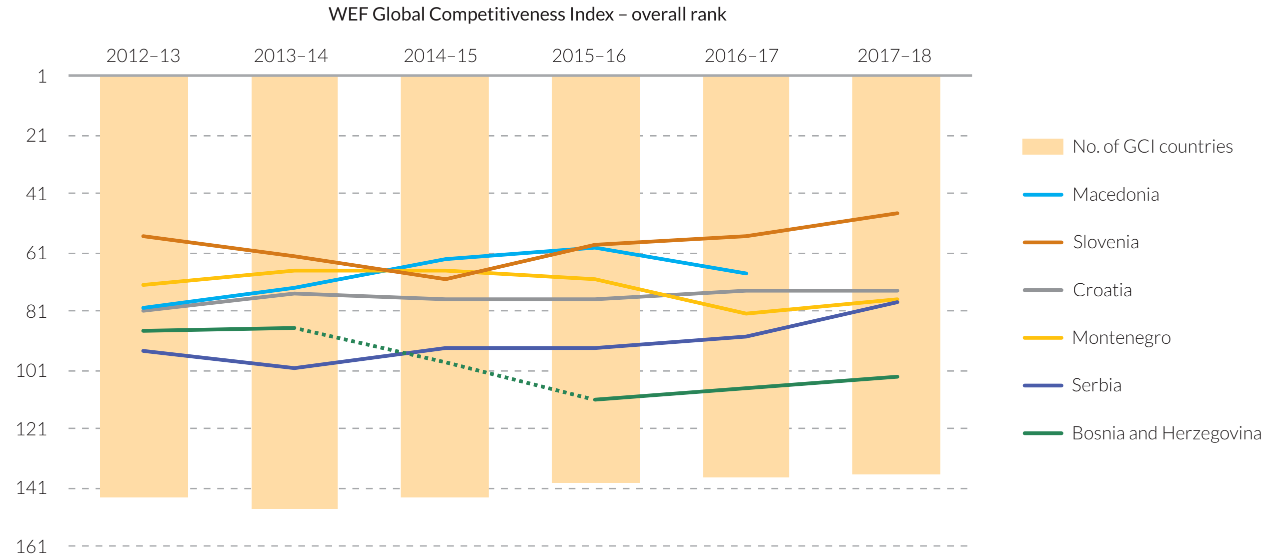
According to the overall GCI index, the most competitive SEE-6 country is Slovenia, ranking 48th in 2017, while Bosnia and Herzegovina ranks the lowest, in the 103rd place. The other SEE-6 countries rank closely together: Macedonia 68th, Croatia 74th, Montenegro 77th, and Serbia 78th. The performance of the SEE-6 countries over the medium-term shows a mixed picture (Figure A1). Serbia and Slovenia seem to have been closing the competitiveness gap to the most competitive world economies in the last years; Croatia's ranking remained stable over time; and Bosnia and Herzegovina and Montenegro seem to have lost ground. Macedonia, which displayed a positive trend before 2015, deteriorated somewhat in 2016.

Figure A2 shows the performance of individual SEE-6 countries on the 12 pillars of the GCI. All SEE-6 economies perform best on the health and primary education pillar, with an average score of 6.0 on a scale from 1 to 7. The macroeconomic pillar and the technological pillar follow with an average score of 4.7. The third competitive advantage of the SEE-6 countries is the quality and quantity of higher education, and the quality and availability of on-the-job training with an average score of 4.5. On the other hand, SEE-6 economies score on average worse on the market size pillar and the innovation pillar, the latter demonstrating the capacity for and a commitment to technological innovation.

One of the common characteristics of SEE-6 countries is a low ranking on the labor market efficiency pillar. Therefore, we have observed in more detail the performance of the countries by individual indicators in this pillar (Table A1). Among them, several stand out for their low average values[1] for the countries: cooperation in labor-employer relations; effect of taxation on incentives to work; reliance on professional management; country capacity to retain talent; country capacity to attract talent.

1 We define "low average values" as rank values above the total pillar country average rank.

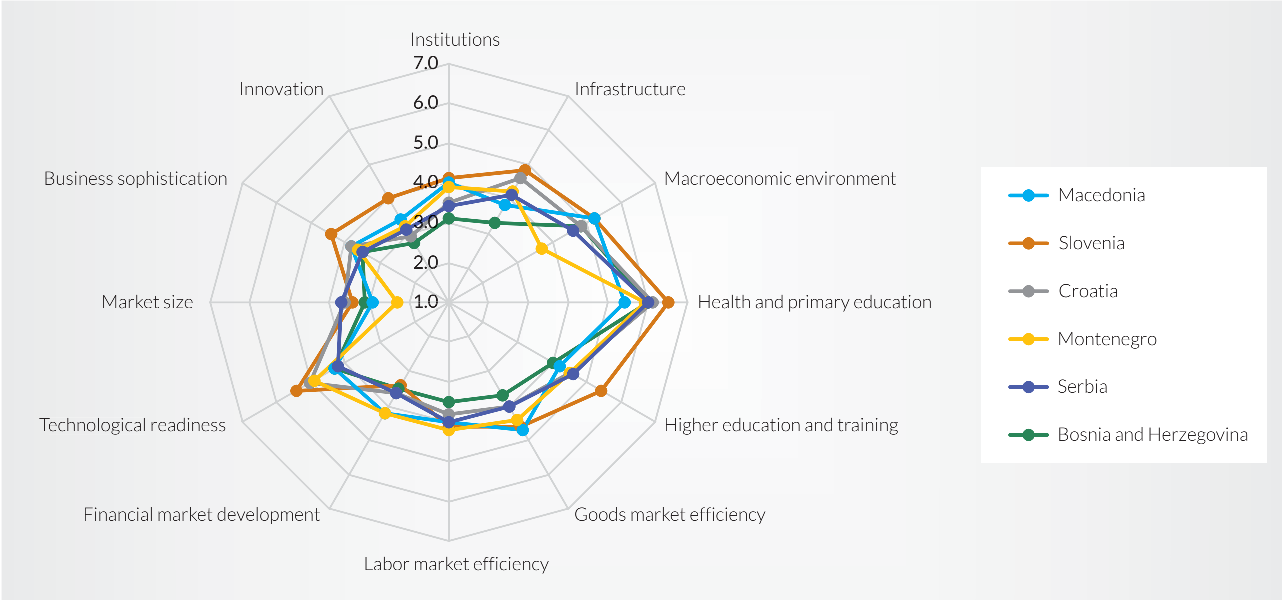
Figure A1 The GCI rankings of SEE-6 countries in the period 2012–2013 to 2017–2018



Source: WEF; The Global Competitiveness Report 2017–2018 and earlier editions.
Notes: Bosnia and Herzegovina not included in 2014–15; Macedonia not included in 2017–18.

Retaining and attracting talent are the most problematic elements of the labor efficiency. With almost no exception, the countries rank 100th or lower in the value of this indicator. It seems that the incentives to work in all SEE-6 countries are insufficient and that policymakers should put much more effort into their improvement. Problems in the cooperation in labor-employer relations are much less pronounced in Slovenia and Macedonia, while they are very problematic in Croatia. On the other hand, Macedonia and Montenegro have a much lower negative effect of taxation on incentives to work while the opposite holds for Croatia, Serbia and, in particular, Slovenia.

Figure A2 The performance of SEE-6 countries on the 12 pillars of the GCI – scores, 2017–2018



Source: WEF; The Global Competitiveness Report 2017–2018 (www.weforum.org/reports/the-global-competitiveness-report-2017-2018).
Note: Note: Macedonia 2016–17.

Table A1 **The performance of SEE-6 countries on the labor market efficiency pillar**

	Bosnia and Herzegovina		Croatia		Macedonia, FYR		Montenegro		Serbia		Slovenia		Total - averages		
	Rank	Value	Rank	Value	Rank	Value	Rank	Value	Rank	Value	Rank	Value	Average rank	Median rank	Rank std.dev.
7th pillar: Labor market efficiency	**123**	**3.5**	**107**	**3.8**	**95**	**4.0**	**74**	**4.2**	**92**	**4.0**	**82**	**4.1**	**95.50**	**93.50**	**17.58**
7.01 Cooperation in labor-employer relations	117	3.8	135	3.4	81	4.3	100	4.0	105	4.0	62	4.4	100.00	**102.50**	25.86
7.02 Flexibility of wage determination	26	5.5	66	4.9	118	4.1	55	5.1	40	5.3	107	4.4	68.67	**60.50**	36.71
7.03 Hiring and firing practices	105	3.3	131	2.6	39	4.2	73	3.7	80	3.6	132	2.4	93.33	**92.50**	36.31
7.04 Redundancy costs	26	9.2	63	15.1	47	13.0	41	11.2	18	7.7	39	10.7	39.00	**40.00**	15.84
7.05 Effect of taxation on incentives to work	123	3.0	133	2.6	51	4.1	67	4.0	125	2.9	135	2.3	105.67	**124.00**	36.78
7.06 Pay and productivity	127	3.0	101	3.5	48	4.3	76	3.8	68	3.9	77	3.8	82.83	**76.50**	27.55
7.07 Reliance on professional management	131	3.0	101	3.7	110	3.6	99	3.7	128	3.3	69	4.2	106.33	**105.50**	22.66
7.08 Country capacity to retain talent	135	1.8	131	2.1	115	2.7	100	3.0	134	1.8	93	3.1	118.00	**123.00**	18.29
7.09 Country capacity to attract talent	136	1.6	135	1.8	128	2.2	107	2.6	132	2.0	114	2.5	125.33	**130.00**	12.03
7.10 Female participation in the labor force	110	0.63	50	0.87	99	0.67	76	0.79	79	0.77	27	0.9	73.50	**77.50**	30.77

Source: WEF, The Global Competitiveness Report 2017-2018 (www.weforum.org/reports/the-global-competitiveness-report-2017-2018), Own calculations.

Note: Macedonia 2016-17. In yellow: problematic indicators.

Bosnia and Herzegovina scores best on health and primary education (56th), macroeconomic environment (64th), and technological readiness (69th). While in terms of health and primary education no indicator stands out specifically, in terms of macroeconomic environment it scores extremely high (15th) on the Government Budget balance. As for the technological readiness, it scores below the 100th place in FDI and technology transfer. Bosnia and Herzegovina scores worst in terms of institutions (126th), goods market efficiency (126th), labor market efficiency (123rd), and innovation (123rd). In terms of labor market efficiency, it scores extremely high in flexibility of wage determination (26th) and redundancy costs (26th), while it scores significantly below the 100th place in all other indicators in this pillar. Bosnia and Herzegovina is an example of a developing country—it aims high in readiness for innovation and some basic characteristics of macroeconomic and social environment while scoring low in institutions and efficiency.

Croatia scores significantly better than Bosnia and Herzegovina in almost all indicators. It achieves its best positions in infrastructure (48th), health and primary education (44th), and technological readiness (43rd). Its worst positions (below the 100th place) are in institutions (102nd), labor market efficiency (107th), and innovation (106th). In terms of individual indicators, it scores extremely high in, e.g. quality of roads (19th) and some health indicators like HIV prevalence (1st), business impact of HIV/AIDS (5th), and business impact of tuberculosis (11th). When it comes to labor market efficiency, Croatia scores high in female participation in the labor force (50th). On the other hand, it scores extremely low on cooperation in labor-employer relations and attracting and retaining talent. Croatia's main obstacle to growth seems to be the poor quality of institutions.

Macedonia, FYR achieves a better position on the total GCI score than Croatia. Its best positions lie in macroeconomic environment (44th), goods market efficiency (34th), financial market development (57th), and innovation (51st). Some indicators in goods market efficiency highly stand out—Macedonia achieves the best position of all countries regarding the number of procedures to start a business, 2nd in time to start a business and 3rd in total tax rate. On the other hand, its drawbacks lie in health and primary education (92nd), labor market efficiency (95th), and market size (110th). In terms of health and primary education, its worst indicator is surely primary education enrolment rate (127th), with several indicators of labor efficiency standing out as well: it scores extremely low in flexibility of wage determination (118th), reliance on professional management (110th), and in attracting (128th) and retaining (115th) talent. In total, Macedonia seems to be a country with high aspirations, very competitively oriented, but lagging in some basic characteristics like market size and labor, including education.

Montenegro and Serbia stand almost the same in the levels of total GCI score and are slightly below the half of the total distribution. Montenegro scores the best in the levels of health and primary education (62nd), higher education and training (61st) and, in particular, financial market development (47th) and technological readiness (48th). Among the individual indicators, HIV prevalence (joint 1st with Croatia, Serbia, and Slovenia), mobile/cellular telephone subscriptions (7th), and legal rights index (1st) stand out. But distribution of scores for individual indicators is extremely uneven in Montenegro which means that the country enjoys a rather uneven scope of development. Among the drawbacks, macroeconomic environment (116th), market size (128th), and business sophistication (101st) stand out. In Montenegro, labor market efficiency is at a slightly higher level than in all other SEE-6 countries.

Serbia enjoys a similar position as Montenegro in terms of total position in the GCI score. In terms of individual pillars, health and primary education (52nd) and higher education and training (59th) stand out in particular. Macroeconomic environment and technological readiness (both 72nd) are slightly higher than most of other pillars for Serbia. In terms of individual indicators, again, HIV prevalence is extremely low (1st), while the country scores very high also on inflation (1st) and redundancy labor costs (18th). Among the country drawbacks, institutions (104th), financial market development (104th), and both goods market efficiency and business sophistication (both 110th) stand out. Just like in Montenegro, development seems quite uneven in Serbia—while having extremely low redundancy labor costs, several other labor market efficiency indicators stand out for its poor value, in particular, the reliance on professional management (128th), and country's capacity to attract (132nd) and retain (134th) talent.

Slovenia enjoys the best overall position (48th). Except for financial market development, where it scores 106th, it scores below the 100th rank in all other aspects. Its strongest points are in health and primary education (14th) and higher education and training (24th), with technological readiness (35th), and innovation (35th) being very high as compared to other SEE-6 countries. Its high position in health and primary education is due to low HIV prevalence (joint 1st), infant mortality (7th) and indicators related to tuberculosis, while its high position in higher education and training is due to high values in the indicators of quality of math and science education (11th), tertiary education enrolment rate (14th), and secondary education enrolment rate (19th). Its main drawbacks lie in labor market efficiency (82nd), financial market development (106th) and market size (82nd). As for labor market efficiency, the country scores very low on hiring and firing practices (132nd), and the effect of taxation on incentives to work (135th). The labor market in Slovenia is rigid, and some other indicators like foreign ownership and effect of taxation on incentives to invest score are also low. Slovenia is a well-developed country, but scoring low on the flexibility of its goods, labor, and financial market means it needs to improve if it wants to provide a more competitive environment in the future.

PUBLISHER INFORMATION

This publication has been prepared by:

Editor: Duško Bodroža, Institute of Economic Sciences, Belgrade

Bosnia and Herzegovina: Mirza Huskić, The Institute of Economics Sarajevo

Croatia: Sandra Švaljek, The Institute of Economics, Zagreb

Macedonia: Tatjana Petkovska-Mirchevska (team leader), Iskra Stancheva-Gigov (coordinator), Biljana Angelova, Verica Janeska, Snezana Kostadinoska-Miloseska, Klimentina Poposka, Elizabeta Dzambaska, Aleksandra Lozanoska and Vladimir Petkovski, The Institute of Economics – Skopje, University "SS. Cyril and Methodius"

Montenegro: Milica Muhadinović, Vladimir Đurišić, Milica Vukčević, The University of Montenegro, Faculty of Economics in Montenegro

Serbia: Jelena Minović (coordinator), Aleksandar Zdravković, Kosovka Ognjenović, Duško Bodroža, Aleksandra Branković, Mihajlo Đukić, Institute of Economic Sciences, Belgrade

Slovenia: Andrej Srakar, Sonja Uršič, Institute for Economic Research, Ljubljana

Analysis: Andrej Srakar, Sonja Uršič, Institute for Economic Research, Ljubljana

Publishers:

Institute of Economic Sciences, Belgrade
Zmaj Jovina 12, 11000 Belgrade, Serbia

The Institute of Economics, Zagreb
Trg J. F. Kennedyja 7, 10000 Zagreb, Croatia

The Institute of Economics Sarajevo
Branilaca Sarajeva 47, 71000 Sarajevo, Bosnia and Herzegovina

The Institute of Economics – Skopje, University "SS. Cyril and Methodius"
Prolet 1, 1000 Skopje, Macedonia

The University of Montenegro, Faculty of Economics Podgorica
Jovana Tomaševića 37, 81000 Podgorica, Montenegro

Institute for Economic Research, Ljubljana
Kardeljeva ploščad 17, 1000 Ljubljana, Slovenia

For the publishers:
Jovan Zubović
Maruška Vizek
Muamer Halilbašić
Zoran Janevski
Nikola Milović
Boris Majcen

E-mail: SEE-6@eizg.hr

Technical editor: Vladimir Sukser

Print: Donat graf d.o.o, Grocka, Serbia

SEE-6 Economic Outlook is published twice a year (Spring and Autumn edition).