

Economic Performance

For economic and democratic reforms to be sustained, solid macroeconomic performance needs to ensue, namely, macroeconomic stability and robust economic growth. In addition, for these macroeconomic trends to occur (and to be sustained), certain key economic structural changes need to take place in the transition, including increasing the proportion of the private sector share of the economy, and increasing the competitiveness of the economy. Seven primary indicators are tracked to assess progress in economic performance (*Tables 7 and 8*): (1) export share of GDP; (2) employment in the small and medium enterprise sector as a percent of total employment; (3) foreign direct investment; (4) private sector share of GDP; (5) external debt as percent of GDP; (6) inflation; and (7) economic growth.

Overall, macroeconomic performance in recent years has been impressive in a large majority of the transition economies. This can be attributed in no small part because key economic structural changes since the transition began have been significant. By most economic performance measures, the Northern Tier CEE countries continue to outperform the rest of the transition countries.

Economic growth has been impressive among the transition countries in recent years (*Figure 19*). Since 2000, the transition region as a whole has witnessed annual economic growth rates in excess of global economic growth rates, averaging more than 5% annually. Of the three transition sub-regions, economic growth has been highest in Eurasia, averaging about 7% annually from 2000 to 2005.

Figures 20-22 attempt to address some key determinants of economic growth in the transition region. For much of the Eurasian countries, much of these high growth rates have presumably stemmed in no small part from high and rising prices of key primary product exports (particularly oil and gas, various metals, and cotton). *Figure 20* shows in fact a close correspondence (beginning in 1998) between rising oil prices and high economic growth among the three primary energy exporters in Eurasia: Kazakhstan; Russia; and Azerbaijan. As suggested in *Figure 21*, this positive relationship generally holds between energy prices and economic growth in all of Eurasia, in no small part because favorable economic developments in Russia in particular continue to spill over to many of the Eurasian countries.

In CEE, as suggested in *Figure 22*, economic growth is increasingly driven by economic growth in Western Europe as the CEE's share of exports to Western Europe increases. Moreover, while the fastest growing economies in recent years have been in Eurasia, it has been primarily the economies of the Northern Tier CEE countries that have been able to sustain relatively robust economic growth to the point where they are well above pre-transition income levels (*Figure 23*). The Northern Tier CEE countries today have economies on average 20% larger than pre-transition GDP. The transition depression was not as deep in the case of the Northern Tier CEE countries, and recovery came sooner; it's been twelve years on average since these economies bottomed out. In contrast, official GDP in seven Eurasian economies and four Southern Tier CEE

economies today is still below what it was in 1989. Georgia and Moldova have economies that remain roughly one-half the size of what they were in 1989 (*Table 8*).

However, the Eurasian economies are far from homogenous on economic growth trends. As shown in *Figure 23*, the three Eurasian non-reformers have a very favorable economic growth profile, roughly comparable to that of the Northern Tier CEE. The three Eurasian oil exporters also have an economic growth profile that is very different than the rest of Eurasia. As in much of Eurasia, these three countries had economies which experienced huge output drops in the 1990s, though it has been followed by economic growth rates far in excess than that experienced by most other transition countries.

Impressive economic growth has been accompanied by generally impressive strides towards macroeconomic stability in most of the transition countries. Inflation rates are single-digit in most transition economies. Only one CEE economy had double-digit inflation in 2005: Serbia-Montenegro (16.2% by EBRD's November 2005 estimate). Seven Eurasian economies had double-digit 2005 inflation rates: Ukraine (14.1%); Russia (12.8%); Moldova (12%); Belarus (10.6%); Turkmenistan (10.5%); Azerbaijan (10.4%); and Uzbekistan (10%). Most of these economies with double-digit inflation rates in 2005 had lower inflation rates in 2004. The three year (2003-2005) average annual inflation rate in the Northern Tier CEE countries was only 3.5%; in the Southern Tier CEE: 5.4%; and in Eurasia, 9.5% (*Table 8*).

With a few exceptions, external debt is manageable if not low (*Table 8*). Where it has been high and particularly burdensome in years past (i.e., among the poorest Eurasian countries), it has been falling, including in Kyrgyz Republic (where debt to GDP in 2004 was highest of all the transition countries, at 95.3%, though down from 132% in 1999), Moldova (74% in 2004 vs. 134% in 2000), and Tajikistan (65% in 2004 vs. 125% in 2000). Where external debt has been relatively high and increasing, it has been among the more advanced CEE countries (notably Estonia, Latvia, Hungary, Slovenia, and Croatia) and one high growth Eurasian country (Kazakhstan).

Virtually all the transition countries have seen very significant increases in the private sector share of GDP since the collapse of communism. All but four countries have private sector shares greater than 50% of GDP. The outliers are Belarus (25%), Turkmenistan (25%), Uzbekistan (45%), and Tajikistan (50%). In contrast, the CEE countries on average have private sectors which constitute roughly 70% of GDP, i.e., within OECD range.

Export shares of GDP are generally much larger in the Northern Tier CEE countries than elsewhere in the transition region: 63% of GDP in 2004 in the Northern Tier CEE vs. 46% in Eurasia, and 36% in the Southern Tier CEE. Outward-orientation has increased in most though not all transition countries (*Table 7*).

Data on the size of the small and medium enterprise sectors (SMEs) are hard to come by and remain incomplete and perhaps very tenuous (*Table 7*). There are data missing for

some countries, and trends over time are available in only a small set of the transition countries. The most recent cross-country data are from the UNECE and are for 2001.¹⁴

Notwithstanding some significant caveats about the data, there are some stark cross-country comparisons apparent. In particular, the SME sectors in the CEE countries (as measured by employment in SMEs as a proportion of total employment) are roughly twice the size of those in Eurasia: on average, 56% in the Northern Tier CEE; 54% in the Southern Tier CEE; and only 27% in Eurasia in 2001. As with export sectors, there is still scope for expansion of the SME sectors in most of the transition countries: SMEs employ 68% of the work force in the EU-15, and 53% in the United States.

Finally, cumulative foreign direct investment per capita continues to be far and away much higher in the Northern Tier CEE countries than elsewhere in the transition region (*Figure 24* and *Table 7*); total cumulative FDI per capita in the Northern Tier CEE is more than three times the amount of what it is in the Southern Tier CEE and closer to six times the volume in Eurasia on average. Moreover, FDI continues to increase at a greater rate in the Northern Tier CEE than in the Southern Tier CEE and Eurasia.

TABLE 7. INDICATORS OF SUSTAINABILITY: ECONOMIC STRUCTURE

	EXPORT SHARE		EXPORT SHARE		SME SHARE OF EMPLOYMENT		SME SHARE OF EMPLOYMENT		FDI CUMULATIVE PER CAPITA		PRIVATE SECTOR SHARE OF GDP	
	(% OF GDP)		(% OF GDP)		(%)		(%)		PER CAPITA		(%)	
	2004		1990		2001		1990-94		1989-05		2005	
CZECH REPUBLIC	72	4.5	45	56.2	4.0	25.0	4,930	5.0	80	5.0		
ESTONIA	78	5.0	60	55.5	4.0	---	4,867	5.0	80	5.0		
HUNGARY	65	4.0	31	49.5	3.5	35.0	3,784	5.0	80	5.0		
SLOVAKIA	77	1.5	27	57.7	4.0	---	2,461	5.0	80	5.0		
POLAND	39	1.5	29	65.4	5.0	19.0	1,480	4.0	75	4.5		
LITHUANIA	54	3.0	52	31.6	2.5	25.0	1,410	4.0	75	4.5		
BULGARIA	58	3.5	33	64.7	4.5	---	1,415	4.0	75	4.5		
ALBANIA	21	0.5	15	75	5.0	---	547	2.0	75	4.5		
ARMENIA	39	1.5	35	25.8	2.0	---	416	2.0	75	4.5		
KYRGYZ REPUBLIC	43	2.0	29	59	4.0	---	129	1.0	75	4.5		
LATVIA	44	2.0	48	69.9	5.0	40.0	1,968	4.5	70	4.0		
ROMANIA	37	1.5	17	20.8	1.5	---	982	3.0	70	4.0		
RUSSIA	35	1.0	18	20	1.5	5.0	90	0.5	65	3.5		
SLOVENIA	77	5.0	91	64.4	4.5	---	1,741	4.5	65	3.5		
KAZAKHSTAN	55	3.0	74	12.9	1.0	12.0	1,605	4.5	65	3.5		
MACEDONIA	40	1.5	26	64.3	4.5	---	633	2.5	65	3.5		
GEORGIA	31	1.0	40	12	1.0	---	495	2.0	65	3.5		
UKRAINE	61	4.0	28	10.8	1.0	4.0	184	1.0	65	3.5		
CROATIA	47	2.5	78	67	5.0	---	2,241	5.0	60	3.0		
AZERBAIJAN	50	2.5	44	2.7	0.5	---	1,329	4.0	60	3.0		
MOLDOVA	51	3.0	48	---	---	---	246	1.5	60	3.0		
SERBIA & MONT	24	0.5	---	32.4	2.5	---	618	2.5	55	2.5		
BOSNIA & HERZ.	26	1.0	---	53	4.0	---	532	2.0	55	2.5		
TAJIKISTAN	46	2.5	28	35.9	3.5	---	80	0.5	50	2.0		
UZBEKISTAN	40	1.5	29	49.7	3.5	---	52	0.5	45	1.5		
TURKMENISTAN	66	4.5	---	60	4.5	---	463	2.0	25	0.5		
BELARUS	68	4.5	46	4.6	0.5	2.0	235	1.5	25	0.5		
CEE & EURASIA	49.8	2.5	40.5	43.1	3.2	18.6	1,294	2.9	64	3.5		
NORTHERN TIER CEE	63.3	3.3	47.9	56.3	4.1	28.8	2,830	4.6	76	4.6		
SOUTHERN TIER CEE	36.1	1.6		53.9	3.9	---	995	3.0	65	3.5		
EURASIA	45.5	2.3	39.0	26.7	2.1	5.8	462	1.9	56	2.6		
ROM & BULG 2002	44.3	2.0		43.5	3.3		519	2.3	70	4.0		
NORTHERN TIER CEE												
AT GRADUATION	53.2	3.0		48.3	3.8		898	2.7	71	4.1		

Shaded columns represent ratings based on a 1 to 5 scale, with 5 representing most advanced.

World Bank, World Development Indicators 2005 (2005), EBRD, Transition Report 2005 (November 2005).

SME data for 2001 are from UNECE, SME Databank (2003); 1990 -94 SME data are from World Bank, Transition: The First Ten Years (2002); and Ayyagari, Beck, and Demircug-Kunt, Small and Medium Enterprises across the Globe: A New Database, World Bank Policy Research Working Paper 3127, (August 2003).

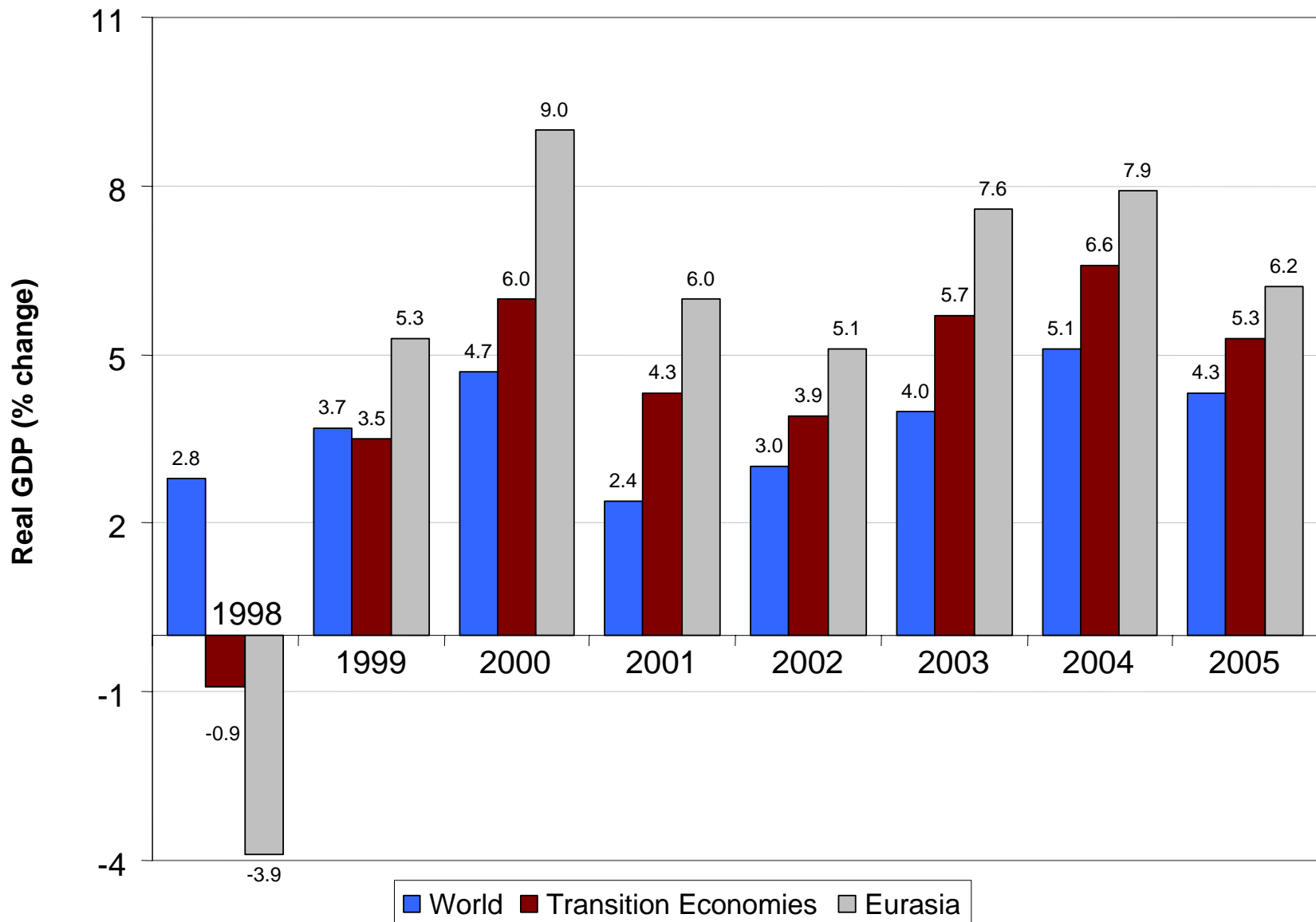
TABLE 8. INDICATORS OF SUSTAINABILITY: MACRO-ECONOMIC PERFORMANCE

	ANNUAL AVERAGE								
	EXTERNAL DEBT		YEARS SINCE GDP BOTTOMED	GROWTH SINCE GDP BOTTOMED (%)	INFLATION 3 YEAR AVERAGE (%)	CONSECUTIVE YEARS INFLATION UNDER 15%		GDP% OF 1989 GDP	
	(% OF GDP)					YEARS SINCE GDP BOTTOMED	YEARS UNDER 15%		
	2004	2005	2005	2003-2005	2005	2005			
POLAND	52.3	3.0	14	4.3	2.1	5.0	9	147	5.0
ALBANIA	22.0	4.5	13	7.1	2.5	5.0	7	144	5.0
SLOVENIA	65.1	2.0	13	3.9	3.9	4.5	11	134	5.0
SLOVAKIA	57.7	2.5	12	4.5	6.1	4.0	12	127	4.5
HUNGARY	70.4	2.0	12	3.7	5.2	4.0	8	126	4.5
TURKMENISTAN	30.1	4.0	8	11.0	9.0	3.5	6	120	4.5
CZECH REPUBLIC	42.3	3.5	13	2.5	1.7	5.0	12	119	4.0
UZBEKISTAN	36.9	3.5	10	3.5	11.2	3.0	3	118	4.0
BELARUS	5.9	5.0	10	6.5	19.0	2.0	1	118	4.0
ESTONIA	89.1	1.0	11	5.6	2.7	5.0	9	112	4.0
KAZAKHSTAN	78.6	1.5	10	6.3	6.7	4.0	8	112	4.0
ARMENIA	33.3	4.0	12	7.7	4.0	4.5	9	106	3.5
ROMANIA	31.2	4.0	13	2.7	16.6	2.5	2	105	3.5
CROATIA	82.1	1.5	12	4.3	2.3	5.0	11	98	3.0
LATVIA	80.0	1.5	11	5.4	5.2	4.0	9	96	3.0
LITHUANIA	47.0	3.0	11	5.5	0.9	5.0	9	95	3.0
AZERBAIJAN	18.6	4.5	10	9.9	6.5	4.0	9	94	3.0
BULGARIA	69.3	2.0	8	4.4	4.2	4.5	7	93	3.0
RUSSIA	33.2	4.0	7	6.5	12.5	3.0	3	89	2.5
KYRGYZ REPUBLIC	95.3	0.5	10	5.2	4.0	4.5	5	83	2.5
MACEDONIA	44.8	3.5	10	1.9	0.3	5.0	10	82	2.5
TAJIKISTAN	39.7	3.5	9	7.5	10.4	3.0	2	75	2.0
BOSNIA & HERZEGOVINA	31.1	4.0	11	18.0	-0.4	5.0	7	63	1.5
UKRAINE	31.1	4.0	6	8.1	9.4	3.5	5	61	1.5
SERBIA & MONTENEGRO	62.4	2.5	12	3.3	12.3	3.0	0	58	1.0
GEORGIA	39.3	3.5	11	6.1	6.7	4.0	6	48	0.5
MOLDOVA	74.2	2.0	7	5.7	12.0	3.0	5	46	0.5
CEE & EURASIA	50	3.0	11	6.0	6.6	4.0	6.9	99	3.1
NORTHERN TIER CEE	63	2.3	12	4.4	3.5	4.6	9.9	120	4.1
SOUTHERN TIER CEE	49	3.1	11	6.0	5.4	4.3	6.3	92	2.8
EURASIA	40	3.3	9	7.1	9.5	3.5	5.2	89	2.7
ROM & BULG 2002	52	3.0			12.3	3.3		83	2.5
NORTH. TIER CEE AT GRADUATION	45	3.3			67.8	2.0		90	2.8

Shaded columns represent ratings based on a 1 to 5 scale, with 5 representing most advanced. EBRD, *Transition Report 2005* (November 2005).

Economic Growth Trends Worldwide

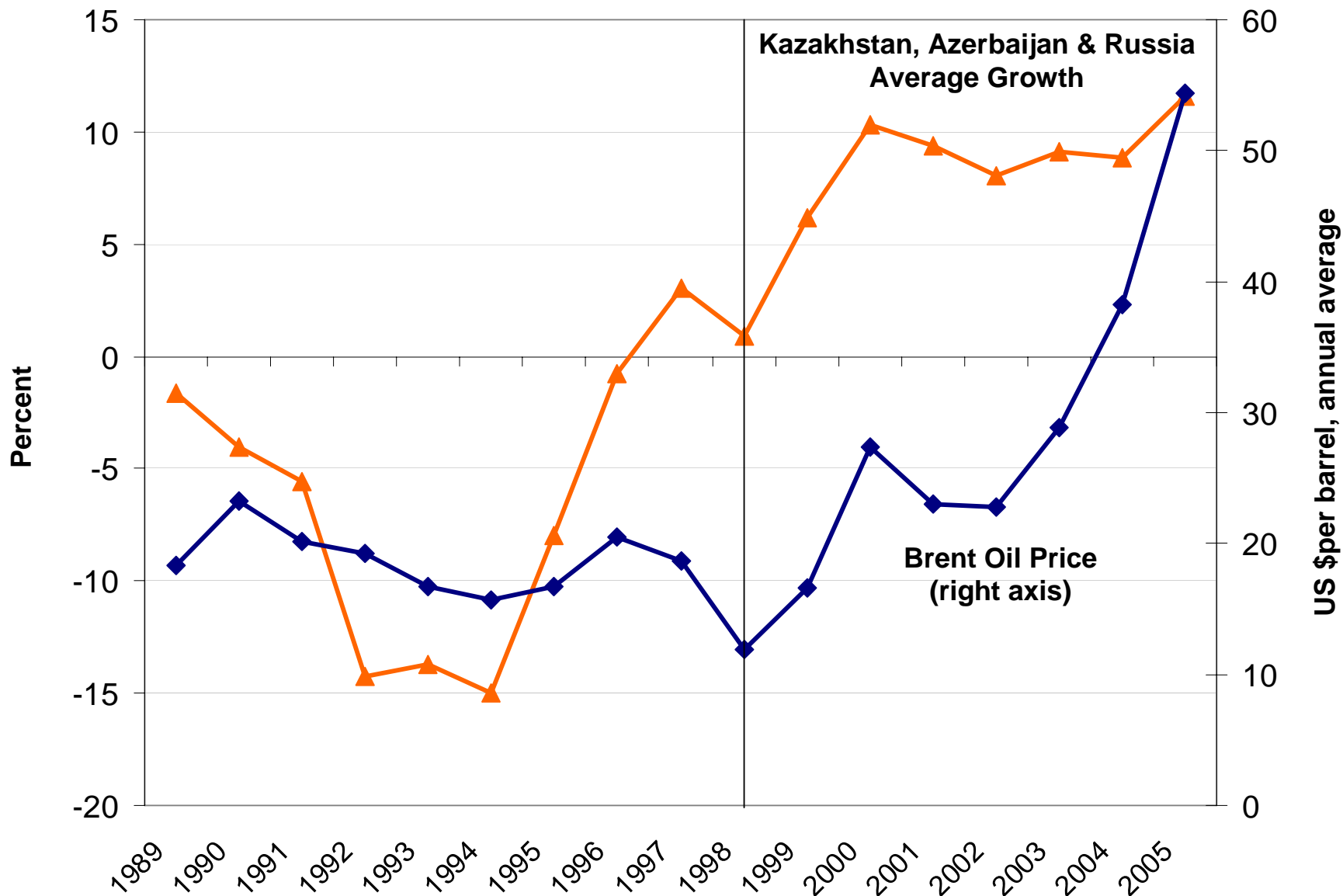
Figure 19



EBRD, *Transition Report 2005* (October 2005); and IMF, *World Economic Outlook* (September 2005).

Oil Prices and Growth in Eurasia

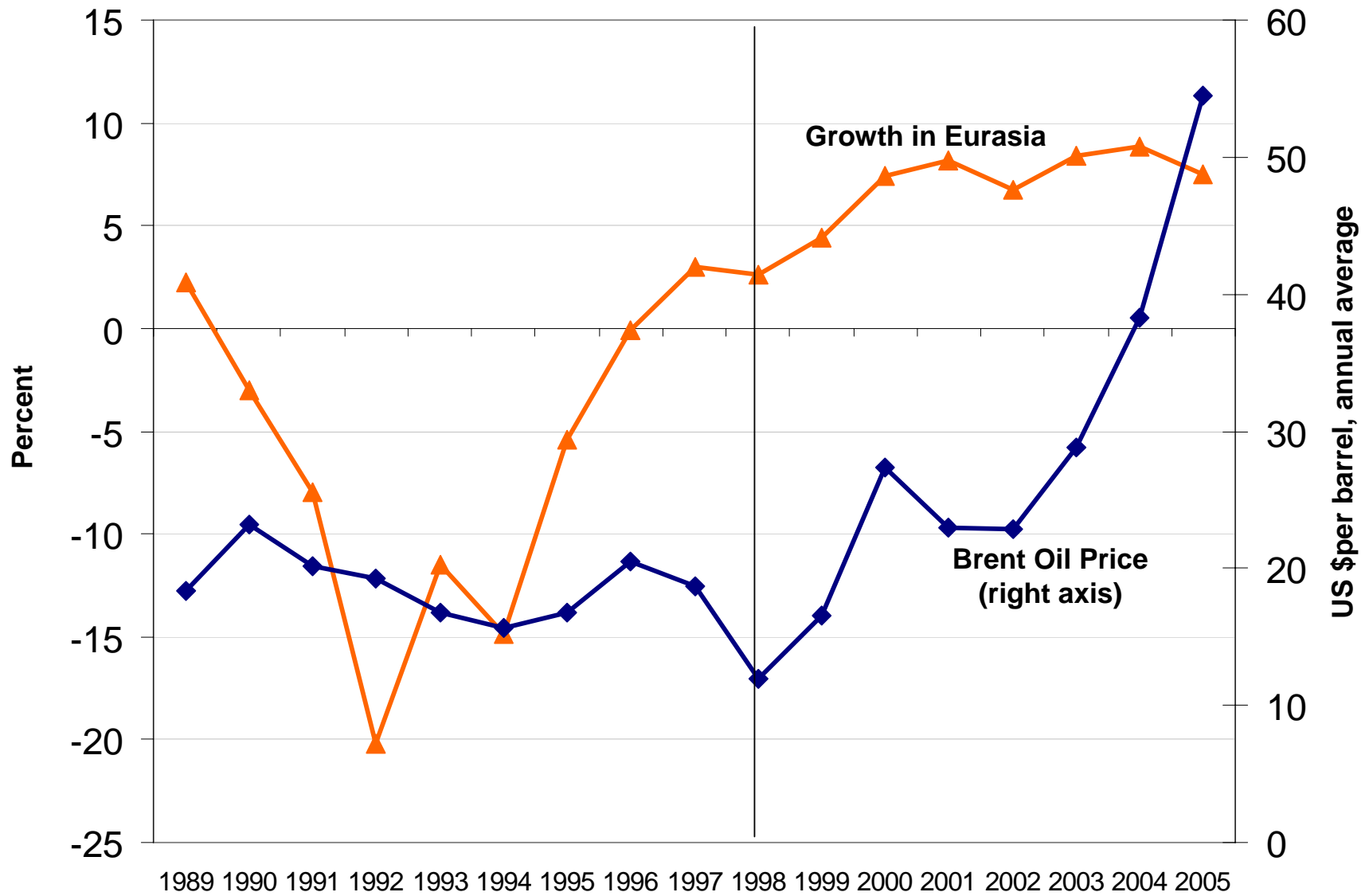
Figure 20



EBRD, *Transition Report 2005* (November 2005); and World Bank, *Commodity Price Data, Pink Sheet* (January 2006).

Oil Prices and Growth in Eurasia

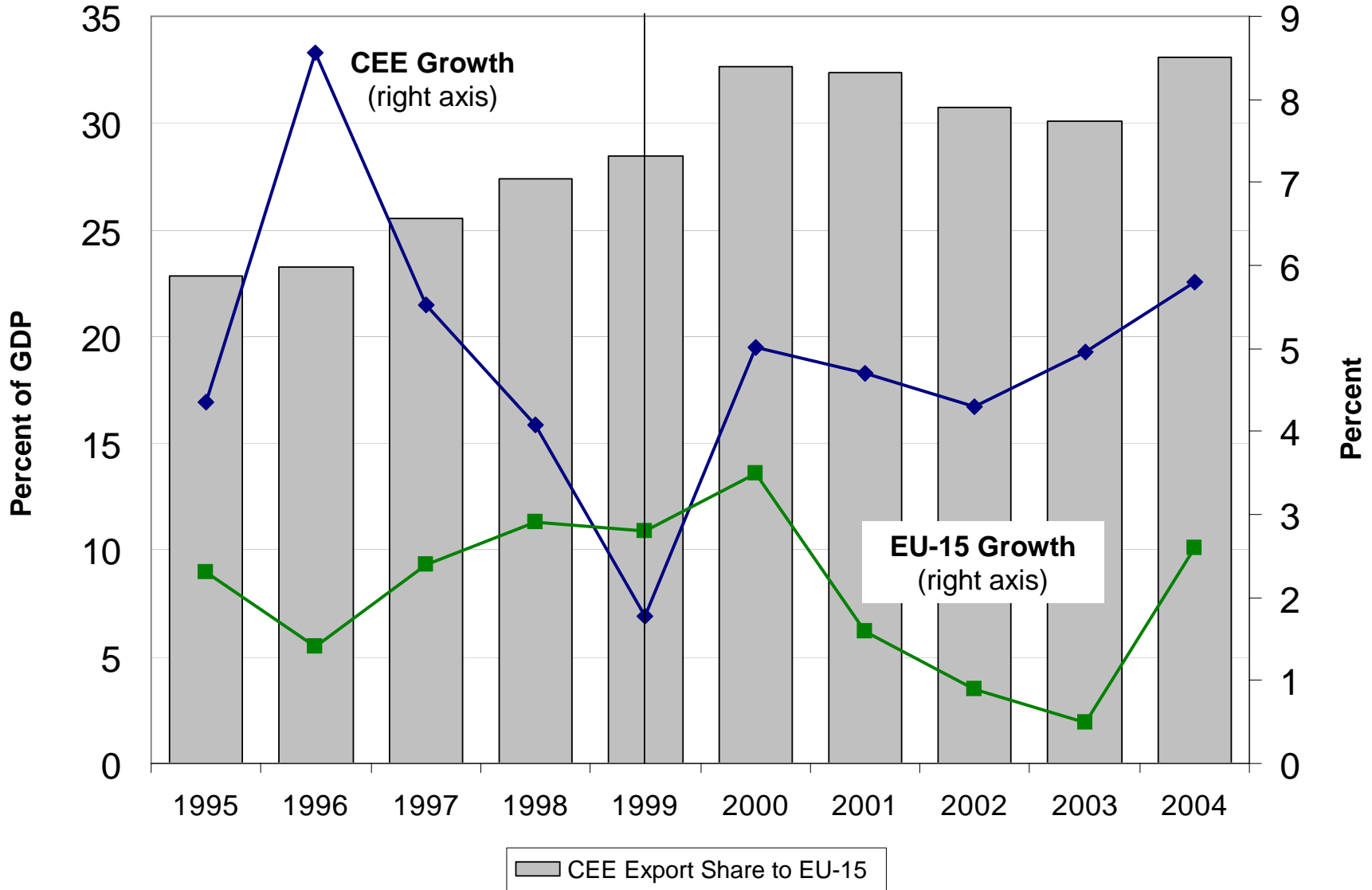
Figure 21



EBRD, *Transition Report 2005* (November 2005); and World Bank, *Commodity Price Data, Pink Sheet* (January 2006).

Figure 22

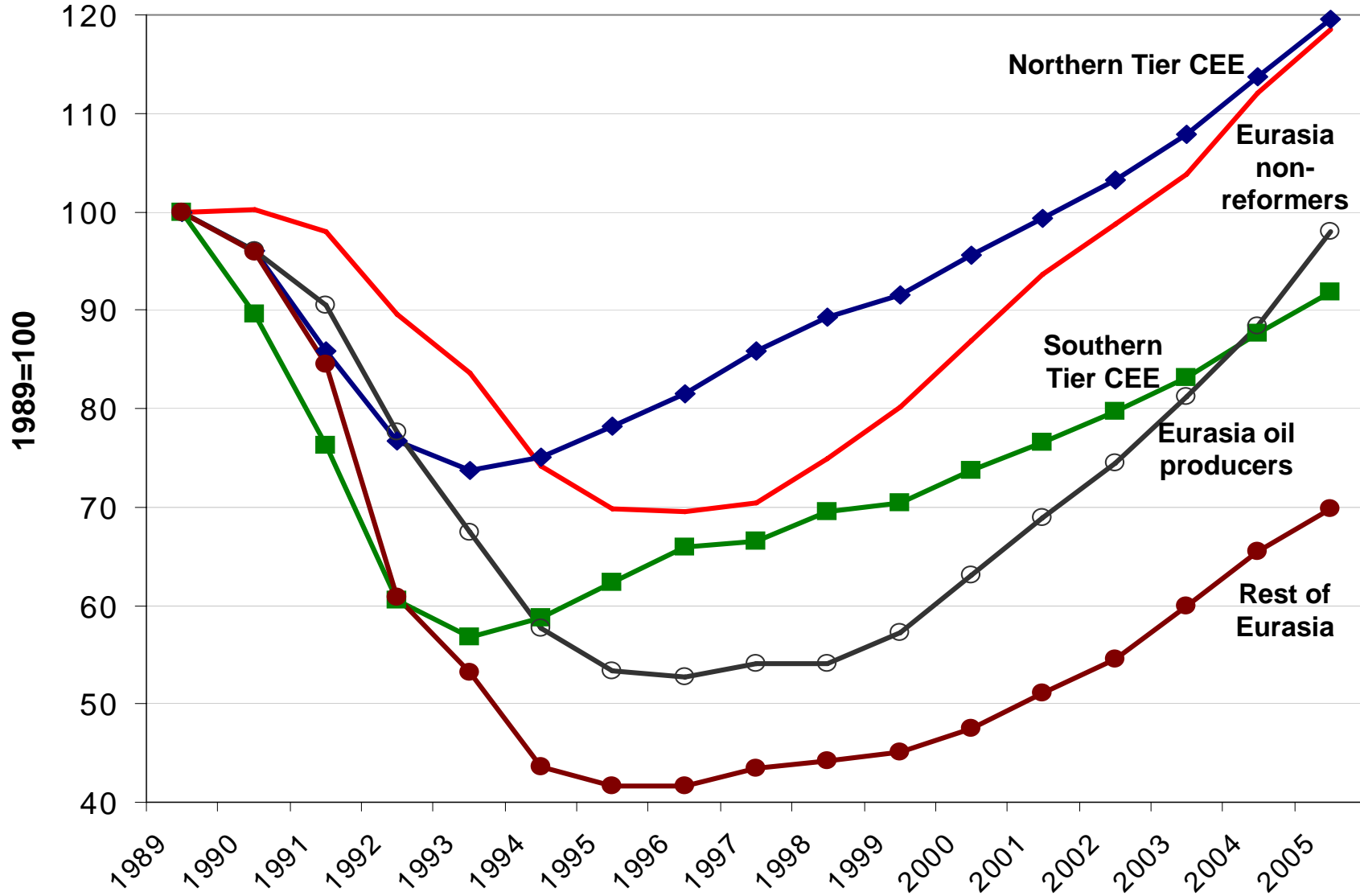
Trade and Growth in Central and Eastern Europe & EU-15



EBRD, *Transition Report 2005* (November 2005); World Bank, *World Development Indicators 2005* (2005); and IMF, *Direction of Trade Database* (January 2006).

GDP as % 1989 GDP

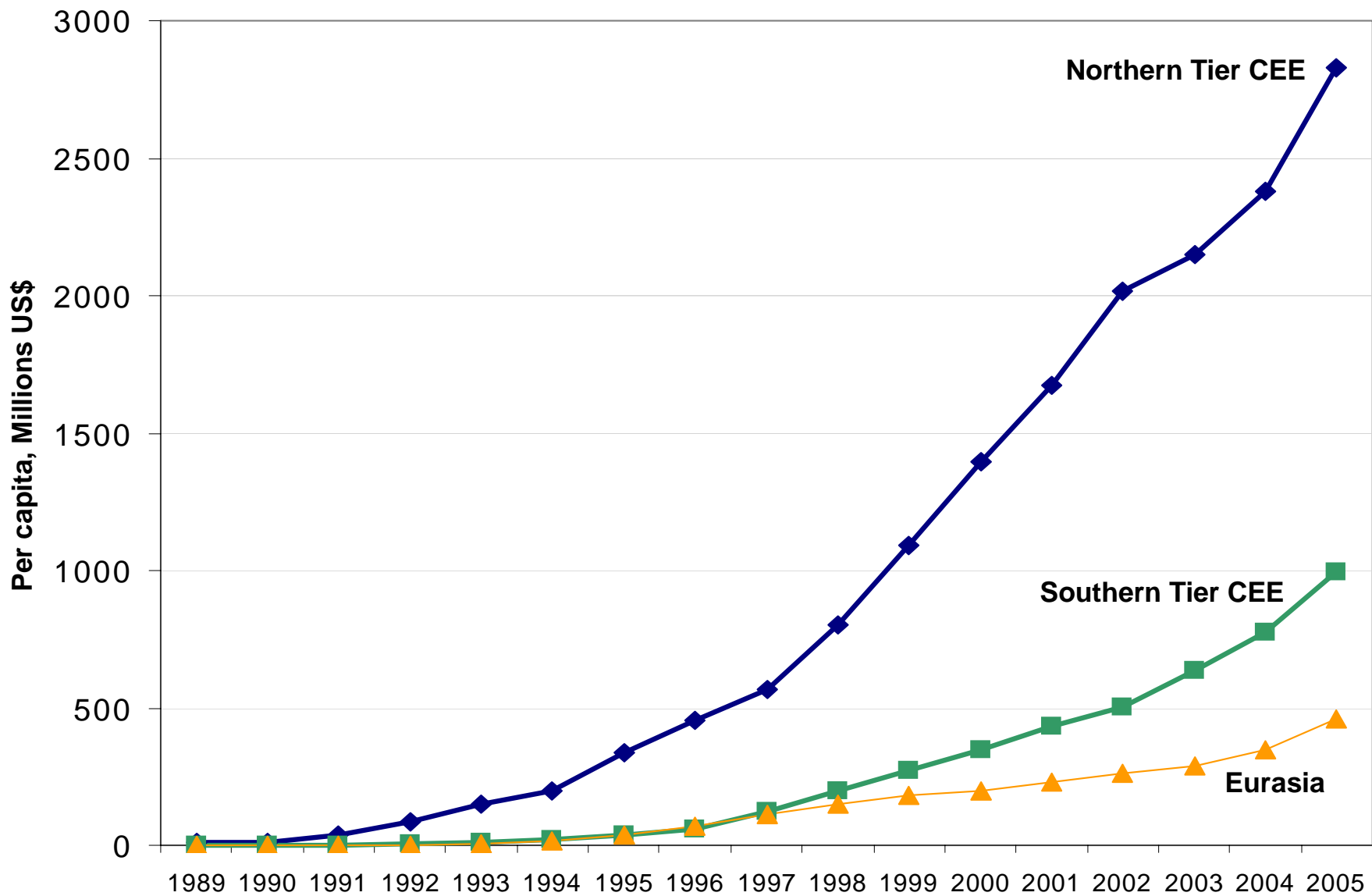
Figure 23



EBRD, *Transition Report 2005* (November 2005). Eurasia non-reformer include Uzbekistan, Belarus & Turkmenistan and Eurasia oil producers include Russia, Kazakhstan and Azerbaijan.

Cumulative FDI per capita, 1989-2005

Figure 24



EBRD, *Transition Report 2005* (November 2005).