Emerging Europe: Oil Prices Offer Respite For Russia; Turkey Calls Early Elections

KEY TAKEAWAY

The review period turned out to be a mixed bag for Russia's economy. While the steady rise in oil prices came as a saving grace for the economy, fresh sanctions imposed in April by the United States were an unexpected shock, clouding the business environment further.

Russia: In addition to structural factors such as a declining population, an unhealthy dependence on the oil and natural gas sector and low investment levels, continuing financial sanctions also bog down the economy.

During the review period, the steady rise in oil prices came as a saving grace for Russia, the largest of the economies under our purview in the emerging Europe region. Yet, structural factors such as a declining population and low investments as well as the continuing financial sanctions cloud the economy's long-term prospects. In Turkey, the surprise call for early elections turned the spotlight on the problems faced by the economy such as slowing growth, soaring inflation and depreciation of its currency lira.

Poland, the largest among the former Soviet satellite states, looks set to sustain its GDP growth rate this year as well after expanding 4.6% in 2017. The political stalemate in the Czech Republic showed no signs of abating as the Prime Minister-in-waiting Andrej Babis is yet to muster the numbers required to form the government. The re-election of Viktor Orban as prime minister ensured policy continuity in Hungary. The largely export-oriented economy is banking on the boom in corporate and household lending to steer economic growth. Greece, which is slowly returning to normalcy, got a shot in the arm as the European Bank for Reconstruction and Development is likely to extend its mandate in the country for five more years.

RUSSIA: OIL PRICES OFFER RESPITE AMID FRESH SANCTIONS

The review period turned out to be a mixed bag for Russia's economy. While the steady rise in oil prices came as a saving grace for the economy, fresh sanctions imposed in April by the United States were an unexpected shock, clouding the business environment further. The impact of sanctions that targeted some Russian individuals and firms was immediately evident in the stock market rout and the plunge in the ruble. What's more, it could likely derail the Russian central bank's plans to reduce interest rates to boost economic growth. Analysts had expected the central bank to trim rates to 7% at its meeting scheduled for June 2018. The sole consolation though is that inflation is expected to remain at 3.4% through the year, below the central bank's target rate of 4%.

Russia's economy, which was reeling under the impact of Western sanctions and lower oil prices, had bounced back in 2017, clocking a growth rate of 1.5%. Looking ahead, Russia appears to have pinned its hopes on the football World Cup to be held in the country in June-July this year to spur economic growth. Deputy Prime Minister Arkady Dvorkovich said the preparations for the World Cup had contributed about 1% to economic growth in the last five years and would continue to add to GDP growth in the short term, according to a *Reuters* news report.

Meanwhile, Vladimir Putin's re-election as president for the fourth term has turned the spotlight back on economic issues that confront the economy. In addition to structural factors such as a declining population, an unhealthy dependence on the oil and natural gas sector and low investment levels, continuing financial sanctions also bog down the economy. Furthermore, the Putin administration is left with little room to launch fiscal stimulus measures to prop up the economy.

TURKEY: ECONOMY IN FOCUS AS ERDOGAN CALLS EARLY ELECTIONS

By many measures, Turkey's economy is in good health. Tourism, an important sector that brings in sizable revenues, is on the road to recovery, the banking sector is doing reasonably well, the country's debt to GDP ratio remains low and above all, last year's growth momentum still lingers. **Still, Deputy Prime Minister Mehmet Simsek acknowledged that current-account deficit and inflation remain the biggest challenges faced by the economy.**

President Tayyip Erdogan called snap elections for June 24, advancing the polls originally scheduled for November 2019. Mr. Erdogan said economic challenges and the ongoing war in neighboring Syria demand a powerful executive presidency that would get approval with the fresh vote, according to a *Reuters* news report. While early elections raised concerns of increasing authoritarianism as it would make Mr. Erdogan more powerful, analysts pointed out that slowing growth – Turkey is expected to expand 4.1% in 2018, below the government's estimate of 5.5% -- would have prompted the president to declare early elections, not to mention the continued depreciation of the lira.

Rating agency Standard & Poor's cut Turkey's credit rating to "junk", citing a bleak inflation outlook and the long-term depreciation and volatility of the nation's exchange rate, a Bloomberg news report said. S&P warned of a hard landing for the credit-fueled, overheated economy, taking special note of its widening current-account deficit and soaring inflation.

KEY TAKEAWAY

Turkey: Rating agency Standard & Poor's cut Turkey's credit rating to "junk", citing a bleak inflation outlook and the long-term depreciation and volatility of the nation's exchange rate. S&P warned of a hard landing for the credit-fueled, overheated economy.

Poland: Observing that Poland's credit profile reflects robust economic growth, Moody's raised its 2018 GDP growth forecast to 4.3% from its earlier view of a 3.5% growth. For 2019, it expects the Polish economy to clock 4.0% growth, revised from its previous forecast of 3.2%.

POLAND: ECONOMY EXPECTED TO SUSTAIN GROWTH IN 2018

Poland appears to be in growth mode, following up on its respectable 4.6% GDP expansion in 2017, rating agency Moody's reported in an assessment of the economy. Moody's said Poland's GDP growth will likely maintain its solid pace in 2018. Observing that Poland's credit profile reflects robust economic growth, the agency raised its 2018 GDP growth forecast to 4.3% from its earlier view of a 3.5% growth. For 2019, it expects the Polish economy to clock 4.0% growth, revised from its previous forecast of 3.2%. However, Moody's said uncertainty regarding government policy remains a concern.

The rise of nationalist governments in central and eastern Europe has raised concerns in the European Union over some of their authoritarian policies. *Reuters* reports that judicial reforms being implemented by the government under the leadership of Prime Minister Mateusz Morawiecki has been a sore point with the European Commission as it holds that the proposed changes undermine the rule of law.

The confrontation had escalated to a level where the EC even sought to suspend Poland's voting rights in the European Union. Recently, Poland agreed to amend some of the provisions to comply with the requirements of the European Commission.

CZECH REPUBLIC: POLITICS STILL IN FOCUS

The political stalemate in the country showed no signs of abating as billionaire Andrej Babis struggles to form the government. Mr. Babis has been functioning as the caretaker prime minister for about five months now. At the crux of the issue are the conditions set by Babis' potential partner, the Social Democrats, to support him as prime minister. Though Mr. Babis won on the back of his anti-immigrant rhetoric and defiance of the European Union, he has been trying to build bridges with Western governments by projecting himself as a pro-European leader.

Czech Republic's economy expanded at an annual 5.1% in the last quarter of 2017, the latest quarter for which data are available. The export-oriented economy had registered a 5% growth in the previous quarter. Since the beginning of 2017, Czech GDP has steadily accelerated.

HUNGARY: BANKING ON LENDING BOOM TO PROPEL GROWTH

Hungary witnessed an unprecedented boom in consumer lending in recent quarters, thanks to a double-digit increase in wages and low interest rates. Central Bank Deputy Governor Marton Nagy said the economy needs even faster growth in lending to sustain its expansion, according to a Reuters news report. Mr. Nagy said while corporate lending should grow at an annual 10-15%, household lending can increase at an even faster rate. On its part, the central bank has kept the base interest rate at a record low of 0.9% until 2020. Mr. Nagy added that growth in both corporate and household lending would propel the economy to expand above 4% in the years ahead.

The re-election of Prime Minister Viktor Orban and his Fidesz party in the April elections sets the stage for Mr. Orban to pursue his anti-immigrant and anti-EU policies unhindered. Mr. Orban's victory points to the increasing popularity of nationalist sentiments in European Union member states.

GREECE: ON THE RIGHT TRACK

Greece is expected to exit its third bailout program in August 2018. **Moreover, the beleaguered south European economy, which is slowly returning to normality, got a shot in the arm as the European Bank for Reconstruction and Development (EBRD) is considering extending its tenure in the country by five more years.** The bank, originally constituted to help the former communist-ruled east European nations in their transition to market economies, has pumped in about $2 billion-worth of investments in Greece over the last two and a half years. The EBRD's work in Greece includes recapitalization of the country's four big banks, funding the upgrade of 14 regional airports and financing renewable energy projects, *Reuters* said in a news report.

Bringing more cheer, Greece exceeded its bailout targets in 2017, the European Commission confirmed. The debt-laden country achieved a budget surplus equivalent to 4.2% of its GDP in 2017, surpassing the 1.75% target set by its lenders, *Bloomberg* reported.

KEY TAKEAWAY

Czech Republic: The economy expanded at an annual 5.1% in the last quarter of 2017, the latest quarter for which data are available. The export-oriented economy had registered a 5% growth in the previous quarter. Since the beginning of 2017, Czech GDP has steadily accelerated.

Hungary: Hungary witnessed an unprecedented boom in consumer lending in recent quarters, thanks to a double-digit increase in wages and low interest rates. Central Bank Deputy Governor Marton Nagy said the economy needs even faster growth in lending to sustain its expansion.