Economic Analysis Division

Emerging Markets Analysis

Bi-Weekly Report

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NBG - Economic Analysis Division
https://www.nbg.gr/en/the-group/press-office/e-spot/reports

Emerging Markets Analysis

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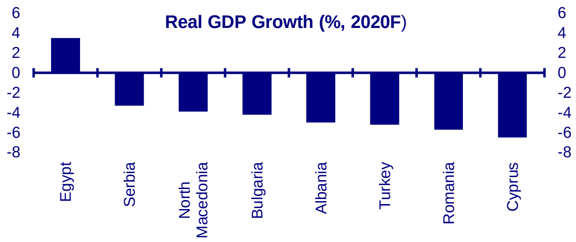
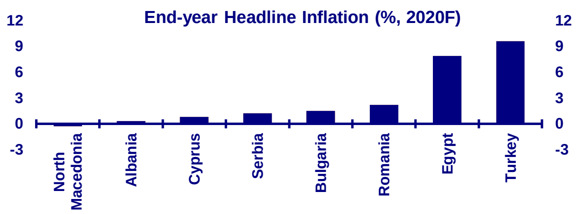
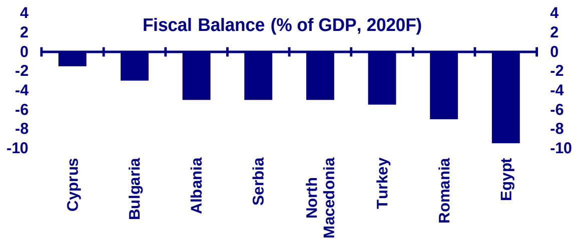
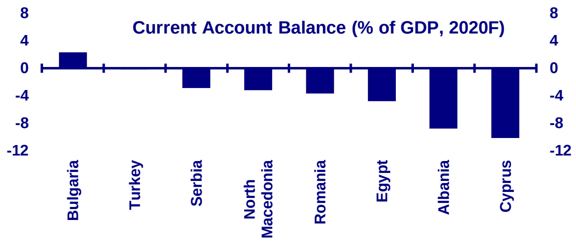








Sources: National authorities, IMF & NBG estimates

Economic activity strengthened in H2:19, due to one-offs, bringing FY:19 GDP growth to a robust 4.2%

GDP is expected to contract this year by 3.3%, due to COVID-19 related disruptions in the supply chain and the sharp slowdown in external demand, especially from the EU

GDP continued to expand at a solid pace in Q4:19 (up 3.4% y-o-y), driven by investment

GDP is set to drop abruptly in the aftermath of the COVID-19 outbreak, with increased uncertainty, quarantine measures and lower remittances from migrants taking their toll on economic activity along with the contraction in external demand

IMF lends EUR 176.5mn to North Macedonia to ease COVID-19 blow

The EU opens accession negotiations with Albania

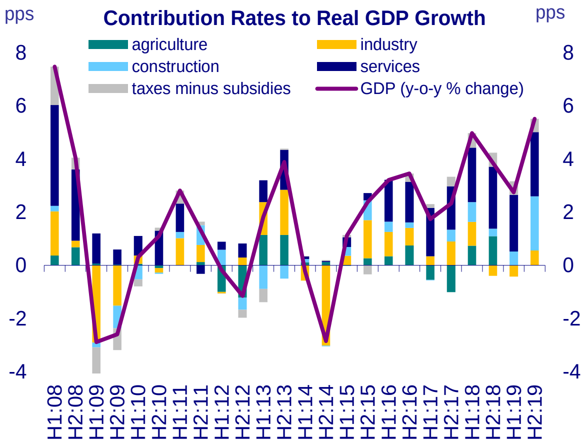
GDP growth eased to 2.2% in FY:19 from a post-GFC high of 4.1% in FY:18, due to base effects

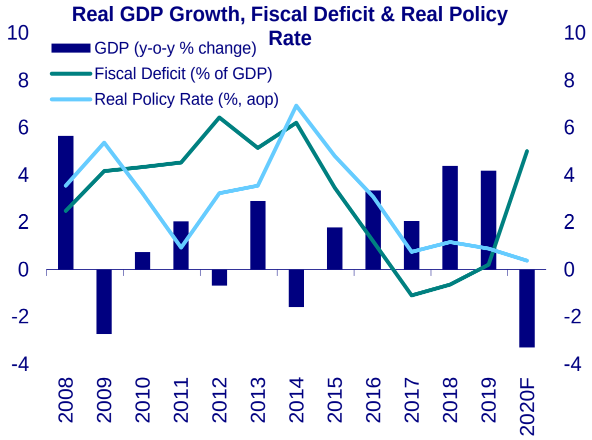
A significant contraction in GDP in FY:20 is unavoidable, with deteriorating economic sentiment weighing on business activity and external demand falling sharply (50% of Albania's exports is channeled to Italy)

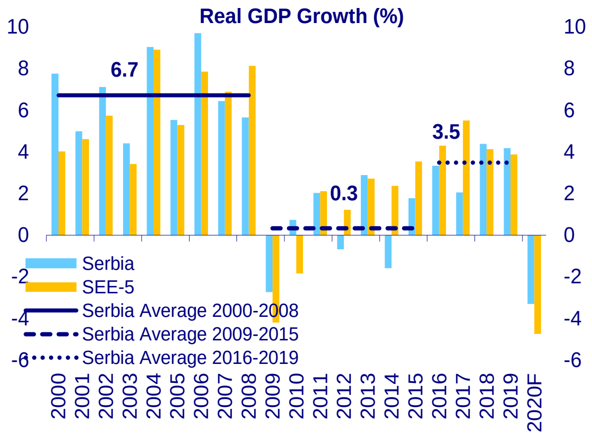
IMF approves EUR 173.7mn in financial support to Albania

Serbia

BB+ / Ba3 / BB+ (S&P / Moody's / Fitch)







	13 Apr.	3-M F	6-M F	12-M F
1-m BELIBOR (%)	0.9	0.9	1.0	1.1
RSD/EUR	117.6	117.8	118.0	117.7
Sov. Spread (2029, bps)	169	165	160	150

	13 Apr.	1-W %	YTD %	2-Y %
BELEX-15	693	4.3	-13.6	-6.3

	2017	2018	2019F	2020F	2021F
Real GDP Growth (%)	2.0	4.4	4.2	-3.3	6.4
Inflation (eop, %)	3.0	2.0	1.9	1.2	2.0
Cur. Acct. Bal. (% GDP)	-5.2	-4.8	-6.9	-6.4	-7.3
Fiscal Bal. (% GDP)	1.1	0.6	-0.2	-5.0	-3.5

Sources: Reuters, OPBC & NBG estimates

Economic activity strengthened in H2:19, due to one-offs, bringing FY:19 GDP growth to a robust 4.2%. GDP growth rebounded to 5.5% y-o-y in H2:19 from 2.8% in H1:19, largely supported by the construction of the TurkStream gas pipeline. Indeed, the contribution of the construction sector to overall growth rose sharply in H2:19 (to a sizeable 2.0 pps from just 0.5 pps in H1:19).

Industrial output also increased strongly in H2:19 (adding 0.6 pps to overall growth against a negative contribution of 0.4 pps in H1:19), due to a positive base effect from the interruption in production in the Pancevo oil refinery and Petrohemija chemical plant, following factory maintenance in H1:19.

Importantly, adjusting for the construction and industrial sectors, GDP growth accelerated to 4.0% y-o-y in H2:19 from 3.6% in H1:19, supported by the services sectors (adding 2.4 pps to overall growth in H2:19 following 2.1 pps in H1:19). This improvement was attributed to: i) a looser fiscal stance; and ii) strong private consumption, on the back of a generous income policy (including a 5-25% rise in pensions and a 9.0% hike in public sector wages) and its spill-over to the private sector amid a tighter labour market.

All said, boosted by the impressive H2:19 performance, FY:19 GDP growth reached a robust 4.2% -- only slightly below a post-global crisis high of 4.4% in FY:18 but still well above its long-term potential (of c. 3.5%) -- recording the highest growth rate in SEE-5. It is important to note that FY:19 economic growth would have been even stronger had external demand not been hit by: i) the economic slowdown in the EU, Serbia's main trade partner (absorbing ⅔ of the country's exports); and ii) the imposition by Kosovo of a 100% tariff on imports from Serbia in Q4:18, effectively halting trade with Kosovo (the latter accounts for 3.0% of Serbia's exports, mainly food).

GDP is expected to contract this year by 2.1%, due to the impact of the COVID-19 outbreak. Serbia's economy is expected to slip into recession this year -- for the first time since the flood-induced contraction in 2014 -- in line with:

i) weaker net exports, on the back of COVID-19 related disruptions in supply chains and the sharp slowdown in external demand, especially from the EU -- Serbia's main trading and investing partner;

ii) a drop in private consumption, due the imposed lockdown as well as lower remittances; and

iii) the halt in investment spending, amid a sharp deterioration in business confidence

The impact of the COVID-19 outbreak on economic activity should be only partly mitigated by the adopted monetary and fiscal stimulus measures. Specifically, the Government announced a package of measures worth EUR 2.8bn (6.1.% of GDP), including tax relief, wage subsidies, a one-off payment of EUR 100 to adult citizens, and loan subsidies, as well as an increase in state guarantees worth EUR 2.3bn (5.0% of GDP).

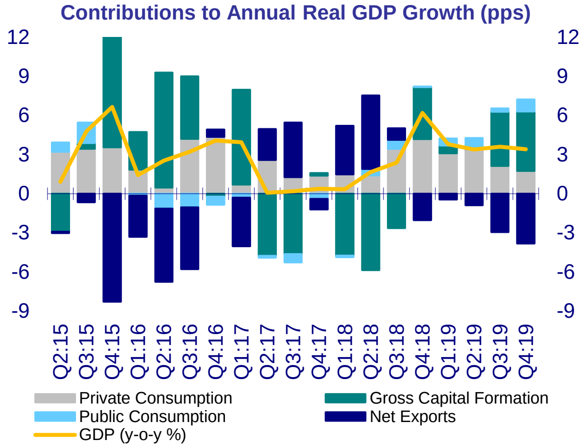
At the same time, the NBS cut its policy rate by 75 bps to an all-time low of 1.50%, providing, at the same time, increased liquidity to the market through repo purchases of securities and FX swap auctions. Moreover, it introduced a 90-day moratorium on loan repayments.

All said, assuming that the COVID-19 pandemic fades in H2:20, we see GDP contracting by 3.3% this year against an expansion of 4.2% in FY:19. Note that Parliamentary elections, initially scheduled for April 26th, have been postponed. According to the latest polls, the ruling SNS party is set to retain an absolute majority.

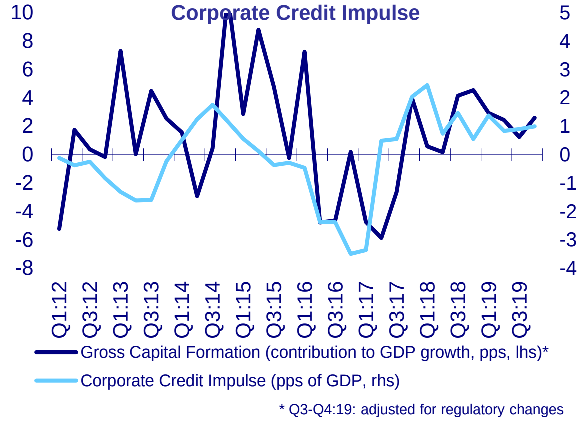
North Macedonia

BB- / NR / BB+ (S&P / Moody's / Fitch)

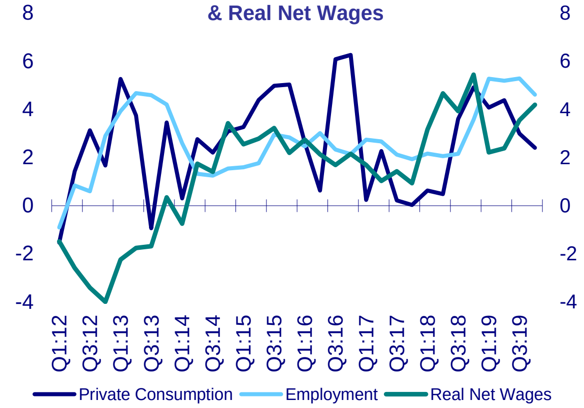
Contributions to Annual Real GDP Growth (pps)



Gross Capital Formation & Corporate Credit Impulse



Private Consumption, Employment & Real Net Wages



	13 Apr.	3-M F	6-M F	12-M F
1-m SKIBOR (%)	1.2	1.2	1.2	1.4
MKD/EUR	61.3	61.3	61.3	61.3
Sov. Spread (2025, bps)	200	193	185	170

	13 Apr.	1-W %	YTD %	2-Y %
MBI 10	4,018	3.3	-13.6	9.4

	2017	2018	2019F	2020F	2021F
Real GDP Growth (%)	1.1	2.7	3.6	-3.9	6.0
Inflation (eop. %)	2.4	0.9	0.5	-0.3	1.0
Cur. Acct. Bal. (% GDP)	-1.0	-0.1	-2.8	-3.2	-3.8
Fiscal Bal. (% GDP)	-2.7	-1.8	-2.0	-5.0	-3.4

Sources: Reuters, State Statistical Office & NBG estimates

GDP continued to expand at a solid pace in Q4:19 (up 3.4% y-o-y), driven by investment. The annual pace of economic expansion eased slightly to 3.4% y-o-y in Q4:19 from 3.6% in Q3:19, bringing the FY:19 figure to a 4-year high of 3.6% from 2.7% in FY:18.

Gross Capital Formation (GFC) continued to drive economic growth in Q4:19 (adding 4.6 pps to GDP against 4.2 pps in Q3:19), supported by the expansion in corporate lending (adjusted for regulatory changes, up c. 8.0% in real *ex-post* terms at end-2019 against a rise of 6.1% at end-2019), in an environment of low interest rates. At the same time, private consumption expanded at a slower, albeit still solid pace (adding 1.8 pps to overall growth against 2.1 pps in Q3:19). Note that private consumption fundamentals remain strong, as suggested by robust employment and real growth (up 2.0% and 4.2%y-o-y, respectively, in Q4:19 following increases of 2.3% and 3.6% in Q3:19). The moderation in private consumption was more than offset by the pick-up in public consumption (adding 0.9 pps to overall growth against 0.3 pps in Q3:19), on the back of a looser fiscal stance.

Unsurprisingly, net exports remained a drag on overall growth in Q4:19 (subtracting 3.8 pps following 2.9 pps in Q3:19), in line with weaker external demand from the EU (absorbing 80% of the country's exports) on the one hand, and robust domestic demand on the other.

GDP is set to drop abruptly in the aftermath of the COVID-19 outbreak. Indeed, private consumption is set to slow, reflecting the impact of quarantine measures, lower remittances from migrants (amounting to a sizeable 15.5% of GDP in FY:19) and weakening economic sentiment. The latter is also set to weigh on GCF, which is expected to slow, despite favourable financing conditions and the extension of a state incentive scheme to support investment. At the same time, COVID-19-related disruptions in global supply chains and subdued external demand should weigh on net exports. Note that c. 50% of the country's exports (equivalent to 26.4% of GDP) is channeled to Germany, whose economic growth has fallen sharply this year (down by c. 6.0%).

The Government has, so far, announced measures worth c. 1.2% of GDP to counter the impact of the COVID-19. These include, *inter alia*, wage and social security contribution subsidies and the postponement of CIT payments for affected industries. The latter will also benefit from financial assistance from the state-owned Development Bank worth 0.5% of GDP. Overall, we see the budget deficit widening to c. 5.0% of GDP in FY:20 from 2.0% in FY:19. Part of the increased financing needs will be covered by a special EU grant and a World Bank loan (amounting to 0.5% and 0.7% of GDP, respectively).

The Central Bank (NBRNM) responded with a further reduction in its key rate (down 25 bps to a record low of 1.75%, implying a real *ex-post* rate of 1.3%) and a series of financial measures (including revising its credit risk regulations to encourage banks to restructure loans temporarily and relaxing the loan classification standards for NPLs).

Moreover, in a bid to boost FX reserves and safeguard financial stability, the authorities turned to the IMF, which approved a 1.6% of GDP disbursement under its Rapid Financing Instrument (RFI), which does not imply the need for a fully-fledged programme or reviews.

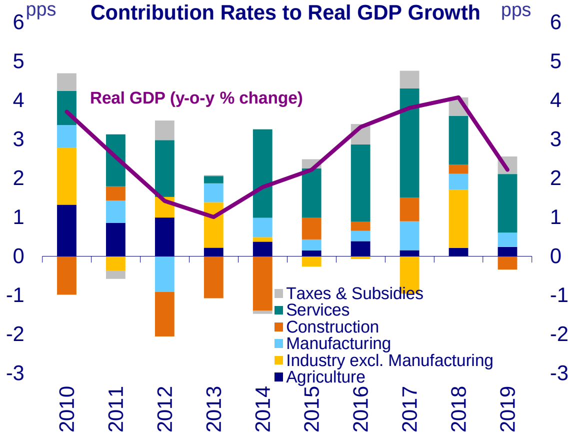
All said, assuming the COVID-19 pandemic fades by end-Q2:20, we see GDP growth declining by 3.9% in FY:20 against a rise of 3.6% in FY:19. Risks to our forecasts are tilted to the downside, reflecting a deeper-than-envisaged slowdown in external demand and/or the imposition of a prolonged domestic lockdown, following the escalation of the COVID-19 pandemic. Note that the (snap) Parliamentary elections, scheduled for April 12th, were postponed. .

Albania

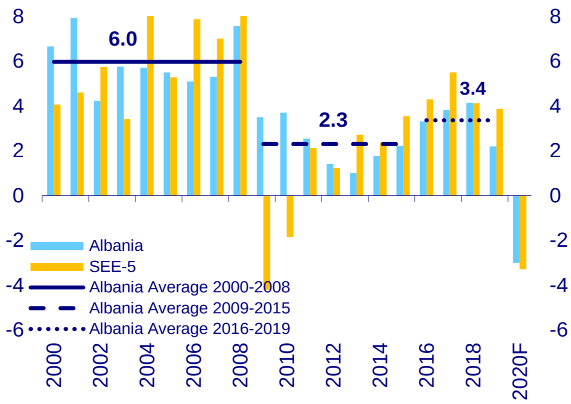
B+ / B1 / NR (S&P / Moody's / Fitch)

Key Dates in Albania's Path towards EU Membership	
Mar. 2020	European Council (EUCO) approves conditional launch of EU membership talks
Mar. 2020	European Commission (EC) repeats its firm recommendation for the opening of membership talks
Oct. 2019	EUCO defers the decision on launching EU membership talks with Albania to May 2020
Jun. 2019	EUCO postpones the launch of EU membership talks with Albania until October 2019
May 2019	EC repeats its unconditional recommendation for the opening of membership talks
Jun. 2018	EUCO postpones a decision to grant a starting date for EU membership talks until June 2019
Apr. 2018	EC recommends the opening of membership talks
Jun. 2014	EUCO grants Albania the status of candidate country for EU membership
June 2006	Signing of the SAA

Contribution Rates to Real GDP Growth



Real GDP Growth (%)



	13 Apr.	3-M F	6-M F	12-M F
1-m TRIBOR (mid, %)	0.7	0.6	0.6	0.6
ALL/EUR	126.3	127.2	128.0	127,0
Sov. Spread (2025, bps)	240	233	225	210

	13 Apr..	1-W %	YTD %	2-Y %
Stock Market	- - -	- - -	- - -	- - -

	2017	2018	2019	2020F	2021F
Real GDP Growth (%)	3.8	4.1	2.2	-5.0	7.0
Inflation (eop. %)	1.8	1.8	1.1	0.3	1.2
Cur. Acct. Bal. (% GDP)	-7.5	-6.7	-7.6	-8.8	-8.3
Fiscal Bal. (% GDP)	-2.0	-1.6	-1.9	-5.0	-3.8

Sources: Reuters, EC, INSTAT & NBG estimates

The EU opens accession negotiations with Albania. At end-March, the European Council (EUCO) approved the conditional launch of EU membership talks with Albania, a candidate country since mid-2014. The EUCO's decision ends 2 years of delays, as the European Commission had already recommended the opening of talks, based on the country's progress in reforming the judicial and public administration and the fight against corruption.

According to the decision, accession negotiations will begin as soon as Albania ensures: i) the adoption of the electoral reform; ii) the continued implementation of the judicial reform, especially the smooth functioning of the Constitutional Court; and iii) the establishment of anti-corruption institutions and organised crime specialised structures.

Based on past experience, negotiations could last 6-7 years, during which Albania must implement wide-range political and economic reforms in order to align with the 35 Chapters of the *Acquis Communautaire*. The ratification by all member states could take a further 2 years, implying that Albania will not join the EU before 2029. Importantly, the launch of accession talks will strengthen the reform momentum and provide a solid policy anchor.

GDP growth eased to 2.2% in FY:19 from a post-GFC high of 4.1% in FY:18, due to base effects. Indeed, the industrial sector's contribution to overall growth diminished in FY:19 (to 0.4 pps from a sizeable 1.9 pps in FY:18), due to the normalization in electricity production (fully based on hydroelectric production), following a sharp rise in FY:18, on the back of favourable weather conditions. Construction was also a drag on GDP growth in FY:19 (subtracting 0.3 pps against a positive contribution of 0.2 pps in FY:18), reflecting the halt in related activity following the devastating earthquake that hit Albania in mid-Q4:19.

On the other hand, economic growth was supported by the services sector (adding 1.5 pps in FY:19 following 1.2 pps in FY:18), despite the impact from the ban on betting operations (subtracting c. 0.4 pps). The improvement was underpinned by stronger private consumption, on the back of a tighter labour market and increasing remittances.

GDP is estimated to contract significantly in FY:20, dragged down by the COVID-19 shock and containment measures. Indeed, private consumption is set to weaken, due to the impact of quarantine measures and deteriorating economic sentiment. The latter should also weigh on investment activity, which is expected to decelerate, despite favourable financing conditions. At the same time, we expect the drag on overall growth from net exports to increase, reflecting disruptions in global supply chains and subdued external demand. Note that 50% of Albania's exports (8.5% of GDP) is channeled to Italy, whose GDP is seen contracting by more than 8.0% this year.

The Government has announced measures worth 1.3% of GDP to counter the impact of the COVID-19 pandemic. These include, *inter alia*, additional funding for the healthcare system, wage subsidies and deferral of tax payments. Overall, we see the budget deficit widening to 5.0% of GDP in FY:20 from 1.9% in FY:19.

At the same time, the Bank of Albania cut its key rate by 50 bps to a low of 0.5% (0% in real *ex-post* terms) and announced a temporary easing in provisioning requirements for banks.

Albania will also benefit from an "unconditional" loan worth 1.3% of GDP under the IMF's Rapid Financing Instrument (RFI), which will be used to address urgent balance of payments needs.

All said, assuming that the COVID-19 pandemic fades by end-Q2:20 and accounting for the impact of the earthquake (despite increased reconstruction spending, we project a net capacity loss of c. 0.5 pps of GDP this year), we see GDP declining by 5.0% in FY:20.