UNECE Trends in Europe and North America 2005 - Economy

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Gross domestic product (GDP)
The slow-down in economic growth began in western countries in 2001. Annual economic growth in the U.S. decreased from 3.8 per cent in the year 2000 to 0.3 per cent in 2001, in Canada from 4.5 to 1.5 per cent, and in the European Union from 3.4 to 1.5 per cent. Economic growth slowed down in all western economies – even in Ireland, which has experienced the most intensive growth in the last decade (the GDP growth rate has been around 10 per cent per year since 1995). Despite the slow-down, the GDP in Ireland still increased 5.7 per cent in 2001. The U.S. and Canada seem to have begun a recovery in 2002 with growth rates at 2.3 and 3.3 % respectively. In the EU, however, growth was even more sluggish in 2002.

GDP growth in central and eastern European countries has followed a somewhat different trend. Typically, the economies of this region declined in the years following the collapse of the Soviet regime (until 1993 or even 1995). After that, the economies began to grow, until there was another slow-down in 1999. The aftershock of the Russian economic crisis in 1998 reinforced the economic weakness in the Baltic area, which went into recession: the GDP growth rate decreased from 6 per cent in 1998 to –0.2 per cent in 1999. Five central European countries (Czech Republic, Hungary, Poland, Slovakia and Slovenia) experienced some slow-down in 2001 (especially Poland). In south-eastern Europe there was a recession from 1997 to 1999, largely due to the war in Bosnia. After those setbacks, the economic development in central and eastern Europe picked up pace and the growth rates remained generally higher than those in western Europe. Despite the unfavourable external environment (weakness of the western export market and weak world market prices), the economic environment in eastern Europe in 2002 remained buoyant and the area as a whole was still among the fastest growing regions in the world.

The countries of the CIS typically experienced a much greater and longer decline after the collapse of the Soviet regime than in central and eastern Europe. The growth of the whole region is very much influenced by the Russian Federation which makes up over two thirds of the volume of GDP for the CIS. Therefore, the economic downturn in Russia in 1998 pulled down the GDP growth rate for the region as a whole. The economies of the Caucasus and central Asian CIS countries overcame the recession already in 1996 and since then have experienced quite strong growth. The three European CIS countries (Belarus, Republic of Moldova, Ukraine) have had a small growth 1997-1999. However, since 1999 this area seems to be on a good road to recovery and the economic growth for this region has been approximately 5% or more each year.

Industrial structure
In western Europe and North America, the industrial structure does not change rapidly because of their advanced stage of development. When examining economies at different stages of development, one observes that the development of society in general goes roughly from an agricultural society to an industrial society and then to a service society. That is, at an earlier stage of economic development, the share of agriculture in the economy is large, but over time this share decreases and the share of industry begins to increase. Finally economies reach the situation, where the shares of agriculture and industry are declining and the share of services is increasing. When looking at the growth patterns of GDP (gross value added) in agriculture, industry and services, agriculture appears to be the most volatile – as it is greatly influenced by the weather conditions of each specific year, and has the lowest (sometimes even negative) growth rates.

In almost all western economies, the share of agriculture in total GDP is less than four per cent. The only exceptions are Greece, Cyprus, Iceland and Turkey. The higher percentage for Iceland can be explained by the importance of fishing in its national economy (fishing is included in agriculture). In the last decade the most rapid drop in the share of agriculture has been in Ireland (from 7.7 to 3.6 % of GDP) owing to the rapid expansion of the information and communication technologies (ICT) industry and services.

The development in central and eastern Europe resembles that in western Europe: the share of agriculture has decreased in all the countries (except for a slight increase in Bulgaria and Bosnia and Herzegovina). However, it is still quite high in the countries of south-east Europe (in Albania the highest in the UNECE: 51%). Also the share of industry has mostly decreased, while the share of services has increased. The development has been quite strong and rapid. In many countries the share of services is close to or over 60% thus approaching the same situation as in western economies.

In the CIS countries, the share of agriculture has in most cases decreased but still remains at a considerably high level compared to other ECE countries. The industry also plays quite a central role. This reflects the phenomenon that can also be seen in GDP growth figures. The recovery from the collapse of the Soviet regime began later than in central and eastern Europe. Therefore, the economies have reverted more toward an agricultural society. Since the economy declined, there was also no room for the expansion of services. However, now the transition process seems to be rather strong and rapid. In most CIS countries, industry is growing faster than services and the share of both is growing at the expense of agriculture.

Inflation

In the UNECE region in general, inflation was higher at the beginning of 1990s than at the end. In western Europe it can clearly be seen that up to the time of the introduction of the Euro in 1999, the price increases had slowed down. This was greatly due to the need of the European Union countries to meet one of the Maastricht convergence criteria to join the European Monetary Union (EMU), that the CPI must not exceed by more than 1.5 percentage points that of the three countries with the lowest inflation. Fourteen out of the 15 countries of the EU satisfied the criteria and were eligible to join the single currency in 1999. Greece did not satisfy the criteria, and the United Kingdom, Denmark and Sweden chose to stand aside in the first wave of Euro introduction. After 1999, the CPI increased again but not yet quite to the level seen at the beginning of the 1990s.

In central and eastern Europe, inflation was extremely high between 1991-1993 owing to the unstable economic situation. Since 1995, the prices began to stabilize in most countries (an exception is Bulgaria where the hyperinflation culminated in 1997). Price increases have not quite slowed down yet in Romania and Serbia and Montenegro, but in all other countries of this region the CPI remains well below 10%. The progress towards price stability and lower rates of inflation in the 8 EU accession countries (Czech Republic, Estonia, Hungary, Latvia, Lithuania, Poland, Slovakia and Slovenia) is also influenced by the limits set in the Maastricht criteria. If these countries join the EU in 2004, they have to meet these criteria within the next few years to be able to join the Euro zone.

In the CIS countries, inflation has not slowed down as quickly and there are considerable differences between countries. In the Caucasian area, prices have stabilized and there has even been deflation in some years. In Belarus, Russian Federation and Tajikistan inflation still remains in the two-digit figures although it is slowing down. In Turkmenistan and Uzbekistan, for the last few years there are no data available to assess the level of inflation. However, the relatively coherent and consistent macroeconomic policies in the CIS countries in recent years have contributed to the strengthening of economic growth and macroeconomic stabilization, which is reflected inter alia in falling inflation rates.

Real wages in central and eastern Europe and CIS

At the start of the transition process, in central and eastern European and CIS countries the real wages (the wages adjusted by the level of inflation) dropped dramatically as the wages could not keep pace with the rapidly increasing prices. In most of central and eastern Europe real wages started to increase in 1993-1994 and in most countries of the region were 30 to 80% higher in 2001 than in 1993. The growth has been somewhat slower in Hungary, Romania and Slovakia. In Hungary, there was a drop in 1995-96, in Romania in 1997 and in Slovakia there has been some decrease in 1999-2000. Owing to these setbacks the real wages in these three countries in 2001 were only 11-15% higher than in 1993. In contrast, in Bulgaria prices have been increasing more quickly than wages since 1994. After the hyperinflation in 1997, the prices are under control and real wages began to increase in 1998. Still in 2001, the real wages in Bulgaria were approximately two thirds of the 1993 level.

As for the economy in general, the positive shift in real wages in the CIS occurred a few years later than in central and eastern Europe. The low point for many CIS countries was in 1994-1995. Since then, wages have in general increased more quickly than prices. Still, by 2001, Kyrgyzstan, Republic of Moldova, Tajikistan and Ukraine had not yet reached the 1993 level. As with the CPI, for Turkmenistan and Uzbekistan there are no data available to evaluate the situation.

Household consumption

The final consumption expenditure of households characterizes the demand side of GDP. Its dynamics allow assessing how the welfare of households has developed on an aggregated level. It reflects the changes in wages and other incomes, but also in employment and in the behaviour towards saving in households. Therefore, the growth of household consumption can be somewhat different from the growth of real wages and incomes.

Household consumption expenditures in western countries have developed quite steadily since 1995. Typically in western Europe and North America, an average of 50-60% of GDP goes into household consumption. In most countries of this area, the increase in household consumption expenditure per capita 1995-2001 has been between 10-20 per cent. The highest increase was in Ireland (44.5%). This was possible owing to the very high GDP growth rates while household consumption grew more slowly than the total GDP.

In central and eastern Europe, the share of household consumption expenditure tends to be somewhat higher than in western countries, mostly between 55-65% of GDP. The consumption of households on an aggregate level has increased in general more rapidly than in the western countries (albeit at a much lower starting level) and often more quickly than the total GDP. Even during the years when real wages were decreasing in some countries (Bulgaria and Romania) household consumption decreased much less, or even continued to increase.

In the CIS countries, the share of private consumption in GDP ranges from 50% in Russia to 94 % in Armenia. The average is somewhere between 65-70%. In several CIS countries the growth in final household consumption has been significant but still not as high as the growth in real wages.

External debt of central and eastern Europe and CIS countries

Among the central and eastern European and CIS countries, the Russian Federation had the highest external debt in 2001 (162 billion US dollars) followed by Poland (72 billion) and the Czech Republic (22 billion). Although the debt for these countries was large in absolute terms, it accounted for about 40-50% of their total GDP. From this viewpoint the situation is most difficult in Kyrgyzstan and the Republic of Moldova where the external debt in 2001 was greater than the total-GDP.