REGIONAL ECONOMIC PROSPECTS

European Bank
for Reconstruction and Development

MAY
2025

Regional Economic Prospects in the EBRD Regions

European Bank for Reconstruction and Development

Uncertain times

May 2025

Average growth in the EBRD regions slowed from 3.4 per cent in 2022 to 2.8 per cent in 2023 and 2024. The 2024 outcome was in line with the forecast made in September 2024, though with weaker-than-expected outturns in most EU-EBRD economies (reflecting sluggish growth in advanced Europe) and stronger-than-expected growth in Türkiye, Central Asia, and the Caucasus.

Trade and economic policy uncertainty has risen sharply in 2025. In this context, the 2025 growth projection for the EBRD regions has been revised down by 0.2 percentage points relative to the February 2025 forecast (following a 0.3 percentage point downward revision in February 2025 relative to September 2024). Growth is expected to average 3 per cent in 2025, with downward revisions across most economies on increased global policy uncertainty, weaker external demand and the direct and indirect effects of the announced increases in import tariffs. Growth is expected to pick up to 3.4 per cent in 2026, unchanged relative to February 2025. Our forecasts reflect heightened uncertainty related to economic and trade policy, as well as the impact of the ongoing war on Ukraine, the war in Gaza and the volatile situation in the Middle East.

Increases in US import tariffs that became effective in 2025 (up to mid-April)—the 25 per cent tariffs on steel, aluminium and cars and the 10 per cent increases in blanket tariffs—are estimated to push the expected average effective US tariff on imports from the EBRD regions from 1.8 per cent in 2024 to 10.5 per cent (based on the 2024 composition of imports). In the EBRD regions the largest direct negative impact of tariff increases on output is estimated for the Slovak Republic (0.8 per cent of GDP), Jordan (0.6 per cent) and Hungary (0.4 per cent). Tariffs on cars account for 83 per cent of the overall impact in the Slovak Republic and 41 per cent in Hungary.

The effects of higher US tariffs and increased trade policy uncertainty could be propagated further through global value chain linkages, including to economies with limited direct exports to the US. While the United States is the key export market globally, for economies in the EBRD regions the top destinations of exports tend to be Germany, other large EU economies and, in some cases, China. Notwithstanding the declining share of Germany and the rising share of China in the cross-border trade of economies in the EBRD regions, Germany remains the largest trading partner for ten economies in the EBRD regions while exports to China account for much smaller shares of total exports for most economies in the EBRD regions (with the notable exception of Mongolia) and are more concentrated in commodities.

On the other hand, the effect of higher US tariffs could be somewhat mitigated by trade diversion due to relative changes in tariff rates whereby economies facing lower relative tariff rates than their competitors in the US market could gain market shares. At present, China is subject to significantly higher US import tariffs than other economies.

Average inflation in the EBRD regions peaked at 17.5 per cent in October 2022 and bottomed out at 5.3 per cent in September 2024 before picking up to 6.1 per cent as of February 2025. Median (typical) inflation points to an even stronger pick-up since September 2024. Inflationary pressures are increasingly demand-driven, reflecting loose fiscal policies and high nominal wage growth.

Despite substantial fiscal pressures, the IMF expects average debt in the EBRD regions to remain broadly stable, at around 52 per cent of GDP over the period 2025-29. These projections appear to assume significant fiscal measures on the part of governments as they combine ambitious revenue projections with spending remaining in line with historical trends. Higher spending on defence, industrial policies and interest payments is thus expected to be financed by cutting expenditure elsewhere. In addition, bond issuance has become more important relative to bilateral and multilateral government debt, both as shares of total external debt and total external government debt of economies in the EBRD regions and emerging markets more generally. As a result, the fiscal accounts of lower-income economies may be more exposed to pressures emanating from policy uncertainty and market volatility than before.

Growth in ***central Europe and the Baltic states*** *picked up from 0.4 per cent in 2023 to 2.1 per cent in 2024 as economies gradually adjusted to a lower supply of Russian gas and higher energy prices following Russia's invasion of Ukraine. Growth is expected at 2.4 per cent in 2025 and 2.7 per cent in 2026. Forecasts for both years have been revised down relative to February 2025 on the direct and indirect impact of new tariffs, increased global policy uncertainty and weaker external demand, in particular from Germany, despite Germany's shift towards more expansionary fiscal policy.*

Growth in the ***south-eastern EU*** *decelerated from 2.3 per cent in 2023 to 1.6 per cent in 2024 on sluggish external demand, a slowdown in investment and more modest fiscal stimulus. Growth is expected to pick up to 2 per cent in 2025 (less than previously expected, despite domestic demand boosting growth in Bulgaria) and 2.4 per cent in 2026.*

Growth in the ***Western Balkans*** *is expected to slow from 3.6 per cent in 2024 to 3.2 per cent in 2025 and 3.4 per cent in 2026. Downward revisions reflect spillovers from slower growth in advanced Europe as well as political instability in Serbia.*

Growth in ***Central Asia*** *moderated from 5.7 per cent in 2023 and 5.6 per cent in 2024 and is expected at 5.5 per cent in 2025 and 5.2 per cent in 2026. Downward revisions for 2025 for Kazakhstan and Mongolia in large part reflect lower expected commodity prices.*

In ***eastern Europe and the Caucasus****, growth slowed from 4.5 per cent in 2023 to 3.9 per cent in 2024 as the boost from intermediated trade and inflows of labour and capital to the economies of the Caucasus waned. Growth is expected to moderate further to 3.5 per cent in 2025 before picking up to 4.3 per cent in 2026. The 2025 growth forecasts for* ***Moldova*** *and* ***Ukraine*** *have been revised down on weaker external demand from the EU while Russia's attacks on Ukraine's energy infrastructure continued to weigh on economic activity.*

In ***Türkiye****, growth moderated from 5.1 per cent in 2023 to 3.2 per cent in 2024 on tighter monetary policy aimed at bringing down persistently high inflation. Growth is expected to moderate further to 2.8 per cent in 2025 before picking up to 3.5 per cent in 2026. The downward revision for 2025 reflects lower domestic and external demand and tighter-than-expected monetary policy.*

Growth in the ***southern and eastern Mediterranean*** *is expected to pick up from 2.7 per cent in 2023 and 2024 to 3.6 per cent in 2025 and 3.9 per cent in 2026. Forecasts for both years have nonetheless been revised down relative to February 2025 reflecting the impact of conflicts (through trade and confidence channels) and increased global policy uncertainty.*

Table 1. GDP growth in real terms

	Actual		Forecast (May'25)		Revision since Feb'25	
	2023	2024	2025	2026	2025	2026
EBRD regions	**2.8**	**2.8**	**3.0**	**3.4**	**-0.2**	**0.0**
Central Asia	**5.7**	**5.6**	**5.5**	**5.2**	**-0.2**	**0.0**
Kazakhstan	5.1	4.8	4.9	4.5	-0.3	0.0
Kyrgyz Republic	6.2	9.0	7.0	6.0	0.0	0.0
Mongolia	7.4	4.9	6.3	6.0	-0.4	0.0
Tajikistan	8.3	8.4	7.0	5.7	0.0	0.0
Turkmenistan	6.3	6.3	6.3	6.3	0.0	0.0
Uzbekistan	6.3	6.5	6.0	6.0	0.0	0.0
Central Europe and the Baltic states	**0.4**	**2.1**	**2.4**	**2.7**	**-0.3**	**-0.1**
Croatia	3.3	3.9	2.9	2.6	-0.1	0.0
Czechia	-0.1	1.1	1.6	2.2	-0.3	-0.2
Estonia	-3.0	-0.3	1.3	2.0	-0.4	-0.6
Hungary	-0.8	0.5	1.5	2.7	-0.5	-0.1
Latvia	2.9	-0.4	1.8	2.4	-0.2	-0.1
Lithuania	0.3	2.8	2.6	2.6	-0.2	-0.1
Poland	0.2	2.9	3.3	3.2	-0.1	0.0
Slovak Republic	2.2	2.1	1.4	1.8	-0.5	-0.4
Slovenia	2.1	1.6	1.9	2.3	-0.1	-0.1
Eastern Europe and the Caucasus	**4.5**	**3.8**	**3.5**	**4.3**	**-0.1**	**0.0**
Armenia	8.3	5.9	5.0	4.5	0.0	0.0
Azerbaijan	1.4	4.1	3.0	2.5	0.0	0.0
Georgia	7.8	9.4	6.0	5.0	0.0	0.0
Moldova	0.7	0.1	1.8	3.8	-0.2	0.0
Ukraine	5.3	2.9	3.3	5.0	-0.2	0.0
South-eastern EU	**2.3**	**1.6**	**2.0**	**2.4**	**-0.1**	**0.0**
Bulgaria	1.9	2.8	2.8	2.6	0.4	-0.2
Greece	2.3	2.3	2.2	2.2	-0.1	-0.1
Romania	2.4	0.8	1.6	2.4	-0.2	0.0
Southern and eastern Mediterranean	**2.7**	**2.7**	**3.6**	**3.9**	**-0.1**	**-0.2**
Egypt	2.9	3.1	4.0	4.5	-0.2	-0.2
Jordan	2.7	2.5	2.2	2.4	-0.1	-0.2
Lebanon	-0.2	-5.7	1.9	2.9	-0.1	-0.1
Morocco	3.4	3.2	3.5	3.4	-0.1	0.0
Tunisia	0.0	1.4	1.7	2.1	-0.1	-0.1
Turkiye	**5.1**	**3.2**	**2.8**	**3.5**	**-0.2**	**0.0**
Western Balkans	**3.4**	**3.6**	**3.2**	**3.4**	**-0.4**	**-0.2**
Albania	3.9	4.0	3.5	3.5	-0.2	-0.2
Bosnia and Herzegovina	1.9	2.5	2.5	2.7	-0.3	-0.3
Kosovo	4.1	4.4	3.9	3.9	-0.1	-0.1
Montenegro	6.3	3.0	2.6	2.7	-0.3	-0.3
North Macedonia	2.1	2.8	2.6	2.7	-0.4	-0.3
Serbia	3.8	3.9	3.5	3.7	-0.5	-0.3
Memo: Egypt (fiscal year to June)	3.8	2.4	3.8	4.4	0.2	-0.2
Memo: EEC excl. Ukraine	3.6	4.9	3.7	3.4	-0.1	0.0
Memo: Belarus	3.9	4.0	2.5	2.5	0.0	0.0
Memo: Russia	4.1	4.3	1.5	1.5	0.0	0.0

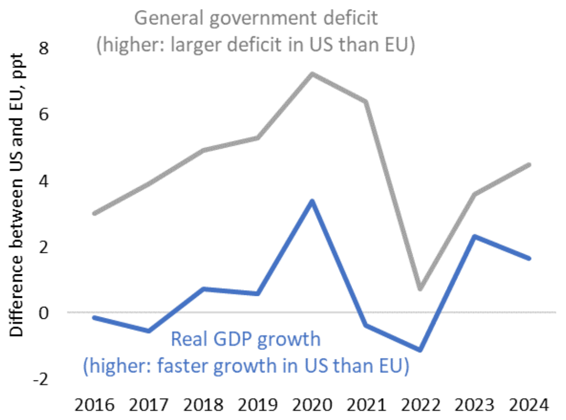
Source: Eurostat for EU economies, national authorities and EBRD. Note: Weights are based on the values of gross domestic product in 2022 at market exchange rates. The table also includes forecasts for Belarus and Russia notwithstanding the fact that Belarus and Russia have had their access to Bank resources suspended under Article 8.3 of the Agreements Establishing the EBRD.

Growth in the EBRD regions in 2024 remained stable at 2.8 per cent

Average growth in the EBRD regions slowed from 3.4 per cent in 2022 to 2.8 per cent in 2023 and 2024. This outcome was in line with the forecast made in September 2024, though with weaker-than-expected outturns in most EU-EBRD economies and stronger-than-expected outturns in Türkiye, Central Asia and eastern Europe and the Caucasus (notably Georgia; see Table 1).

This outcome reflects weak external demand, especially from advanced Europe, with a continued growth divergence between the EU and the US. This divergence in part reflects a consistently more expansionary fiscal stance in the US, before, during and after the Covid-19 pandemic. The difference in deficits between the US and the EU closely tracks the difference in their growth rates (see Chart 1).

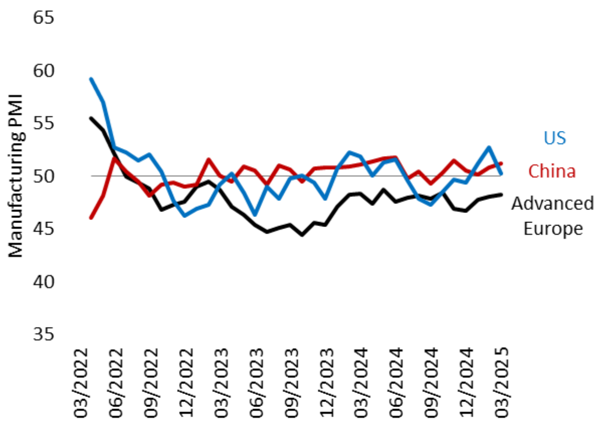
Chart 1. Growing divergence between the US and EU in recent years reflecting different fiscal paths



Source: IMF World Economic Outlook October 2024 and authors' calculations.
Note: Weighted averages across EU economies from the IMF.

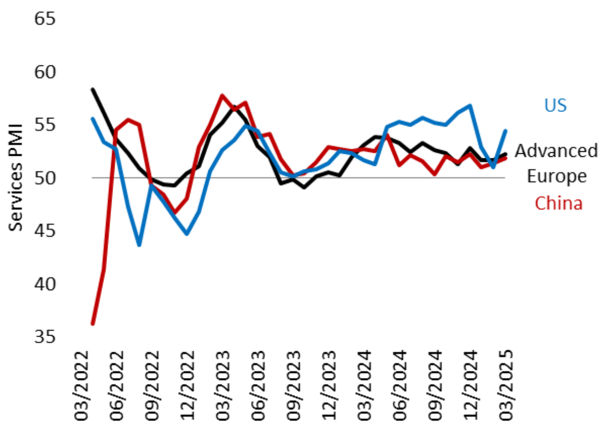
Manufacturing purchasing managers' indices (PMIs) in advanced European economies remained depressed, in part reflecting high and growing uncertainty about the rules governing international trade in goods. PMIs in the US, in particular related to services, were expansionary up to March 2025 despite policy uncertainty (see Charts 2 and 3, where a value above 50 represents an increase relative to the previous month, while a value below 50 represents a decrease). Manufacturing PMI also remained below 50 for most of the past three years for most of the six EBRD economies with such high-frequency indicators (PMI values have been lower in Czechia, Romania and Türkiye; they remained broadly above 50 for Greece and Kazakhstan and recently surpassed 50 in Poland).

Chart 2. Manufacturing PMI remained depressed in advanced European economies



Source: CEIC and authors' calculations.
Note: Advanced Europe based on IMF country grouping excluding economies in the EBRD regions. Latest observation is March 2025.

Chart 3. Services PMI in the US remained expansionary despite policy uncertainty

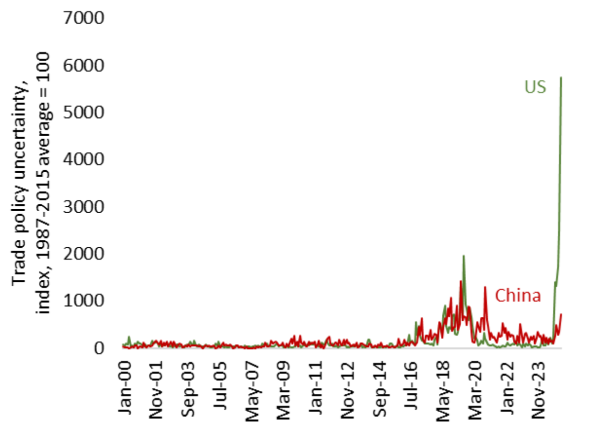


Source: CEIC and authors' calculations.
Note: Advanced Europe based on IMF country grouping excluding economies in the EBRD regions. Latest observation is March 2025.

In the crossfire of trade wars

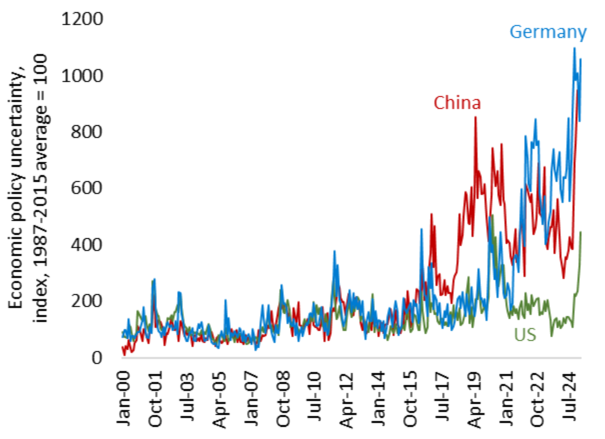
Trade and economic policy uncertainties rose sharply in 2025 reflecting unknowns surrounding potential increases in tariffs on US imports and reciprocal measures by US trade partners. Measures of policy uncertainty are at all-time highs in the US and the same is true in Germany (see Charts 4 and 5). The increased uncertainty about trade rules can, already by itself, have a significant detrimental effect on investment, and production.

Chart 4. Trade policy uncertainty spiked in the US



Source: CEIC, Baker, Bloom and Davis (2016) and authors' calculations.
Note: Latest observation is March 2025.

Chart 5. Economic policy uncertainty is at all-time highs in Germany and the US



Source: CEIC, Baker, Bloom and Davis (2016) and authors' calculations.
Note: Latest observation is March 2025 for Germany and US and January 2025 for China.

Box 1 provides an overview of the tariff changes implemented and announced until mid-April 2025 and examines their potential impact on economies in the EBRD regions and select comparators. It looks at the joint impact of increases in US import tariffs that became effective in 2025: the 25 per cent tariffs on steel, aluminium, and cars, the 125 per cent tariff increase for China and the 10 per cent increases in tariffs for other economies. While the estimates are imprecise and uncertainty about future trade regimes is high, the analysis sheds light on the likely magnitudes of the impact and the relative exposure of various economies to higher tariffs and greater policy uncertainty.

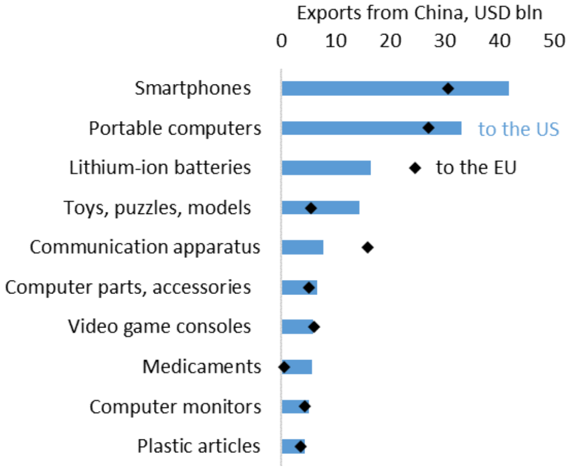
These new tariffs as of mid-April -- the 25 per cent tariffs on steel, aluminium and cars and the 10 per cent increases in blanket tariffs -- are estimated to push the expected average effective US tariff on imports from the EBRD regions from 1.8 per cent in 2024 to 10.5 per cent (based on the 2024 composition of trade).

In the EBRD regions the largest direct negative impact of tariff increases on GDP is estimated for the Slovak Republic (0.8 per cent of GDP), Jordan (0.6 per cent) and Hungary (0.4 per cent). Tariffs on cars account for 83 per cent of the overall impact in the Slovak Republic and 41 per cent in Hungary.

These effects could be propagated further through global value chain linkages, including to economies with limited direct trade links to the US. On the other hand, the effect of higher US tariffs could be somewhat mitigated by trade diversion due to relative changes in tariff rates whereby economies facing lower relative tariff rates than their competitors in the US market could gain market shares. At present, China is subject to significantly higher US import tariffs (ranging from extra 20 per cent on various electronics items to 145 per cent for goods not covered by special provisions).

Changes in relative tariff rates could also result in potential rerouting of Chinese exports from the US to other destinations including the EU. Chart 6 highlights that China's top 10 exports to the US are dominated by consumer electronics and China is also a major exporter of those goods to other markets. For instance, China accounts for 92 per cent of EU imports of portable computers, 87 per cent of imports of lithium-ion batteries and 81 per cent of imports of video-game consoles. In turn, while EU imports from China are high for plastics and medicaments, China is a less important source of these in relative terms (accounting for 42 per cent and only 1 per cent of EU imports of these goods respectively).

Chart 6. China's exports to the US and the EU are dominated by consumer electronics

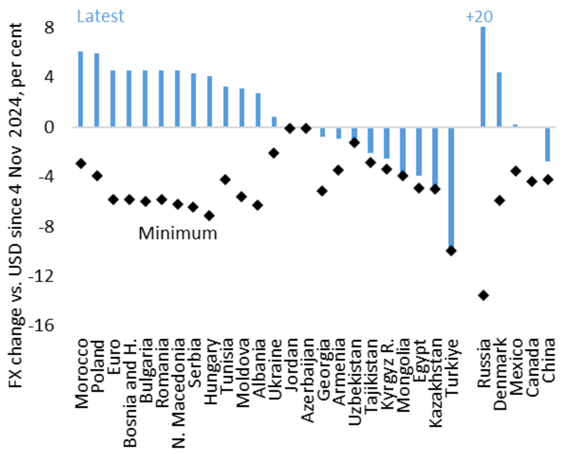


Source: UN COMTRADE and authors' calculations.
Note: 2024 for the US and 2023 for the EU.

Stock markets have exhibited high volatility on tariff announcements, with drops in valuations followed by some corrections on later announcements of pauses in implementation of bilateral US tariffs, partial exemptions for a range of goods and potentially lower tariff rates.

Many currencies in the EBRD regions initially weakened against the US dollar following the US election, however, they have typically strengthened again since amidst broader weakening of the US dollar against major currencies (see Chart 7). Most currencies in the EBRD regions have weakened against the Euro over this period.

Chart 7. Many currencies initially weakened against the US dollar following the US election before strengthening recently

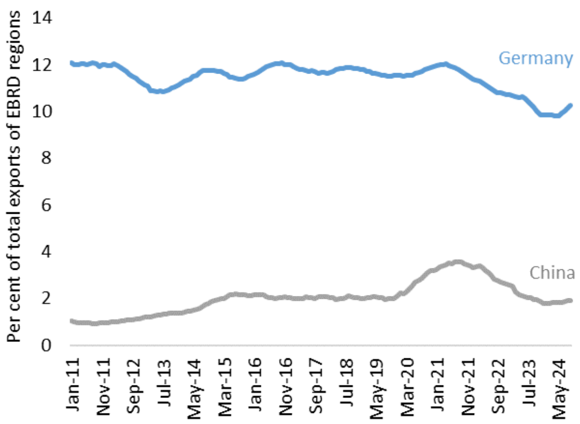


Source: Bloomberg and authors' calculations.
Note: As of 16 April 2025.

Reorientation of trade

While the United States is the key export market globally, for economies in the EBRD regions the top destinations for exports tend to be Germany, other large EU economies and, in some cases, China. Exports from the EBRD regions to Germany declined from around 12 per cent of total exports in 2011-21 to around 10 per cent in 2024 (see Chart 8). Exports to China increased from less than 1 per cent in 2011 to around 2 per cent in 2024 (peaking at over 4 per cent in 2021-22).

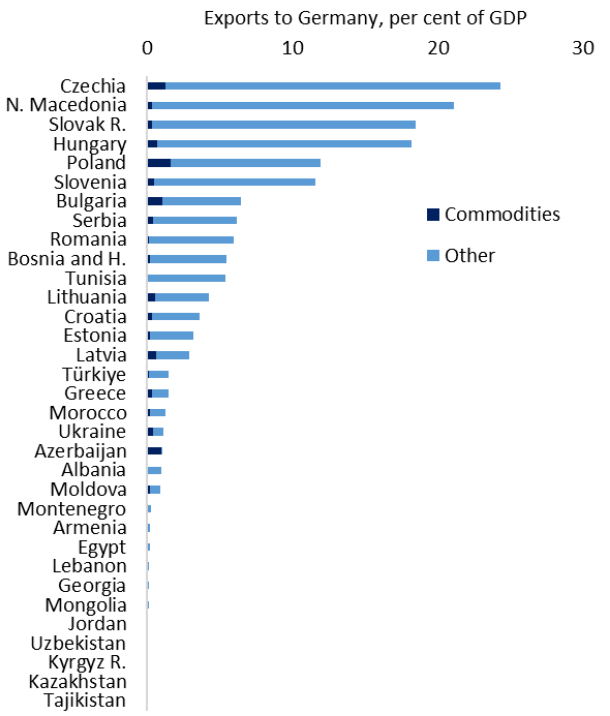
Chart 8. Germany remains an important export market for the EBRD regions



Source: UN COMTRADE and authors' calculations.
Note: Simple average across a balanced panel of 14 economies. 12-month moving average.

Nonetheless, Germany remains the largest trading partner for 10 economies in the EBRD regions, accounting for more than 25 per cent of exports for North Macedonia, Czechia, Poland, and Hungary. In Czechia, North Macedonia, the Slovak Republic, and Hungary exports to Germany exceed 18 per cent of GDP (see Chart 9). For most economies in the EBRD regions, exports to Germany also increased since 2019 (economies in eastern Europe and the Caucasus and Central Asia are the notable exceptions).

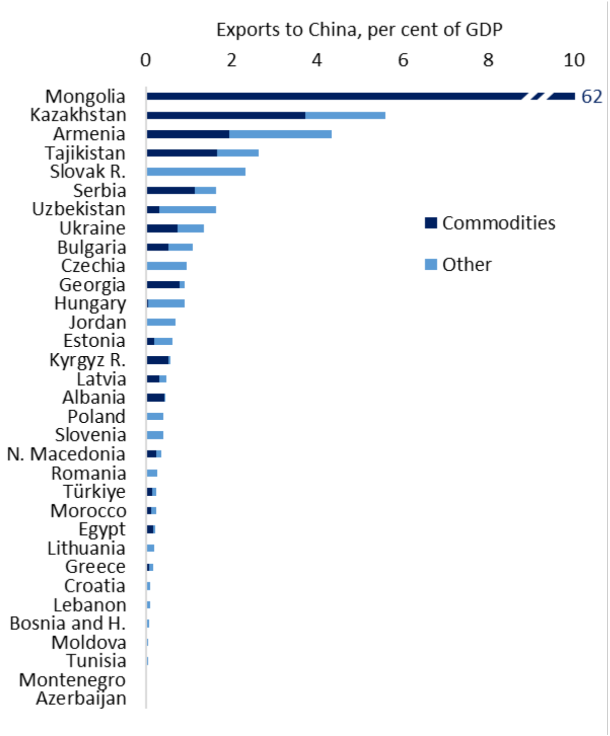
Chart 9. Germany remains an important export destination for many economies in the EBRD regions



Source: UN COMTRADE and authors' calculations. Note: 2024 or latest available. Definition of commodity is based on Broad Economic Categories classification and manual coding.

Exports to China account for much smaller shares of total exports on average, though they exceed 62 per cent of GDP in Mongolia and 4 per cent of GDP in Kazakhstan and Armenia (see Chart 10). They are more concentrated in commodities than exports to Germany.

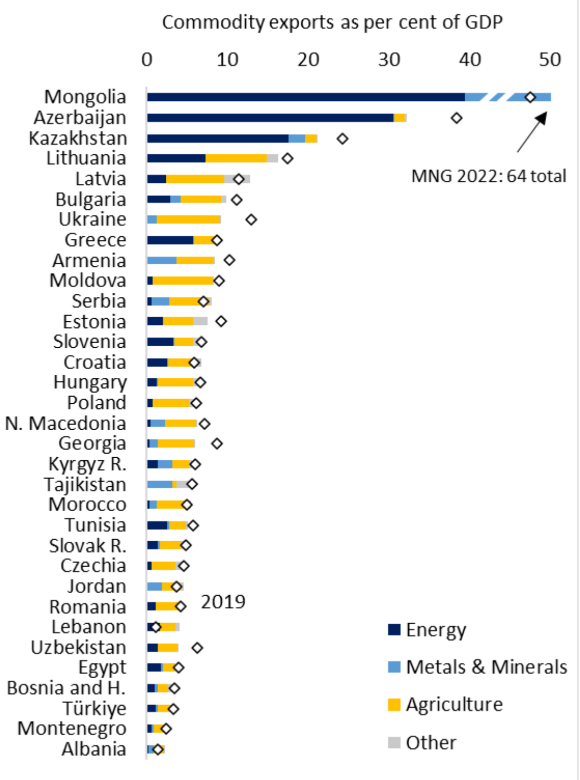
Chart 10. Exports to China exceed 62 per cent of GDP in Mongolia



Source: UN COMTRADE and authors' calculations. Note: 2024 or latest available. Definition of commodity is based on Broad Economic Categories classification and manual coding.

More generally, commodity exports remain important for Mongolia, Azerbaijan, and Kazakhstan, though for many economies dependence on such exports has declined since 2019 (see Chart 11). Real prices of copper, coal and corn are around 20 to 30 per cent higher than they were in 2019; real wheat prices are below their 2019 level.

Chart 11. For many economies dependence on commodity exports has declined since 2019

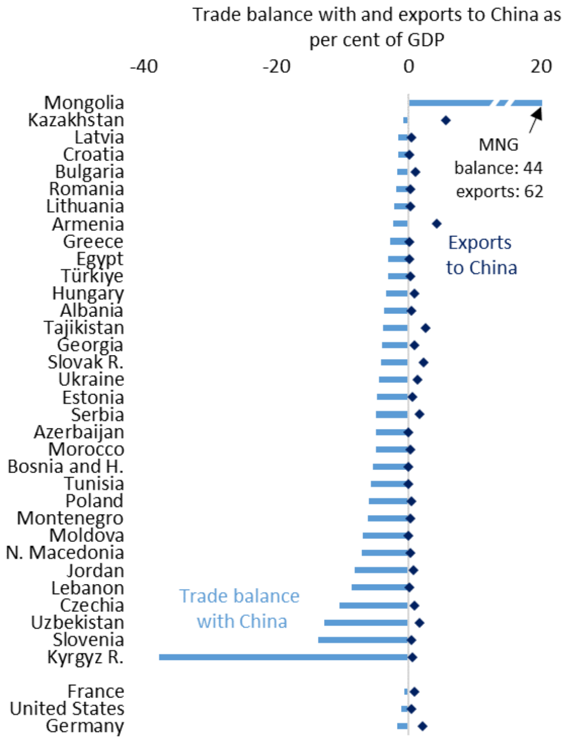


Source: UN COMTRADE and authors' calculations. Note: 2024 or latest available. Definition of commodity is based on Broad Economic Categories classification and manual coding. Diamonds show total commodity exports in 2019.

All economies in the EBRD regions except for Mongolia have a trade deficit with China (see Chart 12). Trade deficits are largest for the Kyrgyz Republic (38 per cent of GDP), Slovenia and Uzbekistan (around 13 per cent of GDP), compared with 1 per cent for the Unites States and 2 per cent for Germany.

Imports from China are highest as a share of GDP in the Kyrgyz Republic, Slovenia, and Czechia—these economies primarily import cars, chemicals and electronics respectively from China.

Chart 12. All economies in the EBRD regions except for Mongolia have a trade deficit with China



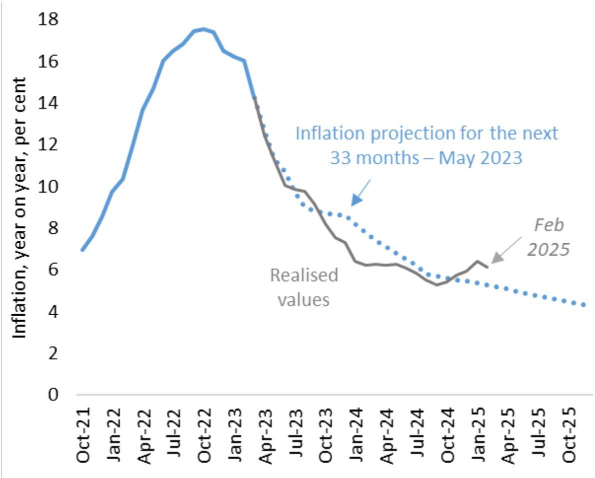
Source: UN COMTRADE and authors' calculations. Note: 2024 or latest.

Global car production has been shifting towards Asia (see Box 2). China's share in global car production rose from 3 per cent in 1997 to 32 per cent in 2023. The shares of advanced Europe and the US declined from 51 per cent to 23 per cent. The share of the EBRD regions rose from 3 per cent to 7 per cent, with substantial gains in Uzbekistan and Morocco and declines in Czechia, the Slovak Republic, and Poland.

Renewed inflationary pressures

Average inflation in the EBRD regions peaked at 17.5 per cent in October 2022 and bottomed out at 5.3 per cent in September 2024 before picking up to 6.1 per cent as of February 2025, more than 1 percentage point above its pre-pandemic average (see Chart 13).

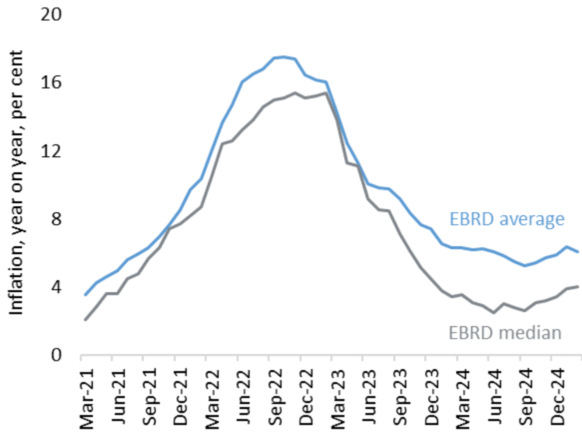
Chart 13. Average inflation in recent months higher than expected



Source: May 2023 Regional Economic Prospects based on IMF, national authorities via CEIC, World Bank Global Inflation database and authors' calculations.
Note: Simple average across 33 economies in the EBRD regions (excluding Ukraine 2024 onwards). Dashed line denotes a month-to-month curve fitted based on end of-year and annual average April 2023 IMF inflation forecasts. Grey line denotes data releases after the May 2023 Regional Economic Prospects.

Median (typical) inflation points to an even stronger pick-up since September 2024, from 2.6 per cent to 4 per cent in February 2025, suggesting that the recent increase is broad-based rather than driven by a few high-inflation economies (see Chart 14).

Chart 14. An even stronger pick-up in median (typical) inflation since September 2024

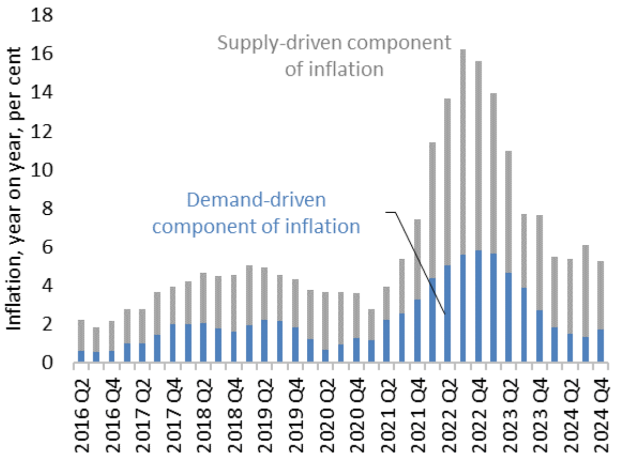


Source: Refinitiv and authors' calculations.
Note: Simple average and median across 33 economies in the EBRD regions.

Inflationary pressures increasingly demand-driven

Inflationary pressures are increasingly demand-driven, reflecting loose fiscal policies and high nominal wage growth (see Chart 15). In contrast, in 2022-23, inflation in the EBRD regions was to a large extent supply-driven reflecting rising food and energy prices and supply chain disruptions. Chart 15 extends the decomposition of inflation into supply- and demand-side factors presented in the earlier Regional Economic Prospects (see EBRD 2025, Firat and Hao 2023 and Shapiro 2022).

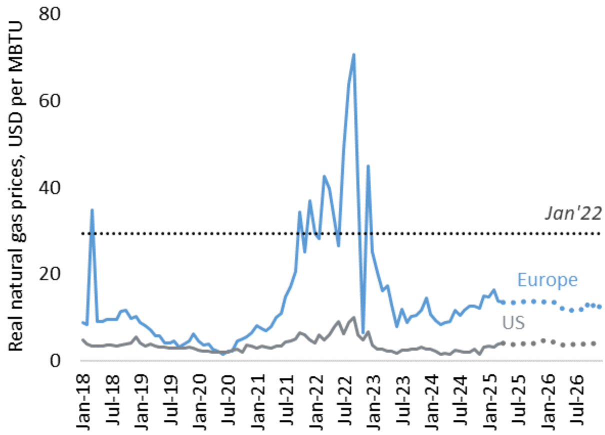
Chart 15. Expansionary fiscal policies and other demand-driven factors contributed to the recent uptick in inflation



Source: CEIC, national statistical agencies and authors' calculations.
Note: Medians across Czechia, Egypt, Estonia, Greece, Hungary, Kazakhstan, Latvia, Poland, Romania, and Türkiye. The inflation decomposition is obtained by estimating a VAR model using the deflator and the volume of a particular sector in first differences with four lags. This VAR model looks at whether inflation in each individual sector can be attributed to supply- or demand-driven factors, following the methodology used in Shapiro (2022).

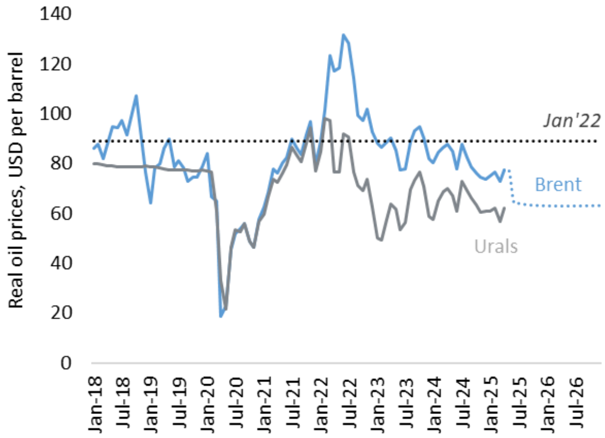
Energy prices moderated, reducing supply-side inflationary pressures. Expectations about future prices fell further on tariff announcements in April (see Charts 16 and 17). By mid-April, Brent crude oil futures prices fell to the US$65 per barrel mark for the first time since February 2021, down from around US$75 at the start of April.

Chart 16. Natural gas prices remain three times the US price in Europe but are expected to moderate



Source: Refinitiv and authors' calculations.
Note: Prices adjusted for US inflation.

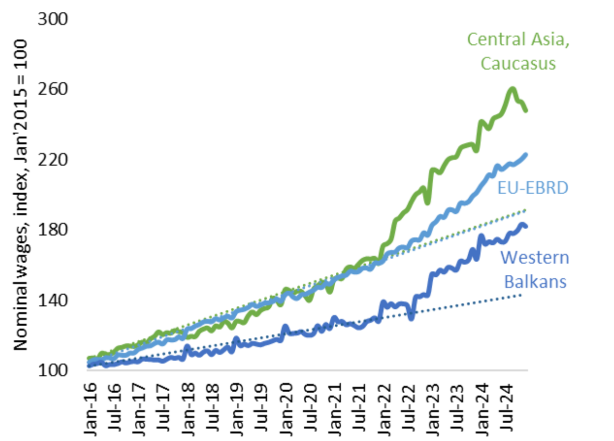
Chart 17. Oil prices have moderated, and expectations fell further on tariff announcements



Source: Refinitiv and authors' calculations.
Note: Prices adjusted for US inflation.

Across the EBRD regions, nominal wage growth picked up and contributed to inflation. By end-2024, nominal wages far exceeded their pre-Covid trends—by 30 per cent in Central Asia and the Caucasus, 17 per cent in EU-EBRD economies and 27 per cent in the Western Balkans (see Chart 18).

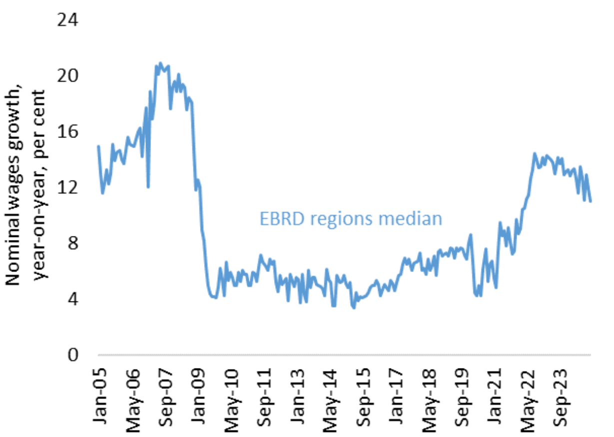
Chart 18. High nominal wage growth across the EBRD regions



Source: Refinitiv Eikon and authors' calculations. Note: Solid lines are actuals, dashed lines denote pre-Covid trends. Simple averages across an unbalanced panel of up to 10 EU-EBRD economies, up to 6 economies in Central Asia and the Caucasus and 5 economies in the Western Balkans. Last observation is December 2024.

Median nominal wage growth in the EBRD regions, at around 11 per cent, was comparable to that seen during the early 2000s boom (see Chart 19).

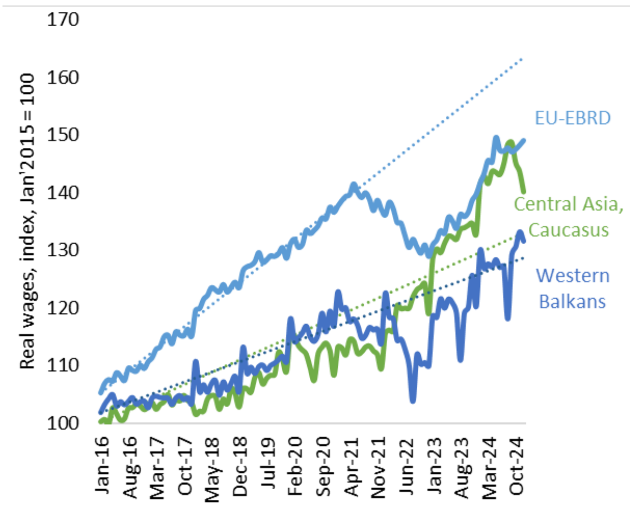
Chart 19. Median nominal wage growth in the EBRD regions comparable to the early 2000s



Source: Refinitiv Eikon and authors' calculations. Note: Simple averages across an unbalanced panel of up to 10 EU-EBRD economies, up to 6 economies in Central Asia and the Caucasus and 5 economies in the Western Balkans. Last observation is December 2024.

As inflation started picking up again and global uncertainty increased, real wage growth started to cool down (see Chart 20). Real wages remain far below their pre-Covid trend in EU-EBRD economies—though relative to a much steeper trend than in Central Asia and the Caucasus and the Western Balkans where real wages remain 5 and 2 per cent respectively above their (flatter) pre-Covid trends.

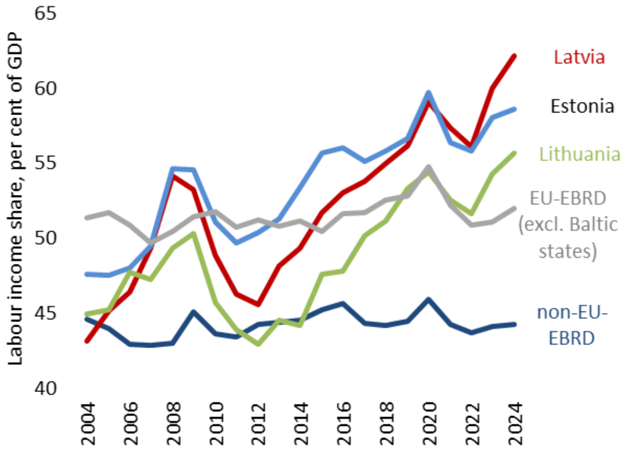
Chart 20. As inflation started picking up again and global uncertainty increased, real wage growth started to cool down



Source: Refinitiv Eikon and authors' calculations. Note: Solid lines are actuals, dashed lines denote pre-Covid trends. Simple averages across an unbalanced panel of up to 10 EU-EBRD economies, up to 6 economies in Central Asia and the Caucasus and 5 economies in the Western Balkans. Last observation is December 2024.

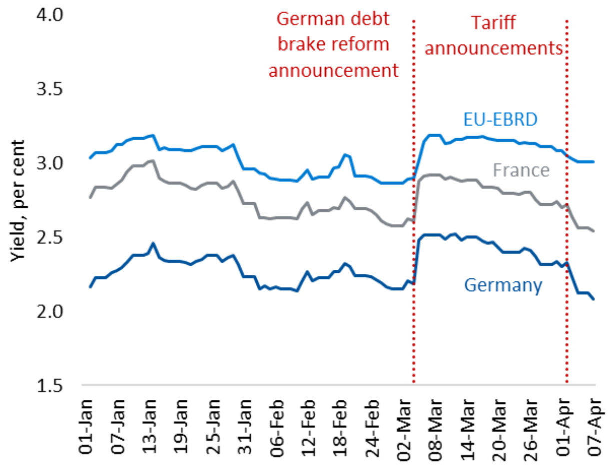
Nonetheless, in some EU-EBRD economies, in particular the Baltic States, continued tightness of labour markets and skill shortages have translated into increasing labour shares of income, likely reflecting increased bargaining power of workers, while the capital share of income (the share of national income going to the owners of capital, including corporations, real estate and financial investments) has declined (see Chart 21).

Chart 21. In the Baltic States, the labour share of income rose



Source: ILO and authors' calculations.

Chart 22. Yields on Germany bonds and in EU-EBRD economies increased on the German debt brake reform announcement



Source: Bloomberg and authors' calculations.
Note: Median shown for EU-EBRD. Changes quoted in the text refer to 4 March – 2 April 2025 relative to 1 January – 3 March 2025.

Fiscal pressures

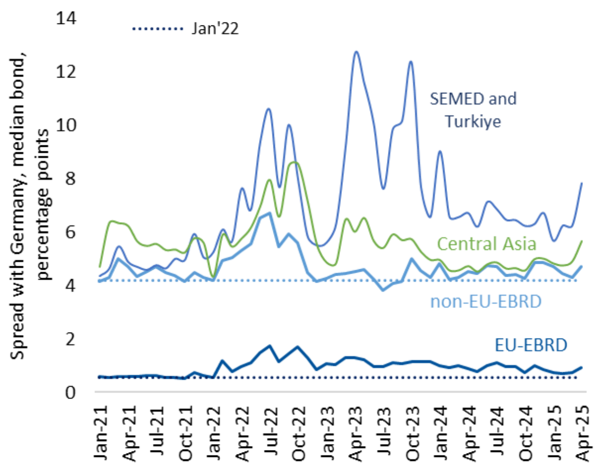
On 21 March 2025, Germany approved a constitutional amendment to its national fiscal rule, the 'debt brake'. Under the amended provisions, defence spending above 1 per cent of GDP will not be subject to any borrowing limit. The amendment also creates a €500 billion extrabudgetary fund for additional infrastructure spending, €100 billion of which is earmarked for climate-related investment. The fund must be spent within 12 years (see Zettelmeyer 2025).

Following the announcement, yields on German bonds increased by 0.16 percentage points (see Chart 22). Yields in EU-EBRD economies followed, rising by 0.12 percentage points (in contrast, yields in non-EU EBRD economies declined by 0.26 percentage points).

However, yields on German and EU-EBRD bonds subsequently declined on tariff announcements in early April, while yields for non-EU-EBRD economies increased.

In the EBRD regions as a whole, the median yield on 5-year government bonds increased by 2.4 percentage points between early February 2022 and mid-April 2025. While the spread relative to Germany returned temporarily to the levels seen before the start of the war on Ukraine, it rose to 0.2 percentage points following tariff announcements in early April (see Chart 23).

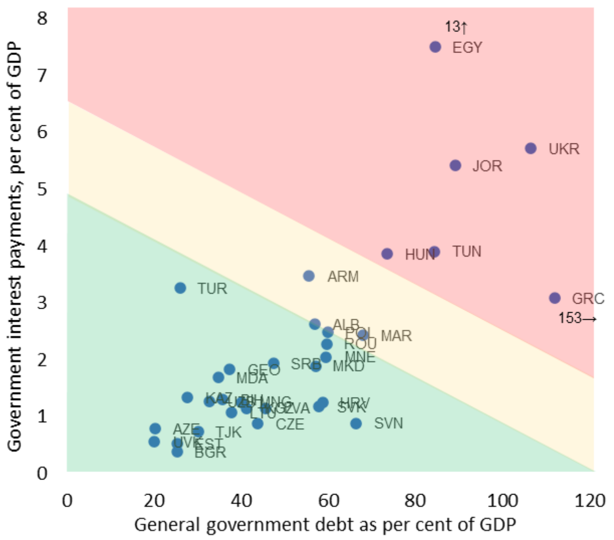
Chart 23. On average, in the EBRD regions, the median yield increased by 2.4 ppt since the start of the war on Ukraine



Source: Bloomberg and authors' calculations.
Note: Spread between the German 5-year bond and median government bond in EUR or USD of maturity between 4 and 7 years. EU-EBRD includes Bulgaria, Croatia, Czechia, Estonia, Hungary, Latvia, Lithuania, Poland, the Slovak Republic, and Slovenia.

Significant fiscal vulnerabilities remain in a number of economies in the EBRD regions—characterised by high government interest payments as a share of GDP and/or high public debt as a share of GDP. These are expected to be highest in Egypt (with interest payments of 13 per cent of GDP), Ukraine, Jordan, Tunisia, Hungary, and Greece (see Chart 24).

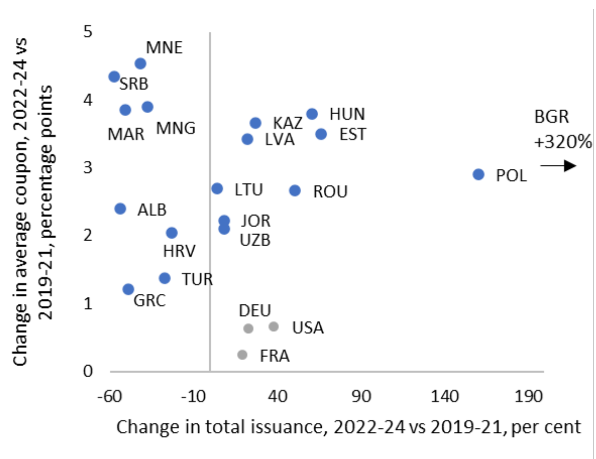
Chart 24. Substantial fiscal vulnerabilities in parts of the southern and eastern Mediterranean, Ukraine, Hungary and Greece



Source: IMF World Economic Outlook October 2024 and authors' calculations.
Note: IMF projections for 2025. Data not available for Lebanon.

Some economies, in particular Mongolia, Morocco, Montenegro and Serbia, faced higher interest rates and reduced Eurobond issuances in 2022-24 compared with 2019-21 (see Chart 25).

Chart 25. Mongolia, Morocco, Montenegro and Serbia faced higher rates and lower issuances in 2022-24 relative to 2019-21



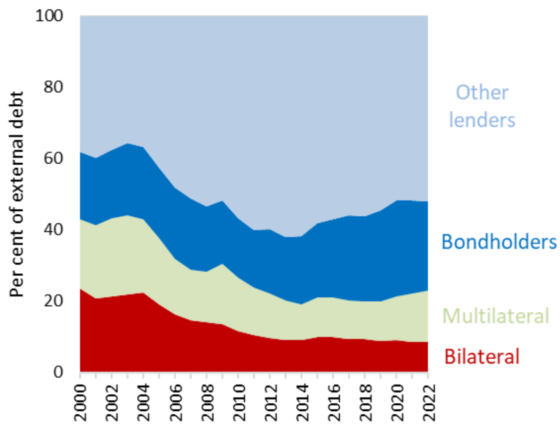
Source: Refinitiv Eikon and authors' calculations.

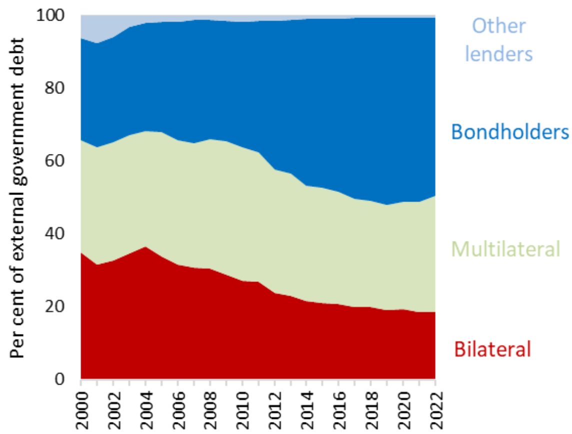
More generally, the structure of external debt has been shifting. Bond issuance has become more important relative to bilateral and multilateral government debt, both as shares of total external debt and total external government debt of emerging markets and low-income economies (see Chart 26). As a result, the fiscal accounts of lower-income economies may be more exposed to pressures emanating from policy uncertainty and market volatility than previously (see also IMF 2025).

While bilateral debt, in particular the rise of non-Paris Club lenders such as China, India and Saudi Arabia has been the subject of increased attention, it has been declining as a share of total debt outstanding. It still tends to account for higher shares of both total government debt and external debt in lower-income economies. On the other hand, higher levels of government debt are not associated with higher shares of bilateral and multilateral debt in total debt outstanding.

In the EBRD regions, China and Japan are key creditors for Central Asian economies; Gulf Cooperation Council economies are becoming more important for the southern and eastern Mediterranean and, alongside China, for the Western Balkans. In turn, the relative shares of EU economies and Russia are shrinking. Bilateral loans account for large shares of total external debt in Egypt (28 per cent, with bilateral loans from the Gulf Cooperation Council economies, as well as China, Germany, Japan, France, and Russia) and the Kyrgyz Republic (23 per cent, with China as the largest creditor). Bilateral loans account for 64 per cent of total external debt in Turkmenistan (with Japan as the largest creditor) but Turkmenistan's overall external debt remains low. Jordan, Morocco and Tunisia have high debt ratios but modest shares of bilateral debt.

Chart 26. Bonds have become more important globally as a share of total debt of emerging markets and low-income economies





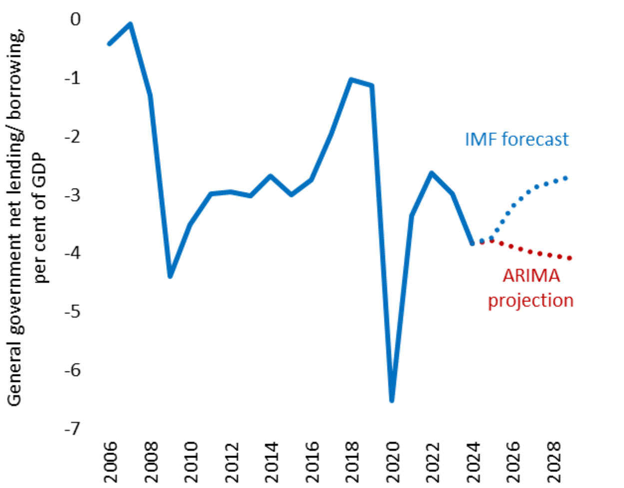
Source: World Bank International Debt Statistics and authors' calculations.
Note: Based on 122 low- and middle-income economies reporting to the World Bank Debtor Reporting System.

Fiscal projections

Looking forward, despite substantial fiscal pressures, the IMF expects average debt in the EBRD regions to remain stable at around 52 per cent of GDP over the period 2025-29. Zooming in on EBRD subregions, debt-to-GDP is expected to edge up in EU-EBRD economies, the Western Balkans and Central Asia but is forecast to decline in the southern and eastern Mediterranean and eastern Europe and the Caucasus.

Based on extrapolations of historical series, these projections appear to assume significant new fiscal measures on the part of governments. A continuation of historical spending and revenue patterns (estimated by fitting an autoregressive integrated moving average model, ARIMA, which uses lagged moving averages to smooth time series data and predicts future values based on past values, see Box 3 for details) could result in cumulative fiscal deficits over the period 2025-29 that are 4.5 percentage points of GDP larger than projected (see Chart 27). These differentials arise across all EBRD subregions except Central Asia.

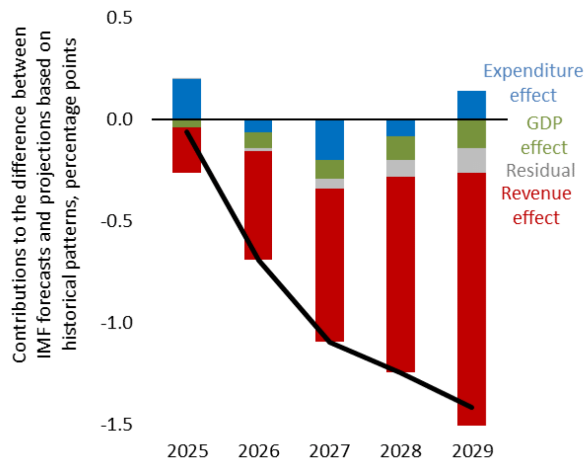
Chart 27. Based on extrapolations of historical series, medium-term fiscal projections of the IMF appear to assume significant new fiscal measures on the part of governments.



Source: IMF World Economic Outlook October 2024 and authors' calculations.
Note: General government revenue, total expenditure, and GDP in national currency converted to real terms using the GDP deflator. Observations prior to 2025 (excluding 2025) used as a training set to fit an ARIMA model to generate five-year forecasts. Simple averages across fiscal balances as shares of GDP in the EBRD regions.

Ambitious revenue projections relative to recent trends account for around 84 per cent of these differentials (see Chart 28). IMF forecasts also expect spending to be in line with historical trends – with higher spending on defence (see Box 4), industrial policies (see EBRD 2024) and interest payments thus expected to be financed by cutting expenditure elsewhere.

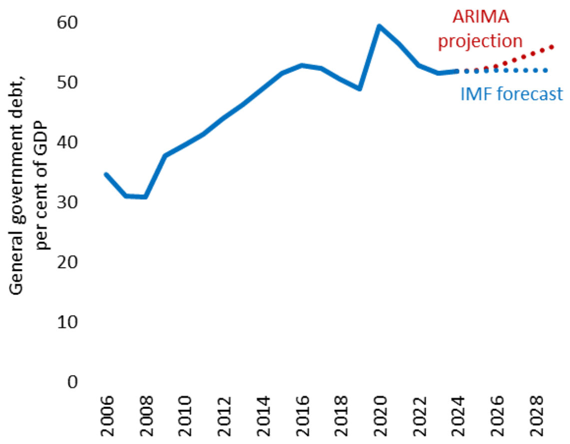
Chart 28. Smaller deficits reflect ambitious revenue projections relative to recent trends coupled with unchanged total government spending



Source: IMF World Economic Outlook October 2024 and authors' calculations.
Note: The black line shows the difference between the total fiscal deficit projected using the ARIMA model and the IMF-projected deficit for a simple average across the EBRD regions. The bars show the average contribution of each component to the fiscal balance ([revenue – total expenditure] / GDP), derived using a first-order Taylor series approximation (all higher-order effects are captured in the residual term).

In a scenario where implicit fiscal measures fail to materialize, the debt-to-GDP ratio might be 4.1 percentage points higher in 2029 than currently projected (see Chart 29), with the largest additional increases in debt in eastern Europe and the Caucasus (notably Ukraine) and the southern and eastern Mediterranean.

Chart 29. In a scenario where implicit fiscal measures fail to materialize, the debt-to-GDP ratio might be 4.1 percentage points higher in 2029 than currently projected



Source: IMF World Economic Outlook October 2024 and authors' calculations.
Note: Each year, the previously calculated deficit ratio (as a share of GDP) is multiplied by the nominal GDP series. The resulting additional nominal debt is added to the nominal debt figure for that year, along with all additional debt accumulated since 2025.

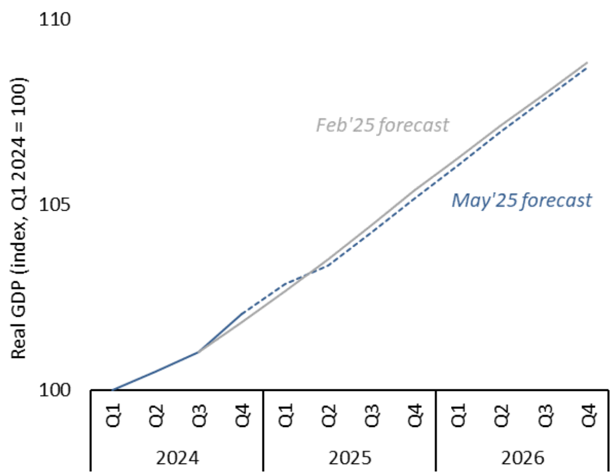
Output in the EBRD regions is expected to grow by 3 per cent in 2025 and 3.4 per cent in 2026

Global growth has been revised down by 0.5 percentage point relative to January 2025 according to the International Monetary Fund's (IMF) April 2025 *World Economic Outlook*. Downward revisions were broad-based, including for the United States (0.9 percentage points), China (0.6 percentage points) and the Euro area (0.2 percentage points, including 0.3 percentage points for Germany) on new import tariff announcements as well as the unpredictability with which events surrounding tariff measures have been unfolding.

Against this backdrop, the 2025 growth projection for the EBRD regions has been revised down by 0.2 percentage points relative to the February 2025 forecast (with a weaker-than-expected second quarter more than offsetting a stronger-than-expected first quarter). Growth is now expected to average 3 per cent in 2025 (see Table 1 and Chart 30). Growth projections have been revised down for almost all economies, with the largest downward revisions for central Europe and the Baltic states (in particular for the Slovak Republic and Hungary, both expected to be heavily impacted by new US tariffs) and the Western Balkans, on weak external demand (see Chart 31).

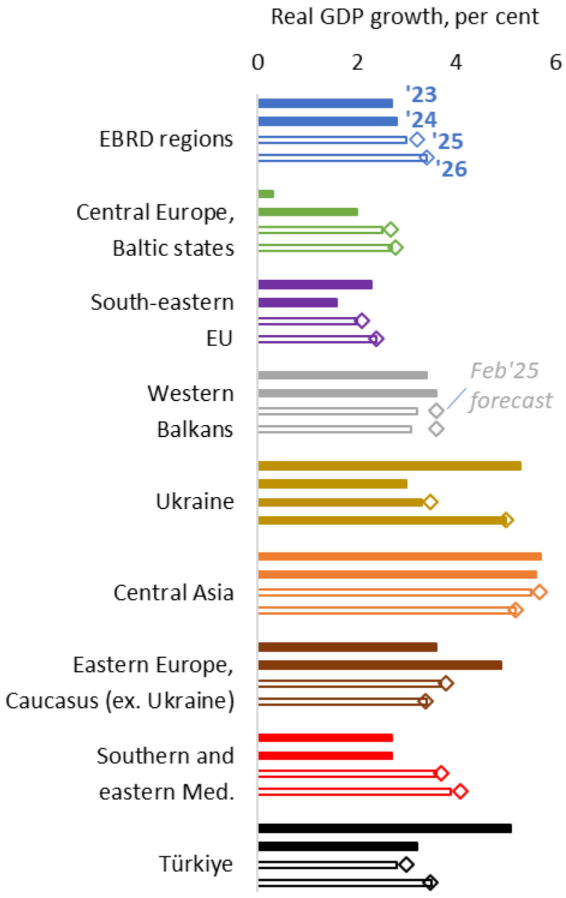
Average growth in the EBRD regions is expected to pick up to 3.4 per cent in 2026, unchanged relative to the February 2025 forecast.

Chart 30. Forecasts of growth in the EBRD regions in 2025 have been revised down by 0.2 ppt since February 2025



Source: National authorities via CEIC and EBRD forecasts.
Note: EBRD average based on the values of gross domestic product in 2022 in current US dollars from the IMF. Growth in 2024 was forecast at 2.8 per cent in September 2024; the preliminary estimate in February 2025 was 2.7, reflecting revisions to historical data growth is now estimated at 2.8 per cent.

Chart 31. Growth in the EBRD regions is expected at 3 per cent in 2025 and 3.4 per cent in 2026



Source: National authorities via CEIC and EBRD forecasts.
Note: EBRD average based on the values of gross domestic product in 2022 in current US dollars from the IMF.

Regional outlooks

Growth in **central Europe and the Baltic states** picked up from 0.4 per cent in 2023 to 2.1 per cent in 2024 as economies gradually adjusted to a lower supply of Russian gas and higher energy prices following Russia's invasion of Ukraine. Growth is expected at 2.4 per cent in 2025 and 2.7 per cent in 2026. Forecasts for both years have been revised down relative to February 2025 on the direct and indirect impact of new tariffs, increased global policy uncertainty and weaker external demand, in particular from Germany, despite Germany's shift towards more expansionary fiscal policy.

Growth in the **south-eastern EU** decelerated from 2.3 per cent in 2023 to 1.6 per cent in 2024 on sluggish external demand, a slowdown in investment and more modest fiscal stimulus. Growth is expected to pick up to 2 per cent in 2025 (less than previously expected, despite domestic demand boosting growth in Bulgaria) and 2.4 per cent in 2026.

Growth in the **Western Balkans** is expected to slow from 3.6 per cent in 2024 to 3.2 per cent in 2025 and 3.4 per cent in 2026. Downward revisions reflect slower growth in advanced Europe as well as political instability in Serbia.

Growth in **Central Asia** moderated from 5.7 per cent in 2023 and 5.6 per cent in 2024 and is expected at 5.5 per cent in 2025 and 5.2 per cent in 2026. Downward revisions in 2025 in Kazakhstan and Mongolia in large part reflect lower expected commodity prices.

In **eastern Europe and the Caucasus**, growth slowed from 4.5 per cent in 2023 to 3.9 per cent in 2024 as the boost from intermediated trade and inflows of labour and capital to the economies of the Caucasus waned. Growth is expected to moderate further to 3.5 per cent in 2025 before picking up to 4.3 per cent in 2026. The 2025 growth forecasts for **Moldova** and **Ukraine** have been revised down on weaker external demand from the EU while Russia's attacks on Ukraine's energy infrastructure continued to weigh on economic activity.

In **Türkiye**, growth moderated from 5.1 per cent in 2023 to 3.2 per cent in 2024 on tighter monetary policy aimed at bringing down persistently high inflation. Growth is expected to moderate further to 2.8 per cent in 2025 before picking up to 3.5 per cent in 2026. The downward revision for 2025 reflects lower domestic and external demand and tighter-than-expected monetary policy.

Growth in the **southern and eastern Mediterranean** is expected to pick up from 2.7 per cent in 2023 and 2024 to 3.6 per cent in 2025 and 3.9 per cent in 2026. Forecasts for both years have nonetheless been revised down relative to February 2025 reflecting the impact of conflicts (through trade and confidence channels) and increased global policy uncertainty.

Risks to the outlook

The outlook for growth in the EBRD regions is subject to numerous risks. These relate to the unprecedented levels of economic policy uncertainty globally, further escalation of geopolitical tensions and trade wars, a potentially greater effect of uncertainty on investment; as well as sharper-than-expected slowdowns in key trading partners such as Germany and China. They could also include renewed inflationary pressures driven by elevated levels of government spending and high nominal wage growth in selected advanced economies as well as the EBRD regions. Extreme weather events such as droughts or floods also continue to present a risk for many economies.

Box 1. Potential impact of increases in US import tariffs on economies in the EBRD regions

This box examines the joint impact of increases in US import tariffs that became effective in 2025 (up to mid-April) for economies in the EBRD regions and select comparators: the 25 per cent tariffs on steel, aluminium and cars and the 10 per cent increases in blanket tariffs.[1] These new tariffs are estimated to push the expected average effective US tariff on imports from the EBRD regions from 1.8 per cent in 2024 to 10.5 per cent (based on the 2024 composition of trade). In the EBRD regions the largest direct negative impact of tariff increases on GDP is estimated for the Slovak Republic (0.8 per cent of GDP), Jordan (0.6 per cent) and Hungary (0.4 per cent). Tariffs on cars account for 83 per cent of the overall impact in the Slovak Republic and 41 per cent in Hungary. These effects could be propagated further through global value chain linkages, including to economies with limited direct trade links to the US. They could be mitigated by trade diversion due to relative tariff rate changes whereby economies facing lower relative tariff rates than their competitors in the US market could gain market shares.

The US increased tariffs on imports from China by 10 per cent on 1 February 2025 followed by another 10 per cent increase on 4 March 2025. In response, China imposed a 15 per cent tariff on selected US goods, including agricultural goods.

Effective 12 March 2025, the US raised tariffs on steel and aluminium entering the US to 25 per cent for all countries. Since 2018, 25 per cent tariffs on steel and 10 per cent tariffs on aluminium applied to many trading partners but the EU, Brazil, Canada, Mexico, and South Korea, among others, subsequently received exemptions. In response, the EU announced plans to reinstate tariffs originally imposed in 2018 and 2020 but these have not yet been implemented as of mid-April.

On 26 March 2025, the US announced 25 per cent tariffs on all car imports and these became effective from 2 April. For Canada and Mexico cars and trucks were not previously subject to import tariffs, while the typical current tariff for other economies was 2.5 per cent for passenger cars and 25 per cent for trucks.

On 2 April 2025, the US announced a 'baseline' 10 per cent tariff on imports into the US from most economies that was set to go into effect on 5 April 2025 as well as 'reciprocal tariffs' on 60 economies that were set to go into effect on 9 April 2025. The rates for the latter corresponded to half of the US trade deficit with the country divided by the country's exports to the US. These tariffs would not affect steel and aluminium articles and cars already subject to tariffs. Further exemptions included copper, pharmaceuticals, semiconductors, lumber articles, certain critical minerals, energy and energy products. No additional tariffs were announced for Canada and Mexico, other economies missing from the new list included Belarus, Burkina Faso, Cuba, North Korea, Russia and Somalia.

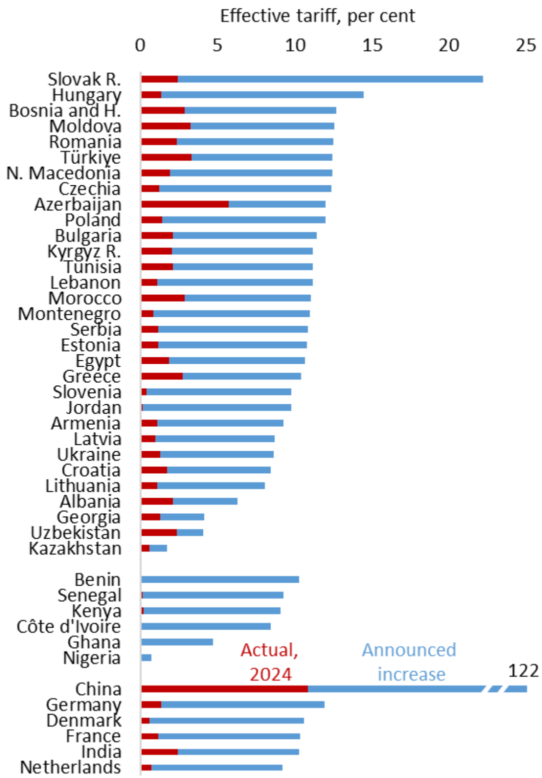
On 9 April 2025, these 'reciprocal' tariffs were announced to be paused for 90 days, until July, for all economies except for China. These economies now face 10 per cent tariff increases. The US tariff on China increased by 125 per cent.

[1] As the details of the implementation of new tariffs and their relationship with existing tariffs and exemptions remain unclear, this note assumes US tariffs increase *by* 125 per cent for China, *by* 10 per cent for other economies and *to* 125 per cent for Chinese tariffs on US goods. It remains unclear how new tariffs might interact with free trade agreements (FTAs) where these are in place—this box assumes that any provisions in the FTAs will be overwritten as per Annex I of the Executive Order. Given uncertainties surrounding further exemptions for smartphones and computers (as announced on 11 April 2025), the overall analysis does not incorporate these, but their potential impact is highlighted separately in Chart 1.2. Tariffs on steel, aluminium and cars are assumed to increase *to* 25 per cent (including for China). The estimates do not incorporate the spillover effects from tariffs imposed by other economies, including China's tariffs on US goods. Given their very limited trade links with economies in the EBRD regions, Canada and Mexico are not included in this analysis.

The China tariff on the US also increased by 84 per cent, then further to 125 per cent on 11 April 2025. China also introduced export controls on critical raw materials (see also EBRD 2023 on the geography of production and global trade in critical raw materials).

The new tariffs are estimated to push the average expected effective US tariff on imports from the EBRD regions from 1.8 per cent in 2024 to 10.5 per cent (based on the 2024 composition of trade and taking exemptions into account, for instance, for energy and pharmaceuticals, see Chart 1.1). In the EBRD regions, the Slovak Republic and Hungary would face the highest effective US import tariffs. In contrast, in 2024, effective US import tariffs were highest for Azerbaijan, Türkiye and Moldova.

Chart 1.1. Effective US tariffs faced by select economies are projected to increase sharply



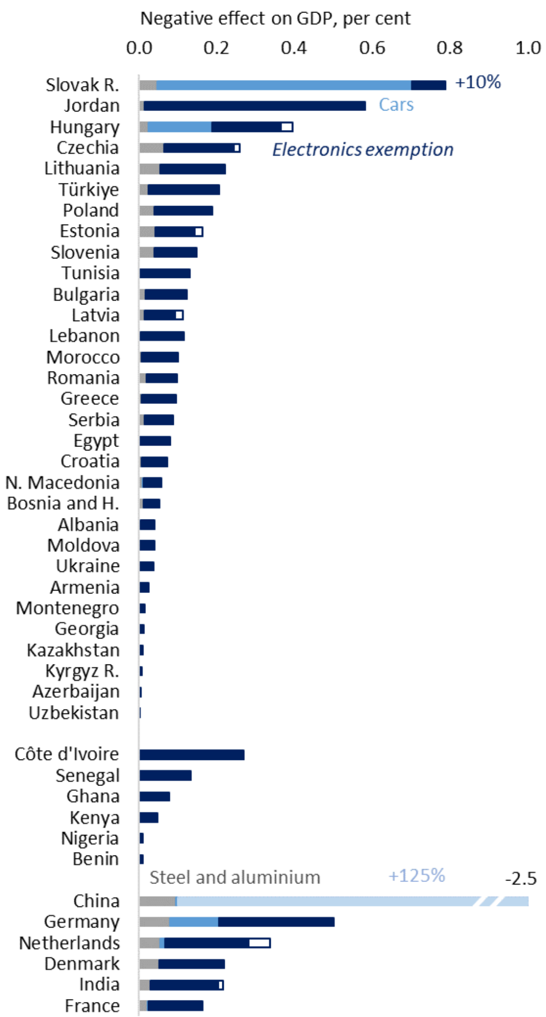
Source: United States International Trade Commission (USITC), UN COMTRADE, White House and authors' calculations.
Note: For 2024, the effective US tariff is calculated as import duties collected by the US in 2024 divided by total imports for consumption (goods that have been cleared through customs). Azerbaijan in 2024 is driven by exports of aluminium to the US which were already subject to a high tariff rate in 2024. The increase in effective tariffs is estimated based on existing HS6-level exports to the US dividing duties collected from newly announced tariffs by total imports. Estimates account for exemptions as listed in Annex II of the Executive Order. Selected comparators shown.

Chart 1.2 shows the potential direct effects of the proposed tariffs assuming a 10 per cent increase in prevailing tariffs (and a 125 per cent increase in tariff for China) and taking exemptions into account (for instance, for energy and pharmaceuticals). Different sectors have varying elasticities of import demand to tariffs: for instance, demand for textile products is relatively elastic (that is, it falls sharply in response to higher tariffs) while demand for commodities such as oil or gas is inelastic, responding less to price changes. The estimate of the impact of tariffs relies on import demand elasticities at the HS6 level of disaggregation (6-digit level of the Harmonized System), the highest level of disaggregation of products that is fully internationally comparable and includes items such as sparkling wines or laptops.

The analysis points to the largest total effects in the EBRD regions for the Slovak Republic (0.8 per cent of GDP), Jordan (0.6 per cent) and Hungary (0.4 per cent). The overall impact on Germany is estimated to be around 0.5 per cent of GDP. The overall impact on China is estimated to be around 2.5 per cent. In this scenario, around 13 per cent of its exports to the US would remain (equivalent to 0.4 per cent of China's GDP). In addition to aluminium, steel and car exports (together accounting for over half of the remaining 13 per cent of exports, almost entirely driven by aluminium), these are goods that are highly inelastic to tariffs including, for instance, seats, brooms and mops, and headgear. While it remains unclear which tariffs would apply to China's car exports, even assuming 125 per cent tariffs, the impact of car tariffs would be negligible (around 0.01 per cent of China's GDP).

Exemptions for smartphones and computers from the 10 per cent tariff increase (announced on 11 April 2025 and as listed in CSMS # 64724565) would have the largest mitigating impact in the EBRD regions for Czechia, Estonia, Hungary and Latvia, but they would only reduce the GDP impact by around 0.02 percentage points on average (these exemptions are shown as hollow bars in Chart 1.2). For China, these exemptions would reduce the overall impact from 2.5 to 2 per cent of GDP.

Chart 1.2. Potential direct effects of proposed tariff increases on GDP



Source: Kee, Nicita and Olarreaga (2008, 2009), UN COMTRADE, White House and authors' calculations.
Note: Based on HS6-level elasticities. For steel and aluminium products, passenger cars and trucks tariffs are assumed to increase to 25 per cent. Steel and aluminium products are based on actual tariff schedules for HS8 goods aggregated at the HS6 level. For China tariffs are assumed to increase by 125 per cent. For all other economies shown, tariffs are assumed to increase by 10 per cent. Where elasticities were missing in Kee, Nicita and Olarreaga (2008, 2009) the median elasticity of around -1 is used. If these lines are instead omitted from the analysis, impacts are somewhat smaller. The demand shock for a particular HS6 product is capped at 100 per cent of existing exports. The estimates shown as dark blue bars (and light blue for China) account for exemptions as listed in Annex II of the Executive Order. Selected comparators shown.

For the **Slovak Republic** and **Hungary**, exports to the US (primarily cars, car parts, batteries, and in the case of Hungary electronics) account for 3 to 4 per cent of GDP though the US only accounts for around 4 per cent of total exports. For car and battery exports, the US accounts for around 7 to 12 per cent of total exports, similar to the exposure for the car industry in Germany. Previously announced tariffs on cars account for 83 per cent of the estimated overall effect of tariffs on the Slovak Republic's output and 41 per cent of the effect on Hungary. The impact of the tariffs would exacerbate broader challenges faced by the car industry (see Box 2), where employment has been already declining and global car production has been shifting towards Asia.

Jordan has historically had close links to the US including a free-trade agreement (FTA) signed in 2000 and in force since end-2001, granting duty-free status to nearly all Jordanian exports to the US. Rules of origin condition duty-free entry of goods on a minimum Jordanian content of 35 per cent. The FTA supported the textile industry, with US firms such as Walmart and Target establishing factories in Jordan. Exports to the US (mostly jewellery and garments) are high both as a share of GDP (5.7 per cent) and as a share of all exports (around 23 per cent), resulting in a trade surplus of 2.4 per cent of GDP with the US. Its next largest trading partners, India and Saudi Arabia only account for around 14 and 11.5 per cent of exports respectively. For textiles and jewellery, the US accounts for 81 and 97 per cent of total exports respectively—comparable to the exposures for car production in Mexico and Canada’s oil. This exposure is exacerbated by high dependence on US foreign assistance (3.4 per cent of GDP in 2023) and a difficult external environment with wars in Gaza and Lebanon weighing on business and consumer confidence.

In sub-Saharan Africa, potential effects would be largest in Côte d’Ivoire (exporting cocoa to the US) and Senegal (mostly textiles). Beyond the potential direct economic impact of tariffs, economies in sub-Saharan Africa face the risk of a possible suspension of the African Growth and Opportunity Act (AGOA). Enacted in 2000, it has given over 30 African economies (including Benin, Côte d’Ivoire, Ghana, Kenya, Nigeria and Senegal) tariff and quota-free access to the US market. Unless renewed, the law underpinning AGOA will expire in September 2025. AGOA is seen as a major tool of US soft power on the continent. According to surveys, it has been the most popular US policy across much of Africa, second only to the programme which directed billions of dollars toward HIV/AIDS treatment and prevention.

Indirect effects through value chains and changes in relative tariff rates

The estimates above are derived from a detailed breakdown of exports to the US and do not take into account spillovers through value chains or redirection of trade.

For instance, in the estimates above, the Slovak Republic is assumed to feel the entire negative impact of fewer cars exported to the US without netting out potentially reduced imports of car components from other countries. In contrast, the direct effect for Kazakhstan is small given the exemption for energy. At the same time, indirect effects may be larger if global demand for energy softens and prices fall.

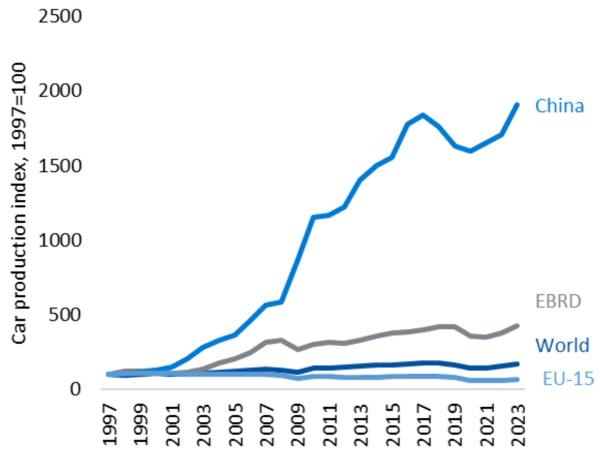
Changes in relative tariffs could also result in shifts in US demand from foreign producers facing higher tariffs to foreign producers facing lower tariffs. For instance, while facing headwinds from higher tariffs on its exports to the US, Jordan could at the same time benefit from a greater differential between tariffs applied on imports from Jordan and imports from China in the US market. Currently around 30 per cent of US textile demand is met by China (and another 30 per cent by domestic producers) while Jordan currently accounts for less than 1 per cent of the US textile market.

Box 2. Shifting global car production

This box examines shifts in global car production. While car production in the US, advanced Europe and Czechia, the Slovak Republic and Poland has declined since 2019, China, India as well as Morocco and Uzbekistan saw substantial gains.

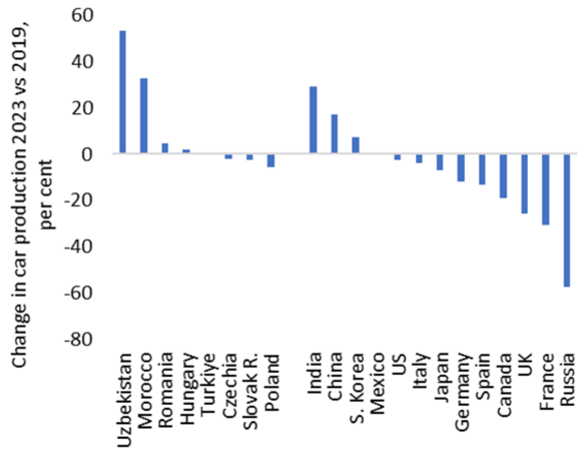
Over the past decades, global car production has been shifting towards Asia, with large increases in output in India, China and South Korea, while in advanced Europe, Japan and the US car production declined (see Charts 2.1, 2.2 and 2.3). In the EBRD regions, Uzbekistan and Morocco saw substantial gains between 2019 and 2023, while Czechia, the Slovak Republic and Poland saw their car production decline.

Chart 2.1. Global car production has been shifting towards Asia



Source: CEIC, International Organization of Motor Vehicle Manufacturers and authors' calculations.

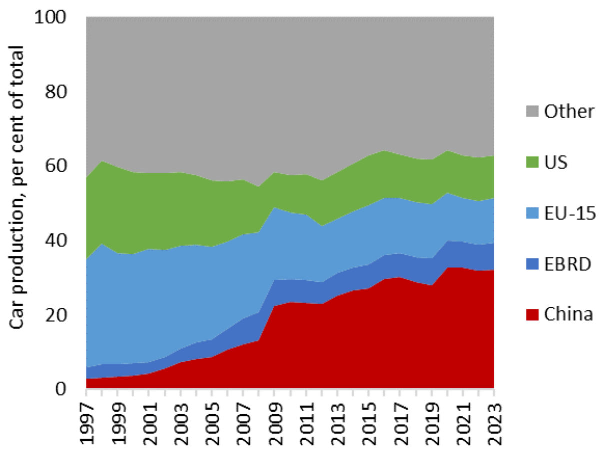
Chart 2.2. Car production declined in advanced economies in 2019-23



Source: CEIC, International Organization of Motor Vehicle Manufacturers and authors' calculations.

China's share in global car production rose from 3 per cent in 1997 to 32 per cent in 2023 (see Chart 2.3). The shares of advanced Europe and the US declined from 51 per cent to 23 per cent. The share of the EBRD regions rose from 3 per cent to 7 per cent.

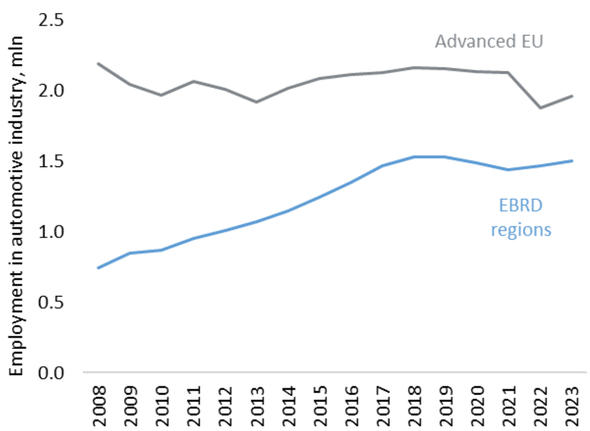
Chart 2.3. China's share in global car production increased 10-fold 1997-2023



Source: CEIC, International Organization of Motor Vehicle Manufacturers and authors' calculations.

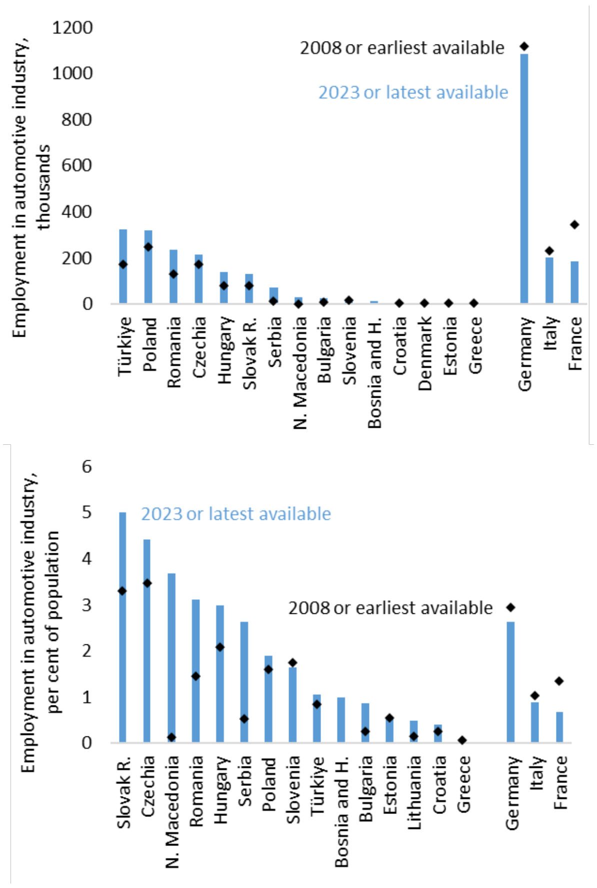
The share of the population employed in the automotive industry has declined in advanced European economies from around 0.9 per cent in 2008 to 0.8 per cent in 2023. In the EBRD regions, it increased from around 1.5 per cent in 2008 to around 2 per cent in 2023. Employment in the automotive sector reached up to 5 per cent of the population in some economies in central Europe, in particular in the Slovak Republic and Czechia. As of 2023, the automotive industry employed 1.5 million people in the EBRD regions and 2 million people in advanced European economies—of these, around 1 million in Germany and over 300,000 each in Poland and Türkiye (see Charts 2.4 and 2.5).

Chart 2.4. Employment in the automotive industry has increased in the EBRD regions



Source: Eurostat and authors' calculations.
Note: Simple averages across unbalanced panels of 12 to 15 economies in advanced EU and 10 to 17 economies in the EBRD regions.

Chart 2.5. Around 1 million people in Germany and over 300,000 each in Poland and Türkiye work in the automotive industry



Source: Eurostat and authors' calculations.

Box 3. Implicit assumptions underpinning fiscal projections

Despite substantial fiscal pressures, the IMF expects average debt in the EBRD regions to remain stable at around 52 per cent of GDP over the period 2025-29. Based on historical trends, these projections appear to assume significant fiscal measures on the part of governments both on the revenue side and on the expenditure side. Likely higher spending on defence, industrial policies and interest payments is implicitly expected to be financed by cutting expenditure elsewhere.

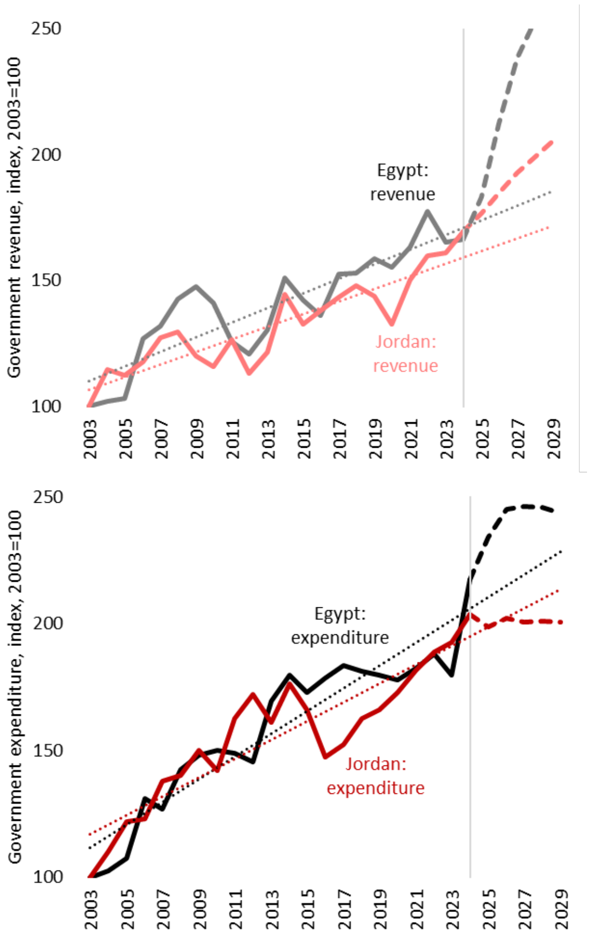
Fiscal projections published in the *World Economic Outlook* of the IMF anticipate medium-term fiscal consolidations across many economies in the EBRD regions, with shrinking fiscal deficits and a stabilisation of general government gross debt as a share of GDP at around 52 per cent for the EBRD regions as a whole.

This box explores how fiscal trajectories would evolve under an alternative scenario in which government expenditure, revenue, and GDP continue along their historical paths and thus derives estimates of fiscal measures implicitly embedded in fiscal forecasts.

To construct these counterfactual projections, an autoregressive integrated moving average (ARIMA) model was estimated for government expenditure, revenue, and GDP for each country. Data were obtained in national currency and current prices from the IMF's October 2024 *World Economic Outlook* database and deflated using country-specific GDP deflators. The models were trained on data through 2024, and projections for 2025–29 were generated using the fable package in R. The order of integration was selected using the KPSS (Kwiatkowski–Phillips–Schmidt–Shin) test, while autoregressive and moving average terms were chosen based on the Akaike Information Criterion.

Chart 3.1 illustrates this analysis for Egypt and Jordan, economies with significant fiscal vulnerabilities. In both cases, fiscal forecasts assume significant increases in revenue relative to the recent trends. In Egypt, an increase in expenditure relative to trend is also implicitly assumed, while in Jordan expenditures broadly follow the trend.

Chart 3.1 Government expenditure and revenue projections in Egypt and Jordan



Source: IMF World Economic Outlook October 2024 and authors' calculations.
Note: In constant prices. Dashed lines denote 2003-2024 trends.

This type of analysis is repeated for each economy. In each case, the estimated differential between the projected path and the trend path derived from historical data is multiplied by the first derivative of the fiscal balance ratio with respect to the variable in question (expenditure, revenue of GDP). This yields a decomposition of the overall difference between projected levels of the fiscal balance and levels based on ARIMA extrapolations.

Government revenue projections make the largest contribution to the difference between the projected fiscal balance and the balance that could be expected based on historical trends. The IMF forecasts thus imply substantial fiscal measures aimed at raising revenue levels in the EBRD regions relative to the no-policy-change scenario. Spending trajectories look broadly in line with historical patterns. This implies that, for instance, any increased spending on defence (see Box 4), industrial policies (see EBRD 2024) and higher interest payments would be offset by reduced spending elsewhere.

Differences in deficits in the two scenarios imply differences in debt ratios. To adjust the IMF-projected debt path, the difference in deficits was multiplied by nominal GDP in each year, and the resulting additional debt stock was added to the previous year's debt and the IMF-projected net debt issuance. The updated debt stock was then divided by projected nominal GDP. The estimates suggest that, by 2029, the debt ratio could be 4 percentage points higher than according to current IMF projections. This is a conservative estimate that does not explicitly account for the cost of servicing additional debt.

The analysis highlights the fact that stabilising the average debt ratio at 52 per cent over the next five years will require substantial policy efforts in many economies.

Box 4. Defence industries

Increased geopolitical tensions have prompted many economies in the EBRD regions and beyond to ramp up their defence spending. While US defence companies dominate the global defence production landscape, a 'buy European' defence fund could provide a substantial boost to economies with strong defence-related production capabilities.

The number of state-based conflicts (including intra-state and inter-state conflicts) reached its highest level since 1946. In response to this trend and the two ongoing wars in the EBRD regions, economies across the EBRD regions have been increasing their military spending. Between 2014 and 2023, defence expenditure in the EBRD regions nearly doubled—from around 1.8 per cent of GDP to approximately 3.5 per cent (2.4 per cent of GDP excluding Ukraine; see EBRD 2025).

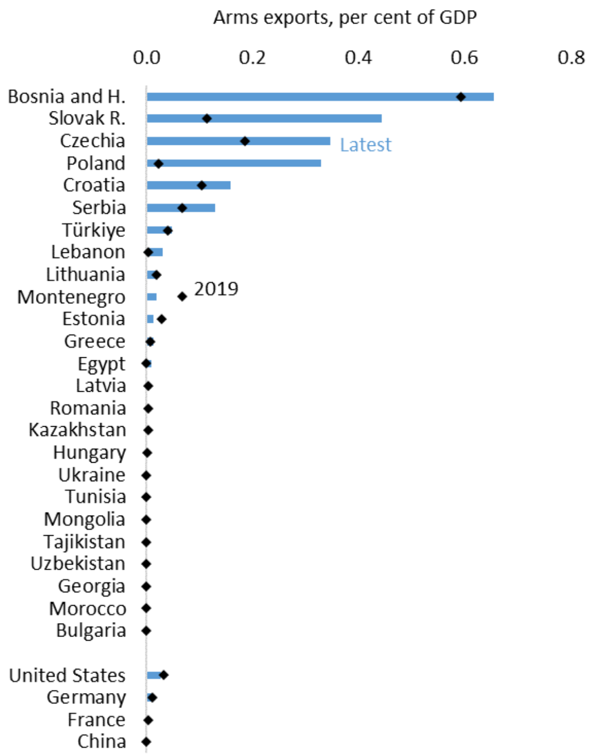
At the EU level, the Readiness 2030 strategy—announced by the President of the European Commission—aims to mobilise up to €800 billion in new defence infrastructure investment. A €150 billion "Buy European" rearmament fund has been proposed to support this effort, with the goal of boosting intra-EU procurement and reducing reliance on external suppliers.

Industrial capacity in defence varies considerably across economies in the EBRD regions. According to the latest available data, arms exports in the regions have risen from 0.05 per cent of GDP in 2019 to 0.09 per cent, with Bosnia and Herzegovina, the Slovak Republic, Czechia and Poland now registering the highest levels of exports (see Chart 4.1).

Expressed in US$ billions, arms exports are highest in Poland (US$ 2.9 billion) and Czechia (US$ 1.2 billion)—compared with US$ 0.7 billion in Germany (Germany's level is similar to those in Türkiye and the Slovak Republic) or US$ 0.1-0.2 billion in China, or France (similar to exports of Croatia and Serbia). These estimates rely on trade values as reported in UN COMTRADE and omit confidential flows and transfers of weapons.

On the other hand, arms transfers data from the Stockholm International Peace Research Institute (SIPRI), point to much higher arms transfers from China, France and Germany, followed distantly by Türkiye and Poland. Those data also account for non-market-based transfers of weapons and are calculated in trend indicator values—a synthetic indicator for military value.

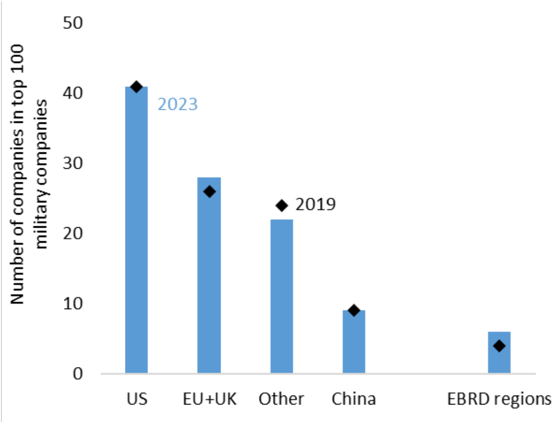
Chart 4.1 Arms exports in the EBRD regions doubled between 2019 and 2024



Source: UN COMTRADE and authors' calculations.
Note: 2024 or latest available. HS 93, 8710, 890610.

US companies dominate the defence production landscape. They account for 41 of the world's 100 largest defence producers, followed by 28 based in the EU and the United Kingdom (see Chart 4.2). Companies in the EBRD regions in the top 100 comprise ASELSAN Türkiye, JSC Ukraine, PGZ Poland, Baykar Türkiye, Turkish Aerospace Türkiye, and Czechoslovak Group Czechia.

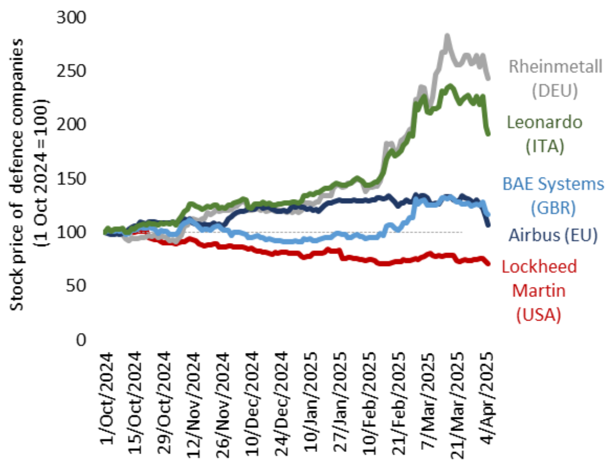
Chart 4.2 US companies dominate the defence production landscape



Source: Stockholm International Peace Research Institute, Yahoo finance and authors' calculations.
Note: Top-100 defined by revenue from the sale of military goods and services specifically designated for military purposes.

At the same time, share prices of major European defence companies have outperformed their US counterparts since the announcement of the EU rearmament fund reflecting investor expectations of increased European-led procurement (see Chart 4.3).

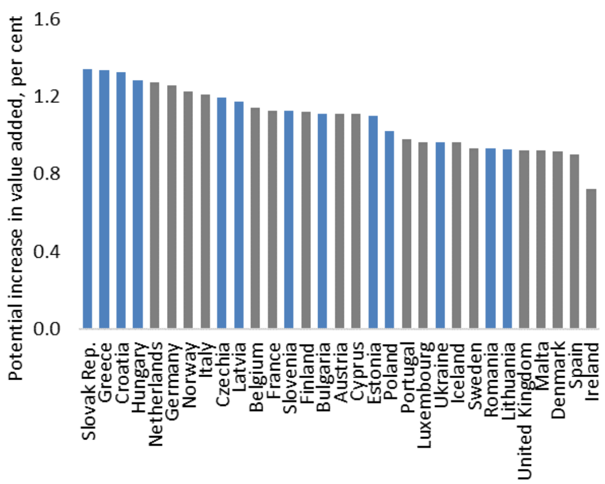
Chart 4.3 Stocks of European defence companies rallied



Source: Stockholm International Peace Research Institute, Yahoo finance and authors' calculations.

Increased defence spending coupled with domestic sourcing could provide a significant boost to output. Chart 4.4 examines the hypothetical impact of a 10 per cent increase in demand for defence-related products from the EEA, UK, and Ukraine—equivalent to roughly US$170 billion—using inter-country input–output tables. This analysis captures the effects of increased demand for output of defence-related sectors—such as electronics, precision engineering, and transport equipment—on other sectors of the economy that provide inputs in defence-related production. The assumed increase in demand could raise global output by an estimated 0.2 per cent. The largest projected short-term gains relative to countries' GDP could accrue to the Slovak Republic, Greece, Croatia, and Hungary, where GDP increases could reach 1 to 1.5 per cent (see Chart 4.4).

Chart 4.4 Increasing demand for defence-related products could provide a significant boost in the Slovak Republic, Greece, Croatia, and Hungary



Source: OECD (2020) Inter-Country Input-Output (ICIO) Tables, 2020, and authors' calculations.
Note: The chart illustrates the potential short-term GDP impact of rising demand for defence-related goods using input–output tables. The scenario assumes that final demand for goods produced by defence-related sectors increases by 10 per cent and that this demand is met by producers in the EEA, the United Kingdom, and Ukraine. The simulated increase in demand is around US$170 billion in current prices. Defence-adjacent products: C25 - Fabricated Metal Products (includes weapons and ammunition manufacturing); C26 – Computer, Electronic and Optical Products (e.g. defence electronics, radar); C28 – Machinery and

Equipment n.e.c. (e.g. specialised military machinery); C30 – Other Transport Equipment (e.g. aircraft, ships, military vehicles); O – Public Administration and Defence. While the sectors assumed to meet this demand are broader than purely defence products, they capture key manufacturing categories relevant to military procurement. Output effects are estimated by multiplying the adjusted demand vector by the Leontief inverse. Gross value added is then calculated as the difference between total output and intermediate consumption.

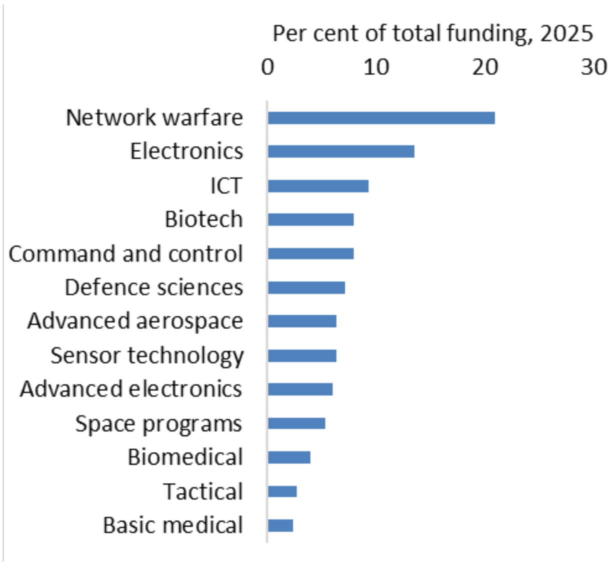
Defence and innovation

Increased defence spending around the world, including in the EBRD regions, has also led to renewed interest in the link between defence spending and innovation. Perhaps the most famous example of such a synergy is the US Defense Advanced Research Projects Agency (DARPA). DARPA (originally ARPA) was launched as a response to the 1957 launch of Sputnik by the USSR which triggered a push to accelerate frontier research in the US. DARPA is best known for its contributions to the development of general-purpose technologies such as the internet (which started as ARPANET), stealth technology, and the global positioning system (GPS). More recently, DARPA provided funding as early as 2013 for the development of mRNA vaccines by Moderna—a technology subsequently used during the COVID-19 pandemic. It also started investing in artificial intelligence and robotics from the early 2000s, launching its first competition between autonomous vehicles in 2004.

While economics research on DARPA remains limited, several studies have found positive effects of similar agencies on innovation and economic growth. Moretti, Steinwender and Van Reenen (2025) found that a 10 per cent increase in public spending on defence-related R&D crowds in an additional 5 to 6 per cent R&D spending by the private sector in the affected industry or firm. Goldstein and Kearney (2024) studied project selection in ARPA-E, the energy arm of ARPA, and found that independent programme directors unconstrained by expert panels allocated funding to more creative research ideas. Yerger (2024) found that over time DARPA shifted away from advanced research and toward shorter-term projects and from entrepreneurial solutions to working with established vendors.

In 2024, DARPA's budget was around US$4.3 billion. In terms of broad areas, IT-related projects accounted for 65 per cent of the total, followed by aerospace (21 per cent), and biology and medicine related projects (14 per cent). Zooming in, the largest share of funding (21 per cent of total) was allocated to network warfare—research aimed at defending or disrupting networked computing systems. Other prominent work streams included electronics, ICT and biotech (see Chart 4.5). In 2025, the largest increases relative to 2024 were observed in basic medical research (showing 96 per cent growth), space technology (67 per cent) and biomedical technology (20 per cent).

Chart 4.5 DARPA funding breakdown



Source: DARPA Justification Books 2021-2025 and authors' calculations.

DARPA divides its research activity into three streams: basic research (fundamental scientific research without a direct practical implementation), applied research (aimed at specific problems), and advanced research (encompassing work on cutting-edge technologies). In 2025, around half of the funding was allocated to advanced research, a third to applied research and the rest to basic research. At the same time, basic research was the only research stream that saw increases in funding (up 11 per cent), while funding for applied and advanced research marginally declined.

DARPA's experience points to three key lessons. First, DARPA invests substantial amounts in fundamental and advanced research, with positive spillovers to other projects, even where direct practical implications of research are not yet spelled out. Second, looking at DARPA's funding plans, current frontier projects combine cyber, space and biotechnology suggesting a broad, inter-disciplinary focus. Third, a key advantage of such agencies may be in their ability to make independent decisions unconstrained by oversight from the rest of the government. Integrating such agencies more closely in civil service structures may result in greater political pressures in project selection at the expense of their innovativeness.

References

EBRD (2023). Transitions big and small, Transition Report 2023-24.

EBRD (2024). Navigating industrial policy, Transition Report 2024-25.

EBRD (2025). Weaker momentum amid fragmenting trade and investment, Regional Economic Prospects, February 2025.

M. Firat and O. Hao (2023). Demand vs. Supply Decomposition of Inflation: Cross-Country Evidence with Applications. IMF Working Paper No. 23/205.

A. Goldstein and M. Kearney (2024). Uncertainty and individual discretion in allocating research funds. National Bureau of Economic Research Working Paper No. w32033.

IMF (2025). Enhancing Resilience amid Uncertainty, Global Financial Stability Report, April 2025.

E. Moretti, C. Steinwender and J. Van Reenen (2025). The intellectual spoils of war? Defense R&D, productivity, and international spillovers. Review of Economics and Statistics, Vol. 107, No. 1, pp. 14-27.

A. H. Shapiro (2022). Decomposing supply and demand driven inflation. Tech. rep. Federal Reserve Bank of San Francisco, San Francisco.

R.H. Yerger Jr (2024). Case study on DARPA: An exemplar for government strategic structuring to foster innovation. Moonshots and the New Industrial Policy: Questioning the Mission Economy, pp. 109-123.

J. Zettelmeyer (2025). What does German debt brake reform mean for Europe? Bruegel Newsletter, 31 March 2025.

Regional updates

Central Asia

Central Asian countries continue to demonstrate strong economic performance, underpinned primarily by domestic demand including public investment. Recent growth has been supported by rising real wages, sustained remittance inflows, and favourable tourism seasons in several countries, which have collectively boosted the services sector. Industrial output has also remained robust across the region. Inflation remains elevated, driven by demand-side pressures, energy tariff adjustments, and, in some cases, currency depreciation against the US dollar. Monetary policy remains tight in response. Fiscal positions deteriorated somewhat in 2024 in most countries. Commodity-exporting economies may face pressure on their external accounts due to global price volatility. The region's economic outlook remains exposed to risks stemming from its dependence on China—particularly in Mongolia, where export concentration is highest. Growing international reserves continue to offer a solid buffer against external shocks.

Kazakhstan

Kazakhstan entered 2025 with strong economic performance, as real GDP grew by 8.3 per cent year on year in the first quarter, driven by the start of the gradual ramp up in production at the expanded Tengiz oilfield in late January. The country will need to balance this increased output with its commitments under the OPEC+ agreement, including compensating for the overproduction since 2024. The April 2025 OPEC+ decision to gradually adjust production volume upward will provide some relief. While growth will continue being supported by the surge in oil production, associated export growth and continued fiscal stimulus, weaker Chinese demand for Kazakh oil, ores, copper and other exports could negatively impact growth, as China remains the second largest export destination. Additionally, elevated inflation and tight monetary policy may eventually dampen consumption. The National Bank of Kazakhstan raised the policy rate further to 16.5 per cent in March and kept it at that level in April, in an effort to stabilise inflation expectations in the context of ongoing fiscal stimulus and robust consumer lending as well as occasional depreciation pressures on the back of volatile oil prices and global uncertainties. Anticipated tax reforms, including a value added tax (VAT) increase, may add to inflationary pressures. However, enhanced revenue mobilisation is expected to contribute to a gradual reduction in fiscal reliance on the National Oil Fund. Real GDP growth is projected at 4.9 per cent in 2025, slowing down to 4.5 per cent in 2026.

Kyrgyz Republic

Strong growth continued into 2025. Real GDP expanded by 10.7 per cent year on year in the first two months, driven by a 14.7 per cent increase in industry and a 17 per cent increase in domestic trade. Investment remained robust, growing by an estimated 13.4 per cent during the same period, supported by high public capital spending backed by strong fiscal revenue growth. Most investments were directed toward the construction of mining facilities, information and communications infrastructure, electricity, gas and steam supply, manufacturing, education, and housing. While external trade remains significantly above its pre-2022 level, its contribution to growth is tapering, with economic momentum now primarily sustained by domestic demand supported by strong remittances, rising wages and expanding credit. Inflation continued to rise, in line with trends in neighbouring economies and reflecting demand-side pressures, reaching 7 per cent in February 2025. The central bank has kept the policy rate unchanged at 9 per cent since May 2024. Gold-based international reserves continued to increase, reaching record highs of US$5.5 billion as of March 2025. Real GDP is projected to grow by 7 per cent in 2025 and 6 per cent in 2026.

Mongolia

Economic growth in 2024 remained robust, though it moderated compared with the previous year. Strong domestic demand was offset by weak net exports, while solid performance in services, mining, and domestic trade outweighed a 29 per cent contraction in the agriculture sector. The current account shifted from near-balance to a 9.3 per cent deficit, driven by a narrowing trade surplus in goods and a widening trade deficit in services. The tugrik remained relatively stable for most of 2024, supported by strong financial inflows, though it experienced some depreciation pressures since late 2024. The fiscal balance recorded a surplus for the fourth consecutive year, though smaller than in 2023. Continued growth in consumption—driven by rising real wages—and investments, particularly in planned large-scale infrastructure projects, alongside a projected recovery in agriculture, are expected to be the main drivers of growth in 2025. However, Mongolia's exceptionally high dependence on a few commodity exports to China—accounting for more than 90 per cent of total exports as of 2024—adds significant uncertainty to export dynamics. In 2024, coal alone accounted for 54 per cent of exports, followed by copper at 21 per cent. Both commodities are highly susceptible to price fluctuations, with coal prices weakening notably since 2024. Coal exports have begun to show signs of strain. Volumes declined by 10.7 per cent in the first quarter of 2025, while export revenues dropped by 42 per cent. Copper exports, by contrast, appear more resilient, buoyed by increasing production from Oyu Tolgoi. In the first quarter of 2025, copper export volumes rose by 24.2 per cent, with revenues up by 45.7 per cent. Given the potential softer demand from China, both external and fiscal balances are likely to face increased pressure. International reserves stood at US$5 billion in March 2025 (down from a peak of US$5.5 billion in December 2024), covering approximately 3.6 months of imports. The currency swap line with China provides additional liquidity assurance. Real GDP is projected to grow by 6.3 per cent in 2025 and 6 per cent in 2026.

Tajikistan

The economy continued to post robust, broad-based growth in 2024, with positive contributions from agriculture, industry and services. Investment remains strong, supported by the ongoing construction of the Rogun dam and other major infrastructure projects. Consumption is also robust, underpinned by sustained remittance inflows and rapid credit expansion, albeit starting from a low base. Inflation remains low and stable, especially when compared with regional peers, at 3.7 per cent in February 2025. The current account surplus widened to 6.1 per cent of GDP in 2024, as strong remittances more than offset the growing trade deficit. Continued monetisation of previously acquired gold has further boosted international reserves, which now cover more than seven months of imports, according to IMF estimates. Fiscal policy remains aligned with the targets under the IMF's Policy Coordination Instrument (PCI) programme. A potential slowdown in China, which accounted for an estimated 14 per cent of Tajik goods exports in 2022, and other key trading partners weighs modestly on the growth outlook. The economy is projected to grow by 7 per cent in 2025 and 5.7 per cent in 2026, supported by ongoing infrastructure investments and remittances.

Turkmenistan

The economy continues to grow robustly, driven by the mining sector, construction, trade and services sectors. Economic activity is supported by credit expansion, rising wages and investment. While both the current account and fiscal balances are estimated to be in surplus, the decline in global commodity prices will negatively impact Turkmenistan's export receipts. Public debt remains negligible. Real GDP is forecast to continue expanding at the rate of 6.3 per cent in 2025 and 2026 as investments in energy, infrastructure, agriculture and food processing continue.

Uzbekistan

The economy grew by 6.5 per cent in 2024, driven by 27.6 per cent investment growth. Robust household consumption—fuelled by strong growth in remittances, credit expansion and rising wages—supported the services sector, which grew by 12.9 per cent. Industry expanded by 6.8 per cent, construction by 8.8 per cent and agriculture by 3.1 per cent. Economic momentum remained strong in early 2025. In the first two months of the year, industrial production grew by 6 per cent, construction by 11.8 per cent, and services by 12.2 per cent compared with the same period in 2024. Inflation peaked in mid-2024 at 10.6 per cent, driven primarily by energy price liberalisation, and has remained elevated, at 10.3 per cent in March 2025. In response, the Central Bank of Uzbekistan maintained a tight monetary policy stance, raising the policy rate by 50 basis points in March 2025 to 14 per cent. Progress on reducing the twin deficits continued. The current account deficit narrowed due to a sharp rise in remittance inflows and a lower deficit in goods trade, while the deficit in services trade increased. On the fiscal side, increased revenues combined with restrained expenditures supported further consolidation. Foreign exchange reserves rose to US$47.9 billion by 1 April 2025, reflecting higher global gold prices. With 7.6 per cent of its exports directed to China in 2024, Uzbekistan faces relatively low direct exposure to a potential slowdown in the Chinese economy. Export volumes rose by 24 per cent in the first two months of 2025. The economy is expected to maintain strong growth, projected at 6 per cent in both 2025 and 2026.

Central Europe and the Baltic states

Increased global trade policy uncertainty will likely negatively impact the economies of the CEB region. Real GDP growth is forecast to reach 2.4 per cent this year before rising to 2.7 per cent in 2026. Increased US import tariffs on cars, aluminium and steel (at 25 per cent) and the 10 per cent tariff increase for other products weigh on the economic outlook. High tariffs on cars and car parts will hit Germany hard, which will negatively affect exporters in the CEB region – both in the automotive industry and more broadly. The escalating trade war risks erasing the positive effects from the easing of fiscal policy in major EU countries and the announced €150 billion EU defence fund, even though high US tariffs on imports from China may somewhat help EU exports to the US. An increase in goods redirected from China to the EU could help reduce inflation. Increased uncertainty regarding the future of trade further weighs on investment. Higher-than-expected demand from Germany and potential nearshoring could present upside risks.

Croatia

The economy is performing robustly, with growth of 3.9 per cent in 2024. Real wage growth of 12 per cent supported a rebound of private consumption, while investment expanded notably backed by EU funds. In addition, expansionary fiscal policy contributed to growth, with the fiscal deficit estimated at 2.1 per cent of GDP in 2024. Real GDP growth is expected to only marginally slowdown in 2025 compared with the previous forecast, to around 2.9 per cent, but downside risks have strengthened with 40 per cent of Croatia’s direct exports to the US being pharmaceuticals, which are vulnerable to a possible introduction of US tariffs on this sector. In 2026, Recovery and Resilience Facility (RRF) funds are again expected to support investment, resulting in output growth of around 2.6 per cent.

Czechia

The economy recorded modest growth of 1.1 per cent in 2024 as a recovery in consumption and positive net exports were offset by a drop in investment and destocking. The economy is highly integrated with Germany, with 60 per cent of exports concentrated in the automotive, electronics and metal sectors. The economic impact of escalating trade frictions on the Czech economy is thus mainly indirect via Germany, while direct exports to the US account for around 2 per cent of GDP. The US tariffs on EU imports imposed as of mid-April 2025 could cut growth by

0.3 percentage points. Real GDP is forecast to grow by 1.6 per cent in 2025 and 2.2 per cent in 2026, subject to upside risks if tariffs on the automotive sector are eased. The negative impact on growth in 2026 will be largely offset by higher fiscal spending in Germany and the EU-level defence spending, with growth opportunities for the Czech defence sector. The upcoming parliamentary election at the end of 2025 could boost spending, putting additional pressure on the budget but supporting near-term GDP growth.

Estonia

After two years of recession, Estonia's economy has embarked on a path of gradual recovery, although the anticipated improvement in economic conditions in advanced Europe risks being offset by the escalating trade tensions. As a small, open economy, where exports accounted for 95 per cent of GDP in 2024, Estonia is vulnerable to increased trade policy uncertainty even if direct trade ties with the US are limited. Although growing more slowly than previously expected, investments and private consumption are projected to remain the main drivers of growth, notwithstanding higher taxes aimed at financing the government's ambitious plan to increase defence spending to 5 per cent of GDP. The so-called defence tax, which envisages a 2-percentage point increase in both income tax and value added tax (VAT) from January 2026 and July 2025, respectively, is now expected to remain permanent, whereas initially, the increases were planned to stay in force until the end of 2028. Real GDP growth is forecast to rise to 1.3 per cent this year and 2 per cent in 2026.

Hungary

The economy is likely to be heavily affected by the additional import tariffs imposed by the US. Exports to Germany account for approximately 18 per cent of GDP, and the increased uncertainty surrounding the outlook in the automotive and battery production sectors could have a paralysing effect on investment decisions. The previously anticipated beneficial impacts of the launch of production this year at the Chinese electric car factory BYD in Szeged and the BMW car and CATL battery factories in Debrecen will likely be delayed until at least 2026. In the medium-term, resources could be redirected from automotive production towards defence manufacturing, provided emphasis on increasing defence spending is sustained. Private consumption is expected to drive growth in 2025 and 2026. Nominal wage growth slowed to around 10 per cent in early 2025 and elevated inflation will hit disposable incomes. Consequently, the central bank is delaying cuts to the main policy rate, currently at 6.5 per cent. In March 2025, the government introduced a 10 per cent profit margin cap on 30 essential foods, effective until the end of May 2025, which is expected to reduce food inflation by 2 percentage points. The spring 2026 parliamentary elections are likely to delay fiscal consolidation, despite the excessive deficit procedure in place. Real GDP growth of 1.5 per cent is expected in 2025 accelerating to 2.7 per cent in 2026.

Latvia

After experiencing a recession in 2024, Latvia's economy has returned to growth this year. While direct exposure to higher US import tariffs is limited, Latvia remains vulnerable to the indirect impact of increased trade policy uncertainty via other EU countries. Private consumption, however, is expected to strengthen in 2025, driven by rising incomes and improved consumer confidence. Investment, in particularly where co-financed by EU funds, including the Recovery and Resilience Facility, is expected to gather momentum. Expanding bank lending to households and businesses is forecast to bolster consumption and, to some extent, investment. In March 2025, the government announced an increase in defence spending to 4 per cent of GDP this year, up from the 3.5 per cent envisaged in the existing budget. This will likely lead to an increase in imports and may constrain fiscal space for social policies. The economy is projected to grow by 1.8 per cent in 2025, accelerating to 2.4 per cent in 2026.

Lithuania

In recent years, Lithuania has deepened its economic links with the US, amid rising foreign direct investment (FDI) and trade flows. Lithuania's direct exports to the US account for around 2.5 per cent of GDP, mostly in commodities, chemicals and services. The direct impact of the increased US tariffs (in place as of mid-April 2025) could cut GDP growth by around 0.2 percentage points, with additional indirect effects via supply chains and weaker global demand. These threats come in the context of higher-than-expected growth in 2024, at 2.8 per cent. Growth was underpinned by a rebound in private consumption after two years of declines. Investment fell in 2024 after three strong years but is expected to recover in 2025. Manufacturing output remained robust in 2024 and early 2025. The planned increase in defence spending towards 5 per cent of GDP by 2026 will widen the fiscal deficit to a planned 3 per cent of GDP this year, further supporting growth. The economy is forecast to grow by 2.6 per cent in both 2025 and 2026, with risks tilted to the upside given the improved outlook for domestic demand.

Poland

The negative impact of the increased US import tariffs on Poland will be mostly indirect, especially through Germany and supply linkages in the automotive sector. Poland's direct trade exposure to the US is small and domestic demand is robust. Slowing inflation and rising real household incomes are expected to sustain private consumption. Accelerated investments, co-financed by EU funds, particularly in infrastructure and energy, are forecast to boost Poland's GDP growth in the short term. Higher private investment is expected in 2026 while the outlook for exports is highly uncertain. Increased spending in the defence sector is expected to continue contributing to GDP growth. Falling commodity prices, including crude oil, along with the anticipated increase in the supply of Chinese products in EU markets, are expected to accelerate the return of inflation to the central bank's target. This creates room for a reduction in the main policy rate, which should stimulate corporate lending and investment. It may also ease the appreciation of the zloty, whose high value could somewhat reduce the competitiveness of Polish exports. Overall, the economy is expected to grow by 3.3 per cent in 2025 and 3.2 per cent in 2026.

Slovak Republic

As the global leader in car production per capita (with 182 cars produced per 1,000 inhabitants last year), the Slovak economy will likely be the hardest hit by the increased US tariffs among EU economies. Since 3 April 2025, a 25 per cent tariff has been imposed on car imports to the US, and from May, the same levy is expected to apply to car parts. The value of Slovak exports to the US amounted to almost 4 per cent of GDP in 2023, with the vast majority being automobiles. The Slovak plants of Volkswagen and Jaguar Land Rover are particularly vulnerable, with the former exporting a quarter of its production to the US market. The central bank estimates that increased trade barriers could jeopardise up to 20,000 jobs in the Slovak Republic and cause a €5 billion shortfall in exports. Beyond the direct impact of US tariffs, the anticipated economic slowdown among key trading partners will also affect its export-driven economy. A diversification towards defence production could partially mitigate these impacts. Taking all these developments into account, real GDP growth is expected to decelerate sharply, to 1.4 per cent in 2025 and 1.8 per cent in 2026. Private consumption is anticipated to continue driving growth despite fiscal consolidation and the increase in the rate of value added tax (VAT) from 20 per cent to 23 per cent in effect from January 2025.

Slovenia

Economic growth slowed to 1.6 per cent in 2024, as recovery in consumption and government spending was offset by negative net exports and a drop in investment. The production of cars further dropped in 2024 and construction also contracted as momentum in the infrastructure sector weakened. Related to this, government spending was lower than the projected 2.4 per cent of GDP, leading to a fiscal deficit of 0.9 per cent of GDP. As a highly open economy, Slovenia will be indirectly affected by higher US import tariffs via their effect on the German and Italian economies. Slovenia's indirect exposure to the US is also notable in the pharmaceutical sector through growing trade with Switzerland in this sector. The US is a key export market for Swiss pharmaceutical companies, posing an important risk to Slovenia if tariffs are raised in this sector. Real GDP is forecast to grow by 1.9 per cent in 2025, as a recovery of public investment offsets the headwinds from US tariff policy. In 2026, economic growth could further increase to 2.3 per cent on higher demand from the EU.

Eastern Europe and the Caucasus

Growth accelerated in 2024 in the Caucasus region, driven by higher real wages, but the effects of inflows of capital and labour from Russia have started to fade, while inflation was more contained than in 2023. Real GDP growth is projected to moderate in 2025 and 2026, reflecting external vulnerabilities and regional instability, but could be strengthened by greater regional trade integration. Signs of economic rebound in Ukraine and Moldova faded in late 2024 while inflation has been rising again. Russian attacks on Ukraine's energy infrastructure and Gazprom's gas cut-off to Moldova's largest power plant will hamper growth in 2025 as well. However, the economy could benefit from external financial support. Inflation is expected to remain elevated in early 2025 but is likely to moderate by year-end.

Armenia

Economic growth in Armenia is moderating towards its long-term potential after two years of rapid expansion. Real GDP grew by 5.9 per cent in 2024, down from 8.3 per cent in 2023 and 12.6 per cent in 2022, reflecting waning inflows of capital from Russia, the diminishing impact of high-skilled Russian migration, and slower growth in trade and ICT services. Meanwhile, inflation remains within the Central Bank of Armenia's (CBA) revised target range of 3 per cent (±1 per cent). Headline inflation accelerated to 3.3 per cent year on year in March 2025, up from an average of 0.3 per cent in 2024, driven mainly by food and utility prices. To support economic activity, in February 2025, the CBA cut its benchmark interest rate by 25 basis points, to 6.75 per cent. This was the 14th rate cut since June 2023, where the rate stood at 10.75 per cent. Real GDP growth is projected to moderate to 5 per cent in 2025 and 4.5 per cent in 2026. The deceleration reflects moderation in domestic demand as the effects of the earlier inflows of capital and labour from Russia dissipate, and the impact of higher US import tariffs on external demand. Public investment, IFI-backed projects, and infrastructure expansion will continue to support economic activity. A potential breakthrough in border negotiations with Türkiye could strengthen Armenia's position in East-West transit and boost regional trade integration. However, geopolitical volatility remains the key downside risk, as delays in finalising peace negotiations with Azerbaijan could undermine economic stability.

Azerbaijan

Azerbaijan's economy grew strongly in 2024, driven by the non-oil sector and public investment. Real GDP expanded by 4.1 per cent in 2024, up from 1.4 per cent in 2023, with non-oil growth reaching 6.2 per cent, compared with 3.7 per cent in 2023. The main non-oil contributors to growth were the construction, ICT, transportation, and tourism sectors. Economic activity was supported by rising real incomes and infrastructure investment, while the oil and gas sector returned to growth in March 2024, as gas production expanded to meet European demand. In the first quarter of 2025, real GDP grew by just 0.3 per cent year on year, compared with 4 per cent in the same period of 2024, as weaker oil and gas sector output offset solid momentum in the non-oil sector. Meanwhile, inflation remained contained, fluctuating between 0 per cent year on year in April 2024 (the lowest level in more than nine years) and 5.9 per cent in March 2025. The recent acceleration was driven by food and services prices, but inflation remains within the target range of the Central Bank of Azerbaijan (CBAR) of 4 per cent (±2 per cent). The CBAR responded to easing inflation pressures in late 2023 by reducing the key policy rate cumulatively by 175 basis points, from 9 per cent in November 2023 to 7.25 per cent by May 2024, and has maintained it at this level since then. Recognising the need for additional measures to manage robust credit growth, which surpassed 20 per cent in 2024, the CBAR announced the activation of a 0.5 per cent countercyclical capital buffer, effective from March 2025. Real GDP growth is projected to moderate to 3 per cent in 2025 and 2.5 per cent in 2026. Growth will be supported by continued expansion in the non-oil economy and sustained public investment. However, the outlook remains highly sensitive to fluctuations in oil and gas prices in the context of increased trade policy uncertainty, weaker external demand and potential setbacks in regional normalisation efforts. In the medium term, trade along the Middle Corridor connecting China to Europe could create opportunities for Azerbaijan's transport and logistics sectors, as peace-building efforts may unlock new trade routes and investment flows.

Georgia

Georgia's economy grew by 9.4 per cent in 2024, surpassing expectations and accelerating from 7.8 per cent in 2023. The ICT, education, public administration, trade and construction sectors drove the expansion, and, despite fading war-related financial inflows and lower Russian migration, domestic consumption remained strong, fuelled by credit growth and wage increases. Meanwhile, inflation remained low in 2024, averaging 1.1 per cent, down from 2.5 per cent in 2023. It started accelerating in October 2024, driven by rising food prices, and reached 3.5 per cent year on year in March 2025, slightly above the National Bank of Georgia's (NBG) target of 3 per cent. The NBG has maintained its policy rate at 8 per cent since May 2024, following a cumulative 150-basis-point reduction earlier in 2024. The NBG's monetary policy stance remains cautious, balancing support for economic growth with reducing external vulnerabilities. The high real interest rate suggests a deliberate attempt to anchor inflation expectations. Real GDP growth is projected to moderate to 6 per cent in 2025 and 5 per cent in 2026, close to the potential growth rate, supported by public infrastructure projects and government-backed initiatives, particularly in the transport, energy, and ICT sectors. Meanwhile, political uncertainty and the suspension of the European Union accession process could drag down export growth and investment, as the one-off effect of migration from Russia fades. Downside risks include weaker external balances and external demand, including because of increased trade tariffs and a deteriorating business environment, and slowing credit expansion.

Moldova

Economic growth decelerated to a mere 0.1 per cent in 2024, driven by an 18.9 per cent decline in agriculture and a 12.6 per cent drop in real exports due to reduced EU and Ukrainian demand. Despite a promising start of the year, the economy fell into recession in the second half of 2024, exacerbated by weak industrial export demand and poor agricultural conditions. At the beginning of 2025, manufacturing and exports remained sluggish, further hindered by disrupted gas supplies from Russia's Gazprom to the unrecognised breakaway region of Transnistria and halted electricity supply from its thermoelectric power plant, necessitating costly electricity imports from Romania. Consequently, retail electricity and heating prices surged by 50 per cent and 25 per cent in January 2025, respectively. This came on top of already accelerating inflation at the end of 2024 due to rising food prices and the scheduled gradual correction of excise goods prices at the beginning of 2025, prompting the central bank to raise the policy rate twice early in 2025, marking the first hikes in over two years. Inflation hit 9.1 per cent in January 2025 but eased slightly to 8.8 per cent by March. The foreign exchange market remains stable thanks to steady official foreign financing. In February 2025, the European Commission granted the country €250 million to offset excess electricity costs for households and social institutions until end-2025, along with aid to vulnerable households and support for agricultural and manufacturing businesses. Combined with the European Commission's Growth Plan for Moldova (€1.9 billion for 2025-2027, including €385 million in grants), these measures aim to bolster the economy. Real GDP growth is projected to reach 1.8 per cent in 2025, rising to 3.8 per cent in 2026.

Ukraine

Real GDP growth fell from 5.3 per cent in 2023 to 2.9 per cent in 2024 due to electricity shortages, weak harvests and acute labour shortages in the economy. While agriculture, energy production, and trade declined, other sectors exhibited solid growth despite challenging conditions and the ongoing Russian war of aggression. Businesses demonstrated resilience and adaptability, which, coupled with the well-functioning Black Sea trade corridor, led to the resumption of export growth after two years of sharp declines. External financing remained at similar levels as in 2023, fully covering the current account deficit and enabling Ukraine to maintain adequate official foreign reserves. The resurgence of inflation in the second half of 2024 was a consequence of rising electricity costs, high real wage increases and the exchange rate depreciation against the US dollar of around 10 per cent since the peg was lifted in October 2023. Inflation stood at 14.6 per cent in March 2025 and is expected to stay elevated in the first half of 2025 but should fall to single digits by year-end. The National Bank of Ukraine responded by raising the policy rate by a cumulative 250 basis points since December 2024, reaching 15.5 per cent in early March 2025. Stable external financing from the EU under Ukraine's Facility and revenue from Russian frozen assets provided by the G7 countries will fully cover external and fiscal deficits in 2025, underpinning macroeconomic stability. The strong stimulus from public consumption and increasing military purchases from domestic industry are expected to support economic growth. However, the recent global trade frictions added additional downside risks to already high uncertainty related to the ongoing Russian war of aggression. Therefore, the real GDP growth forecast has been revised down to 3.3 per cent in 2025. At the same time, the real GDP growth forecast for 2026 is unchanged at 5 per cent, assuming a cessation of hostilities and benefits from post-war reconstruction.

South-eastern EU

Economic growth slowed in 2024, mainly due to a notable deceleration in Romania. While private consumption accelerated on the back of strong wage growth, investment weakened in Bulgaria and Romania, partly due to mounting delays in implementing the Recovery and Resilience Facility (RRF). In contrast, Greece remains among the frontrunners in the absorption of RRF funds among EU economies. Strong domestic demand stimulated imports, and the outlook for exports has worsened on increased trade policy uncertainty. While not as exposed as Central Europe and the Baltic states, the region will be affected indirectly via the main euro area trade partners. Growth will nonetheless be sustained by robust domestic demand conditions.

Bulgaria

Economic growth accelerated in 2024 to 2.8 per cent, driven by a rebound of private consumption. Real wage growth averaged 13 per cent year on year, which supported consumption alongside an acceleration of loans to households, which expanded at the rate of 19 per cent. On the downside, investment contracted in real terms in 2024, although output in the construction sector remained resilient. Weak foreign demand translated into a further decline of industrial output and exports. Inflation declined to 2 per cent by the end of 2024 but has risen to 4 per cent by March 2025. Bulgaria's direct exposure to the US economy is limited, and the indirect impact on the manufacturing sector remains uncertain. Stronger growth in late 2024 created a strong carry-over effect, which is partly offset by the potential negative impact of higher US import tariffs. On balance, the 2025 real GDP growth forecast is revised up to 2.8 per cent. Real GDP growth is expected to moderate to 2.6 per cent in 2026.

Greece

Economic growth remained robust in 2024 at 2.3 per cent, outperforming the euro area average. Growth was supported by EU-funded investment projects and resilient private consumption. Both tourist arrivals and receipts reached historic highs in 2024, with tourism maintaining strong momentum even during the winter months. Soft indicators point to continued growth into early 2025, with the Economic Sentiment Indicator (ESI) and the Purchasing Managers' Index (PMI) standing at 107.7 and 55, respectively, in March 2025 – both above euro area averages. Unemployment has declined further to 8.6 per cent (seasonally adjusted) in February 2025. Fiscal consolidation efforts are ongoing, with the primary surplus forecast at 2.4 per cent of GDP in 2025. HICP inflation was 3 per cent in 2024, and core inflation has proven persistent, standing at 3.6 per cent in 2024 (down from 5.3 per cent in 2023), one of the highest rates in the euro area. The implementation of the revised Recovery and Resilience Plan (RRP) is progressing well, helping to mitigate external risks. As of March 2025, Greece had received €18.2 billion in RRP funds – 51 per cent of the total €36 billion envelope – surpassing the EU average, with 28 per cent of total milestones successfully completed. Given the limited exposure of this mainly service-based economy to global trade policy uncertainty, the economic outlook remains positive, with growth forecast to reach 2.2 per cent in both 2025 and 2026. Downside risks stem from an uncertain geopolitical environment and a sluggish euro area economy amid rising global protectionist pressures.

Romania

Economic growth slowed significantly to 0.8 per cent in 2024. While private consumption grew strongly on the back of real wage growth of 8 per cent, it led to a significant widening of the trade deficit. Consumption showed signs of moderation in early 2025. Investment decelerated significantly, especially in the last quarter, as EU funds absorption slowed. On the supply side, the slowdown was broad-based, with industry, services and construction experiencing notable decelerations, while agriculture was heavily affected by drought. The fiscal position remains challenging and the planned fiscal consolidation this year will likely require additional measures due to the worse-than-expected outturn in 2024. Despite a slight moderation, inflation remains elevated at close to 5 per cent, necessitating a tight monetary policy by the central bank. Romania's economy has limited exposure to the US economy, but it has a considerable level of integration in automotive global supply chains, which is a vulnerability. In light of decelerating consumption and the difficult fiscal position, the 2025 real GDP growth forecast is revised down to 1.6 per cent. In 2026, growth is forecast to return towards its potential level, at 2.4 per cent, assuming an acceleration of EU funds absorption.

Southern and eastern Mediterranean

Growth across the southern and eastern Mediterranean accelerated towards the end of 2024 following a prolonged period of regional instability. Performance is expected to improve further, with average growth reaching 3.6 per cent in 2025 and 3.9 per cent in 2026, although with significant downside risks pertaining to global trade policy uncertainty and the spillover effects of conflicts in Gaza and Lebanon. A more stable macroeconomic environment and falling inflation will likely support investor and consumer confidence in Egypt and a pickup in growth. Fiscal consolidation is expected to continue across the region as part of announced government policy trajectories (in Egypt, Jordan, Tunisia and Morocco). In light of the ongoing ceasefire, growth *in Lebanon may rebound following the implementation of preliminary steps towards long-overdue reforms, particularly related to the restructuring of the banking sector.*

Egypt

Output growth is expected to increase from 2.4 per cent in fiscal year 2024 (FY24) to 3.8 per cent in FY 25 and 4.4 per cent in FY26. On a calendar-year basis, growth is forecast at 4 per cent in 2025 and 4.5 per cent in 2026. Growth rose to 3.9 per cent year on year in the first half of FY25 (July-December 2024), compared with 2.4 per cent in the same period the preceding year, driven by expansion in manufacturing, transportation and wholesale and retail trade. The manufacturing sector began to recover following a strong contraction during the time of foreign exchange shortages prior to March 2024. Output in the oil and gas sector continued to decline and is considered a key issue for government policy in FY25 and FY26, including the resolution of arrears to international energy companies. Inflation declined to 12.8 per cent in February 2025, its lowest level since March 2022, and is expected to continue falling reflecting the central bank's tight monetary policy stance. Rising fuel prices, as part of the government's commitment to reach cost recovery by the end of the year under the IMF-supported programme, may put upwards pressure on consumer prices. Net international reserves rose to US$47.4 billion in February 2025, their highest level in over 20 years, and are expected to remain stable. The growth outlook depends on the implementation of structural reforms, particularly related to the state's presence in the economy, and the continued reduction of debt levels and associated service costs. Risks to the outlook are relatively high given international trade policy uncertainty and Egypt's continued reliance on portfolio investment from abroad as a source of external financing.

Jordan

Economic growth in Jordan proved resilient in 2024 despite the wars in Gaza and Lebanon weighing on business and consumer confidence and lower room for public spending due to decreasing revenues. A quick recovery in tourism receipts in the second half of the year helped support growth. The government's commitment to fiscal discipline and progress on structural reforms further supported economic resilience and preserved market confidence. In the meantime, unemployment remained high, standing at 21.4 per cent by the end of 2024 while inflation stayed low despite a slight uptick to 2.1 per cent in February 2025. The Central Bank of Jordan maintained its policy rate since September 2024, mirroring the decisions of the Federal Reserve as part of its effort to preserve the currency peg. Foreign exchange reserves amounted to US$21.1 billion, covering around eight months of imports. Regional instability affected the external position, with the current account widening to an average of 5.9 per cent of GDP in 2024. Gross general government debt (including guaranteed debt) reached 115 per cent of GDP in December 2024. In 2025, growth is expected to benefit from a recovery in tourism and the re-opening of the Syrian market to Jordanian businesses, but downside risks from uncertainty around US foreign aid and trade policies weigh on the outlook for investment and growth. On balance, growth is expected to reach 2.2 per cent in 2025 picking up to 2.4 per cent in 2026, subject to restoration of regional stability.

Lebanon

The economy contracted further in 2024, by an estimated 5.7 per cent, as the war with Israel resulted in widespread displacement and damages to the country's infrastructure and physical capital. Reconstruction financing needs are estimated at US$11 billion. Inflation continued to decrease on the backdrop of a stabilised exchange rate, reaching 15.6 per cent year on year in February 2025. Public debt reached an estimated 158 per cent of GDP in 2024. Growth is expected to pick up to 1.9 per cent in 2025 and 2.9 per cent in 2026 provided political hurdles to implementation of critical economic reforms are reduced following the formation of the new government. In this respect, the appointment of a new central bank governor and renewed interest in an IMF-supported programme are positive developments. Finding traction on important reforms, including banking sector restructuring, remains critical for reaching agreement and regaining access to international financing and foreign investment. More broadly, risks to the outlook include resumed hostilities in the region, a delayed start to the reconstruction process and any return to political deadlock.

Morocco

Output growth is expected to rise from 3.2 per cent in 2024 to 3.5 per cent in 2025 before moderating to 3.4 per cent in 2026. Growth in 2024 was supported by infrastructure investment and expansions in the extraction, manufacturing and construction industries, while agriculture sharply contracted due to poor weather conditions. Inflation was low, at 0.9 per cent in 2024, enabling Bank al Maghrib to continue loosening its monetary stance and lower its policy rate by 25 basis points in March 2025. Elevated food prices may strengthen inflationary pressure in 2025. The fiscal deficit stood at 4.1 per cent of GDP in 2024 and is expected to fall in 2025 following further fiscal consolidation. Tourism continued to perform well in early 2025, following a record 2024, but may be exposed to a slowdown in global economic growth. Official reserves stood at US$38.2 billion as of February 2025, up 2.3 per cent year on year. Morocco and the IMF recently agreed to replace the current Flexible Credit Line (FCL) with a new US$4.5 billion FCL, which should continue to support external buffers in the event of a crisis. The growth outlook is stable, albeit subject to risks given Morocco's exposure to weather conditions and the potential spillovers of trade policy uncertainty via European markets, the country's main export destination.

Tunisia

Output growth is expected to rise from 1.4 per cent in 2024 to 1.7 per cent in 2025 and 2.1 per cent in 2026. In 2024, expansions in the agriculture, hospitality and transportation sectors outweighed contractions in oil and gas, textiles and construction. Agricultural output rebounded following a strong contraction in the previous year, which was caused by adverse weather conditions. Unemployment remained relatively stable as inflation continued to fall before accelerating slightly, to 5.9 per cent in March 2025. In April 2025, the Central Bank of Tunisia cut its policy rate by 50 basis points to 7.5 per cent, the first change in the policy rate since January 2023. The fiscal deficit fell to 6 per cent of GDP in 2024, lower than the annual budget target, and is expected to fall further as the government continues to implement its medium-term fiscal consolidation plan. Debt-to-GDP stood at 81.2 per cent in 2024 and is expected to fall, with a shift in composition towards domestic debt and away from external sources. The external position is improving, with the current account deficit reduced from 2.3 per cent in 2023 to 1.7 per cent of GDP in 2024 owing to increased tourism and remittances receipts. Vulnerabilities remain however, as international reserves fell to US$7.46 billion in March 2025 from US$7.92 billion at end-2024 as Tunisia met payments on its international borrowing. The growth outlook is stable but subject to downside risks given Tunisia's exposure to potential spillovers from increased global trade policy uncertainty via the European market, a key export destination. A slowdown in the global economy may also affect tourism revenues, which have been an important source of foreign currency. The inflation outlook is also uncertain given repeated recourse to fiscal deficit monetisation in the past.

Türkiye

Growth slowed from 5.1 per cent in 2023 to 3.2 per cent in 2024. Domestic demand weakened significantly but continued to be the main driver of growth as economic policy continued its shift towards orthodoxy, while net exports' contribution to growth turned positive. Activity in the services sector (trade, logistics, and tourism) remained robust while construction activity was supported by post-earthquake reconstruction. On the other hand, the manufacturing sector, typically a major driver of growth, contracted owing to a tighter policy mix.

Monetary policy remained tight throughout 2024, aimed at curbing inflation and restoring macroeconomic stability. The Central Bank of the Republic of Türkiye (CBRT) held its policy rate (the one-week repo auction rate) at 50 per cent between March and December 2024, when it started to ease its policy stance with a cumulative 750 basis points reduction in three steps to 42.5 per cent, with overnight borrowing and lending rates at a margin of ± 150 basis points relative to the policy rate (41-44 per cent). However, in a surprise meeting in March 2025, the CBRT increased the overnight lending rate by 200 basis points to 46 per cent, amid heightened inflation and currency depreciation pressures and financial market volatility in the aftermath of the detention of the mayor of Istanbul following the legal proceedings against him. In its next scheduled meeting in April, the CBRT reversed its rate cutting cycle and hiked the policy rate by 350 basis points while setting the borrowing and lending rates at 44.5 and 49 per cent respectively. Tighter monetary and fiscal policies led to a significant reduction in inflation, from a peak of 75.4 per cent year on year in May 2024 to 38.1 per cent in March 2025, aided by the sharp appreciation of the Turkish lira. In real effective terms it has strengthened by 43 per cent since July 2023. In nominal terms, the lira depreciated by 7 per cent year-to-date, and the CBRT's response to lira depreciation placed renewed pressure on international reserves. To stabilise the currency, the CBRT sold more than US$40 billion in foreign exchange in the weeks following the detention of the mayor of Istanbul, and net reserves (excluding swaps) fell from around US$60 billion to less than US$20 billion.

Despite the appreciation of the currency in real terms, the external position improved significantly. Net exports rose further, and the 12-month cumulative current account deficit declined steadily, from a peak of US$55.1 billion (5.2 per cent of GDP) in May 2023 to US$12.8 billion in February 2025 (1 per cent of GDP). The improvement was led by a lower energy import bill, lower imports of gold and strong tourism receipts. At the same time, foreign direct investment inflows remained relatively low in the same period, at US$12.2 billion (0.9 per cent of GDP).

Economic growth is expected to slow down to 2.8 per cent in 2025, before picking up to 3.5 per cent in 2026. The downward revision of 0.2 percentage points relative to the February forecast for 2025 reflects expectations of tighter domestic financial conditions amidst heightened uncertainty weighing on domestic demand, while external demand could weaken in the context of increased global trade policy uncertainty. Downside risks are related to still-high inflation and the impact of tighter-for-longer global financial conditions on Türkiye's substantial short-term external financing needs.

Western Balkans

Growth in the Western Balkans accelerated slightly from 3.4 per cent in 2023 to 3.6 per cent in 2024. The main growth drivers were private consumption on the back of rising wages as well as public investment. Tourism remained strong, especially in Albania and Kosovo, and to a lesser extent in Montenegro. On the other hand, continuing weak external demand in the region's most significant trading partner, the European Union, kept goods exports subdued. Growth is projected to fall to 3.2 in 2025 on the direct and, more importantly, indirect effects of tariffs newly introduced by the US, before picking up to 3.4 per cent in 2026. Downside risks relate to the possibility of further escalation of a global trade war and, in some economies, continuing political tensions. Economies with a strong, export-oriented manufacturing sector, such as Bosnia and Herzegovina, North Macedonia and Serbia, are expected to face significant indirect negative effects through their exports to the eurozone (and to a lesser extent, Serbia's exports to China), while tourism-dependent economies like Kosovo, Albania, and Montenegro may experience more *moderate impacts from a potential slowdown in tourism from EU countries. Tight labour markets and substantial increases in minimum and public-sector wages will contribute to inflationary pressures and weigh on economies' competitiveness.*

Albania

Economic growth in 2024 was 4 per cent, supported by booming services (especially tourism) and construction while industrial and agricultural production declined. On the expenditure side, private consumption and public investment were the key drivers of growth, while goods exports dropped significantly — negatively impacted by the appreciation of the lek and weak external demand — contributing to a wider current account deficit. Inflation fell to 2.2 per cent on average in 2024 from 4.8 per cent in 2023, allowing the Bank of Albania to lower the base rate from 3.25 per cent at the beginning of 2024 to 2.75 per cent. The financial sector remained stable, with increased credit activity. Real GDP growth of 3.5 per cent is forecast for both 2025 and 2026. Upside risks come from the expected continuation of structural reforms, a strong commitment to EU accession and potential access to financing from the EU. Downside risks stem from weakening demand in the eurozone, a potential decrease in remittances from abroad, and slowing growth in tourism after record numbers in the past two years. Dry weather could negatively affect energy production and lead to higher electricity imports, although these risks are mitigated by increasing production from alternative renewable sources.

Bosnia and Herzegovina

Economic growth in 2024 was 2.5 per cent, according to preliminary data. Net exports made a negative contribution to growth due to a sharp rise in imports and a decline in exports, affected by weak external demand, also reflected in a decline in industrial production. Growth was primarily supported by services and construction, strong private consumption and an increase in investment. Inflation declined from its peak value of 17.4 per cent in October 2022 to 1.7 per cent in November 2024, driven by global disinflation, and has stayed around 2 per cent since then. Our growth forecasts have been revised downwards to 2.5 per cent in 2025 and 2.7 per cent in 2026 based on the expected effect of the new US import tariffs as well as intensifying domestic political tensions negatively affecting the outlook for much-needed reforms and private investment.

Kosovo

Real GDP growth is estimated at 4.4 per cent in 2024, supported by strong private consumption, investment and tourism receipts related to visits by the diaspora. However, net exports remained negative due to higher imports, resulting in a widening of the current account deficit to 8.9 per cent of GDP from 7.5 per cent in 2023. Inflation has decelerated rapidly, from 14.2 per cent year on year in July 2022 to 0.4 per cent in October 2024, before rising to 1.7 per cent in February 2025. Despite increased fiscal spending on capital investments and wages, the budget deficit remained at a similarly low level as in 2023 (0.3 per cent of GDP), thanks to a sharp rise in revenues. Real GDP growth forecasts have been revised down to 3.9 per cent in both 2025 and 2026 due to the expected indirect negative effects on remittances from higher import tariffs in the US. Kosovo could experience faster growth if public investment projects were implemented in a timelier manner. On the other hand, weaker-than-expected economic performance in the eurozone can negatively affect Kosovo's growth, especially through lower remittances. In addition, the caretaker government's mandate is limited, significantly hindering the implementation of structural reforms and capital expenditure projects.

Montenegro

Real GDP growth slowed markedly from 6.3 per cent in 2023 to 3 per cent in 2024 due to a significant slowdown in tourism, after a record season in 2023. Growth in 2024 was driven by private consumption and investment, supported by expansionary fiscal policies, rising wages and pensions and ambitious infrastructure projects. However, net exports contracted as the surge in tourists and immigrants from Russia and Ukraine abated. Inflation declined significantly from its peak of 17.5 per cent in November 2022 to 1 per cent in September 2024 before rising to 2.8 per cent in February 2025. Real GDP growth is projected at 2.6 in 2025 and 2.7 per cent in 2026. Growth is likely to moderate on increasing prices in the tourism sector (driven by large wage increases) that may constrain demand, while the refurbishment of the Pljevlja power plant (providing around 40 per cent of electricity for the country) will significantly decrease domestic electricity production and lead to a substantial increase in electricity imports. On the other hand, continuing wage increases could support fast consumption growth while widening the trade deficit.

North Macedonia

The pace of economic growth in North Macedonia rose to 2.8 per cent in 2024 from 2.1 per cent in 2023. Stronger growth in 2024 was driven by government spending and private consumption, alongside easing inflation and credit expansion. On the other hand, industrial output and value added have declined, while the trade balance flipped from a small surplus in 2023 to a deficit of 2.3 per cent of GDP in 2024, primarily due to low eurozone demand. Strong foreign direct investment (FDI) inflows, reaching 7.1 per cent of GDP in 2024, have been more than sufficient to cover the current account deficit. Growth forecasts have been revised down to 2.6 in 2025 and 2.7 per cent in 2026, on the indirect effect of lower eurozone demand due to the new US import tariffs. On the upside, there is potential for higher growth if structural reforms are implemented effectively and if ambitious capital investment projects are successfully carried out, although concerns about the country's fiscal space and implementation capacity remain.

Serbia

The preliminary estimate of the statistical office indicates 3.9 per cent real GDP growth in 2024, a similar pace as in 2023. The main drivers of growth were trade, tourism and construction, while household consumption and investment provided the strongest boost to demand. On the other hand, net exports made a negative contribution to growth due to higher imports of goods, in line with the recovery of domestic demand, and the continuing real appreciation of the dinar. The current account deficit widened to 6.3 per cent of GDP 2024, up from 2.4 per cent in 2023. Net FDI inflows reached a record level at €4.6 billion but were not sufficient to fully cover the current account deficit. The budget deficit was lower than planned at 2 per cent of GDP. Inflation declined from its peak of 16.2 per cent in March 2023 to 3.8 per cent in June 2024, before rising to 4.5 per cent in February 2025. While inflation remained relatively high in regional comparison, the central bank cut the policy rate from 6.5 per cent at the beginning of 2024 to 5.75 per cent (as of 24 April 2025). Real GDP growth forecasts are revised downwards to 3.5 per cent in 2025 and 3.7 per cent in 2026 on lower expected demand from the eurozone and China due to higher US import tariffs and increased global policy uncertainty. Tightening labour markets and potential slowdown of structural reforms due to continuing political tensions constitute further downside risks. On the other hand, implementation of the ambitious public investment agenda may accelerate growth.

Belarus

Real GDP increased by 4 per cent in 2024, buoyed by expanding manufacturing, construction and trade. However, real GDP growth decelerated in the first quarter of 2025. The slowdown can be attributed to weaker exports to Russia and a decline in manufacturing, highlighting the limitations of import substitution policies as a primary growth driver. Although inflation had eased to 5.2 per cent by the end of 2024, it surged to 5.9 per cent in March 2025 due to rising food prices and strong domestic demand. The increasing dependency of Belarus on the Russian economy is mirrored in a projected moderation of real GDP growth rate to 2.5 per cent in 2025 and 2026, with significant downside risks to the outlook.

Russia

In 2024, real GDP growth accelerated to 4.3 per cent according to official statistics, propelled by substantial military government expenditure, which accounted for nearly 6 per cent of GDP. However, there are increasing indications that war-related growth is losing momentum. The manufacturing sector's growth rate decelerated sharply at the start of 2025, with civil industrial sectors experiencing a prolonged stagnation. Low commodity prices combined with rising nominal wages have squeezed profits to levels that deter private investment, while the slowing growth of consumer lending adversely impacts the demand for durable consumer goods. Inflation has continued along an upward trajectory, reaching 10.3 per cent in March 2025, driven by rising food prices. The Bank of Russia has maintained a policy rate of 21 per cent since December 2024. Real GDP growth is projected to slow to 1.5 per cent in 2025 and 2026, due to tight monetary policies, lower commodity prices and increasingly binding constraints on productive capacity utilisation.

About this report

The Regional Economic Prospects report is published twice a year. The report is prepared by the Office of the Chief Economist and the Department for Policy Strategy and Delivery and contains a summary of regional economic developments and outlook, alongside the EBRD's growth forecasts for the economies where it invests. The report also touches on the economic developments in Belarus and Russia notwithstanding the fact that Belarus and Russia have had their access to Bank resources suspended under Article 8.3 of the Agreements Establishing the EBRD. All historical data are based on estimates by country statistical offices. Since 2022, Russia has stopped releasing detailed statistics on the government budget, external trade and current-account balance. The estimates and projections are based on statistical information available through April 24, 2025.

For more comprehensive coverage of economic policies and structural changes, see the EBRD's country strategies and updates, as well as the Transition Report 2023-24, which are all available on the Bank's website at www.ebrd.com.

Acknowledgements

The report was edited by Zsoka Koczan (koczanz@ebrd.com) and Alexander Plekhanov (plekhana@ebrd.com), under the general guidance of Beata Javorcik, Chief Economist. Box 1 was prepared by Maxim Chupilkin, Zsoka Koczan, Oleg Konovalov and Alexander Plekhanov. Box 2 was prepared by Maxim Chupilkin. Box 3 was prepared by Oleg Konovalov. Box 4 was prepared by Maxim Chupilkin and Oleg Konovalov.

Colleagues in the Communications Department, Policy Strategy and Delivery Department, the Office of the Chief Economist and other departments of the EBRD provided valuable comments and suggestions. Maxim Chupilkin and Oleg Konovalov provided research assistance.

Regional updates were edited by Peter Sanfey (sanfeyp@ebrd.com). The writing teams covering individual countries and regions were:

Albania, Bosnia and Herzegovina, Kosovo, Montenegro, North Macedonia and Serbia: Peter Tabak and Stasa Perisic Petovar

Belarus, Moldova, Russia and Ukraine: Dimitar Bogov and Jongwoo Lim

EU member states (excluding Greece): Marcin Tomaszewski and Radu Cracan

Greece: Peter Sanfey and Dimitris Sourvanos

Egypt, Jordan, Lebanon, Morocco and Tunisia: Alexa Tiemann, Fady Alrayyes, Reem Jodeh, Bassem Nemeh and Salsabil Ayman

Kazakhstan, the Kyrgyz Republic, Mongolia, Tajikistan, Turkmenistan and Uzbekistan: Ana Kresic

Armenia, Azerbaijan, Georgia and Türkiye: Rafik Selim and Goktug Odabasi

European Bank for Reconstruction and Development
Five Bank Street London
E14 4BG
United Kingdom

Tel: +44 20 7338 6000

www.ebrd.com