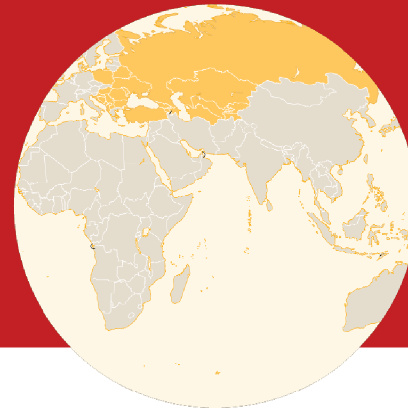
EUROPE and CENTRAL ASIA



Regional growth accelerated from 0.5 percent in 2015 to 1.2 percent in 2016, in line with expectations, due mainly to an easing of the recession in Russia as oil prices stabilized. Excluding Russia, regional growth slowed to 2.4 percent in 2016 from 3.5 percent in 2015, reflecting a slowdown in Turkey amid political uncertainty. In the eastern part of the region performance was mixed: activity picked up in Ukraine after two years of deep recession, growth continued to slow in Kazakhstan, and output contracted in Azerbaijan. In the western part of the region growth generally remained robust, despite moderating in several major countries (Turkey, Poland, and Hungary). Regional growth is expected to rise to 2.8 percent on average in 2018-19, driven mainly by a recovery in commodity exporters and Turkey. Risks remain tilted to the downside, and include the possibility of further weakness in commodity prices, disruptions in financial markets, slower-than-expected Euro Area growth, and political uncertainty. Key policy challenges include ensuring macroeconomic stability during the adjustment to lower commodity prices and dealing with sizable macroeconomic and financial vulnerabilities. Structural reforms would boost potential growth and mitigate the long-term effects of the lackluster external environment and aging populations.

Recent developments

Regional output is estimated to have expanded 1.2 percent in 2016, following 0.5 percent growth in 2015, as the recession in Russia, which accounts for almost 40 percent of regional GDP, eased (Table 2.2.1). Excluding Russia, regional growth in 2016 declined to 2.4 percent from 3.5 percent in 2015 as the Turkish economy slowed amid political uncertainty. Regional activity was supported by stabilizing commodity prices, accommodative policies, reduced geopolitical tensions (Russia, Ukraine), and improved overall confidence for most of 2016.[1]

Financial markets, which were generally stable for most of 2016, turned more volatile in the fourth quarter amid heightened policy uncertainty from both external (the United States and Europe) and domestic (particularly Turkey) factors (Figure 2.2.1). Exchange rates and asset prices, which recouped some of their earlier losses in mid-2016, came under renewed pressure in the fourth quarter, especially in several large western economies with relatively high levels of domestic policy uncertainty and significant vulnerabilities. Turkish lira fell to a record low against the U.S. dollar in December. In contrast, a modest recovery of commodity prices since November supported further rebound of exchange rates and asset prices in energy exporters (Kazakhstan and Russia).

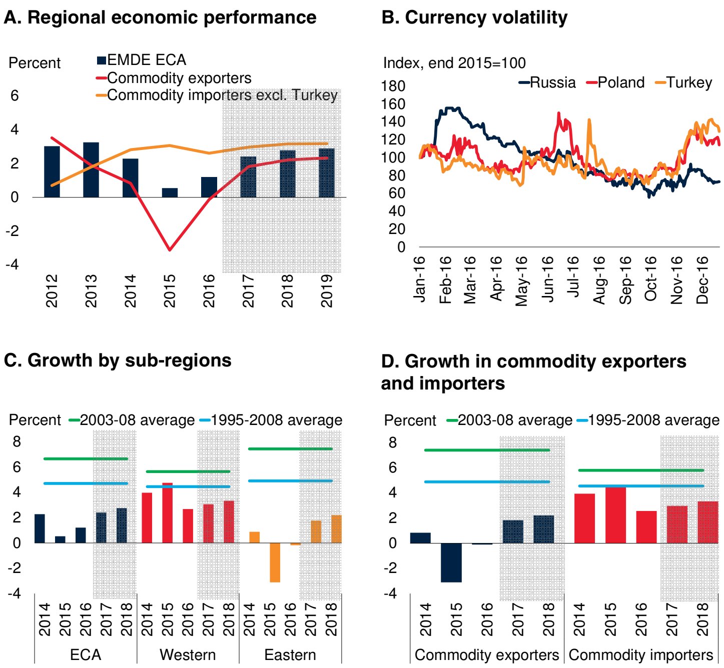
Monetary and fiscal policies followed different courses in the region. Russia and Kazakhstan cut their policy interest rates to support activity, despite above-target or above-trend inflation. Azerbaijan, where inflationary pressures persisted throughout 2016, maintained its tight monetary stance. Turkey raised its benchmark rate for the first time in almost three years in November 2016 amid a depreciating currency and weak external demand. Kazakhstan deployed a fiscal stimulus package equivalent to around 2 percent of GDP on net. Romania implemented a pro-cyclical value-added tax cut.

Note: This section was prepared by Yoki Okawa and Ekaterine Vashakmadze with contributions from Jongrim Ha and Hideaki Matsuoka. Research assistance was provided by Shituo Sun.

[1]The eastern part of the region comprises Eastern Europe (Belarus, Moldova, Ukraine), South Caucasus (Armenia, Azerbaijan and Georgia), Central Asia (Kazakhstan, the Kyrgyz Republic, Tajikistan, Turkmenistan, Uzbekistan) and Russia. The western part of the region includes Central Europe (Bulgaria, Croatia, Hungary, Poland Romania) and the Western Balkans (Albania, Bosnia and Herzegovina, Kosovo, FYR Macedonia, Montenegro, Serbia), and Turkey.

FIGURE 2.2.1 Growth

Regional growth rebounded in 2016, mainly because of an easing of the recession in Russia. The improved regional performance was supported by stabilization in financial markets until the third quarter. Growth is expected to continue to strengthen, led by commodity exporters, but will likely remain below its long-run average.



Sources: Bloomberg, World Bank.
A. Weighted averages. Growth is year-on-year percent change. EMDE ECA = emerging market and developing economies in European and Central Asia. Shadow area indicates projections. The sample includes 24 EMDEs in European and Central Asia.
B. Currency volatility is the 1-month implied volatility for the exchange rate. The volatility of last day in 2015 is set to 100. Last observation is December 21, 2016.
C.D. Weighted averages. Year-on-year real growth. Long term average is for 1995-2008.
C. The western part of the region includes Albania, Bulgaria, Bosnia and Herzegovina, Croatia, Hungary, Kosovo, the FYR Macedonia, Montenegro, Poland, Romania, Serbia and Turkey. The eastern part of region includes Armenia, Azerbaijan, Belarus, Georgia, Kazakhstan, the Kyrgyz Republic, Moldova, Russia, Tajikistan, Turkmenistan, Ukraine, and Uzbekistan.
D. Commodity exporters include Albania, Armenia, Azerbaijan, Kazakhstan, Kyrgyz Republic, Russia, Tajikistan, Turkmenistan, Ukraine, and Uzbekistan. Commodity importers include Bulgaria, Bosnia and Herzegovina, Belarus, Georgia, Croatia, Hungary, Kosovo, FYR Macedonia, Moldova, Montenegro, Poland, Romania, Serbia, and Turkey.

In Russia, the output contraction eased to -0.6 percent in 2016, from -3.7 percent in 2015 (Figure 2.2.2 and Table 2.2.2). Russia's contraction was shallower than projected in June because of overall accommodative fiscal policy in 2016 with the temporary suspension of the fiscal rule and banking sector capital and liquidity injections (IMF 2016h; World Bank 2016g). The flexible exchange rate, which depreciated in real effective terms from 2014 to early 2016, was also a supporting factor. Investment bottomed out faster than expected, as firms started rebuilding inventories, and the contraction in consumption eased as inflation declined to pre-crisis levels.

Growth slowed to 0.9 percent in Kazakhstan and the output contracted in Azerbaijan. The erosion of foreign exchange reserves in an attempt to support their currencies, following the commodity price bust, led to the abandonment of fixed exchange rates in favor of a float in Kazakhstan and a managed float in Azerbaijan (Horton et al. 2016; IMF 2016i). The acute phase of the shock might be over in both countries. However, activity in these countries have been held back by contractions in non-oil activity, particularly the services sector (Kazakhstan) and construction (Azerbaijan), which had previously been supported by public investment (IMF 2015b). Weak growth in Russia, Azerbaijan, and Kazakhstan continues to weigh on Central Asia and the South Caucasus. Growth has remained below long-term trends in Armenia, Georgia, the Kyrgyz Republic, and Tajikistan in 2016.

Growth in Eastern European sub-region is bottoming out after two years of sharp recession. Ukraine grew by 1 percent in 2016, a broad-based recovery from the almost 10 percent contraction in 2015. This reflected an easing of the conflict in eastern Ukraine, along with the impact of significant reforms undertaken during 2014-15 to stabilize the economy and reduce large imbalances. The Second Review of the IMF program was approved in September 2016, which helped to release some previously committed donor funds. Inflation has remained below 15 percent since April, and the exchange rate has stabilized since September. Growth in Moldova bottomed out, and the contraction in Belarus eased, partly because of the recovery in Russia and Ukraine.

Activity in the western part of the region, which is comprised of commodity importers that are more closely linked to, or are members of, the European Union (EU), has generally remained robust. Growth accelerated in Albania, Croatia, Romania, and Serbia reflecting strong domestic demand supported by low energy prices, faster investment growth helped by the disbursement of EU structural funds, labor market improvements, particularly in Albania, and the VAT tax cut in Romania. Strong exports of goods and services to the Euro Area were additional supportive factors in Croatia and Romania. In contrast, easing of domestic demand weighed on growth in Hungary, Poland, and Turkey. In Turkey, activity contracted in the third quarter of 2016, for the first time since 2009, in the wake of the failed coup attempt and resulting deterioration of business conditions.

Vulnerabilities

Several countries in ECA have enhanced their policy frameworks and their resilience to external shocks in recent years, but vulnerabilities in the region are numerous. Some countries face substantial financing needs in excess of reserves. Albania, Georgia, the Kyrgyz Republic, and Turkey are running current account deficits, which are often financed by volatile portfolio flows. Albania, Belarus, Croatia, Hungary, Montenegro, Poland, and Ukraine, are at risk from elevated sovereign debt levels. Croatia, Georgia, Kazakhstan, and Turkey have high stocks of private debt denominated in foreign currencies, the legacy of rapid credit growth in the aftermath of the global financial crisis.

Outlook

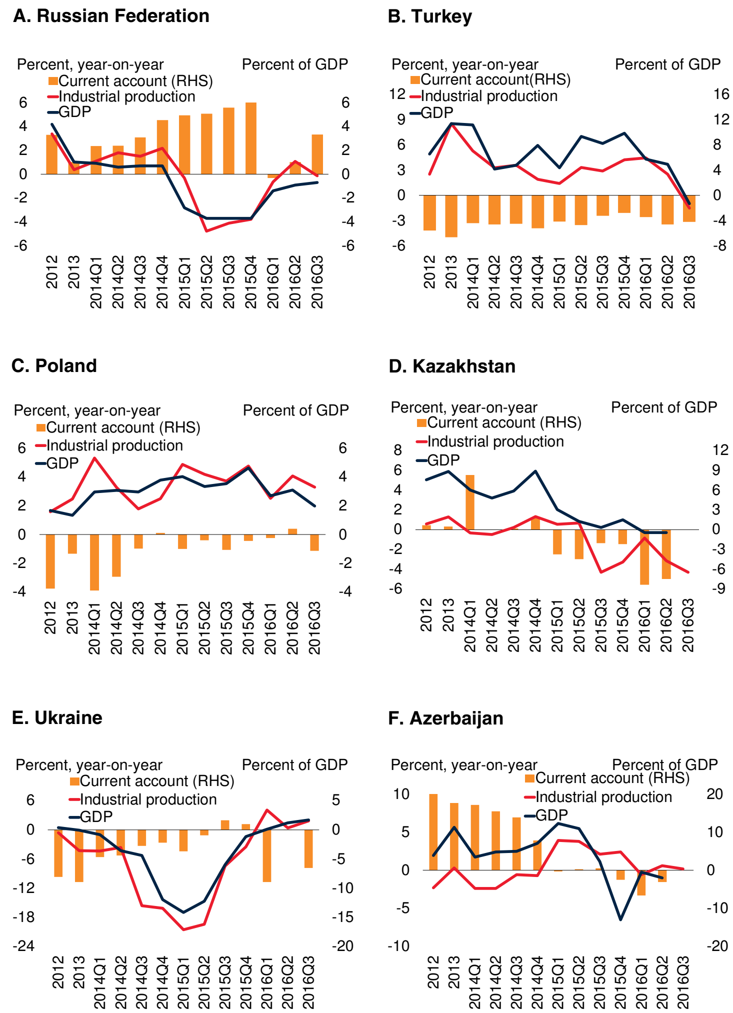
Growth in the region is expected to accelerate to 2.7 percent on average in 2017-19, driven by a recovery in commodity-exporting economies and improved confidence. This outlook is predicated on a continued, but modest, recovery in commodity prices and easing geopolitical tensions.

Growth in the western part of the region, which is close to its long-term average, is projected to remain robust. The economies in the east of the region are expected to continue to strengthen, although growth is projected to remain well below both long-term and pre-crisis averages. Growth in major energy exporters is being held back by weakness in non-oil sectors (IMF 2015a).

Russia's economy will resume growth in 2017, as the adjustment to low oil prices is completed. However, in the baseline scenario, growth will likely remain below the 1995-2008 average of 4.1 percent, partly reflecting persistently low oil prices. The adjustment to the negative terms-of-trade shock in Azerbaijan and Kazakhstan is

FIGURE 2.2.2 Country developments

Recessions in Russia and Ukraine have bottomed out. In Turkey, sharp drop in confidence led to a contraction of activity in the third quarter. Activity moderated in Poland. Growth slowed in Kazakhstan and output contracted in Azerbaijan, reflecting gradual adjustment to low commodity prices.

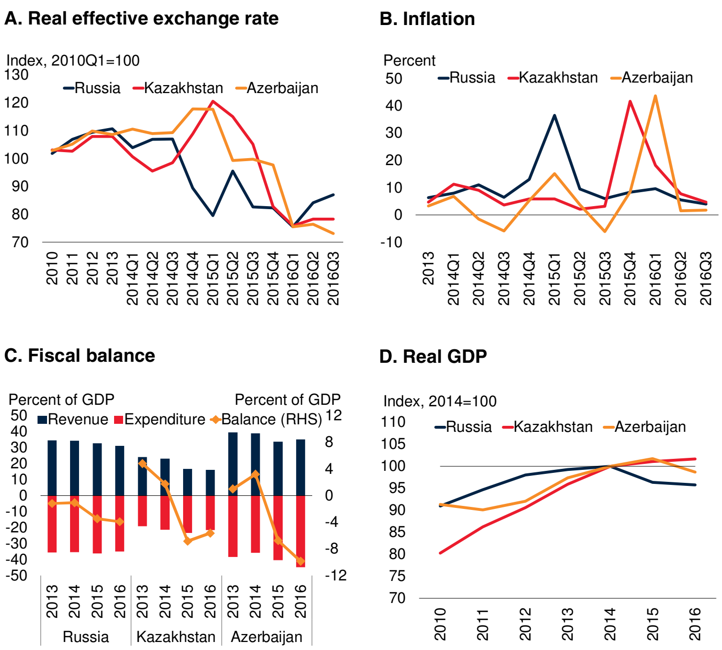


Source: Haver Analytics.
A.-F. Industrial production are year-on-year growth, not seasonally adjusted. Current account balances are seasonally adjusted. Last observation is 2016Q3 for Russia, Turkey, Poland, and Ukraine. Last observation is 2016Q2 for Kazakhstan and Azerbaijan except industrial production.

projected to level off in 2017, as commodity prices stabilize and economic imbalances narrow (Figure 2.2.3; IMF 2015d). Further adjustments that are required in the fiscal and banking spheres constrain the outlook for investment given the high capital intensity of the extractive industry. Strengthened activity in Russia and Kazakhstan will support other economies in the region (Armenia, Belarus, the Kyrgyz Republic) through

FIGURE 2.2.3 Policy responses to lower oil prices and growth

Russia responded to lower oil prices and international sanctions by allowing an early and sharp depreciation of its currency. In Kazakhstan and Azerbaijan, exchange rate adjustments were implemented in late 2015 to early 2016.



Sources: Haver Analytics, International Monetary Fund, World Bank.
B. Inflation is annualized quarter-on-quarter consumer price growth. Last observation is 2016Q3.
C. Revenue is general government revenue; expenditure is general government total expenditure; balance is general government net lending/borrowing.
D. 2016 data are estimates.

rising trade and remittances. Regional integration initiatives (e.g., the Eurasian Economic Union, EEU, the European Union, EU) could help.

Among oil importers, output in Ukraine, which returned to expansion in 2016, is expected to grow as the security situation improves and domestic economic reforms gain traction. Growth in 2017 is projected at 2 percent—unchanged from the June projection. While Ukraine made progress in reforming public finances, debt management, energy subsidies, and the banking system, efforts to address government ineffectiveness, privatization of state-owned enterprises, and pension reform have been delayed (IMF 2016j).

The outlook for countries in the western part of region is mixed. On average, growth is expected to remain steady in Central Europe, despite lower trading partner growth and gradually rising prices for commodity imports. Differences in prospects among countries stem from domestic factors. Romania's strong growth in 2016, boosted by pro-cyclical VAT cut, will stabilize in 2017. In Hungary, growth is projected to accelerate to 2.7 percent on average reflecting a recovery of public investment, including the infrastructure projects financed by EU funds.

In Turkey, growth projected to recover to 3.0 percent in 2017 and 3.6 percent, on average, in 2018-19 helped by improved confidence. However, downside risks to the outlook increased compared to June, reflecting political uncertainty and financial market volatility. Growth in Poland is projected to remain around 3.3 percent in 2017-19, supported by robust domestic demand, especially private consumption. Weak demand from main trading partners, including the United Kingdom and Euro Area, will limit the prospects of further acceleration.

Risks

The risks in the region remains tilted to the downside. The main risks could come from lower commodity prices, financial market disruption, political uncertainty or slower growth in advanced economies, including Europe and the United States, and geopolitical uncertainty in the region.

The primary downside risk for Russia and the eastern part of the region is a stalling or reversing recovery of global energy prices. For energy exporters (Azerbaijan, Kazakhstan, Russia, Turkmenistan, Uzbekistan), energy price shocks could affect macroeconomic stability through spillovers to other sectors, such as construction and transportation, fiscal pressures, strains on the exchange rate, inflation or financial system instability. Financial strains and fiscal deterioration could trigger a pro-cyclical policy tightening to preserve fiscal and reserve buffers, which could include public spending cuts and policy interest rate increases. A deeper or longer-than-expected recession in Russia could generate intensified spillovers for the rest of the eastern part through reduced remittance flows and lower demand for exports (Armenia, Belarus, Georgia, the Kyrgyz Republic, Moldova, Tajikistan, Uzbekistan).

U.S. monetary tightening could be accompanied by bouts of heightened risk aversion and financial stress, which in the past have led to slowing international capital flows with damaging consequences for activity and employment in the region. The economies with significant external financing needs are particularly sensitive to a potential reversal of capital flows (Figure 2.2.6).

Global policy uncertainty has significantly increased following the elections in the United States and the United Kingdom's decision to leave the European Union. The region, especially its western part, has strong ties with the European Union. Heightened uncertainty in advanced economies—in Europe or elsewhere—could have significant impact on trade, external balances, and regional growth prospects. If this risk materializes, the scope for the countercyclical policies could be limited for many countries (Albania, Belarus, Croatia, Hungary, Montenegro, Russia, Serbia, Ukraine; Figure 2.2.4, 2.2.5).

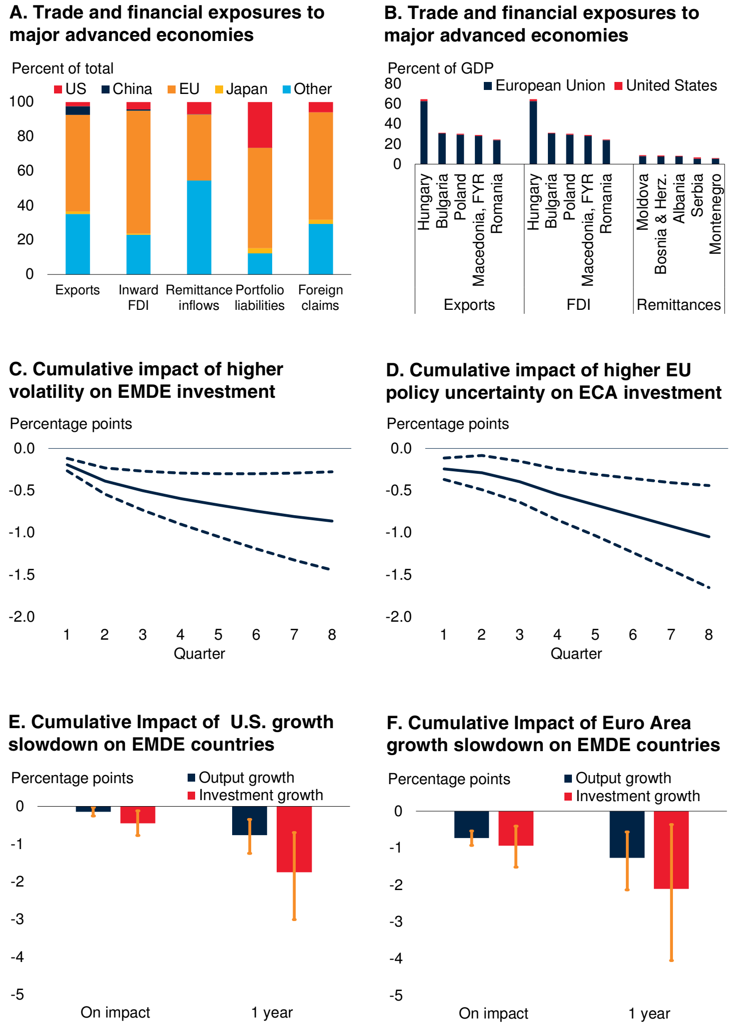
An escalation of geopolitical tensions would also set back growth. Risks include rising tensions in Eastern Ukraine, the conflict in Syria, and the refugee crisis. In Turkey, while a sharp contraction in activity after the failed coup attempt in July is expected to ease gradually in the baseline scenario, uncertainty on the future prospect remain elevated and risks to the outlook are tilted to the downside. If geopolitical and domestic political tensions delay the implementation of necessary reforms and discourage investment, long-term growth prospects would also be adversely affected.

Policy challenges

Despite the recent recovery, growth in the ECA region remains below trend. In several countries (Belarus, Croatia, Ukraine), GDP is still below pre-crisis levels. The high volatility of output in the region hinders its growth prospects (Figure 2.2.6). The key policy challenge for the region is to lift growth back to a stable trend rate. This requires policies that promote macroeconomic and political stability, economic diversification, and improved resilience to external headwinds.

FIGURE 2.2.4 Risks of heightened policy uncertainty in major advanced economies

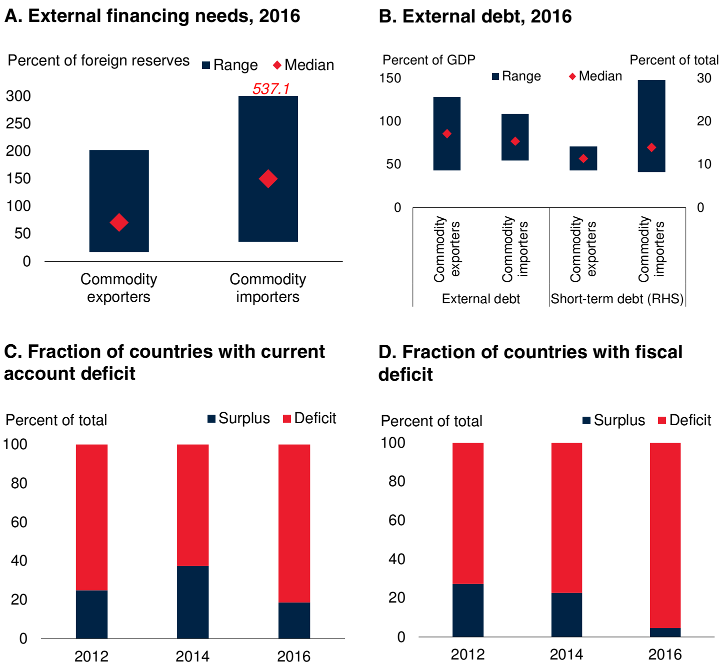
The region, especially its western part, has strong ties with the European Union. Heightened uncertainty in advanced economies—in Europe or elsewhere—could have significant impact on trade, external balances, and regional growth prospects. A slowdown in U.S. or Euro Area growth would reduce growth and investment in EMDEs considerably.



Sources: Baker, Davies, and Bloom (2016); Bank for International Settlements; Haver Analytics; World Bank; International Monetary Fund.
A.B. Foreign claims refer to stock of total claims of BIS-reporting banks on foreign banks and non-banks. Trade refers to goods exports and imports. Data is average of 2010-15.exports to the United States/Euro Area, remittances from the United States/Euro Area, and FDI from the United States/Euro Area (all in percent of GDP). FDI is stock of total FDI. Figure B. shows only the countries with the largest exposures to the United States and Euro Area.
C.D. Cumulative impulse response using a vector autoregression for 18 EMDEs for 1998Q1-2016Q2. Details of the methodology are provided in Annex SF3.2B. Solid lines indicate median responses and dotted lines indicate 16-84 percent confidence intervals. Endogenous variables follow this Cholesky ordering, the VIX or Economic Policy Uncertainty (EPU) Index for the EU, EMDE stock price index, EMDE bond price index, and aggregate real output and investment in EMDEs. Exogenous regressors, included with two lags, are G7 real GDP growth, world stock price index, and U.S. 10-year bond yields. For the estimation of the impact of EU uncertainty (as measured by the EPU, Figure 2.2.4D), the sample includes EMDEs in Europe and Central Asia (Bulgaria, Hungary, Poland, Romania, Russia, Turkey).
E.F. Bars indicate median cumulative impulse responses (vertical lines indicate 16-84th percentile confidence intervals) from a Bayesian structural vector autoregression for 1998Q1–2016Q2, using weighted average data for 18 EMDEs. The regression includes, in this Cholesky ordering, weighted average output growth in major advanced economies and China (excluding either the United States or the Euro Area); U.S. or Euro Area output growth; U.S. 10-year sovereign bond yield; JP Morgan's EMBI index; and aggregate output growth or investment growth in EMDEs (excluding China).
The oil price growth is included as an exogenous regressor in the model. Details are elaborates in Annex 3.2C.

FIGURE 2.2.5 Vulnerabilities

External imbalances and fiscal vulnerabilities are elevated in the region. Short-term financing needs exceed reserves in most countries, particularly among commodity importers.



Sources: Haver Analytics, International Monetary Fund, World Bank.
A. External financing needs are defined as amount of external debt repayment, within one year which includes the short-term and long-term debt, plus current account deficit over foreign reserves. Number in red (537.1) indicates maximum external financing need in percent of foreign reserves among commodity exporters.
C.D. Data is for all EMDE European and Central Asia countries whose data are available.

Cyclical policies

Exchange rate flexibility and monetary policy credibility. For countries hit by large terms-of-trade shocks, especially in the eastern part of the region, it is critical to employ policies to promote adjustment to the new era of low oil prices. These include exchange rate flexibility, policy predictability, and an agile business environment (Svensson 2010; Mollick et al. 2011). The adoption of new monetary policy frameworks could strengthen policy credibility in countries that have recently allowed more exchange rate flexibility, such as Azerbaijan and Kazakhstan. Safeguarding macroeconomic stability and managing volatility is important for commodity importers as well, especially for economies closely related to oil-exporting countries (Armenia, Georgia, Moldova, the Kyrgyz Republic). These countries have limited monetary policy buffers, high dollarization rates, and high risks emanating from elevated foreign currency-denominated private debt.

Financial-sector risk management. Economies with high and rising debt, unhedged foreign liabilities, or heavy reliance on short-term borrowing to fund longer-term investments (Azerbaijan, Hungary, Kazakhstan, and Turkey) would benefit from stronger risk management (IMF 2016k; Claessens 2015), such as requiring greater capital and liquidity buffers for financial institutions exposed to leveraged corporates. Strengthened governance in state-owned enterprises can help contain the buildup of corporate debt. Reforms to insolvency and bankruptcy laws would, among other improvements, allow a more rapid and orderly resolution of distressed companies.

Rebuilding fiscal policy buffers. Improving macroeconomic stability requires fiscal consolidation over the medium term. With few exceptions, commodity importers have limited fiscal buffers, reflecting elevated government debt or large deficits. Commodity exporters, who had smaller deficits than importers, saw a deterioration in fiscal balances as well as from a decline in commodity-related revenue. Unless severe downside risks materialize, the priority in many countries is to rebuild policy buffers and implement fiscal reforms.

For fiscal consolidation, in addition to reducing spending, countries need to broaden their tax base and strengthen tax administration. In Russia, a gradual increase in revenues would support fiscal consolidation. In Ukraine, the fiscal outlook remains challenging, with the general deficit, including Naftogaz, projected at almost 4 percent of GDP in 2016. Measures to improve the quality of public spending, consistent with medium-term expenditure frameworks, would also be appropriate.

Many commodity-exporting economies in the region have sovereign wealth funds, which have helped reduce pro-cyclicality of fiscal policy (Bleaney and Halland 2016; World Bank 2016g). The rules governing these funds could be strengthened to ensure greater counter-cyclicality and intergenerational equity. For example, Russia established two separately managed wealth funds, one to facilitate macroeconomic stabilization, and the other to fund long term pension obligations.

Structural reforms

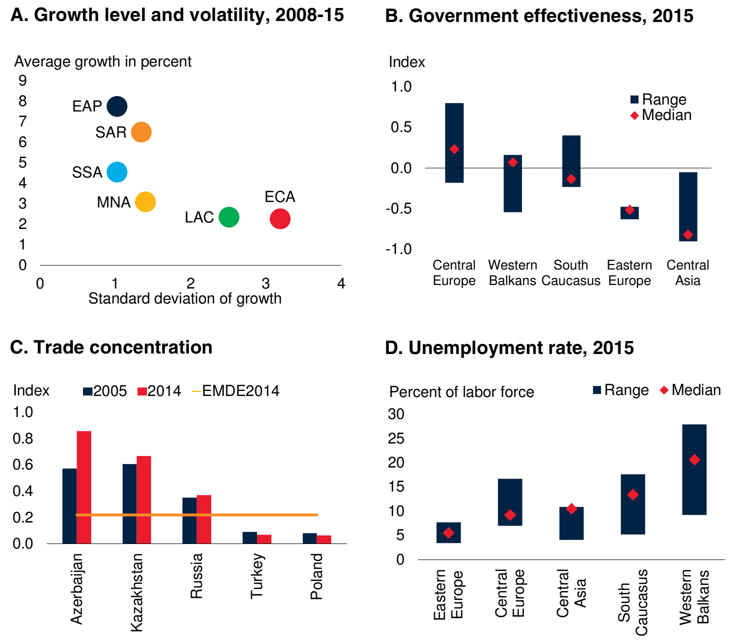
Enhancing productive investment. A sustained recovery in the region requires strengthening investment (Box 2.2.1, Chapter 3; World Bank 2015d). However, a legacy of financial imbalances weighs on investment growth. Policies that boost private investment, encourage more efficient use of public resources, and effective public-private partnerships (PPP) will be critical for recovery. These include reforms to deepen capital markets and strengthen banking systems, such as through faster and more effective insolvency procedures. Improved coordination and deployment of existing regional and global investment initiatives and funds, including EU structural funds, would be useful.

Diversification. Hydrocarbons account for more than 70 percent of goods exports in many countries in the eastern part of the region (Azerbaijan, Kazakhstan, Russia, Turkmenistan). Diversification, which is associated with higher growth and lower output volatility, should rank high among policy priorities (Papageorgiou and Spatafora 2012; Cavalcanti et al. 2015). The use of revenues from natural resources to build up infrastructure, advance education, and improve institutions can promote diversification (Gill et al. 2014). International experience suggests that reducing commodity dependence can be successful over time when the government makes an adequate commitment of time and political effort (Indonesia, Malaysia, Mexico; Cherif, Hasanov, and Zhu 2016).

Labor markets. Many countries in the western part of the region continue to suffer from double-digit unemployment rates. This problem is particularly pronounced in the Western Balkans. Labor market reforms, combined with reforms to improve the business environment, would boost productivity and job creation (Kovtun et al. 2014). Reforms would enable existing firms to grow, become more productive, or exit the market. They would also tap into

FIGURE 2.2.6 Policy challenges

GDP growth in the ECA region is the slowest and most volatile among EMDE regions after the global financial crisis in 2008-09. Low government effectiveness in some sub-regions and high trade concentration in oil exporters can be contributing factors to the high volatility. In some economies, in Western Balkan in particular, lowering high unemployment rates is one of the key challenges.



Sources: Haver Analytics, United Nations Conference on Trade and Development, World Bank.
A. Mean and standard deviation of annual regional GDP growth rate from 2008 to 2015. EAP = East Asia and Pacific, ECA = Europe and Central Asia, LAC = Latin America and the Caribbean, MNA = Middle East and North Africa, SAR = South Asia, SSA = Sub-Saharan Africa. Regional GDP only includes the EMDE countries.
B. The indicator reflects perceptions of the quality of public services, the quality of the civil service and the degree of its independence from political pressures, the quality of policy formulation and implementation, and the credibility of the government's commitment to such policies. The data is for 2015. The index ranges from -2.5 (weak) to 2.5 (strong) governance performance.
C. The trade concentration index is a measure of the degree of product concentration of exports from UNCTAD. An index value closer to 1 indicates higher concentration. EMDE 2014 is the average value weighted by real GDP for the emerging and developing economies in 2014.
D. Data is for 2015.

entrepreneurship potential, so that new firms emerge and succeed quickly and inexpensively.

Labor market initiatives could involve education and training, incentives to be mobile, and regulations eliminating barriers to minorities, women, youth and older workers. (World Bank 2014b). Better quality education and closer alignment with employers' needs can reduce the skill mismatches that contribute to underemployment (Sondergaard and Murthi 2012). Countries could improve their productivity by lowering barriers to service sector liberalization and by reducing administrative burdens on businesses.

TABLE 2.2.1 Europe and Central Asia forecast summary

(Real GDP growth at market prices in percent, unless indicated otherwise)

	2014	2015	2016	2017	2018	2019	2015	2016	2017	2018
			Estimates	Projections			(percentage point difference from June 2016 projections)			
EMDE ECA, GDP[a]	**2.3**	**0.5**	**1.2**	**2.4**	**2.8**	**2.9**	**0.6**	**0.0**	**-0.1**	**0.0**
EMDE ECA, GDP excl. Russia	3.4	3.5	2.4	3.0	3.4	3.6	1.0	-0.5	-0.2	0.0
(Average including countries with full national accounts and balance of payments data only)[b]										
EMDE ECA, GDP[b]	2.3	0.5	1.2	2.4	2.7	2.9	0.7	0.0	0.0	-0.1
GDP per capita (U.S. dollars)	1.8	0.1	0.9	2.1	2.6	2.7	0.6	0.0	-0.1	0.0
PPP GDP	2.1	0.2	1.1	2.4	2.8	2.9	0.5	0.0	0.0	0.0
Private consumption	1.3	-2.8	2.0	2.6	3.0	3.0	0.2	0.1	0.1	0.0
Public consumption	2.2	1.1	0.7	1.2	1.4	1.4	-0.5	-0.5	0.0	-0.1
Fixed investment	2.0	0.4	0.3	4.6	6.7	5.4	2.5	1.3	0.2	1.0
Exports, GNFS[c]	2.9	3.0	2.3	3.1	3.4	3.6	0.2	-0.8	-0.5	-0.2
Imports, GNFS[c]	-0.8	-6.2	3.3	4.7	6.2	5.0	0.8	0.0	0.0	-0.1
Net exports, contribution to growth	1.2	2.9	-0.2	-0.3	-0.7	-0.3	-0.3	-0.3	-0.1	0.0
Memo items: GDP										
Central Europe[d]	3.0	3.6	2.9	3.1	3.2	3.2	0.2	-0.5	-0.2	0.0
Western Balkans[e]	0.5	2.3	2.7	3.2	3.6	3.7	0.0	0.0	0.1	-0.1
Eastern Europe[f]	-3.8	-7.7	-0.1	1.3	2.5	2.6	0.1	0.2	0.1	0.2
South Caucasus[g]	2.7	1.6	-1.2	2.1	3.0	2.9	0.0	-0.7	0.4	0.8
Central Asia[h]	5.5	3.1	2.8	3.8	4.8	5.1	0.1	0.7	0.4	0.2
Russia	0.7	-3.7	-0.6	1.5	1.7	1.8	0.0	0.6	0.1	-0.1
Turkey	5.2	6.1	2.5	3.0	3.5	3.7	2.1	-1.0	-0.5	-0.1
Poland	3.3	3.9	2.5	3.1	3.3	3.4	0.3	-1.2	-0.4	-0.2

Source: World Bank.
World Bank forecasts are frequently updated based on new information and changing (global) circumstances. Consequently, projections presented here may differ from those contained in other Bank documents, even if basic assessments of countries' prospects do not differ at any given moment in time.
a. EMDE refers to emerging market and developing economy. GDP at market prices and expenditure components are measured in constant 2010 U.S. dollars.
b. Sub-region aggregate excludes Bosnia and Herzegovina, Kosovo, Montenegro, Serbia, Tajikistan, and Turkmenistan, for which data limitations prevent the forecasting of GDP components.
c. Exports and imports of goods and non-factor services (GNFS).
d. Includes Bulgaria, Croatia, Hungary, Poland, and Romania.
e. Includes Albania, Bosnia and Herzegovina, Kosovo, FYR Macedonia, Montenegro, and Serbia.
f. Includes Belarus, Moldova, and Ukraine.
g. Includes Armenia, Azerbaijan, and Georgia.
h. Includes Kazakhstan, Kyrgyz Republic, Tajikistan, Turkmenistan, and Uzbekistan.
For additional information, please see www.worldbank.org/gep.

TABLE 2.2.2 Europe and Central Asia country forecasts[a]

(Real GDP growth at market prices in percent, unless indicated otherwise)

	2014	2015	2016	2017	2018	2019	2015	2016	2017	2018
			Estimates	Projections			(percentage point difference from June 2016 projections)			
Albania	1.8	2.6	3.2	3.5	3.5	3.7	0.2	0.0	0.0	-0.3
Armenia	3.6	3.0	2.4	2.7	3.0	3.2	0.0	0.5	-0.1	0.1
Azerbaijan	2.0	1.1	-3.0	1.2	2.3	2.3	0.0	-1.1	0.5	1.0
Belarus	1.7	-3.9	-2.5	-0.5	1.3	1.4	0.0	0.5	0.5	1.0
Bosnia and Herzegovina	1.1	3.0	2.8	3.2	3.7	3.9	-0.2	0.2	0.1	0.2
Bulgaria	1.3	3.6	3.5	3.2	3.1	3.1	0.6	1.3	0.5	0.1
Croatia	-0.4	1.6	2.7	2.5	2.5	2.6	0.0	0.8	0.5	0.1
Georgia	4.6	2.8	3.4	5.2	5.3	5.0	0.0	0.4	0.7	0.3
Hungary	4.0	3.1	2.1	2.6	2.8	2.7	0.2	-0.5	0.2	0.5
Kazakhstan	4.2	1.2	0.9	2.2	3.7	4.0	0.0	0.8	0.3	0.0
Kosovo	1.2	4.1	3.6	3.9	3.7	3.6	0.5	0.0	-0.1	-0.4
Kyrgyz Republic	4.0	3.5	2.2	3.0	3.7	4.9	0.0	-1.2	-0.1	-0.4
Macedonia, FYR	3.6	3.8	2.0	3.3	3.7	4.0	0.1	-1.7	-0.7	-0.3
Moldova	4.8	-0.5	2.2	2.8	3.3	3.7	0.0	1.7	-1.2	-1.2
Montenegro	1.8	3.4	3.2	3.6	3.0	3.0	0.0	-0.5	0.5	0.0
Poland	3.3	3.9	2.5	3.1	3.3	3.4	0.3	-1.2	-0.4	-0.2
Romania	3.1	3.7	4.7	3.7	3.4	3.2	0.0	0.7	0.0	0.0
Russia	0.7	-3.7	-0.6	1.5	1.7	1.8	0.0	0.6	0.1	-0.1
Serbia	-1.8	0.8	2.5	2.8	3.5	3.5	0.0	0.7	0.5	0.0
Tajikistan	6.7	6.0	6.0	4.5	5.2	4.5	1.8	2.0	-0.3	-0.1
Turkey	5.2	6.1	2.5	3.0	3.5	3.7	2.1	-1.0	-0.5	-0.1
Turkmenistan	10.3	6.5	6.2	6.5	6.8	7.0	0.0	1.2	1.5	1.8
Ukraine	-6.6	-9.9	1.0	2.0	3.0	3.0	0.0	0.0	0.0	0.0
Uzbekistan	8.1	8.0	7.3	7.4	7.4	7.4	0.0	0.0	0.2	0.2

Source: World Bank.
World Bank forecasts are frequently updated based on new information and changing (global) circumstances. Consequently, projections presented here may differ from those contained in other Bank documents, even if basic assessments of countries' prospects do not significantly differ at any given moment in time.
a. GDP at market prices and expenditure components are measured in constant 2010 U.S. dollars.
For additional information, please see www.worldbank.org/gep.

BOX 2.2.1 Recent investment slowdown: Europe and Central Asia

Investment growth in the region declined from 10.2 percent in 2011 to 0.4 percent in 2015. The slowdown was initially concentrated in Central Europe and reflected mainly the spillovers from the Euro Area's debt crisis of 2011-12. A recovery of investment growth in Central and South-Eastern Europe started in 2014, but this was more than offset by investment contractions in Russia and other oil-exporting economies. Policy uncertainties and weak banking systems will likely limit regional investment growth in the near-term. The investment slowdown has come at a time when investment needs are sizable. In many commodity-importing economies, years of underinvestment have left substantial infrastructure deficits. Investment is key to boosting productivity and creating hospitable conditions for new growth sectors. However, efforts to address under-investment are likely to be constrained by the need for sustainable financing.

Europe and Central Asia (ECA) accounted for 5 percent of global investment during 2010-15. Investment growth in the region decreased sharply, from a 10.2 percent in 2010 to 0.4 percent in 2015. Partial data for 2016 suggest that investment is bottoming out in 2016, led by easing investment contractions in Russia and Ukraine. However, regional investment growth remains well below its long-term (1995-2008) average of 6.5 percent a year.

This box discusses the following questions.

- How has investment growth in the region evolved?
- What are the region's current and prospective investment needs?
- Which policies can help meet these needs?

The slowdown in investment growth in the ECA region was initially concentrated in the Central Europe in the aftermath of the Euro Area's debt crisis of 2011-12 and associated recession. The post-crisis recovery in Central Europe was weak, reflecting impaired banking systems and corporate sectors in the aftermath of the Euro Area crisis. Lingering concerns about armed conflict and related geopolitical tensions (Russia, Ukraine), policy uncertainty in several major regional economies, and adjustment to the terms-of-trade shock in energy exporters (Russia, Azerbaijan, Kazakhstan) have weighed on regional investment growth.

Meanwhile, current and prospective investment needs are sizable. Investment and major reforms are needed to increase productivity and set the stage for a sustained growth recovery. However, efforts to address under-investment are likely to be constrained by the need for sustainable financing.

Note: This section was prepared by Yoki Okawa and Ekaterine Vashakmadze. Research assistance was provided by Shituo Sun, Trang Thi Thuy Nguyen, and Liwei Liu.

How has investment growth in the region evolved?

The recent investment growth slowdown was sharp and broad based. In 2015, investment growth remained below its long-term averages in three-quarters of the countries in the region, and was negative in one-quarter of them, including Belarus, Russia, and Ukraine (Figure 2.2.1.1). Between 2010 and 2015, investment growth trends differed markedly between commodity importers, which are located in Central, Eastern, and Southeastern Europe, and commodity exporters, mainly Russia and the economies of Central Asia.

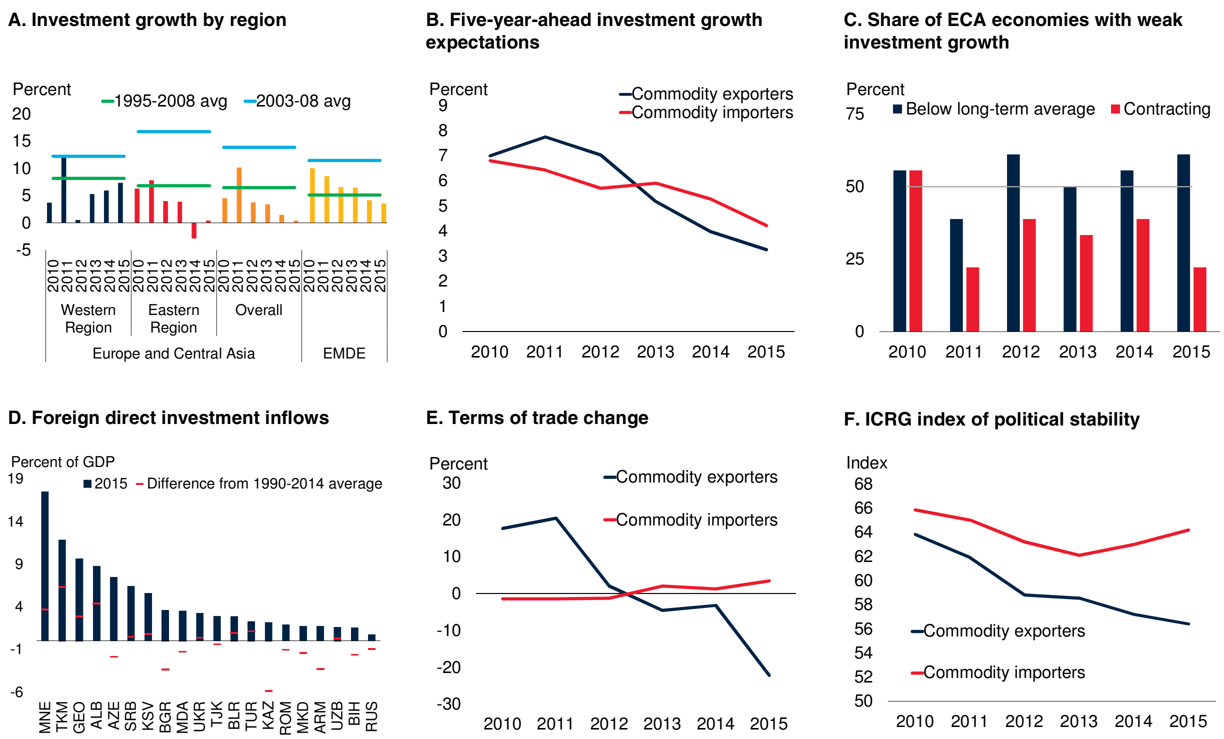
The overall slowdown was partly a correction from historically high investment growth prior to the global financial crisis. Pre-crisis, large capital inflows and credit booms fueled investment growth in the western part of the region as financial systems became more integrated with those in the Euro Area. Proximity to, and rapid convergence with, the Euro Area appeared to promise bright growth prospects as regional labor and product markets became increasingly intertwined (World Bank 2010). In the eastern part of the region, pre-crisis investment growth was buoyed by resource development encouraged by high global commodity prices.

In general, in *commodity-importing EMDEs,* investment financing became difficult to obtain from domestic banking sectors that were still healing from the crisis and pre-crisis credit booms (Hungary, Moldova, Serbia). The 2012-13 debt crisis and subsequent weak growth prospects in the Euro Area weighed on investor sentiment (Chapter 3). Weak trade growth and lower capital inflows reduced prospects for strong investment returns and increased financing costs. Net capital inflows exceeded 10 percent of GDP before the crisis but have been negative since 2013 in the Central and Southeastern Europe. Large foreign currency-denominated debt amplified the damage to the banking sector (EBRD 2015a). In some countries, this was compounded by policy uncertainty and lack of public

BOX 2.2.1 Recent investment slowdown: Europe and Central Asia *(continued)*

FIGURE 2.2.1.1 Investment growth slowdown in Europe and Central Asia, 2010-15

Regional investment growth declined from 10.2 percent in 2011 to 0.4 percent in 2015. Initially, the decline was concentrated in the western part of the region and reflected spillovers from the Euro Area crisis. The recovery of investment growth in the western parts of the region in 2014-15 was outweighed by a contraction in oil-exporting economies in the eastern parts of the region, which suffered a major terms-of-trade shock as a result of the oil price drop. Recession in Russia was exacerbated by international sanctions.



Sources: Consensus Forecasts, EBRD (2015a), Eurostat, Haver Analytics, World Bank.
A.C. Investment growth rates are weighted averages of gross fixed capital formation growth rates in the public and private sectors, respectively, in constant 2005 U.S. dollars.
A. The eastern part of the region comprises Eastern Europe (Belarus, Moldova, and Ukraine), South Caucasus (Armenia, Azerbaijan and Georgia), Central Asia (Kazakhstan, Kyrgyz Republic, Tajikistan, Turkmenistan, and Uzbekistan) and Russia. The western part of the region includes Central Europe (Bulgaria, Croatia, Hungary, Poland and Romania) and the Western Balkans (Albania, Bosnia and Herzegovina, Kosovo, FYR Macedonia, Montenegro, and Serbia), and Turkey.
B. Five-year ahead Consensus Forecasts as of the latest available month in the year denoted.
C. Share of ECA economies with investment growth below its long-term average or negative.
D. MNE = Montenegro, TKM = Turkmenistan, GEO = Georgia, ALB = Albania, AZE = Azerbaijan, SRB = Serbia, KSV = Kosovo, BGR = Bulgaria, MDA = Moldova, Republic of, UKR = Ukraine, TJK = Tajikistan, BLR = Belarus, TUR = Turkey, KAZ = Kazakhstan, ROM = Romania, MKD = FYR Macedonia, ARM = Armenia, UZB = Uzbekistan, BIH = Bosnia and Herzegovina, RUS = Russia.
E. Investment-weighted average. A decline denotes a terms of trade deterioration.
F. ICRG is the International Country Risk Guide, an investment-weighted average of political stability produced by the PRS Group. A higher index denotes greater political stability.

investment (Figure 2.2.1.2). Recovery has been gradual since 2013, despite support from accommodative monetary and fiscal policies in some countries, and sharply lower oil prices that lifted business confidence and real incomes.

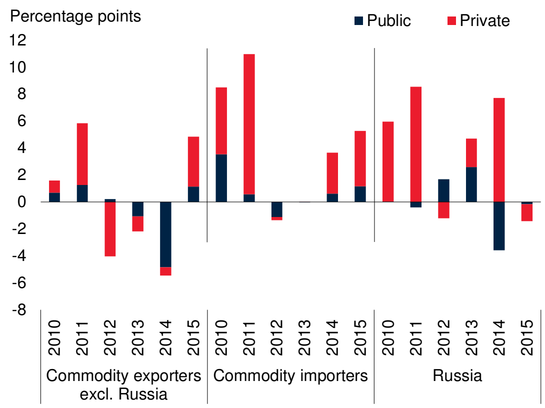
In *commodity-exporting EMDEs*, the global financial crisis-related fiscal stimulus supported double-digit investment growth in 2010. Investment growth remained robust until 2013, but slowed sharply once oil prices started sliding in 2014. Since mid-2014, investment has contracted year-on-year in every quarter, weighed down by the following factors: the unfolding conflict in Ukraine, intermittent border tensions in the Caucasus, international sanctions that heavily restricted access to finance in Russia, a severe terms-of-trade shock that hit energy exporters (Azerbaijan, Kazakhstan, Russia), and contracting public sector investment. Neighboring countries suffered from spillover effects, including weaker trade, remittances, and foreign direct investment (World Bank 2016h).

BOX 2.2.1 Recent investment slowdown: Europe and Central Asia *(continued)*

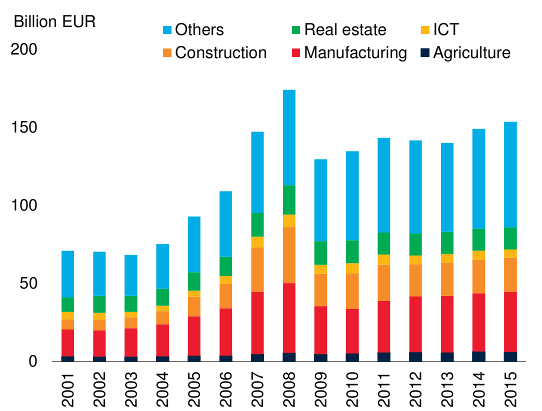
FIGURE 2.2.1.2 Investment decomposition, 2010-15

After the global financial crisis, public investment growth slowed or turned negative across the region. In Central Europe, the slowdown in investment was driven mainly by weak manufacturing sector investment.

A. Contributions to investment growth



B. Contribution to investment in Central Europe



Sources: Haver Analytics, International Monetary Fund, World Bank.
A. Investment growth rates are growth rates of subgroup aggregated gross fixed capital formation in constant 2010 U.S. dollars.
B. EU4 (Bulgaria, Hungary, Poland, Romania). Sectorial allocation of investment is not available for other countries.

What are current and prospective investment needs?

Infrastructure needs are sizable across the ECA region. The additional investment needed to reach the investment levels of economies at similar stages of development has been estimated at 1.3 percent of GDP per year, on average (EBRD 2015a; Figure 2.2.1.3).[1] Investment priorities vary widely across the region.

- *Russia* has implemented important upgrades in certain types of infrastructure, especially railways, mobile-cellular telephone networks, and airlines. However, the overall quality of infrastructure lags many EMDEs at similar levels of development. Roads, port and air transport infrastructure, and electricity supply all need considerable upgrading. The energy extraction sector requires an estimated $1.9-$3.3 trillion in investment between 2014 and 2035, while the power generation sector requires $600 billion (International Energy Agency 2014; Russian Investment Agency 2015).

- Infrastructure in *Turkey* exceeds average EMDE quality, but it has come under pressure as strife in neighboring countries has brought waves of immigrants: Turkey currently accommodates about 56 percent of all registered Syrian refugees. Annual energy investments of $12 billion are required to meet the country's development goals, to diversify the sector, and to help narrow Turkey's current account deficit by reducing energy imports (Winrow 2015; Republic of Turkey, Ministry of Energy and Natural Resources 2014). Turkey plans to increase renewable sources of energy, including nuclear, and improve energy efficiency (EBRD 2015b). From 2014 to 2018, total infrastructure investment needs are estimated at $350 billion (EBRD 2015b).

- For landlocked *Central Asia*, developing and upgrading infrastructure are critical for connectivity and reducing dependence on extractive industries. Investment in the energy sector will help to improve electricity access, a major concern for business (ADB 2016). Waste water systems in rural areas are also underfunded.

- In *other countries* in the ECA region, port, road, and railway infrastructure needs improvement, and logistics infrastructure needs to be upgraded to foster trade and investment (Bosnia and Herzegovina, Bulgaria). Border bottlenecks should be addressed and customs infrastructure improved. Upgrading water supply and irrigation systems will enhance productivity in agriculture and reduce environmental degradation (Azerbaijan, Bosnia and Herzegovina, Serbia, Uzbekistan).

[1] In addition to 24 countries in ECA region, the estimate includes the Arab Republic of Egypt, Estonia, Jordan, Latvia, Lithuania, Mongolia, Morocco, the Slovak Republic, Slovenia, and Tunisia.

BOX 2.2.1 Recent investment slowdown: Europe and Central Asia *(continued)*

Initiatives are already underway to improve infrastructure in the region:

- In *Russia,* for example, several hundred infrastructure projects were announced in the past five years, with more than half scheduled for completion by 2020. These projects are mostly in more densely populated western Russia. The largest allocations are for transport infrastructure (especially high-speed rail, and road and bridge construction). But there are also a large number of projects to improve the supply of utilities (electric power, gas, and water).

- *Turkey* has initiated several public-private partnership (PPP) projects, including the Caspian and Middle Eastern oil and gas pipeline and the $10.2 billion Istanbul Grand Airport. *Countries in Central Asia*—aspiring to become an overland transit and energy hub linking Chinese and European markets—has initiated investment projects in energy and transport sectors. In the energy sector, major projects include a pipeline from Turkmenistan to India, gas sector development in Uzbekistan, and hydroelectric power in Tajikistan. In the transport sector, key projects include highways in Kazakhstan, railroads linking Tajikistan and Kyrgyz Republic to China and the Islamic Republic of Iran, ports in Turkmenistan and Kazakhstan, and an airport in Kyrgyz Republic.

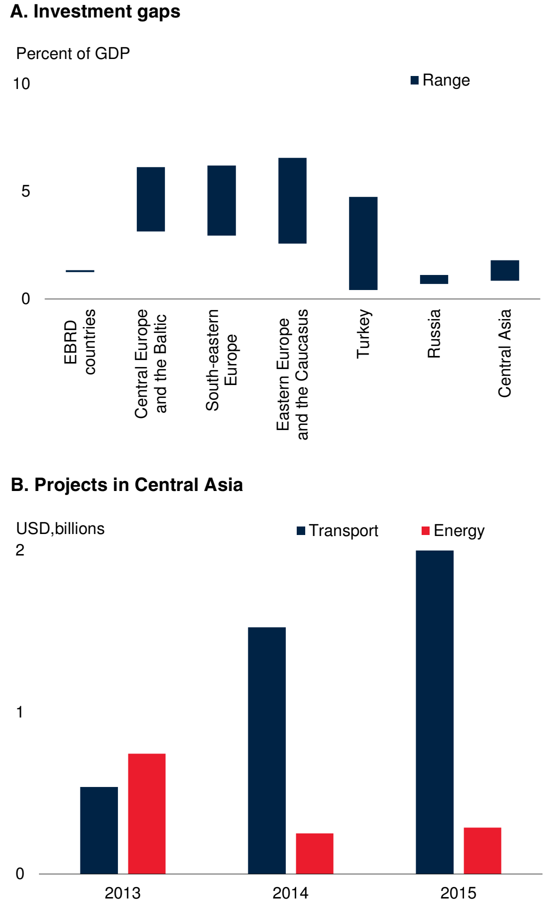
- In *Central and South Eastern Europe,* the investment pipeline largely reflects EU funding to further integrate the EU member states of the region with Western European countries.

Climate adaptation and energy efficiency. ECA is an energy-intensive region that relies heavily on non-renewable energy (Figure 2.2.1.4). Belarus, Bosnia and Herzegovina, and Turkey are implementing policy reforms (such as cost-based energy pricing) and investments in both public infrastructure and private industry, including renewable energy and energy efficiency, in partnership with the World Bank. Efforts to adapt to climate change include improved water resource management (flood protection, water loss reduction, irrigation efficiency) in Kazakhstan; climate-smart agriculture (switching to more resilient crops) in Tajikistan; and better weather forecasting and climate change monitoring in Russia.

Education and health. The region has made significant advances in the area of human development, including reductions in child mortality rates. Many countries in the region have achieved universal primary enrollment and gender parity in both primary and secondary education, and literacy rates are high. On average, the ECA region scores above average among EMDE regions in several education and health indicators. Nevertheless, shortcomings remain. Levels of learning achievement are low in several countries, and socio-economic and ethnic disparities in education persist. Among the basic education indicators, regional gaps are most apparent for math and

FIGURE 2.2.1.3 Investment gaps and projects

Amid sizable investment gaps across the region, large-scale infrastructure investment projects are underway.

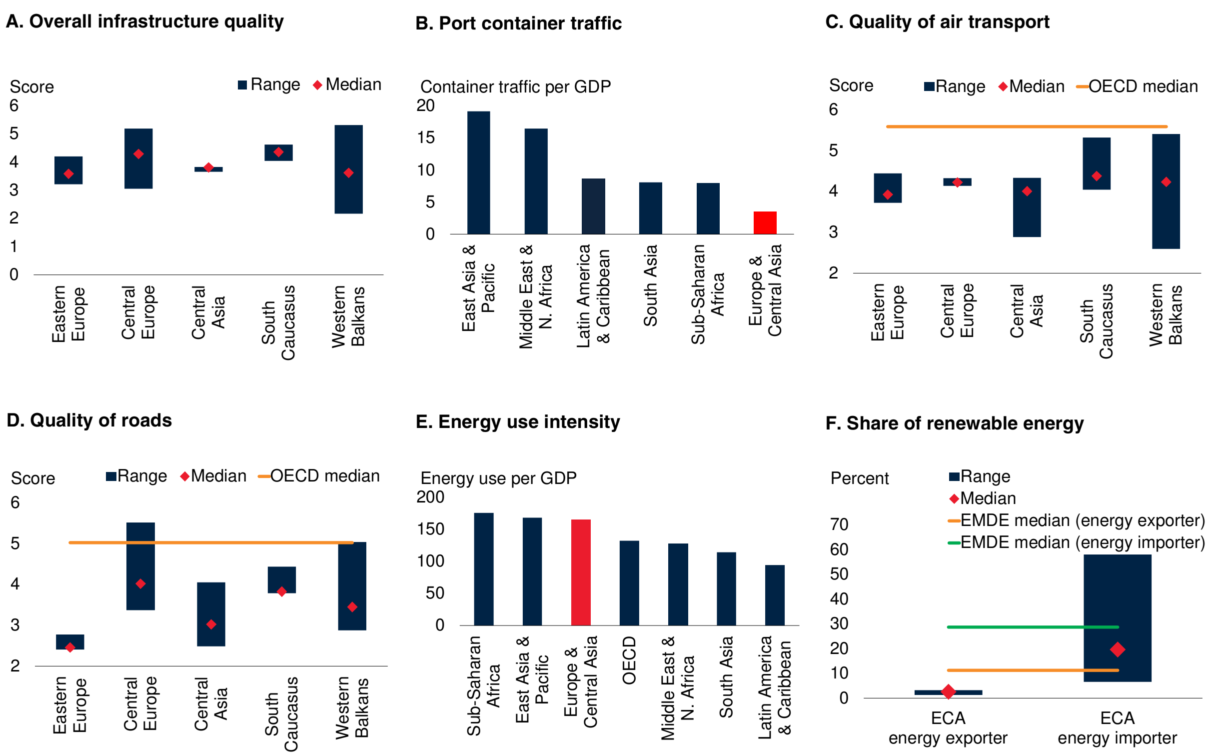


Sources: Central Asia Regional Economic Cooperation (CAREC), European Investment Bank.
A. Range of different investment gap estimates for each region from EBRD (2015a). EBRD countries includes Estonia, Latvia, Lithuania, the Slovak Republic, Slovenia Mongolia, Egypt, Jordan, Morocco, Tunisia in addition to 24 countries in ECA region. Financing gap for Central Asia and the Caucasus includes all infrastructure financing requirements that are not covered by national governments. For Central Asia, the range is GDP weighted average for Azerbaijan, Kazakhstan, Kyrgyz Republic, Mongolia, Tajikistan, and Uzbekistan.
B. Total value of approved CAREC related projects in Azerbaijan, Kazakhstan, Kyrgyz Republic, Mongolia, Pakistan, Tajikistan and Uzbekistan.

BOX 2.2.1 Recent investment slowdown: Europe and Central Asia *(continued)*

FIGURE 2.2.1.4 Infrastructure indicator

The quality of infrastructure in the most of the region is substantially below OECD average. Investment gaps remain large in transportation and energy. Port container traffic is limited, highlighting the region's reliance on road, air, and rail transport. The quality of air and road transport infrastructure remains well below OECD averages in most of the region. The region is energy intensive and heavily reliant on non-renewable energy.



Sources: EBRD (2015a), Haver Analytics, World Bank, World Economic Forum.
A. The score is overall quality of infrastructure. The score from 1 to 7 (best). Investment is the share of fixed capital formation as a percent of GDP. OECD average is the average investment share of OECD countries from 1990 to latest.
B. Regional sum of container port traffic (TEU: 20 foot equivalent) per current USD GDP in millions in 2014.
C.D. The score is from 1 to 7 (best). The OECD and EMDE average are the simple average of all the countries in the respective subgroupings.
E. Regional aggregated number. Data are in 2014 or latest available data. GDP data are in constant 2011 "international dollars."
F. Share of renewable energy consumption as percent of total final energy consumption in 2012. EMDE averages are the simple average of all the countries in the respective subgroupings.

science education. The region scores well below the EMDE average on attracting and retaining talent (Figure 2.2.1.5). Building a highly skilled workforce will require improving the quality of education, investing in on-the-job training, and using talent more effectively.

Which policies can help address investment needs?

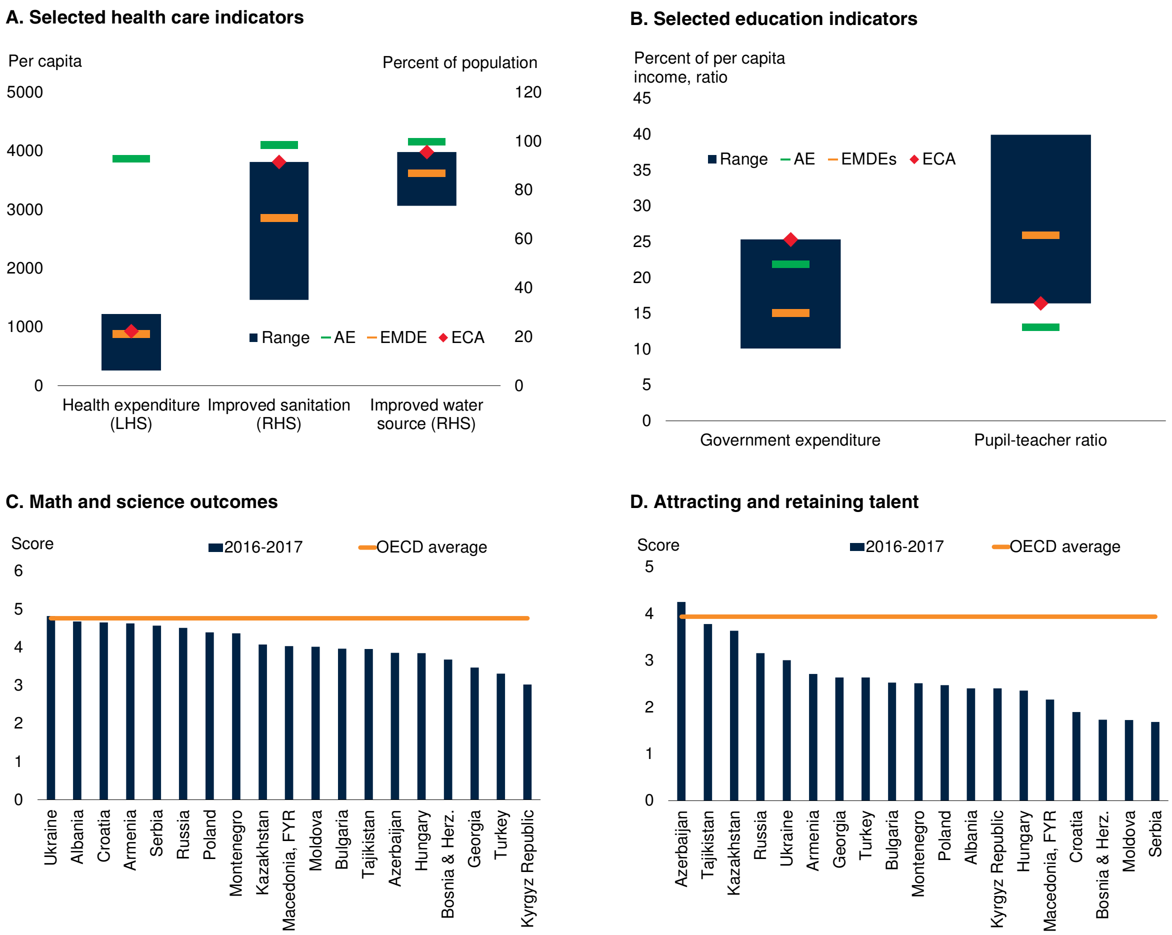
Unmet investment needs limit growth in the region, along with governance, financial, and labor market obstacles (World Bank 2015e-h; World Bank and Vietnam 2016; World Bank 2016h; EBDR 2015a). While policy priorities depend on country circumstances, appropriate cyclical and structural policies are needed in all cases to raise investment growth (Chapter 3). Fiscal policy could help most directly by expanding public investment while monetary policy could boost activity by lowering financing costs. Structural reforms could address factors holding back private investment, including by boosting productivity and aggregate growth prospects and improving the business climate.

Many EMDEs in the ECA region remain under pressure to consolidate their fiscal positions to reduce high debt-to-GDP ratios and ensure long-term fiscal sustainability (Georgia, Hungary, Chapter 2). This constrains their ability to finance public investment and places a premium

BOX 2.2.1 Recent investment slowdown: Europe and Central Asia *(continued)*

FIGURE 2.2.1.5 Human development indicators

Health and educational expenditure is highest among EMDE region and close to the OECD average. The region made significant advances in the area of human development. Nevertheless, important shortcomings remain. Among the basic education indicators, the region scores below the OECD average in math and science outcomes. The region also lags behind both the OECD and the EMDE average in attracting and retaining talent.



Sources: Haver Analytics, World Bank, World Economic Forum.
A. Blue bars denote range of unweighted regional averages across EMDE regions. Health expenditure per capita in purchasing power parity terms, unweighted averages of 199 EMDEs, 34 AEs, and 19 ECA economies. Access to improved sanitation facilities (in percent of population), unweighted averages for 150 EMDEs, 33 AEs, and 22 ECA economies. Access to improved water sources (in percent of population), unweighted averages for 148 EMDEs, 34 AEs, and 22 ECA economies. Latest available data available during 2011-15.
B. Blue bars denote range of unweighted regional averages across EMDE regions. Government expenditure per primary student (in percent of per capita income), unweighted averages of 87 EMDEs, 32 AEs, and 10 ECA economies. Pupil-teacher ratio in primary education (headcount basis), unweighted averages for 165 EMDEs, 31 AEs, and 20 ECA economies. Latest available data available during 2011-15.
C.D. The score is from 1 to 7 (best). The OECD and EMDE average are the simple averages of all the countries in the respective subgroupings.

on reforms that encourage private investment. Only a few regional economies can tap debt markets to finance infrastructure, while weak domestic banking systems and underdeveloped capital markets restrict the ability of governments to borrow domestically.

With weak growth, limited fiscal resources, and net capital outflows, the gap between infrastructure needs and the ability of governments to meet those needs may widen. This places a premium on measures to improve investment efficiency and to obtain funding from multilateral sources or the private sector.

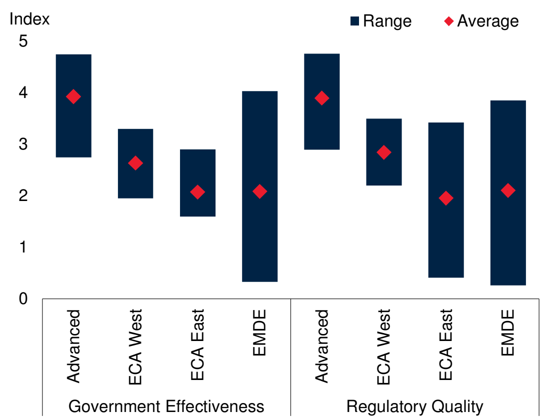
Investment efficiency. Effective public investments can meet needs with less cost (Dabla-Norris et. al. 2012), but regional institutional capacities fall behind the standards in

BOX 2.2.1 Recent investment slowdown: Europe and Central Asia *(continued)*

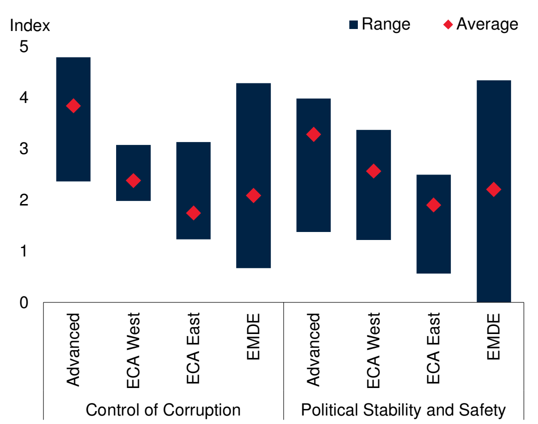
FIGURE 2.2.1.6 Institutional quality

Various measures of institutional efficiency in the ECA region are below the advanced-economy average. The western part of the region performs better than the eastern part on every measure. Governance and stability indicators in the eastern part of the region are often worse than the EMDE average.

A. Government and policy efficiency



B. Governance and stability



Source: World Bank.
A.B. The blue bars mark the range. EMDE is Emerging Market and Developing Economies. ECA stands for the Europe and Central Asia. The eastern part of the region comprises Eastern Europe (Belarus, Moldova, and Ukraine), South Caucasus (Armenia, Azerbaijan and Georgia), Central Asia (Kazakhstan, Kyrgyz Republic, Tajikistan, Turkmenistan, and Uzbekistan) and Russia. The western part of the region includes Central Europe (Bulgaria, Croatia, Hungary, Poland and Romania) and the Western Balkans (Albania, Bosnia and Herzegovina, Kosovo, FYR Macedonia, Montenegro, and Serbia), and Turkey. Scores range from 0 (not efficient) to 5 (efficient). Data from 2015 or latest available data.

advanced economies in this area (Figure 2.2.1.6). The eastern part of the ECA region ranks particularly low in relevant measures, including social stability, government effectiveness, and corruption. The efficiency of investments can be enhanced through a strategic, rigorous and transparent project selection mechanism and through strong institutions able to fund, manage, execute and monitor project implementation (Chapter 3).

Private funding. Policy efforts can be geared toward developing private funding sources for investment. Many countries still lack adequate frameworks for effective public -private partnerships (PPP), which can improve the effectiveness of public investment (Engel, Fischer, and Galetovic 2014). Capital market reforms can help channel domestic savings towards private investment (EBRD 2015a).

Multilateral funding sources. The region, especially the South Caucasus and Central Asia, will continue to depend on financial support from multilateral development institutions like the European Bank for Reconstruction and Development (EBRD), the Asian Development Bank (ADB), and the World Bank. Countries in Central Asia will likely be the largest beneficiaries of China's "One Belt, One Road" (OBOR) initiative, due to their locations and natural resource abundance. EU structural funds will continue to play an important role in closing investment gaps in Central and South Eastern Europe.

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