

## 2. INTERNATIONAL ECONOMIC AND FINANCIAL DEVELOPMENTS

**(6) During the period, the expansion of the global economic activity moderated.** The maturity of the global economy cycle, the diminishing effects of supportive economic policies in advanced economies and the use of tariffs as instruments in trade disputes between the world's largest economies had a negative impact on the growth of trade and the global economy. The conditions in the financial markets of advanced regions tightened somehow over the last months, reflecting concerns over the escalation of trade tensions and expectations for a slowdown in economic growth. In financial markets of advanced regions, dynamics of developments have been diverse, while countries with weak macroeconomic structures and uncertain political climate have been characterized by a build-up of financial pressures. Global inflationary pressures remained subdued reflecting the fall in oil prices, but are expected to gradually rise as a result of spare capacities running up in the global economy. The global economy is expected to slow down even further in 2019 and stabilise thereafter, over the subsequent two years.

**(7) Most euro area member states recorded a positive annual economic growth, but the pace of growth slowed down during the last two quarters of 2018.** Economic activity is underpinned by the pickup in domestic demand, while trade activity contributed negatively. Labour market conditions continued to improve in most euro area countries and employment rose beyond pre-crisis level. As a result, the unemployment rate of this region fell to 7.9% at the end of 2018, the lowest since October 2008. Inflationary pressures subdued during the last months of the year, driven by the fall in oil and food prices. Under these circumstances, the European Central Bank (ECB) maintained the accommodative monetary policy stance, even though the quantitative easing program ended in December 2018.

**(8) In the European banking sector, lending continued to record positive and steady growth rates, albeit at moderate levels.** This performance was supported by still favourable financing conditions and increased demand for loans in all its categories. The overall fall in credit interest rates for all segments of customers and in most euro area countries reflects a more uniform transmission of ECB's accommodative monetary policy over the period.

**(9) Risks to economic outlook in euro area, overall, are assessed as moderated.** They are mainly related to the uncertainty of certain geopolitical developments, the risk of more trade barriers and higher volatility in financial markets. On the other hand, the still favourable financing conditions and the strengthening of domestic demand are expected to further support the



economic expansion of this region. The ECB has stated that its policies will remain accommodative and supportive of economic growth in the euro area.

Table 1. Selected macroeconomic indicators for the U.S. and euro area

	GDP change (annual %)				Annual inflation (annual %)		Unemployment (annual %)		Gross government debt (as a percentage of GDP)	
	Q3'18	Q4'18	2018p	2019p	Sep'18	Dec'18	Sep'18	Dec'18	Q2'18	Q3'18
U.S.	3.4	2.6	2.9	2.5	2.3	1.9	3.7	3.9	103.9	104.2
Euro area	1.6	1.1	1.6	1.7	2.1	1.6	8.0	7.9	86.3	86.1
Germany	1.2	0.6	1.3	1.6	2.2	1.7	3.3	3.3	61.5	61.0
France	1.3	0.9	1.5	1.6	2.5	1.9	9.1	9.1	99.1	99.5
Italy	0.6	0.0	0.6	0.9	1.5	1.2	10.4	10.3	133.1	133.0
Greece	2.1	1.6	:	:	1.1	0.6	18.6	:	177.4	182.2

Source: European Central Bank, Eurostat, p-forecasts (January 2019) of the IMF, BEA –Bureau of Economic Analysis). (U.S. Bureau of Labour Statistics). “:”: no available data.

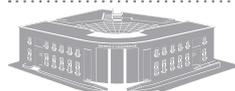
**(10) In the Western Balkans region, economic activity continued to expand but growth dynamics differed among the countries.** In 2018 Q3, the region's economy grew by 3.7%, year-on-year, driven mainly by growth in investments and private consumption. Growth rates slowed down compared to the previous quarter (growth at 4.3%), mainly driven by the decline of economic growth in Serbia. Economic expansion continued to stimulate the creation of new jobs, which led to the decline of unemployment in all the countries of the region. Despite the positive performance, labour market conditions continue to remain challenging and unemployment rates remain at double-digit values. Due to the low production base and low competitiveness, high trade deficit remains a source of weakness for all countries in the region.

**(11) Over the period, inflationary pressures in the countries of the region were moderate and central banks maintained an accommodative monetary policy.** Credit to the economy continued to grow positively and to support economic growth, whilst faster growth of credit to households remains a common feature of the countries of the region. Non-performing loans continued to trend downward in all countries, driven by the improvement of the framework for their treatment and mandatory write offs. The decline in the stock and the ratio of non-performing loans had a positive effect on banks' lending capacity.

Table 2 Selected macroeconomic and financial indicators for Western Balkans

	GDP (real, % annual)			Unemployment (in %)		Sovereign debt (% of GDP)		Credit growth (% annual)		Non-performing loans ratio (in %)	
	Q2'18	Q3'18	2018p	Q2'18	Q3'18	Q2'18	Q3'18	Q2'18	Q3'18	Q2'18	Q3'18
B&H	3.6	3.0	:	:	35.0*	38.6	37.2	6.8	6.5	9.3	9.4
N.Macedonia	3.0	3.0	2.1	21.1	20.8	40.3	40.3	6.0	6.8	6.5	6.3
Montenegro	2.8	3.1	3.9	14.7	14.4	62.8	61.8	12.8	10.7	7.0	6.7
Kosovo	4.2	4.5	4.1	29.4	30.7	16.9	:	10.8	11.6	2.7	:
Serbia	4.9	3.8	4.4	11.9	11.3	59.7	:	0.3	6.0	7.8	6.4
Albania	4.2	4.7	4.1	12.4	12.2	72.5	72.6	-1.8	-1.6	13.3	12.9

Source: European Commission, 'p'-forecasts January 2019; ':': no available data.



**(12) Financing conditions in global financial markets tightened and showed a higher volatility.** This performance reflected the uncertainty regarding the development of the global economy and the prevalence of expectations for tightening of the Federal Reserves' monetary policy. As a result, the main indices of capital markets showed instability and their spreads widened. In emerging markets, the dynamics were more diverse and often linked to specific factors. Capital inflows in these countries were moderated or turned negative, due to tighter liquidity conditions in advanced economies and heightened trade tensions.

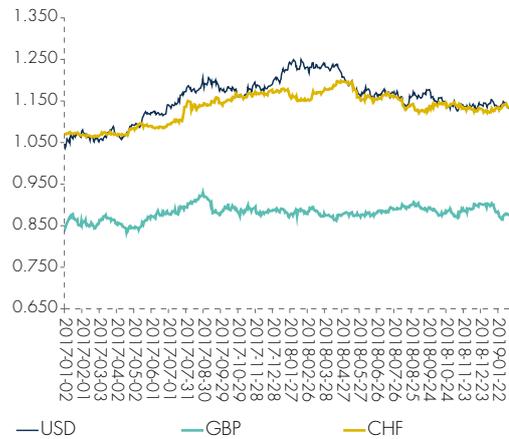
**(13) Less optimistic expectations about the performance of the global economy, or economy of major regions, are reflected in the performance of other markets.** Thus, in the foreign exchange markets, the euro followed a depreciation trend. Also, in commodity markets, metal prices and agricultural products fell over the period. The oil price was volatile during 2018 H2, but the downward trend strengthened in the last quarter of the year, standing at USD 55-60 per barrel.

Chart 7. Main indices in stock markets



Source: European Central Bank

Chart 8. Performance of euro exchange rate against other currencies



Source: European Central Bank

