Growth Returning to Emerging Europe and Central Asia, but Rising Food and Energy Prices Make Some Countries Vulnerable

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WASHINGTON, April 15, 2011 – Every country in the Emerging Europe and Central Asia (ECA) region1[1] is expected to grow in 2011, but some countries are vulnerable to rising food and energy prices, said the World Bank at a press briefing during the World Bank/IMF Spring Meetings 2011.

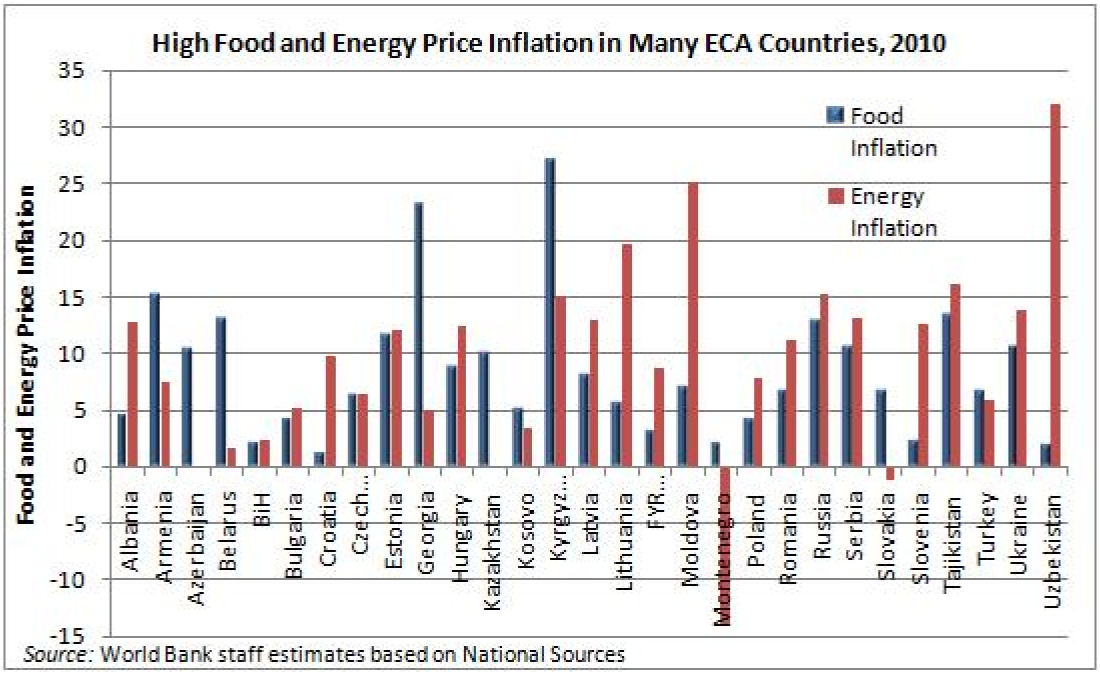
"Rising food and energy prices could push 5.3 million more people into poverty across Emerging Europe and Central Asia," said **Theodore Ahlers, Director of Strategy and Operations of the World Bank's Europe and Central Asia region**. *"For most countries in the region growth returned in 2010, following sharp declines in 2008 and 2009. However, the region's annual growth of around 4.5 percent was much lower than that of other regions in 2010, and projections for 2011–13 indicate only slightly stronger performance."*

Every country in the ECA region should record positive growth in 2011, however growth is more tepid in Central and Southeastern Europe than in the Commonwealth of Independent States (CIS), where high commodity prices have lifted net exports, increased remittance flows from migrants, and boosted private consumption. Yet, higher food and energy prices are a source of vulnerability for net importers as these threaten to increase poverty, particularly in lower income economies in the CIS, and add more pressures to macroeconomic policy management across the region.

Food and Energy Price Inflation

The global food and energy price increases represent an opportunity for commodity exporters. Large oil exporters Azerbaijan, Kazakhstan and Russia, which account for 15 percent of the world's oil production, are benefitting from higher prices which are boosting growth, current account and fiscal balances. At the same time food and energy price inflation represents an additional source of vulnerability for many net importers, particularly Armenia, Georgia, Kyrgyz Republic, Moldova, and Tajikistan

According to **Yvonne Tsikata, Director for Poverty Reduction and Economic Management of the World Bank's Europe and Central Asia region,** *"The poorest people in the region will suffer the most from high food and energy price inflation which reduces their purchasing power. They are particularly vulnerable to food price inflation as food represents a large share of the poor's consumption basket. In the most vulnerable countries, where poverty could increase the most, food price inflation averaged over 17 percent in 2010."*



Macroeconomic and Poverty Impact

Food and energy price inflation is highest among the lower income countries of the region. The highest food inflation rates were in the Kyrgyz Republic (27 percent) and in Georgia (23 percent). Energy inflation is also the highest among the lower income countries of the region.

Despite the nascent recovery, many ECA countries are still grappling with lower wages and higher unemployment resulting from the global crisis. If no countervailing measures are undertaken, and unemployment does not fall fast enough, the increases in food and energy prices could push 5.3 million more people across the region into poverty, with most of the higher poverty due to the food price increases.

Poverty could increase in some of the lower income countries of the region. Potential increases in poverty rates could reach 11 percentage points for the Kyrgyz Republic, 9 for Armenia and Georgia, 8 for Tajikistan, and around 5 percentage points for Moldova. Elevated food and energy prices will also put these countries' external balances under strain, along with Albania, Bosnia Herzegovina, Kosovo, and Montenegro, and hence increase their external financing needs.

Vulnerability and Policy Responses

The countries may need to expand the coverage and adequacy of their social assistance systems in order to protect the additional poor.

Most countries in ECA have some social assistance programs that directly target the poorest. According to **Tsikata**, *"In order to help cushion the impact of higher prices, governments in the region need to ensure that programs targeted to the poor get more funding as necessary, from government budgets. More funding will allow governments to increase the number of people covered in their programs and to better offset their losses."* Fully compensating the poorest 20 percent in countries for the effects of the food and energy price inflation, in countries where poverty is expected to increase the most, could require up to 1 percent of their GDP.

Some policies that were adopted in the region in reaction to the previous food and energy price hikes should be avoided in the face of this price rise.

"Trade restrictions on food exports and price controls are not the best way to protect poor consumers as they hinder longer term adjustment in markets and may worsen price volatility," said **Roumeen Islam, World Bank Economic Advisor and the main author of the report "Rising Food and Energy Prices in Europe and Central Asia".** *"The expansion of targeted social assistance systems should be the preferred method of protecting the poor."*

ECA's food and energy production is important for both regional and global markets. ECA wheat exports account for 25 percent of world wheat exports on average. Countries in the region could double their wheat production by cultivating more land — sustainably — and by increasing yields. Better irrigation and improved post-harvest logistics would help raise yields.

As the cost of energy is rising, ECA countries will need to reform their pricing policies and reduce their energy intensity. Rising oil and gas prices will push up energy trade deficits which are already high for some countries in the region. In 2010, the energy trade deficit was 20 percent of GDP in the Kyrgyz Republic, followed by 14 percent in Georgia and 11 percent in Ukraine. The energy intensity has declined in all ECA countries but can be further reduced with policies and investments that encourage energy efficiency and renewable energy.

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