

# Eastern Europe

Manufacturers across Eastern Europe recovering well in 2010, but Russian and Turkish producers continue to struggle

## Key findings

- **Emerging EU manufacturing sector showed robust recovery in February.**
- **But producers in other emerging economies in the region fared less well.**
- **Exports and productivity help explain the regional disparities.**

The latest PMI data covering emerging markets in Eastern Europe and Central Asia showed differing recovery paths at the start of 2010. Manufacturers in the EU economies of Poland, the Czech Republic and Hungary all reported strengthening expansions in February<sup>1</sup>. A weighted average PMI Output Index for the three countries signalled the fastest rate of expansion since March 2007, consistent with manufacturing output rising at a quarterly rate of growth in excess of 4%.

In January, official output data beat market expectations in Poland, the Czech Republic and Hungary, following the upbeat message from the PMIs. Industrial production increased by 8.5% yr/yr in Poland, beating expectations of 6.2% expansion. In the Czech Republic, output rose by 5.3%, surpassing a forecast of 2.5%. In Hungary, the annual rate of growth was 3.4%, much stronger than expectations of 0.2% expansion.

All three countries are showing signs of export-led recovery in 2010. In January and February, all three registered stronger average growth of new export orders relative to total new business, with Hungary seeing the strongest rate of new export order growth.

The revival in export demand comes despite recent strengthening of the zloty, forint and koruna against the euro, the single market which forms the main export destination for Eastern European manufacturers. That said, the currencies remain weaker than their pre-crisis exchange rates.

Chart 1: PMI Output Index<sup>2</sup> vs official data<sup>3</sup>

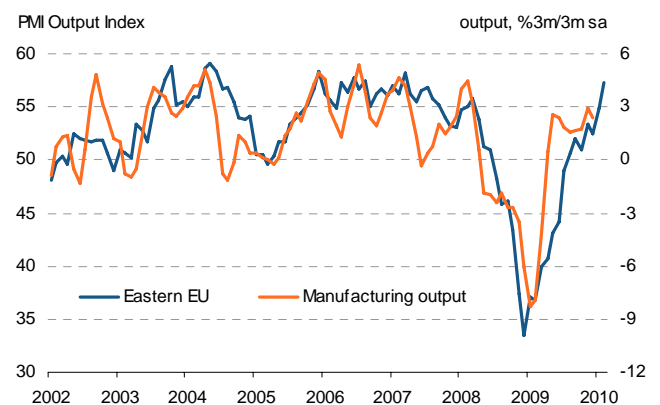
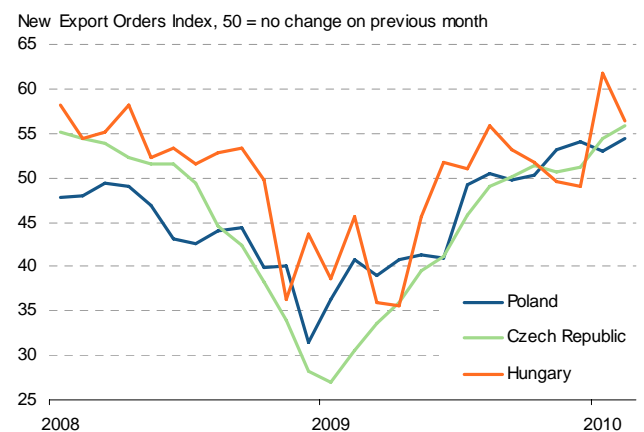


Chart 2: PMI New Export Orders Index



## Weakness evident in Russia and Turkey

However, PMI data suggest that major economies further east have experienced more lacklustre rates of

<sup>1</sup> Markit produces PMI data for Poland, the Czech Republic and Turkey for HSBC, and Russian PMIs for VTB Capital. The Hungarian PMI is produced by the Hungarian Association of Logistics, Purchasing and Inventory Management (HALPIM) and the Hungarian National Bank. The Hungary PMI data are compiled using a different methodology to Markit PMI data, and are included for comparative purposes only.

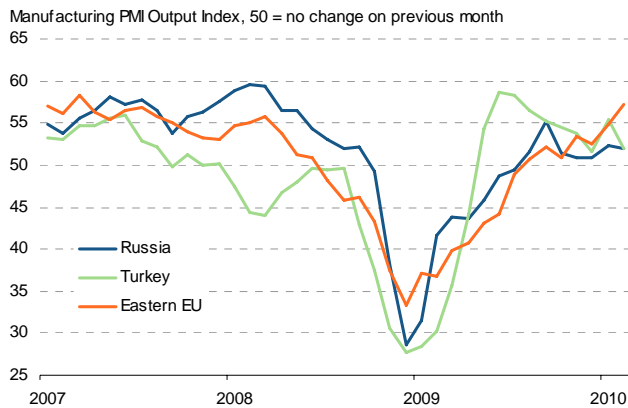
<sup>2</sup> Output Index calculated from Polish, Czech and Hungarian PMI data.

<sup>3</sup> Bulgaria, Czech Republic, Estonia, Latvia, Lithuania, Hungary, Poland, Romania.

manufacturing expansion. Russia's manufacturing sector, in particular, registered only marginal growth in February. Output rose for the seventh month running, but at a weakened pace compared to January. Importantly, Russian new export orders registered only a negligible expansion for the second month running. This suggests that Russian companies are struggling to be internationally competitive, and are not benefitting from resurgent Eurozone demand in the same way that Czech, Polish and Hungarian exporters are.

Turkey's manufacturing recovery also lost momentum in February. Having posted a marked rebound in manufacturing production in mid-2009, the February expansion was the second-weakest of the current ten-month growth phase. In contrast to the situation in Russia, however, the slowdown in Turkey appears to be centred on the domestic market, as new export business rose more sharply than total new orders.

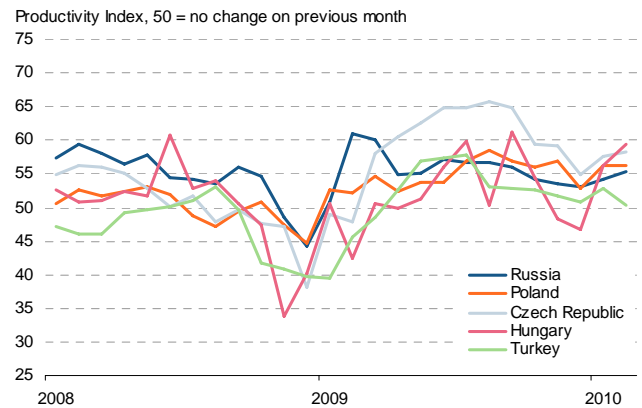
**Chart 3: Russia and Turkey fall behind Eastern European neighbours**



**Productivity trends**

The relative strength of the recoveries in the EU countries compared to Russia and Turkey can perhaps be explained at least to some extent by labour market productivity trends. The PMI data can be used as a guide to output per worker, by dividing the output index by the employment index and multiplying by 50 to form a diffusion index. In February, output per worker rose at the fastest rate in Hungary, followed by the Czech Republic and Poland. Russia and Turkey lagged behind, with the latter registering only a marginal gain.

**Chart 4: Productivity trends by country**



**Forthcoming data (March):**

- 1 April: VTB Capital Russia Manufacturing PMI
- 1 April: HSBC Turkey Manufacturing PMI
- 1 April: HSBC Poland Manufacturing PMI
- 1 April: HSBC Czech Republic Manufacturing PMI

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