

INTERNATIONAL MONETARY FUND

REGIONAL ECONOMIC OUTLOOK

EUROPE

Choosing Growth: Reforms for
Innovation, Scale, and Resilience

2026
OCT



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Contents

Executive Summary	<u>v</u>
Choosing Growth: Reforms for Innovation, Scale, and Resilience	<u>1</u>
Europe Is Growing Slowly in Difficult Circumstances.....	<u>1</u>
Europe’s Critical Structural Challenges Remain	<u>5</u>
Outlook and Risks: Mediocre Growth Continues into the Medium Term.....	<u>9</u>
Macroeconomic Policies Will Need to Tread Carefully.....	<u>11</u>
Reforms for Innovation, Scale, and Resilience	<u>13</u>
Continuing the Energy Transition Will Build Resilience	<u>15</u>
Europe Needs to Fix the Fundamentals to Create the Conditions for Innovation and Scale to Sustain Higher Growth.....	<u>16</u>
CESEE Countries Need to Adapt Policies to Ensure Sustainable Growth.....	<u>18</u>
References.....	<u>20</u>

FIGURES

Figure 1. Recent Developments in Fossil Fuel Prices	<u>1</u>
Figure 2. Financial Conditions.....	<u>2</u>
Figure 3. Euro Area: Real GDP Growth Forecast from World Economic Outlook Vintages in 2026	<u>3</u>
Figure 4. Real GDP Growth Decomposition.....	<u>3</u>
Figure 5. Recent Developments in Inflation	<u>3</u>
Figure 6. Euro Area Inflation Expectations	<u>4</u>
Figure 7. EU Electricity Production by Input.....	<u>4</u>
Figure 8. Monetary Policy Developments	<u>5</u>
Figure 9. Fiscal Policy Developments.....	<u>5</u>
Figure 10. Europe’s Labor Productivity Gap to the United States	<u>6</u>
Figure 11. Intangible-Producing Sectors: Contribution to Labor Productivity Growth	<u>6</u>
Figure 12. AI Exports and Growth Surprises	<u>6</u>
Figure 13. EU Innovation Gaps	<u>7</u>
Figure 14. Industrial Electricity Prices	<u>7</u>
Figure 15. Europe Exports.....	<u>8</u>
Figure 16. External Competitiveness: CESEE	<u>8</u>
Figure 17. Concentration of Supply Chains.....	<u>9</u>
Figure 18. Medium-Term Growth Forecast.....	<u>10</u>
Figure 19. Medium-Term Inflation Forecast	<u>10</u>
Figure 20. Fiscal Balance	<u>11</u>
Figure 21. Long-Term Fiscal Sustainability	<u>12</u>
Figure 22. Gap between Expected Fiscal Adjustment and MTFSP Plans	<u>12</u>
Figure 23. Financial Sector Conditions	<u>14</u>
Figure 24. Volatility and Dispersion of European Electricity Prices.....	<u>15</u>
Figure 25. Levelized Cost of Energy by Source	<u>16</u>
Figure 26. EU Gains from EU and National Reforms	<u>17</u>
Figure 27. Potential GDP Gains from the 28th Regime Pillars	<u>17</u>

Figure 28. Innovation Gains under Scale-Up and Scale-Down Constraints.....	18
Figure 29. The Twin Deficits: CESEE	19
Figure 30. Unrealized Convergence Gains: Moldova and Western Balkans	19

TABLES

Annex Table 1.1. Real GDP Growth	22
Annex Table 1.2. Headline Inflation	24

Executive Summary

Europe's economy continues to grow, if at a slow pace, despite accumulating adverse shocks. This summer's heat wave and drought have added to the negative effects of high energy prices, and external tariffs remain elevated. However, growth is fragile, as large geopolitical and geoeconomic risks persist, defense and other public spending pressures mount, and sovereign yields are rising. In Central, Eastern, and Southeastern European (CESEE) countries, the energy shock has further strained the region's export-led growth drivers and added to preexisting price pressures in some countries. The economic costs of the war in the Middle East would have been worse without Europe's push toward renewable energy. This indicates what Europe can achieve when it acts together and with urgency. Nevertheless, even after energy supply eventually normalizes, Europe's structural weaknesses will hold back growth in the medium term. Slow potential growth is making Europe less resilient, so that the impact of even small shocks can be magnified and threaten recession.

At the heart of Europe's underlying growth problem is weak productivity, reflecting a lack of scale and innovation. Europe was once at the global productivity frontier, but it has gradually fallen behind. Although some reform efforts are underway, a still-incomplete European Union (EU) single market and national barriers make it harder for firms to adjust, scale up, and access a larger market. This also prevents firms from becoming more efficient and dampens incentives to invest. As a result, innovation remains incremental and concentrated in traditional, low-growth industries. These structural weaknesses in innovation and scale are becoming increasingly problematic, given that trade-driven growth is losing some momentum, particularly in CESEE countries, as manufacturing industries face tough competition from abroad. The resilience of the European economy is also threatened by a fragmented energy market, and reliance on fragile global supply chains, for fossil fuels and critical minerals, at a time when geopolitical tensions are high.

Macroeconomic policies will have to tread carefully. Growth is set to remain modest. Although crude oil prices are below the peak reached during the conflict, prices of refined products and natural gas remain painfully high. A period of above-target headline inflation is expected, even if medium-term inflation expectations remain anchored. Underlying price pressures in some CESEE countries, driven by strong wage growth and loose fiscal policy, could still make reducing inflation difficult. Policymakers will need to remain vigilant about a broadening of price pressures. Monetary policy may have to do more, and expansionary fiscal policy should be avoided, to keep pressure off inflation. If energy price relief policies are extended, or new policies introduced, they should be tightly targeted at the most vulnerable and not distort energy prices, to preserve incentives to increase energy efficiency. Financial sector policymakers should pay close attention to the resilience of the system beyond banks, as a global correction of overstretched asset valuations and rising sovereign yields could have an impact on financial stability that is magnified through bank-nonbank linkages.

The key task now is to strengthen Europe's low-growth and shock-prone economy by addressing the region's structural challenges. Protectionist policies and broad-based interventions shielding Europe from changes in global commodity prices or international competition can only buy time and can introduce costly distortions. Moreover, although interventions to address supply-chain risks may be warranted, they need to be limited and based on careful cost-benefit analysis. Instead, Europe should choose higher and more robust growth through reforms for innovation, scale, and resilience. Continuing the energy transition is imperative to lower energy costs and reduce dependence on fossil fuel imports. For firms to scale up and adjust, reforms need to be made at the domestic level to remove inefficiencies, and continue forcefully at national and EU levels, to complete the single market and reduce the remaining barriers that segment product markets and hamper capital and labor mobility.

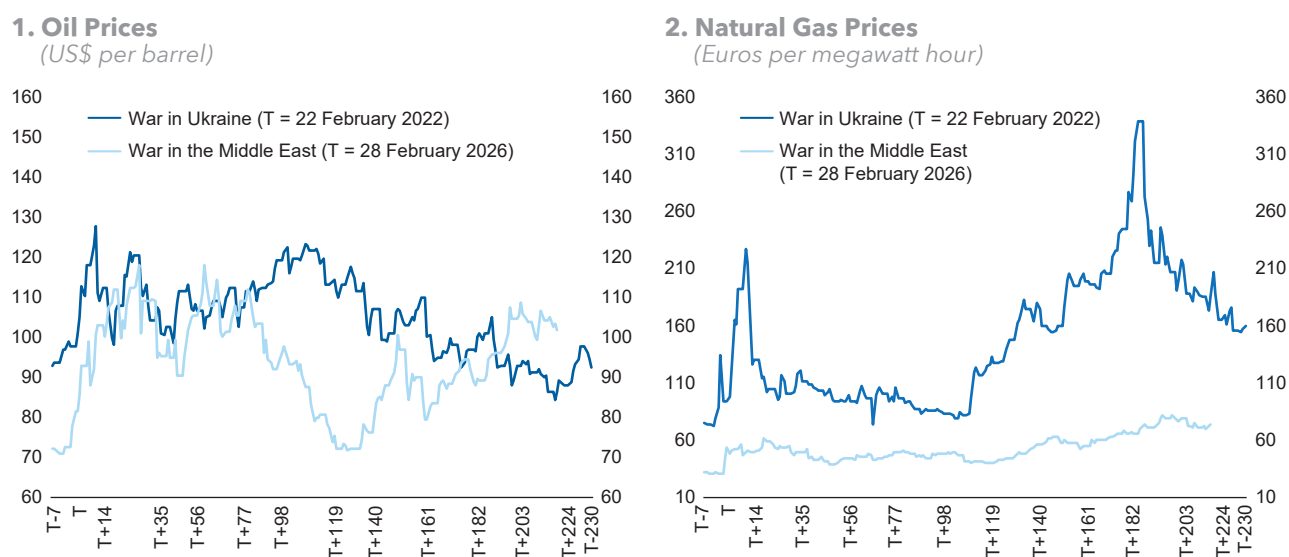
These reforms will also lift the constraints on transformative innovation. In CESEE countries, given the erosion of cost-competitiveness, policymakers should seek growth through investment in skills and by reforms that improve labor market reallocation, strengthen competition, and foster innovation. This will help firms diversify further into new products and markets, and strengthen their performance in external markets. EU candidate countries need ambitious reforms to seize the transformative opportunity offered by EU accession.

Choosing Growth: Reforms for Innovation, Scale, and Resilience^{1,2}

Europe Is Growing Slowly in Difficult Circumstances

The fallout from the war in the Middle East and the summer heatwave and drought have been the latest in a series of adverse shocks that have hit the European economy in recent years. The conflict follows the COVID-19 pandemic, Russia's invasion of Ukraine, and the increase in trade tensions. The significant disruption of the global supply of fossil fuels has been driving up the prices of oil and gas (Figure 1). Crude oil prices remain elevated and volatile, although below the peak reached after the war began. Meanwhile, natural gas prices remain well above prewar levels, but still they are significantly below the levels reached after Russia's invasion of Ukraine. Europe has lower than usual buffers as winter approaches, with gas storage levels below the norm for this time of year, potentially amplifying the impact of elevated natural gas prices on electricity and heating costs. Europe has also experienced record-high temperatures and below-average rainfall in recent months, affecting agriculture, river transport, and electricity generation, with the prospect of more extreme weather to come.

Figure 1. Recent Developments in Fossil Fuel Prices



Source: Bloomberg L.P.

Note: Data as of October 1, 2026. Oil prices are measured using the ICE (Intercontinental Exchange) Brent front-month continuous futures price (US\$ per barrel, trade price). Natural gas prices correspond to the Dutch Title Transfer Facility month-ahead contract, expressed in Euros per megawatt hour, the main benchmark for European wholesale gas markets.

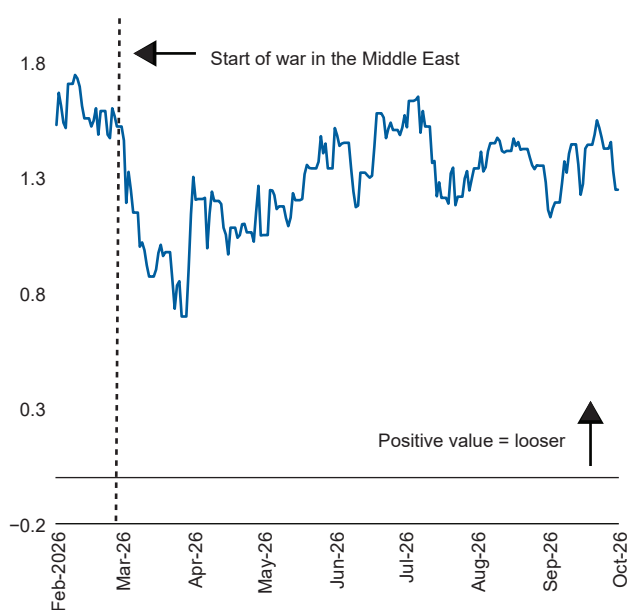
¹ This report was prepared by Xin Tang, with support and contributions from Ben Park and Pierre Rouillard, under the supervision of Andrew Hodge and the overall guidance of Stephan Danninger, Wenjie Chen and Helge Berger. Many other staff whose work is featured in the report have also provided valuable inputs. Agnesa Zalezakova has provided excellent administrative support.

² In this report, unless otherwise indicated, advanced economies (AEs) include Austria, Belgium, Cyprus, Denmark, Finland, France, Germany, Greece, Iceland, Ireland, Israel, Italy, Luxembourg, Malta, the Netherlands, Norway, Portugal, San Marino, Spain, Sweden, Switzerland, and the United Kingdom. In the main text, AE and AE excluding CESEE are used interchangeably. Central, Eastern, and Southeastern Europe (CESEE), for the purpose of this report, refers to CESEE excluding Belarus, Russia, Türkiye, and Ukraine, which includes Albania, Bosnia and Herzegovina, Bulgaria, Croatia, Czech Republic, Estonia, Hungary, Kosovo, Latvia, Lithuania, North Macedonia, Moldova, Montenegro, Poland, Romania, Serbia, Slovak Republic, and Slovenia.

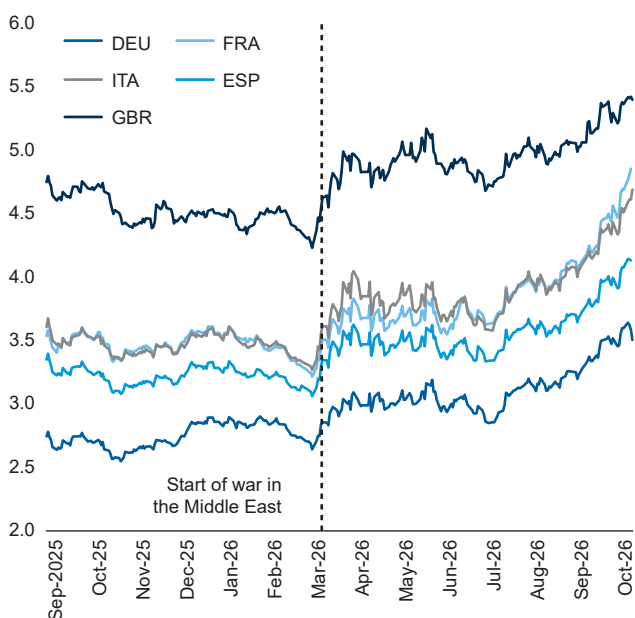
Economic activity has held up better than expected, despite the energy shock and a difficult summer. The European economy entered the year with positive momentum, but the higher energy prices have squeezed household disposable income and raised the costs of doing business. This has weighed on private consumption and kept investment subdued. Higher borrowing costs and stricter lending standards on the back of higher central bank interest rates (for example, the euro area and the Czech Republic) have been adding further headwinds (Figure 2). Sovereign yields have also moved up, reflecting higher inflation, as well as other factors including market concern over high debt levels and spillovers from the US market movements. Low water levels and high temperatures during the summer have been a modest additional drag on aggregate economic activity, with a more pronounced impact in the most affected sectors. Even so, these headwinds did not fully offset Europe’s earlier momentum. Euro area growth (excluding Ireland) was about 1.2 percent (seasonally adjusted annual rate, SAAR) in the second quarter of 2026, which is higher than that anticipated in the April *World Economic Outlook* forecast after the war (Figure 3).³ Growth in CESEE countries also held steady, supported by robust domestic demand (Figure 4). Across Europe, high-frequency indicators for the third quarter are mixed; some point to continued momentum early in the quarter, including business surveys, but retail sales declined in the euro area and industrial production softened.

Figure 2. Financial Conditions

1. Euro Area Financial Conditions Index
(Z-score deviation from precrisis level)



2. 10-Year Government Bond Yield
(Percent)

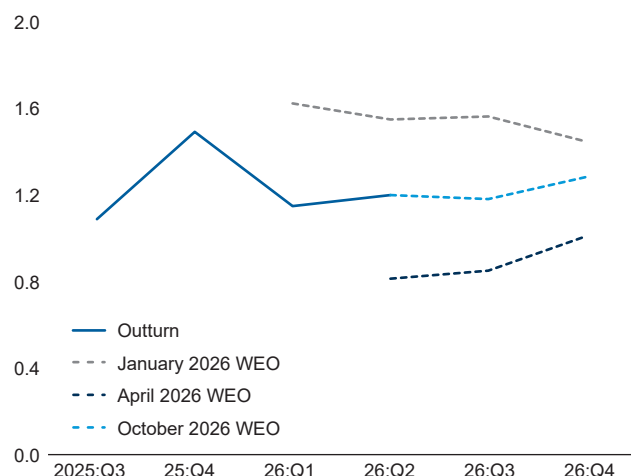


Source: Bloomberg L.P.

Note: Data as of October 1, 2026. In panel 1, precrisis level is defined as period between 1999 and July 1, 2008. Data labels in the figure use International Organization for Standardization (ISO) country code.

³ Ireland’s GDP growth tends to be more volatile than other euro area countries because of the large role of multinational companies.

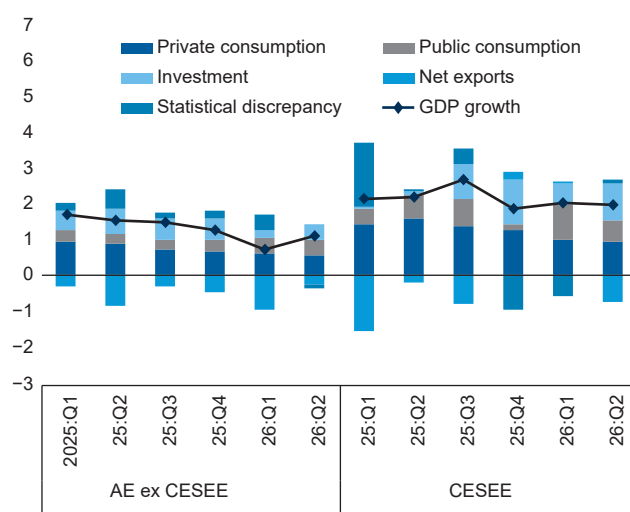
Figure 3. Euro Area: Real GDP Growth Forecast from World Economic Outlook Vintages in 2026
(Percent)



Source: IMF, World Economic Outlook.

Note: The data exclude Ireland. WEO = World Economic Outlook.

Figure 4. Real GDP Growth Decomposition
(Year-over-year percentage change)



Source: IMF, World Economic Outlook; IMF staff calculations.

Note: AE = advanced economy; CESEE = Central, Eastern, and Southeastern European.

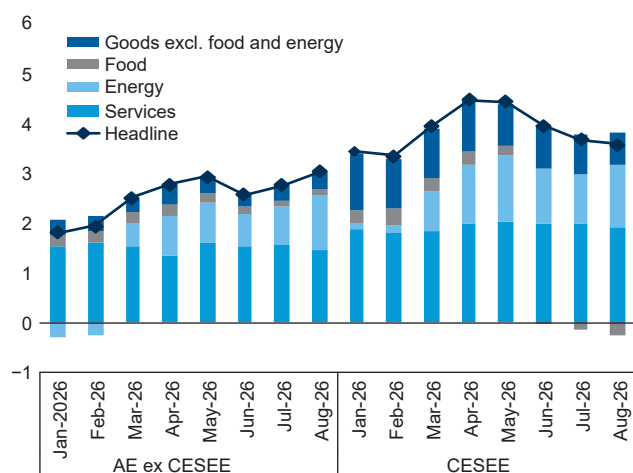
Headline inflation has surged, but underlying inflationary pressures have remained contained so far (Figure 5).

Headline inflation has not translated into a significant increase in core inflation, as medium-term inflation expectations have stayed well anchored (Figure 6), and higher energy prices have not been fully passed through to other consumer prices. In the euro area, where inflation was broadly at target when the war began, inflation has increased from 1.9 percent year over year in February to 3.8 percent year over year in September, whereas core inflation has been more stable, hovering about 2.1–2.3 percent year over year throughout the year so far. Inflation also increased on average in CESEE countries after the outbreak of the war, before easing slightly because of

Figure 5. Recent Developments in Inflation

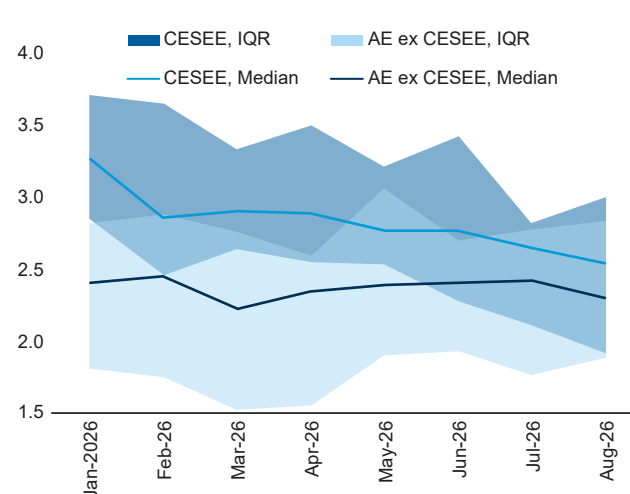
1. Inflation Decomposition

(Year-over-year percentage change)



2. Core Inflation

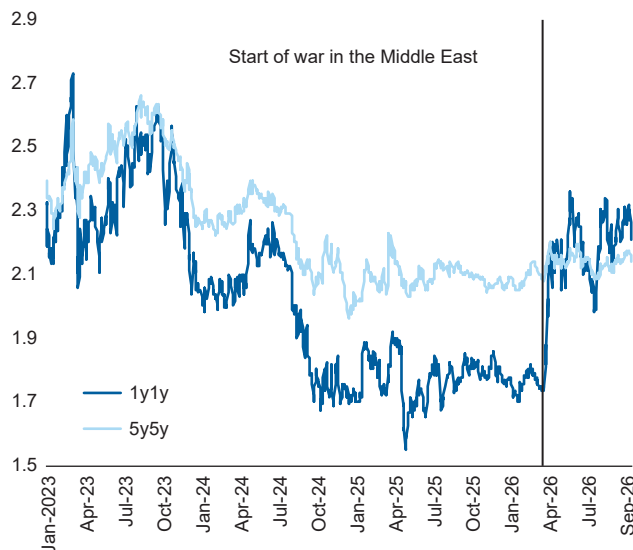
(Year-over-year percentage change)



Sources: Haver Analytics; and IMF staff calculations.

Note: In panel 2, IQR denotes the inter-quartile range (difference between third and first quartiles). AE = advanced economy; CESEE = Central, Eastern, and Southeastern European; IQR = inter-quartile range.

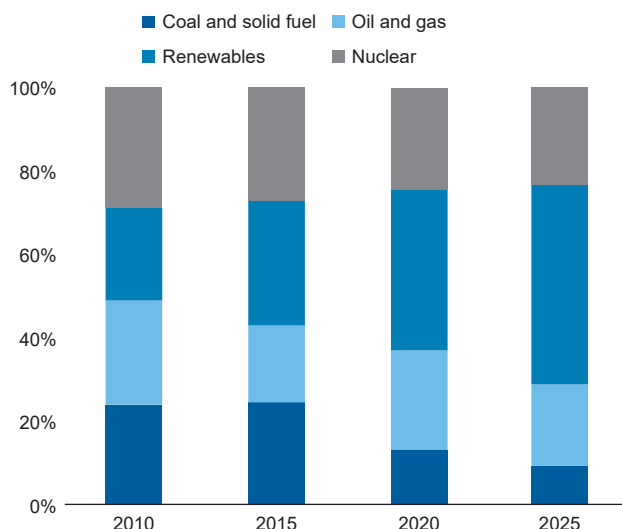
Figure 6. Euro Area Inflation Expectations
(Percent)



Source: LSEG Workspace.

Note: Based on market-implied forward inflation swap rates.

Figure 7. EU Electricity Production by Input
(Percent)



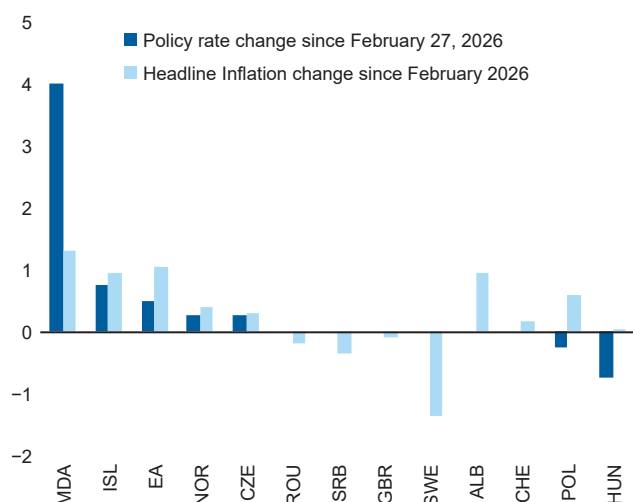
Source: Eurostat.

declining food prices in some countries. However, there are important differences across the region. In some countries, inflationary pressure was already building at the onset of the conflict, reflecting loose fiscal policy, as well as strong growth of wages and credit, with the energy shock having now added to these price pressures (for example, Bulgaria and Romania). In other countries, inflation was at or below target and the inflationary impact of the conflict has been more modest (for example, Hungary).

The economic impact of the conflict would have been worse if not for the progress Europe has made toward achieving the energy transition in recent years. Analysis based on the IMF's Carbon Pricing Assessment Tool model indicates that Europe's adoption of renewables, combined with improved energy efficiency, has reduced the impact of the energy shock on households' energy spending by about 8 percent. As of 2025, close to half of EU electricity generation comes from renewables (wind, solar, hydropower, bioenergy, and waste) (Figure 7)—much more than the United States, where renewables account for one-quarter of generation, and China, which is however closing the gap quickly. This evolution has reduced Europe's dependence on imported fossil fuels, helping to cushion the impact of disruptions caused by the war. It is a testament to what is possible when European countries work together to strengthen efficiency and resilience.

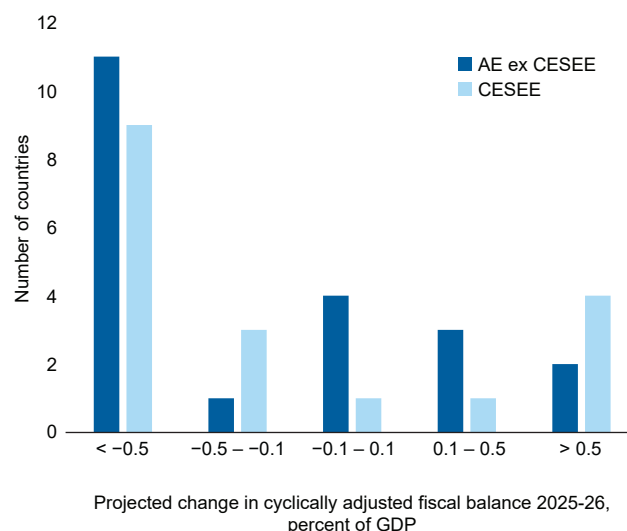
Relatively benign cyclical conditions at the outbreak of the conflict, and a broadly appropriate macroeconomic policy response, have helped to contain underlying inflation. Demand pressures had receded, and labor market slack had increased over the past three years. At the same time, macroeconomic policymakers have been careful not to stoke broader price pressures. Central banks have either raised rates or paused their easing cycles (Figure 8). Fiscal policy has avoided a large discretionary stimulus in the majority of countries and has been broadly neutral on a GDP-weighted basis, although deficit levels remain high in some cases (Figure 9). All countries have introduced measures to provide households and firms with relief from higher energy prices, but these have been far less costly (about 0.3 percent of GDP on average in the EU as of mid-September) than those implemented after Russia's invasion of Ukraine.

Figure 8. Monetary Policy Developments
(Percentage points)



Sources: Haver Analytics; and National Central Banks.
Note: Data as of October 1, 2026. Data labels in the figure use International Organization for Standardization (ISO) country codes. The decreasing inflation in Sweden reflects a marked appreciation of the Swedish Krona in 2025 and several one-off factors in 2026, including a VAT cut on food, dental subsidies, fuel tax cuts, public transportation subsidy, etc. (IMF 2026b).

Figure 9. Fiscal Policy Developments



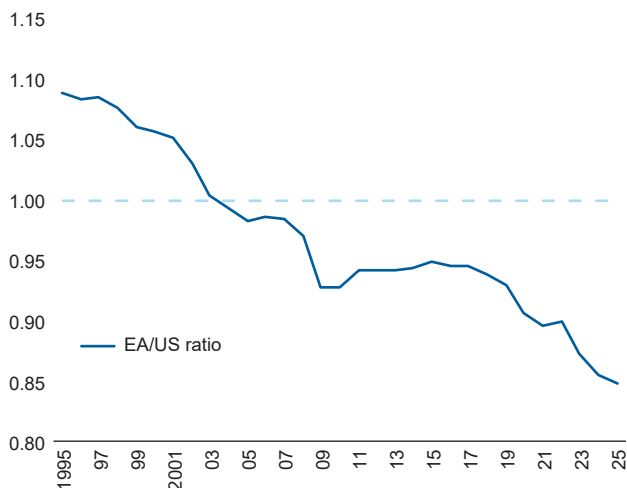
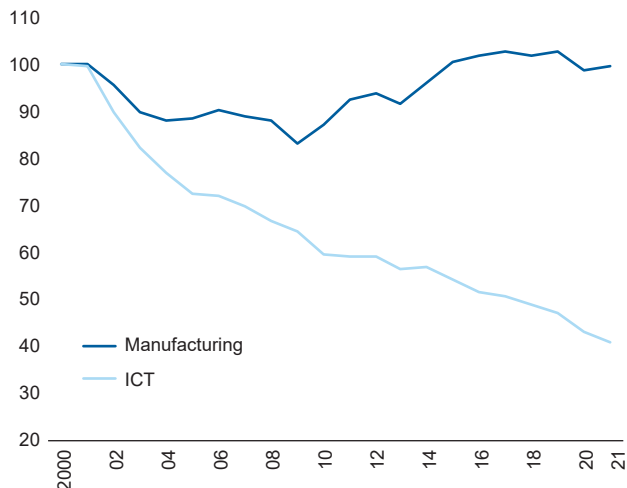
Sources: IMF, World Economic Outlook.
Note: The grouping reflects fiscal stance: >0.5, tight; 0.1-0.5, moderately tight; -0.1-0.1, broadly neutral; -0.5--0.1, moderately loose; <-0.5, loose. AE = advanced economy; CESEE = Central, Eastern, and Southeastern European.

Europe's Critical Structural Challenges Remain

Although Europe has weathered the conflict relatively well, the underlying structural challenges of the European economy persist. The core weakness is sluggish productivity growth, which drags down potential growth and leaves Europe more susceptible to adverse shocks. With medium-term potential growth at about 1.1 percent, even modest shocks threaten to tip the euro area into recession, and at 1.3 percent, EU medium-term potential growth is not much higher either, despite stronger activity in CESEE economies. Although globalization has been a powerful engine of growth, weak productivity dynamics are now dampening Europe's performance in key export markets.

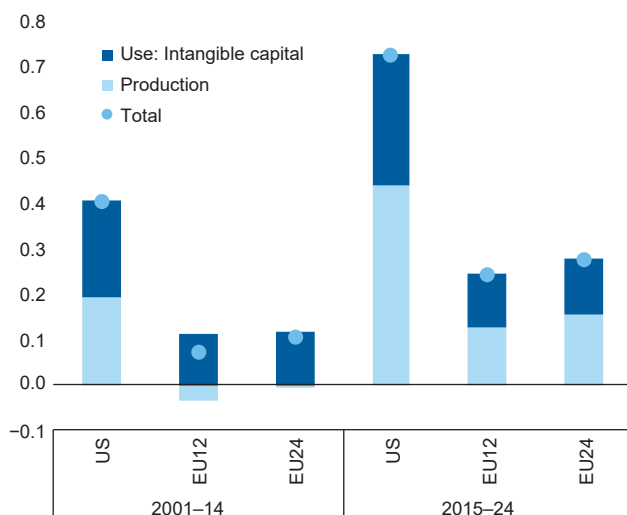
The EU was once at the global productivity frontier but has fallen behind (Figure 10, panel 1). Europe's labor productivity has been consistently falling behind in the information and communications technology (ICT) sector (Figure 10, panel 2).⁴ IMF analysis (Komatsuzaki and others, forthcoming) shows that the development and use of intangible capital, including early forms of artificial intelligence (AI), contributed about $\frac{3}{4}$ of a percentage point to labor productivity growth in the United States during 2015-24, more than twice as much as in the EU (Figure 11). The widening of the gap continues, as the region also appears to be missing out on the ongoing boom in AI-related investment and exports, which has provided some support to growth elsewhere, particularly in Asia (Figure 12). The growth of new AI-related patents has been slower in Europe than in the United States and China, indicating less AI development. Business surveys show that European firms have not adopted and used AI in their operations as deeply as US firms.

⁴ Europe's catching up to the US labor productivity in manufacturing in the early 2000s largely reflects stagnant US labor productivity. Atalay and others (2025) argue that the US total factor productivity growth in manufacturing is understated over this period by failing to fully capture quality adjustments. For the universe of listed firms, IMF (2024a) estimates that Europe's total factor productivity growth has underperformed the United States across both high-tech and non-high-tech sectors.

Figure 10. Europe's Labor Productivity Gap to the United States**1. Euro Area and United States: Aggregate Labor Productivity***(GDP per hour, ratio to US level, constant 2025 purchasing power parity)***2. Labor Productivity of Manufacturing and ICT Sectors***(EU/US ratio, 2000 = 100)*

Source: Ayerst and others, forthcoming.

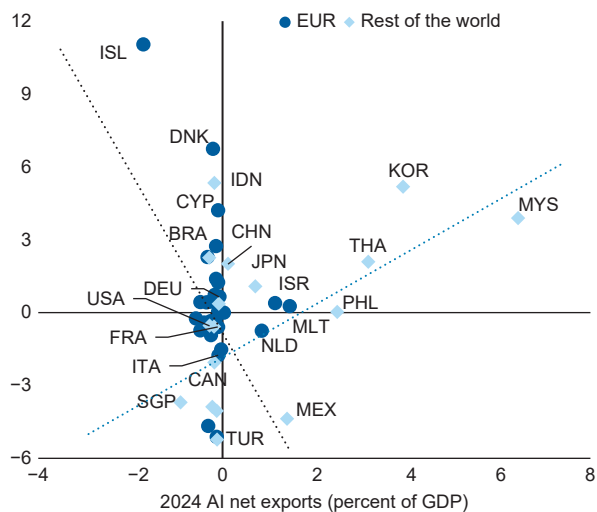
Note: AE = advanced economy; CESEE = Central, Eastern, and Southeastern European; EA = euro area; ICT = information and communications technology.

Figure 11. Intangible-Producing Sectors: Contribution to Labor Productivity Growth*(Percentage points per year)*

Sources: BEA; EU KLEMS; Eurostat; and IMF staff calculations.
 Note: The intangible-producing sector comprises information and communication (J) and professional, scientific, and technical services (M). Production is the total factor productivity growth within these sectors weighted by their value-added share; the bars show economy-wide deepening of intangible capital. EU12 comprises the EU member states prior to the 2004 enlargement, excluding Ireland, Luxembourg, and the United Kingdom, with aggregation at purchasing power parity rates. EU24 is EU12 plus new member states that had sufficient data to be included in the aggregate.

Figure 12. AI Exports and Growth Surprises

2026:Q1 growth surprise (percentage point)



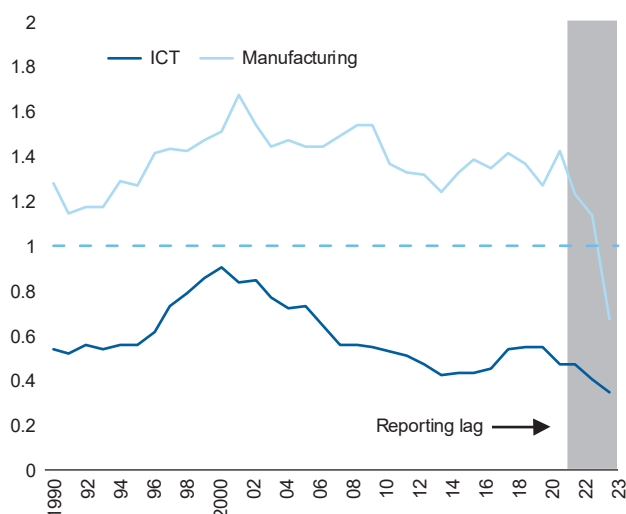
Sources: Haver Analytics; and IMF staff calculations.
 Note: Growth surprises are measured as the difference between outturns and April 2026 *World Economic Outlook* estimates in seasonally adjusted annual rate. AI exposure is constructed from Base pour l'Analyse du Commerce International Harmonized System 22 2024. Trade is aggregated in an 11-code HS6 basket covering data-processing units/parts (847150/170/180/330), CPU and memory integrated circuits (854231/232), and semiconductor-manufacturing equipment (848610/620/630/640/690). The x-axis then shows each country's net exports (exports less imports) of that basket as a percent of 2024 nominal GDP. Data labels in the figure use International Organization for Standardization (ISO) country codes.

A lack of scale is a key driver of these productivity dynamics (IMF 2024a). An incomplete single market—including a fragmented capital market—and a gridlocked domestic reform agenda leave barriers in place that hinder firms from adjusting their size, accessing adequate finance, reaching a larger market, and benefiting from agglomeration externalities. This lack of scale is associated with low investment returns and high uncertainty. As a result, firms are less efficient than they could be and resources fail to move to those that are most productive.

These barriers also structurally weaken firms' incentives for innovation. Innovation and technology adoption are the fundamental drivers of sustained productivity growth. However, despite an abundance of highly skilled labor and research efforts by leading universities and other research institutions in the public sector, innovations by European firms are not as transformative as in the United States and tend to be concentrated in lower-growth, traditional industries, rather than at the high-growth frontier (proxied by manufacturing and ICT sectors, respectively; Figure 13). Over time, European firms have also been slow to adapt to emerging technologies and new sectors. The result is insufficient innovation in the private sector, which is a drag on productivity growth (Ayerst and others, forthcoming).

The lack of innovation and scale is becoming more pressing, as export-driven growth falters in some countries. While exports from advanced economies (AEs) have declined modestly in recent years, CESEE export performance has weakened more markedly (Figure 15, panel 1). The export reduction is broad based in CESEE, with exports to both China and the United States declining, whereas AE exports to the United States have remained resilient (Figure 15, panel 2). Although progress toward the energy transition has continued, structurally high energy costs remain one key factor weighing on the cost-competitiveness of exports (Figure 14), which has affected CESEE countries even more acutely after Russia's invasion of Ukraine. Some CESEE countries also face further pressure because of strong wage growth and real exchange rate appreciation in recent years (Figure 16). Recent trade tensions have also caused significant uncertainty, as can be seen from the sharp frontloading of exports to the United States in the first half of 2025, which has subsequently reversed.

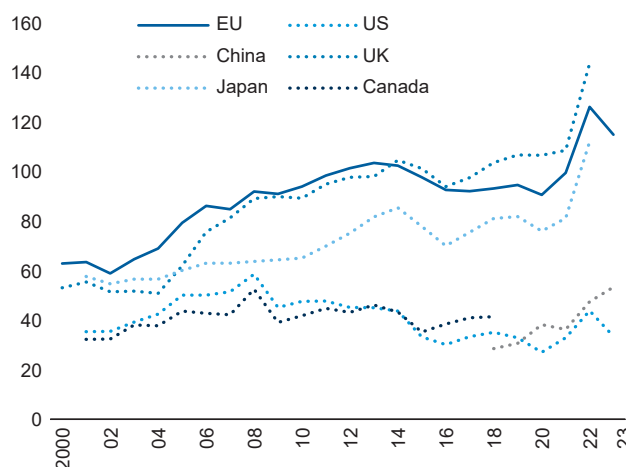
Figure 13. EU Innovation Gaps
(EU Triadic patents, ratio to US level)



Source: Ayerst and others, forthcoming.

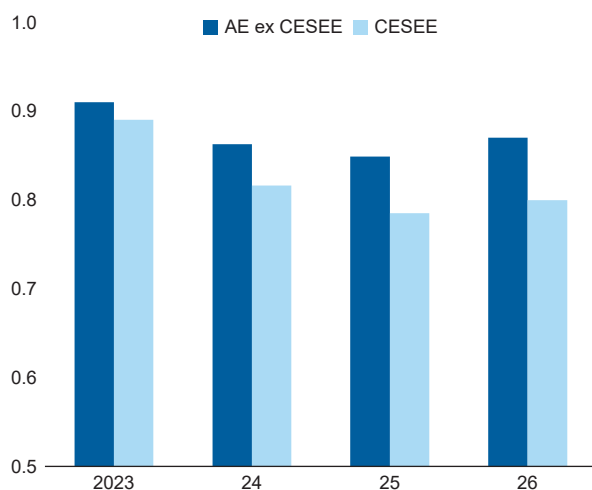
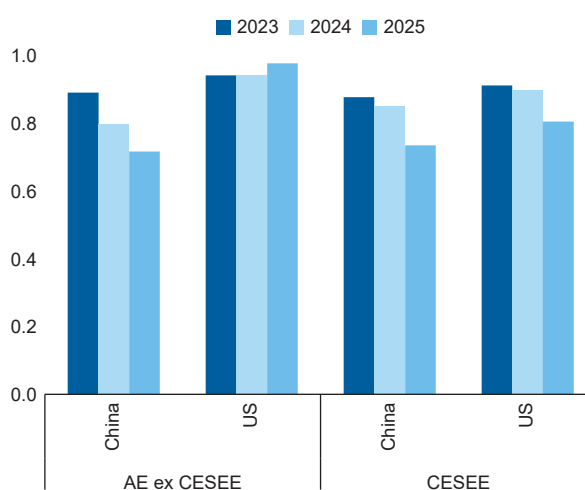
Note: Triadic patents refer to patent families for the same invention filed at and granted by the three most significant patent offices: the European Patent Office, the Japan Patent Office, and the US Patent and Trademark Office. ICT = information and communications technology.

Figure 14. Industrial Electricity Prices
(US\$ per megawatt hour, constant price)



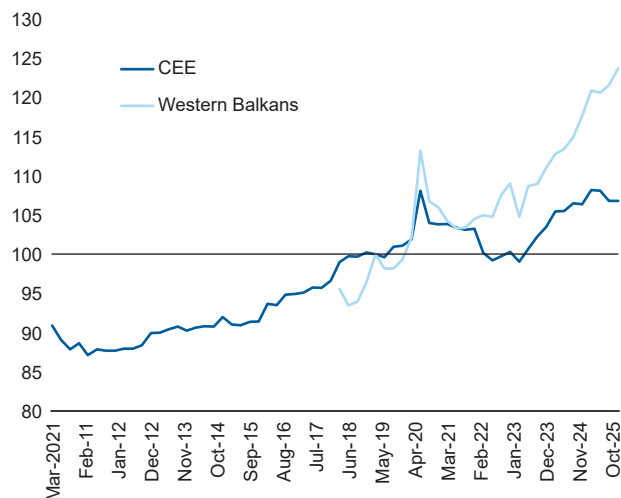
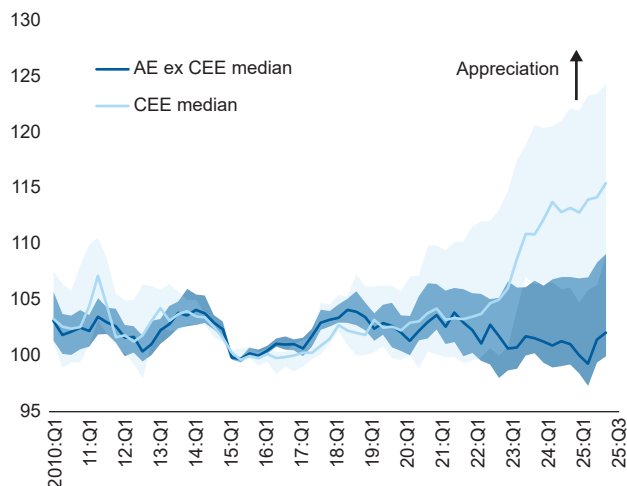
Sources: ENTSO-e; Eurostat; International Energy Agency; National Statistics Institutes; and IMF staff calculations.

Note: AE = advanced economy; CESEE = Central, Eastern, and Southeastern European.

Figure 15. Europe Exports**1. Goods exports***(Exports-to-GDP ratio, indexed to 2022 = 1)***2. Goods Exports by destination***(Exports-to-GDP ratio, indexed to 2022 = 1)*

Sources: IMF, World Economic Outlook; International Merchandise Trade Statistics; and IMF staff calculations.

Note: AE = advanced economy; CESEE = Central, Eastern, and Southeastern European.

Figure 16. External Competitiveness: CESEE**1. Real Wage in CEE and Western Balkans***(Index, March 2019 = 100, seasonally adjusted)***2. Real Effective Exchange Rate***(Index, 2015 = 100, median and inter-quartile range)*

Sources: European Commission; Haver Analytics; and IMF staff calculations.

Note: CEE countries include Bulgaria, Czech Republic, Hungary, Poland, Romania, Slovak Republic, and Slovenia. Western Balkans include Albania, Bosnia and Herzegovina, Kosovo, Montenegro, North Macedonia, and Serbia. In panel 1, Western Balkans are shown separately because data are only available for recent years. AE = advanced economy; CEE = Central and Eastern Europe.

The recent conflict, alongside recurring supply-chain disruptions, also highlights critical import dependencies.

Dependencies along global value chains are often mutual; for example, a country that imports a final product may have supplied the raw materials or intermediate goods that went into it. That said, losing access to critical imports can be very costly. The EU has diversified its sources of fossil fuel imports, reducing especially its dependence on Russia. However, its top trading partners still make up about 70 percent of natural gas imports (Figure 17, panel 1), leaving Europe vulnerable to supply disruptions that can send energy costs surging. At the same time, the European manufacturing sector's dependence on the global supply chain for critical minerals, where just a few suppliers dominate the entire global market, is even more stark (Figure 17, panel 2).

Figure 17. Concentration of Supply Chains

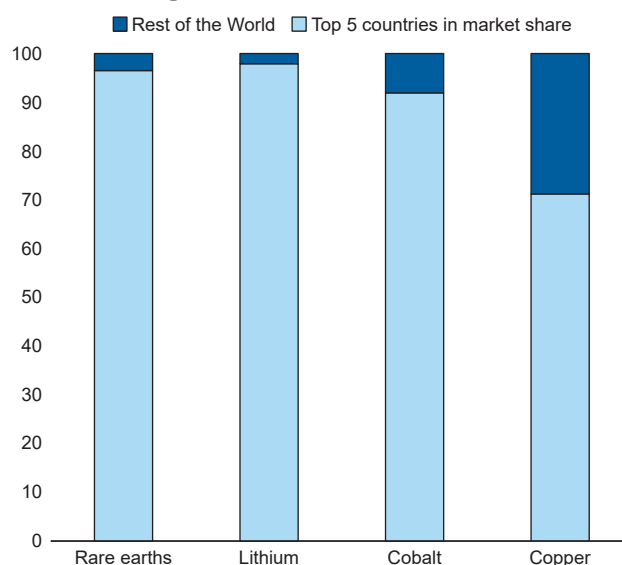
1. EU: Imports of Natural Gas

(Percent share of imports)



2. Refining Activities of Critical Mineral

(Percent in global market share, 2025)



Sources: Eurostat; International Energy Agency; and IMF staff calculations.

Outlook and Risks: Mediocre Growth Continues into the Medium Term

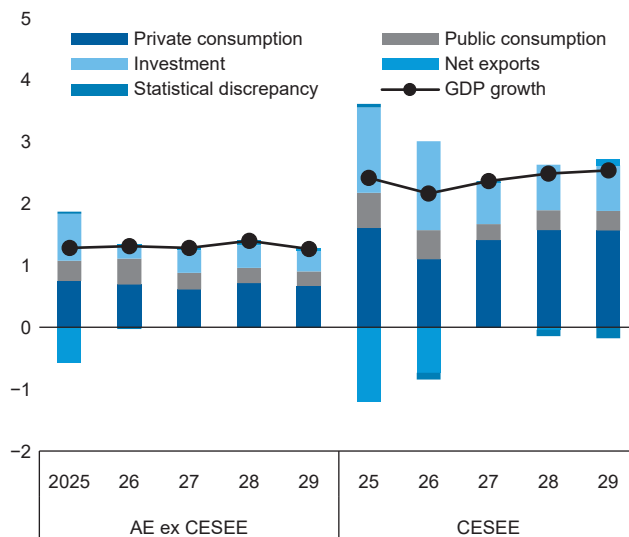
The outlook is for mediocre growth this year that continues into the medium term. The baseline assumes a slow and uneven normalization of energy prices, on account of the still volatile geopolitical situation in the Middle East. Natural gas prices, in particular, are assumed to remain higher in 2027 than assumed in the July *World Economic Outlook*. The growth momentum shown in the first half of this year is expected to wane late in 2026 and into 2027, as high global commodity prices continue to be passed through to consumers and firms. On an annual basis, in AEs (excluding CESEE), the baseline forecast for growth is therefore to remain broadly unchanged at around 1.3 percent from 2025 to 2027 (Figure 18); growth in the euro area, excluding Ireland, is forecast to be 1.2 percent this year and 1.1 percent in 2027. In CESEE countries, growth is expected to slow from 2.4 percent in 2025 to 2.2 percent in 2026, before strengthening the next year. In addition to energy price normalization, these forecasts are based on the assumptions that drought conditions remain temporary, while defense spending across the region, as well as higher infrastructure spending in Germany, will continue to provide some support to growth. It is further assumed that the US effective tariff rate on EU imports will remain about 8.5 percent, broadly unaffected by developments after the February 2026 US Supreme Court ruling.

Inflation is expected to return slowly to target as energy prices normalize. In AEs (excluding CESEE), inflation is expected to peak at 2.9 percent in 2026, before gradually declining. In the euro area, inflation will only return to the target during 2028. In CESEE countries, inflation is projected to be 4.0 percent this year, but decline in 2027. In most CESEE countries, disinflation is also expected by 2028, although in some countries, underlying price pressures or one-off factors (for example, Poland and Romania) are projected to leave inflation still elevated (Figure 19).

The outlook remains highly uncertain, given fragile geopolitical and geoeconomic conditions, and risks are tilted toward lower growth and higher-for-longer inflation.

The most important risk is a further re-escalation of the conflict. This would likely keep energy prices elevated and potentially drive them even higher, putting firms and consumers under more pressure, so that economic activity weakens and inflation becomes more persistent. An increase in medium-term inflation expectations, with some broadening of price pressures, could occur, which would require tighter monetary policy and, in some countries, make fiscal consolidation more important. Even without a re-escalation of the conflict, a stronger recovery in energy demand from Asia and other regions could keep energy prices higher for longer. Pass-through from energy and food prices to other consumer prices could also be stronger than expected, increasing underlying price pressures. A sharp tightening of financial conditions remains a key risk, including as a consequence of the conflict intensifying again, as well as from a correction in overstretched asset valuations. An intensification

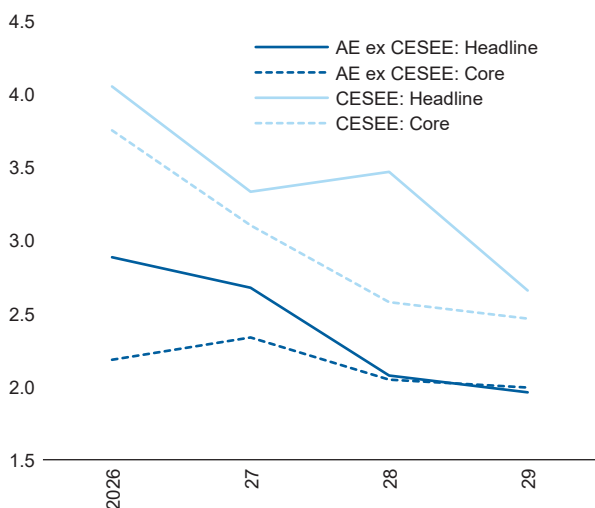
Figure 18. Medium-Term Growth Forecast
(Percentage change, year over year)



Sources: IMF, World Economic Outlook; and IMF staff calculations.
Note: AE = Advanced Economy; CESEE = Central, Eastern, and Southeastern European.

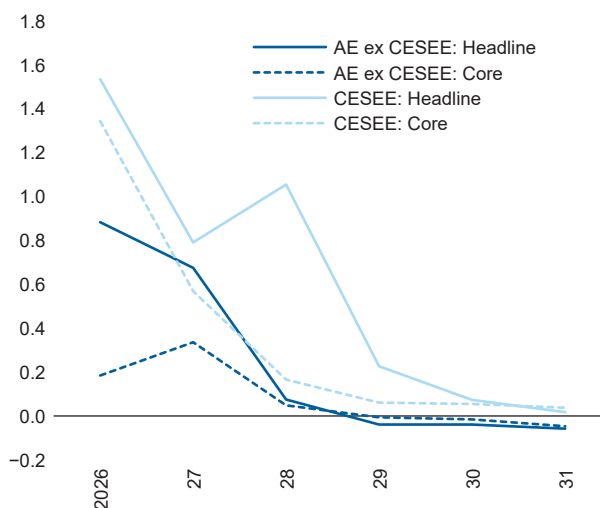
Figure 19. Medium-Term Inflation Forecast

1. Inflation forecast
(Percent)



2. Gap to Inflation Target

(Percentage point, deviation from target)



Source: IMF, World Economic Outlook; National Central Banks.
Note: AE = advanced economy; CESEE = Central, Eastern, and Southeastern European.

of the war in Ukraine, more severe weather events, and a renewed flare-up of global trade tensions are other notable downside risks. On the upside, a faster-than-expected resolution of the war in the Middle East could lift near-term growth and ease inflationary pressures, while strong progress on domestic and single market reforms, or swifter AI development and adoption, could produce higher-than-expected medium-term growth.

Macroeconomic Policies Will Need to Tread Carefully

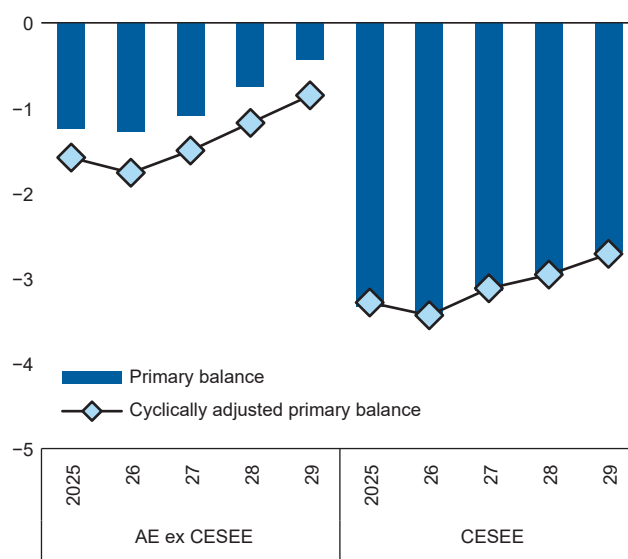
A continuation of growth and moderation of inflation are not guaranteed, and policymakers will have to tread carefully. Monetary policy will need to remain contingent on how energy prices, expectations, and inflation evolve. Fiscal policy should ensure that it does not add to price pressures through unnecessary stimulus, while still supporting the vulnerable. Financial sector policymakers should monitor risks closely, given the potential for adverse shocks to be magnified through the financial system and affect financial stability.

Monetary policy must stand ready to tackle a broadening of price pressures. Although current monetary policy settings are adequate in most countries, more policy action by central banks may be needed, if signs of broader price pressures emerge. To keep inflation expectations well anchored, central banks should continue to communicate their reaction functions and establish clearly how policy would respond to changes in economic conditions.

- In the *euro area*, the European Central Bank has appropriately tightened policy by 25 bps in both June and September, as inflationary pressures have mounted. IMF analysis shows that at least one further 25 bps increase in policy rates in 2026 will be required to ensure that core inflation remains well contained. While policy beyond 2026 should evolve based on how incoming data affects the inflation outlook, further tightening is likely to be warranted to ensure that inflation returns to target in 2028.
- In the *United Kingdom*, inflation remains elevated and the Bank of England should maintain a restrictive stance through 2027 so as to put inflation on an assuredly downward path back toward the target.
- In some *CESEE* countries, where inflation was above target when the conflict began or underlying inflationary pressures are persistent (for example, Czech Republic and Romania), policymakers are more likely to need to tighten policy and keep it restrictive for longer. In other CESEE countries, where inflationary pressures have been more contained, central banks may be more able to keep policy on hold with a tightening bias, and monitor further developments, standing ready to act if needed (for example, Hungary and Poland). Any monetary easing should be resumed cautiously, based on firm evidence that pressures on core inflation are receding, to manage the risk of having to reverse course at a later stage.

Fiscal support to mitigate the effects of higher energy prices, if not carefully calibrated, could undermine disinflation efforts. On average across both AEs and CESEE countries, fiscal balances are expected to deteriorate only slightly this year, without a large expansionary impulse, which is appropriate to avoid adding to price pressures (Figure 20). In countries where economic activity is weaker, automatic stabilizers can be allowed to operate for cushioning the impact of higher energy prices, although offsetting measures may be required in countries without fiscal space. All countries have already introduced

Figure 20. Fiscal Balance
(Percent of GDP)



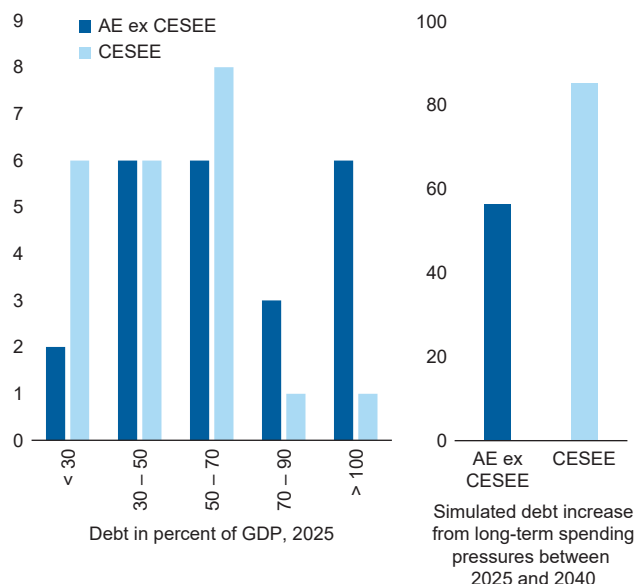
Sources: IMF, World Economic Outlook; and IMF staff calculations.
Note: AE = advanced economy; CESEE = Central, Eastern, and Southeastern European.

measures to provide energy price relief to households and firms, most of which distort energy prices. If support is extended, or a new relief is introduced, given the ongoing energy price volatility, these measures should be tightly targeted at supporting the most vulnerable (through, for example, targeted cash transfers), while leaving the price signal intact, so as to preserve incentives to save energy and improve efficiency.

Fiscal policymakers will have to step up and face the mounting sustainability challenges from higher necessary spending. European governments are being called upon to meet critical spending needs, including for higher defense spending, the energy transition, and pensions and health care associated with population aging. Although these are vital tasks for public policy, the costs are piling up quickly, but fiscal space is limited. It is estimated that these pressures would increase public spending by 4½ percent of GDP by 2040 on average in AE (excluding CESEE) countries and 5½ percent of GDP in CESEE countries. At the same time, public debt is higher than that in the early 2010s. Rising yields in some countries are contributing to a higher interest bill, while lackluster growth stresses debt ratios further. Without fiscal consolidation, these forces would put the public debt of European countries on an unsustainable path, on average (Figure 21).

Policy action is needed to either lift growth or reduce deficits to ensure that debt is on a sustainable path—doing nothing is not an option. Around three-quarters of European countries will need a combination of structural reforms, to increase growth (for example, single market reform) and ease spending pressures (for example, pension reform), together with deficit-reducing consolidation measures of about 3½ percent of GDP on average, over the medium term, to keep debt sustainable. In EU countries, the amount of consolidation planned in MTFSPs (medium-term fiscal-structural plans), which were finalized before the new NATO defense spending target was adopted, averages about 2 percent of GDP, falling short of what will be required in some countries and underscoring the need to recalibrate these plans. Even the consolidation envisaged in the current MTFSPs may prove challenging, given that baseline projections of IMF staff show that fiscal consolidation will undershoot MTFSPs for most countries (Figure 22); however, the gap appears to be small for many AEs. About one-quarter of European

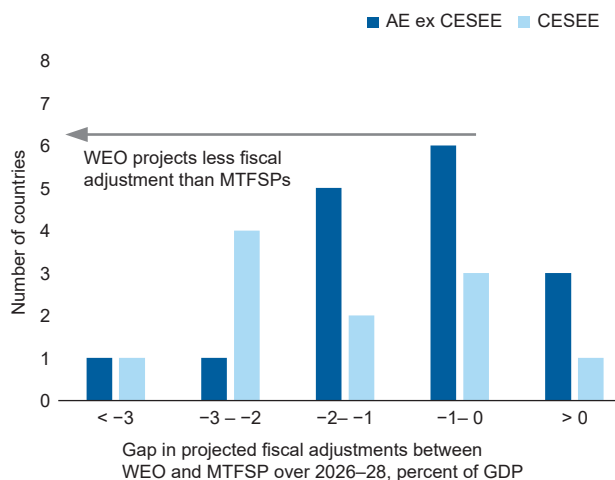
Figure 21. Long-Term Fiscal Sustainability
(Number of countries, left scale; percent of GDP, right scale)



Sources: Eble and others 2025; Eyraud and others 2026; IMF, World Economic Outlook; and IMF staff calculations.

Note: The RHS of the figure shows the simulated increase in public debt between 2025 and 2040 for AEs and CESEE countries (simple average), assuming that primary balances remain unchanged from their 2025 levels apart from the spending pressures described in Eyraud and others 2026. AE = advanced economy; CESEE = Central, Eastern, and Southeastern European; LHS = left-hand side; RHS = right-hand side.

Figure 22. Gap between Expected Fiscal Adjustment and MTFSP Plans



Sources: European Commission; IMF, World Economic Outlook; and IMF staff calculations.

Note: A negative gap indicates that projected consolidation in the WEO is less than assumed in the MTFSP. AE = advanced economy; CESEE = Central, Eastern, and Southeastern European; MTFSP = medium-term fiscal-structural plan; WEO = World Economic Outlook.

countries would need to consolidate by more than 5 percent of GDP, to keep public debt sustainable, more than what has generally proved feasible in the past, leaving no option but to rethink the scope of government activity, and increase the role of the private sector, to fill the gap.

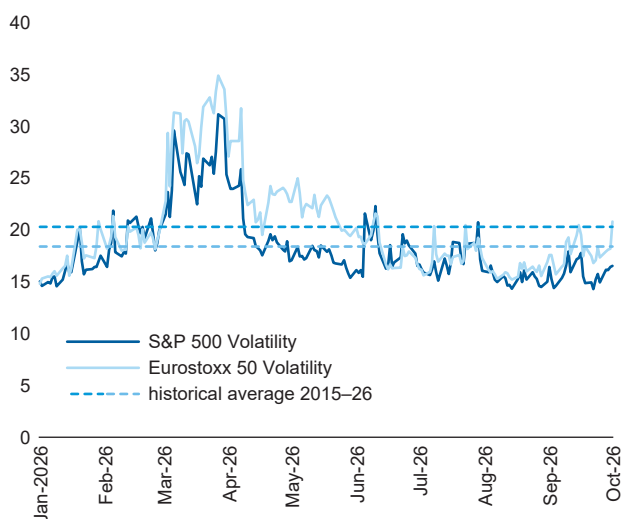
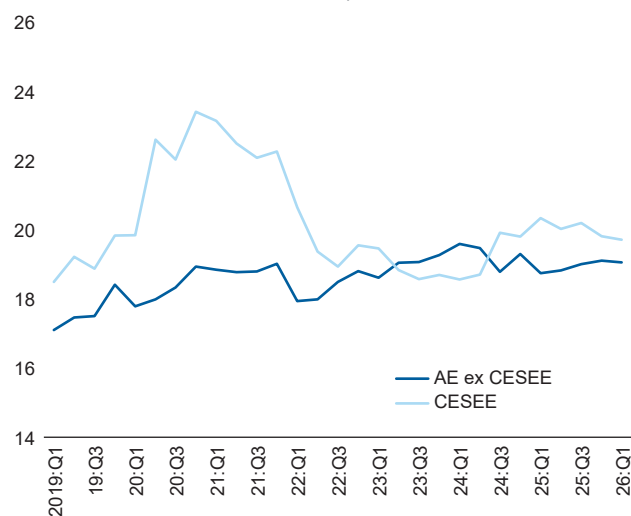
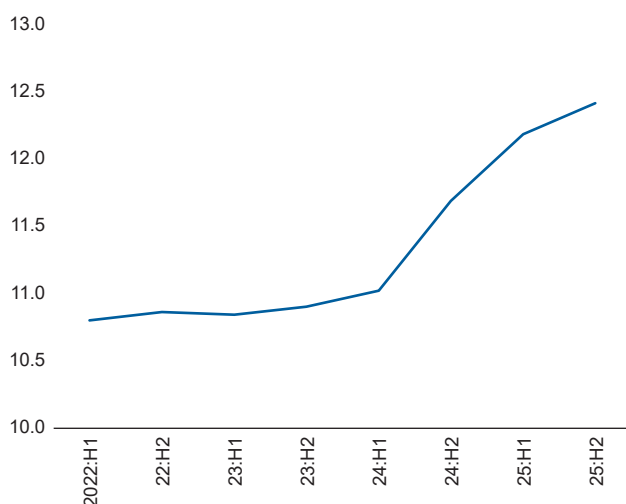
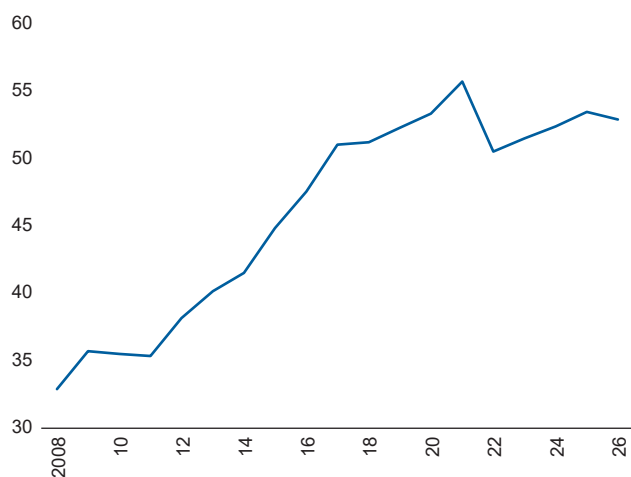
Given elevated uncertainty, it is important to build on Europe's hard-won financial sector resilience. The European banking system remains adequately capitalized and liquid, with rising profits and non-performing loans contained in most countries. Global bank stress tests continue to indicate resilience of the banking sector to severe shocks overall, while also pointing to vulnerabilities in a tail of weaker institutions (IMF 2026a; Figure 1.7). This underscores the importance of maintaining strong capital and liquidity buffers and continuing efforts to strengthen the broader financial safety net. There was a period of market volatility after the conflict began, and growing interconnectedness across financial institutions could amplify any further adverse shocks and pose risks to financial stability (Figure 23, panels 1–2). Policymakers should continue to strengthen the resilience of the financial system beyond banks, focusing on market pricing and NBFIs (nonbank financial institution) concerns:

- *Risks of sudden market repricing.* A sharp deterioration in investor sentiment, triggered by a major re-escalation of the conflict, sovereign market stress, or a reassessment of asset valuations, could abruptly tighten financial conditions. Asset valuations are stretched in several sectors, particularly those exposed to AI, while house prices are also elevated in some European countries. Sovereign debt markets have also become more susceptible to repricing, given a more price-sensitive investor base for sovereign bonds, including hedge funds. After a period of stability, the exposure of significant financial institutions to sovereign borrowers has started rising again (Figure 24, panel 3). In this context, a sudden sell-off in financial markets could put sovereign bond yields under pressure, and create valuation losses, with cross-border spillovers through financial exposures. It could also reduce credit availability to households and firms, and weigh on economic activity, including if house price declines adversely affect banks' asset quality. Policymakers should remain prepared to deploy existing safeguards, including releasing macroprudential buffers if severe stress risks amplifying a credit crunch.
- *Bank-NBFI linkages.* Stress arising from leveraged and less-transparent parts of the NBFI sector could also amplify market volatility and transmit shocks across the financial system (Valderrama and Varghese 2026). Rapid balance sheet growth of NBFIs (Figure 23, panel 4), leverage, and liquidity mismatches in some investment strategies could intensify redemption pressures, margin calls, and asset sales during periods of stress. Risks are compounded by the growing role of some NBFIs, including offshore hedge funds, in sovereign bond markets, where abrupt position unwinds could exacerbate market volatility and funding pressures. Policymakers should continue to close data gaps, particularly regarding cross-border and bank-NBFI exposures; strengthen system-wide stress testing; and enhance supervisory monitoring. In the euro area, liquidity backstops could be extended to selected NBFIs during periods of systemic stress, subject to robust safeguards and oversight.

Resilience could also be enhanced by strengthening the crisis management framework, including by ratifying the reformed European Stability Mechanism treaty in order to have a fully operational backstop for the Single Resolution Fund and introducing European deposit insurance.

Reforms for Innovation, Scale, and Resilience

Giving in to rising calls for more interventionist industrial policy and protectionism will not address Europe's challenges. These policies, though potentially useful in narrowly defined circumstances, cannot durably address Europe's underlying growth problem and may even impose significant long-term costs. Past experience shows that protectionist and broad-based industrial policies aiming, for example, at import substitution or the preservation of existing industries, at best, buy time. More often, they tend to delay necessary structural transformation, generate little productivity gain, sometimes entail substantial fiscal costs, and entrench vested interests that make them difficult to unwind (IMF 2025b). Where well-identified market failures exist, industrial policies can play a role. However, they may create sizable cross-country spillovers and, thus, should be coordinated at the European level

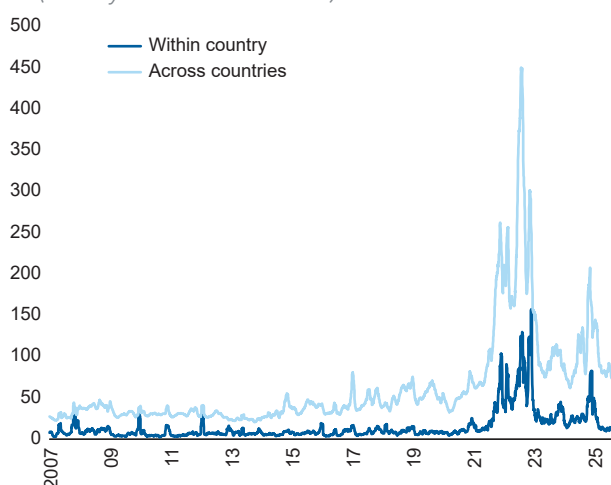
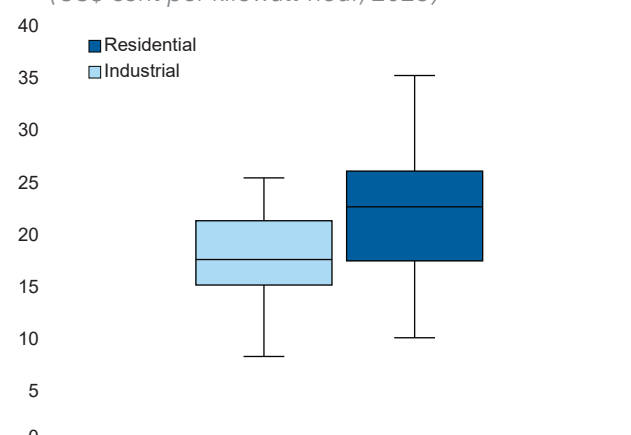
Figure 23. Financial Sector Conditions**1. Market Volatility***(Index)***2. Bank Capital Buffer***(Percent, median of Tier 1 capital ratio)***3. Exposure of Banks to General Government***(Percent of total assets of significant institutions)***4. Financial System Assets Held by NBFIs***(Percent of total financial system assets)*

Sources: Bloomberg L.P.; European Banking Authority; European Central Bank; and IMF staff calculations.

Note: Panel 3 includes all significant institutions in Single Supervisory Mechanism countries. AE = advanced economy; CESEE = Central, Eastern, and Southeastern European; NBFIs = nonbank financial institutions.

and remain consistent with international trade obligations (Hodge and others 2024). At the same time, Europe will benefit from continuing to lead the way to more open, stable, and transparent trade arrangements, particularly larger regional agreements. This approach can reduce policy uncertainty and increase trade diversification of both products and trading partners (Caselli, Mulabdic, and Ruta 2026). Efforts to reduce the dependence on critical inputs and more broadly to diversify trade linkages may be warranted, but they involve an inherent risk-efficiency trade-off (Caselli and others 2020), which policymakers must weigh carefully alongside their fiscal costs.

The key task is to make Europe more dynamic, innovative, and resilient from within. The policy priorities for the region include continuing the energy transition, continuing to deepen the single market, and advancing complementary national reforms. Europe's electricity markets remain far too fragmented, as reflected in high and volatile electricity prices, wide price dispersion across countries (Figure 24), and persistent cross-border

Figure 24. Volatility and Dispersion of European Electricity Prices**1. Volatility of Wholesale European Electricity Prices***(30-day standard deviation)***2. Cross-Country Industrial and Residential Electricity Prices***(US\$ cent per kilowatt-hour, 2025)*

Sources: Bloomberg L.P.; Eurostat; and IMF staff calculations.

congestion. Significant barriers also persist in goods and services markets (Cerdeiro and Rotunno 2026), labor mobility remains limited (Head and Mayer 2021), and capital markets remain fragmented. Although many European countries stand as leading examples in key macrostructural areas, there are significant structural policy gaps relative to the frontier and, therefore, much remaining scope for growth-enhancing reforms (Budina and others 2025). At the same time, growth drivers in CESEE economies are slowing, while EU candidate countries need ambitious reforms to seize the transformative opportunity offered by EU accession.

Together, these measures would enhance energy security, stimulate innovation, and support productivity growth. Greater reliance on renewables can further reduce exposure to volatile gas and coal prices, a point made even clearer by the recent conflict. Single market and national reforms—in both real and financial sectors—will boost productivity by improving capital and labor allocation, enabling firms to scale, strengthening agglomeration externalities, incentivizing risk taking and investment (IMF 2024a, 2025a), while also preparing the ground for transformative innovation. Reforms across Europe are mutually reinforcing. Just as earlier EU enlargements generated benefits for both old and new member states (IMF 2024b), a coordinated push to remove binding constraints, enhance innovation, and deepen integration would yield larger gains than isolated efforts.

Continuing the Energy Transition Will Build Resilience

Achieving an integrated energy grid has the potential to benefit all European countries. Integration benefits can come through three channels: gains from trade, lowering local electricity market mismatch in demand and supply, and strengthening incentives for investment (Gonzales, Ito, and Reguant 2023).⁵ IMF staff analysis (D’Arcangelo and others, forthcoming) finds that deeper interconnection lowers wholesale electricity prices, especially in high-price markets and where transmission constraints are most binding, whereas low-price markets do not necessarily observe systematic price increases; both types of markets also benefit from fewer price spikes. The average lifetime cost of clean energy generation is now below that of fossil fuel generation

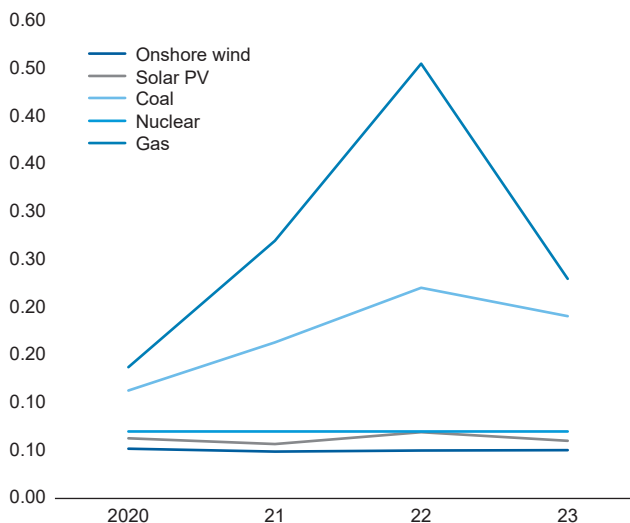
⁵ Gains from trade stem from lower barriers to electricity trade, allowing countries to specialize according to their comparative advantage. Electricity market imbalances can be lowered as countries can share low-cost supply across borders when local supply and demand conditions diverge, which helps to reduce costly scarcity episodes, price volatility, and disruption risks. Dynamic gains emerge because a larger integrated market raises expected returns to high-fixed-cost, low-marginal-cost generation projects, particularly renewables.

in France, Germany, and Italy (Figure 25), making clean energy an increasingly cost-effective source of power, rather than simply a tool for decarbonization. Therefore, electrification will continue to advance, and renewable generation will further expand. Integration gains are likely to grow with the process, also as emerging sources of concentrated demand—such as data centers—place greater pressure on the system. IMF analysis (D’Arcangelo and others, forthcoming) also shows that stronger cross-border interconnectivity and expanded low-carbon generation capacity can fully offset the upward pressure on electricity prices stemming from rising demand and carbon pricing.

Integrating Europe’s energy market and completing the energy transition need a predictable and strategic approach.

Planned initiatives such as the European Commission’s 2025 Grid Package—which aims to accelerate renewables integration, clear connection queues, and improve cross-border energy independence—should be implemented without delay. Europe would also benefit from a common energy-system roadmap covering generation, storage, transmission, and demand management. Such a framework should ensure that infrastructure investment is located where sources of renewable energy are abundant, as well as where demand is growing rapidly, while also investing in regions most exposed to weather-related risks. EU-level financing, clear mechanisms to share costs and gains across countries, and coordinated policy instruments are essential for coordination and avoidance of wasteful duplication.⁶ At the same time, a credible and predictable emissions reduction framework incentivizes private investments in clean technologies. In particular, continued implementation of the EU ETS1 and the rollout of ETS2 will help preserve clear carbon-price signals and support long-term investment decisions. IMF analysis shows that if ETS1 and ETS2 carbon prices rise in line with emissions targets and part of the revenues are recycled into well-targeted green investment support, then the macroeconomic effects would remain moderate, whereas projected ETS revenues over the next decade would exceed the public investment needed for decarbonization (Carton and others 2026). At the same time, tax distortions that raise electricity prices unnecessarily should be removed. Electricity excise taxes should not exceed those on fossil fuels, and a standard value-added tax rate should be maintained.

Figure 25. Levelized Cost of Energy by Source
(US\$ per kilowatt-hour, average of France, Italy, and Germany)



Sources: IRENA; Nuclear Energy Agency; Renewable Power Generation Costs in 2023; and IMF staff calculations.

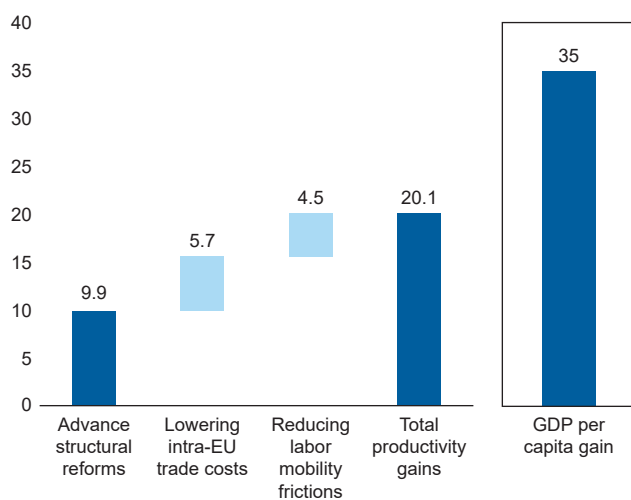
Note: Levelized cost of energy measures the average cost of producing 1 kWh of electricity over a plant’s lifetime, including construction, operation and maintenance, fuel, financing, and decommissioning costs. PV = photovoltaic. Data are available only until 2023.

Europe Needs to Fix the Fundamentals to Create the Conditions for Innovation and Scale to Sustain Higher Growth

Deepening the EU’s single market and closing domestic structural policy gaps remain the most important policy initiatives to lift productivity. Productivity differences continue to be the critical driver of the EU-US per capita income gap. Although there is no doubt that the necessary structural reforms are difficult to implement politically, their potential rewards are large, and the gains from a comprehensive reform agenda would be broadly shared

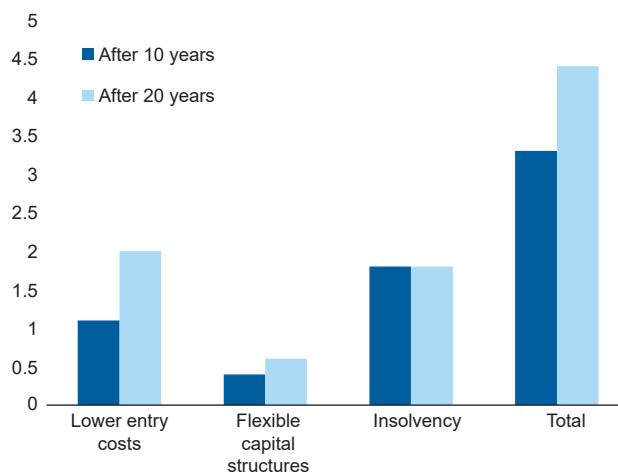
⁶ EU-level financing, such as the Connecting Europe facility, helps overcome coordination problems that contribute to structural underinvestment in interconnectors. Mechanisms to share costs and gains across countries align investment incentives by linking cost allocation more closely to the distribution of benefits, as under the Cross-Border Cost Allocation framework. Coordinated policy instruments help preserve system-wide efficiency and avoid wasteful duplication, such as those arising when national capacity mechanisms encourage investment in domestic backup capacity that could otherwise be provided through cross-border balancing.

Figure 26. EU Gains from EU and National Reforms
(Labor productivity and GDP gains in percent)



Sources: AMECO; IMF 2025a; Kammer, Ayerst, and Tang 2026; IMF, World Economic Outlook; and IMF staff calculations.

Figure 27. Potential GDP Gains from the 28th Regime Pillars
(Percent of GDP)



Source: Fotiou, Dizioli, and Garrido 2026.

across countries. IMF staff analysis shows that eliminating all remaining domestic policy distortions and removing the still existing cross-border obstacles to EU trade and labor mobility have the potential to raise EU productivity by about 20 percent (IMF 2025a). Higher productivity could, in turn, crowd in up to €800 billion in additional investment over a decade and increase GDP per capita by about 35 percent over time (Figure 26; Kammer, Ayerst, and Tang 2026). Financial reforms, such as those that integrate and deepen banking and venture capital markets, can raise output further, while also further strengthening the impact of real-sector reforms.⁷ The reform gains may be even larger still, as these measures bear double dividends by also fostering innovation, which can drive productivity growth directly.

The current reform momentum to complete the single market is promising. The Single Market Roadmap commits the European Parliament, Council, and Commission to a detailed legislative timetable through the end of 2027, but the ambition of the reform package could be strengthened further. It should be complemented by a financial system capable of unlocking savings so that they can be accessed by investors, allocating capital to flow efficiently within and across borders. In this regard, completing the savings and investment union (SIU)—by advancing the banking union, harmonizing corporate insolvency law, expanding the supply of long-term risk capital through pension and insurance reforms, and reducing barriers to cross-border equity investment—could ease cross-border banking frictions and increase the availability of venture capital (Brandao-Marques and others 2026). Establishing a voluntary 28th enterprise regime would further reduce legal fragmentation and facilitate firm scale-up across the single market by addressing a cross section of domestic and EU-level reform needs. The scope of the insolvency framework is particularly important, as a comprehensive, rescue-oriented insolvency regime can have significant macroeconomic benefits, by improving predictability for investors and creditors alike, while facilitating value-preserving restructuring (Figure 27; Fotiou, Dizioli, and Garrido 2026).

⁷ Brandao-Marques and others (2026) consider a financial reform scenario where regulatory distances affecting cross-border banking are reduced by 30 percent, and domestic policy gaps constraining the availability of risk capital are halved. Under this scenario, European output will increase by about 4 percent. A real sector counterpart of such a scenario would be one that closes the policy gap by half, which is associated with a 15 percent output increase, instead of the 35 percent that would eventuate when all gaps are closed as in Kammer, Ayerst, and Tang (2026). Therefore, the total output gain would be 19 percent if real and financial sector reforms are implemented jointly.

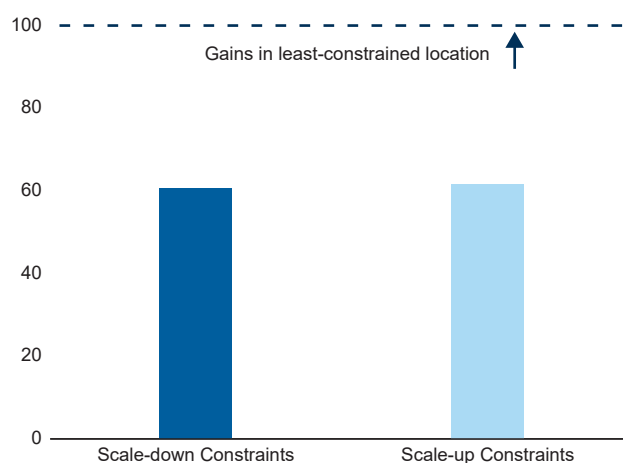
Domestic structural reform gaps—and potential gains as quantified earlier—remain substantial, and addressing them will reinforce the single market reform efforts. IMF staff identify stronger labor market performance and human capital formation as top national reform priorities, alongside product and capital market measures to foster innovation and firm dynamism (Budina and others 2025). IMF staff analysis finds that low housing affordability constrains labor mobility, with inadequate housing supply emerging as a prominent driver of dwelling price increases in recent years. Therefore, policy efforts should focus on expanding housing supply, for example, by releasing land for residential construction, streamlining permitting processes, and improving access to financing for developers. To maximize the likelihood of success, reforms should be designed with political feasibility and implementation capacity in mind; early public engagement, effective communication, learning from the best performers, and smart sequencing and bundling can all help strengthen outcomes.

A broad package of single market and domestic reforms can also remove key obstacles to innovation and help Europe push the technological frontier. Among the most prominent impediments are barriers that hinder firms from scaling up and scaling down—such as overly restrictive labor market regulations that protect jobs rather than workers or tax rules that discourage investment and growth, compounded by a still-incomplete single market (for example, fragmented insolvency regimes across countries or limited availability of skilled labor locally).

Removing these obstacles would increase returns to firms from successful innovations and reduce risks if some innovation efforts fail. IMF staff analysis finds that after filing their first transformative patent, sales of firms in places with more stringent constraints on scaling up and scaling down will grow only about 60 percent as fast as those in the least-constrained locations (Figure 28; Ayerst and others, forthcoming). This implies that policy action that makes it easier for firms to scale up and scale down can significantly incentivize innovation in high-growth sectors and help Europe push the productivity frontier. By contrast, other policy interventions, such as direct R&D support to specific firms or sectors, or a broad relaxation of merger rules, should be used cautiously. Like other forms of industrial policy, they risk creating distortions that may ultimately weaken long-term productivity growth.

Figure 28. Innovation Gains under Scale-Up and Scale-Down Constraints

(Percent of sales increase following transformative innovations in least-constrained locations)



Source: Ayerst and others, forthcoming.

Note: Scale-up constraints are proxied by a measure that captures how employment scales with productivity. Scale-down constraints are proxied by employment protection legislation.

CESEE Countries Need to Adapt Policies to Ensure Sustainable Growth

CESEE countries need to pursue reforms that can sustain convergence to higher income levels. Although CESEE countries, like all of Europe, will benefit from removing barriers to innovation, reducing national-level inefficiencies, and deepening the single market, the reforms needed in CESEE countries go beyond this agenda. The region has benefited enormously from EU integration, supported by strong productivity growth and capital accumulation (IMF 2024b). However, part of this performance was underpinned by expansionary policies in recent years and—although there is still little sign of a broad-based slowdown—pockets of weakness are emerging. Manufacturing exports have come under pressure, because of wages outstripping productivity, real effective exchange rate appreciation, lower foreign direct investment, and intensified external competition. Current account deficits have widened as a result, to which persistent fiscal deficits may have also contributed (Figure 29). These trends are apparent in both Central

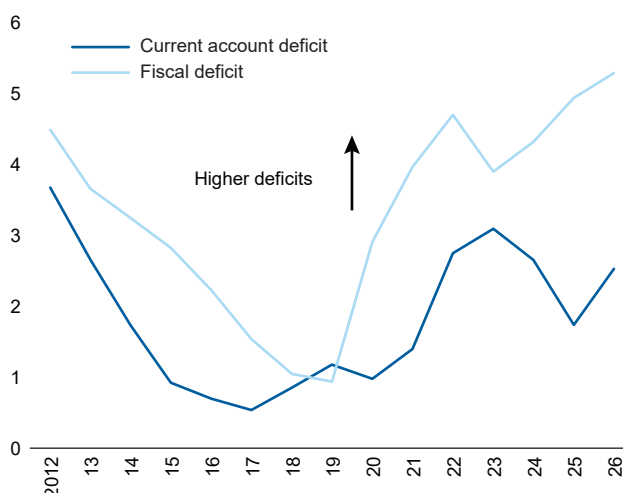
and Eastern Europe (CEE), as well as in Baltic countries and the Western Balkans, casting doubt on the sustainability of the current growth path. In order to reignite the convergence engine, growth in CESEE should rely less on external factors and cost-competitiveness, and shift toward innovation and productivity growth. Preserving competitiveness in existing industries requires a credible institutional environment, a more skilled workforce, stronger domestic private investment, continuing to leverage the opportunities offered by the single market, and strategic use of EU funds (Galante and others, forthcoming). Loose fiscal policies, which have persisted for too long in some countries, need to be recalibrated toward ensuring fiscal sustainability, given rising spending pressures. In the Baltics, labor shortages are particularly pressing structural challenges and need to be addressed—for instance, by increasing labor force participation and reducing skill mismatch. The combination of these policies will also facilitate diversification across products and markets, a move toward higher value-added activities and stronger innovation capacity.

EU accession is a transformative opportunity for the Western Balkans and Moldova, but realizing its full potential will require ambitious domestic reforms (Figure 30).

The experience from previous enlargement rounds and structural model simulations shows that income levels could be about 30 percent higher within a decade of accession (Ayerst and others 2026a). Productivity improvements are at the heart of this payoff, accounting for about two-thirds of overall income gains. Sustained productivity growth requires effective implementation of the EU *acquis* and broad domestic reforms, notably stronger governance and institutions, labor market reforms, enhanced competition, and innovation policies. Effective use of EU funding and deeper integration into the EU single market are equally critical for the overall accession payoff. Together, these mutually reinforcing reforms can translate successful accession into lasting productivity gains, higher investment, and better labor market outcomes, with even greater benefits if the EU continues to deepen single market integration.

A larger, better integrated and more productive EU can be of benefit to all EU member states. In the meantime, policymakers should manage transition risks carefully by strengthening fiscal institutions, ensuring the quality of public investment, and enhancing financial sector oversight to safeguard financial stability.

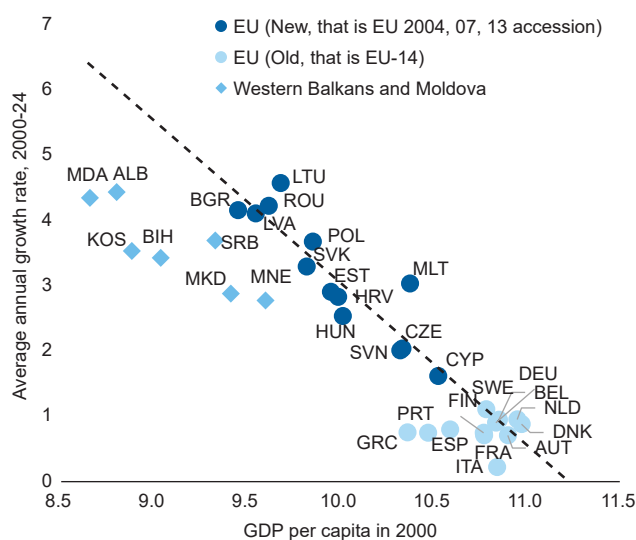
Figure 29. The Twin Deficits: CESEE
(Percent of GDP, three-year trailing moving average)



Sources: IMF, World Economic Outlook.

Note: CESEE = Central, Eastern, and Southeastern European.

Figure 30. Unrealized Convergence Gains: Moldova and Western Balkans



Sources: IMF, World Economic Outlook; and IMF staff calculations.

Note: "New" designates countries that were successively admitted during the 2004, 2007, and 2013 enlargement rounds of the European Union, whereas "Old" designates pre-2004 members.

Data labels in the figure use International Organization for Standardization (ISO) country codes.

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Annex Table 1.1. Real GDP Growth*(Year-over-year percent change; aggregation based on GDP in purchasing power parity terms)*

	October 2026 WEO				April 2026 WEO			Difference		
	2025	2026	2027	2028	2026	2027	2028	2026	2027	2028
Europe	1.6	1.5	1.6	1.7	1.5	1.6	1.8	0.0	0.0	-0.1
Advanced European Economies	1.4	1.4	1.3	1.5	1.2	1.3	1.5	0.2	0.0	0.0
Euro Area	1.2	1.1	1.2	1.3	1.1	1.2	1.4	0.0	0.0	-0.1
Austria	0.8	0.6	0.9	1.2	0.7	1.0	1.3	-0.1	-0.1	-0.1
Belgium	1.0	0.7	1.1	1.2	0.7	1.1	1.1	0.0	0.0	0.1
Bulgaria	3.1	2.6	2.7	2.6	2.8	2.5	2.8	-0.2	0.2	-0.2
Croatia	3.4	2.2	2.3	2.4	2.6	2.6	2.6	-0.4	-0.3	-0.2
Cyprus	3.8	2.9	3.2	3.1	3.0	3.0	3.0	-0.1	0.2	0.1
Estonia	1.3	2.1	2.2	1.9	1.4	1.9	2.3	0.7	0.3	-0.4
Finland	0.8	1.7	1.4	1.2	1.0	1.5	1.4	0.7	-0.1	-0.2
France	0.9	0.4	0.7	1.2	0.9	0.9	1.2	-0.5	-0.2	0.0
Germany	0.2	1.3	1.1	1.1	0.8	1.2	1.2	0.5	-0.1	-0.1
Greece	2.1	1.8	1.8	1.7	1.8	1.7	1.6	0.0	0.1	0.1
Ireland	8.0	-1.0	3.7	2.9	2.5	2.4	2.6	-3.5	1.3	0.3
Italy	0.5	0.8	0.6	0.7	0.5	0.5	0.8	0.3	0.1	-0.1
Latvia	2.1	2.3	1.8	2.1	2.2	2.4	2.4	0.1	-0.6	-0.3
Lithuania	2.9	2.7	2.1	2.6	2.9	2.2	2.6	-0.2	-0.1	0.0
Luxembourg	0.6	1.1	1.6	2.1	1.6	1.7	2.1	-0.5	-0.1	0.0
Malta	4.7	4.2	4.0	4.0	3.7	3.8	4.0	0.5	0.2	0.0
Netherlands	1.6	1.5	1.3	1.4	1.2	1.4	1.4	0.3	-0.1	0.0
Portugal	1.9	2.1	1.9	1.8	1.9	1.8	1.8	0.2	0.1	0.0
Slovak Republic	0.8	0.8	1.6	2.6	0.6	1.6	2.6	0.2	0.0	0.0
Slovenia	1.5	3.2	2.2	2.1	2.0	2.1	2.2	1.2	0.1	-0.1
Spain	2.6	2.5	1.8	1.8	2.1	1.8	1.8	0.4	0.0	0.0
Nordic Economies	1.8	2.5	1.9	1.7	1.8	1.6	1.7	0.7	0.3	0.0
Denmark	3.5	3.7	2.0	1.8	2.0	1.6	1.6	1.7	0.4	0.2
Iceland	1.1	1.4	1.8	2.1	1.9	2.1	2.4	-0.5	-0.3	-0.3
Norway	1.1	1.5	1.3	1.1	1.5	1.3	1.1	0.0	0.0	0.0
Sweden	1.4	2.5	2.2	2.1	2.0	1.9	2.1	0.5	0.3	0.0
Other European Advanced Economies	1.6	1.7	1.6	1.9	1.3	1.7	1.9	0.4	-0.1	0.0
Andorra	3.9	1.9	1.7	1.7	2.1	1.8	1.7	-0.2	-0.1	0.0
Czech Republic	2.6	1.8	1.9	2.2	2.2	2.2	2.1	-0.4	-0.3	0.1
Israel	3.5	4.5	4.4	3.6	3.5	4.4	3.7	1.0	0.0	-0.1
San Marino	1.5	1.3	1.0	1.2	1.3	1.2	1.3	0.0	-0.2	-0.1
Switzerland	1.6	1.9	1.2	1.9	1.3	1.3	1.8	0.6	-0.1	0.1
United Kingdom	1.2	1.3	1.2	1.6	0.8	1.3	1.6	0.5	-0.1	0.0

	October 2026 WEO				April 2026 WEO			Difference		
	2025	2026	2027	2028	2026	2027	2028	2026	2027	2028
Emerging European Economies	2.0	1.7	2.1	2.3	2.0	2.1	2.3	-0.3	0.0	0.0
Central and Southeastern European EU Member States	2.4	2.2	2.4	2.4	2.4	2.4	2.6	-0.2	0.0	-0.2
Hungary	0.5	1.9	2.1	2.3	1.7	2.0	2.3	0.2	0.1	0.0
Poland	3.7	3.4	2.5	2.5	3.3	2.4	2.6	0.1	0.1	-0.1
Romania	0.7	-0.5	2.2	2.5	0.7	2.5	2.7	-1.2	-0.3	-0.2
Eastern Europe	1.1	0.9	1.2	1.3	1.2	1.3	1.3	-0.3	-0.1	0.0
Belarus	1.3	1.9	1.2	1.1	1.2	1.0	1.0	0.7	0.2	0.1
Moldova	2.4	1.5	2.3	3.2	1.9	3.2	3.6	-0.4	-0.9	-0.4
Russia	1.0	0.9	0.9	1.0	1.1	1.1	1.0	-0.2	-0.2	0.0
Ukraine	1.8	1.0	3.5	4.2	2.0	3.5	4.2	-1.0	0.0	0.0
Southeastern European Non-EU Member States	2.6	3.2	3.5	3.3	2.9	3.3	3.3	0.3	0.2	0.0
Albania	3.7	3.5	3.2	3.2	3.4	3.2	3.2	0.1	0.0	0.0
Bosnia and Herzegovina	2.4	2.3	2.6	3.0	2.2	2.7	3.0	0.1	-0.1	0.0
Kosovo	3.6	3.5	3.6	4.0	3.3	3.8	4.0	0.2	-0.2	0.0
Montenegro	2.7	3.0	2.8	3.0	2.8	2.7	3.2	0.2	0.1	-0.2
North Macedonia	3.5	3.5	3.2	3.0	3.1	3.0	3.0	0.4	0.2	0.0
Serbia	2.0	3.3	4.0	3.5	2.8	3.5	3.5	0.5	0.5	0.0
Türkiye	3.7	2.7	3.6	4.0	3.4	3.5	3.8	-0.7	0.1	0.2
Memorandum										
World	3.5	3.1	3.4	3.3	3.1	3.2	3.2	0.0	0.2	0.1
Advanced economies	2.0	2.1	1.8	1.7	1.8	1.7	1.7	0.3	0.1	0.0
Emerging market and developing economies	4.5	3.7	4.4	4.3	3.9	4.2	4.2	-0.2	0.2	0.1
European Union	1.5	1.4	1.4	1.5	1.3	1.4	1.6	0.1	0.0	-0.1
Euro Area excl. Ireland	1.0	1.2	1.1	1.2	1.0	1.2	1.3	0.2	-0.1	-0.1
Emerging and developing Europe	2.0	1.7	2.1	2.3	2.0	2.1	2.3	-0.3	0.0	0.0
Emerging Europe excl. Belarus, Russia, Türkiye and Ukraine	2.5	2.3	2.5	2.6	2.5	2.5	2.7	-0.2	0.0	-0.1
CESEE	2.1	1.7	2.1	2.3	2.0	2.1	2.3	-0.3	0.0	0.0
CESEE excl. Belarus, Russia, Türkiye and Ukraine	2.4	2.2	2.4	2.5	2.4	2.4	2.6	-0.2	0.0	-0.1
United States	2.3	2.3	2.3	2.1	2.3	2.1	2.1	0.0	0.2	0.0
China	5.0	4.5	4.0	4.0	4.4	4.0	4.0	0.1	0.0	0.0

Sources: IMF, World Economic Outlook (WEO); and IMF staff calculations.

Annex Table 1.2. Headline Inflation*(Year-over-year percent change; aggregation based on GDP in purchasing power parity terms)*

	October 2026 WEO				April 2026 WEO			Difference		
	2025	2026	2027	2028	2026	2027	2028	2026	2027	2028
Europe	6.1	5.8	5.1	4.1	5.4	4.3	3.8	0.4	0.8	0.3
Advanced European Economies	2.3	2.9	2.7	2.1	2.6	2.2	2.1	0.3	0.5	0.0
Euro Area	2.1	3.1	2.8	2.2	2.6	2.2	2.1	0.5	0.6	0.1
Austria	3.6	3.1	3.3	2.1	2.5	2.6	2.1	0.6	0.7	0.0
Belgium	3.0	3.8	2.9	2.1	2.8	2.2	2.1	1.0	0.7	0.0
Bulgaria	3.5	4.9	4.8	3.4	3.8	3.7	3.4	1.1	1.1	0.0
Croatia	4.4	4.5	3.3	3.0	4.4	2.7	2.5	0.1	0.6	0.5
Cyprus	0.8	3.7	1.9	2.0	2.6	1.6	2.0	1.1	0.3	0.0
Estonia	4.8	3.0	3.3	2.4	3.8	3.0	2.8	−0.8	0.3	−0.4
Finland	1.8	2.4	1.6	1.8	2.5	2.2	2.0	−0.1	−0.6	−0.2
France	0.9	2.4	2.2	1.9	1.8	1.7	1.9	0.6	0.5	0.0
Germany	2.3	2.7	3.1	2.0	2.7	2.3	2.0	0.0	0.8	0.0
Greece	2.9	4.2	3.6	2.2	3.5	2.7	2.5	0.7	0.9	−0.3
Ireland	2.1	3.4	2.8	1.9	3.1	2.4	1.9	0.3	0.4	0.0
Italy	1.6	3.3	2.8	2.3	2.6	2.4	2.3	0.7	0.4	0.0
Latvia	3.8	3.6	3.9	3.3	3.0	2.7	2.9	0.6	1.2	0.4
Lithuania	3.4	5.4	3.5	3.0	4.0	2.7	2.7	1.4	0.8	0.3
Luxembourg	2.5	3.0	2.6	2.0	2.1	2.2	2.1	0.9	0.4	−0.1
Malta	2.4	2.4	2.2	2.0	2.5	2.4	2.0	−0.1	−0.2	0.0
Netherlands	3.0	2.9	2.8	2.6	2.7	2.4	2.3	0.2	0.4	0.3
Portugal	2.2	3.2	3.0	2.1	3.1	2.3	2.4	0.1	0.7	−0.3
Slovak Republic	4.2	3.6	3.5	2.9	4.2	3.3	2.9	−0.6	0.2	0.0
Slovenia	2.5	3.5	2.5	2.2	2.9	2.1	2.3	0.6	0.4	−0.1
Spain	2.7	3.7	2.7	2.5	3.0	2.3	2.5	0.7	0.4	0.0
Nordic Economies	2.6	2.0	2.4	2.4	2.2	2.2	2.4	−0.2	0.2	0.0
Denmark	1.8	1.8	2.5	2.0	2.0	2.2	2.2	−0.2	0.3	−0.2
Iceland	4.1	5.6	3.6	2.4	4.8	2.8	2.5	0.8	0.8	−0.1
Norway	3.0	3.2	2.8	2.3	3.3	2.6	2.2	−0.1	0.2	0.1
Sweden	2.6	1.1	1.9	2.7	1.5	1.8	2.6	−0.4	0.1	0.1
Other European Advanced Economies	2.8	2.7	2.5	1.9	2.7	2.1	1.9	0.0	0.4	0.0
Andorra	2.4	4.0	3.2	2.4	3.0	2.3	2.0	1.0	0.9	0.4
Czech Republic	2.5	2.1	2.8	2.7	2.4	2.2	2.5	−0.3	0.6	0.2
Israel	3.0	1.8	2.0	2.0	2.3	2.1	2.0	−0.5	−0.1	0.0
San Marino	2.2	2.8	2.6	2.2	2.8	2.6	2.0	0.0	0.0	0.2
Switzerland	0.2	0.7	0.8	0.8	0.5	0.5	0.6	0.2	0.3	0.2
United Kingdom	3.4	3.3	2.8	2.0	3.2	2.4	2.0	0.1	0.4	0.0

	October 2026 WEO				April 2026 WEO			Difference		
	2025	2026	2027	2028	2026	2027	2028	2026	2027	2028
Emerging European Economies	14.0	11.8	9.9	8.2	10.9	8.4	7.3	0.9	1.5	0.9
Central and Southeastern European EU Member States	4.7	4.3	3.2	3.8	4.6	3.5	3.9	-0.3	-0.3	-0.1
Hungary	4.4	1.9	2.8	3.0	3.8	3.5	3.1	-1.9	-0.7	-0.1
Poland	3.6	3.2	2.8	3.9	3.3	3.3	3.9	-0.1	-0.5	0.0
Romania	7.3	8.2	4.1	4.3	7.8	3.9	4.3	0.4	0.2	0.0
Eastern Europe	8.9	6.3	5.1	4.3	5.7	4.6	4.2	0.6	0.5	0.1
Belarus	6.6	5.1	5.1	5.1	6.4	6.2	5.7	-1.3	-1.1	-0.6
Moldova	7.8	7.4	9.0	5.3	6.4	5.5	5.0	1.0	3.5	0.3
Russia	8.7	6.1	4.8	4.0	5.6	4.3	4.0	0.5	0.5	0.0
Ukraine	12.7	8.9	8.7	6.7	6.1	7.7	5.7	2.8	1.0	1.0
Southeastern European Non-EU Member States	3.7	3.8	3.9	2.8	4.7	4.0	2.8	-0.9	-0.1	0.0
Albania	2.2	3.2	3.2	3.0	3.4	3.1	3.0	-0.2	0.1	0.0
Bosnia and Herzegovina	4.0	5.0	3.3	2.0	4.5	2.9	2.0	0.5	0.4	0.0
Kosovo	3.9	6.8	4.5	2.4	5.9	3.6	2.2	0.9	0.9	0.2
Montenegro	3.9	3.5	3.3	2.3	3.2	2.9	2.3	0.3	0.4	0.0
North Macedonia	4.1	4.0	4.5	3.4	4.5	4.1	3.2	-0.5	0.4	0.2
Serbia	3.9	3.1	4.2	3.1	5.2	4.9	3.0	-2.1	-0.7	0.1
Türkiye	34.9	31.2	26.5	20.6	28.6	21.4	17.0	2.6	5.1	3.6
Memorandum										
World	4.1	4.7	4.1	3.5	4.4	3.7	3.4	0.3	0.4	0.1
Advanced economies	2.5	3.1	2.7	2.1	2.8	2.2	2.1	0.3	0.5	0.0
Emerging market and developing economies	5.2	5.7	5.1	4.4	5.5	4.6	4.1	0.2	0.5	0.3
European Union	2.5	3.1	2.8	2.4	2.8	2.4	2.4	0.3	0.4	0.0
Euro Area excl. Ireland	2.1	3.0	2.8	2.2	2.6	2.2	2.2	0.4	0.6	0.0
Emerging and developing Europe	13.5	11.3	9.5	8.0	10.5	8.2	7.1	0.8	1.3	0.9
Emerging Europe excl. Belarus, Russia, Türkiye and Ukraine	4.6	4.4	3.4	3.7	4.6	3.6	3.7	-0.2	-0.2	0.0
CESEE	12.9	10.9	9.2	7.6	10.1	7.9	6.8	0.8	1.3	0.8
CESEE excl. Belarus, Russia, Türkiye and Ukraine	4.2	4.0	3.3	3.5	4.2	3.3	3.4	-0.2	0.0	0.1
United States	2.7	3.6	2.8	2.1	3.2	2.1	2.2	0.4	0.7	-0.1
China	0.0	1.0	1.4	1.6	1.2	1.5	1.8	-0.2	-0.1	-0.2

Sources: IMF, World Economic Outlook (WEO); and IMF staff calculations.

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IN THIS ISSUE

CHAPTER 1

Choosing Growth: Reforms for Innovation, Scale, and Resilience



PUBLICATIONS

REGIONAL ECONOMIC OUTLOOK
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