Macroeconomics of the region

Macroeconomics of countries:

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Trends:

- **The world economy**: relatively even growth of the economies of developed countries, the stability of major currencies against the US dollar following an increase in the Federal Reserve System’s interest rate, a fall in prices of oil and metals in Q3-Q4 2015
- **The United States**: an increase in the interest rate of the Federal Reserve System in December
- **Europe**: the recovery of economic growth amid the loose monetary policy of the European Central Bank
- **Asia**: acceleration of GDP growth in Japan, the careful weakening of the national currency in China
- **The CIS**: A fall in the Russian ruble’s value in July-August, stabilization in September
- Currency depreciation in Kazakhstan, the risk of a slowdown in GDP growth in the Asian part of the region
- Continued Western sanctions against Russia amid efforts to resolve the armed conflict in Ukraine

Outlook and risks:

- **The world economy**: continued GDP growth in developed countries, the risk of a slowdown in growth in China
- **Commodity markets**: volatility amid the resumption of oil exports by Iran
- **The CIS**: the stabilization of economic activity, an improvement in the state of balances of payments amid more flexible exchange rate policies

The present analytical report was prepared by the Research Department of Eurasian Development Bank (EDB). The information and conclusions contained in this report are not a recommendation and are based on public data.

Y. Dmitriyeva, Head of the EDB Research Department

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In Q3 2015 the aggregate GDP of the CIS countries fell by 3.9% compared with Q3 2014 against a year-on-year fall of 4.4% in Q2 2015. The depth of the slump in the region’s economy thus began to decrease, primarily due to the effect of the low base of comparison in Russia, Belarus and Ukraine. The magnitude of the GDP fall in these three countries was smaller than 2014 because their GDPs grew or fell insignificantly compared with Q2 2015. Thus economic activity in the region stabilized as GDP ceased to fall further in the countries that were the first ones to be affected by the current recession.

This stabilization took place despite the fact that oil prices resumed falling in Q3 2015. The fall was caused by: the expected resumption of oil exports from Iran; the slow re-balancing of the oil market after a fall in prices in late 2014 and early 2015; and a slowdown in economic growth in developing countries. Apart from the fall in oil prices, Q3 2015 saw a fall in the world prices of metals, which are an important export item for the CIS countries.

Although there was a decrease in capital outflows as a consequence of some decline in tension over the Ukraine conflict, the decrease in proceeds from oil exports did not lead to a fall in domestic demand, which would have outweighed the continued rise in net exports. The increase in net exports was due to both a real fall in imports and a real rise in exports. This was primarily due to an increase in the physical volume of exports of crude oil, natural gas and metals from Russia.

The GDP dynamics of the group of oil and gas exporting countries, which includes Russia, Kazakhstan and Azerbaijan, slightly improved in Q3 2015 amid mixed dynamics within the group.
The labor exporting countries continue to have a positive annual growth rate of their aggregate GDP. However, the rate fell considerably, decreasing to 2.6% from an impressive 5.4% in Q2 2015. The economic growth of this group of countries continued to be ensured by growth in the extractive and metallurgical industries in Armenia and Kyrgyzstan. Most of the other economic sectors from this group’s countries showed deterioration in Q3 2015. This was amid a decline in the volume of migrant remittances from Russia, which was hit by currency depreciation; and a decline in investment inflows and weaker demand for their major export items. Nonetheless, Moldova was the only country of this group to have a negative GDP growth rate in Q3 2015.

The magnitude of the GDP fall in the group of countries with a diversified structure of exports remains significant.

The positive changes in the state of the balance of payments in the region extend into Q3 2015.

The improvement in the current account balance is more significant in the labor exporting countries, as well as in the countries with a diversified structure of exports.

The labor exporting countries (Armenia, Kyrgyzstan and Tajikistan) still had a positive annual growth rate of their aggregate GDP. However, the rate fell considerably, decreasing to 2.6% from an impressive 5.4% in Q2 2015. The economic growth of this group of countries continued to be ensured by growth in the extractive and metallurgical industries in Armenia and Kyrgyzstan. Most of the other economic sectors of this group’s countries showed deterioration in Q3 2015. This was amid a decline in the volume of migrant remittances from Russia, which was hit by currency depreciation; and a decline in investment inflows and weaker demand for their major export items. Nonetheless, Moldova was the only country of this group to have a negative GDP growth rate in Q3 2015.

The magnitude of the GDP fall in the group of countries with a diversified structure of exports (Belarus, Ukraine and Uzbekistan) remained significant at 6.4%. However, it considerably decreased compared with Q2 2015, when it was 11.8%. This change was largely due to the economic dynamics in Ukraine, where there were signs of a post-war recovery of economic activity as the internal armed conflict settled down to a less intense phase.

The positive changes in the state of the balance of payments in the region that were seen in Q1-Q2 2015 extended into Q3 2015. The CIS countries’ current account surplus grew from 0.9% of their aggregate GDP in Q3 2014 to 1.2% in Q3 2015. The growth of the current account surplus was less significant in the oil and gas exporting countries. This reflected: a decrease in the current account surplus in Russia due to a fall in capital outflows; and deterioration in the balances of payments of Kazakhstan and Azerbaijan amid a relatively tight exchange rate policy pursued by their central banks. Kazakhstan loosened control of the exchange rate of the national currency in Q3 2015 and Azerbaijan did the same in December 2015. Foreign trade statistics indicate that the improvement in the current account balance was more significant in the labor exporting countries. It was also significant in the countries with a diversified structure of exports, where the balance had a surplus equal to 0.2% of GDP after a deficit amounting to 3.5% of GDP in Q3 2014. However, the strengthening of the national currencies in terms of the REER (real effective exchange rate) in Q3 2015 in these groups of countries may lead to doubts about the stability of this improvement.
The state of public finances deteriorated in almost all CIS countries compared with Q3 2014 amid a fall in revenue due to the economic recession and a decrease in export proceeds. Out of the three groups of countries, only the countries with a diversified structure of exports improved the average state budget balance due to an improvement in Ukraine’s budgetary situation. Belarus’s budgetary situation was worse than in Q3 2014 as the budget balance moved into negative territory, but a significant improvement in the state of the country’s budget in Q1-Q2 2015 ensured a positive figure for Q1-Q3 2015. Further acceleration in the fall in oil prices in the middle of 2015 led to increased pressure on the national currencies of the CIS countries. The central banks’ effort to limit the volatility of exchange rates led to the de facto tightening of monetary policy in all countries in the region except Russia, where the central bank was consistent in implementing a floating exchange rate policy. As a result of the tighter monetary policy, the annual growth rate of M2 money supply moved into negative territory for the countries with a diversified structure of exports, shifting from +6% in Q2 2015 to -2% in Q3 2015. The rate remained negative for the labor exporting countries at -4.6%. It continued to be positive and even rose slightly for the oil and gas exporting countries, reflecting the stable dynamics of the money supply in Russia. However, in Kazakhstan and especially Azerbaijan, the rate remained deep in negative territory.

Under these circumstances, annual inflation gradually slowed down in the CIS region to an average of 16.9% in Q3 2015. Moldova was the only country in the region to experience an acceleration of inflation in the period, which was caused by a significant increase in the government-regulated electricity and gas supply rates in August.

Given the deteriorating external environment, central banks changed their policy towards more flexible exchange rates of their national currencies. A significant event for the region was the decision of the National Bank of Kazakhstan to stop pegging the tenge to the dollar and the subsequent considerable depreciation of the tenge. A flexible exchange rate policy was also pursued in Kyrgyzstan, whose currency was falling against the dollar throughout Q3 and in Q4 2015. Other central banks retained a high degree of control over exchange rates. There continued to be relatively stable exchange rates of the Tajik somoni – at the price of tighter control over the currency exchange market in the country – and the Armenian dram. In Belarus, under the conditions of an officially announced flexible exchange rate policy, the national currency sharply depreciated against the currency basket of the dollar, the euro and the Russian ruble. This was followed by a period of stability for the value of the Belarusian rubel.

### Figure 1.5. Government budget: (in % of GDP)

![Graph showing government budget](image1)

**Source:** national agencies

### Figure 1.6. Monetary sphere: (in %, year-on-year)

![Graph showing monetary sphere](image2)

**Source:** national agencies

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**The countries with a diversified structure of exports improve their average state budget balance**

**Further acceleration in the fall in oil prices in the middle of 2015 leads to increased pressure on national currencies**

**Annual inflation gradually slows down in the CIS region to an average of 16.9% in Q3 2015**

**Central banks’ policies change throughout Q3 2015 towards more flexible exchange rates**
As for the negative impact of the new wave of currency depreciation in CIS countries in Q3 and Q4 2015 on economic growth, we predicted in the previous issue of the CIS Macromonitor that this impact would be the most significant for the Central Asian CIS countries. This prediction proved to be correct. There is currently deterioration in the economic dynamics in Kazakhstan and Kyrgyzstan. Armenia and Azerbaijan are also experiencing a slowdown in economic growth. The extent of the slowdown will eventually depend on the dynamics of the prices of primary commodities, especially oil, throughout 2016. If there is no additional significant fall in these prices, one can expect that the relative stability of economic activity in the European part of the region, primarily in Russia, will cause the corrective process in the economies of the Central Asian and Caucasian countries to end relatively quickly. Most of the countries will have positive GDP growth rates in 2016, although they will be significantly lower than those in 2015.

The base-case scenario for the economic situation in the world, which we currently use, assumes that: the economies of developed countries, primarily the United States, the Eurozone countries and Japan, will keep growing at rates similar to the current rates; and that China’s economic growth will stabilize, which will be due, in particular, to the Chinese central bank’s more flexible exchange rate policy. The dynamics of oil prices will depend, on the one hand, on the rise in exports from the OPEC countries, including Iran following the lifting of international sanctions against the country, and on the other hand, on the expected reduction in oil production in fields where production costs are relatively high, primarily in the United States. We expect the average price of Brent oil to be between $40 and $50 per barrel in 2016.

Under this scenario, the aggregate GDP of the CIS countries will fall by 3.5 to 4% in 2015 and resume growth later, increasing by up to 1% in 2016.
Azerbaijan: slowdown in GDP growth and contraction in international reserves amid improvement in public finances and low inflation

Azerbaijan’s GDP growth slowed to almost zero in Q3 2015. This resulted in a year-on-year growth rate of 3.7% in Q1-Q3 2015 compared with a growth of 5.7% in Q1-Q2 2015. The significant slowdown in GDP growth was caused by a shift of the growth rates of the construction sector and the oil and gas sector into negative territory amid steadily low prices of oil and other primary commodities in Q3 2015. Despite showing signs of slowdown, which was fueled by currency depreciation, the non-oil sector remained a major driver of growth (+6.4% in Q1-Q3 2015). High growth rates were shown by the non-oil industrial sector (+10.2%), retail trade (+11.4%), the communications sector (+8.8%) and the services sector (+6.2%). The agricultural sector was also among the drivers of growth with a 6.7% increase in output. Given the negative dynamics of investment and exports (except non-oil exports), consumption was apparently the only source of growth.

The fall in the oil and gas sector amid the continued low crude prices led to a contraction in exports in both real and nominal terms (-6.2% and -46.2% respectively in Q1-Q3 2015). As a result of the depreciation of the manat and the weakening of domestic demand, the growth of imports slowed down further to 4.4% in Q1-Q3 2015. As a consequence, a strong decrease in the trade surplus led to a significant fall in the current account surplus to 0.6% of GDP in Q1-Q3 2015 from 17.6% of GDP in Q1-Q3 2014. Amid a financial account deficit, the decrease in the current account surplus caused a deficit in the balance of payments and a contraction in international reserves. They shrank by $1 billion between March 2015 and the end of September to amount to $8.3 billion.

A combination of the decreased exports and the significant slowdown in economic growth kept affecting the state of the public finances. This was despite some improvement in revenue and a consolidation of expenditure in Q3 2015. State budget revenue fell by 14.2% year-on-year in Q1-Q3 2015 compared with a fall of 16.4% in Q1-Q2 2015, including due to transfers from the State Oil Fund. Expenditure decreased by 4.2% against a year-on-year fall of 1.7% in Q1-Q2 2015.

Nonetheless, the state budget deficit shrank to 0.2% of GDP in Q1-Q3 2015 from 2.9% of GDP in Q1-Q2 2015. The consolidated budget, which includes the State Oil Fund, continued to have a deficit. It stood at 0.6% of GDP in Q1-Q3 2015 as a result of a 44.9% year-on-year decrease in the State Oil Fund’s revenue. The Fund’s assets diminished by $2.4 billion since the beginning of 2015 to $34.7 billion as of the end of September.

The annual inflation rate fell to 3.6% in September 2015 under the influence of external factors, the good performance of the agricultural sector, weakening domestic demand, and a further contraction in the money supply.
Azerbaijan

Figure 2.1. **GDP and output**: GDP growth and output change by sectors, (in %, year-on-year)

Source: the State Statistics Committee of Azerbaijan

Figure 2.2. **Foreign trade**: exports, imports, current account (left scale, in billions of US dollars), real effective exchange rate – REER (right scale, index – Q2 2009 = 100)

Source: national agencies

Figure 2.3. **Government sector**: sum of state budget and oil fund balances (in % of GDP)

Source: national agencies

Figure 2.4. **Monetary sector**: the central bank’s rate (in %), the CPI growth (in %, year-on-year), M2 growth (in %, year-on-year)

Source: national agencies

Figure 2.5. **Economic growth**: GDP growth and forecasts by national and international institutions (in %)

Source: national agencies, estimates by the ADB, the World Bank, the EBRD, the IMF

Figure 2.6. **Savings and investments**: (in % of GDP): balance of private investment and savings (Sp-Ip), state budget (Sg-Ig), current account balance (X-M)

Source: estimates and forecasts by the IMF
Armenia: continued moderate GDP growth amid improvement in balance of payments and low inflation

Armenia’s GDP growth slowed to an estimated 3.3% year-on-year in Q3 2015 compared with a growth of 4.6% in Q2 2015. The slowdown was due to: the continuing recession and currency depreciation in Russia; the low growth rate in Europe; a fall in the prices of metals, including copper; a decrease in food prices, coupled with seasonal factors; tight monetary policy; and declining external competitiveness. Domestic demand weakened due to a 40.4% year-on-year decrease in net cash remittances from abroad and a reduction in lending to the economy in Q3 2015. This led to a continued fall in trade, and kept growth in the construction sector at a low level. The agricultural sector and the mining industry, which experienced positive shocks from the supply side and supported exports, continued to be major drivers of growth. Some branches of the services sector also made a positive contribution. Armenia’s year-on-year GDP growth rate in Q1-Q3 2015 was estimated at 3.5% against a growth of 3.8% in Q1-Q3 2014.

According to the available indirect data, the state of the balance of payments improved in Q3 2015, with the nominal rate remaining stable throughout the period. This is evidenced by the fact that the gross international reserves grew by $79.8 million, or 5.2%, in Q3 2015. The main factor behind the improvement in the balance of payments was apparently a better current account balance, which had a surplus equal to 2.5% of GDP in Q2 2015. This was despite some loss in external competitiveness in the period. The balance of trade deficit decreased by 24.6%. This was due to a combination of expanding exports and a contraction in imports. Exports increased by 17.2% year-on-year in Q3 2015 primarily due to a greater supply of mineral and agricultural products, and imports fell by 10.3%. The financial account also apparently provided some support to the balance of payments.

Despite the GDP growth, which resulted from only a few sectors, the state budget remained in deficit in Q3 2015. The deficit stood at 2.3% of GDP for Q3 2015 and at 1.9% of GDP for Q1-Q3 2015. Given the need to support the weakening domestic demand, the 14.6% year-on-year rise in expenditure significantly outpaced the 4.5% year-on-year increase in revenue, which was affected by declining consumption and the contraction in imports. A distinguishing feature of the state budget in Q3 2015 was a shift of the dynamics of revenue into positive territory. The contraction of major tax revenue became less significant, while more revenue started to be raised from value-added tax and income tax. Also the rise in revenue from customs duties and payments for the use of natural resources became even more pronounced.

Annual inflation slowed to 3.3% in September 2015 due to: external deflationary factors; tight monetary policy (high interest rates, a slowdown in lending growth and a contraction in the money supply); and weakening domestic demand. The central bank apparently preferred to be strict while achieving the goal of keeping the dram stable. The annual growth rate of bank lending fell to 5.7% from 9.6% at the end of Q2 2015, while the share of nonperforming loans in banks’ aggregate loan portfolio decreased to 8.5% from 9.2% in June. The average ROA (return on assets) and ROE (return on equity) ratios remained negative at -0.3% and -2.4%, respectively.
Outlook

Armenia: increased vulnerability of the economy to external factors

The slowdown in economic growth in Q4 2015 may prove sensible because of: deterioration in the terms of trade; the strengthening of the real exchange rate; and a decline in the positive effect of shocks from the supply side in the extractive industry and agricultural sector. The Indicator of Economic Activity entered the phase of recession in October and November 2015. GDP will grow by 2.5 to 2.7% in 2015, whereas the updated consensus forecast predicts a growth of 2.3%.

The outlook for GDP growth in 2016 remains uncertain as a result of increased external vulnerability. There is uncertainty about: the recovery in Russia; the low growth rate in Europe; and the complicated geopolitical situation in the region. Also the low price of metals resulting from the fading effect of shocks from the supply side in combination with the real strengthening of the dram will limit exports and output in the extractive and manufacturing industries. A positive factor for exports may be an increase in the positive effect of the expansion of export routes in the Eurasian Economic Union countries and other regions. The limited instruments of macroeconomic policy, the slowdown in lending growth and the deficiency of structural reform will hold back consumption and investment. The contraction of investment throughout seven years indicates its steady nature. The fall may stop in retail trade, some branches of the services sector, and the construction sector. This may be due to a recovery in migrant remittances. The GDP growth rate in 2016 will be lower than that in 2015 at 1.7% to 2.2%, with the consensus forecast predicting a growth of 2.2%.

The gross international reserves decreased by $75.8 million in October-November 2015 to $1,549.7 million, or 5.2 months’ worth of imports. The deterioration in the state of the balance of payments was caused by the expansion of the trade deficit, which resulted from a decrease in exports and a rise in imports in month-on-month terms. The dram resumed depreciation in the period by virtue of the strengthening of the dollar in world markets. The state of the balance of payments may deteriorate further in 2016 under the influence of: the expansion of the trade deficit and the current account deficit; the continued overvaluation of the dram; and heightened short-term external indebtedness. One should expect continued pressure on the dram and the gross international reserves in the context of difficulties in attracting foreign direct investment.

Low economic activity and the stabilization of foreign trade at a low level will limit opportunities for increasing state budget revenue. Due to this and given the need to maintain social and capital expenditure, the government projects a high state budget deficit at 3.5% of GDP. A combination of the state budget deficit and the current account deficit will determine the extent of the need for external loans, and may become a source of an increase in the public debt. Inflation’s annual rate fell to 1.2% in November 2015, which is below the central bank’s target band of 2.5 to 5.5%. Given the continued stability of the dram’s exchange rate, the major deterrent factors for inflation continue to be: external deflationary factors; tight monetary policy; and weak domestic demand. The government’s ability to keep the inflation rate within the target band in 2016 will mainly depend on the stability of the dram’s exchange rate.

The outlook for GDP growth in 2016 remains uncertain as a result of increased external vulnerability

The balance of payments situation may deteriorate in 2016

The government’s ability to keep the inflation rate within the target band in 2016 will mainly depend on the stability of the dram’s exchange rate
Armenia

Figure 3.1. **GDP and output**: GDP growth and output change by sectors, (in %, year-on-year)

![GDP and output graph]

Source: the National Statistical Service of the Republic of Armenia

Figure 3.2. **Foreign trade**: exports, imports, current account (left scale, in billions of US dollars), real effective exchange rate – REER (right scale, index – Q2 2009 = 100)

![Foreign trade graph]

Source: national agencies, IMF

Figure 3.3. **Government sector**: state budget (in % of GDP)

![Government sector graph]

Source: national agencies

Figure 3.4. **Monetary sector**: the central bank’s rate(in %), the CPI growth (in %, year-on-year), M2 growth (in %, year-on-year)

![Monetary sector graph]

Source: national agencies

Figure 3.5. **Economic growth**: GDP growth and forecasts by national and international institutions (in %)

![Economic growth graph]

Source: national agencies, estimates by the ADB, the World Bank, the EBRD, the IMF

Figure 3.6. **Savings and investments**: (in % of GDP): balance of private investment and savings (Sp-Ip), state budget (Sg-Ig), current account balance (X-M)

![Savings and investments graph]

Source: estimates and forecasts by national agencies and the IMF
Belarus: decrease in magnitude of GDP fall, weakening of national currency in Q3 2015

Belarus’s GDP fell by 3.7% year-on-year in Q1-Q3 2015. As GDP fell by 2.3% in Q1 and 4.5% in Q2, the magnitude of the economic recession decreased to a year-on-year fall of about 4.3% in Q3 2015. Industrial output fell by 7.1% compared with Q1-Q3 2014 after a fall of 7.4% in Q1-Q2 2015, while output in the construction sector decreased by 7.6% after a year-on-year decrease of 7% in Q1-Q2 2015. The fall in GDP was determined by a decrease in fixed capital investment, which fell by 14.2% in Q1-Q3 2015 after a fall of 13.5% in Q1-Q2 2015. Retail sales increased by 0.9% in real terms compared with Q1-Q3 2014 after an increase of 1.1% in Q1-Q2 2015. This indicated the stability of household consumption, although their dynamics deteriorated significantly in September amid a fall in people’s real income following a sharp depreciation of the Belarusian rubel at the end of the summer.

The inflation rate, both monthly and annual, continued to fall throughout most of Q3 2015. The monthly growth rate of the consumer price index decreased to 0.2%, something unseen since 2010, partially due to a seasonal fall in food prices. The annual inflation rate fell to 11.8% in August and rose slightly to 11.9% in September. The government’s success in combating inflation was largely due to the National Bank’s increased control of the exchange rate of the rubel against the currency basket of the U.S. dollar, the euro and the Russian ruble. This resulted in a contraction in money supply (the annual growth rate of the M2 money supply became negative in August), and a resumed rise in the real effective exchange rate (REER). The devaluation of the national currency in late August was a one-time measure. After devaluing the rubel by 12.5% against the currency basket, the National Bank increased control of the rubel again.

The rise in the REER in Q3 2015 amounted to about 2.5% compared with Q2 2015 and 5.4% compared with Q3 2014. It had no immediate impact on the state of the external balance of the economy. The current account balance of the balance of payments remained positive, and had a surplus of $432.6 million (3.1% of GDP) in Q2 2015. Although the surplus decreased to $14 million (about 0.1% of GDP) largely due to the seasonal withdrawal by foreign companies of their investment proceeds. Amid a moderate inflow of capital – the financial account deficit in Q3 2015 amounted to $117 million after a surplus of $523 million in Q2 2015 – the international reserves of the National Bank continued to grow slowly. They amounted to $4,629 million, or 1.6 months’ worth of imports, at the end of September.

The state of the budget balance was also significantly better than 2014. The consolidated budget had a surplus of 2.2% of GDP in Q1-Q3 2015 against a surplus of 0.8% of GDP in Q1-Q3 2014. The government used the surplus to repay the public debt.

The annual growth rate of bank lending to the economy, which began in Q3 2014 with a fall, rose again following the currency devaluation in August, reflecting the revaluation of loans in foreign currency. The rate increased to 30.5% in September from 27.4% in June.
Outlook
Belarus: risk of deeper economic fall amid tight monetary policy, improvement in condition of state budget

The decrease in the magnitude of the fall in investment activity and an improvement in the dynamics of output in the agricultural sector had a positive effect on the GDP dynamics in Q3 2015. Despite this, negative trends in the economy became pronounced in September. Amid a fall in real pay in the country, the growth rate of retail sales shifted into negative territory. This suggested that the steady dynamics of household consumption in Q1-Q3 2015, which had a stabilizing effect on the economy in general, may cease to play such a role in Q4 2015 and in 2016. Simultaneously, under the conditions of the National Bank’s tight monetary policy and the continued high interest rates on loans, the fall in investment activity increased. After the annual fall in fixed capital investment decreased to 10% in August, it reached 12.2% in September and 17.9% in October (partially due to the high base of comparison), and decreased again to 14.7% in November. If the dynamics of private consumption and investment do not change in Q4 2015 and Q1 2016, one can expect that the Belarusian economy will decrease by about 4% in 2015 and be close to zero growth in 2016.

The National Bank’s tight monetary policy resulted in a high degree of stability of the Belarusian ruble against the currency basket, which could be seen again after the devaluation in the late summer. This led to a slowdown in the rise in prices in the country after a short acceleration in September. As a result, the annual growth rate of the consumer price index remained between 11% and 12% and will probably be 11.1 to 11.4% at the end of 2015. Such a rate would mean a significant fall as the annual inflation rate was above 20% in mid-2014 and had never fallen below 14.9% since April 2011. At the same time we are not sure that similar significant progress in fighting inflation will be made in 2016. Firstly, it is most likely that the low volatility of the exchange rate of the Belarusian ruble against the currency basket, which has lasted since September, will eventually create pressure on the balance of payments and economic growth. Secondly, a temporary acceleration of inflation may happen as a consequence of the lifting of government control over prices and an increase in energy prices. As a result, the annual growth rate of the consumer price index may remain in a range from 9 to 10.5%.

Meanwhile, the consolidation of domestic demand in 2015 led to a marked improvement in the state of the balance of payments. The current account deficit in Q1-Q3 2015 amounted to 2% of GDP. Given the Q4 seasonal dynamics (deterioration in the foreign trade balance at the end of 2015 because of a rise in energy imports) the deficit may remain within a range from 2 to 3% of GDP for 2015 against a deficit equal to 6.8% of GDP in 2014. A contribution to the strengthening of the positive trend will be made by relatively tight fiscal policy. Both the republican budget and the consolidated budget of the country will apparently have a surplus in 2015. The adopted 2016 budget estimates also provide for a surplus, which is projected to amount to 2% of GDP and be used for repaying the public debt.
Belarus

Figure 4.1. **GDP and output**: GDP growth and output change by sectors, (in %, year-on-year)

![GDP and output chart]

Source: the National Statistics Committee of Belarus

Figure 4.2. **Foreign trade**: exports, imports, current account (left scale, in billions of US dollars), real effective exchange rate – REER (right scale, index – Q2 2009 = 100)

![Foreign trade chart]

Source: national agencies, IMF

Figure 4.3. **Government sector**: consolidated budget (in % of GDP)

![Government sector chart]

Source: national agencies

Figure 4.4. **Monetary sector**: the central bank’s rate (in %), the CPI growth (in %, year-on-year), M2 growth (in %, year-on-year)

![Monetary sector chart]

Source: national agencies, IMF (IFS)

Figure 4.5. **Economic growth**: GDP growth and forecasts by national and international institutions (in %)

![Economic growth chart]

Source: national agencies, estimates by the EBD, the World Bank, the EBRD, the IMF

Figure 4.6. **Savings and investments**: (in % of GDP): balance of private investment and savings (Sp-Ip), state budget (Sg-Ig), current account balance (X-M)

![Savings and investments chart]

Source: estimates and forecasts by national agencies, the IMF and the EBD
The Kazakh economy experienced difficulties in Q3 2015. The accumulated structural imbalances were strongly aggravated by: a fall in the price of exported primary commodities; a further slowdown in economic growth in China; a weak recovery in growth in Europe; the strengthening of the dollar in world markets; the recession in Russia; and a loss of external competitiveness. The negative impact of the unfavorable external environment amid the heightened vulnerability of the economy to external shocks manifested itself in: zero GDP growth; a decrease in international reserves and depreciation of the tenge after the government switched to a flexible exchange rate regime; expansion of the consolidated budget deficit; forced tightening of monetary policy following a formal transition to inflation targeting; and contraction in bank lending in real terms.

The fall in economic activity in Q3 2015 affected the industrial sector, whose output fell by 4.4% year-on-year. The fall in the mining industry (-7.7%), which reflected a decrease in the production of oil (-4.9%), coal (-6.4%) and ferrous ore (-38.4%) offset modest growth in manufacturing industry (+0.3%), which received support from the government. The weakening of domestic demand caused negative growth rates in retail trade (-2.1%) and the communications sector (-0.2%). An improvement in the growth figures of the agricultural sector (+3.3%), the construction sector (+4%) and the services sector proved insufficient. The growth in these sectors was due to anti-crisis measures aimed at stimulating domestic demand. As a result, the country had zero GDP growth in Q3 2015 and 1% growth in Q1-Q3 2015.

Q3 2015 saw deterioration in the state of the balance of payments. The current account balance had a surplus equal to 3.7% of GDP as a result of a contraction in the foreign trade surplus in the period to 5.8% of GDP from 13.3% of GDP in Q3 2014 amid constantly negative balances of services and revenue. Deterioration of the foreign trade situation provoked a sharp year-on-year decrease in exports (-40.1%), while the fall in imports was less significant at -28.1%. An important factor in this regard was the real strengthening of the tenge, which supported imports. The current account deficit was compensated for by external loans and the international reserves. The gold and foreign exchange reserves of the National Bank shrank by $624 million in Q3 2015, and the resources of the National Fund of Kazakhstan decreased by $1.106 million. The need to reduce external imbalances accelerated the transition to a flexible exchange rate regime in July and August 2015, which eventually led to a 28% correction in the value of the tenge.

There was a negative impact on the state and consolidated budgets from a combination of: zero GDP growth; declining foreign trade; a limited use of transfers from the National Fund of Kazakhstan in the period; and the implementation of anti-crisis measures. The state budget had a deficit equal to 6% of GDP in Q3 2015 and a deficit equal to 2.4% of GDP in Q1-Q3 2015. The consolidated budget had a deficit equal to 4% in Q3 2015 and a deficit amounting to 4.7% of GDP in Q1-Q3 2015. The correction in the value of the tenge had a positive effect on public revenue as early as September. Another consequence of the currency depreciation was acceleration of annual inflation to 4.4%. High inflation expectations amid continuing devaluation expectations led to increased interest rates on loans, problems with liquidity, and a contraction in bank lending.
**Outlook**

**Kazakhstan: low GDP growth rate amid negative current account balance and high inflation**

The rise in the short-term Indicator of Economic Activity in annual terms was negative in October-November 2015 and was 0.4% in the first 11 months of 2015. An improvement in the situation cannot be expected in Q4 2015 amid: the consolidation of public expenditure; limited fiscal stimulus; the negative impact of currency depreciation on private investment and consumption (household real income fell by 5.8% in October 2015 in annual terms); and the continued unfavorable outlook for the external environment. GDP will grow by between 0.7% and 0.9%.

The outlook for the mining industry for 2016 remains negative considering: the less-dynamic-than-expected growth of the global economy; the low growth rate of Kazakhstan’s major trading partners; the continued low prices of oil and other exported primary commodities; and the expected fall in the volume of oil and gas condensate production. Nonetheless, one should expect some stimulus for manufacturing industry, the construction sector and various branches of the services sector from: the improving external competitiveness as a result of the transition to a flexible exchange rate regime; the country’s accession to the WTO; the implementation of structural reform (including measures to foster the private sector); and fiscal stimulation for maintaining household income and investment activity, which will lead to a GDP growth of 0.9% to 1.2%.

The balance of payments remains dependent on: the price of primary commodities; the state of the mining industry; the government’s macroeconomic policy; diminishing foreign investment; and the volume of external borrowings. The state of the balance of payments improved in October-November 2015. This was indirectly evidenced by the fact that the gold and foreign exchange reserves grew by $396 million in the period. On the one hand, due to the currency depreciation, the fall in imports should accelerate. On the other hand, the use of resources from the National Fund of Kazakhstan, whose assets decreased by $3,683 million in October-November 2015, simultaneously supported the budgetary balance and the balance of payments. Despite the improvement in external competitiveness, the current account balance will probably remain negative in the remainder of 2015 and in 2016 because of limited opportunities for increasing exports and a continued strong need for imports.

The state budget had a deficit equal to 3% of GDP in 2015. The state of public finances may improve in 2016 as a result of: fiscal consolidation; the use of resources from the National Fund; and the compensatory effect of the correction in the value of the tenge. The government expects a state budget deficit equal to 1.6% of GDP. The currency depreciation will lead to an acceleration of annual inflation (12.8% in November 2015) throughout Q1-Q2 2016. The expected rise in inflation is attributable to: the significant share of imports in consumption; the transition to a flexible exchange rate regime; and more liberal price formation in the economy, including price formation for fuel and some other goods. In Q3-Q4 2016, inflation should slow down under the influence of tighter monetary policy, weak domestic demand, and external deflationary factors. High inflation and the remaining pressure on the tenge will cause liquidity problems to continue and interest rates on loans to remain high.

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**The country’s GDP will grow by 0.7 to 0.9% in 2015 and by 0.9 to 1.2% in 2016**

**The current account balance will probably remain negative in 2016**

**The state of public finances may improve in 2016**

**Inflation will remain high throughout Q1-Q2 2016**
Kazakhstan

**Figure 5.1. GDP and output**: GDP growth and output change by sectors, (in %, year-on-year)

Source: the Agency of Statistics of Kazakhstan

**Figure 5.2. Foreign trade**: exports, imports, current account (left scale, in billions of US dollars), real effective exchange rate – REER (right scale, index – Q2 2009 = 100)

Source: national agencies, IMF

**Figure 5.3. Government sector**: consolidated and state budgets (in % of GDP)

Source: national agencies

**Figure 5.4. Monetary sector**: the central bank’s rate(in %), the CPI growth (in %, year-on-year), M2 growth (in %, year-on-year)

Source: national agencies, IMF (IFS)

**Figure 5.5. Economic growth**: GDP growth and forecasts by national and international institutions (in %)

Source: estimates and forecasts by national agencies the EDB, ADB, the World Bank, the EBRD, the IMF

**Figure 5.6. Savings and investments**: (in % of GDP): balance of private investment and savings (Sp-Ip), state budget (Sg-Ig), current account balance (X-M)

Source: estimates and forecasts by national agencies, the IMF and the EBD
**Trends**

**Kyrgyzstan: recovery in consumption amid crisis in construction and decrease in gold production**

Kyrgyzstan continued to have quite strong GDP growth with a year-on-year rate of 4.3% in Q3 2015. The growth was supported by a recovery in consumption activity in both the public and private sector. Agricultural output rose by 13.5% year-on-year amid favorable weather conditions and a parliamentary election campaign. Retail sales increased by 7% as a result of increased government spending and a slowdown in inflation. However, statistical data in September saw signs of a crisis in the construction sector and a fall in gold production. Kyrgyzstan’s GDP grew by 6.3% year-on-year in Q1-Q3 2015.

The balance of payments in Q3 2015 was largely determined by external factors such as the fall in the world prices of primary commodities and the weakening of the national currencies of major trading partners. The decrease in foreign currency inflows and deterioration in the current account balance resulted from: the decrease in domestic gold production; lower international gold prices; and the depreciation of many currencies against the US dollar. These dynamics, coupled with the sharp depreciation of the Kazakhstan tenge in August, caused increased volatility in the currency exchange market and a fall in the value of the som. The rise in the price of imported goods led to the weakening of demand for them. As a result, the current account deficit slowed down to 8.8% of GDP. The inflow of foreign direct investment and foreign borrowings by the private sector helped to finance the foreign trade deficit, but not to a sufficient degree.

There was a significant increase in tax revenue in Q3 2015 in both nominal and real terms. Non-tax payments supported the state budget in Q1-Q2 2015 amounting to 16.4% of GDP; they decreased to 4.8% of GDP in Q3 2015. Despite moderate spending on capital expenditure, a rise in operating expenditure led to an increase in the current budget deficit to 5.9% of GDP in Q3 2015. Although the overall deficit was low at 1.2% of GDP, the current budget deficit in Q1-Q3 2015 amounted to 6.1% of GDP amid decreased operating revenue and continued high operating expenditure.

The increased public spending led to inflationary pressure and increased volatility in the currency exchange market. The annual inflation rate rose from 4.6% in June 2015 to 6.4% in September. The National Bank raised its base lending rate and increased its presence in the internal foreign exchange market. Nonetheless, due to the fall in imports, the level of international reserves by the end of September was sufficient to finance 4.2 months’ worth of imports of goods and services.

In September, amid increased depreciation expectations, the expansion of the deposit base was ensured by deposits in foreign currency. Despite the increased role of foreign currency as a means of saving, there were some signs of recovery in the dynamics of deposits in som. At the same time, amid restrictions on lending in foreign currency and a slowdown in the growth of such lending, there was a currency mismatch between the assets and liabilities of banks. It was fraught with problems for the banks in case of deterioration in the financial position of the borrowers.
Outlook
Kyrgyzstan: slowdown in economic growth and a further fall in construction output

Kyrgyzstan’s industrial output decreased and GDP fell by about 8% year-on-year in October-November 2015 amid a contraction in precious metal production. Growth in the construction sector slowed further to 1.8% year-on-year, while fixed capital investment fell by 6.5%. Support for economic growth continued to come from the agricultural sector (+6.6%) and wholesale and retail trade (+6.8%), although the growth rate in the services sector was falling as crisis symptoms in the economy became more pronounced. As a result Kyrgyzstan may have a GDP growth rate of 2.5 to 3% in 2015. The aggravation of the economic situation may cause the GDP growth rate to continue to be low in 2016. However, if the growth of private investment resumes, an acceleration of economic growth can be expected in the long term considering the new opportunities that have been opened up by Kyrgyzstan’s membership in the Eurasian Economic Union.

Amid strong exchange rate shocks, a major contribution to the rise in consumer prices in October-November 2015 was made by the price of non-food consumer goods and services. These are the most sensitive to fluctuations in the exchange rate. Given increased public spending, prices are expected to rise further in December, with the annual inflation rate to be between 6.5% and 7%. Inflationary pressure may increase in 2016 amid a slowdown in economic activity and continued high public expenditure. However, recurrent forex interventions and tight monetary policy offset, to a certain extent, the rise in the inflation rate, which may average at the level of 2015.

Amid the fall in the price of primary commodities, there were changes in the exchange rate regimes in the countries that are the main trading partners of Kyrgyzstan in 2015. These affected the dynamics of the balance of payments, and led to increased volatility in the exchange rate of the som. Downward fluctuations in the exchange rate resumed in August, and caused the som to weaken by 19.6% against the US dollar and strengthen by 24.5% against the Russian ruble. Given these circumstances, it is important for the National Bank to keep pursuing a flexible exchange rate policy in order to support the economy from the standpoint of both the sustainability of external balance and monetary policy. The measures taken by the central bank to keep the banking system stable amid exchange rate shocks proved to have the necessary effect. The annual growth rate of bank lending in foreign currency moved into negative territory in October, while the growth of foreign-currency deposits slowed down.

The expansion of the state budget deficit resulted from the fall in the exchange rate of the som, and the rise in pay and increased social assistance from the government amid low tax revenue. Given the currently available forecasts for 2016, one can expect this trend to continue. This may cause the country’s external public debt to grow further and cross the mark of 60% of GDP before the end of 2015. Nonetheless, the concessional nature of the debt and the possibility for the government to obtain low-interest loans from both international institutions and neighboring countries prompted Moody’s and Standard & Poors to assign B2 and B sovereign ratings with a stable outlook to the country.
Kyrgyzstan

Figure 6.1. **GDP and output**: GDP growth and output change by sectors, (in %, year-on-year)

Source: the National Statistics Committee of Kyrgyzstan

Figure 6.2. **Foreign trade**: exports, imports, current account (left scale, in billions of US dollars), real effective exchange rate – REER (right scale, index – Q2 2009 = 100)

Source: national agencies

Figure 6.3. **Government sector**: state budget (in % of GDP)

Source: national agencies

Figure 6.4. **Monetary sector**: the central bank’s rate (in %), the CPI growth (in %, year-on-year), M2 growth (in %, year-on-year)

Source: national agencies

Figure 6.5. **Economic growth**: GDP growth and forecasts by national and international institutions (in %)

Source: estimates and forecasts by national agencies the EDB, the ADB, the World Bank, the EBRD, the IMF

Figure 6.6. **Savings and investments**: (in % of GDP): balance of private investment and savings (Sp-Ip), state budget (Sg-Ig), current account balance (X-M)

Source: estimates and forecasts by national agencies, the IMF and the EBD
Moldova experienced a year-on-year GDP fall of 3.7% in Q3 2015 amid a continued recession in neighboring economies; the remaining high uncertainty in the country and outside it; and problems in the banking sector. A 4.6% decrease in consumption was reflected in the dynamics of retail sales, which fell by 2.3% year-on-year. Low investment activity led to a 1.8% year-on-year fall in construction output. Agricultural output fell by 17.4% year-on-year. This was caused by weak domestic demand, and a decrease in the yield of major crops due to extremely unfavorable weather conditions amid the high base effect of 2014. Moldova’s GDP grew by 0.5% year-on-year in Q1-Q3 2015, thus marking a significant slowdown from 3.6% in Q1-Q2 2015. The current consensus forecast predicts a GDP fall of 1.5% for 2015 and a slow recovery to a growth of 1% in 2016.

Lower growth rates of the inflow of foreign currency in the form of migrant remittances and export proceeds led to a further weakening of the national currency. After decreasing the volume of forex interventions, the central bank continued to tighten its monetary policy, raising its base rate to 19.5% in September from 15.5% in June 2015. As a result, the international reserves of the National Bank remained almost unchanged at a level sufficient to finance 3.8 months’ worth of imports of goods and services. However, amid the fall in the leu’s exchange rate, the increased prices of imported goods led to a rise in the annual inflation rate from 8.3% in June to 13.5% in November 2015.

A contraction in the volume of foreign trade and the slowdown in economic activity led to lower-than-expected state budget revenue. A consolidation of expenditure helped to keep the state budget deficit in an amount equal to 1% of GDP in Q1-Q3 2015. However, the budget deficit for 2015 is forecast to amount to 3.9% of GDP. This is primarily due to the continued decline in public revenue from taxes and other payments as a consequence of the decrease in the volume of foreign trade. Moldova’s public debt may grow in 2015 to 50% of GDP compared with 30% of GDP in 2014 in connection with financial assistance provided to three major banks (Banca Sociala, Banca de Economii and Unibank).

There was a progressive loss in trust in the banking sector amid the weakening of the national currency and the continuing problems of the insolvent banks. The deposit base (adjusted to exchange rate changes) shrank by 11% in Q1-Q3 2015, which led to a 3.3% decrease in the aggregate loan portfolio. The National Bank revoked the licenses of the three problem banks and started a liquidation procedure for them. After deposits started being transferred from the three banks to other banks, the deposit base of the banking sector grew by 0.6% in October. This circumstance, coupled with the high interest rate on the National Bank’s loans, led to a fall in lending. Banks’ aggregate loan portfolio decreased by 0.6% in October to 39.6 billion lei at the end of the month. The share of nonperforming loans in the banking sector (excluding the three problem banks) was 9.8% at the end of October, while the capital adequacy ratio stood at 24.7%, up from 14.9% in July.
Moldova

Figure 7.1. **GDP and output**: GDP growth and output change by sectors, (in %, year-on-year)

Source: the National Bureau of Statistics of Moldova

Figure 7.2. **Foreign trade**: exports, imports, current account (left scale, in billions of US dollars), real effective exchange rate – REER (right scale, index – Q2 2009 = 100)

Source: national agencies

Figure 7.3. **Government sector**: state budget (in % of GDP)

Source: national agencies

Figure 7.4. **Monetary sector**: the central bank’s rate (in %), the CPI growth (in %, year-on-year), M2 growth (in %, year-on-year)

Source: national agencies

Figure 7.5. **Economic growth**: GDP growth and forecasts by national and international institutions (in %)

Source: estimates and forecasts by national agencies, the World Bank, the EBRD, the IMF

Figure 7.6. **Savings and investments**: (in % of GDP): balance of private investment and savings (Sp-Ip), state budget (Sg-Ig), current account balance (X-M)

Source: estimates and forecasts by national agencies and the IMF
Russia: slowdown in GDP fall, new wave of ruble’s depreciation amid fall in oil prices

Russia’s GDP fell by 4.1% year-on-year in Q3 2015 compared with a 4.6% year-on-year fall in Q2 2015. The decrease in the magnitude of the GDP fall reflected both the low base effect of 2014 and an improvement in the quarterly dynamics. Although the estimates by different agencies of the quarter-on-quarter growth of real GDP differ from each other, it is not unlikely that this growth was above zero. The decrease of the depth of Russia’s GDP fall was due to an insignificant increase in the extent of the fall in fixed capital investment, as well as to a rise in net exports. Investment fell by 6.8% year-on-year in Q3 2015 after a 6.7% year-on-year fall in Q2 2015. Net exports increased due to both a fall in imports and a rise in the real volume of exports, primarily exports of crude oil and metals. Given the dynamics of retail trade, the annual rate of the decline in private consumption continued to increase under the influence of higher inflation and a fall in real wages.

The fall in world oil prices in Q3 2015 led to further depreciation of the Russian ruble. It fell from 55.5 against the dollar in Q2 2015 to 66.2 at the end of Q3 2015. As a consequence, after seasonal fluctuations in July and August, consumer prices rose by 0.6% in September and further to 0.7-0.8% in each of October and November. The annual inflation rate remained at 15.6 to 15.8% throughout Q3 2015. The inflation rate had continued to be at levels above the central bank’s target. This forced the Bank of Russia to slow down the process of reducing its key lending rate, and then stop it after the rate was lowered to 11.0% in early August. The growth rates of money aggregates rose slightly, primarily due to the low base effect of 2014. The annual growth rate of M2 money supply increased from 6.8% in June to 7.5% in September.

Due to seasonal factors, the current account surplus in the balance of payments decreased in Q3 2015 to an estimated $5.4 billion. In terms of percentage of GDP, the surplus was significantly higher at 1.8% than that in Q3 2014 (1.2%). According to data from the central bank, the growth rate of the net outflow of capital taken abroad by companies and banks moved into negative territory for the first time in five years, amounting to $5.3 billion (1.7% of GDP). Under these circumstances, the international reserves of the central bank grew by $9.7 billion (3.2% of GDP).

The deficits of the federal and the consolidated budget decreased from 2.3% and 2.6% of GDP, respectively, in Q1-Q2 2015 to 1.2% and 1.4% in Q1-Q3 2015. This decrease was attributable to both the seasonal dynamics of the budgets and the relatively large share of funds spent in Q1 2015 for financing anti-crisis measures.

The growth of bank lending stabilized in Q3 2015 despite fluctuations caused by the impact of the dynamics of the ruble’s exchange rate on the price of foreign-currency loans. The annual growth rate of banks’ net claims on the other sectors of the economy rose insignificantly from 14.2% at the end of June to 14.4% at the end of September. The capital adequacy ratio increased slightly to 13% from 12.9% at the end of Q2 2015, while the share of problem assets remained unchanged at 8.2%.
Outlook

Russia: looser monetary policy, slow GDP growth

According to data available as of early December, Russia’s economy had zero or low positive seasonally adjusted month-on-month growth rates throughout most of Q3-Q4 2015. These dynamics were determined, on the one hand, by: a recovery in finished product inventories that had sharply decreased earlier; the stabilization of fixed capital investment; and the rise in net exports. On the other hand, they were determined by a fall in household consumption, which resumed in Q4 amid the depreciation of the national currency and the consequent high rate of inflation. One can expect that the annual rate of the fall in real GDP will be lower in Q4 2015 than in Q2 and Q3, and Russia’s GDP will fall by 3.7 to 3.9% in 2015.

A condition for the balance of the effects of the above-mentioned factors to change for the better is the stabilization of the prices of Russia’s major export items. This would ensure the relative stability of the ruble. Under such circumstances, the central bank would be able to resume lowering its key lending rate. This would have a positive effect on lending by speeding up recovery in investment demand and supporting demand from consumers. We expect that the situation will gradually move into this scenario in 2016, which would lead to a GDP growth of zero to 1%. The GDP growth rate may remain negative if the restoration of a balance in the oil market takes more time than we expect. Nonetheless, trends in Q3-Q4 2015 give grounds to believe that the extent of the economy’s adaptation to low oil prices and fluctuations in the ruble’s exchange rate has become sufficient for the deterioration of the terms of trade not to force the central bank to resort to tightening its monetary policy while trying to shore up the ruble amid the fall in oil prices. This makes the negative impact of the fall in oil prices on real economic activity limited, although sufficient for preventing it from recovering.

The dynamics of inflation in Q3-Q4 2015 indicate that the rise in prices is gradually slowing down as the effects fade away of currency depreciation, and shocks from the supply side such as the current restrictions on imports from Turkey. In this regard, it is probable that inflation will slow to less than 0.5% a month in Q1 2016. The annual inflation rate should fall, largely due to the disappearance of the statistical effect of a price hike that happened a year ago, and return to levels below 10% by the spring.

The deficits in the federal and the consolidated budget will amount to 2.5 to 3% of GDP in 2015 and may decrease in 2016 if the economy recovers. A number of developments, including a planned recapitalization of Vneshekonombank, may have a negative effect on these indicators.

The current account surplus in the balance of payments will decrease in 2016 in both nominal terms and terms of percentage of GDP amid a significant fall in capital outflows. The latter will happen partly because expenses for servicing the external public demand will be lower than those in 2015. The current account will remain in surplus irrespective of the dynamics of oil prices amid a flexible exchange rate policy. This policy will cause the overall balance of the balance of payments to be close to zero. It is most likely that the central bank will not be able to resume foreign currency purchases for replenishing its international reserves throughout most of 2016.

The economy has zero or low positive month-on-month growth rates throughout most of Q3-Q4 2015

A condition for sustainable growth to resume is the stabilization of the prices of Russia’s exports, which would prompt the central bank to resume lowering its lending rate

The GDP growth rate may remain negative if the restoration of a balance in the oil market takes more time than we expect

Inflation will probably slow to less than 0.5% a month in Q1 2016 as the effects of currency depreciation fade away

The budget deficit may decrease if the economy recovers

The current account surplus will decrease in 2016 amid a significant fall in capital outflows
Russia

Figure 8.1. **GDP and output**: GDP growth and output change by sectors, (in %, year-on-year)

Source: the Federal State Statistics Service

Figure 8.2. **Foreign trade**: exports, imports, current account (left scale, in billions of US dollars), real effective exchange rate – REER (right scale, index – Q2 2009 = 100)

Source: national agencies

Figure 8.3. **Government sector**: consolidated and federal budget (in % of GDP)

Source: national agencies

Figure 8.4. **Monetary sector**: the central bank’s rate (in %), the CPI growth (in %, year-on-year), M2 growth (in %, year-on-year)

Source: national agencies, IMF (IFS)

Figure 8.5. **Economic growth**: GDP growth and forecasts by national and international institutions (in %)

Source: estimates and forecasts by national agencies, the EBD, the World Bank, the EBRD, the IMF

Figure 8.6. **Savings and investments**: (in % of GDP): balance of private investment and savings (Sp-Ip), state budget (Sg-Ig), current account balance (X-M)

Source: estimates and forecasts by national agencies, the IMF and the EBD
Tajikistan: downturn in services sector amid high growth rate of industrial output

Tajikistan’s economic growth slowed to 6.4% year-on-year in Q3 2015 compared with a year-on-year growth of 7.5% in Q2 2015 and a growth of 7.3% in Q3 2014. The slowdown was mainly due to a downturn in the service-providing sector of the economy, with the volume of paid services falling by 13.8% year-on-year and retail sales increasing by 0.1%. The Russian central bank’s data for cash remittances abroad reveal the cause of the sharp deterioration in the services sector: the volume of net cash remittances from Russia to Tajikistan in Q1-Q3 2015 was 66.6% lower than in Q1-Q3 2014. Nonetheless, Tajikistan’s GDP growth rate remained at quite a high level. Major support for economic growth came from the construction and industrial sectors. The rise in industrial output was supported by high growth rates in: the metallurgical industry; the production of non-metal mineral products; and the textile industry. The high growth rate in the construction sector was attributable to public investment in infrastructure, communications, and power generation and supply.

Foreign trade indicators for Q3 2015 show a significant decrease in the trade deficit (-36.9% compared with Q3 2014). This was due to: a slight fall in exports (exports of mineral products decreased by 13%, while exports of non-precious metals and products from non-precious metals dropped by 24.1%); and a considerable decrease in imports amid significant fluctuations in the national currency’s exchange rate and weak domestic and external demand. In particular, imports of petroleum products and vehicles fell by 25.6% and 52.1%, respectively.

The state budget had a surplus equal to 0.5% in Q3 2015 and a surplus equal to 2.3% of GDP in Q1-Q3 2015 compared with a surplus amounting to 1.9% of GDP in Q1-Q3 2014. Inflow of revenue from non-tax payments and other sources caused overall revenue to increase to 32.2% of GDP. This was despite a decrease in the volume of customs revenue amid the fall in imports. Public investment in the power generation industry and the transport sector continued to be one of the priorities of government expenditure and will remain as such in the years to come.

Annual inflation slowed to 4.9% at the end of Q3 2015. This was to a certain extent due to a fall in the world prices of petroleum products and food, as well as the National Bank’s foreign exchange interventions. Due to fluctuations in the national currency’s exchange rate and increased depreciation expectations, the rise in prices accelerated and so did the pace of dollarization of commercial banks’ deposit base. Under these circumstances, the annual growth rate of bank lending in the national currency fell to 10.4% from 27.5% at the end of 2014, whereas the annual growth rate of lending in foreign currency remained flat throughout 2015 at 30 to 33%. In addition, statistical data indicated deterioration in the quality of commercial banks’ aggregate loan portfolio. In particular, the share of classified loans was 28.5% of the total volume as of October 1, 2015, up from 22.6% at the start of 2015.
Outlook
Tajikistan: slowdown in GDP growth in 2015, possible growth acceleration in medium term

Statistical data for October and November 2015 suggest a continued slowdown in Tajikistan’s economic growth. Due to the decrease in the inflow of migrant remittances, there was a continued fall in the services sector, while the growth rate of retail sales remained at a low level. Public investment in power generation infrastructure, which fueled growth in the construction and industrial sectors, remained key drivers of GDP growth. Volatility in the international financial markets intensified again in Q3 2015. It increased the probability of: an extension of the downward trend in the inflow of cash remittances from abroad; a contraction in domestic demand; and increased pressure in the domestic currency exchange market. The current consensus forecast predicts a GDP growth of 4.6% for 2015 and acceleration to 5% for the medium term.

The acceleration of annual inflation to 5.3% in November 2015 was attributable to both a seasonal rise in food prices and the impact of exchange rate fluctuations on the price of non-food consumer goods. The annual inflation rate may rise to 5.5-6% before the end of 2015. This is a consequence of: some loosening of monetary policy (the annual growth rate of the money supply was 9.1% in October compared with 8% at the end of Q3 2015); and the weakening of the somoni. In mid-December the exchange rate of the somoni against the dollar was 32.6% lower than in January 2015. The National Bank decided to close down all exchange bureaus in the country due to the strong volatility of the exchange rate. Apart from that, amid the high degree of dollarization of the economy and a decrease in the international reserves, the regulator received an additional source for replenishing the reserves by signing a swap agreement with China in the amount of about $470 million.

Foreign trade indicators for Q1-Q4 2015 show a year-on-year decrease of 23.3% in the trade deficit. Although the world prices of cotton and aluminum tend to fall, it is these primary commodities that account for the bulk of export proceeds. Due to the contraction in domestic consumer demand, imports continue to decrease. Despite the fall in the inflow of migrant remittances, the current account deficit will remain moderate for the whole of 2015.

Given the fall in state budget revenue amid the decreased imports, the government decided to cut some non-priority expenditure. It is quite probable that the state budget will be balanced in 2015. The government expects the state budget to increase by 3.3 billion somoni in 2016. The increase would include 1.5 billion somoni in external loans and grants, which would be used for social and economic projects according to officials. The increase in external borrowing may lead to a rise in the country’s external public debt, which amounted to 19.5% of GDP as of the end of June 2015. Tajikistan’s main creditors include the Export-Import Bank of China, the World Bank, the Asian Development Bank, and the Islamic Development Bank.
**Figure 9.1. GDP and output**: GDP growth and output change by sectors, (in %, year-on-year)

Source: the Agency on Statistics under President of Tajikistan

**Figure 9.2. Foreign trade**: exports, imports, current account (left scale, in billions of US dollars), real effective exchange rate – REER (right scale, index – Q2 2009 = 100)

Source: national agencies

**Figure 9.3. Government sector**: state budget (in % of GDP)

Source: national agencies

**Figure 9.4. Monetary sector**: the central bank’s rate (in %), the CPI growth (in %, year-on-year), M2 growth (in %, year-on-year)

Source: national agencies, IMF (IFS)

**Figure 9.5. Economic growth**: GDP growth and forecasts by national and international institutions (in %)

Source: estimates and forecasts by national agencies, the EBD, the ABD, World Bank, the EBRD

**Figure 9.6. Savings and investments**: (in % of GDP): balance of private investment and savings (Sp-Ip), state budget (Sg-Ig), current account balance (X-M)

Source: estimates and forecasts by national agencies, the IMF and the EBD
Trends

Turkmenistan and Uzbekistan: continued slowdown in GDP growth amid a fall in foreign trade

GDP growth in Turkmenistan and Uzbekistan slowed down in Q3 2015 amid: a continued downward trend in the world prices of energy resources and other primary commodities; the recession in Russia; the slowdown in economic growth in China; the low growth rate in Europe; and the complicated geopolitical situation. However, the year-on-year GDP growth rates in Turkmenistan and Uzbekistan remained high compared with other countries in the region. They stood at 7.5% and 8%, respectively, in Q1-Q3 after growth rates of 8.7% and 8.1% in Q1-Q2 2015.

The slowdown in economic growth in Turkmenistan was largely due to a significant slowdown in the rise in industrial output probably because of a decrease in gas exports to Russia. Output increased by 3.5% year-on-year in Q1-Q3 2015 after a 6.2% year-on-year increase in Q1-Q2 2015. In Uzbekistan, the slowdown was less significant but was also due solely to the dynamics in the industrial sector.

Growth in other economic sectors in the two countries remained at high levels and even accelerated. The continued high GDP growth rates were attributable to the governments’ active stimulus efforts within the framework of programs aimed at the modernization and diversification of the national economies. The leadership of the two countries actively uses accumulated and current export earnings for stimulating both capital investment within the framework of industrial policies and domestic consumption within the framework of social policy. Industrial policies include: the expansion of energy export routes; the diversification of exports; the expansion of domestic industrial production; and import substitution industrialization. Social policy aims, among other things, to create new jobs and increase household income.

The downward trend in the foreign trade of Turkmenistan and Uzbekistan apparently accelerated in Q3 2015 amid: additional deterioration in the terms of trade (natural gas decreased in price by 29.2%; gold fell by 12.3%; and cotton fell by 6.3%); and heightened pressure on the nominal exchange rates of the national currencies. The dynamics of exports appear to be the main cause of the fall in foreign trade as imports were supported by domestic consumption, which were actively stimulated by authorities despite intensive import substitution efforts. Nonetheless, the two countries should have continued to run a trade surplus (+$218 million for Uzbekistan). It should be noted that statistical data about foreign trade and the balance of payments were not published in open access in Turkmenistan and Uzbekistan, which considerably complicates analysis.

Despite the diminishing foreign trade, there was a continued balance in public finances due to: the continued high growth rates; the rise in household income; measures to expand the tax base; the use of resources from reserve funds; and the consolidation of public expenditure, which proved to be below the projected levels in both countries. In Turkmenistan, nominal state budget revenue decreased by 1.5% year-on-year in Q1-Q3 2015, while expenditure rose by a moderate 1.3%. In Uzbekistan, the state budget had a surplus equal to 0.1% of GDP, largely due to the expansion of the tax base amid a reduction in the tax burden. According to official statisticians, inflation remained low.
Trends and outlook

Ukraine: decrease in magnitude of GDP fall amid declining intensity of internal armed conflict

Ukraine’s GDP fell by 7.2% year-on-year in Q3 2015. The magnitude of the GDP fall thus decreased significantly compared with Q1 and Q2 2015, when GDP fell by 17.2% and 14.6%, respectively. The improvement was primarily due to the low base effect of Q3 2014, although Q3 2015 saw a moderate rise of 0.5% in seasonally adjusted GDP compared with Q2 2015. This became the first quarter-on-quarter GDP growth in two years. A slow recovery in economic activity began in Ukraine amid the fading armed conflict in the east of the country. Under these circumstances, the year-on-year rate of the fall in industrial output decreased to 5.1% in September from 18.1% in June and 21.1% in March. There was also a decrease in the extent of the fall in retail sales (22.3% in Q1-Q3 2015 against 24.6% in Q1-Q2 2015) and construction output (15.2% in Q1-Q3 2015 against 20.6% in Q1-Q2 2015).

Inflation continued to slow down throughout Q3 2015. The month-on-month growth rate of the consumer price index moved into negative territory in July and August amid weak demand and a seasonal rise in the supply of agricultural produce. The annual inflation rate remained high at 51.9% in September after 57.5% in June, reflecting price hikes in 2014 and early 2015. The stability of the hryvnia’s exchange rate, whose fluctuations continued to be limited by the National Bank and the regulator’s tight monetary policy, had a deterrent effect on the rise in prices in the country. The M2 money supply decreased by 5.6% year-on-year in September.

The high inflation rate in 2014 and early 2015 helped public revenue grow faster than expenditure. In Q1-Q3 2015 the consolidated budget had a surplus equal to 5.9% of GDP, down from 7.6% in Q1-Q3 2014.

Due to a massive consolidation of domestic demand, there was a continued positive shift in the state of the balance of payments. The current account balance, which moved into positive territory in Q2 2015, remained there, with the surplus in Q3 2015 amounting to $77 million (0.3% of GDP). Ukraine had a current account deficit equal to 0.4% of GDP in Q1-Q3 2015 compared with a deficit equal to 3.1% of GDP in Q1-Q3 2014. Funds received from international organizations and foreign states helped the National Bank increase its international reserves from $10.3 billion to $12.8 billion, or from 2.1 to 2.9 months’ worth of imports. A loan tranche received from the International Monetary Fund in August accounted for about half of the increase. The aggregate external debt and external public debt of the country continued to grow, amounting to $127.5 billion and $37 billion (135% and 39% of GDP) at the end of Q3 2015, respectively. In December the parliament adopted budget estimates for 2016, which ensured an extension of the IMF’s support program for Ukraine. Meanwhile, the government’s efforts to have the external debt restructured, which had earlier resulted in deals with some of the creditors, reached a deadlock regarding a $3-billion debt owed to the Russian government. A formal default on this debt is expected to come at the end of 2015.
Ukraine

Figure 10.1. **GDP and output**: GDP growth and output change by sectors, (in %, year-on-year)

Source: the State Statistics Service of Ukraine

Figure 10.2. **Foreign trade**: exports, imports, current account (left scale, in billions of US dollars), real effective exchange rate – REER (right scale, index – Q2 2009 = 100)

Source: national agencies

Figure 10.3. **Government sector**: state budget (in % of GDP)

Source: national agencies

Figure 10.4. **Monetary sector**: the left scale - the central bank’s rate (in %) and CPI growth (in %, year-on-year); the right scale - M2 growth (in %, year-on-year)

Source: national agencies

Figure 10.5. **Economic growth**: GDP growth and forecasts by national and international institutions (in %)

Source: estimates and forecasts by national agencies, the World Bank, the EBRD, the IMF

Figure 10.6. **Savings and investments**: (in % of GDP): balance of private investment and savings (Sp-Ip), state budget (Sg-Ig), current account balance (X-M)

Source: estimates and forecasts by national agencies and the IMF