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Trends in 2014:
- **The world economy** – diverging policies of leading central banks
- **United States** – strong growth in Q3-Q4 2014, a likelihood of tighter monetary policy in 2015
- **Europe** – a gradual recovery in economic growth in the Eurozone, growing expectations of a further easing by the European Central Bank
- **Asia** – a gradual slowdown in GDP growth in China, an end of Japan’s recession caused by an increase in the sales tax rate
- **The CIS**:
  1) A further fall in GDP growth rates amid a fall in oil prices, sanctions against Russia
  2) A strong depreciation of the ruble, the danger of a deterioration of the state of the balances of payments
  3) A deepening downturn in the economy of Ukraine

Outlook and risks:
- **The world economy**: A return to more even and steady growth
- **Commodity markets**: A negative impact of the strengthening dollar on prices, a partial recovery in the oil market
- **The CIS**: The continuing risk of an escalation of the Ukraine conflict, the consolidation of state budgets and external balances, an adjustment of monetary and exchange rate policies

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Vladimir Yasinskiy, Managing Director for Analytics

*The report was prepared by the country analysis unit:*
Konstantin Fedorov (fks@eabr.org) – Macroeconomics of the Region, Belarus, Russia, Ukraine
Arman Ahunbaev (ama@eabr.org) – Azerbaijan, Armenia, Kazakhstan
Aigul Berdiguilova (bar@eabr.org) – Tajikistan, Turkmenistan, Uzbekistan
Elvira Kurmanalieva (kes@eabr.org) – Kyrgyzstan, Moldova
Macroeconomics of the region

The economic growth figures of most of the CIS countries deteriorated again in Q4 2014. This resulted in a decrease in the region’s annual GDP growth rate from 2% in 2013 to 0.6% in 2014. Unlike in Q3 2014, the negative dynamics affected to one extent or another all three major groups of countries: the oil and gas exporters, the labor exporters, and the countries with a diversified structure of exports. Nonetheless, GDP growth remained in positive territory until the end of 2014 in all CIS countries except Ukraine.

The slowdown in GDP growth in the CIS countries was attributable to the deterioration of the external economic situation, which became stronger in the final months of 2014. Q4 2014 saw a continued fall in energy prices, which decreased by 39.5% year-on-year in December compared with an 11.4% year-on-year fall in September (see Figure 1.2), according to World Bank data. Unlike in Q3 2014, there was a fall in prices of metals and agricultural produce, although these commodities decreased in price to a lesser extent than energy goods. Metal prices fell by an average of 11.2% year-on-year in December, whereas prices of agricultural products decreased by 6.5% (also see Figure 1.2). The CIS countries experienced a decrease in the physical volume of exports of certain commodities. In particular, Russia’s natural gas exports fell significantly due to the expected decline in contract gas prices for European customers, which follow global oil prices with a lag, as well as under the influence of the Ukraine developments. The physical volume of oil exports from Kazakhstan and Azerbaijan decreased simultaneously under the influence of technological processes at oil fields.

The negative changes in the external environment had a different direct impact on the economies of the group of oil and gas exporting countries (Azerbaijan, Kazakhstan, Russia and Turkmenistan). The fall in oil prices and a further toughening of international sanctions predictably had the most significant impact on economic growth in Russia. This caused a fall in the GDP growth rate of this group of countries from 1.1% year-on-year in Q3 to 0.7% in Q4 2014. At the same time Kazakhstan and Azerbaijan had an increase in the year-on-year GDP growth rate in Q4 2014 due to an acceleration of growth in retail trade and the construction sector.

Figure 1.1. World industrial production and trade

Figure 1.2. Terms of trade: international commodities’ and food prices

Source: CPB World Trade Monitor, World Bank

Source: Word Bank
The group of labor exporting countries (Armenia, Kyrgyzstan, Moldova and Tajikistan) experienced a fall in the year-on-year GDP growth rate to 4.4% in Q4 2014 from 5% in Q3 2014. The group’s economies were affected by the consequences of the slowdown in economic growth in Russia and the depreciation of the ruble, which led to: a fall in the volume of cash remittances sent home by migrant workers; a decrease in foreign trade; and a fall in investment from Russia. In addition, the central banks of most of the labor exporting countries had to tighten their monetary policies to maintain the exchange rates of the national currencies, which are more rigidly pegged to the US dollar than the Russian currency. This also had a negative effect on their GDP growth. Under these circumstances, a slowdown in economic growth took place in almost all labor exporting countries. It was strongest in Armenia, where the annual GDP growth rate fell from 5.3% in Q3 to 2.9% in Q4 2014. The only exception was Kyrgyzstan, whose annual GDP growth accelerated to 5.4% from 0.8% in Q3 2014 amid increased activity in the construction and trade sectors.

The annual GDP fall in the group of countries with a diversified structure of exports reached 10.4% compared with a 3.1% year-on-year fall in Q3 2014. The dramatic fall in the aggregate GDP of this country group was almost entirely due to a disastrous slump in economic activity in Ukraine resulting from the armed conflict. The annual GDP growth rate of Belarus remained in positive territory in Q4 2014 and only fell moderately compared with Q3 2014.

In Q4 2014 the state of the public finances in the CIS countries began to deteriorate compared with Q4 2013 due to: the slowdown in economic activity; the decrease in cash remittances from abroad; the negative impact of the external economic environment; and a fall in foreign trade. The CIS countries had an average consolidated budget deficit of 10.6% of GDP in Q4 2014 compared with a deficit of 8.4% of GDP in Q4 2013. The loss of certain fiscal revenue was partially offset by: the improvement that could be seen in Q1-Q3 2014; the consolidation of expenditure; and an increase in the efficiency of tax administration. This held back the deterioration in public finances in 2014. The depreciation of the Russian ruble in 2014 supported the level of consolidated budget revenue. This had a favorable effect on the aggregate budget balance for 2014 due to the great significance of Russia for the region’s economies. The surplus amounted to 2.6% of GDP in 2014 compared with a deficit of 1.6% of GDP in 2013.

Figure 1.3. Balance of payments: current account balances’ components and foreign exchange reserves

Source: national agencies

Figure 1.4. CIS countries’ GDP growth (in %, year-on-year)

Source: national agencies
The region’s aggregate balance of payments deteriorated due to the unfavorable dynamics of the financial account balance. Statistical data for the 2014 balance of payments have not yet been published in many CIS countries. Available data suggest that the region’s aggregate balance of payments should have deteriorated. This deterioration was largely due to: the unfavorable dynamics of the financial account balance resulting from the complicated geopolitical situation in the region; the strengthening of the US dollar in international markets against the currencies of developing countries; a fall in the inflows of foreign investment in all CIS countries; and the growing volume of capital outflows. It is remarkable that the foreign trade balance in the region improved in general in 2014 despite the fall in energy and metal prices in Q4 2014. The main reasons for the improvement were: the depreciation of the national currencies in many CIS countries; and the consolidation of domestic demand, which led to a more substantial fall in imports than in exports in almost all countries.

Inflation rates in the region continued to rise. In Q4 2014, the average year-on-year rise in consumer prices in the CIS countries was 10.3% compared with 8.3% in Q3 2014. An acceleration of inflation took place in each of the major CIS country groups. Inflation rose from 7.5% to 9.2% for the oil and gas exporters, primarily due to an acceleration of inflation in Russia amid a sharp currency depreciation. Inflation in Kazakhstan remained at a relatively high level. In Azerbaijan, which had not yet devalued its currency, there was a slowdown in inflation due to a fall in energy and food prices under the influence of external factors. A significant acceleration of inflation – from 16.3% to 21% – occurred in the countries with a diversified structure of exports. Amid some slowdown in inflation in Belarus, this acceleration was primarily due to a strong acceleration of inflation in Ukraine, which followed the depreciation of the hryvnia. In the labor exporting countries, inflation accelerated again, from 4.5% to 5.6%. The fall in the value of the national currency in these highly dollarized economies is rather quickly translated to domestic prices.

The major 2014 trends that had an impact on the CIS economies were: the significant strengthening of the US dollar against local currencies amid differences in the dynamics of the monetary policies of major central banks; and a fall in prices of major primary commodities, primarily crude oil. The consequences will probably continue to determine the economic situation in the region throughout the remaining part of 2015. There are signs of the restoration of evenness in economic growth in the world. This is primarily due to acceleration of growth in the Eurozone and a slowdown in the United States. The signs could be seen in the first months of 2015; and suggest that the dynamics of major currencies against each other will be more moderate in Q2 and Q3 2015 than in the period between mid-2014 and the spring of 2015. In addition, one can expect a partial recovery of prices of primary commodities, including crude oil, after a fall in Q3-Q4 2014 and in early 2015.
This will be favored by a rebalancing of the oil market as a result of a slowdown in growth or a fall in the production of unconventional oil, especially in the United States. These factors will contribute to the stabilization of the Russian ruble and facilitate the adjustment of macroeconomic policy to the changing external conditions for the governments of other CIS countries.

Most of the CIS countries currently take steps in their exchange rate and monetary policies and/or budgetary policy to maintain the sustainability of the balance of payments. This is against the backdrop of: a fall in export revenue; a decrease in foreign investment and the volume of cash remittances from migrant workers; and a decrease in the competitiveness of local manufacturers due to the weakening ruble. In a number of countries, these measures include a revision of the national currency’s pegs and its one-time or gradual devaluation. For instance, Belarus switched from its currency’s de-facto peg to the US dollar to a peg to a basket of three currencies with a 40% share of the Russian ruble. Simultaneously, there is a consolidation of public finances in the region’s countries. Some countries have formally revised their 2015 budgets to provide for a reduction in expenditure and other countries cut public spending without formally revising the budget.

Our GDP growth forecasts for the CIS economies are based on the assumption that there will be a moderate recovery in oil prices throughout 2015. We expect that the average price of Brent crude will be $60 per barrel this year and will increase further in 2016, and that the Western sanctions against Russia in the context of the Ukraine crisis will not be tightened, although they will continue to be in force until at least the end of 2015. Given these circumstances, one can expect that the region’s GDP will fall by 2.4% in 2015 but resume growing in 2016, increasing by about 1.8%. The stabilizing effect on the Russian economy from a flexible exchange rate policy that was timely adopted by the country’s authorities will become a factor that will make the probable fall in the region’s economy significantly smaller than that seen in 2009. The prevention of an increase in external imbalances in CIS countries other than Russia requires consistent and concerted measures in the fields of monetary and budgetary policies. If such measures are not taken, the risk of a loss of external sustainability by the region's economies will remain substantial in the next few years.
Trends and outlook

Azerbaijan: deterioration in external economic conditions leads to GDP growth slowdown, and decrease in export and fiscal revenue

In Q4 2014 Azerbaijan’s GDP growth accelerated to about 3.7% year-on-year, which resulted in 2.8% growth in 2014 compared with 5.8% growth in 2013. The slowdown in the country’s economic growth was due to a 0.7% year-on-year fall in industrial output, which accounted for 41.5% of GDP. Output in the oil and gas sector decreased by 2.4% year-on-year due to a 2.8% fall in oil production – a key factor for the national economy – which declined as an indirect consequence of the fall in oil prices in international markets. This fall offset growth in the non-oil sector of the economy, which was supported by strong investment activity, including public investment activity, and increases in individuals’ disposable income and bank lending. Output in the non-oil branch of the industrial sector rose by 6.9% in 2014, while the construction sector rose by 11.8%. Retail trade rose by 10% and the information and communications sector rose by 15.1%, whereas agricultural output fell by 2.6%.

Data for the balance of payments in 2014 are still unavailable, but given the fall in oil prices and the contraction of oil production, the state of the balance of payments apparently deteriorated in Q4 2014. The country’s trade surplus decreased to 16.7% of GDP in 2014 from 18% of GDP in 2013. This was due to a combination of a 16.8% year-on-year fall in exports in Q4 2014 and a sharp 50% rise in imports, which was caused by the real strengthening of the manat supported by forex interventions.

The state of the current account balance should also have deteriorated. As a result, the international reserves shrank by $1.5 billion in Q4 to amount to $14.7 billion (24.9% of GDP) at the end of 2014.

The state of the public finances deteriorated in Q4 2014 due to a decrease in oil revenue, but remained sustainable in general. The state budget had a surplus equal to 0.5% of GDP in 2014 compared with 0.6% of GDP in 2013. The aggregate surplus of the state budget and the State Oil Fund amounted to 5.7% of GDP, up from 3.7% of GDP in 2013. An improvement was achieved in the state of the consolidated budget due to a reduction in public spending and a decrease in transfers from the State Oil Fund to the state budget. The assets of the State Oil Fund slightly decreased in nominal terms and increased in terms of percentage of GDP to amount to $37.1 billion, or 49.1% of GDP.

Under the influence of a fall in food and energy prices, inflation slowed down in the country throughout Q4 2014. As a result, the annual growth rate of the consumer price index fell to 1.4% in December, with food prices having an annual growth rate of 1% and the prices of non-food consumer goods and services rising by 3.2% and 0.3%, respectively. The deceleration of inflation was due to a slowdown in the growth of the money supply under the influence of the negative dynamics of oil prices and the de-facto fixed exchange rate of the national currency against the US dollar. In particular, M2 grew by only 6% in 2014 compared with a growth of 19% in 2013.

The slowdown in money growth in the economy still had a limited impact on lending activity. The annual growth rate of bank lending was 21.1% in December 2014.
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 national agencies and the IMF
Trends

Armenia: slowdown in GDP growth due to fall in remittances and low investment activity

In Q4 2014 Armenia’s annual GDP growth slowed to 2.6%, which led to a GDP growth rate of 3.4% in 2014 compared with 3.5% in 2013. The main factor behind the slowdown was a decrease in the volume of cash remittances from abroad, which fell by 10.1% in 2014 as a result of the ruble’s depreciation and the recession in Russia. Amid declining investment activity, which fell by 1.7% in Q1-Q3 2014, and a downturn in the construction sector, whose output fell by 3.3% in 2014, lower consumption affected retail sales, which rose by only 0.8%. Declining external demand and a fall in prices of major export commodities had a negative impact on the mining industry (-5.8%). The continued positive GDP growth was largely due to good figures for agricultural output (+7.8%), the manufacturing industry (+7.7%) and the services sector.

The good performance of the agricultural sector and the agricultural product processing industry had a favorable effect on the export of finished food products. Coupled with good figures for exports of precious stones and precious metals, this growth offset a fall in the export of mineral products. As a result, Armenia’s foreign trade deficit decreased to 26.6% of GDP in 2014 from 28.7% of GDP in 2013. The growth rate of exports remained at 2.7%, while imports rose by only 0.4%.

Nonetheless, the state of the current account balance considerably deteriorated due to the decrease in the volume of cash remittances from abroad. The deficit was 10.8% of GDP in Q1-Q3 2014 compared with a deficit of 8.7% of GDP in Q1-Q3 2013.

Coupled with the possible contraction of the financial account surplus, especially in the context of the sharp depreciation of the ruble, this led to a balance of payments deficit. This is evidenced by the depreciation of the dram in November-December 2014 and the steady contraction of the gross international reserves. They decreased by $764 million (34.1%) in 2014 to $1,489.3 million as of the end of 2014.

The state of the public finances deteriorated in Q4 2014. The state budget moved to a deficit position as a result of an acceleration of the growth of expenditure at the end of 2014 amid a moderate rise in revenue. Nonetheless, the state of the public finances remained balanced, with the state budget deficit standing at an estimated 0.7% of GDP in 2014 compared with 1% of GDP in 2013. Despite the slowdown in economic growth, the government continued to pursue a conservative fiscal policy and, in general, managed to meet its targets for tax revenue.

The nominal depreciation of the dram contributed to an acceleration of inflation in Q4 2014. Nonetheless, the annual inflation rate was 4.6% in December 2014 against 5.6% in December 2013. Inflationary pressure was held back by the fall in energy prices and tighter monetary policy. The annual growth rate of bank lending rose to 21.9%, but given the high degree of dollarization of the loan portfolio (66.5%), this acceleration was attributable to a revaluation of the volume of lending after the currency devaluation. The profitability indicators of the banking sector deteriorated, which directly led to an increase in the share of non-performing loans in the economy to 7% from 4.5% at the end of 2013.
Outlook

Armenia: limited GDP growth, conservative fiscal policy, moderate inflation

The Indicator of Economic Activity (IEA) fell to 1.3% in annual terms in January 2015. There was an increased negative effect on domestic demand resulting from the devaluation of the dram, and a fall in cash remittances from Russia, which decreased by 52.9% year-on-year in January. International organizations and the central bank have revised downward their GDP growth forecasts to between 0.4% and 2%. The major external factors for this revision are: the current slowdown and the deteriorating outlook for Russia, which is the main source of remittances and the main trading partner and investor; international metal prices; and continued weak growth in Europe. The negative external environment will limit the positive effect of Armenia’s integration into the Eurasian Economic Union. Apart from the existing structural and social problems, domestic factors that have a negative effect on economic activity include limited opportunities to use instruments of fiscal and monetary policies. According to the consensus forecast of international organizations, Armenia’s GDP will grow by 1.6% in 2015, but this forecast appears too optimistic and one should probably expect a more considerable slowdown.

The volume of migrant workers’ remittances will decrease as a result of the depreciation of the ruble and the contraction of domestic demand. This will have a negative effect not only on economic activity but also on the balance of payments and the public finances in 2015. The negative impact of the fall in migrant remittances on the current account balance will be only partially offset by a simultaneous decrease in imports. The import decrease will be due to a fall in the purchasing capacity of households and a fall in prices of imported primary commodities. As a result, the state of the current account balance may deteriorate. Moreover, amid the expected limited inflow of foreign direct and portfolio investment, the problem of foreign currency liquidity will persist. The overall deterioration of the balance of payments will put pressure on the dram throughout 2015.

The slowdown in GDP growth, the fall in foreign trade and decreased customs duty rates will have a negative impact on the state budget. This will contribute to the expansion of the budget deficit. Revenue losses will be attributable to the possible slowdown in the growth of tax and customs revenue, while expenditure is expected to meet the projected levels. The state of the public finances in Armenia may significantly deteriorate unless the medium-term expenditure parameters are revised and additional measures are taken to consolidate the budget. The expansion of the state budget deficit and the current account deficit amid a diminishing financial account surplus will increase both the financial gap and the need for external sources of finance.

Despite the currency devaluation in late 2014, the inflation rate will probably remain moderate in 2015. It was 5.4% in annual terms as of the end of February 2015, and should continue to be within the central bank’s target band of 2.5 to 5.5%. The negative effect of the devaluation on inflation amid a cautious monetary policy will be offset by: the effect of recession in 2015; the fall in world food and petroleum prices; the decrease in the price of Russian natural gas for Armenia in connection with its accession to the EAEU; and the impact of the ruble’s depreciation on goods imported into Armenia from Russia.

A fall in remittances from Russia and the devaluation of the dram affect domestic demand, the balance of payments and the public finances

The negative impact of the fall in migrant remittances on the current account balance will be only partially offset by a simultaneous decrease in imports

The inflation rate will probably remain moderate in 2015
Armenia

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

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)

Source: national agencies, IMF

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

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)

Source: national agencies

**Figure 3.5. 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 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)

Source: estimates and forecasts by national agencies and the IMF
Belarus: slowdown in consumption growth, fall in investment, sharp deterioration in balance of payments at year’s end

Belarusian economic growth slowed to about 2% year-on-year in Q4 2014 following an annual growth rate of 2.1% in Q3 2014. GDP grew by 1.6% in 2014 against a growth of 0.9% in 2013. The greatest contribution to economic growth was made by the extractive industry (increased by 41.9%), and retail trade (increased by 7.7%). The most significant negative impact on GDP growth came from the construction sector (decreased by 4.5%). A positive contribution to GDP growth was made by: net exports due to both a rise in exports in real terms and a decrease in imports; and household consumption. The rise in private consumption slowed down throughout 2014 as the growth rate of average real pay became negative. Fixed capital investment decreased by 8.5% in 2014.

Inflation substantially slowed down throughout Q4 2014. The annual growth rate of the consumer price index fell from 20.1% in September to 16.2% in December. Major factors behind the slowdown included: the strengthening of the national currency in terms of the nominal effective exchange rate amid the sharp depreciation of the Russian ruble; and the contraction of the money supply amid forex interventions by the National Bank in support of the Belarusian ruble. The annual growth rate of M2 fell from 24.6% in September to 14.5% in December. The M2 supply began to decrease month-on-month in October.

The strengthening of the national currency led to a considerable deterioration of the balance of payments in Q4 2014. In Q1-Q3 2014, the export surplus exceeded the respective figure for Q1-Q3 2013. There was a surplus of $74.9 million in Q3 2014 against a deficit of $967.6 million in Q3 2013. In Q4 2014 there was a deficit of $1.1 billion, slightly down from a deficit of $1.3 billion in Q4 2013. The trade deficit in December 2014 exceeded the deficit in December 2013: $868.6 million against $512.9 million. The National Bank’s support of the Belarusian ruble required massive forex interventions. This caused the international reserves to decrease from $6 billion at the end of September to $5.1 billion at the end of 2014, or from 1.6 months’ to 1.3 months’ worth of imports. The government also had to introduce special measures in December, such as the imposition of a 30% fee on foreign exchange purchases in view of increased demand for foreign currency.

The fiscal situation, on the contrary, significantly improved in Q4 2014. The consolidated budget had a surplus equal to 1% of GDP in 2014 compared with a surplus amounting to only 0.2% of GDP in 2013.

The annual growth rate of bank lending did not reflect the slowdown in the growth of money supply; it was 22.4% at the end of Q4 2014 compared with 18.5% at the end of Q3 2014. This rise was attributable to massive lending to industrial companies amid a continued slowdown in the growth of lending to individuals.
Outlook

Belarus: recession amid tighter monetary and budgetary policies, risk of deterioration in balance of payments

In late 2014 and early 2015, the Belarusian economy experienced the influence of negative external factors, such as a slowdown in economic activity in Russia and the weakening of the Russian ruble. Due to a deterioration of the balance of payments and the contraction of the international reserves, the National Bank changed its policy regarding the national currency’s exchange rate. The Belarusian rouble’s de-facto flexible peg to the US dollar was abandoned and, after a quick currency devaluation at the beginning of January, the National Bank switched to pegging the rouble to a basket of three currencies – the US dollar, the euro and the Russian rouble – simultaneously raising the refinancing rate from 20% to 25%. The exchange rate of the rouble against the basket of currencies has been close to a fixed one since mid-January 2015. The currency devaluation and the transition to the new exchange rate policy helped reduce pressure on the National Bank’s reserves. Nonetheless, the de-facto fixed peg of the rouble to the basket of currencies is ensured by a relatively tight monetary policy. Under these circumstances, there has been no firm return to positive money supply growth rates since the contraction at the end of 2014.

The measures taken in late 2014 to tighten budgetary policy continued in early 2015. They helped ensure a consolidated budget surplus equal to 12.5% of GDP in January 2014 compared with a surplus of 9.3% of GDP in January 2013. The improvement of the state of the budget was achieved due to, in particular, efforts to reduce spending.

From our point of view, the changes in macroeconomic policy that took place in late 2014 and early 2015 helped increase the degree of sustainability of the Belarusian economy. Nonetheless, continued tight control over the exchange rate of the rouble against the basket of currencies is ensured by a relatively tight monetary policy. Under these circumstances, there has been no firm return to positive money supply growth rates since the contraction at the end of 2014.

The National Bank changes its exchange rate policy due to a deterioration of the balance of payments and the contraction of the international reserves.

The exchange rate of the Belarusian rouble against the currency basket has been close to a fixed one since mid-January.

The measures taken in late 2014 to tighten budgetary policy continued in early 2015.

Changes to macroeconomic policy help increase the degree of sustainability of the national economy.

GDP may decrease by 1 to 2% in real terms in 2015.

Given the existing circumstances, the country’s GDP may decrease by 1 to 2% in real terms in 2015. This will be attributable to: the negative contribution of net exports to the overall GDP growth amid the high value of the Belarusian rouble as compared with the Russian rouble; and decreased consumer and investment activity amid relatively tight monetary and budgetary policies. If the National Bank manages to avoid a substantial depreciation of the national currency throughout the remaining part of 2015, then one can expect that inflation in the country will slow to between 9% and 12% at the end of 2015 amid the above-described conditions.
Belarus

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

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)

Source: national agencies, IMF (IFS)

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

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)

Source: national agencies, IMF (IFS)

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

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)

Source: estimates and forecasts by national agencies, the IMF and the EBD
Kazakhstan: anti-crisis measures lead to improvement in macroeconomic figures

Despite some acceleration in Q4 2014, Kazakhstan’s GDP growth slowed to 4.3% in 2014 from 6% in 2013. This slowdown was attributable to external factors such as: the fall in world oil prices; the slowdown in economic growth in Russia and China; the low growth in Europe; and the complicated geopolitical situation in the region. Domestic factors behind the slowdown included: a decrease in consumer activity following the February currency devaluation and the introduction of regulatory measures to curb consumer lending; a decrease in oil production, which fell by 2.2% in 2014; problems in the agricultural sector; and the tightening of monetary policy. Despite its weakening, domestic demand was rather robust due to fiscal stimulus measures, which supported household income and investment activity (+3.9% in 2014). Net exports made a positive contribution because imports fell to a greater extent than exports. While growth in the industrial and agricultural sectors slowed to 0.2% and 0.8% in 2014, respectively, the main drivers of the country’s economic growth were: retail trade (+12.1%), transportation (+7%), communications (+8.5%) and construction (+4.2%).

The balance of payments improved in 2014, which, coupled with the tightening of monetary policy and forex interventions, helped keep the tenge stable. This was despite the deterioration of the external market situation and a decrease in exports, which fell by 7.6% in annual terms. In Q1-Q3 2014, the balance of payments moved from a deficit to a surplus (+$3 billion), while the current account surplus increased to $5.2 billion (3.7% of GDP) compared with a surplus equal to 0.6% of GDP in Q1-Q3 2013. Factors behind the improvement of the balance of payments included: the consolidation of domestic demand and the contraction of imports (-15.6%) following the currency devaluation; and the use of external corporate loans and government loans in October and November 2014 including an issue of $3.5 billion worth of Eurobonds. As a result, the National Bank’s gold and foreign exchange reserves grew by $4.2 billion (17%) in 2014 to a total of $28.9 billion. The international reserves, which also include the resources of the National Fund of Kazakhstan, amounted to $102.4 billion (48.3% of GDP).

The state of the public finances worsened in 2014. The state budget deficit increased to 2.9% of GDP from 2.1% of GDP in 2013. On the one hand, this was attributable to the high growth rate of public expenditure, which increased by 18.7% compared with a rise of 5% in 2013. On the other hand, the revenue contraction resulting from the slowdown in economic activity and the fall in oil prices appears to have not been fully made up for by an increase in the volume of additional transfers from the National Fund of Kazakhstan.

Annual inflation accelerated to 7.4% in December 2014, whereas the target band for 2014 was 6 to 8%. The acceleration of inflation was attributable to the transfer of the rise in import prices following the January currency devaluation to the consumer basket. Lower inflation and producer price deflation (-1.6% in annual terms) resulted from: the tightening of monetary policy with an 8.2% decrease in the M2 supply and a sharp rise in interest rates at the end of 2014; the contraction of exports; weaker domestic demand; administrative control over prices; and declining import prices.

Annual growth in bank lending slowed to 7.2% in 2014, which did not prevent an improvement in banks’ profitability indicators. In particular, the average ROA (return on assets) ratio was 1.6%, while the ROE (return on equity) ratio was 13.2%. Due to regulatory measures, the share of nonperforming loans diminished from 31.2% in 2013 to 23.5% in December 2014.
Outlook

Kazakhstan: slowdown in GDP growth amid decrease in export and fiscal revenue

As Kazakhstan’s economic growth relies heavily on primary commodities and oil, this revenue is critically important for the entire economy. The fall in oil and metal prices, coupled with a decrease in oil production expected in 2015, will determine: the degree of the slowdown in GDP growth; the extent of the deterioration in the balance of payments and the state budget balance; and also the dynamics of monetary balances throughout 2015. In this context, fiscal stimuli measures taken within the framework of a new economic policy, Nurly Zhol, and government programs that are already being implemented will start performing an anti-crisis function.

Signs of a slowdown in economic activity could already be seen in January and February 2015, when the annual growth rate of the short-term Indicator of Economic Activity was only 2.5%. Investment activity and consumption continued to fall as a result of the unfavorable external environment, high devaluation expectations, and a number of seasonal factors. The government’s GDP growth forecasts of 1.5% for 2015 and 2.3% for 2016 appear to be reasonable. These forecasts match updated forecasts from international organizations, which predict an oil price of $50 to $60 per barrel of Brent. These forecasts are characterized by heightened uncertainty regarding oil prices. Additional factors increasing this uncertainty include: the Ukraine crisis; the intensity of confrontation between Russia and the West; the depth of the economic slump in Russia; the degree of the slowdown in China; and the extent of acceleration of global economic growth.

Given the fall in oil and metal prices, the slowdown in economic growth will be accompanied by: a significant decrease in exports; a current account deficit, which the National Bank expects to amount to between 3% and 4% of GDP; and an extra decrease in the inflow of direct investment in view of the complicated geopolitical environment.

The deterioration of the balance of payments and the possible contraction of the international reserves are associated with continued pressure on the tenge. This is further increased by the strengthening of the US dollar in world markets throughout 2015, as well as by the current strengthening of the real effective exchange rate. During 2015, the balance of payments will be influenced by: the direction of the dynamics of oil prices; the government’s efforts to receive new external loans; the intensity of using transfers from the National Fund of Kazakhstan; and the government’s decisiveness in the de-dollarization of the economy.

The key parameters of the 2015 state budget estimates have been revised on the basis of the assumption that oil prices will average $50 per barrel. The government expects a 1.2% decrease in revenue, despite a significant increase in transfers from the National Fund of Kazakhstan. The budget revision has resulted in a substantial cut in expenditure. Public spending is expected to grow by only 0.9%, which will restrain its stimulus effect. The projected budget deficit has been increased to 3% of GDP. Amid the slowdown in economic growth and the deterioration of the foreign trade balance, the growth rate of the money supply should remain at a low level. This will limit the influence of monetary factors on inflation. The fall in world energy and food prices will also curb inflation, which should remain within the target range of 6 to 8%, even in the event of a correction in the exchange rate.

The government’s GDP growth forecasts of 1.5% for 2015 and 2.3% for 2016 appear to be reasonable, but the reliability of the forecasts is undermined by heightened uncertainty regarding oil prices.

A slowdown in economic growth will be accompanied by a significant decrease in exports, a current account deficit, and a fall in direct investment.

The key parameters of the 2015 state budget estimates are revised on the basis of the assumption that oil prices will average $50 per barrel.

The projected budget deficit is increased to 3% of GDP.

Inflation should remain within the target band of 6 to 8%.
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
Kyrgyzstan: growth slowdown, currency depreciation and inflation

Amid the depreciation of the Russian ruble in Q4 2014, the US dollar-denominated volume of migrant remittances from abroad decreased by 22.5% year-on-year in the period, and by 5% on average in 2014 compared with 2013. Migrant remittances play a key role in maintaining purchasing power for internal demand, including demand for imported goods. Therefore the fall in their volume led to a weakening of the som and a decrease in the volume of imports. The foreign trade deficit diminished across almost all categories of goods. The current account balance had a deficit of 22% of GDP in 2014 compared with a deficit of 25% of GDP in 2013. A decrease in foreign direct investment was offset by an inflow of debt capital. The resulting balance of payments deficit was 3.1% of GDP.

In the sphere of public finance, additional non-tax revenues helped to increase state budget revenue to 30% of GDP, up from 29% of GDP in 2013. The government curbed the rise in current expenditure, whereas capital expenditure exceeded the level of 2013 (9.6% of GDP against 8.2% of GDP in 2013). The state budget had a deficit equal to 4.4% of GDP compared with a deficit equal to 6.6% of GDP in 2013. The increase in capital expenditure, which is financed with external loans, affected the situation with regard to the external public debt, which reached 48.2% of GDP at the end of 2014 compared with 43.8% of GDP at the end of 2013.

Amid the balance of payments deficit and the rise in prices, the National Bank raised its base lending rate and made forex interventions. The money supply shrank by 9% in 2014. Forex interventions remained the main instrument of regulating liquidity given the high degree of dollarization of the economy and the low efficiency of the interest rate channel of monetary policy transmission mechanism. The National Bank’s international reserves were still sufficient to finance four months’ worth of imports. The annual growth rate of consumer prices was higher than the National Bank’s projected level in December and moderately decreased by February 2015.

Amid the contraction of the money supply in the economy, the high annual growth rate of banks’ lending (45.9% in December 2014) reflected an increase in the value of foreign-currency-denominated loans. Actually, there was a slowdown in the growth of both som loans and foreign-currency loans, whose terms were adjusted to the change in the exchange rate. Despite a slowdown in the growth of the deposit base and an increase in the volume of "loans under supervision", the performance indicators of the banking sector remained at an acceptable level. The profitability indicators improved in 2014 and the share of nonperforming (classified) loans decreased to 4.5% of the total volume of the banks’ loan portfolio.

The situation in the national economy in 2014 was characterized by a high growth rate in the construction sector and a revival in consumer spending. The high growth rate of construction reflected government investment in energy infrastructure and private investment in housing construction. The rise in retail sales, which accelerated considerably in Q4 2014, was the consumers’ response to the acceleration of the national currency’s depreciation. There was negative growth in the industrial sector, in which the gold mining industry accounts for a large share, because gold production declined at the Kumtor mine.

GDP grows by 3.6% in 2014

Annual inflation accelerates to 10.5% in December 2014

The state budget deficit decreases to 4.4% of GDP in 2014 from 6.6% in 2013

The volume of migrant remittances decreases by 5% in 2014

The banking sector’s efficiency indicators remain beyond critical values
Outlook

Kyrgyzstan: accession to EAEU, parliamentary elections, fall in remittances

Kyrgyzstan’s economy will face three difficult challenges in 2015. Firstly, the crisis in Russia continues to affect the volume of migrant workers’ remittances. Secondly, the country’s accession to the EAEU implies changes in the structure of foreign trade and employment. Thirdly, the forthcoming parliamentary elections may have an impact on the economic situation and the internal political situation. The current median forecast for GDP growth is 1.8%. The economy is expected to receive less support from the services and construction sectors due to a further decrease in the volume of cash remittances from abroad. Moreover, the volume of gold production at the Kumtor mine is expected to be lower this year than in 2014. Data for the first two months of 2015 show a slowdown in the rise in wholesale and retail trade and in the construction sector’s output.

The volume of migrant remittances, which were about 25% of GDP in 2010-2014, may continue to decline in 2015. This will lead to a further decrease in domestic demand. Apart from migrant remittances, the economy is supported by external loans, the re-export of textile industry products and gold exports. With the country becoming a member of the EAEU in the short term, it is likely that unemployment will rise and the balance of payments will deteriorate due to a decline in re-export activity. At the same time an inflow of Russian investment will help to offset the negative effects caused by the process of adaptation to the new external economic conditions. In the medium term, Kyrgyzstan will get the opportunity to enhance its production potential and the competitiveness of its economy through broader access to the EAEU market. This will be the consequence of the harmonization of technical requirements and the elimination of non-trade barriers within the union.

The current account deficit may increase in 2015 in terms of percentage of GDP. This would aggravate the unsustainability of the balance of payments and cause the need to finance it. The external imbalance amid limited opportunities to service the growing external debt will also require a correction of the exchange rate. The correction will be made gradually because the authorities pursue a cautious policy regarding forex interventions with a view to preserving the sustainability of the banking system. Inflation slowed down a little in February and early March but may accelerate in the remaining part of 2015 under the influence of the weakening of the som.

The unemployment and poverty rates may rise in 2015. A fall in the dollar equivalent of wages in Russia will prompt migrant workers to return home. In addition, there will be a loss of jobs in the re-export sector. In the run-up to the country’s parliamentary elections, this may have an impact on the government’s decisions on increasing social security spending and put upward pressure on public expenditure. According to the adopted budget estimates, the 2015 state budget is to have a deficit equal to 3.3% of GDP. However, changes in the external and domestic economic conditions predetermine the likelihood of multiple revisions of fiscal targets and projections.
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: currency depreciation amid problems in banking sector, decrease in exports and remittances**

Q4 2014 was characterized by a sharp decrease in export revenue and cash remittances from abroad amid a deterioration of the economic situation of neighboring countries. Moldova's exports fell by 12.4% and migrant remittances decreased by 20% year-on-year in Q4 2014. The fall in the inflow of foreign currency put pressure on the exchange rate of the leu, which lost 7.2% of its value in Q4 2014. There was still more pressure on the leu in January 2015, when the volume of cash remittances from abroad diminished by 25% year-on-year and the leu weakened by 14.9%.

In the period between November 28, 2014 and March 6, 2015, the National Bank’s foreign exchange reserves shrank by 24.9% to an amount sufficient to cover 3.5 months’ worth of imports. Apart from massive forex interventions, the National Bank raised its base lending rate by 10 percentage points within two months, from 3.5% to 13.5%. The depreciation of the leu increased inflationary pressure. The annual inflation rate rose from 4.7% in December 2014 to 6.5% in February 2015, thereby reaching the upper boundary of the National Bank’s target band of 3.5 to 6.5%. The National Bank revised upwards its forecast for the average inflation rate in 2015 from 4.6% to 5.8%.

At the end of 2014, amid increased currency risks, the National Bank started trying to isolate two problem banks, Banca de Economii and Banca Sociala, from the banking sector. It introduced a special administration regime for the banks and took measures to increase depositors’ confidence and trust. This helped to prevent a massive outflow of deposits from the banks. In the period between late November 2014 and January 31, 2015, the volume of legal entities’ and individuals’ bank deposits in lei decreased by 6% and the share of nonperforming assets in the banking sector remained unchanged. However, the share of such assets grew to 35.7% at Banca Sociala and to 72.2% at Banca de Economii. The capital adequacy ratio continued to fall, decreasing to only 12.68% from 19.9% in June 2014 and 23% at the end of 2013, whereas the minimum required level is 16%.

The state budget had a deficit of 1.9 billion lei, or 1.7% of GDP, in 2014. Public revenue increased across all types of tax revenue in 2014 compared with 2013, amounting to 38% of GDP against 36.7% of GDP in 2013. This made it possible to increase expenditure to 39.8% of GDP from 38.5% of GDP in 2013. The bulk of expenditure traditionally came in Q4. Apart from external factors, the increase in the money supply in lei through state budget operations put additional pressure on the currency exchange market.

GDP growth amounts to 4.6% in 2014 and may slow to 2.8% in 2015.
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: major ruble depreciation, acceleration of inflation, further slowdown in GDP growth

Russia’s annual growth rate fell further in Q4 2014 due to a significant decrease in oil prices and the impact of the Western sanctions against the country over the increasingly serious Ukraine crisis. GDP grew by about 0.2% year-on-year in Q4 2014, and by 0.6% in 2014 compared with 1.3% in 2013. On the demand side, major factors behind the fall in the GDP growth rate were: a slowdown in the growth of household consumption to 1.9% in 2014 from 5% in 2013; and a 2.5% decrease in fixed capital investment after a 1.4% rise in 2013. Net exports, on the contrary, had a positive effect on the overall economic growth amid a 2% fall in exports and a 6.8% decrease in imports. On the supply side, the most significant negative contribution was made by the construction sector, whose output fell by 5.2%.

Under the influence of the fall in oil prices and new sanctions, the ruble’s annual depreciation against the US dollar reached 71% by the end of 2014. As a result, the annual growth rate of consumer prices rose to 11.4% in December from 6.5% in December 2013. The Bank of Russia tightened its monetary policy, raising the base rate from 10.5% to 17% in mid-December, compared with 5.5% in December 2013. The annual growth rate of M2 was 2.2% in December against 14.6% in December 2013. Despite the slowdown in growth, the money supply did not contract and still had positive month-on-month growth rates, with seasonal factors taken into account.

Despite a fall in export revenue, the current account surplus amounted to an estimated $56.7 billion (3% of GDP) in 2014, up from $34.1 billion (1.6% of GDP) in 2013. There was also a year-on-year increase in the current account surplus in Q4 2014 of $10.5 billion (2.7% of GDP) against $8 billion (1.4% of GDP) in Q4 2013. Nonetheless, amid a substantial capital outflow and massive forex interventions by the central bank, which sought to slow the weakening of the ruble, the overall balance of the balance of payments was negative at $107.5 billion (5.7% of GDP) in 2014 and at $64.2 billion (16.4% of GDP) in Q4 2014.

There was a substantial improvement in the state of the public finances throughout the greater part of 2014. However this improvement eventually faded away: the federal budget and the consolidated budget had deficits of 333.8 billion and 844.9 billion rubles (0.5% and 1.2% of GDP), respectively, against deficits equal to 0.5% and 1.2% of GDP in 2013. The deterioration in the state of the public finances in late 2014 was due to the government’s move to sharply beef up the capital of the Deposit Insurance Agency by issuing a large amount of federal bonds and handing them over to the Agency.

Despite the significant increase in the central bank’s base rate, the annual growth rate of banks’ net claims on the other sectors of the economy rose to 22.1% in December 2014 from 18.9% in December 2013. This acceleration reflected the rise in the ruble value of dollar loans amid the ruble’s depreciation. The capital adequacy ratio decreased to 12.5% at the end of 2014 from 13.5% at the end of 2013. The share of problem loans amounted to 6.7% at the end of 2014 compared with 6% at the end of 2013.
Russia: limited fall in GDP amid contraction of domestic demand and rise in net exports

The negatives factors that influenced the economic situation in Russia in 2014 primarily included the fall in world oil prices and restrictions on access to international capital markets for banks and companies. They will continue to affect the country’s GDP growth throughout 2015 and as a result: fixed capital investment and household consumption will show negative growth rates amid a decline in company profits; the cost of refinancing loans will grow; and real income and wages will fall due to the acceleration of inflation and the relatively low projected degree of indexation of public employees’ pay to inflation in 2015. Meanwhile, the flexible exchange rate policy pursued by the central bank ensures a rapid adaptation of the economy to the unfavourable external conditions. Manifestations of this adaptation can be seen in: the rise in net exports; the lack of monetary and lending contraction; and the slow rise in unemployment. These factors will support economic growth in the country. Given the dynamics of the Russian economy since Q4 2014, one can expect that the country will experience a negative GDP growth rate, but this fall will be within 1 to 3%. This is significantly below the 2009 level when Russia’s GDP dropped by 7.8%. In this respect the economic results for 2015 will be largely determined by the dynamics of world oil prices and developments regarding the Western sanctions in the remaining part of the year.

After acceleration resulting from the rouble’s weakening in Q3-Q4 2014, inflation began to show signs of slowdown in late February and early March 2015. One can expect a decline in the annual growth rate of the consumer price index in the remaining part of 2015 amid low economic activity and a slow rise in the money supply. Consumer prices will probably rise by 11 to 14% in 2015. This slowdown would correspond to the central bank’s official inflation target of 4% (+/-1.5%) for 2017. It is most likely that inflation will not slow down faster because the central bank will probably reduce its base lending rate in order to avoid excessive risks for economic growth.

In early 2015, the government substantially revised the budget estimates for the year and redistributed expenditure in favor of a program of “anti-crisis measures.” This included measures aimed at the recapitalization of banks, support for systemically important companies, and the social protection of the population. The government expects that the 2015 budget will have a deficit equal to 3.8% of GDP. The budget deficit may be smaller if the dynamics of major economic indicators, such as oil prices and GDP growth, are more favorable than those predicted when the budget estimates were made. If there are no additional unexpected negative changes in the Russian economy’s external environment, the balance of payments will probably be close to zero. This is because the central bank officially switched to a floating exchange rate regime in December 2014. The financial account deficit may decrease amid a decline in the outflow of capital following a surge in 2014, whereas the current account surplus may diminish amid a partial recovery in imports.
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: impact of fall in remittances offset by high investment activity

Tajikistan’s annual GDP growth slowed down in Q4 2014 to 6.1% compared with 7.3% in Q3 2014. The country’s GDP grew by 6.7% in 2014 compared with a growth of 7.4% in 2013. A weakening of domestic demand resulted from an 8.3% decrease in the inflow of cash remittances from abroad. This was caused by the deterioration of the economic situation in Russia and the ruble’s sharp depreciation. Household real disposable income increased by only 4.3% compared with a rise of 10.5% in 2013. The rise in retail trade slowed to 6.6% from 19.3% in 2013 and the growth rate of the services sector fell to 1.0% from 9.7%. Economic growth was also held back by a decline in crop production. As a result, agricultural output increased by only 4.5% following a rise of 7.6% in 2013. Weaker consumer demand and the slowdown in the agricultural sector were offset by a rise in investment activity (+25.3% in 2014 against +17.2% in 2013) and an acceleration of growth in the industrial sector (+5.1%), due to a high growth rate in the extractive industry (+24.1%).

The country’s foreign trade deficit expanded to $3.3 billion in 2014 from $3.1 billion in 2013. There was an unexpected recovery in exports with a 3.6% increase in 2014 against a decrease of 28.1% in 2013. This was due to a rise in exports of precious stones and metals (7.4pp contribution) and an increase in exports of other goods (12.3pp contribution). The import of alumina fell due to a drop in aluminum production. This led to a slowdown in the overall rise in imports. As the inflow of remittances also decreased, the current account balance should have continued to deteriorate in Q4 2014, which would affect the figure for the entire year.

In 2014 the state budget had a small surplus of 0.3% of GDP. The growth rates of both revenue (+20.3% in 2013) and expenditure (+26.0% in 2013) fell to 15%. An improvement in tax administration contributed to the growth of public revenue to a certain degree. The increase in expenditure in the public sector was due primarily to a rise in social and education spending, and secondly to a rise in spending on the public administration sector.

Annual inflation accelerated to an average 6.8% in Q4 2014 and stood at 7.4% in December. Amid a fall in energy prices and tighter monetary conditions, the acceleration of inflation was attributable to the depreciation of the somoni against the US dollar and a decrease in the domestic food supply. While the rise in prices of services and non-food consumer goods slowed down, food prices were the main driver of inflation. This could be linked to the decrease in agricultural output and the depreciation of the national currency. In response to increased volatility in the domestic exchange market, the National Bank made forex interventions, which led to a decline in the annual growth rate of the money supply from 13.3% in Q3 2014 to 4.6% in Q4 2014 and to 3.5% in December. The annual growth of bank lending slowed to 16.9% from 29.9% in Q1-Q3 2014, while the share of overdue loans grew to 13.6% from 6.1% at the end of 2013. Banks’ average ROA (return on assets) was minus 4.4% at the end of 2014.
Outlook

**Tajikistan: external imbalances may build up in the economy in 2015**

The slowdown in economic growth will continue in 2015. According to different estimates, the expected recession in Russia will increase the decline in the inflow of remittances from 30 to 40%. Apart from this, the weakness of the banking sector, including the growing share of classified loans, may also have a negative effect on the general level of economic activity. On the other hand, foreign investment channeled into the creation of new businesses and infrastructure will support economic growth. According to a median consensus forecast, the country’s GDP will grow by 4.2%, whereas the government expects a growth rate of 7.2%. However, these forecasts may be revised downwards in the event of a greater decrease in the volume of remittances from abroad and a fall in foreign investment.

The recovery in exports in 2014 was short-term and most likely will not continue in 2015. This is due to the deterioration of price competitiveness. The impact of the sharp weakening of the Russian ruble on Tajikistan’s national currency is still limited. The nominal depreciation of the somoni against the US dollar was only 11.2% in 2014, while the somoni strengthened in real terms by 3.1% against the currencies of the main trading partners. The narrow export base will continue to have a negative effect on the overall volume of exports under the conditions of the expected 13% fall in world cotton prices and the insignificant 3% rise in world aluminum prices. The import of consumer goods may also fall due to the significant decrease in the inflow of migrant remittances. The current account balance is expected to continue to deteriorate.

The expected contraction of export revenue and the volume of cash remittances from abroad may put additional pressure on the domestic exchange market. Meanwhile, the National Bank’s international reserves shrank substantially in 2014 to only 1.3 months’ worth of imports. The small foreign exchange reserves pose risks for the monetary authorities with regard to keeping the somoni’s rate stable and, consequently, with regard to curbing inflation. This is because the rise in import prices may complicate the task of keeping the inflation rate within the target rate.

Tajikistan had a balanced state budget in 2014. The government’s budget estimates for 2015 are conservative and envisage a limited increase in expenditure and a deficit equal to 0.5% of GDP. Nonetheless, the deterioration of the external economic environment will also have consequences for the public finances. Given the fact that imports account for almost 60% of tax revenue, there are risks of failure to meet the revenue projection for 2015. This may, in its turn, increase the need for external finance or require revising the projected public sector spending.

Consensus forecast predicts GDP to grow by 4.2% in 2015 and 5.1% in 2016, whereas the government expects growth rates of 7.2% and 7.4%, respectively.

External imbalances may impede economic growth in the long term...

...pose challenge for the monetary authorities...

...and expose to additional risk fiscal sector
Tajikistan

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 and outlook

### Turkmenistan: slowdown in growth of exports offset by investment activity

Turkmenistan’s economy continued to grow strongly in 2014. GDP increased by 10.3% compared with a growth of 10.2% in 2013. Despite the fall in energy prices and signs of recession in Russia, Turkmenistan’s economic growth was ensured by almost all sectors of the economy, with investment and natural gas production being the main drivers. Relatively high growth rates were recorded in power generation (8.8%) and natural gas production (11.1%). Retail sales rose by 17.0% amid a 10.1% increase in average monthly pay. The transport sector showed a growth of 6.4%, while the agricultural sector’s growth rate remained modest at 3.2%. Investment increased by 6.1%, accounting for 40.0 to 45.0% of GDP. Chinese capital investment played an increasingly important role in the economy. The government’s gas export diversification program, aimed at reducing Russia’s share and increasing China’s share, helped alleviate the impact of the economic crisis in Russia on the national economy of Turkmenistan. Nonetheless, given the expected slowdown in economic growth in China, external demand for Turkmen natural gas may have a downward trend. This will become a serious problem if plans to supply gas to Europe fail to come to fruition.

Turkmenistan’s foreign trade increased by 4.2% in 2014. The trend of slowdown in export growth continued into Q4 2014. As a result, the annual growth rate of exports was 4.9% in 2014 compared with 5.6% in Q1-Q3 2014 and 8.3% in Q1-Q2 2014. The rise in imports also slowed in Q4 2014, which resulted in an annual growth rate of 3.4% in 2014 against 4.4% in Q1-Q3 2014. As a result, Turkmenistan is expected to continue to have a trade surplus, but the current account balance may have a slight deficit. Given the slowdown in the growth of foreign trade, which was partly due to the fall in world oil and gas prices, the government carried out a one-time currency devaluation in January 2015, reducing the value of the manat by 19.0%.

The fiscal situation slightly improved in Q4 2014. However the state budget surplus decreased in 2014 to an estimated 0.1% of GDP. The rise in public revenue accelerated in Q4 2014, which resulted in an increase of 8.0% in 2014 following a 6.0% year-on-year increase in Q1-Q3 2014. Meanwhile the growth of public expenditure slowed down, which led to an increase of 11.9% in 2014 following a 16.1% increase in Q1-Q3 2014.

Inflation accelerated in Q4 2014. According to official statistical data, the all-item consumer price index rose to 4.4% against December 2013, compared with 1.7% in September 2014 against December 2013. Independent experts say that in January 2015 the government raised utility prices 15-fold and increased retail gasoline prices by 60%. Given these factors, coupled with the devaluation of the manat, one can expect an acceleration of inflation. The government has raised salaries, pensions and social benefits to compensate the population for the rise in prices, but this move will most likely become an additional burden on the state budget rather than help achieve the objective of increasing the population’s real income.

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**GDP continues to grow strongly in 2014, increasing by 10.3%**

**Natural gas production rises by 11.1%**

**The growth of foreign trade slows from 5.1% in Q1-Q3 2014 to 4.2% in 2014 as a whole**

**The state budget continues to have a surplus**

**The all-item consumer price index rises to 4.4% year-on-year in December 2014**
Figure 10.1. **GDP**: GDP growth (in %, year-on-year)

- 2010: 9.2%
- 2011: 14.7%
- 2012: 11.1%
- 2013: 10.2%
- 2014: 10.3%

Source: national agencies

Figure 10.2. **Foreign trade**: exports, imports (in billions of US dollars)

Source: ADB

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

- 2010: 2.0%
- 2011: 3.5%
- 2012: 5.7%
- 2013: 1.1%
- 2014: 0.1%

Source: national agencies

Figure 10.4. **Monetary sector**: the left scale - CPI growth (in %, year-on-year); the right scale - M2 growth (in %, year-on-year)

Source: national agencies and the ADB

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

Source: estimates and forecasts by the ABD, 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 the IMF
**Trends and outlook**

**Uzbekistan: steady GDP growth despite deterioration in external economic situation**

The closed economic system of Uzbekistan helped the country resist the increased volatility in the world and regional currency exchange and financial markets, as well as to resist a slowdown in the growth of external demand. Uzbekistan’s economic growth rate remained almost unchanged in 2014, standing at 8.1% compared with 8.0% in 2013. Industrial output rose by 8.3%, while agricultural output increased by 6.9%. The construction sector had a growth rate of 10.9%, while the volume of retail sales and services rose by 14.3% and 15.7%, respectively. Investment in the national economy increased by 9.6% in 2014, accounting for almost one-fourth of GDP. Foreign investment and loans accounted for more than 20% of the total volume of capital investment, with foreign direct investment making up 75%. The implementation of government programs aimed at replacing imports with domestic products and increasing the share of local components in finished goods will help maintain Uzbekistan’s economic growth at a high level in 2015. However, external economic factors are expected to affect growth. As a result, Uzbekistan’s economic growth will slow to 7.4% according to the consensus forecast.

The weak economic growth in Russia and the fall in world prices for the country’s major export commodities (natural gas, gold and cotton) have already started to affect Uzbekistan’s foreign trade. The trade surplus shrank to $180 billion in 2014, although the country had a surplus of $900 million in Q1-Q3 2014. There was also a 10% decrease in the volume of cash remittances from Russia. However, the rise in foreign investment not only offset the decrease in the country’s foreign exchange earnings on the current account of the balance of payments, but also made it possible to replenish the gold and foreign exchange reserves, which grew by $1.6 billion. Despite the deterioration of the external economic conditions, Uzbekistan is expected to be one of the few countries in the region to have a current account surplus in 2015.

The state budget had a surplus equal to 0.2% of GDP in 2014 compared with 0.3% of GDP in 2013. There was a slowdown in the growth of public revenue due to a decline in economic activity. There was also a fall in the growth rate of expenditure, which was attributable to a slowdown in the rise in social and public administration spending. The government’s action program provides for some tax relief and therefore public revenue is expected to decrease in 2015.

According to official data, the consumer price index rose by 6.1% year-on-year in December 2014. At the same time international organizations’ estimates put the real inflation rate at 11 to 12%. Moreover, a monetary overhang is being created through the government’s effort to keep the Uzbek sum’s exchange rate from falling against the US dollar. Since the beginning of 2015, the market value of the dollar has risen by about 20%, whereas government data indicate that the sum has depreciated by slightly more than 1%. Given the fact that there has been a ban on the sale of foreign cash to individuals since February 1, 2013, and that the international reserves have increased, the central bank is expected to be able to use administrative levers to control the depreciation of the national currency for the longest time in the region.

**The economic growth rate remains almost unchanged in 2014 at 8.1% against 8.0% in 2013**

**The trade surplus decreases to $180 billion in 2014**

**The state budget has a surplus equal to 0.2% of GDP**

**According to official data, the consumer price index rises by 6.1% year-on-year in December 2014, but international organizations put the actual inflation rate at 11 to 12%**
Uzbekistan

Figure 9.1. **GDP and output**: GDP growth and output change by sectors, (in %, year-on-year)

Source: national agencies

Figure 11.2. **Foreign trade**: exports, imports (in billions of US dollars)

Source: national agencies, ADB

Figure 11.3. **Government sector**: state budget (in % of GDP)

Source: national agencies

Figure 11.4. **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 and the ADB

Figure 11.5. **Economic growth**: GDP growth and forecasts by national and international institutions (in %)

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

Figure 11.6. **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
The magnitude of the fall in Ukraine’s GDP continued to increase in Q4 2014, reaching 14.8% compared with 1.2% in Q1, 4.5% in Q2, 5.4% in Q3, which resulted in a fall of 6.8% in 2014. Double-digit decreases were recorded in most economic sectors, including the extractive industry, the manufacturing sector, retail trade and construction. The few exceptions that showed positive growth rates in Q4 2014 included health services and public administration services. There were double-digit falls in household consumption, fixed capital investment, exports and imports, although the greater decrease in imports ensured net exports’ positive contribution to GDP growth.

The drop in consumer and investment demand led to a considerable decrease in the current account deficit of the balance of payments in both Q4 2014 and 2014 as a whole. According to preliminary data, the deficit amounted to $1.6 billion in Q4 2014 and $5.3 billion in 2014 compared with $5 billion in Q4 2013 and $16.5 billion in 2013. Meanwhile, due to an outflow of capital and the lack of new IMF loan tranches since September, there was a deterioration in the financial account balance, which had a deficit of $6.6 billion in Q4 2014 and a deficit of $8.4 billion in 2014 after a surplus of $5.6 billion in Q4 2013 and a surplus of $18.6 billion in 2013 as a whole. The National Bank tried to fix the hryvnia against the US dollar in October and, following a one-time devaluation in early November, again in the final two months of 2014. Against that backdrop, the National Bank’s international reserves shrank from $16.4 billion (2.3 months’ worth of imports) at the end of September to $7.5 billion (1.2 months’ worth of imports) at the end of 2014.

Inflation accelerated throughout Q4 2014 under the influence of the hryvnia’s depreciation. The annual growth of the consumer price index reached 24.9% in December against 17.5% in September. At the same time the money supply decreased in Q4 2014 amid the National Bank’s forex interventions aimed at supporting the hryvnia’s exchange rate. In particular, M2 decreased by 3.7% in the period between September and December. The impact of the hryvnia’s depreciation on the rise in prices thus outweighed the monetary factors that deterred inflation in Q4 2014.

The state of the public finances deteriorated moderately throughout Q4 2014. Despite the fall in GDP, the high inflation led to a steady rise in public revenue. The consolidated budget had a deficit equal to 4.8% of GDP in 2014, but the deficit was not much higher than that in 2013, when the deficit amounted to 4.4% of GDP. Nonetheless, if the deficit of Naftogaz is taken into account, the consolidated budget deficit deteriorated to 10.3% of GDP from 6.7% of GDP in 2013, according to the IMF’s estimates.

The annual growth rate of bank lending continued to fall, decreasing from 14.8% in September to 12.1% in December amid a fall in real economic activity and the contraction of the money supply. The share of problem loans in the total volume of bank loans reached 19%, increasing from 12.9% in 2013 and 16.7% in Q3 2014.
Ukraine: slowdown in GDP fall, decrease in Naftogaz’s deficit, re-structuring of external debt

Available data for the first months of 2015 suggest that the fall in real economic activity has continued into 2015. In particular, the year-on-year decline in industrial output reached 21.3% in January 2015 compared with 10.1% in December 2014. Given the relatively high comparison base of the first half of 2014, one can expect that the rate of the fall in Ukraine’s GDP will remain double-digit throughout Q1-Q2 2015, but this fall will moderate later in the year. The 2015 budget estimates, adopted in March, are based on the optimistic assumption that GDP will decrease by 5.5% in 2015. The budget estimates provide for a return to economic growth as early as Q3-Q4 2015.

The government’s new IMF-supported economic program, which started to be implemented in March, provides for a substantial reduction in the deficit of Naftogaz. It was estimated at 5.7% of GDP in 2014, and is projected to amount to 3.1% of GDP in 2015, and decrease to zero in 2017. The consolidated budget deficit is expected to decrease at a moderate pace: to 4.2% of GDP in 2015, 3.7% in 2016 and 3.1% in 2017. The government’s efforts to consolidate the public finances will thus focus on the old problem of the national oil and gas monopoly’s deficit. Within the framework of these efforts, the government plans to raise gas and heat prices and take measures to improve the collection of payments due to Naftogaz.

Pressure on the balance of payments would be reduced in 2015 and the following years by: an increase in the inflow of capital into the country and a decline in the outflow of capital in the event of political stabilization in the region; as well as by new loan tranches from the IMF. Under these circumstances, there would be no need for a more substantial consolidation of the trade balance than that achieved in 2014. In this regard the overall deficit of the balance of payments may decrease – the IMF expects it to shrink to 11% of GDP from 14% in 2014 – and eventually turn into a surplus. Nonetheless, under this scenario, Ukraine’s external debt will probably come close to 160% of GDP and the public debt and government-guaranteed debts in it will exceed 90% of GDP, which would make it inevitable for the government to take certain measures to restructure it.

The need to curb the rise in the external debt in terms of percentage of GDP may prompt the National Bank to continue the policy of controlling the exchange rate of the hryvnia despite the declared intention to switch to a floating exchange rate system. Given the limited size of the National Bank’s international reserves and restrictions on their use under the IMF-supported action program, the National Bank may have to pursue a very tight monetary policy, which would create risks for the recovery of economic growth and, eventually, for the restoration of the debt sustainability of the country.

So the government, together with international organizations, plans to carry out a wide range of measures in the field of macroeconomic policy, which may contribute to a recovery in growth and the external sustainability of the Ukrainian economy. The success of the measures depends on whether a large number of conditions are in place. The most important of these conditions are: a de-escalation of the conflict in eastern Ukraine, a restructurin of the external debt and structural reforms in the economy, including the energy sector.
Ukraine

**Figure 12.1. GDP and output**: GDP growth and output change by sectors, (in %, year-on-year)

Source: the State Statistics Service of Ukraine

**Figure 12.2. 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 12.3. Government sector**: state budget (in % of GDP)

Source: national agencies

**Figure 12.4. 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 12.5. 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 12.6. 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