Macroeconomics of the region

Macroeconomics of countries:
Azerbaijan
Armenia
Belarus
Kazakhstan
Kyrgyzstan
Moldova
Russia
Tajikistan
Turkmenistan
Uzbekistan
Ukraine

Trends in 2014:
- **The world economy**: a slowdown in international trade growth in Q1
- **The United States**: an economic decline in Q1 amid abnormally cold weather, the strengthening of positive trends; the resumption of growth in the spring
- **Europe**: the stabilization of economies affected by the debt crisis; slight GDP growth
- **Asia**: a slowdown in GDP growth in China in Q1; a partial recovery of growth in the spring, unstable economic dynamics in Japan amid the central bank’s stimulus policy and an increase in the sales tax rate
- **The CIS**:
  1) A slowdown in economic growth in Q1
  2) An improvement in the region’s balance of payments amid a decline in investment demand and budget consolidation in oil and gas exporting countries
  3) A continued significant external imbalance in Belarus, crisis developments in Ukraine

Outlook and risks:
- **The world economy**: economic growth acceleration following a slowdown in Q1
- **Commodity markets**: stable energy prices; a recovery in metal prices; a rise in physical demand
- **The CIS**: a negative impact of regional instability on economic growth

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Macroeconomics of the region

The CIS countries’ GDP growth slows in Q1 2014

The annual growth of the aggregate GDP of the CIS member countries slowed to 1.2% in Q1 2014 compared with 2.8% in Q4 2013, and 2% in 2013. The fall in the growth rate in Q1 2014 was primarily attributable to a decline in investment activity in Russia and a slowdown in investment growth in Kazakhstan. In addition, the growth of agricultural output declined to different extents in many countries following a temporary sharp rise in Q3 and Q4 2013, which was partly due to the low base of 2012. A slower rise in households’ consumption and exports also contributed to the slowdown in the region’s GDP growth. Unlike in 2013, this process affected all groups of CIS countries, including the oil and gas exporters, the labor exporters and the countries with a diversified structure of exports. It should be noted that the slowdown in the economic growth of the latter of the groups was due to a decline in Ukraine’s GDP, which recommenced amid an acute economic and political crisis in that country, rather than the impact of factors common for all CIS countries.

All groups of CIS countries experience a slowdown in economic growth

External factors also had a negative effect on the CIS economies, whose growth slowdown was simultaneous with the global economic downturn. This affected industrial output and external trade, especially those of emerging economies (see Figure 1.1). A significant but short-term effect on the CIS countries’ economic growth was produced by a warm winter in Europe, which affected energy exports from Russia. Nonetheless, the negative impact of external factors on the region was, in general, of a limited nature. This was because energy prices experienced a moderate fall in Q1 2014 (see Figure 1.2), which was offset by a rise in exports of crude oil from Kazakhstan and, to a lesser extent, a rise in exports of natural gas and petroleum products from Russia. A severe decline occurred in the price of industrial metals and ores (also see Figure 1.2). This had a significant negative effect on the CIS countries that are large exporters of these commodities (in particular, Ukraine and Armenia). The export price of cotton and wheat increased in Q1 2014.

External factors also have a negative effect on the CIS economies

The annual GDP growth rate of the CIS oil and gas exporters (Azerbaijan, Kazakhstan, Russia and Turkmenistan) fell to 1.2% on average in Q1 2014 compared with 2.6% in Q4 2013. Major factors behind the slowdown included: a decline in fixed capital investment, which became stronger in Russia during the period; and a slowdown in the growth in households ‘consumption and government consumption expenditure amid fiscal consolidation in Russia, Kazakhstan and Azerbaijan. In addition, these three countries reduced oil production in Q1 2014. Russia and Kazakhstan managed to increase the total volume of exports in real and nominal dollar terms compared with Q1 2013 despite the reduced oil production.

Energy prices experience a moderate fall in Q1 2014

A serious decline occurred in the price of industrial metals

A decrease in fixed investment becomes the main factor behind the slowdown in GDP growth

A fall in remittances from abroad affects the labor exporting countries

The export price of cotton and wheat increased in Q1 2014.

A fall in the volume of cash remittances from abroad, in particular from Russia, was a common factor behind the slowdown in economic growth of the labor exporting countries (Armenia, Kyrgyzstan, Moldova and Tajikistan). According to data from the Bank of Russia, the nominal dollar volume of remittances made by individuals to CIS countries decreased by 5% year-on-year in Q1 2014. This was apparently due to the slowdown in Russia’s economic growth, and the continued weakening of the Russian ruble against major world currencies. The economic growth of those countries was also affected by the dynamics of agricultural output (see above), and various factors characteristic of specific countries (in particular, the dynamics of the mining and metallurgical industries of Armenia and Kyrgyzstan).
The average economic growth of the group of countries with a diversified structure of exports falls to 0.8% in Q1 2014. This was primarily because the balance of payments crisis in Ukraine entered an acute phase, which was accompanied by a GDP fall.

Belarus, whose situation regarding external sustainability also remained vulnerable, on the contrary achieved a slight acceleration in GDP growth. Uzbekistan’s economic growth slowed but not significantly, with the annual growth rate in Q1 2014 being 7.5% compared with 7.7% in Q4 2013.

The state of public finances in the CIS countries improved in Q1 2014 with consolidated budget surpluses averaging out at 3.2% of GDP compared with 2.6% in Q1 2013. This improvement reflects fiscal consolidation in Russia and Azerbaijan. It led to a general rise in the consolidated budget surplus for the CIS countries despite the fact that Kazakhstan’s surplus decreased. The state of public finances in the labor exporting countries, on the contrary, deteriorated except in Moldova, whose budget deficit slightly decreased compared with Q1 2013. The state of public finances in the countries with a diversified structure of exports changed in different directions. However, given the fact that Ukraine’s positive budget balance dynamics were largely due to a significant increase in the National Bank’s transfers to the budget (see pp. 32-34), it is safe to say that the general state of public finances in this group of countries deteriorated.

The aggregate current account surplus of the CIS countries amounted to 5.4% of GDP in Q1 2014 compared with 3.7% in Q1 2013. The general improvement in the state of public finances in the CIS region was one of the factors behind the increase in the current account surplus. Other factors included the strengthening of domestic demand amid instability in the region and a decline in imports under the influence of the weakening of the national currencies in Russia and Kazakhstan. For the group of oil and gas exporting countries, the current account surplus increased from 5.7% of GDP in Q1 2013 to 7.1% of GDP in Q1 2014. A rise in the current account surplus in Russia and Kazakhstan was partially offset by a decrease in Azerbaijan’s current account surplus. Meanwhile, the labor exporting countries’ current account deficit decreased from 11.1% to 10.2% of GDP; and the countries with a diversified structure of exports reduced their deficits from 8.7% to 4.7% of GDP. The considerable decrease in the current account deficit of the latter group was due to a decrease in the deficits of Belarus and Ukraine.
Inflation slightly accelerated in the CIS region in Q1 2014. The average annual consumer price index was 6.5%, up from 6% at the end of 2013. The acceleration in the rise in prices was largely due to the impact of the depreciation of the national currencies in a number of countries, including Russia, Kazakhstan, Belarus and Ukraine. At the same time the growth in the money supply slowed down significantly in all three groups of countries in the region (oil and gas exporters, labor exporters, and countries with a diversified structure of exports). This was amid a net capital outflow or a decline in net capital inflow, and the central banks’ interventions with a view to curbing the depreciation of the local currencies.

The dynamics of the external economic environment was moderately favorable for the CIS countries. It remained unchanged in Q1/Q2 2014 despite the fact that the world’s major economies experienced a slowdown in GDP growth throughout Q1 2014. In particular, the slowdown was substantial in the United States and, to a lesser extent, in China. The Eurozone’s GDP growth remained slow in Q1 2014. Nonetheless, global economic growth accelerated again throughout Q2 2014, which helped the recovery of prices in commodity markets during the period. World prices of energy resources and especially industrial metals rose throughout Q2 2014. The average annual growth rate of prices of industrial metals was -0.4% in Q2 2014 compared with -12% in Q1 2014, and -10% in Q4 2013 (see World Bank Commodity Data, June 2014). This contributed to a 7% year-on-year rise in the nominal dollar volume of Russian exports of goods in April and May, according to customs data.
The Ukraine crisis continues to be the main source of risk for the region’s economies. The direct impact of the developments in Ukraine on the economies of neighboring countries has been limited— the share of the Ukrainian economy in the economy of the region was only 6.3% in 2013. Despite this, the consequent crisis in the relationship between Russia and the West has led to deterioration in access to international capital markets for Russian companies and a general rise in economic uncertainty. These factors are, to a large extent, responsible for the decline in investment activity in the Russian economy in 2014. Their impact may continue for a long period of time.

Nonetheless, as the Ukraine crisis did not get worse, the dynamics of the economies in the region stabilized in Q2 2014. It appears that the annual GDP growth of the CIS countries in Q2 2014 will exceed the level of Q1 2014. April’s consensus forecast of international organizations predicted a 3% increase in the aggregate GDP of the CIS economies in 2014 (see the previous edition of the CIS Macromonitor). This appears to remain relevant, or require a limited downward revision. Meanwhile, the improvement in the fiscal and external balances of the economy of the region in 2014 enhances its resistance to additional negative shocks. Ukraine and Belarus have the least sustainable balance of payments positions, and continue to be exposed to substantial risks with regard to the stability of their economies.
Azerbaijan: Slowdown in GDP growth amid resumption of decline in oil and gas sector, consolidation of public spending

In Q1 2014, Azerbaijan’s economic growth was slower than in 2013 amid the resumption of a decline in the oil and gas sector. GDP grew by 2.5% compared with Q1 2013 amid a 4.1% decrease in the oil and gas industry, and an 8.8% increase in the other industries. In 2013 Azerbaijan’s GDP grew by 5.8%, while the oil and gas sector had a growth rate of 1% against 10% in the other sectors. The negative growth rate in the oil and gas sector led to the aggregate industrial output falling by 2.4% year-on-year in Q1 2014. The construction sector’s output rose by 7%, while agricultural output increased by 8.8%. Retail trade grew by 9.2% in comparable prices amid a marked rise in average pay, which rose by 6.7% in real terms in the first two months of 2014.

The state of public finances improved in Q1 2014 compared with Q1 2013. The combined surplus of the state budget and the State Oil Fund amounted to 5.9% of GDP against 1.2% in Q1 2013. The growth in the surplus was attributable to: an increase in the State Oil Fund’s revenues, which offset a decrease in budget revenues; and also to a fall in public spending, which amounted to 33.3% of GDP in Q1 2014 compared with 34.9% in Q1 2013. The 2014 state budget provides for a commensurable decrease in public spending in the entire year. The volume of the State Oil Fund’s assets grew to $36.3 billion (50% of GDP) in the past four quarters, from $35.9 billion (48.8% of GDP) at the end of 2013.

The current account surplus continued to decrease, amounting to $3.3 billion (19.8% of GDP) in Q1 2014 against $4 billion (24.5% of GDP) in Q1 2013. This was amid a fall in export revenues and a rise in imports. Simultaneously, a considerable increase occurred in capital inflows into the country in the form of direct and portfolio investments. This led to a decrease in the financial account deficit – a deficit means a net capital outflow – to $609.5 million (3.6% of GDP), from $2.6 billion (15.4% of GDP) in Q1 2013. Reserve assets in Q1 2014 grew by $2.8 billion, which was higher than in Q1 2013 when they increased by $1.7 billion.

The growth in the money supply continued to slow down amid the fixed exchange rate regime maintained by the National Bank. The annual growth rate of M2 was 16.9% at the end of March compared with 19% at the end of 2013. Inflation, which accelerated in late 2013 in connection with a rise in government-regulated motor fuel prices, began to slow down again. The annual consumer price index fell to 2% by the end of Q1 2014 from 2.4% at the end of 2013.

The annual growth rate of bank lending rose to 28% at the end of Q1 2014 compared with 26% at the end of December 2013.
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 – Q1 2008 = 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
**Armenia: Slowdown in economic activity amid low inflation and stable indicators for balance of payments**

In Q1 2014, Armenia’s GDP growth slowed to 3.1% in annual terms from 3.5% in 2013. This was amid a decline in domestic demand that was caused by: a slowdown in lending growth to 11.6%; a low growth rate of the population’s real income (about 3%); a slowdown in the rise in cash remittances from abroad to 6.1%; a 7.9% fall in investment in 2013; an unfavorable external environment (Russia’s economic slowdown, slow growth in Europe and unfavorable prices of exported primary commodities); as well as the high base effect (7.9% year-on-year growth in Q1 2013). Poor economic activity was especially noticeable in the mining industry (a 1.3% output decrease), the construction sector (a 3.3% decrease), and major services sectors such as trade (a 2.8% rise), transportation (a 2.7% rise) and financial intermediation (a 1.3% decrease). The deterioration was partly offset by the good performance of the agricultural sector (a 6.0% output increase) and the manufacturing sector (a 4.5% increase).

The balance of payments deteriorated in Q1 2014. This is evidenced by a continued decline in the gross international reserves and pressure on the dram throughout the entire quarter. The gross international reserves shrunk by $280.4 million from December 2013 to $1,969.3 million (the equivalent of 5.3 months of imports) as of the end of March 2014. The deterioration in the balance of payments was attributable to a significant increase in the current account deficit, which grew to 26.2% of GDP from 20.6% of GDP in Q1 2013. The foreign trade deficit decreased due to the combination of a 1.8% increase in exports and a significant slowdown in the rise in imports, which increased by 0.2% year-on-year in Q1 2014. It should be noted that the deterioration in the current account balance was mainly caused by an increase in the primary income deficit.

The state of public finances deteriorated in Q1 2014 compared with Q1 2013. Nonetheless, it remained stable. The state budget surplus decreased to 0.8% of GDP from 3.5% of GDP in Q1 2013. This was attributable to a slowdown in economic activity and a consequent slowdown in the rise in tax revenue to 1.7%. State budget expenditure significantly increased as a result of a rise in social benefits (32.7% of spending), transfers (13.9% of spending), interest payments on the public debt (8.4% of spending) and, to a certain extent, a more modest rise in pay (9% of spending).

The annual inflation rate remained within the target band, standing at 3.8% at the end of Q1 2014. It appears that the impact of price increases following the rise in energy prices in the middle of 2013 has disappeared. The general slowdown in inflation resulted from: the slowdown in economic growth and lending, which grew by 11.6% in Q1 2014 in annual terms; low inflation pressure from world food prices; and also new agreements with Russia, which fix prices for imported energy resources. This made it possible for the National Bank to loosen its monetary policy. The central bank reduced its refinance rate by 0.25 points to 7.5% and the dram reserve requirement from 4% to 2%.
Outlook

Armenia: Acceleration in GDP growth amid limited inflation

In May 2014, the Indicator of Economic Activity (IEA) rose to 5.1% in annual terms due to the diminishing base effect and an improvement in the indicators of the industrial sector (+7.1%), the agricultural sector (+8.6%) and the services sector (+4.1%). Unlike the other economic branches, there was deterioration in the indicators of the trade and construction sectors, whose annual growth slowed to 4.9% and 0.1%, respectively. As a result, in the first five months of 2014, the IEA growth rate rose to 4%. According to a consensus forecast, despite heightened uncertainty in the external environment, the country’s GDP growth is expected to accelerate to 4.8% in 2014. This will be due to: increased macroeconomic assistance from international donors; the expansion of cooperation with the Customs Union and the diminishing base effect. Major risks currently include: the uncertain economic situation in Russia – with geopolitical processes being among the reasons for it; and a further weakening in domestic demand due to a possible new rise in energy prices.

In May 2014, the balance of payments deteriorated again. This is evidenced by: a decrease in the gross international reserves, which shrank by $386.2 million since December 2013; and recurrent pressure on the dram throughout the entire period. The leadership of the country has made new borrowings as a result of: an increased foreign trade deficit - a slight acceleration in the rise in imports amid a slowdown in the growth of exports; a decline in the annual growth rate of remittances from abroad, which fell to 0.6% in April 2014; and an expected increase in the state budget deficit. Nonetheless, June 2014 saw signs of the strengthening of the national currency, which suggests a decline in tensions in the currency exchange market and lower demand for dollars.

The 2014 state budget envisages a substantial, 18.6% increase in public expenditure without a rise in the tax burden, and consequently, an increase in the budget deficit to 2.3% of GDP. Moreover, given the more pessimistic outlook for GDP growth and the expected low inflation rate (between 2.5 and 5.5%), the government’s expansive fiscal policy will apparently be accompanied by an expansive monetary policy. Such countercyclical macroeconomic policy will certainly stimulate economic activity, but it will lead to a deterioration in external sustainability and, in the light of the modest rise in exports, contribute to the depreciation of the dram and the acceleration of inflation by the end of 2014. However, given the current IMF country program, the deterioration in major macroeconomic indicators will remain under control.
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 – Q1 2008 = 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: Continued external imbalances, high inflation

In Q1 2014, Belarus’s GDP showed positive, although slight, growth, increasing by 0.5% compared with Q1 2013. The economic dynamics continued to be of an uneven nature. Wholesale and retail sales increased by 10.4% and 13.1%, respectively, in comparable prices, while industrial output decreased by 3.4%. In the industrial sector, the most significant decreases occurred in the production of transport vehicles and the production of machines and equipment (24.6% and 17.3%, respectively). Whereas the chemical and the refining industry, which made a significant negative contribution to the general performance of the economy in 2013, resumed growth, increasing their output by 5.3% and 3.6%, respectively. The agricultural sector and the power, gas and water supply sector experienced decreases of 4.7% and 3.1%, respectively. The rise in output in the construction sector slowed to 0.4% from 6.6% in 2013.

The monthly inflation rate was between 1.3 and 2% throughout Q1 2014, remaining at levels similar to those in Q3/Q4 2013. The annual inflation rate fell from 16.5% at the end of 2013 to 16% at the end of Q1 2014. This was mainly because the January rise in government-regulated prices proved lower than that in 2013. There was a slowdown in money growth that took place amid the National Bank’s interventions, which were made with a view to limiting the pace of the Belarusian rouble’s depreciation. Despite this, the annual growth of M3 accelerated from 19.8% at the end of 2013 to 21.3% at the end of March due to the growth in foreign currency deposits in rouble terms. Thus monetary policy did not have a deterring effect on the rise in prices.

The state of the public finances changed for the worse in Q1 2014 compared with 2013. The consolidated budget surplus decreased from 2.9% of GDP in Q1 2013 to 0.4% in Q1 2014. The state of the country’s balance of payments somewhat improved, apparently due to the strengthening of investment demand. The current account deficit in Q1 2014 amounted to 10.9% of GDP, down from 17% in Q1 2013. Amid a decline in capital inflows, the current account deficit was, to a considerable extent, financed with the National Bank’s international reserves, which shrank from $6.7 billion to $5.7 billion in Q1 2014, or from 1.8 months to 1.6 months worth of imports.

The annual growth rate of bank lending was 27.3% at the end of Q1 2014 compared with 28.5% at the end of 2013. At the same time the growth of lending to companies accelerated to 30.1% in March from 22.7% in December. Simultaneously, there was a slowdown in the growth of lending to public non-financial organizations and individuals. The share of problem assets changed insignificantly in Q1 2014, decreasing from 4.5% at the end of 2013 to 4.4% at the end of Q1 2014. The fixed capital adequacy rate fell rapidly in the final months of 2013, decreasing from 19% at the end of Q3 to 15.5% at the end of Q4 2013. It was 15% at the end of Q1 2014.

The country’s GDP shows positive, although slight, growth in Q1 2014

Wholesale and retail sales increase by 10.4% and 13.1%, respectively, while industrial output decreases by 3.4%

The monthly inflation rate is between 1.3 and 2% throughout Q1 2014

The annual growth of M3 accelerates from 19.8% at the end of 2013 to 21.3% in March 2014

The state of the public finances changes for the worse in Q1 2014

The current account deficit in Q1 2014 amounts to 10.9% of GDP, down from 17% in Q1 2013

The annual growth rate of bank lending almost does not change in Q1 2014
Outlook
Belarus: Limited GDP growth, continued risks to external sustainability

The Belarusian economy’s annual growth slowed to negative rates in January and February 2014, but was positive territory for the whole of Q1 2014. According to available data for Q1 2014, Belarus had an annual growth rate of 1 to 2%. The recovery in economic growth was due to three factors. Firstly, a high base effect, which was caused by strong economic activity in early 2013, ceased to influence economic growth. Secondly, Q1 2014 saw a cessation in the decline in the chemical and oil refining industries, which made a major contribution to the general economic dynamics in 2013. Thirdly, economic growth was fueled by the stabilization of the growth rate of bank lending. As we noted above, the growth of lending to companies even accelerated in Q1 2014. To all appearances, the extent of the recovery in economic growth will be held down by demand-side impediments. In particular, one can expect a further slowdown in the growth of household consumption in connection with a fall in the growth rate of average pay in Belarus. The annual growth rate of real pay was 2.1% in March 2014 compared with 5.7% in December 2013, and 16.4% in June 2013. The possibility of further acceleration in the rise in exports will continue to be limited considering the current difficult economic situation in the region.

Inflation in Belarus did not show any signs of deceleration throughout the first half of Q2 2014. The annual consumer price index rose to 19% in May. Despite the acceleration of the rise in prices in Belarus, the National Bank further loosened its monetary policy, successively reducing its base refinance rate in April and May. To all appearances, inertial dynamics in this sphere will result in a rise of 25 to 30% in the consumer price index in 2014. Whereas the government projected a rise of 14 to 16% in its 2014 Monetary Policy Guidelines.

The implementation of the state budget in Q1 2014 also indicates the likelihood that the country’s actual budgetary performance will be worse than specified in the Budget Law, which projects a zero deficit for 2014.

Given the existence of seasonal factors, one can expect that Belarus’ current account deficit will be between 6 and 10% of GDP in 2014. We expect a limited improvement in the country’s external balance position, with a slowdown in the growth of pay and investment being one of the reasons. This slowdown apparently indicates both a change in the authorities’ policies and independent changes in companies’ behavior. More significant consolidation is impeded by the authorities’ expansionary monetary and fiscal policies, which are looser than in 2013. Monetary and fiscal tightening with a view to at least limiting deviations from the targets specified in the Monetary Policy Guidelines and the Budget Law is a condition for the Belarusian economy to regain the ability to maintain external sustainability without the assistance of external donors.

Annual GDP growth returns to positive territory in Q1 2014
A high base effect, caused by strong economic activity in early 2013, ceases to influence economic growth
One can expect a further slowdown in the growth of household consumption
Inflation shows no signs of deceleration throughout the first half of Q2 2014
The National Bank further loosens its monetary policy in April and May
The country’s actual budgetary performance will be worse than specified in the Budget Law
One can expect that the current account deficit will be between 6 and 10% of GDP in 2014

More significant consolidation is impeded by loose monetary and fiscal policies
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 – Q1 2008 = 100)

Source: national agencies, IMF

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
Trends

Kazakhstan: Improvement in balance of payments and public finances amid depreciation of tenge, slowdown in economic growth and acceleration in inflation

In Q1 2014, Kazakhstan’s GDP growth slowed down to 3.8% in annual terms from 6% in 2013 and 4.6% in Q1 2013. This was due to the impact of external factors - a slowdown in economic growth in Russia and China - and also domestic factors. The domestic factors included: weaker consumption; a fall in the annual growth rate of investment from 8.5% in Q1 2013 to 1.9% in Q1 2014 following a devaluation of the national currency in February; and a 1.9% decrease in oil production amid difficulties in increasing oil extraction in existing fields, and the blurred postponement of the start of the development of the Kashagan field. As a result, the industrial sector experienced an output decline of 0.3% against an increase of 1.9% in Q1 2013, while the output of the services sector rose by only 4.6% compared with a rise of 6.9% in Q1 2013. The agricultural and the construction sector continued to have a satisfactory growth rate with 3.6 and 3.9%, respectively.

The February 2014 devaluation of the tenge and the subsequent slowdown in economic activity had a positive effect on the country’s balance of payments. According to a preliminary estimate from the National Bank, the state of the balance of payments substantially improved in Q1 2014. The current account surplus increased to $6.2 billion, or 14.4% of GDP compared with 5% of GDP in Q1 2013. This was due to a 10.8% increase in exports and a 14.6% decrease in imports, as well as a fall in the primary income deficit, which decreased by 4.9%. As a result of the correction of external imbalances, the National Bank was able to resume increasing the gross international reserves, which grew by $1.8 billion from December 2013 to $26.5 billion at the end of Q1 2014, and simultaneously protect the lower boundary of the exchange rate band of between 182 and 188 tenge for one US dollar. The international reserves, including the National Fund of Kazakhstan amounting to $72.8 billion at the end of Q1 2014, reached $99.3 billion in total.

The strong rise in state budget revenue of 15.6% year-on-year in Q1 2014 was as a result of the expansion of the National Bank’s transfers and the tenge devaluation’s positive impact on fiscal revenue from the oil sector. Despite this, therevenue from corporate income tax and VAT decreased by 6.9 and 4.9% year-on-year respectively amid a slowdown in economic activity. The rise in state budget revenue outpaced the growth of public expenditure, which increased by 14% compared with Q1 2013. As a result, the state budget surplus grew to 1.7% of GDP.

The acceleration of inflation following the 19% tenge devaluation in February 2014 was limited. The annual inflation rate was only 6.2% as of the end of Q1 2014, with the target band being between 6% and 8%. The low inflation rate was attributable to: measures taken by the National Bank and the government to curb inflation, which included freezing government-regulated prices; the low impact of monetary factors; and a reduced propensity to consumption. M2 decreased by 1.4% year-on-year in Q1 2014, while the broad money aggregate M3 grew by 15%. This indicated a change in the structure of assets in the economy in favor of dollar deposits. Due to the tenge devaluation, bank lending growth accelerated to 20.2% in Q1 2014 in annual terms. It should be noted that the banking sector’s efficiency indicators deteriorated, with the share of loans overdue for more than 90 days growing to 31.2%.
Outlook

Kazakhstan: Slowdown in GDP growth amid heightened uncertainty

Activity indicators stabilized at a low level in May 2014. The growth of the short-term Indicator of Economic Activity was at 3.2% compared with May 2013. The growth rate of the trade and communications sector fell but remained at a rather high level, while the performance indicators of the transport sector improved significantly. The industrial sector’s growth rate returned to positive territory due to positive dynamics in the manufacturing industry, while oil production continued to decrease. Activity in the construction and agricultural sectors remained in solid positive territory.

The economic situation should improve in Q3/Q4 2014 as a result of: the expansion of fiscal stimulus measures; the implementation of government programs aimed at the development of the non-primary commodity sector of the economy and industrialization; measures taken to improve the banking system; efforts to attract foreign investment; and the anticipated positive effects of the currency devaluation on the real sector of the economy. Nonetheless, the improvement will be more limited than expected. The economic situation of Kazakhstan will be mixed due to the heightened geopolitical uncertainty, and a downward revision of the forecast for oil production in 2014 from 83 million metric tons to 81.8 million tons (the level of 2013). According to the consensus forecast of international organizations, the country’s GDP is expected to grow by 5.4% – EDB predicts a growth of 5.1% – but this forecast already appears too optimistic.

The improvement in the balance of payments in Q1 2014 was caused by a paradoxical 23.5% year-on-year increase in oil exports amid a decrease in oil production in the period. Given the expected continued fall in oil production, one should conclude that the oil export trend will change downwards before the end of 2014, and the positive impact of the devaluation on non-oil exports will be limited. The possible deterioration in the balance of payments before the end of 2014, coupled with acceleration in inflation, may provoke increased pressure on the tenge and lead to its depreciation.

Public expenditure has been expanded in order to, among other things, compensate for the losses caused by the devaluation, and to stimulate the economy. The government expects to ensure a moderate increase in revenue—due to the devaluation’s effects and an increase in customs duty on oil exports—and limit the 2014 budget deficit to 2.3% of GDP. A risk for public finances is posed by difficulties in finding compensation for the lower-than-expected volume of oil production resulting from the delay in the development of the Kashagan field, and technical problems in other oil fields. However, Kazakhstan can rely on: the quite large consolidated budget surplus in Q1 2014 (5.5% of GDP); the continued high level of oil prices; and the accumulated resources of the National Fund of Kazakhstan, which totaled $75.8 billion at the end of May 2014.

In May 2014, the country’s annual inflation rate stood at 6.5%, which is an acceptable level to the government. However, inflation may accelerate before the end of 2014 as the rise in import prices spreads to domestic prices. It may exceed the upper boundary of the National Bank’s target band of 6 to 8% for 2014. For instance, the annual industrial producer price index rose to 17.8% in May, while wholesale food and consumer inflation accelerated to more than 10%.
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 – Q1 2008 = 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: Slowdown in GDP growth, deterioration in balance of payments, depreciation of som and acceleration in inflation

In Q1 2014, Kyrgyzstan’s GDP growth slowed down to 5.6% from 8.8% in Q1 2013. Economic activity was on the decline throughout Q1 2014 due to a high base effect and weakening domestic demand. This was despite the continued strong growth in investments (33.3%), which mainly went into the construction sector. Domestic demand weakened due to: a fall in the growth rate of remittances from abroad; a decrease in external demand, which was caused by a slowdown in economic growth in major trading partners (Russia, Kazakhstan and China); and administrative barriers to exports to the Customs Union’s member countries.

From the sectoral perspectives there was a growth slowdown in retail trade (+4.5% in annual terms) and the services sector in general. The continued strong growth in the manufacturing sector (+7.8%) was due to an increase in gold production to 3.2 metric tons from 2.8 tons in Q1 2013. This growth can be viewed as an expected slowdown when compared with a rise of 25.3% in Q1 2013. Agricultural output increased by only 1.2%. A contribution to economic growth was made by the mining industry (+14.8%) and the construction sector (+24.7%). If the contribution of the companies engaged in the development of the Kumtor gold deposit is not taken into account, Kyrgyzstan’s annual GDP growth slowed down to 4.9% from 6.4% in Q1 2013.

The balance of payments deteriorated in Q1 2014. This was due to: a decrease in net errors and omissions resulting from problems in the currency exchange markets of Russia and Kazakhstan; and a decrease in the inflow of transfers and cash remittances from abroad. The depreciation of the national currencies in partner countries created pressure on the som and forced the National Bank to use foreign exchange interventions. The central bank sold a total of $198.1 million worth of foreign currency during Q1 2014. As a result, the country had a balance of payments deficit of $124.4 million and since December 2013 its gross international reserves shrank by $121.6 billion. This was despite: a decrease in the foreign trade deficit resulting from a strong (15.7%) rise in exports – gold exports grew by 80%; and a modest, 3.3% increase in imports resulting from a slowdown in consumption growth and the som’s depreciation.

The state of public finances in Q1 2014 was worse than in Q1 2013. The low growth rate of public revenue (5.8% in annual terms to 33.6% of GDP), amid a strong, 12.5% increase in expenditure (30.6% of GDP), led to a substantial decrease in the seasonal budget surplus, from 4.9% of GDP in Q1 2013 to 2.9% in Q1 2014. A decrease in fiscal revenue in annual terms changed into growth only in March 2014. This was due to a significant rise in revenue from excise taxes, customs revenues, non-tax revenues and official transfers.

The annual inflation rate rose to 6.3% in March 2014. There was acceleration in price growth across all inflation components except services, whose price growth slowed to 4%. Food, which accounts for more than 50% of the consumer basket, increased in price by 5.4% and alcoholic beverages increased by 9.9%, while prices of non-food consumer goods rose by 4.4%. Amid a slowdown in money growth, the acceleration of inflation was largely attributable to the impact of the som’s depreciation against the US dollar on consumer prices.
Outlook
Kyrgyzstan: Rise in inflation rate, slowdown in GDP growth and decline in external sustainability

In May 2014, Kyrgyzstan’s GDP growth slowed significantly – to 0.7% compared with May 2013 – amounting to 4.3% year-on-year in the first five months of 2014.

Apart from a considerable high base effect, major reasons for the slowdown included: a weakening in domestic demand, which was due to a deceleration in the growth of real wage to 2.1% in January-May 2014; a slowdown in bank lending; restrained public spending; and a slowdown in the rise in investment and cash remittances from abroad. The economic growth slowdown was also attributable to weaker external demand, which led to a 2.2% decrease in imports. If the contribution of the companies engaged in gold mining is not taken into account, the country’s GDP growth slowed down to 4.1% compared with 4.9% in Q1 2014. The consensus forecast of international organizations, which does not include the government’s overestimated expectation, predicts Kyrgyzstan’s GDP to grow by 5.1% in 2014.

The foreign trade deficit retained a downward trend in April 2014. The som’s exchange rate stabilized as a consequence of the stabilization of the national currencies in Russia and Kazakhstan. This helped correct foreign trade imbalances and increase the country’s foreign exchange reserves in April and May. The gross international reserves grew by $38.7 million in May to $2,180 million as of 1 June 2014. Nonetheless, in the remaining part of 2014, general external sustainability will be exposed to three major risks, which may lead to the emergence of periods of heightened volatility for the som’s exchange rate, and support the depreciation trend in the national currency. The three risks are: the extent of economic growth slowdown in Russia and Kazakhstan, which has a direct impact on export activity and the volume of remittances from abroad; the withdrawal of US troops from the Manas military base, which may lead to a more considerable decrease in foreign exchange inflows; and instability in gold production by virtue of technical, domestic political and price factors, including the expected decline in gold prices in international markets.

Annual inflation accelerated to 8.1% as of the end of May, which was apparently due to the depreciation of the som and a seasonal rise in food prices. As a result the National Bank had to use interventions in the currency exchange market, and tighten its monetary policy. According to an updated forecast for 2014 from the National Bank, inflation will continue to rise and reach 10.2% by the end of 2014. The average annual inflation rate is expected to be 8.2%. Since the National Bank is in transition to a more active use of the refinance rate, this rate will apparently be maintained at a high level considering the existing inflation and depreciation risks.

Other short-term risk factors include fiscal sustainability and the pace and conditions of Kyrgyzstan’s accession to the Customs Union of Belarus, Kazakhstan and Russia. In particular, amid the slowdown in economic activity and the withdrawal of US troops from the Manas base, there is a risk of a more significant decrease in fiscal revenue in 2014. The country’s membership in the Customs Union may initially be accompanied by a limited upward price correction, but will have a favorable effect on the economy in general in the medium term.
**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 – Q1 2008 = 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: Moderate slow down in GDP growth, acceleration in inflation under influence of external factors

Moldova’s economy continued its growth in Q1 2014; although the growth somewhat slowed down after a surge in late 2013, which was due to the dynamics of the agricultural sector. The country’s GDP rose by 3.6% compared with Q1 2013. Growth was rather even by sector. Output increased by 7.2% in the agricultural sector, 7.1% in the industrial sector, 8.5% in the construction sector, and 5.4% in the trade sector. In the manufacturing sector, there was 20.5% growth in the food industry, 26.4% growth in the textile industry and 22.9% growth in the chemical industry. Iron and steel output decreased by 0.6%, while the output of machines and equipment fell by 38.7%.

Meanwhile, household consumption rose by 0.6% compared with Q1 2013 and fixed capital investment grew by 8.6%. Exports increased by 3.4% in real terms, while imports fell by 0.5%.

The annual inflation rate was somewhat higher than in 2013, when the consumer price index rose by 5.2% (December on December). Annual inflation accelerated to 5.7% as of the end of Q1 2014. The National Bank did not change its base refinance rate in Q1 2014. According to the central bank’s reports released following its leadership’s meetings on monetary policy, the rise in inflation in the first months of 2014 was attributable to an exogenous acceleration in the rise in food prices. The authorities de facto tightened monetary policy, which manifested itself in a slowdown in the growth of the money supply in the economy. There was a rise in the National Bank’s interventions in the currency exchange market with a view to limiting the fall in the leu’s value that resulted from increased capital outflows from the country at the beginning of 2014. This was a common trend for many emerging economies in that period.

The deficit in the national public (consolidated) budget in Q1 2014 amounted to 0.3% of GDP, slightly decreasing compared with Q1 2013, when the deficit was equal to 0.4% of GDP. Both public revenue and expenditure decreased by about 1% of GDP compared with Q1 2013.

The current account deficit decreased to 5.9% of GDP in Q1 2014 from 7.1% of GDP in Q1 2013. The surplus in the financial account excluding reserve assets - the net capital inflow - decreased more significantly, from 8.9% to 3.4% of GDP.

The National Bank’s efforts aimed at keeping the Moldovan currency’s exchange rate stable amid a decline in the flows of capital and remittances into the country led to a decrease in its international reserves. They shrank to $2.7 billion at the end of March from $2.8 billion at the end of 2013, or to 5.1 months from 5.2 months worth of imports of goods and services.

The annual growth rate of bank lending rose to 21.7% as of the end of Q1 2014 from 18.6% at the end of December 2013. The tightening of monetary policy in Q1 2014 led to a slowdown in lending growth later in Q2.

The banking sector’s sustainability indicators slightly improved in Q1 2014. The capital adequacy ratio rose to 23.5% from 23.4% at the end of 2013. The share of liquid assets in total banking assets decreased to 33.7% from 33.8% at the end of 2013.
Moldova

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

![Graph showing GDP growth and output change by sectors](image)

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 – Q1 2008 = 100)

![Graph showing foreign trade](image)

Source: national agencies

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

![Graph showing government sector](image)

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)

![Graph showing monetary sector](image)

Source: national agencies

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

![Graph showing economic growth](image)

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)

![Graph showing savings and investments](image)

Source: estimates and forecasts by national agencies and the IMF
Russia: Fall in investment, consolidation of fiscal and external balances amid instability in region

Russia’s year-on-year GDP growth fell to 0.9% in Q1 2014 from 2% in Q4 2013. The main factor determining the growth slowdown was a fall in investment activity in the first months of 2014. Fixed capital investment decreased by 4.8% in Q1 2014 in real terms compared with Q1 2013. At the same time household consumption apparently continued to grow at a relatively high rate as retail sales rose by 3.5% in Q1 2014 compared with Q4 2013, against a rise of 4% in Q1 2013.

The fall in fixed investment affected the volume of construction, which decreased by 3.6% compared with Q1 2013. At the same time growth in the manufacturing sector remained at the same level as at the end of 2013. The extractive industries continued to have a moderate growth rate with a 0.8% increase in Q1 2014.

Russia’s balance of payments improved amid instability in the region. The current account surplus in Q1 2014 amounted to $27.1 billion (5.9% of GDP), up from $25 billion (5.2% of GDP) in Q1 2013. The increase in the current account surplus was largely due to a fall in imports of goods, which totaled $71.6 billion compared with $77.1 billion in Q1 2013. At the same time the financial account deficit - the net capital outflow - increased significantly, to $48.6 billion from $12.6 billion in Q1 2013. Against this background, the ruble depreciated from 32.7 for one US dollar at the end of 2013 to 35.7 at the end of Q1. The Bank of Russia tried to slow down the pace of depreciation, increasing its interventions in the currency exchange market compared with 2012 and 2013.

The state of public finances improved, partly due to measures taken by the government in this regard within the framework of the budget for the current fiscal year, and partly as a result of the ruble’s depreciation. In particular, the federal budget had a surplus of 110.3 billion rubles (0.7% of GDP, according to the finance ministry’s estimate) against a deficit amounting to 0.4% of GDP in the Q1 2013.

Annual inflation, which stood at slightly more than 6% in the first two months of 2014, accelerated to 6.9% in March amid the ruble’s weakening. The depreciation of the ruble outweighed the impact of the dynamics of the money supply. The growth of money supply slowed down in Q1 2014 due to both the central bank’s interventions in the exchange market and – probably to a lesser extent – March’s increase in the central bank’s key interest rate. The annual growth rate of M2 fell to 12.1% in March 2014 from 16.3% in December 2013.

The growth rate of bank lending almost did not change in Q1 2014 despite the slowdown in money growth. In particular, the annual growth rate of banks’ net claims on the other sectors of the economy rose to 17.7% at the end of March from 17.5% at the end of December. Some of the banking sector’s sustainability indicators deteriorated in Q1 2014. For instance, the capital adequacy ratio was 13.2% in March compared with 13.5% in December. The share of problem loans grew to 6.4% from 6% at the end of 2013. At the same time the fixed capital adequacy ratio rose to 9.4% from 9.1% at the end of 2013 and the share of highly liquid assets in the total volume of assets increased to 11% from 9.9%.
Outlook

Russia: Slow recovery in investment, improvement in fiscal and external balances

Russia’s economic outcomes for 2014 will be determined by a number of factors. An important one will be the dynamics of fixed capital investment and finished goods inventories, which experienced a decline in 2013 and early 2014. Data for the most recent months indicate that investment activity recovered somewhat following a setback at the beginning of 2014, primarily in January.

Given the fact that a decrease (rather than a slowdown) in fixed investment is a relatively rare occurrence for Russia, and that periods of negative investment growth never lasted long between 1999 and 2012, one may expect a further recovery in investment in the remaining part of 2014 and a probable return to positive territory in the latter half of 2014.

This recovery continues to be impeded by tensions in the region and associated risks to the access to international capital markets for Russian economic entities, to the ties with major trading partners, and the current tightening of the central bank’s policy. It should be noted that the impact of monetary policy tightening is, for the time being, potential rather than actual. Available data do not give strong grounds to believe that the central bank’s policy already has a considerable negative effect on the economy. Given the results of Q1 2014, there are currently grounds to expect Russia’s GDP to grow by 0.5 to 1.5% in 2014.

The rise in prices remained heightened until the end of the spring, as a result of which the annual inflation rate rose to 7.6% in May 2014. It is likely that inflation will slow down in the remaining part of 2014. By the end of 2014, the rise in the consumer price index will be within the central bank’s target band of 3.5 to 6.5% for 2014. The inflation rate will most likely be between 5.9 and 6.4%, which is significantly higher than the target level of 5%. Key factors behind this will be: the stabilization of the ruble’s exchange rate; a moderate rise in government-regulated prices, whose growth was limited by government directives; and primarily the central bank’s policy. The monetary policy of the Bank of Russia will apparently remain tight. Statements by the leadership of the central bank suggest that the key interest rate may be raised if this is deemed necessary for meeting the inflation targets for 2014 and 2015, when the target level is to go down to 4.5%. The central bank already reduced the degree of control over the ruble’s exchange rate in May and expresses an intention to complete a transition to a flexible exchange rate system in accordance with approved plans. This is important from the standpoint of the need for the rise in the money supply - which slowed down in Q1 - and, consequently, the rise in bank lending to be relatively stable in 2014 and 2015.

Amid the relatively weak ruble and relatively high energy prices, the federal budget may have a surplus in 2014. The government currently predicts a budget surplus equal to 0.5% of GDP. The budget was earlier expected to have a deficit amounting to 0.5% of GDP. The same factors, as well as the impact of the instability in the region and the central bank’s tight policy on domestic demand, should contribute to the strengthening of the country’s balance of payments.

The country’s economic indicators for 2014 will be determined by a number of factors, with one of the most important of them being the dynamics of fixed capital investment and finished goods inventories.

Tensions in the region and the current tightening of the central bank’s policy continue to be factors deterring recovery.

The rise in prices remains heightened until the end of the spring.

The central bank reduced the degree of control over the ruble’s exchange rate and intends to complete a transition to a flexible exchange rate system in accordance with approved plans.

The federal budget may have a surplus in 2014.

The relatively weak ruble and relatively high energy prices should contribute to the strengthening of the balance of payments.
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 – Q1 2008 = 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: Unbalanced GDP growth, deterioration in external sustainability and acceleration in inflation

Tajikistan’s GDP growth slowed down in Q1 2014 under the influence of a growth slowdown in Russia, and an unfavorable international price situation for cotton and aluminum, the country’s main export items. However, the annual GDP growth rate remained high at 7%. In particular, Q1 2014 saw high year-on-year growth rates in retail trade (13.1%), the construction sector (13.6%) and the agricultural sector (13.6%). This reflected a relatively robust domestic consumer and investment demand –due to a 38.1% increase in fixed capital investment – and an improvement in the state of livestock farming. An improvement took place in the industrial sector with output increasing by 3.6% in Q1 2014. This was a positive sign attributable to a high growth rate in the extractive industry and growth acceleration in many branches of the manufacturing industry. It offset a decrease of 27.6% in the metallurgical industry’s output and a 33.6% slump in textile output.

The state of the foreign trade balance deteriorated significantly in Q1 2014. The trade deficit increased to $699.8 million from $476.3 million in Q1 2013 because aluminum exports (about 70% of total exports) sharply decreased in terms of both value and volume. As a result, all exports fell by 37.1% year-on-year, while imports continued to rise at a high rate, increasing by 10.7%. The stability of the somoni was affected by: the expansion of the foreign trade deficit, in the context of the depreciation of the national currencies in neighboring countries; the large volume of short-term debts on foreign loans; and a slowdown in the rise in cash remittances from abroad. This forced the National Bank to make interventions to slow down the fall in the somoni’s exchange rate. It led to an additional reduction in the already small gross international reserves that was equivalent to 1.5 months worth of imports as of the end of 2013.

The state of public finances deteriorated in Q1 2014 despite an improvement in tax administration, and a consequent 11.6% year-on-year increase in tax revenue amid continued strong GDP growth. The seasonal budget surplus decreased a little to 6.2% of GDP from 8% of GDP in Q1 2013 because spending growth accelerated to 17% and outpaced the rise in revenue. This was apparently attributable to an increase in capital expenditure amid the need to keep social spending high.

Annual inflation accelerated to 4.9% at the end of Q1 2014 with higher annual growth rates of prices of services (5.4%) and food (4.3%). The annual rise in prices of non-food goods continued to slow, falling to 5.4%. Monetary factors had a limited but positive effect on inflation. The money supply continued to grow at a high rate (21.8%) due to the alarmingly high growth rate of bank lending (39.8%). A positive sign was a slight improvement in the quality of loans. The share of outstanding loans decreased from 9.6 to 9.2% as of the end of March. The average ROA (return on assets) rate of banks was 1.1% at the end of Q1 2014 compared with 0.7% at the end of 2013, while the ROE (return on equity) rate increased to 6.5% from 3.7%.
Outlook

Tajikistan: Slowdown in economic activity in context of limited instruments of monetary policy

The economic results of May 2014 suggest that Tajikistan’s GDP growth may slow to a rate below 7% due to: a fall in investment activity; a slight slowdown in the growth of consumption despite a significant rise in household disposable income; and heightened uncertainty in the external environment in April and May 2014. As a result, May saw a simultaneous deterioration in the growth indicators of the trade, services, agricultural and industrial sectors. A consensus forecast predicts the country’s GDP to grow by 6.2% in 2014, whereas the government expects 7.5% growth. Nonetheless, uncertainty regarding economic trends has increased substantially. On the one hand, this is due to the slowdown in economic growth in Russia, which is the main source of cash remittances and an important trading partner. On the other hand, Tajikistan’s transport and energy dependence on Uzbekistan is an aggravating circumstance considering the complicated relations with that country.

Tajikistan’s trade deficit increased by $427.1 million (40%) in January-May 2014 compared with the same period in 2013. A negative effect on the stability of the somoni is the expansion of the trade deficit, in the context of the small amount of the gross international reserves and the slowdown in the rise in remittances from Russia. The somoni keeps depreciating despite the fact that national currencies in the CIS region have started to show a strengthening trend. Although there are other factors supporting external sustainability, the somoni may undergo a more significant correction, especially in view of the existing gap between the official and the market exchange rate.

Since the growth of public expenditure is expected to slow down and revenues are expected to continue to rise at quite a high rate, the state of public finances will remain stable. Public finances will certainly be exposed to risks stemming from the growth slowdown in Russia, the possible slowdown in the rise in remittances from abroad, and a limited decline in economic activity. The current annual inflation rate of 6.6% is acceptable to Tajikistan. However, the National Bank has shown an intention to tighten its monetary policy. This is despite the weakening monetary factors – money growth slowed to 16.3% as of the end of April 2014 – and the key role of the world prices of petroleum products and food.

Amid the heightened uncertainty of the external environment, the leadership of the country may face difficulties in choosing appropriate tools of macroeconomic policy for stimulating domestic demand, which tends to decline. The use of monetary policy is undesirable – from the standpoint of both inflation and the stability of the somoni’s exchange rate – whereas the potential of budgetary and tax policies remains extremely limited. Given these circumstances, there is a high degree of probability that the leadership of the country will be inclined to use the old quasi-fiscal methods of financing the economy and continue to directly order commercial banks to provide loans to finance specific projects.
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 – Q1 2008 = 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
Turkmenistan: Double-digit GDP growth amid modest improvement in exports

Turkmenistan’s GDP growth remained strong in Q1 2014 with an annual rate of 10.3% against 9.2% in Q1 2013. The growth was fueled by: a strong rise of 8.1% in fixed investment (38.7% of GDP) resulting from the implementation of ambitious government projects in almost all sectors of the economy; a significant rise in pay (+12% for large and medium-sized companies) within the framework of government programs aimed at steadily improving social and living standards; large volumes of incoming foreign investment (including Chinese investment in the country’s fuel and power industry); and an improvement in exports.

Amid high growth rates in various branches of the non-hydrocarbon sector, there was an improvement in the indicators of the fuel and power industry. The construction sector continued to have annual growth rates above 18.8% in Q1 2014, which had a favorable effect on the building materials industry. In particular, cement output increased by 33.9%, bitumen by 21% and non-metallic building materials by 34.1%. Due to robust domestic demand, retail sales increased by 18.7%. The transport sector had a growth of 7.8%. Many priority branches of the industrial sector also had high growth rates. There was an 11% year-on-year increase in the chemical industry’s output and an 18.3% increase in textile output. Q1 2014 saw growth rates rise in many branches of the fuel and power industry. In particular, electricity output increased by 16.2%, gas production by 6.9%, oil refining by 0.9%, gasoline by 2.5% and liquefied hydrocarbon gas by 3.3%. The agricultural sector’s output growth remained modest.

The country’s exports increased by 1.2% in Q1 2014, with natural gas, crude oil and petroleum products accounting for 90% of the total amount. This increase can be viewed as a positive sign, considering the fact that exports fell in 2013. Although the government took comprehensive measures to expand transport routes for gas exports and increase gas production, the rise in exports was still modest - especially considering the accelerating growth in imports, which increased by 16.2% in Q1 2014. Nonetheless, Turkmenistan should continue to have an export surplus. The high growth rate of imports is largely caused by investment demand, which will eventually have a positive effect on the economy in general in the medium term.

Since Turkmenistan’s fiscal revenue depends heavily on exports, the improvement in exports led to a rise in fiscal revenue. It increased by 2.9% year-on-year and exceeded the target by 12.7%. Given the fact that total expenditure was 3.2% less than projected, one can predict that the state budget will have a surplus in 2014. Moreover, the growing buffer reserves in the stabilisation fund continue to protect fiscal and external sustainability from the possible volatility of the prices of exported hydrocarbons. Together with the international reserves, they ensure the stability of the manat’s exchange rate. As for inflation, according to government statistical data, the all-item consumer price index fell by 0.3% compared with December 2013.

GDP growth remains strong in Q1 2014 with an annual rate of 10.3% against 9.2% in Q1 2013

Fixed capital investment grows by 8.1% to amount to 38.7% of GDP

Increased exports lead to a rise in fiscal revenue, which grows by 2.9% year-on-year and exceed the target by 12.7%
Turkmenistan

Figure 10.1. **GDP**: GDP growth (in %, year-on-year)

Source: national agencies

![GDP Growth Chart](chart1)

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

Source: ADB

![Foreign Trade Chart](chart2)

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

Source: national agencies

![Government Sector Chart](chart3)

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

![Monetary Sector Chart](chart4)

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

![Economic Growth Chart](chart5)

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

![Savings and Investments Chart](chart6)
Trends and outlook

Uzbekistan: High GDP growth rate amid moderate improvement in indicators for foreign trade

Uzbekistan's GDP growth was relatively balanced in Q1 2014 and remained strong at 7.5% in annual terms against 7.5% in Q1 2013. The high growth rate was attributable to: strong growth in investment, which increased by 10.1% year-on-year; and a 12.8% rise in the population's real income due to the implementation of procyclical macroeconomic policy, with public spending growing by 37.9% in real terms. Uzbekistan's economic growth was also fueled by: a rise in foreign direct investment, which totaled $525 million, up 70% on Q1 2013; a 31.2% rise in bank lending; and increased remittances from abroad.

The output of consumer goods increased by 12.8% due to measures taken to: diversify the industrial sector, and increase its competitiveness; stimulate domestic demand; and supply the internal market with competitive domestically manufactured goods. The share of consumer goods in industrial output grew to 34.4% compared with 29.5% in Q1 2013. Labor productivity in the industrial sector rose by 7.2%. Product costs were reduced by 8.8% on average, while the energy intensity of GDP decreased by 15%. As a result, high growth rates were achieved in the industrial sector (8.9%), the construction sector (15.5%), the agricultural sector (6.2%), trade (14.3%) and the services sector (9.1%).

Measures taken by the government to increase the competitiveness of the industrial sector’s branches and expand the output and range of export products helped increase exports by 8.4% in Q1 2014. This was despite an unfavorable international price situation for Uzbekistan's major export items (mineral fertilizers, liquefied gas, metal products and finished textile goods). The growth in imports was more modest at 7.5%. In the context of the high GDP growth rate, this was attributable to existing administrative restrictions, and the expansion of a government program aimed at increasing the share of domestically made components in finished products. According to government data, the effect of import substitution in Q1 2014 was estimated at $197.9 million.

The growth in export revenue and the high GDP growth rate led to a state budget surplus in Q1 2014 of 0.3% of GDP. State budget revenue amounted to 35% of GDP, whereas expenditure was equal to 34.7% of GDP. Major factors behind the increase in state budget revenue amid a reduction in the tax burden included the expansion of the tax base and improved tax collection. Public expenditure on social programs and social support for the population made up 58.5% of all spending. The government has projected the state budget to have a deficit equal to 1% of GDP. Revenue is expected to amount to 23.2% of GDP and expenditure is projected to amount to 24.2% of GDP.

According to official statements, in Q1 the annual inflation rate did not exceed the target level of 6 to 7% for 2014, but international organizations estimate the real inflation rate at 11%. Following a reduction in the refinance rate in January 2014, the inflation rate has been around 10%.
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
Ukraine’s economy experienced an appreciable downturn in the first months of 2014. The country’s GDP decreased by 1.1% year-on-year in Q1. A major contribution to the GDP fall was made by a 6.8% year-on-year decrease in industrial output. The construction sector’s output fell by 6.4%, whereas agricultural output rose by 5.9% and freight transportation rose by 2.6%. Retail sales rose by 7.7% in comparable prices. There was a significant, 18.5% growth in the financial services sector. Fixed capital investment fell by 19.1%, while exports and imports decreased by 2% and 7%, in real terms, respectively. Household consumption grew by 5.7%.

Amid the strengthening of domestic demand, the current account deficit decreased to $1.3 billion (3.8% of GDP) in Q1 2014 from $3.1 billion (8.3% of GDP) in Q1 2013. Simultaneously, a sharp fall in capital inflows into the country led to a decrease in the financial account surplus from $4 billion (10.5% of GDP) to $375 million (1.1% of GDP). The National Bank’s international reserves shrank from $20.4 billion (the equivalent of 2.4 months worth of imports) at the end of 2013 to $15.1 billion (1.9 months worth of imports) at the end of March. The decrease mostly occurred in January and February, when the reserves diminished from $20.4 billion to $15.5 billion.

After the hryvnia ceased to be tightly pegged to the US dollar, the pace of the fall in the international reserves slowed down for a while. The hryvnia depreciated by 35% against the dollar in Q1 2014.

The National Bank’s monetary policy was loose throughout Q1 2014. The annual growth rate of M0 was 30.3% as of the end of Q1 2014 compared with 17% at the end of 2013. However, due to a significant slowdown in the growth in bank deposits amid fears of banking sector instability, this acceleration had no impact on growth in the broader money aggregates. The annual growth rate of M2 was 17.7% at the end of Q1 2014, slightly up from 17.5% in December 2013. Nonetheless, the sharp depreciation of the national currency led to acceleration in inflation. The annual consumer price index was 3.4% in March 2014, up from 0.5% in December 2013.

The consolidated budget had a surplus equal to 0.16% of GDP in Q1 2014 against a deficit amounting to 1.9% of GDP in Q1 2013. The only factor behind this improvement was a marked rise in the transfers made by the National Bank to the budget, which increased from 1.3 to 5% of GDP. Other budget revenues, on the contrary, fell by 3.2% of GDP compared with Q1 2013. Consolidated budget expenditures also decreased, but the decrease was less significant at 1.4% of GDP.

The annual growth rate of bank lending rose dramatically in February and March, reaching 21.2% at the end of Q1 2014 compared with 11.7% at the end of 2013. The banking sector’s sustainability indicators deteriorated in general. In particular, the regulatory capital adequacy ratio fell to 14.8% as of the end of Q1 2014 from 18.3% at the end of 2013, while the share of problem loans grew from 12.9% to 13.3% during the period.
Ukraine: Need for further systemic measures for achieving macroeconomic stability

The dynamics of economic activity in Ukraine throughout the remaining part of 2014 will apparently be determined by the further consolidation of domestic demand. This will eventually end with the restoration of sustainability in the balance of payments and the public finances of Ukraine. In Q1 2014 this process primarily had an impact on investment and, to a lesser extent, on government consumption expenditure. House hold consumption continued to show positive annual growth rates, which were supported by continued growth in average pay (a rise of 3.5% in Q1 2014 in real terms). Household consumption will probably experience some decline amid a decrease in real wages due to higher inflation and unemployment. Ukraine’s GDP may fall by 5 to 10% in 2014. The extent of the GDP decline will depend on, among other factors, the dynamics of exports, which will most likely experience a downturn in the remaining part of 2014 due to the probable decline in agricultural exports. Also, there is high uncertainty with regard to the impact that the instability in the country’s relations with trading partners has on exports.

Inflation continued to accelerate after Q1 2014. The annual consumer price index reached 10.9% at the end of May. The depreciation of the hryvnia slowed down in May after the disbursement of the first tranche of the IMF’s financial assistance program made it possible to increase the National Bank’s international reserves to $17.9 billion (the equivalent of about 2.3 months worth of imports of goods and services). The exchange rate of the national currency stabilized at about 12 hryvnia for one US dollar. The National Bank seems to be returning to the fixed exchange rate policy that was pursued between 2010 and 2013 amid a much looser monetary policy and a poorer state of the budget.

The balance of payments of Ukraine improved in Q1 2014, but the external sustainability of the country’s economy may be exposed to new risks throughout the remaining part of 2014. The balance of payments may be negatively affected by an increase in spending on energy imports and a further decline in exports (for reasons stated above). The balance of payments will also be affected by the resumed appreciation of the real effective exchange rate in the context of fixing the hryvnia at a new level, and the substantial acceleration in inflation. The normalization of monetary and fiscal policies amid a reduction in the monetization of the budget deficit would be essential for the strengthening of the positive trends that were seen in the external sustainability of the economy in the first months of 2014.

The general economic situation in the country remains fragile. There are still serious risks with regard to both the prospects for a resumption of GDP growth and the sustainability of the balance of payments. The reestablishment of stability requires strong concerted measures in the field of monetary and fiscal policies. With the exception of the replenishment of the international reserves with the help of the IMF loan and some measures in the field of energy policy, the government had not begun to carry out these measures as of the start of summer 2014.
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 – Q1 2008 = 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