Macroeconomics of the region

Macroeconomics of countries:

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- Armenia: 8-10
- Belarus: 11-13
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- Kyrgyzstan: 17-19
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Trends:

- The world economy: a decline in risks
- The United States: a recovery in activity
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- Asia: signs of recovery in the Japanese economy, an uncertain situation in the Chinese economy
- The CIS:
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- The world economy: continuing gradual recovery in the growth rate
- Commodity markets: a recovery in demand for raw materials
- Developed economies: a recovery in growth amid continued risks from the debt crisis and a decline in the intensity of monetary stimulation
- Developing economies: an improvement in the external environment, a slowdown in the long-term growth trend
- The CIS: growth acceleration due to a general improvement in the world economic situation; risks from continued dependence on the level of prices for raw materials

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Vladimir Yasinskiy, Managing Director for Analytics

The report was prepared by the country analysis unit:

Elvira Kurmanalieva (kes@eabr.org) – Macroeconomics of the Region, Kyrgyzstan, Moldova, Tajikistan
Konstantin Fedorov (fks@eabr.org) – Azerbaijan, Belarus, Russia, Ukraine
Arman Ahunbaev (ama@eabr.org) – Armenia, Kazakhstan, Turkmenistan, Uzbekistan
Macroeconomics of the region

At the beginning of 2013, risks in the global economy slightly diminished after the central banks of leading countries adopted monetary policy stimulus packages, and banking systems continued the deleveraging process. The state of developed economies in general improved: their industrial production showed growth for the first time since Q1 2012. This positive trend produced an immediate effect on global supply chains: the annual growth of world trade accelerated to 1.6% in Q1 2013 comparing to 1.4% in Q4 2012. Nonetheless the previous year’s weak external demand continued to affect developing economies, whose growth figures turned out to be lower than the figures for Q4 2012. Despite that fact Q1 2013 saw a rise in prices for many raw materials. The price of Brent crude averaged out at $112.9 per barrel, increasing by 2.2% compared with Q4 2012. However, oil prices fell compared to the beginning of 2012.

CIS economies were not an exception from developing world. An important feature of Q1 2013 for the CIS economies was a decline in industrial output, which fell by 0.2%. This decline led to a slowdown in the year-on-year aggregate GDP growth of the CIS member countries to 1.7% from 4.6% in Q1 2012. A decline in industrial output occurred in Azerbaijan (-1.8%), Belarus (-1.1%) and Ukraine (-5%). At the same time, favorable conditions amid the poor results of 2012 led to positive trends in the agricultural sector. The weighted average growth rate in agricultural output in the CIS was 2.4%. The main drivers of GDP growth were retail trade and the services sector, which showed a 5.9% growth in Q1 2013. This testifies to high consumer activity in the region. The growth in fixed capital expenditure continued to slow down: its annual growth rate was 1.7% in Q1 2013 compared with 14.7% in Q1 2012.

The economies of the EDB member countries in general showed higher growth rates than the other CIS countries: they had a GDP growth rate of 2%, the same level as Q4 2012. The difference between these two groups of countries is largely attributable to a marked decline in economic activity in Ukraine, whose GDP in Q1 2013 was 1.1% lower than its GDP in Q1 2012.

Figure 1.1. World industrial production and trade (%), year-on-year

Source: CPB World Trade Monitor, World Bank

Figure 1.2. CIS countries’ GDP growth (in %, year-on-year)

Source: national agencies and the CIS Statistics Committee
Prices of raw materials rise compared with Q4 2012 but are still lower than Q1 2012

Exports decrease in almost all CIS countries, while imports increase amid a rise in consumption

Amid a financial account surplus, CIS central banks’ reserves grow by $9 billion in Q1 2013

A decline in the risk of a disturbance to the stability of the world economy helped prices of many commodity products return to positive growth rates in Q1 2013. Prices for oil, natural gas, cotton, copper and iron ore rose compared with Q4 2012. Food prices in Q1 2013 fell by 2.8%, with a fall occurring for almost all categories of food. In annual terms, the growth in prices for crude oil, cotton, aluminum, copper and gold remained negative.

Exports decreased in almost all CIS countries except for Moldova. At the same time, the trade balances of the CIS countries (as a percentage of GDP), and also current account balances showed a better result compared with 2012 due to a lower denominator (GDP). The oil and gas exporting countries – Azerbaijan, Kazakhstan and Russia – had trade surpluses equal to 6% of GDP. A decrease occurred in the current account deficit of Ukraine, which suggests some easing of economic distress. The trade balances of the labor exporting countries – Armenia, Kyrgyzstan, Moldova and Tajikistan – on the contrary deteriorated as a result of high domestic demand. Nonetheless, a continuing steady rise in cash remittances from migrant workers helped those economies slightly improve their trade balances.

Many economies in the region had financial and capital account surpluses, which is attributable to a decrease in the outflow of portfolio investment and other short-term capital, as well as a rise in external borrowings. The aggregate external debt of the CIS countries grew in nominal terms by 6% of the region’s GDP in Q1 2013, with the greater part of this increase being due to borrowings by Russia, whose gross external debt amounted to 31.5% of GDP.

Amid these trends, the international reserves of the central banks grew by $9 billion in Q1 2013, thereby increasing the “safety cushion” of the region. The national currencies of CIS countries, except for the Kazakhstani tenge, Kyrgyzstani som and Ukrainian hryvnia, strengthened in real terms.

Figure 1.3. Terms of trade: international commodities’ prices

Figure 1.4. Balance of payments: current account balances’ components and foreign exchange reserves

Source: World Bank

Source: Central Bank of the Russian Federation (CB RF), national agencies
Less favorable trade conditions lead to budget implementation difficulties

The low growth rates of export prices, the decrease in real exports and the low economic activity in the oil and gas exporting countries had a negative impact on their state budget revenue. In some cases, this caused difficulties for government budgets’ implementation. In Russia, this led to a lower surplus in the consolidated budget; while in Kazakhstan, there was underfunding of some expenditure items. In the labor exporting countries the relatively higher economic growth rates led to an increase in tax revenue, and their aggregate budget balances turned out to be positive for the first time in several years. In some economies, certain spending was postponed to the last months of the fiscal year. Deterioration in the state budget balances in the countries of the third group was largely due to an increase in public expenditure in Ukraine.

Amid difficulties in budget implementation, there was a rise in the public external debt of Russia and Kyrgyzstan. Russia’s public external debt grew to 3.5% of GDP and Kyrgyzstan’s exceeded 50% of GDP. Amid the lack of changes in key interest rates, the annual inflation rates in most countries of the CIS region continued to be at levels slightly higher than those for Q4 2012. The weighted average annual growth rate of consumer prices rose from 6.2% in Q4 2012 to 6.8% in Q1 2013. The downward pressure on prices was created by a decline in world food prices and by low economic activity in the region. The prices were influenced by: current increases in government-regulated services; the low base of 2012; and a weakening of monetary policy that took place in some countries in 2012.

The banking systems of the CIS countries retained sufficient sustainability despite some deterioration in the profitability figures and quality of assets in Armenian banks. The growth rates of bank lending remained stable throughout Q1 2013. A rise in lending activity occurred in Belarus, Russia, Tajikistan and Ukraine.
Weak economic activity and a slow recovery in industrial production in the first months of 2013 prompted many national and international institutions to revise downward their forecasts of economic growth. The weighted average forecast for CIS economic growth for 2013 fell from 4% at the beginning of 2013 to 2.8% in June. The most significant decreases in consensus forecasts were for growth in the largest economies of the region (Belarus, Kazakhstan, Russia and Ukraine). The current Eurasian Development Bank (EDB) forecast predicts a growth of 3.3% in 2013 and acceleration to 4% in 2014. We assume that the CIS economic growth was below its potential in 2012 and the first half of 2013. If there are no significant negative external or domestic shocks, the economy of the CIS region will return to its post-crisis, 2011-2012 level of growth in the second half of 2013 under the influence of stimulus domestic measures and the improving external conditions.

The most-discussed external economic risk is the expected tapering of the US Federal Reserve System’s stimulus program; which, as many experts expect, should increase the cost of borrowing and lead to an outflow of capital from developing markets. The gradual recovery in the US economy indicates that monetary stimulus measures may be winding down. At the same time there are grounds to expect that changes in the policy of the Federal Reserve System will not be so radical and unexpected. In particular, the current cuts in public spending will prevent the United States from sharply tightening monetary policy. We expect the largest economies in the Eurozone to return to positive growth rates as early as 2013. The accommodative monetary policy of the European Central Bank and other central banks will contribute to recovery in Europe. The slowdown in China’s economic growth, and the uncertain situation regarding bank lending in China is another threat to the stability of the global economy. Nonetheless, we still expect that the positive developments in the European and US economies, and also China’s own stimulus measures, will contribute to the stability of the Chinese economy’s growth. International energy prices will, to all appearances, fluctuate around their current levels. According to forecasts from the World Bank, further decline in world food prices can be expected. This would lead to continued low inflation rates in both the world and the region.
**Trends and outlook**

**Azerbaijan: Growth acceleration in non-oil and gas sector, deterioration in budget position, and balance of payments**

Azerbaijan’s GDP increased by 3.1% in Q1 2013, compared with an increase of 2.2% in 2012. The value-added share produced by the oil and gas sector decreased by 4% compared with Q1 2012 due to a natural decline in the potential of the country’s fields. This decline has gradually slowed: oil and gas production decreased by 10.2% in 2011 and 5.1% in 2012. At the same time the non-oil and gas GDP increased by 11.4%, with increases of: 10.4% in the manufacturing industry; 50% in construction; 9.5% in the trade sector; and 4.4% in the agricultural sector. An extraordinarily high rise was shown by fixed capital expenditure, which grew by 36.1%. The population’s real per-capita income rose by 4.5% and real pay by 7.8%.

State budget expenditure in Q1 2013 amounted to 34.9% of GDP, a noticeable increase compared with 23.1% in Q1 2012. The state budget surplus decreased to 1.2% of GDP from 5.2% in Q1 2012. The 2013 budget implies a significant rise in both current expenditure – which, according to the IMF forecast, is to increase by 13% in nominal terms due to rises in the pay of public employees, state purchases and social spending – and expenditure of an investment nature, which is to rise by 20%. The size of the State Oil Fund of Azerbaijan currently amounts to $34.1 billion, or 50% of the nation’s GDP in 2012.

Inflation returned to positive rates in Q1 2013: consumer prices rose by 1.2% in the period after a rate of minus 0.3% in December 2012. The low rise in prices took place amid a de facto fixed exchange rate of the national currency against the US dollar – the manat’s value has varied between $0.78 and $0.79 since mid-2011 – and a slowing money supply growth: the M2 annual increase stood at 22.6% in March 2013 compared with 34.6% in June 2012.

Azerbaijan’s balance of payments slightly deteriorated due to the expansion of public expenditure and lower oil and gas prices: the current account surplus amounted to $4 billion (24.5% of GDP) in Q1 2013 against $4.6 billion (27.9% of GDP) in Q1 2012.

The annual growth rate of bank lending rose to 24.3% in March 2013 compared with 22.1% in December 2012. The sustainability indicators of the banking sector slightly deteriorated compared with the end of 2012. The share of liquid assets in total assets decreased from 15 to 14%, while the ratio of regulatory capital to assets remained at 16.8%.

To conclude, there has been accelerating growth in the non-oil and gas sector of the Azerbaijani economy, which is fuelled by the expansion of public expenditure. This is accompanied by a significant weakening of the nation’s fiscal and external positions.
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**: state budget (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: High GDP growth amid deterioration in balance of payments

Armenia’s GDP growth accelerated to 7.5% in Q1 2013. The pronounced upward trend in economic activity was due to the following factors: the high growth rate in the industrial sector, which was caused by the processing of larger volumes of agricultural production due to a high crop yield in 2012, and an increase in metal ore production and the output of base metals; the relatively robust domestic demand stimulated by migrants’ remittances, which rose by 8.7% compared with Q1 2012; a 24.6% rise in bank lending; and, partially, by an 8% increase in public spending. As a result, good positive trends were shown by almost all branches of the industrial sector, except paradoxically for electric power generation. There was a 6.7% output rise in the manufacturing industry, a 5.9% rise in the mining industry, and an 18.3% rise in the water supply industry. The services sector showed a high growth rate with increases of: 33.2% in health and social services; 16.9% in the telecommunications sector; and an 11.4% in the real estate sector. The trade turnover’s growth rate remained at a modest 3.3%. Agricultural output increased by 2.4%, while the decline in the construction sector increased to 14.8%.

Despite growth in the export-oriented sectors of the national economy, Armenia’s indicators of external economic activity deteriorated amid the recession in the Eurozone and a slowdown in economic growth in Russia. The external vulnerability manifested itself in: a decrease in the gross international reserves, which shrank by 9.4% in Q1 2013 and by 4.8% compared with March 2012; and the depreciation of the dram, which lost 2.2% of value since the beginning of 2013 and 6.6% since March 2012. A foreign-exchange shortage in the highly dollarized Armenian economy was principally caused by contracting capital and financial account surplus due to, among other things, an 11.9% decrease in foreign investment, including a 35.4% fall in direct investment. Taking into account the improvement in the basic items of the current account balance, its deficit should have decreased. Despite a 7.5% fall in copper prices in annual terms and weaker external demand, the trade deficit decreased due to a 14.3% rise in exports amid a lower, 2% rise in imports. At the same time migrants’ remittances grew by 8.7% year-on-year.

The high GDP growth, improved tax administration, and the budget consolidation measures had a favorable effect on the fiscal sector. State budget revenue grew by 23.4% in annual terms. Due to the failure to implement spending plans, expenditure grew by only 8% and therefore the state budget had a surplus of 2.5% of GDP.

In Q1 2013, the annual inflation rate rose to 3.4% against 2.2% in March 2012. This was partly due to the low-base effect and the still-high growth rate of money supply – M2X increased by 20.2% in annual terms, but remained within the central bank’s target band of 2.5 to 5.5%. Some indicators of the banking sector deteriorated, but it generally remained sustainable. In particular, the average ROA (return on assets) rate of commercial banks fell to 1.37%, and the rate of return to equity (ROE) decreased to 8.23%. At the same time, the share of non-performing loans remained stable at 5.6% and the capital adequacy ratio was 16.4%, with the required minimum being 12%.
Armenia: Slowdown in GDP growth and deterioration in macroeconomic indicators

Armenia’s Indicator of Economic Activity (IEA) slowed sharply in April and then contracted by -1.3% in May 2013. This deterioration was due to: a decline in domestic and external demand; and a possible fall in the volume of processed agricultural products, which was previously high due to a good crop yield in 2012. Industrial output decreased by 7.4% in May 2013 in annual terms. The weaker domestic demand manifested by growth slowing to 0.5% in trade turnover and to 1.1% in the services sector, and also by a 7.6% decrease in imports. Agricultural output fell by 2.3% and the drop in the construction sector increased to 15.9%. As a result, the IEA was up 5.3% in January-May 2013.

The deterioration in the IEA was predictable and indicates a slowdown in GDP growth in 2013. It was due to: the recession in the Eurozone; growth deceleration in Russia; a fall in agricultural output; low investment activity; a slowdown in lending growth; and the apparently temporary nature of the high growth rate of the industrial sector. Given the limited space for economic policy in Armenia, the national economy remains vulnerable to changes in the external environment and weather conditions. Therefore the GDP growth is expected to slow down in 2013.

According to a revised consensus forecast, GDP growth will slow down to 5% in 2013.

The expected deterioration in the balance of payments will contribute to the instability of the dram and necessitate additional external borrowings.

The state budget deficit should not exceed the projected level of 2.6% of GDP.

Inflation may accelerate to at least 5.5% in 2013.

Export revenues will be affected by: the slowdown in GDP growth; an output decline in the export-oriented branches of the industrial sector; and the expected low output in the agricultural sector. The economy has a high sensitivity to any depreciation of the national currency, and to the contracting capital and financial account surpluses. This will lead to a deterioration in the balance of payments, contribute to the instability of the dram – despite the still sufficient level of the gross international reserves – and necessitate additional external borrowings.

The state of public finance will deteriorate but remain stable. The slowdown in economic activity and the decrease in export receipts will limit the growth of fiscal revenues. In addition, 2013 is the peak year for payments on external debt, which should exceed $400 million, 50% more than 2012. If budget expenditure will be fully implemented as projected by the government, the state budget will return to a deficit position. If the government signs a new program with the IMF in 2013, the deficit will apparently remain within controllable limits and should not exceed the projected level of 2.6% of GDP.

Given the expected downward trends in GDP growth, lending and money supply growth, the inflation rate should be moderate. However, inflation may accelerate to at least the upper projected level of 5.5% in 2013, as a result of the increased price of Russian natural gas, a likely increase in housing and utilities prices, and the effect of unfavorable weather conditions (hail) for agriculture.
Armenia

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

![GDP and output chart]

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)

![Foreign trade chart]

Source: national agencies, IMF

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

![Government sector chart]

Source: national agencies

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

![Monetary sector chart]

Source: national agencies

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

![Economic growth chart]

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

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

![Savings and investments chart]

Source: estimates and forecasts by national agencies and the IMF
Belarus: Slow growth, continued external imbalance

Belarus’ GDP growth accelerated to 3.5% year-on-year in Q1 2013 from minus 1.5% in Q4 2012 and 1.5% in 2012 as a whole. The recovery of activity was concentrated in retail trade, with retail sales increasing by 18.7%, and fixed capital expenditure, which rose by 12.5%. The high growth rates were largely due to the low-base effect. A factor determining the rise in sales was an increase in average pay, which regained the target $500 monthly level announced by the government before the 2011 crisis. At the same time, industrial output decreased by 1.1% and agricultural output rose by 2.5%.

Inflation remained at the level of the last months of 2012. The annual inflation rate was 22.2% in March compared with 21.8% in December. The National Bank of Belarus (NBB) kept its base refinance rate unchanged throughout the greater part of Q1 2013 amid a slowdown in the growth of bank lending to 2% a month, this compared with an average monthly increase of 3.7% in the second half of 2012. In March 2013, the NBB lowered the refinance rate from 30 to 28.5%, which was followed by three further reductions in the period between April and early June.

The fiscal situation remained stable. In Q1 2013, the national budget had a surplus of 800 billion Belarusian rubles (0.6% of GDP). The surplus was lower than it was in Q1 2012, when it amounted to 2.4% of GDP. However, the extremely high inflation in 2012 made it significantly easier for the authorities to finance the budget.

Meanwhile, the state of the nation’s balance of payments continued to deteriorate. The current account deficit in Q1 2013 amounted to $2.4 billion, or 17.1% of GDP. The main cause of the deterioration was significant income payments on foreign investment during the period. The fact that those payments were not taken out of the country made it possible to preserve the external sustainability of the economy throughout Q1 2013. The trade balance experienced a certain improvement. The nation had an export surplus of some $380 million, or 2.7% of GDP, mainly due to seasonal factors such as lower imports of oil and gas.

The sustainability of the banking system deteriorated in Q1 2013, but this deterioration was not significant. The ratio of risk-weighted assets to regulatory capital fell to 21% by the end of the period from about 22% at the end of 2012. The share of liquid assets in total assets was 27.8% at the end of March compared with over 30% throughout the greater part of 2012. The share of problem loans almost did not change compared with Q4 2012, standing at slightly more than 5%, whereas it did not generally exceed 4% throughout the first three quarters of 2012.
Outlook
Belarus: Inflation slowdown, improvement in balance of payments

The main economic tasks confronting the Belarusian government has not changed in general since the beginning of 2013: the nation needs to strengthen the balance of payments, and reduce inflation. These tasks remain interrelated because a loss of stability in the foreign exchange market, which could be caused by external imbalance, would lead to deterioration in the inflation situation. On the other hand, the rise in prices amid the National Bank’s rigid control over the ruble’s exchange rate leads to its strengthening in real terms, which negatively affects the balance of payments.

Meanwhile, since the beginning of 2013, the government has made certain progress in combating inflation: the monthly inflation rate, which averaged 1.8% in Q1 2013, fell to levels below 1% in April and May. The annual inflation rate can currently be expected to go down to 15% by the end of 2013 if the National Bank does not lower the refinancing rate to an extent that exceeds the decline in inflation, and if the government continues a tight budgetary policy, including its quasi-fiscal component.

The situation regarding the external balance remains worrying. The sustainability of the external balance strongly depends on factors that are difficult to control, such as foreign investors’ willingness to reinvest their income within the country. The international reserves have been slightly more than $8 billion – an amount equal to less than three months’ imports of goods – since the spring of 2012. Given the size of the external imbalance, this level of reserves is not sufficient.

Budgetary policy in the narrow sense of the word is not currently a source of risk for the national economy. The government plans to have a zero budget deficit in 2013. The implementation of the budget in the first months of 2013 suggests that the objective may be reached. Quasi-fiscal financing also remains under control. Taking into account quasi-fiscal financing, we estimate that the consolidated budget will have a deficit equal to 1.2% of GDP. Of greater concern is the government’s policy aimed at raising the level of pay in the country, especially as the Belorussian authorities exert significant influence on the level of wages outside the public sector. The rise in average pay has already exceeded its dollar-equivalent level that existed before the 2011 crisis. It is one of the main factors affecting the nation’s balance of payments in a negative way.

Belarus’ economic growth slowed down, after a rise in Q1 2013, as GDP grew by only 1.1% year-on-year in January-May 2013. Most of the branches of the industrial sector currently have negative growth rates. The oil refining and the chemical industry had the most significant year-on-year output decreases in the first five months of 2013 with 19.8 and 43.2%, respectively.

Belarus can be expected to have moderate GDP growth rates throughout the latter half of 2013 and in 2014 amid a general improvement in the situation in the region. However the unsolved problem of the external imbalance will continue to have a negative impact on economic growth in the medium run.
Belarus

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

![GDP and output graph](image)

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)

![Foreign trade graph](image)

Source: national agencies, IMF

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

![Government sector graph](image)

Source: national agencies

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

![Monetary sector graph](image)

Source: national agencies, IMF (IFS)

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

![Economic growth graph](image)

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

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

![Savings and investments graph](image)

Source: estimates and forecasts by national agencies, the IMF and the EBD
A distinctive feature of Kazakhstan’s economy in Q1 2013 was a weakening of demand. This led to: a slowdown in GDP growth to 4.6% in annual terms against 5.6% in Q1 2012; real wages rose by only 0.9%; total public expenditure grew by only 3.3% in nominal terms; the annual growth rate of lending to the economy fell to 13.3%; and fixed capital expenditure increased by 8.5% in absolute terms and approximately 2% in real terms. The recession in the Eurozone contributed to a weakening of external demand, which manifested through a fall in the price of exported crude oil and metals. As a result, the manufacturing sector experienced a slowdown in growth to 1.6%. This offset a recovery in the extractive industry, which showed a 2.7% output increase; and it contributed to a slowdown in the entire industrial sector, which had an output rise of 1.9%. Agricultural output increased by 0.4%. Despite a slight growth slowdown to 7.8%, the services sector remained the main driver of growth. The construction sector again suffered a fall with output down 4.9%.

The fall in the price of exported raw materials, the weakening of external demand and the sustained uncertainty in international markets led to a contraction of the balance of payments surplus to 0.6% of GDP from 5.3% in Q1 2012. On the one hand, the current account surplus decreased to 3.8% of GDP from 8.1% in Q1 2012 principally due to an 8% increase in imports, while exports have contracted by 7%. Deterioration of the current account balance was also contributed to by: deterioration in the services; compensation of employees; current transfers; and investment income balances. On the other hand, a decline in foreign direct investment and external borrowings in the private sector, and also the likely sustained high level of capital outflow led to a 22% increase in the capital and financial account deficit (including errors and omissions).

The slowdown in economic growth, the decrease in exports, and the fall in the price of exported raw materials also had a negative impact on the state budget revenue. An increase in the state budget surplus in Q1 2013 – 85 billion tenge against 8 billion tenge in Q1 2012, or 1.3% in GDP – can be related to a postponement of spending.

In Q1 2013, inflation accelerated to 6.8% in annual terms, compared with 5.1% in Q1 2012; but it remained within the National Bank’s target band of 6 to 8%. The inflation acceleration reflects a 12.7% annual rise in the price of services. The rise in the inflation rate was primarily due to increases in housing and utilities prices and fuel prices, which in turn led to a rise in the price of medical and educational services. The rise in the price of food and non-food consumer goods remained limited due to a minimal contribution from monetary factors, and a slowdown in the rise of import and export prices. The growth of money supply was modest at 7.6%. This is attributable to: the National Bank’s tight policy; the banking sector’s post-crisis state – the share of non-performing loans was 35.5%; and the negative impact of transactions with the external world.

A weakening of demand leads to a slowdown in GDP growth to 4.6%

Lower export prices, and weaker external demand lead to a contraction of the balance of payments surplus to 0.6% of GDP

An increase in the state budget surplus in Q1 2013 is attributable to a postponement of spending

Annual inflation rises to 6.8% in Q1 2013 from 5.1% in Q1 2012, but remains within the National Bank’s target band of 6 to 8%
Outlook

Kazakhstan: Modest recovery of GDP growth

Despite the slowdown in annual GDP growth, the quarterly dynamics suggest a slight acceleration, which offsets the unsatisfactory results of Q1 2013. According to the government’s estimation, GDP grew by 5% year-on-year in the first five months of 2013. A slight acceleration in economic activity could be seen in the industrial sector, where increases occurred in the production of crude oil, natural gas, and non-ferrous ores, and in output in many branches of the manufacturing industry. The services sector continued to show a high growth rate (12.8%). The decline in the construction sector decelerated to minus 1%. In transportation and the communications sector, the growth rates remained at the former levels of 7 and 15%, respectively. The agricultural sector had a growth rate of 1.1%. There were no obvious signs of acceleration in demand. The real money income of the population increased by only 2.3%. Inflation-adjusted investment is expected to grow by about 2% at best.

It is possible to expect acceleration in GDP growth due to: the relatively high level of oil prices and the upward trend in metal prices; the slight strengthening of external demand in connection with the probable improvement of the situation in the Eurozone; growth recovery in the construction sector; the expected growth acceleration in the agricultural sector; and the potential start of oil production in the Kashagan offshore oil field in the Caspian Sea. This is despite significant impediments to the drivers of domestic demand, which include a downward revision of the state budget, a limited money supply and the limited growth of labor productivity and wages. A revised consensus forecast, based on forecasts from the EDB, the IMF, the World Bank, the Asian Development Bank and the European Bank for Reconstruction and Development, predicts Kazakhstan’s GDP to grow by 5.2% in 2013.

Given the weaker domestic demand and consumption, the growth rate of imports should stabilize and the growth rate of exports may recover to its former level. As a result, one can expect an increase in the trade balance surplus. If there are no additional shocks, the balance of payments should remain positive. The quarterly dynamics show an improvement in the indicators for external economic activities. This is evidenced by a rise in the gross international reserves (including the resources of the National Fund of Kazakhstan), and it suggests that Kazakhstan’s economy is retaining its strong external sustainability.

Given the emergence of signs of weaker domestic demand, the slowdown in GDP growth, and the potential decrease in public revenue, the government revised the national budget downward in May 2013. In addition, the government is carrying out measures aimed at optimizing spending and increasing the efficiency of tax administration. It is also trying to find additional sources of revenue through, among other measures, raising the rate of export duty on crude oil from $40 to $60. We estimate that the state budget deficit should not exceed 2.7% of GDP in 2013 and continue to be controllable. As for inflation, the National Bank predicts that the annual inflation rate will continue to be at a satisfactory level, standing at about 6% throughout the summer months. Despite the low growth of money supply, the National Bank and the government will continue implementing an anti-inflationary policy in 2013 and will try to meet the target of 6 to 8% in order to ensure price stability.
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 budget (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 ended Q1 2013 with an annual GDP growth rate of 7.6%. If Kumtor Gold Company is not taken into account, the nation’s GDP growth accelerated compared with 2012 – from 3.7 to 4.9%. This was due to an expansion in retail trade and the services sector. The growth rate of the industrial sector (excluding Kumtor Gold Company) declined, largely due to a contraction in the textile and the food industry. The industrial sector and foreign trade were affected by: a fall in world gold prices; the remaining problems in gold production; stable domestic demand, which supported the rise in imports; structural reform in light industry’s branches; and a slowdown in trade partners’ economic growth. Despite a rapid rise in metallurgical output, the export of precious metals decreased by 24% year-on-year in Q1 2013. There was also a 35.6% fall in the export of textile products.

Kyrgyzstan ended Q1 2013 with an annual inflation of 7.8%. This was amid a fall in food prices in world commodity markets, which according to the World Bank dropped by 12.6% year-on-year in Q1 2013. There was also a steady growth rate of money supply M2, which had an annual growth rate of 19.3% in March 2013. The rise in consumer prices met the expectations of the National Bank, whose rate on short-term notes stood at 3% at the end of March. The National Bank expects a gradual weakening of inflation pressure in the latter half of 2013.

Amid positive dynamics in the economy, the state budget had a surplus equal to 5.2% of GDP due to a rise in non-tax revenue and grants, and postponed spending. Tax revenue rose along with GDP growth and their size as a percentage of GDP almost did not change. State budget expenditure rose by 0.5% in nominal terms, but all major expenditure items decreased in terms of GDP. The low level of expenditure was due to the underfinancing of unsecured expenditure items in connection with uncertainty regarding disbursement of loans and grants from international organizations. The public external debt, which amounted to 48% of GDP at the end of 2012, grew by 11% in nominal terms in Q1 2013.

According to data published by the National Bank, at the end of Q1 2013, the banking sector had satisfactory indicators for profitability and for the quality of loans. The share of classified loans (NPLs) in total loans shrank to 6.6% from 7.3% at the end of 2012; while the average ROA (return on assets) rate of banks fell to 2.3% from 3%. At the beginning of 2012, amid declining economic activity, bank lending growth varied between 18 and 22% in annual terms. Following the recovery of industrial output, the growth of standard loans (all loans except overdue ones) exceeded 30%. In addition, Q1 2013 saw a rise in overdue (postponed) loans, whose contribution to total lending growth amounted to 1.1%. As for lending growth by sectors, a significant rise occurred in loans for agriculture and the trade sector, while the share of consumer loans decreased.
**Outlook**

**Kyrgyzstan: Social tensions risk disturbing the upward growth trend in 2013, and preventing return to long-term trends in 2014 and 2015**

Despite impressive dynamics in the real sector, the National Bank of Kyrgyzstan estimates that GDP (including Kumtor Gold Company’s gold production) has not yet reached the 2011 level. The revival of the economy is impeded by a slow production recovery at the Kumtor gold mine, as well as by recurrent outbursts of social discontent. Social tensions in the country constitute a threat to further sustainable development of the economy. This uncertainty manifests itself in frequent revisions of growth forecasts by national and international experts. The government expects a GDP growth rate of 8.3% for 2013; whereas the Asian Development Bank and the European Bank for Reconstruction and Development have revised downward their forecasts to 5.5 and 6.5%, respectively, with the consensus forecast predicting a growth rate of 7.4% for 2013. Due to the low base of 2012, the metallurgical industry remains the main driver of 2013’s high economic growth. At the same time there has been a downturn in the textile and food industries.

According to the National Bank’s inflation forecast for 2013, if the acceleration of economic growth continues, and there are no internal shocks and no dramatic upward changes in world food prices, the annual change of inflation rate should be around 6% by the end of 2013. Meanwhile, inflation keeps stable - the annual inflation rate declined to 7.5% in May. The rise in prices continues to be below the level expected by the National Bank.

The projected budget deficit is still high at 5.3% of GDP. This is despite the 2013 state budget being based on conservative revenue forecasts, and including measures for restriction of non-priority capital spending, while preserving social expenditure. In Q1 2013, the rise in state budget revenue exceeded the growth of expenditure; but a peculiarity of Kyrgyzstan’s public finances is that the state budget has a surplus in the first half of the year, and the greater part of expenditure is made at the end of the calendar year. The government forecasts that the state budget deficit will be at a level equal to 4 to 5% of GDP in 2014 and 2015.

The government faces difficult medium-term tasks. The low diversification of the economy and its high vulnerability to shocks, both internal and external, calls for systemic steps toward fiscal consolidation. These should be taken consistently for both improving tax administration and streamlining state budget expenditure.

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**The consensus forecast predicts GDP to grow by 7.4% in 2013, 6.2% in 2014 and 5.4% in 2015**

**The metallurgical industry remains the main driver of growth this year**

**The National Bank expects inflation to slow to 6% by the end of 2013**

**The government predicts the state budget deficit to remain at a level of 4 to 5% of GDP**
Kyrgyzstan

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

![Chart showing GDP growth and output change by sectors.](chart)

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)

![Chart showing foreign trade and REER.](chart)

Source: national agencies

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

![Chart showing government sector.](chart)

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)

![Chart showing monetary sector.](chart)

Source: national agencies

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

![Chart showing economic growth.](chart)

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)

![Chart showing savings and investments.](chart)

Source: estimates and forecasts by national agencies, the IMF and the EBD
Trends
Moldova: Significant growth in first quarter

Following a GDP decline of 0.8% in 2012, the economy of Moldova grew at a 3.5% annual rate in Q1 2013. The main factor behind this growth was a recovery in household consumer activity and construction amid an improvement in external demand. Public expenditure continued to decline under fiscal consolidation programs. Exports rose by 10%, largely due to the increase in agricultural exports, whose share in total exports was about 40%. The food industry also made a significant contribution to the recovery in production activity. An important component of the Moldovan economy is the re-export of products with both low and zero added value including primarily textile products, machines and equipment. There was a small increase in the export and import of these products in Q1 2013. A gradual improvement in the situation in Europe and Russia makes it possible to expect a further increase in re-exports, which account for one-third of the nation’s economy. The recovery in consumer activity is evidenced by a rise in the volumes of wholesale trade and services, which increased by 5.8 and 7.1%, respectively. Moldovan consumer confidence strengthened as a result of a rise in the population’s disposable income – the per capita real income grew by 3.9% – amid stable remittance inflows from abroad, which amounted to 20% of GDP in Q1 2013. The contribution of investment to GDP remained negative. However, a significant 9.4% growth in the construction sector makes it possible to expect a recovery in investment activity in the remaining part of 2013.

Last year’s drought put inflationary pressure on the food sector. The annual growth rate of food prices rose from 0.9% in June 2012 to 5.4% in December and stood at 5.5% in March 2013; whereas the annual consumer price index was 4.1% that month. Given these circumstances, the National Bank of Moldova kept its key rate at 4.5% from March 2012 to March 2013. The annual growth rate of money supply fluctuated around 25% throughout Q1 2013, while the annual growth of bank lending to the economy was about 13 to 14% and the share of non-performing loans (NPLs) remained at a level of 13% of all loans issued by banks. Despite the high share of foreign capital in the banking sector (74%), and its vulnerability to negative effects from the European banking crisis – 30% of the banking sector’s assets are in fact liabilities to European banks – the financial indicators of local banks continue to show relative sustainability. The sector has a capital adequacy ratio of 25.4%, while the profitability of assets (ROA) is 1.9%.

Despite the poor results of the last years, the government continued optimizing public finances. Amid the economic growth in Q1 2013, state budget revenue grew by 14.3% year-on-year. A major contribution to the increase was made by internal taxes on goods and services. As for public spending, there was underfunding across almost all expenditure items. As a result, the national budget had a deficit amounting to about 0.4% of GDP. Moldova’s external public debt amounted to $1.2 billion (20% of GDP) at the end of March 2013, shrinking by 3% since the beginning of 2013.
Outlook

Moldova: Favorable short-term and medium-term outlook

The growth of industrial output accelerated to an annual rate of 6.5% in January-April 2013. The continued upward trend in economic growth is evidenced by the volume of freight turnover, which increased by 16.6% in the first five months. A further improvement in the external economic conditions and the expected high agricultural output should contribute to a high GDP growth rate in 2013. The International Monetary Fund forecasts a growth rate of 4% for 2013, the European Bank for Reconstruction and Development 2.5%, and the World Bank 3%. The Moldovan government initially projected GDP to grow by 4%, but it subsequently revised its projection downward to 3.5%. As a result, the current consensus forecast, which is the median forecast of international institutions, predicts Moldova's GDP to grow by 3.3% in 2013, 4% in 2014 and 5% in 2015. It is quite likely that forecasts will be revised upward as economic growth accelerates. At the same time, all analysts agree that the prospect of economic growth in Moldova is uncertain and depends on the situation regarding cash remittances from abroad, external demand, and investment.

Inflation accelerated to 5.7% in May 2013 after the National Bank reduced its key rate to 3.5% in April. The annual growth rate of food prices rose to 10%, and the growth rate of prices of non-food consumer goods remained at the level of March and April - 3.8 to 4%. The government should refrain from further weakening monetary policy because this could lead to a loss of control over inflation. As world food prices have had a downward trend this year, one can expect that the National Bank will manage to keep inflation within the target band of 3.5 to 6.5% providing the current refinance rate remains unchanged.

The government expects the state budget to have a deficit of no more than 1.1% of GDP due to an improvement in the collection of taxes, including VAT. The government aims to keep the budget deficit at a level close to 1% of GDP in the long term. To all appearances, the authorities continue to rely on international donors for support in carrying out further reforms in the pension system and the education system, and in improving the quality of services. Amid the relatively low level of public debt (24% of GDP), and the displayed commitment to reform, the authorities' goal of streamlining public finances looks achievable. However, due to the high degree of integration with Europe, the national economy remains susceptible to shocks related to debt problems in the European region. The continued high level of external borrowing in the private sector (61% of GDP), in particular dependence on European banks (12.6% of GDP), increases the degree of uncertainty regarding the situation of the Moldovan economy.

A growth acceleration in industrial production and freight transportation, coupled with expected high agricultural output, suggests a favorable outlook for growth in 2013.

The current consensus forecast predicts GDP to grow by 3.3% in 2013, 4% in 2014 and 5% in 2015.

Declining world food prices make it possible to expect the inflation rate to remain within the National Bank's target band.

The high level of the private sector's external debt and vulnerability to external economic risks remain the main risk factors for the economy.
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 – Q1 2008 = 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
Trends
Russia: Low GDP growth amid recession in Europe

Russia’s economic results for Q1 2013 were generally unimpressive: GDP grew by 1.6% year-on-year compared with 3.4% in 2012; the industrial sector showed zero growth; manufacturing industry had a 1.3% year-on-year output increase; the production of mineral resources fell by 4.9%; and a 2.4% decline occurred in the power, gas and water production and supply industry. The agricultural sector resumed growth, with output increasing by 1.6% compared with 2012. Investment growth slowed down to almost zero (0.1%), which was partially due to the fact that some programs financed by the government or state corporations had been completed or passed the peak of activity. At the same time, amid low external demand, the real volume of exports grew by only 0.1%. Nonetheless, household consumption kept rising at a relatively high rate, increasing by 6.1% in real terms compared with Q1 2012.

The current account surplus in Q1 2013 amounted to $27.9 billion, down from $39.2 billion in Q1 2012. The decrease was due to: lower prices for major Russian exports; a lower volume of funds at the disposal of Russian economic entities for investment abroad; and a weakening of factors stimulating the export of capital amid a marked decrease in the level of risks in the world as a whole.

A lower-than-projected level of non-oil and gas revenue, led to difficulties in financing budget expenditure. This was because the so-called budget rule came into force, which requires a share of the country’s oil revenues to be set aside. The government eventually decided not to revise expenditure levels, compensating for a shortage of privatization revenue with oil and gas revenue. In Q1 2013, the federal budget had a deficit amounting to 62.2 billion rubles (0.4% of GDP), while the consolidated budget had a surplus of 290.9 billion rubles (1.9% of GDP). The respective figures for Q1 2012 were 70.2 billion and 519.9 billion rubles.

The annual consumer price index was 7% in March compared with 6.6% at the end of 2012. The Bank of Russia in fact did not change its policy, waiting for the emergence of significant grounds to be confident that it will manage to keep inflation within the target zone of 5 to 6% in 2013. Statements from the leadership of the Bank of Russia, as well as the bank’s move to lower some minor rates, suggest that it is highly probable that the bank will loosen monetary policy in the second half of 2013.

The annual growth of bank lending, which slowed to almost 20% by the end of 2012 from 28% in the middle of the year, continued to stand at that level throughout the first months of 2013. The sustainability indicators of the banking system remained close to the levels reached following consolidation in the second half of 2012: the ratio of banks’ equity capital to risk-weighted assets was 13.4% as of the end of March compared with 13.7% at the end of 2012, and the ratio of risk-weighted assets to total assets, remained at 50.7% at the end of Q1 2013.
Outlook

Russia: Recovery in growth amid improvement in external environment

Currently available data for Q2 2013 suggest a certain recovery in the economic growth rate compared with the first months of 2013. In particular, the growth rate in the extractive sector reversed from negative to positive. The sector’s output increased by 0.6% in April and May. Manufacturing industry did not show a steady acceleration in growth due to a strong negative calendar effect in May, having a growth rate of 0.2% in January-May 2013. As a result, according to data from the Ministry of Economic Development, Russia’s GDP increased by 2 to 2.1% year-on-year in the first two months of Q2 2013.

We expect that the growth in the extractive sector will continue in the second half of 2013 amid a recovery in external demand. Relatively favorable weather earlier in 2013 and the low base of 2012 provide grounds to expect a very high growth rate in the agricultural sector. The reduced rates by the Bank of Russia will also be a positive factor for economic growth in the second half of 2013. In addition, the government may take measures aimed at stimulating economic growth, although a set of measures to this effect has not yet been finalized. A number of large-scale infrastructure projects have been announced by authorities and are to be financed with resources from the National Wealth Fund. They will have an effect on economic growth in 2014 and the following years rather than in 2013. In general, we expect Russia’s GDP to grow by some 3% (between 2.5 and 3.5 %) in 2013.

To all appearances, inflation will slow down and get back into the target zone of 5 to 6% by the end of 2013. Amid these circumstances, the central bank will get the opportunity to start loosening monetary policy, although the degree of this loosening will be determined by the pace of deceleration in inflation. The leadership of the central bank appears to continue to be focused on controlling inflation.

The external balance of the Russian economy may experience certain changes in connection with the spending of resources from the National Wealth Fund. The amount and timing of the spending is difficult to forecast, but it will not apparently be used in significant amounts in 2013. If these transactions are set aside, Russia will continue to have a current account surplus, which is expected to amount to 3 to 4% of GDP, the reverse side of which will be sizable exports of capital by the private sector.

The current forecast of the Ministry of Finance for the federal budget predicts that there will be a budget deficit of up to 0.6% of GDP in 2013. Based on somewhat more optimistic expectations than those of the government with regard to energy prices and economic growth, we estimate that the budget will be close to balance (probably will have an insignificant deficit) in 2013.

As there are no considerable negative shocks, the economy will apparently get back to the level of moderate growth. This is against the backdrop of an improvement in the external environment, and stimulus measures to be taken by authorities in the remaining part of 2013 and in 2014.

Data for April and May 2013 indicate a growth recovery in the extractive sector, a continued stagnation in the manufacturing sector

Growth acceleration may occur in the second half of 2013 in the extractive industry and the agricultural sector

The central bank’s lower rate and the government’s stimulus measures should support GDP growth

Inflation will apparently get back into the target zone of 5 to 6% by the end of 2013

The current account surplus will continue to amount to 3 to 4% of GDP; the external balance may experience changes in connection with the spending of the National Wealth Fund’s resources

The federal budget will be close to balance in 2013
Russia

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

![Graph showing GDP growth and output change by sectors from Jan-Mar 2012 to Jan-Mar 2013.]

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)

![Graph showing foreign trade, exports, imports, current account, and REER from Q1 2011 to Q1 2013.]

Source: national agencies

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

![Graph showing government sector budget from Jan-Mar 2012 to Jan-Mar 2013.]

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)

![Graph showing monetary sector data from May 2011 to May 2013.]

Source: national agencies, IMF (IFS)

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

![Graph showing economic growth from 2000 to 2014.]

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)

![Graph showing savings and investments data from 2006 to 2015.]

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

**Tajikistan: Impressive GDP growth and signs of slowdown in industrial sector**

In Q1 2013, the economy of Tajikistan showed an impressive 7.3% growth, which was based on continued dynamic growth in the services sector. The country’s industrial sector continued to experience a slowdown caused by a 9.5% slump in the metallurgical industry. A 6% decrease occurred in the output of the textile and the garment industry. However, the industrial sector had a growth rate of 5.5% due to mining, and power and heat companies. This slowdown in the industrial sector did not fully affect foreign trade in Q1 2013. The foreign trade deficit decreased by $113 million compared with Q1 2012, which was caused by both a 10.4% year-on-year increase in exports – mainly due to exports of textile products – and an 8.6% year-on-year decrease in imports. With an extra $112 million in cash remittances from abroad taken into account, the current account deficit is estimated to have amounted to approximately 10% of GDP. Cash remittances from abroad led to a rise in the population’s income and, consequently, a rise in consumer activity. A 13.3% increase occurred in fixed capital expenditure, which was ensured by the construction of transport and power-generating facilities and supply lines, as well as by housing construction.

In Q1 2013, the growth of revenue from taxes proved to be lower than the growth of nominal GDP, and the state budget revenue grew mainly due to additional grants. Public spending decreased as a percentage of GDP – this occurred mainly due to underfunding of capital expenditure on power-generating infrastructure and some other expenditure items. As a result, the state budget had a surplus of 7.7% of GDP, which was significantly above the 2012’s level of 4.1% of GDP.

Amid continued high economic activity and low world food prices, inflation remained at a relatively low level throughout the first months of 2013. The annual inflation rate was 6.5%, and the annual growth rate of money supply stood at 10 to 11%. The National Bank of Tajikistan plans to keep inflation at a rate of 9%. Apart from the slowdown in inflation, there were positive trends in the indicators for bank lending. The share of loans in foreign currency in the total volume of loans decreased from 59.6% at the beginning of 2013 to 58.8% in March. The share of classified (non-performing) loans grew to 18.5% of the total volume of loans issued in Q1 2013 from 18.2% at the end of 2012, and the average ROA (return on assets) rate of banks rose from 0.2% to 2%. According to authorities, this was attributable to: an increase in the interest rate margin; a rise in proceeds from foreign exchange transactions; a decrease in operating costs; and a decrease in expenses for the formation of a provision for covering possible losses from loans.
Outlook

Tajikistan: Slight slowdown amid continued consumer activity

The year-on-year growth rate in the manufacturing industry continued to decline after Q1 2013, falling to 0.4% in January-May 2013 from 0.8% in Q1 2013. A downturn continued in the metallurgical industry, which experienced an output decline of 1.7%, while the fall in textile and garment production deteriorated to 12.2%. The power, gas and water supply industry ensured an 8.2% increase in industrial output. The current consensus forecast predicts GDP growth to slow a little, from 7.4% in 2012 to 6.8% in 2013. To all appearances, consumption will continue to be the main factor supporting economic growth. However, declining figures for retail growth suggest a slowdown in growth in consumer activity. The European Bank for Reconstruction and Development has revised downward its forecast for economic growth for 2013 considering the expected slowdown in the rise in cash remittances from abroad.

The impact of lower world prices for aluminum and cotton, the country’s main export items, deteriorated the foreign trade indicators for 2012 and the first half of 2013. Exports decreased by 4.2% year-on-year in the first five months of 2013, while imports rose by 8.8%. Nonetheless, the first signs of a rise in world prices of raw materials should improve the trade balance of Tajikistan.

According to the 2013 budget law, the state budget for 2013 is aimed at promoting better transport connectivity, achieving energy independence, and ensuring food security and the social protection of the population. The government has set a target deficit of 0.5% of GDP. It is most likely that the government will manage to meet the target. However, chronic underfunding of important expenditure items and the budget’s dependence on grants leave a certain degree of uncertainty. As for the longer-term outlook, the government faces the task of reforming the structure of revenues in connection with the country’s accession to the WTO, which may lead to poorer fiscal results.

The National Bank of Tajikistan targets the annual inflation rate at no more than 9% in 2013. Amid the continued high economic activity and low world food prices, inflation has been at a relatively low level since the beginning of 2013. Nonetheless, the annual growth rate of M2 jumped to 16.6% in April after it grew by 10% in March. One can therefore expect a slight acceleration in the rise in prices in the next few months. Amid the sharp increase in the M2 growth rate, the growth of bank lending skyrocketed to 38.2% in April. According to media reports, the share of short-term loans in the total loan portfolio grew to 64.9% from 60% in February. The degree of dollarization of the banking sector continued to rise as well. The share of loans in foreign currency in the total volume of loans grew from 59.4% at the end of 2012 to 62.4% in April 2013.
**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
**Trends and outlook**

**Turkmenistan: Continued high GDP growth rate**

In Q1 2013, Turkmenistan’s GDP growth slowed down to 9.2% from 11.1% in 2012. This was as a result of weaker external demand, declining oil prices and decelerating fixed capital expenditure. The country’s economic growth remained high due to stimulus measures taken by the government within the framework of investment policy. The aims of the policy are: the diversification of the economy through the modernization of production; promotion of the development of new industries (chemical, light and building materials industries); and the construction of infrastructure facilities. Also, growth is high due to measures aimed at increasing the population’s income and raising living standards.

Despite high growth in public spending, which rose by 67% in annual terms, growth in fixed capital expenditure slowed to 5.1% compared with 39.6% in Q1 2012. However it did stimulate growth in many branches of manufacturing industry and in the construction sector. In particular, cement output and the output of rolled metal products increased by 69 and 22.3%, respectively. Given the government’s strategic plans aimed at the expansion of the production potential in the power generation, oil production and gas production industries, the growth rates of these industries should have risen. However statistical data are not available. The oil-refining, chemical, machine-building, food and light industries had more modest growth rates. Also modest were the growth rates of crop production (from 2.9 to 4%) and animal production (from zero to 0.7%). The increase in state budget expenditure in Q1 2013 was caused by a rise in social spending, which contributed to a rise in the population’s income and stimulated household consumption. As a result, the volume of retail trade grew by 19.7% in Q1 2013.

Turkmenistan’s exports rose by 19.3% due to the diversification of gas export routes, the continued high price of hydrocarbons, and a 12.6% increase in the output of raw cotton. At the same time the country’s imports grew by 24.4%, largely due to an increase in investment demand for equipment. A continued significant foreign trade surplus, coupled with a rise in foreign direct investment – in particular, Chinese investment in the fuel and energy sector – helped Turkmenistan maintain a current account surplus.

High export revenues also led to a state budget surplus (6.4% of GDP). Revenue turned out to be 60% higher than forecast due to, among other factors, a rise in tax revenue from the private sector of the economy. The amount of public spending fully met the forecast level. Money supply, bank lending and price formation remain under the government’s control, which makes it difficult to assess inflation risks in the economy.

In 2013, having sufficient financial resources, the government will continue implementing its investment policy and take measures to improve the living standards of the population. However, a possible decline in prices of hydrocarbons may lead to a slight slowdown in economic growth. Nonetheless, the country’s GDP will continue to grow at a high rate. A consensus forecast, based on forecasts by the IMF, the EBRD and the Asian Development Bank, puts Turkmenistan’s GDP growth for 2013 at 8.9%.
Turkmenistan

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

Source: national agencies

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

Source: IMF

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

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
Uzbekistan: GDP growth amid massive government financing

Amid a slowdown in the world economy and a fall in prices for raw materials caused by the continued recession in the Eurozone and also due to seasonal factors - Uzbekistan’s GDP growth slowed down to 7.5% in Q1 2013 from 8.2% in 2012. Nevertheless, growth remained rather high. The slowdown was not significant, but it spread to all major sectors. The growth rate declined to 6% in the industrial sector, 6.2% in the agricultural sector, 13.1% in retail trade, and 8.2% in the services sector. An acceleration to 13.2% from 11.1% in 2012 occurred in the construction sector. This was due to, among other factors, the intensive implementation of a government program aimed at the rapid development of transport infrastructure and modern housing construction in rural areas.

The main driver of economic growth continued to be robust domestic consumer and investment demand. It was stimulated by resources from the state budget and the Fund for Reconstruction and Development within the framework of a social and economic program aimed at modernizing the economy and raising the population’s living standards. The banking sector increased lending to the real sector of the economy by 31%; while the government’s policy aimed at supporting foreign investors contributed to a 35.5% increase in foreign investment, with direct investment accounting for 84% of the total volume. Fourteen new investment projects worth a total of $4.3 billion were launched in Q1 2013; while fixed capital expenditure grew by 7.2%. Cash remittances by migrant workers appear to have totaled at least the same amount as in 2012. Coupled with the high level of social spending, this led to a 15.6% increase in real income.

The negative impact on the economy from lower external demand and a decline in prices for Uzbekistan’s main export items (natural gas, gold and cotton) was offset by: the diversification of gas export routes; the expansion of the production potential for petroleum products; and the export potential of the economy. Seventy six new items of goods were exported in Q1 2013. Given the existing restrictions on imports, the rise in exports should have improved the trade balance of the country, and increased the balance of payments surplus. Continued high oil and gas revenues helped the government maintain a state budget surplus of 0.4% of GDP.

The annual GDP growth rate will remain high in 2013 due to the government’s large-scale financing of economic development. According to the most recent consensus forecast, based on forecasts by the IMF, the World Bank, the EBRD and the Asian Development Bank, the country’s GDP will grow by 7.5% in 2013 - whereas the government expects a growth of 8%. A slight deterioration can be expected in the state of the public finances and the balance of payments due to the current fall in prices for natural gas, gold and cotton. Nonetheless, the nation should maintain its triple surplus: in the state budget, foreign trade, and the balance of payments. The government plans to keep inflation within a band of 7 to 9% – an annual inflation rate of 7.9% was reported for March – but, as was noted earlier, the real inflation rate is apparently higher, with the IMF estimating that it will be 10.9% in 2013.

GDP growth slows down to 7.5% in Q1 2013
Robust domestic consumer and investment demand remains the main driver of growth
Continued high oil and gas revenues contribute to a state budget surplus of 0.4% of GDP
The most recent consensus forecast predicts GDP to grow by 7.5% in 2013, whereas the government expects a growth of 8%
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

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 IMF

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
Trends

Ukraine: GDP decline, decrease in external imbalance

In Q1 2013, Ukraine’s real GDP was down 1.1% from Q1 2012. The economy thus had three consecutive quarters of negative year-on-year GDP growth. Declines occurred across many sectors and industries. There were year-on-year output decreases of: 9.5% in the manufacturing industry; 0.1% in the extractive industry; 7.8% in the power, gas and water production and supply industry; and 14.8% in the construction sector. Appreciable growth occurred in the agricultural sector (5.7%), retail trade (3.1%) and financial services (3.9%).

On the demand side, household consumption and fixed capital expenditure continued to grow, increasing by 4.5% and 4% year-on-year, respectively. Exports fell by 6.8% in real terms, while companies’ inventories kept growing.

As in 2012, the rise in domestic consumption amid declines in production and exports became possible due to external imbalance: the current account deficit in Q1 2013 amounted to 5.9% of GDP. However, the deficit decreased compared with the greater part of 2012, when it was equal to 8 to 10% of GDP. The inflow of capital remained at a level comparable to that in the second half of 2012: the financial account surplus amounted to 8.4% of GDP, appreciably more than in Q1 2012, when it stood at 3.5% of GDP.

There was a significant setback compared with 2012 in the field of fiscal policy: in Q1 2013, the state budget deficit amounted to 1.5% of GDP against a surplus of 0.3% of GDP in Q1 2012. A key factor behind the deterioration in the budget balance was an increase in expenditure, which rose by 3.5% of GDP compared with Q1 2012. The most significant increase occurred in social security expenditure items. Public spending for these purposes grew by 43.5% year-on-year.

The inflation situation did not change compared with Q4 2012. Throughout Q1 2013, the consumer price index showed monthly growth rates close to zero, while the annual inflation rates were negative at minus one to zero %. The National Bank of Ukraine continued to keep the exchange rate of the national currency against the US dollar within a narrow range of between 8.06 to 8.14 hryvnia for one dollar. Amid a decrease in external imbalance, the de facto peg was accompanied by acceleration in the growth of monetary aggregates compared with 2012. In particular, the annual growth rate of M2 was 16% in March against 13% in December 2012. The National Bank’s international reserves, which steadily declined throughout 2012, grew by $479 million in Q1 2013.

The growth in bank lending to the economy accelerated to 5% in March from 1 to 2% in Q4 2012. The financial stability indicators improved in Q1 2013. This included the ratio of regulatory capital to risk-weighted assets, the share of non-performing loans in the total volume of loans, and the share of liquid assets in total assets. This ended the negative trends that took place in that field throughout 2012.

Ukraine’s real GDP decreases by 1.1% year-on-year in Q1 2013; the country thus has three consecutive quarters of negative year-on-year GDP growth

There is growth in retail trade, the agricultural sector and financial services

The current account deficit amounts to 5.9% of GDP, decreasing compared with the greater part of 2012

There is a significant setback compared with 2012 in the field of budgetary policy

The annual inflation rate continues to be negative

Money growth accelerates compared with 2012

Bank lending growth accelerates to 5% in March; the sustainability indicators of banks improve
Outlook

Ukraine: Resumption of growth, consolidation of public finances

The economic situation remained unfavorable during the first five months of 2013. In particular, industrial production further declined compared with the second half of 2012, and did not show any signs of a recovery in April and May. At best, it is possible to talk about some stabilization of activity in the industrial sector in Q2 2013. The downturn in the construction sector appeared to have extended into Q2 2013. However, in a number of other sectors of the economy, negative growth rates began to reverse to positive values. Growth resumed in retail trade – it had almost ceased in Q4 2012. Amid a loosening of monetary policy, the financial services sector started to grow, and so did the agricultural sector, which was affected by a drought in 2012. Throughout the remaining part of 2013 and in 2014, the Ukrainian economy can be expected to resume growth under the influence of a general improvement in the economic situation in the region. However a possible slowdown in growth in household consumption and consumption-oriented industries, in particular retail trade, will have restrictive effects on it. The current rise in consumption too strongly depends on the expansion of public spending to be sustainable.

The decrease in external imbalance was an important result of Q1 2013. It manifested itself in a fall in the current account deficit, and a rise in the financial account surplus. The remaining part of 2013 will show to what extent these trends are steady. In particular, the current account balance should have been positively influenced by seasonal factors in Q1 2013. The stability of the positive trends in the financial account balance also needs to be tested by time. It is subject to risks, in particular related to the difficult situation on the fiscal front. The increase in the budget deficit during Q1 2013 makes one expect that the state budget will have a deficit amounting to 5 to 10% of GDP in 2013. This will pose a significant threat to the stability of the economy. The consolidation of public finances appears to have become a key task for the Ukrainian government.

The situation regarding monetary policy and lending continued to improve in Q2 2013. The growth rate of M2 accelerated to 12.3% in May. Simultaneously, the growth in bank lending accelerated to 6.1%. These changes were closely connected with the improvement in the balance of payments that took place in Q1 2013. The further loosening of monetary conditions and lending activity acceleration may be prevented if the external balance situation changes for the worse again. The degree of this impact and the probability of a new deterioration in the balance of payments could be reduced if the National Bank switched over to a more flexible policy regarding the exchange rate of the hryvnia.

It is possible to conclude that the economic situation in the country experienced a number of positive changes with regard to the balance of payments, monetary conditions, and lending. Their effect on economic growth will become appreciable if these changes prove to be steady and progress further. This in turn largely depends on the nature of the macroeconomic (fiscal and monetary) policy pursued by the government.
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

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