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

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Macroeconomics of the region

Despite an improvement in Q4, world GDP growth slows in 2012

With an average growth rate of about 5.1%, developing countries continued to be the main driving force of economic growth in 2012, as the economies of high-income countries grew by only 1.3%. Business indicators of the world economy show a general improvement in its condition and growth in Q4 2012, after the central banks of leading countries loosened their monetary policies. Although new rounds of quantitative easing took place worldwide, the global economy did not experience significant inflation pressure. There was not an equivalent rise in lending activity, which questions the efficiency of quantitative easing measures. Amid these circumstances, the price of Brent crude averaged out at $112 per barrel in 2012, exceeding the level of 2011 by 1%, whereas Brent oil had increased in price by 39% in 2010.

A sharp slowdown in the percentage increase in the price of the main export commodity of the CIS economies affected the GDP growth rates of these countries. A common feature of the economic situation in the region throughout 2012 was a decrease in investment demand and a slowdown in output growth in export-oriented sectors. Agricultural output also showed a lower growth rate than in 2011. This was because of both a base effect in connection with an exceptionally good harvest in 2011 and a drought in grain producer countries in 2012. Consumer demand and the sectors oriented toward serving it, in particular trade and services, continued to be driving forces of growth in almost all member countries of the CIS. A degree of improvement occurred in construction activity. The financial sector, which had a satisfactory lending growth rate in the first months of 2012, slowed in the second half of the year as a result of a general downturn in economic activity. In the case of Russia, a significant role in this process was played by measures taken by the central bank to restrain the growth of lending. As a result, the aggregate real GDP of the CIS countries grew by 3.4% in 2012, down from 4.7% in 2011. The aggregate GDP of the EDB member countries is estimated to have grown by about 3.5%. Economic growth accelerated in Azerbaijan, Armenia and Tajikistan; and the biggest slowdowns occurred in the growth rates of the largest economies of the region – Russia, Kazakhstan, Belarus and Ukraine – which have the closest economic ties with European countries.
A slowdown in the rise in petroleum product prices has a mixed effect on the foreign trade indicators of the CIS countries. In some economies, the depreciation of the national currency led to a decrease in demand for imported goods and services, which left the countries’ foreign trade balance almost unchanged. In economies with less flexible exchange rates of the national currency, a slowdown in the rise in export prices led to a decrease in the foreign trade surplus and in the international reserves of the central bank. In addition, in the labor exporting countries, there was a slowdown in the growth rate of cash remittances by migrant workers. Coupled with a low volume of exports – in Kyrgyzstan and Moldova – and a significantly higher volume of imports, this led eventually to deterioration in the current account balance.

The financial account balances of the CIS economies did not undergo considerable changes in the first nine months of 2012. Direct investment remained at the former, rather low level. The economies that are exporters of oil and natural gas experienced an outflow of capital, which was taken out for – in the case of Kazakhstan – portfolio investment abroad or for other investment purposes.

All countries of the region except for Belarus and Ukraine had a net inflow of debt capital and a corresponding increase in their external debt. The aggregate external debt of the CIS countries grew by 7.9% in the first nine months of 2012. The private sector’s borrowings made the main contribution to the growth of the external debt of Kazakhstan, Russia, Tajikistan, Kyrgyzstan, Moldova and Ukraine. The private sector of the CIS countries increased the gross external debt by 8%, while the gross public debt contributed 6%. Thus the dynamics of the region’s balance of payments in the first nine months determined a net increase of $21.8 billion, or about 1.2% of the region’s GDP, in the international reserves of the central banks. Significant increases in the international reserves occurred in Azerbaijan (8.9% of GDP), and Moldova (6.2% of GDP), while the size of the international reserves decreased in Armenia, Belarus and Ukraine. As a result of these dynamics of the balances of payments, the real effective exchange rate (REER) of the national currency rose in Azerbaijan, Kazakhstan, Moldova, Russia and Ukraine, and fell in Armenia, Belarus and Kyrgyzstan.

Figure 1.3. External trade: trade balance (% of GDP)

Figure 1.4. Cash remittances by individuals: net, from Russia to CIS countries (in % of GDP)
Amid lower economic activity, a decrease occurred in state budget revenues in the oil and gas exporting countries. Public spending grew in all CIS countries compared with 2011 due to an increase in the pay of public employees, social payments and government investment. In the economies that are net importers of petroleum products, except Kyrgyzstan, there was an improvement in tax administration and moderate expenditure consolidation. In Belarus the state budget had a surplus, while in Ukraine, amid poor economic growth dynamics, the state budget deficit increased.

Due to a slowdown in growth in the real sector and a high-base effect, the first half of 2012 saw a low rise in consumer prices in the region. The low inflation rate prompted the central banks of Belarus, Kazakhstan, Kyrgyzstan and Tajikistan to further loosen their monetary policies. They began to do this in Q1. The Bank of Russia, on the contrary, kept its refinance rate unchanged throughout the first eight months. It raised it in September 2012 following a rise in inflation as a result of a scheduled increase in regulated prices. After the National Bank of Belarus reduced its refinance rate from 4.5 to 3.2% in the first half of 2012, the growth of the money supply accelerated. However, the annual growth rate of consumer prices in Belarus was 21.8% in December 2012, down from an unprecedented 108.7% in December 2011. The region as a whole had a weighted average annual inflation rate of 6.3%, down from 7% in 2011.

Amid a decrease in inflation risks at the beginning of 2012, there was some revival in banks’ lending activity in some CIS countries. However, a slowdown in the second half of 2012 affected bank lending. The annual lending growth rates were within a range of 10 to 22% in all economies of the region, except Armenia, Belarus and Tajikistan, where this rate stood in September at 32, 49 and 30%, respectively. Of certain concern is the growth of lending in foreign currency, as well as a general rise in the volume of problem loans in banks’ portfolios in some CIS countries.
According to the World Bank’s Global Economic Prospects report published in January 2013, the recovery of the global economy is unstable and slow. The growth of the world economy may slow slightly this year but should accelerate in 2014 and 2015. Developing countries will still be the main driving force of economic growth. They are expected to have an annual growth rate of 5.8% in 2015. The economies of high-income nations are predicted to increase their growth rate from 1.3% to 2.3% in the next few years.

Due to the emergence of faint signs of growth recovery in the world economy, the baseline scenario for the medium-term development of the EDB member countries also assumes that the crisis in the Eurozone will abate. This would allow many economies in Europe to show a positive growth rate in 2015. The US economy would avoid recession as the government would likely refrain from a significant reduction of expenditure or a sharp increase in taxes, and the growth rate of the US economy would gradually rise. Positive developments in the European and the US economy, and also China’s own stimulus measures would lead to an acceleration of the Chinese economy’s growth. In 2013 monetary and lending policy is expected to remain soft in all leading economies. The price of the raw materials exported by EDB countries would therefore remain relatively high and so would their volatility.

The oil exporting countries account for the greater part of economic activity in the CIS region. This is why the main scenario is that the region’s growth rate will remain moderately positive. A consensus forecast from various institutions puts it at 3.9% for this year and 4 to 4.5% for 2014 and 2015. As for growth forecasts for the three conventional groups within the region, the oil and gas exporting countries are expected to have an economic growth rate of about 4%, with domestic demand being the main driver. The labor exporting countries are forecast to have a growth rate of 5 to 5.5%. These countries’ balances of payments continue to be significantly dependent on cash remittances from abroad. Ukraine and Belarus are exporters of industrial goods and are the most dependent on the economic situation in Europe. They should have the greatest acceleration of economic growth – from 3.6% in 2013 to 5.2% in 2015 – after experiencing the most significant slowdown in 2012.
**Trends and outlook**

**Azerbaijan: Steady growth in non-oil and gas sector, slowdown or decline in oil production**

The Gross Domestic Product (GDP) of Azerbaijan increased by 2.2% in real terms in 2012 compared with 0.1% in 2011. Economic growth remained relatively low due to a fall in oil and gas production, which was caused by a natural decline in the potential of Azerbaijan’s deposits. The output of the nation’s extractive sector decreased from 10.2% in 2011 to 5.1% in 2012. The economic sectors apart from the oil and gas industry showed steadily high growth rates. There was a 5.3% output rise in the manufacturing sector, an 18% rise in construction, and a 9.6% increase in the trade sector.

Inflation slowed down sharply compared with 2011: consumer prices rose by 1.1% against a rise of 7.8% in 2011. The strong fluctuations in the annual inflation rates were largely due to the National Bank’s rigid pegging of the national currency to the US dollar: the manat’s exchange rate varied between $0.78 and $0.79 during a year and a half. Under these circumstances, the government’s monetary policy was determined by the dynamics in international capital flows and public spending. The lack of a considerable capital inflow into the Azerbaijani economy amid the debt crisis in Europe led to a slowdown in the growth of the money supply in the first half of 2012. In particular, M2 grew by only 6.9% in the first half of 2012. The slow growth of the money aggregates and the lack of a significant increase in the prices of agricultural produce – in contrast to 2011 – determined the low inflation rate in 2012.

**State budget expenditure increased moderately, amounting to 15.8 billion manat (29.2% of GDP), compared with 14.6 billion manat (28.1% of GDP) in 2011. The size of the State Oil Fund increased by $4.3 billion in 2012 to $34.1 billion (81% of GDP). The growth of the government’s reserves slowed down amid the declining oil production, but their volume against GDP is high enough to ensure the stability of the economy in the medium term.**

Bank lending increased by 22.1% in 2012 compared with a rise of only 7.9% in 2011. In the second half of 2012, the volume of lending grew by 2.1% a month on average, whereas the monthly lending growth rate in the first half of 2012 was only 1.2%. The sustainability indicators of the banking sector slightly deteriorated. The ratio of regulatory capital to assets fell from 15% in 2011 to 14.3% in 2012. The share of liquid assets in total assets decreased from 17% in Q4 2011 to 13% in Q3 2012.

**Most analysts forecast an increase in Azerbaijan’s economic growth rate amid the anticipated stabilization of oil production and steady growth in the non-oil and gas sector. The median forecast of international organizations (the International Monetary Fund, the World Bank and the Asian Development Bank) predicts a 4% rise in Azerbaijan’s GDP in 2013 and a 3.7% increase in 2014.**
Azerbaijan

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

Source: the State Statistics Committee of Azerbaijan

Figure 2.2. **Foreign trade**: exports, imports, current account (left scale, in billions of US dollars), real effective exchange rate – REER (right scale, index – Q1 2008 = 100)

Source: national agencies, IMF

Figure 2.3. **Government sector**: state budget (in % of GDP)

Source: national agencies

Figure 2.4. **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, IMF (IFS)

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 and the CIS Statistics Committee

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

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

**Armenia: High GDP growth and improvement in macroeconomic indicators**

Armenia’s economy grew at a rate of 7.2% in real terms in 2012. Industrial output increased by 8.8% and agricultural output by 9.5%. There was a 3.6% rise in the trade sector and a 10.8% increase in the services sector. The high economic growth rate was caused by: the recovery of domestic consumer demand; external demand for exported metals; favorable weather conditions for agriculture; and a low base effect. Favorable trends in all components of domestic demand, with the exception of public spending, stimulated consumption. Cash remittances from abroad recovered to the pre-crisis levels, totaling an estimated $1.4 billion in 2012. Bank lending grew by 26.6%. Despite a slight decrease in the prices of exported metals, exports in nominal terms increased by 7%. This produced a favorable effect on the industrial sector’s indicators. Fixed capital expenditure decreased in real terms in the first three quarters of 2012.

Data for the balance of payments in 2012 have not yet been published. Judging by data for the first three quarters, the current account balance improved due to an export surplus amid the high volume of cash remittances from abroad, with exports rising by 5.1% and imports increasing by only 0.2%. A 9% improvement in the current account balance could not offset 47% deterioration in the financial account balance that resulted from a decrease in foreign direct investment ($325 million) and commercial banks’ external borrowings. This led to: a balance of payments deficit equal to 4.1% of GDP; a shortage of foreign currency; a 13% decrease in the Central Bank’s gross international reserves; and a rise in the external public debt, which grew by $212 million compared with September 2011. Data for 2012 testify to a continued steady rise in exports (7%), which outpaced the growth of imports (2.9%). There was also an increase in the gross international reserves in Q4, which however shrank by 6.9% in 2012. This indicates that Armenia’s balance of payments may have improved in Q4 2012.

The high GDP growth rate and the government’s balanced policy had favorable effects on the fiscal sector. Consolidated budget revenue and expenditure were characterized by a moderate and balanced rise. There was a relatively high rise in government revenue (24% of GDP), especially in revenue from excise taxes, VAT and customs duties (6.9% of GDP). Expenditure (26% of GDP) increased by 1.8%. The budget deficit therefore decreased from 2.8% of GDP in 2011 to 1.6% in 2012.

Armenia had an annual inflation rate of 3.2% in 2012 compared with 4.7% in December 2011. The easing of inflation pressure was caused by a fall in food prices – due to favorable weather conditions – and by the declining growth rate of the money supply. The total amount of M2X increased by 19.5% by the end of 2012. Given the slowdown in money growth in the framework of the government’s monetary policy, the Central Bank kept its base refinance rate at 8% throughout 2012.
Outlook

Armenia: Risk of slowdown in economic activity

In January 2013 Armenia’s economic activity rate increased to 9.1%, which suggests that the economic recovery trend continues. The high results – despite the high 2012 base – are attributable to the extraordinary growth rate shown by the industrial sector (18.8% in annual terms) and an increase in the growth rate in the trade sector (5.7%). There continued to be a high growth rate in the services sector (7.7%), while agricultural output increased at a moderate rate (2.1%). Following a few months of growth, the construction sector experienced a sharp fall. Its output decreased by 17.6% year-on-year and by 92.1% against the previous month, which indicates a continued slump in the sector. A steady domestic demand and the unprecedented rise in industrial output - including the output of exported products - remain the main drivers of economic growth in Q1. Imports rose by 13%, and exports rose by 54.6%. The first half of 2013 will be meaningful - if industrial output and exports continue to rise at the current high rates, it will be possible to talk about a structural improvement in the economy.

As for 2013 as a whole, one should expect a slowdown in Armenia’s economic growth rate. This is in the context of the continued weakness of the world economy and, in particular, the European economy, which accounts for 45 percent% of Armenia’s exports. A consensus forecast - based on forecasts from the IMF, the World Bank and the European Bank for Reconstruction and Development - predicts Armenia’s GDP to grow by 4.6% in 2013. The national government expects a 6.2% rise. The country’s economic growth may slow down due to a possible decline in external demand and a fall in the price of metals, which accounted for 42% of all exports in 2011. The weakness of the world economy may affect the Russian economy, which is the main source of cash remittances and foreign direct investment for Armenia. There is therefore an additional risk of a fall in domestic demand. This includes both consumer demand, fueled by cash remittances from abroad, and investment demand, which has been low since the 2009 crisis. If the Russian economy proves to be more resistant to external factors, then the slowdown in Armenia’s economic growth will be insignificant. The favorable effect of good weather conditions will gradually decrease and a slowdown should be expected in the agricultural sector, which accounted for 15% of GDP in 2011.

The possible slowdown in GDP growth and the expected fall in export prices will affect: the export-oriented branches of the industrial sector; the government’s export and tax revenues; and macroeconomic stability. The increase in the balance of payments deficit will be limited, but it will put depreciatory pressure on the dram. Within the framework of a program of cooperation with the IMF, the government successfully fulfills the task of improving tax administration and optimizing spending. The budget deficit should not exceed the government-projected level of 2.6% of GDP in 2013. The growth rate of money supply will continue to be moderate, and the Central Bank will not additionally stimulate it. The inflation rate will remain moderate and be within the target inflation band of 2.5 to 5.5%. Given the possible slowdown in the agricultural sector, a rise in food prices may cause limited acceleration in inflation.

If industrial output and exports continue to rise at the current high rates, it will be possible to talk about a structural improvement in the economy.

A consensus forecast predicts Armenia’s GDP to grow by 4.6% in 2013.

The possible slowdown in GDP growth and the expected fall in export prices will affect the industrial sector, export and tax revenues.
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 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, IMF (IFS)

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 and the CIS Statistics Committee

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 imbalance, high inflation

Belarus’ economic growth slowed down amid a balance of payments crisis in 2011. It remained low throughout 2012, and the GDP growth rate was 1.5% at the end of 2012. The sectors oriented toward meeting both consumer and investment domestic demand experienced a sharp fall in activity. The decrease in output of the construction sector was 9.8% and the trade sector 6.8%. The difficult economic situation in the world had a negative impact on external demand, and the extractive sector reduced its output by 2.3%. The manufacturing, agriculture, transportation and communications sectors, which are also oriented toward export, showed high growth rates: 6.3, 6.0 and 6.2%, respectively.

According to the National Statistical Committee Belarus had an inflation rate of 21.8% in 2012, down from 108.7% in 2011. However, the rise in consumer prices remained high. There was little change in the inflation rate throughout 2012, varying between 1.4 and 1.9% a month with an average rate of 1.7%. The National Bank’s policy contributed to maintaining inflation at a high level. After the NBB reduced its base refinance rate from 45% at the beginning of the year to 32% in June, the growth of lending activity accelerated. In the first half of 2012 banks’ receivables from other economic sectors grew by 1.9% a month on average. In the second half the average monthly growth rate was 3.4%, bringing the year’s total growth to 36.7%.

The central government’s budget had an almost zero balance. There was a budget surplus equal to less than 0.1% of GDP. Despite the fact that the balanced condition of the budget was largely achieved due to high inflation, the relatively good state of public finances was one of the positive features of the general economic situation in the country.

The balance of payments of the Belarusian economy, which was successfully strengthened in the second half of 2011 and the first half of 2012, significantly deteriorated again in the second half of 2012. The current account surplus of 2.4% of GDP in January-June 2012 was followed by a deficit of 7.7% of GDP - this was only slightly lower than the 2011 deficit of 9.3%. The return of the country’s external balance to a deficit was caused by two factors. Firstly, the policy of stimulating economic growth, which was reflected in a higher growth rate of lending in the second half of 2012, led to a rise in domestic demand. Secondly, in the middle of 2012 the Russian government significantly toughened the terms of trade in crude oil and petroleum products for Belarus.

The banking sector’s sustainability indicators kept deteriorating throughout 2012. However, they remained higher than they had been during the 2011 crisis. For instance, the ratio of risk-weighted assets to regulatory capital was 22 at the end of Q3 compared with 23 in the middle of 2012, 24.7 at the beginning of 2012 and 17 a year before. The ratio of risk-weighted assets to fixed assets was 15.5 at the end of Q3 against 16.6 in the middle of 2012, 18.8 at the beginning of 2012 and 11.9 at the end of Q3 2011.
Outlook

Belarus: Need to consolidate balance of payments

A major task currently confronting the Belarusian government is to restore the stability of the balance of payments. The country’s economy ministry has projected that Belarus will have a current account deficit of about 5% of GDP in 2013. Data for foreign trade in January-February 2013 also suggest that a significant external imbalance persists. Belarus is facing a threat to general economic stability because it has limited international reserves. They have been stable at around $8 billion since spring 2012, an amount equal to up to two months’ imports.

The task of reducing inflation to levels more typical for the region than the rates currently observed in Belarus has to be fulfilled within a short period of time. This is closely connected with the task of restoring the stability of the balance of payments. A tougher monetary policy is a necessary condition for both the deceleration of inflation and the strengthening of external balance stability. Control over inflation will be lost in the event of sharp fluctuations in the national currency’s exchange rate due to the instability of the balance of payments. The persistence of high inflation rates throughout 2012 indicates that the National Bank’s current policy is, at best, neutral to the growth in prices. To achieve progress in reducing inflation, it is necessary to tighten monetary policy – that is, to raise the refinancing rate and curb the banking sector’s lending to the economy – although this may have negative consequences for economic growth in the short term.

The existing need to make more effort to strengthen the balance of payments and reduce inflation constitutes a serious obstacle to restoring domestic demand, which decreased in 2011. Therefore, at least in the next year or two, one should hardly expect a significant and steady rise in activity in the sectors oriented toward households’ consumption or investment, such as trade and construction. There is a potential for growth in traditionally strong and competitive sectors oriented toward export, such as the chemical, petrochemical, machine-building and food industries. These sectors are dependent on the economic situation in the countries that are major trading partners of Belarus, including Russia and the Eurozone countries. Experts of international organizations (the EurAsEC Anti-crisis Fund, the World Bank and the IMF) expect the country’s GDP to annually grow at a rate of 2 to 4% in the next few years.

The economic situation in Belarus is therefore neither excessively unfavorable nor unmanageable. If the government and the National Bank pursue a realistic policy, the country will manage to restore the stability of the economy and achieve a moderate but steady economic growth in a year or two. Premature attempts to boost the GDP growth rate to the levels seen in the previous decade through stimulating the economy may trigger a recurrence of the 2011 economic crisis.
Belarus

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

![GDP and output chart]

Source: the National Statistics Committee of Belarus

Figure 4.2. **Foreign trade**: exports, imports, current account (left scale, in billions of US dollars), real effective exchange rate – REER (right scale, index – Q1 2008 = 100)

![Foreign trade chart]

Source: national agencies, IMF, EBD

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

![Government sector chart]

Source: national agencies

Figure 4.4. **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)

![Monetary sector chart]

Source: national agencies, IMF (IFS)

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

![Economic growth chart]

Source: national agencies, estimates by the World Bank, the EBRD, the IMF and the CIS Statistics Committee

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

![Savings and investments chart]

Source: estimates and forecasts by national agencies, the IMF and the EBD
Trends
Kazakhstan: Robust domestic demand offsets decline in external demand, fall in industrial and agricultural output

Kazakhstan’s economic growth slowed down from 7.5% in 2011 to 5% in 2012 due to weakened external demand, technical problems in the oil sector and a slump in agricultural production. The decline in the external demand and a fall in world metal prices caused a 12% decrease in the country’s ferrous metal output. This affected the overall output of the manufacturing sector, which rose by only 0.7%. Technical problems experienced in some oil fields led to a 1.4% decline in oil production, and limited output growth in the extractive industry to 0.2%. The water supply industry experienced a setback of 5.9%. Less favorable weather conditions and a high base effect led to a 17.5% drop in agricultural output. The main driver of economic growth was the rapidly developing services sector, which accounted for 52% of GDP. Boosted by robust consumer demand, the sector grew by 10%. The growth rate in the construction sector remained low at 2.9%. The power supply industry also had a moderate growth rate of 3.3%.

According to a preliminary estimate by the National Bank of Kazakhstan, the indicators of external economic activities deteriorated, but remained at rather healthy levels and were not of serious concern. It was the first time in five years that Kazakhstan had a balance of payments deficit, which amounted to $2.8 billion, or 1.4% of GDP. The capital and financial account deficit decreased by 13.3%. A decrease occurred in the current account surplus due to the weakening of external demand, worse conditions for trade, and a 5.2% rise in the real effective exchange rate of the national currency. The current account surplus remained impressive at 4.4% of GDP. The exchange rate of the tenge was stable and the gross international reserves, including the National Fund of the Republic of Kazakhstan (NFRK) resources, continued to grow.

The slowdown in industrial output growth, the slump in agricultural production, and the decline in the growth rate of exports in 2012 led to a deterioration of public finances. According to the Kazakh ministry of finance, the consolidated budget surplus shrank to 8.6% of GDP. The growth of consolidated budget revenues, which amounted to 31% of GDP, slowed down to 6.5%. Tax revenues increased by only 2.2%, while a 15% rise in non-tax revenues and transfers from the NFRK accounted for the bulk of the growth of consolidated budget revenue. Consolidated budget expenditure, which accounted for 22% of GDP, rose by 13%. With a 3% share in GDP, oil revenues continued to play an important role in financing the state budget deficit.

In December 2012, Kazakhstan’s overall annual inflation rate rose to 6%. There was a rise in prices across all categories of commodities. Services increased in price by 9.3%, foodstuffs by 5.3% and non-food consumer goods by 3.5% year-on-year. Inflation remained at the lower bound of the National Bank’s target band of 6 to 8%, and can be viewed as acceptable. The inflation rate corresponded with: the lower GDP growth rate; limited external inflation pressure; and a slowdown in the growth of money supply in the second half of 2012. The annual growth rate of M3 was 7.9% in December 2012.

GDP growth slows down to 5% due to a decline in external demand, technical problems in the oil sector and a slump in agriculture

It is the first time in five years that Kazakhstan has had a balance of payments deficit, which amounts to $2.8 billion, or 1.4% of GDP.

Oil revenues continue to play an important role in financing the state budget deficit.

Inflation remains at the lower bound of the National Bank’s target band of 6 to 8% and can be viewed as acceptable.
Outlook

Kazakhstan: Acceleration of economic growth in 2013 and stability of macroeconomic indicators

Given the continued low degree of diversification of Kazakhstan’s economy, the dynamics of many macroeconomic indicators remain dependent on external factors, including the price of oil. If there are no dramatic shocks, one should expect a certain speedup of economic growth to 5.8% in 2013. This is according to a consensus forecast based on forecasts from the EDB, the IMF, the World Bank and the European Bank for Reconstruction and Development.

It is most likely that the major trends of 2012 will continue. The robust domestic demand will be the main driver of growth, and contribute to the dynamic growth of the services sector. The most important factors driving domestic consumption will be the continuing rise in pay and public spending, and a possible increase in bank lending. Given the low growth rate of gross investment in the last three years, one can forecast a slight acceleration of growth as the banking sector recovers, and the government takes measures to diversify the economy. In 2013 the volume of oil production should recover to the former level, which would have a positive effect on the growth rates of both GDP and foreign trade. If the start of oil production in the Kashagan offshore oil field in the Caspian Sea is a success, the country’s economic growth will be given an additional boost. As for agriculture, its growth rate should rise in 2013 because of a low-base effect. If the banking sector recovers and improves its sustainability indicators, it is most likely that lending to the economy will increase. This would have a positive effect on all sectors, including construction.

Volumes of commodity exports will remain strong due to the continued relatively high price of oil ($109-$110 per barrel) and other exported raw materials (such as wheat grain), and the expected increase in oil production. Due to the continuing strengthening of consumer and investment demand, one should expect that the growth of imports will outpace the growth of exports. This would lead to an additional deterioration of the foreign trade balance and the current account balance. Despite the possible deterioration of the balance of payments, the volatility of the tenge will remain low because of the National Bank’s policy and the high volume of international reserves. The continued high export revenues that support domestic demand, and the expected acceleration of economic growth, will contribute to a further increase in both tax revenues and the reserves of the National Fund of Kazakhstan. Despite the likely inflation acceleration resulting from the expected higher growth rates of GDP and bank lending - the rise in prices in the country will probably remain within the medium-term projection range that the National Bank set at 6 to 8%.

A consensus forecast predicts a GDP growth rate of 5.8% for 2013

The recovery of oil production would have a positive effect on the growth rates of both GDP and foreign trade

One should expect that import growth will outpace export growth

The tenge’s volatility will remain low because of the National Bank’s policy and the high volume of international reserves
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, EBD

Figure 5.3. **Government sector**: consolidated budget (in % of GDP)

Source: national agencies

Figure 5.4. **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, 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 ADB, the World Bank, the EBRD, the IMF, the EBD and the CIS Statistics Committee

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: Negative shock from supply side offset by growth of private investment**

Kumtor Gold Company's low output due to technical problems affected Kyrgyzstan’s economic growth, and led to a 0.9% decrease in GDP in 2012. The Kumtor gold mine accounts for about 40% of the country’s industrial output. The industrial sector made a negative contribution to economic growth. This was offset by increases of: 17.3% in the construction sector; 7.9% in the trade sector, and 11.1% in the services sector.

A 63% drop in gold production in terms of volume led to a deterioration of the balance of payments. The country’s exports, of which gold exports make up about a third, significantly decreased, and the foreign trade deficit was 48% of GDP. The increased external imbalance was, to a certain extent, offset by cash remittances from abroad, which totaled $1.9 billion (29% of GDP), and foreign investment, which stimulated domestic consumption and contributed to a rise in services and retail trade. Fixed capital expenditure from all sources of financing increased by 21.5%, with the main contribution being made by the private sector.

Amid the economic downturn, despite improvements in tax administration and the advance payment of tax on the gross earnings of Kumtor Gold Company, state budget revenue saw a marked decrease. This affected the general situation in the economy in the second half of 2012. The government revised its budget projections, and decided to reduce or postpone capital expenditure. The government’s increased obligations regarding the pay of public employees led to a rise in consumer expenditures. As a result, the state budget had a deficit amounting to 6.6% of GDP.

The continued decline in prices in the world food market led to the strengthening of the disinflation trend in the first half of 2012. Amid poor economic activity and record low inflation figures, the National Bank of Kyrgyzstan continued loosening its monetary policy. The interest rate on the National Bank’s short-term notes was lowered from 13.6% at the end of 2011 to 2.6% at the end of 2012. Together with a small rise in world food prices in the middle of the year, this brought the inflation rate to a positive value. Non-food goods steadily contributed to the dynamics of consumer prices; and the base inflation rate testified to the existence of inflation pressure.

Amid declining economic activity in the second half of 2012, there was a slight slowdown in the growth of lending - the annual lending rate was 18.6% in October compared with 22% in March 2012. However, after the recovery of the production and export of gold, the growth of lending accelerated again. There was a significant rise in lending for the development of agriculture and the trade sector, and in mortgage loans. The degree of dollarization of lending (the share of loans in foreign currency in the total volume of loans) slightly decreased from 55% at the end of 2011 to 53% at the end of 2012. The average ROA (return on assets) of banks stood at about 3% in December 2012. The share of non-performing loans shrank from 10.2% of the total volume at the end of 2011 to 7.2% at the end of 2012.
Outlook

Kyrgyzstan: Low base of 2012 to ensure high growth rate in 2013

The economic development of Kyrgyzstan is characterized by high volatility. The national economy’s significant openness makes it vulnerable to the impact of external shocks. The low degree of diversification of production and exports creates dependence on the performance of one or two industrial giants. The large size of the external debt, the inefficiency and weakness of institutions, coupled with recurrent internal and external shocks, have prevented the economy from steadily developing and growing in the last 10 years. In 2012 technological problems at the Kumtor gold mine led to a considerable rise in the foreign trade deficit, and a 0.9% decrease in GDP. The liberal trade and tax regimes led to the establishment of a rapidly developing and quickly adapting private sector, which mainly consists of small and medium-sized businesses. The pace at which the economy recovers from new shocks is due to the efficiency and flexibility of the private sector. According to the government’s estimate, small and medium-sized enterprises accounted for 42% of gross added value in 2012. The resumption of gold production at the end of 2012 allowed Kyrgyzstan to have an impressive economic growth rate of 6.5% in January 2013.

The consensus forecast of international organizations predicts a GDP growth of 7.9% in 2013. Apart from 2012’s low base, internal trade and the services sector will remain major drivers of growth in the next few years. In the more distant future, the economy should return to a long-term growth path. Due to the accession of Kyrgyzstan’s major CIS trading partners to the WTO and the strengthening of integration processes within the Common Economic Space, the national economy faces the possibility of deviating from the current model of development. As a result of recurrent shocks in the last decade, the level of aggregate factor productivity in Kyrgyzstan has experienced a lengthy period of stagnation. However, in connection with the acceleration of liberalization and integration processes in the region, the possibility has emerged of a decrease in the national economy’s volatility and an increase in growth to the maximum possible level. The improvement of the conditions for trade also should lead to a gradual increase in investment. This would, in turn, contribute to economic growth. To achieve this, the government needs to make a considerable effort to improve the institutional environment while ensuring that the conditions for the private sector are maintained. The private sector is facing the need to find new niches in the regional division of labor, and switch over from re-export to the production of goods.

The large size of the external debt, which currently exceeds 100% of GDP, would appear to constitute a major threat to the sustainability of the economy. However, according to the IMF’s assessment of Kyrgyzstan’s debt sustainability, the national economy is at a moderate risk of debt distress in the medium and the long term. The IMF’s debt sustainability analysis takes into consideration most of the agreements reached by the government to reduce the external debt, as well as new borrowings.

Kyrgyzstan’s economic development is notable for high volatility because of its vulnerability to external and internal shocks

The pace at which the economy recovers from new shocks is due to the efficiency and flexibility of the private sector

International organizations’ consensus forecast predicts a GDP growth of 7.9% in 2013

The acceleration of liberalization and integration processes in the region opens up the possibility of a decline in volatility and an increase in economic growth to the maximum possible level
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, IMF, EBD.

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

Source: national agencies.

Figure 6.4. **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, IMF (IFS).

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

Source: estimates and forecasts by national agencies the ADB, the World Bank, the EBRD, the IMF, the EBD and the CIS Statistics Committee.

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.
Trends and outlook

Moldova: Drought, crisis in Eurozone and balanced macroeconomic policy

Moldova’s GDP decreased by 0.8% last year, with the main causes being a drought and the crisis in the Eurozone. In the first half of 2012, external factors led to a decline in both domestic and external demand. The share of the European Union in the total volume of exports decreased from 49 to 47%. In the second half of 2012, the state of the national economy deteriorated due to a strong drought, which affected crop and animal production, the food industry and exports. Agricultural production dropped by 22.4% in 2012, while industrial output declined by 3.1% compared with 2011. The greatest contribution to GDP was made by a rise in wholesale and retail trade. The economic crisis and the low purchasing capacity of the population affected the income of banking institutions, which decreased by almost one-third in 2012. The volume of bank lending fell by 16.1%, and the share of outstanding loans grew to 15%.

There was almost no change to Moldova’s foreign trade deficit, with both exports and imports decreasing last year. Cash remittances from abroad amounted to $1.5 billion, up 3.5% from 2011. The inflow of cash remittances and investment helped increase the country’s foreign currency reserves by 27.75% to $2.5 billion, an amount sufficient to cover almost six months’ imports. The government succeeded in pursuing a balanced macroeconomic policy. It prevented the state budget deficit from rising and timely loosened monetary policy. Both budget revenue and expenditure turned out to be lower than the figures projected for 2012. The state budget deficit amounted to 2.1% of GDP and was financed mainly through external assistance. The total size of the external debt, the bulk of which was made up by the private sector’s loan debts, grew by 6% in the first nine months. The annual inflation rate remained at 4 to 5% throughout 2012 and stood at 4.7% at the end of the year. Inflation was largely determined by food prices, with price of foodstuffs increasing by 5.4%, non-food goods by 3.6% and services by 3%.

Forecasts predict that Moldova’s GDP will grow by 3.6% in 2013, and that the growth rate will accelerate to 5 to 5.5% in the medium term. The prospects for growth depend on factors at the world and the regional level, which include the crisis in the Eurozone, the dynamics of the Chinese economy and the high level of bad debts. The National Bank of Moldova forecasts this year’s inflation at 4.1%, which would be determined by a moderate rise in food prices and a lower rise in the prices of petroleum products. It is now less likely that the government will raise regulated prices. The government’s monetary policy continues to be under the influence of a number of external and internal risks. The external risks include a possible rise in world energy and food prices, and the internal ones are connected with changes in budgetary policy, a slowdown in domestic economic activity and low external demand. These factors can ensure that deflationary pressure on prices in the country persists in 2013.
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, IMF

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

Source: national agencies

Figure 7.4. 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, IMF (IFS)

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 and the CIS Statistics Committee

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

Source: estimates and forecasts by national agencies and the IMF
Russia: Maintaining stability amid crisis in Eurozone

Russia’s GDP growth slowed down to 3.4% in 2012 from 4.3% in 2011. The decline in the economic growth rate was due to a number of factors. Firstly, there was a decrease in external demand for Russian exporters’ products, primarily because of the debt crisis in the Eurozone countries. Secondly, the unfavorable external environment had a negative impact on the investment activity of the private sector. Finally, unfavorable weather conditions led to a fall in agricultural output, which was larger as Russia’s crop production was extremely high in 2011. There was increased output of 0.9% in the extractive sector, 3.2% in the manufacturing industry, 2.0% in construction, and 2.7% in the transport and communications sector. The decrease in agricultural output was 3.8%. Trade, financial services and real estate operations showed rises of 6.5, 15.0 and 4.7%, respectively. From the standpoint of demand, household consumption grew by 6.6% and fixed capital expenditure by 6.0%, mainly due to the carrying out of projects financed by the government. Exports increased by 1.8%, while imports rose by 8.7%. Investment in finished goods inventories fell by 5.9%.

The current account surplus amounted to $81.3 billion (4% of GDP) in 2012. The surplus reached $39 billion in Q1 2012 amid a general capital outflow from emerging markets. It decreased to $6.7 billion in Q3 due to a fall in the price of Russia’s major exports in the middle of the year. It then rose again, increasing by $17.3 billion in October-December, when a rise in the price of raw materials supplied the economy with resources for the export of capital.

According to data from the Federal State Statistics Service, the federal budget had an insignificant deficit in 2012, which amounted to 37.1 billion rubles (0.09% of GDP). The consolidated budget had a surplus of 262.8 billion rubles (0.4% of GDP).

The annual inflation rate accelerated to 6.6% at the end of 2012 – after a record low of 6.1% in 2011. There was high demand for goods and services on the part of households, which was supported by a 7.8% increase in real pay and lending growth. The acceleration of inflation deprived the Bank of Russia of the opportunity to loosen its monetary policy, although general economic growth slowed down. The central bank raised all of its key interest rates by 0.25 percentage points in September, thereby making a symbolic but important step aimed at curbing inflation expectations.

Banks’ lending activity decreased amid the central bank’s relatively tight monetary policy. The annual growth rate of the banking sector’s net receivables, except receivables from governmental agencies and the central bank, fell to 19.7% in December 2012 from more than 28% in the middle of the year. The banking sector’s sustainability indicators ceased to fall or considerably slowed their decline. The ratio of banks’ equity capital to risk-weighted assets, which was 14.7% at the beginning of 2012 and fell to 13.1% at the end of October, rose to 13.7% by the end of 2012. The ratio of risk-weighted assets to total assets, which fell from 58.8% at the beginning of 2012 to 51.4 % in October, later slightly decreased to 50.7%.
Outlook

Russia: Acceleration of growth as external environment normalizes

Currently available data for the first months of 2013 suggest that the slowdown in economic growth seen in Russia in 2012 extended into this year. This means that the results of the first half of 2013 with regard to GDP will most likely be poor. At the same time there are grounds to expect an improvement in the economic dynamics later in 2013. Firstly, the low levels of 2012 were largely due to a marked decline in investment in finished goods inventories. In most cases, such a decline is indicative of a coming increase in production amid the replenishment of inventories. In addition, a positive effect on the economic dynamics should be produced by the expected normalization of the situation in the Eurozone, signs of which have already been seen. Apart from this, the anticipated decline in the inflation rate would create conditions for the Bank of Russia to loosen its monetary policy, which may happen as early as Q2 2013. The positive impact of these factors will most likely become visible in Q3 and Q4. Given these premises, one can expect the country’s GDP to grow by some 3.6% in 2013. As for 2014 and beyond, we expect the GDP growth rate to return to a level of 4 to 5%, which, in our opinion, is its natural level (see the October 2012 CIS Macromonitor’s analytical insert that offers a long-term forecast for economic growth in the EDB member countries).

The annual consumer price index rose to 7.3% in February 2013. The high inflation level is largely due to the fact that it currently reflects the impact of three increases in regulated prices that took place in July 2012, September 2012 and January 2013. One can expect that inflation will fall to 5 to 6%, settling into the central bank’s target band after the impact of the first of the three increases fades away by the middle of 2013. As a result the central bank will be able to lower its interest rates, which may happen as early as the first half of 2013, and loosen its monetary policy. This would contribute to an increase in lending activity in the second half of 2013. A slowdown in lending growth in the last months of 2012 was apparently sufficient to curb inflation and strengthen the sustainability of the banking system.

We do not expect dramatic changes in major indicators of the balance of payments in 2013. In particular, the current account surplus should remain at a level of about 4% of GDP amid a considerable export of capital by both the private sector and the government if the budget has a surplus. The possibility of a budget surplus would be created by a relatively high price of oil. We expect the price to be close to the 2012 average level (about $110 per barrel for Brent crude and slightly less for Urals crude).

The government expects the federal budget to have a deficit of 0.8% of GDP in 2013, with the average price of Urals crude to be $97 per barrel. If the price of Russian major exports turns out to be closer to our expectations, the budget will have a surplus of up to 1% of GDP.

Despite the current slowdown in GDP growth and the existence of serious external risks, the development of the economic situation in the country in 2013 is not of serious concern. The national economy may return to a higher rate of growth later, as the external situation improves.
**Russia**

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

![GDP and output graph]

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)

![Foreign trade graph]

Source: national agencies, IMF, EBD

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

![Government sector graph]

Source: national agencies

**Figure 8.4. 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)

![Monetary sector graph]

Source: national agencies, IMF (IFS)

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

![Economic growth graph]

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

**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)

![Savings and investments graph]

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

**Tajikistan: Solid economic growth amid consumer activity**

The country’s GDP grew by 7.5% in real terms in 2012. The main driver of the growth was consumption, which was stimulated by cash remittances by migrant workers – remittances from Russia alone amounted to 43% of GDP in 2012 – and an 18% increase in real pay. Fixed capital expenditure decreased considerably through a slowdown in the construction of public infrastructure projects. Favorable weather conditions and high agricultural output stimulated growth in certain branches of the food and textile industries. A rise in domestic demand led to an increase in imports, which rose by 17.8%. The country had a foreign trade deficit of $4.2 billion because of a relatively low rise in exports, which increased by 8.1%. Tajikistan’s foreign trade balance was affected by: a fall in world prices for the country’s major exports (aluminum and cotton); high prices of petroleum products; and problems in the transportation of intermediate goods used in aluminum production. However, despite a continued fall in cotton prices, there was an increase in the production and export of cotton fiber. A 98% rise in the physical volume of cotton fiber exports offset the rise in the price of this raw material.

Last year state budget revenue grew at a higher rate than expenditure – 7.4 and 5.9%, respectively – as a result of a rise in incomes in the economy and an improvement in tax administration. The most significant increase occurred in revenue from value-added tax, income tax and social contributions, which resulted from a rise in real pay. As for state budget expenditure, a considerable contribution to its increase was made by social payments and, to a lesser degree, by the public sector’s consumption. Investment spending of the government – in the transport and communications sector – noticeably decreased. According to data from the government, the 2012 state budget surplus was 1.5% of GDP.

Amid the declining world food prices and stability in the fiscal sector, the annual inflation rate in the country continued to decelerate until June, when it stood at 4.5%. This prompted the National Bank of Tajikistan to lower the refinance rate in two steps from 8 to 6.5%. A rise of world food prices in the middle of 2012 contributed to the resumption of a moderate upward trend in inflation. Consumer prices in the country rose by 6.4% in 2012, with food prices accounted for three percentage points and non-food consumer goods for about two points.

There was also a rise in bank lending, which grew by 13% in 2012. A marked increase occurred in the degree of dollarization of the banking sector. The share of loans in foreign currency in the total volume of loans grew from 56% at the end of 2011 to 60% at the end of 2012. As of September 2012, the average ROA (return on assets) of banks stood at 1.56%. The share of non-performing loans increased from 15 to 16.4% in the first nine months of 2012. The banking sector generally remained weak due to banks’ low profitability rates and the rather large share of non-performing loans.
Outlook

Tajikistan: Accession to WTO provides potential for growth through structural reforms

The country’s model of economic development is characterized by a considerable contribution of consumption with a very low volume of private investment. Throughout the last decade, the contribution of investment to economic growth has been about one percentage point of GDP growth. This is with the exception of some periods where the rise in this component of domestic demand was determined by spending on the construction of public facilities. Amid a foreign trade deficit, the main source of financing domestic demand was cash remittances from abroad. The balance of payments is characterized by the fact that cash remittances, on the one hand, stimulate domestic consumption and imports and, on the other hand, helps finance the foreign trade deficit. The current account deficit in the first half of 2012 amounted to 22% of GDP. In the first six months of 2012, there was an inflow of foreign investment and the country’s gross external debt grew by 6.8% to about 46.2% of GDP by July 1, 2012. This was due to an increase in the private sector’s borrowing. In 2012, the country’s international reserves grew by 4% to $308.6 million, which was enough to cover one month’s imports. The small size of the foreign currency reserves, amid the fixed exchange rate of the national currency and the volatility of the conditions for trade, represents a potential risk for further steady economic growth.

Since many international organizations revised upward their forecasts for GDP growth for 2013, the consensus forecast currently predicts a 6% growth rate for both 2013 and the next two years. Despite increased optimism following the release of data for 2012, the economy of Tajikistan remains vulnerable to both internal and external shocks. The poor growth of the world economy and, in particular, the Russian economy should have an impact on the economy of Tajikistan through a slowdown in the inflow of cash remittances in 2013.

If the country preserves its current economic development model, the prospect of further growth is limited. The government faces the need to carry out structural reforms and improve the investment climate in order to stimulate domestic investment. The country’s economic growth rate in the long term should correspond to its potential level, which is rather high at 6%. Tajikistan’s accession to the World Trade Organization provides a potential for additional sources of growth through the liberalization of trade and structural reforms. The carrying out of reforms should direct the financial resources of the economy into a productive channel and allow Tajik exporters to find additional niches in the international division of labor. Cash remittances from abroad will, in general, continue to stimulate consumption and, possibly, begin to contribute to the growth of private investment.

Accession to the WTO provides a potential for growth through the liberalization of trade and structural reforms

The country’s model of economic development is characterized by a considerable contribution of consumption with a very low volume of private investment.

The small international reserves, amid the fixed exchange rate and the volatility of the conditions for trade, represents a risk for economic growth.

The low growth rates of the world economy and, in particular, the Russian economy may lead to Tajikistan’s GDP growth slowing to 6%.

The country’s model of economic development is characterized by a considerable contribution of consumption with a very low volume of private investment.
**Tajikistan**

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

![GDP and output chart](chart1)

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)

![Foreign trade chart](chart2)

Source: national agencies, IMF, EBD

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

![Government sector chart](chart3)

Source: national agencies

**Figure 9.4. 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)

![Monetary sector chart](chart4)

Source: national agencies, IMF (IFS)

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

![Economic growth chart](chart5)

Source: estimates and forecasts by national agencies, the EBD, the ABD, World Bank, the EBRD, the IMF and the CIS Statistics Committee

**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)

![Savings and investments chart](chart6)

Source: estimates and forecasts by national agencies, the IMF and the EBD
Turkmenistan: Public investment constitutes main source of economic growth

Turkmenistan’s GDP grew by 11.1% in 2012 following a growth of 14.7% in 2011. This was due to public investment, a robust households’ consumer demand, and a high external demand for hydrocarbons on the part of China and Iran.

The implementation of investment policy contributed to a 38% increase in fixed capital expenditure (54% of GDP in 2011). The policy was aimed at the diversification of the economy through the modernization of production and the establishment of new industries (chemical, light and building materials industries), and the construction of infrastructure facilities. The rise in investment stimulated growth in the industrial sector and construction. In particular, the output of building materials (cement and rolled metal products) increased by 30 to 31%. The power generation, oil production and gas production industries showed rises ranging from 3.2 to 7.2%. The oil-refining, chemical, machine-building and food industries had more modest growth rates. Due to less favorable weather conditions, growth rates in the agricultural sector did not exceed 2.8% for all categories of products except raw cotton. A rise in incomes stimulated household consumption. This had a direct effect on the volume of retail trade, which increased by 18.5%.

A positive contribution to economic growth was made by growing exports. Turkmenistan’s exports rose by 19.3% in 2012 due to: the diversification of gas export routes; continued high prices 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 retain a current account surplus.

High export revenue also led to a state budget surplus (6.4% of GDP). Revenue turned out to be 60% higher than the projected amount because of, among other factors, a rise in tax revenues from the private sector of the economy. The amount of public spending on the social sectors fully met the projected level. The money supply, bank lending and price formation remain under the government’s control, which makes it difficult to assess inflation risks in the economy. According to data from the government, consumer prices rose by 5.3% in Tajikistan last year.

In 2013 the government will continue implementing its investment policy as it has sufficient financial resources – due to high export and fiscal revenues coming from the fuel and energy sector. This includes its effort to expand gas export routes and North-South and East-West transport corridors, and will contribute to a rise in the population’s living standards. 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: the CIS Statistics Committee and national agencies

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

Source: national agencies and IMF

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

Source: ADB

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

Source: ADB

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

Source: estimates and forecasts by the ABD, the EBRD, the IMF

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

Source: estimates and forecasts by the IMF
Trends and outlook
Uzbekistan: High growth rate amid deterioration in foreign trade balance

Despite a continued uncertainty in the external environment in 2012, Uzbekistan’s GDP growth rate of 8.2% was one of the highest in the region. The main drivers of the country’s economic growth were: a robust domestic consumer and investment demand, stimulated by an expansive budgetary policy; migrant workers’ cash remittances; foreign investment; and good weather conditions. External demand appreciably weakened despite the continued high prices of the main categories of exported raw materials (natural gas, cotton and gold).

Fixed capital expenditure rose by 11.6% to total 22.9% of GDP. This was as a result of the implementation of an economic policy aimed at increasing the competitive capacity of the industrial sector, and foreign investment that amounted to $2.5 billion. According to government sources 205 investment projects were completed in 2012. This contributed to an 11.5% increase in the volume of completed construction, and to a 7.7% increase in industrial output. Favorable weather conditions for cotton production and the government’s efforts to modernize the agricultural sector led to a 7% increase in agricultural output.

Domestic consumption was stimulated by: a rise in the population’s real income, which grew by 26.5% in the public sector and by 17.5% on average; and by a 33.5% increase in cash remittances from abroad, mainly from Russia, to a total of $5.3 billion. This led to a 13.9% rise in retail trade and a 14.2% growth rate in the services sector. Amid a weak external demand – exports decreased by 5.1% – a robust internal demand led to imports increasing by 9%. The decline in external demand affected all categories of exported goods except energy resources and petroleum products. An 81% increase in the export of energy resources and petroleum products offset the general decrease and helped retain a foreign trade surplus. It amounted to $1.12 billion in 2012 against $4.5 billion in 2011. The impressive rise in the export of energy resources and petroleum products ensured a sufficient level of fiscal revenue, with the state budget having a surplus of 0.4% of GDP. The current account balance remained positive, amounting to 4.5% of GDP.

A consensus forecast predicts that Uzbekistan’s economic growth will slow down in 2013, but the growth rate will still be at a relatively high level of 7.5%. The continued uncertainty in the external environment will contribute to a fall in the price of exported raw materials, and a further weakening of external demand including from China and Russia. There will be a decline in the growth of export and fiscal revenue. One can also expect a slowdown in the growth of cash remittances from abroad. The government has sufficient resources to ensure the further modernization of the industrial sector – the Fund for Reconstruction and Development is to provide $809 million to finance 34 projects – and increase the population’s income. Major risks relate to the institutional, political and social aspects of development. It should be noted that the government’s interference in the economy and the inaccuracy and insufficiency of statistical data — the government reported an inflation rate of 7% for 2012, whereas the IMF’s estimate put it at 11% — make it difficult to assess the macroeconomic situation in the country and the likelihood of an overheating of the Uzbek economy.
Uzbekistan

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

- Agricultural output growth
- Industrial output growth
- GDP growth

Source: the CIS Statistics Committee and national agencies

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

- Exports of goods
- Imports of goods

Source: national agencies

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

Source: IMF

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: 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 and the CIS Statistics Committee

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: Near-zero GDP growth amid deflation, external imbalance

The Ukrainian economy's growth slowed sharply to 0.2% in 2012 from a growth rate of 5.2% in 2011. Data for the first three quarters of 2012 indicate a 2.2% decline in the output of the manufacturing sector, a 6.1% decrease in construction and a 1.6% decline in financial services. In Q4 the output of the construction sector dropped by 15.6%. Agricultural output retained a positive growth rate, increasing by 1.2% on average in the first three quarters, but its contribution to the year's economic growth appears to have been negative. The extractive industry also showed a positive growth rate, but it was lower than the previous year - 3.1% on average against 8.3% in 2011.

Despite the low GDP growth in the first three quarters of 2012, household consumption increased by 12%, real pay increased by 14%, and public sector consumption grew by 4.6%. Fixed capital expenditure increased by 7.2% and investment in finished goods inventories experienced a sharp decrease of 130%, probably largely due to a poor crop.

Apart from the fall in finished goods inventories, the growth of consumption amid stagnation in production was connected with a deterioration of the foreign trade balance. In 2012, imports increased by 4.5%, while exports fell by 6.5% in real terms. The foreign trade deficit in the first three quarters amounted to $10 billion (7.8% of GDP) compared with $6.2 billion (5.3% of GDP) in the same period of 2011. The country's international reserves significantly shrank in 2012. They amounted to $24.5 billion (equal to about three months' imports) at the end of 2012 compared with $31.8 billion (equal to almost four months' imports) at the end of 2011. This was due to the external imbalance and the exchange rate policy pursued by the National Bank, which maintained a de facto fixed exchange rate of the national currency against the US dollar. The state budget had a deficit amounting to 3.8% of GDP, which was primarily financed by domestic borrowing.

The policy of pegging the hryvnia to the dollar, pursued in the past two years amid a balance of payments deficit, contributed to a slowdown in the growth of the money supply in the economy. M2 grew by 14.2% in 2011 and by 13.1% in 2012, whereas this monetary aggregate had an annual growth rate of 30 to 50% in the period between 2003 and 2008. The slowdown in money growth had an impact on inflation in the country. The consumer price index began to show negative growth rates. Consumer prices in December 2012 were 0.2% lower than in December 2011.

Another consequence of the slow growth of money supply was a decline in lending activity. The net volume of banks' receivables, except receivables from governmental agencies and the National Bank, grew by only 3.5% last year. The banking sector's sustainability indicators did not show pronounced trends. The ratio of regulatory capital to risk-weighted assets decreased from 18.9% at the end of 2011 to 18% at the end of 2012, but the decrease took place only in the first half of the year. The share of non-performing loans in the total volume increased in 2012 to 19.8% in Q4 compared with 14.7% a year earlier, but it was still far from the levels seen before the 2008-2009 crisis, when it exceeded 50%. 
Outlook

Ukraine: Return to growth, strengthening of balance of payments

The country’s GDP dynamics throughout 2013 will be determined by the influence of several factors. To begin with, economic activity in Ukraine may be supported by a general improvement in the situation in the region as the debt crisis in the Eurozone’s countries is settled. This would increase the demand for products of industries largely oriented toward export, such as the iron and steel, chemical and machine-building industries. As in other countries in the region, the agricultural sector will most likely have a high growth rate in 2013, unless weather conditions are as bad as last year. The significant impact that the fall in investment in finished goods inventories had on the economic results of 2012 suggests that the Ukrainian economy may show a higher growth rate in 2013. In this respect, the situation in Ukraine is similar to that in Russia. At the same time a rapid growth of consumption, supported by the expansion of public spending, cannot be reproduced in 2013 because the state budget already has a considerable deficit. This factor may have a negative impact on economic growth in 2013 and the next few years. Finally, an improvement in the balance of payments as a result of an increase in exports and better access to financing in external markets for Ukrainian companies and banks will begin to contribute to the growth of the money supply in the economy amid the current policy of exchange-rate pegging. This would result in the recovery of bank lending, which would have a positive effect on economic growth, as well as in a cessation of deflation.

In late 2012 and in the first months of 2013, there were signs indicating that the balance of payments was ceasing to deteriorate and its defense by the National Bank was putting less pressure on economic growth. In particular, the international reserves of the National Bank increased in January for the first time in half a year. The growth of monetary aggregates accelerated in the last months of 2012. Although these signs are of a preliminary nature and can be interpreted in various ways, they may mean that the period of economic stagnation, which was the price the country paid for the hryvnia’s continued peg to the dollar, is coming to an end. Nonetheless, the sustainability of the Ukrainian economy, including its growth rate, and its ability to resist external shocks remains fragile because the country still has a significant foreign trade deficit and suffered a serious reduction in its international reserves last year.

One of the key factors influencing the sustainability of Ukraine’s balance of payments is the state of the public finances. If developments in the world economy are favorable and the country recovers economic growth amid this environment, the state budget deficit will decrease in a natural way due to a rise in tax revenues. Further progress in this regard would require the consolidation of public spending. However, it would be realistic to expect the government to make efforts in this regard only in 2014, after an election cycle in Ukraine’s political life is over. Favorable conditions for moving in this direction may be created if the National Bank starts to pursue a more flexible policy regarding the exchange rate of the hryvnia. This would ensure a stable rise in lending and prices in the economy and enable the government to use monetary policy instead of fiscal policy as a tool of stabilizing economic growth.

Economic activity in Ukraine may be supported by a general improvement in the situation in the region

A high growth rate will most likely be shown in 2013 by the agricultural sector

An improvement in the balance of payments and better access to external financing will contribute to the growth of the money supply

Since late 2012, there have been signs indicating that the balance of payments is ceasing to deteriorate

January sees an increase in the international reserves

A factor influencing the sustainability of the balance of payments is the state of the public finances

Favorable conditions for strengthening the public finances may be created in the event of a more flexible exchange rate policy
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, IMF

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, IMF (IFS)

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 and the CIS Statistics Committee

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
Statistical insert

Main macroeconomic indicators of the CIS economies

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## State sector

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### State budget (% of GDP)

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### Public debt (% of GDP)

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## Inflation and banking sector

### CPI growth (%, annual average)

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### CPI growth (%)

- Azerbaijan: 23.7*
- Armenia: 19.6*
- Belarus: 32.0*
- Kazakhstan: 22.8*
- Kyrgyzstan: 30.2*
- Moldova: 23.4
- Russia: 25.7
- Tajikistan: 7.6
- Turkmenistan: 7.6
- Uzbekistan: 18.3
- Ukraine: 18.3

### Public debt (% of GDP)

- Azerbaijan: 9.9
- Armenia: 18.8
- Belarus: 10.4
- Kazakhstan: 6.2
- Kyrgyzstan: 65.9
- Moldova: 26.9
- Russia: 8.2
- Tajikistan: 36.0
- Turkmenistan: 3.5
- Uzbekistan: 19.5
- Ukraine: 12.5

### Inflation and banking sector

- Azerbaijan: 52.3
- Armenia: 8.3
- Belarus: 16.9
- Kazakhstan: 7.6
- Kyrgyzstan: 8.5
- Moldova: 12.5
- Russia: 5.0
- Tajikistan: 7.6
- Turkmenistan: 8.0
- Uzbekistan: 5.3
- Ukraine: 5.3
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