Trends:

- The world economy: uncertainty and volatility
- The United States: signs of growth, and recovery from the crisis
- Europe: hopes for a gradual resolution of the debt crisis; a slowdown of economic activity
- Asia: signs of a decline in demand for export products; cooling of the economies
- CIS:
  1) A change in terms of trade, and diverging trends in external balances
  2) An acceleration of GDP growth due to a revival of consumer and investment activity
  3) A significant alleviation of inflation pressure

Outlook and risks:

- The world economy: a slowdown of economic growth
- Commodity markets: volatility and uncertainty
- Developed economies: a decrease in the probability of large-scale easing on the part of central banks, and a continuation of the debt crisis
- Developing economies: a decline in demand for exports and a deceleration of growth
- CIS:
  1) External risks and a deceleration of economic growth this year
  2) Anti-crisis packages envisage counter-cyclical stimulating measures in oil and gas exporting countries
  3) An improvement in situation with external debt of oil and gas importing countries
Macroeconomics of the region

In 2011 the world’s debt problems, which became particularly critical in the Eurozone countries, had a negative effect on the economies of most of the countries of the region, and influenced near-term outlooks. The year was characterized by increased turbulence in financial markets caused by a string of negative economic and financial reports. Deterioration in the economic situation in developed countries affected the economies of developing countries, which experienced a drop in external demand for their products and a slowdown in foreign investment. One of the consequences of these trends was the fact that the annual economic growth rate of China, the main driver of economic processes in the Asian region in 2011, turned out to be lower than its level in 2010. The growth rate of the global trade volume slowed down from 15.4% in 2010 to 5.9% last year; and the world economy’s growth rate fell from 4.9% in 2010 to 3.3% in 2011.

The CIS economies resisted the global trend, increasing their combined growth rate from 4.4% in 2010 to 4.6% in 2011. Turkmenistan showed the highest growth rate with an increase of 14.7% and Azerbaijan had the lowest rate at 0.1%. One of the positive events of 2011 was a record agricultural crop in CIS countries. This was mainly due to the low base effect caused by the droughts in 2010. There was a weighted average increase of 20% in the region’s agricultural output after a 9% drop in 2010. Signs of recovery were also observed in the construction and financial sectors, especially in the second half of 2011. However the growth rate of industrial output slowed down in the region’s largest economies; this was mainly due to a rise in prices of industrial products, and a fall in demand.

![Figure 1.1. World economy growth (in percent)](image)

![Figure 1.2. GDP growth in CIS countries (in percent)](image)

Source: World Economic Outlook, IMF, January 2012 года

Source: national agencies, the CIS Statistics Committee
Throughout 2011 the dynamics of current account balances were above all determined by significant fluctuations in prices of mineral resources and food. In particular, the annual average price of Brent crude futures rose by 38.1% from $80.3 per barrel in 2010 to $110.9 in 2011. There were record high levels for the price of gold, which was viewed by investors as the “safe haven” amid the unpredictability and volatility. The trade surpluses of net exporters of mineral resources grew significantly, bringing in additional revenues and helping to increase their gold and foreign exchange reserves. On the other hand, net importers of petroleum products and food registered an increase in their trade deficits, which were to a considerable extent compensated for by a rise in cash remittances from labor migrants. This risk-sharing mechanism allowed most of the CIS countries to largely alleviate the growing risks and withstand the slowdown in the world economy.

The balance of payments account for the region in 2011 was characterized by an outflow of surplus capital, in the form of direct and portfolio investment from net petroleum product exporting countries; and by a net increase in liabilities on direct investment and debt capital in the labor exporting countries that are also net importers of crude oil and food. According to balance of payments data, in 2011 the region had a net capital outflow (the current account balance excluding changes in central bank reserves) that exceeded $80 billion.

As a result, the region’s balance of payments dynamics last year led to a net increase of $33 billion, about 1.5% of the region’s GDP, in the reserve assets of the central banks. The largest increase in foreign exchange reserves occurred in Azerbaijan, where they grew by 19.3% of GDP, while in Ukraine the reserves decreased by 1.7% of GDP.

In 2011, the real effective exchange rate (REER) of the national currency rose by 6.9% in Kazakhstan, 5.9% in Moldova and 4.8% in Russia, and fell by 12.7% in Belarus and 1.4% in Armenia.
An increase in foreign currency proceeds, and the economic revival in the region, had a favorable effect on CIS countries’ public revenues. This helped increase social spending, and raised the pay of public employees. Increased public revenues from exports, and a moderate fiscal policy led to the emergence of significant budget surpluses in Kazakhstan and Russia. In the countries with chronic budget deficits, the external public debt was at a high level. The economic situation made it possible to decrease external public debt in most of the CIS countries. The public debt decreased by 6% of GDP on average in Kyrgyzstan, Tajikistan and Ukraine.

The rise in prices, which was mainly caused by a surge in world prices of raw materials and food, slowed down significantly by the end of 2011. A contribution was made by some tightening of monetary policy in all CIS countries. Armenia and Ukraine had the lowest inflation rates, at 4.7% and 4.6%, respectively. Belarus experienced a severe balance of payments crisis caused by excessive stimulation of domestic demand. A significant stabilizing effect on the Belarusian economy was produced: by a sharp depreciation of the national currency in the spring and summer of 2011; by measures taken by the government; and by urgent assistance from the Anti-crisis Fund of EurAsEC, and other donors. This stopped the fall in the Belarusian ruble’s value, and slowed the rise in prices.

In 2011 there was a revival of commercial banks’ lending activity. The volume of loans issued in the national currency increased by more than 25% in Russia, by far exceeding the 2010 growth rate of 5.6%. In Kazakhstan lending in tenge rose by 21.5%. A positive feature of lending expansion in 2011 was a relatively slow rise in lending in foreign currency, at least in major CIS economies. Companies increased their investment activity in the latter half of 2011, though it remained restrained due to the private sector’s uncertainty over the risks associated with negative external factors. The share of problem loans in the loan portfolio of the CIS countries’ banking sectors gradually decreased but still remained significant.

Figure 1.5. **State budget**: (in percent of GDP)

Figure 1.6. **Monetary sphere**: CPI growth (in percent, year-on-year)
Throughout the latter half of 2011 and at the beginning of 2012, many experts revised downward their forecasts for the growth rate of the world economy. National agencies in CIS countries also decreased their forecasts. Considerable decreases occurred in consensus GDP growth forecasts: for Belarus a decrease of 3.5% from 4.6% to 1.1%; for Ukraine a decrease of 0.9%; for Russia a decrease of 0.5%; and for Moldova a decrease of 0.4%. At the same time, the GDP growth forecasts for Central Asian countries were revised upward. As a result, while in the middle of 2011 the region’s economic growth forecast for 2012 was 4.6%, at the present moment the weighted average consensus forecast is 4.1% for 2012 and 4.3% for 2013.

Given the continuing recession in the world economy, external risk factors remain because of the high dependence of the region’s large economies on external demand for mineral resources, which account for the bulk of their exports. The debt crisis in European countries may seriously affect the stability of the global financial system, which also constitutes a threat to the growth of the CIS economies. According to the EDB’s forecast, if oil prices remained at the current level of around $115 a barrel or fell slightly, the region’s weighted average economic growth rate would be 4.9% in 2012 and increase to 5.2% in 2013. A more pessimistic scenario assumes a further deterioration in the economic situation in the Eurozone and a further slowdown of the world economy. This would affect oil prices, which would fall to $90 per barrel on average in 2012 and 2013. This would slow the CIS economies’ growth to 3.2% in 2012 and to 3.9% in 2013.

More detailed possible scenarios for the world economy and economic developments in the CIS region can be found in the analytical insert of this issue of the CIS Macromonitor.

Figure 1.7. Economic growth (GDP growth): forecasts by national and international institutions (in percent)

Figure 1.8. Savings and investment (in percent of GDP): balance of private investment and savings (\(Sp-Ip\)), state budget (\(Sg-Ig\)), current account (\(X-M\))

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

Source: national agencies, estimates and forecasts by the IMF and the EDB
Azerbaijan: Growth slowdown, decrease in inflation

The rate of growth of the Azerbaijan economy slowed throughout last year. The GDP growth rate decreased from 5% in 2010 to 0.1% in 2011. The decrease was due to a significant reduction in industrial output, which fell by 5% in 2011 following a 2.6% rise in 2010. The extractive industry’s output decreased by 8.4%. This was caused by a slump in the oil and gas sector, where the production of oil and natural gas fell by 10.5% and 2.2%, respectively. This decrease was mainly caused by engineering work in the Azeri-Chirag-Guneshli oil field, which accounts for more than 80% of the nation’s hydrocarbon production. Other economic sectors continued to develop at a high pace. Agricultural output rose by 5.8% in 2011 compared with a decrease of 2.2% in the previous year. The growth rate of fixed capital expenditures increased from 21.2% in 2010 to 27.3% in 2011, and retail turnover from 9% to 10.6%.

Due to the production decrease in the oil and gas sector, 2011 saw a reduction in the volume of Azerbaijan’s exports. Crude oil and petroleum products constitute the lion’s share of all exports, accounting for 91.1% in January 2012. The volume of exports decreased by 11.3% in 2011, whereas it rose by 45.1% in 2010. At the same time the volume of imports continued to increase. The growth rate of imports rose from 7.8% in 2010 to 45.3% in 2011. Azerbaijan’s export surplus therefore decreased from 38.1% of GDP in 2010 to 38% in 2011.

Last year’s public revenues exceeded the level of 2010 by 37.7%. The share of taxes in the total volume of revenues decreased – from 35.5% in 2010 to 33.6% in 2011 – but continued to be the largest source of revenue. Expenditure was 30.8% higher in 2011 than in 2010, with social spending accounting for 28.2% of all expenditure. The government went from a budget deficit of 0.9% of GDP in 2010 to running a budget surplus of 0.6% in 2011. This was down from a surplus of 3.2% in the first six months due to the decrease in oil revenues.

In the second half of 2011, there was a decline in inflation pressure in Azerbaijan. After reaching 9.5% in February, the annual inflation rate fell to 6.8% in October and 4.8% in January 2012. This was due to a fall in world food prices in the second half of 2011. Foodstuffs and services were the biggest contributors to the inflation rate in January 2012, increasing in price by 5.7% and 5.5%, respectively, whereas prices of non-food consumer goods increased by 1.3%.

There were positive trends in Azerbaijan’s banking sector throughout 2011. The volume of bank deposits was 23.9% higher in December 2011 than a year before and the volume of loans increased year-on-year by 8.6%. The share of loans issued to households grew from 29.5% in 2010 to 33.3% in 2011. The quality of banks’ loan portfolio deteriorated compared with 2011. The share of outstanding loans increased from 5.4% in 2010 to 6.4% in 2011.
Outlook

Azerbaijan: Timid recovery, risk of inflation

Following a significant decrease in the growth rate in 2011, caused by a drastic fall in industrial output, the economy of Azerbaijan is expected to recover in 2012 and 2013. According to international experts, this will occur through the restoration of oil production to earlier levels and an increased role of the non-oil sector. International institutions’ average forecast GDP growth is 3.7% for 2012, with the IMF forecasting 3.8%, the EBRD 3.5%, the World Bank 3.1% and the ADB 4.5%. For 2013 the IMF forecast 1.9%, the World Bank 3%, and ADB 2.5%. As in 2011, the growth rate of the non-oil sector is expected to be higher than that of the oil sector. The IMF predicts that the oil sector’s growth rate will considerably increase in 2012 and reach 1%, and that the growth rate of the non-oil sector will decrease but continue to be high: 6.2% in 2012 and 4.8% in 2013. The government of Azerbaijan forecasts economic growth at 5.7% in 2012, with the growth rate of the non-oil sector at 8.6% and that of the oil sector 1.5%.

The expected global economic growth deceleration will reduce oil and gas consumption in the countries that are major importers of hydrocarbons from Azerbaijan. The non-diversified nature of the Azerbaijani economy remains therefore a major threat to the sustainable development of the nation. The bulk of Azerbaijan’s public revenues comes from taxes and transfers from the State Oil Fund of the Azerbaijani Republic (SOFAZ) – 89.5% in 2010 and 92.2% in 2011. The national economy continues to be highly dependent on the situation in global resource markets. The government forecasts Azerbaijan’s exports to total $26.6 billion in 2012, with the export of crude oil and petroleum products accounting for 92.4%. Despite the government’s optimism about the likelihood of a gradual increase in the contribution of the non-oil sector to overall economic growth, its share remains low. Investment in the oil sector still outpaces investment in the non-oil sector, which is mainly supported by funds from public sources. Last year investment in the oil sector accounted for 76.8% of the total amount.

There are currently no signs of inflation acceleration. In 2012 there may be a need for fiscal consolidation to avoid an overheated economy and an excessive rise in prices. The government forecasts an inflation rate of 6% for 2012 and 5% for 2013. The IMF expects consumer prices to rise by 7.4% in Azerbaijan in 2012. This need may run counter to the government’s 2012-2015 plans, which envisage large-scale investment in the non-oil sector. For instance, as many as 110 non-oil enterprises were established with public funds in 2011 and the government plans to establish 200 such enterprises this year.
Azerbaijan

Figure 2.1. Real economy growth: GDP and output change by sectors, (in percent, 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, IFS statistics (IMF)

Figure 2.3. State budget: (in percent of GDP)

Source: national agencies

Figure 2.4. Monetary sphere: the left scale - the central bank’s rate(in percent) and CPI growth (in percent, year-on-year); the right scale - M2 growth (in percent, year-on-year)

Source: national agencies, IFS statistics (IMF)

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

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 percent of GDP): balance of private investment and savings (Sp-Ip), state budget (Sg-Ig), current account (X-M)

Source: estimates and forecasts by national agencies and the IMF
In 2011 the economy of Armenia experienced moderate growth. The nation’s GDP rose by 4.6% compared with 2.1% in the previous year. The agricultural sector recovered from a recession caused by a drought in 2010, but the sector’s output did not hit the level of 2009.

The construction sector, which is one of the biggest contributors to GDP with 17% in 2010, continued to be on the decline last year. There was a high increase in industrial output, which rose by 14.1%.

There was a dramatic slowdown in inflation following a surge in late 2009 and the beginning of 2010, which was caused by a rise in energy and food prices. Due to a fall in raw material prices in the second half of 2010, and measures taken by the Central Bank of Armenia (CBA) to toughen its policy, the annual inflation rate fell from 11.5% in March 2010 to 4.7% at the end of the year. In September 2010, the CBA found that inflation pressure had decreased enough for monetary policy to be eased, and lowered its refinance rate from 8.5% to 8%. The rise in consumer prices remained low during the last months of 2011, and in January and February 2012. There was an acceleration of inflation in December and January due to usual seasonal factors. February 2012 saw a negative rise in prices.

Considerable progress was achieved in strengthening public finances. The state budget deficit decreased to 2.9% of GDP, from 7.5% in 2009 and 4.9% in 2010. The actual deficit proved to be lower than both the level forecast at the beginning of 2011, and the level that the government had promised to the IMF.

The nation’s foreign trade balance, which drastically deteriorated in 2008 and 2009, improved slowly. In 2011 the current account deficit reached 11%, down from 16% in 2009 and 14.5% in 2010. The significant foreign trade deficit is a major economic risk factor if the nation experiences shortfalls in external financing. The nation’s ability to resist these problems has significantly decreased since the 2008-2009 crisis due to a drastic increase in external debt. Armenia’s external public debt grew to 39.2% of GDP in 2010 from 17.8% of GDP in 2007.

The banking sector of Armenia continued to rapidly increase lending in the final months of 2011. In Q4 the volume of loans issued by banks increased by 8.3% compared with Q3. The volume of loans grew by 36.8% between December 2010 and December 2011. The high increase in lending produces an effect on the sustainability indicators of banks, such as the ratio of regulatory capital to assets, the ratio of liquid assets to the total volume of assets, and the ratio of liquid assets to short-term liabilities. Almost all these indicators have been on a gradual decline since late 2010. Only one of them, the ratio of liquid assets to short-term liabilities, is still considerably higher than its levels before the 2008-2009 crisis.
Outlook

Armenia: Structural reform, lending growth control for regaining stable growth

Despite an acceleration of economic growth in Armenia in 2011, the growth rate was still significantly lower than throughout most of the 2000s, when it averaged out at 12% between 2000 and 2007. Particular note should be taken of the extremely heterogeneous growth dynamics of economic sectors: growth is to a considerable extent concentrated in the industrial sector, mainly in mining and metallurgy. This concentration, firstly, determines the low overall growth rate of the economy. Its major sectors have yet to recover to the levels of activity registered before the 2008-2009 crisis. Secondly, it makes Armenia's economic growth unstable, as the growth may dramatically decelerate in the event of a fall in metal prices.

If there are no destabilizing external or domestic shocks during 2012 and 2013, the economy of Armenia will resume more even and rapid growth, which may reach at least 6% to 7% a year. Such a growth rate during a long period of time would make it possible to alleviate key structural problems of the nation's economy, such as extreme external imbalances and chronically high unemployment.

Maintaining macroeconomic stability will require a relatively conservative fiscal and monetary policy. Fiscal policy can be used to reduce the current account deficit, and also to minimize the risks associated with it. The existing budget guidelines provide for a budget deficit of 3.1% of GDP in 2012, and a deficit of 2.3% of GDP in 2013. As the budget implementation in 2011 produced a significantly lower-than-expected deficit, the government can now make even more serious progress in the field of fiscal consolidation.

Natural monetary-policy objectives currently include: consolidating the achieved inflation deceleration; and containing lending expansion. An increase in the lending rate may occur as a result of a premature loosening of the central bank’s policy. The lending rate is too high at present for a further increase not to carry risks for the economy. Apart from the deterioration of the sustainability indicators of the banking sector amid rapid lending growth, an issue of concern is the growth of lending in foreign currency. According to data from the Central Bank of Armenia, the share of loans in foreign currency increased from 37.4% of the total volume in June 2008 to 61.7% at the end of 2011.

Apart from macroeconomic stability, regaining a steady high rate of growth requires increasing the competitive capacity of the economy of Armenia by carrying out structural reform. Of particular importance are the “50 measures” that the government plans to take in order to improve the conditions for business activities. These include: tax and customs administration; the registration of businesses and arbitration; and the government’s plans to adopt a program aimed at drastically simplifying the regulation of business activities.
Armenia

Figure 3.1. Real **economy growth**: GDP and output change by sectors, (in percent, 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, IFS statistics (IMF)

Figure 3.3. **State budget**: (in percent of GDP)

Source: national agencies

Figure 3.4. **Monetary sphere**: the left scale - the central bank’s rate(in percent) and CPI growth (in percent, year-on-year); the right scale - M2 growth (in percent, year-on-year)

Source: national agencies

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

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 percent of GDP): balance of private investment and savings (Sp-Ip), state budget (Sg-Ig), current account (X-M)

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

Belarus: Inflation slows down, external imbalance persists

In 2011 Belarus experienced a grave balance of payments crisis caused by the excessive stimulation of domestic demand. This included pay increases in the public sector, and large-scale lending programs for businesses. Amid an increasing current account deficit, which reached 24.4% of GDP in Q1 2011, the fixed exchange rate policy implemented by the National Bank of the Republic of Belarus (NBRB) led to an almost full depletion of the foreign reserves in the first few months of 2011. In May 2011 the Belarusian authorities carried out simultaneously: a sweeping devaluation of the ruble; drastically restricted the convertibility of the national currency; and established multiple exchange rates. A number of measures were taken throughout the summer in order to restore the stability of the economy. In particular, the authorities restricted the growth of government lending, and stopped the NBRB’s direct participation in it. An increase of tax revenues, resulting from a drastic acceleration of inflation amid the depreciation of the ruble, helped keep the state budget balance in a positive zone. The NBRB considerably tightened its monetary policy, raising the base refinance rate from 10.5% at the beginning of 2011 to 45% in December. In October 2011, the authorities re-established a single exchange rate determined by trading at the Belarusian Currency and Stock Exchange. The NBRB started to pursue a relatively flexible policy regarding the ruble’s exchange rate, limiting itself to smoothing rate fluctuations.

Measures taken in late 2011 yielded certain results, and the economy of Belarus began to show signs of regaining stability. The monthly inflation rate in the country fell to 2.3% in December 2011 compared with the highest level of 13.6% in September. Inflation remained moderate in the first months of 2012. Consumer prices reportedly rose by 1.9% in January and 1.5% in February. The slowdown of inflation allowed the NBRB to slightly lower the refinance rate. Belarus posted an appreciable budget surplus for 2011 of 2.6% of GDP. The nation’s GDP growth expectedly slowed down because of the toughening of monetary and fiscal policies. In 2011 GDP rose by 5.3% compared with an increase of 7.7% in 2010. The annual growth rate largely reflected high growth rates in Q1 2011. The nation currently has a much lower growth rate. The government managed to avoid a dramatic economic recession and mass unemployment, which reduced the social costs of the crisis.

The achieved economic stability remains fragile due to the incomplete recovery of a balance in foreign trade. The current account deficit, which decreased in Q2 and Q3 – there even was a slight surplus in Q3 – increased again in Q4. It totaled $1.3 billion, or 11.4% of GDP, by the end of 2011. This significant deficit was financed with several large transfers from the Russian Federation, with the largest one of them being a $2.5 billion payment by Gazprom for the Belarus’ 50% stake in gas pipeline company Beltranshaz. This financing made it possible to stabilize the exchange rate of the national currency, which in turn helped the deceleration of inflation at the end of 2011.
Outlook

Belarus: Recovery of economic stability, risk of premature policy loosening

The main goal currently facing the nation is to consolidate the successes that were achieved in late 2011 in re-establishing the normal functioning of the economy. The still very large current account deficit remains a major threat to the just-achieved economic stability. 2011’s current account deficit was 10.2% of GDP, down from 15% in 2010. It is hard to say whether Belarus will be able to finance its current account deficit in 2012. The deterioration of the foreign trade balance in Q4 2011 was partly attributable to seasonal factors. It is difficult to evaluate them precisely as they are not very stable. Based on previous years it can be predicted that, if the authorities do not change their policy, the 2012 current account deficit may total between $2 billion and $3 billion. Taking into account that the reduced price of Russian natural gas for Belarus will probably produce an effect estimated at up to $3 billion on the nation’s current account, Belarus has a chance of balancing its external accounts next year. The nation’s current account stability is very fragile. It is dependent, for instance, on whether the favorable terms for Belarus for the supply of energy resources extend into 2013. In addition, the current account deficit may increase again if an appreciation of the ruble exchange rate – assuming that the ruble had an “overshooting effect” in 2011 – leads to some decrease in the competitiveness of Belarusian exports. Finally, the fragile stability of Belarus’ balance of payments can be easily disturbed by incautious steps taken by the authorities to boost GDP growth. A premature loosening of fiscal or monetary policy may provoke a recurrence of what happened in 2011. A new deterioration of the foreign trade balance would lead to a drastic depreciation of the national currency, which would inevitably entail a hike in inflation. This may be especially high as the administration has a significant role in keeping the growth in prices at a relatively low level by influencing local manufacturers and traders.

The economic development plan adopted by the government of Belarus in late 2011 generally meets the goal of returning the nation’s economy to the path of sustainable development, providing there is a tight fiscal policy. The government expects a budget surplus to extend into a second consecutive year, predicting it to amount to 0.6% of GDP. If the key ideas of the plan are implemented and the National Bank follows a cautious monetary and lending policy, which it tries to do now, and if the preservation of macroeconomic stability continues to be a priority over other goals of the government, the nation will probably manage to regain the previously enjoyed rates of economic growth in 2013.
Belarus

Figure 4.1. Real economy growth: GDP and output change by sectors, (in percent, year-on-year)

Source: the National Statistics Committee of Belarus

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

Source: national agencies, IFS statistics (IMF)

Figure 4.3. State budget: (in percent of GDP)

Source: national agencies

Figure 4.4. Monetary sphere: the left scale - the central bank’s rate (in percent) and CPI growth (in percent, year-on-year); the right scale - M2 growth (in percent, year-on-year)

Source: national agencies

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

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

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

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

Kazakhstan: Steady growth, slowdown in industrial production, still large share of NPLs

In 2011 the economy of Kazakhstan showed steady growth - GDP rose by 7.5% after increasing by 7.3% in 2010. Throughout 2011 the main drivers of economic growth have been domestic consumer demand and external demand for Kazakhstan’s raw materials. Retail turnover increased by 12.5% and industrial output by 3.5%. Despite the fact that the industrial sector increased output in 2011, its growth rate fell to 3.5% from 10% in 2010. That fall was due to a decrease in oil production, which was caused by the need to do engineering work, and workers’ strikes in some oil fields. Due to the low 2010 level, caused by unfavorable weather conditions, agricultural output rose by 26.7% in 2011. This partly compensated for the decrease in the growth rate of industrial output.

Exports outpaced imports, and the price of exports rose at a higher pace than imports. This created favorable terms of international trade for Kazakhstan in 2011. The volume of exports increased by 48% and imports rose by 25%, while export prices increased by 46.7% – exported raw materials increased in price by 57.9% – and import prices rose by 12.4%. According to a preliminary estimate by the National Bank of Kazakhstan, there was an export surplus of $13.6 billion in 2011, or 7.6% of GDP. This was 4.5 times the export surplus in 2010. Due to an outflow of portfolio investment in Q2, Q3 and Q4 2011, the capital and financial operations account had a deficit of 6.7% of GDP against a surplus of 5.8% of GDP in 2010.

There was a significant surplus in Kazakhstan’s consolidated budget- 10.3% of GDP compared with 8% in 2010. The share of taxes in the total public revenues grew from 79% in 2010 to 84% in 2011. Social spending again constituted the largest part of public expenditure. Education, public health and social security programs accounted for 51% of all public expenditures, up from 50% in 2010. Amid a favorable oil price situation in the world market and a relatively tight fiscal policy, public revenues increased in 2011 by 33% and expenditure by 22%.

There was a decline in inflation pressure in Kazakhstan in the second half of 2011. After the annual rise in prices reached its peak of 9% in August, inflation started to creep downwards and decreased in February 2012 to 4.7%, the lowest level since 1999. As a result the National Bank lowered the refinance rate by 0.5 points to 7% in February this year, and says that the refinance rate may be reduced again in April if the current trends continue.

The low quality of banks’ loan portfolio continued to be a problem. The share of non-performing loans grew from 33.7% in 2010 to 35.9% in 2011. Lending kept increasing throughout 2011, and ultimately had a growth rate of 15.7% against a slight decrease of 0.6% in 2010.
Outlook

Kazakhstan: Moderation in economic growth and inflation pressure

As a result of the expected decrease in the world economic growth rate, the government of Kazakhstan has revised downwards its 2012 growth forecast for the national economy. A reduction in the consumption of Kazakh mineral resources in major importing countries is expected. The government has therefore predicted a slowdown in the growth rates of export-oriented industries. The government expects a 30% decrease in crop production, and has decreased its forecast for oil production from 83 million tons to 81 million tons. The nation’s GDP is currently forecast to grow by 6%, a decrease from the 6.9% that was earlier projected. International institutions also predict a certain deceleration of Kazakhstan’s economic growth in the mid-term future. On average they forecast the nation’s GDP to grow by 6.6% in 2012 and by 5.9% in 2013. According to the EDB, if oil prices continue at the current level, Kazakhstan’s economy will show a growth rate of 6.5% in 2012, and 4.5% in 2013.

Inflation pressure in the country significantly decreased in Q3 and Q4 2011 compared with Q1, when inflation soared due to external factors such as a rise in world food prices, and a shortage of motor fuel. The National Bank of Kazakhstan predicts that the inflation rate in 2012 will be within the target band that was established by the Bank at 6% to 8%. The annual inflation rate is expected to be 5.6% to 5.8% in March and 5.9% to 6.1% in June.

In 2011 the banking sector of Kazakhstan did not solve its main problem: an improvement of the sector’s loan portfolio had been expected for several years, and did not occur. In January 2012 the share of the banking sector’s non-performing loans continued to exceed one-third of the total volume of issued loans, accounting for 35.1%. In 2011 the government took a number of measures aimed at solving the problem. In particular, the government made some amendments to tax laws and adopted the Concept of Improving the Quality of Second-level Banks’ Assets. This provided for the introduction of a number of mechanisms for clearing banks’ balances. BTA Bank, Alliance Bank and Temirbank account for the largest part of bad loans. The successful restructuring of the debts of these banks is the necessary condition for the normalization of the situation in the nation’s banking sector. The government is currently considering a new restructuring of BTA Bank’s liabilities; and the bank plans to complete its talks with creditors in the first half of 2012.

The economy of Kazakhstan continues to be highly dependent on the situation in the world’s resource markets. The predominance of the extractive sector makes the Kazakh economy vulnerable to external shocks and global trends. A slowdown in the global economy’s growth rate may lead to a decrease in external demand for Kazakh mineral resources and, consequently, to the deceleration of the nation’s economic growth. Given the fact that the greater part of public revenues directly depends on oil companies’ tax payments and contributions from the National Fund, the nation’s sustainable economic development is subject to risks associated with volatility in the world’s commodity markets.
Kazakhstan

Figure 5.1. Real economy growth: GDP and output change by sectors, (in percent, 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, IFS statistics (IMF)

Figure 5.3. State budget: (in percent of GDP)

Source: national agencies

Figure 5.4. Monetary sphere: the left scale - the central bank’s rate (in percent) and CPI growth (in percent, year-on-year); the right scale - M2 growth (in percent, year-on-year)

Source: national agencies

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

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

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

Source: estimates and forecasts by national agencies and the IMF
Kyrgyzstan: Deceleration in inflation, normalization in economy

The nation’s GDP growth slowed down in December 2011, with the year’s growth rate being 5.7%, compared with an 8% annual rate in November. This trend continued in January 2012, and was mainly due to a decrease in work to develop the Kumtor gold mine, which accounts for about 50% of the manufacturing industry’s output. Overall industrial output increased by 11% in 2011. An upward trend was also seen in the agricultural sector. Government-financed hydroelectric power plant projects, and projects aimed at the economic recovery of the south of Kyrgyzstan, were key growth drivers in construction. However the private sector did not increase its business activity in the construction sphere.

Foreign trade was a determining factor for the national economy. In 2011 there was a clear upward trend in the foreign trade deficit due to a change in the trade conditions and a decrease in the competitiveness of Kyrgyzstan’s exports. The foreign trade deficit reached 28.1% of GDP, up from 25% in 2010 and 24% in 2009. At the same time the deterioration of the foreign trade balance was to a large extent compensated for by an inflow of cash remittances, which amounted to 30% of GDP in 2011.

The real effective exchange rate of the national currency appreciated by 7.6% in 2011. This was due to a rise in consumer prices, and the som’s stable rate. The inflation rate, which reached 22.7% in June 2011, fell to 5.7% in December 2011. The main drivers of prices were non-monetary factors such as a global surge in food prices in early 2011, and a decline in the prices in the second half of 2011. The National Bank of Kyrgyzstan pursued a relatively tight monetary policy throughout the year, withdrawing excess liquidity by issuing securities and selling foreign currency. As a result, the base rate of the National Bank’s notes rose from 5.5% in December 2010 to 13.6% in December 2011.

In general, the monetary policy of the National Bank was brought into line with the budgetary policy pursued by the finance ministry. In 2011 Kyrgyzstan had a budget deficit of 5% of GDP, which was financed with external loans. 2011’s distinguishing feature was an increased internal financing of the budget through issuing government securities. The emergence of signs of economic growth contributed to a rise in public revenues from taxes, which helped the government finance the greater part of the planned expenditure, including pay increases for public employees.

The banking sector of Kyrgyzstan began 2011 with an increased level of excess liquidity, which was reduced with the assistance of the National Bank. Simultaneously, bank loans issued in the national currency rose by 20% between December 2010 and December 2011, while loans in foreign currency increased by 17.2%. There was an increase in lending to all sectors of the economy except the construction sector, which posted a decrease of 15% in 2011. Loans issued to the trade sector, which accounts for 41% of all lending, rose by 20%. The soundness and profitability of the banking sector increased last year: the share of outstanding loans shrank from 6.1% at the end of 2010 to 4.2% in December 2011, the capital adequacy factor changed insignificantly, standing at a level of 20%, while average ROA (return on assets) rose from 1.1% to 3%.
Outlook

Kyrgyzstan: Continued uncertainty in forecasts

There was a slowdown in the GDP growth rate in January and February 2012, which was caused by strikes and a slowdown in development of the Kumtor mine. As a result, the nation’s economy experienced a setback of 10.5%. Excluding the effects related to Kumtor, there was an increase of 3.5% against a 2.4% growth in January and February 2011. Agricultural output increased by 1% over the same period.

The government forecasts a GDP growth at the level of 6.1% to 7.5% for 2012. The National Bank of Kyrgyzstan is less optimistic, expecting a growth rate of 5%. The difference between the two forecasts is attributable to diverging views regarding the probability of the implementation of public investment projects. The National Bank plans to keep inflation at a single-digit rate. International institutions’ forecasts vary between 4% from the EBRD, and 6.5% from the CIS Statistics Committee.

An analysis of the dynamics of the savings/investment ratio shows that the economy of Kyrgyzstan is characterized by a chronic balance deficit in both the public and the private sector, which was financed with external loans. Preliminary data show that 2011 was an exception to the rule: the main drivers of the 5.7% economic growth were consumption and investment in the public sector, while the private sector preferred saving to spending. The state budget had a 5% deficit, and the current account deficit is preliminarily estimated to have amounted to 3% of GDP. The private sector’s net savings were 2% of GDP. The reason for the trend was a sharp increase in expenditure in the public sector, which probably had a crowding-out effect on private investment.

The government projects a budget deficit of 5.1% of GDP for 2012 and 2013. If there is a slowdown in the growth rate of the economies of Russia and Kazakhstan, a decrease may occur in the volume of cash remittances. This would affect the stability of the balance of payments. The current account deficit is forecast by the IMF at 7% of GDP. The economy of Kyrgyzstan is subject to external shocks associated with the dynamics of global economic development and depends on the world prices of food and mineral resources and changes in trade conditions. Negative trends in external factors can cause the nation’s economic growth prospects to significantly deteriorate.

Fiscal policy measures are an important internal factor that have a significant effect on inflation and growth. Throughout 2011 the government loosened its fiscal policy, which, to a certain degree, contributed to an increase in the growth rate of aggregate demand. The existence of a significant budget deficit in the medium-term, and the resulting need to finance it, pose certain risks for the forecast level of economic development. However, the risks can be reduced if public funds are spent reasonably, and the authorities continue to implement a concerted macroeconomic policy.
Kyrgyzstan

Figure 6.1. Real **economy growth**: GDP change by sectors, (in percent, 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, IFS statistics (IMF)

Figure 6.3. **State budget**: (in percent of GDP)

Source: national agencies

Figure 6.4. **Monetary sphere**: the left scale - the central bank’s rate (in percent) and CPI growth (in percent, year-on-year); the right scale - M2 growth (in percent, year-on-year)

Source: national agencies

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

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

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

Source: estimates and forecasts by national agencies and the IMF
Moldova: Economic growth amid acceleration in industrial production, slowdown in agriculture

The economy of Moldova grew by 6.4% in 2011, down from 6.9% in 2010. Private consumption, investment and exports were key growth drivers. 2011 was distinguished from 2010 by acceleration in the growth rate of industrial output, and a slowdown in agriculture. The manufacturing sector had a growth rate of 8.9%. There were especially high growth rates in the textile, building materials and food industries. The mining industry achieved a growth rate of 17.1%, but the industry does not play a significant role in the national economy. Despite a good harvest, agricultural output increased by only 4.6% compared with 7.9% in 2010, which was mainly due to a slowdown in livestock production.

Pay increases and a rise in the volume of cash remittances from abroad stimulated private consumption. This largely contributed to a 7.1% growth rate in construction and a 14.4% increase in trade, which account for 20% of the nation’s GDP. There was a rise in exports, which was attributable to increased re-exports and increased external demand for farm produce and finished products. An increase in the foreign trade deficit was to a certain extent compensated for by the rise in the volume of cash remittances, which increased by 16.8% compared with 2010 amounting to about 22% of GDP.

The increased domestic demand, and the impact of the rise in world food and energy prices, led to an increase in consumer prices in the middle of the year. The annual inflation rate rose to 9.2% in August. The National Bank of Moldova responded by raising the refinance rate by 2% in August and September, and increasing the reserve requirements for banks. This led to a slowdown of inflation, which fell to 7.8% at the end of 2011. The quick success prompted the National Bank to start loosening its monetary policy. In the period between November 2011 and February 2012, the refinance rate was lowered from 10% to 6.5%.

The state of public finances slightly improved in 2011, although there was a decline in public revenues from taxes and duties. In the middle of 2011 the government revised downwards the expenditure budget. The authorities simultaneously stepped up measures aimed at increasing the efficiency of tax collection. As a result, the state budget deficit was 2.4% of GDP at the end of 2011. The structure of expenditure financing changed towards an increase in financing from internal sources through placing government securities in the domestic market.

The economic growth stimulated the private sector’s demand for loans. The volume of lending rose by 16.9% between December 2010 and December 2011. The share of doubtful loans in the total volume of the banking sector’s loan assets decreased from 13.3% at the end of 2010 to 10.6% in 2011. The sector improved its profitability indicators. The capital adequacy factor rose from 30 to 30.42, while average ROA (return on assets) increased from 0.47 to 1.95.
Outlook

Moldova: Economic slowdown in 2012, growth acceleration in 2013

In the last two years, the economy of Moldova has showed steady growth, with the main drivers being private consumption and private investment. The national economy is characterized by a significant current account deficit of the balance of payments, and a deficit in the private sector’s balance. At the same time the public sector has consolidated considerably, having a relatively small deficit in 2011.

Both international institutions and the national government forecast a slowdown in the Moldovan economy’s growth rate for 2012. The World Bank and the IMF predict a GDP growth rate of 4%, and the EBRD forecasts 3.5%. The Moldovan economic ministry has revised downwards its GDP growth forecast from 4.5% to 3.5 - 4%. The crisis in the Eurozone may cause a decline in both the demand for Moldovan products and in the volume of cash remittances from Moldovan migrant workers. The crisis in Europe may also affect the economies of other trading partners of Moldova.

The economic ministry has developed two possible scenarios for the nation’s economic development in addition to a base-case scenario. In its best-case scenario, Moldova’s GDP growth rate in 2012 would be 1.5% to 2% higher than the base forecast, and in the worst-case scenario, it would be 1.5% to 2% lower. The government has therefore taken a number of anti-crisis measures: stabilizing public finances; providing for reducing the budget deficit in 2012 to 0.9% of GDP; and increasing expenditure for carrying out infrastructure projects.

Major structural reform tasks currently facing the government include continuing privatization, and increasing the competitive capacity and size of the private sector. The government also plans to tie agricultural subsidies to the real capacity of the budget, which would make it more flexible, and to reduce the excessively large education sector. In addition, the government plans to carry out reforms in the social sector with the assistance of the World Bank with a view to increasing targeted support of low-income groups of the population.

Due to the geographic proximity to European countries, the current recession in the Eurozone can be expected to have a significant impact on the economy of Moldova. This may in the first instance lead to a decrease in the foreign trade deficit and in the volume of remittances by migrant workers. The rise in the prices of mineral resources may also have an effect.
**Moldova**

Figure 7.1. **Real economy growth**: GDP change by sectors, (in percent, year-on-year)

![GDP growth chart](image)

Source: the National Bureau of Statistics of Moldova

Figure 7.2. **Foreign trade**: exports, imports, current account (left scale, in billions of US dollars), real effective exchange rate – REER (right scale, index – Q1 2008 = 100)

![Foreign trade chart](image)

Source: national agencies, IFS statistics (IMF)

Figure 7.3. **State budget**: (in percent of GDP)

![State budget chart](image)

Source: national agencies

Figure 7.4. **Monetary sphere**: the left scale - the central bank’s rate(in percent) and CPI growth (in percent, year-on-year); the right scale - M2 growth (in percent, year-on-year)

![Monetary sphere chart](image)

Source: national agencies

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

![Economic growth chart](image)

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

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

![Savings and investments chart](image)

Source: estimates and forecasts by national agencies and the IMF
Russia: Moderate economic growth, record low inflation

The Russian economy showed a moderate growth rate throughout 2011, with GDP rising by 4.3% in real terms. The second half of 2011 turned out to be more successful for the Russian economy: a considerable increase in consumption and investment was observed in Q3 and Q4. Agriculture was the economic sector with the highest growth rate (20%); this was partly due to the recovery from the slump caused by the 2010 drought. The manufacturing sector continued to show a relatively high growth rate; however, the effect of the low base from the recession of 2008-2009 was dissipating, and the rate was on a gradual decline. The extractive industries and utilities did not increase their output significantly in 2011. The Russian economy fully recovered from the consequences of the 2008-2009 recession and reached the pre-crisis level of real GDP in Q4 2011.

An important event of 2011 was a fall in the nation’s inflation rate to record low levels. Consumer prices in Russia rose by 6.1% last year compared with 9% in 2010. One of the reasons for the deceleration of inflation was a decline in world energy and food prices in the second half of 2011. Another factor leading to the slowdown of the price growth was the tightening of monetary policy undertaken by the Bank of Russia over the spring. The role of monetary policy in bringing down the inflation rate is highlighted by the decrease in the base inflation rate from 0.6% to 0.2% - 0.4% a month between the first and the second halves of 2011.

The 2011 fiscal results were significantly better than the forecasts made at the beginning of the year. The federal budget had a surplus amounting to 0.5% of GDP, while the consolidated state budget had a still higher surplus of 1.6% of GDP. The current account balance remained positive, reaching 5.3% of GDP by the end of 2011. This was attributable to the high prices of raw materials, and a capital outflow that was considerably larger than experts had predicted. The uncertainty caused by the difficult global economic situation, and other reasons, resulted in the Russian private sector preferring to invest its high revenues in the safest foreign assets. These revenues came from the high prices for Russian exports, and a rather loose fiscal policy. Despite the large-scale capital outflow, estimated at $80 billion, foreign investment in Russia significantly increased in 2011 to $190.6 billion, a 66% increase from 2010. Foreign direct investment increased 33.3% to $18.4 billion.

Russian banks rapidly increased lending. The volume of loans issued to legal entities and individual entrepreneurs grew by 41% between December 2010 and December 2011. The lending expansion was not impeded by the lack of liquidity that was observed in the interbank market in the last few months of 2011, and was probably caused by the capital outflow amid deterioration in the global economy. Since the lending expansion was accompanied by a considerable rise in real interest rates, it can be concluded that it was mainly driven by increased demand for loans. The demand was recovering from a drastic downturn in the aftermath of the 2008-2009 crisis.
Outlook

Russia: Growth acceleration, risks of external and fiscal instability

The current dynamics of the Russian economy appear to retain the features that can be seen in the last months of 2011: the economy is growing at a steady, though modest, rate of 4.3% a year, which fluctuates depending on seasonal factors. The inflation rate remains low, and does not show signs of acceleration. Now that the prices of Russian exports remain high, especially crude oil, the Russian economy is substantially safe from external turbulence. However the economic growth rate remains low compared with the greater part of the 2000s. The main impediment to economic growth is the relatively weak investment activity, which is attributable to uncertainty regarding the global economic outlook. Fixed capital expenditure rose by 5.8% in 2010 and 8.3% in 2011, compared with increases of 10% to 21% in the period between 2003 and 2008. If external uncertainty decreases in the latter half of 2012, a rise in investment activity and an acceleration of economic growth can be expected. If this is the case, then we predict the Russian economy to grow by 5% in 2012 and 5.5% in 2013. In the event of unfavorable developments in the global economy, which cause oil prices to fall (we consider a scenario when Brent crude falls to $90 per barrel, and remains at this level from Q2 2012 through to Q4 2013), we expect a decline in Russia’s rate of economic growth to 2% to 3% in 2012 and 2013.

The inflation rate will rise from the current low levels in the middle of 2012 when the revision of regulated tariffs takes place. This has been done usually in January, but was postponed this year for several months for political reasons. The authorities expect consumer prices in the country to rise by 5% to 6% this year. The objective of keeping inflation from exceeding this level is quite realistic considering the changes observed in 2010 and 2011 in the policy of the Bank of Russia. It started to pursue a relatively flexible exchange rate policy and show readiness to toughen the policy in the event of inflation acceleration. In fact, given the current situation, the Russian authorities could set themselves more ambitious targets regarding inflation. Its decrease to levels close to those observed in developed countries is the necessary condition for the development of the lending business in Russia, especially long-term lending. This, perhaps, is the most accessible of the major factors that can be used for maintaining an elevated economic growth rate throughout this decade.

The considerable loosening of fiscal policy in 2012 disrupted the progress in the consolidation of public finances, which took place in the previous two years. In the January to February period the federal budget had a deficit of 3% of GDP; the government forecasts a budget deficit of 1.5% of GDP for 2012. It is most likely that the budget balance will continue to fluctuate between a moderate deficit and a moderate surplus in the next few years. Given the fact that Russia’s public debt is not large compared with GDP – 8.5% in 2011 – this fiscal situation does not pose a direct threat to the nation’s economy; although things may change in the event of a steady fall in energy prices.
Russia

Figure 8.1. Real **economy growth**: GDP change by sectors, (in percent, year-on-year)

![Graph showing GDP change by sectors](image1)

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](image2)

Source: national agencies, IFS statistics (IMF)

Figure 8.3. **State budget**: (in percent of GDP)

![Graph showing state budget](image3)

Source: national agencies

Figure 8.4. **Monetary sphere**: the left scale - the central bank’s rate(in percent) and CPI growth (in percent, year-on-year); the right scale - M2 growth (in percent, year-on-year)

![Graph showing monetary sphere](image4)

Source: national agencies

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

![Graph showing economic growth](image5)

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

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

![Graph showing savings and investments](image6)

Source: estimates and forecasts by national agencies and the IMF
Tajikistan: Rise in trade and construction amid increased inflation

A rise in the GDP growth rate and a slowdown in inflation were observed in Tajikistan in 2011. The main growth drivers were trade and the services sector, which were in turn stimulated by a significant inflow of cash remittances from abroad. According to preliminary official data, the volume of cash remittances exceeded 40% of GDP last year. The construction sector also showed a high growth rate; but this rate, like the growth rate in industrial production, significantly declined due to a slowdown in the energy sector.

A rise in import prices led to a greater external imbalance. In 2011 Tajikistan had a trade deficit amounting to 29.8% of GDP, up from 29% in 2010. In the January to September period there was a current account deficit of 12.6% of GDP, compared with 4% in the same period of 2010. Cash remittances from abroad compensated for the increased trade deficit. In the first nine months of 2011 there was a slight increase in foreign direct investment, which totaled $8.8 million, and a more significant inflow of borrowed funds, which included an IMF loan. In 2011 the reserve assets of the National Bank of Tajikistan increased by $109.8 million, or 1.7% of GDP.

The inflation rate, which sharply rose in 2010 and the first half of 2011, began to decline in Q3 2011. Until the middle of 2011 there was a drastic increase in monetary aggregates due to revenue from the sale of stock of Rogun Hydroelectric Power Plant, and due to the National Bank’s increased liquidity support of commercial banks. This led to an average annual inflation rate of 14% in the summer months. The rise in prices continued at a high rate, and ended the year at 9.4%. The deceleration of inflation extended into January 2012, when its annual rate was 7.7%. The National Bank raised its refinancing rate twice in 2011 – from 8.3% at the beginning of the year to 10% in October – and then lowered it to 9% in February 2012.

The state budget had a surplus amounting to 0.8% of GDP, which was mainly due to an increase in tax revenue due to higher import prices. In order to curb inflation, the government abandoned plans to raise electric power prices. Simultaneously, there was an increase in government expenditure, above all capital investment expenditure, which account for more than 30% of all state budget expenditure.

The banking sector’s lending rose by 18.2% between December 2010 and December 2011. Particularly significant increases occurred in the volume of loans issued to agricultural producers - 46%, and to companies engaged in foreign trade - 18.5%, which combined together were almost half of the total loan portfolio of banks. The deteriorated foreign trade balance may have affected the quality of the loan portfolio. According to the National Bank, the share of outstanding loans in the total volume grew to 15% at the end of 2011 from 6.15% a year before.
Outlook

Tajikistan: Need for structural reforms amid slowdown in growth rate

Given the continued high prices of Tajikistan’s exports (aluminum and cotton), and the continued economic growth in the countries that are major trading partners, the government expects the nation’s GDP to grow by 8%, and consumer prices to rise by 10.5%. The IMF and other international agencies forecast that the GDP growth rate will slow down in 2012 to 6% and the inflation rate will be around 8%. According to the IMF, the growth deceleration would be due to the worldwide economic downturn and inflation would slow down due to a fall in food prices. The IMF considers it likely that electricity prices will rise in the next few months because in 2011 the government decided to refrain from raising them in order not to trigger inflation. Among other recommendations, the IMF suggests that the National Bank of Tajikistan should not provide targeted lending, and should require banks to take specific measures to improve their financial situation.

To finance increased social spending, it is critically important to: improve the business environment; create favorable conditions for the development of private businesses; and to improve the tax base. That is why the IMF recommends, among other measures, that the government: increase the efficiency of tax collection through amending the Tax Code; decrease the number of taxes; and reduce tax rates. It proposes a number of measures to ensure the transparency and accountability of government-controlled companies, including Talco Management Ltd. and Rogun Hydroelectric Power Plant.

If the government raises tariff rates and continues the practice of stimulating the public sector amid a deterioration of external factors, it is quite likely that the nation’s annual inflation rate will increase to above 10%. Apart from this, the economy is facing the problem of the growing external debt. The continued high trade deficit is to be financed with external loans. In particular, the IMF is expected to soon disburse the last loan tranche of $20 million, which the government plans to use to finance payments on external liabilities.

The nation’s external debt was more than $2.1 billion at the beginning of 2012. Its absolute size grew by 9.3% last year and amounted to 32.8% of GDP. The greater part of the debt is owed to China and international financial institutions, including the World Bank, the Asian Development Bank and the Islamic Development Bank. Under the government’s mid-term external borrowing program, the nation’s external debt may not exceed 40% of GDP. This year’s loan agreements currently under discussion with lenders are for financing projects in the social sphere and the financial, agricultural and transport sectors. The government expects to obtain loans on concessional terms.
Tajikistan

Figure 9.1. **Real economy growth**: GDP change by sectors, (in percent, year-on-year)

- Agricultural output growth
- Industrial output growth
- GDP growth

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)

Exports of goods
Imports of goods
Current account balance

Source: national agencies, IFS statistics (IMF)

Figure 9.3. **State budget**: (in percent of GDP)

Source: national agencies

Figure 9.4. **Monetary sphere**: the left scale - the central bank’s rate(in percent) and CPI growth (in percent, year-on-year); the right scale - M2 growth (in percent, year-on-year)

Source: national agencies

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

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

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

Source: estimates and forecasts by national agencies and the IMF
Turkmenistan: Steady economic growth amid high gas prices

The growth of the Turkmenistan economy accelerated in 2011: GDP increased by 14.7% compared with 9.2% in 2010. All sectors of the economy retained a high growth rate. Industrial output rose by 40.6%, and the production of crude oil and natural-gas condensate increased by 8.7%. In 2011 there were the following growth rates: 12.5% in the construction sector; 8% in transport and communications; 8.9% in trade; 8.1% in the services sector; and 15.3% in retail turnover. Fixed capital expenditure increased by 23.2%.

Foreign trade turnover grew by 57.2% in 2011; and the rise in exports again outpaced imports. Exports increased by 73.1%, while imports rose by 38.5%. The fast rise in exports was due to favorable external factors, which determined an increase in the export of Turkmenistan’s major products, including natural gas and cotton.

In 2011, state budget revenues exceeded the projected figure by 37.2%, while expenditures amounted to 93.7% of the planned total. Compared with 2010 the revenues were 48.3% higher, and the expenditures were 37.2% higher. According to the 2012 state budget estimates revenues will, as in previous years, mainly come from the oil and gas, chemical, and power generation industries. Due to the social focus of the budget, social spending is to be further increased this year to 76.7% of the total amount.

According to forecasts by international institutions, the economy of Turkmenistan will continue to grow at a steady rate this year. The institutions on average predict the GDP to increase by 9.1% in 2012, with the IMF forecasting 7.2%, and the EBRD and the Asian Development Bank 10%. The IMF believes that the GDP growth rate will decrease to 7% in 2013.

Despite its high rates of economic growth, Turkmenistan depends substantially on the export of natural gas, which makes the national economy vulnerable to external shocks. Natural gas accounts for about 90% of the total volume of exports, with Russia being the main importer until recently. The diversification of export destinations and the diversification of the economy in general, are an extremely important condition for the nation’s long-term sustainable economic development.
Turkmenistan

Figure 10.1. Real **economy growth**: GDP change by sectors, (in percent, year-on-year)

![GDP change by sectors](image)

Source: the CIS Statistics Committee and national agencies

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

![Foreign trade](image)

Source: national agencies

Figure 10.3. **State budget**: (in percent of GDP)

![State budget](image)

Source: the CIS Statistics Committee and national agencies

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

![Monetary sphere](image)

Source: national agencies

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

![Economic growth](image)

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

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

![Savings and investments](image)

Source: estimates and forecasts by national agencies and the IMF
**Uzbekistan: Stable economic growth expected to continue**

The economy of Uzbekistan kept growing at a steady pace last year. GDP increased by 8.3%, slightly down from 8.5% in 2010. Despite the fact that major branches of the real economic sector reduced their growth rates compared with 2010, they were on a general upturn throughout the year. For instance, industrial output increased by 6.3% against 8.3% in 2010, agricultural output by 6.6% against 6.8% in 2010 and fixed capital expenditures by 7.9% against 9.2% in 2010. In the industrial sector, the highest growth rates were achieved by the food industry (13.1%), the machine-building and metalworking industries (12.2%), and the building materials industry (11.9%). The share of foreign investment decreased from 28.8% in 2010 to 25.1% in 2011. Domestic consumption continued to rise, with the growth rate of retail turnover increasing to 16.1% from 14.7% in 2010 and the growth rate of the volume of services provided to private customers rising to 16.1% from 13.4% in 2010. An 11% increase in the production of consumer goods and a 14.5% rise in the volume of imports also indicated increased consumer demand last year.

The volume of Uzbekistan’s foreign trade totaled $25.5 billion last year, increasing by 15% from 2010, while the volume of exports grew by 15.4%. Despite the fact that the share of energy resources and petroleum products in the total volume of exports decreased – from 24.8% in 2010 to 18.5% in 2011 – these commodities remained the main export items. The volume of imports rose by 14.5% in 2011, compared with a 6.8% fall in 2010. The rise was due to a significant increase in the import of machinery and equipment, which were the principal import items, constituting 41.3% of the total volume of imports in 2011. Russia continued to be the main trading partner of Uzbekistan, accounting for 26.2% of foreign trade. The volume of trade with China increased from 9.5% in 2010 to 10.2% in 2011. In 2011 Uzbekistan had a trade surplus of $4.5 billion, or 5.8% of GDP.

The nation’s banking sector continued to be stable. In 2011 banks’ assets increased by 32.4%, and their aggregate capital grew by 30%, while the total volume of deposits rose by 36.3%. Last year saw a 35.6% increase in bank loans, with 85.3% of the total volume coming from internal sources (deposits of legal entities and individuals). Long-term investment loans for a period of more than three years accounted for more than 75% of the total volume.

Given the continued growth of internal consumption and high prices in world commodity markets, international institutions predict that Uzbekistan’s economic growth rate will continue to be at a stable level. On average they forecast a GDP growth rate of 7.6% for 2012. The IMF and the EBRD forecast 7%, while the World Bank and the Asian Development Bank predict growth rates of 8% and 8.4%, respectively. The government of Uzbekistan expects the national economy to grow by 8.2% this year. Agricultural output is forecast to increase by 5.8% and the volume of fixed capital expenditures is expected to rise by 9.3%.
Uzbekistan

Figure 11.1. **Economy growth**: GDP change by sectors, (in percent, year-on-year)

Source: the CIS Statistics Committee and national agencies

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

Source: national agencies

Figure 11.3. **State budget**: (in percent of GDP)

Source: the CIS Statistics Committee and national agencies

Figure 11.4. **Monetary sphere**: the left scale - the central bank’s rate (in percent) and CPI growth (in percent, year-on-year); the right scale - M2 growth (in percent, year-on-year)

Source: national agencies

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

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

Figure 11.6. **Savings and investments** (in percent of GDP): balance of private investment and savings (Sp-Ip), state budget (Sg-Ig), current account (X-M)

Source: estimates and forecasts by national agencies and the IMF
The economy of Ukraine had a high growth rate in 2011, with GDP increasing by 5.2% compared with 2010. Like most of the CIS member countries, Ukraine had acceleration in economic growth in the second half of 2011. It reached its maximum in Q3, when the year-on-year GDP growth rate was 6.6%. The rate decreased to 4.6% in Q4. The economic growth was of a balanced nature: there were strong upward dynamics in industrial output (7.6% increase in 2011), retail trade (13.7% increase) and agricultural output (17.5% increase). Like Russia and Kazakhstan, Ukraine had a very good grain crop in 2011. The nation’s GDP growth may have slowed down in the first months of 2012. In particular, industrial output in January was only 2% higher than in the first month of 2010.

The inflation rate fell significantly in the second half of 2011. Consumer prices rose by 4.6% between December 2010 and December 2011, in comparison with the annual inflation rate of 11.9% in June 2011. The rapid deceleration in inflation was partly attributable to a fall in energy and food prices. In addition, the outflow of capital from Ukraine, which took place amid deterioration in the world economic situation in autumn 2011, was a factor leading to the toughening of monetary policy. The effect of the capital outflow was probably amplified by the de facto fixed exchange rate regime maintained by the central bank. Inflation remained subdued in the first months of 2012. The annual inflation rate in January went down to 3.7%.

The high economic growth rate helped improve the state of public finances. In 2011, Ukraine had a state budget deficit amounting to about 1.8% of GDP, down from 5.9% in 2010, whereas the government had projected a deficit of 3.5% at the beginning of the year.

Simultaneously, the nation’s current account deficit continued to expand, amounting to $9 billion, 5.5% of GDP, by the end of the year, compared with $3 billion, 2.2% of GDP, in 2010.

The amount of lending by the banking sector rose at a faster pace in 2011. The total volume of loans issued to Ukrainian non-financial organizations increased by 14.9% between December 2010 and December 2011 against an increase of 8.4% in 2010. The growth rate of lending in Ukraine remained lower than in other CIS countries, including Russia and Armenia. Despite the relatively cautious lending climate, the sustainability indicators of the nation’s banking sector deteriorated compared with 2010. Some of the indicators, such as the ratio of liquid assets to the total volume of assets, and the ratio of liquid assets to short-term liabilities, ended the year roughly at the same levels as in 2007 and 2008. A significant increase from the pre-crisis level occurred in the capital endowment of banks: the ratio of regulatory capital to the total volume of risk-weighted assets was 21.31 in Q3 2011, compared with 13.92 in the Q4 2007.
Outlook
Ukraine: Recovery to pre-crisis growth levels, improvement of trade balance

If the prices of Ukraine’s major export items, such as metals, coal and agricultural raw materials remain high, and there is a favorable situation in the economies of neighboring countries, the economy will keep growing at a good rate as it did in 2011. The IMF’s forecast seems realistic, predicting Ukraine’s GDP to grow by 4.8% in 2012. The signs of a slowdown in the economic dynamics of the nation at the beginning of 2012 require monitoring – the growth rate of industrial output in Ukraine drastically decreased in January. Optimistic forecasts for the year may have to be revised if the turbulence of the world economy, accompanied by a deceleration in lending expansion in Ukraine, has actually affected real economic activity.

The National Bank of Ukraine will manage to retain control of inflation, keeping it at single-digit or low double-digit rates, unless the growing foreign trade deficit forces it to resort to a devaluation of the hryvnia. The inflation rate will continue to be more volatile than in neighboring countries – perhaps with the exception of Belarus – because the National Bank is following a policy close to a fixed exchange rate regime. This makes inflation in Ukraine extremely dependent on the dynamics of international capital flows.

The maintenance of the hryvnia’s exchange rate at its current level may run counter to the goal of ensuring the stability of the country’s balance of payments. The existing size of the current account deficit, which is 5.5% of GDP, maybe does not require immediate correction, but its rapid growth is a matter of concern. We are not sure that the nation will be able to continue its present exchange rate, budget and tariff policies over a long period of time. A transition to a policy of flexible exchange rate and inflation targeting would help carry out the necessary adjustment of the nation’s external balance in a smooth way. This would avoid the costs associated with drastic and sweeping changes in foreign trade and capital flows.

Another area that has to be addressed to strengthen economic stability is fiscal consolidation. Given the private sector’s current account deficit and the nation’s significant external debt, which was 80% of GDP at the end of 2011 – it would be reasonable to implement a policy where the state budget, with quasi-fiscal operation taken into account, has a surplus during a certain period of time. Some events that took place in 2011 and at the beginning of 2012 were favorable in reaching these outcomes. These included the start of pension reform, and the reaching of an agreement with Gazprom on the price of natural gas for Ukraine. The world economic situation, and budget policy restrictions imposed by the political situation in the country, will determine how far the nation can proceed in this direction.
Ukraine

**Figure 12.1. Real economy growth**: GDP change by sectors, (in percent, 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, IFS statistics (IMF)

**Figure 12.3. State budget**: (in percent of GDP)

Source: national agencies

**Figure 12.4. Monetary sphere**: the left scale - the central bank’s rate (in percent) and CPI growth (in percent, year-on-year); the right scale - M2 growth (in percent, year-on-year)

Source: national agencies

**Figure 12.5. Economic growth**: GDP growth and forecasts by national and international institutions (in percent)

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

**Figure 12.6. Savings and investments** (in percent of GDP): balance of private investment and savings (Sp-Ip), state budget (Sg-Ig), current account (X-M)

Source: estimates and forecasts by national agencies and the IMF
Analytical insert

Impact of global financial and economic instability on CIS economies

By Konstantin Fedorov and Elvira Kurmanalieva

The period from 2007 to 2012 was notable for increased turbulence in the world economy. The mortgage lending crisis in the United States was accompanied by the collapse of large financial institutions, such as Bear Stearns and Lehman Brothers. It caused a drastic fall in economic activity and slumps in stock and commodity markets in 2008. The world economy and markets recovered to a considerable degree in 2009 and 2010 under the influence of active stimulating fiscal and monetary measures, which were taken by governments throughout the world. The situation deteriorated again in 2010 and especially 2011, when a rise in the public debt of a number of countries in the Eurozone made investors doubt about the possibility of further servicing it. In 2010 and 2011 the European authorities have been looking for ways of resolving the debt crisis, granting debtors support through the European Central Bank (ECB) and through newly established mechanisms of stabilization, such as the European Financial Stability Facility (EFSF), and the European Stability Mechanism (ESM) that has yet to be made operational.

The debt crisis has begun to affect the economic situation in developed countries: in Q4 2011 the economy of the Eurozone showed a negative growth rate, and will apparently be in recession during part of 2012. The economic downturn in Europe has had a negative impact on international trade: after a rise of 1.4% in August 2011, the world trade volume fell by 1.4% in October; the exports of developed countries decreased by 2.8%; and those of developing countries fell by 2.1% in September, and 0.1% in October. As for world economic forecasts for 2012 and 2013, it is predicted that economic developments may be in line with the “inertia scenario” and be largely similar to the key developments of 2011. This scenario envisages that the Eurozone’s authorities will retain control of the situation regarding the problem countries through a large-scale write-off of Greece’s debts, and support of other debtors. This would lead to a slight recession in Europe, which would be followed by slow growth in the latter half of 2012. The United States and China will continue to have decreased growth rates. Given these circumstances, international institutions’ and national agencies’ GDP growth forecasts for the CIS economies provide a weighted average consensus forecast rate of 4.1% for 2012. The highest growth rates this year are forecast for Turkmenistan (9.1%) and Uzbekistan (7.8%), and the lowest ones for Belarus (1.1%) and Russia (3.8%).

Cash remittances by labor migrants are currently a key mechanism through which the benefits reaped by the countries that export energy resources, and agricultural raw materials, redistribute a rise in the price of their exports among all countries of the region. Despite its complexity, this mechanism of risk sharing helps the CIS countries withstand external shocks. This is why oil prices are a key factor determining the state of the economies of the CIS countries. We have developed two possible scenarios based on different levels of oil prices. The more optimistic scenario envisions that if oil prices remain at their current high level ($115 per barrel), the CIS economies will, on average, grow by 4.9% in 2012 and 5.2% in 2013.

The more pessimistic scenario predicts a decrease in oil prices to $90 per barrel on average in 2012 and 2013. This would slow the growth of the CIS economies to 3.2% in 2012, and 3.9% in 2013. It is currently possible to identify a few factors that can provoke a further deterioration in the economic situation in the world in 2012 and in the next few years:

a. New outbreaks of Eurozone’s debt crisis

A number of agreements have been reached to restructure the debts of some of the Eurozone nations. They provide for severe austerity measures. However many analysts still believe that Greece, and other European nations with high debt levels, may default and leave the Eurozone. It is pointed out that a significant positive
effect has been produced by the European authorities’ measures on the rating of the debts of the largest crisis-hit economies (Italy and Spain). Despite this the rating of government bonds of more problem nations remain low, and the cost of servicing their debts is dangerously high for them. There is therefore a probability of new outbreaks of the European debt crisis, which would require restructuring the debts of a wider range of countries. The unfavorable consequences of this process for the financial sector, and a new wave of austerity measures, will have a negative impact on the world economic situation. The CIS countries should be prepared for this. The scale of this influence will depend on which countries fall victim to new outbreaks of the debt crisis. If the crisis does not extend beyond small outlying European nations, the associated negative shocks may be rather moderate; but if the debt situation in large states goes out of control, the consequences will be extremely serious. A breakup of the Eurozone – although we do not think things will go so far – would have more grave consequences than the 2008 lending crisis in the United States. Apart from this, there is a likelihood of two negative scenarios, which are stated below:

- A moderately negative scenario will take place if one or two outlying states of the Eurozone (Greece and, possibly, Portugal) default on their sovereign debts. The seriousness of the consequences will depend on the specific measures that will be taken by the European authorities; but there are grounds to believe that this scenario will be moderately serious. In fact, a considerable part of the debts of those countries has already been written off by creditors. In addition, financial institutions, which are holders of the debts, had enough time to build up adequate reserves to deal with a default. Given this, there is a reason to hope that in the event of the moderately negative scenario, financial markets will continue normal functioning, and the corporate sector of the CIS economies will not experience a sudden cessation of external financing. The economic damage from such developments will be significant: Europe will suffer a deeper and lengthier recession, which may last throughout 2012. One can expect a fall in process of all resource commodities. We estimate that in the event of this scenario, Brent crude oil will fall in price to about $90 per barrel and remain at around this level throughout the year (the price level determined by the budget situation of Saudi Arabia, and the maximum oil production costs). The impact of such an outcome on the CIS countries will be significant but not disastrous: the region will continue to have a positive growth rate.

- A scenario of a large-scale crisis in the Eurozone, which we consider unlikely, will take place if the European authorities lose control of the debt crisis. In this case, the cost of servicing the public debt may become an impossible task for large states such as Italy and Spain. The consequences of their default on their liabilities would be an extremely heavy blow to European banks, and also to the international financial sector in general. Collapses of large banks and investment companies would not be unlikely. Under such circumstances, a very significant fall in prices of resources would be highly probable. The price of Brent crude would stand at an estimated $60 a barrel throughout the greater part of 2012. In this case, the CIS countries would certainly fail to avoid a recession. The governments would have to revise their budgets for the next few years, and face a significant increase in their external debt.
b. **Fiscal consolidation in the United States**

A decrease in the US government’s expenditure due to the need to regain control over the growing public debt is another source of risk for the CIS countries. Although this move is expected to have a positive long-term effect, its immediate effect will be a slowdown of growth, or an economic recession, in the United States. There could possibly be a fall in the world prices of raw materials that constitute the bulk of CIS exports. The fact that CIS countries do not have significant direct trade ties with the United States does not matter in this event. Trade in crude oil, metals and grain is global, and a decline in demand for them in one part of the world will affect the price of resources exported by CIS countries.

It should be noted that there are grounds to hope that the impact of the situation in the USA on the rest of the world will be less strong than the 2008 crisis. Firstly, even a rather drastic reduction of public expenditure can exert only limited influence on the US economy. There is no reason to expect that it will lead to financial collapses similar to the bankruptcy of Lehman Brothers. Secondly, the political struggle in the USA in the run-up to presidential and congressional elections, scheduled for November 2012, prevents radical steps from being taken with regard to budgetary policy; despite the heated discussions. Fiscal policy in the United States may be really toughened only in 2013. Thirdly, the situation in the US economy is generally changing for the better. If this trend continues, fiscal consolidation, which is needed to restore the stability of public finances, may turn out to be less radical than seems necessary today.

Earlier consolidation may be provoked by a large-scale crisis in another part of the world, most likely in Europe, if such a crisis makes investors doubt the creditworthiness of the US government.

c. **Economic slowdown, fall in real estate prices in China**

The Chinese economy shows a decline in its growth rate again. In 2009 and 2010 there was a recovery in economic growth as a result of stimulating measures on the part of the government. This facilitated the task for the rest of the world to come out of the crisis. This is partly due to the fact that the Chinese government revised its policy priorities in 2011 because of overheating of the economy. This had led to acceleration of inflation and, in particular, a sharp rise in real estate prices. The government took measures to curb lending expansion. They have proved efficient: the inflation rate has started to decline, and the real estate price boom is gradually fading away. In addition, the slowdown in China’s economic growth was caused by the influence...
of longer-term factors: the difficult situation in Western economies led to a fall in demand for Chinese exports, especially as the rise in prices and pay in the country made its products less competitive. There is currently a probability that the Chinese government will somewhat loosen its monetary policy. This is because the objectives that it set itself last year while toughening the policy have generally been achieved. If the Chinese economy escapes a crisis, China may even become a source of positive effects for the world economy in 2012. This is especially the case in the financial sector, which accumulated a significant volume of bad loans during the recent lending expansion. Since the government still has very large financial reserves, this possibility looks rather likely; but one should not rule out that things will take a different, unfavorable turn. A financial crisis in China, like a premature fiscal consolidation in the USA that we talked about above, may be provoked by unfavorable developments outside the country, for instance in Europe. If it becomes a reality, it will have a significant impact on the world economy.

In general, we expect that the Chinese authorities will manage to prevent crisis phenomena in the financial sector. In this regard, we view the possibility of a financial crisis in China as rather an additional negative factor if other negative scenarios take place, especially the scenario of a large-scale crisis in the Eurozone that we described above. If the Chinese economy’s annual growth rate falls to 4% or 5%, this will be a test for all CIS economies, especially the Central Asian economies, which have closer ties with China.

d. Rise in energy and food prices

In the above sections, we described a number of factors that may lead to a fall in the price of commodities exported by CIS countries, and that may complicate access to international finance markets for the countries’ banks and companies. There is also a danger of the opposite. If the world’s leading economies regain their growth rates, if their central banks start to pursue a very loose monetary policy, and if there are restricted opportunities to increase the production of energy and food raw materials, then energy and food prices may start rising at an unexpectedly high rate. In this case – although a drastic rise in these prices would be beneficial to the region in general – some CIS countries may face difficulties, and need support from other countries in the region.

A sharp rise in world energy and food prices will lead to a situation where the CIS countries will have a dramatic rise in the prices of raw materials instead of a fall, which may be dangerous to the most vulnerable economies of the region. Kyrgyzstan and Tajikistan are the CIS member states most vulnerable to a dramatic rise in food prices. The UN Food and Agriculture Organization (FAO) has entered both countries in its list of nations facing food shortages. FAO estimates that about one-fourth of Kyrgyzstan’s residents, and one-third of the residents of Tajikistan, are undernourished. This situation may deteriorate because of their dependence on food imports, especially from Kazakhstan and Russia. A sharp increase in oil prices may cause damage to the CIS countries that have energy intensive economies, but do not have substantial reserves of oil and natural gas, and a large safety margin in terms of balance of payments. This may be true for Belarus and, although to a much lesser extent, for Ukraine.
### Statistical insert

#### Main macroeconomic indicators of the CIS economies

<table>
<thead>
<tr>
<th></th>
<th>Azerbaijan</th>
<th>Armenia</th>
<th>Belarus</th>
<th>Kazakhstan</th>
<th>Kyrgyzstan</th>
<th>Moldova</th>
<th>Russia</th>
<th>Tajikistan</th>
<th>Turkmenistan</th>
<th>Uzbekistan</th>
<th>Ukraine</th>
</tr>
</thead>
<tbody>
<tr>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>National accounts</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>GDP ($ bln)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2005-2008</td>
<td>29.1</td>
<td>8.1</td>
<td>43.3</td>
<td>93.9</td>
<td>5.3</td>
<td>4.2</td>
<td>1181.2</td>
<td>3.5</td>
<td>29.1</td>
<td>22.6</td>
<td>129.7</td>
</tr>
<tr>
<td>2009</td>
<td>44.3</td>
<td>8.5</td>
<td>49.2</td>
<td>108.8</td>
<td>4.7</td>
<td>5.4</td>
<td>1231.3</td>
<td>4.9</td>
<td>53.2</td>
<td>33.5</td>
<td>117.1</td>
</tr>
<tr>
<td>2010</td>
<td>51.8</td>
<td>9.4</td>
<td>55.1</td>
<td>150.3</td>
<td>4.8</td>
<td>5.8</td>
<td>1478.3</td>
<td>5.6</td>
<td>57.0</td>
<td>39.0</td>
<td>136.5</td>
</tr>
<tr>
<td>2011</td>
<td>64.1</td>
<td>10.2</td>
<td>56.5</td>
<td>186.0</td>
<td>5.9</td>
<td>7.0</td>
<td>1856.1</td>
<td>6.5</td>
<td>165.2</td>
<td></td>
<td></td>
</tr>
<tr>
<td>GDP real growth (%)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2005-2008</td>
<td>24.2</td>
<td>11.9</td>
<td>9.6</td>
<td>8.1</td>
<td>5.0</td>
<td>5.8</td>
<td>7.1</td>
<td>7.4</td>
<td>12.5</td>
<td>8.3</td>
<td>5.0</td>
</tr>
<tr>
<td>2009</td>
<td>9.3</td>
<td>-14.1</td>
<td>0.2</td>
<td>1.2</td>
<td>2.9</td>
<td>-6.0</td>
<td>-7.8</td>
<td>3.9</td>
<td>6.1</td>
<td>8.1</td>
<td>-14.5</td>
</tr>
<tr>
<td>2010</td>
<td>5.0</td>
<td>2.1</td>
<td>7.6</td>
<td>7.3</td>
<td>-0.5</td>
<td>6.9</td>
<td>4.3</td>
<td>6.5</td>
<td>9.2</td>
<td>8.5</td>
<td>4.2</td>
</tr>
<tr>
<td>2011</td>
<td>0.1</td>
<td>4.6</td>
<td>5.3</td>
<td>7.5</td>
<td>5.7</td>
<td>6.4</td>
<td>4.3</td>
<td>7.4</td>
<td>14.7</td>
<td>8.3</td>
<td>5.2</td>
</tr>
<tr>
<td>Final consumption (% of GDP)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2005-2008</td>
<td>45.8</td>
<td>83.0</td>
<td>70.6</td>
<td>56.9</td>
<td>107.5</td>
<td>112.7</td>
<td>66.4</td>
<td>104.8</td>
<td>78.0</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2009</td>
<td>53.9</td>
<td>93.7</td>
<td>72.3</td>
<td>59.0</td>
<td>96.7</td>
<td>113.5</td>
<td>75.4</td>
<td>106.8</td>
<td>84.6</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2010</td>
<td>53.5</td>
<td>94.0</td>
<td>71.3</td>
<td>56.2</td>
<td>102.9</td>
<td>115.8</td>
<td>71.2</td>
<td>104.1</td>
<td>84.5</td>
<td></td>
<td></td>
</tr>
<tr>
<td>2011</td>
<td>95.3</td>
<td>66.7</td>
<td></td>
<td>116.7</td>
<td></td>
<td>68.3</td>
<td></td>
<td></td>
<td>83.9</td>
<td></td>
<td></td>
</tr>
<tr>
<td>Gross capital formation (% of GDP)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2005-2008</td>
<td>27.9</td>
<td>36.3</td>
<td>33.1</td>
<td>32.0</td>
<td>24.1</td>
<td>35.2</td>
<td>22.7</td>
<td>17.2</td>
<td>29.7</td>
<td>25.9</td>
<td></td>
</tr>
<tr>
<td>2009</td>
<td>18.9</td>
<td>34.7</td>
<td>37.3</td>
<td>29.5</td>
<td>27.3</td>
<td>23.1</td>
<td>18.9</td>
<td>17.2</td>
<td>31.0</td>
<td>17.1</td>
<td></td>
</tr>
<tr>
<td>2010</td>
<td>17.1</td>
<td>33.4</td>
<td>41.2</td>
<td>25.3</td>
<td>28.4</td>
<td>23.5</td>
<td>22.8</td>
<td>18.8</td>
<td>30.7</td>
<td>18.5</td>
<td></td>
</tr>
<tr>
<td>2011</td>
<td>27.4</td>
<td>36.3</td>
<td>25.3</td>
<td>24.5</td>
<td>25.0</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td><strong>State sector</strong></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>State budget (% of GDP)</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>2005-2008</td>
<td>0.0</td>
<td>-0.9</td>
<td>1.9</td>
<td>0.2</td>
<td>0.1</td>
<td>6.8</td>
<td>-1.3</td>
<td>5.0</td>
<td>5.5</td>
<td>-1.3</td>
<td></td>
</tr>
<tr>
<td>2009</td>
<td>-0.7</td>
<td>-7.5</td>
<td>-0.4</td>
<td>5.2</td>
<td>-1.5</td>
<td>-6.3</td>
<td>-6.3</td>
<td>1.3</td>
<td>7.6</td>
<td>2.8</td>
<td>-4.1</td>
</tr>
<tr>
<td>2010</td>
<td>-0.9</td>
<td>-4.9</td>
<td>-1.8</td>
<td>8.0</td>
<td>-4.9</td>
<td>-2.5</td>
<td>-3.5</td>
<td>1.0</td>
<td>2.3</td>
<td>4.9</td>
<td>-5.9</td>
</tr>
<tr>
<td>2011</td>
<td>0.6</td>
<td>-2.9</td>
<td>2.4</td>
<td>10.3</td>
<td>-5.0</td>
<td>2.4</td>
<td>1.6</td>
<td></td>
<td></td>
<td>-1.8</td>
<td></td>
</tr>
<tr>
<td>Public debt (% of GDP)</td>
<td>Azerbaijan</td>
<td>Armenia</td>
<td>Belarus</td>
<td>Kazakhstan</td>
<td>Kyrgyzstan</td>
<td>Moldova</td>
<td>Russia</td>
<td>Tajikistan</td>
<td>Turkmenistan</td>
<td>Uzbekistan</td>
<td>Ukraine</td>
</tr>
<tr>
<td>-----------------------</td>
<td>------------</td>
<td>---------</td>
<td>---------</td>
<td>------------</td>
<td>------------</td>
<td>---------</td>
<td>--------</td>
<td>------------</td>
<td>--------------</td>
<td>------------</td>
<td>---------</td>
</tr>
<tr>
<td>2005-2008</td>
<td>8.8</td>
<td>18.8</td>
<td>10.4</td>
<td>9.0</td>
<td>60.0</td>
<td>26.9</td>
<td>8.2</td>
<td>36.0</td>
<td>3.5</td>
<td>19.5</td>
<td>12.5</td>
</tr>
<tr>
<td>2009</td>
<td>7.7</td>
<td>40.2</td>
<td>22.2</td>
<td>12.3</td>
<td>53.7</td>
<td>24.2</td>
<td>7.2</td>
<td>36.6</td>
<td>2.6</td>
<td>11.0</td>
<td>23.2</td>
</tr>
<tr>
<td>2010</td>
<td>7.4</td>
<td>39.2</td>
<td>23.3</td>
<td>14.4</td>
<td>57.5</td>
<td>26.3</td>
<td>7.8</td>
<td>36.7</td>
<td>11.8</td>
<td>10.0</td>
<td>29.9</td>
</tr>
<tr>
<td>2011</td>
<td>7.5</td>
<td>41.7</td>
<td>52.5</td>
<td>12.0</td>
<td>47.9</td>
<td>23.4</td>
<td>8.5</td>
<td></td>
<td></td>
<td></td>
<td>27.1</td>
</tr>
</tbody>
</table>

<table>
<thead>
<tr>
<th>Inflation and banking sector</th>
</tr>
</thead>
<tbody>
<tr>
<td>CPI growth (%, annual average)</td>
</tr>
<tr>
<td>2005-2008</td>
</tr>
<tr>
<td>2009</td>
</tr>
<tr>
<td>2010</td>
</tr>
<tr>
<td>2011</td>
</tr>
</tbody>
</table>

| M2 growth (%, annual average) | Azerbaijan | Armenia | Belarus | Kazakhstan | Kyrgyzstan | Moldova | Russia | Tajikistan | Turkmenistan | Uzbekistan | Ukraine |
| 2005-2008                  | 78.4       | 47.0    | 44.7    | 46.7        | 35.7       | 34.6    | 38.8   | 71.9       | 30.0         | 41.2       | 41.2    |
| 2009                       | 5.7        | -27.7   | -3.8    | 19.2        | 3.7        | -9.4    | -4.4   | 26.1       | 27.5         | 40.8       | 5.9     |
| 2010                       | 29.8       | 8.5     | 29.8    | 31.1        | 26.6       | 20.1    | 33.8   | 28.2       | 52.4         | 14.0       |         |
| 2011                       | 33.3       | 26.1    | 44.1    | 22.0        | 21.9       | 18.6    | 23.5   | 52.3       |              | 20.2       |         |

| Bank credit growth (%, annual average) | Azerbaijan | Armenia | Belarus | Kazakhstan | Kyrgyzstan | Moldova | Russia | Tajikistan | Turkmenistan | Uzbekistan | Ukraine |
| 2005-2008                  | 73.8       | 45.2    | 50.3    | 59.9        | 57.4       | 38.5    | 47.1   | 68.1       |              | 56.4       |         |
| 2009                       | 20.8       | 21.3    | 51.2    | 9.3         | 5.1        | 0.7     | 16.2   | -39.0      |              |            |         |
| 2010                       | 22.9       | 23.9    | 34.8    | -5.3        | 1.1        | 5.2     | 2.1    | 23.6       |              | 5.8        |         |
| 2011                       | 5.8        | 36.8    | 59.2    | 7.3         | 12.0       | 15.0    | 19.7   | 16.9       |              | 10.5       |         |

<table>
<thead>
<tr>
<th>Exchange rate (annual average, national currency per US$)</th>
</tr>
</thead>
<tbody>
<tr>
<td>2005-2008</td>
</tr>
<tr>
<td>2009</td>
</tr>
<tr>
<td>2010</td>
</tr>
<tr>
<td>2011</td>
</tr>
<tr>
<td>External sector</td>
</tr>
<tr>
<td>-----------------</td>
</tr>
<tr>
<td><strong>Current account balance (% of GDP)</strong></td>
</tr>
<tr>
<td>2005-2008</td>
</tr>
<tr>
<td>2009</td>
</tr>
<tr>
<td>2010</td>
</tr>
<tr>
<td>2011</td>
</tr>
<tr>
<td><strong>Trade balance (% of GDP)</strong></td>
</tr>
<tr>
<td>2005-2008</td>
</tr>
<tr>
<td>2009</td>
</tr>
<tr>
<td>2010</td>
</tr>
<tr>
<td>2011</td>
</tr>
<tr>
<td><strong>Current transfers (% of GDP)</strong></td>
</tr>
<tr>
<td>2005-2008</td>
</tr>
<tr>
<td>2009</td>
</tr>
<tr>
<td>2010</td>
</tr>
<tr>
<td>2011</td>
</tr>
<tr>
<td><strong>Foreign direct investments (% of GDP)</strong></td>
</tr>
<tr>
<td>2005-2008</td>
</tr>
<tr>
<td>2009</td>
</tr>
<tr>
<td>2010</td>
</tr>
<tr>
<td>2011</td>
</tr>
<tr>
<td><strong>Gross international reserves (in months of imports)</strong></td>
</tr>
<tr>
<td>2005-2008</td>
</tr>
<tr>
<td>2009</td>
</tr>
<tr>
<td>2010</td>
</tr>
<tr>
<td>2011</td>
</tr>
<tr>
<td><strong>Gross external debt (% of GDP)</strong></td>
</tr>
<tr>
<td>2005-2008</td>
</tr>
<tr>
<td>2009</td>
</tr>
<tr>
<td>2010</td>
</tr>
<tr>
<td>2011</td>
</tr>
</tbody>
</table>