

The Kyrgyz Republic Recent Economic Developments: January-June 2004

Summary

The Kyrgyz economy demonstrated remarkable growth in January-June of this year over the same period of last year: the real GDP grew by 9.2 percent. This growth was provided by continued development of industry and services. Positive characteristic of industrial development is a significant growth of non-gold industry. Gold industry increased also and contributed 1.8 percentage points to the real GDP growth. Services, the most dynamically developing sector, grew by 9 percent. Evolving of construction of third phase of Bishkek-Osh road mainly explains recovery of construction sector. Inflation was low: consumer prices increased by only 1 percent in January-June. The real effective exchange rate depreciated by 2.3 percent, and the real exchange rate of som against US dollar was relatively stable. Current account deficit declined by 0.8 percentage points of GDP due to increase in inflow of private transfers, while trade and income balances deteriorated. Wider use of banking transactions, which are better covered in the BOP statistics, and presumably growth in number of Kyrgyz citizens working abroad explain the increase in inflow of private transfers. Merchandise exports increased by 45 percent and imports by 46 percent. Fiscal deficit of the general government declined to 2.4 percent of GDP from 2.8 percent in January-June of 2003, mainly due to increase in tax collections on imports. In April the government increased salaries of doctors and teachers by 15 percent.

1. Growth

- **Real GDP** grew by 9.2 percent in January-June of this year over the first half of last year, based on contribution of services (3.9 percentage points), gold production (1.8 percentage points), and non-gold industry (1.9 percentage points). Non-gold GDP grew by 7.4 percent.
- **Non-gold industrial output** increased by 12.2 percent in real terms. Among industries, food processing and production of construction materials were the strongly developing industries, and accounting more than 1/3 of non-gold industrial output. Growth of both industries was led by increase in domestic and external demand.
- **Agricultural output** increased by 2.1 percent. Seasonally, harvesting starts at the end of second quarter; therefore, third quarter will better characterize agricultural sector development.
- **Construction sector output** increased by 4.2 percent. Construction of

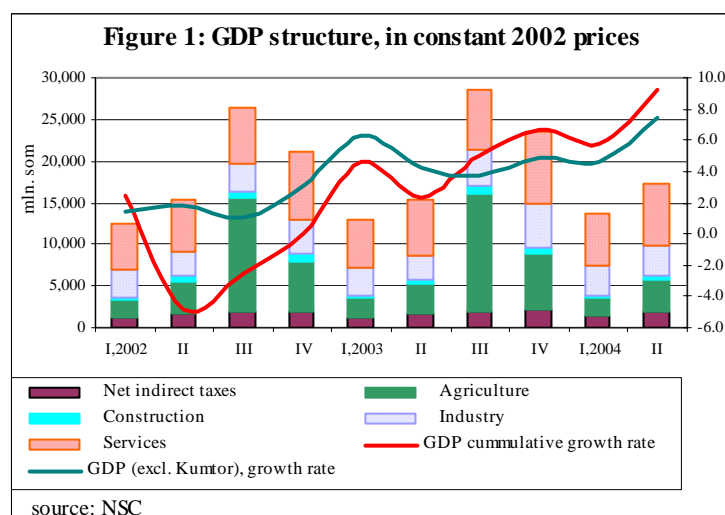


Table 1: Growth rates of GDP and value added of sectors

	2001	2002	2003	6 m. 2003	6 m. 2004
GDP	5.3	0.0	6.7	2.3	9.2
GDP excl. Kumtor-gold	4.1	3.1	4.9	4.3	7.4
Agriculture	7.3	3.0	3.8	-3.4	2.2
Construction	4.0	1.4	-6.8	-9.7	4.2
Industry	4.8	-13.4	17.9	3.1	17.5
Services	3.3	4.4	5.8	6.1	8.9

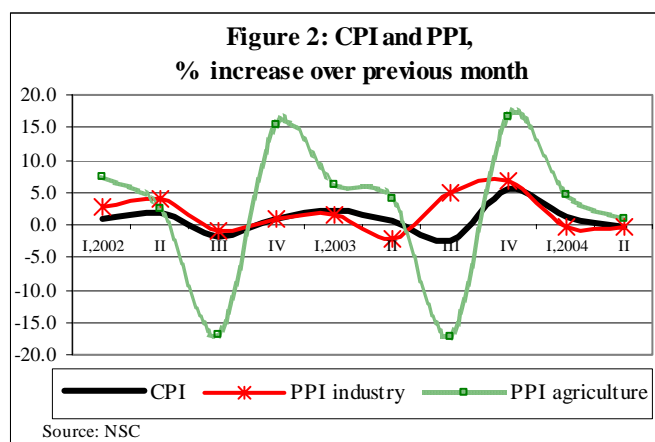
Source: NSC

“Bishkek-Osh” road increased by 3.8 times, reflecting development of the third phase of the “Bishkek-Osh” investment project. Construction in power generation sector continued to increase, albeit still at low level. Significant increase in real estate prices stimulated increase in construction of real estates.

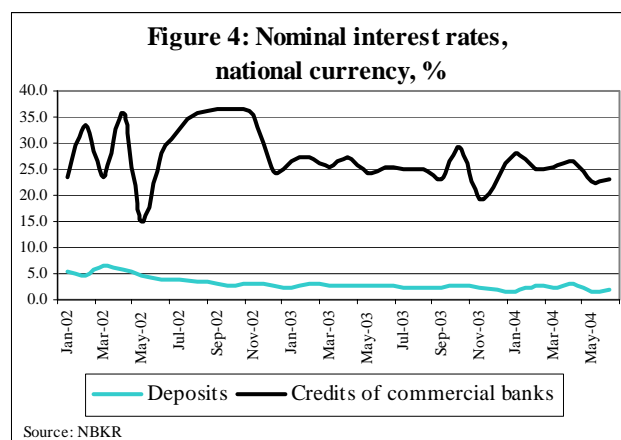
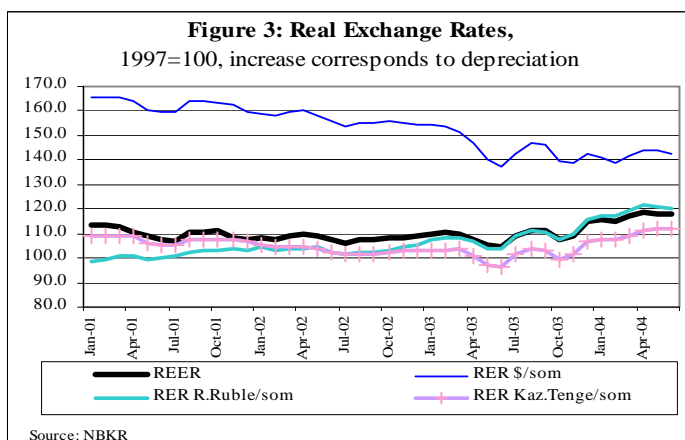
- **Services** grew by 8.9 percent, reflecting continuing growth in trade, other individual services, and hotel and food services. Transport services (mainly railway) increased by 2.7 percent, reflecting an increase in external trade turnover. Communication services also continued to demonstrate rapid growth and increased by 14.9 percent.

2. Inflation, exchange rate, and interest rates.

- **Consumer prices** (June to December) increased only by 1.0 percent; however, average consumer prices in December-June increased by 4.1 over the same period of last year, reflecting increase in prices on meat, milk and wheat. Increase of prices on wheat reflected lower production of wheat in 2003 compared with previous year. Prices on fruits and vegetables declined this year, reflecting their good yield in 2003.



- **The real effective exchange rate** depreciated by 2.3 percent over its December level. The real exchange rate of som against US dollar was stable; however, it depreciated by 3.7 percent against Russian ruble and by 4.9 percent against Kazakh tenge.
- **Interest rates** on commercial bank loans and deposits remained relatively stable, albeit the rates on loans are at high level.



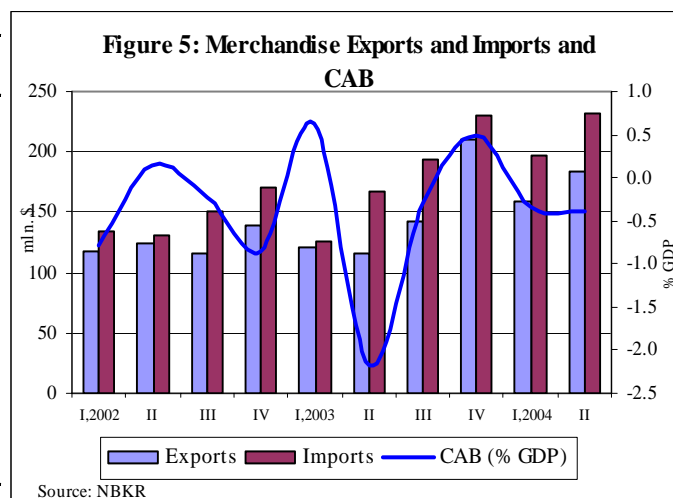
3. External Sector

- **Current account deficit (CAD)** declined to 0.7 percent of GDP from 1.5 percent of GDP in the first half of 2003. All items of current account increased substantially, and especially inflow of private transfers, explaining downward trend of CAD of this year.

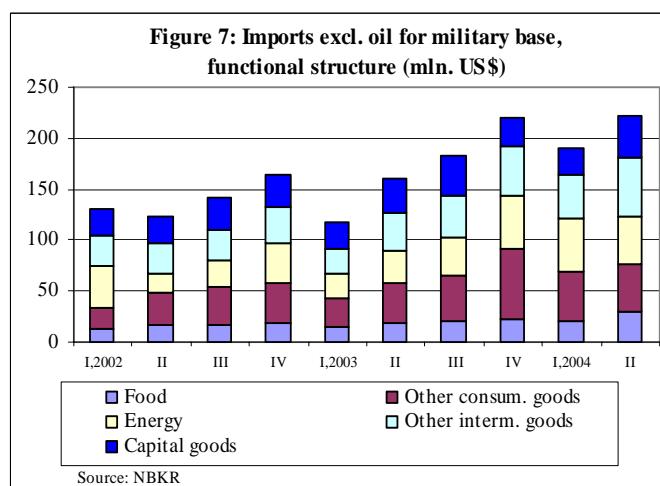
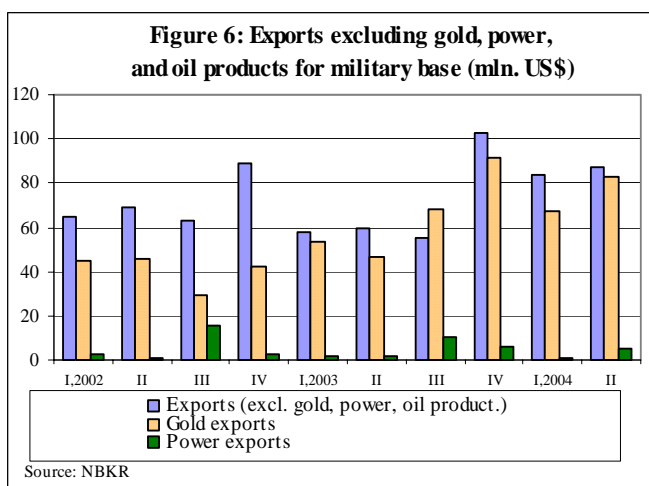
Table 2: Current Account Balance (million US\$)

	2001	2002	2003	6 m. 2003	6 m. 2004
CAB (% GDP)	-1.2	-1.7	-1.3	-1.5	-0.7
CAB (million US\$)	-19	-27	-26	-29	-16
Merchandise Exports	480	498	590	237	343
Gold exports	227	163	260	100	150
Merchandise Imports (fob)	440	552	673	274	394
Exports of services	80	138	146	62	80
Imports of services	125	145	136	68	85
Net income	-66	-56	-62	-23	-38
interest payments (scheduled)	-39	-32	-27	-13	-20
Current Transfers	51	88	112	37	78

Source: NBKR



- **Merchandise exports** increased by 45 percent. Gold exports, which accounted about 44 percent of total exports, increased by 50 percent, due to increase of gold export volume by 31 percent and export price - by 15 percent. Exports, excluding gold, fuel for military base, and power, increased by 46 percent, which is explained largely by increase in exports of sugar, garments, vegetables, and recovery of exports of construction materials and scrap metals. Russia, Kazakhstan, Uzbekistan and China remain traditional export partners.
- **Merchandise imports** (c.i.f.) increased by 46 percent. Imports of all trade categories, especially oil products, increased substantially. Imports of investment goods increased by 12 percent. The Kyrgyz Republic continues to import mainly from Russia, Kazakhstan, Uzbekistan, and China.



4. General Government budget

- **Fiscal deficit** (accrual) of the general government budget was recorded at 2.4 percent of GDP, compared to 2.8 and 2.6 percent in January-June of 2002 and 2003, correspondingly. This reduction in deficit reflects mainly improvement in revenue collection performance.
- **The total general government revenue** amounted to 10.7 percent of GDP, compared to 10.2 percent in January-June 2003. Tax collections, which increased from 7.8 percent of GDP to 8.7

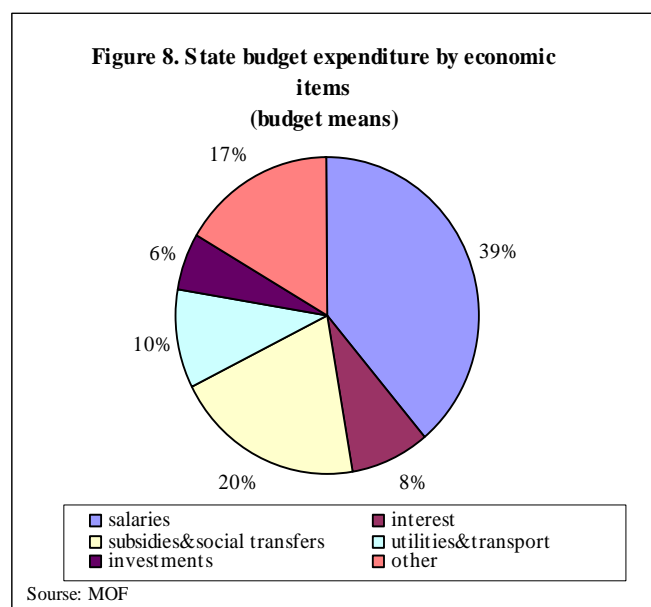
percent, were the main source of revenue increase. Among taxes, collection of VAT and excises on imports increased most significantly (by 1.7 billion soms), reflecting increase in imports. Substantial decline in transfer of the National Bank's profit to the state budget caused decrease in non-tax revenues by 0.5 percentage points, despite some increase in collection of other non-

Table 3: General government budget (% of GDP)

	January-June				
	2002	2003	2002	2003	2004
Total revenue	22.7	22.9	9.8	10.2	10.7
Taxes	17.5	17.8	7.6	7.8	8.7
Income and profit tax	2.9	2.5	1.2	1.2	1.2
VAT	6.4	6.6	2.7	2.7	3.4
Excises	1.4	1.4	0.6	0.6	0.7
Customs	0.6	0.5	0.2	0.2	0.2
Payroll	3.6	3.5	1.6	1.7	1.8
Others	2.7	3.2	1.2	1.4	1.5
Non-tax and Capital	4.1	4.6	1.8	2.3	1.8
Grants	1.1	0.6	0.3	0.1	0.2
Total expenditure	28.5	28.0	12.9	13.0	13.3
Current	22.6	23.2	10.5	11.0	11.3
Wages	5.3	5.7	2.3	2.2	2.4
Transfers&subsidies	9.3	8.7	4.3	3.9	3.8
Interest	1.9	1.6	0.9	0.8	1.1
Goods and services	6.1	7.2	2.9	4.1	4.0
Capital	6.0	4.8	2.4	2.0	2.0
Foreign financed PIP	4.7	3.6	2.1	1.6	1.6
Net lending	-0.6	-0.5	-0.3	-0.2	-0.2
Balance	-5.2	-4.6	-2.8	-2.6	-2.4

Source: the MOF and WB staff calculations

tax revenues, including special means.



- General government expenditure** increased by 0.3 percentage points of GDP, and reached 13.3 percent of GDP. Above noted increase in salaries of doctors and teachers in April of this year explains overall increase of expenditures on salaries by 0.2 percent of GDP. There was an increase in interest payments from 0.8 to 1.1 percent of GDP. Capital expenditure remained at 2003 level. Foreign-financed part of PIP was executed at 41 percent, and government co-financing part only at 25 percent. The Social Fund fully financed labor pensions, albeit partially using funds from Employment and Health Insurance Funds.

5. The main legislative changes with economic impact in January-June 2004

- The law *on technical regulation basis* (approved on May 22, 2004) sets up the main principles to be applied in area of technical regulation.
- The new law *on public procurement* (approved on May 24, 2004) establishes more transparent legal and economic principles in area of procurement of goods, works, services (including consulting services) for public needs, compared with the previous law
- A new *labor code* approved by the Parliament on May 25, 2004. It lays down, inter alia, rights of employers to establish their associations for representation of their interests. Rights of employees were adjusted to market economy condition.
- A new law *on collateral* that is based on existing laws on collateral and on mortgage, approved by the Parliament on June 8, 2004.
- Amendments to the law *on legal and normative acts* (approved on June 11, 2004) envisages more strong involvement of civil and business societies in the process of law making, and demands draft legislation to be published in mass media for public discussions, and approved business-related legislation to come into force not earlier than three months from the date of the official publication.
- Amendments to *the law on investments* (signed by the President on June 14, 2004) withdraws the statement on equal treatment of local and foreign investors.
- Amendments to *the law on joint stock companies* (approved on June 24, 2004; but not yet signed by the President) introduces some changes in decision-making process for JSCs.
- Addenda to *the law on licensing* (approved on June 24, 2004, comes into force in 2005) introduces requirements to license customs-associated services.
- Amendments to *the Tax Code* (signed by the President on July 1, 2004) introduces definitions for the exports of services and works and tax rules for these activities.
- The decree #108 of the State department on antimonopoly policy (passed on May 14, 2004) approves the price list of permits, issued by the executive agencies.
- Agreement between governments of Kyrgyz Republic and Republic of Kazakhstan about transit of goods by motor transport through the territory of Republic of Kazakhstan (approved by the Parliament on June 11, 2004, in force from August 1, 2004) simplifies rules of transit for Kyrgyz goods. In particular, the agreement allows Kyrgyz entrepreneurs to get bank guarantees for transit in Kyrgyz banks versus only Kazakh banks, which was the case previously.

Kyrgyz Republic: Key macroeconomic indicators

	2001	2002	2003	2002	2002	2002	2002	2003	2003	2003	2003	2004	2004
				I	II	III	IV	I	II	III	IV	I	II
GDP and prices													
GDP real growth (%)	5.3	0	6.7	-2.4	6.5	0.3	4.8	4.6	0.8	7.8	10.8	5.7	12.2
GDP, som million	73,883	75,367	83,421	12,372	15,314	26,457	21,223	13,711	16,056	29,264	24,390	15,270	19,281
GDP, USD million	1,525	1,606	1,909	258	321	574	461	298	372	684	569	354	444
GDP per capita dollar (at avg x-rates)	308	322	383	...	...	...	...	...	...	...	...	...	...
Poverty headcount (% of population)	48	44	41	...	...	...	...	...	...	...	...	...	...
Extreme Poverty headcount (% of population)	14	14	9	...	...	...	...	...	...	...	...	...	...
GDP per capita, 1990=100	62	62	65	...	...	...	...	...	...	...	...	...	...
GNI per capita dollar GDP (Atlas)	280	290	350	...	...	...	...	...	...	...	...	...	...
Inflation (% beginning-to-end of period, CPI)	3.7	2.3	5.6	1.1	2.0	-1.7	1.0	2.0	0.5	-2.5	5.6	1.3	-0.4
Inflation (% average, CPI)	6.9	2.1	3.1	2.4	0.5	2.8	2.6	3.0	...	...	...	5.3	4.1
Wage, average for KR (som per month)	1455	1684	1902	1423	1575	1623	1842	1683	1887	1952	2104	1956	2050
Pension, average for KR (som per month)	558	561	647	579	564	602	612	620	654	668	647	684	710
Exchange rate (som/\$, end of period)	48	46	44	48	46	46	46	46	41	43	44	43	43
Exchange rate (som/\$, avg of period)	48	47	44	48	48	46	46	46	43	43	43	43	43
REER (end of period, 1997=100, up=depreciation)	107	109	115	109	107	108	109	110	105	111	115	117	118
M2 (e.o.p as percent of GDP)	11.1	14.6	17.6	11.6	11.7	13.1	14.6	13.8	14.3	15.4	17.6	16.3	17.2
External Sector													
Current account balance (% GDP)	-1.2	-1.7	-1.3	-0.8	0.1	-0.2	-0.8	0.6	-2.2	-0.3	0.5	-0.4	-0.4
Exports (mln US\$, f.o.b.)	480	498	588	117	125	117	140	121	115	142	210	159	184
- Power	47	22	19	2	1	16	3	2	2	10	6	2	6
- Gold	227	163	260	45	46	30	42	54	46	68	92	67	83
- Other	207	313	310	69	78	71	95	66	67	64	112	89	95
Imports (mln US\$, c.i.f.)	472	587	716	135	132	151	170	126	168	193	230	197	231
- Food	44	64.0	78	13	16	16	19	16	19	20	23	20	29
- Other consumer goods	128	130	178	21	33	37	39	28	38	45	68	48	47
- Energy	121	152	180	45	27	35	45	31	40	46	63	60	57
- Other intermediate goods	121	125	152	29	29	31	36	25	38	42	47	42	58
- Capital goods	58	116	128	26	26	32	31	26	33	39	29	26	41
External Debt (mln US\$)	1678	1785	1,961	1,665	1,705	1,738	1,776	1,804	1,840	1,912	1,943	1,965	1,981
Public External Debt (mln US\$)	1436	1576	1,648	1,429	1,498	1,524	1,576	1,602	1,640	1,694	1,701	1,798	1814
External Debt (% GDP)	110.0	111.1	102.7	103.7	106.2	108.2	110.6	94.5	96.4	100.2	101.8	93.6	94.4
Total debt service to exports of GS (%)	30.8	20.7	22	10.0	39.0	9.7	23.4	14.2	24.0	8.0	41.0	29.5	17.4
Public debt service to state revenues&grants (%)	27.7	23.3	15	11.6	50.7	9.8	19.3	19.0	17.7	10.8	17.7	9.3	19.4
Public external borrowing (excl. IMF, mln \$)	110	88	71	14	18	20	36	16	14	20	21	5	18.3
FDI (mln \$) ¹	5	5	46	5	-12	9	3	4	2	6	34	16	8
General Government Budget (percent of GDP)²													
Revenues and grants	20.4	22.7	22.9	4.6	5.2	6.1	6.8	4.3	5.9	6.1	6.7	5.0	5.7
Grants	0.8	1.1	0.6	0.3	0.0	0.3	0.4	0.0	0.1	0.4	0.1	0.2	0
Tax	12.4	13.9	14.3	2.8	3.3	3.8	4.1	2.7	3.4	3.9	4.3	3.1	3.8
Social fund contributions	4.0	4.2	3.4	0.8	0.8	1.0	1.0	0.8	0.8	0.9	0.9	0.9	0.9
Nontax and capital	3.2	3.5	4.6	0.7	1.1	1.0	1.3	0.8	1.5	0.9	1.4	0.7	1.0
Expenditures	26.2	27.9	27.5	5.8	6.9	7.1	8.5	5.5	7.3	7.0	7.7	6.0	7.1
Current (other than interest)	20.5	20.7	21.7	4.5	5.2	5.3	6.0	4.7	5.6	5.4	6.0	5.1	5.1
o.w. transfers & subsidies	8.2	9.4	8.7	2.1	2.2	2.2	2.6	1.7	2.2	2.1	2.7	1.8	2.1
wages & salaries	4.9	5.4	5.7	1.0	1.4	1.3	1.7	1.0	1.2	1.4	2.1	0.9	1.5
Interest payments	1.7	1.9	1.6	0.2	0.7	0.2	0.8	0.2	0.6	0.1	0.6	0.2	0.9
Capital	5.3	6.0	4.8	1.2	1.2	1.7	1.8	0.7	1.2	1.6	1.2	0.8	1.2
of/which foreign financed PIP	4.4	4.7	3.6	1.0	1.0	1.4	1.3	0.6	1.0	1.3	0.7	0.7	0.9
Net lending	-1.1	-0.6	-0.5	-0.1	-0.2	-0.1	-0.2	-0.1	-0.1	-0.1	-0.2	-0.1	-0.1
Fiscal Balance (accrual)	-5.8	-5.2	-4.6	-1.2	-1.6	-1.0	-1.6	-1.2	-1.4	-0.9	-1.0	-1.0	-1.4
Memo:													
Primary Deficit (w/o interest and PIP)	0.2	1.4	0.6	0.0	0.0	0.6	0.5	-0.4	0.2	0.5	0.3	-0.1	0.4
Primary Deficit (w/o interest)	-4.2	-3.3	-3.0	-1.0	-1.0	-0.8	-0.8	-1.0	-0.8	-0.8	-0.4	-0.8	-0.5

Source: Ministry of Finance, National Statistical Committee, Social Fund, National Bank and World Bank staff calculations.

¹ Includes repayment of FDI related debt

² The state budget consolidates central and local budgets and includes the foreign-financed public investment program and the deficit of the social fund, which became an extrabudgetary Fund in 1991. The quarterly data are on cash basis and based on the Treasury reports