Outline

Global Environment

CCA Outlook, Risks, and Policies
Global growth remains moderate and uneven

<table>
<thead>
<tr>
<th>Year</th>
<th>World</th>
<th>U.S.</th>
<th>Euro Area</th>
<th>Emerging markets</th>
<th>China</th>
<th>Russia</th>
</tr>
</thead>
<tbody>
<tr>
<td>2014</td>
<td>3.4</td>
<td>2.4</td>
<td>0.9</td>
<td>4.6</td>
<td>7.4</td>
<td>0.6</td>
</tr>
<tr>
<td>2015</td>
<td>3.5</td>
<td>3.1</td>
<td>1.5</td>
<td>4.3</td>
<td>6.8</td>
<td>-3.8</td>
</tr>
<tr>
<td>2016</td>
<td>3.8</td>
<td>3.1</td>
<td>1.7</td>
<td>4.7</td>
<td>6.3</td>
<td>-1.1</td>
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</table>
Oil prices are expected to remain lower than in the recent past, but uncertainty is large.

**Oil Price Prospects**
*(Brent crude oil; U.S. dollars a barrel)*

**Brent Futures Curve**
*(October 2014 REO vs. May 2015 REO Update)*
Other commodity prices have also declined, although not by as much as oil prices.

Commodity Prices

$(2005=100)$

- Food
- Metals
- Crude oil (APSP)
- Natural gas (Asia)

Jan-11 | Jul-11 | Jan-12 | Jul-12 | Jan-13 | Jul-13 | Jan-14 | Jul-14 | Jan-15
Caucasus and Central Asia

Oil & gas exporters

Oil & gas importers
Growth is expected to weaken further in 2015 with lower oil prices and Russia’s economic contraction.
Ties to Russia go beyond exports and include remittances, FDI and confidence

### Linkages with Russia

<table>
<thead>
<tr>
<th></th>
<th>Exports</th>
<th>Imports</th>
<th>Remittances</th>
<th>FDI</th>
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<tbody>
<tr>
<td>ARM</td>
<td>&lt;3% of GDP</td>
<td>3-10% of GDP</td>
<td>&gt;10% of GDP</td>
<td>&lt;3% of GDP</td>
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<tr>
<td>GEO</td>
<td>&lt;3% of GDP</td>
<td>&lt;3% of GDP</td>
<td>&lt;3% of GDP</td>
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<tr>
<td>KGZ</td>
<td>&lt;3% of GDP</td>
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<td>TJK</td>
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<tr>
<td>AZE</td>
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<tr>
<td>KAZ</td>
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<tr>
<td>TKM</td>
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<tr>
<td>UZB</td>
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<td>&lt;3% of GDP</td>
<td>&lt;3% of GDP</td>
<td>&lt;3% of GDP</td>
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</table>
Lower oil prices and Russia’s contraction are key reasons for downgrading of CCA forecasts.

Oil Exporters
- Russia slowdown
- Oil price decline
- Other country-specific factors

Oil Importers
- Russia slowdown
- Oil price decline
- Other country-specific factors

Graphs showing the impact of various factors on oil prices for different years.
Weakening revenues and countercyclical spending are widening fiscal deficits.
Currencies are weakening against the dollar yet losing competitiveness in real terms.

**Nominal Exchange Rates, Jan. 2011-Feb. 2015**
(U.S. dollars per unit of national currency; Index, Jan. 2011=100)

**Real Effective Exchange Rates, Jan. 2013-Feb. 2015**
(Index, Jan 2014=100)
Depreciations are raising inflationary pressures, despite lower growth and commodity prices.
External positions are worsening, especially for oil exporters

**Current Account Balances**
*(Percent of GDP)*

**Reserve Coverage**
*(Months of Imports)*
The financial sector faces multiple challenges

Non-performing Loans, Dollarization
(Percent of total loans; latest available data)

Capital Adequacy Ratios
(Percent of risk-weighted assets; latest available data)
Risks have increased and remain tilted to the downside

- Weaker growth in trading partners (especially Russia, also China and Europe)
- Further weakening of prices for oil and other commodities
- Risks related to the normalization of U.S. monetary policy
Near-term policy priorities center on preserving macro-financial stability while shoring up growth

**Fiscal**
- Temporary counter-cyclical policies if buffers and fiscal space allow.
- Fiscal consolidation over the medium term, as soon as cyclical conditions allow, to reflect new oil market realities for oil exporters and the need to rebuild buffers among oil importers.

**Monetary & External**
- Greater exchange rate flexibility can help buffer shocks, prevent reserve drawdowns, and protect competitiveness.
- Tighten monetary policy, if inflationary pressures remain elevated and if it does not undermine financial sector stability.

**Financial**
- Monitor and manage the financial stability risks.
- Banks should be required to appropriately classify the loans and have adequate provisions.
- Crisis management frameworks should be strengthened.
Stronger macro-financial policy frameworks can increase resilience to unexpected shocks

**Fiscal Policy:** More fiscal transparency, and stronger medium-term budget frameworks

**Monetary Policy:** Modern monetary policy regimes with clear interest rate guidance

**Financial Sector Policy:** Clear definition of responsibilities, modern supervision practice
Medium-term growth prospects are weakening in the CCA: a “new mediocre”?  

<table>
<thead>
<tr>
<th>Potential GDP Growth (Percent)$^{1,2}$</th>
<th>Differences with EMDC (Percentage points)</th>
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<tbody>
<tr>
<td>CCAOE</td>
<td>8</td>
</tr>
<tr>
<td>CCAOI</td>
<td>7</td>
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$^{1}$

$^{2}$
Structural reforms can help improve competitiveness, raise economic growth and make it more inclusive.

Structural Reform Priorities

CCA
Armenia
Azerbaijan
Georgia
Kazakhstan
Kyrgyz Republic
Sub-Saharan Africa
Latin America
Emerging Europe
Developing Asia
Advanced Economies

Sources: Labor: World Economic Forum (WEF); Corruption: PRS; Infrastructure: WEF; Trade: WEF; Education: WEF; Legal: WEF and World Bank Doing Business; Finance: WEF and World Bank Doing Business; Bureaucracy: PRS; Regulations: World Bank Worldwide Governance Indicators.
Key Messages

• The region is facing new, possibly long-lasting, realities.

• Policy responses so far have been partial and focused on the short term.

• Medium-term fiscal consolidation and greater exchange rate flexibility are needed to maintain macroeconomic stability.

• Enhanced policy frameworks would improve shock resilience.

• Structural reforms would enhance long-term growth potential and make it more inclusive.
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