Overview

- Global outlook
- Caucasus and Central Asia (CCA) outlook and risks
- CCA macroeconomic policies
- CCA structural challenges
The global recovery has weakened

Global Manufacturing PMI
(Index; > 50 = expansion; SA)

Merchandise Exports
(Percent; 3mma annualized)

Source: IMF, Global Data Source.
European financial conditions remain fragile

Government Bond Spreads
(Two-year yield spreads over German bunds; basis points)

Portfolio and Other Investment Capital Flows, Excluding Central Banks
(Cumulative from December 2009, in percent of GDP)

Sources: IMF, World Economic Outlook; and Bloomberg.
Commodity prices are still elevated

Commodity Prices
(Index; 2005=100)

Spot Prices of Major Crops
(Index; 1/3/2005 = 100)

Source: IMF, Global Data Source.
Against this backdrop, the global outlook has deteriorated.
Caucasus and Central Asia: outlook and risks

CCA region:
• Broadly positive growth outlook, but growing external risks

Oil and gas importers:
• Gradual fiscal consolidation, but not enough to rebuild buffers
• External vulnerabilities—large current account deficits

Oil and gas exporters:
• Declining fiscal surpluses amidst some overheating risks
• The challenge of improving the quality of public spending

Medium-term challenges:
• Creating jobs, reducing informal sector, and fostering high and inclusive growth
Growth outlook remains broadly positive

Sources: IMF, *World Economic Outlook*; and IMF staff calculations and projections.
Remittances and commodity prices benefited CCA oil importers

**Remittances from Russia to CCA Countries**¹
*(Three month moving average, 2008:Q2=100)*

- ARM: $330m, 13% of GDP
- GEO: $180m, 5% of GDP
- KGZ: $460m, 27% of GDP
- TJK: $850m, 45% of GDP

**Commodity Terms of Trade**
*(Index; June 2009=100)*

Sources: National authorities; and IMF staff estimates.

1²Boxes show the latest data available (2012:Q2).
But downside risks are elevated
Financial sector: legacy NPLs but little exposure to Europe

Nonperforming Loans
(On a 90-day basis; percent of total loans)

Foreign Liabilities of CCA Banking Sectors
(Percent of total assets, end-2011)

Sources: National authorities; GFSR.

Sources: National authorities; and IMF staff estimates.
Inflation is low but sensitive to food price developments

Headline CPI Inflation
(12-month change; percent)

Sources: National authorities; and IMF staff calculations.
¹IMF world commodity price inflation.
High exposure to international food prices

Food Imports as a Share of GDP
(Percent)

<table>
<thead>
<tr>
<th>Country</th>
<th>2007-08 Average</th>
<th>2010</th>
<th>World Average, 2010</th>
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Sources: National authorities; and IMF staff calculations.

Weight of Food in the Consumer Price Index, 2010
(Percent)

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<th>Country</th>
<th>KAZ</th>
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Sources: IMF staff; OECD StatExtracts; and Eurostat.
Fiscal consolidation is needed, particularly in the oil and gas importers

![Fiscal Deficits](chart1)

*Fiscal Deficits*  
*(Fiscal balance; percent of GDP)*

![Public Debt](chart2)

*Public Debt*  
*(Percent of GDP)*

Sources: National authorities; and IMF staff calculations.

¹ Non-oil and gas fiscal balance as share of non-oil and gas GDP.
Need to address external vulnerabilities in the oil and gas importers

Sources: National authorities, IFS database; and IMF staff calculations and projections.
Policy advice in the event that risks materialize

**Allow greater exchange rate flexibility**
- Step-up communications on risks
- Avoid a “re-run” of the 2008-09 response: limit loss of reserves

**Ease monetary policy, if conditions warrant**
- Subdued inflation may allow for easing of monetary policy

**Improve quality of fiscal spending**
- Reorient and better target spending to protect the most vulnerable
- In CCA countries with fiscal space, consider counter-cyclical response
Structural challenges: need to tackle the informal sector

Large informal sectors
• undermine social protection and growth

Policies to tackle informal sector
• improve business environment and regulation
• improve institutional quality/governance
• relax labor market rigidities while safeguarding adequate social protection
• reduce tax burden (income and social security taxes)
• provide access to skills upgrading for informal workers.

Size of the Informal Economy
(Percent of GDP, 2008)

Source: IMF staff estimates.
Key messages

Rebuild policy buffers

- Oil and gas importers:
  - Fiscal consolidation
  - More exchange rate flexibility

- Oil and gas exporters:
  - Improve quality and reduce rigidity of public spending
  - Diversify tax base

If downside risks materialize:

- Limit loss of reserves → allow currency depreciation
- Where possible, ease fiscal and monetary policies
- Reorient spending to protect the most vulnerable

Revitalize economy for inclusive growth and job creation:

- Improve business environment/institutional quality
- Address excess labor market rigidities and tax wedge on labor
- Provide access to training
### Key messages: Kazakhstan

| Restore the health of the banking system | • Move forcefully to tackle the NPL problem  
| • Address problem banks  
| • Improve corporate governance |
| Reduce the nonoil fiscal deficit to the medium-term sustainable level | • Improve the quality of public spending  
| • Strengthen nonoil tax revenues |
| Revitalize the economy for inclusive growth | • Focus on diversification  
| • Reduce the role of the public sector  
| • Improve competitiveness and the business environment |
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