IMF | Middle East and Central Asia Department

Caucasus and Central Asia: Outlook and Policy Challenges

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Juha Kähkönen
Deputy Director
Middle East and Central Asia Department
Outlook: Global headwinds and trade tensions weigh on growth
Global growth outlook remains largely subdued.

<table>
<thead>
<tr>
<th>Year</th>
<th>World</th>
<th>US</th>
<th>Euro Area</th>
<th>China</th>
<th>Russia</th>
<th>Emerging and Developing Countries</th>
</tr>
</thead>
<tbody>
<tr>
<td>2018</td>
<td>3.6</td>
<td>2.9</td>
<td>1.9</td>
<td>6.6</td>
<td>2.3</td>
<td>4.5</td>
</tr>
<tr>
<td>2019</td>
<td>3.0</td>
<td>2.4</td>
<td>1.2</td>
<td>6.1</td>
<td>1.1</td>
<td>3.9</td>
</tr>
<tr>
<td>Revisions from April 2019</td>
<td>-0.3</td>
<td>0.0</td>
<td>-0.1</td>
<td>-0.1</td>
<td>-0.5</td>
<td>-0.4</td>
</tr>
<tr>
<td>2020</td>
<td>3.4</td>
<td>2.1</td>
<td>1.4</td>
<td>5.8</td>
<td>1.9</td>
<td>4.6</td>
</tr>
<tr>
<td>Revisions from April 2019</td>
<td>-0.2</td>
<td>0.2</td>
<td>-0.2</td>
<td>-0.3</td>
<td>0.2</td>
<td>-0.3</td>
</tr>
</tbody>
</table>

Sources: National authorities; and IMF staff calculations.
Growth in the CCA has stalled...

Sources: National authorities; and IMF staff calculations.

Real GDP Growth
(Percent)

— CCA oil exporters

Projections

2015 16 17 18 19 20 2021–22

UZB
TKM
KAZ
AZE

— CCA oil importers

Projections

2015 16 17 18 19 20 2021–22

GEO
ARM
TJK
KGZ

Sources: National authorities; and IMF staff calculations.
...cushioned by loose fiscal and monetary policy stances

**Overall Fiscal Balance**  
*(Percent of GDP)*

- CCA oil exporters
- CCA oil importers

**Change in Policy Rate in CCA Countries**  
*(Percent, Sep. 2019 – Dec, 2018)*

<table>
<thead>
<tr>
<th>Country</th>
<th>ARM</th>
<th>KAZ</th>
<th>GEO</th>
<th>UZB</th>
<th>KGZ</th>
<th>TJK</th>
<th>AZE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Inflation targeters</td>
<td>-2.0</td>
<td>-1.5</td>
<td>-1.0</td>
<td>-0.5</td>
<td>0.0</td>
<td>0.5</td>
<td>1.0</td>
</tr>
<tr>
<td>Other regimes</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

Source: National authorities; and IMF staff calculations.

Source: Haver Analytics.
...amid weaker external demand...

CCA Export and Import Growth
(Year-on-year percent change)

Current Account Balance
(Percent of GDP)

Sources: National authorities; and IMF staff calculations.
Challenges
Downside risks rise from oil price uncertainty and global trade tensions

Lower and volatile oil prices
(Average petroleum spot price, US dollars a barrel)

Growth of Imports of Top Trading Partners
(Revisions from April 2019)

Sources: National authorities; and IMF staff calculations.

CCA Top 10 Export destinations include China, Italy, Russia, Netherlands, Turkey, Switzerland, France, Spain, Ukraine and Uzbekistan.
Falling productivity and low competitiveness restrain jobs and convergence

Sources: National authorities; and IMF staff calculations.

Challenges to Doing Business in CCA
(Number of countries identifying the constraint among the top five)

Note: Turkmenistan and Uzbekistan are excluded due to data availability.
Therefore, higher and more inclusive growth is needed amid increasing labor force.

**Inclusiveness**

(10 is best and 1 is worst)

### Emerging Europe

<table>
<thead>
<tr>
<th>Country</th>
<th>Inclusiveness Score</th>
</tr>
</thead>
<tbody>
<tr>
<td>KAZ</td>
<td>6</td>
</tr>
<tr>
<td>ARM</td>
<td>5</td>
</tr>
<tr>
<td>UZB</td>
<td>5</td>
</tr>
<tr>
<td>GEO</td>
<td>5</td>
</tr>
<tr>
<td>TKM</td>
<td>5</td>
</tr>
<tr>
<td>TJK</td>
<td>4</td>
</tr>
<tr>
<td>AZE</td>
<td>3</td>
</tr>
<tr>
<td>KGZ</td>
<td>2</td>
</tr>
</tbody>
</table>

Source: European Bank for Reconstruction and Development.

Note: Inclusiveness index aggregates several indicators which measure gender equality, opportunities for youth and regional disparities.

**Projected Cumulative Labor Force Increase Relative to 2018**

(Millions)

- **Oil exporters**: 32.3
- **Oil importers**: 8.6

Labor force in 2018:

- Oil exporters: 32.3
- Oil importers: 8.6

Graph showing projected cumulative labor force increase.
Two thirds of countries in the world rank better than the CCA countries on average in Worldwide Governance Indicators

Worldwide Governance Indicators
(On a -2.5 (weak) to 2.5 (strong) scale)

Building Resilience
Growth-friendly fiscal consolidation is needed to reduce debt vulnerability

Total Public Debt in 2013 vs. 2019
(Percent of GDP)

Overview of Fiscal Management Frameworks

<table>
<thead>
<tr>
<th>Country</th>
<th>Fiscal Rules</th>
<th>Medium-term fiscal framework</th>
</tr>
</thead>
<tbody>
<tr>
<td>Armenia</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Azerbaijan</td>
<td>Yes</td>
<td>In progress</td>
</tr>
<tr>
<td>Georgia</td>
<td>Yes</td>
<td>Yes</td>
</tr>
<tr>
<td>Kazakhstan</td>
<td>In progress</td>
<td>Yes</td>
</tr>
<tr>
<td>Kyrgyz Republic</td>
<td>In progress</td>
<td>No</td>
</tr>
<tr>
<td>Tajikistan</td>
<td>No</td>
<td>No</td>
</tr>
<tr>
<td>Turkmenistan</td>
<td>Yes</td>
<td>No¹</td>
</tr>
<tr>
<td>Uzbekistan</td>
<td>No</td>
<td>No</td>
</tr>
</tbody>
</table>

Fiscal rules are a mechanism for placing durable constraints on fiscal discretion through procedural and numerical limits on budgetary aggregates. Medium-term fiscal frameworks consist of institutional arrangements and procedural or numerical rules that provide incentives for overcoming the deficit bias.

1 Medium-term budgeting is planned to be introduced in 2019.

Source: National authorities; and IMF staff calculations
ER flexibility and modernization of MP frameworks are needed as shock absorbers

Nominal Effective Exchange Rate
(Index, Jan 2010 =100, 3-month moving average)

Source: Information Notice System; and IMF staff calculations

Modern Monetary Policy Framework

- Independent, accountable, and forward-looking interest rate-based monetary policy
- Objectives: price stability while preserving financial stability.
- Clear and timely communication
- Better transmission mechanism
Financial sector repair is needed to allow banks to contribute to growth

Private Credit Growth
(Percent, year-over-year average)

Asset Quality in the CCA
(Percent of total loans, latest available)

Source: National authorities; and IMF staff calculations.

Note: Problem Loans include (1) overdue loans > 90 days; (2) watch loans < 90 days; (3) restructured/prolonged loans; (4) write-offs; and, (5) transfer to special-purpose vehicles or other vehicles.

1. For Uzbekistan restructured loans are related to SOE borrowing (from state owned banks) with government guarantees. The risks for banks are low as the government has high liquid buffers to repay if needed. The amount of restructured loans includes only the restructured parts of the loans. 2. For Armenia total loans include losses and loss loans are loans overdue by 270 days.
Boosting Competitiveness for Higher Inclusive Growth
How competitive are CCA countries?

**Latest IMF Exchange Rate Assessment**
(Number of countries)

- Broadly in line with fundamentals: 5
- Overvalued: 3

Source: Authorities data and IMF staff calculations.

**Global Competitiveness Index**
(0–100, where 100 is best)

Non-commodity export performance in oil exporters has room for improvement

Share of Noncommodity Exports in Global Exports
(Index 2008 = 100, share of volume of world exports)

Sources: National authorities; and IMF staff calculations.

Export Quality¹
(Index 0–1, higher is more diverse)

Sources: IMF Diversification database; and IMF staff calculations.
Note: Export quality index rebased to be from 0 to 1, and is equal to a Theil index of export concentration.
1. 2014 is latest available year for the quality index.
Promote global value chain participation

**Global Value Chain Participation Rate**
*(Share of exports)*

<table>
<thead>
<tr>
<th>Country</th>
<th>Participation Rate</th>
</tr>
</thead>
<tbody>
<tr>
<td>TJK</td>
<td>40</td>
</tr>
<tr>
<td>GEO</td>
<td>35</td>
</tr>
<tr>
<td>KGZ</td>
<td>30</td>
</tr>
<tr>
<td>ARM</td>
<td>25</td>
</tr>
<tr>
<td>UZB</td>
<td>20</td>
</tr>
<tr>
<td>AZE</td>
<td>15</td>
</tr>
<tr>
<td>TKM</td>
<td>10</td>
</tr>
<tr>
<td>KAZ</td>
<td>5</td>
</tr>
</tbody>
</table>

**Transportation Cost**
*(Costs are in 000s of Euros per container)*

<table>
<thead>
<tr>
<th>Destination</th>
<th>Cost Range</th>
</tr>
</thead>
<tbody>
<tr>
<td>To Shanghai</td>
<td>3.9-5.9</td>
</tr>
<tr>
<td>To Rotterdam</td>
<td>1.9-3.9</td>
</tr>
</tbody>
</table>

**Source:** United Nations Conference on Trade and Development (UNCTAD) – Eora Global Value Chain (GVC) database.

**Note:** Data shown does not show actual costs, rather it reflects estimated costs of transportation from the source.
Reform SOEs to reduce state size and foster private sector

SOEs’ Value Added and Employment (Percent)

Business Entry Density Rate (Number of newly registered firms with limited liability per 1,000 working-age people)

Source: National authorities; and IMF staff calculations

Improving Governance
Good governance leads to higher growth, investment, and tax revenue

**Effects of Good Governance**
*(Increase in percentage points of moving up one quartile in the distribution of governance indicators)*


Note: Governance is defined as the average of the Worldwide Governance Indicators (WGI) on: (i) governance effectiveness, (ii) rule of law, (iii) regulatory quality, (iv) voice and accountability, and (v) control of corruption.
There is room to improve fiscal governance ...

**Fiscal Governance**
*(On a 0 (worst) to 1 (best) scale)*

Sources: WEO, World Bank, and IMF staff calculations (2019).
… financial sector oversight …

Compliance to Basel Core Principles for Effective Banking Supervision, by Region, 2019
(on a red/least to green/most compliant scale)

<table>
<thead>
<tr>
<th>Principle</th>
<th>AFR</th>
<th>MENA</th>
<th>WHA</th>
<th>CCA</th>
<th>EUR</th>
<th>APAC</th>
</tr>
</thead>
<tbody>
<tr>
<td>4. Permissible activities</td>
<td></td>
<td></td>
<td></td>
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<td></td>
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<tr>
<td>26. Internal control and audit</td>
<td></td>
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<tr>
<td>2. Independence and resourcing</td>
<td></td>
<td></td>
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<td></td>
<td></td>
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<tr>
<td>21. Country and transfer risks</td>
<td></td>
<td></td>
<td></td>
<td></td>
<td></td>
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<tr>
<td>23. Interest rate risk in the banking book</td>
<td></td>
<td></td>
<td></td>
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<td></td>
<td></td>
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<tr>
<td>29. Abuse of financial services</td>
<td></td>
<td></td>
<td></td>
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</tr>
</tbody>
</table>

Source: IMF Monetary and Capital Markets Department Compliance to Basel Core Principles for Effective Banking Supervision (2019).
AFR: Africa; APAC: Asia-Pacific; EUR: Europe; MENA: Middle East and North Africa; CCA: Caucasus and Central Asia; WHA: Western Hemisphere
Central Bank Governance and Operations

(On a 1 (high) to 4 (low risk) scale)

Source: IMF Safeguards Assessment of Central Banks.
... Anti-Money Laundering / Combatting the Financing of Terrorism

(On a 1 (worst) to 5 (best) scale)

IMF’s Role
Strong IMF engagement in the CCA region

Program and Technical Assistance (TA)

Team Visits Intensity in the CCA
May 2018 – April 2019

Capacity Development (CD)

- Fiscal: public financial and investment management, tax administration, tax policy.
- Monetary policy: monetary policy framework, central bank operations, reserves management and foreign exchange arrangements.
- Financial policies: bank, pensions, and insurance laws and regulations, AML/CFT.
- JVI Training: monetary policy workshop, financial programming and policies.
- New regional TA center in Almaty will fill an important gap!
## Strong IMF engagement in the CCA region (cont.)

### Analytical Work

#### Promote Inclusive Growth

- Papers on: “Promoting Inclusive Growth in the Caucasus and Central Asia” and “Opening Up in the CCA: Policy Frameworks to Support Integration.”
- Fall 2019 REO chapter on fiscal institutions
- Discussion of ministers and governors on inclusive growth at the 2019 annual meetings.
- Note on operationalizing inclusive growth in country work.

#### Bolster Resilience

- Fall 2019 REO chapter on capital flows
- Annual CCA central banks workshop
Takeaways

• Growth in the CCA has stalled amid downside risks.

• To address these risks, enhance resilience by strengthening fiscal, monetary, and financial policies.

• Boost competitiveness and governance through reforms to achieve higher inclusive growth.

• Strong IMF’s engagement, including through the new regional center.
THANK YOU!