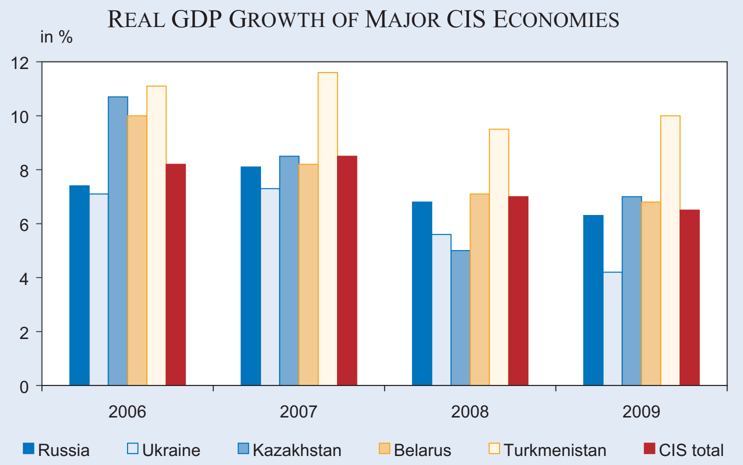
Economic Prospects of Commonwealth of Independent States

Figure 1



Source: IMF and also Table 1.

According to the latest IMF World Economic Outlook, real GDP growth amounted to 8.5 percent in the Commonwealth of Independent States (CIS) in 2007, accompanied by high commodity prices, expansionary macroeconomic policies, strong capital inflows, rapid credit growth and rising asset prices stimulating domestic demand growth.[1] Yet, due to rapidly increasing imports, the contribution of external sector performance to economic growth was negative and current account balances weakened (see Table 1 and Figure 1).

The strong economic growth of recent years has led to the elimination of spare capacity in most CIS economies, while wage growth has continuously risen. Also triggered by accelerating food prices, this has resulted in a sharp increase in inflation across the region very recently. In Russia inflation rose to almost 12 percent in December 2007, while its annual average rate is anticipated to reach around 20 percent in Azerbaijan, Kazakhstan, the Kyrgyz Republic, Tajikistan and Ukraine in 2008.

The instability in global financial markets has begun to affect most CIS economies, particularly since bank and portfolio inflows have recently become the major source of external financing there. In Russia and Ukraine, where banks have borrowed heavily in international markets to finance rapid growth in domestic lending, spreads on external debt have widened remarkably. In Kazakhstan, its impact has been even worse, with external financing drying up, credit growth slowing, and reserves initially declining as the central bank intervened in the foreign exchange market to support the exchange rate.

High oil and commodity prices should continue to provide support for economic growth of CIS, but a

[1] International Monetary Fund (IMF), World Economic Outlook, April 2008, Washington DC, Chapter 2.

Table 1

Real GDP Growth and Development of Consumer Prices and Current Account Balance in CIS Economies
(Annual percent changes unless noted otherwise)

	Real GDP				Consumer prices				Current account balance*			
	2006	2007	2008	2009	2006	2007	2008	2009	2006	2007	2008	2009
Russia	7.4	8.1	6.8	6.3	9.7	9.0	11.4	8.4	9.5	5.9	5.8	2.9
Ukraine	7.1	7.3	5.6	4.2	9.0	12.8	21.9	15.7	– 1.5	– 4.2	– 7.6	– 9.7
Kazakhstan	10.7	8.5	5.0	7.0	8.6	10.8	17.1	8.3	– 2.2	– 6.6	– 1.7	– 1.0
Belarus	10.0	8.2	7.1	6.8	7.0	8.4	11.2	8.8	– 4.1	– 6.6	– 7.5	– 7.7
Turkmenistan	11.1	11.6	9.5	10.0	8.2	6.4	12.0	12.0	15.3	16.8	23.6	28.1
Armenia	13.3	13.8	10.0	8.0	2.9	4.4	6.8	4.5	– 1.8	– 6.5	– 6.8	– 5.0
Azerbaijan	30.5	23.4	18.6	15.6	8.4	16.6	19.6	20.5	17.7	28.8	39.5	39.2
Georgia	9.4	12.4	9.0	9.0	9.2	9.2	9.6	6.4	– 15.9	– 19.7	– 16.6	– 13.2
Kyrgyz Republic	3.1	8.2	7.0	6.5	5.6	10.2	18.8	10.2	– 6.6	– 6.5	– 8.3	– 7.4
Moldova	4.0	5.0	7.0	8.0	12.7	12.6	11.4	7.9	– 12.0	– 9.7	– 10.3	– 10.6
Tajikistan	7.0	7.8	4.1	7.0	10.0	13.2	18.5	10.5	– 3.0	– 9.5	– 8.3	– 7.1
Uzbekistan	7.3	9.5	8.0	7.5	14.2	12.3	11.8	10.9	18.8	23.8	24.6	20.8
CIS total	8.2	8.5	7.0	6.5	9.5	9.7	13.1	9.5	7.5	4.5	4.8	2.4

* Percent of GDP.

Source: IMF.

weaker global economy (which would likely lead to a decline in oil and commodity prices) and slower credit growth could dampen the expansion pace. As a consequence, real GDP growth of CIS is expected to ease to 7 percent in 2008 and 6.5 percent in 2009. For Russia the IMF projects a real GDP growth rate of 6.8 percent in 2008 and 6.3 percent in 2009, compared to that of 5.6 percent (2008) and 4.2 percent (2009) for Ukraine (see also Figure 1). On the other hand, strong growth appears set to continue in some low-income CIS countries like Azerbaijan, Armenia, Moldova and Uzbekistan (see Table 1).

The most immediate policy challenge in the region is to control high inflation. In spite of the expected slowdown in overall economic growth and food price increase, inflation is likely to remain "uncomfortably" high in the short term, unless restrictive macroeconomic and monetary policies are swiftly implemented. For example, fiscal policy has excessively added to demand pressure in Russia, Ukraine, Azerbaijan and Georgia. In addition income policies should be geared toward achieving wage outcomes consistent with "single-digit" inflation, given underlying trends in productivity. Tighter monetary policy combined with greater exchange rate appreciation will also be needed in Russia and Georgia, whereas monetary conditions were tightened in Ukraine beginning in the second half of 2007. As already mentioned above, such monetary policy tightening took place in Kazakhstan in December 2007, as inflation increased and the exchange rate came under strong downward pressure.

In the long run, CIS economies should diversify their production base away from the current strong reliance on commodities. Moreover, with only 22 percent of GDP in 2007, investment in the region remains rather low and is mainly concentrated in extractive industries and construction. Some intensive efforts seem to be additionally necessary in order to stimulate private sector investment, which include improvement of business climate, continuation of trade reforms, development of more diversified domestic financial systems, etc.

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