



## KYRGYZ REPUBLIC

### Highlights

- **The economy is growing strongly.** Real GDP growth reached 5.0 per cent year-on-year in the first nine months of 2017, reflecting partly the low base effect as well as strong gold production and the stabilisation of remittances inflows.
- **The currency has stabilised after significant depreciation during 2014-15.** The som appreciated by around 10.8 per cent from the beginning of 2016 to the end of October 2017, reflecting the rebound in remittances and improvements in the external environment.
- **Banking sector vulnerabilities remain significant.** The weakening of the currency and overall economic slow-down in 2015 and the first half of 2016 contributed to an increase in classified loans to 8.8 per cent by the end of 2016, up from 4.5 per cent in 2014. Dollarisation in the banking sector remains high, but is declining as a result of the National Bank of the Kyrgyz Republic (NBKR)'s policies.

### Key priorities for 2018

- **Simplifying tax administration and other interaction with the government for small and medium-sized enterprises through more efficient public services continues to be of high importance to improve the business climate.** This would also help to move more businesses from the informal to the formal sector.
- **Efforts to strengthen the banking sector should continue for a more resilient financing base for the economy.** Prudential banking rules should be enforced more rigorously.
- **Public utilities should be strengthened through commercialisation and stronger private sector participation.** This would help municipal utilities improve their financial standing, operating practices and governance, and enhance the reliability of the power sector by rehabilitating assets and developing a more attractive institutional framework for private investment.

#### Main macroeconomic indicators %

	2013	2014	2015	2016	2017 proj.
GDP growth	10.5	4.0	3.9	3.8	4.4
Inflation (average)	6.6	7.5	6.5	0.4	3.1
Government balance/GDP	-3.7	1.0	-1.2	-4.5	-3.0
Current account balance/GDP	-13.3	-16.0	-16.0	-9.7	-11.6
Net FDI/GDP [neg. sign = inflows]	-8.5	-3.1	-15.1	-6.6	-6.7
External debt/GDP	71.9	75.6	85.2	84.4	73.1
Gross reserves/GDP	30.5	26.2	26.6	30.0	n.a.
Credit to private sector/GDP	15.4	19.6	21.8	20.4	n.a.

## Macroeconomic performance

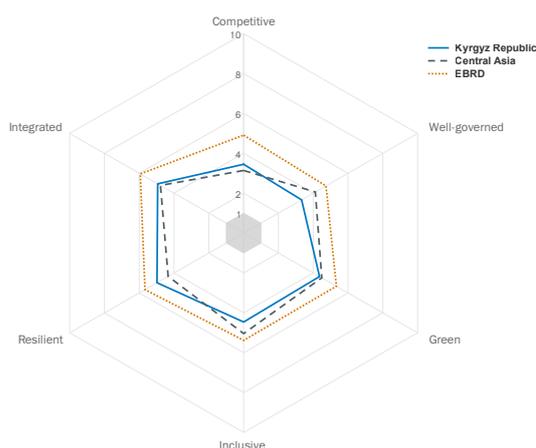
**The economy is growing strongly.** GDP growth reached 5.0 per cent year-on-year in the first nine months of 2017, continuing the strong rebound in the second half of 2016. Excluding the Kumtor gold mine, GDP growth reached 3.6 per cent, slightly lower compared with 2016, when the economy grew by 3.8 per cent. The better 2017 GDP figures not only reflect the significant increase in gold production, but also the low base effect and strong remittances inflows, which increased by 25.4 per cent in US dollar terms and 22.5 per cent in local currency terms year-on-year in the first eight months of 2017.

**The currency has stabilised since 2016.** The som appreciated by around 10.8 per cent from the beginning of 2016 to mid-October 2017, reflecting the rebound in remittances and the stabilisation of the external environment. Currency appreciation and lower fuel prices reduced inflation to only 0.4 per cent in 2016, but the rate accelerated to 3.3 per cent year-on-year in September 2017, mainly due to higher services prices. The NBKR gradually lowered its refinancing rate from 10.0 per cent in 2015 to 5.0 per cent in December 2016. Gross international reserves remained stable, close to US\$ 2.1 billion (covering five months of imports of goods and services) as of September 2017.

**External and fiscal positions remain under pressure.** The fiscal deficit widened to 4.5 per cent of GDP in 2016 from 1.2 per cent in 2015 as a result of weak budget revenues and large infrastructure spending. The government is targeting a deficit of 3.0 per cent of GDP in 2017 as the economy has begun to recover. The current account deficit narrowed to around 9.7 per cent of GDP in 2016 from 16.0 per cent in 2015, reflecting the recovery in external transfers in the second half of the year and a further decline in imports as a result of weak investment and household demand. The deficit will likely further decline this year, but nevertheless remain sizeable.

**Real GDP growth is expected to reach 4.4 per cent in 2017 and 4.2 per cent in 2018,** on the back of strong growth in mining and higher gold exports, as well as continued growth in remittances, boosting household demand. Infrastructure spending from China will likely remain significant. However, the fiscal loosening in the run-up to the presidential election will have to be reversed in order to continue with the IMF programme.

### Assessment of transition qualities (1-10)



## Major structural reform developments

**Business environment and investment climate challenges remain despite improvements in recent years.** The Kyrgyz Republic ranked 77th out of 190 countries in terms of ease of doing business, according to the World Bank *Doing Business 2018* report. The country performs well in areas such as starting a business, registering property, getting credit and dealing with construction permits, but poorly in paying taxes, resolving insolvency, getting electricity, enforcing contracts and trading across borders. Efforts to boost investment are hindered by low state capacity, political volatility and concerns over foreign ownership of economic assets.

**Progress has been made to resolve the long-standing Kumtor gold mine dispute.** At the beginning of September 2017 Canadian mining company Centerra Gold Inc. announced that an agreement had been reached with the Kyrgyz authorities to settle all disputes over the Kumtor gold mine. As a result all environmental claims and court orders against Kumtor will be dropped and Centerra will be able to freely transfer its funds worth US\$ 299 million out of the country, which earlier had been frozen by the Kyrgyz government. Following the deal, there will be no restrictions on Kumtor's ability to distribute funds to Centerra and all restrictions of movement on Kumtor's employees will be lifted. The settlement follows a dispute during which Centerra took the Kyrgyz government to international arbitration in 2016 over a disagreement on profit sharing.

**Banking sector vulnerabilities remain, but are not so significant to sharply constrain credit growth.** The weakening of the currency and the overall economic slow-down in 2015 and the first half of 2016 contributed to an increase in classified loans (overdue and non-performing loans) to 8.8 per cent by the end of 2016 from 4.5 per cent in 2014, falling only marginally to 8.4 per cent as of June 2017. The dollarisation in the banking sector has remained rather high at 48 per cent in deposits and 42 per cent in loans as of June 2017. However, as economic growth has accelerated the banking sector has begun to show signs of recovery with credit to the private sector increasing.

**The Kyrgyz Republic again needs to find a new partner for the Naryn project.** The government approved a contract in August 2017, under which Liglass Trading, a Czech photovoltaic and hydropower investment company, agrees to construct and operate two large hydropower plants in the Upper Naryn cascade and 10 other smaller plants with a capacity of 280 MW. However, after Liglass announced in September 2017 that it would be unable to fulfil obligations to pay US\$ 37 million to RusHydro, the government decided to cancel the contract with the company. The contract for the development of these hydropower plants had previously been awarded to RusHydro, a Russian hydroelectric company. The contract with the Russian company was terminated in 2015 because of the government's concerns regarding the ability of the Russian government to follow through on proposed investments in the project. The successful completion of the Upper Naryn project would be a good sign for other significant endeavours such as the proposed Karambata-1 dam, which will require investment on an even larger scale.