

Turkmenistan

Key developments and challenges

After the successful reunification and redenomination of the exchange rate, the financial sector needs to develop into a sustainable source of funding for the real economy. The entry of foreign strategic investors, a reduction of directed lending and the end of subsidised interest rates would help to meet this challenge.

Private sector development depends on further improvements in the business environment, in particular the lowering of entry barriers, the reduction of the regulatory burden on existing businesses, continued price liberalisation and the abolition of production targets in agriculture and textiles.

Although the establishment of the stabilisation fund is a welcome step towards creating a longer-term approach to public sector investment policy, the budgetary process and public sector finances need to be more transparent.

Country data

Population (in millions)	6.5
Area ('000 sq km)	488.0
GDP (in billion US\$, 2008)	19.0
Average transition score (scale: 1 to 4.33)	1.44

Progress in structural reform

Liberalisation and privatisation

To further its ambitious target to increase the private sector share to 70 per cent of GDP by 2020, the government has taken several legislative initiatives. The new constitution adopted in October 2008 recognises – for the first time in Turkmenistan – the concept of a market economy with private property and independent enterprises. The new constitution complements the investment legislation passed in March 2008 that provides for long-term property leases and the repatriation of profits. In practice, however, the administrative burden on private businesses continues to constrain their development. The agricultural and textile sectors in particular are distorted by production targets and subsidised inputs.

Domestic prices for petrol were liberalised in 2008 with the aim of significantly decreasing car fuel consumption, given that, per capita, consumption of petrol is among the highest in central Asia. Market prices for petrol subsequently increased eightfold (although they remain well below the levels of other countries in the region). A more comprehensive energy reform package, covering not only individual petrol consumption but also the highly energy-inefficient industrial sector, has not been considered yet. Sixteen other basic commodities (including water, salt and bread) remain highly subsidised and price controlled.

Infrastructure

Physical infrastructure outside the capital, Ashgabat, still suffers from years of underinvestment. The government has developed a regional development plan that envisages significant increases in investment in rural infrastructure. However, this programme is yet to be implemented. Efforts to improve regional transport infrastructure, in particular a north-south trade and transportation corridor, have moved forward only slowly. The Iran-Turkmenistan-Kazakhstan rail link only recently secured funding (in July 2009) from the Islamic Development Bank for the southern segment. Disputes over the transit of electricity within Central Asia in January have severely disrupted Turkmenistan's exports of electricity via Uzbekistan to Tajikistan. However, renegotiated contract terms in March, in particular regarding electricity transit, have solved the issue for now and may allow for the necessary investment to upgrade the grid.

Financial sector

Despite the successful reunification of the exchange rate and the new exchange regulations that were introduced in 2008, reform of the financial sector has progressed slowly and continues to be dominated by state-owned banks. Directed lending with subsidised interest rates, in particular to the textile and agriculture sectors, remains endemic. The redenomination of the currency was completed in January 2009 and the central bank remains committed and has intervened regularly on the foreign exchange market to support the new exchange rate and satisfy the increased demand for foreign exchange from commercial banks. The requirement for all banks to use International Financial Reporting Standards (IFRS) as of 2009 has led to initial improvements in accounting. The central bank has also lifted a ban on international banking operations of commercial banks; they are now able to open correspondent accounts with foreign banks and conduct SWIFT transactions. The government has also launched consumer loans for educational purposes via the government-owned banks.

Social sector

To soften the impact of higher food prices, the government approved a small budgetary deficit for both 2008 and 2009 to allow a 10 per cent increase in public sector salaries and pensions as well as health allowances and scholarships. A new Labour Code is also being prepared, which will update the existing labour law that dates from 1993. The Code will expand the rights of employees, including part-time workers. It will limit the use of short-term contracts in the public sector that have, in the past, led to increased side payments to ensure job security. The law also includes provisions for longer annual leave.

With the support of the European Union, ongoing work on reforming the budgetary process has started to improve the transparency of budget operations. An important step was the closure of several extra-budgetary accounts and the establishment of a stabilisation fund under the supervision of the Ministry of Finance. Since October 2008 foreign exchange revenues have been transferred into this new fund. In the short term the fund will be used to counterbalance the limited effects of the global financial crisis. Ultimately it is intended that the fund should be used to make long-term investments targeted at infrastructure, education and health. The authorities aim to model this fund on similar funds in Norway and Russia, but explicit investment rules have yet to be published.

Macroeconomic performance

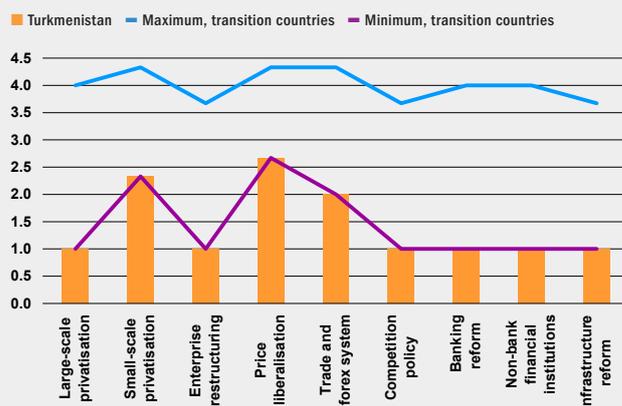
The Turkmen economy has grown strongly in the last few years, with double-digit GDP growth recorded every year between 2004 and 2008, mainly on the back of increasing hydrocarbon prices and higher negotiated off-take volumes. Large public investments in construction and infrastructure and growth in the service sector – particularly transportation, communication and retail – have supported double-digit growth in the non-hydrocarbon sector. The current account surplus has been in strong surplus since 2004, and was nearly 19 per cent of GDP in 2008. Imports of goods and services were boosted by higher domestic demand and better access to foreign exchange. However, higher hydrocarbon earnings have led to a 20 per cent increase in export receipts. Turkmenistan successfully negotiated further significant increases in gas off-take prices and volumes for 2009 onwards and has, for the first time, linked these agreements to loans from off-takers to finance hydrocarbon infrastructure. Foreign direct investment (FDI) inflows continue to mainly finance investments in offshore oil and gas production in the Caspian Sea.

As gas exports prices converge with European levels, international reserves have further increased. Exchange rate unification was completed on 1 May 2008 at the rate of 14,250 manat per US dollar, a level broadly consistent with the country's strong external position. With liberalised petrol prices and higher food prices, inflation at one point reached 13 per cent in 2008. Credit grew strongly up to 2008, mainly reflecting increased directed lending to the cotton sector. A small fiscal deficit was budgeted for 2008 and 2009, but government revenues outperformed expectations and government investments were delayed, leaving the actual budget for 2008 in surplus. Tax collection has also improved, benefiting from streamlined tax and customs procedures.

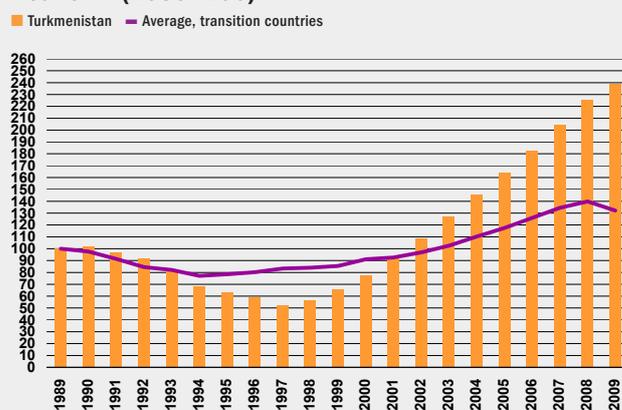
Outlook and risks

The overall outlook for 2009 is favourable given that Turkmenistan's gas export prices are still catching up with European market prices. With new onshore and offshore hydrocarbon discoveries, medium-term growth prospects remain positive. However, a technical accident in the main gas pipeline to Russia in April 2009 disrupted gas supplies and highlighted Turkmenistan's vulnerability regarding their biggest hydrocarbon off-taker. This has led to increased efforts to diversify Turkmenistan's exports. More broadly, Turkmenistan's undiversified economy remains vulnerable to commodity price fluctuations. The main macro risks are therefore related to potential renegotiations of gas off-take prices, lower than planned investment in hydrocarbon infrastructure and weaker than expected international demand for hydrocarbons. Channelling FDI into the non-hydrocarbon sector and creating a business environment that fosters the private sector outside of oil and gas remains a major challenge. Continued inflationary pressures and real appreciation are also a longer-term risk to the competitiveness of the private sector.

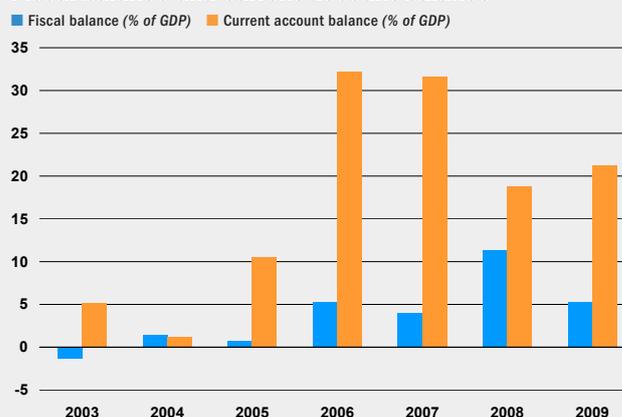
Transition indicators 2009



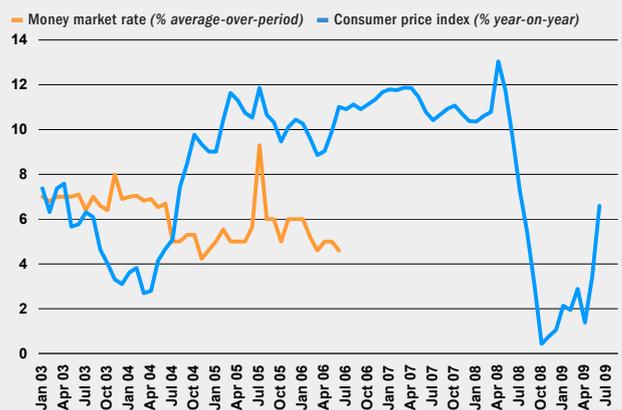
Real GDP (1989=100)



Fiscal balance and current account balance



Interest rates and inflation



Liberalisation and privatisation	Business environment and competition	Infrastructure	Financial sector	Social reform
Current account convertibility – limited	Competition office – no	Telecoms regulatory assessment compliance – low	Capital adequacy ratio – 10 per cent ²	Share of population living in poverty – na
Controls on inward direct investment – no ¹	Quality of insolvency law – very low	Independence of the electricity regulator – no	Deposit insurance system – no	Government expenditure on health – 4.8 per cent (2005)
Interest rate liberalisation – limited de jure	Secured transactions law – malfunctioning	Separation of railway infrastructure from operations – no	Private pension funds – no	Government expenditure on education – 5.4 cent (2005)
Exchange rate regime – fixed		Independence of the road directorate – no		Household expenditure on power and water – 0.3 per cent
Wage regulation – yes				
Tradeability of land – limited de jure				

Structural and institutional change indicators

	2003	2004	2005	2006	2007	2008	2009
Enterprises							
Privatisation revenues (cumulative, in per cent of GDP)	0.6	0.6	0.6	na	na	na	na
Private sector share in GDP (in per cent)	25.0	25.0	25.0	25.0	25.0	25.0	25.0
Private sector share in employment (in per cent)	na	na	na	na	na	na	na
Budgetary subsidies and current transfers (in per cent of GDP)	na	na	na	na	na	na	na
Share of industry in total employment (in per cent)	13.8	14.0	na	na	na	na	na
Change in labour productivity in industry (in per cent)	10.7	12.0	na	na	na	na	na
Investment/GDP (in per cent)	25.3	23.8	na	na	na	na	na
<i>EBRD index of small-scale privatisation</i>	2.0	2.0	2.0	2.0	2.0	2.3	2.3
<i>EBRD index of large-scale privatisation</i>	1.0	1.0	1.0	1.0	1.0	1.0	1.0
<i>EBRD index of enterprise reform</i>	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Markets and trade							
Share of administered prices in CPI (in per cent)	6.7	6.7	6.7	6.7	6.7	6.7	na
Number of goods with administered prices in EBRD-15 basket	5.0	6.0	6.0	6.0	6.0	5.0	na
Share of trade with non-transition countries (in per cent)	54.4	51.2	43.2	46.6	48.8	na	na
Share of trade in GDP (in per cent)	102.1	99.9	94.6	93.5	101.2	90.5	na
Tariff revenues (in per cent of imports) ³	na	na	na	na	na	na	na
<i>EBRD index of price liberalisation</i>	2.7	2.7	2.7	2.7	2.7	2.7	2.7
<i>EBRD index of forex and trade liberalisation</i>	1.0	1.0	1.0	1.0	1.0	2.0	2.0
<i>EBRD index of competition policy</i>	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Financial sector							
Number of banks (foreign-owned)	12 (4)	11 (2)	11 (2)	11 (2)	11 (2)	11 (2)	na
Asset share of state-owned banks (in per cent)	96.1	96.6	96.3	94.8	93.7	96.3	na
Asset share of foreign-owned banks (in per cent)	1.6	1.0	1.0	1.0	1.1	1.2	na
Non-performing loans (in per cent of total loans)	0.5	0.4	0.3	0.2	0.2	0.1	na
Domestic credit to private sector (in per cent of GDP)	1.9	1.6	1.4	na	na	na	na
Domestic credit to households (in per cent of GDP)	0.5	0.5	0.7	0.6	0.8	0.7	na
– Of which mortgage lending (in per cent of GDP)	0.1	0.2	0.2	0.2	0.4	0.3	na
Stock market capitalisation (in per cent of GDP)	na	na	na	na	na	na	na
Stock trading volume (in per cent of market capitalisation)	na	na	na	na	na	na	na
Eurobond issuance (in per cent of GDP)	0.0	0.0	0.0	0.0	0.0	0.0	na
<i>EBRD index of banking sector reform</i>	1.0	1.0	1.0	1.0	1.0	1.0	1.0
<i>EBRD index of reform of non-bank financial institutions</i>	1.0	1.0	1.0	1.0	1.0	1.0	1.0
Infrastructure							
Fixed-line (mobile) penetration rate (per 100 inhabitants)	8.0 (0.2)	8.1 (1.1)	8.2 (2.2)	8.6 (4.4)	9.2 (7.0)	9.2 (7.0)	na
Internet users (per 100 inhabitants)	0.4	0.8	1.0	1.3	1.4	1.4	na
Railway labour productivity (1991=100)	38.1	37.7	41.9	44.8	44.6	44.2	na
Residential electricity tariffs (USc kWh)	0.4	0.4	0.4	0.4	0.4	0.3	na
Average collection rate, electricity (in per cent)	na	na	na	na	na	na	na
GDP per unit of energy use (PPP in US dollars per kgoe)	1.3	na	1.3	na	na	na	na
<i>EBRD index of infrastructure reform</i>	1.0	1.0	1.0	1.0	1.0	1.0	1.0
– <i>Electric power</i>	1.0	1.0	1.0	1.0	1.0	1.0	1.0
– <i>Railways</i>	1.0	1.0	1.0	1.0	1.0	1.0	1.0
– <i>Roads</i>	1.0	1.0	1.0	1.0	1.0	1.0	1.0
– <i>Telecommunications</i>	1.0	1.0	1.0	1.0	1.0	1.7	1.7
– <i>Water and wastewater</i>	1.0	1.0	1.0	1.0	1.0	1.0	1.0

¹ Investors are required to register with the State Service for Foreign Investments.

² Calculated with a risk weight of zero for all loans to state-owned enterprises. These are assumed to be implicitly guaranteed by the state.

³ Refers to differential excise taxes on imports; Turkmenistan does not levy import tariffs.

Macroeconomic indicators

	2003	2004	2005	2006	2007	2008 Estimate	2009 Projection
Output and expenditure	<i>(Percentage change in real terms)</i>						
GDP ¹	17.1	14.7	13.0	11.4	11.6	10.5	6.0
– Private consumption	na	na	na	na	na	na	na
– Public consumption	na	na	na	na	na	na	na
– Gross fixed capital formation	na	na	na	na	na	na	na
– Exports of goods and services	4.0	11.2	28.3	44.9	27.4	29.3	na
– Imports of goods and services	40.8	22.1	-6.4	34.8	47.8	41.9	na
Industrial gross output	13.5	16.4	8.5	na	na	na	na
Agricultural gross output	9.5	13.0	4.0	na	na	na	na
Employment	<i>(Percentage change)</i>						
Labour force (end-year)	3.0	3.0	na	na	na	na	na
Employment (end-year)	2.2	na	na	na	na	na	na
	<i>(In per cent of labour force)</i>						
Unemployment ²	29.8	30.2	na	na	na	na	na
Prices and wages	<i>(Percentage change)</i>						
Consumer prices (annual average)	5.6	5.9	10.7	10.5	8.6	12.0	5.5
Consumer prices (end-year)	3.1	9.0	10.4	7.1	8.6	8.9	6.0
Producer prices (annual average)	na	na	na	na	na	na	na
Producer prices (end-year)	na	na	na	na	na	na	na
Gross average monthly earnings in economy (annual average)	84.2	5.7	21.6	na	na	na	na
Government sector³	<i>(In per cent of GDP)</i>						
General government balance	-1.3	1.4	0.8	5.3	4.0	11.3	5.3
General government expenditure	19.4	18.9	19.7	14.9	13.4	12.3	na
General government debt	na	na	na	na	na	na	na
Monetary sector	<i>(Percentage change)</i>						
Broad money (M3, end-year)	33.4	13.6	5.6	10.7	96.4	-7.6	na
Domestic credit (end-year)	-0.6	3.6	-3.5	-6.7	31.0	52.2	na
	<i>(In per cent of GDP)</i>						
Broad money (M3, end-year)	13.2	12.3	10.2	9.2	15.0	7.7	na
Interest and exchange rates	<i>(In per cent per annum, end-year)</i>						
Refinance rate	10.0	5.0	na	na	na	na	na
Interbank market rate	6.9	4.6	na	na	na	na	na
Deposit rate (6-12 months) ⁴	15.4	11.3	na	na	na	na	na
Lending rate (6-12 months) ⁴	20.4	17.3	na	na	na	na	na
	<i>(Manats per US dollar)</i>						
Exchange rate (end-year) ⁵	10,390.0	10,540.0	10,870.0	10,690.0	10,690.0	14,250.0	na
Exchange rate (annual average)	10,033.5	10,375.0	11,015.2	10,881.9	10,690.0	13,041.5	na
External sector	<i>(In millions of US dollars)</i>						
Current account	305.0	82.2	876.9	3,347.2	4,036.0	3,560.0	5,300.0
Trade balance	886.0	705.5	1,997.1	4,597.8	5,334.0	6,423.0	7,900.0
– Merchandise exports	3,465.0	3,853.9	4,944.1	7,155.5	9,114.0	11,786.0	14,500.0
– Merchandise imports	2,579.0	3,148.4	2,947.0	2,557.7	3,780.0	5,363.0	6,600.0
Foreign direct investment, net	226.0	353.7	418.2	730.9	804.0	820.0	1,355.0
Gross reserves, excluding gold (end-year) ⁶	2,673.0	2,714.0	3,442.0	7,477.2	na	na	na
External debt stock	1,519.0	1,273.0	1,007.0	805.0	na	na	na
	<i>(In months of imports of goods and services)</i>						
Gross reserves, excluding gold (end-year)	9.5	8.0	10.7	25.0	na	na	na
	<i>(In per cent of exports of goods and services)</i>						
Debt service ⁷	11.6	9.6	5.7	3.9	na	na	na
Memorandum items	<i>(Denominations as indicated)</i>						
Population (end-year, million)	6.2	6.5	6.5	6.5	6.5	6.5	6.5
GDP (in billions of manats)	59,404.8	72,706.4	91,863.2	113,073.6	136,244.0	247,152.0	361,670.0
GDP per capita (in US dollars)	954.9	1,078.1	1,283.0	1,598.6	1,960.8	2,915.6	3,837.3
Share of industry in GDP (in per cent)	39.7	38.6	na	na	na	na	na
Share of agriculture in GDP (in per cent)	19.6	18.4	na	na	na	na	na
Current account/GDP (in per cent)	5.2	1.2	10.5	32.2	31.7	18.8	21.2
External debt – reserves (in US\$ million)	-1,154.0	-1,441.0	-2,435.0	-6,672.2	na	na	na
External debt/GDP (in per cent)	25.7	18.2	12.1	7.7	na	na	na
External debt/exports of goods and services (in per cent)	40.8	30.2	19.1	10.7	na	na	na

¹ Official statistics until 2004, but EBRD estimates thereafter.

² Officially registered unemployed.

³ Significant off-budget expenditures occur through extra-budgetary funds and lending.

⁴ Unweighted average deposit and lending rates for individuals (in local currency) of state commercial banks.

⁵ Before May 2008 Turkmenistan operated a dual exchange rate system. The series refers to a weighted average between the official exchange rate and the commercial rate (given as the black market rate). Weights are variable depending on official and shuttle trade.

⁶ Includes foreign exchange reserves of the central bank plus the foreign exchange reserve fund.

⁷ Excludes rescheduled amounts.