Kazakhstan

Highlights

- **Economic growth continues amid rising inflation.** Real gross domestic product (GDP) grew 3.6 per cent year on year in the first half of 2022, driven by strong export growth amid elevated commodity prices. However, rising inflation and logistical challenges suggest a need to expand the capacity of existing trade routes and diversify into new ones.
- **Significant improvements in governance are under way.** Key developments in 2022 include the strengthening of parliament's role, efforts to renationalise embezzled assets and reduce the dominance of vested interests, and the appointment of new leaders to top government and state-owned enterprise management positions.
- **The reform agenda is advancing at a brisk pace.** The government has recently unveiled a comprehensive economic reform package to address gaps in the rule of law and protection of property rights, the competitive environment, industrial policies and social support mechanisms, human capital and public administration.

Key priorities for 2023

- **The government should intensify efforts to diversify trade and investment flows.** In light of the international sanctions imposed on Russia, Kazakhstan needs to re-route trade flows, build new supply-chain relationships and reach international agreements on key investments in alternative trade and transport corridors to take its export products to Europe and other markets, such as the Gulf region and south and south-east Asia.
- **Efforts to restore macroeconomic stability are urgently needed.** Ineffective fiscal stimulus measures, including support policies for small and medium-sized enterprises (SMEs), should be wound down and the central bank's involvement in subsidising the economy reduced as part of a broader effort to curb inflationary pressures, reduce the fiscal deficit and slow debt accumulation.
- **Social policies should be redesigned.** Targeted income support for the vulnerable should replace price controls and tariff subsidies for all. Utility tariffs should be brought closer to cost recovery over time to incentivise resource-saving behaviour, as well as private investment in renewables and energy-efficient technologies.

TABLE Main macroeconomic indicators %

	2018	2019	2020	2021	2022 proj.
GDP growth	4.1	4.5	-2.6	4.1	3.0
Inflation (average)	6.0	5.2	6.8	8.0	14.0
Government balance/GDP	2.6	-0.6	-7.0	-5.0	-2.0
Current account balance/GDP	-0.1	-4.0	-3.8	-2.9	3.0
Net FDI/GDP [neg. sign = inflows]	-0.2	-2.1	-4.2	-0.9	-1.1
External debt/GDP	89.4	87.8	96.2	83.7	n.a.
Gross reserves/GDP	15.7	15.9	20.8	17.4	n.a.
Credit to private sector/GDP	25.9	24.3	25.6	n.a.	n.a.

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Macroeconomic developments and policy response

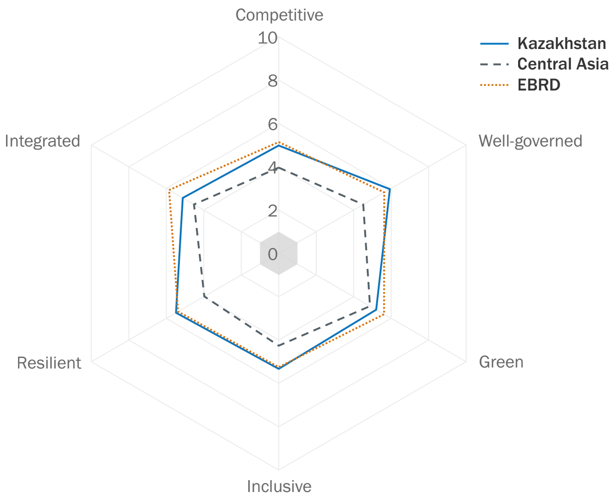
Economic growth has continued. Real GDP grew 3.6 per cent year on year in the first half of 2022. Despite disruptions at the Caspian Pipeline Consortium's terminal in Novorossiysk, exports demonstrated remarkable resilience (up 50.6 per cent year on year in January-August 2022) amid high oil prices. Growth was broad based, driven by the very strong performance of construction, transport and warehousing, and the economy is resilient to external shocks, despite taking on additional debt. Preliminary estimates suggest that the current account achieved a record surplus of US$ 6.6 billion in the first half of 2022, compared with a deficit of US$ 2.8 billion a year ago, driven by external demand for energy products. Official foreign-exchange reserves and assets held by the National Bank of Kazakhstan (NBK) and the National Oil Fund amount to US$ 83.8 billion (approximately 44 per cent of GDP) well above the country's total external public debt (18.4 per cent of GDP).

Inflation has been gaining momentum since late 2021. The war on Ukraine and sanctions on Russia led to a sharp depreciation in the Kazakh tenge (KZT) in late February-March 2022. To prevent excessive exchange-rate volatility, the NBK intervened in the foreign-exchange market and introduced a deposit protection programme, offering a premium interest rate on local currency-denominated deposits held in banks for at least one year. The NBK has also increased the policy rate in steps, from 9.75 per cent in December 2021 to 16.0 per cent in October 2022. However, strong growth of nominal wages (25.6 per cent year on year in September), coupled with a surge in transport, food and commodity prices, added to inflationary pressures, with CPI increasing by 18.8 per cent year on year in October compared with 8.4 per cent in December 2021.

The policy response to global and regional shocks has been varied. In addition to tightening monetary policy, the NBK has scaled back its involvement in financing post-Covid-19 stimulus programmes by exiting five out of seven state support programmes. Meanwhile, the government has introduced a new plan to ensure food security for 2022-24. As a temporary measure, the authorities have banned or restricted exports of certain key products, such as sugar and wheat. The country remains vulnerable to transport and logistics disruptions, as highlighted by "technical" incidents at the Caspian Pipeline Consortium's terminal in Novorossiysk, which accounts for about two-thirds of Kazakhstan's oil exports. While increasing oil shipments through available alternatives, Kazakhstan has joined regional efforts to add capacity on other trade routes, such as the Trans-Caspian Corridor.

Economic growth is likely to slow in the short term. Overall, we expect the economy to expand by 3.0 per cent in 2022 and 3.5 per cent in 2023. Significant downside risks remain, including any potential interruption to oil transit through Novorossiysk and continued challenges related to trade logistics worsening due to a further escalation of the geopolitical conflict over Ukraine.

CHART Assessment of transition qualities (1-10)



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Structural reform developments

Political and economic governance is improving. Following the events of January 2022, the authorities emphasised the need to eliminate all artificial monopolies and underscored the urgency of transitioning from a "super-presidential" form of government to a presidential republic with a strong parliament. A nationwide referendum in June 2022 approved constitutional amendments designed to enhance political competition, reduce the president's powers, strengthen the lower house of parliament and improve human rights. Meanwhile, the government unveiled a comprehensive economic reform package prepared by the Agency for Reforms and Strategic Planning. The package addresses gaps in the rule of law and protection of property rights, the competitive environment, industrial policies and social support mechanisms, human capital and public administration.

A new programme to promote investment is in place. The New Investment Policy Concept of the Republic of Kazakhstan to 2026, approved by the government in June 2022, aims to boost fixed capital investment from 16.3 per cent of GDP in 2021 to 25.1 per cent of GDP by 2026 and to increase the inflow of foreign direct investment (FDI) to US$ 25.5 billion over the same period. The concept emphasises the need to enhance labour productivity, increase export volumes and complexity, develop higher-value-added activities and facilitate technological transfers and the gradual localisation of advanced production processes. In addition, it focuses on investment in transport infrastructure to help integrate regional and global value chains and to develop the skills needed to deliver strategically important investment projects.

SME development is being promoted. In April 2022, the government adopted the Concept for the Development of Small and Medium-sized Enterprises of the Republic of Kazakhstan to 2030. Under this concept, the contribution of SMEs should increase from 33.5 per cent of GDP to 40 per cent by the end of the decade, with medium-sized companies contributing 20 per cent of GDP. To this end, the government has committed to reducing red tape and regulatory barriers for SMEs, enhancing the effectiveness of budgetary spending and existing SME support mechanisms, and developing high-quality infrastructure and automated reporting processes.

New counter-cyclical budgetary rules are being introduced. The new rules, to be implemented in the 2023-25 budgets, are designed to strengthen the country's fiscal stance. Two additional rules concern: (i) a cap on government spending growth; and (ii) setting transfers from the National Fund in relation to a cut-off price for oil.

Kazakhstan is advancing the digitalisation agenda. In June 2022, the NBK launched the Instant Payment System (IPS) platform. The IPS enables 24/7 interbank transfers using a mobile phone number or QR code. The authorities are exploring the opportunity to introduce digital currency (digital tenge), which would enhance financial inclusion by increasing the availability and affordability of financial services. On 1 July 2022 the National Bank and Centre for Development of Payment and Financial Technologies of the National Bank of Kazakhstan published a study discussing a decision-making model for the introduction of digital tenge. The project is currently being piloted. A final decision on the introduction of the digital currency is expected to be made by the end of 2022.

A long-term decarbonisation strategy is being developed. In 2020, Kazakhstan announced its commitment to reaching carbon neutrality by 2060. As part of its decarbonisation strategy, utility tariffs will be gradually brought closer to cost recovery, while the state will provide vulnerable families with targeted assistance. This will help the country remain on track to meet its objectives on the climate front by incentivising private investment in renewables and energy-efficient technologies.

The banking system is adjusting to geopolitical developments. To ensure compliance with international sanctions on Russia, local banks are working to strengthen their "know your client" practices when dealing with international customers. The Kazakh subsidiaries of sanctioned Russian banks Alfa Bank and Sberbank were recently purchased by BCC and Baiterek, respectively, while VTB is still negotiating with potential investors.

Kyrgyz Republic

Highlights

- **The economy is growing strongly in 2022.** Real gross domestic product (GDP) expanded 7.2 per cent year on year from January to September 2022 amid strong growth in industrial production, hospitality, trucking, retail and wholesale trade. However, a 6.5 per cent year-on-year drop in net remittances in January-August 2022 and strong inflationary pressures are clouding the outlook.
- **New tax and customs regulations have been introduced.** The new tax code mandates the use of cash registers, resulting in significantly higher tax revenues. By reducing illicit trade, these reforms may also help level the playing field for companies operating in the formal economy.
- **The investment environment is improving.** Strengthening the powers of the business ombudsman gives Kyrgyz companies an effective channel for addressing grievances. By resolving a long-running dispute with Canada's Centerra Gold Inc over the Kumtor gold mine, the government has cleared a major roadblock to gold exports and further foreign direct investment (FDI) in mining activities.

Key priorities for 2023

- **The need to ensure food and energy security is both urgent and challenging.** With food expenditure accounting for more than 50 per cent of total household spending, rising food and energy prices are putting additional pressure on vulnerable population groups. Because it has limited fiscal space, the government should opt for well-targeted and effective mechanisms to support those in need.
- **The authorities should step up efforts to ensure macroeconomic stability.** The recent increase in government revenues should be used to strengthen fiscal buffers rather than finance additional current expenditures, which may potentially add to inflationary pressures resulting from the country's reliance on imported commodities.
- **Efforts to improve the investment climate must continue.** The government should adopt measures to enhance access to electricity and other essential infrastructure, liberalise the labour market (ease restrictions on the hiring of foreigners) and streamline the licensing, permits and inspection systems. Investment in agriculture could be facilitated by establishing "free agricultural zones" to overcome legal restrictions on the foreign ownership of land.

TABLE Main macroeconomic indicators %

	2018	2019	2020	2021	2022 proj.
GDP growth	3.5	4.6	-8.6	3.7	7.0
Inflation (average)	1.5	1.1	6.3	11.9	13.5
Government balance/GDP	-0.6	-0.1	-3.3	-0.4	-3.3
Current account balance/GDP	-12.1	-11.9	4.8	-8.7	-12.5
Net FDI/GDP [neg. sign = inflows]	-1.7	-4.6	5.2	-6.8	-3.6
External debt/GDP	101.7	104.4	117.4	106.1	n.a.
Gross reserves/GDP	26.1	27.4	36.1	34.9	n.a.
Credit to private sector/GDP	23.4	24.6	28.3	26.0	n.a.

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Macroeconomic developments and policy response

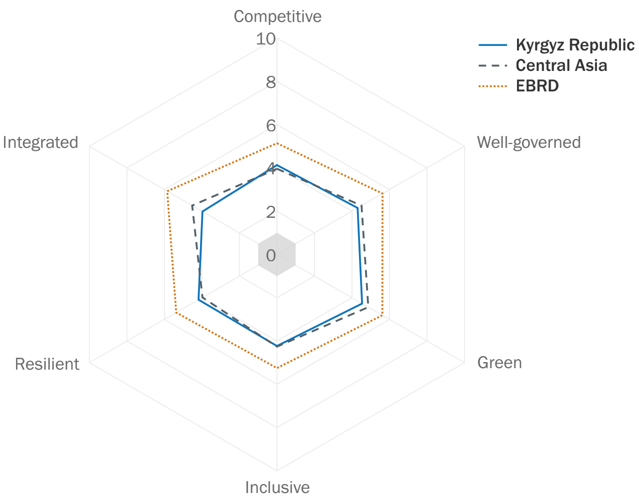
The economy has bounced back robustly in 2022. The economy expanded 7.2 per cent year on year in the first nine months of 2022 despite a major drop in exports. Wage increases for public-sector employees and strong demand for qualified labour, coupled with the government's efforts to reduce informality led to more than a 25 per cent increase in nominal wages – well above inflation (which was 15.5 per cent in September). Strong domestic demand resulted in gains in industrial production (up 16.6 per cent year on year), hospitality (up 19.4 per cent year on year), retail and wholesale trade (up 7.2 per cent year on year) and trucking (up 35.5 per cent year on year). Imports saw a gain of 77.2 per cent year on year in January-August 2022 on the back of higher global prices for food and energy products, as well as lower corruption in customs administration at the country's borders. In the first seven months of 2022, the Kyrgyz Republic imported 4.8 times more knitted fibre and 2.3 times more synthetic fibre than a year ago, suggesting a potential boost in re-exporting activity and textile production. However, stagnant fixed capital investment (up just 0.5 per cent year on year in January-September 2022) may hold back further growth.

Inflationary pressures persist, prompting some short-term measures. Fuelled by rising global prices and supply-chain disruptions, annual inflation reached 15.5 per cent in September 2022, far exceeding the National Bank's target range of 5-7 per cent and putting pressure on vulnerable households. The Kyrgyz som suffered the largest depreciation of the Central Asian currencies following the Russian rouble's collapse in early March 2022, but has since recovered to its pre-war value, in line with its regional peers. To soften the impact, in April 2022 the authorities prolonged until the end of 2022 the zero per cent value added tax (VAT) rate on imported grain for those involved in flour processing. What is more, to prevent a sugar deficit, in March 2022 the government reached agreement with the Eurasian Economic Commission on the delivery of 105,000 tonnes of duty-free sugar and raw materials. Concurrently, the authorities introduced a six-month ban on sugar exports, effective June 2022.

The fiscal stance is improving. In January-August 2022 growth in government spending (up 45.7 per cent year on year) was offset by a substantial (1.5-fold) increase in tax revenues (mostly VAT), resulting in a budget surplus of 1.2 per cent of GDP. However, since the beginning of 2022 gross international reserves have shrunk 18.8 per cent from US$ 2,978 million in December 2021 to US$ 2,416 million in August 2022. On the positive side, the government recently created the Holding of Nomads wealth fund to facilitate the accumulation of revenues from the Kumtor gold mine.

The economy should continue to grow strongly in the short term. We forecast an expansion in GDP of 7.0 per cent in both 2022 and 2023. The economy stands to gain from increased re-export opportunities, the relocation of Russian companies and individuals, including information technology (IT) developers and entrepreneurs. Nevertheless, downside risks remain, mostly related to rising inflation, high reliance on remittances from Russia and other regional and global shocks.

CHART Assessment of transition qualities (1-10)



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Structural reform developments

A new national development programme for 2021-26 was approved in October 2021. The programme seeks to achieve a sustainable 5 per cent annual GDP growth rate, GDP per capita of at least US$ 1,500, a decrease in the unemployment rate to 5 per cent and a reduction in the poverty rate to 20 per cent. A corresponding roadmap was developed in January 2022 to boost economic activity, support entrepreneurship, implement fiscal reforms and promote initiatives in the areas of energy, mining, manufacturing, transport and the green economy.

A new public debt management strategy for 2022-24 has been introduced. The strategy, approved in July 2022, is designed to improve the country's debt sustainability. Under the strategy, new loans should have at least a 35 per cent concessional element, debt servicing should be timely and no more than 45 per cent of total debt should be attributed to a single creditor.

The authorities have introduced a new tax code. The new code, effective from 2022, mandates the use of cash registers at all points of sale. This reform is likely to help the authorities clamp down on illicit trade and shadow economic activities, thus contributing to public revenues, levelling the playing field for companies operating in the formal economy and creating incentives for investment in manufacturing.

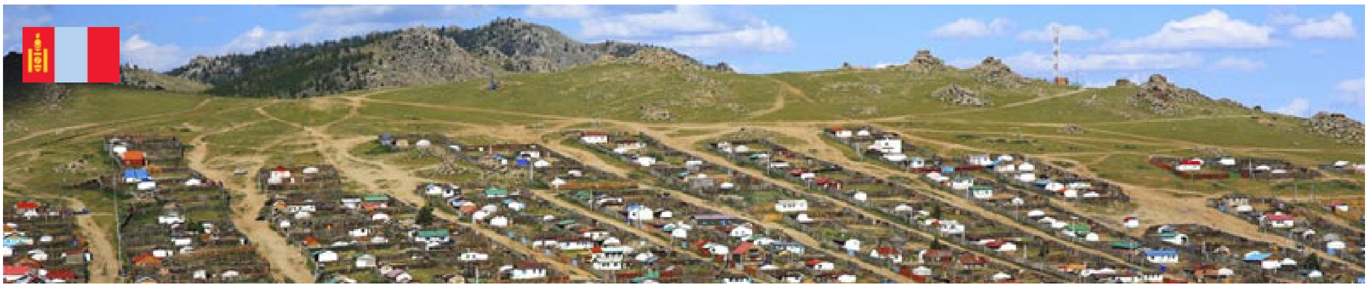
The Kyrgyz authorities have resolved a long-running dispute with a major foreign investor. In April 2022 the authorities reached agreement with Canada's Centerra Gold Inc over Kumtor, the country's largest gold mine. The dispute arose when the government introduced external management to the mine, claiming violation of the country's environmental and mining standards. According to the agreement, Kumtor will be fully transferred to the Kyrgyz Republic. In another positive development, on 3 May 2022, the London Bullion Market Association restored Kyrgyzaltyn, the country's exclusive exporter of gold, to its Good Delivery list of accredited refiners, clearing a major roadblock to future gold exports and FDI.

A major railway construction project is about to be launched. A trilateral agreement signed at the Shanghai Cooperation Organization in Samarkand in September 2022 paves the way for the construction of the US$ 4-5 billion China-Kyrgyz Republic-Uzbekistan railway project. On ice for more than 20 years, this project will enhance regional connectivity by creating strong competition on the east-west railway routes across Eurasia.

A new programme has been launched to develop public-private partnerships (PPPs) from 2022 to 2026. Approved in June 2022, the programme aims to streamline the regulatory and legal framework and introduce financial tools to increase the attractiveness of PPP projects. It mandates the creation of a rigorous PPP methodology and a strengthening of the government's institutional capacity in related areas.

Further measures to diversify the economy are advancing. In an effort to diversify the economy, the Concept for the Development of Creative Economy for 2022-26 was approved in April 2022. In August 2022, the president signed a law on the Park of Creative Industries, seeking to stimulate innovation, increase the investment attractiveness of creative activities and reduce the national economy's dependence on the mining sector and migrant remittances.

In August 2022 the Kyrgyz Republic piloted its Digital Nomad initiative, seeking to create favourable conditions for developers and IT specialists from abroad. The project envisages granting "digital nomad" status to qualified foreigners, which will significantly reduce red tape and ease the relocation process by allowing for visa- and work permit-free entry to and employment in the country.



Mongolia

Highlights

- **Growth is being affected by external shocks.** Real gross domestic product (GDP) grew by 1.9 per cent year on year in the first six months of 2022, despite intermittent border closures due to China's zero-Covid policy. Growth was supported by high commodity prices (total exports gained 29.8 per cent in the first half of the year) and the robust expansion of agriculture and service sectors.
- **The longstanding dispute with Rio Tinto over development costs for the Oyu Tolgoi copper mine has been resolved.** This helps allay concerns about Mongolia's investment climate while at the same time increasing the country's share of any benefits from future foreign direct investment (FDI) in the mining sector.
- **Mongolia is promoting its digitalisation agenda.** The newly established Ministry of Digital Development and Communications signed a memorandum of understanding with Estonia's e-Governance Academy to digitalise a wide range of government services, in a significant step towards Mongolia's digital transformation.

Key priorities for 2023

- **Better targeting of support measures and fiscal consolidation are required to ensure macroeconomic stability and debt sustainability.** Large stimulus spending in 2020-21 led to persistent imbalances, constraining the government's fiscal space and pushing public debt close to 100 per cent of GDP. Monetary policy remains accommodative (the policy rate is below the inflation rate), encouraging growth at the expense of price stability, adding to the inflationary pressures stemming from more complicated import logistics and higher commodity prices.
- **The authorities should step up efforts to improve the management of critical border crossing points and invest in connectivity.** Greater efficiency of and additional physical capacity in freight transport will allow the country to benefit fully from elevated commodity prices and reduce bottlenecks on existing trade routes.
- **Plans to improve regional inclusion should be stepped up.** Current efforts to bring essential services and modern infrastructure to Ulaanbaatar's ger districts and build new modern districts outside the capital should be accelerated. Improved municipal services would boost living conditions for the poor and enhance their access to the labour market.

TABLE Main macroeconomic indicators %

	2018	2019	2020	2021	2022 proj.
GDP growth	7.7	5.6	-4.6	1.6	3.5
Inflation (average)	6.8	7.3	3.7	7.1	14.8
Government balance/GDP	2.9	1.0	-9.2	-3.1	-0.4
Current account balance/GDP	-16.7	-15.2	-5.1	-12.8	-20.3
Net FDI/GDP [neg. sign = inflows]	-14.8	-17.2	-12.9	-13.3	-14.5
External debt/GDP	249.4	250.5	275.8	219.8	n.a.
Gross reserves/GDP	27.0	30.7	34.2	28.9	n.a.
Credit to private sector/GDP	55.4	48.9	45.8	46.3	n.a.

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Macroeconomic developments and policy response

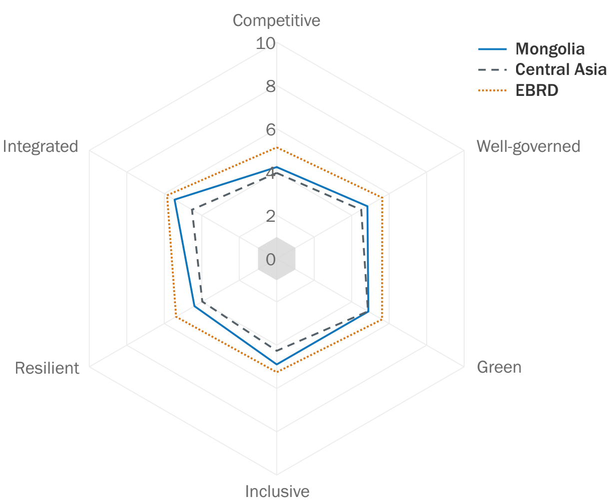
Growth has been modest so far in 2022. The economy shrank by 3.8 per cent year on year in the first quarter of 2022, but rebounded in the second quarter on the back of agriculture (up 11.3 per cent year on year) and services (up 4.9 per cent year on year), giving an overall growth rate of 1.9 per cent year on year in the first half. The country's lack of diversification means that economic performance remains closely linked to China's demand for its key export products (coal, copper and iron ore), though gold provides a significant hedge (increasing from 7.3 to 20 per cent of total exports in 2020). The recent Covid-19 outbreaks in China and Russia's war on Ukraine put further pressure on the Mongolian economy, with volatile demand from China resulting in a contraction in the Mongolian mining and quarrying sector (down 28.8 per cent year on year in the first half).

Inflation has become a key concern, necessitating a policy response. Inflation peaked at 16.9 per cent year on year in June 2022, driven by supply-chain disruptions, higher transport costs and the rising prices of imported goods. Excessive stimulus spending and the accommodative monetary policy stance of the Bank of Mongolia (BoM) have also been important drivers. Having kept its benchmark interest rate unchanged at 6 per cent from November 2020 till March 2022, the BoM raised it stepwise to 12 per cent by September 2022. Consequently, inflation slowed down to 13.8 per cent year on year in September. To counter the impact of rising food prices, the Ministry of Food, Agriculture and Light Industry (MoFALI) has signed agreements with 17 businesses with regard to customs tax exemptions on wholesale imports of rice, sugar and vegetable oil in exchange for ensuring price stability.

External resilience remains a challenge. The currency has come under pressure and lost about 14.6 per cent of its value (as of 23 September 2022) against the US dollar since late February 2022. The BoM's current international reserves (about US$ 3.1 billion) cover six months of imports and 53 per cent of upcoming debt payments. In May 2022 Fitch affirmed Mongolia's B rating with a stable outlook. However, a more recent rating by IHS Markit led to the outlook being downgraded from stable to negative, reflecting negative export dynamics due to frequent border closures with China.

Short-term growth is likely to rise, but downside risks remain significant. We expect real GDP to grow 3.5 per cent in 2022 and 7.0 per cent in 2023. Major downside risks relate mostly to the geopolitical situation and the possibility of negative spill-over effects on Mongolia's main industries. Significant upside potential to 2023 growth lies in the tourism sector, provided it can finally rebound to its pre-pandemic level.

CHART Assessment of transition qualities (1-10)



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Structural reform developments

Major reforms are under way in the banking sector. Amended in January 2021, the Banking Law requires systemically important banks (SIBs) to conduct initial public offerings (IPOs) on the Mongolian Stock Exchange by June 2022 and to reduce maximum ownership by a single shareholder to no more than 20 per cent by 31 December 2023. Complying with the new limit is likely to require SIBs to sell their shares through multiple initial and secondary public offerings (IPOs and SPOs). On the International Monetary Fund's (IMF) recommendation, the deadline for IPOs has been postponed to allow all SIBs to undergo an asset quality review, which was completed by October 2022.

The government launched a new economic reform programme. Introduced in December 2021, the New Recovery Policy envisages a doubling of Mongolia's GDP by 2030 through investment and structural reforms focusing on: (i) border capacity and connectivity; (ii) industrial technology; (iii) regional integration; (iv) energy transmission and distribution networks; (v) climate change mitigation measures; and (vi) governmental and state-owned enterprise (SOE) efficiency. The programme's investment costs are estimated at around MNT 120-150 trillion (US$ 36-45 billion), requiring active cooperation with private-sector companies, foreign investors and international financial institutions.

A major dispute over FDI in the mining sector has been resolved. An important breakthrough occurred in December 2021, when Mongolia's largest foreign investor, Rio Tinto, agreed to write off US$ 2.3 billion of Mongolia's debt related to the Oyu Tolgoi mine. Putting this longstanding dispute to rest will help allay concerns over Mongolia's investment climate, while increasing the country's share of any benefits from future FDI in the mining sector. Meanwhile, in February 2022 the government decided to re-establish the country's Foreign Investment Agency. The agency will be responsible for resolving potential obstacles to FDI, including regulatory barriers and planning issues, as well as for landing high-value investment opportunities in Mongolia. It will also protect investors' interests and provide investor planning support and services.

Mongolia is advancing its digitalisation agenda. In January 2022 the authorities established the Ministry of Digital Development and Communications. In April 2022 the ministry and the Estonian e-Governance academy signed a memorandum of understanding to facilitate Mongolia's digital transformation. The scope of work includes introducing digital identity and electronic signatures, advising civil servants on digital skills and developing digital strategies.

The country is encouraging sustainable finance and mobilising private-sector companies and citizens to reverse deforestation and desertification trends. A national roadmap for sustainable finance, adopted in March 2022, envisages increasing green loans as a share of the total loan portfolios of banks and non-banking financial institutions to 10 and 5 per cent, respectively. Meanwhile, the One Billion Trees national movement, launched in late 2021, envisages the planting of 1 billion trees by 2030, with more than 600 million of those to be planted by large corporations.

Tajikistan

Highlights

- **The economy's post-Covid recovery is continuing apace.** Gross domestic product (GDP) grew 7.4 per cent year on year in the first half of 2022, with strong gains in all sectors. The impact of the war on Ukraine on the economy has been limited, as Russian demand for migrant workers and remittances peaked in the second quarter of 2022, and the country has also improved its external resilience by building up significant international reserves. With inflation at 5.7 per cent in September 2022, Tajikistan is the only regional economy to keep inflation within the central bank's target corridor.
- **Significant amendments to the tax code were put in place in late 2021.** To ease the burden on businesses, reduce informality and support the country's fiscal stance, the number of taxes was decreased from ten to seven and tax rates were reduced across the board. Further improvements and the digitalisation of tax services are envisaged to increase voluntary compliance and minimise corruption.
- **The inclusion agenda is advancing.** The authorities have introduced a new law on equality and the elimination of all forms of discrimination, appointed a Commissioner for Human Rights (ombudsman) and launched a new financial inclusion strategy.

Key priorities for 2023

- **Efforts to bolster food and energy security are required.** In light of export restrictions by neighbouring countries, the authorities should seek ways to diversify import routes. It is vital to ensure price stability by managing food reserves in line with best international practices, balancing market principles and the needs of vulnerable households.
- **The authorities should accelerate infrastructure investment.** The Tajik section of the CASA 1000 transmission line is expected to be completed by the end of 2022. The G7's Partnership for Global Infrastructure and Investment opens up new opportunities for Tajikistan to attract funding for the completion of the Roghun hydropower plant and other infrastructure projects.
- **Tajikistan should continue to improve its tax administration and broaden the tax base to create space for development projects without crowding out social spending or putting debt sustainability at risk.** Measures should include the adoption of a modern risk assessment methodology to guide audits, further simplification of tax reporting requirements, the harmonisation of tax and financial account reporting, the automation of selected taxpayer services, including the value added tax (VAT) refund system, and the gradual deployment of digital technologies, such as digital signatures.

TABLE Main macroeconomic indicators %

	2018	2019	2020	2021	2022 proj.
GDP growth	7.6	7.4	4.39	9.2	7.0
Inflation (average)	3.8	7.8	8.6	9.0	8.3
Government balance/GDP	-2.7	-2.1	-4.3	-0.7	-2.5
Current account balance/GDP	-4.9	-2.2	4.1	8.4	3.8
Net FDI/GDP [neg. sign = inflows]	-2.8	-2.6	-1.3	-0.4	-0.1
External debt/GDP	67.7	69.0	71.1	67.2	n.a.
Gross reserves/GDP	16.5	17.7	27.5	28.6	n.a.
Credit to private sector/GDP	11.9	11.6	13.0	9.7	n.a.

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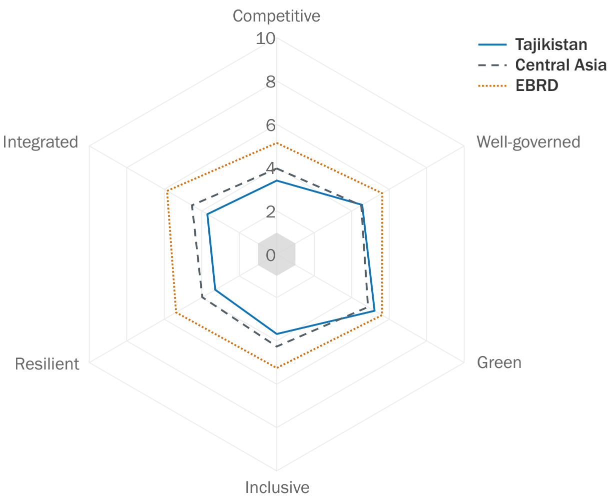
Macroeconomic developments and policy response

Economic growth remains robust. After expanding 9.2 per cent in 2021, the pace of GDP growth slowed marginally in the first half of 2022. An almost complete freeze on the export of precious metals and stones in January to April led to a significant drop in overall exports (down 38 per cent year on year). However, for the first half of 2022, industrial production, including export-oriented mining activities, grew considerably (up 17.3 per cent year on year), while the agriculture sector expanded 7.2 per cent. The rouble's strength and Russia's record demand for migrant workers supported consumer demand, resulting in higher imports (up 25 per cent year on year) and retail trade turnover (up 9.3 per cent year on year). Also, in the first seven months of 2022, Tajikistan saw an 85 per cent increase in imports from China, suggesting that the country is serving as a conduit for parallel imports to Russia. The Tajik somoni recovered almost fully to its pre-war value against the US dollar and appreciated significantly against the euro. Fixed capital investment increased 2.5 per cent on the year in the first half of 2022. Overall, in the first half of 2022 the economy grew 7.4 per cent year on year.

Inflation is easing following timely mitigation measures by the authorities. The National Bank of Tajikistan (NBT) has kept its policy rate well above inflation in 2021-22. Planned tariff increases for utilities (electricity, heat and water) have been postponed until October 2022 to counter the impact of rising food and commodity prices. In August 2022, as inflation slightly exceeded the NBT target range in June and July, the policy rate was increased by 25 basis points (to 13.5 per cent). With inflation easing further to 5.7 per cent in September 2022, the policy rate was restored to 13.0 per cent in November. Tajikistan is currently the only regional economy to keep inflation within the central bank's target corridor (of 4-8 per cent).

Fiscal and external balances have strengthened. In January-May 2022, budget revenues rose 13.6 per cent year on year, driven by a 13 per cent increase in tax receipts. To boost external resilience, Tajikistan has managed to build up significant international reserves. As of 1 July 2022 international reserves provided 8.1 months of import cover. In July total external debt decreased to US$ 3.1 billion from US$ 3.7 billion a month earlier. The country's public debt amounted to US$ 3.1 billion, or 46.3 per cent of GDP and, under the government's debt management strategy 2021-23, will remain below 60 per cent of GDP. Strong growth will continue in the short term. We forecast GDP to grow 7.0 per cent in 2022 and 8.0 per cent in 2023. Downside risks relate to potential violence in Afghanistan spilling over to Tajikistan's territory and/or derailing regional efforts to connect Central Asia to Pakistan and, further south, to India and Iran. Given the importance of the domestic agriculture sector, climate risks present a further vulnerability. An uptick in international financial institution (IFI) investment, supporting Roghun and other infrastructure projects, presents significant upside risk.

CHART Assessment of transition qualities (1-10)



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Structural reform developments

The government has drawn up a new economic plan. Introduced in March 2022, the "action plan for the mitigation/prevention of the potential impacts and risks to the national economy" seeks to maintain macroeconomic stability (control inflation, shift contracts to national currencies, establish correspondent accounts in foreign banks and ensure banking sector stability), protect vulnerable population groups (prevent unreasonable price hikes and ensure adequate stocks of staple goods), improve the investment climate (showcase investment opportunities, allocate concessional credit to domestic producers and facilitate international trade) and ensure the effective and sustainable performance of state-owned enterprises (SOEs) (reduce non-priority expenses, improve financial disclosure and ensure the timely fulfilment of SOEs' obligations to the state budget).

The tax system has been significantly reformed. Significant amendments to the tax code were put in place in late 2021 with a view to weakening the incentives for tax evasion, reducing informality and broadening the tax base. The number of taxes was decreased from ten to seven and tax rates were reduced across the board. Income tax for legal entities was reduced from 23 per cent to 20 per cent and for individuals from 13 per cent to 12 per cent. The VAT rate was reduced from 18 per cent to 15 per cent and further decreases are planned: to 14 per cent in 2023 and 13 per cent in 2027. The social-security tax for employers was reduced from 25 per cent to 20 per cent.

Measures to promote inclusion have advanced. In June 2022 Tajikistan adopted a new law on equality and the elimination of all forms of discrimination – a significant step towards a more inclusive society. The bill introduces legal definitions for segregation, direct and indirect discrimination. In addition, a Commissioner for Human Rights (ombudsman) was appointed to help prevent all forms of discrimination and ensure equality. In a further development in July 2022, the government approved a new strategy for financial inclusion for 2022-26, focusing on digital services, increasing the variety of financial products, protecting customer rights and enhancing financial literacy.

The banking sector is being cleaned up. In 2021 the NBT liquidated three troubled banks – Agroinvestbank, Tojiksodirotbank and Kafolatbank – which had a high concentration of non-performing loans (NPLs). As a result, the NPL ratio declined to 13.4 per cent (as of 30 June 2022) from 22.7 per cent in March 2021.

Reforms to the tariff system in the energy sector are lagging. Overall tax arrears have increased substantially (by 25 per cent year on year in January-May 2022), with more than 40 per cent of them due to Tajiktelekom and two state-owned hydropower plants, Sangtuda and Roghun. Non-cost-reflective electricity tariffs are a major obstacle to the further development of the country's electricity system. Barqi Tojik's (Tajikistan's national power utility company) debt to interdependent power producers and the Ministry of Finance is currently assessed at US$ 3.1 billion.

Turkmenistan

Highlights

- **High gas prices are helping to drive growth.** Real gross domestic product (GDP) grew by 6.2 per cent year on year from January to September 2022, as the country's exports added 50 per cent in the first half of 2022 thanks to higher gas prices.
- **Turkmenistan's external position has strengthened significantly.** Following gas pipeline debt repayment to China in 2021 and domestic debt repayment in January 2022, elevated gas prices are likely to further boost government revenues, contributing to the country's borrowing capacity.
- **Turkmenistan is developing trade and transport relations with its neighbours.** The country has agreed to develop bilateral trade, simplify the visa regime and ensure better transport connectivity with its neighbours, and the recently signed agreement on the construction of the China-Kyrgyz Republic-Uzbekistan railway corridor opens up further opportunities for Turkmenistan as a transit hub to Europe via Türkiye and to India via Iran.

Key priorities for 2023

- **The authorities should further liberalise the foreign exchange market.** The spread between the official and parallel market exchange rates has narrowed in 2022 but remains distortive, with access to foreign exchange at the official rate still used by the authorities as an import substitution subsidy, thus resulting in unfair competition and favouritism.
- **The opportunity to address transport and logistics bottlenecks across the Caspian Sea and the north-south trade corridor should be grasped.** Given its location at an important crossroads, Turkmenistan has an excellent opportunity to attract investment in additional transport and logistics corridors running through its territory, including pipelines, railways, roads, sea transport, and logistics infrastructure.
- **National statistics and economic data reporting standards should be improved.** Reliable and accessible economic data would be of benefit to Turkmen policymakers and businesses alike, enabling them to make informed policy and investment decisions.

TABLE Main macroeconomic indicators %

	2018	2019	2020	2021	2022 proj.
GDP growth	6.2	6.3	5.9	6.2	7.0
Inflation (average)	13.3	5.1	7.6	15.0	17.5
Government balance/GDP	-0.2	-0.3	-0.1	0.3	0.6
Current account balance/GDP	4.9	2.8	-3.3	0.6	2.5
Net FDI/GDP [neg. sign = inflows]	-3.3	-3.5	-2.7	-2.0	-1.2
External debt/GDP	15.7	12.1	9.9	8.4	n.a.
Gross reserves/GDP	n.a.	n.a.	n.a.	n.a.	n.a.
Credit to private sector/GDP	n.a.	n.a.	n.a.	n.a.	n.a.

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Macroeconomic developments and policy response

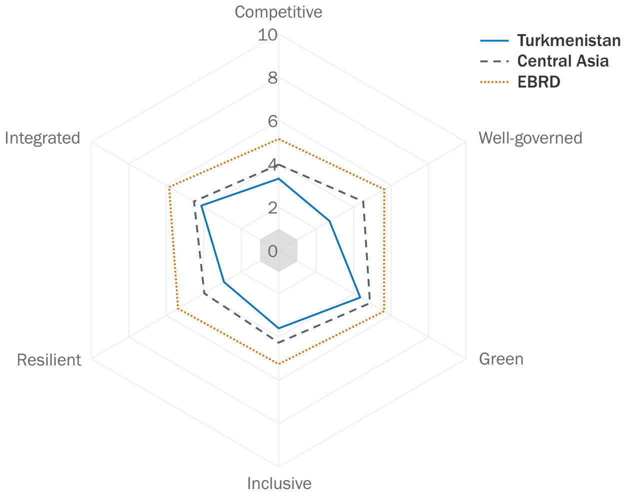
Turkmenistan continues to report remarkably stable growth rates. According to the authorities, the economy expanded by 6.2 per cent year on year from January to September 2022. The construction industry is booming, as reflected in manufacturing and services exceeding the government's plan by 52.5 per cent in January-July. The customs administration reported a particularly strong increase in exports of tomatoes and footwear. Overall, foreign trade turnover increased by 40.7 per cent year on year, and retail trade turnover by 10.5 per cent year on year in the first nine months of 2022.

The gap between the official and market exchange rates has narrowed. The official exchange rate peg continues to be maintained at 3.5 Turkmen manat (TMM) per US dollar. Having appreciated in 2021, the parallel market exchange rate stabilised in March 2022 at around 19 TMM per US$, reflecting greater availability of foreign currency at the heavily subsidised official rate to small and medium-sized enterprises operating in priority sectors (such as food and beverages), in exchange for significant price cuts and/or as a means of encouraging import substitution.

Elevated gas prices have strengthened the country's fiscal stance. In the first half of 2022 the government budget recorded a surplus of 0.1 per cent of GDP; from January to July 2022 government revenues had been officially reported at 103.6 per cent of the target. In August 2022 Fitch affirmed Turkmenistan's "B+" rating with a "Stable" outlook, citing the strong fiscal position but also persistent structural challenges. According to the International Monetary Fund, public debt was just 11.1 per cent of GDP in 2021 and is expected to decline further to 8.4 per cent of GDP in 2022.

Robust growth will continue in the short term. Turkmenistan is likely to continue to benefit from elevated gas prices and the country's "neutral" stance in 2022 and 2023. Overall, the economy is forecast to expand by 7.0 per cent in 2022 and 6.0 per cent in 2023. Downside risk is related to the volatility of gas prices.

CHART Assessment of transition qualities (1-10)



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Structural reform developments

Turkmenistan is gradually ending its self-imposed isolation. Turkmenistan hosted the Ministerial Transport Conference of Landlocked Developing Countries in August 2022, resulting in agreements to jointly develop the international north-south corridor running through Turkmenistan, improve bilateral trade and transport connectivity, and simplify the visa regime. In June 2022 Turkmenistan and Iran signed a cooperation agreement and reached an understanding regarding Iran's outstanding gas debt. The clearing of Iran's US$ 1.8 billion debt will strengthen the government's fiscal accounts and enable the revival of gas exports to Iran, a significant step towards diversification of Turkmen exports. Under an agreement signed in June 2022, a trilateral gas swap deal involving Turkmenistan, Azerbaijan and Iran will allow Turkmenistan to double its gas exports via Azerbaijan.

Work on strengthening the statistical agency is ongoing. The United Nations Development Programme and the State Statistics Committee of Turkmenistan are working to improve the country's statistical capacity. The goal is to streamline existing methodologies in accordance with internationally recognised statistical standards.

Turkmenistan has applied for World Trade Organization (WTO) membership. The application was made in November 2021, and subsequently, Turkmenistan and the WTO reached an agreement to start negotiations. The country's customs authorities are seeking to establish a "single window" for export and import operations and introduced this principle into the Customs Code.

Newly introduced laws significantly harm women's rights. Gender equality has been set back through government-directed social campaigns against certain beauty services and types of clothing, and measures to prevent women from occupying the front seat in private vehicles or using male-driver taxi services.

Uzbekistan

Highlights

- **Strong economic growth is continuing.** The economy expanded by 5.8 per cent year on year in January-September 2022 on the back of a doubling of remittances and gold exports, and macroeconomic stability has been restored following the initially tumultuous reaction to Russia's war on Ukraine.
- **Risks to the investment climate have abated.** Political risks to investment associated with the sudden eruption of social unrest in the Karakalpakstan region have been mitigated through a swift adjustment to the proposed constitutional amendments.
- **Uzbekistan is advancing on the digitalisation agenda.** The authorities have prepared more than 280 projects to facilitate the country's digital transformation, seeking to double the share of digital services in gross domestic product (GDP) in the next two years. Uzbekistan IT Park's "IT visa" mechanism will allow the country to benefit from the inflow of digital nomads, enabling the exchange of knowledge, skills and ideas.

Key priorities for 2023

- **To reduce dependence on Russia's labour market, the authorities should put in place a robust development strategy for small and medium-sized enterprises.** Such a strategy should eliminate artificial incentives for business fragmentation, enabling organic growth, innovation and exports, while addressing the country's regional inclusion challenges.
- **Efforts to accelerate the commercialisation and privatisation of state-owned assets should continue.** The aim should be to achieve greater operational efficiency of strategic state-owned enterprises (SOEs), attract private investment and boost lending to the economy. Privatisations and initial public offerings (IPOs) should be executed in line with best international practice, in a transparent and competitive manner.
- **Further efforts are needed to strengthen food and energy security.** This can be done through improved planning and investment in critical irrigation and food storage infrastructure, and greater energy generation and transmission capacity.

TABLE Main macroeconomic indicators %

	2018	2019	2020	2021	2022 proj.
GDP growth	5.3	5.7	1.9	7.4	5.5
Inflation (average)	17.5	14.5	12.9	10.8	11.2
Government balance/GDP	2.0	-0.3	-3.3	-4.7	-4.0
Current account balance/GDP	-6.8	-5.6	-5.0	-7.0	-3.3
Net FDI/GDP [neg. sign = inflows]	-1.2	-3.9	-2.9	-3.0	-1.3
External debt/GDP	32.5	40.5	56.0	57.7	n.a.
Gross reserves/GDP	51.5	48.7	58.3	50.8	n.a.
Credit to private sector/GDP	22.8	29.0	35.7	35.8	n.a.

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Macroeconomic developments and policy response

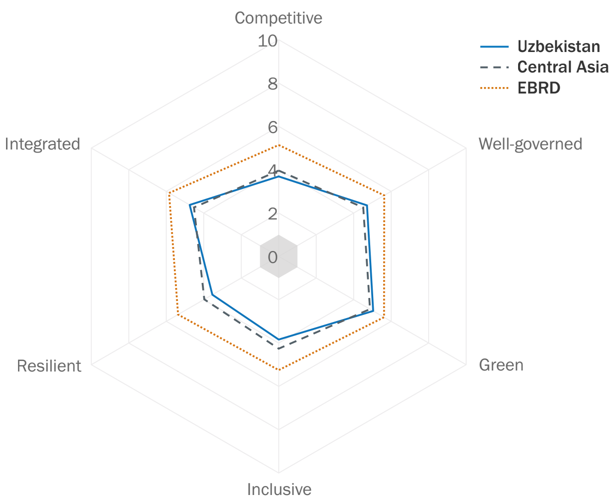
Strong economic growth is continuing in 2022. The economy grew by 5.8 per cent year on year in the first three quarters of 2022, supported by a boost in fixed capital investment (up 5.0 per cent year on year). From January to September 2022 growth was broad-based, with particularly strong gains in construction (up 6.3 per cent year on year), retail trade turnover (up 10.8 per cent year on year) and services (up 15.4 per cent year on year). On 10 March 2022 the Cotton Campaign ended its call for a global boycott of Uzbek cotton, thus creating an opportunity to expand cotton and textile investment and exports. In the first nine months of 2022 exports of goods and services grew by 35.7 per cent year on year, driven by a more than doubling of gold exports (reaching 21.1 per cent of total exports). Imports rose by 22.3 per cent year on year in the same period.

Inflation has reached double-digits, prompting policy rate adjustments. The inflation rate was 12.23 per cent year on year in September 2022. The war on Ukraine initially led to a depreciation of Uzbekistan's national currency, the Uzbek som, in late February and early March 2022. To stabilise the foreign exchange market and limit the pass-through effect on prices, the Central Bank of Uzbekistan raised the policy rate by 300 basis points to 17 per cent in March 2022. Timely actions of the regulator helped the Uzbekistan som to regain its pre-war value. Subsequently, the central bank decreased its policy rate to 16 per cent in June, and further to 15 per cent in July. Foreign currency-denominated loans account for 47.5 per cent of total loans. Non-performing loans have continued to decline, reaching 4.7 per cent of total loans by September 2022 compared with 5.8 per cent a year previously.

The fiscal position is strengthening. The state debt-to-GDP ratio has been declining since the first quarter of 2021. As of 1 April 2022 external public debt amounted to US$ 23.4 billion, and accounted for 32.9 per cent of GDP (down from 38.6 per cent in 2021). Concurrently, high international reserves (US$ 33.4 billion as of 1 October 2022) ensure adequate fiscal buffers. Remittances have increased dramatically during 2022, rising by 96 per cent year on year in the first half of the year.

Robust growth will continue in the short term. The economy is forecast to grow at 5.5 per cent in 2022, and 6.5 per cent in 2023. Uzbekistan's growth continues to rely on its large and industrious labour force, domestic market size, strong and diversified manufacturing capacity, and market-oriented reforms. However, a further deterioration of the Russian economy in 2023 presents a significant downside risk to the outlook.

CHART Assessment of transition qualities (1-10)



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Structural reform developments

Plans for privatisation are advancing but in an uncertain environment. In March 2022 the president signed a Decree "On additional measures to further reduce state participation in the economy and accelerate privatisation", which sets out a privatisation timeline for some SOEs, including Uzbekistan Airways and the national oil and gas company, and initial IPOs for the state-owned banks. However, international sanctions on Russia may hinder this ambitious privatisation agenda, as prospective Russian investors may face sanctions.

Capital market development is ongoing. In January 2022 a 10-year government bond was issued at the Uzbek Republican Currency Exchange auction. In line with the government's agenda of attracting new market participants, individuals and non-residents were allowed to purchase government bonds in February 2022. Furthermore, the first inflation-linked government bond was issued in July 2022, a further step towards diversifying the capital market.

A new development strategy is in place. This Development Strategy for the New Uzbekistan 2022-26 reflects the authorities' stated commitment to strengthening the reform agenda. Centred around seven pillars, the strategy includes establishing a free civil society, strengthening the rule of law, economic development and rapid growth, fair public policies and human capital development, safeguarding national interests, and strengthening security and defence alongside an active foreign policy. In addition, the government set national sustainable development goals up to 2030. The ambitious roadmap envisages: a halving of the poverty rate; sustainable agricultural development to strengthen food security; streamlining existing support mechanisms; a one-third reduction in maternal mortality; rooting out violence against women and children; integrating gender equality principles; increasing water efficiency; achieving full access to reliable and affordable energy; and a 160 per cent increase in per-capita GDP.

The investment environment is improving. The Investment Programme for 2022-26 introduces a central project management office to coordinate strategic investment projects. The Direct Investment Fund will now be able to own up to 49 per cent of the authorised capital of holding companies. In June 2022 the authorities introduced additional measures to improve the management of special economic zones and reduce the time required for decision-making by eliminating the requirement that business plans and feasibility studies for investment projects be pre-assessed by the Centre for the Comprehensive Expertise of Projects and Import Contracts.

Significant progress has been made on the digitalisation agenda. The "Digital Uzbekistan-2030" strategy (introduced in 2020) envisages connecting every settlement to the internet and upgrading digital skills, among other goals. More than 280 projects will facilitate the digital transformation of regions and sectors, aiming to double the share of digital services in GDP in the next two years. As part of the strategy, three new data centres will be launched in Tashkent, Bukhara and Kokand. About US$ 2.5 billion will be invested in digital infrastructure in 2021-22. The strategy also strives for a gradual digitalisation of the banking sector, allowing for wider access to remote banking services by the population at large. Within the framework of the Million Programmers project, more than 100 information technology (IT) schools were organised, and more than 500,000 young people have taken programming courses. To benefit from the inflow of digital nomads, Uzbekistan's IT Park has recently introduced a new mechanism (IT-Visa) to assist in the relocation of IT businesses and programmers. In addition to assistance with registration, IT businesses are offered a tax-and-customs-free regime, and licence-free employment of foreign persons.

The country is progressing on its green agenda. Uzbekistan ratified the Paris Agreement and submitted its first Nationally Determined Contribution (NDC) in 2018. A more ambitious NDC, submitted in 2021, seeks to achieve a 35 per cent reduction in specific greenhouse gas emissions per unit of GDP by 2030 (compared with the 2010 level). Uzbekistan has already committed to a net-zero target for its power sector by 2050 and is in the process of developing an economy-wide long-term strategy. Currently, Uzbekistan has set an ambitious renewable energy target, including 7 GW of solar photovoltaic and 5 GW of wind power by 2030. Moreover, the country joined the Global Methane Pledge in May 2022, intending to reduce global methane emissions by at least 30 per cent by 2030 compared with the 2020 levels. In 2019 the president of Uzbekistan approved the Strategy on the Transition to a Green Economy for 2019-30 aiming to improve energy efficiency, rationalise consumption and conservation of natural resources, reduce greenhouse gas emissions, provide access to green energy, create jobs and ensure resilience to climate change. With its approval pending in 2022, Uzbekistan's Green Growth Strategic Framework provides the operational plan for green transformation across the entire economy.