

# THE WORLD ECONOMIC CRISIS AND ITS IMPACT ON THE ECONOMIC DEVELOPMENT OF THE CENTRAL ASIAN COUNTRIES

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In the Central Asian (CA) countries, the world crisis has mainly had an impact on the financial and investment sphere. The region does not have enough of its own economic resources to overcome the consequences, so it will have to turn for the most part to influential neighbors.

The nature and manifestations of crisis phenomena depend on the level of development and integration of the economic systems of different states into the world economy.

Let's take a look at the situation that has developed in the CA countries under the influence of the world financial crisis, as well as at the possible ways to overcome it and the prospects for the region's further development.

Since the crisis began, there has been a significant drop in the growth rates of the macroeconomic indices in **Kazakhstan's** economy. The 2008 year-end results were not encouraging—the financial and economic spheres had obviously experienced a slump.

By the end of 2008, however, the powers that be had managed to halt the decline in financial indices. But it was the lower investment activity and difficult financial situation in the banking sector in 2007 that led to the economic crisis. This is confirmed by the data of Kazakhstan's Statistics Agency.<sup>1</sup>

The GDP index for 2008 amounted to 103.2% compared to the previous year. Goods production accounted for 45% and services for 52.5%. The total production volume decreased by 2.2% (3,045.9 billion tenge) from January to June 2009 compared to the same period in 2008, giving rise to a corresponding change in the aforementioned indices—36.3% (goods) and 65.8% (services).<sup>2</sup>

The production branches—oil and mining—suffered the most from the crisis. The drop in growth rates in these branches corresponds to the downward trends in economies throughout the world. This reduction in production volume led to a change in the sectoral and geographic structures of the country's industry.

**Box 1. Crude oil production increased in the Atyrau (by 20.6%) and Mangistau (by 2.0%) regions. In the Aktobe and Kzyl-Orda regions, it dropped by 2.6% and 3.7%, respectively. Gas condensate production increased in the Mangistau region 1.6-fold,**

<sup>1</sup> Data of the Kazakhstan Statistics Agency, available at [<http://www.stat.kz/news/Pages/>].

<sup>2</sup> Data of the Kazakhstan Statistics Agency, available at [[http://www.stat.kz/news/Pages/n\\_15\\_07\\_2009\\_3.aspx](http://www.stat.kz/news/Pages/n_15_07_2009_3.aspx)].

*and in the West Kazakhstan region by 0.2%. In the Kostanai region, iron nugget production dropped by 18.9%. Copper ore production rose in the East Kazakhstan (by 68.1%) and Aktobe (by 14.3%) regions, while in the Karaganda region its production dropped by 0.8%. Steel manufacture rose in the Pavlodar (by 24.2%) and Kostanai (by 23.1%) regions, while in the East Kazakhstan and Karaganda regions, steel production dropped by 7.3% and 16.5%, respectively. The production of unwrought zinc increased in the Karaganda region by 5.1% and by 1.6% in the East Kazakhstan region. Refined copper production decreased in Almaty by 16.4% and in the Karaganda region by 0.9%. The greatest increase in energy production volumes was noted in the Zhambyl (by 40.5%), North Kazakhstan (by 20.0%), Almaty (by 11.9%), and Mangistau (by 11.1%) regions, as well as in Astana by 8.2%. The greatest decrease occurred in the Akmolinsk region (by 23.2%). The greatest increase in butter production was seen in the Zhambyl (by 3.9%) and Kostanai (by 1.2%) regions. At the same time, the largest drop in butter production was seen in the East Kazakhstan (by 28.8%) region and Almaty (by 24.9%). An increase in refined sunflower oil production was seen in the East Kazakhstan (by 29.2%) and Aktobe (by 1.2%) regions. A drop in refined sunflower oil production was noted in the South Kazakhstan (by 49.4%) region and in Almaty (by 39.9%). The production of fruit and vegetable juice increased in the Kostanai (by 13.8%) and South Kazakhstan (by 13.3%) regions. A drop in its production was seen in the Almaty region (by 71.6%) and in Almaty (by 23.9%).*

*(Data of the Kazakhstan Statistics Agency)*

The year 2008 was marked by a sharp decrease in Kazakhstan's oil export revenues. The drop in world oil prices in 2009 prompted a decrease in oil production of 3 million tons, contrary to the government's official forecast (77 million tons).<sup>3</sup> In addition, the Ministry of Economics is expecting a drop in production volume (of approximately 1%) in the metallurgical industry.

However in the first half of 2009, particularly in June, industrial production indices grew (see Figure 1); compared with May 2009, accelerated growth rates were seen in the mining (6.3%) and processing industries (9.9%). Crude oil and metallic ore production and the output of the machine-building, metallurgical, and food industries, including beverages and tobacco, increased.

The economic crisis in Kazakhstan is having a negative impact on the rise in the price index. By the end of 2008, prices reached an all-time high at every level. For instance, the consumer price index in December 2008 compared to December 2007 amounted to 109.5%. Food prices grew by 10.8%, non-food prices by 5.7%, and the cost of services by 11.4%. The prices for industrial products put out by manufacturing enterprises dropped by 18.6% in December 2008 compared to December 2007.<sup>4</sup>

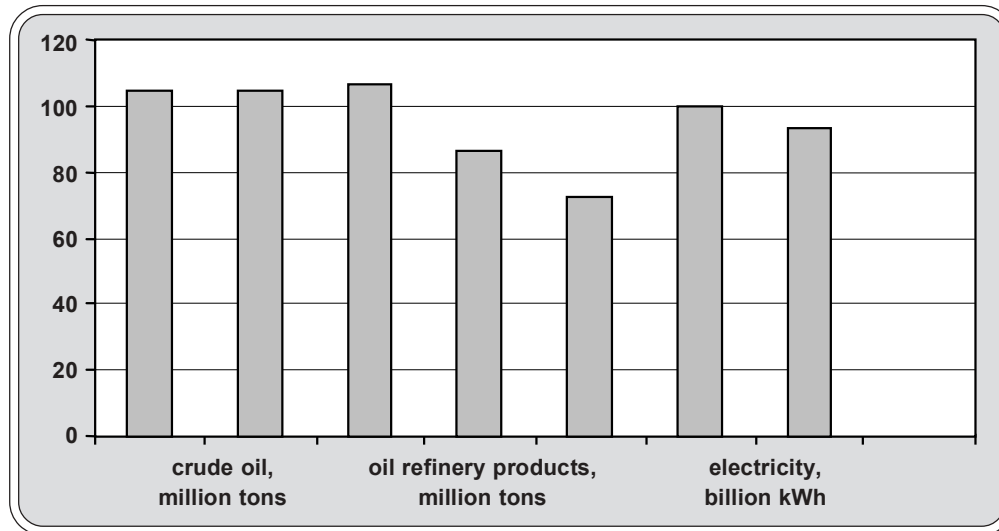
The situation improved slightly in the first half of 2009. In June 2009, the consumer price index amounted to 103.9% compared to December 2008. Food prices grew by 3.5%, non-food prices by 4.9%, and the cost of services by 3.3%. In June 2009, industrial product prices increased by 9.7% compared to December 2008.

<sup>3</sup> According to the data of the State Statistics Agency, in 2008, 58,713,800 tons of crude oil and 12,024,100 tons of gas condensate were produced in Kazakhstan. This is 6.2% and 1.4% more, respectively, than in 2007. At a price of 40 dollars a barrel, it stands to reason that some fields can permit themselves a cutback due to a drop in profitability, available at [<http://regnum.ru/news/1112677.html>].

<sup>4</sup> [[http://www.stat.kz/news/Pages/n\\_17\\_03\\_09.aspx](http://www.stat.kz/news/Pages/n_17_03_09.aspx)].

Figure 1

**Indices of the Physical Volume of Industrial Production  
in Kazakhstan Compared  
to the Corresponding Period of the Previous Year  
(January-June 2009)**



During July 2009, food prices have increased by 0.2%, non-food prices by 0.6%, and the cost of services by 0.4%. But, according to many analysts, the decline in price growth rates was caused by the overall situation in the world, as well as the tight pricing policy conducted; this process will soon come to a halt.

The crisis has resulted in a significant drop in investment activity, both beyond the country and within it. The Kazakhstan government is resolving this problem by mobilizing large amounts of investment capital.

For instance, the Samruk-Kazyna Kazakhstan National Welfare Foundation is planning to attract additional funds (around 4 billion dollars) by floating the bonds of pension savings funds (PSF). There are plans to place the first tranche in March 2009 under the control of the government financial supervision agency (FSA). The average maturity of the bonds will be 15 years with a return on investment of 8.4% per annum, that is, "at the level of average return on investment of pension funds as of today."

The Kazakhstani government's anti-crisis program approved at the end of November 2008 presumes using the resources of the National Fund, budget, and pension funds. According to the FSA, pension savings accumulated in pension savings funds as of 1 November, 2008 amounted to one trillion 343.7 billion tenge (more than 11 billion dollars). At the end of 2008, 14 pension savings funds were functioning in the republic.

A decision was made to compensate for the shortage of financial resources by means of external acquisitions. Vneshekonombank of Russia will allot the Kazakhstan National Welfare Foundation up to 3 billion dollars for implementing several major projects.

In 2009, the government, along with business structures and foreign investors, began financing social projects; this step stabilized the situation in the financial market somewhat. According to the

results of the first half of 2009, the volume of investments in basic capital amounted to 1,794.1 billion tenge, which is 7.3% more than for the same period last year.

By the end of 2008, the economic and financial crisis in Kazakhstan had had such a strong impact on the national economy that it spread beyond the country's borders and affected its integration initiatives. In an attempt to resolve the domestic problems, the president of Kazakhstan came forward with an initiative to create a single world currency.<sup>5</sup>

Such worldwide integration initiatives do not provide real opportunities to use regional resources—currency integration is impossible even at the bilateral level.

In February 2009, the National Bank of Kazakhstan devaluated the local currency by 25%—to 150 tenge to the dollar against 120 tenge. The forecast of the Ministry of Economics and Budget Planning envisages further devaluation of the tenge—by 10% over an extended period.

Currency integration is only possible if there is a full-fledged common market of goods, capital, and labor, whereas Kazakhstan has still not reached that level. So its initiatives in this area can only be used piecewise.

The 2008 year-end results are characterized by a drop in economic growth rates in the **Kyrgyz Republic**, although this drop was alleviated by an increase in GDP in the first six months. Real growth amounted to 7.6% or, not counting the enterprises engaged in developing the Kumtor field, to 5.4%. The per capita volume of GDP amounted to 35,100 soms (959 dollars) and increased by 6.8%.

In addition, the growing negative trade balance predetermined a deterioration in the indices of the balance of payments. According to the 2008 year-end results, Kyrgyzstan's negative trade balance amounted to 2 billion 416 million dollars.<sup>6</sup>

During 2008, industry manufactured products totaling 85.9 billion soms. In so doing, the growth rates compared to 2007 amounted to 114.9% or, not counting the Kumtor enterprises, to 97.9%. This situation arose for the following reasons.

First, the decrease in external demand for construction materials due to the world crisis had a negative impact on the development of industry. This resulted in a significant decrease in the growth rates of rubber and plastic goods production (78.3%) and the manufacture of other non-metal mineral products (88.2%) between January and December 2008.

As a result of the energy crisis due to wear and tear on the industry's fixed assets and the low level of water in the Toktogul reservoir, the growth rates in the production and distribution of electricity slowed down.

In particular, growth rates in the food industry enterprises slowed and amounted to only 101.1% in 2008 (105.2% in 2007). The same situation developed in the sewing industry. Whereas in 2007, the growth rates in this branch amounted to 145.6%, in 2008 they dropped to 115.7%.<sup>7</sup>

According to the National Statistics Committee, 481.0 million dollars in foreign direct investments were pumped into the economy in 2008 (compared to 324.4 million dollars in 2007).

There has also been a significant increase in the outflow of foreign investments, amounting to 287.6 million dollars (60% of the FDI invested), which is 2.1-fold higher than for the same period

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<sup>5</sup> Kazakhstan President Nursultan Nazarbaev believes that a single world currency should be created. According to the Kazinform Agency, the head of the Kazakhstani state said this at a business forum in Delhi. Whereby the head of Kazakhstan, who has previously made statements in favor of the idea of creating regional currencies, spoke against this initiative this time. According to him, such fragmentation could lead to "great chaos." "I think that the future measure consists in having an entirely fair world currency and not one issuer, as we have just now. This is an undemocratic, un-free, uncompetitive, and uncontrollable world currency. Instead of this, countries should come to terms on creating a world currency unit for exchanging goods that would be adopted by the U.N. and controlled by corresponding commissions, and we would have something to do with this currency," said Nursultan Nazarbaev, available at [[http:// www.regnum.ru/news/1115303.html](http://www.regnum.ru/news/1115303.html)].

<sup>6</sup> The 24.kg IA presents these data with reference to the Kyrgyzstan National Statistics Board.

<sup>7</sup> [<http://www.24.kg/economics/2009/25/01/107969.html>].

in 2007. This is explained by the consequences of the financial crisis. During 2008, when there was an acute shortage of funds, active attempts were made to raise the level of the country's investment appeal.<sup>8</sup>

These efforts resulted in a rise in Kyrgyzstan's rating. According to a report by the World Bank, it not only climbed up from 99th to 68th place in the 2009 rating, but was also included among the three countries considered to be advanced reformers. Measures will be carried out to implement the second stage of the Reforms for Business 2009 project, which will make it possible for the republic to raise its ranking even higher.

Kyrgyzstan occupies 7th place in the Free Trade category, 11th place in Investor Protection, 94th in Personal Freedom, and 115th and 117th in Innovations and Technology, respectively. In terms of corruption level, Kyrgyzstan ranks 123rd, with respect to bureaucracy 33rd, in the Tax Environment category it holds 107th place, and in Price Liberation 93rd. *Forbes* describes Kyrgyzstan as a poor mountainous country with a predominantly agricultural economy.<sup>9</sup>

The tight monetary and fiscal policy conducted in Kyrgyzstan kept the inflation rate below 20.0% from January to December 2008.<sup>10</sup> The high inflation rates were caused by the increase in food prices during the second half of the year and the rise in prices for energy resources in the world markets during the first half.

Three factors had an impact on the slowdown in inflation rate—the drop in prices for agricultural products, the policy conducted by the government and National Bank, and the relative stability of the world economy at that time. In July, prices rose very slightly, and in August there was even negative growth.

Kyrgyzstan's financial system is quite stable due to the low level of integration of the country's banking structures into the world financial market. In so doing, it should be noted in particular that the negative impact of the crisis was manifested in a significant reduction in investment funds, since the main sponsors have external financing sources.

Kyrgyzstan's external debt, according to the Ministry of Finance, amounted to 2,076,850 million dollars at the end of December 2007, and 2,127,885 million dollars as of 31 December, 2008. So over the year, the state's external debt rose by 51 million dollars. Over the past four months, the debt has increased by 12 million dollars—in August 2008, it was equal to 2,115,906 million dollars. In December 2008, the Ministry of Finance spent 200 million soms (5 million dollars) to cover the external debt.<sup>11</sup>

Kyrgyzstan lags behind the CIS countries in terms of investment growth rates in basic capital—the decrease in amount of deposits amounted to 5.4%.<sup>12</sup>

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<sup>8</sup> Within the framework of the New Economic Policy defined by the Kyrgyzstan president on 10 January, 2008, a Plan of Action for the country's government has been drawn up and approved for 2008, and a draft of its development strategy prepared (2009-2011). With the assistance of the Ministry of Economic Development, strategies and programs of socio-economic development of the regions for 2008-2011 have been prepared and approved in compliance with the new methodology and in keeping with the objectives and assignments envisaged in the draft of the development strategy renewed until 2011. In addition, the conception of a state regional policy has been drawn up that envisages accelerated development of the regions.

<sup>9</sup> Ratings are compiled taking into account such parameters as human rights, democratic elections, freedom of speech, protection of minority shareholders, freedom of trade, low inflation, low profits tax, investment volume, and stock exchange indices. The top from *Forbes* is based on the assessments of the World Bank, Transparency International, World Economic Forum, Freedom House, the American Chamber of Commerce, the CIA, and several other organizations, available at [<http://www.24.kg/economics/2009/03/20/109765.html>].

<sup>10</sup> The precise consumer price index for the year-end results of 2008 amounted to 20.1%.

<sup>11</sup> [[http://www.madein.kg/ru/Finances/item1245\\_21012009](http://www.madein.kg/ru/Finances/item1245_21012009)].

<sup>12</sup> According to the CIS Statistics Committee, in 2008, the amount of investments in basic capital increased by 10% on average throughout the CIS compared to 2007. In some countries, a decrease in rates of 11% was noted. This is shown by the data of the Commonwealth's Interstate Statistics Committee. In the Commonwealth's other countries, the dynamics

In 2008, the inflow of direct investments into the country amounted to 580 million dollars. According to the 2008 year-end results, it rose in the World Bank's Doing Business rating to 68th place. The number of audits of economic entities in the republic has decreased by 28% and efforts are continuing to cut back on the licensing procedures. The volume of deposits in the country's banks has increased by 26%, while the inflow of loans into the country's economy rose by 20%.

The year 2008 saw a profound energy crisis, which was expressed in regular rolling black-outs for the population and corporations. But the government's main efforts were directed toward generating thermal energy, thanks to which there were no emergencies in the 2008-2009 cold season.

Migrants from Kyrgyzstan who work in Russia sent more than 870 million dollars home in 2008, which is almost twice as much as in 2007. According to the 2008 year-end results, the total amount of money transfers by labor migrants to Kyrgyzstan reached 1.2 billion dollars.

Kyrgyzstan has been focusing significant attention on economic security issues. In so doing, it also examined the financial and investment spheres, but in the context of the high inflation level particular attention was given to resolving food problems.

The official agencies have been reporting on the level of security reached for quite some time now. But the agrarian reforms of the 1990s basically resulted in a crisis in agriculture—local manufacturers could not compete with foreign companies and the rise in inflation essentially destroyed the domestic producers. All of this had a negative effect on the state of the agrarian sector.

This is mentioned in the draft of the republic's food safety conception for 2009-2013 drawn up by the Institute of Economics of the Kyrgyzstan National Academy of Sciences.<sup>13</sup>

The country's financial security is also threatened. According to the CIS Statistics Committee, a large part of investments came from foreign sources (30.6%).<sup>14</sup>

So the world financial crisis has aggravated the situation in the republic, but, on the other hand, it has also had a certain positive impact on the national economy.

*Positive effects of the crisis:*

- First, acute drop in outlays. All commodities that have an artificially high cost will drop in price (rent, real estate, logistics). Many medium-sized companies could become more efficient.
- Second, structural shifts in the economy. Inefficient and uncompetitive enterprises will go bankrupt, and the released resources can be used for other production units.
- Third, restoration and strengthening of sociopolitical stability; keeping macroeconomic sustainability under control, despite the galloping inflation and impact of the world crisis on the economy.
- Fourth, overcoming energy difficulties.
- Fifth, a drop in the total external debt as a percentage of GDP (from 80% to 46%) thanks to a correct strategy.

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are positive. Tajikistan is the leader in terms of an increase in investments in basic capital for the second year running. This is associated with the construction of hydropower facilities. In addition to Tajikistan, the other members of the top three—some are Azerbaijan (34.3%) and Uzbekistan (22.4%). Among the outsiders, apart from Kyrgyzstan, are Armenia (growth at a level of 1.7%), Kazakhstan (4.6%), and Ukraine (4.7%) (see: [<http://www.cis/2009/02/12/106105.html>]).

<sup>13</sup> [<http://www.24.kg/economics/2009/03/20/109731.html>].

<sup>14</sup> According to this index, Kyrgyzstan ranks second in the Commonwealth after Tajikistan, where the percentage of foreign investments in the total amount of investments topped 70%. 28.8% of the investments in Kyrgyzstan were attracted in the form of household funds, 25.3% by means of enterprises' and organizations' own funds, and 11.5% in the form of budget investments.

*Negative effects of the crisis:*

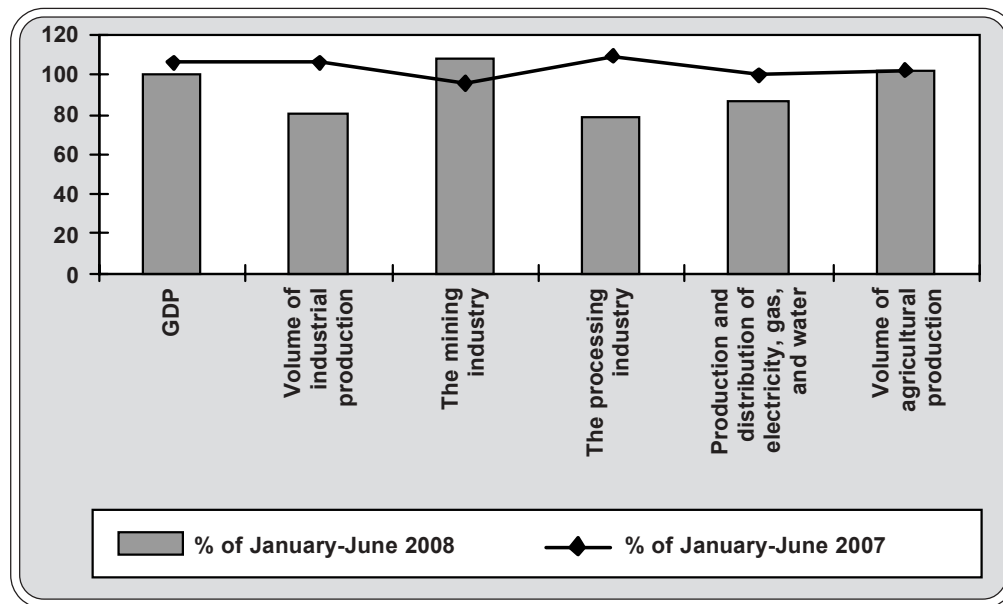
- Steady rise in production outlays and increase in prices for agricultural produce associated with the low demand for it and domestic manufacturers being pushed out by foreign companies.
- Abrupt decrease in funds allotted to agriculture from the state budget.
- Unsophisticated system for selling agricultural products, in which primary income is redistributed in favor of intermediaries.
- Absence of stable prices.
- Underdeveloped infrastructure of wholesale trade.
- Unequal competitive conditions with imported products.

In addition, a tight monetary policy, reform of the tax system, and the set of measures for activating state regulation of the economy in crisis conditions have yielded certain positive results. This is shown by the macroeconomic indices for the first six months of 2009. The volume of GDP in Kyrgyzstan for January-June 2009 amounted to 74,049 million soms, while the growth rates compared to the same period in 2008 reached 100.3% and 106.1%, respectively.<sup>15</sup>

Compared to 2007 (not counting the enterprises developing the Kumtor field), this index for the same period in 2008 was equal to 71,177.4 million soms, and the growth rates amounted to 101.3%. This was caused by a drop in demand for gold in the world markets and the delay in implementing the conditions of a contract with Canada's Centerra Company on field development.

Figure 2

**Indices of Production Volumes**  
(first six months of 2009)



<sup>15</sup> Data of the Kyrgyzstan National Statistics Committee. Express information of 7 July, 2009, available at [<http://stat.kg/>].



The past period of this year was characterized by the negative impact of the world financial crisis on the main industrial branches; only four of them have positive physical volume indices: production of fuel and energy minerals (109.3%), production of other mineral resources (111.7%), manufacture of coke, petroleum products, and nuclear materials (3.8-fold), and manufacture of leather and leather goods (2.5-fold).

The percentage of industries that have not reached the corresponding physical volume index according to the results of the first quarter of 2009 amounted to 95.6%, and of the most backward to 95%.

The decrease in indices (not counting the Kumtor field) is associated with the worsened situation in the key branches of the economy: food production (94.7%), textile and sewing industry (57.8%), manufacture of building materials (36.7%), metallurgy and the production of metal goods (78.7%), and electricity production (84.8%). Their share amounted to 88.5%.

All the same, since March 2009, industry has been experiencing positive dynamics. The enterprises that came to a standstill due to the crisis have begun operating again, their numbers reaching 43.<sup>16</sup>

For instance, the Kant cement, the Kadamjai antimony, and the Khaidarkan mercury combines have resumed operation. However, due to the routine repairs being carried out, the Interglas factory in Tokmak for the manufacture of sheet glass is still standing idle. Special control is being maintained over the situation at the Mayлуу-Suuy electric lamp factory by the Kyrgyz Ministry of the Energy Industry. This factory is operating and putting out products, but the former owners left a multi-million debt.

In June, the consequences of the slump had still not been overcome. In the first half of 2009, the volume of industrial production dropped by 20%. A problematic situation has developed in the manufacture of building materials, due to which Kazakhstan has refused to purchase these products.

The consequences of the financial crisis are still having an impact on Kyrgyzstan's economic development. The drop in demand for the country's products from neighboring countries and the decrease in revenue transferred by labor migrants could lead to a deterioration in the stability of the balance of payments, which will have an effect on the som exchange rate.

In June, the National Bank of Kyrgyzstan continued conducting a policy aimed at preventing abrupt fluctuations in the exchange rate of the national currency, thanks to which stability is being retained.

According to the results of 2008, **Tajikistan** became part of a separate sub-group of the IMF known as "a low-income CIS country."

The real growth of the GDP in Tajikistan in 2008 amounted to 4.1%, while in 2009 IMF experts forecast an increase in this index to 7.0%.<sup>17</sup>

In the first half of 2009, Tajikistan's economy, as economies throughout the world, has been developing in a state of crisis. Tajikistan's economic growth is still at a rather low level—the increase in GDP for the first six months amounted to 2.8%, the gross agricultural product increased by almost 15%, and the domestic consumer demand for goods by 14%. In the first six months, compared to 2008, the GDP level rose by 5.8%.<sup>18</sup>

Due to the dynamic development in the service sphere, Tajikistan managed to keep up the GDP growth despite the significant drop in production, which amounted to 13.3% in January-June of this year (to 2 billion 558.9 million somoni). For the same period in 2008, this index was equal to 3.9%. The drop in manufacture of industrial goods is associated with the cutback in production of primary aluminum, which constitutes the basis of Tajikistan's export. Production in the fuel and energy industry compared to the same period last year decreased by 7% (365.9 million somoni). According to the Statistics Committee, Tajikistan was the only country in the CIS where such a drop in industrial production was registered.

<sup>16</sup> [<http://www.24.kg/economics/2009/07/10/116023.html>].

<sup>17</sup> Earlier, the IMF forecast an 8% increase for the country in 2008.

<sup>18</sup> Data of the Tajikistan State Statistics Committee, available at [<http://www.state.tj>].



There is high social tension in the republic due to galloping inflation and the decrease in household incomes; money transfers from labor migrants have decreased.

There is an unfavorable business atmosphere in the republic, which is making investors less active. Tajikistan occupies 159th place out of 181 in the annual business freedom index of the World Bank. Enterprises are established with great difficulty in the republic, and the mechanisms for obtaining loans and managing international trade are not very effective.

The drop in prices for cotton and other exported agricultural crops has led to a decrease in foreign exchange receipts.<sup>19</sup> In this situation, one of the priority vectors should be diversification of the agricultural sector.

At the end of 2008, the sharp rise in the dollar exchange rate with respect to the national currency (from 3.41 to 3.47 somoni to the dollar) led to an increase in inflation.<sup>20</sup> In January-June 2009, inflation rose by 2.8%, while for the same period of last year its increase amounted to 8.3%, which essentially brings up the low economic growth rates.

In January-June of this year, food prices grew by 2.1%, non-food prices by 2/4%, while the cost of services increased by 7.3%.

In so doing, according to experts, by the end of 2008 Tajik banks essentially had no foreign currency due a significant decrease in the transfers from abroad (including from labor migrants). In addition, the drop in prices and decrease in demand for Tajikistan's main export commodities—aluminum and cotton—played a negative role.

The direct consequence of the financial crisis was the cutback in revenues in 2008 from migrants and their return home. By the end of the year, this process had accelerated and in the first half of 2009 it speeded up even more. For example, 109 Tajik labor migrants were deported from Kazakhstan in 2008.

A dramatic slump is expected in the private sector due to the decrease in monetary transfers sent by migrant workers, and the consequences of this will be felt in the near future.

In the meantime, however, there may be some slight recovery, but this will be followed by an abrupt nose dive. Since the country is an oil importer, it will benefit in the near future from the dramatic drop in prices for energy resources. The same goes for the import of fertilizers and foodstuffs. The drop in prices will help to curb the burgeoning inflation.

This economizing will make it possible to buy raw materials (for example, for the aluminum plant in Tursunzade), but the effect will not be that significant since the prices for the goods produced, including aluminum and cotton (the main articles of the republic's export), are correspondingly dropping.

There is a real danger associated with money transfers. According to different sources, almost 1.5 million residents of Tajikistan's six-million population currently live and work outside the country, mainly in Russia and Kazakhstan. According to the statistics of the World Bank for 2008, migrant workers transferred 1.25 billion dollars home. According to unofficial data, this figure is much higher and could constitute up to 60% of the country's GDP. This makes the question of whether or not the workers living abroad can survive the world economic crisis rather important.

One of the main negative factors influencing the republic's economy is the drop in demand and decrease in world prices for the republic's main export goods—aluminum and cotton fiber. The cutback in trade operations has resulted in a noticeable drop in currency transfers and deterioration in the operation of these branches—during the first half of 2009, the drop in industrial production amounted to 13%.

In the first half of 2009, Tajikistan's foreign trade turnover shrank by 30.6% compared to the same period last year and amounted to 1 billion 615.8 million dollars, including electricity and natural gas, which is 30.6% (713 million dollars) less than the previous index.

<sup>19</sup> Although the country is still mainly oriented toward growing cotton plant, this sector has been experiencing significant losses since the collapse of the Soviet Union in 1991. Between 2003 and 2007, when the prices in the world goods markets dropped, the percentage of cotton plant growing in the volume of the GDP decreased from 9 to 2%.

<sup>20</sup> On the National Bank's website, one dollar is equal to 3.4190 somoni.

A trade deficit (793 dollars) has developed, in particular, the deficit with the CIS countries amounted to 576.3 million dollars, and with the countries of the Far Abroad to 216.7 million dollars.

The volume of goods export for the period under report amounted to 411.4 million dollars, which is 380.4 million dollars (48%) less than for the same period of the previous year. The import of goods into the republic amounted to 1 billion 204.4 million dollars, which is 332.7 million dollars (21.6%) less than the January-June 2008 index for 2008. Compared to the previous month, export in June decreased by 3.2% and import by 9.9%.<sup>21</sup>

The situation in Tajikistan's hydropower sector is still complicated. It is associated not only with the insufficient volumes of electricity production, but also with the disagreements (with Uzbekistan) about building the Rogun GES.

Due to Tajikistan's debts (around 9 million dollars), Uzbekistan has cut back gas deliveries to the republic by 50%. At present, the country is receiving around 800,000 cu m of gas a day instead of the 1.65 million cu m that used to be delivered. The consumers' debt to Tajikistan's gas distributing company is around 18.7 million dollars, 10 million of which is owed by the population of the Tajik capital. As a result, the delivery of blue fuel to the TajikAzot and Tajiktsement enterprises has been completely halted.

Uzbekistan is the only exporter of natural gas to Tajikistan, which is unable to meet its needs by means of its own production, and the price of gas is set annually on the initiative of the Uzbek side.<sup>22</sup>

In 2008, **Uzbekistan** maintained a stable position in the conditions of the international loan crisis and economic slump in the developed countries. The GDP growth rates in the republic amounted to 9%, there is a stable net surplus in foreign financial transactions and the budget, currency reserves continue to increase, and stability is being maintained in the banking system.

The increase in inflation has been curbed, although its rates are still high. Consistent execution of a rather tight monetary policy has made it possible to keep this process within the limits envisaged by the forecasts at a level of 7.8% per annum.<sup>23</sup>

The growth rates in industry amounted to 112.7%; including to 117.7% in the production of consumer goods and to 21.3% in the service sphere.

Other important branches of the economy have also been developing at stable rates: construction has increased by 8.3%, transport shipments by 10.2%, and the trade sphere by 7.2%. In agriculture, the growth rates amounted to 104.5%; 3,410,000 tons of raw cotton have been prepared and 6,330,000 tons of grain have been produced, including 6,145,000 tons of wheat.

The state budget has exceeded the target—instead of the projected deficit, it recorded a surplus of 1.5% of GDP. Such are the data for the end of 2008.

In the first half of 2009, the indicated trends continued. According to the official data,<sup>24</sup> despite the world financial economic crisis, the socioeconomic policy pursued and the timely anti-crisis measures carried out ensured the stable, balanced, and sustainable development of the economy.

According to official statistics, in the first half of 2009, the increase in Uzbekistan's GDP amounted to 8.2%. The increase in industrial production reached 9.1%, in consumer goods 13.1%, in agriculture 4.6%, in services 18.5%, and in construction work 32.5%.

The state budget was executed with a net surplus of 0.3% of GDP, while the inflation level did not exceed the forecast indices. Real household incomes during the first half of the year grew by 25.9%.

<sup>21</sup> Data of the Tajikistan State Statistics Committee, available at [<http://www.state.tj>].

<sup>22</sup> The Uztransgaz Company informed the Tajik side that the price of the blue fuel to be delivered in 2009 would more than double—to 300 dollars per thousand cubic meters of fuel. This price did not suit Tajikgaz. Its representatives say that in the context of the global economic crisis the price of energy resources is dropping in the world markets. In 2008, Tajikistan imported gas at 145 dollars per thousand cubic meters from Uzbekistan, which was 1.5-fold higher than the price for 2007.

<sup>23</sup> Data of the official statistics, available at [<http://www.regnum.ru/news/>].

<sup>24</sup> From the speeches of officials, available at [<http://www.gazeta.uz/2009/07/18/gdp/>].

One hundred and forty-one billion soums have been invested in international and nationwide construction and road repair measures; and work totaling 61.1 billion soums has been carried out at meliorating and irrigation facilities.

The increase in amount of capital investments assimilated in the first half of the year amounted to 32.7%; while foreign direct investments grew 2.6-fold. Seventy-one point one percent of the total investments went to production needs.

Despite the worsening situation in the foreign market, the foreign trade turnover increased by 21.4% in 2008, whereby the export of goods and services rose by 28.7%. As a result, the positive balance in the foreign trade balance increased, which is a very important indication of the reliability of the balance of payments and stability of the economy as a whole.

Stable growth trends in the percentage of competitive production and a drop in the percentage of the deliveries of the raw material branches are clearly seen in the export structure. The production of non-raw material goods in 2008 amounted to more than 71%. In so doing, the export of cotton fiber traditional for Uzbekistan decreased from 20% (2003) to 12% (2008).

Last year, important decisions were made to raise the capitalization level of leading banks such as Uzpromstroibank, Asakabank, Pakhtabank, Gallabank, and others. A presidential decree was adopted on increasing the authorized capital of Mikrokreditbank, which is one of the main lending centers for financing small businesses and private entrepreneurs.

The inflow of additional resources resulted in the total capital of the republic's banks increasing compared to 2007 by 40%, and before 2010 this amount is predicted to double.

However, according to the forecasts for 2009, the slump in the world economy due to the drop in prices for exported goods in Uzbekistan's main trade partner countries will have an effect on the economic situation in the republic, and money transfers will also decrease.

But the country's economy is not integrated into the financial markets of the developed countries and is unlikely to be adversely affected.

"With its strong macroeconomic position, Uzbekistan has significant resources for financing a precisely targeted economic policy that will maintain growth. The task is to alleviate the impact of the world crisis on economic growth with the help of a timely and precisely targeted policy along with ensuring financial stability and a decrease in inflation," this is the official viewpoint, which is confirmed by the data of the republic's Statistics Committee.

All the same, crisis phenomena exist in the national economy. They are evidenced by the following parameters: the high level of inflation, the abrupt drop in the soum exchange rate, the growing level of unemployment, the increase in the number of labor migrants, and the low level of household incomes.

Special attention should be given to the fact that Uzbekistan's aggregate external debt as of 1 January, 2009 amounts to 13.3% of GDP and is characterized according to the international ranking system as "less than moderate."

The main economic regulation measures include an expansive fiscal policy, a tight monetary policy, currency restrictions, and restraining a drop in the soum exchange rate. It is also necessary to bolster trust in the banking system by freeing banks from functions that are not characteristic of them and helping them to acquire cash, as well as resolving issues relating to an increase in national revenues and price formation.

So the state of the economy of the region's countries (Kazakhstan, Uzbekistan, Kyrgyzstan, and Tajikistan) is characterized by an extremely unstable domestic political and economic situation: the state budget is being formed with a large deficit; pricing policy is not coordinated with the purchasing power of the population and the vendibility of the market; there is still high inflation and a crisis in the banking sphere; stagnation of the industrial sector of the economy is increasing, and there is a drop in the GDP growth rates.

Manifestations of the crisis in each of the countries depends on the specifics of branch development of the national economic systems and the level of market changes.

For example, Kazakhstan, which is characterized by a high level of development of market institutions, a powerful industrial complex, and a developed banking system, and which has large investment resources, suffered from the financial crisis more than other countries of the region.

The country's developed banking system, which is integrated into the world financial market, made active use of the contemporary forms of mortgage lending and investments in the securities market. As a result, it is currently dealing with serious problems associated with the lack of solvency and mass bankruptcy of borrowers and the depreciation of the capital being floated on the securities market.

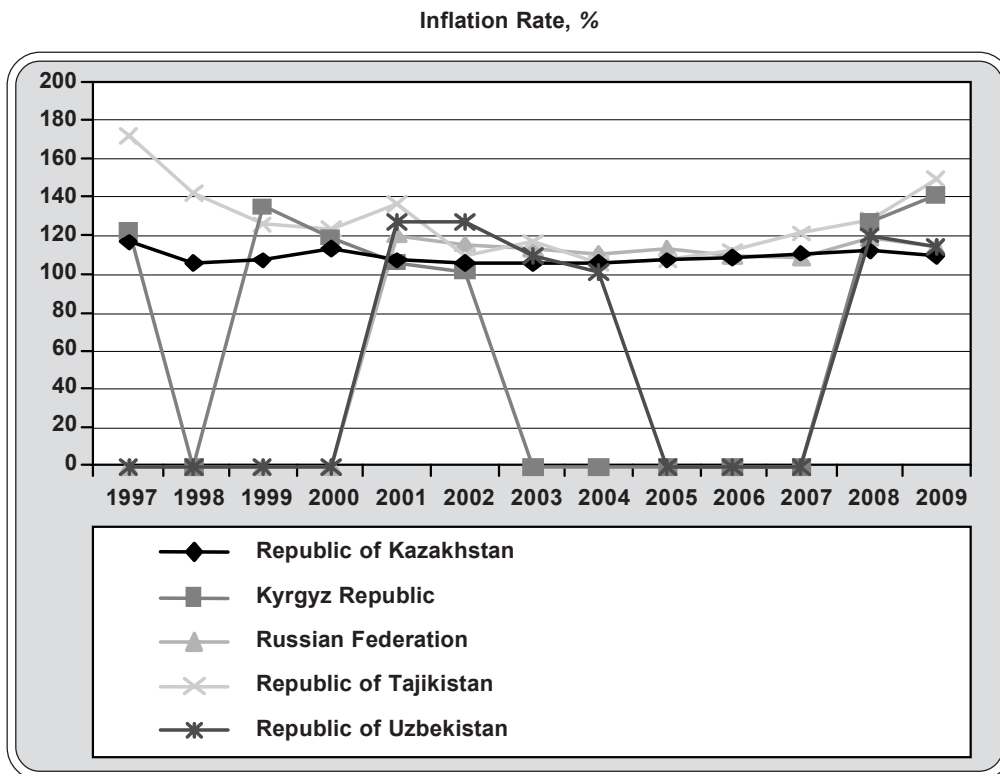
Uzbekistan did not have any particular problems, since the country's economy is the least integrated into the world financial markets ("a closed economy") and has a weak banking system. But this did not save the republic from inflation, a drop in the GDP growth rates, and a decrease in consumer demand.

A profound slump is seen in all branches of the economy in Kyrgyzstan and Tajikistan. These countries have the highest inflation rates—26.6% and 29.8%, respectively, and the lowest GDP growth rate (around 6%). These are the worst indices in terms of the 2008 results in the CIS countries (see Fig. 3), which shows the unsophisticated nature of their national economic systems and national markets.

Kazakhstan is showing the lowest inflation rate, which is approximately at the same level as the Russian Federation. This can be explained by the export resource of fuel and raw minerals. All the same, the republic is unable to help its regional neighbors fight inflation.

It should be noted that the increase in the GDP index shows the gross increase due to inflation and the increase in development rates in the trade and intermediary sectors of the economy. The industry of these countries is increasingly yielding the national market to imported goods.

Figure 3



Inflation on basic goods in Kyrgyzstan and Tajikistan is leading to the depletion of cheap goods, which primarily has an effect on the disadvantaged groups of the population and could lead to an increase in their discontent.

In Kyrgyzstan, inflation on food products has already led more than once to political instability. Today, this turn in events is extremely undesirable since it will deal a hard-felt blow to the faltering national economy.

According to official data, the GDP growth rates in almost all the countries of the region remain at the level of 7-8% a year, whereby the increase in industrial production amounts to 3-4% (see Fig. 4).

Uzbekistan is an exception—it is ahead of its neighbors.

But it should be kept in mind that the increase in GDP is determined taking into account the inflation index. On the whole, relying on the data presented below, the conclusion can be drawn that the CA countries do not have the necessary potential to independently overcome the crisis phenomena in their economies.

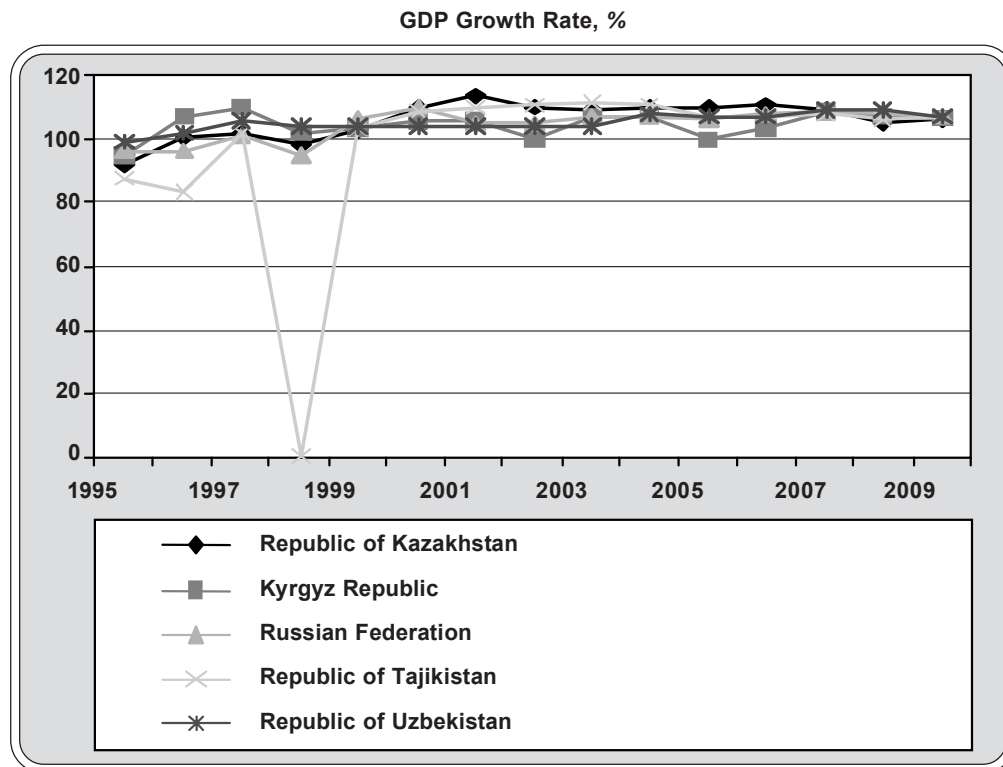
The situation is complicated in Kyrgyzstan and Tajikistan by the energy crisis and its consequences cannot be overcome without help from the outside.

The reasons for the economic instability existing in the republics vary.

The energy crisis in Tajikistan is the result of the civil war, irrational use of resources, and technological backwardness.

In Kyrgyzstan, there is a high level of wear and tear on the basic means of production and an unsophisticated system for using the country's hydro resources.

Figure 4



As early as 1995, specialists warned about the need for rational use of the hydro resources of the Toktogul reservoir; there was talk about the possibility of using different operational regimes for producing electricity and ensuring the needs of agriculture.

But instead of resolving the problems of domestic consumption, electricity manufacturers began orienting themselves more toward the foreign market, which indicates the absence of a balanced state approach to the use of the country's main strategic resource.

Probably the biggest mistake is that instead of mobilizing additional resources to reconstruct the branch, the government decided to raise its efficiency by means of privatization, that is, a change in owner. In the conditions of hydro resource shortage, this decision is absurd. And rolling blackouts are unlikely to resolve the problem, this will not increase the amount of water in the Toktogul reservoir by much.

Here are the main trends that have been seen in the CA countries' economy since the beginning of the world financial crisis.

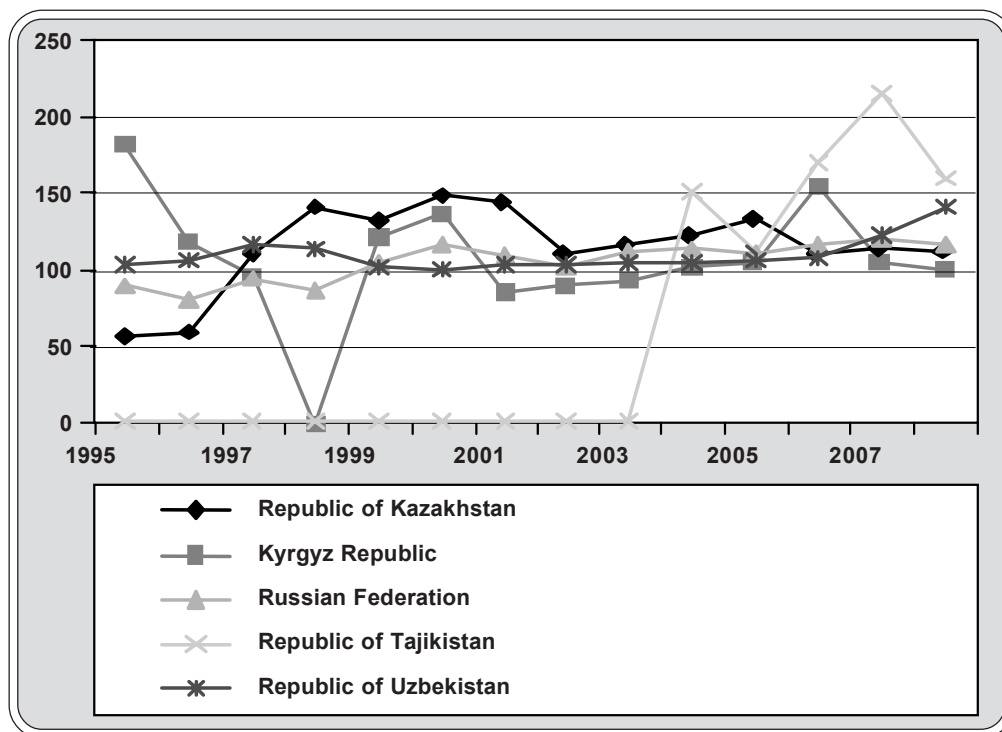
Since August 2008, there has been a sharp increase in inflation rates in essentially all the countries; it reached its peak at the end of September in Tajikistan (29.8%) and in Kyrgyzstan (26.3%).

By the end of the year, the inflation rates had dropped. There are the following reasons for this: the impact of the world economy, the anti-inflation policy conducted by the governments and national banks of the region's countries (drop in interest rate), and the decrease in prices for agricultural products (the region's economy is predominantly agricultural).

During the same period, there was a drop in investment activity due to the impact of the world financial crisis and the shortage of the republics' own financial assets.

Figure 5

Investment Growth Rate in Basic Capital, %



The volume of investments in 2008 compared to 2007 dropped by 2.2%. In Kazakhstan, this index increased by 8.2%, and in Uzbekistan by 19.8%.

The highest investment growth rate in the CIS has been registered in Tajikistan at 77.5%. This abrupt leap was due to the funds invested in the construction of the Rogun GES.

On average, however, the increase in investments in basic capital in all the countries amounted to 13% by the end of 2008, and in January-September 2007 to 21%. The increase in investments from states that are not members of the CIS or the EurAsEC was due to the decrease in investment activity.

Kazakhstan has the best indices in terms of investment growth rates in basic capital and amount of foreign investments. But it should be noted that funds came in spasmodically (see Fig. 5), and in recent years this inflow slowed down even more. This testifies to the republic's unstable financial market, which was confirmed by the 2009 banking crisis.

In recent years, the level of investments in Tajikistan has abruptly risen (almost half of them are Russian), which was promoted by the political stability in the country.

Other countries of the region are showing low investment activity, although in the 2009 forecast Uzbekistan plans to increase its efforts in this area.

On the whole, this indicates the low potential of economic growth in the region's countries.

The currency fluctuations in the exchange rates of the national currency were first characterized by their abrupt growth and then by a drop in the value of monetary units. In this respect, the following possible alternatives were discussed for recovering from the situation that developed: transfer of interstate payments to the ruble zone or transfer to payments using national currencies.

In all the republics, an increase in imports and decrease in exports is seen, which is leading to the formation of a negative trade balance and deterioration of the situation in the payment sphere.

The CA countries have a low export potential (the main index of competitiveness), which is expressed in a high level of raw material production. Despite the increase in the physical volume of export deliveries, the trade balance of the region's countries is worsening (see Fig. 6).

A positive increase in the export of finished products is seen only in Kazakhstan, but its percentage is very small and does not meet the demands of the world competitiveness standards.

From this we can conclude that the foreign trade potential of the CA countries will not allow the region to exist autonomously, that is, it needs help from the outside, which comes mainly from Russia.

The drop in consumer demand was caused by the decrease in the level of household incomes and decline in the profitability of enterprises. This trend is seen mostly in construction and in the service sphere.

All the above-mentioned factors are helping to develop the recession of the national economic systems, particularly in Tajikistan and Kyrgyzstan.

Essentially every country is pursuing a policy of additional capitalization of the banking sector due to the threat of a liquidity crisis. Kazakhstan is in the most difficult situation. Because of the relatively developed nature of its national economy, it has suffered most of all from the mortgage crisis, which created serious threats to the stability of the country's financial sector.

Measures were taken to ensure additional state lending to small and medium businesses, but in two months a positive result was not achieved. This failure is due to the fact that investment funds went into financial circulation, whereas they can only be effective if they are used directly by the state to finance business facilities at low interest rates.

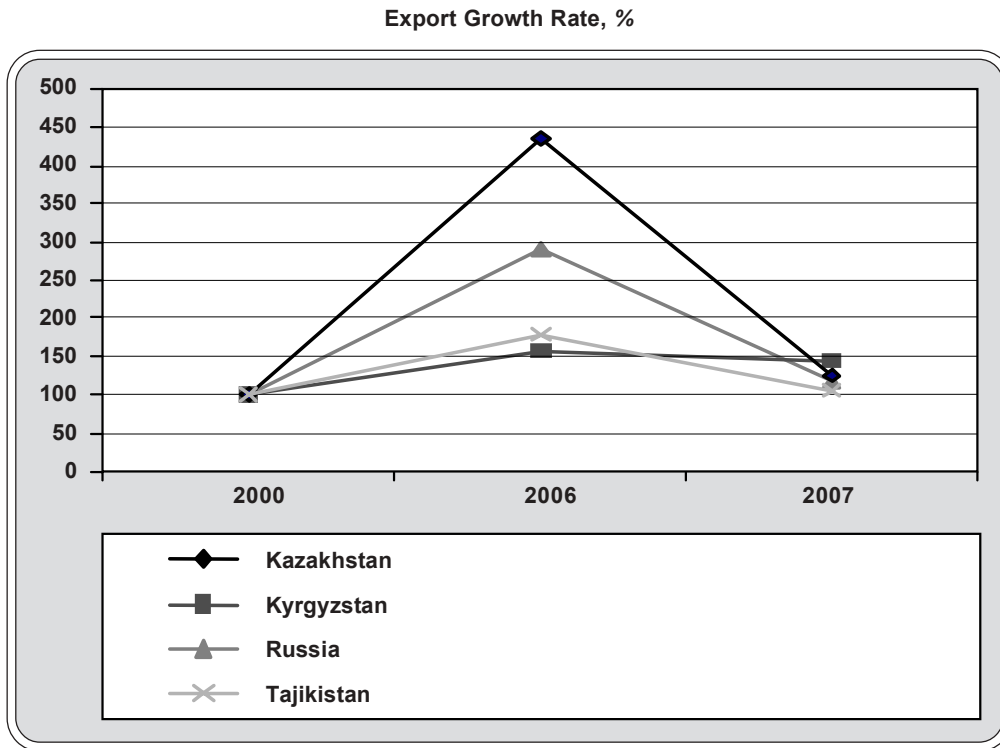
The governments of all the countries of the region have officially recognized the problems their countries are facing and have begun to form a system of anti-crisis management measures, which should have been implemented at least six months ago.

State regulation measures are mainly ineffective, since they do not take into account the specifics of the countries' own economy, are populist in nature, and do not have smoothly operating mechanisms for carrying them out.

For example, state assistance to business in Kazakhstan (from the Kazyna Foundation) has not yielded positive results. Monetary resources transferred to the banking sector were mainly used to



Figure 6



strengthen the liquidity of the banks themselves, while the small amount that was intended for issuing loans became accreted with exorbitant interest rates, that is, state assistance did not reach its target.

In essentially all of the region's countries (with the exception of Kazakhstan), the world financial crisis only exacerbated the economic problems already existing there, sometimes transforming them into a systemic economic crisis.

In Kyrgyzstan and Tajikistan, the structural and energy crisis escalated into a systemic economic crisis, in Kazakhstan, the financial crisis entailed a drop in economic development growth rates (the first sign of an economic crisis); while in Uzbekistan, the structural crisis is acquiring the nature of an economic crisis.

The difficulty of the situation in the region's countries lies not so much in the fact that a crisis exists as in the fact that they do not have their own reserves to overcome it. They are copying the anti-crisis programs of the developed countries, which requires large financial resources and an efficient management system at all levels and also envisages a high level of market relations.

Not one of the CA countries has such resources. This is leading to an increase in financial dependence on external sponsors, that is, to a loss of independence in decision-making. The only solution to this situation might be to pool their own resources and overcome the current contradictions by means of integration both within the region and beyond it.