

# Report on monetary policy for 2013 and medium-term forecast

Approved by  
the resolution of the Board  
of the National Bank of the Kyrgyz Republic  
No. 5/1 of February 25, 2014

## Introduction

During 2013, inflation was within the guideline defined by the Main directions of monetary policy for 2013-2017. In accordance with this document, as the main objective of monetary policy was determined to keep inflation within single digits indices in the medium term. At the end of year, growth of the consumer price index, characterized the rate of inflation, was 4.0 percent (December, 2013 to December, 2012).

The NBKR Notes were the main instrument for withdrawal of excess liquidity in the banking system. Discount rate increased from 2.64 percent to 4.17 percent. Money supply in the economy has been mainly due to the public finance sector. The National Bank conducted mainly sterilization operations. Volume of the NBKR Notes in circulation increased to 6.6 billion KGS by the end of the year from 3.1 billion KGS at the beginning of the year. The National Bank also conducted transactions for the sale of government securities under terms of REPO. Volume of government securities in circulation, sold under terms of REPO, at the end of 2013 amounted to 584.4 million KGS (at the beginning of the year - 795.8 million KGS). Under the credit auctions the credits for the amount of 900.9 million KGS were given for the year.

During 2013 the domestic foreign currency market was balanced, that allowed the NBKR to minimize its presence in the interbank currency market. The volume of currency interventions (sales) of the NBKR was 14.7 million USD. Exchange rate of the USD in relative to the KGS increased by 3.9 percent for the year, from 47.4012 to 49.2470 KGS per 1 USD (in 2012 –by 1.97 percent). The volume of the gross international reserves increased by 172 million USD for the year and at the end of December 2013 amounted to 2238 million USD.

The monetary base increased by 13.4 percent or by 8.6 billion KGS for the year, reaching 73.1 billion KGS at the end of December 2013 (in 2012 – by 17.7 percent). Money M2X increased by 22.8 percent or 22.4 billion KGS and at the end of December 2013 amounted to 120.9 billion KGS (in 2012 – by 23.8 percent).

By the end of 2013 the balance of payments of the Kyrgyz Republic will be in credit in amount of 143.8 million USD. The volume of the gross international reserves will cover 3.5 months of future imports of goods and services. Net inflow of current transfers amounted to 2 238.7 million USD, that is by 8.6 percent more than in 2012. The main growth in this article in the reporting period will be provided by the private transfers, net inflows of which will increase by 8.6 percent and amount to 2 171.1 million USD.

In 2013, GDP grew by 10.5 percent after a decline to -0.1 percent in 2012. Excluding the “Kumtor”, GDP grew by 5.8 percent (by the end of 2012 growth of similar rate amounted to 6.3 percent). GDP deflator was at the level of 2.0 percent against 8.7 percent in 2012.

According to preliminary data of the Central Treasury of the Ministry of finance of the Kyrgyz Republic by the end of 2013 the state budget deficit amounted to 2.3 billion KGS (0.7 percent to GDP<sup>1</sup>) (at the end of 2012 - 6.5 percent to GDP).

During the year, the National Bank has been working to strengthen the interest rate channel of the transmission mechanism of monetary policy. Mechanism of formation of the discount rate was modified from reference to the yield of 28-day Notes of the NBKR to the determination of its size by the Board decision. Decision will come into force from March 2014.

## External Environment

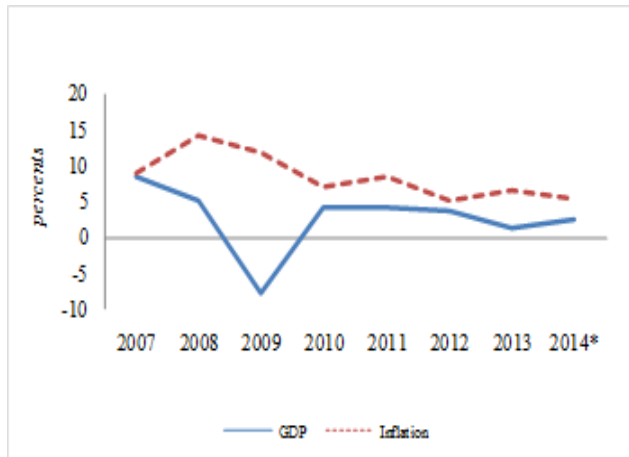
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<sup>1</sup>From September 2013 data calculated on the basis of updated approach to the calculation methodology of the budget indices.

## Economic development of the countries - main trade partners

### Russia

**Chart 1. GDP and inflation growth in Russia**

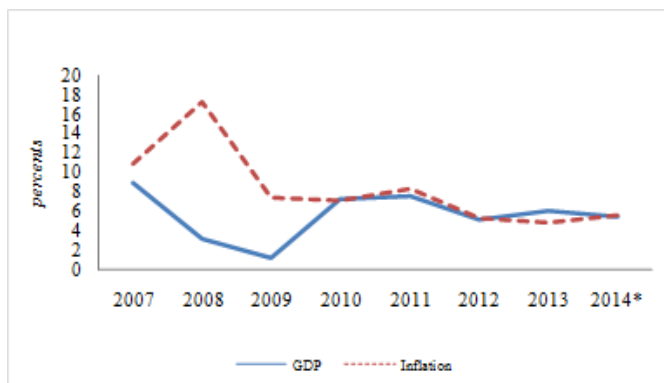


Source: Rosstat, "Bloomberg" IA

Russia's economic growth in 2013 was formed below the forecast.

At mid-year, most international organizations have changed their forecasts for economic growth downward against the background of low indicators of economic development. Previous economic growth forecast by the Government of the Russian Federation was projected at 2.4 percent, by the end of year forecast was corrected to 1.5 percent. Factors contributing to actually prevailing low growth were primarily structural problems in the economy and thereby reduction of production. Decline in investment activity along with capital outflows, low external demand contributed to the slowdown of growth in industrial production that became one of the reasons of appearing of the economic stagnation signs. According to preliminary estimates of the Ministry of Economy of the Russian Federation GDP growth in 2013 was 1.4 percent, inflation for the year has developed better than expected range of 5.0-6.0 percent and amounted to 6.5 percent.

**Chart 2. Growth of GDP and inflation in Kazakhstan**



Source: Statistic Agency of Kazakhstan

### Kazakhstan

In 2013, in Kazakhstan's economy there was observed a continuation of growth rate recovery after the crisis in 2008-2009. Overall in 2013, economic growth and development of the republic corresponded to the plans and forecasts of the Government of the Republic of Kazakhstan. The dynamics of the main macroeconomic indicators in the reporting period remained relatively stable. Real GDP growth in 2013 was 6.0 percent (in 2012 - 5.0 percent). This increase was primarily associated with increased supplies of oil industry and agriculture.

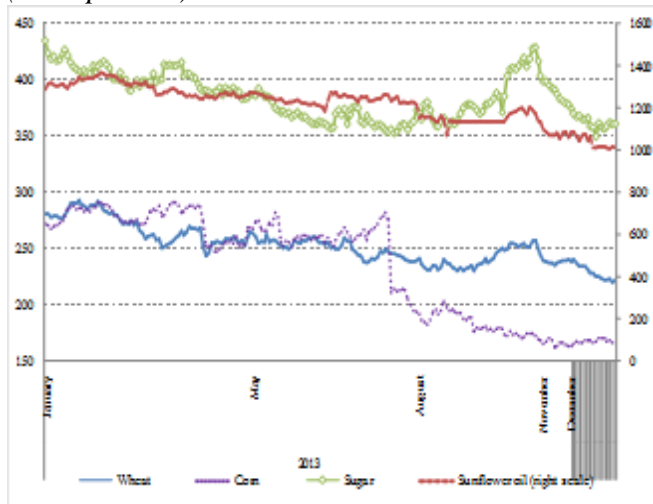
The inflation rate in 2013 was 4.8 percent. Stated level was lower than the expectations of the government of Kazakhstan, which amounted to 6.8 percent. The increase in consumer prices was mainly due to increase in prices for paid services to the population (housing, education, health) and for non-food products.

Despite of the fact that the consequences of the financial crisis eliminated through banking interventions, restructuring and large-scale provision of liquidity, banking

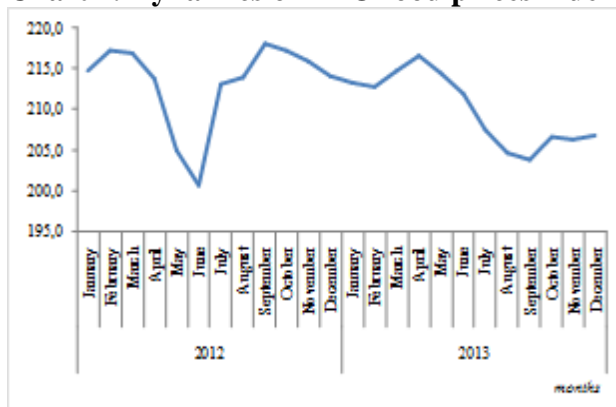
sector is not yet fully recovered. Despite of the stated capital adequacy and banking liquidity, the share of problem loans at the end of 2013 remained high (31.4 percent of total loans) and limited the ability of banks to extend new credits to non-oil sector.

## World commodity markets

**Chart 3. Dynamics of prices for food stuffs (USD per ton)**



**Chart 4. Dynamics of FAO food prices index**



**Chart 5. Dynamics of oil prices in 2013 (USD per barrel)**

## Food Market

In general, food markets in 2013 were relatively calm. Saturation of food markets by rich harvest of 2013-2014 MY allowed balancing supply and demand on the markets and, as a result, to maintain reasonable price stability.

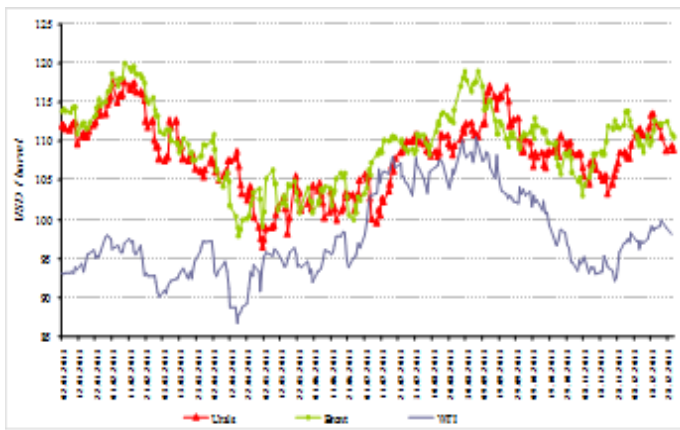
In the fourth quarter of 2013 small price fluctuations in individual commodity units were observed. In October, for the first time since April it was marked an increase in the FAO food prices index, which was caused mainly by increase in prices for sugar and sunflower oil. However, the rise in prices was temporary, after which a gradual decline in futures prices followed.

Record grain harvest in 2013-2014 MY allowed improving the situation with supply in the world and, consequently, to lower world prices for grains, including wheat, corn and rice. Formation of substantial stocks of oilseeds and sugar also contributed to the decline in prices for these commodities. The average value of the FAO food prices index was 209.9 points, by 1.6 points lower than last year.

## The energy market

In 2013, the world energy market which depends on the news background of the global economy, demonstrated volatility, but by the end of 2013 the prices have returned to a price range of the beginning of 2013. In general, the situation on the world oil market in the review period was influenced by: the political and economic situation and climatic factors in the countries - main importers and exporters of oil.

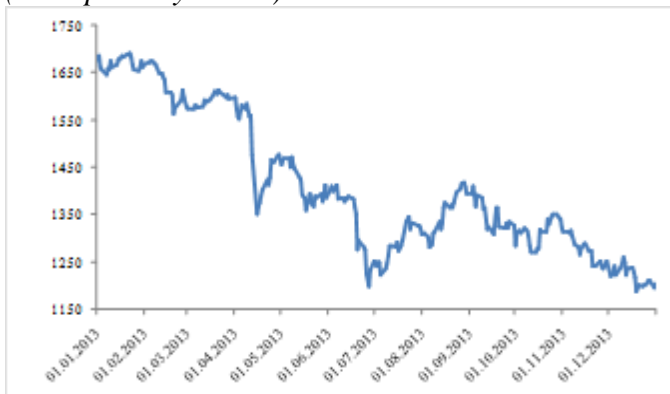
Prices of basic grades of oil (Urals, Brent, WTI) in 2013 fluctuated between 86.7 - 120.1 USD per barrel. The average price of oil of mark "Brent" in the period under review was at 109.6 USD, which is by 2.6 percent less



than the similar indicator in 2012 (112.5 USD).

## Gold market

**Chart 6. Dynamics of prices for gold in 2013**  
(USD per troy ounce)



In the end of 2013 there was a largest fall in gold market: the decline in world prices was 26.4 percent since the beginning of the year (from 1632 to 1200 USD per troy ounce). The main factors that influenced the gold market were as follows:

- waiting for the adoption by the USA Federal Reserve System of decision on tightening of monetary policy and reducing of the program of quantitative easing;

- absence of inflation threat in the world's leading economies, despite of providing by the regulators of flexible monetary policy;

- accumulated economic problems at the largest consumer of gold in the world - India;

- news of a possible sale by Cyprus of significant portion of its gold reserves to stabilize the financial situation in the country and the fear of investors that the central banks of other troubled economies (Italy and Spain) will follow to the example of Cyprus;

- gradual increase in prices for other assets (for example, shares).

## Macroeconomic Development

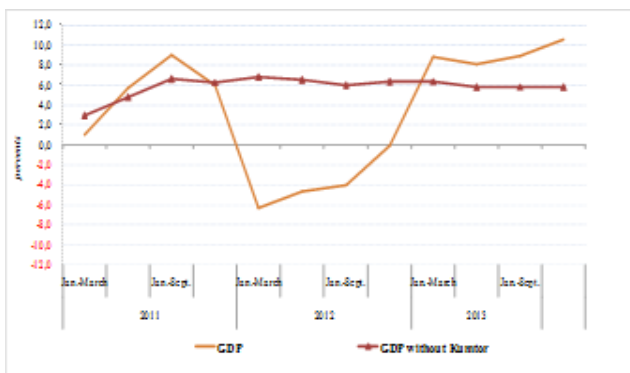
### Supply and demand on the market of goods and services

#### Demand

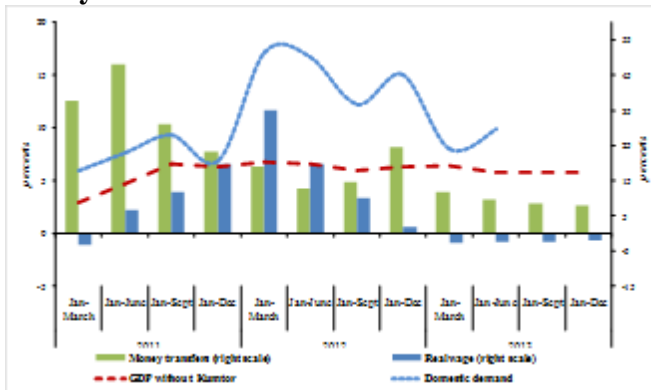
**Chart 7. Dynamics of GDP**

(period /to the corresponding period of the previous year)

Overall, by the results of 2013 economy of Kyrgyzstan has demonstrated significant growth of GDP at 10.5 percent after a decline of 0.1 percent in 2012. High growth rate primarily was due to low statistical base in 2012, as well as the resumption of production at the gold mine "Kumtor" against background of moderate growth in other sectors of the economy. Excluding the

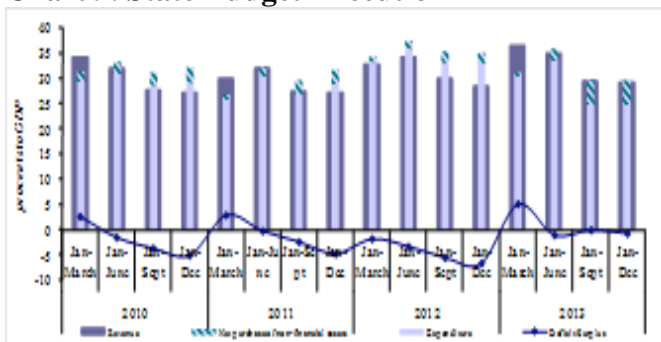


**Chart 8. Dynamics of domestic demand and money transfers**



Source: National Bank of the Kyrgyz Republic

**Chart 9. State Budget Execution**



Source: Central Treasury of Minister of finance of the Kyrgyz Republic, National Bank of the Kyrgyz Republic

**Chart 10. State Budget Execution**

“Kumtor”, volume of GDP grew by 5.8 percent (by the results of 2012 growth rate of similar indicator was to 6.3 percent). GDP deflator was at the level of 2.0 percent against 8.7 percent in 2012.

Domestic demand<sup>1</sup> in January-June 2013 showed more restrained growth rate (+9.9 percent) compared with the same period in 2012 (+17.0 percent). Thus there was a slowdown in growth rate of gross savings in the review period to 5.8 percent, while in January -June 2012, an increase amounted to 37.3 percent. In addition, the dynamics of growth of households’ expenditures on final consumption slowed due to a decrease in real wages in the first half of 2013 by 2.8 percent, as well as sluggish inflow of individuals’ remittances<sup>2</sup> to the country.

Consumption in GDP structure is still a major component of GDP (126.0 percent of GDP), while investments are much less than 31.0 percent of GDP.

According to preliminary data of the Central Treasury of Minister of finance of the Kyrgyz Republic by the results of 2013 the state budget deficit amounted to 2.3 billion KGS (0.7 percent to GDP<sup>3</sup>) (by the results of 2012 - 6.5 percent to GDP).

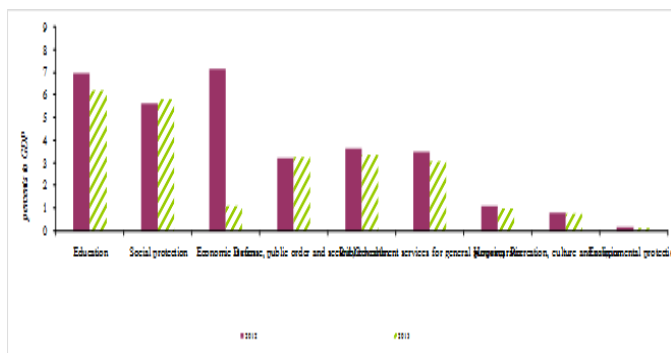
Total revenues of the state budget, including revenues from the sale of non-financial assets amounted to 101.9 billion KGS (29.1 percent to GDP), increasing by 17.1 percent or by 14.9 billion KGS compared to the same indicator in January-December of last year. Tax revenues (10.3 percentage points) made the largest contribution to the increase in operating income, the contribution of official transfers received amounted to 4.1 percentage points and the contribution of non-tax revenues - 2.9 percentage points.

Total expenditure of the state budget, including the cost of acquisition of nonfinancial assets amounted to 104.3 billion KGS (29.8 percent to GDP),

<sup>1</sup>Reference of data for earlier period is caused by the lack of data for 2013.

<sup>2</sup>By the end of 2013 the inflow of remittances increased by 12.5 percent (in 2012– by 19.0 percent).

<sup>3</sup>Since September 2013 there is given a data calculated on the bases of updated approach to the methodology of calculating of budget indicators.



Source: Central Treasury of Minister of finance of the Kyrgyz Republic, National Bank of the Kyrgyz Republic

decreasing compared to the same indicator of January- December 2012 by 2.8 percent or by 3.0 billion KGS.

High proportion of expenditure aimed at current consumption is retaining in the structure of expenditure on economic classification. In the period under review, there was observed an increase in the share of spending on subsidies and social benefits by 7.1 percentage points, formed mainly due to the increase in expenses for the payment of basic part of pension. According to preliminary data of the Social Fund of the Kyrgyz Republic, the Social Fund budget surplus amounted to 0.5 billion KGS (0.1 percent to GDP), income - 33.7 billion KGS (9.6 percent to GDP), expenditure - 33.2 billion KGS (9.5 percent to GDP).

The consolidated budget deficit in the reporting period amounted to 1.9 billion KGS (0.5 percent to GDP). Revenue totaled 118.8 billion KGS (34.0 percent of GDP), and spending - 120.7 billion KGS (34.5 percent to GDP).

Level of investments development in fixed assets in 2013 in real terms increased by only 2.3 percent and in nominal terms amounted to 78.2 billion KGS (in 2012 an increase was 42.1 percent). The priority areas of investments in fixed assets were mining (share in total amounts to 33.1 percent), transport and communication (share - 13.8 percent) and manufacturing (share - 11.1 percent). In the reporting period, investments in fixed assets financed by external funding increased by 10.7 percent, and among them at the expense of foreign direct investments—in 1.8 times, foreign loans - by 0.1 percent, while on the item “foreign grants” and “humanitarian aid” investments, in contrast, declined by 24.3 percent.

**Table 1. Investments in fixed capital by source of funding**

	million KGS		Share	
	January-December		January-December	
	2012	2013	2012	2013
<b>Total</b>	73222.1	78202.6	100.0	100.0
<b>Internal investments</b>	49023.5	50153.1	67.0	64.1
Republic budget (including funds intended for emergency)	3120.1	2679.7	4.3	3.4
Local budget	697.8	589.7	0.9	0.7
Funds of enterprises and organizations	29441.3	29854.5	40.2	38.2
Bank credit	658.7	210	1.2	0.3
Funds of population, including charitable assistance of the K.R. residents	14905.6	16819.2	20.4	21.5
<b>External investments</b>	24198.6	28049.5	33.0	35.9
Foreign credit	17880.1	18733.8	24.4	24.0
Foreign direct investments	3875.1	7407.3	5.3	9.5
Foreign grants and humanitarian aid	2443.4	1908.4	3.3	2.4

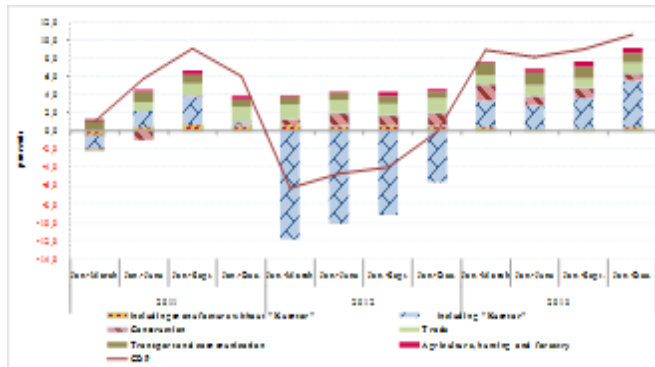
Source: National Statistic Committee of the Kyrgyz Republic

In 2013, level of investments development in fixed assets on the construction of the objects of mining increased by 22.2 percent, 77.0 percent of investments of which were financed by funds of enterprises and organizations, and at the expense of foreign direct investments - 22.3 percent. Investments in the construction of the objects of manufacturing industry exceeded the comparable figure in 2012 by 10.9 percent (78.0 percent of investments used in the construction of facilities for the production of petroleum products). Funding was provided through foreign loans (80.1 percent) which are

mainly represented by investments in the construction of a refinery in Kara-Balta. Volume of investments attracted in the construction of the objects of transport and communications increased by 93.1 percent in compare to the index of 2012.

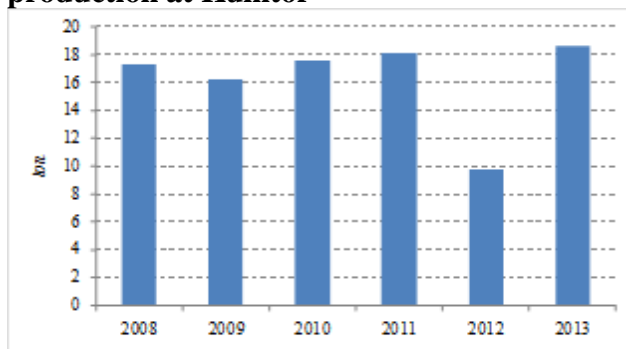
## Supply

**Chart 11. Contribution of the main industries to the GDP growth**  
(period / to the corresponding period of the previous year)



Source: National Bank of the Kyrgyz Republic

**Chart 12. Dynamics of volumes of gold production at Kumtor**



Source: Centerra Gold, National Bank of the Kyrgyz Republic

**Table 2. Dynamics and structure of gross trading turnover**

	Share		Growth Rate
	January-December		
	2012	2013	2012
Trade	100.0	100.0	111.3
Trade in cars, motor vehicles and their spare parts	3.2	3.0	122.8
Car maintenance and repair	0.5	0.4	102.3
Wholesale trade	32.5	31.8	112.0
Motor fuel retail trade	11.2	11.3	125.2
Retail trade	52.5	53.3	107.9
Household Goods Repair	0.2	0.2	95.9

Source: National Statistic Committee of the Kyrgyz Republic, National Bank of the Kyrgyz Republic

In the reporting period the GDP growth was achieved primarily thanks to an increase in value added in manufacturing (+45.4 percent), construction (+12.4 percent) and services (+5.1 percent). Also notable contribution to GDP formation was made by agriculture, where the physical volume of production in 2013 increased by 2.9 percent. The decline in production occurred in the sectors of “mining” (-4.6 percent) and the “production and distribution of electricity, gas and water” (-1.7 percent).

In the period under review, the country’s industrial enterprises produced products with a growth of 34.5 percent, excluding enterprises developing the deposit “Kumtor” - 3.5 percent. The observed high level of growth in the industry is caused primarily by increasing of production in metallurgical production and in fabricated metal products (in 1.9 times) as a result of recovery of output at the Kumtor mine to 18.7 tons of gold by the end of 2013. In manufacturing, there was a decrease in production of textile and apparel products (-16.5 percent), including due to lower export demand for garment products.

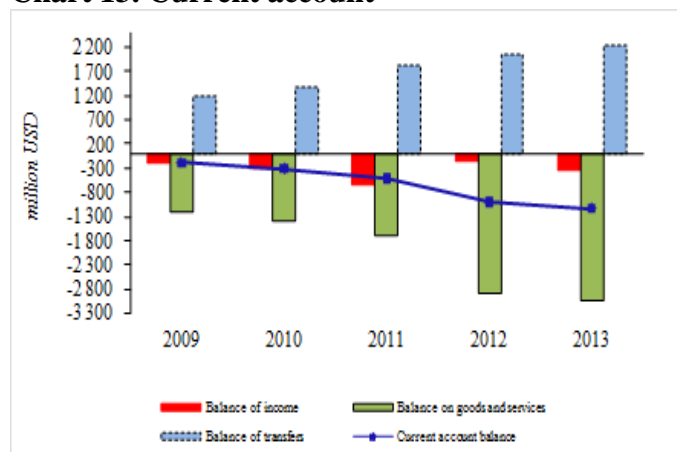
Total output of agricultural products, whose share in the total GDP occupies 15.2 percent, in real terms increased by 2.9 percent in 2013, providing a positive contribution to GDP growth at 0.5 percentage points, mainly due to crop industry. Existing favorable climatic conditions in the country, as well as the project “Financing of agriculture” contributed to the agricultural production growth.

In the services sector, there was noted an increase in value added in trade by 7.0 percent and transport and communications by 12.3 percent. In trade, the gross

turnover of operations in the period under review amounted to 325.8 billion KGS, that is by 7.0 percent more than in 2012 (by the end of 2012 an increase in the volume of trade amounted to 11.3 percent).

### External sector

**Chart 13. Current account**



**Table 3. Trade balance of the Kyrgyz Republic<sup>1</sup>**  
(million USD)

	2012	2013 <sup>*</sup>	Changes, %	Changes, \$
<b>Trade balance</b>	-3001.8	-3455.0	15.1	-453.1
<b>Export (FOB)</b>	1964.7	2108.2	7.3	143.6
Gold	562.3	736.8	31.0	174.5
<b>Import (FOB)</b>	4966.5	5563.2	12.0	596.7
Petroleum	905.6	1055.2	16.5	149.6
<b>Note</b>				
Import in CIF prices	5373.9	6015.2	11.9	641.2
Trade balance (import in CIF prices)	-3409.3	-3906.9	14.6	-497.7
Export without gold	1402.4	1371.5	-2.2	-30.9
Total turnover of	6931.2	7671.4	10.7	740.2

<sup>1</sup> On the ground of actual data of the National Statistics Committee for January-November 2013 and preliminary data of the State Customs Service for December 2013, excluding final appraisals.

**Chart 14. Functional structure of exports of the Kyrgyz Republic** (million USD)

According to the forecasts, by the end of 2013 the extension of the trade balance deficit could lead to a further increase of current account deficit to 15.8 percent to GDP.

According to preliminary data, the balance of trade deficit of the Kyrgyz Republic will grow by 14.7 percent to 3 108.5 million USD (subject to final appraisals of re-exports by the National Bank of the Kyrgyz Republic) at the expense of the following main factors:

- an increase in oil imports by 168.3 million USD;

- a reduction in exports of vehicles for transport of goods and special purpose vehicles<sup>1</sup> by 49.6 million USD and reduction in supply of apparel products by 47.5 million USD and other goods. Exports of goods (at FOB prices, subject to final calculation of re-export of petroleum products) in 2013 will amount to 2 454.7 million USD, increasing by 8.7 percent compared with the same indicator in 2012.

The volume of gold exports is expected to grow by 31.0 percent (by 174.5 million USD in absolute terms). Exports excluding gold<sup>2</sup> will increase by 1.3 percent and will amount to 1718.0 million USD. On the National Bank of the Kyrgyz Republic estimation the growth of re-exports of petroleum products in the reporting year by 18.3 percent (or by 53.7 million USD), as well as an increase in the exports of jet fuel<sup>3</sup> (by 36.7 percent or by 31.6 million USD), vegetables (by 24.9 percent or by 22.0 million USD), rubber tires (in 2.2 times or by 14.0 million USD), rolled glass (by 72.8 percent or by 11.6 million USD) and other goods will contribute to this.

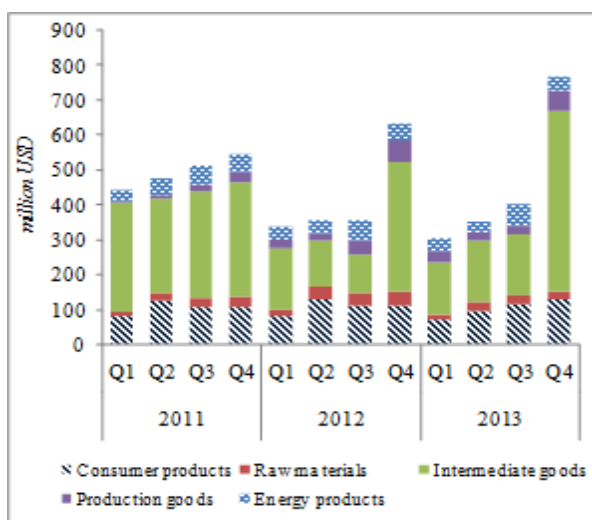
Exports, excluding gold and final calculation of re-export of petroleum products, reached the level of 1 371.5 million USD (reducing by 2.2 percent). Reduction is substantially predetermined by

<sup>1</sup> Re-export.

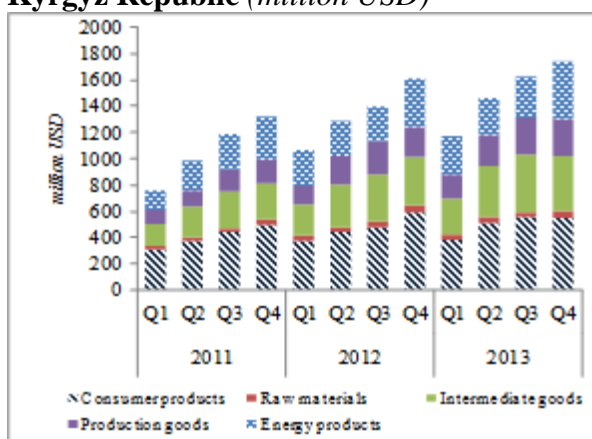
<sup>2</sup> With a glance of final calculation of petroleum products re-export.

<sup>3</sup> Export of on-board reserves.





**Chart 15. Functional structure of imports of the Kyrgyz Republic (million USD)**



**Chart 16. The capital and financial account**

such items like cars for transportation of goods and special purpose vehicles (by 61.8 percent or by 49.6 million USD), articles of clothing and clothing accessories (by 30.3 percent or by 47.5 million USD), ores and precious metals concentrates (by 66.2 percent or by 37.1 million USD) and electric current (by 63.7 percent or by 35.9 million USD).

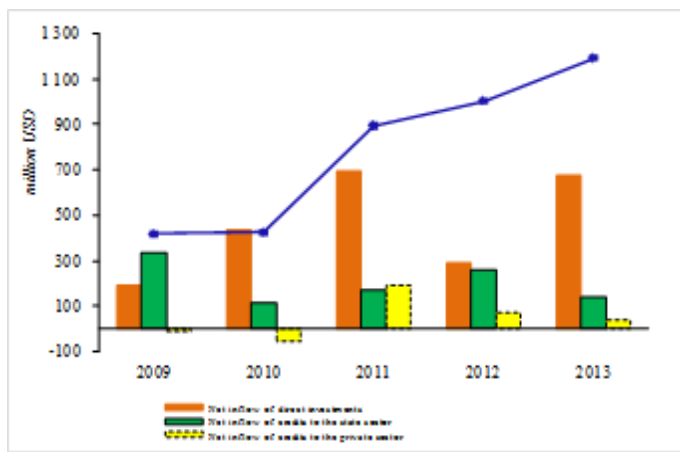
Imports of goods (at FOB prices) for the reporting period will increase by 12.0 percent and will reach to 5 563.2 million USD. The main volume of import growth will be primarily provided by higher volume of imported petroleum products. Also there will be increase of volume of delivery of the structures of iron, steel and aluminum (in 2.7 times or by 69.0 million USD), iron and steel (by 20.3 percent or by 46.2 million USD), cars second-hand (by 8.4 percent or by 32.1 million USD) and other goods.

Balance of services (including final calculation on item “travels”) in the reporting year is expected to be positive and will be at 65.9 million USD, while in 2012 it was negative (183.8 million USD).

In the reporting period it is expected an increase of deficit of income balance by 94.2 percent (to 328.9 million USD). This will be a consequence of the growth of income of foreign direct investors from investing activities in Kyrgyzstan expected, mainly due to increase of volume of reinvested profits of enterprises from 101.0 to 224.2 million USD (an increase in 2.2 times).

Net inflow of current transfers will be in the amount of 2 238.7 million USD, which is by 8.6 percent more than in 2012, that reflecting a slowdown in inflows rate. The main increase on this item in the reporting period will be provided through private transfers, net inflows of which will grow by 8.6 percent and amount to 2 171.1 million USD.

By the end of 2013 the capital and financial account will be formed in credit at a rate of 1 192.2 million USD, which is more than the corresponding figure in 2012



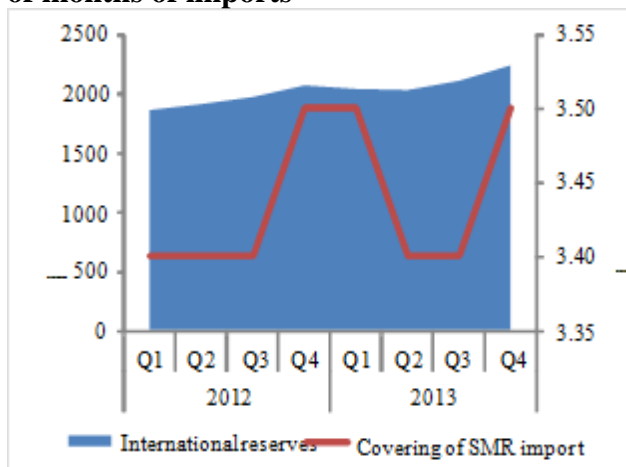
by 18.8 percent.

The balance of the capital account is expected to be positive in the amount of 281.9 million USD, increasing by 69.7 percent in compare with similar indicator in 2012. The main reason for the growth of surplus of capital account was reflection of operation on forgiveness of public debt of the Kyrgyz Republic in the amount of 188.9 million USD to the Russian Federation<sup>1</sup> in the second quarter of 2013/

In the reporting period a positive balance of the financial account will increase by 8.8 percent and amount to 910.3 million USD. The direct and other investments will have the main influence on the balance of the financial account in the reporting period.

The net inflow of direct investments into the country will increase in 2.3 times (up to 675.8 million USD), that will be caused by the increase of the net inflow of funds invested in other capital, in 2.5 times (up to 443.5 million USD), mainly due to loans obtained by direct investment enterprises in the field of exploration of foreign owners.

**Chart 17. Gross international reserves and cover of months of imports**



In the reporting year, net inflows under the item “other investments” will decrease by 56.4 percent and amount to 234.9 million USD. Increase in residents’ liabilities by 342.1 million USD will have primary influence on the mentioned dynamics that is due to increase in net inflow of loans by 177.6 million USD and an increase in accounts payable by 140.5 million USD. Assets of residents in the reporting year will increase by 107.1 million USD that is due to the growth of commercial bank assets and receivables of enterprises.

Thus, by the end of 2013, the balance of payments of the Kyrgyz Republic will be in credit in amount of 143.8 million USD. Gross international reserves<sup>2</sup> will provide cover of 3.5 months of future imports of goods and services.

Item of “Errors and omissions” is

<sup>1</sup>According to the Agreement of September 20, 2012 between the Government of the Kyrgyz Republic and the Government of the Russian Federation on settlement of debts of the Kyrgyz Republic to Russian Federation on credits given earlier (came into force on May 22, 2013).

<sup>2</sup>Gross international reserves by the end of December 2013 will amount to 2 238.2 million USD.

projected at 216.3 million USD that indicates in complete statistical account of operations on export and re-export of goods (cross-border trade), export of tourist services and the net inflow of foreign loans to the private sector.

### Indices of real and nominal effective exchange rate of the KGS

**Table 4. Key figures of the exchange rate**

	2011 (mil.) / 2012 (mil.) / 2013 (mil.)				%	month to the beginning of the year (to the end of month)			
	2011 (mil.)	2012 (mil.)	2013 (mil.)	%		December 2012	December 2013	%	%
REER	112.0	110.7	112.0	1.2	↑	112.6	113.4	0.7	↑
NEER	114.3	113.2	111.6	-1.4	↓	110.8	112.4	1.5	↑
Index of real double-sided exchange rate to CNY	149.8	148.7	141.3	-1.7	↓	146.8	139.1	-4.9	↓
Index of nominal double-sided	80.7	77.4	73.2	-5.4	↓	75.8	71.1	-6.1	↓
Index of real double-sided exchange rate to Euro	134.9	144.2	142.3	-1.3	↓	146.8	137.8	-5.8	↓
Index of nominal double-sided	68.4	72.8	68.4	-6.0	↓	71.0	60.3	-8.0	↓
Index of real double-sided exchange rate to JPY	112.0	110.7	112.0	1.2	↑	112.6	113.4	0.7	↑
Index of nominal double-sided	106.7	106.5	105.5	-1.0	↓	106.6	101.0	-1.5	↓
Index of real double-sided exchange rate to RUB	73.0	74.1	73.6	-0.7	↓	74.2	74.7	0.7	↑
Index of nominal double-sided	107.9	112.1	111.5	-0.6	↓	110.0	113.5	3.2	↑
Index of real double-sided exchange rate to TRY	125.4	124.8	126.9	1.6	↑	125.1	134.5	7.5	↑
Index of nominal double-sided	279.0	294.2	301.9	2.6	↑	289.8	322.4	11.3	↑
Index of real double-sided exchange rate to USD	187.7	184.5	188.1	2.0	↑	192.0	189.1	-1.5	↓
Index of nominal double-sided	103.4	101.5	98.5	-2.9	↓	100.6	96.9	-3.7	↓
* preliminary data									
↓ - devaluation of KGS, improvement of competitiveness									
↑ - strengthening of KGS, deterioration of competitiveness									

According to preliminary data, the index of the nominal effective exchange rate (NEER) of KGS from the beginning of 2013 increased by 1.5 percent and at the end of the reporting year amounted to 112.4. Improvement was due to the strengthening<sup>1</sup> of KGS in December of the reporting year compared with the average rate for December of 2012 against the Japanese yen by 18.8 percent, the Turkish lira by 11.3 percent, the Uzbek sum by 7.1 percent and the Russian ruble - by 3.2 percent. Along with this, there was devaluation of KGS against the euro by 8.0 percent, the Chinese yuan - by 6.1 percent, the USD - by 3.7 percent and the Kazakh tenge - by 1.5 percent.

Despite of lower inflation<sup>2</sup> in the Kyrgyz Republic, strengthening of NEER index of KGS caused increase in the index of the real effective exchange rate (REER), which from December of 2012 increased by 0.7 percent and at the end of this year amounted to 113.4.

## Monetary policy

### Implementation of monetary policy

At the end of the reporting year the actual value of the monetary base amounted to 73.1 billion KGS, which is below the indicative target of 75.0 billion KGS (by 1.9 billion KGS or 2.7 percentage points). Thus, in 2013 the increase in the monetary base amounted to 13.4 percent.

Actual monetary operations of the National Bank of the Kyrgyz Republic for the 4<sup>th</sup> quarter were as follows:

- the National Bank of the Kyrgyz Republic did not conduct operations on the interbank currency market, at the same time at the end of the 4<sup>th</sup> quarter of 2013 the exchange rate of the USD relative to the KGS amounted to 49.4012 KGS per 1 USD;
- volume of Notes of the National Bank of the Kyrgyz Republic in circulation at the end of the 4<sup>th</sup> quarter was 6 645.0 million KGS. National Bank increased the volume of Notes in circulation due to the expected growth in government spending at the year-end;
- outstanding balance of commercial banks on loans refinancing at the end of the 4<sup>th</sup> quarter of 2013 amounted to 392.7 million KGS.

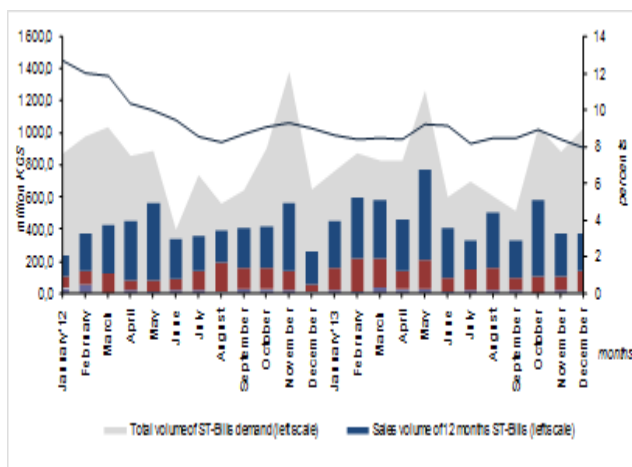
<sup>1</sup>There is given a data on nominal bilateral exchange rate of KGS, 2000 year is used as a basic period for calculating of index.

<sup>2</sup>Inflation in the Kyrgyz Republic for 2013 amounted to 4.0 percent, while the average inflation rate in the countries – main trade partners on preliminary calculation amounted 4.6 percent.

# Monetary policy instruments

## Government securities market

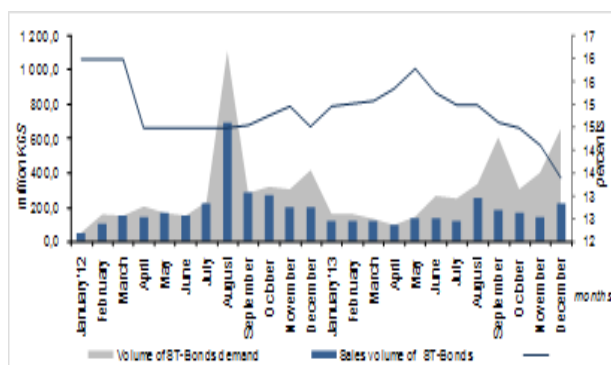
**Chart 18. Dynamics of ST-Bills demand and placement**



### ST-Bills

ST-Bills volume in circulation at end of the period amounted to 4.7 billion KGS, having increased from the beginning of the year by 13.7 percent. The total volume of the announced issuance of bills for January-December 2013 amounted to 5.9 billion KGS, having increased compared to the same period in 2012 by 21.1 percent. Against the background of increasing of demand (+0.2 percent) and sales (+19.3 percent) it was marked the maintenance of downward trend in average yield of ST-Bills in all segments securities placed on the market. Thus, the overall weighted average yield of ST-Bills in January- December 2013 amounted to 8.5 percent (-1.4 percentage points).

**Chart 19. Dynamics of ST-Bonds demand and placement**



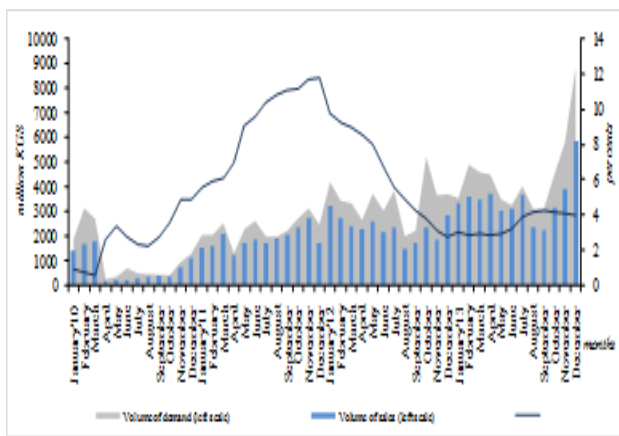
### ST-Bonds

At the end of December 2013 the volume of ST-Bonds in circulation amounted to 5.7 billion KGS, having increased from the beginning of the year by 20.8 percent. Announced volume of issue of ST-Bonds for January- December 2013 amounted to 1.9 billion KGS, having decreased in comparison with the same indicator of 2012 by 29.4 percent. Against the background of the decrease in demand (-0.8 percent) compared with the same indicator in 2012, volume of sales fell by 31.9 percent. The weighted average yield of 2-year ST-Bonds for the period was 14.8 percent, having decreased by 0.1 percentage points compared with the same period in 2012.

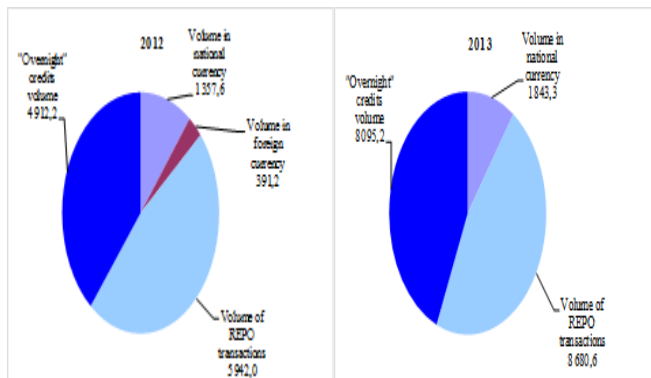
**Chart 20. Dynamics of the NBKR Notes demand and placement**

### Notes of National Bank of the Kyrgyz Republic

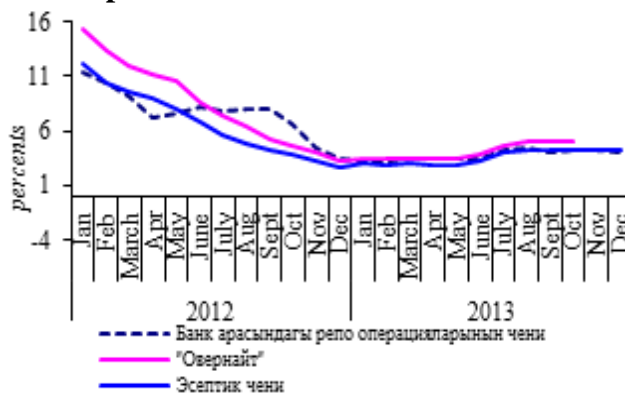
At the end of 2013 the volume of Notes in circulation amounted to 6.6 billion KGS, having increased over the year in 2.2 times. Total volume of issue of the National Bank of the Kyrgyz Republic Notes in the reporting period amounted to 50.6 million KGS, with an increase by 62.2 percent compared with the same period in 2012. In January - December 2013 the volume of demand (+30.8 percent) as well as volume of sales (+52.9 percent) increased. The weighted average yield of



**Chart 21. Volume of transactions on the credit resources interbank market**



**Chart 22. Rates of the NBKR and interbank REPO operations**



**Chart 23. Dynamics of the commercial banks deposits**

Notes of the National Bank of the Kyrgyz Republic in 2013 was 3.5 percent compared to 6.3 percent in the same period in 2012.

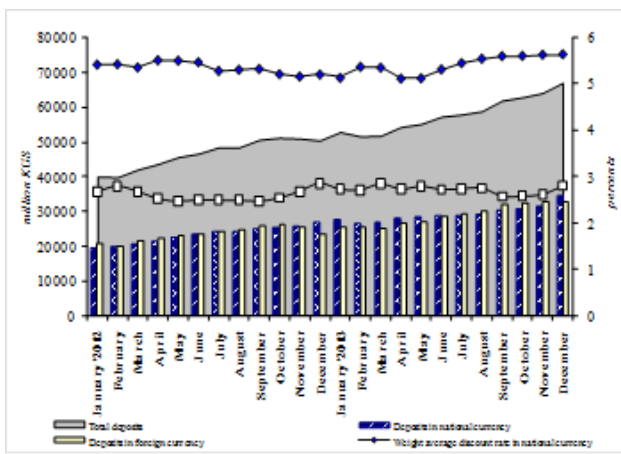
### Interbank market of credit resources

During the period under review there were also conducted operations on the interbank money market. The total volume of loans in KGS was 18.6 billion KGS, due to an increase of the ordinary credit transactions in the national currency by 35.8 percent, which amounted to 1.8 billion KGS with an average interest rate of 7.2 percent. REPO transactions were conducted in the amount of 8.7 billion KGS with an increase of 46.1 percent. Weighted average interest rate on these transactions amounted to 3.8 percent.

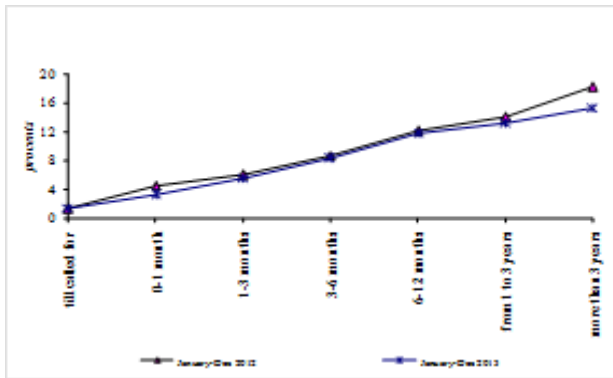
After the increase of issue of the National Bank of the Kyrgyz Republic Notes there was an increase in their yield. As a result, the discount rate, the level of which is tied to the yield of 28-day the National Bank of the Kyrgyz Republic Notes, increased, that generally reflects the direction of current monetary policy. At the end of the reporting period, the discount rate was 4.2 percent (+1.6 percentage points since the beginning of the year). Rate on “overnight” loans as a result decreased by 4.4 percentage points compared with the same period of January- December 2012, at the average for the period was 4.1 percent. The volume of these loans for the year grew to 8.1 billion KGS (+64.8 percent).

### Deposit market

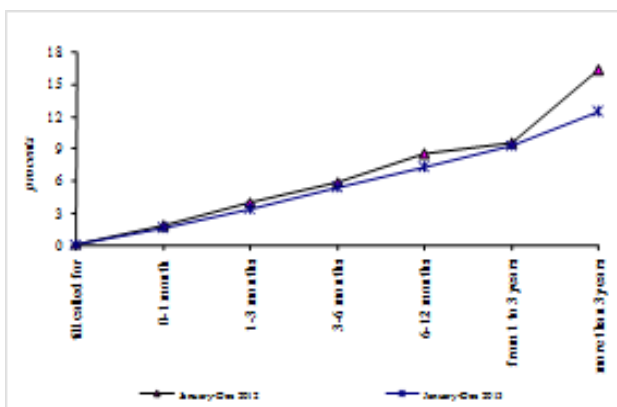
The volume of deposits showed an upward dynamics. The volume of the deposit base of the commercial banks at the end of December 2013 amounted to 67.3 billion KGS, having increased from the beginning of the year by 32.9 percent. This increase was due to growth of deposits in foreign currency (by 38.5 percent to 32.9 billion KGS in equivalent), as



**Chart 24. Rates of new deposits in the national currency by priority rank**



**Chart 25. Rates of new deposits in the foreign currency by priority rank**



well as in national currency (by 28.1 percent to 34.5 billion KGS).

The share of deposits in the structure of the deposit base increased since the beginning of the year from 41.1 percent to 42.1 percent.

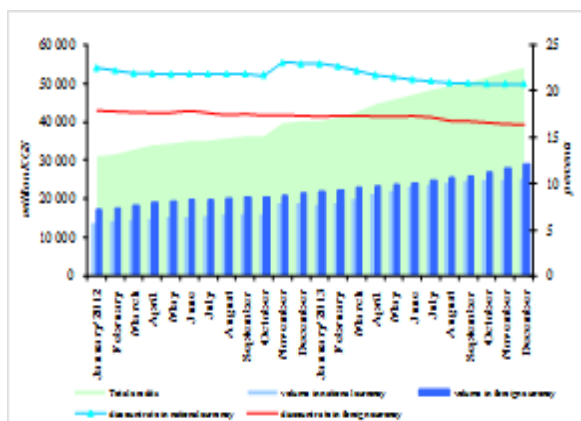
Duration indicator of total deposit base was at the level of beginning of the year at 4.5 months, the duration of time deposits decreased from 13.0 to 11.4 months.

The weighted average interest rate on new deposits in national currency in January-December 2013 was 2.3 percent, haven't changed compared with the same period in 2012, on deposits in foreign currency - also haven't changed and amounted to 0.8 percent. The weighted average interest rate on newly accepted demand deposits in national currency was 1.4 percent, unchanged from the same period in 2012, on fixed deposits - fell by 0.3 percentage points to 9.8 percent. The weighted average interest rate on newly accepted deposits on demand in national currency amounted to 1.4 percent, hasn't changed compared with the same period in 2012, on fixed deposits - has decreased by 0.3 percentage points to 9.8 percent. In foreign currency interest rate on newly accepted deposits on demand hasn't changed compared with the same period in 2012, amounted to 0.1 percent, on fixed deposits - fell to 5.8 percent (-0.8 percentage points).

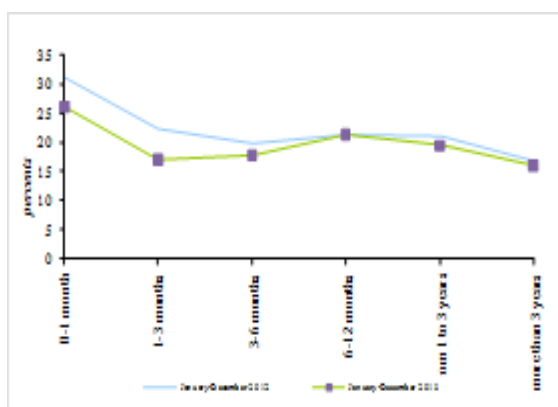
## Credit market

In 2013, lending by commercial banks was boosted at a faster rate, both due to the issuance of foreign currency loans, and due to the credits in the national currency. One of the sources of credit was the project "Financing of agriculture." At the end of December 2013, the loan portfolio of

**Chart 26. Dynamics of credit liabilities of the commercial banks at the end of period**



**Chart 27. Rates of new credits by priority rank**



commercial banks amounted to 54.0 billion KGS, having increased from the beginning of the year by 34.5 percent. Loans in national currency among them totaled 25.0 billion KGS, having increased by 34.9 percent, and in foreign currency - 28.9 billion KGS in equivalent of KGS (+34.2 percent).

In the term structure of the loan portfolio of banks there was a reduction of short-term loans (less than one year). The share of such loans since the beginning of the year fell from 22.8 to 17.0 percent. Share of long-term loans, by contrast, rose to 79.8 percent (+5.8 percentage points).

Indicator of duration from the beginning of the year increased from 27.6 to 29.6 months.

The weighted average interest rate for January-December 2013 on new loans in national currency decreased by 1.7 percentage points and amounted to 21.3 percent, in foreign currency - also fell by 1.4 percentage points to 17.7 percent.

## Secondary market for government securities

In the reporting period in the secondary market of government securities, there were four transactions on purchase and sale of ST-Bills and one - on ST-Bonds.

Transactions with ST-Bills were carried out on 48.1 million KGS at the weighted average rate of 8.7 percent.

ST-Bonds were sold on the secondary interbank market in the amount of 98.8 million KGS, at a rate of 14.6 percent.

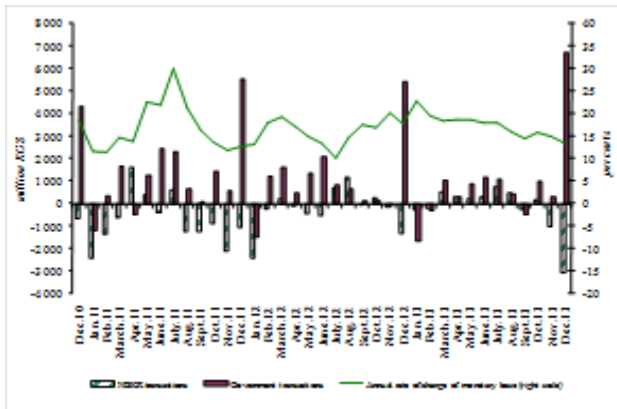
## Dynamics of monetary indicators

### Monetary base

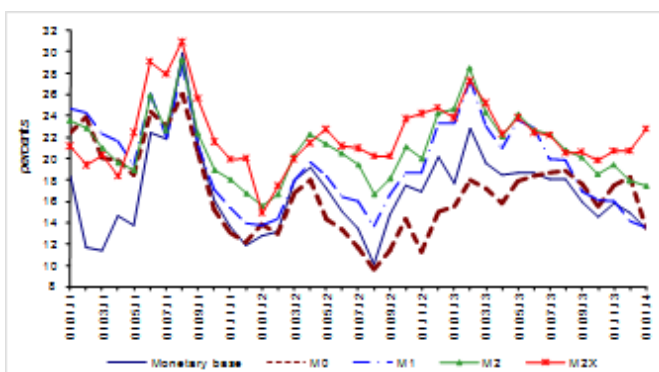
The monetary base by the end of 2013 increased by 13.4 percent or by 8.6 billion KGS on January 1, 2014 amounted to 73.1 billion KGS (in 2012 there was an increase of 17.7 percent). Operations of the Government influenced the growth of the monetary, increased it by 10.4 billion KGS, the National Bank's transactions reduced the monetary base by 1.8 billion KGS.

Due to open market operations the

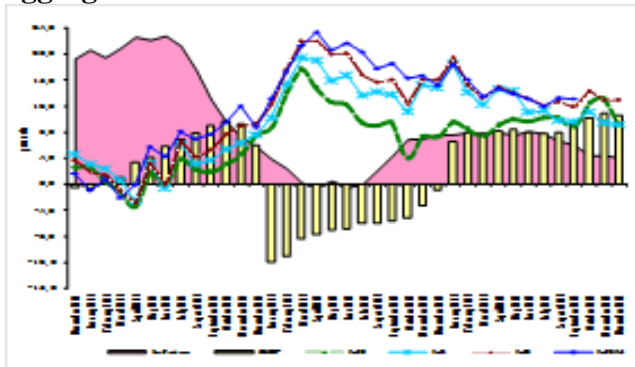
**Chart 28. Contribution of the Government and the NBKR operations to the change of monetary base**



**Chart 29. Nominal growth rates of monetary aggregates (in annual term)**



**Chart 30. Inflation, real growth rate of money aggregates and GDP**



National Bank of the Kyrgyz Republic sterilized 7.2 billion KGS. The National Bank during the year bought gold on the domestic market of 1.2 billion KGS, the amount of funds granted under the credit auctions for refinancing and liquidity support was 900.9 million KGS.

In the structure of the monetary base the share of cash in circulation in 2013 was 91.5 percent, the share of funds on correspondent accounts of commercial banks in the National Bank - 8.5 percent.

### Monetary Aggregates

Nominal growth rate of monetary aggregates in annual terms at the end of 2013 ranged from 13.5 to 22.8 percent, according to the results of 2012 - from 15.5 to 24.7 percent that was reflected on slowing of real annual growth rate of monetary aggregates. M2X among monetary aggregates increased at a most great rate mainly due to the growth of the deposit base in foreign currency.

Broad money M2X, which includes deposits in foreign currency in 2013, amounted to 120.9 billion KGS, having increased from the beginning of the year by 22.8 percent (in 2012 - 23.8 percent). The main contribution to the growth of M2X was made by increase in deposits<sup>1</sup> by 34.2 percent (in 2012 - by 36.1 percent), including the increase in foreign currency deposits amounted to 42.4 percent, in national currency deposits - 26.7 percent (in 2012 - by 20.8 and 53.9 percent, respectively). Excluding the impact of exchange rate changes, total deposits increased by 31.7 percent. In general, the dynamics of development of the deposit base reflects a continuation of confidence in the banking system.

In the context of the sectoral components of broad money M2X nonfinancial corporations<sup>2</sup> deposits grew most rapidly, having increased for the reporting period by 40.7 percent (in 2012 - by 35.7 percent).

Deposits of other resident sectors<sup>3</sup> and other financial corporations<sup>1</sup> in the period

<sup>1</sup>Excluding deposits of the Government and non-residents.

<sup>2</sup>Nonfinancial corporations: corporations, which produce and realize goods and nonfinancial services, and which are not related to the financial sector of economy.

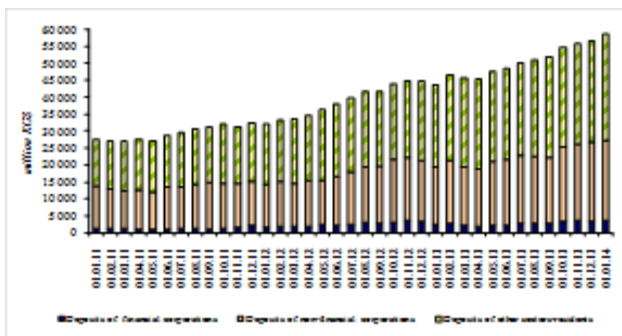
<sup>3</sup>Other resident sectors: include all economic units and noncommercial organizations served them.



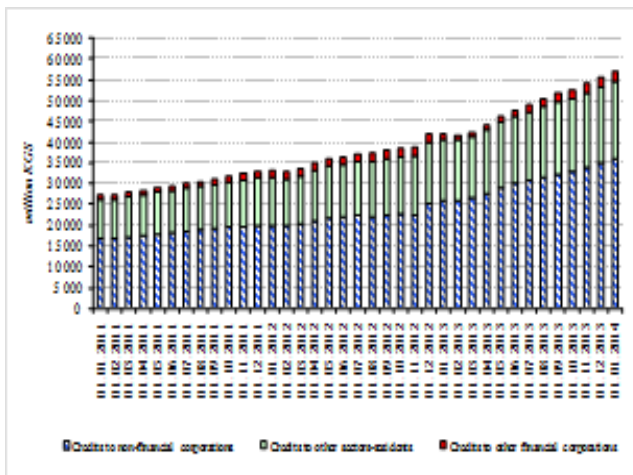
**Chart 31. Dynamics of deposits including in M2X**  
(in annual term)



**Chart 32. Dynamics of deposits including in M2X**



**Chart 33. Dynamics of the credit to the economy by the sectors**



## Dynamics of Inflation

### Consumer price index

under review increased by 29.3 and 38.1 percent, respectively (on the results of 2012 – by 35.7 and 42.9 percent, respectively).

Along with the increase in net foreign assets of the banking system, the expansion of credit activity of commercial banks in the reporting period also contributed to the growth of broad money M2X.

Credit to the economy by the end of 2013 increased by 36.1 percent, while lending in local currency increased by 38.4 percent, and in foreign currency - by 33.9 percent (in 2012 - 27.9 and 24.6 percent, respectively). Excluding the impact of exchange rate<sup>2</sup> credit in the economy increased by 33.4 percent.

In terms of sectors, loans to other financial corporations showed the most rapid growth, which increase from the beginning of 2013 amounted to 76.5 percent. Growth of loans to non-financial corporations was 39.4 percent, loans to other resident sectors - 26.3 percent (on the results of 2012 - 28.6 and 27.2 percent, respectively).

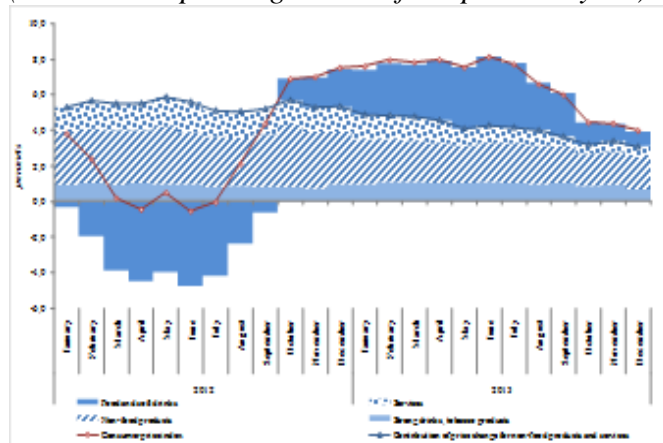
Due to the greater rate of the monetary expansion in compare to the GDP growth rate, economy's monetization ratio, calculated on the monetary aggregate M2X, increased in 2013 from 29.0 percent at the beginning of the year to 30.8 percent. Thus, the velocity of circulation calculated on the same monetary aggregate M2X, decreased in 2013 from 3.4 at the beginning of the year to 3.2.

Broad money M2X multiplier characterizing the degree of financial intermediation has increased from 1.527 at the end of 2012 to 1.653 by the end of 2013 due to an increase in the volume of deposits in broad money M2X.

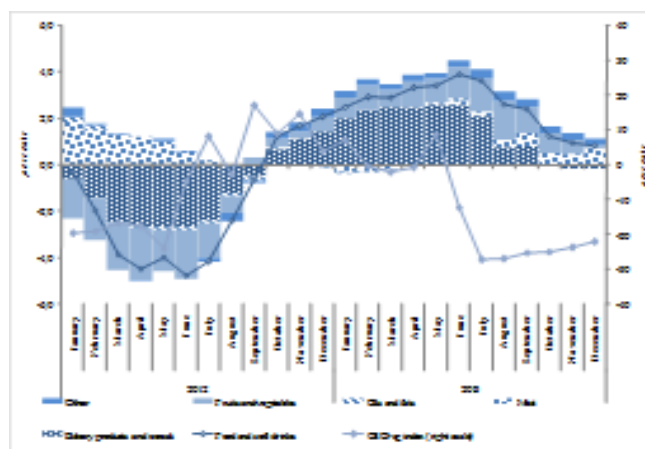
<sup>1</sup>Other financial corporations: institutional units, which don't issue commitments, including to the national definition of broad money M2X (nonbanking financial credit organizations, insurance companies, pension funds, different financial companies refer to them).

<sup>2</sup>Constant (program) exchange rate: 47.0992 KGS per 1 US dollar.

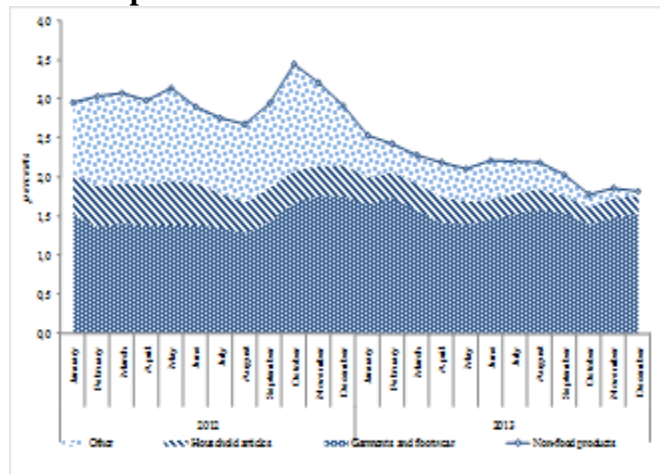
**Chart 34. Dynamics of annual CPI structure (to the corresponding month of the previous year)**



**Chart 35. Dynamics of the contribution of food prices in the annual CPI**



**Chart 36. Dynamics of the contribution of nonfood prices in the annual CPI**



inflation rate was at 6.6 percent. During 2013, inflation rate was within single digits, as it was defined in the Main directions of the monetary policy for 2013-2015.

Dynamics of the general price level in 2013 was formed amid falling world prices for basic food commodities (cereals, oilseeds, sugar). Favorable terms of external trade, a good harvest of major crops in Kyrgyzstan and in countries of major trading partners, moderate wage growth also had a positive impact on the level of inflation in the country.

In 2013, there was a significant slowdown in food prices growth rate. Food commodities for the year rose in price by 1.8 percent. Prices of bread and cereals, a group which accounted for the largest share in the structure of food products, for the year decreased by 0.8 percent as well as the price of the first rate wheat flour decreased by 3.4 percent. Record grain harvest in the region and the subsequent decline in export prices in Kazakhstan by 34.6 percent had a major impact on the dynamics of prices for bakery products.

In the period under review there was volatile trend in prices for fruit and vegetables as well as fruit rose in prices by 25.2 percent, and vegetables fell in prices by 6.7 percent. Overall, the increase of the price index for fruits and vegetables was 2.0 percent.

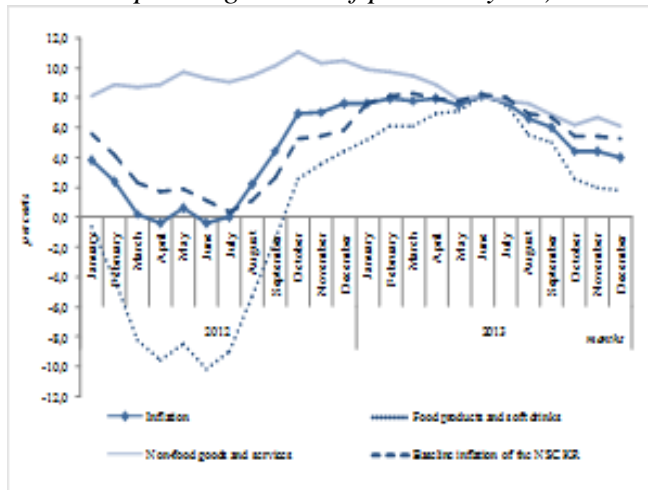
Big crop of oilseeds in Russia and Ukraine, major importers of these products to Kyrgyzstan, has helped to reduce domestic prices of vegetable fats. Commodity group “oils and fats” decreased on an annual basis by 2.2 percent.

The price index for dairy products on an annual basis rose by 6.6 percent.

The price index for non-food commodities showed a significant slowdown in the reporting year. Increase in the index in December in annual terms amounted to 6.3 percent against 8.8 percent in the beginning of the year. Meaning of the price index for non-food items for the year proved to be the lowest since July 2007. The largest price increase occurred in the group of goods “clothing and footwear”, which rose in price by 13.6 percent. Household goods and appliances rose in price by 6.2 percent. The cost of fuel and lubricants in annual terms increased by 0.1 percent as well as gasoline prices have not changed, diesel prices rose by 1.0 percent.

The price index for paid services in annual

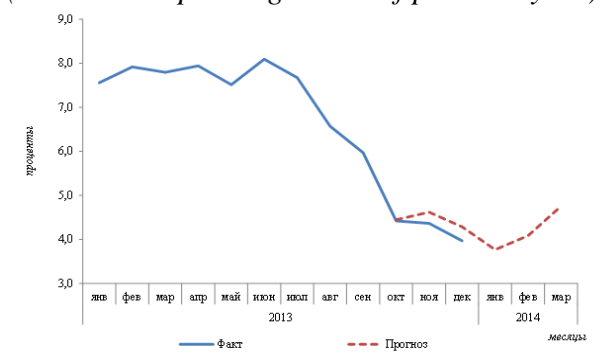
**Chart 37. Dynamics of Consumer price index (to the corresponding month of previous year)**



terms increased by 4.3 percent (in 2012 –by 9.8 percent). Increase in the index in this group was mainly due to increased cost of services of restaurants and hotels by 3.9 percent, education services (+6.1 percent) and transport services (+2.1 percent). Health services rose in price by 10.6 percent. In 2013, there was a slowdown in growth rate of the annual value of core inflation, calculated by the method of the National Statistic Committee of the Kyrgyz Republic, from 7.6 percent in January to 5.3 percent in December 2013.

### Comparison of forecast with the fact

**Chart 38. Actual and projected value of the CPI (to the corresponding month of previous year)**



The actual level of inflation in the fourth quarter of 2013 (2.3 percent) formed slightly below the consensus forecast for this period (2.5 percent). Deviation of predicted values of inflation from the actual caused by greater-than-expected decline in prices of food commodities group due to a rich harvest in the countries producers of the crops.

### Medium-term forecast

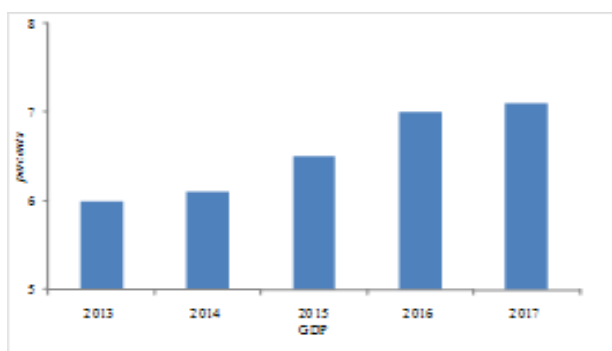
#### Assumptions about the environment

#### Forecast of development of the countries - main trade partners

Updated forecasts of the international organizations assume the global economic recovery in 2014.

#### Russia

**Chart 39. Real GDP growth of Russia (year to year, %)**



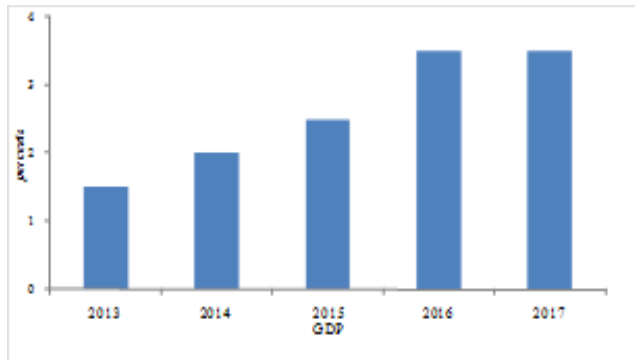
Given the economic slowdown in 2013, the assumptions for 2014 have been revised downward from 3.0 percent to 2.0 percent, for 2015 from 3.5 to 2.5 percent according to the IMF report. Passive investment activity remains as deterrent of economic growth. The projected recovery of developed countries economies may enhance the outflow of capital from developing countries, such as Russia, as well as a decline in investments that will inhibit the growth of the economy of Russia.

Source: IMF

As for the rate of Russian ruble, the key role in its change a capital outflow will play, which will be intensified by the expected reduction of the FRS program on “quantitative easing” and the rise of interest rates in the USA, a capital outflow will follow by this as a whole from developing to developed countries.

### Kazakhstan

**Chart 39. Real GDP growth of Kazakhstan (year to year,%)**



Source: Government of the Republic of Kazakhstan

Real economic growth of Kazakhstan in 2014-2018 is projected at 6.0-7.1 percent. In the terms of slow recovery of external demand for basic goods, economic growth in the medium term will be achieved by increasing of investments volume in the industrial and innovation and infrastructure projects, start of developing of Kashagan oil deposit and growth of population consumption.

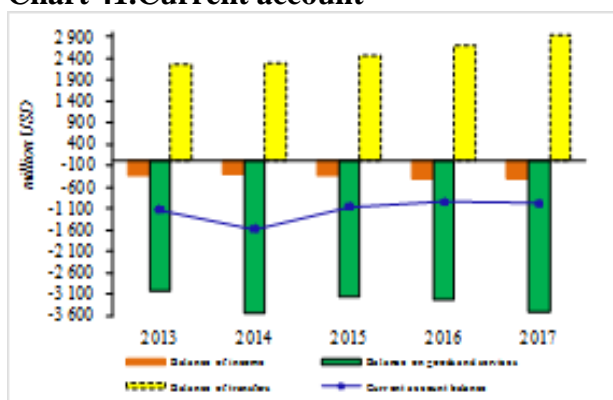
In the short and medium term economic development perspectives depend on the preservation of stability of macroeconomic situation, which in turn depends on the policy of spending of oil revenues on the basis of established rules and sustainable development of the financial sector.

Possible deterioration in the trade may slightly affect the service sector and lead to double surplus of the current account and the state budget balance.

The annual inflation rate in 2014-2018 will be in the range of 6.0-8.0 percent.

### Forecast of the balance of payments for 2014-2017<sup>1</sup>

**Chart 41. Current account**



In 2014 the current account deficit is projected at 19.8 percent to GDP that is higher by 4.0 percentage points than the corresponding figure in 2013.

The deterioration of the trade balance will make the main pressure on the current account: the trade balance deficit will increase by 11.2 percent, reaching 3 457.9 million USD. The prerequisite for this will be the expected decline in exports at 7.0 percent due to a slowdown of growth rate in the export-oriented sectors, primarily in agriculture and slowing of growth of the industrial manufacture excluding Kumtor, as well as the decline in world gold prices. Exports excluding gold will drop by 11.6 percent. Possible increase in supply of certain

<sup>1</sup>In preparation of forecast, it is considered the factor of accession of the Kyrgyz Republic to the Customs Union since 2015.

imported goods (for resale) in connection with the forthcoming accession of the country to the Customs Union will have an upward effect on import volumes. However, given the expected decline in the country's dependence on imports of energy products, in connection with the launch of the refineries, the dynamics of imports growth in 2014 will be at 3.0 percent.

At the same time, a positive growth rate of net inflow of current transfers (at 2.0 percent) will maintain. Toughen of legislation in the host countries of domestic workers will have a downward effect on the dynamics of remittances, growth rate of which will be at 5.3 percent in the forecast year.

Traditionally, current account deficit will be financed by capital inflows on the financial account, primarily due to foreign direct investments (446.8 million USD) and external loans (438.7 million USD).

As a result, the overall balance of payments was in deficit at the level of 54.4 million USD. Coverage level of reserve assets of the National Bank of the Kyrgyz Republic will remain at a safe level (3.5 months of imports).

It is projected an improvement of the current account in 2015 (current account deficit will decline to 12.2 percent to GDP), reduction of the trade balance deficit will contribute to this by reducing import receipts (due to increased customs duties) as well as an increase in transfers growth rates due to the growth of remittances (in connection with the improvement of conditions for the activities of migrant workers in the Russian Federation and Kazakhstan).

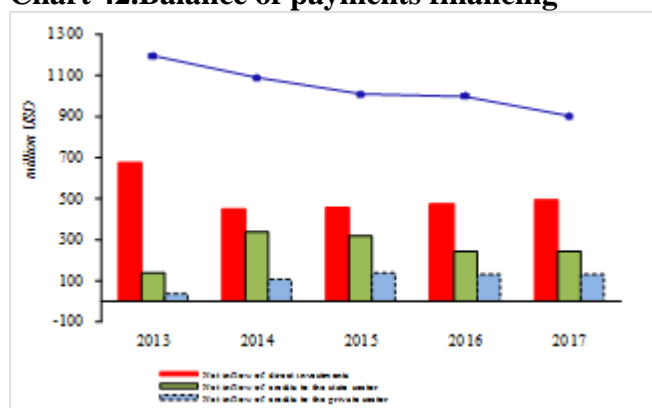
Capital inflows on the capital account and the financial account will maintain at the level of 2014, as a result, the total balance of payments will be positive (27.1 million USD).

It is projected deterioration of the trade balance of the country in 2016-2017 caused by more dynamic growth in import deliveries compared with growth of export earnings. At the same time the growth in the net inflow of current transfers at level of 9.0 percent per year will improve the current account to 8.8 percent to GDP in 2017.

The current account deficit will be financed by the net inflow of loans at an average of 377.0 million USD and foreign direct investments of 482.0 million USD.

In general, the overall balance of payments for 2016-2017 is projected to be positive (an average of 38.7 million USD),

**Chart 42. Balance of payments financing**



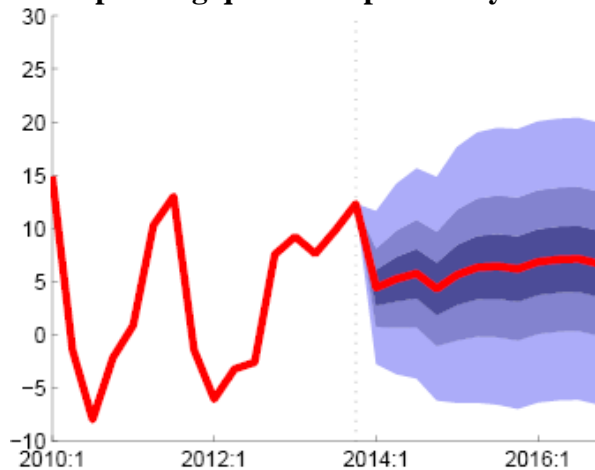
with the criterion of adequacy of reserve assets to cover imports of goods and services is projected at a safe level (an average of 3.4 months of imports).

In a forecast balance of payments of the Kyrgyz Republic for 2013 - 2015, there is still uncertainty and risks:

- continuous work on the development of deposit “Kumtor”;
- volatility of world prices for gold and oil;
- shortfall of the planned volume of foreign loans to the public sector;
- undisturbed operation of a refinery in Kara-Balta and increase its production capacity;
- changes in the terms of trade with the countries - major trade partners.

### Medium-term forecast

**Chart 43. GDP forecast,% quarter/ corresponding quarter of previous year**



### Development of real sector of the economy

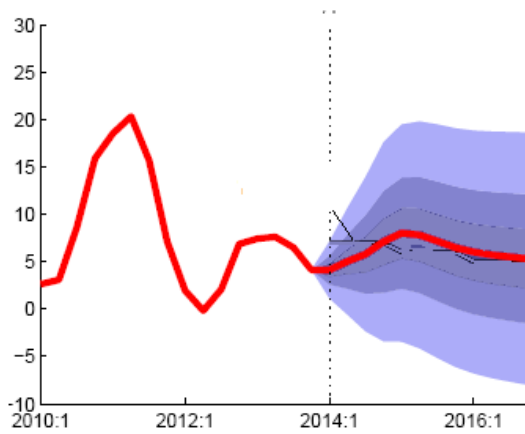
Against the background of significant weakening of external demand, the economy of Kyrgyzstan will experience downward pressure on economic growth in the medium term. It is expected that at the heart of this dynamic there will be a decline in volume of exported goods and a decline in remittances caused by the slowdown in economic growth of Russia and Kazakhstan, as well as the devaluation of the national currency in these countries. On average, up to 2017 economic growth in the country will be 4.72 percent. In the manufacturing industry it is expected a slight decline due to some low volume of gold mining at Kumtor deposit.

Significant devaluation of the currencies in relation with capital outflows from developing countries becomes a key change, with which the region’s economy will face in the coming years. Outflow will be caused by the new policy of the Federal Reserve System for a speedy conclusion of incentive programs and increase in rates.

### Inflation

On average in 2014, inflation will be moderate, but at the end of this year there will be a slight increase in inflationary pressures by increasing food inflation that would result from the dynamics of food prices on world markets and the depreciation of KGS. Upward

**Chart 44. Inflation forecast, %  
corresponding quarter of previous year**



quarter/ trend of inflation will continue in 2015, in which it reaches maximum - 8.4 percent on average for the 1 quarter. In subsequent years, there will be a slowdown in inflation rate growth, mainly due to lower growth in imported inflation for food and non-food inflation slowdown. According to the forecast favorable situation will develop in the global oil market. It is supposed a decline in oil prices in the coming years, due to the contribution of this factor to the increase in non-food inflation from the outside world will be relatively weak.

Prices on the world food market will rise before the end of the forecast period.

Gold prices will fall, as a result of this the export revenue under this item of exports will decline and, respectively, the inflow of currency into the country. At the same time, the latter will largely depend on the dynamics of remittances.