

**Joint Statement
of the Government of the Kyrgyz Republic and the National Bank of the Kyrgyz Republic
on Economic Policy for 2011**

Introduction

As per results of 2010, the Government of the Kyrgyz Republic could overcome threats of the economic growth sharp decline in the conditions of negative influence, caused by April political and June tragic events.

From the beginning of 2010, there were some positive trends in social-economic development of the republic, provided by recovery of the world economy and accelerated recovery of the country's economy after considerable crisis of 2009. As per results of the first quarter of 2010, the real GDP (Gross Domestic Product) growth constituted 116.4%, provided by high growth rates in industry (178.8%) and construction (135.1%) sectors.

Events in April and June in the south of the republic, as well as consequences of political instability in the country, had negative influence on the country's economy and population's living standards. Many enterprises of small and medium business were affected; considerable losses were suffered by the sector of tourism and services; business activity in the country considerably decreased.

In general, inflow of direct foreign investments decreased almost in two times, which testifies about negative expectations of foreign investors. Due to unfavorable social-and-political situation, business activity considerably decreased; implementation of some large projects was suspended, including in the mining industry – individual large enterprises were idle, number of working places decreased. In 2010, the number of unemployed people increased by 3% and constituted 63.4 thousand people.

Growth of prices for basic food products and goods provided decrease in living standards, especially of socially vulnerable segments of the population.

Closing of borders with neighboring countries led to practical termination of export of agricultural production; sewing and processing enterprises considerably suffered.

Owing to these shocks as per results of 2010 and according to preliminary evaluation, the GDP volume amounted to 212.2 billion KGS; at that the GDP volume decrease constituted 1.4% (98.6%). Excluding enterprises developing the gold mining deposit "Kumtor", decrease in the GDP volume made 2.1% (97.9%).

In the reporting period the main factors which had negative influence on the economic growth indices, were as follows:

- tension of the social-economic situation, especially in southern regions of the country;
- reduction of the aggregate demand;
- direct destruction and downtime of enterprises caused by April and June events in the south of the republic;
- unfavorable weather conditions (rainy spring, mudflows and torrid summer);
- difficulties with supplies and growth of prices for fuels and lubricants;
- closing of borders with Kazakhstan and Uzbekistan;

According to the National Statistics Committees of the Kyrgyz Republic, the foreign trade turnover constituted 5265.5 million USD in 2010; and in comparison with 2009, it increased by 11.7 percent, including import increase by 21.2% and export increase by 6.5%. Thus, the trade balance developed negative and constituted (-) 1209.9 million USD.

Price shocks on the world commodity and raw materials markets as well as internal political events and their consequences had influence on the inflation burst and economic recession in 2010. As per results of 2010, inflation constituted 19.2%. Main factors, which had influence on the inflation processes in the past year, were the increase in prices for food products and soft beverages, which appreciated by 27.0%, including vegetable oils – by 47.3%, flour – by 42.6%, fresh meat – by 32.7%, bread – by 22.2%, sugar – by 22.5%. Prices for alcoholic beverages and tobacco products increased by 12.9%.

A number of inflation bursts, which occurred in several previous years, form high inflationary expectations among economic agents and have negative influence on social situation of the country's population.

Considering the above-mentioned facts as well as for the purpose of maintenance and support of economic stability in various sectors of the economy, the Government of the Kyrgyz Republic and the National Bank of the Kyrgyz Republic developed the Joint Statement of the Government of the Kyrgyz Republic and the National Bank of the Kyrgyz Republic on Economic Policy for 2011.

1. Macro-economic policy

Main aim of implementation of the macro-economic policy for 2011 consists in recovery of economic growth rates, achievement and maintenance of price stability, creation of sufficient conditions for economic and social development in the mid-term perspective.

Macro-economic policy for 2011 will be aimed at solution of the following major objectives:

- provision of the real GDP growth rate no less than 6.3%;
- reduction of inflation to 10% on average within three years;
- maintenance of the budget deficit within the range of 8.7% to GDP;
- growth of the average monthly salary rate by 18.0%;
- growth of the industrial sector production by 4.2¹%;
- growth of agricultural production by 4,0%;
- growth of the construction sector by 27.3%;
- growth of the services sector at least by 5.4%;
- complete and timely execution of all social government guarantees.

Difficult macro-economic situation in the country, considerable growth of the budget expenses and deficit of the state budget as well as rising price trends on the world commodity and raw materials markets create pre-conditions for maintenance of high inflationary background in 2011. Government and the National Bank of the Kyrgyz Republic realize that in these conditions factual value of inflation may be higher than the specified inflationary orienting point. A complex of measures aimed at moderation of the prices growth rate will be accepted in 2011, which would enable to decrease inflation to 10% on average within three years.

2. Monetary policy

Achievement and maintenance of prices stability in the mid-term period is still the main aim of the monetary policy; at the same time, the primary objective consists in reduction of high inflationary expectations.

Regulation of the monetary base will be performed for limitation of the monetary component of inflation with the use of standard instruments of the monetary policy, increasing the operations on excess liquidity sterilization in reply to acceleration of the budget expenses. National Bank of the Kyrgyz Republic will continue money supply through non-standard monetary mechanism in the form of activity of the Special Fund for Banks Refinancing. However,

¹ Growth rates are provided without goods made on commission.

after forthcoming of stable signs of the economy recovery, utilization of this mechanism will be limited. Herewith, activity of the National Bank of the Kyrgyz Republic will be concentrated on price stabilization, tightening the monetary policy in case of necessity.

Within the framework of the floating exchange rate policy, the practice of currency interventions, aimed at flexible adjustment of the exchange rate and preventing its sharp fluctuations, will be maintained. In case of increase in pressure on the exchange rate, the National Bank of the Kyrgyz Republic will avoid considerable reduction of international reserves and provide tightening of the monetary policy.

Considering importance of coordination and efficiency of activities of the Government and the National Bank of the Kyrgyz Republic for the purpose of macro-economic stability provision, special attention will be paid to activity of inter-departmental coordinating committee of the Ministry of Economic Regulation of the Kyrgyz Republic, Ministry of Finance of the Kyrgyz Republic and National Bank of the Kyrgyz Republic.

For the purpose of maintenance of stability and integrity of the banking system, the work on strengthening of banking supervision and improvement of legislation with regard to reinforcement of banking supervision and regulation will be performed. Currently, the Mid-term Strategy for Development of Micro-Financing in the Kyrgyz Republic for the Period of 2011-2015 is elaborated. The work on elaboration of the Strategy for the Banking System Development for the Period of 2011-2013 has been started.

Reformation of the payment system will promote development of new and convenient mechanisms of payments settlement for the population and economic agents through accounts in commercial banks. It is planned to transfer central and other government authorities as well as local authorities of the Kyrgyz Republic to collection and settlement of all types of payments, receipt of salaries and other payments through accounts and cash departments of commercial banks and division of the State Enterprise “Kyrgyz Pochtasy”. It is also planned to develop infrastructure for acceptance and servicing of payments with the use of modern banking innovation services and technologies (Internet banking, mobile banking, pre-paid cards and other services and technologies); the systems of settlement with the use of banking payment cards will be introduced all over the republic. In order to reduce financial risks in the payment system, the measures on supervision and control over the banking system will be strengthened.

3. Fiscal policy

In 2011, the fiscal policy will be aimed at provision of increase in tax and customs revenues to the budget, improvement of tax administration system and legalization of non-formal sector of the economy.

For the purpose of increase in tax and customs revenues to the budget, it is planned to perform the following measures:

- arrangement of analysis, production, import, export and consumption in the view of economy branches, entities and trading positions as well as sums of paid taxes and other parameters;
- arrangement of the analysis of macro-economic indices changes and their influence on the budget revenue both for the current year and for next years;
- improvement of the tax and customs administration systems, achievement of efficient balance of rights of entrepreneurs and supervisory authorities, reduction of corruption, provision of transparency and increase in efficiency of their activities;
- maximum exclusion of direct contacts of taxpayers and representatives of the tax service through improvement of the Single Window system during delivery of tax reports;
- expansion of coverage with the electronic submission of tax reports;
- improvement of the patent taxation system.

Legalization of non-formal sector of the economy, which has negative impact on tax and social base, will be provided with the help of the following measures:

- improvement of the mechanism of cash registers usage;

- expansion of coverage with the field tax inspections on the basis of the risk management mechanism;
- performance of analysis and development of measures aimed at legalization of individual sectors such as fuels and lubricants, mobile communication, production of alcohol production, tobacco products etc;
- continuation of work on modernization and automation of the fiscal agencies activity.

Customs policy in 2011 will be aimed at promotion of external trade and stimulation of key export-oriented trends of the economy, simplification of custom inspection procedures on borders and strengthening of custom payments administration.

The following measures will be taken for implementation of the above-mentioned objectives in 2011:

- modernization of the custom and near-custom infrastructure including introduction of modern information technologies;
- activation of work with persistent non-payers of taxes by means of performance of operational-search activities aimed at detection and prevention of contraband;
- introduction of the Single Window principle in the sphere of external trade for arrangement of joint control by the departments responsible for transportation, radiation, veterinary, sanitary, phyto-sanitary and other types of control;
- improvement of the custom administration system;

4. Budgetary policy

The policy of the government expenses in 2011 will be aimed at complete and timely financing of the state social quarantines, creation of favorable conditions for economic growth and improvement of efficiency in utilization of the government resources with introduction of the system for their economic evaluation.

Expenses will be incurred under rigid control and in strict correspondence with the entering income in order to provide progress of gradual reduction of the budget deficit by 2013.

Special attention in the budgetary policy will be paid to the following directions:

- improvement of efficiency in utilization of the government resources;
- introduction of the result-oriented approach during financing of institutions;
- introduction of the system for evaluation of economic efficiency of the budgetary resources utilization;
- strengthening of social payments addressness;
- improvement of the budgetary legislation;

Moreover, in 2011, the work on improvement of the format and procedures for development of the Mid-term Forecast of the Budget, determining the budget policy of the country, will be continued. Introduction of the program format of expenses presentation, enabling to increase efficiency and transparency of the budgetary funds utilization, will be continued.

5. Government debt

Management of the government debt will be performed with regard to gradual decrease in the debt burden, including due to reduction of external borrowings at simultaneous observation of the established repayment schedule for the external debt. Within the framework of new Strategy for Management of the Kyrgyz Republic Government Debt in the Mid-term Perspective as well as for the purpose of achievement of the government debt stable level, optimization of its structure and creation conditions for efficient management of the government debt, it is supposed the following:

- reduction of the government external debt burden;
- timely servicing of the government debt;
- consideration of the possibility for further restructuring of the external debt;

- performance of conversion operations with bilateral creditors;
- attraction of concessional external credits with grant-element of at least 35 percent for efficient and economically sound projects;
- expansion of the range of government securities holders by means of development of primary and secondary markets of government securities;
- increase in the volume of internal borrowings by means of issuance and allocation of government securities;
- diversification of the government securities portfolio;
- introduction of the risk management practice.

6. Real sector development

6.1. Industry

Development of the industrial sector in 2011 will be performed against gradual recovery of social-political situation in the country alongside with reactivation of activity of many idle enterprises, increase in the consumer demand as well as increase in the volume of agricultural production supply to enterprises of the processing industry due to accepted measures on support of agricultural manufacturers and improvement of investment activity.

In 2011, production growth in the industry is forecasted by 4.2% mainly due to increase in the production volumes of food and processing sectors. In 2011, for the purpose of achievement of stable functioning in the sphere of processing sector, competitive recovery of domestic production and increase in export supplies, it is planned to solve the following objectives:

- stabilization of activity of economic-forming industries and large enterprises with determination of 20 largest economic-forming enterprises and development of measures for solution of problematic issues, aimed at development of production, creation of conditions for improvement of their financial situation and increase in assignments to the budget;
- attraction of financial resources for support of small and medium business;
- creation of conditions for recovery of business environment in the southern region;
- expansion of purchases of domestic manufacturers products;
- determination of further policy in the sphere of food and processing sectors with elaboration of the Strategy for Development of Food and Processing Sectors for the Mid-term Period for the purpose of competitiveness provision, more total processing of agricultural production and development of food production export.

Growth of production volumes will be provided by further activities on stabilization and development of the food industry, such as application of regulative measures on priority development of enterprises and branches, oriented at completeness and profoundness of local raw materials processing and production of goods with high added value, development and execution of regulatory legal acts with regard to creation and functioning of clusters in the food industry, enterprises of textile and sewing industry due to gradual increase in production volumes of operating enterprises: JSC “Kasiet”², LLC “Rozkvit”³, Bishkek Kenaf Factory, JSC “Ilbirs”, LLC “Kara-Balta Kilem” as well as restoration of idle enterprises of the chemical industry and stabilization of activity of the LLC “Kyrgyz Chemical Metallurgical Plant - Astra” and Haidarkan Mercury Stock Company.

6.2. Agriculture

Agriculture will still be of high priority because this sector involves about 14% of the total population; moreover, 65% of the population lives in rural areas and their living standards remain low at the present time. In 2011, the real growth rate is expected at the level of 104.0%. This increase will be provided due to expansion of cultivation areas for high-yield winter crops of grain spiked plants, cotton plants, tobacco and sugar beat. Moreover, concessional agricultural credits

² JSC – Joint Stock Company.

³ LLC – Limited Liability Company.

for the total sum of 1 billion KGS will be provided for support of agricultural manufacturers of grain crops, sugar beat, cotton plants and oil-bearing crops.

As a result, the expected growth rate will be achieved by solution of the following objectives: optimization of the cultivation areas structure, development of seed-production farms, introduction of scientific achievements and advanced experience, improvement of provision with material-and-technical resources, renewal of vehicle-tractor force, improvement of animals gene pool and works on reproduction of livestock, rational utilization of pastures, development of maintenance departments in rural areas, improvement of qualification of farmers and peasants.

It is planned to enhance state support of agriculture, to improve and develop cooperation between manufacturing and processing of agricultural production, to create favorable conditions for export of agricultural raw materials, to establish close cooperation with international organizations, to provide assistance to the agriculture sector as well as to attract domestic and foreign direct investments.

6.3. Construction

Priority directions of the construction sector will include construction of individual housing, restoration of Osh and Jalal-Abad cities and rayons which suffered in the course of June events; objects of the traffic artery (automobile roads Osh-Sarytash-Irkeshtam, automobile roads of the Southern Regional Corridor: Bishkek-Naryn-Torugart, Taraz-Talas-Suusamyr, Osh-Isfana, Sarytash-Karamyk, Karakol-Tyup-Kegen); objects of the energy sector (construction and reconstruction of hydropower stations).

Despite worsening of the investment climate owing to political instability, in 2011 it is planned to increase the volumes of capital investments due to completion of construction of the high-voltage line 220 kW “Aigultash-Samat” with reconstruction of the electric power substation 110 kW “Aigultash-Samat” as well as continuation of the project implementation “Experimental engineering and construction of the micro-district – 15 Dzhal Artis” in Bishkek city. Moreover, in order to reconstruct infrastructure of Osh and Jalal-Abad cities and rayons which suffered in the course of June events, the Kyrgyz Republic Government issued the resolution No.164 “On measures for provision of the government assistance to suffered people with regard to construction and reconstruction of objects on the territory of Osh city, Osh and Jalal-Abad oblasts”, dated August 17, 2010, which approved preliminary list of objects, subject to reconstruction and construction, of the State Directorate for Reconstruction and Development of Osh and Jalal-Abad cities. This list stipulates construction of about 207 thousand square meters for housing in 2010-2011.

7. Investment policy

Considerable efforts were taken in recent years for improvement of the investment climate in the city. However after events of 2010, investment attractiveness of the country sharply went down.

Nowadays, there is a number of problems which prevent inflow of direct investments: incompliance of acting legislation, regulating investment activity, with the modern requirements; absence of institutional and regulatory framework, required for development of transportation and energy infrastructures of the country; unpredictability of changes in the economic policy of the country; absence of efficient institutional structure for attraction and promotion of investments; high level of corruption.

For provision of increase in the direct foreign investments inflow, it is necessary to create institutional basis for the economy growth and attraction of investments, to introduce the mechanisms for the state-private partnership and to create the institutional basis for solution of infrastructure problems as well as to establish the system of investment preferences at the legislative level.

For the purpose of improvement of the investment climate and provision of sustainable growth of direct foreign investments inflow into the country, in 2011 it is planned to elaborate the “Strategy for attraction and promotion of direct foreign investments for the period of 2012-2014” as well as to introduce changes into the Kyrgyz Republic Law “On the state-private partnership” and to create the institute of development and investment funds in cooperation with other countries. Also, it is planned to introduce the simplified procedure for issuance of investment visas for foreign citizens.

8. Social policy

Mainly poor and vulnerable segments of the population were affected by negative influence of crisis events. In these conditions, social policy of the state plays a very important role with regard to provision of social security and assistance to the country’s population.

In 2011, major measures in the social sphere will be aimed at provision of social guarantees in full, including provision of assistance to socially vulnerable groups of the population (disabled people, pensioners, low-income families, workers of the social sphere).

Key measures of the social policy will be aimed at reduction of the poverty rate and enhancement of the population’s access to high-quality social services. For these purposes reforms in all spheres of social development will be continued.

Activity of the government authorities will be enhanced in the social sphere with regard to reduction of the prices growth influence on low-income groups of the population due to targeted social assistance.

Social policy will be implemented by means of access of the poor population to the system of social protection and social insurance. Special attention will be paid to provision of social protection to needy population, including low-income groups and socially vulnerable groups.

The following activities will be performed for improvement of living standards of socially vulnerable groups of the population:

- improvement of the methodology for determination of the population’s needs in the state support;
- complete and timely financing of social guarantees of the state;
- improvement of efficiency of the social protection and social insurance system;
- development of the system for provision of social services;
- provision of financial stability of the pension system;
- increase in the average size of pensions;
- reformation of wage conditions for the budget sphere employees.

As for the sphere of the population’s employment, basic measures will be aimed at reduction of the unemployment rate and maximum attraction of unemployed people into active participation in the employment policy (public paid works, micro-crediting and vocational training).

Conclusion

Structural weakness and dependence of the country’s economy on prices of the world commodity and raw materials markets, incompleteness of structural changes, aimed at reformation of the real and foreign trade sectors of the economy for the purpose of increase in the domestic production potential, improvement of the balance between demand and supply of goods and services. may considerably change the conditions of the monetary program as well as the monetary indices and require adjustment of evaluations of macro-economic indices including inflation valuation.