

## Economic Forecast for Member States of Eurasian Economic Union for 2016–2018<sup>1</sup>

Risks of a further slowdown in the world economy and international trade due to the volatility on financial markets, low commodity prices, and persistent deflationary pressures remain high. The recovery of advanced economies is still tepid despite strong impetus from monetary and fiscal policies, and low commodity prices—which may be a result of continuing deceleration of economic growth in developing countries. Other factors of weak recovery include development of a negative feedback between financial and real sectors, and tightening of credit conditions.

The renewed reduction in the oil prices in the fourth quarter of 2015 postponed growth recovery of EAEU's economies trapped in recession, while EAEU countries retaining positive economic growth faced the risk of its further deceleration. Though the intensity of the terms-of-trade shock has decreased, consumer confidence and private investment will experience a further decline pertaining to uncertain prospects for improvement in macroeconomic fundamentals. In a low commodity prices environment, space for fiscal stimulus is limited by already high budget deficits and government debt levels, as well as quick reserve depletion and falling tax receipts due to the further deterioration in economic activity. Declining inflation, attenuation of external shocks, and stabilisation of national currencies open a window for easing of monetary policy, but on the other hand, a spike in country risk premia and persistent capital outflows from emerging markets reduce the space for fiscal stimulus. A protracted period of the recovery of regional economies is expected due to weak domestic and external demand, deterioration of labour market conditions, continuing tight monetary policy and weakening support from fiscal policy in most countries.

### Economic Forecast for EAEU<sup>2</sup>

Year	Real GDP (annual percentage change)		CPI (annual percentage change)		Memorandum URALS oil price, USD/bbl (annual average)	
	Forecast (from 2016)	Difference*, p.p	Forecast (from 2016)	Difference*, p.p	Forecast (from 2016)	Difference*, USD
2015	–3.1	0.1	14.5	0.1	51.3	–0.9
2016	–1.4	–1.6	8.9	0.5	34.5	–17.9
2017	0.9	–0.3	6.3	0.6	41.6	–14.9
2018	1.5	0.2	4.8	–0.4	46.0	–14.1

\* Difference—here and later—from Economic Forecast for Member States of Eurasian Economic Union for 2015–2018 prepared in the fourth quarter of 2015 and available on the website of Eurasian Economic Commission ([www.eurasiancommission.org](http://www.eurasiancommission.org)).

<sup>1</sup> The forecast is prepared by Eurasian Economic Commission and Eurasian Development Bank in March 2016 (latest data point is March 18, 2016).

<sup>2</sup> Weighted average for which the weights used are equal to real GDP (PPP) share in total EAEU GDP.

## The Republic of Armenia

Amid further growth deceleration in most economies in the region, economic growth in Armenia remained positive, albeit slower than in the past. Terms-of-trade deterioration, deepening recession in trading partners' economies, and decline in remittances continue to exert negative effect on economic growth of Armenia. Credit activity remains subdued, with non-financial sector and households deleveraging. Decline in real disposable income as well as deteriorating labour market conditions led to a significant reduction of private sector consumption. Tightening of credit conditions, high interest rates, and capital outflow suppressed investment activity.

Domestic demand decline, which intensified in the second half of 2015, has led to GDP growth slowdown. Against this background, increase of output in mining industry and net exports have had a positive contribution to GDP growth. Increase in export volumes and decrease of import volumes have resulted in a significant improvement of current account balance. Capital inflows on general government operations have allowed foreign-exchange reserves to increase, provided more room for fiscal stimulus and mitigated overall negative effects from external conditions.

Deflationary external conditions in the aftermath of the commodity prices plunge, good agricultural harvest, appreciation of the real effective exchange rate, as well as a weak domestic demand and high real interest rates maintained by monetary authority, have led to a quick inflation decline.

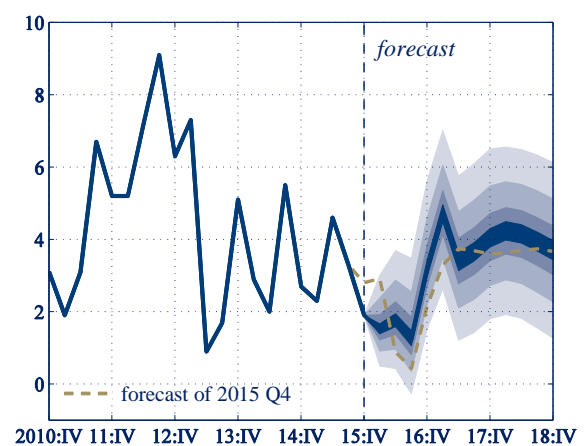
As a result of deflationary pressures coming from external and domestic factors at the end of 2015–beginning of 2016 Armenian CPI growth turned negative (–1.7% y-o-y). In the fourth quarter of 2015 headline inflation was 1.1%, which is lower than the inflation target confidence band of the Central Bank (4% 0+/- 1.5 p.p.).

Henceforth, cyclical factors will have negative effect on GDP growth pertaining to deepening recessionary trends in economies of trading partners, lending slow recovery path and capital inflows decrease.

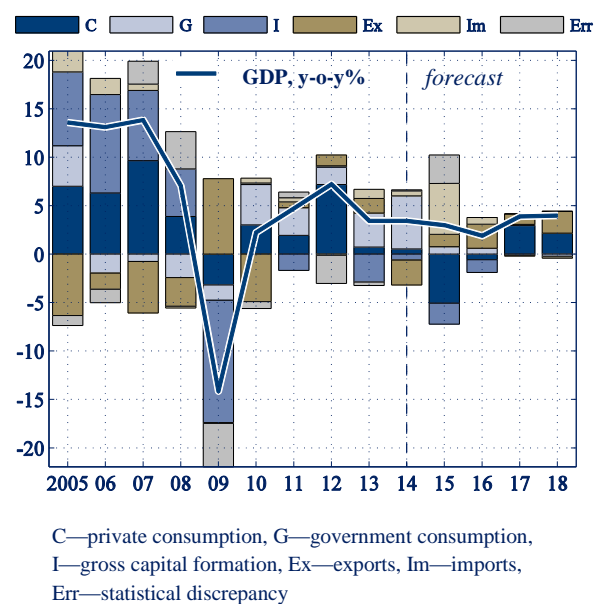
Economic Forecast for the Republic of Armenia

Year	Real GDP (annual percentage change)		CPI (annual percentage change)	
	Forecast (from 2016)	Difference, p.p.	Forecast (from 2016)	Difference, p.p.
2015	3.0	–0.4	3.8	–0.3
2016	1.9	0.3	0.4	–2.7
2017	3.9	0.3	2.6	–1.2
2018	4.0	0.3	3.7	–0.3

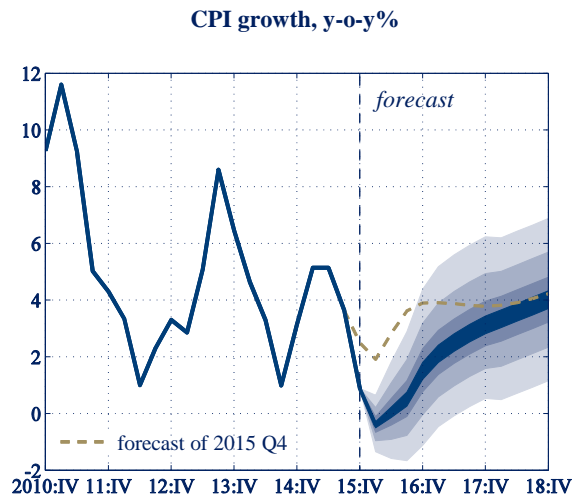
Real GDP growth, y-o-y%



Real GDP growth contributions, p.p.



Despite real wages growth in the public and private sectors, recession in Russia will suppress domestic demand in Armenia due to factor income and remittances decline, and unemployment increase. Mining industry and exports will remain key drivers of economic growth in 2016. Gradual decrease in the refinancing rate (from 10.5% to 8.5% in July 2015–February 2016) is aimed to support domestic demand, which, along with the government measures to stimulate investment, is intended to improve credit access and support broad-based sustainable economic growth in the face of moderate fiscal



consolidation (government budget deficit is planned to decrease to 3.5% of GDP in 2016 and 2.0% in 2017–2018 from 4.8% in 2015). GDP growth rate is expected to decline over the year. Nevertheless, short-term indicators point out strong growth of economic activity at the beginning of 2016. Forecast of GDP growth in 2016 has been revised upwards to 1.9% from 1.6% compared with the previous estimate. In the medium term economic growth will gradually pickup to 3.9% in 2017 and 4.0% in 2018, alongside with the recovery of domestic demand and implementation of infrastructure investment projects.

Consumer price index dynamics has been affected by a prolonged decline of energy and food prices, as well as an appreciation of the real effective exchange rate. Looking forward, inflation is expected to slightly increase but will remain below the inflation target confidence band of the Central Bank over the course of 2016. In the absence of new shocks, annual CPI growth is forecast to hover around 0.4% in 2016. As a result of domestic demand recovery, real effective exchange rate gradual depreciation and imported goods prices increase, inflation is expected to reach 2.6% and 3.7% in 2017–2018.

## The Republic of Belarus

According to preliminary data, Belarus GDP contracted by 3.9% in 2015 due to a significant decline of demand from major trading partners and limited space for stimulating macroeconomic policies. Monetary and fiscal policy tightening, as well as the quasis-fiscal government operations reduction, contributed to the decline of inflationary pressures.

Transition to the monetary targeting regime and flexible exchange rate at the beginning of 2015 facilitated the return of the real effective exchange rate to its equilibrium level. This helped to restore exports competitiveness, decreased inflation expectations and reduced current account deficit. Meanwhile, devaluation expectations remained elevated leading to capital flight and pushing up real interest rate. Tight monetary policy and shrinking domestic demand brought inflation down to 12% in 2015.

According to preliminary estimate for the first quarter of 2016, CPI reached 6% year-to-date, an uptick shift caused by a hike in utility tariffs. However, weak domestic demand is expected to pull inflation down over the year. Inflation is expected to reach 12.8% in 2016, thereafter declining to 10.4% in 2017 and 8% in 2018.

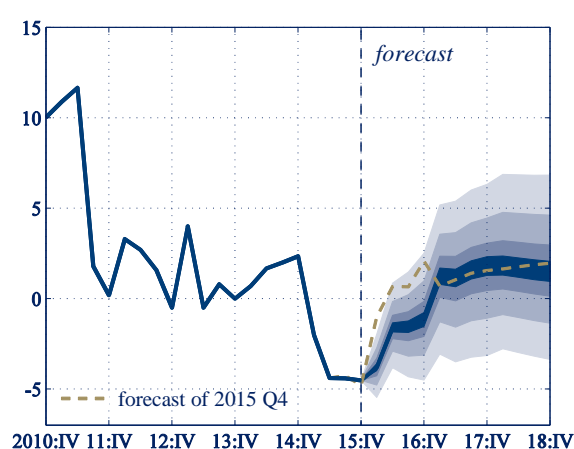
The forecast of economic activity for Belarus in 2016 has been revised down due to industrial output plunge by 5.6% y-o-y in January–February of the current year and expected further Russian GDP contraction in 2016.

High lending real interest rates negatively affect private sector investment and household consumption. Revenue shortfall and limited access to foreign and domestic borrowing, constrain fiscal space for additional budget spending to support economic activity. The government is expected to maintain budget surplus over the medium term to service its domestic and external obligations. Under these circumstances, GDP continued to decline in January–February of the current year by 4% y-o-y. Overall GDP is expected to fall by 2% this year with a moderate growth up to 1.5–1.6% in subsequent years. Recovery from the recession

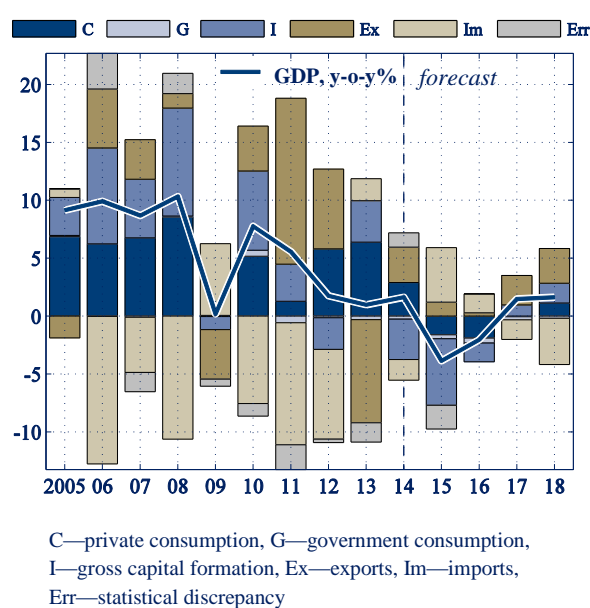
Economic Forecast for the Republic of Belarus

Year	Real GDP (annual percentage change)		CPI (annual percentage change)	
	Forecast (from 2016)	Difference, p.p.	Forecast (from 2016)	Difference, p.p.
2015	-3.9	0.1	13.6	-0.3
2016	-2.0	-2.6	12.8	0.8
2017	1.5	0.3	10.4	1.7
2018	1.6	-0.2	8.0	0.8

Real GDP growth, y-o-y%

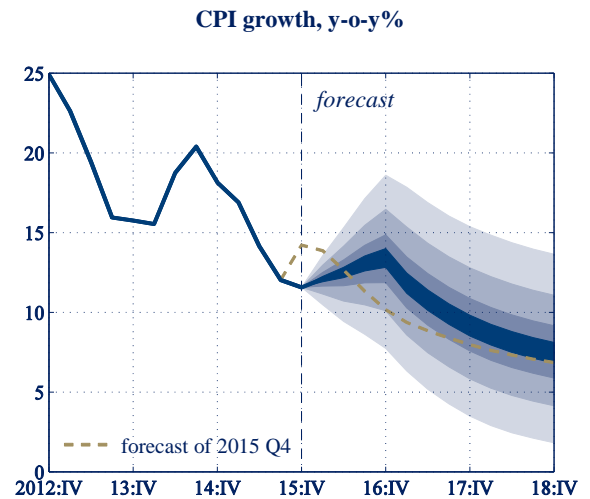


Real GDP growth contributions, p.p.



will still be hampered by unfavorable external conditions. As potential growth showed a sharp slowdown in recent years, there is an acute risk of recession turning into a prolonged stagnation. On the other hand, package of measures adopted by the government in January 2016 is designed to mitigate bottlenecks in Belarus economy. The government will be focused on economic effectiveness improvement and sound macroeconomic policies.

With inflation projected to be slowing down in 2016, the monetary authorities are expected to cut gradually nominal interest rates to support economic activity.



## The Republic of Kazakhstan

Preliminary data show that economic growth in Kazakhstan slowed to 1.2% in 2015 from 4.1% in 2014 due to deteriorating terms-of-trade caused by a continuing decline in oil and metals prices, weaker external demand and faltering domestic demand. The latter is a result of tight financial conditions and a contraction in household lending. The tenge devaluation in the second half of 2015 reduced purchasing power of households due to dwindling real wages and switched consumption from imports to domestic goods, providing support to local producers. As a result, GDP growth picked up to 1.2% in the fourth quarter of 2015 after decelerating to 0.4% in the third quarter of 2015.

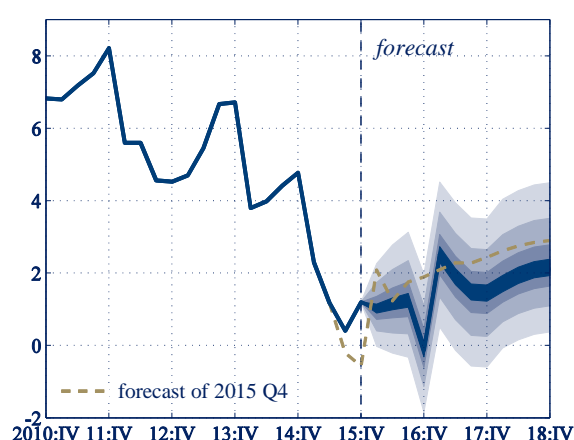
Positive impulse of devaluation for manufacturing is expected to last over the course of this year. Pensions increase by 9%, as well as social benefits and nominal wages in the public sector increase by 20–40% at the beginning of 2016, will be another factor contributing to the domestic demand growth. Aside from the continuing implementation of the medium-term infrastructure programme ‘Nurly Zhol’, the government decided to extend fiscal stimulus package by 2.8% of GDP as part of the Plan of prompt anti-crisis measures. Current estimates suggest that it will add 0.3–0.5 p.p. to GDP growth in 2016. However, expected oil production decline and low oil prices over the forecast horizon will reduce export income and domestic demand further. GDP growth is projected to decelerate to 0.8% in 2016.

The tenge depreciation in the second half of 2015–beginning of 2016 alongside transition to a floating exchange rate regime led to a spike in imported goods prices—especially of non-food. As a result, inflation reached 11.9% in the fourth quarter of 2015. Exchange rate pass-through effect from devaluation will impair price stability over the first half of 2016. In the context of relatively low price change in the first half of 2015, inflation will peak at 16.3% y-o-y in the second quarter of 2016. Fading inflationary effect of the tenge depreciation and weak domestic demand will bring CPI growth down to 8.6% in the fourth quarter of 2016.

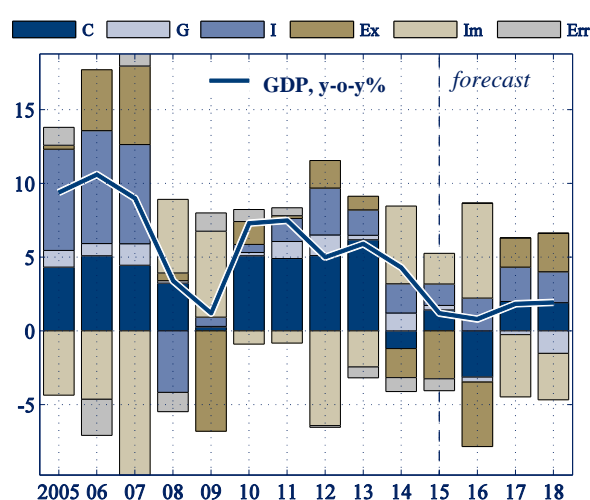
Economic Forecast for the Republic of Kazakhstan

Year	Real GDP (annual percentage change)		CPI (annual percentage change)	
	Forecast (from 2016)	Difference, p.p.	Forecast (from 2016)	Difference, p.p.
2015	1.2	0.5	6.6	-0.2
2016	0.8	-0.9	14.0	-2.5
2017	1.8	-0.5	6.0	-0.4
2018	1.9	-0.9	6.2	-0.1

Real GDP growth, y-o-y%



Real GDP growth contributions, p.p.



C—private consumption, G—government consumption,  
I—gross capital formation, Ex—exports, Im—imports,  
Err—statistical discrepancy

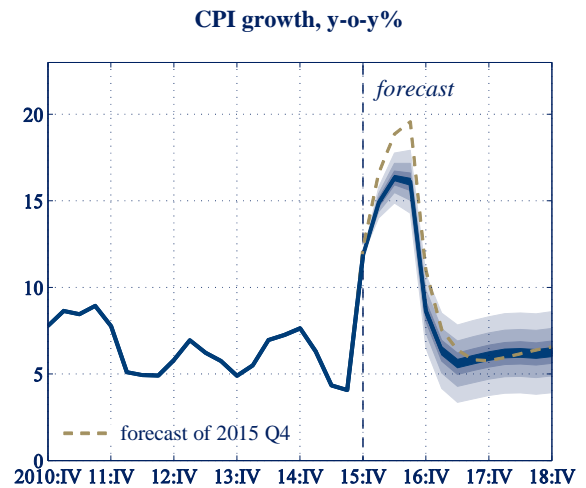


In February-March 2016, volatility of exchange rate and money market rates subsided, and devaluation expectations weakened owing to the base rate increase by the NBRK to 17% in February 2016, the renewal of access to standing facilities, and oil price stabilisation.

The necessity to increase tenge assets attractiveness in the face of high level of dollarisation, elevated country-risk premium and inflationary expectations will push up money market rates during 2016.

The window for monetary policy easing will be limited by capital outflow a surged risk premium compared with 2010–2014 and persistence of the recent terms-of-trade shock.

Recovering external demand from Russia and European Union, gradual increase of oil prices, as well as the planned start of oil production on ‘Kashagan’ oil field will support exports and household consumption growth, which are expected to turn positive in 2017–2018. Infrastructure investment under projects supported by the government, and implementation of the State Program of Industrial and Innovative Development for 2015–2019 will lift medium-term growth potential. At the same time, low oil prices around 30–50 USD/bbl range for an extended period will narrow space for a fiscal stimulus. Thus, budget consolidation is expected to speed up over the medium term, while GDP growth will reach 1.8–1.9% in 2017–2018. Negative output gap, relatively low level of food prices on the world markets, as well as exchange rate stabilisation, will contribute to a CPI inflation decline, which is expected to slide down to 6.0–6.2% in 2017–2018.



## The Kyrgyz Republic

Economic growth in Kyrgyzstan slowed from 6.8% y-o-y in the first 6 months of 2015 to 3.5% in 2015, the main reason being a smoother distribution of gold production over the course of 2015 compared with previous periods, when the bulk of yearly gold production was accounted for in the fourth quarter. Gold mining on ‘Kumtor’ deposit continued to decline in 2015—by 8.3% (5.4% decline in 2014). Services remained key growth driver. In addition, agriculture positively contributed to the GDP growth in 2015, its volume of production increased by 6.2% (following 0.5% decline in 2014).

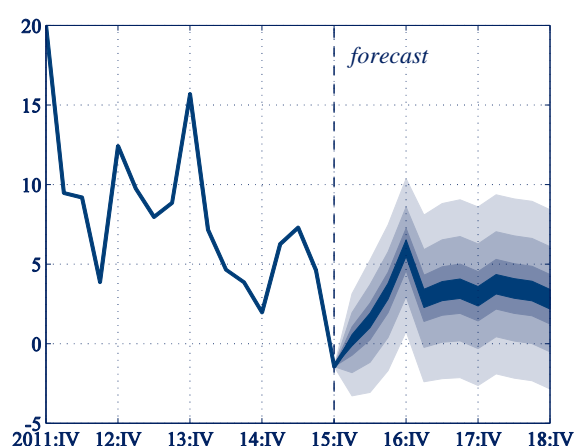
Growth deceleration in China and Kazakhstan, recession in Russia reflect external demand deterioration of Kyrgyz major non-commodity export destinations. Negative output dynamics in Russia and devaluation of the Russian ruble led to the plunge of remittances in dollar terms by 25.8% in 2015, which in turn caused a decline in household consumption and private investment. Weak demand determined growth deceleration in the construction industry—one of the main non-commodity growth drivers of Kyrgyzstan in 2012–2014. Trading partners’ exchange rates weakness, as well as gold production and price decline, led the som to depreciate against the US dollar almost 30% in 2015. To counteract devaluation-inflation spiral development, the National Bank increased its deposit rate by 2 p.p. in September 2015. Tighter financial conditions, weak domestic demand, deflationary pressures from the side of world food and energy prices led to inflation decline from 10.5% y-o-y in December 2014 to 3.4% y-o-y in December 2015.

Despite the recession in the Russian economy, remittances in the Russian rubles increased by 13.5% in 2015 as a result of the number of migrant workers from Kyrgyzstan increase by 1.6%<sup>3</sup>. In the aftermath of the ratification of the Treaty of accession of the Kyrgyz Republic to the EAEU in August 2015 and easing of Russian migration policies towards Kyrgyz workers, the number of migrants from

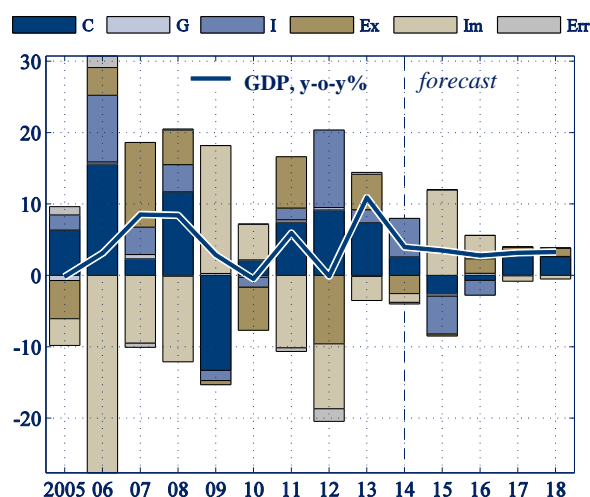
Economic Forecast for the Kyrgyz Republic

Year	Real GDP (annual percentage change)		CPI (annual percentage change)	
	Forecast (from 2016)	Difference, p.p.	Forecast (from 2016)	Difference, p.p.
2015.	3.5	—	6.5	—
2016	2.8	—	2.9	—
2017	3.2	—	4.5	—
2018	3.3	—	4.9	—

Real GDP growth, y-o-y%



Real GDP growth contributions, p.p.



C—private consumption, G—government consumption,  
I—gross capital formation, Ex—exports, Im—imports,  
Err—statistical discrepancy

<sup>3</sup> January 2015 over January 2014, source: Federal Migration Service of Russia.

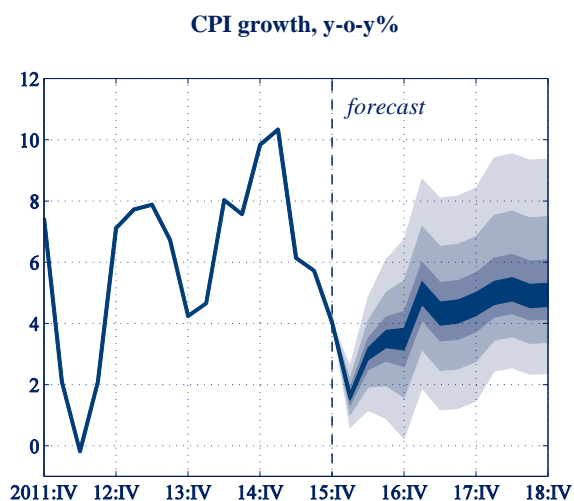


Kyrgyzstan grew by 6.7%<sup>4</sup> from August 2015 to January 2016. Moreover, the number of unemployed workers in the Kyrgyz economy fell down as well. Taking into account continuing recession in Russia in 2016, the main negative effect from the remittances decline on domestic demand will take hold in 2016–2017. Due to the blurred medium term prospects of the Russian potential growth recovery, remittances flows are estimated to reach \$1.2 bn by 2018, which will be much lower compared with the peak of \$1.9 bn in 2013.

Amid a further export income drop, declining remittances inflow, trading partners' currencies depreciation in 2015, the real effective exchange rate of the som remained overvalued during most of the year. The som depreciation in the fourth quarter of 2015 helped to mitigate external imbalances and increased price competitiveness of the Kyrgyz private sector. Consequently, a partial switch of household demand to local producers' goods, as well as a boost to non-commodity exports, are expected in 2016. The government-planned consolidated budget deficit increase up to 4.4% and 3.7% in 2016 and 2017 respectively will provide additional impulse to domestic demand.

In accordance with the projections of Kumtor Gold Company and the Ministry of Economy of the Kyrgyz Republic, gold production is expected to increase by 2.1% in 2016. The increase of gold mining will be sustained by the start of production on new deposits, while the share of 'Kumtor' mine will continue to decline. Gold production is projected to decrease by 7.3% in 2017 and increase by 0.7% in 2018. Taking into account the above mentioned factors and expected gold production patterns, GDP growth in Kyrgyzstan can reach 2.8% in 2016 and 3.2–3.3% in 2017–2018.

According to the government plans, electricity and heating energy tariffs will be increased by 20–30%. Nevertheless, inflation is expected to be staying on the lower margin of the inflation target band of the National Bank of 5–7%<sup>5</sup> in 2016–2018 as the result of tight monetary conditions, as well as weak domestic demand, and low world food and energy prices.



<sup>4</sup> On the other hand, the number of migrants from Uzbekistan and Tajikistan—top labour migrant donors among CIS countries—dropped by 18.6% and 13.7% over the same period, source: Federal Migration Service of Russia.

<sup>5</sup> Medium-term quantitative target of the National Bank of the Kyrgyz Republic.

## The Russian Federation

Negative trends in the Russian economy—following abrupt drop of oil prices, prolongation of Western sanctions and Russian counter-sanctions—alleviated at the beginning of 2016, with signs of economy gradually adapting to new external environment. At the same time, domestic demand remains weak reflecting the decline of real household income and private investment. This has led to a downward revision in medium term inflation projections. According to the Rosstat preliminary data, real GDP contracted by 3.7% in 2015. After a significant plunge in the second quarter output dynamics appeared to stabilise in the third and fourth quarters.

For the first time since January 2015 industrial production grew by 1% y-o-y in January 2016. Capacity utilisation remains on the same level and upward pressures on rising unemployment are contained. Capital outflow from the private sector continued due to debt repayments and limited access of banking and corporate sectors to international financial markets. Persistently low commodity prices in January–February 2016, as well as deterioration of economic growth prospects in developing countries exacerbate risks for a continuing recession in the Russian economy over the course of 2016. Moreover, unfavorable external conditions will have a negative impact on medium- and long-term economic prospects by constraining potential growth.

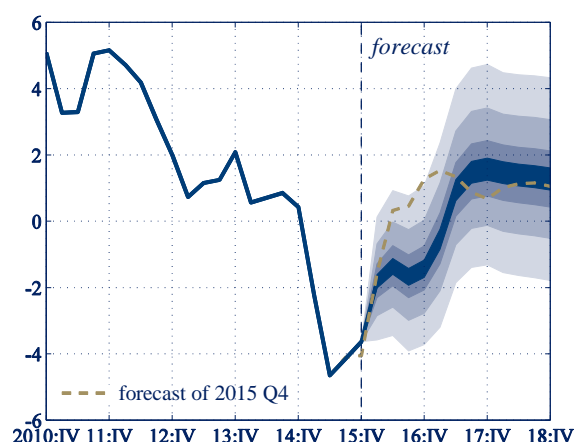
Lack of investor confidence due to sectoral sanctions, and low consumer and business activity are among other factors shaping the weak recovery of domestic demand. Moderate oil price growth over the forecast horizon and economy adaptation to the permanent nature of the terms-of-trade shock are expected to provide a basis for demand recovery for domestic goods in a range of manufacturing industries due to price competitiveness improvement. Exports are expected to remain a key driver of economic growth. GDP will continue to decline in 2016, but the magnitude will be lower—−1.6%.

Taking into account sectoral sanctions, difficulties of key industries with technology imports, along with unfavorable external

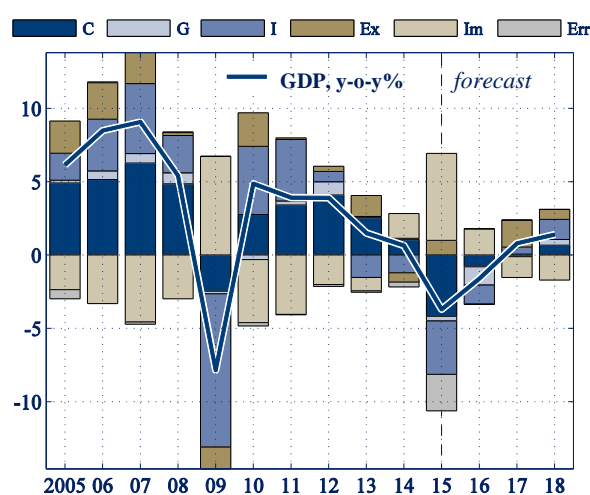
Economic Forecast for the Russian Federation

Year	Real GDP (annual percentage change)		CPI (annual percentage change)	
	Forecast (from 2016)	Difference, p.p.	Forecast (from 2016)	Difference, p.p.
2015	−3.7	0.0	15.6	0.2
2016	−1.6	−1.7	8.2	0.9
2017	0.8	−0.3	6.2	0.7
2018	1.4	0.3	4.5	−0.5

Real GDP growth, y-o-y%



Real GDP growth contributions, p.p.



C—private consumption, G—government consumption, I—gross capital formation, Ex—exports, Im—imports, Err—statistical discrepancy

conditions and low investment activity, economy recovery is expected to start only in 2017–2018 and with the growth at a much slower rate than in 2010–2011.

In March 2016 the government approved a package of countercyclical measures aimed to support living conditions and key industries to provide a basis for sustainable economic growth. Spending under the program is estimated to be around 1% of GDP and is financed from the budget. Against the background of deteriorating external environment, the government budget deficit in 2016 could exceed 3% of GDP. To contain deficit growth, implementation of fiscal consolidation measures is expected to start from 2017 onwards.

Gradual easing of credit conditions via liquidity channel due to the budget spending increase contributed to the attenuation of macroeconomic risks and moderate recovery of the banking sector credit activity. Inflation has been declining since the beginning of 2016, with the yearly figure expected to slide to 8.2% reflecting weak domestic demand. A slight uptick of consumer price growth is likely to occur in the second half of the year due to the scheduled utilities tariffs increase. In line with the forecast, Central Bank adherence to the current direction of monetary policy will contribute to inflation returning to a moderate single digit level: 6.2% in 2017 and 4.5% in 2018.

