

**NATIONAL BANK
OF THE KYRGYZ REPUBLIC**

**Monetary Policy Report
Quarter 2, 2021**

**Bishkek
September 2021**

Monetary Policy Report is released by the National Bank on a quarterly basis. The objective of this Report is to inform the public about the decisions made by the National Bank in the sphere of monetary policy, which are based on analysis and forecast of the main inflation factors and assessments of the economic situation development in the external environment and in the Kyrgyz Republic.

Monetary policy in the Kyrgyz Republic

The objective of the monetary policy is to achieve and maintain price stability through appropriate monetary policy.

The policy rate of the National Bank is the main instrument of the monetary policy. In 2014, the National Bank moved to a new monetary policy framework - when the National Bank policy rate serves as a target for the funds value in the money market - to improve and increase the effectiveness of the monetary policy. The short-term interest rates of the money market are the operational goal of the monetary policy. The purpose of the aforementioned movement is to strengthen the impact of the interest rate channel of the monetary policy, aimed at development of the inter-bank credit market and support for the real sector of economy.

Quantitative benchmark of the monetary policy is to keep inflation rate within 5-7 percent in the medium term. Development and implementation of the monetary policy is carried out within the framework of the Main Directions of the Monetary Policy for the medium term.

Monetary policy of the National Bank is focused on the future, as the decisions made in the field of the monetary policy affect the key macroeconomic indicators of the country with a certain lag. Development of the monetary policy is based on the inflation forecasts for the short and medium term, resulting from consistent and economically reasonable forecast of the economic situation development in the Kyrgyz Republic and in the external environment.

Communication policy is among the main instruments of the monetary policy conducted by the National Bank. The National Bank regularly issues press releases and holds press conferences on the monetary policy to inform the public and form adequate inflationary expectations among the population. Assessment of the current and expected macroeconomic situation in the country made by the National Bank is published in the Monetary Policy Report at the beginning of the third month of each quarter. The schedule of meetings held by the National Bank Board on the size of the policy rate is published on the bank's official website.

Monetary Policy Report for Q2 2021 was approved by the Resolution of the Board of the National Bank of the Kyrgyz Republic No. 2021-II-07/49-2-(ДКП) dated September 1, 2021.

Contents

Chapter 1. External Environment	5
1.1. Economic Development of the EAEU Countries and the Main Trading Partner Countries.....	5
1.2. World Commodity Markets	9
Chapter 2. Macroeconomic Development.....	13
2.1. Demand and Supply in the Commodities and Services Market	13
2.2. External Sector	16
Chapter 3. Monetary Policy	18
3.1. Monetary Policy Implementation	18
3.2. Financial Market Instruments	22
3.3. Dynamics of Monetary Indicators	26
Chapter 4. Inflation Dynamics.....	28
4.1. Consumer Price Index	28
4.2. Comparison of Forecast and Facts.....	29
4.3. Inflation Expectations.....	30
Chapter 5. Medium-Term Forecast.....	31
5.1. External Environment Proposals	31
5.2. Medium-Term Forecast	33
Annex 1. Key Macroeconomic Indicators	38
Annex 2. Glossary.....	39
Annex 3. Abbreviations	41

Summary

The restrictive measures taken due to the spread of the COVID-19 new strains and uncertainty about vaccination of the world's population still have a restraining effect on the global economic growth. At the same time, active revival of demand in the global financial markets has a significant impact on intensification of the inflationary processes in the trading partner countries of the Kyrgyz Republic and, as a result, acceleration of the domestic inflation.

There is a recovery in economic activity in the Kyrgyz Republic (in Q2 2021, the real GDP, excluding the enterprise of the Kumtor Mine, grew by 11.6 percent). At the same time, the reduction in production volumes at the enterprise of the Kumtor Mine restricts the full-scale economic recovery in the country. At the end of the first half of 2021, the economic decline was registered at the level of (-)1.7 percent compared to the same period in 2020, excluding the Kumtor Mine, GDP growth was 3.7 percent.

Domestic demand demonstrates positive dynamics due to a positive inflow of remittances (+31.1 percent in the first half of the year compared to the same period of 2020), however demand is still below the pre-pandemic level.

In Q2 2021, the trade balance was formed under the influence of an increase in import operations. Imports grew by two times due to an increase in the supplies of consumer and intermediate goods. Exports decreased by 8.3 percent. As a result, the trade balance deficit of the country amounted to USD 830.2 million. The volume of foreign trade turnover increased by 53.0 percent and amounted to USD 1.8 billion.

Amid growth in tax revenues, according to the preliminary results of the first half of 2021, there was a KGS 1.4 billion surplus of the state budget or 0.5 percent to GDP (in the same period in 2020, the budget deficit amounted to KGS 16.6 billion or 6.8 percent to GDP). The primary surplus¹ of the state budget amounted to KGS 6.3 billion, or 2.3 percent to GDP.

Rise in prices for consumer goods and services was mainly observed for food products (sunflower oil, meat and sugar) and petroleum, oil, lubricants. In Q2 2021 (quarter to the corresponding quarter of the previous year), the annual inflation rate was 11.3 percent. Due to the absence of seasonal deflation, at the end of the reporting period, there was a sharp rise in prices for vegetables, which made an additional contribution to the current inflation dynamics.

In the context of ongoing inflationary pressure, the National Bank maintained its course towards tightening monetary policy. The monetary sector was characterized by a reduction in excess liquidity in the banking system. Under such circumstances, there was an increase in the activity of money market participants, mainly in the short segment. Short-term money market rates fluctuated within the interest rate corridor set by the National Bank.

In general, the monetary indicators demonstrated positive dynamics, there was ongoing growth of lending to the economy and an increase in the depository base.

¹ Primary deficit/surplus is the excess of the state budget revenues over the state budget expenditures, excluding the amount of interest payments to service the state debt.

Chapter 1. External Environment

1.1. Economic Development of the EAEU Countries and the Main Trading Partner Countries

Recovery of economic activity was still observed in many main trading partner countries of the Kyrgyz Republic, meanwhile there was acceleration of the inflationary processes.

In Q2 2021, Russia demonstrated accelerated economic growth and achievement of pre-pandemic production volumes in many sectors.

The positive dynamics of economic growth was still observed in Kazakhstan. At the end of the first half of 2021, the GDP growth rate in Kazakhstan was 2.2 percent.

In Belarus, in the reporting period, there was a consistent decline in economic growth rates.

Economic recovery in Armenia was faster compared to earlier expectations. The inflation rate in Armenia still accelerated amid weakening Armenian dram and rising inflation risks in the economy.

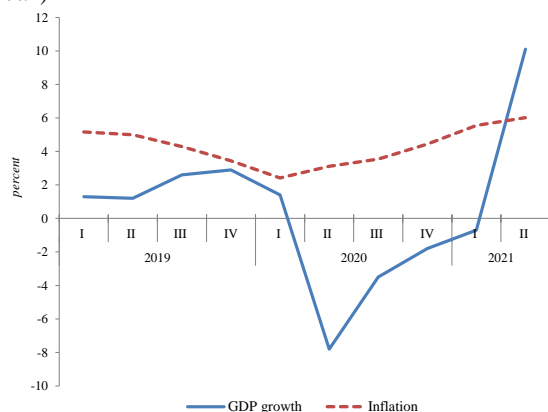
In Q2 2021, economic recovery in China slowed down gradually.

In the United States, there was ongoing economic recovery, while inflationary processes intensified amid rapid growth in external demand and limited supply for some commodity groups.

Russia

Chart 1.1.1. Growth of GDP and Inflation in Russia

(quarter to the corresponding quarter of the previous year)



Source: Ministry of Economic Development of the Russian Federation, IA Bloomberg, Russian Federal State Statistics Service

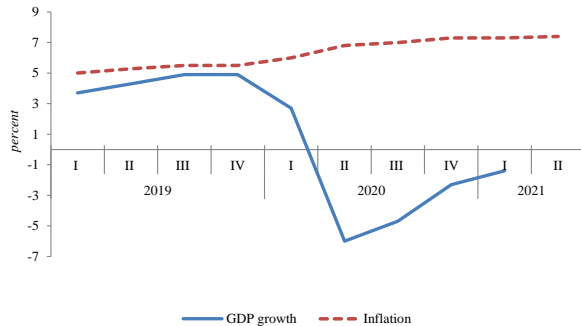
According to the Ministry of Economic Development of the Russian Federation, in June 2021, GDP reached pre-pandemic level (8.5 percent against June 2020). At the end of Q2 2021, GDP growth was 10.1 percent in annual terms. In Q2 of the current year, there was acceleration of economic growth in Russia. The production output of the key non-raw material sectors (processing industry, agriculture, construction) confidently exceeded the pre-crisis levels. According to the Bank of Russia estimates, there was steady growth in consumer and investment demand.. The consumer activity managed to exceed the pre-pandemic levels according to the Bank of Russia estimates. Active acceleration of the services sector was observed despite partial ongoing tightening of the restrictive measures. World economic recovery and rise in prices for raw materials contributed to export development in Russia. Moreover, external demand, which is still growing steadily, supported the economy of the country.

According to the Russian Federal State Statistics Service, in Q2 2021, the inflation rate in Russia was 6.0 percent to the corresponding quarter of the previous year, in June 2021, its annual value increased by 0.5 percentage points up to 6.5 percent. The annual rise in prices for services up to 3.9 percent was the most significant (by 0.7 percentage points compared to May). The annual rate of increase in prices for food products increased up to 7.9 percent (+0.5 percentage points), for non-food products – up to 7.0 percent (+0.4 percentage points). Accelerated rate of rise in prices is mainly due to active expansion of demand exceeding the possibilities to increase the production output.

Kazakhstan

Chart 1.1.2. Growth of GDP and Inflation in Kazakhstan

(quarter to the corresponding quarter of the previous year)



Source: RK Statistics Agency, NBKR calculations

In addition, in January-June, the construction sector (an increase by 11.9 percent) and agriculture (3.2 percent) were the main drivers of economic growth.

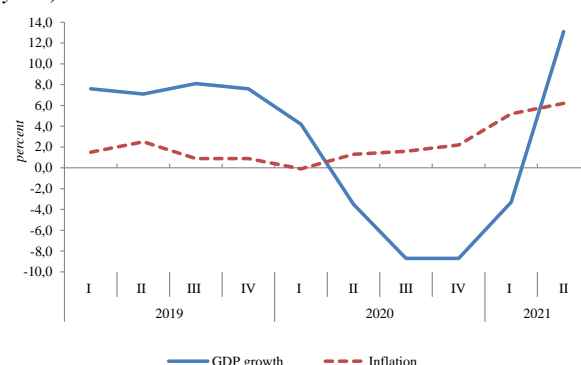
Moreover, in the first half of 2021, revival of the world economy, anti-crisis measures of the state with a decrease in quarantine restrictions, an increase of investments in non-extractive sectors of the economy, growth in wages of the population and positive indicators of the country's creditworthiness contributed to the recovery of business activity in the country.

According to the Bureau of National Statistics of the Agency for Strategic Planning and Reforms of the Republic of Kazakhstan, in January-June 2021, rise in prices constituted 7.3 percent due to an increase in prices for food products by 10.5 percent, for non-food products – by 6.0 percent, for the population's paid services – by 4.4 percent. Increased inflationary expectations, rise in prices in the world food markets, as well as internal and external inflationary risks may restrain the decline of the annual inflation rate in the future.

Armenia

Chart 1.1.3. Growth of GDP and Inflation in Armenia

(quarter to the corresponding quarter of the previous year)



Source: National Statistical Service of the Republic of Armenia, IA Bloomberg, CB RA

By the end of the first half of 2021, the economic growth rate of Kazakhstan reached the pre-pandemic level. The GDP growth rate in January-June of the current year was at the level of 2.2 percent against a decrease of 1.8 percent in the same period of 2020. In the reporting period, the largest contribution to the economic growth was due to an increase in production output in the real sector, in particular in the processing sectors of the economy. Thus, the share in the manufacturing industry (13.1 percent) in the structure of GDP for the first time since 2004 exceeded the share of the mining industry (12.5 percent).

In Q2 2021, Armenia demonstrated faster economic activity recovery compared to expectations. The positive effects of the campaign on the population vaccination against coronavirus and an increase in aggregate demand, as well as a faster resumption of economic activity in Armenia's partner countries contributed to such recovery. According to the preliminary data, in January-June 2021, the indicator of economic activity in Armenia increased by 5.0 percent. Growth was observed in all sectors. At the same time, the investment activity of the private sector still remained weak.

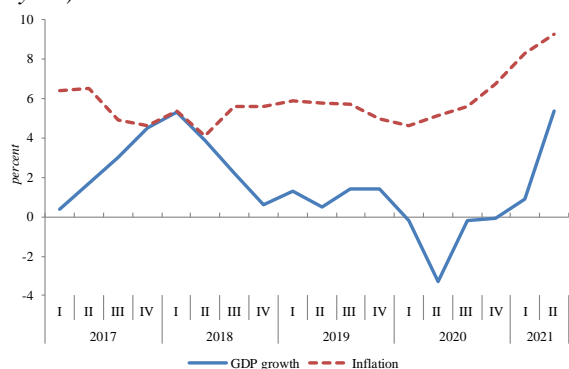
In June 2021, the inflation rate accelerated up to 6.5 percent in annual terms in the consumer market of Armenia, with a target of 4.0 percent. The prices for food products increased by 9.0 percent, for non-food products – by 9.5 percent, and for services – by 2.1 percent. In the context of a high inflationary environment, the Central Bank of Armenia increased the policy interest rate 4

times year-to-date: from 5.25 to 7.0 percent¹. The regulator is considering the need for a possible tightening of the monetary conditions in the future. In such conditions, the inflation rate is forecasted to remain at an increased level in the short term, then gradually decline and strengthen near the target of 4.0 percent.

Belarus

Chart 1.1.4. Growth of GDP and Inflation in Belarus

(quarter to the corresponding quarter of the previous year)



Source: National Statistical Committee of the Republic of Belarus

During Q2 2021, there was a consistent slowdown in economic growth in Belarus.

In general, in the first half of 2021, GDP of Belarus grew by 3.3 percent compared to the same period of 2020, however there was a slowdown in monthly dynamics in April-May: in April, GDP increased by 7.0 percent, in May – by 5.3 percent, in June – by 3.8 percent.

The EDB analysts believe that the GDP dynamics in Belarus and economic sentiment indicate the end of the economic recovery period in the country after recession observed in the last year. This, among other things, is reflected in weakened industrial

growth, which was the driver of economic growth at the beginning of the year due to the external demand strengthening. Exhaustion of the low base effect, most likely in the sectors of oil refining and production of potash fertilizers, affect the industrial production dynamics. At the same time, the information and communication sector provides significant support to GDP: in the first half of the year, its contribution to GDP growth reached 0.6 percentage points. In the second half of the year, the EDB forecasts slowdown in the economic growth in Belarus. The impulse for the exports will become weak amid stabilization of external demand and increased external economic pressure on the Belarusian economy due to the restrictions imposed by the Western countries. Domestic demand will continue to be affected by high uncertainty, a slowdown in the household income growth and an increase in the cost of lending.

In June, the annual inflation rate continued accelerating and amounted to 9.9 percent against 9.4 percent in May, 8.6 percent in April and 8.5 percent in March. In January-June, the prices for food products increased by 6.0 percent (as well as in June by 0.5 percent), for non-food products – by 6.3 percent (by 0.7 percent), the cost of paid services increased by 5,1 percent (in June, an increase by 0.9 percent). The annual inflation rate in Belarus accelerated due to the decisions taken in the field of constantly regulated prices (tariffs), the rise in prices in the market of non-food products, as well as ongoing pressure from the world food prices.

In the current environment, the analysts expect the annual inflation rate to be above 9.0 percent up to November inclusive and to slow down to 8.7 percent in December 2021. The risks of the inflation rate acceleration are assessed as significant, including due to the uncertainty of the consequences of restrictive measures taken in the USA, EU and UK for the exchange rate of the Belarusian ruble and established production chains. An increase in fuel prices in the domestic market in the context of the increased cost of oil is still a significant pro-inflationary factor. The high inflation rate in the Republic of Belarus is also supported by inflationary expectations: according to the calculations of the National Bank of Belarus, in

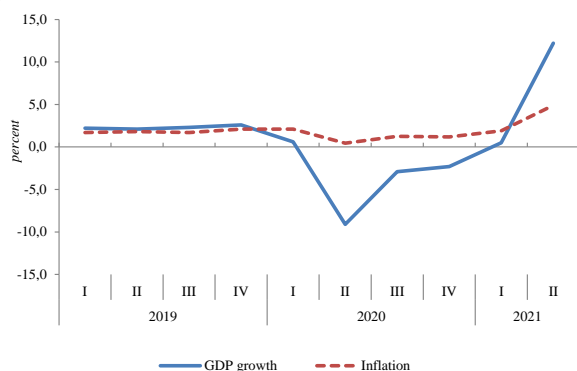
¹ August 3, 2021

June 2021, the inflation rate expected by the population for 12 months was 14.7 percent – the maximum value since the beginning of observations in November 2017.

USA

Chart 1.1.5. Growth of GDP and Inflation in the USA

(quarter to the corresponding quarter of the previous year)



Source: the U.S. Department of Commerce, the U.S. Department of Labor, IA Bloomberg

In the reporting period, the US economy still recovered from the pandemic consequences.

According to the Bureau of Economic Analysis of the U.S. Department of Commerce, in Q2 2021, real GDP in the USA increased by 12.2 percent¹ compared to the same period of 2020. Growth was observed in various sectors, including transport, tourism, manufacturing and non-financial services. The increase in US GDP conditioned reopening of businesses and ongoing government measures taken in response to the COVID-19 pandemic. During the reporting period, the government assistance payments in the form of loans to the enterprises and

grants to the state and local authorities increased, while there was a decrease in the social transfers to the households, such as direct economic impact payments.

The U.S. unemployment rate is declining (5.9 percent in June 2021), however the number of work places in the country decreased by 7.5 million compared to the pre-pandemic level, meanwhile the low-income workers and the representatives of ethnic and other minorities face the greatest difficulties.

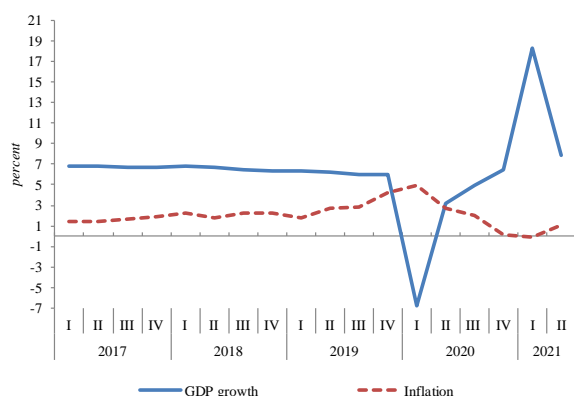
The difficulties due to the COVID-19 pandemic and limited supply of some products resulted in a rapid increase in prices for certain types of products and services in the USA. In addition, a high inflation rate was conditioned by the low base for comparison due to a decrease in prices in the previous year. Thus, the inflation rate in the USA accelerated up to 5.4 percent in June 2021 in annual terms (the highest indicator since August 2008) with a target approaching 2.0 percent. In June 2021, the prices, excluding food and energy prices, increased by 4.5 percent in annual terms, the highest value since November 1991.

¹ Preliminary estimate.

China

Chart 1.1.6. Growth of GDP and Inflation in China

(quarter to the corresponding quarter of the previous year)



Source: National Bureau of Statistics of the PRC, IA Bloomberg

softening to support the economy. The regulator reduced the requirements for the mandatory reserves¹ of the financial institutions. The resulting amount of about CNY one trillion (USD 154.0 billion) will be used to support the economy.

Experts forecast that the economic recovery rate in China may slow down further, however it is likely to exceed the official target of “more than 6 percent”² of GDP growth set for 2021.

In June, the annual inflation rate in China fell to 1.1 percent, which was slightly below the analysts’ expectations. The experts forecasted the value of the indicator at 1.2 percent, while in May the annual inflation rate in the PRC was 1.3 percent. In June, the prices for food products decreased by 1.7 percent in annual terms, the prices for non-food products increased by 1.7 percent, the prices for consumer goods increased by 1.1 percent, for services — by 1.0 percent. According to China’s Social and Economic Development Plan, China’s inflation target is 3.0 percent in 2021.

1.2. World Commodity Markets

The world upward trend in prices for food products and other raw materials made a significant input into inflation in the Kyrgyz Republic. However, the world prices for food products slightly decreased for the first time during the COVID-19 pandemic time. In the reporting period, there was an increased demand in the oil market amid the world economic recovery. The gold market demonstrated an increase in prices in the context of high inflationary risks in the world.

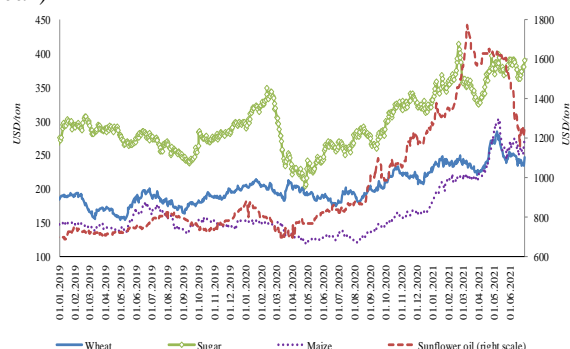
¹ The decision to reduce the standard value entered into force on July 15.

² According to the country’s economic development plan for 2021, approved by the National People’s Congress of China.

Food Market

Chart 1.2.1. Dynamics of Prices for Food Products

(month to the corresponding month of the previous year)



In the reporting period, volatile price dynamics was observed in the global food markets. World food prices still significantly exceed the prices of the same period in 2020. However, at the end of Q2 2021, there was a decrease in prices mainly due to crop harvesting in most of the exporting countries and an increase in supply in the markets, which is sure to result in a decline in prices or a slowdown in their growth rates.

Reduced import demand for vegetable oils, increased inventories and expectation of a good harvest in the large producing countries contributed to a decline in sunflower oil prices. According to the Ministry of Agriculture of the Russian Federation, about 15.9 million tons of sunflower will be harvested in Russia, an increase by 2.6 million tons compared to 2020 (13.3 million tons) due to an increase in acreage. Moreover, a good harvest of sunflower is expected in Ukraine to result in a decline in prices for sunflower oil both in the global market and within Russia.

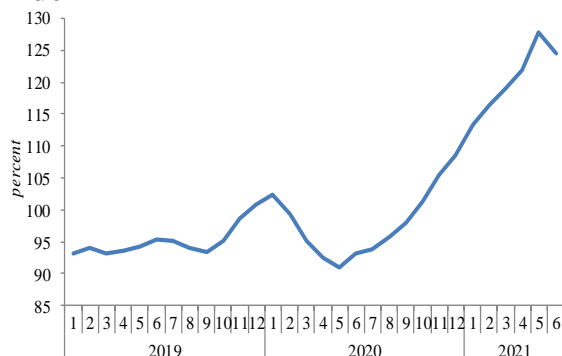
In the reporting period, prices for wheat and maize were growing, however, by the end of Q2 2021, they decreased amid good harvest in 2021-2022 and due to increased supply in Latin America.

World sugar prices demonstrated an upward trend in Q2 2021. This was due to uncertainty conditioned by the impact of bad weather on the harvest in Brazil¹. An increase in oil prices (sugar cane is processed into ethanol) and strengthening of the Brazilian real against the US dollar also contributed to rise in the world sugar prices.

According to the expectations of the financial institutions' analysts and experts, the forecasts for the future harvest, weather conditions, demand for specific types of food from the largest consumers and the oil price movement will influence the prices for food products in the long term. Movement of prices for substitute goods, dynamics of the national currencies exchange rates in the main exporting countries, as well as agriculture regulation in certain countries will be additional factors.

In addition, risks remain high for the importing countries, since from June 1 till June 28, 2021, the cost of transportation increased by almost 20.0 percent, 5.0 percent higher compared to their highest value in May 2021.

Chart 1.2.2. Dynamics of FAO Food Price Index



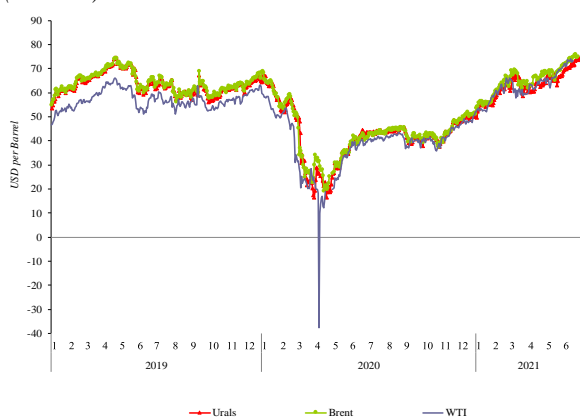
In Q2 2021, the average FAO food price index increased by 35.4 percent compared to the same quarter of 2020 and amounted to 124.8 points. However, by the end of the reporting period for the first time during the year, in June 2021, the FAO food price index decreased by 2.5 percent compared to May, departing from recently achieved ten-year highest values. This was due to a decrease in prices for vegetable oils and crops and, to a lesser extent, for dairy products, meanwhile prices for meat and

¹ Brazil is among the largest suppliers of cane sugar to the world market.

sugar demonstrated ongoing upward dynamics.

Energy Market

Chart 1.2.3. Dynamics of Oil Prices
(in USD)



In Q2 2021, the world oil prices increased amid optimism about world demand for fuel, despite an increase in the number of COVID-19 cases in many countries worldwide.

In Q2 2021, the average price of Brent oil increased by 12.7 percent compared to the previous quarter and amounted to USD 69.1 per barrel (the price increased by 106.9 percent compared to the same period of the previous year).

Fluctuations in the world oil prices increased sharply at the end of June 2021 as a result of conflicts within the OPEC + alliance,

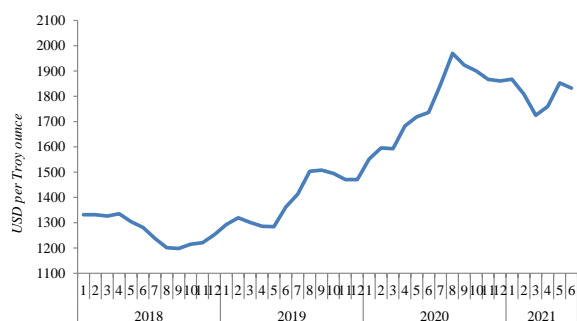
meanwhile expectations about increased demand for energy products and ongoing recovery of the global economy supported the rally in the oil market. At the end of the reporting period, quotes were at the level of USD 70.0-74.0 per barrel due to a decrease in oil reserves in the United States and an increase of selling prices in Saudi Arabia.

The International Energy Agency (hereinafter – IEA) retained its forecast for global oil demand for 2021 and still expects its growth by 5.4 million barrels per day – on average up to 96.4 million barrels per day. In 2022, global demand may increase by 3.0 million barrels per day. The IEA estimates that stable economic growth, increased vaccination coverage and relaxation of restrictive measures worldwide will support higher global demand for oil till the end of 2021. However, the IEA analysts may decrease the forecast, taking into account the situation with the coronavirus pandemic.

The Bank of America analysts raised their oil price forecast for 2021 from USD 60.0 up to USD 70.0 per barrel amid recovery in demand driven by the global coronavirus vaccination process. The oil price forecast for 2022 was increased by USD 15.0: from USD 60.0 up to USD 75.0 per barrel, and in 2023 the bank’s analysts expect the oil price to be at USD 65.0 per barrel.

Gold Market

Chart 1.2.4. Dynamics of Prices for Gold



Source: IA Bloomberg

In the reporting period, there was an increase in quotes in the gold market. Gold was used as an instrument to hedge inflation risks. Gold prices increased as the economic recovery was slightly difficult due to the spread of the coronavirus new strains and rising inflationary pressure.

Thus, in Q2 2021, the gold price increased by 3.7 percent and amounted to USD 1,770.1 per Troy ounce at the end of the period. The quotes were supported by the decline in the yield of the US state bonds and

USD weakening. A slight decrease in gold quotes was observed in June 2021 amid the US Federal Reserve System’s announcement of a more imminent increase in the policy rate compared to previous expectations. Rolling-up economic stimulus measures can result in USD strengthening, putting pressure on gold quotes.

According to the World Gold Council (WGC), in Q2 2021, the central banks of different countries were actively buying gold, replenishing their gold and foreign exchange reserves. The main motives of the regulators were the desire to hedge against growing inflation, as well as to diversify their own international reserves.

The WGC also noted that in Q2 2021, demand for gold, as well as supply thereof increased by 13.0 percent, up to 1,172 tons, mainly due to the growth in gold extraction.

The global regulators policy is still the main factor that affects the price for gold. If, in response to the growth of inflation, it starts tightening, the prices may decrease.

Clarification of the US Federal Reserve System's plans to reduce asset purchases and to raise interest rates will be the main factor determining the dynamics of gold quotes.

Chapter 2. Macroeconomic Development

2.1. Demand and Supply in the Commodities and Services Market

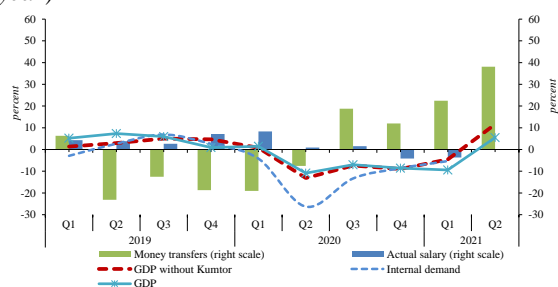
A gradual recovery of economic activity was observed in the Kyrgyz Republic with a slight slowdown in the first half of 2021. The dynamics of domestic demand demonstrates an upward trend, however, at the same time, it has not yet reached the pre-pandemic level. The inflow of remittances into the country demonstrate ongoing positive trend. A decrease in production output at the country's largest gold mining enterprise "Kumtor" conditioned a decrease in the gross domestic product in the Kyrgyz Republic in the first six months of 2021.

At the same time, uncertainty is still observed in the country's economy amid ongoing negative impact of the pandemic consequences and taking into account the risks of the COVID-19 new strains.

Demand

Chart 2.1.1. Dynamics of Internal Demand and Money Transfers

(quarter to the corresponding quarter of the previous year)



Source: NSC KR, calculations: NBKR

During January-June 2021, the economy of the Kyrgyz Republic demonstrated unstable recovery with its slowdown at the end of the reporting period. At the end of the first half of the year, the economic slowdown of the country was observed at the level of (-)1.7 percent compared to the same period of 2020, after (-)1.6 percent in January-May of the current year.

At the same time, in Q2 2021, GDP growth rate, without the enterprise of the Kumtor Mine, shifted into a positive area, having reached the level of 11.6 percent after (-)4.5 percent in Q1 of the current year, and constituted 3.7 percent by the end of the first six months.

At the same time, domestic demand demonstrates a slow recovery dynamics, however has not yet reached the pre-pandemic level. According to the preliminary results of Q1 2021, domestic demand¹ increased up to (-)5.3 percent from (-)8.6 percent in Q4 2020 (in Q1 2020, there was a decrease by 4.2 percent). The recovery in domestic demand was mainly due to an increase in remittances (+ 22.4 percent in Q1 2021). Since the beginning of 2021, net inflow of individuals' remittances via the money transfer systems in USD in the first half of the year increased by 31.1 percent compared to the same period of 2020.

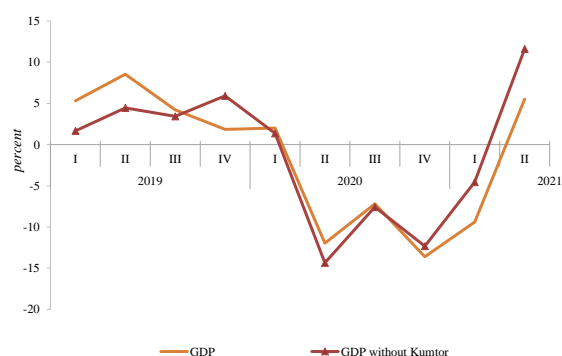
By the end of the first half of 2021, the average monthly nominal wage per one employee² amounted to KGS 19.4 thousand, having increased by 7.8 percent compared to the same period of 2020. A significant increase in the growth rate of average monthly wages was mainly observed in such sectors as transport and storage of goods (28.1 percent), information and communication (18.3 percent), as well as professional, scientific and technical activities (15.3 percent). At the same time, in January-June 2021, the real wages decreased by (-)2.6 percent compared to the same period of 2020.

¹ According to the NSC KR, reference to the data for the earlier period is given due to the lack of more up-to-date data.

² Generally in the republic, excluding small enterprises.

Chart 2.1.2. GDP Dynamics

(quarter to the corresponding quarter of the previous year)



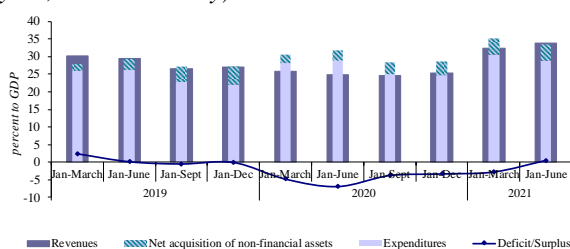
Source: NSC KR, calculations: NBKR

Public Finances Sector

According to the preliminary results for January-June 2021, the state budget surplus amounted to KGS 1.4 billion, or 0.5 percent to GDP (during the same period of 2020, the state budget deficit was KGS 16.6 billion or 6.8 percent to GDP). The primary state budget surplus¹ amounted to KGS 6.3 billion or 2.3 percent to GDP.

Chart 2.1.3. Execution of the State Budget

(period to the corresponding period of the previous year, accumulatively)



Source: CT MEFKR, NBKR

The economic slowdown is mainly conditioned by reduced production output in the sectors of industry and construction.

The negative dynamics in the industrial sector is conditioned by the production indicators at the enterprise of the Kumtor Mine amid events on the field investigation.

The volume of construction decreased by 14.2 percent due to a reduction in the level of capital investments exploitation in the reporting period.

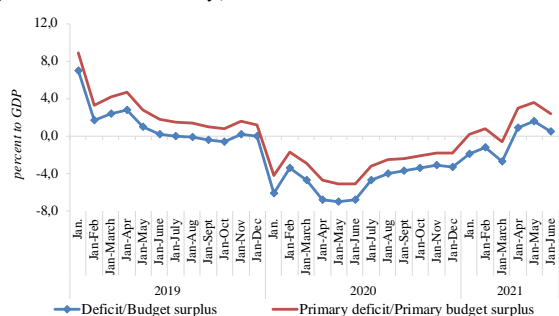
The state budget revenues from operating activities increased by 52.5 percent or KGS 31.7 billion compared to January-June 2020 and amounted to KGS 92.0 billion or 34.0 percent to GDP. Tax revenues occupy the largest share in the structure of current revenues (72.2 percent). Tax, non-tax revenues and official transfers made a positive contribution to an increase in budget revenues in the amount of 36.7 percentage points, 15.5 percentage points, and 0.3 percentage points, respectively.

The state budget expenditures for operating activities increased in annual terms by 11.7 percent or KGS 8.2 billion and amounted to KGS 78.0 billion or 28.8 percent to GDP. In the structure of expenditures by economic classification, there is an increase in expenditures on almost all items, excluding the item “other expenditures”. The structure of expenditures by economic classification changed due to an increase in wages, subsidies and social benefits, as well as due to the fact that since January 2021, the expenditures from the “special account”² are classified according to the corresponding expenditure items (wages, subsidies, social benefits, etc.). In the structure of expenditures by functional classification, the largest contribution to the increase in expenditures was made by expenditures for civil service, economic issues, education, and housing and utilities services.

¹ Primary deficit/surplus is the excess of the state budget revenues over the state budget expenditures, excluding the amount of interest payments to service the state debt.

² Special accounts are the accounts with the receipts recorded in the following forms: a) provision of paid state and municipal services; b) sponsor support and voluntary contributions; c) guardianship fees; d) charitable or grant aid; e) deductions from the international institutions for joint research work; f) funds from the sale of own-produced goods.

Chart 2.1.4. Budget Deficit
(period to the corresponding period of the previous year, accumulatively)



Source: CT MEFKR, NBKR

Table 2.1.1. Capital Investments by Sources of Financing
(millions of KGS, percent)

	January-June			
	2020	2021	2020	2021
	millions of KGS		share, percent	
Total	42 362.4	37 656.7	100.0	100.0
Internal investment	32 019.6	31 111.6	75.6	82.6
Republican budget	980.9	1 328.9	2.3	3.5
Local budget	213.3	345.5	0.5	0.9
Funds of enterprises and organizations	16 054.7	13 984.8	37.9	37.1
Banks' credits	311.2	483.6	0.8	1.3
Population funds including beneficent help of KR residents	14 459.5	14 968.8	34.1	39.8
External investment	10 342.8	6 545.1	24.4	17.4
Foreign credit	6 087.8	4 896.3	14.4	13.0
Direct foreign investments	2 610.3	620.8	6.1	1.7
Foreign grants and humanitarian aid	1 644.7	1 028.0	3.9	2.7

Source: NSC KR

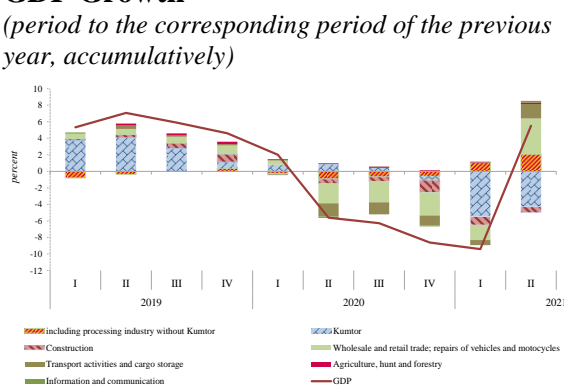
Source: NSC KR

At the end of the first half of 2021, there was a decrease in the volume of capital investments financed from the domestic (-3.6 percent) and foreign (1.6 times) sources. At the same time, the investments financed from the local budget increased by 1.6 times, from the republican budget – 1.3 times, from the bank loans – by 1.5 times.

Supply

According to the preliminary data of the National Statistical Committee of the Kyrgyz Republic, in January-June 2021, the nominal GDP decreased by 1.7 percent in real terms compared to the corresponding period of 2020 (according to updated data for January-June 2020 a decrease was 5.6 percent) and amounted to KGS 270.7 billion.

Chart 2.1.5. Input of Main Sectors in GDP Growth
(period to the corresponding period of the previous year, accumulatively)



Source: NSC KR, calculations: NBKR

11.7 percent compared to the corresponding period of 2020 due to a decrease in output of pharmaceutical products (by 36.5 percent), basic metals and finished metal products, as well as chemical products (by 31.2 percent).

Net outflow of budget funds for operations related to acquisition of non-financial assets (including operations in the following groups: fixed assets, reserves, land) increased by 1.8 times, or by KGS 5.6 billion compared to January-June 2020 and amounted to KGS 12.6 billion or 4.7 percent to GDP. The bulk of capital expenditures falls on acquisition of buildings and structures.

Investments

In January-June 2021, the level of capital investments exploitation decreased by 11.8 percent compared to the same period of 2020.

Decrease of capital investments was observed in the construction of many types of economic activity facilities, excluding agriculture, forestry and fishing, provision (supply) of electricity, gas, steam and conditioned air, information and communication, etc.

The sectors of industry (-2.9 percentage points), construction (-0.9 percentage points) and net taxes on products (-0.2 percentage points) made a negative input in economic decline. At the same time, the mining industry made insignificant positive input of 0.04 percentage points for the first time since January-July 2020. As in Q1 of the current year, agriculture demonstrated ongoing slight positive dynamics of its input to GDP growth (+0.1 percentage point).

In the first half of the current year, the industrial production output reduced by

At the same time, for the first time since January-July 2020, the mining sector demonstrated positive dynamics and amounted to 2.1 percent in the reporting period due an increase in the extraction of coal and brown coal (lignite) – by 41.9 percent, and other minerals – by 36.1 percent, as well as in the extraction of metal ores – by 0.9 percent.

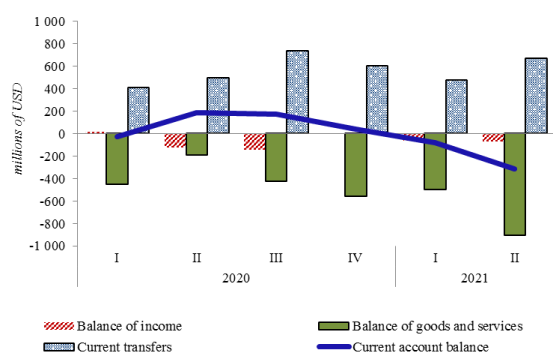
In January-June 2021, the gross agricultural output increased by 1.3 percent compared to the same period of 2020 due to growth in the production output of livestock products.

The GDP deflator was positive and amounted to 13.9 percent, having increased by 9.6 percentage points compared to January-June 2020 (in January-March 2020, the deflator was also positive at 4.3 percent).

2.2. External Sector¹

In Q2 2021, the current account was formed under the influence of an increase in the negative balance of goods trade amid growth in the net inflow of current transfers.

Chart 2.2.1. Current Account



Note: According to the preliminary and forecasted data.

According to the forecasted and preliminary data, in Q2 2021, the current account deficit constituted USD 312.3 million or 2.4 percent of GDP².

In the reporting period, the trade balance of the Kyrgyz Republic was formed with a negative balance and increased by 6.7 times compared to the same period in the previous year, to make USD 830.2 million. This trend is conditioned by an increase in imports, as well as a decrease in exports in the reporting period.

Table 2.2.1. Trade balance of the Kyrgyz Republic³

(millions of USD)

	2018	2019	2020	2020 Q2	2021 [*] Q2	Change in %	Change in millions
Trade balance	-3 033,8	-2 626,0	-1 439,7	-124,0	-830,2	569,5	-706,2
Export (FOB)	1 916,0	2 042,9	2 015,8	522,4	479,2	-8,3	-43,1
Gold	664,2	832,9	987,0	325,2	94,6	-70,9	-230,5
Import (FOB)	4 949,9	4 669,0	3 455,6	646,4	1 309,4	102,6	663,1
Energy products	809,6	627,2	476,6	98,7	174,0	76,4	75,3

*Preliminary data.

In Q2 2021, the import of goods (in FOB prices) increased by 2.0 times, to make USD 1,309.4 million. Growth in the value of import was largely due to price increase. There was an increase in import of goods such as clothes, cast iron and steel, woven fabrics of man-made textile materials, cars and vehicles principally designed for the transport of persons, footwear. Import, excluding energy products, increased by 2.1 times compared to Q2 2020, to make USD 1,135.5 million.

In the reporting period, export of goods (in FOB prices) decreased by 8.3 percent, to make USD 479.2 million. There was a decrease in the supplies of precious metal ores and concentrates, butter and other fats derived from milk, and other goods. At the same time, there

¹ According to the preliminary and forecasted data, including additional estimates of the National Bank of the Kyrgyz Republic. Period of comparison is the quarter to the corresponding quarter of the previous year.

² Ratios to GDP are calculated based on sliding annual data, including the last four quarters.

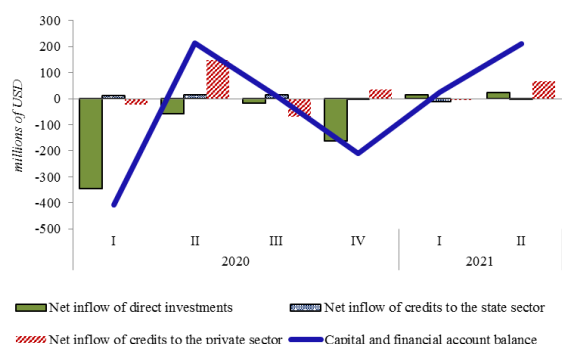
³ The data on the foreign trade are given taking into account the NSC KR additional estimates for sampling survey of mutual trade with the EAEU member states and the NBKR additional estimates on exports.

was an increase in the volume of export of float glass and surface ground glass, clothes, non-ferrous base metal waste and scrap.

In the reporting period, the net inflow of current transfers increased compared to the same period of 2020 mainly due to received private transfers. The net inflow of private transfers increased by 39.5 percent and amounted to USD 659.4 million. In the reporting quarter, the balance of services deficit is estimated at USD 76.6 million, meanwhile the negative balance on the item “income” is expected at USD 72.8 million.

According to preliminary forecast estimates of the National Bank, in Q2 2021, the current account deficit will be accompanied by a net capital inflow on the capital and financial account in the amount of USD 212.5 million. The capital account surplus will make USD 55.6 million, meanwhile the positive balance on the financial account is expected at USD 156.8 million.

Chart 2.2.2. Capital and Financial Account



at the end of Q2 2021.

Net inflow of direct investments is forecasted at USD 24.4 million, meanwhile a net outflow was observed in the same period of the last year. In the reporting quarter, the balance of the item “other investments” will develop positive in the amount of USD 132.5 million, having significantly decreased compared to the corresponding indicator of the previous year.

Thus, the balance of payments of the Kyrgyz Republic will be formed with a positive balance to make USD 112.2 million

Indexes of Real and Nominal Effective Exchange Rate of KGS

Table 2.2.2. Key Values for Exchange Rate

	year (average)			month to the beginning of the year			
	2019 (aver.) (January- December)	2020 (aver.)* (January- December)	%	December 2020	June 2021	* %	
REER	115,7	115,7	0,0	112,8	117,4	4,1	↑
NEER	122,5	122,7	0,1	116,8	119,2	2,1	↑
RBER to CNY	84,5	79,2	-6,3	73,0	75,4	3,2	↑
NBER to CNY	67,1	60,8	-9,3	53,3	51,5	-3,3	↓
RBER to EUR	108,2	101,7	-6,0	93,5	96,5	3,2	↑
NBER to EUR	78,0	69,5	-10,9	60,2	59,8	-0,6	↓
RBER to KZT	141,7	137,4	-3,0	132,7	136,7	3,0	↑
NBER to KZT	171,0	166,7	-2,5	157,3	157,9	0,4	↑
RBER to RUB	122,0	125,8	3,1	123,8	123,5	-0,3	↓
NBER to RUB	140,4	141,0	0,4	134,4	130,1	-3,2	↓
RBER to TRY	165,8	174,3	5,1	176,8	191,1	8,1	↑
NBER to TRY	247,6	275,3	11,2	284,0	310,0	9,1	↑
RBER to USD	87,6	83,1	-5,2	80,7	82,1	1,7	↑
NBER to USD	65,8	59,6	-9,5	55,1	54,4	-1,2	↓

* Preliminary data
 ↓ – Som devaluation, competitiveness improvement
 ↑ – Som strengthening, competitiveness deterioration

by 3.3 percent.

The strengthening of the NEER index and a higher inflation rate in Kyrgyzstan² conditioned an increase in the real effective exchange rate (REER) index, which increased by 4.1 percent since December 2020 and constituted 117.4 at the end of June 2021.

By the end of Q2 2021, the nominal and real effective exchange rates increased compared to December 2020. According to the preliminary data, the index of the nominal effective exchange rate (NEER) of KGS increased by 2.1 percent year-to-date and constituted 119.2 at the end of June 2021. The increase in the index was due to the strengthening¹ of KGS in June 2021 compared to the exchange rate in December 2020 against the Turkish lira by 9.1 percent and the Kazakh tenge by 0.4 percent amid depreciation against the Russian ruble by 3.2 percent, the US dollar – by 1.2 percent, the euro – by 0.6 percent, the Chinese yuan -

¹ The data are given for the nominal bilateral exchange rate of KGS; the year of 2010 is used as the base period for the calculation of the index.

² In Q2 2021, the inflation rate in the Kyrgyz Republic was formed at 7.4 percent, meanwhile, the average inflation rate in the main trading partner countries according to the preliminary calculations was 5.3 percent.

Chapter 3. Monetary Policy

3.1. Monetary Policy Implementation

A faster recovery in demand in the global financial markets and ongoing rise in prices for food products in the world markets and in the EAEU countries are the main reasons for the current inflation risks in the Kyrgyz Republic.

Under these conditions, in Q2 2021, the National Bank continued to adhere to the previous direction of the monetary policy aimed at limiting the influence of the monetary inflation factor. The tightening of the National Bank's interest rate policy in the reporting quarter conditioned an increase in the key rate up to 6.50 percent.

Tactical monetary policy measures were refocused with regard to the behavior of the money market participants operating in the context of a decrease in excess liquidity in the banking system compared to Q1 2021.

The domestic foreign exchange market was less active compared to the previous quarter amid relative balance of supply and demand for foreign currency among the market participants. The National Bank conducted foreign exchange interventions in April to smooth sharp fluctuations of the exchange rate, meanwhile the National Bank did not participate in the foreign exchange market for most of Q2 2021.

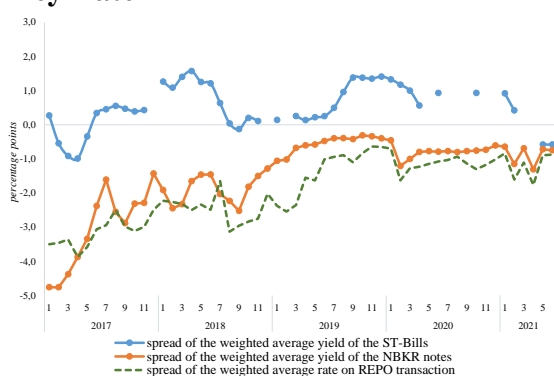
In the context of a reduction in excess liquidity in the banking system, there was a significant rise in demand for short-term liquidity in the national currency to result in a significant increase in the volume of transactions in the short segment of the interbank credit and foreign exchange markets. In general, the short-term money market rates still demonstrated their upward trend and stood mainly near the key rate within the interest rate corridor set by the National Bank.

Interest Rate Policy of the National Bank

At the end of April 2021, for the second time this year, the National Bank's main rates were twice revised in the current year amid the strengthening of inflationary processes in the country and inflation estimates for the medium term. In particular, the size of the policy rate was increased by 100 basis points, up to 6.50 percent, by the decision of the National Bank Board of the in order to limit inflationary pressure, as well as the spillover effects from price increase in the world food markets.

The rates of the interest rate corridor were adjusted upon change of the key rate: the rate on "overnight" deposits was increased from 3.25 to 4.25 percent, the rate on "overnight" credits – from 6.00 to 7.00 percent.

Chart 3.1.1. Spread between the Short-Term Rates of the Money Market and the Key Rate

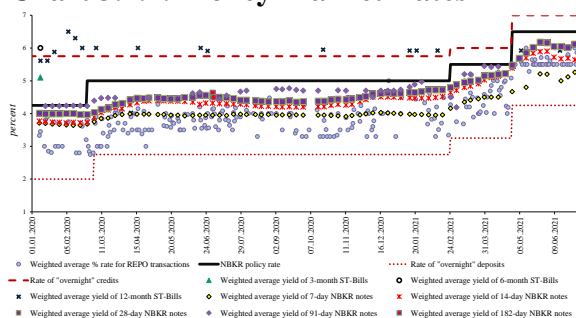


In the context of the ongoing general upward trend in the short-term money market rates amid the interest rate policy conducted by the National Bank in the current year, the gap between the short-term rates and the key rate of the National Bank generally remained at the level of the previous quarter, excluding a temporary increase in the spread at the end of April due to the effect from an increase in the key rate by 100 basis points up to 6.5 percent.

During three consecutive quarters, the average spread of the rate on REPO transactions in the interbank credit market to the policy rate of the National Bank remained practically unchanged and stood at (-)1.18 percentage points. At the same time, the average yield spread of the National Bank's notes to

the policy rate increased slightly (+0.1 percentage points) and amounted to (-)0.9 percentage points.

Chart 3.1.2. Money Market Rates



In Q2 2021, the short-term money market rates continued to respond to the ongoing tightening of the monetary conditions through an increase in the National Bank’s key rates, in particular, there was an increase in the rates of the interbank credit market and the National Bank’s note market.

Under these conditions, the short-term money market rates were still close to the key rate, meanwhile the range of their spread

narrowed. Meanwhile, the rates continued fluctuating within the interest rate corridor set by the National Bank.

In the reporting period, the market of the National Bank’s notes demonstrated decreased activity of the participants. The decrease in activity was characterized by reduction in the number of participants (approximately from 6 to 4 per auction) and a decline in the volumes of supply and demand at the auctions of the National Bank’s notes (in Q2, demand constituted 98.6 percent of the supply volume¹, meanwhile in Q1, demand constituted 102.3 percent with higher supply). However, the yield of the National Bank’s notes of all maturities demonstrated an upward trend due to tightening of the interest rate policy. The total weighted average yield of notes increased from 4.49 percent in Q1 2021 up to 5.58 percent in Q2 2021 (in the reporting period, the total yield varied within the range of 4.5-6.18 percent). At the same time, in terms of maturities, the most significant growth was observed on the rates of the National Bank’s notes with a maturity of up to 28 days inclusive and, to a lesser extent, on 91-day notes.

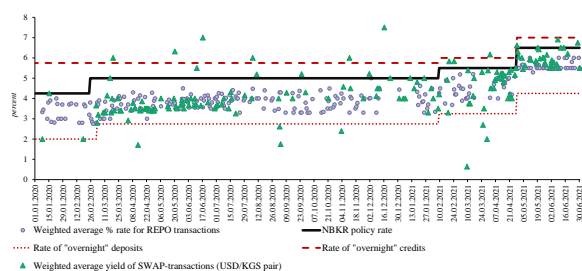
In Q2 2021, the market participants’ preferences at the auctions of the National Bank’s notes (average auction volumes of demand exceeded the volumes of supply) shifted towards 14-day notes, meanwhile in Q1, 7- and 28-day notes were in great demand.

In Q2 2021, as before, the short-term segment of government securities was represented only by the ST-Bills with a maturity of 12 months. In the reporting period, only two auctions were held (the last one was held on June 10, 2021) for sale of 12-month ST-Bills out of 13 auctions of the Ministry of Economy and Finance of the Kyrgyz Republic due to low demand from the financial market participants. The weighted average yield constituted 5.92 percent at these auctions and was within the interest rate corridor set by the National Bank.

During Q2 2021, in the context of a slight decrease in the overall level of excess liquidity in the banking sector, the participants in the interbank credit market actively increased the volume of transactions, the peak of concluded transactions was recorded in April 2021. REPO transactions mainly concluded for 1-3 days prevailed (the share of transactions with this maturity constituted 78 percent of the total number of transactions) due to increased demand of the commercial banks for short-term liquidity in the national currency. The upward factor in demand for borrowed short-term funds, as well as the interest rate policy of the National Bank, conditioned an increase in the drawing price from 4.2 percent (an average value for Q2 2021) up to 5.2 percent (an average value for the reporting period).

¹ Taking into account the failed auctions, where there was no demand or demand was observed from the single participant.

Chart 3.1.3. Rates of the Interest Rate Corridor, REPO and SWAP transactions

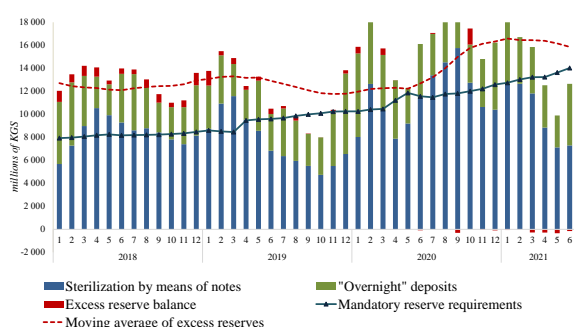


In the reporting period, foreign exchange transactions on a swap basis (USD/KGS pair), along with REPO transactions, were among the main sources of attracting liquidity in the national currency for the commercial banks. The total volume of SWAP transactions conducted by the commercial banks in the domestic market amounted to KGS 11.3 billion (in Q1 2021 – KGS 3.6 billion).

In Q2 2021, the weighted average rate on SWAP transactions (USD/KGS pair) constituted 5.72 percent (in Q1 2021 – 4.76 percent) with the transactions’ weighted average maturity of 6 days (in Q1 – 20 days). In general, in the reporting period, rates on SWAP transactions varied from 4.0 to 8.5 percent, depending on the term of transactions. At the same time, the average spread between rates on these transactions and the key rate constituted (-) 0.78 percent.

Liquidity Regulation in the Banking Sector

Chart 3.1.4. Excess Reserves of the Commercial Banks



In Q2 2021, the average level of excess liquidity decreased compared to the previous quarter (KGS 11.4 billion against KGS 17.1 billion in Q1 of the current year). It should be noted that in June 2021, the previous decrease in excess liquidity of the banking system demonstrated an upward trend.

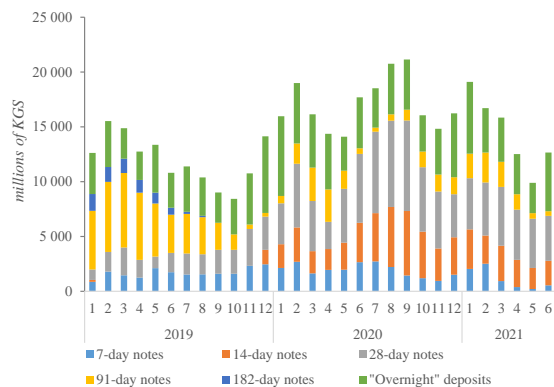
In Q2 2021, the volume of liquidity in the national currency withdrawn due to the National Bank’s operations for sale of foreign currency in the interbank foreign exchange market decreased by KGS 3.9 billion compared to the previous quarter (from KGS 13.4 billion to KGS 9.5 billion).

The operations of the commercial banks to repay credits in the amount of KGS 1.1 billion previously extended by the National Bank and the growth of money outside banks by KGS 7.6 billion were an additional restraining factor to increase excess liquidity in the banking system. In turn, fiscal operations slightly increased liquidity in the banking system by KGS 0.8 billion.

In general, in the reporting period, the banking system continued to function in the conditions of excess liquidity. The average daily volume of this indicator, prior to the sterilization operations conducted by the National Bank, decreased by KGS 5.7 billion compared to the indicator for the previous quarter and stood at KGS 11.4 billion.

In order to limit inflationary pressure, the National Bank continued to conduct the operations to absorb excess liquidity. In Q2 2021, the average daily volume of sterilization operations conducted by the National Bank amounted to KGS 11.7 billion (in Q1 – KGS 17.2 billion).

Chart 3.1.5. Structure of Sterilization



The National Bank’s notes of were the main instrument to withdraw excess liquidity. In the reporting quarter, the average daily volume of notes in circulation amounted to KGS 7.8 billion (in Q1 2021 – KGS 12.3 billion). At the same time, in Q2 2021, the share of the National Bank’s notes in the structure of sterilization operations slightly decreased from 71.5 to 66.4 percent.

The National Bank’s notes with the maturities of 14 and 28 days were the most investment-attractive due to the short maturity of the commercial banks’ available surplus

funds (the total share in the sterilization structure increased by 19.3 percentage points compared to the previous quarter and constituted approximately 85.1 percent due to notes of this maturity).

The volumes of placement of the commercial banks’ available funds on “overnight” deposits also decreased amid general reduction in the volume of excess liquidity. At the same time, the share of “overnight” deposits in the total structure of sterilization increased from 28.5 to 33.6 percent compared to notes due to a less significant decrease in the volume of placements.

Credit Policy of the National Bank

As part of tightening monetary conditions, in the reporting period, the National Bank limited operations to provide long-term liquidity in the national currency through refinancing instruments. This measure is conditioned by the current high level of excess liquidity in the banking system, which is among the factors of inflationary pressure.

At the same time, in Q2 of the current year, there was a need for short-term liquidity in the banking system. Within the framework of the current window of permanent access, “overnight” loans were issued to the banks, the gross volume thereof amounted to KGS 14.2 billion, to cover short-term liquidity gaps.

Foreign Exchange Policy of the National Bank

In Q2, as well as at the beginning of the current year, the KGS exchange rate against the USD demonstrated a relatively stable dynamics. Only at the beginning of the reporting period, the demand for foreign currency exceeded its supply in the domestic foreign exchange market amid influence of external economic conditions.

Within the framework of the adopted floating exchange rate regime, the National Bank, if necessary, participated in the foreign exchange auctions to smooth sharp fluctuations in the exchange rate. In the reporting quarter, the total volume of the National Bank’s interventions on sale of foreign currency in the domestic foreign exchange market amounted to USD 112.5 million (in Q1 2021 – USD 158.0 million). In the reporting period, the National Bank did not conduct transactions on purchase of foreign currency, as in the previous quarter.

In Q2 2021, the USD/KGS exchange rate was fluctuating within the range KGS 83.0132-84.8000 per USD to decrease by 0.14 percent at the end of the reporting quarter. In the reporting quarter, the average exchange rate amounted to 84.5404 KGS per USD and practically did not change compared to the previous quarter (84.4960 KGS/USD).

Monetary Policy Measures in Q2 2021

The decisions were made on the size of the National Bank policy	The Board of the National Bank twice considered the issue of the size of the policy rate – on
---	---

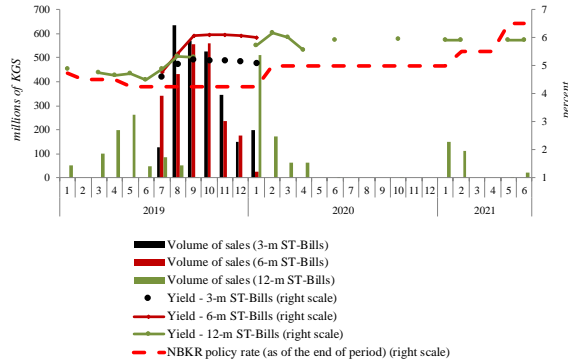
rate and the rates of the interest rate corridor

April 26 and May 31, 2021. Based on the results of the meeting held in April, the decision was made to increase the policy rate by 100 basis points, up to 6.50 percent. Based on the results of the meeting held in May, the decision was made to keep the policy rate unchanged at 6.50 percent.

The rates of the interest rate corridor were adjusted to strengthen the work of the interest rate channel of the monetary policy transmission mechanism: the rate on “overnight” deposits, being the lower rate, was increased up to 4.25 percent, the rate on “overnight” credits, determining the upper rate, was increased up to 7.00 percent.

3.2. Financial Market Instruments Government Securities Market

Chart 3.2.1. Dynamics of ST-Bills Sales Volumes and Yield



ST-Bills

In Q2 2021, there was a decrease in activity in the ST-Bills market. The weighted average yield remained at the level of the previous quarter.

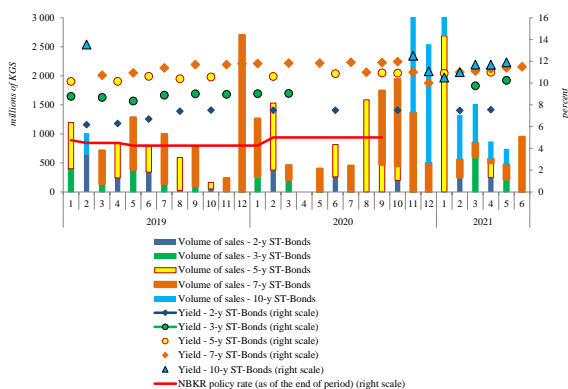
The Ministry of Finance of the Kyrgyz Republic offered only 12-month ST-Bills since February 2020. In Q2 of the current year, the average monthly supply of ST-Bills increased by 32.0 percent compared to the same period in 2020. Demand and sales indicators were weak. In general, in the

reporting period, the volume of supply amounted to KGS 660.0 million, the volume of demand – KGS 56.5 million, and the volume of sales, taking into account additional placements, amounted to KGS 23.1 million.

In the reporting period, the total weighted average yield was 5.92 percent, having not changed compared to Q1 2021.

Due to the lower volumes of ST-Bills sales compared to Q2 2020, their volume in circulation at the end of Q2 2021 decreased by 64.9 percent year-to-date, down to KGS 285.9 million.

Chart 3.2.2. Dynamics of ST-Bonds Sales Volumes and Yield



ST-Bonds

In Q2 2021, the volume of borrowings through the ST-Bonds was reduced compared to the previous quarter, but it increased compared to Q2 2020. The highest demand was observed for 7- and 10-year securities.

In Q2 2021, the total volume of ST-Bonds supply at the auctions increased by 21.9 percent compared to the same period of 2020 and amounted to KGS 3.9 billion. The demand was lower than the proposed volume of ST-Bonds placement and amounted to

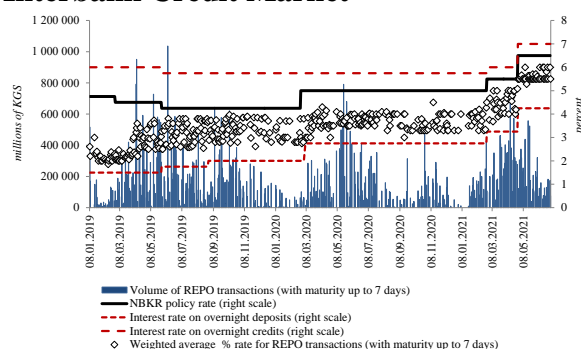
KGS 2.8 billion (-29.3 percent). The demand for 7-year securities constituted 47.0 percent of the total demand for ST-Bonds, the demand for 10-year securities constituted 19.8 percent, for 2-year securities – 16.3 percent. Taking into account the additional placements, the total sales of ST-Bonds decreased by 34.4 percent compared to the volume of supply and amounted to KGS 2.6 billion.

The overall weighted average yield increased by 1.24 percentage points compared to the corresponding period of 2020 and amounted to 10.94 percent.

At the end of the reporting period, the volume of ST-Bonds¹ in circulation increased by 12.0 percent year-to-date, up to KGS 59.2 billion, due to an increase in the portfolio of the institutional investors and resident legal entities.

Interbank Credit Market

Chart 3.2.3. Dynamics of Rates and Volume of Repo Transactions in the Interbank Credit Market



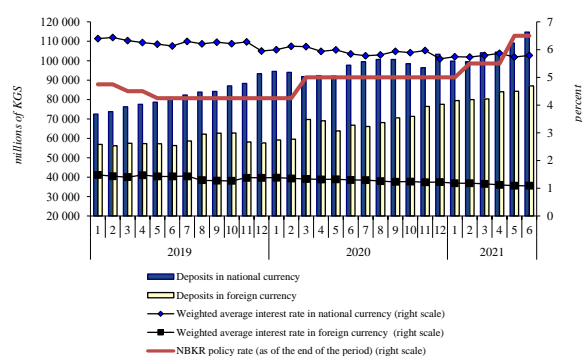
In Q2 2021, the participants' activity in the interbank credit market was at a relatively high level.

In the reporting period, the volume of transactions conducted in the interbank market increased by 75.2 percent compared to Q1 2021 and amounted to KGS 13,335.9 million. All transactions (217) were REPO transactions. The standard transactions in the national currency were not conducted since April 2019. The standard transactions in foreign currency were conducted for the last time in October 2020.

In Q2 2021, the weighted average interest rate in the interbank market increased by 0.17 percentage points compared to the previous quarter and stood at 5.32 percent. The weighted average maturity of the interbank credits decreased down to 3 days (in Q1 2021 – 6 days).

Deposit Market

Chart 3.2.4. Dynamics of Commercial Banks' Deposits



In Q2 2021, the depository base continued to grow, with an increase in deposits in both national and foreign currencies.

As of the end of June 2021, the commercial banks' depository base increased 11.5 percent higher compared to December 2020 and amounted to KGS 201.8 billion. Deposits in the national currency increased by 11.0 percent year-to-date, up to KGS 114.8 billion. Deposits in foreign currency increased by 12.2 percent, up to KGS

87.1 billion. At the same time, deposits in US dollars increased by 11.6 percent in nominal terms year-to-date.

Dollarization of deposits increased by 0.3 percentage points compared to the end of the previous year and amounted to 43.1 percent, meanwhile dollarization adjusted for the exchange rate at the beginning of the year decreased by 0.3 percentage points.

At the end of Q2 2021, the share of time deposits in the structure of the depository base in the national currency decreased by 0.2 percentage points compared to the end of 2020

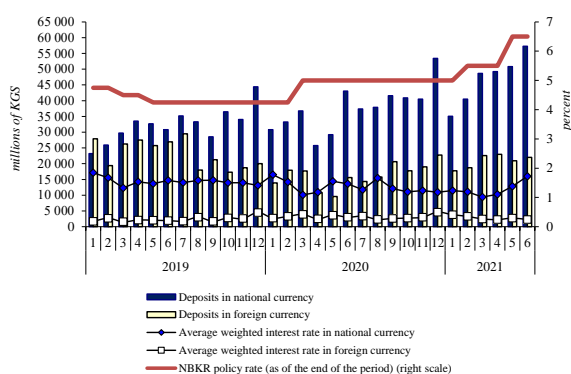
¹Excluding ST-Bonds nominated in foreign currency

and stood at the level of 46.4 percent. The share of deposits with a maturity of more than one year decreased by 0.5 percentage points year-to-date in the structure of time deposits in the national currency. The share of time deposits in foreign currency decreased by 2.1 percentage points, down to 24.6 percent. In the structure of time deposits in foreign currency, the share of deposits with a maturity of more than one year increased by 6.7 percentage points, up to 35.1 percent.

In the reporting quarter, there was a noticeable increase in the volume of new deposits by 66.6 percent compared to the corresponding quarter of the previous year, up to KGS 223.2 billion. The volume of new deposits in the national currency increased by 60.5 percent, up to KGS 157.3 billion, new deposits in foreign currency increased by 83.2 percent, up to KGS 65.9 billion.

The total duration of the depository base was 5.0 months at the end of March 2021 (-0.2 months year-to-date), the duration of time deposits decreased down to 13.4 months (-0.1 month).

Chart 3.2.5. Dynamics of Commercial Banks' Deposits Flows



In January-June 2021, the weighted average rates on new deposits decreased by 0.13 percentage points compared to the corresponding period of 2020, down to 0.98 percent. The interest rates on new deposits in the national currency decreased by 0.16 percentage points compared to January-June 2020 and constituted 1.27 percent, the interest rates on the deposits in foreign currency decreased by 0.04 percentage points and constituted 0.30 percent. The weighted average rate on new time deposits in the national currency increased by

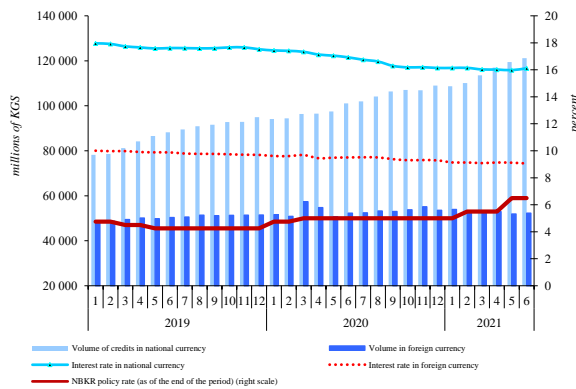
0.75 percentage points, up to 9.93 percent, those in foreign currency decreased by 0.11 percentage points, down to 2.81 percent. The weighted average interest rates in the national currency increased for all maturities, excluding the deposits with a maturity up to 3 months, while those in foreign currency decreased for all maturities, excluding the deposits with the maturities of 1-3 months.

The concentration index¹ in the deposit market increased by 0.01 percentage point year-to-date, up to 0.10, as of the end of the reporting period, which corresponds to the average level of concentration with ten participants with equal shares in the market.

¹ This index shows the degree of concentration in the portfolio of the banks. The concentration index is calculated by the method of calculating the Herfindahl-Hirschman index and is the sum of the squares of specific weights of the indicator in the total volume. The index takes values from 0 to 1. Index value less than 0.10 corresponds to a low level of concentration; from 0.10 to 0.18 - the average level of concentration; over 0.18 - high level of concentration. For example, a concentration index of 0.50 is equivalent to the presence of 2 participants with the same shares in the market, and 0.3 - 3 participants, etc.

Credit Market

Chart 3.2.6. Dynamics of Commercial Banks Credit Debt as of the End of the Period



dynamics since March 2020, when depreciation of the national currency was observed.

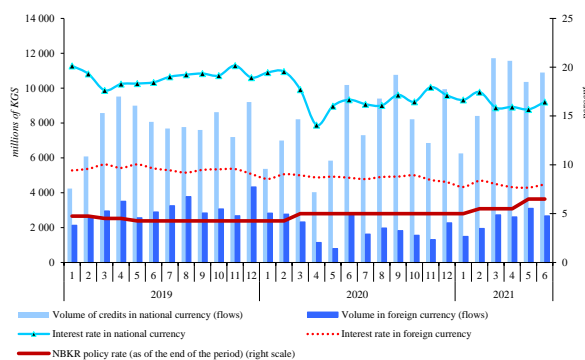
Dollarization of the credit portfolio decreased by 2.8 percentage points year-to-date (as of the end of June), down to 30.1 percent, updating its historically low value. At the same time, dollarization adjusted for changes in the US dollar exchange rate increased by 0.4 percentage points, up to 29.6 percent.

In Q2 2021, the volume of new credits significantly increased compared to the corresponding quarter of 2020, having increased by 66.2 percent and amounted to KGS 41.2 billion. At the same time, there is a significant increase in the volume of new credits in the national currency by 63.6 percent compared to the corresponding quarter of 2020, up to KGS 32.8 billion, an increase was observed for all maturities. Credits in foreign currency increased by 77.4 percent, up to KGS 8.4 billion. This increase was also observed for all maturities.

In Q2 2021, new credits in the national currency increased in all sectors, except for communication, compared to the corresponding period of 2020. A significant growth was observed in the sectors of transport (+254.5 percent), consumer credits (+133.3 percent) and social services (119.8 percent). In the structure of new credits in foreign currency, the volume of credits to agriculture increased by more than 17.0 times amid low base of the previous year due to restrictions conditioned by the spread of COVID-19.

In Q2 2021, duration for new credits in the national currency decreased by 1 month compared to the corresponding quarter of 2020 and amounted to 24 months, in foreign currency it decreased by 3 months and was at the level of 32 months.

Chart 3.2.7. Dynamics of Commercial Banks New Credits for the Period



In April-June 2021, the commercial banks' credit portfolio continued to demonstrate growth.

As of the end of June 2021, the commercial banks' credit portfolio increased by 6.7 percent year-to-date and amounted to KGS 173.5 billion. The credit portfolio grew due to the increase in the volume of credits in the national currency by 11.2 percent, up to KGS 121.2 billion. The credit portfolio in foreign currency decreased by 2.3 percent, down to KGS 52.3 billion. Credits denominated in US dollars in nominal terms were generally characterized by downward

In January-June 2021, the weighted average rates on new credits in the national currency decreased by 0.91 percentage points compared to January-June 2020, down to 16.33 percent. The interest rates in foreign currency decreased by 0.86 percentage points, down to 7.91 percent.

The credit market general concentration index was stable and formed at the level of 0.09, which corresponds to a low level of concentration and is equivalent to the division of the market among twelve banks. The sectoral concentration index was 0.32,

which is equivalent to three main credit sectors.

At the end of June 2021, the qualitative characteristics of the credit portfolio were as follows: the share of overdue credits in the credit portfolio increased by 0.4 percentage points year-to-date and amounted to 2.7 percent. The share of extended credits in relation to the credit portfolio is still at a high level; nevertheless, there is a downward trend from almost historically highest 15.9 percent in January down to 13.6 percent at the end of June (having not changed significantly since December 2020), which reflects a decrease of the stability risks in the banking system.

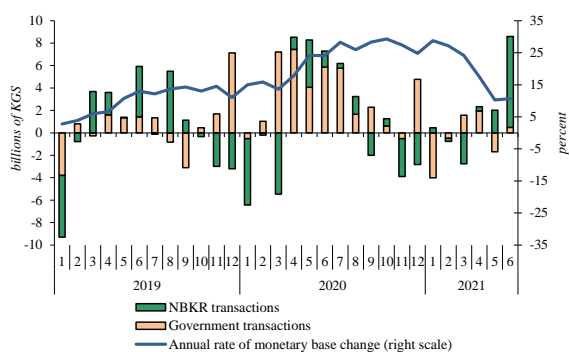
3.3. Dynamics of Monetary Indicators

Monetary Base

In the reporting quarter, the monetary base demonstrated an upward trend mainly due to the National Bank transactions.

According to the results of Q2 2021, the monetary base increased by 7.9 percent or KGS 11.3 billion compared to Q1 of the current year and amounted to KGS 153.1 billion.

Chart 3.3.1. Input of the Government's and NBKR Transactions in Change of Monetary Base



The National Bank transactions in the amount of KGS 10.5 billion were the main factor that influenced the growth of reserve money.

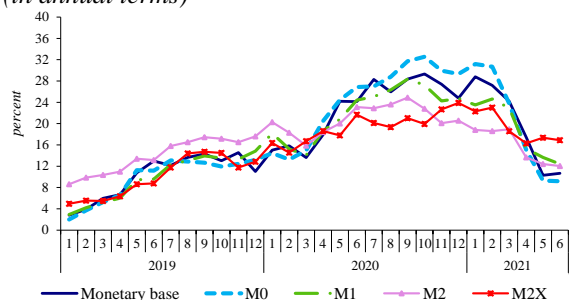
At the same time, the government transactions also had a positive effect on the expansion of reserve money by KGS 0.8 billion.

Reserve money maintained an upward trend and increased by 10.7 percent or KGS 14.8 billion in annual terms.

Monetary Aggregates

Chart 3.3.2. Nominal Growth Rates of Monetary Aggregates

(in annual terms)



In Q2 2021, the growth rates of all monetary aggregates demonstrated ongoing slowdown after their significant acceleration during the past years.

The monetary aggregates increased due to the growth of money outside banks and deposits that are part of broader aggregates. At the same time, at the end of Q2, money outside banks increased by 9.2 percent in annual terms, demonstrating slowdown from 23.7 percent in the previous quarter. This monetary indicator increased by 6.5 percent

during the reporting quarter.

In Q2 2021, the monetary aggregate M2X increased by 16.9 percent in annual terms and amounted to KGS 303.7 billion at the quarter-end. At the same time, the monetary aggregate M2X increased by 7.9 percent during the reporting period.

In the reporting period, deposits¹ included in M2X increased by 23.0 percent due to the growth of deposits in the national currency (by 15.7 percent) and in foreign currency (by 34.8 percent). Meanwhile, deposits in the national currency increased by 8.4 percent, and deposits foreign currency increased by 9.7 percent during the quarter.

Lending to the economy still demonstrate positive growth rates. In Q2 2021, the total volume of credits to the economy² increased by 13.4 percent in annual terms and amounted to KGS 180.5 billion at the quarter-end. The banking sector's credit portfolio increased mainly due to credits in the national currency (+19.5 percent), while lending in foreign currency made a less significant input (+1.3 percent). The volume of credits to the economy increased by 4.0 percent since the beginning of the reporting quarter.

¹ Deposits of individuals, legal entities and other financial-credit organizations, excluding deposits of the Government of the Kyrgyz Republic and non-residents.

² Credit to the economy is an indicator that reflects all the requirements of the banking system to the individuals, legal entities and other financial-credit institutions, in the form of issued credits, deposits and securities, accounted for together with their accrued interest, excluding credits to the Government of the Kyrgyz Republic and non-residents.

Chapter 4. Inflation Dynamics

Since the beginning of 2021, due to the increase in the general level of prices in the world food markets, there has been an acceleration of inflationary processes in Kyrgyzstan. This trend continued in the second quarter as well. The absence of seasonal deflation also made a positive contribution to CPI growth. There was a significant increase in prices for fuel and lubricants, continuing the vector of growth since the beginning of the year.

4.1. Consumer Price Index

Chart 4.1.1. Dynamics of CPI Structure
(quarter to the corresponding quarter of the previous year)

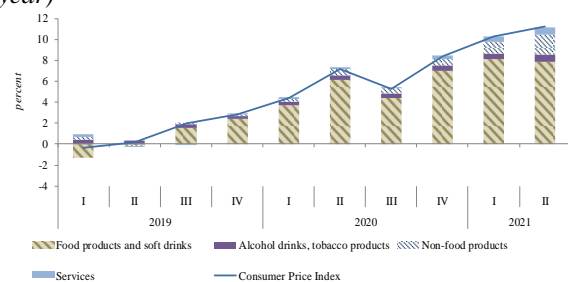


Chart 4.1.2. Dynamics of Food Prices' Contribution to Annual CPI
(month to the corresponding month of the previous year)

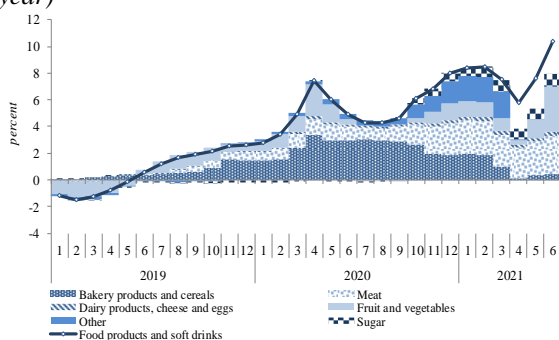
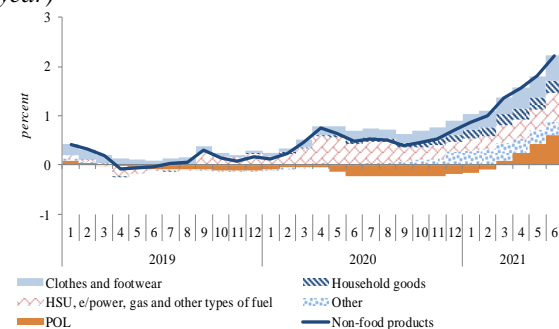


Chart 4.1.3. Dynamics of Non-Food Prices' Contribution to Annual CPI
(month to the corresponding month of the previous year)



In Q2 2021 (quarter to the corresponding quarter of the previous year), the annual inflation rate was **11.3 percent**. In the reporting period, various (approximately 70 percent) non-monetary factors (condition of fixed assets, logistics infrastructure, technological level of production) influenced consumer prices. It should be noted that at the end of Q2 there was no seasonal deflation common to this period of time, which was conditioned by a sharp increase in prices for vegetables.

In the reporting quarter, the food price index increased by 17.3 percent compared to Q2 2020.

In the reporting period, the following groups made the main contribution to the growth of food inflation: “meat”, “oils and fats”, “fruit and vegetables” and “sugar” (7.4 pp). World rise in prices for food products, increased exports of fruit and vegetables and meat products, late sowing of crops, unfavorable weather conditions (winter with little snow, dry summer) are among the main factors that influenced rise in prices for food products. The total contribution of the groups “bakery products”, “cereals”, “dairy products”, “cheeses”, “eggs”, as well as other food products constituted 0.6 percent.

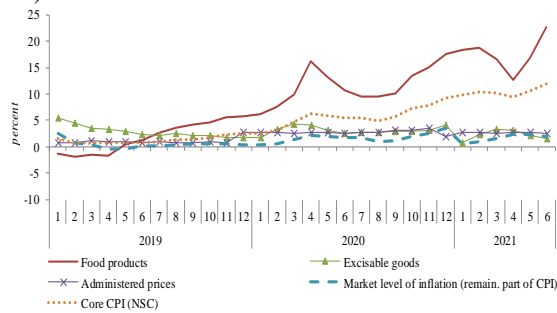
In Q2 2021, prices for non-food products increased by 6.4 percent compared to the same quarter of 2020. Rise in prices for the commodity group “clothes and footwear” (an increase by 4.3 percent) and in the category “gas, natural and liquefied” in the group “housing services” by 11.7 percent made the main contribution to the CPI for

non-food products. Household items and household appliances rose in price by 6.1 percent.

In the reporting period, prices for petroleum, oil and lubricants increased amid growth in purchase prices of the Russian producers, as well as due to the world rise in the oil prices.

Chart 4.1.4. Dynamics of Consumer Price Index by Groups of Commodities

(month to the corresponding month of the previous year)



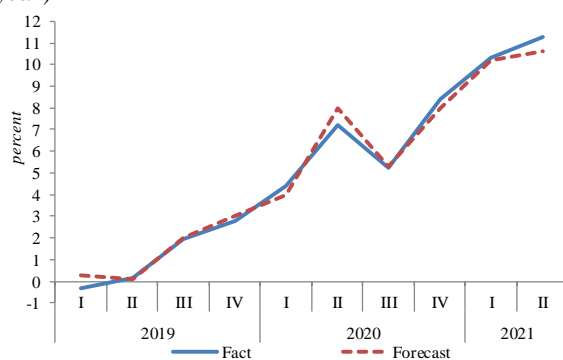
There was an increase in prices at the level of 4.1 percent in the paid services sector due to rise in prices for the groups “transport services” (14.5 percent), “recreation, entertainment and culture” (4.7 percent), “education” (1.9 percent), as well as growth in prices in the group “restaurants and hotels” (1.4 percent). In the reporting quarter, the price index for alcoholic drinks and tobacco products increased by 8.3 percent due to the planned increase in excise rates for tobacco products in early 2021.

Market inflation has been accelerating since the beginning of 2021, however, slightly slowed down in Q2 and constituted 1.9 percent in June 2021. In the reporting period, the core inflation indicator (excluding food and energy products), calculated by the National Statistical Committee of the Kyrgyz Republic, was 11.9 percent in annual terms.

4.2. Comparison of Forecast and Facts

Chart 4.2.1. Actual and Forecasted CPI Values

(quarter to the corresponding quarter of the previous year)

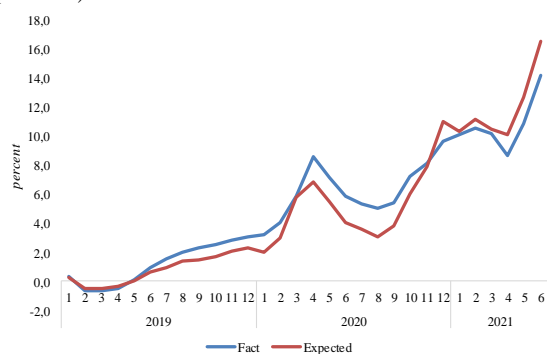


In Q2 2021, the actual inflation rate increased by 0.7 percentage points compared to the expectations of the National Bank.

Deviation of the expected inflation rate from the actual value was due to faster rates of food inflation amid long-lasting increase in prices in the world commodity markets.

4.3. Inflation Expectations¹

Chart 4.3.1. Actual Inflation Value and Expected Inflation of Enterprises
(percent)



The level of inflationary expectations in the Kyrgyz Republic is assessed through the survey of households (5,000 respondents) and enterprises (250 enterprises). The household survey has been conducted by a commercial organization since 2015 on a quarterly basis. Since 2018, the survey of households has been conducted by the National Statistical Committee of the Kyrgyz Republic on a quarterly basis, enterprises - on a monthly basis.

At the end of Q2 (June) 2021, the enterprises expected the inflation rate to increase by 2.4 percentage points compared to the actual inflation rate. According to the survey results in the reporting period, business representatives expected more accelerated growth of the inflation rate.

¹ According to the data provided by the NSC KR

Chapter 5. Medium-Term Forecast

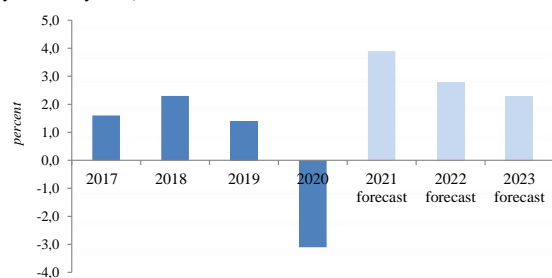
5.1. External Environment Proposals

5.1.1. Development Forecast of Main Trading Partner Countries

Russia

Chart 5.1.1.1. Real GDP Growth in Russia

(year to year)



Source: IMF, IA Bloomberg, Ministry of Economic Development of the Russian Federation, Bank of Russia

According to the Bank of Russia, the economic growth in Russia accelerated in Q2 amid steady inflation rate.

The Ministry of Economic Development of the Russian Federation has improved its estimate of the country's GDP growth rate for 2021: from 2.9 to 3.8 percent. The Russian economy is recovering faster compared to expectations and in June GDP growth reached the pre-pandemic level. Such dynamics is conditioned by investments growth, rise in prices for export goods, as well as the revival of business activity worldwide.

Forecast for GDP growth rates in 2022-2023 remained at the previous levels (3.2 and 3.0 percent, respectively). At the same time, the Ministry raised its expectations for investments growth for the current year - from 3.3 to 4.5 percent, as well as for retail trade turnover - from 5.1 to 6.9 percent.

Taking into account the current economic situation in Russia and worldwide, as well as the OPEC+ decision made in July to expand oil production, the Bank of Russia forecasts GDP growth in 2021 by 4.0-4.5 percent. In 2022-2023, the country's economy, according to the expectations of the Bank of Russia, will grow by 2.0-3.0 percent annually. In the medium term, the domestic demand dynamics will be largely determined by the growth rate of consumer and investment demand.

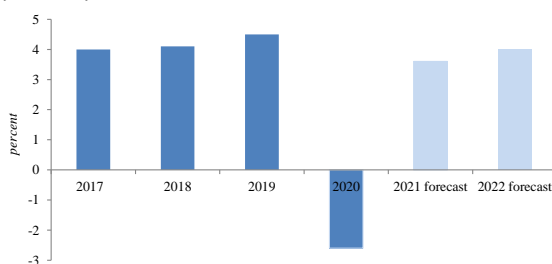
Taking into account increased inflationary expectations and processes in general, the Bank of Russia increased the inflation forecast for 2021 within the range of 5.7-6.2 percent, an increase by 1.0 percentage point compared to previous expectations. The annual inflation rate is expected to decrease down to 4.0-4.5 percent in 2022 and to remain close to 4.0 percent in the future in the context of the ongoing monetary policy.

At the same time, the Ministry of Economic Development of the Russian Federation also revised its estimate of inflation for the current year. According to the Ministry estimates, consumer prices in the country may grow by approximately 5.0 percent from January to December of the current year (instead of 4.3 percent, as previously expected).

Kazakhstan

Chart 5.1.1.2. Real GDP Growth in Kazakhstan

(year to year)



Source: IA Bloomberg, international financial institutions

The current economic forecasts in Kazakhstan for 2021 were revised upward, while the economic dynamics may be adjusted by the likely repeated outbreaks of coronavirus infection and fluctuations in the world oil prices.

The National Bank of the Republic of Kazakhstan informs that the domestic economy demonstrated recovery in the current year and in June 2021 the forecast for GDP growth was revised to 3.6-3.9 percent in 2021 with further acceleration up to 4.0-4.3 percent

in 2022 (previously expected growth for 2021 was within the range of 3.4-3.7 percent).

By the end of 2021, the Government of the Republic of Kazakhstan intends to ensure GDP growth at the level of 3.5-4.0 percent by providing employment for 1.2 million people, continuing to increase wages for the population, supporting agricultural activities, as well as increasing production in the pharmaceutical and medical industries.

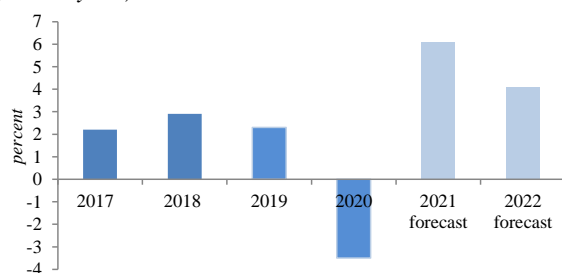
Taking into account the positive dynamics of the country's economic growth, a number of international organizations revised their estimates of GDP growth upward. Thus, the Asian Development Bank adjusted the forecast for the economic growth in Kazakhstan for the current year from 3.2 percent (April forecast) to 3.4 percent, and for 2022 it was kept unchanged at 3.5 percent. At the end of June 2021, the European Bank for Reconstruction and Development also increased its forecast for the country's GDP growth rate for 2021 from 3.0 percent to 3.6 percent and kept it unchanged at 3.8 percent for 2022. Based on the results of the economic growth of Kazakhstan in the first half of the year, the EBRD emphasizes the transition of the country's economy to a recovery growth path. According to the World Bank's updated forecast "Global Economic Prospects" made in June, Kazakhstan's GDP growth is expected at 3.2 percent in 2021, 3.7 percent in 2022 and 4.8 percent in 2023.

According to the NBRK preliminary estimates, the inflation rate is expected at 6.0-7.0 percent by the end of 2021 due to rise in prices for fuel and electricity, increased fiscal stimulus and inflationary expectations. In 2022, the inflation rate is forecasted to enter the target corridor of 4.0-6.0 percent due to weakening of the external inflationary pressure, in particular, the price stabilization in the world food markets and steady oil prices.

USA

Chart 5.1.1.3. Real GDP Growth in the USA

(year to year)



Source: IA Bloomberg, international financial institutions

The economic recovery is still affected by the spread of the coronavirus. Vaccination progress will continue to mitigate the public health crisis impact on the economy, however there are risks for the economic prospects.

According to the Fed data, expectations for demand have improved, however there is uncertainty about supply problems.

The IMF assumes that the US economy will grow by 7.0 percent in 2021 if

the US legislators will approve the president's economic initiatives. The IMF also emphasizes that in 2022 the US economy will continue its recovery from the pandemic effects and the country's GDP will increase by 4.9 percent.

The international rating agency Fitch Ratings has improved the forecast for the US GDP growth rate for 2021 from 6.2 to 6.8 percent.

The WB forecast for the US GDP growth rate was increased up to 6.8 percent (+3.3 percentage points) and the OECD – from 6.5 to 6.9 percent in 2021.

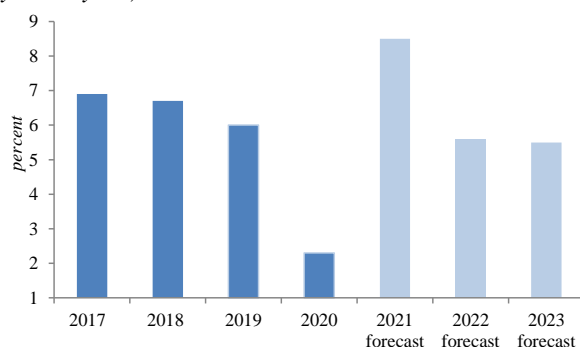
The Fed increased its forecast for the GDP growth rate for 2021 from 6.5 to 7.0 percent, for 2022 it remained unchanged at 3.3 percent and for 2023 – from 2.2 to 2.4 percent.

Progress in the labor market recovery is still insufficient for the Fed to consider it possible to reduce the volume of assistance to the economy. The regulator raised the inflation forecast for 2021 – from 2.4 to 3.4 percent, for 2022 – from 2.0 to 2.1 percent and for 2023 – from 2.1 to 2.2 percent. The regulator aims to achieve maximum employment and inflation rate at 2.0 percent in the long term. The US Federal Reserve System expects ongoing soft monetary policy until these results are achieved. At the same time, the regulator is ready, if

necessary, to adjust the monetary policy course if there are risks that may prevent from the goals achievement.

China

Chart 5.1.1.4. Real GDP Growth in China
(year to year)



Source: National Bureau of Statistics of the PRC, IA Bloomberg

The forecasts for economic growth in China were kept approximately within the same range of 8.0-9.0 percent for 2021.

The official target for GDP growth in the country for 2021 is more than 6.0 percent, a Bloomberg survey demonstrated expectations for economic growth of the country at 8.6 percent, in July, the World Bank and OECD raised their forecasts up to 8.5 percent, the forecast made in July by the international rating agencies Standard & Poors' and Fitch constituted 8.3 and 8.4 percent, respectively, the ADB's expectations

for economic growth remained unchanged at 8.1 percent. The IMF, on the other hand, decreased its forecast for China's economic growth up to 8.1 percent, explaining this measure by a reduction in public investment and general budget support from the state.

At the same time, there are risks of further economic recession amid possible expansion of measures taken to prevent rapid spread of coronavirus pandemic in the country due to the growth of new coronavirus infected cases.

According to the country's economic development plan for 2021, approved by the National People's Congress of China, the country's government has set an inflation target for 2021 at 3.0 percent. According to IMF forecasts, the inflation rate in China will slow down in 2021 to 1.2 percent from 2.4 percent in 2020, and in 2022 it will accelerate up to 1.9 percent. The analysts of Bloomberg and ADB expect prices to rise by 1.5 percent in 2021 and by 2.3 percent in 2022.

5.2. Medium-Term Forecast

The external sector parameters play a special role in the structure of the domestic economy. Such parameters become very significant when making forecasts in the context of a global economic shock. Assumptions regarding the price movement in the world commodity markets, the prospects for economic development in the trading partner countries of the Kyrgyz Republic and other important indicators of the world economic growth are set based on the forecasts of the world research agencies/institutions, official bodies of the countries and expert assessments.

The National Bank of the Kyrgyz Republic analyzes various scenarios for economic growth in our country under the influence of a number of external economic factors and develops appropriate options for the monetary policy directions.

In Q2 2021, there was ongoing gradual economic recovery in the Kyrgyz Republic. A slowdown in GDP growth was observed amid acceleration of the coronavirus infection next wave. There was a period of irrigation water shortage in the north of the country, which will negatively affect production output in the agricultural sector. Planned decline in gold production at the Kumtor Mine is expected in the current year. Ongoing work to bring legislation in line with the new Constitution introduces some uncertainty in the activities of the commercial sector, which will affect economic growth in the short term. It is also important to note that existing geopolitical risks in Central Asia can potentially complicate the crisis recovery. The aforementioned factors will have a restraining effect on the economic recovery.

Energy prices are expected to become stable during the next two years, the current forecast assumes oil prices within the range of USD 65-70 per barrel in the near future. The process of vaccination against coronavirus in the world remains the main factor in the oil price movement. A slowdown in food price increase is expected in the international food markets, as there are risks related to crop yield and weather. Inflationary pressure in the developed markets (USA, EU) resulted from large-scale fiscal support can also contribute to growth in prices in the world commodity markets.

A stable economic recovery in Russia and Kazakhstan is forecasted in the medium term. Despite initiated monetary conditions tightening in the trading partner countries, in 2022, the economies are expected to return to the pre-crisis level and the trade within the EAEU is forecasted to intensify. Such trends can only be possible in the absence of restrictive measures and ongoing vaccination of the population.

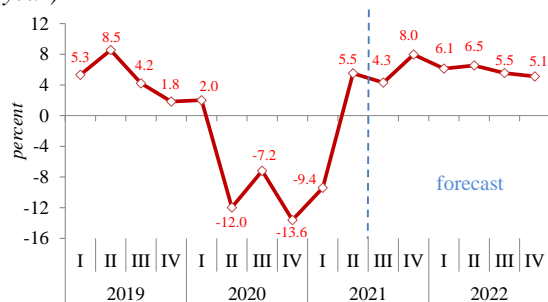
In 2021, net inflow of remittances is expected to increase due to the active economic recovery abroad. Accordingly, the domestic consumer demand in the Kyrgyz Republic will receive additional support. At the same time, export, excluding gold, is assumed to increase in the current year amid revival in external demand, as well as due to rise in prices. In 2021, import will continue to grow due to increase in prices and the low base of the previous year.

In general, the experts assume that the negative production output gap will decrease in the forecast period, the potential GDP growth rate will be observed only by the end of 2022. At the same time, it should be noted that the economic growth potential of Kyrgyzstan decreased due to the shocks of 2020. The economic recovery will require some time and reforms on the part of the Cabinet of Ministers of the Kyrgyz Republic. Taking into account all conditions and risks, the forecast for GDP growth is decreased compared to the previous monetary policy report. Prices will continue increasing, however slowdown is expected by the end of 2021.

The following 2021-2022 forecast was made for the key macroeconomic development indicators of the Kyrgyz Republic taking into account the outlined trends in the trading partner countries' economic growth, as well as the price movement in the world commodity markets in the medium term.

Chart 5.2.1. Forecast of Real GDP

(quarter to the corresponding quarter of the previous year)



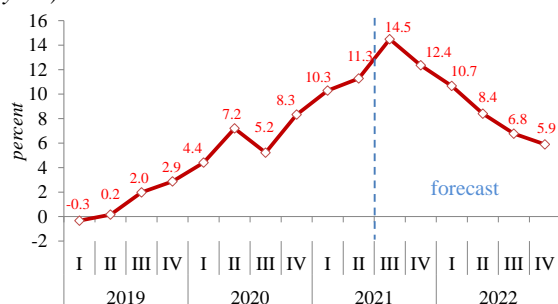
Despite a strong economic recovery in the trading partner countries and improved epidemiological situation in the country by the end of Q2, the economic recovery of the Kyrgyz Republic was slower compared to the previous expectations. Suspension of the economic recovery in the country is mainly due to a decrease in gold production at the Kumtor Mine and a reduction of production output in the agricultural sector. Irrigation problems in Chui region contributed to a

decline of production output in the agricultural sector.

According to the baseline scenario, at the end of 2021, GDP growth in the Kyrgyz Republic is expected at approximately 3.0 percent (-1.0 percentage point compared to the previous forecast). At the same time, the forecast for 2022 was revised upward to 5.7 percent (5.0 percent in the previous forecast), reflecting a faster recovery amid lower levels of 2021 compared to previous expectations. In 2021, the economic growth in Kyrgyzstan is expected at about 4.9 percent excluding the enterprises of the Kumtor Mine (the previous forecast assumed GDP growth by 0.9 percentage points in 2021, excluding the enterprises of the Kumtor Mine).

Chart 5.2.2. Inflation Forecast

(quarter to the corresponding quarter of the previous year)



selected food products until the end of the current year.

Thus, taking into account all expected internal and external factors and risks, the inflation rate at the end of 2021 (December 2021/December 2020) is forecasted in the range of 11-12 percent, the average annual inflation rate may approach the level of approximately 12.0 percent. In 2022, the average inflation rate is expected at approximately 7.0 percent to make 6.5 percent by the end of the year.

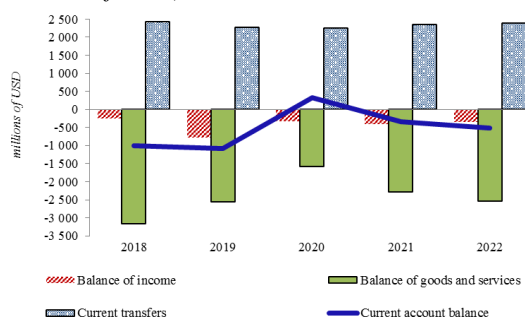
Forecast for the Balance of Payments in 2021-2022¹

In the reporting period, the forecast for the indicators of the external sector of the economy was made under the influence of stable economic recovery worldwide due to relaxing of the restrictive measures. However, the recovery of the economies is uneven across countries. Thus, according to the expectations of the National Bank's experts, the rate of economic recovery in Kyrgyzstan will be slightly lower than the recovery rate in the main partner countries.

The expectations for the main items of the current account were adjusted taking into account the trends of the actual period, updated estimates on the forecast for the trade balance of goods and the foreign investors' income. In general, the current account deficit is expected to increase up to 5.6 percent to GDP in 2021.

Chart 5.2.3. Forecast Data on Current Account

(millions of USD)



In Q2 2021, acceleration of the food inflation rate mainly due to rise in prices for meat and vegetable oil, passively raised the inflation forecast for the current year.

Additional upward pressure on inflation is expected from the supply in the agricultural sector due to a significant decrease in forecasts until the end of 2021 conditioned by the weather conditions being unfavorable for the harvest, as well as ongoing upward trend in the world prices for

In the reporting quarter, updated expectations for gold exports and an increase in external demand for other goods, accompanied by rise in prices, influenced the export forecast. The expected export volumes for 2021, taking into account the data of the actual period, are expected at the level of 2020. The supplies of goods from the textile and apparel production sector, as well as re-export positions will provide significant support for the country's exports, meanwhile gold exports will decline due to expected reduction in metal

production.

The import forecast was adjusted taking into account the data of the actual period, as well as revised rates of economic development in the country. The value of imports is expected to increase by 28.9 percent amid the low base of 2020 and an acceleration in price growth in the world commodity markets due to a slow recovery in the logistics and commodity chains. An increase in imports is expected mainly due to the consumer goods and the intermediate goods. An increase in the supplies of energy products to the country is

¹ The forecast was made taking into account additional estimates of the National Bank of the Kyrgyz Republic to the actual period.

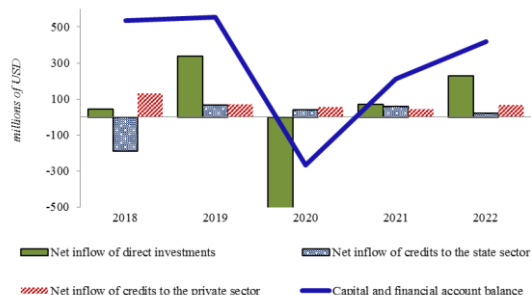
forecasted at the level of 41.6 percent, while the imports of other goods are estimated to increase by 26.9 percent.

The current report updated the expectations for private transfers inflows due to faster recovery of the labor migrants’ remittances inflow in the actual period and their positive dynamics maintaining until the end of the year. An increase in the net inflow of transfers to the private sector is expected at 14.1 percent, while the official transfers are expected to be below the level of 2020.

Ongoing economic activity, measures taken by the governments of the region to vaccinate the population contribute to expected slight revival in the tourism sector. In turn, the group “transport services” will be formed under the influence of the recovery in passenger and cargo transportation and increased prices for this type of services amid growing demand for them.

Chart 5.2.1.4. Forecast Data on Capital and Financial Account

(millions of USD)



Trends for development of the items in the financial and capital account in 2021 remain under the negative influence of the pandemic trends, and therefore there were no significant changes in the estimates of financial flows in the current report.

The net direct investment inflow is forecasted to resume gradually. As before, the main volume of capital inflows on the financial account will be provided by other investments. The balance of the item “other investments” will be formed under the

influence of an increase in foreign liabilities of the public and private sectors. Servicing of previously obtained private sector loans will remain significant with a moderate inflow of private foreign investment.

Thus, the balance of payments will be formed negative, which implies financing the gap from the international reserves of the National Bank.

In 2022, the revised forecasts for the balance of payments indicators in 2021, as well as the adjustment of external economic conditions influenced the dynamics of the external sector indicators. The current account deficit is expected to continue expanding in 2022 and constitute 6.0 percent of GDP. The growing trade balance deficit, positive dynamics in the inflow of private transfers and the gradual recovery of some types of international services will influence this indicator. The forecast for economic activity recovery will contribute to the growth of the trade turnover in the country. In the context of expected growth in external demand, export is forecasted to increase by 8.4 percent due to traditional export items. The economic development in the country and an increase in incomes of the population amid expected rise in the world prices will create preconditions for growth in imports by 5.8 percent.

Thus, the trade balance deficit is expected to increase by 3.6 percent. A positive dynamics of current transfers due to the labor migrants’ remittances is forecasted to increase by 3.6 percent compared to the level of 2021.

In 2022, inflow of foreign capital on the capital and financial account is expected to be more stable, a significant part of the proceeds thereon will be provided by direct foreign investments and other investments to the private sector. Public sector liabilities will continue increasing in 2022. The upward trend in servicing previously received loans and borrowings will remain stable.

The following risks are still observed in the elaborated forecast of the balance of payments of the Kyrgyz Republic for 2021-2022:

- uncertainty associated with the COVID-19 pandemic in the world and the political situation in the country;

- the risks associated with the Kumtor Mine development and other precious metal deposits;
- volatility in the world prices for oil and gold;
- deterioration of the economic situation in the trading partner countries;
- volatility in the exchange rate of the main trading partner countries;
- growing debt burden of the public and private sectors.

Annex 1. Key Macroeconomic Indicators

(quarter to the corresponding quarter of the previous year, if otherwise is not indicated)

Indicator	Unit of measure	2020				2021	
		Q1	Q2	Q3	Q4	Q1	Q2
1. Demand and supply¹ (real growth rates, if otherwise is not indicated)							
Nominal GDP, per quarter	mln. KGS	117 073,2	124 716,3	173 357,9	183 197,1	118 362,0	152 382,0
GDP	%	2,0	-12,0	-7,2	-13,6	-9,4	5,5
GDP, excluding Kumtor	%	1,4	-14,3	-7,6	-12,3	-4,5	11,6
Domestic consumption	%	3,7	-24,0	-12,1	-2,3	-1,6	
Investment	%	-23,7	-33,1	-16,9	-22,5	-17,6	
Net export	%	-16,3	-74,0	-26,8	1,2	19,6	
<i>GDP production:</i>							
Agriculture	%	1,3	0,8	1,0	1,4	0,9	1,5
Industry	%	3,8	-3,2	-8,8	-18,9	-17,9	-5,6
Construction	%	-2,5	-12,7	-5,7	-25,6	-19,8	-10,3
Services	%	1,7	-17,9	-10,8	-10,6	-5,5	14,5
including trade	%	3,4	-31,2	-16,0	-15,4	-12,1	35,9
2. Prices²							
CPI	%	104,4	107,2	105,3	108,4	110,3	111,3
CPI, in annual terms as of the end of period	%	105,9	105,8	105,4	109,7	110,2	114,2
Core inflation	%	103,5	105,8	105,3	108,1	110,1	110,6
<i>CPI by main groups of goods and services:</i>							
Food products	%	108,1	113,4	109,7	115,4	117,9	117,3
Non-food products	%	100,9	102,1	101,6	102,0	103,7	106,4
Alcohol drinks and tobacco products	%	104,2	105,3	105,7	106,3	106,0	108,3
Services	%	101,0	101,0	100,0	102,3	103,3	104,1
<i>CPI, classified by character:</i>							
Excisable goods	%	103,1	103,3	102,8	103,4	102,1	102,3
Regulated prices	%	102,7	102,7	102,8	102,8	102,7	102,7
Market inflation rate (the rest of CPI)	%	100,8	101,9	101,3	102,6	101,0	102,2
3. External sector³ (in percent to GDP)							
Trade balance	% to GDP	-27,6	-22,2	-18,3	-18,7	-19,6	-28,4
Current transaction account	% to GDP	-9,0	-4,0	0,4	4,9	4,2	-2,4
Export of goods and services	% to GDP	34,7	34,2	33,4	31,8	31,3	30,9
Import of goods and services	% to GDP	61,5	56,2	53,0	52,8	53,7	62,1
4. USD exchange rate, as of the end of period							
	KGS	80,8100	75,9887	79,6000	82,6498	84,7792	84,6640
5. Monetary sector							
NBKR policy rate, as of the end of period	%	5,00	5,00	5,00	5,00	5,50	6,50
Rate of "overnight" deposit, as of the end of period	%	2,75	2,75	2,75	2,75	3,25	4,25
Rate of "overnight" credit, as of the end of period	%	5,75	5,75	5,75	5,75	6,00	7,00
Average interest rates of operations in the interbank credit market, per quarter	%	3,55	3,85	3,79	3,79	4,15	5,21
<i>of which:</i>							
of REPO transactions	%	3,55	3,85	3,97	3,84	4,15	5,21
of credits in national currency	%	-	-	-	-	-	-
of credits in foreign currency	%	-	-	2,50	2,50	-	-
Weighted average yield of 7-day notes, as of the end of period	%	3,97	3,95	3,95	4,01	4,50	5,26
Weighted average yield of 14-day notes, as of the end of period	%	4,15	4,32	4,20	4,50	5,03	5,64
Weighted average yield of 28-day notes, as of the end of period	%	4,31	4,52	4,37	4,62	5,15	6,12
Weighted average yield of 91-day notes, as of the end of period	%	4,48	4,65	4,70	4,70	5,45	5,43
Weighted average yield of 182-day notes, as of the end of period	%	-	-	-	-	-	-
Monetary base	%	13,6	24,1	28,3	24,8	24,2	10,7
Money outside banks (M0)	%	14,9	26,9	31,7	29,3	23,7	9,2
Monetary aggregate (M1)	%	14,0	24,4	28,4	24,7	22,9	12,4
Narrow money supply (M2)	%	15,9	23,1	24,9	20,5	18,9	12,0
Money supply (M2X)	%	16,7	21,7	21,0	23,9	18,6	16,9

¹ Estimates of the National Bank of the Kyrgyz Republic on the basis of the data provided by the National Statistics Committee of the Kyrgyz Republic

² Source: National Statistics Committee of the Kyrgyz Republic

³ Coefficients were calculated on the basis of the sliding annual data for the last 4 quarters. Data for Q2 are preliminary

Annex 2. Glossary

Balance of payments is a report, which reflects aggregate economic transactions between the residents and non-residents within a certain period of time.

Consumer price index reflects changes in the prices for goods and services purchased by the standard consumers for non-production purposes. This index is among inflation rate measures, which is based on comparing the value of basic goods basket consumed by the population and weighted in accordance with the share of these goods in the aggregate consumption.

Core inflation is inflation, which excludes short-term, structural and seasonal changes of prices: the growth in prices of goods due to the seasonal, the external factors and the administratively established tariffs is excluded from the calculation of the inflation rate.

Core CPI index is a price excluding the cost of food products, electric energy, gas, and other fuels.

Deposits included in M2X are the deposits of the individuals and legal entities, as well as the deposits of other financial-credit institutions, however, the deposits of the government and nonresidents are excluded.

Dollarization is extensive use of the US dollars in the domestic currency circulation of the country, which possess own national currency.

Inflation is the upward trend in the general level of prices within the certain period of time, which is determined based on the value calculation for the basket of goods and services weighted by the structure of consumer expenses of the standard household. The consumer price index is an indicator, which characterizes the inflation rate in the Kyrgyz Republic.

Monetary aggregate is the money supply classified according to degrees of liquidity: M0; M1; M2; M2X.

M0 – cash in hands.

M1 – M0 + residents' transferable deposits in the national currency.

M2 – M1 + residents' time deposits in the national currency.

M2X – M2 + settlement (current) accounts and residents' deposits in foreign currency.

Monetary base is the obligations of the National Bank on cash in circulation, and the obligations of the National Bank to other depository corporations in the national currency.

Net balance of payments is a difference between receipts from the foreign countries and payments transferred to the foreign countries.

Net balance of trade is a difference between the cost of export and import.

Nominal effective exchange rate (NEER) index is a weighted average value of the nominal exchange rates, which excludes the price tendency in the country under review with respect to the prices in the trading partner countries.

Notes are the discount securities, issued in circulation by the National Bank of the Kyrgyz Republic. By decision of the Monetary Regulation Committee of the National Bank, the notes can be issued for the period from 7 to 364 days. The notes maximum profitability is set to be equal to the policy rate as of the auction day.

Other depositary corporations are all resident financial corporations, except for the central bank, which main activities are aimed at financial intermediation and which issue obligations included into the national definition of the broad money stock (M2X).

Policy rate is a monetary policy tool, which represents an interest rate set by the central bank and is used as the basic reference point when determining the value of monetary resources in the economy.

Real effective exchange rate (REER) index represents the weighted average value of the nominal effective exchange rates adjusted by the value corresponding to the relative change in prices in the trading partner countries. REER is determined by calculation of the weighted real exchange rates of the currency in the country with respect to the currencies of the main trading partner countries.

REPO transactions are the operations on purchase/sale of the government securities in the secondary market with an obligation of their resale/repurchase on a certain date in the future at the pre-agreed price.

State Treasury Bills are the short-term (3-, 6-, 12-month) discount government securities of the Government of the Kyrgyz Republic. The Ministry of Finance of the Kyrgyz Republic is the issuer of the ST-Bills. Placing issues of the ST-Bills is made through weekly auctions conducted by the National Bank of the Kyrgyz Republic. Direct participants enjoy the right to participate in the auctions. The owners of the ST-Bills of the Kyrgyz Republic can be both the legal entities and the individuals. The admission of the foreign investors to the market of the ST-Bills is not limited. The transactions in the secondary market of the ST-Bills are conducted through the electronic trading system of the National Bank of the Kyrgyz Republic, which allows the participants to conduct transactions on purchase/sale of the ST-Bills from their workplaces.

State Treasury Bonds are the long-term government securities of the Government of the Kyrgyz Republic with the interest income (coupon) and maturity over one year. The issuer of the ST-Bonds is the Ministry of Finance of the Kyrgyz Republic. The National Bank of the Kyrgyz Republic is the general agent servicing the issues of the ST-Bonds.

Annex 3. Abbreviations

ADB	Asian Development Bank
CBRF	Central Bank of the Russian Federation
COVID-19	CO rona VI rus D isease 2019
CPI	Consumer Price Index
EAEU	Eurasian Economic Union
EBRD	European Bank for Reconstruction and Development
EDB	Eurasian Development Bank
EU	European Union
FAO	Food and Agricultural Organization of the United Nations
FOB	Cost at the Exporter's Border (Free on Board)
Fed	US Federal Reserve System
GDP	Gross Domestic Product
IBCM	Inter-Bank Credit Market
IEA	International Energy Agency
IMF	International Monetary Fund
KR	Kyrgyz Republic
MNE RK	Ministry of National Economy of the Republic of Kazakhstan
NBKR	National Bank of the Kyrgyz Republic
NBRK	National Bank of the Republic of Kazakhstan
NEER	Nominal Effective Exchange Rate
NSC	National Statistical Committee
OECD	Organization for Economic Cooperation and Development
OPEC+	Organization for Petroleum Exporting Countries
POL	Petroleum, oil, lubricants
PRC	People's Republic of China
RA	Republic of Armenia
RB	Republic of Belarus
REER	Real Effective Exchange Rate
RK	Republic of Kazakhstan
ST-Bonds	State Treasury Bonds
ST-Bills	State Treasury Bills
USA	United States of America
WGC	World Gold Council