

# **Inflation Report**

**July 2010**

## ***Inflation Report***

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This publication contains a description of consumer price developments in the republic and its regions (oblasts), the analysis of key inflation factors, informs on monetary policy decisions of the National Bank of the Kyrgyz Republic and provides an inflation forecast for the forthcoming period. The report is published quarterly in Kyrgyz, Russian and English languages.

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### ***Annual Report of the National Bank of the Kyrgyz Republic***

This publication is a last year statement of the National Bank of the Kyrgyz Republic (NBKR). It contains brief information about the country's economic development and monetary policy, financial statements of the NBKR, general information about the NBKR, and statistic annexes. It is published in Kyrgyz, Russian and English languages.

### ***Bulletin of the National Bank of the Kyrgyz Republic***

This monthly publication contains statistic data for major macroeconomic indicators and sectors of economy of the Kyrgyz Republic. It is published in Kyrgyz, Russian and English languages.

### ***Balance of Payments of the Kyrgyz Republic***

Balance of Payments of the Kyrgyz Republic reflects trends of external sector development, data of the payment balance, foreign trade, international reserves, external debt, and international investment position of the Kyrgyz Republic. It is published on quarterly basis in January, May, July, and October in Kyrgyz, Russian and English languages.

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The objective of this document is to officially publish the statutory acts of the NBKR in order to provide commercial banks and general public with regulatory documents and information about NBKR activities, and to popularize the banking legislation of the Kyrgyz Republic. It is published, as a rule, once a month in Kyrgyz and Russian languages.

### ***Press Release of the National Bank of the Kyrgyz Republic***

Press Release of the NBKR contains the description of events related to the National Bank and banking system, major financial market data for the week and other information for mass media, legal entities and individuals. It is published on a weekly basis in Kyrgyz and Russian languages.

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## Chapter 1. Economic situation in the Kyrgyz Republic

### 1.1. Demand and supply on commodities and services market

#### 1.1.1. Demand

According to the preliminary data, in January to June 2010 the volume of nominal GDP at current prices was Som 81.5 billion, having increased by 5.0 percent in real terms against the volume of GDP for the comparable period of 2009 (in January to June 2009 GDP decreased by 1.8 percent).

Events in the south of the country had a significant impact on the economic development, economic slowdown from 116.4 percent in the first quarter of 2010 to 105.0 percent in January to June 2010. The main reason for the economic slowdown is the decline in trading. Thus, according to the preliminary data in January to June 2010 the total trade turnover, compared to the first half of 2009, was decreased to 11.6 percent (in January to June 2009 growth rate amounted to 3.2 percent).

At that, maintaining the positive economic growth against the backdrop of prevailing conditions is largely due to the slow economic growth rate in the previous year caused by the decline in manufacture in the previous year and general growth retardation in services sector (“low base” effect).

**Table 1.1.1. Real GDP growth rates by expenditure**

(quarter/period to the corresponding quarter/period of the previous year, percent)

	2009				2009	2010
	I	II	III	IV		I
<b>Consumed GDP</b>	<b>-1.3</b>	<b>-2.1</b>	<b>4.5</b>	<b>5.1</b>	<b>2.3</b>	<b>16.4</b>
Final consumption	-7.9	-9.9	2.3	2.5	-2.6	0.7
Individual consumption	-8.8	-11.4	1.9	2.8	-3.2	0.8
Households	-9.8	-13.0	1.9	2.8	-3.7	1.0
NCOSH	-0.2	1.5	1.0	3.1	1.5	-1.9
Public institutions	0.0	1.1	1.8	2.5	1.5	-0.1
Collective consumption	6.7	7.0	8.6	0.4	5.0	-1.0
Gross capital formation	-51.1	-52.5	-26.6	-25.1	-34.3	27.3
Net export of services and goods	-33.7	-55.9	-47.5	-30.5	-42.3	-35.5
Export	6.6	8.7	-7.1	-16.5	-4.6	23.3
Import	-14.2	-22.6	-21.8	-21.5	-20.5	0.9

Source: NSC KR

The structure of GDP by expenditure in the first quarter of 2010<sup>1</sup>, the largest contribution to growth is marked by exports (14.2 percentage points) and the growth of gross capital formation (2.8 percentage points) which in turn was caused by planned increase in production of export-oriented industries (Kumtor Goldfield), growth of investments into the fixed capital (construction of HPP “Kambar-Ata-2”).

GDP deflator amounted to 105.2 percent in January to June 2010.

<sup>1</sup> Hereinafter: reference to earlier periods is conditioned by lack of information for the second quarter of 2010.

**Table 1.1.2. Structure of GDP deflator**  
(year-to-date, percent to the corresponding period of the previous year)

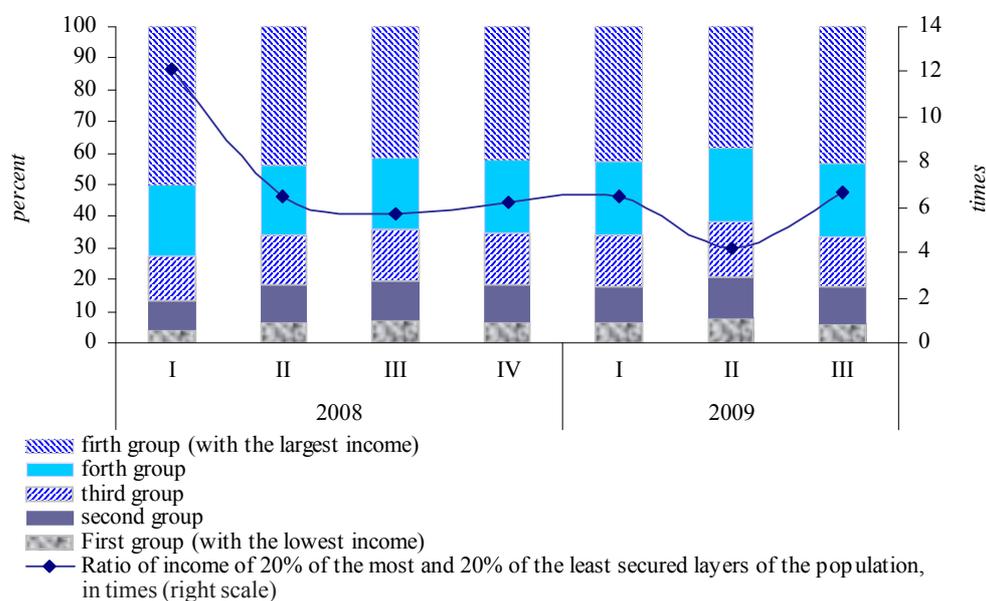
	2009				2010	
	I	II	III	IV	I	II
<b>Gross Domestic Product</b>	<b>109.3</b>	<b>107.9</b>	<b>101.9</b>	<b>102.1</b>	<b>103.5</b>	<b>105.2</b>
Agriculture, hunting & forestry	104.2	102.8	91.5	91.5	98.6	96.4
Mining industry	121.5	124.5	122.7	117.5	105.1	85.9
Processing industry	96.9	103.9	101.7	107.3	110.3	110.7
Electricity, gas, and water generation and distribution	139.4	132.1	131.7	126.4	149.5	142.1
Construction	117.0	111.9	109.0	107.0	105.7	106.7
Trade, repair	111.4	107.3	104.2	103.0	102.7	104.1
Hotels and restaurants	116.6	112.1	108.3	105.6	100.4	101.2
Transport and communication	123.3	120.1	117.2	115.1	108.4	107.3
Financial activity	110.3	91.5	90.8	88.9	95.8	100.5
Real estate transactions, rent	110.8	110.1	109.5	107.2	101.2	100.5
Public administration	147.9	137.5	131.6	135.5	95.4	103.2
Education	133.9	137.9	123.4	116.2	89.9	99.4
Health and provision of social services	84.0	86.6	82.4	81.0	88.8	149.8
Provision of utility and personal services	131.2	126.4	122.2	120.0	109.2	106.2
Net tax on products	86.8	85.9	87.1	86.5	94.5	101.1

Source: NSC KR

According to the preliminary data, in January to May 2010 real wages showed a 9.5 percent growth against 4.0 percent in the same period of 2009.

A differentiation of household income has still remained high. A distribution of the total volume of cash earnings by five groups of population develops in favor of highly remunerative groups. Thus, on the results of the nine months of 2009 the share of income of the most well-to-do group accounted for 43.5 percent of the total volume of household income, having increased by 2.0 percentage points compared to this indicator in the similar period of 2008. The share of income of 20 percent of the least privileged population decreased by 0.9 percentage points amounted to 6.4 percent.

**Chart.1.1.1. Composition of household money income by quintile groups**  
(year-to-date)



According to the preliminary data, in January to May 2010, an inflow of funds of individuals through transfer systems was noted to increase. The total volume of net inflow in January to May 2010 increased by USD 88.8 million or by 32.2 percent compared to this parameter in 2009.

**Table 1.1.3. Remittances of individuals in money transfer systems**  
(*mln. USD*)

	2006	2007	2008	2009	Jan-May 2009	Jan-May 2010 **
<b>Balance</b>	<b>430.3</b>	<b>625.5</b>	<b>1 138.2</b>	<b>893.2</b>	<b>276.0</b>	<b>364.8</b>
<b>Inflow</b>	<b>470.0</b>	<b>688.2</b>	<b>1 205.5</b>	<b>966.7</b>	<b>300.4</b>	<b>398.5</b>
CIS countries	436.7	648.8	1 141.4	894.4	271.2	375.3
Kazakhstan	0.0	7.0	27.9	31.4	9.8	13.6
Russia	436.6	641.8	1 113.5	862.9	261.4	361.8
Other	0.0	0.0	0.1	0.0	0.0	0.0
Non-CIS countries	33.4	39.4	64.1	72.3	29.2	23.2
Belgium	0.0	0.1	0.5	0.5	0.2	0.1
Great Britain	0.9	0.9	1.8	1.4	0.5	0.6
Germany	0.0	0.1	0.2	0.7	0.2	3.7
USA	32.2	38.3	61.4	69.5	28.1	18.8
Other	0.1	0.0	0.2	0.3	0.1	0.0
<b>Outflow</b>	<b>39.7</b>	<b>62.7</b>	<b>67.3</b>	<b>73.6</b>	<b>24.4</b>	<b>33.7</b>
CIS countries	38.5	60.2	65.0	71.8	23.8	33.0
Kazakhstan	0.0	0.2	2.5	0.7	0.1	0.1
Russia	38.4	60.0	62.5	71.1	23.6	32.9
Other	0.0	0.0	0.0	0.0	0.0	0.0
Non-CIS countries	1.2	2.5	2.3	1.8	0.6	0.7
Belgium	0.0	0.1	0.1	0.2	0.0	0.2
Germany	0.0	0.2	0.4	0.4	0.1	0.1
USA	1.1	2.1	1.7	1.1	0.5	0.3
Other	0.1	0.1	0.1	0.1	0.0	0.1

\* Anelik, Blizko, Contact, Migom, MoneyGram, Western Union, Unistream, Zolotaya Korona, Leader, Sibcontact, Bystraya Pochta, Allyur and other money transfer system and remittances via the PE "Kyrgyzpochtasy"

\*\*preliminary data

The south events happened in June 2010 increased uncertainty about future developments in the government sector.

According to the preliminary data of the Central Treasury of the Ministry of Finance of the Kyrgyz Republic, the state budget deficit in January to June 2010 was Som 1.3 billion or 1.6 percent to GDP (in the comparable period of 2009 the state budget surplus amounted to Som 554.8 million or 0.8 percent to GDP). Meanwhile, excluding the tax on Kumtor gross income the state budget was run with deficit of Som 4.1 billion or 5.1 percent to GDP.

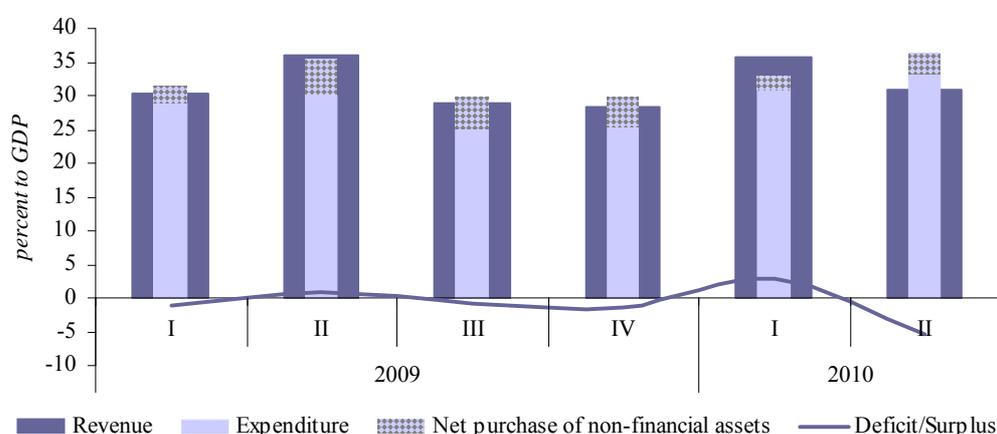
Total state budget expenditures for operating activities in January to June 2010 were Som 26.2 billion or 32.1 percent to GDP, having increased by Som 4.0 billion or 2.1 percentage points to GDP against the comparable indicator for the corresponding period of 2009. Increase in budget current expenditures tends to continue. For instance, expenditures for wages and contributions to the Social Fund of the Kyrgyz Republic,

as well as to social benefits, in January to June 2010 accounted for 58.6 percent of total state budget expenditure for operating activities, having increased by 6.4 percentage points against the comparable indicator for the corresponding period of 2009.

In the reporting period, the net outflow of funds for operations on purchases of non-financial assets amounted to Som 2.1 billion and that was by Som 1.9 billion or 47.4 percent lower as compared to the corresponding period of 2009.

State budget revenue and received official transfers have been by increased 1.1 percent against the comparable indicator for the corresponding period and amounted to Som 27.0 billion or 33.1 percent to GDP. Thus, tax revenues and nontax revenues provided a positive contribution to revenue growth by 10.7 percentage points while the inflow of official transfers was declined, which made a negative contribution in the amount of 9.6 percentage points.

**Chart.1.1.2. State budget implementation**  
(year-to-date)



In January to June 2010, the volume of investments in fixed assets increased by 2.7 percent against the comparable period of the previous year and made Som 13.2 billion, while under the results of first half of 2009 the volume of investments in fixed assets increased by 16.4 percent. A significant slowdown of the investments growth in fixed assets is primarily due to the decline of investments in the energy sector on the background of the completing construction of HPP “Kambar-Ata-2”. In the branch structure, in January to June 2010, the highest share of investments in fixed assets fell on branches of transport and communication (23.9 percent), production and distribution of electricity, gas and water (16.0 percent) as well as on mining (14.8 percent).

**Table 1.1.4. Investments in fixed assets by sources of financing**

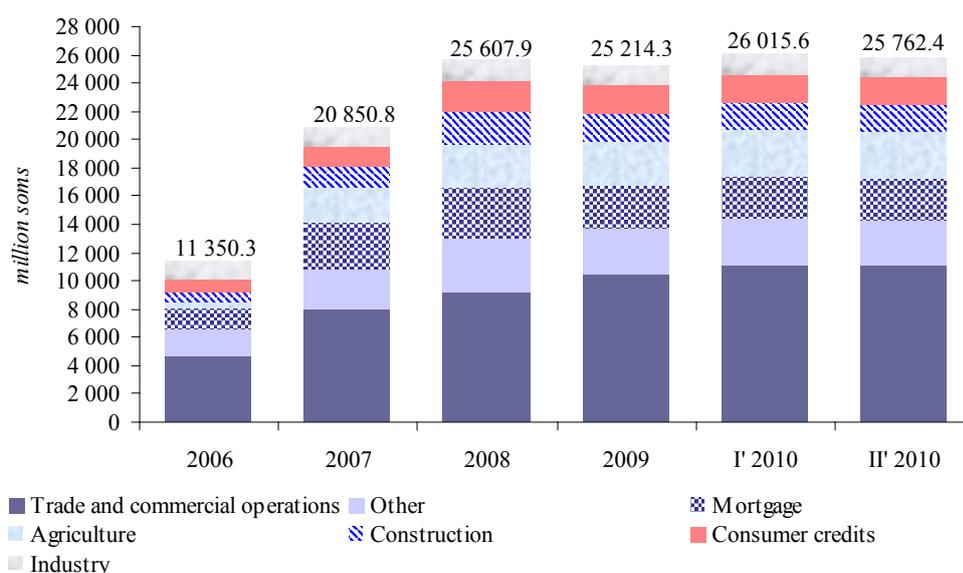
	million soms		percent to total	
	Jan-Jun 2009	Jan-Jun 2010	Jan-Jun 2009	Jan-Jun 2010
<b>Total</b>	<b>12 031.4</b>	<b>13 180.6</b>	<b>100.0</b>	<b>100.0</b>
<b>Domestic investment</b>	<b>9 203.8</b>	<b>9 856.3</b>	<b>76.5</b>	<b>74.8</b>
Republican budget (including emergency funds)	1 907.7	347.3	15.9	2.6
Local budget	180.8	152.7	1.5	1.2
Funds of enterprises and organizations	3 137.7	3 600.1	26.1	27.3
Bank credit	12.4	1 603.9	0.1	12.2
Population assets	3 965.0	4 149.8	33.0	31.5
Humanitarian aid	0.2	2.5	0.0	0.0
<b>Foreign investment</b>	<b>2 827.6</b>	<b>3 324.3</b>	<b>23.5</b>	<b>25.2</b>
Foreign credit	1 863.3	1 906.9	15.5	14.5
Foreign direct investment	672.2	1 104.7	5.6	8.4
Foreign grants and humanitarian aid	292.1	312.7	2.4	2.4

Source: NSC KR

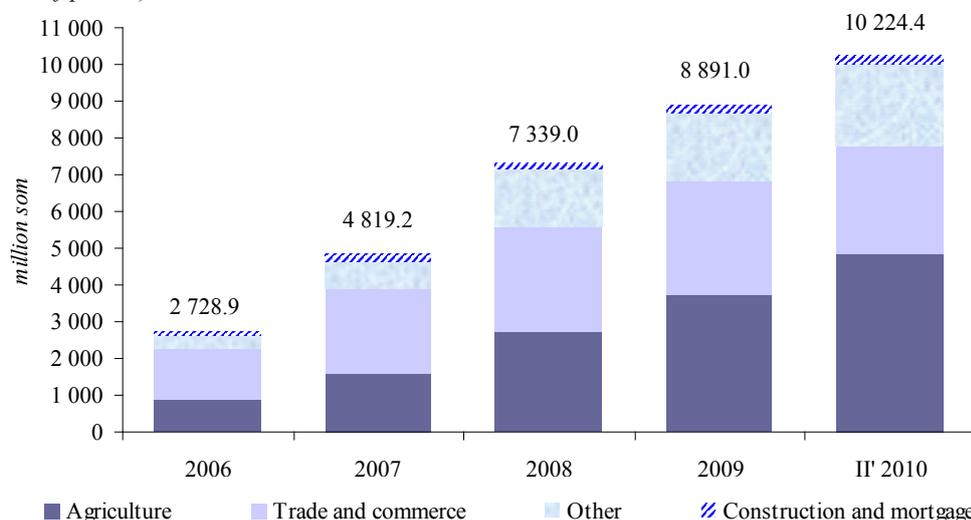
The volume of commercial banks' credit portfolio increased by 2.2 percent (in 2009 the growth of similar indicator amounted to 0.6 percent) to make Som 25.8 billion as of the end of June 2010. However, compared with the data at the end of the first quarter of 2010 there was a decline in lending of the economy by 1.0 percent, which along with data in trade volume is the first sign of the weakening of the economic activity in the country.

**Table 1.1.5. Sectoral commercial bank loan portfolio allocation**

	Jan-Jun 2009		2009		Jan-Jun 2010	
	total, mln.som	rate of growth, percent	total, mln.som	rate of growth, percent	total, mln.som	rate of growth, percent
Trade and commercial operations	9 721.3	5.3	10 457.7	13.2	11 090.9	6.1
Agriculture	3 087.8	5.2	3 084.3	5.1	3 336.8	8.2
Industry	1 543.5	5.4	1 388.8	-5.2	1 377.0	-0.8
Mortgage	3 348.6	-6.9	3 087.9	-14.1	2 934.3	-5.0
Construction	2 166.1	-10.9	1 950.3	-19.8	1 930.6	-1.0
Consumer credits	1 987.1	-6.2	2 028.0	-4.3	1 879.4	-7.3
Other	3 597.5	-6.0	3 217.4	-16.0	3 213.3	-0.1
<b>Credit portfolio</b>	<b>25 451.8</b>	<b>-0.6</b>	<b>25 214.3</b>	<b>-1.5</b>	<b>25 762.4</b>	<b>2.2</b>

**Chart 1.1.3. Sectoral commercial bank loan portfolio allocation***(end of period)*

Along with this, in the first half of 2010 there was an increase in lending by nonbank financial institutions. Thus, according to the preliminary data, at the end of June 2010 the loan portfolio of NBFIs excluding the Development Fund of the Kyrgyz Republic amounted to Som 10.2 billion (39.8 percent of the loan portfolio of commercial banks) having increased by 15.2 percent compared with the given indicator for beginning of this year. In the allocation of loan portfolio of NBFIs the largest share accounted for the financing of agriculture (47.1 percent) and trade (29.0 percent). Lending of the agriculture in January to June 2010 increased by 29.4 percent. At that, the lending of trade operations declined by 3.8 percent (the growth of trade lending at the end of 2009 accounted for 7.8 percent). Despite positive growth rates of the economy lending by nonbank financial institutions in the first half of 2010 the political events happened in April to June will likely have a negative impact on their activities until the end of the year.

**Chart 1.1.4. NBFIs sectoral loan portfolio allocation***(end of period)*

### 1.1.2. Supply

The major contribution to GDP growth in January to June 2010 года was made by processing industry, construction, production and distribution of electricity, gas and water. The volume of total supply of goods and services in January to June 2010 was provided by the products of trade (15.0 percent), agriculture (14.8 percent), processing industry (13.7 percent), transport and communication sectors (9.8 percent) of GDP total volume.

**Table 1.1.6. Contributions to growth/reduction in GDP**

	Jan-Jun 2009		Jan-Jun 2010	
	rate of growth/ percent	input in growth, p.p.	rate of growth/ percent	input in growth, p.p.
<b>Gross Domestic Product</b>	<b>-1,8</b>	<b>-1,8</b>	<b>5,0</b>	<b>5,0</b>
Gross added value	-1,5	-1,5	4,3	4,3
Agriculture, hunting & forestry	2,5	0,4	0,2	0,0
Mining industry	9,2	0,0	7,5	0,0
Processing industry	-21,2	-3,1	49,7	5,6
Electricity, gas, and water generation and distribution	-13,0	-0,2	12,7	0,2
Construction	-9,9	-0,4	7,2	0,3
Trade, repair	4,6	0,8	-9,0	-1,6
Hotels and restaurants	4,4	0,1	-8,0	-0,1
Transport and communication	6,9	0,6	0,2	0,0
Financial activity	7,9	0,1	2,0	0,0
Real estate transactions, rent	2,0	0,1	-4,4	-0,2
Public administration	4,4	0,2	1,5	0,1
Education	1,1	0,1	0,0	0,0
Health and provision of social services	-0,2	0,0	-0,8	0,0
Provision of utility and personal services	-0,7	0,0	-2,9	-0,1
Net tax on products	-1,8	-0,3	5,0	0,6

Source: NSC KR

In the first quarter of 2010, physical volume index of industrial production amounted to 141.8 percent against 81.2 percent in January to June of 2009. Growth of industrial production was marked both for enterprises dealing with developing the *Kumtor* gold-ore field and for enterprises not engaged in gold extraction. For instance, in January to June 2010, the growth of industrial production excluding *Kumtor* enterprises made 126.6 percent.

The increase in the volume of industrial products was achieved due to a considerable growth in metallurgic production and in metallic finished-product output (by 1.7 times), other nonmetallic mineral products (by 1.9 times), textile and clothing manufacture (1.5 times), as well as in production of electric power, gas and water (112.7 percent).

Current growth rates are due, as noted earlier, to the effect of “low base” established in the previous year. In this case, the low base, mainly accounts for the first half of 2009 because this period, in particular, had been marked with the negative growth of the economy, while in the second half of the year was marked by significant growth in the number of sectors (agriculture, construction).

In the reporting period, the turnover of trading operations decreased by 11.6 percent. The decrease in the volumes of wholesale trade had been caused due to the deterioration in the terms of trade with the countries – main trading partners as well as the impact of political events in the Kyrgyz Republic.

**Table 1.1.7. Dynamics and structure of trade operations**

	Jan-Jun 2009		Jan-Jun 2010	
	share, percent of the total	rate of growth, percent	share, percent of the total	rate of growth, percent
<b>Trade</b>	<b>100,0</b>	<b>3,2</b>	<b>100,0</b>	<b>-11,6</b>
Trade in cars and their spare parts	3,5	4,1	3,5	-12,4
Car maintenance	0,6	-3,3	0,5	-12,2
Retail trade in motor oil	6,3	33	8,7	-12,7
Wholesale trade	35,3	-2,3	31,6	-18,5
Retail trade	54,1	3	55,5	-6,9
Repair of household appliances	0,2	-12,3	0,2	-19,6

Source: NSC KR

## 1.2. Monetary trends

### Monetary base<sup>1</sup>

Monetary base increased by 4.2 percent in the second quarter of 2010 (in the second quarter of 2009 the increase was 14.8 percent) and made Som 41.0 billion as of July 1, 2010; the year-on-year monetary base increased by 20.6 percent.

In the second quarter of 2010, the monetary base changed (by Som -1.7 billion), to a far greater degree, due to the Governments operations that increased the monetary base by Som 4.9 billion, whereas the National Bank's operations decreased the monetary base by Som 3.3 billion. For comparison: in the second quarter of 2009 the monetary base increase made Som 4.4 billion; meanwhile, the Government's operations increased the monetary base by Som 4.6 billion, whereas the National Bank's operations decreased the monetary base by Som 0.2 billion.

As of July 1, 2010 money in circulation in the second quarter of 2010 increased by 7.0 percent and made Som 36.9 billion (in the second quarter of 2009, the increase made 14.7 percent). Year-on-year, the increase in money circulation made 25.0 percent.

In the second quarter of 2010, in the structure of monetary base, the share of money in circulation increased from 87.7 to 90.1 percent as compared to the end of July 2010. Correspondingly, the share of funds on correspondent accounts of commercial banks in the National Bank decreased from 12.3 to 9.9 percent.

<sup>1</sup> The monetary base is the obligation of the National Bank of the cash put into circulation, and the obligations of the National Bank to other depository corporations (commercial banks) in the national currency, according to the new Regulation adopted by NBKR Board "On the analytical balance sheet of the National Bank of the Kyrgyz Republic" (Resolution of the NBKR № 51 / 1 as of December 28, 2009)

## **M2 Aggregate**

M2 money supply was Som 45.9 billion as July 1, 2010, and increased by 7.4 percent in the second quarter of 2010 (in the second quarter of 2010 the reduction of M2 was 15.3 percent). Year-on-year, growth of M2 money supply was 26.4 percent.

An increase in the volume of the M2 monetary aggregate was caused by the increase in currency in hands by 8.5 percent and deposits in national currency by 3.6 percent, including the decrease in the volume of other deposits (time deposits) by 15.2 percent and of transferrable (demand deposits) – by 15.1 percent.

## **M2X Aggregate**

Having increased by 1.4 percent in the second quarter of 2010, the volume of M2X broad money, comprising the deposits in foreign currency was Som 57.1 billion as of July 1, 2010 (in the similar period of 2009, the increase of M2X was 13.3 percent. Year-on-year M2X broad money increased by 22.6 percent.

A change in M2X broad money in the second of 2010 resulted from the 8.5 percent increase in money in hands and 8.3 percent decrease in the total volume of deposits<sup>1</sup>, meanwhile, deposits in national currency increased by 3.6 percent, and those in foreign currency decreased by 17.3 percent (in the second quarter of 2009 the change in M2X was observed due to the increase in currency in hands by 13.4 percent and the increase in the total volume of deposits by 13.2 percent).

The M2X currency mix changed as follows as of second quarter of 2010:

- the share of currency in hands increased from 57.8 to 61.9 percent;
- the share of currency in hands increased from 18.1 to 18.5 percent;
- the share of currency in hands decreased from 24.1 to 19.6 percent.

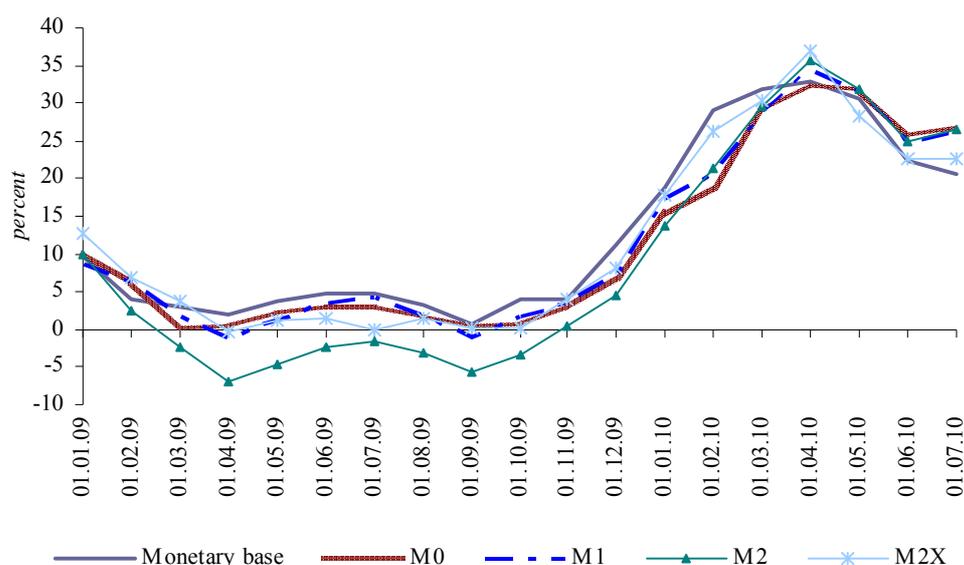
The multiplier of M2X broad money, as an indicator of financial intermediation degree, decreased compared to the end of March in the second quarter of 2010 from 1.431 to 1.393 as of end of June (1.371 as of end of June, 2009).

Velocity of M2X broad money circulation in the second quarter of 2010 decreased from 4.0 as of end of March to 3.8 as of end of June (4.3 as of end of June, 2009). Accordingly, the return rate of velocity – the monetization of the economy coefficient, calculated based on M2X monetary aggregate increased in the second quarter of 2010 from 24.8 percent as of end of March to 26.0 percent as of end of June (23.0 percent as of end of June, 2009).

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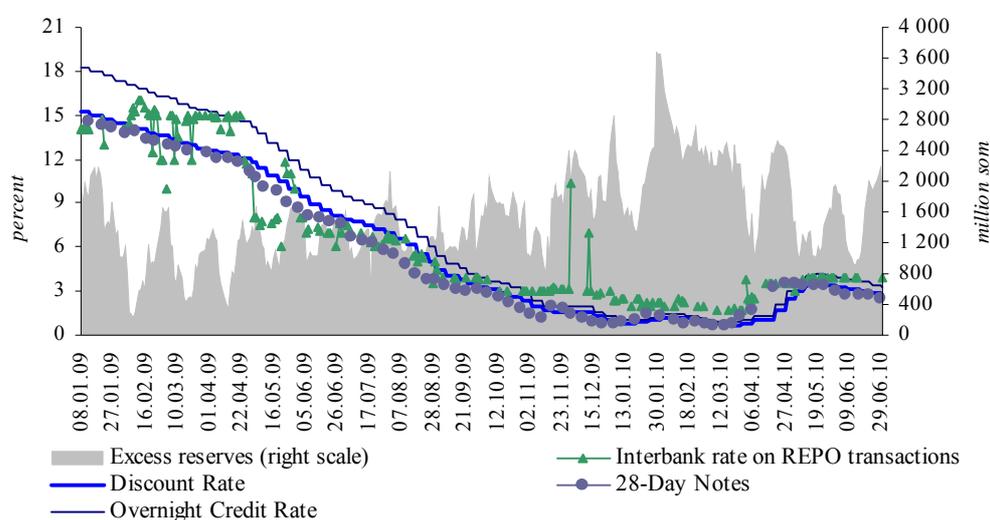
<sup>3</sup> According to the banking system analytical data sheet, the deposits comprise only the deposits of individuals and legal entities, as well as the deposits of other finance and credit institutions, with the Government deposits and the deposits of nonresidents excluded.

Chart 1.2.1. Annual nominal growth rates of monetary aggregates



In the second quarter of 2010, the formation of the situation on the financial markets was influenced with deteriorating political situation and the uncertainty of the economy. Negative expectations of economic agents in April led to an outflow of deposits from the banking system. In addition, fluctuations in the level of excess reserves in commercial banks were accompanied by an increase in demand in the interbank loan market on borrowed resources and value increase.

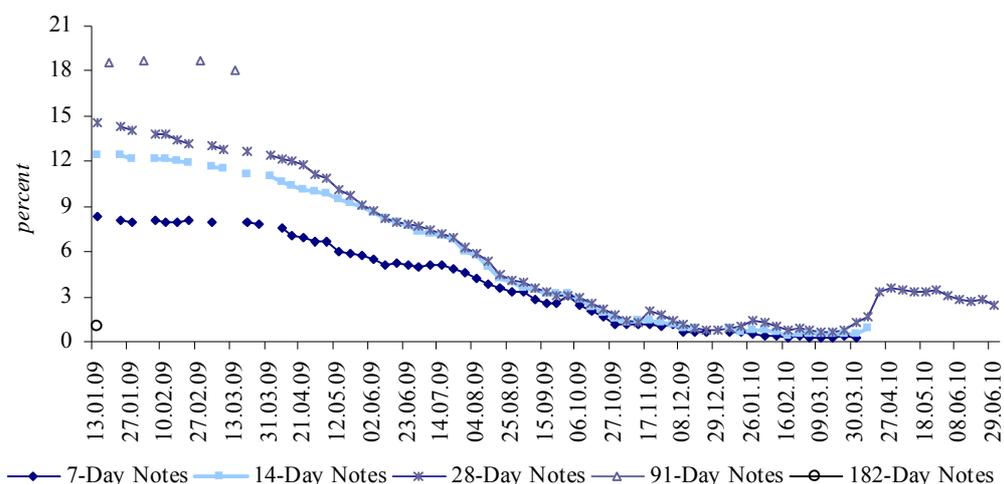
Chart 1.2.2. Dynamics of money market rates



In April to June 2010 the National Bank continued to use NBKR notes as a monetary policy tool for withdrawal of excess liquidity from the banking system. After April events in the commercial banks liquidity level has decreased, and therefore it was decided to reduce the emissions of the NBKR notes. At the same time, the demand for notes has significantly decreased compared with demand in the previous quarter which was associated with withdrawal from the market of several significant investors and a change in the level of liquidity in certain commercial banks. However, an increase in the yield of

all segments of this market was observed as a whole. Auctions for placement of the 7-, 91- and 182- day NBKR Notes were not conducted; only one auction on 14-day notes was conducted. Weighted average yield of the 14- day notes increased by 0.3 percentage points against the yield of the first quarter of 2010 and made 0.9 percentage points, 28-day notes by 2.1 percentage points down to 3.0 percent. Against the comparable period of 2009, the yield of the NBKR 14-day notes decreased by 8.3 percentage points, 28-day notes by 6.9 percentage points.

**Chart 1.2.3. Dynamics of the yield of NBKR notes**



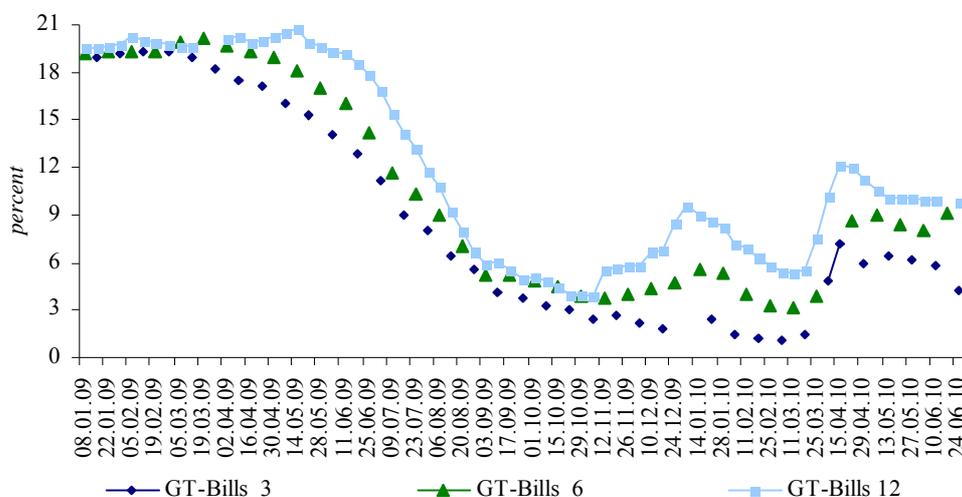
The discount rate defined as the average value of yield of the 28-day NBKR notes, which had developed at the recent four auctions, has been increased and made 2.7 percent as of end of June. The rate for overnight credits made 3.2 percent as of the end of the period. In the reporting quarter the National Bank issued the overnight credits to banks for the total amount of Som 843.0 million with average rate of 2.6 percent.

In the second quarter, the Ministry of Finance maintained the volumes of weekly ST-Bonds supply remained at the first quarter level. The interest in these securities did not exceed supply much due to withdrawal of one of the major market participants and the arrival of new ones. Nevertheless, during the whole quarter the ST-Bonds yield was increasing. As a whole for April to June 2010, ST-Bonds were placed for the amount of Som 287.9 million with weighted average yield of 16.8 percent (+4.8 percentage points).

The emitter slightly increased the volumes of ST-Bills placement in the primary market of ST-Bills, whereas the demand for them decreased more than by one third as compared to the indicator of the first quarter. But despite this, the demand for ST-Bills exceeded its supply. The income dynamics ST-Bills during the quarter was slightly fluctuated, reaching its maximum in mid-April and minimum in late June which was connected with the volatility in the demand due to liquidity fluctuations in some banks. As compared to the indicator of the previous quarter the overall weighted average yield of ST-Bills was increased by 3.7 percentage points for the reporting period to make 9.5 percent. Yield of the 3-month ST-Bills increased by 4.1 percentage points to make 5.8 percent, the 6-month ST-Bills increased by 4.4 percentage points to make 8.6 percent and 12-month ST-Bills by 3.5 percentage points to make 10.5 percent. The overall level of the

ST-Bills yield decreased by 8.3 percentage points against this indicator in the comparable quarter of 2009; the decrease in the yield was observed in all market segments.

**Chart 1.2.4. Dynamics of yield of ST-Bills**



In the second quarter of 2010 demand for borrowed resources in the inter-bank market of credit resources was slightly increased due to the fluctuations in excess reserves in commercial banks. The rise in price for interbank loans in national and foreign currencies increased mainly under the impact of change in the discount rate and in the rates in other segments of monetary market. In the second quarter of 2010, the overall amount of REPO operations decreased by 2.1 percent against the similar indicator for the previous quarter and amounted to Som 1 265.0 million while their weighted average rate increased by 1.6 percentage points to make 3.7 percent. The total volume of interbank loans in national currency was formed in the amount of Som 76.5 million and the weighted average interest rate was 4.9 percent. Compared with similar indicators in the second quarter of 2009, the weighted average interest rate on REPO operations fell by 6.4 percentage points, on interbank loans in national currency by 3.7 percentage points.

In the segment of operations in foreign currency, the volume of transactions in some equivalent made Som 106.4 million, the weighted average interest rate quoted at 3.8 percent this was 2.8 percentage points more than the weighted average value of this indicator for the previous quarter.

In the reporting quarter, the NBKR did not conduct auctions for ST-Bills(s) sales on REPO terms and through swap operations with commercial banks. Commercial banks did not place funds on time deposit accounts in the NBKR.

### 1.3. External economic conditions

#### Trade Balance

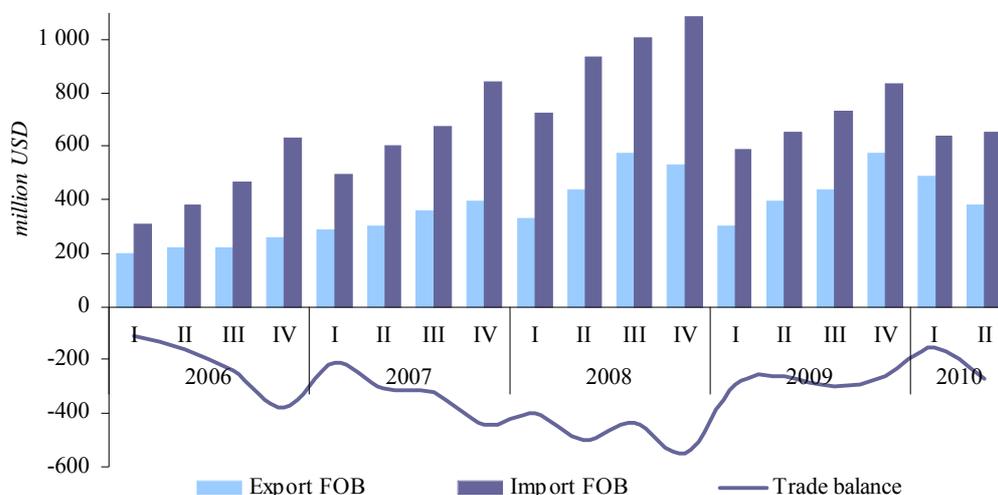
Pursuant to the preliminary data, trade balance deficit of the Kyrgyz Republic decreased by 2.6 percent as compared to the net export in the second quarter of 2010 and made US\$ 270.1 million.

The external sales<sup>1</sup> volume amounted to US\$ 1 031.2 million in the reporting period,

<sup>1</sup> NSC KR and SCC KR data including NBKR adjustments.

having thus exceeded by 0.3 percent. Kyrgyzstan's export transactions were dominated by the CIS countries – 53.1 percent of commodity turnover, the share of non-CIS countries had, respectively, 46.9 percent.

**Chart 1.3.1. Foreign trade**



In the second quarter of 2010, export of goods (at FOB prices)<sup>1</sup> developed in the volume of US\$ 380.5 million that exceeded this parameter for the similar period of 2009 by 1.4 percent or US\$ 5.2 million in absolute terms. Export transactions growth to the non-CIS countries increased by 1.0 percent or by US\$ 7.8 million, whereas the volume of export to the CIS countries slightly decreased by 1.5 percent or by US\$ 2.6 million.

In the reporting period, shares of main articles of the functional structure<sup>2</sup> of export were as follows: intermediate goods – 36.0 percent from the total export volume, consumer goods – 27.3 percent, raw materials – 26.2 percent, energy products – 6.1 percent.

Intermediate goods was the largest export item, the volume of growth of which constituted US\$ 120.0 million despite its small growth increased by 1.1 percent. The commodity structure of this category is dominated by export of gold amounting to US\$101.2 million having increased by 17.8 percent. Export of gold increased mainly due to the volume growth in 1.2 times, while the production volume decreased by 8.8 percent.

Export of consumer goods increased by 31.1 percent and made US\$ 91.1 million. The main contribution to increase was provided by export of non-food products, the volume of which increased by 48.1 percent or by US\$ 17.7 million. Mainly, they include supplies of clothes and clothes accessories that increased in value terms in 1.7 times (by US\$ 17.6 million). In the second quarter of 2010, export of incandescent electric lamps decreased by 11.0 percent or by US\$ 0.4 million, which was provided by decrease of physical volume of export. In the structure of food products, supplies of vegetables increased in 11.6 percent or by US\$ 1.6 million, supplies of fruits in 38.8 percent or by US\$ 2.5 million, mineral waters and non-alcohol beverages by 59.4 percent or by US\$

<sup>1</sup> NSC KR and SCC KR data including NBKR adjustments.

<sup>2</sup> NSC KR and SCC KR data including NBKR adjustments.

0.6 million, vegetable oil and other fats produced from milk increased in 2.6 times or или by US\$ 0.4 million, milk and dairy products, except vegetable oil and cheese by 3.6 percent or by US\$ 0.1 million. Export growth for the above products was due to the growth of physical volume of export, mainly.

Export of raw materials constituted US\$ 87.3 million and exceeded by 3.0 percent. The main share of raw materials export was accounted for inorganic chemicals (84.6 percent out of the total export of raw materials), their export in volume terms increased in 1.4 times in the reporting period whereas export prices decreased by 20.1 percent. Eventually, export in value terms of this type of goods increased by 13.2 percent or by US\$ 8.6 million. Due to the volume growth of supply, the export of raw stock increased in 1.8 times or by US\$ 0.7 million. As a result, the reduction in volume of tobacco exports fell by 13.4 percent or US\$ 1.0 million, while exports of cotton decreased by 77.2 percent or US\$ 1.2 million.

Export of energy resources in the reporting period decreased by 61.9 percent and was US\$ 20.3 million. The share of this category of goods in total exports decreased from 16.2 percent in the second quarter of 2009 to 6.1 percent in the second quarter of 2010. This trend is attributable to reduced re-exports of petroleum products to third countries. Supplies of kerosene decreased by 69.7 percent or US\$ 30.7 million, diesel fuel by 67.6 percent or US\$ 3.4 million, automobile gasoline by 100.0 percent or US\$ 2.3 million. This trend is attributable to reduced volume of supply with an increase in prices of petroleum products. As a result of increased supply in Kazakhstan value of exports of electricity increased in 4.4 times and amounted to US\$ 3.2 million.

In the geographical structure of exports the CIS countries played a dominated role (60.5 percent of total exports), while leading partner countries became Switzerland (22.9 percent), USA (12.8 percent) and UAE (9.3 percent). Main partners in the group of CIS countries were Russia (25.2 percent) and Kazakhstan (9.5 percent).

Import of goods at FOB prices in the first quarter of 2010 decreased by 0.3 percent and amounted to US\$ 650.7 million. The fall in imports was recorded from non-CIS countries by 4.3 percent, while from the CIS countries an increase in imports by 2.9 percent was observed.

According to the functional structure<sup>1</sup> of the largest product categories in import operations were energy products (30.5 percent of total imports), consumer goods (29.0 percent) and intermediate goods (23.8 percent).

Import of energy products in the second quarter of 2010 increased by 23.6 percent and amounted to US\$ 214.9 million. Increasing import duties on petroleum products has led to an increase in import prices by 63.0 percent and reduced the volume of fuel oil by 22.0 percent. Thus, the value of import of jet fuel rose by 18.3 percent (US\$ 13.2 million), gasoline by 11.4 percent (US\$ 5.6 million). Import of diesel fuel was increased by 76.2 percent (US\$ 17.3 million) which was due both to the increase in price and quantitative measure caused by stronger domestic demand due to spring field

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<sup>1</sup> According to NSC KR and SCC KR.

work. Price and quantity factors are also reflected in the import of fuel oil which grew in 3.1 times (US\$ 4.0 million). Natural gas import increased by 16.2 percent (US\$ 1.8 million) due to the increase of volume supplies by 16.7 percent.

Cost of imported consumer goods in the reporting period constituted US\$ 204.0 million and decreased by 5.8 percent. Due to the reduction of the number of imported automobiles by 26.0 percent and fall in prices by 17.0 percent of the value of imports for this category of goods declined by 38.8 percent or US\$ 13.3 million. Import of clothes supplies and clothes accessories were declined by 24.8 percent or US\$ 4.6 million. Due to the reduction of physical volume of imports there was a decrease in import of meat and meat products (by US\$ 1.9 million), chocolate, coffee, tea (US\$ 3.1 million), sugar (for US\$ 2.2 million) milk and dairy products (US\$ 0.6 million). Imports of beer decreased by US\$ 1.5 million under the influence of reducing both price and quantity factors. The increase in revenue was recorded on the medication (by US\$ 5.9 million) and vegetable oil (by US\$ 3.7 million).

In the group of intermediate goods, the volume of import amounted to US\$ 167.8 million which is lower than in the corresponding period in 2009 by 2.5 percent. Import by commodity group “iron and steel” fell by 22.7 percent or US\$ 5.5 million, which was due to the reduction of quantitative indicators. By reducing the price index by 19.3 percent, import of fabrics was declined by 16.4 percent or US\$ 1.8 million. Increasing the volume of supply has led to an increase in the value of the proceeds of rubber tires (by 24.0 percent or US\$ 2.1 million) and fertilizer (in 2.4 times or US\$ 4.7 million).

Import of wheat in the commodities in the second quarter of 2010 was decreased by 31.4 percent or US\$ 5.2 million which was due to a decline in import prices, while physical volume of supplies remained at the same level of the similar period of 2009.

According to the geographical structure, the principal share of import came from CIS countries – 57.1 percent. The share of non-CIS countries, respectively, amounted to 42.9 percent. The main partner countries of Kyrgyzstan to import transactions were Russia (33.5 percent of total import), China (16.6 percent), Kazakhstan (12.9 percent) and USA (6.0 percent).

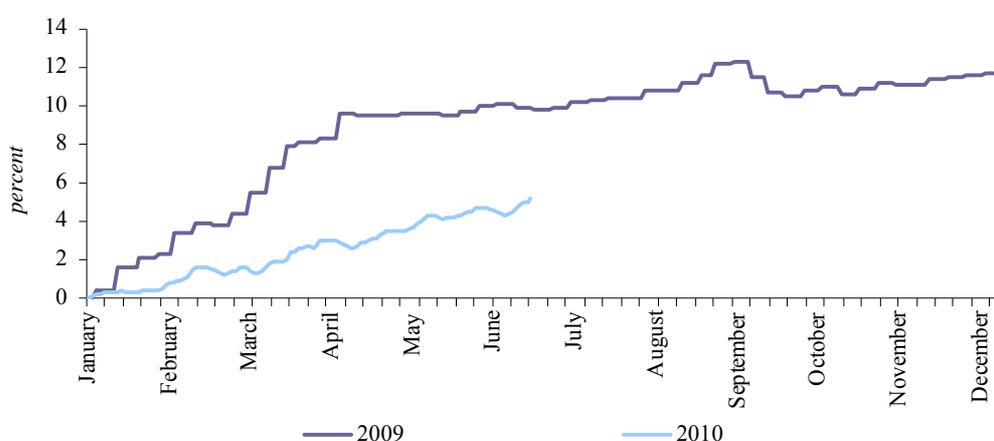
#### **1.4. Exchange rate**

In the second quarter of 2010, on the foreign exchange market there was a tendency for weakening of Kyrgyz Som towards USD. This trend was due to both external and internal factors. The external factors include exchange rate dynamics of the pair USD/EUR on the world markets, where strengthening of USD was noted during the entire quarter. The main determining factor in the domestic market was the ratio between supply and demand of currencies, namely the reduction of foreign currency inflows from exports of goods and services with increasing demand for it (the closure of borders with countries-trade partners of Kazakhstan and Uzbekistan). In addition, the summer is usually characterized by increased foreign currency inflows, including the tourists, as well as lower costs of banks to service imports, in current circumstances have differed from traditional trends, i.e. currency inflow from tourism activities is substantially decreased in the current year.

With the view of maintaining stability of the national currency, the National Bank of the Kyrgyz Republic conducted US dollar sale and purchase operations at the inter-bank foreign exchange sales. For the second quarter the sales by the NBKR of US dollars increased by 67.1 percent, amounting to US\$ 90.1 million and the volume of operations on purchase of US dollars increased by 25.0 percent, amounting to US\$ 2.3 million (in comparison with the second quarter of 2009, the volume of NBKR transactions on sale increased in more than 5 times and on purchase decreased by 80.5 percent).

As of the end of June, the USD discount rate constituted 46.3896 KGS/USD, having increased within the quarter by 2.6 percent (as per results of the second quarter of 2009, the USD discount rate constituted 43.2810 KGS/USD, having increased by 1.5 percent within the quarter).

**Chart 1.4.1 Rates of change of an official rate of US dollar**



The dynamics of the rate of Euro formed on impact of its exchange rate dynamics against US dollar on the foreign markets. During the second quarter, the EUR exchange rate in exchange offices gradually decreased on international markets until the first decade of June, later the dynamics changed its direction towards strengthening. In general, within the quarter the EUR selling rate decreased by 6.6 percent and constituted 56.6155 KGS/EUR as of the end of June.

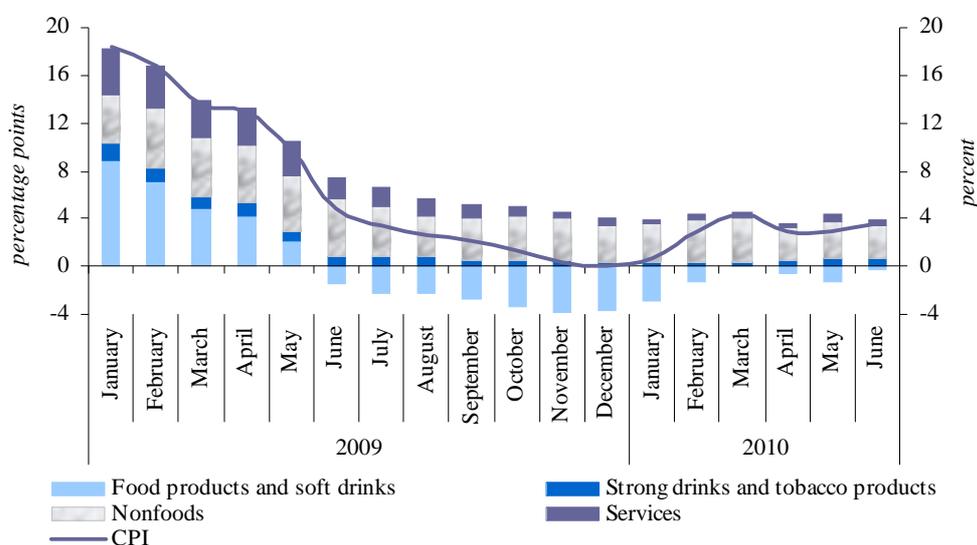
## Chapter 2. Inflation and its components

### 2.1. Consumer price index development<sup>1</sup>

In June 2010 CPI inflation reached 3.6 percent (towards June 2009) whereas during the same period last year – 4.8 percent. The consumer price index of food products and strong drinks in annual terms increased by 0.7 percent. Increase in price recorded for the rest product groups. The largest rise in was noted for non-food products (9.2 percent); strong drinks and tobacco products – by 6.0 percent and paid services – by 5.1 percent.

The present dynamics of prices is influenced by changes in tariffs for electricity, heat energy and hot water and reducing food prices due to the relative stability in world prices growth (grains and sugar).

Chart 2.1.1 Annual CPI and its components

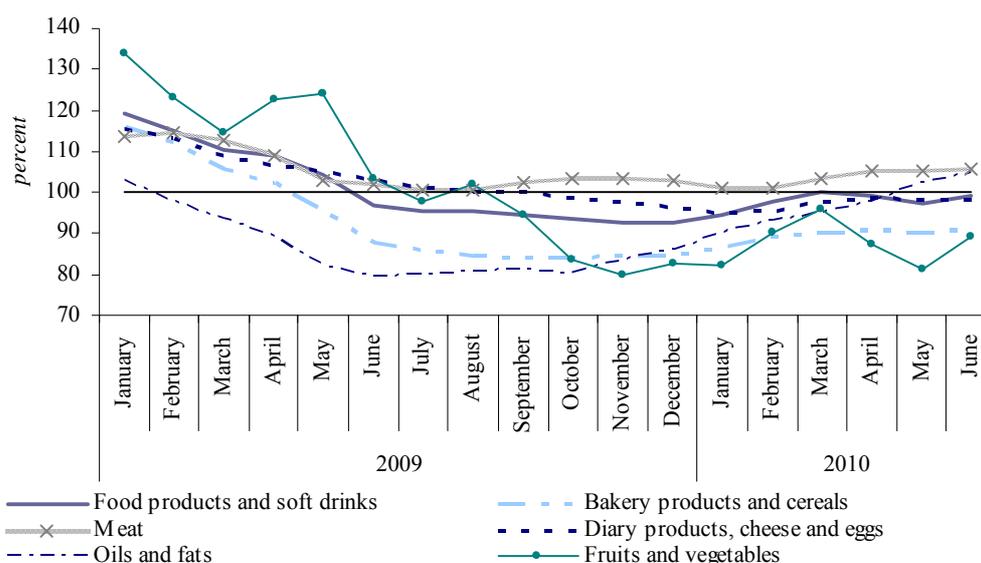


During the second quarter of 2010 consumer price index was negative and constituted 0.7 percent (in the second quarter of 2009 the growth was 0.2 percent). These include the consumer price index for food – 98.0 percent, strong drinks and tobacco products – 103.6 percent, nonfoods – 98.8 percent, paid services – 101.8 percent.

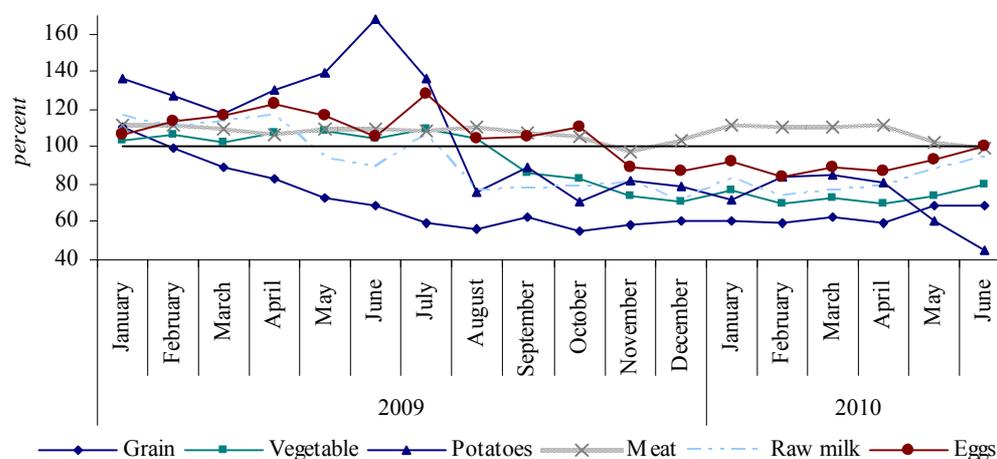
#### 2.1.1. Food products

In general, price situation in the domestic market was highly fluctuated. As of June 2010, prices for food products in annual terms decreased by 0.7 percent (reduction of prices in June 2009 constituted 3.2 percent). Bakery products and cereals went down by 9.5 percent, including light wheat flour by 12.4 percent; there was a decrease in prices for dairy products by 1.6 percent, fruit and vegetable products by 10.6 percent. One of the main factors for dynamics of prices for bakery products were favorable conditions in the grain markets of importing countries and high carryovers of production in the republic.

<sup>1</sup> In accordance with data of the National Statistics Committee of the Kyrgyz Republic

**Chart 2.1.2 Annual dynamics of food prices**

In the second quarter of 2010 producer prices for agricultural products continued to decrease for almost all types of products in comparison with the similar index of the previous year. Thus, producer prices for grain decreased in annual terms by 31.0 percent, for vegetables – by 19.8 percent, for potato – by 54.4 percent, for dairy products – by 5.6 percent and for meat by 0.5 percent.

**Chart 2.1.3 Annual dynamics of the producer price index of agricultural products**

On the consumer market there was also a decrease in prices for flour products. Thus, year-on-year price index for bread, bakery products and cereals decreased by 9.5 percent (in the corresponding period of 2009, the decrease constituted 12.1 percent), bread went down by 4.2 percent. First- and high-grade flour prices declined sharply by 12.4 and 7.5 percent correspondingly.

In the second quarter there was a considerable increase in prices for fruits-and-vegetables to the seasonal factor: of which fruit grew in price by 10.8 percent, and vegetables decreased by 20.1 percent. However, in annual terms prices for fruits increased by 1.5 percent, for vegetables decreased by 16.7 percent.

Supplies of cheaper imported sugar to the domestic market, as well as expectations

that this year the sugar-factory “Kaindy Kant” will restart its work influenced the price for sugar in the country. Thus, in the second quarter of 2010 year-on-year prices for sugar increased by 33.4 percent which is 13 percentage points low than in January of the current year. According to the National Statistics Committee of the Kyrgyz Republic data, an average price for the imported sugar in the second quarter of this year was US\$ 776 per a ton (-2.7 percent against the first quarter of 2010).

Domestic meat production covers about 58 percent of consumption; the rest of the volume is imported. Thus, the rise in the cost of imported goods favors the price development on the domestic market. Following the second quarter of 2010 year-on-year prices for meat products increased by 5.8 percent.

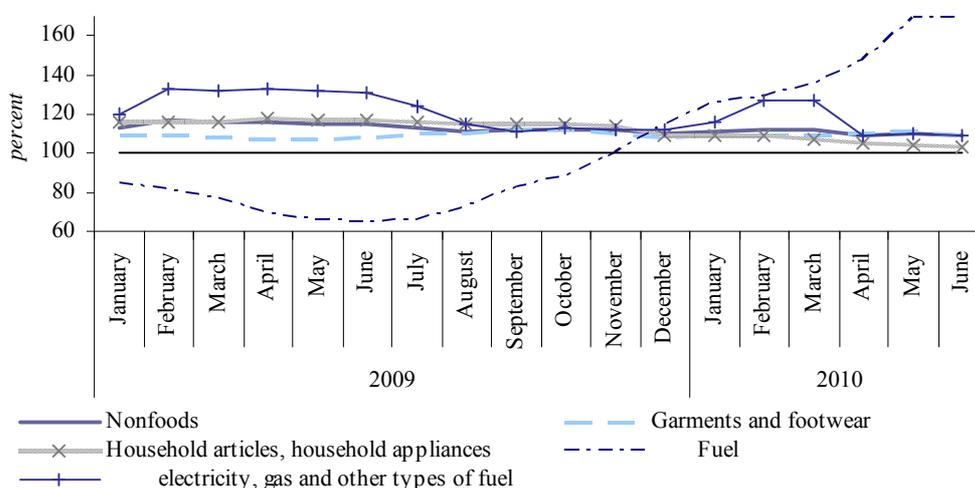
In the second quarter of 2010 there was an increase in prices for the group “oils and fats”. As of the end of the reported period, prices in the market of oils and fats increased by 4.8 percent. At present, the republic imported more than 57 percent of vegetable oil and year-on-year prices for imported goods increased by 3.7 percent and became one of the factors of price development on the domestic market.

In the second quarter due to the seasonal factors there was a decrease in consumer prices for dairy products which made 4.4 percent; in annual terms dairy products went down by 1.6 percent.

### 2.1.2. Non-food products

The growth of the nonfood price index in annual terms constituted 9.2 percent, which is 6.1 percentage points lower of the similar indicator than in 2009. Consumer price index for nonfood products determined the dynamics of rates for electric energy, hot water and central heating influenced by other factors. Thus, the prices for clothes and shoes increased by 9.3 percent mainly due to the rise in prices for women’ and men’ clothing by 13.1 and 11.4 percent respectively. Also there was a decrease in prices for household goods and household appliances which made 3.6 percent. The main reason for such dynamics was decrease in household textile prices from 25.1 to percent in the first quarter of 2010 to 2.6 percent at the end of the second quarter of this year due to the decrease in price for imported products.

Chart 2.1.4. Annual dynamics of non-food prices

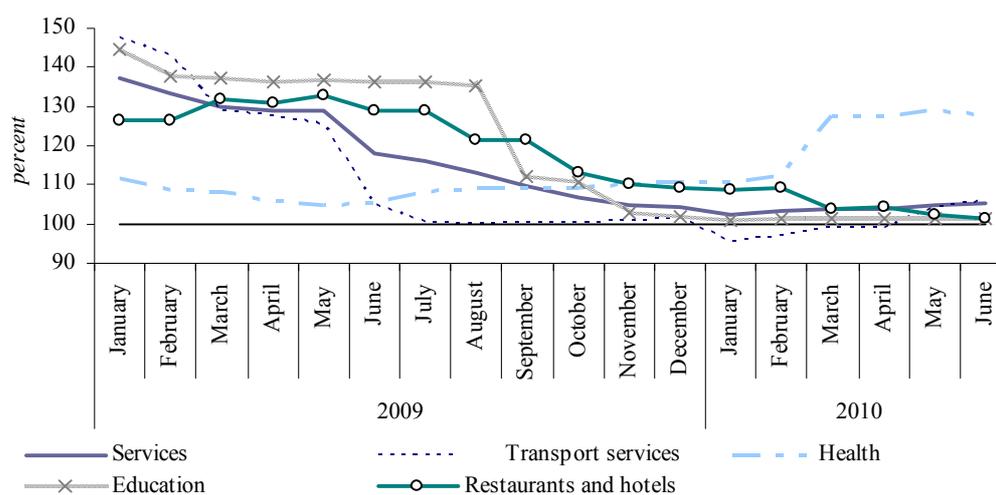


As of the second quarter of 2010, there was a sharp rise in prices for fuels and lubricants, of which annual prices for petrol increased by 73.4 percent and for diesel fuel by 61.3 percent. The main reason of the prevailing trend was the imposition of customs duties on petroleum and its products exported from Russia to Kyrgyzstan from April 1, 2010 and also spring planting began early in the second quarter.

### 2.1.3. Services

In the second quarter of 2010, price index of services in annual terms increased by 5.1 percent (in the second quarter of 2009 – by 18.1 percent). Growth of the index in the given group was driven, mainly, by the rise in transport services (+9.3 percent) due to increased tariffs for fuels and lubricants, public health services (+27.9 percent), caused by the increased tariffs for electric energy; increase in prices for pharmaceuticals and also due to increased tariffs for recreational services (+15.9 percent), due to holiday season. Prices for education services increased by 1.3 percent, those of restaurants and hotels by 1.5 percent, whereas prices for communication services went down by 0.2 percent.

Chart 2.1.5 Annual dynamics of prices for paid services



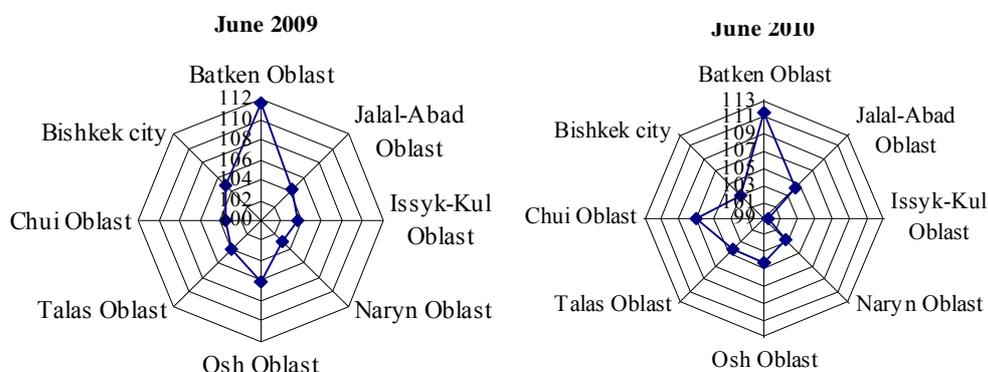
### 2.1.4. Consumer prices in regions

As of the second quarter of 2010, nearly in all oblasts of the republic there was a rise in consumer prices level. The largest increase in prices in annual terms was registered in Batken and Chui oblasts – by 11.3 and 6.9 percent correspondingly. In these areas there was an increase in prices for all groups of goods and services. It should be noted that in June of the current year due to the temporarily formed deficit there was an increase in prices for first-grade wheat flour and high-grade wheat flour in Batken oblast by 9.3 and 5.4 percent respectively, as well as first-grade wheat flour in Issyk-Kul oblast by 6.4 percent and in Jalal-Abad oblast – 3.6 percent.

In other oblasts inflation did not exceed 5 percent. In Osh, Jalal-Abad, Naryn and Talas oblasts consumer prices increased by 4.3 percent, 4.1 percent, 2.4 percent and 3.9 percent correspondingly. In Issyk-Kul oblast there was a deflation on the level of 0.6 percent, mainly due to the decrease in price of food products.

In the capital of the republic there was an increase in the prices at 2.7 percent, while food products decreased by 2.5 percent. Strong drinks, tobacco products, non-food products and paid services increased by 5.8 percent, 9.8 percent and 3.3 percent accordingly.

**Chart 2.1.6 Annual CPI in regions**



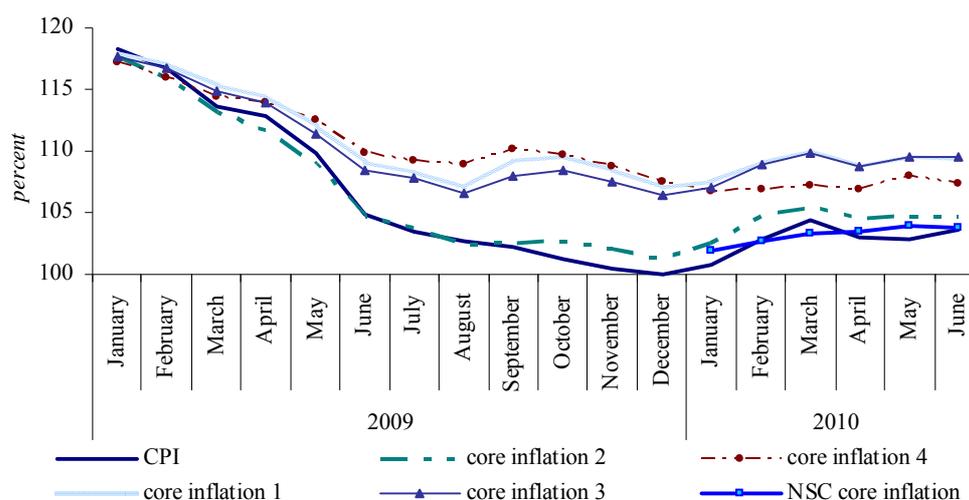
## 2.2. Core inflation

Core inflation is defined as the trend of inflation excluding short-term, structural, and seasonal changes in prices. That means that growth of prices of goods, caused by the seasonal or external factors such, as poor harvest, a price shock in the market of petroleum products, administrative changes in gas and electricity tariffs are removed from the calculation of the rate of inflation.

This method implies the removal of categories or the whole group of goods and services, highly sensitive to shocks, from CPI, having usually one-off and/or short-term character. Traditionally, such goods comprise some food products, energy resources and the tariffs, administratively established by the Government.

Since April 2010 the National Statistical Committee of the Kyrgyz Republic began the calculation of core inflation by simple exceptions (according to the approved methodology № 9 dated 29 April 2010). The calculation excludes such items as milk, sugar, certain types of fruits and vegetables; alcoholic and tobacco products, petroleum products, commodity group “electricity, gas and other fuels”, passenger transport, communications and others. In general, the proportion of excluded products is about 25 percent of the total consumer basket.

The value of core inflation according to the methodology of NSC KR in the second quarter of 2010 was slightly above the headline CPI. This fact indicates the presence in the economy of some pressure on the price dynamics. Core inflation according to NSC KR in annual terms amounted to 3.8 percent, while “crude” inflation – 3.6 percent. At the same time, estimates of core inflation, excluding other combinations of consumer goods, in annual terms remain above the current value of the CPI, indicating a dominance of the dynamics of commodity prices on total consumer price level in the country.

**Chart 2.2.1. Annual dynamics of the estimated core inflation indicator**

Core inflation 1 – the following types of goods are excluded: 1) bakery products and cereals; 2) oils and fats; 3) fruit and vegetables; 4) gas; and 5) materials for repair and construction;

Core inflation 2 – the following types of goods are excluded: 1) meat; 2) fruit and vegetables; 3) gas; and 4) materials for repair and construction;

Core inflation 3 – the following types of goods are excluded: 1) bakery products and cereals; 2) dairy products; 3) fruit and vegetables; 4) gas; and 5) materials for repair and construction;

Core inflation 4 – food products and electricity, gas, and other types of fuel are excluded.

NSC core inflation – milk, sugar, certain types of fruits and vegetables; alcoholic and tobacco products petroleum products, commodity group “electricity, gas and other fuels”, passenger transport, communications and others are excluded.

## **Chapter 3. Monetary Policy Decisions of the National Bank of the Kyrgyz Republic**

### **3.1. Major decisions of the NBKR Board**

The list of basic monetary policy solutions of the Board of the National Bank of the Kyrgyz Republic taken in the second quarter of 2010 is presented below:

1. For the purpose of economic revitalization in activity of the LLC “Specialized Fund for Refinancing of Banks” on reissuance of loan, the Board of the NBKR established a single adjustment factor at “1” rate (Resolution № 26/13 as of May 3, 2010) to create a discount rate in overall lending by SBRF till the end of the third quarter of 2010. For the purpose of enhancing efficiency in activity of the SBRF the Board of the NBKR took a number of decisions in conformity with clause 43 of the Law “On the National Bank of the Kyrgyz Republic” and clause 5 of the SBRF Charter.
2. To increase drawing potential of commercial banks, on May 19, 2010 the Board of the NBKR revised the mandatory reserves of commercial banks towards reduction from 9.5 percent to 8 percent from the calculation base (Resolution № 34/2).
3. To assess the current situation and to develop the scenario for implementation of the relevant monetary policy in the short-term period, the Board of the NBKR considered and approved on May 26 2010 the Monetary Policy Report for the first quarter of 2010 and Monetary Program for the following period (Resolution No 36/1). An informative subset of the document for the first quarter of 2010 was directed to the Provisional Government Office of the Kyrgyz Republic, the Ministry of Finance and the Ministry of Economic Regulation of the Kyrgyz Republic, as well as was placed on the official web-site of the NBKR.
4. In order to support the financial sector to stimulate economic growth, on 26 May 2010 the Board of NBKR adopted a Resolution № 36/11 “On conducting direct swap operations”. According to the Resolution it is allowed, on a provisional basis, to conduct direct swap operations not by auction with commercial banks in the Kyrgyz Republic for the provision of funds to microfinance institutions in the national currency in exchange for cash in U.S. dollars based on standard conditions for a period not exceeding 6 months, with possible further extension under decision of Monetary Policy Committee. At the same time, interest rates and terms and conditions of swap operations are established by the Monetary Policy Committee.
5. As part of the modernization of instruments of monetary policy in order to broaden the base of collateral for overnight and intraday credits, on 30 June 2010, the Board of the NBKR adopted a Resolution № 52/2 on collateral for overnight and intraday credits provided by the National Bank of the Kyrgyz Republic. According to this Resolution, the Government securities of the Kyrgyz Republic, placed by the National Bank (ST-Bonds, ST-Bills and Notes of the National Bank) are accepted as collateral for overnight and intraday credits while the cost of the mortgage is set at 120 percent of the credit amount.

### 3.2. Major decisions of the Monetary Policy Committee

The Monetary Policy Committee develops and takes operative decisions in the monetary sphere. The decisions are taken by the Committee weekly and based on findings of the money market situation assessment. The volumes of operations directed to regulate liquidity in the banking system in the second quarter of 2010 were defined by the Monetary Policy Committee proceeding from the goals and objectives determined by the Board of the NBKR and specified in the main directions of the monetary policy for 2010, and in the monetary program for the forthcoming period as well as taking into account the state of affairs in the banking system and the situation in the fiscal sphere.

In the second quarter of 2010, the Monetary Policy Committee held 13 meetings. The decisions of the Monetary Policy Committee were aimed at regulating liquidity in the banking system by holding weekly auctions of NBKR notes. Due to the decrease of liquidity in the banking system and difficult situation in the fiscal sphere the National Bank in April began to significantly reduce the emission volume of the NBKR notes in order to bring the volume of notes in circulation to about Som 200 million at the end of June 2010 from the level at Som 1.0 billion in late March. At the same time the National Bank stopped holding auctions of NBKR notes with maturity of 7, 14 days, placing only 28-day notes.

The actual sales of NBKR Notes totaled Som 0.7 billion in the second quarter of 2010. Net NBKR sales<sup>1</sup> of US dollars in the quarter under review totaled Som 4.0 billion in the equivalent.

The Monetary Policy Committee establishes the monthly base rate for the purposes of lending for the LLC “Specialized Fund for Refinancing of Banks” once a month. The size of the interest rate of SBRF credit resources is equaled to the base rate with the adjustment factor, depending on the sector of lending. At present and till the end of the third quarter of 2010 the Monetary Policy Committee established the adjustment factor at “1” rate for all lending directions of SBRF, according to the Resolution № 26/13 as of May 3, 2010).

In order to support the real sector in the decrease in lending, in May 2010, the Monetary Policy Committee reduced the base rate for lending purposes of SBRF from 8.0 percent in April to 7.0 percent and remained at this level until the end of the second quarter of 2010.

**Press-release**  
**Meeting of the NBKR Board**  
**on review of monetary policy report of the NBKR for the**  
**first quarter of 2010**

On May 26, 2010 the Board of the National Bank of Kyrgyz Republic considered a report on monetary policy for the first quarter of 2010.

<sup>1</sup> The NBKR follows the floating exchange rate policy adopted by the Kyrgyz Republic.

During the presentation of the report on monetary policy, it was noted that in the first quarter of 2010 the main growth driver of inflationary pressures was the increase in tariffs for electricity and hot water heating from January 2010. As a result of the reporting quarter consumer price index growth was 4.8 percent, whereas during the same period in 2009 inflation was 0.4 percent. In annual terms, the inflation rate for the period under review amounted to 4.0 percent, whereas for the comparable period last year inflation rate made 13.6 percent.

Due to the preservation of inflation risks the National Bank during the reporting period maintained emission volumes of NBKR notes at the optimal level. The volume of the NBKR notes in circulation was at the level of about Som 1 billion and made Som 986.1 million as of the end of March. The NBKR discount rate floated within the range from 0.7 to 1.2 percent and made 0.9 percent as of the end of March.

It was noted that the significant increase of economic growth rates made 16.4 percent which was mainly stipulated by the effect of “low base” of last year. Similarly, there were positive trends in the external sector, where a reduction in the trade deficit was observed and the increased inflow of private transfers as a result of a favorable external environment.

The staff of NBKR assessing the impact of fiscal policy suggests that the determining factor for the deviation of quantitative indicators of monetary policy during the reporting period from the previously approved programs were the operations of general government.

The report noted the events occurred in the Republic in early April which influenced significantly the conditions and nature of monetary policy. Unstable situation stipulated deposit outflow from the banking system which, in turn, was reflected in reduced liquidity of commercial banks. In order to maintain liquidity in the banking system, the Monetary Policy Committee decided to reduce the emissions of the NBKR Notes. As a result, the volume of the NBKR Notes in circulation was reduced from Som 986.1 million to Som 234.4 million. In May, the Board of the National Bank decided starting from May 31 to reduce the mandatory provisions from 9.5 to 8.0 percent as a further measure to ensure the liquidity of commercial banks.

Also, in view of recent changes in tariff policy a question was raised regarding expectations on inflation in the current year. The estimate results by the staff of the National Bank showed that the April revision of the tariff policy in the downward would not be able to reduce inflationary pressures in 2010 maintained by the export duty on crude oil and petroleum products which Russia imposed in April 2010.

Board members also exchanged views on the outcome of monetary policy in the reporting quarter and a significant change in terms of monetary policy at present, discussed the dynamics of basic macroeconomic indicators in the reporting quarter, including the possible effects of political events on the economic situation in the country this year. Thus, there is a threat of economic growth decrease and according to one of the estimates, GDP growth could amount about 2.0 percent in 2010.

During the discussion, the Board also concerned about the significant drop in domestic demand and noted that probably this year, there will be a decrease in real income of individuals and legal entities that may ultimately negatively affect the status of financial institutions. In this connection, it is reasonable for financial and credit institutions to review monetary policy and decrease discount rates to prevent the deterioration of the loan portfolio. The Board stressed that in the current financial state of the banking sector will be one of the key factors determining the monetary policy trend.

In the context of the discussion it was noted that the content of the medium-term economic program of the Government of the Kyrgyz Republic is likely to reflect the program of the political party that wins the parliamentary elections this year. At the same time we must take immediate action to support the economy.

Concerns was also expressed about the unbalance of the state budget in 2010 and increase the cost of servicing domestic debt, which will have a significant impact on monetary policy in the current year.

Following the discussion, the Board members approved the report on monetary policy in the first quarter of this year.

## Chapter 4. Inflation forecast

### 4.1. Forecast of key inflation factors developments

Recent events in the country have made serious changes in economic prospects for the coming years, which increase the uncertainty and difficulty of forecasting the main macroeconomic indicators.

The forecast of the macroeconomic development of the country for 2010, published in the previous “Inflation Report”, due to the unstable situation in the country has been revised downward. It is currently expected drop in GDP which could reach 2.5 percent. Nominal GDP in 2010 is assumed to be at the level of Som 211.7 billion.

The main decline is expected in the service sector and agriculture. The decline in services, to a great extent, will depend on the depth of the fall turnover in trade and how serious will be the consequences of events that occurred in the first half of this year. In agriculture, there is a possible decrease in value against the backdrop of a heavyweight crop in the previous year which also will have a negative impact on economy growth. Growth in the industry will partly compensate the decline in the services sector, thus an increase in production will occur, to a greater extent, at the expense of the industries non-engaged in gold mining, whose activities in January to June this year made a considerable contribution to GDP growth. Herewith it is necessary to consider that the economic growth will also depend to what extent the establishment of the Customs Union between Russia, Belarus and Kazakhstan will have an impact on foreign trade activities in Kyrgyzstan.

**Table 4.1.1. GDP forecast by sectors for 2010**  
(primary)

	factual data					estimated date					
	current prices, mln.som	comparable prices, mln.som	GVA (gross value added), mln.som	real growth, percent	deflator, percent	GVA (gross value added), mln.som	real growth, percent	comparable prices, mln.som	GVA (gross value added), mln.som	real growth, percent	deflator, percent
			2009			Jan-Jun 2010			2010		
Agriculture, hunting & forestry	43 372,8	47 395,8	3 244,9	7,3	-8,5	21,1	0,2	41 984,9	-1 387,9	-3,2	
Industry	29 143,7	26 596,0	-1 928,4	-6,8	9,6	4 387,1	42,5	31 190,5	2 046,8	7,0	
Mining industry	1 232,7	1 048,8	47,1	4,7	17,5	36,6	7,5	1 257,4	24,7	2,0	
Processing industry including Kumtor	24 577,0	22 910,3	-1 940,4	-7,8	7,3	4 166,3	49,7	26 199,1	1 622,1	6,6	
Electricity, gas, and water generation and distribution	13 611,4	10 204,9	-808,6	-7,3	33,4	2 613,6	71,3	14 484,3	872,9	6,4	
Construction	3 334,0	2 636,9	-35,1	-1,3	26,4	184,2	12,7	3 734,1	400,1	12,0	
Trade	11 235,3	10 501,4	621,1	6,3	7,0	227,1	7,2	12 358,8	1 123,5	10,0	
Transport and communication	32 205,2	31 266,4	553,8	1,8	3,0	-1 209,1	-9,0	28 179,6	-4 025,7	-12,5	
Other	17 931,0	15 583,0	757,9	5,1	15,1	74,8	0,2	17 393,1	-537,9	-3,0	
Net tax on products	40 675,1	35 793,1	587,8	1,7	13,6	-232,8	-1,3	39 129,4	-1 545,7	-3,8	
<b>GDP</b>	<b>21 860,0</b>	<b>25 261,2</b>	<b>567,9</b>	<b>2,3</b>	<b>-13,5</b>	<b>467,2</b>	<b>5,0</b>	<b>21 313,5</b>	<b>-546,5</b>	<b>-2,5</b>	<b>10,5</b>

There is a probability of deeper decline in GDP in the case of a more protracted slowdown in the services sector, particularly in trade. In addition, agriculture is also a risk of more pessimistic scenario, as a result of which the economic growth may reach 3.5 percent in 2010.

**Table 4.1.2. GDP forecast by sectors for 2010 (revised)**

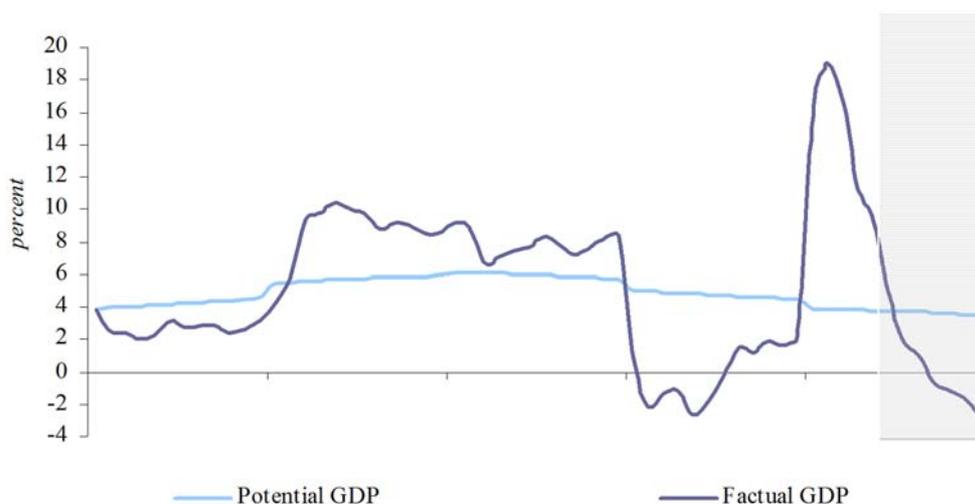
	factual data					estimated data				
	current prices, <i>mln.som</i>	comparable prices, <i>mln.som</i>	GVA (gross value added), <i>mln.som</i>	real growth, <i>percent</i>	deflator, <i>percent</i>	comparable prices, <i>mln.som</i>	GVA (gross value added), <i>mln.som</i>	real growth, <i>percent</i>	deflator, <i>percent</i>	
	2009					2010				
Agriculture, hunting & forestry	43 372,8	47 395,8	3 244,9	7,3	-8,5	41 179,5	-2 193,3	-5,1		
Industry	29 143,7	26 596,0	-1 928,4	-6,8	9,6	31 123,8	1 980,1	6,8		
Mining industry	1 232,7	1 048,8	47,1	4,7	17,5	1 257,4	24,7	2,0		
Processing industry including Kumtor	24 577,0	22 910,3	-1 940,4	-7,8	7,3	26 199,1	1 622,1	6,6		
	13 611,4	10 204,9	-808,6	-7,3	33,4	14 484,3	872,9	6,4		
Electricity, gas, and water generation and distribution	3 334,0	2 636,9	-35,1	-1,3	26,4	3 667,4	333,4	10,0		
Construction	11 235,3	10 501,4	621,1	6,3	7,0	12 920,6	1 685,3	15,0		
Trade	32 205,2	31 266,4	553,8	1,8	3,0	27 374,4	-4 830,8	-15,0		
Transport and communication	17 931,0	15 583,0	757,9	5,1	15,1	17 213,8	-717,2	-4,0		
Other	40 675,1	35 793,1	587,8	1,7	13,6	38 641,3	-2 033,8	-5,0		
Net tax on products	21 860,0	25 261,2	567,9	2,3	-13,5	21 094,9	-765,1	-3,5		
<b>GDP</b>	<b>196 423,1</b>	<b>192 396,9</b>	<b>4 405,0</b>	<b>2,3</b>	<b>2,1</b>	<b>189 548,4</b>	<b>-6 874,7</b>	<b>-3,5</b>	<b>10,5</b>	

An additional indicator of price risks arising in the economy under the influence of growth/decline in GDP may be an indicator of output gap (GDP).

In the first half of 2010 a jump in GDP growth and a corresponding increase in GDP gap, which indicates a possible rise in inflationary pressures in the economy in the period. However, it must be borne in mind that such an increase in GDP was due to the low base of the previous year and won't last long, because on the results of 2010 a decline in economic growth over the previous year is expected. As a result, demonstrated increase of an inflationary pressure in the economy will be offset by decline in economic activity in the second half of the year and won't have a significant impact on inflation upwards.

**Chart 4.1.1. Real and potential GDP forecast**

(growth rate, the beginning of the year to the corresponding period of the previous year)



It is expected that the volume of consumption in the current year will decline by 2.9 percent under the influence of the decline in economic activity and reduce of the aggregate demand. Given some signs of economic recovery in the countries – main trade partners, an inflow of money transfers is expected, which will enable to partially compensate the decline in incomes.

Slight increase is expected in economic investments from the government' side that will be reflected in the increase of capital investments, including the cost of reconstruction of destroyed infrastructure and property of people affected during the recent events. Such measures will help to restore economic activity and allow tempering GDP decline.

Growth of import in 2010 is expected at the level of 108.3 percent, which will be provided by its low level in the previous year and forecasted economy recovery in the countries – main trade partners. It is assumed that income from export will increase by about 3.0 percent.

The question of harmonious coexistence of Kyrgyzstan within the framework of the Customs Union between Russia, Belarus and Kazakhstan is of particular importance, because of productivity to address this issue will depend on continued success in the field of trade and economic co-operation with major trading partners. At that new trading environment may cause major changes in the economy, where trade is the strategic industry for many years, both for the employed population and rate of earnings, and could profoundly affect the development of the national economy in future.

## 4.2. Inflation forecast for 2010 and quarter III of 2010

At forecasting of inflation some of the most important factors of uncertainty can be identified, efficiency of which on final value of inflation will depend on the recovery rate and further development of the economy.

A key role at pricing of the general level of consumer products, especially in the medium term, is the balance between supply and demand of goods and services. Actual data of 2009 and forecast till the year-end of 2010 show that domestic demand in Kyrgyzstan

is being reduced. Socio-political instability during recent months and consequently, decline of business activity in the country, worsening of the investment climate, reduction of trade turnover, and possible retardation of the population's income growth and certain weakening of the aggregate demand will have deterrent effect on the general inflation rate in the country.

However, it should be taken into account the important fact that the decline in demand occurs simultaneously with the growth retardation, but for some items - reduction in supply of goods and services. Thus, according to the actual data for the first half of 2010 there was a growth rate decrease in production of some foods (flour, bread, meat and meat products), which occupy a large share of the consumer basket. Forecasted on the basis of 2010 a moderate decrease in production in agriculture creates additional pre-conditions for the volatility of prices. This factor reduces or even eliminates the deterrent effect on inflation on the part of demand.

Maintaining a positive contribution to the growth of the CPI should be expected from the price of fuel. Moreover, from July of the current year due to inclement weather conditions there was a rise in prices for wheat at the foreign market. According to the reports of the Ministries of Agriculture of Russia and Kazakhstan, sufficient grain reserves and forecasts of the current year do not allow to destabilize grain markets in these countries. In the domestic market of Kyrgyzstan the first increase in the price of flour already recorded, but further price dynamics depends more on the actions of the Kyrgyz Government to prevent speculative price increases and to ensure sufficient government stocks.

Public sector expenditure as the main source of growth in money supply in 2010 is another important factor that affects the current and future inflation. Since May 2010 the Provisional Government of the Kyrgyz Republic has been implementing a number of activities, primarily in support of the affected businesses and the reconstruction of destroyed cities. As a result of these measures on the results of the year, government expenditures are being significantly increased, against the backdrop of decline of tax revenues, lead to an increase of budget deficit and the appropriate needs in its financing. According to the forecasts of the Ministry of Finance of the Kyrgyz Republic government budget deficit in 2010 will increase to about 13 percent of GDP. Thus, medium-term fiscal policy carries some risks for the stability of prices in the country.

**Wheat.** According to April forecast of the US Ministry of Agriculture, world production of wheat in 2010/11 marketing year will make 661.1 million tons, which is low than the indices of the previous forecast for 1.1 percent. The forecast of wheat consumption remained at the same level as in the previous month (667.0 million tons). Thus, the final stocks of wheat will decrease by 3.5 percent and constitute 187.0 million tons in 2010/11 marketing year.

According to the Ministry of Agriculture of Kazakhstan the condition of the stocks of cereals during dry season is satisfactory. During the current year it is planned to obtain 14.5-15.5 million tons of grain, 6.5 million tons of this amount will be put on the foreign markets. It is also reported that the balance of last harvest grain is 8.6 million tons.

According to preliminary data of the State Customs Committee of the Kyrgyz Republic in the second quarter of 2010, 83.1 thousand tons of wheat was imported to the Kyrgyz Republic from Kazakhstan at the average price of US\$ 134.3 per a ton. On July 16, 2010 an average price for wheat 3 grade on DAF terms, Lugovaya station (Kazakhstan-Kyrgyzstan), according to the Information Agency “Kazakh-zerno” made US\$ 151.

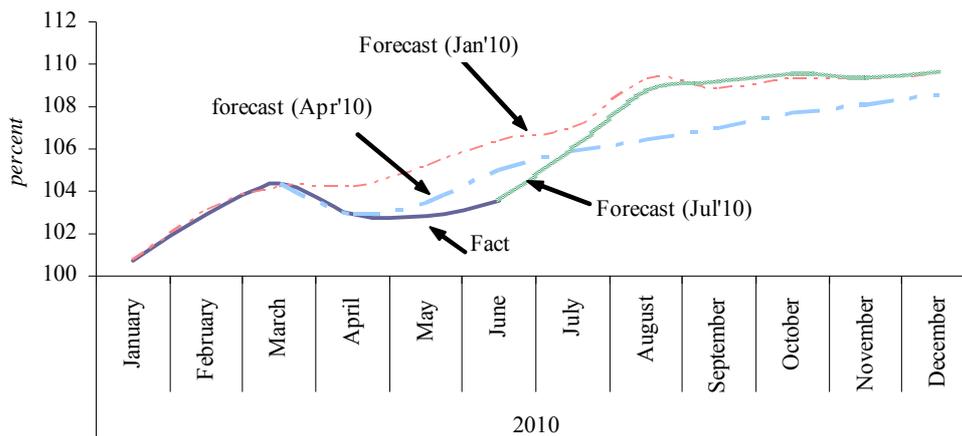
**Rice.** US Ministry of Agriculture in June slightly reduced evaluation of the world consumption of rice for the following marketing year to 459.3 million tons (-0.1 million tons) and the forecast of consumption to 452.1 million tons (-0.6 million tons). Carry-over stocks for this type of grain will amount 96.6 million tons (+0.4 million tons). According to preliminary data of the State Customs Committee of the Kyrgyz Republic in the second quarter of 2010, 2.4 thousand tons of rice was imported to the Kyrgyz Republic from China at the average price of US\$ 358 per a ton.

**Oil.** The International Monetary Fund has lowered the forecast of oil prices in 2010-2011. According to new estimates, the average price for oil per a barrel in 2010 would cost US\$ 75.3 and in 2011 – US\$ 77.5. This is significantly below than in April forecast, which constituted US\$ 80 and US\$ 83 respectively.

Source: Reuters

In general, considering all above-mentioned factors, forecast of the inflation rate for 2010 is maintained at the earlier determined level – in the range between 7.5 – 9.5 percent (to December 2009).

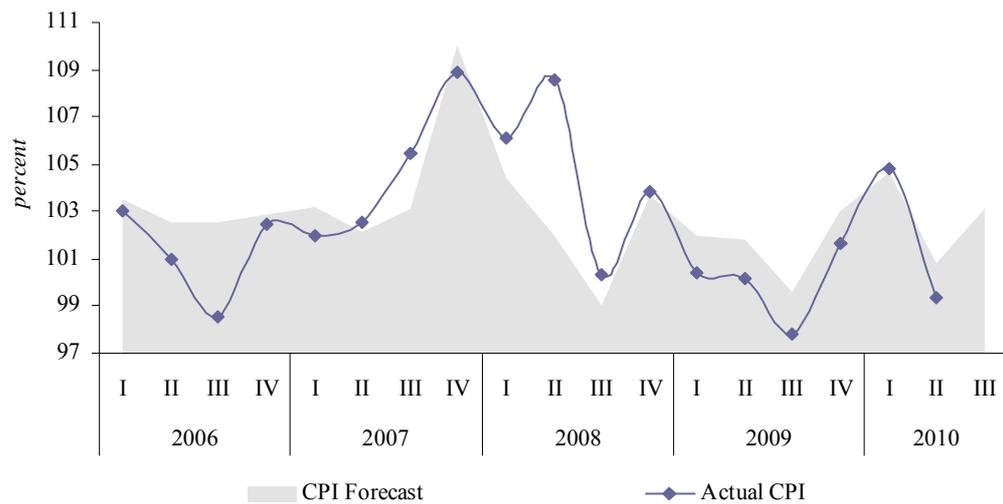
Chart 4.2.1 Annual inflation forecasts



Herewith failing shocks, while balancing between demand and supply at food market, as well as moderate growth in prices for fuel, rate of inflation in 2010 could decrease to 6.5 percent. However, there are risks of exceeding the specified predictive value of inflation. The higher growth in food prices (especially bread), a significant secondary effect of rising prices for fuel and other derivative products and services may lead to inflation above 10 percent.

In the third quarter of 2010, it is assumed that the situation on the consumer market will be formed under the influence of wheat prices and seasonal factors. It is expected that prices for agricultural products will stipulate descending dynamics of CPI. However, there is a probability of additional pressure on inflation in the third quarter mainly on the part of bakery products, lubricants as well as educational services. As a result, growth of prices in the third quarter of 2010 is expected at the rate of 3.0 percent.

**Chart 4.2.2. Inflation forecast for quarter III of 2010**



Another index of the price dynamics in the economy the GDP deflator is forecasted to be 10.5 percent in 2010.

## Statistical Annex

**Table 1. Consumer Price Index**
*(month against corresponding month of the past year, percent)*

	2010					
	January	February	March	April	May	June
<b>Consumer Price Index</b>	<b>101.3</b>	<b>102.5</b>	<b>101.0</b>	<b>99.0</b>	<b>100.2</b>	<b>100.1</b>
<b>Goods</b>	101.4	102.8	101.0	98.8	100.0	100.1
<b>Food products and soft drinks</b>	102.0	101.9	101.5	99.2	98.9	99.9
<b>Strong drinks and tobacco products</b>	100.1	100.2	100.4	102.6	100.5	100.5
<b>Nonfoods</b>	100.9	104.8	100.6	97.3	101.4	100.2
<b>Services</b>	100.4	100.7	100.8	100.1	101.5	100.5
Food products and soft drinks	102.0	101.9	101.5	99.2	98.9	99.9
Bakery products and cereals	99.4	99.8	99.4	99.3	99.7	100.4
high-grade wheat flour	99.6	99.5	99.8	99.5	99.4	100.2
first-grade wheat flour	99.4	99.7	99.4	99.0	99.0	100.7
bread	100.0	101.0	100.0	100.1	99.8	100.5
Meat	101.1	101.3	102.3	100.9	100.6	100.8
Fish	102.4	103.2	100.3	101.3	100.1	100.1
Diary products, cheese and eggs	100.9	99.9	98.4	98.6	98.3	98.7
Oils and fats	101.0	100.1	100.5	100.9	101.4	100.6
Fruits and vegetables	104.4	108.4	105.7	97.1	93.3	97.9
fruits	102.1	101.6	101.4	100.8	100.4	109.5
vegetables	105.8	112.3	108.0	95.3	90.5	92.7
Sugar, jam, honey, chocolate and candies	108.4	101.7	101.4	98.5	98.5	98.9
sugar	113.6	102.4	101.7	97.2	98.0	98.0
other food products	98.1	100.3	100.1	99.9	99.4	103.9
Soft drinks	100.9	100.7	101.8	101.1	101.2	100.7
Strong drinks and tobacco products	100.1	100.2	100.4	102.6	100.5	100.5
Strong drinks	100.2	100.2	100.7	100.3	100.7	100.7
Tobacco products	100.0	100.0	100.0	107.4	100.0	100.0
Garments and footwear	100.4	100.7	100.4	100.9	101.5	100.0
Garments	100.5	100.9	100.6	101.1	101.9	99.9
fabric for garments	103.8	107.5	100.1	100.0	100.0	100.2
garments for men	100.4	100.7	100.0	100.8	102.7	100.1
garments for women	100.4	100.9	101.1	102.0	103.0	99.3
children and newborns garment	100.2	100.2	100.2	100.2	100.1	100.3
Cleaning, mending and renting garments	100.4	101.1	105.3	100.0	101.3	101.3
footwear including repair	100.2	100.2	100.0	100.6	100.4	100.3
men footwear	100.2	100.4	98.3	99.8	100.2	100.2
women footwear	100.0	100.1	102.7	101.6	100.2	100.3
children footwear	100.6	100.2	96.7	99.5	101.8	100.3
shoe repair	100.0	100.2	100.0	100.0	100.5	100.0
Housing services, water, electricity, gas and other fuels	103.0	118.3	100.6	87.5	100.8	99.2
rent of dwelling	100.0	100.0	100.4	100.0	100.0	100.0
material for maintenance and repair of living houses	97.9	99.0	100.2	101.5	103.2	99.8
electricity, gas and other types of fuel	103.9	122.1	99.6	85.2	100.6	99.0
gas	100.7	100.1	100.7	100.9	100.2	100.5
Household articles, household appliances	100.1	100.5	100.4	100.3	99.4	100.2
furniture and floor coverings	100.1	100.3	100.1	100.6	100.1	100.2
household textile items	100.0	100.0	100.1	100.0	100.0	100.1
home appliances	100.0	100.1	100.3	100.0	100.5	100.2
glassworks, tablewares and household stuff	100.3	100.6	100.0	100.4	100.1	100.2
Health	100.3	102.4	113.4	100.3	101.3	99.7
Transport	98.5	100.2	99.7	100.6	104.6	101.6
purchase of cars	100.3	100.5	100.5	100.6	100.6	100.5
petrol and lubricants	97.7	99.5	101.0	105.6	113.4	104.5
gasoline	97.4	99.4	100.3	105.1	112.8	104.5
diesel	99.7	99.7	105.3	108.8	123.1	103.6
transport services	98.4	100.2	99.5	100.1	104.7	101.5
Communication	100.0	99.7	100.0	100.0	100.0	100.0
Recreation, entertainment and culture	100.0	100.8	100.3	100.5	104.4	103.1
cultural events services	100.0	103.9	100.4	100.1	100.0	100.0
papers, books and stationary	100.0	100.0	100.1	100.0	100.0	100.0
Education	99.6	100.5	100.0	100.2	100.0	100.0
Restaurants and hotels	100.3	100.4	100.0	100.2	100.0	100.0
catering	100.3	100.3	100.0	100.0	100.0	100.0
hotel service	100.2	101.6	100.3	103.3	100.7	100.2
Various goods and services	103.0	101.9	101.9	100.3	100.4	100.6
Personal service	103.4	102.1	102.2	100.2	100.3	100.2

Source: NSC KR

**Table 2. Consumer Price Index**  
(month against corresponding month of the past year, percent)

	2010					
	January	February	March	April	May	June
<b>Consumer Price Index</b>	<b>100.7</b>	<b>102.9</b>	<b>104.3</b>	<b>102.9</b>	<b>102.9</b>	<b>103.6</b>
<b>Goods</b>	100.6	103.1	104.7	103.0	102.8	103.5
<b>Food products and soft drinks</b>	94.3	97.5	100.0	98.9	97.4	99.3
<b>Strong drinks and tobacco products</b>	105.1	105.2	105.0	106.9	107.1	106.0
<b>Nonfoods</b>	110.9	111.8	112.4	108.9	110.2	109.2
<b>Services</b>	102.4	103.3	103.6	103.6	104.8	105.1
Food products and soft drinks	94.3	97.5	100.0	98.9	97.4	99.3
Bakery products and cereals	86.6	89.3	90.2	90.6	90.3	90.5
high-grade wheat flour	78.1	82.2	84.2	88.9	93.6	92.5
first-grade wheat flour	74.3	79.2	80.7	83.6	86.8	87.6
bread	90.2	91.8	92.5	94.8	95.3	95.8
Meat	100.9	100.9	103.2	105.3	105.4	105.8
Fish	103.1	105.6	105.1	106.0	105.8	106.7
Diary products, cheese and eggs	94.8	95.5	97.5	98.7	98.1	98.4
Oils and fats	90.2	93.2	94.9	98.0	102.6	104.8
Fruits and vegetables	82.2	90.0	96.0	87.6	81.1	89.4
fruits	88.5	89.4	90.9	89.8	86.8	101.5
vegetables	76.3	87.7	96.0	83.3	76.5	83.3
Sugar, jam, honey, chocolate and candies	126.2	129.7	132.1	129.9	123.5	120.2
sugar	146.4	152.0	155.8	152.0	139.8	133.4
other food products	99.2	99.9	100.5	101.0	100.3	104.3
Soft drinks	112.1	112.3	113.5	112.7	113.9	113.7
Strong drinks and tobacco products	105.1	105.2	105.0	106.9	107.1	106.0
Strong drinks	107.1	107.2	107.0	106.3	106.6	104.9
Tobacco products	101.2	101.1	101.0	107.8	107.8	107.8
Garments and footwear	108.7	108.9	109.3	109.8	110.9	109.3
Garments	110.3	110.5	110.6	110.9	112.6	111.0
fabric for garments	153.5	160.1	139.7	121.3	121.1	112.9
garments for men	110.6	110.5	110.2	110.4	112.9	111.4
garments for women	109.1	109.4	110.3	112.2	115.0	113.1
children and newborns garment	108.0	107.6	108.0	108.3	108.1	107.4
Cleaning, mending and renting garments	107.2	107.9	113.5	111.5	112.0	111.4
footwear including repair	105.7	105.8	106.7	107.5	107.1	105.9
men footwear	105.9	106.2	106.0	107.1	105.6	104.3
women footwear	106.6	106.7	110.2	110.6	110.1	109.2
children footwear	104.2	104.4	101.6	101.9	103.6	102.0
shoe repair	112.9	108.5	106.9	103.9	104.5	103.5
Housing services, water, electricity, gas and other fuels	113.7	122.4	124.1	109.2	110.4	108.4
rent of dwelling	101.0	100.7	100.4	100.4	100.4	100.4
material for maintenance and repair of living houses	106.9	103.2	103.6	105.1	108.1	97.1
electricity, gas and other types of fuel	115.6	126.6	127.2	109.0	110.2	109.3
gas	158.5	102.2	102.9	104.3	105.4	106.2
Household articles, household appliances	109.1	109.0	107.5	105.5	104.5	103.6
furniture and floor coverings	105.2	105.4	104.4	103.2	103.1	103.2
household textile items	140.9	140.0	125.1	110.0	110.1	102.6
home appliances	102.6	102.5	101.9	101.4	101.8	101.8
glassworks, tablewares and household stuff	108.2	108.0	106.0	104.7	104.4	103.2
Health	110.4	112.4	127.5	127.5	128.8	127.9
Transport	98.9	100.4	102.0	102.8	108.2	109.3
purchase of cars	110.7	108.5	105.3	104.3	104.6	105.0
petrol and lubricants	125.4	129.2	135.8	147.0	168.6	168.7
gasoline	134.9	137.0	143.9	155.0	175.7	173.4
diesel	94.4	101.7	109.5	121.6	154.7	161.3
transport services	95.5	97.1	98.7	99.0	104.4	105.5
Communication	100.0	99.7	99.7	99.7	99.8	99.8
Recreation, entertainment and culture	111.3	109.4	108.8	108.6	112.8	115.9
cultural events services	116.7	119.9	120.0	111.2	105.9	105.8
papers, books and stationary	117.6	115.8	115.6	115.5	115.2	114.6
Education	101.0	101.3	101.3	101.4	101.3	101.3
Restaurants and hotels	108.8	108.9	104.0	104.1	102.1	101.5
catering	108.4	108.5	103.3	103.4	101.3	101.1
hotel service	118.3	119.6	118.9	122.2	122.4	108.9
Various goods and services	110.2	109.4	110.6	109.2	109.0	109.8
Personal service	110.2	110.6	112.4	110.5	110.1	110.6

Source: NSC KR

**Table 3. Indices of prices and physical import volume for January-May 2010**

Name of commodity	5 month	5 month	5 month	Indices		
	2010	2010	2009			
	million	million	million	Physical		
	USD	USD	USD	Price	Cal	Cost
	n10*p10	n10*p09	n10*p09	volume		
	A	B	C	A/B	B/C	A/C
Oil, oil products and similar materials	292.8	200.9	238.1	1.46	0.84	1.23
Raw iron and steel	38.3	31.7	36.9	1.21	0.86	1.04
Medical supplies (including veterinarian drugs)	34.6	30.0	29.1	1.15	1.03	1.19
Natural gas	28.3	33.8	39.0	0.84	0.87	0.72
Meat and meat products	26.4	27.2	16.1	0.97	1.69	1.64
Essential oils, resinoids and perfume substances	22.9	28.1	19.5	0.82	1.44	1.18
Non-organic chemical substances	22.0	25.6	29.0	0.86	0.88	0.76
Sugar, sugar products and honey	21.6	14.7	18.6	1.47	0.79	1.16
Grains (including spelt) and mangcorn, unmilled	19.7	28.5	28.6	0.69	1.00	0.69
Automobiles for cargo transportation and automobiles of special designation	18.8	16.3	15.3	1.16	1.07	1.24
Coffee, tea, cocoa, spices and similar products	18.6	15.2	17.0	1.22	0.90	1.09
Vegetable oils and fats	16.9	16.2	14.4	1.04	1.12	1.17
Paper, cardboard and products, made of them	16.8	17.5	14.4	0.96	1.22	1.17
Coal, coke and briquettes	16.8	16.8	7.2	1.00	2.32	2.32
Fruits and vegetables	16.2	15.8	12.7	1.03	1.24	1.28
Rubber tires	15.4	11.6	11.4	1.33	1.02	1.35
Fabrics, made of artificial textile materials	15.1	19.9	19.6	0.76	1.01	0.77
Machines for sorting, grating and separation of coat, stone and ores	13.7	6.0	9.2	2.27	0.66	1.49
Fertilizers	13.6	16.7	6.4	0.82	2.60	2.12
Electrical line telephone or telegraph devices	11.3	17.4	10.2	0.65	1.72	1.11
Alcoholic beverages	9.4	6.8	11.1	1.39	0.61	0.85
Wood of coniferous trees, sawn	9.3	9.2	8.8	1.01	1.05	1.05
Products, made of imperfect metals, not included into another category	9.2	4.6	10.8	1.99	0.42	0.85
Food products, non-included into other categories	8.7	14.8	9.7	0.58	1.53	0.90
Food products and products, non-included into another category	8.6	8.9	9.7	0.97	0.91	0.89
Plastic materials in initial form	8.5	6.3	7.2	1.35	0.87	1.18
Mineral water and nonalcoholic beverages, sweetened with sugar	7.7	7.1	6.6	1.09	1.07	1.17
Compressed or restored wood	6.8	6.7	5.9	1.01	1.14	1.15
Automobiles and transportation means for transportation of people	6.7	5.5	5.7	1.22	0.96	1.18
Products of cereals, flour or starch	6.6	6.5	6.0	1.02	1.09	1.11
Plastic materials in non-initial form	6.3	5.8	4.9	1.10	1.18	1.29
Electric transformers	6.2	1.7	1.0	3.75	1.63	6.11
Coloring and tanning substances	6.0	4.9	6.2	1.22	0.79	0.96
Raw tobacco, markings	5.4	7.1	1.1	0.75	6.24	4.69
Margarine and combined fats	5.3	4.0	5.5	1.32	0.72	0.95
Various chemical products, non-included into other categories	4.4	2.3	4.3	1.91	0.54	1.04
Milk, cream and dairy products, except for butter and cheese	4.4	3.7	3.9	1.20	0.95	1.14
Insecticides, rodenticides, fungicides, herbicides	4.4	5.3	2.8	0.83	1.87	1.55
Manually and machine operated instruments	4.2	5.3	2.9	0.79	1.79	1.42
Medical and pharmaceutical production	4.0	3.7	4.2	1.08	0.88	0.94
Rice	3.9	3.5	8.4	1.12	0.42	0.47
Nails, screws, bolts and other accessories made of iron, steel and copper	3.9	2.8	4.1	1.40	0.67	0.93
Machines for automated processing of data	3.7	3.7	3.0	1.02	1.23	1.26
Bed-clothes, table-clothes, towels	3.5	7.9	2.3	0.45	3.36	1.50
Glass tare, glass corks	3.4	3.6	2.9	0.93	1.25	1.16
<b>Total by nomenclature (million USD)</b>	<b>830.4</b>	<b>731.4</b>	<b>731.9</b>	<b>1.14</b>	<b>1.00</b>	<b>1.13</b>
<b>Total by nomenclature (% out of the total import)</b>	<b>73%</b>		<b>66%</b>			
<b>Total import</b>	<b>1 144.0</b>		<b>1 114.0</b>			

According to NSK in CIF prices, the largest 45 import articles are provided

n - physical volume of goods export

p - estimated import price of goods

**Table 4. Indices of prices and physical export volume for January-May 2010**

<i>Name of goods</i>	<i>5 month</i>	<i>5 month</i>	<i>5 month</i>	<i>Indices</i>		
	<i>2010</i>	<i>2010</i>	<i>2009</i>	<i>Price</i>	<i>Physi- cal</i>	<i>Cost</i>
	<i>million</i>	<i>million</i>	<i>million</i>			
	<i>USD</i>	<i>USD</i>	<i>USD</i>			
<i>n10*p10</i>	<i>n10*p09</i>	<i>n09*p09</i>	<i>volume</i>			
	<b>A</b>	<b>B</b>	<b>C</b>	<b>A/B</b>	<b>B/C</b>	<b>A/C</b>
Non-monetary gold	301.2	240.9	142.8	1.25	1.69	2.11
Inorganic chemicals	120.1	150.4	104.3	0.80	1.44	1.15
Oil, oil products and similar materials	30.0	26.8	69.4	1.12	0.39	0.43
Fruits and vegetables	29.7	39.4	24.3	0.75	1.62	1.22
Blouses and jackets	12.8	12.7	9.1	1.01	1.39	1.41
Milk, cream and dairy products, except for butter and cheese	8.5	10.2	6.3	0.83	1.62	1.35
Raw tobacco; tobacco markings	8.4	8.4	7.0	1.00	1.20	1.20
Incandescent lamps	7.3	7.4	4.8	0.98	1.56	1.52
Dresses	7.2	6.4	4.4	1.11	1.46	1.63
Knitted or jersey garments for women and girls	6.6	8.9	0.3	0.75	25.85	19.30
Trousers, one-piece garments, breeches and briefs for women	6.2	6.0	2.9	1.04	2.04	2.12
Skirts, divided skirts	3.6	3.8	2.2	0.95	1.67	1.58
Current electricity	3.3	3.0	1.4	1.11	2.06	2.28
Leg wear garment, knitted	3.1	2.5	0.5	1.23	5.36	6.61
Trousers, one-piece garments, breeches and briefs for men	2.9	2.7	1.6	1.07	1.71	1.83
Coats, car coats, wraps, raincoats and similar goods	2.6	2.2	1.1	1.21	2.06	2.50
Stone, sand and gravel	2.4	3.3	1.9	0.74	1.78	1.31
Cotton	2.4	2.3	6.8	1.05	0.34	0.36
Mineral water and nonalcoholic beverages, sweetened with sugar	2.4	4.1	1.3	0.58	3.16	1.83
Paper, cardboard and products, made of them	2.3	2.6	2.2	0.91	1.15	1.04
Cheese and curd	2.1	2.9	3.2	0.72	0.93	0.67
Scrap metal and iron industry residues	1.9	2.0	1.5	0.94	1.36	1.28
Products, made of imperfect metals, not included into another category	1.7	1.8	1.8	0.96	0.98	0.94
Automobiles for cargo transportation and automobiles of special designation	1.7	0.6	0.9	3.05	0.60	1.83
Living animals/cattle	1.5	2.5	1.5	0.60	1.72	1.03
Lead	1.2	1.0	0.2	1.17	5.86	6.85
Scrap metal and base metal residues	1.2	1.9	0.3	0.65	5.49	3.55
Jackets and blazers for women	1.2	1.5	0.4	0.78	3.42	2.68
Coat of cattle and raw stock	1.1	1.3	0.9	0.85	1.51	1.29
Costumes and outfit for women	1.1	1.0	1.2	1.04	0.87	0.91
Products of cereals, flour or starch	1.0	0.7	1.0	1.48	0.66	0.97
Butter and other oils and fats, made of milk	0.9	1.6	0.5	0.60	2.92	1.77
Meat and meat products	0.9	1.5	0.3	0.63	4.38	2.76
Food products, non-included into other categories	0.9	0.6	0.9	1.62	0.62	1.01
Manual and machinery tools	0.9	0.2	1.0	4.76	0.20	0.94
Rice	0.9	0.8	0.1	1.09	7.75	8.42
Silver	0.9	0.6	0.5	1.53	1.14	1.74
Raw iron and steel	0.9	1.1	0.5	0.77	2.08	1.61
Wool and other animal hair, including tops	0.8	0.7	0.5	1.08	1.39	1.50
Costumes and outfit for men	0.8	0.7	0.4	1.14	1.73	1.96
Other mineral raw materials	0.8	0.2	0.4	4.01	0.50	1.99
Coffee, tea, cocoa, spices and similar products	0.8	0.8	1.1	0.98	0.68	0.67
Fabrics, made of artificial textile materials	0.7	0.8	0.4	0.94	2.13	1.99
Rubber tires	0.7	3.8	2.5	0.18	1.51	0.27
Finished tobacco	0.7	0.5	0.6	1.33	0.90	1.20
Margarine and combined fats	0.6	0.6	3.5	0.94	0.18	0.17
<b>Total by nomenclature (million USD)</b>	<b>590.8</b>	<b>575.6</b>	<b>420.7</b>	<b>1.03</b>	<b>1.37</b>	<b>1.40</b>
<b>Total by nomenclature (% out of the total export)</b>	<b>92%</b>		<b>91%</b>			
<b>Total export</b>	<b>638.8</b>		<b>461.3</b>			

According to NSK in FOB prices, the largest 46 export articles are provided

n - physical volume of goods export

p - estimated import price of goods

## Glossary

**Break in production (or GDP gap)** – the difference between potentially possible and actual GDP. Break in production may serve as an indicator of activation or stagnant economy. If actual GDP less potential ( $Y < Y^*$ ), then assumed that the economy is so-called “recessionary gap” which indicates the possible presence of deflation processes. Conversely, if actual GDP more potential ( $Y > Y^*$ ), then assumed that the growth of aggregate demand exceeds aggregate supply growth, which contributes to inflationary pressures.

**Core inflation** is inflation excluding short-term, structural and seasonal changes of prices. That is, excluded from the calculation of the inflation factor are growth of prices of goods, caused by seasonal or external factors (such as: the bad crop, the price shock in the market of oil products, administrative changes in tariffs for gas and electricity, etc.).

NBKR calculates the core inflation behavior by the method of simple exclusions. The given method means the exclusion from the CPI of specific categories or the whole group of goods and services, whose prices are highly sensitive to shocks. Traditionally, some food products, energy resources and tariffs administratively established by the Government are referred to such goods.

**Discount rate** is the tool used as the basic reference point when determining the value of monetary resources in the economy. The size of the discount rate is equal to the average value of the yield of 28-day NBKR Notes for the recent 4 auctions on placement of NBKR Notes.

**GDP deflator** is composite index of the economy branches prices, characterizing GDP with regard to growth of prices in the economy. GDP deflator is calculated as the proportion between nominal GDP in prices of the current year against GDP rate of the previous year.

**Inflation** represents the increase in the general level of consumer prices in the economy. The consumer price index is used to quantitatively estimate the rate of inflation. The CPI shows the change in the price level for the goods and services purchased by the population for non-productive consumption. In the calculations of the price index of buyers of selected 342 goods and services is applied and the size of the sample makes 45 thousand prices a month of 1496 trading enterprises and spheres of services in seven city and two regional centers.

**Monetary base** – the obligations of the National Bank of cash put into circulation and the obligations of the National Bank to other depository corporations in national currency of the Kyrgyz Republic.

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

**M0** – currency in hands.

**M1** – M0 + demand deposits in national currency.

**M2** – M1 + time deposits in national currency.

**M2X** – M2 + deposits in foreign currency.

**Money in circulation** – the money in circulation less cash held in NBKR.

**Non-financial assets** include the following categories of economic assets: fixed assets, stocks of tangible current assets, values and non-produced assets (natural and intangible assets).

**Notes** are the Government short-term securities, issued by the NBKR for the term of 7, 14, 28, 91 and 182 days through the weekly auctions. The yield is defined depending on the supply and the demand among the commercial banks. The goal of conducting the auctions of notes is the withdrawal of liquidity in national currency from the banking system.

**Other depository corporations** – all financial resident corporations, except for the central bank, the main activity of which is financial intermediation and which emit the commitments included in the national definition of broad money supply (M2X).

**“Overnight” credit** is given in national currency for one day, for collateral, for maintenance of short-term liquidity of the bank. Government securities of the Kyrgyz Republic placed through the NBKR, with the date of redemption up to 12 months from the date of delivery of the overnight credit are accepted as collateral. The interest rate is set at the rate of 1.2 of the NBKR discount rate. The credit is used on the initiative of the commercial bank.

**Repo operations** – purchase (repo)/selling (reverse repo) operations of government securities with an obligation of their reverse sales/purchase on a specific date in future and at a price agreed earlier.

**Producer price index** measures the average changes in the sales prices got by the local producers for their output. Information, used in the PPI calculations, is collected from 148 enterprises, which represent almost each branch in the industrial sector of the economy. The list of enterprises combines those most typical for the given industry, characteristic for the given region, and irrespective of patterns of ownership.

**Renewable State Treasury Bills for settlement** are the coupon securities with maturities of 3, 6 and 12-months, issued by the Ministry of Finance as a result of restructuring the debt of the Government of the Kyrgyz Republic to the NBKR. The renewable nature of these securities means the following: on the day of redemption of ST-Bills(s) in the NBKR portfolio, the Ministry of Finance simultaneously with the redemption issues new series of ST-Bills(s) in favor of in number equal to the number of sinking securities.

**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 is the emitter of ST-Bills. Issues of ST-Bills are placed weekly and through the NBKR auctions. Direct participants (primary dealers, finance and credit institutions, which concluded the contract with the NBKR) enjoy the right of participation in the auctions. Owners of

ST-Bills of the Kyrgyz Republic could be both the legal entities and the individuals. The admission of foreign investors to the market of ST-Bills is not limited. The transactions in the secondary market of ST-Bills are conducted through the electronic trading system of the NBKR, which allows the primary dealers and their clients to conduct the ST-Bills purchase/sale operation 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 1 year. The issuer of ST-Bonds is the Ministry of Finance. The NBKR is the general agent servicing issues of ST-Bonds.

**State budget operating expenditures** are all of the operations, which lead to the reduction in the net value of assets of the government sector, except for the operations on purchase of non-financial assets.

**Structure of money incomes by quintile groups** reflects the differentiation of the population by size of income for the five (quintile) groups, each of which consists of 20 percent of the population. This approach to determine the income differentiation implies the division of the total ranked population into five equal groups, thus emphasizing, for example, on the proportion of the total income of the society, falling at groups with largest or lowest incomes.

**Swap operations** – operations on the exchange of funds in national currency in the amount equivalent to the amount in foreign currency or, on the contrary, to the obligation of the reverse exchange of principal amounts and accrued interest on the stipulated conditions.

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## Abbreviations

CIF	Cost, Insurance, Freight
CIS	Commonwealth of Independent States
CPI	Consumer Price Index
FOB	Free on Board
GDP	Gross Domestic Product
HPP	Hydro Power Plant
KR	Kyrgyz Republic
LLC	Limited Liability Company
MPC	Monetary Policy Committee
NBKR	National Bank of the Kyrgyz Republic
NCOSH	Non-Commercial Organizations Serving Households
NFCI	Non-Finance and Credit Institutions
NSC	National Statistics Committee
POL	Petroleum, oil, lubricants
PPI	Producer Price Index
SCC	State Customs Committee
SE	State Enterprise
SFRB	Specialized Fund for Refinancing of Banks
ST-Bills	State Treasury Bills
ST-Bills(s)	State Treasury Bills for settlement
ST-Bonds	State Treasury Bonds
USA	United States of America