

**NATIONAL BANK
OF THE KYRGYZ REPUBLIC**

**Monetary Policy Report
Quarter 3, 2021**

**Bishkek
November 2021**

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

Monetary policy in the Kyrgyz Republic

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

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

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

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

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

Monetary Policy Report for Q3 2021 was approved by the Resolution of the Board of the National Bank of the Kyrgyz Republic No. 2021-II-07/65-1-(ДКП) dated November 29, 2021.

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Summary

The global economic recovery slowed down amid ongoing restrictive measures taken to prevent new outbreaks of COVID-19. Problems in the global supply chains amid rapid growth of demand for food products and raw materials aggravate the global inflationary processes that emerged in the previous quarter. Continuing rise in prices in the international commodity markets and acceleration of the inflation rate in the trading partners have a significant negative impact on price dynamics in the Kyrgyz Republic.

In the Kyrgyz Republic, there are positive trends in economic recovery. In January-September 2021, the GDP growth rate was 0.1 percent compared to the same period of 2020. The reduction in production output at the “Kumtor” gold-mining enterprise is still regarded as a restraining factor for the full economy recovery in the Kyrgyz Republic. At the same time, the growth rate of GDP, excluding the “Kumtor” gold-mining enterprises, remained at the level of 3.6 percent throughout Q3.

In Q3 2021, the trade balance was formed under the influence of an increase in the import and export operations. Imports increased by 46.1 percent, whereas export increased by 10.8 percent. As a result, the country’s trade deficit amounted to USD 729.9 million. The volume of foreign trade turnover increased by 32.8 percent and amounted to USD 2.0 billion. In Q3 2021, the volume of remittances increased by 4.1 percent compared to the same indicator in 2020.

According to the preliminary results for January-September 2021, the state budget surplus amounted to KGS 3.7 billion, or 0.8 percent to GDP (in the same period of 2020, the budget deficit amounted to KGS 15.6 billion or 3.7 percent to GDP). The primary surplus¹ of the state budget amounted to KGS 10.4 billion, or 2.2 percent to GDP. Tax and non-tax revenues continue to make a positive contribution to the growth of budget revenues (33.3 and 9.5 percentage points, respectively).

As of the end of September 2021, consumer prices increased by 6.5 percent year-to-date (in annual terms, inflation was 13.5 percent). The greatest contribution to the existing rise in prices was made by food products, among which an increase in prices for four types of food products was the determining one: meat, sunflower oil, sugar and bread. More than 40 percent of the inflation was accumulated year-to-date due to an increase in prices for these four goods.

The current course of monetary policy was continued. The situation in the money market remains stable. The short-term interest rates grew and formed within the interest rate corridor. In the reporting period, there was an increase of excess liquidity in the banking system after a cycle of decline. In these conditions, there was a decrease in the banks’ activity in the short-term segment of the interbank credit market, and the interest in short-term placements in the open market increased. At the same time, a positive dynamics of lending to the economy and the expansion of the banks’ depository base remain.

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

Chapter 1. External Environment

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

In the reporting period, a slowdown in economic recovery and a rapid rise in consumer prices were observed in most of the main trading partners of the Kyrgyz Republic.

In Q3 2021, the economic growth in Russia demonstrated slowdown amid tightening restrictive measures against the spread of COVID-19.

The economy of Kazakhstan continued to show positive growth dynamics, however, there was rapid acceleration of the inflation rate in the reporting period.

The gross domestic product growth in Belarus continues to slow down, prices demonstrate further increase.

In Armenia, consumer activity grew faster compared to previous expectations. The inflation rate in Armenia continued to accelerate amid ongoing pro-inflationary effects in the country and in the external sector.

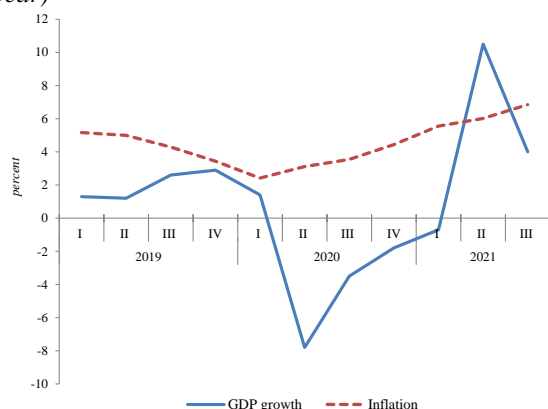
In Q3, the economic growth of China slowed down, which raise fears of the PRC's trading partners and global financial markets. There was a large gap between the producer prices and the consumer prices amid consumer prices regulation by the government and increased producer costs due to the energy crisis, disruptions in supplies of intermediate and raw materials, and an increase in prices for energy and building materials.

In the United States, economic recovery demonstrated slight slowdown amid restricted supply and peak demand due to ongoing concerns over COVID-19. At the same time, inflation in the United States accelerated amid rise in prices for raw materials and food products in the world market, as well as a limited supply of a number of goods due to current logistical problems.

Russia

Chart 1.1.1. Growth of GDP and Inflation in Russia

(quarter to the corresponding quarter of the previous year)



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

In the reporting quarter, there was a slowdown in the economic growth of Russia, demonstrating its return to the balanced growth path. According to the Ministry of Economic Development of the Russian Federation, in September, GDP grew by 3.4 percent in annual terms after 3.7 and 5.0 percent in July and August, respectively. In Q3 2021, the GDP growth was 4.0 percent in annual terms. According to the Bank of Russia, harvest reduction and aggravation of the epizootic situation conditioned the growth rate slowdown in the reporting period. At the same time, consumer demand continued to have a major positive impact on economic growth. In turn, consumer activity was supported by accelerated growth in lending, lump-sum budget payments, and growth in real wages. Increasing internal and external demand, as well as high corporate profits, contributed to ongoing investment activity. At the same time, the service sector recovery was restrained by a difficult epidemic situation.

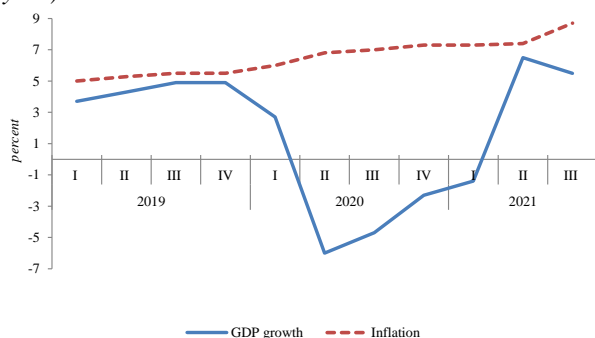
According to the Russian Federal State Statistics Service, in Q3 2021, the inflation rate in Russia was 6.9 percent to the corresponding quarter of the previous year; in September 2021, its annual value increased by 0.7 percentage points, up to 7.4 percent. According to the Bank of Russia, about two-thirds of the growth was formed by one-time factors: accelerated

growth in prices for fruits and vegetables, the effect of the base in the dynamics of prices for educational services and foreign tourism. The group “food products” demonstrated the most significant acceleration of the annual growth in prices, up to 9.2 percent (by 1.5 percentage points compared to August). The prices for non-food products increased by 8.1 percent in annual terms (+0.1 percentage points), for services – 4.2 percent (+0.4 percentage points).

Kazakhstan

Chart 1.1.2. Growth of GDP and Inflation in Kazakhstan

(quarter to the corresponding quarter of the previous year)



Source: RK Statistics Agency, NBRK calculations

In the reporting period, Kazakhstan still demonstrated positive economic growth rates. In January-September of the current year, GDP growth was at 3.4 percent (in the same period of the previous year, there was a decline by 2.8 percent). In the reporting period, there was continued growth in the real sector, in particular, in the processing sector the volume of production increased by 5.7 percent, the volume of construction increased by 9.7 percent, and agricultural growth constituted 1.4 percent. Revival in the services sector, strengthening of the trade balance due to faster export growth and high

investment activity in the non-extractive industries were the main drivers of the economic growth recovery.

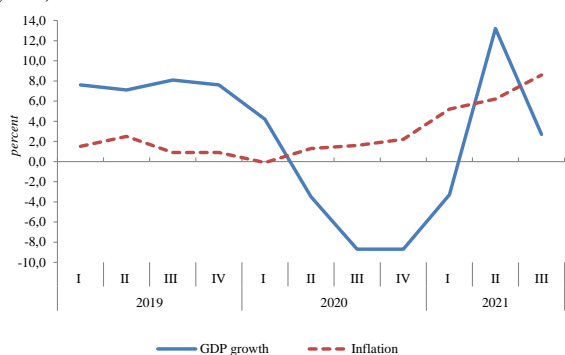
According to the Bureau of National Statistics of the Agency for Strategic Planning and Reforms of the Republic of Kazakhstan, in the reporting period, the inflation demonstrated continued acceleration. At the end of September, the annual inflation rate in Kazakhstan was 8.9 percent, while in June it was at the level of 7.9 percent. In September, the food products made the main contribution to an increase in prices, the growth rate thereof increased from 10.6 percent in June up to 11.5 percent. A significant rise in prices for poultry and beef amid strong global demand and limited supply, as well as price upsurge for dairy products due to rise of prices by the domestic producers influenced acceleration of food inflation. However, there was a slowdown in price upsurge for sugar, oils and fats, which previously demonstrated active growth. In September, non-food annual inflation rate increased up to 7.5 percent (in June 2021 – 6.9 percent). There was primarily increase in prices for household goods, building materials and petroleum, oil and lubricants due to supply disruptions, increased prices for imports and increased demand amid recovery in real incomes of the population. In September, prices for paid services accelerated up to 6.8 percent (in June 2021 – 5.6 percent), mainly due to opening of the educational institutions and a significant rise in the cost of all types of education services. The growth rate of tariffs for regulated services slowed down slightly due to a decrease in prices for water supply services.

In Q3, the National Bank of the Republic of Kazakhstan increased the key rate twice from 9.00 up to 9.25, then up to 9.50 percent, and last time in October – up to 9.75 percent. The decision to increase the key rate was taken amid current pro-inflationary pressure in the economy, price upsurge in the world markets, accelerated inflation in the trading partners and high inflationary expectations within the country.

Armenia

Chart 1.1.3. Growth of GDP and Inflation in Armenia

(quarter to the corresponding quarter of the previous year)



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

demonstrated growth, while investment activity remained weak.

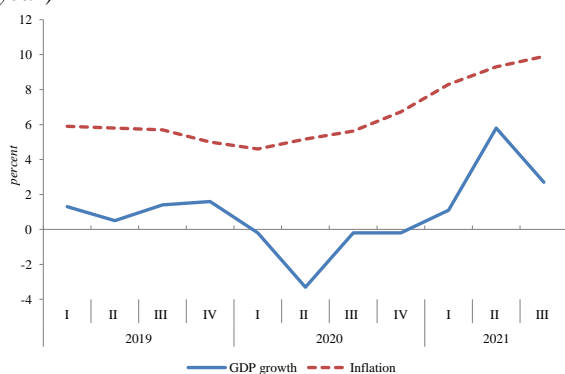
The inflation rate in Armenia accelerated from 6.5 percent in June 2021 up to 8.9 percent in September 2021 in annual terms (1.4 percent in the previous year) due to an increase in prices for food products by 14.7 percent and non-food products – by 9.9 percent with an increase in tariffs for services by 1.6 percent. Global delays in the supplies of goods and high inflationary expectations continued to act as pro-inflationary factors.

Amid high inflationary environment, the Central Bank of Armenia increased the key rate five times year-to-date: from 5.25 up to 7.25 percent. The regulator notes that the consistent, future-oriented tightening of monetary conditions undertaken since the end of last year, has a sufficient impact on the regulation of outstripping demand and inflation control. The inflation rate is expected to remain high until the end of 2021, to approach the target of 4.0 percent in 2022 and remain near this target in the medium term.

Belarus

Chart 1.1.4. Growth of GDP and Inflation in Belarus

(quarter to the corresponding quarter of the previous year)



Source: National Statistical Committee of the Republic of Belarus

Industrial production growth in Belarus remains at the level of 2.3 percent after 3.7 percent in July and 2.7 percent in August. Investments demonstrate a negative growth rate – (-)9.1 percent in September. The analysts believe that it is the result of increased uncertainty during the coronavirus period. Retail trade turnover is also low – 1.7 percent. The EDB analysts believe that slowdown in income growth and, possibly, another wave of a pandemic affect goods consumption.

In Q3 2021, there was an increase in consumer activity in Armenia outstripping production potential growth. Despite rapid spread of the new variant of coronavirus, the country's economy suffered positive impact of the economic activity recovery in Armenia's main partners and the positive dynamics of demand provided by private consumption due to the large volume of remittances from abroad and a decline in private savings. According to the preliminary data, in January-September 2021, the indicator of economic activity in Armenia increased by 4.4 percent. All sectors, excluding agriculture and power generation,

Belarus still demonstrates slow economic growth; at the end of Q3 2021, economic growth slowed down to 2.7 percent.

In September, GDP growth remained below 1.0 percent due to a decrease in agricultural production by almost 14.0 percent. According to the EDB analysts, positive dynamics is observed in the information and communications sector, the gross value added thereof increased by 9.6 percent during nine months. The EDB experts assume that the growth rates indicate that the restrictions imposed by a number of western countries have not yet had a

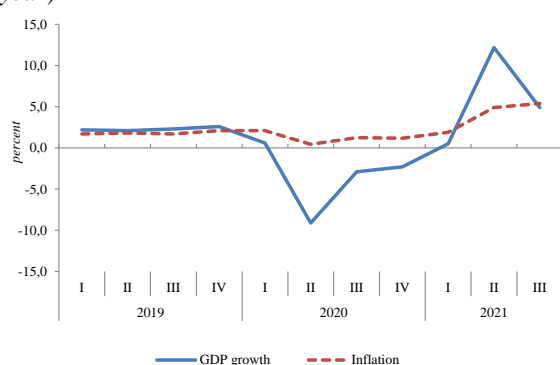
In September, the consumer price index in Belarus increased by 10.2 percent compared to the same period in 2020. In annual terms, the prices for food products increased by 11.2 percent, for non-food products – by 10.3 percent, for services – by 8.5 percent. Annual inflation acceleration in Belarus is due to the decisions taken in the field of constantly regulated prices (tariffs), an increase in prices in the market for non-food products, as well as continuing pressure from the world food prices.

Initially, the official forecast set the threshold for the inflation rate in 2021 at 5.0 percent, afterwards the National Bank of Belarus adjusted the inflation forecast for 2021 to 7.0 percent, and at the end of July it again changed the benchmark by increasing the inflation threshold up to 9.0 percent by the end of the year.

USA

Chart 1.1.5. Growth of GDP and Inflation in the USA

(quarter to the corresponding quarter of the previous year)



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

In the reporting period, the US economic recovery slowed down amid negative consequences of the pandemic. Thus, the GDP growth rate was restrained due to problems in the production supply chains, a shortage of labor and uncertainty about the spread of a new variant of coronavirus. According to the Bureau of Economic Analysis of the U.S. Department of Commerce, in Q3 2021, real GDP in the USA increased by 4.9 percent¹ compared to the same period of 2020 (12.2 percent in the previous quarter).

Most districts in the United States demonstrated an increase in consumer expenditures. Development of the tourism sector was different in each individual district: there was gradual recovery in activity and a decrease in activity amid an increase in the incidence of coronavirus. Industry in each district developed at moderate and high rates. Real estate activity did not change or slowed down slightly.

US employment rate demonstrated moderate growth, it was restrained by strong labor demand and labor shortages. Transport and technology companies experienced particularly severe labor shortages, and many businesses in the sales, industrial and hospitality sectors were forced to cut their work hours or production. Thus, in September 2021, the unemployment rate in the United States decreased down to 4.8 from 5.2 percent in the previous month.

In September 2021, the consumer prices in the United States increased by 5.4 percent in annual terms (5.3 percent in the previous month), having reached their highest level during 13 years. Meanwhile, the US core inflation rate, excluding food and energy prices, was 4.0 percent in annual terms. Prices for food products increased by 4.6 percent, while energy prices increased by 41.7 percent. The main reason for such an increase in inflation in September 2021, first of all, was energy price upsurge. The rise in energy prices is driven by growing demand, which is recovering from the coronavirus pandemic consequences. The plants have to ramp up production that requires energy, however energy supplies are limited.

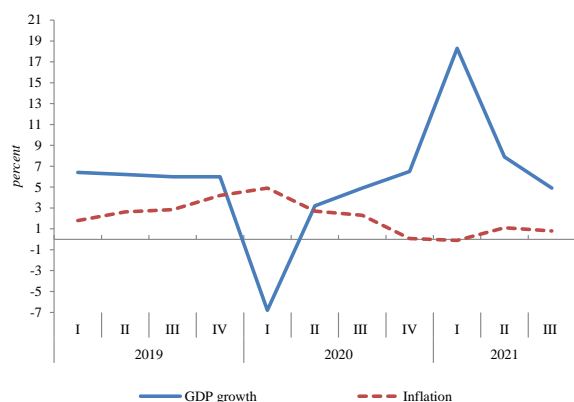
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¹ Preliminary estimate.

China

Chart 1.1.6. Growth of GDP and Inflation in China

(quarter to the corresponding quarter of the previous year)



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

In Q3 2021, the economy of China demonstrated moderate growth, slowing down to 4.9 percent from 7.9 percent in Q2.

The economy of China suffers the attack from all directions - destroying outbreak of the COVID-19 delta strain, real estate troubles, energy crisis, fall of consumer confidence and commodity price upsurge. The severe power shortages faced by the world's largest exporter will undermine domestic economic growth and can also negatively impact supply chains, hitting the global economy, which is fighting against the pandemic.

Nevertheless, experts believe that the country will be able to achieve planned 6.0 percent growth at the end of 2021.

At the consumer level, the inflation rate in China remains low, slowing down to 0.7 percent in September in annual terms, while producer-level inflation in China reached 10.7 percent in the same month, the highest since November 1995. Producer prices growth due to rise in costs amid energy crisis, supply disruptions and an increase in prices for raw materials. The government's attempts to hold consumer prices so far prevented the inflation from spilling over into the domestic market: the Chinese government obliged the enterprises to cover all costs themselves, reducing their own margin, without imposing their costs on the consumers.

The experts assume that the gap between the growth rates of producer prices and the cost of consumer goods reflect gradual pressure from the inflationary burden on the end consumer. There are already estimates of expectations for an increase of consumer prices already at the beginning of Q4 of the current year, since it is impossible to restrain the inflationary wave for a long time.

The annual inflation target set by the Chinese government remains unchanged at 3.0 percent in 2021 compared to 3.5 percent in 2020.

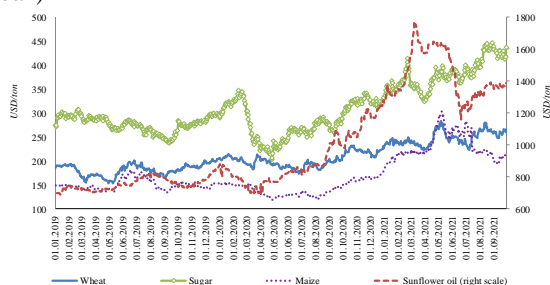
1.2. World Commodity Markets

Since the beginning of the pandemic, prices for food products and raw materials remained high worldwide, including Kyrgyzstan. This was due to the growth rate of prices in the world commodity markets, as well as the trend in the domestic and global economies. In the reporting period, there was an increase in demand in the oil market amid the global economic recovery. There was a decrease in investment interest in this asset in the global gold market due to an increase in the key rates in a number of countries.

Food Market

Chart 1.2.1. Dynamics of Prices for Food Products

(month to the corresponding month of the previous year)



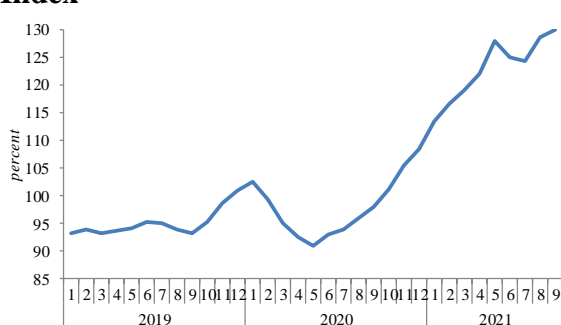
In Q3 2021, there was price upsurge in the world food markets, excluding quotations for maize. In Q3 2021, world prices for wheat increased by 2.7 percent compared to the previous quarter, whereas these prices increased by 33.5 percent compared to the same period of the previous year. This situation was due to deterioration of forecasts for harvest in several large exporting countries. In the reporting period, the US Agricultural Department reduced the estimate of the Russian grain harvest by 12.5 million tons (from 85.0 million down to 72.5 million tons, excluding Crimea). Therefore, there was price upsurge for wheat in the world market. As a result, the wheat market increased in different proportions in the USA and Europe. Prices for American grain of various types rose to a lesser extent compared to the ports of France and Russia.

Quotations for maize had multidirectional dynamics, however in general there was a downward trend due to improved general forecasts for harvest and initiation of the harvesting campaign in the United States and Ukraine.

In the reporting quarter, the global increase in prices for sunflower oil accelerated, after two consecutive months of decline due to a reduction of export supply in the Black Sea region, while waiting for the harvest of 2021–2022 season to enter the market. Thus, the world prices for sunflower oil in annual terms (quarter to the corresponding quarter of 2020) increased by 55.3 percent.

In Q3 2021, world sugar prices increased by 11.7 percent compared to the previous quarter, whereas these prices increased by 61.7 percent compared to the same period of the previous year. This was due to freezing weather in Brazil, the world's largest sugar exporter, as well as price upsurge for crude oil. At the same time, the forecasts for good harvest in India and the European Union contributed to restraining an increase of the world prices. Thus, after five months of continuous growth, sugar prices reached their highest level since February 2017.

Chart 1.2.2. Dynamics of FAO Food Price Index



as wheat and vegetable oils (palm oil).

Prices in the world food markets have a significant impact on inflation in Kyrgyzstan and often play a critical role in the CPI dynamics formation. This is due to the significant

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The FAO¹ food price index has been increasing during the past 15 months. In June and July 2021, the first decline was recorded in 12 months, however at the end of the reporting quarter, the upward trend was again observed. Thus, in Q3 2021, the average FAO food price index increased by 33.1 percent compared to the same quarter of 2020 and amounted to 127.6 points. In the reporting period, the growth of the FAO food price index was mainly due to a decrease in supply and high demand, primarily for products such

¹ The FAO food price index is a weighted average that tracks international price movements for five major food commodity groups (meat, dairy products, crops, vegetable oils and sugar).

degree of price dependence in the country on the foreign markets, as well as the fact that food products, which occupy about half of the consumer basket, make a significant contribution to general inflation.

Energy Market

Chart 1.2.3. Dynamics of Oil Prices
(in USD)



In Q3 2021, the world oil prices demonstrated shift towards steady growth due to recovery in the global demand after lockdowns and OPEC+ actions, which contributed to stable high prices for oil.

In Q3 2021, the average price for Brent oil increased by 6.0 percent compared to the previous quarter and amounted to USD 73.3 per barrel (compared to the same period of the previous year, the price increased by 69.0 percent).

During the reporting period, there was great uncertainty in the world oil market being aggravated by concerns about the conflict of OPEC + participants (Saudi Arabia

and the United Arab Emirates) to take market share without reaching an agreement.

Moreover, further deterioration of the situation due to the COVID-19 delta strain had a significant impact on the quotations and volatility of the oil market. At the end of Q3 2021, the world oil prices increased based on the prospects of demand recovery and supply deficit amid disruptions in US production after Ida¹ Hurricane.

Currently, the world oil market continues to face the risks of reduced investment in exploration and development of new deposits, as well as the risks related to weather factors: hurricanes in the Gulf of Mexico, where a significant part of the oil is produced and processed in the United States.

According to Goldman Sachs, the forecast for Brent oil price was increased from USD 80.0 up to USD 90.0 per barrel as of the end of 2021 as the oil shortage in the market cannot be eliminated in the coming months. The Bank of America assumes that by the end of 2021, the world oil prices can reach USD 100.0 per barrel for the first time since 2014, provided that winter in the Northern Hemisphere is colder than usual.

Currently, the median forecast of the world analysts for Q4 2021 is USD 77.0 per barrel, and for 2022 – USD 72.0 per barrel.

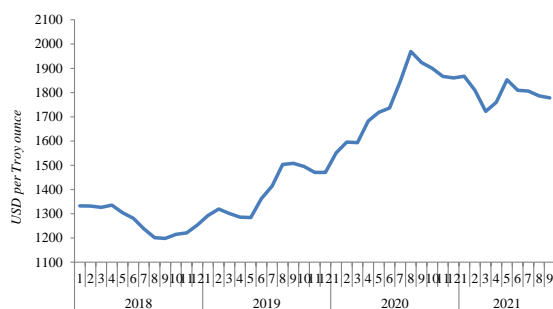
World oil prices have a significant impact on the export price formation in the countries that produce petroleum, oil and lubricants and often play a critical role in price formation at the Russian refineries with Kyrgyzstan to import almost 95 percent of the total volume of imported petroleum, oil and lubricants.

The inflationary component and prices in the world energy markets both largely determine the level of economic activity in Russia and Kazakhstan, which is among the most important factors of demand in the domestic economy.

¹ Ida Hurricane is the 4th category Atlantic cyclone that destroyed the south-eastern part of the United States in August-September 2021. The consequences of the hurricane also spread to the north-eastern part of the United States.

Gold Market

Chart 1.2.4. Dynamics of Prices for Gold



Source: IA Bloomberg

In the reporting period, there was a slight decrease in prices in the gold market amid a reduction in demand for global. According to the World Gold Council (WGC), the world demand for gold decreased by 13.0 percent compared to the previous quarter and by 7.0 percent compared to the same period of the previous year, and amounted to 831.0 tons of gold. The main reason for decline in interest in gold was the decrease in demand for it from the professional investors, whereas the private

investors, primarily from India and China, as well as the jewelry industry increased their purchases. The central banks demonstrated demand for gold amid accelerating inflation. Thus, the Reserve Bank of India (41.0 tons), the Central Bank of Uzbekistan (23.0 tons), the Central Bank of Brazil (9.0 tons) and the Bank of Russia (about 6.0 tons) are the largest buyers of the yellow metal.

In the reporting period, the average price for gold decreased by 1.3 percent compared to the previous quarter and amounted to USD 1,790.1 per Troy ounce. At the same time, the price for gold varied within the range of USD 1,726.0-1,829.0 per Troy ounce. Rise in the US Treasury yields, strengthening of the US dollar and an increase of the interest rates at a number of central banks had a negative impact on the investors' preferences.

At the end of the reporting period, the world gold supply decreased by 3.0 percent per year, down to 1.2 thousand tons. Of the total volume, primary gold production increased by 4.0 percent, up to 1.0 thousand tons, secondary processing decreased by 22.0 percent, down to 0.3 thousand tons.

The policy of global regulators remains the main factor that affects the price for gold. If this policy is tightened in response to the inflation growth, prices are likely to decrease.

Chapter 2. Macroeconomic Development

2.1. Demand and Supply in the Commodities and Services Market

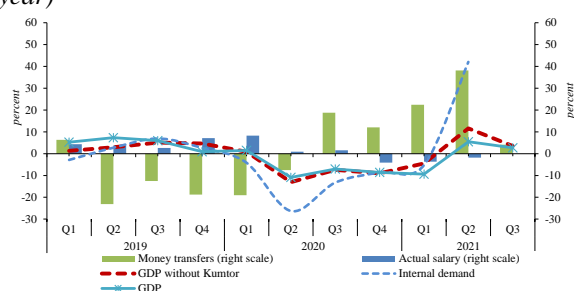
For the first time since the spring of 2020, GDP growth rate demonstrated positive values at the end of nine months of the current year to reflect gradual economic recovery of the Kyrgyz Republic. In Q2, there was sharp increase in the dynamics of domestic demand due to growth in the volume of remittances. The inflow of remittances into the country demonstrates ongoing positive trend. A decrease in production output at the country's largest "Kumtor" gold-mining enterprise continues to make a negative input in GDP growth based on the results of nine months.

At the same time, the economy of the country remains uncertain amid current negative impact of the pandemic consequences, considering the risks of appearance of new variants of COVID-19, as well as the risk of the socio-political instability following the parliamentary elections. The consequences of such natural and climatic factors as drought, probable winter with little snow and low water pose additional risks for further economic growth of the country.

Demand

Chart 2.1.1. Dynamics of Internal Demand and Money Transfers

(quarter to the corresponding quarter of the previous year)



Source: NSC KR, calculations: NBKR

For the first time after the recession observed in March 2020, the economy of the Kyrgyz Republic reached a positive value of 0.1 percent at the end of January-September of the current year. At the same time, GDP growth rate, excluding "Kumtor" gold-mining enterprises, remained at the level of 3.6 percent at the end of nine months since January-July of the current year.

At the same time, in Q2¹, domestic demand demonstrated a significant recovery, having increased by 42.0 percent according to the preliminary data from (-)5.3 percent in Q1 2020 (in Q2 2020, there was a decrease by 26.3 percent). The recovery in domestic demand was mainly due to an increase in remittances. In January-September 2021, net inflow of individuals' remittances via the money transfer systems in USD increased by 19.0 percent compared to the same period of 2020.

According to the results of January-September of the current year, the average monthly nominal wage per one employee² amounted to KGS 19.6 thousand, having increased by 9.5 percent compared to the same period of 2020. Positive growth rates are also conditioned by an increase in labor demand in the first half of the current year³. At the end of six months, net number of created jobs increased almost in all sectors of the economy, therefore the nominal wages increased by 7.8 percent compared to the same period of 2020. The upward trend in the nominal wages in some sectors of the economy may be conditioned by emerging economic recovery. An increase in the growth rates of average monthly nominal wages was mainly observed in such sectors as transport and storage of goods (31.1 percent), information and communication (15.6 percent), as well as transactions with real estate

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

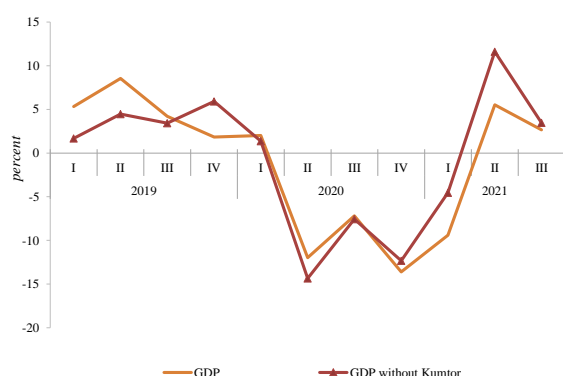
² Generally in the republic, excluding small enterprises.

³ Reference to the data for the earlier period is given due to the lack of more up-to-date data.

(15.5 percent). Meanwhile, in January-August 2021, the decrease in the overall indicator of real wages constituted (-)2.1 percent compared to the same period of 2020.

Chart 2.1.2. GDP Dynamics

(quarter to the corresponding quarter of the previous year)



Source: NSC KR, calculations: NBKR

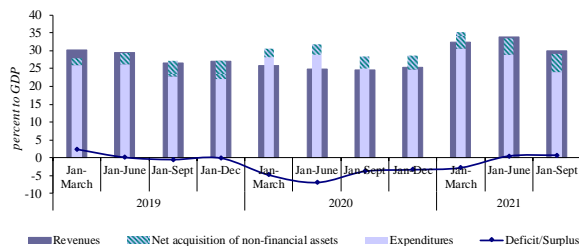
In Q3, economic growth (+2.7 percent after 5.5 percent in Q2 of the current year) was mainly conditioned by the positive growth rates in many sectors, excluding agriculture. In the reporting quarter, industry and construction achieved positive growth rates (6.4 and 0.1 percent, respectively). However, in the industrial sector, the production output of “Kumtor” gold-mining enterprise still remained with negative value (-3.9 percent). During Q3, agriculture remained in the negative area (8.6 percent) due to shortage of irrigation water and drought, which, in turn, resulted in a decrease of plant production output.

Public Finances Sector

According to the preliminary results for January-September 2021, the state budget surplus amounted to KGS 3.7 billion, or 0.8 percent to GDP (during the same period of 2020, the state budget deficit amounted to KGS 15.6 billion or 3.7 percent to GDP). The primary state budget surplus¹ amounted to KGS 10.4 billion or 2.2 percent to GDP.

Chart 2.1.3. Execution of the State Budget

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



Source: CT MFKR, NBKR

The state budget revenues from operating activities increased by 41.5 percent or KGS 42.6 billion compared to January-September 2020 and amounted to KGS 145.3 billion or 29.9 percent to GDP. Tax revenues occupy the largest share in the structure of current revenues (73.9 percent). Tax and non-tax revenues made a positive input in an increase of budget revenues in the amount of 33.3 percentage points and 9.5 percentage points, respectively, whereas the official transfers made a negative input in the amount of 1.3 percentage points due to reduced grants from the international organizations.

The state budget expenditures for operating activities increased in annual terms by 13.0 percent or KGS 13.5 billion and amounted to KGS 117.2 billion or 24.1 percent to GDP. The structure of expenditures by economic classification demonstrated an increase in expenditures for all items, as well as due to the fact that since January 2021, the expenditures from the “special account²” are classified according to the corresponding expenditure items (wages, subsidies, social benefits, etc.). Expenditures for civil service, education, health care

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

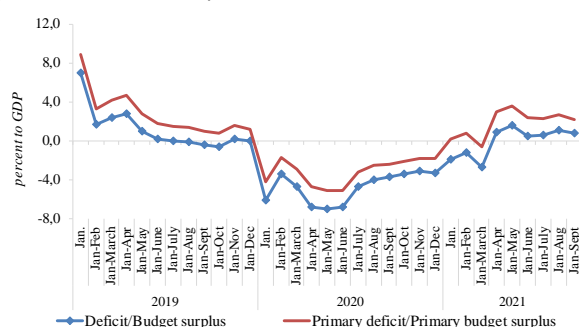
² Special accounts are the accounts with the receipts recorded in the following forms:

- provision of paid state and municipal services;
- sponsor support and voluntary contributions;
- guardianship fees;
- charitable or grant aid;
- deductions from the international institutions for joint research work;
- funds from the sale of own-produced goods.

and economic issues made the most significant input in an increase of expenditures in the structure of expenditures by functional classification.

Chart 2.1.4. Budget Deficit

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



Source: CT MFKR, NBKR

Investments

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

	January-September			
	2020	2021	2020	2021
	millions of KGS		share, percent	
Total	77 632.3	74 685.0	100.0	100.0
Internal investment	57 111.6	58 191.8	73.6	77.9
Republican budget	2 028.8	2 530.7	2.6	3.4
Local budget	644.0	834.2	0.9	1.1
Funds of enterprises and organizations	28 106.5	27 082.8	36.2	36.3
Banks' credits	639.6	997.6	0.8	1.3
Population funds including beneficent help of KR residents	25 692.7	26 746.5	33.1	35.8
External investment	20 520.7	16 493.2	26.4	22.1
Foreign credit	13 464.9	11 791.0	17.3	15.8
Direct foreign investments	4 476.1	1 400.1	5.8	1.9
Foreign grants and humanitarian aid	2 579.7	3 302.1	3.3	4.4

Source: NSC KR

Source: NSC KR

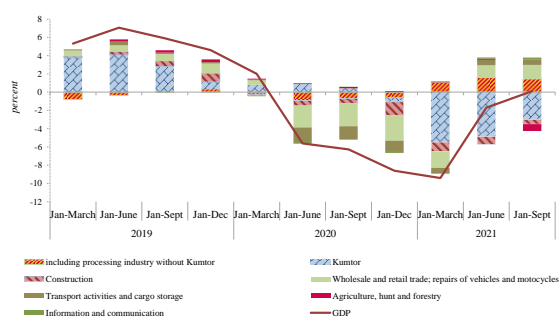
there was a decrease in the volume of capital investments financed from the foreign sources (-21.4 percent), whereas the volume of domestic sources increased by 0.1 percent. At the same time, the investments financed from the local budget increased by 26.8 percent, from the republican budget – by 22.4 percent, from the bank loans – by 1.5 times.

Supply

According to the preliminary data of the National Statistical Committee of the Kyrgyz Republic, in January-September 2021, the nominal GDP increased by 0.1 percent in real terms compared to the corresponding period of 2020 (according to updated data for January-September 2020, a decrease was 6.3 percent) and amounted to KGS 485.7 billion.

Chart 2.1.5. Input of Main Sectors in GDP Growth

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



Source: NSC KR, calculations: NBKR

Net outflow of budget funds for operations related to acquisition of non-financial assets (including operations in the following groups: fixed assets, reserves, land) increased by 1.7 times or by KGS 9.9 billion compared to January-September 2020 and amounted to KGS 24.4 billion or 5.0 percent to GDP. The bulk of capital expenditures falls on acquisition of buildings and structures.

In January-September 2021, the level of capital investments exploitation, decreased by 5.6 percent compared to the same period of 2020, after a decline by 11.8 percent in the first half of the current year.

Decrease of capital investments was observed in the construction of mining, processing, wholesale and retail trade facilities, and others.

At the end of nine months of 2021,

Primarily, the sector of services (+2.5 percent) made a positive input. At the same time, aggravated situation in certain sectors had a restraining effect on GDP growth. Such sectors of economy as industry ((-)1.2 percentage points), agriculture ((-)0.7 percentage points) and construction ((-)0.5 percentage points) made a negative input in economic decline.

In January-September of the current year, the industrial production output reduced by 5.3 percent compared to the corresponding period of 2020 due to a decrease in the output of pharmaceutical products (by 42.0 percent),

chemical products (by 35.0 percent), basic metals and finished metal products, excluding machinery and equipment (by 21.2 percent), as well as due to a decline in the textile sector, in the production output of clothes and footwear, leather and leather products (by 2.7 percent). At the same time, the mining sector continued to demonstrate steady growth since January-June of the current year (+10.3 percent). The volume of industrial production output excluding “Kumtor” gold-mining enterprises increased by 18.9 percent (in January-August 2020, a decrease by 9.5 percent).

A reduction in the agricultural production output by 5.0 percent at the end of nine months was due to a decrease in plant production output (by 11.2 percent).

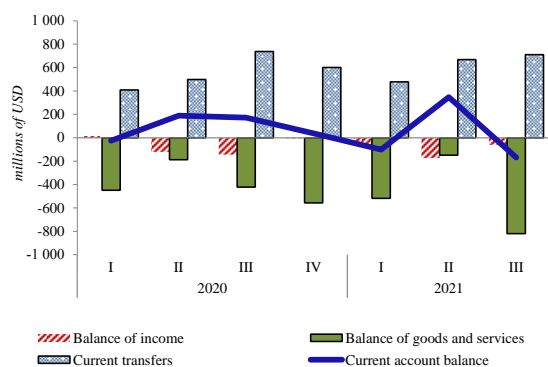
In January-September of the current year, a decline in the construction sector by 7.2 percent compared to the corresponding period of the previous year, in particular, was conditioned by reduced capital investment due to a decrease in external sources of funds by 21.4 percent, whereas the volume of internal funds increased slightly by 0.1 percent.

The GDP deflator was positive and amounted to 16.9 percent, having increased by 11.7 percentage points compared to January-September 2020 (in the same period of 2020, the deflator was also positive at 5.2 percent).

2.2. External Sector¹

In Q3 2021, the current account was formed with a negative sign under the influence of an increase in the negative balance of goods trade and services.

Chart 2.2.1. Current Account



Note: According to the preliminary and forecasted data.

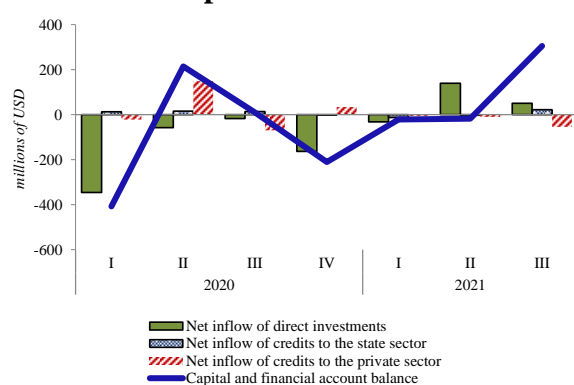
FOB prices) increased by 46.1 percent, to make USD 1,340.9 million. Growth in the value of import was largely due to price increase. There was an increase in import of goods such as clothes, petroleum products, cars and vehicles principally designed for the transport of persons, footwear. Import, excluding energy products, increased by 41.4 percent compared to the same period of the previous year, to make USD 1,147.9 million.

In the reporting period, the export of goods (in FOB prices) increased up to USD 611.0 million. There was an increase in export of rolled glass and glass with a polished surface, cast iron and steel, car parts and accessories. At the same time, there was a decrease in the supplies of vegetables, fruits, precious metals ores and concentrates and other goods.

In the reporting period, the net inflow of current transfers decreased due to a decline in the inflow of official transfers. The net inflow of private transfers was at the level of Q3 2020 and amounted to USD 711.9 million. In the reporting quarter, the balance of services deficit is estimated at USD 89.2 million, meanwhile the negative balance on the item “income” is expected at USD 60.4 million.

According to preliminary forecast estimates of the National Bank, in Q3 2021, capital inflow on the capital and financial account will amount to USD 305.8 million. The capital account surplus will make USD 39.5 million, whereas the positive balance on the financial account is expected at USD 266.4 million.

Chart 2.2.2. Capital and Financial Account



The main capital inflow will be provided on the item “other investments”, the balance thereof will be positive in the amount of USD 215.6 million due to allocation of the special drawing rights by the International Monetary Fund to support national economies during pandemic. Net inflow of direct investments is forecasted at USD 50.8 million, meanwhile a net outflow was observed in the same period of the last year.

Thus, at the end of Q3 2021, the balance of payments of the Kyrgyz Republic will be formed with a positive balance to make USD 357.4 million.

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

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

Indexes of Real and Nominal Effective Exchange Rate of KGS

Table 2.2.1. Key Values for Exchange Rate

	year (average)			month to the beginning of the year			
	2019 (aver.) (January- December)	2020 (aver.)* (January- December)	%	December 2020	June 2021	*	%
REER	115,7	115,7	0,0	112,8	115,3	2,2	↑
NEER	122,5	122,7	0,1	116,8	120,2	2,8	↑
RBER to CNY	84,5	79,2	-6,3	73,0	74,5	2,1	↑
NBER to CNY	67,1	60,8	-9,3	53,3	51,7	-3,0	↓
RBER to EUR	108,2	101,7	-6,0	93,5	96,7	3,4	↑
NBER to EUR	78,0	69,5	-10,9	60,2	60,9	1,2	↑
RBER to KZT	141,7	137,4	-3,0	132,7	132,1	-0,4	↓
NBER to KZT	171,0	166,7	-2,5	157,3	156,4	-0,6	↓
RBER to RUB	122,0	125,8	3,1	123,8	121,4	-1,9	↓
NBER to RUB	140,4	141,0	0,4	134,4	130,3	-3,0	↓
RBER to TRY	165,8	174,3	5,1	176,8	179,1	1,3	↑
NBER to TRY	247,6	275,3	11,2	284,0	305,4	7,5	↑
RBER to USD	87,6	83,1	-5,2	80,7	80,4	-0,4	↓
NBER to USD	65,8	59,6	-9,5	55,1	54,2	-1,6	↓

* Preliminary data

↓ – Som devaluation, competitiveness improvement

↑ – Som strengthening, competitiveness deterioration

yuan – by 3.0 percent.

A lower inflation rate in Kyrgyzstan² conditioned smaller increase in the real effective exchange rate (REER) index, which increased by 2.2 percent since December 2020 and constituted 115.3 at the end of September 2021.

By the end of Q3 2021, the index of nominal and real effective exchange rates increased compared to December 2020. According to the preliminary data, the index of the nominal effective exchange rate (NEER) of KGS increased by 2.8 percent year-to-date and constituted 120.2 at the end of September 2021.

The increase in the index was due to the strengthening¹ of KGS in September 2021 compared to the exchange rate in December 2020 against the Turkish lira by 7.5 percent and the euro by 1.2 percent amid depreciation against the Russian ruble by 3.0 percent, the US dollar – by 1.6 percent and the Chinese

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

² In Q3 2021, the inflation rate in the Kyrgyz Republic was formed at 6.6 percent, meanwhile, the average inflation rate in the main trading partner countries according to the preliminary calculations was 7.2 percent.

Chapter 3. Monetary Policy

3.1. Monetary Policy Implementation

During Q3 2021, the external commodity markets demonstrated ongoing ambiguous situation (due to unfavorable weather conditions in the producing food products countries) and, as a result, there was an increase in the world prices for certain types of food products. During the reporting quarter, these factors posed inflation risks in the economy of our country.

The course of monetary conditions tightening was continued in the context of ongoing inflationary pressures in the Kyrgyz Republic. The National Bank once again increased the key rate by 100 basis points, up to 7.50 percent, based on the inflation forecasts and its factors for the medium term.

Reflecting the current interest rate policy and passing response signals, the short-term rates in all segments of the money market demonstrated an upward trend and were close to the key rate.

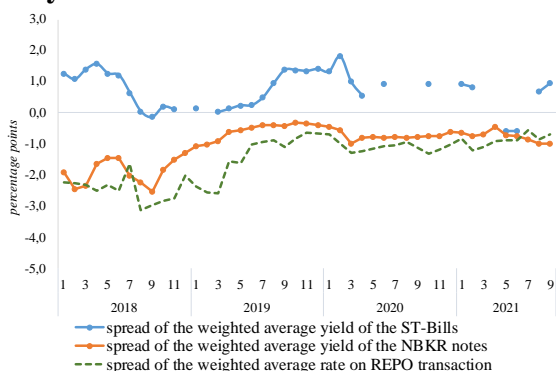
During Q3 2021, tactical decisions in the field of monetary policy were made amid a significant increase in excess liquidity of the banking system and prevalence of the short-term money in it.

The situation in the domestic foreign exchange market demonstrated ongoing stability. During the reporting quarter, the supply of foreign currency and demand for it were balanced, excluding the last ten days of September 2021. During this period, the National Bank conducted one foreign exchange intervention to sell foreign currency in order to smooth sharp fluctuations of the exchange rate.

Interest Rate Policy of the National Bank

Considering acceleration of inflationary processes in the economy of the Kyrgyz Republic and high expectations for the future dynamics of inflation, in July 2021 the National Bank once again increased the key rate from 6.50 to 7.50 percent. Besides change in the policy rate, the rates of the interest rate corridor were revised: the rate on “overnight” deposits was increased from 4.25 to 5.25 percent, the rate on “overnight” credits was increased from 7.00 to 8.00 percent.

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



Measures taken by the National Bank to improve the efficiency of the monetary policy transmission mechanism resulted in reduced volatility of the short-term interest rates in the money market and their formation near the key rate.

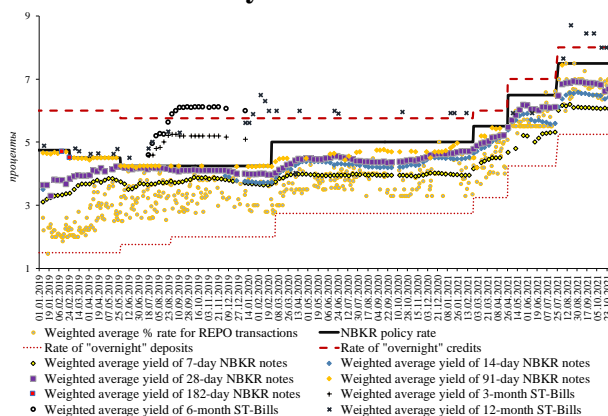
In Q3 2021, the gap between the short-term money market rates and the policy rate of the National Bank demonstrated slight expansion, excluding the rates on REPO transactions. Thus, the spread between the key rate and the rates of the interbank credit market decreased from (-)0.9 percentage points in Q2 down to (-)0.7 percentage points

in Q3 2021.

Meanwhile, the focus of the National Bank’s notes maturity structure on the shorter-term securities expanded the spread between the yield of the National Bank’s notes and the key rate. In the reporting quarter, the average value of the spread was (-)0.9 percentage points against (-)0.6 percentage points in the previous quarter.

In general, in the reporting quarter, the situation in the money market remained stable. The money market environment suffered the effect of the growth in the overall level of excess liquidity in the banking system and, as a result, the banks' increased demand for the National Bank's sterilization instruments. During Q3 2021, the volumes of transactions in the money market increased compared to the previous quarter.

Chart 3.1.2. Money Market Rates



The rates on the main financial instruments demonstrated an upward trend upon an increase in the main policy rates in all segments of the money market.

In addition, the short-term money market rates, excluding the yields on 12-month ST-Bills, were within the interest rate corridor set by the National Bank.

In the reporting quarter, the short-term segment (in this case, up to 28 days) of the money market was characterized by the highest demand from its participants. This segment of the money market was

represented by the market of the National Bank's notes and the interbank credit market (IBCM).

In the context of the excess liquidity accumulation in the banking system, the market of the National Bank's notes demonstrated significantly increased activity. During the reporting quarter, the average auction demand exceeded supply. The total sales of notes of all maturities increased by two times, in particular, the notes with a maturity of 7 days were in high demand among the banks (the volume of sales increased by 4.7 times). At the same time, the sales of 14- and 28-day notes also increased significantly by 1.7 and 1.5 times, respectively.

In Q3 2021, the note yields grew in response to further tightening of the monetary policy. The total weighted average yield of notes increased from 5.75 percent in June 2021 up to 6.51 percent in September 2021 (in the reporting period, the total yield varied within the range of 5.65-6.59 percent). In terms of maturities¹, the situation developed as follows: the rates on 7-day notes increased from 5.16 up to 6.10 percent, on 14-day notes - from 5.72 up to 6.54 percent, on 28-day notes - from 6.08 up to 6.89 percent and on 91 days - from 5.43 (in April 2021) up to 7.45 percent (in August 2021).

In Q3 2021, the participants' activity decreased in the interbank credit market due to a sufficient level of excess liquidity in the banking system. As in the previous periods, REPO transactions prevailed in the structure of transactions, in Q3, the volume thereof decreased by 60.2 percent compared to Q2. It is also important that during the reporting quarter there was a change in the maturity structure of loans, in particular, extending of the transactions average terms and a decrease in the share of loans with a maturity from 1 to 3 days (this short maturity increased sharply in Q2 2021 amid a decrease in the commercial banks' liquidity).

The longer segment of the money market (in this case, over 28 days up to 1 year) - the market for the short-term government securities was represented only by the state treasury bills (ST-Bills) with a maturity of 12 months. As in the previous periods, 12-month ST-Bills were not attractive and the segment of this market demonstrated weak activity. There was a significant increase in the yield of 12-month ST-Bills amid tightened monetary conditions compared to the previous quarter. Thus, in Q3 2021, the yield increased up to 8.32 percent from 5.92 percent in Q2 of the current year.

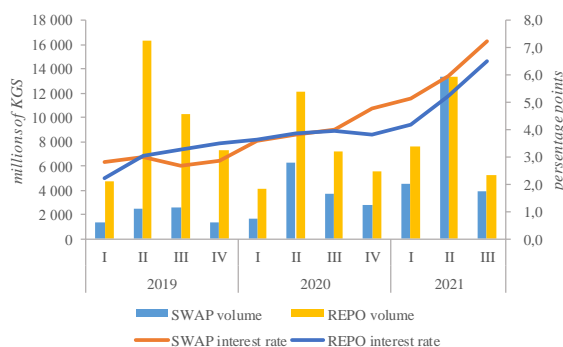
¹ The data on rates are given as of the end of June and September 2021, unless otherwise indicated.

In Q3 2021, the state treasury bonds (ST-Bonds) with the maturities of 2, 3, 7 and 10 years were offered to the participants in the long-term segment of the financial market (over 1 year). In the reporting quarter, the Ministry of Finance of the Kyrgyz Republic, reduced the supply of ST-Bonds by about 30 percent compared to the previous quarter due to budget surplus, however these securities did not generate interest among the market participants. Based on the results of the auctions, in the reporting quarter, the volume of demand for ST-Bonds decreased by more than 75 percent. Based on the results of the auctions held, primarily 2- and 3-year ST-Bonds were in demand. Following the money market rates, the profitability of ST-Bonds on all proposed maturities demonstrated growth compared to the previous quarter. In particular, 3-year securities demonstrated the largest increase in the yield of ST-Bonds (+1.25 percentage points compared to the previous quarter).

Market of REPO and SWAP transactions

The commercial banks actively used foreign exchange transactions on a swap basis (USD/KGS) as an alternative source of funds in the national currency. In the reporting quarter, the total volume of these transactions amounted to KGS 3.9 billion, while the market participants attracted approximately KGS 5.2 billion from the IBCM¹.

Chart 3.1.3. Market of REPO and SWAP transactions

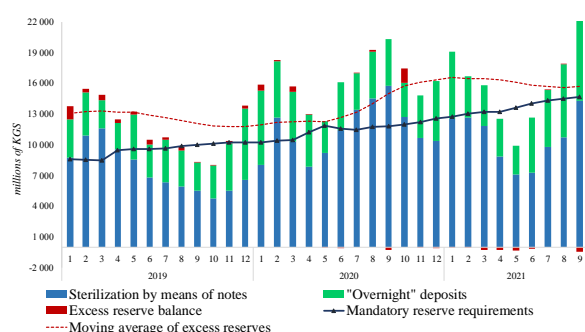


In recent years, the transactions in the domestic foreign exchange SWAP market remained rather short-term (up to 1 month), although in the pre-pandemic period the transactions were concluded for a longer term (up to 6 months). At the same time, the term of SWAP transactions is much longer compared to REPO transactions. Thus, in the reporting quarter, the weighted average term for the transactions in the SWAP market was 23 days, whereas the same indicator for the

IBCM was 5 days. It is worthy of note that the gap between the rates in the SWAP and REPO markets is insignificant (the rates varied from 5.00 to 7.00 percent) in the segment up to 7 days.

Liquidity Regulation in the Banking Sector

Chart 3.1.4. Excess Reserves of the Commercial Banks



After a short cycle of reduction during Q3 2021, excess liquidity in the banking system demonstrated a gradual increase and reached its maximum peak values.

During the quarter, the average level of excess liquidity of the banking system increased by KGS 7.1 billion. At the same time, as previously stated, in September, the level of excess liquidity reached its maximum values for the first time in the history of this indicator.

In general, during Q3 2021, the excess liquidity was formed in the banking system due to the inflow of resources through the monetary and the budgetary channels. At the same time, net input of the National Bank's

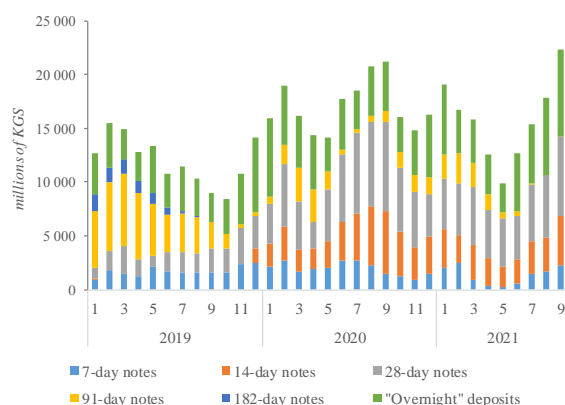
¹ Interbank credit market.

transactions to the growth of excess liquidity amounted to KGS 15.6 billion. Whereas, at the end of the quarter, the government sector transactions and the growth of money outside banks had a downward effect on the commercial banks' liquidity by KGS 3.5 billion and KGS 6.2 billion, respectively.

As before, in the reporting quarter, excess liquidity in the banking system remained at a rather high level. The average daily volume of excess liquidity, prior to the sterilization operations conducted by the National Bank, stood at KGS 18.4 billion, in the previous quarter this indicator amounted to KGS 11.3 billion.

In order to limit the monetary component of inflation, the National Bank actively conducted operations to absorb excess liquidity. Thus, in Q3 2021, as compared to the previous quarter, the average daily volume of sterilization operations conducted by the National Bank increased from KGS 11.7 billion up to KGS 18.5 billion.

Chart 3.1.5. Structure of Sterilization



The National Bank regulated the level of excess liquidity in the banking system, mainly through the operations on notes sale. In Q3, the average daily volume of notes in circulation gradually increased and amounted to KGS 11.6 billion after a decrease down to KGS 7.8 billion in Q2 2021.

At the same time, the share of the National Bank's notes in the structure of sterilization operations continued to decrease and constituted 62.6 percent, whereas in Q2, it stood at 66.4 percent, and in Q1 – 71.7 percent. This was due to reorientation of the banks' investment behavior from the

operations in the open market to surplus resources placement on "overnight" deposits with the National Bank.

Amid change in the maturity structure of excess liquidity with prevalence of available funds with shorter maturity, the total demand for 7-day notes increased by 5 times, while the commercial banks demonstrated moderate interest for 14- and 28-day notes (demand increased by 1.5 times). As a result, the share of 7-day notes in the total absorption volume increased significantly due to notes: from 4.8 percent (Q2 average) up to 15.7 percent (Q3 average). Whereas, the share of 14-day notes reached 30.7 percent (+2.2 percentage points), while the share of sterilization for 28- and 91-day notes decreased down to 52.8 ((-)4.2 percentage points) and 0.8 percent ((-)8.9 percentage points), respectively.

Besides the operations in the open market, the commercial banks dynamically placed their available funds on "overnight" deposits with the National Bank. The share of "overnight" deposits in the total absorption structure increased approximately from 33.6 percent in Q2 up to 37.4 percent in Q3. At the same time, in the reporting quarter, the average daily volume of sterilization due to "overnight" deposits increased by 1.8 times and amounted to KGS 6.9 billion (in Q2 – KGS 3.9 billion).

Credit Policy of the National Bank

In 2021, following the current monetary policy, the National Bank restricted operations to provide long-term liquidity in the national currency through refinancing instruments. This measure is conditioned by the current high level of excess liquidity in the banking system, which is among the factors of inflationary pressure.

During the III quarter of 2021, the commercial banks experienced temporary gaps in short-term liquidity in the national currency. In order to maintain short-term liquidity within the framework of the current window of permanent access, "overnight" loans were issued to the commercial banks, the gross volume thereof amounted to KGS 826.1 million.

Foreign Exchange Policy of the National Bank

Generally, during the reporting quarter, the situation in the foreign exchange market was stable. Meanwhile, at the end of Q3, demand for foreign currency exceeded slightly its supply in the domestic foreign exchange market.

Within the framework of the floating exchange rate regime, the National Bank participated in the foreign exchange auctions to prevent sharp fluctuations in the exchange rate. In the reporting quarter, the total volume of the National Bank's interventions on sale of foreign currency in the domestic foreign exchange market amounted to USD 33.1 million (in Q2 2021 – USD 112.5 million). In the reporting period, the National Bank did not conduct transactions on purchase of foreign currency, as in the previous quarter.

In Q3 2021, the USD/KGS exchange rate was fluctuating within the range KGS 84.2283 -84.8000 per USD to increase by 0.15 percent at the end of the reporting quarter. In the reporting quarter, the average exchange rate amounted to KGS 84.7254 per USD and practically did not change compared to the previous quarter (KGS 84.5404 per USD).

Monetary Policy Measures in Q3 2021

The decisions were made on the size of the National Bank policy rate and the rates of the interest rate corridor

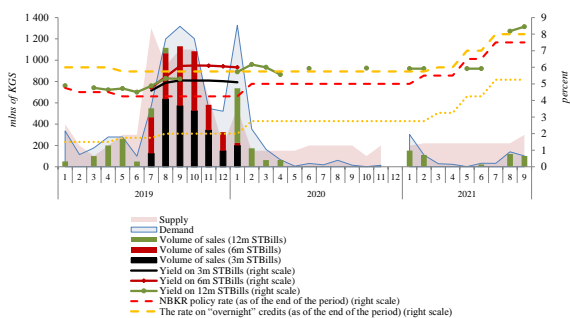
The Board of the National Bank twice considered the issue of the size of the policy rate – on July 26 and September 1, 2021. Based on the results of the meeting held in July, the decision was made to increase the policy rate by 100 basis points, up to 7.50 percent. Based on the results of the meeting held in September, the decision was made to keep the policy rate unchanged at 7.50 percent.

The policy rate change was followed by adjustments of the rates in the interest rate corridor: the rate on “overnight” deposits, being the lower rate, was increased up to 5.25 percent, the rate on “overnight” credits, determining the upper rate, was increased up to 8.00 percent.

3.2. Financial Market Instruments

Government Securities Market

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



ST-Bills

In Q3 2021, as before, the short-term segment of government securities was represented only by ST-Bills with a maturity of 12 months¹. Participants' activity slightly increased compared to Q2.

The increase in the participants' activity was characterized by an increase in the volumes of supply and demand at the ST-Bills auctions. The average number of participants per auction remained unchanged

at two. 6 out of 10 auctions were not conducted: 4 - due to insufficient number of participants, 2 - due to lack of demand.

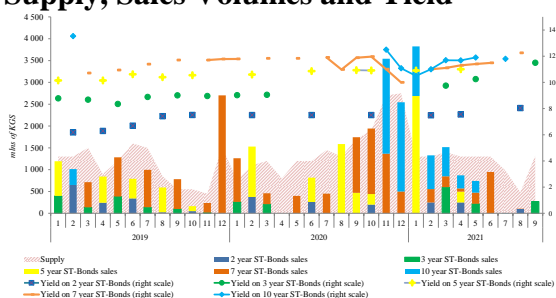
¹ The Ministry of Finance of the Kyrgyz Republic offered only 12-month ST-Bills since February 2020.

The supply of 12-month securities for the first time increased in September up to KGS 300.0 million from KGS 220.0 million being unchanged since February 2021. At the same time, in August, demand and sales indicators are the highest since January 2021 (in July-September, the average monthly demand increased by 4.8 times compared to April-June, supply – by 12.1 percent).

The total weighted average yield of ST-Bills increased by 2.40 percentage points: from 5.92 percentage points in Q2 up to 8.32 percentage points in August-September (in July, the auctions for the ST-Bills sale were declared invalid due to insufficient number of the participants). The yield increased due to low demand for ST-Bills from May to July, as well as due to accelerated inflation rate.

At the end of September, the structure of ST-Bills holders has changed significantly: the largest share is occupied by the commercial banks (47.6 against 23.3 percent at the end of June), the institutional investors come second (42.0 percent against 65.7 percent), the share of resident legal entities remained practically unchanged and constituted 10.4 percent.

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



ST-Bonds

In Q3 2021, the ST-Bonds market was represented by the securities of all types of maturities. The participants' activity decreased compared to the previous quarter amid increased uncertainty and existing risks in the economy. The ST-Bonds yield increased on all types of maturities of placed securities.

In July-September, the average monthly supply of ST-Bonds decreased by 28.7 percent compared to April-June, the volume of demand for these securities decreased by 75.7 percent.

The yield of ST-Bonds increased on all types of maturities. In Q3, the weighted average yield on 2-year securities constituted 8.04 percent (7.55 percent in Q2), on 3-year securities – 11.50 percent (10.25 percent in Q2), on 7-year securities – 12.25 percent (approximately 11.40 percent in Q2), 10-year securities – 11.80 percent (approximately 11.79 percent in Q2). In Q3, offered securities with a maturity of 5 years were not in demand.

In Q3, the participants' demand was focused on the securities with a shorter maturity due to ongoing economic uncertainty: the demand for 2-year ST-Bonds constituted 37.4 percent of the total demand, the demand for 3-year ST-Bonds constituted 60.6 percent, whereas in Q2, 7-year (47.0 percent of the total demand for ST-Bonds) and 10-year securities (19.8 percent of the total demand) were primarily in demand.

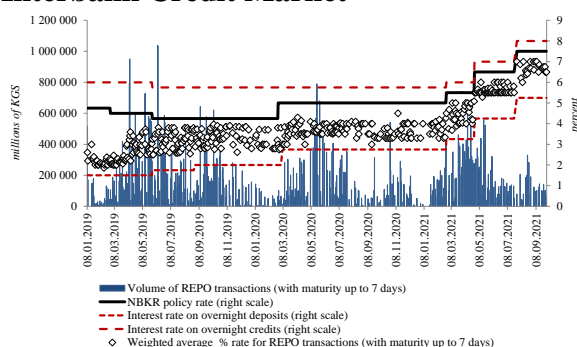
As for sales volumes by maturity, 2- and 3-year ST-Bonds were mainly sold (up to 14.6 and 83.4 percent of the total sales, respectively); on other types of maturities, sales decreased down to minimal volumes.

At the end of the reporting period, the volume of ST-Bonds¹ in circulation increased by 12.2 percent year-to-date, up to KGS 59.3 billion. The structure of ST-Bonds holders remained almost unchanged: the bulk of securities were held by the institutional investors (53.7 percent), the commercial banks (21.8 percent), non-resident legal entities (14.0 percent) and other holders (10.5 percent).

¹Excluding ST-Bonds nominated in foreign currency

Interbank Credit Market

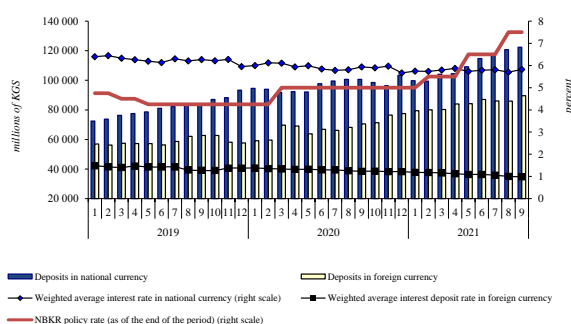
Chart 3.2.3. Dynamics of Rates and Volume of Repo Transactions in the Interbank Credit Market



In Q3 2021, the weighted average rate in the interbank market increased by 1.2 percentage points compared to the previous quarter and stood at 6.5 percent. The weighted average maturity of the interbank credits increased up to 5 days (in Q2 2021 – 3 days).

Deposit Market

Chart 3.2.4. Dynamics of Commercial Banks' Deposits



In Q3 2021, the depository base continued to grow steadily, thus reflecting ongoing confidence of the population in the banking system. Remarkably, in July-September of the current year, there was a significant increase in deposits in the legal entities' settlement accounts.

In the structure of deposits in the national currency, the growth in the legal entities' settlement accounts by 24.1 percent compared to Q2 2021 contributed to the total increase in deposits in the national currency by 80.3 percent.

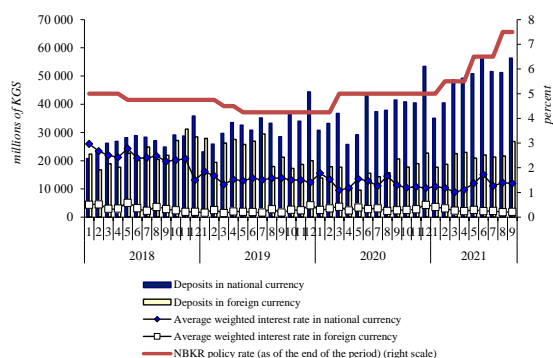
The legal entities' settlement accounts in foreign currency increased by 5.7 percent, up to 73.9 percent of the total increase in deposits in foreign currency in Q3 2021.

At the same time, the growth of individuals' deposits in the national currency and the increase of time deposits in the national currency reflected positive trends witnessing further development of the deposit market. Thus, individuals' deposits in the national currency increased by 2.0 percent, and time deposits in the national currency - by 3.1 percent compared to Q2 of the current year, these indicators increased by 8.9 and 14.0 percent, respectively, since the beginning of 2021.

Despite a slight strengthening of the US dollar year-to-date, in September 2021, dollarization of deposits decreased by 0.6 percentage points compared to December 2020 and constituted 42.3 percent.

There is situation when the share of settlement and demand accounts constitutes about two-thirds of all deposits, while the share of time deposits has decreased since the beginning of 2021. It suggests that the population's preference to time deposits for money holding has slightly weakened. At the end of September 2021, the total duration of the depository base was 4.9 months (-0.2 months year-to-date).

Chart 3.2.5. Dynamics of Commercial Banks' Deposits Flows

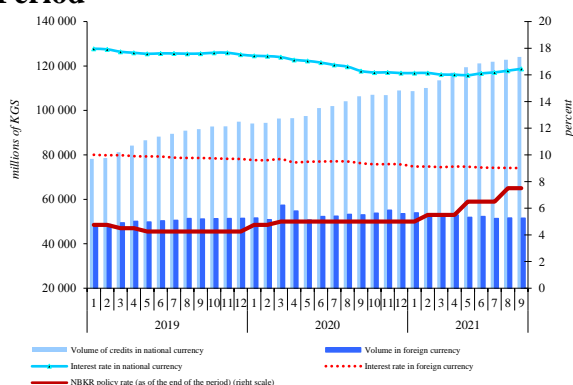


interest rate.

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

Credit Market

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



currency demonstrated ongoing decline, which began in March 2020 after a sharp rise in the US dollar exchange rate.

The dynamics of new credits showed similar trends. The volume of new credits in the national currency increased compared to the corresponding period of 2020 due to the credits extended for consumer credits and trade. The volume of new credits in foreign currency decreased compared to January-September 2020.

Therefore, dollarization of the credit portfolio decreased by 3.6 percentage points compared to December 2020 and in September reached 29.3 percent, demonstrating ongoing update of its historically low values.

The interest rates on time deposits in the national currency were growing year-to-date, reflecting increased competition among the banks to receive population's deposits amid tightening monetary policy and high inflation rate. At the end of September 2021, the interest rate on time deposits in the national currency (balances) increased by 0.7 percentage points compared to December 2020 and constituted 10.9 percent. Generally, the interest rate on the depository base was characterized by rather "sideways" trend due to increased share of deposits with a low

The commercial banks' credit portfolio continued to demonstrate stable growth.

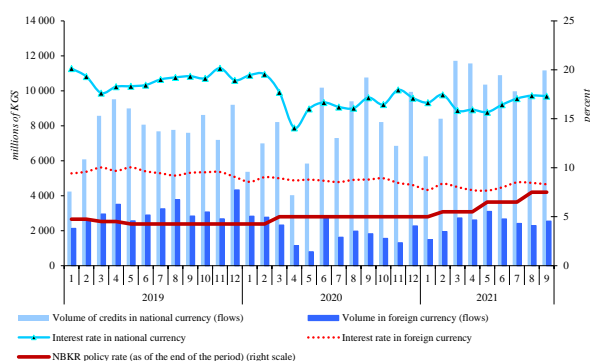
In July-September 2021, the credit portfolio grew due to the increase in the volume of credits issued in the national currency. The sectors of consumer credits, trade and mortgage demonstrated a significant increase in the volume of credits. At the same time, there was slowdown in the growth of the credit portfolio in the national currency in such production sectors as industry and agriculture.

The credit portfolio in foreign

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

In Q3 2021, duration for new credits in the national currency decreased by 3 months compared to the corresponding quarter of 2020 and amounted to 22 months, in foreign currency it remained practically unchanged and was at the level of 33 months.

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



The interest rates of the credit portfolio in the national currency have grown since May of the current year following the growth of the interest rates on time deposits. Moreover, the interest rates on credits increased due to many significant sectors, including agriculture, trade, construction, mortgages and consumer credits. The interest rates on deposits and the interest rates on credits both increased amid tightening monetary policy focused on inflationary processes control.

The credit market general concentration index was stable and formed at the level of 0.08, which corresponds to a low level of concentration and is equivalent to the division of the market among twelve banks. The sectoral concentration index was 0.33, which is equivalent to three main credit sectors.

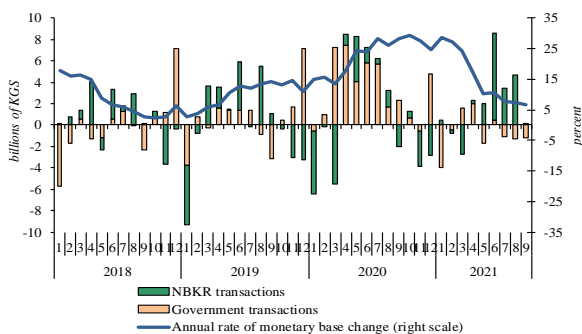
At the end of September 2021, the qualitative characteristics of the credit portfolio were as follows: the share of overdue loans in the credit portfolio increased by 0.3 percentage points year-to-date and amounted to 2.6 percent. The share of extended loans in relation to the credit portfolio is still at a high level; nevertheless, there is a downward trend from almost historically highest 15.9 percent in January down to 13.3 percent at the end of September (having decreased by 0.4 percentage points since December 2020), which reflects a decrease of the stability risks in the banking system.

3.3. Dynamics of Monetary Indicators

Monetary Base

The annual growth rates of the monetary base demonstrate gradual slowdown after accelerated growth in 2020. In the current year, an increase in the budget revenue has a restraining effect on the growth of reserve money, while in 2020, the budget channel was the main factor for their growth. At the end of Q3 2021, the annual growth in the monetary base decreased from 10.7 percent at the end of the previous quarter down to 6.6 percent in the reporting quarter.

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



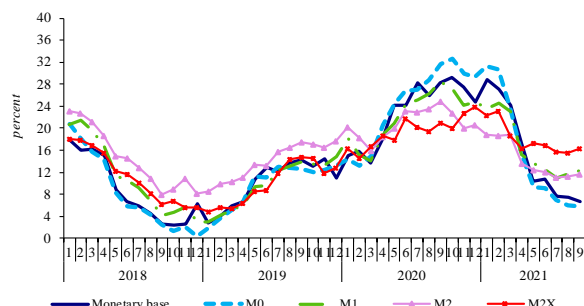
In the reporting quarter, the monetary base increased by 3.1 percent. The National Bank transactions in the amount of KGS 8.3 billion were the main factors that influenced the growth of reserve money during Q3.

At the same time, the government transactions reduced the monetary base by KGS 3.5 billion.

Monetary Aggregates

In Q3 2021, the annual growth rates of monetary aggregates demonstrated ongoing slowdown, whereas they were in the positive zone.

Chart 3.3.2. Nominal Growth Rates of Monetary Aggregates
(in annual terms)



The monetary aggregate M0 demonstrated a relatively more noticeable deceleration. The slowdown is almost insignificant for the aggregates that include deposits due to accelerated growth of the deposits in the national and foreign currencies.

In the reporting quarter, money outside banks (M0) increased by 5.8 percent, whereas the monetary aggregate M0 increased by 9.2 percent in annual terms in the previous quarter.

Deposits included in broad money supply increased by 24.8 percent in annual

terms due to the deposits in the national currency (+19.6 percent) and due to the deposits in foreign currency (+33.0 percent).

At the end of the quarter, the volume of money supply (the monetary aggregate M2X) increased by 16.2 percent in annual terms (at the end of Q2, the annual growth was 16.9 percent) and amounted to KGS 319.1 billion. During the reporting quarter, the money supply increased by KGS 15.4 billion.

Chapter 4. Inflation Dynamics

Steady rise in prices in the world food markets, an increase in tariffs and regulated prices (an increase of the public transportation fare in Bishkek and rise in electricity tariffs for some user groups), as well as price upsurge for petroleum, oil and lubricants due to the worldwide trend of an increase in prices for energy resources are the main factors for the current growth in consumer prices in the Kyrgyz Republic in 2021.

Additional inflationary pressure is conditioned by a decrease in agricultural production output in the current year.

These factors shape an increase of the households' and enterprises' inflationary expectations in the country to have an impact on price upsurge for non-food products and services.

4.1. Consumer Price Index

Chart 4.1.1. Dynamics of CPI Structure

(quarter to the corresponding quarter of the previous year)

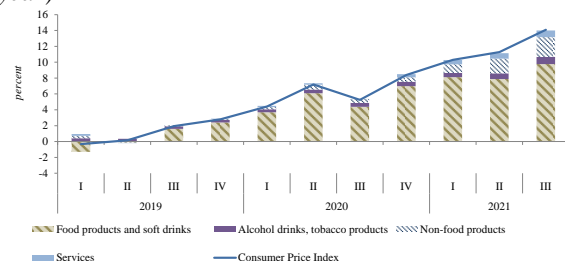


Chart 4.1.2. Dynamics of Food Prices' Contribution to Annual CPI

(month to the corresponding month of the previous year)

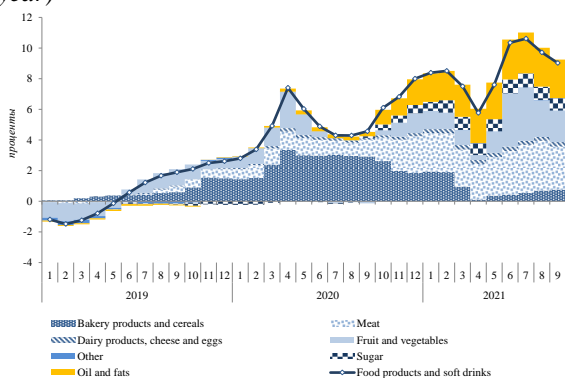
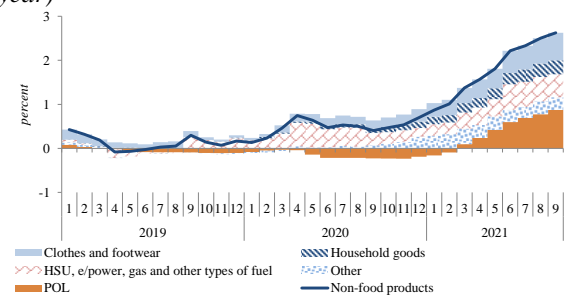


Chart 4.1.3. Dynamics of Non-Food Prices' Contribution to Annual CPI

(month to the corresponding month of the previous year)



In Q3 2021 (quarter to the corresponding quarter of the previous year), the annual inflation rate was **14.1 percent**. In the reporting period, external factors conditioned the main contribution to the CPI growth.

In Q3 of the current year, prices for food products increased by 21.5 percent compared to the corresponding quarter of the previous year. Considering the share of food products in the structure of the CPI basket - 45.6 percent, the contribution of an increase in food prices was crucial.

In Q3 2021, “meat”, “oils and fats”, as well as “fruit and vegetables” (8.3 percentage points) were the main driver that contributed to the growth of food inflation. The factors such as winter with little snow, slow sowing, an increase in the export of livestock and meat early in the year, dry summer in the region and, as a consequence, rise in prices for hay conditioned this trend.

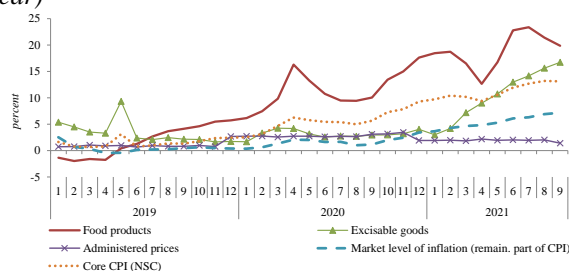
In the reporting quarter of 2021, non-food inflation increased by 8.6 percent compared to the same period of 2020. Price upsurge in the category “gasoline” by 64.8 percent, the commodity group “clothes and footwear” - by 5.5 percent, and “gas (natural and liquefied)” - by 9.6 percent made the largest contribution to an increase in prices for non-food products. Household items and household appliances rose in price by 7.7 percent.

Prices for petroleum, oil and lubricants continued to grow within the country from the beginning of 2021 amid an upward trend in the world oil prices, as well

as an increase in the wholesale selling prices at the Russian refineries.

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

(month to the corresponding month of the previous year)

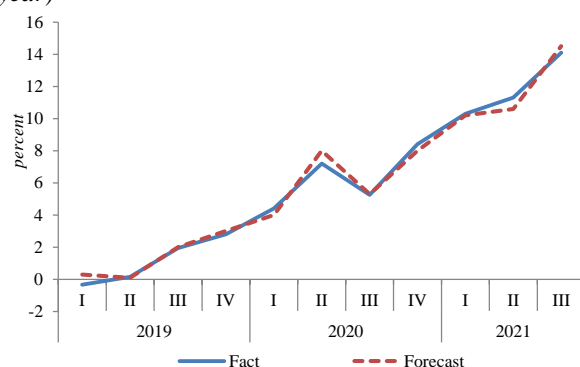


Republic, was 13.1 percent in annual terms.

4.2. Comparison of Forecast and Facts

Chart 4.2.1. Actual and Forecasted CPI Values

(quarter to the corresponding quarter of the previous year)



In the reporting quarter, the price index for alcoholic drinks and tobacco products increased by 10.4 percent amid planned increase in excise rates for tobacco products in early 2021.

Market inflation has been accelerating since the beginning of the current year, to reach 7.2 percent in September 2021. In Q3 2021, the core inflation indicator (excluding food and energy products), calculated by the National Statistical Committee of the Kyrgyz

In Q3 2021, the actual inflation rate decreased by 0.4 percentage points compared to the expectations of the National Bank.

Deviation of the expected inflation rate from the actual value was due to slightly inflated expectations amid accelerated growth in food prices.

4.3. Inflation Expectations

Inflation expectations are quantitative measurement of expected future price movement based on an analysis of the households' and enterprises' views in the Kyrgyz Republic. The household sector survey was launched in early 2015 and was conducted by SIAR research & consulting LLC. Starting from 2018, the National Statistical Committee of the Kyrgyz Republic joined the survey by expanding the sampling in the household sector and involvement of the enterprises in order to increase the respondents' coverage. Currently, the level of inflation expectations is assessed through quarterly survey of the households (5,000 respondents) and 250 enterprises - on a monthly basis.

Chart 4.3.1. Actual Inflation Value and Expected Inflation of Households

(percent)

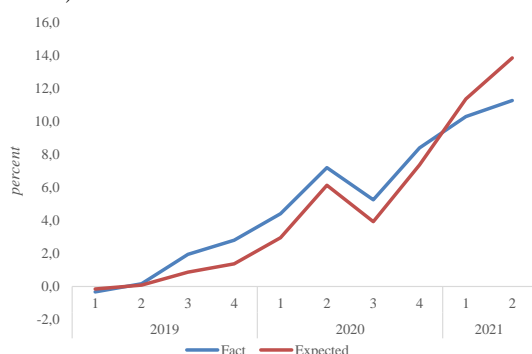
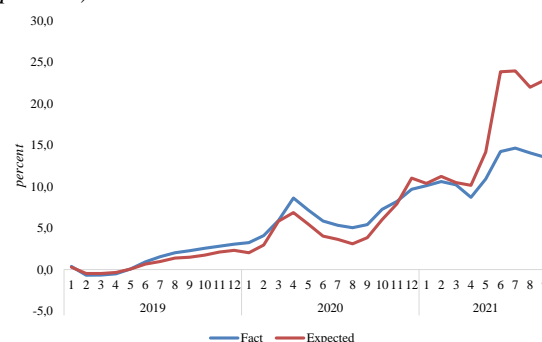


Chart 4.3.2. Actual Inflation Value and Expected Inflation of Enterprises

(percent)

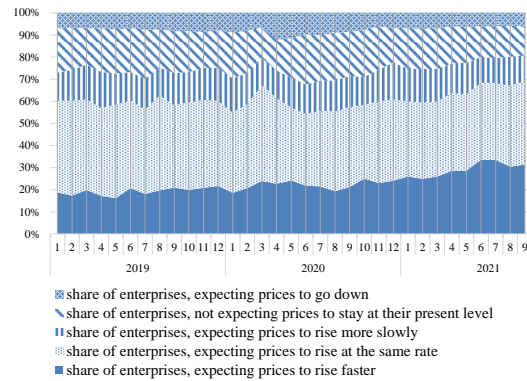


In the reporting period, there was an increase in inflation expectations. According to the survey conducted by the NSC KR, the price expectations of the enterprises and the households are at the maximum level. The enterprises' expectations were at 22.8 percent in September. The gap between the actual inflation rate and the enterprises' expectations has increased dramatically since June of the current year. In Q2 2021, the expected household inflation also increased compared to the actual inflation rate, to make 14.6 percent. The actual inflation rate was 11.3 percent in this quarter.

Chart 4.3.3. Distribution of Responses by Household Sector



Chart 4.3.4. Distribution of Enterprises Responses



The share of respondents in the household sector somehow expecting rise in prices constituted 75 percent at the end of Q2 2021. 30 percent of the respondents expected price upsurge, this indicator increased by three times compared to the beginning of 2019. At the beginning of 2019, the real sector expectations increased compared to the household sector. However, at the end of September 2021, the share of enterprises expecting an increase in prices constituted 81 percent, as well as the share of those expecting price upsurge amounted to 31 percent.

Chapter 5. Medium-Term Forecast

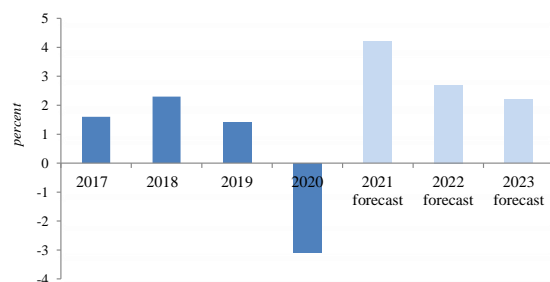
5.1. External Environment Proposals

5.1.1. Development Forecast of Main Trading Partners

Russia

Chart 5.1.1.1. Real GDP Growth in Russia

(year to year)



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

The Bank of Russia informed that slowdown of economic growth in Russia reflects completion of the recovery stage.

The Ministry of Economic Development of the Russian Federation improved the forecast for economic growth rates for 2021 from 3.8 to 4.2 percent. The forecast for GDP growth rates in 2022-2024 is expected at 3.0 percent, whereas the Ministry slightly decreased the forecast for 2022 from 3.2 to 3.0 percent. During the next year, multidirectional factors will affect the GDP growth rate: on the one hand, an increase in

oil production within the framework of the OPEC+ transaction will contribute to economic growth, on the other hand, monetary policy tightening will have a restraining effect.

Considering the current economic situation in Russia and worldwide, including the nature of supply restrictions, in October, the Bank of Russia kept unchanged its GDP growth forecast: in 2021 – 4.0-4.5 percent, in 2022-2024 – 2.0-3.0 percent.

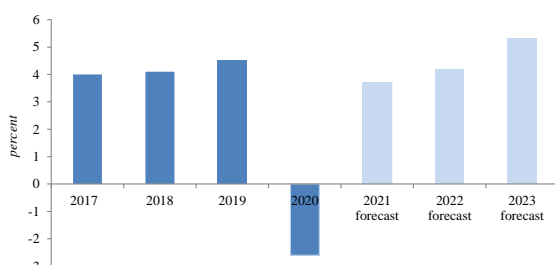
Amid heightened inflationary expectations and processes in general, the Bank of Russia significantly increased the inflation forecast for 2021 up to 7.4-7.9 percent compare to the forecast made in July (5.7-6.2 percent). In the context of the ongoing monetary policy, the annual inflation rate is expected to decrease down to 4.0-4.5 percent in 2022 and will remain close to 4.0 percent in the future.

At the same time, in October, the Ministry of Economic Development of the Russian Federation revised its inflation estimate for the current year. The Ministry expects the inflation rate at 7.4 percent at the end of 2021 (instead of 5.8 percent, according to previous forecasts).

Kazakhstan

Chart 5.1.1.2. Real GDP Growth in Kazakhstan

(year to year)



Source: IA Bloomberg, international financial institutions

The current economic forecasts in Kazakhstan for 2021 were revised mainly upward, however, inflation expectations worsened due to price upsurge in the world food markets and domestic demand recovery.

Amid continuing economic growth of Kazakhstan in January-September of the current year and compliance with the optimistic development scenario, the National Bank of the Republic of Kazakhstan expects GDP growth in 2021 at 3.7-4.0 percent with an average annual oil price of USD 70.0 per

barrel (in June 2021, GDP growth forecast was at 3.6-3.9 percent).

The European Bank for Reconstruction and Development assumes that economic growth of Kazakhstan at the end of the current year will be at 3.6 percent, in 2022 – 3.8 percent due to stronger external demand and fiscal stimulus measures still taken to support

domestic consumption, as well as higher prices for raw materials. However, there are risks of growth slowdown due to the COVID-19 pandemic, which can create obstacles for the trade and economic activity.

A number of the international organizations have improved their forecast for economic growth in Kazakhstan for the current and next years. Thus, the World Bank forecasts the GDP growth in the country in 2021 at 3.5 percent (in June, it was forecasted at 3.2 percent) and left it unchanged for 2022 at 3.7 percent.

According to the IMF forecast made in October in the report “World Economic Outlook”, the expectations for GDP growth in Kazakhstan for 2021 and 2022 were increased by 0.1 percentage points compared to the forecast made in April, up to 3.3 and 3.9 percent, respectively.

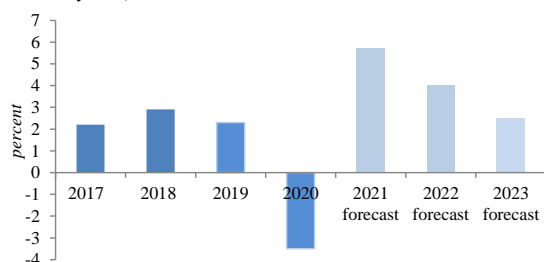
At the end of the current year, the fund forecasts that the average annual inflation rate will be at 7.5 percent, next year – 6.5 percent and it will be within the target range of 4.0 percent during subsequent years until 2026.

The National Bank of Kazakhstan expects the inflation rate in the current year to be at 7.5-8.5 percent (previously it was assumed at 6.0-7.0 percent), considering constant increase in prices in recent months and the degree of effectiveness of the Anti-inflationary response measures¹. Recently taken decision to increase the policy rate, as well as the government measures, will contribute to the inflation rate approaching the target of 4.0-6.0 percent in 2022.

USA

Chart 5.1.1.3. Real GDP Growth in the USA

(year to year)



Source: IA Bloomberg, international financial institutions

for 2022 and 2023 was increased by 0.5 and 0.1 percentage points, up to 3.8 and 2.5 percent, respectively, however, it was kept unchanged at the level of 1.8 percent for the long run. The US unemployment rate, according to new estimates of the US Federal Reserve System, will be at 4.8 percent in 2021, 3.8 percent – in 2022 and 3.5 percent – in 2023.

The IMF decreased the forecast for the US GDP growth in 2021 from 7.0 percent down to 6.0 percent, but improved the expected indicators for 2022 from 4.9 up to 5.2 percent.

The IMF expects the US unemployment rate in 2021 to be at 5.4 percent, and in 2022 – to decrease down to 3.5 percent.

Goldman Sachs investment bank decreased its forecasts for the US economic growth amid reduced budget support until the end of 2022 and a slow recovery in consumer expenditures due to longer impact of coronavirus infection (in 2021 – from 5.7 to 5.6 percent

In general, the forecasts of economic activity for the short-term remain generally positive, however there are increasing uncertainties about the spread of the new variant of the coronavirus to restrain economic growth. Thus, the majority of the international analysts decreased the indicators for US GDP growth during the current year.

In September 2021, the US Federal Reserve System decreased its forecast for the country’s GDP growth in the current year from 7.0 down to 5.9 percent. At the same time, the forecast of the US economic growth

¹ A set of anti-inflationary response measures was approved by the government by order of the President of the Republic of Kazakhstan to improve non-monetary inflation factors. The government assumes that prompt measures will contribute to a decrease of the food inflation rate down to 8.0 percent by the end of the current year.

and in 2022 – from 4.4 to 4.0 percent). The bank said that the coronavirus impact will be longer and that expenditures for certain services and non-durable goods will remain below pre-pandemic levels.

The US Federal Reserve System supported its base interest rate at 0.00-0.25 percent and considers it appropriate to maintain this range until the conditions in the labor market reach the levels corresponding to the maximum employment estimates, however, the inflation growth is targeted at 2.0 percent.

The FRS increased its inflation forecast for 2021 from 3.4 up to 4.2 percent, for 2022 - from 2.1 up to 2.2 percent. In 2023 and 2024, the inflation rate is expected at 2.2 and 2.1 percent, respectively.

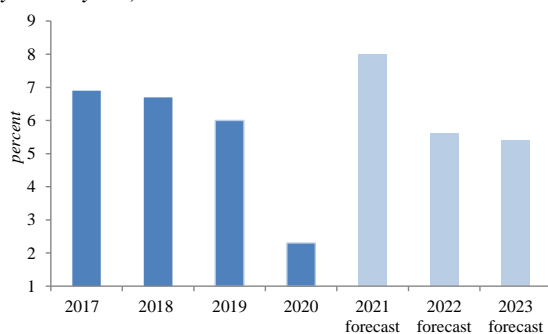
In addition, the US Federal Reserve System announced about initiated reduction of the assets purchase program by USD 15.0 billion per month since November 2021.

The OECD forecast for the US GDP growth rate in 2021 was also decreased from 6.9 down to 6.0 percent, the forecast for 2022 was increased from 3.6 up to 3.9 percent.

The international rating agency Fitch revised downward the forecast for the US GDP growth rate in 2021 from 6.8 down to 6.2 percent.

China

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



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

In 2021, the economists cut their forecasts for economic development in China down to 8.0 percent amid power shortage and deteriorating real estate market.

The official forecast of the Chinese government for GDP growth in the country in 2021 is more than 6.0 percent, a monthly survey of the experts conducted by the Bloomberg agency showed expectations for the country's economic growth at 8.1 percent, in October, the IMF decreased its forecasts down to 8.0 percent, Goldman Sachs'

expectations for economic growth were at 7.2 percent. The September forecast of the international rating agency Standard and Poors' was 8.0 percent. At the same time, the risks of further economic recession exist amid China's energy problems, which affected almost half of the Chinese industry.

According to the country's economic development plan for 2021, approved by the National People's Congress of China, the country's government set an inflation target for 2021 at 3.0 percent.

According to the IMF forecasts, the inflation rate in China will slow down in 2021 down to 1.1 from 2.4 percent in 2020, in 2022 it will accelerate up to 1.8 percent, in 2023 – up to 1.9 percent.

Bloomberg analysts expect prices to rise by 1.0 percent in 2021, 2.2 percent – in 2022, and 2.3 percent – in 2023.

5.2. Medium-Term Forecast

Economic transparency in the Kyrgyz Republic determines the importance of the world geopolitical and socio-economic trends for expanding the internal potential and accelerating the overall economic development of the country. Therefore, a medium-term forecast is made scrupulously considering the shocks and preconditions of the current period, based, inter alia, on the experts' assessments and the forecasts of the world research agencies and institutions. The uncertainties of the external and internal conditions is taken into account by the National Bank of the Kyrgyz Republic when developing monetary policy through modeling and analysis of various scenarios.

In Q3 2021, the economy of the Kyrgyz Republic demonstrated slow growth for the first time after significant recession in Q2 2020, witnessing a gradual recovery in economic activity. Shortage of irrigation water, an increase in prices for petroleum, oil and lubricants and smaller forage reserves for the period to come still pose risks of a significant decrease in growth in the agricultural sector. Planned decline in gold production at the Kumtor Mine is expected in the current year. The listed factors will have a restraining effect on the economic recovery to the pre-crisis level.

In the coming years, energy prices are expected to become stable within the range of USD 70-75 per barrel. Recovery in global demand and the OPEC + decisions are among the main factors for a steady rise in oil prices. The international food markets demonstrated an increase in prices for basic crops to be observed at the beginning of the next year amid unfavorable weather conditions and reduction in yields. Large-scale fiscal support and an increase in money supply in developed economies (USA, EU) is expected to put additional inflationary pressure in the world commodity markets.

Ongoing stable economic recovery is forecasted in Russia and Kazakhstan in the medium term, to have a positive effect on the net inflow of labor migrants' remittances and revival of external and internal demand for domestic goods and services.

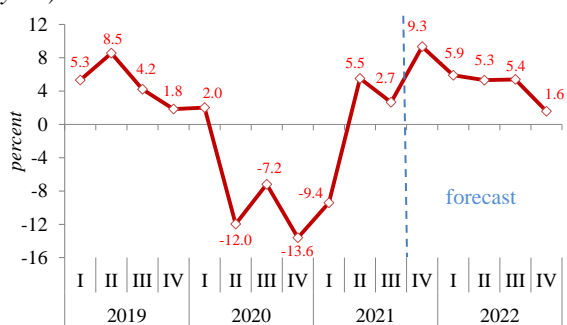
At the same time, export, excluding gold, and import are assumed to increase in the current year amid revival in external demand, as well as due to price upsurge.

In general, the experts assume that the negative production output gap will decrease in the forecast period, the potential GDP growth rate will be observed only by the end of 2022. The economic recovery will require some time and reforms on the part of the government of the country. Considering all conditions and risks, the forecast for GDP growth was decreased compared to the previous monetary policy report.

Savings accumulated during the pandemic period stimulate consumer demand, which together with a gradual economic recovery pose additional inflationary risks. Under such conditions, the actual inflation rate significantly exceeds the equilibrium level. Increased inflationary expectations of the economic agents put additional pressure. Moreover, such expectations extend the period for prices to reach the level of the medium-term target of 5-7 percent.

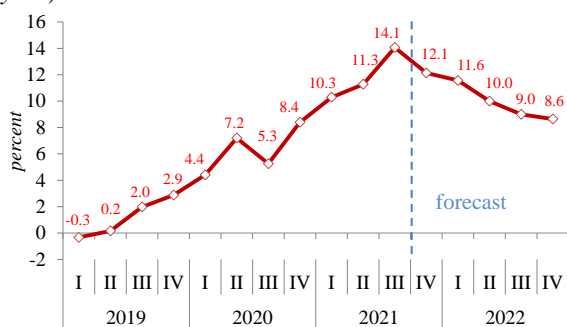
Considering the current trends in economic development of the trading partners, as well as price movement in the world commodity markets, the following forecast of the key macroeconomic indicators of the Kyrgyz Republic development for 2021-2022 was developed in the medium term.

Chart 5.2.1. Forecast of Real GDP
(quarter to the corresponding quarter of the previous year)



2.9 percent (-0.1 percentage point compared to the previous forecast). At the same time, relatively moderate growth rates are expected in 2022 (the forecast was reduced from 5.7 to 4.2 percent) amid slowdown in economic recovery in 2021. In 2021, the economic growth in Kyrgyzstan, excluding the Kumtor gold-mining enterprises, is expected to decrease by 0.2 percentage points compared to the previous forecast, to make approximately 4.7 percent.

Chart 5.2.2. Inflation Forecast
(quarter to the corresponding quarter of the previous year)



12.0 percent. In 2022, the average annual inflation rate is forecasted at 9.0-10.0 percent and by the end of the year it is expected to be within single-digit rates. The forecast for 2022 is based on the assumptions about an increase in excise taxes imposed on tobacco products, alcoholic drinks and utility tariffs.

Forecast for the Balance of Payments in 2021-2022¹

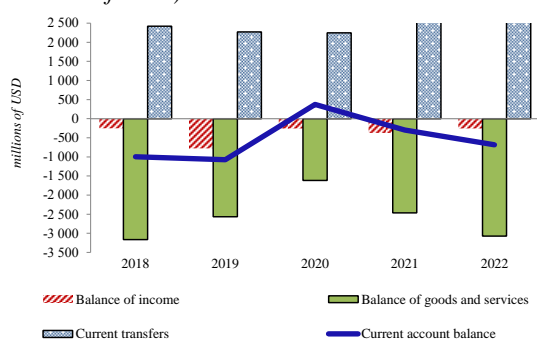
In the reporting period, the forecast of the balance of payments indicators was revised considering the data of the actual period and the revised initial conditions for development of the trading partners and Kyrgyzstan. In general, there are assumptions about uneven economic recovery amid uncertainty related to pandemic consequences and sustainable global economic growth. Assumptions that the economic growth of Kyrgyzstan will be slower compared to the main partners remain.

The current account deficit will decrease compared to the previous expectations, to make 3.7 percent of GDP. The current forecast takes into account the actual period trends. These trends determine the estimates for the forecast of the trade balance of goods and the foreign investors' income.

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

Chart 5.2.3. Forecast Data on Current Account

(millions of USD)



Slow recovery of supplies amid world price upsurge continues to affect foreign trade indicators.

The volumes of forecasted export for 2021, considering the data of the actual period, will increase compared to the level of 2020. The supplies of goods from the textile and apparel production sectors, as well as re-export positions, will provide significant support to the country's export amid increasing external demand in the region.

The import forecast for 2021 did not suffer significant changes and was adjusted

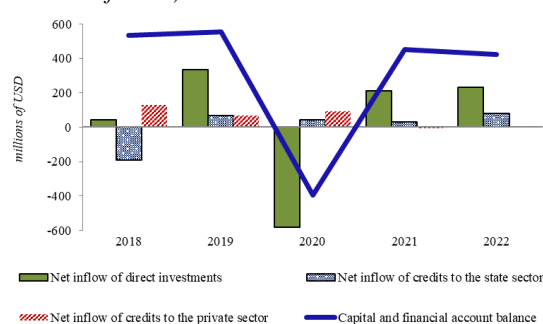
considering the data of the actual period. The value of import will increase by 39.6 percent amid low base of 2020 and price upsurge in the world commodity markets. An increase in import is expected mainly due to the consumer goods and the intermediate goods. An increase in the supplies of energy products to the country is forecasted at 49.1 percent, whereas the import of other goods is estimated to increase by 38.0 percent.

The positive dynamics of private transfer inflow will be observed until the end of the year. An increase in the net inflow of transfers to the private sector is expected at 15.5 percent, whereas the official transfers will decrease compared to the level of 2020.

Slow vaccination procedures and current border crossing restrictions create obstacles for the full recovery of the tourism sector in the country. In turn, transport services will be formed under the influence of the recovery in passenger and cargo transportation and increased prices for this type of services.

Chart 5.2.4. Forecast Data on Capital and Financial Account

(millions of USD)



The financial and capital account still suffers the negative influence of the pandemic consequences, and therefore, there are assumptions of lower financial capital inflows.

Net direct investment inflow is forecasted to grow gradually. As before, the main volume of capital inflows on the financial account will be provided by other investments. The balance of the item "other investments" will be primarily formed under the influence of the IMF allocated funds focused on supporting national economies.

Servicing of previously obtained private sector loans will remain significant with a moderate inflow of private foreign investment.

The revised forecasts of the balance of payments indicators in 2021 affected the dynamics of the balance of payments indicators expected in 2022.

Moreover, the assumptions about economic development in the region were clarified according to the current trends in economic development worldwide and accelerated inflation amid slow activation of distribution chains. The current account deficit is expected to continue expanding in 2022 and constitute 7.7 percent to GDP. Growing trade balance deficit, positive dynamics in the inflow of private transfers and gradual recovery of some types of international services will influence this indicator.

The prospect of economic growth will contribute to an increase of the trade turnover in the country. Export, excluding gold, is forecasted to increase by 7.4 percent due to traditional export positions amid expected growth in external demand.

Economic growth in the country and rise in the world prices will affect an increase in imports being forecasted at 4.4 percent. Thus, the trade balance deficit will increase by 29.4 percent. The positive dynamics of current transfers due to the labor migrants' remittances is forecasted to increase by 5.5 percent compared to the level of 2021.

In 2022, there is the risk of insufficient inflow of foreign capital on the capital and financial account. Direct foreign investments and other investments in the private sector are expected to provide a significant share of the capital inflows. Public sector liabilities will increase. The upward trend in servicing previously received loans and borrowings will remain stable.

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

- uncertainty due to the COVID-19 pandemic in the world and the political situation in the country;
- the risks associated with the Kumtor Mine development and other precious metal deposits;
- volatility in the world prices for oil and gold;
- deterioration of the economic situation in the countries-trading partners;
- volatility in the exchange rate of the main trading partner countries;
- growing debt burden of the public and private sectors.

Annex 1. Key Macroeconomic Indicators

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

Indicator	Unit of measure	2020				2021		
		Q1	Q2	Q3	Q4	Q1	Q2	Q3
1. Demand and supply¹ (real growth rates, if otherwise is not indicated)								
Nominal GDP, per quarter	mln. KGS	117 073,2	124 716,3	173 357,9	183 197,1	118 362,0	152 382,0	214 929,2
GDP	%	2,0	-12,0	-7,2	-13,6	-9,4	5,5	2,7
GDP, excluding Kumtor	%	1,4	-14,3	-7,6	-12,3	-4,5	11,6	3,5
Domestic consumption	%	3,7	-24,0	-12,1	-2,3	-1,6	24,0	
Investment	%	-23,7	-33,1	-16,9	-22,5	-17,6	103,1	
Net export	%	-16,3	-74,0	-26,8	1,2	19,6	377,8	
<i>GDP production:</i>								
Agriculture	%	1,3	0,8	1,0	1,4	0,9	1,5	-8,6
Industry	%	3,8	-3,2	-8,8	-18,9	-17,9	-5,6	6,4
Construction	%	-2,5	-12,7	-5,7	-25,6	-19,8	-10,3	0,1
Services	%	1,7	-17,9	-10,8	-10,6	-5,5	14,5	7,8
including trade	%	3,4	-31,2	-16,0	-15,4	-12,1	35,9	12,0
2. Prices²								
CPI	%	104,4	107,2	105,3	108,4	110,3	111,3	114,1
CPI, in annual terms as of the end of period	%	105,9	105,8	105,4	109,7	110,2	114,2	113,5
Core inflation	%	103,5	105,8	105,3	108,1	110,1	110,6	113,0
<i>CPI by main groups of goods and services:</i>								
Food products	%	108,1	113,4	109,7	115,4	117,9	117,3	121,5
Non-food products	%	100,9	102,1	101,6	102,0	103,7	106,4	108,6
Alcohol drinks and tobacco products	%	104,2	105,3	105,7	106,3	106,0	108,3	110,4
Services	%	101,0	101,0	100,0	102,3	103,3	104,1	105,0
<i>CPI, classified by character:</i>								
Excisable goods	%	103,1	103,3	102,8	103,4	102,1	102,3	115,5
Regulated prices	%	102,7	102,7	102,8	102,8	102,7	102,7	101,8
Market inflation rate (the rest of CPI)	%	100,8	101,9	101,3	102,6	101,0	102,2	106,8
3. External sector³ (in percent to GDP)								
Trade balance	% to GDP	-27,6	-22,2	-18,3	-18,7	-19,9	-19,0	-22,9
Current transaction account	% to GDP	-9,0	-4,0	0,4	4,9	4,0	6,0	1,4
Export of goods and services	% to GDP	34,7	34,2	33,4	31,8	31,2	40,6	39,9
Import of goods and services	% to GDP	61,5	56,2	53,0	52,8	53,9	62,2	65,6
4. USD exchange rate, as of the end of period								
	KGS	80,8100	75,9887	79,6000	82,6498	84,7792	84,6640	
5. Monetary sector								
NBKR policy rate, as of the end of period	%	5,00	5,00	5,00	5,00	5,50	6,50	7,50
Rate of "overnight" deposit, as of the end of period	%	2,75	2,75	2,75	2,75	3,25	4,25	5,25
Rate of "overnight" credit, as of the end of period	%	5,75	5,75	5,75	5,75	6,00	7,00	8,00
Average interest rates of operations in the interbank credit market, per quarter	%	3,55	3,85	3,79	3,79	4,15	5,30	6,50
<i>of which:</i>								
of REPO transactions	%	3,55	3,85	3,97	3,84	4,15	5,30	6,50
of credits in national currency	%	-	-	-	-	-	-	-
of credits in foreign currency	%	-	-	2,50	2,50	-	-	7,00
Weighted average yield of 7-day notes, as of the end of period	%	3,97	3,95	3,95	4,01	4,50	5,26	6,08
Weighted average yield of 14-day notes, as of the end of period	%	4,15	4,32	4,20	4,50	5,03	5,64	6,50
Weighted average yield of 28-day notes, as of the end of period	%	4,31	4,52	4,37	4,62	5,15	6,12	6,87
Weighted average yield of 91-day notes, as of the end of period	%	4,48	4,65	4,70	4,70	5,45	5,43	7,45
Weighted average yield of 182-day notes, as of the end of period	%	-	-	-	-	-	-	-
Monetary base	%	13,6	24,1	28,3	24,8	24,2	10,7	6,6
Money outside banks (M0)	%	14,9	26,9	31,7	29,3	23,7	9,2	5,8
Monetary aggregate (M1)	%	14,0	24,4	28,4	24,7	22,9	12,4	12,3
Narrow money supply (M2)	%	15,9	23,1	24,9	20,5	18,9	12,0	11,7
Money supply (M2X)	%	16,7	21,7	21,0	23,9	18,6	16,9	16,2

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

² Source: National Statistics Committee of the Kyrgyz Republic

³ Coefficients were calculated on the basis of the sliding annual data for the last 4 quarters. Data for Q3 are preliminary

Annex 2. Glossary

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

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

Annex 3. Abbreviations

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