

Launch of the IMF's October 2022 Regional Economic Outlook for the Caucasus and Central Asia

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Press Remarks by

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Welcome to the launch of our Regional Economic Outlook for the Caucasus and Central Asia. I am delighted to be in Samarkand to exchange views about the region's economic prospects and policy priorities.

Let me begin with a snapshot of where the region stands.

The adverse impact of the war in Ukraine on the CCA has been so far milder than expected, with some unforeseen positive spillovers, including an unprecedented surge in financial inflows and the relocation of workers and firms from Russia to several CCA countries, which have supported domestic activity.

Relative to our April projections, growth has been upgraded by 1.2 percentage points to 3.8 percent in 2022, still down from the strong 5.6 percent growth seen in 2021. In addition to the unexpected inflows this upgrade also reflects the upward revision to Russia's real GDP growth forecast, resilient trade, and fiscal stimulus in some countries.

As headwinds from the war in Ukraine and the global slowdown take hold, we expect growth to decelerate to 3.5 percent over the medium term, roughly half of the CCA's average growth rate of almost 7 percent from 2000 to 2018.

As in much of the rest of the world, inflation has continued rising in many CCA countries in 2022 and has become broad-based, despite the increase in policy rates by several central banks in the region. Headline inflation for the region is projected at 12.9 percent on average in 2022 and is expected to remain elevated at 10.5 percent in 2023.

I'd now like to briefly discuss global economic challenges and the risks facing CCA countries.

The global economy is facing extraordinary challenges. CCA countries have not yet felt the full impact of this. The region is facing exceptional uncertainties and downside risks that may be exacerbated by the region's strong ties to Russia.

These risks include scenarios whereby persistently high commodity prices and pervasive food shortages increase food insecurity, fiscal pressures, and social unrest. Tighter-than-expected financial conditions could translate into higher government debt service costs and worsening debt dynamics, further eroding fiscal space. Broadening inflation is also a concern, as it may require tighter disinflationary policies, which have the potential to be more costly than expected. And spillovers from the war in Ukraine could put the CCA's progress toward reducing poverty and inequality at risk, with

poorer households being most at risk from rising food prices and a potential decline in remittances from Russia in the years ahead.

Policy tradeoffs have become increasingly complex. Mitigating the cost-of-living crisis while preserving fiscal sustainability is the most pressing policy priority for all countries in the region.

This entails

- (1) *Restoring price stability* by raising policy rates where inflation is becoming broad-based or where there are signs of de-anchoring inflation expectations;
- (2) *Tackling food insecurity* through decisive efforts to scale up next season's agricultural production by securing access to fertilizers, rebuilding food reserves, and investing in climate-resilient agriculture; and
- (3) *Protecting the vulnerable* while ensuring fiscal sustainability. Having an overall tighter fiscal stance, with support targeted to the most vulnerable, will contribute to disinflation while supporting social cohesion. *Temporary* food subsidies may be used when targeted assistance is not feasible and food insecurity looms large. However, countries should avoid regressive energy subsidies and tax exemptions. Accelerating fiscal adjustment in countries with limited fiscal space will be critical to preserving debt sustainability.

These developments raise the urgency of pressing ahead with structural reforms to bolster growth while transforming economies to become more

resilient, sustainable, and inclusive. These include reforms to strengthen governance and the business environment, reduce the state's footprint, diversify trade, enhance social safety nets, and increase investment in climate-resilient technology and infrastructure.

Our REO takes an in-depth look at a critical issue facing the CCA region: the potential distributional impacts of Russia's war in Ukraine on the CCA.

Continued inflationary pressures and risks of reduced remittances in the war's aftermath have the potential to reverse some of the past gains in reducing poverty and inequality in the CCA. The report finds that the war risks raising poverty by about 1 percentage point and inequality by 1 percent and reducing real household consumption by 2 percentage points, on average. This implies that close to one million people could fall into poverty in the region. Moreover, it is the poorest countries in the region that are expected to bear the brunt of the impact on poverty, which could increase by about twice the regional average. Looking ahead, mitigating the war's potential impact on the vulnerable will be a key priority for policymakers and will require strong investments in enhancing the coverage and the impact of social safety nets.

Let me conclude by underscoring that the IMF's commitment to working with the region is unwavering. We continue to support our member countries through our lending arrangements (most recently through new financing to Georgia and a staff-level agreement with Armenia), tailored policy advice, and technical assistance. The IMF has remained nimble in

addressing members' evolving needs by establishing the Resilience and Sustainability Trust, which will support low-income and vulnerable middle-income countries to build resilience to external shocks and address longer-term challenges, including climate change. To help address the food crisis facing our most vulnerable members, the IMF has established a new food shock window under its emergency financing facilities.

We look forward to our continued strong engagement in the years ahead with countries throughout the region. I'll now open the floor to your questions.