

Turkmenistan

According to official statistics, the economy continued to grow rapidly in 2005, but actual growth was likely much lower than the official estimate. Government has overstated growth in the past. The medium-term outlook is heavily dependent on export prices of a small number of energy and agricultural products, which dominate exports and, for energy, heavily influence state revenues. To diversify exports and achieve more broad-based and sustainable economic growth, Turkmenistan needs to implement market-oriented reforms, improve governance, and reverse recent negative trends in human capital formation.

Economic performance

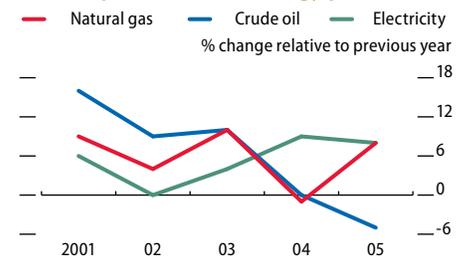
Official statistics suggest that the economy maintained very strong growth momentum in 2005, with aggregate gross output (AGO) growing by 20.7%. As in the previous several years, all sectors recorded double-digit growth rates, with industrial gross output growing by 19.6% and agricultural gross output by 19.8%. It was the fifth year in a row in which AGO reportedly grew by 20% or more.

However, official statistics should be treated with caution, as they tend to overestimate economic growth for at least three reasons. First, the Government uses AGO, rather than gross domestic product (GDP), to measure aggregate output growth. AGO generally gives higher growth rates than GDP in countries where growth is largely driven by material production, like Turkmenistan. In 2003, for example, the official growth rate of AGO (23.1%) was 5 percentage points higher than the official growth rate of GDP (18.1%). Second, official output statistics remain based on reports by enterprises. While private companies generally underreport output growth to evade taxes, state-owned enterprises—which account for the bulk of the economy’s total output—have a strong incentive to exaggerate output because the performance of their managers is evaluated primarily on their meeting government-set production targets. Third, some industries that appear to be expanding when measured in distorted domestic prices may in fact be producing negative value added at international prices.

In addition, the officially reported high growth rate of AGO in 2005 appears inconsistent with official statistics on physical output of energy products, cotton, and wheat, which account for a large proportion of AGO. As indicated in Figures 2.6.1 and 2.6.2, output of these products expanded moderately (or even contracted) in 2005. While necessarily based on incomplete data, the *Asian Development Outlook* estimate for 2005 GDP is 10.0%, a rate that is broadly in accord with the current International Monetary Fund estimate.

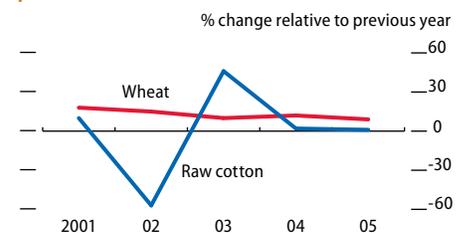
While the official exchange rate of the national currency, the manat, vis-à-vis the dollar remained fixed at TMM5,200/\$1, the black market rate stabilized at around TMM24,000/\$1 in 2005, after substantial fluctuations in 2003 and 2004 (Figure 2.6.3). Official data on inflation in 2005 are not

2.6.1 Output of selected energy products



Sources: Government of Turkmenistan; staff estimates.

2.6.2 Output of selected agricultural products



Sources: Government of Turkmenistan; staff estimates.

yet available, but the relative stability of the dollar black market exchange rate suggests that inflation was most likely kept to single digits.

Preliminary data indicate that the average nominal wage in manats continued to grow slowly in 2005 (Figure 2.6.4) and, while the average nominal wage in dollars started to rise again after declining in 2004, real wage developments are impossible to assess given the lack of data on prices.

As in the previous 4 years, the 2005 state budget was reported as roughly in balance. However, the overall fiscal position of the Government is difficult to assess because a considerable part of state revenue and expenditure is channeled through extrabudgetary funds and off-budget accounts of budgetary organizations, for which few data are available.

The merchandise trade surplus widened to \$1.3 billion (Figure 2.6.5). Although both exports and imports expanded considerably, exports grew much faster due largely to greater export volumes and higher export prices of natural gas. The current account and the overall balance of payments most likely remained in surplus, with gross official international reserves exceeding an estimated \$3.6 billion, equivalent to 10 months of merchandise imports.

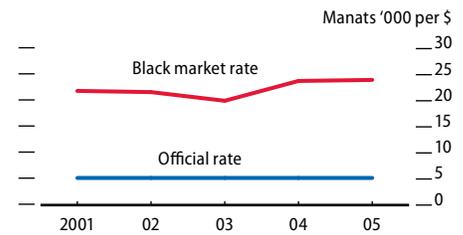
Little progress was made in economic reform. The Government maintains a policy management system akin to central planning. It continues to rely on production targets, mandatory state procurement, directed bank credits, and foreign exchange restrictions. Key sectors of the economy, including the oil and gas sector and the banking system, remain in state hands. As the public enterprise sector continues to operate under soft budget constraints, the Government relies on price controls and restrictions on cash withdrawals from banks to contain open inflation in the consumer goods market.

A central element of the social protection system remains provision to the entire population of basic consumer goods and utilities free of charge or at subsidized rates. While this enables the population to meet the minimum subsistence level and alleviates income poverty, nonincome poverty indicators continue to worsen. The quality of, and access to, health care and education have been adversely affected by underinvestment, low staff salaries, replacement of professional health workers with military conscripts, excessive state intervention in school curricula, and a steep drop in the number of university students.

Economic outlook

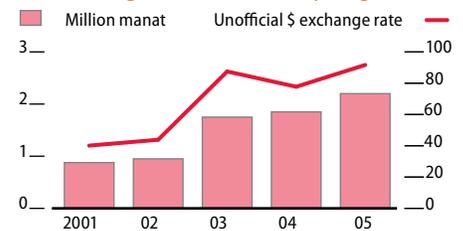
Medium-term growth prospects are subject to considerable uncertainty because of the economy's heavy reliance on exports of only a handful of energy and agricultural products, such as natural gas and cotton. If Turkmenistan manages to raise the price at which it exports natural gas to the Russian Federation and Ukraine (and which are currently well below the prices of Russian exports of natural gas to European countries, including Ukraine) in the course of 2006, this will provide a strong short-term impetus to the economy. GDP should grow by 5–7% a year in 2006–2007, depending on the timing and magnitude of the price adjustment. However, if the Government fails to secure this increase in

2.6.3 Average annual exchange rates



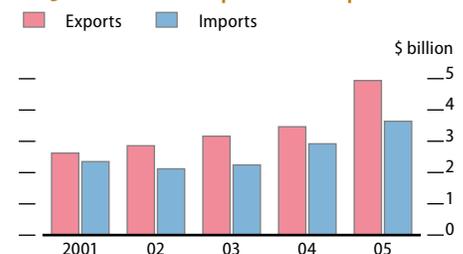
Sources: Government of Turkmenistan; staff estimates.

2.6.4 Average nominal monthly wage



Sources: Government of Turkmenistan; staff estimates.

2.6.5 Merchandise exports and imports



Sources: Government of Turkmenistan; staff estimates.

the export gas price, the economy is projected to grow by only 1–3% a year over the period, driven primarily by state-financed investment demand. In both scenarios, for energy, production and exports are expected to expand slowly due to capacity constraints, but for agriculture, they are forecast to stagnate because of slow progress in rural reform. Nonetheless, inflation is likely to be kept in single digits by a combination of tight monetary policy, price subsidies and controls, and cash restrictions.

From a longer-term perspective, the Government faces challenges on a range of fronts that it needs to tackle if it is to achieve sustainable growth, including widening its export base, implementing market-oriented reforms, strengthening governance, and allowing greater numbers of students to gain the qualifications required in a modern, globally competitive economy. More widely, it should curtail its intervention in economic activities, rationalize public expenditure, and adjust its social policies.