

# INTERNAL STABILITY AND PROBLEMS OF SECURITY DEVELOPMENT IN THE KYRGYZ REPUBLIC

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A number of radical reforms were carried out with the transition to a market economy in Kyrgyzstan, which have created a base for the formation of a multi-layered economy, a market infrastructure and the achievement of macro-economic stabilisation. These reforms have improved the overall environment for business.

At the same time, during the reform process, economic decline was very evident. Even now with apparent stabilisation of the economy, there remains a potential for crisis. The main reason for this is the inconsistency of the current economic policy of the state. The crisis which threatens to engulf the Kyrgyz economy shows how fragile stabilisation is without an expansion of production and an increase in competitiveness, which in turn provide a balanced development, GDP growth and better finances. Since 1990, there has been a sharp recession in industrial production, which was accompanied by degradation of infrastructure, the destruction of the technological core of the economy, the loss of domestic and export markets, and a growth in imports. Non payments throughout the economy have increased which have further destabilised financial markets. In particular, the devaluation of the national currency has provoked the withdrawal of investors from the Kyrgyz market.

There was also a rapid rise in interest rates, which meant that bank finance was concentrated in the informal, non-tax-paying sector. In such a situation, only raw material industries and shadow enterprises thrive. The tax losses due to the complex and inefficient tax system, the relative absence of direct foreign investment, the growth of the shadow economy and corruption throughout all branches of authority are the main reasons for the negative overall situation in the economy.

In my opinion, the adoption of a new edition of the Tax Code will allow us to reduce the general tax burden on investors and to shift part of it onto consumers. The introduction of a unified rate of income tax,

the reduction of the tax on profit, and deductions in non-budget funds will make it possible to increase the tax base and to reduce shadow capital. Moreover, the VAT allowances for new production and investment along with other changes will give a chance to boost foreign capital inflows into the economy of Kyrgyzstan. Such investment is vital for our economy at this moment in time.

The government of Kyrgyzstan carries out a moderate economic policy. It offers a friendly environment for foreign investments and seeks to restructure rather than renege on its external debts. But indecisiveness in actually agreeing and promulgating reform will delay the process of basic socio-economic renewal in the Republic for years to come. The fact that the state lacks control mechanisms combined with the decline in the cultural, moral and ideological potential of society has resulted in the growth of both the shadow economy and corruption.

Low dynamics characterise the real available incomes of the population and investment. The difficult financial position of enterprises in the real sector remains. Our traditional branches of the economy continue to decline due to insufficient funding and the poor state of infrastructure. The competitiveness of what is being sold only remains because of state subsidy. For several years, our shuttle traders have imported goods and taken out mainly US dollars. In this respect the problem of the non-competitiveness of the real sector of the economy has been solved by the invisible hand of the market. Among the countries of the CIS, Kyrgyzstan has the lowest export volumes proportionate to industrial production.

The inadequate development of small and medium-sized business is also an obstacle to economic progress. Given favourable conditions, such businesses can develop very quickly as they are motivated to react rapidly to the requirements of the market. The private sector can be especially effective in the agricultural, tourist and service sectors. The state of small and medium-sized business in Kyrgyzstan is still far from desirable. Under conditions of a transitional economy, such private firms should play a leading role in the national economy. But at present, they only account for one third of GDP rather than the 50-60% of GDP that we believe is necessary and desirable. Moreover, a certain stagnation in general private sector business development has been observed over recent years.

The conclusion remains that it is necessary to create a highly favourable legal, investment, financial, credit and organisational

conditions for the rapid growth of small and medium-sized business in Kyrgyzstan, which would also help in the struggle against poverty by creating new jobs for the people of Kyrgyzstan. The economic crisis combined with political mistakes have resulted in stagnation as far as socio-economic reform is concerned. This has manifested itself in a drop in real incomes and further stratification of society. At the present moment, Kyrgyzstan is one of the poorest republics in the CIS, with an official poverty level of 55.3%. Meanwhile, the social crisis continues, unemployment grows, child mortality is high, and life expectancy has fallen. The scale of these social problems makes it increasingly difficult to enact economic reforms.

One consequence of the growth in poverty and the aggravation of social conflicts are the dissemination of religious extremist ideas and the growth of inter-ethnic conflicts that threaten national security. The expense of countering drug trafficking and international terrorism is extremely high and this is another reason why economic growth is stunted. Thus the tasks which our country faces are complex, the most significant being:

- increasing living standards and the development of human potential;
- improving the competitiveness of the economy.

Without a solution to the first task it is impossible to unite Kyrgyz society. Without a solution to the second task, our country would remain on the periphery of global economic development. Therefore we should undertake maximum efforts to boost future economic development.

Ultimately, solutions to these tasks will determine the development of Kyrgyzstan and it will be necessary to solve them simultaneously over the coming years. Moreover, this might only be possible on the basis of constructing a socially-oriented market economy and the consecutive integration of Kyrgyzstan into the World economic system.

In the medium term, Kyrgyzstan must generate a competitive economy, having I believe the longer-term potential of becoming a dynamic growing economy able to increase the living standards of the population, to modernise production, and to guarantee national security. It will be necessary to solve a number of major social problems, to attract investment, to encourage innovation, to reform

budget-tax and finance-credit policy, and finally to carry out serious institutional reform. To solve the problem of the external debt - which exceeds 100% of GDP - without resort to default, it will be essential to create and maintain macro-economic stability. This should be the overriding task of the state because it is closely connected to the further stable development of the economy and the improvement of the Kyrgyz Republic's reputation in the global economic arena.

There is a further fundamental dilemma before Kyrgyzstan: development or security? Until recently, the answer was 'development', but events in Batken have shown that spending on security should be increased as well. Security spending in turn makes the resolution of social problems more difficult. Indeed, the success or failure of reform programmes in general are always ultimately judged by the living standards of the population. The hopes that the social problems of the transition period would be eased by fast growth of the economy were not realised. The resolution of these problems will require socio-economic policy reform by the state. First of all, it will be necessary to ensure stabilisation whilst simultaneously creating the preconditions for a gradual increase in the real money incomes of the population.

The achievement of all our goals is possible only under conditions of economic growth, which would in turn enable us to reduce poverty and unemployment, improve social standards, make education and public health services more widely available, increase life expectancy, and reduce the massive income differentials between rich and poor. All these things require more effective government as well as economic growth. This means taking resolute action to achieve macro-economic stabilisation. It also means supporting private business, the creation of new jobs, and making sure that growth is shared throughout all regions of the country.

Kyrgyzstan has chosen the socially-guided model of the market economy, which assumes the harmonious marriage of economic efficiency to social justice. Further market transition should be carried out with a deep and comprehensive consideration of the human factor. In Kyrgyzstan as elsewhere, this is the main "resource" of societal development.

The most important tasks to solve, beginning from today, are:

- maintaining economic growth on the basis of the further development of structural reforms;
- complete institutional reform to enable the effective functioning of a market economy;
- maintain the well-being of society as the economy grows;
- direct resources, including human, for the development of priority sectors, these being:
  - hydro-electric power and other non-hydrocarbon forms of energy,
  - agriculture and agri-business,
  - tourism,
  - banking and financial/information technology.

So, the basic purpose of our development should become the steady and stable growth of our economy, with the goal of increasing of well-being of the people. Kyrgyzstan should harmoniously and fully integrate into the World economy, as well as with international and regional economic unions. These links would lift us up onto a higher level of mutually advantageous economic cooperation both with our neighbours and with more distant foreign countries.

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