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# FINANCING FOR DEVELOPMENT IN THE EMERGING MARKETS OF THE UNECE REGION: A 2007 PERSPECTIVE

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## I. Introduction

At the International Conference on Financing for Development (FfD) held in Monterrey, Mexico in 2002, the United Nations member states agreed on a set of actions to address a shortfall that existed in the resources required in order for the world to "eradicate poverty, achieve sustained economic growth and promote sustainable development" while "advancing to a fully inclusive and equitable global economic system". More specifically, these actions can be grouped into the following six categories: 1) mobilizing domestic resources, 2) encouraging foreign direct investment (FDI) and other international capital inflows, 3) promoting international trade and market access, 4) increasing international financial and technical assistance, 5) solving external debt problems, and 6) enhancing the coherence and consistency of the international monetary, financial, and trading system, all with a view of fostering economic and social development. This set of actions must be viewed as part of a global partnership where the ability of each country to fulfill its responsibilities is contingent on others fulfilling theirs.

The emerging markets of the ECE region (ECE-EM) have made some progress over the last several years in regard to four of the six objectives. The two for which progress has been limited – aid and coherence of the international system are largely out of the control of the ECE-EM. The level and efficient use of domestic savings has been significantly enhanced by the substantial progress that has been achieved in improving financial intermediation throughout the region. The ECE-EM represent one of the few areas of the world where a significant percentage of the economies are net importers of capital. Integration within the region as well as globally has continued with the expansion of regional trading arrangements such as with the enlargement of the EU and the Central European Free Trade Area, and further development of EurAsEC. The development infrastructure networks of roads, ports, and pipelines as well as improvements in customs procedures have further supported increased integration in the region. The solid growth of the area has allowed debt levels to be reduced although only a few have benefited from debt write-offs.

All together, progress in these areas combined with the region's rapid economic growth has allowed poverty to decline and progress to be made in terms of the MDGs. Despite these favourable trends, a number of the MDGs are unlikely to be fulfilled without significant policy changes in these economies. The significance of the failure of the advanced economies to uphold their Monterrey commitments should not be overlooked. Aid has not increased to meet agreed upon targets, the outlook for the Doha round is poor given the intransigence of the advanced economies, there has been no significant progress in improving the architecture of the international monetary system, and little has been accomplished in terms of improving the power and voice of the developing and transition countries in the global institutions.

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## II. Current Economic Conditions

The emerging markets in the ECE have enjoyed an extremely favorable economic and financial environment over the last several years. These countries have experienced high domestic growth which has been supported by high commodity prices for their exports combined with solid growth in their export markets, and low interest rates due to low world interest rates combined with reduced credit spreads. Economic growth in the EU New Member States (NMS) continues to be quite high averaging 5.7, 4.7 and 6.2 per cent over the last three years (2004-2006) although it should moderate to about 5.6 per cent in 2007. Growth has been even higher in Southeast Europe (excluding Bulgaria and Romania) averaging 8.7, 6.8, and 5.4 per cent over 2004-2006 with a forecast of 5.2 per cent for 2007. The CIS minus Russia ranks amongst the fastest growing regions of the world having achieved a 9.7 per cent increase in GDP in 2006 (8.4 and 6.6 per cent in 2004-05) and was led by Azerbaijan's 31.0 per cent increase in GDP which makes it the fastest growing economy in the world. Growth there should moderate to 8.3 per cent in 2007. Russia's growth was 7.2, 6.4, 6.7 per cent over 2004-2006 with a forecast of 6.4 per cent for 2007. Economic growth in emerging markets is correlated to a much higher degree with interest rates than growth in developed economies. This explains to a degree their recent success and raises a potential concern about their ability to withstand a protracted increase in global interest rates.

Poverty exists for a number of complex reasons, but the lack of capital -- private capital, social infrastructure, and human capital, and the failure to utilize it efficiently stand out as perhaps the most important factor. In order to address this problem a society must save more domestically, obtain more capital from abroad, or use the capital that it has more efficiently. The FfD framework addresses these channels with the overall objective being to increase the size and efficient use of the capital stock of the developing and transition economies. Besides the countries' growth rates of GDP, the growth of gross capital formation provides a rough measure of their success in increasing their capital stocks. Capital formation fell significantly in the transition economies during the first five years (1990-1995) of the transition process and began to recover sooner in Eastern Europe than in the CIS. In recent years rates in the range of 20-25 per cent of GDP have been attained in most countries in the region; this is roughly similar to global averages. Several economies however, including Belarus, Estonia, Croatia, and Latvia have obtained rates of close to or over 30 per cent; quite remarkably, Azerbaijan has exceeded fifty per cent in several recent years. However the two largest economies, Russia and Turkey, had capital formation of only about 18 per cent of GDP during 2000-2005.

The different sub-regions of the ECE rely on different sources finance for their development. Each of the regions faces significantly different circumstances in terms of their level of development, access to official and private capital, and their ability to generate and use domestic savings. Domestic savings remains the most important source of finance but external sources are also important especially for the least developed economies of the region. The importance of the different types of external finance, whether capital flows, aid, remittances, or exports varies by country as does the way the resources are used such as payment to foreigners for previously invested capital, investment in other (foreign) economies, accumulation of international reserves, or imports of goods and services. It is only in the latter case, however, that a financial transfer is actually translated into a real transfer of resources.

It is difficult to access the financing situation for several of the countries in the region do the lack of appropriate data. This is especially the case for Turkmenistan and Uzbekistan, which do not provide balance of payments data to either the UNECE or the IMF.

## III. Mobilizing Domestic Resources

For most countries domestic savings provides the vast majority of financing for domestic investment. Relative to global standards, the ECE-EM generally have relatively normal levels of investment but relatively low domestic savings rates with the difference being financed by capital inflows from abroad. Therefore an area of particular importance for these regions is the need to better mobilize internal savings; one way to significantly accomplish this is by further developing their financial systems.

The ECE-EM have made significant progress in improving financial intermediation (translating domestic savings into investment) by developing their banking and financial systems primarily through institutional and regulatory reform including privatization. These economies have been progressing from having repressed financial conditions characterized by small banking sectors and low consumer debt to more “normal” market economy conditions. Bank credit, especially to households, has been growing extremely fast over the last several years; most recently, in a number of countries bank loans increased between 25 to 50 per cent over the year ending in the second quarter of 2006 and for some the growth has been even higher such as in Georgia where loans almost doubled. In Kazakhstan loans have grown annually by over 50 per cent over the last five years. Although rapid credit growth is a normal process and characteristic of financial deepening in developing countries, it has recently been much faster in the transition economies than in most other emerging markets, especially those in Asia. In addition, much of the complementary regulatory framework and institutional structure supporting the financial sector such as credit rating agencies, unambiguous ownership registers, appropriate legal instruments for repossessing collateral, and instruments for securitization of risks have in many cases only been recently created and credit histories for properly evaluating risks are not always available. Nevertheless this increase in private sector lending is a positive sign that problems with property rights and contract enforcement which had been questionable have now improved to a sufficient degree so that banks have confidence in making these loans. Nevertheless, this rapid credit growth, although needed for economic development, may have increased too fast in several of the less developed ECE-EM economies given their institutional and regulatory infrastructure and may now pose a financial vulnerability for them. Generally the fastest growth in credit has occurred in the economies where the outstanding “stock” of credit is the lowest as a percentage of GDP. These credit to GDP ratios are low relative to more advanced economies and thus there is considerable room for further growth as long as it proceeds in a well monitored matter.

This expansion of banking credit has allowed a much larger percentage of these economies’ populations to obtain funding and has allowed small enterprises and female entrepreneurs to obtain funding which is especially useful given that it promotes employment of often unskilled workers prone to poverty. Much of this credit expansion has been used to finance house mortgages when previously only those with existing resources were able to purchase homes. Increasing access to bank credit results not just in additional investment but can also lead to additional consumption as households borrow for consumption purposes.

The development of the financial sector, especially in Eastern Europe, has benefited from significant foreign ownership. In Eastern Europe (including Southeast Europe) the market share (in terms of total assets) of foreign owned banks is over 50 per cent in all the economies except Slovenia. Although foreign banks are also present in the most of the CIS, they generally account for less than 50 per cent of assets; an exception is Kyrgyzstan and to a lesser degree Armenia and Georgia. In these economies, where foreign banks are less knowledgeable about local conditions and credit risks, they often concentrate on short-term lending to large companies and the provision of non-lending services such as money transfers and foreign exchange operations. In several of these CIS economies (i.e., Moldova) the authorities have been actively attempting to attract foreign banks.

Although the CIS economies have made significant progress in this area, they nevertheless have the most underdeveloped financial systems in the region with the lowest degree of efficiency in financial intermediation and thus have the most to gain from further improvement. For example, in 2005 bank lending accounted for only 3 per cent of fixed capital investment in Moldova; the majority was self-financed (69 per cent) with state and local governments financing most of the remainder. The efficiency of financial intermediation may be affected by the degree to which the banking sector has been privatized. The banking sector has been largely privatized in most of the economies of the region; however, Belarus, Russia, Turkmenistan, are Uzbekistan are exceptions where state-owned banks continue to account for a significant percentage of banking assets. Financial intermediation is particularly a problem in several of the poorest CIS economies such as Turkmenistan and Uzbekistan. Due to losses historically and poor legal rights for savers, the private sector is distrustful of depositing its funds into the banking sector. For the funds available, they are not invested into the projects likely to provide the highest return but often go to firms favored by the government or the bank's owners. Funding for small and medium-sized enterprises is limited. Overall these financial institutions are poorly regulated and are often subjected to arcane forms of tax treatment. The large spreads between deposit and lending rates reflect the lack of bank competition, inefficient operations, and the generally risky environment in these economies.

Stock markets provide another avenue for channeling savings into productive investment; the capitalization of domestic stock markets of the more advanced ECE-EM (especially the NMS) have been increasing quite rapidly over the last several years, while these markets are still immature or non-existent in the poorer ECE-EM. The institutional development of these financial markets has also allowed the uncertainty which exists in these emerging markets to be measured and packaged into instruments that can be priced and sold to others more willing to accept risks. The securitization of mortgages is one such example. Despite the progress in developing the financial sector in the EME-EM further improvement is needed in regard to improving finance for SME and micro-enterprises, and developing venture capital funding for entrepreneurial activities especially those undertaken by women.

A source of vulnerability in regard to the rapid expansion of credit in these economies concerns the fact that in number of them a high percentage of loans are denominated in foreign currencies. At the beginning of 2006, over half of all outstanding domestic loans were denominated or indexed to foreign currency in a number of countries including (but limited to) Albania, Armenia, Bulgaria, Croatia, Estonia, Georgia, Hungary, Kazakhstan, Latvia, Lithuania, the Kyrgyz Republic and Romania. A currency depreciation can be problematic for borrowers of foreign-currency denominated loans, as the domestic currency costs of servicing these loans would increase. This might have only a limited direct impact on the banks since they generally have followed a risk management strategy which has limited their net foreign currency exposure. However, many of the borrowers of these loans are increasingly consumers (often for mortgages) who have no natural hedge against currency movements and a sufficient number of defaults could place strains on the banking system. At the same time, in several economies the public sector has been able to counter this trend by reducing its reliance on foreign-currency loans and issuing debt in local currency, thus diminishing their vulnerability to an adverse currency movement. Obtaining public financing from domestic sources or in domestic currency also contributes to the development of domestic financial markets.

This rapid growth of domestic credit has financed significant and much needed investment. However there are a number of potential problems associated with it that must be appropriately managed. As discussed, rapid credit growth can result in lower credit worthiness as the financial sector may lack the resources needed to evaluate credit risks. Increased investment spending increases aggregate demand and this can contribute to inflationary pressures, increased imports which can produce current account deficits, and put upward price pressure on investment assets such as equity markets and real estate which can become overvalued as speculators concentrate on recent price trends and not on the underlying productivity of the assets. The increased supply of loanable funds also encourages increased consumption spending as households wish to borrow against future income. The degree to which public policy should attempt to steer the use of these funds towards investment and away from consumption raises a number of difficult policy choices especially in the poorer economies where increased consumption can significantly increase living standards, although the poor have limited access to borrowing. All of these potential concerns are present to varying degrees in a number of the economies in the ECE-EM, and therefore there is a need to concentrate more on these possible macroeconomic implications and the trade-offs they often entail.

Public infrastructure can be financed in a number of ways; one method to reduce government borrowing needs while potentially improving the efficiency of the investment has been to rely on public private partnerships for its financing. However, pricing of these services requires the appropriate regulation to avoid monopoly pricing while pricing that reflects long-term costs may also harm disadvantaged groups that may have previously received these services at subsidized prices. The provision of some of these services may be viewed as a basic human right and thus pricing of these services at cost recovery levels may not be appropriate (without accompanying transfers). In some countries the quality of regulation has been limited due to lack of experience or poor governance generally. The improved financial performance that comes from private sector involvement often reflects the fact that the private sector charges higher prices and pays lower wages; thus the social gains from private sector participation are often much lower than that implied by the improved profitability of the firm. In order to encourage private sector participation, there is in some economies a need to further protect investor rights and improve transparency of information by improving the regulatory environment and the legal system and by strengthening and clarifying contract obligations.

Capital flight which reduces the resources available for domestic investment had plagued a number of the CIS economies, especially Russia, but recently appears to have diminished substantially due to the increased perceived stability of the area, the sizable increase in official international reserves, and the achievement of full currency convertibility; the Russian rouble was made fully convertible in 2006.

## IV. External Finance and Debt

Although domestic savings provides the vast majority of financing for domestic investment, additional externally provided finance can play a significant role in fostering economic development. Economies that are relatively fast growing but relatively poorer than the advanced economies might be expected to borrow from abroad in order to smooth out their long run consumption pattern. External finance can take various forms including capital inflows, foreign aid and remittances. The ECE-EM, especially SEE have benefited considerably from external sources of finance; much more than economies in the other major geographical areas of Africa, Asia, and Latin America. This trend is generally consistent with the underlying "logic" of the FfD proposal in that foreign resources are mobilized to provide the resources needed for achieving the MDGs. Foreign savings have played a dominant role in financing gross capital formation over the last decade in several of the low-income CIS economies such as Armenia, Azerbaijan, Georgia, Kyrgyzstan, and Moldova as well as Macedonia in South-east Europe. However a number of the CIS including Belarus, Kazakhstan, Russia, Tajikistan, Ukraine, and Uzbekistan have relied all most solely on domestic savings. For those economies that have relied on external sources of finance, they have correspondently consistently run sometimes quite large current account deficits over the last decade. This reliance on foreign capital may thus pose a vulnerability for some of these economies. Twelve of the ECE-EM had current account deficits of ten or more per cent of GDP in 2006; the energy-rich CIS economies are exception to this general pattern. In 2006, the ECE-EM in 2006 received almost 44 per cent of total private net flows ($218.4 billion); estimates by the IIF (2007) are that these flows will remain stable in 2007 while accounting for 46 per cent of the world share. This foreign finance, however, does not add to domestic investment dollar for dollar, as a significant share of this leaks back out through various channels and a share of the remainder is used for consumption.

As countries develop there is a trend in which its foreign borrowing switches from mainly being undertaken by governments to being untaken by the private sector; in addition the source of the funds switches from official sources to private sector banks and other sources of equity. This transition in the nature of external borrowing has been quite apparent in the more developed economies of South-east Europe and the CIS. In a group of the CIS (Armenia, Belarus, Kazakhstan, Kyrgyzstan, Russia and Ukraine) for which there is data, public debt as a percentage of total external debt has declined from over 50 per cent as recently as the last quarter of 2003 to below 30 per cent in the first quarter of 2006. A similar trend exists, but to a much smaller degree, in the EU NMS as they made this transition earlier. This trend has positive implications for the FfD agenda to the degree that this represents a shift from financing current government operations to building the private sector capital stock. However this is not a positive trend if it reflects a reduction in public sector infrastructure development towards private sector consumption and real estate speculation.

To a significant degree, this reduction in public sector external debt is due to a reduction in government deficits which in most cases are not greater than three per cent of GDP. Tax revenues have increased substantially due to a number of factors including improved public administration and healthy economic growth, however for a number of the resource rich economics this has been due to taxation of the rents earned by the extractive industries. These rents not only provide a source of funds for public sector infrastructure development but the profits allow further private sector investment in the selected industries. The degree to which these profits can contribute to financing investment in a broader range of industries is dependent of the development of financial sector intermediation. The NMS have been under pressure to control debt and deficits as they attempt to fulfill the Maastricht criteria for euro accession although that may still be several years away for most of them.

The significant inward flow of external capital can present countries with macroeconomic complications. A significant inflow of capital can over stimulate the economy and produce inflation if the central bank attempts to maintain a currency peg. For some of the economies with better developed financial markets (where there is a market for government debt in domestic currency) it may be possible for the central bank to sterilize this inflow; however this results in higher interest rates which reduces domestic investment. This is hardly a desirable policy option if one of the country's primary economic objectives is to enlarge the capital stock. An alternative is to allow the domestic currency to appreciate; this results in an alteration of the relative price of traded and nontraded goods so that the increased demand is spent externally. Although this may allow the financial transfer to result in a real transfer of economic resources (assuming there are minimal terms of trade changes that can result in the classic transfer problem) which is central to the FfD initiative, it reduces the competitiveness of the export sector and may harm the long-run development of the economy. A significant number of the ECE emerging markets are currently having to deal with these macroeconomic trade-offs of inflation and appreciation in connection with capital inflows. Increased export revenues brought on my higher commodity prices and increased remittances have also contributed to this dilemma.

The external debt of the eight low-income ECE economies has generally declined due to prudent debt management and solid economic growth.[1] For example, public and publicly guaranteed debt at the end of 2005 amounted to 22 per cent of GDP for Armenia, 14 per cent for Azerbaijan, 28 per cent for Moldova (down from 95 per cent in 2000). The vast majority of this debt is owed to multilateral international organizations (i.e., for Armenia, it is 89 per cent), primarily the World Bank and to a lesser degree the IMF. Public debt remains quite large in a number of other ECE emerging markets such as Turkey were it is close to 69 per cent of GDP; in fact Turkey accounts for two-thirds of the IMF's total outstanding credit.

The European Bank for Reconstruction and Development (EBRD) has invested considerable funds into the transition economies since it was established in 1991 to support private sector development. It has financed infrastructure projects such as for road building, airport moderation, sea port terminals, energy efficiency projects, and water facilities. In addition the Bank has encouraged institution development such as in the financial sector by developing the supervisory role of the central bank and facilitating privatization as well as assisting in the development of new financial products such as microfinance and mortgages. The Bank has an Early Transition Country (ETC) Initiative which provides some specialized financial instruments for several low income CIS members.

For the ECE-EM overall, the largest source of external finance is from private capital inflows; FDI inflows are averaging around 3.5 per cent of GDP a year while portfolio inflows (equity and bonds) are averaging around 2 per cent a year. Although FDI inflows have been substantial for over a decade, the inflow of portfolio capital, especially equity capital is much more recent. However, the importance of these two types of capital inflows varies amongst the subregions. In the NMS, FDI has averaged 5.25 per cent while portfolio is slightly above

[1] The low income ECE includes the eight economies in the ECE with the lowest per capita income; all of these economies participate under the IMF Poverty Reduction and Growth Facility. This group includes Albania, Armenia, Azerbaijan, Georgia, Kyrgyzstan, Moldova, Tajikistan, and Uzbekistan.

3 per cent of GDP; the percentages are 4 and 1 per cent of GDP in non-EU Southeast Europe (without Turkey), 5.75 and 1.5 in the CIS-11, 2.25 and .5 in Russia, 1.75 and 3.5 in Turkey. In the Low Income ECE-8, FDI inflows have averaged over 8 per cent of GDP but this is skewed by the incredibly high rates of FDI into Azerbaijan (which had exceeded 40 per cent of GDP in 2003 and 2004 before dropping to 13 per cent in 2005); with Azerbaijan dropped, FDI has averaged 4 per cent of GDP for this grouping. Portfolio inflows are insignificant for the low income ECE-8.

Becoming overly dependent on private capital inflows entails significant risks as it increases a country's probability of experiencing a currency crisis. These crises not only result in significant short-term declines in output but also can permanently lower a country's steady state growth path. Currency crises have significant impacts on the working population and can significantly increase the poverty rate. Although avoiding a number of economic situations such as running large fiscal or current account deficit can lower the probability of experiencing such a crisis, there is no risk free economic model that can guarantee stability. Although the region is not immune from currency crises given the crises in Russia in 1998 and Turkey in 2000-2001, the stability of several economies with currency boards including Bulgaria, Estonia, Lithuania might suggest that this form of currency/monetary arrangement might need to be reappraised after being generally discredited following the collapse of such a system in Argentina. These economies have benefited from significant capital inflows with accompanying large current account deficits of over 10 per cent but have maintained macroeconomic stability and rather rapid economic growth.

## V. Foreign Direct Investment

FDI inflows into the ECE-EM have been relatively stable at around three to four per cent of GDP for the last five years. These inflows, as a per cent of GDP, have been slightly higher for the NMS and the CIS-11, about at four per cent for SEE, but significantly lower in the two largest ECE-EM economies, Russia and Turkey. As a per cent of GDP, FDI inflows into Azerbaijan have been one of the highest in the world. Private inflows of FDI should remain relatively stable over the next several years in the emerging markets of the ECE. The conclusion of many privatizations phases will act to reduce FDI flows while the continuing economic prosperity of the region combined with further institutional reform is likely to further encourage FDI including the reinvestment of retained earnings by foreign affiliates which is the main mode FDI investment. However, especially in the CIS there is still significant potential for further privatization; in Russia for instance, there are plans to sell over 1,500 companies in 2007. In terms of the stock of FDI as a per cent of GDP, there has been more investment in the NMS, followed by SEE and then the CIS. FDI remains a genuinely preferred type of capital inflow in that is often accompanied with managerial and technological inputs and has also proven to be less volatile. Empirical research on the ECE region has found that FDI in the region is significantly reduced by political instability. A policy objective for many of the ECE-EM is to increase the linkages to domestic enterprises from FDI.

Outward FDI by developing and transition economies has been increasing significantly over the last several years. This is the result of their increasing per capita incomes, increased domestic profitability which provides a source of funds, and reduced government restrictions often resulting from a less binding foreign exchange constraint due to higher commodity prices for exports. However, for the ECE-EM, Russia is the dominant source of outward FDI and accounted for 87 per cent of the outward FDI from the CIS and

SEE in 2005. A significant share of Russian outward FDI is undertaken by state-owned enterprises and in some cases may be due to geopolitical rather than purely economic considerations. Hungary leads the NMS in terms of outward FDI.

## VI. Other Capital Inflows

The current global expansion has been particularly favourable for emerging markets which have benefited from an abundance of liquidity due to the accommodating monetary policies in the advanced economies and the carry trade that they allowed, monetary expansion by current account surplus emerging markets from their foreign exchange interventions, and the recycling of petrodollars and the foreign exchange reserves of the Asian central banks. This has created a global search for yield that has resulted in an appetite for risks which has decreased the interest rate spread on emerging market debt (relative to risk-free U.S. bonds) to an all-time low in April 2007 based upon the widely used JPMorgan EMBI index. Emerging market bonds which as recently as five years ago had interest spreads of five or more percentage points are now below two percentage points while those of the ECE emerging markets are mostly below one per cent. The NMS appear to have benefited from a EU effect that has allowed them to borrow at rates 50-100 basis points lower than comparable emerging markets. Nevertheless these economies are paying higher interest rates than those of the advanced economies and it is expected that euro accession will further reduce this risk premium. However, capital inflows have historically proven to be very pro-cyclical and this has resulted in a magnification of their business cycles; poverty trends to increase significantly during the downturns.

Companies in the CIS are increasingly able to raise capital in foreign (i.e., London) capital markets. For example during 2005-2006 over $4 billion was raised by Kazakh firms in London markets. Foreign banks, especially those in Eastern Europe, have encouraged the inflow of capital into these economies by obtaining funds from their parent banks and loaning it out domestically where interest rates are often higher. One consequence of this however, is that since these funds are obtained in foreign currency, the domestic branches often prefer to loan these funds in foreign currency in order to limit their vulnerability to exchange rate changes. This shifts the risk on to businesses and consumers who may be ill prepared to deal with these risks.

## VII. Aid

Foreign aid can provide an additional source of finance for various types of projects; an important objective is the selection of projects that will tend to further encourage private investment flows instead of replacing them. The former is more likely if aid is directed towards financing projects with a public goods nature or projects which have significant positive externalities and would not be financed by the private sector. Since private capital markets seem to inadequately finance human capital development for the poorer segment of the population, aid used for health and education of this segment can contribute significantly to economic development while addressing equity concerns as well. Creating a more inclusive society is further likely to contribute to development by increasing political stability. Aid is also important is stabilizing a situation after negative shocks.

For the ECE-EM overall aid has annually been below one per cent of GDP but it has been much greater for SEE and some poorer regions of the CIS. In SEE it is currently about 3 per cent of GDP having fallen from almost twice that several years earlier; it has been especially significant for Bosnia and Herzegovina and Serbia. In the CIS it has been close to or over ten per cent of GDP over the last several years for Armenia, Georgia, Kyrgyzstan and Tajikistan, although it has declined somewhat over this period. Except for Moldova, aid has been quite low in the remaining economies of the CIS and has been quite low for Turkey.

The UN[2] has made estimates of the level of investment required to meet the MDG goals and the level of resources that can be reasonably raised domestically; the difference between these two is termed the MDG financing gap. This gap thus represents the level of aid required to meet the MDG goals. This gap has been estimated to be approximately 10 to 20 per cent of the GDP in five of the ECE low-income 8; this includes the three central Asian CIS, Armenia, and Moldova. The latest estimates (2004) of aid reveal the Kyrgyzstan and Tajikistan receive almost 12 per cent of GDP, Armenia slightly over 7 per cent, Moldova almost 5 per cent and Uzbekistan only 2 per cent if GDP. The other three ECE low-income 8 (Albania, Armenia, and Georgia) have aid levels in the 5 to 7 per cent range. Thus for most of these economies, the aid level is several percentage points of GDP below what is estimated as needed in order to achieve the MDGs; aid flows to Uzbekistan are particularly low and are probably less than 20 per cent of what is needed. As for the other transition economies, aid flows are in the 4 to 7 per cent of GDP range for SEE but below one per cent for the other CIS.

The NMS receive considerable assistance from the EU for infrastructure development of their poorer regions under the structural and cohesion funds; this assistance is generally not included in published aid figures. Over the previous budget period of 2000-2006, this assistance was in the range of 2 to 3 per cent of the NMS' GDPs while it is likely to increase to about 4 per cent of GDP for the next budget cycle of 2007-13. The procedures for obtaining these funds are sometimes difficult to achieve and thus the utilization of these resources has been low especially in the initial years of membership. Generally, however these funds, where committed, have been efficiently used and there are undoubtedly valuable lessons in how this aid is planned, implemented, monitored, and evaluated that could be applied more generally to increasing the absorptive capacity of development assistance supplied to the developing countries in the rest of the world. Because of these difficulties and the nature of other EU programs, Romania for instance, may end up as an actual contributor to the EU budget in 2007 although it is likely to become a recipient in future years. A number of non-EU economies also benefit from EU assistance under the European Neighborhood Policy Instrument and the Macro-Financial Assistance program.

The low-income ECE-8 economies participate in the IMF's Poverty Reduction and Growth Facility (PRGF). This facility provides additional multilateral low-interest loans (an interest rate 0.5 per cent) as part of a comprehensive poverty reduction strategy, which requires the recipient country to satisfy numerous IMF criteria. Although these criteria generally provide for prudent macroeconomic management and a comprehensive program to address poverty, the conditionality of the program can nevertheless raise questions about the loss of national sovereignty.

The Heavily Indebted Poor Countries (HIPC) initiative of the World Bank and IMF allows poor countries to have most of their bilateral external debt written off as long as they pursue an IMF and World Bank adjustment and reform program. Russia has recently decided to cancel the debt of HIPC participants owed to them. So far no ECE country has been

[2] *Investing for Development: A Practical Plan to Achieve the Millennium Development Goals*, UN, 2005.

admitted to the program although Kyrgyzstan has been determined to be a high-debt-distress country and potentially eligible for HIPC assistance. Upon completion of the HIPC, Kyrgyzstan may also be eligible for the Multilateral Debt Relief Initiative (MDRI) which cancels debt owed to the IMF and IDA of the World Bank. Tajikistan is eligible for up to $100 million of debt relief under the MDRI.

The objectives of the FfD and the MDGs should be viewed as a partnership between the advanced and the developing and transition economies. An important component of the advanced economies commitment to this development agenda is an increase in overseas development aid (ODA). Most of the advanced economies are members of the ECE region; ECE members accounted for 85.9 per cent of the ODA by the OECD's Development Assistance Committee (DAC) which provides almost 90 per cent of the world's total ODA (which equaled $107 billion in 2005). Up to this point, the levels of aid have not increased substantially and are not on target to achieve their commitments pledged for the year 2010. In 2005 only four countries (all ECE members) provided more than the UN target of 0.7 per cent of their GNI in aid; these were Luxembourg, Norway, the Netherlands, and Sweden. Several ECE members provided less than the current (2005) DAC average of .33 per cent; these were Greece, Italy, Portugal, Spain, and the United States. The U.S. however is the largest provider of ODA in terms of dollar value and provides over a quarter of total ODA. As part of their EU membership the NMS are committed to becoming donors as their level of development increases.

Seventeen countries in the ECE are recipients of DAC-ODA including all of the CIS except Russia (i.e., CIS-11) and all the non-EU members of South-east Europe including Turkey. Together they received $5.7 billion or 5.4 per cent of worldwide ODA receipts in 2005; approximately 3.4 per cent went to Southeast Europe and 2.0 per cent went to the CIS-11. Serbia and Montenegro received the most in Southeast Europe ($1.1 billion) while Ukraine received the largest amount in the CIS ($410 million).

Currently the effectiveness of aid is reduced by the failure of the donor's to provide the recipient countries with multi-year timetables of aid delivery which would increase the ability of the recipients to properly plan and manage these aid flows. Similarly, an increase in the amount of aid available to the general budget would give the recipient more flexibility than project-based financing but requires the recipient to take on more responsibility for efficiently using the aid since the donor loses a degree of control over its use.

## VIII: Remittances

Remittances are an increasingly important source of external finance for the ECE-EM. Generally NMS workers have gone to Western Europe, SEE workers to the NMS and Western Europe, and CIS workers to Russia. For the ECE-EM they amount to slightly more than one per cent of GDP, but for several of the lower income economies they are an extremely important source of income. The latest estimates (generally for 2005) show that they were valued at over 30 per cent of GDP for Moldova and Tajikistan, over 15 per cent of GDP for Albania, Bosnia and Herzegovina, Kyrgyzstan, and Serbia, over ten per cent of GDP for Armenia, and about five per cent of GDP for Bulgaria, Romania, Azerbaijan, Georgia, and Uzbekistan. Thus for a country such as Moldova, remittances are twice as large as capital inflows and aid combined and almost as large as total exports. As a percentage of GDP, remittances are relatively low for Russia and Turkey averaging less than one-half a per cent. Remittances are an additional source of foreign exchange and like aid, but unlike capital flows, they do not create a future repayment obligation; they have the desirable property of being relatively stable and have even been found to increase when other sources of external finance dry up. Remittances have generally been used to booster consumption but have also been used to finance investment and help establish new enterprises. Given the importance of remittances, banks in the region are attempting to develop better financial products that would insure this income promotes investment.

Where emigration has been significant, it has had important implications for domestic labor markets. The emigration of workers makes the remaining workers scarcer; under conditions of high unemployment, this has the effect of improving the employment prospects of those that remain and may also increase their wage levels. Since emigrants are relatively high-skilled, their leaving can reduce the stock of human capital; however in the longer run they may contribute to the domestic human capital stock if they return with skills that were acquired abroad. In many cases these migration flows do not occur within a legal framework that provides the workers legal protections and as a result they can be subject to various forms of exploitation.

The level of remittances is poorly reported in the balance of payments statistics of the region. According to World Bank surveys of migrants, between one-third to two-thirds of migrants did not use a formal channel such as bank transfers to transmit remittances but instead use an informal channel such as public transportation drivers, friends or family to transfer funds. Thus official balance of payments statistics even where they include remittance entries often undercount the actual level of remittances.[3]

## IX. Trade

Exports provide the ECE-EM with their largest source of foreign exchange. Exports in the region have grown substantially over the last several years due to rapid income growth in their export markets, improvements in their terms of trade especially the natural resource exporters, an improved pan-European infrastructure of roads and rail, progress in implementing regional trade agreements, and the reduction in other trade barriers and other transaction costs associated with trade. Exports have increased by an average of over 20 per cent a year (2003 to 2005) for most of the ECE-EM; the Central Asian economies have experienced solid but less robust export growth. As a result, the ratio of exports to GDP has been on an upward trend for most of the ECE-EM.

Regional trade integration through preferential trade arrangements in the ECE region has been only partially successful. The accession of the NMSs to the EU has been a great success, but regional agreements in SEE and the CIS have been hampered by a number of factors. Regional integration in SEE is hindered in some respects by the countries' ultimate aim of eventual EU membership and the fact that countries have in the past and are likely in the future to leave any SEE regional grouping for EU membership. This creates temporary comparative advantages which may no longer exist after EU membership. The Central European Free Trade Agreement (CEFTA) has had a shifting membership which has included at some point many of the current NMS and is scheduled to be expanded in May 2007 from its current membership of only Croatia and Macedonia to include Albania, Bosnia and Herzegovina, Kosovo, Moldova, Montenegro, and Serbia. It is possible Ukraine may also

[3] This report contains estimates of remittances using a technique developed by the ECE and reported in the UN's *World Economic Situation and Prospects 2007* (box 4.1).

join at some future date. The western Balkan countries have preferential access to the EU under the Stabilization and Association Process arrangements. Turkey and the EU implemented a customs union in 1999 and it has several bilateral agreements with countries in SEE.

Regional economic cooperation among CIS countries is hindered by a variety of technical barriers to trade, incidences of regional instability and conflict, prevalent corruption and lack of transparency of the regulatory environment, drug trafficking, and lack of security. Many of the CIS have limited access to world markets for a number of reasons. High transportation costs in the CIS substantially reduce the competitiveness of their exports on the world market and increase the cost of most imports, thus reducing inter- and intra-regional trade. In Central Asia, transport costs to world markets are much higher than for most countries and in some cases may approach 50 per cent of the value of an item. Such high costs are mainly due to the fact that these CIS countries are disadvantaged geographically, being either landlocked or outside the main trade routes, surrounded by rough terrain, and being great distances from major industrialized regions; in addition, they lack modern infrastructure and have fragmented transport markets that prevent economies of scale. The higher transport costs are significantly exacerbated by the widespread unofficial payments and red tape. Incidence of unofficial payments at the customs control points is most prevalent in Central Asian countries and the Caucasus.

The proposal to create a CIS-wide free trade area or customs union does not seem to have adequate support from a number of the CIS members, and thus its prospects remain unlikely. Much of the liberalization that has occurred has been in smaller regional groupings, especially the Eurasian Economic Community (EurAsEC) which represents probably the grouping most likely to evolve into a legitimate customs union as it has already achieved relatively free trade amongst its members. Although a large number of bilateral free trade agreements have been signed, it is generally conceded that many of these have not been implemented. Out of 132 bilateral trade flows in the CIS, 82 of the flows are covered by a bilateral free trade agreement. This averages out to around seven per country but varies from a low of two for Tajikistan to a high of 10 for Moldova and Uzbekistan. Despite these agreements there are currently only about 50 flows where trade is relatively free, but even with these there are often extensive product exclusions. Even when tariffs are low or free, there are often numerous other types of restrictions that serve to limit trade. Although judging the extent of liberalization is subject to various interpretations, Azerbaijan, Moldova, and Turkmenistan currently seem the least committed to free trade with the other CIS, followed by Armenia, Georgia, and Ukraine. At present, Belarus and Russia are probably the most integrated of any group of CIS members. Current estimates are that only 60 per cent of Russian trade with the other CIS is conducted on a free-trade basis. Other CIS groups include the Central Asia Cooperation Organization (CACO) composed of Russia and four Central Asian countries (all except Turkmenistan), and GUUAM, a regional organization comprised of Georgia, Uzbekistan, Ukraine, Armenia, and Moldova that is aimed at promoting and facilitating multilateral cooperation in a number of areas, including transport and commercial sectors. A number of the CIS have also joined organizations with non-CIS members; prominent among these is the Shanghai Cooperation Organization (SCO) whose original focus was on regional security and stability but has been shifting over the years more towards economic cooperation. The EU’s trade relationship with the European CIS is developed under the European Neighbourhood Policy.

In parallel to regional preferential arrangements, the ECE-EM are also pursuing multilateral integration initiatives, most importantly WTO membership. Membership in the WTO is an important factor in improving market access for exports and thus allowing countries to integrate into the world economy and gain foreign exchange through exporting. Currently only four members of the CIS are WTO members (Armenia, Georgia, Kyrgyzstan, and Moldova) while the rest are in various stages of negotiations (except for Turkmenistan); Russia is the largest economy in the world that remains outside of the WTO system. Although Russia achieved a significant milestone in 2006 by finalizing with the U.S. its last important bilateral agreement, a definitive date for Russian membership has yet to be set. WTO membership for the remaining CIS is not eminent and remains an important barrier to exporting manufactures to the world market. Although it is to be expected that new members accept the existing standards of old members, it appears that current WTO members are using their "insider" power to extract excessive concessions for those wishing to join. Although causality is difficult to establish, a situation suggestive of the possible poor bargaining strength of the new members is that the four CIS economies that are members of the WTO all have significant current account deficits; the deficit in 2006 was 5.6 per cent of GDP for Armenia, 10.0 per cent of GDP for Georgia, 12.8 per cent of GDP for Kyrgyzstan, 11.9 per cent of GDP for Moldova. In SEE, Bosnia and Herzegovina, Montenegro, and Serbia are not WTO members. From the perspective of these non-members more emphasis needs to be placed on modifying WTO accession criteria and less on completion of the Doha trade round. The Doha round, more generally, however has been a disappointment. If a final agreement can be reached, it may offer improved export opportunities which might be a small additional stimulus to development for the poorer economies of the region, but the stated goal of creating a more equitable global trading system has not been given much consideration.

In South-east Europe (including Turkey), the trade-to-GDP ratios have been slowly increasing over the last decade; their share of trade with the EU has been increasing as well. The structure of exports has shifted towards manufactured goods, as there has been a decline in the share of food and raw materials. Nevertheless their exports have remained concentrated in a limited number of goods. All of the CIS have higher export to GDP ratios than in the late 1990s; Moldova's export ratio although higher than in 1998 has been declining over the last several years due to its trade dispute with Russia. Over the last decade the CIS have significantly diversified their geographical destinations for exports of natural resource and raw materials but have been less successful in terms of promoting their manufactures outside the CIS. There is no definitive trend for the degree to which CIS trade is concentrated amongst themselves; the CIS share is down in slightly over half of the economies and up in slightly less than half. Nevertheless Russia remains either the largest import or export partner for all of the CIS and in several cases is the largest for both. In terms of both manufactures and non-manufactures there has been limited progress in diversifying their export structures to cover a wider range of goods. Currently, manufactured exports as a share of total trade vary considerably across the CIS from relatively high levels in Belarus and Ukraine to very low levels for the Central Asian CIS. The CIS under-rely on the other CIS for their imports of manufactures but over-rely on them as a destination for their own manufactures exports. The trade of the CIS is noteworthy to the degree to which there is a relative absence of intra-industry trade; this is even more the case for manufactures. Improvement in the transportation infrastructure of the region is an important requirement for further expansion of export markets.

Overall terms of trade developments in the ECE-EM have been positive and are providing additional revenue much of which is "excess profits" or rents that are heavily taxed and can thus be used for infrastructure development. The Central Asian CIS are producers of commodities (Kazakhstan – hydrocarbons, Kyrgyzstan – gold and silver, Tajikistan – aluminum, Turkmenistan – hydrocarbons, and Uzbekistan – gold and cotton) and have benefited from the global increase in commodity prices. However these price changes have negative implications for many of the energy importers which are generally the poorer ECE economies. The cost of natural gas imported from Russia has more than doubled in several of the CIS over the last several years. There have been several other negative external shocks that have proven significant. For example, Moldova has temporary lost access to Russia for its wine exports due to phytosanitary concerns. Historically Moldova exported 80 to 90 per cent of its wine to Russia and this accounted for almost 10 per cent of its GDP; only a small percentage of the wine has found an alternative export market.

## X. Tourism

A sometimes overlooked source of foreign exchange is tourism. Europe is the largest tourist destination capturing by some accounts over half of the world market. Most European economies have a significant positive balance in terms of tourist revenue. The transition economies especially those in Europe are likely to be able to gain a significant share of this market given that this region has only recently been opened to tourism, has many historical sites, and has costs significantly below those in Western Europe. The accession of the NMS has increased the attractive of these economies as a destination and euro adoption is likely to further improve the attractiveness of this region. For example, Hungary is now attracting over 20 million tourist a year and had tourism receipts of over $3 billion in 2003, this was more than its inward FDI in that year. Over the last four years the number of foreign tourist to Bulgaria has increased by 50 per cent and it is estimated that Bulgaria should earn about $2 to $2.5 billion annually in tourist revenue over the next few years.

## XI. The Use of External Finance

In addition to examining the different sources of external finance, it is also useful to examine how they are used from a foreign exchange perspective. The chief benefit of externally provided finance is the additional real resources that can be transferred to a country so that it is able to consume and invest more than it produces. If restricted to the extra goods and services transferred in the current period, this is measured by the balance of trade and services (or excess of imports over exports) while the current account provides a broader measure which also includes the current use of foreign owned resources. What is apparent from an analysis of the use of external finance is that a significant proportion of it is not used to transfer real resources to the recipient but is instead recycled back to the rest of the world. Overall, the ECE-EM have been allowed to consume extra goods and services valued yearly at approximately 2 per cent of GDP (average over 2004-2005) while the low income ECE-8 have been able to consume an additional 9 per cent of GDP. This extra consumption has been especially large for SEE which has been able to obtain net imports of over 18 per cent of GDP while it has been only 3 per cent for the NMS. Russia and the CIS-11 actually produce more goods and services than they use and thus they actually provide real resources to the rest of the world.

For many of the subregions or countries the actual real transfer of resources which can be used for investment for development or the immediate improvement of living standards through higher consumption is less than one-half of the gross inward transfer of financial resources (Southeast Europe being an exception). This is due to the “leakage” of this inward flow into an outflow of financial resources. In a number of countries which in the past have relied on either private investment or private and official borrowing, there is a need to pay a considerable amount for debt service and repayment or for the repatriation of profits and dividends from previous equity investment. For the EU NMS this amounts to around (depending on year) 3.5 to 4 per cent of GDP while it is about 3 per cent of GDP in the CIS-11, 2 per cent of GDP in Russia, and slightly below 2 per cent of GDP in Southeast Europe including Turkey. The very large current account deficits in Estonia and Hungary are driven not by large deficits in the trade balance but by large deficits in income payments for capital services. For the middle-income countries these payments must be considered as a necessary costs of relying capital inflows; however, for the low-income economies this drain of resources may need to be/ or has been addressed through initiatives directed at debt cancellation.

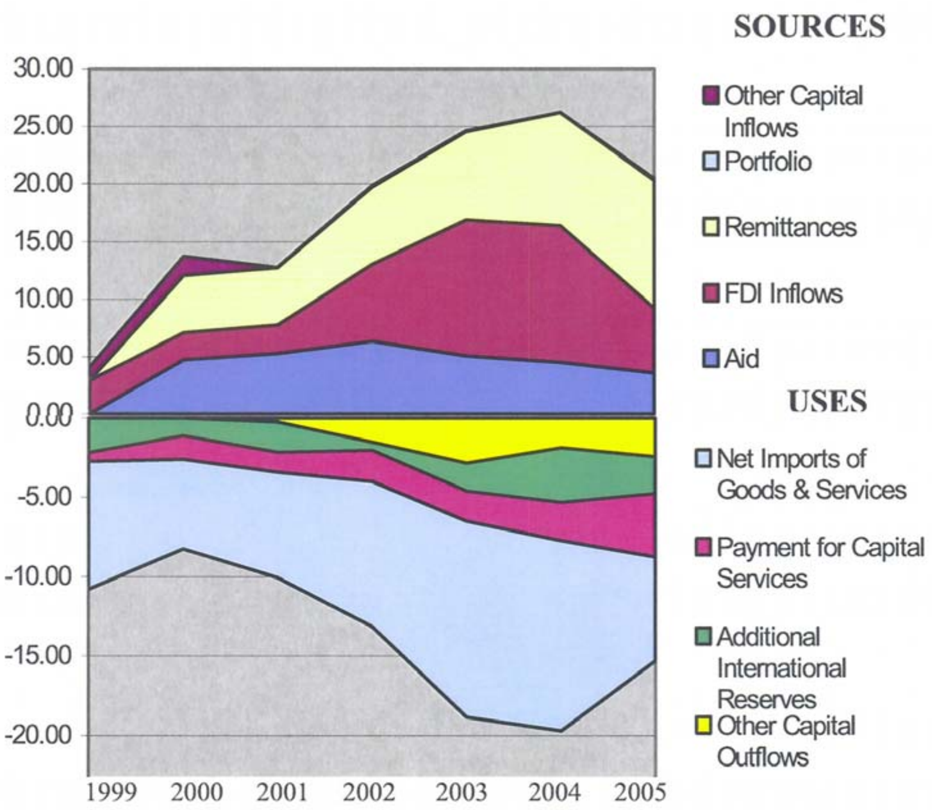
The accumulation of additional foreign exchange reserves is an additional leakage of externally obtained resources that could have been used instead to transfer additional real resources to these economies. For the region overall, reserve accumulation was almost 5.5 per cent of GDP during 2005; this is double the rate of only a few years ago. To some degree this high level and increasing trend is due to the rapid accumulation of reserves by Russia where they amounted to 8 per cent of GDP in 2005 and is probably higher in 2007. For Russia, this would appear to be a sensible policy as a way to smooth consumption due to fluctuating energy prices and ensure some intergenerational equity in consuming its natural resource wealth. In addition, Russia may be reaching limits on its ability to absorb foreign resources without incurring some additional macroeconomic problems. However reserve accumulation in 2005 was also significant for the NMS (accounting for 3.6 per cent of GDP), SEE (4.7 per cent of GDP), the CIS-11 (4.7 per cent of GDP), and Turkey (4.9 per cent of GDP). Reserve accumulation averaged almost 3 per cent of GDP for the low income ECE-8 over 2004-2005. Although accumulation of reserves appears necessary given the nature of the current international monetary system, the fact that they consume such a significant amount of the inflow of external resources further highlights a major shortcoming of the current architecture of the international monetary system and a major costs of relying on private capital inflows. The international monetary system requires a mechanism to provide adequate reserves in crisis situations; the current resources available to the IMF are insufficient for this purpose and that organization has made use of such funds highly undesirable do the stringent conditionality that is applied. This conditionality has often further magnified the economic costs of these crises instead of mitigating them. Regional assistance such as the Chiang Mai Initiative in Asia has not been developed for the ECE region, although there was a Memorandum of Understanding concerning cooperation during cross-border banking crises which was signed in December 2006 between Sweden and the Baltic economies which provides some additional assurances for financial markets.

The accumulation of reserves also has negative implications for government finances when it is necessary for inflation control to sterilize the monetary growth that results from reserve accumulation. In such a situation the government must typically issue high yielding domestic debt in local currency while investing in low yielding foreign bonds. Greater exchange rate flexibility can reduce the need for foreign exchange reserves.

## XII. Conclusion

The ECE emerging markets have made considerable progress in both increasing and better utilizing domestic resources for development purposes and obtaining benefits from further integrating themselves into the global trade and financial system. Nevertheless it must be recognized that there are often difficult tradeoffs in achieving these objectives. Increasing domestic savings and investment not only lowers domestic consumption but is often achieved by implementing policies that have a bias against the lower income segment of the population. Obtaining more capital from abroad can burden future generations with debt and dividend payments and can expose the economy to external shocks such as currency crises. Given the fact that a significant percentage of capital inflows must be used to accumulate additional international reserves and make payments for capital services, the real resource gain form externally obtained finance is much less than what the gross inflows would suggest. Even aid, which does not entail these costs can be detrimental if it is used to postpone needed reforms. Although much has been achieved since the Monterrey conference, neither the developed nor the developing and transition economies have fully lived up to their commitments. The creation of efficient and effective domestic institutions is an important component in enhancing domestic investment; progress in this area has varied greatly amongst the ECE-EM but in some of economies, especially in the CIS, the needed institutional reform has been quite limited. Even less has been accomplished in terms of the goal of creating an international trade and monetary system that is more development friendly. Much of the progress that has been made in terms of increasing the financial resources available for development is the result not of institutional reform but is instead due to the very favorable global economic environment of rapid growth, low interest rates and high commodity prices.

Figure 1
The Sources and Uses of External Finance for the Low Income ECE-8
As a Percentage of GDP



## Table 1

**The Source and Use of Financial Flows in the ECE Emerging Markets**
**As a Percentage of GDP** [4]

All ECE Emerging Markets

| | **1999** | **2000** | **2001** | **2002** | **2003** | **2004** | **2005** |
|---|---|---|---|---|---|---|---|
| Aid | 1.14 | 0.98 | 0.90 | 0.82 | 0.66 | 0.59 | NA |
| FDI Inflows | 3.28 | 3.10 | 3.22 | 3.09 | 2.53 | 3.70 | 3.66 |
| Remittances | 1.36 | 1.41 | 1.31 | 1.17 | 1.10 | 1.24 | 1.41 |
| Portfolio Inflows | 0.76 | -0.52 | 0.02 | 1.01 | 0.79 | 2.31 | 1.74 |
| Other Capital | -2.05 | -2.17 | -2.62 | -0.16 | 0.68 | -2.08 | 0.27 |
| Reserve Changes | -1.67 | -2.42 | -1.56 | -2.93 | -3.03 | -3.67 | -5.49 |
| Net Investment Income | -2.21 | -2.15 | -1.94 | -2.16 | -2.65 | -2.91 | -2.81 |
| Balance on Goods & Services | -0.06 | 1.95 | 1.83 | 0.86 | 0.86 | 1.38 | 2.38 |

New Member States –NMS (including Bulgaria, Romania)

| | **1999** | **2000** | **2001** | **2002** | **2003** | **2004** | **2005** |
|---|---|---|---|---|---|---|---|
| Aid | 1.01 | 0.83 | 0.77 | 0.50 | 0.62 | 0.66 | NA |
| FDI Inflows | 5.17 | 5.75 | 4.75 | 5.09 | 2.64 | 5.23 | 5.25 |
| Remittances | 0.46 | 0.72 | 0.74 | 0.69 | 0.82 | 0.98 | 1.60 |
| Portfolio Inflows | 1.06 | 1.40 | 1.11 | 1.74 | 1.73 | 3.61 | 2.74 |
| Other Capital | 0.38 | -0.62 | -1.84 | 1.00 | 1.73 | -1.78 | -0.50 |
| Reserve Changes | -1.43 | -1.28 | -1.19 | -2.83 | -1.17 | -1.87 | -3.62 |
| Net Investment Income | -1.67 | -1.77 | -1.76 | -2.29 | -2.69 | -4.37 | -3.76 |
| Balance on Goods & Services | -5.59 | -5.03 | -3.98 | -3.48 | -3.59 | -3.48 | -2.57 |

Non EU Southeast Europe – SEE (without Turkey)

| | **1999** | **2000** | **2001** | **2002** | **2003** | **2004** | **2005** |
|---|---|---|---|---|---|---|---|
| Aid | 5.36 | 6.44 | 5.68 | 5.89 | 3.73 | 3.07 | 2.59 |
| FDI Inflows | 4.35 | 4.04 | 5.00 | 3.36 | 5.96 | 3.99 | 4.15 |
| Remittances | 9.23 | 10.39 | 10.44 | 9.80 | 9.43 | 10.23 | 9.85 |
| Portfolio Inflows | 1.36 | 1.88 | 1.61 | 0.34 | 1.18 | 1.46 | -0.54 |
| Other Capital | -1.01 | -0.59 | 1.38 | 3.48 | 1.76 | 0.48 | 4.45 |
| Reserve Changes | -6.41 | -3.41 | -6.29 | -2.57 | -3.74 | -1.46 | -4.73 |
| Net Investment Income | -1.17 | -1.28 | -1.52 | -1.30 | -2.13 | -1.38 | -1.81 |
| Balance on Goods & Services | -16.49 | -16.46 | -16.40 | -19.60 | -18.40 | -19.48 | -17.89 |

[4] Note that the totals need not add to zero since not all items in the BOP are included in the listed categories.

Low Income ECE-8

| | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 |
|---|---|---|---|---|---|---|---|
| Aid | 5.34 | 4.76 | 5.30 | 6.36 | 5.06 | 4.53 | 3.59 |
| FDI Inflows | 2.90 | 2.33 | 2.48 | 6.67 | 11.80 | 11.84 | 5.66 |
| Remittances | 3.12 | 4.46 | 5.51 | 6.78 | 7.74 | 9.84 | 11.02 |
| Portfolio Inflows | 0.00 | -0.01 | -0.01 | -0.12 | -0.05 | -0.01 | 0.14 |
| Other Capital | 1.17 | 1.61 | -0.25 | -1.52 | -2.84 | -1.88 | -2.42 |
| Reserve Changes | -2.18 | -1.11 | -1.90 | -0.51 | -1.77 | -3.43 | -2.33 |
| Net Investment Income | -0.55 | -1.48 | -1.28 | -1.96 | -1.91 | -2.41 | -4.00 |
| Balance on Goods & Services | -8.07 | -5.66 | -6.64 | -9.15 | -12.33 | -11.97 | -6.54 |

CIS-11 (without Russia)

| | 1999 | 2000 | 2001 | 2002 | 2003 | 2004 | 2005 |
|---|---|---|---|---|---|---|---|
| Aid | 2.23 | 2.13 | 2.02 | 2.05 | 1.50 | 1.28 | 1.00 |
| FDI Inflows | 3.79 | 2.93 | 4.20 | 4.75 | 5.55 | 5.94 | 5.47 |
| Remittances | 0.96 | 1.23 | 1.38 | 1.63 | 1.82 | 2.26 | 2.54 |
| Portfolio Inflows | -0.13 | -0.13 | -0.83 | -1.67 | -0.54 | 1.54 | 1.68 |
| Other Capital | -1.40 | -0.92 | -0.29 | -1.12 | -0.55 | -4.65 | -2.85 |
| Reserve Changes | -1.17 | -1.16 | -2.52 | -1.81 | -3.16 | -4.26 | -4.68 |
| Net Investment Income | -1.68 | -2.97 | -2.29 | -2.08 | -2.19 | -2.47 | -3.66 |
| Balance on Goods & Services | -0.64 | 2.47 | -0.92 | 0.40 | 0.22 | 2.39 | 2.50 |