

Rating-Agentur Expert RA confirmed at 'B' the ratings of Kyrgyzstan. The rating outlook changed from stable to negative.

Rating-Agentur Expert RA confirmed the sovereign government credit rating (SGC) of Kyrgyzstan at 'B' (Moderately low level of creditworthiness of the government) in national currency and at 'B' (Moderately low level of creditworthiness of the government) in foreign currency. The rating outlook changed from stable to negative which means that in the mid-term perspective there is a high probability of downgrading the rating score.

MAJOR FACTORS THAT INFLUENCED BOTH TYPES OF RATINGS:

Positive factors:

- According to data from the Ministry of Finance of Kyrgyz Republic (MFKR), as of end 2019 short-term securities represented around 1,3% of total debt and 8% of domestic debt. This remained well-covered by 5x by FX reserves. Moreover, as of 4M 2020 the share of short-terms securities in domestic debt declined to 3,4%;

Restricting factors:

- The economy grew solidly in 2019 by posting a reading of 4,5% y-o-y, which partially resulted due to rising gold output from Kumtor. However, the growth slowed down to 1,5% y-o-y as of 1Q 2020, while in 5M 2020 GDP had already contracted by 4,8%¹ y-o-y and we anticipate a contraction in the economy of around 4% in real terms in 2020 due to the coronavirus crisis. This pandemic has already taken a toll on international trade and other services in the country, as a direct consequence of the border closure with China. Moreover, the economy has also been negatively affected by lower remittances inflow, as well as depressed domestic consumption resulting from the lockdown;
- The inflation rate stood at 3,1% in 2019, which is lower than the target corridor of the National Bank of the Kyrgyz Republic (NBKR) of 5%-7%. During 1H of 2020, we have already observed inflationary pressures resulting from the strong depreciation of the KGS. As of May 2020, the y-o-y inflation stood at 7,2% as food prices and some utilities hiked substantially. We anticipate the metric to rise further up to around 12% by the end of the year deriving from the currency depreciation, as well as further fiscal stimulus;
- As a result of the abovementioned inflationary pressures, the NBRK increased the reference rate up to 5% back in February 2020. Moreover, the boundaries of the interest rate corridor were narrowed in order to increase predictability of the direction of the monetary policy, a positive step towards increased efficiency and credibility of the policy. However, financial dollarization remain elevated;
- Financial soundness indicators remained practically unchanged in 2019. ROA stood at 1,5%, the capital adequacy ratio posted a reading 24%, while the NPLs to total loans ratio recorded a metric of 7,7%. As a consequence of the pandemic, we anticipate these metrics to deteriorate. Nevertheless, the NBRK has already implemented measures to support banks and, at the same time, propel the economy through issuance of credit. Such measures include the temporary suspension of the application of financial regulations, as well as easing liquidity, capital and reserve requirements;
- Ongoing reform regarding special economic zone tax regulations and overall economic

¹ According to preliminary data from local statistical service without taking into account the output on Kumtor gold mine the GDP decline for 4M 2020 was 6,4%.

stability were able to attract investments, as net inflows from foreign direct investment in 2019 is expected to be near 2,5% of GDP. However, this will be hit in 2020 as a result of the cancellation USD 300 m trade and logistics center project by a Chinese investor, which was suspended over local protests against Beijing;

- The overall fiscal deficit in 2019 stood at 0,1%², narrowing down as compared to 2018. Currently, public finances have already felt the consequences of the pandemic as the government budget deficit was at the level of KGS -10,5 bn as of 4M 2020, resulting from higher current and capital expenditures, as well as lower tax revenues. As a result of the plan set up by the government cushion the pandemic effect, we anticipate the deficit to widen to around 8%-9% of GDP in 2020. This plan includes measures, such as delaying tax payments, temporary price controls on food, as well as exemptions of property and land taxes, among others. In our view, it is key that the government is able to find donor support in order to be able to execute the program, while not compromising its debt repayment ability;
- Official unemployment rate in 2019 is around 7%, but we expect this figure to hike substantially in 2020 as a result of the coronavirus crisis;
- According to the World Bank Doing Business Report 2020, Kyrgyz Republic was ranked 80th out of 190 countries, a decline of 10 spots as compared to a year before. However, high corruption perception, unresolved tensions on the border with the neighboring countries, complex tax regulation continue constrain business development;

Negative factors:

- Government debt to GDP declined slightly to 54,1% of GDP and 159,1% of budget revenues in 2019. As with other metrics, the readings are set to increase substantially as the government implements measures equivalent to 7% to 8% of GDP to curve the impact of the coronavirus crisis. Thus, we anticipate the debt to GDP ratio to increase to around 69%. Nevertheless, the high level of debt remains mitigated due to the fact that around 85% of the public debt is in concessional terms. Despite this, there is a concentration of the external debt as 46% of it is owed to the Export-Import Bank of China;
- Kyrgyzstan remains one of the poorest countries in the Central Asia region³ with an estimated GDP per capita in PPP terms at around USD 4,1 th for 2019. The dependence on the gold output from the Kumtor mine, keeps the Kyrgyz economy concentration risk high⁴;
- Despite the level of credit having increased in 2019 as reflected by the level of domestic credit to GDP at around 25% (22,3% in 2018), it remains quite low. What is more, as of April 2020, the highest level of growth was attributed to mortgages, which hiked by 23% y-o-y, followed by consumer loans which grew by 17%; while industry loans climbed by 11%, agricultural credit by 6% and trade loans by 7%. These dynamics reflect that credit towards the productive sector of the economy has not grown as fast as needed to achieve consistent growth and better economic development;
- In the Global Competitiveness Index 4.0 issued in 2019, Kyrgyzstan was ranked 96th out of 141 countries due to the low scores on innovation capability and limited local market opportunities. Moreover, the weak current and external positions also reflect low competitiveness and high dependence on external factors;
- The Kyrgyz Stock Exchange (KSE) remains highly concentrated and provides few products for investors to trade and limited opportunities for companies to seek alternative sources of funding. The total market capitalization of the KSE remained below 5% of GDP in 2019.

² This metric includes lending by the government to state-owned enterprises in the energy sector.

³ GDP per capita in PPP terms of USD estimated by IMF for 2019: Kazakhstan – 28 850, Tajikistan – 3 589, Turkmenistan – 20 410 and Uzbekistan – 8 999.

⁴ “Based on exploration findings, the Kumtor open pit mine-life has been extended to 2023. The period for the gold ore processing at plant – up to 2026”. - <https://www.kumtor.kg/en/about/faq/production/>

Stress factors:

- The economy is highly dependent on other countries in the export market, imports and remittances inflows. In 2019, more than 98% of cross-border payments came from Russia due to the high amount of labor force from Kyrgyzstan and 42% of all export goes to Great Britain (moderately weak stress-factor);
- Financial dollarization in Kyrgyzstan shows encouraging dynamics, but remains high: as of April 2020, 36% of total loans and 43% of total deposits were denominated in foreign currency (very weak stress-factor).

SENSITIVITY ASSESSMENT:

The following developments could lead to an upgrade:

- Further significant decline of external government debt;
- Continued improvement of the country's fiscal stance and trade balance;
- Continued improvement of the banking system performance.

The following developments could lead to a downgrade:

- A lingering economic recession beyond our projected levels;
- Unsustainable increase in the levels of government debt combined with the inability to restructure obligations or obtain further financial support.

ESG Disclosure:

Inherent factors

- Quality of fiscal policy; quality of monetary policy; natural resources; natural and climatic threats; environmental threats; level of corruption, CPI; Government Effectiveness Index; quality of the business environment; position in Doing Business Ranking; level of investment in human capital, adjusted for inequality; Rule of Law Index; transparency of government policymaking Index; level of information transparency of the government; Political Stability and Absence of Violence/Terrorism Index; natural disasters, constant exposure to difficult natural conditions.

Drivers of change factors

- None.

“We have confirmed the credit ratings of Kyrgyzstan at ‘B’; however, the outlook was changed from stable to negative. The adjustment in the outlook is mainly a result of the adverse consequences in the economy, public finances and external stance derived from the coronavirus crisis. We anticipate that, due to the pandemic, the economy will contract in 2020, government debt will substantially increase, the fiscal balance will widen significantly and the balance of payments will deteriorate.

However, we also consider that the country has the ability to receive enough support from international institutions and other donors, which would aid to mitigate the crisis. Moreover, in our view, the improvement in the quality of the monetary policy and the actions taken by the Central Bank will also fare positively against the pandemic.” – Hector Alvarez, Associate Director of Rating-Agentur Expert RA.

Research report on Kyrgyzstan is available at:

https://raexpert.eu/reports/Research_report_Kyrgyzstan_26.06.2020.pdf

Next scheduled rating publication: 18 December 2020. The full sovereign rating calendar can be found at [Sovereign Rating Calendar 2020](#)

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RATING HISTORY:

Date	Review reason	SGC		Outlook	
		National currency	Foreign currency	National currency	Foreign currency
27.12.2019	Scheduled revision of both types of ratings for the country	B	B	Stable	Stable
28.06.2019	Scheduled revision of both types of ratings for the country	B	B	Stable	Stable
04.01.2019	Scheduled revision of both types of ratings for the country	B	B	Stable	Stable
13.07.2018	Scheduled revision of both types of ratings for the country	B	B	Stable	Stable
19.01.2018	Scheduled revision of both types of ratings for the country	B	B	NA	NA
21.07.2017	Scheduled revision of both types of ratings for the country	B	B	NA	NA
27.01.2017	Scheduled revision of both types of ratings for the country	B	B	NA	NA
29.07.2016	Scheduled revision of both types of ratings for the country	B	B	NA	NA
19.02.2016	First assignment of both types of ratings for the country	B	B	NA	NA

Minute's summary

The rating committee for Kyrgyzstan was held on 25 June 2020. The quorum for the rating committee was present. After the responsible expert presented the factors, which influenced the rating assessment, the members of the committee expressed their opinions and suggestions within the framework of the Sovereign methodology. The chairman of the rating committee ensured that every member of the committee expressed his/her opinion before proceeding to the voting.

The following methodology was used for the rating assessment: [Methodology for Assigning Sovereign Government Credit Ratings – Full Public Version](#) (from April 2019). Descriptions and definitions of all rating categories can be found under the [Rating scale](#) section. The user of the rating shall read the methodology in order to have a full understanding of the rating procedure.

The definition of default can be found on the Agency's website in the section for [Internal policies](#).

These ratings are unsolicited. The rated entity did not participate in the rating process.

Main sources of information: International Monetary Fund, World Bank, World Economic Forum, Doing Business, United Nations, Kyrgyz Stock Exchange (KSE), National Bank of Kyrgyzstan (NBKR), Ministry of Finance of the Kyrgyz Republic, Ministry of Economy of the Kyrgyz Republic, National Statistical Committee of the Kyrgyz Republic, Transparency International, Human Development Report.

ESG Disclosure

We consider Environmental, Social, and Governance (ESG) risks and opportunities in the creditworthiness analysis of our Sovereign entities. The disclosure document can be found on the Agency's website in the section: [ESG factors in RAEX-Europe's Credit Ratings](#)

Limits of the Credit Rating

During the rating assignment process, Rating-Agentur Expert RA GmbH (the Agency) used publicly available information that was considered to be reliable, complete and non-biased. The responsible expert performed the rating assessment of the country with information considered as the most reliable and up to date in accordance to the overall position of the country and the Agency's internal criteria for selecting data providers. The information and data used for this specific assessment can be considered as of sufficient quality.

Regulatory use

SGC ratings can be used for regulatory purposes according to the ESMA definition.

Conflict of interest

The responsible expert was neither influenced nor biased by third parties during the rating assessment. All employees involved in the rating assessment and revision of the rated entity have reported absence of conflicts of interests before initiation of the rating process.

Rating-Agentur Expert RA GmbH is completely independent from the activities of other agencies of the RAEX group.

Risk warning

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This press-release represents the opinion of Rating-Agentur Expert RA GmbH and is not a recommendation to buy, hold or sell any securities or assets, or to make investment decisions.

Office responsible for preparing the rating

The office responsible for the preparation and issuance of this credit rating is the office of Rating-Agentur Expert RA GmbH in Frankfurt am Main, Germany.

Rating-Agentur Expert RA GmbH is a credit rating agency established in Germany and therefore shall comply with all applicable regulations currently in force in the European Union.

The European Securities and Markets Authority (ESMA), the EU's direct supervisor of credit rating agencies (CRAs), has registered Rating-Agentur Expert RA GmbH as a CRA under Regulation (EC) No 1060/2009 of the European Parliament and of the Council of 16 September 2009 on credit rating agencies, with effect from 1 December 2015.

Rating-Agentur Expert RA GmbH applies the Code of Conduct Fundamentals for credit rating agencies issued by the International Organization of Securities Commissions (IOSCO Code) and includes the basic principles of IOSCO Code in its Code of Conduct.