

Rating-Agentur Expert RA confirmed at 'B-' the FC rating and at 'B' the NC rating of Tajikistan. The rating outlook is negative.

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

MAJOR FACTORS THAT INFLUENCED BOTH TYPES OF RATINGS:

Positive factors:

- Tajikistan's economic growth, despite a slight slowdown, remains one of the highest in the region at 7,5% in 2019 and expected to be close to 5% within the next years. However, economic growth rates may be negatively affected by the country's high exposure to external and environmental shocks and significant internal imbalances of the national economy;
- After an increase in the level of net FDI inflow in 2018 to 2,9% mostly due to substantial increase of investments of Chinese companies into the mining industry, as well as other FDI to metallurgy and retail, we expect slightly lower metrics in 2019 due to the lower non-residents' investments in equity shares;
- Moderate level of expected debt load with a ratio of public debt to GDP and budget revenues of 45,2% and 162% in 2019 respectively, according to IMF estimates, with a high share of concessional debt from international financial institutions, foreign governments, as well as government related banks¹. In the short term, the government does not plan to increase borrowing to finance the Rogun Hydro Power Plant (HPP); however, taking into account the external liabilities of SOEs accumulated in recent years and the high share of FX-denominated debt (up to 80% of total public debt), the abovementioned debt ratios may exceed 50% of GDP and 180% of budget revenues in case of external shocks.

Restricting factors:

- After a period of expansionary fiscal policy in 2016-2017, the Tajik government turned to fiscal consolidation in 2018 and continued this trend in 2019. For 9M 2019, the fiscal deficit narrowed to 2,8% of GDP as compared to 4,3% in 9M 2018, mostly due to increase of non-tax revenues and under-execution of the non-priority capital expenditures. However, we expect that the expenses execution path in 4Q 2019 increased substantially due to the need to finalize several public projects, which can lead to a reverse trend in fiscal consolidation. We will keep monitoring the final results of 2019, including wide-spread quasi-fiscal operations, as well as the budget execution in 2020;
- The effectiveness of the monetary policy remains limited by still high levels of financial dollarization, the poor stance of the banking system, undeveloped local capital markets, as well as low independency of the National Bank of Tajikistan (NBT). Despite the gradual

¹ The Export-Import Bank of China is the largest creditor of Tajik government.

increase of the NBT's policy efficiency, with the introduction of new instruments², there is still further room for improvement as shown by the dynamic of the refinance rate during 2019. However, we expect the NBT's inflation target for 2019 of 7% (+/- 2p.p.) to have been reached. Moreover, the NBT remains on the path to transit to a fully flexible exchange rate regime by 2023;

- The preliminary inflation data showed a metric of 8% y-o-y by the end of December 2019 (as compared to 5,4% in 2018), which is within the NBT's target of 7% (+/- 2p.p.). Such a negative dynamic was mostly influenced by several sharp increases in food prices during the year, related to unfavorable weather conditions and increase of price for imported goods;
- The overall deficit of public finances, in the IMF definition which includes public infrastructure projects, is expected to have widened up to 3,8% of GDP by end-2019 as compared to 2,8% a year ago, mostly due to additional capital spending at the end of the year. We still expect the budget balance to be volatile in the following years due to the significant volume of investments in infrastructure projects and the lack of internal capacity for revenue growth.

Negative factors:

- The economy remains underdeveloped and inefficient, as evidenced by the WEF competitiveness index in 2019 – 52 (104th place out of 140 countries), persistently high trade deficit and subdued level of GDP per capita in PPP, which is expected to have stood at USD 3,6 th as of the end of 2019, the lowest level among the non-oil regional peers³;
- Contingent liabilities remain substantial arising from the high level of indebtedness of unprofitable SOEs, especially in the energy sector, while problems with two large systemically important banks (Agroinvestbank and Tochiksodirobank) remain in place. These institutions have debts to the state in the amount of about TJS 4 bn altogether;
- The development of the financial system remains subdued as we estimate banks' assets and domestic credit to GDP ratios to have stayed at 28,4% and 15,6% as of end-2019 respectively, as well as absence of listed shares currently traded on the national Central Asia Stock Exchange (Dushanbe);
- The banking system remains very weak with a high concentration of assets in state-owned banks and the presence of large troubled banks. The ratio of NPLs to total loans, as of end 2019 was up to 25,6% of total loans⁴. However, the level of NPLs according to the internationally recognized definition may be lower than the disclosed metrics. On the positive side, the banking sector's profitability remains positive. As of the end of 2019, ROE and ROA amounted to 5,0% and 1,4%, respectively, while capitalization in the system remains adequate as the ratio of capital to assets remained high at 28,3% as of the same date;
- Institutional development and transparency of the government policy in Tajikistan is quite low, as shown by the assessment of international organizations. The Corruption Perception Index stood at 25 (153rd place out of 180 countries) in 2019, while the inequality adjusted HDI index was 0,57 in 2018. Moreover, the country occupied only the 106th position out of 190 countries in the Doing Business 2019 report published by the World Bank;

² See our previous Press-release: https://raexpert.eu/reports/Press_release_Tajikistan_09.08.2019.pdf

³ Central Asia and Caucasus non-oil peers: Armenia, Georgia, Kyrgyzstan and Uzbekistan.

⁴ The figure refers to the local definition of NPLs, which include customer and interbank loans with overdue payments of more than 30 days, instead of the generally accepted number of 90 days.

- According to the ILO methodology, unemployment is estimated at 11% in 2019. This metric is heavily exposed to the conditions of the largest economies in the region, such as Russia and Kazakhstan, where a significant part of the Tajik labor force works. Due to the high level of labor migration to Russia, the employment and income of the population and, accordingly, the volume of remittances, largely depend on the state of the Russian economy;
- The spread for the 10Y USD-denominated Tajikistan government bond with maturity in 2027 (7-year remaining maturity) and 7Y U.S. Treasury bonds is currently more than 9p.p. showing the negative investors' perceptions regarding sovereign risks.

Stress factors:

- Despite positive dynamics over the last two years, financial dollarization remains high with the share of FX-denominated loans and deposits at 50,5% and 46,9%, respectively by December 2019 (very weak stress-factor).

Currency risks:

- The FX-currency market remains managed by the NBT, which constrains access to hard currency and indirectly limits imports. This leads to the presence of an informal market of FX-currency, especially taking into account the size of remittances inflow which accounted to almost 30% of GDP according to the World Bank data;
- The current account deficit is expected to reach 4,5% in 2019, as there is a high dependence on imports with a ratio of imports to GDP of 43% in 2019, while at the same time, exports and remittances were weak. Nevertheless, international reserves stabilized at the level of USD 1,5 bn, which covers more than 5 months of imports and more than 50% of external public debt;
- Very low level of export to GDP at around 15% in 2019;
- Exposure to currency risks of public debt servicing remains high, as about 80% of debt is denominated in foreign currency. However, these risks are partly mitigated by a high share of concessional debt.

SENSITIVITY ASSESSMENT:

The following developments could lead to an upgrade:

- Significant development of the financial market and improvement of the banking system: growth of assets and loans to the economy, further reduction of NPLs, decreasing of financial dollarization and realization of agreements with investors regarding troubled banks;
- Consistent further improvement of the monetary policy and the transmission efficiency, as well as liberalization of the exchange rate regime.

The following developments could lead to a downgrade:

- Significant expansion of budget expenditures in order to finalize infrastructure projects in the energy sector, which will create risks of government debt growth;
- Deterioration of the external position in case of adverse economic conditions in the country's major trade partners and significant external shocks;
- Hikes in inflation and dollarization levels due to external shocks.

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

- Natural disasters, such as earthquakes, floods, mudflows, droughts, and extreme temperatures have significant economic impact through affecting agriculture and damaging of infrastructure. Thus, the factor in our sovereign methodology which could be directly affected by this is ***Level and dynamics of production***.

“The Agency has decided to maintain Tajikistan's ratings at ‘B-’ in FC and ‘B’ in LC with a negative outlook. The rating remains negatively affected by an ineffective economy with a low level of welfare and high unemployment level, subdued and undeveloped financial system, as well as the lingering risk of materialization of contingent liabilities. In addition, the rating is constrained by weak institutional development, imbalanced external position and high financial dollarization. In contrast, the ratings are supported by strong and stable economic growth, the moderate level of the government debt with favorable payment conditions and maturity. The negative outlook reflects the existing risks and vulnerabilities of the external position, which may lead to deterioration of public finances and destabilize the macroeconomic situation.” - Clarified Vladimir Gorchakov, Associate Director of Rating-Agentur Expert RA.

Research report on Tajikistan is available at:

https://raexpert.eu/reports/Research_report_Tajikistan_07.02.2020.pdf

Next scheduled rating publication: 7 August 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
09.08.2019	Scheduled revision of both types of ratings for the country	B	B-	Negative	Negative
10.05.2019	First assignment of both types of ratings	B	B-	Developing	Developing

Minute's summary

The rating committee for Tajikistan was held on 4 February 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: IMF, World Bank, National Bank of Tajikistan, National statistical office of the Republic of Tajikistan, Ministry of finance of the Republic of Tajikistan, Central Asia Stock Exchange, WEF, Transparency international, open sources.

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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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.